Company Focus
Hartalega Holdings

Bloomberg: HART MK EQUITY | Reuters: HTHB.KL

Malaysia Equity Research PP 11272/04/2012(029344) 16 Jun 2011

BUY RM5.59 KLCI : 1,556.19

(Initiate Coverage)
Price Target : 12-Month RM 6.90
Reason for Report : Initiate coverage
Potential Catalyst: Robust healthcare spending, higher demand for nitrile gloves and M&A interest could rerate the stock

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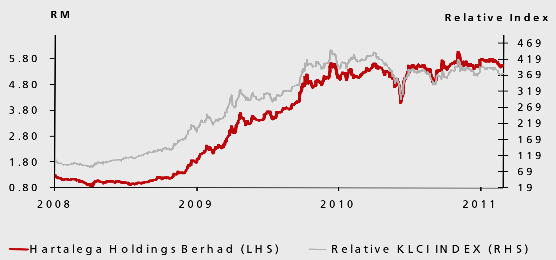
Price Relative



Forecasts and Valuation

FY Mar (RM m)	2011A	2012F	2013F	2014F
Turnover	735	941	1,049	1,223
EBITDA	266	286	322	378
Pre-tax Profit	243	263	291	339
Net Profit	190	202	224	261
Net Pft (Pre Ex.)	190	202	224	261
EPS (sen)	52.3	55.6	61.7	71.9
EPS Pre Ex. (sen)	52.3	55.6	61.7	71.9
EPS Gth Pre Ex (%)	33	6	11	17
Diluted EPS (sen)	52.3	55.6	61.7	71.9
Net DPS (sen)	21.0	21.1	23.4	27.3
BV Per Share (sen)	136.0	170.5	208.7	253.3
PE (X)	10.7	10.1	9.1	7.8
PE Pre Ex. (X)	10.7	10.1	9.1	7.8
P/Cash Flow (X)	9.7	9.1	8.0	6.8
EV/EBITDA (X)	7.4	6.6	5.7	4.5
Net Div Yield (%)	3.8	3.8	4.2	4.9
P/Book Value (X)	4.1	3.3	2.7	2.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	44.8	36.3	32.5	31.1
Consensus EPS (sen):		57.8	65.9	88.2
Other Broker Recs:		B: 8	S: 0	H: 2

ICB Industry : Health Care
ICB Sector: Health Care Equipment & Servic
Principal Business: Latex examination gloves, nitrile gloves and technical rubber products manufacturer

Source of all data: Company, DBS Vickers, Bloomberg

Nitrile gloves outpacing latex

- **Strong demand for nitrile gloves as latex prices remained high**
- **Attractive valuation for the largest nitrile glove maker with highest ROE and margins**
- **Buy for 23% upside to our RM6.90 TP**

Unrivalled dominance in nitrile gloves. Hartalega is currently the largest nitrile glove maker in the world with 9.6 bn pieces annual production capacity or 6% market share. It is known to be the most efficient glove maker with first class product and engineering innovations, which has allowed it to reap superior operating margins (28% vs 16% industry average) and ROE (36% vs 22% industry average). Future expansion will be supported by its strong balance sheet (RM78m net cash or 21 sen per share). Hartalega is building Factory 6 to raise capacity to 13 bn pieces (+42%) over the next two years. Although nitrile costs had risen in the past six months, nitrile gloves remained relatively cheaper than latex gloves due to the persistently high latex costs. This pricing gap would continue to create strong demand for nitrile gloves. Hartalega's FY11 (FYE Mar) net profit of RM190m (+33% yoy) has closed its gap with Top Glove.

Attractive valuation. As the industry continues to consolidate, Hartalega is a compelling M&A target given its niche in product and engineering innovation, higher-than-industry operating margins and ROE. And given its most attractive ROE-PE multiple matrix, Hartalega could set a new valuation benchmark.

BUY; RM6.90 TP is pegged to 12x CY12 EPS or 10% discount to our 13x target PE for Top Glove. We forecast Hartalega's net profit could surpass RM200m in FYMar12F and there is potential for rerating, premised on Top Glove's 16x PE when it posted RM245m net profit in FYAug10. Key catalysts are robust healthcare spending, higher demand for nitrile gloves and M&A interests.

At A Glance

Issued Capital (m shrs)	364
Mkt. Cap (RMm/US$m)	2,032 / 672
Major Shareholders	
Hartalega Industries (%)	50.6
Budi Tenggara (%)	5.1
Free Float (%)	40.3
Avg. Daily Vol.('000)	266

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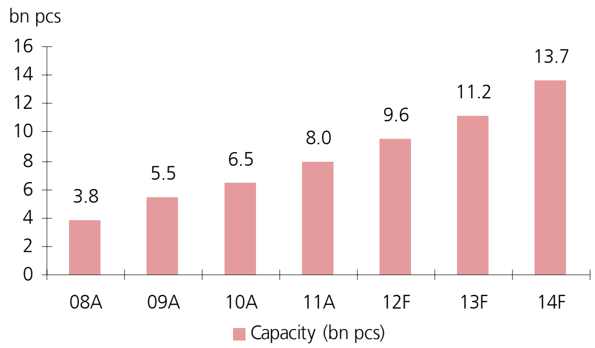
The Business Model

Hartalega has over 20 years of track record, and has risen up the ranks to become the leader in the global nitrile glove market. It is also known as the most efficient glove maker with superior product innovation and automation technology in its production process. Hartalega was listed on the Main Board of Bursa Malaysia in April 2008. The IPO price was RM1.80 per share, based on 11x FY08 EPS or 3.6x FY08 BVPS.

