Challenging times ahead; maintain HOLD

We remain cautious on UMW Holdings (UMWH)'s near-term outlook, as we believe the Covid-19 pandemic will likely reduce demand for its auto and equipment segments. We believe these concerns and the decline in foreign shareholding have resulted in UMWH's share price falling by 66% in the past year, retracing back to its 2007 share price levels. In view of the challenging business outlook, we lower our SOTP-based 12-month TP to RM2.00 (from RM2.30) based on lower valuation multiples. At a 10.8x 2020E PER, the valuation looks fair.

Expect weaker automotive sales in 2020E

Toyota and UMWH's 38%-owned Perodua are guiding for flat to lower sales in 2020, targeting to sell 66k units (-6% yoy) and 240k units (-0.1% yoy) respectively. We believe these targets are hard to reach in a weak consumption environment, and we estimate lower Toyota and Perodua sales of 57k units (-19% yoy) and 217k units (-10% yoy) respectively. UMW Toyota hopes to cushion the impact by introducing 4 new SUVs in 2020, namely the Lexus UX, Toyota RAV4, and two undisclosed SUV models.

Near-term upside remains limited for the equipment segment

Management acknowledged that the outlook for heavy equipment remains subdued for the key markets in which it operates – largely due to the reduced infrastructure spending in Malaysia and mining suspension in Myanmar. We believe this shortfall may be cushioned by the steady leasing business in the warehouse and logistics sectors.

M&E segment remains the bright spot

We expect UMW Aerospace (UMWA) to contribute positively in 2020 as it ramps up to 70%/90% utilisation rates (or 175/225 fan cases) in 2020/2021. Management guided that the Covid-19 outbreak is unlikely to result in any cancellation of orders due to the high backlog of orders currently.

Reaffirm HOLD with a lower TP of RM2.00

We are keeping our forecasts unchanged, but lowering our TP to RM2.00 (from RM2.30) based on lower valuation multiples (Fig 10), in view of the challenging business outlook. At a 10.8x 2020E PER (close to the post O&G demerger -2SD PER of 9x), UMWH's valuation looks fair, considering the tough business outlook.

Earnings & Valuation Summary

FYE 31 Dec	2018	2019	2020E	2021E	2022E
Revenue (RMm)	11,303.6	11,739.1	9,940.0	10,309.3	10,514.7
EBITDA (RMm)	853.2	594.0	570.6	718.8	841.5
Pretax profit (RMm)	800.3	754.8	417.0	550.0	651.1
Net profit (RMm)	344.5	454.4	208.1	284.3	340.4
EPS (sen)	29.5	38.9	17.8	24.3	29.1
PER (x)	6.5	5.0	10.8	7.9	6.6
Core net profit (RMm)	558.1	198.9	223.1	294.3	348.4
Core EPS (sen)	47.8	17.0	19.1	25.2	29.8
Core EPS growth (%)	238.8	(64.4)	12.2	31.9	18.4
Core PER (x)	4.0	11.3	10.1	7.7	6.5
Net DPS (sen)	7.5	6.0	5.0	6.5	7.5
Dividend Yield (%)	3.9	3.1	2.6	3.4	3.9
EV/EBITDA (x)	4.4	5.5	5.5	4.4	2.7
Chg in EPS (%)			-	-	-
Affin/Consensus (x)			0.7	0.9	1.1

Source: Company, Bloomberg, Affin Hwang estimates

Company Update

UMW Holdings

UMWH MK
Sector: Auto & Autoparts

RM1.93 @ 16 March 2020

HOLD (maintain)

Upside: 3.6%

Price Target: RM2.00

Previous Target: RM2.30

Price Performance

	1M	3M	12M
Absolute	-52.3%	-56.6%	-66.3%
Rel to KLCI	-42.6%	-46.9%	-55.8%

Stock Data

Issued shares (m)	1,168.3
Mkt cap (RMm)/(US$m)	2254.8/523.5
Avg daily vol - 6mth (m)	0.5
52-wk range (RM)	1.9-5.76
Est free float	28.3%
BV per share (RM)	3.16
P/BV (x)	0.61
Net cash/ (debt) (RMm)	(59.81)
Derivatives	No
Shariah Compliant	Yes

