

## Staging a comeback

## Hong Kong Industrials

**Playmates (635 HK, HK\$1.09)**

**BUY (unchanged)**

**Target price: HK\$1.50 (+37.6%)**

**Table 1: Results review**

	06A	05A	YoY (%)	Remarks on FY12/06 results	Outlook
<b>Sales</b>					
Toys business	1,128.0	1,277.6	(11.7)	Industry slowdown; Lower TMNT sales	Industry resume growth; APS +3%
Property investment	43.9	32.7	34.3	Rental income +30%	Continue to benefit from the strong property market
<b>Total</b>	<b>1,171.9</b>	<b>1,310.3</b>	<b>(10.6)</b>		
Gross margins (%) - Toys	48.0	50.1		Contribution from higher margin TMNT products fell	Gross margins expected widen back to 50%
Operating margins (%) - Toys	2.5	7.5		Higher marketing and distribution costs	
Revaluation surplus on investment properties	238.5	74.9	218.4		
Operating profit	268.4	172.4	55.7		
Pre-tax profit	314.8	198.8	58.3		
<b>Net profit</b>	<b>260.4</b>	<b>196.0</b>	<b>32.8</b>	<b>Better than expected</b>	
EPS (HK\$) - Basic	0.139	0.110	26.6		
EPS (HK\$) - F.D.	0.138	0.108	27.7		
DPS (HK\$)	0.070	0.050	40.0	Higher payout; special DPS HK\$0.02	

Source: SBI E2-Capital

**Result summary.** FY12/06A results came better than expected, with net profit up 32.8% YoY at HK\$260.4m despite a 10.6% YoY decline (1H FY12/06A: -26.7%) in sales to HK\$1,172m caused by lower sales in the toy business due to a downturn in its key product categories (action figures, dolls and plush toys) in the U.S. In 2H FY12/06A, toy sales fared better and declined only 2.3% YoY, compared with a 29.1% YoY drop in 1H FY12/06A. The sales of the Amazing series and two new brands, Strawberry Shortcake and Disney Fairies, have offset the decline in TMNT sales and the phasing out of King Kong and Speedeez brands. Net profit was buoyed by a revaluation gain on investment properties of HK\$238.4m and investment gains of HK\$37.2m. Excluding the property revaluation gain, operating income declined c.60% YoY to c.HK\$30m.

**Table 1: Financial summary**

Year to Dec	Net profit HK\$m	EPS HK\$	EPS Δ %	P/E x	P/B x	EV/EBITDA x	Yield %	ROE %	ROCE %	N. Gearing %
04A	255.3	0.167	198.5	6.5	0.0	7.3	3.7	24.7	20.5	Cash
05A	196.1	0.110	(34.2)	9.9	0.0	13.3	4.6	13.7	11.7	Cash
06A	260.4	0.138	25.3	7.9	0.0	38.0	3.8	14.6	1.7	Cash
07F	180.6	0.097	*(29.9)	11.3	0.0	9.4	3.5	9.3	8.0	Cash
08F	213.1	0.114	18.0	9.6	0.1	7.4	4.2	9.3	8.0	Cash

\*Distorted by property revaluation gain

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**Toys segment.****Table 2: Sales breakdown by brand**

	%
TMNT	c.20
Disney Princess	c.20
Disney Fairies	c.10
Strawberry Shortcake	c.20
Amazing Dolls	c.20

*Figures in the table represent an approximation*

*Source: Company data*

- **Pressure in FY12/06A.** The toys segment faced sales and operating pressure in FY12/06A. Sales pressure was mainly due to 1) lower TMNT sales, since 2006 was a planned transition year for TMNT in anticipation of the CGI animated motion picture in Mar 2007; 2) industry slowdown, especially in Playmates' key product categories and 3) more restrictive inventory policies by major retailers in the U.S., turnaround down from eight weeks to four to six weeks. Operating pressure came from higher S&G and distributing expenses. Beside, the gross margin narrowed 2.1% to 48.0%, as a result of greater contribution from lower margin products, such as the Amazing Dolls. The contribution of TMNT, which usually command higher margins, declined from c.33% of sales in FY12/05A to c.20% of sales in FY12/06A.
- **Bottoming out in FY12/07F.** Management expects the ASP to rise c.2-3% in FY12/07F as retailers begun to accept the industry's price adjustment. The gross margin should return to 50% in FY12/07F on higher TMNT sales with the CGI movie premier in Mar 2007. The actual sales impact of TMNT's brand new image is expected to emerge in Apr-Jun figures. It has seen a 30% increase in shelf-space in Spring already. Further off, Playmates have started to diversity into the most lucrative preschool segment with the premier of "The Land Before Time" by Universal Studios in Spring 2007 and will launch a series of pre-school figures, playsets and plush toys. The Viva Piñata game with Microsoft Xbox is expected to be launched in FY12/08F. The company will also start distributing TMNT in China under with a local partner, which has point-of-sales in Shanghai.

**Property segment.**

- **Revaluation gain and higher rental income.** Operating profit surged 1.8x to HK\$261.4m, including a revaluation surplus of HK\$238.5m. The exceptional performance was mainly due to c.30% YoY increase in rental income as a result of adding higher profile tenants after a remodelling exercise over the past few years. The monthly rental rate rose from HK\$10-20/sq.ft. to HK\$30/sq.ft and is expected to increase further, though at a lesser extent in FY12/07F.

**Valuation.**

- **Forecast revised up.** We have revised our earnings upwards by 6-8% for FY12/07F to FY12/08F to reflect higher margins. The Group is in a net cash position of HK\$393.4m, or HK\$0.21 per share. We maintain our forecast and BUY rating, with a target price of HK\$1.5, a 34% discount to our estimated NAV per share of HK\$1.7. We believe Playmates is bottoming out, staging a sales comeback on its toys segment. The property segment is attractive with redevelopment potentials.