

China / Hong Kong Company Update

GOME Retail Holdings

Bloomberg: 493 HK Equity | Reuters: 0493.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

1 Sep 2022

HOLD

Last Traded Price (31 Aug 2022): HK\$0.246 (HSI : 19,954)
 Price Target 12-mth: HK\$0.24 (2.4% downside) (Prev HK\$0.55)

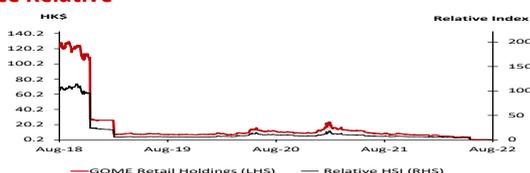
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What's New

- Closure of offline stores hit 1H22 financial performance
- While evident GP margin improvement could prove better efficiency of its newer retail strategies
- Uncertainties linger amid weak macros and intense market competition. Maintain HOLD with a lower TP of HK\$0.24 to stay more prudent

Price Relative



Forecasts and Valuation

FY Dec (RMBm)	2020A	2021A	2022F	2023F
Turnover	44,119	46,484	27,961	32,623
EBITDA	(2,408)	(2,424)	(2,622)	(526)
Pre-tax Profit	(7,169)	(4,728)	(5,131)	(3,053)
Net Profit	(6,994)	(4,402)	(4,877)	(2,780)
Net Pft (Pre Ex) (core profit)	(6,994)	(4,402)	(4,877)	(2,780)
Net Profit Gth (Pre-ex) (%)	(170.0)	37.1	(10.8)	43.0
EPS (RMB)	(0.35)	(0.15)	(0.14)	(0.09)
EPS (HK\$)	(0.40)	(0.17)	(0.16)	(0.11)
Core EPS (RMB)	(0.35)	(0.15)	(0.14)	(0.09)
Core EPS (HK\$)	(0.40)	(0.17)	(0.16)	(0.11)
EPS Gth (%)	(169.8)	57.1	8.6	32.2
Core EPS Gth (%)	(169.8)	57.1	8.6	32.2
Diluted EPS (HK\$)	0.00	0.00	0.00	0.00
DPS (HK\$)	0.00	0.00	0.00	0.00
BV Per Share (HK\$)	0.07	0.68	0.24	0.52
PE (X)	nm	nm	nm	nm
CorePE (X)	nm	nm	nm	nm
P/Cash Flow (X)	2.3	9.8	3.3	1.5
P/Free CF (X)	66.8	nm	5.6	1.9
EV/EBITDA (X)	nm	nm	nm	nm
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	3.4	0.4	1.0	0.5
Net Debt/Equity (X)	20.2	1.5	2.2	2.0
ROAE(%)	(84.7)	(33.2)	(25.3)	(15.7)
Earnings Rev (%)			(147)	(235)
Consensus EPS (RMB)			(0.04)	(0.01)
Other Broker Recs:		B:0	S:0	H:3

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Takes time to bear fruit

Investment Thesis

Strategic third-party cooperation. GOME's proactive move in terms of channel collaboration with competent partners, including JD.com and PinDuoDuo, should improve its overall supply chain and sales growth prospects over the medium-term to achieve a win-win situation.

Consumer experience upgrade. The company is putting in more efforts to enhance its product offerings and service quality, with an aim to develop itself as a one-stop retailer that focuses on overall home solutions and offers better consumer experience, hence gradually improving customer stickiness and loyalty ahead.

New retail strategies. More emphasis on the deployment of GOME's newer omnichannel strategies should support business expansion, while the uncertainty over COVID-19 should overshadow the overall picture in near-term. Coupled with intense market competition and weak macro environment, we believe its newer business approach could still need more time to bear fruit.

Valuation:

In view of its lower-than-expected bottom-line performance for 1H22, we widened our projected losses by 147%/235% for FY22/FY23. Our new target price is HK\$0.24, pegged to 0.6x FY22F P/BV (or 2 S.D. below average P/BV), amid a more volatile operating environment due to COVID-19 impacts and business adjustments (previous TP: HK\$0.55 based on 1x P/BV).

Where we differ:

We stay conservative on the company's near-term performance given lingering COVID-19 impacts, intense market competition, and uncertainties related to the implementation of its newer business plans. However, an enhanced 1H22 GP margin should prove the effectiveness of its newer retail strategies, and see room to lift our estimates once solid income starts to flow in.

Key Risks to Our View:

Upside risks: Earlier-than-expected earnings turnaround.
Downside risks: Slow execution of new retail strategies; COVID-19 affecting consumer sentiment; new home demand remains slow.

