OM Holdings Limited (OMH MK)

Pioneering Affordable and Clean Ferroalloy Smelter

- **OMH Holdings Limited (OMH) is a vertically integrated company that operates in the manganese and ferroalloy industries. The group is involved in the whole value chain from upstream activities such as exploration and mining of manganese ore, to downstream including smelting and trading of manganese ore and ferroalloys.**
- **OMH key growth drivers include: i) structural cost advantage over global peers given its position as a low-cost quartile ferroalloy smelter, ii) strong growth prospects banking on capacity expansion and diversified products offering, and iii) elevated ASPs on the back of a recovery in China's steel industry following China's full economic reopening. Above all, OMH is expected to benefit from rapid industry consolidation and OMH is expected to outshine due to their competitive and low-cost structure.**
- **We forecast core net profit of USD74.6mn-USD105mn for FY23-25F with 10.3-12.3% core net profit margin to be backed by elevated ferroalloy prices, higher output as well as capacity expansion.**
- **We initiate coverage on OMH with a BUY call and TP of RM2.91 derived based on 6x PER (30% discount to 1-year average peers PE of 8.7x) that is pegged to FY24F EPS of 48.5 sen. The attractive return is also supported by the recent share price pullback and the stock is ripe for a rebound.**

Competitive Advantage as Lowest Ferroalloy Smelter Player

OMH has a significant cost advantage over its global peers as the plant operates on *renewable hydro-power* through long-term hydropower supply contract with Bakun Dam at competitive rates. This contract provides them with a reliable and low-cost source of energy for Sarawak smelting operation, which enables them to produce ferroalloy products at lower cost. This a clear cost advantage given many European smelters that are facing with high electricity costs due to surging fuel prices. Note that many European smelters rely on fossil fuels for their energy needs, which expose them to price fluctuations. The rising fuel costs have made it difficult for these smelters to maintain their cost competitiveness, hence potentially impact their market share and consequently, profitability. This has triggered plants close down which drove rapid industry consolidation.

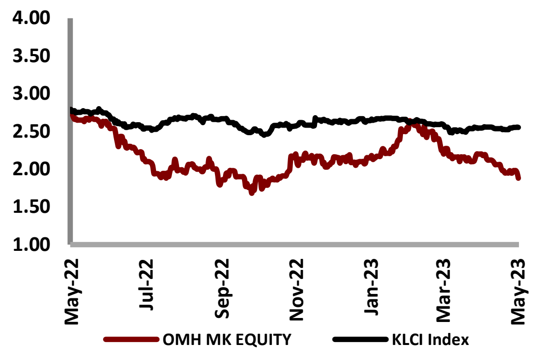
Imbalanced Market Dynamic to Elevate Prices

Escalating power costs have led to a challenging operating environment for some European smelters, forcing them to cut production capacity and/or shut down the plants. On the same note, strict environmental regulations have also forced some Chinese smelters to close production. The ongoing war between Russia-Ukraine has also been a bane which triggered supply shortage. Note that Ukraine is the world's second-largest manganese (Mn) alloys producer while Russia is the world's second biggest exporter of ferrosilicon (FeSi) in the world. These factors have caused supply-demand imbalance for FeSi and Mn alloys, emerging as drivers to prices and hence, upside risks to earnings. China's full economic reopening will also buoy demand thanks to revival in their construction activity.

BUY

Share Price	**RM1.88**	
Target Price	**RM2.91**	**+54.8%**

Price Chart (RM)



Share Performance (%)	**1m**	**3m**	**12m**
Absolute	(8.0)	(22.8)	(24.2)
vs FBM KLCI	(9.5)	(22.0)	(19.3)

Stock Data	
ESG Rating	Good
Mkt Cap (RM)	1,455.1
Adjusted Beta	1.453
Free float (%)	63.8
Issued shares (m)	738.6
52w H/L (RM)	2.73 / 1.6
3m avg daily volume (m)	51,822

Major Shareholders (%)	
Gang Huang	14.0
AMPLEWOOD RESOURCES	12.8
Low Ngee Tong	9.3

