

InNature Bhd

INITIATION COVERAGE

BUY

Closing Price	RM 0.55
Target Price	RM 0.70
Consensus Price	RM 0.62

Stock Return Information

KLCI	1,394.63
Expected share price return (%)	27.3
Expected dividend return (%)	3.6
Expected total return (%)	30.9

Key Statistics

Shariah Compliant	YES
Bloomberg Ticker	INNATURE MK
Msia Ticker/Stock Code	INNATURE/5295
Shares Issued (m)	705.9
Market Capitalisation (RM m)	388.2
52 Week Hi/Lo Price (RM)	0.89/0.46
Avg Trading Volume (3-mth)	865,709
Est Free Float (%)	15.7
YTD Returns (%)	-18.5
Beta (x)	0.86

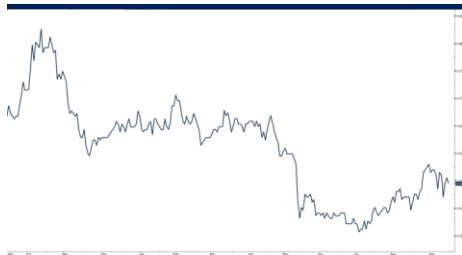
Share Price Performance (%)

Price Change	Absolute	Relative
1 mth	5.77	13.53
3 mth	11.11	14.54
12 mth	-21.43	-12.12

Major Shareholders (%)

Etheco Sdn Bhd	51.0
Blueplanet Sdn Bhd	17.9

1-Year Share Price Performance



Analyst : Lai Yoon Hui, David
Email : davidlai@interpac.com.my

Strong Comeback From The Pandemic Effects

We initiate coverage on InNature Bhd with a BUY recommendation and a target price of RM0.70, by ascribing a target PER of 20.5x (in line with its historical average forward 12-months PER) to its CY23F EPS. We anticipate InNature to deliver a CAGR of 27.6% in earnings between CY21-23F. After reporting slightly lower-than-estimated 2QCY22 earnings, its share price dropped steeply by c.18% from its peak in May 2022, trading at only 15.9x forward PER which represents an attractive 22% discount to the company's historical average forward PER. Key downside risks: 1) slower-than-expected recovery of sales per store, 2) longer gestation period for new stores, 3) delays of expansion plans

InNature is a leading regional mono-brand retailer of cosmetics and personal care (CPC) products carrying The Body Shop (TBS) and Natura brands in Malaysia, Vietnam and Cambodia with omnichannel sales strategy such as own TBS websites, Love Your Body (LYB) mobile apps and 3rd-party e-commerce platforms.

TBS to Benefit from Southeast Asia's Resilient Cosmetics and Personal Care Industry

Euromonitor has projected that beauty and personal care industry in Southeast Asia will grow at a 5.0% CAGR for the next 5 years. This is due to Southeast Asia's increasing urbanisation rate, rising awareness of beauty and growing e-commerce sales. InNature, as a leading regional mono-brand retailer, is poised to benefit from the growth of the industry.

A Good Proxy for Economic Recovery

According to Retail Group Malaysia, Malaysia's retail industry recorded a 62.5% Y-o-Y growth in 2Q2022, while the personal care sub-sector resumed its growth at 79.8% Y-o-Y and projected an average growth rate of 25.7% Y-o-Y in the retail industry during 2Q2022. Therefore, we estimate a 9.3% Y-o-Y growth in its TBS retail stores sales in CY23F on the back of: 1) reopening of borders, 2) opening of new outlets, and 3) boosting brand value with refurbishment of existing outlets.

Robust Earnings Recovery, Improved Profitability and Decent Dividend Yield

We project CY22F/23F topline to grow 18.7%/8.6% Y-o-Y and 49.5%/9.0% Y-o-Y growth in its bottomline, backed by increased retail stores performance and improved profitability following a c. 7 % hike in price on all existing products, albeit lower sales from the remote channel. We anticipate a dividend payout of at least 2.0 sen in CY22F/23F, potentially rewarding shareholders with a decent 3.6% dividend yield.

Figure 1: Historical and Forecast Financial Performance

FYE (RM m)	CY19	CY20	CY21	CY22(F)	CY23(F)
Revenue	191.7	155.4	131.9	156.6	170.1
EBITDA	65.9	50.6	41.4	46.7	51.7
EBITDA margin (%)	34.4	32.6	31.3	29.8	30.4
PAT	30.2	20.0	14.9	22.3	24.2
PATAMI	30.2	20.0	14.9	22.3	24.2
PAT margin (%)	15.7	12.9	11.3	14.2	14.3
EPS (sen)	4.3	2.8	2.1	3.2	3.4
Earnings growth (%)	(33.9)	(33.8)	(25.5)	49.5	9.0
PER (x)	12.9	19.4	26.1	17.4	16.0
DPS (sen)	nm	2.0	2.0	2.0	2.0
Dividend yield (%)	nm	3.6	3.6	3.6	3.6
ROE (%)	37.1	17.7	10.5	15.0	15.4
Net gearing ratio	0.3	Net Cash	Net Cash	Net Cash	Net Cash
P/B (x)	4.4	2.8	2.7	2.5	2.4

Source: Bloomberg, Inter-Pacific Research

Note: nm = not meaningful

BUSINESS OVERVIEW

Background

InNature is principally involved in retailing and distribution of personal care products, namely TBS in Malaysia (except Sarawak), Vietnam and Cambodia using omnichannel sales strategy through retail store, own website and 3rd-party e-commerce platforms. TBS expanded its exposure into Vietnam and Cambodia in 2009 and 2019 respectively.

All TBS franchise agreements were renewed and granted for a period of 10 years commencing from June 19, 2019 with an option to renew the franchise for a further 5 years.

History and Business Model of The Body Shop International (TBSI)

TBSI is a global manufacturer and retailer of TBS personal care products, founded in UK in 1976 which is owned by Brazil-based Natura & Co – 4th largest cosmetics group in the world and listed on the New York Stock Exchange. With around 3,000 stores globally spanning across Europe, North and South America, TBSI offers a diverse range of products for different usage such as skincare, body care, haircare, fragrance, makeup and others.

It is also B Corp certified which demonstrates its ability to meet the highest verified standards of social and environmental performance, transparency and accountability. Products offered by TBSI are completely vegan or vegetarian that are not tested on animal and its natural ingredients are sourced from regenerative farming that supports the regeneration of ecosystems.

Figure 2: TBS' Activist Makers Workshop in Sunway Pyramid



Source: Company

Figure 3: TBS' High Street Outlet in Hanoi, Vietnam

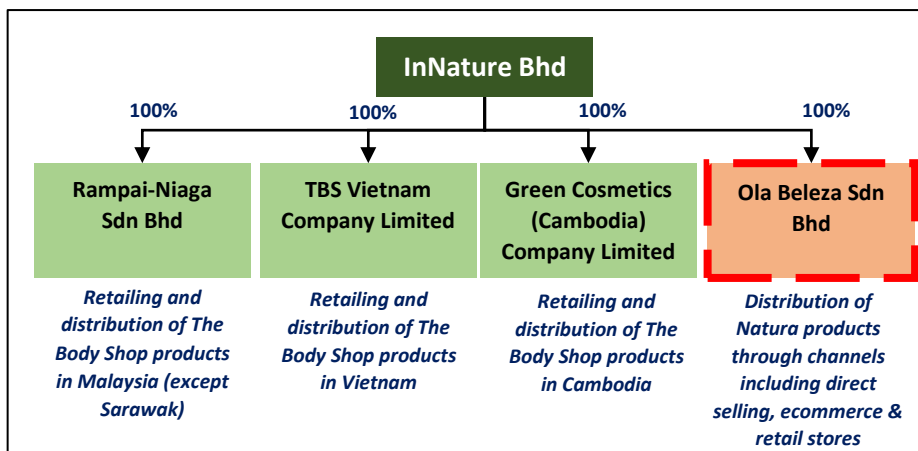


Source: Company

Corporate Structure of InNature

InNature incorporated subsidiaries such as Rampai-Niaga, TBS Vietnam, Green Cosmetics for supervision of TBS operations in Malaysia, Vietnam and Cambodia respectively.

Figure 4: Key Subsidiaries of InNature



Source: Company

Note: Ola Beleza Sdn Bhd will no longer be the subsidiary of InNature after the disposal exercise.

Vast TBS Retail Store Networks in Malaysia

InNature has set up 75 TBS stores in Malaysia, 39 stores in Vietnam and 2 stores in Cambodia as of June 2022. As per figure 5, InNature has established strong presence in West Malaysia with more stores set up in high population density areas such as Selangor (18), Kuala Lumpur (14) and Johor (9). In contrast to West Malaysia, there are only 7 stores and 1 store set up in Sabah and Labuan respectively (excluding stores in Sarawak as they are not owned by InNature). Most of the TBS stores in Malaysia are located in high-traffic shopping malls such as Sunway Pyramid, Pavillion KL, Mid Valley Southkey JB.

