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4QCY23 Report Card: Seasonality and Cyclical Uptick

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The sector's earnings delivery (against our expectations) improved in the recently concluded 4QCY23 reporting season sequentially on the back of a combination of seasonality and potentially the start of a cyclical upturn. D&O (MP; TP: RM3.60) reported its highest quarterly revenue and a 33% QoQ jump in net profit driven by restocking by its Chinese clients. PIE (OP; TP: RM4.00) reported improved orders across the board while KGB (OP; TP: RM3.40) delivered another record-breaking number on robust project deliveries and improved margins. Keeping in mind seasonality in 4QFY23 numbers, we advocate investors to cherry-pick proven names such as: (i) KGB for its strong earnings visibility backed by a RM1.3b order book, (ii) INARI (OP; TP: RM4.05) on its growing its exposure to China smartphone and AI-fuelled data centre boom, and (iii) PIE for its strong earnings growth trajectory that is driven by a wide range of customers.

The sector's earnings delivery (against our expectations) improved in the recently-concluded 4QCY23 reporting season sequentially with 23%, 62%, and 15% of companies under our coverage coming in above, within and below our forecasts, vs. 15%, 38%, and 47% during the last quarter (see Exhibit 1), respectively. We believe the improvement could be attributed to a combination of seasonality and potentially the start of a cyclical upturn.

D&O finally turned the corner in 4QCY23, having missed its guidance for the past few quarters. D&O reported its highest quarterly revenue of RM310m in 4QCY23, with a 33% QoQ jump in net profit to RM24.3m due to higher restocking orders for its automotive LEDs from customers, particularly from China, which accounts for approximately 50% of the group's revenue. This was in line with reports from the China Association of Automobile Manufacturers (CAAM), indicating significant increases of 11.4%, 25.3%, and 23.3% in passenger car sales in the last three months of 2023.

PIE saw strong order volumes across its customers in the EMS segment, coupled with write-back of provisions for slow-moving goods throughout the year and a lower tax rate resulting from received reinvestment allowances. Another positive surprise came from **KGB** underpinned by robust project deliveries across all operating markets, while margins improved due to a favorable revenue mix.

Worst is likely over but recovery will be gradual. 'The worst is over' outlook as guided by corporates has gained more credibility this time, supported by the improved QoQ performance in 4QCY23. However, it should be noted that the bumper 4QCY23 is typically followed by a seasonal low cycle in 1QCY24 owing to the Chinese New Year break where companies have scheduled plant shutdown. With that said, a handful of companies are guiding that the seasonal lull in 1QCY24 may not necessarily be a drastic decline from 4QCY23. This is echoed by the likes of D&O which is expecting a mild QoQ dip, cushioned by on-going restocking activities. As such, the group is strengthening its regional sales teams by focusing on more design-in projects for which there is a growing market in India. Meanwhile, **UNISEM (MP; TP: RM2.95**) guided for a flattish QoQ performance, albeit from a low base. It is poised to initiate qualification for new products from new IDM customers, particularly in the areas of NAND flash, radio frequency switches, and MEMS microphones for US smartphones. Qualification is set to commence in 1HCY24, with pilot runs scheduled for 2HCY24, in line with the anticipation of more meaningful recovery for the group.

Maintain NEUTRAL. We found it hard to distinguish between seasonality and potential start of a cyclical upturn in 4QFY23 numbers: hence, we maintain our **NEUTRAL** stance. We encourage investors to focus on names that offer certainty in earnings, pending confirmation that the sector as a whole has turned the corner. We maintain high conviction on **KGB** owing to its ability to delivery resilient earnings thanks to: (i) it being a direct proxy to the front-end wafer fab expansion, (ii) its strong earnings visibility underpinned by its robust RM1.3b order book, and (iii) its strong foothold in multiple markets, i.e. Malaysia, Singapore and China. Additionally, we like **INARI** as it has indicated a very strong ramp-up of its RF business, ability to turn positive quicker than its peers and still being able to retain its lucrative profit margins amidst the rising operating cost environment. We also like **PIE** for: (i) its comprehensive skillset, making it a top-choice EMS provider for MNCs, (ii) various competitive advantages it enjoys as a unit of Foxconn, and (iii) its diversified and evolving client base, from those involved in communication devices and power tools to the latest DeFi equipment.

