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Zacks Small-Cap Research

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Cango Inc-Adr (CANG-NYSE)

CANG: Results stabilized in the third quarter but challenges remain.

Revenues rebounded sharply from Q2 and slightly exceeded our model for Q3 as auto demand was bolstered by new government incentives and easing used car regulations in China.

Current Price (11/29/22)	$1.52
Valuation	**$3.00**

Cango Inc's (CANG) Q3 results were slightly better than our expectations as the company navigated a challenging operating environment in China with continued supply chain disruptions and additional COVID-related shutdowns impacting consumers.

We previously called 2022 a transition year for Cango as it attempts to become a one-stop shop for auto dealers and consumers. These results indicate that the transition is moving ahead and some cost saving initiatives might even be ahead of schedule.

The company maintains a very strong balance sheet with estimated cash and short-term investment balances of $2.35-2.50/ADS.

OUTLOOK

SUMMARY DATA

52-Week High	**$3.70**
52-Week Low	**$1.52**
One-Year Return (%)	**-43.45**
Beta	**0.98**
Average Daily Volume (sh)	**310,175**
Shares Outstanding (mil)	**136**
Market Capitalization ($mil)	**$206**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**23**
Insider Ownership (%)	**29**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2022 Estimate	**N/A**
P/E using 2023 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Avg.,**
Type of Stock	**Small-Value**
Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of RMB)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2020	246 A	274 A	435 A	1,097 A	2,052 A
2021	1,124 A	947 A	801 A	1,051 A	3,922 A
2022	788 A	289 A	416 A	498 E	1,992 E
2023	560 E	605 E	629 E	670 E	2,465 E

EPS
(in RMB)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2020	-$0.04 A	$0.07 A	$1.73 A	$1.59 A	$3.40 A
2021	-$0.28 A	$0.58 A	-$0.45 A	$0.14 A	-$0.01 A
2022	-$0.98 A	-$2.08 A	-$0.96 A	-$0.99 E	-$5.00 E
2023	-$1.01 E	-$0.90 E	-$0.80 E	-$0.77 E	-$3.49 E

Quarterly estimates may not sum due to rounding.

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WHAT'S NEW

Business Update

Cango reported third quarter 2022 results after the market closed last night and as we anticipated, the company appears to have stabilized their operations after a difficult spring when COVID-related shutdowns severely impacted results. The revenue mix continues the transition toward the auto trading business and while the margins are very thin in that business today, we believe there is room for improvement over time as Cango expands its used car operations and offers dealers and consumers additional value-added services. Despite significant cost savings initiatives, the combination of the low gross margin auto trading business and existing overhead led to a net loss of RMB130 million ($18.3 mil USD) for the quarter but that was a 54% improvement versus the second quarter loss.

On the company's conference call management indicated that despite the continued COVID-related disruptions, the release of pent-up consumer demand should enable sequential revenue growth in the fourth quarter of 2022 to RMB450 and RMB500 million which will represent sequential growth of 8% to 20% over Q3 2022.

This is roughly in line with our previous forecast of RMB513 million and represents the first time that the company has provided guidance near our expectations since we initiated coverage.

Highlights of the Earnings Conference Call

- Cango continues to face the combined challenge of shifting their business model in 2022 while also dealing with a significant slowdown in the new car business in China. We believe that expectations have been lowered sufficiently and that the company should be able to demonstrate sequential growth going forward. However, uncertainties surrounding COVID-related shutdowns by the Chinese government remains a significant unknown variable. In the long-run, we believe that the COVID-related impacts on the auto industry – namely, increased online research, increased online purchasing and a more expansive used car market – will all be net positives for Cango but it may take 18-24 months for investors to recognized this fact.

- Cango noted that New Energy Vehicle (NEVs) sales have continued to outpace traditional internal combustion engine (ICE) models despite pricing discounts for the ICE vehicles. NEV sales have totaled over 7,600 in the first 9 months of 2022 for Cango or more than 60% of total sales.

- As a result of the proceeds the company received from the timely sale of Li Auto shares, Cango still reported RMB 3,443 million of cash and short-term investments ($484 million USD) at 9/30/22. Based on the current share count this means the company was holding over $3.50 per ADS at 9/30/22. The company did complete its second $1.00/ADS special dividend of 2022 in November, so we believe that the cash on hand today is probably between $2.35 and $2.50 per ADS. While the share price has clearly underperformed since our initiation, investors have received $2.00 of dividends per ADS and the company still has sufficient resources to pursue strategic acquisitions or significant share buybacks if the stock price continues to underperform.

June 2022 Quarter Results

Cango reported revenue of RMB416 million in the third quarter ending September 30 2022 which was about 3.7% above our forecast of RMB405 million. Sequentially, revenues were up RMB127 million or 43% as revenues rebounded from widespread COVID-related shutdowns of April and May. Barring another significant shutdown across China we believe the June quarter should market the low water mark for Cango's revenues.

The gross margin also improved slightly over the second quarter as higher priced NEV became a larger percentage of overall sales and the used car market experienced a resurgence.

For the first time in 2022, the company's guidance for Q4 was roughly in line with our model (guidance of RMB450 – RMB500 million versus our previous estimate of RMB 513 million) and we have only made a minor adjustment to our revenue model for Q4 2022 to RMB498 million.

We believe the company still has most of a $50 million stock buyback authorization available at its disposal and we anticipate that some of the company's significant cash balances may be used to repurchase shares at the current prices.

Model Update

We now forecast revenues for the quarter ending 12/31/22 to be at the very high end of management's projections at RMB498 million with over 80% of revenues coming from the auto trading business. We also have made minor adjustments to the revenue model for 2023, reducing total revenues for the year by a little over 2% to RMB2.47 billion.

PROJECTED INCOME STATEMENT

	2018	2019	2020	2021	Mar 1Q22A	June 2Q22A	Sept 3Q22A	Dec 4Q22E	2022E	2023E
Metrics & KPIs:										
Dealers Covered Count	**46,565**	**49,238**	**48,487**	**45,930**	44,771					
% change (yoy)	***34%***	**6%**	**-2%**	**-5%**	-5%					
Financing Transactions Amount (millions)	**21,719**	**28,054**	**27,680**	**30,128**	2,637					
% change (yoy)	**-18%**	**29%**	**-1%**	**9%**	-75%					
Outstanding Financing Transactions (millions)	**34,256**	**40,032**	**43,505**	**45,930**	44,771					
% change (yoy)	**20%**	**17%**	**9%**	**6%**	-6%					
M1+ Overdue Ratio (30-179 days past due)	0.90%	0.80%	1.42%	1.45%	1.76%	2.21%				
M3+ Overdue Ratio (90-179 days past due)	0.41%	0.35%	0.59%	0.71%	0.80%	1.07%				
(RMB Renminbi in Millions; December Year-End)										
Revenues:										
Loan Facilitation Income & Related Income	**916.3**	**913.8**	**891.8**	**1,233.6**	105.9	14.6	14.7	15.1	**150.3**	**74.0**
% change (yoy)	**-10%**	**0%**	**-2%**	**38%**	-74%	-95%	-92%	-94%	**-88%**	**-51%**
Leasing Income	**59.1**	**300.1**	**286.1**	**251.3**	50.1	42.7	34.7	36.9	**164.4**	**148.1**
% change (yoy)	NM	**408%**	**-5%**	**-12%**	-31%	-34%	-38%	-30%	**-35%**	**-10%**
Aftermarket Services Income	**100.1**	**206.0**	**241.2**	**193.8**	25.8	10.5	19.4	18.4	**74.1**	**76.1**
% change (yoy)	**283%**	**106%**	**17%**	**-20%**	-59%	-80%	-67%	-50%	**-62%**	**3%**
Automobile Trading Income	**6.6**	**11.4**	**624.8**	**2,227.2**	599.3	218.6	347.2	422	**1,587.5**	**2,150.9**
% change (yoy)	NM	73%	5374%	**256%**	5%	-58%	-23%	-40%	**-29%**	**35%**
Other	**9.4**	**8.7**	**8.5**	**15.9**	6.6	2.7	0.4	5.6	**15.3**	**15.3**
% change (yoy)	NM	**-7%**	**-2%**	**86%**	35%	0%	5%	7%	**-4%**	**0%**
Total Revenues	**1,091**	**1,440**	**2,052**	**3,922**	**788**	**289**	**416**	**498**	**1,992**	**2,465**
% change (yoy)	**4%**	**32%**	**43%**	**91%**	**-30%**	**-69%**	**-48%**	**-53%**	**-49%**	**24%**
Cost of Revenues	430	539	1,098	2,958	687	273	389	465	1,814	2,305
Gross Profit	661	901	954	964	101	17	28	33	178	160
% change (yoy)		36%	6%	1%	-72%	-93%	-85%	-81%	-82%	-10%
Gross Profit Margin	**60.6%**	**62.6%**	**46.5%**	**24.6%**	**12.8%**	**5.7%**	**6.7%**	**6.6%**	**8.9%**	**6.5%**
Operating Expenses:										
Selling & Marketing Expense	167	193	196	239	54	42	18	21	134	105
% of Sales	15.3%	13.4%	9.5%	6.1%	6.8%	14.5%	4.3%	4.2%	6.7%	4.3%
General & Administrative Expense	151	237	266	276	51	125	58	64	298	312
Research & Development Expense	47	57	63	70	14	13	10	11	49	33
Net (Gain) Loss on Risk Assurance Liabilities	(0)	34	2	198	99	53	85	60	297	177
Provision for Credit Losses	20	56	110	203	72	138	49	45	304	134
Total Operating Expenses	**385**	**578**	**636**	**987**	**290**	**371**	**220**	**202**	**1,082**	**761**
% change (yoy)		**50%**	**10%**	**55%**	**48%**	**57%**	**-4%**	**-38%**	**10%**	**-30%**
Operating Income (Loss)	**277**	**323**	**318**	**(23)**	**(189)**	**(354)**	**(192)**	**(169)**	**(904)**	**(601)**
Interest & Investment Income	61	96	73	50	5	7	15	13	40	52
Fair Value Change of Equity Investment (Li Auto)	0	42	3,315	(37)	(19)	2	0	0	(18)	0
Income (Loss) from Equity Method Investments	43	(1)	0	0	0	0	4	0	4	0
Interest Expense	(19)	(13)	(3)	(14)	(4)	(4)	(3)	(1)	(13)	(5)
Foreign Exchange Gain (Loss)	1	5	(9)	1	(0)	4	4	0	7	-
Other Income	33	41	49	42	34	3	4	6	47	24
Other Expenses	0	(5)	(1)	(7)	(0)	(1)	0	0	(1)	-
Income before Taxes	**396**	**488**	**3,743**	**12**	**(173)**	**(344)**	**(170)**	**(151)**	**(836)**	**(530)**
Income Taxes or Benefit	(89)	(83)	(370)	(21)	37	58	39	15	149	53
Minority Interest Portion of Net Income	4	14	4	0	0	0	0	0	0	0
Net Income (Loss) reported	**303**	**391**	**3,370**	**(9)**	**(136)**	**(286)**	**(130)**	**(136)**	**(687)**	**(477)**
Net Income Adjusted (excl stock comp & one-off	**336**	**473**	**3,448**	**79**	**(113)**	**(190)**	**(110)**	**(110)**	**(522)**	**(295)**
% change (yoy)		**41%**	**629%**	**-98%**	-55%	-133%	-72%	-175%	**-760%**	**-43%**
EPS reported	**2.16**	**2.58**	**22.18**	**(0.06)**	**(0.98)**	**(2.08)**	**(0.96)**	**(0.99)**	**(5.00)**	**(3.49)**
EPS Adjusted (excl stock-based compensation)	**2.39**	**3.12**	**22.69**	**0.54**	**(0.81)**	**(1.38)**	**(0.81)**	**(0.81)**	**(3.80)**	**(2.16)**
% change (yoy)		**30%**	**627%**	**-98%**	-52%	-135%	-70%	-178%	**-805%**	**-43%**
EBITDA reported	**284**	**334**	**328**	**(14)**	**(187)**	**(352)**	**(190)**	**(166)**	**(894)**	**(591)**
Depreciation & Amortization	7	10	10	10	3	3	3	3	10	10
Share-based Compensation Expense	33	82	79	88	23	96	20	26	165	181
EBITDA Adjusted (excl stock comp)	**317**	**416**	**407**	**74**	(164)	(255)	(169)	(141)	**(729)**	**(409)**
Diluted Shares (weighted average)	**140.4**	**151.6**	**152.0**	**146.9**	139.2	137.6	136.4	136.4	**137.4**	**136.4**
Margins:										
Gross Margin	**60.6%**	**62.6%**	**46.5%**	**24.6%**	12.8%	5.7%	6.7%	6.6%	**8.9%**	**6.5%**
EBITDA Margin Adjusted (excl one-offs & stock co	**29.1%**	**28.9%**	**19.8%**	**1.9%**	-20.8%	-88.3%	-40.7%	-28.2%	**-36.6%**	**-16.6%**
EBITDA Margin (reported)	26.0%	23.2%	16.0%	-0.3%	-23.7%	-121.6%	-45.6%	-33.3%	-44.9%	-24.0%
Net Margin Adjusted (excl stock comp)	**30.8%**	**32.9%**	**168.0%**	**2.0%**	-14.4%	-65.6%	-26.4%	-22.1%	**-26.2%**	**-12.0%**
OpEx % of Revenues	**35.2%**	**40.1%**	**31.0%**	**25.2%**	36.8%	128.2%	52.8%	40.5%	**54.3%**	**30.9%**
Selling & Marketing % of Revenues	15.3%	13.4%	9.5%	6.1%	5.8%	14.5%	4.3%	4.2%	6.7%	4.3%
General & Administrative % of Revenues	13.8%	16.4%	12.9%	7.0%	7.2%	43.1%	13.9%	12.9%	14.9%	12.6%
R&D % of Revenues	4.3%	4.0%	3.0%	1.8%	1.7%	4.4%	2.4%	2.3%	2.5%	1.3%

1 ADS (American Depository Share) = 2 Class A ordinary shares
Li Auto stock shares stake contributed a large majority of net income and ROA in 2020.

Source: Zacks SCR, Brian Lantier, Company Filings

VALUATION

We continue to believe that until the company returns to profitability the stock is likely to trade at a multiple of the cash on the balance sheet. Currently, the company is trading a material discount to our estimate of cash on the balance sheet due to uncertainty around the auto market in China and concerns over the length of time until the company can generate positive cash flow. However, we believe that the demonstrated revenue growth in the second half of 2022 will eventually give investors confidence that the company can return to profitability though the timeline might be extended.

In light of the company's latest special dividend payment and the fact that some of the competitors are trading at 1.1 times cash on the balance sheet we are lowering our price target from $4 per ADS to $3 per ADS.

HISTORICAL STOCK PRICE



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