
4. RISK FACTORS

NOTWITHSTANDING THE PROSPECTS OF THE MSB GROUP OUTLINED IN THIS PROSPECTUS, APPLICANTS SHOULD CAREFULLY CONSIDER THE FOLLOWING RISK FACTORS (WHICH MAY NOT BE EXHAUSTIVE) THAT MAY HAVE A SIGNIFICANT IMPACT ON THE FUTURE PERFORMANCE OF THE MSB GROUP, IN ADDITION TO OTHER INFORMATION CONTAINED ELSEWHERE HEREIN, BEFORE APPLYING FOR THE OFFER SHARES.

4.1 NO PRIOR MARKET FOR MSB SHARES

There has been no prior public market for MSB Shares. The Offer Price was agreed upon by MSB and OSK as Adviser, Managing Underwriter and Placement Agent based upon several factors and may not be an indication of the market price of MSB Shares after the Public Offer and Listing. See Section 3.6 of this Prospectus on the basis for the determination of the Offer Price.

There can be no assurance that an active public market in MSB Shares will be developed or be sustained after this Public Offer and Listing, or that the market price of MSB Shares will not decline below the Offer Price.

A number of factors may cause the price of MSB Shares to fluctuate, including (without limitation) sales of substantial amounts of MSB Shares in the public market in the immediate future; announcements of developments relating to MSB's business; fluctuations in MSB's operating results and sales levels; the conditions of the general industry, or the national or world-wide economy; changes in regulation; announcements of new products or product enhancements by the MSB Group and/or its competitors.

4.2 CAPITAL MARKET RISKS

As an investor of MSB, it is to be noted that MSB will be listed on the Main Board of Bursa Malaysia. The performance of Bursa Malaysia is, to a certain extent, dependent on external factors such as the performance of the regional and world bourses and the inflow or outflow of foreign funds. Market sentiments are also largely driven by internal factors such as the economic and political conditions of the country as well as the potential growth of the various sectors of the economy. These factors will invariably contribute to the volatility of trading volumes on Bursa Malaysia, thus adding risk to the market price of MSB Shares.

4.3 BUSINESS RISKS

MSB is subject to certain business risks, such as labour and raw material shortages, increase in costs of labour, utilities and raw materials, changes in general economic, and business and credit conditions. Although the Group seeks to limit these risks through, *inter-alia*, semi-automated operations, conservative management policies, and maintaining long term business relationships with its suppliers and customers, no assurance can be given that any change to these factors will not have material adverse effects on the Group's business.

4.4 ECONOMIC AND POLITICAL CONSIDERATIONS

The Group's business activities are focused mainly in Malaysia. Any adverse development in the economic, political and financial conditions in Malaysia could materially and adversely affect the financial and operational conditions and profitability of the MSB Group. These risks include the risks of an economic downturn, changes in interest rates and unfavourable changes in government policies such as changes in method of taxation and the introduction of new regulations. Whilst the MSB Group will continue to take effective measures such as prudent financial management and efficient operating procedures, there is no assurance that adverse political and economic factors will not materially affect the MSB Group.

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4.5 DEPENDENCE ON THE MANUFACTURING SECTOR

CRC manufactured by MSCRC is mainly used in the manufacturing of steel pipes and tubes, steel furniture, home appliances, electrical appliances, steel drums, automobile bodies, steel strappings and raw material for galvanised and coated steel sheets. As such, the demand for MSCRC's products is mainly dependent on, inter-alia, the prospects of the local manufacturing industry.

In an effort to reduce MSCRC's dependence on the local manufacturing industry, MSCRC has been exploring the possibility of exporting its products to other overseas countries if the prices offered are attractive. In the FYE 31 January 2004, MSCRC exported 7,053 mt of CRC to the People's Republic of China.

However, the exporting of CRC to overseas markets usually involves high freight and transportation charges, in addition to the stiff competition from other foreign CRC manufacturers. As such, it may not be profitable to export its products overseas unless the prices are favourable to MSCRC. There can be no assurance that the prices of CRC in overseas markets will be favourable to MSCRC.

4.6 COMPETITION

To date, there are only two producers of CRC in Malaysia, namely MSCRC and Ornasteel. In 2002, Ornasteel and MSCRC produced an aggregate of 551,000 mt of CRC, which accounted for approximately 44.3% of the total local consumption of 1,244,000 mt. However, the Lion Group plans to establish a cold rolling mill, which is due to begin operations in 2004. The plant will have a capacity of 1.5 million mt.

