

23 July 2024

Glove

A Love Not About to be Rekindled

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UNDERWEIGHT



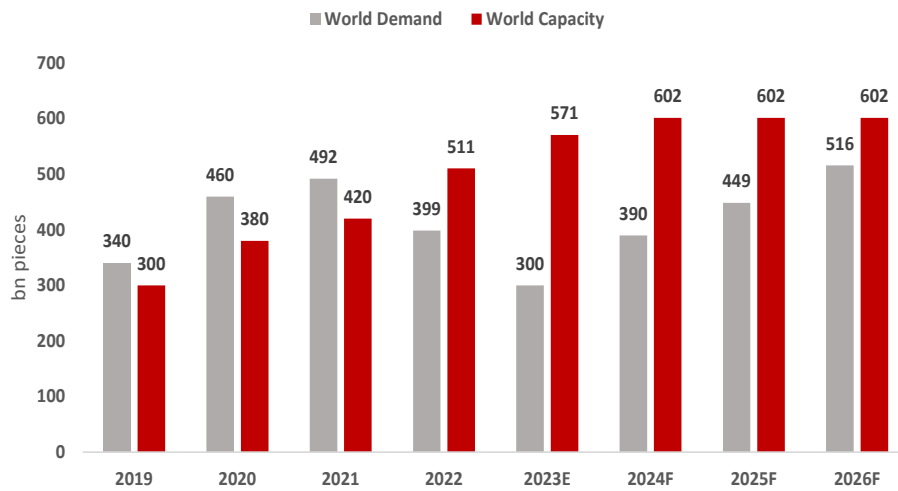
We reiterate our UNDERWEIGHT rating on the sector. We expect the sector's tough operating environment to persist over the immediate term, judging from the still weak earnings undertone in 1QCY24, plagued by overcapacity, predatory pricing by certain overseas players, weak demand and the high cost of inputs. The situation is further aggravated by sustained high operating cost and poor economies of scale from less-than-optimum sales volume despite some recovery in orders. On a slightly brighter note, further decommissioning of older production facilities locally should help to ease supply pressure, at least bringing about more rational competition amongst local players. We avoid all names under our coverage, namely HARTA (UP; TP: RM2.33), KOSSAN (UP; TP: RM1.48), TOPGLOV (UP; TP: RM0.75) and SUPERMX (UP; TP: RM0.83), as tepid profitability does not support the current lofty valuations.

Challenging operating environment to persist in 2HCY24. We reiterate our view that the challenging and competitive business landscape currently faced by the sector will persist in 2HCY24. The weak earnings undertone in 1QCY24 suggests the operating environment remains challenging, plagued by overcapacity, predatory pricing by certain overseas players, weak demand, and the high cost of inputs. While some players have returned to the black, the tepid profitability does not support the lofty valuations. The industry will continue to face massive over-supply, predatory pricing by certain overseas players (i.e. selling below cost over an extended period of time to eliminate competitors), weak demand and the high cost of inputs such as nitrile butadiene rubber and latex. Generally, players continue to grapple with the high operating cost and sustained poor economies of scale from less than optimum sales volume despite seeing incremental orders. The industry expect volatile quarterly sales as distributors and buyers sees no urgency to place sizeable orders or hold substantial stocks as supply is plentiful and readily available. Overall, the industry is cautious about raising prices significantly (to fully pass on the higher input cost) given the still competitive landscape in the industry. With a low industry utilisation of about 45%, this is without a doubt still a buyers' market.

Mixed signals in input raw material price trend, savings from decommissioning old plants in 2HCY24. Moving into 2HCY24, we expect input latex price to ease or taper off as the wintering months (low production during the wintering months between Dec till May) come to an end. However, nitrile butadiene rubber price is expected to continue to remain stubbornly high (YTD CY24: +10%). On the other hand, we understand that natural gas which accounts for 15% of total cost is expected to be higher H-o-H. Elsewhere, we expect cost savings initiatives arising from decommissioning of old plants to cushion losses as well. Overall, all players are mindful that the prospect of raising ASP further in subsequent quarters is challenging due to the current massive overcapacity situation, with only a handful of customers agreeing thus far. Due to the current competitive pressure emanating from massive oversupply and low industry utilisation averaging 40%, customers can walk away and choose to buy from other players whenever there is an attempt to raise prices. Case in point, buyers can turn to Chinese manufacturers which are still selling below USD20 per 1,000 pieces at USD16-18 per 1,000 pieces.

Oversupply to persist throughout CY24. Based on our estimates, the demand-supply situation will only start to head towards equilibrium in CY26 when there is virtually no more new capacity coming onstream while assuming the global demand for gloves is to rise by 15% underpinned by rising hygiene awareness. MARGMA projects global demand for gloves to grow by 12% to 15% annually from CY24, following an estimated 25% contraction to 300b pieces in CY23. We project the demand for gloves to rise by 30% in CY24 to 390b pieces on restocking before moderating to its organic growth of 15% annually. This will still result in an excess capacity of 212b pieces in CY24. The overcapacity still persists which means low prices and depressed plant utilisation will continue to plague the industry in CY24. Our CY24 forecasts assume: (i) an ASP per 1,000 pieces of USD20, similar to CY23, and (ii) an average plant utilisation of 45% vs. an estimated 40% in CY23. In the meantime, we do not have any top pick for the sector.

Exhibit 1: Estimated Global Demand/Supply - Excess Supply over CY22-CY25



Source: Kenanga Research

23 July 2024

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RMm)	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	3.40	2.33	-31%	11,605	Y	03/2024	1.5	1.5	297%	4%	229.4	221.0	2.5	1.1%	0.0	0.0%
KOSSAN RUBBER INDUSTRIES	UP	2.43	1.48	-39%	6,200	Y	12/2024	4.7	4.9	140%	5%	52.2	49.7	1.6	3.1%	2.0	0.8%
SUPERMAX CORP BHD	UP	0.915	0.830	-9%	2,344	N	06/2024	(1.9)	0.7	-134%	-62%	NM	131.0	0.6	-1.1%	0.0	0.0%
TOP GLOVE CORP BHD	UP	1.22	0.750	-39%	9,772	Y	08/2024	(1.6)	0.8	-114%	-49%	NM	153.0	2.2	-2.7%	0.0	0.0%

Source: Kenanga Research

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23 July 2024

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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