

07 September 2021

Malaysia Smelting Corp

The World's Largest Toll Smelter

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Last Price: RM2.36

	Rating	Fair Value
Kenanga Consensus	Not Rated N/A	RM2.32 N/A

INVESTMENT MERIT

MSC, a world's leading tin smelter with 120 years of history, stands poised to benefit from a new and modern smelting plant in Pulau Indah replacing the aging inefficient smelter in Butterworth. The new plant capacity is 50% higher than the old one and uses superior smelting technology that saves cost by 30%. In addition, there is potential value unlocking of the Butterworth's plant site. Nonetheless, with LME tin prices at all-time-high coupled with its share price surging 65% YTD, MSC appears to have fairly priced in all the positive catalysts. Not Rated.

The world's largest toll smelter. Malaysia Smelting Corporation Bhd (MSC) is one of the world's leading integrated producers of tin metal and tin-based products with 120 years of history. It is involved in the upstream and downstream sectors of the tin industry through tin mining and custom tin smelting. MSC owns the country's largest tin mine, Rahman Hydraulic Tin Mine (RHT) in Pangkalan Hulu, Perak. Established since 1902 as a smelting plant in Butterworth, it is today the world's largest toll smelter, smelting third-party tin concentrates from all over the world. Its current smelting facilities are able to handle tin ore capacity of 40,000 MTPA.

New smelting plant, a game changer. The new Pulau Indah Plant, with total capex RM130m, is equipped with cutting-edge smelting technology of top submerged lance furnace which will see significant improvement in reaction and production rates as opposed to the aging reverberatory furnace in Butterworth plant. Its enhanced extractive yield in the single-stage smelting system will free up tin caught in intermediates occurring in the old facility. It also has low labour requirement of 300 employees vs. 550 workers in the old facility. In addition, it has a smaller carbon footprint with the use of natural gas, solar panels and waste heat recovery. Once the new facility is fully commissioned with 60,000 MTPA by this year-end or early of next year, cost savings is c.30% against the old facility in Butterworth.

Unlocking value of Butterworth site. A redevelopment of the Butterworth smelting plant site is already planned to unlock the land value once the smelting operations is fully relocated to Pulau Indah. The smelting facility is sitting on 13.9 acres of land while the parent company Straits Trading Company (STC) owns the adjacent piece of land spanning 26.2 acres. The combined land will be redeveloped into a mixed residential and commercial property project and a master plan has been approved with STC which is in property development to head the development. Meanwhile, development works are being carried out on the 26.2 acre STC land currently while MSC's 13.9 acre land, which with book value of RM78.7m, will only see work commencing three years later after the smelting operations cease.

Tin prices off all-time high of USD35,798/MT in mid-Aug, to USD33,055/MT last Friday. Tin price has risen 63% YTD due to supply-demand dynamic where supply was constrained by lockdown disrupting mine output and shipping routes with strong demand emanating from booming sales of electronics in the work-from-home era. Also, the world's top tin producer China is still likely to be disrupted by environment constraints while the world's largest exporter Indonesia has seen declining exports owing to regulatory policies. Meanwhile, tin demand will continue to rise in view of elevated demand in electronics which consumes tin while demand for tin metal compound in lithium-ion batteries will grow stronger as more EVs are introduced.

A good ESG profile. In today's investment world, ESG has become a very important metrics for investor to value companies. And, MSC has made efforts to improve its ESG rating, such as the new smelting plant having green energy efficiency initiatives while RHT is powered by 1.0MW hydro energy. It has also invested RM6.7m in environmental initiatives coupled with other ESG efforts.

Near-term positive priced in; Not Rated. While we expect FY21 earnings to triple on the back of strong tin prices, we expect tin prices to taper off as the supply-demand equilibrium will slowly skew back to pre-COVID situation, in FY22-FY23 where we expect earnings to grow at 23-24% on the overall structural cost savings from the new plant. As such, we believe MSC should value at +0.5SD to its 3-year mean of 13.6x from its mean level of 11.6x given a reasonable earnings growth for the next two years. This values MSC at RM2.32.

