

21 November 2022

## KESM Industries

### Still Navigating Headwinds

By Samuel Tan | [samueltan@kenanga.com.my](mailto:samueltan@kenanga.com.my)

**KESM's 1QFY23 results missed expectations. It registered another quarterly loss as it scaled down its EMS business. Its burn-in and test segment saw lower demand, resulting in the overall utilisation rate falling below the optimal level. It will still incur overheads over the next 1-2 quarters while the workers are fully retrained and absorbed into the burn-in business. We cut FY23-24F net profit forecasts by 66-40% but only trim our asset-based TP by 1% to RM6.60 (from RM6.65). Maintain MARKET PERFORM.**

**Below expectations.** 1QFY23 net loss of RM1.5m (-153% YoY) missed both our and consensus full-year net profit estimates of RM3.5m and RM3.3m, respectively.

**Results' highlight. YoY,** 1QFY23 revenue fell 23.1% as the group continued to wind down the EMS business which the group has decided to discontinue owing to unfavourable margins on sustained elevated materials costs. In addition, the group's core business — automotive burn-in and testing — also saw lower loading volume. This resulted in the group reporting a net loss of RM1.5m for 1QFY23 due to underutilised capacity.

**Capacity realignment.** While the majority of the EMS business has fully scaled down in 1QFY22, it will still incur overheads over the next 1-2 quarters while the workers are fully retrained and absorbed into the burn-in business. Meanwhile, KESM is expecting the new investment for equipment will begin commissioning in 2QFY23 and gradually ramp up in 2HFY23.

**Forecasts.** Reduce FY23-24F CNP by 66-40%.

We like KESM for: (i) being a proxy to the promising prospects of automotive semiconductors, (ii) being one of the largest independent burn-in and test service provider in Malaysia to potentially benefit from MNCs expansions in the country, and (iii) its physical presence in China to ride on the government's ambitious plans for the semiconductor industry. However, we remain cautious in the immediate term as the group is still in the capacity restructuring phase with 1-2 more quarters of unabsorbed overheads.

**Maintain MARKET PERFORM with a lower TP of RM6.60** (previously RM6.65) based on 0.8x FY23F PBV. The 10% discount to its BV is to reflect potential losses that could erode its asset value. The average PBV of 2.8x of its peers may not serve as a good reference given that they are mostly highly profitable. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

**Risks to our call include:** (i) faster-than-expected ramp-up in volume for burn-in and test services, (ii) faster-than-expected adoption of new semiconductor modules in automobiles, and (iii) sudden surge in customer forecast.

## MARKET PERFORM ↔

Price: RM7.00

Target Price: RM6.60 ↓

Expected Capital Gain: -RM0.40 -5.7%  
Expected Divd. Yield: RM0.09 1.3%  
Expected Total Return: -RM0.31 -4.4%

KLCI Index 1,449.3

### Stock Information

Bloomberg Ticker	KESM MK Equity
Bursa Code	9334
Listing Market	Main Market
Shariah Compliant	Yes
Shares Outstanding	43.0
Market Cap (RM m)	301.1
52-week range (H)	14.60
52-week range (L)	6.10
Free Float	27.9%
Beta	0.70
3-mth avg daily vol:	7,882.5

### Major Shareholders

Sunright Ltd	48.4%
Tan Kong Hong Alex	4.8%
Abrdn Plc	3.7%

### Summary Earnings Table

FY July (RM m)	2022A	2023F	2024F
Revenue	246.7	239.0	256.4
EBIT	1.1	(1.0)	1.6
PBT	4.2	1.3	4.1
Net profit	0.2	1.2	3.7
<b>Core Net Profit</b>	<b>0.2</b>	<b>1.2</b>	<b>3.7</b>
Consensus (NP)	n.a.	3.3	7.8
Earnings Revision	n.a.	-66%	-40%
Core EPS (sen)	0.5	2.8	8.5
Core EPS growth (%)	-94.5	443.8	205.4
DPS (sen)	7.5	7.5	7.5
BV/Share (RM)	8.3	8.2	8.3
Core PER (x)	1366	251.2	82.2
PBV (x)	0.8	0.8	0.8
Net. Gearing (x)	-0.4	-0.4	-0.5
Div. Yield (%)	1.1	1.1	1.1

### Share Price Performance



	1 mth	3 mths	12 mths
Absolute (%)	4.6%	-4.1%	-43.1%
Relative (%)	-1.0%	-0.6%	-38.2%



21 November 2022

## Results Highlights

	1Q	4Q	QoQ	1Q	YoY	3M	3M	YoY
FYE July (RM m)	FY23	FY22	Chg	FY22	Chg	FY23	FY22	Chg
<b>Revenue</b>	<b>52.8</b>	<b>55.7</b>	<b>-5.2%</b>	<b>68.6</b>	<b>-23.1%</b>	<b>52.8</b>	<b>68.6</b>	<b>-23.1%</b>
EBITDA	8.3	8.8	-6.2%	23.3	-64.6%	8.3	23.3	-64.6%
EBIT	-1.4	-2.3	39.8%	8.8	-115.7%	-1.4	8.8	-115.7%
PBT	-1.7	-2.6	34.7%	8.7	-119.6%	-1.7	8.7	-119.6%
Taxation	0.2	0.1	68.1%	-1.1	113.5%	0.2	-1.1	113.5%
<b>Net Profit</b>	<b>-1.5</b>	<b>-2.5</b>	<b>38.5%</b>	<b>7.5</b>	<b>-120.5%</b>	<b>-1.5</b>	<b>7.5</b>	<b>-120.5%</b>
<b>Core Net Profit</b>	<b>-1.5</b>	<b>-2.5</b>	<b>38.5%</b>	<b>2.9</b>	<b>-152.7%</b>	<b>-1.5</b>	<b>2.9</b>	<b>-152.7%</b>
EPS (sen)	-3.6	-5.8	38.5%	6.8	-152.7%	-3.6	6.8	-152.7%
DPS (sen)	0.0	6.0		0.0		0.0	0.0	
EBITDA margin	15.6%	15.8%		34.0%		15.6%	34.0%	
EBIT margin	-2.6%	-4.1%		12.8%		-2.6%	12.8%	
PBT margin	-3.2%	-4.7%		12.6%		-3.2%	12.6%	
PATAMI margin	-2.9%	-4.5%		4.3%		-2.9%	4.3%	
Effective tax rate	-9.0%	-3.5%		-13.1%		-9.0%	-13.1%	

Source: Company, Kenanga Research

21 November 2022

### 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	OP	3.77	4.45	18.04%	4,664.4	Y	12/2022	11.3	14.4	27.1%	26.6%	33.2	26.3	5.2	16.3%	1.9	0.5%
GHL SYSTEMS BHD	MP	0.700	1.10	57.14%	793.3	Y	12/2022	2.1	2.7	-16.4%	30.2%	34.0	26.1	1.5	4.5%	0.0	0.0%
INARI AMERTRON BHD	MP	2.58	2.85	10.47%	9,630.6	Y	06/2023	10.2	11.5	-3.2%	12.7%	25.3	22.4	3.8	15.0%	9.7	3.8%
JHM CONSOLIDATION BHD	MP	0.74	0.90	21.62%	412.6	Y	12/2022	5.7	6.7	15.8%	17.7%	13.0	11.1	1.4	11.6%	0.5	0.7%
KELINGTON GROUP BHD	OP	1.30	1.80	38.46%	835.9	Y	12/2022	7.8	8.1	57.9%	4.0%	16.6	16.0	3.6	23.4%	2.0	1.4%
KESM INDUSTRIES BHD	MP	7.00	6.60	-5.71%	301.1	Y	07/2023	2.8	8.6	500.0%	208.3%	251.2	82.2	0.8	0.3%	7.5	1.1%
LGMS BHD	OP	1.20	1.50	25.00%	547.2	Y	12/2022	2.7	3.5	20.4%	29.0%	44.1	34.1	6.5	22.0%	0.0	0.0%
MALAYSIAN PACIFIC INDUSTRIES BHD	MP	26.10	34.50	32.18%	5,191.2	Y	06/2023	173.0	182.5	4.1%	5.5%	15.1	14.3	2.3	16.0%	35.0	1.3%
P.I.E. INDUSTRIAL BHD	OP	2.56	3.15	23.05%	983.1	Y	12/2022	16.6	19.7	6.0%	18.5%	15.4	13.0	1.7	11.6%	7.0	2.7%
SKP RESOURCES BHD	OP	1.62	2.10	29.63%	2,531.0	Y	03/2023	11.6	12.4	6.3%	7.7%	14.0	13.1	2.8	21.1%	5.8	3.6%
UNISEM (M) BHD	MP	2.61	2.75	5.36%	4,210.1	Y	12/2022	14.4	15.3	17.7%	6.2%	18.1	17.0	1.8	10.4%	6.0	2.3%
Simple Average								23.5	25.9	57.8%	33.3%	43.6	25.1	2.8	13.9%		1.6%

Source: Bloomberg, Kenanga Research

21 November 2022

**Stock ESG Ratings:**

	Criterion	Rating		
<b>GENERAL</b>	Earnings Sustainability & Quality	★	★	☆
	Corporate Social Responsibility	★	★	★
	Management/Workforce Diversity	★	★	☆
	Accessibility & Transparency	★	★	☆
	Corruption-Free Pledge	★	★	★
	Carbon-Neutral Initiatives	★	★	☆
<b>SPECIFIC</b>	Foreign Worker Welfare	★	★	★
	Supply Chain Auditing	★	★	★
	Waste disposal / pollution control	★	★	☆
	Energy Efficiency	★	★	★
	Work Site Safety	★	★	★
	Digital Transformation	★	★	☆
<b>OVERALL</b>		★	★	★

☆ 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.**

This report has been prepared by Kenanga Investment Bank Berhad pursuant to the Mid and Small Cap Research Scheme ("MidS") administered by Bursa Malaysia Berhad. This report has been produced independent of any influence from Bursa Malaysia Berhad or the subject company. Bursa Malaysia Berhad and its group of companies disclaim any and all liability, howsoever arising, out of or in relation to the administration of MidS and/or this report.

This document has been prepared for general circulation based on information obtained from sources believed to be reliable but we do not make any representations as to its accuracy or completeness. Any recommendation contained in this document does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may read this document. This document is for the information of addressees only and is not to be taken in substitution for the exercise of judgement by addressees. Kenanga Investment Bank Berhad accepts no liability whatsoever for any direct or consequential loss arising from any use of this document or any solicitations of an offer to buy or sell any securities. Kenanga Investment Bank Berhad and its associates, their directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein from time to time in the open market or otherwise, and may receive brokerage fees or act as principal or agent in dealings with respect to these companies.

Published by:

**KENANGA INVESTMENT BANK BERHAD (15678-H)**

Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia  
Telephone: (603) 2172 0880 Website: [www.kenanga.com.my](http://www.kenanga.com.my) E-mail: [research@kenanga.com.my](mailto:research@kenanga.com.my)

This report is accessible at [www.bursamids.com](http://www.bursamids.com) too.