

PP14767/09/2012(030761)

Wednesday, May 04, 2016

Hartalega Holdings Berhad

“Double-Digit Growth amid Challenging Times”

Results Review

- Actual vs. Expectations.** For 12M16, Hartalega Holdings Berhad (Hartalega) recorded RM1,498 million in revenue (+31% y-o-y) underpinned by stronger demand and favourable USD/MYR trends. EBITDA rose 22% y-o-y to RM419 million while PBT and PAT improved 15% and 23% to RM317 million and RM258 million, respectively. PATMI touched RM257.6 million, making up 96% of our full year FY16 forecast of RM267.8 million. The strong double digit-growth in earnings was generally credited to progressive contribution from Next Generation Complex (NGC) Plant 1 & 2, increase in glove demand and strengthening of USD.
- Dividend.** Hartalega declared second interim dividend of 2.0 sen yesterday, totalling 6.0 sen for 12M16 vs. 13.0 sen in the same previous corresponding period. To recap, Hartalega had distributed 1:1 share bonus in September 2015.
- Q4 FY16 Results.** Hartalega has beaten its previous record revenue in 3Q16 of RM398 million after delivering a new record revenue of RM400 million (+31% y-o-y) in 4Q16, thanks to the group’s continuous expansion in production capacity and steady growth in glove demand. During the quarter, sales quantity surged 45% y-o-y from 3.3 billion pieces to 4.4 billion pieces, 95% were made up by nitrile gloves and 5% latex gloves. EBITDA rose significantly by 20% y-o-y but dropped by 12% q-o-q to RM109 million. PATMI improved by 12% y-o-y to RM62 million, translating into PATMI margin of 15%. EPS increased 7% to 3.8 sen for the quarter after having adjusted to the recent 1 for 1 bonus issue.

BUY (TP:RM4.78)

Current Price (RM)	RM4.14
New Target Price (RM)	RM4.78
Previous Fair Value (RM)	RM5.70
Previous Recommend.	HOLD
Upside To Fair Value	15%
Dividend Yield (FY16)	2%

Stock Code

Bloomberg	HARTA MK
-----------	----------

Stock & Market Data

Listing	MAIN MARKET	
Sector	Glove	
Shariah Compliance	Yes	
Issued Shares (mn)	1,641.0	
Market Cap (RM mn)	6,793.9	
YTD Chg In Share Price	-30.3%	
Beta (x)	0.51	
52-week Hi/Lo (RM)	RM6.15	RM3.85
3M Average Volume (shrs)	1.8mn	
Estimated Free Float	28.6%	

Major Shareholders

Hartalega Industries S/B	49%
EPF	7%
Budi Tenggara S/B	3%

- **Production Capacity & Utilization Rate.** The completion of NGC Plant 1 & 2 has progressively ramped up the total capacity to 19 billion pieces from 14 billion pieces (+37% y-o-y) in 12M FY16, strengthening the overall economies of scale. Hartalega added 8 additional lines in FY16, making up 69 lines with an average utilisation rate of 81%.
- **Nitrile Glove Production.** In Q4 FY16, the average selling price (ASP) of nitrile gloves dropped 11% q-o-q, however, the earnings were cushioned by 10% y-o-y jump in sales quantity from 3.1 billion pieces to 4.2 billion pieces. As much as 94% of total revenue was contributed from nitrile gloves amounting to RM377 million or the industry's highest in terms of the sales of nitrile gloves.
- **Latex Glove Production.** The ASP of latex gloves, on the other hand, merely registered a 5% decline which subsequently led to 14% drop in sales contribution in Q4 FY16. Quantity sales decreased from 256 million pieces in previous quarter to 229 million pieces in tandem with management's effort on product switching from latex to nitrile gloves. Sales of latex gloves touched RM23 million (-14 % q-o-q) or 5% of the total sales.
- **Changes to forecast.** In view of weakening US dollar while commodity prices are gaining further traction, we have cut our forecast on USD/Ringgit in FY17-18 from previously RM4.20 to RM4.00 as we believe the tailwinds of softening USD will continue to blow in the months ahead. Our FY17/18 EPS has been revised from 20.5 sen/21.6 sen to 19.1 sen/20.1 sen, respectively.
- **Outlook.** We believe all glove players including Hartalega are feeling the heat in the face of rising operating costs, increasingly competitive sales and weakening US dollar which used to favour export-oriented glove companies in the past few years. The impact on government policy of increasing utility costs, increasing foreign levy, freezing intake of foreign labour as well as external factors such as rising latex prices and recovery of oil prices have resulted in glove manufacturers to lose their shine among investors. However, we reckon that the impact is temporary until the government announce the lift of freeze hiring and subsequent cost pass on to customers which will eventually see continued rise on the bottom line of glove makers.

