Kelington steps outside semi-con industry

Diversification pays off, revenue set to overtake all-time high

Kelington is already the go-to name for the semiconductor industry ... and our reputation is cast in stone, says Gan

by Farah Saad

ENGINEERING-BASED Kelington Group Bhd's diversification has started to pay off, as the company's 2014 revenue looks to overtake an all-time high of RM139 mil set in 2011. Barely three months into its 2014 financial year, Kelington has RM201 mil in its outstanding order book.

The company has begun to offer its services to industries outside electronics and semiconductors, which have been its staple source of revenue for 10 years.

From providing UHP (ultra-high-purity) mechanical and electrical services and systems for the semiconductor and electronics industry, Kelington has expanded into providing engineering services for the healthcare and pharmaceutical industries, as well as palm oil refineries and petrochemical plants.

Kelington founder and group chairman/CEO Raymond Gan says this is a step in the right direction, and the timing could not be better.

"We are already the go-to name for the semiconductor industry ... and our reputation is cast in stone. The next step is how we grow and break the RM100 mil market-capital mark," Gan tells ***FocusM***.

Kelington group president and chief operating officer Steven Ong adds it is a matter of needing a steady stream of income to ride out the more volatile semiconductor industry, where most of its business originates.

"Being involved in different industries, we hope their respective cycles will overlap; so this means a steady income stream for us. We are not reducing income from our semiconductor business – we are adding to it," says Ong.

He says the company had been planning its diversification since 2012; but it wasn't until it landed its largest contract to date that the vision became reality.

In December, Kelington was awarded a RM148 mil contract by Singapore-listed International Healthway Corp Ltd (IHC) to provide UHP mechanical and electrical services and medical systems for IHC's Holland Village maternity facility in Shanghai, China. The contract is valid to October this year. To back its work on the project, Kelington has secured a US$14 mil (RM45.81 mil) facility from EXIM (Export-Import) Bank of Malaysia Bhd.

FocusM also reported in Issue 69, quoting sources, that Kelington could be appointed by IHC as its supplier of UHP gas infrastructure for the group's planned mixed-use development in Jalan Kia Peng, Kuala Lumpur.

Sources reportedly said the contract amount could be roughly the same as that of the Shanghai job, given the similar facilities required. The Jalan Kia Peng development is a combination of specialist medical suites and residences, with allocated retail space; while the main building will be a 33-storey integrated mixed-use development.

IHC has 15 similar healthcare projects in various locations across Asia and Kelington hopes to take advantage of IHC's presence.

"[The contract] could serve as a catalyst in generating new contracts for the group," says TA Securities analyst Tan Kam Meng.

"Note that IHC has undergone an initial public offering in Singapore and has planned to expand its network. It has three pipeline projects which will require a UHP gas supply."

> "The bonus issue is to reward our shareholders and to get some attention from the market, and bring in capital. Something big is coming up this year ..."
> – Ong

Kelington is also expected to secure a contract for a biodiesel project in Taiwan, for which the company has a letter of intent. The contract will involve the installation of piping estimated to be valued at RM35 mil.

There is little additional capital or additional risk involved in its diversification plans, says Gan, as the business is more human capital-oriented and is not reliant on machinery or factories.

"There is minimal risk, because whatever the industry, we go back to our core skill – engineering. So we are not deviating much from our core capabilities. Another advantage is we are asset-light, so we invest in human capital instead of in plants and machinery," says Gan.

Improving financial performance

Financially, 2014 is shaping up as a much better year for Kelington than last year, when it suffered abysmal results. The company's net profit for FY13 contracted 73% to RM1.6 mil.

The company was reliant on income from the semiconductor industry, which experienced a bad year. Major players were cutting expenditure, which trickled down to service providers like Kelington. The company also had to undercut pricing to remain competitive, and saw its margins shrink considerably.

However the bulk of these low-margin contracts have been completed, so the company can start this year with a clean slate.

Kelington aims to have at least 30% of its revenue from recurring sources, with the remaining 70% to come from one-off, larger-scale projects. Its recurring jobs are from two of the world's largest chip manufacturers. This means Kelington, while keeping the core of its income stream intact, will be able to keep one hand free to bid for projects.

"We realised we needed to maintain recurring income and be able to ride out the fluctuations in the industry. Recurring income at 30% is a comfortable level for us to sustain our business," says Gan.

We are not reducing income from our semiconductor business – we are adding to it, says Ong

The company also plans to reduce its reliance on one country and have a more even spread across Malaysia, China, Singapore and Taiwan. Currently, 40% of its income is Malaysia-based.

As for possible expansion outside its current markets, Kelington has earmarked Vietnam, where it has completed several projects but has yet to set up an office.

Ong says an asset-light business is an advantage when setting up operations in another country, where the risk of failure is generally higher. Gan adds: "When going overseas, you must be lean and mean!"

However setting up a new base is not something to be rushed, says Ong. The company has been looking into India for the past six years but has decided not to venture there until it can secure a stable income from the country.

Bonus issue

In a hint of better things to come, Kelington has proposed a one-for-three bonus issue of shares and warrants.

"The bonus issue is to reward our shareholders and to get some attention from the market, and bring in capital. Something big is coming up this year. There are projects which we are bidding for but have not yet confirmed," says Ong.

In light of this, Kelington's dividend payout policy remains unchanged at 25%. From 2009 to 2012, the company paid out an average of 35% to its shareholders.

Its share price since the beginning of March has increased some 37%, closing at 56.5 sen on March 27. Is this share price justified?

"If we do everything as planned, it could be more! In the end, it all falls back on fundamentals. We cannot speculate. Everyone feels their company can do better," says Gan. FocusM