

06 June 2012

COMPANY UPDATE

PT UNITED TRACTORS Tbk

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Attractive valuation but short-term downside bias remains strong

BUY

We maintained our BUY rating on PT United Tractors with lower target price.

Current valuation is cheap and we feel that market overreacted with the disappointing first quarter profitability and lower-than-expected Komatsu heavy equipment sales leading to falling market share. The condition is further exacerbated by worsening situation in Eurozone, softening Chinese economy, falling commodity prices (especially coal), and uncertainties surrounding taxation on exports minerals and coals. However, Rupiah depreciation against the greenback will provide temporary relief to UNTR as UNTR derived most of its income in USD while its costs (especially labor) are denominated in IDR.

According to the firm, the indicative May sales volume was around 772 units (+3.1% mom, +25.1% yoy) and this can probably be attributed to drier weather condition facilitating delivery of heavy equipment.

Disappointing 1Q12 Margin

UNTR 1Q2012 gross margin disappointed us with margin compression continued to persist—overall gross margin fell to 17.4% (-200 bps qoq; -30bps yoy); EBITDA margin fell to 18.9% (-70bps qoq; -90bps yoy). Dissecting the revenue breakdown does reveal that the mining contracting segment is dragging down the overall performance, followed by mining division. The firm cited rising fuel costs and wet weather conditions which increased the operational costs of mining and mining contracting division, thus leading to margin compression. Going forward, we remain sanguine on the margin expansion in the mining and mining contracting divisions as we progress into drier season and falling crude oil prices will soften the blow from falling coal prices.

Resilient Mining Contracting

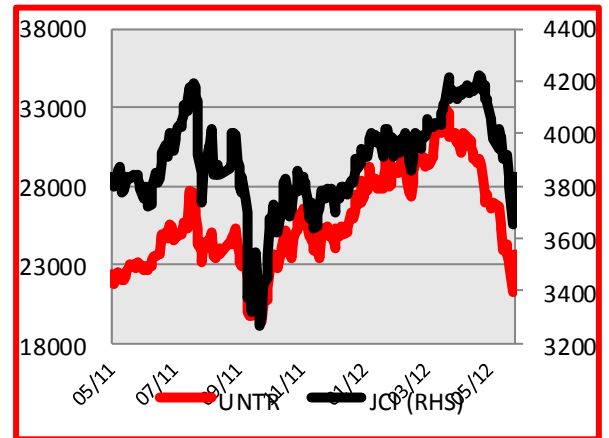
Mining Contracting division tends to be resilient as it has no direct impact from declining coal prices. Annual target volume of OB removed, coal mined and their respective prices have been stated in the contract and the firm has locked in the minimum price and volume. As such we still expect a marginal growth of around 13% amid the pessimistic climate in coal industry.

Wibowo Ng
Research Analyst
Wibowo.ng@sinarmassekuritas.co.id

Stock Data

Sector	Heavy Equipment
Price (5 June 2012)	IDR 21,850
Target Price 2012	IDR 29,100
12-month Rating	BUY
Prior	BUY (TP IDR 30,500)
Ticker	UNTR.IJ (BBG); UNTR.JK (RIC)
Market Cap	IDR85.6 tn
Shares Outstanding	3,730 mn
Free Float	1,511 mn

UNTR Performance against JCI Index



Source: Bloomberg

	2010	2011	2012E	2013F	2014F
Revenues	37,324	55,053	64,681	76,517	92,201
EBIT	5,163	7,615	8,953	10,739	12,629
Net Income	3,873	5,901	6,701	8,010	9,514
EPS	1,164	1,657	1,796	2,147	2,551
Net DPS	441	663	719	859	1,020

In bn IDR except per share data; Source: Bloomberg, Company data, SinarMas Sekuritas Research

Profitability	5-yr avg	2011	2012E	2013F	2014F
Gross Margin%	19.4%	18.5%	18.3%	18.4%	18.1%
EBIT Margin%	14.8%	13.8%	13.8%	14.0%	13.7%
EDBITDA Margin%	21.0%	20.1%	20.0%	20.0%	17.7%
EV/EBITDA x		9.5	8.1	6.9	6.5
P/E x		17.6	16.2	13.6	11.4
Net Dividend Yield		2.3%	2.5%	3.0%	3.6%