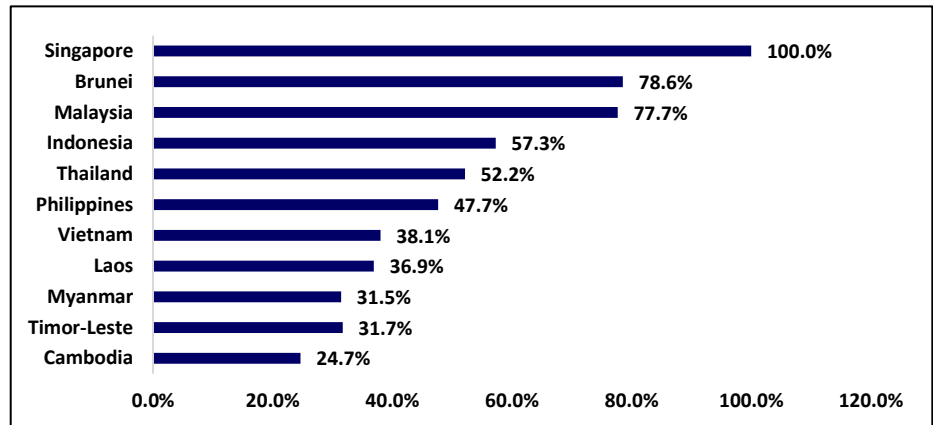
Figure 5: 75 TBS Stores in Malaysia



Source: Company

InNature has forayed into Vietnam and Cambodia, which both have combined 114m population, as compared to only 32m population in Malaysia. Despite the urbanisation rate in Vietnam and Cambodia that is at the mid-or-lower end among other Southeast Asia countries, both are highly potential markets for InNature due to tremendous growth of foreign direct investments and increasing internet penetration driving e-commerce and social media marketing growth in both countries are expected to accelerate their urbanisation rate and growth in affluence.

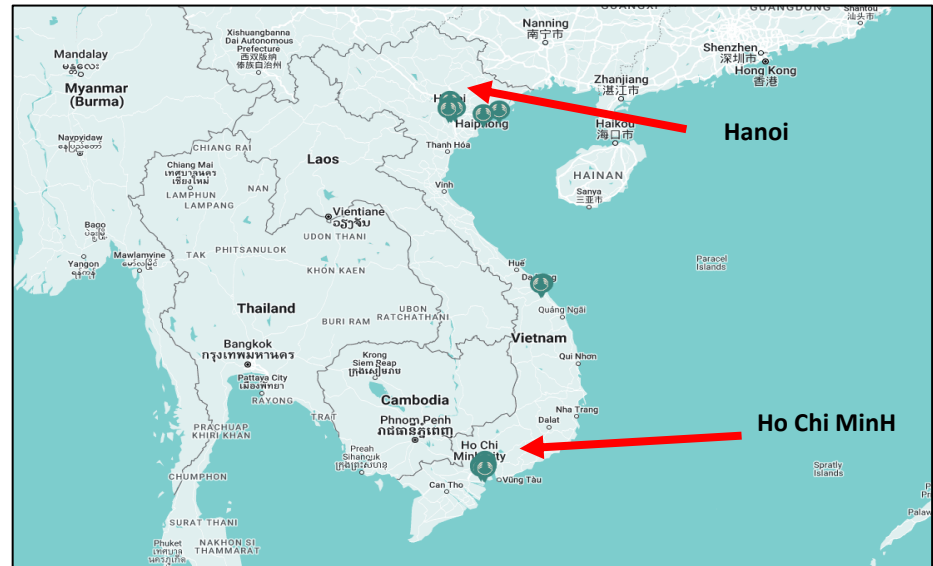
Figure 6: Urbanisation Rate of Each Countries in Southeast Asia in 2021



Source: TheGlobalEconomy.com, Statista, Inter-Pacific Research

InNature established its presence in Vietnam via 39 retail stores where most stores are in special class municipalities like Ho Chi Minh and Hanoi (total of 34 stores). Some retail stores can be seen in 1st class municipalities like Da Nang and Hai Phong or other cities like BinH Duong and Ha Long. These areas are well known for their robust transportation network, high populations, emerging hotspot for foreign investments and attractive tourist spots. However, unlike retail stores in Malaysia, only two-third of the stores are located in shopping malls and remaining are high street stores located in prominent streets, airport or department stores due to lack of modern retail space within shopping malls.

Figure 7: 39 TBS Stores in Vietnam



Source: Company

TBS is relatively new in Cambodia as there are only two TBS stores available in shopping malls in Phnom Penh.

Figure 8: Number of InNature's TBS Stores in Each Location as of June 2022

Malaysia	No of Stores	Vietnam	No of Stores	Cambodia	No of Stores
Selangor	18	Ho Chi Minh	20	Phnom Penh	2
Kuala Lumpur	14	Hanoi	14		
Johor	9	Da Nang	2		
Sabah	7	Binh Duong	1		
Perak	5	Hai Phong	1		
Pulau Pinang	4	Ha Long	1		
Negeri Sembilan	3				
Terengganu	3				
Kedah	3				
Melaka	3				
Kelantan	2				
Pahang	2				
Putrajaya	1				
Labuan	1				

Source: Company

Note: TBS stores established in Sarawak are excluded from the list as they are not owned by InNature.

Figure 9: Population of Each Municipalities/Cities in Vietnam as of June 2022

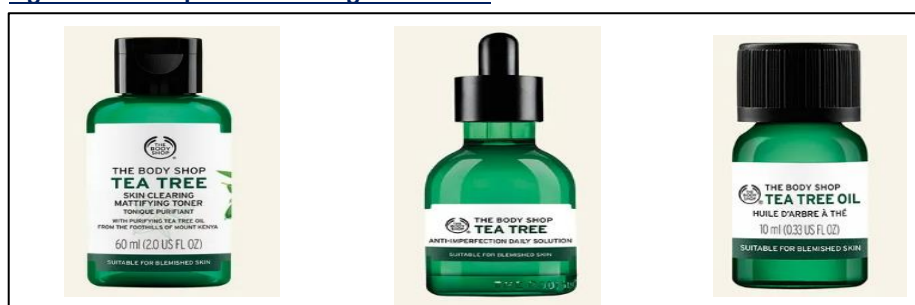
City	Population	Ranking of Total Population in Vietnam
Ho Chi Minh	3,467,331	1
Hanoi	1,431,270	2
Da Nang	752,493	3
Haiphong	602,695	4
Ha Long	148,066	20

Source: Worldometers, Inter-Pacific Research

Natural and Diverse Range of TBS Products

TBS products are completely vegetarian and vegan where the ingredients are sourced from plants or minerals like shea butter from Ghana and tea tree oil from Kenya. Vegetarian products are free of any animal-derived ingredients obtained as a result of intended death to animals but not limited to ingredients such as honey, beeswax and lanolin, while vegan products are completely devoid of animal ingredients. However, TBSI is gradually phasing out the vegetarian products by removing those ingredients from existing products and introducing new vegan products.

Figure 10: Examples of TBS' Vegan Products



Source: Company

TBS products are comprehensive and diverse, offered to both women and men such as:

- ◆ Face/Skincare: Cleansers, Toners, Serum, Moisturisers, Face Masks
- ◆ Body care: Hand Wash, Hand Care, Foot Care, Hair Care, Body Lotions, Deodorant
- ◆ Fragrance
- ◆ Makeup products: Foundations, Eye Liners, Lipstick
- ◆ Gift bundle

Figure 11: Newly Introduced Range of Fragrances - CHOICE



Source: Company

Figure 12: One of Its Signature Range – Shea Butter



Source: Company

INDUSTRY OVERVIEW AND KEY GROWTH DRIVERS

Global Cosmetics and Personal Care (CPC) Industry Landscape

According to Business Wire, global beauty and personal care market is forecasted to grow at a 4.8% CAGR from 2022 to reach approximately US\$558.1b in 2026, at a faster pace of growth rate than 4.6% CAGR from 2009 to 2019 (*source: McKinsey & Co.*) The upcoming growth is premised on:

- ◆ Rapid urbanisation
- ◆ Growing disposable income
- ◆ Rising consumer awareness towards sustainable brands and products
- ◆ Rising social media influence among millennials and gen Z
- ◆ Rising employment of e-commerce platforms
- ◆ Increasing men's CPC market

CPC Industry in Vietnam Is Anticipated to Grow at A Faster Pace than Malaysia

According to Frost & Sullivan, the CPC industry in Malaysia grew at a CAGR of 6.2% from 2013 to US\$9.03b in 2018, whereas it is forecasted to grow at a faster CAGR of 8.0% between 2018 and 2023.

The CPC market in Vietnam grew at a CAGR of 12% from 2013 to about US\$1.69b (VND39.19 trillion) in 2018, while Frost & Sullivan also forecasts the CAGR between 2018 and 2023 will be 8.8%. To be emphasised, the CPC market in Vietnam is still significantly underserved, considering that it is much smaller in market size compared to Malaysia despite the fact that its population is approximately three times that of Malaysia (98.5m vs 32.7m in 2021).

Furthermore, the female population still represents the largest consumer category for the CPC market. As compared to other nations in Southeast Asia, Vietnam's higher female-to-male ratio (female: 50.07% in 2021) (*source: PopulationPyramid*) bodes well for the country's local CPC market. In addition, Vietnam's female labour participation rate outstrips the advanced economies and maintains a rate above 70% for almost two decades — an accomplishment unprecedented even among advanced economies, in accordance with the IMF. Women's increased expenditure on CPC items in Vietnam is also boosted by the country's high women employment rate.

