Automotive

Stronger Recovery Drive Ahead

OVERWEIGHT
↑

By Wan Mustaqim Bin Wan Ab Aziz I wanmustaqim@kenanga.com.my

We upgrade our sector call to OVERWEIGHT (from NEUTRAL) following the re-opening of economic activities, and further driven by buoyant recovery in car sales as evident from the growing number of back-logged bookings for popular models (up to 6 months), with stream of new higher-margin models launched in 2022 (including models that were postponed from 2021). Positively, we expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Our 2022 TIV target at 600k units (+18%) is in line with MAA's 2022 TIV target.

The sector is currently trading at trailing 12x PER which is at a 25% discount to pre-pandemic mean of 16x PER. We expect profits in subsequent quarters to gradually normalise to pre-pandemic levels on the back of sector earnings growth of 22% in FY23 which should justify sector PER to gradually reverting closer to the mean.

We prefer players with industry leading market position, and sustainable high-margin profit models. We like MBMR (OP; TP: RM4.10) given their market leading position in the national marques space. We believe the player that benefits most from high-margin new launches is BAUTO (OP; TP: RM2.30) given that it's just added two new marques under its stable (Kia and Peugeot) with 18 new models including Mazda starting 4QCY21 until 2023.

Upgrade to OVERWEIGHT from NEUTRAL with unchanged 2022 TIV target of 600k units (+18%). The revision is driven by the re-opening of economic activities, and further boosted by buoyant recovery in car sales as evident from the growing number of back-logged bookings for popular models (up to 6 months), with stream of new higher-margin models launched in 2022 (including models that were postponed from 2021). Positively, we expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Our 2022 TIV target at 600k units (+18%) is in line with MAA's 2022 TIV target. Additionally, Battery Electric Vehicles (BEVs) new launches are expected to be boosted by full exemption on import & excise duties, sales tax, road tax, and individual tax relief of up to RM2,500 for the costs of purchase and installation as well as rental and subscription fees of EV charging facilities up to 31 December 2025 (for CKD and CBU up to 2023) to support development of the local EV industry. Nevertheless, for certain models, the recovery of car production could be limited by the on-going global constraint in semiconductor chips supply. Automakers have prioritized their usage of such resources, diverting any precious semiconductors they have to their most profitable vehicles such as full-size trucks and SUVs, as well as luxury vehicles. Malaysian Automotive Association (MAA) is vying for further SST exemption extension to end-2022 as the current chip shortages are limiting automakers' ability to maximise production capacity to meet back-logged demand which stretched up to 6 months for certain models. Our 2022 TIV target at 600k units (+18%) is in line with MAA's 2022 TIV target.

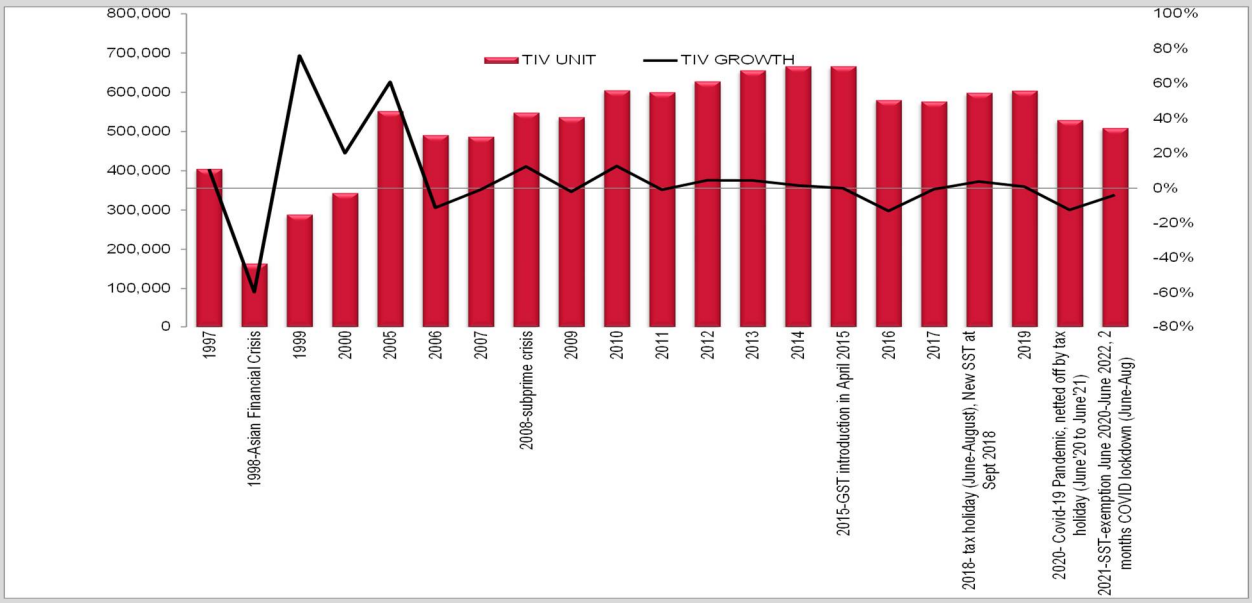
Discount to mean valuation is unjustified. The sector is currently trading at trailing 12x PER which is at a 25% discount to pre-pandemic mean of 16x PER. We expect profits in subsequent quarters to gradually normalise to pre-pandemic levels on the back of sector earnings growth of 22% in FY23 which should justify sector PER to gradually reverting closer to the mean.

