

27 September 2019

# Top Glove Corporation

## Competitive Pressure In Latex Gloves To Stymie Growth

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**FY19 PATAMI of RM370.6m (-13% YoY) came in below expectations, at 94%/90% of our/consensus full-year forecasts. The negative variance from our forecast is due to lower-than-expected margins for latex gloves due to competitive pressure. As such, we cut our FY20E net profit by 20%. Correspondingly, we also downgrade our TP from RM4.50 to RM4.00. Downgrade from MARKET PERFORM to UNDERPERFORM.**

**FY19 PATAMI of RM370.6m (-13% YoY) came in below expectations at 94%/90% of our/consensus full-year forecasts. The negative variance from our forecast is due to lower-than-expected margins for latex gloves due to competitive pressure. A 4.0 sen dividend per share was declared bringing FY19 DPS to 7.5 sen in line with expectation.**

**Key result highlights. QoQ, 4Q19** revenue came in flat (-0.1%) due to lower sales volume (-5%) but mitigated by higher ASP (+4%). PBT margin was flat at 6.8% despite higher ASP due to lower profit contribution from natural rubber glove segment due to lower sales volume in latex gloves and a small loss in the vinyl glove segment. This brings 4Q19 PATAMI to RM80.1m (+7.2%) boosted by a lower effective tax rate of 1.2% compared to 8.6% in 3Q19.

**YoY, FY19** revenue rose 14% due to higher sales volume (+10%) and ASP (+0.7%). However, PBT fell 17% mainly attributed to a sharp upward movement in the 3Q19 input natural latex price (+22%) and intense competition in the latex segment leading to lower margins which adversely impacted bottom line. As a result, FY19 PATAMI was lower by 13% cushioned by a lower effective tax rate of 13.3% compared to 16.3% in FY18.

**Intense competition in latex more than offset uptick in nitrile demand.** Looking ahead, the keen competition in the latex segment could negatively impact latex gloves margin. Although we are positive on growth in subsequent quarters underpinned by uptick in nitrile demand driven by re-stocking activities, the group is plagued with competitive pressure from low margins latex gloves (accounts for estimated 50% of product mix) which could offset the gains in the nitrile segment. The robust demand for nitrile gloves led to longer delivery lead times to between 45 to 50 days as compared to 30 to 40 days previously.

**Expansion plans.** Top Glove's capacity expansion includes: Factory 32 (Phases 2 to commence production by 4Q 2019; 1.2b pieces), Factory 2B (operational by 4Q19; 0.8b pieces), Factory 5A (operational by 1Q 2020; 2b pieces), Factory F40 (Phase 1 operational by 2Q 2020 and Phase 2 operational by 3Q 2020; 3.6b pieces), Factory F41 (operational 2Q 2020; 4b pieces PVC gloves) Factory F42 (operational by 4Q 2020; 4.8b pieces), and Factory 8A (operational by 4Q 2020 delayed from early 2020; 2.8b pieces) which will boost the group's total production capacity by 20.2b gloves per annum to 84.1b (+32%).

**Downgrade our FY20E net profit by 20%** due to the lower-than-expected pre-tax margin from 10% to 9%, no thanks to lower latex glove margin. We introduced FY21E NP into our earnings forecasts.

**Downgrade from MP to UP.** Correspondingly, our TP is cut from RM4.50 to RM4.00 based on unchanged 25.5x CY20E revised EPS of 15.8 sen (at +1.0SD above 5-year historical forward mean). Although we expect uptick in nitrile demand to anchor growth in subsequent quarters, the group overall profitability is plagued with competitive pressure from low margins latex gloves and a slow recovery at Aspion.

