

Top Glove Corporation Berhad

(7113 | TOPG MK) Health Care | Health Care Equipment & Services

Well-positioned to capture the sudden surge in demand

KEY INVESTMENT HIGHLIGHTS

- **2QFY20 earnings came in at RM115.7m (+9.3%yoy) in view of higher sales volume and better margins of nitrile gloves**
- **Despite the dragged from natural rubber glove, 1HFY20 earnings performance met our and consensus expectations**
- **The group has closed the 2QFY20 quarterly performance with a solid balance sheet and stronger cash flow position**
- **We expect a solid 2HFY20 performance as we believe the group has the capacity to meet the sudden spike in demand**
- **Upgrade to BUY with a revised TP of RM6.63**

Earnings met expectations. Top Glove's 2QFY20 earnings came in at RM115.7m. This translates into earnings expansion of +9.3%yoy and +3.8%qoq respectively. Cumulatively, this bring its 1HFY20 earnings to RM227.1m (+5.2%yoy), which met our and consensus full-year FY19 earnings estimates at 46.0% and 47.8% respectively. For 2HFY20, we expect an even stronger earnings performance as the Covid-19 crisis has led to an increasing awareness and usage of glove products.

Nitrile rubber glove continue to be the key earnings driver. The improvement in 2QFY20 earnings was mainly attributable to the: (i) strong increase in sales volume of Nitrile rubber glove by +14.0%yoy and; (ii) lower average nitrile latex price which down by -8.3%yoy. On the contrary, sales volume for natural rubber glove was reduced by -6.0%yoy while its profit margin was further compressed by the surge of natural rubber latex concentrate (+19.0%yoy). The subdued performance of natural rubber glove segment was mitigated by the solid performance of Nitrile rubber glove segment given the latter's contribution to revenue has surpassed the former.

Well prepared to deal with the surge in sales order. Initially, the Coronavirus-led demand came mainly from China, Hong Kong, Singapore and South Korea. The management indicated that they have recently received surge in sales order from Europe and US as well following the Covid-19 spread to these regions. We estimate that the sales volume for FY20 could rose by more than +25.0%yoy to about 70.0b pieces per annum. Capacity-wise, Top Glove is able to produce about 73.4b pieces per annum at present. We understand that the group is prepared to further ramp-up production close to 100.0% to meet the surge in demand. Nonetheless, it will add a capacity of 8.2b by end of CY20 to support the higher demand.

Stronger balance sheet position. The net gearing had reduced to 0.24x as at 2QFY20 (vs 0.90x as at 1QFY20) resulting from the issuance of RM1.3b perpetual Sukuk which will be utilised to refinance existing borrowings. Accordingly, we project a better cash flow position going forward driven by a lower finance cost as well as receipt of RM245.0m for the full settlement of Aspion case. In addition, the group will continue to enjoy lower tax expense as it benefits from tax incentives from its ongoing expansion and unutilised tax allowance from its subsidiaries.

Upgrade to BUY

(Previously NEUTRAL)

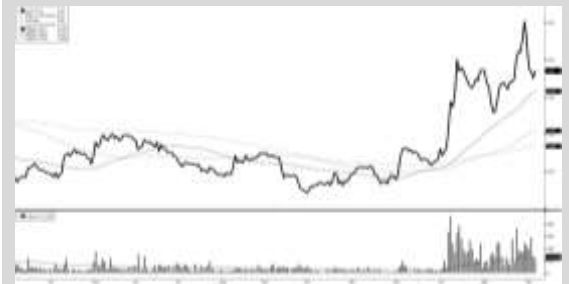
Revised Target Price: RM6.63

(Previously RM4.58)

RETURN STATISTICS

Price @19 th March 2020 (RM)	5.85
Expected share price return (%)	+13.3
Expected dividend yield (%)	+2.0
Expected total return (%)	+15.3

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	10.38	38.91
3 months	24.47	60.56
12 months	27.73	76.37

KEY STATISTICS

FBM KLCI	1,219.72
Syariah compliant	Yes
Issue shares (m)	2,559.81
Estimated free float (%)	48.56
Market Capitalisation (RM'm)	14,985.43
52-wk price range	RM4.21 - RM6.69
Beta vs FBM KLCI (x)	0.14
Monthly velocity (%)	11.02
Monthly volatility (%)	17.40
3-mth average daily volume (m)	13.56
3-mth average daily value (RM'm)	77.19
Top Shareholders (%)	
Lim Wee Chai	26.92
FIRSTWAY UNITED CORP	7.18
Employees Provident Fund Board	4.81

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Impact to earnings. We are revising our FY20, FY21 and FY22 earnings forecast upwards by +6.4%, +6.2% and +5.4% respectively to take into account the: (i) sudden increase in sales order; (ii) an improved profit margin for Nitrile rubber glove segment attributable to the lower raw material price and; (iii) reduction in interest expense.