Stock Information

Shariah Status	No
Stock Name	Malaysia Smelting Corp Bhd
CAT Code	5916
Industry	Commodity
Industry Sub-sector	Tin Mining & Smelting
YTD stock price chg	65.03%
Market Cap (RM m)	991.20
Issued shares (m)	420.00
52-week range (Hi)	2.93
52-week range (Low)	0.675
3-mth avg daily vol:	703,375
Free Float	44.3%
Beta	1.03
Altman's Z-score	2.42

Major Shareholders

Straits Trading Co Ltd	26.8%
Straits Trading Amalgamate	16.6%
Sword Investments Private Limited	5.1%

Financials

FY Dec (RM m)	2020A	2021E	2022E
Revenue	813.4	1,304.1	1,207.5
EBITDA	60.6	111.2	135.4
Profit Before Tax	24.2	75.7	92.0
Net Profit	15.2	58.4	71.9
EPS (sen)	3.8	13.9	17.1
BV/Share (RM)	1.0	1.1	1.3
PER (x)	62.8	17.1	13.9
P/B (x)	2.4	2.1	1.9
Net Gearing (x)	0.95	0.96	0.82
DPS (sen)	2.0	3.5	4.3
Div Yield (%)	0.8	1.5	1.8

Quarterly Financial

Data (RM m)	3Q20	4Q20	1Q21
Revenue	232.6	275.9	327.1
PBT/(LBT)	22.1	30.2	4.1
Net Profit	15.9	22.1	2.9
Basic EPS (sen)	3.8	13.9	17.1
Revenue Growth (QoQ)	-35.6	18.6	18.6
EPS growth (QoQ)	26.5	39.5	-86.8
Net Margin	6.8	8.0	0.9

Peers Comparisons

	PER (FY22E)	Div. Yld (%)	Mkt Cap (USD m)
Yunnan Tin (China)	15.6	N/A	5,784
PT Timah (Indonesia)	39.6	1.0	790
Minsur SA (Peru)	N/A	N/A	1,831

Average 27.6 1.0

Daily Charting – Malaysia Smelting Corporation



Comment: After peaking at RM2.93 in February this year, the stock formed a double-top pattern before correcting 40% to find support at the 50% Fibonacci retracement level of RM1.77. Since then, the stock has been on an uptrend, forming both higher highs and lows and thus, drawing an ascending channel. The MACD on the weekly timeframe also confirms that the long-term downward momentum has waned, with upward momentum gaining steam. Based on the above, coupled with a bullish parabolic SAR indicator, we believe the stock may continue moving higher and potentially testing the resistance levels of RM2.59 (R1) and RM2.92 (R2). Conversely, downside support can be found at RM2.13 (S1) and RM1.86 (S2).

Source: Kenanga Research

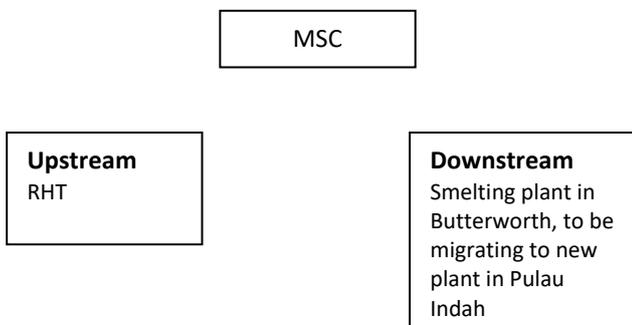
About the stock:

Name : Malaysia Smelting Corp Bhd
Bursa Code : MSC
CAT Code : 5916

Key Support & Resistance level

Resistance : RM2.59 (R1) RM2.92 (R2)
Support : RM2.13 (S1) RM1.86 (S2)
Outlook : Positive

CORPORATE STRUCTURE



BUSINESS OVERVIEW

Started as a smelting plant in Butterworth since 1902, MSC is the world's largest toll smelter, smelting third party tin concentrates from all over the world. It is replacing its aging reverberation furnaces, upgrading its smelting technology via relocating to a new and modern plant in Pulau Indah. This will increase its smelting capacity to 60,000 MTPA from 40,000 MTPA currently. On the other hand, through RHT which was acquired in Nov 2004, MSC owns the country's largest open-pit alluvial tin mine, Rahman Hydraulic Tine Mine, located in Pangkalan Hulu, Perak.

BUSINESS SEGMENTS

MSC business are segmented into upstream tin mining through RHT and downstream smelting plant which is in the midst of migrating from Butterworth plant to new facility in Pulau Indah.

