

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.3 CASH FLOW STATEMENTS OF PSSB

| | Note | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|--|--------|--------------------|--------------------|--------------------|----------------------|--------------------|
| CASH FLOW FROM/(FOR) OPERATING ACTIVITIES | | | | | | |
| (Loss)/Profit before taxation | | (103,126) | 96,461 | 162,586 | 41,578 | 94,676 |
| Adjustments for:- | | | | | | |
| Allowance for doubtful debts | | - | 1,658 | 2,541 | - | 3,509 |
| Amortisation of prepaid lease payments | | 732 | 734 | 732 | 244 | 244 |
| Bad debts written off | | 16,057 | - | - | - | 49 |
| Depreciation for property, plant and equipment | | 66,950 | 67,713 | 67,930 | 22,573 | 22,856 |
| Equipment written off | | 3,133 | 2,717 | - | - | - |
| Interest expense | | 54,653 | 34,826 | 66,003 | 14,900 | 22,685 |
| Provision for loss from termination of freight contracts | | 34,626 | - | - | - | - |
| Unrealised (gain)/loss on foreign exchange | | (1,030) | (3,265) | 2,470 | - | 2,430 |
| Gain on disposal of property, plant and equipment | | (115) | - | - | - | - |
| Interest income | | - | - | (997) | (27) | (252) |
| Waiver of debts | | - | (65,068) | (87,194) | - | - |
| Writeback of allowance of doubtful debts | | (18,274) | - | - | - | - |
| Operating profit before working capital changes | | 53,606 | 135,776 | 214,071 | 79,268 | 146,197 |
| Decrease/(Increase) in inventories | | 92,132 | (72,127) | (142,539) | (3,565) | (51,185) |
| Decrease/(Increase) in trade and other receivables | | 54,967 | (66,227) | 3,369 | 29,349 | (44,983) |
| (Decrease)/Increase in trade and other payables | | (139,446) | (219,083) | (161,986) | 73,895 | (12,231) |
| Increase/(Decrease) in amount owing to ultimate holding company | | 20,679 | 5,502 | 14,600 | (3,224) | (20,295) |
| Increase/(Decrease) in amount owing to immediate holding company | | 69,251 | 93,374 | 27,173 | (47,281) | 32,050 |
| (Decrease)/Increase in amount owing to related companies | | (44) | (31,633) | 6,073 | (95,051) | 9,996 |
| Decrease in amount owing to related parties | | (13,082) | (43,133) | (11,023) | (3,554) | (5,829) |
| CASH FROM/(FOR) OPERATIONS | | 138,063 | (197,551) | (50,262) | 29,837 | 53,720 |
| Interest paid | | (17,092) | (20,695) | (56,908) | (14,900) | (15,453) |
| NET CASH FROM/(FOR) OPERATING ACTIVITIES | | 120,971 | (218,246) | (107,170) | 14,937 | 38,267 |
| CASH FLOW FOR INVESTING ACTIVITIES | | | | | | |
| Proceeds from disposal of equipment | | 115 | - | - | - | - |
| Purchase of property, plant and equipment | 7.2.35 | (49,237) | (5,144) | (7,759) | (1,620) | (19,912) |
| Interest received | | - | - | 997 | 27 | 252 |
| Repayment from related parties | | 17,406 | - | - | - | - |
| Subscription of subordinated bonds | | - | - | (4,000) | (4,000) | - |
| NET CASH FOR INVESTING ACTIVITIES | | (31,716) | (5,144) | (10,762) | (5,593) | (19,660) |
| BALANCE CARRIED FORWARD | | 89,255 | (223,330) | (117,932) | 9,344 | 18,607 |

- Not audited and is included for comparison purposes only.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.3 CASH FLOW STATEMENTS OF PSSB (CONT'D)

| Note | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|----------------------|--------------------|
| BALANCE BROUGHT FORWARD | 89,255 | (223,390) | (117,932) | 9,344 | 18,607 |
| CASH FLOW (FOR)/FROM FINANCING ACTIVITIES | | | | | |
| Repayment of term loans | - | (56,847) | - | - | - |
| Repayment of Malaysian Government Loan | - | - | - | - | (14,000) |
| Drawdown of murabahah medium term loan | - | 310,000 | - | - | - |
| Drawdown of collateralised loan | - | - | 40,000 | 40,000 | - |
| (Repayment of)/Drawdown of bankers' acceptances | (553) | (3,823) | 125,471 | (347) | 9,474 |
| Repayment of hire purchase and lease obligations | (6,354) | (8,574) | (4,962) | (2,362) | (951) |
| Advances from/(Repayment to) related companies | - | 3,607 | 12,822 | (3,601) | (16,382) |
| (Repayment to)/Advances from related parties | (79,477) | (932) | (31,881) | 3,744 | (759) |
| Advances from/(Repayment to) immediate holding company | 6 | 4 | 8,835 | (3,413) | (19,261) |
| NET CASH (FOR)/FROM FINANCING ACTIVITIES | (86,378) | 243,435 | 150,285 | 34,021 | (41,879) |
| NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS | 2,877 | 20,045 | 32,353 | 43,365 | (23,272) |
| EFFECT OF EXCHANGE RATE CHANGES | - | - | (3,828) | - | - |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF THE FINANCIAL YEAR/PERIOD | (8,300) | (5,423) | 14,622 | 14,622 | 43,147 |
| CASH AND CASH EQUIVALENTS AT END OF THE FINANCIAL YEAR/PERIOD | 7.2.36 (5,423) | 14,622 | 43,147 | 57,987 | 19,875 |

- Not audited and is included for comparison purposes only.

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16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.4 STATEMENTS OF CHANGES IN EQUITY OF PSSB

| | Share capital RM'000 | Share premium RM'000 | Accumulated losses RM'000 | Total RM'000 |
|--|----------------------------|----------------------------|---------------------------------|-----------------|
| Balance at 1.1.2005 | 1,216,181 | 121,618 | (645,944) | 691,855 |
| Prior year adjustment | - | - | (170,000) | (170,000) |
| Balance at 1.1.2005 (Restated) | 1,216,181 | 121,618 | (815,944) | 521,855 |
| Loss for the financial year | - | - | (103,126) | (103,126) |
| Balance at 31.12.2005/ 1.1.2006 | 1,216,181 | 121,618 | (919,070) | 418,729 |
| Profit after taxation for the financial year | - | - | 206,461 | 206,461 |
| Balance at 31.12.2006/ 1.1.2007 | 1,216,181 | 121,618 | (712,609) | 625,190 |
| Profit for the financial year | - | - | 162,586 | 162,586 |
| Balance at 31.12.2007/ 1.1.2008 | 1,216,181 | 121,618 | (550,023) | 787,776 |
| Profit for the financial period | - | - | 94,676 | 94,676 |
| Balance at 30.4.2008 | 1,216,181 | 121,618 | (455,347) | 882,452 |

7.2.5 REVENUE

Revenue represents the invoiced value of goods sold less trade discounts and returns.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.6 (LOSS)/PROFIT BEFORE TAXATION

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|----------------------|--------------------|
| (Loss)/Profit before taxation is arrived at after charging/(crediting):- | | | | | |
| Allowance for doubtful debts | - | 1,658 | 2,541 | - | 3,509 |
| Amortisation of prepaid lease payments | 732 | 734 | 732 | 244 | 244 |
| Audit fee | 100 | 150 | 150 | - | - |
| Bad debts written off | 16,057 | - | - | - | 49 |
| Depreciation of property, plant and equipment | 66,950 | 67,713 | 67,930 | 22,573 | 22,856 |
| Directors' fee | - | - | 2,167 | - | 1,006 |
| Directors' non-fee emoluments | - | 600 | 1,623 | - | 1,014 |
| Equipment written off | 3,133 | 2,717 | - | - | - |
| Interest expense | | | | | |
| - bankers' acceptances | 10,738 | 14,563 | 10,724 | 1,203 | 5,732 |
| - bank overdraft | 691 | 625 | 340 | 122 | 109 |
| - collateralised obligations | - | - | 2,625 | 1,004 | 945 |
| - hire purchase | 1,245 | 203 | (68) | 36 | 62 |
| - holding company | - | 9,049 | 22,687 | 2,384 | 6,598 |
| - medium term loan | - | 6,712 | 26,850 | 8,950 | 8,950 |
| - others | 33,814 | 3,674 | 2,845 | 1,201 | 289 |
| - term loans | 8,165 | - | - | - | - |
| Provision for loss from termination of freight contracts | 34,626 | - | - | - | - |
| Rental of equipment | 1,748 | 1,982 | 927 | 350 | 295 |
| Staff costs | 19,750 | 34,353 | 48,907 | 14,899 | 18,364 |
| Gain on disposal of property, plant and equipment | (115) | - | - | - | - |
| (Gain)/Loss on foreign exchange | | | | | |
| - realised | (816) | (3,040) | (13,596) | 191 | (6,082) |
| - unrealised | (1,030) | (3,265) | 2,470 | - | 2,430 |
| Interest income | - | - | (997) | (27) | (252) |
| Rental income | (874) | (457) | (224) | - | (74) |
| Waiver of debts | - | (65,068) | (87,194) | - | - |
| Writeback of allowance for doubtful debts | (18,274) | - | - | - | - |

- Not audited and is included for comparison purposes only.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.7 INCOME TAX EXPENSE

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|----------------------|--------------------|
| Deferred tax asset recognised during the financial year/period (Note 7.2.12) | - | (110,000) | - | - | - |
| (Loss)/Profit before taxation | (103,126) | 96,461 | 162,586 | 41,578 | 94,676 |
| Tax at the statutory tax rates | (28,875) | 27,010 | 43,898 | 11,226 | 24,616 |
| Tax effects of:- | | | | | |
| Non-taxable gains | (5,117) | - | - | - | - |
| Non-deductible expenses | 20,249 | 1,230 | 1,177 | 115 | 365 |
| Deferred tax assets not recognised during the financial year/period | 13,743 | - | - | - | - |
| Utilisation of deferred tax assets not recognised in prior year | - | (28,240) | (45,075) | (11,341) | (24,981) |
| Deferred tax asset recognised in the financial year/period | - | (110,000) | - | - | - |
| | - | (110,000) | - | - | - |

No deferred tax asset is recognised in respect of the following item:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|-----------------------|--------------------|--------------------|--------------------|----------------------|--------------------|
| Unutilised tax losses | 1,689,000 | 1,181,000 | 1,014,000 | 1,139,000 | 902,000 |

