

UMW (UMWH MK)

Consumer Cyclical - Auto & Autoparts

Market Cap: USD3,458m

Sell (Maintained)

Target Price: MYR8.65

Price: MYR10.70

Buffeted By Abundant Headwinds

 Macro ◆◆◆
 Risks ◆◆
 Growth ◆
 Value ◆


Source: Bloomberg

| | |
|----------------------------|-------------|
| Avg Turnover (MYR/USD) | 13.2m/3.59m |
| Cons. Upside (%) | 4.7 |
| Upside (%) | -19.2 |
| 52-wk Price low/high (MYR) | 10.3 - 12.5 |
| Free float (%) | 35 |
| Share outstanding (m) | 1,168 |
| Shareholders (%) | |
| PNB Funds | 50.1 |

Share Performance (%)

| | YTD | 1m | 3m | 6m | 12m |
|----------|-------|-------|-------|-------|-------|
| Absolute | (2.4) | (1.8) | (3.1) | (5.3) | (0.9) |
| Relative | (2.7) | 3.3 | (0.2) | (1.2) | 4.2 |

Shariah compliant

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UMW's 1Q15 results were below expectations from a plunge in Toyota sales and disappointing earnings at UMWOG, offset by stronger heavy equipment deliveries. We reiterate our SELL call and cut our TP to MYR8.65 (19% downside). We expect headwinds to persist at these two key divisions. The stock trades at unjustified valuations well in excess of the historical average.

- ◆ **A tepid 1Q15.** UMW reported net profit of MYR165.2m for the quarter, reaching just 19.1% and 18.2% or our previous forecast and the consensus estimate respectively. Earnings fell 29.9% YoY but nearly doubled QoQ due to heavy provisioning in 4Q14 at the "Others" division – a motley combination of disparate legacy non-core oil & gas assets that were left out of the 2013 listing of UMW Oil & Gas (UMWOG) (UMWOG MK, NR). The weaker earnings were attributed to the collapse in Toyota vehicle sales during the quarter, along with soft earnings at UMWOG – although this was offset by higher heavy equipment sales.
- ◆ **Toyota sales plunge.** Toyota unit sales for the quarter reached just 16,603 units (-40.3% QoQ, -32.6% YoY) on the back of severe competition from other marques such as Honda and Mazda and exacerbated by the absence of new models. The stronger USD and negative operating leverage resulted in pretax margins falling to 11.6% during the quarter from 15.3% in 1Q14. UMWOG's revenue and pretax profit fell 4.6% and 50.5% QoQ respectively from lower charter and utilisation rates, as well as NAGA-7 costs after the termination of its contract with Frontier Oil. Heavy equipment sales were higher than expected, which management attributed to pre-GST purchases and supplies to the jade mining industry in Myanmar. The "Others" division continued to bleed, as it booked a MYR49.5m net loss in 1Q15.
- ◆ **Forecasts and risks.** We slash our 2015-2017 estimates by 14.5%-21.1%. Headwinds at the automotive and oil & gas divisions may continue to persist, while equipment sales are likely to have peaked. The main risks are unfavourable exchange rates, weaker consumer sentiment and lower oil prices.
- ◆ **Unjustifiable valuations.** UMW trades at a forward P/E of 16x – well in excess of its historical average P/E of 12x that we are unable to justify given the lack of earnings growth. Assuming a payout ratio of 60%, the stock offers an unattractive yield of 3.3%. We cut our SOP-derived TP to MYR8.65 (see Figure 5) from MYR9.70, and reiterate our SELL call.