At A Glance

Issued Capital (m shrs)	33,757
Mkt Cap (HKm/US\$m)	8,304 / 1,058
Major Shareholders (%)	
Wong (Kwong Yu)	51.8
Free Float (%)	48.2
3m Avg. Daily Val. (US\$m)	21.24
GICS Industry: Consumer Discretionary / Retailing	



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GOME Retail Holdings**WHAT'S NEW****1H22 interim results briefing takeaways**

1H22 results below expectations. Affected by COVID-19 resurgence in the domestic market, most cities in China have implemented risk control measures, and offline business operations have been significantly affected. GOME saw c.54% y-o-y decline in the top line to RMB12.1bn. Gross profit was down by 33% to RMB2bn, while GP margin recorded a 5.1ppt increase to 17.2%, indicating effectiveness of its new retail strategy to some extent. Net loss expanded by 58% to RMB3.2bn, which included a one-time impairment provision of RMB0.96bn mainly coming from the closure of underperformed stores. Net margin was -27% (1H21: -7.9%).

More focus to be placed on core businesses. Since 2Q22, GOME has significantly scaled down its inefficient and loss-making businesses and plans to focus on its retail products and services. Without affecting its coverage, the company closed approximately 370 loss-making stores in 1H22. Such reductions will continue in 2H22 and are expected to result in RMB0.2bn in rent savings. Going forward, the overall loss is expected to reduce by RMB1bn-RMB1.5bn after the business adjustment.

Shopping experience enhancement. Given that consumers are no longer satisfied with a single consumption scenario, the company plans to establish about 100 city showrooms in core locations of each city to showcase its products and services, hence enabling brand promotion of each merchant and providing a scenario-based shopping experience for its consumers. Assisted by high-tech features such as voice guides, smart robots, and interactive game devices, the company should be able to keep consumers longer in its stores and increase the frequency of its interactions with customers. Currently, GOME has a total of 3,825 offline stores across 1,379 cities in China, including 370 self-operated stores to provide more quality services. The company targets to increase the number of self-operated stores to around 700-800, while the rest will be operated through franchising.

Business adjustment and cooperation. GOME has adjusted its revenue and profit model by signing exhibition and sales contracts with various vendors, enabling the

company to obtain display fee income in addition to the revenue from product sales. Such initiative also helped to lift GP margin significantly in 1H22. Meanwhile, GOME has also entered into strategic cooperation agreements with Tencent, Huawei, and Alibaba Cloud to accelerate the digital transformation of its offline stores, reduce traffic costs, and build accurate marketing capabilities. Anxun, the logistics service platform of GOME, covers 99% of fourth-tier areas and over 80% of rural areas. Under the influence of COVID and weak macroeconomics, Anxun was able to achieve c.20% growth in revenue to RMB1.5bn and a net profit of over RMB50m. It is expected that Anxun will maintain similar growth momentum ahead.

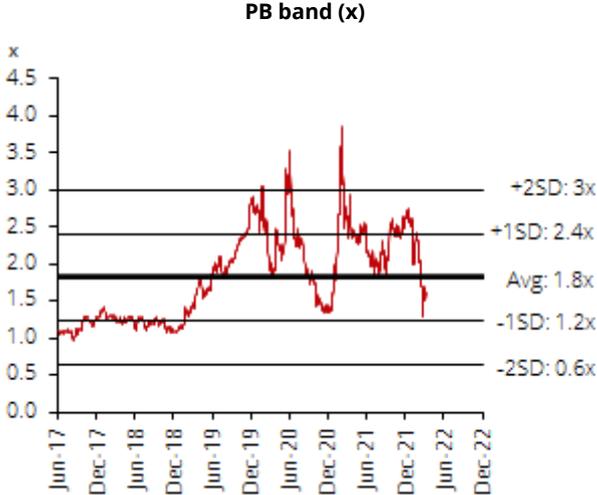
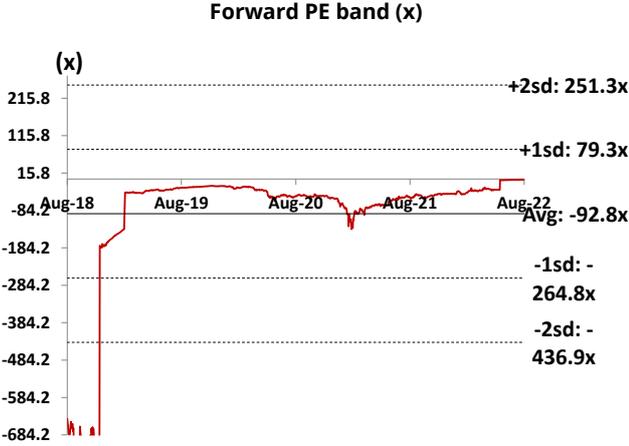
Overall outlook. We have seen a weak macro environment in China, with GDP growth of merely 0.4% in 2Q22. However, as the COVID-19 situation gradually stabilises, total retail sales of consumer goods in China rebounded by 3.1% y-o-y in Jun (May 2022: -6.7%), and the pressure on the retail industry is expected to ease further in 2H22. Stimulated by a series of consumption vouchers and subsidies, overall consumer sentiment could gradually improve in the coming months. Coupled with over 10% m-o-m recovery in GOME's sales by Aug, 2H22 sales momentum is expected to outperform 1H22's. On the other hand, as the uncertainty over COVID-19 continues to overshadow the near-term outlook, while GOME's new business strategies might still need more time to become fruitful on the back of weak macros and intense market competition, we maintain HOLD on the counter and await better financial performance ahead.

