



## Supermax Corporation Berhad

Turning Point?

TP: RM 3.90 (+19.6%)

Last traded: RM3.26

BUY

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Supermax held an analyst briefing on Tuesday. In summary, the industry's prospects should improve, now that natural latex prices have softened and the USD strengthened. Management expects latex prices to continue retreating to around RM7.00 per kg by 1Q 2012. According to the Malaysian Rubber Board (MRB), latex-in-bulk traded at around RM8.00 per kg last Tuesday. Furthermore, the change in Supermax's dividend payout policy – up from 20% to 30% in FY12 – should make good investment case for investors searching for decent dividend returns amid the volatile global outlook. Highlights from the meeting are as follows:

### Improving results performance

Supermax reported sequential net profit growth for the first time in 6 quarters. Excluding the RM4.0mn bond investment write off last quarter, we note a turnaround in the group's financials since 2Q. That said, EBITDA continued to advance to RM46.4mn from RM38.1mn on easier natural rubber latex prices, stable exchange rate and solid demand for nitrile gloves. This resulted in better EBITDA margin of 17.1% vs. 16.0% in 2Q FY11.

### Demand still intact

Management believes the overcapacity problem is still prevalent in certain segments of the industry, namely the powdered and PF latex gloves. However, orders are still strong for Supermax due to its sound OBM business model and entrenched distribution network. Furthermore, most of the group's production lines can inter switch to produce either latex or nitrile gloves. In view of the current appetite for nitrile gloves, Supermax has steadily raised the production mix of its nitrile gloves to 36% from 34% in the previous quarter. That said, we understand that the lead time for ordering nitrile gloves currently stands at around 4-5 months while the lead time for ordering latex gloves are much lower at around 45-60 days.

### Glut of nitrile gloves in 2012?

With most glove manufacturers locally and in China ramping up production of nitrile gloves, management believes the industry could see a glut of nitrile gloves by 2012. Strong competition would subsequently lead to pressure on pricing and margins. In the meantime, we note the pricing gap between nitrile and latex gloves are narrowing given: 1) ASP of latex is showing a consistent and sustainable downtrend because the cost of producing natural latex gloves is easing, and 2) ASP for nitrile gloves are rising due to the recent spike in synthetic raw material prices.

### Other key earnings drivers

Management sees new markets, namely China and India opening up. Additionally, management is looking to capture a larger chunk of US, Canada and Germany's medical industry. In Germany, management noted that Supermax has recently passed the country's stringent production and quality audit requirements.

### Share Information

Bloomberg Code	SUCB MK
Stock Code	7106
Listing	Main Market
Share Cap (mn)	340.1
Market Cap (RMmn)	1108.7
Par Value	0.50
52-wk Hi/Low (RM)	4.83/2.26
12-mth Avg Daily Vol ('000 shrs)	1016.5
Estimated Free Float (%)	52.9
Beta	1.49

### Major Shareholders (%)

Dato' Seri Stanley Thai	- 35.6
EPF	- 8.3

### Forecast Revision

	FY11	FY12
Forecast Revision (%)	-	-
Net profit (RMmn)	106.7	123.7
Consensus	112.9	135.6
TA's / Consensus (%)	94.5	91.2
Previous Rating	Buy (Maintained)	

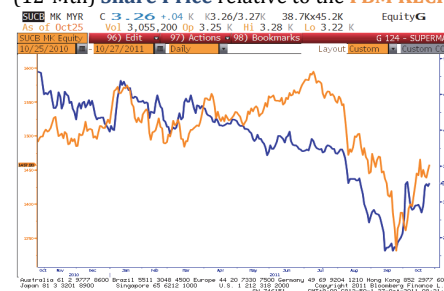
### Financial Indicators

	FY11	FY12
Net gearing (x)	0.5	0.5
CFPS (RM)	0.8	1.4
P/CFPS (x)	4.0	2.4
ROAA (%)	9.0	9.8
ROAE (%)	17.1	17.4
NTA/Share (RM)	1.9	2.1
Price/ NTA (x)	1.7	1.5

### Share Performance (%)

Price Change	SUCB	FBM KLCI
1 mth	27.3	9.5
3 mth	(11.2)	(6.7)
6 mth	(21.1)	(4.6)
12 mth	(27.6)	(2.6)

### (12-Mth) Share Price relative to the FBM KLCI



Elsewhere, we believe Supermax's decision to bump up production of surgical gloves from 30mn pairs to 336mn pairs earlier this year - potentially generating additional sales and net profit of around USD67.2mn and USD10.1mn - was timely. Here, the new lines for surgical gloves is expected to be commissioned by 4Q 2011.

#### Key risks: Brazil's import tax and preference for thinner gloves

Last quarter, management talked about potentially gaining market share for surgical gloves in Brazil. However, we foresee the possibility of demand for gloves in Brazil declining gradually. This comes after the government recently raised the import tariffs of latex gloves from 16% to 35% to protect the local glove manufacturers. Here, we understand that Supermax currently has some 35% share of the market in Brazil.

Meanwhile, we also understand that customers are trending towards thinner nitrile gloves, which could weigh as low as 2.5g to 3.5g per piece vs. the average weight of 5.5g to 6.5g for natural latex gloves. This could potentially discourage nitrile gloves users to switch back to natural latex gloves. On a positive note, the thinner the gloves, the lower the content of raw material is needed to produce each piece of glove.

#### Earnings guidance for FY11 achievable

9M FY11 results were within our expectations. No change to our earnings estimates. We note that our FY11e net profit of RM106.7mn is in line with management's PAT guidance of between RM100mn and RM120mn. We believe the increase in Supermax's dividend policy to 30% of PAT for FY2012 from 20% in FY2011 should make good investment case for investors searching for decent dividend yields. Based on our forecasts, we estimate that the increase in payout along with profit growth should raise DPS to 13.6 sen and 14.9 sen from for FY12 and FY13 from our conservative 8.0 sen previously. The higher DPS will translate to attractive dividend yields of 4.2% to 4.6% for FY12 and FY13.

#### Valuation and recommendation

TP maintained at RM3.90. Our valuation is based on a 10% discount to the industry's targeted PE multiple 12x to Supermax's FY12e EPS of 36.4 sen. With that, we reiterate our **BUY** recommendation on Supermax premised on the potential 19.6% upside from the stock's last close.

**Table 1: Earnings Summary**

FYE Dec	2009	2010	2011F	2012F	2013F
Turnover	803.6	923.3	1098.6	1117.5	1136.5
Pretax profit	151.5	177.4	127.0	147.2	160.0
Net profit	126.6	168.2	106.7	123.7	134.4
Net profit - adjusted	126.6	168.2	106.7	123.7	134.4
EPS	37.2	49.5	31.4	36.4	39.5
EPS - adjusted	37.2	49.5	31.4	36.4	39.5
EPS growth (%)	169.2	32.8	(36.6)	15.9	8.7
PER	8.8	6.6	10.4	9.0	8.2
Dividend (sen)	11.0	9.4	7.6	13.6	14.9
Dividend yield (%)	3.4	2.9	2.3	4.2	4.6

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