- Not audited and is included for comparison purposes only.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.8 PROPERTY, PLANT AND EQUIPMENT

| | At 1.1.2005 RM'000 | Additions RM'000 | Transfer RM'001 | Written off RM'000 | Depreciation charge RM'000 | At 31.12.2005 RM'000 |
|---|-----------------------|---------------------|--------------------|-----------------------|----------------------------------|-------------------------|
| Net Book Value | | | | | | |
| Buildings | 27,600 | 1,095 | - | - | (878) | 27,817 |
| Land improvements and infrastructure | 11,220 | - | - | - | (353) | 10,867 |
| Plant and machinery | 1,516,293 | 39,171 | 710 | - | (63,182) | 1,492,992 |
| Motor vehicles | 5,810 | 409 | - | - | (1,749) | 4,470 |
| Electrical installations, furniture, fittings and office equipment | 2,773 | 175 | - | - | (776) | 2,172 |
| Renovation | - | 1,739 | - | - | (12) | 1,727 |
| Capital work-in-progress | 12,400 | 7,062 | (710) | (3,133) | - | 15,619 |
| | 1,576,096 | 49,651 | - | (3,133) | (66,950) | 1,555,664 |

| | At 1.1.2006 RM'000 | Additions RM'000 | Disposal RM'000 | Written off RM'000 | Depreciation charge RM'000 | At 31.12.2006 RM'000 |
|---|-----------------------|---------------------|--------------------|-----------------------|----------------------------------|-------------------------|
| Net Book Value | | | | | | |
| Buildings | 27,817 | - | - | (115) | (928) | 26,774 |
| Land improvements and infrastructure | 10,867 | - | - | - | (363) | 10,504 |
| Plant and machinery | 1,492,992 | 3,739 | - | (2,433) | (64,108) | 1,430,190 |
| Motor vehicles | 4,470 | 330 | - | (98) | (1,594) | 3,108 |
| Electrical installations, furniture, fittings and office equipment | 2,172 | 586 | (6) | (71) | (678) | 2,003 |
| Renovation | 1,727 | 487 | - | - | (42) | 2,172 |
| Capital work-in-progress | 15,619 | 2 | - | - | - | 15,621 |
| | 1,555,664 | 5,144 | (6) | (2,717) | (67,713) | 1,490,372 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.8 PROPERTY, PLANT AND EQUIPMENT (CONT'D)

| | At 1.1.2007 RM'000 | Additions RM'000 | Depreciation charge RM'000 | At 31.12.2007 RM'000 |
|---|-----------------------|---------------------|----------------------------------|-------------------------|
| Net Book Value | | | | |
| Buildings | 26,774 | - | (958) | 25,816 |
| Land improvements and infrastructure | 10,504 | - | (376) | 10,128 |
| Plant and machinery | 1,430,190 | 4,820 | (64,258) | 1,370,752 |
| Motor vehicles | 3,108 | 3,059 | (1,640) | 4,527 |
| Electrical installations, furniture, fittings and office equipment | 2,003 | 219 | (650) | 1,572 |
| Renovation | 2,172 | 874 | (48) | 2,998 |
| Capital work-in-progress | 15,621 | 4,593 | - | 20,214 |
| | 1,490,372 | 13,565 | (67,930) | 1,436,007 |

| | At 1.1.2008 RM'000 | Additions RM'000 | Transfer RM'000 | Depreciation charge RM'000 | At 30.4.2008 RM'000 |
|---|-----------------------|---------------------|--------------------|----------------------------------|------------------------|
| Net Book Value | | | | | |
| Buildings | 25,816 | 1,421 | - | (324) | 26,913 |
| Land improvements and infrastructure | 10,128 | - | - | (127) | 10,001 |
| Plant and machinery | 1,370,752 | 3,282 | 31,947 | (21,472) | 1,384,509 |
| Motor vehicles | 4,527 | 1,623 | - | (719) | 5,431 |
| Electrical installations, furniture, fittings and office equipment | 1,572 | 62 | - | (193) | 1,441 |
| Renovation | 2,998 | - | - | (21) | 2,977 |
| Capital work-in-progress | 20,214 | 13,677 | (31,947) | - | 1,944 |
| | 1,436,007 | 20,065 | - | (22,856) | 1,433,216 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.8 PROPERTY, PLANT AND EQUIPMENT (CONT'D)

| | At cost RM'000 | Accumulated impairment RM'000 | Accumulated depreciation RM'000 | Net book value RM'000 |
|---|-------------------|-------------------------------------|---------------------------------------|-----------------------------|
| At 31.12.2005 | | | | |
| Buildings | 120,203 | (63,126) | (29,260) | 27,817 |
| Land improvements and infrastructure | 114,560 | (76,083) | (27,610) | 10,867 |
| Plant and machinery | 2,494,111 | (263,353) | (737,766) | 1,492,992 |
| Motor vehicles | 47,373 | - | (42,903) | 4,470 |
| Electrical installations, furniture, fittings and office equipment | 42,519 | - | (40,347) | 2,172 |
| Renovation | 1,739 | - | (12) | 1,727 |
| Capital work-in-progress | 15,619 | - | - | 15,619 |
| | 2,836,124 | (402,562) | (877,898) | 1,555,664 |
| At 31.12.2006 | | | | |
| Buildings | 120,234 | (63,126) | (30,334) | 26,774 |
| Land improvements and infrastructure | 114,560 | (76,083) | (27,973) | 10,504 |
| Plant and machinery | 2,497,850 | (263,353) | (804,307) | 1,430,190 |
| Motor vehicles | 47,703 | - | (44,595) | 3,108 |
| Electrical installations, furniture, fittings and office equipment | 43,081 | - | (41,078) | 2,003 |
| Renovation | 2,226 | - | (54) | 2,172 |
| Capital work-in-progress | 15,621 | - | - | 15,621 |
| | 2,841,275 | (402,562) | (948,341) | 1,490,372 |
| At 31.12.2007 | | | | |
| Buildings | 120,234 | (63,126) | (31,292) | 25,816 |
| Land improvements and infrastructure | 114,560 | (76,083) | (28,349) | 10,128 |
| Plant and machinery | 2,502,670 | (263,353) | (868,565) | 1,370,752 |
| Motor vehicles | 50,762 | - | (46,235) | 4,527 |
| Electrical installations, furniture, fittings and office equipment | 43,300 | - | (41,728) | 1,572 |
| Renovation | 3,100 | - | (102) | 2,998 |
| Capital work-in-progress | 20,214 | - | - | 20,214 |
| | 2,854,840 | (402,562) | (1,016,271) | 1,436,007 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.8 PROPERTY, PLANT AND EQUIPMENT (CONT'D)

| | At cost RM'000 | Accumulated impairment RM'000 | Accumulated depreciation RM'000 | Net book value RM'000 |
|---|-------------------|-------------------------------------|---------------------------------------|-----------------------------|
| At 30.4.2008 | | | | |
| Buildings | 121,655 | (63,126) | (31,616) | 26,913 |
| Land improvements and infrastructure | 114,560 | (76,083) | (28,476) | 10,001 |
| Plant and machinery | 2,537,899 | (263,353) | (890,037) | 1,384,509 |
| Motor vehicles | 52,385 | - | (46,954) | 5,431 |
| Electrical installations, furniture, fittings and office equipment | 43,362 | - | (41,921) | 1,441 |
| Renovation | 3,100 | - | (123) | 2,977 |
| Capital work-in-progress | 1,944 | - | - | 1,944 |
| | <u>2,874,905</u> | <u>(402,562)</u> | <u>(1,039,127)</u> | <u>1,433,216</u> |

The property, plant and equipment at the balance sheet date were charged to financial institutions as security for banking facilities granted to PSSB as disclosed in Paragraphs 7.2.24 and 7.2.31.

Included in property, plant and equipment of PSSB are the following assets acquired under hire purchase terms:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--------------------------|--------------------|--------------------|--------------------|--------------------|
| Capital work-in-progress | - | - | 8,911 | - |
| Motor vehicles | 403 | 347 | 609 | 726 |
| Plant and equipment | 226 | 226 | - | 8,086 |
| | <u>629</u> | <u>573</u> | <u>9,520</u> | <u>8,812</u> |

Motor vehicles with the following net book values were held in trust by a director and a shareholder at the balance sheet date:

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------|--------------------|--------------------|--------------------|--------------------|
| A director | 92 | 55 | 18 | 6 |
| A shareholders | 294 | 233 | 173 | 151 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.9 PREPAID LEASE PAYMENTS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| At cost | 40,796 | 40,796 | 40,796 | 40,796 |
| Accumulated amortisation | (11,138) | (11,872) | (12,604) | (12,848) |
| | <u>29,658</u> | <u>28,924</u> | <u>28,192</u> | <u>27,948</u> |
| Accumulated amortisation At 1.1.2005/2006/2007/2008 | 10,406 | 11,138 | 11,872 | 12,604 |
| Amortisation for the financial year/period | 732 | 734 | 732 | 244 |
| At 31.12.2005/2006/2007/30.4.2008 | <u>11,138</u> | <u>11,872</u> | <u>12,604</u> | <u>12,848</u> |

Prepaid lease payments which represent leasehold land have been pledged as security for banking facilities granted to PSSB as disclosed in Paragraphs 7.2.24 and 7.2.31.

7.2.10 INVESTMENT IN AN ASSOCIATE

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--------------------------|--------------------|--------------------|--------------------|--------------------|
| Unquoted shares, at cost | 510 | 510 | - | - |
| Impairment loss | (510) | (510) | - | - |
| | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |

Details of the associate, which is incorporated in Malaysia, are as follows:-

| Name of Company | Effective Equity Interest | | | | Principal Activities |
|--------------------------------|---------------------------|-----------------|-----------------|----------------|----------------------|
| | 31.12.2005 % | 31.12.2006 % | 31.12.2007 % | 30.4.2008 % | |
| South Vest Corporation Sdn Bhd | 48.6 | 48.6 | - | - | Dormant. |

On 18 October 2007, the associate was wound up. Accordingly, the investment in the associate was written off in FYE 2007.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.11 OTHER INVESTMENT

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|-----------------------------|--------------------|--------------------|--------------------|--------------------|
| Subordinated bonds, at cost | - | - | 4,000 | 4,000 |

The subordinated bonds are related to the collateralised loan disclosed in Paragraph 7.2.25 below. The collateralised loan was provided by a syndication of lenders and one of the conditions is that the borrowers (PSSB being one of them) are required to participate in the pool of lenders, limited to 10% of the amount borrowed.

7.2.12 DEFERRED TAX ASSET

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| At 1.1.2005/2006/2007/2008 | - | - | 110,000 | 110,000 |
| Recognised in the financial year/period (Note 7.2.7) | - | 110,000 | - | - |
| At 31.12.2005/2006/2007/30.4.2008 | - | 110,000 | 110,000 | 110,000 |

The deferred tax asset represents the tax benefits from the expected utilisation of the unutilised tax losses in the foreseeable future, based on the prevailing applicable tax rate.

7.2.13 INVENTORIES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|------------------------------------|--------------------|--------------------|--------------------|--------------------|
| At cost:- | | | | |
| Raw materials | 29,220 | 105,381 | 175,310 | 235,075 |
| Engineering spares and consumables | 95,205 | 73,241 | 112,509 | 125,037 |
| Finished goods | 48,361 | 66,291 | 65,322 | 47,912 |
| | 172,786 | 244,913 | 353,141 | 408,024 |
| At net realisable value:- | | | | |
| Raw materials | - | - | 34,311 | 30,613 |
| | 172,786 | 244,913 | 387,452 | 438,637 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.14 TRADE RECEIVABLES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| Trade receivables | 8,507 | 40,230 | 17,200 | 48,522 |
| Allowance for doubtful debts | (3,283) | (4,489) | (5,519) | (9,028) |
| | <u>5,224</u> | <u>35,741</u> | <u>11,681</u> | <u>39,494</u> |
| Allowance for doubtful debts | | | | |
| At 1.1.2005/2006/2007/2008 | 10,048 | 3,283 | 4,489 | 5,519 |
| Addition for the financial year/period | - | 1,206 | 2,236 | 3,509 |
| Writeback during the financial year/period | (6,765) | - | - | - |
| Write-off during the financial year/period | - | - | (1,206) | - |
| At 31.12.2005/2006/2007/30.4.2008 | <u>3,283</u> | <u>4,489</u> | <u>5,519</u> | <u>9,028</u> |

PSSB's normal trade credit terms range from cash terms to 14 days. Other credit terms are assessed and approved on a case-by-case basis.

The foreign currency exposure profile of trade receivables is as follows:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------------|--------------------|--------------------|--------------------|--------------------|
| United States Dollar | 2,213 | 9,178 | 545 | 34,550 |

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16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.15 OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| Gross receivables | 11,088 | 37,676 | 55,748 | 67,170 |
| Allowance for doubtful debts | (5,317) | (5,769) | (5,622) | (5,317) |
| | 5,771 | 31,907 | 50,126 | 61,853 |
| Deposits and prepayments | 1,252 | 5,680 | 3,877 | 5,780 |
| | 7,023 | 37,587 | 54,003 | 67,633 |
| Allowance for doubtful debts At 1.1.2005/2006/2007/2008 | 5,317 | 5,317 | 5,769 | 5,622 |
| Addition for the financial year/period | - | 452 | 305 | - |
| Write-off during the financial year/period | - | - | (452) | (305) |
| At 31.12.2005/2006/2007/30.4.2008 | 5,317 | 5,769 | 5,622 | 5,317 |

Included in other receivables of PSSB are the following:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| Advances to suppliers in respect of raw materials purchased | 1,252 | 5,680 | 43,119 | 55,185 |

Included in deposits of PSSB are amounts of RM975,000 and RM505,000 in FYE 2006 and FYE 2005 respectively pledged to licensed banks for credit facilities granted to PSSB.

