Hartalega Holdings Berhad

(5168 | HART MK) Main | Health Care| Health Care Equipment & Services

Retiring Bestari Jaya's Manufacturing Plant

Maintain **NEUTRAL**

Revised **Target Price: RM1.75**

(Previously RM1.80)

KEY INVESTMENT HIGHLIGHTS

- **Decommissioning manufacturing plants**
- **Challenging near-to-midterm outlook remains**
- **Positive from the long-term perspective**
- **Healthy balance sheet**
- **Revised earnings projections for FY23F-25F**
- **Maintain NEUTRAL with a revised TP of RM1.75 (previously RM1.80)**

Decommissioning manufacturing plants. Hartalega announced the shutdown of the Bestari Jaya manufacturing plant and consolidating operations at the Next Generation Integrated Glove Manufacturing Complex in Sepang. The decommissioning is anticipated to close down four (4) manufacturing facilities with 40 production lines by end of CY2023. The total production capacity will be reduced from 44b gloves to 31b gloves.

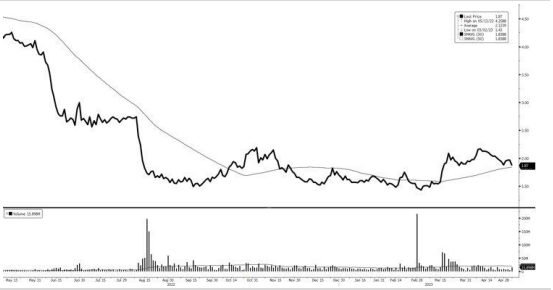
Challenging near-to-midterm outlook remains. We are negative on the announcement as it signals challenging near-to-middle term outlook for gloves sector due to the ongoing oversupply of glove situation. Moreover, the impairment loss of RM347m for FY23F and provision for retrenchment costs and contract obligation expenses of RM70m for FY24F will further raise input costs and compress margins. While the reduction in production capacity to improve utilization rates, but the continuous oversupply of gloves will likely limit any improvements.

Positive from the long-term perspective. On a longer term, the decommissioning of less efficient production plants is anticipated to reduce operating and depreciation costs, which would then lead to improved operational efficiency. Note that the Bestari Jaya plant, as compared to the NGC, is (1) less efficient, (2) constrained by outdated technology, and (3) generates greater energy, labour, and maintenance expenses. This was due to the age of the facility. While the oversupply of gloves in the market remains a concern in the near-to-middle term outlook, we believe the decommissioning may increase cost effectiveness and competitiveness in the long-term.

Healthy balance sheet. The group possesses a healthy net cash position of RM1.76b, which is equivalent to 27.5% of the total market capitalization. This demonstrates that the group has a healthy balance sheet to support the closure of the plants in Bestari Jaya and finance the consolidation at NGC.

RETURN STATISTICS	
Price @ 8th May 2023 (RM)	1.87
Expected share price return (%)	-6.6
Expected dividend yield (%)	0.00
Expected total return (%)	**-6.6**

SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	-8.8	-9.2
3 months	-1.6	26.2
12 months	-57.2	-53.3

INVESTMENT STATISTICS

FYE Mar	2023E	2024F	2025F
Revenue	2,249.5	1,488.1	1,776.1
EBITDA	270.1	76.5	228.0
Profit before tax (PBT)	(200.1)	(114.4)	107.3
Core PATANCI	103.4	(66.0)	87.8
Core EPS (sen)	3.0	(1.9)	2.6
DPS (sen)	0.0	0.0	1.6
Dividend Yield (%)	0.0	0.0	0.9

KEY STATISTICS	
FBM KLCI	1,433.74
Issue shares (m)	3427.61
Estimated free float (%)	38.13
Market Capitalisation (RM'm)	6,390.65
52-wk price range	RM1.4 – RM4.5
3-mth average daily volume (m)	21.17
3-mth average daily value (RM'm)	36.98
Top Shareholders (%)	
Hartalega Industries Sdn Bhd	34.39
BUDI TENGGARA SDN BHD	8.63
Employees Provident Fund Board	4.97

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Revised earnings projections for FY23F-25F. We lowered our earnings forecasts for FY23F-25F by 34.7%/ -131.5%/-70.8% to reflect the challenging near-to-midterm outlook. This was after factoring a low average selling price (ASP), reduced total production capacity, and lower sales volume. As such, we expect a net loss in the final quarter of FY23F, and a net loss for FY24F. These projections reflect the challenging situation for the glove sector, which include post-pandemic demand normalisation and oversupply due to aggressive capacity expansion by existing players and new entrants during the pandemic period.

Maintain NEUTRAL with a revised TP of RM1.75 (previously RM1.80). Our revised **TP** of **RM1.75** is based on its 2-year historical -1SD P/BV of 1.2x multiplied by a revised FY24F BVPS of 145.5sen. Hence, retain **NEUTRAL**. Despite the anticipated increase in utilization rates following the decommissioning, we believe that the improvement is limited in the near-term due to the normalization of demand post-pandemic and the oversupply of gloves leading to limited buying interest. As such, we remain cautious that the supply-demand dynamic will take 1-2 years to return to normal resulting in a soft average selling price (ASP) and demand for gloves. In addition, rising energy and labor costs, combined with low utilization rates, will increase the production cost per unit and compress profit margins, leading to anticipated net losses for 4QFY23F and FY24F. However, the group's solid net cash position of RM1.76b provides protection against potential downside risks, and the decommissioning initiative has the potential to increase production efficiency and reduce operational costs in the long run. **Upside risks** are: (1) further exits of new and existing players from the market, (2) fluctuations in raw material prices and currency exchange rates, and (3) potential increased demand due to the emergence of new variants or diseases.

