Company

Global Markets Research

Asia ASEAN Malaysia

Industrials

Deutsche Bank

6 May 2010

Rubber Gloves

Gloving the world

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FITT Research

Fundamental, Industry, Thematic, Thought Leading

Deutsche Bank Company Research's Investment Policy Committee has deemed this work F.I.T.T. for investors seeking differentiated ideas. The Malaysian glove industry is a rare proxy to rising global healthcare spending. The leaders in the industry dominate by sheer economies of scale, wide distribution networks and pricing power. Our in-depth industry supply and demand analysis underpins our Buy ratings on Top Glove and Supermax.

Fundamental: The market has under-estimated 13% demand CAGR till 2020

Industry: Global leaders to extend dominance in a growing market

Thematic: Multi-year growth trend; global healthcare spending accelerates

Thought-leading: Deutsche Bank's in-depth supply-demand analysis

Deutsche Bank AG/Hong Kong

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Fundamental: The market has under-estimated 13% demand CAGR till 2020

The rubber gloves industry is a proxy to the rising incidences of diseases and global healthcare spending. We expect the glove industry to generate sustainable growth of 13% until 2020. This is driven by global healthcare reforms in developed markets and rising hygiene standards in emerging markets. Despite an increasingly strong fundamental backdrop, the Malaysian glove industry as a whole trades at just 12x FY10E PE, a 23% and 16% discount to the Malaysian and ASEAN markets, respectively, but yet offers a brighter growth outlook.

Industry: Global leaders to extend dominance in a growing market

The rubber gloves industry is a classic, volume driven economies of scale manufacturing sector. Significant consolidation over the last 10 years has resulted in just a handful of large players dominating the global market space. The top 3 players in Malaysia alone command 43% of the world's glove supply. Economies of scale, wide distribution networks, increasing outsourcing by healthcare product providers, the need to be close to raw materials and strong pricing power should allow the top producers to extend their lead.

Thematic: Multi-year growth trend; global healthcare spending accelerates

The US and China governments are budgeting more than US$100bn in healthcare spending over the next two years. This should underpin demand for the glove replacement market (85-90% of demand). Sporadic outbreaks of diseases too should also help create 'new' demand (2%), with underlying organic growth at 8%). We expect this multi-year growth trend to persist. We expect the scarcity value of these companies to appreciate over time.

Thought-leading: Deutsche Bank's in-depth supply-demand analysis

Our in-depth demand and supply analysis suggests earnings growth of 40% in FY10E and a three-year EPS CAGR of c. 22% from 2009-12E for the glove industry. We expect the demand for gloves to increase at a 13% CAGR over the next 10 years, driven by creation of new sources of demand from global healthcare reforms and improving hygiene standards. We expect glove usage per person to increase 3.3x from 21 pieces in 2009 to 70 pieces by 2020E, versus glove usage per capita of 108 pieces per year in the US and the EU currently.

Initiating coverage of Top Glove and Supermax with Buy ratings

Top Glove (market share 23%) and Supermax (11%) are the world's largest producers of gloves. Our DCF-based valuations of the two companies offer over 30% in potential upside to our targets. In an ASEAN context, both stocks offer rare exposure to global healthcare spending momentum, above market and industry EPS growth of 62% FY10E, under-leveraged balance sheets, cash flow generative business and increasing dominance in the industry. Our top pick is Supermax for its liquidity and cheaper valuations.

FITT Research

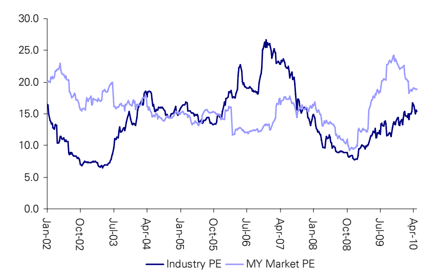
Top pick

Supermax (SUPM.KL),MYR6.36	**Buy**

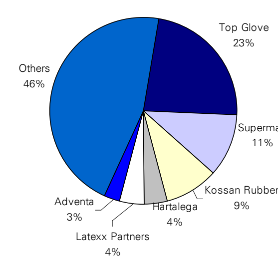
Companies featured

Top Glove (TPGC.KL),MYR11.60			**Buy**
	2009A	2010E	2011E
P/E (x)	11.8	14.2	12.2
EV/EBITDA (x)	7.0	9.2	8.0
Price/book (x)	3.7	3.6	3.0
Supermax (SUPM.KL),MYR6.36			**Buy**
	2009A	2010E	2011E
P/E (x)	4.4	9.3	7.8
EV/EBITDA (x)	3.5	7.6	6.0
Price/book (x)	2.3	2.5	2.0

Trading at a discount to market



Global market share of gloves



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Executive summary

Outlook

- Malaysia is the world's largest supplier of global rubber gloves (medical, surgical, etc.) demand with 65% of global market share. We are bullish on demand for gloves and expect long-term growth of 13% CAGR for the next ten years. We expect glove usage per person to increase by 3.3x from 21 pieces in 2009 to 70 pieces by 2020E.
- Near term, we are expecting the glove industry as a whole to see earnings growth of 49% in FY10E and three-year EPS CAGR of c. 22% for 2009-12E.
- The Malaysian glove industry, currently trading at 12x FY10E PE, is at a 23% discount to the Malaysian market. We see room for valuation growth given its defensive and stronger-than-market earnings growth momentum, low gearing levels and above-market ROEs.
- Glove suppliers have announced aggressive capacity expansion plans. However, the glove supply overcapacity concerns are overdone in our view. We believe that the new capacity addition is likely to be about 19-21bn pieces in 2010E and another 20-22bn pieces in 2011E, which would be just enough to meet global demand for gloves. Bottlenecks in natural gas supply, delays in equipment delivery, time needed for plant set-up and lower actual capacity utilization, cap the absolute amount of gloves supply at lower than the actual planned capacity.
- We believe Malaysia's rubber glove industry offers investors a unique proposition: reasonably priced and fundamentally strong companies in an industry driven by secular long-term growth that offers products with inelastic demand. We rate Top Glove and Supermax, the two market leaders in the industry, Buy.

Valuation and recommendations

We initiate coverage of Top Glove and Supermax with Buy recommendations. Our DCF-based valuations of the two companies offer over 30% in potential upside. We like Top Glove's market leading position in the industry, unlevered balance sheet with a net cash position and its strategy of focusing on capturing the emerging markets' glove demand through its production of low-cost medical natural rubber powdered gloves. We like Supermax for its strong number two position in the global glove industry, low net gearing of 0.3x and its strategy of developing its own brand of gloves on top of being an OEM manufacturer, which would generate both manufacturing and distribution income.

We base our target prices on DCF valuations, to take into account the strong cash flow generation and sustainable earnings growth for these companies.

Risks

Industry risks include: 1) overcapacity; 2) sharp volatility in latex costs and foreign currencies resulting in near-term margin squeeze; 3) political risks, domestic and regional; and 4) infrastructural bottlenecks and labour shortages.

Valuations and rating

Key themes

- Despite an increasingly strong fundamental backdrop, the Malaysian glove industry as a whole trades at just 12x FY10E PE, a 23% and 16% discount to the Malaysian and ASEAN markets, respectively.
- Initiating coverage of Top Glove and Supermax with Buy ratings and DCF valuations that offer over 30% potential upside.

Growth in value to continue

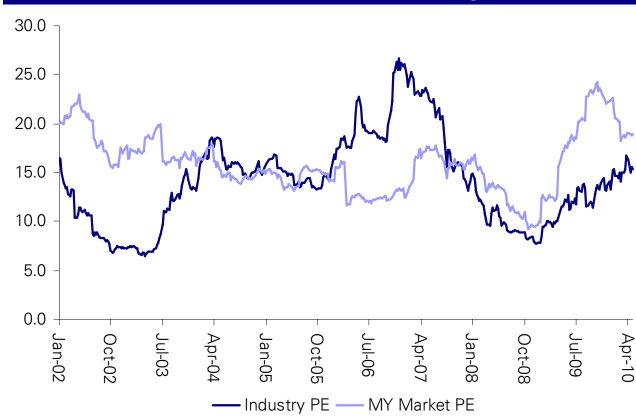
Expect the top three players to register average earnings growth of c.61% in FY10E

We expect the top three Malaysian glove manufacturers (Top Glove – 23%, Supermax – 11%, Kossan [KRI MK, RM7.50, NR] – 9%), which together command c.43% of the global glove industry, to post earnings growth of c.61% in FY10E, above Deutsche Bank's earnings growth expectation of 35% for the Malaysian market. We see strong earnings growth driven by new demand from the implementation of healthcare reforms by governments around the world, rising global healthcare spending, more stringent regulations on hygiene standards across the world, government's stock ups in preparation for potential healthcare emergencies and secular growth such as world population and aging population growth.

Malaysian glove industry as a whole trades at just 12x FY10E PE, a 23% discount to the Malaysian market

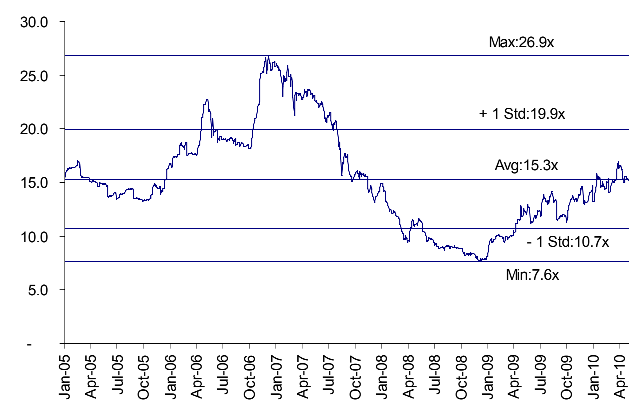
The aggregate top three Malaysian glove manufacturers currently trade at 12x FY10E PE, below its five-year historical average PE of 15.3x. Peak and trough PE valuations for the sector have ranged from 26.9x to 7.6x since 2002. Despite the better-than-market earnings profile, ROE and gearing levels, the Malaysian glove industry as a whole trades at just 12x FY10E PE, a 23% and 16% discount to the Malaysian and ASEAN markets, respectively.

Figure 1: Malaysia's top three glove manufacturer PE versus the Malaysian market PE – trading at discount



Source: Deutsche Bank

Figure 2: Aggregate PE valuation of the top three glove manufacturers by global market share



Source: Deutsche Bank

We believe the glove industry still offers a value proposition as we expect the glove industry to generate sustainable growth of 13% p.a. until 2020. The glove industry generally has a low beta compared with the world economic environment and is generally driven by more secular growth. Industry players generally have pricing power and are able to pass on higher cost increases.

Recent weakness is an opportunity, in our view

This as an opportunity to enter a market that offers a proxy to rising healthcare spending globally in order to ride the sector's multi-year growth trend

The rubber glove industry has had a strong performance year to date. However, the sector has been under selling pressure recently as investors raised concerns on whether the industry's share price re-rating cycle is over after such a long period of outperformance. These concerns are exacerbated by the recent surge in latex prices, stronger MYR and concerns of overly aggressive capacity expansion by industry players, leading to some sell down in the sector. We see this as an opportunity to enter a market that offers a proxy to rising healthcare spending globally in order to ride the sector's multi-year growth trend.

Short-term re-rating catalysts for the industry are latex prices normalizing to lower levels after the wintering season of the commodity in mid-May and news flow on new H1N1 outbreak, while longer-term triggers can include consistent earnings growth and the government's successful implementation of healthcare reforms.

Key recommendations: Buy Top Glove and Supermax

We initiate on Top Glove with a Buy recommendation based on a DCF-derived target price of RM16.50

Top Glove: We initiate on Top Glove with a Buy recommendation based on a DCF-derived target price of RM16.50. We like Top Glove's market leading position in the industry (23% global market share), net cash balance sheet and its strategy of focusing on capturing the emerging markets' glove demand through its production of low-cost medical natural rubber powdered gloves. We expect the company to deliver a three-year EPS CAGR of 25% for 2009-12E.

We initiate on Supermax with a Buy recommendation based on a DCF-derived target price of MYR9.00

Supermax: We initiate on Supermax with a Buy recommendation based on a DCF-derived target price of MYR9.00. Supermax is a strong number two player in the industry with 11% global market share of the glove market. We expect the company to generate a three-year NP CAGR of 27.4% for FY10-12E. Its low net gearing of 0.3x and strategy of developing its own brand of gloves on top of being an OEM manufacturer will see the company being able to generate both manufacturing and distribution income.

Please refer to our company initiation reports included at the end of this chapter for more details.

Valuation methodology: DCF and sector PE

Our DCF fair valuations for Top Glove and Supermax offer over 30% potential upside

We have utilized a DCF-based valuation methodology to value the companies to take into account the industry's strong cash flow generation abilities, defensive nature and multi-year growth prospects. We also looked at sector PE to compare implied discount and/or premium valuations to market and peers. Our DCF fair valuations for Top Glove and Supermax offer over 30% potential upside, justifying our Buy recommendations. Our key assumptions are: 1) Malaysian market WACC of 10.1% (6.1% equity risk premium, 4.1% risk-free rate), in line with Deutsche Bank's cost of equity expectations; 2) two-year average stock beta of 0.8-1.1x; and 3) a terminal growth rate of 5% to take into account the inelastic nature of demand for rubber gloves, which is likely to grow at a higher rate than combined world population and aging population growth of 3% p.a.

We believe Top Glove and Supermax are global market leaders that offer above-market average growth profiles, strong balance sheets with net cash and 0.3x net gearing levels.

Sensitivity analysis

The industry's strong net profit growth indicates that it is able to pass on sustained cost increases (and reductions) to customers

Latex accounts for 55-60% of a glove manufacturer's total operating costs. Despite the 5.5x increase in rubber prices, the industry's strong net profit growth has indicated that it is able to pass on sustained cost increases (and reductions) to customers. The risk to earnings arises in case of a sharp upward movement in prices. Margins during this period will be negatively affected until the price increase is pushed through.

Our sensitivity analysis shows that every 1% increase in latex prices implies a 3% decline in Top Glove's FY10E net profit and a 0.5% decline in our DCF valuation, and a 2.4% decline in Supermax's FY10E net profit and a 0.6% decline in our DCF valuation.

Figure 3: Sensitivity to 1% change in costs

	Change in FY10E NP		Change in DCF valuations	
	Top Glove	**Supermax**	**Top Glove**	**Supermax**
Latex costs (MYR/kg)	3.0%	2.4%	0.5%	0.6%
MYR/US$	6.1%	5.2%	1.0%	1.3%
Total costs (MYR m)	5.4%	4.4%	0.9%	1.1%

Source: Deutsche Bank

Figure 4: Peer valuations

Deutsche Bank - Global Rubber Comps — As at 04-May-10

Company	BBerg	Year End	Rec	Currcy	Price (Local Currency)	TP (Local Currency)	Market Cap (Local Currency)	Market Cap (US$ m)	3M ADTV (US$ m)	EV/EBITDA (x) 2009E	EV/EBITDA (x) 2010E	EV/EBITDA (x) 2011E	P/E (x) 2009E	P/E (x) 2010E	P/E (x) 2011E	EPSg 2009E	EPSg 2010E	EPSg 2011E	P/BV (x) 2009E	P/BV (x) 2010E	P/BV (x) 2011E	Div Yield (%) 2009E	Div Yield (%) 2010E	Div Yield (%) 2011E	ROE (%) 2009E	ROE (%) 2010E	ROE (%) 2011E	Net Gearing (%) 2009E	Net Gearing (%) 2010E	Net Gearing (%) 2011E
MNC resellers																														
Kimberly-Clark	KMB US	31-Dec	Hold	USD	61.19	65.00	25,471	25,471.0	176.0	7.1	7.7	7.1	12.2	12.6	11.6	12.0	7.9	7.9	4.7	4.6	4.5	4.4	4.3	4.7	39.4	34.2	39.1	80.9	85.6	84.4
Beiersdorf	BEI GR	31-Dec	Buy	EUR	42.97	50.00	9,745	12,701.2	30.7	10.6	10.1	8.8	22.4	20.3	17.5	(22.9)	28.5	15.5	4.0	3.4	3.0	1.9	2.1	2.4	14.7	17.4	18.1	(26.1)	(30.1)	(34.8)
Cardinal Health	CAH US	30-Jun	Hold	USD	34.87	37.00	12,604	12,603.8	114.7	6.1	7.7	7.0	11.4	15.5	13.7	(34.5)	(9.8)	13.6	0.9	1.3	1.2	2.0	2.0	2.0	10.9	8.6	9.0	20.6	3.5	4.8
SSL International	SSL LN	31-Mar	Hold	GBP	852.50	825.00	1,800	2,720.3	701.3	9.3	13.2	12.4	16.6	25.5	21.8	34.3	22.0	16.9	3.1	5.4	4.6	2.0	1.2	1.2	27.8	23.6	23.2	6.1	2.1	19.6
MNC resellers								**13,374.1**	**255.7**	**8.3**	**10.3**	**9.4**	**16.8**	**20.4**	**17.7**	**(7.7)**	**13.6**	**15.3**	**2.7**	**3.3**	**2.9**	**1.9**	**1.8**	**1.9**	**17.8**	**16.6**	**16.8**	**0.2**	**(8.1)**	**(3.5)**
Rubber glove																														
Top Glove	TOPG MK	31-Dec	Buy	MYR	12.34	16.50	3,704	1,140	3.7	7.0	9.8	8.5	11.8	15.1	13.0	52.7	46.7	16.3	3.7	3.8	3.2	2.4	2.6	3.1	22.7	27.4	26.8	(19.5)	(27.0)	(32.3)
Ansell	ANN AU	30-Jun	Buy	USD	13.02	12.75	1,736	1,575	9.1	9.01	11.3	9.6	12.7	17.4	14.8	(5.9)	13.0	17.0	1.8	3.0	2.6	2.7	2.2	2.3	16.0	17.6	18.6	19.2	22.6	8.5
Semperit	SEM AV	31-Dec	Buy	EUR	30.48	37.00	627	807	1.0	3.18	5.2	4.7	10.7	15.0	13.3	3.2	8.0	12.7	1.8	1.9	1.8	5.7	4.3	4.8	12.9	13.1	13.9	(49.0)	(41.3)	(44.2)
Supermax	SUCB MK	31-Dec	Buy	MYR	6.66	9.00	1,761	542	5.7	3.50	8.0	6.3	14.1	9.7	8.1	173.0	41.7	19.7	2.3	2.6	2.1	1.4	2.4	2.8	26.6	29.5	28.2	31.5	23.7	16.5
Kossan	KRI MK	12/2009	NR	MYR	7.82	NA	1,247	384	1.2	10.08	7.5	6.3	16.7	10.9	9.0	NA	94.7	27.0	3.7	2.7	2.2	3.9	4.2	4.6	21.4	27.5	25.5	23.2	33.0	17.9
Hartalega	HART MK	31-Mar	NR	MYR	7.63	NA	1,844	568	0.6	17.40	9.9	8.4	24.5	13.7	11.6	87.9	79.4	17.8	0.4	5.0	3.7	1.3	2.3	2.7	33.3	38.4	33.5	-	(25.5)	(71.5)
Latexx Partners	LTX MK	12/2009	NR	MYR	3.70	NA	743	229	2.4	11.88	6.5	5.0	18.9	9.7	7.7	NA	69.4	38.2	-	-	-	1.0	1.7	2.3	35.9	46.5	40.4	-	-	-
Adventa	ADV MK	10/2009	NR	MYR	3.31	NA	487	150	1.6	15.58	9.3	6.8	18.8	11.1	8.0	NA	41.5	39.1	2.4	2.2	1.8	1.1	2.2	3.1	8.6	22.7	24.1	51.8	70.7	79.9
Malaysia Top 3 (41% Mkt share)								**689**	**3.6**	**6.9**	**8.4**	**7.0**	**14.2**	**11.9**	**10.0**	**112.9**	**61.0**	**21.0**	**3.2**	**3.0**	**2.5**	**2.6**	**3.1**	**3.5**	**23.6**	**28.1**	**26.8**	**11.7**	**9.9**	**0.7**
Malaysia (51% Mkt share)								**502**	**2.5**	**10.9**	**8.5**	**6.9**	**17.5**	**11.7**	**9.6**	**104.5**	**62.2**	**26.4**	**2.5**	**3.3**	**2.6**	**1.9**	**2.6**	**3.1**	**24.8**	**32.0**	**29.7**	**21.7**	**15.0**	**2.1**
Top 5 regional (62% Mkt share)								**890**	**4.1**	**6.6**	**8.4**	**7.1**	**13.2**	**13.6**	**11.6**	**55.7**	**40.8**	**18.6**	**2.6**	**2.8**	**2.4**	**3.2**	**3.1**	**3.5**	**19.9**	**23.0**	**22.6**	**1.1**	**2.2**	**(6.7)**
Rubber glove								**674**	**3.2**	**9.7**	**8.4**	**7.0**	**16.0**	**12.8**	**10.7**	**62.2**	**49.3**	**23.5**	**2.3**	**3.0**	**2.5**	**2.4**	**2.7**	**3.2**	**22.2**	**27.9**	**26.4**	**9.5**	**8.0**	**(3.6)**
Rubber products																														
Lanxess	LXS GR	31-Dec	Buy	EUR	35.50	38.00	2,953	3,849.1	27.1	6.7	6.8	5.5	16.3	12.7	9.5	(69.4)	143.9	33.8	1.5	1.9	1.6	2.7	2.1	2.8	2.8	14.0	18.3	54.9	57.1	47.0
Sumitomo Rubber	5110 JP	31-Dec	NR	JPY	844.00	NA	222,008	2,343.6	13.0	8.1	7.4	6.6	36.4	17.4	12.3	121.2	109.6	40.6	1.2	1.2	1.1	2.1	2.0	2.2	3.5	6.5	8.7	119.5	124.6	114.5
Yokohama Rubber	5101 JP	31-Mar	NR	JPY	441.00	NA	151,086	1,594.9	8.3	8.6	6.7	6.6	-	16.2	14.9	(124.6)	(261.6)	8.7	1.0	1.0	1.0	2.4	2.3	2.4	(4.7)	6.1	6.8	112.3	97.8	90.2
Tokai Rubber Ind	5191 JP	31-Dec	NR	JPY	1,154.00	NA	120,065	1,267.4	4.3	4.2	4.1	3.7	80.0	44.4	19.0	(90.1)	80.1	133.6	0.8	0.9	0.9	1.2	1.0	1.2	1.0	2.5	4.8	(4.6)	(12.9)	(19.8)
Sri Trang Agro	STA TB	12/2009	NR	THB	55.00	NA	11,000	339.9	3.1	12.8	20.2	18.9	9.5	15.9	16.9	108.1	(40.6)	(6.1)	1.7	1.5	1.4	3.1	1.8	1.8	19.2	9.1	8.9	-	-	-
Rubber products								**1,879.0**	**11.2**	**8.1**	**9.0**	**8.2**	**35.5**	**21.3**	**14.5**	**(11.0)**	**6.3**	**42.1**	**1.3**	**1.3**	**1.2**	**2.3**	**1.8**	**2.1**	**4.4**	**7.7**	**9.5**	**70.5**	**66.6**	**58.0**
DB global rubbber universe average									**90.0**	**8.7**	**9.3**	**8.2**	**22.8**	**18.2**	**14.3**	**14.5**	**23.0**	**27.0**	**2.1**	**2.5**	**2.2**	**2.2**	**2.1**	**2.4**	**14.8**	**17.4**	**17.5**	**26.8**	**22.2**	**17.0**

