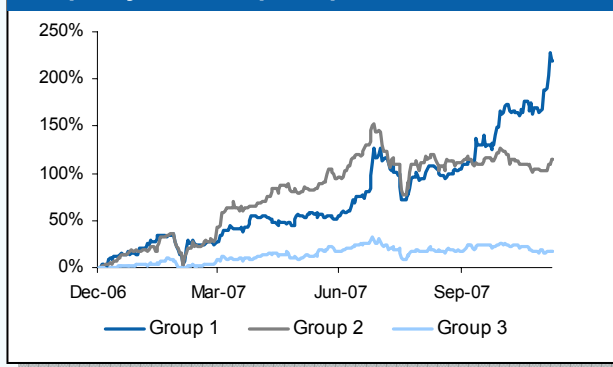


10 December 2007

Putting things into perspective

Disparity in share price performance YTD



Source: Bloomberg

Contrast between Buys, Adds and Reduces

Basket	PER	CAGR	PEG	P/B	ROE	ROE/PBV	Yield
Buys	12.2	27.5	0.4	2.3	20.2	8.7	2.9
Adds	19.1	51.8	0.4	6.3	38.0	6.0	0.6
Reduces	23.3	42.4	0.5	4.6	21.6	4.8	1.6

Source: Bloomberg, KAF

Summary of stock recommendations

Buy	Add	Reduce
APB Resources	KNM Group	Dialog Group
Petra Perdana	Alam Maritim	Kencana Petroleum
Muhibbah Engineering		Wah Seong Corporation
Shell Refining Company		
Scomi Group		
Tanjung Offshore		

Source: KAF

- The Oil & Gas industry has been one of the best performing sectors this year up 100% YTD. However, this out-performance has not been broad-based.
- While structural growth over the medium term is clear and the general outlook has improved, we believe there are opportunities to capitalise on valuation disparities and the differing extents to which these good prospects have been captured in the respective companies. **Switch.**

- Our list of six Buys trades at 12.2x 2008 PER, 0.4x PEG, has an ROE/PBV ratio of 8.7x and offers 2.9% dividend yield.
- This compares favourably to our basket of three Reduces which trades at a much higher 23.3x PER and 0.5x PEG with lower ROE/PBV of 4.8x and dividend yield of 1.6%.

- Our sector top pick is Petra Perdana.
- We also like APB, Muhibbah, Shell, Scomi, Tanjung Offshore and Alam Maritim.
- We added RM1.50 to our target price for KNM to reflect upside from M&A. However, we downgrade the stock from Buy to Add following the recent surge in share price.
- Reduce Dialog, Kencana and Wah Seong as high expectations have been built into share prices whilst potential for earnings disappointments are not factored in.

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PUTTING THINGS INTO PERSPECTIVE

The Malaysian Oil & Gas industry has been one of the best performing sectors this year (up a meteoric 100% year-to-date versus the broader market's 31%) driven by record high oil prices inducing a speed-up in capital expenditure, amongst other factors. However, this out-performance has not been broad-based across all companies. While structural growth over the medium term is clear and the general outlook has improved, we believe there are opportunities to capitalise on disparities in current valuations and the differing extents to which these good prospects have been captured in the respective companies.

Our top pick for the sector is Petra Perdana. We also reiterate our Buy calls on APB Resources and Shell Refining Company. Dialog Group remains a Reduce, purely on the back of its steep valuations.

We have upgraded Scomi Group from a Reduce to a Buy after revising earnings upwards by an average of 26% over 2007-2009.

For KNM, we have increased our sustainable ROE variable by 9 percentage points to capture the potential value add from possible M&A adding RM1.50 to our target price. Yet, we downgrade our long-standing Buy recommendation to Add on account of the further surge in share price over the past month. Wah Seong moves from an Add to a Reduce as the stock now provides some downside to our unchanged target price.

In this report, we also initiate coverage on four new companies, namely Alam Maritim Resources (Add), Kencana Petroleum (Reduce), Muhibbah Engineering (M) (Buy), and Tanjung Offshore (Buy) (company-specific information on pages 13-24).

Table 1: Summary of stock recommendations

Company	Mkt cap (RM m)	Rec.	Current price (RM)	Target price (RM)	Upside (%)
APB Resources	145	Buy	1.64	2.85	74
Petra Perdana	1,475	Buy	5.45	7.30	34
Muhibbah Engineering	1,351	Buy	3.52	4.60	31
Shell Refining Company	3,360	Buy	11.20	14.00	25
Scomi Group	1,446	Buy	1.42	1.75	23
Tanjung Offshore	583	Buy	2.88	3.30	15
KNM Group	7,797	Add	7.45	8.50	14
Alam Maritim	1,147	Add	2.52	2.85	13
Wah Seong Corporation	1,717	Reduce	4.00	3.80	(5)
Kencana Petroleum	2,220	Reduce	2.49	2.30	(8)
Dialog Group	2,544	Reduce	1.80	1.50	(17)

Source: Bloomberg, KAF

Our list of six Buys trades at 12.2x 2008 PER, 0.4x PEG, has an ROE/PBV ratio of 8.7x and offers 2.9% dividend yield. This compares favourably to our basket of three Reduces which trades at a much higher 23.3x PER and 0.5x PEG with lower ROE/PBV of 4.8x and dividend yield of 1.6%.

Table 2: Contrast between Buys, Adds and Reduces

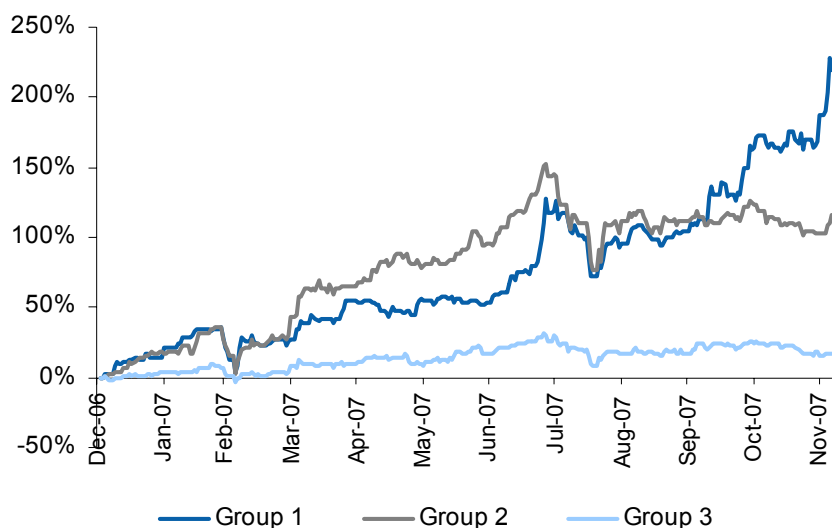
Basket	PER	CAGR	PEG	P/B	ROE	ROE/PBV	Yield
Buys	12.2	27.5	0.4	2.3	20.2	8.7	2.9
Adds	19.1	51.8	0.4	6.3	38.0	6.0	0.6
Reduces	23.3	42.4	0.5	4.6	21.6	4.8	1.6

Source: Bloomberg, KAF

A FUNCTION OF PRICE

Overall, the Malaysian Oil Services companies have done extremely well compared to a year ago. Nevertheless, there has been a performance disparity over the past 1-6 months. These historical share price movements can be split into the following categories:

Chart 1: Disparity in share price performance year-to-date



Source: Bloomberg

Group 1: Consistent out-performers – Notable stocks which have consistently outshone are Alam Maritim and KNM Group.

- Given strong expected earnings growth at Alam Maritim over the next few years, we do not think that further share price increases are unreasonable as valuations do not appear stretched yet.
- While KNM's performance has been well deserved for the excellent track record that it boasts, we think that high growth expectations have been factored in to a large extent whilst there could be potential earnings disappointments in the future, coming off a high base. With that said, further out-performance in the near term is possible on the back of potential M&A.

Group 2: Over past 12-months, strong performance initially but poor thereafter – Stocks that fall into this category are Dialog Group, Kencana Petroleum, Muhibbah Engineering, Petra Perdana and Wah Seong Corporation.

- Dialog experienced an incredible run-up between Dec-06 and Apr-07 but underperformed considerably over the past month, quarter and six-months. We believe that this correction marks the start of some doubts on the deliverability of the huge expectations factored in at that time. Full year net profit fell short of our expectations by 15% for FY07 (June), and our forecasts were even below consensus.
- Kencana did well soon after its listing at the end of last year, but has underperformed over the last four months. Here, we feel that the share price could have run ahead of expectations whilst a sustainable track record still remains to be proven. In fact, earnings in the most recent quarter to July were down by 38% sequentially.
- Muhibbah has been the biggest out-performer over the past year. We think this is a function of growing interest in the company where previously it was under-researched. However, the stock has not done much over the past four months and we believe this provides an opportunity to accumulate.
- Petra Perdana did well over a six to 12-month horizon but has underperformed recently. We believe it has the potential to continue doing well given plenty of room

for an expansion in valuations as the market increasingly recognises the quality exposure it provides into the marine and brown-field segments of the industry.

- Wah Seong's share price performance, in our opinion, was a play on anticipation of potential mega projects being announced earlier this year. We believe the stock was sidelined by investors more recently due to the cooler news flow stream. Nonetheless, we do not dispute that heated news flow on these projects may materialise again next year but think that valuations are on the high side.

Group 3: Total laggards – APB Resources, Scomi Group, Shell Refining Company and Tanjung Offshore are laggards in the sector.

