

UMW Holdings

Moving into recovery phase, value unlocking soon

- **Significantly lower USD locked in for 2H17, a chance for volume to outperform**
- **Monetisation of Serendah land kickstarting soon, exploring methods to bring forward value unlocking**
- **Disposal of non-listed O&G well on track**
- **Reaffirm BUY at unchanged TP of RM7.20/share.**

We attended UMW's analyst briefing yesterday. Below are the key takeaways:

A chance to outperform? We gather that sales have picked up since launch of the four facelift models and new variants this month i.e. Vios / Fortuner / Hilux / Innova and group is well on track to achieve, if not exceed its FY17F target volume of 70K units (which implies a conservative 9.8%yoy growth). YTD, Toyota TIV has far outstripped industry growth at +21.7% (vs. industry: +4.7%).

Addressing forex volatility for autos. (1) Increasing local content e.g. Vios localisation rate increased from 51% to 58% for the current facelift model launched late FY16 - besides reducing forex exposure, UMW also benefits from lower effective excise duties (2) Increasing CKD models from the current six CKD models (and 6 CBU models); most of this will materialise after the new Bukit Raja plant is up by FY19F (3) Expanding contribution from after sales operations. UMW Toyota is also looking to rationalise its distribution network (its own branches) and focus on expanding dealerships (sales & service outlets operated by 3rd parties). Other than UMW's own measure to address forex volatility, we gather that the principal, Toyota Motor Corp (TMC) has also been providing incentives to UMW on a case by case basis since early FY17F.

3Q17 to see much lower USD rates. Average rates incurred for 1H17 was USD:RM4.37 (1H16: RM4.24). UMW has locked up rates till Sep17 at a much lower RM4.24 (3% improvement vs. 1H17) and this is expected to reduce further to RM4.21 in 4Q17. Spot rates currently stand at an even lower RM4.19. This should provide a big kicker to auto earnings in 2H17. Every 1% change in USD impacts FY18F earnings by 4.7% on our estimates.

CHR may come sooner than expected. The CHR is planned for launch in 1Q18. This is much earlier than previous indication of 3Q18 launch based on our earlier channel checks. The CHR will initially be brought in as a CBU. While registration of interest has been encouraging (>3K based on our ground checks), conversion into actual bookings is very dependent on pricing, which is expected to be finalised within the next month or so. A new CKD Camry is also on track for FY18F launch.

Maintain BUY

Unchanged Target Price (TP):RM7.20

RETURN STATS	
Price (19 Sep 2017)	RM5.44
Target Price	RM7.20
Expected Share Price Return	+32.4%
Expected Dividend Yield	+0.0%
Expected Total Return	+32.4%

STOCK INFO	
KLCI	1,776.66
Bursa / Bloomberg	4588 / UMWK MK
Board / Sector	Main/Automotive
Syariah Compliant	Yes
Issued shares (mil)	1,168.29
Market cap. (RM'm)	6,717.69
Price over NA	1.90
52-wk price Range	RM4.09 – RM5.98
Beta (against KLCI)	1.31
3-mth Avg Daily Vol	0.43m
3-mth Avg Daily Value	RM2.55m
Major Shareholders (%)	
SKIM ASB	42.1%
EPF	11.7%
KWAP	8.3%

INVESTMENT STATISTICS





FYE Dec	FY14	FY15	FY16	FY17F	FY18F
Revenue (RM'm)	14,932.5	14,419.8	10,965.1	11,208.8	10,228.9
EBIT (RM'm)	1,432.9	134.9	(2,202.8)	691.9	1,108.4
Pre-tax Profit (RM'm)	1,621.5	265.6	(2,153.8)	600.1	977.8
Core net profit (RM'm)	836.8	338.0	(401.8)	328.9	479.1
FD EPS (sen)	71.6	28.9	(34.4)	28.2	41.0
EPS growth (%)	(12.9)	(59.6)	NA	181.9	45.6
PER (x)	7.6	18.8	NA	19.3	13.3
Net Dividend (sen)	41.0	20.0	0.0	0.0	0.0
Net Dividend Yield (%)	7.5	3.7	0.0	0.0	0.0

Source: Company, MIDFR

Non-listed-O&G asset disposal well in progress. Altogether there are 16 assets to exit within 4 different segments:

- (1) Drilling & exploration – this is mainly in Oman and the group has already ceased operations and in active negotiations to dispose of the 7 land rigs it owns. These have also been written down substantially while the one –off cost for ceasing operations e.g. retrenchments and inventory write-offs of RM55m in total was booked in 2Q17. The remaining 2 assets in this segment are actually profitable.
- (2) OCTG & Line Pipe – offers have been received for the Indian unit and group is in active negotiations to dispose of another 2 units. 2 more assets are targeted for disposal by end FY18F.
- (3) Fabrication – Offers have been received and is in final negotiations. Targeted to complete soon.
- (4) Trading & oilfield services – this is a very small segment.

