STOCKS DOWN UNDER

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ASX Small Caps Stocks Down Under

Rarely do more than three or four variables really count [in investing]. Everything else is noise.

- Martin J. Whitman (1924-2018), Third Avenue Management founder

BWX

Still hopeful about better times

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Stocks Down Under rating: ★★★★

ASX: BWX
Market cap: A$204.3M

52-week range: A$1.25 / A$5.63
Share price: A$1.26

The beauty industry wouldn't have the best reputation with ASX investors given the flop of the Adore Beauty IPO. But it is home to a handful of companies that were in the space long before COVID and BWX is one of them. Yes, it too is below its IPO price, but it has mostly been above water until the recent market crash brought shares down. Given its reasonable multiples and track record of profitability, the current dip could represent a good buying opportunity for investors.

Share price chart

Source: Tradingview

ESG commands a premium…until it doesn't

BWX specialises in natural skincare products as a developer, manufacturer and distributor. It operates more than half a dozen brands, but its most famous is Sukin, which was born in 2007. Products are stocked through ecommerce channels and in stores, including in Woolworths, Coles and Chemist Warehouse in Australia as well as TMall in China, plus Walmart, Target and Whole Foods in North America. BWX's products are marketed as being ethical in that they are made without animal testing.

BWX believes that ethically focused consumers will pay a premium for natural skincare products that don't use animal testing, are eco-conscious and don't contain unnecessary toxins. And industry growth figures affirm – beauty and personal care products generally are only growing at 5% CAGR to 2026, but green beauty products are expected to grow 12% over that same time period.

BWX listed on the ASX in late 2015 raising $39.3m at $1.50 per share. Its early years were successful – growing its revenue tenfold between 2014 and 2018 and nearly reaching $8 per share in early 2018. But it endured a 75%+ tumble across 2018 due to slowing growth, which meant the company missed its guidance, along with a Bain Capital takeover bid falling through. Factors to blame for BWX's performance included slowing sales momentum in China and the US.

The company had (and still has) a heavy focus on China, not just because of its large population, but also because of China's regulations being favourable. Since 2014, China has banned imported goods from using

animal testing while exempting local products, allowing BWX to enter the market, selling in China via cross-border e-commerce. Although things have never been the same in China since 2018, 2019 was a better year for the company as the share price slowly recovered. BWX had been on an M&A binge in previous years but took a break from acquisitions more recently and continued to roll out Sukin. Its results improved, driven mostly by demand in the US and it strengthened its balance sheet through a refinancing. And the company remains hopeful that it could succeed in China with recent regulatory changes enabling the direct import of products without animal testing. It has been exploring these pathways to launch Sukin into China through direct domestic sales.

Multiple cycles

BWX started 2020 well, only to be hit by the pandemic. The company's share price was hit by the Corona Crash, but during the pandemic itself demand for some of its products declined, such as makeup and lipstick, but others rose – most notably its range of hand sanitisers in March 2020 along with its other personal care products. The closure of beauty salons, hairdressers and brick and mortar stores meant consumers had no choice but to shop online. And BWX was the beneficiary.

Overall, its sales rose 25% to $187.7m during FY20, which was driven by increased sales in its Sukin range. Yes, this was hand sanitisers, but arguably more importantly, the brand was launched in Target stores in the US. In FY21, it delivered $194.1m revenue (less than 3% higher year-on-year), but NPAT came in at $23.7m (which was 61% higher than FY20).

The company has completed two capital raisings since the pandemic. First in June 2020 where it raised $50m to build a new manufacturing facility. Second in late August 2021 when it raised $100m to buy just over 50% of Zoe Foster Blake's Go-To-Skincare brand.

Is it time to buy the dip?

The last six months have been tough for the company with the market conditions as well as guidance for its FY22 results due in August. For FY22, the company is expecting $233-$243m revenue, which would be up 20-25%, and $27-$30m EBITDA, which would be down 10-19% from a year before. The company blamed a higher operating cost base (including freight and supply chain costs) and those recent acquisitions were not yet meeting growth expectations.

The company recently hired a new CEO in Rory Gration and conducted a business-wide review of its financial and operating performance. We also think the company has suffered from being in the same industry as Adore Beauty (ASX: ABY), another industry IPO that was overpriced and has been a complete flop for investors. But even with its decline, BWX is only slightly below its IPO price.

Can it bounce back in FY23? Consensus estimates believe so, with $274.9m in revenue and $45.2m EBITDA forecasted. Compared to the midway point of its FY22 estimates, these figures would represent growth of 17% and 60% respectively. And the company is trading at just 6.3x EV/EBITDA and 12.7x P/E. Adore Beauty meanwhile is trading at 15.1x EV/EBITDA and 36.1x P/E for FY23 and consensus estimates forecast just $7.1m EBITDA in FY23 which would represent just 32% growth.

We admit that the market may not be keen on this company until its FY22 results are over and done with. And we are sceptical that BWX can retain its pre-2018 momentum in China as the company's management seemingly hopes. But to be fair, that is the case with almost every China-focused company on the ASX.

Yet even though its FY22 results might appear a step backwards, we think BWX has enough momentum in its other markets to bounce back in FY23. So, it's four stars from us. Notwithstanding this, we think investors should wait to see a clear uptrend before buying in. It appears to have a support level established, but it isn't in an uptrend just yet.

Pitt Street Research Pty Ltd

3 Spring Street, Sydney, NSW 2000, Australia

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