

Company Guide

UMW Holdings

Version 2 | Bloomberg: UMWK MK | Reuters: UMWS.KL

Refer to important disclosures at the end of this report

Malaysia Equity Research

26 Feb 2016

HOLD

Last Traded Price: RM6.95 (KLCI : 1,658.16)

Price Target : RM6.40 (-8% downside) (Prev RM7.40)

Shariah Compliant: Yes

Where we differ: We are below consensus on slower car sales growth

Analyst

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What's New

- 4Q15 net profit was below expectations
- Lower contribution from oil and gas segment; margins contracted
- Cut FY16-17F net profit by 24-32%

Price Relative



Forecasts and Valuation

FY Dec (RM m)	2015A	2016F	2017F	2018F
Revenue	14,420	13,326	13,641	13,878
EBITDA	900	961	1,082	1,154
Pre-tax Profit	266	707	871	944
Net Profit	(38.9)	353	429	462
Net Pft (Pre Ex.)	578	353	429	462
Net Pft Gth (Pre-ex) (%)	77.4	(38.9)	21.6	7.8
EPS (sen)	(3.3)	30.2	36.7	39.6
EPS Pre Ex. (sen)	49.5	30.2	36.7	39.6
EPS Gth Pre Ex (%)	77	(39)	22	8
Diluted EPS (sen)	49.5	30.2	36.7	39.6
Net DPS (sen)	20.0	15.1	18.4	19.8
BV Per Share (sen)	548	563	581	601
PE (X)	nm	23.0	18.9	17.6
PE Pre Ex. (X)	14.1	23.0	18.9	17.6
P/Cash Flow (X)	21.6	5.9	9.4	9.2
EV/EBITDA (X)	16.1	15.0	14.0	13.7
Net Div Yield (%)	2.9	2.2	2.6	2.8
P/Book Value (X)	1.3	1.2	1.2	1.2
Net Debt/Equity (X)	0.4	0.3	0.4	0.4
ROAE (%)	(0.6)	5.4	6.4	6.7
Earnings Rev (%):		(32)	(24)	N/A
Consensus EPS (sen):		41.9	48.3	N/A
Other Broker Recs:		B: 1	S: 9	H: 6

Source of all data: Company, AllianceDBS Research, Bloomberg Finance L.P

Navigating a tough course

Cautious outlook for near-term earnings. We cut FY16-17F earnings by 24%-32% after imputing lower margins for the auto business due to increasingly competitive operating conditions as well as further weakness in the oil and gas segment. We maintain our Hold rating for UMW with a reduced TP of RM6.40 based on SOP valuation. The group faces near-term earnings headwinds as its O&G business will be hurt by the sharp drop in oil prices, while the Toyota franchise wrestles with a challenging operating environment.

Dragged by O&G segment. Low crude oil prices will see lower activities in both exploration and development of new oil and gas fields, resulting in lower drilling and workover activities. The impact is spilling over into UMWOG, which has been seeing slower tender activity in recent months.

Auto sales facing intense competition. The group's Toyota sales recorded a 7.5% drop y-o-y to 95,861 units in 2015. We expect 1H16 sales outlook to remain difficult because of intense competition amid a more challenging economic environment and weak consumer sentiment. Despite relatively resilient Perodua sales (+9.1% y-o-y), the associate's contribution is not sufficient to overturn slower earnings from lower Toyota profits.

Valuation:

Maintain Hold call. We maintain our Hold rating for UMW with a reduced TP of RM6.40 based on SOP. In our view, a recovery in O&G earnings and Toyota profits would be catalysts.

Key Risks to Our View:

Sharp recovery in auto sales. Significantly stronger Toyota vehicle unit sales could revive earnings and re-rate the stock.

