

Uncertainty looms over MSM

BY JOSE BARROCK

Sugar refiner MSM Malaysia Holdings Bhd is likely to have to swallow a bitter pill should the new government cut sugar prices in its attempt to reduce the cost of living.

Last week, Deputy Minister of Domestic Trade and Consumer Affairs Chong Chieng Jen said the ministry was looking to negotiate for lower prices with sugar refiners and issue more approved permits (APs) for the sugar imports, thus encouraging competition and driving prices down.

Chong, however, said the current retail price of coarse sugar in Malaysia of RM2.95 per kg is already the lowest in Asia. The price of sugar in Indonesia, Vietnam and Singapore is RM3.58, RM4.41 and RM4.65 per kg respectively.

It may be too early to draw any conclusion

on the significance of a price cut for sugar refiners. But it is apparent that this will not augur well for MSM's earnings prospects.

When contacted, MSM executive director Datuk Khairil Anuar Aziz says he hopes the government will take into consideration the plight of the sugar refiners before any decision is made.

"Our (refined sugar) prices are already among the lowest in the world. We hope the government will consider our plight. Actually, the government should support us, we provide employment," he says.

MSM — a 51%-owned unit of FGV Holdings Bhd (in which the Federal Land Development Authority controls 33.67%) — together with businessman Tan Sri Syed Mokhtar Albukhary's Tradewinds Bhd, controls the sugar refining capacity locally.

MSM controls MSM Prai Bhd — which oper-

ates the Prai sugar refinery in Penang — MSM Perlis Sdn Bhd and MSM Sugar Refinery (Johor) Sdn Bhd, which commenced operations recently.

It has a workforce of 1,244, according to its 2017 annual report. But this figure could have increased by now.

MSM spent RM1.1 billion on building a new refinery in Johor, which came onstream last month. Including this plant, MSM and Tradewinds have a refining capacity of three million tonnes of sugar a year.

"Malaysia's consumption of [refined] sugar is only 1.5 million to 1.6 million tonnes per annum," Khairil says, suggesting that the move to issue more APs may not be a wise one.

Apart from the two refiners, there are also a handful of companies that have been given APs to bring in refined sugar, such as Nerdz Resources Sdn Bhd — which was allowed to import 10,000 tonnes for eight months, from

May to December last year — and a couple of firms linked to businessman Tan Sri Tan Kean Soon and politician cum businessman Datuk Seri Tiong King Sing.

"[So] we (MSM) are far from a monopoly," Khairil tells *The Edge* over the phone.

"We have a lot of obligations. We have to bear the import costs, transport costs, we pay taxes, we pay zakat and our business is [adversely] impacted by foreign exchange. We are at the mercy of world [raw sugar] prices. This year, there has been a glut [of refined sugar], but it is a cyclical business, so things will pick up.

"We are already saddled with higher gas tariffs and electricity charges, and soon, we will have [to fork out] more when the minimum wage [is increased]."

Mounting cost pressure

Last month, gas prices were raised to RM32.69 per million British thermal units (MMBtu) from RM32.52 per MMBtu for the non-power sector in Peninsular Malaysia while electricity tariffs for the commercial sector rose following the implementation of the imbalance cost pass-through (ICPT) mechanism.

Under the ICPT mechanism, non-domestic users are no longer given a rebate of 1.52 sen per kilowatt-hour (kWh) and are required to pay an ICPT surcharge of 1.35 sen per kWh, meaning a non-domestic user faces an increase of 2.87 sen per kWh, or 6.6%.

On top of that, the government intends to raise the minimum wage from the current RM1,000 in Peninsular Malaysia and RM920 in Sabah and Sarawak to RM1,500 by the end of Pakatan Harapan's first administration term.

Khairil says at the rate things are going, MSM may have to scale down operations and possibly even shut down one of its refineries. Consequently, it may have to lay off some workers.

However, the move by the government may not be a surprise to some.

In a report released in late May, GCS CIMB says, "The new Pakatan Harapan government has indicated in its election manifesto that it intends to lower the cost of living of the people. As such, we think there is a risk it may consider reviewing and potentially lowering the ceiling price of refined sugar in view of lower raw sugar prices, which will be a negative for MSM."

For its first financial quarter ended March this year, MSM registered a net profit of RM15.81 million on revenue of RM549.06 million. For the corresponding period a year ago, it suffered a net loss of RM34.62 million on revenue of RM640.05 million.

In a review of its financial performance, MSM says its revenue fell 14.2% as a result of a 7% dip in its tonnage sold and a lower average selling price.

"We expect a better 2Q2018 but weaker 2H2018 earnings for the group due to the negative impact of higher depreciation and interest expense costs relating to its new sugar refinery in Johor, which cost RM1.1 billion," says GCS CIMB.

The research outfit has maintained a "reduce" call on MSM and has cut its FY18-FY20F EPS by 41%-55% to reflect the lower refining margins and poor 1Q results. It forecast MSM registering RM69 million in net profit from RM2.43 billion in revenue for the current financial year ending Dec 31.

In line with the earnings downgrade, GCS CIMB has lowered its target price to RM2.77, based on a price-to-book value of one times. MSM closed last Thursday at RM3.80 per share, which means that GCS CIMB pegged a 27% discount to its target price.

"We continue to rate MSM a 'reduce', given its rich valuations, potential losses from its new sugar refinery and a rising net gearing ratio (52% as at March 31, 2018)."