KKB Engineering Berhad

(9466 | KKB MK) Main | Industrial Products & Services

***Maintain* BUY**

Weaker bottom line but prospects intact

***Unchanged* Target Price: RM1.50**

KEY INVESTMENT HIGHLIGHTS

- **2QFY22 core net profit down -34.7%yoy to RM1.6m, despite stronger revenue at +35.4%yoy to RM109.7m**
- **Compressed margins mainly due to higher Covid-related costs and unfavourable weather affecting offshore steel fabrication**
- **Extra costs incurred to be recovered in subsequent quarters**
- **Civil construction revenue surged +142%yoy to RM71m from Pan Borneo Highway and water-related construction jobs**
- **Maintain BUY with an unchanged target price of RM1.50**

Below expectation. KKB Engineering's 2QFY22 core net profit dipped -34.7%yoy to RM1.6m, despite a stronger quarterly revenue which came in +35.4%yoy higher at RM109.7m, attributable to eroded margins from the group's steel fabrication division. For the cumulative 1HFY22, core earnings were lower by -67.5%yoy at RM3.8m, which is below our expectations, making up only 15.3% of our full year estimates.

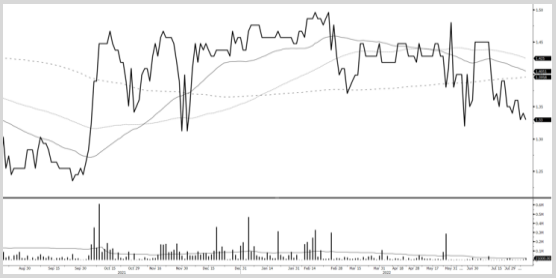
Eroded margins. Revenue from the group's engineering segment, which comprises civil construction, steel fabrication and hot dip galvanising divisions, jumped +44.1%yoy to RM107.5m for the quarter, but margins declined to 2.5% as compared to 4.5% from the same quarter last year. Management guided that margins were lower due to higher Covid-related costs from its offshore steel fabrication jobs where strict measures had to be complied with, such as quarantine and frequent testing. Higher costs were also incurred due to the hiring of vessels for the jobs due to the unfavourable weather during the quarter. This also resulted in revenue from steel fabrication declining -19%yoy to RM35.8m. Management is confident of recovering the additional costs from their clients by way of variation order in the coming quarters.

Stronger civil construction revenue. KKB's civil construction revenue surged +142%yoy for the quarter to RM71m, contributed mainly from higher progress claims from the Pan Borneo Highway project, where the group is undertaking Phase 1 of Works Package Contract-09 (WPC-09), in a 70:30 joint-venture arrangement with WCT Bhd. This came up to RM59.4m, as compared to RM18.8m in 2QFY21. Water-related construction jobs also posted higher revenue at RM10.7m, which was 6%yoy higher.

Weaker manufacturing numbers. KKB's manufacturing segment was -65%yoy lower while the segment's earnings slipped into the red at -RM314,222. This was attributed to lower activities for both the steel pipes and LP gas cylinders manufacturing divisions. On a quarter-on-quarter basis however, this was an improvement in both revenue and earnings by +66.8%qoq and +73.7%qoq respectively.

RETURN STATISTICS	
Price @ 18th August 2022 (RM)	**1.33**
Expected share price return (%)	**+12.8**
Expected dividend yield (%)	**+3.3**
Expected total return (%)	**+16.1**

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-1.5	-7.1
3 months	-2.2	-9.1
12 months	-1.5	-0.9

KEY STATISTICS	
FBM KLCI	1,516.62
Syariah compliant	Yes
F4BGM Index	N.A.
ESG Grading Band (Star Rating)	☆
Issue shares (m)	288.73
Estimated free float (%)	15.30
Market Capitalisation (RM'm)	384.01
52-wk price range	RM1.28 - RM1.58
Beta vs FBM KLCI (x)	0.69
Monthly velocity (%)	0.00
Monthly volatility (%)	20.85
3-mth average daily volume (m)	0.01
3-mth average daily value (RM'm)	0.01
Top Shareholders (%)	
Kho Kak Beng Holding Co Sdn Bhd	38.83
Cahya Mata Sarawak Bhd	17.90
Sarawak Economic Development Corp	10.71

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Earnings estimates. We are making no changes to our FY22 and FY24 estimates.

