

29 August 2017

Consumer Cyclical | Auto & Autoparts

UMW Holdings

Transformation Pains

UMW's 2Q17 results fell short of both our and consensus estimates. All segments contributed to the disappointing quarter, which was topped off by an unexpected MYR126.8m loss on the demerger. Meanwhile, its legacy non-core oil & gas business chipped in with a larger-than-expected pre-tax loss. The prolonged exit process from the non-core oil & gas business would continue to be a drag. UMW's earnings trend in the next two years is likely to be uneven, due to gestational losses from its aerospace arm and pre-operating expenses arising from its new Toyota assembly plant. We still think its share price has outstripped fundamentals. Maintain SELL, with a lower TP of MYR4.90 (from MYR5.15, 14.8% downside).

SELL. We reiterate that UMW's valuations no longer correctly reflect its fundamentals. Valuations are demanding, given the continued legacy oil & gas losses and pre-operating costs from the new plant, which may dampen 2018 earnings. Our new MYR4.90 TP is derived from applying a 1.62x target P/BV (10% discount to the 7-year historical mean), from a P/E based SOP approach.

The long goodbye. While operational losses from UMW Oil & Gas are in line, the demerger loss of MYR126.9m was unexpected. The unlisted oil & gas unit continued to disappoint despite previous impairment charges. Losses for the quarter spiked higher, attributed to lower revenue and redundancy expenses incurred on the cessation of drilling operations in Oman. Automotive revenue grew, reflecting the demand for new models but segmental profit declined YoY on unfavourable forex rates. Similarly, its equipment division booked higher revenue but lower profits due to forex and a competitive operating environment. Profitability at its mechanical and engineering (M&E) unit was impacted by pre-operating expenses incurred for the aerospace business that were higher than previously guided. Its "Others" division also recorded sharply higher losses, likely arising from costs associated by the issuance of MYR700m of Islamic medium-term notes programme. No dividend was declared during the quarter.

Transformation pains. While we believe UMW's initiatives to refocus on its core businesses are a step in the right direction, the process of exiting its non-core oil & gas businesses is taking much longer than expected, with a heavy price still being paid from the recognition of ongoing losses. Expect more gestational losses arising from its aerospace venture, while pre-operating losses are likely to be incurred as the new Toyota plant reaches the final stages of construction. While there is some market excitement on the new Toyota C-HR SUV, it will not be locally assembled until the new plant is commissioned in 2019. Also, the likely high selling price upon its launch in 2018 would cap potential sales volumes.

Forecasts and risks. We now expect UMW to record a consolidated net loss of MYR176.4m in 2017 while our 2018-2019 earnings estimates have been cut by 14.6% and 13% respectively. Key upside risks to our recommendation and TP include more favourable exchange rates, stronger sales volumes and higher oil prices leading to reduced residual oil & gas losses.

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (MYRm)	14,442	10,965	11,802	12,188	12,975
Reported net profit (MYRm)	299	222	(176)	349	399
Recurring net profit (MYRm)	150	(213)	(176)	349	399
Recurring net profit growth (%)	(81.2)	(241.9)	(17.3)	0.0	14.3
Recurring EPS (MYR)	0.13	(0.18)	(0.15)	0.30	0.34
DPS (MYR)	0.20	na	0.10	0.10	0.10
Recurring P/E (x)	44.7	na	na	19.3	16.8
P/B (x)	1.05	1.42	2.62	2.48	2.33
P/CF (x)	11.5	na	11.7	19.5	13.3
Dividend Yield (%)	3.5	na	1.7	1.7	1.7
EV/EBITDA (x)	11.9	38.5	12.9	8.4	7.8
Return on average equity (%)	4.6	4.0	(4.8)	13.2	14.3
Net debt to equity (%)	34.8	61.2	19.0	34.6	42.4
Our vs consensus EPS (adjusted) (%)			(167.3)	(14.6)	(13.0)

Source: Company data, RHB

Sell (Maintained)

Target Price:	MYR4.90
Price:	MYR5.75
Market Cap:	USD1,574m
Bloomberg Ticker:	UMWH MK

Share Data

Avg Daily Turnover (MYR/USD)	2.33m/0.54m
52-wk Price low/high (MYR)	4.11 - 5.90
Free Float (%)	25
Shares outstanding (m)	1,168
Estimated Return	-15%

