

# MAN WAH HLDGS (1999.HK)

Strong domestic sales growth and promising prospects

Hong Kong | Consumption | Company report

27 February 2018

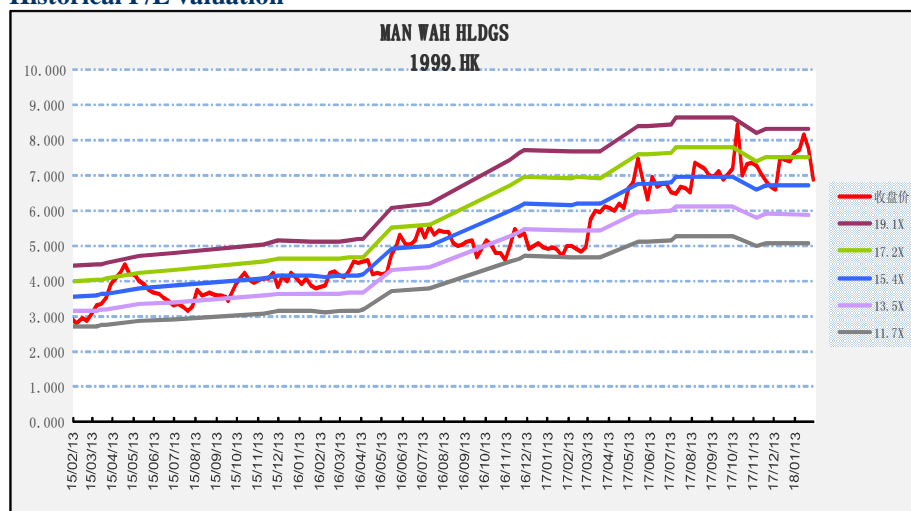
## Summary of Investment

- Interim net profit fell by 10% yoy, with short-term pressure on gross margin;
- Strong sales growth in Chinese market, and gradual improvement in European and American markets;

**Buy**

CMP: HKD 7.43  
(Closing price as at 23 Feb 2018)  
TARGET: HKD 9.18 (23.6%)

## Historical P/E valuation



Source: Wind, Phillip Securities HK Research

## COMPANY DATA

O/S SHARES (MN) :	3829
MARKET CAP (HKD MN) :	28447
52 - WK HI/LO (HKD):	8.62/4.74

## SHARE HOLDING PATTERN , %

Min Hua Investment Company Limited	63.83
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## PRICE PERFORMANCE , %

	1-Month	3-Month	1-Year
MAN WAH	-9.72	5.84	48.6
HSI	-5.97	4.23	28.4

## PRICE VS. HSI



Source: Phillip Securities (HK) Research

## Investment Rating

Recently, the Company has acquired two target companies, namely Jiangsu Yulong and Jiangsu Delancey. Upon the completion of the acquisition, the Company will effectively enhance the production capacity and productivity in respect of the business of iron frame and functional sofa in China. We are optimistic about the Company's endogenous growth in the Chinese market. Driven by product price increases, capacity expansion and cost control, the overall gross margin is expected to stabilize and rise. It is estimated that the net profits attributable to the parent company for 2018-2019 will reach HKD1757 million and HKD2077 million, respectively; EPS will be 0.46 and 0.54, respectively, equivalent to PE 16.2 and 13.7, respectively. The rating of "Buy" is given. (Closing price as at 23 Feb 2018)

## KEY FINANCIALS

HKDmn	FY16	FY17	FY18E	FY19E
Revenue	7382	7841	9448	11400
Net Profit	1327	1752	1757	2077
P/E,x	21.4	16.2	16.2	13.7
EPS, HKD	0.35	0.46	0.46	0.54
P/B, x	6.0	4.9	4.2	3.6
BVPS, HKD	1.23	1.51	1.75	2.07
ROE, %	28.2	30.3	26.2	26.2

Source: Company reports, Phillip Securities Est.

