

Malaysia Steel Works (KL)

Recommendation: **BUY**

Stock Code: **5098**

Bloomberg: **MSW MK**

Price: **MYR0.94**

12-Month Target Price: **MYR1.10**

Date: **June 1, 2010**

Board: Main

Sector: Industrial Products

GICS: Materials/Steel

Market Value - Total: MYR193.0 mln

Summary: Malaysia Steel Works (KL) (Masteel) is a steel producer with a capacity of 800,000 tons per annum (tpa). It produces steel billets and bars that are sold to downstream steel companies for the manufacturing of bars and other long products for the construction sector. The stock is a component of FBM EMAS.

Analyst: Su Peng Ng



Results Review & Earnings Outlook

- Masteel's 1Q10 results were below our expectations as margins were lower than expected. Net profit of MYR6.4 mln accounted for only 15% of our previous 2010 estimate.
- 1Q10 revenue surged 48% YoY on the back of higher demand and average selling prices (ASPs), as global and domestic economies rebound. With a lower average raw material cost for 1Q10, Masteel turned in an operating profit of MYR9.7 mln compared with a loss of MYR26.8 mln in 1Q09.
- Improved ASPs boosted 1Q10 revenue marginally over 4Q09. However, due to rising raw material costs, operating profit fell 31% QoQ.
- We look for Masteel to post better results as the year progresses, as steel prices adjust to higher iron ore and scrap prices in 2Q10. Masteel has also been producing at full capacity in the last few months, indicating demand is strong. In addition, we anticipate an increasing pace of domestic infrastructure rollout in 2H10, which should boost Masteel's second half earnings.
- Nevertheless, with poor 1Q10 results, we adjust our 2010-2011 estimates after imputing a higher cost of sales. Our new 2010 and 2011 net profit estimates are MYR30 mln (from MYR42.1 mln) and MYR36 mln (from MYR51.2 mln) respectively.

Recommendation & Investment Risks

- We lower our recommendation on Masteel to a Buy (from Strong Buy) with a lower 12-month target price of MYR1.10 (from MYR1.35).
- Our target price remains derived using a blend of PER and P/B methodology. We utilize a PER of 6x (from 7x) and P/B of 0.5x (from 0.6x) against our estimated 2011 (rolled over from 2010) EPS and BVPS respectively. The lower multiples reflect lower peer valuations.
- Masteel recently proposed an issue of 1 warrant for every 2 shares held to raise MYR21.4 mln to fund working capital. The dilution from these warrants on the group's FY11 EPS is a significant 28%. We believe that Masteel may be preserving its gearing levels in anticipation of its new MYR300 mln downstream project that is expected to come in by 2012. Despite the longer-term plans, we believe the dilutive aspect of the warrants issue will possibly cap upside in the near term and is a factor in our downgrade.
- Risks to our recommendation and target price include lower steel prices, higher-than-expected raw material prices and lower-than-expected demand.

Key Stock Statistics

FY Dec.	2009	2010E
Reported EPS (sen)	-4.4	14.6
PER (x)	NM	6.4
Dividend/Share (sen)	0.0	2.3
NTA/Share (MYR)	1.95	1.41
Book Value/Share (MYR)	1.95	2.20
No. of Outstanding Shares (mln)	205.4	
52-week Share Price Range (MYR)	0.87 - 1.17	
Major Shareholders:	%	
Soon Seng Company	20.6	
Lembaga Tabung Haji	5.8	
Ikhwan Salim bin Sujak	5.2	

Per Share Data

FY Dec.	2007	2008	2009	2010E
Book Value (MYR)	1.83	2.21	1.95	2.20
Cash Flow (sen)	29.6	48.5	4.0	25.4
Reported Earnings (sen)	22.8	48.2	-4.4	14.6
Dividend (sen)	2.3	2.3	0.0	2.3
Payout Ratio (%)	9.9	5.5	0.0	15.4
PER (x)	4.1	2.0	NM	6.4
P/Cash Flow (x)	3.2	1.9	23.7	3.7
P/Book Value (x)	0.5	0.4	0.5	0.4
Dividend Yield (%)	2.4	2.4	0.0	2.4
ROE (%)	13.5	20.2	-2.0	6.9
Net Gearing (%)	54.8	51.9	53.0	74.8

* Stock deemed Shariah compliant by the Securities Commission

All required disclosures and analyst certification appear on the last two pages of this report. Additional information is available upon request.

