12 October 2016 | Sector Update

Automotive

***Maintain* NEUTRAL**

First Car Buyer Scheme

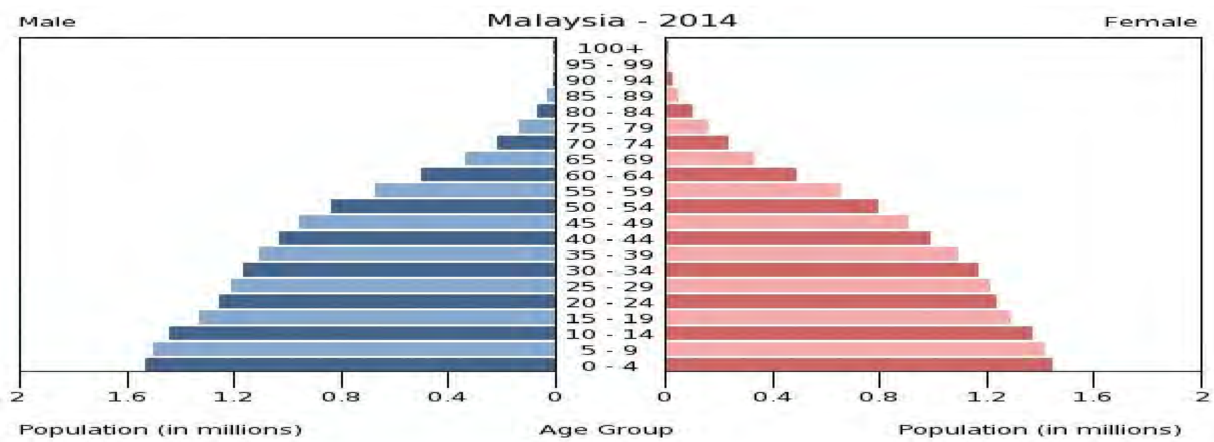
INVESTMENT HIGHLIGHTS

- **Newsflows suggest possible First Car Buyer Scheme under Budget 2017**
- **Likely to create temporary momentum, especially for non-national B-segment models**
- **UMW, Tan Chong among potential beneficiaries (pending details) if scheme materialises**
- **Maintain NEUTRAL on autos, Berjaya Auto (BUY, TP: RM2.50/share) is still our top sector pick**

Latest newsflows suggest possible 1st Car Buyer Scheme. Recent newsflows are suggesting that a 1st Car Buyer Scheme will be implemented under Budget 2017. The scheme is said to involve excise duty exemption for selective locally assembled cars with a cap on engine capacity. It is also said that the customs will determine the list of cars that will benefit from the scheme. Since the scheme looks likely to be borne by the Government, it basically means the Government will have to forgo some of its revenue from import/excise duties. Revenues from import /excise duties is estimated to account for only around 1.4% of Government revenues, but 75% of total tax collection from vehicle sales come from excise duties, i.e. around RM7.3b back in 2013. At an estimated RM15,000-RM18,000 per car however, the spending is likely to be higher than Thailand's THB100,000 (RM10,000) per car for its First Car Buyer Scheme back in 2012.

Will it have an impact on sales? The straight answer is yes, it will almost definitely have a positive impact on sales, particularly if the scheme is offered only for a limited period of time, which will essentially bring forward future sales. The Malaysian population age distribution leans significantly towards the younger generation (which is likely to be the main target market for this scheme) with the 15-24 years age group accounting for 16% (or 5.2m) of the population and the 21-54 years age group accounting for 41% of the population (See Exhibit 1). Generally, the idea looks good as it is a targeted scheme to just first car buyers and limits the increase in household debt. However, the buyer pool may expand to indirect buyers, e.g. parents who are buying for their children (or probably use their "car-less" kids' or siblings' name to purchase a car under the scheme), which is when the targeting element loses some effectiveness.

