

# Malaysia Steel Works (MSW MK)

Basic Materials - Metals

Market Cap: USD58.4m

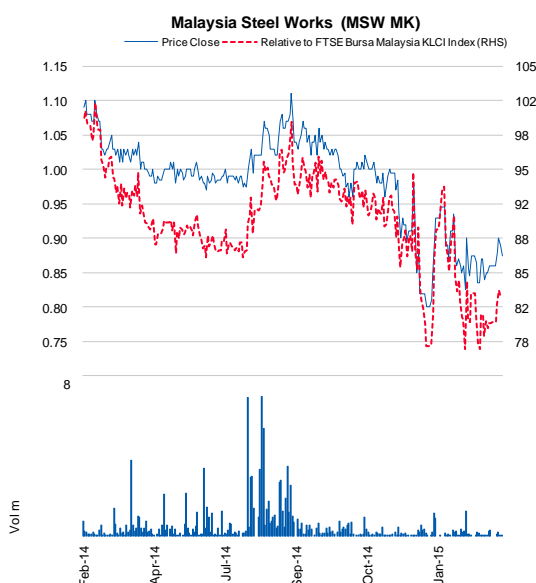
Buy (Maintained)

Target Price: MYR1.16

Price: MYR0.88

## A Standout In The Challenging Steel Market

Macro	◆◆
Risks	◆◆
Growth	◆◆◆◆
Value	◆◆◆◆



Source: Bloomberg

Avg Turnover (MYR/USD)	0.14m/0.04m
Cons. Upside (%)	23.9
Upside (%)	31.8
52-wk Price low/high (MYR)	0.80 - 1.11
Free float (%)	35
Share outstanding (m)	239
<b>Shareholders (%)</b>	
TYT Resources	30.9
Lembaga Tabung Haji	5.1

### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(5.9)	6.1	(9.8)	(19.0)	(20.5)
Relative	(9.0)	5.0	(8.4)	(16.5)	(20.1)

### Shariah compliant

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We deem FY14's MYR15.8m earnings commendable, despite being under our and street estimates. This justifies a BUY, with trimmed TP of MYR1.16 (vs MYR1.26), 32% upside. Masteel is one of the best survivors in this challenging steel market. Its smaller production volume facilitates easier manoeuvrability and its new rolling mill, adjacent to its meltshop, provides a solid medium-term earnings growth prospect.

- ◆ **FY14 numbers missed.** Malaysia Steel Works' (Masteel) MYR4.5m 4Q14 net profit (+174% QoQ) lifted FY14 earnings to MYR15.8m. While full-year results were short of our and street estimates, we deem it commendable given an unrealised MYR8.2m 4Q forex loss that partly cut bottomline. Despite a drop in selling prices and continued competition from imported steel, the higher sales tonnage helped to boost overall revenue by 5.6% YoY.
- ◆ **Better survivor in a difficult time.** 4Q14's results again demonstrated Masteel's ability to stay in the black despite poor market conditions. Its new rolling mill – adjacent to its meltshop in Klang with 200,000 tonnes/annum (tpa) rated capacity – is set for commissioning in 2H15. This should boost its profitability on better cost efficiencies from continuous casting operations and lift its profits, given that Masteel has been selling its excess upstream volume as billets at lower margins, or outsourced the rolling process on a profit-sharing basis.
- ◆ **Maintain BUY.** Meanwhile, we think prices of local steel bars and wire rods may soon drop below MYR1,800/tonne despite having been fairly firm in the falling global steel price environment. However, as scrap prices have fallen 26% to USD250/tonne in just >4 months, this is set to net benefit Masteel's operating costs and, hence, its profit margins. There may be a 2-3 months' time lag, though. The reduction of electricity tariffs by 2.25 sen/kilowatt-hour (kWh) for four months is also timely in lowering Masteel's production cost. That said, we stay cautious on the steel market and expect continued competition from imported steel. Hence, we trim our FY15F earnings by 19.9% but raise FY16F net profit by 9.9% and introduce our FY17 numbers. TP is lowered to MYR1.16 (from MYR1.26) despite raising our valuation to 0.56x FY15F P/BV – derived from +2SD (from +1SD) of its 5-year historical trading range – as we now are using a fully-diluted share base. The TP implies 11.5x/8x FY15F/FY16F P/E's respectively as fair and, thus, we reiterate BUY.

