

自然美 (157)

买入 (首次覆盖)

行业：美容

价值与美丽结合

我们首次覆盖内地发展成熟的护肤及美容生产商自然美。集团拥有完整的产品系列、强劲的研发能力、训练有素的美容师，以及庞大的销售网络。集团的业务能抵御经济周期起伏，同时连续 12 年创造自由现金流，足证其商业模式成功。近期的股权重组将有助其长远业务增长。我们建议买入，目标价 1.02 元。

完整产品系列配合强劲研发能力。自然美共有 352 种产品，涵盖护肤、美容、香熏、化妆及保健食品。这些产品各有特定功效及为不同年龄和皮肤情况的人而设。截止今年 10 月底，集团推出共 27 样新产品，包括全新的医学美容产品。集团持续推出高质素及具成交效益的新产品将推动其盈利增长。

庞大销售网络及训练有素的美容师。截至今年 6 月底，自然美共有 1,078 间加盟水疗中心，其中四分之三位于内地。这些水疗中心由加盟商及受培训的美容师经营，他们透过为客人提供面部及身体护理服务使用及销售自然美产品。集团正鼓励加盟商于三、四线城市开设小型水疗中心，以进一步扩展其销售网络。

具差异性并能抵御经济周期起伏的商业模式。自然美不单是一家护肤品生产商，而是透过加盟商为客人提供产品加服务的组合。这让集团享有高客户黏度、低资本支出以及低推广开支，其创造现金能力证明此模式成功。

评级买入，目标价 1.02 港元。目标价是以集团 17 财年预期 13 倍市盈率计算，这相当于其过去 5 年平均市盈率及相对丽丰(4137 TT) 23% 的折让。现金流折现法亦支持此估值。

主要风险：竞争较预期大；产品销售较预期少。

(百万港元)	14财年	15财年	16财年 预测	17财年 预测	18财年 预测
收入	506	507	498	529	582
毛利	389	397	372	391	434
经营利润	116	170	204	211	235
报告利润	71	137	151	156	174
经常性利润	100	141	145	156	174
经常性利润增长率 (%)	85%	41%	3%	8%	12%
每股经常性利润 (分港元)	5.0	7.0	7.2	7.8	8.7
经常性市盈率 (倍)	17.5	12.4	12.1	11.1	10.0
经常性市账率 (倍)	2.1	2.2	2.4	2.6	2.7
股息率 (%)	4.6	8.8	9.3	9.6	10.8
股本回报率 (%)	12.7	18.7	20.7	24.2	28.6
净债务股本比	(75.4)	(68.6)	(76.5)	(75.6)	(72.4)

来源：公司、中投证券

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目标价与评级

6-12 个月目标价： 1.02 港元 (+18%)

当前股价： 0.86 港元

评级调整： 首次覆盖

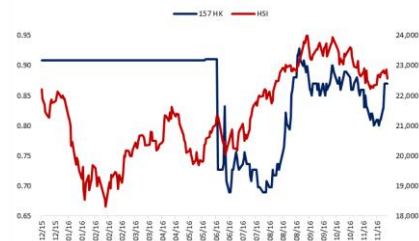
公司简介

制造及销售护肤、美容及香熏产品及提供肌肤护理、美容及 spa 服务以及肌肤护理顾问服务及美容培训。

基本数据

总股本 (百万股)	2,002
总市值 (百万港元)	1,742
平均成交(百万港元)	0.8
52 周股价波幅	0.624-0.984
主要股东	Next Focus (73.33%)

股价表现



相关报告

Natural Beauty (157 HK)

BUY (Initiation)

Sector: Cosmetics

Value and Beauty Converge

We initiate coverage on Natural Beauty (NB), a well-established skin-care and cosmetics products manufacturer in China. It has a resilient business model powered by a comprehensive product line, strong R&D capability, well-trained beauticians and an extensive distribution network. The model proves successful by 12 consecutive years of free cash flow generation. Recent shareholding restructuring will facilitate long-term business growth. We initiate BUY with an HKD1.02TP.

Comprehensive product line with strong R&D capability. NB has 352 types of products covering skin-care, beauty, aroma-therapeutic, make-up and health supplements. These products have specific functions and tailored to women of different ages and different skin conditions. By end-Oct 16, the Group launched 27 new products, including new medical cosmetology products. Continuous launch of new products will drive sales growth. The Group continues to create high-quality beauty and skin-care products in a cost-effective manner, driving its earnings growth.

Well-trained beauticians in extensive distribution network. By end-Jun 16, the Group had 1,078 franchised spas, of which third-fourths in mainland China. These spas are run under the brand of NB by well-trained franchisees and beauticians who effectively distribute the Group's products through facial and body treatment to customers. NB is penetrating into tier 3 and tier 4 cities by encouraging franchisees to set up mini spas to further expand the network.

Resilient business model with high differentiation. NB is more than just a skin-care manufacturer as it provides customers with a bundle of products and services through franchisees. It has high customers' stickiness, low CAPEX and low advertising and promotion expenses. The model proves successful by its cash generation capability.

Initiate BUY with a HK\$1.02 TP. Our TP is derived by using 13x FY17F PER, which is equivalent to its 5-year mean, and 23% discount from its closest listed peer, Chiltina (4137 TT). The TP is supported by DCF methodology.

Key Risks: Keener-than-expected competition; weaker-than-expected product sales

Research Analyst

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Target Price and Rating

 6-12m TP : **HK\$1.02 (+18%)**

 Current Price : **HK\$0.86**

 Rating Change: **Initiation**

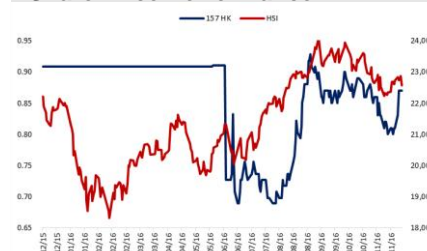
Company description

Manufacture and selling of skin care, beauty and aroma therapeutic products and provision of skin treatments, beauty and spa services and skin care consulting and beauty training.