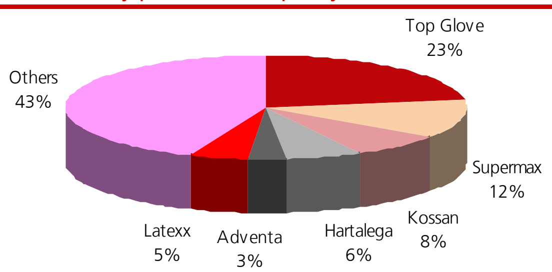
World's largest nitrile glove maker. Hartalega is currently the largest producer of nitrile gloves in the world with annual production capacity of 9.6 billion pieces, which it plans to increase to 13 billion pieces by 2013. It operates five factories with a total of 43 production lines. All its factories are located on a single site in Batang Berjuntai, Selangor, that spans 37 acres. It plans to construct Factory 6 in 1QFY12 and targets to complete that in FY14.

Capacity: 2-year CAGR of 20%



Source: Company

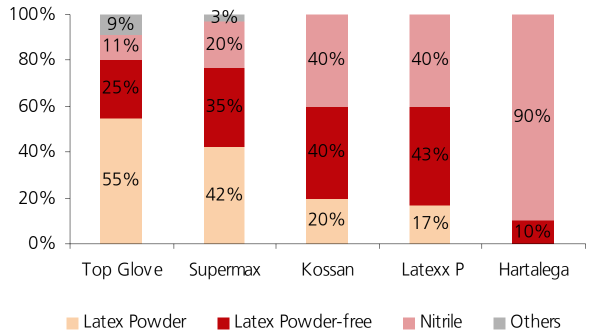
Market share by production capacity



Source: DBS Vickers (estimated based on global demand of 150bn pieces)

Niche player. Hartalega's current 9.6 billion pieces capacity is equivalent to 6% market share, the fourth largest (overall) glove producer after Top Glove, Supermax and Kossan. Currently, 90% of its capacity or 8.6 billion pieces is allocated for nitrile gloves, while the rest are for powder-free latex gloves. Its average utilisation rate is 90%. The gloves are mainly sold to the healthcare and laboratory industry.

The largest nitrile glove maker

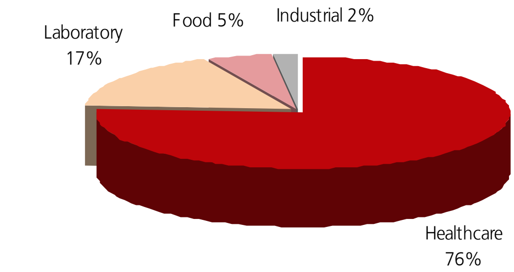


Source: Companies, DBS Vickers

Nitrile gloves is the solution to protein allergy. Nitrile gloves are made from synthetic rubber, and are latex and protein free. Given rising awareness of protein allergy issues among healthcare practitioners, nitrile gloves are slowly gaining prominence in the medical industry.

End users are not price-sensitive. Previously, nitrile gloves were more expensive than latex gloves, with an average pricing gap of USD5 per box. But since late 2010, prices of powder-free latex gloves have surpassed nitrile gloves due to higher latex costs. The current average selling price (ASP) for nitrile gloves is USD34-35 per box (1,000 pieces), whereas a box of powder-free latex gloves would cost USD38-40. Like other glove manufacturers, Hartalega is able to pass on costs to customers because end-users are not sensitive to increases in glove prices because they are an insignificant cost item relative to total medical costs. A pair of nitrile gloves costs less than 20 cents (based on USD35 per box).

Resilient demand from healthcare supporting growth

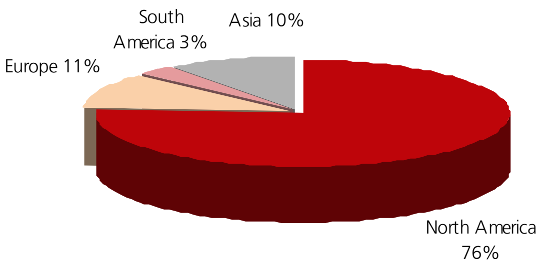


Source: Company

Backed by reputable MNC customers. Microflex Corporation and Medline Industries are Hartalega's main customers, accounting for c.50% of its total sales. Hartalega has established strong business relationships with Microflex Corporation (over 20 years) and Medline (five years). In terms of geographical breakdown, the US and Europe markets remain its top export destinations at 76% and 11% of total sales, respectively. Hartalega currently has 137 customers, and the number is growing.

Good paymasters. The average receivable period is two months, which is in line with Hartalega's credit terms.

More than 80% are sold to US and Europe

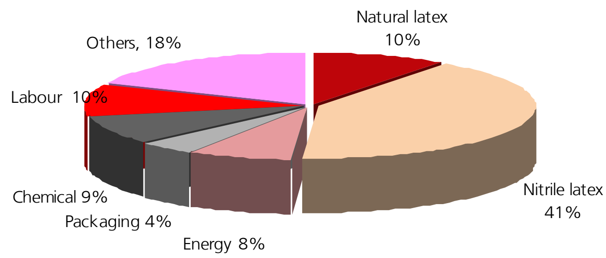


Source: Company

Cost Structure

Able to weather rising costs. Hartalega's major cost components are nitrile latex and natural latex. It has proven its ability to weather rising costs during periods of high latex and crude prices, and this is testimony to its competitive cost structure and superior product innovation. EBIT margin for Mar-11 quarter rose to 35% (from 33% in Dec-10) despite higher raw material costs (nitrile latex rose by approximately 10% qoq in Mar-11).

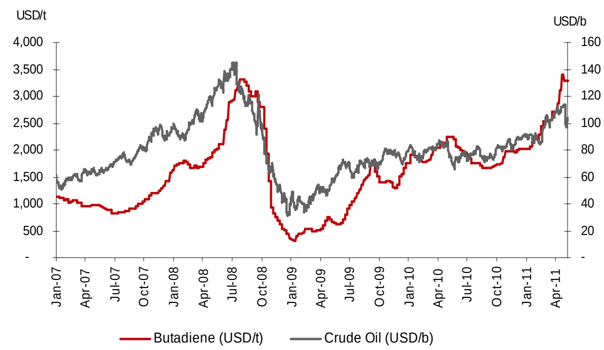
Cost breakdown



Source: Company

Crude oil, butadiene and natural latex prices were high…
Nitrile latex is a mixture of nitrile butadiene, acrylonitrile and other chemical compounds. Butadiene is a by-product of crude oil and hence, butadiene prices track crude prices closely (see chart below). Currently the average cost of nitrile latex is USD1.80 per kg (for Jun delivery) against average of USD1.30 in 2010. Meanwhile, natural latex prices remain high in 2011, peaking at RM10.93 per kg (or USD3.65) in Apr-11.