FYE 31 Dec (RM'mn)	**FY21**	**FY22**	**FY23F**	**FY24F**	**FY25F**
Turnover	3,249	3,773	3,028	3,169	3,506
EBITDA	498.2	579.6	550.4	591.8	672.2
Pretax Profit	352.2	465.2	322.5	367.7	443.3
Core Net Profit	**267.8**	**319.1**	**313.2**	**357.1**	**430.4**
Consensus NP			369.8	366.8	469.0
Core EPS (sen)	36.3	43.3	42.5	48.5	58.4
PER (x)	-73.8	5.2	4.3	4.4	3.9
DPS (sen)	0.0	0.1	0.0	12.8	14.5
D. Yield (%)	-	0.0	-	6.8	7.7
P/B (x)	0.9	0.7	0.8	0.8	0.7
Key Ratios (%)					
ROE	17.5	18.3	18.0	18.0	18.0
EBITDA margin	15.3	15.4	19.2	19.2	19.2
Pretax margin	10.8	12.3	10.7	12.6	12.6
Net margin	8.2	8.5	12.6	12.6	12.6

Source: Bloomberg, BIMB Securities

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Initiate with a BUY call with TP of RM2.91

We initiate coverage on OMH with a **BUY** recommendation and **TP of RM2.91**. We favour OMH due to i) competitive advantage as low-cost ferroalloy smelter players, a significant advantage compared to peers, ii) extended capacity growth and diversified products mix, and iii) impressive ESG standing thanks to exposure to clean energy resources.

Background

OM Holdings Limited (OMH) started off back in 1994 and has now evolved into one of the largest vertically integrated manganese ore and ferroalloy players in South East Asia. OMH and its subsidiaries have an established track record of over 25 years in exploration, operations and marketing and trading. With vertically integrated operations globally in exploration, mining, smelting, sintering and marketing and trading, the group is able to capture significant value and margins along the entire value chain. The group's three core businesses are comprised of exploration and mining of manganese ore, production of manganese alloys and ferrosilicon and marketing and trading of manganese ore and ferroalloys. Today, the group is one of the world's major manganese ore, ferrosilicon and manganese alloy producers with market presence and operation in Australia, China, Japan, Malaysia and South Africa. It has dual listing in Australian Securities Exchange (ASX) and Bursa Malaysia and this gives the group a unique exposure to the niche manganese and silicon space essential to the modern world.

Figure 1: Key products

Source: Company, BIMB Securities

Chart 1: Key products details

Manganese ore (Mn Ore)

- Raw material in smelting to produce silicon manganese (SiMn), High-carbon ferromanganese (HC FeMn) and other manganese (Mn) alloys products.

Ferrosilicon (Fesi)

- An alloy of silicon (Si) and iron (Fe)

- Produce at OM Sarawak

Manganese alloys (Mn Alloys)

- Comprise of :

i) Silicomanganese (SiMn) - an alloy of manganese (Mn), silicon (Si), and iron (Fe), and

ii) High-carbon ferromanganese (HC FeMn) - an alloy of manganese (Mn) and iron (Fe)

- Produced SiMn in OM Sarawak while HC FeMn in OM Sarawak and OM Qinzhou

Source: Company, BIMB Securities

Table 1: Key operation

Exploration & Mining	**Australia (100%)** Exploration + Tailings Plant *Noted that this mine has ceased operation since Dec'21 due to end of life mine **Tshipi Borwa - South Africa (13%*)** Manganese ore: 3.0-3.6 Mtpa **Effective interest held via J/V with Ntsimbintle (a BEE group)*
Smelting & Sintering	**Sarawak - Malaysia (100%)** Mn alloy: 333-400ktpa, Ferrosilicon: 120-126ktpa Sinter ore: ~250ktpa Silicon Metal: 21-24.5ktpa **Qinzhou - China** (100%) Mn alloy: 80-95kpta Sinter ore: 300ktpa
Marketing & Trading	**Singapore/China (100%)** Global sales and procurement Manganese ore, Ferrosilicon, Silicomanganese, Ferromanganese, Quartz, Reductants (coke, coal), Fe units

Source: Company, BIMB Securities

Operational Highlight

Commendable hydropower energy rate. OMH plants at Samalaju Smelting Complex are running using hydropower supply from the Bakun Dam and have locked-in a competitive power tariff, thanks to a 20-year PPA with the Sarawak State Energy. The group is able to secure a competitive electricity tariff rate through the PPA, with incremental tariff of c.2.5% per annum. This agreement is expected to expire in 2033 and the group is planning to negotiate the extension of the contract. Note that all smelting production are currently coming from their Sarawak plant as they have closed their Qinzhou plant in China since 3QCY21 due to rising power costs and unfavourable policy by the government. The group is still considering to sell the plant or turn it into a warehouse/logistic hub given its strategic location which is close to the Qinzhou Port.

