

28 February 2023

Construction & Engineering | Industrial

Kelington Group (KGRB MK)

Neutral (Maintained)

Doubling Up; Maintain NEUTRAL

Target Price (Return):	MYR1.59 (+5%)
Price (Market Cap):	MYR1.52 (USD218m)
ESG score:	3.00 (out of 4)
Avg Daily Turnover (MYR/USD)	2.20m/0.50m

- **NEUTRAL, new MYR1.59 TP from MYR1.53, 5% upside with c.2% FY23F yield.** Kelington Group's FY22 results were a beat, thanks to higher-than-expected revenue recognition, with quarterly revenue and earnings at record highs. We see FY23F earnings growth being supported by the solid MYR1.71bn outstanding orderbook. At +0.5SD from its historical P/E mean, the stock's valuation is fair, and reflects sentiment on the tech sector.

- **Ending the year on a high.** 4Q22 core earnings of MYR18m (+15% QoQ, +123% YoY) brought FY22 earnings to MYR55.6m (+91% YoY). This was 7% ahead of our and consensus' estimates. FY22 revenue jumped 147% YoY from higher contributions across all segments, particularly general contracting (GC; +350% YoY). Consequently, the EBIT margin was whittled down to 6.2% in FY22 (FY21: 7.4%) with the higher mix of GC revenue. We see margins normalising in the subsequent quarters, with a chunky GC project at its tail end and larger contributions from the higher-margin industrial gas business. A DPS of 1.5 sen was declared, bringing the full-year DPS to 2.5 sen (FY21: 1.5sen), implying a 29% payout.

- **Improvements all around.** Revenue from the ultra-high purity segment surged (+41% QoQ, YTD: +135%) on new contract wins from foundry capacity expansion, particularly in Singapore. The GC segment posted the highest topline growth (-28% QoQ, YTD: +350%), with the recognition of the MYR420m turnkey contract secured in 3Q21. Earnings prospects remained strong, backed by its MYR1.71bn outstanding orderbook and the record MYR1.85bn new orders secured in FY22 (FY21: MYR1.2bn). The group will focus on executing these projects, as well as seek new opportunities, with management previously guiding for fresh tenders to be called in 1H23 from principals such as Soitec, Micron, SMIC and Siltronic.

- **Industrial gas business building steam.** The segment continues to grow (-1% QoQ, YTD: +81) from stronger customer demand due to the economic reopening and exposure to new markets, including the Oceania countries. The second liquid carbon dioxide (LCO2) plant (70,000 tonnes), which is adjacent to its Phase 1 facility (50,000 tonnes), is expected to come on-stream by end-2023 and drive stronger recurring earnings going forward, providing some buffer to its project-based revenues.

- **Forecasts.** Our FY23-24F core earnings are adjusted by -1 to 6% post results. We introduce our FY25F earnings of MYR71m. Our TP rises to MYR1.59 after rolling forward to our base valuation year FY24F, and is still pegged to 21x. At +0.5SD from its historical P/E mean, we believe the strong earnings growth into FY24F has been priced in. Key upside/downside risks: Stronger-/weaker-than-expected earnings/margin and orderbook replenishment, and a re-/de-rating in the tech sector.

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (MYRm)	515	1,270	1,296	1,292	1,302
Recurring net profit (MYRm)	29	56	62	65	71
Recurring net profit growth (%)	89.7	90.9	11.5	5.2	8.2
Recurring P/E (x)	44.82	23.48	21.07	20.02	18.51
P/B (x)	6.8	5.5	5.0	4.4	3.8
P/CF (x)	na	46.06	4.49	18.40	17.16
Dividend Yield (%)	1.0	1.6	1.9	2.0	2.2
EV/EBITDA (x)	26.05	15.02	10.39	9.66	8.68
Return on average equity (%)	16.1	25.7	24.8	23.3	22.0
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

