

HLIB Research

PP 9484/12/2012 (031413)

Sheikh Abdullah
Sheikh@hlib.hongleong.com.my

(603) 2083 1711

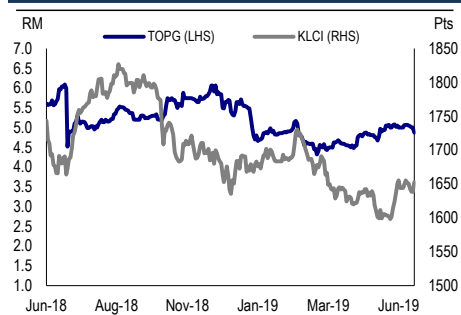
BUY (Maintain)

Target Price: **RM5.31**
Previously: **RM5.31**
Current Price: **RM4.87**

Capital upside	9.0%
Dividend yield	1.7%
Expected total return	10.7%

Sector coverage: Rubber Gloves

Company description: Top Glove is the biggest producer of rubber gloves in Malaysia by volume.

Share price


	1M	3M	12M
Historical return (%)	-1.4	7.7	-14.6
Absolute	-1.4	7.7	-14.6
Relative	-4.2	10.2	-9.9

Stock information

Bloomberg ticker	TOPG MK
Bursa code	7113
Issued shares (m)	2,562
Market capitalisation (RM m)	12,477
3-mth average volume ('000)	4,830
SC Shariah compliant	Yes

Major shareholders

Lim Wee Chai	28.6%
Firstway Utd Corp	7.2%
EPF	6.4%

Earnings summary

FYE (Aug)	FY18	FY19f	FY20f
PATMI – core (RM m)	433.6	398.3	521.4
EPS – core (sen)	16.9	15.6	20.4
P/E (x)	28.7	31.2	23.9

Top Glove

Margins to recover next quarter

9MFY19 core PATAMI of RM299.5m was below expectations. The results were below mainly due to a spike in prices of natural rubber during the quarter (+22.0% QoQ) and the subsequent lag in ASP revision which affected margins. We expect this to reverse in 4QFY19 given that prices have been revised upward since May (+8.8%). Maintain BUY and TP of RM5.31, based on FY20 earnings pegged to a PE multiple of 26x.

Below expectations: 9MFY19 core PATAMI came in at RM299.5m (-11.0% YoY), accounting for 68.2% of our and 65.1% of consensus estimates. The results were below mainly due to a spike in prices of natural rubber during the quarter (+22.0% QoQ) and the subsequent lag in ASP revision which affected margins. We expect this to reverse in 4QFY19 given that prices have been revised upward since May (+8.8%).

Dividend. Declared first interim dividend of 3.5 sen/share going ex-2nd July 2019.

QoQ. Revenue improved by 2.6% in tandem with volume growth of 2% QoQ. EBITDA declined 23.3% QoQ to RM182.3m, whilst EBITDA margin declined by 4.0 ppts to 11.7% (from 15.7%). This is attributed to a 22% increase in latex prices in 2Q19 and the subsequent time lag associated with passing on the cost to customers (note that latex accounts for 45.0% of production costs for Natural rubber gloves). Core PATAMI declined by 3.1% despite a lower tax expense (8.6% vs. 15% in 2Q19 – due to a write back for an overprovision – we expect subsequent quarters tax rate to normalize on a full year basis c. 18%-19%). In computing our core PATAMI we added back RM15.0m of forex losses.

YoY. Revenue grew 8.1% to RM1.19bn (from RM1.10bn) from higher volumes sold (+9%) whilst ASP was flattish. The volume growth mainly came from the nitrile (+25%) and surgical (+29%) offset by vinyl gloves (-42%). EBITDA declined 20.4% YoY (to RM139.7m) and margins eroded by 4.2ppts due to the sharp spike in natural rubber prices associated with a multitude of factors; (1) wintering season (February to May) (2) the run up to the Thai elections saw rubber prices boosted and (3) the ongoing drought in Thailand. PBT declined 38.7% YoY to RM82.2m due to a higher interest expense (+58.0% YoY) due to M&A and organic expansion. Subsequently, core PATAMI declined 29.7% YoY (to RM89.5m after adjusting for FX losses amounting to RM11.4m vs RM1.2m in 3Q18). A higher effective tax rate (16.0% vs. 12.0% in 3Q18) accentuated the decline.

