

VEEKO INT'L (1173.HK)



Looking forward to the cosmetics business, but valuation fully reflected

Phillip Securities (Hong Kong) Ltd
Phillip Securities Research

Bloomberg | Reuters | POEMS

1173.HK | 1173.HK | 1173.HK

Industry: HK Retailer

5 February 2014

Rating: Reduce, CP: HKD0.35, TP: HKD0.33

Company Profile

Veeko International is engaged in the trade, manufacture and wholesale ladies apparel under brandnames Veeko and Wanko. The Group has launched chain cosmetics retail business in Oct 2004 and established Colourmix stores. As of the end of Sep 2013, the Group has 201 Veeko/Wanko outlets and 70 Colourmix outlets in Hong Kong, Macau and China.

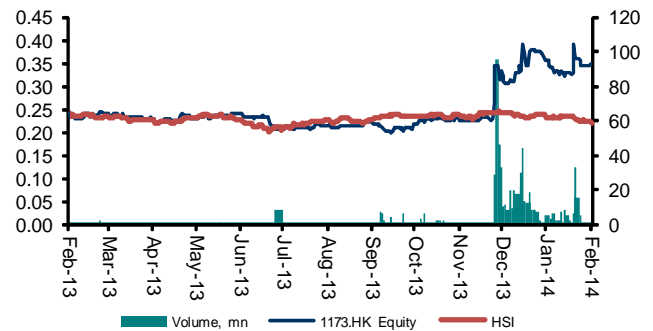
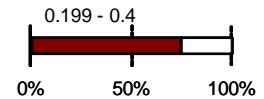
Investment rationales

Cosmetics business continues to expand, offsetting sluggish fashion business: For the interim results ended Sep 13, the Group's cosmetics business recorded operating profit of HKD20.9 mn, up 97.1% YoY. In the same period, operating profit for fashion business fell 81.2% YoY to HKD1.4 mn. The Group's overall operating profit surged 25% YoY to HKD22.3 mn. The Group started cosmetics retail business since 2004, which has already accounted for 93.9% of total operating profit. We believe the Group will invest more resources in the cosmetics business, which is in the high-growth phase, in the future, to offset the downturn of fashion business. Cosmetics business has become a key growth driver for the Group.

Cosmetics business performed well in past years: The Group has increased its cosmetics stores, Colourmix, to 66 by the end of Mar 13 from 37 by the end of Mar 10, 8-12 stores were added each year. The 3-year CAGR for revenue was 41.3%, 3-year CAGR for operating profit was 27.3%, 3-year CAGR for sales per store was 16.3%, 4-year average of SSSG was 12.5%, reflecting the Group has gained good progress in the cosmetics business in past few years, and brought decent return to investors. But look at the FY13 figures only, the Group's operating profit for cosmetics business recorded the first setback in 5 years. SSSG recorded a rare single digit of 7.3%. Management attributed it to some turnover decreased inevitably due to renovation of some outlets, some outlets were moved due to unreasonable rentals increment, which resulted in more expenses for restoration and depreciation and decrease in gross margin. But management said the effect was temporary and remained optimistic for the business outlook after renovation. The latest interim results confirmed the management's confidence, SSSG of cosmetics business rose to 21% high level, gross margin rebounded to 37.2% (vs. 1HFY13: 37.5% and FY13: 36.4%). The operating profit of cosmetics business was nearly doubled.

VEEKO INTL HLDGS

Rating	4.00	Reduce
- Previous Rating	N/A	Not Rated
Target Price (HKD)	0.33	
- Previous Target Price (HKD)	N/A	
Closing Price (HKD)	0.35	
Expected Capital Gains (%)	-5.7%	
Expected Dividend Yield (%)	4.0%	
Expected Total Return (%)	-1.7%	
Market Cap. (HKD mn)	809	
Enterprise Value (HKD mn)	832	
3M Average Daily T/O (mn)	9.5	
52 week range (HKD)	0.199 - 0.4	
Closing Price in 52 week range		



Key Financial Summary

FYEMAR	FY12	FY13	FY14E	FY15E
Revenue (HKD mn)	1,280	1,409	1,674	1,889
Net Profit, adj. (HKD mn)	57	31	42	59
EPS, adj. (HKD cents)	2.61	1.39	1.84	2.42
P/E (X)	7.4	15.5	17.9	13.7
P/B (X)	0.7	0.8	1.2	1.1
DPS (HKD cents)	1.50	1.40	1.40	1.40
Div Yield (%)	7.8%	6.5%	4.2%	4.2%

Source: Bloomberg, PSR est.

