

PP14767/09/2012(030761)

Monday, May 30, 2016

Supermax Corporation Berhad

“Cheap but Sound Fundamentals”

Results Review

- Actual vs. expectations.** Supermax Corporation Berhad (Supermax) posted 5Q16 net profit of RM20 million (-21% y-o-y; with 1Q16 end-March results for comparative purposes) had pushed 15M16 earnings to RM147 million, which came in line with our estimates, making up 95% of our 15-month-calendarised FY16 earnings forecast. The lower earnings were generally dragged by faltering top-line as a result of weakening average selling price (ASP) in highly competitive environment. EPS registered a steep decline in growth of -21% y-o-y or -49% q-o-q to 2.9 sen.
- Dividend.** The Board declared an interim dividend of 4% or 2 sen payout, amounting to a total payout of 6 sen for FY16. Dividend yield stood at 2.3% based on the share price ending March 2016.
- Modest 5QFY16 results.** Supermax posted 5Q16 revenue of RM225 million (+1% y-o-y; -23% q-o-q) and EBITDA of RM44 million (+16% y-o-y ; -19% q-o-q), underpinned by intensified pricing competition in 5Q (ending March-2016) which point towards a decline from the topline all the way to the bottom line ranging from negative growth of -19 to -49% on quarterly basis. However, earnings improvement were seen on year-on-year basis due to stronger USD coupled with increased capacity output from new and refurbished production lines compared to preceding year.
- Raw material prices remained stable.** In Q1 CY16, natural rubber (NR) price dropped to RM3.71/kg (-5.8% y-o-y ; -2.3% q-o-q) while nitrile latex (NBR) price slid below USD1/kg at USD 0.97/kg (-2.8% y-o-y ; -4.7% q-o-q). Stabilized raw material prices during the quarter supported EBITDA margin and PBT margin at 19% (+2% y-o-y) and 15% (+2% y-o-y), respectively. Despite the effort made by some major rubber producing countries (Thailand, Malaysia and Indonesia) to shore up natural rubber (NR) prices by cutting export output, the results were proved unsustainable in

BUY (TP:RM2.94)

Current Price (RM)	RM2.57
New Target Price (RM)	RM2.94
Previous Target Price (RM)	RM2.28
Previous Recommendation	HOLD
Upside/(Downside) To Target	14%
Dividend Yield (FY16)	2%

Stock Code

Bloomberg	SUCB MK
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Stock Information

Listing	MAIN MARKET	
Sector	Glove	
Shariah Compliance	Yes	
Issued Shares (mn)	671.3	
Market Cap (RM mn)	1,725	
YTD Chg in Share Price	-10%	
Beta (x)	0.72	
52-week Hi/Low (RM)	3.56	1.93
3M Average Volume (shrs)	1.8mn	
Estimated Free Float	55%	

Major Shareholders

Kim Sim Thai	21%
Bee Geok Tan	15%
EPF	5%

May'16 after the NR prices retraced to RM4.48/kg in May from the YTD high of RM5.12/kg due to lacklustre demand and high inventory backlog.

Similarly, nitrile latex (NBR) prices also showed its consistency during the quarter (see chart 1 &2), staying at around USD1/kg level. This is crucial to many other glove players including Supermax as the industry has been ramping up capacity output for NBR gloves to cater for strong rising demand worldwide. We expect the NR prices to stay below RM6.00/kg level and NBR prices to remain below USD1.50/kg level for the short to mid term which we think still acceptable for glove industry.

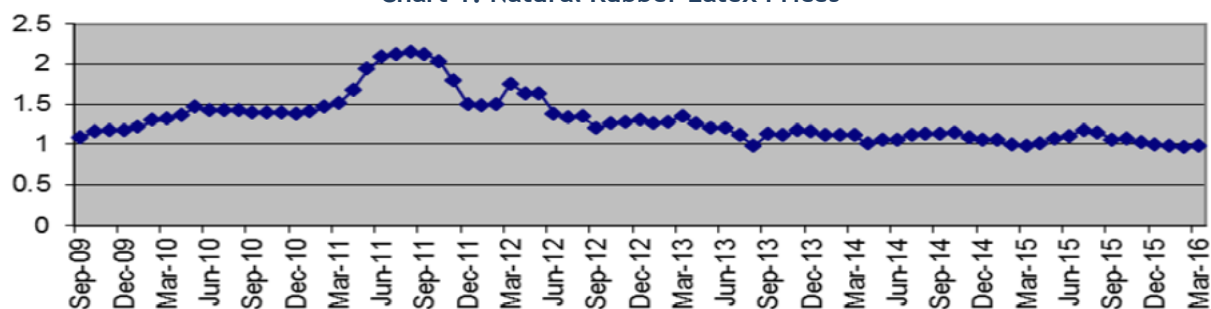
- **Outlook.** We expect the demand for gloves will continue to stay robust by growing double-digit in the next few years from now, accommodated by aggressive expansion plans carried out by producers across the industry. The decline in ASP is inevitable due to rising competition whilst cost management has turned into prerequisite (instead of competitive advantage) for the industry to stay competitive moving forward. However, the suppressed ASP will be lifted by continued strong performance in USD against Ringgit as the market widely predicts a second interest rate hike as soon as in June 2016. We assume RM4.00/ USD1 in our earnings model for FY17-18F for now and will duly adjust should there be any major developments in the currency exchange movement moving forward. On the other hand, headwinds faced by glove manufacturers especially after the recent hike in natural gas prices and soon-to-be revised minimum wage in July 2016 could be adding fuel into fire. Potential freeze-lifting on the hiring of foreign labour (which has already been applied in 4 sectors in early-May 2016) could help unload pressure on labour shortage in the glove industry as well.

At the operational front, we understand that Supermax is currently embarking on line commissioning for the remaining 12 lines roofed under Plant 10 and Plant 11 situated in Meru, Klang. There are 8 production lines fully commissioned in the 2 plants, ramping up the total capacity to about 20 billion pieces per annum. The management expects the remaining 12 lines to be fully commissioned in June-2016 after the infrastructure issues have been resolved, bringing in another 3.4 billion gloves capacity totalling 23.2 billion gloves per annum (+17% from Dec-2015).

In mid-term, Bukit Kapar Project (a.k.a Glove City) is expected to see commencement of construction works for its Factory 1 as early as 3Q16 which is equipped with 7.9 billion gloves per annum capacity and slated to complete after 3Q17. There will be 4 factories in total being built in the Glove City with an estimated 7.9 billion gloves/annum in each factory.

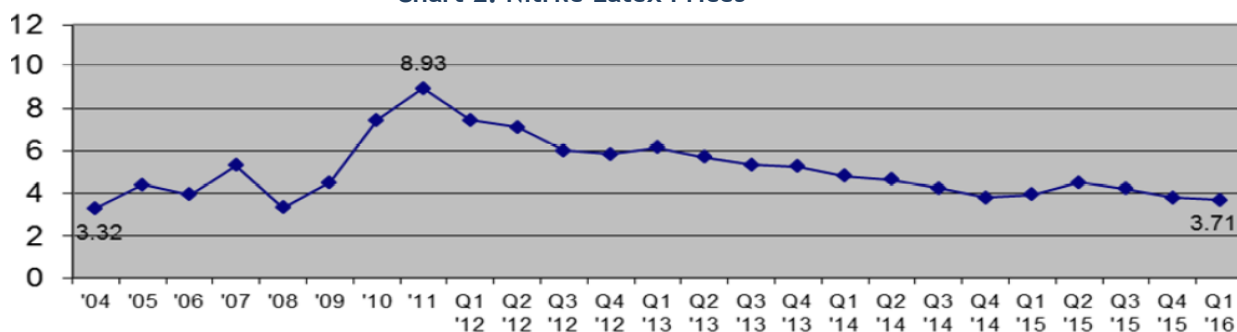
- **Valuation.** We maintain our target price at RM2.94 premised on a target PER pegged to FY17 earnings forecast of 19 sen, upgrading to a **BUY** call from previous **HOLD** after witnessing sharp drop in the share price since our last report in preceding quarter. We reckon the growth drivers have not fully been factored in the current price which is believed to have suffered from the overselling activity in recent months.