7.2.16 AMOUNT OWING BY AN ASSOCIATE

The non-trade advance is unsecured, interest-free and receivable on demand. The advance is to be settled in cash.

7.2.17 AMOUNT OWING BY/(TO) RELATED COMPANIES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------------|--------------------|--------------------|--------------------|--------------------|
| Amount owing by: | | | | |
| - trade | 11,097 | 45,385 | 45,376 | 34,916 |
| - non-trade advances | - | (3,601) | (16,423) | (41) |
| | 11,097 | 41,784 | 28,953 | 34,875 |
| Amount owing to: | | | | |
| - trade | (1,454) | (4,109) | (10,173) | (9,709) |
| - non-trade advances | (245) | (245) | (245) | (245) |
| | (1,699) | (4,354) | (10,418) | (9,954) |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.17 AMOUNT OWING BY/(TO) RELATED COMPANIES (CONT'D)

The trade amounts owing are subject to normal credit terms. The amounts owing are unsecured and to be settled in cash.

The non-trade advances are unsecured, interest-free and receivable/repayable on demand. The advances are to be settled in cash.

7.2.18 AMOUNT OWING BY/(TO) RELATED PARTIES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| Gross amount owing by related parties | 17,981 | 26,531 | 14,544 | 21,136 |
| Allowance for doubtful debts | (13,616) | (13,616) | (13,616) | (13,616) |
| | 4,365 | 12,915 | 928 | 7,520 |
| Allowance for doubtful debts: At 1.1.2005/2006/2007/2008 | 25,125 | 13,616 | 13,616 | 13,616 |
| Writeback during the financial year/period | (11,509) | - | - | - |
| At 31.12.2005/2006/2007/30.4.2008 | 13,616 | 13,616 | 13,616 | 13,616 |
| Amount owing by: - trade | 4,365 | 12,915 | 928 | 7,520 |
| Amount owing to: - trade | (62,846) | (37,296) | (14,286) | (15,049) |
| - non-trade advances | (39,464) | (36,614) | (2,999) | (2,240) |
| | (102,310) | (73,910) | (17,285) | (17,289) |

The trade amounts owing are subject to normal credit terms. The amounts owing are unsecured and to be settled in cash.

The non-trade advances are unsecured, interest-free and receivable/repayable on demand. The advances are to be settled in cash.

7.2.19 FIXED DEPOSIT WITH A FINANCIAL INSTITUTION

The fixed deposit has been pledged for the Murabahah Medium Term Loan issued by PSSB.

The interest rate per annum of the fixed deposit in FYE 2007 and FPE 2008 was 3.0%.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.20 CASH AND BANK BALANCES

The foreign currency exposure profile of cash and bank balances is as follows:-

| | RM'000 | RM'000 | RM'000 | RM'000 |
|----------------------|--------|--------|--------|--------|
| United States Dollar | - | - | 27,368 | 11,184 |

7.2.21 SHARE CAPITAL

| | FYE 2005 (('000)) | FYE 2006 (('000)) | FYE 2007 (('000)) | FPE 2008 (('000)) | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|----------------------|----------------------|----------------------|----------------------|--------------------|--------------------|--------------------|--------------------|
| AUTHORISED:- | | | | | | | | |
| Ordinary shares of RM1 each | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 |
| 5% cumulative convertible preference shares of RM1 each | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 |
| | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> | <u>2,000,000</u> |
| ISSUED AND FULLY PAID UP:- | | | | | | | | |
| Ordinary shares of RM1 each | 1,216,181 | 1,216,181 | 1,216,131 | 1,216,181 | 1,216,181 | 1,216,181 | 1,216,181 | 1,216,181 |

7.2.22 SHARE PREMIUM

The share premium is not distributable by way of dividends and can be utilised only in the manner as set out in Section 60(3) of the Companies Act, 1965.

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16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.23 LONG-TERM BORROWINGS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| Hire purchase payables (Note 7.2.32) | 379 | 1,812 | 4,524 | 4,017 |
| Loan from a related party | (a) 106,816 | 106,816 | 85,746 | 85,746 |
| Loan from the Malaysian Government | (b) 148,614 | 148,614 | 118,891 | 104,891 |
| | 255,809 | 257,242 | 209,161 | 194,654 |
| (a) Loan from a related party | | | | |
| Current portion: | | | | |
| Repayable within one year (Note 7.2.31) | - | - | 21,070 | 21,070 |
| Non-current portion | | | | |
| Repayable between one to two years | - | 21,070 | 21,070 | 21,070 |
| Repayable between two to five years | 106,816 | 85,746 | 64,676 | 64,676 |
| | 106,816 | 106,816 | 85,746 | 85,746 |
| | 106,816 | 106,816 | 106,816 | 106,816 |

The related party is Equal Concept Sdn. Bhd. ("ECSB"), a subsidiary of Maju Holdings Sdn. Bhd.. The loan is unsecured, interest-free and is repayable in five equal installments of approximately RM21.1 million, commencing on or before 4 September 2008.

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| (b) Loan from the Malaysian Government | | | | |
| Current portion: | | | | |
| Repayable within one year (Note 7.2.31) | - | - | 29,723 | 29,723 |
| Non-current portion | | | | |
| Repayable between one to two years | - | 29,723 | 29,723 | 29,723 |
| Repayable between two to five years | 148,614 | 118,891 | 89,168 | 75,168 |
| | 148,614 | 148,614 | 118,891 | 104,891 |
| | 148,614 | 148,614 | 148,614 | 134,614 |

The loan from the Malaysian Government is unsecured and interest-free.

The loan is repayable as follows:

- (i) 2 years moratorium from having to repay any outstanding amount until January 2008; and
- (ii) upon expiry of the 2 years moratorium period, RM50 million will be paid to the Malaysian Government annually for the next 5 years towards the full settlement of the advances.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.24 MURABAHAH MEDIUM TERM LOAN

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|-------------------------------------|--------------------|--------------------|--------------------|--------------------|
| Repayable between one to two years | - | - | 50,000 | 50,000 |
| Repayable between two to five years | - | 150,000 | 150,000 | 150,000 |
| Repayable after five years | - | 160,000 | 110,000 | 110,000 |
| | - | 310,000 | 310,000 | 310,000 |

On 25 September 2006, PSSB issued a RM310 million 9-year Medium Term Loan for the purpose of refinancing existing banking facilities, debts settlement to Tenaga National Berhad and for its working capital.

The principal terms of Medium Term Loan are as follows:-

(a) *Maturity and profit rate*

| Tranche | Tenure (Years) | RM'million | Profit rate (%) |
|---------|-------------------|------------|--------------------|
| 1 | 3 | 50 | 7.6 |
| 2 | 4 | 50 | 8.1 |
| 3 | 5 | 50 | 8.5 |
| 4 | 6 | 50 | 8.9 |
| 5 | 7 | 50 | 9.2 |
| 6 | 8 | 40 | 9.4 |
| 7 | 9 | 20 | 9.7 |
| | | <u>310</u> | |

Profit shall be payable semi-annually commencing 6 months from date of first issue until final maturity of the respective tranches.

(b) *Security*

- (i) Debenture creating first fixed and floating charge on all assets, present and future of the PSSB;
- (ii) First legal charge over the PSSB's leasehold land together with the plants erected thereon; and
- (iii) Fixed charge over all proceeds in the Designated Accounts, comprising the Escrow Account and Finance Service Reserve Account.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.24 MURABAHAH MEDIUM TERM LOAN (CONT'D)

(c) *Basis of Arrangement*

On a "bought deal" basis.

(d) *Issue and Redemption*

The Medium Term Loan was issued at par and redeemable at par on the respective maturities.

7.2.25 COLLATERALISED LOAN

| | FYE 2005 | FYE 2006 | FYE 2007 | FPE 2008 |
|-------------------------|----------|----------|----------|----------|
| Effective interest rate | N/A | N/A | 7.1% | 7.1% |

The unsecured collateralised loan is repayable on 18 January 2012.

7.2.26 TRADE PAYABLES

The normal trade credit terms granted to PSSB range from 30 to 90 days.

The foreign currency exposure profile of trade payables is as follows:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------------|--------------------|--------------------|--------------------|--------------------|
| Euro | 1,121 | 595 | 1,135 | 2,120 |
| United States Dollar | 183,223 | 43,705 | 10,355 | 9,035 |
| Swiss Franc | 209 | 176 | 176 | 392 |
| Japanese Yen | 947 | 13,927 | 1,092 | 4,222 |
| Others | 17 | 2,751 | 1,387 | 1,358 |

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.27 OTHER PAYABLES AND ACCRUALS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--------------------------|--------------------|--------------------|--------------------|--------------------|
| Accrued interest | 13,370 | 11,329 | 9,871 | 17,103 |
| Trade advance collection | 43,613 | 854 | 1,803 | 7,104 |
| Other payables | 47,743 | 40,753 | 13,180 | 10,681 |
| Other accruals | 12,097 | 10,213 | 3,943 | 3,971 |
| | 116,823 | 63,149 | 28,797 | 38,859 |

7.2.28 AMOUNT OWING TO ULTIMATE HOLDING COMPANY

The trade amount owing is subject to normal credit terms. The amount owing is unsecured and to be settled in cash.

7.2.29 AMOUNT OWING TO IMMEDIATE HOLDING COMPANY

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------------------|--------------------|--------------------|--------------------|--------------------|
| Amount owing by: | | | | |
| Trade balances | 5,436 | 61,485 | 86,672 | 20,834 |
| Non-trade balances | 6 | - | 11 | 11 |
| | 5,442 | 61,485 | 86,683 | 20,845 |
| Amount owing to: | | | | |
| Trade balances | (74,699) | (230,337) | (281,319) | (249,961) |
| Non-trade balances | - | 10 | (19,261) | - |
| | (74,699) | (230,327) | (300,580) | (249,961) |
| | (69,257) | (168,842) | (213,897) | (229,116) |
| Amount subject to interest | - | 204,706 | 223,385 | 174,961 |
| Effective interest rate | - | 8.0% | 8.4% | 8.4% |

The foreign currency exposure profile of the amount owing to immediate holding company is as follows:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|----------------------|--------------------|--------------------|--------------------|--------------------|
| United States Dollar | - | - | 72,262 | 51,634 |

The trade amount owing is subject to normal credit terms. The amount owing is unsecured and to be settled in cash.

The non-trade advances are unsecured and repayable on demand. The advances are to be settled in cash.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.30 PROVISION

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| At 1.1.2005/2006/2007/2008 | - | 34,826 | 10,943 | - |
| Addition for the financial year/period | 34,626 | - | - | - |
| Utilised for the financial year/period | - | (23,683) | (10,943) | - |
| At 31.12.2005/2006/2007/30.4.2008 | 34,626 | 10,943 | - | - |

7.2.31 SHORT-TERM BORROWINGS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| Bankers' acceptances | 149,197 | 145,374 | 270,845 | 280,319 |
| Loan from a related party (Note 7.2.23) | - | - | 21,070 | 21,070 |
| Loan from the Malaysian Government (Note 7.2.23) | - | - | 29,723 | 29,723 |
| Hire purchase payables (Note 7.2.32) | 13,465 | 3,769 | 2,815 | 2,524 |
| Lease payable (Note 7.2.33) | 1,225 | 914 | - | - |
| Term loans | 56,847 | - | - | - |
| | 220,734 | 150,057 | 324,453 | 333,636 |
| Weighted average effective interest rate:- | | | | |
| Bankers' acceptances | 3.1% | 5.0% | 6.2% | 5.5% |
| Term Loans | 6.4% | N/A | N/A | N/A |

The bankers' acceptances are secured by way of:-

- (i) fixed and floating charges over all of PSSB's property, plant and equipment;
- (ii) a debenture on all present and future assets of PSSB;
- (iii) a first legal charge over PSSB's leasehold land; and
- (iv) a corporate guarantee from Kinsteel Bhd.