At A Glance

Issued Capital (m shrs)	1,168
Mkt. Cap (RMm/US\$m)	8,120 / 1,929
Major Shareholders (%)	
Skim Amanah Saham Bumiputera	43.4
Permodalan Nasional Bhd	12.6
Employees Provident Fund	6.7
Free Float (%)	37.3
3m Avg. Daily Val (US\$m)	1.7
ICB Industry : Consumer Goods / Automobiles & Parts	

WHAT'S NEW**4Q15 results in the red****Highlights****Below expectations**

- UMW recorded net loss of RM286.0m in 4Q15. YTD net loss came in at RM38.9m, below our and consensus expectations. This was largely due to the total asset and goodwill impairment of RM337.3m for oil and gas segment and forex impact of RM700m.
- The group declared 10 sen DPS. This brings total DPS for FY15 to 20 sen (41 sen in FY14).

Lower contribution from segments

- Auto pretax profit fell by 21% y-o-y to RM247.8m dragged by lower margins and impact from the depreciating ringgit against USD. The aggressive promotions and road shows on top of the weaker Ringgit Malaysia caused pre-tax profit margins to drop y-o-y to 7.3% (in 4Q15) from 12.2% (in 4Q14) despite 31% y-o-y higher revenue of RM3,375.9m.
- Oil and gas recorded pre-tax loss of RM411.3m in 4Q15 mainly from the provision of assets and goodwill impairment (RM337.7m) as well as lower time charter rates and lower utilisation of assets. Before asset and goodwill impairment, oil and gas recorded a loss before taxation of RM73.6m in 4Q15.

- Equipment segment recorded lower revenue (-10 y-o-y to RM402.9m) and lower profit before tax (-65% y-o-y to RM27.5m) when compared to 4Q14, which was boosted by the resumption of jade activity in Myanmar. Demand subsequently normalised in 2015.

Cut FY16-17F net profit by 24%/32%

- We cut our FY15/16F net profit by 32%/24% incorporating lower auto sales and larger losses for the oil and gas segment.

Outlook**Near term earnings under pressure**

- January 2016 numbers for auto sales were weak, with TIV of 44,591 units (-35.8% q-o-q; -11.9% y-o-y). This could be the trend for auto sales in the near term given the hike in prices and tough economic conditions.
- There could be further weakness ahead for the oil & gas operations as most of its drilling rigs are on short-term charters. With the decline in charter rates and oversupply of jack-up rigs, we expect recovery in the drilling market will take another 2-3 years.

Valuation

We maintain our Hold rating for UMW with a reduced TP of RM6.40 based on SOP valuation factoring in lower earnings from the auto sales and oil and gas segment.

Quarterly / Interim Income Statement (RMm)

FY Dec	4Q2014	3Q2015	4Q2015	% chg yoy	% chg qoq
Revenue	3,703	3,533	4,161	12.4	17.8
Cost of Goods Sold	(3,344)	(3,631)	(4,546)	35.9	25.2
Gross Profit	358	(97.4)	(385)	nm	nm
Other Oper. (Exp)/Inc	25.6	164	25.2	(1.7)	(84.7)
Operating Profit	384	66.8	(360)	nm	nm
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	nm	nm
Associates & JV Inc	25.6	(0.3)	35.8	39.6	nm
Net Interest (Exp)/Inc	20.7	5.75	(10.3)	nm	nm
Pre-tax Profit	430	72.2	(334)	nm	nm
Tax	(101)	(44.3)	(57.3)	(43.0)	29.3
Minority Interest	(133)	(14.4)	106	nm	nm
Net Profit	197	13.5	(286)	nm	nm
Net profit bef Except.	229	(73.7)	(44.7)	nm	39.4
EBITDA	384	66.8	(360)	nm	nm
Margins (%)					
Gross Margins	9.7	(2.8)	(9.2)		
Opg Profit Margins	10.4	1.9	(8.6)		
Net Profit Margins	5.3	0.4	(6.9)		

Source of all data: Company, AllianceDBS Research

CRITICAL DATA POINTS TO WATCH

Earnings Drivers:

