



AmInvestment Bank

Company report

UMW HOLDINGS

(UMWH MK EQUITY, UMWS.KL)

20 Jan 2017

Exit from O&G

HOLD

(Maintained)

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Rationale for report: Company update

Price	RM4.62
Fair Value	RM4.60
52-week High/Low	RM7.37/RM4.43

Key Changes

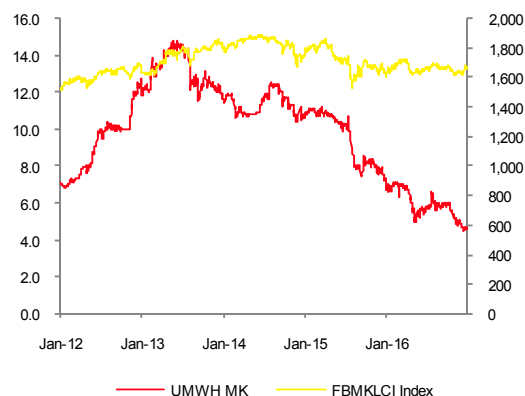
Fair value	↔
EPS	↔

YE to Dec	FY15	FY16F	FY17F	FY18F
Revenue (RM mil)	14,441.6	10,963.5	12,193.4	13,111.1
Core net profit (RM mil)	216.6	(143.4)	82.9	105.4
FD Core EPS (sen)	18.5	(12.3)	7.1	9.0
FD Core EPS growth (%)	(74.3)	(166.2)	(157.8)	27.2
Consensus Net Profit (RM mil)	-	(38.1)	195.1	244.5
DPS (sen)	41.0	(6.1)	3.5	4.5
PE (x)	24.9	nm	65.1	51.2
EV/EBITDA (x)	13.4	nm	19.3	16.2
Div yield (%)	8.9	(1.3)	0.8	1.0
ROE (%)	(0.4)	(2.2)	1.3	1.6
Net Gearing (%)	49.8	44.5	65.0	82.8

Stock and Financial Data

Shares Outstanding (million)	1,168.3
Market Cap (RMmil)	5,397.6
Book Value (RM/share)	5.64
P/BV (x)	0.8
ROE (%)	(0.4)
Net Gearing (%)	49.8
Major Shareholders	Skim ASB (41.7%) EPF (16.0%)
Free Float	32.6
Avg Daily Value (RMmil)	2.9

Price performance	3mth	6mth	12mth
Absolute (%)	(21.7)	(19.8)	(34.5)
Relative (%)	(21.6)	(19.6)	(35.9)



Investment Highlights

- We maintain our HOLD call and FV of RM4.60 for UMW. UMW has mapped a plan to exit the O&G sector entirely: (1) it will de-merge from UMW O&G (UMWOG) by distribution in specie of its 55.7% stake to existing UMW shareholders. (2) it will make further impairments on the non-listed O&G assets that have been loss-making.
- UMW said this will allow it to focus on the areas of auto, equipment and manufacturing & engineering. The auto segment has contributed 70-80% of revenue and taking the O&G segment out will allow UMW to focus on reforming the former.
- In terms of the impact to earnings, we estimate UMW could see an improvement of at least 1.2 times to its net profit going forward, as our projected losses before tax of -RM371mil and -RM173mil are removed from UMW's income statement for FY17F-FY18F. In terms of topline, we project there could be an erosion of 1-6% given the contribution of O&G (which last shrunk to 3% from 6-7% historically).
- The move will also lower its borrowings and net gearing. UMW will take the RM2.6bil in borrowings under UMWOG off its books, reducing its total borrowings to RM2.7bil from RM5.3bil and net gearing to 10% from 51% as of end-Sept 2016. It could also see a reduction by about half in interests costs of RM40mil/quarter.
- For existing UMW shareholders, they would have the option to exit from the O&G side following the completion of this exercise by end-2Q. As mentioned by UMW management, investors will be able to manage their exposures to the O&G and non-O&G sides independently.
- For the rest, we believe the share price could appreciate on the view that this presents an opportunity to enter into UMWOG. We note the gap between the targeted completion of the separation from UMWOG (end-2Q) and the restructuring of UMWOG (end-3Q).
- Following the demerger, there will be more room for (and pressure on) UMW to shape up its auto business. The focus next should be on what UMW can do to lift Toyota sales, in what looks to be another grim year for the sector. Toyota was the worst performer last year with a 32% YoY drop in sales.

TWO-FOLD PLAN FOR EXIT FROM O&G

□ *The plan for UMW Holdings*

UMW Holdings is currently the biggest shareholder in UMWOG with a 55.7% stake. UMW is going to distribute this stake in UMWOG to existing shareholders of UMW in specie. UMWOG will no longer be a unit of UMW, and the existing stakes of UMW shareholders in UMWOG will be enlarged: PNB & funds will hold 45.4% of UMWOG from 13.1% before, EPF 13.8% from 4.7%, and others 38.1% from 25.7%.

UMW will undertake a bonus issue of 1.2bil redeemable preference shares (RPS) on the basis of 1.03 RPS for every existing UMW share. These shares will be redeemed with the 1.2bil UMWOG shares currently held by UMW. This exercise will rely on UMW's share premium account rather than its retained earnings.

