

28 August 2014 | 2Q14 Results Review

KNM Group Berhad

Continued improvements on all fronts

Maintain NEUTRAL

Unchanged Target Price (TP): RM1.15

INVESTMENT HIGHLIGHTS

- KNM Group's 2Q14 reported earnings more than doubled to RM25m compared with the same period a year ago
- Every operating geographic segment recorded positive earnings with Europe leading the group
- EBITDA margin for the quarter expanded +2pp to 12.2%
- Reiterate NEUTRAL with an unchanged TP of RM1.15

Substantial rise in earnings. KNM's 2Q14 earnings more than doubled to RM25.3m compared with the same period a year earlier. Excluding the deferred tax of RM4.98m accumulated in the first six months of this year, normalised earnings of RM30.2m came in within ours and consensus' expectations, accounting for 50% and 45% of full year's estimates respectively. EBITDA margin for 6M14 expanded by +4.2ppts to 12.6%. Normalised net margin for the quarter of 5.2% was the highest recorded for the past many years.

Asia and Oceanic. Segment revenue grew +14.8%yoy to RM134.7m while EBITDA grew at a faster pace of +75.4%yoy. Management guided that this was mainly attributable to the execution of projects with higher margins. Moving forward, management remains optimistic that the segment orderbook will continue to grow, especially with the newly secured sub-contracting works from Sinopec for the refinery plant at the Pengerang Integrated Complex.


Europe is still the key earnings driver. Contribution from Europe, primarily Borsig GmbH remains the key growth driver for the group as quarterly topline contribution expanded +13.6%yoy to RM340.7m. EBITDA followed suit, expanding by +19.4%yoy to RM40.2m. Management attributed the results to expanding orderbook while having a bullish outlook on securing more jobs in Europe. EBITDA margin grew marginally by +0.5ppts to 11.8%.

Americas. Despite segment revenue still lingering in the teens, EBITDA margin is a strong 23%, propelling earnings out of the reds to RM3.2m. Management is confident that contributions from this geographic segment will continue to improve.

RETURN STATS	
Price (27 August 2014)	RM1.00
Target Price	RM1.15
Expected Share Price Return	+15.0%
Expected Dividend Yield	0.0%
Expected Total Return	+15.0%*

**Maintain Neutral as total upside potential is at a borderline threshold*

STOCK INFO	
KLCI	1,872.38
Bursa / Bloomberg	7164/ KNMG MK
Board / Sector	Main/ Trading Services
Syariah Compliant	Yes
Issued shares (mil)	1,614.4
Par Value (RM)	0.50
Market cap. (RM'm)	1,614.4
Price over NA	0.60x
52-wk price Range	RM0.39 – RM1.10
Beta (against KLCI)	0.72
3-mth Avg Daily Vol	19.8m
3-mth Avg Daily Value	RM13.3m
Major Shareholders (%)	
Inter merger	16.19
Employees Provident Fund (via external fund managers)	6.35
Aveda Assets Capital	5.57

Maintain NEUTRAL. We are maintaining our **NEUTRAL** stance on KNM Group with an unchanged target price of **RM1.15** per share. This is based on an EPS15 of 7.2sen and PER15 of 16x. Our target PER of 16x is based on KNM's 10-year historical average PER and our house PER target for small-mid cap oil and gas service providers. We believe that the management of the company has achieved significant progress in orchestrating a turnaround for the company. In addition, we remain positive on the prospects of the Peterborough project and expect a financial close this year. Moving forward, we are optimistic that the SINOPEC-KNM partnership will be winning more Pengerang-related jobs. 

INVESTMENT STATISTICS

FYE Dec	FY11	FY12	FY13	FY14F	FY15F
Revenue (RM'm)	1,982.3	2,377.3	1,985.2	1,818.8	2,806.5
EBIT (RM'm)	-98.4	107.3	100.7	127.3	196.5
Pretax Profit (RM'm)	-147.5	21	45.8	75.1	144.2
Net Profit (RM'm)	-83.4	82	20.3	60.0	115.4
EPS (sen)	-5.2	7.9	1.6	3.8	7.2
EPS growth (%)	-1.7	251.5	-79.4	130.2	92.1
PER(x)	-19.2	12.7	61.3	26.6	13.9

Source: MIDFR Estimates

DAILY PRICE CHART

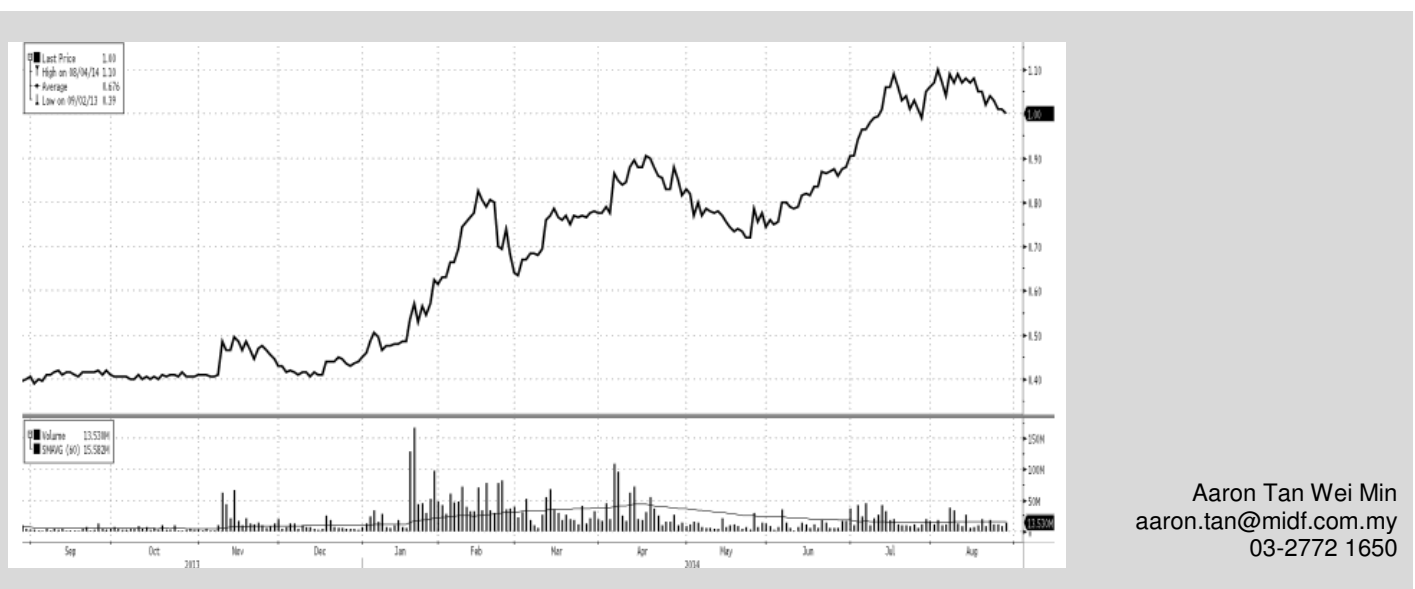
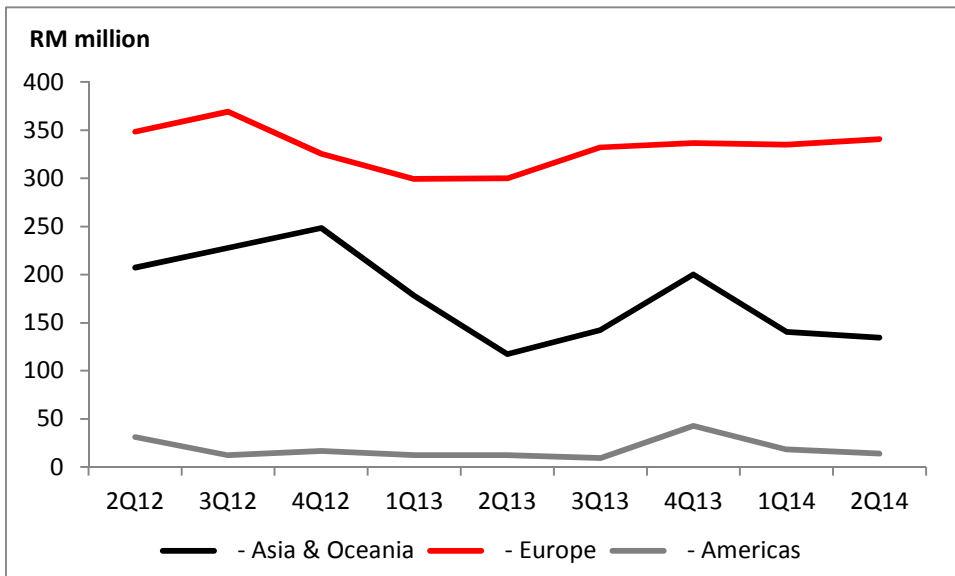


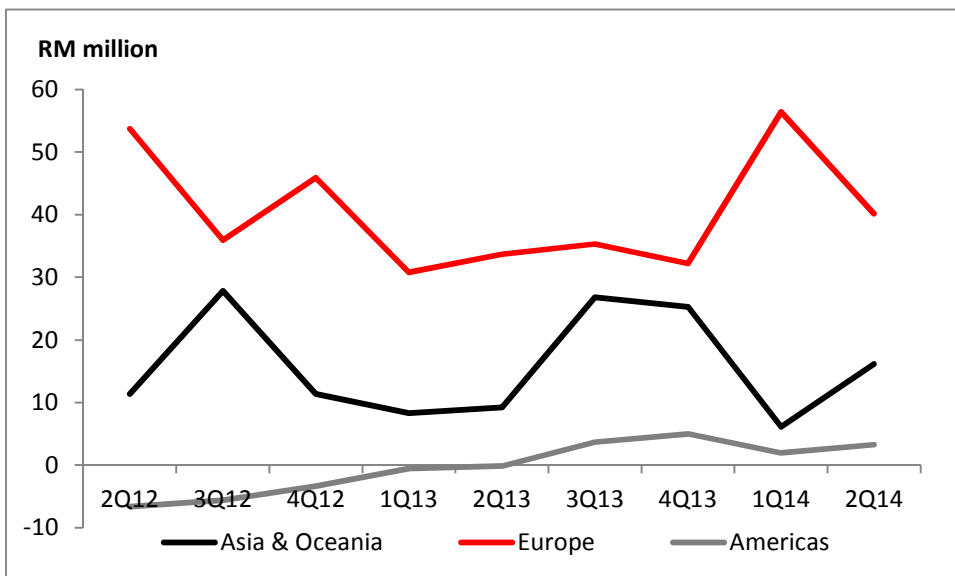
Figure 1: Revenue contributions by geographic segment



Source: Company, MIDFR

Europe is still a key earnings driver while Americas is stabilising

Figure 2: EBITDA contributions by geographic segment



Source: Company, MIDFR

Asia and Oceania has been improving since 1Q14 while the Americas has been successfully recording profits the past five quarters

KNM Group: 2QFY14 Results Summary

FYE Dec (RM m)	Quarterly Results			Cumulative			Comments
	2Q14	QoQ (%)	YoY (%)	6M13	6M14	YoY (%)	
Revenue	489.3	-0.9	13.9	923.7	983.2	6.4	
Operating Profit	33.9	-12.1	92.5	27.6	72.5	162.7	
Finance Costs	-14.4	-3.0	36.3	-21.5	-29.3	36.3	
Interest Income	0.7	2.1	-9.6	1.3	1.3	-2.2	
JCE	-0.4	-65.8	-59.9	-1.7	-1.5	-13.1	
PBT	19.8	-15.0	189.9	5.7	43.0	649.6	
Tax	-9.3	-2.9	-358.0	2.6	-19.0	nm	Tax rate higher than statutory rate due to deferred tax
PATAMI	25.3	78.5	121.5	9.6	25.3	163.0	
Normalised-PAT (minus deferred tax and tax incentives)	26.0	40.6	127.9	7.4	30.3	307.6	
<i>Revenue</i>							
- Asia & Oceania	134.7	-4.3	14.8	299.7	275.5	-8.1	
- Europe	340.7	1.7	13.6	599.4	675.7	12.7	
- Americas	13.9	-23.4	13.0	22.2	32.1	44.7	
Discontinued Ops	-	-	-	2.5	-	nm	
Total	489.3	-0.9	13.9	923.7	983.2	6.4	
<i>EBITDA</i>							
- Asia & Oceania	16.1	163.9	75.4	13.5	22.3	64.4	Projects with higher margins
- Europe	40.2	-28.8	19.4	64.4	96.6	49.9	
- Americas	3.2	68.3	nm	1.4	5.2	270.1	
Discontinued Ops	-	-	-	-2.1	-	nm	
Total	59.6	-7.6	39.4	77.3	124.1	60.5	

Source: MIDF, Company

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	<i>Negative</i> total return is expected, by -15% or more, over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% 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.