

14 July 2020

Consumer Non-cyclical | Rubber Products

Supermax Corp (SUCB MK)

Buy (Maintained)

Steeper ASP Increases At Distribution Level; BUY

Target Price (Return): MYR18.88 (18.1%)
 Price: MYR16.00
 Market Cap: USD4,837m
 Avg Daily Turnover (MYR/USD): 211m/45.9m

- **Keep BUY with higher DCF-derived MYR18.88 TP from MYR13.88, 18% upside and c.1% yield.** Gloves shortages have worsened, as COVID-19 cases in the US have surged 24% MTD. We increase our earnings estimates and TP due to higher ASPs. As Supermax Corp has its own distribution channel in the US, we expect its earnings to outperform peers. Our new TP reflects 27.5x FY21F (Jun) P/E – a 23% discount against the sector average due to SUCB's smaller market cap/ liquidity.
- **Gloves demand estimates have increased, as COVID-19 cases in the US surged 24% MTD.** Over the past five days (8-12 Jul), the number of new cases daily has surged >60,000. As of 12 Jul, the total number of cases has surged by 367,000, or 24% on a MTD basis to 3.27m. As COVID-19 cases remain high in the US, gloves demand should stay exceptionally high due to the important need to protect healthcare workers. As the US is the biggest gloves consumer globally, stubbornly high number of COVID-19 cases means that gloves demand should continue to rise.
- **Gloves shortages have worsened.** Within a period of two weeks, the number of new COVID-19 cases in the US has increased more than expected. As a result, we estimate gloves demand there has increased and caused further depletion in global stock levels. Our estimate shows that levels should have declined by another 2% to 10.8bn pieces globally. This is enough for 15 days of demand from 15.2 days previously. It is also much lower than the pre-pandemic level average of 60 days.
- **ASP assumptions increased.** Our channel checks also reveal the shortage of certain raw materials used in gloves manufacturing. This has capped near-term supply. We have increased FY21-22 ASP assumptions by 2-9%. This increase is higher than SUCB's peers due to its distribution channels in eight countries, including the US and Brazil. These countries are still registering high new COVID-19 cases. FY20F earnings remain unchanged, as the financial year ended in June.
- **BUY with a higher TP.** We have increased our FY21F-23F earnings forecasts by 14-19%. In the short term, 1QFY21 core earnings should show significant improvement QoQ, as ASPs are on an increasing trend. Post COVID-19, SUCB's earnings growth outlook remains positive, as we expect gloves demand to continue the usual uptrend growth of 8-10% due to higher hygiene awareness globally.
- **Risks:** An effective COVID-19 vaccine available globally faster than expected, lower-than-expected sales volumes/USD, and higher-than-expected raw material prices.

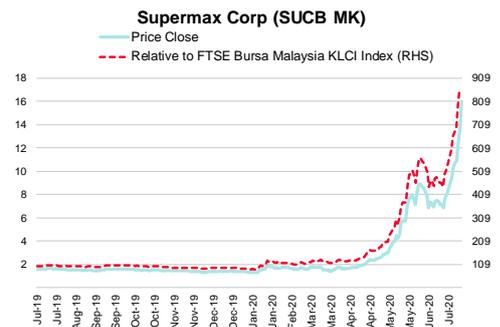
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	1049.6	102.0	834.5	1119.8	895.6
Relative	1049.4	99.0	817.1	1119.4	900.3
52-wk Price low/high (MYR)				1.30	16.0



Source: Bloomberg

Forecasts and Valuation	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
Total turnover (MYRm)	1,304	1,538	2,026	2,981	3,330
Recurring net profit (MYRm)	107	123	419	898	1,085
Recurring net profit growth (%)	-	15.5	240.4	114.2	20.8
Recurring P/E (x)	195.72	169.45	49.77	23.24	19.23
P/B (x)	20.6	18.6	14.7	10.2	7.4
P/CF (x)	117.81	88.81	32.78	18.65	17.16
Dividend Yield (%)	0.5	0.1	0.7	1.5	1.8
EV/EBITDA (x)	85.93	90.20	33.44	16.09	13.00
Return on average equity (%)	-	11.5	33.0	51.7	44.6
Net debt to equity (%)	28.5	19.2	net cash	net cash	net cash

