Start-up losses

Supermax reported yet another disappointing quarterly results despite the improving outlook for the Rubber Gloves sector. Although 3Q revenue rose a strong 30% qoq, core net profit fell 13% on a combination of a margin squeeze in the Glove division and ongoing start-up losses in its Contact Lens division, which is still in the nascent growth phase. With the lack of visible capacity growth coupled with the drag from the Contact Lens division, Supermax's earnings growth is likely to stay tepid in the near term. HOLD.

Higher revenue on sales volume recovery

Supermax's 3Q revenue rose a strong 30% qoq to RM308m. The higher revenue was primarily due to a higher sales volume of gloves, as it has completed the refurbishment of its existing capacity that had been a drag on volume sales previously. Supermax also benefited from the higher ASP for gloves sold, as the industry supply-demand equilibrium normalised, along with the weaker Ringgit, qoq.

Margin squeeze from higher raw material costs

Despite the higher topline, Supermax's core net profit fell 13% yoy to RM20m, which came in below our and consensus estimates. Supermax's contracting margin trend is a stark contrast to that of its peers, as most, if not all, of the glove manufacturers reported margin expansion on higher ASP. EBITDA margin fell 5ppts to 10% during the quarter, one of the lowest margins recorded since FY11. Management attributed the lower margin to the higher raw material prices and its inability to pass through the cost increase, but we believe that Supermax's lagging efficiency also played a part. In addition, Supermax continued to incur higher start-up losses and marketing costs as it ramps up its Contact Lens division.

Maintain HOLD; TP unchanged at RM1.90

While the Rubber Gloves sector continues to exhibit resilient volume growth momentum owing to the rebalancing of sector dynamics, we believe Supermax has yet to position itself to capture the earnings upcycle with its lack of visible capacity expansion. The lack of disclosure for its Contact Lens division also makes it difficult to decipher the financial viability of the new business stream. We lower our earnings forecasts by 5%-17% for FY17-19 on lower margin assumptions due to higher-than-expected start-up losses. However, our TP is unchanged at RM1.90 as we rolled forward our investment horizon to CY18E on an unchanged target PER of 13x.

Earnings & Valuation Summary

FYE Jun	2015A*	2016A#	2017E	2018E	2019E
Revenue (RMm)	1,053.2	1,092.2	1,088.0	1,127.9	1,161.7
EBITDA (RMm)	175.7	196.8	134.2	146.7	158.5
Pretax profit (RMm)	152.4	162.8	97.4	109.7	121.3
Net profit (RMm)	126.9	103.1	81.3	91.5	101.2
EPS (sen)	19.0	15.5	12.2	13.7	15.2
PER (x)	10.5	12.9	16.4	14.6	13.2
Core net profit (RMm)	126.9	103.1	81.3	91.5	101.2
Core EPS (sen)	19.0	15.5	12.2	13.7	15.2
Core EPS growth (%)	32.9	(18.7)	(21.2)	12.6	10.6
Core PER (x)	10.5	12.9	16.4	14.6	13.2
Net DPS (sen)	-	6.1	4.8	5.5	6.0
Dividend Yield (%)	-	3.0	2.4	2.7	3.0
EV/EBITDA (x)	8.3	7.5	11.0	10.1	9.4
Chg in EPS (%)			(5.3)	(16.3)	(17.2)
Affin/Consensus (x)			0.7	0.7	0.8

Source: Company, Bloomberg, Affin Hwang forecasts

** For comparison purposes only as FYE was changed from Dec to June in FY15.*

 # Cumulative 12 months

Results Note

SUPERMAX

SUCB MK

Sector: Rubber Products

RM2.00 @ 30 May 2017

HOLD (maintain)

Downside: -5%

Price Target: RM1.90

Previous Target: RM1.90

Price Performance

	1M	3M	12M
Absolute	+4.2%	-0.5%	-19.4%
Rel to KLCI	+4.3%	-4.5%	-25.5%

Stock Data

Issued shares (m)	667.5
Mkt cap (RMm)/(US$m)	1,334.9/311.7
Avg daily vol - 6mth (m)	1.5
52-wk range (RM)	2.88-2.53
Est free float	58.1%
BV per share (RM)	1.59
P/BV (x)	1.26
Net cash/ (debt) (RMm)	(302.1)
ROE (2017E)	6.9%
Derivatives	Nil
Shariah Compliant	Yes

Key Shareholders

Kim Sim Thai	20.8%
Bee Geok Tan	10.5%
EPF	5.1%

Source: Affin Hwang, Bloomberg

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Fig 1: Results Comparison

FYE June (RMm)	3QFY17	QoQ % chg	YoY % chg	9MFY17	YoY % chg	3Q comments
Revenue	308.2	30.2	37.0	814.0	(1.4)	3Q revenue rose a strong 30% qoq underpinned by a firmer rubber glove sales volume, higher ASP owing to favourable industry supply-demand dynamics, as well as the weakening of the Ringgit.
Op costs	(276.9)	37.8	51.7	(712.7)	5.1	
EBITDA	31.3	(12.5)	(26.3)	101.3	(31.5)	
EBITDA margin (%)	*10.2*	*-5.0ppts*	*-8.7ppts*	*12.4*	*-5.5ppts*	Despite strong revenue growth, EBITDA margin fell 5% due to higher raw material prices, as well as the inability to pass on the cost increase via a higher ASP. The margin also declined largely due to ongoing start-up losses in the Contact Lens division.
Depn and amort	(11.2)	25.0	53.7	(28.7)	38.4	Higher depreciation charges incurred likely due to the refurbishment of newer lines to replace older and inefficient production lines.
EBIT	20.1	(25.0)	(42.9)	72.6	(42.9)	
EBIT margin (%)	*6.5*	*-4.8ppts*	*-9.1ppts*	*8.9*	*-6.5ppts*	
Int expense	(3.0)	49.1	0.7	(7.4)	7.1	
Int and other income	-	na	na	-	na	
Inc/loss from associates	3.8	73.4	>100	9.2	16.7	
EI	-	na	na	-	na	
Pretax profit	**20.9**	(22.6)	(37.6)	74.4	(41.9)	
Tax	(1.6)	(67.0)	(87.9)	(13.1)	(57.9)	
Tax rate (%)	*7.7*	*-10.3ppts*	*-31.8ppts*	*25.2*	*+4.5ppts*	Supermax's effective tax rate of 8% for the current quarter is lower than the statutory tax rate due to tax incentives claimed.
MI	0.5	3.6	nm	0.6	>100	
Net profit	**19.8**	(12.5)	0.4	61.9	(36.2)	
EPS (sen)	2.9	(12.5)	0.4	9.2	(36.2)	
Core net profit	**19.8**	(12.5)	0.4	61.9	(36.2)	Overall results below our and consensus expectations.

Source: Affin Hwang, Company

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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