

# GLOVES

**Maintain NEUTRAL**

## Positive earnings outlook largely priced in

### KEY INVESTMENT HIGHLIGHTS

- **1QCY20 earnings beat expectations due to surge in demand for gloves.**
- **Expanding production capacity to meet higher demand**
- **Margin to continue expanding in 2QCY2020**
- **Earnings forecast revised higher as we expect upward revision of ASP to be strong**
- **Top Glove (BUY, TP: RM26.12) is the top pick for the sector**
- **Maintain NEUTRAL on the sector as we see positive earnings outlook were largely priced in**

**1QCY20 earnings beat expectations due to surge in demand for gloves.** Three out of four gloves producers under our coverage reported better than expected earnings in 1QCY2020, boosted by increase in average selling price (ASP) of gloves and higher sales volume of gloves. The widening of Covid-19 outbreak worldwide and its incessant nature has led to higher demand for gloves which resulted in upward revision in ASP. The surge in demand for gloves has resulted in demand outstripping supply and longer delivery lead times. Besides, earnings of glove makers were also helped by lower raw material prices and strengthening of USD. This has resulted in margin expansion of glove produces in 1QCY20.

**Expanding production capacity to meet higher demand.** Glove makers are expanding their production capacity to meet the growing demand for gloves. Notably, production capacity of Top Glove is expected to grow by 36% from 73.8b pieces in 3QFY20 to 100.4b pieces in 4QFY21. Similarly, Hartalega will continue with its NGC capacity expansion plan whereby annual installed capacity is expected to increase from current 38.1b to 43.7b pieces by FY22. Meanwhile, Plant 19 of Kossan Rubber has so far commissioned 6 production lines beginning January while all 10 lines are expected to fully commissioning by June 2020. Lastly, Supermax is expanding its production capacity with 3 plants under construction. The 3 plants would increase Supermax's installed capacity by 12b pieces from 26.18b gloves to 38.18b gloves by CY2022.

**Margin to continue expanding in 2QCY2020.** Profit margins of glove makers are expected to continue expand due to: (i) continuous upward revision in ASP, (ii) strengthening of US Dollar, and (iii) subdued raw material prices. Glove makers are expected to continue revise ASP higher due to the robust demand for gloves. Impact of upward revision of gloves ASP will be more significant in 2QCY2020 as ASP of gloves were set few months before delivery time hence the spike in ASP for the period February to April will be reflected in 2QCY2020. Besides, glove makers are the main beneficiaries of stronger US Dollar as gloves are priced in US Dollar. Meanwhile, prices of raw material such as nitrile-butadiene rubber (NBR) is expected to remain subdued due to the trade

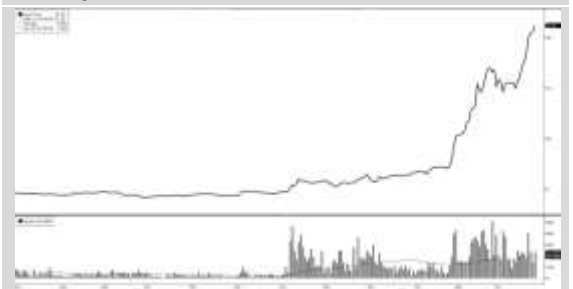
### COMPANY IN FOCUS

#### Top Glove Corporation Berhad

Upgrade to **BUY** | Revised Target price: RM26.12  
Price @ 9<sup>th</sup> July 2020: RM21.18

- Strong earnings in 9MFY20 on higher sales of gloves and lower raw material prices
- ASP of gloves will be higher in 4Q20 as demand for gloves remains strong
- Record earnings year expected for FY20 and FY21

