

Chelsea Chew

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Recommendation:	Subscribe
IPO Price:	RM 0.30
Previous Target Price:	-
Target Price:	RM 0.54
Upside/Downside:	80.0%

Company Brief

Engaged in 2D animation production services.

Stock Information

Board	ACE Market
Sector	Teleco & Media
Bursa / Bloomberg Code	0315 / KUCINGKO MK
Syariah Compliant	No
Shares issued (m)	100.0
Market Cap (RM' m)	150.0
Free float (%)	40.0

Top 3 Shareholders (%)

Cat Ching	34.6
Netval Ventures	25.4
See Chin Joo	0.1

IPO Timetable Date

Opening of IPO application	28/6/2024
Closing of IPO application	12/7/2024
Balloting of IPO application	16/7/2024
Allotment of IPO shares	23/7/2024
Listing of IPO on Bursa Malaysia	26/7/2024

Kucingko Berhad

Imagination Adventure Unleashed

Summary

- Engages in 2D animation production services using digital drawn 2D images and create animated visual content, primarily for animated series, by simulating movement.
- Core earnings are anticipated to improve from growth in 2D animation production services segment, equipped with strong market presence in the foreign market and we foresee rising demand for 2D animation services from digital content distribution expansion.
- Kucingko is valued by pegging its FY25F core EPS of 1.9 sen to PE multiple of 28.0x, leading to a FV of RM0.54 (80.0% potential upside from IPO price).

Company Background

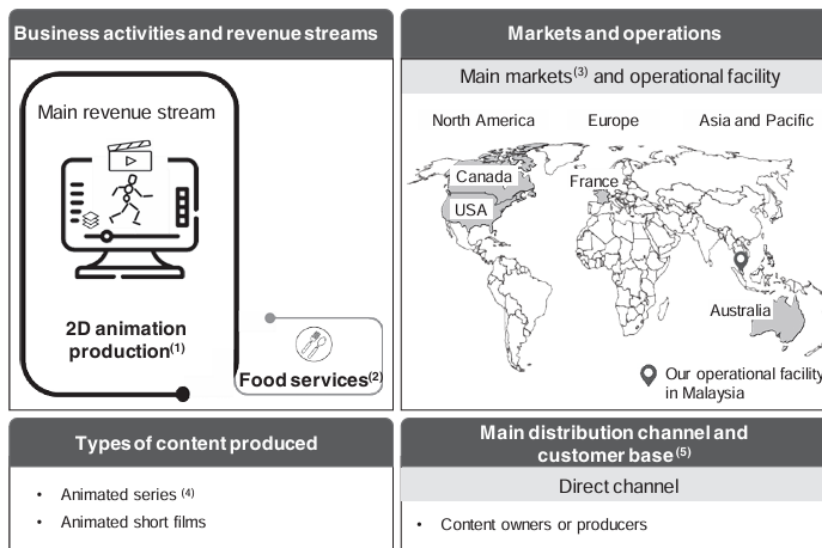
- Kucingko Berhad's (Kucingko) history traces back to 2002 which is known as Inspidea. In 2005, Netval Ventures, a registered venture capital corporation under the Securities Commission, became Inspidea's shareholder by subscribing to 10,000 convertible preference shares. Netval Ventures is sleeping investor for Inspidea and does not participate in our day-to-day operations.
- In 2007, Inspidea shifted its focus from creation of proprietary content to provision of 2D animation production services. On 9 of May 2024, Inspidea became a wholly-owned subsidiary of Kucingko.
- The Group's primary business revolves around 2D animation production services, managed by Inspidea. A smaller part of the business operations involves food services, handled by one of the subsidiaries; Bowleh. Kucingko's 2D animation production services predominantly use digitally drawn images to create movement and visual content for animated series.
- Under the financial years reviewed up to LPD (FY20 to LPD), Kucingko has completed 63 animation production projects, with a total of RM75.6m in contract value and approximately 5,015 minutes of runtime.

