

**UPDATE REPORT**

21 Apr 2011

<b>Poh Kong Holdings Berhad</b>		<i>Market Price:</i>	RM0.46
		<i>Market Capitalisation:</i>	RM188.8m
		<i>Board:</i>	Main Market
<i>Recommendation:</i>	HOLD	<i>Sector:</i>	Consumer Products
<i>Target Price:</i>	RM0.52	<i>Stock Code/Name:</i>	5080 / POHKONG

Analyst: Edmund Tham



Source: Handal website

**BACKGROUND**

Poh Kong started off humbly in 1976 with just an outlet in Petaling Jaya, Selangor. Growing since then, it has now got around 100 outlets across the country. In March 2004, Poh Kong was listed on the Main Board of Bursa Malaysia. Poh Kong’s core business encompasses the manufacturing and trading of jewellery and gold ornaments. The company manufactures and deals in jewellery, precious stones and gold ornaments. Its trading business involves being the supplier and retailer of gold ornaments, jewellery and other precious stones.

**“Largest Jewellery Chain Store in Malaysia”**

Poh Kong is widely-known as the sector leader in terms of both sales revenue and the number of retail outlets in the country, and is acknowledged by the Malaysia Book Of Records as the “Largest Jewellery Chain Store” in Malaysia.

**Dato’ Eddie Choon** is the Executive Chairman and Group Managing Director of Poh Kong. He had been at the helm of Poh Kong group since its inception as Poh Kong Jewellers. He had won numerous prestigious awards such as “19 Years At The Top” given by Malaysia Tatler in 2008 and “Super Star of the Year 2008” by the Malaysian Retailer-Chains Association (MRCA) for his leadership and business achievements. In 2010, Dato’ Eddie received the “MRCA Achievers Book 2010” Award for being one of the outstanding and leading entrepreneurs in the development of the retail chains industry and in pioneering a successful business model for Poh Kong.

Poh Kong focuses on having modern, contemporary and more “Westernized” designs. The company has its own highly-trained in-house designers and its own factory in Shah Alam. The factory was set up as an ultra modern RM12 million manufacturing facility with an initial 60,000 sq ft and has an expansion capacity of three times its initial size. Poh Kong’s management emphasizes on competing based on design, craftsmanship and premium quality.

**“Local representative for premium brands”**

The group also represents exclusive designer brands from international houses, namely Alessandro Fanfani (a goldsmith shop in Italy), Angel Diamonds from Belgium, Lapplesite Collection (chunky, uniquely designed jewellery), Luca Carati (one of Italy’s most

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prestigious jewellers), Rodney Rayner (luxury jewellery from the United Kingdom), SunDay Collection (handset precious stones), Verdi Gioielli (bangles and bracelets from Italy) and Schoeffel (luxury pearls from Germany).

#### “Range of in-house brands”

Poh Kong currently operates specialty brands and retail concept stores - Tranz, Walt Disney collection, Diamond Boutique, Diamond & Gold, Jade Gallery, Oro Bianco (white gold jewellery), Poh Kong Gallery and Schoeffel, as well as the Schoeffel Time Collection, a range of luxury ladies watches. Tranz is an in-house Poh Kong brand launched in 2001 – aimed at the young and trendy clientele segment. Meanwhile, Poh Kong Gallery is the quintessential brand store among its premium portfolio of concept stores.

#### “Winner of numerous awards”

In 2008, Poh Kong was recognized and conferred the Reader's Digest Trusted Brands Award in the Jewellery Shop category for the 3rd year running. The Reader's Digest Trusted Brands Survey, partnered with Nielsen Media Research, is recognized for being one of the most transparent branding surveys in the Asian region.

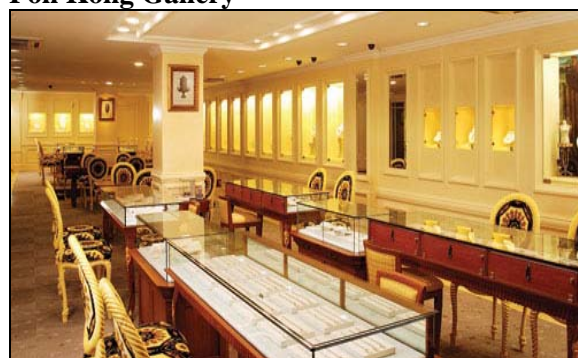
Other awards that Poh Kong has won include The Largest Jewellery Chain Store (1998) award by the Malaysia Book of Records. Poh Kong was listed as one of the companies in the region's 2009 and 2010 Retail Asia-Pacific Top 500 retail companies in their annual ranking based on sales value generated by retailers in 14 Asian economies.

