

20 January 2017 | Corporate Update

UMW Holdings

Positive catalyst from O&G exit

- **UMW exiting the O&G industry via re-distribution of UMWOG shares to shareholders**
- **Removes a key drag on balance sheet and bottomline can possibly swing into profits**
- **Improvement in risk profile might pave the way for more value creation**
- **Meantime, this positive news is likely to drive a fresh round of valuation re-rating. We raise UMW to a TRADING BUY at unchanged TP of RM5.15/share**

Exiting the O&G industry. UMW Holdings (UMW) announced that it will redistribute (hence dispose) its entire 56% stake in UMW Oil & Gas (UMWOG) to UMW's shareholders. This will be done via dividend-in-specie at date to be determined later. Post-exercise, UMW's shareholders will own shares directly in UMWOG.

The exercise is part of UMW's plan to exit the O&G industry. The remaining unlisted O&G businesses currently sitting at UMW (comprising mainly pipe manufacturing, land rigs and trading) will be gradually disposed off. PNB and EPF will end up with 45% and 14% direct stakes in UMWOG from 13% and 5% currently.

UMWOG to undertake industry consolidation. After the demerger from UMW, UMWOG will undertake a merger exercise with Ekuinas-controlled Icon Offshore and Orkim Sdn. Bhd. The plan is to acquire 100% in Icon by issuing new shares in UMWOG (valued at RM0.80/share, a 10% discount to current market price) to the respective sellers. Icon shares in turn are valued at RM0.50/share (a 15% premium to current market price). As for Orkim, UMWOG will pay RM475m cash for Ekuinas' 96% stake in the company.

Post-consolidation, the enlarged UMWOG group will undertake a rights issue to raise RM1.8b mainly to repay debt, of which part of it will be used for the acquisitions. The demerger from UMW is expected to be completed by April 2017, while the consolidation and rights issue are expected to be completed in July and August respectively.

**Upgraded TRADING BUY
(Previously NEUTRAL)
Maintain Target price (TP): RM5.15**

RETURN STATS	
Price (19 Jan 2017)	RM4.62
Target Price	RM5.15
Expected Share Price Return	+11.5%
Expected Dividend Yield	+0.7%
Expected Total Return	+12.2%

STOCK INFO	
KLCI	1,647.47
Bursa / Bloomberg	4588 / UMWH MK
Board / Sector	Main/Automotive
Syariah Compliant	Yes
Issued shares (mil)	1,168.29
Par Value (RM)	1.00
Market cap. (RM'm)	5,198.91
Price over NA	0.83
52-wk price Range	RM4.43 – RM7.77
Beta (against KLCI)	1.15
3-mth Avg Daily Vol	0.46m
3-mth Avg Daily Value	RM2.48m
Major Shareholders (%)	
SKIM ASB	42.11%
EPF	15.96%
YPB	5.72%

INVESTMENT STATISTICS

FYE Dec	FY13	FY14	FY15	FY16F	FY17F
Revenue (RM'm)	13,951.5	14,932.5	14,419.8	10,543.9	12,067.3
EBIT (RM'm)	1,296.5	1,432.9	134.9	-182.2	-134.3
Pre-tax Profit (RM'm)	1,501.6	1,621.5	265.6	-204.0	-201.9
Core net profit (RM'm)	960.4	836.8	338.0	-160.9	-161.0
FD EPS (sen)	82.2	71.6	28.9	-13.8	-13.8
EPS growth (%)	0.9	-12.9	-59.6	-147.6	0.1
PER (x)	5.4	6.2	15.4	-32.3	-32.3
Net Dividend (sen)	44.0	41.0	20.0	3.0	3.0
Net Dividend Yield (%)	9.9	9.2	4.5	0.7	0.7

Source: Company, MIDFR

OUR TAKE ON UMWOG DEMERGER:

The exercise is very positive for UMW given that:

- (1) Avoids further cash leakage.** UMWOG requires further injection of capital and post-consolidation with Icon and Orkim (further details in this report), will undertake a rights issue to raise fresh capital for debt repayment – also partly to fund the acquisitions (See Exhibit 1). UMW gets to avoid further cash leakage into UMWOG as it will dispose of its stake prior to this cash call.
- (2) Improves UMW's financial position significantly.** UMWOG registered ~RM370m net loss in FY15 and this was a big drag to UMW. UMW's bottomline can easily swing into profits post-disposal of UMWOG. More importantly, balance sheet is expected to improve significantly - gearing is expected to more than halve while total borrowing will reduce by 67% (based on FY15 statements).

