Investorfirst Securities

Research | Emerging Companies | Mining Services

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LaserBond

Initiating Coverage

LaserBond (LBL) specialises in the reclamation and surface engineering of industrial components operating in severe environments (prone to corrosion and/or wear) and critical applications. LBL's products include: LaserBond™ cladding, High-Pressure High-Velocity Oxy Fuel (HP HVOF) and Thermal Spraying.

Stronger for longer

Improving performance, reducing costly downtime

LaserBond (LBL) specialises in reclamation and surface engineering of worn or corroded project-critical metallurgical surfaces in a range of industrial processes. That is, LBL's resurfacing techniques reduce downtime, on-going maintenance costs and extend the life of machinery. Around 60% of LBL's sales are into the mining and related industries with a further ~20% into metals manufacturing. New areas of growth include transport and electricity generation. With 10 years of experience and a growing book of positive referrals LBL is enjoying strong growth and is expanding its core NSW base to meet this demand.

In Sydney and Gladstone, expansion to focus on WA & SA

LBL's larger growth challenge is that the cost of transporting very large and heavy components to service centres for reclamation can be inhibitive, so LBL needs to go to the customer. LBL made its first foray into geographic expansion in 2008, acquiring Peachey's Engineering in Gladstone, Queensland. Management has gained valuable insight into the challenges of integration and development of new business lines and has remained very vigilant with regard to its cost base. Now that Gladstone is bedded down, LBL is looking to WA and SA for expansion opportunities and completed a $2.1m capital raising at 23 cents a share in May 2012 to fund this growth.

Buy recommendation and $0.235 a share valuation

We initiate with a Buy rating and $0.235 a share valuation. LBL is well placed for significant growth in the coming years as its LaserBond™-cladding offering gains recognition and acceptance in its various markets. Peer comparison is limited due to the specialist nature of LBL's business.

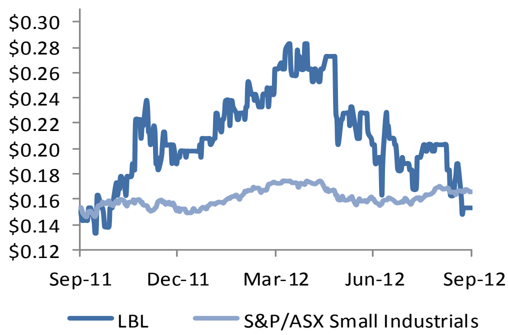
Our valuation is a blend of our base case ($0.21/sh) and acquisition case valuations ($0.26/sh). Each of those valuations is comprised of a 50/50 weighting of our discounted cash flow (DCF) valuation and FY13f EV/EBITDA at 6.5x. Given LBL's small size and the risks involved in expansion we apply a cost of capital of 13.7%; LBL holds a net cash position. We apply a terminal growth rate of 3.0%.

Investorfirst Securities managed and underwrote the issue of 9.1 million shares in LBL in May 2012 and received fees for this

Rating	Valuation	ASX code
Buy	$0.235	LBL

Pricing Data

52-w range ($)	$0.12 - $0.28
Current price ($)	**$0.150**
Diluted shares (m)	84.7
Market cap ($m)	12.71
Net debt ($m)	-1.37
EV ($m)	11.34



Key Financial Metrics & Forecasts

$m	FY11a	FY12a	FY13f*	FY14f*
Revenue	13.3	14.4	15.5	16.8
EBIT adj.	2.14	1.92	2.07	2.10
Net profit (adj)	1.43	1.29	1.38	1.41
EPS (adj) (c)	2.02	1.74	1.63	1.67
Dividend (c)	0.5	0.5	0.6	0.6
EV/EBITDA	4.9x	5.0x	4.6x	4.5x
P/E	7.4x	8.6x	9.2x	9.0x
Net yield	3.3%	3.3%	3.9%	3.9%

**'base case' forecast (excludes potential acquisitions)*

Background and Board

LaserBond (LBL) was founded in 1992 as HVOF Australia Pty Ltd. LBL ran as a family business until listing in 2007. Founder Greg Hooper and his brother Wayne remain executive directors today and the Hooper family remains the largest shareholder bloc with ~47% of shares on issue.

LBL specialises in reclamation and surface engineering of industrial components. That is, LBL can repair worn or corroded project-critical metallurgical surfaces in a range of industrial processes using LaserBond™ Cladding precision welding of materials and/or High Pressure High Velocity Oxy Fuel (HP HVOF) thermal spraying. LBL's resurfacing techniques reduce downtime, on-going maintenance costs and extend the life of machinery.

Approximately 60% of sales are into resource mining-related businesses. A further 20% of customers are in the aluminium and steel manufacturing sectors, with the remaining going to a vast array of industries. The downsizing of the steel manufacturing sector has not impacted LBL to date but aluminium sector woes are providing a challenge in Queensland. However, LBL actually expects to be a beneficiary of the carbon tax. While its own systems are energy intensive, LBL can reclaim a worn component using as little as 5% of the energy required to manufacture a replacement part, increasing its total cost advantage versus replacing a worn part.

LBL's growth challenge is that the cost of transporting very large and heavy wear-plate components from site to service centres can be inhibitive and so LBL needs to go to the customer. To that end LBL acquired a Gladstone-based engineering business in mid-2008. After suffering early integration challenges, Gladstone is now bedded down. This has allowed LBL to progress with the development of a new 5,400m^2 site to bring together its NSW operations, which currently operate at capacity out of two sites. Gladstone's progress also provides management the opportunity to pursue acquisition or greenfield growth opportunities in WA and SA.

