

28 July 2022

Construction & Engineering | Industrial

Kelington Group (KGRB MK)

Buy (Maintained)

Exceeding MYR2bn In Tenderbook; Maintain BUY

Target Price (Return): MYR1.69 (+42%)
 Price (Market Cap): MYR1.19 (USD172m)
 ESG score: 3.00 (out of 4)
 Avg Daily Turnover (MYR/USD) 1.11m/0.25m

- Keep BUY, with new MYR1.69 TP from MYR1.60, 42% upside.** We raise our TP and earnings forecasts after bumping up our orderbook replenishment assumptions to factor in stronger-than-expected YTD project wins. The structural fab capacity expansion and prevailing tight supply situation globally should keep Kelington Group (KGB) busy over the next 18 months, with a burgeoning MYR1.6bn orderbook at hand. Our TP bakes in a parity ESG score, based on our in-house methodology.
- Exceeding MYR1.6bn outstanding orderbook and growing.** KGB saw a slew of contract wins in 1H22, valued at c.MYR762m. This already made up 64% of FY21 order wins and looks to be on track to surpass the previous record by end-4Q22. Notable contract wins to-date include: i) A MYR114m general construction (GC) job for a European semiconductor manufacturer for the design, engineering and construction works in Johor, and ii) a MYR62m gas hook-up job for China's largest chip foundry, the second after an earlier award in May (MYR80m). We expect further orderbook replenishment (likely in successive batches) over the next couple of months and into FY23F, supported by the latest tenderbook of >MYR2bn.
- Stellar 2Q22 expected.** Despite being a seasonal lull, 1Q22 revenue was the highest ever achieved by the group for the same quarter (+65% YoY), while core earnings surged 45% YoY. This was fuelled by a more than doubling of general contracting (GC) revenue, mainly from a chunky MYR432m turnkey job from a leading hard drive maker secured last September. We expect 2Q22 core earnings (to be announced on 15 Aug) to jump 18-30% YoY on stronger project recognition in Singapore, Malaysia and China, as well as margins.
- Prolonged upcycle.** The drawn-out Russian-Ukrainian conflict should see the chip shortage persist until 2024, according to SEMI. KGB should continue to ride on the coattails of the fab capacity expansion globally, being a core engineering solutions provider with a leading share of the Singapore and China markets. China's zero-COVID policy has thus far not disrupted job orders with sufficient materials available on-site. We see the risk from rising material costs being mitigated by shorter tender periods for ultra-high purity (UHP) projects where cost escalations are built into project cost at the outset.
- Forecasts and TP raised.** We lift FY22F-24F core earnings by 2-11% after bumping up our orderbook replenishment assumptions by 11-38%. This lifts out TP to MYR1.69, which is still based on 28x FY23F fully diluted EPS. We continue to see KGB as a strategic proxy to the structural expansion in wafer foundry capacity (front-end), arising from the tight supply situation. Key risks are lower-than-expected margins, faster-than-expected normalisation of the demand-supply imbalance in the chip sector, and weaker orderbook replenishment.

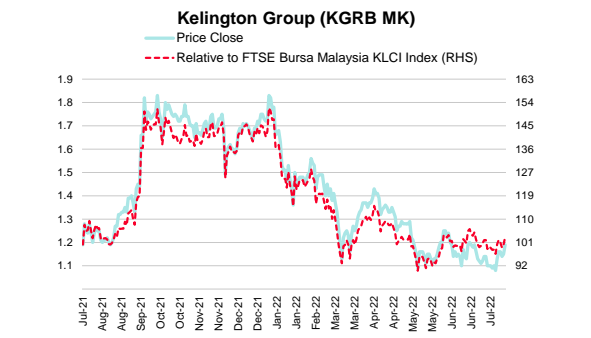
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(30.8)	(0.8)	(6.3)	(17.4)	0.0
Relative	(24.6)	(3.1)	1.0	(14.4)	2.9
52-wk Price low/high (MYR)	1.08 – 1.83				



Source: Bloomberg

Overall ESG Score: 3.00 (out of 4)

E: GOOD

KGB is committed to preserving the environment through various practices such as reducing electricity and water consumption. It is also managing the usage of materials to reduce waste. There is however a lack of environmental statistics on pollution and waste management

S: GOOD

Apart from up-to-standard health & safety policies, we see active community engagements, and efforts to uplift employee relations. KGB is focused on attracting and retaining talent, and helping employees develop their skills to drive further success

G: GOOD

KGB's Chairman is also the Group CEO. The board does not utilise independent sources to identify the appointment of directors, which could limit operational checks and balances. A third party investor relations unit facilitates the communication with the investment community with periodic meetings convened

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (MYRm)	395	515	920	947	945
Recurring net profit (MYRm)	15	29	47	52	54
Recurring net profit growth (%)	(34.3)	89.7	62.1	10.0	4.0
Recurring P/E (x)	66.56	35.09	21.65	19.67	18.91
P/B (x)	6.1	5.3	4.5	3.9	3.4
P/CF (x)	22.36	na	19.21	18.35	17.07
Dividend Yield (%)	1.3	0.7	1.2	1.3	1.3
EV/EBITDA (x)	28.23	20.15	14.03	12.56	11.33
Return on average equity (%)	10.8	16.1	22.7	21.3	19.8
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

See important disclosures at the end of this report

Market Dateline / PP 19489/05/2019 (035080)