EXHIBIT 1: POSITIVE IMPACT OF DEMERGER ON UMW

Based on FY15 Financial Statements	Pre-demerger	Post-demerger
Shareholders Fund (RMm)	6,584.5	4,727.0
UMW shares out (m)	1,168.3	1,168.3
Book value/share (RM)	5.64	4.05
Total borrowings (RMm)	6,014.8	2,010.5
Gearing (x)	0.91	0.43
Estimated net profit (RMm)	(38.9)	166.3

Source: Company, MIDFR

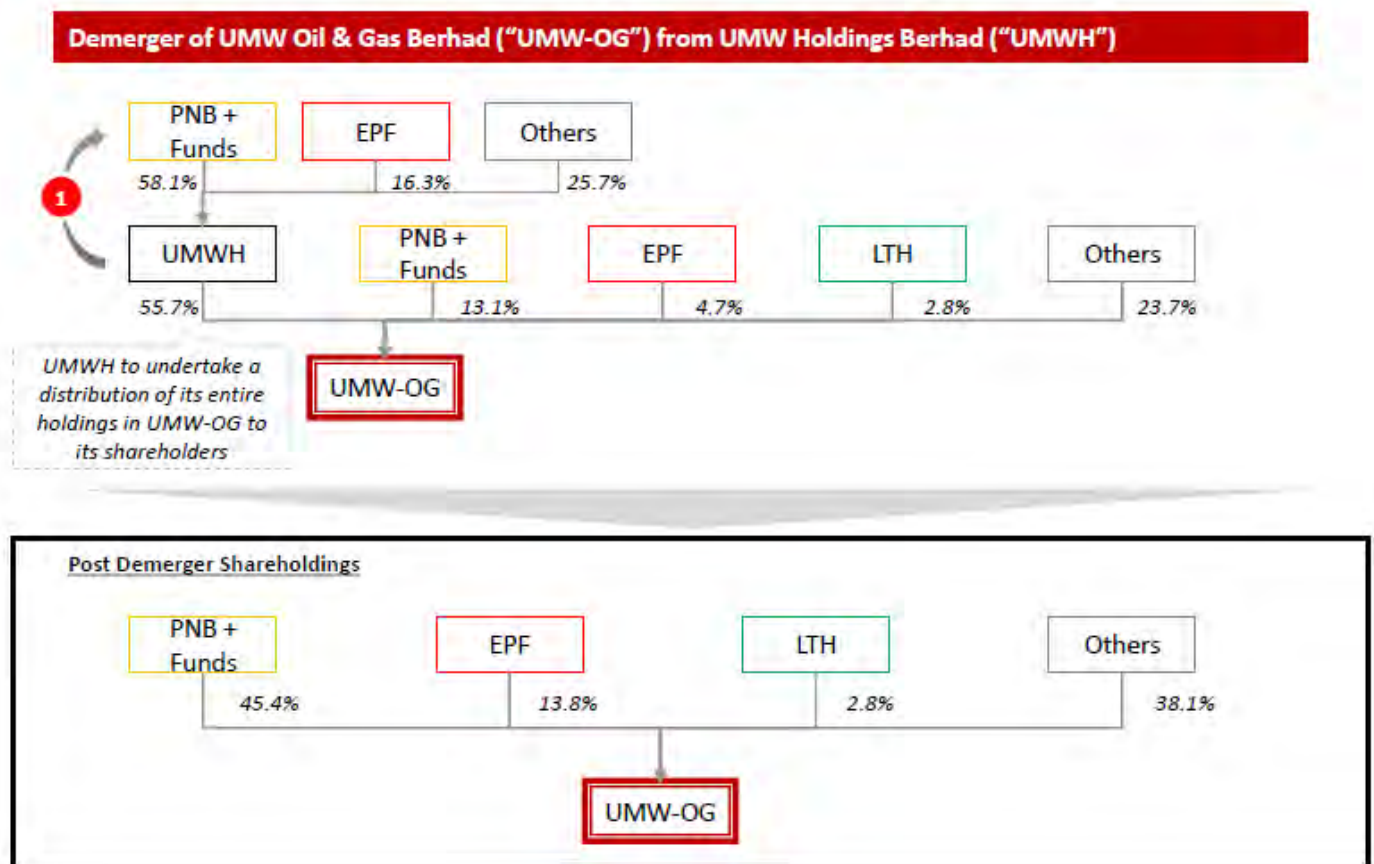
- (3) Paves the way for more value creation at UMW?** Oil & gas is a capital intensive business and following the sharp drop in revenues, has taken a massive toll on balance sheet of industry players, including UMWOG. The demerger, paves the way for more value creation at UMW (e.g. merger with another automotive group with common shareholders) as the disposal of UMWOG takes out a key risk within the group which might have hindered possible M&As in the past, we think.
- (4) Possible valuation re-rating?** The removal of a key drag to UMW's earnings and balance sheet is likely to lead to a fresh round of valuation re-rating for UMW. The stock is currently trading at a 10% discount to FY17F book value.