Key Shareholders

ASB	41.1%
EPF	2.3%
Yayasan Pelaburan Bumiputra	7.7%
KWAP	7.1%

Source: Affin Hwang, Bloomberg

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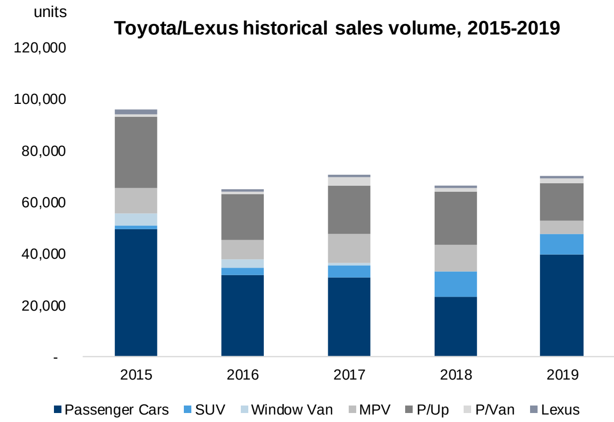
Automotive segment

2020 automotive sales likely to fall short of initial target

Both Toyota and UMWH's 38%-owned Perodua saw higher 2019 sales volumes of 70k units (+5% yoy, driven by volume-driven models like Vios and Yaris) and 240k units (+6% yoy) respectively; their combined 2019 market share rose to 51.4% (2018: 49.1%). Both car brands are guiding for flat to lower 2020 sales – Toyota targets to sell 66k units (-6% yoy or at least 12% share of Malaysia's automotive market) and Perodua aims to achieve 240k units (-0.1% yoy).

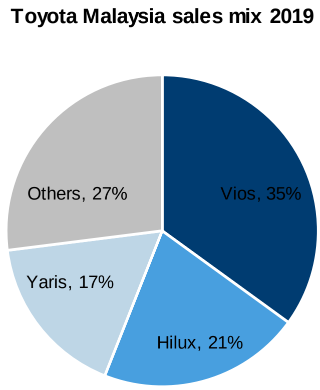
We believe these targets may not be achievable in a weak consumption environment, and we anticipate lower Toyota and Perodua sales of 57k units (-19% yoy) and 217k units (-10% yoy) respectively. Using the SARS outbreak in 2002-2003 as a reference point, Perodua's sales volume declined by 4% yoy to 126k units whereas Toyota's sales volume rose to 40k units (+47% yoy, thanks to the maiden Malaysian launch of the Toyota Vios in 2003).

Fig 1: Revamped passenger car line-up lifted Toyota car sales volume in 2019 by 5% yoy



Source: Malaysia Automotive Association (MAA)

Fig 2: Toyota's best-selling models in Malaysia are Vios (35%), Yaris (17%) and Hilux (21%).



Source: Company

Major line-up revamp on the cards for Toyota

Although Toyota's Jan20 sales volume of 3.7k units (+16% yoy; from low base effect) looks encouraging, we are concerned that the momentum may not last. UMW Toyota (UMWT) hopes to cushion the impact by:

i) expanding its model line-up with a strong focus on SUVs

UMWT plans to introduce 4 new SUV models in 2020, namely the Lexus UX, Toyota RAV4, and two undisclosed SUV models, likely arriving in a fully-imported form (CBU) from either Japan or Thailand. We do not expect robust SUV sales due to the higher price point of the CBU variants and intense competition in the SUV space in Malaysia. For instance, the response to the all-new CBU C-HR (launched in Jan18) was relatively poor, at only 2.5k units (-47% yoy) in 2019.

ii) offering attractive step-up financing packages

To target first-time buyers, Toyota Capital is offering a 9-year financing plan, known as Toyota EZ Beli. Briefly, the plan is divided into 3-tiers - the buyer can enjoy lower monthly instalments for the first 3 years, followed by a slight increase in monthly instalments in years 4-6, and then a flexible option to continue at the same repayment terms or trade in for a new Toyota from year 7 onwards.

iii) collaborating with dealers to boost after-sales service.