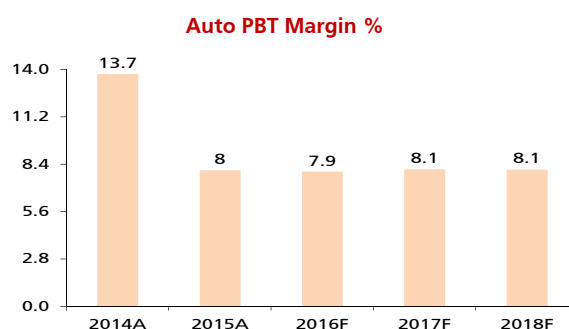
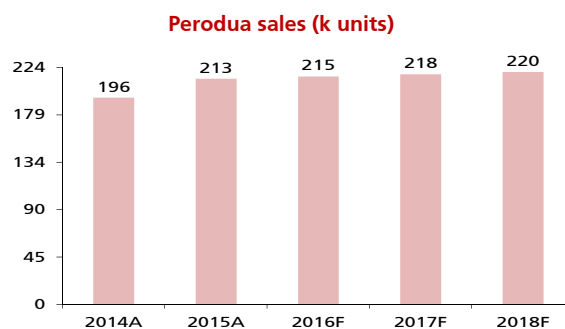
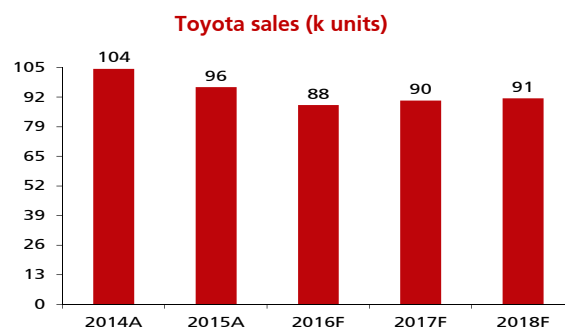
Expect lower Toyota sales volume this year. UMW's assembly and distribution operation for Toyota and Lexus cars contributed 81% of group revenue in 4Q15. Following a weak 3Q15, sales recovered by 36% q-o-q to 32,398 units in 4Q15. YTD Toyota's market share came in at 14.4% making it the top non-national car, slightly ahead of Honda's 14.2% market share. Overall, we expect Toyota sales volume to decline in FY16 as guided by management and improve marginally in FY17-18F.

Promotions and new launches will help lift sales volumes. The volume recovery in 4Q15 was supported by recent promotions as well as consumers buying forward in anticipation of higher car prices in 2016. The new Lexus IS 200t, Lexus RX as well as the Toyota Avanza were launched in 4Q15. Upcoming launches such as the new Toyota Hilux, Toyota Fortuner SUV and Toyota Innova MPV which will be coming in by 2Q16 and the all-new Toyota Alphard and Vellfire planned for 3Q16 should help sales volume and capture market share.

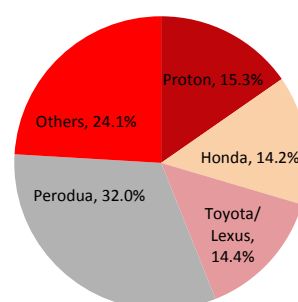
Margins under pressure. Although the promotions and added features would help to support sales volumes for the rest of the year, they could also result in weaker margins for the auto division. Pretax profit margins for the division have fallen for five consecutive years. Margins were also weighed down by higher costs (for imported materials) arising from the weaker ringgit.

Resilient Perodua volumes. UMW has a 38% stake in Perodua. Perodua had done well the past few quarters with impressive sales of new models. Perodua had 32.0% market share in FY15, way above Proton's 15.3% market share. Perodua is attracting buyers amid the slower economy, by offering a solid value proposition at reasonable pricing for Myvi (RM44k) and Axia (RM33k). As of now, it is holding on to current prices as much as it can. However, it does not rule out the possibility of a price increase should the foreign exchange situation worsen.

Challenging outlook for O&G segment. UMW has a 55.2% stake in UMWOG. The O&G segment accounted for 3% of group revenue in 4Q15. Contracting activity has shrunk significantly, with only three rigs contracted in June-July, compared to eight in May. In our view, the weak drilling market will persist as oil producers continue to cut capex and scale back exploration activity amid the crude oil supply glut.