Source: Deutsche Bank estimates, Bloomberg

** Refers to Bloomberg consensus estimates*

Source: Deutsche Bank, Bloomberg

Malaysian glove industry

Key themes

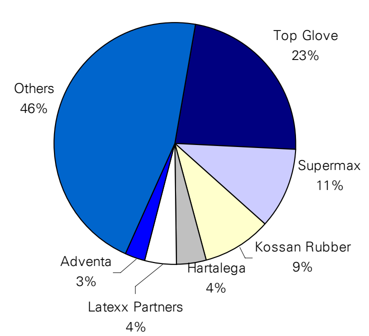
- Malaysia is the world's largest supplier of global rubber gloves (medical, surgical, etc.) demand with 65% of global market share.
- Significant consolidation over the last 10 years has resulted in just a handful of large players dominating the global market space. The top three players in Malaysia alone command 43% of the world's glove supply.

Industry overview – sheer dominance in the industry

Malaysia is the world's largest exporter and producer of rubber gloves, supplying 60-65% of global demand

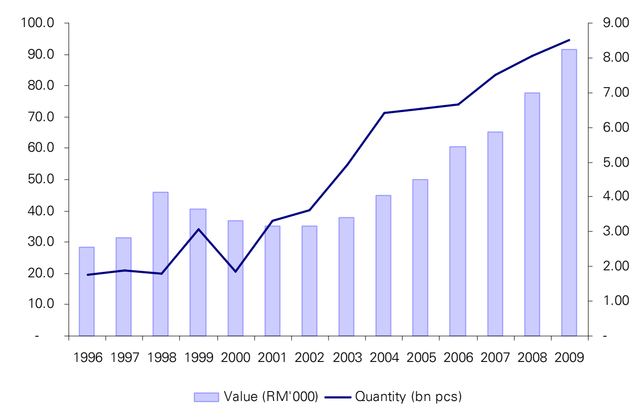
The Malaysian rubber glove industry is one of the few industries where domestic companies boast global market dominance. Malaysia is the world's largest exporter and producer of rubber gloves, supplying 60-65% of global demand. As of 2009, the industry generated MYR7.4bn in export revenues and 92bn pieces of gloves were produced. Malaysia's top six players in the industry, namely Top Glove, Supermax, Kossan Rubber, Hartalega, Latexx Partners and Adventa control a combined 51% of the total global supply of rubber gloves, producing a combined annual volume of c.74bn pieces of gloves in 2009.

Figure 5: Malaysian companies dominate the industry



Source: Deutsche Bank, company data

Figure 6: Malaysian exports and value of rubber gloves



Source: Deutsche Bank

The market has consolidated significantly

The rubber glove industry in Malaysia is currently dominated by very few large players

The initial surge in rubber glove demand started in the early 1990s due to the spread of AIDS and a heightened need for protection in the medical industry against contamination. Malaysia is one of the top three producers of natural rubber (NR) in the world. Given its close proximity to the source of raw material, natural rubber, hundreds of local, small glove manufacturers started mushrooming up in the country. The glove industry has been consolidating over recent years, with many smaller players shutting down due to the lack of economies of scale, falling glove prices and more stringent regulations on the quality of gloves from various governments. The number of Malaysian companies producing gloves fell from 133 in 2000 to c.45 currently. Globally, more and more companies are looking to Asia, i.e. Malaysia and Thailand, to outsource the manufacturing of rubber gloves for cost reasons. The rubber glove industry in Malaysia is currently dominated by very few large players.

Major clients

Most of the glove manufacturers in the industry are predominantly original equipment manufacturers (OEM) and produce gloves to sell mainly to multinational resellers such as Ansell, Kimberly Clark, Cardinal Health, Medline and Microflex. Given the near commoditization of the product, whereby pricing plays an important decision factor for these multinational resellers, the industry has become highly competitive.

Differentiating to compete

The companies have taken to positioning themselves with different strategies to compete.

Top Glove has emerged as the leading market leader in the glove industry with 33bn pieces production capacity.

- **Production scale.** Top Glove has emerged as the leading market leader in the glove industry. In 20 years, the company has increased its production capacity from one factory producing 1.5bn pieces of gloves in 1991 to 20 factories producing 33bn pieces of gloves currently. While other manufacturers have started to vary their product mix to increase margins through producing higher valued rubber gloves such as powder-free natural rubber and nitrile gloves, Top Glove has kept its focus on capturing market share of emerging market glove demand. Top Glove continues to allocate c.58% of its production capacity on powdered NR gloves, which has allowed the company to enter emerging markets where awareness of hygiene standards is still in its infancy stage and price-sensitive consumers demand low-cost powdered natural rubber gloves as a start to its healthcare reforms.

Figure 7: Capacity expansion of the top four glove manufacturers in Malaysia

	As at			Absolute increase in no. of gloves		Growth in capacity	
	2009	2010E	2011E	2010E	2011E	2010E	2011E
Top Glove	31.5	35.3	41.3	3.8	6.0	12%	17%
Supermax	14.5	17.6	21.7	3.1	4.1	21%	23%
Kossan*	11.0	14.5	17.4	3.5	1.0	32%	20%
Hartalega*	6.2	8.4	9.9	2.2	1.5	35%	18%

**Estimates for both companies are provided by the companies themselves. Source: Deutsche Bank estimates, company data*

Malaysian gloves are predominantly sold to multinational original equipment manufacturing (OEM) resellers

- **Growing the original brand manufacturing (OBM) segment**. Malaysian gloves are predominantly sold to multinational original equipment manufacturing (OEM) resellers. The average requirement ratio among glove buyers is about 80% for OEM production versus 20% for original brand manufacturing (OBM) production.

Figure 8: Revenue mix between OEM and OBM

	OEM	OBM
Top Glove	80%	20%
Supermax	70%	30%
Kossan Rubber	90%	10%
Hartalega	87%	13%

Source: Deutsche Bank estimates, company data

Shifting production mix towards the powder-free and nitrile segment for better margins

- **Balancing the product mix for better margins.** Powder-free NR and nitrile gloves usually command a 10-15% premium versus the powdered NR gloves. Given the higher pricing and margins, glove manufacturers in Malaysia have increased their production mix towards the powder-free and nitrile segment.

Figure 9: Product mix of the top four glove manufacturers in Malaysia

	Powdered	Powder-free	Nitrile	Others
Top Glove	58	23	7	12
Supermax	45	35	20	-
Kossan Rubber	20	40	40	-
Hartalega	4	16	80	-

Source: Deutsche Bank, company reports

- **Integrating businesses to capture efficiencies of the value chain.** Most glove manufacturers focus primarily on manufacturing. However, we have seen more efforts by the dominant players to integrate their business to capture the value chain. Top Glove has gone upstream through two latex concentrate manufacturing plants in Thailand and has maintained that it is looking to expand its upstream capabilities. Supermax expanded its downstream capabilities through developing its own brand of gloves and setting up its own distribution centres in their major markets.

Pricing power sustained

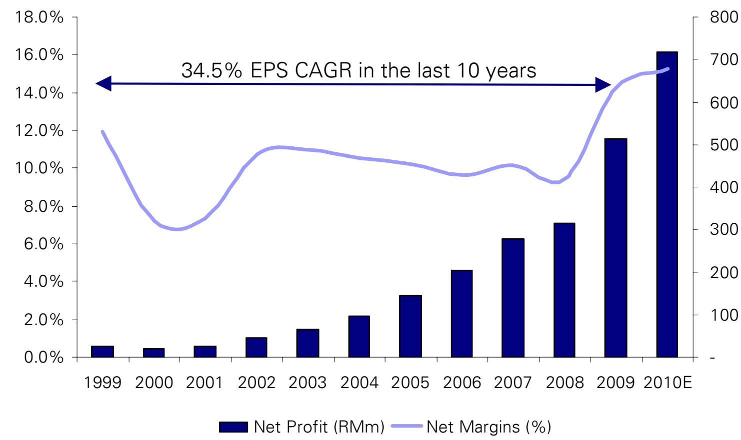
We believe that most of the appreciating momentum for the MYR has peaked and is now on neutral levels

The MYR has been one of the best performing currencies in Asia YTD, having appreciated 8% against the US dollar. Deutsche Bank's economics team now believes most of the appreciating momentum for the MYR has peaked and is now on neutral levels. We have assumed average US$/MYR of MYR3.10 for 2010E and US$/MYR of MYR3.00 for FY11-12E for our earnings forecasts for Top Glove and Supermax. While we believe that, in general, a stronger MYR is negative for the glove manufacturers given that more than c.90% of their revenues are from export businesses, we note glove manufacturers have incorporated this volatility in their selling prices and should thus sustain margins.

Negative effect on margins owing to the current run-up in costs would be short term until higher selling prices are pushed through

We believe the negative effect on margins owing to the current run-up in costs would be short term, as glove manufacturers are more efficient in pushing through price increases this time around. After the lessons learned from 2008, we believe glove manufacturers are now more sophisticated in managing their risks to these costs pressure. Apart from passing on the cost increases to customers and limiting price quotes to one-month forward sales in the short term to mitigate margin risks, manufacturers have also made efforts to enhance their internal production efficiencies, such as installing automated glove stripping machines as opposed to using manual labour, longer and faster production lines to increase output and utilization rates and burning fuel more efficiently, etc., which has led to an improvement in margins.

Figure 10: The glove industry's net profit increased at 34.5% CAGR over the last 10 years despite rising input costs



*Source: Deutsche Bank * Industry revenue is an aggregate of the top 4 players in Malaysia, namely Top Glove, Supermax, Kossan and Hartalega*

Glove demand

Key themes

- We are bullish on demand for gloves and expect long-term growth of 13% CAGR for the next 10 years. We expect glove usage per person to increase 3.3x from 21 pieces in 2009 to 70 pieces by 2020E. (The current average developed market consumption is 108 pieces, while the average in emerging markets (China and India) is three pieces.)
- Growth in demand is driven by population and aging population growth, increased penetration in emerging markets due to sanitation awareness, government healthcare reforms and regulations.
- Demand is inelastic to economic cycles given that it is a basic necessity for protection in the healthcare industry. This should underpin demand for the glove replacement market (85-90% of demand). Sporadic outbreaks of diseases too should also help to create 'new' demand (2%), with underlying organic growth at (8%). We expect this multi-year growth trend to persist.

Growth = healthcare reforms + health scare precautions

Based on our supply and demand analysis, we are bullish on demand for rubber gloves and expect the industry to grow at a CAGR of 13% for the next 10 years

Based on our supply and demand analysis, we are bullish on demand for rubber gloves and expect the industry to grow at a CAGR of 13% for the next 10 years. Historically, glove demand has been growing at an 8-10% annual rate for the past 10 years. Our expectations for the higher growth are driven by the assumption that there will be new demand from 1) aggressive healthcare reforms by governments around the world, especially the US and China; and 2) the ever-present threat of outbreaks of diseases globally and governments' initiatives to stock up medical supplies to cater to such emergencies. Growth also underpins our view that glove demand is relatively inelastic to economic cycles given its use as a basic necessity for protection against contamination in the healthcare industry and that the per unit usage cost for gloves (c.US$0.06/pair of powder-free examination gloves) is insignificant relative to total healthcare spending.

Global demand for rubber gloves grew 16.2% YoY to 145.3bn pieces in 2009. Assuming on a normalized basis that the industry grew at a 10% rate in 2009, we estimate that the H1N1 flu pandemic contributed to an additional 12.5bn pieces, or a c.15% increase in absolute industry volume during the year. We expect governments' efforts to ensure they are stocked up with basic medical protection in the event of further disease outbreak risks to ensure stepped up demand for disposal rubber gloves. The US and Europe currently account for c.70%, or 102bn pieces, of total world demand for rubber gloves, implying that an average person in the US and the EU uses about 108 pieces of gloves annually. This is 5x more than the current world average of 21 pieces of glove usage per person per year globally.

Figure 11: Healthcare spending and glove consumption estimates

Country	Population (bn)	Healthcare expenditure per capita (US$)	Healthcare % of GDP	Glove usage per capita (pcs)
United States	0.303	6,714	15.3	127.0
EU	0.492	2,323	8.0	89.0
Japan	0.128	2,514	7.9	38.0
Australia	0.021	3,122	8.7	133.0
Brazil	0.189	765	7.5	22.0
Russia	0.143	638	5.3	17.0
China	1.328	342	4.5	3.5
India	1.152	109	4.9	3.0

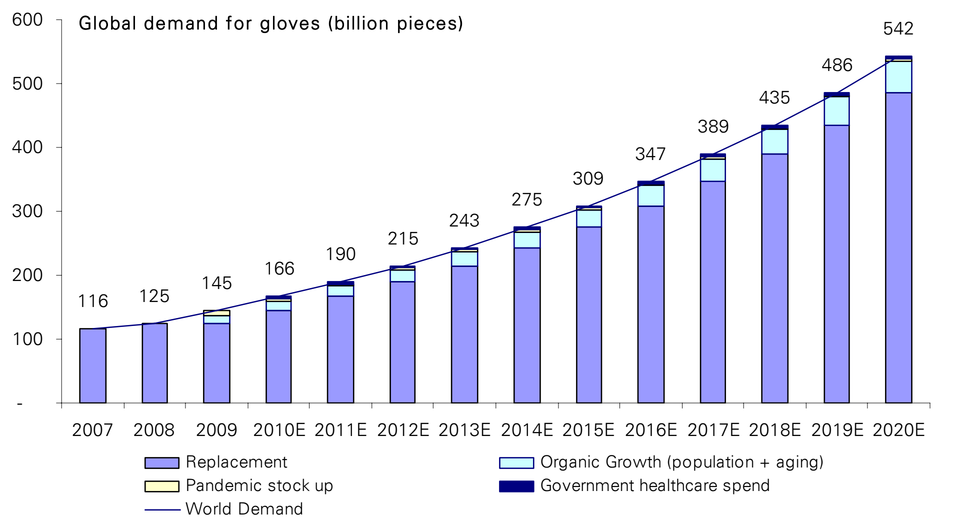
Source: Deutsche Bank, WHO 2006 Yearbook

Figure 12: Our forecast of glove demand

Billion pieces	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Replacement	125	145	166	190	215	243	275	309	347	389	435	486
Organic growth	12.5	14.5	16.6	19.0	21.5	24.3	27.5	30.9	34.7	38.9	43.5	48.6
Pandemic stock up	10.0	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5
Government healthcare spending		3.1	3.2	3.3	3.4	3.5	3.6	3.7	3.8	3.9	4.0	4.1
Total world demand	**145**	**166**	**190**	**215**	**243**	**275**	**309**	**347**	**389**	**435**	**486**	**542**
% change YoY	**16%**	**14%**	**14%**	**14%**	**13%**	**13%**	**13%**	**12%**	**12%**	**12%**	**12%**	**12%**

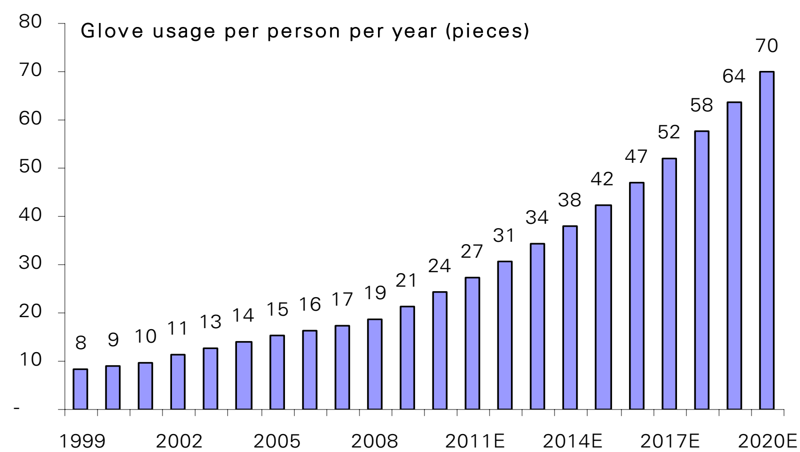
Source: Deutsche Bank estimates and company reports

Figure 13: We expect global demand for gloves to increase at a CAGR of 13% for the next 10 years



Source: Deutsche Bank, UN Population estimates

Figure 14: Global usage for gloves is still low at 21 pieces per person



Source: Deutsche Bank, UN Population estimates

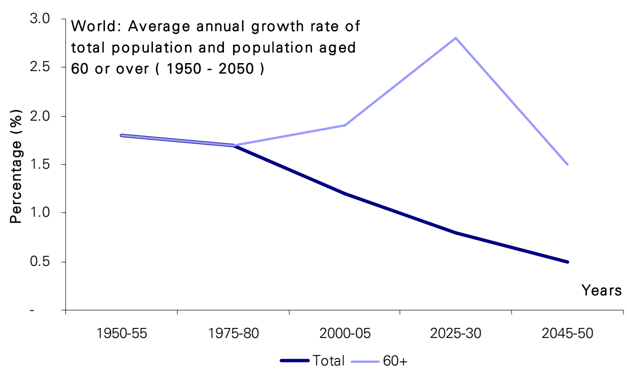
Demand drivers

We expect global demand for rubber gloves (medical examination in general, including exam and surgical) to increase and intensify due to growth in the aging population, greater awareness of hygiene standards in emerging markets such as China, India and Africa, increasing occupational safety standards and regulation, government healthcare reforms as well as high replacement in Western countries given their high and stable healthcare spends as a percentage of GDP.