IPO Utilisation

Details of utilisation	Estimated time frame for utilisation	
		RM'm (%)
Capacity Expansion	Within 36 months	17.8 (59.2%)
USA sales office	Within 36 months	4.4 (14.6%)
Working capital	Within 12 months	18.8 (16.4%)
Listing expenses	Immediate	3.0 (2.6%)
Total		43.9 (100.0%)

Source: Kucingko, prospectus

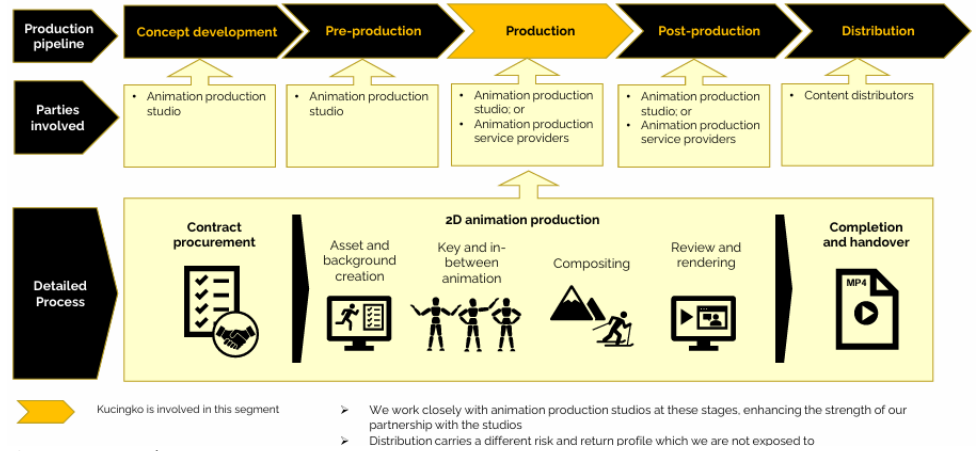
Business Overview



Source: Kucingko, prospectus

- Kucingko principally engage in 2D animation production services, which is undertaken by one of the subsidiaries, Inspidea. The Group utilise digital drawn 2D images to generate an illusion of movement to form the animated visual content mainly for animated series.
- In FY23, the 2D animation production service segment made up to RM28.1m or 99.8% of total revenue, while food services accounted for 0.2% of the total revenue at RM 0.1m.
- The process of creating animated content generally involves three main phases: pre-production, production, and post-production. Kucingko’s 2D animation production service specifically concentrates on the production phase. Here, the Group create 2D animations using pre-production materials provided by clients. These animations are primarily designed for television broadcasting and digital online streaming, reaching a global audience.
- In addition, Kucingko also contributes a small proportion of its revenue through food services. This includes operating a restaurant near their office, managed by their subsidiary, Bowleh. For each of the financial years under review, food services accounted for less than 1.0% of the total revenue.
- Geographically, the Group primarily serves foreign markets in North America, Asia Pacific, and Europe. Revenue from the aforementioned regions accounted for almost all of Kucingko's total revenue in FY20 till FY23, generated exclusively from 2D animation production services. A small portion of revenue derived from Malaysia, specifically from the Group's food services segment. North America, comprising the USA, Canada, and Mexico, represented the largest market share, followed by Europe (Netherlands, France, United Kingdom) and Asia Pacific (Australia, Malaysia, Japan, Hong Kong, Singapore). Operational wise, Kucingko conducts all 2D animation production digitally from Malaysia, facilitating towards global project execution.

2D animation production services



Source: Kucingko, prospectus

- The 2D animation production process revolves around three main phases. Kucingko's role in this segment is solely production. As content owner or producer, Kucingko would require to provide the pre-production package to production houses. Once delivered, production then commence. Completed animations are then handed back to the content owner or producer for post-production tasks such as reviewing, editing, sound design, music composition, colour grading, and final rendering. The Group does not handle post-production due to its focus is on 2D animation production, while post-production requires distinct skill sets.
- The Group 2D animation production uses digitally drawn 2D still images of characters, backgrounds and other elements and compiled into a suitable format to form the visual content and to create the illusion of motion.

Digital 2D animation frame



Source: Kucingko, prospectus

- The Group's 2D animation projects rely on customer-provided pre-production packages, including storyboards, scripts, colour keys, character, and background designs. Although primary focus is production, The Group may provide value added services such as aid in storyboarding to streamline processes. When included, storyboarding is outlined in contract's scope, associated costs are integrated into fixed lump sum contracts. These packages guide animation process, providing detailed plans, sketches, and designs essential for meeting the visual and technical requirements of the content owner or producer.

