



## Company report

# KOSSAN RUBBER

(KRI MK EQUITY, KRIB.KL)

22 May 2020

*Expecting ASP to improve further*

## BUY

(Maintained)

Nafisah Azmi

nafisah-azmi@ambankgroup.com

03-2036 2250

**Rationale for report: Company results**

Price	RM8.63
Fair Value	RM9.72
52-week High/Low	RM8.65/RM3.71

### Key Changes

Fair value	⬇️
EPS	⬇️

YE to Dec	FY19	FY20F	FY21F	FY22F
Revenue (RM mil)	2,217.2	3,204.8	3,305.7	3,276.6
Core net profit (RM mil)	224.0	498.3	460.6	337.9
FD Core EPS (sen)	17.5	39.0	36.0	26.4
FD Core EPS growth (%)	12.0	122.5	(7.6)	(26.6)
Consensus Net Profit (RM mil)		279.8	299.3	326.5
DPS (sen)	5.5	15.6	14.4	10.6
PE (x)	49.3	22.2	24.0	32.7
EV/EBITDA (x)	30.3	14.6	15.0	18.2
Div yield (%)	0.6	1.8	1.7	1.2
ROE (%)	16.3	31.7	24.7	16.1
Net Gearing (%)	28.3	10.6	nm	nm

### Stock and Financial Data

Shares Outstanding (million)	1,278.9
Market Cap (RM mil)	11,037.2
Book Value (RM/share)	1.13
P/BV (x)	7.6
ROE (%)	16.3
Net Gearing (%)	28.3
Major Shareholders	Kossan Holdings (49.6%) EPF (5.3%) KWAP (2.2%)
Free Float	0.4
Avg Daily Value (RM mil)	25.3

Price performance	3mth	6mth	12mth
Absolute (%)	85.6	106.0	128.9
Relative (%)	95.7	125.8	152.8



### Investment Highlights

- We maintain BUY on Kossan Rubber Industries (Kossan) with a higher FV of RM9.72. Our valuation is based on a P/E of 27x FY21F EPS.
- We raise our earnings forecasts by 62% for FY20F, 62% for FY21F and 9% for FY22F. This is to account for higher average selling price (ASP) and sales volume. We increase our assumptions for ASP by 15% and for sales volume by 6% for FY20F–FY22F.
- Kossan's 1QFY20 core PATAMI of RM64.2mil (+9% YoY; -1% QoQ) which made up 21% of ours and 23% of street's full-year earnings forecasts, was in line with expectations.
- Kossan's 1QFY20 revenue grew 9% YoY (+6% QoQ) to RM611.5mil while PBT margin was flat 13.5% (+0.1ppt YoY; +1.0ppt QoQ) (see segmental breakdown in Exhibit 1).
- The glove division's revenue climbed 10% YoY (+7% QoQ) to RM548.2mil and recorded a PBT margin of 14% (+0.4ppt YoY; +1.2ppt QoQ) on the back of strong demand growth from the Covid-19 pandemic. Sales volume rose 7.4% YoY (+8.3% QoQ).
- Glove average selling prices increased 1–2% YoY (grew less than 0.5% QoQ). Price of nitrile material was higher by 5–7% YoY (+1–3% QoQ) while latex material price dropped 10–12% YoY (6–8% QoQ).
- The technical rubber product (TRP) division experienced lower sales deliveries in 1QFY20 which resulted in an 18% YoY (-15% QoQ) decline in revenue to RM38.4mil and 49% YoY (29% QoQ) drop in PBT to RM82.5mil.
- PBT margin was 9% as it slid 6ppt YoY (2ppt QoQ). We believe this was because of a drop in demand as infrastructure projects were halted due to the Covid-19 pandemic as well as less demand from the automotive segment.
- Glove demand arising from Covid-19 began to jump from April onwards. This resulted in a supply constraint and subsequently drove selling prices higher. Kossan has received orders close to 10 months ahead of delivery with prices to be finalized 1–2 months prior to delivery.
- We like Kossan for its expansionary plans and efforts in improving quality and operational efficiency as well as increasing automation. Moving forward, we expect a stronger performance for the year due to the increased demand from Covid-19 pandemic further buoyed by its expansion plans.