Redistribution or reproduction is prohibited without written permission. Copyright © 2010 The McGraw-Hill Companies, Inc.

Page 1 of 4

Malaysia Steel Works (KL)

Recommendation: **BUY**Stock Code: **5098**Bloomberg: **MSW MK**Price: **MYR0.94**12-Month Target Price: **MYR1.10**Date: **June 1, 2010****Quarterly Performance**

FY Dec. / MYR mln	1Q10	1Q09	% Change
Reported Revenue	192.1	130.1	47.7
Reported Operating Profit	9.7	-26.8	NM
Depreciation & Amortization	NA	NA	NA
Net Interest Income / (Expense)	-3.0	-3.6	-16.1
Reported Pre-tax Profit	6.7	-30.4	NM
Reported Net Profit	6.4	-30.4	NM
Reported Operating Margin (%)	5.1	-20.6	-
Reported Pre-tax Margin (%)	3.5	-23.4	-
Reported Net Margin (%)	3.3	-23.4	-

Source: Company data

Profit & Loss

FY Dec. / MYR mln	2008	2009	2010E	2011E
Reported Revenue	881.2	687.3	812.5	960.4
Reported Operating Profit	99.4	5.6	47.3	59.4
Depreciation & Amortization	-15.1	-16.2	-22.2	-28.2
Net Interest Income / (Expense)	-13.5	-14.1	-15.7	-21.5
Reported Pre-tax Profit	85.7	-8.4	31.5	37.9
Effective Tax Rate (%)	7.5	NM	5.0	5.0
Reported Net Profit	79.3	-8.5	30.0	36.0
Reported Operating Margin (%)	11.3	0.8	5.8	6.2
Reported Pre-tax Margin (%)	9.7	-1.2	3.9	3.9
Reported Net Margin (%)	9.0	-1.2	3.7	3.8

Source: Company data, S&P Equity Research

Standard & Poor's Equity Research Services

Standard & Poor's Equity Research Services U.S. includes Standard & Poor's Investment Advisory Services LLC; Standard & Poor's Equity Research Services Europe includes Standard & Poor's LLC- London; Standard & Poor's Equity Research Services Asia includes Standard & Poor's LLC's offices in Hong Kong and Singapore, Standard & Poor's Malaysia Sdn Bhd, and Standard & Poor's Information Services (Australia) Pty Ltd.

Glossary

Strong Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months, with shares rising in price on an absolute basis.

Hold: Total return is expected to closely approximate the total return of the KLCI or KL Emas Index respectively, over the coming 12 months with shares generally rising in price on an absolute basis.

Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months and share price is not anticipated to show a gain.

Strong Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months by a wide margin, with shares falling in price on an absolute basis.

S&P 12 Month Target Price – The S&P equity analyst's projection of the market price a given security will command 12 months hence, based on a combination of intrinsic, relative, and private market valuation metrics.

Shariah-compliant stock - As defined by the Shariah Advisory Council of Malaysia's Securities Commission

Required Disclosures

All of the views expressed in this research report accurately reflect the research analyst's personal views regarding any and all of the subject securities or issuers. No part of analyst compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

Additional information is available upon request.

Other Disclosures

This report has been prepared and issued by Standard & Poor's and/or one of its affiliates. In the United States, research reports are prepared by Standard & Poor's Investment Advisory Services LLC ("SPIAS"). In the United States, research reports are issued by Standard & Poor's ("S&P"); in the United Kingdom by Standard & Poor's LLC ("S&P LLC"), which is authorized and regulated by the Financial Services Authority; in Hong Kong by Standard & Poor's LLC, which is regulated by the Hong Kong Securities Futures Commission; in Singapore by Standard & Poor's LLC, which is regulated by the Monetary Authority of Singapore; in Malaysia by Standard & Poor's Malaysia Sdn Bhd ("S&PM"), which is regulated by the Securities Commission; in Australia by Standard & Poor's Information Services (Australia) Pty Ltd ("SPIS"), which is regulated by the Australian Securities & Investments Commission; and in Korea by SPIAS, which is also registered in Korea as a cross-border investment advisory company.

The research and analytical services performed by SPIAS, S&P LLC, S&PM, and SPIS are each conducted separately from any other analytical activity of Standard & Poor's.