We expect glove demand to be driven by faster growth in the aging population

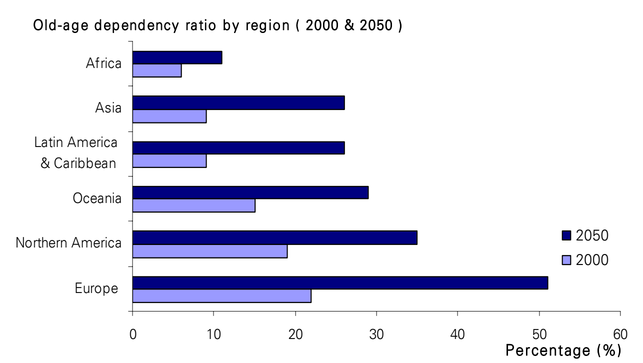
1. **Population growth and aging population:** We expect glove demand to be driven by faster growth in the aging population. The older population is growing at a faster rate than the total population in practically all regions of the world. According to the UN World Population Aging Report 1950-2050, the current growth rate for older populations is 1.9% p.a., compared to the total population growth rate of 1.2% p.a., and the gap is increasing. In the next half century, the difference between the two growth rates should widen to more than 3x as the baby boom generation starts to reach older ages in the more developed parts of the world. A research survey conducted by the WHO reveals that aging citizens are 3.2x more prone to develop chronic diseases compared to other age groups. With heightened demand for medical treatment, glove usage will also increase.

Figure 15: Aging population growing faster than world population



Source: UN World Population Aging 1950 - 2050

Figure 16: Developed world population dynamics allow for sustained replacement demand for gloves



Source: United Nations World Aging Population 1950 - 2050 report

Europe and North America represent high-volume replacement markets

2. **Replacement demand for gloves in the Western world is likely to be sustained.** Although growth in glove demand seems relatively limited in mature Western markets like Europe and North America (demand saturated, penetration high and marginally flat healthcare spend), these markets represent high-volume replacement markets. Meanwhile, the need for more healthcare services by the aging population and because these developed parts of the world will see a faster rate of aging population growth, we expect more nursing homes to be established in these countries. As a result, we expect replacement demand from gloves in the Western world to be sustained given that it already accounts for 75% of world demand currently.

The US and China governments are budgeting more than US$100bn in healthcare spending over the next two years

3. **Increasing healthcare spending and reforms**. Healthcare spending as a percentage of GDP is still relatively low in developing and emerging markets, but we expect these countries to play catch up on spending and will see it likely to converge to Western standards quickly. China, for example, is likely to increase healthcare spending by 7x, or c.20% p.a., between 2008 and 2018. This, compounded by demand from the recently passed US healthcare reform bill, will see at least another 10%, or 4.5bn pieces, of new demand for gloves in 2010E.

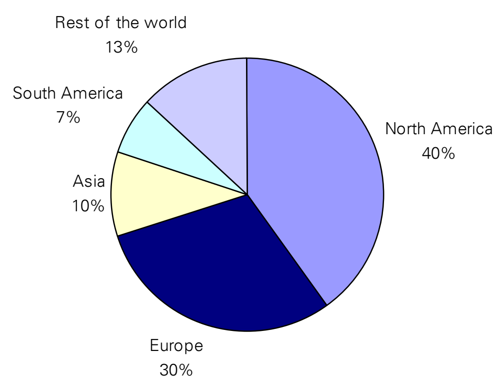
Figure 17: 2006: WHO healthcare spending and statistics

Indicator	US	Germany	France	Switzerland	Japan	China	India	Mexico	Brazil
GNP per capita (US$)	44,070	32,680	32,240	40,480	32,840	4,660	2,460	11,990	8,700
Govt. expenditure as a % of total health expenditure	45.8%	76.6%	79.7%	60.3%	82.2%	42.0%	19.6%	43.3%	47.9%
Private expenditure as a % of total health expenditure	54.2%	23.4%	20.3%	39.7%	17.8%	58.0%	80.4%	56.7%	52.1%
Out-of-pocket expenses as a % of private expenditure on health	23.5%	56.7%	33.2%	76.2%	82.4%	92.9%	94.0%	92.5%	64.0%
Per capita govt. expenditure on health (avg. ex-rate US$)	3,074	2,809	3,233	3,541	2,212	38	8	217	204
Per capita total expenditure on health (avg. ex-rate US$)	6,714	3,669	4,056	5,878	2,690	90	39	500	426
Govt. expenditure on health as a % of total govt. expenditure	19.10%	17.60%	16.70%	19.60%	17.70%	9.90%	3.40%	11.00%	7.20%
Healthcare expenditure as a % of GDP	15.30%	10.40%	11.10%	11.30%	7.90%	4.50%	4.90%	6.20%	7.50%
Adult mortality rate per 1000 persons (persons)	109	81	91	63	67	116	241	122	176
Infant mortality rate per 1000 persons (persons)	7	4	4	4	3	20	57	29	19
Life expectancy at birth for both sexes (years)	78	80	81	82	83	73	63	74	72

Source: WHO

1. **Growth in emerging market demand.** Currently 70% of the world's demand for gloves is consumed by c.12% of the world's population. Assuming that every citizen in China and India starts using a piece of glove during the year, it would add 2.5bn pieces (or 2%) to global demand.

Figure 18: Global glove demand by region



Source: Deutsche Bank, company reports and industry feedback

Glove supply

Key themes

- Contrary to market expectations, we believe new glove supply will only grow by c.13% in 2010E and 17% in 2011E, or realistically see about 19bn pieces of new gloves supply in 2010E and another 22bn pieces in 2011E, just enough to meet global demand for gloves.
- We expect new additions to be progressive rather than immediate, and the absolute amount of gloves supplied in the industry is only about 75% of total planned capacity, given bottlenecks in the natural gas supply, delays in equipment delivery and lag-time needed for production set up to reach optimum utilization.

Scaling up to meet demand

A trend towards outsourcing glove production to Asia continued by MNCs to keep costs low has allowed Malaysian manufacturers to continue to scale up production and maintain their market leader position in the supply of gloves (NR and SR) due to the strategic location to the main source of raw materials, economies of scale, production efficiency and established distributor network.

We believe the current average capacity expansion plan of 17% p.a. in 2010-11E for the industry players is to catch up to pent up demand rolled over from 2009

We believe the concern of overcapacity in the glove industry is overdone. The glove industry did not expand its capacity significantly in 2009 but saw heightened demand during the year as a result of the H1N1 outbreak. Our observations on the industry is that the players are usually cautious and its capacity expansion plans are almost demand led, motivated by indications of forwards orders by its larger customers (i.e., the MNC resellers). We believe the current average capacity expansion plan of 17% p.a. in 2010-11E for the industry players is to catch up to pent up demand rolled over from 2009.

We estimate that the increase in total capacity by the four largest players in the industry is likely to add 20% of planned capacity in 2010E and 19% in 2011E, implying an additional 12.8bn and 14.7bn pieces of gloves in absolute terms for 2010-11E, respectively. Assuming that the rest of the glove manufacturers expand at a rate of 15% p.a. (the slower growth expectations are based on MNC manufacturers under this classification not expanding capacity and the rest of the manufacturers being too small to make a significant effect in absolute terms), we believe the industry will only realistically see about 19-21bn pieces of new glove supply in 2010E and another 20-22bn pieces in 2011E, just enough to meet global demand for gloves.

Figure 19: Global capacity addition estimates

	As at			Absolute increase in no. of gloves		Growth in capacity		Global market share (%)
	2009	**2010E**	**2011E**	**2010E**	**2011E**	**2010E**	**2011E**	**2009**
Top Glove	31.5	35.3	41.3	3.8	6.0	12%	17%	22%
Supermax	14.5	17.6	21.7	3.1	4.1	21%	23%	10%
Kossan*	11.0	14.5	17.4	3.5	2.5	32%	20%	8%
Hartalega*	6.2	8.4	9.9	2.2	1.5	35%	18%	4%
Rest of the world	83.0	95.5	109.8	12.5	14.3	15%	15%	57%
Total World Supply	**146.2**	**171.2**	**200.1**	**25.0**	**28.9**	**17%**	**17%**	**100%**
75% utilization	**146.2**	**165.0**	**192.7**	**18.8**	**21.6**	**13%**	**17%**	

**Estimates for both companies are provided by the companies themselves. Source: Deutsche Bank calculations, company data*

New capacity additions to be progressive rather than immediate

While glove manufactures announce aggressive capacity expansion plans, we expect new capacity additions to be progressive rather than immediate. This is due to the new set up of production lines that takes time to achieve optimum utilization, which typically ranged around 75-80%. Capacity expansion is also constrained by there being only a limited number of suppliers of specialized equipments (formers, chains, etc.) in the glove industry and these suppliers have limited spare capacity to cater to heighten demand. As such, we see bottlenecks in natural gas supply, delays in equipment delivery, time needed for production set up as well as lower actual capacity utilization that cap the absolute amount of gloves supplied in the industry to be lower than actual planned capacity.

Rubber market overview

Key themes

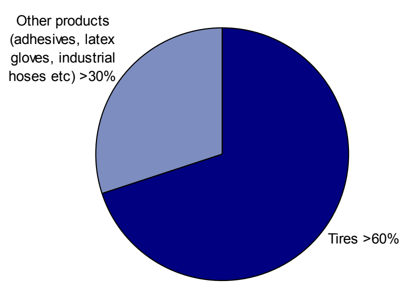
- The rubber industry has lagged other soft commodities in terms of new plantings due to historically weak prices and the switch of land use to oil palm plantations.
- Structurally, we believe rubber prices will stay higher due to rising demand globally, especially from the automotive industry, coupled with limited supply growth due to lower yields from mature trees in top producing countries and progressive declines in tapped areas in countries such as Malaysia

Dynamics of rubber demand and supply

The automotive industry is the largest end-consumer of rubber

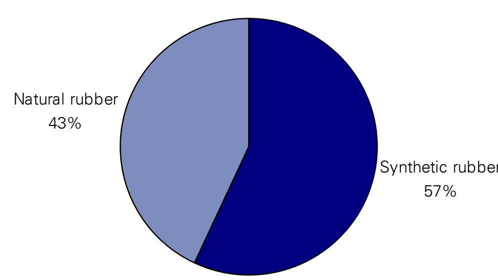
The rubber industry sources two main kinds of rubber – natural and synthetic – in order to produce intermediate and finished products. The automotive industry is the largest end-consumer, as tires account for around two-thirds of all rubber parts produced for different applications. Apart from tires, rubber is used in industrial machinery and equipment, building and construction, fashion and sports (shoes, balls, clothes, etc.) and healthcare products (gloves, condoms, etc.). The industry is fragmented, featuring various sub-sectors that produce a range of products for different uses and industries. Economies of scale, different processing and manufacturing technologies, supply and sales distribution network are key differentiating factors in the industry.

Figure 20: Rubber consumption by application/product



Source: International Rubber Study Group

Figure 21: Rubber consumption by type, 2009

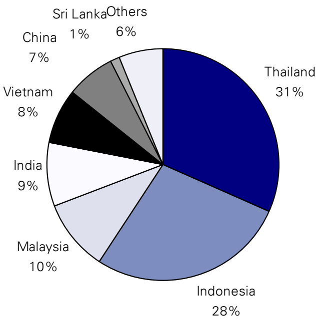


Source: International Rubber Study Group

More than 94% of NR is produced in Asia, of which Thailand, Indonesia and Malaysia account for 69% of the global supply

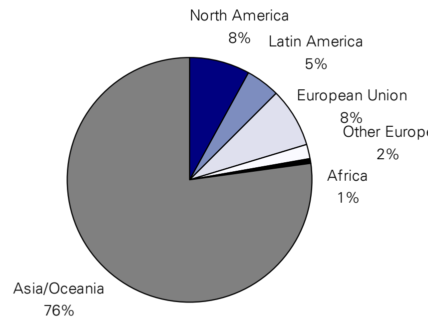
Natural rubber production is a labour-intensive process, with the major producers and/or exporters located mainly in developing Asia. More than 94% of NR is produced in Asia, of which Thailand, Indonesia and Malaysia account for 69% of the global supply. Meanwhile, Asia is also the largest consumer of NR, accounting for 76% of global consumption.

Figure 22: Natural rubber production, 2010 estimates



Source: Association of Natural Rubber Producing Countries (ANRPC), Deutsche Bank

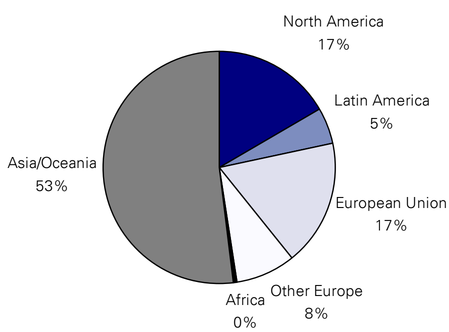
Figure 23: Natural rubber consumption, 2009



Source: International Rubber Study Group

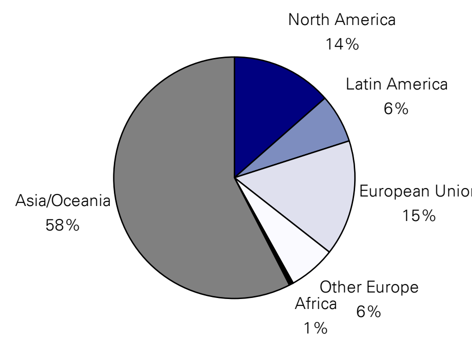
Asia is also the largest producer/consumer of SR, used to extend and/or substitute NR supply. Accordingly, SR is also produced in Western markets like Europe and North America which account for quite respectable shares in global SR production and consumption after Asia.

Figure 24: Synthetic rubber production, 2009



Source: Association of Natural Rubber Producing Countries (ANRPC), Deutsche Bank

Figure 25: Synthetic rubber consumption, 2009



Source: International Rubber Study Group

The rubber market is currently driven by buoyant demand and limited growth in supply

The rubber market is currently driven by buoyant demand as a result of global economic recovery and limited growth in supply due to poor weather conditions in major producing countries, a longer-term, progressive decline in tapped rubber areas in major rubber producing countries such as Malaysia and declining yields, given that the large extent of existing yielding trees in all major producing countries that were planted during the 1980s have reached maturity and a phase of declining yields.

According to Association of Natural Rubber Producing Countries (ANRPC), which tabulates demand and supply data for 94% of the global supply of natural rubber, the global supply of NR is unlikely to rise beyond 6% in 2010. However, NR consumption in the first two months of 2010 in China, India and Malaysia, which accounts for 45% of global NR consumption, grew 13.9% YoY.

Figure 26: Natural rubber production by major countries (94% to total world production)

	NR production ('000 tons)								Tapped area ('000 ha)			
	2007	**yoy**	**2008**	**yoy**	**2009**	**yoy**	**2010**	**Yoy**	**2007**	**2008**	**2009**	**2010**
Thailand	3,056	(2.6)	3,090	1.1	3,164	2.4	3,164	-	1,774	1,819	1,840	1,840
Indonesia	2,755	4.5	2,751	(0.1)	2,595	(5.7)	2,770	6.7	2,776	2,769	2,770	2,773
Malaysia	1,200	(6.5)	1,072	(10.7)	856	(20.1)	1,000	16.8	1,146	760	740	740
India	811	(4.9)	881	8.6	820	(6.9)	891	8.7	459	463	466	472
Vietnam	606	9.1	660	8.9	724	9.7	770	6.4	373	339	422	445
China	588	9.3	548	(6.8)	646	17.8	680	5.3	503	520	545	567
Sri Lanka	118	7.7	129	9.9	137	6.0	142	3.7	94	94	95	95
Total	**9,134**	**0.2**	**9,131**	**(0.0)**	**8,942**	**(2.1)**	**9,417**	**5.3**	**7,126**	**6,764**	**6,878**	**6,932**
Average yield kg/ha									**1,282**	**1,350**	**1,300**	**1,358**

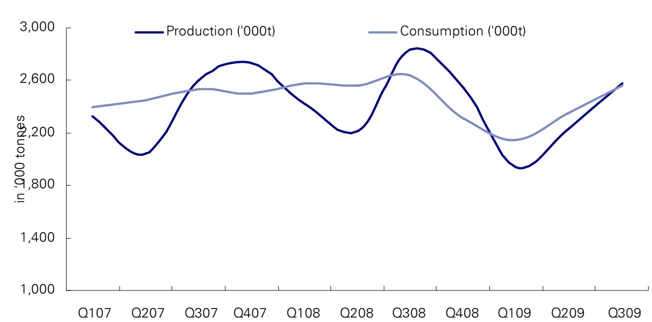
*Source: Deutsche Bank, Association of Natural Rubber Producing Countries (ANRPC). * Where there are no data, i.e. Thailand 2010 production forecast, we have assumed flat growth and rolled over the data from 2009.*

Figure 27: Top three global consumers of NR (YTD February 2010)

	YTD Feb-10	YTD Feb-09	% change
China	370.0	330.0	12.1%
India	159.0	136.0	16.9%
Malaysia	81.0	69.5	16.5%
Total	**610.0**	**535.5**	**13.9%**

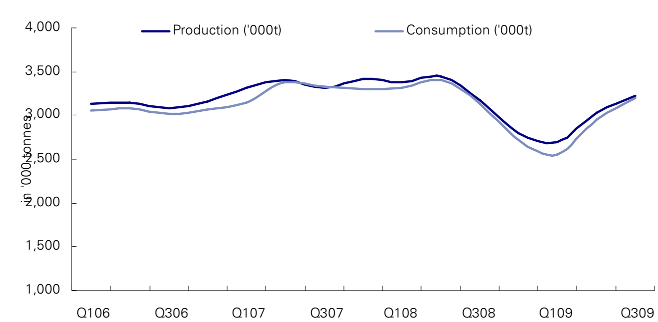
Source: Deutsche Bank, Association of Natural Rubber Producing Countries (ANRPC)

Figure 28: NR – quarterly demand/supply development



Source: International Rubber Study Group

Figure 29: SR – quarterly demand/supply development



Source: International Rubber Study Group

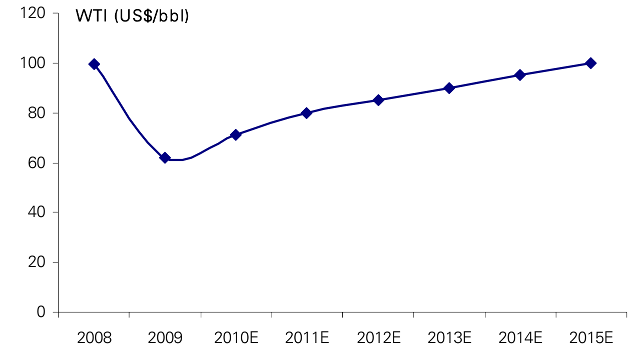
Rubber price outlook

Besides the normal demand and supply dynamics, NR and SR prices are also influenced by US dollar strength/weakness against the major producing countries, the wintering season for the rubber crops, crude oil prices and the availability of the supply of its basic feedstock butadiene in the case of SR.

