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Stock Digest

Thursday, 21 Apr, 2022

M+ Online
Malacca Securities Sdn Bhd
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Malaysia Smelting Corporation Bhd

Global integrated tin mining & smelting player

- **Malaysia Smelting Corporation Bhd (MSC) history traces back to 1902 and is now ranked as one of the largest producer of tin metal and tin-based products in the world with total smelting capacity of 80,000 MT pa.**
- **Tin mining production is gradually on the uptrend, owing to better production efficiency, while new smelting plant at Pulau Indah is expected to anchor the smelting division's growth.**
- **We initiate coverage on MSC with a HOLD call and fair value of RM5.36, based on 13.0x P/E pegged to its forward FY23f EPS of 41.2 sen.**

Investment Highlights

- **Largest local integrated tin mining and smelting player**. Through Rahman Hydraulic Tin Sdn Bhd, MSC owns the largest and one of the oldest tin mines in Malaysia since 2004 that spans across 267.3-ha and is equipped with 1.0MW hydropower station. The mine has a mining lease till November 2034 and has consistently delivered improvement mining output throughout the years. Today, MSC is ranked as one of the largest producer of tin metal and tin-based products in the world.

- **Well supported by 2 smelting plants.** MSC currently operates 2 smelting facilities with a total annual production capacity of 40,000 MT each, with the newer plant (located at Pulau Indah) that is equipped with the cutting-edge Top Submerged Lance (TSL) furnace able to scale up the annual production capacity to 60,000 MT through oxygen enrichment process.

- **Leveraging onto elevated tin prices.** Tin prices have hit a historical all-time high level (above USD 50,000 MT) in March 2022. While the rally has cooled off in recent weeks, we think that tin prices will stay elevated above the pre-pandemic levels, owing to the supply shortage and rising demand from the gradual electric vehicles production, usage of electronic devices and the focus towards ESG practices through the installation of solar PV both residential and commercial premises.

Financial highlights

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Revenue	813.4	1,076.6	1,495.3	1,594.2	1,686.3
EBITDA	60.0	181.4	254.2	263.0	274.0
PATMI - Core	15.2	118.1	166.1	173.0	181.8
PATMI - Reported	14.7	118.5	167.0	173.9	182.7
Revenue growth (%)	-17.3%	32.4%	38.9%	6.6%	5.8%
Core PATMI growth (%)	-50.6%	678.5%	40.7%	4.1%	5.1%
Core EPS (sen)	3.6	28.1	39.6	41.2	43.3
P/E (x)	144.0	18.5	13.1	12.6	12.0
DPS (sen)	2.0	7.0	10.0	11.0	11.0
Dividend yield (%)	0.4%	1.3%	1.9%	2.1%	2.1%
P/B (x)	5.6	3.8	3.1	2.6	2.3
ROE (%)	3.9%	20.3%	23.6%	20.8%	18.8%
Net Gearing (%)	94.8%	58.2%	40.1%	27.9%	2.7%

Source: MSC, M+ Online

Initiation Coverage

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HOLD

Share price	**RM5.20**
Target price	**RM5.36**
Previous TP	-
Capital upside	3.0%
Dividend return	2.1%
Total return	5.1%

Company profile

Principally involved in tin mining and smelting

Stock information	
Bursa Code	5916
Bloomberg ticker	SMELT MK
Listing market	MAIN
Share issued (m)	420.0
Market Cap (m)	2,184.0
52W High/Low	5.46 / 1.74
Est. Free float	44.2
Beta	0.7
3-mth avg vol ('000)	1,537.7
Shariah compliant	No

Major shareholders	%
Straits Trading Co Ltd	26.8
Straits Trading Amg	16.6
Sword Investments Pvt Ltd	5.1

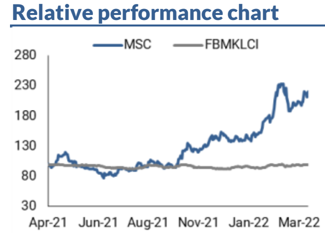
Share price vs. KLCI (%)

Hist. return	1M	3M	12M
Absolute	12.6	54.5	147.3
Relative	12.6	48.6	131.0

Earnings snapshot

FYE (Dec)	FY21	FY22f	FY23f
PATMI (m)	118.1	166.1	173.0
EPS (sen)	28.1	39.6	41.2
P/E (x)	17.9	12.7	12.2

Relative performance chart



Company Background

- **Global Integrated Tin Mining & Smelting Group**. With over 100 years of operational history, MSC is regarded as one of the leading global tin players that operates Malaysia's largest tin mine at Klian Intan, Perak with a mining lease until November 2034. MSC is also touted to be one of the world's largest toll smelters with tin ore capacity of 60,000 Metric Tonnes per annum (Mtpa), smelting third party tin concentrates from all over the world.

