PP14767/09/2012(030761)

Monday, May 25, 2015

Market Access

Sime Darby Berhad

"Tough Business Conditions"

Results Review

- **Actual vs. expectations.** SIME Darby Berhad (SIME) 9M15 earnings performance was below our estimates as net earnings slid by 39% to RM1,324.1 million from RM2,159.8 million in 9M14. Disappointing net profit was caused by weaker-than-expected PBIT contribution from all divisions except for property division (+95% y-o-y) and energy and utilities division (+546% y-o-y), impacted by 1) weak CPO and PK prices; 2) lower FFB production in 9M15 that dropped by 6% y-o-y; 3) declining profit from midstream and downstream business due to lower off-take of biodiesel and lower sales volume and margin; and 4) lower equipment deliveries and margin realisation in the product support segment in Australasia as well as lower equipment and engine sales to the construction, mining and shipyard sectors. The Group recorded lower revenue of RM30.86 billion during the period compared to RM31.39 billion in 9M14.

- **Dividend.** No dividend has been proposed for this quarter.

- **Plantation division.** Plantation division posted lower revenue of RM6,849.5 million in 9M15 (9M14: RM7,670.1 million) due to lower FFB production during the period as FFB yield fell by 4.4% y-o-y due to a change in crop pattern as a result of delayed impact of adverse weather condition in Malaysia and Indonesia last year coupled with the dry weather during early 2015 in East Malaysia that run concurrently with seasonally low cycle during the period. However, we anticipate that SIME's FFB production may start to pick-up in the month of April 2015 as the sector moves into up cycle production month that normally experience in the month of April till October (April 2015 FFB production increase 10% q-o-q to 951,102 MT from 865,279 MT in March 2015). Of note, Malaysian estates recorded a lower FFB production of 4.26 million MT (-8% y-o-y) compared to Indonesian

HOLD (TP: RM9.00)

Current Price (RM)	RM8.96
New Target Price (RM)	**RM9.00**
Previous Target Price (RM)	RM9.08
Previous Recommend.	HOLD
Upside To Target Price	**0.4%**
Dividend Yield (FY15F)	**3.2%**

Stock Code

Bloomberg	Sime MK

Stock & Market Data

Listing		MAIN MARKET
Sector		CONGLOMERATE
Shariah Compliance		YES
Issued Shares (mn)		6,211
Market Cap (RM mn)		55,652
YTD Chg In Share Price		-2.5%
Beta (x)		0.76
52-week Hi/Lo (RM)	RM9.79	RM8.78
3M Average Volume ('000 shares)		4,142
Estimated Free Float		28%

Major Shareholders

Skim ASB	39.98%
EPF	13.38%
PNB	7.71%

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estates that recorded a lower FFB production that dipped by 7% y-o-y to 2.33 million MT. As such, plantation division PBT declined by 46% y-o-y to RM658.7 million from RM1,216.9 million in 9M14 impacted by 1) lower CPO price realised of RM2,171/MT against RM2,439/MT in 9M14; 2) lower FFB production in 9M15 by -6% y-o-y; 3) higher plantation's cost of production, where 3Q15 is the highest cost incurred among the 3 quarters of approximately RM1,600/MT; and 4) lower profit from midstream and downstream business of RM30.3 million (9M14: RM67.8 million) due to lower off-take of biodiesel from petroleum companies due to the drop in crude oil prices and lower sales volume and margins of differentiated products. This has squeezed plantation's total margin to 9.6% from 15.9% a year before. Of note, SIME has completed the acquisition of NBPOL on 2nd March 2015, and that has increased its oil palm planted areas by another 79,800 ha to 605,090 ha (as at FY14: 525,290 ha) with 2 refineries, one in PNG and the other in Liverpool, England. For the period post-acquisition, NBPOL contributed a profit of RM7.5 million. We foresee that the acquisition will add steady profitability and cash generation to the group's earnings moving forwards.

