

Kossan Rubber Industries Berhad

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

Yet to Reach Supply-Demand Equilibrium

KEY INVESTMENT HIGHLIGHTS

- **Maintain NEUTRAL with a lower target price of RM1.89 post the 2QFY24 results announcement**
- **Slow demand recovery led to 1HFY24 earnings disappointment of RM52.0m only**
- **Near-term demand outlook remains challenging which is further compounded by competitive pricing from its oversea peers**
- **On the flip side, there is little risk of the group to be in a loss-making position again**

Pace of recovery to remain tepid. We are maintaining our **NEUTRAL recommendation** on Kossan with a lower target price of **RM1.89** (previously RM2.45) post the group's 2QFY24 results announcement. While the worst is over, we view the industry outlook remain challenging caused by supply-demand imbalance in the foreseeable term as well as competitive pricing by the international competitors. Given the prevailing landscape, we see minimal risk of the group to be loss-making. That being said, we do not foresee commendable growth in future earnings at this juncture.

Remain profitable. 2FY24 normalised earnings came in at RM27.3m, a reversal from a loss of -RM2.8m a year ago. This was mainly supported by stronger revenue of RM429.9m (+10.9%yoy). On this note, the higher revenue was contributed by all the division.

Below expectation. On a cumulative basis, 1HFY24 normalised earnings amounted to RM52.0m from a loss of -RM37.3m. This was mainly supported by +12.7%yoy recovery in revenue to RM881.5m as well as an active effort to enhance cost efficiency.

All in, Kossan's 1HFY24 financial performance came in below our expectation, making up only 36.1% of our full year FY24 earnings estimates. The variance mainly came from the weaker-than-expected recovery in demand.

A more conservative earnings estimate. Taking cue from the group's 2FY24 financial results, we are inputting a slower pace of demand recovery which in-turn affect the profit margin. These led to reduction in earnings estimates of between -24.1% to -46.9% for FY24 to FY26.

Shift in valuation methodology. While the supply-demand imbalance will persist, the overall landscape has become more favourable. This is in view of stabilising demand pattern post the pandemic period. Moreover, industry consolidation, capacity streamlining as well as exit of newer entrants has helped to combat the oversupply situation. As such, we do not expect the group would be loss-making in the foreseeable term. Thus, we take this opportunity to switch our valuation methodology to PER from PBV previously.

Maintain NEUTRAL

Revised Target Price: RM1.89
(Previously RM2.45)

RETURN STATISTICS

Price @ 22 nd August 2024 (RM)	2.04
Expected share price return (%)	-7.3
Expected dividend yield (%)	+1.2
Expected total return (%)	-6.1

SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	-16.2	-17.1
3 months	-11.9	-17.9
12 months	53.3	34.0

INVESTMENT STATISTICS

FYE Dec (RM'm)	2024F	2025F	2026F
Revenue	1,797.2	2,060.2	2,256.0
EBITDA	157.8	177.4	204.0
Profit Before Tax	147.6	164.9	189.2
Core PATANCI	109.4	122.3	140.3
Core EPS (sen)	4.3	4.8	5.5
DPS (sen)	2.0	2.5	3.0
Dividend Yield (%)	1.0	1.2	1.5

KEY STATISTICS

FBM KLCI	1,641.66
Issue shares (m)	2551.62
Estimated free float (%)	46.52
Market Capitalisation (RM'm)	5,281.85
52-wk price range	RM1.28 - RM2.83
3-mth average daily volume (m)	5.97
3-mth average daily value (RM'm)	13.17
Top Shareholders (%)	
Kossan Holdings M Sdn Bhd	35.00
Employees Provident Fund	12.74
abrdrn plc	5.10

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Revised target. Premised on the above, we are pegging FY25EPS of 4.8sen against target PER of 39.4x which is the two-year mean. This led to a revised target price of **RM1.89** (previously RM2.45).



Kossan Rubber Industries: 2QFY24 Results Summary

FYE Dec (RM's)	Quarterly results					Cumulative results		
	2QFY24	1QFY24	2QFY23	YoY (%)	QoQ (%)	1HFY24	1HFY23	YoY (%)
Revenue	429.9	451.6	387.5	10.9	(4.8)	881.5	782.3	12.7
Operating expenses	(409.0)	(429.4)	(401.8)	1.8	(4.7)	(838.4)	(832.4)	0.7
Other operating income	17.8	18.8	17.1	4.0	(5.6)	36.6	34.3	6.5
Operating profit (EBIT)	38.7	41.0	2.8	1,286.9	(5.8)	79.7	(15.8)	(603.1)
Net finance income/(cost)	(0.1)	(0.1)	(0.3)	(68.9)	37.9	(0.1)	(0.7)	(80.4)
Profit before tax (PBT)	38.6	41.0	2.5	1,424.6	(5.9)	79.6	(16.5)	(580.9)
Taxation	(6.4)	(8.9)	(5.2)	23.9	(28.1)	(15.4)	(9.7)	58.6
Profit After tax (PAT)	32.1	32.0	(2.7)	(1,310.3)	0.3	64.2	(26.2)	(344.7)
PATANCI	31.3	31.5	(3.3)	(1,050.3)	(0.4)	62.8	(27.6)	(327.9)
Core PATANCI	27.3	24.7	(2.8)	(1,088.1)	10.5	52.0	(37.3)	(239.3)
Basic EPS (sen)	1.2	1.2	(0.1)	(1,046.2)	0.0	2.5	(1.1)	(327.8)
DPS (sen)	0.0	0.0	0.0	n.m.	n.m.	0.0	0.0	n.m.
Growth & Margin (%)				+ / (-) ppts	+ / (-) ppts			+ / (-) ppts
Operating Profit Margin	9.0	9.1	0.7	8.3	(0.1)	9.0	(2.0)	11.1
PBT Margin	9.0	9.1	0.7	8.3	(0.1)	9.0	(2.1)	11.1
Core PATANCI Margin	6.4	5.5	(0.7)	7.1	0.9	5.9	(4.8)	10.7
Ratios & Valuation				+ / (-) ppts	+ / (-) ppts			+ / (-) ppts
Net cash/market cap (%)	24.5	25.2	23.6	1.0	(0.7)	24.5	23.6	1.0
Effective tax rate (%)	16.7	21.8	205.0	(188.3)	(5.1)	19.3	(58.6)	77.9