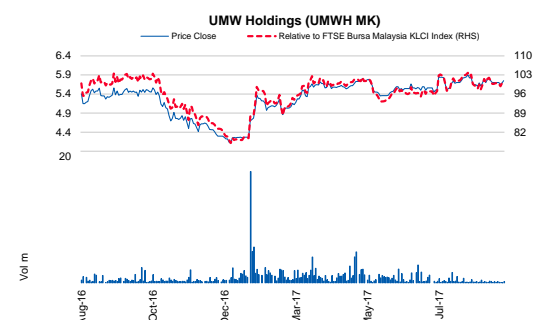
Shareholders (%)

PNB Funds	57.6
EPF	16.5

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	36.2	(1.2)	2.9	12.3	2.9
Relative	28.4	(1.3)	3.1	7.8	(2.2)

Source: Bloomberg



Source: Bloomberg

Analyst

Alexander Chia
+603 9280 8889
alexander.chia@rhbgroup.com



Financial Exhibits

Financial model updated on : 2017-08-28.

Asia		Financial summary	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Malaysia		Recurring EPS (MYR)	0.13	(0.18)	(0.15)	0.30	0.34
Consumer Cyclical		EPS (MYR)	0.26	0.19	(0.15)	0.30	0.34
UMW Holdings		DPS (MYR)	0.20	0.00	0.10	0.10	0.10
Bloomberg	UMWH MK	BVPS (MYR)	5.48	4.04	2.20	2.32	2.47
Sell		Weighted avg adjusted shares (m)	1,168	1,168	1,168	1,168	1,168
Valuation basis		Valuation metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
SOP		Recurring P/E (x)	44.7	na	na	19.3	16.8
Key drivers		P/E (x)	22.4	30.3	na	19.3	16.8
i. Introduction of attractive new car models;		P/B (x)	1.05	1.42	2.62	2.48	2.33
ii. Turnaround at various legacy non-core oil and gas businesses;		FCF Yield (%)	(22.9)	(16.0)	(6.3)	(9.7)	(4.4)
iii. Long-term growth potential from aerospace business.		Dividend Yield (%)	3.5	0.0	1.7	1.7	1.7
Key risks		EV/EBITDA (x)	11.9	38.5	12.9	8.4	7.8
i. Weaker MYR;		EV/EBIT (x)	22.6	na	na	12.2	10.5
ii. Weaker-than-expected economic growth;		Income statement (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
iii. Higher start-up losses from aerospace venture.		Total turnover	14,442	10,965	11,802	12,188	12,975
Company Profile		Gross profit	3,971	3,015	3,245	3,352	3,568
UMW is the largest company in the automotive sector. Its 51%-owned subsidiary UMW-Toyota imports, assembles and distributes Toyota and Lexus vehicles in Malaysia.		EBITDA	900	264	312	570	688
		Depreciation and amortisation	(428)	(555)	(414)	(175)	(178)
		Operating profit	472	(291)	(102)	395	510
		Net interest	(0)	(106)	(71)	(28)	(50)
		Income from associates & JVs	134	155	142	153	158
		Pre-tax profit	606	(242)	(31)	520	618
		Taxation	(267)	(141)	(130)	(114)	(136)
		Minority interests	(39)	604	(15)	(57)	(83)
		Recurring net profit	150	(213)	(176)	349	399
		Cash flow (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
		Change in working capital	241	775	524	(36)	27
		Cash flow from operations	584	(151)	575	345	505
		Capex	(2,125)	(925)	(1,000)	(1,000)	(800)
		Cash flow from investing activities	(1,904)	(596)	(436)	(954)	(776)
		Dividends paid	(479)	(234)	0	(117)	(117)
		Cash flow from financing activities	414	(36)	(4,061)	(322)	(340)
		Cash at beginning of period	3,376	2,728	2,179	1,617	804
		Net change in cash	(906)	(783)	(3,923)	(931)	(610)
		Ending balance cash	2,728	2,179	1,617	827	427
		Balance sheet (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
		Total cash and equivalents	2,728	2,179	1,617	804	310
		Tangible fixed assets	8,133	7,639	3,064	3,889	4,511
		Intangible assets	38	0	0	0	0
		Total investments	1,975	2,081	2,220	2,373	2,531
		Total other assets	365	350	348	348	348
		Total assets	18,081	16,206	10,035	10,540	10,924
		Short-term debt	3,159	2,617	1,112	1,112	1,112
		Total long-term debt	2,783	3,789	1,413	1,413	1,413
		Other liabilities	279	803	803	803	803
		Total liabilities	8,857	9,297	5,267	5,572	5,697
		Shareholders' equity	6,397	4,722	2,565	2,709	2,885
		Minority interests	2,827	2,187	2,203	2,259	2,343
		Total equity	9,224	6,909	4,768	4,969	5,227
		Net debt	3,213	4,226	907	1,721	2,215
		Total liabilities & equity	18,081	16,206	10,035	10,540	10,924
		Key metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
		Revenue growth (%)	(3.5)	(24.1)	7.6	3.3	6.5
		Recurrent EPS growth (%)	(81.2)	(241.9)	(17.3)	0.0	14.3
		Gross margin (%)	27.5	27.5	27.5	27.5	27.5
		Operating EBITDA margin (%)	6.2	2.4	2.6	4.7	5.3
		Net profit margin (%)	2.1	2.0	(1.5)	2.9	3.1
		Dividend payout ratio (%)	78.1	0.0	(66.2)	33.5	29.3
		Capex/sales (%)	14.7	8.4	8.5	8.2	6.2
		Interest cover (x)	3.72	(1.56)	(0.76)	5.32	6.87