Board

Chairman (non-exec) - Timothy McCauley: Previously MD of Auto One Ltd and currently MD of Artiana Imports. Previous operations management experience. Began career with KPMG.

Executive Director - Wayne Hooper: Engineer with experience in manufacturing and engineering industries including design, maintenance and project management. Also spent time with BTR Nylex's building products division. Joined LBL in 1994.

Executive Director - Greg Hooper: Founded LBL in 1992. Previous engineering and sales experience in welding and thermal spray industries. Greg has been instrumental in developing the company's H.V.O.F. and LaserBond™ processes using LBL's in-house laboratory. Greg's focus is on continual development of these processes and training of personnel to run these applications.

Non-Executive Director - Philip Suriano: Currently Equity Capital Markets Division Director at Arthur Phillip. Joined board in 2008. Early career in corporate banking at CBA. Experience in operations, sales and marketing.

Contents

The founding Hooper family hold ~47% of shares on issue

Operations in Sydney and Gladstone—looking west for growth

Business segments

The core of LBL's operation is a traditional surface engineering and reclamation business. However, LBL has had a very strong focus on developing new and existing technologies and is a leader in the relatively new technology of LaserBond™ cladding. LBL developed its own laser-cladding system and commenced using it on client applications in 2001.

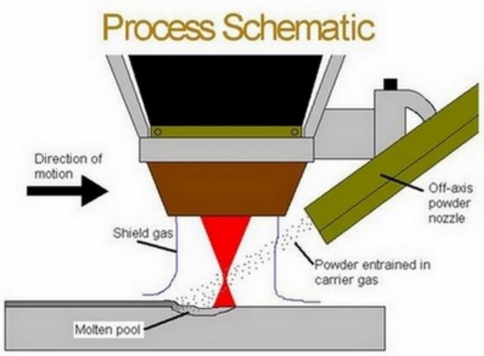
LaserBond™-cladding

LaserBond™ cladding involves the precision application of heat (which minimises total heat) via a laser and firing specialised carbide (a binary compound consisting of carbon and a more electropositive element) powders onto the surface to be welded. The resulting weld is metallurgically sound and the minimal heat input required greatly reduces decomposition of the metals and improves the wear resistance of the finished surface.

Reclaimed (laser-clad) surfaces commonly last 2x-4x longer than the original component

One of the biggest benefits of the process is that it allows the reclamation of worn industrial products that require precision surfaces and are often discarded. A further benefit is that the process has been shown to materially extend the life of reclaimed parts (reclaimed surfaces are lasting for materially longer than the original piece). This has lead to some companies requesting LBL to "resurface" brand new equipment. Usual life extension is commonly in the range of two to four times expected lifetimes. In many cases, the biggest advantage of this life extension revolves around the reduction in down time of revenue generating machinery.

Figure 1: LaserBond ™ schematic



Source: Company

LBL has now developed three LaserBond™-cladding systems. The inner laser equipment is purchased from a German supplier and LBL has developed the powders and robotics necessary to ensure the required precision of the system. Two systems are in Sydney with the third now in operation in Gladstone. Development and construction cost for a new LaserBond™ cladding system is approximately $2m.

We estimate LBL can generate approximately $5.5m of revenue directly attributable to each LaserBond™ cladding equipment set

Thermal Spraying

High Pressure High Velocity Oxy-Fuel: This process involves spraying the molten droplets of coating at extremely high velocity. The process greatly increases wear resistance.

Electric Arc Spraying: Electric arc spray devices are thermally efficient and, because there is no flame or plasma, little heat is transferred to the part being coated. This process is predominantly used for budget-focussed rebuilds.

Plasma Arc Spraying: This process involves materials that can be sprayed through an arc in a plasma forming gas. As the plasma gas is heated by the arc, it expands and is accelerated through a shaped nozzle.

Has its own laboratory

LBL is focused on continual improvement and can tailor solutions to individual client needs. LBL continually develops and tests new techniques and metal combinations. The laboratory allows tuning of surface equipment system parameters and coating of materials as well as bond strength testing and hardness testers. The metallurgical powders used in the weld are imported, largely from China.

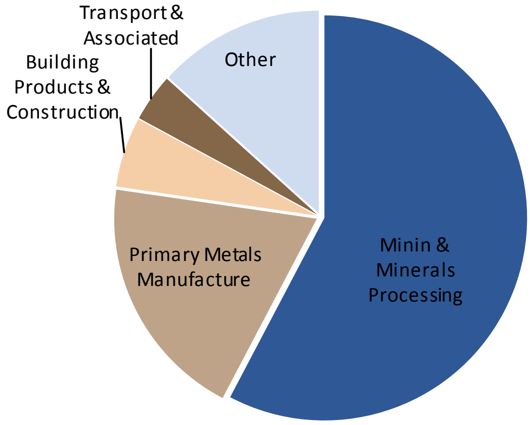
Customer base and focus industries

LBL is heavily focused on the mining & minerals processing sector as highlighted by Figure 2; this increased following the entry into the Queensland market. 97% of sales come from the states in which LBL operates (NSW & Qld), further highlighting the importance of geographic growth. Repeat customers currently account for 90% of sales.

