

21 November 2018 | 9MFY18 Results Review

KKB Engineering Bhd

Showing its mettle

Maintain BUY

Maintain Target Price (TP): RM1.13

INVESTMENT HIGHLIGHTS

- **3QFY18 earnings were ahead of ours and market consensus estimates.**
- **Higher contribution from Pan Borneo Highway and steel fabrication projects steered revenue upwards**
- **Earnings forecasts fine-tuned to reflect better progress rate**
- **We maintain our BUY call on KKB with an unchanged TP of RM1.13**

3QFY18 earnings stronger than expected. KKB's 3QFY18 PATAMI came in strong at RM6.9m (+>100%yoy). As a result, its 9MFY18 earnings came in ahead of ours and consensus expectations. Main contributor was the significant improvement in both steel fabrication and construction segments contributions.

Higher contribution from Pan Borneo Highway (PBH) ... The group's operating revenue staged major improvement compared to last year, rising by +127.5%yoy to RM112.2m. Revenue contributions were largely driven by engineering and construction sector, which made up 88.9% of the quarterly aggregate. The segment was strongly supported by PBH package, which have so far recognized progression of approximately 20%. Recall that the project was awarded to KKB-WCT JV (70:30) in 3Q16, which had added a whopping RM900.0m to its order book.

...and steel fabrication projects steered revenue upwards. The strength in revenue was also backed by steel fabrication division, which added another RM39.7m (+98.5%yoy) to revenue. We noted that the work orders for D28 Phase 1 project by Petronas Carigali has started to contribute earnings positively. It was awarded to KKB in March 2018, with construction works expected to complete by year end. In subsequent months onwards, we expect contribution of similar quantum will be recognized as we take into account the work progress of Wellhead Platforms for D18 Phase 2 project.

KKB's latest outstanding order book stood at RM0.9b, implying 4.0x cover to FY17 revenue. Moving forward, its healthy order book will provide stable outlook for FYE18/FYE19/FYE20 respectively. We expect the group's engineering and construction sector to be the driver of earnings, owing to the contribution from PBH and steel fabrication projects. Going ahead, further optimism is fuelled by Sarawak government's persistence, in solving the problem of water supply coverage. We noted that a sum of RM2.8b was allocated to fund a total of 247 water and water-related projects for implementation in the next two years.

RETURN STATS	
Price (19 Nov 2018)	RM0.90
Target Price	RM1.13
Expected Share Price Return	+25.6%
Expected Dividend Yield	2.2%
Expected Total Return	+27.8%

STOCK INFO	
KLCI	1,710.7
Bursa / Bloomberg	9466 / KKB MK
Board / Sector	Main/Construction
Syariah Compliant	Yes
Issued shares (mil)	257.8
Market cap. (RM'm)	233.3
Price over NA	0.82x
52-wk price Range	RM0.78 – RM1.08
Beta (against KLCI)	0.95x
3-mth Avg Daily Vol	0.05m
3-mth Avg Daily Value	RM0.05m
Major Shareholders (%)	
Kho Kak Beng Hldg	42.93
CMSB	20.05
Laman Satria S/B	5.59

Experience counts. KKB's long experience in the business as well as its value chain advantage will remain their competitive edge, to compete for future infrastructure and engineering projects in East Malaysia. As Sarawak's sole water pipe manufacturer, KKB is poised to benefit from projects which involve the supply of steel water pipes and structural steel, which are potentially be awarded under the state water grid project.

Changes in earnings. Our earnings forecasts are revised to reflect on the better progress billings for the works completed. To reflect this development, we have adjusted our net profit forecast in FY18 to a quantum of RM14.0m. We maintain our FY19 forecast at this juncture, to make allowance for the warranty period (12 months) for its Petronas Wellhead platform projects.

Our view. We have to be mindful that KKB's prospect is not in isolation of the local construction industry outlook. The trend was apparent post election, with the revision of mega projects led to sector-wide uncertainties. Like most construction-related stocks, KKB's stock was not exempted from the weaken share price performance (-17.0%). Despite the drift, we highlight KKB's strong prospect as it is mainly exclusive to Sarawak infrastructure development, helmed by the internal state funds. This should mitigate any headwinds that are facing the construction sector currently.