Completed 2D animation production projects

Mao Mao Heroes of Pure Heart



Source: Cartoon network

Monster Beach



Source: Cartoon network

Lamput 3



Source: Cartoon network

The Harper House



Source: Cartoon network

Food Services



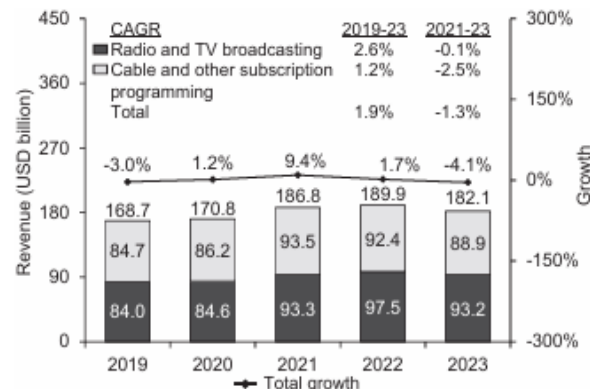
Source: Kucingko, prospectus

- The Group also operates a restaurant near their head office at Glomac Square, Petaling Jaya, offering a variety of Western and Asian cuisines including roasts, grills, pasta, poke bowls, and beverages. Employees receive a 20% staff discount. The restaurant caters to dine-in, takeaway, and food delivery customers, primarily ensuring food availability for staff. Revenue from the Group's food services outlet accounted for 0.3% (RM0.04m), 0.5% (RM0.1m), 0.4% (RM0.1m), and 0.2% (RM0.1m) of total revenue for FY20 to FY23, respectively.

Industry Overview

- The broadcasting industry in the US, excluding internet, is expanding as a major content distribution hub. The distribution of 2D animation content has evolved significantly, driven initially by TV and cinema, and now flourishing on digital platforms like Netflix, Amazon Prime Video, Disney+, YouTube, Vimeo, and social media platforms. This shift has broadened global access to 2D animation, catering to changing consumer preferences.
- In 2023, US broadcasting revenue declined 4.1% yoy to US\$182.1m, due to the rise of online streaming services and disruptions in scripted content production for cable TV. The shift in consumer behaviour towards online streaming and downloads has shaped content demand, presenting growth opportunities for providers of 2D animation services targeting the US market.

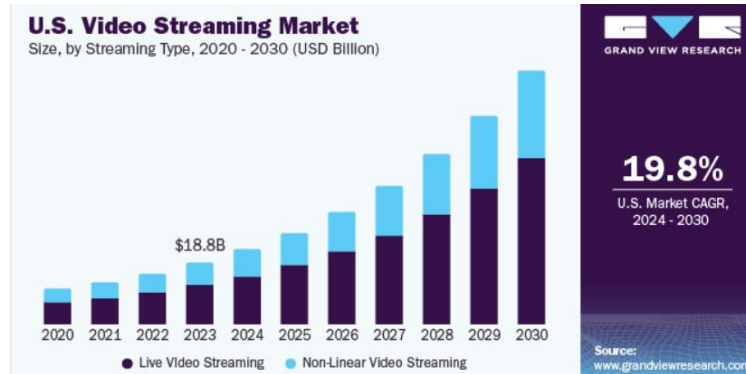
Broadcasting Revenue (except internet) Industry in the US



Source: US Census Bureau

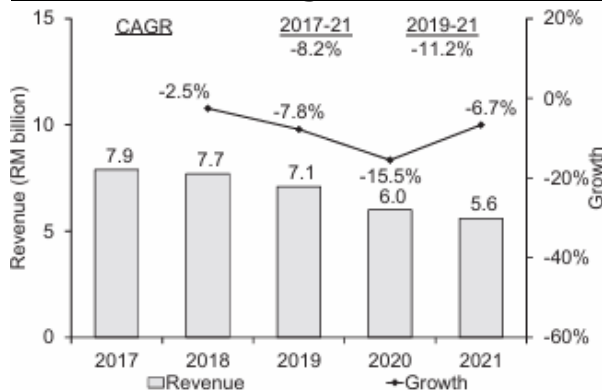
- We gathered that the US video streaming market was valued at US\$18.79bn in 2023 and is forecasted to grow at a six-year CAGR of 19.8% from 2024E to 2030F. Growth is anticipated to be driven by factors such as increased internet penetration, evolving consumer preferences, and the rollout of 5G technology, which enhances speed and performance. Adoption of major streaming platforms such as Netflix, Hulu, Disney+, and expanding, potentially surpassing traditional TV services.
- High-definition content and digital sports are key drivers of this expansion, alongside rising data consumption per smartphone. In 2023 December, Netflix, with 260.3m global paid memberships is heavily investing in the US market, supported by 80.1m subscribers in the US and Canada alone.