Valuation Method

PE

Analyst

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Scale just after Sa Sa, but operational efficiency needs to be improved:

The Group currently has 68 cosmetics stores (vs. Sa Sa: 103 stores and Bonjour: 45 stores). But its operational efficiency was significantly weaker than the peers. For the latest interim results, the Group's sales per store was ~HKD6.5 mn (vs. Sa Sa: HKD30.4 mn and Bonjour: HKD28.6 mn). The Group's operating profit margin was 4.6% only (vs. Sa Sa: 12.0% and Bonjour: 10.4%). Nevertheless, Sa Sa and Bonjour opened their first store in 1990 and 1991 respectively. Their management accumulated relatively more experience. We believe Colourmix has relatively more room for growth. Indeed, operating profit margin of Colourmix has been up from 4.1% in FY09 to 5.7% in FY13 (vs. Sa Sa improved from 10.3% in FY09 to 12.9% in FY13). Sales per store for Colourmix climbed from HKD6.7 mn in FY09 to HKD12.6 mn in FY13 (vs. Sa Sa's rose from HKD49.1 mn in FY09 to HKD61.5 mn in FY13). With a lower base, Colourmix has a larger room for growth.

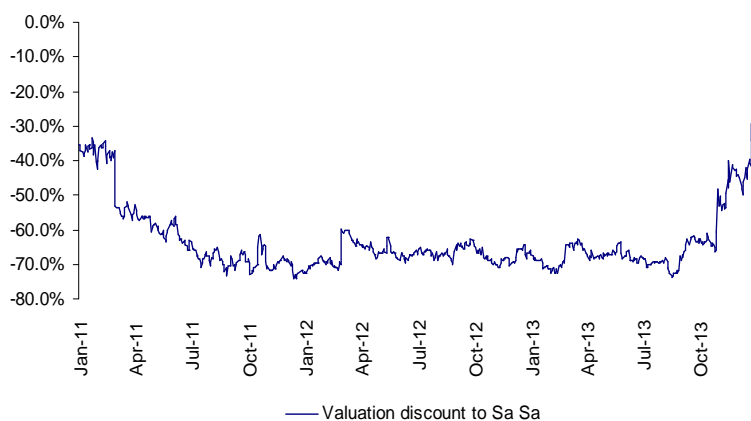
Valuation: Veeko is trading at trailing P/E of 25.2x (excluded non-recurring items). Driven by cosmetics business, we expect the Group's core EPS to reach HKD 1.84/2.42 cents in FY14/FY15, up 32.4%/31.5%, FY15 earnings will be close to FY12 level. Following the Group posted FY14 interim results, its valuation discount to Sa Sa Int'l became smaller significantly, which is believe to be due to the decent performance of its cosmetics business attracted investors' attention. If the Group's cosmetics business kept a desirable growth, we believe the valuation discount to peers will be further narrowed. Sa Sa Int'l is now trading at FY14 P/E est. of 20.2x. Given Veeko's smaller size, weaker operational efficiency and higher operating risk being dragged by fashion business, we give a target price of HKD0.33, equivalent to FY14/FY15 forecast P/E of 18x/13.6x. We give a "Reduce" rating with downside potential of 5.7%. Veeko's share price has recorded an increase of 59% in last 3 months, we suggest investors to wait for a better buying opportunity.

Fig.1 5-year P/E band



Source: PSR, Bloomberg

Fig.2 P/E valuation discount to Sa Sa (178.HK)



Source: PSR, Bloomberg

Fig.3 Revenue projections

FYE MAR	FY10	FY11	FY12	FY13	FY14E	FY15E
Sales (HKD mn)						
Fashion	591	624	592	576	579	593
Cosmetics	295	488	687	833	1,095	1,296
Sales YoY growth (%)						
Fashion	-4.1%	5.5%	-5.1%	-2.8%	0.5%	2.4%
Cosmetics	70.2%	65.4%	41.0%	21.2%	31.5%	18.4%
Operating profit (HKD mn)						
Fashion	25	48	35	14	3	3
Cosmetics	16	25	36	33	55	66
Operating margin (%)						
Fashion	4.2%	7.7%	6.0%	2.5%	0.5%	0.5%
Cosmetics	5.5%	5.2%	5.2%	4.0%	5.0%	5.1%
SSSG (%)						
Fashion (HK & Macau)	N/A	8.0%	4.6%	9.0%	-2.0%	-1.0%
Cosmetics	12.2%	16.2%	14.4%	7.3%	21.9%	9.9%
No. of store						
Fashion (HK & Macau)	72	70	69	77	82	84
Cosmetics	37	45	57	66	73	81
Sales per store (HKD mn)						
Fashion (HK & Macau)	4.7	5.3	5.4	5.0	4.8	4.8
Cosmetics	8.0	10.8	12.1	12.6	15.0	16.0
Sales per store YoY growth (%)						
Fashion (HK & Macau)	-4.7%	11.4%	3.4%	-7.4%	-4.5%	0
Cosmetics	19.6%	36.0%	11.3%	4.6%	18.9%	6.7%