(Source: MISIF Report 2003)

MSCRC is expected to maintain its market share at its current level as the Lion Group's cold rolling mill is expected to produce only approximately 400,000 mt of CRC per annum during its initial years of operations. To the best of their knowledge, management is not aware of any other CRC plants currently being planned.

Notwithstanding the above, the CRC sector is still highly competitive as it faces competition in the global steel industry. With the initiation of the Common Effective Preferential Tariff scheme under the AFTA, tariff on goods traded within the region, which meet a 40% ASEAN content requirement, will be reduced to 0% - 5% by the 2003 (2006 for Vietnam and 2008 for Laos and Myanmar). This would result in a liberalised market and intensify competition among steel producers in the region. Hence, manufacturers in certain selected industries can easily import cheaper CRC from the other ASEAN countries and other parts of the world.

In order to remain ahead of its competitors, the Group intends to continually improve the quality of its products as well as to increase its focus on pricing its products competitively. Although the MSB Group has taken efforts to maintain its competitiveness, there is still no assurance that it will maintain its market share in the future.

4.7 IMPACT OF AFTA

The AFTA agreement was signed in 1992 between Malaysia, Thailand, Singapore, Indonesia, Philippines and Brunei to promote economic co-operation and increased competitiveness by reducing inter-regional tariffs between member countries. AFTA has resulted in a gradual reduction of trade barriers in ASEAN. Under AFTA, member countries have begun to lower import tariffs, export subsidies and tax relief since the year 2000 and would totally abolish them by 2003. With the initiation of the Common Effective Preferential Tariff scheme under AFTA, tariff on goods traded within the region, which meets a 40% ASEAN content requirement, will be reduced to 0% - 5%. This would result in a liberalised market and intensify competition among steel producers in the region.

4. RISK FACTORS

Although competition among steel producers is expected to intensify under AFTA, the market liberalisation of the steel industry is expected to present opportunities to efficiently-run steel producers to increase their market shares both domestically and regionally if they are able to emerge as low cost producers under the AFTA regime.

MSCRC has been operating under the AFTA regime when the provisions under the AFTA agreement came into effect on 1 January 2003. As at the date of the Prospectus, there has been no material impact on MSCRC's operations. However, there is no assurance that MSCRC's sales, costs and profits will not be affected in the future.

To enhance its competitiveness under the AFTA regime, the MSB Group plans to continually improve the quality of its products as well as to increase its focus on pricing its products competitively. In addition, the MSB Group periodically performs upgrading works on its machinery and undertakes training programmes for its workforce to keep them abreast with current production technologies and technical know-how.

4.8 DEPENDENCE ON KEY PERSONNEL

As in other businesses, the Group believes that its continued success depends significantly on the abilities and continued efforts of its existing Directors, senior management and long service technical support staff, further details of which may be found in Sections 6.2 and 6.4 of this Prospectus.

The loss of any of the key members of the Group including Directors and senior management, could adversely affect the Group's performance. However, with the rigorous on-the-job training extended to the middle management and operations staff as well as strong technical support from various suppliers, coupled with a competitive remuneration scheme, the Group's management has expanded and strengthened over the years. Thus, the Group is confident that with the capabilities of its employees, it would not expect any difficulties in grooming the younger members of the management team to eventually take over from their seniors in the future.

Therefore, every effort has been made by the MSB Group to ensure a smooth transition in the management team. Hence, the Group's future success will also depend upon its ability to retain, as well as to attract new, skilled personnel.

4.9 FUTURE CAPITAL INJECTIONS

The Directors of MSB believe that the net proceeds from the Public Offer, together with cash flow generated from MSB's operations and other existing sources of funds, will be sufficient to meet the projected working capital and other cash requirements.

However, there is no assurance that future events may not cause the MSB Group to seek additional capital sooner. If additional capital is required, there can be no assurance that it will be available, or if available, that it will be on terms satisfactory or favourable to the MSB Group. The issue of additional equity or other convertible securities by MSB may result in the dilution of the interests of the then shareholders of MSB.

4.10 INVESTMENT RISKS

If appropriate opportunities present themselves, whether in Malaysia or elsewhere, the MSB Group may decide to acquire businesses, products or technologies, or enter into joint ventures, alliances or partnerships with third parties, or to expand into other geographical markets.

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There can be no assurance that the MSB Group will be able to successfully identify, negotiate, finance or implement these ventures or investments, to successfully integrate these ventures or investments with its current business and operations, or to benefit from the same. These ventures and investments may also require additional capital, which may or may not be available on terms satisfactory to the MSB Group. However, any venture or investment of such nature will be carefully considered by the Directors of MSB and its subsidiary with due care.

