STANDARD & POOR'S

Lysaght Galvanized Steel

Recommendation: **HOLD**

Stock Code: 9199 | Bloomberg: LYSA MK | Price: MYR1.00 | 12-Month Target Price: MYR1.10 | Date: March 27, 2008

Board: Second

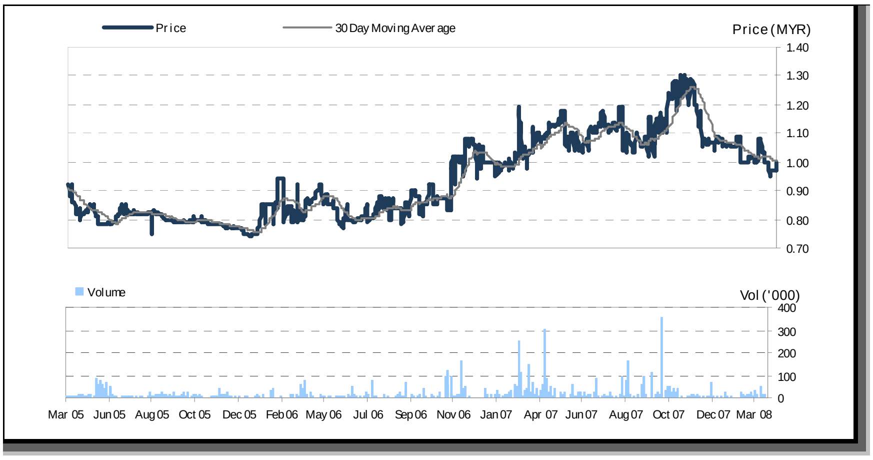
Sector: Industrial Products

GICS: Materials/Steel

Market Value - Total: MYR41.6 mln

Summary: Lysaght Galvanized Steel (Lysaght) is one of two domestic manufacturers of poles and masts. Its products are utilized in a variety of industries, in particular in road and highway lighting, traffic gantry, air and sea port terminals as well as telecommunication antennas. The group has an annual production capacity of 24,000 tpa.

Analyst: Su Peng Ng



Highlights

- We expect a tougher 2008 for Lysaght with lower revenue and margin compression reflecting a slowdown in construction related projects compounded by surging raw material costs.
- We believe volume sales will decline as potential infrastructure projects are reviewed with roll-out being deferred after the recent general election results.
- Furthermore, Lysaght's main raw material component, hot-rolled coils (HRC) is expected to increase in price after the recent agreement between global steel millers and iron ore producers for a 65% increase in iron ore prices.
- Despite declining zinc prices (Lysaghts's other main raw material) and an appreciating MYR against the US$, we expect higher steel prices and lower sales volume to squeeze in 2008 operating profit margins to 12% from 13.5% in 2007.

Investment Risks

- Risks to our recommendation and target price include slower-than-expected implementation of infrastructure projects and higher-than-expected raw material costs.

Recommendation

- We initiate coverage on Lysaght with a Hold recommendation and a 12-month target price of MYR1.10.
- We utilize a relative valuation methodology to arrive at our target price. As Lysaght does not have a direct listed peer, our target multiple is benchmarked our target PER for small-to-mid-sized contractors within our coverage ranging from 10x-12x. Our target PER multiple of 6.5x is applied against 2008 earnings EPS and we add our estimated 2007 tax-exempt DPS of 4 sen to arrive at our 12-month target price. The target multiple is a 35% discount to the lower end of our PER range for small- to mid-sized contractors and reflects Lysaght's relatively small market capitalization and thin trading volume. The target multiple is also a discount to Lysaght's historical average trading PER of 7.5x.
- We believe Lysaght's share price has reflected most of the potential negative news with regards to possible lower sales and rising raw material costs. We expect the decent dividend yield of 4.1% to support its share price. As such, we believe downside is limited for Lysaght but out-performance may be capped given weak investor sentiment to the construction sector and its supporting industries at this juncture.
- From its latest 2006 annual report, we note that there was no mention of any corporate social responsibility (CSR) activities undertaken by the group during the year.

