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21 April 2010

Supermax Corporation

Good health plan

RECOM	Buy
PRICE	RM7.10
MKT CAPITALISATION	RM1.93bn
BOARD	Main (Syariah stock)
SECTOR	Industrial
INDEX COMPONENT	KLCI, FBMSC, FBMS FBMEMAS

SUCB MK / SUPM.KL

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Investment highlights

- Maintain BUY.** At its 1Q10 results briefing yesterday, Supermax elaborated on the group's 1Q10 performance, provided updates on its plans and shared its outlook for the rubber glove sector. There were no major surprises. Management is confident that demand will remain strong and that a supply glut will not be a concern for at least the next 1½-3 years, which is in line with our demand-supply assumptions. We retain our earnings forecasts and target price of RM11.90, still pegged to 13.2x P/E or a 20% discount to Top Glove's target P/E of 16.5x. We maintain our BUY call on Supermax as we expect the continued growth of global glove demand and the company's upcoming capacity expansion to extend its re-rating. The stock remains one of our top picks for the sector.
- More on 1Q10 results.** Supermax's management attributed the 161% surge in 1Q net profit to strong global demand as well as cost savings from higher efficiency and productivity due to improved processes and refurbished lines. Another factor was the 25.7% cut in interest expense to RM3.7m (1Q09: RM5m) following the full redemption of its RM120m serial bond in Nov last year. All these factors drove an upsurge of its net profit margin from 10.2% in 1Q09 to 23.3% in 1Q10.
- Demand remains strong.** According to the company, the current high latex prices have prompted some customers to hold back their orders in anticipation of lower latex prices after the rubber wintering season ends. As a result, its order backlog has fallen from five months to about three months. The company, however, said that it does not indicate a significant drop in demand as it was in a similar situation in 1Q09 when customers reduced inventories on the expectation of a downturn in latex prices. Management expressed conviction that orders will rebound towards the end of 2Q10.

Key stock statistics

	2009	2010F
FYE Dec		
EPS (sen)	48.1	77.8
P/E (x)	14.8	9.1
Dividend/Share (sen)	11.0	15.0
NTA/Share (RM)	2.1	2.7
Book Value/Share (RM)	2.1	2.7
Issued Capital (m shares)		271.4
52-weeks Share Price Range (RM)	RM7.45/RM1.19	
Major Shareholders:	%	
Dato' Seri Thai Kim Sim, Stanley	20.4	
Datin Seri Tan Bee Geok, Cheryl	14.6	
Koperasi Permodalan Felda	5.5	

Per share data

	2007	2008	2009	2010F
FYE Dec				
Book Value (RM)	1.7	1.6	2.1	2.7
Cash Flow (sen)	32.0	37.3	87.9	56.1
Earnings (sen)	22.6	17.7	48.1	77.8
Dividend (sen)	3.0	3.2	11.0	15.0
Payout Ratio (%)	13.3	18.1	22.9	19.3
P/E (x)	31.4	40.2	14.8	9.1
P/Cash Flow (x)	22.2	19.0	8.1	12.7
P/Book Value (x)	4.3	4.5	3.4	2.6
Dividend Yield (%)	0.4	0.5	1.5	2.1
ROE (%)	17.9	11.7	26.6	32.5
Net Gearing (%)	87.9	90.0	31.5	20.2

Source: Company, CIMB estimates, Bloomberg

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Recent developments

Expansion remains on track. Supermax's capacity expansion is on track. The additional capacity from the refurbished lines at its Lahat plant and three new lines at its Sungai Buloh plant started contributing in 1Q10. On top of that, the company will start testing the first few lines at its Meru plant this month. It has started clearing the site for the first factory at its Glove City. The company's expansion plans will take its annual capacity to 17.6bn pieces this year from 14.5bn pieces last year (Figure 1).

Back orders now stand at 4.9bn. In 1Q10, the company has back orders for 4.9bn pieces (Figure 2) as its capacity could not handle all the orders. But prices are high now, prompting some customers to defer their shipments to the later part of this year when prices are expected to stabilise. Supermax estimates that the earliest it can clear the order backlog is towards the end of 3Q10.

Figure 1: Supermax's expansion plans (m pieces p.a.)