Company Background

GOME is one of the leading retailers in appliances and electronics in China. The company was renamed from "GOME Electrical Appliances Holding" to "GOME Retail Holdings" in 2017 to reflect its repositioning as a general retailer.

GOME Retail Holdings

Historical PE and PB band



Source: Thomson Reuters, DBS HK

GOME Retail Holdings

Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
Store number	2,735.0	3,421.0	3,956.0	4,496.0	5,036.0
Offline sales (RMB)	57,427.0	40,619.1	42,983.8	24,285.9	26,927.2
Online Revenue (RMB m)	2,055.8	3,500.0	3,500.0	3,675.0	5,696.3
Net gearing (%)	223.6	2,018.1	146.1	218.4	204.4
Gross profit margin (%)	15.3	10.3	11.8	19.3	20.0

Source: Company, DBS HK

Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenues (RMB m)					
Online Revenue (RMB)	2,056	3,500	3,500	3,675	5,696
Offline Revenue (RMB)	57,427	40,619	42,984	24,286	26,927
Total	59,483	44,119	46,484	27,961	32,623
Gross Profit (RMB m)					
Online Revenue (RMB)	31	35	35	184	342
Offline Revenue (RMB)	9,080	4,515	5,472	5,221	6,193
Total	9,111	4,550	5,507	5,405	6,535
Gross Profit Margins (%)					
Online Revenue (RMB)	1.5	1.0	1.0	5.0	6.0
Offline Revenue (RMB)	15.8	11.1	12.7	21.5	23.0
Total	15.3	10.3	11.8	19.3	20.0

Source: Company, DBS HK

GOME Retail Holdings

Income Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	59,483	44,119	46,484	27,961	32,623
Cost of Goods Sold	(50,372)	(39,569)	(40,977)	(22,556)	(26,088)
Gross Profit	9,111	4,550	5,507	5,405	6,535
Other Opng (Exp)/Inc	(10,239)	(10,248)	(8,892)	(8,946)	(7,949)
Operating Profit	(1,129)	(5,697)	(3,385)	(3,541)	(1,414)
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(105)	(6)	(17)	(6)	(6)
Net Interest (Exp)/Inc	(1,662)	(1,465)	(1,327)	(1,583)	(1,633)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	(2,896)	(7,169)	(4,728)	(5,131)	(3,053)
Tax	(72)	(35)	(44)	(46)	(27)
Minority Interest	379	210	371	300	300
Preference Dividend	0	0	0	0	0
Net Profit	(2,590)	(6,994)	(4,402)	(4,877)	(2,780)
Net Profit before Except.	(2,590)	(6,994)	(4,402)	(4,877)	(2,780)
EBITDA	2,728	(2,408)	(2,424)	(2,622)	(526)
Growth					
Revenue Gth (%)	(7.6)	(25.8)	5.4	(39.8)	16.7
EBITDA Gth (%)	N/A	N/A	(0.7)	(8.1)	79.9
Opg Profit Gth (%)	(75.9)	404.7	(40.6)	4.6	(60.1)
Net Profit Gth (%)	47.0	(170.0)	37.1	(10.8)	43.0
Margins & Ratio					
Gross Margins (%)	15.3	10.3	11.8	19.3	20.0
Opg Profit Margin (%)	(1.9)	(12.9)	(7.3)	(12.7)	(4.3)
Net Profit Margin (%)	(4.4)	(15.9)	(9.5)	(17.4)	(8.5)
ROAE (%)	(20.2)	(84.7)	(33.2)	(25.3)	(15.7)
ROA (%)	(3.9)	(9.8)	(5.8)	(6.5)	(3.9)
ROCE (%)	(2.9)	(13.0)	(7.0)	(6.9)	(2.8)
Div Payout Ratio (%)	N/A	N/A	N/A	N/A	N/A
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS HK

