

COMPANY UPDATE

OM Holdings (OMH MK)

Stronger Earnings Ahead Leveraging On The Rally In Ferroalloy Prices

OMH is set to achieve more robust earnings ahead on the back of a production recovery and strong ferroalloy prices. We raised our earnings forecast for 2021-23 to reflect higher ferroalloy prices. Being the world's lowest-quartiles-cost manganese smelter, OMH is expected to post a 3-year net profit CAGR of +150% from 2020, supported by favourable prices and strong global demand amid the structural supply shortage. Maintain BUY with a higher target price of RM3.46.

WHAT'S NEW

- Production recovery ahead.** In the post-results briefing yesterday, OM Holdings (OMH) mentioned that it has gradually ramped up production post-lockdown with 12 out of 16 furnaces (6 FeSi and 6 Mn alloy) operating currently so we can expect higher production output ahead. OMH mentioned that the 50% workforce requirement under the current SOP will not affect the production level as the workers work in shifts. A more meaningful growth will be seen in 2022 when the remaining four furnaces are fully restarted once manpower constraints have been alleviated with the border reopening. Note that 1H21 production volumes of ferrosilicon (FeSi) and manganese (Mn) alloy fell to 61,472mt (-36.3% yoy) and 94,827mt (-13.3% yoy), forming about 53.5% and 55.8% of our full-year forecasts respectively. The decline is due to the 5-week temporary suspension in June.
- Strong ferroalloy prices...** FeSi and Mn alloy prices jumped higher to US\$1,920/mt (+32.0% qoq, +87.3% yoy) and US\$1,545/mt (+20.7% qoq, +49.5% yoy) respectively towards the end of 2Q21. According to OMH, FeSi production constraint in China further intensified in 3Q21 as power cuts across the country, due to power rationing amid high power demand, shortage of renewable power, and lower coal availability, has resulted in production uncertainty. This factor coupled with China's increase in export tax of 25% for Fesi to discourage power intensive industrials, have continued to provide strength to the current prices. Similarly, Mn alloy's prices also continued to rally in 1H21 as certain producing countries like China and India continued to face temporary disruptions.
- ...to boost earnings further.** We believe there is more room for immediate upside in the ferroalloy price trajectory, and it could sustain at least until the later part of 2H21, benefitting from the global return in demand, coupled with slow supply response due to the ongoing production disruption and logistics issues amid the global decarbonisation trend. Note that in 3Q21 so far, FeSi continued to rise further to over RM2,000/mt. However, in the long run, we believe prices will gradually ease but still remain firm, albeit not at the current high, as the global supply cannot catch up with the increasing demand.

KEY FINANCIALS

Year to 31 Dec (RMm)	2019	2020	2021F	2022F	2023F
Net Turnover	2,976.7	2,275.4	2,710.1	3,398.0	3,573.2
EBITDA	317.0	164.1	270.3	359.5	378.4
Operating Profit	176.2	22.2	158.3	227.8	235.4
Net Profit (Reported/Actual)	164.3	15.5	138.1	202.6	218.7
Net Profit (Adjusted)	185.3	14.0	138.1	202.6	218.7
EPS (sen)	22.3	1.9	18.7	27.5	29.7
PE (x)	10.8	127.4	12.9	8.8	8.1
P/B (x)	1.2	1.3	1.2	1.1	1.0
EV/EBITDA (x)	10.1	18.3	10.7	7.8	6.7
Dividend Yield (%)	1.2	-	1.0	1.5	1.6
Net Margin (%)	6.2	0.6	5.1	6.0	6.1
Net Debt/(Cash) to Equity (%)	55.7	47.8	43.2	38.9	28.2
Interest Cover (x)	1.9	0.3	2.1	3.4	4.0
ROE (%)	15.0	1.2	10.7	13.8	13.1

Source: OMH, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	RM2.59
Target Price	RM3.46
Upside	+33.6%
(Previous TP	RM3.27)

COMPANY DESCRIPTION

ASX-listed OM Holdings is an integrated manganese player engaged in the mining, smelting, trading and marketing of manganese ores, manganese alloys and ferrosilicon. Its smelting plants in Sarawak operate using low-cost sustainable energy – hydropower.

STOCK DATA

GICS sector	Materials
Bloomberg ticker:	OMH MK
Shares issued (m):	738.6
Market cap (RMm):	2,060.7
Market cap (US\$m):	490.6
3-mth avg daily t'over (US\$m):	n.a.