Basic Information

No. of shares (m)	2,002
Market Cap (HKDm)	1,742
Avg turnover (HKDm)	0.8
52-week range (HKD)	0.624-0.984
Major shareholders	Next Focus (73.33%)

Share Price Performance



Related Research Reports

(HKDm)	FY14	FY15	FY16F	FY17F	FY18F
Revenue	506	507	498	529	582
Gross Profit	389	397	372	391	434
EBIT	116	170	204	211	235
Reported net profit	71	137	151	156	174
Recurring net profit	100	141	145	156	174
Recurring net profit growth (%)	85%	41%	3%	8%	12%
Recurring EPS (cents)	5.0	7.0	7.2	7.8	8.7
Recurring P/E (x)	17.5	12.4	12.1	11.1	10.0
P/B (x)	2.1	2.2	2.4	2.6	2.7
Dividend Yield (%)	4.6	8.8	9.3	9.6	10.8
ROE (%)	12.7	18.7	20.7	24.2	28.6
Net debt to equity (%)	-75.4	-68.6	-76.5	-75.6	-72.4

Source: Company data, CIS(HK)

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Comprehensive product lines with strong R&D capability

Comprehensive product lines. NB has 6 major product lines, namely NB-1, Bio-tech, Oriental Herbal, AnMi, Essence Oils and Health and Food Supplements, which range from facial and body care to food supplements. Consistent with the Group's core value of 'Nature is the source of Beauty', the products are all made of natural ingredients, mainly plant extracts.

Under these 6 product lines, the Group has developed a broad range of more than 352 types of products which have specific functions and tailored to women of different ages and different skin conditions. Major functions include anti-wrinkle, skin whitening, skin refining, skin moisturizing, skin pH balancing, deep facial cleansing, health care and so on. NB's product effectiveness has been proved over a long period of time. According to a market study on China's spa industry conducted by Synovate in 2010, 92% of customers and 93% of franchisees were satisfied with NB's product quality and effectiveness.

Take its best-selling and time-tested product line, NB-1, as an example. It is a premium product line that targets mature Asian women with high income, with prices ranging from Rmb450 to 5,000. The products are made of US patented Stem Cell Technology (SCT) ingredients and natural plant extracts which refine and whiten skin, and prevent wrinkles.

Figure 1: Features of product lines

	NB -1 御妍	Bio-tech 生化	Oriental Herbal 汉方	Yam 山药	AnMi 安蜜	Essence Oils 香熏精油	Health and Food Supplements 保健品
SKUs	68	47	95	9	7	41	35
Major functions	Anti-wrinkle Skin refining Skin whitening	Skin whitening Skin refining Skin pH balancing	Skin whitening Skin refining Skin pH balancing	Anti-wrinkle Skin refining	Skin moisturising Facial cleansing	Health care Skin refining Skin moisturisation	Health care
Target customer	Asian women >35	Asian women >22	Asian women >22	Asian women >35	Asian women >18	General	General
Positioning	High-end	Middle- to High-end	Low- to Middle-end	Middle- to High-end	Low- to Middle-end	High-end	Middle- to High-end
Ingredients	Bio-tech ingredients and natural plant extracts	Bio-tech ingredients and natural plant extracts	Natural plant extracts with Chinese herbs	Natural plant extracts	Plants, animals and minerals	Natural plant extracts	Natural plant extracts
Price (Rmb)	500 - 8,900	250 - 800	100 - 350	520 - 2,250	100 - 250	350 - 1,500	NB1: 380 - 1,600 Bio: 100 - 500
Remarks	Best selling product portfolio US patented Stem Cell Tech (SCT) ingredients	\	\	Use of Mexican yam	Basic skin care line for counter channel	Used with European style (lymph) massage and Chinese medicine (five elements)	Preventive, Medication products Ingredients imported from Europe, the US and Australia

Source: Company, CIS (HK)

Figure 2: Ace products

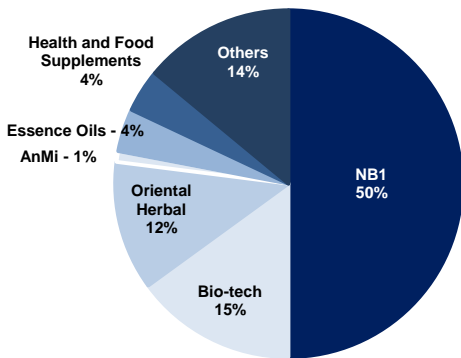


Source: Company, CIS (HK)

Being the core product line, NB-1 accounted for half of the Group's 1H16 revenue. The second and third largest product lines in terms of revenue were Bio-tech and Oriental Herbal respectively, targeting young Asian women. These 3 product lines represent more than three-fourths of NB's total revenue.

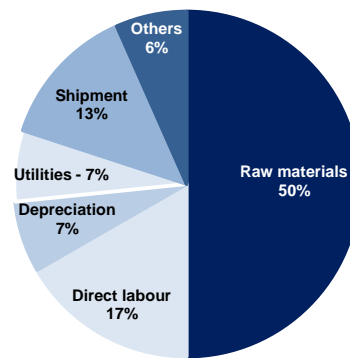
The Group enjoys high GPM (78% on 5-year average) due to low and steady COGS. Half of its COGS was raw materials, mainly natural plant extracts. About 90% of the raw materials originated from Taiwan, which are re-exported through Hong Kong to Mainland China. Direct labour and Shipment combined represented 30% of the COGS. Depreciation and Utilities only accounted for 7% of the COGS respectively.

Figure 3: 1H16 revenue breakdown by product lines



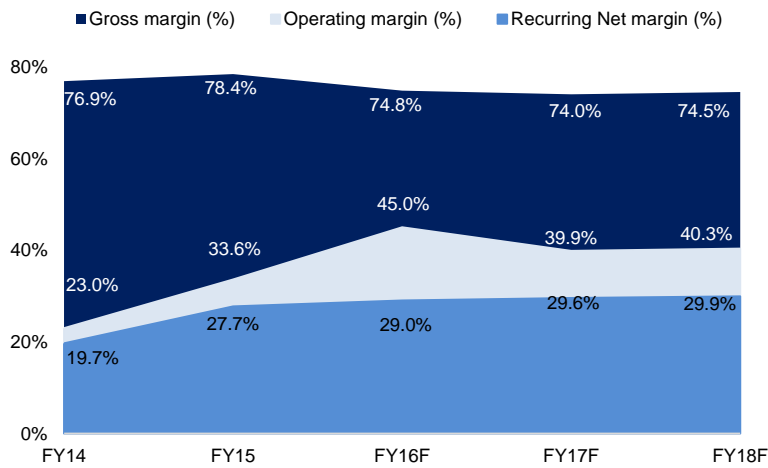
Source: Company, CIS (HK)

Figure 4: 1H16 COGS breakdown



Source: Company, CIS (HK)







Figure 5: Gross, Operating and Recurring net margins



Source: Company, CIS (HK)

Strong R&D supports new product launch. To maintain its competitive edge, the Group places strong emphasis on R&D to improve the quality of existing products and develop new products. Collaborating with overseas skin-care companies, NB's R&D is composed of overseas consultants specializing in cosmetics, medicine, pharmacy and bio-chemistry. By the end of Oct 16, the Group launched 27 new products, including a new product line of medical cosmetology called STREMARK in mid-16. All the new products contributed HKD62m of sales, with R&D costs amounting to HKD3.4m. Led by Chairperson Dr. TSAI Yen-Yu, the Group continues to create high-quality beauty and skin-care products in a cost-effective manner, driving its earnings growth.

Figure 6: New products in 2016

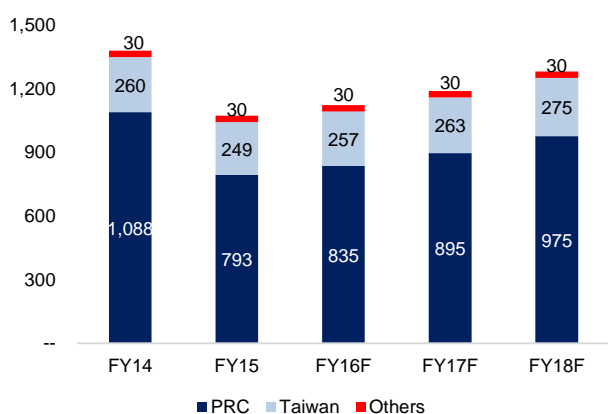
	NB-1 Plus Brightening and Repair Essence	y-PGA Hydrating Complex Serum
2Q16		
	Moisturizing Lipstick	Essential Oil Lip Gloss
3Q16		
	Yam Collagen Firming Crème	Yam Collagen Firming Essence
4Q16		

Source: Company, CIS (HK)

Well-trained beauticians in extensive distribution network

The Group operated a large and extensive retail network in mainland China, with concentration in Tier 1 and 2 cities. Stores in Tier 1 cities such as Shanghai (113), Beijing (55) and Nanjing (34) amounted to 254; Tier 2 cities such as Suzhou (43) and Fuzhou (21) amounted to 532. As these cities are relatively well-developed and wealthier, people have higher disposable income and demand for beauty services, facilitating the Group's rapid expansion.

Figure 7: Number of stores



Source: Company, CIS (HK)

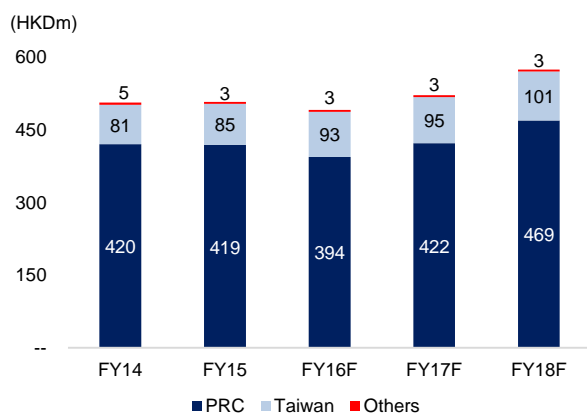
Figure 8: Store network



Source: Company, CIS (HK)

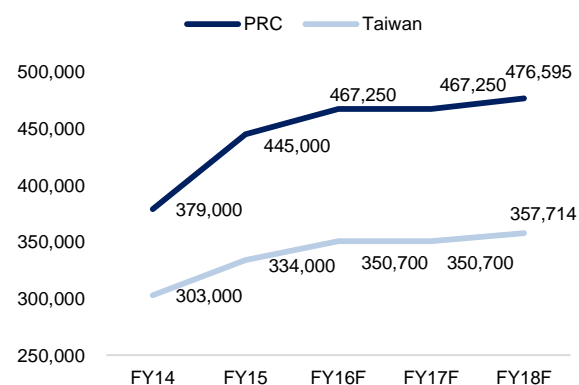
Mainland China is the Group's largest market in terms of revenue and the number of stores. In 1H16, 81% of revenue was generated on the mainland, 18% from Taiwan and the remainder from other markets. As for the number of stores, the Group had 1,078 stores as of 30 Jun 16, of which 798 (74%) were in mainland China, 250 (23%) in Taiwan and 30 (3%) in HK, Macau and Malaysia.

Figure 9: Revenue by geographical breakdown



Source: Company, CIS (HK)

Figure 10: Average sales per store



Source: Company, CIS (HK)

Among the stores, 98% of them are operated on franchise basis where selected franchisees pay a one-off deposit of Rmb5,000-10,000 and they can operate spas under the brand of NB. Products sold by the Group to franchisees are made on non-consignment basis. The locations of stores established by franchisees are subject to the Group's approval, and the franchisees are required to sell or use exclusively NB's products in the beauty centers. The stores offer a wide range of services including facial treatment, hydrotherapy, body care and skin care analysis. The store ownership is highly diversified that top 5 franchisees operate in total 15 stores only.

The Group in turn provides training to the beauticians so as to ensure their service quality and product knowledge. NB divides its mainland China store network into five regions, namely Eastern, Southern, Western, Northern and Central China, and assign a regional training team for each region. The headquarter organizes national training activities at least once a quarter, and regional trainers provide training sessions covering product updates and skills training to the beauticians every month. This is particularly important as it not only enhances product knowledge and skills, but also promotes corporate value and offer support to the franchisees.

Figure 11: Spa interior



Source: Company, CIS (HK)

Penetration into tier-2 & -3 cities

The Group plans to further expand its store network by 50% or around 500 stores in 5 years. The rationale behind the strategy is 'Suburbs around cities' where the expansion will mainly concentrate in tier 2 and tier 3 cities in mainland China. It is due to keen competition in tier 1 cities and increasing income and beauty treatment awareness in lower tier cities.

To accelerate the penetration into the cities, NB encourages franchisees to set up 'mini spas'. Unlike the traditional spas offering a full range of services, the mini spas only focus on facial treatment. The area required is able to reduce to 80m² and the set up costs will be as low as Rmb150,000. Franchisees can not only capitalize on the well-established brand and the complete product line of NB, they are also provided with comprehensive training in facial treatment skills and store management. This strategic store type facilitates individuals who are interested in setting up their own beauty salons.

Resilient business model with high differentiation

NB is characterized by its business model. The Group manufactures a wide range of skin care, beauty, aroma-therapeutic, make-up products and health supplements, all under the brand of NB. These products are mainly sold to its franchised spas, which are obliged to use the brand's products throughout the facial and body treatment by well-trained beauticians. Moreover, beauticians will also sell the products to the products to customers for their daily use.