YTD. Revenue improved to RM3.61bn (+20.5%) attributed namely to higher volumes (+15% YoY). The volume growth mainly came from nitrile (+35%) and surgical (+75%) offset by vinyl gloves (-25%). EBITDA improved to RM518.6m (+11.2%), whilst EBITDA margins declined 0.9ppts (to 14.3%) due to higher raw material prices and competitive pressures. Core PATAMI of RM299.5m (-11.0%) exhibited negative growth YoY due to the same above mentioned factors- namely commodity swing and higher finance costs.

Capacity expansion. We understand that F32 1st phase (Nitrile/Latex) and F33 (Latex) are operational and currently producing. In 2HCY19 we will see additional 1.2bn pieces of new installed capacity. This implies that in CY19 TG will increase new capacity to a maximum of 4.6bn pieces or 7.6% YoY, which is well within the range of the annual demand growth (see figure #2).

Outlook. ASP for the latex segment has already been revised upward from May onward (+8.8%) which should normalize margins moving forward, *ceteris paribus* (c.15%-16% at the EBITDA level). Aspion achieved an EBITDA of RM40.6m and as such, no impairments were necessary. We expect Top Glove to conclude FY19 on a better standing on improved profitability QoQ.

BioGreen. Top Glove recently launched its bio-degradable nitrile examination gloves. The product is proven to decay 10x faster compared to existing conventional nitrile gloves. We understand that it has been well received in developed nations (EU, Japan and USA). Management didn't share the product's pricing, however given the recent global enthusiasm on environmental issues and recent rubbish dumping by western nations to Malaysia and alike; we can expect Top Glove to leverage this product to their benefit.

Forecast. We adjust our FY19 earnings downward by 9.3% as we recalibrate our model with higher average latex prices for FY19. However, FY20-21 earnings are unchanged as the ASP price revision in May should help preserve margins going forward.

Maintain BUY, TP: RM5.31. Maintain TP of RM5.31 and our BUY call. Our TP is based on FY20 earnings pegged to a PE multiple of 26x. We like Top Glove for its more diverse product mix and its prime position to chip away market share.

Figure #1 Quarterly results comparison

FYE Dec (RM m)	3QFY18	2QFY19	3QFY19	QoQ (%)	YoY (%)	9M18	9M19	YoY (%)
Revenue	1,100.6	1,160.0	1,190.2	2.6	8.1	2,997.1	3,612.2	20.5
EBITDA	175.5	182.3	139.7	(23.3)	(20.4)	466.2	518.3	11.2
EBIT	136.6	134.9	89.1	(34.0)	(34.8)	363.3	372.6	2.6
PBT	134.2	125.5	82.2	(34.5)	(38.7)	380.7	349.6	(8.2)
PAT	119.4	106.7	75.2	(29.5)	(37.0)	335.3	293.5	(12.5)
Core PATMI	127.4	92.4	89.5	(3.1)	(29.7)	336.4	299.5	(11.0)
Reported PATMI	117.6	105.8	74.7	(29.4)	(36.5)	331.9	290.4	(12.5)
Core EPS (sen)	4.6	3.6	3.5			13.2	11.7	
EBITDA margin (%)	15.6	15.7				15.6		
EBIT margin (%)	12.4	11.6				12.1		
PBT margin (%)	12.2	10.8				12.7		
PATMI margin (%)	10.7	7.9				11.1		

Bursa, HLIB Research

Figure #2 Capacity Expansion Schedule

Manufacturing	Production Commencement (Calendar quarter)	Country	Glove type	Number of production lines	Capacity (pcs per annum)	Capital Expenditure (RM mil)
Current:						
32 glove factories			All	648 lines	60.5 bn	
Expansion in progress : Glove						
F32 New Factory 1 st Phase	2 nd quarter 2019	Malaysia	Nitrile/Latex	22 lines	2.2 bn	134 mil
F33 New Block	2 nd quarter 2019	Malaysia	Latex	12 lines	1.2 bn	37 mil
F32 New Factory 2 nd Phase	3 rd quarter 2019	Malaysia	Nitrile/Latex	12 lines	1.2 bn	56 mil
F2B Refurbishment	4 th quarter 2019	Malaysia	Nitrile	4 lines	0.8 bn	70 mil
Total new capacity in 2019				50 lines	5.4 bn	297 mil*
F5A New Factory	1 st quarter 2020	Malaysia	Nitrile	20 lines	2.0 bn	95 mil
F40 New Factory 1 st Phase	1 st quarter 2020	Malaysia	Nitrile	22 lines	2.2 bn	131 mil
F41 New Factory 1 st Phase	2 nd quarter 2020	Vietnam	PVC	40 lines	4.0 bn	208 mil
F40 New Factory 2 nd Phase	3 rd quarter 2020	Malaysia	Nitrile	16 lines	1.6 bn	81 mil
F8A New Factory 1 st Phase	4 th quarter 2020	Thailand	Nitrile	28 lines	2.8 bn	197 mil
F42 New Factory 1 st Phase	4 th quarter 2020	Malaysia	Nitrile	48 lines	4.8 bn	307 mil
Total new capacity in 2020				174 lines	17.4 bn	1,019 mil*
Total expansion				224 lines	22.8 bn	1,316 mil*
Total by December 2020 : 38 glove factories				872 lines	83.3 bn	