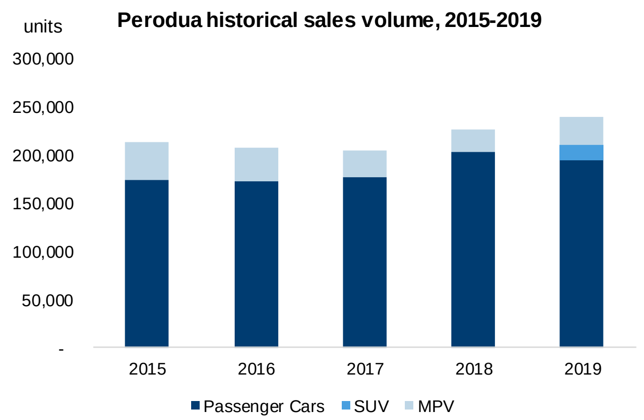
Perodua continued to perform well in 2019 …

UMWH saw an 8% increase in associate and joint-venture contribution to RM292k units, largely due to Perodua's record sales volume of 240k units (+6% yoy) in 2019, supported by popular demand for most of its key models; Perodua Aruz was the country's best-selling SUV at 30k units in 2019 (vs. Proton X70's sales volume of ~27k units).

… but we believe this momentum may not last into 2020.

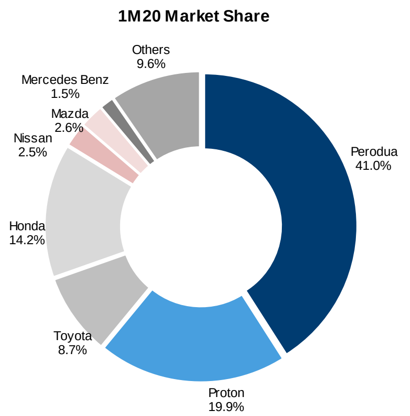
On a less positive note, we note that Perodua's sales volume peaked in Oct19 at 22.8k units, and since then, the sales momentum has gradually declined; Perodua's Jan20 sales volume declined to 17.5k units (-13% yoy, -5% mom). If this trend continues for the rest of 2020, we believe Perodua is unlikely to meet its earlier sales target of 240k units. In terms of new model launches, Perodua has so far introduced the facelifted Bezza and we believe the company is slated to launch the D55L SUV likely by 4Q20.

Fig 4: Perodua's 2019 sales volume improved by 6% to 240k units



Source: Company

Fig 5: Combined 1M20 market share for Toyota and Perodua is close to 50% (1M19: 49%).



Source: Company

We expect auto margins to be weaker in 2020E

We estimate UMWH's auto pre-tax margins to be weaker, at 5%-6% in 2020-22E (average 3-year pre-tax margin of 6%), in view of likely softer automotive sales, coupled with the added depreciation cost following the completion of its Bukit Raja plant. UMWH's depreciation and amortisation cost rose by 27% yoy to RM346m in 2019. In addition, we believe the temporary weakness in the RM (vs. the US$) will likely squeeze its profit margin given the US$ import cost for the auto-parts and CBU units.

UMW Toyota Motor (UMWT) had announced that there is no planned price increase for CKD variant models in 2020 but there are no price updates for the CBU variants. Assuming the CBU car prices remain the same, we suspect UMWT may have to absorb the volatility in exchange rates based on the revised Open Market Value calculation to keep Toyota cars competitive among its peers.

Equipment segment

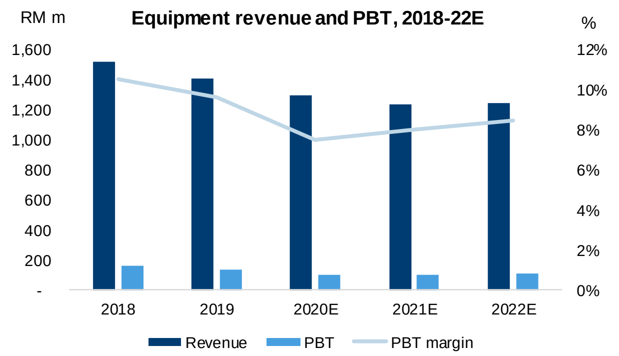
Possibly another weaker year for equipment segment

The equipment division's 2019 PBT declined by 15% yoy to RM135.7m, due to a 9% drop in revenue and narrowing margins as pricing competition remained stiff. Management acknowledged that the outlook for heavy equipment remains subdued for the key markets in which it operates – largely due to the reduced infrastructure spending in Malaysia and ban on new equipment imports following the mining suspension in Myanmar. We estimate that combined sales in Malaysia and Myanmar contributed 71% of 2019 heavy equipment sub-segment revenue. The subdued outlook is likely to be cushioned by the steady leasing business in the warehouse and logistics sectors. UMWH has plans to reinvigorate the following segments:

For heavy equipment. 1) enhancing its product offering to cater to the demand in more urbanised sectors – construction & mega infrastructure, 2) leverage on Papua New Guinea's gold mining and construction sector, 3) expand product line-up, 4) provision of value-added services, 5) implement an extended warranty programme and maintenance service contract and 6) venture into the leasing business model and equipment-as-a-service.