Key Stock Statistics

FY Dec.	2007	2008E
Reported EPS (sen)	19.7	16.3
PER (x)	5.1	6.1
Dividend/Share (sen)	4.0	4.0
NTA/Share (MYR)	1.60	1.72
Book Value/Share (MYR)	1.60	1.73
No. of Outstanding Shares (mln)	41.6	
52-week Share Price Range (MYR)	0.95 - 1.30	
Major Shareholders:	%	
Chew Kar Heing and wife	55.2	
Liew Hoi Foo and wife	13.5	

* This is a Syariah-compliant stock

Per Share Data

FY Dec.	2005	2006	2007	2008E
Book Value (MYR)	1.34	1.45	1.60	1.73
Cash Flow (sen)	14.0	18.2	24.1	21.0
Reported Earnings (sen)	8.5	13.9	19.7	16.3
Dividend (sen)	3.0	4.0	4.0	4.0
Payout Ratio (%)	35.3	28.9	20.3	24.5
PER (x)	11.8	7.2	5.1	6.1
P/Cash Flow (x)	7.1	5.5	4.2	4.8
P/Book Value (x)	0.7	0.7	0.6	0.6
Dividend Yield (%)	3.0	4.0	4.0	4.0
ROE (%)	6.5	10.0	13.0	9.8
Net Gearing (%)	0.0	0.0	0.0	0.0

Lysaght Galvanized Steel

Recommendation: **HOLD**

Stock Code: 9199 | Bloomberg: LYSA MK | Price: MYR1.00 | 12-Month Target Price: MYR1.10 | Date: March 27, 2008

Background

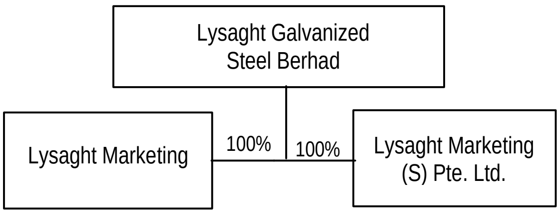
Corporate Profile

The Lysaght group has been manufacturing galvanized steel products in Malaysia since 1972. The group was listed on Second Board of Bursa Malaysia on June 28, 1994 under the name Lysaght Galvanized Steel Berhad.

The group was founded by Mr Chew Kar Heing who has been on Lysaght's board of directors since 1979. Mr Chew is currently a Non-Independent Non-Executive Director. He and his wife, Mdm Lim Lee Kuan, who also sits on Lysaght's board, are major shareholders of Lysaght with a total shareholding of 55.2%. The company is presently led by its' Managing Director, Mr Liew Hoi Foo who is also the son-in-law of Mr Chew and Mdm Lee. In total, the family has a 68.7% stake in Lysaght.

Lysaght's board of directors has nine members comprising the Managing Director, Executive Director, four Independent Non-Executive Directors and three Non-Independent Non-Executive Directors. The board composition meets the listing requirement set by Bursa Securities which requires at least two or one third of the board to be independent directors.

Corporate Structure



Source: Company data

Business

Lysaght is one of two domestic manufacturers of galvanized poles and masts. The other manufacturer is Galvapole Industries Sdn Bhd (Unlisted). While poles and masts are mainly used for highway lighting, they can also be applied to among others, telecommunication and power transmission industries.

Lysaght has the capability to manufacture poles and masts ranging from a height of 3 to 60 meters. It also produces a specialist range of architectural and decorative poles to complement its core range of products. One of the group's strong points is the advanced technology it applies to its products which ensure longer life expectancy, minimal maintenance combined with an attractive appearance for its products.

Poles are mainly used for streetlights and are between 3 to 12 meters in height. Meanwhile, masts are much larger in size and are mainly used to hold multiple lights at highway interchanges. Masts are usually between 20-60 meters in height. Other than to provide lighting to highways, air and sea port terminals, Lysaght's poles and masts can be utilised for outdoor floodlighting, recreational and stadium masts, flag poles and high voltage substation structures among its many uses.

Lysaght operates from three factories located in Tasek, Perak with a combined production capacity of 24,000 tonnes per annum. Management has no plans to increase capacity at this point. Revenue is mainly generated from the domestic market (70%) while Asean and East Asia markets make up 20% with the balance 10% derived from Middle East and India. The revenue breakdown between poles and masts are about 40%:60%.

Lysaght's main raw materials are steel [hot-rolled coils (HRC)] and zinc. HRC accounts for about 2/3 of cost of production while zinc accounts for the balance. The group purchases all its HRC requirements locally while it fully imports its zinc requirements. Due to the current volatility of its raw material prices, Lysaght places its order for the two commodities on a monthly basis and has kept stocks at a minimal level (approximately 2 months). Prices of HRC has risen significantly over the last 12 months (+35%) hence we continue to expect 2008 average HRC pricing be higher compared to 2007. Meanwhile, zinc prices have declined steadily from a high of US$4,515/mt in late-2006 to around US$2,500/mt currently. As such, average 2008 pricing is likely to be lower than the average pricing recorded in 2007. Going forward, zinc supply will likely outpace consumption and prices are expected to remain at current levels.

