PP14767/09/2012(030761)

Thursday, October 13, 2016

Market Access

Top Glove Corporation Berhad

"Hit by Higher Overheads"

Results Review

- **Actual vs. expectations.** For 12MFY16, Top Glove Corporation Berhad (TOPG) reported a record sales of RM2.89 billion (+15% y-o-y), primarily boosted by escalating sales quantity which grew 11% y-o-y as well as the strengthening in US dollar. EBITDA rose from RM446 million to RM526 million (+18% y-o-y) with identically strong EBITDA margin of 18% as compared to 12M15. PBT was also spurred by strong top-line performance that subsequently registered a respectable 22% y-o-y growth to RM443 million. Nonetheless, net profit came within below our expectation at RM363 million or equivalent to 90% of our FY16 earnings forecast due to comparatively weak 4Q16 results.

- **Dividend.** The Board proposed 8.5 sen final interim dividend in 4QFY16, translating into a potential dividend yield of 2.9% based on RM4.95 per share.

- **4Q FY16 results.** TOPG posted RM722 million (+7% q-o-q; +2% y-o-y) revenue in 4Q16, which is within our expectation. We anticipated flattish growth in the topline after the robust performance in sales quantity in 4Q15 and 3Q16. Intensifying pricing competition also buffered sales growth in 4Q16 which we do not see any signs of mitigation in short term. PBT was squeezed by 44% y-o-y to RM76 million due to escalating operating expenses which soared 14% y-o-y. Exceptional natural gas price hike (twice a year in 2016; +24% y-o-y) coupled with incremental minimum wage (+11% y-o-y) were the culprits that hammered the bottom-line growth in 4Q16.

BUY (TP:RM6.12)

Current Price (RM)	RM5.00
Previous Target Price (RM)	RM4.95
Previous Recommendation	HOLD
Upside/(Downside) To Target	22%
Dividend Yield (FY16)	3%

Stock Code

Bloomberg	TOPG MK

Stock Information

Listing		MAIN MARKET
Sector		Glove
Shariah Compliance		Yes
Issued Shares (mn)		1,252.7
Market Cap (RM mn)		6,263.5
YTD Chg in Share Price		-26.2%
Beta (x)		-0.05
52-week Hi/Lo (RM)	7.03	3.99
3M Average Volume (shrs)		5.2mn
Estimated Free Float		45.1%

Major Shareholders

Lim Wee Chai	29.4%
EPF	8.0%
Firstway United Corp	5.1%

Research Team
hcchoo@mna.com.my
03-22821820 ext. 219

- **Focus on growing NBR production.** Product mix by sales quantity was seen moving towards more balanced over the time where nitrile gloves (NBR) made up 34%, merely 1% lower than latex powdered gloves while the remaining 31% consisted of latex powder-free, surgical, vinyl and TPE/CPE gloves. TOPG is underway in expanding its NBR production capacity by building 2 new factories (F30 and F31) in Klang which would have 100 new NBR production lines with 10.8 billion pcs/annum capacity. Thus, we expect NBR production to surpass natural rubber gloves (NR) by end-2017. For FY16, the NR:NBR product mix stayed at 58:32, versus 64:28 in FY15.

- **Switching to NBR generates more stable costing.** The cut-down in NR production will reduce the group's exposure to the movement of natural rubber latex prices which have been rebounding and tend to be more fluctuating compared to nitrile latex. This, hence, minimizes the mismatch in the cost-pass through system. The recent rebound in crude oil prices was fuelled by the news of production cut in Saudi Arabia and Russia which subsequently boost the Brent crude to USD 53.14/barrel on Tuesday. As synthetic rubber is partly produced from petroleum and tyre manufacturers shift between synthetic and natural rubber depending on which is cheaper, we expect NR price will be lifted up to RM5.50/kg should the oil price continues to move northbound.