Price Performance (%)

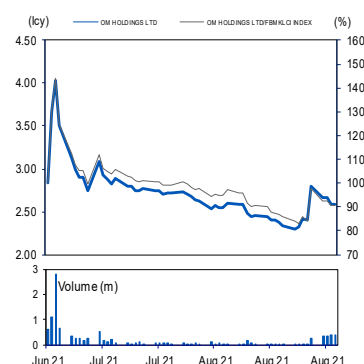
52-week high/low	RM4.03/RM2.30			
1mth	3mth	6mth	1yr	YTD
6.1	(10.1)	9.6	150.0	45.5

Major Shareholders

	%
Huang Gang	14.0
Amplewood Resourced Ltd	13.6
Low Ngee Tong	9.2

FY21 NAV/Share (RM)	2.0
FY21 Net Debt/Share (RM)	1.3

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- Strategically mitigating the impact of price volatility.** OMH monitors the market on a weekly basis, efficiently pricing its products to maximise profitability. Generally, about half of OMH's contracts with its customers use fixed prices (lock spot prices on the agreement date) while the remaining half use a formulated (floating) price based on the spot prices in the coming months when the orders are delivered, which allow OMH to benefit from any potential uplift in the future price. This helps to hedge the volatility risk of ferroalloy prices. OMH indicated sales have been fully booked until December.
- Sales volume increased due to stronger demand.** The global demand is stronger in 1H21 moving in tandem with steel's demand growth amid the economic recovery. Mn alloy's volumes traded in jumped 30.1% to 141,693mt, with a total revenue contribution of around RM592.1m. Mn ore volumes traded also surged by 77.9% to 842,327mt, contributing to about RM467m of OMH's revenue. The yoy increase was mainly due to higher demand and the temporary mining suspension last year caused by the pandemic. On the other hand, FeSi volumes traded fell by 27.6% yoy to 58,324mt contributing to about RM323m of OMH's revenue. However, this decrease was partially mitigated by the higher average transacted price of US\$1,302/mt (+11.2% yoy).
- Leveraging on growing demand for steel.** According to International Manganese Institute (IMnI), world crude steel production in 2Q21 was 353.5m mt, up 21.3% yoy, indicating a strong rebound from the low base numbers in 2020. In August, hot rolled coil prices rose 54% yoy (to RM3,849/mt) while bar prices rose 46% yoy (to RM3,589/mt). Even with China's ongoing efforts to curb its commodity prices, we believe steel supply-demand dynamics should remain favourable to support lofty prices in the long term, albeit not at the current high. Based on China's official index compiler CFLP Steel Logistics Professional Committee, China's steel demand may pick up again in August, while steel mills may cut down on their output at the same time, which will further support steel prices.
- Mining (Australia).** Mn ore prices slightly declined to US\$5.02/dmtu (-1% yoy) in 1H21. Although Mn ore prices followed the same uptrend as FeSi and Mn alloys in 2Q20, prices started to stabilise from 3Q20 onwards as South African mines resumed operations faster than expected post-lockdown while Australian mines were relatively unaffected. 1H21 production volume of Mn ores increased to 414,549mt (+7.9% yoy), forming about 42% of our full-year forecast. For 2H21, we believe OMH will boost production as its last mile strategy since Bootu's mining operations will end in 4Q21. OMH will obtain its Mn ore supply from Element 25 for 365,000mt/year and another 250,000mt/year from its Ultra Fines Plant (UFP) from 2022 onwards.
- New lawsuit in Australia.** OMH's mining entity, OMM, has been served a summon by the Work Health Authority for the Northern Territory in Australia. This charge relates to the alleged health and safety failures in relation to an accident at Bootu Creek mine in 2019 that resulted in the death of its employees. According to OMH, it is still premature to provide any fair estimate on the likely liability of OMM at this stage. This case will be heard in court on 12 Oct, of which further details will be disclosed then.

EARNINGS REVISION/RISK

- Raise 2021-23 net profit forecasts.** We raise our 2021-23 earnings forecasts by 17.7%, 21.1% and 15.4% respectively as we increase our ASP assumptions of FeSi and Mn alloy to US\$1,600/US\$1,400/US\$1,300 and US\$1,450/US\$1,250/US\$1,200 per mt for 2021-23 accordingly. If prices continue to rise, based on our sensitivity analysis, every US\$100/mt rise in our FeSi and Mn alloy price assumptions will boost earnings by about 25% per year.

VALUATION/RECOMMENDATION

- Maintain BUY with a higher target price of RM3.46.** Our SOTP-based target price implies 13x 2022F PE, close to its 5-year PE mean of 15x. Strong alloy prices and its low-cost hydropower will provide OMH with a profit CAGR of 150.2% for 2020-23. We have not incorporated its future capacity expansion into our valuation. The completion of those plans will prompt a valuation re-rating.