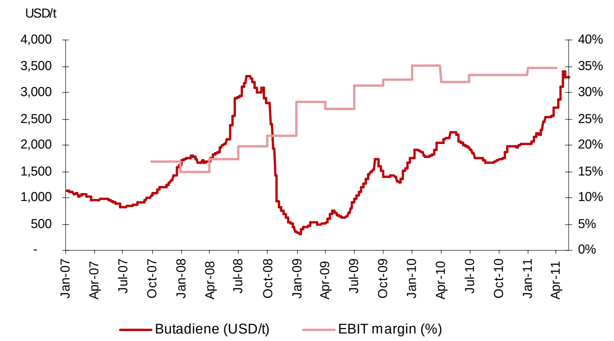
Butadiene vs crude oil price



Source: Bloomberg, Company

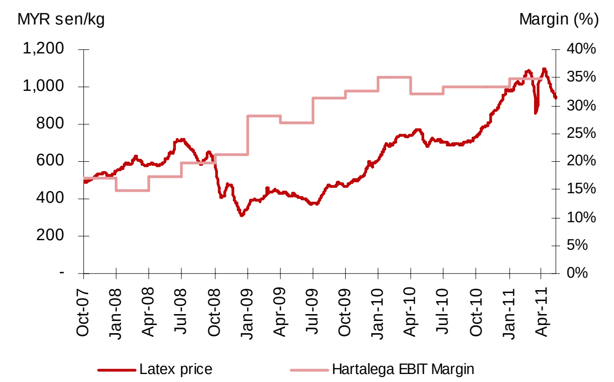
… but operating margins remain resilient. Hartalega's operating margins was resilient despite rising raw material costs because it was able to pass on the higher costs to customers. We imputed nitrile costs of RM4.70 per kg (or USD1.60 per kg) in our FY12-14 forecasts. Our sensitivity analysis shows that every 5% increase in nitrile costs would reduce net profit by 6%, assuming Hartalega absorbs the increased costs.

Steady operating margins vs rising butadiene prices



Source: Bloomberg, Company, DBS Vickers

Steady operating margin vs rising latex prices



Source: Bloomberg, Company, DBS Vickers

Steady supply of nitrile latex. Hartalega mainly sources nitrile latex from Japan and Korea. We understand Japanese supplies have been consistent. In any case, we believe any shortfall from Japan can be substituted by other suppliers (local and abroad). We estimate Hartalega's nitrile latex requirement for FY11 is 80,000 tonnes at 80% utilisation.

Malaysia houses two of the world's largest nitrile latex producers, namely PolymerLatex and Synthomer. PolymerLatex operates in Pasir Gudang, Johor and has 100,000 tonnes annual capacity, while Synthomer is located in Kluang, Johor, with 130,000 tonnes annual capacity. Both are subsidiaries of Yule Catto, a 19%-owned unit of Kuala Lumpur Kepong Bhd. We understand Yule Catto plans to build another plant in Asia in view of rising demand for nitrile latex, particularly in the glove industry.

Margins resilient despite competition. The persistent high natural latex prices have placed nitrile gloves in the spotlight as the cheaper alternative to latex gloves. Since late 2010, manufacturers have been allocating more capacities to produce nitrile gloves because of more lucrative margins. Given the additional nitrile capacities coming on stream, we expect more price competition. But so far, Hartalega has been able to preserve its market share and remain competitive in costs and pricing. In the Mar-11 quarter, Hartalega's operating margins improved to 35% (from 33%) on the back of 2% qoq growth in revenue.

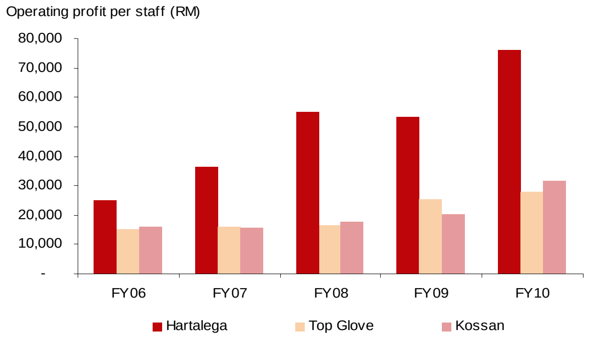
Defensive margins led by strong efficiency and innovation. Hartalega has first mover advantage in nitrile glove, which allows it to defend its forte despite rising competition. Some of its "firsts" in the market are as follows:

- Hartalega, together with Microflex, has successfully developed and commercialised a range of nitrile gloves that replicates the natural elastic properties of natural rubber gloves in 2005. Microflex subsequently obtained the patent and Hartalega was granted exclusive rights to make and sell the products;

- In-house inventions such as (i) double former dipping line with unrivalled efficiency of 30,000 pieces per hour vs industry average of 12,000-18,000 pieces per hour; (ii) robotic glove stripping system (a proprietary technology since 1995), and (iii) glove puller and stacker system at above 30,000 pieces per hour.

Hartalega's defensive margins are largely efficiency and innovation driven. It has the highest operating profit per staff in the industry. We do not discount the possibility of other glove makers stepping up efficiency and innovation, but we believe it will take time to achieve Hartalega's levels given the current disparity. With the efficient production process and innovative technology, we believe it can weather rising costs in periods of high latex and crude prices.

Highest operating profit per staff



Source: Company, DBS Vickers

Higher energy costs. Energy costs account for c.8% of Hartalega's total production cost. Effective Jun-11, the government has raised gas price to RM16.07 per mmbtu (+7%) from RM15 per mmbtu, and there will be 8-19% increase in gas price every 6 months until 2015. At the same time, electricity tariff rate was raised by 8-10%. The hike in energy prices were expected as we think it makes sense to gradually reduce the subsidy for sustainability and competitiveness reasons. The way forward is to remain innovative in the production process - a strength that is displayed by Hartalega. In any case, Hartalega could pass on cost increases to customers, and any negative impact to earnings should be temporary.