Laser-cladding accounts for 45% of sales

At present around 45% of sales are directly attributable to LaserBond™ cladding. General machining work accounts for 30-35% of revenue—this work increased as a share of revenue following the Peachey's Engineering (Qld) acquisition and is likely to fall as the Queensland operation begins to move customers across to its laser clad options. The balance is attributable to the thermal spray facilities including HP HVOF process that LBL can offer.

Figure 2: Revenue split 1H12*



Source: Company
**2H12/FY12 not yet available*

Key customer —Weir Minerals (Weir Group PLC)

Weir Minerals is LBL's largest customer. Weir now accounts for up to 30% of group sales. It is part of UK-based Weir Group PLC (£3.6 billion market cap). Weir Minerals designs and manufactures slurry handling equipment, including pumps, hydrocyclones, valves, and other complementary equipment primarily for the mining, flue gas desulphurisation and oil sands markets.

Weir Minerals has been crucial to LBL's development of laser cladding and HP HVOF, as well as its revenue growth, for the past 20 years. Sales to Weir have outpaced group sales growth in recent years. and

New customers take time—new dedicated sales managers

Laser cladding in the industrial space is a relatively new process. Throughout the 1980s and 1990s a range of new techniques for the reclamation of worn and corroded industrial products entered the market with widely varying levels of performance—often wildly underperforming expectations.

With this in mind, many companies and their procurement and engineering departments are hesitant to try another reclamation system. Most new customer wins to date have been based on referrals from existing customers. Customers will send a portion of their worn "reclaimables" for restoration and then run internal testing on those components before gradually directing a larger portion of their relevant work to LBL.

More recently, and with a decade of track record for its systems, LBL has been able to provide potential new customers with case studies such as the Bluescope (ASX: BSL) case study provided in LBL's company update release of 16 April 2012—BSL tested a LaserBond™ reclaimed welder carry-over roll, which normally last six weeks, and has found it to still be usable some 4.5 years later—usual life extension is commonly in the range of 2x-4x.

LBL appointed new dedicated sales managers in 2012. This role will be focused on introducing new industries and companies to LBL's offering (transport [rail] remains a focus).

Main customer:

- **Weir Minerals**

Other blue-chip customers:

- **Alcoa**
- **Bluescope**
- **Rio Tinto**
- **QR National**
- **UGL**
- **Loy Yang**
- **Joy Mining Machinery**

Competition and alternatives

Equipment replacement

At present much of the equipment that could be re-engineered and repaired by LBL's processes is simply replaced with new parts. The tyranny of distance looms large, given the remote and disparate nature of mining operations and the costs of transport to and from the west to east coast to deliver parts to LBL's east-coast base.

Other laser cladding providers

Brenco: Brenco is a similar sized business based in Melbourne. It has additional sites in Brisbane and Perth and will soon open a facility in Singapore. Brenco focuses on both aerospace applications (it has deals with Rolls Royce and Qantas) and surface engineering (oil & gas industry focus). The business has spent periods as a subsidiary of both Repco and Muswellbrook Energy and Minerals. Its current business was formed in 1991 through a management buyout.

Hardchrome: Hardchrome's processes and technologies cover a wide range including laser cladding (4kW fiber laser), chrome and nickel plating, hydraulic component repair and manufacture, application of polymeric, metallic and composite coatings and fully automated and computerised heat treatment and nitriding furnace technologies.

There are also smaller single-site operators in each state.

Laserline—Germany

We understand that LBL has sourced laser equipment from Laserline and that both Brenco and Hardchrome use Laserline equipment (imported by Raymax). Laserline was established in 1997. It focuses on production of laser cladding equipment and has over 85 employees.

Other laser-cladding equipment manufacturers

A range of predominantly German and US based companies manufacture laser welding and cutting equipment. The majority of these companies are of a similar size to LBL, however, TRUMPF of Germany manufacturers a laser welding/cladding technology among a broad range of industrial products:

TRUMPF (Germany)

TRUMPF engages in the production and sale of manufacturing equipment, photonics, and medical technology worldwide. It provides machines for laser cutting, welding and processing among a range of product categories.
Revenue: €2,024m
EBITDA: €269m

Others

- FW Gartner Thermal Spraying (US): Primary markets include refining/ petrochemicals/oil and gas, power generation, valves, marine, pulp and paper, and military (Revenue: $16.7m).
- Optomec (US): The company offers lens systems that are used to fabricate, enhance, and repair high-value metal components (Revenue: $5.6m).

*revenue estimates drawn from Capital IQ

Historical financials

NSW providing solid organic revenue growth

NSW has provided the bulk of LBL's growth over the past three years. Margins were impacted in 2012 as LBL began its NSW expansion program taking on increased rental costs and a larger sales force. The Queensland operation has had to contend with "boom town" pricing for labour, accommodation and transport. This has been hard to pass on to the existing customer base, not all of which is working in or for the mining or LNG industries that dominate the area. Both NSW and QLD operations were impacted by a reportedly industry-wide slowdown in maintenance and capex spend between February and April this year. The slowdown was enough to push QLD operations back into the red in 2H12.

