ecmlibra INVESTMENT RESEARCH

27 August 2008

KNM Group — Buy

(RM1.61 KNMG MK) *Target Price: RM1.81*

2QFY08 : Borsig trickles in — OIL & GAS

- **Within Expectations**
  With the consolidation of Borsig from 6th June, 2Q08 earnings got a boost from the <1month contributions from KNM's latest acquisition. 1H08 net profit now makes up 36.8% of our full year net profit projections and similarly for street estimates.

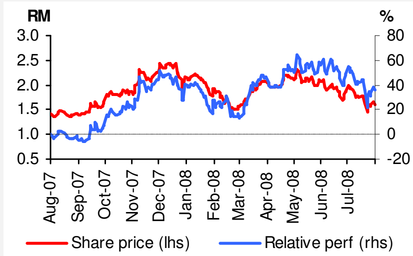
- **Margins on the rise**
  Margins for 1H08 have improved to 16.2% from 14.4% in the previous corresponding quarter and this is much within expectations. As mentioned before, KNM has been actively doing away with manufacture of low end process equipment and increased its profile in the high end and mid end segment through several key acquisitions as well as internal changes in capabilities.

- **Other points to highlight – est. RM4.4bn orderbook**
  KNM's orderbook continues to be strong and the group recently added another RM463m to its orderbook over June. To note, of total orderbook, Borsig accounts for about RM1.5bn. Also to note, average selling price per tonne should see a trading up, nearing RM18,000 per mt by year end from <RM15,000 per mt seen over 2007. Towards 2009 however, this should increase to >RM22,000 per mt. Current manufacturing capacity of the Group stands at 160,300 mt while utilisation is at an estimated 88%. This is because newer capacity takes some time to come on-stream. Looking into 2009, we expect capacity to grow by at least 15% from organic growth in their plants and utilisation is expected to be optimum at 90%.

- **Maintain BUY. TP RM1.81**
  We see it hard to fault KNM at this juncture as with earnings from Borsig coming through, even a high interest rate paid on the RM600m term loan would damage bottom-line only minimally. The Group still is on a steep growth path and despite that some smaller acquisitions do not go as smoothly as expected (like HZM in Brazil); organic growth by itself can pull them through double digit growth. Process equipment has vast applications, not just for the oil & gas industry, but in the food, chemical and even biodiesel/ethanol industries hence there is a lot of long term potential seen in their business. The group will hold a briefing on the 28th of August.

FYE 31 Dec RM m	2Q08	1Q08	2Q07	% YoY chg	% QoQ chg	6M08	6M07	% YoY chg
Revenue	599.4	331.2	262.8	128.1	81.0	930.6	525.0	77.3
EBITDA	122.5	66.8	38.6	217.6	83.3	189.4	86.1	119.8
PBT	109.5	61.4	33.6	226.0	78.2	171.0	78.5	117.9
Net Profit	96.3	54.1	37.1	159.7	77.9	150.4	75.4	99.5
Margin (%)								
EBITDA	20.4%	20.2%	14.7%			20.4%	16.4%	
Net Profit	16.1%	16.3%	14.1%			16.2%	14.4%	
EPS (sen)	2.43	1.37	0.94			3.80	1.91	
DPS (sen)	-	-	-			-	-	
NTA (RM)						1.09	1.05	

Share Price Chart



Source: Bloomberg

Price Performance

Price (RM)			1.61
52-week Range (RM)			2.44 – 1.35
Avg Daily Volume ('000)			13513
	1M	3M	6M
Absolute (%)	-14.4	-25.1	-16.8
Relative (%)	-8.7	-11.7	7.1

Key Data

Market Cap (RM m)	6527
Issued Shares (m)	3956
Free Float	70.7

Major Shareholders	%
Inter Merger Sdn Bhd	24.5
EPF	3.5
Small Cap World Fund	3.0

Balance Sheet Highlights (RM m)
(@ 31.12.2008) (performance indicator's annualised)

Total Assets	1249.7
Total Liabilities	263.4
Total Debt (Gross)	1245.9
Shareholders' Equity	576.6
Return on Assets (%)	18.2
Return on Equity (%)	72.1
Net Cash / Share (RM)	9.7
Debt/Equity (x)	2.2
Interest Cover (x)	8.6

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KNM Group — **Financial Summary** — **Share Price: RM 1.61**

