

**Hartalega (HOLD ↓, EPS ↔)**

INDUSTRY: OVERWEIGHT

NEWSBREAK

13 June 2013

Price Target: RM6.37 (↔)

Share Price: RM6.30

**NGC - Nurturing Growth Commitment**
**Highlights**

- In its exchange filing, Hartalega announced that its wholly-owned subsidiary, Hartalega NGC SB has entered into an agreement with Kumpulan Tanjung Balai SB to acquire 3 plots of land for a total cash consideration of RM97.0m.
- The total land areas measured up to 120 hectares is located at Mukim Labu, Daerah Sepang, Selangor.
- The objective of the land purchase is to expand its production capacities by erecting 6 manufacturing facilities leveraging on new in-house developed technologies. They will house 72 production lines (PL) which was accorded the EPP under ETP due to its high economic impact.
- The expansion will be spread over two 4-year phases and employ about 5k workers.
  1. 2013 - 2017: 42 PL with total annual capacity of 16.5bn.
  2. 2018 - 2021: 30 PL with total annual capacity of 12.0bn.
- The land development also includes administration office, centre of excellence, learning and development centre, sports and recreation centre and staff's accommodation.
- The whole project was allocated with a budget of RM1.9bn.
- The construction layout is subject to the approvals by relevant local authorities.
- The price tag of RM97.0m which was derived based on willing-buyer willing-seller basis will be funded by internally generated funds and bank borrowings, without specifying the ratio. We are not too concern as Hartalega ended FY13 with a net cash position of RM170.3m.

**Financial Impact**
**Comments**

- Additional capacity from NGC is expected to commence production only in FY15.
- Emphasizes on human capital as the operations will be highly dependent on the skilled workforce. As mitigation measure, Hartalega has pre-employed factory workers now at 3.9k compared to a year ago at 2.9k.

**Risks**

- Delays in capacity expansion plans.
- Surge in nitrile latex prices.
- Shift in demand to natural latex gloves from nitrile gloves, if prices of natural latex fall significantly below nitrile latex.
- Depreciation of USD vs. MYR.
- Unchanged as we have factored this expansion based on previous guidance.

**Forecasts**
**Rating**
**HOLD ↓, TP: RM6.37 ↔**

- Positives – Leader in nitrile glove market; highest ROE and net profit margins; most efficient and profitable glove maker. In the event of a price war, Hartalega's earnings will be the least affected, shielded by its high profit margins.
- Negatives – Possibility of increased competition in nitrile glove market.

**Valuation**

- Since our upgrade in early May, share price has performed well, rallied by 17.4% from RM5.45 to reach all time high of RM6.40 and slightly topped our TP.
- As such, considering that there is limited upside, we downgrade our call on the equity from BUY to HOLD based on unchanged TP of RM6.37 derived based on 17.5x CY14 EPS. At this juncture, we believe that it is fairly valued.

Low Yee Huap, CFA

[yhlow@hlib.hongleong.com.my](mailto:yhlow@hlib.hongleong.com.my)

(603) 2168 1078

KLCI	1775.1
Expected share price return	1.1%
Expected dividend return	1.7%
Expected total return	2.8%

**Share price**

**Information**

Bloomberg Ticker	HART MK
Bursa Code	5168
Issued Shares (m)	734
Market cap (RM m)	4,624
3-mth avg. volume ('000)	733

Price Performance	1M	3M	12M
Absolute	9.2	31.3	61.1
Relative	10.0	21.7	43.1

**Major Shareholders**

Hartalega Industries SB	50.1%
Budi Tenggara Sdn Bhd	4.9%
BNP Paribas Singapore	7.7%