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Malaysia	Recurring EPS	0.02	0.03	0.05	0.06	0.06
Construction & Engineering	DPS	0.02	0.01	0.01	0.02	0.02
Kelington Group	BVPS	0.20	0.22	0.26	0.31	0.35
KGRB MK	Return on average equity (%)	10.8	16.1	22.7	21.3	19.8
Buy						
	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Valuation basis	Recurring P/E (x)	66.56	35.09	21.65	19.67	18.91
28x FY23F P/E	P/B (x)	6.1	5.3	4.5	3.9	3.4
	FCF Yield (%)	3.4	(1.3)	4.7	5.0	5.4
Key drivers	Dividend Yield (%)	1.3	0.7	1.2	1.3	1.3
i. Tight inventory situation in the semiconductor industry	EV/EBITDA (x)	28.23	20.15	14.03	12.56	11.33
ii. New contract wins	EV/EBIT (x)	33.33	22.85	14.88	13.29	11.96
iii. Stronger contributions from the industrial gas (LCO2) business						
	Income statement (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Key risks	Total turnover	395	515	920	947	945
i. Sector valuation de-rating;	Gross profit	59	85	144	151	156
ii. Weaker than expected earnings/margins;	EBITDA	34	48	66	70	75
iii. Slower than expected orderbook replenishment.	Depreciation and amortisation	(5)	(6)	(4)	(4)	(4)
	Operating profit	28	42	62	67	71
	Net interest	(2)	(3)	(2)	(1)	(0)
Company Profile	Pre-tax profit	21	36	60	66	71
Kelington Group is involved in ultra-high purity (UHP) delivery systems, process engineering and general contracting. The company commenced maiden production of Liquid Carbon Dioxide (LCO2) in 4Q19	Taxation	(3)	(6)	(12)	(13)	(14)
	Reported net profit	17	29	47	52	56
	Recurring net profit	15	29	47	52	54
	Cash flow (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Change in working capital	18	(45)	1	(1)	(1)
	Cash flow from operations	46	(4)	53	56	60
	Capex	(11)	(10)	(5)	(5)	(5)
	Cash flow from investing activities	(10)	(17)	(5)	(5)	(5)
	Dividends paid	(5)	(6)	0	(12)	(13)
	Cash flow from financing activities	12	(10)	(25)	(37)	(13)
	Cash at beginning of period	85	132	106	128	142
	Net change in cash	47	(30)	23	14	42
	Ending balance cash	133	104	130	142	184
	Balance sheet (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total cash and equivalents	132	106	128	142	182
	Tangible fixed assets	60	64	66	67	68
	Total assets	350	404	501	521	562
	Short-term debt	28	29	4	4	4
	Total long-term debt	27	23	23	(2)	(2)
	Total liabilities	182	211	274	254	254
	Total equity	168	193	227	267	308
	Total liabilities & equity	350	404	501	521	562
	Key metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Revenue growth (%)	3.9	30.4	78.9	2.9	(0.1)
	Recurrent EPS growth (%)	(34.3)	89.7	62.1	10.0	4.0
	Gross margin (%)	14.9	16.6	15.6	16.0	16.5
	Operating EBITDA margin (%)	8.5	9.4	7.2	7.4	7.9
	Net profit margin (%)	4.4	5.6	5.1	5.5	5.9
	Dividend payout ratio (%)	73.7	25.0	25.0	25.0	24.0
	Capex/sales (%)	2.8	1.9	0.5	0.5	0.5
	Interest cover (x)	11.5	16.1	29.7	90.8	647.5

Source: Company data, RHB

Recommendation Chart

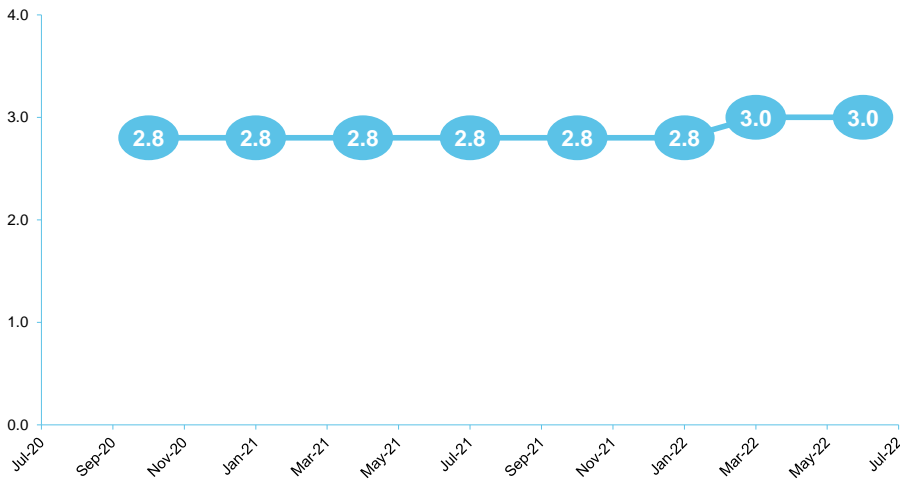


Source: RHB, Bloomberg

Date	Recommendation	Target Price
2022-06-03	Buy	1.60
2022-05-25	Buy	1.50
2022-03-09	Buy	1.70
2022-02-28	Buy	1.70
2022-02-09	Neutral	1.60
2021-12-01	Neutral	1.75
2021-10-07	Neutral	1.76
2021-09-15	Neutral	1.45
2021-08-25	Neutral	1.16
2021-06-15	Neutral	2.02
2021-03-16	Neutral	1.83
2021-03-05	Sell	1.83

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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