

04 December 2013

Supermax Corporation

Exciting Times Ahead

OUTPERFORM ↔

Price: **RM2.69**
Target Price: **RM3.06** ↔

We came away from Supermax ("SUPERMX") 3Q13 post results briefing feeling excited about growth prospects going forward. We believe that SUPERMX is on track to delivering mid-teens growth over the next two years. The key takeaways from SUPERMX briefing include the followings: - (i) explanation of the massive expansion plans for Glove City and Supermax Business Park, (ii) new capacity's net margin ranges between 9% to 11% due to intense competition, (iii) new capacity from factory Lot 6058 & 6059 to drive growth over the next two years, and (iv) minimal concerns about higher energy costs going forward. Maintain OUTPERFORM and TP is RM3.06 based on 13x FY14E EPS.

Massive expansion plans for Glove City and SUPERMX Business Park. During the briefing, SUPERMX outlined its plans for both Glove City and its recently acquired land in Serendah, otherwise known as SUPERMX Business Park. The expansion at both sites will cost a total RM1.3b over an estimated 11 years. The first phase of Glove City, comprising of six large plants with a total capacity of 24.6b pieces. It is expected to commence in 1H2015 after Lot 6058 and Lot 6059 have been fully commissioned with an estimated CAPEX of RM95m. Key infrastructure, including water and natural gas, is now in place, which is the main reason for the delays in the past. We understand that Glove City's 36-acre land which is located in Bukit Kapar was purchased for RM18m (RM11psf) which is fair considering that the industrial lands in the area are around RM16psf. Concurrently, the recently acquired 100-acre land in Serendah (SUPERMX Business Park) is expected to be developed in 2H2014. To recap, the project will be located at the new site measuring 100 acres of which 60 acres will be utilised for an Integrated Glove Manufacturing Complex (IGMC). The project will be spread over two phases over nine years whereby the first phase is scheduled to commence in 2014-2018 comprising 28 production lines (production capacity of 10.9b p.a.) and the second phase is scheduled to begin in 2019-2022 comprising 12 production lines (production capacity of 4.7b p.a.). CAPEX for IGMC's first phase is expected to be RM70m. We understand that the remaining 40% of the land has been earmarked for property development, which targets the gloves industry supporting businesses and will have an estimated GDV of RM350m-RM400m. For illustrative purposes, assuming a conservative pre-tax margin of 25% (net: 19%), the project would generate a total net profit of RM66-75m over a 5-year period. We are not overly concerned with funding considering that SUPERMX has a net gearing of 12% as at 30 Sept 2013 and operating cashflow which we forecast will average RM115m p.a.. Additionally profits gained from sale of the factories built for supporting industries can plough back into the CAPEX for IGMC.

Management anticipates a net margin range of 9% to 11% due to intense competition going forward. In anticipation of intense competition, management guided that average selling price (ASPs) of the new capacity of gloves will be priced such that net margins will range at 9% to 11%. Although this is slightly below our 11.9% net margin forecast in FY14, we are not overly concerned. This is simply because SUPERMX is gradually automating its production processes starting from Lot 6070. When completed, the two new plants in Lot 6058 and Lot 6059 in Meru, Klang is expected to be fully automated from automated mechanical stripping to packing of gloves, leading to higher production efficiency. As such, we believe overall margins could improve. Additionally, unlike other glove players, SUPERMX does not face the risk of long production downtimes since they do not cater much to clientele requesting for highly customized single-product. Thus, this translates into lesser idle period required to accommodate such requirements.

2 new plants to drive growth going forward. The two plants namely Lot 6059 and Lot 6058 are on track to commission commercial productions in 1Q 2014. Lot 6059 and 6058 will have 24 and 16 production lines producing 3.2b and 2.2b pieces of nitrile gloves, respectively, bringing the total nitrile production capacity from 6.9b (including the 1.4bn in Lot 6070) to 12.3b pieces p.a. or 52% of the total installed capacity. Given the strong demand for nitrile gloves, SUPERMX is currently facing a 2-month oversold position.

Not concerned about potential high energy costs going forward. Management guided that the new electricity tariff hike will cost an additional RM3.5m or 2.4% of our FY14 net profit forecast. Electricity accounts for an estimated 20-30% fuel costs which in turn make up 10% of SUPERMX total production costs. Natural gas accounts for the remaining 60-70%. The impact of the electricity hike is not a significant dampener to rubber gloves players' earnings, including SUPERMX. In the past, SUPERMX has managed to pass on the energy-related cost increases. Case in point is back in when the June-2011 hike in gas and electricity tariffs while SUPERMX earnings were not impacted. SUPERMX recorded 2Q11, 3Q11 and 4Q11 net profit of RM22.6m, RM30.9m and RM28.2m respectively. Specifically, pre-tax margins pre and post-implementation hike in gas and electricity tariff were 10.1% (2Q11), 12.5% (3Q11) and 10.6% (4Q11) respectively.