The target completion date for this is by end-2QFY17.

□ *Disposal of "other" O&G assets*

This part will mark a complete exit by UMW from the sector. Assets of this segment comprise Oil Country Tubular Goods (OCTG) and pipe manufacturing assets in China, India and Indonesia; land rig assets in Oman and India; oil field services and international pipe trading companies.

There is no breakdown available for the contributions and value of these assets, but they have been a drag on earnings: registering a total of –RM99mil in losses in 9MFY16, and –RM456mil in 2015.

It has been a long journey since UMW resolved to dispose of these assets five years ago, and the company warned that it will have to make further impairments on their carrying values with the quantum to be finalized by the end of Feb

RATIONALE FOR THE MOVE

UMW intends To focus on its core areas of auto, equipment and manufacturing & engineering. The auto segment has always been the main business for UMW and responsible for about 70-80% of revenue.

UMW via this segment has a 51% stake in UMW Toyota Motor Sdn Bhd (which sells Lexus and Toyota) and a 38% stake in Perodua. Both the auto and O&G segments have decline tremendously on unfavorable macro factors, taking O&G out of the picture would allow UMW to focus on reforming the auto side.

THE IMPACT TO UMW

□ *Lower debt levels*

UMW will take the RM2.1bil in short term borrowings under UMWOG off its books, reducing its total borrowings to RM3.2bil from RM5.3bil and net gearing to 18% from 51% as of end-Sept 2016. This will also serve to reduce the high interest costs of above RM40mil/quarter UMW has been paying

□ *Earnings improvement*

We estimate UMW could see an improvement of at least 1.2 times to its net profit going forward, as our projected losses before tax of –RM371mil and –RM173mil are removed from UMW's income statement for FY17F-FY18F. In terms of topline, we project there could be an erosion of 1-6% given the contribution of O&G (which last shrunk to 3% from 6-7% historically).

IMPACT TO SHAREHOLDERS

Following the completion of the exercise, existing shareholders would have the option to exit from the O&G side. As put by UMW, shareholders will be able to manage their exposures (to the auto and O&G sides) independently.

For the rest, we believe the share price could appreciate on the view that this presents an opportunity to enter into UMWOG (if the prospects of the unit are seen positively, following the restructuring).

We note the gap between the targeted completion of the separation from UMWOG (end-2Q) and the restructuring of UMWOG (end-3Q).

WHAT'S NEXT?

Following the demerger of UMWOG, there will be more room for (and pressure on) UMW to shape up its auto business. This segment is facing the dual problem of poor sales and poor profitability. For 9MFY16, Auto topline fell 18% YoY and net profit fell 34% YoY. This is on account of Toyota sales dropping 28% during the period. Due partly to the forex impact, net margin for the segment net margin for the segment has stayed low at 3.4% vs. 4.0-6.3% historically.

The focus next should be on what UMW can do to lift Toyota sales, in what looks to be another grim year for the sector. Toyota was the worst performer last year with a 32% YoY drop in sales.

