

Date: 16 May 2007

<b>Eastern Pacific Industrial Corporation Berhad (EPIC)</b>		<b>Price:</b>	RM2.16
<i>Transformation Plans Taking Shape</i>		<b>Market Capitalisation:</b>	RM365.5m
		<b>Board:</b>	Main Board
		<b>Sector:</b>	Trading & Services
<b>Stock Code:</b>	8265	<b>Recommendation:</b>	<b>BUY</b>

(latest figures)

<u>Key Stock Statistics</u>	2006	2007F
EPS (sen)	4.8	19.7
Core EPS (sen)	18.8	19.7
Core P/E (x)	11.5	10.9
Dividend/Share (sen)	9.4	9.9
NTA/Share (RM)	1.44	1.54
Book Value/Share	1.44	1.54
Issued Capital (mil shares)	165.0	
52-weeks Share Price Range	1.13-2.50	
<u>Major Shareholders:</u>		
Perbadanan Memajukan Iktisad Negeri Terengganu (PMINT)	44.0	
Lembaga Tabung Haji	20.8	

Share Price Chart



<u>Per Share Data</u>	2005	2006	2007F	2008F
Book Value (RM)	1.49	1.44	1.54	1.65
Cash Flow (sen)	5.7	6.4	23.6	28.2
EPS (sen)	1.3	4.8	19.7	21.8
Core EPS (sen)	12.0	18.8	19.7	21.8
Dividend (sen)	17.5	9.4	9.9	10.9
Payout Ratio (%)	1,306.8	50.0	50.0	50.0
PER (x)	161.3	44.9	10.9	9.9
Core PER (x)	18.1	11.5	10.9	9.9
P/Cash Flow (x)	37.3	33.7	9.1	7.7
P/Book Value (x)	1.4	1.5	1.4	1.3
Dividend Yield (%)	8.1	4.3	4.6	5.1
ROE (%)	8.0	13.0	12.8	13.2
Net Gearing (%)	net cash	net cash	net cash	net cash

<u>P&amp;L Analysis (RM mil)</u>	2005	2006	2007F	2008F
Year-end: Dec				
Revenue	84.3	112.2	135.4	146.5
EBITDA	31.1	46.4	54.2	59.9
Depreciation	(7.1)	(7.9)	(8.6)	(9.4)
Interest Expenses	1.0	2.0	3.0	4.0
Pre-tax Profit	13.7	18.5	48.7	53.6
Effective Tax Rate (%)	82.7	51.6	27.0	26.0
Net Profit	2.2	7.9	32.6	36.1
Core Net Profit	19.7	31.0	32.6	36.1
EBITDA Margin (%)	36.9	41.3	40.1	40.9
Pre-tax Margin (%)	16.3	16.5	36.0	36.6
Net-Margin (%)	2.6	7.1	24.1	24.6

**1. Highlights:**

**Transformation.** We met with management of EPIC yesterday and talked about the company's transformation plans from an oil and gas supply base owner-operator into something more substantial while remaining focused on the industry.

- **Fabrication** – The company is looking at developing expertise in platform fabrication, initially with plans to acquire a minor Petronas-licensed fabricator, and longer-term to become a major fabricator joining the select group of seven Petronas licencees currently. 60 acres of land has been identified within the Kemaman Supply Base for the fabrication yard.
- **Ship repair and maintenance** – Land 5km away from KSB has also been identified for ship repair and maintenance.
- **East Wharf** – A general purpose wharf catering mainly to its largest customer Perwaja Steel. There are plans at a later stage to expand the terminal although this will depend on securing more non-oil and gas customers and traffic to the port.
- **Liquid Chemical Berth** – KPK has already begun plans to upgrade and expand the LCB at a cost of RM35m to handle 150,000 DWT vessels and increase the capacity to 2.6m tones p.a. by March 2008. This is crucial as a newly-completed bitumen plant next door (owned by Seloga Holdings and Thai partners) will process heavy crude from Venezuela, transported in 150,000 DWT oil tankers. Temporarily, crude is being off-loaded at West Wharf, but this will shift to LCB after the expansion.

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- **Manufacturing** – The manufacturing zone under the East Coast Corridor initiative has been designated within an area from Pahang (extended down to Mersing) and up to Paka in Terengganu. While the products have not been confirmed, management believes the focus will be on petrochemical-related industries such as plastics. EPIC is looking at areas in which it may be involved but there are no firm plans as yet.
  - **Overseas supply base** – EPIC will be submitting its technical proposal for a new oil and gas supply base in Cambodia on 21 May. Plans are to be an equity partner with the National Cambodia Petroleum Authority (NCPA), as well as operator.

**Accretion.** FY07 earnings growth will likely come from full-year contribution from Kemaman Port (East Wharf and Liquid Chemical Berth). In FY08-09, the expansion and upgrading of existing facilities at KSB and Kemaman Port will also be earnings-accretive. We further estimate the acquisition of the minor fab will initially add around 5% to FY08 earnings. The additional profit may be small in the early stages but we see net profit accelerating in FY08-09, with forecast EPS growth of 11% and 13% respectively. The company has conservatively forecast EPS CAGR of 14% for FY07-10, but we believe this does not fully reflect the new businesses to be introduced under the East Coast Corridor initiative or the plans to replicate the supply base model overseas.

## **2. Recommendation:**

**Delivery.** Given EPIC's lack of expertise in other oil and gas businesses, execution risk will be a key concern. We note that management remains conservative, preferring to downplay earnings expectations for new ventures. We are more optimistic, given the company's long-standing business with Petronas.

**1Q07 results preview.** In the 1Q07 results to be announced on 17 May, we expect 1Q07 net profit of RM7.5m (+34% yoy) or 23% of our full-year forecast of RM32.6m. We believe our FY07 forecast is achievable.

**Undervalued.** Fundamentally, the stock remains undervalued trading at 36% discount to peers weighted average. To factor in liquidity, we have assumed 10% discount, which implies a fair value of RM3.12/share at 15x one-year forward EPS. We thus maintain our **BUY** call on the stock.

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**Outperform** = The stock return is expected to exceed the KLCI benchmark by greater than five percentage points over the next 6-12 months.

**Trading Buy** = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

**Market Perform** = The stock return is expected to be in line with the KLCI benchmark (+/- five percentage points) over the next 6-12 months.

**Underperform** = The stock return is expected to underperform the KLCI benchmark by more than five percentage points over the next 6-12 months.

### **Industry/Sector Ratings**

**Overweight** = Industry expected to outperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

**Neutral** = Industry expected to perform in line with the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

**Underweight** = Industry expected to underperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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