Quarterly Results Overview

	4QCY23						3QCY23					
	KENANGA			CONSENSUS			KENANGA			CONSENSUS		
	Above	Within	Below	Above	Within	Below	Above	Within	Below	Above	Within	Below
D&O		1				1			1			1
GHLSYS		1			1				1			1
INARI		1			1			1			1	
JHM		1				1			1			1
KGB	1			1			1			1		
KESM		1			1				1			1
LGMS	1			1				1			1	
MPI			1			1	1					1
NATGATE			1			1		1			1	
OPPSTAR		1			1			1			1	
PIE	1			1					1			1
SKP		1			1			1			1	
UNISEM		1			1				1			1
Total	**3**	**8**	**2**	**3**	**6**	**4**	**2**	**5**	**6**	**1**	**5**	**7**
Total (%)	**23**	**62**	**15**	**23**	**46**	**28**	**15**	**38**	**47**	**8**	**38**	**54**

Source: Kenanga Research

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	MP	3.06	3.60	17.6%	3,813.9	Y	12/2024	8.5	12.0	133.7%	41.6%	36.2	25.5	3.8	10.8%	1.4	0.5%
GHL SYSTEMS BHD	OP	0.635	0.880	38.6%	690.6	Y	12/2024	2.4	2.8	-3.5%	15.8%	26.6	23.0	1.3	5.2%	0.0	0.0%
INARI AMERTRON BHD	OP	3.14	4.05	29.0%	11,638.3	Y	06/2024	9.9	12.1	14.0%	22.1%	31.8	26.0	4.5	14.1%	9.3	3.0%
JHM CONSOLIDATION BHD	MP	0.600	0.700	16.7%	363.6	Y	12/2024	4.7	5.2	94.5%	11.0%	12.9	11.6	1.1	8.5%	0.5	0.8%
KELINGTON GROUP BHD	OP	2.56	3.40	32.8%	1,659.9	Y	12/2024	16.1	19.4	1.0%	20.5%	15.9	13.2	4.0	27.7%	4.5	1.8%
KESM INDUSTRIES BHD	MP	6.40	7.06	10.3%	275.3	Y	07/2024	6.3	10.2	-44.9%	63.0%	103.5	61.9	0.8	0.8%	0.0	0.0%
LGMS BHD	OP	1.00	1.16	16.0%	437.8	Y	12/2024	4.6	5.6	88.4%	21.8%	21.6	17.7	4.4	22.2%	0.9	0.9%
M'SIAN PACIFIC INDUSTRIES BHD	MP	29.70	24.30	-18.2%	5,729.2	Y	06/2024	59.6	118.3	93.5%	98.3%	49.8	25.1	2.9	5.8%	35.0	1.2%
NATIONGATE HOLDINGS BHD	OP	1.31	1.58	20.6%	2,779.1	Y	12/2024	6.3	6.9	114.8%	9.6%	20.8	19.0	5.1	27.4%	1.0	0.8%
OPPSTAR BHD	OP	1.15	1.72	49.6%	742.3	Y	03/2024	3.4	5.7	3.3%	66.7%	33.4	20.0	4.8	15.1%	0.9	0.8%
P.I.E. INDUSTRIAL BHD	OP	3.34	4.00	19.8%	1,263.5	Y	12/2024	22.2	26.1	15.7%	17.4%	15.0	12.8	1.9	13.4%	7.0	2.1%
SKP RESOURCES BHD	MP	0.815	0.850	4.3%	1,257.7	Y	03/2024	5.7	6.4	-38.4%	13.1%	14.3	12.7	1.5	10.3%	2.8	3.4%
UNISEM (M) BHD	MP	3.50	2.95	-15.7%	5,516.7	Y	12/2024	10.2	12.7	100.1%	24.9%	34.4	27.6	2.3	6.8%	6.0	1.7%
Simple Average										31.4%	29.3%	28.6	22.1	2.9	12.9%		1.3%

Source: Kenanga Research

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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.***

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