- Although APB's much-awaited capacity expansion continues to get delayed, we think that this setback has been more than priced in whilst the company has not even been rewarded for doubling its earnings last year. Also, entry at this level is very cheap and the stock could see a sharp re-rating upon conclusion of an expansion plan.
- Scomi's consistent underperformance in the past is justified, we think, given the issue of over-promises and under-delivery which used to plague the group. Nonetheless, quarterly earnings this year have improved tremendously and should transform investor sentiment in the process. Normalised net profit for the nine-month period to September was up 41% on the back of a 30% rise in revenue.
- Shell's share price has done poorly for the longest time despite great earnings driven by high refining margins and soaring oil prices. We maintain that this is unjustified and urge investors to accumulate on a cash generative business backed by great yields of around 8%.
- Tanjung Offshore has not really participated in the general appreciation experienced by other industry players this year. This is an opportunity to accumulate seeing that the company has delivered on earnings and is set for good growth going forward. For the nine-months to September, net profit grew by 34% and seems on track to meet our 37% growth forecast for the full year.

Table 3: Disparity in share price performance

Company	Absolute Performance				Relative Performance			
	1 mth	3 mth	6 mth	12 mth	1 mth	3 mth	6 mth	12 mth
Alam Maritim	(3)	47	66	131	(4)	34	58	77
APB Resources	(8)	(11)	(11)	20	(9)	(19)	(16)	(8)
Dialog Group	6	(4)	1	125	4	(13)	(4)	72
Kencana Petroleum	(4)	(2)	41	nm	(5)	(11)	35	nm
KNM Group	25	54	110	229	23	40	100	152
Muhibbah Engineering	(4)	(4)	31	231	(6)	(12)	25	153
Petra Perdana	1	9	38	103	(0)	(0)	32	56
Scomi Group	(13)	(9)	1	35	(15)	(17)	(3)	4
Shell Refining Company	(3)	4	7	7	(4)	(6)	1	(18)
Tanjung Offshore	(4)	(6)	1	39	(5)	(14)	(4)	7
Wah Seong Corporation	8	3	13	88	7	(7)	8	44

Source: Bloomberg

CROSS-SECTOR COMPARATIVES

In this section, we compare all 11 companies based on various operational and valuation criteria to see how each one measures up. Going with the assumption that all these companies should benefit from current buoyant industry conditions, we think that picking and choosing from the lot should to some extent depend on the relative standing of each based on the chosen operational and valuation metrics. In addition, due recognition, of course, needs to be given to those companies that have consistently delivered while a discount needs to be applied to those that have disappointed.

Table 4: Operational comparative

Operational Comparative	Mkt Cap (RM m)	Rec.	2008 (%) (annualised)					
			CAGR	ROE	ROIC	Net gearing	Net margin	FCF margin
Alam Maritim	1,147	Add	47	29	18	133	24	(2)
APB Resources	145	Buy	34	19	24	(8)	11	9
Dialog Group	2,544	Reduce	33	23	16	136	10	8
Kencana Petroleum	2,220	Reduce	52	23	38	(37)	7	2
KNM Group	7,797	Add	57	47	45	3	17	5
Muhibbah Engineering	1,351	Buy	31	24	19	55	4	(3)
Petra Perdana	1,475	Buy	37	25	20	34	15	7
Scomi Group	1,446	Buy	17	16	12	68	6	1
Shell Refining Company	3,360	Buy	(3)	12	13	(2)	3	4
Tanjung Offshore	583	Buy	48	26	13	183	6	(9)
Wah Seong Corporation	1,717	Reduce	42	19	15	68	5	(4)
Simple Average			36	24	21	57	10	2
Simple Average ex-Shell			40	25	22	63	11	1

Note: CAGR between CY07 and CY09

Source: Bloomberg, KAF

Table 5: Valuation comparative

Valuation Comparative	Price (RM)	Target (RM)	2008 (x) (annualised)					
			PER	PEG	P/BV	ROE/PBV	EV/EBITDA	Yield (%)
Alam Maritim	2.52	2.85	16.3	0.3	4.1	5.3	10.0	0.6
APB Resources	1.64	2.85	7.1	0.2	1.2	13.0	3.4	4.9
Dialog Group	1.80	1.50	30.3	0.9	6.5	3.1	23.4	2.0
Kencana Petroleum	2.49	2.30	20.7	0.4	3.9	3.6	11.9	-
KNM Group	7.45	8.50	22.0	0.4	8.5	3.5	17.4	0.6
Muhibbah Engineering	3.52	4.60	13.0	0.4	2.8	6.8	10.1	1.1
Petra Perdana	5.45	7.30	13.5	0.4	3.0	6.5	7.2	0.7
Scomi Group	1.42	1.75	10.2	0.6	1.5	9.1	6.5	1.8
Shell Refining Company	11.20	14.00	13.2	(4.7)	1.6	7.5	7.2	8.0
Tanjung Offshore	2.88	3.30	16.1	0.3	3.8	5.5	13.1	1.1
Wah Seong Corporation	4.00	3.80	18.9	0.4	3.3	4.9	7.8	2.9
Simple Average			16.5	(0.0)	3.7	6.3	10.7	2.1
Simple Average ex-Shell			16.8	0.4	3.9	6.1	11.1	1.6

Note: CY08 ROE / CY07 PBV

Source: Bloomberg, KAF

The following are some interesting observations from the tables above:

Operational comparative

- Growth is expected to be highly exciting in excess of 30% CAGR over 2007-2009 for all companies, with the exception of Shell (where we have taken a more conservative stance in terms of refining margins and oil prices) and Scomi (where we have exercised some caution in growth rates and margins to buffer against potential shortfalls due to its track record in the past).

- There are marked disparities between ROE's and ROIC's. In particular, ROE's are substantially higher than ROIC's at Alam Maritim and Tanjung Offshore which reflects the high gearing levels at these firms. What this shows is that marine plays are generally susceptible to a very high level of borrowings, which places Petra Perdana in a superior position to its peers as net gearing is at a manageable 34%.
- Another aspect to observe is the net margin differential realised by the various companies. This percentage ranges from low single digits to mid-20%. While we think that low net margins are acceptable as long as strong volume growth is present, unusually low margins provide very little buffer in the event of any unexpected issues that may crop up along the way such project delays and cost overruns. The ones that appear somewhat vulnerable are Kencana, Muhibbah, Scomi, Tanjung Offshore and Wah Seong.
- Free cash flow generation remains poor across the board. Although this is due to high capex to increase capacity in lieu of future earnings, we believe that investors should exercise a little caution when pricing in growth and also consider the potential execution risks involved.

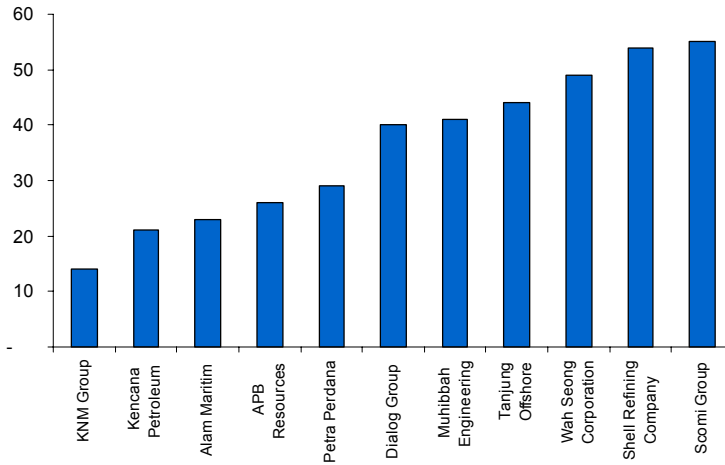
Valuation comparative

- Although certain companies may not stack up so well in the operational comparative, they look very attractive from a valuation standpoint.
- Given strong macro support currently, even the operationally weaker companies should do well and thus valuations play an increasingly vital role.
- Stocks that look cheap on a PER comparison are APB, Muhibbah, Petra Perdana, Scomi and Shell. These companies also rank quite well on the ROE/PBV, EV/EBITDA and dividend yield measures. Interestingly, they make up five out of our list of six Buys.
- The ones that look expensive from a PER standpoint are Dialog, Kencana, KNM and Wah Seong. These stocks are the poorest ranking in terms of ROE/PBV as well, which could imply that prices have run ahead of fundamentals.

FORCED RANKING

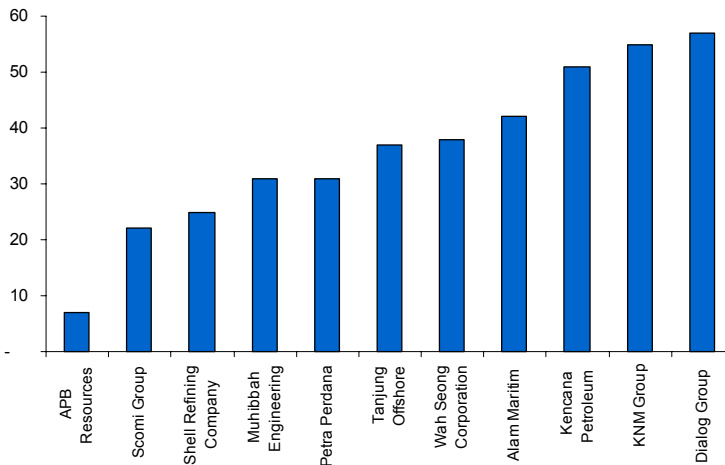
Based on the twelve variables used in the operational and valuation metrics above, we force-ranked the 11 companies to cross-check some of our calls. We assigned a score of 1 for the company which measures the best in each category, all the way to 11 for the worst ranking company. The following charts illustrate the outcomes of this exercise.

