

Kelington Group Bhd

13 Jul 2010

KDN: PP10837/03/2011(029371)

NOT RATED

Current Price	RM0.73
Target Price	RM0.79
Upside To Target	-

Stock Codes

Masa	KGB / 0151
Bloomberg	KGRB MK

Stock & Market Data

KLCI	1,326.74
Listing	ACE Board
Sector	Trading/ Service
Syariah Compliance	Yes
Par Value	RM1.00
Issued Shares	65mn
Market Capitalisation	RM34.45mn
YTD Chg In Share Price	RM0.90/RM0.53

Majority Shareholders

Palace Star Sdn Bhd	53.19%
Allied Moral Investment Limited	7.88%

Historical Price Ratios

FYE	2010
PER (x)	525
PBV (x)	1.37
ROE (%)	N.A.

Share Performance

(%)	1mth	3mth	12mth
Absolute	1.3	0.0	N.A.
vs. KLCI	-0.7	2.5	N.A.



A Leader in Ultra High Purity Engineering

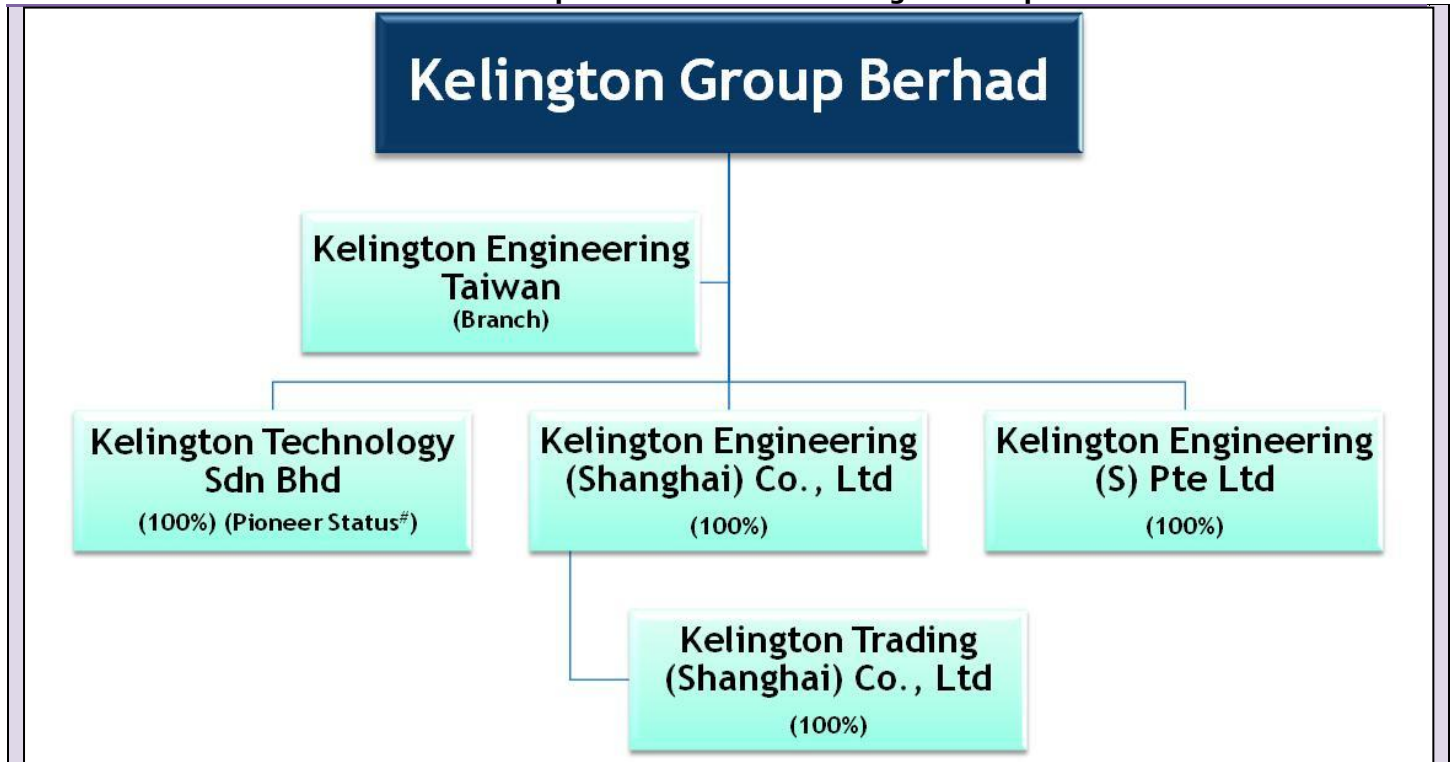
- Company Background.** Kelington is principally engaged in the business of providing engineering services, specifically in the provision of Ultra-High Purity (UHP) gas & chemical delivery systems solutions. Kelington was listed on the ACE market of Bursa Malaysia in year 2009.
- Products & Services.** Their products and services include UHP system design, fabrication & installation, QA & QC services, control and instrumentation to high-technology industries such as wafer fabrication, Flat Panel Display (FPD) manufacturing, solar energy, pharmaceutical, Light Emitting Diode (LED) & storage media. Kelington operational structure is segregated geographically among Malaysia, China, Taiwan & Singapore.
- Corporate Milestone.** Kelington's business can be traced back to 2000 when its founder Raymond Gan started a Malaysian-owned engineering company by having a secured maiden key project in Malaysia for SilTerra Malaysia's foundry at Kulim. Through its outstanding quality services, Kelington has penetrated into Taiwan in year 2003 by implemented first project for HannStar Display. In year 2004, Kelington began expanding fast by implemented a major project in China for Taiwan Semiconductor Manufacturing Corporation in wafer fabrication. At the same year, Kelington also manufactured valve manifold box and panel for Taiwan. Kelington first solar cell project is for Suntech Power Holdings in China. Renewable energy project in Singapore proved Kelington's competency in year 2008 and Pioneer Status is attained. In year 2009, implementation of Turnkey Bulk Chemical Delivery System for Seagate Skudai show great competence and ability to undertake a large scale UHP project. To date, Kelington has earned internationally prestige through its extensive experience and constant pursuit of excellent.