Rising Consumer Awareness Towards Sustainable Brands and Products

According to a survey conducted by the Boston Consulting Group, the Covid-19 pandemic has elevated consciousness of people towards sustainability, reflected by the fact that 70% of survey participants claimed that they are more aware of environmental issues than they were prior to the pandemic and 87% of the respondents stated that companies should integrate environmental concerns into their products, indicating a significant shift of consumer behaviour when they are purchasing the products.

To accommodate the change of consumer behaviour, more beauty and personal care companies are embedding sustainability into entire business ecosystems, from various aspects such as: 1) sourcing environmental-friendly ingredients for their products, 2) utilise biodegradable or recyclable materials for their packaging, 3) ethical ingredients' supplies sourcing.

In recent years, beauty and personal care products with natural and sustainable ingredients have garnered widespread popularity, particularly on vegetarian and

vegan products as modern consumers are increasingly cognisant of the materials used in products. For example, according to Grand View Research, the global market for vegan cosmetics market is expected to track US\$26.2b by 2030 with a CAGR of 6.3% from 2022 to 2030, compared to only US\$15.2b in 2021. Other brand leaders such as Sephora, Estee Lauder, Shiseido and Clinique also announced their commitment towards sustainability of the ingredients, packaging of their products and 100% free from animal cruelty.

Figure 13: Rare Beauty's (100% Vegan) Shelves in Sephora



Source: Sephora

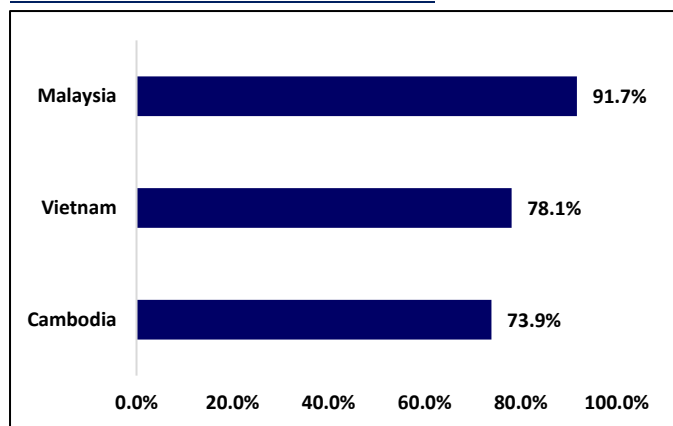
Apart from the sustainability of the ingredients and packaging of the products, consumers place utmost importance on the supply chain or suppliers of the brands, as illustrated by researchers at the MIT Sloan School of Management that consumers may be willing to pay 2% to 10% more for products from companies that provide greater supply chain transparency (*source: Business Harvard Review*). Enhancing supply chain transparency has several advantages for brands, including fostering customer confidence and brand loyalty by making them more aware of the origin of ingredients, the quality of products and the ability of enterprises to monitor and enhance the supply chain.

TBS is proactively sourcing ethical and high-quality ingredients and accessories from producers, farmers and artisans across the world. For example, TBS sources shea butter — a core ingredient in TBS products from Ghana, a country facing unemployment crisis at fair prices, providing additional income to women there. In terms of packaging materials, TBS sources paper and gift packaging from Get Paper Industry in Nepal as the artisans use waste and recycled materials to create the paper and buy recycled plastic from waste pickers in India to use for their plastic packaging.

Increasing Social Media Influence, Especially Among Millennials and Gen Z

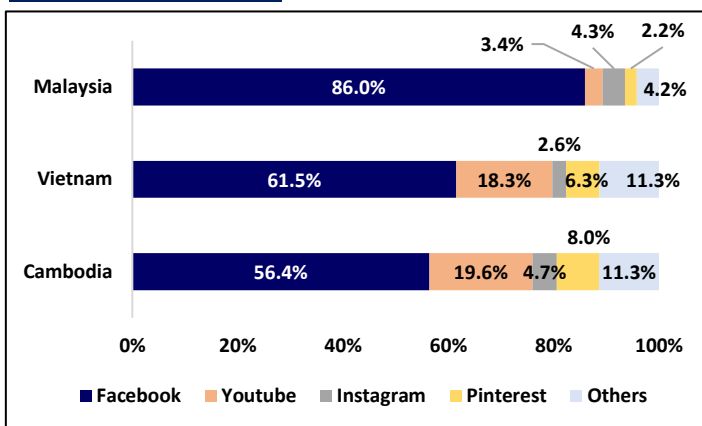
During the Covid-19 pandemic, the rise of social media has played a major role in the transformation of consumer behaviour and become a powerful tool for the beauty and personal care companies to promote their products and to engage with customers, particularly the millennials and gen Z who became more beauty conscious. The use of social media by the beauty and personal care companies in Southeast Asia region is further boosted by the high social media penetration rate in the region, especially Malaysia. As it is, the combined population of millennials and generation Z (deemed as individuals aged between 10 and 41 years) — the digital natives in the region, constituted for around 52.5% of overall population (*source: Department of Statistics Malaysia*).

Figure 14: Penetration Rate of Social Media in Malaysia, Vietnam and Cambodia as of Feb 2022



Source: Statista, Inter-Pacific Research

Figure 15: Share of Social Media in Malaysia, Vietnam and Cambodia as of Jan 2022



Source: Statista, Inter-Pacific Research

In tandem with the increasing number of influencers on social media such as Instagram, YouTube or TikTok, beauty and personal care companies are partnering with influencers to promote their products as digital shoppers are greatly influenced by the explanation and the appearance of the influencers after using the products. Apart from partnering with influencers, the companies launch their own page in various social media or websites to improve customer engagement by notifying them of festive sales, promoting new product launches, gathering feedback from consumers and even establishing an instant customer consultation function.

In digital marketing space in Malaysia and Vietnam, TBS is one of the leaders with the highest number of followers for its Malaysian official Facebook and Instagram page, as well as high number of followers on its Vietnam's official Facebook and Instagram page compared to other brands which own official social media page in both countries. TBS' fan base in Vietnam has grown at a remarkable rate with a 25% increase to 873k followers on Facebook as of September 2022, from 698k as of Dec 2019 (*source: Company's IPO Prospectus*).

Figure 16: Number of Followers of Each Brand Which Owns Official Page in Malaysia and Vietnam as of September 2022

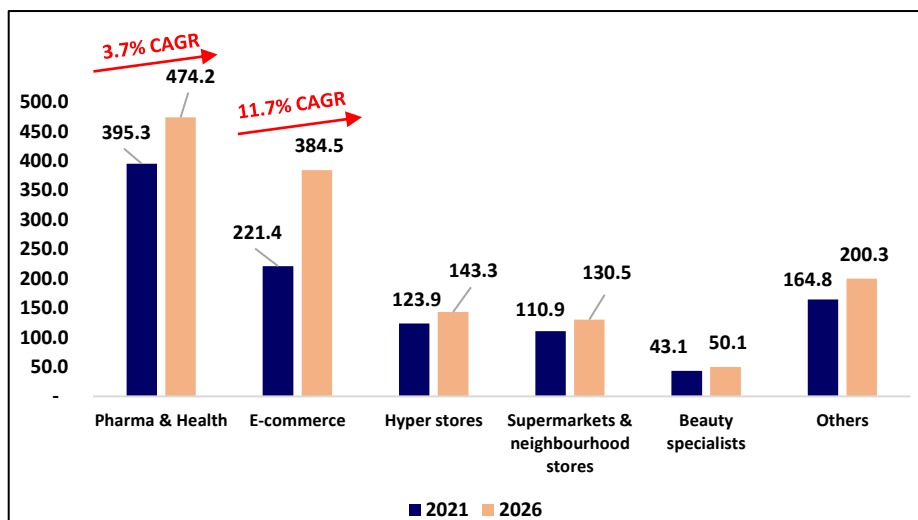
Brand	Followers of Malaysia Facebook Page	Followers on Malaysia Instagram Page	Followers of Vietnam Facebook Page	Followers on Vietnam Instagram Page
The Body Shop	500k	261k	873k	95k
SK-II	385k	na	na	na
Innisfree	341k	157k	946k	71k
The Face Shop	228k	102k	591k	na
Estee Lauder	225k	na	245k	7k

Source: Facebook, Instagram, Inter-Pacific Research

Rising Employment of E-commerce Platforms in the CPC Industry

In the light of extensive internet service and growing number of mobile phones, consumers' purchasing habit across the globe has shifted drastically from purchasing products in physical stores only to purchasing items via omnichannel such as e-commerce platforms. According to Statista, e-commerce is the second largest sales channel for global health, beauty and personal care, ranking behind pharmaceutical stores in 2021 and sales via the channel is expected to grow at 11.7% annually over the next 5 years, compared to the 5-year CAGR of 3.7% for pharmaceutical stores.