NR prices will likely remain high

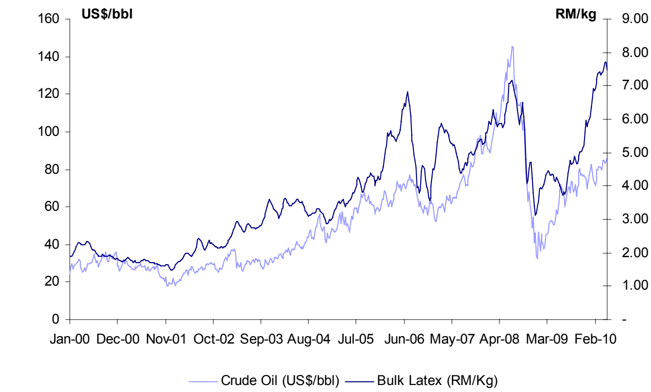
We believe that, in the longer term, NR prices will likely remain high, driven by the three major producing countries, Thailand, Indonesia and Malaysia, and three major consuming economies, China, India and Malaysia, being the fastest growing economies in the world. NR prices will likely remain high, with continued global demand for NR, compounded by progressive declines in tapped areas and existing yielding trees in all major producing countries being planted during the 1980s and having now reached the declining yield phase, whereby the composition of the existing yielding area is unfavourable to an improvement in yield. Meanwhile, SR rubber is a function of the outlook for crude oil prices. Deutsche Bank's global commodities team has forecast crude oil of US$85/bbl in 2010E and US$95/bbl.

Figure 30: Deutsche Bank oil price forecasts (US$/bbl)



Source: Deutsche Bank

Figure 31: Crude oil vs. Malaysian grade rubber shows close correlation

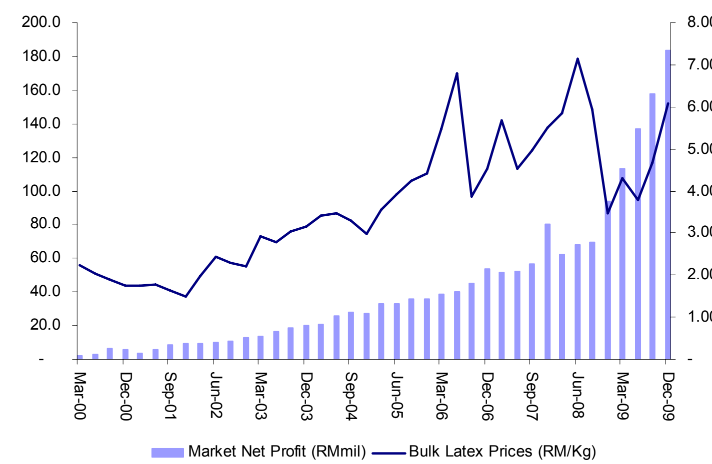


Source: Deutsche Bank, Bloomberg

We assumed that latex prices will normalize to a higher level of MYR5.90/kg in 2010

After the subdued 2009 prices, we assumed that latex prices will normalize to a higher level of MYR5.90/kg in 2010, 4% higher than the 2008 average price of MYR5.68/kg, as a result of recovery in demand and limited growth in supply conditions. Latex costs account for 55-60% of the gloves manufacturers' costs of production. While latex price volatility is a major concern for glove manufacturers, they have historically been able to pass on higher costs to customers, albeit with a one- to two-months time lag. This can been seen by the aggregate total net profits of the four largest glove manufacturers rising 400% over the last five years while rubber prices increased 88% during the same period.

Figure 32: Glove manufacturers have generally been able to pass on higher latex costs, and increase their net profits over the years



Source: Deutsche Bank calculations, company data

Risks

Key risks

Industry risks

1. Excess capacity. The players in the industry have undertaken aggressive capacity expansion plans and may result in an oversupply situation.

2. Sharp volatility in latex costs and foreign currencies resulting in near-term margin squeeze.

3. Political risks, domestic and regional. Glove manufacturers source c.50% of their raw material (natural rubber latex) from Thailand. The risks are shortage of NR latex supply slowing production output at glove manufacturers.

4. Infrastructural bottlenecks and labour shortages. Malaysia's natural gas supply to the glove industry has reached maximum capacity allocation and new allocations are expected to come on stream only in 2012. Any delay in new allocation will limit capacity expansion for the manufactures and they may have to look for alternative fuel; this may be less efficient or even cost more.

Company-specific risks

1. Weaker-than-expected sales volume.

2. Volatility in prices of raw materials and fuel, which are the two main costs of the company and may result in margin contraction or even losses as there is a lag in cost pass-through.

3. Execution risks related aggressive capacity expansion plans. The market is constantly concerned about excess capacity plans, given that most of the major players plan to expand capacity in the next two years.

4. Over-paying for acquisitions or investments.

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Asia ASEAN Malaysia
Industrials Manufacturing

6 May 2010

Top Glove

Reuters: **TPGC.KL** Bloomberg: **TOPG MK**

Dominant leader; initiate with Buy

Global leader in a growing market
Top Glove is the world's leading disposal glove manufacturer, with a 23% global market share. The company is extending its lead in the global glove industry, which is growing at 13% pa, thanks to increasing global healthcare needs, government healthcare reforms and improving hygiene standards. With a three-year EPS CAGR of 25% and the ability to pass on higher costs, margins should be maintained. We initiate coverage with a Buy rating based on a DCF-derived target price of RM16.50/share, which suggests 34% upside potential.

Positioning itself to capture market share in developing markets
Top Glove has positioned itself as the world's largest producer of basic, entry-level powdered latex gloves, which will allow it to capture growth in demand from emerging markets such as China and India, where consumers are price sensitive and glove usage per capita averages 3.0-4.0 pieces per year. This contrasts with developed markets such as the US and the EU where glove usage per capita averages 108 pieces per year.

Significant balance sheet strength, fund-raising unlikely
As of 2Q FY10, Top Glove had net cash of RM277.7m on its balance sheet. The company has managed to maintain its net cash position for the past five quarters through sound working capital management and strong cash flow generation. We expect that annual free cash flow in excess of RM200m will be more than sufficient to fund capex and debt obligations while at the same time allowing for sustained increased dividends. (Current dividend policy is to pay out 40% of PAT.)

Still room for growth in value; DCF-based target price of RM16.50; risks
Our target price of RM16.50 is based on WACC of 9.98%. This values Top Glove at 18.6x annualized FY10 PE, which is its five-year historical average premium of 21% to the Malaysian market. We believe that the premium valuation for Top Glove is justified given it is a global leader in a defensive industry and offers above-market EPS growth, ROEs and a net-cash balance sheet. Key downside risks include weaker-than-expected demand and volatility in raw material prices.

Forecasts and ratios

Year End Dec 31	2008A	2009A	**2010E**	2011E	2012E
Sales (MYRm)	1,377.9	1,529.1	**2,161.9**	2,497.2	2,750.9
EBITDA (MYRm)	197.9	287.5	**389.7**	451.3	502.4
Reported NPAT (MYRm)	110.0	169.1	**250.6**	293.1	328.1
Reported EPS FD(MYR)	0.37	0.56	**0.82**	0.95	1.07
DB EPS FD(MYR)	0.37	0.56	**0.82**	0.95	1.07
DB EPS growth (%)	16.7	52.7	**46.7**	16.3	11.9
PER (x)	11.9	11.8	**14.2**	12.2	10.9
EV/EBITDA (x)	7.6	7.0	**9.2**	8.0	7.2
DPS (net) (MYR)	0.08	0.16	**0.33**	0.38	0.43
Yield (net) (%)	1.8	2.4	**2.8**	3.3	3.7

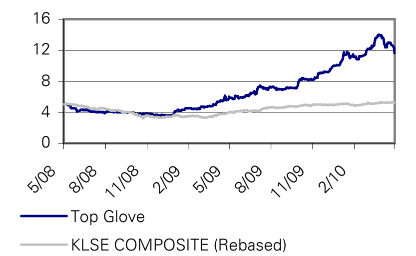
Source: Deutsche Bank estimates, company data

[1] DB EPS is fully diluted and excludes non-recurring items
[2] Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close

Buy

Price at 6 May 2010 (MYR)	**11.60**
Price target - 12mth (MYR)	**16.50**
52-week range (MYR)	**14.00 - 5.70**
KLSE COMPOSITE	**1,332**

Price/price relative



Performance (%)	1m	3m	12m
Absolute	*-16.5*	*3.9*	*93.3*
KLSE COMPOSITE	*-0.9*	*6.7*	*30.1*

Stock data

Market cap (MYRm)	**3,573**
Market cap (USDm)	**1,106**
Shares outstanding (m)	**306.2**
Major shareholders	**Mr Lim Wee-Chai (38.85%)**
Free float (%)	**58**
Avg daily value traded (USDm)	**3.7**

Key indicators (FY1)

ROE (%)	**27.4**
Net debt/equity (%)	**-27.0**
Book value/share (MYR)	**3.26**
Price/book (x)	**3.6**
Net interest cover (x)	**–**
Operating profit margin (%)	**15.2**

Model updated:05 May 2010

Running the numbers

Asia

ASEAN Malaysia

Manufacturing

Top Glove

Reuters: TPGC.KL Bloomberg: TOPG MK

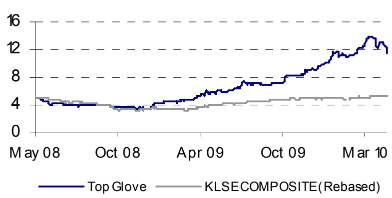
Buy

Price (6 May 10)	MYR 11.60
Target price	MYR 16.50
52-week Range	MYR 5.70 - 14.00
Market Cap (m)	MYRm 3,573 USDm 1,106

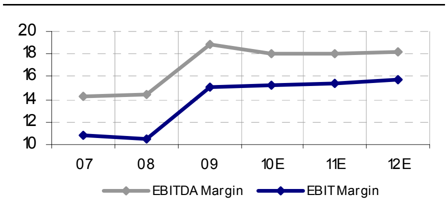
Company Profile

Top Glove Corporation is the world's largest glove manufacturer with an estimated 23% global market share. The company produces a wide range of gloves catering to the medical, food and services, high technology and industrial markets.

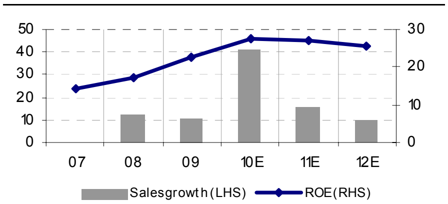
Price Performance



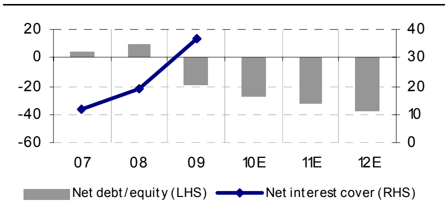
Margin Trends



Growth & Profitability



Solvency



Michelle Foong
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Fiscal year end 31-Dec	2007	2008	2009	2010E	2011E	2012E
Financial Summary						
DB EPS (MYR)	0.31	0.37	0.56	0.82	0.95	1.07
Reported EPS (MYR)	0.31	0.37	0.56	0.82	0.95	1.07
DPS (MYR)	6.67	0.08	0.16	0.33	0.38	0.43
BVPS (MYR)	2.1	2.2	2.7	3.3	3.8	4.5
Weighted average shares (m)	286	301	303	306	308	308
Average market cap (MYRm)	2,241	1,309	1,989	3,573	3,573	3,573
Enterprise value (MYRm)	2,446	1,506	2,021	3,603	3,605	3,607
Valuation Metrics						
P/E (DB) (x)	25.0	11.9	11.8	14.2	12.2	10.9
P/E (Reported) (x)	25.0	11.9	11.8	14.2	12.2	10.9
P/BV (x)	3.15	1.58	3.71	3.56	3.02	2.58
FCF Yield (%)	0.1	1.8	13.3	5.9	8.3	10.0
Dividend Yield (%)	85.0	1.8	2.4	2.8	3.3	3.7
EV/Sales (x)	2.0	1.1	1.3	1.7	1.4	1.3
EV/EBITDA (x)	13.9	7.6	7.0	9.2	8.0	7.2
EV/EBIT (x)	18.5	10.4	8.8	10.9	9.4	8.4
Income Statement (MYRm)						
Sales revenue	**1,229**	**1,378**	**1,529**	**2,162**	**2,497**	**2,751**
Gross profit	**176**	**198**	**288**	**390**	**451**	**502**
EBITDA	**176**	**198**	**288**	**390**	**451**	**502**
Depreciation	43	53	57	60	66	71
Amortisation	0	0	0	0	0	0
EBIT	**132**	**145**	**231**	**329**	**386**	**432**
Net interest income(expense)	-11	-8	-6	1	1	1
Associates/affiliates	0	1	-1	-1	-1	-1
Exceptionals/extraordinaries	0	0	0	0	0	0
Other pre-tax income/(expense)	-3	-4	-1	0	0	0
Profit before tax	**119**	**135**	**222**	**330**	**386**	**432**
Income tax expense	30	27	54	80	94	105
Minorities	-1	-2	-1	-1	-1	-1
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	**90**	**110**	**169**	**251**	**293**	**328**
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	**90**	**110**	**169**	**251**	**293**	**328**
Cash Flow (MYRm)						
Cash flow from operations	**106**	**88**	**332**	**309**	**417**	**476**
Net Capex	-105	-65	-67	-100	-120	-120
Free cash flow	**2**	**23**	**265**	**209**	**297**	**356**
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	0	0	0	0	0	0
Net inc/(dec) in borrowings	-136	-5	-166	-9	1	1
Other investing/financing cash flows	240	-62	-33	-77	-190	-298
Net cash flow	**106**	**-44**	**65**	**123**	**108**	**59**
Change in working capital	*-28*	*-28*	*70*	*-79*	*-87*	*-96*
Balance Sheet (MYRm)						
Cash and other liquid assets	166	122	186	288	403	546
Tangible fixed assets	548	559	564	604	658	707
Goodwill/intangible assets	21	20	20	22	22	22
Associates/investments	18	22	36	31	32	32
Other assets	300	386	326	474	547	603
Total assets	**1,054**	**1,110**	**1,132**	**1,420**	**1,662**	**1,911**
Interest bearing debt	192	187	21	11	12	13
Other liabilities	220	236	266	383	443	489
Total liabilities	**413**	**423**	**286**	**394**	**456**	**503**
Shareholders' equity	620	667	825	1,003	1,183	1,383
Minorities	21	20	21	23	24	25
Total shareholders' equity	**641**	**687**	**846**	**1,025**	**1,207**	**1,408**
Net debt	*27*	*65*	*-165*	*-277*	*-390*	*-533*
Key Company Metrics						
Sales growth (%)	nm	12.1	11.0	41.4	15.5	10.2
DB EPS growth (%)	na	16.7	52.7	46.7	16.3	11.9
EBITDA Margin (%)	14.3	14.4	18.8	18.0	18.1	18.3
EBIT Margin (%)	10.8	10.5	15.1	15.2	15.4	15.7
Payout ratio (%)	nm	21.7	28.6	39.8	40.0	40.0
ROE (%)	14.4	17.1	22.7	27.4	26.8	25.6
Capex/sales (%)	8.5	4.7	4.4	4.6	4.8	4.4
Capex/depreciation (x)	2.4	1.2	1.2	1.7	1.8	1.7
Net debt/equity (%)	4.2	9.5	-19.5	-27.0	-32.3	-37.8
Net interest cover (x)	12.1	19.0	36.6	nm	nm	nm

Source: Company data, Deutsche Bank estimates

Investment thesis

Outlook

Top Glove is extending its lead in the global glove industry. The company is expected to expand its capacity by 12% and 17% in FY10E and FY11E, respectively, adding an absolute 3.75bn pieces and 6bn pieces of gloves over the next two years. With its next closet competitor, Supermax, having only half its production capacity, we expect Top Glove to retain its dominant market leader position.

We estimate that global glove demand will grow at an estimated 13% pa in the coming years, driven by government healthcare reforms, increasing healthcare needs and a general shift toward higher hygiene standards in the emerging markets. Top Glove's market positioning as the world's largest producer of basic, entry-level rubber gloves (powdered latex gloves) will allow it to capture growth in demand from emerging markets such as China and India, where consumers are price sensitive and glove usage per capita averages 3.0 -4.0 pieces per year. This contrasts with developed markets such as the US and the EU where glove usage per capita average 108 pieces per year.

Valuation

We use DCF and PE to value Top Glove. DCF is our primary tool to take into account top Glove's strong cash flow generation and current net cash balance sheet. Our target price of RM16.50 is based on WACC of 9.98% (4.1% risk-free rate, 6.1% average Malaysia market equity risk premium and average 2-year beta of 0.8x) and a terminal growth rate of 5%. The terminal growth rate is based on our longer-term view that glove demand will be driven by both overall population growth and growth of the aging population.

Our target price values Top Glove at 18.6x annualized FY10 PE or a 21% premium to the market PE of 15.4x. The stock has been trading at a five-year historical average premium of 21.1% to the Malaysian market. We believe that the premium valuation for Top Glove is justified given the company's higher-than-market earning growth (EPS growth of 47% in FY10E vs. the market's 29%) and strong balance sheet (net cash vs. market's net gearing of 36%). The market has always applied a premium to quality companies such as Public Bank and KL Kepong in Malaysia and we believe that Top Glove, given its global leader position in a defensive industry, should trade at such a premium.

Risks

Key risks include: 1) excess production capacity going into 2H10 as glove manufacturers had embarked on aggressive capacity expansion plans that started in mid-2009 following the run-up in demand during the peak of the pandemic influenza threat; 2) volatility in raw material costs and currency fluctuations, which would affect margins; and 3) slowing global demand for gloves, as concerns over the threat of the H1N1 influenza subside.