- **History traces back for more than 100 years**. Malaysia Smelting Corporation Bhd (MSC) history traces back to 1902 following a site purchase in Butterworth and official smelting works commenced during the year. Throughout the years, the group has expanded and successfully made its debut on the Main Market of Bursa Malaysia in 1994.

- **Strengthening core business**. In 2004, the group expanded upstream in tin mining with the acquisition of Rahman Hydraulic Tin Sdn Bhd, which owns the largest and one of the oldest hard rock open-pit tin mines in Malaysia. This subsequently transformed MSC into a fully integrated tin producer. Thereafter in 2014, Rahman Hydraulic Tin acquired 80.0% interest in SL Tin Sdn. Bhd, a company that holds a mining lease over an area of 267.3-ha in Sungai Lembing, Pahang, for a period of 15 years. Meanwhile, MSC has divested its mining subsidiaries in Indonesia to focus on its operations in Malaysia.

- **Expansion in Pulau Indah**. In 2016, MSC embarked on a new phase of expansion with the acquisition of 3 parcels of industrial land, plant and machinery inclusive of a production facility in Pulau Indah, Klang for RM50.0m. Originally a lead smelter, MSC has retrofitted the plant to become one of the most modern tin smelters in the region equipped with the cutting-edge Top Submerged Lance (TSL) furnace.

Business Model

Source: MSC, M+ Online

- **Tin Mining**. Tin mining refers to activities involving the exploration for and mining of tin. Tin ores are extracted and processed into tin-in-concentrates to support smelting activities.

- MSC currently owns and operates the largest hard rock open-pit tin mine in Malaysia located at Klian Intan, Perak with a mining lease for a period till 11th November 2034 through Rahman Hydraulic Tin Sdn Bhd (RHT). The tin mine has an area of 700-ha and is equipped with 1.0MW hydropower station to generate energy. Since the acquisition in 2004, MSC has undertaken improvement works in mining and pit operations to enhance efficiencies. As a result, tin-in-concentrates production has grown more than three-fold from 750 tonnes in 2004 to 2,408 tonnes in 2021.

- Meanwhile, RHT also owns 80.0% stake in SL Tin Sdn Bhd that has a mining lease over a 267.3-ha area in Sungai Lembing, Hulu Kuantan, in Pahang for a period of 15 years. We gathered that Sungai Lembing mine has commenced commercial production in FY21 with modest production. Upon full operations, the mine is expected to contribute 1,200 MTpa.

- We understand that ores produced by RHT is high grade, containing 73.0-75.0% of tin vs the world average at 60.0%. In 2021, nett tin ore production stood at 2,408MT (+2.5% YoY).

- MSC is able to leverage onto the rising average selling prices (ASP) of tin, whereby average tin prices stood at RM130,575/MT in FY2021 (+82.5% YoY). As such, the tin mining pre-tax profit surged 372.1% YoY to RM145.2m in FY21.

- Moving forward, we expect average tin prices to hover at an average of RM123,000/MT (USD30,000 with an exchange rate assumption of USD/MYR at 4.10) for FY22f. This is premised to the progress of economic recovery that will continue to drive demand alongside with the higher global consumption from the usage in electric vehicles (EV), solar photovoltaic (PV) installations and electronic applications.

Rahman Hydraulic Tin Mine

Source: MSC

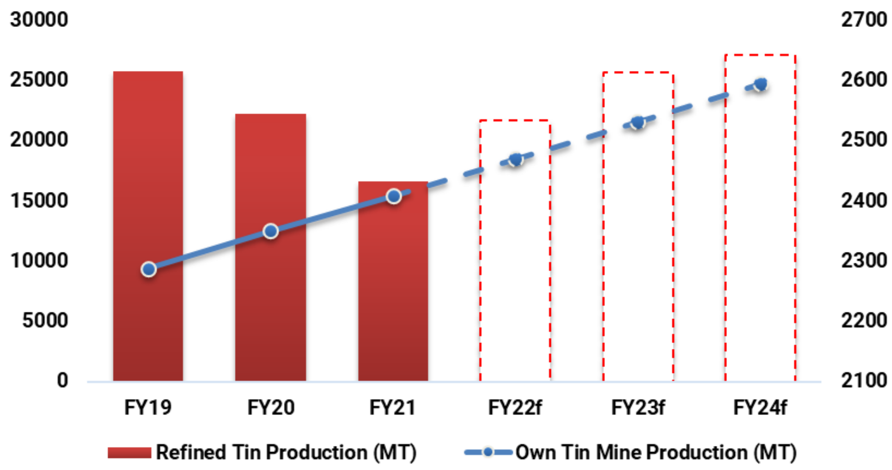
- **Tin Smelting.** Tin smelting refers to the process of smelting of tin-in-concentrates and tin bearing materials to produce various grades of refined tin metal for the sale and delivery of refined tin metal and byproducts. MSC started their tin smelting business in 1887.

