

KOSSAN RUBBER INDUSTRIES BHD

Company No. 48166-W

(Incorporated in Malaysia)

INTERIM FINANCIAL REPORT FOR THE QUARTER ENDED 30 JUNE 2016

Explanatory Notes

1. Basis of Preparation

The unaudited interim financial statements have been prepared in accordance with the Malaysian Financial Reporting Standards and Chapter 9 Part K of the Bursa Securities Listing Requirements. The accounting policies and method of computation adopted for the interim financial reports were consistent with those adopted for the audited financial statements for the year ended 31 December 2015.

Unless otherwise described below, the adoption of the above pronouncements are expected to have no significant impact to the financial statements of the Group upon their initial application.

2. Annual Audit Report

The audit report of the audited financial statements for the year ended 31 December 2015 was not subject to any qualification.

3. Seasonal or Cyclical Operations

The operations of the Group were not affected by any seasonal or cyclical factors.

4. Extraordinary and Exceptional Items

There were no extraordinary and exceptional items of an unusual nature affecting assets, liabilities, equity, net income, or cash flows for the current quarter and unaudited financial period ended 30 June 2016.

5. Changes in Material Estimates

There were no estimates used in the current quarter and financial period ended 30 June 2016 or in prior interim periods of the current financial year or prior financial year.

6. Movement of Company's Securities

There were no issuance and repayment of debt and equity securities, share cancellations and resale of treasury shares in the current quarter and financial period ended 30 June 2016.

7. Dividend

On 19 November 2015, the directors approved a interim tax exempt dividend of 5.5 sen per ordinary share of RM 0.50 each for the financial year ended 31 December 2015. The dividend of RM 35,170,735 was paid on 12 January 2016.

On 23 March 2016, the directors recommended a final tax exempt dividend of 6.5 sen per ordinary share of RM 0.50 each for the financial year ended 31 December 2015. This was approved at the 2016 Annual General Meeting and the dividend of RM 41,565,420 was paid on 5 July 2016.

There were no other dividends declared or paid in the current quarter and financial period ended 30 June 2016.

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Explanatory Notes**8. Segmental Reporting**

	Divisions				Total RM '000
	Technical Rubber RM '000	Gloves RM '000	Clean-Room RM '000	Investment Holding RM '000	
Financial period ended					
- 30/06/2016					
Revenue	82,074	700,057	31,997	327,940	1,142,068
Intercompany elimination	0	0	0	(326,015)	(326,015)
	<u>82,074</u>	<u>700,057</u>	<u>31,997</u>	<u>1,925</u>	<u>816,053</u>
Results	14,705	100,527	797	365	116,394
- 30/06/2015					
Revenue	74,278	652,066	28,691	0	755,035
Results	3,733	113,437	2,010	0	119,180
Quarter ended					
- 30/06/2016					
Revenue	40,651	345,808	16,159	309,147	711,765
Intercompany elimination	0	0	0	(307,992)	(307,992)
	<u>40,651</u>	<u>345,808</u>	<u>16,159</u>	<u>1,155</u>	<u>403,773</u>
Results	7,863	42,397	283	198	50,741
- 30/06/2015					
Revenue	39,053	329,976	16,750	0	385,779
Results	2,385	56,655	1,134	0	60,174

9. Valuation of Property, Plant and Equipment

There were no changes or amendments to the valuation of property plant and equipment from the previous year audited financial statements.

10. Material Events Subsequent to the End of the Interim Report

There were no significant event that has occurred between 01 July 2016 and the date of this announcement which will materially affect the earnings or income of the Group.

11. Changes in the Composition of the Group

There were no significant changes in the composition of the Group including disposal of subsidiaries and long-term investment, restructuring and discontinuing operations of the Group in the current quarter and financial period ended 30 June 2016.

12. Contingent Liabilities

As at 30 June 2016, the Company has unsecured outstanding contingent liabilities amounting to RM213.149 million (31 Dec 2015: RM 225.438 million) being corporate guarantees given to financial institutions for banking facilities granted to certain subsidiaries.

