

18 July 2018 | Sector Update

## Automotive

**Maintain POSITIVE**

### *June TIV could test record levels*

#### **INVESTMENT HIGHLIGHTS**

- **June TIV could test record levels**
- **Key players such as Toyota may more than double sales on year-on-year basis**
- **Cautious of bottlenecks and post-tax holiday impact**
- **Bermaz Auto (BUY, TP: RM2.70/share) is our top pick for a solid 35% earnings CAGR and attractive 7% yield, followed by Tan Chong (BUY, TP: RM2.05), UMW (BUY, TP: RM7.11) and MBM (BUY, TP: RM3.20)**

**TIV could test record levels in June.** June TIV expected to be released this week could test record highs being the maiden month of the tax-free period up till mid-Sep 2018. For June, we expect key players such as UMW Toyota to stage a strong rebound given pent up demand (as consumers waited for 1<sup>st</sup> June to put in bookings) and as consumers also brought forward purchases into the 3.5 months of tax holiday period. We would not rule out Toyota TIV rising more than 5 times sequentially and more than doubling on a year-on-year basis. Our channel checks suggests that Mazda's waiting list exceeds 5 months (some of these might be cancelled if delivery is after mid-Sep 2018 we think), while some distributors have already suspended bookings for selective high volume models. For Perodua however, we expect sales volume to contract sequentially as sales in May was inflated given a pre-tax holiday GST rebate by Perodua from mid-May 2018.

**Consumers held back purchases in May.** To recap, following the announcement in mid-May of the tax holiday from 1<sup>st</sup> June till mid-Sep, consumers held back purchases to take advantage of the GST/SST free period. Several players offered to absorb GST even prior to the actual zero-rated GST implementation but this was insufficient to entirely fill the vacuum. May sales fell 9%mom and 15%yoy to 42,983 units.

**Players that absorbed GST gained share.** Notably, players that bucked the trend in May18 were those that offered to absorb GST up till 31<sup>st</sup> May, before actual GST/SST free period commenced from 1<sup>st</sup> June. While these players gained market share, 2Q18 margins are likely to be slightly impacted. Among the key gainers were Perodua, Proton, Honda and Nissan, with the latter registering the strongest volume growth of 30%mom. Tan Chong has abundant old stock of the Almera and it may take advantage of the surge in demand to clear these off.

**Short notice to meaningfully ramp up production?** Industry production (TIP) did not show any meaningful spike in May, but we expect the numbers to increase in the post-Raya period. Our checks with players suggest there has been a pre-Raya production ramp-up (to meet the typical surge in demand prior to Raya) but in mid-June, plants are typically closed up to 2 weeks during Raya for annual maintenance. Nonetheless, for select players (e.g. Mazda), there is the possibility of clawing back export volumes to meet the temporary surge in domestic demand, should there be a shortage in kit supply from Japan. Additionally, most of the key players have ample capacity to ramp-up production with the majority running on high rate single-shift. Production can easily be increased to double-shift, 2.5 shifts or stretching works days into the weekend to temporarily meet surging demand.

**Bottleneck risks.** Whilst demand will naturally increase tremendously over the tax holiday period, we would bear in mind the bottlenecks e.g. registration systems and banks' capacity to process and approve loans over this short 3.5-month period. Chances are, replacement buyers are likely to return to the market prematurely, and the market would dry up post Sept 15<sup>th</sup>.

**BAuto (TP: RM2.70) remains our top sector pick.** Key catalysts over the next 12 months:

- 1. An 11%yoy Mazda TIV growth** (FY19F) coupled with margin expansion driven by full year impact of new CX5 from 3QFY18 onwards
- 2. Ringgit strength** against the JPY
- 3. A more than doubling in associate earnings contribution** to group (via 30%-owned Mazda Malaysia SB and 29%-owned Inokom) given export market expansion to South East Asia (ex-Vietnam) and re-acceleration in production for the domestic market.
- 4. Launch of CBU CX8** in 2QCY18 and CKD variants in CY19F.
- 5. Attractive dividend yield of 7%** - net cash accounts for 10% of market cap coupled with solid 9% FCFE yield (FY19F). Our payout assumption is capped at 80% vs. historical 80%-113% payout.

**Our contrarian BUY on UMW (TP: RM7.11) is re-affirmed.** Key catalysts: **(1) A deleveraged balance sheet** post UMWOG demerger allows room for acquisitive growth and possible resumption of dividend payouts – successful acquisitions from PNB and MBM to increase Perodua stake are strong share price catalysts **(2) Reversal of prior years' market share loss**, structural cost reduction and pricing advantage from UMW Toyota's EEV-focused strategy **(3) Redevelopment of UMW's 830 acres Serendah land** which will unlock value of the asset – easily worth 40sen/share on our estimates **(4) A more than quadrupling of M&E division earnings** once its aerospace division reaches full scale production.