Sustainable car sales despite the ending of SST-exempted period. We expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Current backlog as shared by the Ministry of Finance (MoF) is at 264,000 units which translated into 4 to 5 months delivery queue from the supply chain disruption (based on our target of 600,000 units) which could as well to drive the back-log orders up to 9 months. This also provides assurances to the automakers to fast-track their production level and safeguard their margin if there is a need to increase the car prices given the increase in auto parts procurement costs (final car prices is reflected in the final invoice, not during the booking).

Our sector top picks are MBMR and BAUTO. We like MBMR (OP; TP: RM4.10) for its: (i) deep value stake in 22.58%-owned Perodua, and (ii) dual-income streams as the largest Perodua dealer and spare parts supplier for most of the popular marques. We like BAUTO (OP; TP: RM2.30) as it offers: (i) one of the highest dividend yields in our auto universe coverage, and (ii) the highest PATAMI margin which is head and shoulders compared to peers.

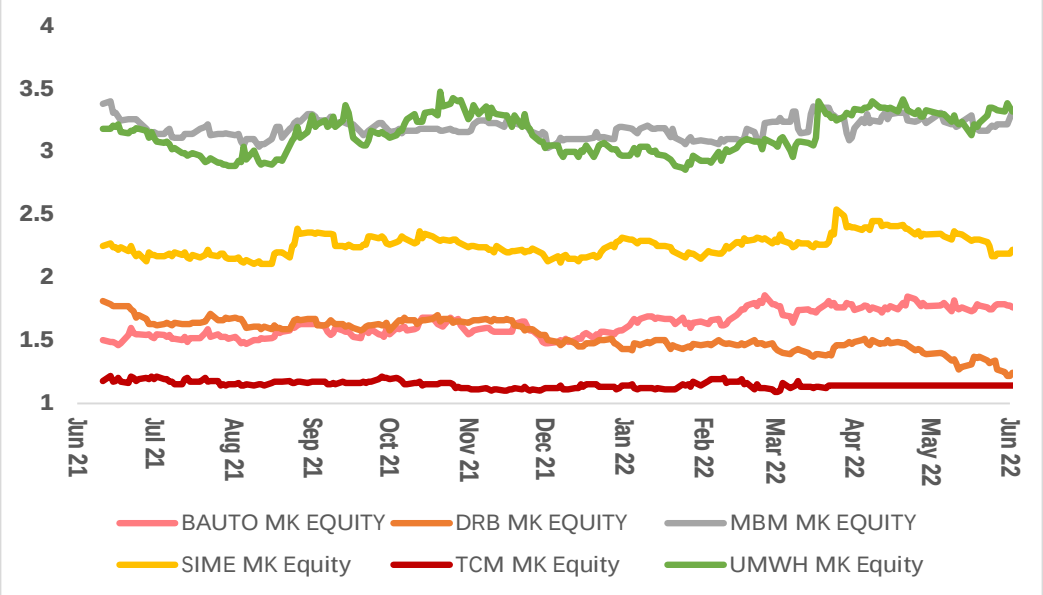
Risks to our sector rating are: (i) slower-than-expected recovery in production volume from the supply-chain disruption, (ii) lower-than-expected margin for companies under our coverage, and (iii) stricter government regulation on the automotive industry especially on excise duties calculation which could trigger pushing vehicles already selling at higher prices out of the affordable range.

Total Industry Volume from1997 to 2021



Source: MAA, Kenanga Research

Share Price Movement June 2021-June 2022



Source: MAA, Kenanga Research

TIV Market Share Movement

Position	Marques	4M22	4M21	Market Share	Sales	Comment
1st	Perodua	40%	39%	▲	11%	Driven by the all-new Axia, Myvi, and Ativa, shifting toward SUV.
2nd	Proton	16%	24%	▼	-28%	Driven by Proton X70 and further all-new X50, and PIES line-ups.
3rd	Toyota	14%	13%	▲	12%	The all-new Toyota Vios, all-new Toyota Yaris, and Toyota Hilux received overwhelming responses.
4th	Honda	12%	10%	▲	31%	Driven by all-new Honda City and HR-V 2021.
5th	Nissan	2%	2%	◄►	24%	Lack of new volume-driven model launches.
6th	Mazda	3%	2%	▲	35%	Driven by CX-5 and all-new CX-8.
National Marques		56%	63%	▼		Shift toward lower volume SUV for Perodua and boosted by Proton.
Non-national Marques		44%	37%	▲		Increasing new launches of updated volume driven models.