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023E	2024F	2025F
Revenue	6,703.5	7,888.3	2,249.5	1,488.1	1,776.1
Cost of Sales	(2,605.5)	(3,093.1)	(1,837.6)	(1,292.2)	(1,399.3)
Gross Profit	**4,098.0**	**4,795.1**	**411.9**	**195.9**	**376.8**
Other Income	8.2	3.4	11.4	7.9	11.4
Distribution expenses	(44.4)	(65.3)	(23.2)	(18.4)	(21.5)
Administrative expenses	(249.3)	(159.8)	(106.1)	(89.8)	(112.6)
Other operating expenses	(37.8)	(23.7)	(23.9)	(19.0)	(26.1)
EBITDA	**3,912.8**	**4,701.6**	**270.1**	**76.5**	**228.0**
EBIT	**3,774.8**	**4,549.7**	**(214.9)**	**(132.8)**	**88.7**
Profit before tax (PBT)	**3,773.9**	**4,555.5**	**(200.1)**	**(114.4)**	**107.3**
Tax expense	(909.6)	(1,394.6)	(43.5)	(24.8)	(19.5)
Profit After tax (PAT)	**2,864.2**	**3,160.9**	**(243.6)**	**(139.3)**	**87.8**
Core PATANCI	**2,845.9**	**3,123.5**	**103.4**	**(66.0)**	**87.8**
Basic EPS (sen)	84.4	94.3	(7.1)	(4.1)	2.6
Core EPS (sen)	83.3	91.4	3.0	(1.9)	2.6
DPS (sen)	51.0	53.5	0.0	0.0	1.6

Balance Sheet (RM'm)	2021A	2022A	2023E	2024F	2025F
Property,plant and equipment	2,156.4	2,367.0	2,152.2	2,236.2	2,363.4
Intangible assets	32.6	30.8	40.5	44.6	48.0
Total Non-current assets	**2,451.8**	**3,150.1**	**3,152.3**	**3,248.9**	**3,389.5**
Inventories	633.5	396.9	260.2	274.4	267.5
ST - Trade and other receivables	1,110.7	418.6	218.1	209.2	212.2
Cash and cash equivalents	2,668.7	2,378.1	2,009.5	1,949.2	1,978.5
Total current assets	**4,414.2**	**3,197.3**	**2,491.4**	**2,435.0**	**2,460.5**
Total Assets	**6,866.0**	**6,347.4**	**5,643.7**	**5,683.9**	**5,850.0**
Total Equity	**4,999.1**	**5,124.6**	**4,924.1**	**4,973.3**	**5,123.6**
LT Lease Liabiltiies	2.1	3.2	2.2	1.3	1.5
LT Loans and borrowings	250.1	136.7	95.7	100.4	103.5
Total Non-current liabilities	**450.3**	**385.7**	**300.4**	**310.1**	**335.9**
ST Trade and other payables	1,091.3	378.2	303.7	320.3	319.1
ST Loans and borrowings	92.9	102.1	71.5	75.1	77.3
Total Current Liabilities	**1,416.6**	**816.8**	**419.3**	**400.5**	**390.6**
Total Liabilities	**1,866.9**	**1,202.5**	**719.7**	**710.6**	**726.4**

Cash Flow (RM'm)	2021A	2022A	2023E	2024F	2025F
Pretax profit	3,773.9	4,555.5	(200.1)	(114.4)	107.3
Cash flow from operations	3,088.2	3,716.4	474.8	44.6	192.7
Cash flow from investing	(345.7)	(810.0)	25.9	(70.3)	(113.3)
Cash flow from financing	(384.7)	(3,210.3)	(869.3)	(34.6)	(50.1)
Net cash flow	**2,357.8**	**(303.9)**	**(368.6)**	**(60.3)**	**29.2**
(+/-) Adjustments	5.8	13.3	0.0	0.0	0.0
Net cash/(debt) b/f	**305.2**	**2,668.8**	**2,378.1**	**2,009.5**	**1,949.2**
Net cash/(debt) c/f	**2,668.8**	**2,378.1**	**2,009.5**	**1,949.2**	**1,978.5**

Key Metrics	2021A	2022A	2023E	2024F	2025F
Cash/Market Capitalisation (sen)	41.8	37.2	31.4	30.5	31.0
Cash/share (sen)	78.1	69.6	58.8	57.0	57.9
P/BV ratio (x)	1.28	1.25	1.30	1.28	1.25

Profitability Margins	2021A	2022A	2023E	2024F	2025F
Gross Profit Margin (%)	61.1	60.8	18.3	13.2	21.2
EBIT Margin (%)	56.3	57.7	(9.6)	(8.9)	5.0
Core PATANCI Margin (%)	42.5	39.6	4.6	(4.4)	4.9

Source: Bloomberg, 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 *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