The MSB Group may also from time to time invest in new ventures and products. These investments may not be successful, or may have a delayed gestation period. In this event, MSB may not be able, or may be slow, to recover its investments and/or achieve satisfactory returns. However, any venture or investment of such nature will be carefully considered by the Directors of MSB and its subsidiary with due care.

4.11 CONTINUED CONTROL BY EXISTING SHAREHOLDERS

Upon completion of the Public Offer, the Directors, executive officers and substantial shareholders of MSB will, in the aggregate, beneficially own approximately 52.8% of the issued and paid-up share capital of MSB. As a result, these shareholders, if acting together, will possess voting control over MSB, giving them the ability, amongst others, to elect at least a majority of MSB's Directors and to control the vote on significant corporate transactions.

Nonetheless, MSB has appointed three (3) independent directors as a step towards good corporate governance to ensure that any future transactions involving related parties, if any, are entered into on arms-length terms.

4.12 RELATED PARTY TRANSACTIONS

Certain Directors and substantial shareholders of the MSB Group have interests in companies carrying out similar business activities as the MSB Group. Please refer to **Section 9.3** of this Prospectus for details of disclosure on any potential conflict of interests and factors that would avert any potential conflict of interests.

The MSB Group may continue to enter into business or other transactions with related parties in the future. However, the MSB Group has internal control systems to ensure that the recurrent related party transactions are undertaken on an arm's length basis and on normal commercial terms consistent with the Group's usual business practices and policies, which are no more favourable to the interested parties than those extended to third parties/ public and are not to the detriment of the minority shareholders. These include transacting at the prevailing market rates/prices for the service or product, on the service or product provider's usual commercial terms, and otherwise in accordance with applicable industry norm.

4.13 LITIGATION RISKS

The MSB Group's agreements with customers typically contain provisions designed to limit the Group's exposure to potential product or other liability claims. MSB has not, to date, experienced any material product or other liability claims. However, it is possible that the limitation and/or exclusion of liability provisions in the Group's agreements with customers may not be effective as a result of existing or future laws, or unfavourable judicial decisions.

4.14 PRODUCTION RISKS

MSCRC currently operates a single production line of various independent processes for its products. Consequently, any breakdown of critical machinery along the production line as a result of a disruption in energy supply, fire outbreaks or other emergencies may adversely affect MSCRC's production capabilities. Since the last twelve (12) months, MSCRC has not experienced any breakdown that has severely disrupted its operations.

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Nonetheless, to minimize the risk of any such future breakdown, MSCRC employs a strict preventive maintenance and service procedure for its production line. The production line is checked regularly by MSCRC's trained personnel, while its critical facilities are serviced once every five (5) years by experts from the relevant equipment suppliers.

Additionally, the Group has built a back-up generator that will provide electricity for the operation of the batch annealing furnaces in the plant, the sales and delivery departments as well as the other office operations. The MSB Group has also established a health, safety and security measure for each level of operation that is strictly adhered to by its employees. An appropriate emergency response and back-up plan has also been put in place by management to cater for any accidents and/or emergency situations.

4.15 UNDERWRITING RISKS

Up to 20,002,000 of the Offer Shares are to be underwritten by the Managing Underwriter and the Underwriter mentioned in **Section 1** of this Prospectus. The underwriting commission is payable by the Company at a rate of 1.5% of the offer price of RM1.40 per Share for the Offer Shares made available for the Malaysian Public and any Offer Shares reserved for the Directors, eligible employees and business associates of the MSB Group and the MIG Group that are not subscribed and therefore underwritten by the Managing Underwriter and Underwriter. However, the agreement of the Managing Underwriter and Underwriter to underwrite up to 20,002,000 of the Offer Shares should not be taken as an indication of the merits or assurance of the value of the Offer Shares.

4.16 RELIANCE ON MAJOR RELATIONSHIPS

The raw material currently used in the MSB Group's production is sourced from several main suppliers, namely Megasteel from Malaysia and other HRC producers from Japan. While the Group has established good long-term relationship with its suppliers, there is no assurance that their relationship will continue in the post-Listing period. However, the Company has already identified a list of alternative suppliers from which to source the raw material should the current suppliers fail to honour their obligations. Notwithstanding the foregoing, the Directors of the Company are confident that the long-term relationship that they have nurtured with its suppliers, ranging from 4 to 8 years, will ensure that the Group easily obtains an adequate supply of HRC at competitive prices in the future.

The MSB Group has not entered into any long term contracts to supply to its major customers as it is the norm in the steel industry to negotiate contracts on a quarterly basis. However, the Group has a track record of getting recurrent orders as evidenced by the long-term relationship with its customers. The Group's long standing customer relationships also serves as an endorsement of the quality of its CRC.

