

Daphne (210 HK)

FY14 results in line; 1Q15 SSS still weak

FY14 results in line Net profit fell 47% YoY to HK\$176m. 2H14 net profit came in at HK\$4m, lower than the HK\$19m in 2H13, and in line with the trend mentioned in the company's 4Q14 operational update released on Jan 22. FY14 revenue dropped 1% YoY. SSS declined 3.4% YoY. GM fell 0.5pp YoY to 55.4%. Excluding the HK\$120m inventory provision write-back (vs HK\$245m write-off in FY13), GM would have dropped 4pp to 54.2% driven by aggressive clearance of off-season products. Operating profit plunged 50% YoY due to deleveraging as SG&A expenses ratio increased 2.2pp. No final dividend was announced.

Performance by brand Profit for its core brands slumped 64% YoY to HK\$225m in FY14. This segment reported a HK\$40m loss in 2H14 mainly due to a 2.7pp YoY contraction in GM to 53.3%. We believe some off-season products were sold at very aggressive discounts in 2H14. However, its other brands turned profitable, with profit improving from a loss of HK\$86m in FY13 to a profit of HK\$18m, driven by 15% revenue growth and 7.3pp expansion in GM.

Inventory balance down 14% YoY Inventory turnover days in 2H14 declined 4 days YoY to 194 days (vs 208 days in 1H14). Inventory mix also improved. Off-season product inventories for the spring, autumn and winter seasons are at a healthy level. Net cash balance rose 32% YoY to HK\$752m. Management targets to lower inventory turnover days to less than 180 days by the end of FY15.

FY15 outlook 1) SSS has been weak in 1Q15. We estimate YTD SSS may be in the negative mid to high-single-digit range. Management expect SSS to improve in 2Q15 led by further market segmentation by product series with a wider price range and new celebrity advertising campaigns. 2) Management expects A&P expenses ratio to increase YoY by not greater than 0.5pp, still within 1-2% of revenue. 3) Driven by a healthier inventory mix and lower raw material costs, management expects GM to improve by 1-2pp YoY and a certain portion of GM expansion to pass through to a net profit margin gain. 4) Management targets to add 100-150 new stores in FY15, focusing on lower-tier cities. 5) The company has plans for capex of HK\$300-400m during the year, mainly for new stores and old store renovation.

Maintain Hold and cut TP to HK\$2.48 We revise down our FY15/16 earnings forecasts by 7%/10% on lower SSSG assumptions (from 4%/3% to 2%/3% in FY15/16). We expect GM to expand in FY15 as inventory destocking is almost complete. However, new product sales visibility remains low due to competition from online channels and mass market brands. 2Q15 SSS data will be key as a way of assessing customer response to its further segmented products. Daphne's shares have fallen 22% over the past three months, meaning the weak FY14 results are priced in, in our view. Share purchases by major shareholders or share buybacks would be positive catalysts. We cut our target price from HK\$2.60 to HK\$2.48, based on 0.75x P/B (previously 0.77x), to factor in our lowered FY15 ROE estimate of 5.5% (previously 5.9%).

Upside risks 1) Consolidation of Taobao market as sellers on the platform may be taxed; 2) ASP increase led by improving brand equity. **Downside risks** 1) weaker-than-expected SSS.

Stock valuation

	Turnover (HK\$ m)	Net profit (HK\$ m)	Core profit (HK\$ m)	Core EPS (HK\$)	EPS YoY (%)	Core P/E	Yield (%)	BPS (HK\$)	P/B	ROE (%)
2012	10,529	956	963	0.585	-4	3.9	8.0	2.9	0.8	21.7
2013	10,447	329	358	0.217	-63	10.4	3.5	3.1	0.7	7.3
2014	10,356	176	173	0.105	-52	21.6	1.5	3.1	0.7	3.4
2015E	10,712	286	286	0.173	65	13.0	2.3	3.3	0.7	5.5
2016E	11,078	312	312	0.189	9	11.9	2.5	3.4	0.7	5.8

Hold (maintained) Target price: HK\$2.48



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Source: Bioomber

Key data

Mar 25 close (HK\$)	2.26
Shares in issue (m)	1649.142
Major shareholder	Lucky Earn (24.3%)
Market cap (HK\$ bn)	3.7
3M avg. vol. (m)	5.2
52W high/low (HK\$)	4.10/1.86

Source: Bloomberg

Sources: Company data, GF Securities (HK) Note: Core profit excludes fair value change of financial assets and derivatives, impairment loss of intangible assets

