

Hartalega Holdings

Buy (Unchanged)

Share price: RM5.46
Target price: RM6.80 (Unchanged)

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Description: OEM gloves manufacturer.

Information:

Ticker:	HART MK
Shares Issued (m):	364.0
Market Cap (RM m):	1,987.5
3-mth Avg Daily Volume (m):	0.26
KLCI:	1,480.46

Major Shareholders:

	%
Hartalega Industries SB	50.5
Budi Tenggara SB	5.0

Price Performance:

52-week High/Low RM6.08/RM4.85

1-mth	3-mth	6-mth	1-yr	YTD
(1.8)	(2.8)	(4.7)	(2.2)	2.2

Price Chart (RM5.46)



Dichotomy between profitability and valuation

Still growing albeit slower pace QoQ. Even with the RM9m unrealised forex loss, 1HFY12 net profit of RM101m (+14% YoY) was in line at 49% of our and consensus full-year estimates. We continue to like the stock for its nitrile glove growth story and net dividend yield of 5%. As Hartalega consistently deliver growth and convince market of its newly-gained leadership status (CY12 net profit is 56% above Top Glove's), we believe the valuation gap between Top Glove (CY12 PER 18x) and Hartalega (9x) will close. Buy with DCF-based TP of RM6.80.

Dip in volume and margins. 2QFY12 core net profit of RM55m was flattish QoQ (+17% YoY) due to: (i) volume sales being stable QoQ (-2% QoQ, +23% YoY) with minimal new capacity added in the quarter (+1% QoQ, +20% YoY); and (ii) EBIT margin contracting 2.1-ppt QoQ to 30% (-2.6-ppt YoY) as Hartalega absorbed bulk of the cost inflation (NBR cost: +13% QoQ) to ensure competitive pricing. Additionally, bottomline was impacted by a RM9m mark-to-market forex loss, bringing the total 1H net profit to RM101m (+14% YoY). A first interim dividend of 6sen/shr (2QFY11: 4sen/shr) was also declared.

Forgoing a tad of superior margins for volume. Though NBR cost has fallen sharply by 21% to USD1.70/kg from its August peak, margin may see a slight contraction in the sequential quarters as management ensures competitive pricing and defends market share, in view of the incoming capacity in the nitrile segment. Note that Hartalega still has a lot of room to play with pricing as its EBIT margin is 13-23-ppt above peers. Sequential earnings growth will come from 2 new lines at Plant 5 (by Feb '12), adding 500m capacity to its existing 9.7b pcs p.a. (+5%).

Maintain forecasts. We expect the group to meet our 9% YoY earnings growth forecast for FY12. Hartalega offers both growth (3-year net profit CAGR of 15%) and defensiveness with its net dividend yield of 5%. Our DCF-based TP of RM6.80 implies just 10.8x CY12 PER and 9x CY13, and we believe an upward re-rating is due for the stock.

Hartalega – Summary Earnings Table

FYE Mar (RM m)	2010A	2011A	2012F	2013F	2014F
Revenue	571.9	734.9	924.0	1,073.9	1,306.6
EBITDA	199.9	267.9	296.6	339.4	412.9
Recurring Net Profit	142.9	190.3	207.9	235.7	290.4
Recurring Basic EPS (Sen)	39.3	52.3	57.2	64.8	79.9
EPS growth (%)	69.1	33.1	9.2	13.4	23.2
Net DPS (Sen)	13.3	21.0	25.7	29.2	35.9
PER	13.9	10.4	9.5	8.4	6.8
EV/EBITDA (x)	9.8	7.1	6.3	5.5	4.3
Div Yield (%)	2.4	3.8	4.7	5.3	6.6
P/BV(x)	5.6	4.0	3.3	2.7	2.2
Net Gearing (%)	Cash	Cash	Cash	Cash	Cash
ROE (%)	40.3	38.5	34.2	31.9	32.3
ROA (%)	30.0	30.1	27.5	26.6	27.8
Consensus Net Profit (RM m)	-	-	209.3	235.4	269.2

Source: Maybank-IB

Hartalega: Results Summary Table

FY Mar(RM m)	Quarterly					Cumulative		
	2QFY12	2QFY11	% YoY	1QFY12	% QoQ	6MFY12	6MFY11	% YoY
Turnover	229.5	184.3	24.5	219.4	4.6	448.9	354.3	26.7
EBIT	68.4	59.8	14.4	70.1	(2.4)	138.6	113.6	22.0
Net interest exp	(0.2)	(0.4)	(39.3)	(0.2)	10.7	(0.5)	(0.4)	15.6
Unrealised forex gain/(loss)	(8.7)	1.6	n.m.	0.0	n.m.	(7.9)	1.6	n.m.
Pre-tax profit	59.6	61.0	(2.4)	70.7	(15.7)	130.2	114.8	13.5
Tax	(13.4)	(13.9)	(3.8)	(15.9)	(16.0)	(29.3)	(26.2)	11.8
Minority Interest	0.0	(0.0)	n.m.	0.0	n.m.	0.0	(0.1)	n.m.
Net profit	46.2	47.1	(2.0)	54.8	(15.7)	100.9	88.6	14.0
Net profit (ex-forex)	54.8	45.5	20.5	54.8	0.1	108.8	87.0	25.1
	2QFY12	2QFY11	+/- ppt	1QFY12	+/- ppt	6MFY12	6MFY11	+/- ppt
EBIT margin (%)	29.8	32.5	(2.6)	32.0	(2.1)	30.9	32.1	(1.2)
Tax rate (%)	22.5	22.8	(0.3)	22.5	(0.1)	22.5	22.8	(0.3)