Forecasts and Valuations	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total turnover (MYRm)	1,375	1,452	1,260	1,298	1,305
Reported net profit (MYRm)	28.8	15.8	32.1	46.2	50.2
Recurring net profit (MYRm)	28.8	15.8	32.1	46.2	50.2
Recurring net profit growth (%)	18.2	(45.1)	103.4	43.9	8.6
Recurring EPS (MYR)	0.13	0.07	0.12	0.14	0.16
DPS (MYR)	0.02	0.00	0.01	0.01	0.02
Recurring P/E (x)	6.7	12.7	7.6	6.1	5.6
P/B (x)	0.35	0.36	0.42	0.40	0.37
P/CF (x)	4.17	7.13	3.48	3.34	3.05
Dividend Yield (%)	1.7	0.0	1.1	1.6	1.8
EV/EBITDA (x)	6.23	7.12	4.52	3.85	3.13
Return on average equity (%)	5.3	2.8	5.2	6.8	6.9
Net debt to equity (%)	41.2	47.0	28.5	18.6	8.4
Our vs consensus EPS (adjusted) (%)			(15.8)	(3.8)	0.0

Source: Company data, RHB

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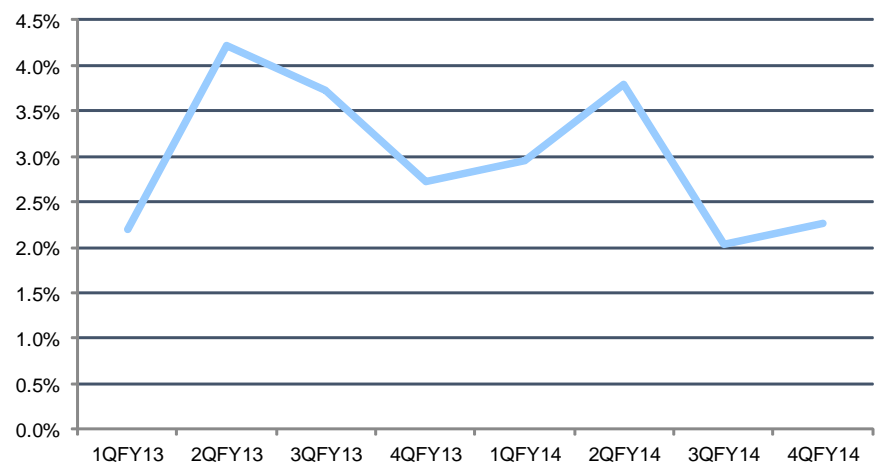
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Figure 1: Masteel's results table

FYE Dec (MYRm)	4Q13	3Q14	4Q14	QoQ (%)	YoY (%)	FY13	FY14	YoY (%)	Comments
<b>Revenue</b>	<b>352.0</b>	<b>362.1</b>	<b>392.2</b>	<b>8.3</b>	<b>11.4</b>	<b>1,375.4</b>	<b>1,451.9</b>	<b>5.6</b>	Higher sales tonnage more than compensated for a slight drop in selling prices. Hence a higher revenue YoY
<b>EBITDA</b>	<b>15.5</b>	<b>12.5</b>	<b>14.5</b>	<b>15.9</b>	<b>(6.3)</b>	<b>66.0</b>	<b>62.3</b>	<b>(5.6)</b>	Slight reduced in EBITDA YoY despite higher sales tonnage. Partly attributed to unrealised forex loss
<i>EBITDA margin (%)</i>	<i>4.4</i>	<i>3.5</i>	<i>3.7</i>			<i>4.8</i>	<i>4.3</i>		
Depreciation	(5.9)	(5.1)	(5.6)	9.6	(4.2)	(21.6)	(22.4)	3.5	
<b>EBIT</b>	<b>9.6</b>	<b>7.4</b>	<b>8.9</b>	<b>20.3</b>	<b>(7.5)</b>	<b>44.3</b>	<b>39.9</b>	<b>(10.0)</b>	
<i>EBIT margin (%)</i>	<i>2.7</i>	<i>2.0</i>	<i>2.3</i>			<i>3.2</i>	<i>2.7</i>		
Interest expense	(4.8)	(3.8)	(5.0)	32.2	5.1	(17.2)	(16.4)	(4.4)	
Interest income	0.1	0.0	2.5	nm	>500	0.2	2.5	>500	
Associates	(0.0)	(0.2)	(0.2)	(10.2)	542.3	(0.1)	(0.4)	580.4	
El/others	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
<b>Pretax profit</b>	<b>5.8</b>	<b>3.5</b>	<b>6.2</b>	<b>78.5</b>	<b>6.3</b>	<b>30.7</b>	<b>28.1</b>	<b>(8.5)</b>	
<i>Pretax margin (%)</i>	<i>1.7</i>	<i>1.0</i>	<i>1.6</i>			<i>2.2</i>	<i>1.9</i>		
Tax	(0.4)	(9.6)	(1.7)	(82.5)	296.9	(1.9)	(12.3)	533.6	Higher corporate tax rate as a result of a deferred tax liability
<i>Effective tax rate (%)</i>	<i>(7.2)</i>	<i>(276.0)</i>	<i>(27.0)</i>			<i>(6.3)</i>	<i>(43.8)</i>		
Minority interest	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
<b>Net profit</b>	<b>5.4</b>	<b>(6.1)</b>	<b>4.5</b>	<b>174.0</b>	<b>(16.4)</b>	<b>28.8</b>	<b>15.8</b>	<b>(45.1)</b>	FY14 net profit was below our and street estimates
<b>Core profit</b>	<b>5.4</b>	<b>(6.1)</b>	<b>4.5</b>	<b>174.0</b>	<b>(16.4)</b>	<b>28.8</b>	<b>15.8</b>	<b>(45.1)</b>	
<i>Net margin (%)</i>	<i>1.5</i>	<i>(1.7)</i>	<i>1.2</i>			<i>2.1</i>	<i>1.1</i>		