Source: Company data, RHB

Transformation Pains

Figure 1: Earnings review

FYE Dec (MYRm)	2Q16	1Q17	2Q17	QoQ (%)	YoY (%)	1H16	1H17	YoY (%)	Comments
Revenue	2,846.8	2,729.3	2,785.7	2.1	(2.1)	5,046.0	5,515.0	9.3	Higher revenue mainly from the recovery in Toyota sales
EBIT	41.1	90.0	(35.3)	139.2	(185.9)	58.2	54.7	(6.0)	Unfavourable forex and higher legacy non-core oil & gas losses helped to drive margins down
EBIT margin (%)	1.4	3.3	(1.3)	0.0	0.0	1.2	1.0	0.0	
Finance costs	(41.3)	(28.8)	(24.0)	(16.7)	(41.8)	(84.6)	(52.9)	(37.5)	
Associates	26.5	40.0	28.0	(29.9)	5.7	48.6	68.0	40.0	Associate earnings mainly from 38%-owned Perodua fell as the company prepares to launch the new Myvi in 4Q17
Investment income	18.5	18.1	20.1	10.7	8.6	43.6	38.2	(12.5)	
Pretax Profit	44.8	119.3	(11.2)	109.4	(125.0)	65.9	108.1	64.1	
Pretax margin (%)	1.6	4.4	(0.4)	0.0	0.0	1.3	2.0	0.0	
Tax	(48.5)	(24.9)	(35.2)	41.3	(27.4)	(74.5)	(60.2)	(19.3)	
Effective tax rate (%)	(108.3)	(20.9)	314.7	0.0	0.0	(113.1)	(55.7)	0.0	
Loss from discontinued operations	0.0	(104.9)	(178.5)	(70.1)	NA	0.0	(283.4)	NA	MYR126.9m loss on demerger was unexpected
MI - Continuing	(8.4)	(16.2)	(7.5)	53.4	(10.3)	13.1	(23.7)	(280.8)	
MI - Discontinued	0.0	46.9	23.1	50.7	NA	0.0	70.0	NA	
Net profit - Continuing	(12.1)	78.2	(54.0)	169.0	345.1	4.5	24.2	443.6	
Net Profit - Discontinued	0.0	(58.0)	(155.3)	(167.7)	NA	0.0	(213.3)	NA	
Net Profit - Total	(12.1)	20.2	(209.3)	1,138.0	1,625.9	4.5	(189.1)	(4,347.4)	

Source: Company data, RHB

Figure 2: UMW vehicle sales summary

FYE Dec (units)	2Q16	1Q17	2Q17	QoQ (%)	YoY (%)	1H16	1H17	YoY (%)
Toyota	17,392	16,694	17,439	4.5	0.3	27,880	34,133	22.4
- Passenger	12,443	12,297	12,060	(1.9)	(3.1)	19,485	24,357	25.0
- Commercial	4,949	4,397	5,379	22.3	8.7	8,395	9,776	16.5
Perodua	50,189	50,265	49,410	(1.7)	(1.6)	97,370	99,675	2.4
- Passenger	50,189	50,265	49,410	(1.7)	(1.6)	97,370	99,675	2.4
- Commercial	0	0	0	0.0	0.0	0	0	0.0
Total	67,581	66,959	66,849	(0.2)	(1.1)	125,250	133,808	6.8