EXHIBIT 1: MALAYSIAN POPULATION DISTRIBUTION LEANS HEAVILY TOWARDS YOUNG AGE GROUP

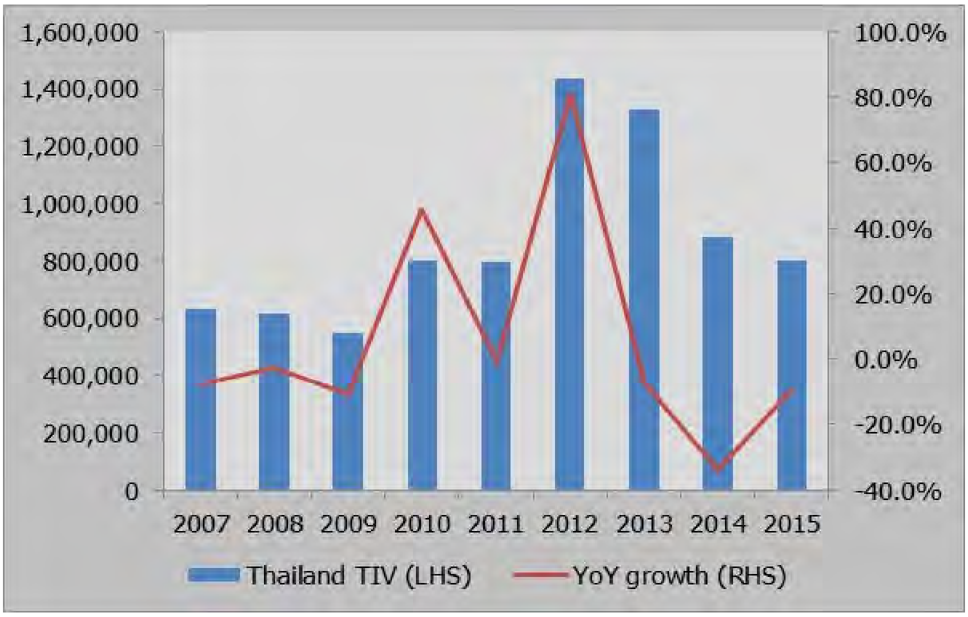


Source: CIA World Factbook, MIDFR

Who are the potential beneficiaries? Locally assembled models with low localisation rates will benefit the most from the excise duty exemption and will likely see the most price cuts effectively, if all the duty savings are passed on to the consumer. Assuming the scheme limits engine capacity at just 1.5-litre, the non-national B-segment models are likely to benefit the most. The Vios is likely to be one of the biggest beneficiaries given low localisation rate of 50%-55%. The Almera and the City entails up to 65%-70% localization rate to our understanding. The national A/B segment makes on the other hand, already entail very high localisation rate of 80%-95% suggesting little room for significant cost savings from excise duty exemptions. We estimate excise duty paid for the Vios at around RM15,000-RM18,000/car – which is likely to be the savings for consumers if all of this is passed on, to give an illustration. This translates into circa 18%-20% in effective price reduction. More importantly, the A/B segments account for >50% of TIV, meaning a targeted buying scheme for this segment is likely to sway overall industry volumes.

Lesson from the past. Thailand adopted a First Car Buyer (FCB) Scheme back in 2012. The FCB scheme entailed tax refunds of up to THB100,000 (circa RM10,000 equivalent back then) for first time car buyers that bought Eco Car qualified models and was meant to drive Thailand's then, new green car program and more importantly to revive Thailand's auto market which was devastated by the big floods in 2011. The Eco Car program is the equivalent of Malaysia's Energy Efficient Vehicle program but with a rigid target segment and differing incentives. Thailand spent a total of USD2.5b for the program, according to World Bank Estimates, benefitting some 1.2m Thai car buyers. Thailand's scheme was strictly targeted towards new car buyers, but nonetheless helped to drive Thailand's TIV growth by 81% in 2012 to 1.4m units, while auto production grew by 68% during the period (See Exhibit 3).