Source: Company data, RHB

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Financial Exhibits

Asia	Financial summary (MYR)	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
Malaysia	Recurring EPS	0.08	0.09	0.32	0.69	0.83
Consumer Non-cyclical	DPS	0.08	0.02	0.11	0.24	0.29
Supermax Corp	BVPS	0.78	0.86	1.09	1.57	2.16
SUCB MK	Return on average equity (%)	-	11.5	33.0	51.7	44.6
Buy						
	Valuation metrics	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
	Recurring P/E (x)	195.72	169.45	49.77	23.24	19.23
	P/B (x)	20.6	18.6	14.7	10.2	7.4
	FCF Yield (%)	0.6	0.6	2.3	4.6	5.1
	Dividend Yield (%)	0.5	0.1	0.7	1.5	1.8
	EV/EBITDA (x)	85.93	90.20	33.44	16.09	13.00
	EV/EBIT (x)	103.66	111.99	38.47	17.37	13.93
	Income statement (MYRm)	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
	Total turnover	1,304	1,538	2,026	2,981	3,330
	Gross profit	430	510	992	1,706	1,970
	EBITDA	244	232	613	1,231	1,465
	Depreciation and amortisation	(42)	(45)	(80)	(91)	(98)
	Operating profit	202	187	533	1,140	1,367
	Net interest	(14)	(20)	(3)	10	26
	Pre-tax profit	162	172	551	1,180	1,426
	Taxation	(52)	(49)	(129)	(277)	(335)
	Reported net profit	107	123	419	898	1,085
	Recurring net profit	107	123	419	898	1,085
	Cash flow (MYRm)	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
	Change in working capital	57	31	132	136	53
	Cash flow from operations	177	235	637	1,120	1,216
	Capex	(59)	(112)	(150)	(150)	(150)
	Cash flow from investing activities	(55)	(112)	(141)	(129)	(114)
	Dividends paid	(76)	(33)	(126)	(269)	(326)
	Cash flow from financing activities	(126)	(104)	(95)	(250)	(367)
	Cash at beginning of period	156	145	174	584	1,334
	Net change in cash	(4)	19	401	740	735
	Ending balance cash	145	174	584	1,334	2,079
	Balance sheet (MYRm)	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
	Total cash and equivalents	145	174	584	1,334	2,079
	Tangible fixed assets	900	969	1,018	1,068	1,121
	Total investments	197	208	208	208	208
	Total assets	1,700	1,843	2,326	3,244	4,071
	Short-term debt	374	331	294	336	327
	Total long-term debt	62	61	129	121	114
	Total liabilities	677	708	897	1,185	1,251
	Total equity	1,023	1,134	1,429	2,059	2,820
	Total liabilities & equity	1,700	1,843	2,326	3,244	4,071
	Key metrics	Jun-18	Jun-19	Jun-20F	Jun-21F	Jun-22F
	Revenue growth (%)	0.0	17.9	31.7	47.1	11.7
	Recurrent EPS growth (%)	0.0	15.5	240.4	114.2	20.8
	Gross margin (%)	33.0	33.2	49.0	57.2	59.1
	Operating EBITDA margin (%)	18.7	15.1	30.3	41.3	44.0
	Net profit margin (%)	8.2	8.0	20.7	30.1	32.6
	Capex/sales (%)	4.5	7.3	7.4	5.0	4.5
	Interest cover (x)	14.5	9.5	46.2	106.4	138.3

Source: Company data, RHB

Sector Demand-Supply Outlook

Figure 1: Demand-supply estimates

Pieces (bn)	2018	2019	2020F	2021F	2022F
Hartalega	33.0	36.6	40.1	43.7	48.5
<i>Growth (%)</i>	<i>10.0%</i>	<i>10.9%</i>	<i>9.6%</i>	<i>9.0%</i>	<i>11.0%</i>
Kossan Rubber	26.5	29.0	32.0	35.0	38.4
<i>Growth (%)</i>	<i>20.5%</i>	<i>9.4%</i>	<i>10.3%</i>	<i>9.4%</i>	<i>9.7%</i>
Top Glove	60.5	70.1	78.7	100.4	106.6
<i>Growth (%)</i>	<i>17.2%</i>	<i>15.9%</i>	<i>12.3%</i>	<i>27.6%</i>	<i>6.2%</i>
Supermax	22.0	21.7	26.2	31.1	38.2
<i>Growth (%)</i>	<i>-6.0%</i>	<i>-1.4%</i>	<i>20.6%</i>	<i>18.6%</i>	<i>22.9%</i>
Sri Trang*	21.0	27.0	33.0	38.0	43.0
<i>Growth (%)</i>	<i>NA</i>	<i>28.6%</i>	<i>22.2%</i>	<i>15.2%</i>	<i>13.2%</i>
China	7.0	9.0	18.0	37.0	56.0
<i>Growth (%)</i>	<i>NA</i>	<i>28.6%</i>	<i>100.0%</i>	<i>105.6%</i>	<i>51.4%</i>
Others	70.0	74.2	81.6	89.8	97.0
<i>Growth (%)</i>	<i>NA</i>	<i>6.0%</i>	<i>10.0%</i>	<i>10.0%</i>	<i>8.0%</i>
Estimated manufacturing capacity	240.0	270.0	309.6	374.9	427.6
Supply change	92.0	30.0	39.6	65.3	52.7
<i>Supply growth</i>	<i>62.2%</i>	<i>12.5%</i>	<i>14.7%</i>	<i>21.1%</i>	<i>14.1%</i>
Global demand	256.0	263.0	333.9	384.2	428.6
Demand change	28.0	7.0	70.9	50.3	44.4
<i>Demand growth</i>	<i>12.3%</i>	<i>2.7%</i>	<i>26.9%</i>	<i>15.1%</i>	<i>11.6%</i>
Surplus/(deficit)	-16.0	7.0	-24.3	-9.2	-0.9

