

2QFY11 RESULTS UPDATE

18 August 2011

# K-One Technology Berhad

Price : RM0.325

Market Capitalization : RM111.1 mln

Market : ACE Market

Sector : Technology

Recommendation : Buy

Bursa / Bloomberg Code: 0111 / KONE MK  
Shariah-Compliant Stock

## K1: 2QFY11 results

FYE Dec RM mln	Quarter-on-Quarter			Year-on-Year		Year to date		
	Jun 11	Mar 11	% chg	Jun 10	% chg	1HFY11	1HFY10	% chg
Turnover	34.1	31.2	9.1%	33.8	0.8%	65.3	58.1	12.2%
Operating profit	2.5	2.4	3.8%	2.5	2.9%	5.0	4.3	14.3%
Interest cost	(0.3)	(0.4)		(0.3)		(0.7)	(0.6)	
Pre-tax profit	2.2	2.1	5.6%	2.2	1.8%	4.3	3.7	14.1%
Tax	(0.0)	(0.0)		0.0		(0.0)	-	
Net profit	2.2	2.1	5.9%	2.2	0.8%	4.2	3.7	13.2%
Reported EPS (sen)	0.6	1.0		2.0		1.5	3.4	
Op profit margin	7.4%	7.8%		7.3%		7.6%	7.3%	
Pre-tax margin	6.4%	6.7%		6.4%		6.5%	6.4%	
Net profit margin	6.4%	6.6%		6.4%		6.5%	6.4%	
NA per share (RM)	0.18							

## 2QFY11 Results Review

- K-One Technology Bhd (K1)'s 2QFY11 net profit increased 5.9% q-o-q and 0.8% y-o-y to RM2.2 mln, bringing 1HFY11 net profit to RM4.2 mln. Following a lengthy discussion with the management, we deem the results to be in line with our expectations although 1HFY11 net profit constitutes only 30% of our full year projection, as we expect a much more robust 2HFY11 performance to make up the slack.
- 1HFY11 revenue and net profit were 12.2% and 13.2% higher y-o-y at RM65.3 mln and RM4.2 mln respectively, on increased contributions from the mass production of new network cameras and electronic sports headlamps, as well as sales from the household appliances and hygiene-care categories.
- From our conversation with the management, it is noteworthy to mention that the Group recorded higher sequential revenue and net profit in 2QFY11 despite reduced contribution from sales of its USB cables during the quarter under review. To recap, K1's USB cables are bundled together with Sony Ericsson's new mobile phones, and the earthquake in Japan in March 2011 disrupted the production of certain components found in the Sony Ericsson mobile phones, resulting in much lower sales in 2QFY11. This in turn, affected K1's sale of USB cables to Sony Ericsson. Fortunately, rising contributions other products as well as additional revenue streams from new clients had more than offset the decline in USB cable sales.
- Despite the challenging operating environment, it is commendable that K1 managed to grow its business while sustaining its profit margins. 1HFY11 net margin of 6.5% was comparable to the 6.4% achieved in 1HFY10.
- On balance sheet strength, the Group's NTA/share stood at 18 sen with a manageable net gearing of 0.5x as at end-June 2011.

- Looking ahead, K1's prospects in the 2HFY11 appear to be positive, notwithstanding the expected slower world economic growth brought upon by the downgrade in the US credit rating and the Euro debt crisis. Our optimism is premised upon several factors, that are i) normalization of sales of USB cables since 3QFY11; ii) absence of signs of demand slowdown for K1's products based on rolling 12-month production forecast provided by its major customers; iii) rollout of new products in the mobile phone accessories category in 3QFY11; iv) rollout of new models for its network cameras and sports headlamps; and v) growing contribution from its household appliances and hygiene-care clients.
- On its geographical exposure to Europe, which contributed 58% to Group revenue in 1HFY11, management clarified that the classification is based on the location of its client's headquarter. In actual fact, K1's products are eventually sold across the globe, and often, in the Asian countries where domestic consumption growth is higher than the Western counterparts. As such, it does not expect slowdown in its business activities at this juncture.
- K1 does get affected by the appreciating Ringgit as all its overseas sales (86% of revenue as of 1HFY11) are transacted in the USD. In order to minimize currency risk, K1 adopts natural hedge whereby it pays its suppliers in USD instead of Ringgit.
- With our expectation of a strong rebound in 2HFY11 performance, we leave our existing FY11 net profit estimate of RM14.2 mln unchanged at this juncture. We shall revisit our projections upon the release of 3QFY11 results in November 2011.

## Recent Developments

- K1 (through its investment banker, AmlInvestment Band Bhd) announced on 2 August 2011 that Securities Commission (SC) had rejected its proposed transfer to the Main Market in view of the non-compliance to paragraph 1.06(a) (General Principles) of the SC's Equity Guidelines.
- Despite the rejection, we do not expect any impact to our valuation arising from this development as the fundamentals of the company are strong and its business growth remain intact moving forward.

## Recommendation

We maintain our **Buy** recommendation at this juncture but lower our fair value to **46 sen** from 50 sen. We derive our fair value from pegging a PER of 11x (from 12x) against FY11 EPS of 4.2 sen. The lower PER multiple reflects the reduced average PER of selected global peers in the electronics manufacturing industry following the recent sell-down in the equity market. Meanwhile, we view the recent decline in K1's share price from 45 sen in early July 2011 to the current level as reflective of the weak investor sentiment in the broader equity market, as fundamentals of the company remain healthy and prospects remain bright.

## Per Share Data

FYE Dec	FY09	FY10	FY11f
Book Value (sen)	14.0	16.4	20.3
Cash Flow (sen)	1.0	2.7	5.6
Earnings (sen)	0.3	2.3	4.2
Net Dividend (sen)	-	-	1.0
Payout Ratio (%)	-	-	24.1
PER (x)	108.3	14.1	7.8
P/Cash Flow (x)	32.9	12.1	5.8
P/Book Value (x)	2.3	2.0	1.6
Dividend Yield (%)	-	-	3.1%
ROE (%)	2.1%	14.0%	20.5%
Net Gearing (x)	0.4	0.3	0.5

Note: FY09 & FY10 figures adjusted retrospectively to reflect a 2-for-1 bonus issue effective in Feb 2011.

## P&amp;L Summary

FYE Dec (RM m ln)	FY09	FY10	FY11f
Revenue	84.1	132.8	177.7
Operating profit	2.1	9.2	15.1
Net Int Exp	(1.1)	(1.2)	(1.4)
Pre-tax Profit	1.1	8.0	14.7
Eff. Tax Rate	nm	1.6%	3.0%
Net Profit	1.1	7.9	14.2
Op Profit Margin (%)	2.5%	6.9%	8.5%
Pre-tax Margin (%)	1.3%	6.0%	8.2%
Net Margin (%)	1.3%	5.9%	8.0%

## K1's last 12-month share price chart



source: Bloomberg

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**RATING GUIDE**

BUY	Price appreciation expected to exceed 10% within the next 12 months
SELL	Price depreciation expected to exceed 10% within the next 12 months
HOLD	Price movement expected to be between -10% and +10% over the next 12 months from current level

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