EXHIBIT 1: PB BAND CHART

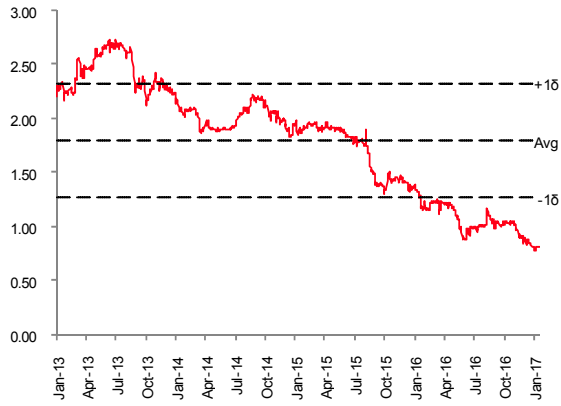


EXHIBIT 2: PE BAND CHART

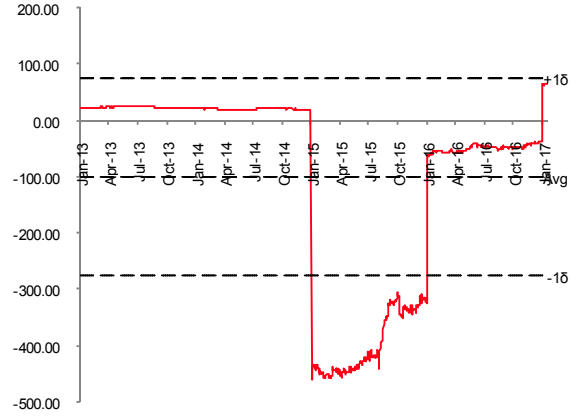


EXHIBIT 3: FINANCIAL DATA

Income Statement (RMmil, YE 31 Dec)	FY14	FY15	FY16F	FY17F	FY18F
Revenue	14,932.5	14,441.6	10,963.5	12,193.4	13,111.1
EBITDA	1,811.7	646.3	(126.6)	501.7	670.2
Depreciation/Amortisation	(378.7)	(502.0)	(570.9)	(638.9)	(706.9)
Operating income (EBIT)	1,432.9	144.4	(697.5)	(137.2)	(36.7)
Other income & associates	139.6	134.4	196.0	212.1	228.7
Net interest	48.9	(0.4)	(1.5)	(17.9)	(90.7)
Exceptional items	-	-	-	-	-
Pretax profit	1,621.5	278.4	(503.0)	57.0	101.2
Taxation	(408.5)	(267.5)	122.2	(13.9)	(24.6)
Minorities/pref dividends	(561.0)	(39.4)	237.4	39.7	28.8
Net profit	652.0	(28.4)	(143.4)	82.9	105.4
Core net profit	842.5	216.6	(143.4)	82.9	105.4
Balance Sheet (RMmil, YE 31 Dec)	FY14	FY15	FY16F	FY17F	FY18F
Fixed assets	5,669.7	8,102.8	9,142.1	10,121.3	11,040.6
Intangible assets	25.6	25.2	25.2	25.2	25.2
Other long-term assets	2,353.3	2,429.9	318.2	(1,438.8)	(3,351.6)
Total non-current assets	8,048.5	10,557.9	9,485.4	8,707.7	7,714.2
Cash & equivalent	3,370.7	2,734.1	4,254.8	1,762.8	(147.2)
Stock	1,830.4	1,890.0	1,434.8	1,595.7	1,715.8
Trade debtors	2,078.5	1,833.4	1,391.8	1,548.0	1,664.5
Other current assets	1,191.5	1,209.9	1,200.5	1,200.5	1,200.5
Total current assets	8,471.1	7,667.4	8,281.9	6,107.0	4,433.6
Trade creditors	2,217.0	2,241.2	1,701.4	1,892.3	2,034.7
Short-term borrowings	2,386.7	3,725.0	4,064.5	3,826.7	3,731.4
Other current liabilities	465.8	371.8	46.7	91.5	95.1
Total current liabilities	5,069.6	6,338.0	5,812.7	5,810.6	5,861.2
Long-term borrowings	1,803.0	2,289.8	3,119.3	2,216.6	1,575.2
Other long-term liabilities	214.0	213.7	83.5	83.5	83.5
Total long-term liabilities	2,017.0	2,503.4	3,202.8	2,300.1	1,658.7
Shareholders' funds	6,580.5	6,584.4	6,584.4	6,584.4	6,584.5
Minority interests	2,852.6	2,799.4	2,848.0	2,819.7	2,783.8
BV/share (RM)	5.63	5.64	5.64	5.64	5.64
Cash Flow (RMmil, YE 31 Dec)	FY14	FY15	FY16F	FY17F	FY18F
Pretax profit	1,621.5	278.4	(503.0)	57.0	101.2
Depreciation/Amortisation	378.7	502.0	570.9	638.9	706.9
Net change in working capital	(149.1)	67.9	231.6	(81.4)	(90.7)
Others	(486.1)	100.7	(73.8)	(226.0)	(253.3)
Cash flow from operations	1,364.9	949.0	225.7	388.5	464.2
Capital expenditure	(2,185.5)	(2,280.4)	(1,500.0)	(1,500.0)	(1,500.0)
Net investments & sale of fixed assets	2,250.8	1,180.0	-	-	-
Others	(380.3)	(639.9)	1,300.0	1,300.0	1,200.0
Cash flow from investing	(315.0)	(1,740.3)	(200.0)	(200.0)	(300.0)
Debt raised/(repaid)	1,151.6	1,323.4	-	-	-
Equity raised/(repaid)	-	-	-	-	-
Dividends paid	(947.2)	(805.2)	120.5	(69.6)	(88.6)
Others	(0.9)	(0.9)	-	-	-
Cash flow from financing	203.6	517.3	1,608.1	(2,680.5)	(2,074.1)
Net cash flow	1,253.5	(274.0)	1,633.8	(2,492.0)	(1,909.9)
Net cash/(debt) b/f	1,565.1	2,830.4	2,620.9	4,254.8	1,762.8
Net cash/(debt) c/f	2,825.0	2,620.9	4,254.8	1,762.8	(147.2)
Key Ratios (YE 31 Dec)	FY14	FY15	FY16F	FY17F	FY18F
Revenue growth (%)	7.0	(3.3)	(24.1)	11.2	7.5
EBITDA growth (%)	11.7	(64.3)	(119.6)	(496.4)	33.6
Pretax margin (%)	10.9	1.9	(4.6)	0.5	0.8
Net profit margin (%)	4.4	(0.2)	(1.3)	0.7	0.8
Interest cover (x)	nm	358.2	(45,509.4%)	(767.2%)	(40.5%)
Effective tax rate (%)	25.2	96.1	24.3	24.3	24.3
Dividend payout (%)	59.1	nm	nm	37.5	37.5
Debtors turnover (days)	48	49	54	44	45
Stock turnover (days)	44	47	55	45	46
Creditors turnover (days)	52	56	66	54	55

Source: Company, AmlInvestment Bank Bhd estimates

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