

Hosa International Limited

GP Margin expansion...

to summarize...

- The group reported annual result of FY12/11A. Revenue increased 99.9% YoY to RMB695.2m. The increase was due to expansion in number of retail outlets from 666 to 1,212 and the reduction of the wholesale discount from 75% to 65%.
- Gross profit of the period increased 155% YoY to RMB432.6m. Operating profit of the period increased 175% YoY to RMB317.2m. Net profit increased 190% YoY to RMB273.7m. Earnings per share increase by 120% to RMB22 cent and declare final dividend of HK\$8.4 cents per share.
- Gross margin increase 13.5 PCP to 62.2%. The increased was due to sales of higher margin products and greater economy of scale. Net profit margin increase 6 PCP to 39.4%.
- Total number of unit increased to 10,078 from 8,149 in the previous year. For FY2012 total number of POS is targeted to be around 1,800 and 2,000 for FY2013.
- Hosa is currently trading at 6.7x current year fwd P/E and 6.1x 1-yr fwd P/E on consensus. The average Hong Kong listed peer is trading at 9.1x current year forward P/E and 8.4x 1-year forward P/E.

Latest reported results: The group reported annual result of FY12/11A. Revenue increased 99.9% YoY to RMB695.2m. The increase was due to expansion in number of retail outlets from 666 to 1,212 and the reduction of the wholesale discount from 75% to 65%. Gross profit of the period increased 155% YoY to RMB432.6m. Operating profit of the period increased 175% YoY to RMB317.2m. Net profit increased 190% YoY to RMB273.7m. Earnings per share increase by 120% to RMB22 cent and declare final dividend of HK\$8.4 cents per share.

Table 1. FY 12/11A result

12 months to Dec	Turnover (RMB)	Gross Profit (RMB)	Gross margin (%)	Pre-tax profit (RMB)	Tax rate (%)	Net profit (RMB)
FY 12/11A	695.2	432.6	62.2	315.7	13.3	273.7
FY 12/10A	347.8	169.4	48.7	108.8	13.2	116.1
YoY(%)	99.9%	155%		190%		190%

Source: Company data

Sales composition: Swimwear accounted for 34.1% of sales compared to 41.3% in the previous period. Fitness wear accounted for 22.3%. Sports underwear accounted for 38.9% and accessories accounted for 4.7%. In terms of geographic sales channels, domestic customers accounted for 99.3% compare to 85.3% in the previous period. Foreign sales accounted for 0.7%.

Margins: Gross margin increase 13.5 PCP to 62.2%. The increased was due to sales of higher margin products and greater economy of scale. Net profit margin increase 6 PCP to 39.4%.

Unit & ASP: Total number of unit increased to 10,078 from 8,149 in the previous year. Swimwear accounted for 3,686 unit (FY2010A: 4,002) with ASP of RMB64.4 (FY2010A: RMB35.8). Fitness wear accounted for 2,104 unit (FY2010A: 1,428) with ASP of RMB73.8 (FY2010A: RMB51.7). Sports underwear accounted for 3,342 unit (FY2010A: 2,016) with ASP of RMB80.9 (FY2010A: RMB55.3). Accessories accounted for 946 unit (FY2010A: 703) with ASP of RMB34.2 (FY2010A: RMB26.9).

Cost structure: Cost of sales for consists of raw materials, labor, manufacturing overhead, and procurement costs of finished products. Raw materials accounted for

Ticker	2200 HK
Rating	Not Rated
Price (HK\$)	1.77
Target Price (HK\$)	-
12m Price Range (HK\$)	1.28-1.90
Market cap. (US\$m)	363.1
Daily t/o (US\$m)	0.1
Free float (%)	25.1

Financial summary

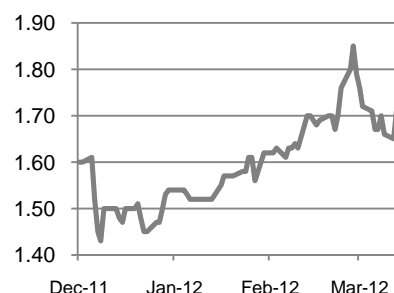
Year to Dec	09A	10A	11A
Turnover (RMB)	159.2	347.8	695.2
Net Profit (RMB)	28.7	116.1	273.7
EPS (RMB)	0.020	0.097	0.225
P/E (x)	91.0	22.5	9.7
P/B (x)	21.65	8.78	3.02
EV/EBITDA (x)	96.5	23.1	6.5
Yield (%)	-	-	4.7
ROE (%)	47.6	55.6	46.6
ROCE (%)	-	113.1	58.7
N. Gear. (%)	Cash	Cash	Cash

Source: Company

	12F	13F	
Consensus EPS (RMB)	0.215	0.235	-
Previous EPS (RMB)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	10.2	7.5	-
Actual price changes (%)	4.7	20.4	-



Source: Bloomberg

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69.8% decrease from 71.9% in the previous period. Labor cost accounted for 12.4%, manufacturing overhead accounted for 3.4% and procurement costs of finished products accounted for 14.4%.