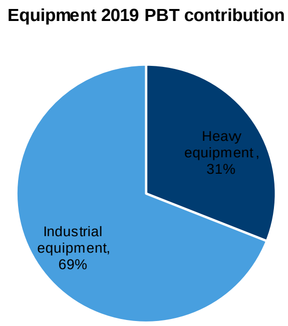
For industrial equipment. (i) further expansion in the leasing business, (ii) tap into the manufacturing and e-commerce sectors in Vietnam, and (iii) diversify product base.

Fig 6: Lower heavy equipment sales in Malaysia and Myanmar are expected to weigh on equipment earnings.



Source: Company, Affin Hwang estimates

Fig 7: Industrial segment contributed about 69% of equipment PBT.



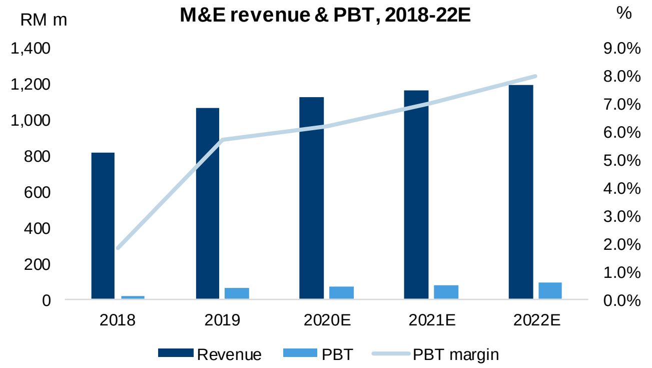
Source: Company

Manufacturing & Engineering Segment

Aerospace business likely to boost M&E segments earnings

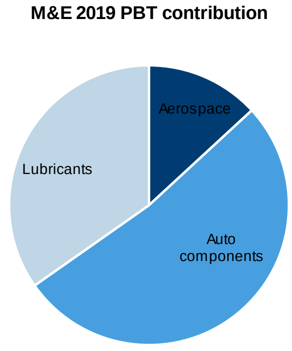
Prospects for the Manufacturing & Engineering (M&E) segment remain encouraging – 2019 PBT nearly tripled to RM60.9m from RM21.5m in 2018, driven by higher delivery of fan cases and auto-parts components. We gather from our last briefing in Dec19 that UMW Aerospace (UMWA) has delivered >150 units of Trent 1000 fan cases to Rolls Royce (since the start of production in 2017), and has turned profitable since 4Q19. Moving ahead, we expect UMWA to contribute positively in 2020 as it ramps up to 70%/90% utilisation rates (or 175/225 fan cases) in 2020/2021. Management guided that the Covid-19 pandemic is unlikely to see order cancellations due to the huge backlog of orders. UMWA is also slated to commence production of Trent 7000 fan cases in 4Q20.

Fig 8: We expect the higher aerospace plant utilisation rate to boost M&E earnings contribution.



Source: Company, Affin Hwang estimates

Fig 9: Auto components contributed about 52% of M&E's 2019 PBT.



Source: Company

Unlisted Oil & Gas

Divestment of unlisted O&G taking longer-than-expected

Management guided that they are aggressively looking to divest the companies in the unlisted Oil & Gas (O&G) segment. We gather that there are 6 remaining units, and UMWH was not able to dispose any unit back in 2019. Therefore, we expect operating losses to persist, albeit to a lesser extent than in the previous quarters as the carrying value of these units is c.RM48m. To recap, the unlisted O&G segment recorded a 2019 LBT of RM13.6m (from LBT of RM175.3m in 2018).

Earnings and recommendation

Maintain HOLD

We had previously cut our 2020-22 earnings forecasts by 5-19% and lowered our SOTP-based target price to RM2.30 (from RM3.30) in our strategy report (see page 15), considering the potential negative impact on earnings from the Covid-19 outbreak. UMWH's share price declined by more than 15% today (16 March), but we think it is still premature to revisit the stock and thus lower our TP further to RM2.00 (Fig 10). At a 10.8x 2020E PER (close to the post O&G demerger -2SDs PER of 9x), UMWH's valuation looks fair.

