



Corporate News Flash

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AUTOMOTIVE

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Proton Holdings

TRADING BUY	Upgrade
Price	RM2.99
Target	RM3.65

Proton to divest Edar To EON

The Financial Times reported today that Proton is expected to make an announcement anytime next month that it will divest its distribution arm, Proton Edar, to Edaran Otomobil Nasional (EON) in exchange for shares.

COMMENTS

Focus on manufacturing. We are generally neutral on the news despite the attempt to consolidate its distribution arm. In this report, we will discuss the announcement's pros and cons and how this would impact on Proton in the future towards achieving its long term objective to be a leading national car manufacturer. Although the move for a consolidated distribution network of auto dealers will remove cost inefficiencies due to unnecessary competition between Proton Edar and EON, the benefit of the divestment of Proton Edar ultimately lies in how big a stake in EON that Proton would end up with. Depending on ownership level, should Proton end up with a stake that does not give it control over EON, this would be deemed unfavorable to Proton's long term objective given the fact that DRB-Hicom currently controls 79.05% of EON. It is worth noting that in 2007 when negotiations on an equity partnership with Volkswagen failed when it seemed like the latter was eyeing Proton's distribution network. Therefore, the divestment of Proton Edar to EON would prove favourable for Proton in protecting EON's distributorship network as such a takeover will be more difficult as it would require shareholder approval. We believe that this would generally be beneficial over the short term as the divestment solely focuses on enhancing Proton's manufacturing focus by removing the "social burden" of maintaining its large distribution network.

Proton Edar the larger piece of the pie. Proton Edar currently holds a 60% share of Proton's showrooms, with the remainder held by EON, which on top of Proton cars also distributes marques such as Volkswagen, Mitsubishi, Suzuki and Audi. EON's net profit is attributed to its decent margin of 4.5% owing to the success of Proton's remodeled Saga.

How big a stake can Proton take up? Looking at the assets owned by Proton Edar, we believe the divestment of Proton Edar could range from RM200m-RM230m. However, EON's market cap is currently at just RM145m. Hence, we believe this could likely involve DRB-Hicom giving up a substantial portion of its shares. However, this adds more uncertainty to the deal with the involvement of DRB-Hicom, which wants to fully privatise EON.

TP raised based on higher P/NTA. With the expectation of more favourable news flowing in, including the pending outcome of Proton's technology tie-up with Mitsubishi and the positive political factors such as the pending NAP policy, which has been postponed to the end of 2009, we upgrade our call to trading buy with a target price of RM3.65 from RM1.46, based on a discounted forward P/NTA of 0.40x against earlier target P/NTA of 0.16x. Proton's shares have made a spectacular recovery over the last two months given its heavily discounted valuation after having bottomed out at 0.17x P/NTA late last month.

OSK Research Guide to Investment Ratings**Buy:** Share price may exceed 10% over the next 12 months**Trading Buy:** Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months**Take Profit:** Target price has been attained. Look to accumulate at lower levels**Sell:** Share price may fall by more than 10% over the next 12 months**Not Rated:** Stock is not within regular research coverage

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