

28 July 2021

# Kossan Rubber Industries

## 1HFY21 Impacted by Lower-than-expected Volume Sales

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1HFY21 Core PATAMI of RM2,182m (+10-fold YoY) came in below expectations at 59%/66% of our/consensus full-year forecasts. The negative variance from our forecast is due to lower-than-expected volume sales. As such, we lower our FY21E net profit by 8%, taking into account a lower utilisation rate but maintain FY22E earnings forecast. In our view, the anticipated ASP weakness is already discounted by the share price. However, we conservatively lowered our TP from RM5.84 to RM5.00 based on 10x CY22E EPS (at -1.0SD below 5-year forward historical mean). Reiterate OP.

**Key results' highlights.** QoQ, 2QFY21 revenue rose 2% due to higher contribution from rubber gloves (+95% of total revenue) as higher ASP(+5%-7%) was negated by lower volume sales (-4%). This brings 2QFY21 core net profit to RM1,089m (-0.2%). A 2<sup>nd</sup> interim DPS of 12.0 sen was declared bringing 1HFY21 DPS to 24.0 sen which came in within our expectation.

**YoY,** 1HFY21 revenue rose 237% due to higher contribution from glove division (+256%), underpinned by higher volume sales (+5%) and ASP(+250%). This elevated 1HFY21 core net profit to RM2,182m (+10-fold).

**Outlook.** In our view, at current price levels, the weakness reflects an overly bearish reaction to expected decline in ASP in subsequent quarters ahead. We expect gloves players' to benefit from weakening of the RM against the USD over the short to medium-term. YTD average USDMYR is RM4.11 compared to the current RM4.23. Since sales are USD-denominated, theoretically, a depreciating ringgit against the dollar will lead to more revenue receipts for glove makers. Overall, the group expect ASPs to decline gradually underpin by sustained demand post pandemic. Note that delivery lead time for certain industry players have been reduced, suggesting lower nitrile ASP ahead. The group is confident of strong demand being sustained with orders lined up till end-CY21 while capacity ramp-up is on track to commence gradually, staggered throughout Oct, Nov, and Dec. In the meantime, the planned capacity expansion over the next two years are as follows:- (i) Plant 20 located adjacent to Plants 18 and 19 with 1.5b pieces capacity which is expected to come on stream by early 2021 – 2 lines from Plant 18 have commenced production, (ii) a recently acquired land in Meru located adjacent to one of its current plants is earmarked for a single plant with 5b pieces capacity to be completed in two phases i.e. Phase 1 – 6 lines, 2b pieces commencing in 2H 2021 and Phase 2 – 10 lines, 3b pieces commencing in 1H 2022, and (iii) 12 lines with 4b pieces capacity to fully commission in 2HCY22 in Bidor. Upon completion, these three new plants will bring the group's total installed capacity from 32b to 42.4b (+33%) pieces of gloves per annum.

**Lowered our FY21E net profit by 8%** as we factor in lower utilisation rate to 90% from 98% into our earnings model. Our FY22E ASP assumption remains at USD40/1,000 pieces.

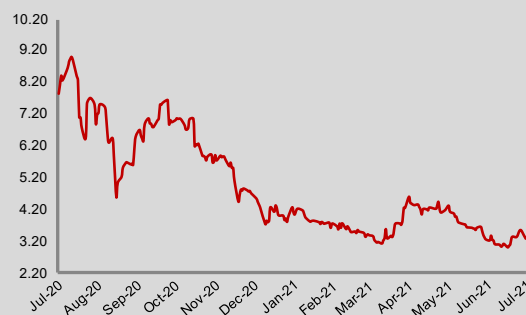
**Maintain OP.** However, we conservatively lowered our TP from RM5.84 to RM5.00 based on 10x CY22E EPS (at -1.0SD below 5-year forward historical mean) (previously 11.7x). Our target PER is at a 50% discount to normalised 5-year pre-COVID-19 historical forward mean averaging 15-18x. We still see significant value in Malaysian glove players which command 65-68% of global market share and have consistently evolve and innovate in terms of products and plant modernization via automations.

**Key risks to our call include:** (i) ASP falling steeper and sooner than expected and (ii) faster-than-expected vaccine roll-outs.

# OUTPERFORM ↔

Price: **RM3.29**  
Target Price: **RM5.00 ↓**

### Share Price Performance



|                     |          |
|---------------------|----------|
| KLCI                | 1,514.60 |
| YTD KLCI chg        | -6.9%    |
| YTD stock price chg | -25.3%   |

### Stock Information

|                      |               |
|----------------------|---------------|
| Shariah Compliant    | Yes           |
| Bloomberg Ticker     | KRI MK Equity |
| Market Cap (RM m)    | 8,394.8       |
| Shares Outstanding   | 2,551.6       |
| 52-week range (H)    | 9.54          |
| 52-week range (L)    | 2.93          |
| 3-mth avg daily vol: | 7,441,340     |
| Free Float           | 39%           |
| Beta                 | 0.8           |

### Major Shareholders

|                          |       |
|--------------------------|-------|
| Kossan Holdings SdnBhd   | 47.1% |
| Employees Provident Fund | 8.8%  |
| KWAP                     | 2.4%  |

### Summary Earnings Table

| FY Dec (RMm)           | 2020A         | 2021E         | 2022E         |
|------------------------|---------------|---------------|---------------|
| Turnover               | 3653.5        | 7542.9        | 4986.4        |
| PBT                    | 1444.6        | 4307.1        | 1642.8        |
| <b>Net Profit (NP)</b> | <b>1087.1</b> | <b>3366.2</b> | <b>1280.8</b> |
| Consensus (NP)         | -             | 3298.7        | 1054.3        |
| Earnings Revision      | -             | -8%           | -             |
| Core EPS (sen)         | 40.5          | 131.6         | 50.1          |
| Core EPS growth (%)    | 361.2         | 224.7         | (62.0)        |
| NDPS (sen)             | 14.0          | 35.0          | 15.0          |
| BVPS (RM)              | 0.93          | 1.90          | 2.25          |
| Core PER (x)           | 7.7           | 2.5           | 6.6           |
| Price/BV (x)           | 3.5           | 1.7           | 1.5           |
| Net Gearing (%)        | N.Cash        | N.Cash        | N.Cash        |
| Net Div. Yield (%)     | 4.3           | 10.6          | 4.6           |

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## Result Highlight

|                          | 2Q                   | 1Q                   | Q-o-Q | 2Q    | Y-o-Y | 6M      | 6M      | Y-o-Y   |
|--------------------------|----------------------|----------------------|-------|-------|-------|---------|---------|---------|
| FY Dec (RM m)            | FY21                 | FY21                 | Chg % | FY20  | Chg % | FY20    | FY21    | Chg %   |
| Turnover                 | 2,238.0              | 2,192.1              | 2.1   | 701.7 | 219.0 | 1,313.1 | 4,430.2 | 237.4   |
| EBITDA                   | 1,432.8              | 1,403.3              | 2.1   | 188.8 | 658.9 | 299.4   | 2,836.1 | 847.1   |
| PBT                      | 1,403.7              | 1,373.5              | 2.2   | 160.8 | 772.8 | 243.4   | 2,777.3 | 1,041.2 |
| PATAMI (NP)              | 1,064.8              | 1,041.8              | 2.2   | 131.1 | 712.5 | 195.9   | 2,106.7 | 975.6   |
| Core PATAMI <sup>^</sup> | 1,089.8 <sup>^</sup> | 1,091.8 <sup>*</sup> | -0.2  | 131.1 | 712.5 | 195.9   | 2,181.6 | 1,013.6 |
| EPS (sen)                | 41.6                 | 40.8                 | 2.4   | 5.1   | 712.6 | 7.7     | 82.4    | 975.8   |
| EBITDA margin (%)        | 64.0                 | 64.0                 |       | 26.9  |       | 22.8    | 64.0    |         |
| PBT margin (%)           | 62.7                 | 62.7                 |       | 22.9  |       | 18.5    | 62.7    |         |
| NP margin (%)            | 47.6                 | 47.5                 |       | 18.7  |       | 14.9    | 47.6    |         |
| Effective tax rate (%)   | 24.1                 | 24.1                 |       | 17.7  |       | 18.8    | 24.1    |         |