Valuation

DCF-based target price of RM16.50, implies 36.3% total return

DCF is our primary valuation methodology as it takes into account Top Glove's strong cash flow generation, its net cash balance sheet and the defensive nature of its business. Our target price of RM16.50 is based on WACC of 9.98% (4.1% risk-free rate, 6.1% equity risk premium and two-year average beta of 0.8x). The terminal growth rate is based on our longer-term view that glove demand will be driven by both the overall population the aging population, which the UN projects to grow at 1.2% pa and 2.8% pa, respectively, over the next half-century. We initiate coverage on Top Glove with a Buy recommendation and, at our price target of RM16.50, the stock offers total potential return of 36.3% (33.7% share price potential upside and 2.6% dividend yield).

Figure 33: DCF valuation for Top Glove

(RMm)	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Revenue	2,161.9	2,497.2	2,750.9	3,053.5	3,389.4	3,762.2	4,138.5	4,552.3	5,007.5	5,508.3	6,059.1
Operating EBIT	329.3	385.5	431.7	488.6	508.4	564.3	620.8	682.8	751.1	826.2	908.9
Less: Cash tax	(80.1)	(93.7)	(104.9)	(122.1)	(127.1)	(141.1)	(155.2)	(170.7)	(187.8)	(206.6)	(227.2)
NOPLAT	249.3	291.8	326.8	366.4	381.3	423.3	465.6	512.1	563.3	619.7	681.6
Add: Depreciation	60.4	65.8	70.7	76.4	82.5	89.1	96.2	103.9	112.3	121.2	130.9
Less: Working capital	(78.8)	(87.4)	(96.3)	(106.9)	(118.6)	(131.7)	(144.8)	(159.3)	(175.3)	(192.8)	(212.1)
Less: Capex	(100.0)	(120.0)	(120.0)	(137.4)	(152.5)	(169.3)	(186.2)	(204.9)	(225.3)	(247.9)	(272.7)
Op Free Cash Flow	130.9	150.2	181.2	198.5	192.7	211.4	230.7	251.9	275.0	300.3	327.9

	RMm
Explicit forecast	1,467.9
Terminal Valuation	3,334.8
Add: Cash	277.7
Less: Debt	7.9
Total value of equity	5,088.3
Current no. of shares	308.4
Equity value per unit (RM/shr)	**16.50**

Source: Deutsche Bank

Premium valuations justified for a global market leader

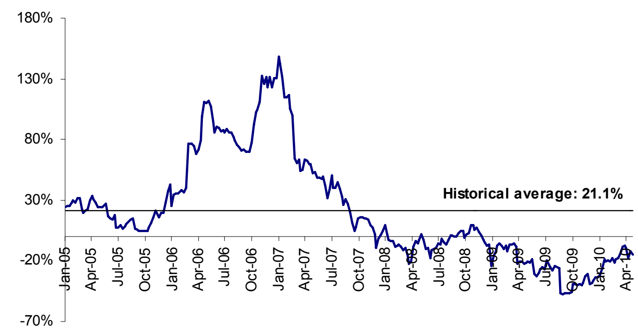
Top Glove is a global leader in a growth market. Our target price values Top Glove at 18.6x annualized FY10 PE or a 21% premium to the market PE of 15.4x. The stock has been trading at a five-year historical average premium of 21.1% to the Malaysian market. We believe that the premium valuation for Top Glove is justified given the company's higher-than-market earnings growth (EPS growth of 47% in FY10E vs. market's 29%) and strong balance sheet, (net cash vs. market's net gearing of 36%). The market has always implied a premium for quality companies such as Public Bank and KL Kepong in Malaysia and we believe that Top Glove, given its global leader position in a defensive industry should trade at such a premium.

Top Glove is currently trading at 15.1x FY10E PE. We are of view that the company's valuations are still attractive compared with the domestic market and global peers as well as considering its own growth prospects. The company is a market leader in an industry that is defensive in nature and continues to offer investors EPS growth of 12-47% in FY10-12E, sustainable ROEs above 25% and a decent dividend yield of 3%. We initiate coverage on Top

Glove with a Buy recommendation and expect a total return of 36.3% (33.7% share price upside and 2.6% dividend yield).

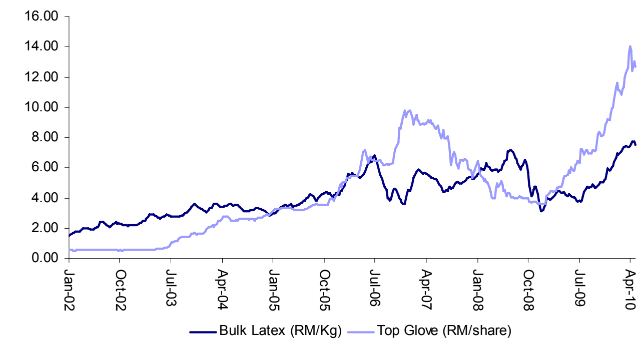
We expect the stock to be re-rated (near term) when the currently all-time-high bulk latex prices normalize once the winter season for the commodity ends in mid-May. On a longer-term view, consistently high earnings growth achieved by the company will provide further scope for valuation upside.

Figure 34: Top Glove's five-year average PE trades at a 25% premium to market



Source: Deutsche Bank. Bloomberg

Figure 35: Top Glove's share price movement is correlated to bulk latex prices



Source: Deutsche Bank, Bloomberg

Figure 36: Peer valuation

Deutsche Bank - Global Rubber Comps — As at 04-May-10

Company	BBerg	Year End	Rec	Currcy	Price (Local Currency)	TP (Local Currency)	Market Cap (Local Currency)	Market Cap (US$ m)	3M ADTV (US$ m)	EV/EBITDA (x)			P/E (x)			EPSg			P/BV (x)			Div Yield (%)			ROE (%)			Net Gearing (%)		
										2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E
MNC resellers																														
Kimberly-Clark	KMB US	31-Dec	Hold	USD	61.19	65.00	25,471	25,471.0	176.0	7.1	7.7	7.1	12.2	12.6	11.6	12.0	7.9	7.9	4.7	4.6	4.5	4.4	4.3	4.7	39.4	34.2	39.1	80.9	85.6	84.4
Beiersdorf	BEI GR	31-Dec	Buy	EUR	42.97	50.00	9,745	12,701.2	30.7	10.6	10.1	8.8	22.4	20.3	17.5	(22.9)	28.5	15.5	4.0	3.4	3.0	1.9	2.1	2.4	14.7	17.4	18.1	(26.1)	(30.1)	(34.8)
Cardinal Health	CAH US	30-Jun	Hold	USD	34.87	37.00	12,604	12,603.8	114.7	6.1	7.7	7.0	11.4	15.5	13.7	(34.5)	(9.8)	13.6	0.9	1.3	1.2	2.0	2.0	2.0	10.9	8.6	9.0	20.6	3.5	4.8
SSL International	SSL LN	31-Mar	Hold	GBP	852.50	825.00	1,800	2,720.3	701.3	9.3	13.2	12.4	16.6	25.5	21.8	34.3	22.0	16.9	3.1	5.4	4.6	2.0	1.2	1.2	27.8	23.6	23.2	6.1	2.1	19.6
MNC resellers								**13,374.1**	**255.7**	**8.3**	**10.3**	**9.4**	**16.8**	**20.4**	**17.7**	**(7.7)**	**13.6**	**15.3**	**2.7**	**3.3**	**2.9**	**1.9**	**1.8**	**1.9**	**17.8**	**16.6**	**16.8**	**0.2**	**(8.1)**	**(3.5)**
Rubber glove																														
Top Glove	TOPG MK	31-Dec	Buy	MYR	12.34	16.50	3,704	1,140	3.7	7.0	9.8	8.5	11.8	15.1	13.0	52.7	46.7	16.3	3.7	3.8	3.2	2.4	2.6	3.1	22.7	27.4	26.8	(19.5)	(27.0)	(32.3)
Ansell	ANN AU	30-Jun	Buy	USD	13.02	12.75	1,736	1,575	9.1	9.01	11.3	9.6	12.7	17.4	14.8	(5.9)	13.0	17.0	1.8	3.0	2.6	2.7	2.2	2.3	16.0	17.6	18.6	19.2	22.6	8.5
Semperit	SEM AV	31-Dec	Buy	EUR	30.48	37.00	627	807	1.0	3.18	5.2	4.7	10.7	15.0	13.3	3.2	8.0	12.7	1.8	1.9	1.8	5.7	4.3	4.8	12.9	13.1	13.9	(49.0)	(41.3)	(44.2)
Supermax	SUCB MK	31-Dec	Buy	MYR	6.66	9.00	1,761	542	5.7	3.50	8.0	6.3	14.1	9.7	8.1	173.0	41.7	19.7	2.3	2.6	2.1	1.4	2.4	2.8	26.6	29.5	28.2	31.5	23.7	16.5
Kossan	KRI MK	12/2009	NR	MYR	7.82	NA	1,247	384	1.2	10.08	7.5	6.3	16.7	10.9	9.0	NA	94.7	27.0	3.7	2.7	2.2	3.9	4.2	4.6	21.4	27.5	25.5	23.2	33.0	17.9
Hartalega	HART MK	31-Mar	NR	MYR	7.63	NA	1,844	568	0.6	17.40	9.9	8.4	24.5	13.7	11.6	87.9	79.4	17.8	0.4	5.0	3.7	1.3	2.3	2.7	33.3	38.4	33.5	-	(25.5)	(71.5)
Latexx Partners	LTX MK	12/2009	NR	MYR	3.70	NA	743	229	2.4	11.88	6.5	5.0	18.9	9.7	7.7	NA	69.4	38.2	-	-	-	1.0	1.7	2.3	35.9	46.5	40.4	-	-	-
Adventa	ADV MK	10/2009	NR	MYR	3.31	NA	487	150	1.6	15.58	9.3	6.8	18.8	11.1	8.0	NA	41.5	39.1	2.4	2.2	1.8	1.1	2.2	3.1	8.6	22.7	24.1	51.8	70.7	79.9
Malaysia Top 3 (41% Mkt share)								**689**	**3.6**	**6.9**	**8.4**	**7.0**	**14.2**	**11.9**	**10.0**	**112.9**	**61.0**	**21.0**	**3.2**	**3.0**	**2.5**	**2.6**	**3.1**	**3.5**	**23.6**	**28.1**	**26.8**	**11.7**	**9.9**	**0.7**
Malaysia (51% Mkt share)								**502**	**2.5**	**10.9**	**8.5**	**6.9**	**17.5**	**11.7**	**9.6**	**104.5**	**62.2**	**26.4**	**2.5**	**3.3**	**2.6**	**1.9**	**2.6**	**3.1**	**24.8**	**32.0**	**29.7**	**21.7**	**15.0**	**2.1**
Top 5 regional (62% Mkt share)								**890**	**4.1**	**6.6**	**8.4**	**7.1**	**13.2**	**13.6**	**11.6**	**55.7**	**40.8**	**18.6**	**2.6**	**2.8**	**2.4**	**3.2**	**3.1**	**3.5**	**19.9**	**23.0**	**22.6**	**1.1**	**2.2**	**(6.7)**
Rubber glove								**674**	**3.2**	**9.7**	**8.4**	**7.0**	**16.0**	**12.8**	**10.7**	**62.2**	**49.3**	**23.5**	**2.3**	**3.0**	**2.5**	**2.4**	**2.7**	**3.2**	**22.2**	**27.9**	**26.4**	**9.5**	**8.0**	**(3.6)**
Rubber products																														
Lanxess	LXS GR	31-Dec	Buy	EUR	35.50	38.00	2,953	3,849.1	27.1	6.7	6.8	5.5	16.3	12.7	9.5	(69.4)	143.9	33.8	1.5	1.9	1.6	2.7	2.1	2.8	2.8	14.0	18.3	54.9	57.1	47.0
Sumitomo Rubber	5110 JP	31-Dec	NR	JPY	844.00	NA	222,008	2,343.6	13.0	8.1	7.4	6.6	36.4	17.4	12.3	121.2	109.6	40.6	1.2	1.2	1.1	2.1	2.0	2.2	3.5	6.5	8.7	119.5	124.6	114.5
Yokohama Rubber	5101 JP	31-Mar	NR	JPY	441.00	NA	151,086	1,594.9	8.3	8.6	6.7	6.6	-	16.2	14.9	(124.6)	(261.6)	8.7	1.0	1.0	1.0	2.4	2.3	2.4	(4.7)	6.1	6.8	112.3	97.8	90.2
Tokai Rubber Ind	5191 JP	31-Dec	NR	JPY	1,154.00	NA	120,065	1,267.4	4.3	4.2	4.1	3.7	80.0	44.4	19.0	(90.1)	80.1	133.6	0.8	0.9	0.9	1.2	1.0	1.2	1.0	2.5	4.8	(4.6)	(12.9)	(19.8)
Sri Trang Agro	STA TB	12/2009	NR	THB	55.00	NA	11,000	339.9	3.1	12.8	20.2	18.9	9.5	15.9	16.9	108.1	(40.6)	(6.1)	1.7	1.5	1.4	3.1	1.8	1.8	19.2	9.1	8.9	-	-	-
Rubber products								**1,879.0**	**11.2**	**8.1**	**9.0**	**8.2**	**35.5**	**21.3**	**14.5**	**(11.0)**	**6.3**	**42.1**	**1.3**	**1.3**	**1.2**	**2.3**	**1.8**	**2.1**	**4.4**	**7.7**	**9.5**	**70.5**	**66.6**	**58.0**
DB global rubbber universe average									**90.0**	**8.7**	**9.3**	**8.2**	**22.8**	**18.2**	**14.3**	**14.5**	**23.0**	**27.0**	**2.1**	**2.5**	**2.2**	**2.2**	**2.1**	**2.4**	**14.8**	**17.4**	**17.5**	**26.8**	**22.2**	**17.0**

Source: Deutsche Bank estimates, Bloomberg
** Refers to Bloomberg consensus estimates*

Source: Deutsche Bank

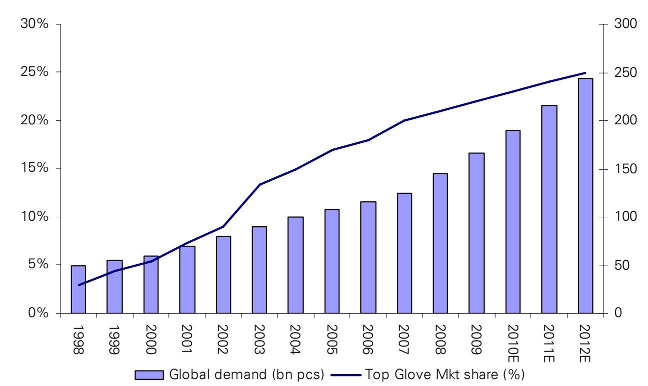
By far the market leader

Top Glove is extending its lead as the global leader

Wide distribution network. The key to Top Glove's success through the years has been its ability to not only expand market share but also, and more important, to control costs. While Top Glove is able to pass on raw material cost increases to clients, its ability to control other costs—fuel, labour and packaging—is key to sustaining long-term profitability and competitiveness in this global business. The company currently sells to 900 customers in 180 countries and no single customer accounts for more than 4% of its revenue.

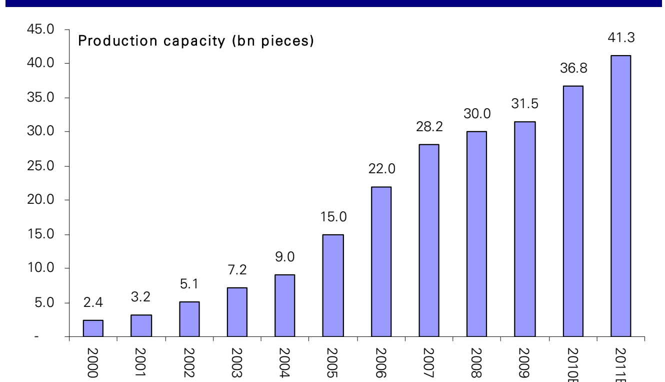
Increasing capacity. Through capacity expansion and sound market strategy, Top Glove has grown its global market share from c.3% in 1999 to 23% currently. We believe that the company will be able to extend its lead in the global glove industry. Global demand for gloves is currently at 145.3bn pieces and it is expected to grow at a compounded 13% pa based on our estimates. The key drivers for this growth are government healthcare reforms, still low usage for general healthcare protection and a growing aging population. The company is expected to expand its capacity by 12% and 17% in FY10E and FY11E, respectively, contributing an absolute 3.75bn pieces and 6bn pieces of gloves of new supply in the next two years. Top Glove offers six broad ranges of gloves. The bulk of these are made from natural rubber (85% of revenue) and the rest are made from synthetic rubber (nitrile) as well as Vinyl (at the China plant).

Figure 37: Top Glove has grown its market share from c.3% in 1999 to 23% currently



Source: Deutsche Bank, industry and company data

Figure 38: Expanding its capacity = growing market share

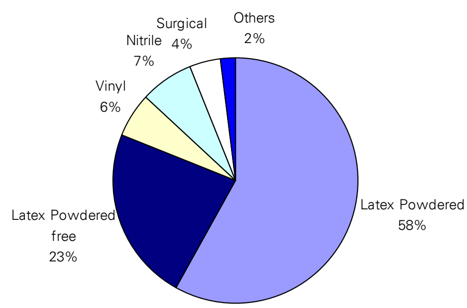


Source: Deutsche Bank, company data

Capturing market share in emerging markets

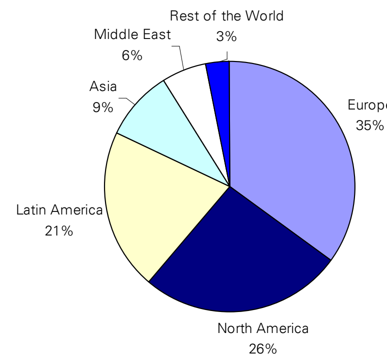
Top Glove's market positioning as the world largest producer of basic entry-level powdered latex gloves will allow it to capture growth in demand from emerging markets such as China and India where consumers are price sensitive and glove usage per capita averages about 3.0-4.0 pieces per year. This contrasts to developed markets such as the US and the EU where glove usage per capita averages 108 pieces per year. With its next closet competitor, Supermax, having only half its production capacity, we expect Top Glove to retain its dominant market leader position.

Figure 39: Revenue breakdown by product



Source: Deutsche Bank, company data

Figure 40: Revenue breakdown by geographical region



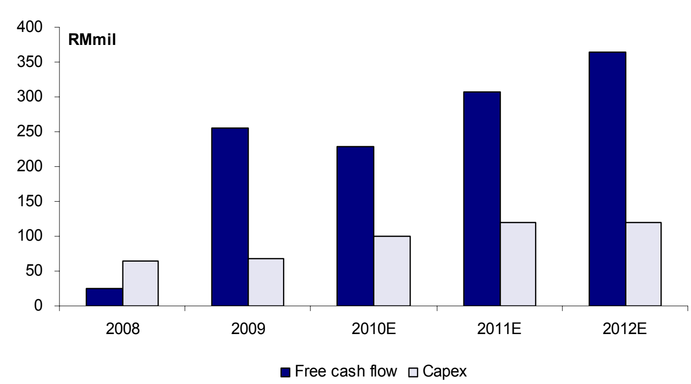
Source: Deutsche Bank, company data

Under-leveraged balance sheet

As of 2Q FY10, Top Glove had net cash of RM277.7m on its balance sheet. The company has managed to maintain its net cash position for the past five quarters through sound working capital management and strong cash flow generation from its business operations. We expect that annual free cash flow in access of RM200m will be more than sufficient to fund capex and debt obligations while at the same time allowing for increased dividends. Top Glove increased its target dividend payout from 30% of profit after tax to 40%, starting from 2009.

