

30 Aug 2018

Consumer Cyclical | Auto &amp; Autoparts

## UMW Holdings

### Turning The Corner; Raise To NEUTRAL

We upgrade UMW to NEUTRAL from Sell, with a new TP of MYR5.59 from MYR5.50, offering 8% downside. 1H18 results are in line with our expectation but slightly below consensus'. Core earnings of MYR170.2m (+109% YoY, 1H17: MYR81.5m) accounted for 51% and 46% of our forecast and consensus estimates. The better performance was mainly attributed to higher associate contribution from Perodua and improved performance by the equipment segment. Moving forward, we expect Toyota to see stronger sales volumes in 3Q18 but then slow once SST is re-imposed, and for Perodua to sustain its 1H18 performance for the remainder of the year.

1H18 core earnings are in line with our previous forecast but slightly below consensus expectation (51% and 46% of full-year estimates). Core earnings of MYR170.2m are after stripping out a non-recurring item – estimated at MYR150m of provision reversal on financial guarantee that was incurred in 4Q17. The better performance was mainly attributed to higher associate contribution from Perodua and improved performance by the equipment segment. Meanwhile, Toyota/Lexus sales volume was lower. UMW's earnings were also hit by a write-down of investment to fair value on its unlisted oil & gas segment amounting to MYR121.9m, shown as a discontinued business.

Toyota/Lexus 1H18 sales fell 5.9% YoY and is reflected in weaker revenue contribution by the automotive segment of MYR4,259.7m (-4.3% YoY). This was mainly due to weaker sales in 1Q18. However, we expect a stronger 3Q18 performance due to the tax holiday sales jump. Toyota might wait until year-end before offering any promotions, so we could expect a slowdown in sales after September (post GST). Strong demand for the Myvi continues to drive Perodua's associate contribution and we think this is likely to continue through to the end of the year. Perodua sales volume grew to 117,098 units (+17.5% YoY) in 1H18. Meanwhile, the Perodua SUV will only be introduced in 1Q19.

**Equipment and M&E segments.** The equipment segment registered higher earnings of MYR66.4m (+18.7% YoY) due to higher export sales and increased demand from the construction sector. Meanwhile, the manufacturing & engineering (M&E) segment narrowed its losses to MYR15.4m (1H17: net loss of MYR16.5m) due to increase in sales contribution by the aerospace and higher profit from lubricants businesses. Management is guiding for the aerospace business to turn profitable by 2020.

**Key risks and forecasts.** We adjust FY18F-20F earnings higher by 0.7-6.7% after lifting our sales volume forecast for Perodua, to reflect the introduction of the new Perodua SUV. Risks to our call include a weaker-than-expected USD/MYR and stronger consumer sentiment.

**Upgrade to NEUTRAL,** after Perodua showed a sustainable associate contribution, as well as on expecting Toyota to offer more CKD product variants upon the commissioning of its new assembly facility. Our new TP of MYR5.59 is derived from ascribing 14x target P/E (unchanged) on 2019 earnings, close to the sector average. We believe the outlook for the auto business in 2019 will be boosted by the introduction of the new Toyota assembly plant early next year.

Forecasts and Valuations	Dec-16	Dec-17	Dec 18F	Dec 19F	Dec 20F
Total turnover (MYRm)	10,437	11,046	11,096	12,825	13,536
Reported net profit (MYRm)	(497)	24	354	466	542
Recurring net profit (MYRm)	208	278	354	466	542
Recurring net profit growth (%)	38.46	33.80	27.25	31.55	16.23
Recurring EPS (MYR)	0.18	0.24	0.30	0.40	0.46
DPS (MYR)	0.00	0.00	0.10	0.10	0.10
Recurring P/E (x)	36.4	27.2	21.4	16.3	14.0
P/B (x)	1.61	2.46	2.36	2.22	2.05
P/CF (x)	23.5	15.4	na	13.6	15.7
Dividend Yield (%)	na	na	1.5	1.5	1.5
EV/EBITDA (x)	14.5	12.9	18.1	14.3	13.3
Return on average equity (%)	4.5	6.4	7.9	9.7	10.5
Net debt to equity (%)	93.4	36.5	72.1	69.5	67.7
Our vs consensus EPS (adjusted) (%)			(4.73)	2.07	4.92

