Top Glove Corporation Berhad

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

***Downgrade* SELL**

Bottoming ASPs and utilisation rate

***Revised* Target Price: RM0.54**

(Previously RM1.01)

KEY INVESTMENT HIGHLIGHTS

- **12MFY22 earnings were below expectations.**
- **Negative 4QFY22 earnings.**
- **Core profits for 12MFY22 fell by -97.7%yoy to RM175.2m**
- **Postponed new expansion plans for CY23/CY24/CY25.**
- **Earnings reduced by -38.4%/-39.7% for FY23F/FY24F.**
- **Downgrade to SELL (from NEUTRAL) with a revised TP of RM0.54 (from RM1.01)**

12MFY22 earnings were below expectations. Top Glove Corporation ("Top Glove") reported a core PATANCI of RM175.2m in 12MFY22. This is after excluding a one-time-off item of RM60.8m. The results came in below ours and consensus estimation at 51% of ours and 58.3% of streets' FY22F. The key variance was mainly due to lower-than-expected deals from the customer which resulted in weaker sales volume and utilization rate. No dividend was declared for the quarter to preserve cash.

Negative 4QFY22 earnings. Top Glove's revenue slumped -52.3%yoy and -32.4%qoq to RM990.1m in 4QFY22. The negative performance was largely due to the lower average selling price (ASPs) for gloves and reduced orders from customers. Despite softer demand, the group recorded a remarkable pick up in sales from North America (+98%yoy). This is due to low-base effect as the group was only permitted to be cleared and allowed to begin exporting and selling gloves to the US effective 10 September 2021. Meanwhile, Top Glove recorded core net loss of RM80.7m in 4QFY22 against core net profit of RM441.4 in 4QFY21, mainly due to higher production costs as a result of global supply chain disruptions and the inflationary effect. Quarterly, the group's core net loss of -RM80.7m in line with a negative operating profit margin of -4.2% from +2.8%. The poor performance was attributed to several factors, including lower ASPs (-5.4%qoq), reduced sales volume (-35%qoq), increased natural gas tariff (+10% qoq), the full effects of the increased minimum wage, as well as higher packaging materials and chemicals cost.

Core profits for 12MFY22 fell by -97.7%yoy to RM175.2m, in tandem with reduced revenue of RM5.57b (-65.9%yoy). The weaker revenue was caused by lower sales volume and ASPs. Nitrile gloves made up 39% of the overall sales volume during FY22, which was less than FY21's 44%. This is followed by NR powdered gloves, NR powdered-free gloves, Vinyl/PE/CPE, and surgical gloves at 27%/26%/5%/3%. In 12MFY22, operating profit margin decreased by -54.6ppt yoy to 6.7%, mostly due to higher natural gas tariff (+60%yoy) and higher minimum wage.

RETURN STATISTICS	
Price @ 20th September 2022 (RM)	0.69
Expected share price return (%)	-22.07
Expected dividend yield (%)	2.08
Expected total return (%)	**-19.99**

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-20.1	-18.0
3 months	-33.2	-30.6
12 months	-75.1	-74.1

KEY STATISTICS	
FBM KLCI	1461.10
Syariah compliant	Yes
Issue shares (m)	8,006.95
F4BGM Index	Yes
ESG Grading Band (Star rating)	☆☆☆
Estimated free float (%)	44.38
Market Capitalisation (RM'm)	5,565.10
52-wk price range	RM0.68 - RM3.43
Beta vs FBM KLCI (x)	1.16
Monthly velocity (%)	0.19
Monthly volatility (%)	29.01
3-mth average daily volume (m)	56.68
3-mth average daily value (RM'm)	52.28
Top Shareholders (%)	
Lim Wee Chai	27.66
Central Depository Pte Ltd/The	7.65
FIRSTWAY UNITED CORP	6.93

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Decreased sales volume across the product range. In 4QFY22, sales volume fell by -35%qoq due to supply-demand mismatches, and weaker demand from buyers amid stockpiles in customers' warehouses. Natural rubber glove sales fell by -44%qoq in 4QFY22 as customers switched to nitrile gloves in search of lower pricing. Despite a change in demand from natural rubber gloves to nitrile gloves, nitrile glove sales volume declined by -26%qoq as customers lacked the urgency to place bulk purchases in anticipation of a further drop in ASPs and a reduction in delivery time.

Declining ASPs and utilization rate. The blended ASP in 4QFY22 was at USD24 per 1000 pieces, which is slightly higher than the pre-pandemic level of USD21-USD23 per 1000pieces. The intense competition from Chinese glovemakers and the exceptionally cheap pricing from those glovemakers who are exiting the market caused the ASP for nitrile gloves to fall by 10%qoq in 4QFY22. Utilization rate decreased to 30%–40% throughout the quarter, resulting in an average of 50% for FY22. Currently, the industry's average utilization rate is below 50%. In view of the stabilizing ASPs, the group increased its ASP by 5% for October 2022 to pass through the cost. We think that the group has limited room to fully pass on the cost to the customer by further raising the selling prices on the back of the supply-demand mismatches and intense price competition from Chinese and Thai glovemakers.