The term loans are secured by way of:-

- (i) fixed charges over PSSB's land and plant in Kemaman;
- (ii) third party fixed charges over 9 units of leasehold 1 ½ storey semi-detached factory lots and a unit of 1 ½ storey factory lot;
- (iii) a debenture on all present and future assets of PSSB;
- (iv) the joint and several guarantee by certain directors of PSSB; and
- (v) a corporate guarantee by the Maju Holdings Sdn. Bhd..

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.32 HIRE PURCHASE PAYABLES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| Minimum lease and hire purchase payables: | | | | |
| - not later than one year | 14,283 | 4,056 | 3,166 | 2,836 |
| - later than one year and not later than five years | 432 | 1,949 | 5,074 | 4,502 |
| | 14,715 | 6,005 | 8,240 | 7,338 |
| Future finance charges | (871) | (424) | (901) | (797) |
| Present value of lease and hire purchase payables | 13,844 | 5,581 | 7,339 | 6,541 |
| Current: | | | | |
| - not later than one year (Note 7.2.31) | 13,465 | 3,769 | 2,815 | 2,524 |
| Non-current: | | | | |
| - later than one year and not later than five years (Note 7.2.23) | 379 | 1,812 | 4,524 | 4,017 |
| | 13,844 | 5,581 | 7,339 | 6,541 |
| Effective interest rates | 4.90% - 17.27% | 4.90% - 17.27% | 4.10% - 17.27% | 4.50% - 15.86% |

7.2.33 LEASE PAYABLES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---------------------------------------|--------------------|--------------------|--------------------|--------------------|
| Payable within one year (Note 7.2.31) | 1,225 | 914 | - | - |
| Effective interest rates | 9.95% - 13.50% | 9.95% - 13.50% | - | - |

7.2.34 BANK OVERDRAFT

| | FYE 2005 | FYE 2006 | FYE 2007 | FPE 2008 |
|--------------------------------|----------|----------|----------|----------|
| Weighted average interest rate | 8.75% | 8.75% | 8.04% | 8.19% |

The bank overdraft is secured in the same manner as the bankers' acceptances disclosed in Paragraph 7.2.31.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.35 PURCHASE OF PROPERTY, PLANT AND EQUIPMENT

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|----------------------|--------------------|
| Cost of property, plant and equipment purchased | 49,651 | 5,144 | 13,565 | 1,620 | 20,065 |
| Amount financed through hire purchase | (414) | - | (5,806) | - | (153) |
| Cash disbursed for purchase of property, plant and equipment | 49,237 | 5,144 | 7,759 | 1,620 | 19,912 |

- Not audited and is included for comparison purposes only.

7.2.36 CASH AND CASH EQUIVALENTS

For the purpose of the cash flow statements, cash and cash equivalents comprise the following:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|----------------------|--------------------|
| Fixed deposit with a financial institution | - | - | 13,500 | 13,425 | 13,275 |
| Cash and bank balances | 944 | 18,578 | 31,281 | 75,532 | 11,646 |
| Bank overdrafts | (6,367) | (3,956) | (1,634) | (30,970) | (5,046) |
| | (5,423) | 14,622 | 43,147 | 57,987 | 19,875 |

- Not audited and is included for comparison purposes only.

Included in cash and bank balances were amounts of RM13.3 million and RM13.4 million in FPE 2007 and FYE 2006 respectively which were charged to the Murabahah Medium Term Loan.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.37 SIGNIFICANT RELATED COMPANY TRANSACTIONS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|----------------------|--------------------|
| Sales to immediate holding company | 251,737 | 432,701 | 838,680 | 221,137 | 423,830 |
| Sales to related companies | 11,097 | 94,879 | 350,214 | 94,145 | 126,995 |
| Purchases from ultimate holding company | 80,702 | 124,466 | 279,674 | 55,220 | 111,788 |
| Purchases from immediate holding company | 36,695 | 170,016 | 126,966 | 5,130 | - |
| Purchases to related companies | 4,960 | 15,759 | 24,001 | 6,015 | 6,909 |
| Interest charges payable to holding company | - | 9,049 | 22,687 | 2,384 | 6,598 |

- Not audited and is included for comparison purposes only.

7.2.38 SIGNIFICANT RELATED PARTY TRANSACTIONS

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2007 # RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|----------------------|--------------------|
| Sales to related parties | 205,730 | 50,653 | 10,273 | - | 12,732 |
| Purchases from related parties | 123,091 | 41,260 | 43,582 | 30,706 | 8,071 |
| Purchases of plant and equipment from related parties | 42,765 | - | - | - | - |
| Transportation charged by related parties | 8,316 | 9,401 | - | - | - |
| Services charged by related parties | 6,698 | - | 21,161 | 4,298 | 3,447 |
| Rental charged by related parties | - | 495 | - | - | 108 |
| Rental income from a related party | 282 | 150 | - | - | - |
| Catering services charged by a related party | - | - | 1,529 | - | 748 |

- Not audited and is included for comparison purposes only.

A related party refers to a company in which certain directors have substantial financial interests.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.39 CAPITAL COMMITMENT

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|-----------------------------------|--------------------|--------------------|--------------------|--------------------|
| Plant and equipment | | | | |
| - Approved and contracted for | 15,087 | 15,087 | 27,466 | 14,188 |
| - Approved and not contracted for | - | - | - | 1,500 |
| | <u>15,087</u> | <u>15,087</u> | <u>27,466</u> | <u>15,688</u> |

7.2.40 CONTINGENT LIABILITIES

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---|--------------------|--------------------|--------------------|--------------------|
| Claim by related parties against PSSB # | - | 7,265 | 8,672 | 6,690 |
| Claim by a third party against PSSB * | - | - | 36,080 | 36,080 |
| | <u>-</u> | <u>7,265</u> | <u>44,752</u> | <u>42,770</u> |

- A claim was made by related parties in FYE 2006, FYE 2007 and FPE 2008 on goods transferred to PSSB. PSSB does not agree with the amount claimed. To date, no legal action has been instituted by the related parties.

* - A claim has been filed in the Court by a customer against PSSB for alleged breach of contract. PSSB has made a counterclaim against this customer for the recovery of an amount of approximately RM3.3 million for goods sold. The case management has been further adjourned to 25 July 2008. Based on legal advice, the directors are of the opinion that the claim against PSSB will not succeed.

16. ACCOUNTANTS' REPORT (Cont'd)



7. AUDITED FINANCIAL STATEMENTS (CONT'D)

7.2 PSSB (CONT'D)

7.2.41 FAIR VALUES OF FINANCIAL INSTRUMENTS

Fair value is defined as the amount at which the financial instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm's length transaction, other than in a forced sale or liquidation. Fair values are obtained from quoted market prices, discounted cash flow models and option pricing models as appropriate.

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:-

(a) Long-Term Loans

The fair values of the long-term loans are determined by discounting the relevant cash flows using current interest rates for similar instruments at the balance sheet date.

The carrying amounts and their fair values are as follows:

| | Carrying amount RM'000 | Fair value RM'000 |
|------------------------------------|------------------------------|----------------------|
| Collateralised loan | 40,000 | 40,000 |
| Loan from a related party | 106,816 | 95,035 |
| Loan from the Malaysian Government | 134,614 | 119,767 |
| Murabahah Medium Term Loan | 310,000 | 306,625 |

(b) Hire Purchase and Lease Obligations

The carrying amounts approximated the fair values of these instruments. The fair values of hire purchase and lease obligations are determined by discounting the relevant cash flows using current interest rates for similar instruments at the balance sheet date.

(c) Cash and Bank Balances and Other Short-Term Receivables/Payables

The carrying amounts approximated their fair values due to the relatively short-term maturity of these instruments.

(d) Contingent liabilities

It is not practicable to estimate the fair value of the contingent liabilities reliably due to uncertainties of timing, costs and eventual outcome.

16. ACCOUNTANTS' REPORT (Cont'd)



8. DIVIDENDS FOR THE RELEVANT FINANCIAL PERIODS

PHB and PSSB did not pay or declare any dividends during the Relevant Financial Periods.

9. RESTATEMENT TO THE AUDITED FINANCIAL STATEMENTS

In preparing this report, certain reclassifications were made to ensure the consistency of presentation of information for comparison purposes. The details of the reclassifications made are set out as follows:-

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|--|--------------------|--------------------|--------------------|--------------------|
| BALANCE SHEET (EXTRACT) | | | | |
| (a) Amount owing by an associate | | | | |
| As per audited financial statements | - | - | - | - |
| Reclassification (i) | 94 | 18 | 18 | - |
| As per accountants' report | <u>94</u> | <u>18</u> | <u>18</u> | <u>-</u> |
| (b) Amount owing by related parties | | | | |
| As per audited financial statements | 4,683 | 12,915 | 928 | 7,520 |
| Reclassification (i) | (318) | - | - | - |
| As per accountants' report | <u>4,365</u> | <u>12,915</u> | <u>928</u> | <u>7,520</u> |
| (c) Amount owing to related parties | | | | |
| As per audited financial statements | 109,743 | 72,176 | 17,285 | 17,289 |
| Reclassification (i) | (7,433) | 1,734 | - | - |
| As per accountants' report | <u>102,310</u> | <u>73,910</u> | <u>17,285</u> | <u>17,289</u> |
| (d) Trade receivables | | | | |
| As per audited financial statements | - | 35,741 | 11,681 | 39,494 |
| Reclassification (i) | 4,906 | - | - | - |
| As per accountants' report | <u>5,224</u> | <u>35,741</u> | <u>11,681</u> | <u>39,494</u> |

16. ACCOUNTANTS' REPORT (Cont'd)



9. RESTATEMENT TO THE AUDITED FINANCIAL STATEMENTS (CONT'D)

| | FYE 2005 RM'000 | FYE 2006 RM'000 | FYE 2007 RM'000 | FPE 2008 RM'000 |
|---------------------------------------|--------------------|--------------------|--------------------|--------------------|
| (e) Other receivables | | | | |
| As per audited financial statements | 5,142 | 35,871 | 54,021 | 67,633 |
| Reclassification (i) | 1,881 | 1,716 | (18) | - |
| As per accountants' report | <u>7,023</u> | <u>37,587</u> | <u>54,003</u> | <u>67,633</u> |
| (f) Other payables and accruals | | | | |
| As per audited financial statements | 107,415 | 63,149 | 28,797 | 38,859 |
| Reclassification (i) | 9,408 | - | - | - |
| As per accountants' report | <u>116,823</u> | <u>63,149</u> | <u>28,797</u> | <u>38,859</u> |
| INCOME STATEMENT (EXTRACT) | | | | |
| (a) Administrative expenses | | | | |
| As per audited financial statements | 76,124 | 40,118 | 40,742 | 18,414 |
| Reclassification (ii) | 12 | - | - | - |
| As per accountants' report | <u>76,236</u> | <u>40,118</u> | <u>40,742</u> | <u>18,414</u> |
| (b) Finance costs | | | | |
| As per audited financial statements | 54,765 | 34,826 | 66,003 | 22,685 |
| Reclassification (ii) | (112) | - | - | - |
| As per accountants' report | <u>54,653</u> | <u>34,826</u> | <u>66,003</u> | <u>22,685</u> |

Notes:-

- (i) reclassification on changes in PSSB group structure
- (ii) reclassification of bank charges

16. ACCOUNTANTS' REPORT (Cont'd)



10. SUBSEQUENT EVENTS

There were no significant subsequent events between the date of the last financial statements used in the preparation of this report and the date of this report which will affect materially the contents of this report except as disclosed in the report.

11. AUDITED FINANCIAL STATEMENTS

As at the date of this Report, no audited financial statements have been prepared in respect of any period subsequent to 30 April 2008 for PHB and PSSB.

Yours faithfully

A handwritten signature in black ink, appearing to be "J. K.", written over a horizontal line.

Horwath
Firm No : AF 1018
Chartered Accountants

A handwritten signature in black ink, appearing to be "Onn Kien Hoe", written over a horizontal line.

Onn Kien Hoe
Approval No : 1772/11/08 (J/PH)
Partner

16. ACCOUNTANTS' REPORT (Cont'd)



APPENDIX I

Horwath AF No 1018
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Chartered Accountants

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**REPORT OF THE AUDITORS TO THE MEMBERS OF
PERWAJA HOLDINGS BERHAD**

(Formerly Known As Vertical Winners Sdn. Bhd.)
(Incorporated in Malaysia)
Company No: 798513 - D

We have audited the financial statements set out on pages 3 to 13. The preparation of the financial statements is the responsibility of the Company's directors.

We conducted our audit in accordance with approved standards on auditing in Malaysia. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. Our audit also included an assessment of the accounting principles used and significant estimates made by the directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements are properly drawn up in accordance with applicable approved Financial Reporting Standards in Malaysia so as to give a true and fair view of the state of affairs of the Company at 30 April 2008 and its results and cash flows for the financial period ended on that date.

A handwritten signature in black ink, appearing to be "J. K. S.", written over a horizontal line.

Horwath
Firm No: AF 1018
Chartered Accountants

Kuala Lumpur

24 JUN 2008

16. ACCOUNTANTS' REPORT (Cont'd)



APPENDIX II

Horwath AF No 1018
Kuala Lumpur Office
Chartered Accountants

Level 16 Tower C
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12 Jalan Yap Kwan Seng
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603.2166.1000 Fax

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**REPORT OF THE AUDITORS TO THE MEMBERS OF
PERWAJA STEEL SDN. BHD.**

(Incorporated in Malaysia)
Company No: 187922 - H

We have audited the financial statements set out on pages 8 to 43. The preparation of the financial statements is the responsibility of the Company's directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, in accordance with Section 174 of the Companies Act, 1965 and for no other purpose. We do not assume responsibility to any other person for the content of this report.

We conducted our audit in accordance with approved standards on auditing in Malaysia. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. Our audit also included an assessment of the accounting principles used and significant estimates made by the directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion:-

- (a) the financial statements are properly drawn up in accordance with the provisions of the Companies Act, 1965 and applicable approved accounting standards in Malaysia so as to give a true and fair view of:-
 - (i) the state of affairs of the Company at 31 December 2005 and their results and cash flows for the financial year ended on that date; and
 - (ii) the matters required by Section 169 of the Companies Act, 1965 to be dealt with in the financial statements of the Company; and
- (b) the accounting and other records and the registers required by the Companies Act, 1965 to be kept by the Company have been properly kept in accordance with the provisions of the said Act.

Horwath
Firm No: AF 1018
Chartered Accountants

Onn Kien Hoe
Approval No: 1772/11/06 (J/PH)
Partner

Kuala Lumpur

08 JUN 2006

Page 7

Horwath Offices in Malaysia:

Johor Bahru • Klang • Kota Kinabalu • Kuala Lumpur • Kuching • Labuan • Melaka • Penang • Prai

16. ACCOUNTANTS' REPORT (Cont'd)



APPENDIX II

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**REPORT OF THE AUDITORS TO THE MEMBERS OF
PERWAJA STEEL SDN. BHD.**

(Incorporated in Malaysia)
Company No: 187922 - H

We have audited the financial statements set out on pages 9 to 49. The preparation of the financial statements is the responsibility of the Company's directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, in accordance with Section 174 of the Companies Act, 1965 and for no other purpose. We do not assume responsibility to any other person for the content of this report.

We conducted our audit in accordance with approved standards on auditing in Malaysia. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. Our audit also included an assessment of the accounting principles used and significant estimates made by the directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion:-

- (a) the financial statements are properly drawn up in accordance with the provisions of the Companies Act, 1965 and applicable MASB approved accounting standards in Malaysia for Entities Other Than Private Entities so as to give a true and fair view of:-
 - (i) the state of affairs of the Company at 31 December 2006 and its results and cash flows for the financial year ended on that date; and
 - (ii) the matters required by Section 169 of the Companies Act, 1965 to be dealt with in the financial statements of the Company; and
- (b) the accounting and other records and the registers required by the Companies Act, 1965 to be kept by the Company have been properly kept in accordance with the provisions of the said Act.

Horwath
Firm No: AF 1018
Chartered Accountants

Kuala Lumpur

26 APR 2007

Onn Kien Hoe
Approval No: 1772/11/08 (J/PH)
Partner

Horwath Offices in Malaysia:

Johor Bahru • Klang • Kota Kinabalu • Kuala Lumpur • Kuching • Labuan • Melaka • Penang



**REPORT OF THE AUDITORS TO THE DIRECTORS OF
PERWAJA STEEL SDN. BHD.**

(Incorporated in Malaysia)
Company No: 187922 - H

We have audited the financial statements set out on pages 10 to 62. The preparation of the financial statements is the responsibility of the Company's directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, in accordance with Section 174 of the Companies Act, 1965 and for no other purpose. We do not assume responsibility to any other person for the content of this report.

We conducted our audit in accordance with approved standards on auditing in Malaysia. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. Our audit also included an assessment of the accounting principles used and significant estimates made by the directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion,

- (a) the financial statements are properly drawn up in accordance with the provisions of the Companies Act, 1965 and applicable approved Financial Reporting Standards in Malaysia so as to give a true and fair view of:-
 - (i) the state of affairs of the Company at 31 December 2007 and its results and cash flows for the financial year ended on that date; and
 - (ii) the matters required by Section 169 of the Companies Act, 1965 to be dealt with in the financial statements of the Company; and
- (b) the accounting and other records and the registers required by the Companies Act, 1965 to be kept by the Company have been properly kept in accordance with the provisions of the said Act.

A handwritten signature in black ink, appearing to be "J. K.", written over a horizontal line.

Horwath
Firm No: AF 1018
Chartered Accountants

Kuala Lumpur

28 APR 2008

A handwritten signature in black ink, appearing to be "Onn Kien Hoe", written over a horizontal line.

Onn Kien Hoe
Approval No: 1772/11/06 (J/PH)
Partner

16. ACCOUNTANTS' REPORT (Cont'd)



APPENDIX II

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**REPORT OF THE AUDITORS TO THE MEMBERS OF
PERWAJA STEEL SDN. BHD.**

(Incorporated in Malaysia)
Company No: 187922 - H

We have audited the financial statements set out on pages 3 to 50. The preparation of the financial statements is the responsibility of the Company's directors.

We conducted our audit in accordance with approved standards on auditing in Malaysia. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. Our audit also included an assessment of the accounting principles used and significant estimates made by the directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements are properly drawn up in accordance with applicable approved Financial Reporting Standards in Malaysia so as to give a true and fair view of the state of affairs of the Company at 30 April 2008 and its results and cash flows for the financial period ended on that date.

A handwritten signature in black ink, appearing to be 'J. P. W.' or similar, written over a horizontal line.

Horwath
Firm No: AF 1018
Chartered Accountants

Kuala Lumpur

24 JUN 2008

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT

(Prepared for inclusion in this Prospectus)



VITAL FACTOR CONSULTING

Creating Winning Business Solutions

27 JUN 2008

The Board of Directors
Level 31, Maju Tower
1001 Jalan Sultan Ismail
50250 Kuala Lumpur

Dear Sirs

Assessment of the Primary Steel Products Industry

The following is a summary of the independent **Assessment of the Primary Steel Products Industry** in Malaysia prepared by Vital Factor Consulting Sdn Bhd for inclusion in the Prospectus of **Perwaja Holdings Berhad** (herein together with its subsidiary company will be referred to as "Perwaja Group" or the "Group") in relation to its listing on the Main Board of Bursa Malaysia Securities Berhad.

1 BACKGROUND

- The objective of the report is to provide an independent assessment of the Primary Steel Products Industry in Malaysia.
- Perwaja Group is primarily involved in the manufacture of primary steel products in the form of Direct Reduced Iron (DRI) and semi-finished long steel products.
- For the financial year ended 31 December 2007, the total revenue of Perwaja Group was RM1.7 billion. For the 4-month period ended 30 April 2008, the total revenue of the Group was RM661.4 million.

2 OVERVIEW OF THE OVERALL IRON AND STEEL INDUSTRY

- The Iron and Steel Industry plays a key role in the growth and development of the Malaysian economy and this is substantiated by the following:
 - Iron and steel are the basic raw materials for many industries including, among others, the overall manufacturing industry, building and construction industry, infrastructure, machinery, electrical and electronics, oil and gas, and other fabricated metal Industries.
 - The Iron and Steel Industry is also a major contributor of export earnings for Malaysia. In 2007, the value of exports increased by 12.2% to reach RM10.4 billion *(Source: Department of Statistics)*.
 - Between 2004 and 2007, the sales value of the manufacture of basic iron and steel products increased at an average annual rate of 19.1% to reach RM23.0 billion *(Source: Department of Statistics)*.
- As Perwaja Group is involved in the production of DRI and semi-finished long steel products, this report will focus mainly on the Primary Steel Products Industry.

Vital Factor Consulting Sdn Bhd
(Company No.: 266797-T)

75C & 77C Jalan SS22/19
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47400 Petaling Jaya
Selangor Darul Ehsan, Malaysia

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Fax: (603) 7728-7248

Email: enquires@vitalfactor.com

Website: www.vitalfactor.com



VITAL FACTOR CONSULTING
Creating Winning Business Solutions

3 IRON AND STEEL INDUSTRY OVERALL STRUCTURE

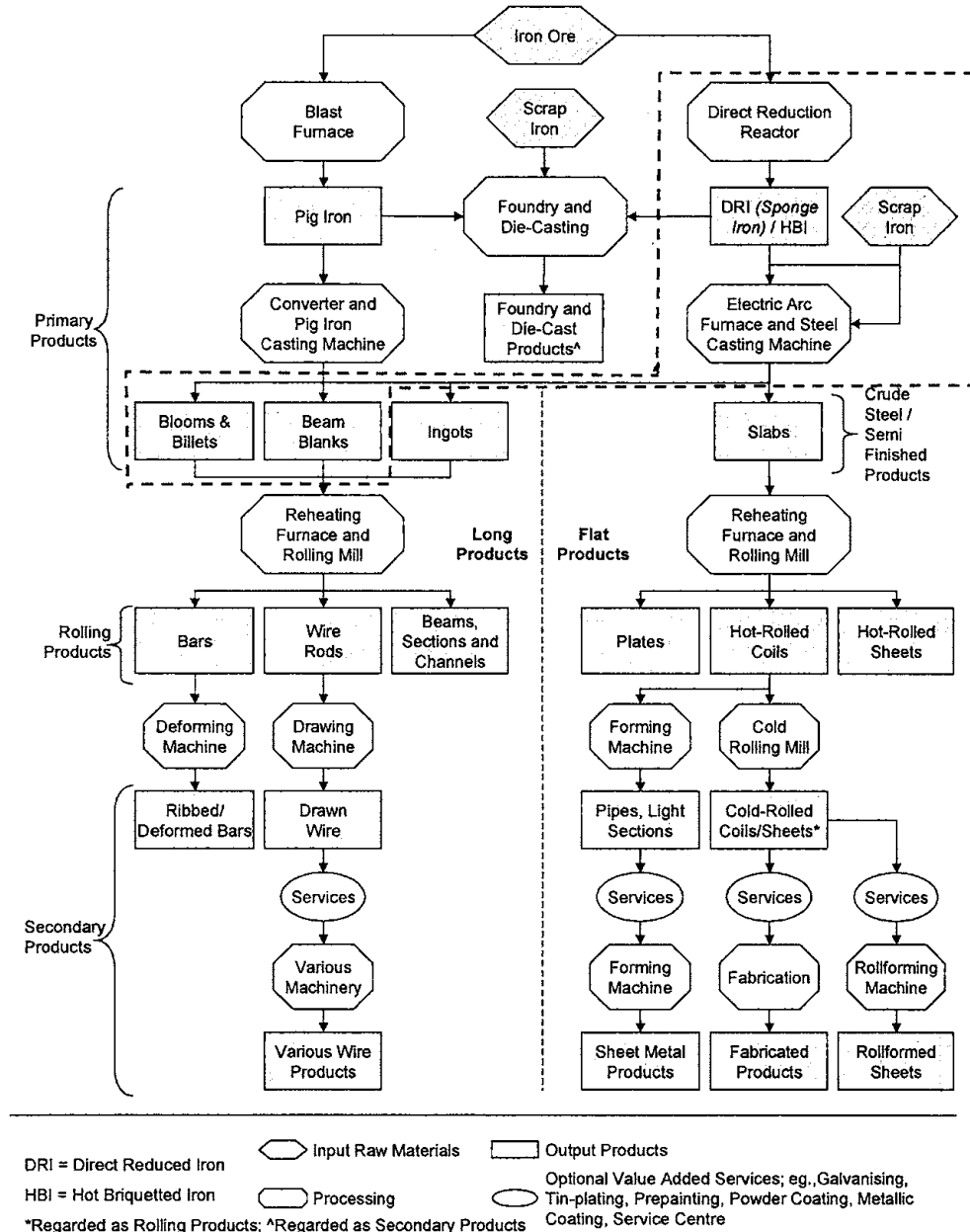


Figure 1 Iron and Steel Industry Overall Structure

3.1 Iron Ore

- Iron ore is the basic raw material in the manufacture of iron and steel products. Typical iron ore consists of Hematite (Fe₂O₃) and Magnetite (Fe₃O₄), having iron content of 70% and 72%, respectively. Iron ore may be used to produce primary steel products such as pig iron in a blast furnace, or directly reduced in a Direct Reduced Iron (DRI) reactor to produce DRI.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

