UMW Holdings Berhad

(4588 | UMWH MK) Consumer Products & Services | Automotive & Parts

Maintain **BUY**

Gap-Up in 2H20

Unchanged **Target Price: RM3.40**

KEY INVESTMENT HIGHLIGHTS

- **1Q20 core earnings accounted for 26% of our FY20F despite expectations of a backloaded year; potential upside risk if 2Q20 turns out more resilient than expected**
- **Positive surprise from briefing - two new CKD models scheduled for launch in 2H20**
- **Signals renewed optimism given tax-holiday incentive, cost optimization in the works**
- **M&E division is a bright spot, Trent 7000 fan case production scheduled for 4Q20**
- **Re-affirm BUY at unchanged TP of RM3.40**

Possible chance of outperformance. UMW's 1Q20 core net profit of RM49m accounted for up to 26% of our FY20F (23% of consensus) although we had expected earnings to be largely backloaded into the 2H20 this year (given that the tax-holiday demand boost will only come from June onwards). We deem the results in-line as we anticipate a weaker 2Q20, but we flag upside risk to our forecasts should the 2Q20 turn out to be more resilient than expected. Its 1Q20 core net profit of RM49m was derived after normalizing for RM20m reversal of receivables impaired previously, RM28m forex loss on sale of unlisted O&G assets & RM3.2m gain on disposal of properties.

Weak 1Q20 not unexpected. Group core earnings fell -44%yoy but this was not unexpected given the MCO from 18th March till 4th May, which impacted the auto, equipment and M&E division in 1Q20. Autos and equipment division resumed operations since early May while the aerospace division resumed operations earlier in mid-April. Despite the lockdowns, the M&E division registered much higher profits in 1Q20 (+350%) given that it achieved breakeven in late FY19, ahead of previous expectations.

FY20F auto earnings to be backloaded. We expect 2Q20 performance for autos to weaken further before a strong rebound in 3Q20 as 2Q20 will reflect a full month of lockdown vs. half a month in 1Q20, UMW Toyota had an FY20F TIV target of 45K (-35%yoy), but this is based on the previous MAA projections prior to implementation of the tax-holiday – management expects the numbers to be revised upwards, but affirmed that it would still be targeting to maintain a market share of 11.3%; this is in-line with our current projected market share for Toyota. Management was tight-lipped on the magnitude of daily bookings post-tax-holiday announcement, but did not stop short of signaling renewed optimism and improvements in sales trends as a result of the incentive. This is coupled with a step-up in launches in 2H20, which includes new locally assembled models (1H20 launches were mostly CBU models). Management also indicated that Perodua is less impacted by the economic impact of the pandemic outbreak given downtrading by consumers; Perodua's previous TIV projection implied a lower-than-industry contraction in sales.

RETURN STATISTICS	
Price @ 15th June 2020 (RM)	2.65
Expected share price return (%)	+28.3
Expected dividend yield (%)	+1.5
Expected total return (%)	**+29.8**

SHARE PRICE CHART

Share price performance (%)	Absolute	Relative
1 month	33.8	18.8
3 months	35.0	-2.3
12 months	-44.8	-41.5

KEY STATISTICS	
FBM KLCI	1498.83
Syariah compliant	Yes
Issue shares (m)	1168.29
Estimated free float (%)	26.53
Market Capitalisation (RM'm)	3,376.37
52-wk price range	RM1.65 - RM5.5
Beta vs FBM KLCI (x)	1.86
Monthly velocity (%)	0.00
Monthly volatility (%)	13.91
3-mth average daily volume (m)	2.58
3-mth average daily value (RM'm)	5.78
Top Shareholders (%)	
Skim Amanah Saham Bumiputera	43.84
Employees Provident Fund Board	13.76
Yayasan Pelaburan Bumiputra	7.66