Figure 3: Revenue by segment

	New South Wales			Queensland		
	FY10	FY11	FY12	FY10	FY11	FY12
Revenue	5.89	8.16	9.79	4.53	5.12	4.59
PBT	1.13	2.00	1.99	-0.52	0.05	-0.40
Margin %	19.1%	24.5%	20.3%	-11.4%	0.9%	-8.7%

Source: Company

Balance sheet

LBL runs a very conservative balance sheet, with net debt of $0.6m (ex capital raising—reported net cash of $1.4m at 30 June 2012) and a working capital (current) ratio of 3.3x. It is important to note that approximately half of LBL's property plant and equipment is reported as an operating lease expense. Operating lease commitments totalled $1.5m at 30 June 2012, with $0.6m falling due during FY13. Lease expenses were $0.47m for FY12. LBL's auditor has requested a change in LBL's treatment of leases—LBL will record leases on new equipment as financial leases. This will bring new assets onto the balance sheet along with an offsetting liability. Over time it will lead to an apparent EBITDA improvement as operating leases expensed above the EBITDA line wind down and finance lease costs move below the line.

Figure 4: Balance sheet

$m	FY11a	FY12a
Cash	1.0	2.8
Receivables	3.3	3.6
PPE	0.7	1.8
Intangible	3.6	3.6
Other	1.8	2.0
Assets	**10.3**	**13.8**
ST debt	0.1	0.4
Payables	1.1	1.4
LT debt	0.5	1.0
Other	1.1	-0.1
Liabilities	**2.7**	**2.7**
Net Assets	**7.0**	**10.2**
NTA	**3.4**	**6.6**
NTA/sh	**0.097**	**0.122**

Source: Company; Investorfirst estimates

EBIT margin now above 10%

Figure 5 (below) displays LBL's historical group margin and earnings growth. EBIT margins have held consistently above 10% since 2H10 and the EBIT margin is likely to average over 15% across FY13.

Figure 5: LaserBond income statement

	1H09	2H09	FY09	1H10	2H10	FY10	1H11	2H11	FY11	1H12	2H12	FY12
Sales	2.9	6.1	8.9	5.4	5.0	10.4	6.0	7.3	13.3	7.7	6.7	14.4
EBIT	0.2	0.4	0.6	0.2	0.6	0.7	0.7	1.5	2.1	1.1	0.8	2.0
Margin	*5.8%*	*7.4%*	*6.9%*	*3.1%*	*11.1%*	*7.0%*	*11.1%*	*20.2%*	*16.1%*	*14.9%*	*12.3%*	*13.7%*
Profit pre-tax	0.2	0.0	0.2	0.2	0.5	0.7	0.6	1.4	2.0	1.1	0.5	1.6
NPAT rep	0.1	0.1	0.2	0.1	0.4	0.6	0.4	1.0	1.3	0.8	0.3	1.1
NPAT adj	**0.1**	**0.3**	**0.42**	**0.1**	**0.4**	**0.47**	**0.4**	**1.0**	**1.43**	**0.8**	**0.5**	**1.32**
Margin	*4.0%*	*5.1%*	*4.7%*	*2.0%*	*7.1%*	*4.5%*	*7.2%*	*13.7%*	*10.8%*	*10.1%*	*8.2%*	*9.2%*

Source: Company; Investorfirst estimates **first period including Peachey Engineering (Gladstone)*

Growth opportunities

$2.1m capital raising provides funding for growth

LBL raised $2.1m through the issue of 9.1 million new shares at 23 cents each in May 2012. This capital has been earmarked for acquisitive growth. We understand LBL is reviewing a range of opportunities, particularly in South Australia and Western Australia.

Geographic expansion (Gladstone)—learning by doing

LBL's first foray into geographic expansion, into Gladstone, QLD, hasn't been without challenges. The November 2008 timing of the purchase of long-time customer Peachey's Engineering has proven to have been less than ideal. This was compounded by unforeseeable circumstances related to the senior management of that business. Each of these headwinds were largely outside of LBL's control. The GFC downturn led to reduced fabrication work that had been the higher-margin provider in the Peachey operation—fabrication has picked up in the past six months and has been supported by the installed and operational LBL LaserBond™ cladding equipment.

Labour costs are the largest on-going challenge for operations in resource-based regions

An on-going challenge in Gladstone—and one that will likely be a challenge out west—has been spiralling labour costs as LBL competes with multinational resources and energy companies for finite skilled labour. LBL has been working with customers to pass-through cost increases to cover these wage costs.

However, all of these challenges have seen LBL remain very vigilant with regard to its cost base (see NSW site expansion over page) and the Gladstone operation is now operationally cash-flow positive. This has allowed LBL to finally expand its core NSW operations and given the board the option of looking at new regions for growth.

Geographic expansion—Perth & SA in focus

LBL is currently looking at opportunities for expansion into Western Australia or South Australia. Growth will not be forced with management stating that it will only purchase existing profitable operations "one at a time". LBL is particularly interested in businesses with owners a few years shy of retirement and lacking a succession plan.

Actively seeking opportunities for acquisitions in Perth and South Australia

The focus on existing profitable businesses will allow LBL to integrate its laser-cladding technology properly, given its limited skilled laser technicians. Training took six months in Gladstone, with LBL's trainer staying in Gladstone for the better part of a year to ensure the skills and processes were fully bedded down.