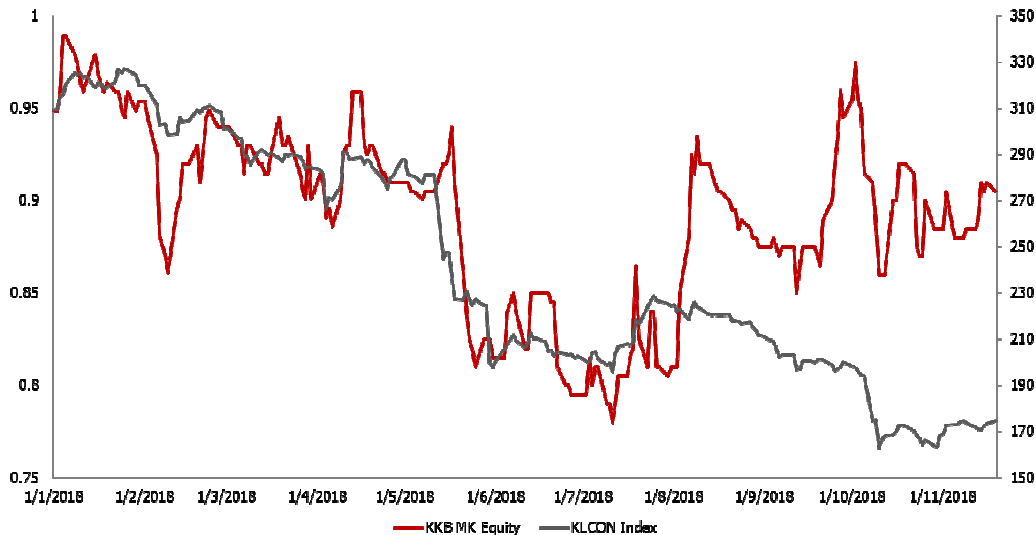
Recommendation. We have seen KKB's price revival sparked by succeeding progressive news flows i.e. the continuation of Pan Borneo Highway and the state's position over the long-drawn out plan of water grid system. On that water grid's note, local players with proven track record and competitive value chain are expected to benefit from the potential roll-out of work packages. In the near term, KKB is expected to bid further open tenders worth approximately RM350m. The total sum is primarily a combination of Oil & Gas, water projects, and pipe supplies. If these tenders are successful, KKB expects to be awarded with the new projects within 1QFY19 to 2QFY19. At this juncture, we believe the risk-reward return embedded in KKB's potential is attractive. Hence, we maintain our **BUY** call on the stock with unchanged **TP** of **RM1.13**. 

INVESTMENT STATISTICS

FYE Dec	FY2015	FY2016	FY2017	FY2018F	FY2019F
Revenue (RMm)	127.9	103.1	209.3	350.2	224.2
Pretax Profit (RMm)	37.6	(9.1)	6.4	17.5	10.0
Profit After Tax (RMm)	29.1	(5.7)	3.3	15.8	5.5
Profit After Tax and Non-controlling Interests (RMm)	26.0	(5.8)	1.6	14.0	3.0
PATANCI margin (%)	20.4	(5.6)	0.8	4.0	1.4
EPS (sen)	10.1	(2.2)	0.6	1.6	1.2
EPS Growth (%)	24.1	n.a.	n.a.	142.4	12.8
PER (x)	8.9	(40.1)	140.6	58.0	76.4
Net Dividend (sen)	4.0	0.0	2.0	2.0	2.0
Dividend yield (%)	4.4	0.0	2.2	2.2	2.2
ROA (%)	7.8	(1.7)	0.5	3.9	0.9
ROE (%)	8.6	(2.0)	0.6	4.7	1.1