Source: Bloomberg, Company data, SinarMas Sekuritas Research

Top Holders

PT Astra International Tbk	59.50%
Institutional Ownership	16.30%

Source: Bloomberg (as of 31 May 2012)

Higher ASP at the expense of market share

UNTR sold 2,207 units of Komatsu heavy machineries in 1Q2012 (no change yoy; +136 units qoq) at ASP of IDR2,353mn (-0.01% qoq; +7.9% yoy) with market share of only 44% (below target set of 45%-46%). In 4M2012, UNTR sold 2,956 units (-18 units yoy). The fall in volume sales and market share can be attributed to the stabilization of manufacturing and supply of its Japanese competitors post-tsunami and reallocation of resources of competitors from China to other Emerging Markets (including Indonesia) leading to intensified competition resulting in depressed Komatsu's market share. Competition in 20-ton excavator is so intense that UNTR was losing market share to its competitors which offer better pricing. The firm is still adamant that it will reach its target of selling 9,500 units (our target 9,406 units) and it plans to re-strategize its marketing program to re-gain Komatsu's market share in the 20-ton excavator categories.

Falling coal prices might cloud the planned capital investment by mining companies and this has the potential to affect Komatsu sales volume. However, rising sales from agriculture and construction, especially with higher planned new planting by palm oil firms and proposed infrastructure investment, might relieve the downward pressure on sales of heavy equipment in mining sector.

Re-strategize Marketing Program

Package financing will be the key strategy – UNTR will maintain its price increment at around 3-5% p.a. while offering package financing via collaboration with heavy equipment financing division of Astra International (SANF and Komatsu Astra Finance) allows UNTR to package its products and offer it at more competitive financing rate. The potential ramification will be further margin compression to around 16.5% (vs our prior assumption of 20.3%) in 2012E and we surmise that this trend will persist as competition intensified especially with the expansion of Korean heavy equipment companies in Indonesia.

Coal volume to boost top-line revenue

TTA has begun producing coal from previous-greenfield concession and it contributed 51% of total coal produced. TTA coal with ADB around 6,300 kcal which is sold at around 13% discount to Newcastle benchmark while DEJ coal with ADB of 6,700 kcal is sold at Newcastle Benchmark. We estimate that the firm will produce 6.1mn tons (target: 6-7mn tons) and in the 4M2012, the firm has accomplished 32% of our 2012 target (28% of its own target of 7mn tons) despite wet weather conditions. The higher target will offset the lower ASP due to higher proportion of TTA coal.

Key Risks

Key downside Risks include: (1) further aggravation in Eurozone crisis leading to crisis of confidence and contagion risks spreading to emerging markets dampening investor's sentiments; (2) falling commodity prices; (3) the breakdown of correlation between crude oil and coal prices leading to margin compression in mining division; (4) softening capital investment by mining companies will have adverse impact on the profitability of the firm; (5) intensified competition within the heavy equipment market.

From the market view, short-term downside bias is particularly strong as foreign institutional clients are reducing their positions in the emerging markets. As such, we recommend extreme caution and prudence in purchasing/accumulating the shares.

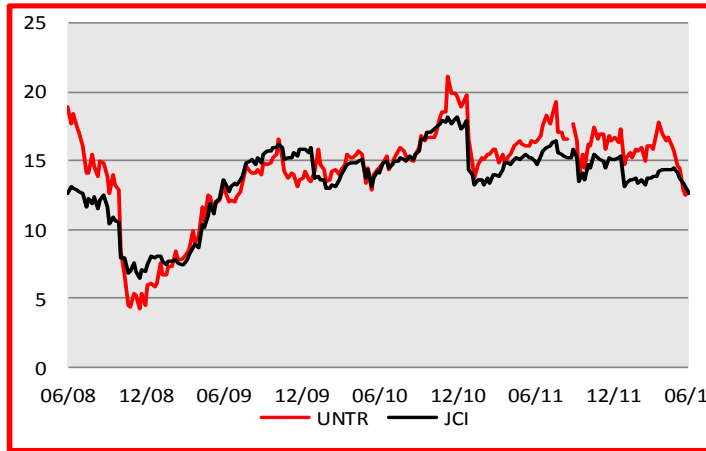
Upside Potential

Upside potential might include: (1) the approval of its import tax break on hybrid excavator (which is more fuel efficient despite higher cost) and the implementation of the requirement of companies to use more fuel efficient equipment in order to ensure available supply of fuel in mining regions; (2) acquisition of distressed mines at low valuation; (3) re-positioning of market share of Komatsu which will be confirmed in 2Q2012 at better-than-expected profitability metric.