Chart 2: Operational forced ranking (lower the better)



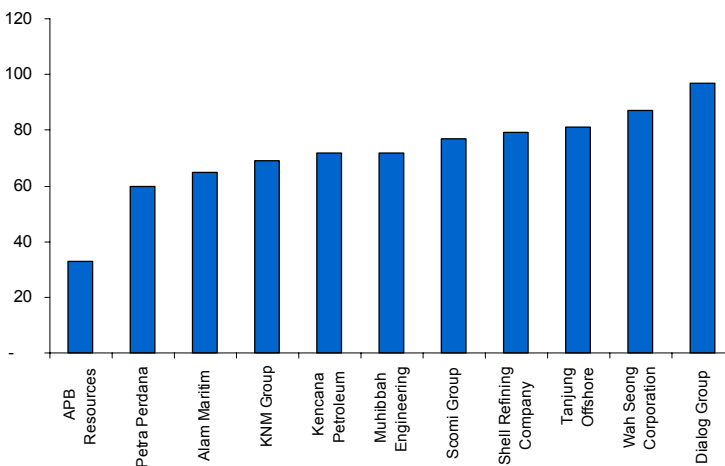
Source: KAF

Chart 3: Valuation forced ranking (lower the better)



Source: KAF

Chart 4: Overall forced ranking (lower the better)



Source: KAF

The following are some key observations we would like to highlight:

- KNM stacks up best in the operational comparative whereas Scomi ranks the worst, largely a function of the former's superior execution record whereas the latter has been somewhat patchy. Kencana and Alam Maritim also stacked up well given their high growth rates and superior ROE's, amongst other factors. On the other hand, Shell and Wah Seong scored rather poorly due to forecasted earnings contraction for the former and vulnerable cash flows for the latter.
- From a valuation standpoint, APB, Scomi and Shell look fairly undervalued whilst Dialog, KNM and Kencana appear quite expensive. APB's cheap valuations are in spite of a reasonable ranking on the operational side while the share prices of Shell and Scomi are possibly already pricing in some of their weaker operational attributes. The relatively poor valuation rankings of KNM and Kencana are supported to some extent by their superior operating characteristics. However, the same cannot be said for Dialog which comes in sixth on the operational measure and last on a valuation basis.
- Interestingly, we have positive calls on the top four companies ranked overall (APB, Petra Perdana, Alam Maritim and KNM), and we have Reduce recommendations on Dialog and Wah Seong which fall at the bottom of the spectrum.

While our recommendations are not based solely on how these companies measured up in terms of the above exercise, it does provide some guidance on relative standing. We do not dispute that the stocks that look expensive now may well deserve to be so, due to superior execution in the past, but investors should be wary of potential disappointments in future as relatively high expectations appear to be already built into share prices.

OUR FORECASTS VERSUS CONSENSUS

As another sanity check, we compiled the following table to see how our forecasts measure up against consensus. We are generally in line for seven companies, above for three (APB, Petra Perdana and Wah Seong), and below for one (Dialog).

Our APB forecasts are underpinned by a belief that capacity expansion will eventually come through whilst consensus has likely dismissed that possibility completely. In Petra Perdana's case, we have imputed earnings based on the new vessels coming on-stream which have been announced by the company. Finally, our forecasts for Wah Seong are based on good order book replenishments on the pipe-coating side and relatively high capacity utilisation for the gas compressors business.

We are unsure of what the market is pricing in for Dialog, but we do not think that our forecasts are conservative on most of its business divisions and maintain our estimates pending any new developments.

Table 6: Our earnings forecasts versus consensus

Normalised net profit (RM m)	KAF			Consensus			% Difference		
	FY07	FY08	FY09	FY07	FY08	FY09	FY07	FY08	FY09
Alam Maritim	44	69	95	44	65	90	0	6	5
APB Resources *	22	35	45	21	27	na	2	26	Nm
Dialog Group *	73	95	122	102	136	195	(28)	(30)	(38)
Kencana Petroleum *	95	149	187	92	144	193	3	3	(3)
KNM Group	197	349	483	186	323	442	6	8	9
Muhibbah Engineering	66	101	114	66	103	117	0	(2)	(3)
Petra Perdana	87	120	164	91	106	141	(4)	13	16
Scomi Group	116	140	160	112	131	152	3	7	5
Shell Refining Company	304	254	288	311	237	279	(2)	7	3
Tanjung Offshore	25	40	55	24	40	52	3	1	6
Wah Seong Corporation	81	119	165	83	110	138	(2)	9	20

* FY07 over, so forecasts refer to FY08-10

Source: Bloomberg, KAF

TARGET PRICES AND STOCK PICKS

For most of the Oil & Gas companies under our coverage, we have implicitly derived target prices based on the Gordon growth version of the dividend discount model, which gives a fair P/B multiple. The only exceptions are Dialog (where we have used a sum-of-parts methodology) and Shell (where we have used an adjusted target P/B to account for its excess capital).

The driver of the Gordon growth formula is the assumption of “sustainable ROE”. Note from the table below that, in our target price calculations, we assume the most ROE expansion for KNM, Tanjung Offshore and Alam Maritim over the medium term and the least for Kencana (albeit this is distorted due to the planned private placement exercise), Petra Perdana and Scomi.

Table 7: Target price derivation

Company	FY07 ROE	Sustainable ROE	ROE Diff.	COE	g	Fair P/B	BVPS	Target Price
Alam Maritim	24%	29%	+5%	10.5%	5.5%	4.7	0.61	2.85
APB Resources	17%	20%	+2%	11.0%	5.5%	2.6	1.10	2.85
Kencana Petroleum	30%	24%	-7%	10.5%	5.5%	3.6	0.63	2.30
KNM Group	41%	54%	+13%	10.5%	5.5%	9.7	0.88	8.50
Muhibbah Engineering	19%	24%	+5%	10.5%	5.5%	3.7	1.26	4.60
Petra Perdana	27%	26%	-1%	10.5%	5.5%	4.1	1.80	7.30
Scomi Group	16%	16%	-1%	11.0%	5.5%	1.8	0.95	1.75
Tanjung Offshore	20%	27%	+7%	10.5%	5.5%	4.3	0.76	3.30
Wah Seong Corporation	17%	21%	+4%	10.5%	5.5%	3.1	1.22	3.80

Source: KAF

We force-ranked the list in terms of implied PER at fair value to see if the target prices make sense and appropriately reflect track record. The forced ranking places Dialog at the top of the pack at 25.2x 2008 PER and APB at the bottom at 12.3x, which we believe is reasonable given the current profiles of these companies.

Note that at fair value, Petra Perdana would still trade at a discount to the other marine plays. Also, whilst we acknowledge that companies like APB and Scomi have had deliverability issues in the past, the valuation differential looks excessive, in our opinion.

Table 8: Implied valuations at fair value

At Fair Value	PER (x)			P/B (x)		Yield (x)	
	CY07	CY08	CY09	CY07	CY08	CY07	CY08
Dialog Group	34.6	25.2	19.6	6.1	5.4	2.2	2.4
KNM Group	44.5	25.1	18.1	15.3	9.7	0.3	0.5
Kencana Petroleum	31.6	19.2	13.7	6.0	3.6	-	-
Tanjung Offshore	29.7	18.5	13.5	5.5	4.4	0.9	0.9
Alam Maritim	29.1	18.4	13.5	6.2	4.7	0.3	0.5
Petra Perdana	24.9	18.1	13.2	5.1	4.1	0.4	0.5
Wah Seong Corporation	26.4	17.9	13.0	3.6	3.1	2.0	3.0
Muhibbah Engineering	26.0	17.0	15.2	4.6	3.6	0.5	0.8
Shell Refining Company	13.8	16.5	14.6	2.0	2.0	6.4	6.4
Scomi Group	15.2	12.6	11.0	2.1	1.8	1.2	1.4
APB Resources	14.9	12.3	8.3	2.5	2.1	2.3	2.8
Simple Average	26.4	18.3	14.0	5.4	4.0	1.5	1.8
Simple Average ex-Shell	27.7	18.4	13.9	5.7	4.2	1.0	1.3

Source: KAF

STOCK SELECTION

Petra Perdana is our top pick in the sector given a very reasonable entry multiple of 13.5x 2008 PER into an Oil Services player with a good track record and relatively visible growth potential of 37% CAGR over 2007-2009, driven by rising charter rates, new capacity, and an expected increase in platform upgrading works in the region.

Although capacity is still delayed at APB, it is no longer possible to find Oil Services exposure at 7.1x 2008 PER supported by strong 34% CAGR over 2007-2009. Also, we have not assumed much incremental capacity for FY08 (September) (only a 7% increase) as most of our growth assumptions come in FY09, of which there is still some time for the company to announce a concrete plan.

For an indirect play into the rising oil price trend, we continue to like Shell Refining Company. Whilst earnings growth profile cannot compare to the likes of the Oil Services companies, its strong cash generative business allows sustainable dividend payments translating to 8% gross yield. More importantly, the replacement cost of its refinery works out to RM25 per share, assuming a capacity replacement value of US\$17,000 per barrel.

We have upgraded Scomi Group from a Reduce to a Buy following updates from a recent company visit. We have revised earnings upwards over the next three years by an average of 26%, mainly on the back of a substantial improvement in our growth assumptions for the Oilfield Services division, which we believe is reasonable given that Scomi has below 4% market share in a segment growing by 11% annually. This has had a material impact on earnings given that it constitutes more than 70% of group EBIT. Our perception of the company has changed to some extent as we now believe it is finally focusing on expanding the business organically and fewer resources are being utilised in M&A activities.

For KNM Group, we have not revised our numbers to account for non-organic expansion as our 57% CAGR forecast over 2007-2009 is not conservative and more importantly, it is difficult to quantify the impact of M&A into explicit earnings estimates. However, we have done some calculations to impute the effect of earnings enhancing M&A exercises over the medium term on fair value. There has been a lot of publicity surrounding its potential RM2bn foreign acquisition and management indicated that M&A-driven growth is a focus area going forward, as long as certain investment criteria are met. Assuming that the company remains geared at the current rate of 23% over the next two years and invests the excess funds at half of its current ROIC of 36%, we estimate that it will add 9 percentage points to group ROE. Therefore, we have added the incremental returns to our sustainable ROE assumption of 45% in deriving our revised target price of RM8.50. However, this provides less than 15% upside from current levels following the share's further 25% appreciation in the past month, thus prompting a downgrade from our long-standing Buy recommendation to Add.

Whilst our perception of Wah Seong Corporation being an industry leader in its chosen field led by quality management remains unchanged, we downgrade our recommendation from an Add to a Reduce as the stock now offers slight downside to our target price. The company offers a good 42% CAGR over 2007-2009 driven by regular order book replenishments on the pipe-coating side and higher capacity at its gas compressors business, but we believe most of these are in the price given that it trades on 18.9x 2008 earnings.

We reiterate our Reduce call on Dialog Group since our argument has not changed. Although we acknowledge that the company should trade at a premium for the recurrent income and cash flows from its centralised tankage facilities at Kertih Terminals and the more recently announced replica at Tanjung Langsat Port, we think that the market has more than priced these in given a steep valuation of 30.3x 2008 PER. Our forecasts on the catalyst handling division are also not conservative, where we have assumed a 10-fold increase in revenue over a three year period.

In addition to our seven existing companies, we initiate coverage on Alam Maritim Resources (AMRB MK, RM2.52, Add, TP: RM2.85), Kencana Petroleum (KEPB MK,

RM2.49, Reduce, TP: RM2.30), Muhibbah Engineering (M) (MUHI MK, RM3.52, Buy, TP: RM4.60), and Tanjung Offshore (TOFF MK, RM2.88, Buy, RM3.30).

Based on current capacity expansion plans coupled with the expected upward trend in charter rates, Alam Maritim looks set to grow earnings by 47% CAGR over 2007-2009. It trades at 16.3x 2008 PER which is reasonable, in our view, given its exciting growth prospects and high value creation. However, the stock has risen by 47% over the past three months in a time where most Oil Services companies have not performed, thus prompting our Add recommendation at current levels.

Kencana offers quality larger cap exposure into the booming Malaysian Oil & Gas sector which would ride on accelerated spending over the medium term. The group has managed to gain access into the lucrative upstream drilling business through recent tie-up with Mermaid. However, the stock has increased by 6x from its IPO price of 41 sen in December last year. At 20.7x 2008 PER on the back of strong growth assumptions of 52% EPS CAGR over 2007-2009, we think it is fully valued up to two years forward.

Despite having a good mix of large scale construction projects, sufficient fabrication capacity for expansion of its cranes and shipyard divisions, and recurrent income from valuable concessions, Muhibbah trades at a discount to the sector at 13.0x 2008 PER supported by strong 31% CAGR over 2007-2009. We believe this is unjustified given exciting growth prospects on all fronts and initiate coverage with a Buy.

Tanjung Offshore is a great smaller cap Oil Services player with meaningful exposure in two recurring income streams; vessel and drilling rig charters. The marine side is the main driver behind our 48% EPS CAGR forecast over 2007-2009 due to a jump in capacity coupled with rising charter rates. Furthermore, there are additional kickers from its smaller, but extremely scaleable, business segments which are essentially less capital intensive. In our view, a valuation of 16.1x 2008 PER is reasonable for exposure into lower-risk growth.

The following pages provide company-specific information on the new stocks under our coverage.



**Add
RM2.52**

Alam Maritim Resources

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Purest marine play

Market Data

Bloomberg code	AMRB MK
Shares o/s (m)	455
Mkt Cap (RMm)	1,147
52 week high/low (RM)	2.86/1.05
Avg daily trading value (RMm)	0.5
KLCI	1,434

Target Price Methodology

Target (RM)	RM2.85 (+13%)
Methodology	Gordon growth, fair P/B
Key Assumptions	ROE=29.0%, COE=10.5%
FY08 PER (x)	18.4
FY08 P/B (x)	4.7
FY08 Yield (x)	0.5

Share Price Performance

Performance (%)	3m	6m	12m	YTD
Absolute	47	66	131	121
Relative to KLCI	34	58	77	69

Source: Bloomberg

Share Price Movement



Source: Bloomberg

Based on current capacity expansion plans coupled with the expected upward trend in charter rates, Alam Maritim looks set to grow earnings by 47% CAGR over FY07-FY09. It trades at 16.3x FY08 PER which is acceptable, in our view, given its exciting growth prospects. However, the stock has done well and we recommend Add at current levels.

■ **Capacity to double over next three years**

Similar to other marine plays, Alam Maritim is embarking on an aggressive fleet expansion plan over the medium term to take advantage of tight supply conditions driving supernormal vessel rates. The company is doubling total capacity from 87K bhp to 175K bhp between FY07 and FY10 through the addition of 15 new vessels, of which 13 are expected to come on-stream by end-FY08 and should see full year contributions by FY09.

■ **Half of incremental capacity to be funded via sale and leaseback**

Seven of these vessels will be financed off-balance sheet. Arrangements have not been finalised yet but the rationale behind this scheme is to ride on the lucrative earnings potential from additional capacity, which would not be possible via usual borrowings given that net gearing is close to being maxed out at 1.9x currently.

■ **Long-term charters would cushion full impact of rising rates**

Whilst we do not doubt that prevailing macro conditions will continue to support high spot rates, note that 80% of Alam Maritim's vessels are leased out on long-term charters, where rates are typically locked in for a few years. Nevertheless, given that there are several opportunities to revise these at various intervals, we have imputed a 20% increase in overall group charter rates for FY07 and 12% per annum thereafter.

■ **Strong growth to provide valuation support**

Alam Maritim trades on 16.3x FY08 earnings and 4.1x P/B, which is acceptable for the good growth prospects it offers and high ROE. However, the share price has risen by 47% over the past three months in a time where most Oil Services stocks have not performed. Due to the strong share price movement, we see only 13% upside to our RM2.85 fair value and recommend Add.

Financial Highlights

FYE December	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	137.7	151.2	214.0	289.2	372.4
Pretax profit	29.4	60.9	60.4	95.5	130.2
Net profit	19.8	49.5	43.8	69.3	94.6
EPS (sen)	3.9	11.1	9.8	15.5	21.2
EPS growth (%)	nm	186.7	(11.5)	58.3	36.5
Gross DPS (sen)	-	0.6	0.9	1.5	2.0
P/E (x)	65.3	22.8	25.7	16.3	11.9
ROE (%)	11.6	29.5	23.5	28.9	29.7
Gross yield (%)	-	0.2	0.4	0.6	0.8
Dividend payout (%)	-	7.0	7.0	7.0	7.0
Net gearing (%)	53.8	159.3	157.0	133.1	104.0
P/BV (x)	7.6	6.8	5.4	4.1	3.1

Source: Company, KAF

PROFIT AND LOSS STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Turnover	137.7	151.2	214.0	289.2	372.4	444.3
Operating costs	(91.7)	(88.2)	(107.8)	(136.1)	(180.3)	(215.4)
EBITDA	46.1	63.0	106.2	153.1	192.1	228.9
Depreciation & amortisation	(9.5)	(14.3)	(24.2)	(28.8)	(33.1)	(37.2)
EBIT	36.5	48.6	82.1	124.3	159.0	191.7
Net interest income	(7.2)	(12.0)	(22.0)	(29.3)	(29.4)	(29.4)
Associates	0.1	0.3	0.4	0.4	0.5	0.6
Exceptionals	-	23.9	-	-	-	-
Pretax profit	29.4	60.9	60.4	95.5	130.2	162.9
Taxation	(9.1)	(10.8)	(15.7)	(24.8)	(33.8)	(42.4)
Minority interest	(0.5)	(0.5)	(0.9)	(1.4)	(1.7)	(2.1)
Net profit	19.8	49.5	43.8	69.3	94.6	118.5
Normalised net profit	19.8	25.6	43.8	69.3	94.6	118.5
No. of shares (m)	513.4	447.0	447.0	447.0	447.0	447.0
EPS (sen)	3.9	11.1	9.8	15.5	21.2	26.5
Normalised EPS (sen)	3.9	5.7	9.8	15.5	21.2	26.5

BALANCE SHEET

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Non-current assets						
Property, vessels and equipment	268.4	452.4	538.4	619.8	696.9	769.9
Investment in an associate	0.4	0.6	1.0	1.4	2.0	2.6
Total non-current assets	268.7	453.0	539.4	621.3	698.8	772.4
Current assets						
Trade and other receivables	61.7	92.5	129.6	173.9	223.0	265.4
Tax recoverable	0.7	0.0	0.0	0.0	0.0	0.0
Cash and bank balances	95.2	19.1	255.8	217.8	205.4	223.1
Total current assets	157.6	111.7	385.4	391.7	428.4	488.5
Total Assets	426.3	564.7	924.8	1,013.0	1,127.3	1,260.9
Current liabilities						
Trade and other payables	33.6	54.0	71.2	91.7	114.5	134.2
Borrowings	24.2	53.6	53.6	53.6	53.6	53.6
Tax payable	-	6.4	6.4	6.4	6.4	6.4
Dues to related company	4.8	-	-	-	-	-
Total current liabilities	62.5	114.0	131.2	151.8	174.6	194.2
Financed by:						
Share capital	93.3	81.3	81.3	81.3	81.3	81.3
Reserves	76.9	83.7	125.7	192.0	281.7	393.6
Shareholders' funds	170.2	165.0	207.0	273.2	363.0	474.9
Minority interest	1.9	9.2	10.1	11.4	13.2	15.3
Borrowings	163.6	243.0	543.0	543.0	543.0	543.0
Deferred tax liabilities	28.0	33.5	33.5	33.5	33.5	33.5
Total Liabilities & Shareholders' Funds	426.3	564.7	924.8	1,013.0	1,127.3	1,260.9

Source: Company, KAF

CASHFLOW STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Cashflow from operations (CFO)						
Pretax profit	29.4	60.9	60.4	95.5	130.2	162.9
Non-cash items	16.8	(0.9)	45.8	57.6	62.0	66.0
Tax paid	(7.2)	(1.7)	(15.7)	(24.8)	(33.8)	(42.4)
Interest paid	(7.5)	(12.2)	(22.5)	(30.0)	(30.0)	(30.0)
Net change in working capital	(1.9)	(8.3)	(19.9)	(23.8)	(26.3)	(22.7)
CFO	29.7	37.7	48.2	74.5	102.0	133.8
Cashflow from investing (CFI)						
Purchase of plant and equipment (CAPEX)	(134.6)	(129.6)	(110.2)	(110.2)	(110.2)	(110.2)
Others	0.0	12.7	0.4	0.7	0.7	0.7
CFI	(134.6)	(116.9)	(109.8)	(109.4)	(109.5)	(109.5)
Cashflow from financing (CFF)						
Dividends paid	-	-	(1.8)	(3.0)	(4.8)	(6.6)
Net proceeds from issuance of shares	86.1	45.5	-	-	-	-
Changes in borrowings	93.6	19.8	300.0	-	-	-
Others	-	17.3	-	-	-	-
CFF	179.7	82.5	298.2	(3.0)	(4.8)	(6.6)
Net change in cash and cash equivalents	74.8	3.4	236.7	(38.0)	(12.4)	17.7

Per Share Data

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EPS (sen)	3.9	11.1	9.8	15.5	21.2	26.5
Normalised EPS (sen)	3.9	5.7	9.8	15.5	21.2	26.5
Gross DPS (sen)	-	0.6	0.9	1.5	2.0	2.6
Book value per share (RM)	0.3	0.4	0.5	0.6	0.8	1.1
Cash earnings per share (sen)	7.6	11.4	18.8	27.7	36.4	44.6
FCF per share (sen)	(19.0)	(17.2)	(8.8)	(1.3)	4.9	12.0

Operational ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EBITDA margin (%)	33.5	41.7	49.6	52.9	51.6	51.5
EBIT margin (%)	26.5	32.2	38.4	43.0	42.7	43.1
Pretax margin (%)	21.4	40.3	28.2	33.0	35.0	36.7
Net margin (%)	14.4	32.7	20.5	24.0	25.4	26.7
Normalised net margin (%)	14.4	16.9	20.5	24.0	25.4	26.7
EBITDA interest cover (x)	6.4	5.2	4.8	5.2	6.5	7.8
Net gearing (%)	53.8	159.3	157.0	133.1	104.0	76.2
ROE (%)	11.6	29.5	23.5	28.9	29.7	28.3
FCF/Revenue (%)	(70.9)	(50.7)	(18.5)	(2.0)	5.9	12.1

Valuation ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
PER (X)	65.3	22.8	25.7	16.3	11.9	9.5
Normalised PER (X)	65.3	44.1	25.7	16.3	11.9	9.5
P/BV (X)	7.6	6.8	5.4	4.1	3.1	2.4
Gross yield (%)	-	0.2	0.4	0.6	0.8	1.0
Dividend payout (%)	-	7.0	7.0	7.0	7.0	7.0

Source: Company, KAF



Reduce
RM2.49

Kencana Petroleum

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Richly valued

Market Data

Bloomberg code	KEPB MK
Shares o/s (m)	892
Mkt Cap (RMm)	2,220
52 week high/low (RM)	3.00/0.41
Avg daily trading value (RMm)	11.1
KLCI	1,434

Target Price Methodology

Target (RM)	RM2.30 (-8%)
Methodology	Gordon growth, fair P/B
Key Assumptions	ROE=23.6%, COE=10.5%
FY09 PER (x)	15.1
FY09 P/B (x)	3.2
FY09 Yield (x)	0.0

Share Price Performance

Performance (%)	3m	6m	12m	YTD
Absolute	(2)	41	nm	113
Relative to KLCI	(11)	35	nm	63

Source: Bloomberg

Share Price Movement



Source: Bloomberg

Kencana offers quality larger cap exposure into the booming Malaysian Oil & Gas sector which would ride on accelerated spending over the medium term. The group has managed to gain access into the lucrative upstream drilling business through recent tie-up with Mermaid. However, the stock has increased by 6x from its IPO price of 41 sen. At 16.4x FY09 PER despite strong growth assumptions of 51% EPS CAGR over FY07-FY10, we think it is richly valued up to two years forward.

■ **Good order book visibility over next 12 months**

Based on current outstanding order book of RM1.8bn, we believe our 63% revenue growth forecast and corresponding 94% bottom-line increase for FY08 is locked in. Management has provided a detailed breakdown of current jobs which depicts a notable clientele profile.

■ **Direct penetration into drilling business through JV with Mermaid**

Moreover, Kencana recently announced a 25:75 JV with Mermaid Drilling of Singapore to co-own and operate a drilling rig to be deployed in Malaysian waters, with the possibility of another three rigs in coming years. The venture is a huge leap into direct exposure to upstream activities. Fabrication of these rigs will be fully undertaken by Kencana and marks its first foray into the higher margin rig construction business.

■ **Our forecasts are not conservative**

We have assumed annual order book replenishments of RM2bn in FY09 growing to RM3bn in FY10, riding on the expected up-cycle in Oil & Gas spending. Our forecasts also assume an average increase in gross margins of 30 bps annually to account for a continual move towards higher-end products, while a possibility of cost overruns eating into net margins which are already quite thin at 6-7% has not been factored in.

■ **Stock looks richly valued up to FY09**

The share price has increased by 6x since its listing in December 2006 whilst earnings grew by a much smaller, albeit impressive, 84% in FY07. This implies a PER re-rating of more than 3x in less than a year. We opine that the stock seems richly valued up to two years forward given that it already trades at 25.6x FY08 PER falling to 15.7x in FY09, on the back of strong 51% EPS CAGR over FY07-FY10.

Financial Highlights

(RMm)

FYE July	FY06A	FY07A	FY08F	FY09F	FY10F
Revenue	437.3	824.5	1,345.5	1,945.2	2,329.8
Pretax profit	29.1	75.6	128.8	199.2	247.8
Net profit	26.7	57.2	95.4	148.9	186.7
EPS (sen)	4.5	6.4	9.7	15.2	19.0
EPS growth (%)	nm	44.0	51.7	56.1	25.4
Gross DPS (sen)	-	-	-	-	-
P/E (x)	55.9	38.8	25.6	16.4	13.1
ROE (%)	25.1	35.0	24.3	23.3	23.1
Gross yield (%)	-	-	-	-	-
Dividend payout (%)	-	-	-	-	-
Net gearing (%)	34.3	(31.9)	(41.8)	(30.9)	(27.2)
P/BV (x)	14.0	10.1	4.3	3.4	2.7

Source: Company, KAF

PROFIT AND LOSS STATEMENT

FYE July (RM m)	2006	2007	2008F	2009F	2010F	2011F
Turnover	437.3	824.5	1,345.5	1,945.2	2,329.8	2,920.0
Cost of goods sold	(384.5)	(728.7)	(1,182.1)	(1,706.2)	(2,037.9)	(2,540.4)
Gross profit	47.0	52.8	95.8	163.3	239.0	291.9
Operating costs	(14.5)	(18.9)	(24.5)	(31.9)	(41.5)	(53.9)
EBITDA	38.3	77.0	138.8	207.1	250.5	325.7
Depreciation & amortisation	(5.8)	(5.9)	(8.4)	(12.8)	(14.6)	(16.2)
EBIT	32.6	71.1	130.3	194.3	235.9	309.5
Net interest income	(3.8)	(3.7)	(1.8)	(0.8)	(0.7)	0.7
Associates & JVs	0.4	0.3	0.3	5.7	12.6	13.8
Exceptionals	-	7.9	-	-	-	-
Pretax profit	29.1	75.6	128.8	199.2	247.8	324.0
Taxation	(2.4)	(18.5)	(33.4)	(50.3)	(61.2)	(80.7)
Net profit	26.7	57.2	95.4	148.9	186.7	243.3
Normalised net profit	26.7	49.3	95.4	148.9	186.7	243.3
No. of shares (m)	600.0	891.5	980.7	980.7	980.7	980.7
EPS (sen)	4.5	6.4	9.7	15.2	19.0	24.8
Normalised EPS (sen)	4.5	5.5	9.7	15.2	19.0	24.8

BALANCE SHEET

FYE July (RM m)	2006	2007	2008F	2009F	2010F	2011F
Non-current assets						
Property, plant and equipment	126.2	181.4	275.4	312.6	348.1	381.9
Investments in associates and JVs	0.8	1.2	1.5	119.5	240.9	254.7
Goodwill	0.8	24.2	46.4	46.4	46.4	46.4
Total non-current assets	127.8	206.9	323.4	478.5	635.3	682.9
Current assets						
Trade and other receivables	135.5	211.5	381.0	550.8	659.7	826.9
Tax recoverable	10.5	-	-	-	-	-
Cash and bank balances	53.8	163.5	329.3	314.1	338.2	525.1
Total current assets	199.8	374.9	710.3	864.9	997.9	1,352.0
Total Assets	327.6	581.8	1,033.6	1,343.4	1,633.2	2,034.9
Current liabilities						
Trade and other payables	99.8	254.1	360.9	521.7	624.9	783.2
Short term borrowings	76.7	40.5	40.5	40.5	40.5	40.5
Taxation	2.1	-	-	-	-	-
Total current liabilities	178.6	294.5	401.4	562.2	665.4	823.7
Financed by:						
Share capital	60.0	89.2	98.1	98.1	98.1	98.1
Reserves	46.5	130.8	466.9	615.8	802.5	1,045.8
Shareholders' funds	106.5	219.9	565.0	713.9	900.5	1,143.9
Long term borrowings	13.6	52.8	52.8	52.8	52.8	52.8
Deferred taxation	8.3	14.5	14.5	14.5	14.5	14.5
Others	20.6	-	-	-	-	-
Total Liabilities & Shareholders' Funds	327.6	581.8	1,033.6	1,343.4	1,633.2	2,034.9

Source: Company, KAF

CASHFLOW STATEMENT

FYE July (RM m)	2006	2007	2008F	2009F	2010F	2011F
Cashflow from operations (CFO)						
Pretax profit	29.1	75.6	128.8	199.2	247.8	324.0
Non-cash items	10.5	9.2	10.0	7.9	2.7	1.7
Tax paid	(6.2)	(18.5)	(33.4)	(50.3)	(61.2)	(80.7)
Interest paid	(4.6)	(5.2)	(5.2)	(5.2)	(5.2)	(5.2)
Net change in working capital	(33.0)	31.9	(62.7)	(9.0)	(5.8)	(8.8)
CFO	(4.2)	93.2	37.4	142.6	178.3	231.0
Cashflow from investing (CFI)						
Purchase of plant and equipment (CAPEX)	(29.4)	(41.9)	(50.0)	(50.0)	(50.0)	(50.0)
Acquisition of subsidiaries	-	-	(74.6)	-	-	-
Investment in Mermaid Kencana Rigs	-	-	-	(112.2)	(108.8)	-
Interest received	0.7	1.5	3.4	4.4	4.5	6.0
CFI	(28.7)	(40.4)	(121.2)	(157.8)	(154.3)	(44.0)
Cashflow from financing (CFF)						
Net proceeds from issuance of shares	-	56.3	249.6	-	-	-
Changes in borrowings	12.5	32.3	-	-	-	-
Advance from shareholders	7.2	(20.0)	-	-	-	-
Advance from associates	0.6	(0.6)	-	-	-	-
CFF	20.3	68.1	249.6	-	-	-
Net change in cash and cash equivalents	(12.6)	120.8	165.8	(15.2)	24.0	186.9

Per Share Data

FYE July	2006	2007	2008F	2009F	2010F	2011F
EPS (sen)	4.5	6.4	9.7	15.2	19.0	24.8
Normalised EPS (sen)	4.5	5.5	9.7	15.2	19.0	24.8
Gross DPS (sen)	-	-	-	-	-	-
Book value per share (RM)	0.2	0.2	0.6	0.7	0.9	1.2
Cash earnings per share (sen)	5.8	8.2	14.0	21.0	25.5	33.3
FCF per share (sen)	(5.1)	5.4	(0.7)	10.0	13.6	19.0

Operational ratios

FYE July	2006	2007	2008F	2009F	2010F	2011F
Gross margin (%)	12.1	11.6	12.1	12.3	12.5	13.0
EBITDA margin (%)	8.8	9.3	10.3	10.6	10.8	11.2
EBIT margin (%)	7.4	8.6	9.7	10.0	10.1	10.6
Pretax margin (%)	6.7	9.2	9.6	10.2	10.6	11.1
Net margin (%)	6.1	6.9	7.1	7.7	8.0	8.3
Normalised net margin (%)	6.1	6.0	7.1	7.7	8.0	8.3
EBITDA interest cover (x)	10.0	21.0	75.5	260.1	340.8	(450.2)
Net gearing (%)	34.3	(31.9)	(41.8)	(30.9)	(27.2)	(37.8)
ROE (%)	25.1	35.0	24.3	23.3	23.1	23.8
FCF/Revenue (%)	(7.0)	5.9	(0.5)	5.0	5.7	6.4

Valuation ratios

FYE July	2006	2007	2008F	2009F	2010F	2011F
PER (X)	55.9	38.8	25.6	16.4	13.1	10.0
Normalised PER (X)	55.9	45.1	25.6	16.4	13.1	10.0
P/BV (X)	14.0	10.1	4.3	3.4	2.7	2.1
Gross yield (%)	-	-	-	-	-	-
Dividend payout (%)	-	-	-	-	-	-

Source: Company, KAF



Buy
RM3.52

Muhibbah Engineering (M)

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Still at a discount

Market Data

Bloomberg code	MUHI MK
Shares o/s (m)	384
Mkt Cap (RMm)	1,351
52 week high/low (RM)	4.28/0.94
Avg daily trading value (RMm)	4.2
KLCI	1,434

Target Price Methodology

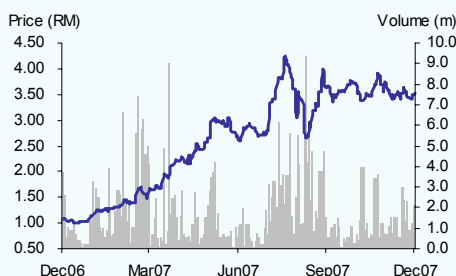
Target (RM)	RM4.60 (+31%)
Methodology	Gordon growth, fair P/B
Key Assumptions	ROE=23.8%, COE=10.5%
FY08 PER (x)	17.0
FY08 P/B (x)	3.6
FY08 Yield (x)	0.8

Share Price Performance

Performance (%)	3m	6m	12m	YTD
Absolute	(4)	31	231	238
Relative to KLCI	(12)	25	153	159

Source: Bloomberg

Share Price Movement



Source: Bloomberg

Despite having a good mix of large scale construction projects, sufficient fabrication capacity for expansion of its cranes and shipyard divisions, and recurrent income from valuable concessions, Muhibbah trades at a discount to the sector at 13.0x FY08 PER supported by strong 31% CAGR over FY07-FY09. We believe this is unjustified. Buy.

Large construction order book already locked in

Although the bulk of Muhibbah's construction order book of RM3.5bn is contributed by non-Oil & Gas related projects (such as the South Klang Valley Expressway and the catering facility at the New Doha International Airport), these projects would lock in a continual income stream all the way through to FY10. We have assumed an order book replenishment of RM1bn in FY08 and RM1.5bn in FY09, with conservative EBIT margins of only 4-5%.

Sufficient capacity for cranes and shipyard divisions

Given robust demand for the supply of Oil & Gas amenities, available capacity is the key to securing high-end job orders commanding good margins. We estimate that Muhibbah has sufficient land area to ramp up production materially without incurring high capex over the medium term. Between FY06 and FY09, we have assumed a cumulative 45% increase in cranes volumes with 5% CAGR in prices, and a cumulative 41% increase in shipyard volumes with 18% CAGR in prices.

Concessions to provide a firm and recurring base

Furthermore, its valuable Cambodian airports and Malaysian federal roads maintenance concessions will continue to supply recurring income and cash flow streams to the group over the longer term. We have imputed 15-20% annual growth in visitor arrivals at the airports on the back of buoyant tourism trends in the region, and a much slower 5% annual growth for the roads concession.

Buy despite out-performance

While the stock has re-rated significantly year-to-date, it still trades at a huge discount to the sector at 13.0x FY08 PER, 2.8x P/B and 1.1% dividend yield. We believe this is unjustified for a company offering strong 31% CAGR over FY07-FY09 and good ROE expansion.