Auto Sales YTD 2015



Source: Company, AllianceDBS Research

UMW Holdings

New aerospace venture. UMW has recently entered into an agreement with Rolls Royce to manufacture and assemble fan cases for the Trent 1000 engines. This potential new earnings stream is conceptually positive and allows the group to reduce dependence on the auto and O&G businesses. The production and facility details have not been finalised. We do not expect the business to contribute until FY2018. It has recently earmarked 12ha of land in Serendah, Selangor for a proposed plant. The earthworks on the site is progressing as planned and the group is currently on course to deliver its first unit of Trent 1000 fan case aero engines upon receipt of first purchase order targeted for October 2017.

Balance Sheet:

O&G business has USD debt exposure. Net gearing stood at 0.38x as at end-FY15. Total debt amounted to RM5.9bn, mostly denominated in USD (including USD931.6m at UMWOG). Capex was RM2.2bn in FY15 with RM1.6bn for the O&G segment. The group has RM2.7bn consolidated cash and deposits, and net asset per share is RM5.48 as at FY15.

Share Price Drivers:

Stronger auto sales and margins; reversal in crude oil prices. The stock price has fallen along with the slower sales and more competitive auto industry. A recovery in Toyota unit sales and margins would be a key earnings and share price driver. The stock also took a hit following the sharp drop in crude oil prices in late 2014, as the group's O&G profits tumbled along with oil prices. A reversal in crude oil prices will likely boost UMW's share price.

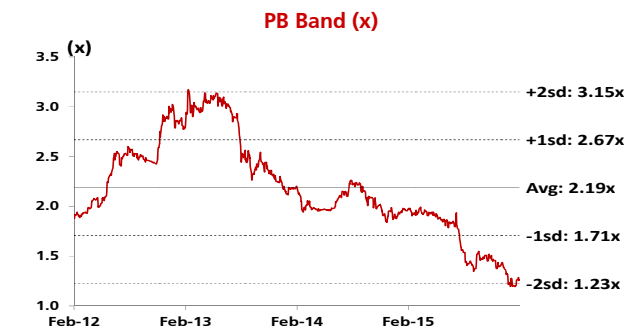
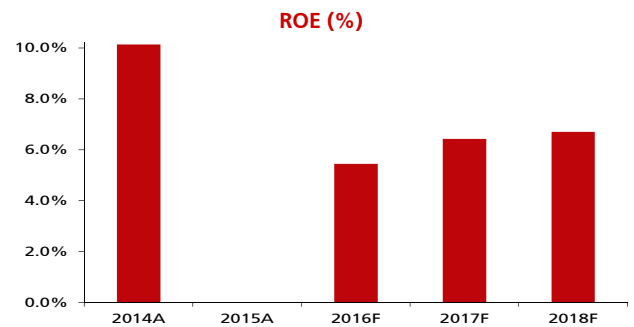
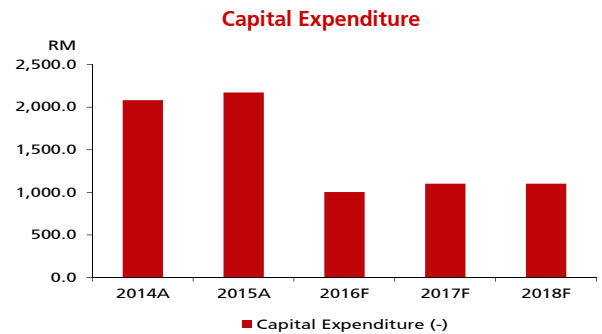
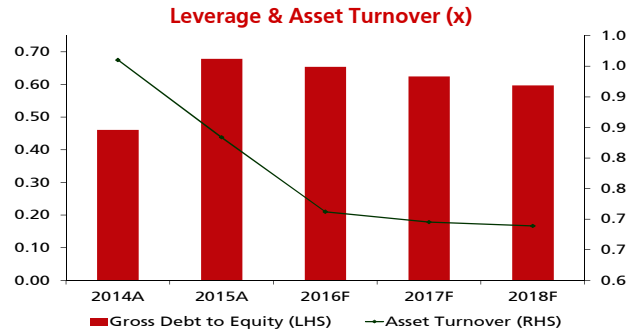
Key Risks:

Sharp recovery in auto sales. Significantly stronger Toyota vehicle unit sales could revive earnings and re-rate the stock.

