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OSK



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## Corporate News Flash

# Malaysia Steel Works (KL)

## *RM300m Expansion*

**STEEL**

**BUY**

| | |
|---|---|
| **Target** | **RM1.45** |
| **Previous** | **RM1.45** |
| **Price** | **RM1.05** |

### THE BUZZ

Malaysia Steel Works (KL) (Masteel) announced to Bursa Malaysia that the Company intends to invest approximately RM300m in a downstream expansion project to meet demand from the growing local and export markets. The project will be located adjacent to the company's existing meltshop in Bukit Raja, Klang, covering about 20 acres. The feedstock will be the company's billets produced at the meltshop. There is no immediate effect but once the project is completed in 2 years, the company sees it auguring for its margin and profitability. Consequently, this should improve stakeholders' value and expectations.

### OUR TAKE

**Improving efficiency.** The project details are sketchy and management is not reachable for comment. Nonetheless, as the project will be adjacent to the existing meltshop in Bukit Raja, Klang, it will definitely help to integrate the company's operation and hence efficiency and margins. Presently, Masteel operates a 450,000 tonne per year (tpy) meltshop in Klang but its 350,000 tpy downstream operation is separately located in Petaling Jaya some 15km away. Putting the upstream and downstream operations together obviously will translate into savings in terms of transport and handling costs, which may come to USD5 to USD10 per tonne. Also, an integrated operation would allow continuous casting, which would lead to savings on energy costs as the hot billets can be rolled over directly to finished goods without the need for re-heating.

**Up the value chain?** While we see some potential cost benefits from the plant integration, we think that it may not justify the huge Capex investment of RM300m unless it comes with other forms of investment. In addition, Masteel can opt to relocate its existing rolling mill to Klang, which may cost no more than RM30m. As the company's downstream operation is now limited to steel bar production and management indicated that the feed material for the new plant will be the company's own billets, we suspect that it may be looking to invest in industrial grade wire rods. Apart from that, we also think the investment may cover light section rolling mills such as “C”, “L” and “U” channels and others that offer better margins.

**Reiterate BUY.** Pending further details, our main concern on the proposal is the company's gearing, which may increase from 0.53x to 1.26x if the RM300m expansion eventually kicks in. Meanwhile, we also suspect the quoted Capex may be on the high side considering the investment proposal is only limited to downstream expansion. Aside from balance sheet concerns, we stick to our bullish view on the company being the beneficiary of the potential price and demand escalation post Chinese New Year celebrations, and thus maintain our BUY call on Masteel. Our target price of RM1.45 is derived from a blended valuation of 6x FY10 EPS and 0.59x NTA/share, or +1 standard deviation of its historical trading band.

**OSK Research 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 (NR)**: Stock is not within regular research coverage

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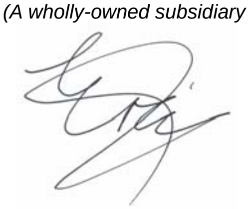

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