Analyst(s)
HAFRIZ Hezry
hafriz.hezry@midf.com.my
03-2173 8392

INVESTMENT STATISTICS

FYE Dec	FY17	FY18	FY19	FY20F	FY21F
Revenue (RM'm)	11,046.5	11,306.3	11,739.1	11,229.8	11,494.6
EBIT (RM'm)	120.4	522.9	332.6	111.7	210.3
Pre-tax Profit (RM'm)	252.9	786.2	754.8	266.5	362.9
Core net profit (RM'm)	163.8	341.7	266.3	186.0	224.1
FD EPS (sen)	14.0	29.2	22.8	15.9	19.2
EPS growth (%)	NA	108.6	(22.1)	(30.2)	20.5
PER (x)	18.9	9.1	11.4	16.6	13.8
Net Dividend (sen)	6.5	7.5	6.0	3.2	3.9
Net Dividend Yield (%)	2.5	2.8	2.3	1.2	1.5

Source: Company, MIDFR

Two CKD launches in 2H20. Our meeting with UMW previously suggested four new SUV launches for FY20F. This includes the CBU Lexus UX (launched in Mar20) and the CBU RAV4 (scheduled for launch on 18th June). Two more remaining launches this year are scheduled in 2H20. The positive surprise is that both the models are expected to be locally assembled, though management is still tight lipped on the actual models. We note however, that UMW Toyota has a pretty large gap in its mass market SUV offering, particularly in the B and C-segment SUV price points currently dominated by Honda CRV/HRV and Mazda CX5/CX30/CX3. We had indicated possibilities of localizing the CHR previously (currently a CBU priced at RM150K), but we expected this to happen only after the facelift is launched - the facelift CHR was already launched in selective international markets (e.g. Europe, Australia) since late-2019. The two CKD launches will coincide with the 6.5 months tax holiday (Jun20-Dec20); this should give UMW Toyota a strong TIV uplift in 2H20 and contribute towards Bukit Raja's pretax breakeven.

Going creative. UMW Toyota's priority is to maintain margins rather than resort to throwing excessive discounts beyond the tax-holiday savings merely in order to match competitors' discount. The group is instead embarking on incentivizing consumers via attractive financing offers e.g. 100% car financing in co-operation with Maybank and offering attractive monthly instalments (via tiered instalment structures) for selective models e.g. the Yaris could fetch monthly instalment of as low as RM498/month which is comparable to even a Perodua MyVi's instalment.

Embarking on cost optimization exercise. Management indicated that it is undergoing a cost optimization exercise this year. This is a two-pronged involving a variable component (efforts on component cost, logistics cost and productivity improvement) and a fixed cost component) through the tackling of non-strategic spending e.g. promotional expenses and opex). The former is pretty much an annual effort but the latter is expected to be temporary and exceptional to the usual cost optimization exercise. Combined, both the cost optimization effort is expected to contribute to "a few hundred million" in savings for the group (relative to our FY20F net profit of RM186m, this seems pretty substantial). Marketing and A&P expenses in particular, are pretty realistic to be brought down given the tax-holiday incentive in 2H20; it was the same case when a similar tax-holiday was implemented in FY18, which helped auto players improve margins (on top of volumes) in the period as it required less promotional efforts to attract consumers to the showrooms.

Bukit Raja progressing towards break-even. The highly automated Bukit Raja plant (45% automation rate) which commenced operations in FY19 generates much better EBITDA margins than the old ASSB Shah Alam plant given higher efficiency, but it is still loss making at the pretax level (as a standalone company) due to high depreciation (RM80m-RM100m/annum). Bukit Raja is currently producing the new Vios and Yaris and is running on a 2-shift cycle with a base capacity of 50K unit/annum on a single-shift. The ASSB plant meanwhile (38K unit/annum capacity) is producing the IMV models (Innova, Fortuner, Hilux) and the Hiace. A previously planned upgrade for ASSB to enhance its automation has been put on hold as the majority of new CKDs are likely to be produced at the Bukit Raja plant. The new locally assembled models scheduled for 2H20 are potential catalysts to drive Bukit Raja's breakeven.

