

26 November 2020

Consumer Cyclical | Auto & Autoparts

UMW (UMWH MK)

Neutral (Maintained)

Long-Term Prospects Remain Uncertain

Target Price (Return): MYR2.65 (-1%)
Price: MYR2.68
Market Cap: USD766m
Avg Daily Turnover (MYR/USD) 1.17m/0.28m

- **NEUTRAL, with new MYR2.65 TP from MYR2.40, 1% downside.** 3Q20 core earnings of MYR80m exceeded expectations, largely attributed to stronger-than-expected Perodua sales and margins improvement from cost optimisation initiatives. However, we believe intense competition in the local automotive market is likely to limit UMW's earnings growth ahead. The equipment unit's earnings should only witness a pick-up once material progress in construction activities is seen. The aerospace wing is unlikely to recover from COVID-19's impact anytime soon.
- **UMW's 3Q20 exceeded our and Street's expectations,** with core net profit of MYR80m (-22.6% YoY, 2Q20: MYR33.2m core net loss), which brought 9M20 core earnings to MYR95.5m (-60% YoY). The positive variance was mainly on higher-than-expected Perodua sales during the quarter. UMW's optimisation is also bearing fruit, as margins improved during the quarter, especially for the equipment and manufacturing & engineering (M&E) divisions (Figure 2). No dividend was declared.
- **The automotive unit's earnings have recovered** from 2Q20's decline, bolstered by the sales tax exemption. Toyota/Lexus and Perodua recorded sales volumes of 18,870 units (+13.5% YoY, >100% QoQ) and 70,842 units (+24.3% YoY, >100% QoQ) in 3Q20. We do not expect the recently announced Toyota Vios and Yaris facelifts to provide material boosts to earnings, given the recent introduction of the all-new Nissan Almera and Honda City, which are likely to get more attention from prospective buyers. Perodua's D55L is on track for introduction in early 2021. Management remains tight-lipped on details of the Toyota SUVs that should be in the pipeline for 2021.
- **Both equipment and M&E divisions' 3Q20 earnings improved sequentially,** as businesses headed for normalisation. Notably, margins for both segments improved on cost-optimisation initiatives done by the group, eg sharing services among operating units and managing receivables/payables better. However, near-term heavy equipment demand is likely to remain weak, at least until we see a material pick-up in pump-priming activities, ie public spending on mega projects. UMW managed to secure new order for its aerospace wing, but we believe these orders will not be sufficient to offset the reduced ones from Rolls-Royce.
- **Forecasts.** We increase FY20F-22F earnings by 46%, 11%, and 9% after imputing higher Perodua sales (Figure 3).
- **Maintain NEUTRAL with higher TP of MYR2.65** based on an unchanged 13x FY21F P/E. Intense competition in the local automotive market is likely to limit earnings growth. UMW's share price looks fairly valued, trading close to the 12x P/E sector average.
- **Risks.** A resurgence of COVID-19 cases may affect all segments' earnings, while stiff competition in the automotive sector might exert downwards pressure on the bottomline.

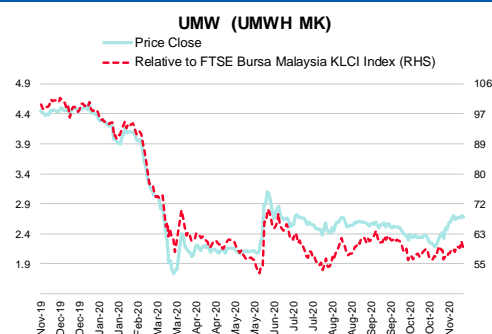
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(40.3)	13.1	3.9	27.6	(41.5)
Relative	(40.9)	6.2	1.2	16.4	(41.9)
52-wk Price low/high (MYR)				1.74	4.57



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (MYRm)	11,304	11,739	9,045	10,452	11,210
Recurring net profit (MYRm)	308	259	152	238	278
Recurring net profit growth (%)	6.6	(16.0)	(41.4)	56.9	16.6
Recurring P/E (x)	10.15	12.08	20.62	13.14	11.27
P/B (x)	0.9	0.8	0.8	0.8	0.8
P/CF (x)	na	5.88	4.42	8.78	7.47
Dividend Yield (%)	2.8	2.2	2.2	2.2	2.2
EV/EBITDA (x)	74.84	5.40	5.44	4.32	4.26
Return on average equity (%)	10.7	9.3	5.9	8.0	8.7
Net debt to equity (%)	26.6	17.0	4.5	6.5	7.5

