M&A MOVE GOOD FOR TOP GLOVE

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Analyst says acquisition takes shorter time than setting up a factory

PETALING JAYA: Top Glove Corporation Bhd's move to explore the merger and acquisition (M&A) route would allow it to expand capacity for nitrile gloves at a quicker pace, says UOB Kay Hian.

A typical acquisition timeline of six months is relatively shorter compared to the one and a half to two years' timeframe required to commission a factory.

"Given the robust demand and huge substantial order backlogs for nitrile gloves, we believe that an M&A would be the right way to sustain its production growth momentum and it would also be in line with the group's expansion plan of achieving a 50% nitrile glove production mix, from the current 32%, over the next three to five years," added the research house.

On Wednesday, the cash-rich rubber glove manufacturer said that it would embark on at least one acquisition exercise by August this year and that it was already in talks with three parties in the rubber-related industry for the planned acquisition.

According to recent industry data, Malaysia’s cumulative nine months of 2015 (9M15) export volume of nitrile gloves had risen by 29.7% year-on-year (y-o-y).

This was largely attributed to the glove manufacturers’ aggressive push to fully utilise new nitrile glove capacity and higher market share gains by Malaysian glove makers as compared to industry players in neighbouring countries, especially Thailand.

Nevertheless, Top Glove, which traditionally focuses on latex gloves, had demonstrated the ability to compete effectively in the nitrile glove market with the group achieving a higher 9M15 nitrile glove export market share of 16.4% on the back of a higher-than-industry y-o-y nitrile glove export volume growth of 41.8%.

Although the expansive pipeline of capacity expansion plans for this segment had triggered lingering concerns on rising price competition, the group has expressed confidence that its continuous quality improvement, research and development (R&D) initiatives as well as the gradual revamp of production lines at older factories, would help the company expand its earnings before interest and tax (EBIT) margins to healthy 16%-18% levels.

Top Glove is targeting a 10% to 15% sales volume growth in financial year 2016 (FY16).

This is in line with Kenanga Research’s assumption of 10% growth and Maybank IB Research’s 13% growth in FY16.

“We believe a 10% volume growth in FY16 is achieveable due to the solid demand where Malaysia’s exports of rubber gloves rose 30% in 9M15.

“The 1% quarter-on-quarter volume growth in the first quarter of FY16 was largely due to the full utilisation for nitrile gloves, of which new capacity of 2bil pieces is coming on-stream by February 2016,” said

Kenanga Research.

The group’s sales volume growth expectation is premised on the positive demand for both latex and nitrile gloves, commissioning of a new nitrile plant in February 2016 and present plant utilisation rate of 80%.

The new nitrile plant is set to contribute 4% capacity growth to the group.

Top Glove has earmarked an estimated capex of RM150mil to RM200mil per annum for the building of a new factory and production lines.

Besides that, the management has plans to raise production capacity by an additional 7.8bil pieces of gloves to 52.4bil, by the end of February 2017.

Its two plants, namely F27 in Lukut, Port Dickson, and F30 in Klang, will focus on producing two billion and 4.4 billion pieces of nitrile gloves, respectively.

The additional 6.4 billion pieces per annum of new nitrile glove production capacity in the pipeline would boost Top Glove’s nitrile glove production capacity to 16.2bil pieces within the next three years.

Meanwhile, the F6 plant in Phuket, Thailand, will cater tor the production of 1.4 billion pieces of latex gloves.

Top Glove’s first quarter of FY16 revenue was driven by higher sales volume of 15%.

Nitrile gloves accounted for 32% of total product mix and continue to gather momentum, as compared to an average of 25% over the last few quarters.

“In terms of profitability, its quarter net profit rose more than 100% y-o-y due to higher mix of nitrile gloves and high utilisation rates for both nitrile and latex gloves, margin expansion emanating from more efficient production lines and automation of old lines, as well as a 31% US dollar appreciation against the ringgit,” said Kenanga Research.

Top Glove closed 0.29% lower at RM13.84 yesterday with 2.78mil shares done.