Source: Bloomberg, MIDFR

KKB's Share Price vs KLCON Index



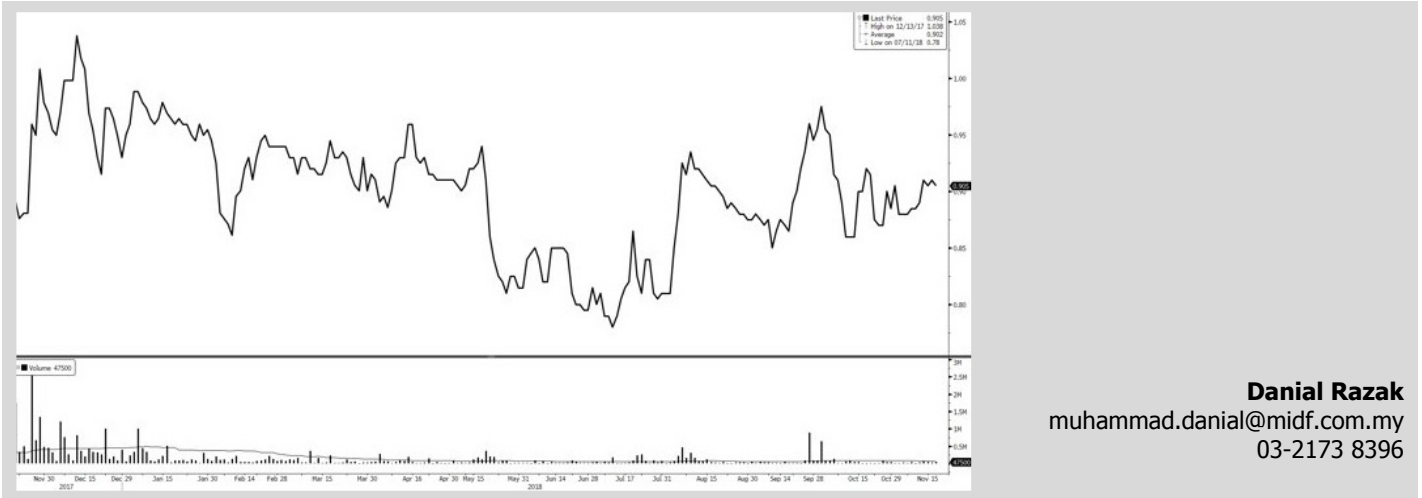
Source: Bloomberg, MIDFR

9MFY18 RESULTS SUMMARY

FYE Dec (RM'm)	Quarterly results					Cumulative results		
	3QFY18	3QFY17	2QFY18	YoY (%)	QoQ (%)	9MFY18	9MFY17	YoY (%)
Revenue	112.2	49.3	93.2	127.5%	20.4%	269.9	139.1	94.1%
Cost of sales	(95.2)	(41.3)	(84.7)	-130.2%	-12.4%	(239.4)	(138.5)	-72.9%
Gross profit	17.0	8.0	8.5	113.5%	99.4%	30.5	0.6	4988.0%
Other income	1.2	1.9	1.5	-34.6%	-17.2%	6.2	7.0	-12.0%
Distribution costs	(0.3)	(0.3)	(0.3)	-0.4%	-12.2%	(0.7)	(0.4)	-69.4%
Administrative expenses	(6.7)	(3.5)	(5.7)	-95.0%	-17.5%	(17.7)	(11.1)	-59.0%
Other expenses	(0.4)	(0.3)	(0.6)	-41.8%	30.5%	(1.4)	(0.8)	-64.4%
Finance costs	(0.1)	(0.1)	(0.1)	-84.5%	-40.9%	(0.3)	(0.5)	29.5%
Share of results of associates	0.0	1.1	0.0	-97.8%	235.6%	(0.2)	1.4	-114.2%
PBT	10.6	6.8	3.3	55.7%	223.0%	16.4	(3.9)	520.2%
Taxation	(2.1)	(1.6)	(0.7)	-26.9%	-194.6%	(3.8)	1.0	-483.0%
PAT	8.6	5.2	2.6	64.6%	230.7%	12.6	(2.9)	532.9%
Non-controlling interests	(1.7)	(0.2)	(0.8)	-579.3%	-97.7%	(2.5)	(0.8)	-213.4%
PATANCI	6.9	5.0	1.8	39.4%	293.9%	10.0	(3.7)	371.0%
Basic EPS (sen)	2.69	1.93	0.68	39.4%	295.6%	3.89	(1.44)	370.1%
				+ / (-) ppts				+ / (-) ppts
Gross profit (%)	15.1	16.1	9.1	(1.0)	6.0	11.3	0.4	10.9
PBT margin (%)	9.5	13.9	3.5	(4.4)	6.0	6.1	(2.8)	8.9
PAT margin (%)	7.7	10.6	2.8	(2.9)	4.9	4.7	(2.1)	6.7
PATANCI margin (%)	6.2	10.1	1.9	(3.9)	4.3	3.7	(2.7)	6.4
Tax rate (%)	19.3	23.7	21.2	(4.4)	(1.9)	23.3	25.5	(2.3)

Source: MIDFR, Bursa Malaysia

DAILY PRICE CHART



Source: Bloomberg

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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 <i>rise</i> 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 <i>fall</i> 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.