13. Capital and other Commitments

	As at financial period ended	
	30/06/2016 RM'000	31/12/2015 RM'000
Property, plant and equipment		
Within one year: Contracted but not provided	<u>4,234</u>	<u>4,234</u>

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Explanatory Notes**14. Additional Information required by the Bursa Securities Listing Requirements****14.1 Review of Results**

	Divisions				
	Technical Rubber RM '000	Gloves RM '000	Clean-Room RM '000	Investment Holding RM '000	Total RM '000
Financial period ended					
- 30/06/2016					
Revenue	82,074	700,057	31,997	327,940	1,142,068
Intercompany elimination	0	0	0	(326,015)	(326,015)
	<u>82,074</u>	<u>700,057</u>	<u>31,997</u>	<u>1,925</u>	<u>816,053</u>
Results	14,705	100,527	797	365	116,394
Percentage %	17.92	14.36	2.49	18.96	14.26
- 30/06/2015					
Revenue	74,278	652,066	28,691	0	755,035
Results	3,733	113,437	2,010	0	119,180
Percentage %	5.03	17.40	7.00	na	15.78
Comparison of financial period					
Percentage change	%	%	%	%	%
Revenue	10.50	7.36	11.52	na	8.08
Results	393.92	(11.38)	(60.35)	na	(2.34)

Quarter ended					
- 30/06/2016					
Revenue	40,651	345,808	16,159	309,147	711,765
Intercompany elimination	0	0	0	(307,992)	(307,992)
	<u>40,651</u>	<u>345,808</u>	<u>16,159</u>	<u>1,155</u>	<u>403,773</u>
Results	7,863	42,397	283	198	50,741
Percentage %	19.34	12.26	1.75	17.14	12.57
- 30/06/2015					
Revenue	39,053	329,976	16,750	0	385,779
Results	2,385	56,655	1,134	0	60,174
Percentage %	6.11	17.17	6.77	na	15.60
Comparison of Quarters ended					
Percentage change	%	%	%	%	%
Revenue	4.09	4.80	(3.53)	na	4.66
Results	329.69	(25.17)	(75.04)	na	(15.68)

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Explanatory Notes

14.1 Review of Results

Current Year To Date ("6M16") compared with Preceding Year To Date ("6M15")

The Group reported an 8.1% growth in its revenue for 6M16 to RM816.05 million, from RM755.04 million in 6M15. All three (3) divisions - glove, technical rubber products and cleanroom continued to deliver healthy growth in revenue ranging from 2.5% to 17.9% respectively. The increase in revenue was mainly attributed to higher sales volume. Its profit before taxation of RM116.39 million for the 6M16 was marginally 2.3% lower as compared with 6M15 of RM119.18 million. The marginally lower profit before taxation was mainly attributed to higher production cost on higher natural gas cost and increasing pricing pressures in glove products as compared with 6M15.

For 6M16, the TRPs division registered a 10.50% and 393.92% growth in revenue and profit before taxation as compared with 6M15. The stronger revenue performance was mainly due to higher sales volume in infrastructure products whereas the drastic increase in its profitability was largely attributed to lower management fees on effect of post restructuring exercise. Profitability of TRPs are better reflective after the restructuring exercise.

Sales of Glove division was higher by 7.36%, driven by continued healthy demand growth for our glove products and better product mix. Glove reported a revenue of RM700.06 million, a RM48.0 million higher in 6M16 as compared with RM652.07 million of the same corresponding period in FY2015. Despite of higher sales, its profit before taxation was 11.38% lower for 6M16 compared with 6M15. The lower profitability was mainly attributed to compression in margin on the back of stiffer pricing competition and slightly higher sales volume in glove products with lower profit margin.

On the positive notes, demand for our glove products continued to make record high with approximately 5.0% more in quantity of glove sold in 6M16 as compared with 6M15. For the 1st 6 months ending 30 June, the product mix of nitrile and natural latex glove stood at 70:30 and as usual, the Glove division continued to operate with almost full capacity at above 80% of its installed capacity.

Cleanroom division registered an 11.52% revenue for 6M16, mainly driven by stronger demand for cleanroom products as compared with 6M15. Profit before taxation was however, reduced by 60.35%, from RM2.01 million of 6M15 to current's RM797,000 due mainly to less favourable exchange rate.

Current Quarter ("2Q16") compared with Comparative Quarter of Preceding Year ("2Q15")

The Group reported a healthy growth in revenue by 4.66% for the current quarter as compared with its corresponding quarter of previous year. Total revenue swung higher to RM403.77 million from RM385.78 million in 2Q15. Profit before taxation was however, reduced by 15.68%, from RM60.17 million in 2Q15 to current's RM50.74 million.