| Forecasts and Valuations | Dec-13 | Dec-14 | Dec-15F | Dec-16F | Dec-17F |
|-------------------------------------|--------|--------|---------|---------|---------|
| Total turnover (MYRm) | 13,951 | 14,959 | 12,645 | 14,207 | 3,583 |
| Reported net profit (MYRm) | 653 | 658 | 681 | 780 | 829 |
| Recurring net profit (MYRm) | 853 | 514 | 681 | 780 | 829 |
| Recurring net profit growth (%) | (14.2) | (39.7) | 32.5 | 14.7 | 6.3 |
| Recurring EPS (MYR) | 0.73 | 0.44 | 0.58 | 0.67 | 0.71 |
| DPS (MYR) | 0.44 | 0.41 | 0.35 | 0.40 | 0.43 |
| Recurring P/E (x) | 14.7 | 24.3 | 18.4 | 16.0 | 15.1 |
| P/B (x) | 1.96 | 1.90 | 1.90 | 1.91 | 1.92 |
| P/CF (x) | 13.9 | 11.8 | 7.7 | 11.3 | 5.1 |
| Dividend Yield (%) | 4.1 | 3.8 | 3.3 | 3.7 | 4.0 |
| EV/EBITDA (x) | 8.97 | 8.34 | 9.68 | 9.31 | 8.85 |
| Return on average equity (%) | 11.6 | 10.2 | 10.3 | 11.9 | 12.7 |
| Net debt to equity (%) | 4.6 | 7.6 | 8.4 | 15.4 | 9.6 |
| Our vs consensus EPS (adjusted) (%) | | | (24.9) | (21.0) | (16.7) |

Source: Company data, RHB

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Figure 1: Earnings review

| FYE Dec (MYRm) | 1Q14 | 4Q14 | 1Q15 | QoQ (%) | YoY (%) | Comments |
|--------------------------|----------------|----------------|----------------|---------------|---------------|--|
| Revenue | 3,583.4 | 3,706.1 | 3,240.4 | (12.6) | (9.6) | Lower revenue due mainly to significantly weaker Toyota sales |
| EBIT | 433.3 | 226.5 | 283.5 | 25.1 | (34.6) | Weaker EBIT margins YoY due to the stronger USD and negative operating leverage at the automotive division. Note that 4Q14 earnings were depressed by heavy provisioning at its "Others" division. |
| <i>EBIT margin (%)</i> | <i>12.1</i> | <i>6.1</i> | <i>8.7</i> | | | |
| Finance costs | (25.2) | (23.9) | (32.2) | 34.5 | 27.8 | |
| Associates | 40.7 | 49.4 | 33.4 | (32.3) | (17.8) | |
| Investment income | 30.5 | 37.1 | 35.3 | (5.0) | 15.5 | |
| Pretax Profit | 479.4 | 289.1 | 320.0 | 10.7 | (33.2) | |
| <i>Pretax margin (%)</i> | <i>13.4</i> | <i>7.8</i> | <i>9.9</i> | | | |
| Tax | (87.3) | (93.1) | (84.0) | (9.8) | (3.8) | Effective tax rate was in line |
| <i>Eff tax rate (%)</i> | <i>(18.2)</i> | <i>(32.2)</i> | <i>(26.3)</i> | | | |
| MI | (156.5) | (112.8) | (70.9) | (37.2) | (54.7) | |
| Net Profit | 235.5 | 83.2 | 165.2 | 98.6 | (29.9) | |
| <i>Net Margin (%)</i> | <i>6.6</i> | <i>2.2</i> | <i>5.1</i> | | | |