- Apart from its tin ore production from the RHT mine, MSC procures tin ores from other mines in Malaysia and the rest of the world to undertake the smelting process. MSC currently has 2 smelting facilities located at (i) Butterworth, Penang and (ii) Pulau Indah, Selangor. Both smelters have an annual production capacity of 40,000 MT each, with the latter plant able to scale up the annual production capacity to 60,000 MT through oxygen enrichment process. This process involves pumping in oxygen to improve production capacity.

- The Butterworth smelter uses reverberatory furnace that involves multi-stage smelting process. Meanwhile, the Pulau Indah smelter is equipped with state-of-the-art technology using Top Submerge Lance (TSL) that involves single stage smelting process. The latter allows MSC to reap better margins from better yields and operational efficiency through automation which lowers manpower requirements from 550 to 300 employees. The new smelter is also more environmentally-friendly with the installation of 1.26MWp solar photovoltaic panels on the rooftop of the plant, as well as a waste heat recovery system to harness thermal energy to generate power.

- We came to understand that MSC plans to de-commission the Butterworth smelter over the next couple of years. With a total of 40.1-ac (MSC portion of 13.9-ac and STC portion of 26.2-ac), the Butterworth land has been earmarked for a mixed residential and commercial development project. As the focus now shifts to the Pulau Indah smelter that operates the TSL furnace, this allows the group to improve operational efficiency. The new plant is also strategically located in close proximity to Westport and London Metal Exchange (LME) warehouse, which then reduce logistical cost.

Historical & Forecasted Tin Production



Source: MSC, M+ Online

- Over the past 2 years (2020 & 2021), MSC recorded lower refined tin production, with its operations temporarily halted in adherence to the Movement Control Order (MCO) due to the COVID-19 pandemic. MSC also instituted a force majeure that was in effect from 7th June 2021 to 20th December 2021. For FY21, refined tin production fell 25.3% YoY to 16,619MT. As at end-FY21, the Butterworth smelter is operating at 67.0% capacity, while the Pulau Indah smelter is operating at 75.0% capacity.

- We also gather that MSC has commenced the smelting of tin intermediates from 3QFY21 with net reduction of 343 MT of tin intermediates were processed in FY21. For FY21, the tin smelting pre-tax profit soared 363.9% YoY to RM18.2m, supported by higher profit margins from sales of refined tin derived from its tin intermediates.

- For FY21, the refined tin production fell 25.3% YoY to 16,619MT. Moving forward, we expect refined tin production to see improvement, climbing back above 20,000 level in FY22f as Pulau Indah smelting plant has completed refurbishment in 2021 and is expected to operate at close to optimum capacity (barring any unforeseen further closures).

Outlook

- **Full production coming on stream.** With Malaysia entering into the endemic phase, we believe that there would be no further lockdowns moving forward and the Pulau Indah smelter would be able to operate at full capacity from 2022. With more than half a year of force majeure closure, MSC will be kept busy with the smelting of tin ores backlog from the Covid-19 pandemic as well as tin intermediates of 6,555 MT**.**

- **Continuous efforts to improve mining output.** We understand that MSC is continuously making efforts to improve mining output and efficiencies through mechanisation of processes and exploring new mining methodologies at RHT tin mine site. As a result, daily production of tin ore reached 11.0 MT per day in FY21, and is expected to increase to 12.0 MT per day in 2022.

- **Tin prices to stay elevated.** We gather that tin prices hit a historical all-time high level of USD50,025 MT on 8th March 2022. Despite the rally cooling off in recent weeks, we think that tin prices will stay elevated above the pre-pandemic levels, owing to the supply shortage and rising demand. Demand is expected to be driven by the gradual transitioning into electric vehicles, rising demand for electronic devices alongside technological advancement and focus on ESG measures with increasing numbers of households and commercials undertaking the installation of solar PV at their premises.