Source: Company data, RHB

Figure 2: Masteel's EBIT margins evolution



Source: Company data, RHB

**Figure 3: Masteel's past eight quarters results**

FYE Dec (MYRm)	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	2QFY14	3QFY14	4QFY14
<b>Revenue</b>	<b>330.0</b>	<b>342.3</b>	<b>351.2</b>	<b>352.0</b>	<b>337.7</b>	<b>360.0</b>	<b>362.1</b>	<b>392.2</b>
<b>EBITDA</b>	<b>12.4</b>	<b>19.7</b>	<b>18.5</b>	<b>15.5</b>	<b>15.6</b>	<b>19.7</b>	<b>12.5</b>	<b>14.5</b>
<i>EBITDA Margin (%)</i>	3.8	5.7	5.3	4.4	4.6	5.5	3.5	3.7
Depreciation	(5.2)	(5.2)	(5.4)	(5.9)	(5.6)	(6.0)	(5.1)	(5.6)
<b>EBIT</b>	<b>7.2</b>	<b>14.4</b>	<b>13.1</b>	<b>9.6</b>	<b>10.0</b>	<b>13.7</b>	<b>7.4</b>	<b>8.9</b>
<i>EBIT Margin (%)</i>	2.2	4.2	3.7	2.7	3.0	3.8	2.0	2.3
Interest expense	(3.8)	(3.6)	(5.0)	(4.8)	(4.0)	(3.6)	(3.8)	(5.0)
Interest income	0.0	0.0	0.0	0.1	0.0	(0.0)	0.0	2.5
Associates	(0.0)	(0.0)	0.0	(0.0)	(0.0)	(0.0)	(0.2)	(0.2)
El/Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Pretax profit</b>	<b>3.8</b>	<b>10.9</b>	<b>10.3</b>	<b>5.8</b>	<b>7.7</b>	<b>10.8</b>	<b>3.5</b>	<b>6.2</b>
<i>Pretax Margin (%)</i>	1.1	3.2	2.9	1.7	2.3	3.0	1.0	1.6
Tax	(0.2)	(0.7)	(0.6)	(0.4)	(0.4)	(0.7)	(9.6)	(1.7)
<i>Effective tax rate (%)</i>	(6.0)	(6.7)	(5.5)	(7.2)	(5.0)	(6.4)	(276.0)	(27.0)
Minority Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>3.6</b>	<b>10.1</b>	<b>9.7</b>	<b>5.4</b>	<b>7.3</b>	<b>10.1</b>	<b>(6.1)</b>	<b>4.5</b>
<b>Core Profit</b>	<b>3.6</b>	<b>10.1</b>	<b>9.7</b>	<b>5.4</b>	<b>7.3</b>	<b>10.1</b>	<b>(6.1)</b>	<b>4.5</b>
<i>Net Margin (%)</i>	1.1	3.0	2.8	1.5	2.2	2.8	(1.7)	1.2

