

25 May 2016 | 1Q16 Result Review

## UMW Holdings

*Red ink*

- **UMW's 1Q16 fell into the red, missing estimates**
- **O&G remained in the red while autos saw massive earnings deterioration**
- **Forecasts slashed by 54%/48% over FY16F/17F following our recent -16% Toyota TIV cut. Coincidentally, management also trimmed Toyota-Lexus TIV forecast to 80K from 87K previously**
- **Maintain NEUTRAL and TP trimmed to RM5.60/share as we fall back to a book value based valuation**

**Falls into the red.** UMW registered a core net loss of RM202m for its 1Q16 (excluding unrealised fair value gain of RM216m, inventory write down of RM1.2m, provision for asset impairment of RM3.8m and reversal of impairment on receivables of RM8.1m) against consensus estimate of RM362m FY16F net profit and our previous FY16F net profit of RM334m. Bottomline fell into the red for the first time in this downcycle dragged mainly by O&G and autos.

**O&G division.** O&G revenue fell 33%qoq given lower rig utilisation and charter rate discounts. As we had mentioned in our recent report (dated 17<sup>th</sup> Mar 2016), those rigs that are in operations are now employed on a per well basis instead of a fixed timeline. As rigs are not necessarily deployed to the next well immediately upon completion of one, this negatively impacts utilisation rates.

Four of seven of UMW's jack-up rigs are still lying idle and this will be a key drag to profitability going forward. Of the three that is employed, Naga 4's contract expired in April 2016. The previous contract with Carigali provides a 2-year extension option but renewal rates are likely to be 30%-40% lower than previous contracted levels given depressed spot rates currently.

Current jack-up rig spot rates stand at USD80K-90K/day versus a range of USD145K-155K secured under previous contracts. The O&G division's core losses will persist into 2Q16 if the four laid-up rigs remain idle and if utilisation rates for the contracted rigs remain poor. We would not rule out further asset impairments if the situation persists.

**1Q16 should mark bottom though:** Auto earnings saw massive deterioration (-67%yoy). Firstly, Toyota TIV in 1Q16 (-68%qoq) was only a third that achieved in 4Q15, reflecting the drastic drying up of demand following pre-price hike purchases in the Nov-Dec 2015 period. Second, the 1Q16 reflected peak USD rates of 4.28 (vs. 4.05 in 4Q15 and 3.36 in 1Q15).

**Maintain NEUTRAL**  
**Revised Target price (TP): RM5.60**  
**(Previously RM6.00)**

RETURN STATS	
Price (24 May 2016)	RM5.40
Target Price	RM5.60
Expected Share Price Return	+3.7%
Expected Dividend Yield	+0.7%
<b>Expected Total Return</b>	<b>+4.4 %</b>

STOCK INFO	
KLCI	1,625.84
Bursa / Bloomberg	4588 / UMWK MK
Board / Sector	Main/Automotive
Syariah Compliant	Yes
Issued shares (mil)	1,168.29
Par Value (RM)	1.00
Market cap. (RM'm)	6,308.79
Price over NA	0.96
52-wk price Range	RM5.39 - RM10.9
Beta (against KLCI)	1.05
3-mth Avg Daily Vol	0.92m
3-mth Avg Daily Value	RM5.99m
Major Shareholders (%)	
SKIM ASB	40.8%
EPF	17.3%
PNB	5.7%

**INVESTMENT STATISTICS**

<b>FYE Dec</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16F</b>	<b>FY17F</b>
Revenue (RM'm)	13,951.5	14,932.5	14,419.8	12,453.7	13,234.5
EBIT (RM'm)	1,296.5	1,432.9	134.9	565.7	654.1
Pre-tax Profit (RM'm)	1,501.6	1,621.5	265.6	546.0	625.6
Core net profit (RM'm)	960.4	836.8	338.0	154.2	185.3
FD EPS (sen)	82.2	71.6	28.9	13.2	15.9
EPS growth (%)	0.9	-12.9	-59.6	-54.4	20.2
PER (x)	6.6	7.5	18.7	40.9	34.0
Net Dividend (sen)	44.0	41.0	20.0	4.0	4.8
Net Dividend Yield (%)	8.1	7.6	3.7	0.7	0.9

Source: Company, MIDFR

We expect the 1Q16 earnings to be weakest in the year due to the exceptionally weak TIV and sustained O&G losses from idle rigs, but the quarter should mark bottom in UMW's earnings trends. Having said that, a meaningful recovery is not yet visible given the still weak underlying demand for autos and still tough outlook for UMWOG.

