MICROCAP COMPANY RESEARCH

19th March 2012

LaserBond Limited

GICS: **Industrials – Commercial & Professional Services**

First Half Results...

Recent News

LaserBond Limited [ASX:LBL] announced its first half results with solid growth in both sales and underlying profit. NSW and QLD divisions demonstrated steady growth for the period. We reiterate FY12 EBIT and NPAT guidance of $2.9m and $2.1m respectively.

1H FY12

Event

- **1H12 results:** LaserBond is on track to meet FY12 EBIT and FY12 NPAT guidance of $2.9m and $2.1 respectively. First half NPAT was up 117% to $0.79m on the back of a 28.3% rise in revenue to $7.65m.
- **Strong growth all round:** LaserBond (NSW) posted strong performance of 34.5% half-on-half revenue growth and Gladstone (QLD) division grew its top line by 16.9% compared to 1H11. The QLD division is still making losses, but significantly cut its losses, on successful cost cutting measures and efficiency improvement.

View

- **Solid earnings in FY12:** We maintain our FY12 revenue and EBIT forecasts to $16.5 and $2.9m (FY12 EBIT margin: 17.8%) respectively. These forecasts reflect strong half on half revenue growth and healthy margin assumptions.
- **Exposure to resources boom:** Circa 45% of LaserBond's revenue is related to resources extraction and processing. Continued growth in mining investment in FY12-13 will drive increases in revenue
- **Full year dividends:** We maintain our expectation of a 0.5c full year dividend, representing a 18% payout ratio based on our 2.8c EPS forecast.
- **Potential acquisitions:** Management has flagged potential acquisitions in WA. Whilst not factored into our modelling, acquisitions could provide added upside to our valuation.

Valuation

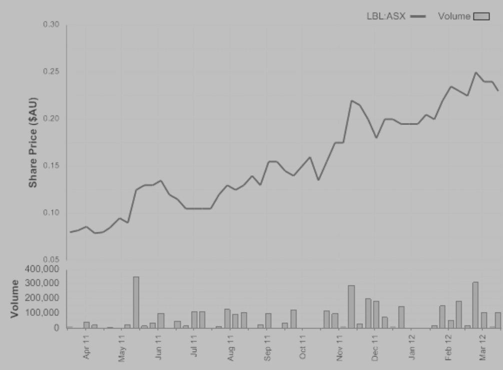
We maintain our **BUY** recommendation despite the recent run up in the share price. We raise our price objective from $0.28 to $0.32, representing a 30% premium to the last traded price of $0.245. LBL remains on a very attractive FY12 EV/EBIT multiple of 6.0x. Its favourable organic growth profile, efficient cost management and upside from future acquisitions justify our recommendation.

LBL | **BUY**

Price Objective: **$0.32**

Last traded	A$	0.245
Market Cap	A$'m	18.2
Nº of Shares	m	74.3
2011A EPS	¢	1.8
2012e EPS	¢	2.8
2012e PE	x	8.5
2012e EV/EBITDA	x	5.7
DPS 2012e	¢	0.5
Div Yield 2012e	%	2.9
Revenue 2011A	m	13.5
Revenue 2012e	m	16.5
EBITDA 2011A	m	2.3
EBITDA 2012e	m	3.1
NPAT 2011A	m	1.3
NPAT 2012e	m	2.1

Share Price | 1 Year



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IMPORTANT DISCLOSURE INFORMATION AT THE END OF THIS REPORT

FIRST HALF UPDATE

LBL: HALF-YEAR FIANCIAL RESULTS

Figures in A$m	1H FY12	1H FY11	Change
Revenue	7.65	5.96	28.4%
COGS	4.02	3.11	29.3%
Gross Profit	**3.63**	**2.86**	**26.9%**
GP Margin, %	*47.4%*	*47.9%*	
Other Income	0.10	0.05	100%
Operating Expenses	2.50	2.17	15.2%
EBITDA	**1.22**	**0.74**	**64.9%**
EBITDA Margin, %	*16.0%*	*12.3%*	
D&A	0.11	0.08	37.5%
EBIT	**1.12**	**0.66**	**69.7%**
EBIT Margin, %	*14.6%*	*11.0%*	
Net Interest	0.01	0.04	-75%
Profit Before Tax	**1.11**	**0.61**	**82%**
Tax	0.32	0.25	82%
NPAT	**0.79**	**0.36**	**119%**
NPAT Margin, %	*10.3%*	*6.1%*	
EPS (basic)	1.07	0.51	110%