Higher cost. The increase in car prices will help manufacturers cover part of the increase in imported cost (arising from the Ringgit's depreciation). However, further weakening of the Ringgit would be a risk for the manufacturers.

Company Background

UMW is the sole assembler and distributor of Toyota and Lexus vehicles. This includes marketing, sales services and auto parts trading. Its other business segments are Oil & Gas (owns jack-up drilling rigs and onshore rigs), Equipment (trading of industrial heavy equipment) and Manufacturing & Engineering (trading of lubricants).



Source: Company, AllianceDBS Research

Key Assumptions

FY Dec	2014A	2015A	2016F	2017F	2018F
Toyota sales (k units)	104	95.9	88.2	89.5	90.9
Perodua sales (k units)	196	213	215	218	220
Auto PBT Margin %	13.7	8.01	7.93	8.07	8.06

Segmental Breakdown

FY Dec	2014A	2015A	2016F	2017F	2018F
Revenues (RMm)					
Auto	10,766	10,710	9,481	9,623	9,768
Equipment	1,767	1,884	1,960	1,979	1,999
Manufacturing	725	703	710	717	724
O&G	1,015	840	805	944	1,002
Others	659	283	370	377	385
Total	14,932	14,420	13,326	13,641	13,878
PBT (RMm)					
Auto	1,475	858	752	777	787
Equipment	218	225	235	239	242
Manufacturing	14.8	16.3	15.6	15.8	15.9
O&G	284	(349)	(92.9)	(43.8)	(28.6)
Others	(371)	(484)	(203)	(117)	(72.4)
Total	1,621	266	707	871	944
PBT Margins (%)					
Auto	13.7	8.0	7.9	8.1	8.1
Equipment	12.3	11.9	12.0	12.1	12.1
Manufacturing	2.0	2.3	2.2	2.2	2.2
O&G	28.0	(41.6)	(11.5)	(4.6)	(2.9)
Others	(56.3)	(171.1)	(54.8)	(31.0)	(18.8)
Total	10.9	1.8	5.3	6.4	6.8

Income Statement (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Revenue	14,932	14,420	13,326	13,641	13,878
Cost of Goods Sold	(10,860)	(11,519)	(10,645)	(10,897)	(11,086)
Gross Profit	4,072	2,901	2,681	2,744	2,792
Other Opng (Exp)/Inc	(2,853)	(2,880)	(2,661)	(2,724)	(2,771)
Operating Profit	1,433	135	601	740	829
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	140	130	119	136	139
Net Interest (Exp)/Inc	48.9	0.59	(12.8)	(4.4)	(23.2)
Pre-tax Profit	1,621	266	707	871	944
Tax	(408)	(260)	(177)	(218)	(236)
Minority Interest	(561)	(44.6)	(178)	(224)	(246)
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	652	(38.9)	353	429	462
Net Profit before Except.	326	578	353	429	462
EBITDA	1,812	900	961	1,082	1,154
Growth					
Revenue Gth (%)	7.0	(3.4)	(7.6)	2.4	1.7
EBITDA Gth (%)	11.7	(50.3)	6.8	12.6	6.6
Opg Profit Gth (%)	10.5	(90.6)	345.7	23.1	12.0
Net Profit Gth (Pre-ex) (%)	(56.1)	77.4	(38.9)	21.6	7.8
Margins & Ratio					
Gross Margins (%)	27.3	20.1	20.1	20.1	20.1
Opg Profit Margin (%)	9.6	0.9	4.5	5.4	6.0
Net Profit Margin (%)	4.4	(0.3)	2.6	3.1	3.3
ROAE (%)	10.1	(0.6)	5.4	6.4	6.7
ROA (%)	4.2	(0.2)	1.9	2.2	2.3
ROCE (%)	8.3	0.0	2.9	3.4	3.7
Div Payout Ratio (%)	73.5	N/A	50.0	50.0	50.0
Net Interest Cover (x)	NM	NM	47.0	166.7	35.7

