

GNC Holdings Inc

Buy Trade – Position Open

USA | CONSUMER NON-DURABLES | TRADING NOTE

10 February 2017

Investment Action

GNC Holdings Inc (GNC) has had an abysmal year, with shares falling from a 52 week high of US\$35.90, to a low of US\$7.62, about a 78.8% decrease. Share price fell on the back of falling revenues and earnings, as consumers came to view their offerings as too pricey and they faced weaker traffic. Revenue had been flat for the past 3 years and is expected to fall about 3.7% yoy when GNC reports its 2016 results. Its GAAP net income fell 14.3% in 2015 and is expected to fall another 22% in 2016. With the fall in share price, GNC is now trading at a PER of about 3.20, and a dividend yield of 9.45%, which we believe to be very much undervalued.

Following a failed turn around attempt, the previous CEO of GNC stepped down in July 2016. Robert Moran, an independent director, then stepped in as interim CEO. After taking some time to do an honest evaluation of the company, Moran was candid about the company's poor business model and proposed a new business plan, dubbed New GNC. The plan would call for lowering of single product pricing policies, introduction of new products, new loyalty programs, and addition of new technologies like a mobile app to improve and personalize the shopping experience.

We believe that despite the trend of falling revenue and earnings, the tumble in the share price of GNC is overdone and has caused GNC to become attractively valued. GNC is currently still profitable and there were many low hanging fruits for management to take advantage of to turn things around, such as poor inventory management, that caused items to be out of stock. At current pricing, GNC has been priced for failure and the company, while struggling, is not out for the count yet.

Key Points:

- Valuations.** GNC currently trades at a PER of about 4. In comparison, its closest competitor, Vitamin Shoppe Inc (VSI) is trading at a PER of 12.50. Earnings for the quarter will be coming out on 16th February, where we will see if Robert Moran's plan for the new GNC has been able to stem the tide of falling sales and earnings. GNC does hold on to a very large amount of debt, which does worry us. However, the debt is being held at a very low interest rate. The bulk of its debt is due on 2019 and is priced at an interest rate of 3.75%, with a total annual interest expense of about US\$46 mn. GNC's net income in the 9 months of 2016 reported so far has been a total of about US\$147.2 mn and they were able to generate about US\$169.75 mn in operating cash flow. As such, we believe that GNC's debt, while large, is still within the company's ability to manage. GNC also pays a dividend of about US\$0.20 per share per quarter, about **9.45% yield** at current price. This amounts to about US\$ 41.61 mn in cash outlay for the 9 months of 2016 reported and a payout ratio of about 28%. This leads us to believe that GNC's dividend is sufficiently covered and barring any severe impact on earnings, GNC's dividend should be relatively safe from a cut. As of Q3 2016, GNC has an operating margin of about 10.27% and a net profit margin of 5.15%. Overall, we believe GNC is very **Under Valued**. Comparing GNC to its closest competitor, assuming a PER of 12.5, the price for GNC would be about US\$25, based on its current earnings. However, given GNC's struggles at the moment, we believe a more realistic **target price** in the short term would be **US\$14**. However, pending its earnings release, we would also put a **Stop Loss** at the share's 52 week low of **US\$7.62**.

Positive

CLOSING PRICE	USD 8.47
ENTRY PRICE	USD 8.47
STOP LOSS	USD 7.62
TARGET PRICE	USD 14.00
RISK/REWARD	6.5

COMPANY DATA

O/S SHARES (MN):	68
MARKET CAP (USD mn / SGD mn):	579 / 579
52 - WK HVLO (USD):	35.9 / 7.63
3M Average Daily T/O (mn):	2.46

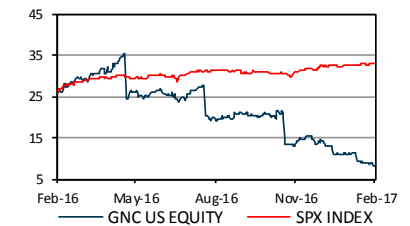
MAJOR SHAREHOLDERS (%)

FMR LLC	14.99%
VANGUARD GROUP	7.88%
BLACKROCK	6.08%

PRICE PERFORMANCE (%)

	1M TH	3 M TH	1Y R
COMPANY	(23.3)	(35.5)	(65.5)
SPX RETURN	186	7.23	27.33

PRICE VS. SPX



Source: Bloomberg, PSR

KEY FINANCIALS

USD BN	FY 13	FY 14	FY 15	FY 16e
Revenue	2.6	2.6	2.6	2.5
EBITDA	0.5	0.5	0.5	0.4
NPAT (adj.)	0.3	0.3	0.2	0.2
EPS (adj.)	2.85	2.83	2.92	2.45
PER, x (adj.)	20.50	16.57	10.6	3.5
P/BV, x	6.74	5.49	5.1	16
DPS (USD)	0.6	0.6	0.7	0.8
Div Yield, %	10%	14%	2.3%	9.4%
ROE, %	31%	33%	36%	35%

Source: Company Data, PSR est.

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- **Risk.** GNC reports its earnings for the recent quarter on February 16. If the results are poorer than expected and show that Robert Moran's new GNC plan is not gaining traction, we expect GNC's price to continue to tumble. Furthermore, GNC will continue to face challenges from consumer trends, such as ecommerce, which continue to result in weaker traffic in their stores. If GNC does not take steps to address this issue, it may continue to face erosion in its sales.
- **Description.** GNC is a specialty retailer of health, wellness and performance products, which include vitamins and herbal supplements, sports nutrition and diet products. The company operates in three segments: Retail, Franchising and Manufacturing/Wholesale.

Counter	Sector	Ticker	Currency	Last Price	Time Horizon	Entry	Stop Loss	Target	Bloomberg Consensus T/P
GNC Holdings Inc	Consumer Non-Durables	GNC	USD	8.47	9-12 Month	8.47	7.62	14	12.06

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