The glove industry has been consolidating over recent years, with many players shutting down owing to the lack of economies of scale, raising costs of operations and falling glove prices. Companies with sound balance sheets and strong working capital management such as Top Glove should be able to take advantage of potential acquisition opportunities. Top Glove previously indicated that it would like to invest in more upstream activities such as owning rubber plantations to ensure that it has constant supply of the raw material. We see the company's strategy of enhancing its operational capabilities as positive; the risk, however, would be the company overpaying for investments.

Figure 41: Top Glove free cash flow and capex. Net cash balance sheet in 2009



Source: Deutsche Bank, company data

Forecasts and earnings model

Three-year EPS CAGR of 25% from 2009-2012E

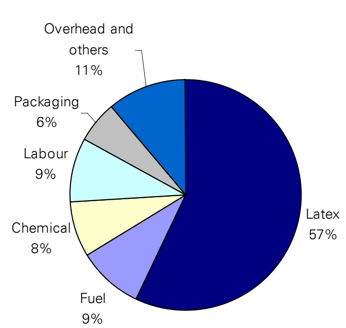
We expect Top Glove to deliver 25% EPS CAGR from 2009-12E, driven by strong industry demand growth of 13% pa, strong operating margins and sustainable cash flow. As Top Glove increases its capacity to cater to the increase in demand, we expect the company to be able to generate strong revenue growth of 10-41% in FY10-12E. We have assumed sustained operating margins of 15.7-16.0% over the forecast years even as we expect higher latex prices as we are of view that the company has pricing power to increase its selling prices as its input costs increase.

Figure 42: Key assumptions

	2008	2009	2010E	2011E	2012E
Installed capacity - Yr End (bn pcs)	30,000	31,500	35,250	41,250	44,550
% change	3%	5%	12%	17%	8%
Utilisation rate (%)	75.0	85.0	80.0	80.0	80.0
ASP (US$/1000 pcs)	23.10	20.50	24.73	25.22	25.73
% change	10%	-11%	21%	2%	2%
RM/US$	3.33	3.40	3.10	3.00	3.00
% change	-5%	2%	-9%	-3%	0%
Latex price (RM/kg)	5.68	4.51	5.90	6.08	6.26
% change	14%	-21%	31%	3%	3%

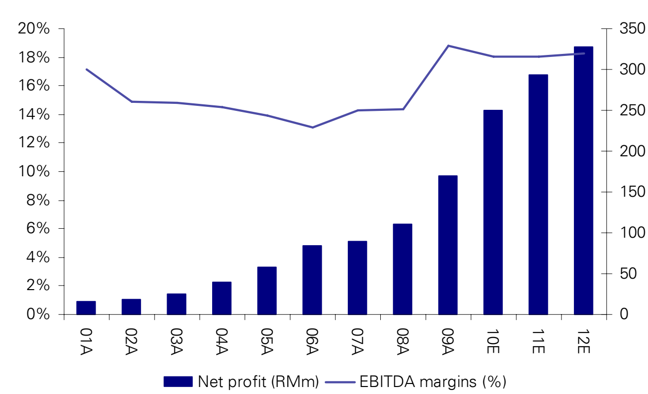
Source: Deutsche Bank estimates, company data

Figure 43: Costs breakdown (FY10E)



Source: Deutsche Bank

Figure 44: EBITDA margins and net earnings

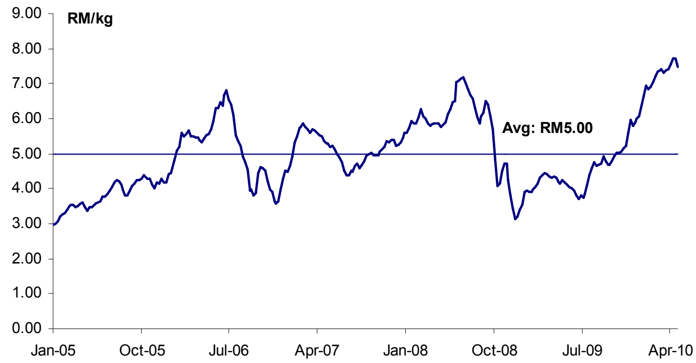


Source: Deutsche Bank, Bloomberg

Cost assumptions

The price of latex, which is a major cost component for Top Glove, has increased c.80% from a year ago and is c.63% higher YTD versus the 2009 average of RM4.68/kg. Rising demand globally, especially from the automotive sector, coupled with limited supply growth due to unfavourable weather conditions, lower yields from mature trees and progressive loss of tapped rubber areas, especially in Malaysia, owing to replanting with oil palms have led to this increase in prices. We expect bulk latex prices to stay above the five-year average of RM5.00/kg.

Figure 45: Bulk latex prices (RM/kg) – Prices to stay high



Source: Deutsche Bank, Bloomberg

While there is a forward market for latex, it is not an efficient hedging tool. Suppliers and traders who sell forward have been known to default when prices rise sharply, leading to production problems when inventories are low. Top Glove and other manufacturers in the industry usually buy the bulk of their requirements from established suppliers with track records. Latex prices quoted by these suppliers are usually based on the previous month's average market price for bulk latex.

We have assumed an average latex price of RM5.90/kg for 2010E and expect prices to increase 3% pa in 2011-12E. While the company is not able to control the rising latex cost, it has historically be able to pass through sustained costs increases (and reductions) to customers. The risk for earnings is when there is a sharp and volatile upward movement in prices. Margins during this period will be hurt until the price increase is pushed through.

Sensitivity analysis

Our sensitivity analysis suggests that every 1% change in latex costs will change our FY10E net earnings forecast by 3% and our DCF valuation by 0.5%. And every 1% change in USD/MYR will change our FY10E net earnings by 6.1% and DCF valuation by 1%.

Figure 46: Sensitivity to 1% change in costs

	Change in FY10E NP	Change in DCF valuations
Latex costs	3.0%	0.6%
MYR/US$	6.1%	1.3%
Total costs	5.4%	1.1%

Source: Deutsche Bank

Risks

Industry risks include: 1) industry over-expansion of capacity overhang; 2) sharp volatility in latex costs and foreign currencies, which results in a near-term margin squeeze; 3) political risks domestically and regionally (Glove manufacturers source about 50% of their raw material (natural rubber latex) from Thailand. The risk is shortage of NR latex supply and thus slow production output on the glove manufacturers' end.); and 4) infrastructure and labour shortages. Malaysia's natural gas supply to the glove industry has reached maximum capacity allocation and new allocations are only expected to come on stream in 2012. Delays in new allocation will limit capacity expansion for the manufactures and they may have to source alternative fuel that may be less efficient or cost more.

Company-risks include: 1) weaker-than-expected sales volume; 2) volatile raw materials and fuel costs, which are the two main costs for the company, may result in margin contraction or even losses for the company as there is a time lag in costs' pass-through; 3) stronger-than-expected MYR vs. the USD (Top Glove exports 95% of its output. Even thought there is a natural hedge given that some of its costs are in USD, a stronger MYR would imply slower revenue growth and translation losses); 4) execution risks from its aggressive capacity expansion plans. (The market is constantly concern about excess capacity from the industry given that most of the major players are expanding capacity in the next two years.); and 5) Over-paying for its acquisitions or investments. The company has indicated that, besides organic growth, it will need M&A to grow its global market share from 22% currently to 30% by 2012. Meanwhile, Top Glove is also looking to increase its upstream capability to include owning rubber plantations. The risk is the company overpaying for these investments in the pursuit of expanding its size and operational capabilities.

Company overview

The company and major shareholder

Top Glove is the world's largest rubber glove manufacturer with an estimated 23% global market share based on its existing production capacity of 33bn pieces of gloves. Incorporated in 1991, the group is listed on the main board of Bursa Malaysia. The company currently has 371 production lines in 20 factories located in Malaysia, Thailand and China. It also has two latex concentrate plants in Thailand with a combined capacity of 78,500 tonnes pa. Top Glove produces a diversified range of gloves catering to the medical, food and services, high technology and industrial markets; the gloves are predominantly sold to multinational original equipment manufacturer (OEM) resellers. The company exports 95% of its glove production across 180 countries. Eighty percent of the company's total glove sales are bound for the medical/healthcare industry with no single customer accounting for more than 5% of its sales. Its closest competitors include Safeskin Corp, a subsidiary of Kimberly Clark, Semperit Corp in Thailand and other Malaysian manufacturers, i.e. Supermax. Kossan Rubber, Latexx Partners and Adventa.

Management and shareholdings

Top Glove was set up in 1991 by Mr. Lim Wee Chai as a rubber glove trading company before setting up manufacturing operations in 1992. Mr. Lim was formerly a sales manager at OYL Industries (which was formerly owned by Hong Leong Group). Based on our visits to Top Glove's factory-cum-HQ in the outskirts of Klang, we believe much of the work and corporate culture of the OYL group has been incorporated at Top Glove. The offices are basic and operations ran smoothly and efficiently.

Figure 47: Management profile

	Prior experience
Tan Sri Dato Sri Lim, Wee-Chai **Chairman**	– Founder of the Top Glove Group of Companies, in 1991, with only three production lines – Awarded prestigious Master and Country Entrepreneur of Malaysia award for 2004 by EY – Served various directorial roles with the MARGMA, AMMI and Malaysian Rubber Board – Over 20 years' experience in the rubber and latex manufacturing industry – Obtained a BSc from University Malaya and an MBA from Sul Ross State University (Texas)
Lee Kim Meow **Managing Director**	– Joined Top Glove in 1997 as a General Manager and was re-designated as MD in April 2009 – Current President of the Malaysian Rubber Glove Manufacturers' Association (MARGMA) – Has more than 12 years of experience in marketing of financial services and credit control operations through prior employment
Lim Hooi Sin **Executive Director**	– Spent 14 years with MetLife Financial Services - one of the largest insurance & financial services companies in the US – Founder of TG Medical US, Inc. in 1994 and has vast experience in the US glove market – A resident of the United States where he obtained a BSc from Oklahoma State University and an MBA from Arizona State University
Lim Chong Guan **Executive Director**	– Responsible for the accounting, treasury, corporate finance and investor relations at Top Glove – Began his career with PWC and subsequently held various key positions at a number of publicly-listed companies – A director of the Malaysian Investor Relations Association Bhd

Source: Company Data

The founder and chairman hold approximately 38.9% of shares outstanding and about 61.1% of the shares are free floating. 35% of the shares are held by foreign shareholders currently and the rest domestic. Among institutions, the leading holders are Matthews International Capital Management (5.4%) and Overlook Partners (6.7%) with a total of 12.1% shares. The average daily volume traded over the past three months on the stock was 1.2m shares or just over US$3.7m per day.

Asia ASEAN Malaysia

Industrials Manufacturing

6 May 2010

Supermax Corporation

Reuters: **SUPM.KL** Bloomberg: **SUCB MK**

A strong number two; initiate with Buy

A strong number two player

Supermax is the world's second largest disposable glove manufacturer with c.11% of the global market share. Its differentiated business strategy of having its own distribution centres in its major exports market and own-brand gloves that make it the second largest supplier to the US dental market should allow it to enjoy better margins. Due to a backlog of orders, the company plans to expand capacity by c.50% over the next two years to grow revenues. We initiate coverage with a DCF-derived target of RM9.00/share. Buy on 37.5% upside potential.

Improving balance sheet, cash flow sufficient to fund expansion plans

We expect the company to generate three-year NP CAGR of 27.4% on the back of sustained margins and 13% p.a. compounded growth in global glove demand. Its balance sheet, with 0.3x (FY09) net gearing, is expected to improve as the company generates strong cash flow over FY10-12E. The company's annual free cash flow in excess of RM120m p.a. should be more than sufficient to fund its capex and repay its debt obligations, while also allowing for higher dividend payments. Supermax currently has a dividend payout of c. 23%.

Differentiated business strategy

Supermax differentiates itself by growing its downstream capabilities by 1) setting up its own distribution centre in its major exports market and 2) growing awareness of its own branded glove which should allow the company to enjoy both manufacturing and distribution profits. It is currently the second largest supplier of its own 'Supermax' brand gloves to the US dental market.

DCF-based target price of RM9.00/share; latex price hikes a risk

Our DCF-derived target price of RM9.00/share is based on an 11.6% WACC. This values the company at 12.3x forward FY10E PE or at a 34% discount to Top Glove's implied PE target of 18.6x. Historically, Supermax's five-year PE valuations have traded at a 37% discount to Top Glove's. We are of the view that its current valuations are undemanding and its above-market earnings growth in a defensive market is attractive and supports our Buy. Key downside risks include 1) excess capacity in the industry, 2) sharp increases in latex prices, and 3) US$ weakness

Forecasts and ratios

Year End Dec 31	2008A	2009A	2010E	2011E	2012E
Sales (MYRm)	811.8	814.8	**1,151.2**	1,418.2	1,739.6
EBITDA (MYRm)	98.9	205.9	**219.4**	264.4	321.9
Reported NPAT (MYRm)	47.0	129.8	**186.0**	222.6	268.3
Reported EPS FD(MYR)	0.18	0.48	**0.69**	0.82	0.99
DB EPS growth (%)	-16.0	173.0	**41.7**	19.7	20.5
PER (x)	7.8	4.4	**9.3**	7.8	6.4
EV/EBITDA (x)	6.7	3.5	**7.6**	6.0	4.5
DPS (net) (MYR)	0.03	0.11	**0.16**	0.19	0.23
Yield (net) (%)	2.3	5.1	**2.5**	3.0	3.6

Source: Deutsche Bank estimates, company data

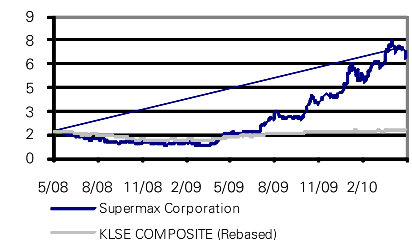
[1] DB EPS is fully diluted and excludes non-recurring items

[2] Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close

Buy

Price at 6 May 2010 (MYR)	**6.36**
Price target - 12mth (MYR)	**9.00**
52-week range (MYR)	**7.45 - 1.51**
KLSE COMPOSITE	**1,332**

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-11.0	26.7	310.3
KLSE COMPOSITE	-0.9	6.7	30.1

Stock data

Market cap (MYRm)	**1,726**
Market cap (USDm)	**534**
Shares outstanding (m)	**269.8**
Major shareholders	**Dato' Seri Stanley Tai (20.4%)**
Free float (%)	**60**
Avg daily value traded (USDm)	**5.7**

Key indicators (FY1)

ROE (%)	**29.5**
Net debt/equity (%)	**23.7**
Book value/share (MYR)	**2.59**
Price/book (x)	**2.5**
Net interest cover (x)	**11.8**
Operating profit margin (%)	**16.4**

Model updated:05 May 2010

Running the numbers

Asia

ASEAN Malaysia

Manufacturing

Supermax Corporation Berhad

Reuters: SUPM.KL Bloomberg: SUCB MK

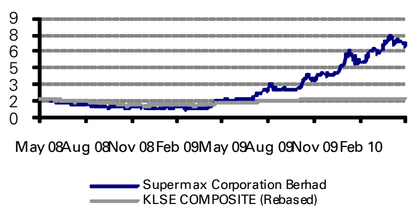
Buy

Price (6 May 10)	MYR 6.36
Target price	MYR 9.00
52-week Range	MYR 1.51 - 7.45
Market Cap (m)	MYRm 1,726 USDm 534

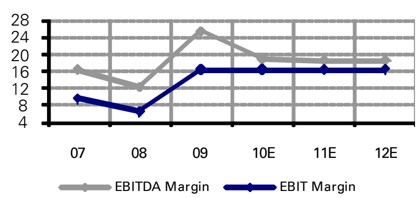
Company Profile

Supermax is currently the world's second-largest glove manufacturer for disposable rubber gloves with an estimated 10% global market share. Supermax produces a diversified range of gloves catering to the medical, dental, bio-tech, industrial and food & services industries.

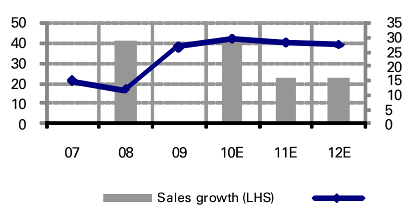
Price Performance



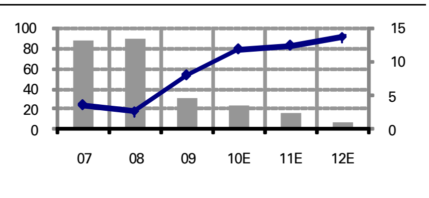
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec	2007	2008	2009	2010E	2011E	2012E
Financial Summary						
DB EPS (MYR)	0.21	0.18	0.48	0.69	0.82	0.99
Reported EPS (MYR)	0.21	0.18	0.48	0.69	0.82	0.99
DPS (MYR)	0.03	0.03	0.11	0.16	0.19	0.23
BVPS (MYR)	1.4	1.6	2.1	2.6	3.2	4.0
Weighted average shares (m)	265	265	267	270	271	271
Average market cap (MYRm)	606	366	574	1,726	1,726	1,726
Enterprise value (MYRm)	880	660	717	1,670	1,597	1,464
Valuation Metrics						
P/E (DB) (x)	10.8	7.8	4.4	9.3	7.8	6.4
P/E (Reported) (x)	10.8	7.8	4.4	9.3	7.8	6.4
P/BV (x)	1.51	0.51	2.27	2.46	1.97	1.60
FCF Yield (%)	6.6	16.3	37.2	7.5	9.6	14.0
Dividend Yield (%)	1.4	2.3	5.1	2.5	3.0	3.6
EV/Sales (x)	1.5	0.8	0.9	1.5	1.1	0.8
EV/EBITDA (x)	9.4	6.7	3.5	7.6	6.0	4.5
EV/EBIT (x)	16.0	12.4	5.4	8.8	6.9	5.1
Income Statement (MYRm)						
Sales revenue	**574**	**812**	**815**	**1,151**	**1,418**	**1,740**
Gross profit	**93**	**99**	**206**	**219**	**264**	**322**
EBITDA	**93**	**99**	**206**	**219**	**264**	**322**
Depreciation	38	46	73	31	32	36
Amortisation	0	0	0	0	0	0
EBIT	**55**	**53**	**132**	**189**	**232**	**286**
Net interest income(expense)	-15	-20	-17	-16	-19	-21
Associates/affiliates	18	19	42	46	48	51
Exceptionals/extraordinaries	0	0	-5	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0	0
Profit before tax	**59**	**52**	**152**	**219**	**262**	**316**
Income tax expense	3	5	22	33	39	47
Minorities	0	0	0	0	0	0
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	**56**	**47**	**130**	**186**	**223**	**268**
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	**56**	**47**	**130**	**186**	**223**	**268**
Cash Flow (MYRm)						
Cash flow from operations	**74**	**98**	**236**	**179**	**245**	**292**
Net Capex	-34	-39	-23	-50	-80	-50
Free cash flow	**40**	**60**	**213**	**129**	**165**	**242**
Equity raised/(bought back)	5	-6	27	0	0	0
Dividends paid	-7	-9	-19	-43	-51	-62
Net inc/(dec) in borrowings	-14	-16	-101	-46	-7	-16
Other investing/financing cash flows	-20	-28	-33	-19	-32	-48
Net cash flow	**3**	**2**	**88**	**22**	**75**	**116**
Change in working capital	*-2*	*3*	*85*	*-53*	*-28*	*-34*
Balance Sheet (MYRm)						
Cash and other liquid assets	29	31	119	141	215	331
Tangible fixed assets	373	383	379	402	450	464
Goodwill/intangible assets	40	35	35	35	35	35
Associates/investments	101	121	155	223	273	335
Other assets	325	376	246	338	418	513
Total assets	**869**	**947**	**934**	**1,139**	**1,392**	**1,678**
Interest bearing debt	366	406	295	307	359	404
Other liabilities	118	125	82	129	158	193
Total liabilities	**485**	**530**	**376**	**436**	**518**	**597**
Shareholders' equity	384	416	558	703	874	1,081
Minorities	0	0	0	0	0	0
Total shareholders' equity	**384**	**416**	**558**	**703**	**874**	**1,081**
Net debt	*337*	*375*	*176*	*166*	*144*	*72*
Key Company Metrics						
Sales growth (%)	nm	41.4	0.4	41.3	23.2	22.7
DB EPS growth (%)	na	-16.0	173.0	41.7	19.7	20.5
EBITDA Margin (%)	16.2	12.2	25.3	19.1	18.6	18.5
EBIT Margin (%)	9.6	6.6	16.3	16.4	16.4	16.4
Payout ratio (%)	15.4	18.0	22.7	22.9	23.0	23.0
ROE (%)	14.6	11.7	26.6	29.5	28.2	27.4
Capex/sales (%)	5.9	4.7	2.8	4.3	5.6	2.9
Capex/depreciation (x)	0.9	0.8	0.3	1.6	2.5	1.4
Net debt/equity (%)	87.9	90.0	31.5	23.7	16.5	6.7
Net interest cover (x)	3.6	2.6	7.9	11.8	12.4	13.6

Source: Company data, Deutsche Bank estimates

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Investment thesis

Outlook

Supermax is currently the second largest glove manufacturer in the world with c.11% market share of the global disposable glove market. Given the backlog in glove delivery, we expect the company to grow its revenue in the next two years through capacity expansion. Supermax is looking to add 3.1bn and 4.1bn pieces of new gloves to its supply p.a. in the next two years, respectively, which would boost its total capacity by c.50% to 21.7bn pieces of gloves by end-2011E. Supermax's differentiated business strategy of growing its downstream capabilities by 1) setting up its own distribution operations in the major countries to which it exports and 2) growing awareness of its own branded gloves could bring further margin improvements as it benefits from manufacturing sales and earnings contribution from its distribution operations.