SOURCE: COMPANY DATA, MICROEQUITIES ESTIMATES

Revenue up 28.3%, EBITDA up 65% and NPAT up 117%

LBL delivered a strong first half result in our view. The demand for LBL's surface engineering services has increased and resulted in credible operating performance for the period. Both NSW and QLD divisions posted solid growth in sales (NSW division up 34.4% to $5.2m and QLD division up 16.9% to $2.45m) and operating profit (mainly due to NSW division and partial losses recovery in QLD division), translating into a spectacular 110% increase in EPS (1.07 cent per share) on pcp. Moreover, cost growth was contained lagging behind increase in revenue, thus resulted in stronger operating margins.

Strong divisional performance at both top and bottom line levels

LBL: BALANCE SHEET

Figures in A$m	1H FY12	1H FY11	Change
Cash	1.06	0.98	8.2%
Current Assets	6.23	5.81	7.2%
PP&E	0.58	0.65	-10.8%
Total Assets	**10.69**	**10.34**	**3.4%**
ST Debt	0.08	0.09	-11.1%
LT Debt	0.42	0.45	-6.7%
Total Liabilities	**3.00**	**3.36**	**-10.7%**
Equity	**7.68**	**6.98**	10%
Conv. Notes	0.35	0.47	**-25.5%**

SOURCE: COMPANY DATA, MICROEQUITIES ESTIMATES

Conservative debt and working capital policy

The company's financial position is solid, given the net cash position. Debt stood at $0.5m versus a cash balance of over $1.06m as at 31 Dec 2011. Net Working Capital maintained at over $4m, with current assets (without cash balance) of $5.2m far exceeding trade payables of $1.2m.

Despite a circa 25% decline in absolute terms (mainly due to rising wages), operating cash flow stood at $0.35m leading to a further increase in the cash balance as at 1H FY12.

In April 2010, the company issued unsecured convertible notes with face value $350,000 to raise additional working capital. The repayment date of the notes and optional conversion to ordinary fully paid shares expires at 30 June 2012. The conversion price is determined as the lesser of either issue price of 15 cents per share or 85% of VWAP over the last 5 days that trades were recorded prior to the conversion date.

Notes conversion expected to complete in June 2012

As at 31 Dec 2011, $240,000 of notes remained unconverted with $120,000 notes converted into 800,000 shares (@15 cents per share) in Jan-Feb 2012. The outstanding $120,000 notes are expected to be converted by June, adding 1.6m shares or approximately 2.2% of LaserBond's share capital. The dilutionary impact has been factored into our EPS metrics.

Dividend payouts set to continue for the full year period

The Board declared interim dividend of 0.3 cent per share (FY11: 0.5 cent) fully franked that translated to a payout ratio of circa 28% of NPAT. The Board expects further positive growth, solid margins and stable financial position, thus we expect dividend payout is likely to continue.

