

## Kossan Rubber Industries Berhad

(7153 | KRI MK) Main | Healthcare | Healthcare Equipment and Services

### Earnings Turned into Black in 3QFY23

#### KEY INVESTMENT HIGHLIGHTS

- **Above expectations**
- **Improved operating profit margin in 3QFY23**
- **Raised earnings projections for FY23F-25F**
- **Changed valuation to 2-year historical average P/BV**
- **Upgrade to NEUTRAL (from SELL) with a higher TP of RM1.38 (previously RM0.88)**

**Above expectations.** Kossan Rubber Industries ("KRI") reported a core net loss of -RM3.1m in 9MFY23, after excluding a one-time item of -RM16.5m. The core net loss was narrower than ours and consensus full-year FY23F estimation of -RM55.3m/-RM66.5m respectively. This was mainly driven by: (1) higher-than-expected sales volume and (2) lower-than-expected operating costs, thanks to reduced raw material costs, natural gas expenses, and production costs per unit. No dividends were declared in the quarter.

**Improved operating profit margin in 3QFY23.** On sequential basis, revenue rose +4.1%qoq to RM403.5m, primarily due to increased sales volume offsetting a slight decline in blended ASP. The 3QFY23 operating margin improved by +11.5ppt qoq to 12.2%, driven by higher revenue across all divisions along with enhanced cost control, lower input costs from natural gas and raw materials. Consequently, core PATANCI turned positive, from a core net loss of -RM2.8m in 2QFY22 to RM34.3m in 3QFY23. On a yearly basis, despite a -28%yoy decrease in revenue to RM403.5m, core PATANCI surged +73.4%yoy to RM34.3m. This was fuelled by improved cost control for the gloves division and the sale of higher-margin infrastructure products from the TRP division.

**Core net loss in 9MFY23 due to oversupply situation.** Cumulatively, KRI reported a core net loss of -RM3.1m in 9MFY23 vs. a core PATANCI of RM146.3m in 9MFY22. This was primarily due to the lower revenue in gloves and cleanroom divisions, coupled with rising input costs, resulting in elevated production costs per unit.

**Raised earnings projections for FY23F-25F.** Given that the earnings came above our expectation, we raised our earnings forecast for FY23F from a net loss of -RM55.3m to a core PATANCI of RM37.1m. This was after factoring in (1) slightly higher sales volume, (2) updating the exchange rate to be in line with our in-house economists' forecast, (3) lower raw material costs, as well as (4) a better operating profit margin due to the better utilization rate that lowers the production cost per unit. We also raised our earnings forecast for FY24F-25F higher by 48% and 4%, respectively.

**Upgrade to NEUTRAL**

(Previously SELL)

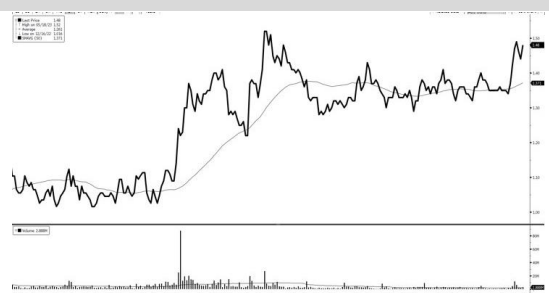
**Revised Target Price: RM1.38**

(Previously: RM0.88)

#### RETURN STATISTICS

Price @ 15 <sup>th</sup> Nov 2023 (RM)	1.48
Expected share price return (%)	-6.60
Expected dividend yield (%)	0.0
Expected total return (%)	-6.60

#### SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	8.8	7.1
3 months	12.1	10.8
12 months	31.0	29.5

#### INVESTMENT STATISTICS

FYE Dec (RM'm)	2023F	2024F	2025F
Revenue	1,637.3	1,872.6	2,234.7
EBITDA	151.7	239.8	315.0
Profit Before Tax	65.6	152.1	225.3
Core PATANCI	37.1	124.3	184.2
Core EPS (sen)	1.5	4.9	7.2
DPS (sen)	0.0	1.5	2.2
Dividend Yield (%)	0.0	1.1	1.6

#### KEY STATISTICS

FBM KLCI	1,466.84
Issue shares (m)	2545.37
Estimated free float (%)	45.18
Market Capitalisation (RM'm)	3,776.40
52-wk price range	RM1.02- RM1.62
3-mth average daily volume (m)	2.23
3-mth average daily value (RM'm)	3.07
Top Shareholders (%)	
Kossan Holdings M Sdn Bhd	35.00
Abrdn PLC	5.87
Employees Provident Fund Board	3.77


**Analyst(s)**

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**Changed valuation to 2-year historical average P/BV.** Given the turnaround in earnings during the quarter, which reflect a sign of stability. Hence, we changed our valuation from a 2-year historical -1SD P/BV of 0.59x to a 2-year historical average P/BV of 0.89x to better reflect the medium to long-term outlook.

**Upgrade to NEUTRAL (from SELL) with a higher TP of RM1.38 (previously RM0.88).** Our revised TP is based on a higher FY24F BVPS of 155sen (previously 150 sen), pegged to a revised P/BV of 0.89x PER (from 0.59), which represents its 2-year historical average P/BV. Hence, we upgrade to NEUTRAL from SELL. Moving forward, we anticipate the ASP for the gloves division to remain flattish in the near term due to the ongoing oversupply situation and intense competition from Chinese glove manufacturers. On a positive note, we observed a slight turnaround in the glove divisions as buyers replenish their inventory following the expiration of pandemic-related stockpiles. This could result in an improved utilization rate ahead, leading to lower production costs per unit and consequently improved margins. Furthermore, we are optimistic about the robust performance of the Technical Rubber Products division ("TRP"), driven by the recovery in global economic activity and increased infrastructure spending, which could provide protection against challenges in the glove divisions. We also appreciate Kossan Rubber's status as a net cash company, boasting a net cash position of RM1.26b (36.2% of market cap) as of 3QFY23, offering protection against downside risks.

**Potential catalysts** include: (i) a faster-than-expected recovery in utilization rate; and (ii) more new entrants leaving the market and/or existing companies discontinuing certain manufacturing lines. 

### Kossan Rubber Industries: 3QFY23 Results Summary

FYE Dec (RM's)	Quarterly results					Cumulative results		
	3QFY23	2QFY23	3QFY22	YoY (%)	QoQ (%)	9MFY23	9MFY22	YoY (%)
Revenue	403.5	387.5	560.5	(28.0)	4.1	1,185.7	1,841.0	(35.6)
Operating expenses	(373.8)	(401.8)	(546.2)	(31.6)	(7.0)	(1,206.2)	(1,664.5)	(27.5)
Other operating income	19.5	17.1	14.6	33.5	14.1	53.8	38.5	39.7
<b>Operating profit (EBIT)</b>	<b>49.1</b>	<b>2.8</b>	<b>28.9</b>	<b>69.8</b>	<b>1,663.0</b>	<b>33.3</b>	<b>215.1</b>	<b>(84.5)</b>
Net finance income/(cost)	(0.2)	(0.3)	(1.1)	(84.4)	(30.4)	(0.9)	(3.1)	(71.8)
Profit before tax (PBT)	49.0	2.5	27.8	76.1	1,835.1	32.4	211.9	(84.7)
Taxation	(7.2)	(5.2)	(3.2)	127.0	38.1	(16.9)	(50.1)	(66.4)
<b>Profit After tax (PAT)</b>	<b>41.8</b>	<b>(2.7)</b>	<b>24.6</b>	<b>69.6</b>	<b>&gt;(100.0)</b>	<b>15.6</b>	<b>161.8</b>	<b>(90.4)</b>
PATANCI	41.0	(3.3)	23.3	76.1	>(100.0)	13.4	159.4	(91.6)
<b>Core PATANCI</b>	<b>34.3</b>	<b>(2.8)</b>	<b>19.8</b>	<b>73.4</b>	<b>&gt;(100.0)</b>	<b>(3.1)</b>	<b>146.3</b>	<b>&gt;(100.0)</b>
Basic EPS (sen)	1.6	(0.1)	0.9	76.9	>(100.0)	0.5	6.2	(91.5)
DPS (sen)	0.0	0.0	0.0	n.m.	n.m.	0.0	0.0	n.m.
<b>Growth &amp; Margin (%)</b>				<b>+ / (-) ppts</b>	<b>+ / (-) ppts</b>			<b>+ / (-) ppts</b>
Operating Profit Margin	12.2	0.7	5.2	7.0	11.5	2.8	11.7	(8.9)
PBT Margin	12.1	0.7	5.0	7.2	11.5	2.7	11.5	(8.8)
Core PATANCI Margin	8.5	(0.7)	3.5	5.0	9.2	(0.3)	7.9	(8.2)
<b>Ratios &amp; Valuation</b>				<b>+ / (-) ppts</b>	<b>+ / (-) ppts</b>			<b>+ / (-) ppts</b>
Net cash/market cap (%)	36.2	35.3	34.7	1.4	0.9	36.2	34.7	1.4
Effective tax rate (%)	14.6	n.m.	11.3	3.3	n.m.	52.0	23.7	28.3

