

02 April 2024

KAREX

A Postcard from Hat Yai

By Cheow Ming Liang | cheowml@kenanga.com.my

We visited KAREX's plant in Hat Yai, Thailand, which has access to labour and input latex at lower costs and enjoys attractive investment allowances and a lower corporate tax, as compared to its three plants in Malaysia. KAREX's plan to put onto the market a new product, i.e. synthetic condoms, is on track. We maintain our forecasts, TP of RM1.06 and OUTPERFORM call.

We recently visited Karex's manufacturing plant in Hat Yai, Thailand, which reinforces our optimism on its outlook. The key takeaways are as follows:

- Background.** The plant is the largest of KAREX's total four plants with the remaining in Port Klang, Pontian, and Senai, Malaysia. This Thai plant boasts 25 manufacturing lines with a capacity of 2.5 billion pieces annually. It employs approximately 1.5k Thai workers, making up about 44% of KAREX's total workforce. Note that, the group has zero migrant worker in both its Thai and Malaysian plants, which will spare it from forced labour issues that plagued certain glove producers in recent years. In addition to its core products of condoms and personal lubricants, the plant has also initiated two nitrile glove lines, being part of its plan to eventually boast an annual capacity of 500 million pieces. KAREX does not intend to produce mass-market gloves but specialised ones to complement the needs of its existing clients.

KAREX's rationales for setting up this plant include access to labour and input latex at lower costs, a lower corporate tax rate of 20% (vs. 24% in Malaysia) and attractive investment allowances.

- Synthetic condoms pending CE certification.** KARE remains upbeat on its high-margin new product, i.e. synthetic condoms, which is thinner (and thus require less material to produce) with improved heat sensitivity (which may boost customer satisfaction resulting in repeat purchases). It is currently engaging with key OEM clients with a product launch targeted in FY25. It plans to add five more dipping lines in its Thai plant (from only two lines for the entire group at present), boosting its annual capacity by 2.5x from c.200 million pieces at present to c.700 million pieces by CY24. It remains hopeful to secure CE certification (compliance with EU safety, health and environmental protection requirements) by June 2024, followed by US FDA approval in 1HFY25.

- Enhancing operational efficiency.** KAREX is enhancing efficiency in its tender business (which accounted for c.16% to the group's 1HFY24 turnover) by automating testing process to handle standardized client orders. The firm has already deployed five automated electronic testing machines (see Exhibit 4) in its plants in Thailand and Klang, with a testing rate of exceeding 200 pieces per minute (vs. 40 pieces per minute if done manually, see Exhibit 5). Additionally, a planned 2.5MW solar installation at its Thai plant, accounting for 45% of its total manufacturing capacity, is expected to reduce the plant's energy bills by 30% to 50% over the long-term.

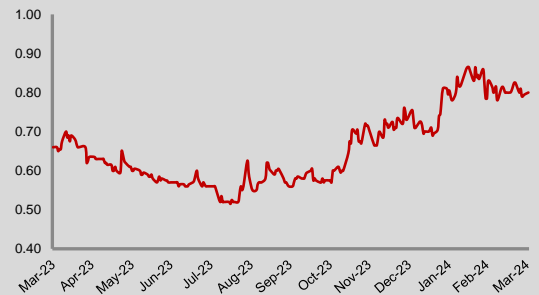
Forecasts. Maintained.

Valuations. We also keep our TP of RM1.06 based on an unchanged FY25F targeted PER of 25x, at a 20% premium to the average historical 5-year forward PER of its international peers to reflect its dominant market position and strong growth prospect. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 6).

OUTPERFORM ↔

Price: **RM0.800**
Target Price: **RM1.06** ↔

Share Price Performance



KLCI	1,544.02
YTD KLCI chg	6.1%
YTD stock price chg	9.6%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	KAREX MK EQUITY
Market Cap (RM m)	842.8
Shares Outstanding	1,053.5
52-week Range (H)	0.88
52-week Range (L)	0.51
3-mth Avg.Daily Vol.:	2,006,423
Free Float	25%
Beta	0.9

Major Shareholders

Karex One Ltd	17.5%
Bnp Paribas	16.9%
Maryen Holdings Limi	11.5%

Summary Earnings Table

FY Jun (RM m)	2023A	2024F	2025F
Turnover	532	589	669
EBIT	22	41	69
PBT	15	32	60
Net Profit	10	24	44
Consensus		24	44
Earnings Revision	-	-	-
EPS (sen)	1.0	2.2	4.2
EPS Growth (%)	269	126	88
NDPS (sen)	0.5	0.5	0.9
BVPS (RM)	0.45	0.47	0.50
Core PER (x)	80.4	35.6	19.0
Price/BV (x)	1.8	1.7	1.6
Net Gearing (x)	-0.3	-0.2	-0.1
Net Div. Yield (%)	0.6	0.6	1.1

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Investment case. We continue to like KAREX for: (i) its leading market position and global reach in the rapidly growing condom industry, projected by industry experts at a CAGR of 8% to 9% over the immediate term; (ii) its strong R&D and product innovation; (iii) its adherence to international standards and certifications, (iv) its strategic shift in moving up higher the value chain, and (v) post-pandemic market recovery and changing consumer preferences, especially in markets like China, and growing preference for high quality innovative condom products. Maintain **OUTPERFORM**.

Risks to our call include: (i) reduced spending by governments around the world on birth control, (ii) lower acceptance rate for its new synthetic rubber condoms, (iii) less favourable product mix, and (iv) inability to raise prices to safeguard profit margins.

Exhibit 1: Karex’s Plant in Thailand



Source: KAREX, Kenanga Research, Google

Exhibit 2: Rubber Compounding Section



Source: KAREX, Kenanga Research

Exhibit 3: Rubber Compounding Section



Source: KAREX, Kenanga Research

Exhibit 4: Automatic Electric Testing Machine



Source: KAREX, Kenanga Research

Exhibit 5: Manual Testing



Source: KAREX, Kenanga Research

Exhibit 6: Packing Process



Source: KAREX, Kenanga Research

Exhibit 7: Glove Manufacturing Lines



Source: KAREX, Kenanga Research

Exhibit 8: Synthetic Condom Manufacturing Plant



Source: KAREX, Kenanga Research

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Peer Comparison

Name	Rating	Last Price at 1-Apr (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)		Net Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	
CONSUMER																		
AEON CO. (M) BHD	UP	1.10	1.00	-9.1%	1,544.4	Y	12/2024	8.3	8.4	1.2%	2.1%	13.3	13.0	0.8	6.2%	4.0	3.6%	
DUTCH LADY MILK INDUSTRIES BHD*	OP	32.50	26.90	-17.2%	2,080.0	Y	12/2024	123.1	126.3	9.4%	2.5%	26.4	25.7	4.3	17.1%	50.0	1.5%	
FRASER & NEAVE HOLDINGS BHD	OP	29.38	33.80	15.0%	10,776.0	Y	09/2024	150.2	155.7	13.8%	3.6%	19.6	18.9	3.0	16.0%	77.0	2.6%	
MR D.I.Y. GROUP (M) BHD	OP	1.49	1.75	17.4%	14,077.0	Y	12/2024	7.0	7.8	17.6%	12.2%	21.4	19.1	6.9	34.8%	4.0	2.7%	
NESTLE (MALAYSIA) BHD	UP	118.10	115.00	-2.6%	27,694.5	Y	12/2024	290.8	305.0	3.3%	4.9%	40.6	38.7	42.4	102.7%	300.0	2.5%	
PADINI HOLDINGS BHD	UP	3.45	3.20	-7.2%	2,269.8	Y	06/2024	23.0	26.7	-31.9%	15.7%	15.0	12.9	2.0	14.0%	10.0	2.9%	
POWER ROOT BHD	UP	1.64	1.55	-5.5%	756.7	Y	03/2024	10.2	11.6	-25.0%	13.4%	16.0	14.1	2.4	15.0%	8.0	4.9%	
QL RESOURCES BHD	MP	5.90	6.25	5.9%	14,358.6	Y	03/2024	17.8	19.5	25.2%	9.2%	33.1	30.3	4.9	17.0%	9.0	1.5%	
KAREX BHD	OP	0.800	1.06	32.5%	842.8	Y	06/2024	2.3	4.2	125.7%	87.8%	35.5	18.9	1.7	4.9%	0.5	0.6%	
SECTOR AGGREGATE					74,399.7					8.3%	8.3%	27.1	25.0	5.5	20.2%		2.5%	

Source: Bloomberg, Kenanga Research

*Under Review

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Stock ESG Ratings:

	Criterion	Rating			
GENERAL	ESG Framework & Policies	★	★	★	★
	Earnings Sustainability & Quality	★	★	★	★
	Balance Sheet	★	★	★	★
	Community Investment	★	★	★	★
	Workers Safety & Wellbeing	★	★	★	★
	Corporate Governance	★	★	★	
SPECIFIC	Product Quality & Safety	★	★	★	☆
	Effluent & Waste Management	★	★	★	☆
	Digitalisation & Innovation	★	★	★	☆
	Supply Chain Management	★	★	★	☆
	Energy Efficiency	★	★		
OVERALL		★	★	★	

☆ denotes half-star
 ★ -10% discount to TP
 ★★ -5% discount to TP
 ★★★ TP unchanged
 ★★★★ +5% premium to TP
 ★★★★★ +10% premium to TP

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