

23 May 2024

# KAREX

## Earnings Driven by Margin Expansion

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**KAREX's 9MFY24 results beat our forecast. Its 9MFY24 net profit almost tripled driven by strong margins on an improved product mix. Its outlook will be buoyed by the roll-out of high-margin synthetic products. We raise our FY24-25F net profit forecasts by 5% and 4%, respectively, lift our TP by 4% to RM1.10 (from RM1.06) and maintain our OUTPERFORM call.**

KAREX's 9MFY24 net profit of RM18.6m surpassed our expectation, coming in at 79% of our full-year forecast (consensus estimate is not available in the absence of coverage apart from ourselves). The key variance against our forecast came from a better-than-expected product mix, resulting in higher margins. It surprised the market with a 0.5 sen dividend, bringing YTD DPS to 1.0 sen (compared to our previous estimate of 0.5 sen). Consequently, we raise our full-year DPS forecast to 1.0 sen, translating into a payout of 42% (KAREX has a dividend payout policy of at least 25%).

**YoY**, its 9MFY24 top line fell 3% primarily due to weakness in the tender market, partially cushioned by robust demand for personal lubricants. This is reflective of its conscious decision to shift its focus away from the less steady and less lucrative tender market (of which funding comes predominantly from humanitarian aid programmes and has been affected by regime changes in certain third-world countries). However, its net profit almost tripled driven by a higher gross margin of 33.2% (from 25.4% a year ago) on an improved product mix and stabilised input cost, efficiency gains and favourable exchange rates.

**QoQ**, its 3QFY24 top line was flattish as higher condom sales in the tender market (on the delivery of order backlogs from previous quarters) was offset by lower sales of lubricants and probe covers in the commercial market. Its net profit declined by 18% as gross profit margin softened to 33.7% (vs. 35.3% previously) on a less favourable product mix.

**Outlook.** KAREX is poised to benefit significantly from the increase in global condom demand, projected by industry experts at a CAGR of 8%-9% over the coming decade. It is riding on the trend towards premium products that fetch higher margins. In addition, it is benefitting from the more benign input and freight costs. It is also poised to obtain the CE certification (compliance with EU safety, health and environmental protection requirements) by Jun 2024 and US FDA approval in 1HFY25 for its new synthetic condom products, which should start to contribute from 2HFY25.

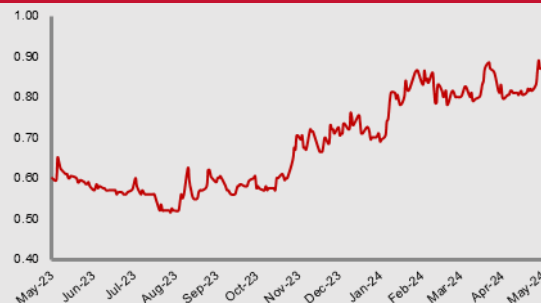
**Forecasts.** We cut our FY24-25F turnover projections by 13% and 16% respectively to reflect lower sales in the tender market. However, we raise our FY24-25F net profit forecasts by 5% and 4%, respectively, after incorporating a higher gross profit margin of 33% (previously 30%) due to a favourable product mix.

**Valuations.** Consequently, we raise our TP by 4% to RM1.10 (from 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 prospects. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

# OUTPERFORM ↔

Price : RM0.860  
Target Price : RM1.10 ↑

### Share Price Performance



KLCI	1,622.09
YTD KLCI chg	11.5%
YTD stock price chg	17.8%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	KAREX MK EQUITY
Market Cap (RM m)	906.0
Shares Outstanding	1,053.5
52-week range (H)	0.91
52-week range (L)	0.51
3-mth avg. daily vol	1,627,288
Free Float	25%
Beta	1.0

### 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	512	560
EBIT	22	43	71
PBT	15	34	62
<b>Net Profit</b>	10	25	46
Consensus	-	-	-
Earnings Revision	-	+5%	+4%
EPS (sen)	1.0	2.4	4.4
EPS growth (%)	269	138	85
NDPS (sen)	0.5	1.0	1.1
BVPS (RM)	0.45	0.47	0.50
PER (x)	86.4	36.4	19.6
Price/BV (x)	1.9	1.8	1.7
Net Gearing (x)	-0.3	-0.2	-0.2
Net Div. Yield (%)	0.6	1.2	1.3

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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) growing preference for high quality innovative condom products. Maintain **OUTPERFORM**.

**Risks to our call include:** (i) reduced spending by government around the world on birth control, (ii) underwhelming response to its new synthetic rubber condoms, (iii) a less favourable product mix, and (iv) inability to raise prices to defend profit margins.

