Top Glove Corporation

Losses Widen in 1QFY23

UNDERPERFORM ↔

Price:	**RM0.785**
Target Price:	**RM0.60** ↔

By Raymond Choo Ping Khoon l pkchoo@kenanga.com.my

TOPGLOV's 1QFY23 results disappointed due to lower-than-expected sales volume. The group anticipate the current challenging environment to persist into 2023 and only expect to return to profitability in 9-12 months. We now project a net loss of RM356m in FY23 (from a net profit of RM177m previously). We also cut our FY24F net profit forecast by 77% and maintain our asset-based TP of RM0.60 and UNDERPERFORM call.

TOPGLOV disappointed with a second consecutive quarterly loss. It registered a net loss of RM168m in 1QFY23 compared to our full-year net profit forecast of RM177m and the full-year consensus net profit estimates of RM133m. The variance against our forecast came largely from the weaker-than-expected sales volume.

QoQ, 1QFY23 revenue fell 36% due to lower ASP (-8%) and sales volume (-32%). It plunged to a loss of RM62m at the EBITDA level due to: (i) excess capacity leading to reluctance of customers to commit to sizeable orders and hold substantial stocks on expectations of further decline in prices, (ii) the sale of high-priced inventory at falling market prices which could well mean that certain shipments were sold at a loss, and (iii) reduced economies of scale, particularly, poor cost absorption, as its utilisation rate has halved to 30% from 60% three months ago. As a result, 1QFY23 losses widened to RM168m compared to RM53m in 4QFY22. No dividend was declared in this quarter as expected.

YoY, 1QFY23 revenue fell 61% due to lower ASP (-34%) and volume sales (-48%) with utilisation plunging to 30% from 65%-70% in 1QFY22.

The key takeaways from the analyst briefing yesterday are as follows:

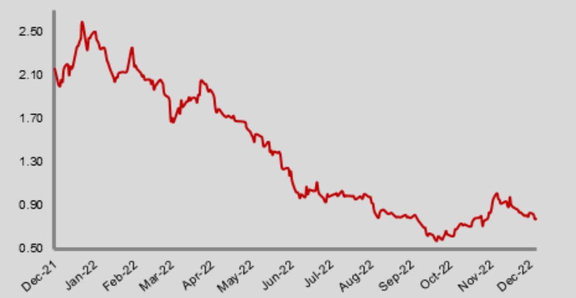
1. TOPGLOV anticipates the current challenging environment to persist into 2023 and only expect to return to the black in 9-12 months. Specifically, the group hope to narrow its losses at the EBITDA level in 2QFY23, turn EBITDA positive in 3QFY23 and break even or return to the black from 4QFY23.

2. TOPGLOV said that that the rate of decline in glove ASPs is slowing. We are unsure if this is sustainable as we gathered from sources that Chinese players are still undercutting by selling as low as USD14-16 per 1,000 pieces.

3. It said that there has been an uptick in orders for delivery in Dec 2022 and Jan 2023, boosting its utilisation rate to 40% from 30% in 1QFY23. Similarly, we are unsure if this is sustainable given the massive overcapacity out there and buyers generally are still unwilling to place sizeable orders or hold substantial stocks on expectations of further decline in prices.

4. The group now mainly run the newer and more efficient factories under its stable while temporarily shutting down the old and less efficient ones. It has embarked on initiatives to boost operational efficiency and rationalise costs to mitigate the impact from the topline contraction including internal mobility from manufacturing to surgical glove sterilisation and chemical divisions, as well as active mobilisation of foreign labour between plants to reduce idle time.

Share Price Performance



KLCI	1,483.17
YTD KLCI change	-5.4%
YTD stock price change	-69.7%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TOPG MK EQUITY
Market Cap (RM m)	6,285.8
Shares Outstanding	8,007.3
52-week range (H)	2.59
52-week range (L)	0.57
3-mth avg daily vol:	85,012,200
Free Float	44%
Beta	1.6

Major Shareholders

Tan Sri Dr Lim Wee Chai	27.8%
Central Depository Pte Ltd	7.7%
Firstway United Corp	6.9%