Decent raw material prices ahead. In 4QFY22, the average natural latex concentrate price decreased 10%qoq to RM5.85/kg (USD1.4/kg) and nitrile latex price dropped 5%qoq to USD1.05/kg. Moving forward, the group expects natural latex concentrate price to at USD1.03/kg for October 2022, supported by rising yields but declining demand and consumption for glove manufacturing. The nitrile latex price expected at USD0.93/kg for October 2022, eased by the deferred capacity expansion and lower production by glovemakers.

Postponed new expansion plans for CY23/CY24/CY25 by -10/-15/-16b pieces to match glove supply and demand. The group expects total production capacity for CY23/CY24/CY25 to be at 100b/104b/115b pieces. With the deferred new expansion plans, the group anticipates a capital expenditure (CAPEX) of RM470m for FY23. Management expects 46% of FY23F's CAPEX is expected to fund current construction projects and renovations of existing facilities to automate and improve the manufacturing and packaging processes, while 27% will be devoted to improving the supply of houses. The construction of the Kenangan Meru Apartment that will provide room for about 2000 employees once completed in December 2022 would cost a total of 11% of FY23's capex budget. The remaining 16% of the budget is allocated for supplemental capital expenses.

Earnings reduced by -38.4%/-39.7% for FY23F/FY24F. In view of the earnings that missed our expectations, we lower our earnings projections for FY23F and FY24F to reflect lower sales volume expectations. This is after factoring in a lower utilization rate of 47.1% for FY23F and 53.8% for FY24F.

Downgrade to SELL (from NEUTRAL) with a revised TP of RM0.54 (from RM1.01) given the downward earnings adjustment in this report. Our valuation is based on FY24F earnings of 4.0sen multiplied by PER multiple 13.5x, slightly above its 2-year historical average PE of 13.2x. We believe that the group has limited capacity to completely pass on the cost going forward by increasing the ASPs since the customer can simply switch to other glovemakers. The demand-supply dynamics are anticipated to continue in the near term as more countries enter endemic phases, which weaken demand. Potential upside risk: (i) increased in ASP and sales volume; (ii) smaller players leaving the market and (iii) industry consolidation due to low valuation. The dividend yield is estimated at 2.2% for FY23F.

INVESTMENT STATISTICS

FYE AUG (RM'm)	FY2020	FY2021	FY2022A	FY2023F	FY2024F
Revenue	7,237.4	16,361.4	5,572.5	4,600.4	5,708.8
Cost of sales	(4,387.0)	(5,259.3)	(4,653.0)	(3,822.2)	(4,719.3)
Gross profit	**2,850.4**	**11,102.1**	**919.5**	**778.3**	**989.5**
Interest income	23.9	61.6	20.8	17.1	21.3
Other operating income	33.1	83.3	28.4	23.4	29.1
Distribution and selling costs	(155.0)	(253.7)	(161.6)	(135.4)	(169.7)
Administrative and general expenses	(551.0)	(958.0)	(433.7)	(360.9)	(452.3)
Operating profit	**2,201.4**	**10,035.4**	**373.6**	**322.6**	**417.8**
Finance costs	(34.4)	(4.2)	(4.4)	(6.2)	(7.0)
Share of gain/(loss) of associate	(1.4)	2.6	(3.7)	0.0	0.0
PBT	**2,165.6**	**10,033.8**	**365.5**	**316.3**	**410.9**
Income tax expense	(376.7)	(2,209.8)	(73.2)	(63.4)	(82.2)
PAT	**1,788.8**	**7,824.0**	**292.2**	**253.0**	**328.7**
PATANCI	1,778.2	7,761.7	236.0	251.2	326.4
Core PATANCI	**1,768.5**	**7,741.1**	**175.2**	**251.2**	**326.4**
EPS (sen)	21.9	96.9	2.9	3.1	4.0
Dividend per share (sen)	11.8	65.1	1.4	1.5	2.0
Dividend yield (%)	17.1	94.3	2.1	2.2	2.9
Growth & Valuation (%)					
Revenue Growth	50.7	126.1	(65.9)	(17.4)	24.1
Gross Profit Growth	222.4	289.5	(91.7)	(15.4)	27.1
Core PATANCI Growth	374.6	337.7	(97.7)	43.4	29.9
Gross Profit Margin	39.4	67.9	16.5	16.9	17.3
PBT Margin	29.9	61.3	6.6	6.9	7.2
Core PATANCI Margin	24.4	47.3	3.1	5.5	5.7
Effective tax rate	17.4	22.0	20.0	20.0	20.0
PER (x)	3.2	0.7	24.0	22.5	17.3
Net debt/Total Equity (%)	NET CASH	NET CASH	NET CASH	NET CASH	NET CASH
Cash/Mkt Cap (x)	11.7	7.2	0.8	1.2	1.5

