

Nova Wellness Group Berhad

Initial Public Offering

SUBSCRIBE

IPO Price	RM 0.55
Fair Value	RM 0.61

IPO Summary

Enlarged issued share capital	317.7m
Malaysian Public	16.0m
Eligible Persons	15.0m
Private Placement	50.6m
Market Capitalisation	RM174.8m
Share Capital	RM60.1m

Major Shareholders (%)

Tan Sok Mooi	42.5
Phang Nyie Lin	7.95
Phang Yeen Nung	7.95
Phang Yeen Aun	7.95
Phang Yeen Hung	7.95

Indicative Timetable

Issuance of Prospectus	28/6/18
Opening of application for IPO	28/6/18
Closing of application for IPO	09/7/18
Balloting of shares	11/7/18
Allotment of shares	19/7/18
Listing on the Ace Market	20/7/18

Analyst: Wong Ling Ling

Email: wongll@interpac.com.my

Wellness is the Key

We place a fair value of RM0.61 with a SUBSCRIBE recommendation on Nova Wellness.

We derive our fair value based on our forecast FY19 EPS of 4.7 sen pegged to a 13x PER.

The nutraceutical industry in Malaysia is forecasted to grow with the backing of the increase in awareness and demand for preventive healthcare. In addition, Nova Wellness is also looking to expand its presence in the skincare products segment. We favour Nova Wellness for the reasons: 1) Nova has an in-house R&D department 2) An experienced management team 3) Intended dividend payout policy of 30% offers a good yield 4) Capacity expansion after new GMP-compliant production facility is ready

Company Overview

The Nova Wellness Group was first incorporated as Nova Laboratories in 1989 when the co-founder Mr Phang undertook the trading of animal health products. It gradually progressed by undertaking their own Research & Development (R&D). The Nova Wellness Group is involved in the research, development, production, and sales of nutraceutical and skincare goods under an in-house brand, as well as the provision of OEM services for manufacturing dietary supplements and functional food products.

Table 1 :Investment Highlights & Earnings Forecasts

FYE June (RM'mil)	2015	2016	2017	2018(F)	2019(F)
Revenue	22.8	24.3	24.5	25.5	27.0
GP	16.8	17.7	17.6	18.4	19.6
PBT	12.3	13.6	13.6	14.1	15.0
PAT	12.3	13.5	13.7	14.0	15.0
GP Margin (%)	73.3	72.9	71.7	72.0	72.4
PBT Margin (%)	53.9	55.8	55.5	55.2	55.7
PAT Margin (%)	53.7	55.8	55.9	55.0	55.5
EPS (sen)	3.9	4.3	4.3	4.4	4.7
PER (x)	14.2	12.9	12.7	12.5	11.7
DPS (sen)	NA	NA	NA	1.5	2.0
Dividend Yield (%)	NA	NA	NA	2.7	3.6
ROE (%)	63.4	76.3	70.8	26.4	26.9
ROA (%)	49.2	51.1	52.1	26.8	23.7
P/BV (x)	9.0	9.9	9.0	3.3	3.1
Net Gearing Ratio (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

Source: Company, Inter-Pacific

Business Overview

The group generates revenue from its 3 main segments namely its House Brand, OEM and Animal Health segments, with a key focus on educating consumers on the importance of nutrition in their diet as a preventive measure against chronic diseases. House Brand products are grouped into 2 main categories; nutraceutical products and skincare products. The OEM segment provides OEM services such as customised formulation of products, procurement of raw materials, and packaging materials, production and final packaging of finished products. End products are sold under the customers’ own brand. In total, the Group has nine OEM customers, seven local and two abroad, located in Hong Kong and Singapore respectively.

