

Recasting an Industry

Malaysian steelmakers require careful selection

By Steven K.C. Poh, Kuala Lumpur

FIRST THE GOOD NEWS: Malaysian steel will enjoy tariff protection and rising demand -- up 12% a year from construction -- for several more years. "Malaysian producers will have more time to become competitive, especially in flat products," says Jennifer Chai of TA Securities. Duties of 30% hit most imports. Billets are restricted; they come in only after local supplies run out. But shifts in the industry mean that investors still need to choose counters with care.

Unlisted, state-backed Perwaja Steel, saddled by debts and \$2.6 billion in losses, is being resuscitated. Southern Steel is being injected into Malex Industries, a property and cement products company which also plans to buy 20.1% of New Zealand's Brierley Investments. Smallish, unlisted Antara Steel Mills is to be subsumed by property company Damansara Realty. And Pernas International Holdings, just after a management buyout, is to purchase Malayawata Steel.

"We are cautious over the long term, as the sector is exposed to competition and oversupply," adds Patrick Lim of Jupiter Securities. "Other concerns include high risks, a long payback period and the huge capital outlay." Lim says an oversupply in long products like rods is anticipated in 1998. Simone Yeoh of HSBC James Capel likes Lion Land, which owns 99% of Amsteel Mills, "despite investors' skepticism about the group's belief in diversification." Steel will remain its core business with over 85% of operating profits, Yeoh explains. "Lion Land is the cheapest steel stock on the exchange," she adds. Its ratios of share price to earnings per share (p/e) are 9.2 times 1996 EPS and 8.4 times 1997 (market avg 17; sector avg 12).

Amsteel Corp., another Lion Group venture, owns 56% of Lion Land and half of Megasteel, which will start up Malaysia's first flat-steel plant in late 1998 (capacity: 4 million tons/yr). Demand for flat steel products, poised to grow about 20% a year, will be a boon for Amsteel Corp. But its p/e of 19 is far higher than the industry norm, notes Lee Kar Len of Mohaiyani Securities. "And high-risk China operations and high net debt-to-equity ratio compound the negative sentiment."

Jupiter's Lim defends the counter. He blames the stock's lethargy on the large amount in public hands, high gearing and the company's non-steel businesses, which make it less focused. But Lim says its debt of 2.7 times equity is normal for domestic steel companies and should fall about 15% once warrants to buy the company's stock are exercised. Lim adds that a 50% share in Megasteel's profits will boost Amsteel Corp.'s EPS by 35% from now until 1999.

David Ong of Nomura Research Institute's Singapore office is also generally bullish. He favors Maruichi (Malaysia) Steel Tube, though it may lag for a time. "It's a long-term buy," he stresses. "Maruichi is the leading producer of steel pipes in Malaysia and one of the most efficient manufacturers of tubular steel." Other pluses: a resilient record of earnings growth since 1985, strong management and technical expertise. Ong also likes Southern, a pure steel play in long products, with good management, rising earnings and efficient, expanded plants.

Ong believes Pernas's buyout bid will give greater focus to Malayawata Steel activities. It is No. 2 in bars, with strong earnings growth tipped in the next two years, and low debt -- a plus as interest rates surge. But Mohaiyani's Lee thinks Malayawata is the weakest steel stock. Its

operating margins are much lower than Southern's. And unlike Southern and Lion Land, Malayawata has yet to unveil expansion plans to make hay while demand and duties are high.

