Sequential recovery

Top Glove's 3QFY16 revenue was slightly lower while core net profit came in below our expectation on a sharp contraction in the EBITDA margin. Quarterly core net profit fell on the weaker US$, higher raw material prices and declining nitrile gloves ASP. We expect 4QFY16 to recover sequentially on higher sales volume and easing ASP worries. Maintain BUY but we lower our TP to RM6.30 based on 21x CY16E.

Sales volume growth commendable

Top Glove reported revenue of RM672.3m (-3% qoq; +2%) for the quarter. The healthy sales volume growth (+5% qoq; +11% yoy) was commendable, while the overall topline was dragged down by the weaker U$ and lower ASP. We estimate that the US$ ASP has declined by 2% qoq and 19% yoy, largely due to the supply overhang in the nitrile gloves segment.

Results dragged down by sharp margin contraction

3QFY16 core net profit fell to RM62.5m (-40% qoq; -14% yoy), which was below our earlier estimated range of RM80m-RM90m. While we had projected a sequential decline *(Read: Speed bump)*, we were surprised by the steeper-than-expected margin contraction. EBITDA margin fell sharply to 15% (-8ppts qoq) on: (i) a weaker US$ vs Ringgit (-6% qoq); (ii) higher raw material prices (+29% qoq); and (iii) higher utility costs. Overall, 9MFY16 core net profit missed expectation at 70% of our previous estimate but was in line with consensus at 73% of its full-year forecast.

Easing ASP competition

We view the weak 3QFY16 as a blip and expect sequential recovery in 4QFY16 as the ASP has been adjusted upwards in June. Nitrile gloves pricing competition has eased on slower capacity growth while tailwinds from the weaker Ringgit and latex prices should alleviate margin pressure. We also expect incremental sales from the commissioning of two new plants in 4QFY16 to sustain sequential growth.

Reaffirm BUY, but with a lower TP of RM6.30

We lower our FY16-18E earnings by 12-13%, largely on lower EBITDA margin assumptions. We still like Top Glove for its attractive valuation at 16x CY16E PER and favourable product mix management in line with its nitrile expansion. Maintain **BUY** call but with a lower 12-month TP of RM6.30, based on an unchanged CY16E PER of 21x (+1SD above past-3-year mean PER). Risk: currency volatility.

Earnings & Valuation Summary

FYE Aug	2014	2015	2016E	2017E	2018E
Revenue (RMm)	2,275.4	2,510.5	2,816.1	3,148.6	3,282.7
EBITDA (RMm)	265.4	434.9	567.5	580.8	602.9
Pretax profit (RMm)	212.1	355.2	466.8	480.0	496.5
Net profit (RMm)	176.4	271.5	372.0	382.6	395.8
EPS (sen)	14.1	21.7	29.7	30.6	31.6
PER (x)	34.8	22.6	16.5	16.1	15.5
Core net profit (RMm)	158.4	268.5	372.0	382.6	395.8
Core EPS (sen)	12.7	21.4	29.7	30.6	31.6
Core EPS growth (%)	(6.8)	69.5	38.6	2.9	3.5
Core PER (x)	38.8	22.9	16.5	16.1	15.5
Net DPS (sen)	7.9	8.4	14.9	15.3	15.9
Dividend Yield (%)	1.6	1.7	3.0	3.1	3.2
EV/EBITDA (x)	22.6	13.7	10.3	9.9	9.3
Chg in EPS (%)			(11.9)	(12.9)	(11.8)
Affin/Consensus (x)			0.9	0.9	0.9

Source: Company, Affin Hwang forecasts, Bloomberg

Results Note

Top Glove

TOPG MK
Sector: Rubber Products

RM4.91 @ 15 June 2016

BUY (maintain)

Upside +28%

Price Target: RM6.30

Previous Target: RM7.17

Price Performance

	1M	3M	12M
Absolute	-3.0%	-7.7%	68.2%
Rel to KLCI	-3.0%	-4.2%	77.9%

Stock Data

Issued shares (m)	1,252.5
Mkt cap (RMm)/(US$m)	6,150/1,501
Avg daily vol - 6mth (m)	5.9
52-wk range (RM)	2.87-7.03
Est free float	46.1%
BV per share (RM)	1.41
P/BV (x)	3.48
Net cash/ (debt) (RMm)	337.4
ROE (2016E)	20.7%
Derivatives	Nil
Shariah Compliant	Yes

Key Shareholders

Wee Chai Lim	29.4%
Employees Provident Fund	7.0%
Firstway United Corp	5.1%

Source: Affin Hwang, Bloomberg

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Fig 1: Results Comparison

FYE 31 Aug (RMm)	3QFY16	QoQ % chg	YoY % chg	9MFY16	YoY % chg	Comment
Revenue	672.3	(3.1)	1.7	2,166.4	20.3	Higher sales volume but offset by lower ASP
Op costs	571.4	7.1	7.0	1,713.6	15.0	
EBITDA	100.9	(37.0)	(20.6)	452.9	45.9	
EBITDA margin (%)	*15.0*	*-8.1ppts*	*-4.2ppts*	*20.9*	*+7.5ppts*	Margins contracted on: (i) lower US$; (ii) higher raw material prices ; (iii) lower ASP
Depn and amort	26.5	(1.4)	4.2	80.7	11.5	
EBIT	74.4	(44.2)	(26.8)	372.1	56.4	
EBIT margin (%)	*11.1*	*-8.1ppts*	*-4.3ppts*	*17.2*	*+8.0ppts*	
Int expense	(1.3)	(16.5)	25.6	(6.0)	75.3	
EI	-	na	na	-	na	
Inc/(loss) from affiliates	0.6	>100	nm	0.7	nm	
Pretax profit	73.7	(44.1)	(26.6)	366.9	60.2	
Tax	(11.0)	(58.8)	(60.7)	(70.0)	36.7	
Tax rate (%)	*14.9*	*-5.3ppts*	*-12.9ppts*	*19.1*	*+2.0ppts*	Lower tax rate due to tax incentives
MI	(0.3)	(48.8)	(19.3)	(1.6)	72.7	
Net profit	62.5	(40.3)	(13.5)	295.4	67.0	
EPS (sen)	5.0	(40.3)	(13.5)	23.6	67.0	
Core net profit	62.5	(40.3)	(13.5)	295.4	67.0	Missed our previous estimate but in line with consensus forecast

Source: Affin Hwang, Company data

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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