Cost of growth—we estimate $5 million per site

Peachey's Engineering cost LBL just over $3m in cash and shares (of which ~$2.5m was cash). It costs LBL another $2m to build and commission each laser cladding system. This includes installation on site. LBL believes acquisitions of the size of Peachey's are appropriate to give it the scale of sales, floor space and infrastructure (eg. heavy lift cranes) it needs to justify installation of its laser-cladding equipment.

The addition of LaserBond™ cladding capacity is majority funded through a finance lease. EBITDA margins will gain an accounting based lift as new equipment is recorded under financing versus the current operating leases.

Growth opportunities continued

NSW site expansion to 5,400m^2 doubles NSW capacity

NSW is running beyond capacity (some 3rd party storage has been secured near existing operations and LBL's car park hasn't been able to take cars for several months). This space bottleneck was a known problem for the past two years, however, the focus on preserving capital to support the QLD operation meant that site relocation was delayed.

NSW site expansion to double available space in Sydney

A new site with twice the floor space of the current combined sites has been secured. This will allow organic growth in the NSW operations for several years without the need for further major capex. LBL is currently in the process of moving to this site. Management expects the process to take one to two months as the move plan ensures that only one of its two NSW laser cladding systems will be offline at any time. We have factored in an additional rental expense of $300k for this site over the existing NSW rental expense. This should be absorbed by the capacity increase the site will allow.

Challenge of operating three sites separated by 5,000km

Executive directors Greg and Wayne Hooper are integral in the running of the business' core NSW operations. To make a successful transition to a larger business with a national footprint, management will need to spread time across the entire group, which will have the effect of ceding some day-to-day control of the Sydney operations.

Growing board experience

The board consists of the founding family plus two business advisors. In our view, the business could be strengthened through the inclusion of an independent director drawn from industry who could provide LBL with valuable insight into the existing networks and opportunities within LBL's markets of interest.

The appointment of a well-known and well-regarded director from among LBL's existing or potential customer base may also shift investor perceptions as a credibility "tick" and demonstration of an intention to evolve in the listed environment.

LBL's potential earnings over a business cycle

An on-going challenge for LBL could be something that similarly effects agricultural input manufacturers. When conditions are great then the need for fertiliser/feed diminishes; if the weather turns, then there is a boom period for these manufacturers where farmers fertilise/feed to keep their yields up in anticipation of good conditions returning; but, should the downturn be prolonged, they may simply stop farming.

A period of softening commodity prices would likely focus miner's attention on cost management—this would be LBL's golden time

In the same way, there is a possibility that in times of booming demand and prices for hard commodities, miners and their direct suppliers may simply find it easier to splash the cash on replacement equipment. A period of softening prices would likely focus their attention on cost management—**this would be LBL's golden time** where it is relatively inexpensive and long-lasting reclamations would be most highly valued. The risk though is that a continuing downturn in hard commodity prices may induce some mines to simply cease production, reducing demand for LBL's services.

Outlook

FY13 will see LBL move from its recent focus on running lean to fund QLD back towards a growth orientated business. Additional costs will include a doubling in the size of its Sydney workspace and a rental increase in Gladstone. A further impost will come in the form of building a stronger sales team in NSW and QLD following the appointment of the national sales manager.

These cost rises should be initially offset by improved productivity and increased fabrication contract work out of Gladstone. Longer-term, both the NSW site expansion and new sales manager should help drive revenue growth, however the Gladstone rent hike is a cost of doing business in a mining boom town.

New customers and industries

LBL announced in April 2012 that it had won a competitive tender to supply Alcoa worldwide with its LaserBond™ cladding pump shaft sleeves. Projected revenue of $500,000 is modest but the contract highlights the regard with which LBL and its laser-clad work is held by large multinationals.

While LBL is focused on growing its recurring income it still acknowledges that it is in large part a “job-shop”, which poses a challenge in terms of timing of workload and the revenue that it generates. A large job falling either side of a reporting date could have a material impact on the apparent profitability of the business.

There are more moving parts in FY13. There is recently commenced NSW shop relocation. This should cause minimal disruption as one of the existing sites will operate while the other is moved—and there are two lasers in NSW. While planning says it should be fine the proof will be in the pudding.

Gladstone’s performance is going to be determined by uptake of the laser-clad service and bespoke fabrication projects. We are forecasting 7% sales growth for Gladstone, much of which should be achieved through better capacity utilisation, with some offset for higher labour and rent costs. We are forecasting revenue of $4.9m for an EBITDA pre corporate allocation of $0.6m.

After taking into consideration the loss of six weeks revenue to allow for downtime in equipment moves to the new site should still lead to growth in Sydney’s revenue line in FY13, without further rental increases. We are forecasting revenue growth of 9.3% over FY12 to reach $10.6m. Our EBITDA pre corporate costs is forecast at $2.5m. This takes into account an uplift in sales as room constraints are lifted in the NSW operation.

FY13 forecasts

Formal FY13 forecast—on-going operations only

We forecast the current LBL business to generate revenues of $15.5m in FY13. Our FY13 group EBITDA estimate under this base case scenario is $2.5m. A summary table of revenue by site and expected margins can be found on the following page. Further detail can be found on our financials summary on page 13.

We are forecasting a 27.3% increase in reported net profit after tax to $1.4m in FY13 in the event that no acquisition is completed. However, we estimate this would equate to only a 7.6% increase in earnings per share to 1.63cps following the May 2012 equity issue.