**MBM Resources (BUY, TP: RM3.20) is a cheap proxy to Perodua's** volume expansion and the spillover on its parts manufacturing and Perodua dealership units. With an attractive 39%yoy earnings growth (FY18F); all this for less than half of FY18F BV and on the back of a lean balance sheet (9% net gearing). Key catalysts: (1) Strong growth in Perodua TIV on the back of the new MyVi and potentially a new SUV to fill up a vacuum in its model mix (2) A stronger Ringgit (3) A recovery in industry production driven by new national car launches.

**Tan Chong is also our non-consensus BUY (TP: RM2.05)** as a deep value play into the sector's earnings recovery driven by the strong Ringgit and a bottoming in market share. Having seen share price fall some 40% in the past 24 months, Tan Chong now trades at just 0.4x FY18F PBV (which is lower than even its historical trough PBV of 0.5x) amid a potential turnaround in earnings over the next few years. Key catalysts include: (1) Resumption of new model launch in FY18F (2) Sustained Ringgit strength (3) Narrowing in losses from Indochina operations.

## EXHIBIT 4: MAY 2018 TIV SUMMARY

Marques	May-17	Apr-18	May-18	YoY	MoM	YTD17	YTD18	YTD %	Market share	
									May-17	May-18
Proton	7,176	3,999	4,091	-43.0%	2.3%	32,168	20,933	-34.9%	14.2%	9.5%
Perodua	17,211	19,939	21,980	27.7%	10.2%	81,854	97,487	19.1%	34.0%	51.1%
Toyota	6,072	5,517	2,027	-66.6%	-63.3%	28,393	20,227	-28.8%	12.0%	4.7%
Honda	9,153	7,708	8,046	-12.1%	4.4%	43,719	39,936	-8.7%	18.1%	18.7%
Nissan	2,650	1,570	2,038	-23.1%	29.8%	10,799	8,918	-17.4%	5.2%	4.7%
Mazda	900	1,127	616	-31.6%	-45.3%	3,970	5,182	30.5%	1.8%	1.4%
Others	7,438	7,229	4,185	-43.7%	-42.1%	33,283	32,529	-2.3%	14.7%	9.7%
<b>Total</b>	<b>50,600</b>	<b>47,089</b>	<b>42,983</b>	<b>-15.1%</b>	<b>-8.7%</b>	<b>234,186</b>	<b>225,212</b>	<b>-3.8%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: MAA, MIDF

## EXHIBIT 5: MAY 2018 TIV SUMMARY BY VEHICLE TYPE

Segment	May-17	Apr-18	May-18	YoY	MoM	YTD17	YTD18	YTD %
Passenger cars	45,139	41,982	40,221	-10.9%	-4.2%	210,410	203,299	-3.4%
Commercial vehicles	5,461	5,107	2,762	-49.4%	-45.9%	23,776	21,913	-7.8%
<b>Total</b>	<b>50,600</b>	<b>47,089</b>	<b>42,983</b>	<b>-15.1%</b>	<b>-8.7%</b>	<b>234,186</b>	<b>225,212</b>	<b>-3.8%</b>

Source: MAA, MIDF

## EXHIBIT 6: MAY 2018 TIV SUMMARY BY VEHICLE TYPE

Segment	May-17	Apr-18	May-18	YoY	MoM	YTD17	YTD18	YTD %	Market share	
									May-17	May-18
National cars	24,387	23,938	26,071	6.9%	8.9%	114,022	118,420	3.9%	48.2%	60.7%
Non-nationals	26,213	23,151	16,912	-35.5%	-26.9%	120,164	106,792	-11.1%	51.8%	39.3%
<b>Total</b>	<b>50,600</b>	<b>47,089</b>	<b>42,983</b>	<b>-15.1%</b>	<b>-8.7%</b>	<b>234,186</b>	<b>225,212</b>	<b>-3.8%</b>		

Source: MAA, MIDF

## VALUATION AND RECOMMENDATION

Companies	Rating	Shr Price (RM)	EPS (sen)		PE (x)		P/BV (x)	ROE (%)	Div Yield (%)	Target Price (RM)	Total Upside (%)
			CY18F	CY19F	CY18F	CY19F					
Bermaz Auto	BUY	2.25	16.7	20.1	13.4	11.2	4.9	35.2	7.1	2.70	27.1
Tan Chong	BUY	1.82	3.1	9.0	59.6	20.2	0.4	1.1	1.8	2.05	14.4
UMW	BUY	6.10	31.7	47.5	19.2	12.8	1.1	5.4	2.4	7.11	19.0
MBM	BUY	2.40	25.9	31.5	9.3	7.6	0.5	5.5	3.0	3.20	36.3
<b>Average</b>					<b>14.0</b>	<b>10.6</b>	<b>1.7</b>	<b>11.8</b>	<b>3.6</b>		

Source: Bloomberg, Companies, MIDF

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### 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 <i>rise</i> 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 <i>fall</i> 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.