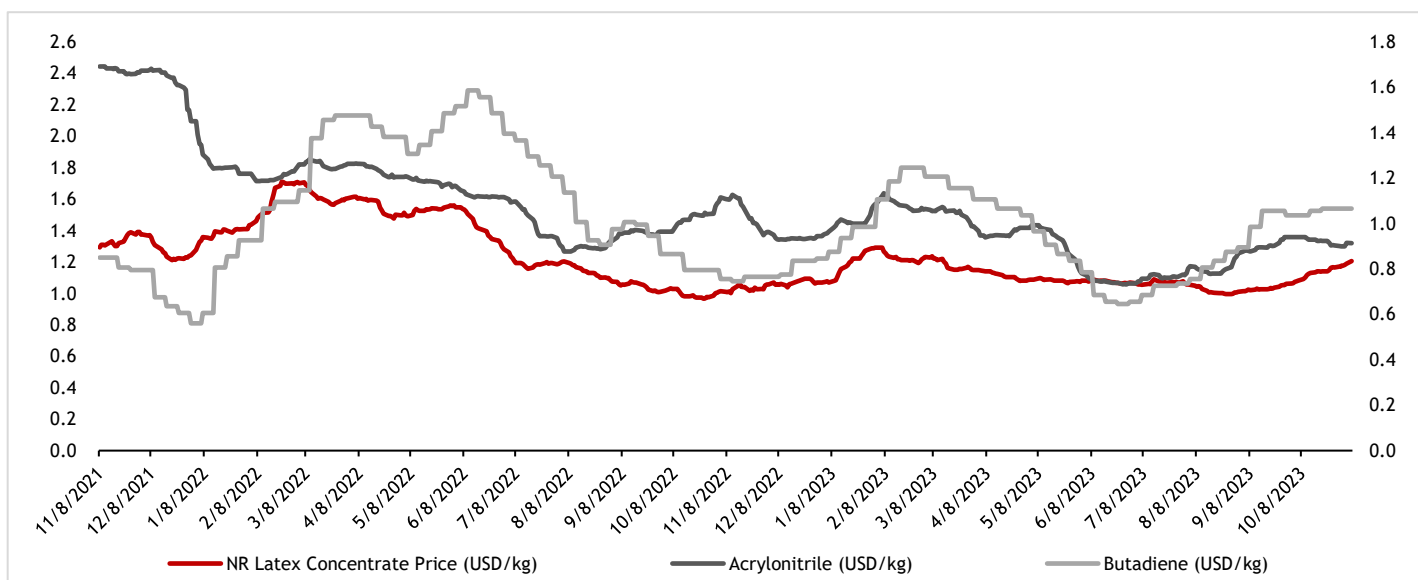
Source: Company, MIDFR

## Kossan Rubber Industries: Breakdown by operating segment

FYE Dec (RM'm)	Quarterly results					Cumulative results		
	3QFY23	2QFY23	3QFY22	YoY (%)	QoQ (%)	9MFY23	9MFY22	YoY (%)
<b>Revenue (RM'm):</b>								
Gloves Division	321.2	315.9	464.2	(30.8)	1.7	954.6	1,593.8	(40.1)
Technical Rubber Division	56.3	47.8	64.7	(12.9)	17.8	160.3	152.6	5.1
Cleanroom Division	25.9	23.9	31.7	(18.1)	8.6	70.8	91.0	(22.2)
Others	0.0	0.0	0.0	n.m.	n.m.	0.0	2.7	(100.0)
<b>Total</b>	<b>403.5</b>	<b>387.5</b>	<b>560.5</b>	<b>(28.0)</b>	<b>4.1</b>	<b>1,185.7</b>	<b>1,840.1</b>	<b>(35.6)</b>
<b>Operating Profit (RM'm):</b>								
Gloves Division	31.2	(12.1)	1.0	2,993.4	(358.5)	(15.8)	165.4	(109.5)
Technical Rubber Division	11.0	8.6	5.6	94.7	27.9	27.5	14.7	86.7
Cleanroom Division	2.8	2.4	4.5	(37.9)	18.4	6.8	7.9	(13.9)
Others	4.0	3.6	16.6	(76.2)	8.4	13.9	24.0	(41.9)
<b>Total</b>	<b>49.0</b>	<b>2.5</b>	<b>27.8</b>	<b>76.1</b>	<b>1,835.1</b>	<b>32.4</b>	<b>211.9</b>	<b>(84.7)</b>
<b>Operating profit margin (%)</b>				<b>+ / (-) ppts</b>	<b>+ / (-) ppts</b>			<b>+ / (-) ppts</b>
Gloves Division	9.7	(3.8)	0.2	9.5	13.5	(1.7)	10.4	(12.0)
Technical Rubber Division	19.5	17.9	8.7	10.8	1.5	17.1	9.6	7.5
Cleanroom Division	10.9	10.0	14.3	(3.5)	0.9	9.6	8.7	0.9
Others	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.	>100.0	n.m.
