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Oil & Gas

Key notes from the 12th Asia Oil & Gas Conference: 'The shared future'

OVERWEIGHT

- Global energy demand is expected to remain robust but long term sustainability could be a key issue due to exhaustion of hydrocarbons.
- Alternative energy; i.e. nuclear may be a solution. Elsewhere, escalating costs and skill shortage will remain an issue to the sector, at least in the near-to-mid term in the era of high oil prices.
- Nevertheless, we remain Overweight on the Oil & Gas sector, in anticipation of a greater push for E&P activities, leading to greater demand for supplies and services. Maintain Strong Buy recommendations on Ramunia and KNM, and Buys calls on Petronas Gas, EPIC, Dialog, Wah Seong, Petra Perdana, and Alam Maritim.

Growing energy demand. The key takeaways from the recently concluded 12th Asia Oil & Gas Conference are as follows: (i) Global energy demand is expected to remain robust over the next few years, underpinned by rapid economic growth in Asia (i.e. China, India & Middle East); (ii) Oil consumption is expected to grow by a CAGR of 1.6% from 2007-2030 to 120m bpd, creating a new requirement of c.30m bpd; (iii) Global energy demand growth outlook (CAGR from 2007-2030) - oil: +1.6%; gas: +2.3%; coal: +1.5%; others: +0.8% and nuclear: +0.4%.

Sustainable energy security may be an issue. However, there is an overriding concern on sustainable energy security, as demand growth may not be matched by supply due to continuous depletion in resources and low replacement in new reserves/discoveries over consumption. This could have to adverse impacts – tight market environment, economic disruption, possibilities of extreme political reactions, just to name a few.

Maintain Overweight. Despite the many challenges faced by the industry as a whole, we remain Overweight on the Oil & Gas sector. We continue to believe that there will be a greater push for E&P activities, leading to greater demand for supplies and services.

Sector Summary Table

Company	Rec	Price (RM)	TP (RM)	EPS (sen)		EPS Grth (%)		PE (x)		DPS (sen)		Yield (%)		PBV
				07F	08F	07F	08F	07F	08F	07F	08F	07F	08F	
Alam Maritim	Buy	4.20	4.65	26.7	33.2	39.3	24.1	15.7	12.7	1.5	1.5	0.4	0.4	3.2
Dialog	Buy	1.81	2.35	5.6	7.5	45.6	35.3	32.5	32.5	3.9	5.2	2.1	2.9	8.0
EPIC	Buy	2.38	2.60	19.5	21.6	11.7	10.6	12.2	11.0	7.5	8.5	3.2	3.6	1.5
Kencana	N.R	1.75	N.R	8.7	10.9	47.4	24.9	20.1	16.1	0.0	0.0	0.0	0.0	6.4
KNM	Str Buy	14.10	17.00	66.7	114.1	52.4	71.2	21.1	12.4	10.1	15.4	0.7	1.1	6.6
MISC	Buy	9.80	11.00	69.2	74.1	6.6	7.0	14.2	13.2	30.0	30.0	3.1	3.1	1.8
Petra Perdana	Buy	3.92	4.00	26.9	34.1	51.2	32.8	14.6	11.5	1.0	1.0	0.3	0.3	2.7
P Gas	Buy	9.70	11.20	62.1	62.9	0.1	1.2	15.6	15.4	46.0	47.0	4.7	4.8	2.4
Ramunia	Str Buy	1.60	1.80	11.7	15.6	110.6	33.4	13.7	10.2	0.0	0.0	0.0	0.0	1.1
Shell	FV	10.40	9.10	65.1	62.4	-17.8	-4.3	16.0	16.7	50.0	50.0	4.8	4.8	1.6
Tj. Offshore	Buy	2.77	4.00	14.6	22.0	35.0	50.7	19.0	12.6	3.9	4.4	1.4	1.6	2.9
Wah Seong	Buy	3.66	4.10	15.3	18.9	50.9	23.6	24.0	19.4	9.0	11.0	2.5	3.0	3.4

Source: Aseambankers

Alternative energy. Although oil & gas will continue to be the main energy source, these finite resources are not adequate to complement growing demand. As such, there will be a more significant substitution to other forms of energy to meet demand.