The Company

• Tin Mining

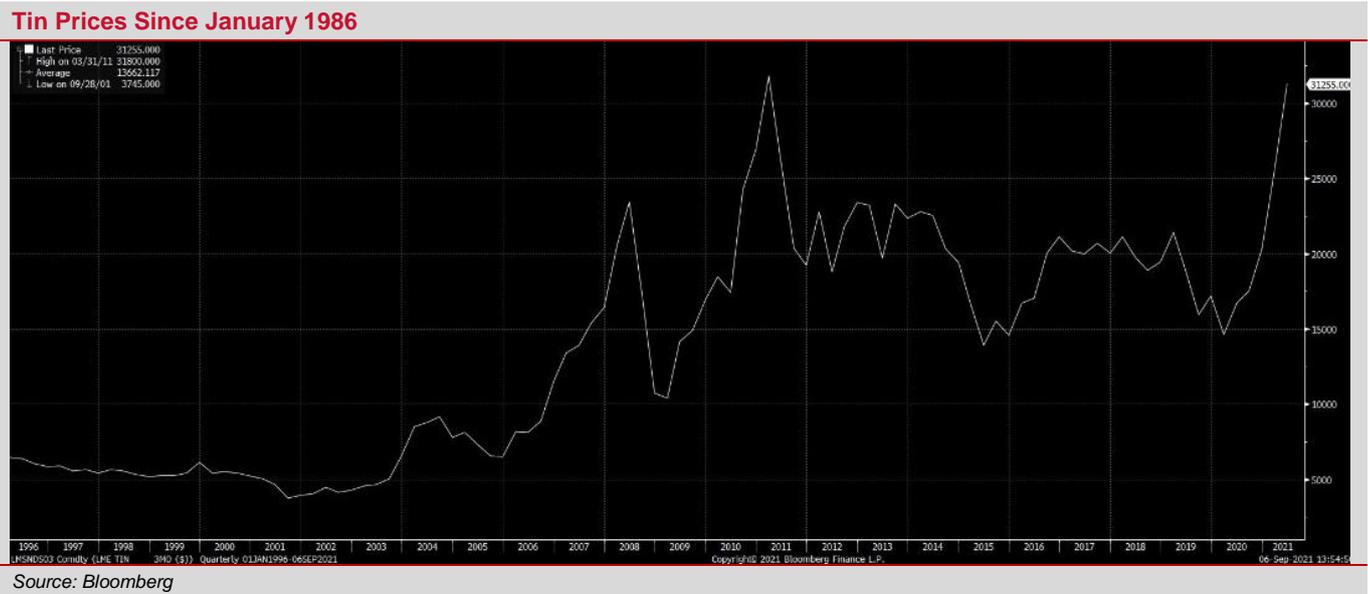
Through wholly-owned subsidiary Rahman Hydraulic Tin Sdn Bhd (RHT) which was acquired in Nov 2004, MSC has the country's largest open-pit alluvial tin mine, Rahman Hydraulic Tin Mine, located in Pangkalan Hulu, Perak. Extensive exploration works and improvement to its process flow sheet since the takeover have transformed RHT to become a very significant tin producer in Malaysia. With improved mining and processing methods and mechanised operations to expand productivity, the average daily mining output of tin ore rose from 8 to 10 MT per day in 2020. It produced a total tin concentrate of 2,350 MT in 2020. RHT, with remaining tin mining lease until Nov 2034, has estimated tin deposits of 48,403 MT valued at USD1.69b based on tin price of USD35,000/MT.

• Tin Smelting

Started as a smelting plant in Butterworth since 1902, MSC is the world's largest toll smelter as it smelts third party tin concentrates from all over the world. However, due to its aging reverberation furnaces, it is upgrading its smelting technology and relocating to a new and modern plant in Pulau Indah to gain benefits from cost savings and enhanced production efficiencies. The Pulau Indah smelting plant is currently running at 30% capacity and targeted to be 100% ready by this year-end or beginning of next year to replace the Butterworth plant by then. Currently, MSC smelting facilities are able to handle tin ore capacity of 40,000 MT per year with 22,325 MT of refined tin production in 2020.

