Top Glove Corporation

A Third Consecutive Quarterly Loss

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UNDERPERFORM ↔

Price:	RM0.84
Target Price:	RM0.58 ↓

TOPGLOV's 1HFY23 results disappointed due to lower-than-expected sales volume. The group reiterated that the challenging and competitive business landscape will persist throughout 2023. We widen our FY23F net loss by 26% to RM450m (from RM356m) but keep our FY24F net profit unchanged. We trim our asset-based TP slightly to RM0.58 (from RM0.60) and reiterate our UNDERPERFORM call.

TOPGLOV disappointed with a third consecutive quarterly loss, registering a net loss of RM333m in 1HFY23 compared to our full-year net loss forecast of RM356m and the full-year consensus net loss estimate of RM303m. The variance against our forecast came largely from weaker-than-expected sales volume and higher-than-expected cost.

QoQ, 2QFY23 revenue fell 2% due to lower average selling price (ASP) (-4%) which was offset slightly by higher sales volume (+6%). At EBITDA level, it plunged to a loss of RM54m compared to RM62m in 1QFY23 due to: (i) excessive industry capacity leading to reluctance of customers to commit to sizeable orders and hold substantial stocks on expectations of further price decline, (ii) margin erosion as costs remains elevated including natural gas and electricity tariff and labour costs against falling selling prices (ASP/1,000 pieces of USD19-21 vs. cost which we estimate to be USD21-23 per 1,000 pieces), and (iii) reduced economies of scale, particularly, poor cost absorption, as its utilisation rate continues to remain weak at 35% compared to 30% in 1QFY23. As a result, 2QFY23 losses came in at RM165m compared to RM168m in 1QFY23. No dividend was declared in this quarter as expected. **YoY,** 1HFY23 revenue fell 60% due to lower ASP (-28%) and volume sales (-49%) bringing 1HFY23 losses to RM333m.

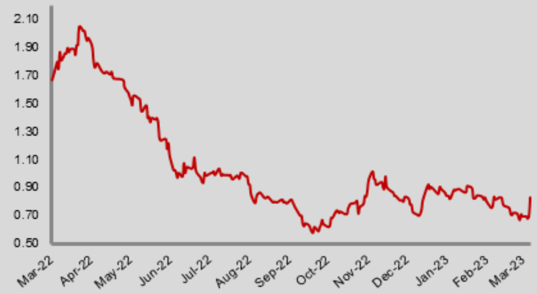
The key takeaways from the analyst briefing yesterday are as follows:

1. TOPGLOV believes that the rate of decline in ASPs has bottomed out and is trying to raise ASP by 5%-10% to USD21 per 1,000 pieces for Mar to April shipments. However, clients may push back as we gathered from sources that Chinese players are selling lower at USD17 per 1,000 pieces.

2. There has been an uptick in orders for the Mar and Apr deliveries, potentially boosting its 3QFY23 utilisation rate to 40% from 35%. There are also signs of buyers returning as stocks are depleting at their customers' warehouses due to products approaching expiration dates. However, we are uncertain if this is sustainable given the massive industry overcapacity with buyers generally still reluctant to place sizeable orders or hold substantial stocks on expectations of further decline in prices. Moreover, the higher sales volume in 2QFY23 could be partly due to a lumpy order from a certain client which accounts for 5%-8% volume sales.

3. TOPGLOV reiterated that a challenging and competitive business landscape will persist through 2023 and only expect to return to the black in 9 to12 months. Specifically, the group hope to turn EBITDA positive in 3QFY23 and break even or return to the black from 4QFY23.

Share Price Performance



KLCI	1,391.60
YTD KLCI change	-6.9%
YTD stock price change	-7.7%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TOPG MK
Market Cap (RM m)	6,686.1
Shares Outstanding	8,007.3
52-week range (H)	2.09
52-week range (L)	0.57
3-mth avg daily vol:	42,833,270
Free Float	44%
Beta	1.7

Major Shareholders

Tan Sri Dr Lim Wee Chai	27.8%
Central Depository Pte Ltd	7.7%
Firstway United Corp	6.9%

