

5 November 2020

# Rubberex Corporation (RBRX MK)

**More Than Just An ASP Hike; BUY**

- **BUY, new DCF-derived MYR3.00 TP from MYR2.20, 32% upside with c.3% FY20F yield.** We expect Rubberex to book strong 3QFY20 earnings, given its higher-than-expected ASP. In 4Q20, its new capacity for nitrile gloves should surge 150% QoQ to 2.5bn ppa. By percentage, its capacity growth is the industry's highest. Our TP implies 9.8x FY21F P/E – a 45% discount to peer average, reflecting its smaller market cap and liquidity.
- **Expecting a strong 3Q20.** We expect Rubberex to announce its 3Q20 results by the end of the month. In view of its high glove ASP for July-September, 3Q20 earnings should double QoQ and surge >10 times YoY.
- **ASP higher than expected.** Based on the results and outlook shared by Hartalega (HART MK, BUY, TP: MYR23.50) and Supermax (SUCB MK, BUY, TP: MYR13.25) – both companies reported their earnings in October – we may have underestimated the quantum of ASP increase. This is due to the worse-than-expected rate of COVID-19 infections globally, and shortage of nitrile butadiene (the raw material used to manufacture nitrile gloves). Nitrile gloves accounted for c.45% of Rubberex's total FY19 revenue, and we expect this to increase to 80% in FY21.
- **Nitrile glove production capacity to surge 150% QoQ (highest in the industry by percentage).** The company has completed building its new factory, and is in the final round of trial runs to optimise the production process. We expect earnings contributions from the new factory to start in December, so 4Q20 earnings should be much better QoQ. For the nitrile gloves segment, Rubberex's capacity will increase 150% to 2.5bn ppa from 1.0bn ppa currently, once the factory is ready in December.
- **Share buyback worth MYR26.9m (price range: MYR1.88-2.62 post-bonus issue).** Over 2-14 Oct, Rubberex bought back its shares at prices ranging from MYR5.63 to MYR7.87 (pre-bonus issue). This is equivalent to MYR1.88-2.62 post bonus issue. We believe this is a strategic move by Management, when it deemed its shares undervalued. Separately, on 21 Oct, Rubberex completed its 2-for-1 bonus issue with the listing of 555m shares. Post-bonus issue and share buyback, its latest number of shares total 800m.
- **BUY, with higher MYR3.00 TP.** We lift FY21-23F core earnings by 48-136% on higher ASP assumptions. The higher TP is in line with our assumption of elevated earnings growth. However, our DCF valuation's long-term growth estimate has dropped to 1% (from 3%), as we expect to see more competition in the long term, due to high ASP. In the short term, 3Q20 earnings should improve QoQ due to the ASP increase.
- **Risks.** The biggest downside risk is a safe and effective COVID-19 vaccine being made available globally faster than expected. Other risks: Lower-than-expected sales volume/USD, and higher-than-estimated raw material prices.

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (MYRm)	205	223	458	687	584
Recurring net profit (MYRm)	9	11	139	255	175
Recurring net profit growth (%)	-	30.7	1,119.9	84.2	(31.6)
Recurring P/E (x)	218.49	167.14	13.70	7.44	10.87
P/B (x)	8.8	9.3	6.7	4.5	3.7
P/CF (x)	43.11	16.71	16.37	8.37	8.27
Dividend Yield (%)	0.8	0.9	3.3	6.0	4.1
EV/EBITDA (x)	77.08	72.64	9.37	4.95	6.65
Return on average equity (%)	-	5.4	57.0	72.6	37.2
Net debt to equity (%)	9.6	net cash	net cash	net cash	net cash

Source: Company data, RHB

See important disclosures at the end of this report

Market Dateline / PP 19489/05/2019 (035080)

Consumer Non-cyclical | Rubber Products

**Buy** (Maintained)

Target Price (Return):	MYR3.00 (+32%)
Price:	MYR2.28
Market Cap:	USD439m
Avg Daily Turnover (MYR/USD)	39.3m/9.35m