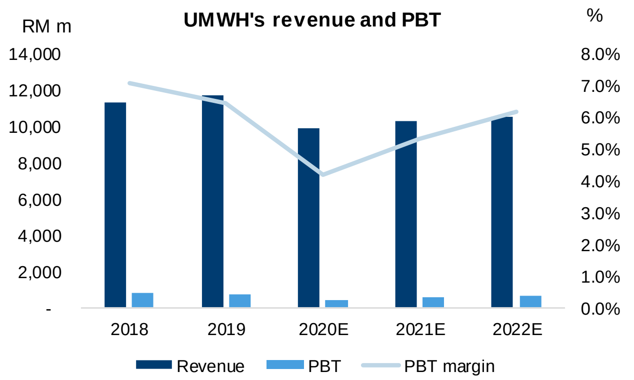
Key upside risks: higher-than-expected contribution from the aerospace segment, a strong rebound in Toyota sales, and a pick-up in construction and mining activities which would spur equipment sales, and the strengthening of the RM. Key downside risk: intense competition in the automotive and equipment segments.

Fig 10: Revised SOTP of RM2.00 (from RM2.30)

Segmental	Equity value (RMm)	multiple	Equity value per share (RM)	Comment
Automotive				
- Toyota	330.8	**PE 6.0x**	0.28	Pegged to 6x forward earnings (from 8x)
- Perodua	1,466.5	**PE 6.0x**	1.26	Pegged to 6x forward earnings (from 8x)
Equipment	300.0	**PE 4.0x**	0.26	Pegged to 4x forward earnings
M&E	395.9	**PE 7.0x**	0.34	Pegged to 7x forward earnings (from 9x)
Serendah land	905.0		0.77	RM25/sq ft
Total equity value (RMm)	2,493.1		**2.91**	
Add: net cash/(debt) per share			**(0.89)**	
SOP (RM)			**2.00**	

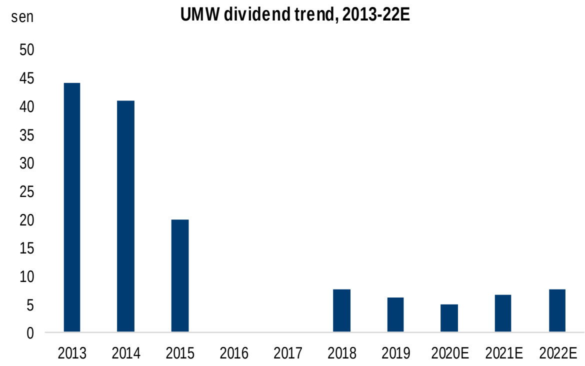
Source: Affin Hwang estimates

Fig 11: Forecasting a dip in 2020E earnings, likely weighed by softer demand from auto and equipment segments



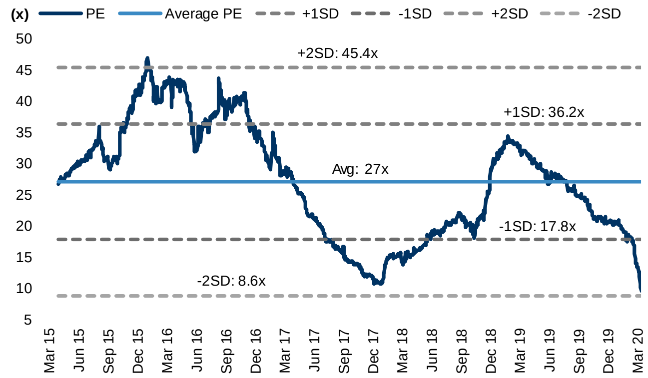
Source: Company, Affin Hwang estimates

Fig 12: A glimpse of UMWH's DPS; 2020-22E yields of 3-4% look unattractive.