Raise UMW to Trading Buy. We upgrade UMW to a Trading BUY from NEUTRAL at unchanged BV-based TP of RM5.15/share. The demerger of UMWOG removes a big drag to UMW and is likely to catalyse a valuation re-rating for the group. Current share price implies a 10% discount to FY17F BV, which is likely to have been dragged by expectations of further losses at UMWOG.

Possible asset impairment in the upcoming 4Q16 result will drive down book value and is a key risk to our BV-based valuations. Based on last year's impairment of RM338m, this will reduce our FY16F/17F by circa 6% and reduces our TP to RM4.90/share. Our forecasts have already factored in core net losses of RM161m (excluding asset impairments) for both FY16F and FY17F and we are already at the lowest end of consensus.

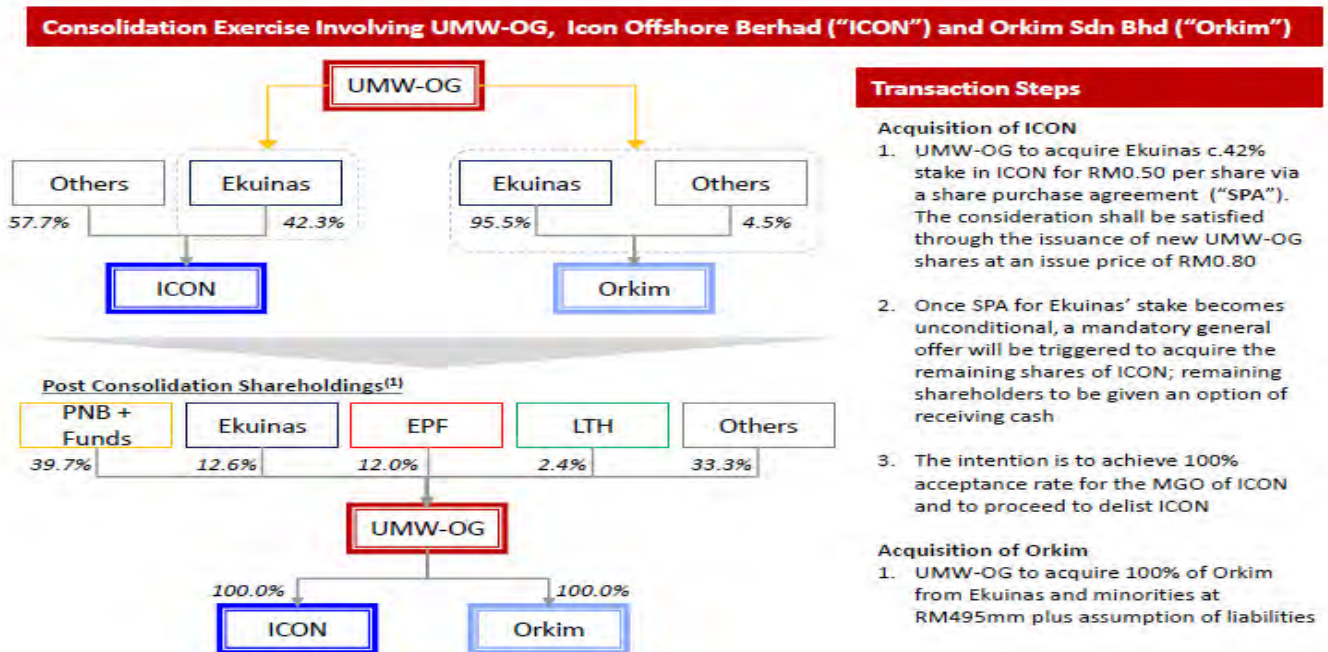
Still, market price of RM4.62/share is at a 6% discount to the estimated post-impairment book value of ~RM4.90/share (implying 0.9x FY17F PBV post-estimated impairments) suggesting the market may have already discounted the risk of the impairment. In this regard, we see trading opportunities arising for the short-term. The impact on net gearing and borrowing capacity from the resultant reduction in equity should not be too significant i.e. an increase in net gearing from 47% to 49% (pre-demerger of UMWOG).

EXHIBIT 2: DEMERGER OF UMWOG FROM UMW



Source: Company, MIDFR

EXHIBIT 3: CONSOLIDATION OF UMWOG-ICON-ORKIM



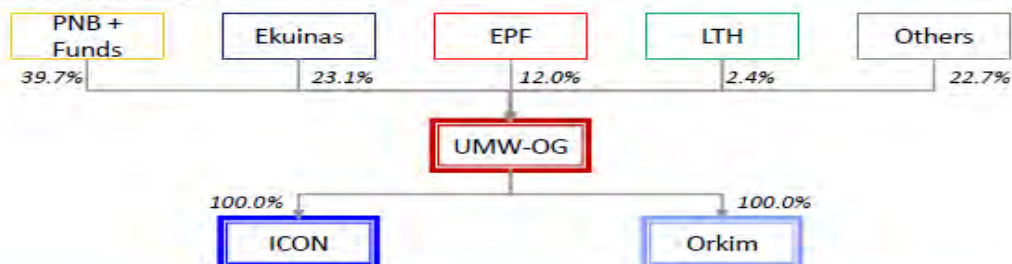
Source: Company, MIDFR

EXHIBIT 4: DETAILS OF POST-CONSOLIDATION RIGHTS ISSUE FOR UMWOG

Merged Entity to Raise Approximately RM1.8bn via a Rights Issue

Recapitalisation via a Rights Issue of RM1.8bn

Post Rights Issue Shareholdings⁽¹⁾



Rights Issue Subscription Assumptions and Indicative Utilisation of Proceeds

Shareholder	Rights Issue			Utilisation of Proceeds	RM mm
	Entitlement Value (RM'mm)	Support Value (RM'mm)	Subscription Value (RM'mm)		
PNB + Funds	720	0	720	Part repayment of bank borrowings	850
Ekuinas	228	322	550	Repayment of bridging facility	835
EPF	218	0	218	Repayment of Orkim shareholders' loan	80
LTH	44	0	44	Working capital	50
Others	604	0	282	Total Equity Size	1,815
Total	1,815	322	1,815		

Source: Company, MIDFR

EXHIBIT 5: TIMELINE FOR COMPLETION OF EXERCISES

Proposed Demerger	
23 Feb 2017	<ul style="list-style-type: none">▪ Despatch of the Circular for the proposed demerger
March 2017	<ul style="list-style-type: none">▪ EGM / shareholders' approval for the demerger▪ Application to Bursa Depository for the distribution of UMW-OG's shares – approval expected within 1 week▪ Announcement of the book closure date for the demerger
April 2017	<ul style="list-style-type: none">▪ Distribution of UMW-OG's shares▪ Announcement of completion of the demerger

Proposed Consolidation & Recapitalisation	
19 Jan 2017	<ul style="list-style-type: none">▪ Entry into SPA
March/ April 2017	<ul style="list-style-type: none">▪ Completion of due diligence exercise▪ Engagement with lenders for their consent▪ Finalise terms of the recapitalization exercise▪ Finalise terms of the proposed consolidation exercise
May/ June 2017	<ul style="list-style-type: none">▪ Seek shareholders' approval for the proposed consolidation exercise
July 2017	<ul style="list-style-type: none">▪ Acquisitions to be completed▪ Recapitalisation exercise commences
August 2017	<ul style="list-style-type: none">▪ Abridged prospectus for proposed recapitalization exercise despatched▪ Recapitalisation exercise completed