Trading at an average 33% discount to the sector average. Since our TP/CALL upgrade in Feb 2013, the stock has risen by 35%. We continue to like the stock for its steep 33% discount to its peers as well as being a beneficiary of the weakening Ringgit against the USD as it does not hedge its US dollar receipts. SUPERMX is trading at 11.5x FY14 earnings while KOSSAN is trading at 15.1x FY14 earnings. We believe the valuation gap should narrow when we consider that SUPERMX's capacity and net profit are at levels similar to KOSSAN. Maintain OUTPERFORM with a TP of RM3.06 based on 13x FY14 EPS (applied targeted PER is at +1.0SD level above the 5-year historical average).

Share Price Performance



KLCI	1,828.06
YTD KLCI chg	8.2%
YTD stock price chg	36.8%

Stock Information

Bloomberg Ticker	SUCB MK Equity
Market Cap (RM m)	1,827.0
Issued shares	679.2
52-week range (H)	2.85
52-week range (L)	1.79
3-mth avg daily vol:	3,173,370
Free Float	59%
Beta	0.9

Major Shareholders

KIM SIM THAI	20.5%
BEE GEOK TAN	15.2%

Summary Earnings Table

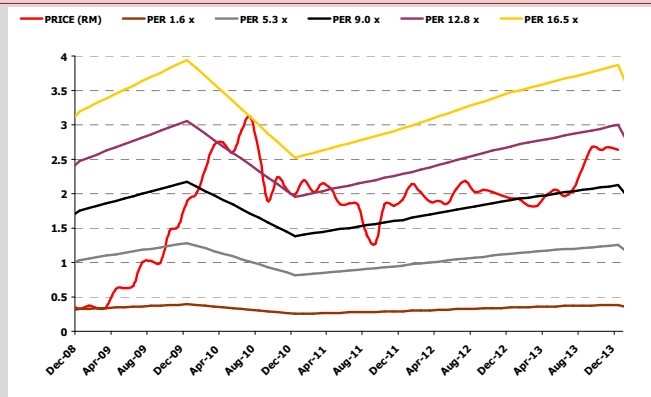
FY Dec (RM'm)	2012A	2013E	2014E
Turnover	1048.2	1200.1	1340.2
EBIT	126.7	152.4	171.2
PBT	140.2	165.2	184.1
Net Profit (NP)	121.8	143.2	159.6
Consensus (NP)		139.0	157.9
Earnings Revision		-	-
EPS (sen)	17.9	21.1	23.5
EPS growth (%)	17.0	17.6	11.4
NDPS (sen)	5.0	6.3	7.0
BVPS (RM)	1.29	1.43	1.60
PER (X)	15.0	12.8	11.5
PBV (X)	2.1	1.9	1.7
Net Gearing (%)	18.3	13.7	12.8
Net Div. Yield (%)	1.9	2.3	2.6