GOME Retail Holdings

Balance Sheet (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	6,733	6,296	6,715	6,303	5,932
Invt in Associates & JVs	180	176	634	176	634
Other LT Assets	31,615	27,063	42,773	43,445	42,450
Cash & ST Invt	8,776	10,015	5,320	3,293	2,867
Inventory	7,688	8,368	6,352	2,579	4,646
Debtors	3,448	3,662	4,666	2,284	3,960
Other Current Assets	13,431	14,914	14,463	11,340	11,730
Total Assets	71,872	70,494	80,923	69,419	72,218
ST Debt	18,445	25,858	24,554	24,126	24,126
Creditors	23,685	25,408	24,844	17,314	18,908
Other Current Liab	4,282	1,677	2,751	2,250	2,458
LT Debt	8,581	9,739	6,451	6,885	6,885
Other LT Liabilities	8,717	6,544	4,737	6,151	6,071
Shareholder's Equity	11,600	4,916	21,604	17,012	18,389
Minority Interests	(3,439)	(3,649)	(4,020)	(4,320)	(4,620)
Total Cap. & Liab.	71,872	70,494	80,923	69,419	72,218
Non-Cash Wkg. Capital	(3,400)	(141)	(2,115)	(3,362)	(1,031)
Net Cash/(Debt)	(18,250)	(25,583)	(25,685)	(27,718)	(28,144)
Debtors Turn (avg days)	28.8	29.4	32.7	45.4	34.9
Creditors Turn (avg days)	175.0	226.4	223.8	341.1	253.4
Inventory Turn (avg days)	57.6	74.1	65.6	72.3	50.5
Asset Turnover (x)	0.9	0.6	0.6	0.4	0.5
Current Ratio (x)	0.7	0.7	0.6	0.4	0.5
Quick Ratio (x)	0.3	0.3	0.2	0.1	0.2
Net Debt/Equity (X)	2.2	20.2	1.5	2.2	2.0
Net Debt/Equity ex MI (X)	1.6	5.2	1.2	1.6	1.5
Capex to Debt (%)	5.0	5.0	13.5	3.2	3.0
Z-Score (X)	0.9	1.0	1.1	1.3	1.3

Source: Company, DBS HK

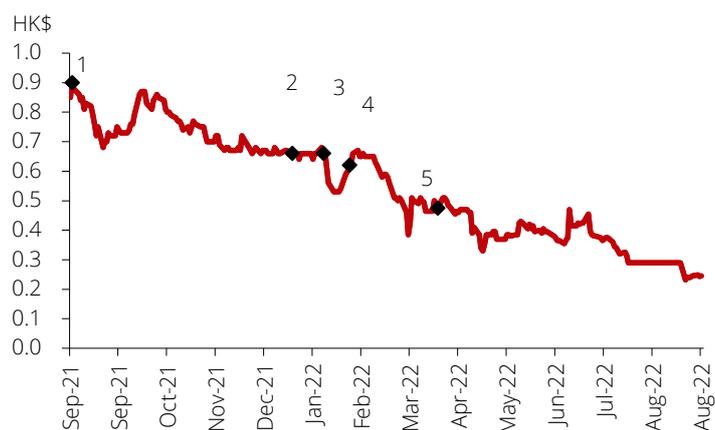
Cash Flow Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	(2,896)	(7,169)	(4,728)	(5,131)	(3,053)
Dep. & Amort.	3,962	3,296	2,326	4,976	4,944
Tax Paid	(125)	20	(44)	(46)	(27)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	386	2,179	(46)	294	277
Chg in Wkg.Cap.	(406)	2,215	580	580	743
Other Operating CF	1,480	1,311	2,562	1,697	1,504
Net Operating CF	2,401	1,851	649	2,370	4,388
Capital Exp.(net)	(1,341)	(1,786)	(4,180)	(998)	(940)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	(199)	(1)	(329)	(165)	(247)
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	439	810	3,040	1,312	1,092
Net Investing CF	(1,100)	(978)	(1,469)	149	(95)
Div Paid	0	0	0	0	0
Chg in Gross Debt	5,946	8,301	285	285	285
Capital Issues	0	(16)	0	0	0
Other Financing CF	(9,217)	(7,692)	(4,663)	(4,251)	(5,174)
Net Financing CF	(3,271)	593	(4,378)	(3,966)	(4,889)
Currency Adjustments	14	(55)	(21)	(38)	(29)
Chg in Cash	(1,957)	1,411	(5,219)	(1,485)	(626)
Opg CFPS (RMB)	0.14	(0.02)	0.00	0.05	0.12
Free CFPS (RMB)	0.05	0.00	(0.12)	0.04	0.11

Source: Company, DBS HK

GOME Retail Holdings

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	2-Sep-21	HK\$0.90	HK\$0.71	Fully Valued
2:	7-Jan-22	HK\$0.66	HK\$0.75	Hold
3:	25-Jan-22	HK\$0.68	HK\$0.75	Hold
4:	9-Feb-22	HK\$0.59	HK\$0.75	Hold
5:	1-Apr-22	HK\$0.49	HK\$0.55	Hold

Source: DBS HK

Analyst: Mavis Hui
Kay Tan

GOME Retail Holdings

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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GOME Retail Holdings

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