Financial Highlights

FYE December	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	970.7	1,086.4	1,454.3	2,421.9	2,708.9
Pretax profit	45.7	65.1	103.1	158.7	181.0
Net profit	26.1	33.8	66.3	101.0	113.5
EPS (sen)	7.2	9.0	17.7	27.0	30.4
EPS growth (%)	232.8	25.3	96.2	52.3	12.4
Gross DPS (sen)	2.8	3.8	2.5	3.7	4.2
P/E (x)	48.8	39.0	19.9	13.0	11.6
ROE (%)	9.4	11.1	19.0	23.8	21.7
Gross yield (%)	0.8	1.1	0.7	1.1	1.2
Dividend payout (%)	20.3	23.7	10.0	10.0	10.0
Net gearing (%)	39.0	44.3	45.2	55.2	48.4
P/BV (x)	4.4	4.1	3.5	2.8	2.3

Source: Company, KAF

PROFIT AND LOSS STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Turnover	970.7	1,086.4	1,454.3	2,421.9	2,708.9	2,732.6
Operating costs	(911.3)	(1,017.7)	(1,348.4)	(2,258.9)	(2,521.9)	(2,538.8)
EBITDA	59.5	68.7	105.8	163.0	187.0	193.8
Depreciation & amortisation	(9.8)	(18.6)	(19.9)	(21.9)	(23.8)	(25.5)
EBIT	49.6	50.2	85.9	141.0	163.2	168.3
Net interest income	(11.0)	(8.7)	(13.7)	(17.1)	(20.2)	(19.7)
Associates and JVs	16.7	32.4	31.0	34.8	38.0	41.6
Exceptionals	(9.6)	(8.8)	-	-	-	-
Pretax profit	45.7	65.1	103.1	158.7	181.0	190.1
Taxation	(2.7)	(17.3)	(25.8)	(39.7)	(45.3)	(47.5)
Minority interest	(17.0)	(14.0)	(11.0)	(18.1)	(22.2)	(23.2)
Net profit	26.1	33.8	66.3	101.0	113.5	119.4
Normalised net profit	35.6	42.6	66.3	101.0	113.5	119.4
No. of shares (m)	361.4	374.0	374.0	374.0	374.0	374.0
EPS (sen)	7.2	9.0	17.7	27.0	30.4	31.9
Normalised EPS (sen)	9.9	11.4	17.7	27.0	30.4	31.9

BALANCE SHEET

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Non-current assets						
Property, plant and equipment	261.0	283.3	315.1	345.0	373.0	399.3
Prepaid lease payments	34.4	33.7	33.7	33.7	33.7	33.7
Investments in associates	120.3	131.0	147.8	168.4	192.2	219.5
Intangible assets	8.1	6.7	6.7	6.7	6.7	6.7
Deferred tax assets	2.1	0.2	0.2	0.2	0.2	0.2
Total non-current assets	425.8	454.9	503.5	553.9	605.8	659.4
Current assets						
Inventories	95.1	124.9	167.2	278.5	311.5	314.3
Trade and other receivables	581.8	693.8	835.9	1,252.9	1,401.3	1,413.6
Current tax assets	10.8	5.1	5.1	5.1	5.1	5.1
Cash and bank balances	105.3	99.5	70.7	75.3	60.8	109.8
Others	0.4	0.7	0.7	0.7	0.7	0.7
Total current assets	793.5	924.1	1,079.5	1,612.4	1,779.4	1,843.4
Total Assets	1,219.3	1,378.9	1,583.0	2,166.4	2,385.2	2,502.8
Current liabilities						
Trade and other payables	337.5	436.8	584.6	973.6	1,089.0	1,098.6
Bills payable	314.2	252.8	252.8	252.8	252.8	252.8
Loans and borrowings	165.5	180.8	180.8	180.8	180.8	180.8
Others	20.0	13.6	13.6	13.6	13.6	13.6
Total current liabilities	837.2	884.0	1,031.8	1,420.8	1,536.2	1,545.8
Financed by:						
Share capital	180.7	187.0	187.0	187.0	187.0	187.0
Reserves	106.5	134.4	190.6	285.0	388.4	496.5
Shareholders' funds	287.2	321.4	377.6	472.0	575.4	683.5
Minority interest	12.1	57.6	57.6	57.6	57.6	57.6
Advances from minority shareholders	18.2	17.7	17.7	17.7	17.7	17.7
Loans and borrowings	56.6	86.6	86.6	186.6	186.6	186.6
Deferred tax liabilities	7.9	11.7	11.7	11.7	11.7	11.7
Total Liabilities & Shareholders' Funds	1,219.3	1,378.9	1,583.0	2,166.4	2,385.2	2,502.8

Source: Company, KAF

CASHFLOW STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Cashflow from operations (CFO)						
Pretax profit	45.7	65.1	103.1	158.7	181.0	190.1
Non-cash items	39.1	1.4	2.7	4.2	6.0	3.7
Tax paid	(6.6)	(4.2)	(25.8)	(39.7)	(45.3)	(47.5)
Net interest	(9.3)	(3.1)	(13.7)	(17.1)	(20.2)	(19.7)
Net change in working capital	(42.5)	(37.9)	(36.5)	(139.3)	(66.1)	(5.5)
CFO	26.4	21.4	29.8	(33.0)	55.4	121.1
Cashflow from investing (CFI)						
Purchase of plant and equipment (CAPEX)	(25.0)	(51.8)	(51.8)	(51.8)	(51.8)	(51.8)
Acquisition of associates	(13.5)	(0.2)	-	-	-	-
Dividends received from associates	9.2	14.2	14.2	14.2	14.2	14.2
Others	2.9	47.3	-	-	-	-
CFI	(26.5)	9.4	(37.6)	(37.6)	(37.6)	(37.6)
Cashflow from financing (CFF)						
Dividends paid to shareholders	(4.3)	(6.0)	(10.1)	(6.6)	(10.1)	(11.4)
Dividends paid to minority shareholders	(16.8)	(14.0)	(11.0)	(18.1)	(22.2)	(23.2)
Changes in borrowings	61.0	(44.4)	-	100.0	-	-
Interest paid	0.3	(1.1)	-	-	-	-
CFF	40.1	(65.6)	(21.1)	75.3	(32.3)	(34.5)
Currency translation differences	0.2	3.0	-	-	-	-
Net change in cash and cash equivalents	40.1	(31.8)	(28.9)	4.6	(14.5)	49.0

Per Share Data

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EPS (sen)	7.2	9.0	17.7	27.0	30.4	31.9
Normalised EPS (sen)	9.9	11.4	17.7	27.0	30.4	31.9
Gross DPS (sen)	2.8	3.8	2.5	3.7	4.2	4.4
Book value per share (RM)	0.8	0.9	1.0	1.3	1.5	1.8
Cash earnings per share (sen)	13.4	16.0	24.6	39.0	44.6	46.5
FCF per share (sen)	(4.1)	(6.7)	(2.2)	(18.1)	6.4	23.8

Operational ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EBITDA margin (%)	6.1	6.3	7.3	6.7	6.9	7.1
EBIT margin (%)	5.1	4.6	5.9	5.8	6.0	6.2
Pretax margin (%)	4.7	6.0	7.1	6.6	6.7	7.0
Net margin (%)	2.7	3.1	4.6	4.2	4.2	4.4
Normalised net margin (%)	3.7	3.9	4.6	4.2	4.2	4.4
EBITDA interest cover (x)	5.4	7.9	7.7	9.5	9.3	9.8
Net gearing (%)	39.0	44.3	45.2	55.2	48.4	34.8
ROE (%)	9.4	11.1	19.0	23.8	21.7	19.0
FCF/Revenue (%)	(1.5)	(2.3)	(0.6)	(2.8)	0.9	3.3

Valuation ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
PER (X)	48.8	39.0	19.9	13.0	11.6	11.0
Normalised PER (X)	35.7	30.9	19.9	13.0	11.6	11.0
P/BV (X)	4.4	4.1	3.5	2.8	2.3	1.9
Gross yield (%)	0.8	1.1	0.7	1.1	1.2	1.3
Dividend payout (%)	20.3	23.7	10.0	10.0	10.0	10.0

Source: Company, KAF



Buy
RM2.88

Tanjung Offshore

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Expansion via conservative policies

Market Data

Bloomberg code	TOFF MK
Shares o/s (m)	202
Mkt Cap (RMm)	583
52 week high/low (RM)	3.70/1.92
Avg daily trading value (RMm)	0.7
KLCI	1,434

Target Price Methodology

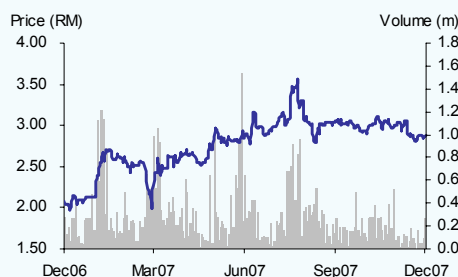
Target (RM)	RM3.30 (+15%)
Methodology	Gordon growth, fair P/B
Key Assumptions	ROE=27.2%, COE=10.5%
FY08 PER (x)	18.5
FY08 P/B (x)	4.4
FY08 Yield (x)	0.9

Share Price Performance

Performance (%)	3m	6m	12m	YTD
Absolute	(6)	0	39	35
Relative to KLCI	(14)	(4)	7	3

Source: Bloomberg

Share Price Movement



Source: Bloomberg

Tanjung Offshore is a great smaller cap Oil Services player with meaningful exposure in two recurring income streams; vessel and drilling rig charters. The marine side is expected to drive our 48% EPS CAGR forecast over FY07-FY09 due to a jump in capacity coupled with rising charter rates. It trades on reasonable 16.1x FY08 earnings. Buy.

■ Growth fuelled by marine division

Tanjung Offshore is looking to add five new vessels to its current fleet of seven, most with full year contributions by FY09. In our view, the company's ability to substantially increase its fleet size via internal financing and bank borrowings, albeit off a lower base, demonstrates a more conservative approach to its expansion policies. We estimate that the marine segment constitutes about 50-60% of group earnings.