Source: Company data

Figure 2: Earnings review – segmental breakdown

| FYE Dec (MYRm) | 1Q14 | 4Q14 | 1Q15 | QoQ (%) | YoY (%) | Comments |
|-------------------|----------------|----------------|----------------|---------------|---------------|--|
| Automotive | 2,656.4 | 2,573.5 | 2,005.5 | (22.1) | (24.5) | Affected by lower Toyota sales |
| Oil & Gas | 195.6 | 327.7 | 312.5 | (4.6) | 59.8 | Lower charter rates and lower rig utilisation rates |
| Equipment | 434.9 | 445.6 | 653.0 | 46.5 | 50.1 | Above expectations from pre-GST purchases and sales to the Myanmar jade mining industry. May not be sustainable in subsequent quarters |
| Mfg & Eng | 181.9 | 173.3 | 171.1 | (1.3) | (6.0) | |
| Others | 114.5 | 186.1 | 98.3 | (47.2) | (14.2) | |
| Revenue | 3,583.4 | 3,706.1 | 3,240.4 | (12.6) | (9.6) | |
| Automotive | 406.6 | 313.1 | 233.5 | (25.4) | (42.6) | Affected by the stronger USD and negative operating leverage |
| Oil & Gas | 58.3 | 85.8 | 42.5 | (50.5) | (27.2) | |
| Equipment | 39.1 | 78.7 | 99.3 | 26.2 | 154.0 | Improved operating leverage from higher revenue |
| Mfg & Eng | 9.6 | (4.4) | 1.8 | (141.0) | (81.3) | |
| Others | (34.2) | (184.1) | (57.1) | (69.0) | 66.8 | |
| PBT | 479.4 | 289.1 | 320.0 | 10.7 | (33.2) | |
| Margins | | | | | | |
| Automotive | 15.3 | 12.2 | 11.6 | | | |
| Oil & Gas | 29.8 | 26.2 | 13.6 | | | |
| Equipment | 9.0 | 17.7 | 15.2 | | | |
| Mfg & Eng | 5.3 | (2.5) | 1.1 | | | |
| Others | (29.9) | (98.9) | (58.1) | | | |
| PBT | 13.4 | 7.8 | 9.9 | | | |
| Automotive | 192.3 | 152.8 | 116.7 | (23.6) | (39.3) | |
| Oil & Gas | 29.6 | 39.3 | 17.9 | (54.4) | (39.5) | |
| Equipment | 38.7 | 69.4 | 78.7 | 13.4 | 103.4 | |
| Mfg & Eng | 4.3 | 1.5 | 1.3 | (12.0) | (69.4) | |
| Others | (29.3) | (179.8) | (49.5) | (72.5) | 68.6 | |
| NP | 235.5 | 83.2 | 165.2 | 98.6 | (29.9) | |
| NP Margins | | | | | | |
| Automotive | 7.2 | 5.9 | 5.8 | | | |
| Oil & Gas | 15.1 | 12.0 | 5.7 | | | |
| Equipment | 8.9 | 15.6 | 12.1 | | | |
| Mfg & Eng | 2.3 | 0.9 | 0.8 | | | |
| Others | (25.6) | (96.6) | (50.4) | | | |
| | 6.6 | 2.9 | 5.1 | | | |

Source: Company data

Figure 3: UMW's vehicle sales summary

| FYE Dec (units) | 1Q14 | 4Q14 | 1Q15 | QoQ (%) | YoY (%) |
|--------------------|---------------|---------------|---------------|---------------|---------------|
| Toyota | 24,634 | 27,821 | 16,603 | (40.3) | (32.6) |
| - Passenger | 18,325 | 19,708 | 11,084 | (43.8) | (39.5) |
| - Commercial | 6,309 | 8,113 | 5,519 | (32.0) | (12.5) |
| Perodua | 44,024 | 55,262 | 57,153 | 3.4 | 29.8 |
| - Passenger | 44,024 | 55,262 | 57,153 | 3.4 | 29.8 |
| - Commercial | 0 | 0 | 0 | 0.0 | 0.0 |
| Total | 68,658 | 83,083 | 73,756 | (11.2) | 7.4 |

Source: MAA

Figure 4: Forecast assumptions

| FYE Dec | 2014 | 2015F | 2016F | 2017F |
|------------------------|---------|---------|---------|---------|
| Toyota / Lexus (units) | 103,636 | 80,000 | 90,000 | 95,000 |
| Perodua (units) | 195,579 | 208,000 | 210,000 | 211,000 |
| Forex (JPY/MYR)* | 3.15 | 3.00 | 3.00 | 3.00 |
| Forex (USD/MYR)* | 3.25 | 3.50 | 3.50 | 3.50 |
| *average rate | | | | |

Source: RHB estimates

Figure 5: SOP valuation

| | P/E (x) | Valuation (MYR) | Stake (%) | Discount (%) | Per UMW share (MYR) |
|-------|---------|-----------------|-----------|--------------|---------------------|
| UMWOG | | MYR 1.78 | 55.15 | 10 | 1.63 |
| Auto | 13.0 | | | | 6.75 |
| Other | 10.0 | | | | 0.26 |
| | | | | | 8.65 |