- **Outlook.** Challenging moments as we notice raw material prices tend to edge higher from the trough in tandem with the recovery in crude oil prices. This could further pressure glove makers of their pricing strategy amid the narrowing supply-demand gap due to industry wide expansion in production capacity. Moreover, heightened cost of operation attributed by more expensive natural gas and labour costs will be the headwinds for the bottom line growth moving forward. That said, profitability is highly dependent on several key factors including product innovation, optimization of production efficiency, expanding economies of scale and cutting dependency on certain major customers to avoid margins squeeze.

  Despite challenging business environment, we reckon that TOPG is resilient to weather the headwinds owing to i) highly diversified clientele base with over 2,000 customers worldwide with no single customer contributes more than 4% of revenue, ii) fast respond to market demand by shifting the focus on latex glove to nitrile glove (product mix of latex to nitrile from 81:11 to 58:32 within 5-year period), iii) undergoing expansion plan by adding additional 12 billion pieces glove per annum by 4Q17, keep on growing the already largest production capacity in the world, iv) increased automation throughout the manufacturing process and on-going facility optimization initiatives to boost production efficiency.

- **Changes of forecast.** We make no changes in our earnings forecast, maintaining FY17/18 PAT of RM507 million and RM499 million, respectively.

- **Valuations & recommendation.** Maintain target price at RM6.12 based on our target PER and FY17 earnings estimates, recommending a **BUY** call with an upside of 22% from yesterday's closing price. Given the anticipation of the US interest rate hike by end of the year, we are

Research Team
hcchoo@mna.com.my
03-22821820 ext. 219

positive on export-oriented company like TOPG as the hike could be positive for its bottom-line growth.

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				
Top Glove	Aug	5.00	23	23	17	17	3	3	25	3	**6.12**	**BUY**
Kossan	Dec	6.90	30	32	29	29	4	6	21	2	**8.55**	**BUY**
Hartalega	Mar	4.90	14	16	32	31	5	5	17	2	**4.78**	**BUY**
Supermax	Jun	2.23	14	15	12	14	2	1	10	3	**2.94**	**BUY**

Source: Bloomberg, M&A Securities

Table 2: Financial Summary

FYE AUG (RM million)	4Q16	3Q16	4Q15	Q-o-Q	Y-o-Y	12M15	12M16	Y-o-Y
Revenue	722	672	709	7%	2%	2,511	2,889	15%
EBITDA	97	94	159	4%	-39%	446	526	18%
D&A	(27)	(26)	(26)	2%	4%	(98)	(108)	9%
EBIT	70	67	133	5%	-47%	348	418	20%
Net interest income	5	7	7	-18%	-25%	21	24	16%
PBT	76	74	134	3%	-44%	364	443	22%
Tax	(10)	(11)	(31)	-9%	-68%	(82)	(80)	-3%
PAT	66	63	104	5%	-36%	282	363	29%
MI	(0)	(0)	(0)	-40%	-59%	(1)	(2)	21%
PATMI	66	62	103	5%	-36%	280	361	29%
EPS (sen)	5	5	8	5%	-37%	23	29	27%
EBITDA margin	13%	23%	22%	-10%	-9%	18%	18%	0%
EBIT margin	10%	11%	19%	-1%	-9%	14%	14%	1%
PBT margin	10%	11%	19%	0%	-8%	14%	15%	1%
Net profit margin	9%	9%	15%	0%	-5%	11%	12%	1%