#### Share price chart

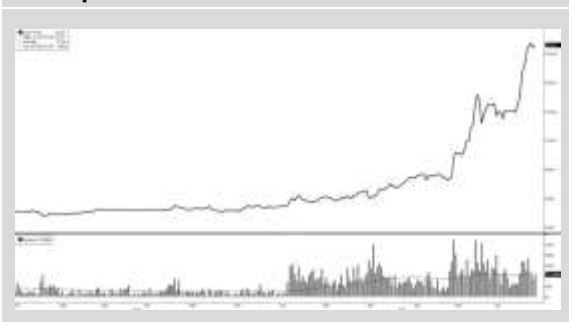


#### Hartalega Holdings Berhad

Maintain **NEUTRAL** | Revised Target price: RM15.69  
Price @ 9<sup>th</sup> July 2020: RM16.60

- FY20 earnings were little-changed as higher sales volume were mitigated by lower ASP of gloves
- ASP of gloves expected to grow at double digit in 1HFY21 due to strong demand for gloves
- Annual installed capacity is expected to increase to 43.7 billion pieces by FY22.

#### Share price chart

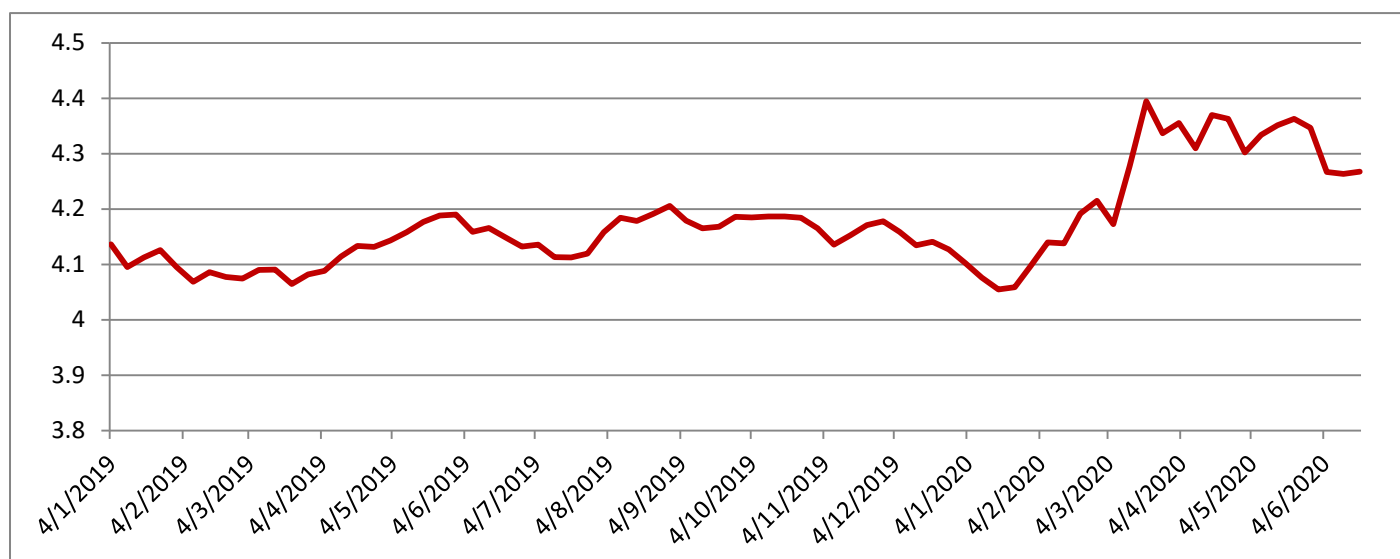


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war tension. On the other hand, prices of natural rubber latex have been trending upwards recently due to wintering season which we are not overly concern as the increase in ASP is more than enough to offset the increase in raw material prices.

**Figure 1: USD Exchange Rate**



Source: Bloomberg, MIDF Research

**Earnings forecast revised higher as we expect upward revision of ASP to be strong.** We gather that upwards revision in ASP of gloves is remains encouraging in June to September due to strong demand for gloves. ASP of gloves is expected to revise higher at double-digit on monthly basis which should translate into strong earnings in 3QCY2020. As such, we are revising our earnings forecast for glove makers under our coverage to take into account of the strong ASP. Earnings forecast for Top Glove Corp is revised higher by 10.6%/57.9%/39.6% for FY20/21/22F while earnings estimate for Hartalega is revised higher by 37.4%/38.9% for FY21/22F. Similarly, earnings estimate for Supermax is adjusted higher by 34.8%/81.4%/75.2% for FY20/21/22F while earnings forecast for Kossan Rubber is revised upwards by 16.3%/28.1%/29.8% for FY20/21/22F.

**Figure 2: Investment Statistics for Top Glove Corporation**

FYE Aug (RM'm)	FY2018	FY2019	FY2020E	FY2021F	FY2022F
<b>Revenue</b>	<b>4220.7</b>	<b>4801.1</b>	<b>8364.5</b>	<b>11129.8</b>	<b>9756.8</b>
PBT	522.8	423.6	1328.1	1803.2	1483.2
<b>PATANCI</b>	<b>428.8</b>	<b>364.7</b>	<b>1146.4</b>	<b>1556.5</b>	<b>1280.3</b>
EPS (sen)	16.7	14.2	44.7	60.7	50.0
EPS Growth (%)	29.7	-15.0	214.4	35.8	-17.7
PBT margin (%)	12.4	8.8	15.9	16.2	15.2
PATANCI margin (%)	10.2	7.6	13.7	14.0	13.1
PER (x)	126.6	148.8	47.3	34.9	42.4
Dividend per share (sen)	8.0	7.5	22	30	25
Dividend yield (%)	0.4	0.4	1.1	1.4	1.2

Source: MIDF Research

**Figure 3: Investment Statistics for Hartalega Holdings**

Financial year ending 31st March (in RM'm, unless otherwise stated)	FY2018	FY2019	FY2020	FY2021F	F2022F
<b>Revenue</b>	<b>2405.6</b>	<b>2827.2</b>	<b>2961.3</b>	<b>5351.7</b>	<b>6021.5</b>
Cost of goods sold	-1790.9	-2119.0	-2328.6	-3962.6	-4444.7
<b>Gross profit</b>	<b>614.8</b>	<b>708.2</b>	<b>595.4</b>	<b>1389.1</b>	<b>1576.8</b>
Finance costs	-7.9	-10.6	-10.8	-18.7	-24.1
<b>Profit before tax</b>	<b>526.4</b>	<b>550.8</b>	<b>556.3</b>	<b>1019.8</b>	<b>1156.8</b>
<b>Core PATANCI</b>	<b>439.6</b>	<b>474.0</b>	<b>472.6</b>	<b>836.2</b>	<b>948.6</b>
EPS (sen)	12.8	13.7	14.2	25.1	28.5
EPS Growth (%)	55.1	7.0	3.4	77.0	13.4
PER (x)	129.7	36.8	116.8	66.0	58.2
Dividend Per Share (sen)	5.9	8.2	7.6	9.5	10.3
Dividend yield (%)	0.4	0.5	0.5	0.6	0.6

Source: MIDF Research

**Figure 4: Investment Statistics for Supermax Corporation**

Financial year ending 30th June (in RM'm, unless otherwise stated)	2018A	2019A	2020E	2021F	2022F
<b>Revenue</b>	<b>1,304.5</b>	<b>1,538.2</b>	<b>2,433.3</b>	<b>3,362.9</b>	<b>3,308.1</b>
<b>Gross profit</b>	<b>169.9</b>	<b>186.6</b>	<b>414.7</b>	<b>586.6</b>	<b>570.4</b>
Finance costs	(14.0)	(19.7)	(31.2)	(43.1)	(42.4)
<b>PBT</b>	<b>161.9</b>	<b>172.4</b>	<b>394.3</b>	<b>558.4</b>	<b>542.7</b>
Taxation	(51.8)	(49.3)	(118.3)	(167.5)	(162.8)
<b>PATANCI</b>	<b>106.7</b>	<b>123.1</b>	<b>272.8</b>	<b>386.4</b>	<b>375.5</b>
EPS (sen)	8.1	9.4	20.8	29.5	28.6
EPS Growth (%)	58.7	15.4	121.6	41.7	(2.8)
PER (x)	152.9	132.4	59.8	42.2	43.4
Dividend (sen)	4.0	1.5	5.0	5.0	5.0
Dividend Yield (%)	0.3	0.1	0.4	0.4	0.4


