TOP GLOVE WORKING ON DERIVING MORE SYNERGIES AFTER ASPION BUY

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Top Glove Corp Bhd

(June 20, RM11.36)

Maintain neutral with a higher target price of RM10.65: Top Glove Corp Bhd's revenue for its third quarter of financial year 2018 (3QFY18) grew 26.6% year-on-year (y-o-y) to RM1.1 billion, with a net profit of RM117.6 million (+51.3% y-o-y) owing to the historical-high y-o-y sales volume growth of 37% (partly contributed by Aspion). The strong demand growth, which stemmed particularly from Asia (where demand growth from India, China, and Vietnam surpassed 100% in its first nine months of FY18), Eastern Europe, the Middle East, and Latin America, was mainly supported by the increasing usage of gloves due to concern over the Ebola outbreak, rising healthcare awareness and hygiene standards, and the switching trend towards disposable gloves, especially in emerging markets. The high utilisation rate of close to 90% (compared with 80% in 3QFY17) coupled with an improvement in production efficiency led to better cost-efficiency, and hence the operating margin improved to 13.4%

in 3QFY18 (+2.7 percentage points).

Post completion of the acquisition on April 5, Aspion has contributed about two months' revenue of RM97 million to the group. However, the group's profit after tax was lowered by RM3 million with the acquisition as the finance cost and acquisition-related transaction cost outstripped Aspion's contribution. Currently the integration of the two businesses is in progress and Top Glove is working on deriving more synergies via cost savings and cross selling. Note that Aspion's utilisation rate is currently low at slightly below 70%.

Raw material prices were lower y-o-y, with average natural rubber and nitrile prices easing 38% and 14.2% to RM4.38/kg and US$1.15 (RM4.61)/kg respectively. On a quarter-on-quarter basis, the average natural rubber price eased 0.5% while the average nitrile price rose 8.5%. Meanwhile, for the natural gas tariff hike in the second half of calendar year 2018, the estimated impact is minimal with a less than 0.1% increase in total manufacturing cost.

The operation of factory F31 has been postponed to July 2018 (from June 2018), while F32 remains on schedule (operational by early-2019). Meanwhile, its condom manufacturing facility is expected to be operational by end-June 2018.

Vinyl gloves' average selling price (ASP) was driven up to the highest point in the period of March to May due to the temporary vinyl glove supply disruption. With the big boys in China slowly coming back to production, we believe the vinyl glove supply and ASP are expected to normalise starting from June onwards.

Top Glove aims to achieve a 30% glove market share in 2020. With current market share (post acquisition of Aspion) standing at 27%, the remaining 3% is expected to be achieved via both organic growth (such as capturing growth in emerging-market demand, penetrating into more markets, capacity growth, and improvement in manufacturing process) and inorganic growth (such as mergers and acquisitions or joint ventures).

We maintain our forecasts for FY18 but raise our earnings estimates by about 7% for FY19 and FY20 to account for stronger demand from emerging markets due to rising healthcare awareness and hygiene standards. *— PublicInvest Research, June 20*