Conversion provides flexibility and diversity. OMH has undergone substantial conversion and maintenance work in FY22 and successfully modified and converted two FeSi furnaces to produce silicon metal (MetSi). This furnace is able to produce 11-24ktpa of production output once its fully commence. We understand that the conversion and maintenance activities will take about six months to complete. The group is now running with five furnaces of FeSi and Mn alloys respectively and plans to commissioning one of MetSi furnaces. Moving forward, the group is targeting to operate eighteen furnaces in total which include six FeSi furnaces, eight Mn alloys furnaces, two MetSi furnaces, as well as another two Mn alloys furnaces (with addition of new 33 mega volt amp [MVA]), thus pushing cumulative total production to 610-640ktpa.

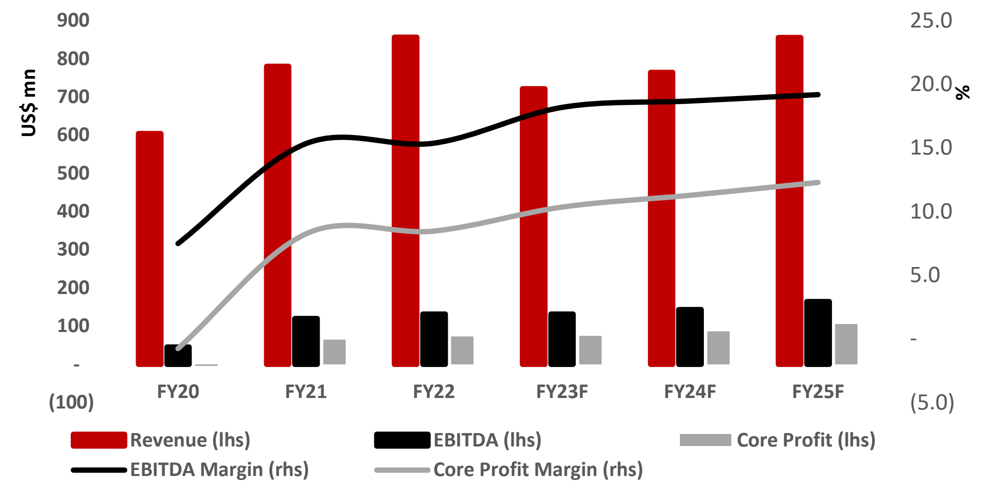
Figure 2: Development plan

Source: Company, BIMB Securities

Exploring downstream opportunities. The conversion of furnaces enables OMH diversify its products offering where this is expected to spur potential growth of the group in the long-run. Through furnaces conversion to produce high grade MetSi, this diversification helps OMH to explore different industries as it can be used for manufacturing microchips, steel as well as solar cell, tapping into downstream business industries. First MetSi furnace is currently undergoing hot commissioning and performance testing. The initial commissioning of MetSi has been delayed however as the furnace is not performing as anticipated within the framework of the EPC contract. On top of that, MetSi furnaces are expected to produce FeSi for more flexibility in terms of product mix. MetSi is offering higher margin compared to FeSi and Mn Alloys but the pricing and cost structured are comparable to Fesi. The only major difference is the electricity usage as it requires 50% more electricity to produce.

Financial Highlight

Chart 2: OMH's annual performance, FY19A - FY25F



Source: Company, BIMB Securities

Substantial FY22 production ending. Output for FeSi and Mn alloys dropped slightly or by 7.4% QoQ and 23.2% QoQ during 4QFY22 hampered by plants major maintenance work where one FeSi furnace and four Mn Alloys furnaces were temporarily shut down for this. Nevertheless, full year 2022 production of FeSi and Mn Alloys production volume escalated by 7.1% YoY and 0.1% YoY to 140,3kmt and 216.8kmt, thanks to Malaysia's full economic reopening and low base effect given the absent of COVID-19 lockdown measures. Therefore, OMH reported convincing revenue and core net profit of USD856.6mn (+9% YoY) and USD72.4mn (+12.7% yoy), thanks to higher ferroalloy prices and production, aided as well by the absence of the loss-making mining segment (Bootu Creek Mine).

Major maintenance in place. As at March 2023, eleven out of 16 furnaces were in operation (five Fesi and six Mn alloys). For the remaining five furnaces, three are undergoing scheduled maintenance work and the remaining two are undergoing reviews to solve the issues regarding the production of MetSi. All in all, four furnaces have completed their maintenance work with eight to undergo major maintenance in FY23 in order to minimise disruption. As such, 1QFY23 FeSi production volumes of FeSi have eased to 29,707mt (-13.5% qoq) while Mn alloys improved to 52,151mt (+25.7% qoq). Despite a decline in FeSi production due to suspension of operation, Mn alloys production improved as two furnaces resumed operations earlier this year after the completion of maintenance works in the previous quarter.