<b>Total</b>	<b>12.1</b>	<b>0.7</b>	<b>5.0</b>	<b>7.2</b>	<b>11.5</b>	<b>2.7</b>	<b>11.5</b>	<b>(8.8)</b>

Source: Company, MIDFR

TABLE 1: Raw Material Futures Price Trend (USD/MT)



Source: MIDFR, Bloomberg

**FINANCIAL SUMMARY**

<b>Income Statement (RM'm)</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
<b>Revenue</b>	<b>6,631.5</b>	<b>2,343.8</b>	<b>1,637.3</b>	<b>1,872.6</b>	<b>2,234.7</b>
Raw materials and consumable used	(1,945.6)	(1,263.3)	(957.5)	(1,089.7)	(1,287.3)
Changes in inventories of finished goods & WIP	(39.4)	(71.7)	(19.6)	32.4	49.1
Goods purchased for resale	(45.1)	(57.9)	(40.8)	(47.2)	(56.8)
<b>Gross Profit</b>	<b>4,601.4</b>	<b>950.9</b>	<b>619.4</b>	<b>768.2</b>	<b>939.6</b>
Other (expense)/income	15.0	44.1	35.3	40.6	48.7
Staff costs	(419.7)	(374.5)	(266.8)	(308.3)	(371.5)
Other operating expenses	(355.2)	(304.6)	(236.2)	(260.7)	(301.8)
<b>EBITDA</b>	<b>3,841.5</b>	<b>315.9</b>	<b>151.7</b>	<b>239.8</b>	<b>315.0</b>
<b>EBIT</b>	<b>3,721.9</b>	<b>184.5</b>	<b>30.7</b>	<b>117.7</b>	<b>188.4</b>
<b>Profit before tax (PBT)</b>	<b>3,747.3</b>	<b>213.5</b>	<b>65.6</b>	<b>152.1</b>	<b>225.3</b>
<b>Profit After tax (PAT)</b>	<b>2,856.9</b>	<b>159.2</b>	<b>53.6</b>	<b>124.3</b>	<b>184.2</b>
<b>Core PATANCI</b>	<b>2,857.1</b>	<b>145.7</b>	<b>37.1</b>	<b>124.3</b>	<b>184.2</b>
Core EPS (sen)	112.0	5.7	1.5	4.9	7.2
DPS (sen)	48.0	2.5	0.0	1.5	2.2

