

25 May 2016

Consumer Cyclical | Auto & Autoparts

UMW

Sell (Maintained)

The Long And Winding Road

2016 is likely to be another difficult year for UMW. With consumer sentiment remaining tepid, coupled with slow upstream oil & gas activity, its automotive and oil & gas businesses should remain under pressure. Although we are positive on its longer term strategic initiatives, there are few re-rating catalysts for the stock in the near term. The counter is likely to be dropped from the FBM KLCI at the upcoming review. Reiterate SELL, with a revised MYR 4.00 TP (from MYR5.00, 26% downside).

Tough operating environment persists. In our view, while Toyota is expected to refresh its product pipeline this year, sales are likely to remain dampened. This is given the slower-than-expected recovery in consumer spending and cutthroat market. We anticipate profit margins to remain compressed, mainly attributed to the weak MYR and higher costs from aggressive marketing activities. UMW Oil & Gas Corp (UMWOG) (UMWOG MK, NR) is to continue to endure low utilisation rate for its drilling rigs, as some of its existing charters are expected to expire this year amidst soft demand for drilling services. We cannot rule out further impairments for UMW's oil & gas assets.

Long-term growth from strategic initiatives. It was recently reported that UMW intends to build a new MYR1.1bn plant in Malaysia with a capacity for 50,000 vehicles pa. The group also requires MYR750m for its new aerospace venture. We believe that UMW is able to fund these projects, which are likely to have a gestation period of 2-3 years.

Risks. After updating our assumptions, we tweak our 2016F-2018F earnings by 26.1%/16%/11.6% respectively. Upside risks to our call and TP include a stronger MYR, faster recovery in consumer spending, higher crude oil prices, and turnarounds at both its core and non-core oil & gas businesses.

1Q16 earnings – below expectations

(MYRm)	1Q16	4Q15	QoQ (%)	1Q15	YoY (%)	Comments
Revenue	2,199	4,161	(47.1)	3,240	(32.1)	Revenue was lower mainly due to weak auto sales and lower rig utilisation
EBIT	17	(360)	104.8	284	(94.0)	
EBIT (%)	0.8%	-8.6%		8.7%		
NI	17	(286)	105.8	165	(90.0)	Net income was depressed by the weak MYR and a net loss from UMWOG
NI (%)	0.8%	-6.9%		5.1%		

Source: Company data, RHB

Maintain SELL. We maintain our SELL call on the stock with a revised SOP-derived TP of MYR4.00 (from MYR5.00), which implies 0.74x FY16 P/BV. While the stock has been trading above its book value for the past 10 years, we believe that the implied P/BV is justified as its valuation multiple remains relatively higher to its peers while its lowest historical trough was 1998's 0.4x. Based on our house view, the stock is likely to be dropped from the FBM KLCI component list at the upcoming review.

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	14,959	14,420	10,538	12,001	12,860
Reported net profit (MYRm)	658	(39)	303	404	463
Recurring net profit (MYRm)	802	147	303	404	463
Recurring net profit growth (%)	(6.0)	(81.7)	106.6	33.2	14.7
Recurring EPS (MYR)	0.69	0.13	0.26	0.35	0.40
DPS (MYR)	0.41	0.20	0.18	0.24	0.28
Recurring P/E (x)	7.9	43.0	20.8	15.6	13.6
P/B (x)	0.96	0.99	1.00	1.02	1.06
P/CF (x)	6.0	10.7	7.4	10.4	4.5
Dividend Yield (%)	7.6	3.7	3.4	4.5	5.1
EV/EBITDA (x)	4.5	18.5	12.1	10.4	9.1
Return on average equity (%)	10.2	(0.6)	4.8	6.5	7.7
Net debt to equity (%)	7.6	34.8	32.0	43.1	47.1
Our vs consensus EPS (adjusted) (%)			(15.8)	(11.1)	(7.2)

Source: Company data, RHB

Target Price:	MYR4.00
Price:	MYR5.40
Market Cap:	USD1,531m
Bloomberg Ticker:	UMWH MK

Share Data

Avg Daily Turnover (MYR/USD)	5.90m/1.46m
52-wk Price low/high (MYR)	5.40 - 10.7
Free Float (%)	35
Shares outstanding (m)	1,168
Estimated Return	-26%

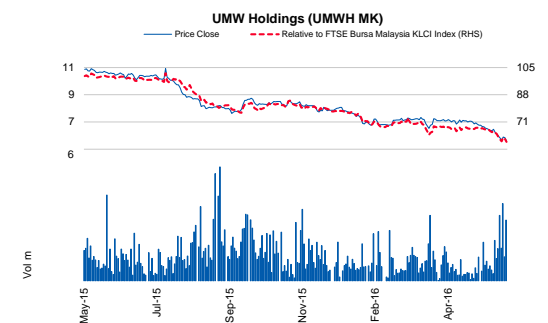
Shareholders (%)

Permodalan Nasional funds	51.6
Employees Provident Fund	17.6

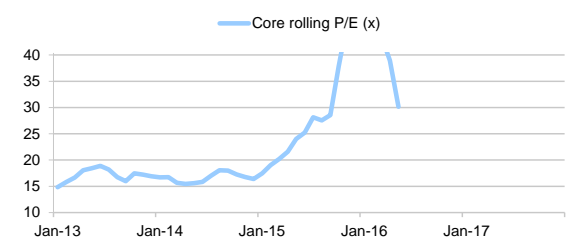
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(31.4)	(21.3)	(21.7)	(33.7)	(49.4)
Relative	(27.5)	(15.9)	(19.4)	(30.6)	(40.3)

Source: Bloomberg



Source: Bloomberg



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The Long And Winding Road

Figure 1: UMW's earnings review

FYE Dec (MYRm)	1Q15	4Q15	1Q16	QoQ (%)	YoY (%)	Comments
Revenue	3,240.4	4,160.9	2,199.2	(47.1)	(32.1)	Revenue was 47.1% QoQ and 32.1% YoY lower due to weak vehicle sales. This was attributed to poor consumer sentiment and reduced time charter rates.
EBIT	283.5	(359.7)	17.1	104.8	(94.0)	EBIT decreased 94% YoY. This was attributed to higher cost of sales due to the weak MYR.
<i>EBIT margin (%)</i>	8.7	(8.6)	0.8			
Finance costs	(32.2)	(41.9)	(43.3)	3.4	34.5	
Associates	33.4	35.8	22.1	(38.3)	(34.0)	Associate contributions were hit by Perodua's weaker sales, in line with the overall declined in auto sales.
Investment income	35.3	31.5	25.2	(20.2)	(28.7)	
PBT	320.0	(334.2)	21.1	106.3	(93.4)	Overall PBT was dragged by a PBT loss at its oil & gas division. This was due to reduced charter rates on the back of soft demand for drilling services.
<i>PBT margin (%)</i>	9.9	(8.0)	1.0			
Tax	(84.0)	(57.3)	(26.0)	(54.6)	(69.0)	
<i>Effective tax rate (%)</i>	(26.3)	17.1	(123.4)			
MI	(70.9)	105.5	21.5	(79.6)	(130.4)	
Net Profit	165.2	(286.0)	16.6	105.8	(90.0)	
<i>Net Margin (%)</i>	5.1	(6.9)	0.8			

Source: Company data, RHB

Figure 2: UMW's earnings review – segmental breakdown

FYE Dec (MYRm)	1Q15	4Q15	1Q16	QoQ (%)	YoY (%)	Comments
Automotive	2,005.5	3,375.9	1,556.0	(53.9)	(22.4)	Revenue declined due to weaker auto sales.
Oil & gas	312.5	131.0	87.7	(33.0)	(71.9)	
Equipment	653.0	402.9	358.0	(11.1)	(45.2)	Revenue decrease was mainly caused by weak market sentiment in the construction and mining sectors.
Manufacturing & engineering	171.1	182.4	145.4	(20.3)	(15.0)	
Others	98.3	68.8	52.1	(24.3)	(47.0)	Weaker revenue attributed to lower demand for lubricants and auto components products.
Revenue	3,240.4	4,160.9	2,199.2	(47.1)	(32.1)	
Automotive	233.5	247.9	82.7	(66.6)	(64.6)	Drop in PBT was largely due to higher cost of sales as a result of the weak MYR.
Oil & gas	42.5	(411.3)	(68.4)	83.4	(261.1)	
Equipment	99.3	27.5	39.2	42.5	(60.5)	
Manufacturing & engineering	1.8	13.4	6.6	(50.8)	265.6	PBT improving 265.6% YoY was mainly attributed to the disposal of loss-making automotive components companies in India in Nov 2015.
Others	(57.1)	(211.8)	(39.1)	81.5	31.5	
PBT	320.0	(334.3)	21.1	(106.3)	(93.4)	
PBT Margins						
Automotive	11.6	7.3	5.3			
Oil & gas	13.6	(314.1)	(78.0)			
Equipment	15.2	6.8	11.0			
Manufacturing & engineering	1.1	7.3	4.5			
Others	(58.1)	(307.7)	(75.0)			
	9.9	(8.0)	1.0			
Automotive	116.7	124.5	55.5	(55.4)	(52.5)	
Oil & Gas	17.9	(228.0)	(36.2)	(84.1)	(302.1)	
Equipment	78.7	26.4	30.2	14.5	(61.7)	
Manufacturing & engineering	1.3	8.5	1.1	(86.5)	(12.6)	
Others	(49.5)	(217.4)	(34.0)	(84.4)	(31.3)	
NP	165.2	(286.0)	16.6	105.8	(90.0)	Net profit was 105.8% higher QoQ due to a MYR337.7m in impairment charges in 4Q15.
NP Margins						
Automotive	5.8	3.7	3.6			
Oil & Gas	5.7	(174.1)	(41.3)			
Equipment	12.1	6.5	8.4			
Manufacturing & engineering	0.8	4.6	0.8			
Others	(50.4)	(315.9)	(65.3)			
	5.1	(6.9)	0.8			

