KKB Engineering

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

***Upgrade to* BUY**

Higher costs weigh on earnings

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

KEY INVESTMENT HIGHLIGHTS

- **9MY22 core net profit down -68.0%yoy to RM6.8m, despite stronger revenue at +9.0%yoy to RM305.1m**
- **Excluded one-off RM2m donation made in conjunction with 60th anniversary**
- **Eroded margins due to higher raw material prices and input costs.**
- **Civil construction revenue almost doubled to RM70.9m for the quarter**
- **Upgrade to BUY (downgraded previously due to run-up in share price) with an unchanged target price of RM1.50**

Below expectations. KKB Engineering's 3QFY22 core net profit dipped -68.5%yoy to RM3.0m, after excluding a one-off RM2.0m donation in September that was made in conjunction with the company's 60th anniversary. For the cumulative 9MFY22, core earnings were -68.0%yoy lower at RM6.8m which was below our expectations, making up only 27.6% of our full-year estimates.

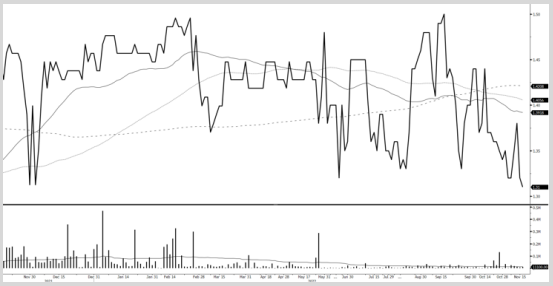
Weaker margins. The group's total revenue for the quarter was RM102.0m, an increase of +2.9%yoy. Operating profit was -57.9%yoy lower to RM5.7m, representing a margin of 5.6% as compared to 13.6% in 3QFY21. However, this was an improvement over 2QFY22 which recorded a margin of 2.0%. For 9MFY22, KKB's revenue was RM305.1m, an increase of +9.0%yoy. Despite that, operating profit recorded a –66.2%yoy decline to RM10.5m. Margins saw a decline from 11.1% to 3.5%. The eroded margins can be attributable to higher raw material prices and input costs.

Engineering segment. Revenue from this segment was the main contributor to the group at RM97.0m in the quarter. Though this was a +3.7%yoy increase, earnings saw a decline of -58.9%yoy to RM3.8m. The main driver for the segment was the civil construction division, which almost doubled to RM70.9m in revenue, mainly due to higher progress claims from its Pan Borneo Highway package in Sarawak. KKB's steel fabrication division which is also parked under this segment, saw a decline in revenue by -54.9% to RM25.3m for the quarter.

Manufacturing segment. KKB's manufacturing segment declined -10.0%yoy to RM5m for the quarter. On a quarter-on-quarter comparison however, this more than doubled from RM2.3m in 2QFY22. The bottom line for the segment was still in the red at -RM250,740, though this had picked up by about +20.2% from the previous quarter. This was due to lower activities for its steel pipes and LP gas cylinders manufacturing divisions, which contributed RM1.9m and RM3.1m of revenues respectively. While the latter continues to be supported with its supply of LPG compact valves, new cylinders and reconditioning/requalification, the performance of the steel pipes

RETURN STATISTICS	
Price @ 16th Nov 2022 (RM)	**1.31**
Expected share price return (%)	**+14.5**
Expected dividend yield (%)	**+3.3**
Expected total return (%)	**+17.8**

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-9.0	-12.9
3 months	-6.4	2.5
12 months	-12.7	-8.0

KEY STATISTICS	
FBM KLCI	1,448.38
Syariah compliant	Yes
F4BGM Index	N.A.
ESG Grading Band (Star Rating)	☆
Issue shares (m)	288.73
Estimated free float (%)	15.24
Market Capitalisation (RM'm)	378.23
52-wk price range	RM1.28 - RM1.58
Beta vs FBM KLCI (x)	0.52
3-mth average daily volume (m)	0.01
3-mth average daily value (RM'm)	0.02
Top Shareholders (%)	
Kho Kak Beng Holding Co Sdn Bhd	38.89
Cahya Mata Sarawak Bhd	17.90
Sarawak Economic Development Corp	10.71

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division is expected to be division is expected to be weighed by the ongoing absence of new major contracts.

Earnings estimates. We expect our revenue projections to remain intact but we are slashing our FY22E core earnings expectations by 30% to RM17.3m to reflect the weaker margins. We are maintaining our FY23F expectations for now as we expect a favourable year for the construction sector next year.

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 jobs in Sarawak.

Upgrade to BUY. We are upgrading our recommendation to **BUY**. We have previously downgraded KKB to NEUTRAL mainly due to the run up in its share price. We remain optimistic on KKB's prospects as evident from its improving civil construction division. Margins are also expected to improve in the coming quarters with the easing of building material prices such as steel bars, which has declined for four consecutive months up to October. 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.

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	55.3	77.1	74.4
Operating profit	35.0	38.0	27.0	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	27.9	44.7	40.1
Income tax expense	(13.7)	(5.2)	(2.5)	(10.8)	(10.2)
Profit for the period	21.8	28.9	21.2	33.9	29.9
Basic EPS	6.9	10.1	9.99	11.7	10.4
Dividend per share (sen)	4.0	5.0	4.0	5.0	5.0
Core net profit	17.5	25.9	17.3	28.0	25.0
Core EPS	6.8	9.0	6.0	9.7	8.7

Source: Company, MIDFR

KKB Engineering: 3QFY22 RESULTS SUMMARY

All in RM'm unless stated otherwise	**Quarterly Results**					**Cumulative**		
Income Statement	**Q322**	**Q222**	**Q321**	**QoQ**	**YoY**	**9M22**	**9M21**	**YoY**
Revenue	102.0	109.7	99.1	**-7%**	**3%**	305.1	279.9	**9%**
Gross profit	13.5	10.6	22.0	**28%**	**-38%**	35.4	57.6	**-39%**
Administrative expenses	-7.8	-8.3	-8.2	**-6%**	**-5%**	-24.7	-25.8	**-4%**
Finance costs	-0.1	-0.1	-0.9	**>100%**	**-86%**	-0.2	-2.6	**-92%**
Other expenses	-2.5	-0.6	-0.7	**>100%**	**>100%**	-3.7	-2.1	**75%**
Other income	1.0	0.8	1.3	**17%**	**-22%**	2.8	3.3	**-14%**
Share of results of associates	0.4	0.3	0.2	**27%**	**>100%**	0.7	1.0	**-33%**
Profit before tax	4.5	2.8	13.5	**59%**	**-67%**	10.5	31.3	**-67%**
Tax expense	-0.9	-0.4	-3.6	**>100%**	**-75%**	-2.4	-6.1	**-61%**
Core net profit	3.0	1.6	9.6	**88%**	**-69%**	6.8	21.4	**-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