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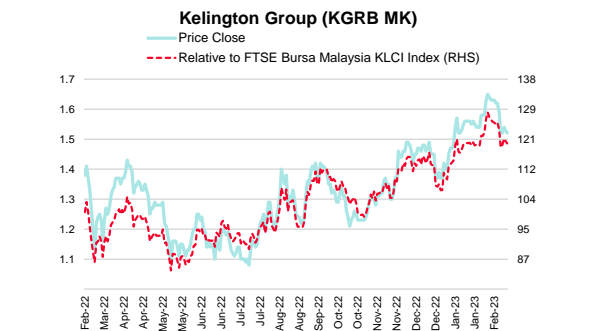


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	10.9	(2.6)	5.6	16.9	6.3
Relative	13.6	0.2	7.7	19.9	14.9
52-wk Price low/high (MYR)	1.08 – 1.65				



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.

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Malaysia	Recurring EPS	0.03	0.06	0.07	0.08	0.08
Construction & Engineering	DPS	0.02	0.03	0.03	0.03	0.03
Kelington Group	BVPS	0.22	0.28	0.30	0.35	0.40
KGRB MK	Return on average equity (%)	16.1	25.7	24.8	23.3	22.0
Neutral						
	Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Recurring P/E (x)	44.82	23.48	21.07	20.02	18.51
	P/B (x)	6.8	5.5	5.0	4.4	3.8
	FCF Yield (%)	(1.0)	(1.2)	21.9	5.1	5.4
	Dividend Yield (%)	1.0	1.6	1.9	2.0	2.2
	EV/EBITDA (x)	26.05	15.02	10.39	9.66	8.68
	EV/EBIT (x)	29.54	16.46	11.05	10.25	9.17
	Income statement (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Total turnover	515	1,270	1,296	1,292	1,302
	Gross profit	85	140	158	171	187
	EBITDA	48	86	98	101	108
	Depreciation and amortisation	(6)	(8)	(6)	(6)	(6)
	Operating profit	42	78	92	96	102
	Net interest	(3)	(5)	(11)	(11)	(11)
	Pre-tax profit	36	74	81	85	92
	Taxation	(6)	(15)	(16)	(17)	(18)
	Reported net profit	29	55	62	65	71
	Recurring net profit	29	56	62	65	71
	Cash flow (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Change in working capital	(45)	(56)	220	(3)	(3)
	Cash flow from operations	(4)	28	291	71	76
	Capex	(10)	(44)	(5)	(5)	(5)
	Cash flow from investing activities	(13)	(51)	(11)	(5)	(5)
	Dividends paid	(6)	(13)	0	(25)	(26)
	Cash flow from financing activities	(10)	164	(25)	(25)	(26)
	Cash at beginning of period	132	106	259	506	547
	Net change in cash	(26)	141	255	41	45
	Ending balance cash	108	250	514	547	592
	Balance sheet (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Total cash and equivalents	106	259	506	547	592
	Tangible fixed assets	64	102	101	101	100
	Total assets	404	1,060	1,143	1,183	1,229
	Short-term debt	29	203	203	203	203
	Total long-term debt	23	33	8	8	8
	Total liabilities	211	817	876	874	874
	Total equity	193	242	267	309	354
	Total liabilities & equity	404	1,060	1,143	1,183	1,229
	Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Revenue growth (%)	30.4	146.7	2.1	(0.3)	0.8
	Recurrent EPS growth (%)	89.7	90.9	11.5	5.2	8.2
	Gross margin (%)	16.6	11.1	12.2	13.3	14.4
	Operating EBITDA margin (%)	9.4	6.7	7.6	7.9	8.3
	Net profit margin (%)	5.6	4.4	4.8	5.1	5.4
	Dividend payout ratio (%)	44.5	38.8	40.0	40.0	40.0
	Capex/sales (%)	1.9	3.4	0.4	0.4	0.4
	Interest cover (x)	16.1	17.2	8.2	9.1	9.7