The changed lease reporting will see a reduction over time in lease expense and an approximately offsetting increase in both depreciation charge and reported interest expense.

Potential acquisition scenario

Due to uncertainty around timing and size of any acquisition we do not build a acquisitions into our formal forecast. However, we view it as a distinct possibility that LBL will complete an acquisition during fiscal year 2013. We have considered a scenario where it does so on January 1, 2013. We assume a total cost of $5m, paid for out of cash, shares and lease financing (as discussed on page 7). This is broadly in line with management's stated objective. The cash portion will be funded out of the recent equity issuance which raised $2.1m. We assume two million new shares are issued to the vendor at 20 cps.

Margins used for the prophesied acquisition are mid-way between those forecast for the established NSW operation and the QLD operation (see page 6). QLD and NSW operations are unaffected by this change. We estimate an additional corporate cost of $0.2m which is primarily attributable to executive wages. This acquisition is premised on an additional $3.5m revenue in its first six months and an EBITDA pre corporate costs of $0.5m. Mid-to-long term growth rates used are as per existing site (see below) for our acquisition case.

Under this scenario total FY13 revenue is forecast at $19.0m leading to an EBITDA of $2.9m and an NPAT of $1.7m and EPS growth of 29.6% to 1.97cps.

Medium term assumptions—all scenarios

In FY14 & 15 we use 5% per annum revenue growth and no further acquisitions. For FY16 we reduce revenue growth to 3% and beyond this we apply a 3% terminal growth rate. We apply an EBITDA margin of 16% throughout the period beyond FY13 (FY11 17.3% / FY12 16.2%).

Figure 6: FY13f & M&A scenario

	FY13f
Sydney	
Revenue	10.6
EBITDA pre-corporate	2.5
Margin	*23.5%*
Gladstone	
Revenue	4.9
EBITDA pre-corporate	0.6
Margin	*13.0%*
Total - ex acquisition	
Revenue	**15.5**
EBITDA pre-corporate	3.1
Corporate	0.6
EBITDA	**2.5**
Margin	*16.0%*
Int, Tax, D&A	1.1
NPAT	**1.4**
Acquisition Scenario*	
Revenue	3.5
EBITDA pre-corporate	0.5
Margin	*13.0%*
Total - acquisition	
Revenue	**19.0**
EBITDA pre-corporate	3.6
Corporate	0.7
EBITDA	**2.9**
Margin	*15.4%*
Int, Tax, D&A	1.2
NPAT	**1.7**

Source: Investorfirst estimates
**Assumes six-month contribution*

Valuation: $0.235 a share

$0.235 valuation leads to Buy recommendation

With 10 years of experience and a growing book of positive referrals, LBL is enjoying strong growth and is expanding its NSW base to meet this demand.

We initiate with a Buy rating and $0.235 a share valuation. LBL is well placed to enjoy significant growth in the coming years as its LaserBond™-cladding offering gains recognition and acceptance in its various markets.

Peer comparison is limited due to the specialist nature of LBL's business.

Our valuation is a blend of our base case and acquisition case valuation (50/50). Each of those valuations is comprised of a 50/50 blend of our discounted cash flow (DCF) valuation and FY13f EV/EBITDA at 6.5x. Given LBL's small size and the risks involved in expansion we apply a cost of capital of 13.7%; LBL holds a net cash position.

Maintenance capex spend & the addressable market

A constant focus of the established businesses is planning and managing its maintenance, repairs & operational (MRO) expenses procurement and delivery requirements.

$18 billion spent on maintenance capex in Australia

We have made a back-of-the-envelope estimate of maintenance capital expenditure required to maintain Australia's current installed property, plant & equipment (PPE). This was based on depreciation expense attributable to PPE on a range of Australian and international materials, energy, industrial and auto component companies that report an Australasian sales segment. The results of this screen indicated that these companies would need to spend an amount equivalent to 7.6% of sales (or 8.0% of net PPE) on maintenance capital expenditure annually to maintain their current level of PPE[7].

If we make a broad assumption that 50% of PPE relates to Plant & Equipment then this equates to $9.3 billion of maintenance capex in Australia. LBL could materially increase its revenue base without causing much more than a ripple in the market for replacement parts and equipment in Australia.

Addressable market

While these vast sums suggest there is plenty o scope for LBL's growth it is important to note that LBL's offering applies to specialist parts within equipment and not full refurbishments. A mining services peer noted that of a $2m piece of equipment, the wear plate component that is suitable for laser-clad refurbishment may cost $100,000 (5% of total value) to replace—which leads us back to the risk of site managers being lazy in the good times when percentage of total cost is small. LBL will likely have to rely on its reduced downtime over the medium to long term to win these customers.

Australian planned commodities project capital expenditure

BREE's recent Australian commodities project outlook[1] estimates that there is currently A$260 billion worth of planned capital expenditure related to new minerals and metals projects in Australia. BREE's expectation is for total capital expenditure of A$80 billion in 2011-12. Most planned expenditure is in Western Australia (61%) and Queensland (28%) - which helps to explain LBL's interest in developing in these markets.

So, while difficult to measure precisely, the overall indication is that the market for replacement parts and machinery in Australia is likely in the tens of billions of dollars annually. Of relevance to LBL is that in a market of this size, it should be able to achieve material revenue growth while continuing to fly under the radar of global competitors. Avoiding the wrath of these well-funded competitors (likely through development of competing offerings), will be important while establishes itself as the pre-eminent laser-cladding industrial product reclamation company.