**Summary Earnings Table**

FYE Mar (RM m)	2012A	2013A	2014E	2015E
Turnover	931.1	1032.0	1288.2	1509.5
EBITDA	289.2	337.1	405.1	465.1
PBT	258.4	305.9	343.8	382.3
Net profit	201.4	234.7	268.1	298.1
EPS (sen)	27.5	32.1	34.7	37.0
Diluted EPS (sen)	25.0	31.8	33.3	37.0
P/E	25.2	19.8	18.9	17.0
BV/share (RM)	0.85	1.05	1.34	1.71
P/BV	7.4	6.0	4.7	3.7
Net DY (%)	1.7	1.7	2.7	3.0
ROE (%)	32.5	30.7	24.9	21.6
ROA (%)	26.6	25.1	20.0	18.1

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## Financial Projections

### Income statement

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
<b>Revenue</b>	<b>734.9</b>	<b>931.1</b>	<b>1032.0</b>	<b>1288.2</b>	<b>1509.5</b>
<b>EBITDA</b>	<b>270.3</b>	<b>289.2</b>	<b>337.1</b>	<b>405.1</b>	<b>465.1</b>
Dept. & Amort.	-24.9	-29.0	-31.9	-55.1	-77.1
Interest income	2.4	0.9	0.8	4.5	5.0
Interest expense	-2.5	-1.7	-0.9	-6.2	-5.7
Exceptionals	0.0	0.0	0.0	0.0	0.0
<b>PBT</b>	<b>242.8</b>	<b>258.4</b>	<b>305.9</b>	<b>343.8</b>	<b>382.3</b>
Taxation	-52.5	-57.0	-70.8	-75.6	-84.1
Minorities	0.03	0.05	-0.33	0.05	0.05
<b>Net profit</b>	<b>190.3</b>	<b>201.4</b>	<b>234.7</b>	<b>268.1</b>	<b>298.1</b>
No. of shares (m)	731.1	731.1	731.1	771.8	805.1
<b>Basic EPS (sen)</b>	<b>26.0</b>	<b>27.5</b>	<b>32.1</b>	<b>34.7</b>	<b>37.0</b>
<b>Diluted EPS (sen)</b>	<b>23.6</b>	<b>25.0</b>	<b>31.8</b>	<b>33.3</b>	<b>37.0</b>

### Balance sheet

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
Fixed assets	348.6	379.7	534.9	856.9	1029.7
Other long-term assets	0.3	0.5	7.6	0.0	0.0
Other short-term assets	3.4	0.1	0.1	0.0	0.0
<b>Working capital</b>	<b>108.5</b>	<b>154.2</b>	<b>118.5</b>	<b>213.7</b>	<b>255.1</b>
Receivables	101.0	117.1	124.7	212.5	254.1
Payables	-57.2	-60.4	-92.8	-106.2	-127.1
Inventories	64.7	97.5	86.6	107.5	128.1
<b>Net cash</b>	<b>78.0</b>	<b>138.6</b>	<b>170.3</b>	<b>47.2</b>	<b>133.9</b>
Cash	117.0	163.2	182.4	161.9	238.5
ST debt	-14.5	-12.6	-7.7	-12.6	-12.6
LT debt	-24.5	-12.1	-4.5	-102.1	-92.1
<b>Shareholder's funds</b>	<b>494.4</b>	<b>619.5</b>	<b>765.5</b>	<b>1077.0</b>	<b>1377.9</b>
Share capital	181.8	182.5	366.7	385.9	402.5
Reserves	312.7	437.0	398.9	691.1	975.4
Minorities	0.4	0.6	1.0	0.6	0.6
Other liabilities	44.0	53.0	64.8	40.2	40.2

### Assumption Metrics

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
Effective capacity (bn)	8.33	9.78	11.0	13.7	15.7
Utilisation rate (%)	80	83	85	85	85
NBR latex price (USD/kg)	1.79	1.48	1.60	1.70	1.80
NR latex price (RM/kg)	8.21	8.29	6.36	6.96	7.48

