28 August 2014

Buy

Price
RM12.28

Target price
RM14.20

Bloomberg Code
UMWH MK

Equity | Malaysia | Autos

Flashnote

UMW Holdings

Improvement in core businesses

All of UMW's core businesses except the equipment division performed better and 1H14's normalised pretax profit was up by 8%, making up 47% of our full year estimate. Net profit came in at a lower 42%. However, not only do we suspect there were some lumpy non-core losses in 2Q14, in particular, but we expect the three main segments to perform better in subsequent quarters. Maintain Buy.

- After stripping out a RM93m provision related to the divestment of the India auto business as well as property and derivative gain, UMW's 2Q14 normalised pretax profit was up 12% yoy and up 8% for the six-month period. The core businesses save for the equipment division performed better. Sequentially, normalised pretax profit was flattish despite improvement from the Oil & Gas division on the back of contribution from the new Naga 5 rig and stronger contribution from the equipment division.
- This is due to much lower contributions from associates. We believe this could be due to losses from the non-core oil & gas division as sales from Perodua had actually improved by 15% qoq. Also the associate numbers of MBM, which mainly comprises its Perodua stake, made up 49% of our full year estimate and were up strong sequentially, whereas in UMW's case, it is 14% below our annualised estimate and was down 22% qoq.
- Pretax profit for the automotive division improved by 14% yoy and 12% ytd. While there was a decline in Perodua sales, it was offset by the improvement in Toyota sales. Toyota sales was flat yoy but improved by 8% ytd on the back of the new Vios and Altis models. The 1H14 numbers made up 53% of our full year estimate.
- The Oil & Gas division's pretax profit improved by 29% for the ytd period. The stronger contribution is on the back of higher operating days for Naga 1, higher daily rates for Naga 2 and also full contribution from Naga 4, which commenced operations in April 2013. Although the first half number is running slightly behind, constituting 47% of our full year forecast, we expect a better second half with the contribution from Naga 5, which was delivered in April. We also anticipate that Naga 6, which will be delivered in September 2014, should be able to secure contracts by then and begin contributing this year.
- Manufacturing and Engineering 1H14 pretax profit improved strongly by >100% benefitting from the stronger contribution in Malaysia and China although demand in India operation remains weak. The 1H14's profit made up 73% of our estimate.
- The equipment division is the only core business that posted weaker results, which is due to the lower contribution from the overseas operation. Nevertheless, the first half numbers made up 45% of our full year target and we expect a stronger second half on the back of the lifting of the suspension of jade mining activities in Myanmar in September
- Overall, the core businesses performed better and normalised pretax profit made up 47% of our estimates. Despite the better performance of the core businesses, normalised earnings for 1H14 declined 12% and only made up 42% of our forecast.
- We note that tax rates were higher while minorities are also running ahead of expectations. We think the former is partially explained by the provisions in India that are not deductible and we suspect there could have been some lumpy losses from some of the other non-core subsidiaries (mainly on the Oil & Gas side).

Analyst

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- Nevertheless, we expect the subsequent quarters to be stronger on the back of a stronger ringgit, which will benefit the auto division and higher contribution from the Oil & Gas division. Some of the losses under the non-listed oil & gas business could also be transient in nature.
- We view positively management's efforts in its divestment of the loss-making businesses such as the India auto business, which will be completed at the end of the year as this would then enable the healthy core results to be better reflected at the Group level.
- UMW remains one of our top picks underpinned by reasonable valuations, good yields and improving earnings momentum.

Table 1 : Quarterly earnings

(RMm)	Quarter								% chg		Cumulative			KAF	
FYE 31 Dec	**Sep-12**	**Dec-12**	**Mar-13**	**Jun-13**	**Sep-13**	**Dec-13**	**Mar-14**	**Jun-14**	**qoq**	**yoy**	**1H13**	**1H14**	**% chg**	**2014F**	**6M/F**
Turnover	3,958	4,090	3,359	3,499	3,457	3,892	3,583	3,967	11	13	6,858	7,550	10	14,918	51
EBIT	**537**	**439**	**403**	**383**	**291**	**424**	**423**	**420**	**(1)**	**10**	**786**	**843**	**7**	**1,764**	**48**
Margin (%)	13.6%	10.7%	12.0%	10.9%	8.4%	10.9%	11.8%	10.6%	(10)	(3)	11.5%	11.2%		11.8%	
Net interest income	1	(5)	(1)	(12)	(3)	(4)	5	15	185	(226)	(13)	21	(262)	22	95
Exceptional	1	(17)	(8)	33	(105)	(120)	20	(37)	(282)	(212)	25	(17)	nm	0	nm
Associates	57	43	38	39	62	34	31	24	(22)	(39)	78	54	(30)	149	36
Pretax profit	**596**	**459**	**433**	**443**	**246**	**334**	**479**	**422**	**(12)**	**(5)**	**876**	**901**	**3**	**1,935**	**47**
Tax	(122)	(117)	(98)	(101)	(67)	(104)	(87)	(128)	47	27	(199)	(215)	8	(407)	53
Minorities	(174)	(135)	(116)	(91)	(78)	(121)	(157)	(152)	(3)	67	(207)	(309)	49	(586)	53
Net earnings	299	208	220	251	101	109	236	142	(40)	(43)	471	378	(20)	942	40
Normalised net earnings	**298**	**225**	**227**	**218**	**206**	**229**	**215**	**179**	**(17)**	**(18)**	**446**	**394**	**(12)**	**942**	**42**
Normalised pretax profit	**595**	**477**	**440**	**410**	**351**	**454**	**459**	**459**	**(0)**	**12**	**851**	**918**	**8**	**1,935**	**47**

Source: Company, KAF

Table 2 : Quarterly sales trend

Reported sales	Quarter								% chg		Cumulative			KAF	
(units)	**Sep-12**	**Dec-12**	**Mar-13**	**Jun-13**	**Sep-13**	**Dec-13**	**Mar-14**	**Jun-14**	**qoq**	**yoy**	**1H13**	**1H14**	**% chg**	**2014F**	**6M/F**
Toyota															
Cars	12,967	14,988	9,052	14,589	8,063	14,546	14,516	15,653	8	7	23,641	30,169	28	49,196	61
Commercial	4,264	4,815	3,451	4,390	3,986	3,841	2,808	3,612	29	(18)	7,841	6,420	(18)	15,903	40
FWD	7,620	8,949	7,634	8,032	8,280	8,496	6,861	7,672	12	(4)	15,666	14,533	(7)	30,820	47
Total units	**24,851**	**28,752**	**20,137**	**27,011**	**20,329**	**26,883**	**24,185**	**26,937**	**11**	**(0)**	**47,148**	**51,122**	**8**	**95,919**	**53**
Perodua															
Cars	35,849	39,035	35,489	50,960	25,220	38,380	30,515	33,813	11	(34)	86,449	64,328	(26)	150,049	43
Commercial	10,639	10,691	11,207	11,812	12,764	10,293	13,509	16,643	23	41	23,019	30,152	31	50,684	59
Total units	**46,488**	**49,726**	**46,696**	**62,772**	**37,984**	**48,673**	**44,024**	**50,456**	**15**	**(20)**	**109,468**	**94,480**	**(14)**	**200,733**	**47**

Source: Company, KAF

Table 3 : Segmental breakdown

(RMm)			Quarter				% chg		Cumulative			KAF	
FYE 31 Dec	**Mar-13**	**Jun-13**	**Sep-13**	**Dec-13**	**Mar-14**	**Jun-14**	**qoq**	**yoy**	**1H13**	**1H14**	**% chg**	**2014F**	**6M/F**
Revenue													
Motor	2,392	2,571	2,433	2,623	2,656	2,904	9	13	4,963	5,561	12	10,598	52%
O&G	158	168	205	207	196	239	22	42	325	434	34	929	47%
Equipment	479	444		371	434	454	4	2	924	888	(4)	1,777	50%
M&E	177	188		182	182	189	4	1	365	371	2	814	46%
Others	153	128	818	253	115	181	57	41	281	296	5	801	37%
Group	**3,359**	**3,499**	**3,457**	**3,636**	**3,583**	**3,967**	**11**	**13**	**6,858**	**7,550**	**10**	**14,918**	**51%**
									6,858	7,550			
PBT													
Motor	368	358	295	392	407	409	0	14	726	815	12	1,530	53%
O&G	21	76	56	56	58	66	14	(13)	96	125	29	265	47%
Equipment	59	52		29	39	55	41	6	111	94	(15)	209	45%
M&E	9	(3)		(15)	10	12	24	(570)	7	22	214	30	73%
Others	(24)	(40)	(105)	(129)	(34)	(120)	250	199	(65)	(154)	139	(99)	155%
Group	**433**	**443**	**246**	**334**	**479**	**422**	**(12)**	**(5)**	**876**	**901**	**3**	**1,935**	**47**

Source: Company, KAF

Disclosure Appendix

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

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