

EARNINGS NORMALISING FOR TOP GLOVE

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Top Glove Corp Bhd

(June 14, RM5.02)

Downgrade to hold with a lower target price (TP) of RM4.60:

While Top Glove Corp Bhd's upcoming third quarter ended May 31, 2016 (3QFY16) results could be sequentially weaker, it could still be within our and the market's expectations. Nevertheless, we cut our financial year ending Aug 31, 2017 (FY17) to FY18 earnings per share (EPS) forecasts by 11% per annum on a lower US dollar/ringgit assumption of 4.00. We also lower 2017 price-earnings ratio (PER) target to its mean of 15 times (from 19 times) given its normalising earnings outlook. Consequently, our new TP is RM4.60 (from RM6.50) and the stock is now a "hold" (previously "buy").

Its 3QFY16 results are scheduled for release today. We estimate its net profit to be sequentially weaker at RM65 million to RM75 million (-28% to -38% quarter-on-quarter [q-o-q]; -10% to +4% year-on-year [y-o-y]) as benefits of a stronger sales volume (about +5% q-o-q, +12% y-o-y) would likely be offset by i) a weaker US dollar/ringgit average rate of 4.01 (-6%

q-o-q, +10% y-o-y); ii) a higher latex average price of RM4.55 per kg (+29% q-o-q, +10% y-o-y); and iii) more intense nitrile glove average selling prices (ASPs). We expect its operating margin to contract around four percentage points q-o-q (flattish y-o-y).

We think its earnings could improve in 4QFY16, considering that latex prices will soften seasonally from this month, offsetting the higher minimum wage and potential gas tariff hikes, both in July. Also, nitrile competition has eased this month, on slower capacity growth, and glove makers have pushed through higher nitrile glove ASPs. Meanwhile, the 4QFY16 US dollar/ringgit rate will continue to hover at the 3QFY16 level.

We maintain our FY16 earnings forecasts, but lower our FY17 to FY18 EPS by 11% per annum as we lower our US dollar/ringgit assumptions to an average of 4.00 (from 4.10).

On normalising external tailwinds (stable US dollar/ringgit rate and still low latex prices), we now project Top Glove's net profit to contract 8% y-o-y in FY17. As earnings normalise, we lower our target 2017 PER to its mean of 15 times (from +1 standard deviation to the mean of 19 times), resulting in a new RM4.60 TP. — *Maybank Investment Bank Research*, June 13

The Edge Markets

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