

Kossan Rubber Industries Berhad

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

Building Strength Amidst Improving Demand

Upgrade to NEUTRAL
(Previously SELL)
Revised Target Price: RM2.45
(Previously RM1.35)

KEY INVESTMENT HIGHLIGHTS

- **Within expectation**
- **1QFY24 Core earnings turned positive**
- **Better outlook backed by easing oversupply situation**
- **Revised FY24-F26F earnings forecast higher and upgrade valuation.**
- **Upgrade to NEUTRAL (previously SELL) with a higher TP of RM2.45 (previously RM1.35)**

Within expectation. Kossan Rubber's 1QFY24 core PATANCI was RM24.7m, excluding a one-time expense of -RM6.7m. This aligned with our full-year FY24 forecast but fell short of consensus estimates, representing 21.5% of our and 16.9% of the street's full-year FY24 forecast. No dividend was declared during 1QFY24, as anticipated.

1QFY24 Core earnings turned positive. The revenue rose +14.4%yoy to RM451.6m, mainly due to higher sales volumes of gloves and increased clean-room division sales. Core earnings turned positive, from a net loss of -RM34.6m in 1QFY23 to RM24.7m in 1QFY24. This was driven by (1) improved profit margins in the gloves division, due to higher sales and lower natural gas prices reducing production costs, and (2) better product mix in the TRP division. On quarterly basis, topline increased +12.9%yoy to RM451.6m, driven by higher glove sales and TRP product deliveries. Despite higher revenue, core PATANCI dropped by -19.6%qoq to RM24.67m due to lower PBT from both the TRP and cleanroom divisions.

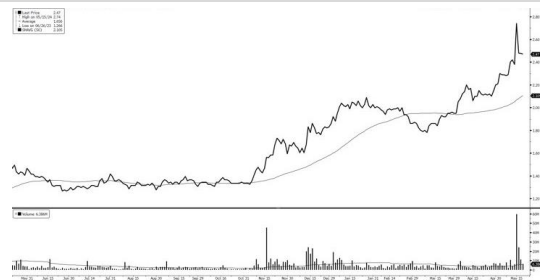
Better outlook backed by easing oversupply situation. We gather that the ongoing industry consolidation and capacity adjustment have reduced the oversupply situation. Although ASP pressure from international competitors remains, stricter standards and increased hygiene awareness in medical and industrial sectors have shifted customer preference towards high-quality gloves, benefiting Malaysian manufacturers. The gradual increase in global economic activity and infrastructure investment is expected to stimulate demand for technical rubber products in FY24.

Revised FY24-F26F earnings forecast higher and upgrade valuation. We raised our earnings projection for FY24-26F by +25.7%/+36.5%/+43.3%, reflecting the recovery of global glove demand and infrastructure investment. This was after factoring in (1) higher TRP revenue, (2) better sales volume of gloves product, (3) higher margins per unit for gloves due to increased utilisation rates. We have also upgraded our valuation from a 2-year historical average P/BV of 0.89x to a 3-year historical +1SD P/BV of 1.52x, considering the positive mid-to-long-term outlook. We also brought forward our FY25 BVPS of 161 sen from the FY24F BVPS of 153 sen.

RETURN STATISTICS

| | |
|---------------------------------|------|
| Price @ 21st May 2024 (RM) | 2.44 |
| Expected share price return (%) | +0.5 |
| Expected dividend yield (%) | +1.0 |
| Expected total return (%) | +1.5 |

SHARE PRICE CHART



| Price performance (%) | Absolute | Relative |
|-----------------------|----------|----------|
| 1 month | 16.5 | 11.0 |
| 3 months | 26.7 | 17.1 |
| 12 months | 62.5 | 42.9 |


INVESTMENT STATISTICS

| FYE Dec (RM'm) | 2024F | 2025F | 2026F |
|--------------------|---------|---------|---------|
| Revenue | 1,958.4 | 2,310.8 | 2,529.9 |
| EBITDA | 204.8 | 320.0 | 371.4 |
| Profit Before Tax | 194.5 | 307.5 | 356.5 |
| Core PATANCI | 144.2 | 228.0 | 264.3 |
| Core EPS (sen) | 5.7 | 8.9 | 10.4 |
| DPS (sen) | 2.0 | 2.5 | 3.0 |
| Dividend Yield (%) | 0.8 | 1.0 | 1.2 |