Propel by expanded production and price recovery. Looking forward, we expect OMH revenue to be in a range USD721mn-USD855.1mn for FY23-FY25F backed by elevated ferroalloy price, higher output as well as expanded capacity. China's full economic reopening coupled with supply constraints in Europe are expected to drive prices further. China's full economic re-openings will push demand further and hence, the average selling prices (ASPs).

Dividend policy formalized effective FY2023. The group's official dividend policy entails a distribution of 10%-30% of net profit after tax, subject to a cap of 50% free cash flow and other considerations. For FY23-25F, we assume a 30% net profit distribution as dividend which translate into 6.8-9.3% dividend yields (based on EPS in RM) at current share price.

Valuation

We initiate coverage on OMH with a **BUY call** and **TP of RM2.91** derived based on 6x PER (30% discount to 1-year average peers PE of 8.7x) that is pegged to FY24F EPS of 48.5 sen. We apply a discount to PER in view of moderating global growth, global inflationary pressure and lacklustre sentiment in equity markets amid various externals headwinds. Total return remain remains attractive and this will be powered by OMH i) competitive advantage as a low-cost ferroalloy smelter players compared to its peer, ii) extended capacity growth and diversified products mix, and iii) enviable ESG standing given their exposure to clean energy resource. Above all, OMH is expected to benefit from rapid industry consolidation and OMH is expected to outshine due to their competitive and low-cost structure.

Table 2: OMH peers' comparison

Company	Stock Recom.	Price @ 10-May-23	Target Price (RM)	Market Cap. (USD'M)	PE(x) 2022	PE(x) 2023	PE(x) 2024	PB(x)	ROE (%)	Div. Yield (%)
OM Holdings	**BUY**	**RM1.88**	**2.91**	**1,455.1**	**-**	**3.7**	**3.7**	**-**	**17.8**	**2.3**
Malaysia Peers										
Press Metal Aluminium	N/A	RM4.89	N/A	40,374.1	28.3	23.2	19.8	6.1	27.0	1.4
Malaysia Smelting Corp	N/A	RM2.08	N/A	856.8	8.7	7.8	7.3	1.2	15.1	3.4
Global Peers										
Jupiter Mines	N/A	AUD0.21	N/A	421.2	5.5	5.7	6.0	0.9	16.9	10.2
South32	N/A	AUD4.15	N/A	18,584.2	5.5	9.7	8.6	1.2	23.0	8.0
GMS	N/A	USD59.61	N/A	2,462.2	7.7	6.6	8.7	2.0	29.9	-
Elkem ASA	N/A	NOK29.28	N/A	18,722.8	2.4	6.4	6.7	0.6	29.9	20.5
Average				**11,839.5**	**9.7**	**9.0**	**8.7**	**2.0**	**22.8**	**7.6**

Source: Bloomberg, BIMB Securities

Key Risks

- **Business operations depend on adequate and timely supply of electricity and water.** OMH's smelting operation consumes substantial amount of electricity for the production of ferrosilicon and manganese alloys. The reliability and sustainability of electricity supply is critical to ensure production continuity for smelting operations. Any unexpected disruption of electricity supply could hamper the smelting process and affect production volumes.

- **Mining and production activities may be affected by national and local environmental laws and regulations.** Operations in countries (Bootu Creek Mine in Australia, Qinzhou Plant in China, and Sarawak Plant in Malaysia) are bound by national and local environmental laws and regulations. These laws and rules create specific guidelines for maintaining good health and protecting the environment. They also outline punishments and responsibilities for breaking these guidelines, and sometimes require companies to fix any damage they have caused in the past.

- **Unfavourable currency movement.** The volatility in USD or downside risks to the currency could hurt OMH given the significance of USD in their products pricing and hence, revenue and consequently, profitability.

Key Catalyst

- **Optimize performance by enhancing operational efficiency.** Enhancing operational efficiencies while developing new products solution such as creating synergies between mining and smelting operation, continue research and development as well as localizing raw material sources in the long run.
- **Strategically diversify products portfolio and increase production capacities.** Production of Metsi will allow the group to diversify to downstream user, reaching wider group of buyers. On top of that, OMH are upbeat to embark on the production of other specialty grades of ferroalloys such as high purity ferroalloys.