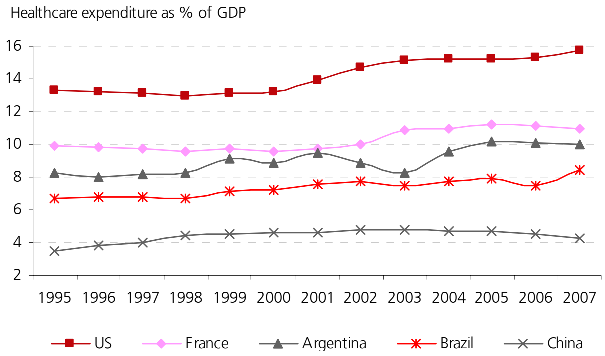
The more pressing issue faced by glove manufacturers is limited new gas supply, which makes expansion difficult. Nevertheless, we understand Hartalega has secured the required natural gas supply for Factory 6, which will be built adjacent to its existing factories.

Biomass energy as back-up. Hartalega also uses biomass fuel, but that is less than 20% of its total energy consumption currently. The constraint is that it takes 9-12 months to build, test and commission a biomass boiler, as opposed to under 6 months to connect natural gas pipes to the factory. As such, biomass will only be a backup fuel source in the event of insufficient natural gas supply.

Growth Prospects

Steady demand underpinned by robust healthcare spending. The use of medical gloves is expected to remain resilient due to stringent safety and hygiene requirements in developed nations. In the US, healthcare expenditure had risen from 13% of GDP in 1995 to 16% in 2007. As such, glove demand should be sustainable over the long term. Some Latin American countries have also reported increasing healthcare expenditure as a percentage of GDP over the past ten years. For example, we note a steady rise in Brazil (from 6.7% to 8.4%) and Argentina (from 8.3% to 10.1%). We expect other developing countries, such as China and India, to eventually pick up this trend and increase the use of rubber gloves.

Healthcare expenditure as a percentage of GDP

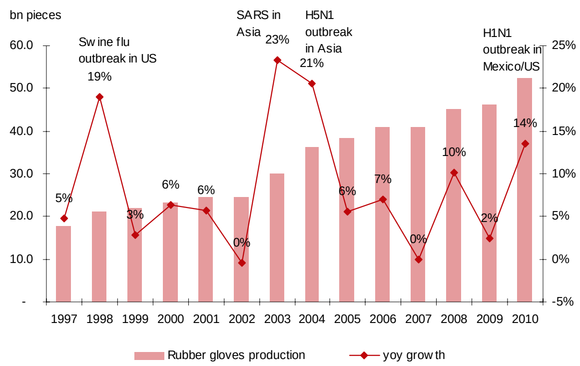


Source: World Health Organisation

Disease outbreaks are catalysts for demand. Flu and disease outbreaks in the recent two decades have raised awareness and new demand for gloves in the medical industry (see chart below). The practice of using gloves as a protective barrier is usually continued once started. Hence, the new demand created is sustainable, and there are vast opportunities to grow glove sales in emerging nations.

Based on the latest data from Bank Negara, Malaysia's rubber gloves production for 1Q 2011 was 13.6bn pieces. Annualising the 1Q 2011's production numbers, we are looking at 54.5bn pieces for the full year. This translates to 4% annual growth for 2011. We think there could be further upside in our estimates as we expect more aggressive restocking activities once latex prices ease.

Malaysia rubber glove production



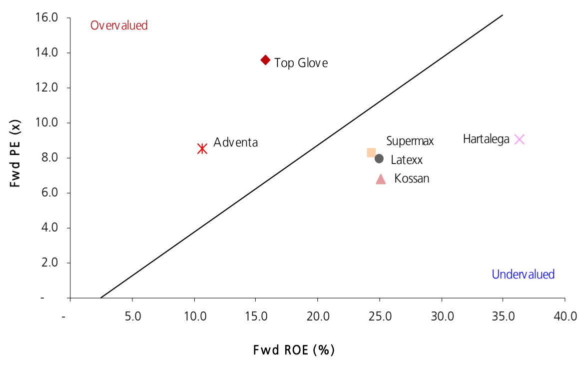
Source: Bank Negara Statistics, DBS Vickers

Attractive M&A target, with new valuation benchmark. The trend towards a balanced mix of nitrile and latex gloves, or simply the need to create a larger presence, could trigger the next round of consolidation in the glove sector. We understand several private equity firms are interested to acquire and consolidate first and second tier glove makers to create size and enhance value. The potential M&As could lift the sector's valuation, in our opinion.

In Jan-11, private equity firm Navis Asia offered to acquire 100% stake in Latexx Partners for RM852m (or RM3.10 per share), implying 2.8x BV or 10x FY10 EPS. However, the deal fell through subsequently, as both parties could not agree on the terms of settlement. Subsequent to that, YTY Industries proposed a merger with Latex Partners, which involves the sale of YTY Industries' subsidiaries for RM1.25bn (initial offer was RM1.37bn). This translates into 10.4x PE multiple (based on YTY Industries' FY11 net profit of RM120m).

We think Hartalega could be a compelling M&A target given its niche in product and engineering innovation in nitrile gloves, sturdy operating margins (28% vs 16% industry average) and superior ROE (36% vs 22% industry average). In our opinion, Hartalega should fetch higher valuations as it has the most attractive ROE-PE multiple matrix in the sector.

