Power tariff hike to have minimal impact on glove makers

by Fatin Rasyiqah Mustaza

KUALA LUMPUR: The recent electricity tariff hike coupled with the aggressive capacity expansion are expected to have a minimal impact on the earnings growth of rubber glove makers, said analysts.

Alliance Research Sdn Bhd analyst Ian Wan said glove makers are able to mitigate the effect of the tariff hike via their dominance in the global glove market, cost savings from automation and cost pass through mechanisms.

Malaysia commands 55% share of the world’s rubber glove export market.

“The higher power rates will have a minimal impact on rubber glove makers,” Wan told The Edge Financial Daily.

“They will be able to pass on the cost increase [to customers by raising selling prices], of which fuel costs constitute only 8% to 9% of the overall production costs,” he said.

On the potential upward adjustments in natural gas prices, Wan estimates that if the cost reaches 10%, glove makers will have to adjust their prices by 0.8%.

Analysts at Kenanga Research expects the hike to hit earnings of rubber glove makers by only 2% to 3%.

“We are not overly concerned since rubber glove players are generally able to pass on the cost increase judging by past electricity and natural gas tariff hikes.

“Electricity accounts for an estimated 20% to 30% of fuel costs which in turn make up 10% of total production costs of rubber glove players. Natural gas accounts for the remaining 60% to 70%,” he said.

Both analysts see positive demand growth for the local glove sector this year.

Wan expects demand for rubber gloves to grow 8% to 10% and higher at 15% if there is a global epidemic.

“This shows high support for earnings growth [of rubber glove companies],” he said, projecting growth of 14% this year and a “neutral” call on the sector.

With the top four glove players — Top Glove Corp Bhd, Supermax Corp Bhd, Kossan Rubber Industries Bhd and Hartalega Holdings Bhd increasing their capacity aggressively, Wan is expecting an average volume growth of 15% this year.

Kenanga’s analyst expects an average of 10% demand growth per year in the next few years.

“The demand and strong double digit [earnings] growth rate of glove makers are expected to continue, with nitrile gloves taking the lead. We also expect latex-based gloves to continue to register positive volume sales as well from stable latex price,” he added.

Although the glove players are increasing their capacity, the analyst is not overly concerned about a potential oversupply situation at least for 2014.

“Based on the back-of-the-envelope calculations, applying the same sales volume growth of 15% achieved in 2012 and exports of 81.4 billion pieces of rubber gloves in 2013 and 2014, this would yield an additional increase of 12.2 billion and 14.1 billion pieces respectively,” the analyst said.

“Most glove manufacturers can only run at an average maximum utilisation rate of 90% as they require some down time for maintenance while industry capacity expansion is only coming in progressively throughout 2014. This implies the addition of only 14.8 billion pieces at end-2014,” he said.

Kenanga Research has an “overweight” call on the sector.