## Analyst

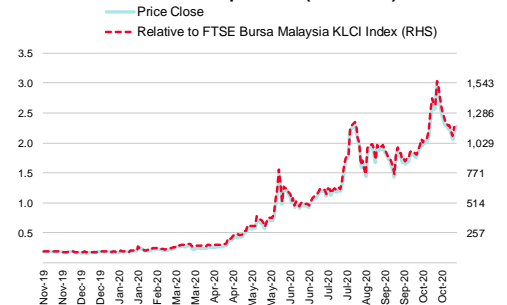
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## Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	1166.7	19.8	1.8	284.5	1100.0
Relative	1174.7	22.4	9.1	278.3	1108.9
52-wk Price low/high (MYR)				0.16 – 2.95	

## Rubberex Corporation (RBRX MK)



Source: Bloomberg

## Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

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## Financial Exhibits

<b>Asia</b>	<b>Financial summary (MYR)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
Malaysia	Recurring EPS	0.01	0.01	0.17	0.31	0.21
Consumer Non-cyclical	DPS	0.02	0.02	0.07	0.14	0.09
<b>Rubberex Corporation</b>	BVPS	0.26	0.25	0.34	0.51	0.62
RBRX MK	Return on average equity (%)	-	5.4	57.0	72.6	37.2
Buy						
<b>Valuation basis</b>	<b>Valuation metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
DCF	Recurring P/E (x)	218.49	167.14	13.70	7.44	10.87
	P/B (x)	8.8	9.3	6.7	4.5	3.7
	FCF Yield (%)	1.3	3.7	3.2	10.6	10.7
	Dividend Yield (%)	0.8	0.9	3.3	6.0	4.1
<b>Key drivers</b>	EV/EBITDA (x)	77.08	72.64	9.37	4.95	6.65
i. Volume of sales;	EV/EBIT (x)	148.37	105.19	9.77	5.07	6.89
ii. USD/MYR rates positively impacting its numbers;						
iii. Nitrile butadiene price.						
<b>Key risks</b>	<b>Income statement (MYRm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
i. Lower-than-expected sales volume;	Total turnover	205	223	458	687	584
ii. Lower-than-expected USD/MYR;	Gross profit	26	32	203	364	254
iii. Higher-than-expected raw material prices.	EBITDA	25	26	198	358	248
	Depreciation and amortisation	(12)	(8)	(8)	(8)	(9)
	Operating profit	13	18	190	350	240
	Net interest	(3)	(2)	(1)	(1)	(1)
	Pre-tax profit	10	16	190	349	239
	Taxation	(1)	(4)	(51)	(94)	(65)
	Reported net profit	9	11	139	255	175
	Recurring net profit	9	11	139	255	175
<b>Company Profile</b>	<b>Cash flow (MYRm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
Rubberex produces nitrile disposable gloves, household gloves and industrial gloves.	Cash flow from operations	44.0	113.6	115.9	226.6	229.5
	Capex	(18.9)	(43.0)	(55.0)	(25.0)	(26.3)
	Cash flow from investing activities	(18.8)	(43.3)	(55.0)	(25.0)	(26.3)
	Dividends paid	(14.6)	(16.6)	(62.3)	(114.8)	(78.5)
	Cash flow from financing activities	(27.6)	(39.3)	(62.6)	(116.7)	(80.5)
	Cash at beginning of period	26.1	23.9	56.1	53.0	137.9
	Net change in cash	(2.3)	30.9	(1.7)	84.9	122.8
	Ending balance cash	23.7	54.8	54.4	137.9	260.7
	<b>Balance sheet (MYRm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Total cash and equivalents	24	56	53	138	261
	Tangible fixed assets	87	125	169	183	198
	Total assets	295	270	372	540	646
	Short-term debt	31	11	11	12	12
	Total long-term debt	13	1	1	1	1
	Total liabilities	80	65	91	118	128
	Total equity	214	205	281	421	517
	Total liabilities & equity	295	270	372	540	646
	<b>Key metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Revenue growth (%)	0.0	8.6	105.4	50.1	(15.1)
	Recurrent EPS growth (%)	0.0	30.7	1119.9	84.2	(31.6)
	Gross margin (%)	12.8	14.2	44.4	52.9	43.5
	Operating EBITDA margin (%)	12.1	11.5	43.3	52.1	42.5
	Net profit margin (%)	4.2	5.1	30.2	37.1	29.9
	Dividend payout ratio (%)	167.7	146.6	45.0	45.0	45.0
	Capex/sales (%)	9.2	19.3	12.0	3.6	4.5
	Interest cover (x)	4.64	9.34	380.45	699.90	479.19