Animation market size 2023 to 2033 (USD' bn)



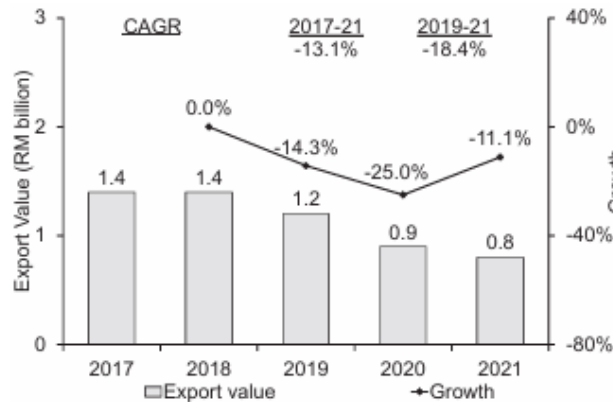
- Meanwhile, 2D animation production is part of the digital creative content industry, involving content development, production, and distribution technologies in Malaysia. From 2019 to 2021, Malaysia’s digital creative content industry saw annual decline of 11.2% in revenue and 18.4% in export value. But by mid-2022, the industry revenue reached RM2.80bn, with exports totalling RM400m, impacted by competition from over-the-top platforms and a crowded broadcast market. Covid-19 also affected export values, and regulations such as Children’s Online Privacy Protection Rule influenced content distribution on platforms such as YouTube. Malaysia’s broader motion picture, video, TV program production, sound recording, and music publishing activities experienced modest growth, reaching RM3.9bn in gross output by 2021, with a marginal CAGR of 0.5% from 2017 to 2021.

Revenue of Digital Creative Content in Malaysia



Source: Vital Factor Consulting

Export Value of Digital Creative Content in Malaysia



Source: Vital Factor Consulting

- Quality of 2D animation production hinges on skilled production staff, with salaries and wages representing a significant production cost. From 2017 to 2021, Malaysia's motion picture, video, TV program production, sound recording, and music publishing sectors saw minimal workforce growth at a four-year CAGR of 0.1%, while salaries and wages increased at a four-year CAGR of 0.9%. This resulted in a four-year 0.8% CAGR for average salaries and wages per person engaged.
- The Mid-Term Review of the Twelfth Malaysia Plan (12MP) outlines government initiatives to promote creative career paths and enhance industry bridging programs with local and global digital content studios. Malaysia Digital Economy Corporation (MDEC) has implemented key programs like the Digital Content Grant, which funds local companies in developing digital content such as animation and games. Digital Creative Content Creator Studio offers training allowances to studios for internships, benefiting both companies and Malaysian youth. Meanwhile, Enterprise Development Programme (EDP) provides free or low-cost courses covering technical and business aspects of the creative industry.
- Digital Content Creators Challenge (DC3) promotes the creation of digital content through competitions, supporting winners with mentorship and funding. 'Kre8tif!' serves as a networking platform for industry players to connect and pitch ideas to global buyers. These initiatives aim to boost Malaysia's digital creative content sector, including providers in 2D animation like Kucingko Group.
- Additionally, the Film in Malaysia Incentive (FIMI) by FINAS offers up to 30.0% cash rebate on qualifying Malaysian production expenditures (QMPE), encouraging local and foreign production companies to engage in productions like animations and documentaries, thereby lowering production costs and enhancing opportunities for Malaysia's 2D animation production service providers.

