

Results Update

Hosa International 2200 HK

Satisfactory interim results bode well for the future

- *Hosa recorded revenue and net profit attributable to shareholders of RMB563.5m and RMB199.4m in 1H FY12/14, representing a YoY increase of 20.3% and 28.2% respectively.*
- *The company was in an ample cash position of RMB1,156.7m by the end of 1H FY12/14, which we believe would be enough for its near-term expansion given its limited capex needs.*
- *The company will continue to roll out new products which we believe will lead growth in the future.*
- *We believe the company deserves a higher valuation given its higher-than-average profitability, liquidity and growth rate.*

Research Team

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Stock Data (2200 HK)

	Not Rated
Rating	Not Rated
Price (HK\$)	2.48
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	1.94-3.25
Market cap. (HK\$m)	4,103.4
Daily t/o (HK\$m)	0.5
Free float (%)	27.5
Source: Bloomberg	

Water Cube Swimwear line led the growth: The company's "Water Cube" swimwear line saw a significant growth in FY12/13, with revenue generated from sales of the products up by 161.9% YoY. We believe the company will see continuous growth with more of its new products rolled out on the mid-to-high end market in the next couple of years.

Net cash position improved: The net cash of the company increase to RMB1,156.7m, representing a growth of 9.2% compared with the net cash at the end of FY12/13. We believe the ample net cash position would enable the company to explore investment and business opportunities in the expanding apparel industry. We do not see any urgent funding needs of the company in the short run.

Expansion of sales channel by developing online business: The company is planning to promote its online business strategy and develop its mobile Internet in the coming years. In our view, Online sales does not only provide another sales channel for the company, but it can also have synergies with its offline operation and thus helps gain its market share.

The company will benefit from the growing indoor sports industry: Sportswear industry in China was growing at a CAGR of 14.4% during the 4-yr period from 2009 and 2013. We believe indoor sportswear will grow at a faster pace than outdoor sportswear, as indoor sports are gaining popularity with increasing severity of the air pollution in China. Hosa is undoubtedly a beneficiary of the fast growing indoor sportswear industry in China.

Undemanding valuation compared with peers: The company is currently trading at a 2013 historical P/E and 2014 prospective P/E of 7.9x and 7.7x respectively, both of which are below the average level that the sportswear and underwear companies are trading. We believe the company deserves a much higher valuation, given i) higher-than-average profitability indicated by its ROE and ROA; ii) higher CAGR in net profit; and iii) better net cash position, which is a prerequisite of higher dividend payout in the future.