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

Financial Exhibits

Asia	Financial summary (MYR)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Malaysia	Recurring EPS	0.26	0.22	0.13	0.20	0.24
Consumer Cyclical	DPS	0.08	0.06	0.06	0.06	0.06
UMW	BVPS	2.86	3.16	3.24	3.36	3.50
UMWH MK	Return on average equity (%)	10.7	9.3	5.9	8.0	8.7
Neutral						
	Valuation metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Recurring P/E (x)	10.15	12.08	20.62	13.14	11.27
	P/B (x)	0.9	0.8	0.8	0.8	0.8
	FCF Yield (%)	(75.9)	6.0	9.8	(1.4)	0.6
	Dividend Yield (%)	2.8	2.2	2.2	2.2	2.2
	EV/EBITDA (x)	74.84	5.40	5.44	4.32	4.26
	EV/EBIT (x)	11.90	11.02	15.52	8.34	7.74
	Income statement (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total turnover	11,304	11,739	9,045	10,452	11,210
	Gross profit	3,109	3,228	2,487	2,874	3,083
	EBITDA	53	679	522	689	724
	Depreciation and amortisation	282	(346)	(339)	(332)	(325)
	Operating profit	335	333	183	357	399
	Net interest	(13)	(58)	(44)	(71)	(72)
	Pre-tax profit	593	567	379	547	609
	Taxation	(124)	(109)	(72)	(104)	(116)
	Reported net profit	344	329	222	308	348
	Recurring net profit	308	259	152	238	278
	Cash flow (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Change in working capital	(1,104)	(169)	370	(90)	(48)
	Cash flow from operations	(1,460)	533	708	357	419
	Capex	(915)	(346)	(400)	(400)	(400)
	Cash flow from investing activities	(431)	394	(232)	(232)	(232)
	Dividends paid	0	(88)	(70)	(70)	(70)
	Cash flow from financing activities	(145)	(518)	1,273	(140)	(248)
	Cash at beginning of period	1,163	1,312	1,472	3,706	3,661
	Net change in cash	(2,036)	409	1,750	(15)	(60)
	Ending balance cash	(1,187)	1,738	3,238	3,708	3,618
	Balance sheet (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total cash and equivalents	1,312	1,472	3,706	3,661	3,571
	Tangible fixed assets	2,821	2,757	2,266	2,334	2,409
	Total investments	2,069	2,130	2,370	2,631	2,913
	Total assets	10,758	11,148	12,105	12,702	13,138
	Short-term debt	534	386	386	386	386
	Total long-term debt	2,298	2,123	3,600	3,700	3,700
	Total liabilities	5,044	5,053	5,836	6,160	6,280
	Total equity	5,714	6,094	6,268	6,542	6,857
	Total liabilities & equity	10,758	11,148	12,105	12,702	13,138
	Key metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Revenue growth (%)	2.1	3.9	(22.9)	15.6	7.3
	Recurrent EPS growth (%)	6.6	(16.0)	(41.4)	56.9	16.6
	Gross margin (%)	27.5	27.5	27.5	27.5	27.5
	Operating EBITDA margin (%)	0.5	5.8	5.8	6.6	6.5
	Net profit margin (%)	3.0	2.8	2.5	2.9	3.1
	Dividend payout ratio (%)	25.5	21.3	31.6	22.7	20.1
	Capex/sales (%)	8.1	2.9	4.4	3.8	3.6
	Interest cover (x)	3.41	2.64	1.64	2.57	2.84

Source: Company data, RHB

Results At a Glance

Figure 1: Earnings review

FYE Dec (MYRm)	3Q19	2Q20	3Q20	QoQ (%)	YoY (%)	9M19	9M20	YoY (%)	Comments
Revenue	2,882.7	1,529.7	2,663.3	74.1	(7.6)	8,623.5	6,312.3	(26.8)	All segments revenue improved as businesses heads for normalisation
EBIT	80.1	31.2	60.2	92.7	(24.8)	257.5	141.6	(45.0)	
<i>EBIT margin (%)</i>	<i>2.8</i>	<i>2.0</i>	<i>2.3</i>			<i>3.0</i>	<i>2.2</i>		
Finance costs	(30.8)	(30.1)	(26.5)	(11.8)	(13.7)	(93.3)	(86.4)	(7.4)	
Associates	85.2	(26.9)	94.3	<100	10.6	227.0	96.5	(57.5)	In line with stronger Perodua sales volume
Investment income	15.7	12.2	10.3	(15.2)	(34.3)	51.9	40.5	(22.0)	
Pre-tax profit	150.3	(13.6)	138.3	nm	(8.0)	443.1	192.1	(56.6)	
<i>Pre-tax margin (%)</i>	<i>5.2</i>	<i>(0.9)</i>	<i>5.2</i>			<i>5.1</i>	<i>3.0</i>		
Tax	(21.0)	4.7	(41.9)	nm	99.6	(86.8)	(51.4)	(40.7)	
<i>Eff tax rate (%)</i>	<i>(14.0)</i>	<i>(34.8)</i>	<i>(30.3)</i>			<i>(19.6)</i>	<i>(26.8)</i>		
MI	(20.9)	10.5	(16.3)	nm	(21.9)	(67.0)	(10.4)	(84.5)	
Core net profit	103.3	(33.2)	80.0	nm	(22.6)	239.1	95.5	(60.0)	Above our and consensus expectations
<i>Net margin (%)</i>	<i>3.6</i>	<i>(2.2)</i>	<i>3.0</i>			<i>2.8</i>	<i>1.5</i>		