Source: MIDF Research

**Figure 4: Investment Statistics for Kossan Rubber Industries**

Financial year ending 31st Dec (in RM'm, unless otherwise stated)	FY2018	FY2019	FY2020F	FY2021F	FY2022F
<b>Revenue</b>	<b>2144.2</b>	<b>2221.6</b>	<b>3301.8</b>	<b>3695.4</b>	<b>3893.4</b>
Operating Profit	264.7	290.6	551.7	627.9	651.1
PBT	250.2	280.1	535.2	609.4	631.7
<b>PATANCI</b>	<b>199.8</b>	<b>224.8</b>	<b>432.3</b>	<b>492.3</b>	<b>510.2</b>
Operating Profit margin (%)	12.3	13.1	16.7	17.0	16.7
PBT margin (%)	11.7	12.6	16.2	16.5	16.2
EPS (sen)	15.8	17.6	33.8	38.5	39.9
EPS Growth (%)	10.7	11.2	92.3	13.9	3.6
PER (x)	24.2	66.5	34.6	30.3	29.3
Dividend per share (sen)	6.0	7.0	9.0	10.0	10.0
Dividend yield (%)	1.4	0.6	0.8	0.9	0.9

Source: MIDF Research

**Top Glove is the top pick for the sector.** Post earnings revision, we upgrade **Top Glove to BUY from NEUTRAL** with a **revised target price (TP) of RM26.12** (previously RM17.30), pegging FY21F EPS of 60.8sen at PER of 43x. We value Top Glove at its upcycle PER of +1SD 3-year historical mean PER in view of the positive outlook for gloves demand. Meanwhile, we are keeping our **NEUTRAL** call for (i) **Hartalega** with a **revised TP of RM15.69** (previously RM8.78), pegging FY22 EPS of 28.5sen at PER of 55x, (ii) **Supermax Corporations** with a **revised TP of RM11.20** (previously RM4.09), pegging FY21 EPS of 29.5 at PER of 38x, and (iii) **Kossan Rubber** with a **revised TP of RM12.32** (previously RM9.00), pegging FY21 EPS of 38.5sen at PER of 32x. Note that we value glove makers at +1SD mean valuation due to upcycle in earnings.

**Maintain Neutral on gloves sector.** Overall, we expect earnings outlook for glove makers to remain positive in 2HCY2020 due to continuous upward revision in gloves ASP and favorable forex as well as raw material prices. We think that the tight supply situation in the gloves industry would continue in the medium term. Nevertheless, we believe that the positives have been largely priced in following the good run in share prices of glove counters. Hence, we maintain **NEUTRAL** on the sector. 

### PEER COMPARISON TABLE

Stock	FYE	Rec.	Price @ 9-July-2020	Tgt Price (RM)	Core EPS		Core PE (sen)		Net DPS		Net Dvd Yield	
					FY20A	FY21F	FY20A	FY21F	FY20A	FY21F	FY20A	FY21F
Top Glove Corp	Aug	BUY	21.18	26.12	44.7	60.7	47.4	34.9	22.0	30.0	1.0%	1.4%
Hartalega Holding	March	NEUTRAL	16.60	15.69	14.2	25.1	116.9	66.1	7.6	9.5	0.5%	0.6%
Supermax Corp	June	NEUTRAL	12.44	11.20	20.8	29.5	59.8	42.2	5.0	5.0	0.4%	0.4%
Kossan Rubber Industries	Dec	NEUTRAL	11.680	12.32	33.8	38.5	34.6	30.3	9.0	10.0	0.8%	0.9%

Source: MIDF Research

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#### STOCK RECOMMENDATIONS

<b>BUY</b>	Total return is expected to be >10% over the next 12 months.
<b>TRADING BUY</b>	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.
<b>NEUTRAL</b>	Total return is expected to be between -10% and +10% over the next 12 months.
<b>SELL</b>	Total return is expected to be <10% over the next 12 months.
<b>TRADING SELL</b>	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

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