

Industry Focus

Rubber Gloves

Malaysia Equity Research PP 12942/03/2013(031972)

2 May 2012

Minimum wage will dent earnings

- The minimum wage will take effect six months after the Order is gazetted
- Expect higher staff costs, but impact softened as certain fixed allowances are included as part of minimum wage
- Earnings will be dampened pending additional wages passed on to customers

Minimum wage set at RM800-900 per month. The minimum wage for the private sector was set at RM900 per month for employees in the peninsula, and RM800 for workers in Sarawak, Sabah and the Federal Territory of Labuan. There will be a six-month grace period for implementation from the date the Minimum Wage Order is gazetted. The government has also provided some flexibility whereby some allowances or fixed cash payments are allowed to be absorbed in the calculation for minimum wage.

Higher staff costs, lower earnings. In our previous report, we highlighted the impact of minimum wages on the glove makers. Our sensitivity analysis showed staff costs would increase by 17-22% while earnings could fall by 5-19%, if minimum wage of RM900 per month is implemented assuming no change in ASPs.

Hartalega is the least affected; Top Glove most affected. Based on our estimates, Hartalega's salary costs could rise by RM10m a year (+17%) and this would lower FY13F net profit by 5%. For Top Glove, staff costs could rise as much as RM39m (+22%), denting FY13F earnings by 19%. Meanwhile, we estimate Kossan's annual salary costs to increase by RM18m (+17%) and net profit to fall by 13%. However, if fixed allowances or cash payments are allowed in the calculation for minimum wages, the impact will be softened.

No change to our HOLD ratings. We maintain Hold for Top Glove (TP: RM4.80), Hartalega (TP: RM7.70) and Kossan (TP: RM3.30). We expect the additional staff costs to be passed to customers over time, but in the immediate term, we expect earnings and margins to be dampened.

KLCI : 1,570.61

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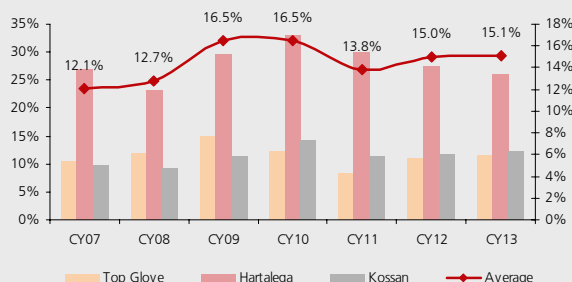
Source: DBS Vickers

	Price RM	Mkt Cap US\$m	Target Price RM	Performance (%)		Rating
				3 mth	12 mth	
Top Glove	4.69	959	4.80	(6.9)	(9.6)	HOLD
Hartalega Holdings	7.80	942	7.70	8.5	36.8	HOLD
Kossan Rubber	3.25	343	3.30	(7.1)	0.6	HOLD

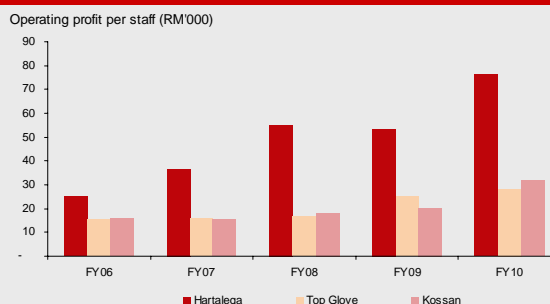
Minimum wage sensitivity analysis (RM900 per month)

	Workforce (no. of staff)	% affected by minimum wage	% to total production costs	(Based on RM900) Additional salary costs (RMm)	Impact on salary	Impact on profit
Top Glove	10,900	70%	9%	39	+22%	-19%
Kossan	5,000	80%	8%	18	+17%	-13%
Hartalega	2,900	75%	8%	10	+17%	-5%

EBIT margin trends



Hartalega has the highest operating profit per staff



Source: Companies, DBS Vickers


Peer comparison

Company	Share Price (RM)	Market Cap (US\$m)	PE (x) CY11	PE (x) CY12	PE (x) CY13	P/BV (x)	Div Yield (%)	ROE (%)	ROA (%)
Top Glove	4.69	949	21.4	15.3	13.5	2.4	2.8	10.2	10.5
Hartalega	7.80	932	14.2	13.2	11.8	4.6	3.3	36.3	36.6
Supermax	1.89	421	9.5	8.7	7.5	1.4	2.8	19.3	15.5
Kossan Rubber	3.25	340	11.4	8.8	7.5	1.7	2.7	20.4	13.0
Latexx Partners	1.41	103	5.9	5.0	4.4	1.3	3.4	16.7	na
Adventa	1.43	71	30.3	9.9	7.3	1.0	5.2	8.7	4.6
Simple Average			15.5	10.2	8.7	2.1	3.4	18.6	16.0

Prices as of 30 April 2012

Source: Bloomberg, DBS Vickers

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