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20 April 2010

Supermax Corporation

Profit maxed despite concerns

RECOM	Buy
PRICE	RM6.90
MKT CAPITALISATION	RM1.87bn
BOARD	Main (Syariah stock)
SECTOR	Industrial
INDEX COMPONENT	KLCI, FBMSC, FBMS FBMEMAS

SUCB MK / SUPM.KL

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Results highlights

- **Above expectations, maintain BUY.** As highlighted in our update last week, Supermax reported another strong quarter yesterday. Annualised 1Q net profit beat our forecast by 21% and consensus by 24%. The results were clearly above our expectations as the remaining quarters should at least match 1Q earnings given the additional capacity coming in from 2Q onwards. As expected, no dividends were declared for the quarter, which was no surprise as the company usually announces dividends during 2H. We have revised our assumptions for latex price and ASP, leading to a 23-24% upgrade of our FY10-12 earnings forecasts. Our target price rises from RM9.65 to RM11.90 as we continue to value the stock at a 20% discount to Top Glove's target P/E of 16.5x. We maintain our BUY call on Supermax, premised on the potential re-rating catalysts of these strong results, continuing rise in demand and upcoming capacity expansion. The stock remains one of our top picks for the rubber glove sector.
- **Stronger earnings qoq and yoy.** We highlighted in our results preview that Supermax could report a net profit rise of about 13% qoq and a more than doubling on yoy basis. The company did not disappoint. Yesterday, it announced a 1Q10 net profit of RM51.5m, an increase of 17% qoq and 161% yoy. The growth was achieved through strong global demand and rising awareness of the importance of rubber glove usage. Sales volume rose 8% qoq and 21% yoy to 3.21bn. On top of that, net profit margin improved from 10.2% in 1Q09 to 23.3% in 1Q10.
- **Still positive on glove makers.** Of late, rubber glove stocks have been hammered by concerns over the potential earnings impact of high latex costs and a weakening US\$. As we noted in our update last week, any impact on margins would be temporary given the glovemakers' ability to pass through cost increases.

Key stock statistics

	2009	2010F
FYE Dec		
EPS (sen)	48.1	77.8
P/E (x)	14.3	8.9
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	3.3	11.0	15.0
Payout Ratio (%)	13.3	18.6	22.9	19.3
P/E (x)	30.5	39.1	14.3	8.9
P/Cash Flow (x)	21.5	18.5	7.8	12.3
P/Book Value (x)	4.1	4.4	3.3	2.5
Dividend Yield (%)	0.4	0.5	1.6	2.2
ROE (%)	17.9	11.7	26.6	32.5
Net Gearing (%)	87.9	90.0	31.5	20.2

Source: Company, CIMB estimates, Bloomberg

Please read carefully the important disclosures at the end of this publication.

More on the results

Rising latex costs and weaker US\$ affecting margins. Although rising latex and weaker US\$ could have a negative impact on glovemakers' margins, the impact on Supermax is minimal as it is able to adjust its selling prices to take into account of the higher costs and changes in exchange rates subject to a lag of 1-2 months. Although its 1Q operating margin shrank about 3.8% pts qoq to 26.3%, we view this as a temporary setback as the company will revise selling prices for future orders. We, therefore, believe that the firmer ringgit and rising latex should have minimal impact on the company's bottomline

Figure 1: Results comparison (RM m)

FYE Dec	1QFY10	1QFY09	% Change
Revenue	220.7	192.4	14.7
Operating Profit (EBIT)	58.0	28.5	103.5
Depreciation	(8.1)	(7.2)	12.4
Interest Expenses	(3.7)	(5.0)	(25.7)
Associates	10.5	8.1	28.4
Pretax Profit	54.3	23.5	131.3
Net Profit	51.5	19.7	161.2
Operating Margin	26.3	14.8	77.5
Pretax Margin	24.6	12.2	101.7
Net Margin	23.3	10.2	127.7

Source: Company, CIMB estimates

Earnings outlook

Earnings raised. Given the weaker US\$ and record latex prices, we are revising our FY10-12 ASPs from US\$26-28 to US\$28-30 which should more than offset the higher latex cost assumption of RM6.00-6.20/kg vs. RM5.80-6.00/kg previously. The net effect of these adjustments is a 23-24% increase in our FY10-12 earnings forecasts.