Source: Company data, RHB

## Financial Exhibits

<b>Profit &amp; Loss (MYRm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Total turnover	1,375	1,452	1,260	1,298	1,305
Cost of sales	(1,280)	(1,350)	(1,143)	(1,163)	(1,168)
<b>Gross profit</b>	<b>95</b>	<b>102</b>	<b>117</b>	<b>134</b>	<b>137</b>
Gen & admin expenses	(30)	(30)	(38)	(38)	(38)
Selling expenses	(20)	(20)	(19)	(19)	(19)
Other operating costs	(0)	(10)	-	-	-
<b>Operating profit</b>	<b>45</b>	<b>42</b>	<b>61</b>	<b>77</b>	<b>80</b>
Operating EBITDA	67	65	89	106	109
Depreciation of fixed assets	(22)	(22)	(29)	(29)	(29)
<b>Operating EBIT</b>	<b>45</b>	<b>42</b>	<b>61</b>	<b>77</b>	<b>80</b>
Net income from investments	0	(0)	-	-	-
Other recurring income	2	2	1	1	1
Interest income	0	0	-	-	-
Interest expense	(17)	(16)	(19)	(17)	(14)
<b>Pre-tax profit</b>	<b>31</b>	<b>28</b>	<b>43</b>	<b>62</b>	<b>67</b>
Taxation	(2)	(12)	(11)	(15)	(17)
<b>Profit after tax &amp; minorities</b>	<b>29</b>	<b>16</b>	<b>32</b>	<b>46</b>	<b>50</b>
<b>Reported net profit</b>	<b>29</b>	<b>16</b>	<b>32</b>	<b>46</b>	<b>50</b>
<b>Recurring net profit</b>	<b>29</b>	<b>16</b>	<b>32</b>	<b>46</b>	<b>50</b>

Source: Company data, RHB

<b>Cash flow (MYRm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
<b>Operating profit</b>	<b>45</b>	<b>42</b>	<b>61</b>	<b>77</b>	<b>80</b>
<b>Depreciation &amp; amortisation</b>	<b>22</b>	<b>22</b>	<b>29</b>	<b>29</b>	<b>29</b>
<b>Change in working capital</b>	<b>(6)</b>	<b>(28)</b>	<b>(0)</b>	<b>(8)</b>	<b>(2)</b>
Other operating cash flow	(31)	(22)	(18)	(15)	(13)
<b>Operating cash flow</b>	<b>30</b>	<b>14</b>	<b>71</b>	<b>83</b>	<b>95</b>
Interest paid	17	16	19	17	14
Tax paid	(1)	(2)	(20)	(15)	(17)
<b>Cash flow from operations</b>	<b>46</b>	<b>28</b>	<b>70</b>	<b>84</b>	<b>92</b>
Capex	(44)	(77)	(21)	(5)	(5)
Other new investments	(1)	(1)	-	-	-
Other investing cash flow	0	0	-	-	-
<b>Cash flow from investing activities</b>	<b>(45)</b>	<b>(77)</b>	<b>(21)</b>	<b>(5)</b>	<b>(5)</b>
Dividends paid	(2)	(2)	(3)	(5)	(5)
Proceeds from issue of shares	3	10	42	-	-
Increase in debt	10	20	(40)	(40)	(40)
Other financing cash flow	(0)	(0)	(19)	(17)	(14)
<b>Cash flow from financing activities</b>	<b>10</b>	<b>27</b>	<b>(21)</b>	<b>(61)</b>	<b>(59)</b>
Cash at beginning of period	48	60	42	85	102
<b>Total cash generated</b>	<b>12</b>	<b>(22)</b>	<b>28</b>	<b>17</b>	<b>28</b>
Forex effects	2	-	-	-	-
<b>Implied cash at end of period</b>	<b>62</b>	<b>39</b>	<b>71</b>	<b>102</b>	<b>130</b>