Illustration 1: Corporate Structure

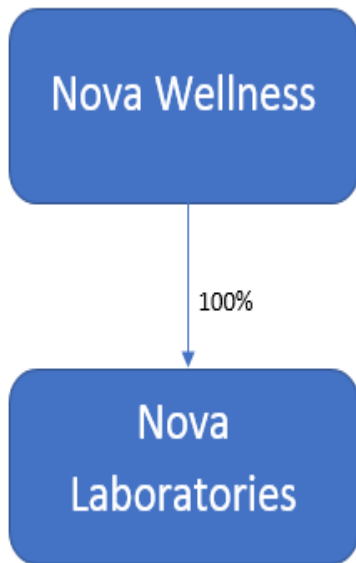


Illustration 2: Nova Wellness principal business activities



Source: Company prospectus, Inter-pacific Research

Marketing through Nova Wellness Partnership Program (NWPP)

One of the marketing strategies employed by the Group is the NWPP. Exclusive distribution rights within specified areas were given to independent retail pharmacies. NWPP partners will act as their sales channel, where retail staff are more engaging in their approach with customers than chain pharmacies and large supermarkets to offer a more engaging shopping experience hence building longer lasting relationships and health awareness amongst their customers. Such appointed independent retail pharmacies have to maintain a minimum purchase every month during the duration. Agreements on the program are valid for one year, open to renewal. This minimum purchase requirement provides some level of certainty to Nova’s recurring revenue base. Per prospectus information, Nova has 105 independent retail pharmacies and looks to focus on expanding the numbers in the NWPP in the coming few years.

Products and Services

Nutraceutical products

(i) Dietary supplements

Dietary supplements include vitamin, mineral and herbal supplements. Formulated to increase daily intake of nutrient(s), they are marketed under the 'Nova' House Brand. Currently, there are 49 dietary supplements being marketed.



Hepar-P, one of the earliest in their product line and is a key product of the Group, contains extracts of Phyllanthus niruri which is used as a liver tonic.

(ii) Functional food products

Formulated with a focus on having low glycemic index and balanced nutrients, the products are sold under two House Brands, 'Activmax' and 'Sustinex'. Currently, there are 11 functional food products being marketed.



Products and food with low glycemic index indicates that it is slow to digest and sugars are metabolised at a slower rate, making it easier to manage blood glucose levels.

(iii) Skincare products

Mainly natural ingredients from plants are used in the development of Nova Wellness Group's skincare products. They are marketed under the 'Novavis' and 'SP8' House brands. Currently, there are 28 separate skincare products being marketed.



The production of skincare products is currently outsourced to Nutriskin Marketing Sdn Bhd based on the Group's formulation.

Table 2: IPO Utilisation

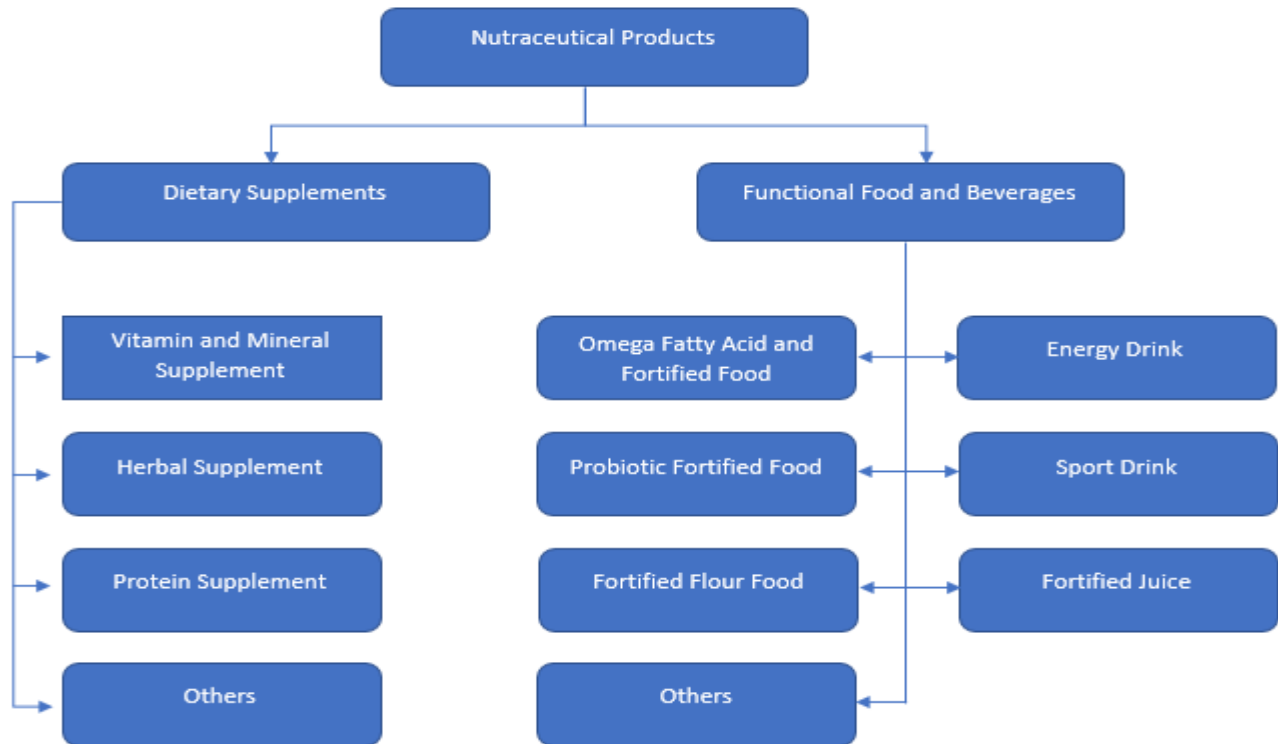
Description	Amount (RM'm)	Percentage of total gross proceeds (%)	Estimated Timeframe for utilisation upon Listing
Construction of a new GMP-compliant production facility	16.5	36.7	Within 24 months
R&D activities	11.6	25.8	Within 36 months
Expansion of retail market presence	5.0	11.2	Within 36 months
Working Capital	9.2	20.5	Within 12 months
Estimated listing expenses	2.6	5.8	Immediate
Total gross proceeds	44.9	100.0	