Research Analyst  
**Wang Yannan**  
(+ 86 21 51699400-107)  
wangyannan@phillip.com.cn

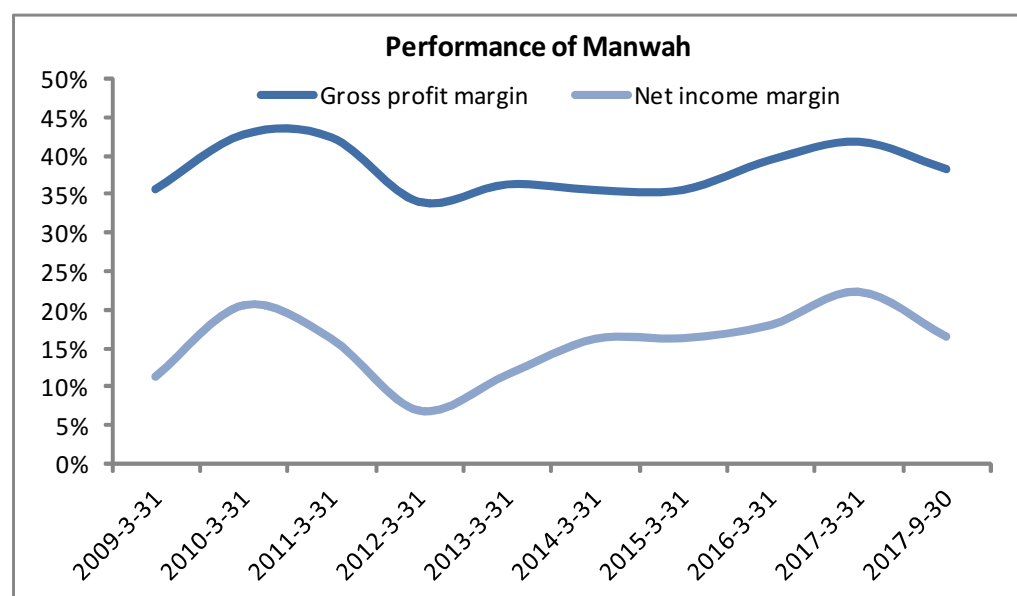
## Interim net profit fell by 10% yoy

Man Wah Holdings recorded a revenue of HK \$4.62 billion in H1 of FY2018, an increase of 28.8% over the same period of last year. Net profit attributable to the listed company was HK \$793 million, down by 10.3% yoy. Specifically, the revenue from the sales of sofas and accessory products was HK \$3,369 million (+ 13.1%), accounting for 72.8% of the total. The retail business of sofa and related products contributed to revenue of HK \$446 million (+ 26.2%), accounting for 9.7% of the total. Revenue of other products recorded RMB420 million (+ 62.1%), accounting for 9.1%. Home Group business recorded a revenue of RMB391 million, accounting for 8.5%.

## Gross margin was affected by rising raw material costs

In terms of profitability, the overall gross margin was 38.3%, down by 4.4pct yoy. The decrease in gross margin was partly due to the large increase in the price of raw materials, and, on the other hand, was caused by the merger of the business of the Home Group. The gross margin of the Home Group was approximately 23.6%. Excluding the impact of merger, the gross margin of the Group was approximately 39.7%. In response to the rising cost of raw materials, the Company raised the prices of its products in the market of mainland China by 8%, in which the price of functional sofas rose by about 8% and non-functional sofas and bedding products increased by 5%.

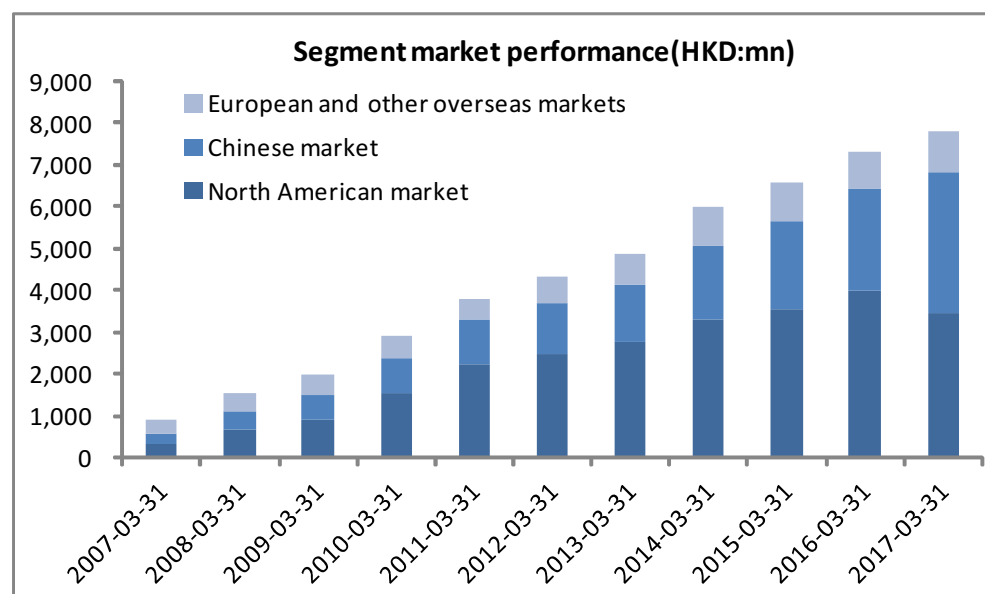
During the period, the expense ratio was 19.83%, up by 1.06pct yoy, of which, the administration expense rate slightly decreased to 4.27% and the selling expense ratio increased by 1.26% to 15.26% yoy. It was mainly due to the merger of Home Group business and rising ocean freight costs. The financial expense ratio rose slightly to 0.2%. In addition, foreign exchange gains and losses during the period dropped from HK \$+84 million in the same period of previous year to HK \$ -30 million. In summary, the rising cost of raw materials, the rising expense ratio and the exchange losses eventually dragged down the net profit growth.