Source: Company data, RHB

Figure 2: Earnings review – segmental breakdown

FYE Dec (MYRm)	3Q19	2Q20	3Q20	QoQ (%)	YoY (%)	9M19	9M20	YoY (%)	Comments
Automotive	2,296.9	1,102.0	2,127.5	93.1	(7.4)	6,845.9	4,815.5	(29.7)	Toyota reported higher sales volume
Equipment	353.7	233.2	297.0	27.3	(16.0)	1,080.1	819.4	(24.1)	
Manufacturing & engineering	252.4	183.3	242.3	32.1	(4.0)	734.0	674.1	(8.2)	Businesses were allowed to reopen
Others	(20.3)	11.1	(3.4)	<100	(83.1)	(36.6)	3.3	<100	in 3Q20
Revenue	2,882.7	1,529.7	2,663.3	74.1	(7.6)	8,623.5	6,312.3	(26.8)	
Automotive	140.1	(41.7)	131.6	nm	(6.1)	415.4	143.6	(65.4)	
Equipment	30.8	24.6	34.0	38.1	10.6	108.4	84.4	(22.1)	
Manufacturing & engineering	15.4	8.0	20.3	>100	32.4	30.9	38.8	25.6	
Others	(35.9)	(54.3)	(26.4)	51.4	26.5	(111.6)	(103.1)	(7.7)	
PBT	150.3	(63.3)	159.5	(351.9)	6.1	443.1	163.8	(63.0)	
PBT Margins									
Automotive	6.1	(3.8)	6.2			6.1	3.0		
Equipment	8.7	10.6	11.5			10.0	10.3		Margin improved thanks to the group's cost optimisation initiatives
Manufacturing & engineering	6.1	4.4	8.4			4.2	5.8		
Others	>100	<100	>100			>100	<100		
	5.2	(4.1)	6.0			5.1	2.6		
Automotive	104.4	(17.4)	94.6	nm	(9.4)	292.4	127.7	(56.3)	
Equipment	23.2	21.0	24.3	15.7	5.0	82.2	61.0	(25.8)	
Manufacturing & engineering	9.1	7.8	9.7	24.6	7.1	12.6	24.1	90.6	
Others	(33.3)	(10.6)	(48.0)	>100	44.1	(113.3)	(82.5)	(27.2)	
Less: Profit attributable to holders of perpetual sukuk	0.0	(34.1)	(0.7)	nm	nm	(34.8)	(34.8)	0.0	
NP	103.3	(33.2)	80.0	340.6	(22.6)	239.1	95.5	(60.0)	
NP Margins									
Automotive	4.5	(1.6)	4.4			4.3	2.7		
Equipment	6.6	9.0	8.2			7.6	7.4		
Manufacturing & engineering	3.6	4.3	4.0			1.7	3.6		
Others	>100	(95.4)	>100			>100	<100		
	3.6	(2.2)	3.0			3.2	2.1		

Source: Company data

Figure 3: Forecast assumptions

FYE Dec	2016	2017	2018	2019	2020F	2021F	2022F
Toyota / Lexus (units)	65,110	70,474	66,562	70,009	55,000	65,000	70,000
Perodua (units) - current	207,110	204,887	227,243	240,341	223,000	235,000	245,000
Perodua (units) - previous					200,000	214,000	225,000
FX (JPY/MYR)*	3.82	3.85	3.65	3.80	4.00	4.00	4.00
FX(USD/MYR)*	4.14	4.30	4.04	4.14	4.23	4.03	4.03
*Average rate							

Source: RHB

Figure 4: UMW vehicle sales summary

FYE Dec (units)	3Q19	2Q20	3Q20	QoQ (%)	YoY (%)	9M19	9M20	YoY (%)
Toyota/Lexus	16,628	7,886	18,870	139.3	13.5	48,151	37,339	(22.5)
- Passenger	12,313	6,040	14,965	147.8	21.5	36,253	28,746	(20.7)
- Commercial	4,315	1,846	3,905	111.5	(9.5)	11,898	8,593	(27.8)
Perodua	56,972	29,193	70,842	142.7	24.3	178,754	145,012	(18.9)
- Passenger	56,972	29,193	70,842	142.7	24.3	178,754	145,012	(18.9)
- Commercial	0	0	0	0.0	0.0	0	0	0.0
Total	73,600	37,079	89,712	141.9	21.9	226,905	182,351	(19.6)