V/EDec (HKS m) FY13 % Change 2111 2113 % Change 1114 1113 % Change Revenue 10.356 10,447 -1% 5.275 5.278 0% 5.081 5.168 -2% Cost of sales (4,618) (4,608) 0% (2,403) (2,425) -2% 2,862 2,872 2,825 2% 2,866 3,013 -5% Other income 84 95 -11% 41 58 -29% 42 36 18% Selling and distribution expenses (492) (480) 3% (247) (230) 8% (245) (250) -2% Operating profit 287 578 -50% 49 117 -58% 238 461 -48% Finance costs (34) (53) -36% (12) (27) -42% 3 111 -125% Associates and IVs (7) (3) 129% (5) 14 211 -411% %	0									
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Operating margin 2.8 5.5 (2.8) 0.9 2.2 (1.3) 4.7 8.9 (4.2) SG&A expenses ratio 53.4 51.3 2.2 54.3 52.4 1.9 52.6 50.1 2.5 Net margin 1.7 3.2 (1.5) 0.1 0.4 (0.3) 3.4 6.0 (2.6) Effective tax rate 1.7 28.0 (10.3) (49.2) 54.4 (103.6) 19.2 25.6 (6.3) Payout ratio 32.8 40.1 (7.3) - 114 1113 change Inventory days 194 198 change - 114 1113 change A/C receivables days 12 12 0 - 13 14 (1) A/C payable days 103 79 24 - 114 89 25	down/write back of inventories	54.2	58.2	(4.0)	52.7	56.6	(3.9)	55.8	59.8	(4.0)
SG&A expenses ratio 53.4 51.3 2.2 54.3 52.4 1.9 52.6 50.1 2.5 Net margin 1.7 3.2 (1.5) 0.1 0.4 (0.3) 3.4 6.0 (2.6) Effective tax rate 17.7 28.0 (10.3) (49.2) 54.4 (103.6) 19.2 25.6 (6.3) Payout ratio 32.8 40.1 (7.3) -	provisions)									
Net margin 1.7 3.2 (1.5) 0.1 0.4 (0.3) 3.4 6.0 (2.6) Effective tax rate 17.7 28.0 (10.3) (49.2) 54.4 (103.6) 19.2 25.6 (6.3) Payout ratio 32.8 40.1 (7.3) - 61.7 60.2 1.5 Inventory days 194 FY13 change - 1H14 1H13 change I/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25 FY14 FY13 change 114 89 25 114 89 25	Operating margin	2.8	5.5	(2.8)	0.9	2.2	(1.3)	4.7	8.9	(4.2)
Effective tax rate 17.7 28.0 (10.3) (49.2) 54.4 (103.6) 19.2 25.6 (6.3) Payout ratio 32.8 40.1 (7.3) 61.7 60.2 1.5 Inventory days 194 198 (4) 208 209 (1) A/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25	SG&A expenses ratio	53.4	51.3	2.2	54.3	52.4	1.9	52.6	50.1	2.5
Payout ratio 32.8 40.1 (7.3) 61.7 60.2 1.5 FY14 FY13 change 1114 1113 change Inventory days 194 198 (4) 208 209 (1) A/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25 FY14 FY13 change 1114 FY13 change	Net margin	1.7	3.2	(1.5)	0.1	0.4	(0.3)	3.4	6.0	(2.6)
FY14 FY13 change 1H14 1H13 change Inventory days 194 198 (4) 208 209 (1) A/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25 FY14 FY13 change 1H14 FY13 change	Effective tax rate	17.7	28.0	(10.3)	(49.2)	54.4	(103.6)	19.2	25.6	(6.3)
Inventory days 194 198 (4) 208 209 (1) A/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25 FY14 FY13 change 1H14 FY13 change	Payout ratio	32.8	40.1	(7.3)				61.7	60.2	1.5
A/C receivables days 12 12 0 13 14 (1) A/C payable days 103 79 24 114 89 25 FY14 FY13 change 1H14 FY13 change		FY14	FY13	change				1H14	1H13	change
A/C payable days 103 79 24 114 89 25 FY14 FY13 change 1H14 FY13 change	Inventory days	194	198	(4)				208	209	(1)
FY14 FY13 change 1H14 FY13 change	A/C receivables days	12	12	0				13	14	(1)
· · · ·	A/C payable days	103	79	24				114	89	25
Core brands 6,402 6,319 1% 6,234 6,581 -5%		FY14	FY13	change				1H14	FY13	change
	Core brands	6,402	6,319	1%				6,234	6,581	-5%
Net cash (HK\$m) 752 568 32% 614 589 4%	Net cash (HK\$m)	752	568	32%				614	589	4%

