KNM: PN17 status not a cause for concern

Once touted as the darling of investors, KNM Group Bhd finds itself in the league of distressed companies after it slipped into the Practice Note 17(PN17) category.

Its shares plunged to five sen each, current liabilities have exceeded current assets and the group foresees itself returning to profitability only in the next "two to three years".

Cash crunch issues are also limiting KNM from taking on more new projects.

The root cause of the quagmire plaguing KNM could be traced back to the series of acquisitions the group made many years ago.

The acquisitions, despite injecting good assets into KNM, had over-leveraged the group and by the time the Covid-19 pandemic hit, KNM’s cash generation was no longer able of meeting the high debt levels.

The current line-up of board members, who are onboard since the second half of last year, recognise the urgent need to de-leverage KNM.

This includes the single largest shareholder, Datuk Tunku Yaacob Khyra, who controls a 9.4% stake in KNM.

They have been working on removing highly-leveraged assets from the group’s books.

KNM is expected to be a cash-rich company with a healthier balance sheet by the end of next year.

Executive chairman Tan Sri Zulhasnan Rafique says KNM would not have slipped into PN17 had the proposed disposal of its entire stake in Borsig GmbH, a German-based process equipment manufacturer, was completed before the deadline of KNM’s financial audit.

“We only secured the shareholders’ approval in September (to sell Borsig). It will take a few months to complete the disposal.

“If the disposal had been completed before end-October, we would have settled the amount owed on the bond we defaulted earlier.

“This triggered the PN17 criteria,” the former Federal Territories Minister tells StarBizWeek.

It is noteworthy that KNM had, in Nov 2021, missed principal and coupon payments on bonds issued in Thailand worth 2.78 billion baht (RM356.8mil).

The bonds are guaranteed by Credit Guarantee and Investment Facility (CGIF), a trust fund managed by the Asian Development Bank.

CGIF has paid the bondholders on behalf of KNM.

“CGIF has been quite patient with us and they have been working with KNM to make sure that the sale of Borsig will go through and from it (the disposal), it will get paid,” he says.

Zulhasnan points out that the disposal of Borsig will “definitely” be completed by next month and that investors should not be worried about the PN17 status.

KNM bought Borsig for $350mil (RM1.65bil) in 2008. It will be selling the subsidiary for $220.8mil (RM1.04bil).

Zulhasnan says KNM will still record a gain from the disposal of Borsig, considering the cashflow of $212.8mil (RM1bil) it has received from the subsidiary over the years.

According to Zulhasnan, about 90% of the ‘clean-up works’ at KNM would be completed, post-Borsig disposal.

In addition to the sale of Borsig, KNM is also looking at selling its waste-to-energy power plant project in Peterborough, the United Kingdom as well as an ethanol plant in Thailand.

“For the Peterborough plant, which is yet to be built but we have the land and all the approvals, we are negotiating with the potential buyer.

“We hope to sell it by the end of next year.”

“As for the Thai plant, it should also be completed by end-2023,” he says.

With the sale of the Peterborough, Zulhasnan noted that KNM will be a cash-rich entity, with about RM200mil borrowings.

“And with the listing of FBM Hudson Italiana SpA, we will no longer have any borrowing.”

“We will then have an optimal capital base that will allow us to take on more projects in the future,” Zulhasnan points out.

KNM plans to list FBM Hudson Italiana SpA and its wholly owned subsidiary, FBM-KNM FZCO, next year on the Catalist Board of the Singapore Stock Exchange.

“The indicative market capitalisation of the listed entity would be around US$100mil (RM461mil), and KNM will have about 25% stake in it,” he says.

Moving forward, the Italy-based FBM Hudson would be a major driver for KNM, according to Zulhasnan.

“Before this, FBM Hudson was not able to bid for some projects because our Borsig was also competing for similar projects.”

“With the disposal of Borsig, FBM Hudson would be able to tender for more projects of a bigger scale,” he adds.

It is worth noting KNM had, on Aug 30, proposed to change its name to Hudson Group Bhd to reflect its future direction.

KNM is also banking on one of FBM Hudson’s main products, namely the heat exchangers, as an important engine of growth for the group.

Heat exchangers are used in industrial gas separation processes, typically for oil and gas (O&G) and petrochemical industries.

“Heat exchangers can also be used for removal of carbon dioxide.”

“As countries are racing towards reducing carbon footprint, there will a stronger demand for KNM’s heat exchangers in the future.”

“Our heat exchangers can be custom-made based on the requirements of our clients or industries.”

“This is actually a natural progression for KNM,” Zulhasnan says.

However, Zulhasnan clarifies that KNM is not interested in venturing into renewable energy (RE) businesses, although it welcomes opportunities to supply equipment to industry players involved in RE.

“The decision (by previous management) to go into renewables namely Peterborough (power station) and ethanol (Thai plant) was a distraction they did not need to do.”

“It is actually not attractive to go into RE. Socially, it sounds good, but from a financial point of view, a 10% internal rate of return (IRR) as delivered by many RE businesses is not exciting.”

“I would rather put the money in the engineering side, where we can have 15% to 25% IRR. We would like to stick to our core business,” he says.

Zulhasnan says KNM has managed to remain resilient, despite the cashflow issues and the PN17 status.

“It is business as usual at our subsidiaries. We are also getting new contracts and queries from prospective customers.”
“In fact, in September 2022, Petronas Gas Bhd awarded us an engineering, procurement, construction and commissioning contract worth RM25.69mil.”

“If our business is indeed falling apart, customers would not even consider us in the first place,” he says.

At the same time, KNM plans to strengthen its presence in its existing markets, especially in Malaysia and the Middle East.

This would potentially include a relocation of operations.

“KNM is very famous in Malaysia as one of the best engineering companies in the country. It is time we get it back to where it was before,” he adds.

The Star, 12 Nov 2022
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