■ Drilling rigs segment to see step jumps from incremental assets

As the exclusive agent in Malaysia for global rig owner Hercules Offshore, the company currently supplies a jack-up drilling rig and a self-elevating relocating facility (SERF) to Murphy Oil. Negotiations are underway to market up to two more rigs for Malaysian waters by year end. Given that Tanjung Offshore earns a clean 3% margin for the provision and mobilisation of these rigs, any increase in asset size would automatically boost bottom-line at virtually no investment cost.

■ Additional kickers from engineering equipment and maintenance

Our forecasts have only assumed annual revenue growth of 5% for engineering equipment and 10% for maintenance with a slight expansion in margins over the next few years. Being the exclusive agent for a range of foreign products which ultimately require servicing and replacement, these businesses are actually very scalable and contributions could surprise on the upside. We estimate that combined profits would constitute approximately 27% of group earnings this year.

■ Good growth off a low base

We believe that this relatively small cap play has a greater potential to achieve strong 48% CAGR over FY07-FY09, coming off a lower base. We see 15% upside to current valuations of 16.1x FY08 PER and 3.8x P/B given strong growth prospects and superior mid-20% ROE.

Financial Highlights

FYE December	FY05A	FY06A	FY07F	FY08F	FY09F
Revenue	205.5	293.3	447.4	659.4	732.5
Pretax profit	11.6	17.5	27.9	44.8	61.5
Net profit	16.0	18.3	25.1	40.3	55.4
EPS (sen)	13.6	8.1	11.1	17.8	24.5
EPS growth (%)	nm	(40.5)	37.4	60.5	37.3
Gross DPS (sen)	-	1.8	3.0	3.0	3.0
P/E (x)	21.2	35.6	25.9	16.1	11.8
ROE (%)	22.0	19.7	20.3	26.3	28.1
Gross yield (%)	-	0.6	1.1	1.1	1.1
Dividend payout (%)	-	13.8	17.3	10.8	7.8
Net gearing (%)	56.1	132.2	174.6	182.6	160.4
P/BV (x)	4.7	5.8	4.8	3.8	2.9

Source: Company, KAF

PROFIT AND LOSS STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Turnover	205.5	293.3	447.4	659.4	732.5	745.6
Operating costs	(192.7)	(271.7)	(403.1)	(590.8)	(640.7)	(642.9)
EBITDA	12.8	21.5	44.3	68.6	91.8	102.8
Depreciation & amortisation	(2.0)	(4.3)	(7.5)	(10.8)	(14.0)	(17.1)
EBIT	10.8	17.2	36.8	57.8	77.8	85.7
Net interest income	(0.7)	(1.6)	(10.0)	(14.0)	(17.4)	(19.0)
Associates	1.4	1.9	1.1	1.1	1.2	1.1
Exceptionals	-	-	-	-	-	-
Pretax profit	11.6	17.5	27.9	44.8	61.5	67.9
Taxation	4.5	0.8	(2.8)	(4.5)	(6.2)	(6.8)
Minority interest	(0.0)	-	-	-	-	-
Net profit	16.0	18.3	25.1	40.3	55.4	61.1
Normalised net profit	16.0	18.3	25.1	40.3	55.4	61.1
Basic no. of shares (m)	117.8	198.2	198.2	198.2	198.2	198.2
Fully diluted no. of shares (m)	117.8	226.0	226.0	226.0	226.0	226.0
EPS (sen)	13.6	8.1	11.1	17.8	24.5	27.0
Normalised EPS (sen)	13.6	8.1	11.1	17.8	24.5	27.0

BALANCE SHEET

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Non-current assets						
Property, plant and equipment	122.0	211.3	303.7	392.9	478.9	511.9
Investments in associates	4.2	1.8	2.9	3.9	5.1	6.2
Deferred taxation	4.3	5.5	5.5	5.5	5.5	5.5
Total non-current assets	130.5	218.5	312.1	402.4	489.5	523.6
Current assets						
Inventories	1.0	1.8	2.7	3.9	4.4	4.5
Trade and other receivables	73.8	129.2	186.5	265.2	292.3	297.2
Amount owing by associate	2.8	-	-	-	-	-
Cash and bank balances	10.6	20.4	13.2	16.6	52.7	114.0
Total current assets	88.2	151.4	202.3	285.7	349.4	415.6
Total Assets	218.6	369.9	514.4	688.0	838.9	939.2
Current liabilities						
Trade and other payables	94.6	87.8	129.8	187.4	207.2	210.8
Short term borrowings	10.5	22.2	22.2	22.2	22.2	22.2
Provision for taxation	0.0	0.0	0.0	0.0	0.0	0.0
Total current liabilities	105.1	110.1	152.0	209.7	229.5	233.1
Financed by:						
Share capital	58.9	99.1	99.1	99.1	99.1	99.1
Reserves	13.7	13.6	36.2	72.1	123.2	179.9
Shareholders' funds	72.7	112.7	135.3	171.3	222.3	279.0
Bank borrowings	40.8	1.5	81.5	161.5	241.5	281.5
Serial fixed rate bond	-	145.6	145.6	145.6	145.6	145.6
Total Liabilities & Shareholders' Funds	218.6	369.9	514.4	688.0	838.9	939.2

Source: Company, KAF

CASHFLOW STATEMENT

FYE Dec (RM m)	2005	2006	2007F	2008F	2009F	2010F
Cashflow from operations (CFO)						
Pretax profit	11.6	17.5	27.9	44.8	61.5	67.9
Non-cash items	0.6	4.1	16.4	23.8	30.2	34.9
Tax paid	(2.9)	(0.1)	(2.8)	(4.5)	(6.2)	(6.8)
Net change in working capital	(13.6)	(61.9)	(16.2)	(22.3)	(7.7)	(1.4)
CFO	(4.3)	(40.5)	25.3	41.8	77.9	94.6
Cashflow from investing (CFI)						
Purchase of plant and equipment (CAPEX)	(47.0)	(92.4)	(100.0)	(100.0)	(100.0)	(50.0)
Interest received	0.3	1.5	0.5	0.4	1.0	2.5
Others	(0.3)	6.1	-	-	-	-
CFI	(47.1)	(84.8)	(99.5)	(99.6)	(99.0)	(47.5)
Cashflow from financing (CFF)						
Dividends paid	-	(2.0)	(2.5)	(4.3)	(4.3)	(4.3)
Proceeds from issuance of shares	38.2	19.2	-	-	-	-
Proceeds of the Bonds issue	-	145.6	-	-	-	-
Changes in borrowings	16.6	(44.3)	80.0	80.0	80.0	40.0
Interest paid	(0.4)	(3.0)	(10.5)	(14.5)	(18.5)	(21.5)
Others	(0.7)	4.4	-	-	-	-
CFF	53.7	119.9	67.0	61.2	57.2	14.2
Net change in cash and cash equivalents	2.4	(5.3)	(7.2)	3.4	36.2	61.3

Per Share Data

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EPS (sen)	13.6	8.1	11.1	17.8	24.5	27.0
Normalised EPS (sen)	13.6	8.1	11.1	17.8	24.5	27.0
Gross DPS (sen)	-	1.8	3.0	3.0	3.0	3.0
Book value per share (RM)	0.6	0.5	0.6	0.8	1.0	1.2
Cash earnings per share (sen)	10.3	8.8	15.2	24.1	32.9	37.1
FCF per share (sen)	(43.1)	(67.1)	(37.7)	(29.4)	(11.1)	22.5

Operational ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
EBITDA margin (%)	6.2	7.3	9.9	10.4	12.5	13.8
EBIT margin (%)	5.3	5.9	8.2	8.8	10.6	11.5
Pretax margin (%)	5.6	6.0	6.2	6.8	8.4	9.1
Net margin (%)	7.8	6.2	5.6	6.1	7.6	8.2
Normalised net margin (%)	7.8	6.2	5.6	6.1	7.6	8.2
EBITDA interest cover (x)	18.8	13.3	4.4	4.9	5.3	5.4
Net gearing (%)	56.1	132.2	174.6	182.6	160.4	120.2
ROE (%)	22.0	19.7	20.3	26.3	28.1	24.4
FCF/Revenue (%)	(24.7)	(45.3)	(16.7)	(8.8)	(3.0)	6.0

Valuation ratios

FYE Dec	2005	2006	2007F	2008F	2009F	2010F
PER (X)	21.2	35.6	25.9	16.1	11.8	10.7
Normalised PER (X)	21.2	35.6	25.9	16.1	11.8	10.7
P/BV (X)	4.7	5.8	4.8	3.8	2.9	2.3
Gross yield (%)	-	0.6	1.1	1.1	1.1	1.1
Dividend payout (%)	-	13.8	17.3	10.8	7.8	7.1

Source: Company, KAF

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*Dato' Ahmad Bin Kadis
Managing Director*

Recommendation Structure

KAF-Seagroatt & Campbell Securities Sdn Bhd uses the following rating system:

BUY	Price appreciation in excess of 15% expected in the next 12 months
SELL	Price depreciation in excess of 15% expected in the next 12 months
ADD	Price appreciation between 0-15% in the next 12 months
REDUCE	Price depreciation between 0-15% in the next 12 months

Applicability of Ratings:

The respective analyst maintains a coverage universe of stocks, the list of which may be adjusted according to needs. Investment ratings are only applicable to the stocks, which form part of the coverage universe. Reports on companies, which are not part of the coverage, do not carry investment ratings as we do not actively follow developments in these companies.

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