

## Company Update

# RM Group Holdings Limited <sup>8185 HK</sup>

## Get ready for a fruitful 2014!

- *RM Group's 1Q-3Q results for FY03/14 was negatively affected by one-off expenses including share-based payments and listing expenses, which cumulatively amounted to HKD22.7m during the 9-month period*
- *SG&A to sales ratio increased by 11.0ppt to 61.8% in 1Q-3Q FY03/14. However, we expect it will normalize in FY03/15, and the increase in marketing expenses will translate to higher revenue growth in the future*
- *We expect the company will see substantial growth in turnover and profit in 1Q FY03/15, due to the absence of listing expenses and new product launch*

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**Stock Data (8185 HK)**

Rating	Not Rated
Price (HK\$)	1.74
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	1.07-2.95
Market cap. (HK\$m)	896.1
Daily t/o (HK\$m)	1.6
Free float (%)	25.2

Source: Bloomberg

RM Group is principally engaged in the business of formulating, marketing, sales and distribution of health and beauty supplements in Hong Kong and Taiwan.

**What's New:** RM Group announced the quarterly results for 3Q FY03/14. During the 3-month period, the company's revenue was up by 27.6% YoY to HKD56.2m, mainly driven by the increase in the sales of health supplement and beauty supplement products, which were up by 31.8% YoY and 7.7% YoY respectively. Gross margin was 78.9%, which similar to the historical level. However, the company recorded an operating loss for the period due to higher SG&A expenses (3Q FY03/14: HKD32.4m vs. 3Q FY03/13:20.6m), higher share-based payments (HKD7.4m), and listing expenses (HKD11.1m). The company recorded a net loss attributable to shareholders of HKD9.6m in 3Q FY03/14, as compared to a net profit attributable to shareholders of HKD9.9m in the same period last year.

For 1Q-3Q FY03/14, the company's revenue was up by 10.7% YoY to HKD130.4m. The company recorded a net loss attributable to shareholders of HKD5.4m as compared to a net profit attributable to shareholders of HKD22.9m in the same period last year.

In fact, the company has announced a profit warning in late January, stating that the company is expected to record a loss for Q1-Q3 FY03/14. The loss was mainly due to an increase in listing expenses and share-based payments for share options granted. The loss, therefore, was within market expectation and should not be a surprise to the market.

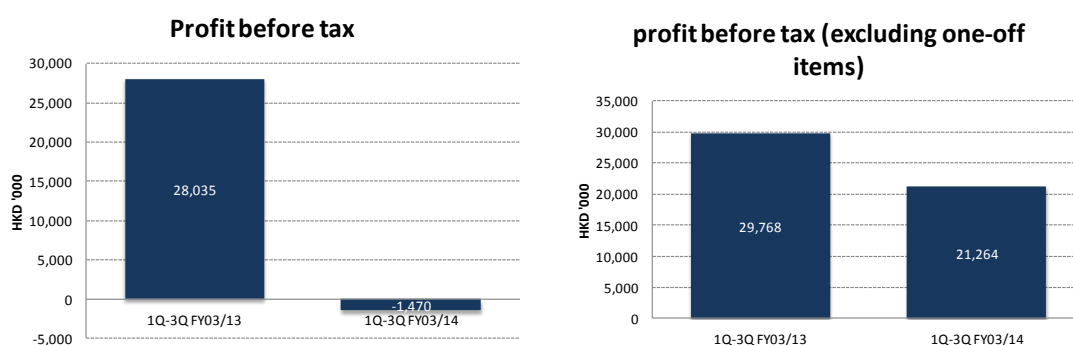
**Figure 1: Forecasts and Valuation**

	FY03/12	FY03/13	FY03/14E	FY03/15E	FY03/16E
	HKD '000	HKD '000	HKD '000	HKD '000	HKD '000
Revenue	158,793	163,767	175,259	189,680	207,663
Gross profit	126,344	129,010	128,710	148,861	163,118
Profit from operation	52,725	46,594	11,712	55,520	61,666
Net profit attributable to shareholders	43,032	39,264	9,172	45,309	49,047
Net profit attributable to shareholders (adjusted for listing expenses and share-based payment)	45,422	40,652	27,124	45,309	49,047
EPS - Basic (HK cents)			1.8	8.8	9.5
EPS - Diluted (HK cents)			1.7	8.2	8.9
P/E (x)	-	-	99.4	20.1	18.6
P/B (x)	-	-	5.6	4.9	4.4