Source: Inter-Pacific Research

Industry Overview

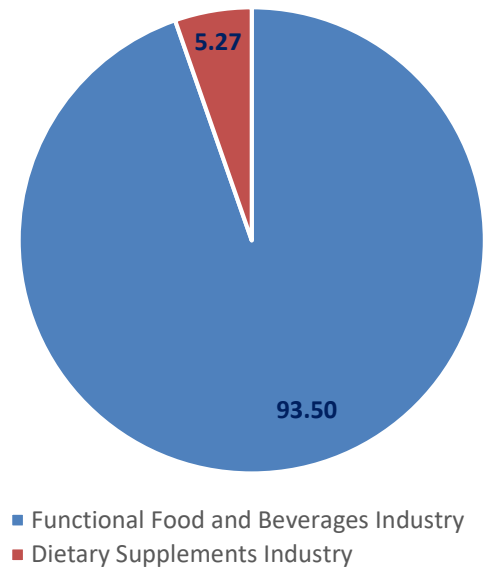
The nutraceutical industry is generally divided into two segments, functional foods and dietary supplements. Nova Wellness is mainly involved in the industry of manufacturing dietary supplements.

Illustration 3: Types of Nutraceutical Products in Malaysia



Source: Protégé Associates, Inter-Pacific Research

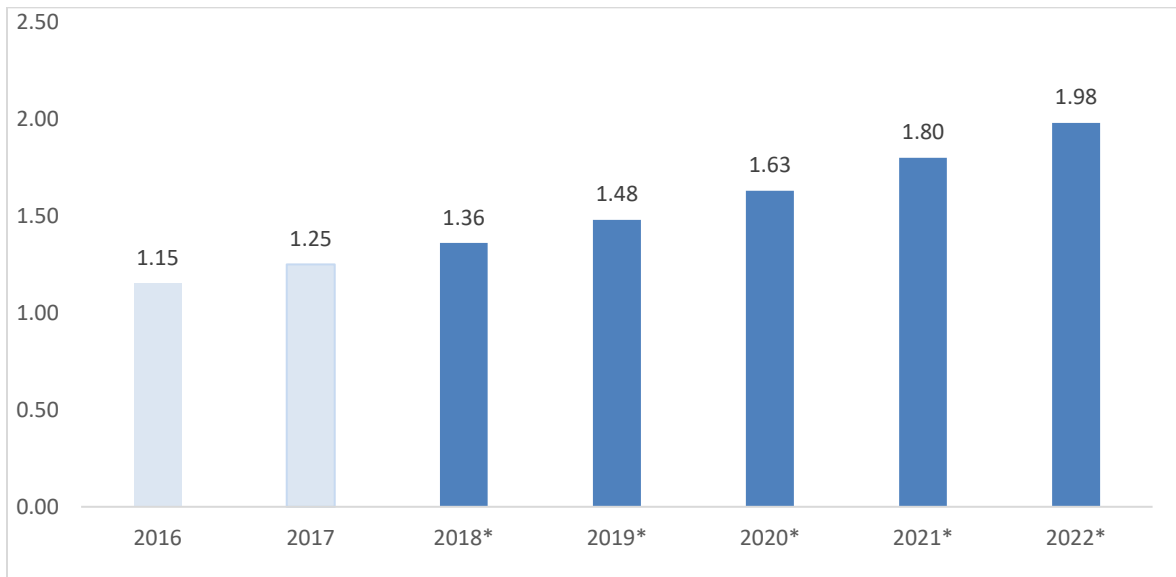
Graph 1: Functional Food vs Dietary Supplement Industry Size in Malaysia (RM'bil)