Creating Winning Business Solutions

3.2 DRI, HBI, Pig Iron and Scrap Iron

- DRI/HBI, pig iron and scrap iron are the raw materials or feedstock to produce semi-finished long steel products (blooms, billets and beam blanks) and semi-finished flat steel products (slabs).
- DRI/HBI and pig iron are derived from mined iron ore, while scrap iron comprises recycled iron and steel products:

- **Direct Reduced Iron (DRI)** is mined iron ore (in pellet, lump or fine form) that has undergone a process of chemical reduction to remove the oxides (rust) from the iron ore. A reducing agent is introduced to the iron ore. A series of chemical reactions occur under high temperature in the presence of a catalyst. The maximum reduction rate is about 95%, and the result is DRI with iron content (purity) of up to 97%.

The resulting DRI is produced in the form of small pellets or lumps. DRI is also known as sponge iron due to its spongy or cell-like microstructure. The relatively small pellet size and the spongy microstructure create a relatively large surface area to volume ratio, which makes re-melting easier. However, it also makes DRI more sensitive to reoxidation and ignition.

- **Hot Briquetted Iron (HBI)** is similar to DRI, but compacted into larger blocks in briquette form, eliminating the spongy microstructure. The smaller surface area to volume ratio makes transportation easier, and HBI may also be stored longer before being used as reoxidation and ignition is significantly reduced compared to DRI. These features make HBI more suitable for export.
- **Pig iron** is made from smelting iron ore with coke and limestone in a blast furnace. It has a very high carbon content, typically 4% - 5% by weight, which makes it very brittle and not useful if used directly. Pig iron normally has to go through an additional process to burn off the excess carbon in a controlled manner through a Bessemer Converter or basic oxygen furnace. There are currently no producers of pig iron operating in Malaysia.

- As DRI and HBI are similar except for the final shape and size, they are normally discussed together, and are regarded as being perfect substitutes for one another.
- Perwaja Group is a producer of DRI.
- Scrap iron refers to recycled iron and steel material that is generally remelted and recast into new steel material.
- Malaysia's Iron and Steel Industry relies heavily on scrap iron as feedstock for the production of all iron and steel products. Malaysia sources approximately two thirds of its scrap iron from overseas.

3.3 Semi-Finished Steel Products

- DRI, HBI and/or steel scrap is usually melted in an electric arc furnace, from which it is tapped into a ladle furnace for further ladle processes and alloying.
- Pig iron ingots are remelted in a converter, where its carbon content is also reduced. Alternatively, molten iron may be used directly from a blast furnace. Alloying material may be added to alter the chemical composition of the steel, and the resulting metal is used to produce semi-finished steel products.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (Cont'd)



VITAL FACTOR CONSULTING
Creating Winning Business Solutions

- Semi-finished steel products are normally produced using continuous casting machines. Semi-finished long steel products include billets, blooms, beam blanks and ingots. They are typically used to produce long steel products. Semi-finished flat steel products include slabs, which are typically used to produce flat steel products.

3.4 Long Steel Products

- Semi-finished long steel products such as billets, blooms, beam blanks and ingots are first heated in a reheating furnace and passed through the rolling mill to produce long steel products such as light and heavy sections, bars, and wire rods. These long steel products are also known as rolling products.

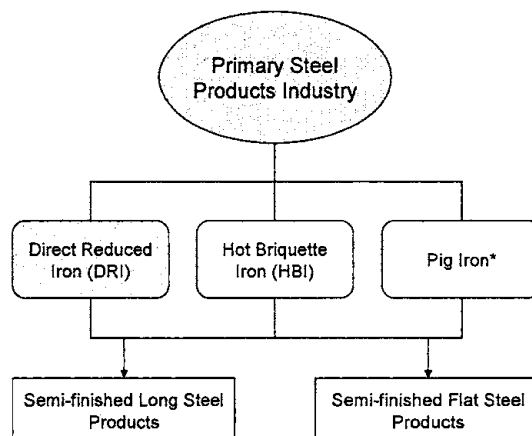
3.5 Flat Steel Products

- Semi-finished flat steel products in the form of slabs are used to produce flat steel products including plates, hot-rolled coils and sheets, and cold-rolled coils and sheets. These flat steel products are also known as rolling products.

4 OVERVIEW OF THE PRIMARY STEEL PRODUCTS INDUSTRY IN MALAYSIA

4.1 Industry Overview

- As part of the Iron and Steel Industry, the Primary Steel Products Industry plays an important role as the producer of feedstock for the further downstream processing and manufacturing of semi-finished and finished iron and steel products.
- This is reflected by the fact that local production of primary steel products amounted to approximately 10.1 million tonnes in 2007 (Source: Primary Market Research undertaken by Vital Factor Consulting Sdn Bhd).
- The overall Primary Steel Products Industry can be broadly categorised as follows:



*No local production of Pig Iron.

Figure 2 Overall Structure – Primary Steel Products Industry

- Perwaja Group is currently engaged in the production of DRI and semi-finished long steel products.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (Cont'd)

**VITAL FACTOR CONSULTING**

Creating Winning Business Solutions

- In 2007, output from the Primary Steel Products Industry amounted to approximately 10.1 million tonnes. Estimated capacity utilisation of the overall Primary Steel Products Industry in 2007 is as follows:

| Primary Steel Product | Production (Tonnes) | Installed Capacity (Tonnes) | Utilisation Rate |
|--|------------------------|--------------------------------|------------------|
| DRI and HBI | 1,828,983 | 2,080,000 | 88% |
| Semi-finished Long Steel Products | 5,302,256 | 6,500,000 | 82% |
| Semi-finished Flat Steel Products | 3,000,000 | 3,500,000 | 86% |
| Overall Primary Steel Products Industry | 10,131,239 | 11,630,000 | 87% |

Source: Primary Market Research undertaken by Vital Factor Consulting Sdn Bhd

Figure 4 Capacity Utilisation of Local Primary Steel Product Operators - 2007

- Based on the above observation, the Primary Steel Products Industry is operating at a relatively high level of capacity utilisation.

5 SUBSTITUTE PRODUCTS

- In general, the primary steel products produced by Perwaja Group is faced with the threat posed by the use of other materials.
- Scrap is a substitute to the DRI produced by Perwaja Group.

5.1 The Use of Materials Other Than Steel

- Alternative materials that can be used as a substitute for steel includes stainless steel, non-ferrous metals such as aluminium and titanium, plastic, ceramics and composite materials.

Mitigation

- Stainless steel is generally not a substitute to steel in most applications as stainless steel is many times more costly than steel. For example, in September 2007, the global price of grade 316 stainless steel hot rolled coil was approximately 10 times higher than carbon steel hot rolled coil (Source: Secondary Market Research undertaken by Vital Factor Consulting Sdn Bhd). As a result, the use of stainless steel is restricted to specialised applications where properties such as corrosion resistance and mechanical strength are critical.
- Based on current technology, steel will continue to dominate as the material of choice for most of its current applications. This is mainly due to the following reasons:
 - Steel has been used for a very long time and its properties and applications are well understood, tested and is proven;
 - Many of the alternative materials are not fully tested over time and there is some reluctance for operators to try them out;
 - Some of the proposed new materials could perform better than steel, but in most cases their costs are prohibitive without providing sufficient compensating benefits to enable them to be economical.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

Creating Winning Business Solutions

5.2 Scrap

- Scrap is currently a substitute to DRI in most steel production processes. For example, an electric arc furnace may be charged with DRI only, or scrap only, or some mixture of both to produce steel.
- The advantage of scrap over DRI are:
 - Scrap is generally cheaper than DRI;
 - Scrap does not require specialised handling and storage procedures to prevent re-oxidation.

Mitigation

- Scrap is unlikely to replace DRI completely in steel production. Scrap contains an unknown quantity and composition of tramp elements, whose presence can alter the chemical composition of the steel produced. As a result, steel producers usually require some quantity of additional DRI to “dilute” and control the proportion of tramp elements in steel.
- In addition, DRI is preferred to scrap in the production of high-grade steel and alloy steel. As the chemical composition of a batch of DRI can be easily determined through chemical analysis of a sample, steel makers can carefully closely the chemical composition of the steel produced by adding alloying materials.

6 GOVERNMENT LEGISLATION, POLICIES AND INCENTIVES**6.1 Manufacturing Licence**

- Apart from the normal manufacturing licence, there are no material Government laws, regulations and policies that may impede on the performance and growth of operators within a free enterprise environment.
- The Industrial Coordination Act 1975 requires companies engaging in any manufacturing activity with shareholders' funds of RM2.5 million and above or employing 75 or more full-time paid employees to obtain a manufacturing licence (*Source: Malaysian Industrial Development Authority*).
- Perwaja Steel obtained the following manufacturing licences from the Ministry of International Trade and Industry:
 - Perwaja Steel obtained a manufacturing licence on 30 September 2004 with respect to the manufacture of “Sponge iron, hot briquetted iron and steel billets” of which manufacturing activities are allowed to commence from 1 October 1991;
 - Perwaja Steel obtained a manufacturing licence on 22 December 2004 with respect to the manufacture of “Blooms and beam blanks”, of which manufacturing activities are allowed to commence from 30 October 2004.
- Perwaja Steel has also obtained a manufacturing licence with respect to the manufacture of “Pig iron” from the Ministry of International Trade and Industry on 8 April 2008.

6.2 Atomic Energy Licence

- According to the Atomic Energy Licensing Act 1984, any company dealing in and possess any radioactive material or irradiating apparatus must obtain a licence.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (Cont'd)

**VITAL FACTOR CONSULTING**

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- Perwaja Group has a licence issued under the Atomic Energy Licensing Act 1984, for the purpose of "Purchasing, owning, possessing, using, operating, storing, transporting and importing/exporting radioactive materials and irradiating apparatus". The license is valid from 1 March 2008 to 28 February 2011.