Source: Company data, RHB

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Consumer Non-cyclical | Rubber Products

Figure 1: DCF valuation

FYE Dec (MYRm)	FY20F	FY21F	FY22F	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	Terminal
CFO	116	227	229	213	239	271	323	375	428	470	
+ Interest (1 - Tax Rate)	0	0	0	0	0	0	0	0	0	0	
- capital expenditure	(55)	(25)	(26)	(28)	(29)	(30)	(32)	(34)	(35)	(37)	
<b>Free cash flow to firm (FCFF)</b>	<b>61</b>	<b>202</b>	<b>204</b>	<b>185</b>	<b>211</b>	<b>241</b>	<b>291</b>	<b>342</b>	<b>394</b>	<b>433</b>	<b>3,737</b>
Discount factor	0.98	0.85	0.74	0.65	0.57	0.50	0.43	0.38	0.33	0.29	0.29
PV of FCFF	60	172	152	121	120	120	126	129	130	125	1,075
Risk-free	4.0%										
Beta	1.22										
Cost of Equity	11.3%										
WACC	12.7%										
Terminal growth	1.0%										
Enterprise Value (MYR m)	2,328										
Cash	76										
- Debt	(4)										
Equity Value (MYR m)	2,400										
No of shares (m)	800										
<b>Fair Value (MYR)</b>	<b>3.00</b>										

Source: RHB

Figure 2: Key assumptions

Key Assumptions	FY20F	FY21F	FY22F
Installed year-end capacity (m ppa)	2,500	2,500	2,500
Blended ASP (USD per 1,000 pieces)	50	60	50
Average USDMYR	4.025	4.025	4.025
Utilisation rate	60%	88%	85%

Source: RHB

Figure 3: TP sensitivity based on bull, base and bear cases for nitrile glove ASPs

Scenario	FY20F	FY21F	FY22F	Long Term	TP (MYR)
Bull	50	70	60	57	3.90
Base	50	60	50	47	3.00
Bear	50	50	40	37	2.10

Source: RHB

**Base case assumption for vaccine development.** Our base case scenario is that a safe and effective vaccine will be available in 1H21 under an Emergency Use Authorisation clause. This should lead to lower 2H21 glove demand, assuming that COVID-19 cases decline by then. As 85% of glove demand is from the medical segment, fewer COVID-19 cases should reduce demand from the segment. However, it is impossible to determine if any of the vaccine candidates currently under trial will work, as even the most promising Phase 2 results can fail in Phase 3, according to the US Food and Drug Administration.

We will be monitoring the progress of vaccine development closely, as this is a potential leading indicator for a decline in COVID-19 cases in the future. Historically, after the H1N1 pandemic (2009-2010), demand fell only slightly in 2011 YoY, by 1.3% or 2bn to 148bn pieces pa (ppa) then. Demand growth continued from 2012 onwards, and remains in positive growth. This is reflected in our lower ASP for FY22F, compared to that of FY21F.

**Upside risk to ASP is possible due to raw material shortage.** Due to the unprecedented demand for nitrile gloves, demand for nitrile butadiene has spiked. The situation has worsened, leading to nitrile butadiene suppliers raising the price of this raw material by 20% each month since September. This is a strong indicator that almost all nitrile butadiene supply in the market has been booked, as buyers are now willing to pay higher prices. If this situation persists into 1Q21, it would lead to a longer-than-expected sustained increase in nitrile glove ASPs – as demand would continue to grow, but supply is capped by the shortage of raw materials.

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-08-28	Buy	2.20	1.89
2020-04-28	Buy	0.56	0.43

Source: RHB, Bloomberg

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<b>Trading Buy:</b>	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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