It is more than just a skin-care and cosmetics manufacturer in the following areas:

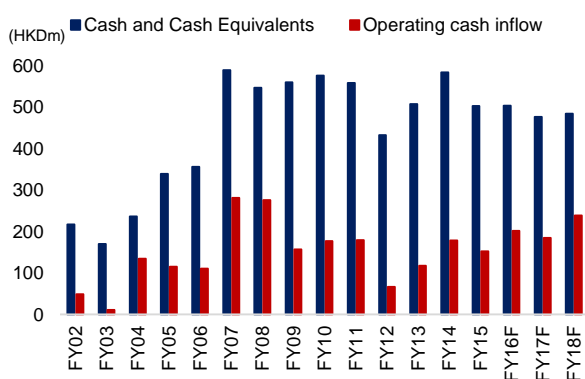
- a) **Products bundling with services.** When customers go to the stores for the first time, they are suggested to perform skin care analysis. It helps beauticians understand their customers' face skin quality and the problems facing them. The beauticians can thus tailor made skin treatment and choose products suitable for the customers. As the facial scanned images are kept in stores, customers are able to monitor the progress by comparing its skin quality before and after the treatment, which boosts their confidence in NB's products and services. The products sold are supported by spas' services, differentiating the Group from general cosmetic manufacturers or beauty parlors.
- b) **High customer stickiness.** These beauticians are trained by the Group for its beauty treatment skills and product knowledge. Throughout the beauty treatment process, the beauticians have intimate contact and emotional communication with the customers, which is easier for them to establish close relationships and trust. It in turn gradually increases customers' stickiness to the products and the brand. These loyal engaged customers repeatedly consume NB's services and products, and are likely less price sensitive, supporting the Group in the long run.
- c) **Low Advertising and Promotion expenses.** In 2015, advertising and promotion (A&P) expenses amounted to HKD33.8m, representing only 6.7% of the Group's revenue. We expect FY16F A&P to further decline to 5% of revenue. Instead of commercials on TV or the internet, NB's A&P are largely based on word of mouth. Money was mainly spent on supporting franchisees to increase sell-through activities, such as customer events, indoor salons and roadshows. It will help franchisees to strengthen relationships with their customers and maintain a healthy inventory level. On the other hand, in order to increase exposure to young customers, the Group tries to boost its online presence by establishing its official WeChat account as a first step. It serves a platform for attracting new members by product coupons and skin-care advice column. The Group can then direct the members to stores for services, as a B2B2C model.

Resilience through economic cycles. The model is highly resilient through economic cycles and proves successful over time. Its major customers are women who desire to improve their appearance. The demand for facial and body care is relatively less influenced by macro environment.

In the past 14 years of listing, the Group generated operating cash inflow in every single year, totaling HKD2b. The operating cash generated was not adversely affected by economic downturn in years like 2003 and 2008. Moreover, NB's business model requires low CAPEX. The average annual CAPEX over the past 14 years since listing was merely HKD32m. As a result, the Group was able to generate free cash flow in the past 13 out of 14 years.

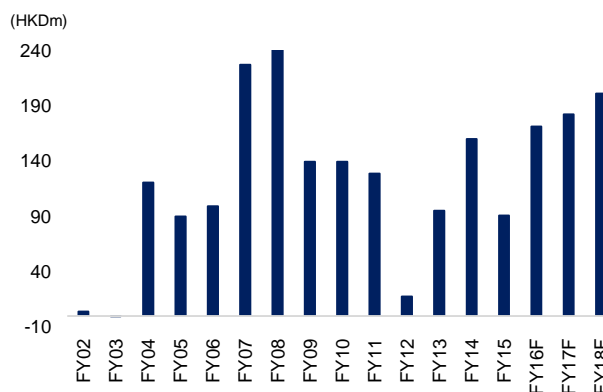
The only year which had negative free cash flow was 2003. The total amount of free cash flow generated reached HKD1.6b. The consistent cash generating capability shows its business model is highly resilient of economic cycles where it can maintain profitability in spite of macro headwinds.

Figure 12: Cash level and CFO



Source: Company, CIS (HK)

Figure 13: Free cash flow since listing



Source: Company, CIS (HK)

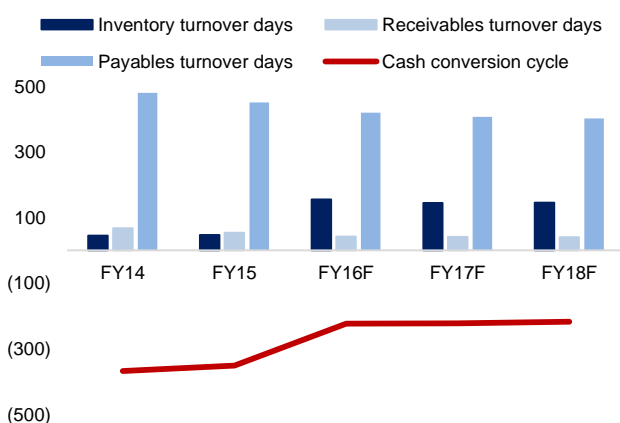
Financials

With solid financials where it has no debt and HKD564m of cash as at 30 Jun 16, NB's cash level is approximately one-third of its market capitalization. The high cash level is due to its strong cash generating capabilities. The Group generated net operating cash inflows in the past 14 consecutive years since its listing. As mentioned, the Group's CAPEX is low. We expect it to be HKD25m, HKD60m and HKD80m from FY16 to FY18.

Given it is basically a cash business, the Group has a small amount of HKD54m trade and other receivables in FY15, representing about 11% of its FY15 revenue. Inventories are relatively low and amounted to HKD47m in FY15, equivalent to 9% of FY15 sales. With large trade and other payables, the Group had a negative cash conversion cycle of 255 days in FY15.

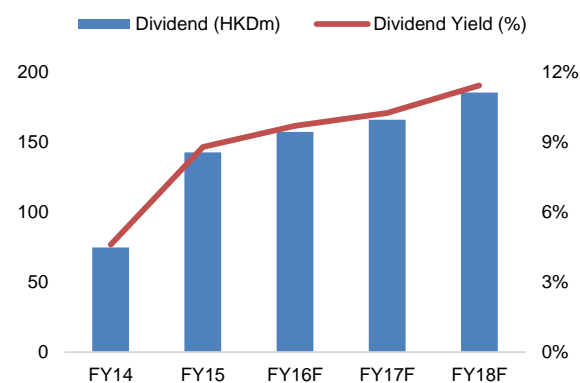
High cash level coupled with strong operating cash flow allows the Group to maintain high payout ratio and dividend yield. Except 2013, NB's payout ratio averaged at 127% over the past 14 years. FY15 dividend yield was 8.8%, and we expect its FY16F yield to reach 9.7% on moderate earnings increase.

Figure 14: Turnover days and Cash conversion cycle



Source: Company, CIS (HK)

Figure 15: Dividend and Dividend yield



Source: Company, CIS (HK)

Valuation

Peer Comparisons

The Group offers customers a bundle of products and services, delivered through well-trained beauticians in its extensive franchised spa network. It has no direct peers among the HK-listed companies. Skin-care product manufacturers like L'Occitane (973 HK) and China Child Care (1259 HK) produce products and distribute through wholesalers. Beauty salons operators such as Modern Beauty (919 HK) and Perfect Shape (1830 HK) focus on service provision.

The closest peer is Taiwan-listed Chiltina (4137 TT), which manufactures skin-care and beauty products and has a large franchised spa network of >3,000 stores in China. The major difference is Chiltina engages more in direct sales of products, where NB mainly sold its products through customers' consumption in spas.

According to a market study conducted by Synovate in 2010, NB was ranked No.1 in terms of brand awareness among spas in China, and Chiltina No.2. Moreover, NB has higher gross margin, net margin and dividend yield than Chiltina. Nevertheless, Chiltina's market capitalization and recurring net profit are 60% and 55% higher than NB. NB has been trading at 23% discount of PER to Chiltina in the past 3 years comparable period, mainly due to faster earnings growth of the latter.

Figure 16: Peer comparison table I

Company	Ticker	Price	Mkt Cap (HKDm)	3-mth		P/E			P/B	EPS (YoY%)			PEG(x)	Dvd yld	
				avg t/o (HKDm)	Hist	FY1	FY2	FY1		FY1	FY2	FY3		Hist(%)	FY1(%)
NATURAL BEAUTY	157	HK	0.86	1,722	0.8	12.2	11.9	11.0	2.4	2.8	8.2	11.5	4.3	8.8	9.3
<u>Skin-care products</u>															
LOCCITANE	973	HK	15.10	22,302	11.9	20.9	21.4	19.4	2.9	-12.2	9.3	10.4	-1.8	1.9	1.9
CHINA CHILD CARE	1259	HK	0.55	556	0.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.0	n.a.
Average				11,429	6.4	20.9	21.4	19.4	2.9	-12.2	9.3	10.4	-1.8	0.9	1.9
<u>Beauty salons</u>															
MODERN BEAUTY SALON	919	HK	0.39	341	0.4	33.4	n.a.	n.a.	n.a.	-79.4	n.a.	n.a.	n.a.	2.1	n.a.
PERFECT SHAPE BEAUTY	1830	HK	0.58	651	1.2	7.3	n.a.	n.a.	n.a.	-4.6	n.a.	n.a.	n.a.	13.6	n.a.
SAU SAN TONG	8200	HK	0.10	175	0.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.0	n.a.
Average				389	0.6	20.4	n.a.	n.a.	n.a.	-42.0	n.a.	n.a.	n.a.	5.2	n.a.
<u>Health supplements</u>															
RM GROUP	932	HK	3.41	1,803	14.4	51.0	n.a.	n.a.	n.a.	-64.7	n.a.	n.a.	n.a.	0.0	n.a.
REAL NUTRICEUTICAL	2010	HK	0.61	971	2.0	2.3	n.a.	n.a.	n.a.	-46.6	n.a.	n.a.	n.a.	9.1	n.a.
AUSUPREME	2031	HK	0.44	330	6.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Average				1,035	7.5	26.7	n.a.	n.a.	n.a.	-55.6	n.a.	n.a.	n.a.	4.5	n.a.
<u>Taiwan-listed peers</u>															
CHILTINA	4137	TT	35.23	2,800	161.9	23.4	12.6	17.0	3.0	54.0	-21.4	-26.3	0.2	2.9	4.5
JOURDENESS GROUP	4190	TT	20.55	1,256	35.1	21.3	18.5	15.0	3.6	10.4	-29.7	23.7	1.8	3.6	5.9
Average				2,028	98.5	22.4	15.5	16.0	3.3	32.2	-25.6	-1.3	1.0	3.3	5.2

Source: Company, CIS (HK)

Figure 17: Peer comparison table II

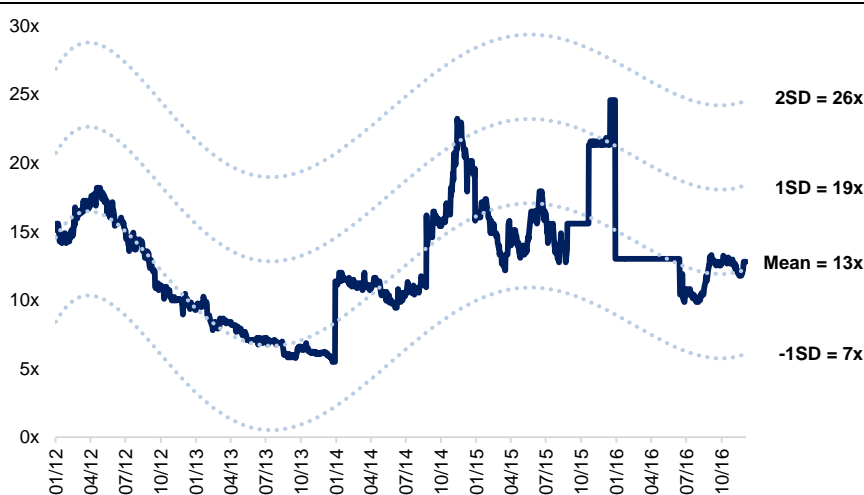
Company	Ticker	Revenue		Recur. net profit		Net gearing	Unlev Beta	Gross Margin	Net Margin	ROE (%)			Sh px 1-mth (%)	Sh px 3-mth (%)
		Hist (HKDm)	FY1 (HKDm)	Hist (HKDm)	FY1 (HKDm)					Hist(%)	FY1(%)	FY2(%)		
NATURAL BEAUTY	157	507	498	141	145	-68.6	0.4	78.4	27.7	18.7	20.7	24.2	-2.2	13.0
Skin-care products														
L'OCCITANE	973	10,988	10,988	945	1,031	-39.3	n.a.	82.8	8.6	12.9	14.1	14.3	-7.2	-7.9
CHINA CHILD CARE	1259	1,127	n.a.	-62	n.a.	-65.1	1.1	39.3	-5.5	-3.5	10.7	11.7	-5.2	18.3
Average		6,058	10,988	442	1,031	-52.2	1.1	61.0	1.5	4.7	12.4	13.0	-6.2	5.2
Beauty salons														
MODERN BEAUTY SALON	919	775	n.a.	13	n.a.	-226.5	n.a.	96.8	1.6	7.6	n.a.	n.a.	8.1	2.6
PERFECT SHAPE BEAUTY	1830	879	n.a.	130	n.a.	-56.0	n.a.	n.a.	14.8	27.1	n.a.	n.a.	-25.0	-26.0
SAU SAN TONG	8200	1,694	n.a.	-4	n.a.	-51.1	0.6	10.9	-0.2	-0.8	n.a.	n.a.	-6.1	-24.6
Average		1,116	n.a.	46	n.a.	(111.2)	0.6	53.8	5.4	11.3	n.a.	n.a.	(7.7)	(16.0)
Health supplements														
RM GROUP	932	190	n.a.	10	n.a.	-36.4	0.4	77.4	5.5	5.8	n.a.	n.a.	82.8	70.3
REAL NUTRICEUTICAL	2010	2,531	n.a.	495	n.a.	-34.5	0.7	65.4	19.6	8.1	n.a.	n.a.	-9.0	-15.3
AUSUPREME	2031	211	n.a.	12	n.a.	-30.3	0.1	85.5	5.8	20.4	n.a.	n.a.	-9.1	n.a.
Average		977	n.a.	173	n.a.	(33.7)	0.4	76.1	10.3	11.4	n.a.	n.a.	21.6	27.5
Taiwan-listed peers														
CHLITINA	4137	1,073	946	285	224	-64.5	0.6	76.0	26.6	32.1	23.4	17.5	0.0	-16.4
JOURDENESS GROUP	4190	424	441	83	68	-91.8	1.4	67.7	19.7	29.4	20.9	23.6	-10.5	-6.9
Average		749	693	184	146	-78.1	1.0	71.9	23.1	30.7	22.2	20.5	-5.2	-11.7