Source: Company data, RHB

**Neutral** (from Sell)

Target Price: MYR5.59

Price: MYR6.05

Market Cap: USD1,714.2m

Bloomberg Ticker: UMWH MK

#### Share Data

Avg Daily Turnover (MYR/USD)	4.21m/1.02m
52-wk Price low/high (MYR)	4.7 - 6.98
Free Float (%)	33
Shares outstanding (m)	1,168
Estimated Return	-8%

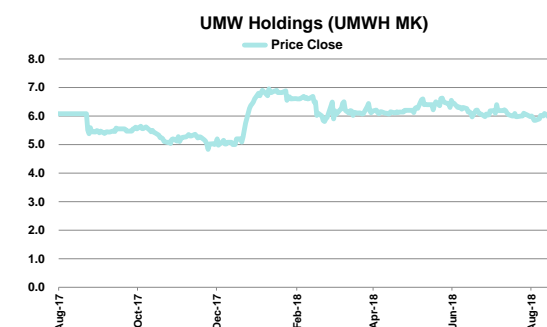
#### Shareholders (%)

Permodalan Nasional	40.8
Employees Provident Fund	10.3

#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	16.3	0.0	(5.5)	(6.9)	7.3
Relative	15.0	(2.9)	(8.0)	(5.0)	3.9

Source: Bloomberg



Source: Bloomberg

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## Turning The Corner

Figure 1: Earnings review

FYE Dec (MYRm)	2Q17	1Q18	2Q18	QoQ (%)	YoY (%)	1H17	1H18	YoY (%)	Comments
Revenue	2,757.5	2,415.3	2,919.1	20.9	5.9	5,452.7	5,334.5	(2.2)	Lower Toyota/Lexus sales volume
EBIT	10.6	91.7	241.5	(163.4)	2,171.2	107.9	333.1	208.7	
EBIT margin (%)	0.4	3.8	8.3			2.0	6.2		
Finance costs	(14.3)	(23.6)	(13.8)	(41.3)	(3.0)	(32.0)	(37.4)	16.8	
Associates	31.9	57.6	54.4	(5.6)	70.4	73.2	112.0	53.1	Higher than expected Myvi sales
Investmt income	20.0	21.6	19.3	(10.5)	(3.7)	38.1	40.9	7.3	
Pretax Profit	48.3	147.3	301.3	(104.6)	523.3	187.2	448.6	139.7	
Pretax margin (%)	1.8	6.1	10.3			3.4	8.4		
Tax	(35.2)	(29.6)	(39.6)	33.7	12.6	(59.8)	(69.2)	15.7	
Eff tax rate (%)	(72.7)	(20.1)	(13.1)			(31.9)	(15.4)		
Discontinued Op	(238.1)	(23.9)	(122.1)	411.1	(48.7)	(362.9)	(146.0)	(59.8)	
MI	15.6	(19.7)	(15.2)	(22.8)	(197.6)	46.3	(34.9)	(175.4)	
Net Profit	(209.3)	74.1	124.4	(67.9)	(159.4)	(189.1)	198.5	(204.9)	
Net Margin (%)	(7.6)	3.1	4.3			(3.5)	3.7		
Core Net Profit	(11.1)	91.2	79.0	(13.4)	(809.7)	81.5	170.2	108.8	Stripped out MYR150m from reversal of provision on financial guarantee

