Cahya Mata Sarawak Berhad

(2852 | CMSB MK) Main | Construction

Dispute with SESCO in Arbitration

Maintain **BUY**

Unchanged **Target Price: RM1.55**

KEY INVESTMENT HIGHLIGHTS

- **Dispute between Cahya Mata Phosphates Industries and SESCO regarding PPA now in arbitration**
- **SESCO deemed the PPA terminated and planned to terminate electricity supply on May 15, a decision which was then reversed**
- **CMSB maintained PPA still on foot, determined to find favourable solution**
- **Maintain BUY with an unchanged TP of RM1.55**

Dispute with SESCO. There is an ongoing dispute between Cahya Mata Sarawak Bhd's (CMSB's) 80.18%-owned Cahya Mata Phosphates Industries Sdn Bhd and Sarawak Energy Bhd's utility arm Syarikat SESCO Bhd, regarding a power purchase agreement (PPA) that was inked on Jan 15, 2019. This had to do with the commercialisation milestone that was set in the PPA. In a call yesterday evening, management said the plant's progress suffered delays due to the Covid-19 pandemic but SESCO is adamant in charging Cahya Mata Phosphates a higher tiered tariff, which does not reflect the plant's current status. The dispute is now in arbitration.

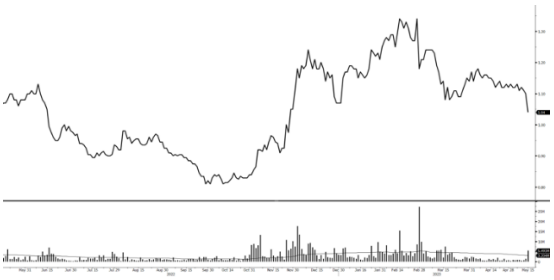
Yet to achieve commercial operations. While the phosphate plant in Samalaju has been fully commissioned with all the four furnaces fired up in Dec-22, it has yet to commence commercialisation as Cahya Mata Phosphates is still awaiting approvals for necessary licenses for it to begin selling. Management guided that it was stated clearly in the PPA that the higher tariff would only kick in upon commercialisation, which is when it starts selling products, which has yet to happen to date. It currently has about 10,000 drums of phosphorus in its inventory which cannot be sold yet unless it acquires all the required licenses. SESCO billed CMSB RM266m for cumulative electricity consumption shortfall and payment security shortfall as of Dec 31, 2022.

Threats of power termination. SESCO had on May 11, issued a default notice that the PPA with Cahya Mata Phosphates was deemed terminated and that it would terminate the electricity supply to its plant, a decision which was then reversed though SESCO maintained that the PPA was terminated. CMSB's management maintained that the PPA is still on foot. We note that it is still business as usual at the phosphate plant with no issues on the electricity supply.

Delay in arbitration. The dispute has since been in arbitration since Nov-22 when Cahya Mata Phosphates commenced the proceedings against SESCO with the Asian International Arbitration Centre (AIAC). There is a however, a delay in the process due to the delay of the appointment of the AIAC director. The position was vacant for three months since Dec-22 until the new director was appointed in Mar-23. CMSB reaffirmed its dedication to protect its rights and will continue to pursue possible ways to resolve the matter amicably. An arbitration will usually take about 18 to 24 months.

RETURN STATISTICS	
Price @ 15th May 2023 (RM)	1.04
Expected share price return (%)	+49.04
Expected dividend yield (%)	1.94
Expected total return (%)	**+50.98**

SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	-9.6	-8.4
3 months	-8.8	-18.5
12 months	-3.7	4.9

INVESTMENT STATISTICS

FYE Dec	2022A	2023E	2024F
Revenue	1009.0	1,187.5	1,211.3
Operating Profit	259.5	116.4	119.9
Profit Before Tax	412.3	213.8	285.9
Core net profit	118.7	207.8	200.8
Core EPS (sen)	11.1	19.4	21.5
DPS (sen)	3.0	3.0	3.0
Dividend Yield	2.0%	2.0%	2.0%

KEY STATISTICS	
FBM KLCI	1,417.37
Issue shares (m)	1073.98
Estimated free float (%)	55.71
Market Capitalisation (RM'm)	1,117.14
52-wk price range	RM0.8 - RM1.36
3-mth average daily volume (m)	3.23
3-mth average daily value (RM'm)	3.89
Top Shareholders (%)	
Majaharta Sdn Bhd	12.55
Leija Taib	10.33
Lembaga Tabung Haji	7.46

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Contingent liability. CMSB has recognised a contingent liability of RM266m in its FY22 financial statements, arising from the PPA dispute, which is the amount billed by SESCO. The group said the termination of the PPA and electricity supply could have possible impact on the Phosphates business operations and Cahya Mata Group's financial performance, though legal advice it has obtained said Cahya Mata Phosphates is not liable to pay the amount billed by SESCO on the basis that it has yet to achieve commercialisation during the financial year.