The stock is the most liquid among all the listed rubber gloves stocks and currently sees an average three-month daily value traded of US$5.8m. We find its current valuation of 9.7x FY10E PE and 8.1x FY11E PE attractive versus its peers' 14.3x FY10E PE and its own historical average PE of 8.4x. We expect Supermax to generate three-year net earnings CAGR of 27.4%

Valuation

We use DCF as our primary valuation methodology for Supermax to take into account its strong cash flow generation and low gearing balance sheet of 0.3x (as at FY09). Our target price of RM9.00/share is based on a WACC of 11.6% (4.1% risk-free rate, 6.1% average equity risk premium and two-year average beta of 1.1x). We initiate on Supermax with a Buy recommendation; at our price target, we expect the stock to generate a total return of 37.5% (35.1% share price upside and 2.4% dividend yield).

Our price target values the company at 12.3x forward-rolling PE (May10-Apr-11E) or at a 34% discount to Top Glove's implied PE target of 18.6x on forward-rolling EPS (May 2010-April 2011E). Historically, Supermax's five-year PE valuations have traded at a 37% discount to Top Glove's. We believe that the discount is justified as the market needs to take into account risks on small cap stocks and that Supermax is c.50% the size of Top Glove in terms of production capacity, market share of the global glove industry and market capitalization.

Risks

Key risks include 1) excess production capacity going into 2H10 as glove manufacturers have embarked on an aggressive capacity expansion, 2) volatile raw material costs and currency fluctuations which would impact margins, and 3) a slowdown in global demand for gloves as concerns over the threat of the H1N1 influenza subsides.

Valuation

DCF-based target price of RM9.00, implies 35.9% total return

DCF is our primary valuation methodology for Supermax as it allows us to take into account the company's strong cash flow generation and low gearing balance sheet of 0.3x (as at FY09). Our target price of RM9.00/share is based on a WACC of 11.6% (4.1% risk-free rate, 6.1% equity risk premium and two-year average beta of 1.1x). We have assumed a terminal growth rate of 5% based on our longer term view that glove demand will be driven by secular growth such as population and aging population growth which the UN expects to grow at 1.2% and 2.8%, respectively, over the next half-century. We initiate on Supermax with a Buy recommendation and at our price target, we expect the stock to generate a total return of 35.9% (33.5% share price upside and 2.4% dividend yield).

Figure 48: Supermax DCF valuation

(RMm)	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Revenue	**1,151.2**	**1,418.2**	**1,739.6**	**1,913.6**	**2,105.0**	**2,315.5**	**2,547.0**	**2,750.8**	**2,970.8**	**3,208.5**	**3,465.2**
Operating EBIT	188.8	232.2	285.9	306.2	336.8	370.5	407.5	440.1	475.3	513.4	554.4
Less: Cash tax	(32.8)	(39.3)	(47.3)	(45.9)	(50.5)	(55.6)	(81.5)	(88.0)	(95.1)	(102.7)	(110.9)
NOPLAT	**155.9**	**192.9**	**238.5**	**260.3**	**286.3**	**314.9**	**326.0**	**352.1**	**380.3**	**410.7**	**443.5**
Add: Depreciation	30.6	32.2	36.0	38.9	42.0	45.3	49.0	52.9	57.1	61.7	66.6
Less: Working capital	(53.1)	(28.3)	(33.7)	(57.4)	(63.1)	(69.5)	(76.4)	(82.5)	(89.1)	(96.3)	(104.0)
Less: Capex	(50.0)	(80.0)	(50.0)	(95.7)	(105.2)	(115.8)	(127.4)	(137.5)	(148.5)	(160.4)	(173.3)
Op Free Cash Flow	**83.5**	**116.8**	**190.8**	**146.0**	**159.9**	**175.0**	**171.2**	**184.9**	**199.7**	**215.7**	**233.0**

	RMm
Explicit forecast	1,068.2
Terminal Valuation	1,565.4
Add: Cash	106.0
Less: Debt	295.8
Total value of equity	2,443.9
Current no. of shares	271.4
Equity value per unit (RM/share)	**9.00**

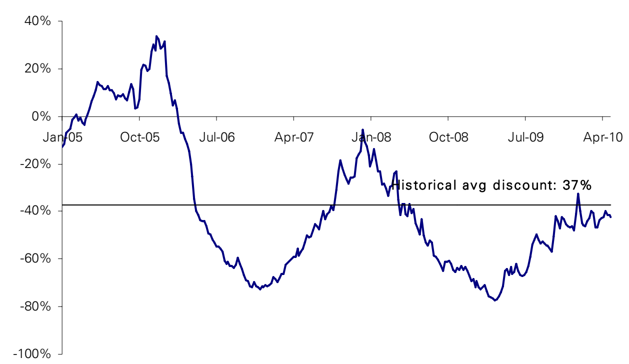
Source: Deutsche Bank estimates

Valuations at a discount to the global leader

Our price target values the company at 12.3x forward-rolling PE (May 2010-April 2011E) or at a 34% discount to Top Glove's implied PE target of 18.6x on forward-rolling EPS (May 2010-April 2011E). Historically, Supermax's five-year PE valuations have traded at a 37% discount to Top Glove's. We believe that the discount is justified as the market needs to take into account risks on small cap stocks and that Supermax is c.50% the size of Top Glove in terms of production capacity, market share of the global glove industry and market capitalization.

Currently trading at 9.7x FY10E PE and 8.1x FY11E PE, valuation for the stock is undemanding compared to its peers and its historical average of 8.4x PE. We expect Supermax to generate three-year net earnings CAGR of 27.4% and believe that its differentiated business model, strong earnings growth in a defensive market, above-market ROEs and relatively strong balance sheet are attractive. We see further scope for a re-rating of the stock as the company continues to generate strong earnings growth over the quarters. Meanwhile short-term catalysts for a share price rally include the easing of latex prices and news on new H1N1 outbreaks.

Figure 49: Historically, Supermax has traded at a 37% discount to Top Glove's PE valuations



Source: Deutsche Bank, Bloomberg

Figure 50: Supermax P/E band

Source: Deutsche Bank, Bloomberg

Figure 51: Peer valuation

Deutsche Bank - Global Rubber Comps — As at 04-May-10

Company	BBerg	Year End	Rec	Currcy	Price (Local Currency)	TP (Local Currency)	Market Cap	Market Cap (US$ m)	3M ADTV (US$ m)	EV/EBITDA (x) 2009E	EV/EBITDA (x) 2010E	EV/EBITDA (x) 2011E	P/E (x) 2009E	P/E (x) 2010E	P/E (x) 2011E	EPSg 2009E	EPSg 2010E	EPSg 2011E	P/BV (x) 2009E	P/BV (x) 2010E	P/BV (x) 2011E	Div Yield (%) 2009E	Div Yield (%) 2010E	Div Yield (%) 2011E	ROE (%) 2009E	ROE (%) 2010E	ROE (%) 2011E	Net Gearing (%) 2009E	Net Gearing (%) 2010E	Net Gearing (%) 2011E
MNC resellers																														
Kimberly-Clark	KMB US	31-Dec	Hold	USD	61.19	65.00	25,471	25,471.0	176.0	7.1	7.7	7.1	12.2	12.6	11.6	12.0	7.9	7.9	4.7	4.6	4.5	4.4	4.3	4.7	39.4	34.2	39.1	80.9	85.6	84.4
Beiersdorf	BEI GR	31-Dec	Buy	EUR	42.97	50.00	9,745	12,701.2	30.7	10.6	10.1	8.8	22.4	20.3	17.5	(22.9)	28.5	15.5	4.0	3.4	3.0	1.9	2.1	2.4	14.7	17.4	18.1	(26.1)	(30.1)	(34.8)
Cardinal Health	CAH US	30-Jun	Hold	USD	34.87	37.00	12,604	12,603.8	114.7	6.1	7.7	7.0	11.4	15.5	13.7	(34.5)	(9.8)	13.6	0.9	1.3	1.2	2.0	2.0	2.0	10.9	8.6	9.0	20.6	3.5	4.8
SSL International	SSL LN	31-Mar	Hold	GBP	852.50	825.00	1,800	2,720.3	701.3	9.3	13.2	12.4	16.6	25.5	21.8	34.3	22.0	16.9	3.1	5.4	4.6	2.0	1.2	1.2	27.8	23.6	23.2	6.1	2.1	19.6
MNC resellers								**13,374.1**	**255.7**	**8.3**	**10.3**	**9.4**	**16.8**	**20.4**	**17.7**	**(7.7)**	**13.6**	**15.3**	**2.7**	**3.3**	**2.9**	**1.9**	**1.8**	**1.9**	**17.8**	**16.6**	**16.8**	**0.2**	**(8.1)**	**(3.5)**
Rubber glove																														
Top Glove	TOPG MK	31-Dec	Buy	MYR	12.34	16.50	3,704	1,140	3.7	7.0	9.8	8.5	11.8	15.1	13.0	52.7	46.7	16.3	3.7	3.8	3.2	2.4	2.6	3.1	22.7	27.4	26.8	(19.5)	(27.0)	(32.3)
Ansell	ANN AU	30-Jun	Buy	USD	13.02	12.75	1,736	1,575	9.1	9.01	11.3	9.6	12.7	17.4	14.8	(5.9)	13.0	17.0	1.8	3.0	2.6	2.7	2.2	2.3	16.0	17.6	18.6	19.2	22.6	8.5
Semperit	SEM AV	31-Dec	Buy	EUR	30.48	37.00	627	807	1.0	3.18	5.2	4.7	10.7	15.0	13.3	3.2	8.0	12.7	1.8	1.9	1.8	5.7	4.3	4.8	12.9	13.1	13.9	(49.0)	(41.3)	(44.2)
Supermax	SUCB MK	31-Dec	Buy	MYR	6.66	9.00	1,761	542	5.7	3.50	8.0	6.3	14.1	9.7	8.1	173.0	41.7	19.7	2.3	2.6	2.1	1.4	2.4	2.8	26.6	29.5	28.2	31.5	23.7	16.5
Kossan	KRI MK	12/2009	NR	MYR	7.82	NA	1,247	384	1.2	10.08	7.5	6.3	16.7	10.9	9.0	NA	94.7	27.0	3.7	2.7	2.2	3.9	4.2	4.6	21.4	27.5	25.5	23.2	33.0	17.9
Hartalega	HART MK	31-Mar	NR	MYR	7.63	NA	1,844	568	0.6	17.40	9.9	8.4	24.5	13.7	11.6	87.9	79.4	17.8	0.4	5.0	3.7	1.3	2.3	2.7	33.3	38.4	33.5	-	(25.5)	(71.5)
Latexx Partners	LTX MK	12/2009	NR	MYR	3.70	NA	743	229	2.4	11.88	6.5	5.0	18.9	9.7	7.7	NA	69.4	38.2	-	-	-	1.0	1.7	2.3	35.9	46.5	40.4	-	-	-
Adventa	ADV MK	10/2009	NR	MYR	3.31	NA	487	150	1.6	15.58	9.3	6.8	18.8	11.1	8.0	NA	41.5	39.1	2.4	2.2	1.8	1.1	2.2	3.1	8.6	22.7	24.1	51.8	70.7	79.9
Malaysia Top 3 (41% Mkt share)								**689**	**3.6**	**6.9**	**8.4**	**7.0**	**14.2**	**11.9**	**10.0**	**112.9**	**61.0**	**21.0**	**3.2**	**3.0**	**2.5**	**2.6**	**3.1**	**3.5**	**23.6**	**28.1**	**26.8**	**11.7**	**9.9**	**0.7**
Malaysia (51% Mkt share)								**502**	**2.5**	**10.9**	**8.5**	**6.9**	**17.5**	**11.7**	**9.6**	**104.5**	**62.2**	**26.4**	**2.5**	**3.3**	**2.6**	**1.9**	**2.6**	**3.1**	**24.8**	**32.0**	**29.7**	**21.7**	**15.0**	**2.1**
Top 5 regional (62% Mkt share)								**890**	**4.1**	**6.6**	**8.4**	**7.1**	**13.2**	**13.6**	**11.6**	**55.7**	**40.8**	**18.6**	**2.6**	**2.8**	**2.4**	**3.2**	**3.1**	**3.5**	**19.9**	**23.0**	**22.6**	**1.1**	**2.2**	**(6.7)**
Rubber glove								**674**	**3.2**	**9.7**	**8.4**	**7.0**	**16.0**	**12.8**	**10.7**	**62.2**	**49.3**	**23.5**	**2.3**	**3.0**	**2.5**	**2.4**	**2.7**	**3.2**	**22.2**	**27.9**	**26.4**	**9.5**	**8.0**	**(3.6)**
Rubber products																														
Lanxess	LXS GR	31-Dec	Buy	EUR	35.50	38.00	2,953	3,849.1	27.1	6.7	6.8	5.5	16.3	12.7	9.5	(69.4)	143.9	33.8	1.5	1.9	1.6	2.7	2.1	2.8	2.8	14.0	18.3	54.9	57.1	47.0
Sumitomo Rubber	5110 JP	31-Dec	NR	JPY	844.00	NA	222,008	2,343.6	13.0	8.1	7.4	6.6	36.4	17.4	12.3	121.2	109.6	40.6	1.2	1.2	1.1	2.1	2.0	2.2	3.5	6.5	8.7	119.5	124.6	114.5
Yokohama Rubber	5101 JP	31-Mar	NR	JPY	441.00	NA	151,086	1,594.9	8.3	8.6	6.7	6.6	-	16.2	14.9	(124.6)	(261.6)	8.7	1.0	1.0	1.0	2.4	2.3	2.4	(4.7)	6.1	6.8	112.3	97.8	90.2
Tokai Rubber Ind	5191 JP	31-Dec	NR	JPY	1,154.00	NA	120,065	1,267.4	4.3	4.2	4.1	3.7	80.0	44.4	19.0	(90.1)	80.1	133.6	0.8	0.9	0.9	1.2	1.0	1.2	1.0	2.5	4.8	(4.6)	(12.9)	(19.8)
Sri Trang Agro	STA TB	12/2009	NR	THB	55.00	NA	11,000	339.9	3.1	12.8	20.2	18.9	9.5	15.9	16.9	108.1	(40.6)	(6.1)	1.7	1.5	1.4	3.1	1.8	1.8	19.2	9.1	8.9	-	-	-
Rubber products								**1,879.0**	**11.2**	**8.1**	**9.0**	**8.2**	**35.5**	**21.3**	**14.5**	**(11.0)**	**6.3**	**42.1**	**1.3**	**1.3**	**1.2**	**2.3**	**1.8**	**2.1**	**4.4**	**7.7**	**9.5**	**70.5**	**66.6**	**58.0**
DB global rubbber universe average									**90.0**	**8.7**	**9.3**	**8.2**	**22.8**	**18.2**	**14.3**	**14.5**	**23.0**	**27.0**	**2.1**	**2.5**	**2.2**	**2.2**	**2.1**	**2.4**	**14.8**	**17.4**	**17.5**	**26.8**	**22.2**	**17.0**

Source: Deutsche Bank estimates, Bloomberg
** Refers to Bloomberg consensus estimates*

Source: Deutsche Bank, Bloomberg

Investment bullets

A strong challenger

Supermax is currently the second largest glove manufacturer in the world with c.10% market share of the 145.3bn-piece global disposable glove market. We expect global glove demand to grow at a compounded rate of 13% p.a. Supermax maintains that the demand for its gloves continues to be strong. In 1Q10, the company had back orders of 4.9bn pieces of gloves in which it will likely need another two quarters to clear due to the lack of spare capacity at its factories. Although the company has seen customers deferring their orders to the later part of the year on expectations that the recent increase in selling prices will normalize towards 2H10 as latex prices ease, demand has exceeded the company's supply.

Figure 52: Back orders suggest sustainability of demand going into 2H10

	2008			2009			2010	
Orders received		1Q09	2Q09	3Q09	4Q09	Total	1Q10	Total
From Supermax & Seal Polymer's customer	13,500	3,050	4,000	4,000	3,800	14,850	7,540	7,540
From APLI's clients	2,640	330	330	330	330	1,320	330	330
H1N1 orders	-	-	450	330	300	1,050	200	200
Total orders received	16,140	3,810	4,630	4,630	4,430	17,500	8,070	8,070
Total shipped	12,765	2,995	3,015	3,130	2,975	12,115	3,205	3,205
Back orders	**3,375**	**815**	**1,615**	**1,500**	**1,455**	**5,385**	**4,865**	**4,865**
*Back orders % of total shipped	26%	27%	54%	48%	49%	44%	152%	152%

Source: Company data

The company has a total of nine factories located in Malaysia with total production capacity of 14.7bn pieces of gloves currently.