KEY STATISTICS

| | |
|----------------------------------|----------|
| FBM KLCI | 1,622.09 |
| Issue shares (m) | 2551.62 |
| Estimated free float (%) | 40.15 |
| Market Capitalisation (RM'm) | 6,302.50 |
| 52-wk price range | RM1.27- |
| 3-mth average daily volume (m) | 5.70 |
| 3-mth average daily value (RM'm) | 12.67 |
| Top Shareholders (%) | |
| Kossan Holdings M Sdn Bhd | 35.00 |
| Employees Provident Fund Board | 5.65 |
| abrdrn plc | 5.41 |

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Upgrade to NEUTRAL (previously SELL) with a higher TP of RM2.45 (previously RM1.35). Our revised TP is based on FY25F BVPS of 161 sen (previously FY24F BVPS of 153 sen), pegged to a revised P/BV of 1.52x. We are optimistic about Kossan's FY24 outlook, considering the softer oversupply situation due to ongoing industry consolidation and capacity adjustments. This is further supported by recovering global glove demand for high-quality products following the replenishment of pandemic stockpiles and increased hygiene awareness in the medical and industrial sectors. Additionally, we anticipate better performance for TRP products in FY24, driven by growth in infrastructure sectors. However, we believe that ASP pressure from international competitors will persist, limiting the producers' ability to significantly raise substantial ASP hike. **Potential downside risks** include: (i) a slower or weaker-than-expected recovery in global glove demand; (ii) higher-than-expected production costs; and (iii) lower-than-expected TRP product sales. 

Kossan Rubber Industries: 1QFY24 Results Summary

| FYE Dec (RM's) | Quarterly results | | | | | Cumulative results | | |
|--------------------------------|-------------------|-------------|---------------|---------------------|---------------------|--------------------|---------------|---------------------|
| | 1QFY24 | 4QFY23 | 1QFY23 | YoY (%) | QoQ (%) | 3MFY24 | 3MFY23 | YoY (%) |
| Revenue | 451.6 | 400.1 | 394.7 | 14.4 | 12.9 | 451.6 | 394.7 | 14.4 |
| Operating expenses | (429.4) | (414.8) | (430.6) | (0.3) | 3.5 | (429.4) | (430.6) | (0.3) |
| Other operating income | 18.8 | 18.8 | 17.2 | 9.0 | 0.1 | 18.8 | 17.2 | 9.0 |
| Operating profit (EBIT) | 41.0 | 4.2 | (18.6) | >(100.0) | 883.2 | 41.0 | (18.6) | >(100.0) |
| Net finance income/(cost) | (0.1) | (0.7) | (0.4) | (87.1) | (92.2) | (0.1) | (0.4) | (87.1) |
| Profit before tax (PBT) | 41.0 | 3.4 | (19.1) | >(100.0) | >100.0 | 41.0 | (19.1) | >(100.0) |
| Taxation | (8.9) | (1.8) | (4.5) | 98.5 | >100.0 | (8.9) | (4.5) | 98.5 |
| Profit After tax (PAT) | 32.0 | 1.6 | (23.6) | >(100.0) | >100.0 | 32.0 | (23.6) | >(100.0) |
| PATANCI | 31.5 | 0.8 | (24.3) | >(100.0) | >100.0 | 31.5 | (24.3) | >(100.0) |
| Core PATANCI | 24.7 | 30.7 | (34.6) | >(100.0) | (19.6) | 24.7 | (34.6) | >(100.0) |
| Basic EPS (sen) | 1.2 | 0.0 | (1.0) | >(100.0) | >100.0 | 1.2 | (1.0) | >(100.0) |
| DPS (sen) | 0.0 | 2.0 | 0.0 | n.m. | (100.0) | 0.0 | 0.0 | n.m. |
| Growth & Margin (%) | | | | + / (-) ppts | + / (-) ppts | | | + / (-) ppts |
| Operating Profit Margin | 9.1 | 1.0 | (4.7) | 13.8 | 8.0 | 9.1 | (4.7) | 13.8 |
| PBT Margin | 9.1 | 0.9 | (4.8) | 13.9 | 8.2 | 9.1 | (4.8) | 13.9 |
| Core PATANCI Margin | 5.5 | 7.7 | (8.8) | 14.2 | (2.2) | 5.5 | (8.8) | 14.2 |
| Ratios & Valuation | | | | + / (-) ppts | + / (-) ppts | | | + / (-) ppts |
| Net cash/market cap (%) | 21.1 | 20.2 | 20.2 | 0.9 | 0.9 | 21.1 | 20.2 | 0.9 |
| Effective tax rate (%) | 21.8 | 53.5 | (23.6) | 45.4 | (31.7) | 21.8 | (23.6) | 45.4 |

Source: Company, MIDFR

Kossan Rubber Industries: Breakdown by operating segment

| FYE Dec (RM'm) | Quarterly results | | | | | Cumulative results | | |
|------------------------------------|-------------------|--------------|---------------|---------------------|---------------------|--------------------|---------------|---------------------|
| | 1QFY24 | 4QFY23 | 1QFY23 | YoY (%) | QoQ (%) | 3MFY24 | 3MFY23 | YoY (%) |
| Revenue (RM'm): | | | | | | | | |
| Gloves Division | 379.6 | 329.6 | 317.5 | 19.6 | 15.2 | 379.6 | 317.5 | 19.6 |
| Technical Rubber Division | 48.9 | 44.4 | 56.2 | (12.8) | 10.1 | 48.9 | 56.2 | (12.8) |
| Cleanroom Division | 23.0 | 26.1 | 21.0 | 9.6 | (11.8) | 23.0 | 21.0 | 9.6 |
| Total | 451.6 | 400.1 | 394.7 | 14.4 | 12.9 | 451.6 | 394.7 | 14.4 |
| Operating Profit (RM'm): | | | | | | | | |
| Gloves Division | 26.6 | (9.3) | (34.9) | >(100.0) | >(100.0) | 26.6 | (34.9) | >(100.0) |
| Technical Rubber Division | 8.9 | 10.0 | 7.9 | 12.7 | (10.7) | 8.9 | 7.9 | 12.7 |
| Cleanroom Division | 2.4 | 2.8 | 1.6 | 52.1 | (14.6) | 2.4 | 1.6 | 52.1 |
| Total | 41.0 | 3.4 | (19.1) | >(100.0) | >100.0 | 41.0 | (19.1) | >(100.0) |
| Operating profit margin (%) | | | | + / (-) ppts | + / (-) ppts | | | + / (-) ppts |
| Gloves Division | 7.0 | (2.8) | (11.0) | 18.0 | 9.8 | 7.0 | (11.0) | 18.0 |
| Technical Rubber Division | 18.2 | 22.5 | 14.1 | 4.1 | (4.3) | 18.2 | 14.1 | 4.1 |
| Cleanroom Division | 10.5 | 10.9 | 7.6 | 2.9 | (0.3) | 10.5 | 7.6 | 2.9 |
| Total | 9.1 | 0.9 | (4.8) | 13.9 | 8.2 | 9.1 | (4.8) | 13.9 |

Source: Company, MIDFR

FINANCIAL SUMMARY

| Income Statement (RM'm) | 2022A | 2023A | 2024F | 2025F | 2026F |
|--|----------------|----------------|----------------|----------------|----------------|
| Revenue | 2,343.8 | 1,591.0 | 1,958.4 | 2,310.8 | 2,529.9 |
| Raw materials and consumable used | (1,263.3) | (885.2) | (1,135.3) | (1,326.2) | (1,422.9) |
| Changes in inventories of finished goods & WIP | (71.7) | (33.4) | 22.6 | 52.6 | 36.9 |
| Goods purchased for resale | (57.9) | (31.9) | (39.3) | (46.4) | (50.8) |
| Gross Profit | 950.9 | 640.6 | 806.4 | 990.9 | 1,093.1 |
| Other (expense)/income | 44.1 | 47.5 | 24.4 | 28.8 | 31.5 |
| Staff costs | (374.5) | (299.2) | (314.1) | (329.9) | (346.3) |
| Other operating expenses | (304.6) | (252.1) | (311.8) | (369.8) | (406.9) |
| EBITDA | 315.9 | 136.8 | 204.8 | 320.0 | 371.4 |
| EBIT | 184.5 | (7.1) | 157.2 | 270.0 | 318.8 |
| Profit before tax (PBT) | 213.5 | 34.5 | 194.5 | 307.5 | 356.5 |
| Profit After tax (PAT) | 159.2 | 16.3 | 144.2 | 228.0 | 264.3 |
| Core PATANCI | 144.9 | 31.8 | 144.2 | 228.0 | 264.3 |
| Core EPS (sen) | 5.7 | 1.2 | 5.7 | 8.9 | 10.4 |
| DPS (sen) | 2.5 | 2.0 | 2.0 | 2.5 | 3.0 |