Future Prospect

CAGR: Between FY08A and FY11A, Hosa's revenue increased at a CAGR of 35.8%, from RMB204.6m to RMB695.2m. Meanwhile, the group's net earnings increase at a CAGR of 75.3%, from RMB28.9m to RMB273.7m. The growth in the group's earnings was driven by increase in sales volume and product ASP, as well as margin expansion. The company is targeting to grow at around 20% for 2012 and 2013.

Table 2. Unit sold & average selling prices

	2009 Unit ('000)	ASP	2010 Unit ('000)	ASP	2011 Unit ('000)	ASP
Swimwear	2,574	27.4	4,002	35.8	3,686	64.4
Fitness wear	613	51.1	1,428	51.7	2,140	73.8
Sports underwear	1,357	39.0	2,016	55.3	3,342	80.9
Accessories	250	17.4	703	26.9	946	34.2
Total	4,794		8,149		10,078	

Source: Company data

Margin expansion: The group's blended profit margin expanded from 30.4% in FY08A to 62.2% in FY11A. The rapid expansion in the group's blended margin was the result of improvement in sales mix and increase in sales of premium functional products with higher ASP, as well as reduction of wholesales discount due to strong demand for its products. Going forward the group is targeting to maintain gross profit margin of 60% to 62%.

Table 3. Cost of sales

	2009 (RMB'000)	(%)	2010 (RMB'000)	(%)	2011 (RMB'000)	(%)
Raw materials	61,631	64.0	128,335	71.9	18,3366	69.8
Labor	14,049	14.6	20,613	11.6	32,485	12.4
Manufacturing overhead	12,090	12.6	19,350	10.8	8,840	3.4
Procurement costs of finished products	8,483	8.8	10,084	5.7	37,861	14.4
Total	96,253	100	178,382	100	262,552	100

Source: Company data

Sales network: The group's rapid revenue growth between FY08A and FY11A was partially attributable to expansion in its sales network and effective marketing strategy. The group's POS increased from 505 reported in FY08A to 1,212 in FY11A. It is worth to note that some of the group's POSs were located in gym and health club, which allows the group to sell its products to its end customers directly. For FY2012 total number of POS is targeted to be around 1,800 and 2,000 for FY2013. There currently 238 professional retail channels, 68 specialty stores, and 906 department stores.

Table 4. Retail outlets

	2008A	2009A	2010A	2011A
Department stores	499	516	562	906
Professional retail outlets	1	1	62	238
Hosa Specialty stores	5	5	42	68
Total	505	522	666	1,212

Source: Company data

Valuation & our view: The group's share is trading at 6.7x current year forward P/E and 6.1x 1-yr forward PE. The average Hong Kong listed peer is trading at 9.1x current year forward P/E and 8.4x 1-year forward P/E. In Chinese sportswear sector, Hosa has a unique position as it is a leader of indoor sportswear segment in China.

Table 5. Valuation Comparison

Company name	Ticker	Mkt cap (US\$m)	Last Price (Local)	His P/E (x)	1-Yr P/E (x)	2-Yr P/E (x)	PB (x)	Est ROE (%)
Anta Sports	2020 HK	2,606.1	8.15	9.5	10.5	10.2	2.59	27.7
Li Ning	2331 HK	1,169.6	8.64	9.0	17.9	16.1	2.12	23.1
Xtep Int'l	1368 HK	926.3	3.32	6.1	6.5	6.5	1.62	7.3
China Dongxiang	3818 HK	881.6	1.22	55.0	12.7	11.3	0.74	12.5
361 Degrees	1361 HK	622.9	2.35	3.5	3.7	3.7	0.93	20.1
Peak Sport	1968 HK	508.4	1.89	4.1	5.4	5.1	0.86	-
Hosa	2200 HK	363.1	1.77	6.5	6.7	6.1		
Average				13.4	9.1	8.4		

Source: Bloomberg

Company Background

Description: Hosa engages in the designs and production of sportswear products in the People's Republic of China. The range of product includes: swimwear, fitness wear, sports underwear and accessories. All products are selling under its own Hosa brand. The Company's segments include: Swimwear, which includes swimsuits and beachwear for women, men and children. They are the largest indoor sportswear brand in terms of 2010 ex-factory sales in China, captured 6.1%, 4.6% and 31.1% in the swimwear, fitness wear and sports underwear market sectors respectively.

