

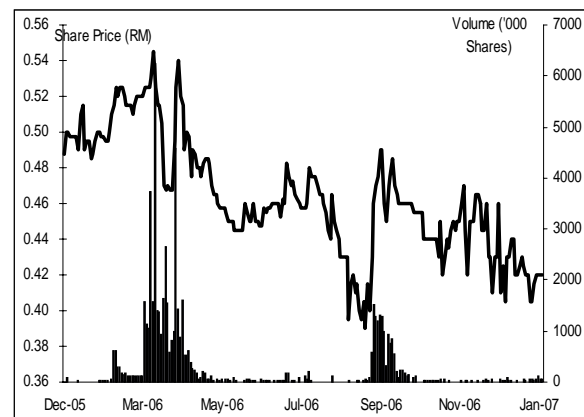
Grand-Flo Solution Berhad		Price:	RM0.50
		Market Capitalisation:	RM61.8m
		Board:	Mesdaq
		Sector:	Technology
Stock Code:	0056	Recommendation:	BUY

Key Stock Statistics	FY05	FY06F	FY07F
EPS (sen)	2.7	3.2	5.8
P/E on EPS	18.8	15.5	8.5
Dividend/Share	0.0	1.6	1.8
NTA/Share (sen)	20.3	12.7	19.7
Book Value/Share (sen)	27.1	24.1	30.9
Issued Capital (m shares)	50.0	123.6	123.6
52-weeks price range (RM)	0.34 – 0.58		

Note: Historical EPS adjusted for proposed bonus issue for comparison purposes

Major Shareholders:	%
Tan Bak Hong and Yap Li Li	23.5%
Tan Bak Leng	12.3%
Tan Chuan Hock	8.0%

Share Price Chart



Per Share Data	2004	2005	2006F	2007F
Book Value (RM)	0.11	0.14	0.24	0.31
Cash Flow (sen)	22.2	3.8	3.7	7.4
Earnings (sen)	2.0	2.7	3.2	5.8
Dividend (sen)	0.0	0.0	1.6	1.8
Payout Ratio (%)	0.0	0.0	50.0	30.0
PER (x)	25.0	18.8	15.5	8.5
P/Cash Flow (x)	2.2	13.2	13.6	6.7
P/Book Value (x)	4.6	3.7	2.1	1.6
Dividend Yield (%)	0.0	0.0	3.2	3.5
ROE (%)	15.8	20.1	13.4	18.9
Net Gearing (%)	n.c.	n.c.	n.c.	n.c.

n.c. – net cash

P&L Analysis (RM mil)	2004	2005	2006F	2007F
Year-end: 31 Dec				
Revenue	13.3	30.2	45.3	69.9
Operating Profit	2.4	6.6	9.0	14.5
Depreciation	-0.2	-0.9	-1.0	-1.3
Interest Expenses	-0.1	-0.1	0.1	0.2
Pre-tax Profit	2.2	5.6	8.1	13.4
Effective Tax Rate	20%	27%	27%	25%
Net Profit	1.7	2.7	4.0	7.2
Operating Margin	18%	22%	20%	21%
Pre-tax Margin	16%	19%	18%	19%
Net-Margin	13%	9%	9%	10%

1. Latest Development

- We met up with the management of Grand-Flo Solution (GF) recently and came back with positive feedback. To recap, the group's recent 9MFY06 earnings were in line with our forecasts, and management believes that our forecast of RM4.0m net profit for the full year is achievable. Next year's growth would be much stronger with the full year contribution from the new acquisitions. As such, we are maintaining our estimates for FY06 and FY07 for the group.
- GF's share price has been relatively flat, hovering at around 42 sen for the past few months. However, it has crept up almost 20% in the last two days, which we believe is not only due to the stronger market sentiment but also a likely re-rating of the group by the market given its undervalued share price vis-à-vis its strong earnings growth prospect.
- With the deemed completion of the acquisition of 100% of Spritvest Sdn Bhd and 100% of Data Centrix Sdn Bhd (Spritvest's R&D arm) on 2 October 2006, GF is now probably the largest enterprise data collection and collation system (EDCCS) provider in Malaysia with a market

share of about 40%. The group is also a strong regional player, with its market share now having risen to about 30% in Thailand via its 49%-owned subsidiary with deemed control, Simat Technologies Public Company Limited (ST). GF management said that the new acquisitions have achieved their profit guarantee of RM2m for FY06, and this will be reflected in the upcoming final quarter results of FY06. In addition, management is also optimistic that the profit guarantee of RM2.5m for FY07 would be fulfilled as well.

