



## AmInvest Research Reports

Author: [AmInvest](#) | Latest post: Tue, 23 Oct 2018, 09:13 AM

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## MSM Malaysia - Sugar tax in Budget 2019?

Author: [AmInvest](#) | Publish date: Mon, 22 Oct 2018, 10:00 AM

### Investment Highlights

- Maintain **SELL** on MSM Malaysia with an unchanged **fair value of RM3.27/share**. Our fair value for MSM is based on an FY19F PE of 25x.
- Although MSM's net profit in FY19F is expected to be better than FY18E, we are not upgrading our recommendation for MSM yet. There are a few risks. First, if the government imposes a sugar tax during the upcoming budget on 2 November 2018, this will hurt the demand for refined sugar in the future.
- Second, it remains to be seen if MSM would be able to find sufficient customers for its new sugar refinery in Johor. The refinery, which commands an annual production capacity of one million tonnes per year, will officially commence operations in November 2018. We understand that the new refinery will sell about 100,000 tonnes of refined sugar this year. Third, if raw sugar price continues to rise, this would hurt MSM's operating profit margin.
- FY18E is expected to be challenging due to competition from imported sugar in 1HFY18, start-up costs for the new refinery in Johor in 2HFY18 and a fall in the selling price of refined sugar for the retail market in September 2018.
- Although the government has abolished the AP for imported sugar, we gather that the switch to locally produced refined sugar may only be seen in FY19F. This is because some of the AP holders still have inventory of imported sugar. They are believed to have imported 50,000 to 100,000 tonnes of refined sugar into Malaysia.
- The reduction in the selling price of refined sugar for the retail market of 10 sen/kg in September 2018 is expected to hit MSM's operating profit margin in 4QFY18. The retail market accounted for 48.3% of MSM's sales volume in 1HFY18. Although the selling price of refined sugar for the retail market has dropped, MSM's cost of raw sugar in 2HFY18 is expected to be similar to 1HFY18 as the group still has inventory of raw sugar purchased at high cost.
- We think that MSM has locked in raw sugar at US\$0.12 to US\$0.13/pound for 1QFY19. MSM is now hedging its raw sugar and forex requirements only three months ahead to be prudent. According to Bloomberg, the price of raw sugar has risen by 27.3% to US\$0.1389/pound since touching a low of US\$0.1091 on 26 September. The rise in raw sugar price was due to concerns over lower exports from Brazil resulting from the appreciation of the real.
- MSM would be recognising depreciation expense for the new sugar refinery in Johor in 4QFY18. Depreciation expense is estimated to be RM40mil p.a.. With higher depreciation expense and start-up costs and minimal revenue, the refinery is expected to erode MSM's operating profit margin in 4QFY18.

Source: [AmInvest Research](#) - 22 Oct 2018

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