Summary Earnings Table

FY Aug (RM m)	2022A	2023F	2024F
Turnover	5573	3980	4280
PBT	365	-246	381
Net Profit / (loss)	236	-498	121
Core NP	236	-450	41
Consensus NP	-	-303	148
Earnings Revision	-	-26%	-
EPS (sen)	2.9	-5.5	0.5
EPS growth (%)	(97.1)	(290.6)	109.2
NDPS (sen)	1.2	0.0	0.3
BVPS (RM)	0.68	0.64	0.64
PER (x)	29.0	(15.2)	165.8
PBV (x)	1.2	1.3	1.3
Net gearing (x)	Net Cash	Net cash	Net cash
Net Div. Yield (%)	1.4	NA	0.3

Outlook. MARGMA projects 12%-15% growth in the global demand for rubber gloves annually from 2023, following an estimated 19% contraction to 399b pieces in 2022. It believes the supply-demand equilibrium may return in 6 to 9 months. However, we beg to differ, expecting the overcapacity situation to persist at least over the next two years. Based on our estimates, the demand-supply situation will only start to head towards equilibrium in 2025 when there is virtually no more new capacity coming onstream while the global demand for gloves continues to rise by 15% per annum underpinned by rising hygiene awareness. Still, capacity is seen to expand further in 2023. We project the demand for gloves to rise by 15% in 2023, which is consistent with MARGMA's forecast. However, this will do little to ease the overcapacity situation as the global glove production capacity will grow another 16% to 595b pieces during the year, as more capacity planned by incumbent and new players during the pandemic years - enticed by super-fat margins that had evaporated - finally come on-line. This will result in the excess capacity rising by 22% to 137b pieces from 112b pieces in 2022. The expanded overcapacity means low prices and depressed plant utilisation will likely persist in 2023. Not helping the already dire situation is the reluctance of customers to commit to sizeable orders and hold substantial stocks on expectations of further decline in prices.

Forecasts. We widen our FY23F net loss by 26% to RM450m (from RM356m) as we reduce our utilisation assumption to 35% from 40%. However, we keep our FY24F earning unchanged.

We reiterate our **UNDERPERFORM** call but nudge our TP down slightly by 3% to RM0.58 (previously RM0.60) based on 0.9x FY23F BVPS, at a 50% discount to the sector's average of 1.7x seen during the last downturns in 2008-2011 and 2014-2015 as we believe the current downturn could go down in history as one of the deepest ever. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 3).

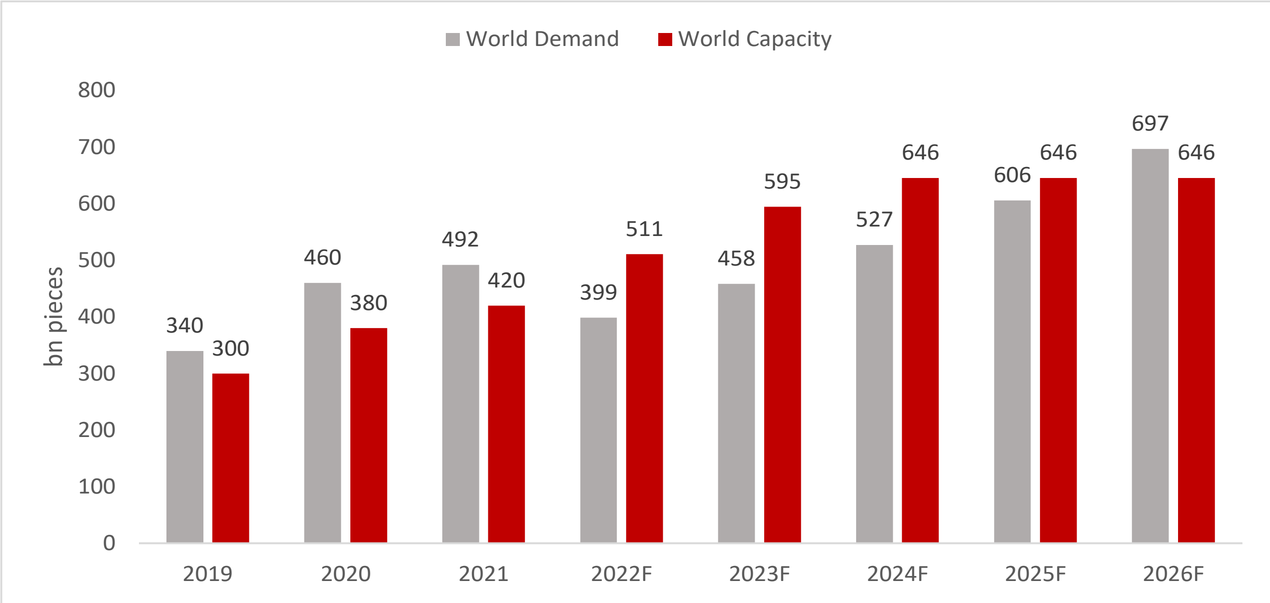
Key risks to our recommendation: (i) the industry turning the corner sooner on stronger-than-expected growth in demand for gloves driven by rising hygiene standards and health awareness globally, (ii) industry consolidation reducing competition among players, and (iii) epidemic and pandemic occurrences.

