

Xtep (1368 HK)

Solid cash position to yield attractive dividend

Cut TP to HK\$ 2.90 but maintain BUY due to attractive dividend yield of 7.5% in FY20E, based on a 10x FY20E P/E (down from 13x due to sector de-rating). We now revised our retail sales growth forecast to a 5% drop in FY20E (-16%/ +5% in 1H20E/ 2H20E), from 15% increase previously.

- **FY19E net profit roughly inline.** FY19 net profit grew by 11% to RMB728mn, 5%/ 3% above CMBI/ BBG's est.. Noted that if we exclude exceptional items (including write back of receivable provisions, inventory provisions, gains from land sales for RMB 53mn and M&A expenses of RMB 100mn), adjusted net profit would go up by 14% YoY.
- **Retail sales is much less negative in early Mar 2020.** Management cited that retail sales growth was robust (20%+ YoY) in first three weeks in Jan, but plummeted since then into Feb (similar to industry, with deepest daily decline was at ~80% YoY) and improved meaningfully in first two weeks in Mar (down by ~40% YoY). They expect retail sales to decline by 25-30% YoY in 1Q20E as a whole. Noted that, e-commerce performed comfortably well with 40%+ growth YTD, because the Company adapted well to the virus outbreak by leveraging various online platforms (such as wechat mini programs, encouraging all employees to promote products online, live streaming promotions by staffs at distributors' stores, etc.).
- **Channel inventory surged and retail discounts widened.** Also cited by management, channel inventory level is now at 5-5.5 months (vs 4-4.5 normally) and retail discounts YTD is 35-45% off (vs 25-30% normally).
- **Policies to support distributors.** To support the distributors, which are suffering from lack of cash flow in 1Q20E, Xtep decided to temporarily lengthen the credit period (from 120 days to 150 days), as well as allowing an one-off SKUs swaps (can delay 20% of 1Q20E SKUs shipment to 3Q20E, and cancel up to equal amount of orders in 3Q20E). Moreover, management estimated that over 80% of their retail stores had certain rental benefits provided by the landlords (both street level and shopping mall stores). All in all, we believe Xtep's distributors will be able to survive this coronavirus crisis.
- **Maintain BUY but cut TP to HK\$ 2.90.** We cut our FY20E/21E EPS estimates by 22.3%/ 15.2%, to factor in 1) reduction and cancellation of trade fair sales, and 2) higher-than-expected finance costs. The counter is trading at 8x FY20E P/E, below its 5 years average of 12x. Our TP is based on 10x FY20E P/E and we maintain BUY due to its high dividend yield of 7.5%.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	6,383	8,183	8,307	9,505	10,514
YoY growth (%)	24.8	28.2	1.5	14.4	10.6
Net income (RMB mn)	657	728	622	815	965
EPS (RMB)	0.295	0.302	0.250	0.327	0.387
YoY growth (%)	60.6	2.3	(17.2)	30.9	18.4
P/E (x)	6.8	6.6	8.0	6.1	5.2
P/B (x)	0.8	0.7	0.7	0.7	0.6
Yield (%)	8.8	8.8	7.5	9.8	11.6
ROE (%)	12.3	11.8	8.8	11.1	12.4
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price	HK\$2.90
(Previous TP	HK\$4.47)
Up/Downside	+25.2%
Current Price	HK\$2.32

China Sportswear Sector

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Stock Data

Mkt Cap (HK\$ mn)	5,829
Avg 3 mths t/o (HK\$ mn)	23.40
52w High/Low (HK\$)	6.74/3.81
Total Issued Shares (mn)	2,512.4

Source: Bloomberg

Shareholding Structure

Mr Ding Shui Po & Family	53.89%
Templeton Investments	2.62%
Employee incentive scheme	4.01%
Free Float	39.48%

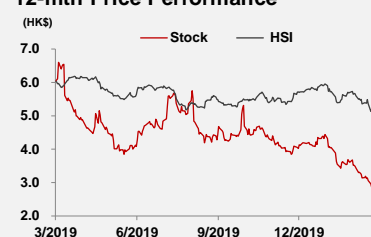
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-34.1%	-18.6%
3-mth	-42.3%	-27.8%
6-mth	-47.7%	-37.3%
12-mth	-60.8%	-48.3%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

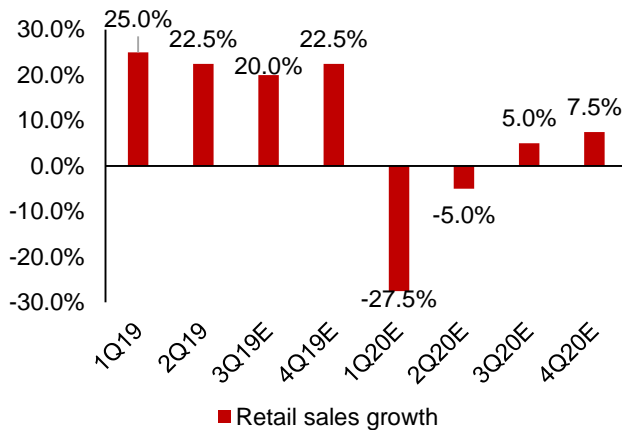
Auditor: Ernst & Young

Related Reports

1. Xtep (1368 HK) – Good 4Q19 but likely a temporary drag in 1Q20 – 5 Feb 2020
2. Xtep (1368 HK) – New brands require both time and investments – 22 Nov 2019
3. Xtep (1368 HK) – For the greater good and a brighter future – 22 Aug 2019