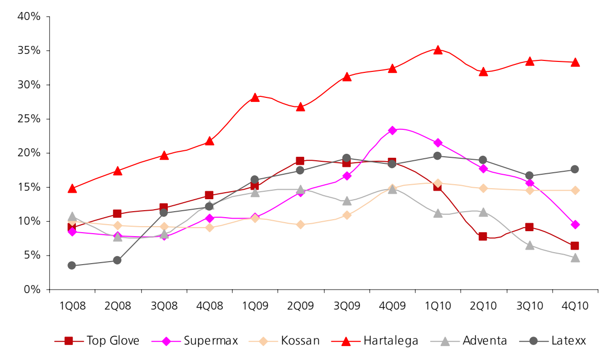
Most attractive ROE-PE matrix



Source: Bloomberg, Companies, DBS Vickers

Most efficient glove maker. Hartalega has displayed a distinct quality in product and engineering innovations, making it the most efficient glove maker in the world. It has an excellent track record of superior operating margins relative to peers (see following chart).

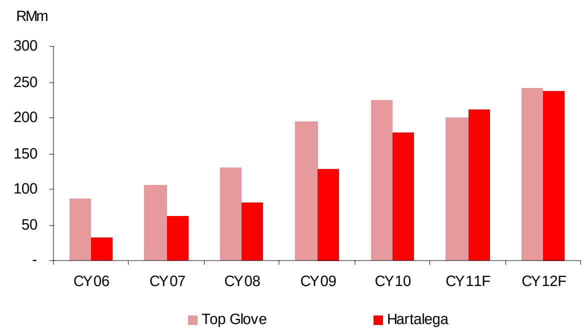
Highest operating margins among peers



Source: Companies, DBS Vickers

Profitability is moving up the ranks. Over the last five years (FY06-11), Hartalega's net profit had been expanding at an astounding 59% CAGR. Going forward, we estimate its net profit will expand at 3-year CAGR (FY11-14F) of 11%. Hartalega's FY11 (FYE Mar) net profit of RM190m (+33% yoy) has closed its gap with Top Glove in terms of earnings. The pricing gap between latex and nitrile glove currently would continue to create strong demand for nitrile gloves.

Net profit: Hartalega closing the gap with Top Glove



Source: Companies, DBS Vickers

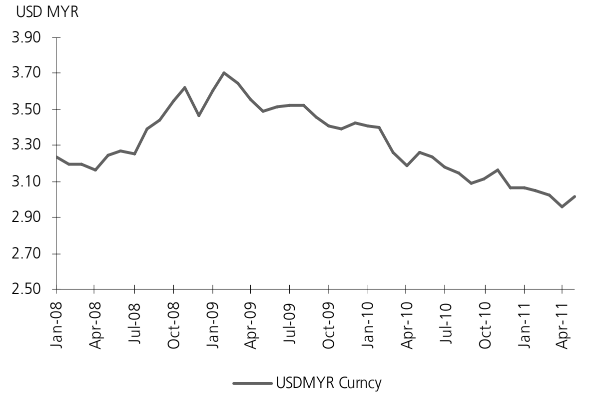
Future expansion is supported by strong balance sheet. At end Mar-11, Hartalega was in a net cash position (RM78m or 21 sen per share). Cash and cash equivalent stood at RM117m, while total borrowings were RM39m. Premised on the strong cashflows, Hartalega is poised for further expansion. It plans to build Factory 6 with 2.5 billion pieces annual capacity that will cost c.RM170m. The production lines will be commissioned progressively, with the first line expected to commence in early 2012. We understand there will be further improvements at Factory 6 and the efficiency could exceed Factory 5, which Hartalega claims is running at 35,000 pieces per hour vs industry average of 18,000 pieces.

Key Risks

Volatile crude oil and latex prices. The key risks to earnings are rising crude oil and latex prices, which would raise the costs of nitrile and natural latex, and consequently, squeeze margins. The price of butadiene (a component of nitrile latex) tracks crude oil prices closely. Meanwhile, the price of natural latex is largely driven by (i) rubber supply (harvest is seasonal), and (ii) rubber demand trends in the automobile, electronic & electrical, industrial and construction industries.

Weakening USD against Ringgit. This could reduce the value of Hartalega's exports and profits in Ringgit. Hartalega's hedging policy (for USD currency) is aligned with its receivables, which is approximately two to three months.

Weakening USD against Ringgit



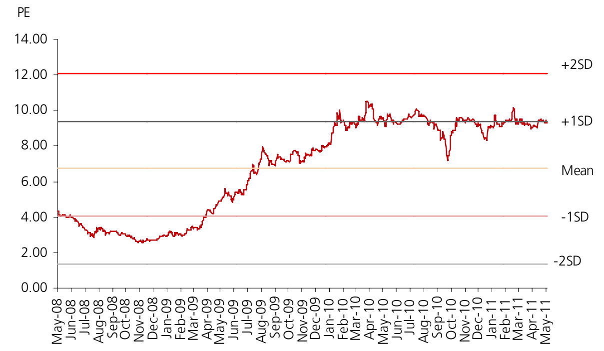
Source: Bloomberg

Valuation

Initiate coverage with Buy rating and RM6.90 target price. Our target price is pegged to 12x CY12 EPS, which is 10% discount to Top Glove's valuation. We estimate Hartalega's earnings growth will surpass the industry average in the next two years. Our estimated 11% (3-year) earnings CAGR for Hartalega is higher than the industry average of 9%. The persistent high latex prices, coupled with more lucrative margins for nitrile gloves, have created remarkable demand for nitrile gloves.

Top Glove's valuation peaked at an average PE multiple of 16x when it delivered net profit of RM245m for FYAug10. For Hartalega, we estimate its net profit could surpass the RM200m mark in FYMar12. Based on the valuation benchmark set by Top Glove, there could be further valuation upside for Hartalega.

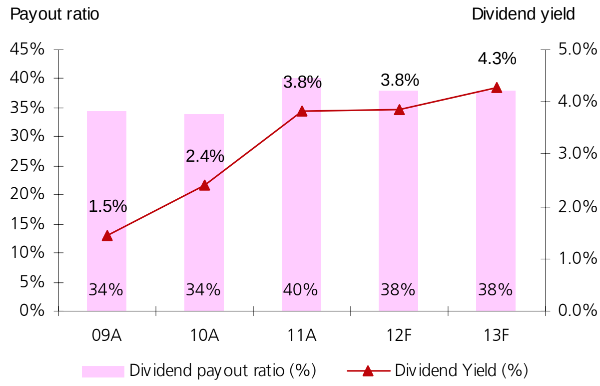
Hartalega: 1-year rolling forward PBV band



Source: Bloomberg

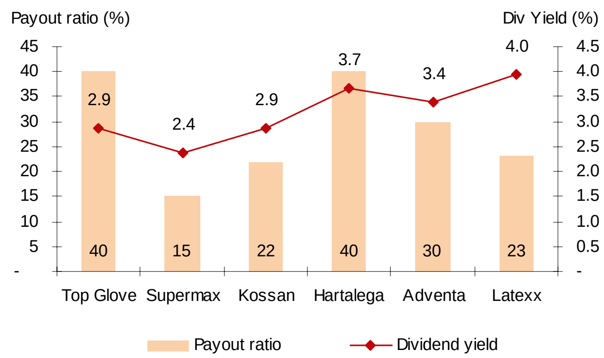
Expect 35-40% dividend payout. Hartalega does not have a formal dividend policy. For FY11, it declared 21 sen DPS, which translates into 40% payout. We have conservatively imputed 21 sen DPS for FY12F, which is equivalent to 38% payout.

Hartalega: Dividend payout ratio trend



Source: Companies, Bloomberg, DBS Vickers

Hartalega offers one of the highest payout ratios



Source: Companies, Bloomberg, DBS Vickers

Operating matrix for local glove manufacturers

		Revenue (RMm)		EBIT (RMm)		Net Profit (RMm)		EBIT margin		Net profit margin	
Company	FYE	FY09	FY10	FY09	FY10	FY09	FY10	FY09	FY10	FY09	FY10
Top Glove	Aug	1,529	2,079	229	307	169	245	15.0%	14.7%	11.1%	11.8%
Supermax	Dec	815	923	132	148	130	168	16.3%	16.1%	15.9%	18.2%
Kossan Rubber	Dec	837	1,048	97	156	67	119	11.5%	14.9%	8.0%	11.4%
Hartalega*	Mar	572	735	180	246	143	190	31.5%	33.4%	25.0%	25.9%
Adventa	Oct	283	336	39	36	17	36	13.8%	10.8%	6.0%	10.7%
Latexx	Dec	328	497	59	91	52	70	17.8%	18.2%	15.9%	14.1%

** Refers to FY10 and FY11 as Hartalega's FYE is March.*
Source: Bloomberg, DBS Vickers

Peer comparison

Company	Share Price (RM)	Market Cap (US$m)	Average daily trading value (US$m)	PE (x) CY10	PE (x) CY11	PE (x) CY12	P/BV CY11(x)	Div Yield (%)	ROE (%)	ROA (%)
Top Glove	5.26	1,072.8	3.03	15.6	19.3	13.5	2.8	2.6	12	12
Hartalega	5.59	670.5	0.83	11.4	10.2	9.3	4.3	3.8	36	37
Supermax	3.90	437.4	2.57	8.0	9.4	8.4	1.6	2.2	24	20
Kossan Rubber	3.19	336.3	0.68	8.6	8.5	7.0	1.9	2.9	25	18
Latexx Partners	2.23	163.3	0.77	6.8	8.1	7.4	2.0	3.6	25	19
Adventa	2.07	104.3	0.27	9.0	11.2	8.4	1.3	3.5	11	6
Simple Average				9.9	11.1	9.0	2.3	3.1	22	19

Source: Bloomberg, DBS Vickers

ROE decomposition

	Operating profit margin	x	Asset Turnover	-	Interest expense rate	x	Equity Multiplier	x	Taxes and others	=	ROE
Top Glove	9.0%		1.32		0.000		1.29		0.76		12%
Hartalega	28.2%		1.32		0.004		1.31		0.75		36%
Supermax	14.3%		0.87		0.014		1.62		1.35		24%
Kossan Rubber	14.9%		1.43		0.009		1.71		0.70		25%
Latexx Partners	16.7%		1.15		0.011		1.79		0.74		24%
Adventa	11.0%		1.09		0.016		1.54		0.70		11%

Source: Bloomberg, Companies, DBS Vickers

Key Management Team

Management	Current position	Previous experience and current role
Kuan Kam Hon @ Kwan Kam Onn (Appointed in 2007, aged 63)	Executive Chairman, Managing Director	Hartalega was founded by Kuan Kam Hon @ Kwan Kam Onn, who is currently the executive chairman and managing director of the Group. Mr Kuan is primarily responsible for the overall business, strategic planning and entire operations of the Group, including research and development. He began his career in the building and construction sector in 1969 under Kuan Yuen & Sons Company. In 1978, he started Timol Weaving Sdn Bhd before moving on to form Hartalega.
Abdul Hamid bin Sh Mohamed (Appointed in 2007)	Independent Non-Executive Director	He held diverse roles throughout his career and has experience in strategy, corporate finance, business transformation, finance and administration, treasury, external affairs and public relations.
Dato' Mohamed Zakri bin Abdul Rashid (Appointed in 2007)	Independent Non-Executive Director	He served the Government in the Ministry of Transport, Ministry of Finance and the Prime Minister's Department for more than 30 years. Currently, he sits on the company's Audit Committee.
Sannusi bin Ngah (Appointed in 2007)	Non-Independent Non-Executive Director	Throughout his years, he has been involved in various corporate advisory exercises ranging from initial public offerings to corporate restructuring.
Chuah Phaik Sim (Appointed in 2007)	Independent Non-Executive Director	She has experience in external audits, restructuring, as well as initial public offering and valuation exercises. Currently, she remains active in providing corporate advisory and consultancy services.
Liew Ben Poh (Appointed in 2010)	Non-Independent Non-Executive Director	He has vast knowledge of the latex glove industry and was originally an Executive Director in Hartalega before he was re-designated after retiring from his post as Sales and Marketing Director.
Kuan Mun Leong (Appointed in 2007)	Non-Independent Executive Director	He graduated from Monash University, Australia with a Bachelor's Degree in Mechanical Engineering and later obtained a Masters in Business Administration (MBA) from University of Strathclyde, Scotland. He began his career in the industrial boiler sector before becoming an Executive Director as well as Deputy Managing Director, assisting the Managing Director in the business operations of Hartalega.
Kuan Mun Keng (Appointed in 2008)	Non-Independent Executive Director	He graduated with a Bachelor's Degree in Business (Accounting) and a Bachelor's Degree in Computing from Monash University, Australia. He is also a Certified Practising Accountant with CPA Australia. Upon graduation, he joined Kassim Chan Business Services as an Analyst in the Information Technology Consultation Division before joining Hartalega. Presently, he is the Sales and Marketing Director of Hartalega and is also responsible for the Group's Corporate Finance.