Investment Merits

- **New smelting plant, a game changer.** The new Pulau Indah Plant (total investment cost of RM130m) is equipped with cutting-edge smelting technology of top submerged lance furnace which will see significant improvement in reaction and production rates as opposed to the aging reverberatory furnace in Butterworth plant. Its enhanced extractive yield in the single-stage smelting system will free up tin caught in intermediates like those in the old facility. The new plant also has low labour requirement of 300 employees as compared to old facility of 550 workers. In addition, it also has a smaller carbon footprint with the use of natural gas, solar panels and waste heat recovery. Management indicated that once the new facility is fully commissioned with 60,000 MT/year capacity by end of this year or early of next year, cost savings from this new plant is c.30% against its old facility in Butterworth.
- **Unlocking value of Butterworth land.** A redevelopment of the Butterworth smelting plant site is already planned to unlock the land value once the smelting plant is fully relocated to Pulau Indah. The smelting facility is sitting on 13.9 acres of land while the parent company Straits Trading Company (STC) owns the adjacent piece of land spanning 26.2 acres. Together, the combined 40.1 acres of land will be redeveloped into a mixed residential and commercial property project and a master plan has been approved. MSC and STC have entered into an agreement for STC to head the development as it is the latter which has the expertise in such property development. Meanwhile, development works are being carried out on the 26.2 acre STC land currently while MSC's 13.9 acre land will only see work commencing three years later after the smelting operations cease. As such, the value unlocking of the Butterworth land, which currently has a book value of RM78.7m, will only be realised in three years' time. However, management is unable to disclose details of STC-MSC project partnership at this juncture. Nonetheless, there is still another value unlocking from this smelting plant of 7,258MT tin intermediates valued at cost of c.USD18,000.
- **Tin prices at all-time-high.** Based on Bloomberg's available data since 1986, tin price has risen 73% YTD to an all-time-high of USD35,084/MT on 11 Aug 2021 due to supply-demand dynamic whereby supply was constrained by lockdown disrupting mine output and shipping routes while strong demand stemmed from booming sales of electronics in the work-from-home era. For the top-two tin producers; China's near-term production by small and medium sized smelters are likely to be still disrupted due to environmental constraints while the world's largest exporter Indonesia have seen declining exports over the past three years owing to changes in regulatory policies. Meanwhile, on the demand side, tin is widely used in electronic solder where the 5G revolution will also elevate demand in electronics, and tin also improves performance and lifecycle of lead acid batteries. In addition, demand for tin metal compound in lithium-ion batteries will grow stronger as more electric vehicles are introduced. All these will contribute to the continued rise in tin demand.



- A good ESG profile.** In today's investment world, ESG has become a very important metrics for investors to value companies. Companies with good ESG scores are attracting buying interest while stocks with poor ESG scores are faced with selling pressure with changing valuation metrics. On the other hand, MSC has made efforts to improve ESG such as the new smelting plant that has green energy-efficiency initiatives like 1.26MWp Solar PV panels on rooftops and waste heat recovery system. Meanwhile, its tin mining is powered by 1.0MW hydro energy. It has also invested a total of RM6.7m in environmental initiatives, RM116k in employee development and RM206k in community outreach with 76% local work-force. All these are good ESG efforts.

Earnings Profile

Financials	2018A	2019A	2020A	2021E	2022E	2023E
Revenue	1,280.9	983.6	813.4	1,304.1	1,207.5	1,134.0
EBITDA	91.1	75.6	60.6	111.2	135.4	154.9
Depreciation	-17.4	-18.5	-17.1	-17.8	-24.2	-24.2
Operating Profit	73.7	57.0	43.4	93.4	111.2	130.7
Interest Income	0.8	2.3	0.8	0.9	1.3	2.5
Interest Expense	-17.1	-15.3	-14.5	-17.4	-19.2	-17.3
Other Non-operating Gain/(Loss)	-0.1	0.7	-4.8	-1.3	-1.3	-1.4
PBT	49.8	44.7	24.2	75.7	92.0	114.5
Taxation	-15.5	-14.0	-9.5	-18.9	-22.1	-27.5
MI	0.0	0.0	0.5	1.6	2.0	2.4
Net Profit	34.3	30.7	15.2	58.4	71.9	89.5
Assumptions						
Refined Production (MT)	27,085	25,752	22,345	23,000	25,000	27,000
Average Tin Price based on revenue/Vol (MYR/MT) - (a)	47,292	38,194	36,400	56,700	48,300	42,000
Actual Tin Price (USD/MT)	20,071	18,585	17,107	27,000	23,000	20,000
USD/MYR	4,0351	4,1421	4,2006	4,2000	4,2000	4,2000
Actual Tin Price (MYR/MT) - (b)	80,989	76,983	71,858	113,400	96,600	84,000
Reported Tin Price vs. Actual Tin Price - (a/b)	58.4%	49.6%	50.7%	50.0%	50.0%	50.0%