Investment Highlights

- **Established track record of 22 years in 2D animation production to sustain and grow the 2D animation business.** Kucingko has accumulated 22 years of experience in 2D animation production since establishment in 2002. Over the years, the Group has developed 12 projects, comprising nine animated series, 1one short film, one graphic novel, and one animated character, totalling approximately 1,900 minutes of proprietary 2D animation content. Subsequently, the Group shifted its focus to providing 2D animation production services.
- **First 2D animation company listed on Bursa Malaysia with decent growth prospects.** Based on the latest financial reporting period, Kucingko has successfully completed 63 animation projects, with a collective contract value of RM75.6m and a total runtime of approximately 5,015 minutes. Currently, the Group is managing 10 ongoing animation projects valued at RM45.4m, with a total runtime of about 1,792 minutes. As of the latest reporting date, the Group is equipped with an unbilled order book with a total of RM23.3m from ongoing projects, expected to be recognised between FY24F and FY25F.
- **Strong customer base in foreign markets.** Over the years, the Group's has developed and extensive track record served as a foundation for future growth, to effectively serve existing clients and attract new ones seeking reliable and experienced animation production services. Kucingko primarily operates in six to eight foreign countries annually, including North America (USA, Canada, Mexico), Asia Pacific (Australia, Singapore, Japan, Hong Kong), and Europe (United Kingdom, France, Netherlands). Revenue from 2D animation production services derived from international markets, contributed 99.7% (RM14.8m), 99.5% (RM17.6m), 99.6% (RM23.4m), and 99.8% (RM28.1m) to total revenue for FY20, FY21, FY22, and FY23 respectively. This underscores Kucingko's ability to access diverse global markets. Capability to serve multiple international markets, coupled with their established presence in the North American entertainment sector, well positioned for sustainability.
- **Engaged in animation projects distributed through traditional television broadcasting and online streaming platforms to reach a global audience.** Kucingko serves internationally recognised brands in the entertainment industry, including owners, producers, and distributors of 2D animated series for the global market. Key customers such as Warner Bros Group and Titmouse Group have entrusted the Group with notable projects such as Monster Beach, Lamput 3, The Harper House, and Mao Mao Heroes of Pure Heart. The animated series are broadcasted on traditional television and online streaming platforms, reaching a worldwide audience. The Group's ability to consistently meet customer requirements is evidenced by long-standing relationships with top clients; three of their top five customers in FY22 have been with them for between 9 to 16 years.
- **Sound Financial Condition.** The Group maintained strong double-digit PAT margins and a robust balance sheet over the years. EBITDA stepped up from RM6.2m in FY20 to RM11.9m in FY23. Moreover, the Group maintains a low gearing ratio of 0.1x and a healthy trade receivables turnover of 30 days, indicating strong receivables management. Additionally, Kucingko is committed to a dividend policy that distributes at least 40% of PAT.

Financial Highlights

- Kucingko's core net profit has demonstrated sturdy performance, reaching RM8.4m in FY23 (three-year CAGR of +31.5%). Growth was primarily driven by increased revenue from the 2D animation production services segment. Concurrently, net margins have steadily improved from 24.7% in FY20 to 29.7% in FY23. However, PAT margin shrank from 34.0% in FY22 to 29.7% in FY23 was mainly due to lower other operating income and higher operating and tax expenses relative to revenue. This were largely impacted by higher professional expenses, including listing expenses, and increased staff costs.
- Looking ahead, we project a gradual 13.3% yoy improvement in core net profit for FY24F at RM9.5m, despite anticipated higher costs related to listing and staff expenses. Our projections include factoring in RM23.3m of unbilled projects and recognition of additional tender book.
- Going to FY25F, we anticipate Kucingko to achieve a top line of RM39.8m (+2.5% yoy) and a bottom line of RM9.7m (+2.5% yoy). Growth is expected to be driven by (i) partial recognition from RM30.0m in order replenishment, (ii) aggressive marketing initiatives aimed at capturing additional market share from untapped segments, and (iii) increasing manpower to cater for more projects from larger parties in entertainment industries.