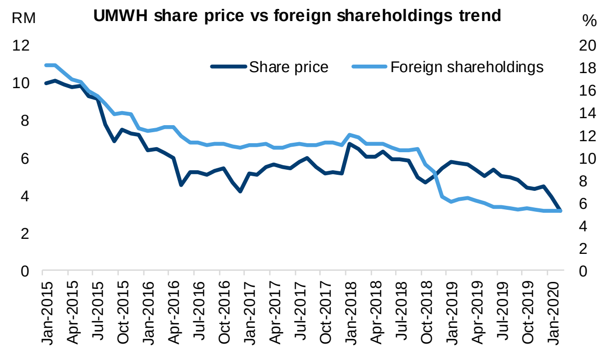
Source: Company, Affin Hwang estimates

Fig 13: At a 10.8x 2020E PER, UMWH's valuation looks fair considering its challenging business outlook



Source: Company

Fig 14: UMWH's share price falling in tandem with the lower foreign shareholdings



Source: Bloomberg, Company

UMWH – FINANCIAL SUMMARY

Profit & Loss Statement

FYE 31 Dec (RMm)	2018	2019	2020E	2021E	2022E
Revenue	11,303.6	11,739.1	9,940.0	10,309.3	10,514.7
Operating expenses	(10,450.5)	(11,145.1)	(9,369.4)	(9,590.4)	(9,673.2)
EBITDA	853.2	594.0	570.6	718.8	841.5
Depreciation	(273.7)	(346.2)	(335.1)	(373.6)	(401.6)
EBIT	579.5	247.9	235.5	345.3	440.0
Net int inc/(exp)	(12.6)	(57.6)	(62.9)	(55.3)	(54.5)
Associates' contribution	270.7	291.6	244.4	260.1	265.7
EI	(37.3)	272.9	0.0	0.0	0.0
Pretax profit	800.3	754.8	417.0	550.0	651.1
Discon. Operation	(176.3)	(17.4)	(15.0)	(10.0)	(8.0)
Tax	(124.1)	(108.7)	(95.9)	(126.5)	(149.8)
Minority interest	(155.4)	(174.3)	(98.0)	(129.3)	(153.0)
Net profit	**344.5**	**454.4**	**208.1**	**284.3**	**340.4**
Core net profit	**558.1**	**198.9**	**223.1**	**294.3**	**348.4**

Balance Sheet Statement

FYE 31 Dec (RMm)	2018	2019	2020E	2021E	2022E
Fixed assets	2,820.9	2,756.8	3,043.4	3,169.8	3,068.3
Other long term assets	2,570.2	2,748.2	2,870.4	3,000.4	3,133.3
Total non-curr assets	**5,391.2**	**5,504.9**	**5,913.8**	**6,170.3**	**6,201.5**
Cash and equivalents	1,311.8	1,472.1	1,587.0	1,517.7	1,779.6
Stocks	1,548.5	1,589.6	1,345.9	1,396.0	1,423.8
Debtors	1,076.6	1,243.0	1,052.5	1,091.6	1,113.3
Other current assets	1,148.3	1,285.0	1,285.0	1,285.0	1,285.0
Total current assets	**5,085.1**	**5,589.7**	**5,270.4**	**5,290.2**	**5,601.7**
Creditors	1,854.0	941.3	791.3	810.0	817.0
Short term borrowings	535.0	386.4	380.0	350.0	330.0
Other current liabilities	106.3	1,290.2	1,290.2	1,290.2	1,290.2
Total current liab	**2,495.3**	**2,617.9**	**2,461.5**	**2,450.2**	**2,437.2**
Long term borrowings	2,298.2	2,123.4	2,100.0	2,050.0	2,000.0
Other long term liabilities	250.0	312.1	312.1	312.1	312.1
Total long term liab	**2,548.3**	**2,435.6**	**2,412.1**	**2,362.1**	**2,312.1**
Shareholders' Funds	**5,432.8**	**6,041.2**	**6,310.5**	**6,648.1**	**7,053.9**

Cash Flow Statement

FYE 31 Dec (RMm)	2018	2019	2020E	2021E	2022E
PBT	800.3	754.8	417.0	550.0	651.1
Depreciation & amortisation	281.9	303.6	335.1	373.6	401.6
Working capital changes	(204.1)	(1,120.2)	284.1	(70.4)	(42.6)
Cash tax paid	(139.0)	(108.7)	(95.9)	(126.5)	(149.8)
Others	(564.8)	(377.3)	(321.2)	(336.7)	(337.4)
Cashflow frm operation	**174.4**	**(547.8)**	**619.1**	**389.9**	**522.9**
Capex	(915.0)	(300.0)	(600.0)	(500.0)	(300.0)
Disposal/(purchases)	0.0	0.0	0.0	0.0	0.0
Others	596.4	214.1	184.0	196.7	196.6
Cash flow frm investing	**(318.7)**	**(85.9)**	**(416.0)**	**(303.3)**	**(103.4)**
Debt raised/(repaid)	(175.4)	(323.4)	(29.8)	(80.0)	(70.0)
Equity raised/(repaid)	0.0	0.0	0.0	0.0	0.0
Net int inc/(exp)	0.0	0.0	0.0	0.0	0.0
Dividends paid	(87.6)	(70.1)	(58.4)	(75.9)	(87.6)
Others	1,282.2	0.0	0.0	0.0	0.0
Cash flow from financing	**1,019.2**	**(393.5)**	**(88.2)**	**(155.9)**	**(157.6)**
Free Cash Flow	**(740.6)**	**(847.8)**	**19.1**	**(110.1)**	**222.9**