- Earning is always about ASP and volume.** From FY18 to FY20, earnings for MSC were on the downtrend given the declining business volume and tin prices. In FY19, net profit fell 10% to RM30.7m on the back of 23% decline in revenue as production and average tin price fell 5% and 7%, respectively. With production falling further by 13% sharply on lockdown disruptions to mine output and shipping routes, coupled with 8% decline in average tin prices over the year, FY20 results were badly hit with net profit plunging 52% to RM15.2m as revenue tumbled 17%. However, in 1HFY21, MSC reported net profit of RM25.1m which was higher than the FY20 full-year net profit of RM15.2m. This was largely attributed to a strong surge in tin prices where 1HFY21 average tin prices of USD26,384/MT was 54% higher than the average of USD17,107/MT in FY20.

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- New plant's efficiency to lead earnings growth.** With tin prices continuing to trend upward solidly, it has risen 73% YTD to all-time-high of above USD35,000/MT currently. As such, we have assumed average tin prices of USD27,000 for FY21 with a similar production volume of 23,000MT as last year. This will almost triple FY21 net profit forecast to RM58.4m. However, we expect tin prices to taper off as the supply-demand equilibrium will slowly skew back to pre-COVID situation as lockdown will be lifted once vaccination targets are met. This also means that production volume should likely improve to pre-COVID level. As such, we expect tin prices to soften from USD27,000/MT in FY21 to USD23,000/MT in FY22 and USD20,000/MT in FY23 while production volume will rise to 25,000MT (FY22) and 27,000/MT (FY23) from 23,000MT in FY21, lowering revenues by 7% and 6%, respectively. Nonetheless, we expect an overall structural cost savings of 5% and 10% as the Butterworth's plant is phased out. FY22-FY23 net profits are forecasted at RM71.9m and RM89.5m, respectively.

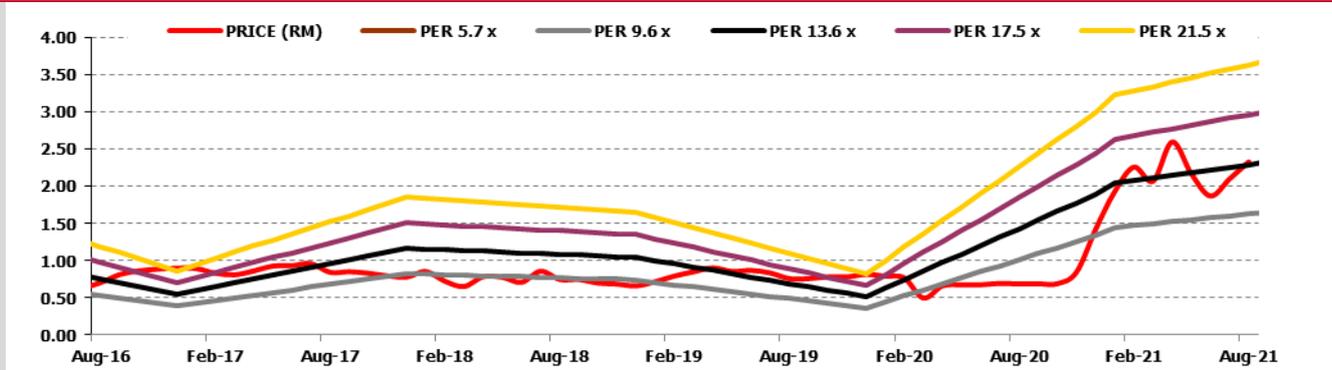
Recent Corporate Development

- Raised RM38m from private placement.** On 02 Aug, 20m new MSC shares were listed after the completion of a private placement which was priced at RM1.90/share, raising RM38m. This brought MSC's total issued shares to 420m shares or issued share capital of RM238m. It has earmarked RM30m of the proceeds for bank borrowings repayment while RM6.2m will be for working capital.

Valuation

- Trading at +0.5SD 3-year mean PER of 13.9x.** Based on 3-year PER band, the stock's mean earnings multiplier is 11.6x with 0.5SD and 1.0SD above its mean are 13.6x and 15.5x, respectively, while at 0.5SD and 1.0SD below its mean, targeted PERs are 9.6x and 7.7x respectively. At current price of RM2.36, MSC is trading closer to its +0.5SD to its 3-year mean at 13.9x.

