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AFFIN INVESTMENT BANK
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Flash Note

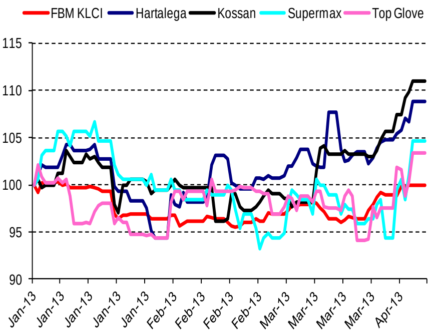
A 'lift from H9N7 viral outbreak in China

OVERWEIGHT (maintain)

Absolute Performance (%)

	1M	3M	12M
Kossan	+13.0	+9.7	+16.2
Supermax	**+6.3**	**-1.0**	**+6.3**
Top Glove	+4.8	+1.6	+28.5
Hartalega	**+4.9**	**+4.7**	**+29.9**

Fig 1: Relative performance chart



Source: Bloomberg, Affin

Share prices of glove companies rallied due to H9N7 flu virus in China

Last week, share prices of rubber gloves stocks rallied following the news of an outbreak of H9N7 flu virus in China. It has been reported that the total number of confirmed cases now stands at 18, with 6 deaths. While we are hopeful that the outbreak would be contained soon, we believe this incident would fuel demand for examination gloves (increasing hygiene awareness and health alert,) and thus benefiting the whole rubber gloves sector. To recap, the most recent 2009-10 H1N1 flu had killed c. 12,470 people around the world, with the Southeast Asia and Africa being the hardest hit regions. According to *The Lancet Infectious Disease,* c.60% of the total deaths is from these two continents.

Potentially higher orders in anticipation of higher future demand

Although the actual increase in the use of examination gloves is not immediate, the potential for increased usage of gloves in the coming months will prompt healthcare companies to stock up on gloves and plan to place bigger new orders. This is expected to put more pressure on the supply of gloves, of which glove makers (ex-Top Glove) are already operating at near maximum optimal capacity, with an average utilization rate of 90%.

A boost from growing healthcare awareness

Unlike in 2009 during which the surge in glove usage arose from a recovery in the global economy and the H1N1 pandemic, we believe that orders are on the rise because the global population is increasingly becoming more hygiene conscious. Some have even set more stringent requirements on the quality of gloves used while others are encouraging more healthcare centres to use them, especially the developing countries where the practice of using gloves is still minimal. We believe the hygiene concerns of both individuals and governments will gradually lead to higher glove usage over time. In fact, the rubber glove industry is eyeing on China and India, where the anticipated demand (should their governments start to enforce the use of examination gloves) may increase by 2-3x of the current world demand of c.160bn pieces.

Operating environment is still healthy

The sector's key growth driver, latex price, which makes up 55%-60% of glove manufacturers' production cost, is still low at RM5.80-6.30/kg despite entering into the wintering period. (Wintering period starts from January-May every year and note that latex price has fallen by -26% since its peak in March 2012 of RM7.92/kg). Coupled with the increase in plant automations to help boost operating efficiencies, we are positive on the glove manufacturers' ability in sustaining healthy operating margins.

Maintain Overweight on the sector.

In view of: 1) the low and stable latex cost; 2) resilient demand from both developed and developing economies due to improving health awareness and more stringent regulations; and 3) improving plant automations, we remains positive on the rubber glove sector. We maintain our **OVERWEIGHT** view with **Supermax (BUY, RM2.50)** as our top pick for the sector due to its undemanding valuations and good earnings visibility.

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Figure 2: Valuation matrix

Stock	Rating	Sh Pr (RM)	TP (RM)	Shares out	Mkt Cap (RMm)	Year End	Core PE (x) CY12	Core PE (x) CY13	EPS growth (%) CY12	EPS growth (%) CY13	EV/EBITDA (x)	P/B (x)	Net Div Yield (%) FY12	Net Div Yield (%) FY13
Kossan	BUY	3.73	3.77	318.62	1,188	Dec	8.7	7.9	14.4	10.6	6.9	2.1	2.4	2.7
Top Glove	ADD	5.73	6.28	619.42	3,549	Aug	14.0	12.0	7.4	15.9	10.8	2.9	3.7	4.2
Supermax	BUY	2.02	2.50	679.15	1,372	Dec	8.0	7.6	18.0	5.2	9.3	1.3	3.5	4.5
Hartalega	ADD	5.13	5.15	733.31	3,762	Mar	14.4	12.9	13.7	11.3	11.5	5.2	2.9	3.1
Simple average							11.3	10.1	13.4	10.8	9.6	2.9	3.1	3.6

Source: Bloomberg, Affin

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +15% over a 12-month period
TRADING BUY (TR BUY)	Total return is expected to exceed +15% over a 3-month period due to short-term positive development, but fundamentals are not strong enough to warrant a Buy call. This is to cater to investors who are willing to take on higher risks
ADD	Total return is expected to be between 0% to +15% over a 12-month period
REDUCE	Total return is expected to be between 0% to -15% over a 12-month period
TRADING SELL (TR SELL)	Total return is expected to exceed -15% over a 3-month period due to short-term negative development, but fundamentals are strong enough to avoid a Sell call. This is to cater to investors who are willing to take on higher risks
SELL	Total return is expected to be below -15% over a 12-month period
NOT RATED	Affin Investment Bank does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation
OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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