Source: Company, CIS (HK)

TP of HKD1.02 (18% upside)

Our TP is derived using 13x FY17F P/E, which is equivalent to its 5-year PER mean, and 23% discount from its closest listed peer, Chiltina. The TP is supported by the DCF methodology.

Figure 18: Historical 5-year P/E band



Source: Company, CIS (HK)

Figure 19: DCF valuation

	Mar-17	Mar-18	Mar-19	Mar-20	Mar-21	Mar-22	Mar-23	Mar-24	Mar-25	Mar-26	Term Val.
EBIT	211	235	242	249	254	259	265	267	270	273	
Multi-stage growth rate	0.0%	11.5%	3.0%	3.0%	2.0%	2.0%	2.0%	1.0%	1.0%	1.0%	
Tax Rate	25.8%	25.8%	25.8%	25.8%	25.8%	25.8%	25.8%	25.8%	25.8%	25.8%	
Net Operating Profit After Tax (NOPAT)	156	174	180	185	189	192	196	198	200	202	
Depreciation	37	41	42	43	44	45	46	46	47	47	
ΔCapEx	-60	-80	-82	-85	-87	-90	-93	-96	-98	-101	
ΔNet working Capital	2	3	3	3	3	3	3	3	3	3	
Free Cash Flow (FCF)	135	138	142	146	148	150	153	152	152	151	152
NPV*	125	118	112	107	100	94	88	81	75	69	902

DCF Valuation

 NPV of discrete forecasts
 NPV of terminal value

 968
 902

Firm Value

 Add: Net Cash/(Debt)
 Less: Minority Interests

1,871
 476
 0

Equity Value (HKD)

 Shares Outstanding
 Value per Share (HKD)

2,346
 2,002
 1.17

Terminal Value

 Terminal Growth Rate
 WACC

 1%
 8%

Terminal Value FCF

152

NPV of Terminal Value (End)

1,971

NPV of Terminal Value (Today)

902

Source: Company, CIS (HK)

Figure 20: Sensitivity analysis on EPS

	FY17F GPM change (ppts)						
	-5	-3	-1	0	1	+3	+5
+20%	12%	15%	18%	20%	22%	25%	28%
+15%	7%	10%	13%	15%	17%	20%	23%
+10%	3%	6%	9%	10%	11%	14%	17%
+5%	-2%	1%	4%	5%	6%	9%	12%
Base	-7%	-4%	-1%	0%	1%	4%	7%
-5%	-11%	-9%	-6%	-5%	-4%	-1%	1%
-10%	-16%	-14%	-11%	-10%	-9%	-6%	-4%
-15%	-21%	-18%	-16%	-15%	-14%	-12%	-9%
-20%	-25%	-23%	-21%	-20%	-19%	-17%	-15%

Source: Company, CIS (HK)

Figure 21: Sensitivity analysis on Target Price

	Target P/E				
	11x	12x	13x	14x	15x
+20%	1.03	1.12	1.22	1.31	1.41
+15%	0.99	1.08	1.17	1.26	1.35
+10%	0.94	1.03	1.12	1.20	1.29
+5%	0.90	0.98	1.07	1.15	1.23
0	0.86	0.94	1.02	1.09	1.17
-5%	0.82	0.89	0.96	1.04	1.11
-10%	0.77	0.84	0.91	0.98	1.05
-15%	0.73	0.80	0.86	0.93	1.00
-20%	0.69	0.75	0.81	0.87	0.94

Source: Company, CIS (HK)

Appendix

Company Overview

Business and History

NB is established with the belief of 'Nature is the source of beauty'. Following this core value, the Group emphasizes 'Research, Education, Service and Marketing' of its products. It is persistent in developing products ranging from facial and body care, food supplement to essential oil by using principally natural ingredients, particularly plant-extracted essence. These products are used for skin treatment and SPA services through its beauty centers, and marketed under the brand name of 'NB'. The Group emphasizes Witness (Before and after comparison), Evidence (Product effectiveness) and Science (scientific skin analysis).

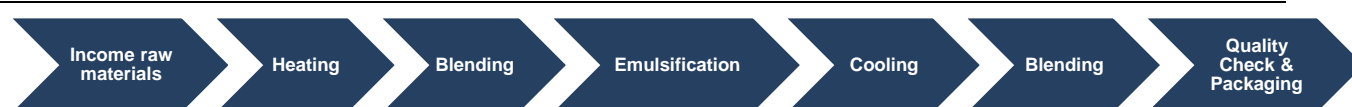
Founded by the Chairperson Dr. TSAI Yen-Yu in Taiwan in 1984 for providing skin treatments, the Group captured the growing awareness of skin treatment in Taiwan, the Group launched a franchise program inviting beauticians to establish franchised beauty centers under the brand name of 'Natural Beauty'. In 1985, the Group built a production plant in Taipei for manufacturing NB beauty and skin care products. The products were mainly distributed to South-East Asian markets including Taiwan, Singapore, Malaysia, as well as non-Asian markets such as Germany.

