

TOP GLOVE EARNINGS IMPROVES ON HIGHER OPERATIONAL EFFICIENCY

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Top Glove Corp Bhd

(Oct 18, RM11.52)

Maintain neutral with an unchanged target price (TP) of RM10: To recap, Top Glove Corp Bhd's financial year 2018 (FY18) revenue and net profit grew 23.6% and 32% year-on-year (y-o-y) respectively. The robust performance was mainly driven by sales volume growth (+26% y-o-y) with a high utilisation rate (90%); improvement in operational efficiency and hence, lower cost; higher sales of latex gloves with lower natural rubber latex price; and a higher average selling price which offset the external factors impact.

The group's earnings before interest, taxes, depreciation and amortisation margin improved by 2.2 percentage points (ppts) to 16.4% mainly attributable to the improvement in operational efficiency through digitalisation and automation via the application of the Internet of things, robotics and automated real-time manufacturing system.

As a result, the group managed to derive 20% of gas energy savings in FY18, which minimised the 24% natural gas tariff hike impact. In addition, it is also reducing its reliance on workers with a 14% reduction in workers over the past 12 months, which resulted in the number of workers per million pieces of gloves falling from 2.9 workers to 2.5 workers (only include direct workers). The group has also improved its line speed by 10%.

In terms of product mix, latex gloves continued to account for the bulk at 51%, followed by nitrile gloves at 36%, vinyl/thermoplastic elastomer/cast polyethylene gloves at 11% and surgical gloves at 2%. We understand that the group prefers to have a balanced and diversified product mix in order to capture the demand growth from emerging markets which are more price sensitive.

By geography, the bulk of the group's sales growth in FY18 was mainly driven by developing regions (72%). This was led by Asia ex-Japan (+58%), Eastern Europe (+39.6%), Middle East (+38.7%) as well as Africa (+35.3%). For Asia ex-Japan especially, demand growth from China, India and Vietnam surpassed 100% in FY18, though coming from a small base.

China accounts for 4% of the group's total sales in FY18 (from 2% in FY17), while India made up 2% of the group's total sales in FY18 (from 1% in FY17).

We believe the growth was contributed by the rising healthcare awareness and hygiene standards in developing regions, the switching trends towards disposable gloves and the vinyl glove supply disruption in

China.

In line with the demand growth from developing regions, we note that Top Glove's latex powdered glove sales volume grew by 24% y-o-y in FY18 after three years of consecutive decline in sales volume. In addition, we understand that the sales growth in FY18 was mainly from its existing customer (90%).

Based on a five-year discounted cash flow projection, no impairment provision is required. The net projected profit for the impairment test range from RM40 million (FY19F forecast [FY19F]) to RM65 million (FY23F).

Note that impairment provision is required to be conducted every financial year end. With the help of technology and the group's track record and experience in turning around loss-making glove factories, Top Glove is confident of its ability to enhance Aspion's contribution going forward via the allocation of additional resources from Top Glove team, further improvement of glove production process, synergies and cost savings. —

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The Edge Markets