

Company Name : Kossan Rubber Industries Berhad
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Kossan Is CIMB Research Top Pick For Glove Sector



KUALA LUMPUR: CIMB Equities Research is upbeat about Kossan Rubber Industries' prospects and it is maintaining its Add with a higher target price of RM7.55, based on an unchanged 19 times CY18F price-to-earnings (P/E).

The research house said on Tuesday Kossan is the top pick in the glove sector, with valuations below its peers (Hartalega and Top Glove).

"We expect its share price to move higher in tandem with stronger earnings delivery, especially in 2H17F. Downside risks: delays in expansion plans and stronger pricing competition," it said.

CIMB Research recently hosted a meeting with Kossan's management where 25 fund managers and buy-side analysts attended.

The bulk of the discussion was about its future, with the group revealing its expansion plans to drive earnings.

The decline in FY16 net profit to RM170.9m (-15.6% on-year) was due to a combination of external and internal factors.

In addition to stronger-than-expected pricing competition, Kossan suffered capacity loss (10%-12% of total capacity) from two factories that faced revamp works starting from 2Q16 to up to early-4Q16. Also, margins were hit by hikes in natural gas prices and minimum wages.

From 1Q17, Kossan recorded sequentially stronger performance (1Q17 net profit: +4.3% on-quarter) as total capacity reverted to normal.

“We expect Kossan to record stronger performance in FY17F, supported by a better 2H17F, with a new three billion pieces (of gloves) per annum plant beginning operations by July 2017. This is the first new plant to be added since December 2015, growing capacity to 25 billion pieces per annum (+13.6%).

“This timeline is ahead of our estimates as we had earlier projected for the new plant to only begin production in 4Q17F. This leads to earnings upside to our FY17F estimates,” it said.

Another two new plants (4.5 billion pieces per annum) to come onstream in FY18F. Also, Kossan will add two new plants in FY18F with total capacity of 4.5 billion pieces per annum.

The first plant is slated for completion by 1Q18F and the second plant will begin operations in 3Q18F. Total capacity will rise to 29.5bn p.a. by 3QCY18F.

“We gather that all of its new plants have been earmarked to manufacture its patented accelerator-free nitrile gloves, with latest automation to be installed along with high-speed dipping manufacturing lines.

“Kossan will carry on conducting revamp works on its existing facilities to increase overall operating efficiencies.

“However, this will be conducted on a gradual basis to ensure production is not disrupted again. Revamp works include plans to utilise more automation in its production flow in a bid to increase cost savings and production output,” it said.

CIMB Research said with its new capacity coming on-stream earlier than expected, its FY17-19F EPS is adjusted higher by 2.2%-4.6%.

“Accordingly, our target price is raised to RM7.55 based on an unchanged 19 times CY18F P/E (+one standard deviation from its five-year mean),” it said.