Based on an industry research report by Protégé Associates, revenues generated by the nutraceutical industry in Malaysia amounted to RM98.8bil in 2017 where, inclusive of imports and locally manufactured products, functional foods made up 94.7% by size, and dietary supplements made up the remaining 5.3%. The CAGR for dietary supplements manufacturing in Malaysia from 2018 to 2022, with 2017 as base year, is forecasted to be 9.7%. The total market size for the Dietary Supplements manufacturing industry in Malaysia in year 2017 is RM1.25bil. Nova Wellness recorded a total revenue of RM19.8mil in 2017 from sales of dietary supplements which translates to approximately 1.6% by market share. The nutraceutical industry in Malaysia is a saturated industry has an approximately 600 industry players involved in the manufacturing or important of dietary supplements.

Source: Protégé Associates, Inter-Pacific Research

Graph 2: Dietary Supplement Manufacturing Industry Size and Forecast in Malaysia (RM'bil)



*denotes forecast

Source: Protégé Associates, Inter-pacific Research

The nutraceutical industry’s forecast CAGR from 2018 to 2022 is 2.5%, with the industry size projected to reach RM111.51bil in 2022. The Malaysian dietary supplement manufacturing industry is forecasted to reach RM1.98bil by 2022 implying strong growth

between 9% to 10.5% from 2018 to 2022. Potential key catalysts expected to drive the demand for the nutraceutical industry are the increased financial burden from higher medical costs leading to the increase in the awareness of the value of preventive healthcare, the increasing prevalence of chronic lifestyle diseases and higher disposable income. Besides, the aging Malaysian population is also expected to increase Malaysians demand on nutraceutical products to prevent/delay age-related diseases.

Competitive Advantage

Wide distribution network across Malaysia for House Brand products

Nova Wellness has a wide distribution network for their own House Brand products across Malaysia. The group distributes their products via independent retail pharmacies. Per prospectus information, there are currently a total of 227 independent retail pharmacies in Malaysia that sells Nova Wellness's own brand products. Among the 227 independent retail pharmacies, a total of 105 pharmacies are NWPP partners. In return, NWPP partners provide valuable feedback and information based on the most recent market trends and consumer preferences back to Nova Wellness. The group will thus be able to keep its competitiveness especially vis-à-vis larger competitors who have a presence in the international market.

In-house R&D and production facility

The group's Managing Director, Mr Phang Nyie Lin spearheads the R&D department. An in-house R&D facility in Sepang provides Nova Wellness with the platform to expand their product range as well as to improve our existing products to meet market demand and customers' requirements. The current R&D team consists of a registered pharmacist, two microbiologists and two laboratory technicians. To-date, the group has managed to develop 49 dietary supplements, 11 functional food products and 28 skincare products. All products are currently available for sale in both the domestic and international market.