Investment Statistics

FYE 31 December (RMmn)	2009	2010F	2011F	2012F
Revenue	63.84	79.85	87.41	94.99
Growth (%)	6.3	25.1	9.5	8.7
PBT	8.64	8.75	9.77	11.02
Growth (%)	22.4	1.2	11.7	12.8
Net Profit	8.07	8.13	9.09	10.25
Growth (%)	22.2	0.8	11.7	12.8
EPS (sen)	10.8	10.9	12.2	13.7
PER (x)	6.8	6.7	6.0	5.3
Dividend yield (%)	N.A.	3.7	4.2	4.7
ROE (%)	23.5	21.7	20.7	20.0
ROA (%)	14.2	13.3	13.0	13.0

- **Financial Highlights.** Kelington has recorded a 5-Year revenue CAGR of 37.3% (from 04-09). The 5-Year CAGR of EBITDA and net profit have been also showing delighted growth of 40.1% & 44.9% respectively. Meanwhile, Kelington is also enjoying a low corporate tax rate (6.5% on average in FY07 and FY08) due to its Pioneer Status. We understand that the Group will continue to enjoy this tax exemption for the next 8 years.
- **Going forward,** the Group plans to broaden its UHP product scope into other utilities such as water and vacuum. Besides, the Group also keen on enter new industries and markets. Apart from business developments, the Group will in addition focus on R&D to enhance its capabilities. In fact, we understand that the Group is in the midst of improving its UHP system equipments and parts as well as enhancing its nano-technology skills.
- **Earnings Projections.** We believe the Group should comfortably achieve approximately RM80mn sales in FY10 and RM87mn in FY11, representing revenue growth of 25.1% and 9.5%, respectively. However, we understand that the pre-tax margin going forward will be slightly lower than that of in FY09 due to an exceptional project that command good margin in that particular year. And, we understand from management that this margin is not likely to repeat in the next 1-2 years. As such, we have projected a lower average PBT margin of 11.1% for the next 2 years vis-à-vis 13.5% in FY09. Thus, the net profit for the Group is projected at RM8.1mn and RM9.1mn for FY10 and FY11, implying an average net profit growth and margin of 6.2% and 10.3%, respectively, as opposed to 22.2% and 12.6% in FY09. ROE is estimated to range between 20% to 22% for the next 3 years.
- **Solid Financial Position.** Due to the nature of its business, the Group's balance sheet and cash flow have been in pink health. We believe the Group will still be in a net cash position even with their aggressive business development plans thanks for its strong cash flow generating ability, say >RM6.0mn a year. The current borrowing of RM1.3mn was mainly used in financing the Group's factory-cum-office in Bukit Jelutong.
- **Our View.** We reckon that the profit growth of Kelington is sustainable due to its rapid expansion and high barrier of entry (extensive technical-know-how is required). Due to its strong financial track records, we do not rule out the possibility of the Group to migrate to Main Market, which could serve as a price catalyst. Besides, due to its strong cash flow generating ability, we also do not rule out that the Group to start paying dividends from this financial year onwards. However, we do understand that the Group is still in an expansion mode, hence the dividend payout ratio, if any, will likely be capped below 25%. Based on our FY10 and FY11 earnings estimates, the stock is traded at undemanding valuations of 6.7x and 6.0x on the back of 21.7% and 20.7% in FY10 and FY11 ROEs. The pullbacks are (i) the low liquidity and (ii) its listing on ACE Market, which could limit its upside for now. Valuation wise, based on last year's price multiples and FY11 numbers, the stock should be valued at RM0.79. **NOT RATED.**