### Cashflow

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
Pretax profit	242.8	258.4	305.88	343.77	382.25
Dep. and Amort.	25.0	29.0	31.9	55.1	77.1
Changes in working cap	-40.9	-44.5	35.7	-44.8	-41.4
Net interest received/(paid)	-0.1	1.9	2.9	-1.7	-0.7
Tax paid	-47.8	-48.8	-59.2	-75.6	-84.1
Others	5.7	4.3	-0.1	1.7	0.7
<b>Operating Cash Flow</b>	<b>184.8</b>	<b>200.3</b>	<b>317.2</b>	<b>278.4</b>	<b>333.9</b>
Capex	-81.3	-60.2	-187.0	-300.0	-250.0
Others	0.3	0.1	-7.0	0.0	0.0
<b>Investing Cash Flow</b>	<b>-81.0</b>	<b>-60.1</b>	<b>-194.0</b>	<b>-300.0</b>	<b>-250.0</b>
Div paid	-56.9	-87.4	-98.8	-120.5	-135.1
Changes in borrowings	-2.5	-14.6	-12.5	-10.0	-10.0
Issuance of shares	0.3	6.9	0.0	168.5	137.9
Others	0.0	0.0	7.3	0.0	0.0
<b>Financing Cash Flow</b>	<b>-59.1</b>	<b>-95.0</b>	<b>-104.0</b>	<b>38.0</b>	<b>-7.2</b>
Net cash flow	44.7	45.2	19.2	16.4	76.6
Forex	-2.3	1.0	0.0	0.0	0.0
<b>Beginning cash</b>	<b>38.2</b>	<b>74.6</b>	<b>163.2</b>	<b>163.2</b>	<b>145.5</b>
<b>Ending cash</b>	<b>117.0</b>	<b>163.2</b>	<b>182.4</b>	<b>161.9</b>	<b>238.5</b>

### Valuation Ratios

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
EPS (sen)	26.0	27.5	32.1	34.7	37.0
Diluted EPS (sen)	23.6	25.0	31.8	33.3	37.0
P/E (x)	26.7	25.2	19.8	18.9	17.0
Net DPS (sen)	10.5	10.8	10.5	17.0	19.0
Net DY (%)	1.7	1.7	1.7	2.7	3.0
BV/share (RM)	0.68	0.85	1.05	1.34	1.71
P/BV (x)	9.3	7.4	6.0	4.7	3.7
FCF/share (sen)	14.2	19.2	17.8	-2.8	10.4
FCF yield (%)	2.2	3.0	2.8	-0.4	1.7
Market cap	4605.9	4605.9	4605.9	4862.3	5072.1
Net cash	78.0	138.6	170.3	47.2	133.9
EV	4527.9	4467.3	4435.6	4815.1	4938.2
EV/EBITDA	16.8	15.4	13.2	11.9	10.6
ROE (%)	38.5	32.5	30.7	24.9	21.6
ROA (%)	30.0	26.6	25.1	20.0	18.1

### Other Ratios

FYE 31 Mar (RMm)	2011A	2012A	2013A	2014E	2015E
<b>Growth (%)</b>					
Sales Growth	28.5	26.7	9.9	25.8	17.2
EBITDA Growth	34.5	7.0	13.9	23.0	14.8
PBT Growth	36.6	6.4	14.1	16.6	11.2
Net Profit Growth	33.2	5.8	14.2	16.6	11.2
<b>Margins (%)</b>					
EBITDA Margin	36.8	31.1	32.2	31.4	30.8
PBT Margin	33.0	27.8	28.8	26.7	25.3
Net Profit Margin	25.9	21.6	22.5	20.8	19.7

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 (Formerly known as MIMB Investment Bank Berhad)  
 Level 8, Menara HLA  
 No. 3, Jalan Kia Peng  
 50450 Kuala Lumpur  
 Tel 603 2168 1168 / 603 2710 1168  
 Fax 603 2161 3880

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<b>BUY</b>	Positive recommendation of stock under coverage. Expected absolute return of more than +10% over 12-months, with low risk of sustained downside.
<b>TRADING BUY</b>	Positive recommendation of stock not under coverage. Expected absolute return of more than +10% over 6-months. Situational or arbitrage trading opportunity.
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