

23 February 2018 | 4QFY17 Results Review

Kossan Rubber Industries

Higher revenue across all business segments

Maintain NEUTRAL

Revised Target Price (TP): RM8.78
(Previously RM7.57)

INVESTMENT HIGHLIGHTS

- **4QFY17 earnings within expectations at RM45.9m**
- **Higher revenue contribution across business segments**
- **New capacity expansion on track**
- **Proposed share split of 1-to-2 of Kossan shares**
- **FY18F earnings forecasts increased by +6.6%**
- **Maintain NEUTRAL with a revised TP of RM8.78**

Within expectations. Kossan's 4QFY17 earnings came in at RM45.9m. This brings its FY17 earnings to RM183.6m which is within our but below consensus' full-year earnings expectation at 99.9% and 95% of full year forecasts respectively. Against last year, revenue and earnings increased by +9.0% and +2.9% respectively. However, on a quarterly sequential basis, it recorded a marginal decline in revenue by -2.3% and +0.5% in earnings respectively. No dividend was declared for the quarter under review.

Higher revenue contribution across business segments. In 4QFY17, the increase in revenue year-over-year was mainly attributable to: (i) increase in sales volume (5.0%yoy) and; (ii) higher revenue contribution across its business segments. During the quarter, its gloves division recorded a revenue increase of +8.77%yoy. Meanwhile, its technical rubber products (TRP) as well as Cleanroom division also recorded a +10.3% and +28.7% increase in revenue respectively vs 4Q16. In addition, efficient manufacturing processes, increased automation as well as; higher sales deliveries were among the factors contributing to the higher revenue. Furthermore, revenue and earnings during the quarter were also assisted by the increase in average selling prices (ASP) for its gloves which grew by an average of +%3.0yoy.

New capacity expansion on track. Management disclosed that Kossan's Plant 16's that will contribute +3.0b new capacity has been fully-commissioned last December 2017. Plant 16 will begin to contribute to Kossan's revenue in FY18. Meanwhile, the other two plants to be built along Jalan Meru (Plant 17 and 18) are now currently under construction and are expected to be completed by 2018 and will start contributing to Kossan's revenue thereafter. These two new plants will add +4.5b of new capacity to Kossan's production going forward.

RETURN STATS	
Price (22 February 2018)	RM8.70
Target Price	RM8.78
Expected Share Price Return	+0.9%
Expected Dividend Yield	+1.3%
Expected Total Return	+2.2%

STOCK INFO	
KLCI	1,855.07
Bursa / Bloomberg	7153 / KRI MK
Board / Sector	Main / Trading Services
Syariah Compliant	YES
Issued shares (mil)	639.47
Market cap. (RM'm)	5,563.37
Price over NA	4.86
52-wk price Range	RM5.62 – RM8.79
Beta (against KLCI)	0.5
3-mth Avg Daily Vol	0.75m
3-mth Avg Daily Value	RM6.22m
Major Shareholders (%)	
Kossan Holdings Sdn Bhd	51.06
EPF	8.54
Citibank New York	1.95

Proposed share split of 1-to-2 Kossan shares. Kossan has also announced a proposed 1-for-2 subdivision of shares yesterday. The share division which is slated to be completed by end of September 2018, is expected to boost the trading liquidity of its shares as well as encourage participation from new investors in the company's growth. Post the subdivision, its share base will increase to 1,278.9m from the current 639.5m. We are neutral on this announcement as despite the increase in number of shares allocated to investors, there will be dilution in earnings per share (EPS) from the current FY18F EPS of 36.6sen to 18.3sen. Subsequently, our **TP will be revised to RM4.39** to reflect the enlarged share based once the exercise is completed in 3Q18.

Earnings forecast. Post earnings announcement, we are revising our FY18F earnings forecasts up by +6.6% as we increase our ASP assumption due to the increase in production cost such as: natural gas. Key risks to our earnings would most likely be: (i) increasing competition which may squeeze margins and ASP; (ii) sudden jump in raw materials prices i.e latex and nitrile and; (iii) demand and supply mismatch.


Maintain NEUTRAL with a revised Target Price (TP) of RM8.78. Post earnings announcement and adjustment, we are maintaining our **NEUTRAL** recommendation on Kossan with a revised TP of **RM8.78** per share. Our TP is derived via pegging our FY18F EPS of 36.6sen to a revised PER18 of 24x, representing the average PER across three years. We believe that despite the high demand for gloves, earnings growth for this year will continue to be constrained as currently Kossan is already operating at full capacity with its latest Plant 16's capacity being sold out and new capacity of +4.5b will only come in by end-2018. In addition, as its share price has recently surge to current level last seen since October 2016, we are expecting limited upside to its share price at this juncture. 