Source: Kenanga Research, Bursa Malaysia

<sup>\*</sup>excluding one-off contribution towards COVID-19 vaccination (RM50m)<sup>^</sup>excluding one-off balance workers remediation fees (RM25m)

## Quarterly segmental breakdown

|  | 1Q21    | 2Q21    | Chg %  | 6M      | 6M      | Chg %   |
|--|---------|---------|--------|---------|---------|---------|
|  |         |         | q-o-q  | FY20    | FY21    | y-o-y   |
| <b>Revenue (RM m)</b>                    |         |         |        |         |         |         |
| Gloves division                          | 2,092.9 | 2,124.7 | 1.5    | 1,178.8 | 4,217.6 | 257.8   |
| Technical rubber products (TRP) division | 41.5    | 50.4    | 21.3   | 63.5    | 91.9    | 44.7    |
| Cleanroom products division              | 56.3    | 61.2    | 8.6    | 70.1    | 117.5   | 67.6    |
| Investment Holding                       | 1.3     | 1.8     | 32.0   | 0.7     | 3.1     | 340.0   |
| Total                                    | 2,192.1 | 2,238.0 | 2.1    | 1,313.1 | 4,430.2 | 237.4   |
| <b>Pre-tax profit (RM m)</b>             |         |         |        |         |         |         |
| Gloves division                          | 1,354.7 | 1,384.3 | 2.2    | 227.7   | 2,739.0 | 1,102.7 |
| Technical rubber products (TRP) division | 8.9     | 6.9     | (22.9) | 5.0     | 15.8    | 218.4   |
| Cleanroom products division              | 11.5    | 13.7    | 18.7   | 10.4    | 25.1    | 141.6   |
| Investment Holding                       | (1.6)   | (1.1)   | (27.4) | 0.2     | (2.7)   | NM      |
| Total                                    | 1,373.5 | 1,403.7 | 2.2    | 243.4   | 2,777.3 | 1,041.2 |
| <b>Pre-tax profit margin (%)</b>         |         |         |        |         |         |         |
| Gloves division                          | 65      | 65      |        | 19      | 65      |         |
| Technical rubber products division       | 22      | 14      |        | 8       | 17      |         |
| Cleanroom products division              | 20      | 22      |        | 15      | 21      |         |

Source: Kenanga Research, Bursa Malaysia

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## Peer Comparison

| Name                     | Last Price (RM) | Market Cap (RM'm) | Shariah Compliant | Current FYE | Revenue Growth |            | Core Earnings Growth |            | PER (x) - Core Earnings |            |            | PBV (x) |            | ROE (%)    | Net DivYld (%) | 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. |                |                   |        |
| <b>RUBBER GLOVES</b>     |                 |                   |                   |             |                |            |                      |            |                         |            |            |         |            |            |                |                   |        |
| HARTALEGA HOLDINGS BHD   | 7.30            | 24,947            | Y                 | 03/2022     | 129%           | 47%        | 45%                  | -33%       | 8.6                     | 5.9        | 8.9        | 5.0     | 3.7        | 72%        | 10%            | 13.80             | OP     |
| KOSSAN RUBBER INDUSTRIES | 3.29            | 8,394             | Y                 | 12/2021     | 106%           | -34%       | 210%                 | -62%       | 7.7                     | 2.5        | 6.6        | 3.5     | 1.7        | 93%        | 11%            | 5.00              | OP     |
| SUPERMAX CORP BHD        | 3.34            | 8,742             | Y                 | 06/2021     | 244%           | -26%       | 630%                 | -47%       | 17.5                    | 2.4        | 4.5        | 5.7     | 2.2        | 133%       | 14%            | 6.49              | OP     |
| TOP GLOVE CORP BHD       | 4.00            | 32,018            | Y                 | 08/2021     | 157%           | -28%       | 395%                 | -56%       | 17.5                    | 3.5        | 8.0        | 6.6     | 4.5        | 150%       | 19%            | 5.60              | 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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