Balance Sheet	**2006**	**2007**	**2008E**	**2009E**	**2010E**
FY 31 Dec (RM'mil)					
Fixed Assets	457.0	524.9	1234.5	1320.9	1406.2
Intangible Assets	4.2	6.7	6.7	6.7	6.7
Inventories	24.8	62.2	51.7	72.5	86.4
Receivables	438.5	547.9	1082.6	1519.8	1775.1
Other Asset	0.0	2.7	2.7	2.7	2.7
Cash and ST Funds	91.2	105.3	861.8	606.9	653.3
Total Assets	**1015.7**	**1249.7**	**3240.0**	**3529.3**	**3930.3**
Payables	295.6	310.4	465.7	652.3	734.3
ST Borrowings	156.6	220.9	1,021.6	980.6	939.6
Other ST Liability	27.9	27.7	859.1	806.2	885.4
LT Borrowings	42.9	45.0	224.3	215.3	206.3
Other LT Liability	87.6	90.0	92.7	95.2	97.7
Liabilities	**610.7**	**694.0**	**2,663.4**	**2,749.6**	**2,863.3**
MI	14.7	0.2	0.2	0.2	0.2
Share Capital	128.9	261.6	262.4	262.4	262.4
Reserves	261.4	293.8	314.0	517.1	804.4
Shareholders' Fund	**405.0**	**555.7**	**576.6**	**779.7**	**1,067.0**
Liabilities & Equities	**1,015.7**	**1,249.7**	**3,240.0**	**3,529.3**	**3,930.3**
Cashflow Statement	**2006**	**2007E**	**2008E**	**2009E**	**2010E**
FY 31 Dec (RM'mil)					
Profit Before Tax	147.5	170.3	473.8	698.2	794.1
Dep/Amortisation	8.2	5.6	9.6	13.6	14.6
Financing Cost	2.7	34.4	34.4	35.2	36.1
Change in WC	-	(57.3)	(286.3)	(333.3)	(159.4)
Other Non-cash Items	(26.4)	(62.0)	(98.4)	(161.0)	(147.2)
Tax Paid	(138.2)	28.9	64.0	97.7	111.2
Operating Cashflow	**(28.1)**	**120.0**	**197.1**	**350.5**	**649.3**
	(34.3)				
Capex		(101.0)	(700.0)	(100.0)	(100.0)
Disposal	(23.5)	-	-	-	-
Others	4.5	-	-	-	-
Investing Cashflow	**(18.9)**	**(101.0)**	**(700.0)**	**(100.0)**	**(100.0)**
Equity Raised	22.4	10.3	11.3	-	-
Borrowings	(5.5)	2,000.0	-	-	-
Repayment	108.4	-	(20.0)	(50.0)	(50.0)
Dividends Paid	(29.6)	(284.8)	(395.6)	(395.6)	(395.6)
Others	95.7	38.0	(62.3)	(59.8)	(57.3)
Financing Cashflow		**1,763.4**	**(466.6)**	**(505.4)**	**(502.9)**
	42				
Net Cashflow	15.6	2.1	(969.5)	(254.9)	46.4
Changes in Forex	58.0	-	-	-	-
Beginning Cash		48.9	1,831.3	861.8	606.9
Ending Cash	**(57.8)**	**51.0**	**861.8**	**606.9**	**653.3**

Income Statement	**2006**	**2007**	**2008E**	**2009E**	**2010E**
FY 31 Dec (RM'mil)					
Revenue	909.0	1,230.1	2,634.4	3,698.2	4,319.4
EBITDA	131.5	228.6	545.7	799.6	866.0
Dep/Amortisation	2.5	5.6	9.6	13.6	14.6
EBIT	129.0	223.0	536.1	786.0	851.4
Other Operating Income	16.4	-	-	-	-
Financing Cost	(8.9)	(7.5)	(62.3)	(87.8)	(57.3)
Exceptional Item	-	-	-	-	-
Pretax Profit	**147.5**	**215.6**	**473.8**	**698.2**	**794.1**
Taxation	(9.4)	(28.9)	(64.0)	(97.7)	(111.2)
Minority Interest	(5.7)	1.7	(1.7)	(1.7)	(1.7)
Net Profit	**132.5**	**188.3**	**408.2**	**598.8**	**681.2**
FY 31 Dec (RM'mil)					
Growth					
Turnover	164	35	114	40	17
EBITDA	137	74	139	47	8
Pretax Profit	178	46	120	47	14
Net Profit	222	42	117	47	14
EPS	97	-67	-43	47	14
Efficiency					
Inv. Processing (days)	8	16	10	10	10
Rec. Collection (days)	115	146	150	150	150
Pay. Payment (days)	94	113	90	90	85
Cash Conversion (days)	28	49	70	70	75
Profitability					
EBITDA Margin	14.5%	18.6%	20.7%	21.6%	20.0%
Pretax Profit Margin	16.2%	17.5%	18.0%	18.9%	18.4%
Net Profit Margin	14.6%	15.3%	15.5%	16.2%	15.8%
Return on Asset	19.3%	16.6%	18.2%	17.7%	18.3%
Return on Equity	47.1%	39.2%	72.1%	88.3%	74.0%
Leverage					
Total debt/Total Asset(x)	0.2	0.2	0.4	0.3	0.3
Total debt/Equity (x)	0.5	0.5	2.2	1.5	1.1
Net Gearing Ratio (%)	26.7%	28.9%	66.6%	75.5%	-168.6%
Valuations					
EPS (sen)	54.1	18.0	10.3	15.1	17.3
PER (x)	3.0	8.9	15.6	10.6	9.3
DPS (sen)	6.9	10.0	10.0	10.0	10.0
Dividend Yield (%)	4.3%	6.2%	6.2%	6.2%	6.2%
NTA/Share	1.55	1.05	1.09	1.48	2.03
P/NTA (x)	1.0	1.5	1.5	1.1	0.8

For ECM Libra Capital Sdn Bhd (579116-A) (PP 13693/03/2009(020539)