Summary Earnings Table

FY Aug (RM m)	2022A	2023F	2024F
Turnover	5573	4109	4280
PBT	365	-378	121
Net Profit (NP)	236	-356	41
Core NP	236	-356	41
Consensus NP		176	313
Earnings Revision		-301%	-77%
EPS (sen)	2.9	-4.3	0.5
EPS growth (%)	(97.1)	(250.9)	(111.6)
NDPS (sen)	1.2	0.0	0.3
BVPS (RM)	0.68	0.65	0.65
PER (x)	27.3	(18.1)	155.9
PBV (x)	1.1	1.2	1.2
Net gearing (x)	Net Cash	Net cash	Net cash
Net Div. Yield (%)	1.7	NA	0.3

Outlook. MARGMA holds the view that: (i) the global demand for rubber gloves is expected to return to growth in 2023 averaging between 12%-15% per annum, after a 19% contraction to an estimated 399b pieces in 2022, and (ii) as such, supply-demand equilibrium will return in 6-9 months. However, we are less optimistic and expect oversupply to persist over the next 12-24 months.

Based on our estimates, the demand-supply situation will only start to head towards an equilibrium in 2025 (against MARGMA's forecast of a supply-demand equilibrium in six to nine months) when there is virtually no more new capacity coming onstream while the global demand for gloves continues to rise by 15% per annum underpinned by rising hygiene awareness. Our supply-demand projections are pointing towards a persistent oversupply over the next two years. As a result of massive capacity expansion by incumbent players as well as new players during the pandemic years - enticed by super fat margins that had eventually evaporated —we estimate that the global glove manufacturing capacity is poised to jump by 22% to 511b pieces in 2022 (see chart on page 2).

On the other hand, as more countries come out the other end of the pandemic, we project the global demand for gloves to ease by 19% in 2022 to 399b pieces (partly also due to the destocking activities along the distribution network). This will result in an excess supply of 112b pieces (assuming, hypothetically, capacity utilisation is maximised). In 2023, we estimate that the global glove manufacturing capacity will surge by another 16% to 595b pieces (as more capacity planned during the pandemic years finally come on-line) while the global demand for gloves resume its organic growth of 15% annually (taking our cue from MARGMA's projection of 10%-15% growth in global glove demand yearly), resulting in the excess supply rising further to 137b pieces.

In 2023, we estimate that the global glove manufacturing capacity will surge by another 16% to 595b pieces (as more capacity planned during the pandemic years finally comes on-line) while the global demand for gloves resumes its organic growth of 15% annually (taking our cue from MARGMA's projection of 10-15% growth in global glove demand yearly), resulting in the excess supply rising further to 150b pieces. Based on our estimates, the demand-supply situation will only start to head towards equilibrium in 2025 when there is virtually no more new capacity coming onstream while the global demand for gloves continues to rise by 15% per annum underpinned by rising hygiene awareness.

Forecasts. We now project a net loss of RM356m in FY23 (instead of a profit of RM177m) as we reduce our utilisation assumption to 40% from 60%. We cut our FY24F net profit by 77% as we reduce our utilisation assumption to 45% from 60%.

We reiterate our **UNDERPERFORM** call and TP of RM0.60 based on 0.9x FY23F BVPS, at a 50% discount to the sector's average of 1.7x during the last downturns in 2008-2011 and 2014-2015 as we believe the current downturn could go down in history as one of the deepest ever. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 3).