Source: MAA, Kenanga Research

Exciting New Launches

All-New Proton X50 (CKD)	2022 Toyota Vios
	
All-New Toyota Corrolla Cross Hybrid	**Face-lifted 2022 Perodua Myvi**
	
Mazda CX-30 CKD launching in Malaysia by 4Q22	**All-new Mazda MX-30 Electric-Q32022**
	
All-New 2022 Honda HR-V in July 2022	**2022 Honda City Hatchback - 1.5L i-VTEC, e:HEV RS hybrid early 2022**
	
Proton All-new SUV 7-seater- early 2023	**All-New Perodua D27A MPV/ Alza – June/July 2022**
	

Source: Various Sources

Valuation &Outlook

Company	TP (RM)	Calls	Valuation basis	Comments
BAUTO	2.30	OP	15x CY23E EPS on par with local peers' average 1-year Fwd. PER of 15x and at a 15% premium to its Japanese peers' average PER of 13x given its standing with one of the highest PAT margin among automakers (commanding an average of 8% compared to average PAT margin of both local and Japanese peers at 5%) which also translated to 5-year Fwd. historical mean PER.	**Exciting new launches ahead.** New Mazda launches are the all-new CX-3 IPM4 version (Jan 2022), CX-30 IPM4 version (Feb 2022), CX-8 IPM4 version (June 2022) and all-new Mazda MX-30 EV (3Q 2022). PEUGEOT's current line-ups are the 2008, 3008 and 5008 SUVs, while upcoming models are Landtrek (3Q 2022), 3008/5008 IPM version (July 2022), all new e-2008 EV CBU (4Q 2022), and 508 Electric Hybrid (in discussion). Kia's current line-ups for now is Carnival with upcoming models such as Sportage PHEV (3Q/4Q 2022, CKD 2023), EV6/PBV1 EV (4Q 2022), and all new Niro/Sorento (4Q 2022) (refer to image table overleaf).**We like the stock as it offers: (i) one of the highest dividend yields in our auto universe coverage, and (ii) the highest PATAMI margin which is head and shoulders compared to peers.**
DRBHCOM	1.80	OP	SoP valuation which implied PER of 13x on FY23E EPS, a discount of 13% to local peers' average 1-year Fwd. PER of 15x and on par with its Japanese peers' average PER of 13x given its standing close to 30% of Automotive industry market share through various associates shareholding with strategic stake in certain government contract.	**DRB-HICOM's automotive segment remains a driving force for the group's growth.** Proton and Honda are expected to chart stronger volume in 2022 with Proton striving for a target of 150,000 units (+34%) in 2022. The positive momentum is expected to continue with the extension of sales tax exemption for passenger vehicles until 30 June 2022 (with MAA vying for an extension to December 2022) and new launches ahead to fortify the group market share position. As the global economy gradually reopens further, aerospace and defence business are expected to gear up their production whilst staying flexible in meeting ever-changing customers' demands. For the postal segment, the on-going turnaround plan focusing primarily on rigorous cost efficiency and customer-centric strategy is expected to improve its overall performance. Other businesses in banking, services and properties will continue to operate efficiently by optimising cost management and improving business productivity. **We like the stock as it: (i) is driving on Proton with its highest volume growth and Honda with its sought-after range of vehicles earning the title affordable premium vehicles, and (ii) turnaround story from heavy losses to profit making in the next 2 years with proven volume growth and costs savings strategy.**
MBMR	4.10	OP	7x FY23E EPS is at a discount of 53% to local peers' average 1-year Fwd. PER of 15x and a discount of 46% with its Japanese peers' average PER of 13x given its business model was more toward dealerships in compared to others which have more shareholding towards automakers. This valuation also translated to -1.0 SD of 5-year forward historical mean PER.	**The largest Perodua dealership in Malaysia.** Perodua's market share is supported by higher delivery of all-new Myvi, all-new Perodua ARUZ, and the all-new ATIVA which provide better margins compared to the previous models. The group is cautiously optimistic on CY22 prospects with the continued strong demand for vehicles supported by favourable interest rates, continuation of sales tax exemption until 30 June 2022, and introduction of new models including electric vehicles (EV) under Volvo at more competitive prices with potential Hybrid model for Perodua in the making. **We like the stocks for its: (i) deep value stake in 22.58%-owned Perodua, and (ii) dual-income streams as the largest Perodua dealer and spare parts supply business for most of the popular marques**
SIME	2.60	OP	SoP valuation which implied PER of 15x on FY23E EPS, on par with local peers' average 1-year Fwd. PER of 15x and at a 15% premium to its Japanese peers' average PER of 13x given its exposure more towards international space where most of its automotive volume are from China and c.40% derived from industrials.	**Driven by global recovery**. Management noted that most of the group's operations are in countries/territories that are not subjected to significant movement restrictions and the recovery in motor vehicle sales has generally been strong despite minor setback in global supply chain that could limit sales due insufficient inventories of certain new models. Industrials segment is directly impacted by trade tensions with China on the mining sector in Australia which is likely to be manageable due to the robust coal demand from alternative markets in South Korea, Japan and elsewhere, while outlook for construction industry in New Zealand remains positive due to pent-up demand. China's fiscal stimulus to boost infrastructure investment which is expected to be rolled out in the near term to counter emerging economic challenges is seen to benefit its Industrial division. **We like the stocks for its: (i) diversified business operation driven by economic recovery, and (ii) major brands under its stable ensuring sustainable profit growth (such as BMW, Caterpillar).**
TCHONG	1.00	UP	0.24x FY22E BVPS (at -1.0SD to 5-year historical mean PBV).	**Running on fumes.** Despite the launching of the all-new Nissan Almera in November 2020, overall sales have remained weak, with only one model to drive the group. It is still uncertain at the moment whether this will prove to be the catalyst needed for TCHONG to strongly return to profitability, and to offset the negative impact from its under-utilised Danang plant in Vietnam and the expiration of both CBU and CKD agreements there with its principal on 30 September 2020 and 19 September 2020, respectively.

