Company Name : **Kossan Rubber Industries Berhad**
Date : **04 October 2017**
Source : **The Edge Financial Daily**

Kossan expected to emerge stronger in 2H

Kossan Rubber Industries Bhd (Oct 3, RM6.90)

Reiterate hold with a target price of RM7.35: From our meeting with management, we continue to expect Kossan Rubber Industries Bhd to emerge stronger in the second half of financial year 2017 (2HFY17), underpinned by Plant 16, its latest glove plant.

However, we note that a pick-up in contribution is only likely to be observed in the fourth quarter of FY17 (4QFY17). Our earlier capacity growth assumptions were a tad bullish. After moderating it, we now estimate earnings growth for FY17/FY18/FY19 at 20.9%/22.5%/11.2%, from 29.9%/17.9%/15.5% before.

Management reiterated its expansion ambitions, which entail glove capacity growing at a compound annual growth rate (CAGR) of 11.3% across 2018 to 2023. With regard to headwinds from volatility in the US dollar/ringgit exchange rate and prices of raw materials, management reassured of the group's ability to pass through costs, albeit with a time lag.

Meanwhile, we note that the group will continue to focus on efficiency improvements and product innovation to remain competitive.

We continue to expect Kossan to emerge stronger in 2HFY17. While the group's 1HFY17 earnings of RM92 million (-0.2% year-on-year [y-o-y]) accounted for 45.6% of our latest FY17 estimate of RM201.9 million, expectations are for 2HFY17 to be underpinned by the ramp-up of Plant 16 — the group's latest glove plant in Jalan Meru, Klang, which commenced operations in 3QFY17.

Kossan Rubber Industries Bhd

FYE DEC (RM MIL)	2015	2016	2017F	2018F	2019F
Revenue	1,639.5	1,668.0	2,014.8	2,172.3	2,483.8
Ebitda	337.6	279.3	337.8	402.6	443.6
Dep & amortisation	(66.9)	(69.3)	(70.1)	(76.1)	(81.6)
Net finance cost	(2.1)	(0.0)	(3.9)	(3.4)	(2.5)
EI	(1.0)	0.0	0.0	0.0	0.0
PBT	267.6	210.0	263.8	323.2	359.4
Taxation	(62.2)	(39.0)	(56.7)	(69.5)	(77.3)
MI	(5.1)	(4.1)	(5.2)	(6.3)	(7.1)
Net profit	200.2	166.9	201.9	247.4	275.1
EPS (sen)	32.5	26.1	31.6	38.7	43.0
DPS (sen)	12.0	13.1	15.8	19.3	21.5

Source: TA Securities

To recap, the plant has a capacity of three billion gloves per annum and enlarges the group's capacity by 13.6% to 25 billion gloves per annum. However, do note that a pickup in contributions is only likely to be observed in 4QFY17 as the commissioning of production lines in stages is still under way with completion expected in November 2017.

Indicative of healthy plant utilisation rates as well as an upside to the group's 1HFY17 sales volume growth of 6.7% y-o-y, we take note of the sustained growth in demand for the group's latest innovation — accelerator free nitrile gloves featuring low dermatitis potential.

Management reiterated its ambitions to continue expanding the glove division — the group's core division which accounts for about 85% to 90% of revenue. Apart from the long-term growth potential for medical gloves, especially from populated emerging markets with low usage per capita, growth opportunities are also present for non-medical gloves. No specific timeline was given, but the group seeks to double the capacity of its special purpose and industrial gloves to 30%.

Based on latest expansion plans, during 2018 to 2023, the glove division's capacity is expected to be enlarged by 22.5 billion gloves per annum to 47.5 billion gloves per annum, translating into a CAGR of 11.3%.

Right now, the group is working on the construction of Plant 17 (+1.5 billion gloves per annum) and Plant 18 (+three billion gloves per annum) in Jalan Meru, which are expected to commence operations respectively in 3QFY18 and 4QFY18. As for the subsequent phase of expansion in Bestari Jaya, which entails four plants (Plant 19 to Plant 22), each with a capacity of 4.5 billion gloves per annum, construction is expected to begin in 2018. Our earnings growth projections for FY17/FY18/FY19 are at 20.9%/22.5%/11.2%. — *TA Securities, Oct 3*