4.17 FORWARD LOOKING STATEMENTS

Certain statements in this Prospectus are based on historical data which may not be reflective of the future results, while others are forward-looking in nature which are subject to uncertainties and contingencies. All forward-looking statements are based on estimates and assumptions made by the Directors of MSB, and although believed to be reasonable, are subject to known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements to differ materially from the future results. Although MSB believes that the expectations reflected in such forward-looking statements are reasonable at this time, there can be no assurance that such expectations will prove to have been correct.

The inclusion of the forward-looking statements in the Prospectus should not be regarded that the plans and objectives of the MSB Group will be achieved.

4. RISK FACTORS

4.18 BORROWING RISK

The MSB Group may from time to time obtain credit facilities from banks and financiers to finance its operations and business activities. Interest may be charged on these credit facilities by the banks and financiers. Fluctuations in interest rates may have a material impact on the MSB Group's profitability. These credit facilities may also be subject to terms and conditions which may limit the MSB Group's operating and financial flexibility. Any act or omission by the MSB Group that breaches such terms and conditions may give rise to rights by the banks or financiers to terminate the relevant credit facilities and/or enforce any security granted, in relation to those credit facilities, and which may also cause cross-defaults of other facilities. There can be no assurance that the aforesaid breaches will not have any adverse impact on the MSB Group's operational and financial results.

As at 30 April 2004, the proforma MSB Group's total borrowings amounted to approximately RM65.5 million comprising of trust receipts and bankers acceptance. The MSB Group will be utilising part of the proceeds from the Public Offer for reducing bank borrowings and working capital purposes. The MSB Group is not presently in breach of any such term or condition of any credit facility, and will at all times take all reasonable efforts to observe such terms and conditions.

4.19 FOREIGN EXCHANGE RISK

The MSB Group currently imports approximately 60% of its raw materials from Japan, while, for the FYE 31 January 2004, less than 5% of its production was exported overseas on an irregular basis. These transactions are mainly denominated in foreign currencies mainly in USD. The risk of foreign exchange fluctuations has been reduced since the imposition of a fixed exchange rate for the RM against the USD in September 1998. However, in the event that the fixed exchange rate is lifted or re-pegged to a new rate, the Group may or may not have a greater exposure to foreign currency fluctuations. The Group will, as a mitigating factor, attempt to use various hedging techniques to mitigate this risk. However, there can be no assurance that any future significant fluctuations in exchange rates and financial crisis will not materially or adversely affect the MSB Group's operations.

4.20 CHANGES IN GOVERNMENT REGULATIONS

Changes or additions in the regulatory conditions in Malaysia and the other countries where the MSB Group is currently obtaining its raw materials could materially and adversely affect the financial prospects of the MSB Group. Any withdrawal or reduction of import duty exemption in Malaysia on HRC will increase MSCRC's raw material cost. This higher cost will be passed on to MSCRC's customers as this is the norm in the local steel industry.

However, no assurance can be given that there will be no changes or additions made to rules and regulations in the future to which the Group's operations are governed by and that such changes or additions, if made, will not have an adverse effect on the Group's operations. For further details concerning the government legislation and policies affecting the MSB Group, please refer to **Section 8.5** of this Prospectus.

4. RISK FACTORS

4.21 ADEQUACY OF INSURANCE COVERAGE ON THE GROUP'S ASSETS

The MSB Group is aware of the adverse consequences arising from inadequate insurance coverage that could adversely affect its business operations. In ensuring such risks are reduced to the minimum, the MSB Group reviews and ensures adequate coverage for its assets on a continuous basis. For the MSB Group's operations, all assets such as office equipment, furniture, fittings, machinery and premises are sufficiently insured for fire and other risks. However, there can be no assurance that the insurance coverage would be adequate for the replacement cost of the assets or any consequential loss arising therefrom.

4.22 ENVIRONMENTAL CONCERNS

The Group believes its existing operations are in compliance with the relevant environmental legislation governing activities within Malaysia. Nevertheless, there is a possibility that the Government may change its regulations with regards to environmental matters in future which would require the Group to modify its facilities or incur expenses that could have an adverse effect on the Group's operating results. In the event the relevant environmental regulations in Malaysia are changed, no assurance can be given that the measures taken by the Group to comply with such new regulations will not have a material effect on its operating results. To date, the Group has installed a waste water treatment plant at its plant and is actively implementing treatment, recycling and disposal procedures in line with standards prescribed by the relevant authorities at its plant.

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