Source: Company, MIDFR

Kossan Rubber Industries: Breakdown by operating segment

FYE Dec (RM'm)	Quarterly results					Cumulative results		
	2QFY24	1QFY24	2QFY23	YoY (%)	QoQ (%)	1HFY24	1HFY23	YoY (%)
Revenue (RM'm):								
Gloves Division	353.0	379.6	315.9	11.8	(7.0)	732.6	633.4	15.7
Technical Rubber Division	49.9	48.9	47.8	4.4	2.0	98.9	104.0	(4.9)
Cleanroom Division	27.0	23.0	23.9	13.1	17.1	50.0	44.9	11.5
Total	429.9	451.6	387.5	10.9	(4.8)	881.5	782.3	12.7
Operating Profit (RM'm):								
Gloves Division	22.1	26.6	(12.1)	(282.9)	(16.9)	48.6	(47.0)	(203.6)
Technical Rubber Division	10.5	8.9	8.6	22.6	17.9	19.4	16.5	17.8
Cleanroom Division	2.5	2.4	2.4	3.9	2.0	4.9	4.0	23.2
Total	38.6	41.0	2.5	1,424.5	(5.9)	79.6	(16.5)	(580.9)
Operating profit margin (%)				+ / (-) ppts	+ / (-) ppts			+ / (-) ppts
Gloves Division	6.3	7.0	(3.8)	10.1	(0.7)	6.6	(7.4)	14.1
Technical Rubber Division	21.1	18.2	17.9	3.1	2.8	19.7	15.9	3.8
Cleanroom Division	9.2	10.5	10.0	(0.8)	(1.4)	9.8	8.9	0.9
Total	9.0	9.1	0.7	8.3	(0.1)	9.0	(2.1)	11.1

Source: Company, MIDFR

FINANCIAL SUMMARY

Income Statement (RM'm)	2022A	2023A	2024F	2025F	2026F
Revenue	2,343.8	1,591.0	1,797.2	2,060.2	2,256.0
Raw materials and consumable used	(1,263.3)	(885.2)	(1,021.8)	(1,206.5)	(1,321.2)
Changes in inventories of finished goods & WIP	(71.7)	(33.4)	(3.6)	22.5	24.5
Goods purchased for resale	(57.9)	(31.9)	(36.1)	(61.8)	(67.7)
Gross Profit	950.9	640.6	735.7	814.4	891.7
Other (expense)/income	44.1	47.5	22.4	25.7	28.1
Staff costs	(374.5)	(299.2)	(314.1)	(333.0)	(353.0)
Other operating expenses	(304.6)	(252.1)	(286.2)	(329.7)	(362.8)
EBITDA	315.9	136.8	157.8	177.4	204.0
EBIT	184.5	(7.1)	110.3	127.4	151.5
Profit before tax (PBT)	213.5	34.5	147.6	164.9	189.2
Profit After tax (PAT)	159.2	16.3	109.4	122.3	140.3
Core PATANCI	144.9	31.8	109.4	122.3	140.3
Core EPS (sen)	5.7	1.2	4.3	4.8	5.5
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	1,292.4	1,310.1	1,357.6
Intangible assets & Goodwill	6.0	6.1	6.1	6.1	6.1
Total Non-current assets	1,470.6	1,402.7	1,408.7	1,436.0	1,493.6
Inventories	287.1	239.2	235.7	258.2	282.7
ST - Trade and other receivables	276.0	248.4	317.5	364.0	398.6
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	2,927.9	3,064.3	3,195.8
Total Assets	4,327.1	4,202.3	4,336.6	4,500.3	4,689.4
LT Loans and borrowings	0.9	0.3	1.7	1.7	1.8
LT Lease Liabilities	5.8	4.9	5.5	6.3	6.9
Total Non-current liabilities	144.5	125.6	145.7	160.4	168.7
ST Loans and borrowings	71.3	10.2	66.2	68.2	70.2
ST Trade and other payables	200.2	192.0	196.3	231.8	253.8
Total Current Liabilities	284.7	213.7	274.5	312.7	337.3
Total Liabilities	429.2	339.3	420.3	473.1	506.0

Cash Flow (RM'm)	2022A	2023A	2024F	2025F	2026F
Pretax profit	213.5	34.5	147.6	164.9	189.2
Cash flow from operations	93.4	202.8	16.2	108.1	154.3
Cash flow from investing	(812.3)	(162.1)	(10.5)	(34.3)	(67.5)
Cash flow from financing	(480.9)	(129.8)	7.0	(60.9)	(73.9)
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)	33.1	392.3	47.6	42.6	37.1
P/BV ratio (x)	1.34	1.35	1.33	1.29	1.24
Cash/Market Capitalisation (%)	24.5	24.2	23.4	23.6	23.8
Cash/share (sen)	3.7	7.9	0.6	4.2	6.0

Profitability Margins	2022A	2023A	2024F	2025F	2026F
Gross Profit Margin (%)	40.6	40.3	40.9	39.5	39.5
EBIT Margin (%)	7.9	(0.4)	6.1	6.2	6.7
Core PATANCI Margin (%)	6.2	2.0	6.1	5.9	6.2

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