Expansion in the region

- The contribution from GF's overseas operations has risen substantially, predominantly from ST. Overseas operations accounted for 62.7% of the total revenue for 9M06, compared to the previous 52.6% in 9M05; and at the PBT level, overseas operations made up 84.0% of total PBT for 9M06, compared to the previous 68.9% in 9M05. The group is currently looking to expand into more countries in the region such as Vietnam, Indonesia and China but these ventures are still only at early stages of discussion. These expansions will likely be via ST in view of its planned listing on the Market for Alternative Investment in Thailand in the coming months. Note that the listing of ST would have been sooner if not for the delays due to the recent unrest in Thailand.
- GF has also set up a subsidiary under ST in Thailand recently (99.9% owned by ST) called Simat Soft Co. Ltd (SS). The company's principal activities are to produce, develop, modify and sell computer software and to engage in consultancy service involving computer software. SS is likely to be used as the future vehicle for further expansion in Thailand given its attractive tax exemption status. Among the privileges and benefits granted by the Board of Investment of Thailand to SS are:
 - 1) Permitted employment of foreigners as skilled technicians or experts;
 - 2) Allow to apply for work permit for such foreigners in (1) above;
 - 3) Exemption from import duty for imports of machinery (such as computers, notebooks, etc); and
 - 4) Exemption from corporate income tax for a period of eight years from the date of the first income and any losses incurred are allowed to be carried forward and deductible as expenses for up to a period of five years.
- Management believes that there will be substantial tax savings for its Thailand operations in the future especially through new SS operations. Currently the effective tax rate for ST stands at about 30%. We understand that the expected tax savings for FY07 could be approximately RM0.6m at ST level and there will be further tax savings as ST's Thailand operations expand through SS.

Potential revenue growth from Radio Frequency Identification (RFID) technology

- We understand that GF has been planning to incorporate the more advanced RFID technology into its EDCCS solutions as the future of the auto-ID industry is already moving towards RFID technology. The global RFID industry is valued at slightly over USD1.0b annually and is expected to grow threefold over the next three years. The group is believed to be in the process of identifying various potential projects in the pipeline involving RFID technology. Note that GF's products currently are geared almost 100% towards bar coding technologies and as such, any new RFID projects are likely to give a boost to earnings.
- To recap, RFID allows data that is stored in a tag (which is made up of a microchip and a built-in antenna) to be sent out via radio waves and captured by readers. It is gaining popularity due to the significant range, speed and unattended reading advantages it provides as compared to bar codes. It also possesses greater flexibility in positioning, less prone to fault in harsh and challenging environment, as well as offering a longer lifetime and larger memory capacity.

2. Recommendation

- With strong growth prospects, underpinned by its dominant position in a growing bar code industry and its successful overseas market breakthrough, GF has a strong niche that is yet to be reflected in its share price. We believe the market is likely to re-rate the stock further in the coming months as the group potentially announces more new projects.
- At the current price level, GF is still trading at an attractive PER of just 8.5x based on its FY07 forecast EPS of 5.8 sen. We reckon the stock deserves to trade at a PE multiple of at least 10x – 15x (at a PE to growth ratio of 1.0x), which is very likely to be its sustainable growth rate over the longer term. Even then, GF's growth rate could surpass our expectations if its new RFID projects materialise.

- Given its continued strong growth prospects and still low valuations, we are maintaining a BUY recommendation on the stock with a target price of RM0.70 or a 40% upside from its current share price of RM0.50, ascribing it a conservative 12.0x multiple for its FY07 EPS.

Investment ratings:

Buy (generally >10% upside over the next 12 months)

Hold (generally negative 10% downside to positive 10% upside over the next 12 months)

Sell (generally >10% downside over the next 12 months)

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