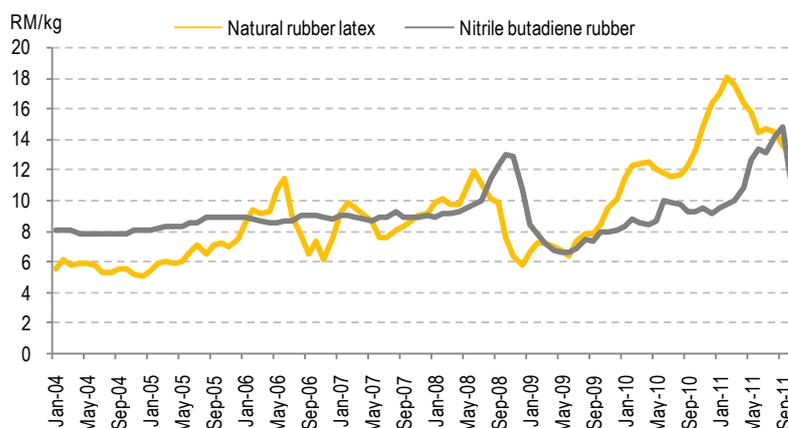
Source: Company, Maybank-IB

Hartalega: Capacity expansion (billion pieces p.a.)

Timeline	1QFY12 (Apr-Jun 2011)	4QFY12 (Jan-Mar 2012)	End-FY14
	Plants 1-5	Plant 4 (retrofit) + Plant 5 (2 new lines)	Plant 6
Total capacity	9.6	10.4	13.9
New capacity	-	+0.75	+3.5

Sources: Company, Maybank-IB

NBR-to-latex price gap: NBR is now 11% cheaper than latex



Note: NR and NBR costs are adjusted for respective rubber conversion ratios

Sources: Company, Bloomberg, Maybank-IB

Hartalega: Highest profitability player at 9x forward PER



Sources: Bloomberg, Maybank-IB

Sector comparison table: Hartalega's CY12 net profit is 56% above Top Glove, yields are also higher, yet CY12 PER valuation is 52% lower

Stock	Rec	Shr px (RM)	Mkt cap (RMm)	TP (RM)	Net profit (RM m) CY12	PER (x)		3-yr EPS CAGR (%)	Net yield (%)		P/B (x) CY11
						CY11	CY12		CY11	CY12	
Top Glove	Sell	4.24	2,618.2	3.40	21.7	17.9	16.2	2.7	3.1	2.2	4.24
Hartalega	Buy	5.41	1,966.4	6.80	9.7	8.6	15.7	4.4	5.1	3.4	5.41
Supermax *	NR	3.72	1,262.8	NR	11.3	9.5	(4.1)	2.3	2.9	1.5	3.72
Kossan	Buy	2.87	917.6	3.60	6.7	6.2	6.7	3.3	3.6	1.6	2.87
Latexx Partner *	NR	1.91	417.2	NR	6.4	6.2	2.0	4.2	4.3	NA	1.91
Average					11.1	9.7	7.3	3.4	3.8	2.2	

Source: Maybank-IB, Consensus (*)

INCOME STATEMENT (RM m)

FYE Mar	2011A	2012F	2013F	2014F
Revenue	734.9	924.0	1,073.9	1,306.6
EBITDA	267.9	296.6	339.4	412.9
Depreciation & Amortisation	(25.0)	(31.0)	(39.0)	(44.3)
Operating Profit (EBIT)	242.9	265.6	300.4	368.6
Interest (Exp)/Inc	(0.1)	0.9	1.7	4.3
Associates	0.0	0.0	0.0	0.0
One-offs	0.0	0.0	0.0	0.0
Pre-Tax Profit	242.8	266.5	302.2	372.9
Tax	(52.5)	(58.6)	(66.5)	(82.0)
Minority Interest	(0.0)	0.0	0.0	0.0
Net Profit	190.3	207.9	235.7	290.9
Recurring Net Profit	190.3	207.9	235.7	290.9
Revenue Growth %	28.5	25.7	16.2	21.7
EBITDA Growth (%)	34.0	10.7	14.4	21.7
EBIT Growth (%)	34.9	9.4	13.1	22.7
Net Profit Growth (%)	33.2	9.2	13.4	23.4
Recurring Net Profit Growth (%)	33.2	9.2	13.4	23.4
Tax Rate %	21.6	22.0	22.0	22.0