Source: Company Annual Report 2010

Key Assumptions

FY Mar	2009A	2010A	2011A	2012F	2013F	2014F
Capacity (bln pcs)	5.5	6.5	8.0	9.6	11.2	13.7
Utilisation (%)	80.0	80.0	80.0	80.0	80.0	80.0
Nitrile price (RM/kg)	3.3	3.6	3.5	4.7	4.7	4.7
Latex price (RM/kg)	4.3	6.5	8.2	8.9	8.6	8.2

Sensitivity Analysis

	2011
Nitrile costs +/- 1%	Net Profit +/- 2%
Energy costs +/- 1%	Net Profit +/-0.2 %

We assume capacity would grow by 17%-22% over FY12-14F, driven by progressive commissioning of Factory 6 and upgrading of old production lines.

We assumed nitrile latex (which comprise c.40% of total production costs) to rise to RM4.70/kg in FY12F and would stay flat subsequently.

Segmental Breakdown

FY Mar	2009A	2010A	2011A	2012F	2013F	2014F
Revenues (RM m)						
North America	354	427	538	699	752	857
South America	0	15	19	23	29	36
Asia	36	43	56	73	99	133
Europe	41	68	95	114	131	151
Others	12	19	26	32	38	46
Total	443	572	735	941	1,049	1,223
Revenues breakdown (%)						
North America	80%	75%	73%	74%	72%	70%
South America	0%	3%	3%	2%	3%	3%
Asia	8%	8%	8%	8%	9%	11%
Europe	9%	12%	13%	12%	13%	12%
Others	3%	3%	4%	3%	4%	4%
Total	100%	100%	100%	100%	100%	100%

North America and Europe remain Hartalega's key export destinations at a combined c.82% of total sales.

Hartalega is also working to expand its presence in Asia to capture the vast growth potential in this region.

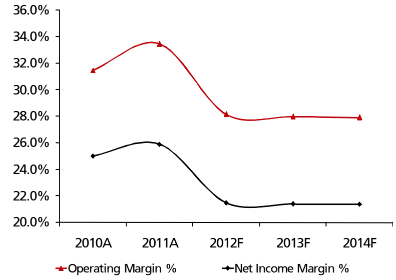
Source: Company, DBS Vickers

Income Statement (RM m)

FY Mar	2009A	2010A	2011A	2012F	2013F	2014F
Revenue	443	572	735	941	1,049	1,223
Cost of Goods Sold	(333)	(364)	(498)	(685)	(764)	(890)
Gross Profit	110	208	237	256	285	333
Other Opng (Exp)/Inc	(12)	(28)	9	9	9	9
Operating Profit	98	180	246	265	293	341
Other Non Opg (Exp)/Inc	0	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0	0
Net Interest (Exp)/Inc	(2)	(2)	(2)	(2)	(2)	(2)
Exceptional Gain/(Loss)	0	0	0	0	0	0
Pre-tax Profit	95	178	243	263	291	339
Tax	(11)	(35)	(53)	(60)	(67)	(78)
Minority Interest	0	0	0	0	0	0
Preference Dividend	0	0	0	0	0	0
Net Profit	85	143	190	202	224	261
Net Profit before Except.	85	143	190	202	224	261
EBITDA	107	195	266	286	322	378
Growth						
Revenue Gth (%)	72.1	29.0	28.5	28.1	11.5	16.6
EBITDA Gth (%)	24.7	81.9	35.9	7.6	12.7	17.4
Opg Profit Gth (%)	N/A	83.7	36.6	7.8	10.7	16.3
Net Profit Gth (%)	21.5	69.1	33.1	6.3	10.9	16.6
Margins & Ratio						
Gross Margins (%)	24.9	36.4	32.3	27.2	27.1	27.2
Opg Profit Margin (%)	22.1	31.5	33.4	28.2	28.0	27.9
Net Profit Margin (%)	19.1	25.0	25.9	21.5	21.4	21.4
ROAE (%)	39.0	47.0	44.8	36.3	32.5	31.1
ROA (%)	26.2	33.5	34.3	27.9	25.2	24.8
ROCE (%)	30.1	38.1	38.7	32.4	29.8	29.1
Div Payout Ratio (%)	34.4	33.9	40.1	38.0	38.0	38.0
Net Interest Cover (x)	40.3	85.6	99.7	110.8	140.8	192.0

Source: Company, DBS Vickers

Margins Trend



We forecast net profit to grow at 3-year CAGR (FY11-14F) of 11% and revenue at 19%, with stronger growth visible in FY14F when Factory 6 is fully commissioned

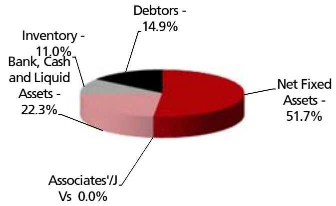
We expect gross margins would fall as Hartalega pass on higher nitrile costs to customers. Based on our assumption, nitrile latex would rise to RM4.70/kg in FY12F (from RM3.50 in FY11) and would stay flat subsequently.