Products: Swimwear includes swimsuits and beach wear for men women and children. Fitness wear includes apparel for women and men for indoor fitness activities, including yoga, gym and dance, such as body-sculpting yoga suits, loose-fitting yoga suits, track suits, general training suits, performance shirts and jackets, shape-enhancing fitness leggings and dance apparel. Sports underwear includes professional sports underwear and casual sports underwear for women and men. And accessories items includes accessories that complement its swimwear and fitness wear products, including swim goggles and caps, beach sandals and beach bags, as well as yoga mats, dance shoes, gym bags, sport towels, wristbands, headbands and water bottles.

Table 6. Sales by product

	2009 (RMB'000)	(%)	2010 (RMB'000)	(%)	2011 (RMB'000)	(%)
Swimwear	70,631	44.4	143,477	41.3	237,249	34.1
Fitness wear	31,316	19.7	73,806	21.2	155,276	22.3
Sports underwear	52,873	33.2	111,582	32.1	270,269	38.9
Accessories	4,349	2.7	18,922	5.4	32,374	4.7
Total	159,169	100	347,787	100	695,168	100

Source: Company data

Branding: Hosa's fitness wear products were recognized as one of China's Top Ten Innovative Sports Products in 2011. It is marketed as a symbol for active, fashionable and healthy lifestyles and as the premium brand for indoor sportswear products. They have been participating in sponsorship of national and international events, such as Miss Asia, Miss Bikini International and Asia Super Model Contest, in which company's products are modeled. The swimwear industry is highly fashion driven business and therefore highly sensitive to changes in consumer preferences. The company works closely with Italian and French fashion consulting firms to conduct market research, to keep its products in vogue. Since 2003, Hosa and China Fashion designer Association has co-operated the Hosa Cup China Swimwear Design contest to promote, attract innovative swimwear design. Hosa's tight-fitting fitness wear product was recognized as one of the China's top ten innovative products in 2010.

Table 7. Sales by geographical region

	2008 (RMB'000)	(%)	2009 (RMB'000)	(%)	2010 (RMB'000)	(%)	2011 (RMB'000)	(%)
Domestic sales	131,959	64.5	125,144	78.6	296,798	85.3	690,306	99.3
Overseas sales	72,684	35.5	340,258	21.4	50,989	14.7	4,862	0.7
Total	204,643	100	159,169	100	347,787	100	302,347	100

Source: Company data

Sales and distribution: Hosa has sales coverage throughout the first tier-cities in China, and is further extending to second and third-tiers cities. Hosa sold its products via 29 distributors, who operated 1,149 retail outlets across 26 provinces as well as utilized the online sales platforms in China. The majority of retails store are located on the first-ties cities in China. Going forward, they are set to open new retail outlets, and is targeted to further penetration in Northern China, North East China, Eastern China and Central China and on enhancing our presence in the second- and third- tiers cities.

History: The Company originally named Haosha was founded by the Shi Brothers in 1996. They started with main products including swimwear, fitness wear and then introduced sports underwear product line in 2000. Initially sell its entire product directly to end customers. From 2002 to 2006, the company began to develop and engage in 3rd party distributors in second and third tier cities. At the same time begin to market under the new English brand name Hosa. From 2007 to 2009, they established its own distribution subsidiaries to facilitate the expansion of distribution network. From 2010 to 2011, they disposed of distributor subsidiary to independent third parties as distribution model matures, and transition of business model to pure distributorship.

IPO: The company was listed on the Hong Kong Stock Exchange in December 2011 raising HK\$640m. The Book Runners were Bank of America Merrill Lynch and BOC International. The use of proceeds were 35% allocated for the expansion of distribution network and supporting the company's distributors in opening new retail outlets as well as upgrading existing retail outlets. 25% allocated to further enhance brand image through marketing and promotion, 15 allocated for the expansion of production capacity, 10% allocated for research, design and development activities, 5% allocated for further developing and updating supply chain and information management systems, and 10% for working capital and general corporate purposes.

Table 8. Historical P & L

Year to Dec (RMBm)	2009A	2010A	2011A
Revenue	159.2	347.8	695.2
Cost of sales	(96.3)	(178.4)	(262.6)
Gross profit	62.9	169.4	432.6
Other revenue	0.7	1.9	4.7
Other net income/(loss)	0.1	(0.4)	(0.4)
Selling and distribution costs	(23.7)	(29.1)	(65.3)
Administrative expenses	(10.0)	(26.7)	(55.1)
Other operating expenses	-	-	-
Profit from operations	29.9	115.1	317.2
Finance costs	(2.6)	(6.4)	(1.5)
Share of Profit of associates	-	-	-
Profit before tax	27.2	108.8	315.7
Income tax	1.4	(14.4)	(41.9)
Net profit	28.6	94.4	273.7

Source: Company data

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