

Kelington Group

Poised for Better Margins and More Jobs

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KGB guided for its boosted margins to sustain in the coming quarters given the delivery of high-margin ultra-high purity (UHP) gas systems. It is poised to bag a few more jobs to end the year with RM1b job wins (vs. YTD RM858m). Its LCO2 Plant 2 is coming online by end-CY23, just in time to capitalise on the current LCO2 shortages in the market. We maintain our forecasts, TP of RM3.28 and OUTPERFORM call.

We came away from KGB's post-3QFY23 briefing thrilled about its near-term prospects. The key takeaways from the meeting are as follow:

1. The margin recovery in the reported 3QFY23 was on the back of favourable revenue mix as the group refocused its resources on higher-margin UHP gas systems after completing the turnkey job for an MNC that produces memory chips. With UHP making up 68% (vs. 59% in the recent 3QFY23) of its RM1.5b outstanding orderbook, the group anticipates improving margins and hence profitability in coming quarters.
2. Despite *SEMI*'s estimate of an 18% decline in fab equipment spending in 2023, KGB has successfully replenished RM858m net orders YTD. With several high-potential orders in final stages, including a significant hook-up job in China's largest foundry, the company is poised to achieve our RM1b replenishment target. Upon securing this, it will add on to the existing five foundries from the same customer that KGB has secured renewals until the end of 2024, solidifying its position as the leader in the region.
3. Its LCO2 (liquid CO2) Plant 2, with capacity of 70k tonnes/year or 1.4x of Plant 1, has been completed and will begin testing and commissioning next week. This means the group could start exporting from Plant 2 as early as end-2023. This will alleviate the bottleneck at Plant 1 (running near 100%) as demand continues to increase with a worsening shortage of LCO2 in Asia and the Oceania region.
4. Our conviction in KGB's prospects is well-founded, supported by its impressive >RM2.1b tender book and its commanding presence in the regions it serves. The robust tender pipeline is in line with *SEMI*'s forecast of a 12% recovery in 2024, followed by a substantial 24% upcycle in 2025. Be it a smooth or bumpy recovery for the semiconductor sector, the group still has RM1.5b outstanding orders in its bag to navigate any obstacles that may come along, thereby fortifying its readiness for the next wave.

Forecasts. Maintained.

We keep our TP of RM3.28 based on an unchanged 21x FY24F PER. Our valuation represents a c.10% discount to peer's forward mean PER of 24x which includes global players such as Air Products, Air Liquide and Linde. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

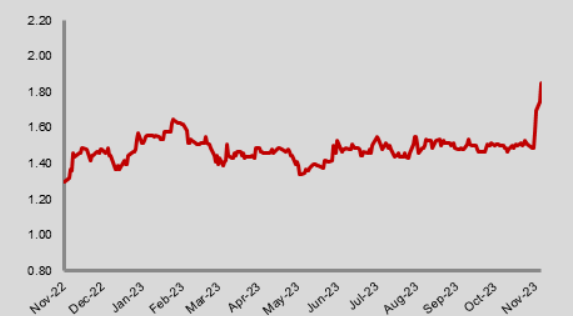
Investment thesis. We like KGB for: (i) it being a direct proxy to the front-end wafer fab expansion, (ii) its strong earnings visibility underpinned by robust order book and tender book exceeding RM1b, and (iii) its strong foothold in multiple markets, i.e. Malaysia, Singapore and China. Maintain **OUTPERFORM**.

Risks to our call include: (i) chip makers halting their expansion plans due to oversupply, (ii) worsening Sino-US chip war, and (iii) delays in its LCO2 plant expansion.

OUTPERFORM ↔

Price : **RM1.84**
Target Price : **RM3.28** ↔

Share Price Performance



KLCI	1,446.1
YTD KLCI chg	-3.1%
YTD stock price chg	27.0%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	KGRB MK Equity
Market Cap (RM m)	1,186.4
Shares Outstanding	643.0
52-week range (H)	1.80
52-week range (L)	1.31
3-mth avg daily vol:	1,390,747
Free Float	49.8%
Beta	0.9

Major Shareholders

Palace Star	21.1%
Sun Lead International Ltd	6.2%
AmanahRaya Trustees	5.5%

Summary Earnings Table

FYE Dec (RM m)	2022A	2023F	2024F
Turnover	1,269.5	1,508.8	1,565.3
EBITDA	85.7	139.5	155.7
PBT	73.6	120.2	133.3
Net Profit	55.4	90.4	100.3
Consensus	-	84.2	88.8
Earning. Revision	-	-	-
EPS (sen)	8.6	14.1	15.6
EPS growth (%)	74.1	63.3	10.9
NDPS (sen)	2.5	3.9	4.3
BVPS (RM)	0.37	0.47	0.59
Price/BV (x)	4.9	3.9	3.1
PER (x)	21.2	13.0	11.7
Net gearing (x)	(0.2)	0.0	(0.2)
ROA (%)	5.2	8.0	8.2
ROE (%)	23.2	29.7	26.6
Dividend Yield (%)	1.4	2.1	2.4