On top of this, the group's own production facility enables Nova Wellness to produce a range of nutraceutical products under their own house-brands and to conform to the standards required by relevant authorities including GMP-compliance and Halal certification. An in-house production facility allows the group to control the entire production process to minimize unplanned interruptions hence ensuring the quality of products and making it safe for use. In the long run, the group plans to increase its production capacity for functional food and skincare products by acquiring new machinery with the IPO proceeds.

Table 3: Shareholdings of Promoters and substantial shareholders before and after IPO

	Before the IPO				After the IPO			
	Direct		Indirect		Direct		Indirect	
	No. of Shares (m)	%	No. of Shares (m)	%	No. of Shares (m)	%	No. of Shares (m)	%
Phang Nyie Lin	25.2	10.7	210.8	89.3	25.2	8.0	210.8	66.4
Tan Sok Mooi	135.1	57.2	-	-	135.1	42.5	-	-
Phang Yeen Nung	25.2	10.7	-	-	25.2	8.0	-	-
Phang Yeen Aun	25.2	10.7	-	-	25.2	8.0	-	-
Phang Yeen Hung	25.2	10.7	-	-	25.2	8.0	-	-

Source: Company prospectus, Inter-pacific Research

Future Plans

1. Construction of a new GMP-Compliant Production Facility
 - a) To expand on the production capacity of the Group's functional food and skincare products
2. R&D Activities
 - a) To manufacture products with clinically confirmed health benefits which are expected to lend further credence and to increase the acceptance of the group's products.
3. Expansion of Retail Market
 - a) Expanding the group's geographical footprint and increase a presence in the online retail space by creating brand awareness through promotional campaigns.

Investment Risks

Dependent on major customers and NWPP partners

Nova Wellness's top 3 major customers each contributed to approximately 10% of the group's total revenue in FY17 while the NWPP partners contributed significantly towards the group's revenue. NWPP partners clocked in a total revenue of RM14.8mil which translates to approximately 60.4% of the group's total revenue in FY17. As there is no assurance that the NWPP partners will continue to provide support in the near future, the group's operating results will see a material impact if there are NWPP partners which discontinue the partnership arrangement.

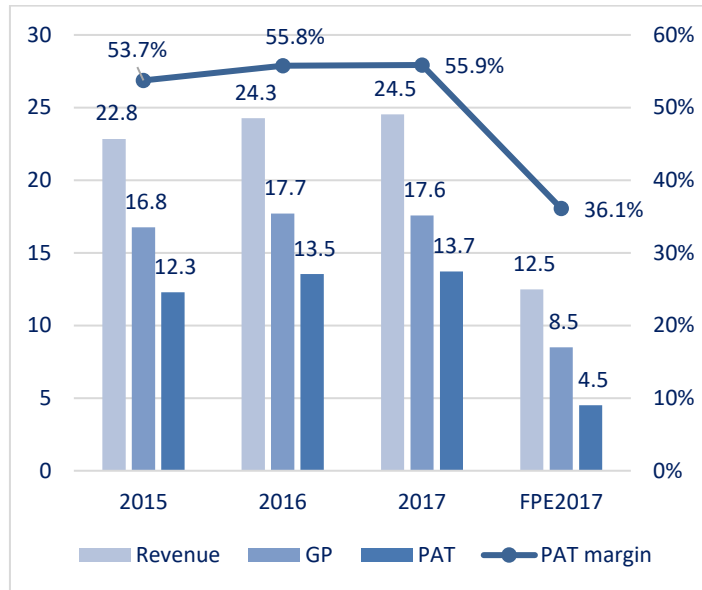
Exposed to risk of unsuccessful pre-clinical and clinical trials

The group currently estimated the cost for pre-clinical and clinical trials for Hepar-P at RM13.2mil. With funds being generated from NKEA grant worth RM2.6mil, the remaining RM10.6mil will be funded using the IPO proceeds. As with all pre-clinical and clinical trials, it will be exposed to the risk of unsuccessful trials. Any unsuccessful trial will affect the group's competitiveness and their ability to promote and increasing the sales of Hepar-P Capsule. If such an event does occur, Nova Wellness will not be able to recover costs incurred previously.