## EXHIBIT 1: FINANCIAL RESULTS

FYE 31 Dec (MYR m)	1QFY19	4QFY19	1QFY20	QoQ (%)	YoY (%)
<b>Revenue</b>	<b>561.5</b>	<b>578.3</b>	<b>611.5</b>	<b>5.7</b>	<b>8.9</b>
<b>EBITDA</b>	<b>102.9</b>	<b>98.3</b>	<b>111.6</b>	<b>13.6</b>	<b>8.5</b>
<i>EBITDA Margin (%)</i>	18.3	17.0	18.3	1.3ppt	-0.1ppt
Depreciation	(23.2)	(23.8)	(25.4)	6.6	9.3
<b>EBIT</b>	<b>79.7</b>	<b>74.5</b>	<b>86.3</b>	<b>15.8</b>	<b>8.2</b>
<i>EBIT Margin (%)</i>	14.2	12.9	14.1	1.2ppt	-0.1ppt
Interest expense	(4.6)	(2.2)	(3.7)	68.9	(19.5)
<b>Pretax profit</b>	<b>75.1</b>	<b>72.3</b>	<b>82.5</b>	<b>14.2</b>	<b>9.9</b>
<i>Pretax Margin (%)</i>	13.4	12.5	13.5	1.0ppt	0.1ppt
Tax	(15.6)	(10.7)	(17.3)	61.3	10.6
<i>Effective tax rate (%)</i>	(20.8)	(14.8)	(20.9)	-6.1ppt	-0.1ppt
Minority Interest	(0.7)	(0.6)	(0.5)	(18.6)	(37.7)
<b>Core PATAMI</b>	<b>58.7</b>	<b>64.9</b>	<b>64.2</b>	<b>(1.2)</b>	<b>9.2</b>
Net Margin (%)	10.5	11.2	10.5	-0.7ppt	0.0ppt
<u>Segmental revenue</u>					
Gloves	497.0	512.0	548.2	7.1	10.3
Technical Rubber Products	46.7	44.9	38.4	(14.5)	(17.8)
Clean-Room Division	17.1	20.9	24.5	17.2	43.4
Others	0.7	0.5	0.3	(35.6)	(57.4)
<u>Segmental pretax profit</u>					
Gloves	68.0	66.0	77.1	16.8	13.5
Technical Rubber Products	6.8	4.9	3.5	(29.3)	(49.3)
Clean-Room Division	0.6	0.8	1.8	140.5	220.3
Others	(0.3)	0.6	0.1	(82.2)	(139.8)