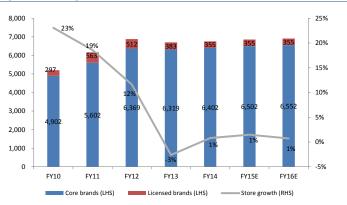
Figure 1: Results review

Sources: Company data, GF Securities (HK)





Figure 3: Store growth

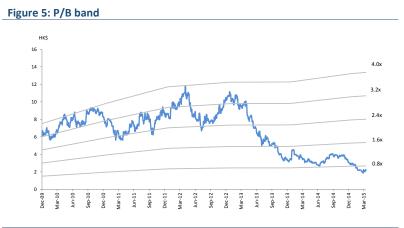


Sources: Company data, GF Securities (HK)

Sources: Company data, GF Securities (HK) estimates



Sources: Bloomberg, GF Securities (HK) estimates



Sources: Bloomberg, GF Securities (HK) estimates

Figure 6: Key assumptions

(HK\$ m)	FY12	FY13	FY14	FY15E	FY16E
Total revenue	10,529	10,447	10,356	10,712	11,078
growth %	22.8%	-0.8%	-0.9%	3.4%	3.4%
Core brands SSSG (%)	9.0%	-10.4%	-3.4%	2.0%	3.0%
Gross profit	6,229	5,838	5,738	6,113	6,360
Gross margin	59.2%	55.9%	55.4%	57.1%	57.4%
SG&A expenses ratio	47.1%	51.3%	53.4%	54.1%	54.1%
Operating profit margin	12.7%	5.2%	2.3%	3.5%	3.8%
Effective tax rate	25.4%	28.0%	17.7%	25.2%	25.2%
Net profit	956	329	176	286	312
growth %	2.4%	-65.6%	-46.5%	62.3%	9.2%
Core profit	963	358	173	286	312
growth %	-3.2%	-62.8%	-51.7%	65.3%	9.2%
Core profit margin	9.1%	3.4%	1.7%	2.7%	2.8%
Payout ratio	31.0%	40.1%	32.8%	30.0%	30.0%

