STOCKS DOWN UNDER

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ASX Small Caps Stocks Down Under

> *As long as inflation exists, it is the enemy of economic growth.*

- Henry Hazlitt (1894-1993), New York-based economics journalist and author

AMA GROUP

Better opportunities elsewhere

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Stocks Down Under rating: ★ ★

ASX: AMA
Market cap: A$275.8M

52-week range: A$0.14 / A$0.50
Share price: A$0.26

Fewer companies have been more snake-bitten than AMA Group (ASX: AMA). The smash repairer has been hit by reduced business due to Covid lockdowns, lawsuits from its disgruntled ex-chief executive and operators of a company it had acquired, labour shortages, supply chain issues and inflation. These dramas have shown in the company's share price – it is 80% lower than three years ago. Long-suffering shareholders appear to believe the worst is over, judging by the share price spike in the last month, and the company does too. That may be so, but we think it is too early to say it has turned a corner.

Share price chart

Source: Tradingview

Lockdowns bite

Everybody knows that lockdowns meant less people on the roads and therefore less business for companies that had anything to do with the roads or vehicles using them, most prominently Transurban (ASX:TCL). But as people returned to the roads, business returned. In FY21, AMA's revenue rose 11% to $919m and EBITDA rose 25% to $71.5m. We last covered AMA in October 2021 in the aftermath of these results and noted that consensus EBITDA was $85m for FY22 and $127m for FY23, representing 18% and 49% growth.

However, this is not what happened in FY22. Sadly, lockdowns returned in the early part of FY22 and drivers left their cars parked. The company had to raise capital - $150m through a rights issue and convertible notes. Nearly half of this amount was just used to repay debt. And when lockdowns ended, it wasn't 'back to normal' this time around. In the second half of the financial year the company was hit by labour shortages, inflation and supply chain issues. There was significant absenteeism due to COVID, the flu and other viruses along with difficulty in finding new talent. Supply chain constraints and inflation impacted the availability of parts and the pricing of them.

A hell of a year takes a significant toll

Thanks to all these dramas, revenue fell 8% to $845.1m and EBITDA collapsed by over 80% to $21.8m. The company's net loss was $148m, increased by $78m in depreciation and $105.5m in non-cash impairments against goodwill and right of use assets. Briefly turning to the cash flow statement, AMA lost $28.2m in cash flow from operations. And despite the capital raise, it finished the year with 19% less cash than it begun the year with, at $52.2m. And with $165m in drawn down debt and the ~$50m in convertible notes, it closed FY22 with a ~$164m net debt position – admittedly a position 9% lower than 12 months prior.

AMA was forced to shift to quarterly reporting by the ASX, given that it was now unprofitable. The company told shareholders that 'the request to do so reflects the attention drawn to material uncertainty regarding AMA Group's ability to continue as a going concern, identified by the Auditors in the FY21 Annual Report'.

Does FY23 look better?

The company told shareholders FY23 would be a transition year, but provided significantly improved EBITDA guidance at $70-$90m for FY23 and $120-$140m for FY24. Even the lower end of the former figure is more than thrice the size of EBITDA in FY22. AMA claimed to have rebased the company to focus on more profitable work rather than being measured on repair volumes and site numbers. Still, it told shareholders to expect acquisitions to help it achieve its strategic objectives. We briefly observe that it has also set strategic targets for FY27 hoping for over $1.2bn in revenue across its various segments.

Consensus estimates are cautious, calling for $73m in EBITDA for FY23 and $118.9m for FY24, but both would still represent significant growth with FY23 representing 234% growth and FY24 representing 63% growth. Revenue growth is expected to be 15% in FY23 (to $969.5m) and 10% in FY24 (to $1.07bn). On the consensus EBITDA numbers, AMA shares are trading at 10.2x EV/EBITDA for FY23 and 6.2x for FY24, which could be considered very attractive given the expected EBITDA growth for these years. However, as FY22 has shown, there is still a lot that can go wrong for AMA this year.

EPS is still expected to be negative in FY23 at -/-$0.01 on a normalized basis and positive by $0.02 in FY24. This is most likely because of continued amortisation. Consequently, on a P/E basis AMA trades at 15.5x for FY24. Despite optimism about AMA's earnings, the 6 analysts covering the stock are not so optimistic about the share price. The median price target is $0.23 per share with the highest being $0.32 per share, which would only be 19% higher.

Not the right time

Even the most ardent haters of this company can't deny it is in a better position now than 12 months ago. But the immediate future isn't too promising. inflation doesn't appear to be easing. And Q1 could have been better. It is true that receipts from customers grew by more than 5% to $240.2m and AMA was cash flow positive from operating activities to the tune of $1.1m. However, its cash balance fell by ~$8m to $44.4m thanks to leasing and capital expenditure. Bear in mind that this includes a $15.3m tax refund, so it could have been a lot worse otherwise.

Although volume demand remains strong, there still isn't enough labour and parts to complete the current work volume. And remember that Q1 is typically the strongest being the only one not impacted by holidays (Christmas impacts Q2 and Q3 while Easter impacts Q4).

The company reaffirmed its EBITDA guidance for both FY23 and FY24, but we'll have to wait until its half-yearly results (due in February) to know if it really is on track. We are also concerned about its high levels of debt and that a significant portion of it is due within the next couple of years, maturing in October 2024.

We think day traders might see AMA as an opportunity given it is still in the All Ords and could move upwards with the index as it recovers from the Tech Wreck of 2022. But for longer term investors, there are too many other opportunities on the ASX that aren't being as significantly impacted by inflation and have significantly healthier balance sheets. So, its two stars for now.

Pitt Street Research Pty Ltd

3 Spring Street, Sydney, NSW 2000, Australia