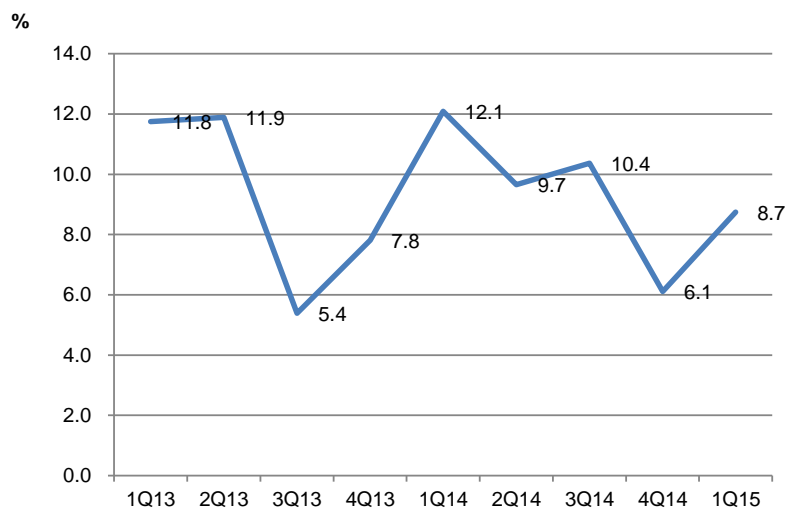
Source: RHB estimates

Figure 6: Historical quarterly earnings

| FYE Dec (MYRm) | 2Q13 | 3Q13 | 4Q13 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 1Q15 |
|-------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Revenue | 3,499.2 | 3,456.6 | 3,891.8 | 3,583.4 | 3,966.8 | 3,702.5 | 3,706.1 | 3,240.4 |
| Growth q-o-q (%) | 4.2 | -1.2 | 12.6 | -7.9 | 10.7 | -6.7 | 0.1 | -12.6 |
| Growth y-o-y (%) | -14.8 | -12.7 | -3.9 | 6.7 | 13.4 | 7.1 | -4.8 | -9.6 |
| EBIT | 415.9 | 186.3 | 304.1 | 433.3 | 382.9 | 383.9 | 226.5 | 283.5 |
| <i>EBIT Margin (%)</i> | <i>11.9</i> | <i>5.4</i> | <i>7.8</i> | <i>12.1</i> | <i>9.7</i> | <i>10.4</i> | <i>6.1</i> | <i>8.7</i> |
| Interest expense | (28.8) | (21.5) | (32.2) | (25.2) | (20.1) | (12.8) | (23.9) | (32.2) |
| Interest income | 16.6 | 18.6 | 28.1 | 30.5 | 35.4 | 33.5 | 37.1 | 35.3 |
| Associates | 39.4 | 62.2 | 33.6 | 40.7 | 23.8 | 25.6 | 49.4 | 33.4 |
| EI/Others | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Pretax profit | 443.2 | 245.6 | 333.7 | 479.4 | 422.1 | 430.3 | 289.1 | 320.0 |
| <i>Pretax Margin (%)</i> | <i>12.7</i> | <i>7.1</i> | <i>8.6</i> | <i>13.4</i> | <i>10.6</i> | <i>11.6</i> | <i>7.8</i> | <i>9.9</i> |
| Tax | (101.2) | (66.7) | (104.0) | (87.3) | (128.1) | (100.6) | (93.1) | (84.0) |
| <i>Effective tax rate (%)</i> | <i>22.8</i> | <i>27.1</i> | <i>31.2</i> | <i>18.2</i> | <i>30.3</i> | <i>23.4</i> | <i>32.2</i> | <i>26.3</i> |
| Minority Interest | (91.0) | (77.5) | (120.6) | (156.5) | (152.0) | (132.7) | (112.8) | (70.9) |
| Net Profit | 251.0 | 101.5 | 109.1 | 235.5 | 142.0 | 197.0 | 83.2 | 165.2 |
| Core Profit | 251.0 | 101.5 | 109.1 | 235.5 | 142.0 | 197.0 | 83.2 | 165.2 |
| <i>Net Margin (%)</i> | <i>7.2</i> | <i>2.9</i> | <i>2.8</i> | <i>6.6</i> | <i>3.6</i> | <i>5.3</i> | <i>2.2</i> | <i>5.1</i> |