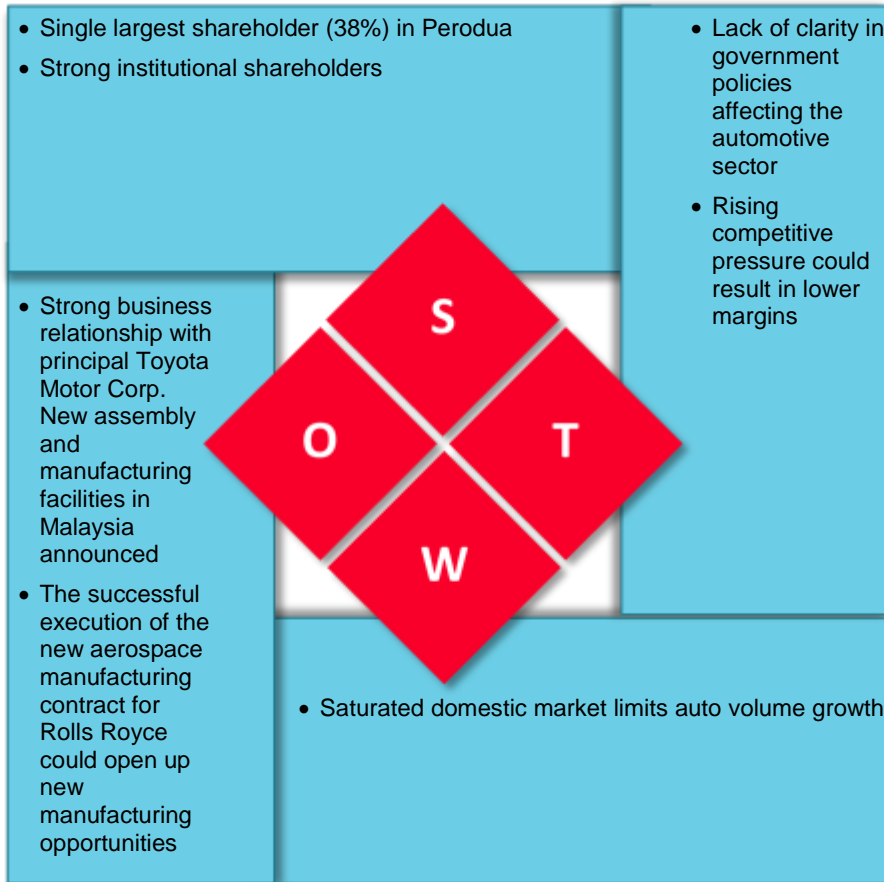
Source: MAA

Figure 3: Forecast assumptions

FYE Dec	2016	2017F	2018F	2019F
Toyota / Lexus (units)	65,110	72,000	75,000	79,000
Perodua (units)	207,110	205,000	210,000	212,000
Forex (JPY/MYR)*	3.82	3.80	3.80	3.80
Forex (USD/MYR)*	4.14	4.31	4.20	4.10
*average rate				

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-07-04	Sell	5.1	5.8
2017-05-24	Neutral	5.6	5.5
2017-02-28	Neutral	5.5	5.1
2017-02-16	Neutral	5.4	5.0
2016-11-03	Sell	4.1	5.4
2016-08-30	Sell	4.3	5.1
2016-05-25	Sell	4.0	4.8
2016-02-26	Sell	5.0	6.5
2016-01-17	Sell	5.0	6.7
2015-11-27	Sell	5.0	7.4

Source: RHB, Bloomberg

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Kuala Lumpur	Hong Kong	Singapore
<p>RHB Research Institute Sdn Bhd Level 3A, Tower One, RHB Centre Jalan Tun Razak Kuala Lumpur 50400 Malaysia Tel : +(60) 3 9280 8888 Fax : +(60) 3 9200 2216</p>	<p>RHB Securities Hong Kong Ltd. 12th Floor World-Wide House 19 Des Voeux Road Central, Hong Kong Tel : +(852) 2525 1118 Fax : +(852) 2810 0908</p>	<p>RHB Research Institute Singapore Pte Ltd. 10 Collyer Quay #09-08 Ocean Financial Centre Singapore 049315 Tel : +(65) 6533 1818 Fax : +(65) 6532 6211</p>
Jakarta	Shanghai	Bangkok
<p>PT RHB Sekuritas Indonesia Wisma Mulia, 20th Floor Jl. Jenderal Gatot Subroto No. 42 Jakarta 12710, Indonesia Tel : +(6221) 2783 0888 Fax : +(6221) 2783 0777</p>	<p>RHB (China) Investment Advisory Co. Ltd. Suite 4005, CITIC Square 1168 Nanjing West Road Shanghai 20041 China Tel : +(8621) 6288 9611 Fax : +(8621) 6288 9633</p>	<p>RHB Securities (Thailand) PCL 10th Floor, Sathorn Square Office Tower 98, North Sathorn Road, Silom Bangrak, Bangkok 10500 Thailand Tel: +(66) 2 088 9999 Fax : +(66) 2 088 9799</p>