Source: M&A Securities

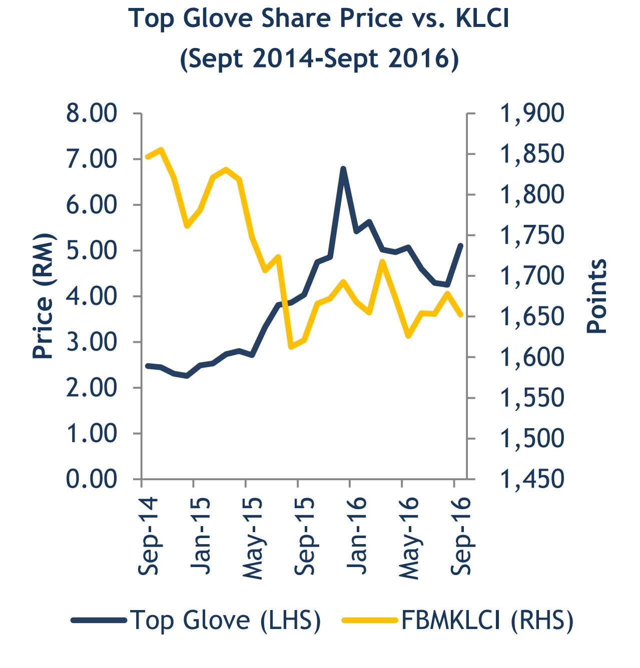
Research Team
hcchoo@mna.com.my
03-22821820 ext. 219

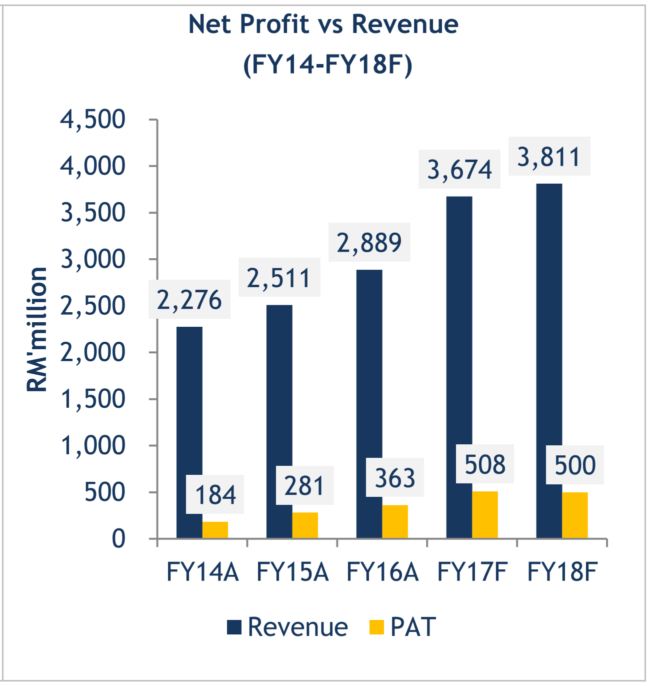
Market Access

Table 3: Financial Forecast

FYE AUGUST (RM million)	FY14A	FY15A	FY16A	FY17F	FY18F
Revenue	2,276	2,511	2,889	3,674	3,811
EBITDA	266	436	526	764	768
D&A	(92)	(99)	(108)	(123)	(135)
EBIT	174	337	418	641	633
Net interest income	6	20	24	16	15
PBT	216	364	443	657	647
Tax	(33)	(82)	(80)	(149)	(146)
PAT	184	281	363	508	500
MI	(3)	(1)	(2)	(1)	(1)
PATMI	181	280	361	507	499
EPS (sen)	15	22	29	41	40
EBITDA margin	12%	17%	18%	21%	20%
EBIT margin	8%	13%	14%	17%	17%
PBT margin	9.50%	14%	15%	18%	17%
Net profit margin	8%	11%	13%	14%	13%
PER (x)	19.4	12.5	17.6	13.9	14.1
P/BV (x)	2.5	2.2	3.9	3.4	3.1
Dividend (sen)	16.0	23.0	16.0	20.2	20.3
Dividend yield	3%	4%	3%	4%	4%

Source: M&A Securities





Source: Bloomberg, M&A Securities

Research Team
hcchoo@mna.com.my
03-22821820 ext. 219

M&A Securities

STOCK RECOMMENDATIONS

BUY	*Share price is expected to be ≥+10% over the next 12 months.*
TRADING BUY	*Share price is expected to be ≥+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 ≥-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

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

Research Team
hcchoo@mna.com.my
03-22821820 ext. 219