

29 April 2024

Consumer Cyclical | Consumer Products

Synergy House (SYNERGY MK)

Buy (Maintained)

Going All Out; Keep BUY

Target Price (Return): MYR1.61 (21%)
 Price (Market Cap): MYR1.33 (USD139m)
 ESG score: 2.9 (out of 4)
 Avg Daily Turnover (MYR/USD) 1.06m/0.22m

- **Keep BUY, new MYR1.61 TP from MYR1.08 (21% upside), c.2% FY25F yield.** We are optimistic on the potential of data analytics to study customer behaviour and boost traffic, thereby driving scalability in Synergy House's business-to-consumer (B2C) e-commerce business. Given its higher-than-expected earnings growth (compelling FY24F PEG of 0.3x) and scalability, we have raised the P/E ratio from 15x to 20x FY24F earnings, resulting in our higher TP. The valuation is consistent with the 5-year average P/E of its closest regional peer, Zhiou Home Furnishing Tech.
- **Business-to-business (B2B) sales growing.** In 4Q23, Synergy fulfilled the first batch of a new order for interlocking drawers from its US wholesaler, Customer A. The order was in response to new safety standards enforced by the US Consumer Product Safety Commission, requiring interlocks in clothing storage units. Following positive customer feedback, Customer A placed 400 more container orders for one of the world's largest hypermarkets to sell in stores and online in the US. While existing B2B product line orders are unchanged, we adjusted our B2B sales growth from flattish to a 10% hike. We revise FY24F and FY25F core earnings projections upwards by 12% and 12.5% to MYR40.2m (+54% YoY) and MYR51.3m.
- **Embracing artificial intelligence (AI).** At a recent site visit, we saw how Synergy fully integrated AI and data analytics into its operations, from design and development to project management, advertising, monitoring, marketing, and shipping. It has adopted cutting-edge semi-automatic drawing software for product design, and instead of manual photography, it uses 3D product images and room views. In advertising and monitoring, it conducts competitor analysis by monitoring changes in pricing and sales via AI-powered tools. It uses data analytics to identify most-searched keywords to reach its target customers. In marketing, it uses data analytics to access real-time data from online platforms on order replenishment and market trend analysis, including preferred colours and best-selling designs. AI is used in drafting product descriptions, while chatbots and AI are used for customer service. AI adoption enhances productivity and speeds up B2C sales growth.
- **Expansion on track.** Synergy had 185 employees as of March, and aims to reach 200 this year. In efforts to diversify its reliance on Wayfair US, its B2C sales in the UK and other new platforms are growing fast. Early this year, Synergy kept sufficient inventory in third-party fulfilment centres for new year sales in the US and UK after experiencing a shortage in 1Q23. This year, it is also increasing its B2C SKUs by 25%. As B2C sales growth is anticipated to outpace B2B, we expect higher-margin B2C sales to eclipse B2B sales in FY24. B2C sales are also expected to account for 70% of total sales in FY25.
- **Key risks:** Absence of long-term contracts with B2B customers, competition risk, and high exposure to FX fluctuations.

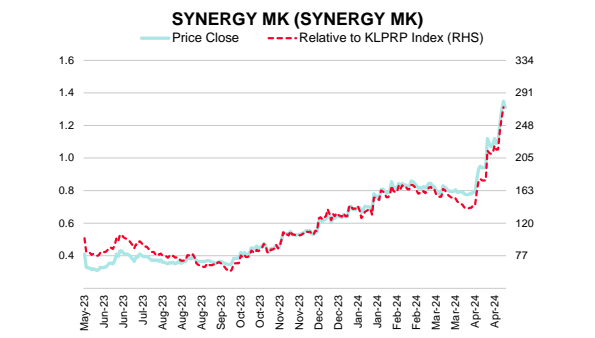
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	88.7	66.3	62.2	186.0	0.0
Relative	71.6	65.9	53.0	167.2	0.0
52-wk Price low/high (MYR)	0.33 – 1.37				



Source: Bloomberg

Overall ESG Score: 2.9 (out of 4)

E: GOOD

Synergy uses particle boards which do not contribute to more deforestation, as the raw material of its home furniture sold and has obtained Forest Stewardship Council (FSC) certificates.

S: MODERATE

Synergy promotes good health and a healthy working environment by having company events and weekly sports activities among its staffs. It also contributes to the society via donation.

G: EXCELLENT

Synergy established a comprehensive framework for the prevention and detection of bribery and corruption. The group also introduced an Internal Controls Policy which includes code of conduct declaration by all employees as well as mandatory learning to cover business ethics.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (MYRm)	194	270	376	456	569
Recurring net profit (MYRm)	17	26	40	51	70
Recurring net profit growth (%)	(5.8)	51.1	54.2	27.4	36.1
Recurring P/E (x)	38.52	25.49	16.53	12.97	9.53
P/B (x)	14.3	6.6	5.1	4.0	3.1
P/CF (x)	34.04	na	11.40	15.73	12.14
Dividend Yield (%)	0.9	1.2	1.8	2.3	3.1
EV/EBITDA (x)	23.95	16.25	10.63	8.12	5.80
Return on average equity (%)	41.2	34.7	35.0	34.8	36.7
Net debt to equity (%)	76.7	17.0	net cash	net cash	net cash

Source: Company data, RHB

See important disclosures at the end of this report

Market Dateline / PP 19489/05/2019 (035080)