Table 1: Kossan's quarterly earnings review

FYE Dec (RM'm)	Quarterly results					Cumulative results		
	4QFY16	3QFY17	4QFY17	QoQ (%)	YoY (%)	FY16	FY17	YoY (%)
Revenue	438.2	489.2	477.8	(2.3)	9.0	1,668.3	1,957.4	17.3
Operating expenses	(382.3)	(428.7)	(416.3)	(2.9)	8.9	(1,448.3)	(1,720.0)	18.8
Other operating income	1.2	0.9	0.8	(12.5)	(34.3)	3.4	3.5	2.8
Finance costs	(2.6)	(3.1)	(3.3)	4.5	24.9	(10.0)	(11.3)	13.1
Profit Before Tax	54.4	58.2	59.0	1.4	8.5	213.4	229.6	7.6
Taxation	(9.0)	(12.2)	(12.5)	3.0	38.9	(39.2)	(44.0)	12.4
Profit After Tax	45.4	46.0	46.5	1.0	2.4	174.2	185.6	6.5
Non-controlling interest	0.7	0.3	0.6	61.4	(24.4)	3.3	2.0	(41.0)
PATANCI	44.6	45.7	45.9	0.5	2.9	170.9	183.6	7.4
Basic EPS (sen)	7.0	7.1	7.2	0.5	2.9	26.7	28.7	7.4
PBT margin (%)	12.4	11.9	12.3	0.1	(7.6)	17.3	18.7	1.3
PAT margin (%)	10.4	9.4	9.7	0.0	(6.6)	14.2	15.1	0.9
PATANCI margin (%)	10.2	9.3	9.6	0.0	(6.5)	13.9	14.9	1.0
Tax rate (%)	16.6	20.9	21.2	0.3	4.7	18.4	19.2	0.8
Segments								
Revenue								
Technical Rubber Division	38.2	37.9	42.2	11.2	10.3	160.6	162.0	0.9
Gloves Division	380.9	425.9	414.3	(2.7)	8.8	1,436.8	1,716.4	19.5
Clean Room Division	15.7	24.8	20.2	(18.4)	29.1	64.8	76.4	17.9
PBT								
Technical Rubber	8.7	3.6	4.4	21.7	(49.3)	30.5	16.2	(46.7)
Gloves	43.0	53.6	53.5	(0.1)	24.4	178.6	209.9	17.5
Clean Room	1.3	0.8	0.6	(18.9)	(49.9)	2.6	2.9	11.9

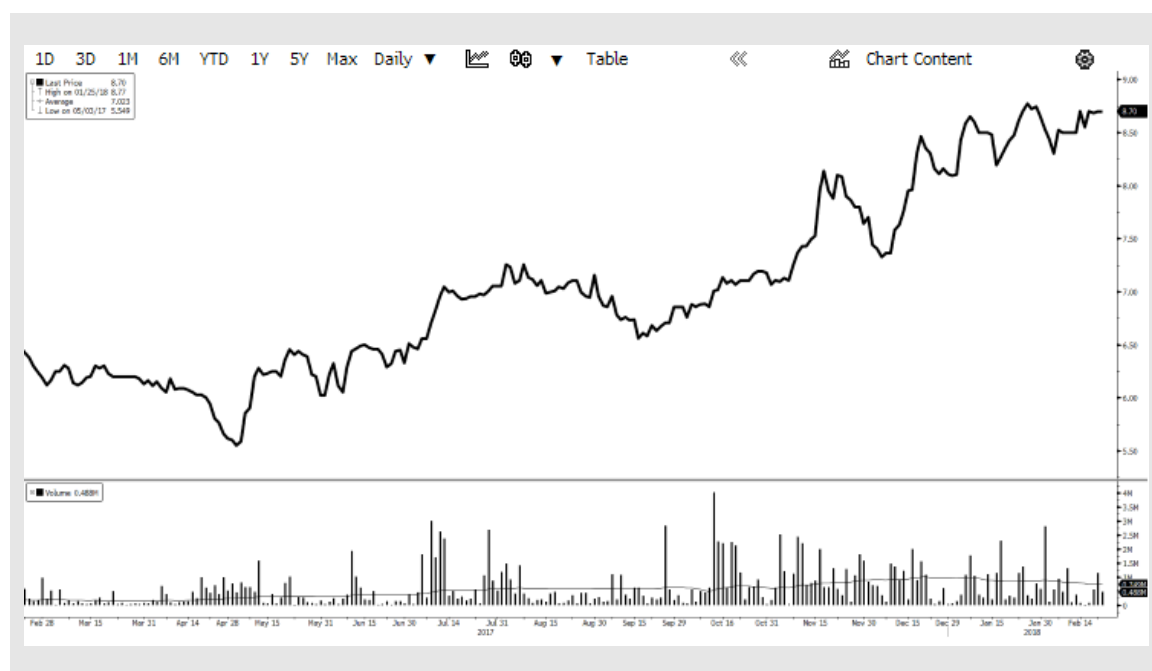
Source: Company

INVESTMENT STATISTICS

FYE Dec (RMm)	FY2015	FY2016	FY2017	FY2018F	FY2019F
Revenue	1635.9	1668.3	1957.4	1927.8	2107.7
Operating Profit	278.6	223.4	240.9	321.0	374.2
Profit Before Tax	268.5	213.4	229.6	312.5	365.8
Profit After Tax	207.1	174.2	185.6	234.4	274.3
Operating Profit margin (%)	17.0	13.4	12.3	16.7	17.8
PBT margin (%)	16.4	12.8	11.7	16.2	17.4
PATAMI margin (%)	12.7	10.4	9.5	12.2	13.0
EPS (sen)	31.8	27.2	28.8	36.6	42.9
EPS Growth (%)	44.0	-14.3	5.6	27.4	17.1
PER (x)	27.4	31.9	30.2	23.7	20.3
Dividend per share (sen)	5.5	7.5	5.0	10.8	13.1
Dividend yield (%)	0.6	0.9	0.6	1.2	1.5

Source: Company, Forecasts by MIDFR

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.