Bright spot in M&E division. The M&E division is a bright spot and a growth area for UMW. UMW aerospace in particular, saw earnings turnaround a year earlier than planned in FY19 (previously targeted for FY20F) given higher volumes for fan cases and cost optimization (improved learning curve & employee capability, efficient utility cost management, reduction in expatriate staff and efficiency in material sourcing). The group is looking at plant utilization to improve to 70% in FY20F from around 50% last year given further volume ramp-up and commencement of Trent 7000 fan case production in 4Q20.

Recommendation. Maintain **BUY** on UMW at unchanged sum-of-parts derived **TP of RM3.40**. Key catalysts: (1) A turnaround in group earnings from 3Q20 driven mainly by the automotive division (2) Potential launches of mass market/CKD SUV models (3) Commencement of Trent 7000 engine assembly in 4Q20. Key risk to our call is a second wave of the pandemic and a weaker than expected demand recovery.

Table 1: UMW Sum-of-Parts Valuation

Segments	FY21F net profit (RMm)	Valuation	Multiple (x)	Value (RMm)	Comments
Automotive	266	PER	10	2,656	
Equipment	58	PER	10	577	
Serendah land		RNAV		558	RNAV of Serendah land (791acres@RM16psf) (net of debt)
Aerospace		DCF		133	Equity NPV of 25-year Rolls Royce contract (WACC: 8.7%)
Non-listed O&G		PBV		26	50% discount to Net Book Value
Total value				**3,951**	
No of shares (m)				1,168	
Fair value (RM)				**3.40**	

Source: Company, MIDFR

Income Statement (RMm)	FY17	FY18	FY19	FY20F	FY21F
Revenue	**11,046.5**	**11,306.3**	**11,739.1**	**11,229.8**	**11,494.6**
Operating expenses	(10,926.1)	(10,783.4)	(11,513.6)	(11,118.1)	(11,284.3)
EBIT	**120.4**	**522.9**	**332.6**	**111.7**	**210.3**
Net interest expense	(39.2)	(88.1)	(125.9)	(106.4)	(119.0)
Associates	171.7	265.6	291.6	261.2	271.6
PBT	**252.9**	**786.2**	**754.8**	**266.5**	**362.9**
Taxation	(122.3)	(142.5)	(108.7)	(1.3)	(22.8)
Minority Interest/PERP	(22.8)	139.9	174.3	79.2	115.0
Net profit	(651.2)	341.7	454.4	186.0	225.1
Core net profit	**163.8**	**341.7**	**266.3**	**186.0**	**224.1**
Consensus net profit	*80.0*	*433.4*	*339.2*	*216.1*	*278.2*
MIDF vs. consensus				*-14.0%*	*-19.4%*

Balance Sheet (RMm)	FY17	FY18	FY19	FY20F	FY21F
Non-current assets	**4,833.8**	**5,391.2**	**5,504.9**	**5,980.8**	**6,441.8**
PPE	2,658.1	2,820.9	2,756.8	2,971.5	3,160.8
Investments in associate	1,661.5	1,792.4	1,866.4	2,127.6	2,399.2
Others	514.2	777.9	881.8	881.8	881.8
Current assets	**5,261.9**	**5,366.8**	**5,642.9**	**5,281.3**	**5,103.8**
Inventories	1,410.7	1,548.5	1,589.6	1,783.0	1,825.0
Receivables	1,029.1	960.4	1,243.0	1,105.8	1,131.9
Others	1,658.6	1,546.1	1,338.3	1,338.3	1,338.3
Cash & equivalent	1,163.4	1,311.8	1,472.1	1,054.3	808.6
TOTAL ASSETS	**10,095.7**	**10,758.0**	**11,147.8**	**11,262.1**	**11,545.6**
Share capital	584.1	584.1	584.1	584.1	584.1
Minority Interest	1,131.2	2,369.8	2,401.7	2,411.1	2,456.2
Reserves	2,463.1	2,760.5	3,108.5	3,257.3	3,437.4
TOTAL EQUITY	**4,178.4**	**5,714.4**	**6,094.4**	**6,252.6**	**6,477.8**
Non-current liabilities	**2,264.4**	**2,548.3**	**2,435.6**	**2,435.7**	**2,435.9**
Long-term borrowings	2,069.7	2,298.2	2,123.4	2,123.6	2,123.7
Deferred tax liabilities	34.0	26.9	39.1	39.1	39.1
Others	160.7	223.2	273.1	273.1	273.1
Current liabilities	**3,652.9**	**2,495.3**	**2,617.9**	**2,573.9**	**2,631.9**
Short-term borrowings	685.3	534.5	386.4	386.4	386.4
Payables	2,795.5	1,854.0	2,093.4	2,134.8	2,185.1
Others	172.0	106.7	138.1	52.7	60.4
TOTAL LIABILITIES	**5,917.3**	**5,043.6**	**5,053.4**	**5,009.6**	**5,067.8**