Earnings Outlook

Lysaght turned in a strong 2007 performance with revenue and net profit increasing by 25% and 42%, respectively. Despite higher domestic sales and exports, the group suffered from high raw material costs such as steel and zinc which squeezed 2007 gross profit margin to 23.1% from 26.6% in 2006. The group also provided for diminution in value for its zinc stock amounting to about MYR1.2 mln in 2007 but tightened cost controls over administration and marketing expenses as well as registering improvement in other income (mainly from sales of steel and zinc scrap). These controls had a positive impact on 2007 operating profit which grew 46% and operating margins which expanded to 13.5% from 11.5% in 2006. Lysaght has not yet announced its dividend payment for 2007 but we expect it to maintain its dividend payment at 4% tax exempt (yield of 4.1%) which will be announced at its Annual General Meeting.

As the bulk of Lysaght's products rely on infrastructure projects (such as highways, roads and housing development), we exercise caution on the visibility ahead after the unexpected general elections outcome which could result in a review and deferment in the implementation of some projects. Looking beyond Malaysia, we do not see exports making up for the potential slowdown in domestic projects as Malaysia still contributes the bulk of the revenue (70%). We are projecting a slight decline in revenue for 2008 for Lysaght (-7%) and a slight pick up in 2009 (+4.6%) when we expect most projects to begin rolling out.

In addition, we believe Lysaght may suffer from margin compression in 2008 given surging steel prices. Lower YoY average 2008 zinc pricing and an appreciating MYR against the US$ may help to stem the rise in HRC pricing. Global steel manufacturers and iron ore producers have reached an agreement for a 65% YoY increase in iron ore pricing, a major raw material component for steel production. As such, we expect average 2008 HRC pricing to be approximately 21% higher than that registered in 2007. Meanwhile, our assumption on zinc calls for prices to remain at around the US$2,500/mt levels, a decline from 2007's average of US$3,248/mt.

Although Lysaght may be able to pass on the bulk of its rising costs, we remain cautious over how much and how quickly these costs can be passed through. Given this uncertainty, we are assuming a squeeze in 2008 operating margins to 12% from 13.5% in 2007 and a decline in net profit to MYR6.8 mln (-17.3% YoY). We expect margins to bounce back towards 13.5% in 2009 on expectation of stability in commodity prices and further appreciation of the MYR against US$. This will result in 2009 net profit increasing to MYR8.1 mln (+19.8% YoY).

Valuation

As Lysaght does not have a directly comparable listed peer, we have based our valuation on the group to our target PER for small to mid-sized contractors within our coverage, which ranges between 10x-12x.

Our target PER multiple of 6.5x stands at a 35% discount to the lower end of our PER range for small- to mid-sized contractors. The discount reflects Lysaght's relatively small market capitalization, thinly traded volumes and the current weak investor sentiment toward the construction sector and its supporting industries. Our target multiple is also below the group's historical average trading PER of 7.5x. After adding our estimated 2007 tax-exempt DPS of 4 sen, we arrive at a 12-month target price of MYR1.10 for Lysaght.

Profit & Loss

FY Dec. / MYR mln	2006	2007	2008E	2009E
Reported Revenue	66.6	82.9	75.5	78.9
Reported Operating Profit	7.6	11.2	9.1	10.6
Depreciation & Amortization	-1.8	-1.8	-1.9	-1.8
Net Interest Income / (Expense)	0.0	0.0	0.0	0.0
Reported Pre-tax Profit	7.7	11.2	9.2	10.8
Effective Tax Rate (%)	25.3	26.5	26.0	25.0
Reported Net Profit	5.8	8.2	6.8	8.1
Reported Operating Margin (%)	11.5	13.5	12.0	13.5
Reported Pre-tax Margin (%)	11.6	13.5	12.2	13.7
Reported Net Margin (%)	8.7	9.9	9.0	10.3

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 and Standard & Poor's AB (Sweden); Standard & Poor's Equity Research Services Asia includes Standard & Poor's LLC's offices in Hong Kong, Singapore and Tokyo, 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.

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 Japan by Standard & Poor's LLC, which is regulated by the Kanto Financial Bureau; in Sweden by Standard & Poor's AB ("S&P AB"), 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&P AB, S&PM, SPIS and SPIAS LLC (Korea) 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.

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 by S&P LLC-Japan and in the case of inconsistencies between the English and Japanese version of a report, the English version prevails. Neither S&P LLC nor S&P guarantees 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 Malaysia. All queries in relation to this report should be referred to Alexander Chia, Desmond Ch'ng or Ching Wah Tam.

Recommendation and Target Price History

Date	Recommendation	Target Price
New	Hold	1.10