

Unlock value in service providers

INVESTMENT IN RELATED STOCKS

Companies providing essential services to the miners provide an avenue for investors seeking exposure to the industry, writes James Dunn

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INVESTORS wanting exposure to the coal industry do not have to choose only from the miners. Many companies on the stock exchange provide a range of essential services to the coal companies.

Diversified industrial company Ludowici Limited (ASX code LDW) serves the coal industry through its subsidiary Ludowici Mineral Processing Equipment (LMPE), which manufactures and markets large-scale mining and materials-handling equipment such as coal screens, centrifuges, slurry treatment plants, dewatering cyclones, valves, shiploaders and conveyor belts. LMPE accounts for 72 per cent of Ludowici's turnover, which reached \$144.8 million in 2006. The shares have moved from \$4.35 three years ago to \$7.50, capitalising Ludowici at \$133 million.

Hugh Robertson, at stockbroking firm Bell Potter, says Ludowici is the ultimate obscure company. "Companies don't get much more obscure, but it's a marvellous company. It's a typical small cap, it flies below the radar and doesn't court publicity. But it is one of the few really international businesses in the resources sector that's listed on the Australian share market -- it makes sales in South Africa, South America, Asia, North America. Effectively it has a presence in most parts of the world when it comes to coal and resources." Robertson describes Ludowici as a "sleep-well-at-night stock". "It's very well-run, and it's definitely one of the most interesting exposures to coal, because I think the underlying business is probably worth double the current share price. Sooner or later, somebody will come knocking at its door, and say, 'Would you like to sell your assets to us for a vast amount of money?' If you look at comparative sales around the world of these kinds of assets, I think you can find \$15 a share pretty easily."

Another interesting -- but tiny -- exposure is QMastor Limited (QML), which is valued at just \$9.9 million on the stock exchange. QMastor provides coal quality management and stockpile tracking software systems to the mining, port and power generation industries. QMastor's systems track the tonnage, quality and value of bulk materials across the supply chain. Its flagship products include the pit-to-port integrated mining supply chain management system, and the QMastor stockpile management system. In 2005-06, QMastor lifted its revenue by 26 per cent to \$1.95 million, but reported a loss of \$85,000. At the December half-year, however, it posted a net profit of \$96,000, on the back of a 73 per cent surge in revenue to \$1.4 million.

A broker who follows the stock closely says QMastor is an under-rated company. "It is very thinly traded but it is an excellent exposure to the coal industry. It has developed a technology in association with BHP to monitor the quality of bulk materials as they move from their original source, through to the port -- pit-to-port,

as the company calls it. What impresses me is that this technology, which was originally developed for coal, has now been accepted by Comalco for bauxite, OneSteel and Robe River for iron ore, and most recently by Societe Le Nickel in New Caledonia. It is now cashflow-positive and a lot of the revenue from here on flows through to the bottom line. It's a stock that I think will be paying a dividend within 12 months."

QMastor was originally the technology arm of coal services group CCI Holdings Limited (CHL), which floated it off in December 2001. CCI -- which supplies technical services such as superintending (export certification), consulting, training, exploration, quality control, in-pit drilling and environmental services, asset management and engineering services -- has been another coal exposure on the ASX, but is about to leave. In March, CCI announced a merger with the Australian subsidiary of Paris-based international conformity assessment group Bureau Veritas SA, which operates in the fields of quality, health, safety, environment and social responsibility. This was shortly after reporting a record net profit for the December 2006 of \$2.48 million, up 71 per cent on the corresponding period.

However, there are some recent additions to the sector. Brisbane-based engineering company Sedgman Limited (SDM) listed on the stock market in June 2006. Sedgman, a market leader in the design, construction, operation and maintenance of coal handling and preparation plants (CHPPs), saw its \$1 shares jumped to \$1.40 on its first day, and they have subsequently risen to \$2.34.

Also welcomed by investors has been Walter Diversified Services (WDS), which came to the stock market in December 2006, provides services for the underground coal mining industry, and also provides pipeline construction and maintenance services for the water, gas, and oil industries. WDS has turned its IPO price of \$1.50 into a share price of \$2.30, a handy 53 per cent premium in four months, enough to value it at \$180 million.

The reception for Sedgman and Walter contrasts with that accorded mining equipment hire company Emeco Limited (EHL), which despite listing just a month after Sedgman in July 2006, showed poor timing -- for reasons beyond the company's control.

Emeco, which generates 40 per cent of its revenue from the coalmining industry, saw the prospects for its \$940 million float crimped when the close of the institutional bookbuild coincided with the release of Australia's worst inflation figures in five years. The prospect of higher interest rates alarmed the market, and the bookbuild set a final price on Emeco of \$1.90 a share, compared to the indicative range of \$2.10-\$2.50 stated in the prospectus. Trading in the shares opened at \$1.82, a 21 per cent discount to the mid-point of the indicated value range, and the shares still trade below issue price, at \$1.73.

Also in the coal services business are engineering groups Clough Limited (CLO), which works in the Indonesian coal mining industry; and AJ Lucas Limited (AJL), whose Lucas Coal Technologies division has carved out a significant market share in the in-seam drilling business; and mining contractor Monadelphous Limited (MND), which moved into coal in March with the purchase of Hunter Valley-based coal services business Ellavale Engineering. "If it is true to form, Monadelphous will do remarkable things with that acquisition," says Robertson.

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