COMPANY UPDATE Consumer discretionary ▪ Singapore

Best World International

(BEST SP/BEST.SI)

Strong growth in China but risks remain

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- BEST's 4Q18 increased 29% YoY to S$28.1mn, driven mainly by its franchise business in China.
- It reported S$78.8mn sales from its franchise business, which contributed 62% of total revenues in 4Q18. This would imply a 121% YoY increase in its China sales from 4Q17, when it was still classified under the export business segment.
- Declared 4.2 cents final and 0.8 cents special dividend, compared to 2.6 cents final in FY17. When including the interim dividends, full-year FY18 payout translates to S$40.7m.
- Valuations are at a discount to international peers but may be warranted given the key overhangs. Our sensitivity analysis based on 3Q/4Q FY18 earnings when its franchise business started contribution implies a P/E range of 12x to 18x.

Figure 1: PATMI trend (Quarterly)

	1Q 2018	2Q 2018	3Q 2018	4Q 2018
PATMI (S$'000)	5,771	9,128	29,887	28,106

Source: Company data, KGI Research

Analyst briefing summary. BEST's 4Q18 earnings came in above street estimates. Performance in the quarter was driven by its franchise business in China, which contributed 62% of total revenues. China growth remains strong and management is confident of achieving growth in top and bottom line in FY19. BEST's 4Q18 China revenues surged 121% YoY to S$80mn. Balance sheet is healthy, with S$195mn net cash as at end Dec 2018.

BEST reported S$78.8mn in revenues from the new franchise segment, which only started contribution in 3Q18. It was previously classified under Export in 4Q17.

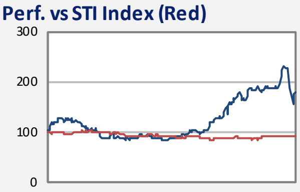
Figure 2: Revenue by business segments in 4Q18

S$'000	4Q 2018	4Q 2017	% Change
Direct Selling	47,519	35,021	35.7%
Export	84	35,100	(99.8%)
Manufacturing/Wholesale	1,231	1,360	(9.5%)
Franchise	78,817	–	NM
Total Revenue	**127,651**	**71,481**	**78.6%**

Source: Company data, KGI Research

Concerns. Concerns were raised during the briefing regarding the transparency of its franchise business in China. BEST is just starting out this new business model, which is currently only used in China. As such, it is still refining the model and is taking steps to ensure the quality of its franchisees. Management has ordered an independent review of its China business but has not given any indication

Not Rated			
Price as of 27 Feb 19 (SGD	2.56	**Performance (Absolute)**	
12M TP ($)	-	1 Month (%)	-4.5
Previous TP ($)	-	3 Month (%)	13.5
Upside (%)	-	12 Month (%)	83.6
Trading data		**Perf. vs STI Index (Red)**	
Mkt Cap ($mn)	1,406		
Issued Shares (mn)	549		
Vol - 3M Daily avg (mn)	3.9		
Val - 3M Daily avg ($mn)	9.9		
Free Float (%)	48.9%		
Major Shareholders		**Previous Recommendations**	
D2 Investment	34.1%		
Mui Hoan Beng	5.9%		
Moi Tan Nee	5.7%		



of who it will engage to conduct the review or when it will start.

Valuation & Action:

4Q strongest quarter. BEST's 4Q is typically its strongest quarter and 1Q19 numbers are expected to drop QoQ given the CNY holidays, but will be higher YoY given that 1Q18 did not have contribution from the franchise business.

Cheap but perhaps warranted. A sensitivity analysis based on S$20m, S$25m and S$30mn in quarterly earnings would imply 18x, 14x and 12x P/E. These multiples are cheaper compared to international peers. However, we think the discount may be justified for now until its franchise model proves to be sustainable.

Figure 3: Valuation sensitivity analysis

Quarterly Earnings (S$'000)	20,000	25,000	30,000
Implied P/E at current price	17.6x	14.1x	11.7x

Source: KGI Research

Assessing risks. Although we note that management will have to provide more disclosures of its franchise business, a bigger risk, in our view, is from government regulations in China. BEST does not have control over its franchisees in China and as such, may possibly experience increased scrutiny from authorities over customer complaints, exaggerated advertisements, or questionable practices of its franchisees.

Risks: Shift in government regulations in China would severely restrict BEST's growth potential and cause a downward re-rating in valuations.

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