- (i) **Nuclear as an alternative.** To compensate for the shortfall in energy requirements, more and more countries are re-considering using nuclear energy as an alternative fuel. Nuclear energy is the only green house gas emitting power source that can effectively replace fossil fuels and satisfy global demand. Nuclear price is competitive vis-à-vis gas price at US\$5-6/mmBtu. Nuclear power is less competitive compared with coal but CO² concerns/penalties can help close the gap.
- (ii) **Bio fuels; an emerging alternative but inadequate.** Bio-diesel is an emerging alternative fuel. Biofuel plants are relatively small, inexpensive and can be brought on stream fairly quickly. World biofuel production was at 750k bpd in 2006, with Brazil and USA dominating the market, at 300k bpd and 320k bpd respectively. Meanwhile, the European Union's biodiesel production was at 90k bpd. Biofuel is an interesting alternative source of energy, but it is expected to have a limited impact. The volume of energy that can be potentially supplied is limited (c. 1.4-1.6m bpd by 2010), and may face struggling issues on cyclical profitability on rising feedstock costs, de-forestation and carbon footprints.
- (iii) **Canadian oil sands and Venezuela's heavy oil.** These are expected to contribute between 150-200k barrels per day (bpd) of new oil supply to the market but contributions are limited.

Escalating Costs. Meanwhile, exploration & production (E&P) companies are living in a rising cost environment in response to the high energy prices. As a consequence, equipment is becoming more expensive with longer delivery periods, and fabrication yards are reaching capacity. Many projects have been cancelled or delayed, and there is an acute shortage in personnel – these are just some of the key concerns. According to the IHS 2007 press release, offshore rigs and offshore marine vessels led the charge, increasing by 309% and 41% YoY. This is followed by engineering and project management (+23%), yard fabrication (+22%), equipment (+17%) and steel (+4%).

Skills Shortage. The mismatch of human capital in the O&G sector is a big concern. Demand for skilled personnel (i.e. graduates in geo-science and petroleum engineering disciplines) has exceeded supply. According to Schlumberger, this could be addressed/overcome by investing in conventional and unconventional training, and transferring the knowledge of experienced employees nearing retirement age to younger counterparts via training. However, such benefits are lacking in Asian companies.

Technology. Oil majors have not been investing in technology, or research & development (R&D) spending.

Our Strong Buys for the O&G sector are: Ramunia (RH MK; TP: RM1.80) and KNM Group (KNMG MK; TP: RM17.00). We also have Buy calls on Petronas Gas (PTG MK; TP: RM11.20), EPIC (EPIC MK; TP: RMRM2.60), Dialog (DLG: RM2.35), Wah Seong (WSC MK; TP: RM4.10), Petra Perdana (PETR MK; TP: RM4.10), and Alam Maritim (AMRB MK; RM4.65).

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EBIT = Earnings Before Interest And Tax	P = Price	WACC = Weighted Average Cost Of Capital
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13 June 2007

Description: Diversified food and agro-based player with a stellar track record of unbroken annual profit growth since listing in 2001.

Catalyst: Continuous >20% net profit growth and likely overseas expansion.

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QL Resources

Buy

(unchanged)

Primed for re-rating

TP: RM4.15

Current Price: RM3.22

- We are raising our TP for QL Resources to RM4.15 based on 12x CY08 PE (from RM3.80 on 10x CY08 PE), as we foresee its planned growth activities finally catching the market's attention.
- Our current estimate of an 18% EPS growth for each of CY07 and CY08 is well-founded, while the seeds of similar growth through to CY11 are already well advanced.
- Maintain Buy as QL chugs along towards the RM1b market cap mark and may well emerge as a KLCI constituent by end CY08.

Undemanding valuations. With continuous strong growth and its dominant position in agro-based activities, we expect QL to start trading back to the 12x forward PE range soon. With calendarised EPS growth rates closer to the 20% mark expected for the next four to five years, this implies a doubling of QL's EPS and thus gross dividends over a five-year holding period.

Better earnings clarity. We believe that QL is well-placed to achieve our expectations for 18% net profit growth for CY07 and CY08 respectively. We see its deep-sea fishing fleet growing from the current 14 to 20 vessels by end-CY07 and do not rule out further investments in CY08. Similarly, at QL's layer farming activities, we expect its Kuching farm to be fully converted to a closed-house system in the next two quarters, raising output from that farm by another 40-50% annually. This should raise total egg production growth for CY07 and CY08 into the double-digit territory again.

Stellar earnings track record continues. QL's growth strategy should translate into the continuation of its unbroken earnings growth record since listing in 2001, and its inching towards the RM1b market capitalisation mark by 2008 or 2009 in our estimation. It would also be reasonable to subscribe that with its high level of corporate governance, active social responsibility record and admirable growth story, QL may well be included as a KLCI constituent sooner rather than later. Maintain **Buy** with a raised RM4.15 TP based on 12x CY08 PE.