Chart 1: Natural Rubber Latex Prices



Source: Company

Chart 2: Nitrile Latex Prices



Source: Company

Chart 3: Peers Comparison

Company	Year Ended	Price (RM)	EPS (sen)		P/E (X)		P/B (X)		ROE (%)	Div Yield (%)	Target Price	Call
			FY14	FY15	FY14	FY15	FY14	FY15				
Supermax	Jun	2.57	17	15	10	22	1	2	11	3	2.94	BUY
Kossan	Dec	6.64	23	30	20	20	4	4	22	2	8.62	BUY
Hartalega	Mar	4.25	16	14	22	32	5	5	19	2	4.78	BUY
Top Glove	Aug	5.04	15	23	16	17	2	3	23	3	6.12	BUY
Average			18	21	17	23	3	4				

Source: Bloomberg, M&A Securities

Chart 4: Results Analysis

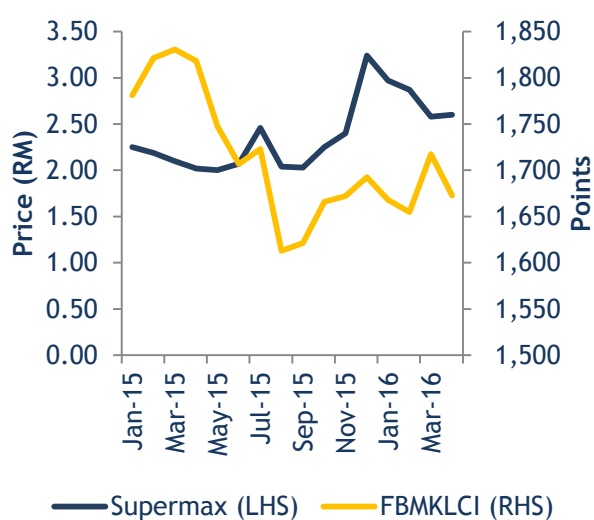
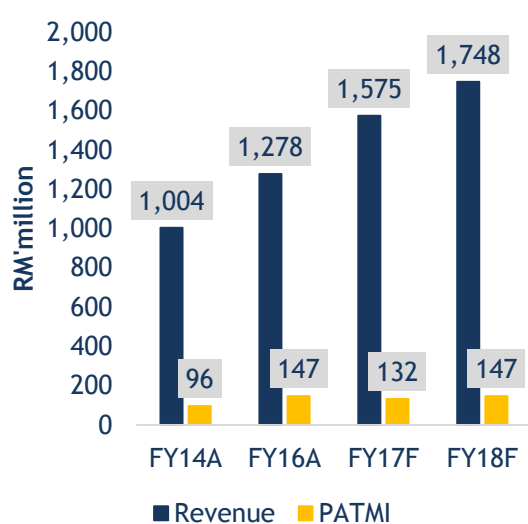
FYE DEC (RM million)	31-Mar-16	31-Dec-15	31-Mar-15	Q-o-Q	Y-o-Y
Turnover	225	291	223	-23%	1%
EBITDA	44	54	38	-19%	16%
EBIT	36	47	30	-23%	20%
D&A	(7)	(7)	(7)	11%	0%
Interest expense	(3)	(1)	(2)	144%	34%
Pretax profit	33	46	28	-28%	19%
Taxation	(13)	(8)	(3)	66%	281%
Minority interest	(0.60)	0.54	0	NM	NM
PATMI	19.67	38.82	25	-49%	-21%
EPS	3	6	4	-49%	-21%
EBITDA margin	19%	19%	17%	1%	3%
EBIT margin	16%	16%	14%	0%	3%
PBT margin	15%	16%	13%	-1%	2%
Net profit margin	9%	13%	11%	-5%	-2%

Source: Company, M&A Securities

Table 3: Financial Forecast

FYE Jun (RM million)	FY14A	FY16A(15M)	FY17F	FY18F
Revenue	1,004	1,278	1,575	1,748
EBITDA	165	232	236	262
D&A	-29	-36	-56	-62
EBIT	136	197	181	200
Net interest income	-8	-11	-10	-10
PBT	128	186	170	190
Tax	-33	-39	-38	-43
PAT	95	147	132	147
MI	0	0	0	0
PATMI	96	147	132	147
EPS	14	22	19	22
EBITDA margin	16%	18%	15%	15%
EBIT margin	14%	15%	11%	11%
PBT margin	13%	15%	11%	11%
Net profit margin	10%	11%	8%	8%
PER (x)	18	14	13	12
P/BV (x)	2	2	1	1
Dividend (sen)	5	6	6	6
Dividend yield	2%	2%	2%	3%

Source: M&A Securities

Supermax Share Price vs. KLCI
(January 2015-April 2016)Revenue vs Net Profit
(FY14-FY18F)

Source: Bloomberg, M&A Securities

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

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