EXHIBIT 1: PROGRESS OF EXIT FROM NON-LISTED O&G UNITS

	No. of Assets	Target 2017	Target 2018
 Drilling & Exploration	3	1- Ceased operations, to dispose assets 2- Active negotiations	-
 OCTG & Line Pipe	5	1- Offer received, to exit 2- Active negotiations	2- active negotiations
 Fabrication	2	2 – Offer received, final negotiations	-
 Trading and Oilfield services	6	1 – Phased out exit (Phase 1 completed, Phase 2 by year end) 1 - Offer received, finalisation 1 - Restructure and exit 1 – To cease operations	2- exit
Total	16		

Source: Company, MIDFR

Monetisation of Serendah land. UMW is in talks with potential buyers of two land plots in Serendah which will unlock significant value. To recap, total land owned by UMW is 861 acres, of which only 30 acres is occupied by UMW's fan case manufacturing plant. This land is valued at circa RM2psf in UMW's books while estimated market rates of RM12-16psf (depending on size of plots for sale) is 6x-8x higher. Total value of UMW's Serendah land is worth 40sen/share, easily 6% of our SOP valuation. The two buyers are high value manufacturing companies (tie-ups with foreign partners) and is part of UMW's larger plan to create an aerospace industry cluster at Serendah. The remaining land of 551 acres is slated for mixed development in the future with a strategic partner. Interestingly, we understand UMW is exploring methods to bring forward the value unlocking and monetisation of its vast Serendah landbank.

Reinforcing position in equipment market. UMW's equipment division can be segregated into two (almost equal contribution from each), i.e. the industrial equipment unit via a tie-up with Toyota and heavy equipment as a distributor for Komatsu. UMW recently entered into a deal with Komatsu to allow the latter to take up a 26% stake in the Komatsu distribution business, allowing greater participation of the principal. This is expected to open up new markets (currently in Malaysia, Singapore, PNG and Myanmar), expand product range and client as well as see better financing assistance from the principal going forward. The deal is expected to be finalised by year end.

RR fan case loss lower than expected. The pre-operating loss from UMW's new fan case plant was lower than our earlier estimate of RM14m/quarter. Actual loss in 1H17 was RM25m (or RM12.5m/quarter). This loss is expected to reduce from 4Q17 as supplies will commence from Oct17 and revenue is generated. The unit is expected to achieve profits in FY19F. At full capacity, UMW is expected to supply 250 fan cases/annum – at this rate, we estimate revenue contribution of RM735m/annum or 7% of group revenue.

Strong 2H17 recovery intact. As we had alluded to, UMW's FY17F earnings is backloaded and the catalysts for earnings to improve in 2H17 is falling into place: (1) A much stronger Ringgit against the USD (2) Launch of four new facelifts in Sep17 (3) Elimination of UMWOG losses which stood at RM86m in 1H17. (4) Launch of new MyVi in 4Q17. Meanwhile, the gradual monetisation of UMW's massive Serendah land which will kickstart soon and progress in disposing the non-listed O&G units should also act as strong share price catalysts in the near-term.

Reaffirm contrarian BUY at unchanged TP of RM7.20/share. Key catalysts: **(1) Demerger of O&G units** de-leverages balance sheet, drives UMW back into the black and allows better focus on core divisions **(2) Reversal of prior years' market share loss**, structural cost reduction and pricing advantage from UMW Toyota's EEV-focused strategy **(3) Monetisation of UMW's 711 acres Serendah land** which will unlock value of the asset – easily worth 40sen/share on our estimates, or 6% of our SOP value **(4) A more than quadrupling of M&E division earnings** once the aerospace division reaches full scale production

EXHIBIT 2: UMW SUM-OF-PARTS VALUATION

Segments	FY18F net profit attributable to UMW (RMm)	PE (x)	Value (RMm)	Comments
Auto related	482	13	6,264	
Equipment	140	12	1,681	
Serendah land		RNAV	452	<i>RNAV of Serendah land (711 acres @ RM16psf)</i>
M&E / Others / O&G	(143)	NA		<i>Attribute no value given lack of details on segmental book value</i>
Total value	479		8,397	
No of shares (m)			1,168	
Fair value (RM)			7.20	