Source: Company data

Figure 7: EBIT margin trend



Source: Company data

Financial Exhibits

| Profit & Loss (MYRm) | Dec-13 | Dec-14 | Dec-15F | Dec-16F | Dec-17F |
|--|---------------|---------------|----------------|----------------|----------------|
| Total turnover | 13,951 | 14,959 | 12,645 | 14,207 | 3,583 |
| Cost of sales | (10,129) | (10,845) | (9,168) | (10,300) | (2,598) |
| Gross profit | 3,823 | 4,114 | 3,477 | 3,907 | 985 |
| Gen & admin expenses | (1,278) | (1,393) | (1,519) | (1,655) | (1,804) |
| Selling expenses | (453) | (507) | (391) | (440) | (465) |
| Other operating costs | (795) | (787) | (347) | (394) | 2,803 |
| Operating profit | 1,296 | 1,427 | 1,220 | 1,417 | 1,519 |
| Operating EBITDA | 1,612 | 1,806 | 1,617 | 1,822 | 1,924 |
| Depreciation of fixed assets | (315) | (379) | (397) | (405) | (405) |
| Operating EBIT | 1,296 | 1,427 | 1,220 | 1,417 | 1,519 |
| Net income from investments | 158 | 140 | 159 | 178 | 192 |
| Interest income | 81 | 137 | 166 | 144 | 139 |
| Interest expense | (99) | (82) | (96) | (96) | (96) |
| Pre-tax profit | 1,436 | 1,621 | 1,449 | 1,643 | 1,754 |
| Taxation | (351) | (409) | (362) | (394) | (421) |
| Minority interests | (431) | (554) | (406) | (469) | (504) |
| Profit after tax & minorities | 653 | 658 | 681 | 780 | 829 |
| Reported net profit | 653 | 658 | 681 | 780 | 829 |
| Recurring net profit | 853 | 514 | 681 | 780 | 829 |

Source: Company data, RHB

| Cash flow (MYRm) | Dec-13 | Dec-14 | Dec-15F | Dec-16F | Dec-17F |
|--|----------------|---------------|----------------|----------------|----------------|
| Operating profit | 1,296 | 1,427 | 1,220 | 1,417 | 1,519 |
| Depreciation & amortisation | 315 | 379 | 397 | 405 | 405 |
| Change in working capital | (414) | (205) | 466 | (226) | 1,056 |
| Other operating cash flow | 176 | (43) | - | - | - |
| Operating cash flow | 1,374 | 1,558 | 2,084 | 1,596 | 2,980 |
| Interest paid | (95) | (90) | (96) | (96) | (96) |
| Tax paid | (381) | (409) | (362) | (394) | (421) |
| Cash flow from operations | 898 | 1,059 | 1,625 | 1,106 | 2,463 |
| Capex | (950) | (2,080) | (1,200) | (1,200) | (1,200) |
| Other new investments | (217) | (44) | - | - | - |
| Other investing cash flow | 1,055 | 1,400 | 166 | 144 | 139 |
| Cash flow from investing activities | (111) | (723) | (1,034) | (1,056) | (1,061) |
| Dividends paid | (584) | (514) | (479) | (408) | (468) |
| Proceeds from issue of shares | 1 | - | - | - | - |
| Increase in debt | 308 | 1,183 | (14) | - | - |
| Other financing cash flow | (1,052) | (1,023) | (704) | (801) | (849) |
| Cash flow from financing activities | (1,327) | (354) | (1,197) | (1,209) | (1,317) |
| Cash at beginning of period | 2,493 | 2,544 | 3,376 | 3,249 | 2,497 |
| Total cash generated | (540) | (19) | (606) | (1,160) | 85 |
| Forex effects | 591 | 851 | 479 | 408 | 468 |
| Implied cash at end of period | 2,544 | 3,376 | 3,249 | 2,497 | 3,050 |