Source: Company data, RHB

## Financial Exhibits

Balance Sheet (MYRm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total cash and equivalents	60	42	85	102	130
Inventories	221	165	206	210	210
Accounts receivable	240	332	213	219	220
Other current assets	3	2	2	2	2
<b>Total current assets</b>	<b>524</b>	<b>541</b>	<b>505</b>	<b>533</b>	<b>563</b>
Total investments	9	9	9	9	9
Tangible fixed assets	482	537	529	505	481
Total non-current assets	491	546	538	514	490
<b>Total assets</b>	<b>1,015</b>	<b>1,087</b>	<b>1,043</b>	<b>1,047</b>	<b>1,052</b>
Short-term debt	264	279	239	199	159
Accounts payable	171	187	108	110	111
<b>Total current liabilities</b>	<b>435</b>	<b>466</b>	<b>347</b>	<b>309</b>	<b>269</b>
Total long-term debt	25	35	35	35	35
Other liabilities	-	10	-	-	-
<b>Total non-current liabilities</b>	<b>25</b>	<b>44</b>	<b>35</b>	<b>35</b>	<b>35</b>
<b>Total liabilities</b>	<b>460</b>	<b>510</b>	<b>381</b>	<b>343</b>	<b>304</b>
Share capital	111	118	160	160	160
Retained earnings reserve	372	388	416	458	503
Other reserves	72	71	85	85	85
<b>Shareholders' equity</b>	<b>555</b>	<b>577</b>	<b>662</b>	<b>704</b>	<b>749</b>
<b>Total equity</b>	<b>555</b>	<b>577</b>	<b>662</b>	<b>704</b>	<b>749</b>
<b>Total liabilities &amp; equity</b>	<b>1,015</b>	<b>1,087</b>	<b>1,043</b>	<b>1,047</b>	<b>1,052</b>

Source: Company data, RHB

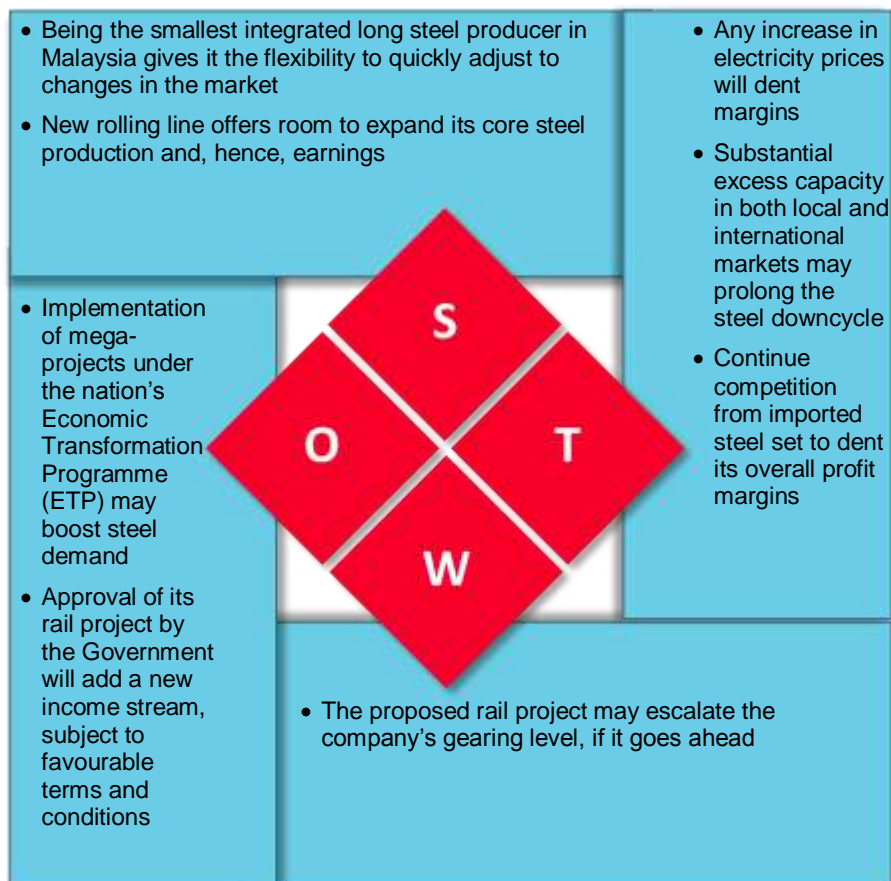
Key Ratios (MYR)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Revenue growth (%)	4.8	5.6	(13.2)	3.0	0.6
Operating profit growth (%)	23.8	(6.5)	44.3	26.4	3.4
Net profit growth (%)	18.2	(45.1)	103.4	43.9	8.6
EPS growth (%)	15.2	(47.4)	67.5	25.0	8.6
Bv per share growth (%)	3.6	(2.5)	(15.3)	6.3	6.4
Operating margin (%)	3.3	2.9	4.8	5.9	6.1
Net profit margin (%)	2.1	1.1	2.6	3.6	3.8
Return on average assets (%)	3.0	1.5	3.0	4.4	4.8
Return on average equity (%)	5.3	2.8	5.2	6.8	6.9
Net debt to equity (%)	41.2	47.0	28.5	18.6	8.4
DPS	0.02	0.00	0.01	0.01	0.02
Recurrent cash flow per share	0.21	0.12	0.25	0.26	0.29