Source: Company, MIDFR

Income Statement (RMm) (FYE Dec)	FY14	FY15	FY16	FY17F	FY18F
Revenue	14,932.5	14,419.8	10,965.1	11,208.8	10,228.9
Operating expenses	(13,499.6)	(14,157.6)	(13,167.9)	(10,516.9)	(9,120.4)
EBIT	1,567.0	262.1	(2,202.8)	691.9	1,108.4
Net interest expense	(85.1)	(126.6)	(105.7)	(176.0)	(196.5)
Associates	139.6	130.1	154.8	84.2	65.9
PBT	1,621.5	265.6	(2,153.8)	600.1	977.8
Taxation	(408.5)	(259.9)	(140.7)	(77.4)	(182.4)
Minority Interest	(561.0)	44.6	(603.9)	(193.8)	(316.4)
Net profit	652.0	(38.9)	(1,690.6)	328.9	479.1
Core net profit	836.8	338.0	(401.8)	328.9	479.1
Core net profit (ex-O&G)	NA	NA	414.4	411.1	479.1
Consensus net profit	836.8	338.0	103.9	259.3	405.6
Balance Sheet	FY14	FY15	FY16	FY17F	FY17F
Non-current assets	7,923.4	10,511.7	10,070.2	11,921.1	12,529.6
PPE	5,669.7	8,132.7	7,639.0	9,323.9	9,866.5
Investments in associate	1,797.5	1,894.5	1,996.7	2,112.7	2,178.6
Others	456.3	484.6	434.4	484.6	484.6
Current assets	8,596.2	7,568.9	6,136.0	8,078.2	9,088.1
Inventories	1,830.4	1,891.6	1,517.9	1,681.3	1,534.3
Receivables	1,238.3	1,273.3	1,416.7	1,681.3	1,534.3
Others	2,156.8	1,675.7	278.0	1,210.1	1,210.1
Cash & equivalent	3,370.7	2,728.3	2,923.5	3,505.4	4,809.3
TOTAL ASSETS	16,519.7	18,080.6	16,206.1	19,999.3	21,617.7
Share capital	584.1	584.1	584.1	584.1	584.1
Minority Interest	2,852.6	2,827.1	3,082.3	3,276.2	3,592.5
Reserves	5,996.3	5,812.7	5,860.9	6,189.8	6,668.9
TOTAL EQUITY	9,433.1	9,223.9	9,527.4	10,050.1	10,845.6
Non-current liabilities	2,017.0	3,165.1	4,678.1	5,065.1	6,015.1
Long-term borrowings	1,803.0	2,782.5	3,732.5	4,682.5	5,632.5
Deferred tax liabilities	27.4	34.1	34.1	34.1	34.1
Others	186.6	348.5	911.5	348.5	348.5
Current liabilities	5,069.6	5,691.6	4,619.2	4,884.1	4,757.1
Short-term borrowings	2,292.6	3,159.1	2,859.1	2,859.1	2,859.1
Payables	2,217.0	2,230.3	1,623.5	1,798.3	1,641.1
Others	560.0	302.2	136.6	226.6	256.8
TOTAL LIABILITIES	7,086.6	8,856.7	9,297.3	9,949.1	10,772.1

Cash Flow Statement	FY14	FY15	FY16	FY17F	FY18F
Operating activities					
PBT	1,621.5	265.6	302.7	600.1	977.8
Depreciation & Amortization	378.7	765.5	488.0	524.8	559.4
Chgs in working capital	(149.1)	(134.2)	69.3	(229.5)	167.0
Interest expense	(48.9)	(120.8)	(155.8)	(176.0)	(196.5)
Tax paid	(418.3)	(275.5)	0.0	(77.4)	(182.4)
Others	(18.9)	(125.3)	(855.0)	91.8	130.6
CF from Operations	1,364.9	375.3	(150.9)	733.9	1,455.9
Investing activities					
Capex	(2,185.5)	(2,168.8)	(966.3)	(1,250.0)	(1,250.0)
Others	1,870.6	264.6	370.7	148.0	148.0
CF from Investments	(315.0)	(1,904.2)	(595.6)	(1,102.0)	(1,102.0)
Financing activities					
Dividends paid	(947.2)	(806.1)	0.0	0.0	0.0
Net proceeds in borrowings	1,150.7	1,692.3	650.0	950.0	950.0
Others	0.0	0.0	(429.2)	0.0	0.0
CF from Financing	203.6	886.3	220.8	950.0	950.0
Net changes in cash	1,253.5	(642.6)	(525.7)	581.9	1,303.9
Beginning cash	1,492.3	3,276.6	2,649.5	2,923.5	3,505.4
Overdrafts & Deposits	1,565.1	15.6	31.2	0.0	0.0
Ending cash	4,310.9	2,649.5	2,154.9	3,505.4	4,809.3
Ratios	FY14	FY15	FY16	FY17F	FY17F
Revenue growth	7.0%	-3.4%	-29.8%	10.8%	-8.7%
EBIT growth	10.5%	-90.6%	>100%	113.2%	60.2%
Core net profit growth	-12.9%	-59.6%	-218.9%	-181.9%	45.6%
PBT margin	10.9%	1.8%	3.0%	5.4%	9.6%
Core net profit margin	5.6%	2.3%	-3.7%	2.9%	4.7%
ROE	10.1%	-0.6%	0.7%	5.0%	6.8%
ROA	9.1%	0.8%	1.8%	3.6%	5.3%
Net gearing (%)	7.7%	34.8%	38.5%	40.2%	34.0%
Book value/share (RM)	5.63	5.48	5.52	5.80	6.21
PBV (x)	1.02	1.05	1.04	0.99	0.92
EV/EBITDA (x)	4.1	11.0	12.7	8.8	6.2

DAILY PRICE CHART



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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.