Historical Tin Prices per Metric Tonne (USD)

Source: Bloomberg

SWOT Analysis

Strength	Weakness
• Malaysia's largest tin player • Consistent improvement in tin mining output	• Labour and capital intensive • Dependency on single product (tin)
Opportunity	**Threat**
• Ramping up Pulau Indah's smelting operations • Riding onto the elevated tin prices • Unlocking value through Butterworth land disposal	• Fluctuation in tin prices may affect margins • Fluctuation in foreign exchange rates between USD and RM

Source: M+ Online

Financials

- Following a downbeat performance in FY20 (net profit sank 50.6% YoY to RM15.2m) that was marred by Covid-19, MSC has responded with a sharp uptick with net profit surging to record high of RM118.1m. Despite being affected by the force majeure closure of its smelting plants from 7th June 2021 to 20th December 2021, the sky-rocketing tin prices to record high levels lifted the group's overall performance.

- For FY22f, we reckon that MSC would be able to deliver another year of solid improvement, backed by the resumption of its production activities at full-scale and the elevated tin prices. With the smelting production expected to operate at full scale, we expect bottomline to record improvement of +40.7% YoY to RM166.1m. Although we anticipate tin prices to soften in 2H22, prices are expected to remain above pre-pandemic levels and the more efficient production process from the Pulau Indah smelter will keep margins intact.

- We expect improvements in subsequent years (both FY23f and FY24f) to be supported by the gradual improvement in tin mining progress as well as the better efficiency from Pulau Indah smelting plant. The upcoming supply stream would likely to be absorbed gradual improvement of demand, particularly from consumer electronic devices, progressive transitioning into EV and increasing demand of solar photovoltaic panels.

- Given much of CAPEX (approximately RM150.0m) have been spent for the Pulau Indah smelting plant, we foresee that CAPEX is expected to remain minimal with only the additions of 3 rotary furnaces (valued approximately RM1.0m each), going forward. Thereafter, we expect gradual paring down of their debt level with net gearing to stay below 0.5x.

Valuations

- At RM5.20, MSC is trading at PERs for FY22f and FY23f of 13.1x and 12.6x, respectively. We assigned a P/E multiple of 13.0x to FY23f EPS of 41.2 sen, arriving at a fair value of RM5.36.

- We gather that MSC is trading close the local and regional peers' average P/E multiple of 13.6x for 2022f. The assigned target P/E represents a slight discount to the average of 14.0x of selected tin-related and mining companies listed on Bursa Malaysia as well as international scale.

- We also came to understand that MSC does not have any formal dividend policy. Still, the group is committing to carve out approximately 25.0% pay-out from net profit as dividends, barring any unforeseen circumstances. For FY21, MSC has declared a total dividend of 7.0 sen per share. Moving forward, we have imputed an assumption pay out of 10.0-11.0 sen over the next 3 years, representing pay-out ratio of 25.0-27.0% from FY22f to FY24f.

Peers comparison

Company	Market Group	FYE	Price (RM)	Market Cap (RM 'm)	P/E (x) FY21	P/E (x) FY22f	Gross DY (%)	Revenue (RM 'm)	Net Income (RM 'm)
Malaysia Smelting Corporation Bhd	**MAIN**	**Dec**	**5.20**	**2184.0**	**18.5**	**13.1**	**1.3**	**1076.6**	**118.1**
Local									
Press Metal Holdings Bhd	MAIN	Dec	6.55	52898.8	51.3	25.2	1.7	10994.2	1030.5
OM Holdings Ltd	MAIN	Dec	2.86	2112.5	8.3	7.7	2.1	3238.8	254.9
Perusahaan Sadur Timah Malaysia Bh	MAIN	Mar	4.01	517.7	9.9	11.2	5.0	832.5	52.2
International									
Timah Tbk PT	-	Dec	1990.00	14821028.5	10.8	12.1	2.8	14607.0	1302.8
Avg ex-Malaysia Smelting Corporation Bhd					**20.1**	**14.0**	**2.9**	**7418.1**	**660.1**

**Timah Tbk PT metrics are based on IDR*

Source: Bloomberg, M+ Online

Investment risks

- **Slowdown in demand for tin and related products.** Given that MSC sales are largely dependent on the demand for tin and related products, a downturn tin and related products demand would hamper the utilisation rates of the smelters.

- **Fluctuation in raw material prices.** Average selling prices are largely correlated with the raw material prices. Any fluctuation in raw material prices, namely tin prices due to the demand-supply imbalances may trigger changes in revenue and margins assumption.

- **Exposure to currency risk.** Given that tin prices are traded in USD, and MSC purchased most of their raw material from other miners, the group runs the risk of volatility in foreign exchange markets. With most of the products are also sold in USD, a stronger Greenback against the ringgit would benefit MSC and vice versa.