**Volume bounce from 2Q16?** The new Hilux was launched early May and should start trickling into numbers from 2Q16. As a recap, the new Hilux is priced at ~10% higher than the previous generation due to the weak Ringgit. A combination of higher pricing and the initial hype for a new model to drive demand should translate into some improvement in earnings. Moreover, the Hilux is UMW's 2<sup>nd</sup> largest volume contributor after the Vios accounting for 30% of Toyota TIV. Secondly, average USD rates incurred for 2Q16-3Q16 are likely to have eased at an estimated 4.19 (2Q16) and 3.96 (3Q16).

**Implications from our recent TIV cut.** Following the recent cut in our FY16F TIV forecast and our volume projection for UMW, we slash our FY16F/17F earnings by 54%/48%. To recap, our FY16F TIV was trimmed by 6% to 626,633 units (+6%yoy) while for Toyota specifically, FY16F volume forecast was trimmed by 16% to 77,832 units (-17%yoy). Coincidentally, in its results note to analysts, management also trimmed FY16F Toyota-Lexus TIV forecast to 80K units from 87K units. UMW is now close to breakeven and any small changes in variables e.g. currency or volume forecasts will have a large impact on earnings.

**Recommendation:** Since our downgrade back in Nov 2015, UMW's share price has fallen 33%. We think share price at current levels has almost sufficiently priced in the weak FY16F earnings and we think we are close to a bottoming, though this does not necessarily mean a recovery will come any time soon. Maintain NEUTRAL on UMW but trim our TP to RM5.60/share (from RM6.00/share) as we fall back to BV based valuation – pegging UMW at its FY16F BV. Key risk to our valuation are potential impairments, particularly on UMW's O&G assets which are now deeply underutilised.

Key earnings risk: (1) Our forecast assumes the idle rigs will find a home this year albeit at a lower rate – delays in securing contracts will result in further earnings cuts, (2) Weak underlying demand for autos exacerbated by recent price hikes, (3) Still weak Ringgit and low plant utilisation rates which are negative for margins.

**UMWOG debt obligations an overhanging concern.** Concerns still surround UMWOG's ~RM2b debt that is due within the next 12 months given negative cashflows and a depressed operating outlook currently. Despite troubles at UMWOG however, UMW's balance sheet is still strong at 39% net gearing, meaning UMW has ample room to gear up in the case of a cash call at UMWOG- UMW owns 56% of UMWOG.

## EXHIBIT 1: UMW 1Q16 RESULT SUMMARY

31 Dec (RMm)	1Q15	4Q15	1Q16	YoY	QoQ
<b>Revenue</b>	<b>3,240.4</b>	<b>4,160.9</b>	<b>2,199.2</b>	<b>-32.1%</b>	<b>-47.1%</b>
<b>Operating Profit</b>	<b>283.5</b>	<b>(359.7)</b>	<b>17.1</b>	<b>NA</b>	<b>NA</b>
Finance Cost	(32.1)	(41.9)	(43.3)	34.7%	3.4%
Associates	33.4	35.8	22.1	-34.0%	NA
Investment Income	35.3	31.5	25.2	-28.7%	-20.2%
<b>Pretax Profit</b>	<b>320.1</b>	<b>(334.3)</b>	<b>21.1</b>	<b>NA</b>	<b>NA</b>
Taxation	(84.0)	(57.3)	(26.0)		
Minorities	70.9	(105.5)	(21.5)	NA	NA
Net Profit	165.2	(286.0)	16.6	NA	NA
<b>Core net profit</b>	<b>181.9</b>	<b>51.7</b>	<b>(202.4)</b>	<b>-211.3%</b>	<b>-491.8%</b>
EPS (FD, sen)	15.6	4.4	-17.3		
DPS (sen)	0.0	10.0	0.0		
<b>Margins (%):</b>					
Operating	8.7%	-8.6%	0.8%		
Pretax Profit	9.9%	-8.0%	1.0%		
Core Net Profit	5.6%	1.2%	-9.2%		
Tax Rate	26.2%	-17.1%	123.4%		

Source: Company, MIDFR

Segmental Breakdown	1Q15	4Q15	1Q16	YoY	QoQ
Automotive	2,006	3,375.9	1,556.0	-22.4%	-53.9%
Equipment	653	402.9	358.0	-45.2%	-11.1%
Manuf & Eng	171	182.4	145.4	-15.0%	-20.3%
Oil & Gas	312	131.0	87.7	-71.9%	-33.0%
<b>Revenue</b>	<b>3,142</b>	<b>4,092</b>	<b>2,147</b>	<b>-31.7%</b>	<b>-47.5%</b>
Automotive	233.5	247.9	82.7	-64.6%	-66.6%
Equipment	99.3	27.5	39.2	-60.5%	42.5%
Manuf & Eng	1.8	13.4	6.6	NA	-50.8%
Oil & Gas	42.5	(411.3)	(68.4)	NA	NA
<b>Pretax profit</b>	<b>377</b>	<b>(122)</b>	<b>60</b>	<b>-84%</b>	<b>-149%</b>
<b>Pretax margins</b>					
Automotive	11.6%	7.3%	5.3%		
Equipment	15.2%	6.8%	11.0%		
Manuf & Eng	1.1%	7.3%	4.5%		
Oil & Gas	13.6%	-314.1%	-78.0%		
Toyota TIV (units)	16,241	31,663	10,216	-37.1%	-67.7%
Average revenue/car (RM)	123,487	106,618	152,309	23.3%	42.9%

Source: Company, MIDFR

<b>Income Statement</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16F</b>	<b>FY17F</b>
<b>Revenue</b>	<b>13,951.5</b>	<b>14,932.5</b>	<b>14,419.8</b>	<b>12,453.7</b>	<b>13,234.5</b>
Operating expenses	(12,655.0)	(13,499.6)	(14,157.6)	(11,888.1)	(12,580.4)
<b>EBIT</b>	<b>1,296.5</b>	<b>1,567.0</b>	<b>262.1</b>	<b>565.7</b>	<b>654.1</b>
Net interest expense	(18.3)	(85.1)	(126.6)	(155.8)	(165.1)
Associates	157.5	139.6	130.1	136.1	136.7
<b>PBT</b>	<b>1,501.6</b>	<b>1,621.5</b>	<b>265.6</b>	<b>546.0</b>	<b>625.6</b>
Taxation	(351.5)	(408.5)	(259.9)	(102.5)	(122.2)
Minority Interest	(431.3)	(561.0)	44.6	(289.4)	(318.1)
<b>Net profit</b>	<b>718.9</b>	<b>652.0</b>	<b>(38.9)</b>	<b>154.2</b>	<b>185.3</b>
<b>Core net profit</b>	<b>960.4</b>	<b>836.8</b>	<b>338.0</b>	<b>154.2</b>	<b>185.3</b>
Consensus net profit	960.4	836.8	338.0	362.2	456.6
<b>Balance Sheet</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16F</b>	<b>FY17F</b>
<b>Non-current assets</b>	<b>6,075.2</b>	<b>7,923.4</b>	<b>10,511.7</b>	<b>11,011.9</b>	<b>11,490.8</b>
PPE	3,893.3	5,669.7	8,132.7	8,496.7	8,838.9
Investments in associate	1,776.2	1,797.5	1,894.5	2,030.6	2,167.3
Others	405.7	456.3	484.6	484.6	484.6
<b>Current assets</b>	<b>8,731.4</b>	<b>8,596.2</b>	<b>7,568.9</b>	<b>6,773.0</b>	<b>6,785.6</b>
Inventories	1,754.2	1,830.4	1,891.6	1,868.1	1,985.2
Receivables	1,855.1	1,238.3	1,273.3	1,743.5	1,985.2
Others	2,578.4	2,156.8	1,675.7	1,210.1	1,210.1
Cash & equivalent	2,543.8	3,370.7	2,728.3	1,951.3	1,605.1
<b>TOTAL ASSETS</b>	<b>14,806.7</b>	<b>16,519.7</b>	<b>18,080.6</b>	<b>17,784.9</b>	<b>18,276.4</b>
Share capital	584.1	584.1	584.1	584.1	584.1
Minority Interest	2,613.9	2,852.6	2,827.1	3,084.9	3,365.0
Reserves	5,778.6	5,996.3	5,812.7	5,921.4	6,051.1
<b>TOTAL EQUITY</b>	<b>8,976.6</b>	<b>9,433.1</b>	<b>9,223.9</b>	<b>9,590.4</b>	<b>10,000.2</b>
<b>Non-current liabilities</b>	<b>1,774.7</b>	<b>2,017.0</b>	<b>3,165.1</b>	<b>3,115.1</b>	<b>3,065.1</b>
Long-term borrowings	1,602.2	1,803.0	2,782.5	2,732.5	2,682.5
Deferred tax liabilities	34.2	27.4	34.1	34.1	34.1
Others	138.3	186.6	348.5	348.5	348.5
<b>Current liabilities</b>	<b>4,055.4</b>	<b>5,069.6</b>	<b>5,691.6</b>	<b>5,079.5</b>	<b>5,211.1</b>
Short-term borrowings	1,464.3	2,292.6	3,159.1	2,859.1	2,859.1
Payables	2,070.1	2,217.0	2,230.3	1,998.0	2,123.3
Others	520.9	560.0	302.2	222.3	228.7
<b>TOTAL LIABILITIES</b>	<b>5,830.0</b>	<b>7,086.6</b>	<b>8,856.7</b>	<b>8,194.5</b>	<b>8,276.2</b>