Source: The company, SBI E2-Capital

**FY03/14 profit negatively affected by one-off expenses:** The company recorded share-based payments and listing expenses of HKD7.4m and HKD15.4m for the 1Q-3Q FY03/14. In fact, stripping off those one-off expenses the company would have recorded profit before tax of HKD21.3m during the 9-month period, as compared to HKD29.8m in the corresponding period last year. Similarly to other newly listed companies in HK, the company's P/L was negatively affected by the related listing expenses after its IPO. However, as those expenses were mostly one-off in nature, we believe the company will have a good chance to turn around next year.

Figure 2: Profit before tax (with and without one-off items)



Source: The company

**Health supplements continue to lead growth:** Health supplements, in which Royal Medic CS-4 is categorized, were up by 20.7% YoY to HKD99.4m in 1Q-3Q FY03/14, accounting for 76.2% of the company's total revenue during the period. We expect that health supplements will continue to lead growth as our financial model forecasts that this segment will grow by 8.4%, 9.4% and 11.0% in FY03/14, FY03/15, and FY03/16 respectively.

Figure 3: Revenue breakdown for 1Q-3Q FY03/13 & 1Q-3Q FY03/14

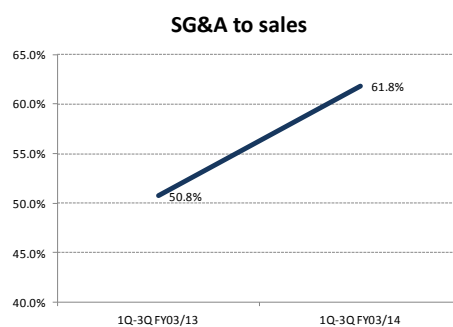
Revenue breakdown	1Q-3Q FY03/14 HKD'000	1Q-3Q FY03/13 HKD'000	YoY Change
<b>Health Supplements</b>			
Proprietary brands	80,125	71,790	12%
Private label brands	19,291	10,603	82%
	<b>99,416</b>	<b>82,393</b>	<b>21%</b>
<b>Beauty supplements</b>			
Proprietary brands	22,783	21,287	7%
Private label brands	7,583	13,570	-44%
	<b>30,366</b>	<b>34,857</b>	<b>-13%</b>
Others	639	558	15%
<b>Total</b>	<b>130,421</b>	<b>117,808</b>	<b>11%</b>

Source: The company

**Increases in marketing expenses will translate into higher turnover in the future:** The Company's SG&A to sales ratio increased by 11.0ppt to 61.8% in 1Q-3Q FY03/14 from 50.8% in 1Q-3Q FY03/13. The increase in SG&A was mainly due to increases in marketing expenses, which were up by HKD4.8m in 3Q FY03/14. Although it is true that the increase in marketing expenses will drag down profit during the period, we believe it will be a good investment and will have an overall positive effect on its future business, because i) turnover in 1Q-3Q FY03/14 was up by 10.7% YoY to HKD130.4m, being the testament of the effective marketing expenses; ii) the company will launch a number new health-care products, including 4 new products together developed with the CUCAMed, in FY03/15; and iii) its Taiwan business is in its initial stages (accounted for 1.1% of total revenue in 1Q-3Q FY03/14), and marketing expenses are expected to translate into higher turnover and thereby higher business growth in the future.

We also believe that the SG&A to sales ratio will normalize in FY03/15, due to cost containment measures implemented by the company, and the reduction of IPO related marketing expenses next year.

Figure 4: SG&A to sales ratio



Source: the company

**We expect the company will see strong growth in turnover and profit in 1Q FY03/15.** Based on the assumptions that health supplements will lead growth and will increase by 8.4% YoY, 9.4% YoY, and 11.0% YoY in FY03/14, FY03/15 and FY03/16, we expect the corresponding revenue of the company will increase by 7.0% YoY, 8.2% YoY, and 9.5% YoY to HKD175.3m, 189.7HKD m and HKD207.7m. We also forecast the corresponding net profit attributable to shareholders will be HKD9.2m, HKD45.3m, and HKD49.0m, respectively.