Table 3: SWOT analysis

Strength	Weakness
• Well-known position as one the largest leading suppliers of manganese ores and ferroalloys in South East Asia • Low-cost quartile smelter - through 20-year power purchase agreement with Sarawak Energy	• Fluctuation of ferrosilicon and silicon manganese prices • Labour shortage
Opportunities	**Threat**
• Expanding production and increasing plant utilization in order to meet strong demand. • Furnaces conversion into metallic silicon that drive margins	• Fluctuation in foreign exchange rates, particularly between USD, AUD and RM

Source: Company, BIMB Securities

ESG Exposure and Score

Our ESG score rating stipulates a score on how well a company's ESG risks are being executed. We opine the group's score is "Good" with 3.9 out of 5.0 points.

Table 4: BIMB ESG score rating for OMH

	Weighted (%)	ESG Rating
Environmental	33.33	1.33
Social	33.33	1.22
Governance	33.33	1.33
SUM	**100.0**	**3.9**

Source: BIMB Securities

Table 5: BIMB ESG Rating Classification

Rating	
4.5 - 5.0	Excellent
4.0 - 4.4	Best
3.0 - 3.9	Good
2.0 - 2.9	Fair
1.0 - 1.9	Poor

Source: BIMB Securities

Income Statement

FYE 31 Dec (USDmn)	FY21	FY22	FY23F	FY24F	FY25F
Revenue	**779.9**	**856.6**	**721.0**	**763.7**	**855.1**
Operating cost	-573.9	-649.7	-526.3	-553.6	-615.7
EBITDA	**119.6**	**131.6**	**131.0**	**142.6**	**164.0**
Depreciation & ammortisation	-42.3	-27.1	-39.4	-40.7	-42.9
EBIT	**77.3**	104.5	**91.6**	**101.9**	**121.1**
Interest income	0.2	1.2	2.4	4.3	5.6
Interest expense	-14.8	-18.7	-17.2	-17.6	-18.6
Pre-tax profit	**84.5**	**105.6**	**76.8**	**88.6**	**108.1**
Income tax	-2.5	-23.0	-2.2	-2.6	-3.1
Core Net profit	**64.3**	**72.4**	**74.6**	**86.0**	**105.0**

Balance Sheet

FYE 31 Dec (USDmn)	FY21	FY22	FY23F	FY24F	FY25F
Non-Current Asset	561.1	554.3	533.6	514.2	520.6
Current Asset	382.5	331.7	384.6	460.2	550.6
Total Asset	**943.6**	**886.0**	**918.2**	**974.4**	**1,071.3**
Non-Current Liabilities	271.7	291.2	291.2	296.2	311.2
Current Liabilities	228.2	195.1	178.7	169.7	178.0
Total Liabilities	**499.9**	**486.3**	**469.9**	**465.9**	**489.2**
Total Equity	**443.7**	**399.7**	**448.3**	**508.5**	**582.0**
Total liabilities & equity	**943.6**	**886.0**	**918.2**	**974.4**	**1,071.3**

Cash Flow

FYE 31 Dec (USDmn)	FY21	FY22	FY23F	FY24F	FY25F
Cash flow from operating activities (CFO)	**70.2**	**197.0**	**165.9**	**196.6**	**274.4**
Cash flow from investing activities (CFI)	**4.4**	**-30.9**	**-19.6**	**-22.1**	**-50.2**
Cash flow from financing activities (CFF)	**-40.2**	**-180.7**	**-83.2**	**-78.5**	**-153.6**
Net change in cash & cash equivalent	**34.4**	**-14.7**	**63.1**	**95.9**	**70.6**

Source: Company, BIMB Securities

DEFINITION OF RATINGS

BIMB Securities uses the following rating system:

STOCK RECOMMENDATION

BUY	Total return (price appreciation plus dividend yield) is expected to exceed 10% in the next 12 months.
TRADING BUY	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain.
HOLD	Share price may fall within the range of +/- 10% over the next 12 months
TAKE PROFIT	Target price has been attained. Fundamentals remain intact. Look to accumulate at lower levels.
TRADING SELL	Share price may fall by more than 15% in the next 3 months.
SELL	Share price may fall by more than 10% over the next 12 months.
NOT RATED	Stock is not within regular research coverage.

SECTOR RECOMMENDATION

OVERWEIGHT	The Industry as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 12 months
NEUTRAL	The Industry as defined by the analyst's coverage universe, is expected to perform in line with the relevant primary market index over the next 12 months
UNDERWEIGHT	The Industry as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 12 months

Applicability of ratings

The respective analyst maintains a coverage universe of stocks, the list of which may be adjusted according to needs. Investment ratings are only applicable to the stocks which form part of the coverage universe. Reports on companies which are not part of the coverage do not carry investment ratings as we do not actively follow developments in these companies.

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