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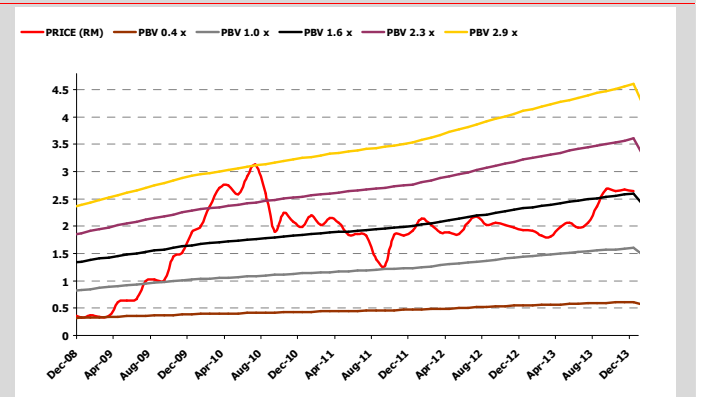
Income Statement						Financial Data & Ratios					
FY Dec (RM m)	2010A	2011A	2012A	2013E	2014E	FY Dec (RM m)	2010A	2011A	2012A	2013E	2014E
Revenue	977.3	1021.4	1048.2	1206.9	1361.7	Growth					
EBITDA	181.4	114.4	151.3	178.6	201.5	Turnover (%)	21.6%	4.5%	2.6%	15.1%	12.8%
Depreciation	-26.0	-24.1	-24.3	-26.3	-30.4	EBITDA (%)	-9.7%	-36.9%	32.2%	18.1%	12.8%
Operating Profit	155.5	90.4	127.0	152.3	171.2	Operating Profit (%)	-14.2%	-41.9%	40.6%	19.9%	12.4%
Other Income	0.3	0.0	0.0	0.0	0.0	PBT (%)	92.5%	-39.0%	25.3%	17.6%	11.4%
Interest Exp	-13.9	-13.1	-9.9	-11.2	-11.2	Core Net Profit (%)	88.1%	-34.5%	16.9%	17.6%	11.4%
Associate	42.0	34.8	23.4	24.1	24.1						
Exceptional Items	0.0	0.0	0.0	0.0	0.0	Profitability (%)					
PBT	183.8	112.1	140.5	165.2	184.0	EBITDA Margin	18.6%	11.2%	14.4%	14.8%	14.8%
Taxation	-24.9	-8.1	-18.7	-22.0	-24.5	Operating Margin	15.9%	8.8%	12.1%	12.6%	12.6%
Minority Interest	0.0	0.1	0.0	0.0	0.0	PBT Margin	18.8%	11.0%	13.4%	13.7%	13.5%
Net Profit	158.9	104.2	121.8	143.2	159.5	Core Net Margin	16.3%	10.2%	11.6%	11.9%	11.7%
						Effective Tax Rate	13.5%	7.2%	13.3%	13.3%	13.3%
						ROA	14.9%	8.6%	9.7%	10.3%	10.5%
						ROE	23.0%	13.5%	13.9%	14.7%	14.7%
Balance Sheet						DuPont Analysis					
FY Dec (RM m)	2010A	2011A	2012A	2013E	2014E	Net Margin (%)	16.3%	10.2%	11.6%	11.9%	11.7%
Fixed Assets	387.9	402.2	450.5	499.9	569.6	Assets Turnover (x)	1.1	1.2	1.2	1.2	1.1
Investments in associates	193.5	228.4	251.7	251.7	251.7	Leverage Factor (x)	1.5	1.6	1.4	1.4	1.4
Intangible Assets	28.7	28.7	28.7	28.7	28.7	ROE (%)	23.0%	13.5%	13.9%	14.7%	14.7%
Other FA	10.1	5.1	2.4	2.4	2.4	Leverage					
Inventories	133.1	223.1	233.6	269.0	303.5	Debt/Asset (x)	0.3	0.3	0.2	0.2	0.2
Receivables	119.4	115.6	171.8	190.6	215.1	Debt/Equity (x)	0.4	0.4	0.3	0.3	0.3
Other CA	95.2	97.8	0.0	0.0	0.0	Net Cash/(Debt)	28.7	29.4	18.4	13.7	12.8
Cash	97.4	104.5	122.3	149.7	144.0	Net Debt/Equity (x)	28.7	29.4	18.4	13.7	12.8
Total Assets	1065.4	1205.4	1261.1	1392.1	1515.1						
Payables	40.1	60.0	48.7	56.1	63.3	Valuations					
ST	155.1	190.5	142.1	142.1	142.1	EPS (sen)	23.4	15.3	17.9	21.0	23.5
Borrowings	24.5	27.3	41.0	64.3	68.5	NDPS (sen)	7.5	4.8	5.0	6.3	7.0
Other ST	140.5	140.5	141.2	141.2	141.2	BVPS (RM)	1.0	1.1	1.3	1.4	1.6
Liability	13.6	18.2	12.4	12.4	12.4	PER (x)	11.5	17.6	15.0	12.8	11.5
LT Borrowings	0.1	-0.1	0.0	0.0	0.0	Net Div. Yield (%)	2.8	0.7	1.9	2.3	2.6
Other LT	0.1	-0.1	0.0	0.0	0.0	P/BV (x)	2.8	2.5	2.1	1.9	1.7
Liability											
Minorities Int.											
Net Assets	691.5	769.1	875.7	976.0	1087.7						
Share Capital	170.0	170.0	340.1	340.1	340.1						
Reserves	521.4	599.1	535.7	635.9	747.6						
Equity	691.5	769.1	875.7	976.0	1087.7						
Cashflow Statement											
FY Dec (RM m)	2010A	2011A	2012A	2013E	2014E						
Operating CF	46.9	43.6	167.8	122.0	118.2						
Investing CF	(46.1)	(38.1)	(68.1)	(100.0)	(100.0)						
Financing CF	(21.6)	0.6	(81.0)	4.6	(23.9)						
Change In Cash	(20.8)	6.0	18.6	26.6	(5.6)						
Free CF	0.3	5.4	99.7	22.0	18.2						

Source: Kenanga Research, Bloomberg

Fwd PER Band



Fwd PBV Band



Source: Kenanga Research, Bloomberg

Stock Ratings are defined as follows:

Stock Recommendations

- OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
(An approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%)
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of 3% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than 3%
(An approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate)

Sector Recommendations***

- OVERWEIGHT : A particular stock's Expected Total Return is MORE than 10%
(An approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%)
NEUTRAL : A particular stock's Expected Total Return is WITHIN the range of 3% to 10%
UNDERWEIGHT : A particular stock's Expected Total Return is LESS than 3%
(An approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate)

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

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