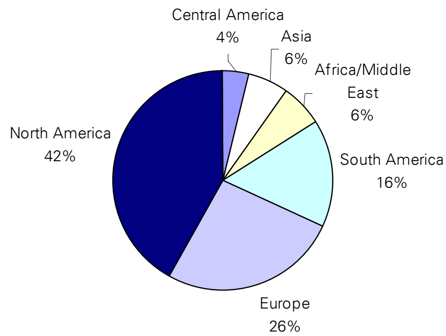
Given the backlog in glove delivery, we expect the company to grow its revenue in the next two years through capacity expansion. Supermax has earmarked RM130m to expand its production capacity by 21% and 23% in FY10E and FY11E respectively or an annual 3.1bn and 4.1bn pieces of new glove supply over the next two years. This would boost its total capacity by c.50% to 21.7bn pieces of gloves by end-2011E. The company is also undertaking refurbishment works on its older plants to improve overall efficiency of its production lines.

Over a longer term, Supermax intends to build a 'Glove City' on a 36.8-acre plot of land in Bukit Kapar, Klang. Phase 1 construction of the project will commence in 2011 and is part of the company's 4.1bn new capacity expansion plan. We expect Supermax to develop Glove City over a period of 10 years and require capex of RM40-50m/factory. Upon completion, Glove City will be able accommodate six factories and provide a total production capacity of 18bn pieces of gloves annually. While the company have intended for its Glove City project to stretch over a 10-year period, it is able to fast track the project in the event that the demand for gloves is stronger than expected.

Differentiated business strategy

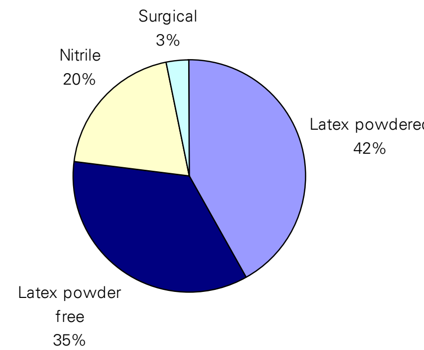
Supermax currently derives 42% of its revenues from sales to the US. It has a 100%-owned glove distribution company "Supermax Inc" which contributed 12.9% of the company's FY09 net earnings. Unlike its competitor, Top Glove, who has invested in upstream capabilities through two latex concentrate plants in Thailand, Supermax has chosen to grow its downstream capabilities by 1) setting up its own distribution operations in the major countries to which it exports its products and 2) growing awareness on its own branded gloves.

Figure 53: Sales by region



Source: Deutsche Bank, company

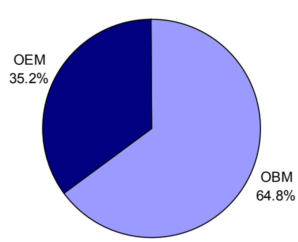
Figure 54: Product mix



Source: Deutsche Bank, company

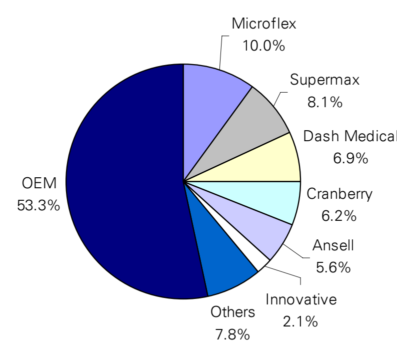
Supermax entered the US market with its own brand of products in 2000. Over the years, its OBM gloves products have gained significant market share of targeted sub-sectors. As reported by Strategic Dental Marketing, Supermax's market share of the US Dental market (which has a market size of US$650m/year in 2008) has grown from 2.5% (5^{th} place) in 2005 to 8.1% (2^{nd} place) in 4Q09 ahead of the larger MNCs suppliers such as Ansell and Dash Medical. The company is targeting for its OBM business to contribute 70% of revenues by 2011E from the current split of 65-35 (OBM-OEM). Looking ahead, we believe that Supermax could see further margin improvements as it benefits from manufacturing sales and earnings contribution from its distribution operations.

Figure 55: Currently at 64.8% and growing to 70% by end-FY11E



Source: Deutsche Bank, company

Figure 56: Market share of Supermax branded gloves in the US dental market

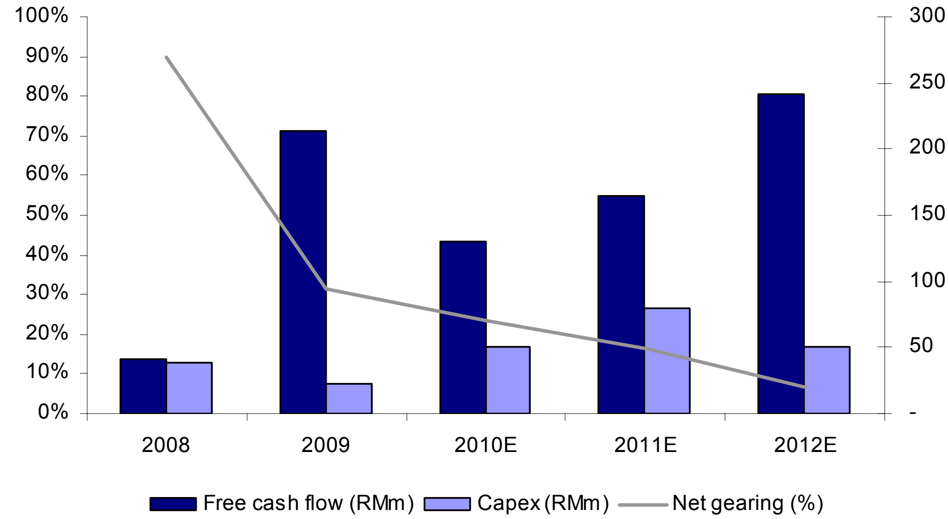


Source: Deutsche Bank, company

Fundamentally sound balance sheet

Having fully written down its investment into APLI in 2008 and generated strong earnings growth in 2009, Supermax has seen an improvement in its balance sheet position. Net gearing has declined from 0.9x in 2008 to 0.3x in 2009. We expect the company's balance sheet strength to improve going forward and net gearing levels to decline from 0.3x in 2009 to 0.07x in FY12E on sustained earnings growth momentum and better cash flow management. Despite Supermax's aggressive expansion plans, we do not expect Supermax to require capital injections going forward. The company's annual free cash flow in excess of RM120m p.a. will be more than sufficient to fund its capex and repay its debt obligations, while at the same time allow for higher dividend payments.

Figure 57: Strong cash flow generation will see strength in its balance sheet



Source: Deutsche Bank, company data

Forecast and earnings model

Three-year net earnings CAGR of 27.4% from 2009-2012E

Earnings drivers: We expect Supermax to deliver a three-year net earnings CAGR of 27.4% from 2009-2012E driven by the company's capacity expansion of 21.5% in 2010E and 23.6% in 2011E and stable utilisation rate of 85% p.a. for FY10-12E. The new capacity should drive revenue growth of 23-41% in FY10-12E. We have assumed stable operating margins of 16% for FY10-12E on the basis that improved efficiencies from the company's ongoing refurbishment of its older production lines and ability to pass on the higher increase in input (latex, fuel, etc.) costs will cap margin erosion.

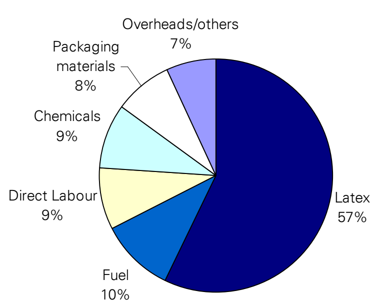
We have assumed an average latex price of RM5.90/kg for 2010E and expect prices to increase 3% p.a. for 2011-12E. While the company is not able to control the rising latex cost, it has historically been able to pass through sustained cost increases (and reductions) to customers. A sharp and volatile upward movement in prices is a possible risk to earnings. Margins during this period will be negatively affected until the price increase is pushed through. We expect Supermax to spend RM50-80m p.a. on capex over the next three years to expand its capacity. Given its strong cash generation, we expect the company to be able to finance its expansion plans internally and still be able to increase dividend payouts.

Figure 58: Key assumptions

	2008	2009	2010E	2011E	2012E
Installed capacity Yr End (mil pcs)	14,476	14,476	17,588	21,738	25,888
% change	7%	0%	22%	24%	19%
Utilization rate	75%	84%	85%	85%	85%
RM/US$	3.50	3.52	3.10	3.00	3.00
% change	3%	1%	-12%	-3%	0%
ASP (US$/1000 pcs)	21.36	19.11	24.84	25.58	26.35
% change	48%	-11%	30%	3%	3%
Latex Price	5.68	4.51	5.90	6.08	6.26
% change	9%	-21%	31%	3%	3%

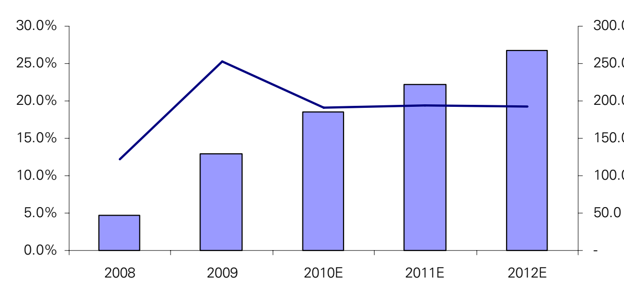
Source: Deutsche Bank, Company data

Figure 59: FY10E cost breakdown



Source: Deutsche Bank, company data

Figure 60: EBITDA margins and net earnings



Source: Deutsche Bank, company data

Sensitivity

Our sensitivity analysis suggests that every 1% change in latex costs will change our FY10E net earnings forecast by 2.4% and DCF valuation by 0.6%.

Figure 61: Sensitivity to 1% change in costs

	Change in FY10E NP	Change in DCF Valuations
Latex costs	2.4%	0.6%
MYR/US$	5.2%	1.3%
Total costs	4.4%	1.1%

Source: Deutsche Bank

Risks

Industry risks include:

1. industry over-expansion capacity overhang.
2. sharp volatility in latex costs and foreign currencies which results in near-term margin squeeze.
3. political risks domestically and regionally.
4. glove manufacturers source c.50% of their raw material (natural rubber latex) from Thailand. A shortage of NR latex supply and thus slow production output on the glove manufacturers' end is a risk.
5. infrastructural bottlenecks and labour shortages.
6. Malaysia's natural gas supply to the glove industry has reached maximum capacity allocation and new allocations are only scheduled to come on stream in 2012. Delays in new allocation will limit capacity expansion for the manufactures and they may have to source for alternative fuel that may be less efficient or cost more.

Company-specific risks include:

1. weaker-than-expected sales volume.
2. execution risks from its aggressive capacity expansion plans. The market is constantly concerned about excess capacity from the industry given that most of the major players plan to expand capacity in the next two years.
3. over-paying for its acquisitions or investments.

Company profile

Company background

Supermax is currently the world's second largest glove manufacturer for disposable rubber gloves with an estimated 10% global market share base on its existing production capacity of 14.5bn pieces of gloves. Established in 1987 as a trading company to distribute latex gloves, the company now has nine factories located in Malaysia and manufacturing a range of latex gloves for export to over 145 countries. Supermax produces a diversified range of gloves catering to the medical, dental, bio-tech, industrial and food & services industries. As an own-brand manufacturer, Supermax has developed a range of successful brands such as Supermax, Aurelia, Maxter, Medic-dent and Supergloves. Its 'Supermax' brand of dental gloves currently commands 8.1% market share of the US dental market. The company has grown its downstream capabilities and currently has six distribution centres with corporate offices based in the US, Brazil, Europe, Australia and Canada, and collaborates with 250 independent distributors. Its closest competitors include Safeskin Corp, a subsidiary of Kimberly Clark, Semperit Corp in Thailand and other Malaysian manufacturers i.e., Top Glove, Kossan Rubber, Latexx Partners and Adventa.

Management and shareholdings

Supermax was founded by Dato' Seri Stanley Thai and his wife Datin Seri Cheryl Tan in 1987 as a trading business distributing latex gloves; they started their first manufacturing facility in 1989. Supermax ventured into own-brand manufacturing and became the first OBM (own brand manufacturing) latex glove manufacturer in Malaysia when it launched its first branded gloves 'Supermax'. The company is still very much run by the founder-manager of the company.

Figure 62: Key management personnel

	Prior experience
Dato' Seri Thai Kim Sim, Stanley Executive Chairman cum Group MD	Started his early business training with Mulpha International, before being appointed CEO of Supermax Actively involved in overseas trade promotions and programs organised by the Ministry of International Trade and Industry Obtained a Bcom (Hons) from the University of Windsor, Ontario, Canada
Datin Seri Tan Bee Geok, Cheryl Executive Director	Heads the finance, operations and administration of the Supermax Group Received her early business training in credit administration with a local financial institution Graduated with Bcom (Hons) from University of Windsor, Ontario, Canada
Dato' Tan Geok Swee Non-Executive Director	Appointed to this position on 18 June 2000 and is a member of the Remuneration Committee Currently the Managing Director of MIFF Sdn The Executive Advisor to the Malaysian Furniture Industry Council and KL & Selangor Furniture Industry Association
Mr Gong Wooi Teik, Felix Independent Non-Executive Director	The Managing Partner of GEP Associates, which is a member firm of AGN International Appointed as an Independent Non-Executive Director of Supermax Corporation Berhad on 28 December 2001 and is a member of the Audit Committee Also a Director of Nikko Electronics Berhad and Cheetah Holdings
Dr. Tan Joo Chai Independent Non-Executive Director	Appointed to this position on 18 June 2000 and is the Chairman of the Nomination Committee. Obtained a PhD in Environmental Engineering from University of Singapore in 1994

Source: Company Data

Insiders hold approximately 35.94% of shares outstanding and about 64.1% of the shares are free floating. 13.8% of the shares are held by foreign shareholders and the rest are domestic. Among institutions, the leading shareholders are Lembaga Tabung Haji (5.1%) and Alantis Investment (4.9%) with a total of 10% of shares. The average daily volume traded on the stock over the past three months was 3.3m shares or just over US$5.8m a day.

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist			
Company	**Ticker**	**Recent price***	**Disclosure**
Supermax	SUPM.KL	6.36 (MYR) 6 May 10	NA
Top Glove	TPGC.KL	11.60 (MYR) 6 May 10	NA

*Prices are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

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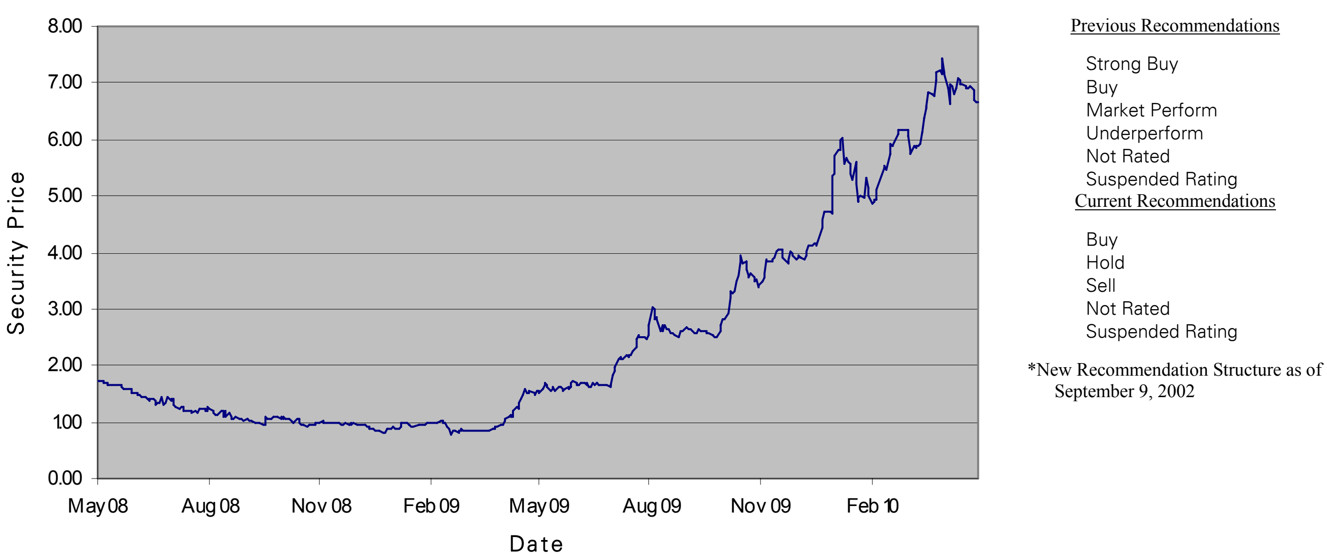
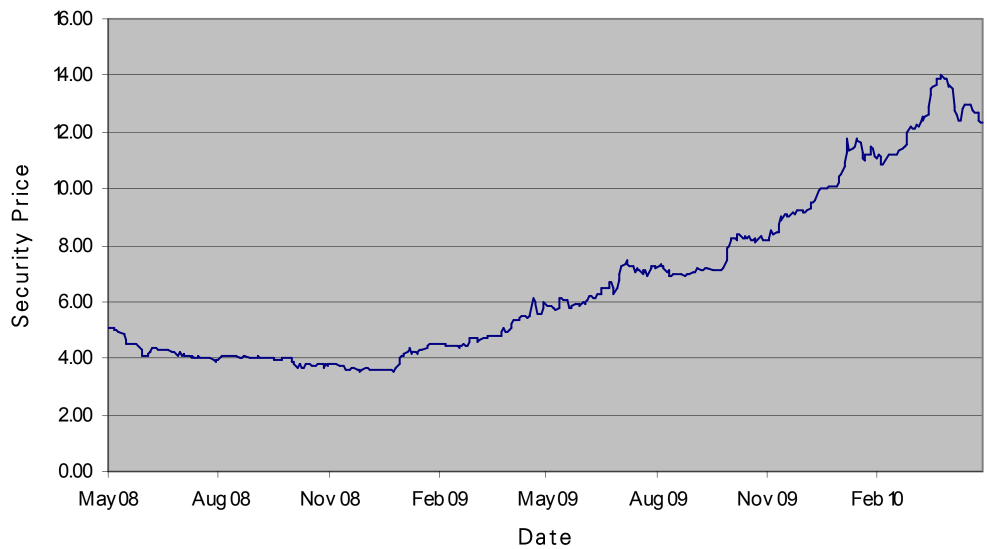
Historical recommendations and target price: Supermax (SUPM.KL)

(as of 06/05/2010)



Historical recommendations and target price: Top Glove (TPGC.KL)

(as of 06/05/2010)



Previous Recommendations

Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9, 2002

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Buy: Based on a current 12- month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus pro-jected dividend yield) , we recommend that investors buy the stock.

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Sell: Expected total return (including dividends) of -10% or worse over a 12-month period

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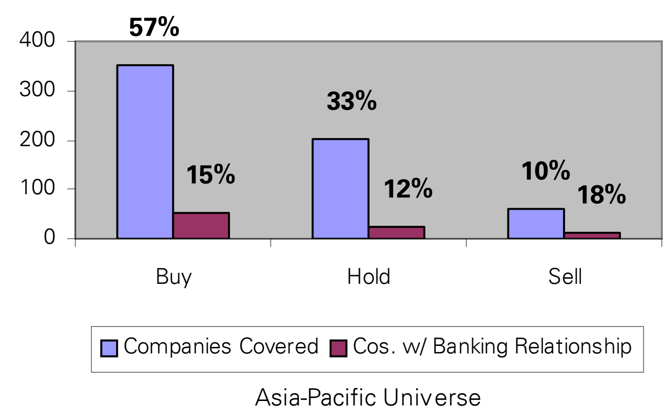

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