HLIB Research, Top Glove

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Aug	FY17	FY18	FY19f	FY20f	FY21f
Cash	240.1	164.2	351.3	409.7	419.9
Receivables	419.3	671.3	608.1	655.0	714.3
Inventories	315.8	513.7	464.6	483.8	526.0
PPE	1,523.4	2,082.2	2,230.7	2,391.1	2,634.5
Others	437.7	1,842.0	1,836.3	1,835.7	1,836.1
Assets	2,936.3	5,273.4	5,491.1	5,775.3	6,130.7
Payables	418.8	485.3	506.4	527.3	573.2
Debt	415.8	915.9	2,213.2	2,213.2	2,213.2
Others	-834.6	-1401.2	159.8	159.8	159.8
Liabilities	-	-	2,879.4	2,900.3	2,946.2
Shareholder's eq	62.5	4.5	2,599.1	2,859.8	3,166.2
Minority interest	2,003.3	2,404.5	12.6	15.2	18.3
Equity	9.2	10.6	2,611.7	2,875.1	3,184.5

Cash Flow Statement

FYE Aug	FY17	FY18	FY19f	FY20f	FY20f
Profit before tax	383.1	522.7	487.9	638.8	748.3
D&A	111.8	146.0	181.5	194.5	198.9
Working capital	(272.0)	(198.5)	91.1	(86.9)	(147.4)
Taxation	(65.5)	(36.8)	(87.6)	(114.7)	(134.5)
Others	(6.3)	(35.3)	29.8	28.9	76.8
CFO	151.2	398.2	702.7	660.5	742.2
Capex	(482.9)	(458.4)	(329.0)	(354.3)	(441.6)
Others	306.2	(1,233.3)	(12.5)	(12.9)	(15.0)
CFI	(176.7)	(1,691.7)	(316.5)	(341.4)	(426.6)
Changes in debt	(28.6)	1,471.7	-	-	-
Dividends	(181.7)	(196.1)	(199.1)	(260.7)	(305.4)
Others	(2.9)	(9.1)	-	-	-
CFF	(206.6)	1,284.6	(199.1)	(260.7)	(305.4)
Net cash flow	(0.9)	(63.0)	187.1	58.4	10.2
Forex	17.8	(12.9)	-	-	-
Others	-	-	-	-	-
Beginning cash	223.2	240.1	164.2	351.3	409.7
Ending cash	240.1	164.2	351.3	409.7	419.9

Income Statement

FYE Aug	FY17	FY18	FY19f	FY20f	FY21f
Revenue	3,409.2	4,214.0	4,699.3	5,061.4	5,520.1
EBITDA	458.3	653.6	707.9	871.3	983.1
EBIT	346.5	507.5	526.3	676.8	784.2
Finance cost	(6.3)	(35.3)	(59.5)	(59.0)	(56.9)
Associates & JV	(1.0)	1.7	1.3	1.3	1.3
Profit before tax	383.1	522.7	487.9	638.8	748.3
Tax	(54.7)	(85.4)	(87.6)	(114.7)	(134.5)
Net profit	328.4	437.3	400.3	524.0	613.8
Minority interest	(0.1)	(3.7)	(2.0)	(2.6)	(3.1)
Core PATMI	328.2	433.5	398.3	521.4	610.8
Exceptionals	(3.7)	14.3	-	-	-
Reported PATMI	324.4	447.7	398.3	521.4	610.8
Consensus Core PATMI	NA	NA	515.8	573.2	648.8
HLIB/Consensus	NA	NA	-23%	-9%	-6%

Valuation & Ratios

FYE Aug	FY17	FY18	FY19f	FY20f	FY21f
Core EPS (sen)	12.8	16.9	15.6	20.4	23.9
P/E (x)	38.0	28.7	31.2	23.9	20.4
EV/EBITDA (x)	27.5	22.2	20.2	16.3	14.5
DPS (sen)	7.3	8.5	8.5	10.2	12.0
Dividend yield (%)	1.5	1.7	1.7	2.1	2.5
BVPS (RM)	0.8	0.9	1.0	1.1	1.2
P/B (x)	6.2	5.2	4.8	4.3	3.9
EBITDA margin	13.4	15.5	15.1	17.2	17.8
EBIT margin	10.2	12.0	11.2	13.4	14.2
PBT margin	11.2	12.4	10.4	12.6	13.6
Net margin	9.6	10.4	8.5	10.4	11.1
ROE	16.2	18.6	15.3	18.2	19.3
ROA	11.2	8.2	7.3	9.0	10.0
Net gearing	6.8	85.2	71.6	63.1	56.6

Assumptions

FYE Dec	FY17	FY18	FY19f	FY20f	FY21f
Utilization rate (%)	80.0	85.0	80.0	80.0	80.0
MYRUSD	4.2	4.1	4.2	4.2	4.2

Disclaimer

The information contained in this report is based on data obtained from sources believed to be reliable. However, the data and/or sources have not been independently verified and as such, no representation, express or implied, are made as to the accuracy, adequacy, completeness or reliability of the info or opinions in the report.

Accordingly, neither Hong Leong Investment Bank Berhad nor any of its related companies and associates nor person connected to it accept any liability whatsoever for any direct, indirect or consequential losses (including loss of profits) or damages that may arise from the use or reliance on the info or opinions in this publication.

Any information, opinions or recommendations contained herein are subject to change at any time without prior notice. Hong Leong Investment Bank Berhad has no obligation to update its opinion or the information in this report.

Investors are advised to make their own independent evaluation of the info contained in this report and seek independent financial, legal or other advice regarding the appropriateness of investing in any securities or the investment strategies discussed or recommended in this report. Nothing in this report constitutes investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate to your individual circumstances or otherwise represents a personal recommendation to you.

Under no circumstances should this report be considered as an offer to sell or a solicitation of any offer to buy any securities referred to herein.

Hong Leong Investment Bank Berhad and its related companies, their associates, directors, connected parties and/or employees may, from time to time, own, have positions or be materially interested in any securities mentioned herein or any securities related thereto, and may further act as market maker or have assumed underwriting commitment or deal with such securities and provide advisory, investment or other services for or do business with any companies or entities mentioned in this report. In reviewing the report, investors should be aware that any or all of the foregoing among other things, may give rise to real or potential conflict of interests.

This research report is being supplied to you on a strictly confidential basis solely for your information and is made strictly on the basis that it will remain confidential. All materials presented in this report, unless specifically indicated otherwise, are under copyright to Hong Leong Investment Bank Berhad. This research report and its contents may not be reproduced, stored in a retrieval system, redistributed, transmitted or passed on, directly or indirectly, to any person or published in whole or in part, or altered in any way, for any purpose.

This report may provide the addresses of, or contain hyperlinks to websites. Hong Leong Investment Bank Berhad takes no responsibility for the content contained therein. Such addresses or hyperlinks (including addresses or hyperlinks to Hong Leong Investment Bank Berhad own website material) are provided solely for your convenience. The information and the content of the linked site do not in any way form part of this report. Accessing such website or following such link through the report or Hong Leong Investment Bank Berhad website shall be at your own risk.

1. As of 19 June 2019, Hong Leong Investment Bank Berhad has proprietary interest in the following securities covered in this report:

(a) -

2. As of 19 June 2019, the analyst(s) whose name(s) appears on the front page, who prepared this report, has interest in the following securities covered in this report:

(a) -

Published & printed by:

Hong Leong Investment Bank Berhad (10209-W)

Level 28, Menara Hong Leong,

No. 6, Jalan Damanlela,

Bukit Damansara,

50490 Kuala Lumpur

Tel: (603) 2083 1800

Fax: (603) 2083 1766

Stock rating guide

BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% over the next 12 months.
SELL	Expected absolute return of -10% or less over the next 12 months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result in a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating guide

OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next 12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

The stock rating guide as stipulated above serves as a guiding principle to stock ratings. However, apart from the abovementioned quantitative definitions, other qualitative measures and situational aspects will also be considered when arriving at the final stock rating. Stock rating may also be affected by the market capitalisation of the individual stock under review.