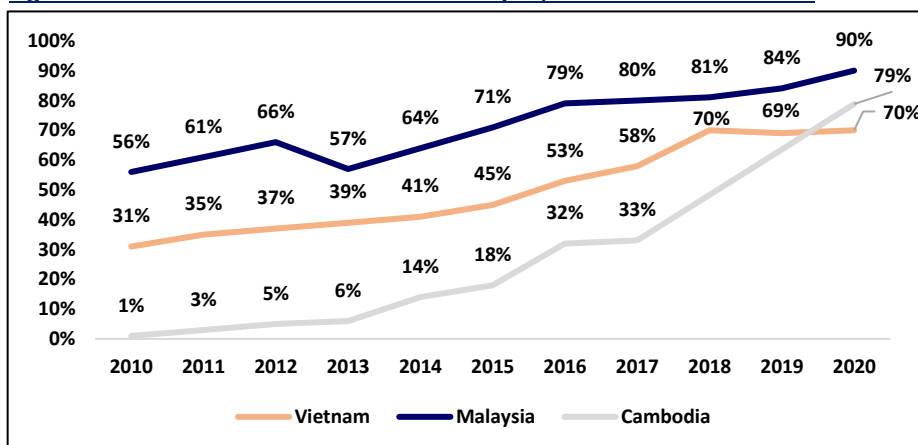
Figure 17: Global Health, Beauty and Personal Care Sales Value Via Each Channels



Source: Statista, Inter-Pacific Research

The Southeast Asian market is quickly adopting into ecommerce trends as e-commerce sales of beauty and personal care is anticipated to accelerate tremendously over the next few years as well. A survey conducted by Facebook and Bain & Co has projected online retail sales of personal care and beauty in Southeast Asia to grow at 25% annually from 2020 to 2025.

Figure 18: Internet Penetration Rate in Malaysia, Vietnam and Cambodia



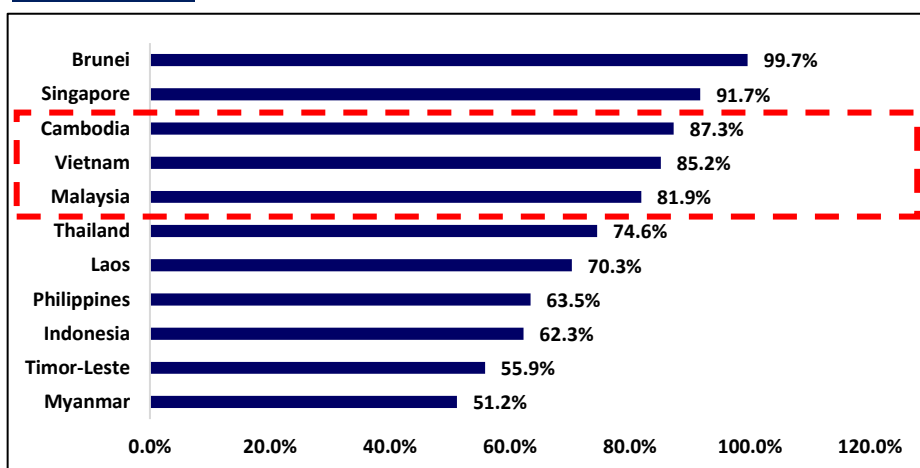
Source: World Bank Data, Inter-Pacific Research

PROSPECTS

Resurgence of Local Consumer Demand to Boost TBS Retail Store Sales

In CY20 and CY21, InNature's retail store sales in 3 geographical locations encountered speed bumps due to lockdown measures imposed by the governments of Malaysia, Vietnam and Cambodia. Nevertheless, the footfalls at shopping malls in these countries are expected to rebound strongly on the grounds that: 1) most Covid's restrictions have been abolished, 2) high vaccination rate among the population of SEA countries, 3) increased spending by local consumers after 2 years of movement restrictions. Given the aforementioned factors, a strong recovery in InNature's retail store sales is projected in Malaysia and Cambodia, where most of the outlets are in shopping malls. We also expect InNature to capitalise on the revival of local demand in Vietnam as they are planning to open more outlets in prominent shopping malls, despite roughly one-third of its outlets in Vietnam are currently high-street stores.

Figure 19: Percentage of Fully Vaccinated Population Across SEA Countries as of September 2022

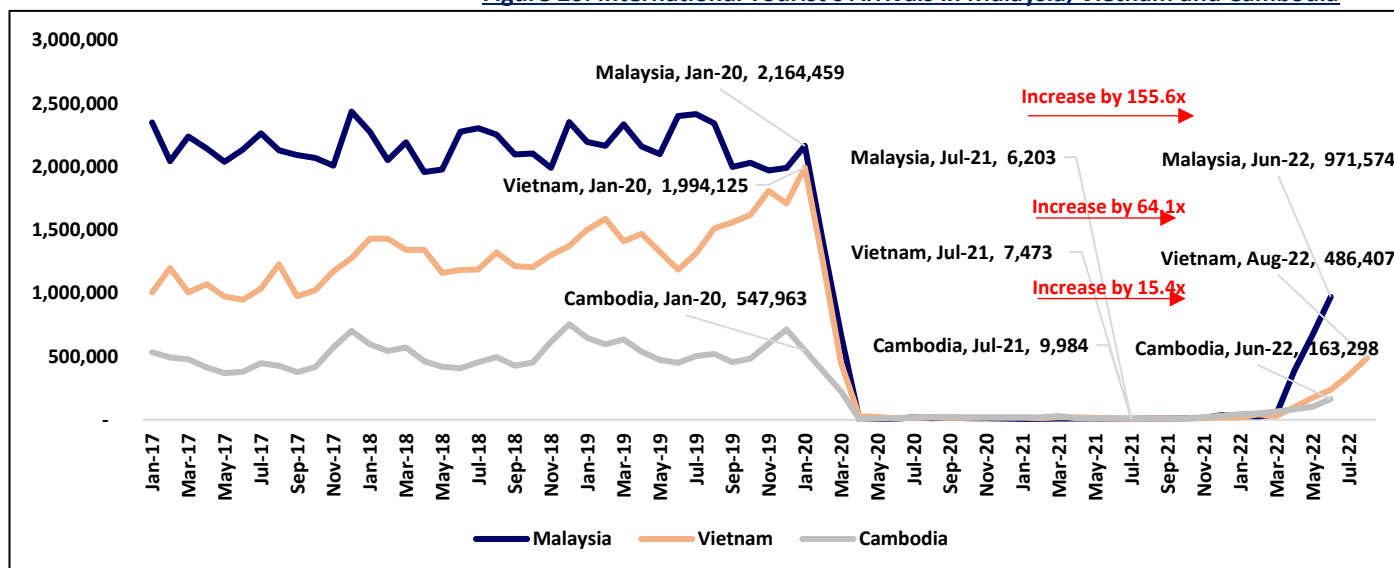


Source: Our World In Data

Strong Rebound for Foreign Tourist Arrivals to Strengthen Recovery of Retail Store Sales

Management had indicated that around 15% of pre-pandemic sales were contributed by the foreign tourist, indicating the importance of foreign tourists towards the recovery of InNature's retail store sales. In Figure 20, we observed that the number of tourists arrivals in these 3 countries recovered strongly from its low in 2021 when the majority of these countries were under lockdown following the spike in Covid-19 cases. Nevertheless, there is still ample room for the recovery of the retail sector, given that the number of tourists remains exceptionally low compared to 2019. Malaysia, Vietnam and Cambodia are expected to welcome 4.5m/5.0m/1.3m international tourists respectively by the end of 2022 and the number of foreign tourists will reach 17%/32%/21% of their respective pre-pandemic level. To capture the demand from foreigners in Malaysia, InNature is also proactively negotiating with authorities to regain their presence in airports, and we believe that increased demand from international tourists will boost TBS retail store sales even further.

Figure 20: International Tourist's Arrivals in Malaysia, Vietnam and Cambodia



Polishing ESG Standards to Capture Interest of Millennials and Gen Z Who Are Much More Favourable Towards Sustainable Business

InNature's franchisor, TBSI is vigorously pursuing ESG standards by using completely vegan or vegetarian ingredients in its products and banning animal testing. InNature is actively launching new range of vegan products to replace previous products of similar functions and aim to have fully vegan TBS products in their stores within two years. Already they introduced the "Edelweiss" range in May 2022 to replace the existing "Drops of Youth" range of products which serve the same purposes to promote fresher and healthier-looking skin. It is also noteworthy that TBS prohibits the experiments of the products on animals which makes the products cruelty-free. This will attract the younger generation to purchase TBS products along with the increasing demand of natural, dangerous ingredients-free, cruelty-free and vegan beauty products, mainly because they perceived that natural product are much more efficient and sustainable.

To reduce plastic bottles used, InNature will also set up refill stations at all existing TBS outlets following the launch of its first refill trolley at its KLCC outlet in 2021 and the introduction of refill stations will encourage customers to replenish their products as the purchasers of the 300ml refill aluminium bottle enjoy cheaper rates than to refill larger volumes of shower gel and shampoo. As of June 2022, InNature had already introduced refills stations in 34 stores and 2 stores in Malaysia and Vietnam respectively and plans to introduce more refillable products.

Figure 21: Refill Rates of TBS' Products

Item	1st Time Purchase & Refill (Member/Non-member)	Refill Only
Shower gel	RM59/RM63	RM34
Shampoo	RM65/RM75	RM46

Source: Company

Figure 22: TBS' Refill Station



Source: Company

In 2022, InNature relocated its store in Sunway Pyramid and created its 1st sustainability store — the Activist Makers Workshop, before opening a second sustainability store in Mid Valley Southkey. The majority of the store's fixtures and fittings are manufactured from recyclable plastic, wood, or other recyclable materials. We also understand from management that they intend to open new stores that adhere to the new sustainability concept and provide customers an eco-friendlier shopping environment. We believe that more younger customers will be attracted to shop in TBS' new concept stores as 51% of gen Z and millennials value the in-store experience when buying beauty and personal care products, according to Statista.