6.3 Wholesaler's Poison Licence

- An organisation that is involved in importation, possession, manufacture, compounding, storage, transport, sale and use of poisons, is subjected to The Poisons Act, 1952. The licence is granted to an individual person, and not to a company with a business address.
- Perwaja Group has the following Wholesaler's Poison Licence:

| | |
|----------------------|--|
| Licence holder | Zuriana Binti Zainal |
| Company | Perwaja Steel Sdn Bhd |
| Issuing Authority | Ministry of Health, Terengganu |
| Valid Period | 15 February 2008 to 14 February 2009 |
| Approved Poison List | <ol style="list-style-type: none"> 1. Dithienylallylamines, dithieny alkylamines their salts; 2. Bromides; inorganic and ammonium bromide; 3. Mercury; organic and inorganic; 4. Sodium hydroxide (12% and over); 5. Hydrochloric acid (9% and over as HCl); 6. Ammonia (6% and above); 7. Hydrofluoric acid; 8. Nitric acid (9% w/w and over); 9. Potassium hydroxide (12% and over); 10. Sulphuric acid (9% w/w and over). |

Figure 5 Perwaja Group's Wholesaler's Poison Licence

6.4 Government Incentives

- The major government incentives for companies engaged in the manufacturing sector include Pioneer Status, Investment Tax Allowance, Reinvestment Allowance and Tax Exemption (*Source: Malaysian Industrial Development Authority*).
- Perwaja Steel is eligible for Investment Tax Allowance benefits. The Group has not utilised Investment Tax Allowance benefits.

6.5 Government Control of the Price of Billets

- The prices of billets sold in the Malaysian market were previously under Government control, whereby the prices of billets were set by the Ministry of Domestic Trade and Consumer Affairs.
- The price control on billets of the type sold by Perwaja Group in Malaysia was lifted on 12 May 2008.

6.6 Government Control of the Export of Billets

- Previously, an export permit issued by the Ministry of International Trade and Industry was required for the export of billets of the type produced by Perwaja Group.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

Creating Winning Business Solutions

- The requirement to obtain an export permit to export billets of the type exported by Perwaja Group was lifted on 12 May 2008.

6.7 Environmental Regulations**Scheduled Waste**

- During the normal course of its production operations, Perwaja Steel generates the following types of Scheduled Waste:
 - According to the Environmental Quality (Scheduled Wastes) Regulations 2005, the spent alkali generated by Perwaja Steel is classified as “SW401, spent alkalis containing heavy metals”;
 - According to the Environmental Quality (Scheduled Wastes) Regulations 2005, the spent hydraulic oil by Perwaja Steel is classified as “SW305, spent hydraulic oil”;
 - According to the Environmental Quality (Scheduled Wastes) Regulations 2005, the grease by Perwaja Steel is classified as “SW312, oily residue from automotive workshop, service station oil or grease interceptor”;

(Source: Environmental Quality Act and Regulations, all amendments up to January 2006).

- Perwaja Steel has appointed Kualiti Alam Sdn Bhd, a company licensed by the Department of Environment, to collect and transport the spent alkali and grease generated during the manufacturing process to the premises of Kualiti Alam Sdn Bhd.
- Perwaja Steel has appointed Aldwiche Berhad, a company licensed by the Department of Environment, to collect and transport the spent hydraulic generated during the manufacturing process to the premises of Aldwiche Berhad.

Compounds

- The Department of Environment has issued compounds to Perwaja Steel with respect to offences related to the following:
 - A compound of RM6,000 in relation to oil spillage;
 - A compound of RM6,000 in relation to dust pollution.
- Perwaja Steel has successfully appealed for a reduction of the compound amount, to RM4,000 for each offence. Perwaja Steel settled the compound in full on 8 October 2007.
- Perwaja Steel informed the Department of Environment of the following measures taken to address environmental issues in a letter dated 1 October 2007:
 - Perwaja Steel is building a new facility to treat waste oil before it is sent to third parties;
 - Perwaja Steel is currently seeking quotes from consultants to install a continuous air quality monitoring system at its premises. This is in response to a request from the Department of Environment that such a system be installed at Perwaja Steel's premises.
- As at 30 May 2008, the facility to treat waste oil has been completed. In regard to the installation of the continuous air quality monitoring system at its premises, Perwaja Steel is currently awaiting detailed guidelines from the Department of Environment.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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7 SUPPLY

- Perwaja Group is primarily a producer of DRI and semi-finished long steel products.
- Malaysia is both a local producer and importer of DRI and HBI, and semi-finished long steel products.

7.1 Local Production of DRI and HBI

- Between 2002 and 2006, the local production quantity of DRI and HBI increased at an average annual rate of 8.9%. In 2006, production quantity of DRI and HBI increased by 10.7% to reach approximately 1.5 million tonnes (*Source: Malaysian Iron and Steel Industry Federation*).

7.2 Imports of DRI and HBI

- Between 2003 and 2007, import quantity of DRI and HBI decreased at an average annual rate of 74.5%. In 2007, the import quantity of DRI and HBI was only 76 tonnes (*Source: Department of Statistics*).
- The sharp decline in the quantity of DRI and HBI imported to Malaysia was primarily due to Malaysian producers of semi-finished steel products switching to locally produced DRI and HBI.

7.3 Local Production of Semi-finished Long Steel Products

- Between 2002 and 2006, production quantity of semi-finished long steel products increased at an average annual rate of 4.2%. In 2006, the production quantity of semi-finished long steel products increased marginally to 3.80 million tonnes (*Source: Malaysian Iron and Steel Industry Federation*).

7.4 Imports of Semi-finished Long Steel Products**Imports of Semi-Finished Products of Iron or Non-alloy Steel**

- Between 2003 and 2007, the import quantity of semi-finished products of iron or non-alloy steel increased at an average annual rate of 19.8%. In 2007, preliminary data indicated that import quantity increased by 46.5% to 617,586 tonnes.
- Between 2003 and 2007, the import value of semi-finished products of iron or non-alloy steel increased at an average annual rate of 17.5%. In 2007, preliminary data indicates that import value increased by 24.4% to RM719.5 million.
- In 2007, China was the largest source of imports of semi-finished products of iron or non-alloy steel, which accounted for 94.6% of imports by value. Other sources of imports were Brazil and Japan, which accounted for 3.3% and 1.0% of imports by value respectively.

(*Source: Department of Statistics*)

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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Imports of Rectangular Semi-finished Products of Iron or Non-alloy Steel Containing by Weight Less Than 0.25% Carbon

- Between 2003 and 2007, the import quantity of rectangular semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon, declined at an average annual rate of 26.6%. In 2007, preliminary data indicated that import quantity declined by 46.0% to 19,397 tonnes.
- Between 2003 and 2007, the import value of rectangular semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon, declined at an average annual rate of 22.4%. In 2007, preliminary data indicated that import value declined by 44.6% to RM30.8 million.

*(Source: Department of Statistics)***Imports of Other Rectangular Semi-finished Products of Iron or Non-alloy Steel Containing by Weight Less Than 0.25% Carbon**

- Between 2003 and 2007, the import quantity of other rectangular semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon, increased at an average annual rate of 41.9%. In 2007, preliminary data indicated that import quantity increased by 2.4% to reach 374,941 tonnes.
- Between 2003 and 2007, the import value of other rectangular semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon, increased at an average annual rate of 50.2%. In 2007, preliminary data indicated that import value increased by 34.3% to reach RM678.0 million.
- In 2007, China accounted for 99.7% of the imports by value of other rectangular semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon. Other sources of imports were Brazil, Singapore, Germany and Taiwan.

*(Source: Department of Statistics)***Imports of Other Semi-finished Products of Iron or Non-alloy Steel Containing by Weight Less Than 0.25% Carbon**

- Between 2003 and 2007, the import quantity of other semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon declined at an average annual rate of 85.2%. In 2007, preliminary data indicated that import quantity increased by 184.3% to 9 tonnes.
- Between 2003 and 2007, the import value of other semi-finished products of iron or non-alloy steel containing by weight less than 0.25% carbon declined at an average annual rate of 74.3%. In 2007, preliminary data indicated that import value increased by 101.3% to RM0.1 million.

*(Source: Department of Statistics)***Imports of Rectangular Semi-finished Products of Iron or Non-alloy Steel Containing by Weight More Than 0.25% Carbon**

- The semi-finished long steel products produced and exported by Perwaja Group are classified under the category "Rectangular semi-finished products of iron or non-alloy steel containing by weight more than 0.25% carbon".

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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- Between 2003 and 2007, the import value of rectangular semi-finished products of iron or non-alloy steel containing by weight more than 0.25% carbon, declined at an average annual rate of 47.7%. In 2007, preliminary data indicated that import value declined by 39.4% to RM10.7 million.

(Source: Department of Statistics)

8 SUPPLY DEPENDENCIES

- Iron ore is the main raw material used in producing DRI and HBI.
- DRI and scrap iron are the main raw materials used by Perwaja Group in the production of semi-finished long steel products. All of the DRI that are used by Perwaja Group for the production of semi-finished long steel products is produced in-house by the Group.

8.1 Local Production of Iron Ore

- Between 2002 and 2006, local production quantity of iron ore increased at an average annual rate of 13.3%. In 2006, local production quantity of iron ore declined by 29.8% to 667,082 tonnes.
- There were a total of 11 iron ore mines operating in Malaysia in 2006. The iron ore produced in Malaysia is mostly of a lower grade, which is mainly used by pipe-coating factories for the Oil and Gas Industry, with a small amount used by local cement producers. Some of the locally produced iron ore is exported to China.

(Source: Ministry of Natural Resources and Environment)

- The iron ore currently produced in Malaysia is not suitable for use in producing DRI.

8.2 Imports of Iron Ore

- Between 2003 and 2007, import value of iron ore and concentrates increased at an average annual growth rate of 30.7%. In 2007, preliminary data indicated that import value increased by 15.3% to RM1.1 billion.
- Brazil is the largest source of imports for iron ore and concentrates, which accounted for 41.9% of imports by value in 2007. This is followed by Chile and Mexico, which accounted for 20.6% and 13.3% of imports by value respectively. Other sources of imports of iron ore included Bahrain, Greece and China.

(Source: Department of Statistics)

8.3 Local Supply of Scrap Iron

- Between 2002 and 2006, local supply of scrap declined at an average annual rate of 0.5%. In 2006, local supply of scrap increased by 11.1% to 1.6 million tonnes *(Source: Malaysian Iron and Steel Industry Federation)*.

8.4 Imports of Scrap Iron

- Between 2003 and 2007, import value of scrap iron increased at an average annual growth rate of 32.0%. In 2007, preliminary data indicated that import value of scrap iron increased by 38.8% to RM4.2 billion.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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- United States was the largest source of imports for scrap, accounting for 38.5% of imports by value in 2007. This is followed by the United Kingdom and Australia, which accounted for 17.5% and 15.4% of imports by value respectively. Other sources of imports of scrap were South Africa, Singapore, the Philippines and Germany.

(Source: Department of Statistics)

9 DEMAND DEPENDENCIES

- DRI and HBI are used as feedstock in a diverse number of industries, including the foundry and die-casting industries. DRI and HBI are also used in the production of semi-finished steel products, which in turn is used for all downstream steel products.
- As such, demand for DRI and HBI are dependent on the downstream demand of the following types of steel products:
 - Semi-finished products
 - Long products such as blooms, billets and beam blanks;
 - Flat products such as slabs.
 - Intermediate user industries (finished/rolling products)
 - Long products, including sections, bars, and wire rods;
 - Flat products, including hot-rolled coils, sheets and plates, and cold-rolled sheets and coils.
 - Secondary steel user industries
 - Long products, including wire and wire products;
 - Flat products, including sheet metal, welded tubes and pipes, fabricated and roll formed products.
 - End-user Industries
 - Building and Construction;
 - Infrastructure;
 - Oil, Gas and Petrochemicals;
 - Consumer electronics and appliances;
 - Fabricated metal products;
 - Machinery and Equipment;
 - Transportation.