Source: Company, AmInvestment Bank Bhd

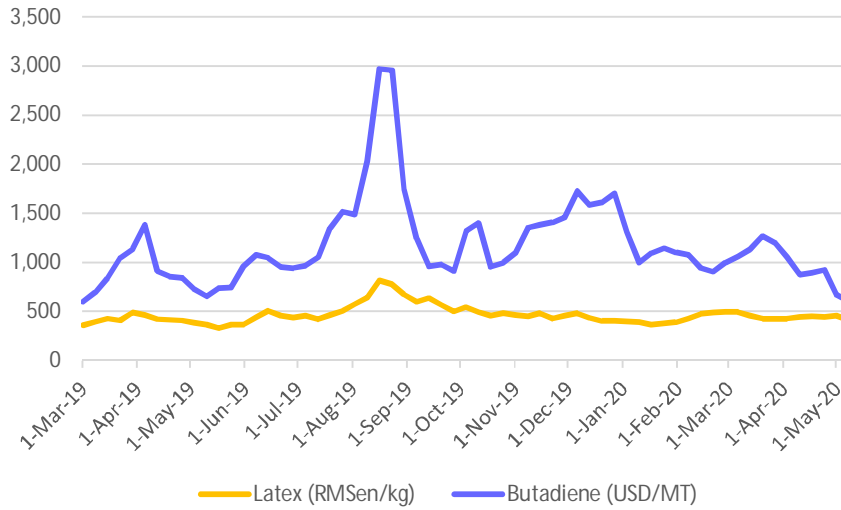
## EXHIBIT 2: PEER COMPARISON

	Recomm.	FV (RM)	Mkt Cap (RMmil)	FYE	EPS (sen)		EPS growth %		P/E (x)		ROE*	NDPS* (sen)	DY*	Estimated Capacity		
					FY20F	FY21F	FY20F	FY21F	FY20F	FY21F				(%)	CY19F	CY20F
Top Glove	BUY	12.23	26,826.7	Aug	40.8	37.0	186.4	-9.2	25.7	28.3	37.2	20.4	1.9	70.1	84.0	91.0
Hartalega#	UNDERWEIGHT	7.37	30,796.4	Mar	20.6	17.0	56.9	-17.5	44.4	53.8	27.0	12.3	1.3	36.5	41.2	44.6
Kossan	BUY	9.72	11,037.2	Dec	39.0	36.0	122.5	-7.6	22.2	24.0	31.7	15.6	1.8	31.5	34.5	34.5
<b>Simple Average</b>							<b>121.9</b>	<b>-11.4</b>	<b>30.7</b>	<b>35.4</b>				<b>138.1</b>	<b>159.7</b>	<b>170.1</b>
<b>Weighted Average</b>							<b>118.0</b>	<b>-12.6</b>	<b>33.5</b>	<b>39.0</b>						