### Results Highlights

FYE Jun (RM m)	3Q24	2Q24	QoQ Chg	3Q23	YoY Chg	9M24	9M23	YoY Chg
Turnover	127.0	127.4	-0.3%	123.7	2.7%	383.9	397.2	-3.3%
Gross Profit	42.8	45.0	-4.9%	33.1	29.2%	127.5	100.7	26.6%
EBIT	10.7	12.5	-14.8%	5.9	79.6%	32.4	14.5	124.2%
Interest Exp.	(2.3)	(2.3)	-1.0%	(2.0)	15.5%	(6.7)	(4.9)	37.7%
PBT/(LPT)	8.4	10.2	-18.0%	3.9	112.1%	25.7	9.6	168.0%
Taxation	(2.3)	(2.9)	-18.6%	(1.7)	35.6%	(7.1)	(3.1)	132.6%
Net Profit	6.0	7.3	-17.8%	2.2	171.3%	18.6	6.5	184.5%
EPS (sen)	0.6	0.7	-17.8%	0.2	171.3%	1.8	0.6	184.5%
DPS (sen)	0.5	0.0	NA	0.0	NA	1.0	0.0	NA
Gross Margin	33.7%	35.3%		26.8%		33.2%	25.4%	
EBIT Margin	8.4%	9.8%		4.8%		8.4%	3.6%	
PBT Margin	6.6%	8.0%		3.2%		6.7%	2.4%	
NP Margin	4.7%	5.8%		1.8%		4.8%	1.6%	
Tax Rate	-27.9%	-28.1%		-43.6%		-27.6%	-31.8%	

Source: Company

### Segment Breakdown

Revenue (RM m)	3Q24	2Q24	QoQ Chg	3Q23	YoY Chg	9M24	9M23	YoY Chg
Sexual Wellness	116.5	115.4	1%	111.5	4%	350.0	362.6	-3%
Medical	7.4	8.7	-15%	10.0	-26%	24.4	27.6	-12%
Others	3.1	3.3	-5%	2.2	43%	9.5	7.0	36%
<b>Total</b>	<b>127.0</b>	<b>127.4</b>	<b>0%</b>	<b>123.7</b>	<b>3%</b>	<b>383.9</b>	<b>397.2</b>	<b>-3%</b>
<b>Operating Profit (RM m)</b>								
Sexual Wellness	10.8	10.2	6%	6.6	63%	31.5	15.6	102%
Medical	- 1.7	4.9	-135%	- 0.7	146%	1.7	- 0.7	-330%
Others	0.4	0.3	43%	0.1	265%	1.0	1.1	-13%
<b>Total</b>	<b>9.5</b>	<b>15.4</b>	<b>-38%</b>	<b>6.0</b>	<b>57%</b>	<b>34.2</b>	<b>16.0</b>	<b>113%</b>
<b>Operating Margin</b>								
Sexual Wellness	9%	9%		6%		9%	4%	
Medical	-23%	56%		-7%		7%	-3%	
Others	14%	9%		6%		10%	16%	
<b>Total</b>	<b>7%</b>	<b>12%</b>		<b>5%</b>		<b>9%</b>	<b>4%</b>	

Source: Company

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## Peer Table Comparison

Name	Rating	Last Price @ 21 May (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.
<b>CONSUMER</b>																	
AEON CO. (M) BHD	MP	1.39	1.21	-12.9%	1,951.6	Y	12/2024	8.7	8.9	6.9%	2.1%	15.9	15.6	1.0	6.5%	4.0	2.9%
DUTCH LADY MILK INDUSTRIES BHD	UP	33.22	27.65	-16.8%	2,126.1	Y	12/2024	123.1	126.3	9.4%	2.5%	27.0	26.3	4.4	17.1%	50.0	1.5%
FRASER & NEAVE HOLDINGS BHD	OP	33.00	38.25	15.9%	12,103.7	Y	09/2024	167.6	176.4	26.9%	5.3%	19.7	18.7	3.3	17.7%	85.0	2.6%
MR D.I.Y. GROUP (M) BHD	OP	1.83	1.97	7.7%	17,292.3	Y	12/2024	7.0	7.9	18.2%	12.6%	26.1	23.2	8.6	35.4%	4.0	2.2%
NESTLE (MALAYSIA) BHD	UP	129.50	115.00	-11.2%	30,367.8	Y	12/2024	292.3	306.0	3.8%	4.7%	44.3	42.3	46.2	102.9%	300.0	2.3%
PADINI HOLDINGS BHD	UP	3.77	3.20	-15.1%	2,480.3	Y	06/2024	23.0	26.7	-31.9%	15.7%	16.4	14.1	2.2	14.0%	10.0	2.7%
POWER ROOT BHD	UP	1.77	1.55	-12.4%	815.2	Y	03/2024	10.2	11.6	-25.0%	13.4%	17.3	15.3	2.6	15.0%	8.0	4.5%
QL RESOURCES BHD	MP	6.44	6.25	-3.0%	15,672.8	Y	03/2024	17.8	19.5	25.2%	9.2%	36.1	33.1	5.4	17.0%	9.0	1.4%
KAREX BHD	OP	0.860	1.10	27.9%	906.0	Y	06/2024	2.4	4.4	137.1%	85.1%	36.4	19.6	1.8	5.1%	1.0	1.2%
<b>SECTOR AGGREGATE</b>					<b>83,715.6</b>					<b>11.4%</b>	<b>8.6%</b>	<b>29.7</b>	<b>27.3</b>	<b>6.2</b>	<b>20.8%</b>		<b>2.4%</b>

Source: Kenanga Research

**Stock ESG Ratings:**

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

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