In 1992, envisaging the growing popularity of beauty and skin care products and services in mainland China, NB formed a JV in Shanghai. The Shanghai division was mainly engaged in R&D as well as production and sale of NB products. In 1993, the Group began to provide training courses to beauticians employed, franchisees and individuals who were interested in setting up their own beauty centers, which became the foundation for the subsequent rapid expansion of its franchisee network on the mainland.

Production process

NB manufactures skin care, beauty, aroma-therapeutic, make-up products and health supplements under the Natural Beauty brand. Production process varies across products. Take the cream and lotion form products as an example. The raw materials which are natural plant extracts are heated for 20-30 minutes. Then the materials are blended and subsequently emulsified for 8-20 minutes. The products are thus cooled for about 1 hour before the final blending. After proper quality check, the cream and lotion form products are packaged as final products.

Figure 22: Production process of cream and lotion form products

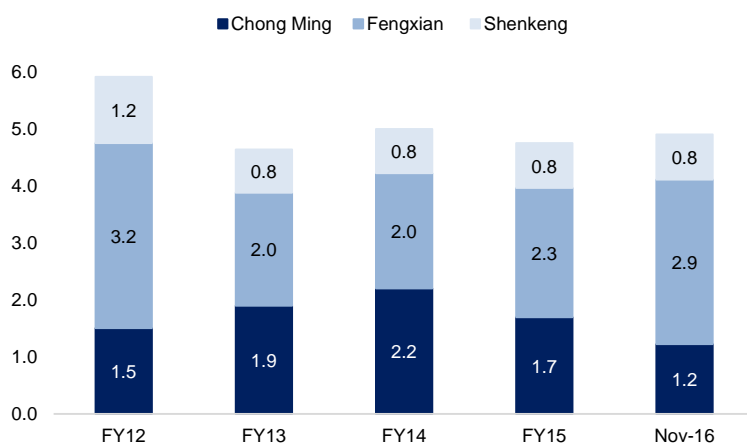


Source: Company, CIS (HK)

Production volume and new plant construction

The products are produced by the 3 plants of NB, one in Taiwan (Shenkeng) and two in Shanghai (Fengxian and Chong Ming). Fengxian is the largest plant with production volume of 2.3m in FY15. Chong Ming the second largest with production volume of 1.7m units last year. Shenkeng, the first and oldest plant, manufactured 0.8m units in FY15. FY15 total production volume of NB was 4.8m units.

Figure 23: Production volume (m units)



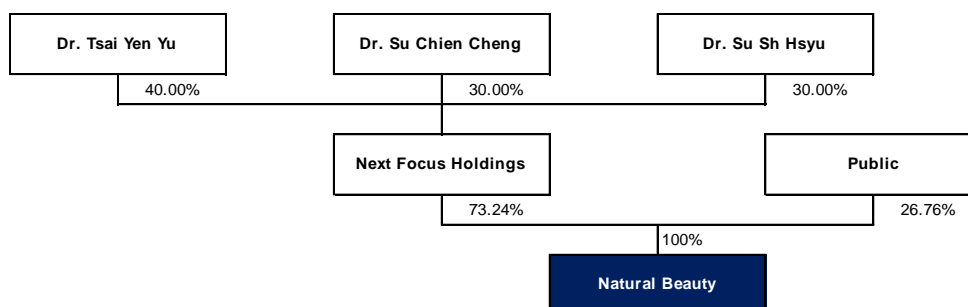
Source: Company, CIS (HK)

In 2015, the Group acquired a land in Fengxian for HKD46.4m, next to its existing Fengxian plant, for setting up a new plant. On the land acquired, together with its Fengxian factory area, NB plans to consolidate its production, research, logistics base and even the headquarters in Fengxian, which is expected to increase operating efficiency and reduce logistics costs. There are 3 phases for construction, where the first phase will commence in 2017. Total investment of the construction is Rmb185m.

Shareholding structure

Next Focus Holdings is now the largest shareholder of NB where it holds 73.24% of the total number of shares. Dr. Tsai Yen Yu, (Founder and Chairperson) and her children Dr. Su Chien Cheng (Executive Director) and Dr. Su Sh Hsyu (Non-executive Director) own Next Focus Holdings by 40%, 30% and 30% respectively.

Figure 24: Shareholding structure



Source: Company, CIS (HK)

In 2009, NB underwent shareholding restructuring and invited The Carlyle Group as a major shareholder, in hope of introducing professional management and promoting international expansion. Dr. Tsi Yen Yu and her children Su Chien-Cheng and Su Sh-Hsyu sold half of their own shares, equivalent to 32.77% of the total share capital of NB to Carlyle at HKD1.25/share for HKD820m. Carlyle were entitled to nominated 4 out of 8 Broad of Directors, actively engaging in management. Subsequently, the Group changed the CEO in Dec 09, and again in Dec 12.

However, due to differences in management philosophy, Carlyle decided to quit NB in 2015, after 6 years of shareholding. Dr. Tsi Yen Yu and her children bought back all the shares from Carlyle at HKD0.8608/share for HKD566m, and became the largest shareholder of the Group again. The Group then nominated Mr. Hsiao Wen-Chung as COO and acting CEO in Dec 15. In Aug 16, he became the CEO of the Group.