The mixed performance above was mainly attributed to the following:

i. TRPs division

Revenue contribution for current quarter was 4.09% higher driven by higher sales in infrastructure products as compared with 2Q15. Its profit before taxation grew by 329.69% mainly due to lower management fees on the effects of post restructuring exercise besides the better sales performance in 2Q16.

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Explanatory Notes**ii. Glove division**

Quantity of glove sold for 2Q16 was 2.3% higher as compared with 2Q15 and brought the revenue higher to RM345.81 million, 4.8% higher 2Q15's RM329.98 million. Nevertheless, profit before taxation of Glove division in the current quarter reduced by 25.17%, from RM56.66 million reported in 2Q15 to RM42.40 million. The lower performance for the current quarter as compared with its corresponding quarter of FY2015 was largely attributed to

- Persistent industry wide selling price pressures;
- Loss of production output as a consequence of scheduled revamp works on one of the plants since 1Q16;
- Higher natural latex prices (averagely 3.4% higher i.e. RM4.67 per/kg in 2Q16 vs. RM4.52 per/kg in 2Q15);
- Increased natural gas cost (from RM19.77 to RM21.80mmBtu, by 10.3% effective 1 July 2015); and
- Higher labour cost due to industry wide labour shortage.

iii. Cleanroom

Sales volume of current quarter remained flattish pending on new projects kick-start. Less favourable exchange rate was the major factor of 75.04% lower in its profit before taxation in 2Q16.

14.2 Explanatory comments on any material change in the profit before taxation for the quarter reported on as compared with the preceding quarter.

	Divisions				Total RM '000
	Technical Rubber RM '000	Gloves RM '000	Clean-Room RM '000	Investment Holding RM '000	
Current Quarter ended - 30/06/2016					
Revenue	40,651	345,808	16,159	309,147	711,765
Intercompany elimination	0	0	0	(307,992)	(307,992)
	<u>40,651</u>	<u>345,808</u>	<u>16,159</u>	<u>1,155</u>	<u>403,773</u>
Results	7,863	42,397	283	198	50,741
Percentage %	19.34	12.26	1.75	1.71	12.57
Preceding Quarter ended - 31/03/2016					
Revenue	41,423	354,249	15,838	4,478	415,988
Intercompany elimination	0	0	0	(3,708)	(3,708)
	<u>41,423</u>	<u>354,249</u>	<u>15,838</u>	<u>770</u>	<u>412,280</u>
Results	6,843	58,130	512	167	65,652
Percentage %	16.52	16.41	3.23	22.69	15.92
Comparison of quarters					
Percentage change	%	%	%	%	%
Revenue	(1.86)	(2.38)	2.03	na	(2.06)
Results	14.91	(27.06)	(44.73)	na	(22.71)

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Explanatory Notes

14.2 continue

Variation of Results Against Preceding Quarter

(Comparison of current quarter 2Q16 with immediate preceding quarter 1Q16)

For the current quarter under review, the Group's revenue and profit before taxation was 2.3% and 22.71% lower respectively as compared with its immediate preceding quarter. Both Glove and Cleanroom divisions largely contributed to the lower profitability for the current quarter.

The weaker performance of current quarter was the consequence of the following factors which affecting the entire glove industry over the last 3 to 6 months:

- i. Riffing pricing competition industry wide on the backdrop of sudden surge in capacity;
- ii. Higher natural rubber prices by 26.1% in 2Q16 (average RM4.67 per/kg in 2Q16 vs. RM3.72 per/kg in 1Q16);
- iii. Weakening US dollar exchange experienced in current quarter;

During the quarter under review, Glove division experienced a lower glove output as compared with its immediate preceding quarter as the scheduled revamp work on one of the plants which commenced in 2Q16 had led to loss of production output.

14.3 Current Year Prospects

For the remaining period of the current year, the continued pricing pressure, as a consequence of sudden capacity surge within short period of time and coupled with higher production cost; will continue to place the overall profitability of glove makers under pressure. The Group is mindful and vigilant to this challenges and has since taken strategic moves to counter the situation.