BALANCE SHEET (RM m)

FYE Mar	2011A	2012F	2013F	2014F
Fixed Assets	348.6	407.7	488.7	524.4
Other LT Assets	0.2	0.2	0.2	0.2
Cash/ST Investments	117.0	144.4	160.9	200.8
Other Current Assets	165.4	203.8	236.9	288.2
Total Assets	631.3	756.1	886.7	1,013.7
ST Debt	14.5	14.5	14.5	14.5
Other Current Liabilities	60.9	71.4	82.3	99.3
LT Debt	24.4	24.4	14.4	(35.6)
Other LT Liabilities	36.8	36.8	36.8	36.8
Minority Interest	0.4	0.4	0.4	0.4
Shareholders' Equity	494.3	608.6	738.3	898.3
Total Liabilities-Capital	631.3	756.2	886.8	1,013.7
Share Capital (m)	363.6	363.6	363.6	363.6
Net Debt/(Cash)	Cash	Cash	Cash	Cash
Working capital	108.3	136.2	158.3	192.6

CASH FLOW (RM m)

FYE Mar	2011A	2012F	2013F	2014F
Profit before taxation	242.8	266.5	302.2	372.4
Depreciation	25.0	31.0	39.0	44.3
Net interest receipts/(payments)	0.1	(0.9)	(1.7)	(3.7)
Working capital change	(41.7)	(27.9)	(22.1)	(34.3)
Cash tax paid	(47.8)	(58.6)	(66.5)	(81.9)
Others (incl'd exceptional items)	4.2	0.0	0.0	0.0
Cash flow from operations	182.5	210.1	250.8	296.7
Capex	(81.3)	(90.0)	(120.0)	(80.0)
Disposal/(purchase)	0.2	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0
Cash flow from investing	(81.1)	(90.0)	(120.0)	(80.0)
Debt raised/(repaid)	0.3	0.0	(10.0)	(20.0)
Equity raised/(repaid)	1.0	2.0	3.0	4.0
Dividends (paid)	(56.9)	(93.6)	(106.1)	(130.7)
Interest payments	(0.1)	0.9	1.7	3.7
Others	(1.0)	(2.0)	(3.0)	(4.0)
Cash flow from financing	(56.8)	(92.7)	(114.3)	(146.9)
Change in cash	44.7	27.4	16.5	69.7

RATES & RATIOS

FYE Mar	2011A	2012F	2013F	2014F
EBITDA Margin %	36.4	32.1	31.6	31.6
Op. Profit Margin %	33.1	28.8	28.0	28.2
Net Profit Margin %	25.9	22.5	21.9	22.2
ROE %	38.5	34.2	31.9	32.3
ROA %	30.1	27.5	26.6	27.8
Net Margin Ex. EI %	25.9	22.5	21.9	22.2
Dividend Cover (x)	2.5	2.2	2.2	2.2
Interest Cover (x)	77.0	86.8	112.8	249.0
Asset Turnover (x)	1.2	1.2	1.2	1.3
Asset/Debt (x)	16.2	19.4	30.6	116.2
Debtors Turn (days)	48.1	48.1	48.1	48.1
Creditors Turn (days)	26.7	26.7	26.7	26.7
Inventory Turn (days)	32.3	32.3	32.3	32.3
Net Gearing %	Cash	Cash	Cash	Cash
Debt/EBITDA (x)	0.1	0.1	0.1	0.0
Debt/Market Cap (x)	0.0	0.0	0.0	0.0

Sources: Company, Maybank IB

APPENDIX 1

Definition of Ratings

Maybank Investment Bank Research uses the following rating system:

BUY	Total return is expected to be above 10% in the next 12 months
HOLD	Total return is expected to be between -5% to 10% in the next 12 months
SELL	Total return is expected to be below -5% in the next 12 months

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Some common terms abbreviated in this report (where they appear):

Adex = Advertising Expenditure	FCF = Free Cashflow	PE = Price Earnings
BV = Book Value	FV = Fair Value	PEG = PE Ratio To Growth
CAGR = Compounded Annual Growth Rate	FY = Financial Year	PER = PE Ratio
Capex = Capital Expenditure	FYE = Financial Year End	QoQ = Quarter-On-Quarter
CY = Calendar Year	MoM = Month-On-Month	ROA = Return On Asset
DCF = Discounted Cashflow	NAV = Net Asset Value	ROE = Return On Equity
DPS = Dividend Per Share	NTA = Net Tangible Asset	ROSF = Return On Shareholders' Funds
EBIT = Earnings Before Interest And Tax	P = Price	WACC = Weighted Average Cost Of Capital
EBITDA = EBIT, Depreciation And Amortisation	P.A. = Per Annum	YoY = Year-On-Year
EPS = Earnings Per Share	PAT = Profit After Tax	YTD = Year-To-Date
EV = Enterprise Value	PBT = Profit Before Tax	

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