Financial Highlights

Income Statement

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Revenue	**813.4**	**1,076.6**	**1,495.3**	**1,594.2**	**1,686.3**
EBITDA	60.0	181.4	254.2	263.0	274.0
EBIT	42.8	169.3	239.0	247.3	257.8
Net finance income/ (cost)	(14.8)	(15.4)	(17.1)	(16.3)	(15.0)
Associates & JV	(4.3)	4.4	3.7	4.0	4.2
Profit before tax	**24.2**	**158.4**	**225.6**	**235.0**	**246.9**
Tax	9.5	39.9	58.7	61.1	64.2
Net profit	**14.7**	**118.5**	**167.0**	**173.9**	**182.7**
Minority interest	(0.5)	0.4	0.8	0.9	0.9
Core earnings	**15.2**	**118.1**	**166.1**	**173.0**	**181.8**
Exceptional items	-	-	-	-	-
Reported earnings	15.2	118.1	166.1	173.0	181.8

Cash Flow Statement

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Profit before taxation	24.2	158.4	225.6	235.0	246.9
Depreciation & amortisation	17.1	12.0	15.2	15.7	16.3
Changes in working capital	(137.5)	(92.5)	92.8	27.8	79.5
Share of JV profits	-	-	-	-	-
Taxation	(5.1)	(8.1)	(1.7)	(2.1)	(4.0)
Others	15.5	(16.5)	(20.0)	(20.0)	(20.0)
Operating cash flow	**(106.4)**	**12.6**	**163.7**	**158.5**	**172.8**
Net capex	(14.7)	(9.0)	0.3	7.2	8.2
Others	(1.1)	(0.5)	-	-	-
Investing cash flow	**(15.8)**	**(9.5)**	**0.3**	**7.2**	**8.2**
Changes in borrowings	131.4	49.5	(150.0)	(200.0)	(200.0)
Issuance of shares	-	-	-	-	-
Dividends paid	(8.0)	(4.0)	(42.0)	(46.2)	(46.2)
Others	-	37.2	-	-	-
Financing cash flow	**123.4**	**82.7**	**(192.0)**	**(246.2)**	**(246.2)**
Net cash flow	**1.1**	**85.8**	**(28.0)**	**(80.4)**	**(65.2)**
Forex	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
Others	-	-	-	-	-
Beginning cash	35.7	36.8	122.6	166.5	205.9
Ending cash	36.8	122.6	166.5	205.9	400.9

Balance Sheet

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Cash	37.5	122.6	166.5	205.9	400.9
Receivables	25.6	11.3	20.5	21.8	23.1
Inventories	604.1	789.9	829.6	818.9	866.2
PPE	216.6	216.9	224.1	232.4	241.4
Others	110.7	173.8	166.3	206.8	206.9
Assets	**994.5**	**1,314.4**	**1,407.0**	**1,485.7**	**1,738.5**
Debts	410.4	460.7	449.2	438.0	427.0
Payables	133.1	187.9	237.1	255.7	300.2
Others	57.7	85.1	40.5	99.6	43.8
Liabilities	**601.2**	**733.7**	**726.8**	**793.3**	**771.0**
Shareholder's equity	364.5	371.7	522.9	647.1	773.9
Minority interest	(0.2)	0.2	0.5	0.5	0.5
Equity	**393.3**	**580.6**	**705.1**	**831.9**	**967.5**

Valuation & Ratios

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Core EPS (sen)	3.6	28.1	39.6	41.2	43.3
P/E (x)	144.0	18.5	13.1	12.6	12.0
DPS (sen)	2.0	7.0	10.0	11.0	11.0
Dividend yield	0.4%	1.3%	1.9%	2.1%	2.1%
BVPS (RM)	0.94	1.38	1.68	1.98	2.30
P/B (x)	5.6	3.8	3.1	2.6	2.3
EBITDA margin	7.4%	16.8%	17.0%	16.5%	16.3%
EBIT margin	5.3%	15.7%	16.0%	15.5%	15.3%
PBT margin	3.0%	14.7%	15.1%	14.7%	14.6%
PAT margin	1.8%	11.0%	11.2%	10.9%	10.8%
Core PAT margin	1.9%	11.0%	11.1%	10.9%	10.8%
ROE	3.9%	20.3%	23.6%	20.8%	18.8%
ROA	1.5%	9.0%	11.8%	11.6%	10.5%
Net gearing	94.8%	58.2%	40.1%	27.9%	2.7%