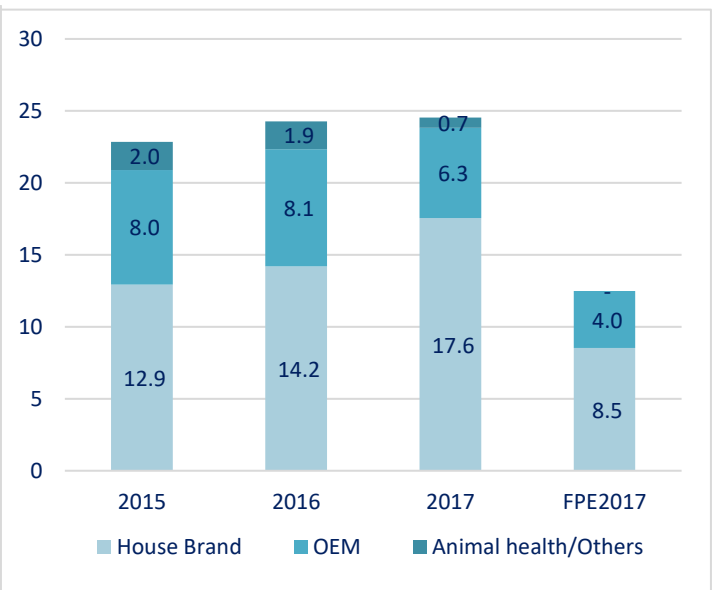
Company Financials

Nova Wellness recorded a total revenue of RM24.5mil for FY17. Revenue grew at a CAGR of 3.7% between FY2015 to FY2017. The House Brand Segment remains as the biggest contributor to the group in revenue terms. In FY17, the House Brand segment grew by 23.7% as the brand managed to achieve a better market penetration rate in the local market. The group enjoyed higher sales of their dietary supplement products and incremental volume orders from their NWPP partners. However, the growth in the total revenue were offset by the decline in the revenue for both the OEM and Animal Health segments.

Graph 3: Financial Highlights (RM'mil)



Graph 4: Revenue Breakdown by Segment (RM'mil)



Source: Company prospectus, Inter-Pacific Research

Note: FPE17 denotes the 6-month period ending 31st Dec2017

Margin wise, the House Brand segment enjoys the highest margin among the segments with the skincare products providing the highest GP margins for all. However, sales for the skincare segment is relatively low. Hence, in the long run, the group hopes to expand this segment. Nova Wellness enjoys a PAT Margin of 55.9% in FY17 in line with the industry average. The group enjoys a lower effective tax rate compared to the Malaysian statutory tax rate of 24%. Nova Wellness was granted a 100% tax exemption on the statutory income from the tax incentive arising from the BioNexus-status on qualifying activities from FY2008 to FY2017. Tax exemption expired in FY17 and the group is currently applying for the extension to its Malaysian Bioeconomy Development status. Pending approval, the PAT margin for FPE2017 was calculated based on the assumption that Nova Wellness will not be able to renew the BioNexus-status.

The group intends to adopt a 30% distribution rate on annual audited profit as its formal dividend policy. As of Prospectus launch, the group does not have any outstanding borrowings, hence the group maintains a net cash position.

Valuation

We value Nova Wellness at a target price of RM0.61 pegged to a 13x PER based on our forecast FY19 EPS of 4.7sen. Our target price implies a potential upside of 10.9% from its IPO price. The new GMP-Compliant Production Facility is targeted to commence operation by March 2019 however, we use a more conservative approach on the earnings forecast as we factor in the possibility of teething problems on the new plant before it fully commences. For reference, we benchmark Nova Wellness Group shares against Bioalpha Holdings and CCM Duopharma Biotech as its closest peers on the local bourse.