Source: Company, Affinhwang estimates

Key Financial Ratios and Margins

FYE 31 Dec (RMm)	2017	2018	2019	2020E	2021E	2022E
Growth						
Revenue (%)	6.0	2.1	3.9	(15.3)	3.7	2.0
EBITDA (%)	(252.4)	119.3	(30.4)	(3.9)	26.0	17.1
Core net profit (%)	(16.0)	n.m.	(64.4)	12.2	31.9	18.4
Profitability						
EBITDA margin (%)	3.5	7.5	5.1	5.7	7.0	8.0
PBT margin (%)	2.4	7.1	6.4	4.2	5.3	6.2
Net profit margin (%)	1.5	4.9	1.7	2.2	2.9	3.3
Effective tax rate (%)	45.6	15.5	14.4	23.0	23.0	23.0
ROA (%)	(6.3)	3.2	4.1	1.9	2.5	2.9
Core ROE (%)	(21.0)	10.3	12.3	5.4	7.0	7.9
ROCE (%)	(21.0)	10.3	12.3	5.4	7.0	7.9
Dividend payout ratio (%)	-	25.4	35.2	26.2	25.8	25.2
Liquidity						
Current ratio (x)	1.3	2.0	2.1	2.1	2.2	2.3
Op. cash flow (RMm)	389.0	853.2	594.0	570.6	718.8	841.5
Free cashflow (RMm)	260	(741)	(848)	19	(110)	223
FCF/share (sen)	22.2	(63.4)	(72.6)	1.6	(9.4)	19.1
Asset management						
Debtors turnover (days)	33.7	34.8	38.6	38.6	38.6	38.6
Stock turnover (days)	46.5	50.0	49.4	49.4	49.4	49.4
Creditors turnover (days)	99.9	65.1	30.8	30.8	30.8	30.8
Capital structure						
Net gearing (%)	52.2	45.5	28.1	23.2	21.8	12.8
Interest cover (x)	3.3	8.7	4.7	4.6	5.9	7.1

Quarterly Profit & Loss

FYE 31 Dec (RMm)	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
Revenue	3,289.8	2,679.4	2,774.8	2,966.0	2,882.7	3,115.7
Operating expenses	(3,107.4)	(2,498.8)	(2,610.8)	(2,831.0)	(2,729.7)	(2,973.6)
EBITDA	182.5	180.5	164.0	135.0	153.0	142.1
Dept and amort	-49.1	-54.3	-86.5	-85.0	-82.0	-92.8
EBIT	133.4	126.3	77.5	50.0	71.0	49.4
Int expense	(26.4)	(53.5)	(19.2)	(43.3)	(30.8)	(32.6)
Associates' contribution	58.3	100.4	65.6	76.1	85.2	64.6
Investment income/ (expenses)	23.4	21.5	17.7	18.4	15.7	16.4
EI	-11.416	-43.389	-0.99	50.871	9.126	213.905
Pretax profit	177.2	151.2	140.7	152.1	150.3	311.7
Discon. Ops	38.4	(45.3)	(0.4)	(2.0)	1.9	(16.9)
Tax	(43.5)	(11.4)	(29.5)	(36.3)	(21.0)	(21.9)
Minority interest	(43.9)	(41.2)	(24.3)	(56.6)	(20.9)	(37.6)
Net profit	128.1	53.3	86.5	57.2	110.3	235.3
Core net profit	139.5	96.7	87.5	6.3	101.2	21.4
Margins (%)						
EBIT	4.1	4.7	2.8	1.7	2.5	1.6
PBT	5.4	5.6	5.1	5.1	5.2	10.0
Net profit	3.9	2.0	3.1	1.9	3.8	7.6
Core net profit	4.2	3.6	3.2	0.2	3.5	0.7

Important Disclosures and Disclaimer

Outthink. Outperform.

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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