1H21 PRODUCTION

	2021	1Q21	qoq % chg	yoy % chg
Production ('000 mt)				
Mn Ore				
Australia	203	210	(3.3)	1.1
S. Africa	814	795	2.4	54.4
Alloy				
Malaysia - FeSi	23	38	(40.0)	(47.8)
Malaysia - Mn	37	57	(34.0)	(34.7)
China - Mn	16	8	87.1	>100.0

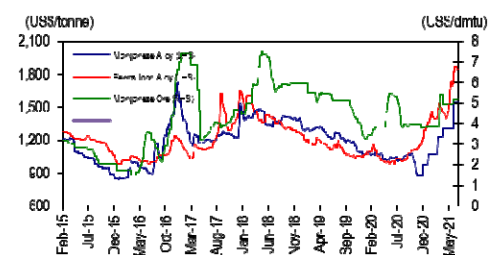
Source: OMH, UOB Kay Hian

KEY ASSUMPTIONS

	2020	2021F	2022F	2023F
Production ('000 mt)				
Mn Ore				
Australia	738	1,000	615	700
S. Africa	3,359	3,527	3,703	3,888
Alloy				
Malaysia - FeSi	167	115	180	185
Malaysia - Mn	227	170	300	350
China - Mn	10	68	85	90
ASP (US\$/mt)				
Mn ore	4.66	5.00	4.70	4.50
FeSi alloy	1,100	1,600	1,400	1,300
Mn alloy	1,000	1,450	1,250	1,200

Source: OMH, UOB Kay Hian

ALLOY AND ORE PRICES



Source: Bloomberg

SENSITIVITY ANALYSIS

Manganese (Mn) Ore	Every US\$1/dmtu reduction from our Mn ore assumption of US\$4.70/dmtu in 2022 would increase OMH's earnings by about 10%.
Ferrosilicon (FeSi) and Mn Alloy	Every US\$100/tonne increase to our current spot FeSi and Mn alloy price assumption of US\$1,400/mt and US\$1,250/mt in 2022 would increase OMH's earnings by 25% annually.

Source: UOB Kay Hian

PROFIT & LOSS

Year to 31 Dec (RMm)	2020	2021F	2022F	2023F
Net turnover	2,275	2,710	3,398	3,573
EBITDA	164	270	359	378
Deprec. & amort.	(142)	(112)	(132)	(143)
EBIT	22	158	228	235
Associate contributions	48	87	89	92
Net interest income/(expense)	(84)	(75)	(67)	(58)
Pre-tax profit	(14)	170	250	270
Tax	5	(26)	(38)	(40)
Minorities	24	(7)	(10)	(10)
Net profit	16	138	202	218
Net profit (adj.)	14	138	202	218

CASH FLOW

Year to 31 Dec (RMm)	2020	2021F	2022F	2023F
Operating	222	188.3	235.8	344.5
Pre-tax profit	(14)	170.4	249.9	269.5
Tax	5	(26)	(38)	(40)
Deprec. & amort.	142	112	132	143
Working capital changes	85	(68)	(108)	(27)
Other operating cashflows	0	-	-	-
Investing	(31)	(30)	(117)	(88)
Capex (growth)	(4)	(30)	(117)	(88)
Investments	0	-	-	-
Proceeds from Sale of Assets	(45)	-	-	-
Others	18	-	-	-
Financing	(192)	(105)	(171)	(173)
Dividend payments	(21)	(18)	(26)	(28)
Issue of shares	0	-	-	-
Proceeds from borrowings	38	-	-	-
Loan repayment	(96)	(87)	(145)	(145)
Others/interest paid	(112)	-	-	-
Net cash inflow (outflow)	0	53	(53)	83
Beginning cash & cash equivalent	142	141	194	141
Changes due to forex impact	0	-	-	-
Ending cash & cash equivalent	133	194	141	224

BALANCE SHEET

Year to 31 Dec (RMm)	2020	2021F	2022F	2023F
Fixed assets	1,777	1,913	2,116	2,279
Other LT assets	502	277	34	(209)
Cash/ST investment	183	194	141	224
Other current assets	826	946	1,169	1,240
Total assets	3,287	3,364	3,516	3,581
ST debt	368	368	368	368
Other current liabilities	499	540	664	704
LT debt	836	749	604	459
Other LT liabilities	226	211	195	179
Shareholders' equity	1,159	1,285	1,471	1,672
Minority interest	199	192	183	173
Total liabilities & equity	3,287	3,364	3,516	3,581

KEY METRICS

Year to 31 Dec (%)	2020	2021F	2022F	2023F
Profitability				
EBITDA margin	7.2	10.0	10.6	10.6
Pre-tax margin	(0.6)	6.3	7.4	7.5
Net margin	0.6	5.1	6.0	6.1
ROA	0.4	4.1	5.8	6.1
ROE	1.2	10.7	13.8	13.1
Growth				
Turnover	(23.6)	19.1	25.4	5.2
EBITDA	(48.2)	64.7	33.0	5.3
Pre-tax profit	(107.9)	(1,362.0)	46.7	7.8
Net profit	(92.5)	889.1	46.7	8.0
EPS	(91.5)	889.1	46.7	8.0
Leverage				
Debt to total capital	(0.4)	(0.3)	(0.2)	(0.2)
Debt to equity	(1.0)	(0.8)	(0.6)	(0.4)
Net debt/(cash) to equity	0.9	0.7	0.5	0.3
Interest cover (x)	0.3	2.1	3.4	4.0

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