While the supply of nitrile gloves has increased tremendously in the wake of switching momentum to meet global demand, the demand-supply gap is hence, narrowed down over the time which partly explained why Hartalega's ASP registered negative 6% y-o-y in Q4 FY16. Notwithstanding that, the fundamentally sound company is expected to continue stand out from its peers provided its superior product quality and extremely high nitrile-latex product mix of 95%. The progress of building new manufacturing facility is still well on track despite some minor delay due to temporary shortage of hand formers. Upon completion of NGC 8-year project, the total capacity will be ramped up to 42 billion pieces, running at >45,000 pieces/hour/line, arguably still the world's largest nitrile glove maker by 2021.

- **Valuation & Recommendation.** Taking into consideration of increasing competition in the industry such as lower ASP and pricier operating environment, we revise our target price from RM5.70 to RM4.78 based on the Hartalega's 3-year PER of 25x against FY17 EPS of 19.1 sen. Nevertheless, we continue to be positive on the company's prospects moving forward given the robust world demand in medical gloves which expected to grow 8-10% per annum especially in nitrile glove segment which Hartalega has great competitive advantage over its peers in terms of technology and economies of scale. Maintain **BUY**.

Table 1: Peers Comparison

Company	Year Ended	Price (RM)	EPS (sen)		P/E (X)		P/B (X)		ROE (%)	Div Yield (%)	Target Price	Call
			FY15	FY16	FY15	FY16	FY15	FY16				
Hartalega	Mar	4.14	14	20	32	29	3	7	17.9	1.8	4.78	BUY
Top Glove	Aug	4.96	58	67	17	21	4	4	22.5	2.3	6.12	BUY
Kossan	Dec	5.99	29	38	19	20	5	5	21.7	1.7	8.62	BUY
Supermax	Dec	2.59	16	20	11	16	1	2	10.8	1.5	2.94	HOLD
Average			29	36	41	22	3	5				

Source: Bloomberg, M&A Securities

Table 2: Financial Summary

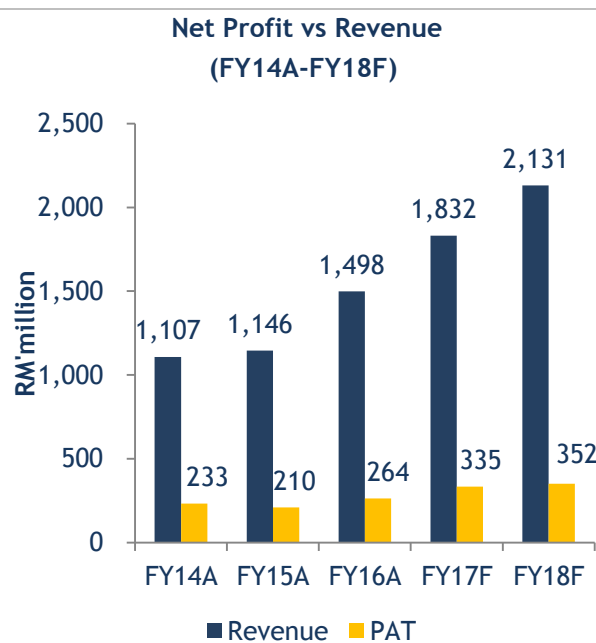
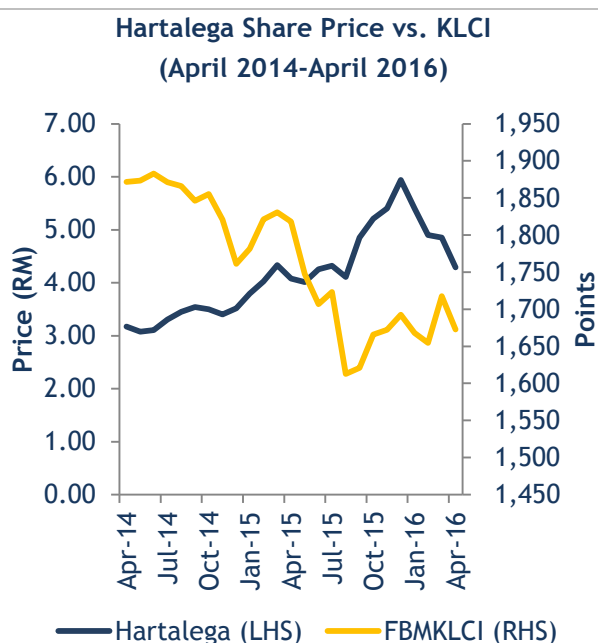
FYE MAR (RM million)	4Q15	3Q16	4Q16	Q-o-Q	Y-o-Y	12M15	12M16	Y-o-Y
Revenue	305	398	400	1%	31%	1,146	1,498	31%
EBITDA	91	124	109	-12%	20%	343	419	22%
D&A	(24)	(33)	(38)	14%	57%	(68)	(102)	51%
EBIT	67	91	71	-22%	7%	275	316	15%
Net interest income	1	0	0	-78%	-89%	2	1	-51%
PBT	67	91	71	-22%	6%	277	317	15%
Tax	(12)	(18)	(9)	-48%	-24%	(67)	(59)	-11%
PAT	55	73	62	-15%	12%	210	258	23%
MI	(0)	(0)	(0)	-52%	-32%	(1)	(0)	-21%
PATMI	55	73	62	-15%	12%	210	258	23%
EPS	4	4	4	-15%	-9%	13	16	17%
EBITDA margin	30%	31%	27%	-4%	-3%	30%	28%	-7%
EBIT margin	22%	23%	18%	-5%	-4%	24%	21%	-12%
PBT margin	22%	23%	18%	-5%	-4%	24%	21%	-12%
Net profit margin	18%	18%	15%	-3%	-3%	18%	17%	-6%