Balance Sheet (RM m)

FY Mar	2009A	2010A	2011A	2012F	2013F	2014F
Net Fixed Assets	246	284	349	420	483	518
Invts in Associates & JVs	0	0	0	0	0	0
Other LT Assets	0	9	0	0	0	0
Cash & ST Invts	38	75	117	181	240	344
Inventory	25	28	65	90	99	115
Debtors	66	83	94	121	135	157
Other Current Assets	0	0	6	6	6	6
Total Assets	375	479	631	818	963	1,141
ST Debt	15	14	15	15	15	15
Other Current Liab	38	55	61	127	139	158
LT Debt	43	28	24	19	14	10
Other LT Liabilities	25	28	37	37	37	37
Shareholder's Equity	254	354	494	620	759	921
Minority Interests	0	0	0	0	0	1
Total Cap. & Liab.	375	479	631	818	963	1,141
Non-Cash Wkg. Capital	52	56	105	89	101	120
Net Cash/(Debt)	(19)	33	78	147	211	319
Debtors Turn (avg days)	42.9	47.4	44.0	41.7	44.4	43.5
Creditors Turn (avg days)	37.1	42.3	30.0	22.2	24.5	24.0
Inventory Turn (avg days)	26.3	27.6	35.6	42.5	46.9	45.9
Asset Turnover (x)	1.4	1.3	1.3	1.3	1.2	1.2
Current Ratio (x)	2.4	2.7	3.7	2.8	3.1	3.6
Quick Ratio (x)	2.0	2.3	2.8	2.1	2.4	2.9
Net Debt/Equity (X)	0.1	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	0.1	(0.1)	(0.2)	(0.2)	(0.3)	(0.3)
Capex to Debt (%)	30.8	162.0	208.7	294.3	345.1	320.3
Z-Score (X)	NA	NA	NA	NA	NA	NA

Source: Company, DBS Vickers

Asset Breakdown



Hartalega has a strong balance sheet and had been in net cash position since FY10. Its strong balance sheet position will support Hartalega's future expansion plans.

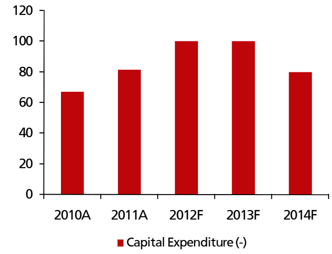
We assumed receivables and inventory turnover should remain stable at 30-60 days.

Cash Flow Statement (RM m)

FY Mar	2009A	2010A	2011A	2012F	2013F	2014F
Pre-Tax Profit	95	178	243	263	291	339
Dep. & Amort.	16	20	21	29	37	45
Tax Paid	(4)	(22)	(48)	(7)	(60)	(67)
Assoc. & JV Inc/(loss)	0	0	0	0	0	0
Chg in Wkg.Cap.	(23)	(15)	(42)	(38)	(18)	(30)
Other Operating CF	1	4	8	0	0	0
Net Operating CF	85	164	182	246	249	287
Capital Exp.(net)	(18)	(67)	(81)	(100)	(100)	(80)
Other Invts.(net)	0	0	0	0	0	0
Invts in Assoc. & JV	0	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0	0
Other Investing CF	(43)	0	0	0	0	0
Net Investing CF	(61)	(67)	(81)	(100)	(100)	(80)
Div Paid	(8)	(45)	(57)	(77)	(85)	(99)
Chg in Gross Debt	14	(15)	(2)	(5)	(5)	(4)
Capital Issues	0	0	0	0	0	0
Other Financing CF	0	0	0	0	0	0
Net Financing CF	6	(60)	(59)	(82)	(90)	(103)
Currency Adjustments	0	(1)	0	0	0	0
Chg in Cash	30	37	42	64	59	104
Opg CFPS (sen)	29.8	49.2	61.7	78.2	73.7	87.3
Free CFPS (sen)	18.6	26.6	27.8	40.2	41.1	57.0

Source: Company, DBS Vickers

Capital Expenditure



We understand Hartalega has allocated RM170-200m capex for Factory 6, which will be funded internally.

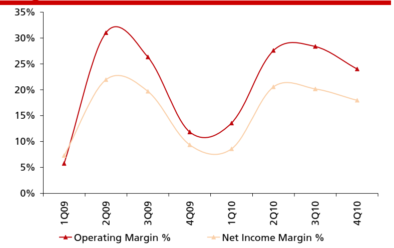
For FY11, Hartalega proposed 21sen DPS, which translate into 40% payout. In our forecasts, we conservatively assumed 38% payout ratio or 21 sen DPS.

Quarterly / Interim Income Statement (RM m)

FY Mar	3Q2010	4Q2010	1Q2011	2Q2011	3Q2011	4Q2011
Revenue	149	163	170	184	188	193
Cost of Goods Sold	(101)	(106)	(116)	(125)	(127)	(130)
Gross Profit	48	57	54	59	61	63
Other Oper. (Exp)/Inc	1	0	1	2	2	4
Operating Profit	48	57	54	62	63	67
Other Non Opg (Exp)/Inc	0	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0	0
Net Interest (Exp)/Inc	(1)	(1)	(1)	(1)	(1)	(1)
Exceptional Gain/(Loss)	0	0	0	0	0	0
Pre-tax Profit	47	57	54	61	62	66
Tax	(10)	(10)	(12)	(14)	(13)	(14)
Minority Interest	0	0	0	0	0	0
Net Profit	37	46	41	47	49	52
Net profit bef Except.	37	46	41	47	49	52
Growth						
Revenue Gth (%)	10.4	10.0	4.0	8.4	2.1	2.3
Opg Profit Gth (%)	14.8	18.9	(5.1)	13.3	1.9	6.4
Net Profit Gth (%)	12.5	24.6	(10.7)	13.6	4.5	6.5
Margins						
Gross Margins (%)	32.0	34.9	31.7	32.3	32.5	32.5
Opg Profit Margins (%)	32.5	35.1	32.0	33.4	33.4	34.7
Net Profit Margins (%)	25.1	28.4	24.4	25.6	26.2	27.2

Source: Company, DBS Vickers

Margins Trend



Driven by resilience margins at 32.5% while revenue grew 2% qoq. Utilisation rate remained stable at c.80%.

Quarterly performance has proven its resilience in margins. Its initiatives in automating processes and innovative product engineering have given it an edge over peers.

Wong Ming Tek, Head of Research

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