AUTHOR: MIDF Research SECTION: INVESTMENT PAGE: 18 PRINTED SIZE: 267.00cm² REGION: KL
MARKET: Malaysia PHOTO: Full Color ASR: MYR 2,813.00 ITEM ID: MY0037023330

23 AUG, 2019

MSM biz conditions continue to deteriorate on ASP price war

The Malaysian Reserve, Malaysia

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▶ Recommendation: Sell
TARGET Price: RM0.88
by MIDF Research (Aug 22)

▶ MSM MALAYSIA HOLDINGS BHD				
FYE DEC 31	FY18A	FY19F	FY20F	FY21F
REVENUE (RM mil)	2,215.5	1,955.0	2,028.0	2,214.8
CORE NET INCOME (RM mil)	35.1	-140.0	-120.0	-36.0
CORE EPS (sen)	4.99	NA	NA	NA
PER (x)	29.2	NA	NA	NA

MSM Malaysia Holdings Bhd's 1H19 core losses plunged to -RM74m, compared to a profit of RM32.3m in the prior year. The larger than expected negative earnings results was predominantly due to the continued deteriorating refined sugar's average selling price (ASP) amid a worsening price war, as well as higher finance and refining cost mainly from the operation of the Johor refinery.

Falling ASP, sales volume. The group's 1H19 revenue dropped by -14.5% YoY to RM959.5m primarily as a result of lower ASP of refined sugars. The 1H19 ASP of refined sugars fell by -9.3% YoY to RM1,994 per metric tonnes (MT), a new record low in two years. Note that the group's ASP has been on the decline since 1Q17 when the ASP was still hovering around the RM2,600 level. Total sales volume has also waned by -3.3% YoY to 446m/MT. This was mainly attributable to the liberalisation of the sugar industry (ie increase in approved permits), which gave rise to an oversupply of cheaper foreign refined sugars in the domestic market.

Moving forward, we are of the view that its ASP of refined sugars and volume will continue to face an uphill battle to see signs of recovery in the foreseeable future.

Operating loss to persist. On top of the poor ASP of refined sugars, the operating loss was further exacerbated by higher finance and refining cost arising mainly from its Johor refinery plant. Note that 1H19's finance cost has risen by +287% YoY to -RM48.4m as a result of modification to certain terms in respect of the Islamic term loan, which was an accounting impact. Management guided that the finance cost was expected to normalise in coming quarters to around the RM20m level. In addition, the low utilisation rate of the Johor refinery of between 20% and 30% contributed to higher refining cost, which further weigh on the margin. We expect the utilisation rate to remain low in view of the competitive sugar market.

Earnings revised downward. We are reducing further our FY19 and FY20 core losses to -RM140m and -RM120m respectively in view of the current heightened domestic sugar price war and dwindling sales demand, as well as higher refining and finance cost.

Valuation. Subsequent to our earnings adjustment, we are deriving a new target price of RM0.88 (previously RM1.07). Our valuation is based on forecast FY20 book value per share of RM1.76 to its two-year historical price-to-book ratio of 0.5x.

The outlook of the group's fundamentals remains bleak as it continues to be suffered from lower ASP of its refined sugars and higher operating costs. This negative repercussions from the liberalisation of the sugar industry by the government have also been reverberating across MSM's domestic market where it derives approximately 90% of its revenue. We maintain our 'Sell' recommendation on the stock.

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SUMMARIES

MSM Malaysia Holdings Bhd's 1H19 core losses plunged to -RM74m, compared to a profit of RM32.3m in the prior year. The larger than expected negative earnings results was predominantly due to the continued deteriorating refined sugar's average selling price (ASP) amid a worsening price war, as well as higher finance and refining cost mainly from the operation of the Johor refinery. Falling ASP, sales volume. The group's 1H19 revenue dropped by -14.