Source: M&A Securities

Table 3: Financial Forecast

FYE MAR (RM million)	FY14A	FY15A	FY16A	FY17F	FY18F
Revenue	1,107.2	1,146.0	1,498.3	1,744.4	2,029.6
EBITDA	353.6	321.6	401.1	482.3	522.9
D&A	(45.2)	(45.9)	(70.6)	(90.6)	(110.6)
EBIT	308.4	275.7	330.5	391.7	412.3
Net interest income	0.8	1.2	0.0	0.0	0.0
PBT	309.2	276.9	330.5	391.7	412.3
Tax	(75.4)	(66.7)	(66.1)	(78.6)	(83.0)
PAT	233.2	209.7	264.4	313.1	329.3
MI	(0.5)	(0.5)	(0.4)	(0.5)	(0.5)
PATMI	232.7	209.2	264.0	312.6	328.9
EPS	14.2	12.8	16.1	19.1	20.1
EBITDA margin	32%	28%	27%	28%	26%
EBIT margin	28%	24%	22%	22%	20%
PBT margin	28%	24%	22%	22%	20%
Net profit margin	21%	18%	18%	18%	16%
PER (x)	42.1	46.8	37.1	31.3	29.8
P/BV (x)	10.5	7.9	6.6	5.7	5.0
Dividend (sen)	14.5	13.5	8.1	9.5	10.0
Dividend yield	2%	2%	1.35%	1.60%	1.68%

Source: M&A Securities



Source: Bloomberg, M&A Securities

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

DISCLOSURES AND DISCLAIMER

This report has been prepared by M&A SECURITIES SDN BHD. Readers should be fully aware that this report is for informational purposes only and no representation or warranty, expressed or implied is made as to the accuracy, completeness or reliability of the information or opinion contained herein. The recommendation and opinion are based on information obtained or derived from sources believed to be reliable.

This report contains financial forecast/projection based on our assumptions which may defer from the actual financial results announced by the companies under coverage. All opinions, estimates and assumptions are subject to change without notice. Analysts will initiate, update and cease coverage solely at the discretion of M&A SECURITIES SDN BHD.

Investors are to be cautioned that value of any securities invested may fluctuate from time to time. We advise investors to seek financial, legal and other advice for investing based on the recommendation of our report as we have not taken into account each investors' specific investment objectives, risk tolerance and financial position.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. M&A SECURITIES SDN BHD can accept no liability for any consequential loss or damage whether direct or indirect. Investment should be made at investors' own risks.

M&A SECURITIES SDN BHD and INSAS GROUP of companies, their respective directors, officers, employees and connected parties may have interest in any of the securities mentioned and may benefit from the information herein. M&A SECURITIES SDN BHD and INSAS GROUP of companies and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This report may not be reproduced, distributed or published in any form or for any purpose.

M & A Securities SdnBhd (15017-H)

(A wholly-owned subsidiary of INSAS BERHAD)

A Participating Organisation of Bursa Malaysia Securities Berhad

Principal Office:

Level 1,2,3 No.45 & 47,43-6

The Boulevard, Mid Valley City,

Lingkaran Syed Putra,

59200 Kuala Lumpur

Tel: +603 - 2282 1820 Fax: +603 - 2283 1893

Website: www.mnaonline.com.my