Sources: Company data, GF Securities (HK) estimates

Figure 7: Financial statements

	Income Statement						Balance She	et			
'ear end Dec 31 (HK\$ m)	FY12	FY13	FY14	FY15E	FY16E	Year end Dec 31 (HK\$ m)	FY12	FY13	FY14	FY15E	FY:
evenue	10,529	10,447	10,356	10,712	11,078	Fixed assets					
ost of sales	(4,300)	(4,608)	(4,618)	(4,599)	(4,717)	PPE	1,184	1,188	1,377	1,411	1,4
oss profit	6,229	5,838	5,738	6,113	6,360	Land use rights	50	55	77	72	1,4
	0,225	3,838	5,750	0,115	0,500	Intangible assets	115	85	79	72	
her income	67	61	37	51	52	Asso & JV	115	8	6	(1)	
&A expenses	(3,866)	(4,395)	(4,550)	(5,791)		Others	234	245	191	196	2
-					(5,996)						
perating profit	1,342	545	240	373	416	Deferred tax assets	111 1,706	151 1,731	178 1,908	178 1,928	1,9
t finance cost	(6)	(19)	13	33	25		1,,,00	1,751	1,500	1,520	2,5
her gains/(losses), net	(20)	(57)	(28)	(8)	(8)	Current assets					
r value change of AFS and derivatives	0	(1)	3	0	0	Inventories	2,369	2,643	2,273	2,180	2,2
are of profit of asso and JV	(8)	(3)	(7)	(7)	(7)	A/C receivables	347	366	327	338	
ofit before tax	1,307	464	221	391	426	Other receivables	1,278	1,604	1,552	1,606	1,0
come tax expense	(333)	(130)	(39)	(99)	(107)	Entrusted loans	0	104	3	0	-,
n-controlling interests	(19)	(150)	(6)	(7)	(107)	Income tax recoverable	0	0	69	0	
t profit	956	329	176	286	312	Structured bank deposit	0	638	1,065	450	
	963	358	173	286	312		0	4	1,005	430	
re profit						Plegded bank deposit					
5 (HK\$)	0.58	0.20	0.11	0.17	0.19	Time deposit	0	33	0	0	
re EPS (HK\$)	0.58	0.22	0.10	0.17	0.19	Cash and cash equivalents	<u>1,495</u> 5,489	699 6,091	457 5,753	656 5,237	5,
owth rates (%)							5,485	0,091	5,755	3,237	5,
venue	23	(1)	(1)	3	3	Total assets	7,194	7,822	7,660	7,165	7,
re profit	(3)	(63)	(52)	65	9						
re EPS	(4)	(63)	(52)	65	9	Current liabilities					
						A/C payables	866	1,126	1,005	984	1,
argin & ratios (%)						Other payables	478	589	551	570	,
oss margin	59.2	55.9	55.4	57.1	57.4	Others	0	1	0	0	
U U	12.7	5.2	2.3	3.5	3.8	Bank borrowings	7	117	96	96	
OP margin 12.7 5.2 2.3 Core margin 9.1 3.4 1.7		2.7	2.8	CB	, 0	689	681	0			
ective tax rate	25.4	28.0	17.7	25.2	25.2		151	25	56	42	
yout ratio	31.0	40.1	32.8	30.0	30.0	Tax payables	1,502	2,548	2,389	1,692	1,
,		-					,	,	,	,	,
	Cash Flow Statemer					Non-current liabilities					
ar end Dec 31 (HK\$m)	FY12	FY13	FY14	FY15E	FY16E	Others	0	0	0	0	
						CB	640	0	0	0	
ofit before tax	1,307	464		391	426	Deferred tax liabilities	16	24	19	19	
are of profit of asso and JV	8	3		7	7		656	24	19	19	
preciation and amortization	261	313		329	336						
t finance cost	6	19		(33)	(25)	Equity					
hers	62	76		0	0	Shareholders' equity	4,825	5,044	5,058	5,252	5,
ange of working capital	(772)	(155)		26	(122)	Non-controlling interests	211	206	194	201	
x paid	(442)	(288)		(69)	(103)		5,037	5,250	5,252	5,453	5,
erating cash flow	431	433	668	650	519		5,057	5,250	5,252	5,155	5,
						Total liabilities & equity	7,194	7,822	7,660	7,165	7,
pex	(521)	(343)	(519)	(350)	(350)						
erest received	43	28	40	35	27		Financial rat				
hers	3	2	2	0	0	Year end Dec 31	FY12	FY13	FY14	FY15E	F
ange in entrusted loans	0	(104)	99	3	0						
ange in structured bank deposit	0	(633)	(427)	615	0	Current ratio	3.7	2.4	2.4	3.1	
ange in pledged deposit	0	(4)	(2)	0	0	Quick ratio	2.1	1.4	1.5	1.8	
ange in time deposit	0	(33)	33	0	0	Inventory turnover days	188	198	194	177	
esting cash flow	(475)	(1,088)	(775)	303	(323)	A/C payable turnover days	72	79	84	79	
-						A/C receivable turnover days	11	12	12	11	
ange of borrowings	0	110	(21)	0	0						
payment of CB	0	0	0	(681)	0	Asset turnover	1.5	1.3	1.4	1.5	
hers	(4)	(13)	0	0	0	Total assets/total equity	1.4	1.5	1.5	1.3	
erest paid	(21)	(22)	0	(1)	(1)	Net cash (HK\$m)	848	568	752	1,017	1,:
vidend paid	(297)	(247)	(92)	(72)	(90)	, /				,	_,
are issue	45	(247)	(52)	0	(50)	Core ROE (%)	21.7	7.3	3.4	5.5	
nancing cash flow	(277)	, (165)	(113)	(754)	(91)	Core ROA (%)	14.1	4.8	2.2	3.9	
	(004)	(820)	(219)	199	105						
et change of cash flow prex changes	(321) 20	25	(213)	0	0						

Sources: Company data, GF Securities (HK) estimates

Rating definitions

Benchmark: Hong Kong Hang Seng Index Time horizon: 12 months

Company ratings						
Buy	Stock expected to outperform benchmark by more than 15%					
Accumulate	Stock expected to outperform benchmark by more than 5% but not more than 15%					
Hold	Expected stock relative performance ranges between -5% and 5%					
Underperform	Stock expected to underperform benchmark by more than 5%					
Sector ratings						
Positive	Sector expected to outperform benchmark by more than 10%					
Neutral	Expected sector relative performance ranges between -10% and 10%					
Cautious	Sector expected to underperform benchmark by more than 10%					

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