| Balance Sheet (RM'm) | 2022A | 2023A | 2024F | 2025F | 2026F |
|--------------------------------------|----------------|----------------|----------------|----------------|----------------|
| Property, plant and equipment | 1,356.9 | 1,294.4 | 1,296.5 | 1,322.3 | 1,381.9 |
| Intangible assets & Goodwill | 6.0 | 6.1 | 6.1 | 6.1 | 6.1 |
| Total Non-current assets | 1,470.6 | 1,402.7 | 1,414.2 | 1,451.4 | 1,522.7 |
| Inventories | 287.1 | 239.2 | 261.8 | 314.5 | 351.3 |
| ST - Trade and other receivables | 276.0 | 248.4 | 346.0 | 408.3 | 447.0 |
| Cash and cash equivalents | 1,348.0 | 1,271.3 | 1,284.0 | 1,296.9 | 1,309.8 |
| Total current assets | 2,856.5 | 2,799.6 | 2,982.6 | 3,165.0 | 3,313.0 |
| Total Assets | 4,327.1 | 4,202.3 | 4,396.8 | 4,616.4 | 4,835.7 |
| LT Loans and borrowings | 0.9 | 0.3 | 1.7 | 1.7 | 1.8 |
| LT Lease Liabilities | 5.8 | 4.9 | 6.0 | 7.1 | 7.8 |
| Total Non-current liabilities | 144.5 | 125.6 | 146.2 | 161.2 | 169.5 |
| ST Loans and borrowings | 71.3 | 10.2 | 66.2 | 68.2 | 70.2 |
| ST Trade and other payables | 200.2 | 192.0 | 218.1 | 254.8 | 273.4 |
| Total Current Liabilities | 284.7 | 213.7 | 296.8 | 336.3 | 357.5 |
| Total Liabilities | 429.2 | 339.3 | 443.0 | 497.5 | 527.1 |

| Cash Flow (RM'm) | 2022A | 2023A | 2024F | 2025F | 2026F |
|----------------------------|------------------|----------------|----------------|----------------|----------------|
| Pretax profit | 213.5 | 34.5 | 194.5 | 307.5 | 356.5 |
| Cash flow from operations | 93.4 | 202.8 | 20.8 | 117.7 | 168.2 |
| Cash flow from investing | (812.3) | (162.1) | (15.6) | (44.2) | (81.4) |
| Cash flow from financing | (480.9) | (129.8) | 7.5 | (60.7) | (73.8) |
| Net cash flow | (1,199.9) | (89.2) | 12.7 | 12.8 | 13.0 |
| Net cash/(debt) b/f | 2,557.8 | 1,348.0 | 1,271.3 | 1,284.0 | 1,296.9 |
| Net cash/(debt) c/f | 1,348.0 | 1,271.3 | 1,284.0 | 1,296.9 | 1,309.8 |

| Key Metrics | 2022A | 2023A | 2024F | 2025F | 2026F |
|--------------------------------|-------|-------|-------|-------|-------|
| Effective tax rate (%) | 25.4 | 52.8 | 25.9 | 25.9 | 25.9 |
| PER (x) | 39.6 | 469.2 | 43.2 | 27.3 | 23.6 |
| P/BV ratio (x) | 1.60 | 1.61 | 1.57 | 1.51 | 1.44 |
| Cash/Market Capitalisation (%) | 20.5 | 20.3 | 19.5 | 19.7 | 19.9 |
| Cash/share (sen) | 3.7 | 7.9 | 0.8 | 4.6 | 6.6 |

| Profitability Margins | 2022A | 2023A | 2024F | 2025F | 2026F |
|-------------------------|-------|-------|-------|-------|-------|
| Gross Profit Margin (%) | 40.6 | 40.3 | 41.2 | 42.9 | 43.2 |
| EBIT Margin (%) | 7.9 | (0.4) | 8.0 | 11.7 | 12.6 |
| Core PATANCI Margin (%) | 6.2 | 2.0 | 7.4 | 9.9 | 10.4 |

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