Source: Company data, RHB

Figure 3: Summary of UMW's vehicle sales

FYE Dec (units)	1Q15	4Q15	1Q16	QoQ (%)	YoY (%)
Toyota	16,603	32,398	10,488	(67.6)	(36.8)
- Passenger	11,084	23,372	7,316	(68.7)	(34.0)
- Commercial	5,519	9,026	3,172	(64.9)	(42.5)
Perodua	57,153	55,780	47,181	(15.4)	(17.4)
- Passenger	57,153	55,780	47,181	(15.4)	(17.4)
- Commercial	0	0	0	0.0	0.0
Total	73,756	74,436	57,669	(22.5)	(21.8)

Source: Malaysian Automotive Association (MAA)

Figure 4: Forecast assumptions

FYE Dec	2014	2015	2016F	2017F	2018F
Toyota / Lexus (units)	103,636	95,861	75,000	85,000	90,000
Perodua (units)	195,579	213,307	195,000	205,000	215,000
Forex (JPY/MYR)*	3.15	3.25	3.70	3.60	3.60
Forex (USD/MYR)*	3.25	3.90	4.00	3.80	3.80

*Average rate

Source: RHB

Figure 5: SOP valuation

	P/E (x)	Valuation (MYR)	Stake (%)	Discount (%)	Per UMW share (MYR)
UMWOG		MYR 0.90	55.15	10	0.83
Other businesses	11.0				3.14
					3.96

Source: RHB

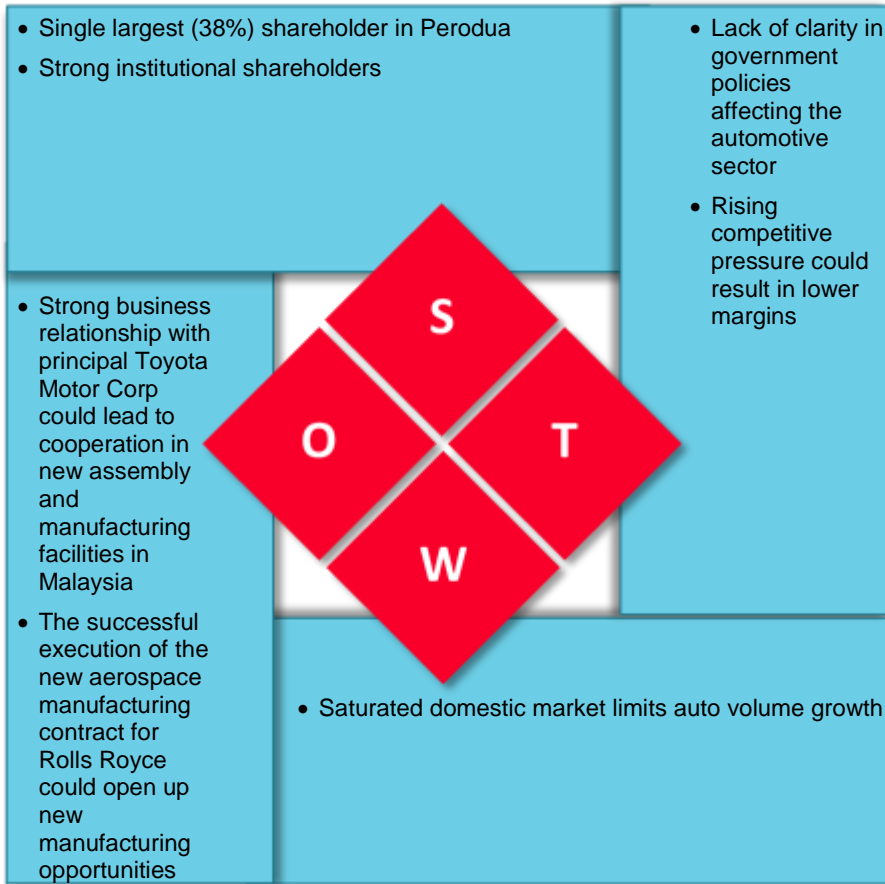
Financial Exhibits

Financial model updated on: 2016-05-24.