\*FY20 #FY20F and FY21F refer to FY21F and FY22F

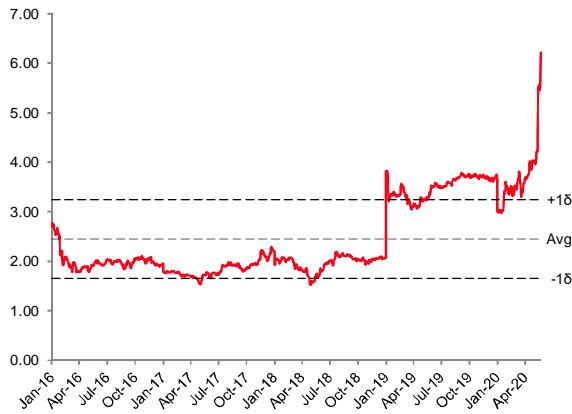
Source: Company, AmInvestment Bank Bhd

**EXHIBIT 3: LATEX AND BUTADIENE PRICE**

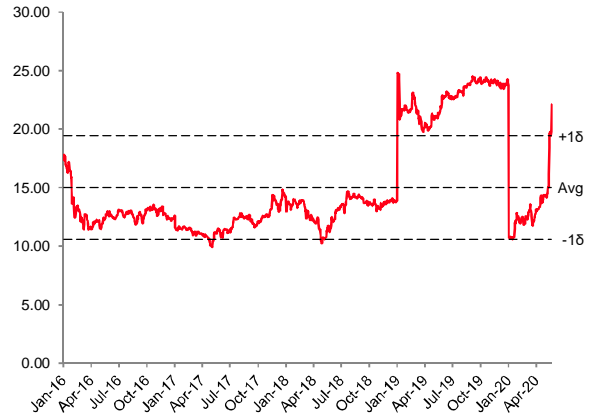


Source: Company, AmlInvestment Bank Bhd

**EXHIBIT 4: PB BAND CHART**



**EXHIBIT 5: PE BAND CHART**



## EXHIBIT 6: FINANCIAL DATA

Income Statement (RMmil, YE 31 Dec)	FY18	FY19	FY20F	FY21F	FY22F
Revenue	2,140.6	2,217.2	3,204.8	3,305.7	3,276.6
EBITDA	341.3	378.2	766.8	737.2	602.4
Depreciation/Amortisation	(76.8)	(91.2)	(115.7)	(131.5)	(147.3)
Operating income (EBIT)	264.5	287.0	651.1	605.7	455.0
Other income & associates	-	-	-	-	-
Net interest	(15.1)	(11.3)	(23.2)	(21.7)	(23.9)
<b>Exceptional items</b>	-	-	-	-	-
Pretax profit	249.4	275.7	627.8	584.0	431.1
Taxation	(44.7)	(48.5)	(122.4)	(116.8)	(88.4)
<b>Minorities/pref dividends</b>	<b>(4.8)</b>	<b>(3.2)</b>	<b>(7.1)</b>	<b>(6.6)</b>	<b>(4.8)</b>
Net profit	199.9	224.0	498.3	460.6	337.9
Core net profit	199.9	224.0	498.3	460.6	337.9
<b>Balance Sheet (RMmil, YE 31 Dec)</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20F</b>	<b>FY21F</b>	<b>FY22F</b>
Fixed assets	1,267.9	1,206.9	1,406.0	1,589.4	1,756.9
Intangible assets	1.6	-	-	-	-
<b>Other long-term assets</b>	<b>2.1</b>	<b>15.2</b>	<b>15.2</b>	<b>15.2</b>	<b>15.2</b>
Total non-current assets	1,271.7	1,222.0	1,421.2	1,604.6	1,772.1
Cash & equivalent	146.3	162.3	4.5	135.7	132.8
Stock	249.0	321.5	357.3	377.4	400.8
Trade debtors	436.4	415.3	653.4	674.0	668.0
<b>Other current assets</b>	<b>33.9</b>	<b>38.2</b>	<b>38.2</b>	<b>38.2</b>	<b>38.2</b>
Total current assets	865.7	937.2	1,053.5	1,225.3	1,239.9
Trade creditors	206.6	253.2	276.1	291.6	309.8
Short-term borrowings	279.4	401.9	62.5	62.5	62.5
<b>Other current liabilities</b>	<b>0.8</b>	<b>1.9</b>	<b>1.9</b>	<b>1.9</b>	<b>1.9</b>
Total current liabilities	486.8	657.0	340.5	356.0	374.2
Long-term borrowings	229.3	163.3	125.0	62.5	-
<b>Other long-term liabilities</b>	<b>89.8</b>	<b>93.0</b>	<b>93.0</b>	<b>93.0</b>	<b>93.0</b>
<b>Total long-term liabilities</b>	<b>319.1</b>	<b>256.3</b>	<b>218.0</b>	<b>155.5</b>	<b>93.0</b>
Shareholders' funds	1,315.1	1,424.7	1,723.6	2,000.0	2,202.8
Minority interests	27.5	26.7	51.7	53.3	52.8
BV/share (RM)	2.10	1.13	1.39	1.61	1.76
<b>Cash Flow (RMmil, YE 31 Dec)</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20F</b>	<b>FY21F</b>	<b>FY22F</b>
Pretax profit	249.4	275.7	627.8	584.0	431.1
Depreciation/Amortisation	76.8	91.2	115.7	131.5	147.3
Net change in working capital	(91.3)	(45.6)	(251.0)	(25.1)	0.6
<b>Others</b>	<b>(39.3)</b>	<b>(58.0)</b>	<b>(99.2)</b>	<b>(95.1)</b>	<b>(64.5)</b>
Cash flow from operations	195.7	263.3	393.4	595.3	514.6
Capital expenditure	(314.9)	(207.7)	(314.9)	(314.9)	(314.9)
Net investments & sale of fixed assets	0.8	1.2	1.2	1.2	1.2
<b>Others</b>	<b>0.1</b>	-	-	-	-
Cash flow from investing	(314.0)	(206.6)	(313.7)	(313.7)	(313.7)
Debt raised/(repaid)	60.0	132.3	(38.6)	55.0	(43.0)
Equity raised/(repaid)	-	-	-	-	-
Dividends paid	-	-	(199.3)	(184.2)	(135.2)
<b>Others</b>	<b>(13.3)</b>	<b>(16.1)</b>	<b>1.7</b>	<b>(20.1)</b>	<b>(24.4)</b>
<b>Cash flow from financing</b>	<b>46.7</b>	<b>116.2</b>	<b>(236.2)</b>	<b>(149.3)</b>	<b>(202.6)</b>
<b>Net cash flow</b>	<b>(71.5)</b>	<b>172.9</b>	<b>(156.5)</b>	<b>132.3</b>	<b>(1.7)</b>
<b>Net cash/(debt) b/f</b>	<b>210.4</b>	<b>146.3</b>	<b>162.3</b>	<b>4.5</b>	<b>135.7</b>
Net cash/(debt) c/f	137.5	319.0	5.5	136.6	133.7
<b>Key Ratios (YE 31 Dec)</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20F</b>	<b>FY21F</b>	<b>FY22F</b>
Revenue growth (%)	9.3	3.6	44.5	3.1	(0.9)
EBITDA growth (%)	10.4	10.8	102.8	(3.9)	(18.3)
Pretax margin (%)	11.7	12.4	19.6	17.7	13.2
Net profit margin (%)	9.3	10.1	15.5	13.9	10.3
Interest cover (x)	17.5	25.4	28.0	27.9	19.0
Effective tax rate (%)	17.9	17.6	19.5	20.0	20.5
Dividend payout (%)	19.2	31.4	40.0	40.0	40.0
Debtors turnover (days)	69	70	61	73	75
Stock turnover (days)	39	47	39	41	43
Creditors turnover (days)	35	38	30	31	33

Source: Company, AmInvestment Bank Bhd estimates

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