

JPM-pp1

Asia Pacific Equity Research

02 March 2015

Giordano (709 HK)

Neutral

FY14 Preview - reporting 3 March 2015

Price: HK\$3.87

02 Mar 2015

Price Target: HK\$3.70

PT End Date: 31 Dec 2015

Giordano will report its FY14 result on 3 March 2015 during the lunch break. The company will hold its briefing at 4:30pm Hong Kong time.

• **We forecast FY14 net profit of HK\$409m, down 38% y/y.** We expect sales to decline 4.7%. We forecast EBIT margin contraction of ~470bps to reflect ~300bps of gross margin contraction and operating leverage. We continue to expect the company's financial performance to be negatively impacted by: (1) Adverse FX movements; (2) Weak sales in core regions; (3) Operating margin pressure, particularly in high operating margin regions such as Hong Kong and Rest of Asia Pacific.

• **Key issues to look out for during result briefing.** (1) Current trading and outlook with respect to sales for each of the operating regions. (2) Outlook with respect to cash generation and dividend policy.

Table 1: Giordano: 2014 J.P. Morgan and consensus estimates

HKD in millions	FY13	FY14E	FY14E / FY13	1H14 (%chg y/y)	2H14E (%chg y/y)	FY14E - Consensus	JPMf vs. Consensus
Revenue	5,848	5,576	-4.7%	-5.9%	-3.4%	5,580	-0.1%
Gross Profit	3,551	3,216	-9.4%	-11.3%	-7.6%		
Operating Profit	804	502	-37.5%	-46.4%	-28.1%		
Net interest income	20	21	4.4%	-10.0%	18.9%		
Share of associates and JVs	79	68	-14.3%	-20.0%	-9.8%		
Other income	0	0	NM	NM	NM		
PBT	903	591	-34.5%	-43.6%	-25.2%		
Tax	-173	-135	-22.2%	-22.2%	-16.0%		
PAT	730	456	-37.5%	-46.8%	-27.6%		
Minority stake	-67	-47	-29.9%	-27.8%	-32.3%		
Net income to Equity Holders	663	409	-38.3%	-48.8%	-27.1%	404	1.3%
Gross Margin	60.7%	57.7%	(305 bp)				
Operating margin	13.7%	9.0%	(474 bp)				
Net Margin	11.3%	7.3%	(400 bp)				
Tax rate	19.2%	22.8%	362 bp				

Source: Company data, Bloomberg and J.P. Morgan estimates.

Table 2: Giordano: 2H14 J.P. Morgan and consensus estimates

HKD in millions	1H13	1H14	1H14 / 1H13	2H13	2H14E	2H14E / 2H13	2H14E - Consensus	JPMf vs. Consensus
Revenue	2,841	2,672	-5.9%	3,007	2,904	-3.4%	2,908	-0.1%
Gross Profit	1,765	1,565	-11.3%	1,786	1,651	-7.6%		
Operating Profit	414	222	-46.4%	390	280	-28.1%		
Net interest income	10	9	-10.0%	10	12	18.9%		
Share of associates and JVs	35	28	-20.0%	44	40	-9.8%		
Other income	0	0	NM	0	0	NM		
PBT	459	259	-43.6%	444	332	-25.2%		
Tax	-83	-59	-28.9%	-90	-76	-16.0%		
PAT	376	200	-46.8%	354	256	-27.6%		
Minority stake	-36	-26	-27.8%	-31	-21	-32.3%		
Net income to Equity Holders	340	174	-48.8%	323	235	-27.1%	230	2.2%
Gross Margin	62.1%	58.6%	(356 bp)	59.4%	56.8%	(255 bp)		
Operating margin	14.6%	8.3%	(626 bp)	13.0%	9.7%	(331 bp)		
Net Margin	12.0%	6.5%	(546 bp)	10.7%	8.1%	(264 bp)		
Tax rate	18.1%	22.8%	470 bp	20.3%	22.8%	251 bp		

Source: Company data, Bloomberg and J.P. Morgan estimates.

Investment Thesis

We believe Giordano faces a number of headwinds in the short to medium term: p1) the company is reporting weak sales in its core operating regions; 2) the company faces currency headwinds; and 3) the company is facing operating margin pressure in both Hong Kong and Rest of Asia-Pacific. We believe weak sales in HK and SE Asia will be the biggest drivers of EBIT margin compression for Giordano, given rental cost pressures and the importance of the SE Asian region. However, we recognize that Giordano is trading at a FY15E P/E of ~14x and a dividend yield of ~6%, which we believe provide valuation support.

Valuation

Our Dec-15 price target of HK\$3.70 is based on 13x our earnings forecasts for the year ending Dec-16, in line with the historical average forward P/E

for Giordano.

Risks to Rating and Price Target

Key upside risks include: 1) an improvement in the macroeconomic and retail environment in Giordano's markets; 2) an improvement in SSSG for Giordano; 3) any favourable movement in FX from a currency translation perspective; 4) any unforeseen reduction in sourcing costs or operating expenses; and 5) positive currency movement with respect to key FX exposure.

Key downside risks include: 1) a change in Giordano's dividend policy; 2) a significant downturn in the retail environment; 3) unforeseen sourcing cost pressures that in turn lead to gross margin contraction; and 4) an increase in the competitive intensity of apparel retail in the markets in which Giordano operates.

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
11-Dec-06	UW	4.09	4.00
22-Mar-07	UW	3.41	3.30
29-Mar-08	N	3.10	3.60
26-Mar-09	N	1.70	2.00
28-Aug-09	UW	2.14	2.00
26-Mar-10	OW	2.81	3.20
18-Jan-11	N	4.88	4.90
25-Mar-11	N	4.44	5.00
28-Jul-11	N	6.19	6.00
31-Aug-11	OW	6.45	7.50
12-Oct-11	OW	5.20	6.60
22-Mar-12	OW	6.49	7.00
02-Jul-12	OW	5.47	6.50
16-Aug-12	OW	5.36	7.00
15-Sep-12	OW	6.11	6.70
05-Dec-12	OW	6.87	7.70
16-Jan-13	OW	7.41	7.90
01-Mar-13	OW	7.80	8.40
15-May-13	OW	7.78	8.10
13-Aug-13	OW	7.87	8.40
31-Oct-13	OW	7.31	8.10
11-Feb-14	OW	5.75	6.70
27-Feb-14	OW	5.12	6.30
08-May-14	N	4.31	4.20
14-Aug-14	N	4.60	4.10
05-Nov-14	N	3.96	3.70

<http://gps-app.amer.jpmchase.net:6080/server/console/chart/?shareClassId=502083&shareClassServerId=4&chartDesignation=1&actionType=C>

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