In 2010, several subsidiaries of the Poh Kong group received the Fair Price Shop Awards 2010 in the jewellery category from YB Dato' Sri Ismail Sabri Yaakob, Minister of Domestic Trade, Co-operatives and Consumer Affairs in recognition of the company's outstanding contributions to the country's economy.

#### “Many outlets at shopping malls”

Poh Kong's retail outlets are concentrated mostly in Peninsular Malaysia, with the exception of a franchised outlet in Kota Kinabalu, Sabah. Quite a number of Poh Kong's retail outlets are situated in shopping malls, around anchor tenants such as Tesco, Aeon (Jusco) and The Store. Among the largest of its shops (by floor space) are at its headquarters (Petaling Jaya), Aeon Shopping Mall (5400sf at Bukit Tinggi, Klang) and a new one at Aeon Mall (Malacca). Poh Kong Gallery, a stylish VIP lounge occupying 5,000 sq ft and refurbished with a classic Italian ambience was set up at its headquarters in Jalan 52/4, Petaling Jaya.

#### Poh Kong Gallery



Source: Poh Kong

#### PERFORMANCE – 1H/FY11

2Q/ 31 Jan	2Q11	2Q10	yov %	1Q11	qoq%
Rev (RMm)	170.5	144.2	18.2	169.5	0.6
EBIT (RMm)	15.6	13.7	14.5	17.5	(10.9)
NPAT (RMm)	9.5	7.5	27.1	10.9	(12.5)
EPS (sen)	2.3	1.8	27.1	2.7	(12.5)

\*based on 410.4 million shares

6M/ 31 Jan	1H/FY11	1H/FY10	yov %
Rev (RMm)	339.9	296.6	14.6
EBIT (RMm)	33.2	30.0	10.7
NPAT (RMm)	20.4	17.4	17.6
EPS (sen)	5.0	4.2	17.6

\*based on 410.4 million shares

Poh Kong's revenue for its 2Q/FY11 of RM170.5 million was higher as compared to the corresponding 2Q/FY10 revenue of RM144.2 million. This was a y-o-y increase of RM26.3 million or 18.2%. The increase in revenue was due to the group's existing stores registering higher sales. The shopping period for Christmas

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and Chinese New Year (mostly) occurred during the quarter.

#### “Strong 1H/FY11 performance”

The group's 2Q/FY11 net profit after tax (NPAT) of RM9.5 million was higher as compared to the net profit before tax of RM7.5 million in the corresponding 2Q/FY10. This was an increase of 27.1% y-o-y. The increase in net profit before tax was mainly due to the higher sales registered during the quarter.

Comparing q-o-q versus 1Q/FY11, Poh Kong's revenue of RM170.5 million was 0.6% higher. Nevertheless, the group's 2Q/FY11 NPAT of RM9.5 million lower by 12.5% q-o-q. This decrease was due higher operating costs and tax expenses.

### OUTLOOK/CORP. UPDATES

Poh Kong's management plans to continue its drive to build market share by enhancing and differentiating its product offerings to its targeted market segments. The group actively evaluates various initiatives and opportunities to attract new customers through the introduction of new product lines/designs and enhanced customer service.

#### “Favourable economic factors”

Malaysia had also reported a very respectable 4Q/2010 GDP growth of +4.8% (+7.2% for full year 2010 GDP), stable 4Q/2010 unemployment rate of 3.2% and manageable CPI of 3.0% (March 2011). Meanwhile, Bank Negara Malaysia (BNM) had last reaffirmed its accommodative overnight policy rate (OPR) of 2.75% on 11<sup>th</sup> March 2011.

**BNM** may decide to increase its OPR during the year to contain inflationary pressures. A steady economic growth would also lead to higher consumer optimism and hence assist to raise domestic consumption, including spending on retail gold or jewellery products.

According to **Retail Group Malaysia (RGM)** which tabulates retail data, Malaysia's retail industry recorded sales growth of 8.5% in the fourth quarter of 2010, higher than the earlier estimate of 6% by RGM. The rising prices of retail goods and year-end holidays contributed to the strong growth during the last three months of 2010, according to data in RGM's Malaysia Retail Industry Report. For full-year 2010, the domestic retail industry had increased by 8.4% compared to 2009.

#### “Gold prices reached US\$1500/ounce”

Gold spot prices have held steadily above the US1400/troy ounce level since mid-March 2011. The spot rate for gold traded on the NYMEX (New York Mercantile Exchange) is currently just above the US\$1500/troy ounce level.

According to the World Gold Council, robust market fundamentals, including evidence of stronger demand for gold jewellery in China and India, have continued to support the gold prices performance. Gold plays a role in hedging and has been regarded as a safe, long term investment that provides protection against unforeseen risks in the economic cycle.

Large jewellers like Poh Kong do have revenues coming from sales of gold bars, though its management has not given any guidance on the quantum. Gold bars, which are 999.9% pure gold, are commonly available in 1g, 5g, 10g, 20g, 50g and 100g weight denominations. Gold wafers are sold in the denominations of 25g, 50g and 100g. More often than not, gold jewellery are bought largely for ornamental usage e.g. for wedding dowry, ceremonial/formal functions and as gifts to spouses or close family members.

Besides gold wafers, gold bars and gold-based jewellery, there are also other gold-investment options. Consumers nowadays have the option of investing in gold via commercial banks (via “gold investment accounts”) or even via MLM (multilevel-marketing) companies that may offer gold-based investment products (e.g. gold coins and gold bars). In some countries, gold-related investments could also be done via gold ETFs

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(exchange traded funds), gold certificates and gold-based derivatives.

At the moment, Poh Kong has no plans to expand its outlets to overseas locations. In terms of revenue, about 80% of Poh Kong's revenue is derived from gold, with the remainder 20% from gem stones (e.g. diamonds). From the gold-revenue segment, about 75% is derived from yellow-gold sales while 25% is from white-gold sales. The 'Malay and Indian' market clientele traditionally prefers yellow-gold based ornamental products.

Gold jewellery remains Poh Kong's main revenue contributor although the group has stepped up the sales of diamonds and gems in its advertising and promotion campaigns. The branding strategy of these stores has been adopted so that the company becomes less dependent on its traditional yellow gold jewellery. The group will select stores to refurbish and also find strategic locations for outlets across the country which has the best potential for higher revenue growth and consumer demand.

Poh Kong practices the four core business principles of quality, value, trustworthiness and choice, to target its market segments. This incorporates values such as design, craftsmanship, reputation, and competitive pricing. The group constantly evaluates its operational efficiency/costs, capital expenditure, outlet-expansion plans, gearing, cash flow needs and gold inventory levels.

On the marketing side – the group's intensified efforts in advertising and promotions (A&P) (especially during festivals), merchandising and product launches, sponsorships and road shows during the year would help to maintain the group's market leading position.

## VALUATION / CONCLUSION

Poh Kong had obtained shareholders' approval at its Eighth Annual General Meeting (AGM) in January 2011 to declare a first and final

dividend of 1.4 sen single tier dividend per share for its financial year ended 31<sup>st</sup> July 2010 (FY10). The net dividend amount of RM5.7 million was paid in March 2011 to the entitled shareholders.

### “Consistent dividends”

Poh Kong's future dividends would be largely determined by the performance and cashflow needs of the group. The group's dividend payout ratios have been quite consistent near the 20% level. As such, we expect that Poh Kong would be able to maintain a reasonable dividend payout ratio of around 20% of its annual net earnings for its FY11.

With a close adjusted beta (correlation factor) of 1.06 to the KLCI, Poh Kong (-6.1% YTD) has slightly underperformed the KLCI (+0.7%) this year. Market conditions have also been volatile lately, impacted by the recent political uprisings in the Middle East/North Africa and major earthquake in Japan. As Poh Kong is not a particularly large market-cap stock, this may put a dampener on its market visibility and trading volume.

### “Hold Call”

Based on our forecast of Poh Kong's FY11 EPS and an estimated P/E of 5.5 times (within its historical range), we set a FY11-end **Target Price (TP) of RM0.52**. This TP offers a 13.8% upside from its current market price, and represents a Hold Call. Our TP for Poh Kong reflects a P/BV of 0.63 times over its FY11F BV/share. Meanwhile, the local “Clothes & Accessories” sector's average P/E and P/BV is 8.2 times and 0.9 times, respectively.

### “Undemanding Valuations”

We find that Poh Kong's FY11F P/E and P/BV valuations are undemanding, while it has reasonable net gearing ratio, dividend yield and ROE. We are pleased with Poh Kong's strong performance in its 1H/FY11. If the group can maintain the strong performance in its upcoming

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quarters, we may consider upgrading our Target Price and Call on the group.