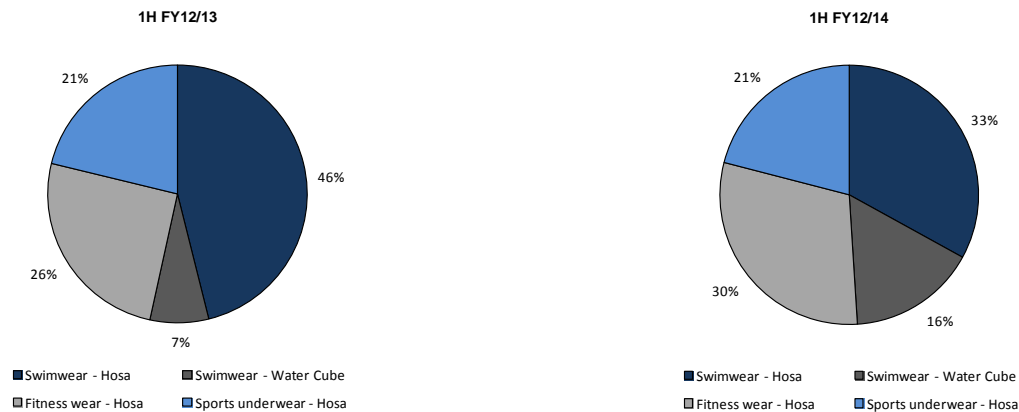
Figure 1: Financials and valuation

	FY12/11	FY12/12	FY12/13	1H FY12/14
Total revenue (RMB m)	695.2	848.1	1,021.5	563.5
Revenue growth (YoY)	99.9%	22.0%	20.5%	20.3%
Gross profit (RMB m)	432.6	514.2	590.3	305.2
PBT growth (YoY)	155.4%	18.9%	14.8%	9.5%
Net profit (RMB m)	273.7	331.1	370.4	199.4
Net profit growth (YoY)	135.8%	21.0%	11.9%	28.2%
EPS (RMB)	0.22	0.21	0.23	0.12
DPS (RMB)	0.07	0.08	0.09	0.05
P/E (x)	9.0	9.4	8.6	-
Dividend yield	3.5%	4.1%	4.6%	2.7%

Source: Company data

Please refer to important disclosures at the end of this report

Figure 2. Revenue breakdown by segment in 1H FY12/13 & 1H FY12/14



Source: Company data

Figure 3. Change in revenue components

	1H FY12/14 RMB m	1H FY12/13 RMB m	Change (%)
Swimwear - Hosa	186.1	215.9	-13.8%
Swimwear - Water Cube	90.0	34.4	161.9%
Fitness wear - Hosa	169.3	118.7	42.6%
Sports underwear - Hosa	118.1	99.3	18.9%
Total revenue	563.5	468.3	20.3%

Source: Company data

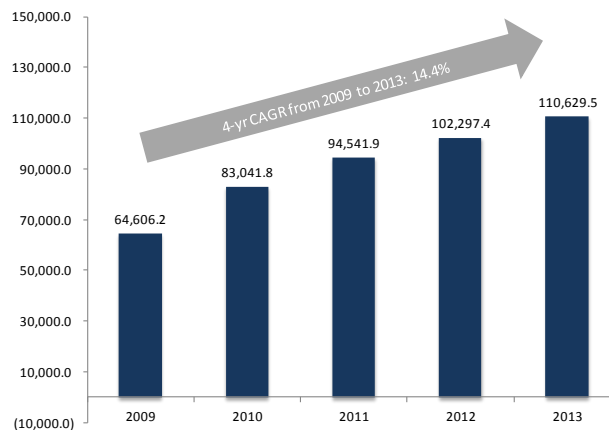
Water Cube Swimwear line led the growth: The “Water Cube” swimwear line, which was launched in FY12/13 and was designed to serve as a supplement to its “Hosa” brand swimwear, saw a significant growth in FY12/13, with revenue generated from sales of the products up by 161.9% YoY. The company revealed that it plans to put more new products on the mid-to-high end market in the next couple of years, which we believe might become its growth driver in the future. We also expect its existing products, including fitness wear and sports underwear, to grow steadily, with the increasing popularity of indoor sports activities on the back of serious air pollution in the country.

Net cash position improved: By the end of 1H FY12/14, Hosa was in a net cash position of RMB1,156.7m, which was 9.2% higher than its net cash of RMB1059.1m by the end of FY12/13. In our view, the strong cash position would enable the company to explore investment and business opportunities in the expanding apparel industry. We do not see any urgent funding needs of the company in the short run.

Expansion of sales channel by developing online business: To cater to the growing demand for online shopping in China, the company is planning to promote its online business strategy and develop its mobile Internet in the coming years. Specifically, Hosa will continue to aid and encourage its distributors to develop the online shops and micro-mall in the 2H of FY12/14. Additionally, Hosa is also considering developing its huge database about sports and health, which will cover all its products and services in the industry. Online sales, in our view, does not only provide another sales channel for the company, but it can also have synergies with its offline operation (e.g., out-of-date clothing can be sold online with discount, while up-to-date clothes are sold in the brick and mortar stores), and thus helps gain market shares.

The company will benefit from the growing indoor sports industry: Hosa is a beneficiary of the fast growing sportswear industry in China, which saw its revenue growing at a CAGR of 14.4% during 4-year period between 2009 and 2013 (See Figure 4).