Valuation: maintain our BUY rating with lower price target of IDR 29,100

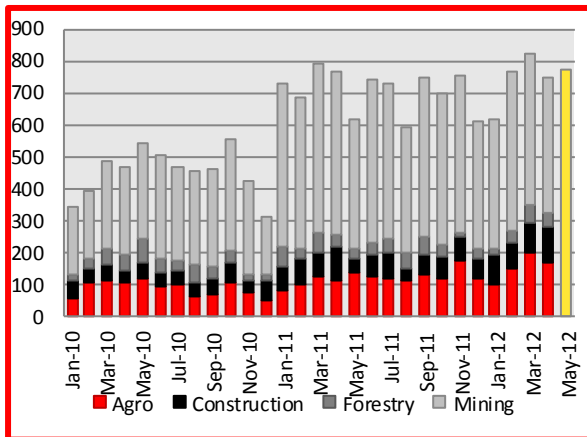
We derive our target price from a DCF-based valuation with a discrete growth rate forecast till FY2025E, followed by a terminal growth rate of 4%. We assume 15.4% WACC. Our target price indicates a 33% upside potential with 2012E and 2013E P/E of 16.2x and 13.6x, respectively, and a 0.9x PEG.

Chart 1: Comparison of 12-M Forward P/E for UNTR and JCI Index.



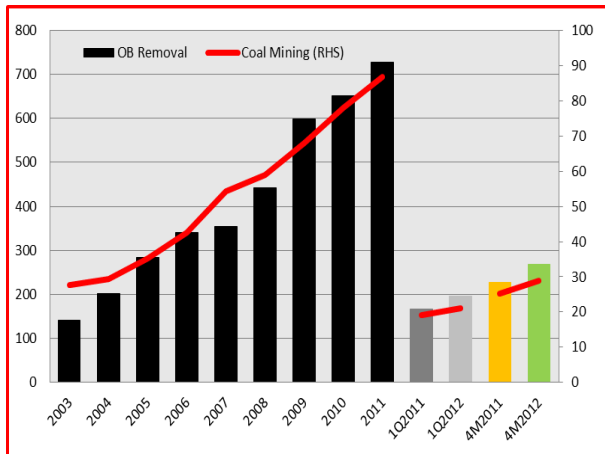
Source: Bloomberg

Chart 2: Disappointing 4M2012 Komatsu Volume Sales but Indicative May-12 Sales have shown some positive results from better weather conditions and the new marketing campaign



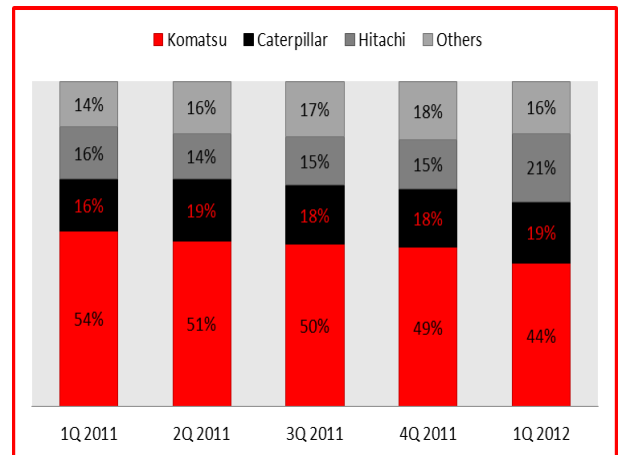
Source: Company data; May-12 value is indicative