Source: Company data, RHB

Results At a Glance

Figure 1: KGB's results summary

FYE Dec (MYRm)	4Q21	3Q22	4Q22	QoQ (%)	YoY (%)	FY21	FY22	YoY (%)	Comments
Revenue	177.0	366.4	417.4	14%	136%	514.6	1,269.5	147%	Higher contributions across all divisions
EBIT	10.9	20.0	27.9	39%	156%	38.3	78.2	104%	
<i>EBIT margin (%)</i>	6.2%	5.5%	6.7%			7.4%	6.2%		FY22 EBIT margin narrowed, with revenue contributions from GC
Other income	1.4	0.3	2.5	882%	84%	6.1	4.2	-30%	
Finance Costs	(0.4)	(1.2)	(1.7)	-46%	-293%	(2.6)	(4.5)	-72%	
Pretax profit	10.5	18.8	26.2	39%	150%	35.7	73.6	106%	
<i>Pretax margin (%)</i>	5.9%	5.1%	6.3%			7%	6%		
Tax	(2.1)	(2.5)	(6.8)	-171%	-218%	(6.0)	(15.5)	-158%	
Effective tax rate (%)	20%	13%	26%			17%	21%		
Minority interest	0.2	0.6	1.5	145%	607%	0.7	2.8		
Net Profit	8.1	15.7	17.8	14%	120%	29.0	55.4	91%	
Core Profit	8.1	15.7	18.0	15%	123%	29.2	55.6	91%	Ahead of expectations
<i>Core net margin (%)</i>	5%	4%	4%			5.7%	4.4%		

Source: Company data

Figure 2: Segmental revenue

FYE Dec (MYRm)	4Q21	3Q22	4Q22	QoQ (%)	YoY (%)	FY21	FY22	YoY (%)
Ultra High Purity	109.1	209.9	295.8	41%	171%	344.3	810.3	135%
Process Engineering	22.8	14.1	13.4	-5%	-41%	62.0	51.0	-18%
General Contracting	37.7	121.9	87.8	-28%	133%	76.9	345.8	350%
Industrial Gases	10.6	20.5	20.3	-1%	92%	34.5	62.4	81%
Total Revenue	180.1	366.4	417.4	14%	132%	517.7	1269.5	145%

Source: Company data

Recommendation Chart

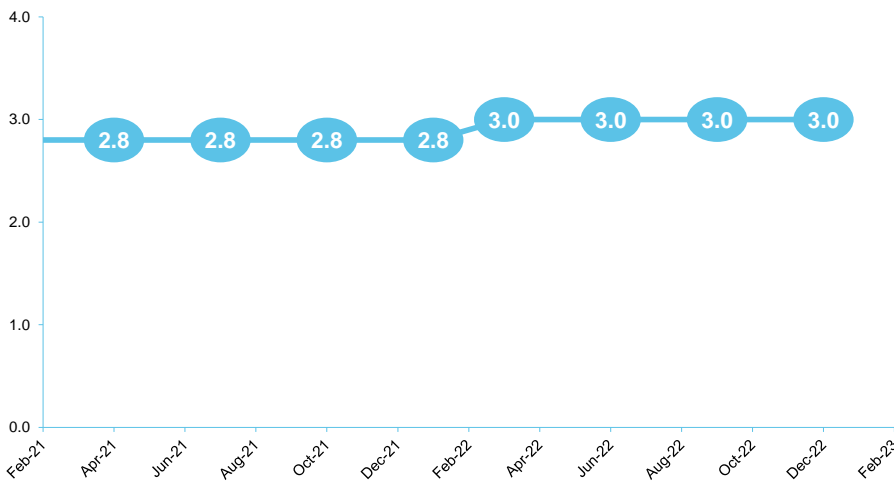


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-12-22	Neutral	1.53	1.45
2022-11-21	Buy	1.53	1.32
2022-09-08	Buy	1.71	1.35
2022-07-28	Buy	1.69	1.22
2022-06-03	Buy	1.60	1.25
2022-05-25	Buy	1.50	1.11
2022-03-09	Buy	1.70	1.22
2022-02-28	Buy	1.70	1.38
2022-02-09	Neutral	1.60	1.56
2021-12-01	Neutral	1.75	1.62
2021-10-07	Neutral	1.76	1.77
2021-09-15	Neutral	1.45	1.66
2021-08-25	Neutral	1.16	1.27
2021-06-15	Neutral	2.02	1.10
2021-03-16	Neutral	1.83	0.98

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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