SEGMENT PERFORMANCE

LBL: SEGMENT HALF-YEAR FINANCIAL RESULTS

	LaserBond (NSW)		LaserBond (QLD)		Consolidated	
Figures in A$m	1H FY12	1H FY11	1H FY12	1H FY11	1H FY12	1H FY11
Revenue	5.2	3.87	2.45	2.1	7.65	5.97
PBT	1.15	0.8	(0.04)	(0.19)	1.11	0.61
Assets	10.52	8.77	1.76	1.73	10.69	9.1
Liabilities	2.35	1.92	2.24	2.3	3.0	2.81
CapEx	0.03	0.01	0.02	-	0.05	0.01

SOURCE: COMPANY DATA, MICROEQUITIES ESTIMATES

LASERBOND (NSW)

The NSW division demonstrated impressive sales growth in 1H FY12 (Sales up 34.4% to $5.2m and PBT up 44% to $1.15m). The management expects the top-line growth to continue in the second half of the financial year but such a forecast is subject to the successful expansion of engineering capacity. The capital investments that is necessary to sustain further growth have been recently undertaken and the company aims to undertake the required further investment in the capacity.

The undertaken or ongoing investments include:

- New operational facility in Smeaton Grange, NSW. In July 2012, LaserBond (NSW) relocates to a new, purpose-built 5,400m^2 engineering facility that is currently under construction. Currently, LBL rents a temporary facility in Minto, NSW;
- Circa $2m capital expenditures in cladding and other equipment;
- Recruitment of a National Sales Manager who will be responsible for managing all sales and marketing activities as well as potential acquisitions.

LaserBond (QLD)

The QLD division posted solid sales growth in machining and cladding services (over 27% growth on pcp) but continuing contraction in project style (fabrication facilities) segment. However, the company has successfully developed its pipeline of projects in the segment that are expected to deliver growth in the second half of the year.

Margins were under further pressure due to growing engineering capacity and hiring of skilled professional staff (machinists and boilermakers). Real wages keep rising in and around Gladstone due to demand exerted by construction of LNG plants in the region. The company aims to manage the negative effects on margins by improving efficiency and reducing non-core costs.

With the growing machining, cladding work and promising pipeline of fabrication project work, LBL expects the division to deliver further growth and improvement in operating margins.

Expansion in other regions

Management continues to actively investigate different acquisition opportunities in Western Australia. Currently, the company has completed preliminary discussions with potential partners that could result in an actual acquisition during 2012 calendar year. LBL continues to focus on organic growth in NSW and QLD regions as there are a growing number of new and existing customers, predominantly from the resource and aluminum & steel manufacturing sectors, and extended engineering capacity (i.e. new facility in NSW and recent investments in cladding equipment).

FY12 UPDATE

LBL on track to meet our revenue and profit forecasts

We reiterate our forecasts for both FY12 and FY13. Management reaffirms that the company has all capabilities to deliver $8m+ revenue for the second half of FY12, bringing full year revenue to $16-17m. Margins are expected to stay at current levels with some potential to improve, given less pressure from rising wages and the ability to pass some costs on to customers. However, we should highlight that engineering services are contract-driven, usually short-term and sensitive to individual customer orders. This imposes the risk of insufficient contracts/order flow to generate additional revenue. Moreover, there is still a lot of uncertainty about individual contracts for the project style work in the QLD division.

LBL has largely completed its investment program (new operational facility in Smeaton Grange and purchases/repair of cladding equipment) with no plans for further significant capital expenditure in 2H12.

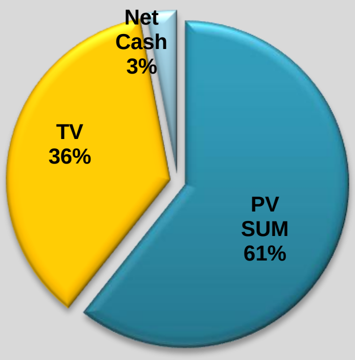
The convertible notes program is expires in June 2012 and the company does not aim to raise any debt from external sources later on. Thus, we expect LaserBond will maintain a negligible level of debt, resulting in a positive net cash position for both FY12 and FY13 ($2.0 and $3.4m respectively). We also forecast that cash flow generating capacity is strong enough to finance current working capital requirements. The only foreseeable scenario for leverage growth is a potential significant acquisition in Western Australia. However, the company announced that it would prefer to rely more on internal cash funding rather than on external debt.