- **Property division.** In 9M15, the group's profit increased by 95% y-o-y to RM473.0 million on the back of 53% increase in revenue of RM2,092.4 million (9M14: RM1,369.7 million) boosted by higher earnings contributions from Elmina East township and Bandar Bukit Raja township together with a jump in contribution from construction progress of the Pagoh Education Hub, Johor project coupled with gain from compulsory land acquisition in Ampar Tenang by the government and the gains of RM55.5 million on the disposal of 9.9% equity interest in Eastern & Oriental Berhad and Subang Avenue of RM55.2 million. Of note, in 9M15, the group's sold 1,241 units of properties with gross sales value of RM1.4 billion while reaching unbilled sales of RM1.8 billion as at 31st March 2015.

- **Motor Division.** Although revenue increased by 8% y-o-y to RM13,800.3 million but profit in 9M15 declined 18% y-o-y to RM331.2 million due to 1) lower sales and margins from all brands recorded from Malaysia operations that declined by 42% y-o-y to RM132.0 million mainly impacted by customers holding back purchases and dealers reducing their inventory holding due to implementation of GST coupled with tighter credit from financial institutions; and 2) a drop in China's profit contribution by 50% y-o-y to RM82.6 million resultant from reduced profit contribution from BMW operations as well as austerity measure that affected the luxury car segment. Lower contribution from China and Malaysia was mitigated by improving performance from Australia, Vietnam and New Zealand, benefitting from the newly acquired BMW operations in April 2014 (Australia) and November 2013 (Vietnam), as well as improving contribution from trucks operations in New Zealand.

- **Industrial division.** Industrial division recorded a lower profit of RM7,516.3 million (-16% y-o-y) in 9M15 due to lower equipment deliveries and product support sales in Australia as mining players margin has been squeezed, attributable to their cost savings measure as well as persistent weak coal prices. Malaysia, China/HK and SE Asia's industrial division also recorded lower performance of RM69.2 million (-29% y-o-y), RM86.7 million (-8% y-o-y) and RM86.2 million (-39% y-o-y) respectively in 9M15 underpinned by lower equipment and engine sales as slowdown in demand from the construction, mining, shipyard and electric power generation sectors. According to the management, the Group managed to gain an order book of RM2.4 billion for heavy equipment in the 3Q15.

- **Energy and Utilities division.** Profit from this division rose to RM88.5 million (+546% y-o-y) in 9M15 resultant from higher profit from ports and water operations in China on account of an increase in throughput and high average tariff rate achieved. Ports' throughput by general cargo increased by 15% y-o-y to 23.98 million tonnes while Weifang port's container throughput jumped by 166% y-o-y to 147,804 TEUs. According to the management, higher container throughput in 9M15 was due to higher demand for coal cargo and usage of land transit facilities. Of note, the higher profit was also contributed by the recognition of a net gain of RM21 million on disposals of wave-breakers in Weifang Port to a joint venture company, Weifang Port Services Co Ltd.

- **Sector Outlook.** We are maintaining our **NEUTRAL** call on the plantation sector due to the absence of new fresh catalyst with prolong supply-demand miss-match coming on stream as production may build-up amid seasonal production growth cycle. In addition, demand is expected to be moderate in 2015 as import from major trading partner is likely to be slower. We are of the view that the only re-rating catalyst for CPO price in 2015 will be the widening premium of soybean oil against the palm oil and weather abnormalities, if any. We assume CPO prices to hover around RM2,100/MT – RM2,500/MT throughout the year and averaging at RM2,300/MT in 2015.

- **Change forecast.** SIME has announced that its will likely achieve lower earnings than was set out in the initial KPI target for FY15 of RM2.5 billion to be between RM2.0 billion – RM2.1 billion due to challenging business environment as lower commodity prices, drop in automobile sales and lower equipment deliveries and product support sales, weighing on the overall earnings of the group. In-line with the new KPI target by management, we have tweaked our FY15 and FY16 earnings forecast to RM2,107 million and RM2,681 million respectively after imputing 1) our new view on CPO price assumption; 2) uncertain outlook with challenging business environment due to slower economic growth and un-clear direction of global commodity prices; and 3) the expected volatility of Ringgit exchange rate.

