

## Hosa International Limited

### Stand out from the sportswear industry strait

To summarize...

- Announced FY12/12A annual result, Hosa recorded turnover growth by 22% YoY and net growth by 21% YoY.
- Good % growth in each product line; fitness wear sales increased by 34% leverage on parent's Hosa fitness center chain expansion.
- Defensive financial position, remain cash rich with net cash value of RMB741.9m, equivalent to HK\$0.58 per share
- Updated 12A historical P/E of 9.3x is trading 12% discount to outdoor sportswear leader.

**What news?** Hosa released its 12A annual result yesterday after market. Sales of each products segment reported a good % growth. Sales turnover from swimwear, fitness wear, sports underwear and accessories were up by 28%, 34%, 12% and 8%. Group turnover increased by 22% YoY to RMB848.1m while gross profit increased by 19% with margin dropped by 1.6pp YoY to 60.6%. Slight decline in gross margin was due to change in product mix in sport underwear, which contributed 36% of company sales. Operating profit and net profit were in line with sales growth, were up by 20% and 21% to RMB379.6m and RMB330.9m respectively. Operating margin and net profit margin maintained at good level, dropped by 0.7pp and 0.3pp YoY to 44.7% and 39.0%. The slight decline in margin was due to increase in % of SG&A to sales by 1.8pp to 19.1% and decline in gross margin. The effect was partly offset by increase in other income from government grants and written back for long-aged liabilities. Total other income was up by 4.5x YoY to RMB27.3m.

Table 1: Earning result summary

	FY10A	FY11A	FY12A	g % YoY
Turnover	347.8	695.2	848.1	22%
Swimwear	143.5	237.2	304.0	28%
Fitness wear	73.8	155.3	207.6	34%
Sports underwear	111.6	270.3	301.6	12%
Accessories	18.9	32.4	34.8	8%
Gross profit	169.4	432.6	514.2	19%
Operating Profit	115.1	317.2	379.6	20%
Net profit	94.4	273.7	331.1	21%

Source: the company

**In terms of Balance sheet result.** Hosa financial position remained strong. Net cash position was reported since listed in 2011. Hosa reported a net cash value of RMB741.9m as on Dec 12, equivalent to HK\$0.58 per share or 26% of market value. Operating cash cycle was up by 36 days as a result of decline in trade payable turnover days. Trade payable turnover days dropped by 34 days to 86 days. Inventory and trade receivables days maintained at similar level as in 2011. Inventory turnover days increased by 6 days to 111 days, whereas trade receivables days dropped by 4 days to 100 days. Increase in cash cycle has led to decline in cash flow from operation, dropped by 17% YoY to RMB256.1m/ 77% of net profit.

Table 2: Operating cash cycle

	FY10A	FY11A	FY12A
Receivable turnover days	94	99	104
Inventory turnover days	253	123	105
Payable turnover days	180	113	120
Cash cycle	167	109	89

Source: the company

Ticker	2200 HK
Rating	Not Rated
Price (HK\$)	2.37
Target Price (HK\$)	-
12m Price Range (HK\$)	1.6 – 2.65
Market cap. (US\$m)	486.2
Daily t/o (US\$m)	0.1
Free float (%)	25

#### Financial summary

Year to Dec	10A	11A	12A
Turnover (RMB)	348	695	848
Net Profit (RMB)	94	274	331
EPS (RMB)	0.06	0.17	0.21
P/E (x)	30	11	9
P/B (x)	12	4	3
EV/EBITDA (x)	20	5	6
Yield (%)	-	-	-
ROE (%)	45%	47%	34%
ROCE (%)	55%	54%	43%
N. Gear. (%)	N. Cash	N. Cash	N. Cash

Source: Company

	12F	13F	14F
Consensus EPS (RMB)	-	-	-
Previous EPS (RMB)	-	-	-

#### Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	12.2	(4.5)	31.9
Actual price changes (%)	8.2	(0.8)	41.1



Source: Bloomberg

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**1 'strong ASP growth' + 2 'strong volume growth'.** Since 2H FY11, Hosa has successfully repositioned its swimwear product line to the high-end market. Average retail price was around RMB260 ~ RMB280 per swimsuit as opposed to previously around RMB100- RMB150. The successful repositioning led Hosa swimwear ex-factory ASP to increase by 43% to average RMB92.2 in FY12A, traded off for lower sales volume (dropped by 11% YoY to 3.3m units). As for fitness wear and sports underwear, both product lines recorded a good sales volume growth with ASP at similar level in 11A. Total unit sold of fitness wear and sports underwear increased by 32% and 15% YoY to 2.8m units and 3.9m units. Strong growth in Fitness wear and sport underwear were largely due to the enhanced synergy effect from parent company fitness business expansion. Hosa fitness (owned by the parent company) is one of the largest chained fitness centers in China, operates over 70 fitness centers with more than 300,000 gym members. The strong sales were also rewarded from vigorous marketing campaign; includes sponsorship of Miss Asia Final, International Miss Bikini Contest, promotional activities on TV and magazines etc. In Oct 2012, company has launched a lifestyle sports magazine namely Hosa Joy to promote fitness news and Hosa brand. Company has been awarded by World Brand Lab as one of the 'China's 500 Most Valuable Brands' with brand value of RM2.1b in 2012.

**Illustration 1. Indoor sportswear market leader**



Source: www.hosa.com.cn

**Maintain high margins.** 12A COGS to sales ratio increased by 1.5pp to 39.4%, which was largely due to increase in raw materials cost by 40% YoY (at a faster pace than sales growth). Manufacturing overhead and labour increased by 24% and 13% while procurement cost of finish products dropped by 21%. They accounted for 77%, 11%, 3% and 9% of COGS orderly. Breakdown by product line, fitness wear yielded the highest margin at 68% in FY12A, i.e. average cost of RMB24 in FY12A. Swimwear margin increased slightly by 0.8pp despite the rally in ASP by 43%, average cost was RMB32 increased by 39% YoY. Gross margin of sports underwear dropped by 6.7pp YoY to 50.3%, due to increase in cost (by RMB4) coupled with decrease in ASP (by RMB2.7). In terms of SG&A expenses, SG&A to sales ratio increased by 1.8pp YoY to 19.1%. Administrative expense increased by 28% YoY to RMB70.4m whereas selling and distribution expense increased by 40% YoY to RMB91.5m. Selling and distribution was mainly accounted for marketing (~50%) and distributor rebate (~50%).

**Table 3. ASP, margin & volume breakdown**

	1H 12A Sales		2H 12A Sales		1H 12A GP		2H 12A GP		
	Swimwear	Accessories	Swimwear	Accessories	Swimwear	Accessories	Swimwear	Accessories	
ASP (RMB)	1H F11A	2H F11A	1H F12A	2H F12A	GP Margin	1H F11A	2H F11A	1H F12A	2H F12A
Swimwear	52	95	93	91	63%	66%	65%	66%	
Fitness wear	69	80	73	76	67%	67%	66%	69%	
Sports underwear	80	81	83	76	61%	56%	52%	49%	
Accessories	35	33	34	38	68%	61%	72%	65%	
Average Cost (RMB)					Unit Sold (m)				
Swimwear	19	32	33	31	2.64	1.05	1.69	1.61	
Fitness wear	23	26	25	24	1.14	0.97	1.24	1.54	
Sports underwear	32	36	40	39	0.85	2.49	1.36	2.49	
Accessories	11	13	9	13	0.54	0.41	0.23	0.70	

Source: SBI E2 Capital

Table 4. Financial Summary

	FY09A	FY10A	FY11A	FY12A
Turnover (RMB m)	159.2	347.8	695.2	848.1
Growth (%)	(22%)	119%	100%	22%
Gross profit (RMB m)	62.9	169.4	432.6	514.2
GP (%)	40%	49%	62%	61%
Pre-tax profit (RMB m)	27.2	108.8	315.7	379.0
Profit from discontinued operation (RMB m)	0.8	4.1	-	-
Gain on disposal of assets (RMB m)	-	17.6	-	-
Net profit (RMB m)	28.6	94.4	273.7	331.1
Growth (%)	1%	230%	190%	21%
Cash generated from operations (RMB m)	(68.4)	107.3	309.3	256.1
Receivable turnover days	94.0	99.0	103.5	100.0
Inventory turnover days	253.0	122.6	105.3	111.0
Net debt/cash (RMB m)	98.0	(22.9)	(648.8)	(642.7)
Total asset (RMB m)	360.3	533.4	1,043.8	1,268.1
Equity (RMB m)	120.6	297.4	877.2	1,052.1
Net debt to asset (%)	27%	(4%)	(62%)	(51%)
Net debt to equity (%)	81%	N Cash	N Cash	N Cash
EPS (RMB)	0.0	0.1	0.2	0.2
Growth (%)	1%	230%	190%	21%

Source: the company

**Our view and valuation.** Hosa strong FY12/12A performance has beat consensus estimate by 7%. As a China leading indoor sportswear brand, Hosa is trading at 12A P/E 9.3x and 13F P/E 9.5x as opposed to outdoor market leader, Anta (2020 HK), trading at 12A P/E of 10.6x and 13F P/E 14.2x. Li Ning (2331 HK), another sizable sportswear brand who is to be more focused on swimwear business, is trading at 11A P/E of 29.7x and an expected loss in 12F. In our view, despite the sluggish China consumer performance during the period, e.g. decrease in sales growth/ sales decline in major shopping mall operate and sales decline, intensive competition in sportswear sector, Hosa has outperformed the market with turnover and net profit growth over 20% YoY.

Table 5. Valuation Comparison

Company name	Ticker	Fiscal year	Mkt cap (US\$m)	His P/E (x)	1-Yr P/E (x)	2-Yr P/E (x)	PB (x)	Est ROE (%)
ANTA	2020 HK	12/2012	2,317.2	10.6	14.2	13.9	2.1	20.7
XTEP INTERNATIONAL	1368 HK	12/2011	853.7	5.5	6.1	7.8	1.3	7.9
LI NING CO LTD	2331 HK	12/2011	654.0	29.7	-	93.9	1.1	3.8
361 DEGREES	1361 HK	06/2011	605.6	2.8	5.5	6.6	0.8	8.9
CHINA DONGXIANG	3818 HK	12/2011	742.9	-	19.4	18.1	0.7	(0.4)
<b>HOSA</b>	<b>2200 HK</b>	<b>12/2012</b>	<b>489.3</b>	<b>9.3</b>	<b>9.5</b>	<b>-</b>	<b>3.3</b>	<b>9.9</b>
PEAK SPORT	1968 HK	12/2011	392.5	4.1	5.8	6.0	0.6	15.2
<b>Average</b>			<b>865.0</b>	<b>10.3</b>	<b>10.1</b>	<b>24.4</b>	<b>1.4</b>	<b>9.4</b>

Source: Bloomberg

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