Source: Wind, Phillip Securities HK Research

## Strong sales growth in Chinese market

During the period, the wholesale business achieved a substantial growth in Chinese market with an increase of 40.2% yoy to HK \$1,285 million with a gross margin basically unchanged. The number of outlets increased from 1,504 in March 2017 to 1,630 with an increase of 8.4%. The average sales volume increased by 16.1% yoy, and the operating efficiency improved significantly. The future growth in the Chinese market, on one hand, comes from the Company's continuous efforts to expand online and offline distribution channels. In the future, the offline outlets will have a broad space for expansion, while online e-commerce platforms still boast good growth potential; on the other hand, the current functional sofa witnessed a period of rapid development, and the Company is expected to further enhance market share through its brands and channels.



Source: Wind, Phillip Securities HK Research

## Exports in European and American markets gradually improved

Revenue in North America market grew by 2.1% yoy to RMB1,756 million, with gross margin dropping 5.3pct, while revenue in Europe and other markets dropped by 2.6% to RMB329 million, with gross margin decreasing 4.9pct. In the North American market, the Company achieved a monthly improvement in sales growth by enriching product lines, strengthening sales team building and expanding new customers. In addition, the Company has embarked on an expansion project to boost production capacity in the European market, and put wood processing plants into operation recently, which are expected to significantly reduce the cost of raw materials. In our opinion, the collaborative advantages brought by the acquisition of Home Group will help the Company continue to explore the European market and the Chinese market.

## Risk Warnings

Market competition is intensified;

Gross margin goes downward;

Sales growth is less than expected;

## Financials

FYE	FY15	FY16	FY17E	FY18E	FY19E
<b>Valuation Ratios</b>					
Price Earnings(P/E)	26.5	21.4	16.2	16.2	13.7
Price to Book(P/B)	6.5	6.0	4.9	4.2	3.6
<b>Per share data(HKD)</b>					
EPS,Adjusted	0.28	0.35	0.46	0.46	0.54
Book Value Per Share	1.15	1.23	1.51	1.75	2.07
Dividends Per Share	0.19	0.18	0.22	0.22	0.26
<b>Growth &amp; Margins(%)</b>					
<b>Growth</b>					
Revenue	9.4%	11.7%	6.2%	20.5%	20.7%
Operating income	16.9%	35.1%	29.9%	6.0%	20.5%
Net profit	10.0%	23.4%	32.0%	0.3%	18.3%
<b>Margins</b>					
Gross profit margin	36.1%	40.0%	42.3%	39.4%	39.6%
Operating profit margin	15.4%	18.6%	22.7%	20.0%	20.0%
Net income margin	16.3%	18.0%	22.3%	18.6%	18.2%
<b>Key Ratios</b>					
ROE(%)	24.5%	28.2%	30.3%	26.2%	26.2%
ROA(%)	17.6%	22.6%	27.3%	22.7%	22.8%
<b>Income Statement(HKD mn)</b>					
<b>Revenue</b>	6,606	7,382	7,841	9,448	11,400
- Cost of Goods Sold	4,222	4,432	4,521	5,722	6,884
<b>Gross Income</b>	2,384	2,950	3,320	3,726	4,516
- Operating Expenses	1,369	1,580	1,539	1,838	2,242
<b>Operating Income</b>	1,015	1,371	1,781	1,888	2,275
- Net Non-Operating Losses (Gains)	(244)	(119)	(271)	(120)	(108)
<b>Pretax Income</b>	1,259	1,490	2,052	2,008	2,383
- Income Tax Expense	175	150	293	241	293
<b>Net profit</b>	1,075	1,327	1,752	1,757	2,077