Fwd PER Band



Source: Bloomberg, Kenanga Research

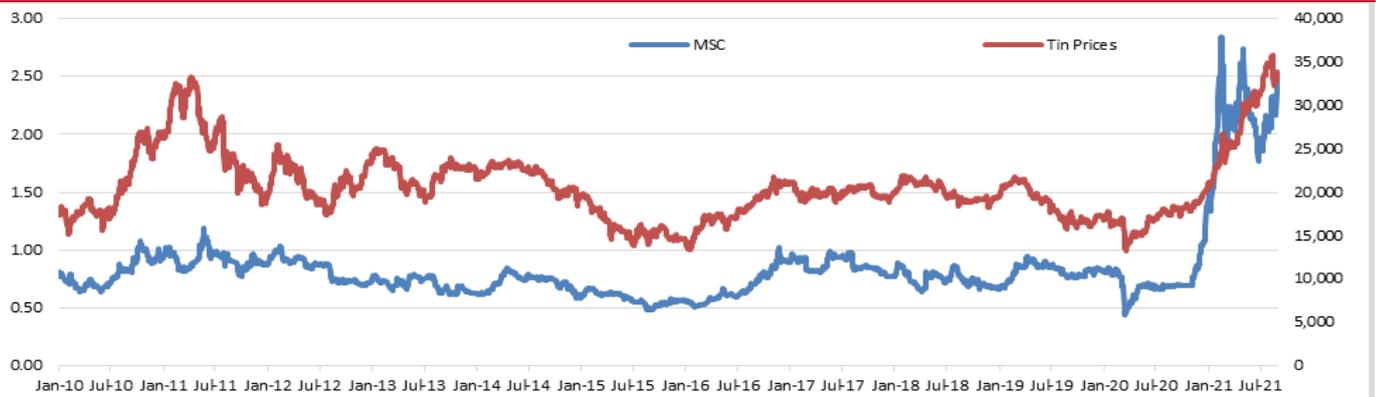
- MSC is fairly priced currently.** The top four world's largest tin smelters; Yunnan Tin of China and PT Timah of Indonesia are trading at prospective PER of 15.6x and 39.6x, respectively, while MSC and Minsur of Peru have no consensus forecasts. Based on our forecast, MSC is trading at 13.9x PER which is 10% discount to the world's largest tin smelter Yunnan Tin which is fair given its relatively smaller size. As such, we believe MSC share price has already priced in the near-term strong tin prices.

Global Peer Comparison

	Price	Mkt Cap (USD m)	Forex	Revenue Growth 2020A	Revenue Growth 2021F	Earnings Growth 2020A	Earnings Growth 2021F	PER (x) 2020A	PER (x) 2021F	PER (x) 2022F	PBV (x) 2020A	PBV (x) 2021F	ROE 2021F	Net Yld 2021F
Yunnan Tin	22.36	5778.0	CNY	4.4%	11.9%	-19%	217%	26.7	17.1	15.6	2.6	2.5	5.4%	N.A.
PT Timah	1505.00	787.9	IDR	-21.2%	-17.7%	-62%	-218%	N.A.	48.7	39.6	2.1	2.1	-6.7%	1.0%
MSC	2.36	239.0	MYR	-17.3%	N.A.	-52%	N.A.	37.6	N.A.	N.A.	2.2	N.A.	4.0%	N.A.
Minsur	2.60	1831.1	PEN	-8.8%	N.A.	-91%	N.A.	N.A.	N.A.	N.A.	0.6	N.A.	0.8%	N.A.

Source: Bloomberg

MSC Share Price vs. Tin Prices



Source: Bloomberg

Our Takes

- We believe the stock has already priced in the near-term strong tin prices which is already at an all-time-high fuelled by supply-demand dynamic. This is also in-line with other commodities' rally since the end of last year. We expect the tin price uptrend to reverse once the pandemic is under control.
- We reckon that the new smelting plant in Pulau Indah is a game changer to MSC in term of production efficiency leading to margin expansion. Its immediate competitor – Thaisarco of Thailand is still using the same aging reverberatory furnace technology as MSC's Butterworth plant. Therefore, MSC has cost advantage over Thaisarco to compete in the international arena.
- While there is value unlocking for its Butterworth land, there are uncertainties given that MSC's land development will only start three years later.
- We value the stock at RM2.32 based on +0.5SD to its 3-year mean of 13.6x PER given a reasonable earnings growth for the next two years.

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