A reference to a particular investment or security by Standard & Poor's and/or one of its affiliates is not a recommendation to buy, sell, or hold such investment or security, nor is it considered to be investment advice.

Indexes are unmanaged, statistical composites and their returns do not include payment of any sales charges or fees an investor would pay to purchase the securities they represent. Such costs would lower performance. It is not possible to invest directly in an index.

Standard & Poor's and its affiliates provide a wide range of services to, or relating to, many organizations, including issuers of securities, investment advisers, broker-dealers, investment banks, other financial institutions and financial intermediaries, and accordingly may receive fees or other economic benefits from those organizations, including organizations whose securities or services they may recommend, rate, include in model portfolios, evaluate or otherwise address.

CMDF-Bursa Research Scheme ("CBRS")

This report has been prepared by S&PM for purposes of CBRS administered by Bursa Malaysia Berhad, independent from any influence from CBRS or the subject company. S&P will receive total compensation of RM15,000 each year for each company covered by it under CBRS. For more information about CBRS, please visit Bursa Malaysia's website at: <http://www.bursamalaysia.com/website/bm/>

Disclaimers

This material is based upon information that we consider to be reliable, but neither S&P nor its affiliates warrant its completeness, accuracy or adequacy and it should not be relied upon as such. With respect to reports issued to clients in Japan and in the case of inconsistencies between the English and Japanese version of a report, the English version prevails. With respect to reports issued to clients in Germany and in the case of inconsistencies between the English and German version of a report, the English version prevails. Neither S&P nor its affiliates guarantee the accuracy of the translation. Assumptions, opinions and estimates constitute our judgment as of the date of this material and are subject to change without notice. Neither S&P nor its affiliates are responsible for any errors or omissions or for results obtained from the use of this information. Past performance is not necessarily indicative of future results.

This material is not intended as an offer or solicitation for the purchase or sale of any security or other financial instrument. Securities, financial instruments or strategies mentioned herein may not be suitable for all investors. Any opinions expressed herein are given in good faith, are subject to change without notice, and are only correct as of the stated date of their issue. Prices, values, or income from any securities or investments mentioned in this report may fall against the interests of the investor and the investor may get back less than the amount invested. Where an investment is described as being likely to yield income, please note that the amount of income that the investor will receive from such an investment may fluctuate. Where an investment or security is denominated in a different currency to the investor's currency of reference, changes in rates of exchange may have an adverse effect on the value, price or income of or from that investment to the investor. The information contained in this report does not constitute advice on the tax consequences of making any particular investment decision. This material is not intended for any specific investor and does not take into account your particular investment objectives, financial situations or needs and is not intended as a recommendation of particular securities, financial instruments or strategies to you. Before acting on any recommendation in this material, you should consider whether it is suitable for your particular circumstances and, if necessary, seek professional advice.

For residents of the U.K. This report is only directed at and should only be relied on by persons outside of the United Kingdom or persons who are inside the United Kingdom and who have professional experience in matters relating to investments or who are high net worth persons, as defined in Article 19(5) or Article 49(2) (a) to (d) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, respectively.

For residents of Singapore - Anything herein that may be construed as a recommendation is intended for general circulation and does not take into account the specific investment objectives, financial situation or particular needs of any particular person. Advice should be sought from a financial adviser regarding the suitability of an investment, taking into account the specific investment objectives, financial situation or particular needs of any person in receipt of the recommendation, before the person makes a commitment to purchase the investment product.

For residents of Malaysia. All queries in relation to this report should be referred to Alexander Chia, Desmond Ch'ng or Ching Wah Tam.

Required Disclosures

Recommendation and Target Price History

Date	Recommendation	Target Price
New	Buy	1.10
24-Feb-10	Strong Buy	1.35
27-Aug-09	Strong Buy	1.15
29-May-09	Buy	1.05
6-May-09	Buy	0.95
19-Feb-09	Buy	0.75
27-Nov-08	Hold	0.75
2-Sep-08	Strong Buy	1.40
6-Jun-08	Strong Buy	1.95
2-Jun-08	Strong Buy	1.88
3-Mar-08	Strong Buy	1.76
23-Nov-07	Strong Buy	1.50
5-Nov-07	Strong Buy	1.46
30-Aug-07	Strong Buy	1.61