Financial Highlights

FYE Dec (RM m)	FY21	FY22	FY23	FY24F	FY25F
Revenue	17.7	23.5	28.2	38.8	39.8
EBITDA	9.1	10.4	11.9	14.6	14.9
Pre-tax Profit	8.2	9.4	10.8	12.6	12.9
Profit After Tax	6.5	8.0	8.4	9.5	9.7
Net Profit	6.5	8.0	8.4	9.5	9.7
Core Net Profit	6.5	8.0	8.4	9.5	9.7
Core EPS (sen)	1.3	1.6	1.7	1.9	1.9
Core P/E (x)	23.1	18.8	17.9	15.8	15.5
Dividend Yield (%)	N/A	N/A	N/A	2.5	2.6
P/B (x)	10.3	9.5	8.4	6.9	5.9
ROE (%)	44.6	50.5	46.6	43.6	37.9
Gearing (%)	6.0	6.3	4.7	3.9	3.3

Source: Kucingko, Apex Securities

Valuation & Recommendation

- At an IPO offer price of RM0.30, Kucingko's forward PE valuation for FY24F and FY25F is projected at 15.8x and 15.5x, based on our estimated FY24F and FY25F EPS of 1.9 sen and 1.9 sen respectively. We arrived at our fair value of RM0.54 (80.0% potential upside from its IPO price) by assigning a target PE of 28.0x to its FY25F EPS.
- The assigned target PE represents approximately 10.0% discount to selected peers that offer media services such as ASTRO, STAR and SJC that are trading at an average forward PE of 29.7x for 2025F. The discount to selected peers is justifiable, premised on Kucingko's niche business in the provision of 2D animation production

and successfully secured a few well-known entertainment industry players projects for a couple of years.

- We favour Kucingko for its dominant position in the foreign market, recognising approximately 74.0% of revenue in the North America region as of FY23. The US video streaming market is projected to grow at a six-year CAGR of 19.8% from 2024 to 2030. Anticipated expansion in digital content distribution is expected to further drive demand for the Group's 2D animation services. Additionally, we like Kucingko for its consistent strong double-digit return on equity (ROE) over the years, robust balance sheet, and healthy cash position.
- However, we forecast that Kucingko will experience slower growth rate in core net profit, primarily due to increasing manpower. The Group is currently facing a shortage of manpower due to various ongoing projects. We anticipate bulk of the expenses will be channelled to expansion and staffing costs, resulting in a higher quantum of increase in net profit starting from FY26F onwards.
- Kucingko also adopt a formal dividend policy, with a not less than 40% dividend payout from net profit. Based on our forecasted core net profit, projected dividend yields are fairly decent at 2.5% and 2.6% for FY24F and FY25F respectively.

Peers Comparison

Company	Market Group	FYE	Price (RM)	Market Cap (RM 'm)	P/E (x)		Gross DY (%)	Revenue RM 'm	Net Income RM 'm
					FY24F	FY25F			
Kucingko Berhad	ACE	Dec	0.300	150.0	17.9	15.8	-	28.2	8.4
Astro Holdings Bhd	MAIN	Jan	0.32	1644.0	31.5	11.3	0.79	3290.7	37.9
Star Media Group Bhd	MAIN	Dec	0.39	279.0	385.0	48.1	2.60	221.3	6.2
Seni Jaya Corporation Bhd	MAIN	Dec	0.26	55.5	9.5	12.0	-	21.5	9.3
Avg ex-Kucingko Berhad					208.3	29.7	1.7	1756.0	22.0

Source: Kucingko, Bloomberg, Apex Securities

Investment Risk

- Exposed to fluctuations in foreign exchange rates.
- Relies on the capability to secure new and significant projects.
- High client concentration

APEX SECURITIES BERHAD – CONTACT LIST

APEX SECURITIES BHD	DEALING TEAM	RESEARCH TEAM
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RESEARCH RECOMMENDATION FRAMEWORK

STOCK RECOMMENDATIONS

BUY: Total returns* are expected to exceed 10% within the next 12 months.
HOLD: Total returns* are expected to be within +10% to – 10% within the next 12 months.
SELL: Total returns* are expected to be below -10% within the next 12 months.
TRADING BUY: Total returns* are expected to exceed 10% within the next 3 months.
TRADING SELL: Total returns* are expected to be below -10% within the next 3 months.
 *Capital gain + dividend yield

SECTOR RECOMMENDATIONS

OVERWEIGHT: The industry defined by the analyst is expected to exceed 10% within the next 12 months.
NEUTRAL: The industry defined by the analyst is expected to be within +10% to – 10% within the next 12 months.
UNDERWEIGHT: The industry defined by the analyst, is expected to be below -10% within the next 12 months.

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