Income Statement

FY Dec (RM m)	2020A	2021A	2022A	2023F	2024F
Revenue	394.6	517.7	1,269.5	1,508.8	1,565.3
EBITDA	33.5	46.9	85.7	139.5	155.7
Depre & Amor	-5.1	-5.7	-7.5	-9.3	-12.5
Operating Profit	28.4	41.3	78.2	130.2	143.3
Other Income	8.7	5.8	4.2	5.0	5.2
Interest Exp	-2.5	-2.8	-4.5	-9.9	-9.9
Associate	-5.0	0.0	0.0	0.0	0.0
PBT	20.9	38.5	73.6	120.2	133.3
Taxation	-3.4	-5.9	-15.5	-25.3	-28.1
Minority Interest	0.1	0.7	2.8	4.5	5.0
Net Profit	17.5	31.8	55.4	90.4	100.3
Core Net Profit	17.5	31.8	55.4	90.4	100.3

Balance Sheet

FY Dec (RM m)	2020A	2021A	2022A	2023F	2024F
Fixed Assets	59.7	64.2	102.4	136.6	144.1
Intangible Assets	6.4	5.5	6.8	6.8	6.8
Other FA	4.7	7.0	8.4	8.4	8.4
Inventories	2.8	6.9	21.3	24.7	25.4
Receivables	74.2	91.7	384.6	457.1	474.3
Other CA	70.6	128.7	276.6	276.6	276.6
Cash	132.0	106.3	259.5	221.7	283.3
Total Assets	350.3	410.3	1,059.5	1,131.8	1,218.9
Payables	89.1	118.5	263.9	305.2	314.2
ST Borrowings	28.3	26.9	202.8	202.8	202.8
Other ST Liability	35.1	40.6	311.2	290.7	295.6
LT Borrowings	27.2	25.1	20.1	20.1	20.1
Other LT Liability	2.4	3.6	3.6	3.6	3.6
Net Assets	168.3	195.6	258.1	309.4	382.6
Shr. Equity	168.0	194.6	238.6	304.6	377.1
Mnrt. Interest	0.3	1.0	3.8	4.9	5.5
Total Equity	168.3	195.6	242.4	309.4	382.6

Cashflow Statement

FY Dec (RM m)	2020A	2021A	2022A	2023F	2024F
Operating CF	45.7	-6.2	28.4	58.2	106.4
Investing CF	-12.0	-13.3	-51.4	-43.6	-20.0
Financing CF	11.3	-10.9	163.8	-22.0	-24.7

Financial Data & Ratios

FY Dec	2020A	2021A	2022A	2023F	2024F
Growth (%)					
Turnover	3.9	31.2	145.2	18.8	3.7
EBITDA	-4.1	40.0	82.5	62.9	11.6
Operating Profit	-13.6	45.3	89.5	66.5	10.1
PBT	-33.7	83.8	91.3	63.3	10.9
Adj Net Profit	-28.3	81.8	74.1	63.3	10.9
Profitability (%)					
EBITDA Margin	8.5	9.1	6.7	9.2	10.0
Operating Margin	7.2	8.0	6.2	8.6	9.2
PBT Margin	5.3	7.4	5.8	8.0	8.5
Core Net Margin	4.4	6.1	4.4	6.0	6.4
Effective Tax Rate	16.0	15.4	21.0	21.0	21.0
ROA	6.1	5.0	7.8	5.2	8.0
ROE	10.4	16.4	23.2	29.7	26.6
DuPont Analysis					
Net Margin (%)	4.4	6.1	4.4	6.0	6.4
Assets Turnover (x)	1.1	1.3	1.2	1.3	1.3
Leverage Factor (x)	2.1	2.1	4.4	3.7	3.2
ROE (%)	10.4	16.4	23.2	29.7	26.6
Leverage					
Debt/Asset (x)	0.2	0.1	0.2	0.2	0.2
Debt/Equity (x)	0.3	0.3	0.9	0.7	0.6
Net (Cash)/Debt	-76.5	-54.3	-36.6	1.1	-60.5
Net Debt/Equity (x)	-0.5	-0.3	-0.2	0.0	-0.2
Valuations					
Core EPS (sen)	2.8	4.9	8.6	14.1	15.6
DPS (sen)	0.8	1.5	2.5	3.9	4.3
BVPS (RM)	0.3	0.3	0.4	0.5	0.6
PER (x)	66.1	37.0	21.2	13.0	11.7
Div. Yield (%)	0.4	0.8	1.4	2.1	2.4
P/BV (x)	6.9	6.0	4.9	3.9	3.1
EV/EBITDA (x)	32.2	23.9	13.3	8.5	7.2

Source: Kenanga Research

30 November 2023

Malaysian Technology Peers Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Mkt Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) – Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div. Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
D&O GREEN TECHNOLOGIES BHD	UP	3.53	2.30	-34.8%	4,371.2	Y	12/2023	3.7	7.0	-52.9%	89.7%	95.4	50.3	5.0	5.2%	0.6	0.2%
GHL SYSTEMS BHD	OP	0.750	0.880	17.3%	856.1	Y	12/2023	2.4	2.8	-3.5%	15.8%	31.4	27.2	1.6	5.2%	0.0	0.0%
INARI AMERTRON BHD	OP	2.88	4.17	44.8%	10,785.0	Y	06/2024	10.4	12.4	20.5%	18.8%	27.6	23.2	4.1	14.9%	9.9	3.4%
JHM CONSOLIDATION BHD	MP	0.710	0.700	-1.4%	430.3	Y	12/2023	2.1	4.6	-43.5%	116.2%	33.2	15.3	1.3	4.1%	0.5	0.7%
KELINGTON GROUP BHD	OP	1.84	3.28	78.3%	1,186.4	Y	12/2023	14.1	15.6	63.2%	11.0%	13.1	11.8	3.8	32.8%	3.9	2.1%
KESM INDUSTRIES BHD	MP	6.86	7.06	2.9%	295.1	Y	07/2024	6.3	10.2	-44.9%	63.0%	110.9	66.3	0.8	0.8%	0.0	0.0%
LGMS BHD	OP	0.980	1.16	18.4%	446.9	Y	12/2023	2.2	4.6	-19.0%	106.9%	43.9	21.2	4.8	11.5%	0.0	0.0%
M'SIAN PACIFIC INDUSTRIES BHD	MP	26.98	27.20	0.8%	5,366.2	Y	06/2024	80.9	118.2	162.5%	46.1%	33.3	22.8	2.5	7.8%	35.0	1.3%
NATIONGATE HOLDINGS BHD	OP	1.31	1.70	29.8%	2,716.9	Y	12/2023	3.4	6.8	-16.6%	97.5%	38.1	19.3	9.2	27.2%	0.3	0.2%
OPPSTAR BHD	MP	1.28	1.82	42.2%	814.3	Y	03/2024	4.0	6.1	20.8%	50.8%	31.8	21.1	5.2	17.5%	1.0	0.8%
P.I.E. INDUSTRIAL BHD	OP	3.21	3.80	18.4%	1,232.8	Y	12/2022	17.7	21.1	-4.2%	19.5%	18.1	15.2	2.0	11.7%	7.0	2.2%
SKP RESOURCES BHD	MP	0.790	0.950	20.3%	1,226.5	Y	03/2024	6.3	7.1	-31.6%	12.5%	12.5	11.1	1.4	11.4%	3.2	4.1%
UNISEM (M) BHD	UP	3.38	2.00	-40.8%	5,452.2	Y	12/2023	4.7	10.0	-68.6%	111.6%	71.4	33.7	2.3	3.2%	6.0	1.8%
Simple Average										-7.0%	39.2%	32.6	23.4	3.4	11.8%		1.3%

Source: Kenanga Research

Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★	☆	
	Community Investment	★	★	★	☆	
	Workers Safety & Wellbeing	★	★	★		
	Corporate Governance	★	★	★		
	Anti-Corruption Policy	★	★	★		
	Emissions Management	★	★	★	★	
SPECIFIC	Technology & Innovation	★	★	☆		
	Supply Chain Management	★	★	★	☆	
	Energy Efficiency	★	★	★		
	Effluent/Water Management	★	★	★		
	Waste Management	★	★	★		
	Ethical Practices	★	★	★		
OVERALL		★	★	★		

- ☆ denotes half-star
- ★ -10% discount to TP
- ★★ -5% discount to TP
- ★★★ TP unchanged
- ★★★★ +5% premium to TP
- ★★★★★ +10% premium to TP

Stock Ratings are defined as follows:

Stock Recommendations

- OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
- MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
- UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

- OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
- NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
- UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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