We believe indoor sportswear will grow at a faster pace than outdoor sportswear, as indoor sports are gaining popularity with increasing severity of the air pollution in China. Within the indoor sportswear segment, fitness wear, which is widely regarded as a high-end sport, is expected to grow at a fast rate with increasing wealth and public awareness of health. According to an independent research “Market Analysis on China’s Indoor Sportswear Industry” conducted by Frost & Sullivan, the CAGR of fitness wear market is expected to be around 34.5% for the next 5 years, while the CAGR for swimwear industry and sports wear industry will be approximately 18.9% and 19.3%, respectively.

Figure 4: Total revenue of sports goods industry in China (RMB m)


Source: WIND, SBI China Capital

Brand value of Hosa on the rise: The Hosa brand was once again recognized as China's 500 Most Valuable Brands by the World Brand Lab, with its brand value increased from RMB2.8b in 2013 to RMB3.5b in June 2014, indicating its increasing popularity in China. According to the report of "Market Analysis on China's Indoor Sportswear Industry", the market share of its three product lines, including fitness wear, swimwear and sports underwear in China, amounted to 8.4%, 10.5% and 44.1%, respectively, all of which ranked the first in their respective market segments.

Valuation

The company is currently trading at a 2013 historical P/E and 2014 prospective P/E of 7.9x and 7.7x respectively, both of which are below the average level that the sportswear and underwear companies are trading. As shown in figure 5, sportswear companies are on average trading at a 2013 historical P/E and 2014 prospective P/E of 16.2x and 13.7x, while the underwear companies are on average trading at 27.2x and 13.3x, respectively.

We believe the company deserves a much higher valuation, given i) higher-than-average profitability indicated by its ROE and ROA; ii) higher CAGR in net profit; and iii) better net cash position, which is a prerequisite of higher dividend payout in the future.

Figure 5. Peer comparison

Company	Ticker	Mkt Cap (HKD m)	3M avg turnover (HKD m)	2013 P/E (x)	2014E P/E (x)	2010-2013 profit CAGR (%)	P/book (x)	ROE (%)	ROA (%)	Dvd Yield (%)	Net Debt/Total Equity
Hosa International	2020 HK	4,103.4	0.5	8.6	7.7	47.2%	2.3	30.3	26.0	4.6	Net Debt/Total Equity (71.5)
Sportswear											
361 Degrees	1361 HK	3,907.8	1.5	14.7	10.7	-40%	0.7	4.5	2.9	7.3	(38.4)
Anta Sports	2020 HK	36,387.5	38.1	19.4	18.8	-5%	3.9	21.0	14.2	3.2	(65.6)
Li Ning	2331 HK	6,758.1	26.9	n.a.	n.a.	-171%	2.0	(18.2)	(6.5)	0.0	(7.7)
Peak Sport	1968 HK	4,469.0	4.2	14.5	11.5	-33%	0.9	6.0	4.7	3.8	(52.0)
Average		12,880.6	17.7	16.2	13.7	(0.6)	1.9	3.3	3.8	3.6	(40.9)
Underwear											
Embry Holdings	1388 HK	1,770.8	0.3	8.9	n.a.	16.3%	1.1	12.9	9.8	2.8	(13.8)
Top Form International	333 HK	400.0	0.2	52.3	n.a.	-145.1%	0.8	1.5	1.1	2.7	(26.2)
Cosmo Lady	2298 HK	6,996.7	37.9	20.3	13.3	n.a.	2.8	42.6	23.0	0.0	(42.2)
Average		3,055.8	12.8	27.2	13.3	-64.4%	1.6	19.0	11.3	1.8	(27.4)
Average of all*		8,670.0	15.6	21.7	13.6	-63.0%	1.7	10.0	7.0	2.8	(35.1)

Source: Company data

*Hosa International is not included in the average figure

Figure 6. Per share items

	FY12/11	FY12/12	FY12/13	1H FY12/14
EPS (RMB)				
- Basic	0.2	0.2	0.2	0.1
- Diluted	0.2	0.2	0.2	0.1
DPS (HKD)	0.07	0.08	0.09	0.05
BVPS (RMB)	0.5	0.6	0.8	0.9

Source: Company data

Figure 7. Ratio analysis

	FY12/11	FY12/12	FY12/13	1H FY12/14
Growth (YoY)				
Revenue	99.9%	22.0%	20.5%	20.3%
Net profit	135.8%	21.0%	11.9%	28.2%
Margins				
Gross margin	62.2%	60.6%	57.8%	54.2%
Net profit margin	39.4%	39.0%	36.3%	35.4%
Other ratios				
Return on average assets	34.7%	28.6%	26.0%	13.1%
Return on average equity	46.6%	34.3%	30.3%	15.1%
Dividend payout ratio	31.8%	38.1%	39.1%	44.2%
Valuation measures				
P/E (x)	9.0	9.4	8.6	-
P/B (x)	3.7	3.1	2.3	2.2
Dividend yield	3.5%	4.1%	4.6%	2.7%

Source: Company data

Figure 8. Income statement (HKD m)

	FY12/11	FY12/12	FY12/13	1H FY12/14
Revenue	695.2	848.1	1,021.5	563.5
COGS	(262.6)	(333.9)	(431.2)	(258.3)
Gross profit	432.6	514.2	590.3	305.2
Other income/(loss)	5.0	27.3	28.3	21.2
SG&A	(120.4)	(161.9)	(179.8)	(88.7)
Profit from operations	317.2	379.6	438.8	237.7
Finance costs	(1.5)	(0.6)	(0.4)	0.0
Income tax	(41.9)	(47.9)	(68.1)	(38.3)
Net profit attributable to shareholders	273.7	331.1	370.4	199.4

Source: Company data

Figure 9. Balance sheet (HKD m)

	FY12/11	FY12/12	FY12/13	1H FY12/14
Non-current assets				
Property, plant and equipment	48.4	46.2	59.1	72.2
Lease prepayments	11.9	11.6	18.6	18.4
Others	8.0	7.1	4.0	4.2
Total non-current assets	68.3	64.9	81.7	94.7
Current assets				
Inventories	100.1	102.2	151.4	195.8
Trade and other receivables	226.7	272.2	269.0	271.9
Others	13.2	426.3	741.6	1,151.3
Cash and cash equivalents	635.6	402.5	335.2	21.4
Total current assets	975.5	1,203.2	1,497.2	1,640.4
Current liabilities				
Borrowings	0.0	(86.9)	0.0	0.0
Trade and other payables	(149.8)	(117.0)	(174.1)	(212.0)
Others	(16.8)	(12.1)	(8.7)	(16.8)
Total current liabilities	(166.6)	(216.0)	(182.8)	(228.8)
Net assets	877.2	1,052.1	1,396.1	1,506.3
Equity				
Equity attributable to owners of the Company	13.0	13.0	13.5	13.5
Non-controlling interests	864.2	1,039.1	1,382.6	1,492.8
Total Equity	877.2	1,052.1	1,396.1	1,506.3

Source: Company data

Figure 10. Cash flow statement (HKD m)

	FY12/11	FY12/12	FY12/13	1H FY12/14
Operating activities				
Cash generated from operations	345.3	305.8	428.7	227.5
Tax paid	(36.0)	(49.8)	(67.1)	(30.3)
Net cash generated from operating activities	309.3	256.1	361.6	197.2
Net cash flow from investing activities	36.3	(332.9)	(318.2)	(418.6)
Net cash flow from financing activities	206.2	(75.2)	(110.7)	(92)
Net increase in cash and cash equivalent	551.8	(152.0)	(67.3)	(314)
Cash and cash equivalents at the beginning of the year	83.8	554.5	402.5	335.2
Cash and cash equivalents at the end of the year	635.6	402.5	335.2	21.4

Source: Company data

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