<b>Cash Flow Statement</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16F</b>	<b>FY17F</b>
<b>Operating activities</b>					
PBT	1,501.6	1,621.5	265.6	546.0	625.6
Depreciation & Amortization	325.3	378.7	765.5	488.0	509.8
Chgs in working capital	(423.7)	(149.1)	(134.2)	(213.7)	(227.1)
Interest expense	18.3	(48.9)	(120.8)	(155.8)	(165.1)
Tax paid	(374.4)	(418.3)	(275.5)	(102.5)	(122.2)
Others	(152.5)	(18.9)	(125.3)	19.7	28.4
<b>CF from Operations</b>	<b>894.6</b>	<b>1,364.9</b>	<b>375.3</b>	<b>581.6</b>	<b>649.4</b>
<b>Investing activities</b>					
Capex	(999.9)	(2,185.5)	(2,168.8)	(1,000.0)	(1,000.0)
Others	888.7	1,870.6	264.6	148.0	148.0
<b>CF from Investments</b>	<b>(111.2)</b>	<b>(315.0)</b>	<b>(1,904.2)</b>	<b>(852.0)</b>	<b>(852.0)</b>
<b>Financing activities</b>					
Dividends paid	(1,050.3)	(947.2)	(806.1)	(77.8)	(93.5)
Net proceeds in borrowings	240.7	1,150.7	1,692.3	(350.0)	(50.0)
Others	66.9	-	-	-	-
<b>CF from Financing</b>	<b>(742.7)</b>	<b>203.6</b>	<b>886.3</b>	<b>(427.8)</b>	<b>(143.5)</b>
<b>Net changes in cash</b>	<b>40.7</b>	<b>1,253.5</b>	<b>(642.6)</b>	<b>(698.2)</b>	<b>(346.2)</b>
Beginning cash	1,547.7	1,492.3	3,276.6	2,649.5	1,951.3
Overdrafts & Deposits	-	-	15.6	-	-
<b>Ending cash</b>	<b>1,588.3</b>	<b>2,745.8</b>	<b>2,649.5</b>	<b>1,951.3</b>	<b>1,605.1</b>
<b>Ratios</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16F</b>	<b>FY17F</b>
Revenue growth	0.6%	7.0%	-3.4%	-13.6%	6.3%
EBIT growth	-32.0%	10.5%	-90.6%	>100%	15.6%
Core net profit growth	-24.5%	-12.9%	-59.6%	-54.4%	20.2%
PBT margin	10.8%	10.9%	1.8%	4.4%	4.7%
Core net profit margin	5.2%	5.6%	2.3%	1.2%	1.4%
ROE	12.9%	10.1%	-0.6%	2.4%	2.8%
ROA	9.7%	9.1%	0.8%	3.2%	3.6%
Net gearing (%)	5.8%	7.7%	34.8%	38.0%	39.4%
Book value/share (RM)	5.45	5.63	5.48	5.57	5.68
PBV (x)	1.28	1.24	1.27	1.25	1.23
EV/EBITDA (x)	4.2	3.9	10.6	9.4	8.8

## DAILY PRICE CHART



Source: Bloomberg, MIDFR

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### MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

#### STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

#### SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.