<b>Balance Sheet (RM'm)</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
Property, plant and equipment	1,373.7	1,356.9	1,243.0	1,128.9	1,087.8
Intangible assets & Goodwill	6.0	6.0	4.2	4.8	5.8
<b>Total Non-current assets</b>	<b>1,495.2</b>	<b>1,470.6</b>	<b>1,384.5</b>	<b>1,285.6</b>	<b>1,263.8</b>
Inventories	424.0	287.1	267.5	299.9	349.0
ST - Trade and other receivables	558.6	276.0	292.3	329.3	387.1
Cash and cash equivalents	2,557.8	1,348.0	1,299.5	1,412.0	1,516.5
<b>Total current assets</b>	<b>3,584.6</b>	<b>2,856.5</b>	<b>2,864.5</b>	<b>3,089.1</b>	<b>3,392.9</b>
<b>Total Assets</b>	<b>5,079.8</b>	<b>4,327.1</b>	<b>4,249.1</b>	<b>4,374.6</b>	<b>4,656.7</b>
LT Loans and borrowings	56.0	0.9	0.1	0.1	0.1
LT Lease Liabilities	8.7	5.8	1.6	1.7	1.9
<b>Total Non-current liabilities</b>	<b>194.1</b>	<b>144.5</b>	<b>59.4</b>	<b>61.2</b>	<b>72.9</b>
ST Loans and borrowings	182.4	71.3	7.1	7.2	7.3
ST Trade and other payables	297.3	200.2	185.3	206.6	239.2
<b>Total Current Liabilities</b>	<b>825.3</b>	<b>284.7</b>	<b>266.7</b>	<b>352.7</b>	<b>546.7</b>
<b>Total Liabilities</b>	<b>1,019.4</b>	<b>429.2</b>	<b>326.1</b>	<b>413.9</b>	<b>619.6</b>

<b>Cash Flow (RM'm)</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
Pretax profit	3,747.3	213.5	65.6	152.1	225.3
Cash flow from operations	3,236.0	103.7	(14.6)	139.4	227.1
Cash flow from investing	(222.9)	(812.3)	13.7	10.2	(67.7)
Cash flow from financing	(1,540.1)	(480.9)	(69.2)	(37.1)	(54.9)
<b>Net cash flow</b>	<b>1,473.0</b>	<b>(1,189.6)</b>	<b>(70.1)</b>	<b>112.5</b>	<b>104.5</b>
(+/-) Adjustments	6.5	(9.9)	0.0	0.0	0.0
<b>Net cash/(debt) b/f</b>	<b>1,089.5</b>	<b>2,569.1</b>	<b>1,369.6</b>	<b>1,299.5</b>	<b>1,412.0</b>

<b>Key Metrics</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
Effective tax rate (%)	23.8	25.4	18.3	18.3	18.3
PER (x)	1.2	22.1	64.7	27.9	18.8
P/BV ratio (x)	0.85	0.89	0.88	0.88	0.86
Cash/Market Capitalisation (%)	66.8	36.8	37.2	40.5	43.5
Cash/share (sen)	126.8	4.1	(0.6)	5.5	8.9

<b>Profitability Margins</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	<b>2025F</b>
Gross Profit Margin (%)	69.4	40.6	37.8	41.0	42.0
EBIT Margin (%)	56.1	7.9	1.9	6.3	8.4
Core PATANCI Margin (%)	43.1	6.2	2.3	6.6	8.2

Source: Bloomberg, MIDFR

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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.

#### ESG RECOMMENDATIONS\* - source Bursa Malaysia and FTSE Russell

☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

\* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology