

Oriental Watch Holdings Limited (398.HK)

HK operation outperformed the market,
 Conservative spending on high-end luxury goods become a concern
 Consumer | Luxury Retail

5 May 2023

Oriental Watch Holdings Limited (Oriental Watch) that founded in 1961, has developed an extensive retail shop network in the Greater China area, and has become one of the largest watch retailers. Company carries around a hundred prestigious brands, in particular, famous Swiss brands such as Rolex, Tudor, Piaget, Vacheron Constantin, IWC, Jaeger-LeCoultre, Girard Perregaux, Longines, Omega, etc. Company operates a total of 12 shops in HK SAR and Macau SAR, including Oriental Watch Company, La Suisse Watch Company, Rolex and Tudor Boutique and Breitling Boutique. In 2004, company expanded its watch retail business to Mainland China. Since then, company has opened a number of outlets and boutiques covering various cities in Mainland, China. Subsequently, company has further expanded its businesses to Taiwan region. As at 30 September 2022, company operates 44 retail points (including associate retail stores) in the Greater China region, and 1 online store in each of the Mainland China and HK respectively.

HK operation outperformed the market with revenue increased by 6.1%

In 1HFY2023 (for the six months ended 30 September 2022), company's revenue decreased by 10.0% yoy to HK\$1,674 million, which was mainly attributable to the decrease in revenue in the Mainland China market as a result of business interruptions due to such lockdown policy and restrictions. In line with the decrease in revenue, gross profit decreased by 6.9% to HK\$537 million, with gross profit margin increased by 1.1 percentage points to 32.1%, and profit attributable to owners of the company decreased by 9.6% to HK\$151 million. Basic EPS were 31.03 HK cents, down 9.2% yoy. Interim dividend of 7.8 HK cents per share (1HFY2022: 8.6 HK cents per share) and a special dividend of 23.5 HK cents per share (1HFY2022: 25.8 HK cents per share).

During the Period, the company's aggregated expenses related to leases increased slightly by 5.3% to HK\$80 million, accounting for 23.1% of the overall operating expenses (1HFY2022: 22.2%). The increase was mainly due to the lease renewal of retail stores which command a relatively higher rental rate.

In Hong Kong, the COVID-19 pandemic situation has been under control since the first quarter of 2022. Yet, clouded by market uncertainty, the market sentiment remained cautious with the value of total retail sales decreased by 1.3% yoy during the first nine months of the year. However, sales of jewelry, watches and clocks, and valuable gifts recorded a slight increase of 0.2% during the same period. Despite the uncertain retail market sentiment, Hong Kong operation still outperformed the market with revenue increased by 6.1% to HK\$504 million for the period, accounting for 30.1% of the overall revenue, segment profit increased by 81.8% to HK\$42.75 million.

According to the National Bureau of Statistics, the PRC's gross domestic product (GDP) has recorded a 0.4% yoy growth and 3.9% yoy growth in the second and third quarter respectively, which grew at a softer pace compared with the same period of last year. The slowdown of economic growth was attributable to the widespread lockdown as well as the weakening market sentiment. Sales of gold, silver and jewelry also recorded a decrease of 0.8% yoy from April to September 2022. According to the Federation of the Swiss Watch Industry FH, the Swiss watch exports to the PRC during the Period decreased 13.7% yoy to CHF1,267.3 million, showcasing the country's conservative sentiment on purchasing luxury watches. Due to the economic condition as well as the temporary business suspension mentioned above, revenue from Mainland China operation decreased by 15.4% to HK\$1,101 million, accounting for 65.8% of the overall revenue, segment profit decreased by 23% to HK\$189.86 million.

Accumulate

CMP HKD4.49
 (Closing price as of 2 May)
 Target HKD 5.14 (+14.5%)

COMPANY DATA

O/S SHARES (MN) :	487.358
MARKET CAP (HKD MN) :	2188.2
52 - WK HI/LO (HKD):	4.63/2.937

SHARE HOLDING PATTERN, %

Yeung Ming Biu	31.96%
Ntasian Discovery Master Fund	5.11%
TIG Advisors LLC	5.05%

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

HKD mn	FY21	FY22E	FY23E	FY24E
Revenue	3,504.0	3,639.8	3,826.5	4,148.2
Net profit	233.3	362.6	357.2	367.3
Reported EPS	0.43	0.74	0.75	0.78
P/E ratio, x	10.4	6.0	6.0	5.7
Dividend Yield, %	11.4%	16.7%	16.6%	17.4%

Source: Company reports, Phillip Securities Est.

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Investment Thesis

Looking ahead, although China and Hong Kong have entered the road to normal after the epidemic, with the uncertainty from the increase in interest rate, and the management also expects consumers to become more conservative in consumption, especially on purchasing of high-end luxury goods. Hence, the business will be under some pressure over the upcoming periods. We expect FY2023-FY2024 EPS to be 74.62 HK cents and 78.10 HK cents respectively, with PT of HKD5.14, implies a FY2023E P/B of 1.21x (~1-yrs historical average plus 1 SD). Our investment rating is "Accumulate".

Risk factors

1) Economic recovery momentum is slowing down; 2) Operating costs are higher than expected; 3) Luxury goods consumption is lower than expected.

Financial

Consolidated Statement of Profit or Loss

Mar Y/E, HKD mn	FY20	FY21	FY22	FY23E	FY24E
Revenue	2,352.7	3,504.0	3,639.8	3,826.5	4,148.2
COGS	(1,707.4)	(2,541.9)	(2,459.5)	(2,602.3)	(2,857.9)
Gross Profit	645.3	962.1	1,180.3	1,224.2	1,290.3
Other income	28.4	34.6	42.8	41.3	46.6
Other gains and losses	(32.2)	5.3	17.5	(5.6)	(6.1)
Impairment, net	(15.5)	(1.7)	18.2	(2.6)	(2.1)
Selling and distribution costs	(334.4)	(431.5)	(504.7)	(522.9)	(558.5)
Administrative expenses	(155.3)	(212.0)	(243.7)	(246.8)	(267.5)
Financial cost, net	(14.2)	(10.2)	(12.0)	-	-
Share of results of associates	5.4	9.2	14.8	16.6	18.0
Share of result of a JV	(0.1)	(0.0)	0.4	(0.4)	(0.4)
Profit before tax	127.4	355.7	513.4	503.8	520.1
Income tax	(28.3)	(123.1)	(150.5)	(146.2)	(152.4)
Profit for the year	99.1	232.6	363.0	357.6	367.7
Minority interest	(1.2)	(0.6)	0.4	0.4	0.4
Shareholders Net profit	100.3	233.3	362.6	357.2	367.3
Reported EPS (HKD)	0.18	0.43	0.74	0.75	0.78
DPS (HKD)	0.25	0.51	0.75	0.75	0.78
Payout ratio	139.3%	118.1%	100.7%	100.0%	100.0%

Key Financial Data

Mar Y/E	FY20	FY21	FY22	FY23E	FY24E
Valuation Ratio					
P/S ratio, x	1.1	0.7	0.6	0.6	0.5
P/E ratio, x	25.5	10.4	6.0	6.0	5.7
Dividend Yield, %	5.5%	11.4%	16.7%	16.6%	17.4%

Per share data (HKD)

EPS	0.18	0.43	0.74	0.75	0.78
BVPS	3.65	3.69	4.18	4.24	4.33
DPS (HKD)	0.25	0.51	0.75	0.75	0.78

Growth & Margin

Growth					
Revenue Growth	-3.5%	48.9%	3.9%	5.1%	8.4%
Gross Profit Growth	7.0%	49.1%	22.7%	3.7%	5.4%
Net Profit Growth	-28.2%	134.7%	56.0%	-1.5%	2.8%
Margin					
Gross Profit Margin	27.4%	27.5%	32.4%	32.0%	31.1%
Net Profit Margin	4.3%	6.7%	10.0%	9.3%	8.9%

Key Ratios

ROE	4.7%	11.4%	18.0%	17.6%	18.1%
ROA	4.1%	8.9%	12.9%	12.5%	13.1%

Consolidated Statement of Financial Position

Mar Y/E, HKD mn	FY20	FY21	FY22	FY23E	FY24E
Non Current Asset					
PPE	213.0	208.1	244.1	247.5	247.8
Right-of-use assets	287.8	334.1	415.3	390.5	408.1
Others	134.0	186.6	184.4	196.0	207.6
Total Non Current Assets	634.9	728.8	843.9	834.1	863.5
Current Asset					
Inventories	798.7	622.8	483.6	656.5	933.2
Trade and other receivables	112.8	286.0	205.1	237.9	235.8
Bank balance and cash	936.6	1,061.3	1,282.4	1,053.4	737.7
Others	30.7	28.7	64.2	45.7	27.1
Total Current Assets	1,878.8	1,998.8	2,035.4	1,993.5	1,933.9
Total Assets	2,513.6	2,727.5	2,879.3	2,827.6	2,797.4
Current Liabilities					
Payables	86.8	287.4	270.8	257.7	224.5
Short term borrowings	5.7	17.5	28.7	-	-
Other current Liabilities	118.3	147.6	186.5	196.5	206.5
Total current Liabilities	210.7	452.5	486.1	454.2	431.0
Non Current Liabilities					
Lease liabilities	205.8	265.7	326.7	300.3	268.9
Others	13.9	18.8	30.4	44.4	58.4
Total Non-Current Liabilities	219.6	284.5	357.0	344.6	327.2
Equity					
Shareholders' equity	2,083.6	1,991.5	2,035.0	2,027.6	2,038.0
Non-controlling interests	(0.3)	(0.9)	1.2	1.2	1.2
Total equity	2,083.3	1,990.5	2,036.2	2,028.8	2,039.2
Total Liabilities and Equity	2,513.6	2,727.5	2,879.3	2,827.6	2,797.4

Consolidated Statement of Cash Flow

Mar Y/E, HKD mn	FY20	FY21	FY22	FY23E	FY24E
CFO					
Profit before income tax	127.4	355.7	513.4	503.8	520.1
D&A add-back	165.5	141.9	165.4	162.9	168.6
Others	58.9	(11.1)	(53.1)	(16.6)	(18.0)
Net (inc)/dec working capital	(19.6)	231.2	246.0	(218.9)	(307.9)
Tax	(25.8)	(74.2)	(139.1)	(132.2)	(138.4)
Net cash flow from operating activities	306.4	643.5	732.7	299.1	224.4
CFI					
Purchase of PP&E and Investment	(53.1)	(30.0)	(51.0)	(34.0)	(31.0)
Others	4.7	(18.0)	(26.6)	16.6	18.0
Net cash flow from investing activities	(48.4)	(48.0)	(77.6)	(17.4)	(13.0)
CFF					
Net Borrowings	(57.9)	12.0	11.2	(28.7)	-
Others	(324.0)	(509.8)	(469.6)	(482.0)	(527.1)
Net cash flows from financing activities	(381.8)	(497.9)	(458.4)	(510.7)	(527.1)
Net Change in Cash	(148.3)	124.7	221.1	(229.0)	(315.7)
Cash and CE at Y/E	936.6	1,061.3	1,282.4	1,053.4	737.7

Current Price as of: May 2

Source: PSHK Est.

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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