Asia	Financial summary	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Malaysia	Recurring EPS (MYR)	0.69	0.13	0.26	0.35	0.40
Consumer Cyclical	EPS (MYR)	0.56	(0.03)	0.26	0.35	0.40
UMW	DPS (MYR)	0.41	0.20	0.18	0.24	0.28
Bloomberg UMW MK	BVPS (MYR)	5.64	5.48	5.39	5.27	5.09
Sell	Weighted avg adjusted shares (m)	1,168	1,168	1,168	1,168	1,168
Valuation basis	Valuation metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
SOP valuation.	Recurring P/E (x)	7.9	43.0	20.8	15.6	13.6
Key drivers	P/E (x)	9.6	na	20.8	15.6	13.6
i. Introduction of attractive new car models;	P/B (x)	0.96	0.99	1.00	1.02	1.06
ii. Turnaround at various legacy non-core oil & gas businesses;	FCF Yield (%)	(16.2)	(24.3)	(5.5)	(9.4)	3.3
iii. Long-term growth potential from the aerospace business.	Dividend Yield (%)	7.6	3.7	3.4	4.5	5.1
Key risks	EV/EBITDA (x)	4.5	18.5	12.1	10.4	9.1
i. Stronger MYR;	EV/EBIT (x)	5.7	77.1	30.4	19.2	14.8
ii. Better-than-expected economic growth;	Income statement (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
iii. Recovery in crude oil prices.	Total turnover	14,959	14,420	10,538	12,001	12,860
Company Profile	Gross profit	4,114	3,965	2,898	3,300	3,537
UMW is the largest company in the automotive sector and is 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 Corp (UMWOG).	EBITDA	1,806	563	821	1,042	1,206
	Depreciation and amortisation	(379)	(428)	(494)	(481)	(462)
	Operating profit	1,427	135	327	561	744
	Net interest	55	1	(44)	(63)	(88)
	Income from associates & JVs	140	130	81	99	118
	Pre-tax profit	1,621	266	365	596	774
	Taxation	(409)	(260)	(98)	(161)	(209)
	Minority interests	(554)	(45)	37	(32)	(102)
	Recurring net profit	802	147	303	404	463
	Cash flow (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Change in working capital	(205)	241	269	(142)	518
	Cash flow from operations	1,059	591	850	609	1,407
	Capex	(2,080)	(2,125)	(1,200)	(1,200)	(1,200)
	Cash flow from investing activities	(723)	(1,904)	(143)	(1,018)	(1,043)
	Dividends paid	(514)	(479)	(234)	(212)	(283)
	Cash flow from financing activities	(354)	407	(1,518)	(759)	(957)
	Balance sheet (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Total cash and equivalents	3,376	2,728	2,151	1,194	883
	Tangible fixed assets	5,646	8,133	8,839	9,557	10,295
	Intangible assets	38	38	38	38	38
	Total investments	1,878	1,975	2,057	2,156	2,273
	Total other assets	344	365	365	365	365
	Total assets	16,439	18,081	16,318	16,413	16,604
	Short-term debt	2,177	3,159	3,159	3,159	3,159
	Other liabilities	122	279	279	279	279
	Total liabilities	6,997	8,857	7,230	7,436	7,737
	Shareholders' equity	6,590	6,397	6,298	6,155	5,943
	Minority interests	2,853	2,827	2,790	2,821	2,923
	Total equity	9,443	9,224	9,088	8,977	8,867
	Net debt	715	3,213	2,909	3,865	4,177
	Total liabilities & equity	16,439	18,081	16,318	16,413	16,604
	Key metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Revenue growth (%)	7.2	(3.6)	(26.9)	13.9	7.2
	Recurrent EPS growth (%)	(6.0)	(81.7)	106.6	33.2	14.7
	Gross margin (%)	27.5	27.5	27.5	27.5	27.5
	Operating EBITDA margin (%)	12.1	3.9	7.8	8.7	9.4
	Net profit margin (%)	4.4	(0.3)	2.9	3.4	3.6
	Dividend payout ratio (%)	72.8	(600.3)	70.0	70.0	70.0
	Capex/sales (%)	13.9	14.7	11.4	10.0	9.3
	Interest cover (x)	17.4	1.1	2.3	4.3	5.7

Source: Company data, RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2016-02-26	Sell	5.0	7.0
2016-01-17	Sell	5.0	7.3
2015-11-27	Sell	5.0	8.0
2015-10-06	Sell	5.0	7.6
2015-08-27	Sell	5.4	8.5
2015-05-26	Sell	8.7	10.7
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

Source: RHB, Bloomberg

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

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