Table 4: Peer comparison table as of 5th July 2018

	Share Price (RM)	Market Capitalisation (RM'm)	EPS (sen)	PER (x)	ROE (%)	ROA (%)	Dividend Yield(%)
Bioalpha Holdings Berhad	0.235	190.2	1.3	17.1	8.2	7.3	0.4
CCM Duopharma Biotech Berhad	1.3	846.2	6.7	19.3	9.1	6	2.8
Nova Wellness Group Berhad	0.55	174.7	4.3	12.7	70.8	52.1	NA

Table 5: Profile of Key Management

Name	Designation	Background
Yeoh Kim Kooi	CFO	Aged 34. Graduated with a Bachelor of Science in Applied Accounting at Oxford Brookes University, UK in 2008. Previously worked as a senior auditor and as a financial controller at different firms.
Nicholas Cheong Peck Hiang	Chief Business Officer	Aged 36. Graduated from University of Northumbria, UK with a Bachelor of Arts in Marketing in 2004. Worked as a sales representative for Nova Laboratories in 2005, was later promoted to sales manager in 2007, and then CBO in 2015.
Tan Kiat Wei	Chief Production Officer	Aged 31. Graduated from Cyberjaya University College of Medical Sciences with a Bachelor of Pharmacy in 2012. Underwent a training as a trainee in 2012 and moved onto become a production pharmacist in a cream manufacturing and packaging division. In 2014, he started at Nova Laboratories as a marketing manager and later transferred over to the production department as a production manager. Was promoted to Chief Production Officer in 2016.
Sangeetha Thuraisingam	Chief Quality Officer	Aged 33. Graduated from Tunku Abdul Rahman University with a Bachelor of Science in Biotechnology in 2006. Joined Nova Laboratories in after graduating as an executive. Became Regulatory Manager in 2007 and later Regulatory & QA Manager in 2008, overseeing GMP Quality System functions, and ensuring, compliance, safety and quality of products. In 2016, was appointed CQO where she is responsible for quality and compliance throughout the production.

Table 6: Profile of Board of Directors

Name	Designation	Background
Phang Nyie Lin	Co-founder, Promoter, Managing Director, Chief Research Officer	Aged 63, appointed to the Board on 31 October 2017. Graduated with a Bachelor of Pharmacy from Universiti Sains Malaysia in 1980. As MD, he is responsible for the direction and supervision of the company. As Chief Research Officer and qualified pharmacist, he leads R&D activities which mainly involves research of natural botanical ingredients and developing new products and improving existing products of the Group.
Phang Yeen Nung	Promoter, Executive Director	Aged 35, appointed to the Board on 31 October 2017. Graduated with a Bachelor of Laws at the University of Kent, UK in 2012. Became business development director in 2014, in charge of procuring new business contracts and managing customer relations for the Group. Son to Phang Nyie Lin and Tan Sok Mooi. Brother to Phang Yeen Aun and Phang Yeen Hung.
Phang Yeen Aun	Promoter, Executive Director	Aged 32, appointed to the Board on 31 October 2017. Graduated with a Bachelor of Pharmacy at the International Medical University, Malaysia in 2009. Oversees marketing activities in the Group and assisting in R&D particularly product formulation.
Dr Abdul Manaf bin Mohamad Radzi	Independent Non-Executive Chairman	Appointed to the Board on 31 October 2017. Chairman of Remuneration and Nomination Committees and a member of the Audit and Risk Management Committees.
Dr Munavvar Zubaid bin Abdul Sattar	Independent Non-Executive Director	Appointed to the Board on 31 October 2017. Member of Remuneration, Nomination and Risk Management Committees.
Sulaiman bin Haji Ahmad	Non-Independent Non-Executive Director	Appointed to the Board on 31 October 2017. Member of Remuneration and Nomination Committees.
Sim Seng Loong @ Tai Seng	Independent Non-Executive Director	Appointed to the Board on 31 October 2017. Chairman of the Audit Committee and Risk Management Committee.
Tan Mio Har	Independent Non-Executive Director	Appointed to the Board on 31 October 2017. Member of Audit Committee.

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(ii) As of July 9, 2018, the analyst(s) who prepared this report, and the associate(s), has / have an interest in the securities (which may include but not limited to shares, warrants, call warrants and/or any other derivatives) in the following company or companies covered or recommended in this report: (a) Wong Ling Ling - nil.

Signed



Pong Teng Siew
Director
Inter-Pacific Research Sdn Bhd

Ratings System

Ratings:	Description:
BUY	Total return is expected to exceed 15% in the next 12 months
NEUTRAL	Total return is expected to be between above -15% to 15% in the next 12 months
SELL	Total return is expected to be below -15% in the next 12 months

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 SdnBhd (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