Chart 1: Corporate Structure of Kelington Group

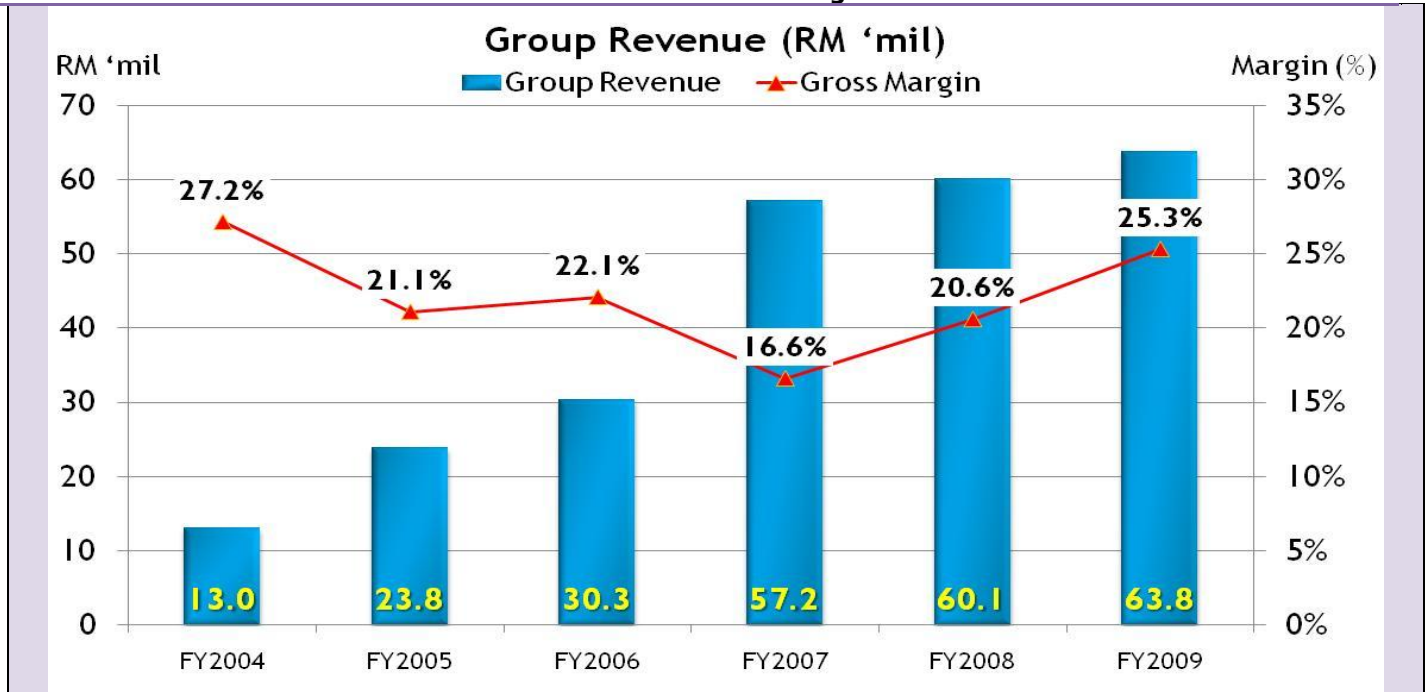


Source: Company

Table 1: SWOT Analysis

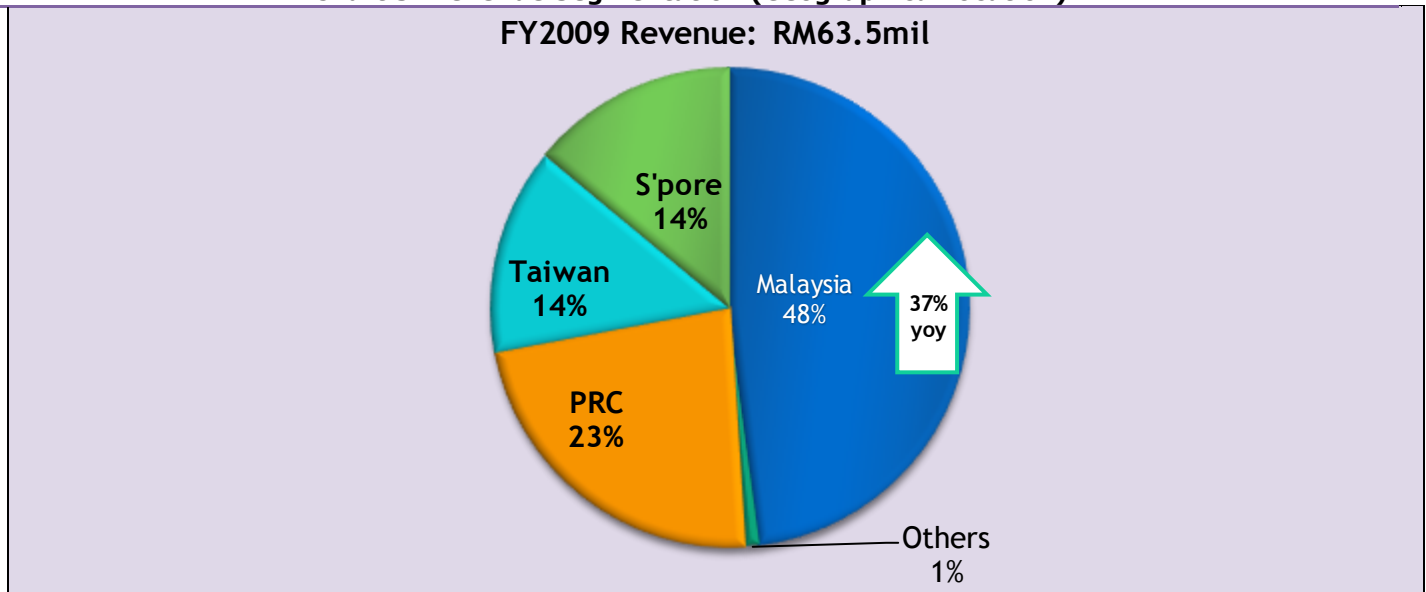
Strengths	Weaknesses
<ul style="list-style-type: none"> • Strong engineering expertise & certified quality personnel • Ability to undertake turnkey projects • Established relationship with gas & chemical manufacturers • Recurring revenue through business expansion of existing customer • High barrier of entry • Capital levels are healthy 	<ul style="list-style-type: none"> • Human capital & intellectual properties • Lack of long term contracts
Opportunities	Threats
<ul style="list-style-type: none"> • Increasing demand for innovative consumer electronics • Strong government support for high-technology & emerging sectors 	<ul style="list-style-type: none"> • Cyclical nature of the semiconductor industry • Rapid changes & technological innovations