Table 1: Top Glove's expansion plan for calendar year 2020 and 2021

Plants	Commence production by (Calendar qtr)	Country	Glove type	Number of production lines	Capacity (bn pcs per annum)
Current:					
34 glove factories			All	711.0	73.4
Expansion in progress: Glove					
F40 New factory 1st Phase	2QCY20	Malaysia	Nitrile	22.0	2.7
F41 New factory 1st Phase	3QCY20	Vietnam	PVC	20.0	2.0
F8A New factory 1st Phase	4QCY20	Thailand	Nitrile	28.0	3.5
Total new capacity end 2020				70.0	8.2
F40 New Factory 2nd Phase	1QCY21	Malaysia	Nitrile	16.0	2.0
F42 New factory 1st Phase	1QCY21	Malaysia	Nitrile	24.0	3.0
F41 New factory 2nd Phase	4QCY21	Vietnam	PVC	20.0	2.0
F45 New factory 1st Phase	4QCY21	Malaysia	Nitrile	20.0	2.5
Total new capacity end 2021				80.0	9.5
Total capacity (39 factories)				861.0	91.1

Source: Company, MIDFR

Target price. Consequently, our TP is revised to **RM6.63** (previously RM4.58) per share as we rolled forward our valuation to FY21 EPS of 22.1sen pegged to a revised PER of 30.0x (previously 25.0x). The PER represents the company's updated three-year historical average PER.

Upgrade to BUY. We view that Top Glove's outlook will continue to be underpinned by stronger growth in demand of disposable medical glove as hygiene standard become more stringent due to the Covid-19 outbreak worldwide. In addition, we expect the group is in the best position to capture the sudden surge in global demand as it has additional capacity available in comparison to other major glove manufacturers. Furthermore, the recent plunge in oil price augurs well for the group given that Nitrile latex cost which now command a substantial portion of its total cost of raw material could remain subdued. Coupled with a stronger balance sheet and improving cash flow position, we are upgrading our call recommendation on the stock to **BUY** (previously Neutral). 

INVESTMENT STATISTICS

Financial year ending 31st August (in RM'm, unless otherwise stated)	FY2018	FY2019	FY2020E	FY2021F	FY2022F
Revenue	4220.7	4801.1	5576.3	6183.2	6504.5
PBT	522.8	423.6	608.7	655.5	689.6
PATANCI	428.8	364.7	525.5	565.8	595.2
EPS (sen)	16.7	14.2	20.5	22.1	23.2
EPS Growth (%)	29.7	-15.0	44.1	7.7	5.2
PBT margin (%)	12.4	8.8	10.9	10.6	10.6
PATANCI margin (%)	10.2	7.6	9.4	9.2	9.2
PER (x)	34.4	40.4	28.0	26.0	24.8
Dividend per share (sen)	8.0	7.5	10.5	11.5	12.0
Dividend yield (%)	1.4	1.3	1.8	2.0	2.1

Source: Company, MIDFR

Table 1: Top Glove's quarterly earnings review

FYE Aug (RM'm)	Quarterly results			Cumulative results		
	2QFY20	YoY (%)	QoQ (%)	1HFY20	1HFY19	YoY (%)
Revenue	1,229.8	6.0	1.7	2,438.9	2,421.9	0.7
Operating expenses	(1,091.6)	6.5	1.4	(2,168.4)	(2,138.4)	1.4
Other operating income	11.2	7.3	19.6	20.5	21.6	(4.9)
Finance costs	(18.2)	(8.6)	(3.0)	(36.9)	(38.5)	(4.3)
Share of results of associates	(0.8)	nm	>(100)	1.8	0.8	122.7
Profit Before Tax	130.4	3.9	3.9	255.8	267.3	(4.3)
Taxation	(14.4)	(23.6)	4.9	(28.1)	(49.0)	(42.7)
Profit After Tax	116.0	8.8	3.8	227.8	218.3	4.3
Non-controlling interests	0.3	(62.8)	(0.6)	0.7	2.5	(73.6)
PATAMI	115.7	9.3	3.8	227.1	215.8	5.2
Basic EPS (sen)	4.5	9.2	3.7	8.9	8.0	10.7
PBT margin (%)	10.6	(2.0)	2.2	10.5	11.0	(5.0)
PAT margin (%)	9.4	2.6	2.1	9.3	9.0	3.6
PATAMI margin (%)	9.4	3.1	2.1	9.3	8.9	4.5
Effective tax rate (%)	11.0	(26.5)	0.9	11.0	18.3	(40.2)

Source: Company, MIDFR

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.