Source: Company, MIDFR

Income Statement	FY13	FY14	FY15	FY16F	FY17F
Revenue	13,951.5	14,932.5	14,419.8	10,543.9	12,067.3
Operating expenses	(12,655.0)	(13,499.6)	(14,157.6)	(10,726.0)	(12,201.6)
EBIT	1,296.5	1,567.0	262.1	(182.2)	(134.3)
Net interest expense	(18.3)	(85.1)	(126.6)	(155.8)	(193.2)
Associates	157.5	139.6	130.1	134.0	125.6
PBT	1,501.6	1,621.5	265.6	(204.0)	(201.9)
Taxation	(351.5)	(408.5)	(259.9)	84.5	81.9
Minority Interest	(431.3)	(561.0)	44.6	(41.4)	(40.9)
Net profit	718.9	652.0	(38.9)	(160.9)	(161.0)
Core net profit	960.4	836.8	338.0	(160.9)	(161.0)
Consensus net profit	960.4	836.8	338.0	103.9	270.3
Balance Sheet	FY13	FY14	FY15	FY16F	FY17F
Non-current assets	6,075.2	7,923.4	10,511.7	11,259.8	11,962.6
PPE	3,893.3	5,669.7	8,132.7	8,746.7	9,323.9
Investments in associate	1,776.2	1,797.5	1,894.5	2,028.5	2,154.1
Others	405.7	456.3	484.6	484.6	484.6
Current assets	8,731.4	8,596.2	7,568.9	6,615.4	6,929.0
Inventories	1,754.2	1,830.4	1,891.6	1,581.6	1,810.1
Receivables	1,855.1	1,238.3	1,273.3	1,476.1	1,810.1
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	2,347.6	2,098.7
TOTAL ASSETS	14,806.7	16,519.7	18,080.6	17,875.2	18,891.6
Share capital	584.1	584.1	584.1	584.1	584.1
Minority Interest	2,613.9	2,852.6	2,827.1	2,844.9	2,862.2
Reserves	5,778.6	5,996.3	5,812.7	5,618.1	5,422.6
TOTAL EQUITY	8,976.6	9,433.1	9,223.9	9,047.1	8,868.9
Non-current liabilities	1,774.7	2,017.0	3,165.1	4,115.1	5,065.1
Long-term borrowings	1,602.2	1,803.0	2,782.5	3,732.5	4,682.5
Deferred tax liabilities	34.2	27.4	34.1	34.1	34.1
Others	138.3	186.6	348.5	348.5	348.5
Current liabilities	4,055.4	5,069.6	5,691.6	4,713.1	4,957.6
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	1,691.6	1,936.0
Others	520.9	560.0	302.2	162.3	162.5
TOTAL LIABILITIES	5,830.0	7,086.6	8,856.7	8,828.1	10,022.7

Cash Flow Statement	FY13	FY14	FY15	FY16F	FY17F
Operating activities					
PBT	1,501.6	1,621.5	265.6	(204.0)	(201.9)
Depreciation & Amortization	325.3	378.7	765.5	488.0	524.8
Chgs in working capital	(423.7)	(149.1)	(134.2)	(26.3)	(317.9)
Interest expense	18.3	(48.9)	(120.8)	(155.8)	(193.2)
Tax paid	(374.4)	(418.3)	(275.5)	84.5	81.9
Others	(152.5)	(18.9)	(125.3)	21.8	67.6
CF from Operations	894.6	1,364.9	375.3	208.2	(38.8)
Investing activities					
Capex	(999.9)	(2,185.5)	(2,168.8)	(1,250.0)	(1,250.0)
Others	888.7	1,870.6	264.6	148.0	148.0
CF from Investments	(111.2)	(315.0)	(1,904.2)	(1,102.0)	(1,102.0)
Financing activities					
Dividends paid	(1,050.3)	(947.2)	(806.1)	(58.1)	(58.1)
Net proceeds in borrowings	240.7	1,150.7	1,692.3	650.0	950.0
Others	66.9	-	-	-	-
CF from Financing	(742.7)	203.6	886.3	591.9	891.9
Net changes in cash	40.7	1,253.5	(642.6)	(301.9)	(248.9)
Beginning cash	1,547.7	1,492.3	3,276.6	2,649.5	2,347.6
Overdrafts & Deposits	-	-	15.6	-	-
Ending cash	1,588.3	2,745.8	2,649.5	2,347.6	2,098.7
Ratios	FY13	FY14	FY15	FY16F	FY17F
Revenue growth	0.6%	7.0%	-3.4%	-26.9%	14.4%
EBIT growth	-32.0%	10.5%	-90.6%	>100%	-26.3%
Core net profit growth	-24.5%	-12.9%	-59.6%	-147.6%	0.1%
PBT margin	10.8%	10.9%	1.8%	-1.9%	-1.7%
Core net profit margin	5.2%	5.6%	2.3%	-1.5%	-1.3%
ROE	12.9%	10.1%	-0.6%	-2.6%	-2.6%
ROA	9.7%	9.1%	0.8%	-1.0%	-0.7%
Net gearing (%)	5.8%	7.7%	34.8%	46.9%	61.4%
Book value/share (RM)	5.45	5.63	5.48	5.31	5.14
PBV (x)	0.82	0.79	0.81	0.84	0.87
EV/EBITDA (x)	3.5	3.3	9.3	30.9	27.3

DAILY PRICE CHART



Hafriz Hezry
hafriz.hezry@midf.com.my
03-2173 8392

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).

(Bank Pelaburan)

(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This document may not be reproduced, distributed or published in any form or for any purpose.

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.