	2008	2009	2010F	2011F
Installed capacity	14,476	14,476	14,476	17,588
Capacity contribution from APLI	2,640	-	-	-
Additional via lines upgrade or expansion	-	-	3,112	4,150
Total capacity	17,116	14,476	17,588	21,738

Source: Company

Figure 2: Supermax's back orders (m pieces)

Orders Received	2008	2009				Total	2010	
		1Q09	2Q09	3Q09	4Q09		1Q10	Total
From Supermax & Seal Polymer's customers	13,500	3,050	4,000	4,000	3,800	14,850	7,540	7,540
From APLI's customers H1N1	2,640 Nil	330 Nil	330 450	330 300	330 300	1,320 1,050	330 200	330 200
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 against shipment	26%	27%	54%	48%	49%	44%	152%	152%

Source: Company

Earnings outlook

No change to our forecasts. Supermax indicated that it is looking at a minimum net profit of RM168m for FY10. We maintain our recently revised forecast of RM211m as the company should be able to at least match 1Q's performance in the remaining quarters given the strong demand this year and will have the ability to take in more orders given the new capacity that is coming in over the next few quarters. It maintains its dividend policy of 20% payout and will pay out as special dividends any earnings in excess of its internal forecast.

Figure 3: P&L analysis (RM m)

FYE Dec	2007	2008	2009	2010F
Revenue	574.3	811.8	814.8	1,249.3
Operating Profit (EBIT)	74.9	98.9	164.0	255.0
Depreciation	(19.9)	(28.8)	(31.6)	(37.7)
Interest Expenses	(15.3)	(20.3)	(16.7)	(14.9)
Pretax Profit	58.6	52.0	152.1	248.4
Effective Tax Rate (%)	4.4	9.6	14.7	15.0
Net Profit	55.9	47.0	129.8	211.1
Operating Margin (%)	13.0	12.2	20.1	20.4
Pretax Margin (%)	10.2	6.4	18.7	19.9
Net Margin (%)	9.7	5.8	15.9	16.9

Source: Company, CIMB estimates

Recommendation

Maintain BUY. The outlook remains healthy for Supermax this year. Although customers' order cycle has been reduced and there could be a slight margin contraction due to high latex prices and the weak US\$, we think this is temporary and will return to normal when the wintering season ends in May. We maintain our BUY call on Supermax. Our target price remains intact at RM11.90, pegged to 13.2x P/E or a 20% discount to Top Glove's target P/E of 16.5x. Potential re-rating catalysts include the continuing uptick in demand and ongoing capacity expansion. The group's foreign shareholding has improved tremendously from less than 2% a year ago to 13.8%. Given its size (second largest in terms of capacity), liquidity (the most liquid rubber glove stock), earnings consistency (strong earnings since APLI write-off) and strong prospects for its OBM gloves and overseas distribution centres, the stock remains one of our top picks for the sector. Investors with a high risk appetite can consider Supermax's two call warrants (Figure 4).

Figure 4: Details of call warrants

Bloomberg code	7106CA CIMBB	7106CB OSK IB
Issuer	CIMB Bank	OSK Investment Bank
Type	European-style	European-style
Settlement	Cash-settled	Cash-settled
Exercise ratio (CW:SUCB share)	8CW-to-1	10CW-to-1
Exercise price	RM5.60	RM6.50
Issue price	RM0.175	RM0.150
Expiry date	10-Mar-11	4-Feb-11

Source: Bloomberg, Bursa Malaysia

Figure 5: Share price chart (RM)



Source: Bloomberg

Financial summary

FYE Dec	2008	2009	2010F	2011F	2012F
Revenue (RM m)	811.8	814.8	1,249.3	1,522.4	1,683.6
EBITDA (RM m)	98.9	164.0	255.0	299.1	324.7
EBITDA margins (%)	12.2%	20.1%	20.4%	19.6%	19.3%
Pretax profit (RM m)	52.0	152.1	248.4	287.3	306.6
Net profit (RM m)	47.0	129.8	211.1	244.2	260.6
EPS (sen)	17.7	48.1	77.8	90.0	96.0
EPS growth (%)	-21.9%	172.2%	61.8%	15.7%	6.7%
P/E (x)	40.2	14.8	9.1	7.9	7.4
Core EPS (sen)	23.3	49.8	77.8	90.0	96.0
Core EPS growth (%)	3.1%	113.4%	56.2%	15.7%	6.7%
Core P/E (x)	30.4	14.3	9.1	7.9	7.4
Gross DPS (sen)	3.2	11.0	15.0	18.0	20.0
Dividend yield (%)	0.5%	1.5%	2.1%	2.5%	2.8%
P/NTA (x)	4.5	3.4	2.6	2.0	1.7
ROE (%)	11.7%	26.6%	32.5%	28.9%	24.6%
Net gearing (%)	90.0%	31.5%	20.2%	4.0%	N/A
Net cash per share (RM)	N/A	N/A	N/A	N/A	0.4
P/CF (x)	73.7	17.0	19.7	9.6	7.7
EV/EBITDA (x)	21.8	11.8	7.5	6.0	5.0
% change in EPS estimates			-	-	-
CIMB/Consensus (x)			1.26	1.27	1.03

Source: Company, CIMB Research, Reuters Estimates

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