The company reaffirms its intention to pay full year dividend contingent on operating performance and cash funding requirements (acquisition, continuing operations etc.). We reiterate our dividend forecast of 0.5 cent per share that translates to effective payout ratio of 18% of full year EPS.

VALUATION | RECOMMENDATION

DCF valuation

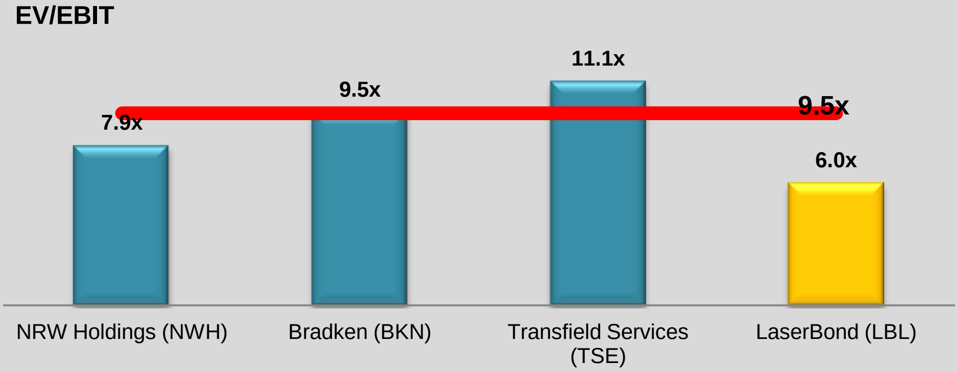
Our DCF model provides us with a valuation of $0.255, representing a 4% premium to the current market price of $0.245. The DCF valuation has decreased marginally from $0.26 to $0.255 due to an increase in the risk free rate and beta for the period. We maintain the same assumptions in our model. We have used a fundamental beta of 1.24, WACC of 13.38% and a long-term growth rate of 2.0%.



DCF Inputs			
Equity Beta:	1.24	**Interest-bearing debt:**	$0.50m
Risk free rate:	4.16%	**Cost of Debt:**	15.48%
Return on Equity:	13.45%	**WACC:**	13.38%
LT Growth Rate:	2.00%		

Relative EV/EBIT valuation

Peer group summary (*as at 16th March 2012)*



LaserBond is the only ASX listed laser cladding and CNC machining player. We have undertaken a relative valuation using the most appropriate peer comparisons available that include other specialist engineering service providers and materials manufacturers with exposure to the mining and industrials sectors. Using a forecast FY12 EV/EBIT multiple of 9.5x we have derived a relative valuation of $0.38 per share, representing a 56% premium to the last traded price of $0.245. We have removed Ludowici Limited (ASX:LDW) from our peer valuation analysis as the company is a takeover target in an ongoing bidding war. The current bid of $11 is at a 215% premium to the pre-bid price of $3.50. The significant increase in peer EV/EBIT multiples to 9.5x from 7.7x (Jan 24, 2012) is largely due to the general improvement in sector sentiment.

Investment Opinion

We issue an updated report on LaserBond with a BUY recommendation and a price objective of $0.32. The price objective is based on a combination of the DCF valuation of $0.255 and our relative peer valuation of $0.38.

PRICE OBJECTIVE & RECOMMENDATION HISTORY

Changes to recommendations and/or price objectives			
Date	**Recommendation**	**Price at time of Rec**	**Price Objective**
19/03/2012	BUY	$0.245	$0.32
24/01/2012	BUY	$0.205	$0.280

FINANCIAL SUMMARY

PROFIT & LOSS SUMMARY ($m)