We expect the company will see a strong growth in its turnover and profit in 1Q FY03/15, because i) there will be no listing expenses in FY03/15, and ii) there will be a number of new products being launched in 1Q FY03/15, including 4 new products together developed with the CUCAMed. We believe the new products will gain popularity in the market and will contribute to the turnover and profit of the company.

**Valuation.** The international peers of the company, including Herbalife (HLF US), Nu Skin (NUS US), USANA (USNA US), FANCL (4921 JP), and Eu Yan Sang (EYSAN SP), are on average trading at a trailing 12-month historical P/E of 16.0x and a prospectively P/E of 32.1x for 2013.

Figure 5. Peer Comparison (International)

Name	Ticker	Market Cap (HK\$ m)	Trailing 12M EV/EBITDA	Price to EBITDA	2012 P/E (x)	2013E P/E (x)	P/book (x)	ROE (%)
FANCL	4921 JP	5,944.59	n.a.	12.25	n.a.	104.16	1.09	-4.96
Eu Yan Sang International	EYSAN SP	2,218.41	13.86	10.36	20.25	18.84	2.52	13.09
Herbalife Ltd.	HLF US	52,007.68	8.96	8.68	12.91	12.36	14.76	126.20
Nu Skin Enterprises	NUS US	35,252.61	10.40	8.92	15.63	12.86	6.02	46.23
USANA Health Science	USNA US	8,132.30	8.75	8.36	13.57	12.52	4.02	35.43
<b>Average</b>		<b>20,711</b>	<b>10.49</b>	<b>9.71</b>	<b>15.59</b>	<b>32.15</b>	<b>5.68</b>	<b>43.20</b>

Source: Bloomberg, SBI E2-Capital

As for HK-listed peers, there are six companies that are engaged in manufacturing and selling of healthcare products in HK and China. These companies include Wai Yuen Tong (897 HK), Tong Ren Tang (1666 HK), Beijing Tong Ren Tang Chines (8138 HK), CK Life Sciences International (775 HK), Besunyen (926 HK) and Reak Nutraceutical (2010 HK). On average, these companies are trading at a trailing 12-month P/E of 19.85x and a prospective P/E of 36.0x for 20113.

Figure 6. Peer Comparison (HK)

Name	Ticker	Mkt Cap (HK\$ m)	Trailing 12M EV/EBITDA	Price to EBITDA	2012E P/E (x)	2013E P/E (x)	P/book (x)	ROE (%)
Wai Yuen Tong Medicine	897 HK	618.47	10.98	9.31	2.99	n.a.	0.36	11.04
Tong Ren Tang Technologies	1666 HK	17,674.82	16.51	20.13	33.20	29.93	5.81	19.17
CK Life Sciences International	775 HK	7,977.19	18.03	15.25	39.71	n.a.	1.60	3.89
Besunyen Holdings	926 HK	604.23	n.a.	n.a.	n.a.	n.a.	0.38	-13.55
Beijing Tong Ren Tang Chines	8138 HK	9,229.60	n.a.	n.a.	n.a.	41.96	n.a.	n.a.
Reak Nutraceutical	2010 HK	2,043.93	1.53	2.11	3.51	n.a.	0.45	13.60
<b>Average</b>		<b>6,358</b>	<b>11.76</b>	<b>11.70</b>	<b>19.85</b>	<b>35.95</b>	<b>1.72</b>	<b>6.83</b>

