

06 October 2017

United U-Li Corporation Shifting Appetite

Steel prices are at a rising phase owing to supply constraints from China. While we do not expect ULICORP to be adversely affected given its cost structure and margin expansion, market appetite has moved in favour of upstream players in lieu of shorter term growth opportunities. We maintain our OUTPERFORM recommendation but lower our TP to RM4.95 as we tone down our valuation to 14.0x FY18E PER on a lower +0.5SD (from +1.0SD, previously) over the 5-year mean.

Earnings recovery from margin expansions. The group registered a decline in 1H17 sales by 7% YoY. Its main contributor - cable support system segment suffered a 12% earnings decrease, attributed by delays in project delivery of outsourced components and activities. However, PBT margin improved to 21.8% (+0.6pts) on the back of better sales mix on stainless steel products and improved economies of scale. Margins could have been significantly higher as 1Q17's performance was underpinned by high gestation expenses. On the other hand, the group's lighting segment saw a 19% boost in sales on higher project demand but was dragged by higher marketing spend in 1Q17, leading to lower PBT margins at 8.7% (-2.7pts).

Positives to hold up. Management viewed the delay in outsourced project delivery to be a one-off incident and does not foresee further recurrences. Top-line performance for the group will be driven by the unhindered implementation of domestic infrastructure projects, which could provide some assurance on the overall stability of the group's order-books for the medium term. The added capacity of the new Nilai plant should sufficiently support the increase in demand. Furthermore, with the added capacity, the group intends to increase its presence in the foreign markets (i.e. Cambodia, Vietnam, Middle East) to improve project flows. However, we believe major domestic infrastructure projects are still expected to be the primary contributor to group performance as export contribution is relatively small (i.e. less than 20%). At the meantime, the commissioning of the new in-house hot dip galvanising facility and extended powder spray line is expected to translate to better cost savings for the group.

Steel prices aloft which benefits upstream player more. Steel prices has seen a significant upward shift (+c.25%) following a combination of factors namely; (i) the extension of Federal Government safeguards to increase import duties of steel rebars and wire rods, (ii) anticipated supply constraints from China from stockpiling during the winter construction period, and (iii) tighter Chinese government controls to control carbon footprint, which could further dampen supply flow. While ULICORP is not significantly affected by the rise in prices as they are able to pass down costs to some degree, market trading sentiment appears to lean towards the direct benefactors of the higher steel prices (i.e. upstream steel millers such as ANNJO, LIONIND, SSTEEL, MASTEEL). We believe that this may have led to the switch of interest towards more towards upstream players given their shorter-term reflection in growth.

Maintain OUTPERFORM with a lower TP of RM4.95, (from RM5.60, previously). While our earnings assumptions remain unchanged (FY19E EPS of 35.2 sen), we believe the shift in market preference to upstream steel counters could dampen trading sentiments for the stock. This is further seen in the lower trailing Fwd. PER during the year which lingered at its average rate. Hence, we tone down our valuation assumptions from 16.0x PER (+1.0SD over the 5-year mean) to 14.0x (+0.5SD over the 5-year mean). Nonetheless, we still like the stock and view its valuation as undemanding given its: (i) leading market position, (ii) strong expected growth prospect (2-year Forward CAGR of 28%), (iii) expanding margins, and (iv) net cash position. We reiterate our OUTPERFORM call.

OUTPERFORM ↔

Price: RM4.30
Target Price: RM4.95 ↓

Expected Capital Gain: RM0.65 +15.1%
Expected Divd. Yield: RM0.16 +3.7%
Expected Total Return: RM0.81 +18.8%

KLCI Index 1,759.09

Stock Information

Bloomberg Ticker	UULI MK Equity
Bursa Code	7133
Listing Market	Main Market
Shariah Compliant	No
Issued shares	145.2
Market Cap (RM m)	624.4
Par value per share (RM)	0.50
52-week range (H)	4.93
52-week range (L)	3.36
Free Float	48%
Beta	0.8
3-mth avg daily vol	32,587

Major Shareholders

Pearl Deal M Sdn Bhd	37.2%
RHB Asset Management	11.1%
Kumpulan Wang Persaraan	3.2%

Summary Earnings Table

FY Dec (RM m)	2016A	2017E	2018E
Turnover	201.1	231.2	274.0
EBIT	43.0	51.8	67.7
PBT	43.5	52.0	68.2
Net Profit	31.1	39.0	51.1
Core PATAMI	31.1	39.0	51.1
Consensus (NP)	-	36.5	49.1
Earnings Revision	-	0%	0%
Core EPS (sen)	21.4	26.9	35.2
Core EPS growth (%)	19.7%	25.3%	31.1%
NDPS (sen)	12.0	12.0	16.0
NTA per Share (RM)	0.82	0.87	0.92
Price to NTA (x)	2.3	2.1	2.0
PER (x)	20.1	16.0	12.2
Debt-to-Equity ratio (x)	(0.0)	(0.2)	(0.2)
Return on Asset (%)	9.7%	10.9%	12.8%
Return on Equity (%)	11.8%	13.9%	16.7%
Net Div. Yield (%)	2.8%	2.8%	3.7%

Share Price Performance



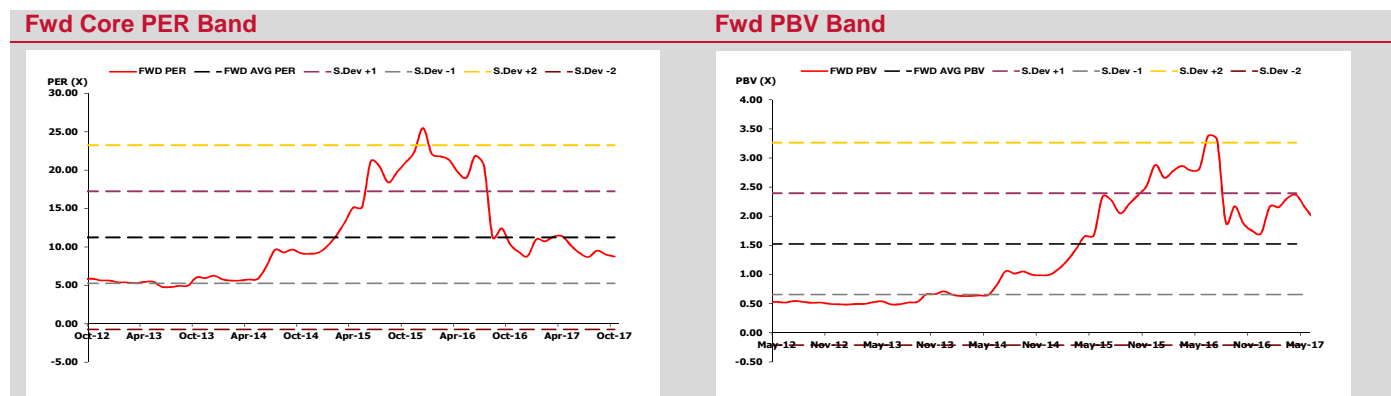
	1 mth	3 mths	12 mths
Absolute (%)	-9.2%	-15.6%	-3.8%
Relative (%)	-9.6%	-15.4%	-8.7%

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Income Statement						Financial Data & Ratios					
FY Dec (RM'm)	2014A	2015A	2016A	2017E	2018E	FY Dec (RM'm)	2014A	2015A	2016A	2017E	2018E
Revenue	172.3	179.2	201.1	231.2	274.0	Growth (%)					
Operating Profit	30.7	35.1	43.0	51.8	67.7	Turnover	11.6%	4.0%	12.2%	15.0%	18.5%
Depreciation	-5.6	-5.5	-7.2	-8.5	-9.2	EBITDA	19.2%	12.0%	23.5%	20.0%	27.6%
Interest Inc/(Exp)	0.0	0.6	0.5	0.2	0.4	Operating Profit	22.0%	14.3%	22.5%	20.4%	30.8%
Associate Earnings	0.0	0.0	0.0	0.0	0.0	PBT	25.4%	16.0%	21.9%	19.6%	31.1%
Profit Before Tax	30.8	35.7	43.5	52.0	68.2	Core Net Profit	40.0%	11.9%	19.7%	25.3%	31.1%
Taxation	-7.5	-9.7	-12.4	-13.0	-17.0	Profitability (%)					
Net Profit	23.2	26.0	31.1	39.0	51.1	Operating Margin	17.8%	19.6%	21.4%	22.4%	24.7%
Core Net Profit	23.2	26.0	31.1	39.0	51.1	PBT Margin	17.9%	19.9%	21.6%	22.5%	24.9%
						Core NP Margin	13.5%	14.5%	15.5%	16.9%	18.7%
						Effective Tax	24.5%	27.1%	28.4%	25.0%	25.0%
						ROA	9.9%	9.4%	9.7%	10.9%	12.8%
						ROE	11.7%	11.3%	11.8%	13.9%	16.7%
						DuPont Analysis					
						Net Margin (%)	13.5%	14.5%	15.5%	16.9%	18.7%
						Assets Turnover (x)	0.7	0.6	0.6	0.6	0.7
						Leverage Factor (x)	1.2	1.2	1.2	1.3	1.3
						ROE (%)	11.7%	11.3%	11.8%	13.9%	16.7%
						Leverage					
						Debt/Asset (x)	0.1	0.1	0.1	0.1	0.1
						Debt/Equity (x)	0.1	0.1	0.1	0.1	0.1
						Net (Cash)/Debt	(49.7)	(82.0)	(48.3)	(66.1)	(70.1)
						Net Debt/Equity (x)	(0.2)	(0.3)	(0.2)	(0.2)	(0.2)
						Valuations					
						Core EPS (sen)	16.0	17.9	21.4	26.9	35.2
						NDPS (sen)	10.0	12.0	12.0	12.0	16.0
						BV/sh (RM)	1.4	1.8	1.9	2.0	2.2
						PER (x)	26.9	24.0	20.1	16.0	12.2
						Div. Yield (%)	2.3%	2.8%	2.8%	2.8%	3.7%
						PBV (x)	3.0	2.4	2.3	2.1	2.0
						EV/EBITDA (x)	8.4	21.5	11.1	10.9	10.2

Source: Kenanga Research



Source: Bloomberg, Kenanga Research

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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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