### “Concerns & Risk Factors”

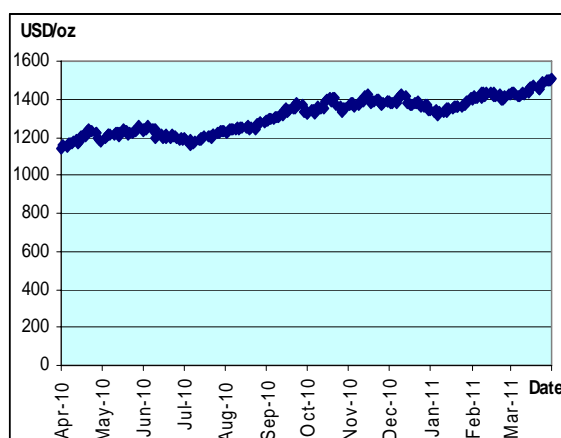
Meanwhile, the group also face business risks such as any future economic downturn, consumer pessimism, uneven monthly sales (due to festive seasons), fluctuating raw material prices and foreign exchange rates and strong competition from its peers. Going forward, the group’s upside would be largely dependent on its management’s marketing and growth strategy, and also on the overall economic conditions.

### Poh Kong: Share Price



Source: NextView

### Gold price chart



Source: Bloomberg

## KEY FINANCIALS

Key Stock Statistics	2011E
<b>Year end: Jul 31</b>	
Earnings/Share (sen)	9.5
P/E Ratio (x)	4.8
Dividend/Share (sen)	1.9
NTA/Share (RM)	0.83
Book Value/Share (RM)	0.83
Issued Capital (mil shares)	410.4
52-weeks share price (RM)	0.35 – 0.515
<b>Major Shareholder:</b>	
.Poh Kong S/B	58.3%

\*RM0.50 par value

Ratios Analysis^	2008	2009	2010	2011E
<b>Year end: Jul 31</b>				
Book Value/Share (RM)	0.64	0.69	0.75	0.83
Earnings/Share (sen)	7.0	7.0	7.7	9.5
Dividend/Share (sen)	1.4	1.4	1.4	1.9
Div. Payout Ratio (%)	20.0	20.1	18.2	20.0
P/E Ratio (x)	6.6	6.6	6.0	4.8
P/Book Value (x)	0.72	0.67	0.61	0.55
Dividend Yield (%)	3.0	3.0	3.0	4.1
ROE (%)	11.0	10.1	10.2	11.5
Net Gearing (or cash) (x)	0.68	0.49	0.43	0.38

\*2011E figures are our estimates

^based on 410.4 million share base

P&L Analysis (RM mil)	2008	2009	2010	2011E
<b>Year end: Jul 31</b>				
Revenue	509.4	541.6	561.2	625.7
Operating Profit	50.1	49.2	54.7	66.1
Depreciation	(7.0)	(7.9)	(8.6)	(9.3)
Interest Expenses	(10.2)	(10.6)	(10.4)	(10.4)
Pre-tax Profit	40.0	38.6	44.3	55.7
Effective Tax Rate (%)	28.0	26.2	28.7	29.9
Net Profit	28.7	28.5	31.6	39.1
Operating Margin (%)	9.8	9.1	9.8	10.6
Pre-tax Margin (%)	7.8	7.1	7.9	8.9
Net Margin (%)	5.6	5.3	5.6	6.2

\*2011E figures are our estimates

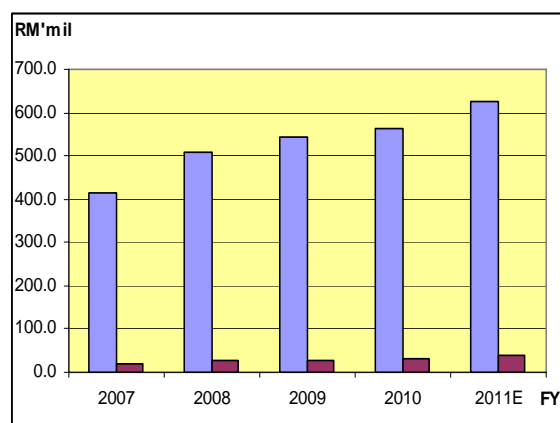
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**Poh Kong: Outlet Locations**

OUTLET TYPE/ LOCATION	NO. OF OUTLETS
<b>#Poh Kong Jewellers</b>	
Selangor	21
Kuala Lumpur	22
Perak	3
Penang	4
Kedah	3
N.Sembilan	5
Malacca	4
Johor	7
Pahang	2
Kelantan	1
Sabah	1
<b>#Tranz</b>	1
<b>#Diamond Boutique</b>	4
<b>#Diamond &amp; Gold</b>	18
<b>#Jade Gallery</b>	1
<b>#Oro Bianco</b>	1
<b>#Poh Kong Gallery</b>	2

Source: Poh Kong website/annual report

**Poh Kong: Revenue & NPAT trend**

Source: Poh Kong

\*FY2011E figures represent our estimates

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