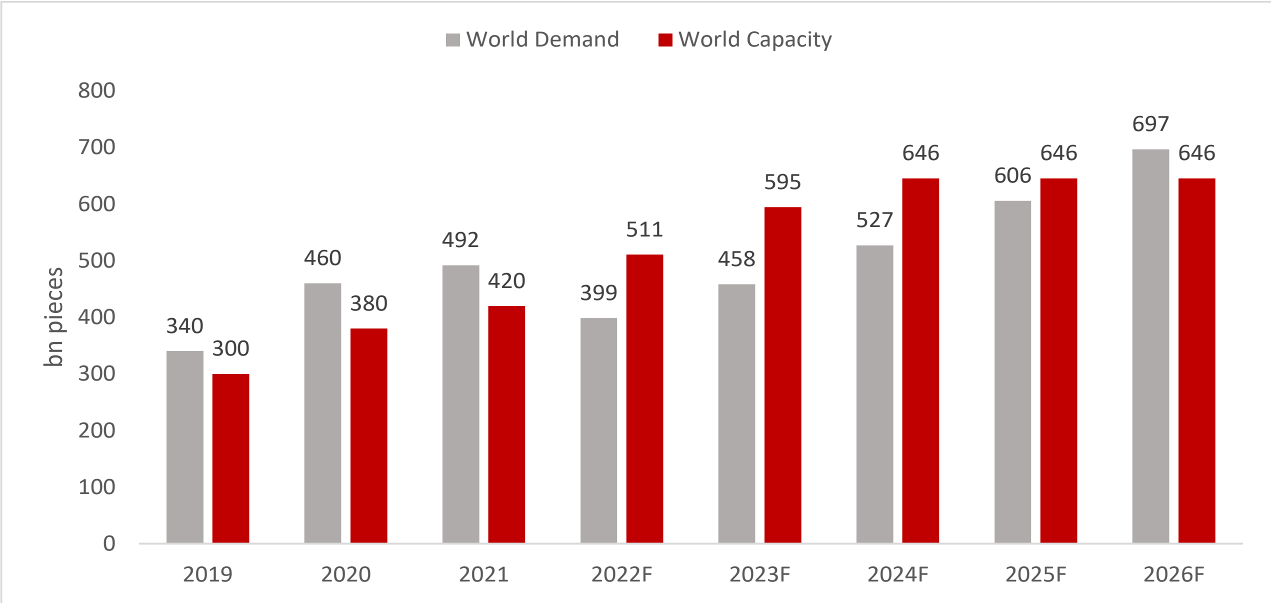
Key risks to our recommendation: (i) the industry turning the corner sooner on stronger-than-expected growth in demand for gloves driven by rising hygiene standards and health awareness globally, (ii) industry consolidation reducing competition among players, and (iii) epidemic and pandemic occurrences.

Results Highlights

FY Aug (RM m)	4Q FY22	1Q FY22	1Q FY23	YoY Chg %	QoQ Chg %
Turnover	990.1	1,611.1	632.5	(60.7)	(36.1)
EBITDA	48.4	344.2	(61.6)	(117.9)	(227.2)
EBIT	(41.3)	260.6	(149.6)	(157.4)	262.6
PBT	(44.0)	258.8	(151.6)	(158.6)	244.4
PATAMI (NP)	(52.6)	185.7	(168.2)	(190.6)	219.9
EPS (sen)	-0.7	2.3	-2.1	NM	210.9
EBITDA margin (%)	4.9	21.4%	-9.7%		
PBT margin (%)	-4.4	16.1%	-24.0%		
NP margin (%)	-5.3	11.5%	-26.6%		
Effective tax rate (%)	5.2	21.8%	-3.9%		

Source: Company, Kenanga Research, Bursa Malaysia

Estimated Global Demand/Supply - Excess Supply over CY22-CY24



Source: Kenanga Research

Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	☆		
	Corporate Social Responsibility	★	★	★		
	Management/Workforce Diversity	★	★	★		
	Accessibility & Transparency	★	★	★	☆	
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	☆		
SPECIFIC	Migrant Worker Welfare	★	★	★	☆	
	Pollution Control/Waste Management	★	★	★		
	Automation/Industry 4.0	★	★	★		
	Energy Efficiency	★	★	★		
	Work Site Safety	★	★	★		
	Set-off for Single-Use Product	★				
	OVERALL	★	★	★		

☆ denotes half-star
★ -10% discount to TP
★★ -5% discount to TP
★★★ TP unchanged
★★★★ +5% premium to TP
★★★★★ +10% premium to TP

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net. Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
HARTALEGA HOLDINGS BHD	UP	1.57	1.39	-11.5%	5,365	Y	03/2023	5.0	5.9	-95%	18%	31.1	26.5	1.0	3.3%	3.0	1.9%
KOSSAN RUBBER INDUSTRIES	UP	1.10	0.850	-22.7%	2,807	Y	12/2022	6.4	6.6	-94%	4%	17.3	16.6	0.7	4.0%	3.0	2.7%
SUPERMAX CORP BHD	UP	0.810	0.700	-13.6%	2,142	Y	06/2023	3.2	3.3	-88%	1%	25.2	24.8	0.4	1.8%	1.0	1.2%
TOP GLOVE CORP BHD	UP	0.785	0.600	-23.6%	6,286	Y	08/2023	(4.3)	0.5	-251%	-88%	N.A.	155.9	1.2	-6.4%	0.0	0.0%

Source: Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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