Results Highlights

	2Q	1Q	QoQ	2Q	YoY	6M	6M	YoY
FYE Aug (RM m)	**FY23**	**FY23**	**Chg %**	**FY22**	**Chg %**	**FY22**	**FY23**	**Chg %**
Turnover	618.0	632.5	(2.3)	1,478.6	(58.2)	3,089.7	1,250.5	(59.5)
EBITDA / (LBITDA)	(54.3)	(61.6)	(11.8)	198.7	(127.3)	542.8	(115.9)	(121.4)
EBIT (LBIT)	(142.8)	(149.6)	(4.6)	112.8	(226.6)	373.4	(292.4)	(178.3)
PBT / (LBT)	(145.9)	(151.6)	(3.8)	112.3	(230.0)	371.1	(297.6)	(180.2)
Net profit / (loss)	(164.7)	(168.2)	(2.1)	87.5	(288.1)	273.3	(332.9)	(221.8)
EPS / (LPS) (sen)	(2.0)	(2.1)	(2.1)	1.1	(284.2)	3.4	(4.1)	(219.1)
EBITDA margin (%)	-8.8	-9.7		13.4		17.6	-9.3	
PBT margin (%)	-23.6	-24.0		7.6		12.0	-23.8	
NP margin (%)	-26.6	-26.6		5.9		8.8	-26.6	
Effective tax rate (%)	-6.2	-3.9		8.9		17.9	-5.0	

Source: Company, Kenanga Research, Bursa Malaysia

Estimated Global Demand/Supply - Excess Supply over CY22-CY24



Source: Kenanga Research

Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	☆		
	Corporate Social Responsibility	★	★	★		
	Management/Workforce Diversity	★	★	★		
	Accessibility & Transparency	★	★	★	☆	
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	☆		
SPECIFIC	Migrant Worker Welfare	★	★	★	☆	
	Pollution Control/Waste Management	★	★	★		
	Automation/Industry 4.0	★	★	★		
	Energy Efficiency	★	★	★		
	Work Site Safety	★	★	★		
	Set-off for Single-Use Product	★				
	OVERALL	★	★	★		

☆ denotes half-star
★ -10% discount to TP
★★ -5% discount to TP
★★★ TP unchanged
★★★★ +5% premium to TP
★★★★★ +10% premium to TP

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net. Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
HARTALEGA HOLDINGS BHD	UP	1.78	1.35	-24%	6,083	Y	03/2023	0.7	(0.7)	-99%	-202%	253.2	N.A.	1.2	0.5%	3.0	1.7%
KOSSAN RUBBER INDUSTRIES	UP	1.24	0.850	-31%	3,164	Y	12/2023	(1.1)	0.9	-101%	-19%	N.A.	138.5	0.8	-0.7%	0.0	0.0%
SUPERMAX CORP BHD	UP	0.850	0.700	-18%	2,248	Y	06/2023	(6.3)	0.9	-124%	-86%	N.A.	95.2	0.5	-3.6%	0.0	0.0%
TOP GLOVE CORP BHD	UP	0.835	0.580	-31%	6,686	Y	08/2023	(5.5)	0.5	-291%	109%	N.A.	165.8	1.3	-8.3%	0.0	0.0%

Source: Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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