- **Valuation & recommendation.** We re-initiate SIME Darby with a **HOLD** call**.** Based on slower earnings projections in FY15 and FY16 we have a new target price of RM9.00 that is derived from sum-of-parts valuation methodology which implies FY15 PER of 26.5x compared to 5-years average PER of 21x.

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Table 1: Results Review - Quarterly figures

FYE 30 June (RM'm)	2Q14	1Q15	2Q15	q-o-q	y-o-y	IH14	1H15	y-o-y
Revenue	10,101.9	10,742.0	9,997.8	-6.9%	-1.0%	31,394.4	30,864.2	-1.7%
EBIT	1,031.5	657.4	679.6	3.4%	-34.1%	2,787.7	2,082.0	-25.3%
Pretax profit	960.5	592.7	595.2	0.4%	-38.0%	2,584.0	1,862.8	-27.9%
Taxation	-109.1	-127.9	-166.8	30.4%	52.9%	-430.4	-443.0	2.9%
Net Profit	852.5	437.4	386.0	-11.8%	-54.7%	2,159.8	1,324.1	-38.7%
EPS (sen)	13.73	7.04	6.21	-11.8%	-54.7%	34.77	21.32	-38.7%
Net gearing (x)	0.25	0.23	0.49	112.7%	95.7%	0.25	0.49	95.7%
EBIT margin (%)	10.2	6.1	6.8			8.9	6.7	
PBT margin (%)	9.5	5.5	6.0			8.2	6.0	
Net margin (%)	8.4	4.1	3.9			6.9	4.3	

Table 2: Financial Summary

YE: June (RM'Mill)	2011	2012	2013	2014	2015F	2016F
Revenue	41,859	47,255	46,109	43,908	41,939	43,514
EBIT	5,616	5,831	4,624	3,999	3,218	4,023
PBT	5,449	5,695	4,314	3,965	2,902	3,694
Net profit	3,665	4,150	3,701	3,353	2,107	2,681
EPS (sen)	59.0	66.8	59.6	54.0	33.9	43.2
Pre-tax margin	13%	12%	9%	9%	7%	8%
Net profit margin	9%	9%	8%	8%	5%	6%
PER (x)	15.2	13.4	15.0	16.6	26.4	20.8
P/BV (x)	2.2	2.1	2.0	1.9	1.9	1.8
ROE	16%	17%	14%	12%	7%	9%
ROA	9%	9%	8%	7%	4%	5%
Dividend (RM)	0.30	0.35	0.34	0.36	0.29	0.41
Dividend Yield	3.3	3.9	3.8	4.0	3.2	4.5

Source: Bursa Malaysia, M&A Securities

Table 3: Results Analysis - Segmental Results

FYE: June (RM'mil)	3Q14	2Q15	3Q15	q-o-q	y-o-y	9M14	9M15	y-o-y
Plantation	454.8	269.8	99.6	-63.1%	-78.1%	1,216.9	658.7	-45.9%
Motor	142.9	138.2	83.0	-39.9%	-41.9%	402.9	331.2	-17.8%
Industrial	220.6	126.1	79.2	-37.2%	-64.1%	809.3	395.4	-51.1%
Property	105.5	62.1	273.8	340.9%	159.5%	243.2	473.0	94.5%
Energy & Utilities	-2.3	47.8	19.0	-60.3%	-926.1%	13.7	88.5	546.0%
Others	25.3	-2.9	-53.9	1758.6%	-313.0%	49.4	-48.5	-198.2%

Source: Bursa Malaysia, M&A Securities

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Table 4: Plantation Statistics

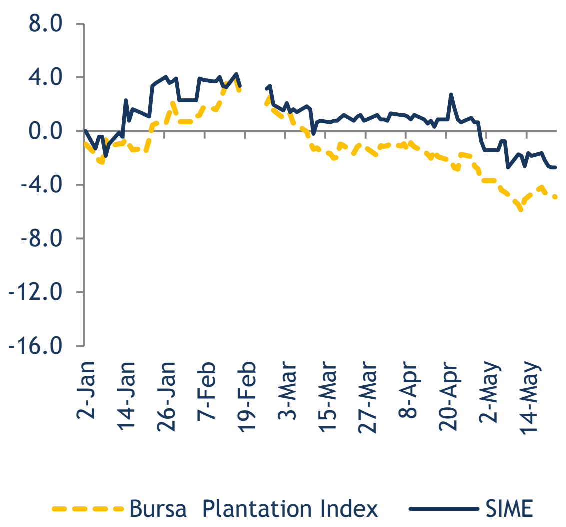
FYE: June (tonne)	9M15	9M14	y-o-y
FFB Production (mn MT)	6.74	7.14	-5.6%
FFB Yield per mature hectare	14.72	15.39	-4.4%
CPO Production (mn MT)	1.63	1.73	-5.8%
PK Production (mn MT)	0.38	0.40	-5.0%
CPO Extraction Rate (%)	21.79	21.86	-0.3%
Palm Kernel Extraction Rate (%)	5.01	4.99	0.4%
Average selling price - CPO (RM/MT)	2,171	2,439	-11.0%
Average selling price - PK (RM/MT)	1,377	1,464	-5.9%

Source: Company, M&A Securities

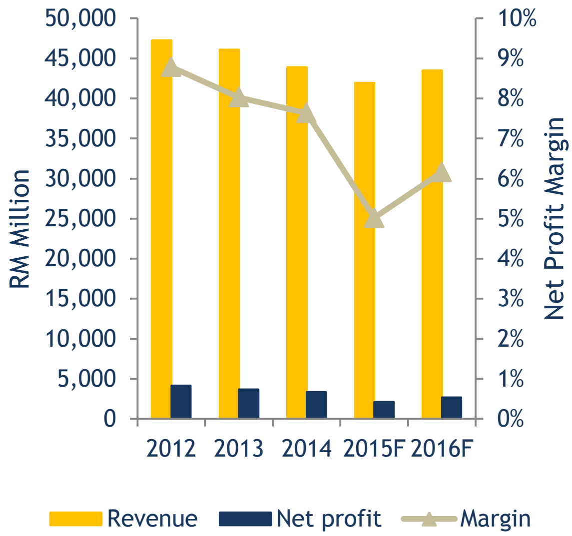
Table 5: Sum-of-parts Derived TP

Division	NBV	CY16 Earnings	PER (x)	Value (RM'Mil)
Plantation (21x CY16 PER)		1,745.5	21	36,654.5
Property (15x PER)	436	654.4	15	9,815.4
Industrial (13x CY15 PER)		668.3	13	8,554.5
Motors (11x CY15 PER)		606.3	11	6,548.1
Energy & Utilities (1x P/B)	1,243	20.8		1,242.8
Net Cash				(6,945.5)
Cash				4,381.8
Total Borrowings				(11,327.3)
Total Equity Value				55,869.9
Share base				6,211.2
Fair Value (RM)				**9.00**

KLCI Plantation Index vs. Sime Darby (YTD Performance)



Revenue and Net Profit (FY12-FY16F)



Source: Bursa Malaysia, M&A Securities

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STOCK RECOMMENDATIONS

BUY *Share price is expected to be ≥+10% over the next 12 months.*
TRADING BUY *Share price is expected to be ≥+10% within 3-months due to positive newsflow.*
HOLD *Share price is expected to be between -10% and +10% over the next 12 months.*
SELL *Share price is expected to be ≥-10% over the next 12 months.*

SECTOR RECOMMENDATIONS

OVERWEIGHT *The sector is expected to outperform the FBM KLCI over the next 12 months.*
NEUTRAL *The sector is expected to perform in line with the FBM KLCI over the next 12 months.*
UNDERWEIGHT *The sector is expected to underperform the FBM KLCI over the next 12 months.*

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