Earnings estimates. We maintain our projections pending further developments of the dispute.

Target price. Our **TP** is maintained at **RM1.55** as we peg the group's FY23E EPS of 19.4 sen per share to a PER of 8x.

Maintain BUY. We maintain our positive outlook for CMSB, pending further developments on the arbitration of the dispute. We remain optimistic that it would be able to be resolved amicably, for the betterment of Sarawak's economy. The group's integrated phosphate complex in Samalaju is the only one of its kind in Malaysia whereas in the region, there has been no new entrant at least over the past decade in a market dominated by Vietnam and Kazakhstan producers. CMSB's plant has an annual capacity of 57,600 metric tonnes or 288,000 drums. Management's initial target for commercialisation was mid-2023, though we do not discount the possibility of delays due to the ongoing dispute. On another note, we remain sanguine on CMSB's earnings outlook in FY23, as the expected improvement in construction job flows would benefit the group in terms of cement supply, construction projects and road maintenance jobs. We reiterate our **BUY** recommendation on **CMSB**.

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023E	2024F	2025F
Revenue	814.6	1,009.0	1,187.5	1,211.3	1,367.7
Gross profit	145.3	188.0	290.9	245.9	288.6
Operating profit	62.1	259.5	116.4	119.9	123.2
Finance costs	(28.3)	(18.40)	(23.8)	(24.2)	(27.4)
Profit before tax	234.6	412.3	213.8	285.9	300.9
Tax	(29.9)	(110.7)	(42.8)	(57.2)	(60.2)
Net profit	204.2	298.1	207.8	200.8	247.5
Core net profit	172.1	118.7	207.8	200.8	247.5

Balance Sheet (RM'm)	2021A	2022A	2023E	2024F	2025F
Fixed assets	1,342.3	1,420.0	1,462.6	1,506.5	1,551.7
Intangible assets	0.6	2.4	3.0	3.5	3.5
Non-current assets	**3,119.6**	**2,867.5**	**2,953.5**	**3,042.1**	**3,133.4**
Cash	545.7	965.3	772.2	787.7	803.4
Trade debtors	191.0	250.5	255.5	260.6	265.8
Current assets	1,729.9	2,046.0	2,107.4	2,170.6	2,235.7
Trade creditors	615.9	688.2	702.0	716.0	730.3
Short-term debt	625.1	282.0	286.2	286.2	286.2
Current liabilities	**1,260.1**	**1,050.6**	**1,103.1**	**1,158.3**	**1,216.2**
Long-term debt	273.4	255.8	255.8	255.8	255.8
Non-current liabilities	**357.0**	**374.7**	**382.2**	**389.8**	**397.6**
Share capital	867.9	867.9	867.9	867.9	867.9
Retained earnings	2,122.9	2,399.6	2,607.4	2,808.2	3,055.7
Equity	**3,232.4**	**3,488.8**	**3,488.8**	**3,488.8**	**3,488.8**

Cash Flow (RM'm)	2021A	2022A	2023E	2024F	2025F
PBT	**234.6**	**412.3**	**213.8**	**285.9**	**300.9**
Depreciation & amortisation	63.0	63.5	64.1	64.8	65.43
Changes in working capital	132.6	-64.4	-19.3	-5.8	-5.8
Operating cash flow	**220.7**	**9.7**	**115.4**	**139.3**	**144.9**
Capital expenditure	-88.8	-43.7	-78.7	-82.6	-86.7
Investing cash flow	**25**	**823.5**	**247.1**	**247.1**	**247.1**
Debt raised/(repaid)	36.7	-376.5	-125	-125	**-**
Dividends paid	-35.5	-23.5	-23.5	-23.5	-23.5
Financing cash flow	**16.7**	**-410.5**	**-150**	**-150**	**-30**
Net cash flow	**262.4**	**422.8**	**212.5**	**236.4**	**362**
Beginning cash flow	**277.2**	**540.7**	**962.7**	**1,175.2**	**1,411.6**
Ending cash flow	**540.7**	**962.7**	**1,175.2**	**1,411.6**	**1,773.6**

Profitability Margins	2021A	2022A	2023E	2024F	2025F
Gross profit margin	17.8%	18.6%	24.5%	20.3%	21.1%
PBT margin	28.8%	40.9%	18.0%	23.6%	22.0%
PAT margin	25.1%	29.5%	17.5%	16.6%	18.1%
Core PAT margin	21.1%	11.8%	17.5%	16.6%	18.1%

Source: Bloomberg, MIDFR

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MIDF AMANAH INVESTMENT BANK: GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology