

14 June 2018 | Sector Update

Gloves Sector

Maintain NEUTRAL

Minimal increase in natural gas tariff

INVESTMENT HIGHLIGHTS

- Natural gas tariff increased minimally from RM32.52/MMBtu to RM32.69/MMBtu
- Negligible impact on earnings
- Maintain NEUTRAL on the sector


Minimal increase in natural gas tariff from RM32.52/MMBtu to RM32.69/MMBtu. On 13 June 2018, **Gas Malaysia Berhad (BUY, TP: RM3.50)** announced that the government has approved the revision of natural gas tariff for the non-power sector in Peninsular Malaysia from 1 July 2018 to 31 December 2018. The tariff revision is in line with the national rationalisation plan and Gas Cost Pass Through (GCPT) mechanism that includes the revision of piped gas price taking place every six months, as indicated by Suruhanjaya Tenaga. The increase in the natural gas tariff is due to the surcharge of RM0.77/MMBtu under the GCPT mechanism which will apply to all tariff categories during the said period. Hence, the average effective gas tariff will be revised from RM32.52/MMBtu to RM32.69/MMBtu. We are neutral on this revision as the increase in effective gas tariff is only +0.5% from the previous revised tariff.

Table 1: Revised natural gas tariff schedule

Tariff Category	Annual gas consumption (MMBtu)	Existing Base Tariff (RM/MMBtu)	Revised Base Tariff after GCPT 1 January – 30 June 2018 (RM/MMBtu)	Base Tariff Effective 1 July– 31 December 2018 (RM/MMBtu)	Revised Effective Tariff after GCPT (RM/MMBtu)
A	Residential	22.30	23.92	23.03	23.80
B	0-600	28.78	30.40	29.73	30.50
C	601-5,000	28.93	30.55	29.88	30.65
D	5,001-50,000	29.22	30.84	30.19	30.96
E	50,001-200,000	30.48	32.10	31.49	32.26
F	200,001-750,000	30.48	32.10	31.49	32.26
L	Above 750,000	31.50	33.12	32.55	33.32
Average		30.90	32.52	31.92	32.69

Source: Gas Malaysia, MIDFR

Negligible impact on earnings. Most of the major glove players fall within the category F and L where according to our calculation will experience on average <1.0% increment in effective gas tariff from the previous tariff. On average, natural gas constitutes of about 10-12% of the total glove production costs for the glove producers under our coverage. Hence, according to our calculations all four glove producers under our coverage will have negligible impact on earnings of about <1.0% arising from this latest revision in natural gas tariff as the increase in effective gas tariff is only +0.5% compared to the previous period. In addition, we believe that the impact on the glove producers will be fairly minimal as the glove producers will be passing on the cost increase to their customers which will in turn result in higher average selling prices (ASPs).

Maintain NEUTRAL on the sector. All factors considered, we are making no changes to our recommendations, earnings estimate and target price of the gloves producers under our coverage at this juncture. Despite a positive outlook for the rubber gloves sector this year, we are of the opinion that the near term prospects for some of the rubber glove producers will remain subdued due to the constraint in terms of capacity. This is largely due to the delay in capacity expansion for some of the producers caused by incomplete parts of the production lines. Moreover, the upside earnings potential of these producers might be capped due to closure of some production lines for upgrades and revamps. Hence, we are maintaining our **NEUTRAL** stance on the sector in view of the capacity constraint as well as; the lack of strong catalysts for the sector at this juncture with **Supermax** as our Top Picks for the sector. We like Supermax for its: (i) attractive valuation at 11.4x FY19F PER vs its peers of >20x FY19F PER; (ii) revamp of older production lines which helped to boost productivity and; (iii) efficient cost management. 

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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.