Source: Company, AllianceDBS Research

Quarterly / Interim Income Statement (RMm)

FY Dec	4Q2014	1Q2015	2Q2015	3Q2015	4Q2015
Revenue	3,703	3,240	3,485	3,533	4,161
Cost of Goods Sold	(3,344)	(3,029)	(3,337)	(3,631)	(4,546)
Gross Profit	358	212	149	(97.4)	(385)
Other Oper. (Exp)/Inc	25.6	72.0	27.3	164	25.2
Operating Profit	384	284	176	66.8	(360)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	25.6	33.4	29.5	(0.3)	35.8
Net Interest (Exp)/Inc	20.7	3.08	2.10	5.75	(10.3)
Pre-tax Profit	430	320	208	72.2	(334)
Tax	(101)	(84.0)	(74.3)	(44.3)	(57.3)
Minority Interest	(133)	(70.9)	(64.9)	(14.4)	106
Net Profit	197	165	68.4	13.5	(286)
Net profit bef Except.	229	159	67.0	(73.7)	(44.7)
EBITDA	384	284	176	66.8	(360)

Growth

Revenue Gth (%)	0.0	(12.5)	7.6	1.4	17.8
EBITDA Gth (%)	0.0	(26.2)	(37.9)	(62.0)	nm
Opg Profit Gth (%)	0.0	(26.2)	(37.9)	(62.0)	nm
Net Profit Gth (Pre-ex) (%)	27.1	(30.7)	(57.8)	nm	39.4

Margins

Gross Margins (%)	9.7	6.5	4.3	(2.8)	(9.2)
Opg Profit Margins (%)	10.4	8.7	5.0	1.9	(8.6)
Net Profit Margins (%)	5.3	5.1	2.0	0.4	(6.9)

Balance Sheet (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Net Fixed Assets	5,670	8,133	8,773	9,531	10,306
Invts in Associates & JVs	1,857	1,950	2,069	2,205	2,343
Other LT Assets	399	429	429	429	429
Cash & ST Invts	3,371	2,728	2,929	2,479	2,034
Inventory	1,830	1,892	1,633	1,672	1,701
Debtors	2,079	1,273	1,855	1,899	1,932
Other Current Assets	1,314	1,676	1,676	1,676	1,676
Total Assets	16,520	18,081	19,364	19,890	20,421
ST Debt	2,387	3,159	3,159	3,159	3,159
Creditor	2,217	1,165	1,979	2,025	2,060
Other Current Liab	466	1,368	1,483	1,524	1,542
LT Debt	1,959	3,100	3,100	3,100	3,100
Other LT Liabilities	57.8	64.8	64.8	64.8	64.8
Shareholder's Equity	6,580	6,397	6,573	6,788	7,019
Minority Interests	2,853	2,827	3,005	3,229	3,475
Total Cap. & Liab.	16,520	18,081	19,364	19,890	20,421
Non-Cash Wkg. Capital	2,540	2,308	1,703	1,698	1,706
Net Cash/(Debt)	(975)	(3,531)	(3,331)	(3,780)	(4,226)
Debtors Turn (avg days)	48.1	42.4	42.8	50.2	50.4
Creditors Turn (avg days)	74.6	57.4	55.8	69.2	69.3
Inventory Turn (avg days)	62.4	63.2	62.5	57.2	57.2
Asset Turnover (x)	1.0	0.8	0.7	0.7	0.7
Current Ratio (x)	1.7	1.3	1.2	1.2	1.1
Quick Ratio (x)	1.1	0.7	0.7	0.7	0.6
Net Debt/Equity (X)	0.1	0.4	0.3	0.4	0.4
Net Debt/Equity ex MI (X)	0.1	0.6	0.5	0.6	0.6
Capex to Debt (%)	47.8	34.6	16.0	17.6	17.6
Z-Score (X)	2.5	2.2	2.2	2.2	2.2