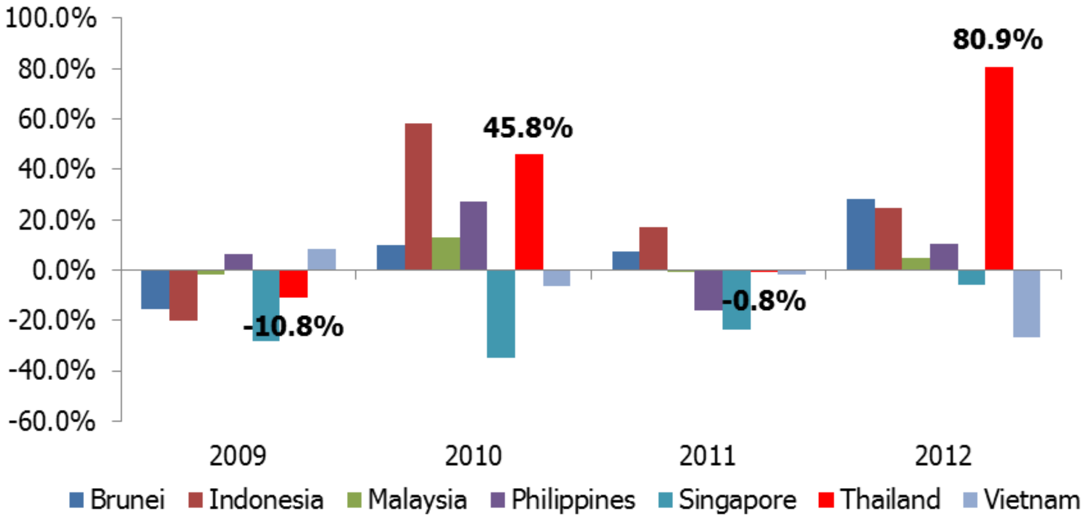
EXHIBIT 2: TEMPORARY BOOST TO THAILAND'S TIV GROWTH FROM FIRST CAR BUYER SCHEME



Source: AAF, MIDFR

The scheme comes with risks. The 1st Car Buyer Scheme is likely to create a temporary momentum in car sales, but once it ends, will result in a sharp drop in volumes and an overhang in the market, similar to what happened in Thailand when their 1st car buyer scheme ended (See Exhibit 2). Thailand also saw massive defaults on loan instalments for buyers under the scheme (anywhere between 100,000-200,000 buyers). Even worse, the large number of loan defaults meant that manufacturers and 2nd hand dealers had to contend with finance companies overloaded with repossessed cars and ultimately, a loss of resale value for the cars.

EXHIBIT 3: CAR BUYER'S SCHEME BOLSTERED THAILAND'S TIV RECOVERY IN 2012 (YOY GROWTH)



Source: AAF, MIDFR

Maintain NEUTRAL on autos. Berjaya Auto (BUY, TP: RM2.50/share) is still our top sector pick: Key share price catalysts over the next 12 months: (1) Attractive dividend yield of 7% underpinned by solid net cash which accounts for 14% of market cap and strong FCFE yield of 10% (FY17F), (2) Further market share wins driven by new launches, i.e. the CKD Mazda 6 and diesel variants of the CX5, Mazda 2 and Mazda 6, (3) Recovery in manufacturing earnings (via 30%-owned Mazda Malaysia SB and 29%-owned Inokom) after the launch of the facelift CX5, and (4) Value unlocking from the potential listing of BAuto Philippines. Ex-cash, BAuto trades at just 10x CY17F earnings.

UMW remains a NEUTRAL at unchanged TP of RM5.30/share. UMW Oil & Gas will see further earnings pressure in 2H16 as the number of idle rigs has increased from 4 to 6 out of a total of 8 rigs. UMW's auto division should also see some weakness in 3Q16 as the impact of the new Hilux fizzles out while the run-out of several end-of-life models will impact margins negatively. Our forecast losses for FY16F/17F are below consensus' net profit estimates of RM217m/RM338m respectively.

Tan Chong also remains a NEUTRAL at unchanged TP of RM1.95/share. Tan Chong's balance sheet is increasingly stretched as a result of the demand downcycle but admittedly share price is already trading at depressed levels. Our forecast losses are below consensus' FY16F/17F net profit estimates of RM33m/RM51m respectively.

VALUATION AND RECOMMENDATION

		Shr Price	EPS (sen)		PE (x)		P/BV	ROE	Div Yield	Target	Total
Company	**Rating**	**(RM)**	**CY16 F**	**CY17 F**	**CY16 F**	**CY17F**	**(x)**	**(%)**	**(%)**	**Price (RM)**	**Upside (%)**
B.Auto	BUY	2.25	18.9	20.4	11.9	11.0	4.5	40.2	7.4	2.50	18.5
Tan Chong	NEUTRAL	1.84	-12.2	-12.1	-15.1	-15.3	0.5	-1.5	0.0	1.95	6.0
UMW	NEUTRAL	5.75	-10.5	-1.1	-54.6	-532.5	1.1	-0.2	0.5	5.30	-7.3
Sector average					***-19.3***	***-178.9***	***2.0***	***12.8***	***2.6***		

Source: Bloomberg, Companies, MIDFR

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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 *rise* 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 *fall* 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.