Chart 2: Revenue & Gross Margin Trend



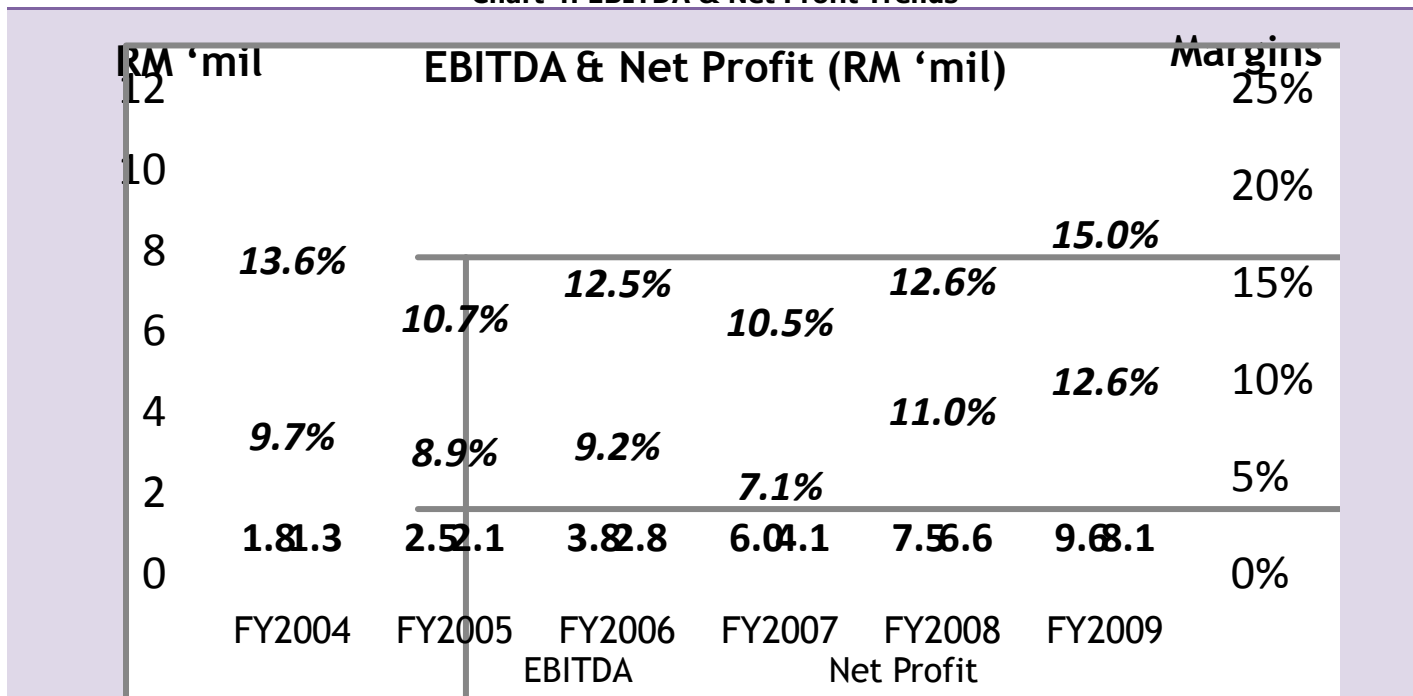
Source: Company

Chart 3: Revenue Segmentation (Geographical location)



Source: Company

Chart 4: EBITDA & Net Profit Trends



Source: Company

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Stock ratings used in this report are defined as follows:

BUY	Share price expected to appreciate more than 15% over a 12-month period
TRADING BUY	Share price expected to appreciate 10% or more within a 3- to 6-month period
NEUTRAL	Share price expected to be within +/- 15% over a 12-month period
TAKE PROFIT	Target price reached, may accumulate if share price drops more than 15% below target price
SELL	Share price expected to depreciate more than 15% over a 12-month period
NOT RATED	MIMB does not provide research coverage or rating for this company

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