Source: Company data, RHB

**Figure 2: Earnings review – segmental breakdown**

FYE Dec (MYRm)	2Q17	1Q18	2Q18	QoQ (%)	YoY (%)	1H17	1H18	YoY (%)	Comments
Automotive	2,260.3	1,877.1	2,382.7	26.9	5.4	4,451.2	4,259.7	(4.3)	Weighed down by lower Toyota/Lexus sales
Equipment	351.4	373.0	365.9	(1.9)	4.2	693.8	739.0	6.5	Higher export sales and increased demand
Mfg & Eng	153.9	168.5	178.3	5.8	15.9	319.8	346.8	8.5	from construction sector
Others - O&G	0.0	0.0	0.0	na	na	0.0	0.0	na	
Others	(11.6)	(3.2)	(7.8)	141.6	(32.6)	(17.7)	(11.0)	(37.7)	
<b>Revenue</b>	<b>2,754.0</b>	<b>2,415.3</b>	<b>2,919.1</b>	<b>20.9</b>	<b>6.0</b>	<b>5,447.0</b>	<b>5,334.5</b>	<b>(2.1)</b>	
Automotive	99.0	125.9	142.4	13.1	43.9	186.0	268.4	44.3	
Equipment	32.2	44.9	37.8	(15.9)	17.4	71.7	82.7	15.3	
Mfg & Eng	(9.6)	(2.9)	(0.5)	(80.8)	(94.3)	(6.5)	(3.4)	(47.7)	
Others	(62.1)	(20.7)	121.6	687.0	295.8	(57.5)	100.9	(275.4)	MYR150m gain from non-recurring, reversal of provision on financial guarantee incurred in 4Q18
<b>PBT</b>	<b>59.4</b>	<b>147.3</b>	<b>301.3</b>	<b>104.6</b>	<b>407.0</b>	<b>193.8</b>	<b>448.6</b>	<b>131.5</b>	
<b>PBT Margins</b>									
Automotive	4.4	6.7	6.0			4.2	6.3		
Equipment	9.2	12.0	10.3			10.3	11.2		
Mfg & Eng	(6.2)	(1.7)	(0.3)			(2.0)	(1.0)		
Others	537.2	641.9	(1,559.4)			325.2	(915.1)		
	<b>2.2</b>	<b>6.1</b>	<b>10.3</b>			<b>3.6</b>	<b>8.4</b>		
Automotive	57.0	81.4	86.7	6.5	52.2	112.9	168.1	48.8	Higher contribution from Perodua and better
Equipment	24.8	36.6	29.8	(18.7)	20.1	55.9	66.4	18.7	margin due to stronger MYR against USD
Mfg & Eng	(14.1)	(9.2)	(6.2)	(32.4)	(56.1)	(16.5)	(15.4)	(7.2)	Higher profit contribution from auto
Others	(69.6)	(17.7)	118.8	(772.1)	(270.6)	(65.3)	101.1	(254.8)	components and lubricants businesses
<b>NP</b>	<b>(2.0)</b>	<b>91.1</b>	<b>229.0</b>	<b>(151.3)</b>	<b>(11,529.5)</b>	<b>86.9</b>	<b>320.2</b>	<b>268.3</b>	
<b>NP Margins</b>									
Automotive	2.5	4.3	3.6			2.5	3.9		
Equipment	7.1	9.8	8.1			8.1	9.0		
Mfg & Eng	(9.2)	(5.4)	(3.5)			(5.2)	(4.4)		
Others	602.0	547.5	(1,523.0)			369.3	(916.9)		
	<b>(0.1)</b>	<b>3.8</b>	<b>7.8</b>			<b>1.6</b>	<b>6.0</b>		

Source: Company data

**Figure 3: UMW vehicle sales summary**

FYE Dec (units)	2Q17	1Q18	2Q18	QoQ (%)	YoY (%)	1H17	1H18	YoY (%)
<b>Toyota/Lexus</b>	<b>17,439</b>	<b>12,826</b>	<b>19,308</b>	<b>50.5</b>	<b>10.7</b>	<b>34,133</b>	<b>32,134</b>	<b>(5.9)</b>
- Passenger	12,060	8,614	14,329	66.3	18.8	24,357	22,943	(5.8)
- Commercial	5,379	4,212	4,979	18.2	(7.4)	9,776	9,191	(6.0)
<b>Perodua</b>	<b>49,410</b>	<b>55,568</b>	<b>61,530</b>	<b>10.7</b>	<b>24.5</b>	<b>99,675</b>	<b>117,098</b>	<b>17.5</b>
<b>Total</b>	<b>66,849</b>	<b>68,394</b>	<b>80,838</b>	<b>18.2</b>	<b>20.9</b>	<b>133,808</b>	<b>149,232</b>	<b>11.5</b>

Source: Malaysian Automotive Association (MAA)

Figure 4: Forecast assumptions

FYE Dec	2016	2017	2018F	2019F	2020F
Toyota / Lexus (units)	65,110	70,474	68,000	78,000	80,000
Perodua (units)	207,110	204,887	230,000	225,000	225,000
Forex (JPY/MYR)*	3.82	3.85	3.70	3.70	3.70
Forex (USD/MYR)*	4.14	4.30	4.00	4.00	4.00

\*Average rate

Source: RHB

Figure 5: USD/MYR trend



Source: Bloomberg, RHB

Figure 6: 100 JPY/MYR trend



Source: Bloomberg, RHB

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**Trading Buy:** Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months

**Take Profit:** Target price has been attained. Look to accumulate at lower levels

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