Figure 25: Management Profile

Name	Age	Position	Experience
Dr. TSAI Yen-Yu	68	Chairperson & Executive Directors	Dr. TSAI Yen-Yu founded the Group in Taiwan in 1984. Over the past 32 years, the Group expanded from a local beauty salon to one of the largest franchised spa network in China.
Mr. LEE Ming-Ta	68	Vice Chairman & Executive Directors	Mr. LEE is the husband of Dr. TSAI Yen-Yu and the father of Dr. SU Chien-Cheng (Executive Director) and Dr. SU Sh-Hsyu (Non-Executive Director). He has over 10 years of corporate management and staff training experience.
Mr. HSIAO Wen-Chung	59	Chief Executive Officer	Mr. HSIAO has over 33 years of operational management experience in the consumer goods industry. He joined the Group in 2006 and was subsequently appointed as the Chief Operating Officer of the Group until Feb 10. He re-joined the Group in Dec 15 and was re-designated as Chief Executive Officer in Sep 16.
Mr. TSAI Tien-Chun	46	Chief Financial Officer	Mr. TSAI has over 20 years of finance and management experience. Prior to joining the Group, Mr. TSAI worked for Ta-Yung Shin Yeh and Yulon Motor. He was appointed as the CFO in Jul 16.
Dr. SU Chien-Cheng	44	Executive Directors	Dr. SU is the son of Dr. TSAI Yen-Yu and Mr. LEE Ming-Ta. He joined the Group in 1999 and is involved in the financial management and strategic management of the Group at Board level. He was a Non-Executive Director and re-designated as Executive Director effective from Dec 11.
Dr. SU Sh-Hsyu	42	Non-Executive Director	Dr. SU is the daughter of Dr. TSAI Yen-Yu and Mr. LEE Ming-Ta. She joined the Group in 2004 as an Executive Director in 2004, involving in strategic management of the Group. She was subsequently re-designated as a Non-Executive Director effective from Dec 13.
Mr. CHEN Ruey-Long	67	Independent Non-Executive Directors	Mr. CHEN was the Minister of the Ministry of Economic Affairs of Taiwan from 2006 to 2008. Prior to that, he held various positions and represented the Ministry of Economic Affairs of Taiwan in various countries. He was first appointed as Non-Executive Director in Feb 10.
Mr. LU Chi-Chant	64	Independent Non-Executive Directors	Mr. LU has over 27 years of accounting and auditing experience. He is currently an independent non-executive director of Eagle Nice (2368 HK), an independent director of K Laser Technology (2461 TT), Li Peng Enterprise (1447 TT) and Nyquest Technology (6494 TT). He was appointed as the Group's Independent Non-Executive Director in Dec 15.
Mr. HSIEH Pang-Chang	53	Independent Non-Executive Directors	Mr. HSIEH is the associate dean of the College of Management in the Taipei Medical University. He is currently an independent director of Sirtec International (5356 TT), a director of Waterland Financial Holding (2899 TT) and International Bills Finance Corporation (5840 TT).

Source: Company, CIS (HK)

Financial Data and Forecast

Balance Sheet (HKD mn)	FY14	FY15	FY16F	FY17F	FY18F
PPE	224	187	158	160	180
Others	58	92	74	62	54
Total Non-Current Assets	282	279	232	223	234
Inventories	45	47	51	57	61
Account and bills receivables	67	54	60	60	68
Cash and Cash Equivalents	583	503	509	476	427
Others	0.3	6	6	6	6
Total Current Assets	696	610	626	599	562
Trade payables	153	117	150	156	173
Deferred income	8	7	7	7	7
Tax payable	30	20	23	24	22
Total Current Liabilities	191	144	177	161	174
Retirement benefit obligations	13	12	13	13	13
Total Non-Current Liabilities	13	12	13	13	13
Share capital	200	200	200	200	200
Total reserve	574	532	465	429	390
Total equity	774	733	665	629	590
Net Cash	583	503	509	476	427

Cash Flow (HKD mn)	FY14	FY15	FY16F	FY17F	FY18F
Profit before tax	116	170	204	211	235
Depreciation of PPE	39	34	35	37	41
Others	16	14	4	5	5
Changes in working capital	26	(34)	22	2	3
Income tax paid	(32)	(44)	(53)	(54)	(61)
Net operating cash flows	165	140	212	200	223
Purchase of PPE	(19)	(14)	(25)	(60)	(80)
Others	14	(32)	11	13	13
Net investing cash flows	(5)	(46)	(14)	(47)	(67)
Dividend paid	(75)	(142)	(151)	(156)	(174)
Net financing activities cash flows	(75)	(142)	(151)	(156)	(174)
Net (decrease) / increase in cash	86	(48)	47	(4)	(18)
Exchange gains/(losses)	(10)	(32)	(40)	(30)	(30)
Cash at beginning of year	507	583	503	509	476
Cash at end of year	583	503	509	476	427

Income Statement (HKD mn)	FY14	FY15	FY16F	FY17F	FY18F
Total Turnover	506	507	498	529	582
Cost of sales	(117)	(109)	(125)	(137)	(149)
Gross profit	389	397	372	391	434
Other income & expenses	(10)	17	(10)	20	19
Operating expense	(262)	(267)	(262)	(247)	(187)
Profit before tax	116	147	100	164	265
Income tax expense	(45)	(34)	(53)	(54)	(61)
Reported net profit	71	137	151	156	174
Recurring net profit	100	141	145	156	174
Recurring EPS (HKD cents)	5.0	7.0	7.2	7.8	8.7

Ratio Analysis	FY14	FY15	FY16F	FY17F	FY18F
Growth YoY					
Revenue	15.1%	0.2%	-1.8%	6.2%	10.2%
Operating profit	40.0%	46.5%	19.5%	3.4%	11.5%
Recurring net profit	85.1%	41.2%	2.8%	8.2%	11.5%
Recurring EPS	85.1%	41.2%	2.8%	8.2%	11.5%
Margin					
GPM	76.9%	78.4%	74.8%	74.0%	74.5%
OPM	23.0%	29.1%	20.1%	31.0%	45.5%
Recurring NPM	19.7%	27.7%	29.0%	29.6%	29.9%
ROA	10.2%	15.8%	16.9%	19.0%	21.9%
ROE	12.9%	19.2%	21.7%	24.9%	29.5%
Liquidity & Solvency					
Current Ratio	3.6	4.2	3.5	3.7	3.2
Quick Ratio	3.4	3.9	3.2	3.3	2.8
Cash Ratio	3.1	3.5	2.9	3.0	2.5
Net debt to equity	-75%	-69%	-77%	-76%	-72%
Working Capital					
AR days	65	44	42	41	40
Inventories days	144	153	142	144	146
AP days	480	452	388	405	404
DuPont Analysis					
Net Profit Margin	19.7%	27.7%	29.0%	29.6%	29.9%
Asset Turnover	0.5	0.6	0.6	0.6	0.7
Leverage Ratio	1.3	1.2	1.3	1.3	1.3

Source: Company, CIS (HK)

Disclaimer

Investment Recommendation System

Company Rating:

Strong Buy: Expecting a relative return of over 20% against Hang Seng Index in coming 6-12months

Buy: Expecting a relative return of 10-20% against Hang Seng Index in coming 6-12months

Hold: Expecting a relative return of $\pm 10\%$ against Hang Seng Index in coming 6-12months

Avoid: Expecting a relative return of -10% or less against Hang Seng Index in coming 6-12months

Sector Rating

Outperform: Expecting a relative return of over 5% against Hang Seng Index in coming 6-12months

Neutral: Expecting a relative return of over $\pm 5\%$ against Hang Seng Index in coming 6-12months

Underperform: Expecting a relative return of -5% or less against Hang Seng Index in coming 6-12months

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