Source: Bloomberg, SBI E2-Capital

Figure 7: Income Statement

	FY03/12 HKD '000	FY03/13 HKD '000	FY03/14E HKD '000	FY03/15E HKD '000	FY03/16E HKD '000
<b>Revenue</b>	<b>158,793</b>	<b>163,767</b>	<b>175,259</b>	<b>189,680</b>	<b>207,663</b>
Cost of good sold	(32,449)	(34,757)	-46,549	-40,819	-44,545
<b>Gross profit</b>	<b>126,344</b>	<b>129,010</b>	<b>128,710</b>	<b>148,861</b>	<b>163,118</b>
other revenue and other net income	31	1337	2,629	1,477	2,380
Selling, distribution and administrative expenses	-70,729	-82,110	-96,893	-94,818	-103,831
Listing expenses & share based payment	-2,921	-1,643	-22,734	0	0
<b>Profit from operations</b>	<b>52,725</b>	<b>46,594</b>	<b>11,712</b>	<b>55,520</b>	<b>61,666</b>
Finance costs	-131	-110	-97	-97	-97
<b>Profit before taxation</b>	<b>52,594</b>	<b>46,484</b>	<b>11,615</b>	<b>55,423</b>	<b>61,570</b>
Taxation	-9,562	-7,220	-2,443	-10,114	-12,522
<b>Profit attributable to shareholders</b>	<b>43,032</b>	<b>39,264</b>	<b>9,172</b>	<b>45,309</b>	<b>49,047</b>
EPS - Basic (HK cents)			1.8	8.8	9.5
- Diluted (HK cents)			1.7	8.2	8.9

Source: The Company

Figure 8: Ratio Analysis

	FY03/12	FY03/13	FY03/14E	FY03/15E	FY03/16E
<b>Growth (YoY)</b>					
Revenue	-	3.1%	7.0%	8.2%	9.5%
Gross profit	-	2.1%	-0.2%	15.7%	9.6%
Operating profit	-	-11.6%	-74.9%	374.1%	11.1%
Net profit	-	-8.8%	-76.6%	394.0%	8.3%
<b>Margin</b>					
Gross margin	79.6%	78.8%	73.4%	78.5%	78.5%
Operating margin	33.2%	28.5%	6.7%	29.3%	29.7%
Net profit margin	27.1%	24.0%	5.2%	23.9%	23.6%
<b>Other Ratios</b>					
Return on asset	48.1%	47.3%	4.7%	18.6%	17.5%
Return on equity	109.5%	101.8%	5.7%	24.5%	23.4%
<b>Valuation</b>					
P/E (x)	-	-	99.4	20.1	18.6
P/B (x)	-	-	5.6	4.9	4.4

Source: The Company

Figure 9: Segment Financials

	FY03/12 HKD '000	FY03/13 HKD '000	FY03/14E HKD '000	FY03/15E HKD '000	FY03/16E HKD '000
<b>Revenue breakdown by segments</b>					
<b>Health Supplements</b>					
Proprietary brands	105667	105168	114,244	125,154	139,052
Private label brands	3802	14914	15,958	17,235	18,958
<b>Beauty supplements</b>					
Proprietary brands	30256	27203	28,250	29,832	31,516
Private label brands	18528	15637	15,921	16,528	17,159
<b>Others</b>	540	845	887	932	978
<b>YoY Growth</b>					
<b>Health Supplements</b>					
Proprietary brands	-	0%	9%	10%	11%
Private label brands	-	292%	7%	8%	10%
<b>Beauty supplements</b>					
Proprietary brands	-	-10%	4%	6%	6%
Private label brands	-	-16%	2%	4%	4%
<b>Others</b>	-	56%	5%	5%	5%

Source: The Company

Figure 10: Balance Sheet

	FY03/12 HKD '000	FY03/13 HKD '000	FY03/14 HKD '000	FY03/15 HKD '000	FY03/16 HKD '000
<b>Non-current assets</b>					
Property, plant and equipment	16,303	16,868	16,944	16,628	15,921
Intangible asset	0	0	800	800	800
	16,303	16,868	17,744	17,428	16,721
<b>Current assets</b>					
Inventories	11,109	12,765	15,164	9,327	17,401
Trade and other receivables	27,304	32,572	25,047	37,313	30,960
Pledged bank deposit	0	5,000	0	0	0
Cash and cash equivalents	34,812	15,708	135,755	179,312	214,455
Tax recoverable	0	16	655	655	655
	73,225	66,061	176,622	226,607	263,470
<b>Current liabilities</b>					
Trade and other payables	21,694	13,202	23,405	32,351	42,114
Obligations under finance lease	90	47	0	0	0
Secured bank loans	4,020	3,491	3,221	3,221	3,221
Amounts due to related parties	2,418	26,529	0	0	0
Dividend Payable	0	0	4,586	22,654	24,524
Tax payables	21,076	0	0	0	0
Provisions	860	1,038	946	946	946
	50,158	44,307	32,157	59,172	70,805
<b>Non-current liabilities</b>					
Obligations under finance lease	47	0	0	0	0
Deferred tax liabilities	36	71	71	71	71
	83	71	71	71	71
<b>Net Asset</b>	<b>39,287</b>	<b>38,551</b>	<b>162,137</b>	<b>184,791</b>	<b>209,315</b>
<b>EQUITY</b>					
Equity attributable to owners of the Company					
Share capital	0	0	10	10	10
Reserves	39,287	38,551	162,127	184,781	209,305
<b>TOTAL EQUITY</b>	<b>39,287</b>	<b>38,551</b>	<b>162,137</b>	<b>184,791</b>	<b>209,315</b>