Year Ending June	FY11A	FY12F	FY13F
Revenue	13.5	16.5	19.4
Cost of sales	(7.1)	(8.5)	(10.1)
Operating expenses	(4.3)	(5.3)	(5.8)
+ D&A	0.2	0.2	0.2
+ Net interest expense	0.1	0.1	0.1
EBITDA	**2.3**	**3.1**	**4.0**
% EBITDA margin	17%	19%	20%
% Change YOY	161%	36%	27%
D&A	(0.2)	(0.2)	(0.2)
EBIT	**2.1**	**2.9**	**3.8**
% EBIT margin	16%	18%	19%
Net interest expense	(0.1)	(0.1)	(0.1)
Profit before tax	2.0	2.8	3.7
Tax	(0.7)	(0.7)	(0.9)
NPAT	**1.3**	**2.1**	**2.7**

PROFITABILITY RATIOS

Year Ending June	FY11A	FY12F	FY13F
Sales ($'m)	13.3	16.4	19.4
Price/Sales (x)	1.3	1.1	0.9
EPS (cents)	1.8	2.8	3.6
% Change YoY	159.0%	59.4%	27.9%
P/E (x)	**13.5**	**8.4**	**6.5**
Entrepise Value ($'m)	17.3	17.3	17.3
EV/EBIT (x)	**8.1**	**5.9**	**4.6**
EV/EBITDA (x)	**7.6**	**5.6**	**4.4**
DPS Net (¢)	0.50	0.50	0.50
DPS Gross (¢)	0.71	0.71	0.71
Gross Dividend Yield (%)	3.0%	3.0%	3.0%
ROE (%)	19.1%	24.0%	24.5%
ROA (%)	12.9%	16.5%	17.3%

BALANCE SHEET SUMMARY ($m)

Year Ending June	FY11A	FY12F	FY13F
Cash	1.0	2.5	3.9
Receivables	3.3	3.7	4.5
Inventories	1.5	2.0	2.6
Current assets	**5.8**	**8.3**	**11.0**
Plant & equipment	0.7	0.8	0.9
Intangible assets	3.6	3.6	3.6
Deferred tax assets	0.3	0.3	0.3
Non-current assets	**4.5**	**4.6**	**4.8**
TOTAL ASSETS	**10.3**	**12.9**	**15.8**
Payables	1.1	1.6	1.8
Provisions	0.7	0.8	0.9
Interest-bearing liabilities	0.1	0.1	0.1
Current tax liabilities	0.8	0.8	1.1
Current liab.	**2.7**	**3.3**	**3.9**
Interest-bearing liabilities	0.5	0.5	0.5
Provisions	0.2	0.3	0.3
Non-current liabilities	0.7	0.7	0.8
TOTAL LIABILITIES	**3.3**	**4.0**	**4.7**
Net Assets	7.0	8.9	11.1
Net Tangible Assets	3.1	5.0	7.3

CASH FLOW SUMMARY ($m)

Year Ending June	FY11A	FY12F	FY13F
EBITDA	2.3	3.1	4.0
Decr/(incr) in working cap	(0.9)	(0.5)	(1.0)
Net interest received	0.0	0.0	0.0
Taxes paid	(0.7)	(0.7)	(0.9)
Incr/(decr) in provisions	0.2	0.2	0.1
Cash from Operations	**0.9**	**2.2**	**2.1**
CAPEX	(0.1)	(0.3)	(0.4)
Disposals/(acquisitions)	(0.2)	-	-
Cash from Investing	**(0.3)**	**(0.3)**	**(0.4)**
Incr/(decr) in equity	-	0.2	-
Incr/(decr) in debt	-	(0.2)	-
Dividends paid	-	(0.4)	(0.4)
Other fin cash flows	(0.1)	-	-
Cash from Financing	**(0.1)**	**(0.4)**	**(0.4)**
Net incr/(decr) in cash	0.6	1.5	1.4

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RECOMMENDATION GUIDE

Recommendation	Market Price undervalued/overvalued to Microequities price objective
Strong Buy	Above 40%
Buy	20 to 40%
Hold	0 to 20%
Sell	0 to -20%
Strong Sell	Greater than 20%

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Investment Banking	Staff Interest	Analyst personal Interest	Equity Stake By Microequities Associates	Disclosure to Company	Business Relationship
NO	NO	NO	NO	✓	✓

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