UMW	4.40	OP	13x FY22E EPS a discount of 13% to local peers' average 1-year Fwd. PER of 15x and on par with its Japanese peers' average PER of 13x given its close to 30% of automotive industry market share through various associates shareholding with strategic stake in certain government contract. This valuation also translated to -1.0 SD of 5-year forward historical mean PER.	**Driven by Automotive industry market share.** For Equipment division, the group will continue to leverage on its partners (KOMATSU & TICO)'s strengths and new collaborative robots ("Cobots")'s venture with Universal Robot A/S, while UMW Aerospace is expected to recover with the relaxation of travel restrictions. **We like the stock for its: (i) stream of new models such as Vios and face-lifted Yaris, Toyota RAV4 CBU, Lexus UX200, Toyota Hilux Rogue, Innova and Fortuner, Toyota Corolla Cross Hybrid, Harrier, and (ii) its 38%-owned Perodua with the launches of all-new Perodua Ativa, refreshed ARUZ, and the recent face-lifted Myvi**.

Source: Kenanga Research

Peer Comparison

Name	Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld(%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE																	
BERMAZ AUTO BHD	1.72	1,996.9	Y	04/2022	1.1%	10.1%	5.1%	14.4%	12.8	12.2	10.7	3.1	2.8	24.4%	4.9%	2.30	OP
DRB-HICOM BHD	1.14	2,203.6	Y	12/2022	29.5%	11.7%	-7.5%	35.4%	N.A.	11.3	8.4	0.2	0.2	2.1%	1.8%	1.80	OP
MBM RESOURCES BERHAD	3.17	1,239.2	Y	12/2022	33.7%	11.4%	16.5%	16.6%	7.4	6.3	5.4	0.6	0.5	8.7%	6.3%	4.10	OP
SIME DARBY BERHAD	2.16	14,690.2	Y	06/2022	5.0%	5.0%	3.9%	3.9%	12.9	12.4	11.9	0.9	0.9	7.2%	5.1%	2.60	OP
TAN CHONG MOTOR HOLDINGS BHD	1.14	766.1	N	12/2022	32.9%	10.2%	-31.3%	54.4%	N.A.	61.3	39.7	0.3	0.3	0.5%	2.6%	1.00	UP
UMW HOLDINGS BHD	3.09	3,610.0	Y	12/2022	7.1%	7.9%	60.5%	9.9%	16.2	10.1	9.2	0.5	0.5	4.9%	1.9%	4.40	OP
Simple Average					**18.2%**	**9.4%**	**7.9%**	**22.4%**	**12.3**	**18.9**	**14.2**	**0.9**	**0.9**	**8.0%**	**3.8%**		

Source: Bloomberg, Kenanga Research

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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KENANGA INVESTMENT BANK BERHAD (15678-H)
Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my