Source: The Company

Figure 11: Cash Flow Statement

	FY03/12 HKD'000	FY03/13 HKD'000	FY03/14 HKD'000	FY03/15 HKD'000	FY03/16 HKD'000
<b>OPERATING ACTIVITIES</b>					
Profit before taxation	52,594	46,484	11,615	55,423	61,570
Adjustments for:	0	0	0	0	0
Finance costs	131	110	97	97	97
Write down of inventories	1,962	1,147		0	0
Reversal of write-down of inventories	-453	-508	-92	0	0
Depreciation on property, plant and equipment	884	1,467	1,924	2,316	2,707
Bank interest income	-12		0	0	0
Net gain on disposal of property, plant and equipment	0	-1,246	0	0	0
	55,106	47,454	13,544	57,835	64,373
Changes in working capital					
Increase in inventories	-6,969	-2,295	-2,399	5,838	-8,074
Increase in trade and other receivables	-6,439	-5,268	7,525	-12,266	6,353
Decrease in amount due from a related party	278	0	0	0	0
Increase/(decrease) in trade and other payables	8,353	-8,492	10,203	8,947	9,763
Decrease in amounts due to related parties	-2,596	-2,389	0	0	0
(Decrease)/increase in provisions	-112	178	0	0	0
<b>CASH GENERATED FROM OPERATIONS</b>	<b>47,621</b>	<b>29,188</b>	<b>28,872</b>	<b>60,354</b>	<b>72,416</b>
Hong Kong profits tax paid	-133	-28,277	-3,082	-10,114	-12,522
<b>NET CASH GENERATED FROM OPERATING ACTIVITIES</b>	<b>47,488</b>	<b>911</b>	<b>25,789</b>	<b>50,240</b>	<b>59,893</b>
<b>INVESTING ACTIVITIES</b>					
Purchase of property, plant and equipment	-5,991	-2,886	-2,000	-2,000	-2,000
Proceeds from sale of property, plant and equipment	0	2,100	0	0	0
Increase in intangible assets	0	0	-800	0	0
Bank interest received	12	0	0	0	0
Increase in pledged bank deposit	0	-5,000	5,000	0	0
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>-5,979</b>	<b>-5,786</b>	<b>2,200</b>	<b>-2,000</b>	<b>-2,000</b>
<b>FINANCING ACTIVITIES</b>					
Proceeds from IPO			119,000	0	0
Repayment of secured bank loans	-515	-529	-270	0	0
Interests paid	-119	-104	-97	-97	-97
Decrease in amounts due to related parties	-29,921	-13,500	-26,529	0	0
Capital element of finance lease payments	-84	-90	-47	0	0
Interest element of finance lease payments	-12	-6	0	0	0
Dividend paid	0	0	0	-4,586	-22,654
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<b>-30,651</b>	<b>-14,229</b>	<b>92,057</b>	<b>-4,682</b>	<b>-22,751</b>
Net increase/ decrease in cash and cash equivalent	10,858	-19,104	120,047	43,557	35,143
cash and cash equivalent at the end of last period	23,954	34,812	15,708	135,755	179,312
Exchange rate effect	0	0	0	0	0
<b>cash and cash equivalent at the end of the current period</b>	<b>34,812</b>	<b>15,708</b>	<b>135,755</b>	<b>179,312</b>	<b>214,455</b>

Source: The Company

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