[1]Capital IQ data screening
[2]BREE, "Mining Industry Major Projects—April 2012"

Risks

We believe the following to be among the key risks to LBL's operations. This list should not be considered exhaustive.

- **Replacement parts become materially cheaper:** At present LBL's biggest competition comes direct from OEMs in the form of replacement parts. Should OEMs begin to offer materially cheaper spares then this would negate a key point of difference for LBL.
- **Competition:** LBL's technology in this form is relatively new. It is possible that larger companies may be able to fabricate their own laser cladding system to compete with LBL and others. LBL's decade of experience and expertise negates some of its size disadvantage.
- **Securing labour:** This has proved to be challenging in the company's QLD operations, where LBL competes with multinational scale companies for skilled and unskilled labour. We foresee this being a challenge on any move to Perth or South Australia as well. The lack of labour availability means wages have been driven higher in those regions impacted by materials and energy exploration and mining.
- **Reliance on key customer:** Weir Minerals represents approximately 30% of LBL's revenue at present. Should Weir move its business away from LBL this would have a materially negative impact on LBL's operations.
- **Reliance on key management:** Greg Hooper's experience and expertise in the development of laser cladding has been the driving force in the growth of the company. The Hooper family has indicated it is committed to the long-term future of LBL. Should that position change it would represent a key risk.
- **Raw materials pricing:** Raw materials (primarily metals and their powder derivatives) are subject to global commodity pricing, with local costs subject further to exchange rate movements.
- **Commodity prices:** Commodity price rises have driven the growth in exploration and mine development in the past decade. Exceptionally strong commodity prices could lead to lazy procurement departments simply buying new parts. Conversely, a steep fall in commodity prices could see mines become uneconomic and close down.
- **Broad economic conditions:** A material portion of LBL's revenue is derived from "traditional" manufacturers that have been subject to years of headwinds. A further deterioration in economic conditions from the perspective of these customers could see them close operations, which would impact on LBL.
- **Liquidity risk:** From an investor's perspective there is a liquidity risk to investing in LBL. The company is small and approximately 46% of shares are still owned by founders and acquires. On average 98,163 shares trade each day (that equates to ~$21,600 a day).
- **Execution risk on acquisitions:** LBL needs to grow to ensure its relevance in the market place. It has stated that it is looking at moving west to Perth and South Australia. Each of these proposals involves execution risk—as was the case in QLD (QLD did have specific circumstances that are unlikely to be repeated and were unforeseeable).
- **Key equipment:** A breakdown of key equipment (laser or HVOF) could cause a short to medium term impact on the company.
- **Site relocation:** A short-term risk relates to LBL's move to its new facility, scheduled to take place in 2HCY12. Risks relate to reinstalling the laser equipment and delays causing lost work time.

Laserbond

ASX code LBL	Recommendation: Buy	Share price	$0.150
Bloomberg LBL AU	Valuation: $0.235	No. shares	84.7m
Reuters LBL.AX	Financial risk: 8.03 (Z Score) -2.29 (M Score)	Options etc.	0.0m
	BASE CASE SCENARIO - NO ACQUISITION	Market cap	$12.7m

$m — Financial year end: June 30

Income Statement	FY10a	FY11a	FY12a	FY13f	FY14f
Operating revenue	10.4	13.3	14.4	15.5	16.8
EBITDA	0.93	2.30	2.29	2.48	2.54
Deprec & Amort	-0.21	-0.16	-0.36	-0.41	-0.44
EBIT	0.73	2.14	1.92	2.07	2.10
Net interest expense	-0.06	-0.10	-0.08	-0.09	-0.08
PBT	0.67	2.04	1.84	1.98	2.02
Non-recurring items	0.00	0.00	-0.25	0.00	0.00
Tax Expense	-0.11	-0.70	-0.47	-0.59	-0.61
Equity-accounted	0.00	0.00	0.00	0.00	0.00
Reported net profit	**0.56**	**1.34**	**1.12**	**1.38**	**1.41**
Adjusted net profit	0.47	1.43	1.29	1.38	1.41
Adjusted EPS ₵	**0.67**	**2.02**	**1.74**	**1.63**	**1.67**
Dividends per share ₵	0.000	0.005	0.005	0.006	0.006

First half review	1H10a	1H11a	1H12a	1H13f	1H14f
First half revenue ($m)	5.42	6.02	7.77	7.77	8.65
First half EBITDA	0.27	0.74	1.25	1.21	1.29
First half adj net profit	0.11	0.43	0.78	0.67	0.72

Cash Flow	FY10a	FY11a	FY12a	FY13f	FY14f
Reported net profit	0.56	1.34	1.12	1.38	1.41
Deprec & Amort	0.21	0.16	0.36	0.41	0.44
Working capital	-2.30	-0.59	-0.81	0.52	-0.20
Others	0.00	0.00	0.00	0.00	0.00
Net operating cash flow	**-1.54**	**0.90**	**0.67**	**2.31**	**1.65**
Capex	-0.21	-0.12	-1.52	-0.48	-0.25
Acquisitions	-0.26	-0.15	0.01	0.00	0.00
Others	0.00	0.00	0.00	0.00	0.00
Net investing cash flow	**-0.46**	**-0.27**	**-1.51**	**-0.48**	**-0.25**
Change in debt	0.13	-0.07	0.00	0.00	0.00
Equity issuance	0.46	0.00	1.91	0.12	0.00
Dividends	0.00	0.00	-0.29	-0.49	-0.49
Other	0.00	0.00	1.01	0.00	0.00
Net financing cash flow	**0.59**	**-0.07**	**2.63**	**-0.37**	**-0.49**
Net cash flow	**-1.41**	**0.56**	**1.80**	**1.46**	**0.90**