- ◆ Our capacity supply assumptions may be less aggressive than glove producers' plans
- ◆ Our key assumption: Rational capacity expansions, in which producers will balance between volume growth and margins

Source: Company data, RHB

Figure 2: Key assumptions

Key assumptions	FY20F	FY21F	FY22F
Installed capacity (m pieces pa)	26,200	31,100	38,200
ASP change YoY	28%	26%	7%
Average USD/MYR	4.28	4.28	4.28
Utilisation rate	80%	90%	90%

Source: RHB

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Valuation

FCFF increased. In our DCF valuation we have increased FCFF assumptions – this is in line with better earnings prospects and driven by a better ASP outlook, as demand-supply remains extremely tight.

Our DCF-derived TP of MYR18.88 reflects 27.5x FY21 P/E. The TP implies a 23% discount against the sector average forward P/E. This is justified, given SUCB's smaller market cap and lower liquidity.

For the discount factor, we have applied an 11-month discount to FY22 for the first cash flow to estimate the TP, as of Jul 2021, ie 12 months from now.

SUCB's implied forward P/E of 27.5x is lower than the implied forward P/E for Hartalega (HART MK, BUY, TP: MYR21.60; 44.9x), Top Glove (TOPG MK, BUY, TP: MYR28.88; 33.5x), and Kossan (KRI MK, BUY, TP: MYR15.50; 31.3x). The implied forward P/E is lower than Hartalega and Top Glove's, as SUCB is not an FBM KLCI member. As compared to Kossan, the forward P/E is lower due to the company's decreased exposure to nitrile gloves, at 63%. Kossan's exposure is higher at 80%. Nitrile gloves ASPs are higher, and usually command elevated margins vis-à-vis latex gloves.

Figure 3: DCF valuation

FYE Dec (MYRm)	FY22F	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F	Terminal
CFO	1,216	1,180	1,292	1,386	1,413	1,497	1,599	1,660	1,710	1,761	
+ Interest (1 - tax rate)	(8)	(7)	(6)	(6)	(5)	(4)	(4)	(3)	(3)	(3)	
- capital expenditure	(150)	(150)	(150)	(150)	(150)	(150)	(150)	(150)	(155)	(159)	
FCFF	1,059	1,023	1,136	1,230	1,258	1,343	1,445	1,507	1,552	1,598	39,315
Discount factor	0.92	0.85	0.78	0.71	0.66	0.60	0.55	0.51	0.47	0.43	0.43
PV of FCFF	979	867	884	879	825	808	798	763	722	682	16,778
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Risk-free	4.0%										
Beta	0.86										
Cost of Equity	9.2%										
WACC	8.2%										
Terminal growth	4.0%										
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Enterprise value (MYRm)	24,985										
Cash	218										
- Debt	(473)										
Equity value (MYRm)	24,731										
Number of shares (m)	1,309.90										
Fair Value (MYR)	18.88										

Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-07-08	Buy	13.9	10.9
2020-06-02	Buy	10.5	7.6
2020-05-22	Buy	6.7	5.8
2020-05-21	Buy	6.1	5.4
2020-05-13	Buy	3.9	3.6
2020-03-15	Buy	1.9	1.7
2019-11-29	Neutral	1.5	1.3
2019-09-03	Neutral	1.6	1.5
2019-07-19	Buy	1.9	1.6
2019-01-08	Neutral	1.9	1.6
2018-08-30	Neutral	4.2	1.7

Source: RHB, Bloomberg

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
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