Source: Company, MIDFR

Table 1: Top Glove's quarterly earnings review

FYE AUG (RM'm)	Quarterly results					Cumulatively results		
	4QFY22	3QFY22	4QFY21	YoY (%)	QoQ (%)	12MFY22	12MFY21	YoY (%)
Revenue	**990.1**	**1,464.6**	**2,074.9**	**(52.3)**	**(32.4)**	**5,572.5**	**16,361.4**	**(65.9)**
Operating expenses	(1,073.4)	(1,468.3)	(1,499.4)	(28.4)	(26.9)	(5,318.9)	(6,471.0)	(17.8)
Other operating income	42.0	45.1	46.4	(9.5)	(6.9)	120.0	144.9	(17.2)
Operating profit	**(41.3)**	**41.5**	**621.9**	**(106.6)**	**(199.5)**	**373.6**	**10,035.4**	**(96.3)**
Finance cost	(1.3)	(1.0)	(1.1)	22.7	28.7	(4.4)	(4.2)	5.3
Share of result of associate	(1.4)	(2.0)	(0.2)	815.5	(30.3)	(3.7)	2.6	(240.3)
Profit before tax (PBT)	**(44.0)**	**38.4**	**620.6**	**(107.1)**	**(214.7)**	**365.5**	**10,033.8**	**(96.4)**
Income tax expense	2.3	(9.1)	(150.0)	(101.5)	(125.2)	(73.2)	(2,209.8)	(96.7)
Profit after tax (PAT)	**(41.7)**	**29.3**	**470.6**	**(108.9)**	**(242.6)**	**292.2**	**7,824.0**	**(96.3)**
Perpetual Sukuk	11.7	1.6	12.9	(9.2)	640.7	50.2	51.4	(2.3)
Non-controlling interests	(0.9)	12.4	10.3	(108.8)	(107.3)	6.1	62.3	(90.2)
PATANCI	**(52.6)**	**15.3**	**447.4**	**(111.8)**	**(443.9)**	**236.0**	**7,710.3**	**(96.9)**
EI	(28.1)	(23.9)	(6.0)	365.1	17.5	(60.8)	(37.3)	63.0
Core PATANCI	**(80.7)**	**(8.6)**	**441.4**	**(118.3)**	**834.9**	**175.2**	**7,673.0**	**(97.7)**
Basic EPS (sen)	0.7	0.2	7.6	(91.3)	247.4	3.0	95.9	(96.9)
Growth & Margin (%)				*+/(-) ppts*	*+/(-) ppts*			*+/(-) ppts*
Revenue Growth	(32.4)	1.1	(50.2)	17.8	(33.5)	23.9	14.5	9.4
Operating Profit Growth	(199.5)	(63.3)	(76.1)	(123.4)	(136.3)	(9.9)	6.6	(16.6)
Core PATANCI Growth	834.9	(109.3)	(78.0)	912.9	944.2	(31.8)	6.3	(38.0)
Operating Profit Margin	(4.2)	2.8	30.0	(34.1)	(7.0)	6.7	61.3	(54.6)
PBT Margin	(4.4)	2.6	29.9	(34.4)	(7.1)	6.6	61.3	(54.8)
Core PATANCI Margin	(8.1)	(0.6)	21.3	(29.4)	(7.6)	3.1	46.9	(43.8)
Ratios & Valuation				*+/(-) ppts*	*+/(-) ppts*			*+/(-) ppts*
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net debt/total equity (%)	NET CASH	NET CASH	NET CASH	n.m.	n.m.	NET CASH	NET CASH	n.m.
Net cash/market cap (%)	0.7	0.5	7.5	(6.8)	0.2	0.7	7.5	(6.8)
Effective tax rate (%)	5.2	23.7	24.2	(19.0)	(18.5)	20.0	22.0	(2.0)

Table 2: SEGMENTAL BREAKDOWN

FYE AUG (RM'm)	Quarterly results					Cumulatively results		
	4QFY22	3QFY22	4QFY21	YoY (%)	QoQ (%)	12MFY22	12MFY21	YoY (%)
Revenue								
Malaysia	918.0	1,272.5	1,974.0	(1,056.0)	(354.5)	4,813.3	13,940.4	(9,127.1)
Thailand	90.1	124.1	78.0	12.1	(34.0)	446.4	1,201.6	(755.1)
China	6.4	4.8	17.6	(11.2)	1.5	30.7	429.9	(399.3)
Others	60.0	63.2	46.8	13.2	(3.2)	282.1	831.0	(548.9)
Total Revenue	**1,074.4**	**1,464.6**	**2,116.4**	**(1,041.9)**	**(390.2)**	**5,572.5**	**16,403.0**	**(10,830.4)**
Operating Income:								
Malaysia	(40.7)	31.8	728.0	(768.7)	(72.5)	297.2	8,918.7	(8,621.5)
Thailand	5.5	37.3	22.6	(17.1)	(31.8)	104.5	833.1	(728.6)
China	(4.1)	(4.5)	(7.2)	3.1	0.4	(8.8)	220.0	(228.8)
Others	(2.0)	(23.2)	(13.7)	11.7	21.2	(19.3)	172.3	(191.6)
Total Income	**(41.3)**	**41.5**	**729.8**	**(771.0)**	**(82.7)**	**373.6**	**10,144.2**	**(9,770.6)**

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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 *rise* 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 *fall* 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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology