

MDARA: H1 2020 Results Review

Results much stronger than predicted, driven by e-commerce and new products

MADARA Cosmetics ('MADARA' or the 'Company'), a leading Latvian producer of natural beauty products, is listed on Nasdaq Baltic First North and reports a full set of numbers semi-annually. MADARA succeeded to surprise us positively in terms of Q2 2020 revenues and overall profitability for the first half of this year, especially considering the coronavirus pandemic and temporary closures of several stores. When explaining its excellent results for H1 2020, the management refers to three main aspects, including a strong expansion of e-commerce channels, a growing network of resellers in Germany and France, as well as successful launch of some new products. Overall, H1 2020 total sales came in much stronger than anticipated, along with impressive profit figures, backed by improved gross margins and slower growth in selling expenses in comparison with the revenues.

In H1 2020, the Company's net sales amounted to EUR 8.22m (+47.0% y-o-y), nearly EUR 2m higher than our estimates. Compared to H2 2019, sales advanced 38.0%. Contrary to our expectations, considering the coronavirus related movement restrictions and temporary closures of physical stores, MADARA's sales growth sharply accelerated in Q2 2020. Taking into account the preliminary Q1 2020 sales figure of EUR 3.23m (+25% y-o-y), announced in April, MADARA generated sales of nearly EUR 5.0m in Q2 2020 alone, up 66% y-o-y and presenting a new quarterly record. Please note that all four MADARA stores located in shopping centres in Riga were closed on weekends and holidays from 28th March till 12th May, while many specialised cosmetics stores of the Company's retail partners were also closed during the peak of the coronavirus outbreak in April-May. It seems we underestimated the strong shift of MADARA's customers towards e-channels over the recent quarters. The Company was able to ramp up sales on its own e-store platform, while MADARA's resale customers with a strong e-commerce profile also showed solid performance recently. During the past couple of years, MADARA made substantial investments into developments of e-commerce channels, and these investments have started to pay off. Apart from e-commerce, the Company claims it has succeeded to expand the number of resellers (physical stores) in Germany and France during H1 2020, with MADARA products being present in several dozen new outlets recently. In addition to the launch of its new organic make-up product line on 26th September 2019, MADARA introduced several new products in H1 2020, including facial care, self-tanning, herbal active ingredient concentrates, skin disinfectants, and functional hair products. Following the coronavirus outbreak and growing demand for sanitising products, the Company launched a new hand cleaner and disinfection line, ANTI, which also contributed to the overall sales result in H1 2020, accounting for over 3% of the total revenues.

In terms of sales by market in H1 2020, 95% of sales (H1 2019: 94%) came from the EU countries, with Latvia accounting for about 28% of the total sales (H1 2019: 26%). In H1 2020, sales in Latvia grew 56.7% y-o-y to EUR 2.28m, while those in other EU countries

Key Numbers (EURm)	2017	2018	2019	2020E*	2021E*	2022E*
Sales (EURm)	7.4	9.5	11.5	13.5	15.7	18.0
Sales growth (%)	26.3	28.7	21.2	16.7	16.8	14.4
Net profit (EURm)	1.2	1.5	1.6	1.7	2.0	2.4
EPS (EUR)	0.33	0.40	0.42	0.46	0.53	0.63
P/E (x)	22.5	19.6	18.8	20.3	17.6	14.7
Payout per share (EUR)*	0.05	0.09	0.12	0.15	0.18	0.26
Payout yield (%)	0.7	1.1	1.5	1.6	2.0	2.8
P/B (x)	3.9	3.5	3.1	3.3	2.9	2.6
EV/Sales (x)	3.2	2.7	2.3	2.4	2.0	1.8
EV/EBITDA (x)	13.5	13.0	12.0	12.6	10.6	9.1
EV/EBIT (x)	17.7	17.6	17.8	18.7	15.0	12.3
ROE (%)	24.6	19.3	17.4	17.0	17.4	18.7

Source: MDARA, LHV *2020E-2022E multiples are based on the share price (25th Aug 2020) of EUR 9.30 per share. *Payout per share include dividends and share capital reduction.

Company Profile

Listing Market:	First North Baltic Share List
Bloomberg Ticker:	MDARA LR
ISIN:	LV0000101624
Industry:	Consumer Goods
Sector:	Personal & Household Goods
No. of Employees:	142
Website:	www.madaracosmetics.com

Share Data, as of 25th Aug 2020

Current Share Price (EUR):	9.30
Fair Value Range (FVR), EUR:	8.60-9.40
Downside, % (to mid-point of FVR):	3.23
52-week High/Low (EUR):	10.10/6.50
3m Avg. Daily Volume (th):	0.09
Market Cap (EURm):	34.83
Ordinary Shares (m):	3.75

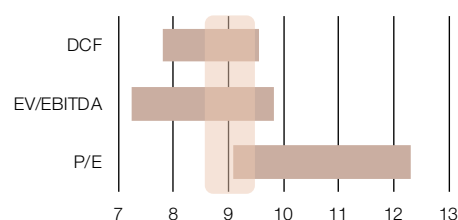
Key Shareholders, as of 30th June 2020

Uldis Iltners	24.08%
Lote Tisenkopfa-Iltnere	23.92%
Oy Transmeri Group AB	23.09%
Zane Tamane	7.61%
Liene Drāzniece	6.83%

12-Month Price Performance



LHV Fair Value Range: EUR 8.60-9.40*



* As of 27th July 2020

MADARA: Results Review, EURm	H1/20A	H1/19A	% y-o-y	H1/20E	Dev, abs	Dev, %
Net sales	8.22	5.59	47.0	6.30	1.92	30.4
Other EU	5.43	3.73	45.5	4.10	1.33	32.3
Latvia	2.28	1.46	56.7	1.72	0.56	32.8
Outside EU	0.40	0.34	19.2	0.40	(0.00)	(0.7)
Other revenues	0.10	0.07	58.8	0.07	0.03	44.3
Gross profit	5.18	3.46	49.8	3.87	1.30	33.6
EBITDA	2.17	1.11	95.4	1.23	0.95	76.9
Operating profit	1.77	0.78	127.6	0.83	0.94	114.2
Net profit	1.81	0.81	123.3	0.84	0.97	116.1
Gross margin, %	63.0	61.8		61.5		
EBITDA margin, %	26.5	19.9		19.5		
Operating margin, %	21.5	13.9		13.1		
Net margin, %	22.0	14.5		13.3		

Source: MADARA, LHV

(excluding Latvia) were up 45.5% y-o-y, reaching EUR 5.43m. Sadly, the Company does not disclose the breakdown of its sales by EU countries, stating only that Finland still holds the position as the largest export market, but the respective sales declined about 2% y-o-y to EUR 1.32m in H1 2020, forming 16% of the total. Given the overall strong sales dynamics, we consider the revenues from Finland as disappointing. Regarding other EU countries, apart from Latvia and Finland, MADARA focuses mostly on expansion in Germany, France, Netherlands, Spain, and the UK. MADARA's sales outside of the EU also improved in H1 2020, rising 19.2% y-o-y to EUR 0.40m. In terms of revenues by type of activity, MADARA-branded products formed 89% of sales in H1 2020 (H1 2019: 86%), while the proportion of MOSSA products remained steady at 10% (H1 2019: 10%), with the proportion of contract manufacturing services declining from 4% in H1 2019 to just 1% in H1 2020. The recently launched new products have affected the breakdown of MADARA's revenues by product groups this year. In H1 2020, the most important product categories remained facial care, anti-ageing cosmetics, and body care, accounting for 52% (H1 2019: 59%), 15% (H1 2019: 11%), and 14% (H1 2019: 18%) of the total, respectively. The proportion of hair products dropped from 10% in H1 2019 to 7% in H1 2020. The recently introduced organic make-up line captured an 11% share of the total sales in H1 2020. Taking into account that the Company launched the new line at the end of September 2019, we consider this as a fairly strong start to the new segment, allowing us to expect further positive developments in the coming years. In its comments on 2019 results, MADARA said it anticipates the new segment to form 7-10% of sales this year, with a gradual increase in the following years.

The strong sales growth and economies of scale enabled MADARA to improve its gross margins in the latest half-year period, rising

1.2pp y-o-y to 63.0%, the highest semi-annual level since H1 2018. The Company continues to make strong efforts to expand its export markets and improve its e-commerce platform, leading to a substantial boost in selling expenses. However, it was positive to note that MADARA's selling expenses grew somewhat slower compared to the sales growth, despite the recent launch of the new product segment and the expanding retail network in Western Europe, rising 37.8% y-o-y to EUR 2.95m. Adding to the positives, in H1 2020, MADARA managed to reduce its administrative expenses by 9.1% y-o-y to EUR 0.58m. Overall, MADARA's gross profit jumped 49.8% y-o-y to EUR 5.18m, c.a. EUR 1.3m more than our estimates. EBITDA increased 95.4% y-o-y to EUR 2.17m, with operating profits rising 2.3x y-o-y to EUR 1.77m and net profits advancing 2.2x y-o-y to EUR 1.81m. The H1 2020 EBITDA and net profit numbers already exceed the respective full-year 2019 figures, also beating our estimates by nearly EUR 1m each. Such dynamics primarily reflects surprisingly strong sales performance during Q2 2020, despite the coronavirus situation. The Company also remains strongly capitalised and highly liquid, supporting its further growth. As at the end of H1 2020, total cash amounted to EUR 5.6m, while total debt remaining below EUR 0.1m.

Overall, the Company's H1 2020 figures are quite impressive, with many encouraging signs about its ability to avoid any setbacks related to the coronavirus pandemic and successfully continue its growth strategy with a strong focus on e-commerce. The management reiterated its 2020 revenue guidance of EUR 15m. Considering the recent developments, we believe the Company should have no serious issues to meet this guidance, and we are likely to upgrade our conservative projections for this year, but no significant adjustments to our fair value range for the stock should be expected at this stage.

Contacts:**Ivars Bergmanis**

Head of Institutional Markets

Tel: +372 680 2720

Mob: +372 534 11114

ivars.bergmanis@lhv.ee

Sander Danil

Senior Analyst

Tel: +372 680 2793

sander.danil@lhv.ee

Date and time of sign-off: Wednesday 26th Aug, 17:00**Disclaimer**

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