Source: PSR, Company reports

Fig.4 Peers comparison for cosmetics business

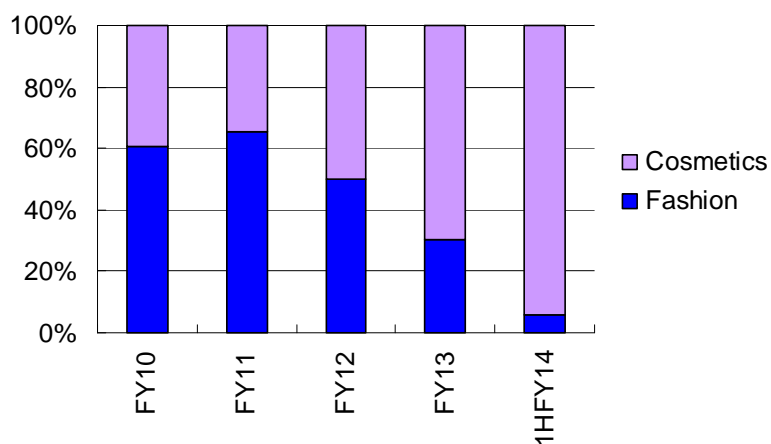
Name	Stock code	Year end	Mkt Cap (HKD mn)	FY14 P/E est. (x)	No. of store (HK & Macau)	Sales per store (HKD mn)	SSSG (%)	Operating profit margin (%)
Veeko	1173.HK	MAR	798	18.0	68	~6.5	21.0%	4.6%
Sa Sa	178.HK	MAR	21,121	20.3	103	30.4	13.0%	12.0%
Bonjour	653.HK	Dec	4,595	13.8	45	~28.6	18.8%	10.4%

* Data are from latest interim results

* Sales per store are half-year figures

Source: PSR, Bloomberg, Company reports

Fig.5 Operating profit breakdown



Source: PSR, Company reports

Major risks

Fashion business turns to loss

Rental costs surge

Gross margin drops

Inventory levels soar

Financial Status

FYE MAR	FY11	FY12	FY13	FY14E	FY15E
Valuation Ratios					
P/E (X), adj.	10.1	7.4	15.5	17.9	13.7
P/B (X)	1.2	0.7	0.8	1.2	1.1
Dividend Yield (%)	5.2%	7.8%	6.5%	4.2%	4.2%
Per share data (HKD cents)					
EPS, reported	3.36	2.79	2.44	1.84	2.42
EPS, adj.	3.22	2.61	1.39	1.84	2.42
DPS	1.70	1.50	1.40	1.40	1.40
BVPS	28.22	27.41	27.99	28.03	30.08
Growth & Margins (%)					
Growth					
Revenue	25.4%	15.1%	10.1%	18.8%	12.9%
EBIT	154.4%	-3.6%	-7.1%	-16.2%	33.1%
Net profit, adj.	80.2%	-11.2%	-45.7%	35.0%	34.0%
Margins					
Gross profit	54.6%	51.4%	47.9%	45.5%	44.2%
EBIT	6.3%	5.3%	4.5%	3.1%	3.7%
Net profit, adj.	5.8%	4.4%	2.2%	2.5%	3.0%
Key Ratios					
ROE (%)	13.1%	9.8%	5.1%	6.6%	8.4%
Total debt/ equity (%)	3.1	10.3	12.3	16.5	15.1
Asset turnover (x)	1.9	1.9	1.9	2.1	2.2
Inventory days	159.2	154.9	163.4	151.7	147.5
Account receivable days	15.4	14.7	14.7	14.3	13.9
Account payable days	43.4	33.6	33.4	30.4	28.5
Income Statement (HKD mn)					
Revenue	1,111	1,280	1,409	1,674	1,889
COGS	(505)	(621)	(734)	(911)	(1,054)
Gross profit	606	658	675	762	834
SG&A	(552)	(601)	(635)	(720)	(774)
Other income	16	10	23	10	10
EBIT	70	68	63	53	70
Net finance costs	(1)	(1)	(2)	(2)	(2)
Other items	3	3	6	0	0
Associates & JVs	0	0	0	0	0
Profit before tax	72	69	67	51	68
Tax	(5)	(8)	(12)	(9)	(12)
Profit after tax	67	61	54	42	56
Non-controlling interest	0	0	0	0	0
Net profit, reported	67	61	54	42	56
Net profit, adj.	64	57	31	42	56

Source: PSR

Balance Sheet (HKD mn)	FY11	FY12	FY13	FY14E	FY15E
PP&E	149	166	156	166	170
Goodwill	0	0	0	0	0
Associates & JVs	0	0	0	0	0
LT Investments	0	0	0	0	0
Others	65	78	80	73	75
Total non-current assets	214	243	235	239	245
Inventories	228	299	358	400	452
Accounts Receivables	52	51	63	69	75
ST investments	(2)	(1)	0	1	2
Cash or equivalents	118	106	83	80	84
Others	34	36	43	44	45
Total current assets	429	492	546	594	658
Total Assets	644	735	782	833	903
ST loans	10	58	75	69	70
Accounts Payables	59	69	76	83	90
Others	4	6	3	3	4
Total current liabilities	72	133	154	155	164
LT loans	8	4	1	36	35
Others	5	2	5	6	7
Total non-current liabilities	13	5	6	42	42
Minority Interests	(2)	(1)	0	1	2
Shareholder Equity	561	598	622	635	695

Source: PSR

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Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within \pm 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

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