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Malaysia	Recurring EPS	0.03	0.05	0.08	0.10	0.14
Consumer Cyclical	DPS	0.01	0.02	0.02	0.03	0.04
Synergy House	BVPS	0.09	0.20	0.26	0.33	0.43
SYNERGY MK	Return on average equity (%)	41.2	34.7	35.0	34.8	36.7
Buy						
	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Valuation basis	Recurring P/E (x)	38.52	25.49	16.53	12.97	9.53
20x P/E on FY24F EPS	P/B (x)	14.3	6.6	5.1	4.0	3.1
	FCF Yield (%)	1.5	(1.2)	8.2	6.1	7.9
Key drivers	Dividend Yield (%)	0.9	1.2	1.8	2.3	3.1
i. Business-to-business (B2B) sales growing;	EV/EBITDA (x)	23.95	16.25	10.63	8.12	5.80
ii. Embracing AI;	EV/EBIT (x)	25.45	17.03	10.99	8.42	5.96
iii. Expansion on track.						
	Income statement (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Key risks	Total turnover	194	270	376	456	569
i. Dependent on third-party manufacturers;	Gross profit	46	81	115	144	185
ii. Absence of long-term contracts with B2B customers;	EBITDA	29	42	60	76	102
iii. High exposure to FX fluctuation;	Depreciation and amortisation	(2)	(2)	(2)	(3)	(3)
iv. Competition risk.	Operating profit	28	40	58	74	99
	Net interest	(3)	(3)	(3)	(2)	(2)
	Pre-tax profit	23	36	56	71	97
Company Profile	Taxation	(7)	(10)	(15)	(20)	(27)
Synergy is a cross border e-commerce seller and furniture exporter who specialises in aesthetically pleasing designs which are affordable and ready-to-assemble (RTA) home furniture.	Reported net profit	17	26	40	51	70
	Recurring net profit	17	26	40	51	70
	Cash flow (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Change in working capital	0.0	0.0	13.4	(14.0)	(19.6)
	Cash flow from operations	19.5	(5.6)	58.3	42.3	54.8
	Capex	(9.7)	(2.6)	(3.5)	(2.0)	(2.0)
	Cash flow from investing activities	(14.7)	(3.5)	(3.5)	(2.0)	(2.0)
	Dividends paid	(5.9)	(0.7)	(11.9)	(15.1)	(20.6)
	Cash flow from financing activities	(3.6)	28.4	(21.5)	(17.4)	(22.4)
	Cash at beginning of period	21.5	27.4	46.7	80.0	102.8
	Net change in cash	1.3	19.3	33.3	22.8	30.4
	Ending balance cash	27.4	46.7	80.0	102.8	133.2
	Balance sheet (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total cash and equivalents	27	47	80	103	133
	Tangible fixed assets	55	56	57	56	56
	Total assets	131	220	258	304	366
	Short-term debt	25	38	31	31	31
	Total long-term debt	38	26	26	26	26
	Total liabilities	85	120	128	138	151
	Total equity	46	101	130	166	215
	Total liabilities & equity	131	220	258	304	366
	Key metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Revenue growth (%)	5.3	39.2	39.1	21.4	24.7
	Recurrent EPS growth (%)	(5.8)	51.1	54.2	27.4	36.1
	Gross margin (%)	23.9	30.1	30.7	31.6	32.5
	Operating EBITDA margin (%)	15.1	15.5	16.1	16.7	17.9
	Net profit margin (%)	8.6	9.4	10.7	11.2	12.3
	Dividend payout ratio (%)	35.5	31.4	29.5	29.5	29.5
	Capex/sales (%)	5.0	1.0	0.9	0.4	0.4
	Interest cover (x)	8.07	10.36	15.38	18.50	24.85

Source: Company data, RHB

Emissions And ESG

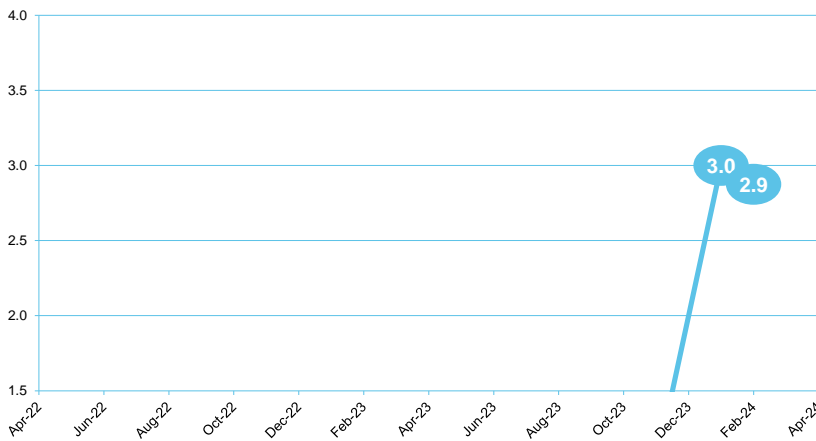
Trend analysis	Emissions (tCO2e)	Dec-21	Dec-22	Dec-23
na	Scope 1	na	na	na
	Scope 2	na	na	na
	Scope 3	na	na	na
	Total emissions	na	na	na

Source: Company data, RHB

Latest ESG-Related Developments

- Synergy uses particle boards, which do not contribute to more deforestation, as the raw material of its home furniture sold. It has also obtained Forest Stewardship Council (FSC) certificates.

ESG Rating History



Source: RHB

Recommendation Chart



Date	Recommendation	Target Price	Price
2024-02-28	Buy	1.08	0.87
2024-01-14	Buy	1.08	0.69
2023-10-02	Buy	0.64	0.44

Source: RHB, Bloomberg

Source: RHB, Bloomberg

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-	-

(2) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

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