Source: Company data, RHB

Financial Exhibits

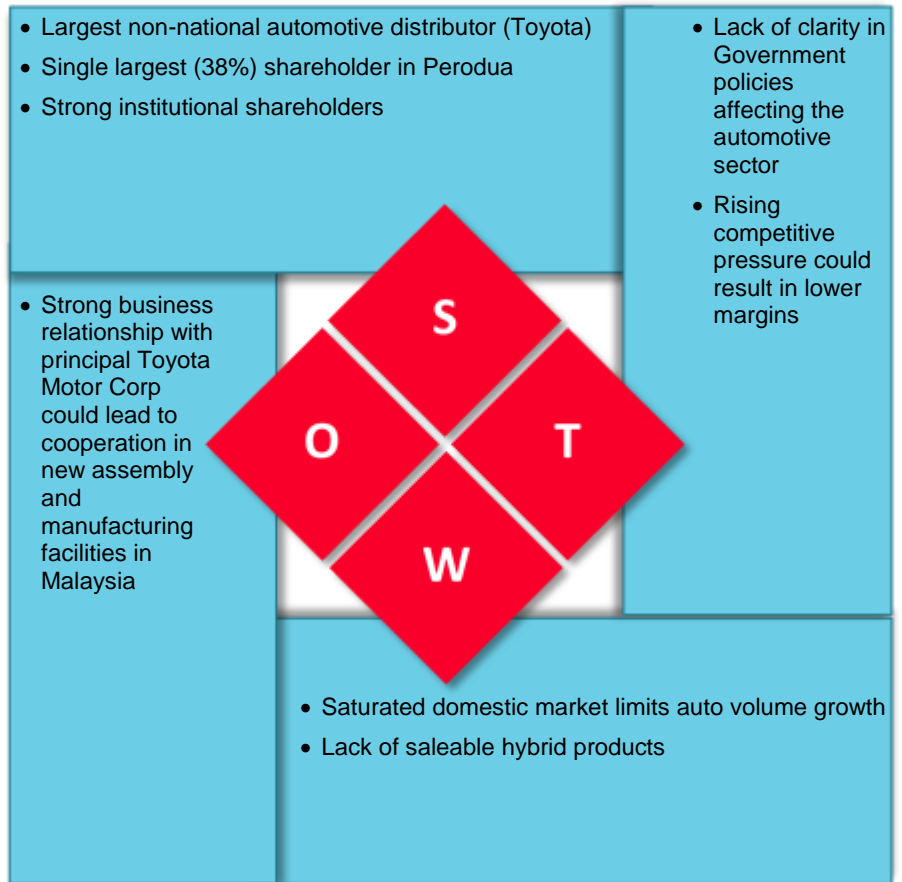
| Balance Sheet (MYRm) | Dec-13 | Dec-14 | Dec-15F | Dec-16F | Dec-17F |
|---------------------------------------|---------------|---------------|----------------|----------------|----------------|
| Total cash and equivalents | 2,544 | 3,376 | 3,249 | 2,497 | 3,050 |
| Inventories | 1,752 | 1,835 | 1,559 | 1,752 | 442 |
| Accounts receivable | 1,229 | 1,326 | 866 | 973 | 245 |
| Other current assets | 3,207 | 1,997 | 1,931 | 2,078 | 1,561 |
| Total current assets | 8,731 | 8,534 | 7,605 | 7,299 | 5,298 |
| Total investments | 1,827 | 1,878 | 2,036 | 2,215 | 2,407 |
| Tangible fixed assets | 3,893 | 5,646 | 6,449 | 7,244 | 8,039 |
| Intangible assets | 38 | 38 | 38 | 38 | 38 |
| Total other assets | 317 | 344 | 344 | 344 | 344 |
| Total non-current assets | 6,075 | 7,905 | 8,867 | 9,841 | 10,828 |
| Total assets | 14,807 | 16,439 | 16,472 | 17,140 | 16,126 |
| Short-term debt | 1,354 | 2,177 | 2,177 | 2,177 | 2,177 |
| Accounts payable | 1,186 | 1,173 | 879 | 988 | 249 |
| Other current liabilities | 1,516 | 1,536 | 1,494 | 1,606 | 846 |
| Total current liabilities | 4,055 | 4,886 | 4,551 | 4,771 | 3,273 |
| Total long-term debt | 1,602 | 1,914 | 1,900 | 1,900 | 1,900 |
| Other liabilities | 172 | 196 | 196 | 196 | 196 |
| Total non-current liabilities | 1,775 | 2,110 | 2,096 | 2,096 | 2,096 |
| Total liabilities | 5,830 | 6,997 | 6,647 | 6,867 | 5,369 |
| Share capital | 584 | 584 | 584 | 584 | 584 |
| Retained earnings reserve | 4,924 | 5,116 | 5,093 | 5,072 | 5,052 |
| Other reserves | 854 | 890 | 890 | 890 | 890 |
| Shareholders' equity | 6,363 | 6,590 | 6,566 | 6,546 | 6,526 |
| Minority interests | 2,614 | 2,853 | 3,259 | 3,727 | 4,231 |
| Total equity | 8,977 | 9,443 | 9,825 | 10,273 | 10,757 |
| Total liabilities & equity | 14,807 | 16,439 | 16,472 | 17,140 | 16,126 |