(Note: Not all applications described above can be satisfied locally as some of these require special treatment and quality standards which are not undertaken in Malaysia. One example is railway tracks)

- Local production of semi-finished long steel products are addressed in Section 7 of this Expert Letter.
- Generally, dependencies on end-user industries can be categorised based on the type of steel products involved, as follows:
 - Long products
 - Building, construction and infrastructure
 - Flat products
 - Manufacture of industrial and consumer products
 - Metal casting
 - Foundry and die-casting products

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (Cont'd)

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9.1 Local Production of Semi-finished Flat Steel Products

- In 2007, there was only one producer of semi-finished flat steel products, Megasteel Sdn Bhd, operating in Malaysia. Local production quantity of slabs totalled 3.0 million tonnes in 2007. Megasteel currently uses all the slabs produced by the company for further in-house processing to produce hot-rolled coils and plates (*Source: Primary Market Research undertaken by Vital Factor Consulting Sdn Bhd*).

9.2 Demand from End-user Industries

- Demand for DRI and HBI is ultimately driven by its end-user industries, which can be segmented into the following major categories:
 - Overall Iron and Steel Industry;
 - Building, construction and infrastructure;
 - Manufacture of consumer and industrial products.
- DRI and HBI are used as feedstock for the production of various types of semi-finished steel products, which are further processed to produce finished steel products such as light and heavy sections, bars, rods, wire products, hot and cold rolled coils and plates.
- Demand for semi-finished long steel products is ultimately driven by the Building, Construction and Infrastructure Industries.
- DRI and HBI are also used as raw materials in the Die-casting and Foundry Industries. Foundry and die-cast products are in turn used in many manufacturing industries, such as the Electrical and Electronics Industry, Machinery and Equipment Industry, and Automotive Industry, whose performance are captured by the performance of the Overall Manufacturing Industry.
- The following section assesses the performance of the end-user industries, which will impact on the demand for DRI and HBI, and semi-finished long steel products.

Manufacture of Basic Iron and Steel Products

- Between 2004 and 2007, the sales value of the manufacture of basic iron and steel products increased at an average annual rate of 19.1%. In 2007, the sales value of the manufacture of basic iron and steel products increased by 23.6% to RM23.0 billion (*Source: Department of Statistics*).

Construction Industry

- Between 2005 and 2007, the GDP contribution of the Construction Industry increased at an average annual rate of 1.0%. In 2007, the GDP contribution of the Construction Industry increased by 4.6%. The Construction Industry remains an important component of the Malaysian economy. In 2007, the GDP contribution of the Construction Industry at current prices was RM15.2 billion (*Source: Bank Negara Malaysia*).

Manufacturing Industry

- Between 2005 and 2007, the GDP contribution of the Manufacturing Industry grew at an average annual rate of 5.1%. In 2007, the GDP contribution of the Manufacturing Industry grew at 3.1% (*Source: Bank Negara Malaysia*).
- The growth of the Manufacturing Industry in Malaysia will continue to stimulate demand for DRI, HBI, semi-finished steel products and finished steel products.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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10 DEMAND**10.1 Apparent Consumption of DRI and HBI**

- In 2006, Malaysia's estimated apparent consumption of DRI and HBI increased by 3.8% to 1.30 million tonnes. Between 2002 and 2006, it is estimated that apparent local consumption of DRI and HBI increased at an average annual rate of 14.0% (*Source: Malaysian Iron and Steel Industry Federation*).
- The high rate of growth in apparent consumption suggests that there is an increasing demand for DRI and HBI to meet the growing needs of downstream and end-user industries.

10.2 Exports of DRI and HBI

- According to the Department of Statistics, exports of DRI and HBI are classified under the following category:
 - Ferrous products obtained by direct reduction of iron ore and other spongy ferrous products, in lumps, pellets or smaller forms; iron having a minimum purity by weight of 99.94%, in lumps, pellets or similar forms (hereafter referred to as "DRI and HBI").
- Between 2003 and 2007, export quantity of DRI and HBI declined at an average annual rate of 14.3%. In 2007, preliminary data indicated that the export quantity of DRI and HBI increased by 60.8% to reach 321,309 tonnes.
- Indonesia was the largest market for exports of DRI and HBI, accounting for 45.8% of exports by quantity in 2007. This is followed by Iran and Thailand, which accounted for 15.1% and 11.2% of exports by quantity respectively. Other export markets for DRI and HBI included China, Korea and Taiwan.
- Between 2003 and 2007, export value of DRI and HBI increased at an average annual rate of 1.6%. In 2007, preliminary data indicated that the export value of DRI and HBI increased by 50.9% to reach RM314.4 million.

(*Source: Department of Statistics*)

10.3 Apparent Consumption of Semi-Finished Long Steel Products

- In 2006, Malaysia's estimated apparent consumption of semi-finished long steel products increased by 8.3% to an estimated 3.58 million tonnes. Between 2002 and 2006, it is estimated that apparent local consumption of semi-finished long steel products increased at an average annual rate of 1.8% (*Source: Malaysian Iron and Steel Industry Federation*).
- The increase seen in the apparent local consumption of semi-finished long steel products indicates a continuing demand for semi-finished long steel products.

10.4 Exports of Semi-finished Long Steel Products

- Semi-finished long steel products exported by Perwaja Group are classified under the broad umbrella of semi-finished long steel products.
- Between 2003 and 2007, export value of semi-finished long steel products increased at an average annual rate of 30.2%. In 2007, preliminary data indicated that export value increased by 282.0% to reach RM1.7 billion.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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- Vietnam was the largest market for exports of semi-finished long steel products, accounting for 53.6% of exports by value in 2007. This is followed by Indonesia and Thailand, which accounted for 17.0% and 7.5% of exports by value respectively. Other export markets for semi-finished long steel products were Thailand, Philippines, and Iran.

(Source: Department of Statistics)

11 RELIANCE ON AND VULNERABILITY TO IMPORTS

- The Primary Steel Products Industry in Malaysia is reliant on imports for the supply of iron ore and scrap iron.
- Although Malaysia is a producer of iron ore, the iron ore produced in Malaysia is mostly of a lower grade that is not suitable for use in producing DRI.
- Local supply of scrap is not sufficient to meet the needs of the local Primary Steel Products Industry. As a result, scrap iron has to be imported into Malaysia.
- The Primary Steel Products Industry in Malaysia is not vulnerable to imported raw materials, as both iron ore and scrap are widely traded commodities.
- Perwaja Group has entered into long-term contracts for the supply of iron ore, which gives the Group the right to purchase a specified quantity of iron ore. This provides the Group with some assurance that it will be able to secure supplies of iron ore from overseas.
- Perwaja Group currently sources scrap iron from both Malaysian and overseas suppliers, and is not entirely reliant on imported scrap iron.

12 PRICE VOLATILITY OF PRINCIPAL RAW MATERIALS

- In general, there is some volatility in the price of iron ore. The benchmark global market price for most types of traded iron ore is largely determined by annual negotiations between the major users and producers of iron ore. Between 1997 and 2003, the price index for iron ore pellets fluctuated between the index values of 90 to 100. The price index subsequently from 99.8 in 2003 to an estimated index value of 395.5 in 2008.
- The price of scrap also exhibits some volatility. The price of scrap usually varies from month to month. The price of scrap has generally followed an upward trend from June 2003 to December 2007, where the index value for scrap increased from a base index value of 100.0 in June 2003 to an index value of 228.0 in December 2007.

(Source: Secondary Market Research conducted by Vital Factor Consulting Sdn Bhd)

- As iron ore and scrap are internationally traded commodities, all operators in the primary steel products industry that purchase iron ore and scrap will be subjected to the same volatility in their pricing.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

Creating Winning Business Solutions

13 COMPETITIVE NATURE AND INTENSITY**13.1 Nature of Competition in the Industry**

- Operators in the Primary Steel Products Industry engaged in the production of DRI and semi-finished long steel products in Malaysia face normal competitive conditions.

13.2 Factors of Competition

- As with most free enterprise environment, competition amongst producers of DRI and semi-finished long steel products is based on a number of factors, including:
 - Contractual arrangements with suppliers of iron ore;
 - Financial strength to ensure continuous supply of imported raw materials;
 - Contractual arrangements with customers;
 - Ability to exploit economies of scale;
 - Established track record.

13.3 Impact of Factors of Competition of Perwaja Group

- **Contractual Arrangements with Suppliers of Iron Ore:** Perwaja Group has entered into long-term supply contracts for iron ore with some of its suppliers. The Group's long-term supply contracts provide the Group with assurance that it will be able to secure iron ore to help guard against disruptions of the Group's operations due to supply of iron ore. This will help Perwaja Group in competing against other producers of primary steel products.
- **Financial Strength to compete and grow the business:** For the financial year ended 31 December 2007, Perwaja Group's profit after tax amounted to RM162.6 million. Perwaja Group's high profitability will help it in competing against other producers as it provides the Group with the financial strength to support its on-going operations, as well as make strategic investments or to grow the company to address business opportunities.
- **Contractual arrangements with customers:** Perwaja Group has entered into long-term contracts for the supply of DRI and semi-finished long steel products with some of its customers. Securing long-term contracts with buyers will help Perwaja Group compete, as it ensures that there will be a secure market for the Group's going forward. It also assists the Group in scheduling production and ensuring that the Group's large fixed assets are optimally utilised.
- **Ability to exploit economies of scale:** The manufacturing of DRI is capital-intensive requiring significant economies of scale to be profitable. In addition, the production process of DRI and semi-finished long steel products favour continuous 24-hour operation to reduce wastage in energy cost created by cooling down and heating up again for production.

Perwaja Group currently enjoys these economies of scale due to the Group's high capacity utilisation rates for the production of DRI and semi-finished long steel products. As the Group is able to consume all of the DRI produced either in the form of DRI or converted to semi-finished long steel products, Perwaja Group is able to operate the DRI reactor at a high rate of utilisation.

The ability to exploit economies of scale will help Perwaja Group compete against other producers, as the Group optimally operates its fixed assets and minimises production costs.

17. EXECUTIVE SUMMARY OF THE INDEPENDENT MARKET RESEARCH REPORT (*Cont'd*)**VITAL FACTOR CONSULTING**

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- **Established Track Record:** Perwaja Group has been in operation since 1985. This long and established track record provides it with a competitive advantage over new entrants and companies who have been operating over a short period of time.

13.4 General Industry Competitive Intensity

- The overall competition among producers of DRI and semi-finished long steel products is **low**.
- This is substantiated by the following:
 - As at April 2008, there are two manufacturers of DRI and HBI, and six manufacturers of semi-finished long steel products operating in Malaysia. The small number of manufacturers reduces competitive intensity (*Source: Primary Market Research undertaken by Vital Factor Consulting Sdn Bhd*);
 - New entrants wishing to engage in the production of DRI, HBI and semi-finished long steel products are faced with very high barriers to entry. The very high barriers to entry serve to deter new entrants, and helps to reduce competitive intensity.

14 OPERATORS IN THE INDUSTRY

- As at April 2008, there were two producers of DRI and HBI operating in Malaysia:
 - Perwaja Steel Sdn Bhd;
 - Antara Steel Mills Sdn Bhd.
- As at April 2008, there were six producers of semi-finished long steel products operating in Malaysia:
 - Perwaja Steel Sdn Bhd;
 - Amsteel Mills Sdn Bhd;
 - Ann Joo Steel Berhad (formerly known as Malayawata Steel);
 - Antara Steel Mills Sdn Bhd;
 - Malaysia Steel Works (KL) Berhad;
 - Southern Steel Berhad.

(*Source: Primary Market Research undertaken by Vital Factor Consulting Sdn Bhd*)

15 BARRIERS TO ENTRY

- The barriers to entry for a new entrant to the primary steel product industry intending to produce DRI and HBI, and semi-finished long steel products are:
 - Capital and set-up cost;
 - Working capital;
 - Technical skills.

15.1 Capital and Set-up Cost for the Production of Primary Products

- Capital and set-up cost creates a **very high** barrier to entry for new entrants wishing to produce DRI and HBI.
- It is estimated that Megasteel Sdn Bhd's new Midrex DRI plant in Banting, Selangor costs approximately RM2 billion to set-up. The major plant, machinery and facilities required includes a DRI reactor, briquetting plant to produce HBI (if desired), port facilities to handle incoming iron ore and other feedstock, and outgoing DRI (including cost of dredging), iron ore handling facilities, and DRI handling and