Source: Company, AllianceDBS Research

Cash Flow Statement (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Pre-Tax Profit	1,621	266	707	871	944
Dep. & Amort.	379	765	360	342	326
Tax Paid	(418)	(276)	(61.8)	(177)	(218)
Assoc. & JV Inc/(loss)	(140)	(130)	(119)	(136)	(139)
Chg in Wkg.Cap.	(149)	(134)	490	(35.7)	(26.8)
Other Operating CF	71.8	(116)	0.0	0.0	0.0
Net Operating CF	1,365	375	1,377	865	887
Capital Exp.(net)	(2,079)	(2,169)	(1,000)	(1,100)	(1,100)
Other Invt.(net)	(4.7)	(2.6)	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc & JV	122	100	0.0	0.0	0.0
Other Investing CF	1,647	167	0.0	0.0	0.0
Net Investing CF	(315)	(1,904)	(1,000)	(1,100)	(1,100)
Div Paid	(479)	(234)	(176)	(214)	(231)
Chg in Gross Debt	1,280	1,914	0.0	0.0	0.0
Capital Issues	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(597)	(794)	0.0	0.0	0.0
Net Financing CF	204	886	(176)	(214)	(231)
Currency Adjustments	6.44	15.6	0.0	0.0	0.0
Chg in Cash	1,260	(627)	201	(450)	(444)
Opg CFPS (sen)	130	43.6	75.9	77.1	78.2
Free CFPS (sen)	(61.1)	(154)	32.3	(20.1)	(18.2)

Source: Company, AllianceDBS Research

SOP Valuations

Division	Stake	Valuation	Value (RM m)	Per share
Automotive				
Toyota	51.0%	PE 12x	2828.71	2.42
Perodua	38.0%	PE 12x	1631.96	1.40
O&G	55.2%	0.5x book value	927.58	0.79
Equipment	100.0%	PE 11x	1940.07	1.66
Manufacturing & engineering	100.0%	PE 11x	128.81	0.11
Total			7,457.13	6.40

Target Price & Ratings History



S.No.	Date	Closing Price	Target Price	Rating
1:	27 Feb 15	11.08	12.70	HOLD
2:	13 Apr 15	10.76	10.80	HOLD
3:	18 May 15	10.82	10.80	HOLD
4:	27 May 15	10.56	10.80	HOLD
5:	22 Jun 15	10.28	9.90	HOLD
6:	26 Oct 15	8.12	7.95	HOLD
7:	16 Nov 15	8.00	7.95	HOLD
8:	27 Nov 15	8.03	7.40	HOLD
9:	11 Jan 16	7.47	7.40	HOLD
10:	18 Jan 16	7.22	7.40	HOLD
11:	25 Jan 16	6.78	7.40	HOLD
12:	01 Feb 16	7.01	7.40	HOLD
13:	10 Feb 16	6.59	7.40	HOLD

Note: Share price and Target price are adjusted for corporate actions.

Source: AllianceDBS Research

DISCLOSURE

Stock rating definitions

STRONG BUY	-	> 20% total return over the next 3 months, with identifiable share price catalysts within this time frame
BUY	-	> 15% total return over the next 12 months for small caps, >10% for large caps
HOLD	-	-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps
FULLY VALUED	-	negative total return > -10% over the next 12 months
SELL	-	negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame

Commonly used abbreviations

Adex = advertising expenditure	EPS = earnings per share	PBT = profit before tax
bn = billion	EV = enterprise value	P/B = price / book ratio
BV = book value	FCF = free cash flow	P/E = price / earnings ratio
CF = cash flow	FV = fair value	PEG = P/E ratio to growth ratio
CAGR = compounded annual growth rate	FY = financial year	q-o-q = quarter-on-quarter
Capex = capital expenditure	m = million	RM = Ringgit
CY = calendar year	M-o-m = month-on-month	ROA = return on assets
Div yld = dividend yield	NAV = net assets value	ROE = return on equity
DCF = discounted cash flow	NM = not meaningful	TP = target price
DDM = dividend discount model	NTA = net tangible assets	trn = trillion
DPS = dividend per share	NR = not rated	WACC = weighted average cost of capital
EBIT = earnings before interest & tax	p.a. = per annum	y-o-y = year-on-year
EBITDA = EBIT before depreciation and amortisation	PAT = profit after tax	YTD = year-to-date

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