Figure 23: Fixture and Fittings Made Up of Wood



Source: Company

Figure 24: Fixture and Fittings Made Up of Recycled Materials



Source: Company

Disposing Unprofitable Business — Natura to Focus Expanding TBS Network

In June 2022, InNature announced for the disposal of its 100%-owned subsidiary, Ola Beleza Sdn Bhd, which carries out the business of distribution and commercialisation of Natura products in Malaysia to Natura AP for an aggregate consideration of RM2.0m, after taking into account the net assets of Ola Beleza as of Aug 31, 2021. Natura has incurred gestation losses of RM3.1m/RM1.4m in CY20/21, dragging the group earnings.

The disposal is favourable for InNature going forward as: 1) Natura only contributes negligible revenue, 2) Natura's gestation loss is anticipated to continue for a few more years along with the need to fund its expansion plan, 3) InNature can focus on expanding TBS business, and 4) the sale proceeds can be used as working capital for TBS' new opening or renovation of outlets

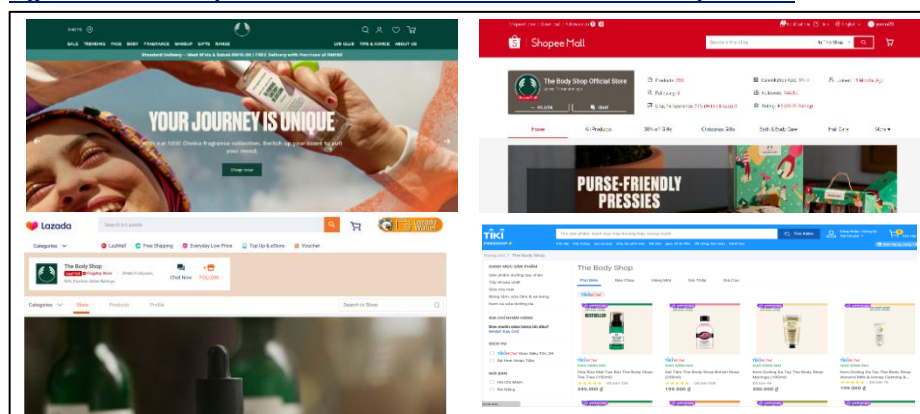
Based on our estimates, InNature's net profit in CY20/C21 would have been around 9.0%-16% higher after omitting Natura's gestation losses.

Leveraging Omnichannel Retail Strategy to Retain and Gain More TBS Customers

InNature is proactively promoting and improving the shopping experience of its various channels for customers to purchase TBS products since 2012 as its loyalty data research for the period between Nov 2018 and Oct 2019 showed that multichannel customers spent 91.6% more than single channel customers.

InNature launched TBS online website in Malaysia (2012), Vietnam (2013) and Cambodia (2019). Apart from employing TBS websites to market the products, InNature is also retailing the products through 3rd-party online stores such as Hermo, Shopee, Lazada in Malaysia and Tiki in Vietnam. Utilisation of e-commerce platforms have provided more accessibility channels to TBS customers, especially those who stay in suburban areas to purchase their products at the same price in retail stores.

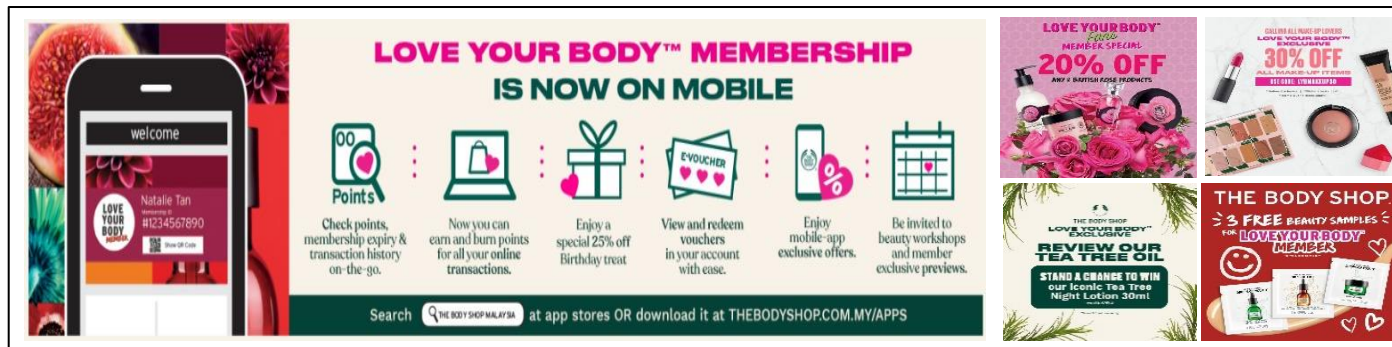
Figure 25: Various platforms and websites for TBS and Natura products



Source: TBS website, Shopee, Lazada, Tiki

InNature has introduced a mobile app for TBS, namely The Body Shop Malaysia which enables customers to purchase the products through mobile apps and keep updated with their memberships' benefits and status. All customers are eligible to register for Love You Body's membership if they spend RM100 in a single receipt with the purchase of products in TBS' retail stores. New members will receive welcome offers such as 20% off for purchase of 2 products of any range. There are also various benefits offered by the LYB club such as 25% off birthday treat, RM15 rebate voucher for every 150 points collected, free gift-wrapping service, festive promotions and more. With abundant benefits offered by the LYB club, we believe that the mobile loyalty app will further build customers' brand affinity towards TBS products as we can see that active LYB customers made up around 75% of group sales in CY21.

Figure 26: Various Benefits of LYB's Members



Source: Company

To efficiently keep existing and potential customers informed of new promotions or new products offered by TBS, InNature also established its presence in various social media platforms like Facebook, Instagram, Twitter and Tiktok and we believe that the live-streaming or the short videos taken by TBS will further strengthen interaction between customers and the TBS brand.

Steady Expansion Plans and Refurbishment of TBS Stores Across Different Geographical Locations

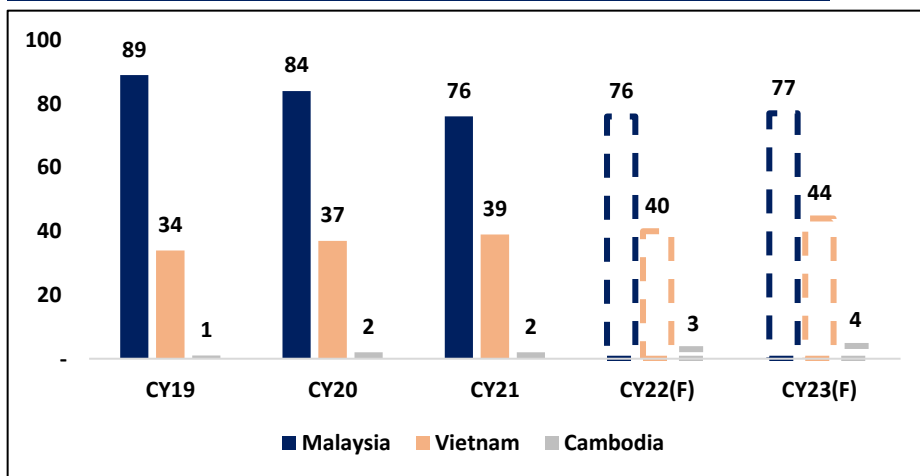
Given that InNature has a strong presence in West Malaysia via its vast network of TBS retail stores, InNature's focus will be improving the same store sales growth in Malaysia's existing TBS stores via sustainable marketing efforts and the replacement of small underperforming outlets with the opening of larger concept stores which tend to have better yields, according to management. To illustrate, it is believed that the transformation of the Sunway Pyramid outlet to an Activist Maker Shop increased the outlet's monthly sales by 38% above the pre-pandemic level and the newly opened concept store in Johor Bahru has become one of the top 10 stores in terms of sales contribution.

In Vietnam, InNature is planning to open more new outlets in 2nd-tier cities, unlike Hanoi and Ho Chi Minh as 2nd-tier cities are still underserved and potentially yield better results due to the suburban population accessibility. In addition, management intends to gradually open more outlets in shopping malls rather than on the high street as they have observed that outlets in shopping malls are better positioned to capitalise on shopping traffic.

For the rest of the year, InNature plans to have at least 1 new TBS store in Malaysia, Vietnam and Cambodia respectively. Moving forward, management guided that InNature will open at least 2 and 6 stores annually in Malaysia and Vietnam and 4 new stores in Cambodia within 3 years while progressively refurbishing existing outlets with concept stores elements.

