

UOBKH HIGHLIGHTS

UMW Holdings (UMWH MK/SELL/RM5.85/Target: RM4.70)

2Q16: Dragged Down By Its Oil & Gas Business

Year to 31 Dec	2Q16 (RMm)	qoq % chg	yoy % chg	1H16 (RMm)	yoy % chg	Year	EPS (sen)	Revision (%)	PE (x)	P/B (x)
Revenue	2,846.8	29.4	(18.3)	5,046.0	(25.0)	2016F	(1.2)	(114.1)	na	1.1
-Auto	2,177.1	39.9	(20.3)	3,733.1	(21.2)	2017F	5.9	(53.1)	99.2	1.1
-Equipment	351.2	(1.9)	(0.7)	709.1	(29.6)	2018F	16.1	(31.8)	36.4	1.0
-Mfg & Eng	157.0	7.9	(5.1)	302.4	(10.1)					
-Oil & gas	130.0	48.3	(29.1)	217.7	(56.1)					
-Others	31.5	(39.4)	(37.2)	83.6	(43.7)					
EBIT	41.1	139.5	(76.7)	58.2	(87.3)					
Associates	26.5	20.2	(10.2)	48.6	(22.8)					
PBT	44.8	112.6	(78.4)	65.9	(87.5)					
-Auto	133.3	61.1	(49.4)	216.0	(56.5)					
-Equipment	43.3	10.4	28.7	82.6	(37.9)					
-Mfg & Eng	10.9	65.5	2627.0	17.5	694.3					
-Oil & gas	(64.0)	(6.5)	(900.5)	(132.4)	(362.4)					
-Others	(78.7)	101.5	(19.5)	(117.8)	(23.9)					
Net profit	(12.1)	(173.1)	(117.7)	4.5	(98.1)					
Core Net profit	(14.9)	(187.8)	(123.7)	2.1	(99.1)					
Toyota sales (units)	17,033	66.7	(24.5)	27,249	(29.8)					
Perodua sales (units)	50,189	6.4	(2.3)	97,370	(10.3)					

Source: UMW Holdings, UOB Kay Hian

WHAT'S NEW

- **UMW Holdings (UMW)'s 2Q16 core net loss of RM14.9m was below our and consensus expectations**, with 1H16 results accounting for 2% and 1% of 2016 earnings forecasts respectively. 2Q16 underperformance largely stemmed from: a) a RM78.7m loss before tax in its others segment, which consists of oil and gas (O&G)-related companies that are not part of its 55.7%-owned UMW O&G, and b) higher-than-expected tax of RM48.5m (2Q15: RM74.3m tax against a PBT of RM207.6m). No dividend was declared ytd (1H15: 10 sen) given that the company may be under the strain of cash crunch.
- **Strong qoq recovery in automobile segment.** 2Q16 PBT declined 49.4% yoy due to weak sales volume, coupled with the weak ringgit that eroded its margins. However, we note a strong qoq recovery in the segment in tandem with its sales (see table) due to: a) higher sales volume of Hilux which was launched in early May, and b) aggressive promotion and discounts. We note that Toyota may fall short of its 2016 sales forecasts of 70,000 units (previously 80,000 units) but we believe Perodua will be able to achieve its 2016 targeted sales forecasts of 216,000 units given the successful launch of its first sedan – Bezza – in early July 16.
- No improvement in sight for its O&G business. UMW O&G recorded a pre-tax loss of RM64m (2Q15: RM8m PBT, 1Q16: loss before tax of RM68.4m) against the backdrop of: a) lower charter rates, and b) high operating expenses from its uncontracted rigs. Currently, only 2 out of its 8 rigs are contracted. We also note that the contracted rigs are on a “pay per use” basis. Meanwhile, its non-core O&G business suffered as well against the backdrop of: a) low oil price environment, b) lacklustre demand for drilling rigs, pipes and related services, as well as c) slowdown in new pipeline projects in China.

COMMENT

- **UMW to be dragged down by its O&G business in the near to mid-term.** Given that the ringgit remains weak against the greenback and that competition continues to be stiff amid soft consumer sentiment, outlook for auto sector continues to be weak. However, we reckon that domestic auto sector has probably reached the bottom. Meanwhile, we still do not see light at the end of the tunnel yet for its 55.7%-owned UMW O&G. In the current oversupplied rig market, charter rates will remain low in the near to mid-term until a strong and sustained recovery in oil price is seen. Current charter rates in the Southeast Asian region stood at US\$70,000-90,000 per day and we gather that at current rates, UMW O&G needs 5-6 working rigs to achieve net profit breakeven.
- We cut our 2016-18 earnings forecasts by 114%/53%/32% to -RM14m/RM69m/RM188m respectively after incorporating losses from its non-core O&G-related ventures and adjusting tax rate assumption. We make no changes to our projections from auto, equipment, manufacturing and engineering segments, as well as UMW O&G. In addition, we also cut our 2016-18F DPS assumptions to nil/3 sen/8 sen respectively, which represent yields of 0-1.1% for 2016-18.
- **Maintain SELL and SOTP-based target price of RM4.70**, implying a 0.9x 2017F P/B. We do not see any re-rating catalysts in the near-to-midterm as all its major divisions are operating in extremely challenging environments.

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