Balance Sheet	FY10a	FY11a	FY12a	FY13f	FY14f
Cash	0.42	0.98	2.78	4.24	5.15
Receivables	2.27	3.28	3.61	3.19	3.34
Inventory	1.61	1.55	1.77	1.67	1.81
Other	0.00	0.00	0.00	0.13	0.14
Total current assets	**4.30**	**5.81**	**8.17**	**9.23**	**10.44**
PP&E	0.69	0.65	1.80	1.88	1.69
Intangibles	3.46	3.61	3.61	3.61	3.61
Other non-current	0.27	0.27	0.24	0.24	0.24
Total non-current assets	**4.42**	**4.53**	**5.65**	**5.73**	**5.54**
Total assets	***8.72***	***10.34***	***13.82***	***14.96***	***15.98***
Current debt	0.10	0.09	0.42	0.42	0.42
Payables	1.09	1.10	1.41	1.34	1.42
Provisions	0.00	0.65	0.51	0.55	0.58
Other	0.89	0.82	0.16	0.30	0.30
Total current liabilities	**2.08**	**2.66**	**2.50**	**2.62**	**2.72**
Non-current debt	0.27	0.45	0.99	0.99	0.99
Other	0.22	0.25	0.11	0.11	0.11
Total non-current liabilities	**0.49**	**0.70**	**1.10**	**1.10**	**1.10**
Total liabilities	***2.56***	***3.36***	***3.60***	***3.72***	***3.82***
Net assets	***6.16***	***6.98***	***10.22***	***11.24***	***12.16***

Valuation Metrics	FY10a	FY11a	FY12a	FY13f	FY14f
Price / earnings (adj)	22.2x	7.4x	8.6x	9.2x	9.0x
EV/EBITDA	12.2x	4.9x	5.0x	4.6x	4.5x
EV/EBIT	15.6x	5.3x	5.9x	5.5x	5.4x
Dividend yield	0.0%	3.3%	3.3%	3.9%	3.9%
Current price / book			1.2x		
Current price / NTA			1.9x		

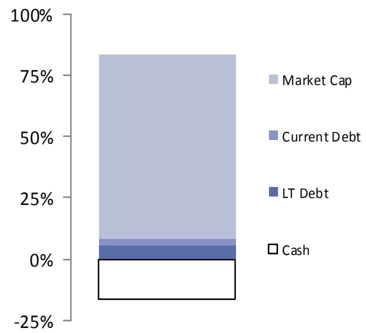
Margins	FY10a	FY11a	FY12a	FY13f	FY14f
EBITDA margin	8.94%	17.31%	15.88%	15.99%	15.17%
EBIT margin	6.96%	16.12%	13.36%	13.35%	12.54%
PBT margin	6.39%	15.38%	12.80%	12.77%	12.06%
Adj. net profit margin	4.47%	10.77%	8.96%	8.94%	8.44%

Growth	FY10a	FY11a	FY12a	FY13f	FY14f
Revenue growth	15.0%	27.4%	8.4%	7.7%	8.2%
EBITDA growth	30.6%	146.6%	-0.6%	8.4%	2.6%
EPS growth	n/a	198.9%	-13.6%	-6.1%	2.1%

Du Pont Analysis (reported ROE)	FY10a	FY11a	FY12a	FY13f	FY14f
Operating profit margin	7.0%	16.1%	11.6%	13.4%	12.5%
Asset turnover	128.5%	139.3%	119.1%	107.6%	108.3%
Interest expense rate	0.7%	1.0%	0.7%	0.6%	0.5%
Equity multiplier	141.7%	145.1%	140.4%	134.1%	132.2%
Tax retention rate	83.5%	65.5%	70.3%	70.0%	70.0%
Return on equity	**9.7%**	**20.4%**	**13.0%**	**12.9%**	**12.1%**
Net tangible assets	2.69	3.37	6.61	7.63	8.55
Net debt (cash)	-0.06	-0.44	-1.37	-2.83	-3.73
W/av diluted shares on issue	**69.1m**	**71.2m**	**76.3m**	**84.7m**	**84.7m**
Share Outstanding	**69.1m**	**72.1m**	**83.9m**	**84.7m**	**84.7m**

Segment Sales

Capital Structure



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Research Ratings Methodology

Sell: Valuation < (Share Price X 0.9)
Hold: Valuation > (Share Price X 0.9) < Share Price
Buy: Valuation > Share Price

Speculative (in addition to Buy/Hold/Sell): no history of positive earnings or cash flow; or highly geared; or highly volatile & inherently uncertain earnings

Financial Risk Metrics

General Z-Score: indicator of risk of bankruptcy

- <1.1: may be in financial distress
- 1.1 to 2.6: potential warning of financial distress
- >2.6: may be in good financial shape

Beneish M-Score: indicator of potential earnings manipulation. A result below –2.22 indicates no apparent manipulation of financial results