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Eastern Pacific Ind. Corp. Bhd **RM1.78**

Venturing into pipe threading **Fair value : RM2.30**

BUY

- **This is EPIC's maiden venture into pipe threading.**
- **We are positive on this acquisition: provides potential earnings expansion in an area that EPIC is familiar with (i.e. O&G)**
- **However, we estimate a marginal improvement on bottomline.**
- **Maintain BUY with fair value of RM2.30. We like EPIC's steady financial position, strong management team and attractive valuations (PER05 of 11.5X, DY: 7%).**

Last Friday EPIC to acquire a 95% stake in Tubex Sdn Bhd for RM18.5m from Ancom Energy & Services Sdn Bhd (AES), Suhaimi bin Mukhtar and Datuk Ismail Hashim. EPIC intends to finance the acquisition entirely through internally generated funds. This should not be a burden since EPIC's cash hoard stood at RM70.5m as at end-March 2005. EPIC has no borrowings.

Tubex Sdn Bhd. Tubex provides pipe threading and ancillary services specialising in threading and cutting of tubular, casing and down hole equipment used in oil and gas offshore drilling activities, tubular inspection and maintenance services. Tubex is based in Kemaman, the oil and gas hub in Peninsular Malaysia.

We are positive on the acquisition. Our optimism is backed by these factors:

1. **Purchase price:** The purchase price is at 1.9X estimate FY05 NTA, but valuation is decent with an estimated PER of 10X based on FY05e net profit of RM1.7m. We believe the premium is due to Tubex's current profit-making operations. Nevertheless, EPIC is likely to obtain a RM250,000 reduction in purchase price should the audited FY05 NTA be less than that of the unaudited accounts. On the other hand, should the audited NTA be higher, the purchase price shall not be increased or adjusted upwards.

Earnings Forecast

Year End Dec	2003A	2004A	2005F	2006F	2007F
Turnover (RM m)	70.5	80.1	82.5	87.5	92.9
Net Profit (RM m)	19.8	23.2	25.2	27.3	27.9
EPS (sen)	12.2	14.2	15.5	16.8	17.1
DPS (sen)	13.0	13.0	13.0	13.0	13.0
P/E Ratio (x)	14.6	12.5	11.5	10.5	10.4
Div. Yield (%)	7.3	7.3	7.3	7.3	7.3

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Source: Mayban Securities

2. *Shareholding*: Suhaimi Mukhtar shall retain his 5% stake in Tubex and will continue to serve as the Chief Operating Officer or such other position determined by EPIC for a period of two years from the completion date. We view this arrangement positively since Suhaimi is the founder and “brain” of Tubex. Thus, it makes sense for EPIC to retain him by allowing him a 5% share in Tubex.
3. *Earnings expansion opportunity*: The proposed acquisition would provide EPIC the opportunity to enlarge its earnings base. Tubex’s FY04 profit after tax was RM603,760 while FY05 PBT stood at RM2.4m. Currently, the bulk of EPIC’s turnover and earnings are driven by the Kemaman Supply Base.
4. *Synergistic operations*: EPIC is not new in the O&G sector. Besides owning and managing the petroleum supply base in Kemaman, EPIC’s other O&G related business is the environmental services operation. Tubex’s pipe threading operations would increase EPIC’s O&G related businesses.
5. *The growing O&G industry*: The increased exploration and production (E&P) activities should increase demand for O&G pipes, thus creating demand for Tubex’s pipe threading services. The continued growth of E&P in Malaysia and the world should provide continuous opportunity for Tubex to grow its earnings base.

Table 2: Environmental services

Services	Remarks
Sludge	The Sludge Profiler for Oil Tanks (SPOT) system is used, quantification replacing the inaccurate manual dipping method. SPOT is based on sonar and can accurately locate, map and quantify the level of sludge in a crude oil tank during service.
Sludge removal	Natuream uses a system that incorporates robotic or manually driven Hydrodozers and a range of purpose build pumping equipment. This will minimise man entry into confined spaces.
Sludge treatment	Natuream’s range of mobile processing equipment will treat sludge, recovering oil and minimise wastage.

Source: EPIC

Marginal earnings impact. This acquisition is expected to be completed in 4Q05, therefore impact on earnings would only surface in FY06. Assuming Tubex makes a 10% net profit growth over its estimated FY05 performance, the additional earnings would add 1.1sen to EPIC’s EPS06. We are maintaining FY05 turnover and net profit of RM82.5m and RM25.2m, respectively.

Valuation and recommendation. We continue to like EPIC for its 1) steady earnings growth from the Kemaman supply base, 2) potential earnings from the sludge management, 3) focused shareholders and management team, 4) strong financial standing and 4) undemanding valuations.

EPIC is trading at PER05 of 11.5X based on EPS05 of 15.5sen. Forecast FY05 dividend yield is an attractive 7%. We arrive at a fair value of RM2.30 after pegging EPS05 to market PER of 15X. Maintain **BUY (52w Hi-Low: RM1.96-RM1.40, FV= RM2.30)**

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Some common terms abbreviated in this report (where they appear):

P = price	PBT/PAT = Profit before tax/Profit after tax	mom= month-on-month
PE/PER = price earnings/ PE ratio	NTA = net tangible asset	yoy = year-on-year
PEG = PE ratio to growth	NAV = net asset value	qoq = quarter-on-quarter
FV = fair value	EBIT= Earnings before interest, tax	ytd = year-to-date
BV = book value	EBITDA= EBIT, depreciation and amortisation	FY/FYE = financial year/ financial year end
EV = enterprise		value CY = calendar year
DCF = discounted cashflow	ROE = return on equity	capex = capital expenditure
FCF = free cashflow	ROA = return on asset	adex = advertising expenditure
CAGR = compounded annual growth rate	ROS = return on shareholders' funds	p.a = per annum
WACC = weighted average cost of capital	EPS = earnings per share	
	DPS = dividend per share	



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