Chart 4: OB Removal and coal mining are on track despite poor weather conditions



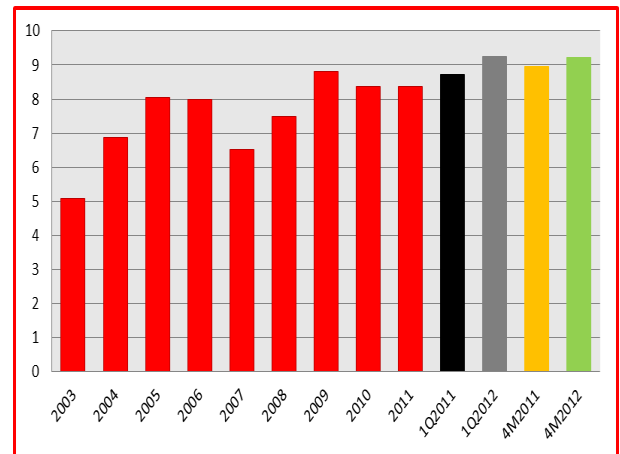
Source: Company data

Chart 3: Leading to declining market share



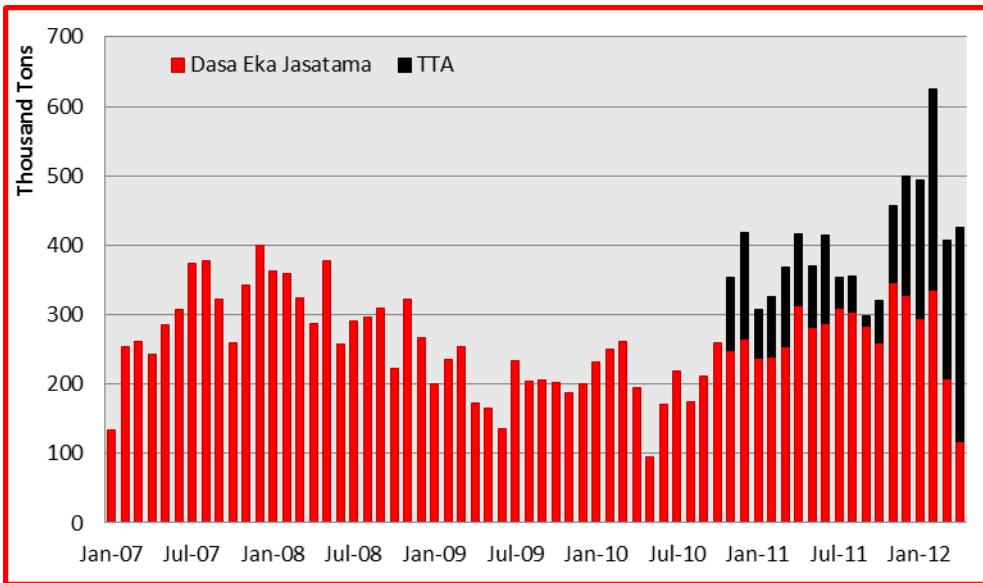
Source: Company data

Chart 5: Implied Stripping Ratio



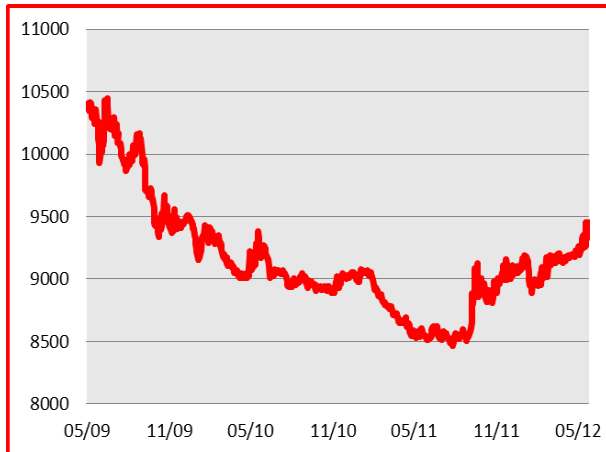
Source: Company data

Chart 6: Coal Volume is expected to rise with 2012 target of 6.1 mn tons



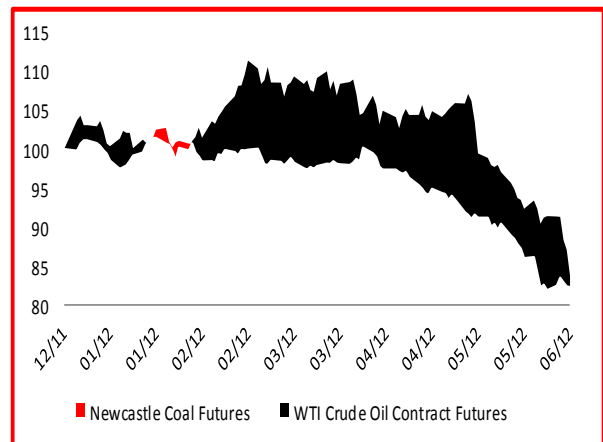
Source: Company data

Chart 7: IDR depreciating vs USD



Source: Bloomberg

Chart 8: Crude Oil prices rose faster than Coal leading to margin compression in mining division



Source: Bloomberg; Normalized at 01/03/12 = 100

Table 1: Income Statement Summary (IDR mn)

	2010	2011	2012E	2013F	2014F
Revenues	37,323,872	55,052,562	64,680,557	76,517,273	92,201,348
Cost of Revenue	(30,528,174)	(44,859,041)	(52,835,888)	(62,431,519)	(75,523,175)
Gross Profit	6,795,698	10,193,521	11,844,669	14,085,754	16,678,174
SG&A	(1,633,177)	(2,578,423)	(2,891,688)	(3,347,176)	(4,049,642)
EBIT	5,162,521	7,615,098	8,952,982	10,738,578	12,628,531
Other non-operating income	38,939	208,282	373,772	386,180	566,480
interest, net	(140,200)	(38,803)	(64,124)	(104,770)	1,423
Profit before tax	5,061,260	7,784,577	9,262,630	11,019,988	13,196,434
Taxation	(1,186,745)	(1,885,071)	(2,233,534)	(2,669,929)	(3,171,319)
Profit after tax	3,874,515	5,899,506	7,029,096	8,350,058	10,025,115