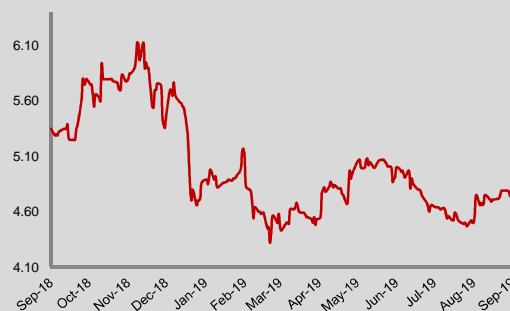
**A key upside risk to our call is the better-than-expected margin.**

**UNDERPERFORM** ↓

Price : **RM4.72**

Target Price : **RM4.00** ↓

### Share Price Performance



KLCI	1,593.00
YTD KLCI change	-5.8%
YTD stock price change	-15.7%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TOPG MK Equity
Market Cap (RM m)	12,082.3
Shares Outstanding	2,559.8
52-week range (H)	6.36
52-week range (L)	4.30
3-mth avg daily vol:	3,799,478
Free Float	46%
Beta	0.4

### Major Shareholders

Tan Sri Dr Lim Wee Chai	26.8%
Employees Provident Fund	7.2%
Firstway United Corp	6.7%

### Summary Earnings Table

FY Aug (RM'm)	2019A	2020E	2021E
Turnover	4801.8	5106.3	4825.6
PBT	430.7	463.1	516.4
<b>Net Profit (NP)</b>	<b>370.6</b>	<b>390.6</b>	<b>425.4</b>
<b>Core NP</b>	<b>370.6</b>	<b>390.6</b>	<b>425.4</b>
Consensus NP	-	485.9	557.4
Earnings Revision	-	-20%	NEW
EPS (sen)	14.5	15.3	16.7
EPS growth (%)	(15.5)	5.8	8.9
NDPS (sen)	7.5	7.5	7.5
BVPS (RM)	0.95	1.07	1.15
PER (x)	32.6	30.8	28.2
PBV (x)	5.0	4.4	4.1
Net gearing (x)	0.9	0.7	0.7
Net Div. Yield (%)	1.6	1.6	1.6

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<b>Result Highlight</b>								
	<b>4Q</b>	<b>3Q</b>	<b>QoQ</b>	<b>4Q</b>	<b>YoY</b>			<b>YoY</b>
<b>FY Aug (RM'm)</b>	<b>FY19</b>	<b>FY19</b>	<b>Chg %</b>	<b>FY18</b>	<b>Chg %</b>	<b>FY18</b>	<b>FY19</b>	<b>Chg %</b>
Turnover	1,189.6	1,190.2	(0.1)	1,223.6	(2.8)	4,220.7	4,801.8	13.8
EBITDA	151.8	154.8	(2.0)	201.2	(24.6)	699.1	706.8	1.1
EBIT	102.5	104.2	(1.6)	158.1	(35.2)	553.4	511.7	(7.5)
PBT	81.2	82.2	(1.3)	137.6	(41.0)	518.4	430.7	(16.9)
<b>PATAMI (NP)</b>	<b>80.1</b>	<b>74.7</b>	<b>7.2</b>	<b>92.3</b>	<b>(13.3)</b>	<b>424.4</b>	<b>370.6</b>	<b>(12.7)</b>
EPS (sen)	3.1	2.9	7.2	3.6	(13.3)	16.6	14.47	(12.8)
EBITDA margin (%)	12.8	13.0		16.4		16.7	14.7	
PBT margin (%)	6.8	6.9		11.2		12.4	9.0	
NP margin (%)	6.7	6.3		7.5		10.3	7.7	
Effective tax rate (%)	1.3	8.6		32.1		16.3	13.3	

*Source: Company, Kenanga Research, Bursa Malaysia*

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Peer Comparison																		
Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating	
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.				
<b>RUBBER GLOVES</b>																		
HARTALEGA HOLDINGS BHD	5.27	17707.2	Y	03/2020	3.7	6.2	11.6	6.7	38.1	34.1	32.0	7.8	6.9	20.3	1.3	5.85	OP	
KOSSAN RUBBER INDUSTRIES	4.26	5448.3	Y	12/2019	8.4	4.4	23.7	6.0	27.1	21.9	20.7	4.1	3.7	16.7	1.4	5.25	OP	
SUPERMAX CORP BHD	1.59	2077.0	Y	06/2020	2.8	6.0	4.1	6.3	17.0	16.3	15.4	1.9	1.8	11.1	2.5	1.75	OP	
TOP GLOVE CORP BHD	4.72	12082.3	Y	08/2020	6.3	-5.5	5.4	8.9	32.6	30.8	28.2	5.0	4.4	14.3	1.6	4.00	UP	

Source: Bloomberg, Kenanga Research

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**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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