Target price. We are maintaining our TP of **RM1.50** by pegging its FY23F core EPS of 9.7 sen to our target PER of 15.5x, which is +0.25 SD above the Group's 4-year mean PER. We believe is justified in view of the Group's normalising earnings after rebounding from its net loss in FY16 and the improved prospects of it securing more infrastructure and oil and gas related jobs in Sarawak.

Maintain BUY. We remain optimistic on KKB's prospects as evident from its improving civil construction earnings. Opportunities in securing new jobs remains aplenty in Sarawak with the state government projecting a capital injection of about RM100b by 2030. We expect job flows in the nearer term to come from retendering of delayed or abandoned projects as the administration focuses on fixing sick projects, on top of rolling out new infrastructure works. Management is also optimistic on being awarded that numerous tenders it is currently pursuing will be awarded next year. The state-owned Sarawak Economic Development Corporation (SEDC) holds 10.7% in KKB through a private placement in Dec-21 and KKB aims to leverage on this and make use of the competitive strength of both KKB and SEDC to expand and tap into the vast business opportunities in Sarawak.

INVESTMENT STATISTICS

FYE 31st Dec (All in RM'm unless stated otherwise)	**2020A**	**2021A**	**2022F**	**2023F**	**2024F**
Revenue	407.9	391.6	414.5	437.2	430.4
Gross profit	67.4	71.6	69.2	77.1	74.4
Operating profit	35.0	38.0	38.5	44.0	40.5
Share of results of associates	1.7	1.1	1.1	1.0	1.0
Profit before tax	35.5	34.0	39.8	44.7	40.1
Income tax expense	(13.7)	(5.2)	(9.5)	(10.8)	(10.2)
Profit for the period	21.8	28.9	30.3	33.9	29.9
Basic EPS	6.9	10.1	10.5	11.7	10.4
Dividend per share (sen)	4.0	5.0	5.0	5.0	5.0
Core net profit	17.5	25.9	24.8	28.0	25.0
Core EPS	6.8	9.0	8.6	9.7	8.7

Source: Company, MIDFR

KKB Engineering: QFY22 RESULTS SUMMARY

All in RM'm unless stated otherwise	Quarterly Results					Cumulative		
Income Statement	**Q222**	**Q122**	**Q221**	**QoQ**	**YoY**	**2H22**	**2H21**	**YoY**
Revenue	109.7	93.4	81.0	**17%**	**35%**	203.1	180.8	**12%**
Gross profit	10.6	11.3	14.0	**-6%**	**-25%**	21.9	35.6	**-39%**
Administrative expenses	-8.3	-8.5	-9.2	**-2%**	**-9%**	-16.9	-17.6	**-4%**
Finance costs	-0.1	0.0	-0.8	**>100%**	**-93%**	-0.1	-1.7	**-95%**
Other expenses	-0.6	-0.6	-0.6	**-1%**	**0%**	-1.2	-1.5	**-20%**
Other income	0.8	1.0	1.0	**-20%**	**-14%**	1.9	2.1	**-9%**
Share of results of associates	0.3	0.0	0.3	**>100%**	**2%**	0.3	0.9	**-65%**
Profit before tax	2.8	3.2	4.6	**-10%**	**-39%**	6.0	17.8	**-66%**
Tax expense	-0.4	-1.1	-1.1	**-63%**	**-63%**	-1.5	-2.5	**-40%**
Core net profit	1.6	2.2	2.5	**-27%**	**-35%**	3.8	11.7	**-68%**

Source: Company, MIDFR

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MIDF AMANAH INVESTMENT BANK: GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology