Expanding Its Coke Producing

INVEST speaks with Sino Hua-An International Berhad's Executive Chairman, Y.A.M. Tunku Naquiyuddin ibini Tuanku Ja'afar about ramping up their operations in China.

1) Has the group's revenue for the 2007 fiscal year benefited from the rising prices of raw materials worldwide?

Metallurgical coke, being one of the critical raw materials for the manufacturing of steel in China, registered a robust increase in price throughout 2007, in tandem with the general rise in prices of raw materials worldwide. From an average coke price of RMB1,088 per tonne registered in 2006, our Company experienced an increasing pricing trend for our coke from RMB1,130 in January 2007 to RMB1,580 in December 2007. Such increases have inherently improved our overall profit margins and profitability for our financial year 2007. Admittedly, the price of coking coal (which is our principal raw material) had also seen an increasing trend in 2007. However, such an increase did not (and will not) pose a problem for our Company as it is seen as a "pass-through" cost element, i.e. we are able to pass on entirely the effects of increases in coal prices to our customers, the steel players. Additionally, as evidenced by our records of price movements of coke vis-à-vis that of coal, the quantum increases in the coke price is relatively greater than that of coal.

Further to that, we have also commissioned our own coal washing facility in May 2007 and have already seen the benefits of it resulting from the overall reduction in total cost of production by virtue of being able to purchase raw coal now compared to pre-washed coal previously, which is relatively more expensive than the former. We expect the overall cost savings to be in the region of 3-5 per cent.

We expect the price for coke to continue to remain strong in 2008, stemming from the strong growth in the China steel industry. Research has shown that steel will continue to be a much sought after commodity in 2008 and users worldwide will have to come to terms with higher steel prices. China alone produces and consumes approximately 30 per cent of total steel worldwide, not forgetting other steel-hungry emerging nations like India, Brazil, Russia, Vietnam, etc. Steel production has risen dramatically since the turn of the century and the world demand projected to grow at a compounded annual rate of 4.9 per cent from 2007 to 2010.

2) Is the group planning to scale up production capacity either though upgrading of its production plant at Shen Quan Zhuang Industrial Park or through the acquisition of more production facilities to meet the rising worldwide demand for raw materials?

Yes, we are in fact in the process of expanding of existing coke production capacity from 1.2 million tonnes to 1.8 million tonnes. Construction of the said additional 600,000 tonnes capacity coking oven is close to completion and we expect to be able to fully commission it by June 2008. This new coking ovens are being constructed on our existing site at the Shen Quan Zhuang Industrial Park.

We were also looking for prospective acquisitions of other coke production facilities around China. However, at this juncture, those that are available for sale are either not as efficient as ours and/or saddled with old technology plants/ovens. The ones that are appropriate and relevant however, are either not available for sale or are priced at a ridiculously high price. Notwithstanding that, we are constantly on the lookout for potentially good and fairly-priced coke plants and if one is available, we will seriously consider it.

3) Is the group planning to do a secondary listing on either the Shanghai or Shenzhen stock exchanges to raise capital for future investments?

The question of a secondary listing either on the Shanghai, Shenzhen or even Hongkong, Singapore or Dubai was also raised be some of our shareholders, fund managers and analysts during our continuous Investor Relation initiatives to update the developments of our Group to the stakeholders of Sino Hua-An. These foreign bourses in recent times had seen unprecedented growth and that China companies/businesses listed therein generally garner strong following and are generally given a healthy valuations. For example Hidili, China Coal and China Shenhua (listed on Hong Kong Stock Exchange) are all trading at over PE 30X. This secondary listing became increasingly pertinent during these current times when our share price is presently vastly undervalued

Y.A.M. Tunku Naquiyuddin ibni Tuanku Ja'afar
Executive Chairman
Sino Hua-An International Berhad

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on Bursa Malaysia. People who have good understanding of our Company and able to appreciate the prospects of the coke business in China relative to the China steel industry think that our share price should be traded in and around the price valuation of companies with similar businesses listed in the other regional bourses. However, instead of jumping onto the bandwagon to list on these foreign bourses, we are seriously looking into and evaluating such possibility and exploring with our advisors on the appropriateness, viability and the timing of such initiative, if at all we decide to go down that route.

Notwithstanding the above, we are also still hopeful that local investors in Bursa Malaysia will slowly but surely be able to understand the unique circumstances of our Company and will eventually be willing to offer a higher and more justifiable premium to our share price. In this respect, we are stepping up our IR efforts and going into the market to introduce our Group, and explaining its strong fundamentals and competencies to the general investors at large.

4) With the proposed acquisition of a 49 per cent stake in Linyi Jiangxin Steel Co. Ltd to enhance downstream activities in August 2007, is the group looking to position itself as a supply chain leader in the steel production industry in the near future?

Yes. It has always been our aspiration to build the Group into a serious heavy industry player in China and subsequently in the region. As such, the proposed acquisition of Linyi Jiangxin Steel Co. Ltd will be our first step towards that direction. We are also looking at other M&A activities to help realize our ultimate goal but we will want to stagger such exercises to ensure that each of these strategic expansion and diversification plans are carefully considered and implemented to bring out their fullest potential for the benefit of the enlarged Sino Hua-An Group.

5) One of the by-products in the production of metallurgical coke is coal gas. Does the group have any plans to tap into the regional market for the trading of carbon credits as outlined in the Kyoto Protocol?

Coal gas is indeed one of the main by-products generated from our coking facility. However, instead of releasing it into the atmosphere or combusting it thus generating carbon dioxide (amongst other potential GHG gases) we sell all our coal gas by piping directly to our customers, namely the power plant and ceramics factory, both of which are located just next door.

Notwithstanding that, we have indeed explored the possibilities of earning carbon credits from our existing operations by engaging in several discussions with relevant experts in this field. At the outset, we have already put up a relatively technologically advanced environmental pollution and gas emission control facility on our coking plant when our Chinese partners built it in 2004 (unfortunately before fully understanding the procedures involved in applying for eligibility to earning carbon credits). As such, the carbon credits that could be potentially earned, if any, based on our existing operations would be minimal unless we further embark on further investments in “improvement” projects to show significant incremental reductions of GHG emissions.

6) Is the company planning to ship and supply other countries in the region with its metallurgical coke products in the near future?

Even though we do not export our coke products currently, we do not discount the possibility of doing so in the future. In business, as long as it makes economic sense, then why not? When I talk about making economic sense here, I mean we need to not only consider the pricing aspect that we might be able to procure by selling our coke outside of China. We have to also take cognizance of other socioeconomic considerations in order to ensure whatever decision we make it can translate to long-term business sustainability to the Group and enhancing our profitability and shareholders’ value.

We are very thankful of the current strong demand situation for our coke where we are operating and we believe this would continue in the foreseeable future. The demand for our coke has been very encouraging and that we are unable to satisfy entirely the coke requirements of all of our customers even though we are currently already operating at 110% above our designed production capacity. There are also instances where some of our customers prepay us just to secure the specified quantity of coke from us. Given such dearth in the supply of coke to our existing customers, we need to ensure that consistent supply of coke is given to our existing valued and loyal customers, vis-à-vis our consideration for export. In addition to that, there is also in existence an export quota implemented by the Chinese Government which allows only about 5 per cent of the total coke output in China to be exported each year.