Source: Company data, RHB

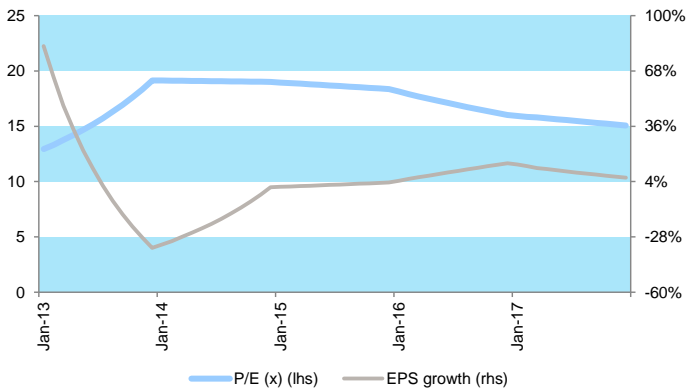
| Key Ratios (MYR) | Dec-13 | Dec-14 | Dec-15F | Dec-16F | Dec-17F |
|-------------------------------|---------------|---------------|----------------|----------------|----------------|
| Revenue growth (%) | (11.8) | 7.2 | (15.5) | 12.3 | (74.8) |
| Operating profit growth (%) | (31.7) | 10.1 | (14.5) | 16.1 | 7.2 |
| Net profit growth (%) | (34.3) | 0.7 | 3.5 | 14.7 | 6.3 |
| EPS growth (%) | (34.3) | 0.7 | 3.5 | 14.7 | 6.3 |
| BVPS growth (%) | 31.2 | 3.6 | (0.4) | (0.3) | (0.3) |
| Operating margin (%) | 9.3 | 9.5 | 9.7 | 10.0 | 42.4 |
| Net profit margin (%) | 4.7 | 4.4 | 5.4 | 5.5 | 23.1 |
| Return on average assets (%) | 5.0 | 4.2 | 4.1 | 4.6 | 5.0 |
| Return on average equity (%) | 11.6 | 10.2 | 10.3 | 11.9 | 12.7 |
| Net debt to equity (%) | 4.6 | 7.6 | 8.4 | 15.4 | 9.6 |
| DPS | 0.44 | 0.41 | 0.35 | 0.40 | 0.43 |
| Recurrent cash flow per share | 0.77 | 0.91 | 1.39 | 0.95 | 2.11 |

Source: Company data, RHB

SWOT Analysis

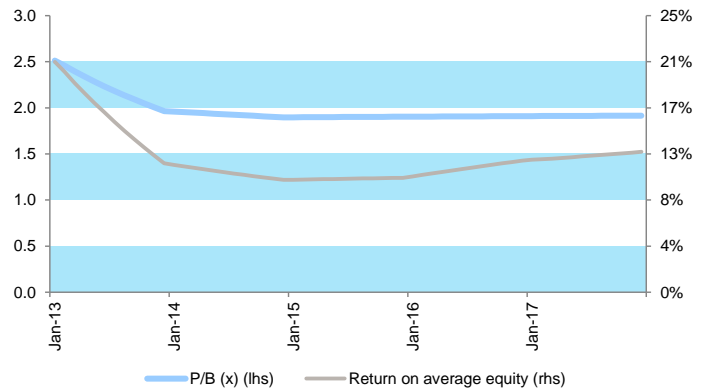


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

Company Profile

UMW is the largest company in the automotive sector and a component stock of the FBM KLCI. Its 51%-owned subsidiary UMW-Toyota imports, assembles and distributes Toyota and Lexus vehicles in Malaysia. UMW also owns a 55% stake in listed UMW Oil & Gas.

Recommendation Chart



Source: RHB, Bloomberg

| Date | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 2015-02-27 | Sell | 9.7 | 11.1 |
| 2014-11-27 | Neutral | 11.0 | 11.3 |
| 2014-08-28 | Neutral | 12.4 | 12.3 |
| 2014-05-25 | Neutral | 11.3 | 10.8 |
| 2014-04-29 | Neutral | 11.3 | 10.8 |
| 2013-03-20 | Neutral | 12.9 | 13.3 |
| 2013-02-28 | Neutral | 12.9 | 12.8 |
| 2013-02-27 | Neutral | 12.9 | 12.3 |
| 2013-02-26 | Neutral | 13.1 | 12.1 |
| 2013-01-25 | Neutral | 13.1 | 12.1 |

Source : RHB, Bloomberg

RHB Guide to Investment Ratings

Buy: Share price may exceed 10% over the next 12 months

Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated: Stock is not within regular research coverage

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