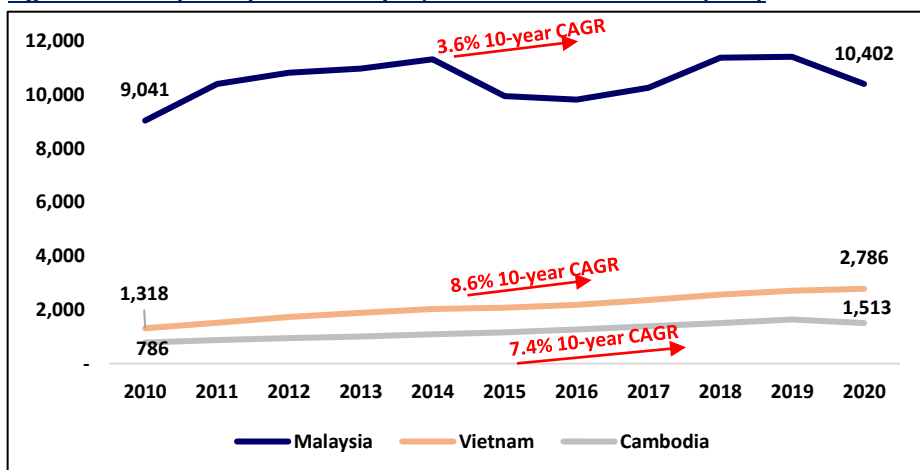
In CY23F, we anticipate that there will be at least a net addition of 1/4/1 new TBS stores in Malaysia, Vietnam and Cambodia respectively while the more aggressive opening of outlets in Vietnam is in line with its firmer 10-year per capita GDP CAGR of 8.6% compared to Malaysia (3.6%) and Cambodia (7.4%), and this is expected to be beneficial for the growth of TBS' operations there.

Figure 27: Estimated Number of TBS Stores in Each Geographical Locations



Source: Company, Inter-Pacific Research

Figure 28: GDP per Capita in Malaysia, Vietnam and Cambodia (USD)



Source: World Bank, Inter-Pacific Research

KEY RISKS

Reliance on the Franchisor

InNature does not own the TBS brand. Therefore, it relies on the product innovation of its franchisor to retain and gain new customers. As a franchisee, InNature must also maintain its performance via various marketing strategies, or it might fail to renew its franchise agreement and there are also no assurances that InNature can renew the agreement once it expires. As retailing of TBS products is the sole business of InNature, the operations of the company will be adversely impacted if the franchise is not renewed.

In accordance with the franchise agreement, InNature sources all products from TBSI and any disruptions in product supply would adversely impact InNature's operations.

Dependant on the Experienced Management Team

Datin Mina, as the Non-Independent Executive Director and Managing Director of InNature, has more than 30 years of expertise in the retail and cosmetics and toiletries industry and Molly Fong Hui Sain — Non-Independent Executive Director and Chief Executive Officer of InNature, are the key personnel of the company. In recent years, InNature has grown steadily under their direction and that of its senior management team. Any material changes on the board of directors or senior management team in the future is expected to have long-term impact on the company's direction and operations.

Squeeze on Both Ends, Higher Material Cost and Lower Purchasing Power Parity

Cost push inflation driven by supply chain disruption and higher inflation across the globe will adversely affect InNature's financial performance. If InNature is unable to fully pass down the rising material and distribution cost to consumers, its profitability will be affected. Meanwhile, the worldwide inflation has dampened consumer purchasing power which is likely to adversely affect InNature's sales target. In addition, to combat the high inflation, central bank across the globe have lifted interest rates aggressively that could ultimately slow down the economy at a faster pace and potentially affect consumer decisions on the purchase of discretionary goods.

As a result, the company is closely monitoring its cost structure and inventory levels to ensure that supplies from the franchisor arrives in a timely manner so that there are sufficient stocks available for customers, while also preventing overstocking which might result in cost overruns.

Foreign Exchange Rate Risks

InNature is exposed to fluctuations of the GBP as TBS products are sourced from United Kingdom. In addition, InNature will also face foreign exchange translation risk for its operations in Vietnam and Cambodia as its reporting currency in its consolidated financial statements are in Ringgit Malaysia.

Fragmented Cosmetics and Personal Care Industry

In Malaysia and Vietnam, there are at least 10 CPC players and none of them have market shares more than 20% as of 2018, according to Frost and Sullivan. Therefore, consumer substitution costs are generally low, and if InNature fails to maintain its brand prestige through innovation and effective marketing, the company risks losing customers or market share. Nevertheless, InNature is a prominent retailer of single-brand beauty products, and it plans to maintain its market-leading position via various innovative marketing strategies.

FINANCIAL HIGHLIGHTS

Revenue Grew at 3-Year CAGR of 6.2% in 2019 until Hit by Covid

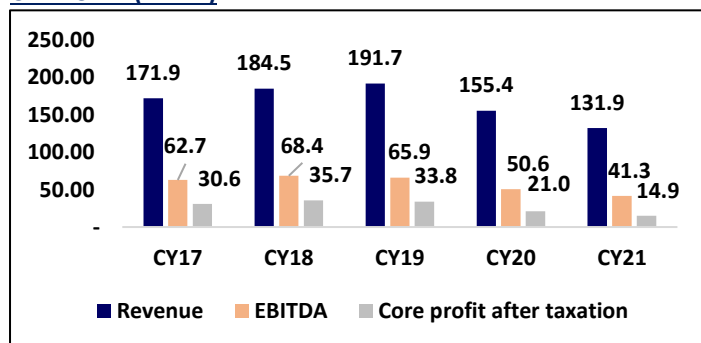
The combined revenue of InNature grew at a 3-year CAGR of 6.2% to RM191.7m in CY19, underpinned by opening of new outlets in Malaysia, Vietnam and expansion into Cambodia, coupled with improvements in average sales per store in Malaysia. Its remote channel sales had also improved significantly to RM5.0m in CY19 (CY17: RM3.3m), generating about 2.6% of InNature's total sales in CY19, albeit physical store sales remain as the largest revenue contributor.

Pandemic Speed Bumps Adversely Affected Topline

In CY20 and CY21, due to lockdown measures, InNature's retail stores sales in Malaysia were adversely impacted. Revenue of retail stores declined by 23.5% and 34.0% Y-o-Y respectively in CY20 and CY21, exacerbated by closing of non-performing outlets in Malaysia. However, this was partially cushioned by around 152% and 200% jump in remote channel sales in CY20 and CY21 respectively, making up 8.1% and 28.6% of total sales respectively, compared to only 2.6% in CY19. Most of the surge in remote sales were mainly attributed to InNature's management's efforts to promote omnichannel sales strategy which tends to encourage customers to shop more during movement restrictions and increase their brand loyalty via mobile apps along with the shift of shopping habits of consumers during and post-pandemic. We also note that Vietnam's sales still recorded 5.0% Y-o-Y growth in CY20 due to the opening of new outlets and surge in remote sales but registered a 17.7% Y-o-Y drop in CY21, impacted by lockdown measures imposed in Vietnam. Cambodia's sales were resilient in CY21 as it only decreased marginally by 2.2%, albeit movement restrictions were implemented in the country. It was noteworthy that in 1HCY22, the Cambodia operation recorded revenue of RM1.8m was at the highest level since CY20.

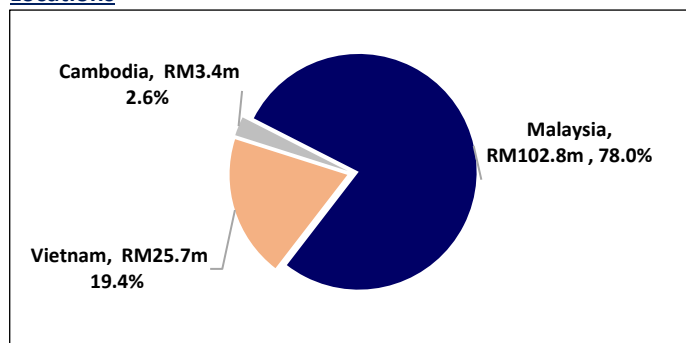
Apart from that, InNature is gradually and actively broadening its revenue contribution to Vietnam and Cambodia to prevent over-reliance on its Malaysia operations, as evidenced by the strong sales growth in Vietnam that grew by 39.4% between CY17-CY21 and Cambodia's sales grew 509% between CY19-CY21. In CY21, sales in Vietnam and Cambodia contributed 19.4% (CY16: 10.4%) and 2.6% (CY19: 0.3%) of the group's total sales respectively. Despite Cambodia's minimal contribution to the group's sales, it is believed that the payback period of new stores in Cambodia is the shortest among the 3 countries due to their better performance.

Figure 29: Revenue, EBITDA, Core Profit After Taxation between CY17-CY21 (RM m)



Source: Company, Inter-Pacific Research

Figure 30: Contribution of CY21 Sales from Each Geographical Locations



Source: Company, Inter-Pacific Research

Profitability Slightly Affected Amid Weaker Operating Environment

InNature's gross profit margin was maintained at a range of 66%-67%. However, it was compressed to 64.4% in CY21, impacted by lower sales revenue following aggressive discounts provided to clear inventories and write-off of slow-moving inventories of around RM700k. At the same time, rental rebates given by landlords in Vietnam partially mitigated the margin compression. Despite Covid-19 measures leading to lower profitability, management was still able to maintain the core net profit margin at double-digits level. To curb the inflationary pressure, InNature hiked the price of certain SKUs in 2021 and plans to introduce new range of products with higher selling price.