Source: Company, Phillip Securities (HK) Research Estimates

(Financial figures as at 23 Feb 2018)

**PHILLIP RESEARCH STOCK SELECTION SYSTEMS**

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

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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**Contact Information (Regional Member Companies)**

**SINGAPORE**

**Phillip Securities Pte Ltd**  
Raffles City Tower  
250, North Bridge Road #06-00  
Singapore 179101  
Tel : (65) 6533 6001  
Fax : (65) 6535 6631  
Website: [www.poems.com.sg](http://www.poems.com.sg)

**HONG KONG**

**Phillip Securities (HK) Ltd**  
Exchange Participant of the Stock Exchange of Hong Kong  
11/F United Centre 95 Queensway  
Hong Kong  
Tel (852) 22776600  
Fax (852) 28685307  
Websites: [www.phillip.com.hk](http://www.phillip.com.hk)

**INDONESIA**

**PT Phillip Securities Indonesia**  
ANZ Tower Level 23B,  
Jl Jend Sudirman Kav 33A  
Jakarta 10220 – Indonesia  
Tel (62-21) 57900800  
Fax (62-21) 57900809  
Website: [www.phillip.co.id](http://www.phillip.co.id)

**THAILAND**

**Phillip Securities (Thailand) Public Co. Ltd**  
15th Floor, Vorawat Building,  
849 Silom Road, Silom, Bangrak,  
Bangkok 10500 Thailand  
Tel (66-2) 6351700 / 22680999  
Fax (66-2) 22680921  
Website: [www.phillip.co.th](http://www.phillip.co.th)

**UNITED KINGDOM**

**King & Shaxson Capital Limited**  
6th Floor, Candlewick House,  
120 Cannon Street,  
London, EC4N 6AS  
Tel (44-20) 7426 5950  
Fax (44-20) 7626 1757  
Website: [www.kingandshaxson.com](http://www.kingandshaxson.com)

**AUSTRALIA**

**PhillipCapital Australia**  
Level 12, 15 William Street,  
Melbourne, Victoria 3000, Australia  
Tel (613) 96188238  
Fax (613) 92002272  
Website: [www.phillipcapital.com.au](http://www.phillipcapital.com.au)

**MALAYSIA**

**Phillip Capital Management Sdn Bhd**  
B-3-6 Block B Level 3 Megan Avenue II,  
No. 12, Jalan Yap Kwan Seng, 50450  
Kuala Lumpur  
Tel (603) 21628841  
Fax (603) 21665099  
Website: [www.poems.com.my](http://www.poems.com.my)

**JAPAN**

**PhillipCapital Japan K.K.**  
Nagata-cho Bldg.,  
8F, 2-4-3 Nagata-cho,  
Chiyoda-ku, Tokyo 100-0014  
Tel (81-3) 35953631  
Fax (81-3) 35953630  
Website: [www.phillip.co.jp](http://www.phillip.co.jp)

**CHINA**

**Phillip Financial Advisory (Shanghai) Co. Ltd**  
No 436 Hengfeng Road,  
Greentech Unit 604,  
Postal code 200070  
Tel (86-21) 51699400  
Fax (86-21) 63532643  
Website: [www.phillip.com.cn](http://www.phillip.com.cn)

**FRANCE**

**King & Shaxson Capital Limited**  
3rd Floor, 35 Rue de la Bienfaisance 75008  
Paris France  
Tel (33-1) 45633100  
Fax (33-1) 45636017  
Website: [www.kingandshaxson.com](http://www.kingandshaxson.com)

**UNITED STATES**

**Phillip Futures Inc**  
141 W Jackson Blvd Ste 3050  
The Chicago Board of Trade Building  
Chicago, IL 60604 USA  
Tel +1.312.356.9000  
Fax +1.312.356.9005