Cash Flow Statement (RMm)	FY17	FY18	FY19	FY20F	FY21F
Operating activities					
PBT	109.5	619.8	547.8	266.5	362.9
Depreciation & Amortization	105.1	281.9	346.2	338.3	364.6
Chgs in working capital	1,124.6	(950.0)	(63.1)	(54.7)	(10.1)
Interest expense	(175.9)	(74.6)	(130.6)	(106.4)	(119.0)
Tax paid	(131.9)	(138.8)	(64.5)	(1.3)	(22.8)
Others	(585.9)	436.0	(357.3)	(203.8)	(152.6)
CF from Operations	**445.6**	**174.4**	**278.4**	**238.5**	**423.1**
Investing activities					
Capex	(1,003.8)	(914.7)	(345.5)	(700.0)	(700.0)
Others	(976.7)	596.0	837.0	147.0	146.0
CF from Investments	**(1,980.5)**	**(318.7)**	**491.5**	**(553.0)**	**(554.0)**
Financing activities					
Dividends paid	(75.9)	(6.2)	(70.6)	(37.2)	(45.0)
Net proceeds in borrowings	176.0	104.1	480.2	0.2	0.2
Others	0.0	921.3	(992.4)	(69.9)	(69.9)
CF from Financing	**100.1**	**1,019.2**	**(582.8)**	**(106.9)**	**(114.7)**
Net changes in cash	**(1,434.8)**	**874.9**	**187.1**	**(421.4)**	**(245.6)**
Beginning cash	1,607.3	1,181.5	1,315.2	1,475.6	1,054.3
Overdrafts & Deposits	176.6	(741.1)	(26.7)	0.0	0.0
Ending cash	**1,187.9**	**1,315.2**	**1,475.6**	**1,054.3**	**808.6**

Ratios	FY17	FY18	FY19	FY20F	FY21F
Revenue growth	8.7%	-11.4%	22.0%	-5.7%	2.4%
EBIT growth	-6.0%	67.6%	-24.0%	-71.3%	88.3%
Core net profit growth	-140.8%	108.6%	-22.1%	-30.2%	20.5%
PBT margin	2.3%	7.0%	6.4%	2.4%	3.2%
Core net profit margin	1.5%	3.0%	2.3%	1.7%	1.9%
ROE	2.2%	11.0%	8.0%	4.9%	5.7%
ROA	2.1%	4.9%	3.5%	1.0%	1.8%
Net gearing (%)	38.1%	26.6%	17.0%	23.3%	26.3%
Book value/share (RM)	2.61	2.86	3.16	3.29	3.44
PBV (x)	1.11	1.01	0.91	0.88	0.84
EV/EBITDA (x)	12.1	6.2	6.0	10.7	8.8
EBIT margin	1.1%	4.6%	2.8%	1.0%	1.8%

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (197501002077 (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 >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% 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.