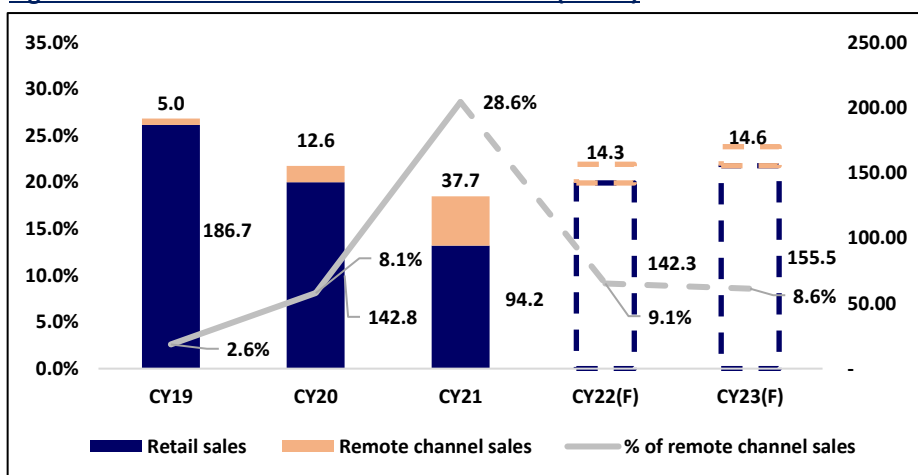
Projecting a 2-Year Revenue CAGR of 13.5% in CY21-CY23F with Improved Profit Margin

Moving forward, we estimate there will be a net addition of an outlet in Malaysia in CY23 with sales per store recovering to 80% of CY19 level, due to the launch of large-format concept stores and refurbishment of existing outlets which will attract more shoppers. For its Vietnam and Cambodia operations, we expect there will be at least a net addition of 4 and an outlet in CY23, where sales per store in both countries to recover relatively faster following the reopening of their borders. However, remote sales are likely to moderate following increasing outlet shopping traffic, coupled with opening of new outlets in 2nd tier cities in Vietnam, as management predicted that these outlets would make it easier for locals to shop in person rather than online.

We expect InNature's gross profit margin to progressively revert back to the 66%-67% levels on the back of: 1) hike in selling price of existing and new products, 2) launch of refill stations in at least half of the existing outlets which will diminish the usage of plastic bottles, 3) closure of more less-performing small outlets with opening of new larger-format outlets, 4) no more aggressive discounting and massive write-offs of inventory.

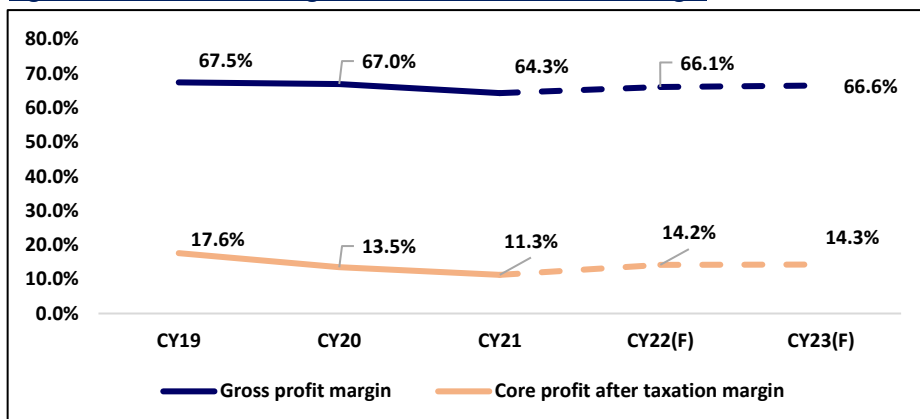
We also expect the core profit after tax margin to recover gradually to 14.2% and 14.3% in CY22F and CY23F respectively due to company's high operating leverage, in line with the 18.7% and 8.6% growth of sales in CY22F and CY23F respectively.

Figure 31: Retail Sales and Remote Channel Sales (RM m)



Source: Company, Inter-Pacific Research

Figure 32: Gross Profit Margin and Core Profit After Tax Margin



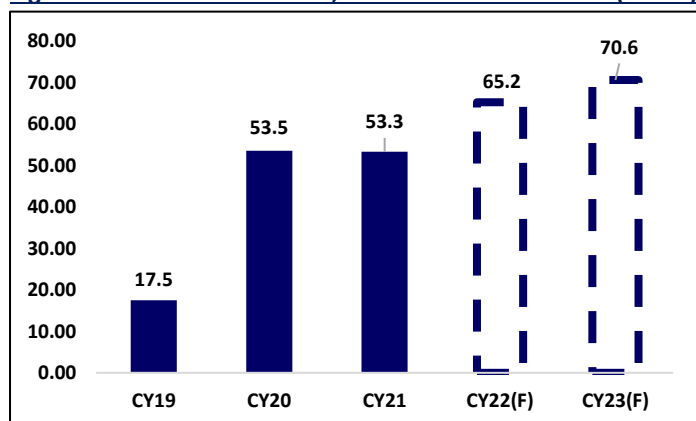
Source: Company, Inter-Pacific Research

Healthy Balance Sheet with Ample Cash Balances and Low Debts

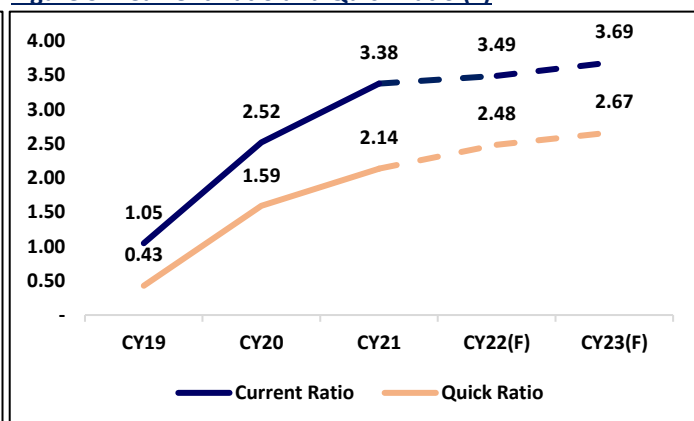
InNature's balance sheet is sturdy, with growing cash and bank balances and other investments. As of CY21, the cash and cash equivalents of RM53.3m were more than adequate to satisfy long-term and short-term commitments of RM20.9m. Thanks to its strong cash position and low debt level, InNature could easily fund its expansion plan. Although more than 50% of its total obligations comprised short-term debts, InNature's liquidity remained robust as its current ratio and quick ratio had improved strongly from CY19 to CY21, from 1.05x to 3.38x and from 0.43x to 2.14x respectively.

After InNature repaid RM16.0m to settle its revolving credit in CY20, its total debts as of CY21 decreased drastically by around 50%. Most of its current debt is in its lease liabilities with negligible amount of bank borrowings. InNature's gearing ratio stood at 0.14x as of CY21 and is expected to stay at this level for the foreseeable future.

Figure 33: Other Investments, Cash and Bank Balances (RM m) **Figure 34: Current Ratio and Quick Ratio (x)**

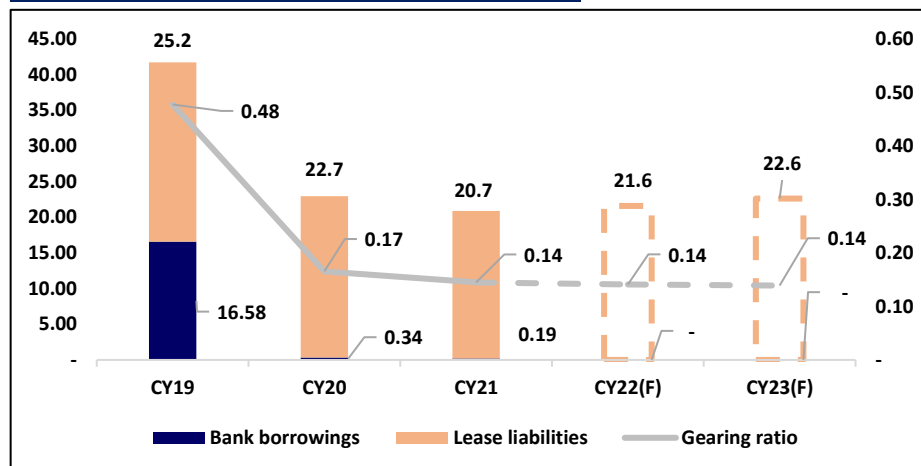


Source: Company, Inter-Pacific Research



Source: Company, Inter-Pacific Research

Figure 35: Total Debts (RM m) and Gearing Ratio (x)

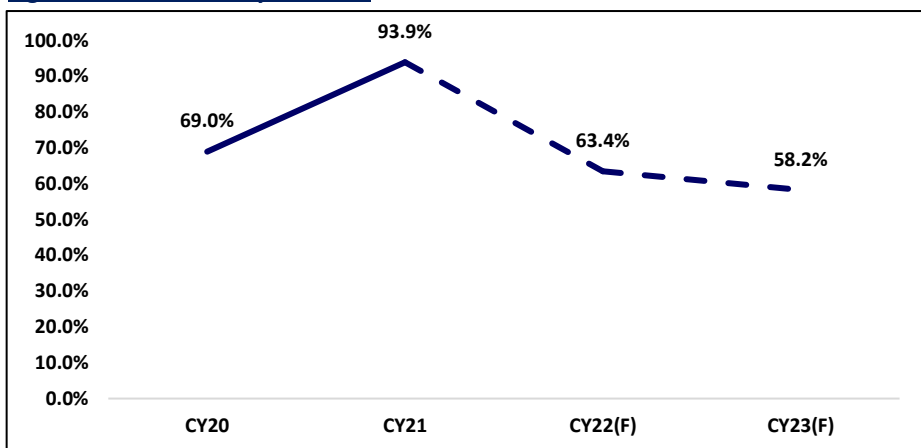


Source: Company, Inter-Pacific Research

At least 2.0 sen in Dividend to be Declared Annually from CY22F-CY23F

InNature has dividend policy of distributing at least 30% of annual audited shareholders' profit after tax as dividend. In CY20/21, company declared a 2.0 sen dividends each year with a payout ratio of 69.0%/93.9%. With the improvement of its projected financial performance, we expect at least 2.0 sen dividend to be declared in CY22F/23F, with a payout ratio of 63.4%/58.2%, translating into an approximate dividend yield of 3.6%.