Net cash from FY12? Our revised earnings also suggest a rise in Supermax's ROE to about 32.5% this year (FY09: 26.6%). We raise our FY10-12 DPS forecasts accordingly from 13-18 sen to 15-20 sen as the company is firm about maintaining its dividend payout of 20% for now. However, based on its potential strong growth in earnings and annual capex of around RM60m, we estimate that the company could be in a net cash position as early as FY12. This leads to further upside to our dividend forecast for FY12 onwards.

Figure 2: Supermax's expansion plans ('000 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 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

Target price raised to RM11.90. Using our revised earnings, we derive a new target price of RM11.90 (RM9.65 previously), pegged to a P/E of 13.2x which is based on an unchanged 20% discount to Top Glove's target P/E of 16.5x. This represents 73% upside from yesterday's closing share price of RM6.90. The stock will go ex of its proposed special dividend of 4.5 sen today. On top of that, a final dividend of 4 sen and the 1-to-4 bonus issue are estimated to go ex by the end of June (Figure 4). They are currently subject to shareholders' approval at the AGM which will be held in May. The bonus issue will enhance the stock's liquidity and make it more affordable in terms of absolute cost. Based on our revised earnings, the stock is now trading at an attractive FY11 P/E of 7.7x, slightly below the sector average of 8.4x. We maintain our BUY call on Supermax, premised on the potential re-rating catalysts of these strong results, the continuing rise in glove demand and upcoming capacity expansion. Supermax remains one of our top picks for the sector. Investors with a high risk appetite can consider Supermax's two call warrants (Figure 5).

Trading at 40% discount to Top Glove. Relative to Top Glove, Supermax has been at P/E discounts of 14-77% (Figure 6) over the past five years. Since the write-off of its investment in APLI at end-08, the gap between its P/E and Top Glove's has narrowed. Currently, it is trading at about 40% discount to Top Glove.

Figure 4: Key dates

Key dates	Timeline
Ex- special div date (4Q09)	20-Apr
Ex- final div date (4Q09) *	End-June
Ex-bonus date *	End-June

*Subject to shareholders' approval

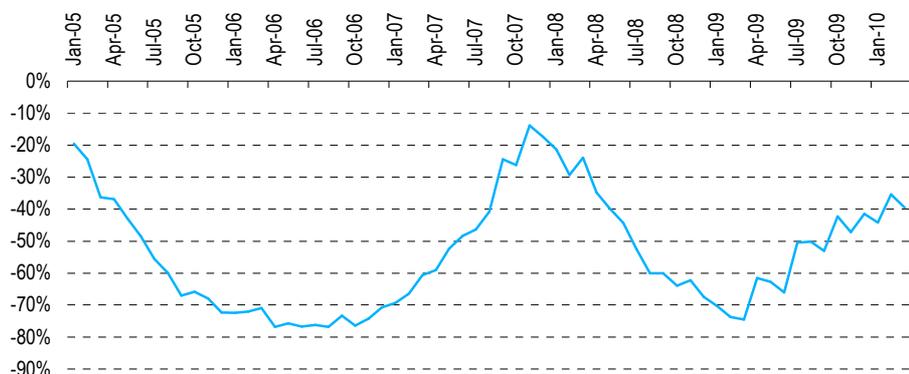
Source: Company

Figure 5: Details of call warrants

	7106CA CIMBB	7106CB OSK IB
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 6: Supermax's 1-year forward P/E relative to Top Glove



Source: CIMB estimates, Bloomberg

Figure 7: 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)	39.1	14.3	8.9	7.7	7.2
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)	29.6	13.9	8.9	7.7	7.2
Gross DPS (sen)	3.3	11.0	15.0	18.0	20.0
Dividend yield (%)	0.5%	1.6%	2.2%	2.6%	2.9%
P/NTA (x)	4.4	3.3	2.5	2.0	1.6
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)	71.6	16.5	19.1	9.4	7.5
EV/EBITDA (x)	21.2	11.5	7.3	5.8	4.8
% change in EPS estimates			24.1	23.2	23.7
CIMB/Consensus (x)			1.26	1.29	1.10

Source: Company, CIMB Research, Reuters Estimates

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