Minorities	(1,584)	1,402	0	0	0
Net Profit	3,872,931	5,900,908	7,029,096	8,350,058	10,025,115
Gross Margin	18.2%	18.5%	18.3%	18.4%	18.1%
EBITDA margin	21.7%	20.1%	20.0%	20.0%	17.7%
EBIT Margin	13.8%	13.8%	13.8%	14.0%	13.7%
NOPAT Margin	10.4%	10.7%	10.9%	10.9%	10.9%
Net Margin	10.4%	10.7%	10.9%	10.9%	10.9%
Revenue Growth	27.6%	47.5%	17.5%	18.3%	20.5%
EBITDA Growth	13.9%	36.1%	17.4%	18.3%	6.4%
EBIT Growth	-2.0%	47.5%	17.6%	19.9%	17.6%
Net Profit Growth	1.5%	52.4%	13.6%	19.5%	18.8%

Source: Company data, Sinarmas Sekuritas

Table 2: Assumption Summary

	2010	2011	2012F	2013F	2014F
Construction Machinery					
Unit of Heavy Equipment Sold	5,404	8,467	9,405	10,534	11,798
<i>yoy growth rate</i>	74%	57%	11%	12%	12%
ASP per unit (IDR mn)	2,436.48	2,604	2,707	2,789.35	2,899
<i>yoy growth rate</i>	3%	7%	4%	3%	4%
Parts & Services	4,108,000	5,145,569	6,310,100	7,974,595	9,968,243
<i>yoy growth rate</i>	14%	25%	23%	26%	25%
Mining Contracting					
Overburden Removed	651	789	894	1,004	1,155
<i>yoy growth rate</i>	9%	21%	13%	12%	15%
Coal mined	78	87	98	111	128
<i>yoy growth rate</i>	15%	11%	13%	14%	15%
Implied Strip Ratio	8.35	9.10	9.10	9.00	9.00
Mining					
Coal Production volume	2,842,000	4,488,000	6,101,900	9,950,000	12,935,000
<i>yoy growth rate</i>	19%	58%	36%	63%	30%
ASP (IDR)	1,098,020	1,210,866	1,011,348	975,895	1,028,742
<i>yoy growth rate</i>	-7%	10%	-16%	-4%	5%