Figure 36: Dividend Payout Ratio



Source: Company, Inter-Pacific Research

Note: Dividend declared in CY19 was prior to the listing period, therefore it is not included in the graph.

VALUATION AND RECOMMENDATION

Initiate coverage with BUY call and a TP of RM0.70

We initiate coverage on InNature with a **BUY** recommendation with target price of **RM0.70**, pegged to a target PER of 20.5x which translates to a potential 27.3% upside. We deem the PER valuation methodology as suitable for InNature as we project a strong recovery in InNature's earnings in CY22F and CY23F respectively and this approach is typically used in valuing consumer companies in Malaysia.

We also believe that the 20.5x target PER is justifiable for InNature on the back of: 1) robust rebound of its topline and bottomline, 2) excellent financial position, 3) improved profitability, and 4) decent dividend yield. The target PER is also at its historical average forward 12-month PER. Due to absence of comparable peers in Malaysia, we peg the peer comparison to selected retail operators in Malaysia and opined that a premium to the simple average forward PER of its peers is justifiable on the basis of its: 1) superior ESG initiatives, 2) better profitability, and 3) regional diversification of revenue.

Despite being a franchisee of the TBS brand, InNature's gross profit margin and net profit margin are comparable to the selected global cosmetics and personal care companies' average. Nevertheless, a discount to the simple average forward PER of global peers is deemed appropriate given its much smaller market capitalisation and absence of ownership of the brand.

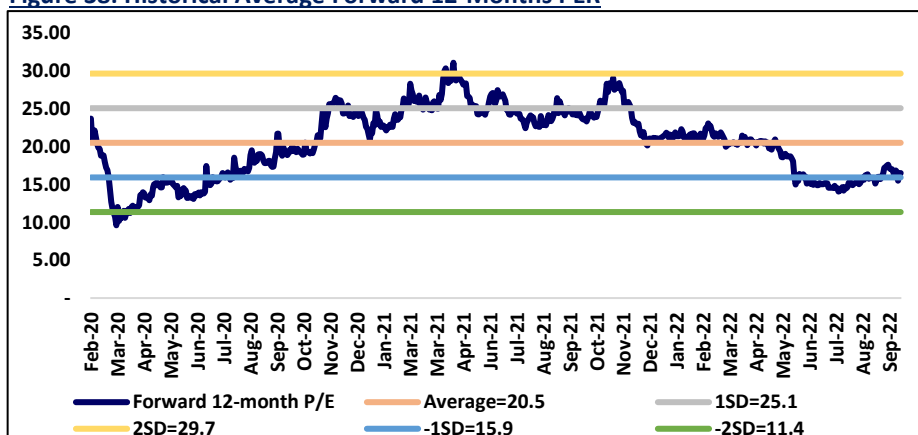
Figure 37: Peer Comparison of Selected Retail Players in Malaysia

Companies	Innature Bhd	Padini Holdings Bhd	Berjaya Food Bhd	Amway Malaysia Holdings Bhd	Bonia Corporation Bhd	Focus Point Holdings Bhd	Simple Average
FYE	Dec-22	Jun-22	Jun-22	Dec-22	Jun-22	Dec-22	
Share price	0.55	3.15	0.87	5.00	1.93	0.74	
Market Cap	388.2	2,072.4	1,684.7	821.9	389.0	242.5	
2022 P/E (x)	17.5	13.4	12.7	18.8	8.6	7.1	13.0
2023 P/E (x)	16.0	13.9	12.4	13.8	9.0	7.0	12.0
2022 P/B (x)	2.5	2.3	3.2	3.6	1.0	2.5	2.5
2023 P/B (x)	2.4	2.2	2.8	3.5	1.0	1.8	2.3
ROE (%)	10.6	18.2	28.5	16.7	11.8	19.5	17.6
DPS (sen)	3.0	10.0	5.5	24.0	8.0	2.0	
Dividend yield (%)	5.5	3.2	6.4	4.8	4.1	2.7	4.4

Source: Bloomberg, Inter-Pacific Research

Note: Bonia Corporation Bhd's 11 sen special dividend was excluded.

Figure 38: Historical Average Forward 12-Months PER



Source: Bloomberg, Inter-Pacific Research

FINANCIAL HIGHLIGHTS

FYE Dec	CY19	CY20	CY21	CY22(F)	CY23(F)
Income Statement (RM m)					
Revenue	191.7	155.4	131.9	156.6	170.1
EBITDA	65.9	50.6	41.4	46.7	51.7
Depreciation and amortisation	21.0	21.4	20.2	16.3	18.7
Net interest (expenses)/income	(1.8)	(1.3)	(0.7)	(1.1)	(1.1)
Pre-tax profit	40.4	27.4	20.4	29.3	31.9
Tax	(10.2)	(7.4)	(5.5)	(7.0)	(7.7)
PATAMI	30.2	20.0	14.9	22.3	24.2
EPS	4.3	2.8	2.1	3.2	3.4

Source: Company, Inter-Pacific Research

FYE Dec	CY19	CY20	CY21	CY22(F)	CY23(F)
Balance Sheet (RM m)					
Property, plant & equipment	14.0	12.9	8.9	11.8	16.0
Other LT assets	84.4	81.8	79.6	80.2	81.0
Total cash and equivalents	17.5	53.5	53.3	65.2	70.6
Other ST assets	39.6	40.1	42.1	36.3	36.8
Total assets	155.4	188.2	183.9	193.5	204.3
ST borrowings	30.4	12.6	11.2	12.0	12.0
Other ST liabilities	24.1	24.6	17.1	17.1	17.1
LT borrowings	11.4	10.4	9.7	9.6	10.6
Other LT liabilities	2.2	2.0	1.8	1.8	1.8
Total liabilities	68.1	49.6	39.8	40.5	41.5
Share capital	4.4	50.3	50.3	50.3	50.3
Other equity and reserves	83.0	88.4	93.8	102.7	112.4
Total equity	87.3	138.7	144.1	153.0	162.7
Total equity and liabilities	155.4	188.2	183.9	193.5	204.3

Source: Company, Inter-Pacific Research

FYE Dec	CY19	CY20	CY21	CY22(F)	CY23(F)
Key Metrics					
Revenue growth (%)	3.9	(19.0)	(15.1)	18.7	8.6
EBITDA growth	(3.6)	(23.2)	(18.3)	12.9	10.8
PATAMI growth	(33.9)	(33.8)	(25.5)	49.5	9.0
EBITDA margin (%)	34.4	32.6	31.3	29.8	30.4
PATAMI margin (%)	15.7	12.9	11.3	14.2	14.3
Net gearing ratio (x)	0.3	Net Cash	Net Cash	Net Cash	Net Cash
ROE (%)	37.1	17.7	10.5	15.0	15.4
ROA (%)	20.2	11.6	8.0	11.8	12.2

Source: Company, Inter-Pacific Research

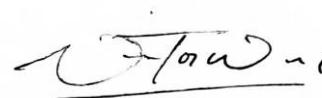
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Signed



Victor Wan Kum Seng
Head of Research
Inter-Pacific Research Sdn Bhd

Rating Systems

Ratings:	Description:
BUY	Total return is expected to exceed 15% in the next 12 months
TRADING BUY	Total return is expected to exceed 10% in the next 3 months
NEUTRAL	Total return is expected to be between -15% to 15% in the next 12 months
SELL	Total return is expected to be below -15% in the next 12 months
TRADING SELL	Total return is expected to be below -10% in the next 3 months
NOT RATED	The stock is not within regular research coverage

Abbreviation

Abbreviation	Definition	Abbreviation	Definition
PER	Price Earnings Ratio	CAGR	Compounded Annual Growth Rate
PEG	PER to Growth	CAPEX	Capital Expenditure
EPS	Earnings per Share	DPS	Dividend per Share
FYE	Financial Year End	ROA	Return on Asset
FY	Financial Year	ROE	Return on Equity
CY	Calendar Year	PBT	Profit Before Tax
MoM	Month-on-Month	PAT	Profit After Tax
QoQ	Quarter-on-Quarter	EV	Enterprise Value
YoY	Year-on-Year	EBIT	Earnings Before Interest And Tax
YTD	Year-to-Date	EBITDA	EBIT Depreciation & Amortisation
p.a.	Per Annum	WACC	Weighted Average Cost of Capital
DCF	Discounted Cash Flow	NTA	Net Tangible Asset
FCF	Free Cash Flow	BV	Book Value
NAV	Net Asset Value		

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Inter-Pacific Research Sdn Bhd (449005-X)

West Wing, Level 13,
Berjaya Times Square,
No.1, Jalan Imbi,
55100 Kuala Lumpur
General Line : 03-2117 1888 Fax : 03-2142 7678