Source: Company data, RHB

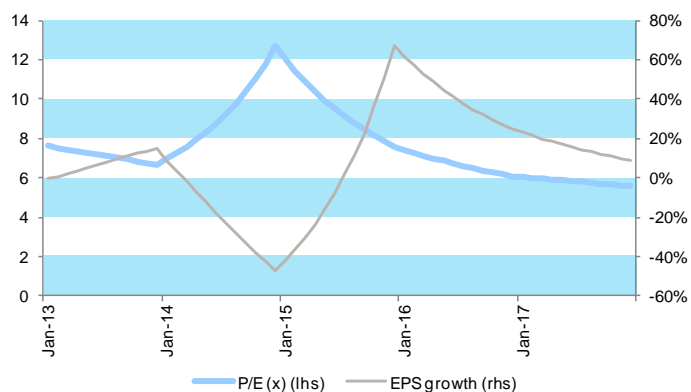
Key assumptions	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Capacity - electric arc furnace	650,000	700,000	700,000	700,000	700,000
Capacity - rolling	400,000	450,000	550,000	650,000	650,000
Utilisation - electric arc furnace	90%	91%	92%	92%	93%
Utilisation - rolling	98%	98%	96%	96%	97%
ASP - billets (MYR/MT)	1,750	1,725	1,400	1,428	1,436
ASP - bars/wire rods (MYR/MT)	2,100	2,000	1,750	1,750	1,750

Source: RHB

## SWOT Analysis

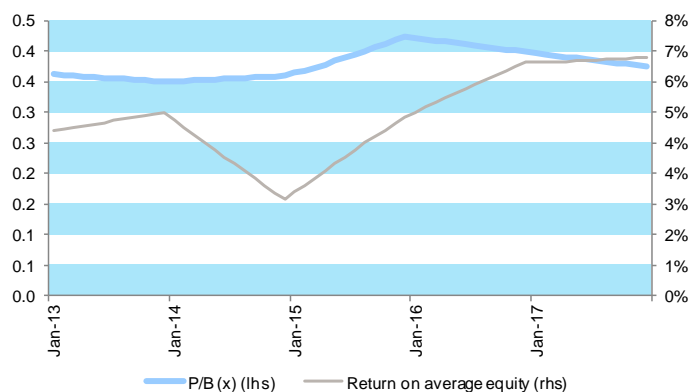


**P/E (x) vs EPS growth**



Source: Company data, RHB

**P/BV (x) vs ROAE**



Source: Company data, RHB

## Company Profile

Malaysia Steel Works (KL) (Masteel) is an integrated steel manufacturer with a focus on long steel products.

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2014-11-28	Buy	1.26	0.94
2014-08-28	Buy	1.31	1.07
2014-05-29	Neutral	1.05	1.00
2014-02-28	Neutral	1.10	1.10
2013-12-03	Neutral	1.07	1.07
2013-12-02	Trading Buy	1.30	1.05
2013-09-02	Trading Buy	1.08	0.91
2013-08-26	Neutral	1.08	0.94
2013-06-03	Trading Buy	1.08	0.95
2013-03-01	Neutral	0.91	0.80

Source: RHB, Bloomberg

## RHB Guide to Investment Ratings

**Buy:** Share price may exceed 10% over the next 12 months

**Trading Buy:** Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months

**Take Profit:** Target price has been attained. Look to accumulate at lower levels

**Sell:** Share price may fall by more than 10% over the next 12 months

**Not Rated:** Stock is not within regular research coverage

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