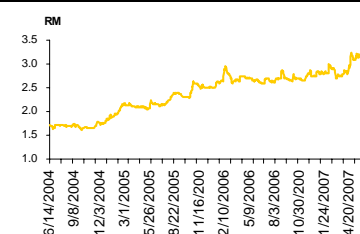
Stock Information:

Ticker:	QLG MK
Closing Price:	RM3.22
KLCI:	1360.58
Sector:	Consumer
Shares Issued (m):	220.0
Market Cap (RM m):	708.4
3-mth Avg Daily Volume (m):	0.4

Major Shareholders:

	%
CBG Holdings	44.5
Farsathy Holdings	12.8

Price Chart (RM3.22)



QL Resources – Summary Earnings Table

FYF Mar (RM m)	FY05A	FY06A	FY07A	FY08F	FY09F
Turnover	941.6	1,010.5	1,118.5	1,254.5	1,388.3
EBITDA	71.5	89.7	112.3	133.0	157.7
Pretax profit	46.1	59.1	76.2	90.1	106.1
Net profit - Ex EI	36.1	48.3	62.4	73.5	86.6
EPS - Ex EI (sen)	24.1	23.9	28.3	33.4	39.4
EPS growth (%)	7.7	(0.8)	18.4	17.9	17.8
DPS (sen)	7.5	9.0	10.0	11.0	12.0
PER (x)	13.3	13.5	11.4	9.6	8.2
P/BV (x)	2.8	2.7	2.0	1.8	1.5
Div. Yield (%)	2.3	2.8	3.1	3.4	3.7
EV / EBITDA (x)	9.5	9.8	7.6	6.3	5.2
ROE (%)	20.6	17.9	17.8	18.3	17.8
Gearing (x)	1.3	0.8	0.6	0.5	0.3
Consensus net profit (RM m)	n.a.	n.a.	n.a.	70.0	78.5
Revision (%)	n.a.	n.a.	n.a.	-	-

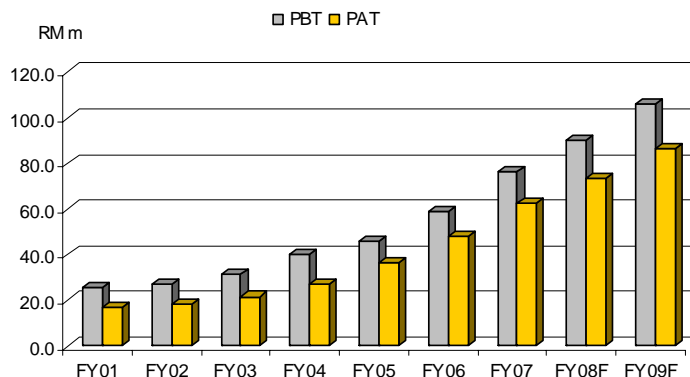
Source: Aseambankers

Price Performance:

52-week High/Low RM3.36/RM2.57

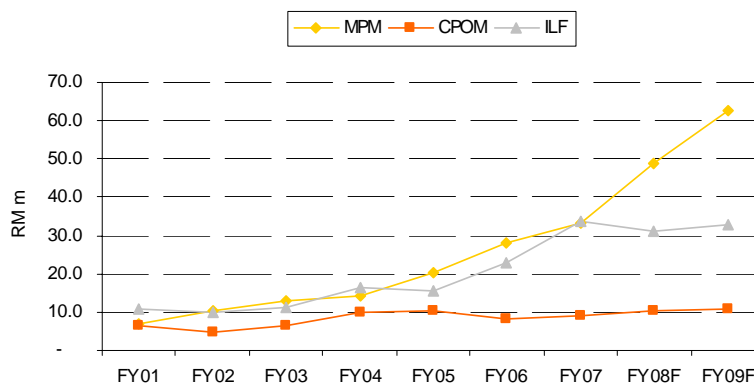
1-mth	3-mth	6-mth	1-yr	YTD
(2.1)	(2.1)	4.5	4.1	(2.1)

QL Resources: PBT and PAT trend FY01 to FY09F



Source: Aseambankers

QL Resources: PBT contribution by segment



Source: Aseambankers

QL Resources: P&L Summary

YE 31 Mar	FY05	FY06	FY07	FY08F	FY09F
Turnover	941.6	1,010.5	1,118.5	1,254.5	1,388.3
<i>Marine-based</i>	130.0	190.6	245.4	336.7	419.9
<i>Integrated Livestock</i>	603.4	620.3	656.5	689.3	727.2
<i>Palm oil</i>	208.2	199.7	216.6	228.5	241.1
EBITDA	71.5	89.7	112.3	133.0	157.7
Net interest expense	(8.9)	(11.0)	(11.8)	(18.1)	(24.1)
Depreciation and amort.	(16.8)	(20.3)	(24.7)	(25.1)	(27.7)
Pretax profit	46.0	59.1	76.2	90.1	106.1
<i>Marine-based</i>	20.2	27.3	33.5	48.8	62.6
<i>Integrated Livestock</i>	15.7	24.1	33.5	31.0	32.7
<i>Palm oil</i>	10.2	7.7	9.3	10.3	10.9
Taxation	(7.9)	(7.7)	(8.5)	(10.3)	(12.1)
Minorities	(2.1)	(3.1)	(5.3)	(6.3)	(7.4)
Net profit	36.2	48.3	62.4	73.5	86.6
EBITDA margin (%)	7.6	8.9	10.0	10.6	11.4
Turnover growth (%)	4.7	7.3	10.7	12.2	10.7
Pretax profit growth (%)	14.6	28.5	29.0	18.2	17.8
Net profit growth (%)	34.6	33.6	29.0	17.9	17.8
Effective tax (%)	17.2	13.0	11.2	11.4	11.4

Source: Company, Aseambankers

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13 June 2007

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Water

Overweight (unchanged)

Of the Pahang-S'gor project, SPAN and PAAB

- **Key take-aways from yesterday's Malaysia PFI Conference reaffirm our positive outlook for the water sector, especially for the long term.**
- **The Pahang-Selangor water transfer project would be implemented in 2H07, and this should positively impact the local construction boys – Gamuda, IJM Corp, UEM Builders, Loh & Loh, Salcon and Taliworks.**
- **Water related assets in Negeri Sembilan would also be taken over by PAAB – Ranhill Utilities could benefit.**

Things are moving in the water sector! Key take-aways from yesterday's Malaysia PFI (Private Finance Initiative) Conference reaffirm our positive outlook for the water sector, especially for the long term. Developments and discussions relating to the water sector were led by Mr Teo Yen Hwa, Chief Executive Officer of Suruhanjaya Perkhidmatan Air Negara.

- **On the Pahang-Selangor water transfer project** – the project would be implemented in 2H07, mainly to be funded by a loan from the Japan Bank of International Cooperation (JBIC).
- **On Pengurusan Aset Air Bhd (PAAB)** – PAAB is now finalising the take-over of water related assets in Negeri Sembilan from the State Government. This would be the showcase for PAAB in its role as the national water asset management company under the Ministry of Finance.

PAAB is also finalising discussions with the Melaka State for the transfer of the State's water assets to the Federal level.

- **On Suruhanjaya Perkhidmatan Air Negara (SPAN)** – since its commissioning on 1 Mar 2007 with skeletal staff force, SPAN has been busy recruiting employees.

We understand from industry sources that SPAN has also met up with the water concessionaires on a number of occasions relating to the migration to a new regulatory regime. Existing concessionaires would have to decide whether they will continue with their concessions, or surrender all water assets and liabilities to the Government, in return for an operating licence.

Consistent with our expectations. We highlighted in our *Water Sector* piece in April 2007, the government's plans for an international tender for the 44.6 km tunnel works relating to the Pahang-Selangor water project, to be called within these few months and for construction works to start in early-2008.

This would lead to the roll-out of the other main packages of the project, which we estimate would cost at least RM9b in total. The timeline for project roll-out revealed yesterday is consistent with our expectations.

Peer Valuation Table

Stock	Rec	Price	TP	EPS (sen)			EPS (growth)		PE (x)			DPS (sen)		Yld (%)	
				FY06	FY07	FY08	FY07	FY08	FY06	FY07	FY08	FY07	FY08	FY07	FY08
Gamuda	Buy	8.75	8.50	22.3	23.4	40.3	5.1	72.1	39.3	37.4	21.7	46.0	50.0	5.3	5.7
IJM Corp	Hold	8.25	8.25	34.0	38.0	34.3	11.7	(9.7)	24.2	21.7	24.1	15.0	15.0	1.8	1.8
Loh & Loh	Buy	2.70	3.50	13.0	19.5	24.6	49.6	26.5	20.8	13.9	11.0	8.0	8.0	3.0	3.0
YLI Hldgs	Buy	3.12	3.50	13.1	14.2	17.6	8.4	23.9	23.8	22.0	17.7	7.0	7.0	2.2	2.2

Source: Aseambankers

Potential beneficiaries. Potential beneficiaries for construction works for the Pahang-Selangor water transfer project are Gamuda (**GAM MK; Hold; TP: RM8.50**), IJM Corp (**IJM MK; Hold; TP: RM8.25**), UEM Builders (**UEMB MK; Not Rated**) and Kumpulan Perangsang Selangor (**KUPS MK, Not Rated**), while the smaller boys like Loh & Loh (**LLHL MK; Buy; TP: RM3.50**), Salcon (**SALC MK; Not Rated**) and Taliworks (**CI MK; Not Rated**) could feature at the sub-contracting levels.

That PAAB is actively involved in discussions to take-over water related assets in the two states of Negeri Sembilan and Melaka, is also positive development. Here, we understand that **Ranhill Utilities (RANU MK, Not Rated)** is vying a role in the operation and maintenance of water treatment plants in Melaka.

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EV = Enterprise Value	PBT = Profit Before Tax	

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