

16 December 2020

Kossan Rubber Industries

Just a Few Wrinkles

By Raymond Choo Ping Khoo | pkchoo@kenanga.com.my

We remain positive on Kossan's prospects in FY21 following a meeting with management together with other sell-side analysts. The highlights are as follow:- (i) minimal impact to bottom-line from COVID cases in its plants (ii) management is confident of sustained strong demand with orders filled up till end-CY21, with ASP playing catch-up in 4QFY20 and 1QFY21, and (iii) given that gloves shortage will likely persist until end-2021 and management's view that a decline in ASP in 2022, if any, is expected to be gradual driven by re-stocking activities. We maintain our target price of RM9.36 based on 11x FY21 EPS. Reiterate OP.

Hit by COVID infections but minimal impact to FY20E net profit. The group conducted a voluntary COVID-19 screening test in its Glove division from Dec 4 to Dec 10. Out of a total of 7,004 workers, five out of six locations registered zero cases with only one site reporting 427 positive cases out of 2,104 employees. The factory stopped operations for sanitisation which has been completed. Presently, the 1,667 workers are undergoing quarantine and will undergo a 2nd round of test on 16 and 17 Dec and the results are expected to be out on Dec 18. Thereafter, the group will undergo random sampling for antigen test due to asymptomatic symptoms in every two weeks (20% of workers). The operation is expected to gradually ramp up productions by Dec 20. The temporary loss in production comprised 25% of total output volume for two weeks which is expected to impact FY20E bottom-line by 2%.

ASP to rise in 4QFY20 and 1QFY21. The group is confident of sustained strong demand with orders filled up till end-CY21, reassuring us that lag impact from ASP hike will be felt in 4Q 2020 (50% QoQ) and 1Q 2021 (+30% QoQ). Management highlighted that it is difficult to predict when ASP will retrace but they stopped short of believing ASP hikes will gradually ease sometime in 4Q 2020, but more likely a case in 2022 (rather than facing a steep decline) depending on the outcome of the effectiveness of COVID vaccines. A retracement in ASP then, if any, would likely in their view, be gradual to be driven by restocking activities.

Planned capacity expansion. The planned capacity over the next two years are: (i) Plant 20 located adjacent to Plant 18 and 19 with 1.4b pieces capacity is expected to come on stream by early 2021, (ii) recently acquired land in Meru adjacent to one of its current plants is earmarked for a single plant with 5b pieces capacity and to be completed in two phases i.e. Phase 1 – 6 lines, 2b pieces commence in 2H 2021 and Phase 2 – 10 lines, 3b pieces commence in 1H 2022, and (iii) Bidor – 12 lines with 4b pieces capacity to fully commission in 2H 2022.

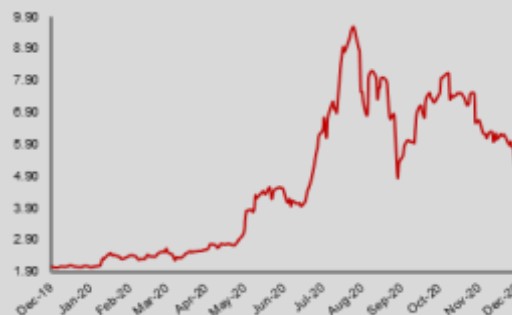
Maintain OP. We highlight that to reduce the spread of COVID-19 infection; vaccine coverage should reach at 60%-70% to build some form of herd immunity. Typically, herd immunity occurs when enough people in a population develop protection against a disease that it can no longer spread easily among them. Elsewhere, to scale up production of vaccines and distribution could pose a challenge which means the pandemic is likely to remain over the medium term. We maintain our target price of RM9.36 based on 11x FY21 EPS. Reiterate OP.

Key risk to our call is lower-than-expected ASP and demand beyond FY21.

OUTPERFORM ↔

Price : RM4.90
Target Price : RM9.36 ↔

Share Price Performance



KLCI	1,674.02
YTD KLCI chg	5.4%
YTD stock price chg	135.6%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	KRI MK Equity
Market Cap (RM m)	12,533.6
Shares Outstanding	2,557.9
52-week range (H)	9.75
52-week range (L)	2.05
3-mth avg daily vol:	10,668,780
Free Float	39%
Beta	0.8

Major Shareholders

Kossan Holdings Sdn Bhd	46.9%
Employees Provident Fund	8.8%
KWAP	2.4%

Summary Earnings Table

FY Dec (RM m)	2019A	2020E	2021E
Turnover	2221.6	3841.1	6144.0
PBT	280.1	1269.8	2786.8
Net Profit (NP)	224.8	1029.7	2176.7
Consensus (NP)	-	1014.8	2072.6
Earnings Revision	-	-	-
Core EPS (sen)	8.8	40.3	85.1
Core EPS growth (%)	12.0	358.1	111.4
NDPS (sen)	6.0	10.0	25.0
BVPS (RM)	0.56	0.86	1.46
Core PER (x)	55.8	12.2	5.8
Price/BV (x)	8.8	5.7	3.4
Net Gearing (%)	28.2	5.6	Net cash
Net Div. Yield (%)	1.2	2.0	5.1



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Income Statement

FY Dec (RM m)	2017A	2018A	2019A	2020E	2021E
Revenue	1957	2144	2183	3841.1	6144
EBITDA	309.6	344.4	393.0	1382.8	2893
Depn. & Amort	-72.1	-77.0	-83.1	-103.9	-110.2
Operating Profit	237.5	267.4	309.9	1278.9	2783
PBT	229.6	249.3	291.5	1269.8	2787
Taxation	-44.0	-44.0	-58.3	-234.7	-601
MI	-1.6	-4.5	-4.6	-5.4	-8.7
Net Profit	183.9	200.8	228.6	1029.7	2177

Balance Sheet

FY Dec (RM m)	2017A	2018A	2019A	2020E	2021E
Fixed Assets	1,028	1,266	1,398	1,534	1,664
Int. Assets	4.9	4.9	6.6	6.6	6.6
Other FA	8.5	8.4	18.1	7.0	7.0
Inventories	206.2	251.6	324.5	561.1	897.5
Receivables	341.1	405.9	404.9	700.0	1,120
Other CA	48.9	37.6	30.4	50.9	80.0
Cash	208.0	143.1	162.9	442.8	1,332
Total Assets	1,846	2,117	2,345	3,302	5,106
Payables	185.1	191.5	249.1	430.7	688.9
ST Borrowings	206.8	242.4	392.9	393.0	392.9
Ot. ST Liability	(3.9)	(16.0)	(19.9)	(19.8)	(19.7)
LT Borrowings	187.0	264.4	172.3	172.3	172.3
Ot. LT Liability	87.5	89.7	92.2	92.2	92.2
Minorities Int.	26.7	28.9	31.7	33.0	41.7
Net Assets	1,157	1,317	1,427	2,201	3,738
Share Capital	319.7	323.9	323.9	323.9	323.9
Reserves	836.5	992.6	1,103	1,877	3,415
Equity	1,156	1,317	1,427	2,201	3,739

Cashflow Statement

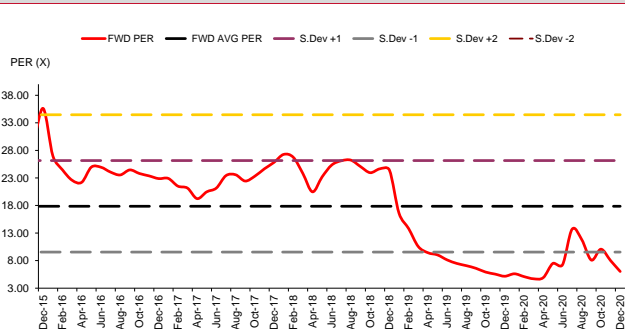
FY Dec (RM m)	2017A	2018A	2019A	2020E	2021E
Operating CF	123.0	135.7	183.0	768.5	1,767
Investing CF	(121)	(315)	(224)	(200.0)	(200)
Financing CF	98.3	112.2	58.4	(288.7)	(679)
Change In Cash	100.2	(67.1)	16.6	279.8	889
Free CF	33.0	35.7	83.0	568.5	1,569

Financial Data & Ratios

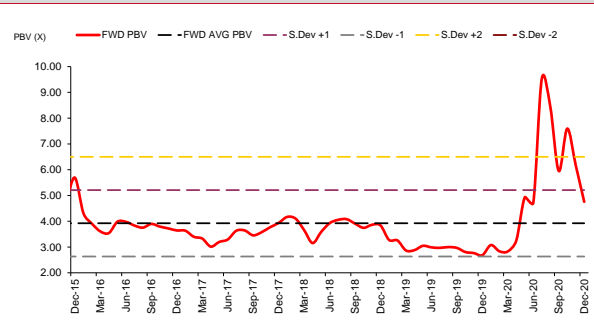
FY Dec	2017A	2018A	2019A	2020E	2021E
Growth (%)					
Turnover	17.4%	9.5%	3.6%	72.9%	60.0%
EBITDA	8.3%	11.3%	11.5%	259.9%	109%
Operating Profit	9.7%	12.6%	9.5%	336.5%	117%
PBT	9.3%	8.6%	12.3%	353.3%	119%
Net Profit /(loss)	10.1%	9.2%	12.0%	358.1%	111%
Profitability (%)					
EBITDA Margin	15.8%	16.1%	17.3%	36.0%	47.1%
Operating Margin	12.1%	12.5%	13.2%	25.0%	33.3%
PBT Margin	11.7%	11.6%	12.6%	33.1%	45.4%
Core Net Margin	9.4%	9.4%	10.1%	26.8%	35.4%
Eff. Tax Rate	23.7%	21.4%	20.0%	18.5%	21.6%
ROA	10.0%	9.5%	9.6%	31.2%	42.6%
ROE	15.9%	15.3%	15.8%	46.8%	58.2%
DuPont Analysis					
Net Margin (%)	9.4%	9.4%	10.1%	26.8%	35.4%
Assets T/O (x)	0.9	1.0	1.1	0.9	0.8
Lev. Factor (x)	1.6	1.6	1.6	1.5	1.4
ROE (%)	15.9%	15.3%	15.8%	46.8%	58.2%
Leverage					
Debt/Asset (x)	0.2	0.2	0.2	0.2	0.1
Debt/Equity (x)	0.3	0.4	0.4	0.3	0.2
Valuations					
EPS (sen)	14.4	15.7	17.6	40.3	85.1
NDPS (sen)	6.0	6.0	6.0	10.0	25.0
BVPS (RM)	0.90	1.03	1.12	0.86	1.46
PER (x)	68.1	62.4	55.8	12.2	5.8
Net Div. Yld (%)	0.4	1.2	1.2	1.2	2.0
PBV	10.8	9.5	8.8	5.7	3.4

Source: Kenanga Research

Fwd PER Band



Fwd PBV Band



Source: Kenanga Research, Bloomberg

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Peer Comparison

Name	Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.			
RUBBER GLOVES																	
HARTALEGA HOLDINGS BHD	11.98	41,063	Y	03/2021	158%	48%	564%	75.7%	87.4	14.1	8.0	15.9	11.0	92.6%	4.3%	26.22	OP
KOSSAN RUBBER INDUSTRIES	4.90	12,533	Y	12/2020	72.9%	60%	358%	111%	55.8	12.2	5.8	8.8	5.7	56.8%	2.0%	9.36	OP
SUPERMAX CORP BHD	6.79	17,829	Y	06/2021	229%	-27%	510%	-41%	35.6	5.8	10.0	11.6	5.3	125%	6.9%	12.00	OP
TOP GLOVE CORP BHD	6.41	51,400	Y	08/2021	205%	-39%	400%	-56%	28.1	5.6	12.8	10.5	5.9	134%	9.0%	10.68	OP

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my