While the Group is focusing on its patented accelerator free nitrile ("NBR") gloves and other more unique types of product to alleviate the impact led by unhealthy industry wide price competition, the Group will continue to embark on various improvement programs to increase the overall productivity and optimizing its manufacturing process to reduce the chemical usage and utilities consumption in order to bring down the overall production cost. The Group will also focus on automation and lean process to reduce the redundancy in manpower.

The Group is currently operating with 22 billion pieces of gloves per annum and all its plants are operating in almost full capacity. At the moment, the Group is facing capacity constraints to fully satisfy the growing orders on its gloves. Therefore, the Group need to build new plants to sustain its business growth and most needed transformation to bring the company to another high level of efficiency and productivity. These plants, once completed and built with higher degree of automation, are expected capable to tackle the labour shortage problem besides creating a more conducive working environment. While recognising the operating environment for glove industry is getting more challenging ahead, continuous transformation to strengthen its manufacturing capability has been the centre stage in our strategic business planning.

The construction of one new plant at Jalan Meru which commenced in May 2016 has been progressing well. This new plant is equipped with advanced high speed dipping technology with higher degree of automation and; is capable to produce 3.0 billion pieces of glove per annum once it is completed in third quarter of 2017. Meantime, planning on capacity expansion for our Bestari Jaya land (approximately 56 acres industrial land) is ongoing and the construction work of its 1st plant which is capable to produce 4.5 billion pieces of glove per annum is expected to kick start within the next 2 to 3 months.

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Explanatory Notes**14.3 Current Year Prospects - continue**

The Group is confident to be able to ride through the challenges smoothly with our business strategies and our manufacturing capability. The Management expects the impact on the Group, arising from these industry wide challenges to be minimal and strives to maintain its profit growth momentum for the remaining period of the current year.

14.4 Explanatory notes for variance of actual from forecast profit and shortfall in the profit guarantee (only applicable to the final quarter).

Not applicable.

14.5 Taxation

	Quarter period ended 30/06/2016	Financial period ended 30/06/2016
	RM'000	RM'000
Tax expense - current	7,348	19,135
Deferred taxation	<u>1,555</u>	<u>3,110</u>
	<u>8,903</u>	<u>22,245</u>

The effective income tax rate for the current quarter and financial period ended 30 June 2016 was lower than the statutory rate due to the availability of tax incentives.

14.6 Status of Corporate Proposal announced but not completed

There were no corporate proposals announced but not completed, for the current quarter and financial period ended 30 June 2016.

14.7 Group Borrowings

a) The Group borrowings as at 30 June 2016 were as follows:

	Total Unsecured RM'000
Short Term	
Revolving credit	65,717
Bankers' acceptance	51,886
Term loan due within 12 months	<u>26,375</u>
	143,978
Long Term	
Term loan due after 12 months	<u>69,171</u>
	<u>213,149</u>

Included in unsecured short-term revolving credit is an amount of USD 10.0 million (31 December 2015: nil) obtained by four subsidiaries of the Company. Other than the above, all the other borrowings were denominated in Ringgit Malaysia.

b) There were no debt securities for the financial period ended 30 June 2016.

14.8 Material Litigation

There were no pending material litigation since the last audited annual financial statements date to the date of issue of the quarterly report.

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Explanatory Notes**14.9 Earnings Per Share**

	Current Quarter ended		Financial period ended	
	30/06/2016	31/03/2015	30/06/2016	31/03/2015
	RM'000	RM'000	RM'000	RM'000
Profit after tax and minority interest	40,968	47,440	92,274	92,890
Basic earnings per share				
Basic number of ordinary shares in issue ('000)	639,468	639,468	639,468	639,468
Basic earnings per share (sen)	6.41	7.42	14.43	14.53

14.10 Realised and Unrealised Retained Earnings

	Financial period ended	
	30/06/2016	31/12/2015
	(unaudited)	(audited)
	RM'000	RM'000
Total retained earnings of Kossan Rubber Industries Bhd and its subsidiaries		
Realised	722,642	668,823
Unrealised	(31,975)	(28,865)
	<u>690,667</u>	<u>639,958</u>
Less Consolidation adjustment	(20,339)	(20,339)
	<u>670,328</u>	<u>619,619</u>

On behalf of the Board

Dato' Lim Kuang Sia
Managing Director
23 August 2016