Source: Company data, Sinarmas Sekuritas

Fiscal Year End					
Income Statement (IDR mn)	2010	2011	2012E	2013F	2014F
Sales Revenue	37,323,872	55,052,562	64,680,557	76,517,273	92,201,348
Gross Profit	6,795,698	10,193,521	11,844,669	14,085,754	16,678,174
Operating Income	5,162,521	7,615,098	8,952,982	10,738,578	12,628,531
Depreciation & Amortization	2,952,125	3,428,272	4,010,195	4,591,036	3,688,054
EBITDA	8,114,646	11,043,370	12,963,176	15,329,614	16,316,585
Other non-operating income	38,939	208,282	373,772	386,180	566,480
Net Interest Income (expense)	(140,200)	(38,803)	(64,124)	(104,770)	1,423
Profit before tax	5,061,260	7,784,577	9,262,630	11,019,988	13,196,434
Tax expenses	(1,186,745)	(1,885,071)	(2,233,534)	(2,669,929)	(3,171,319)
Profit after tax	3,874,515	5,899,506	7,029,096	8,350,058	10,025,115
Minority Interests	(1,584)	1,402	0	0	0
Net Profit	3,872,931	5,900,908	7,029,096	8,350,058	10,025,115
Cash Flow (IDR mn)					
Operating Cash Flow	2,423,881	9,947,819	11,534,432	8,255,445	14,754,359
Capex	3,357,689	5,258,071	6,250,000	5,626,136	6,076,227
Free Cash Flow	(933,808)	4,689,748	9,351,756	2,904,230	9,117,178
Dividends Received from Investments	23,550	17,939	0	0	0
Dividends Paid	(1,629,228)	(1,697,214)	(2,680,240)	(3,203,915)	(3,805,583)
Debt Issuance (redemption)	1,539,128	(1,493,506)	2,435,130	953,110	1,176,283
Share Capital increase	0	6,023,188	0	0	0
Net debt (cash)	3,879,249	(3,065,384)	(5,395,294)	(5,101,957)	(10,341,184)
Balance Sheet (IDR mn)					
Cash & cash equivalents	1,343,220	7,135,386	11,731,982	12,152,501	18,255,681
Account Receivables	5,349,688	9,969,714	7,997,107	13,257,691	12,353,795
Inventories	6,931,631	7,129,459	8,255,607	9,754,925	11,800,496
Other Current assets	1,908,223	1,391,019	1,637,436	1,942,812	2,335,006
Net fixed assets	13,261,374	19,395,857	17,379,576	18,414,676	20,802,848
Other non-current assets	906,778	1,418,627	4,213,785	3,887,949	3,611,561
Total Assets	29,700,914	46,440,062	51,215,495	59,410,553	69,159,388
Short term Liabilities	9,919,225	14,930,069	15,134,818	17,795,854	20,938,817
Long term Liabilities	3,616,283	4,006,045	4,539,140	5,249,190	6,127,677
Total Liabilities	13,535,508	18,936,114	19,673,958	23,045,045	27,066,494
Shareholders' Equity	16,136,338	26,320,449	30,358,038	35,182,009	40,909,395
Minority Interest	29,068	1,183,499	1,183,499	1,183,499	1,183,499
Total Equity & Liabilities	29,700,914	46,440,062	51,215,495	59,410,553	69,159,388
Key Ratio					
Revenue Growth (%)	27.6%	47.5%	17.5%	18.3%	20.5%
EPS Growth (%)	1.5%	42.3%	8.4%	19.5%	18.8%
EBITDA Margin (%)	21.7%	20.1%	20.0%	20.0%	17.7%
Payout Ratio (%)	37.9%	40.0%	40.0%	40.0%	40.0%
ROE (%)	24.0%	22.4%	22.1%	22.8%	23.3%
Quick Ratio (x)	0.87	1.24	1.41	1.54	1.57
Debt/Equity (%)	35.2%	17.9%	23.5%	23.0%	22.7%

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