Source: Malaysian Automotive Association

Figure 5: Operational updates and outlook – automotive segment

Expansion of model line-up – to appeal to a wider audience	Provide innovative financing packages to potential customers	Expansion of sales network into e-commerce
<ul style="list-style-type: none"> Improved Alphard and Vellfire (9 Mar), all-new Lexus UX 200 (4 Mar), all-new Toyota RAV4 (18 Jun) and improved Toyota Hilux (8 Oct) were launched. Order taking has started for the newly-revised Toyota Yaris (2 Nov) and Toyota Vios (16 Nov). More new models planned for 2021. 	<p>In partnership with Toyota Capital and other financial institutions.</p>	<p>Toyota Malaysia Flagship Stores via Lazada and Shopee – to ease purchase of vehicles as well as value for money deals.</p>



Source: Company

Figure 6: Operational updates and outlook – industrial segment

 INDUSTRIAL EQUIPMENT	 HEAVY EQUIPMENT
<ul style="list-style-type: none"> Diversify product base Support customers during recovery period - to reduce operating cost <ul style="list-style-type: none"> Flexible short-term rental Special discount on maintenance services and spare parts Leverage on potential increased trade - especially export-based manufacturing industries 	<ul style="list-style-type: none"> Ride on the rebound in economic activity to seek new opportunities <ul style="list-style-type: none"> Securing tender for infrastructure projects in Malaysia and Myanmar. Strong gold prices to spur demand in PNG Close collaboration with Komatsu for support and to enhance competitiveness

Source: Company

Figure 7: Operational updates and outlook – M&E segment

	AEROSPACE		AUTO COMPONENTS & LUBRICANTS
<ul style="list-style-type: none"> • Maiden delivery of Trent 7000 fan case in October 2020 <ul style="list-style-type: none"> ▪ Continues to receive orders for fan cases albeit slightly lower numbers. • Fully utilise existing aerospace capabilities <ul style="list-style-type: none"> ▪ Considering expanding existing aerospace capabilities involving parts machining into non-aero machining works. • Product diversification - active on-going discussions with OEM for manufacturing of new products. • Collaborate with existing MROs to increase local content 		<ul style="list-style-type: none"> • Leveraging on the sales tax exemption for the automotive industry <ul style="list-style-type: none"> ▪ Rising demand in OEM and REM markets. ▪ Lubricant plant running almost at full capacity since September 2020. • Completion of KYB-UMW plant expansion and modernization <ul style="list-style-type: none"> ▪ Additional 20% capacity as well as improved logistics and plant efficiency. • Lubricants - to continue to leverage on its OEM partners <ul style="list-style-type: none"> ▪ To strengthen domestic sales and export to ASEAN countries. 	

Source: Company

Figure 8: 9M20 exceptional items

	RM million	Remarks
Reported PATAMI	67.2	Includes distribution to Perpetual Sukuk holders of RM34.8 million in April 2020.
*ADJUSTMENTS	Amount recognised in PATAMI	
Reversal of impairment on receivables	(31.7)	Debt recovery from an earlier investment.
Reversal of impairment on PPE	(0.02)	-
Loss on sale on investment (net)	27.9	Crystallisation of forex loss on divestment of a company in Unlisted O&G.
Net gain on disposal of PPE not relating to business operations	(1.6)	Excluding RM15.3 million, which is mainly sale of leased asset in the Equipment segment.
Share of results from Toyota Capital Malaysia (TCM)	33.8	<ul style="list-style-type: none"> • Share of results from TCM in 3Q20 was RM10.3 million, reducing the share of losses in 9M20 to RM33.8 million. • The losses in 1H20 were due to present value impact of loan moratorium and unfavourable mark-to-market value of interest rate swaps. • The provision of the impact of loan moratorium, was fully recognised in 2Q20.
CORE PATAMI	95.6	

Source: Company

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-08-28	Neutral	2.40	2.60
2020-06-08	Neutral	2.65	2.89
2020-03-27	Neutral	2.40	2.34
2020-02-28	Sell	2.90	3.16
2019-11-29	Neutral	4.45	4.37
2019-11-18	Neutral	4.60	4.47
2019-08-28	Neutral	5.30	5.01
2019-05-23	Neutral	5.75	5.28
2019-02-28	Neutral	6.20	5.80
2019-01-07	Neutral	5.85	5.45
2018-12-03	Buy	5.70	5.40
2018-10-30	Buy	5.59	4.69

Source: RHB, Bloomberg

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