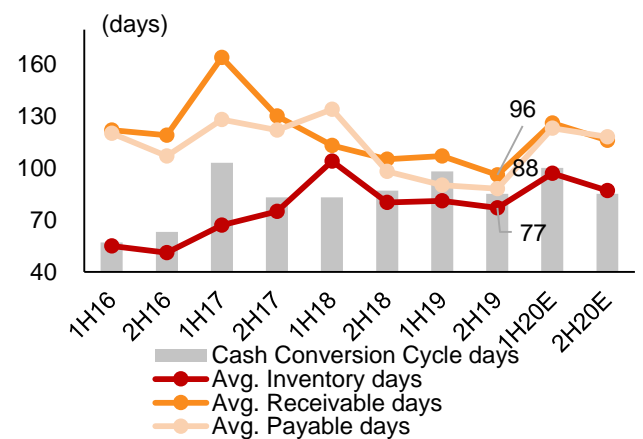
Focus Charts

Figure 1: Xtep's retail sales growth (CMBI est.)



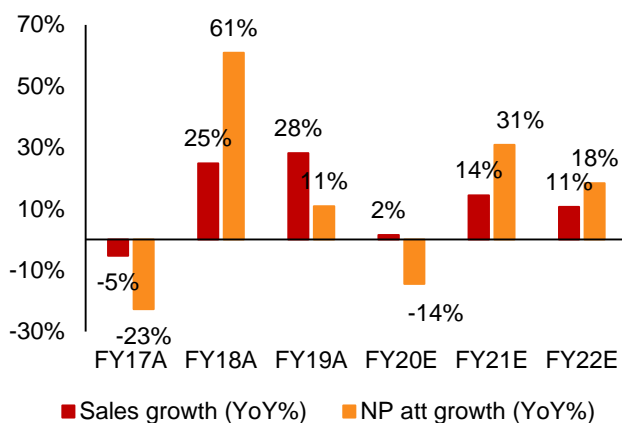
Source: Company data, CMBIS estimates

Figure 2: Xtep's same store sales growth



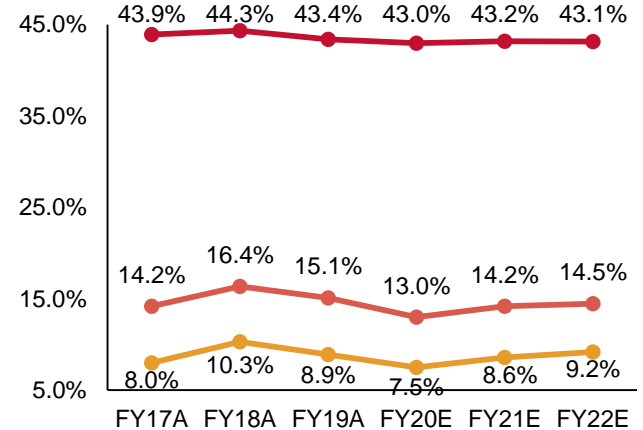
Source: Company data, CMBIS estimates

Figure 3: Sales/ net profit growth



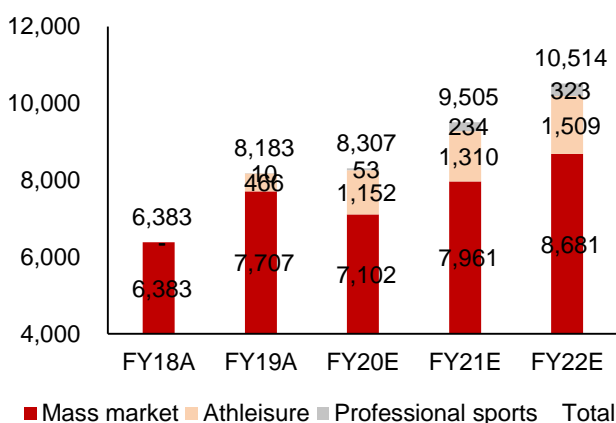
Source: Company data, CMBIS estimates

Figure 4: GP/ OP/ NP margin



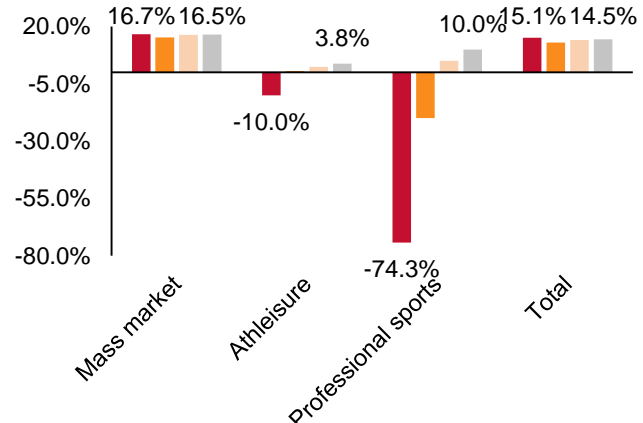
Source: Company data, CMBIS estimates

Figure 5: Sales breakdown, by segment



Source: Company data, CMBIS estimates

Figure 6: OP margin, by segment



Source: Company data, Tmall, CMBIS estimates

Results Summary

Figure 7: Results preview – Half Year

Half yearly (RMB mn)	1H18	2H18	1H19	2H19	1H18 YoY	2H18 YoY	1H19 YoY	2H19 YoY	2H19E CMBI	Actual vs CMBI
Revenue	2,729	3,654	3,357	4,826	18%	30%	23%	32%	4,867	-1%
COGS	(1,536)	(2,019)	(1,860)	(2,773)					(2,744)	
Gross profit	1,193	1,635	1,497	2,053	17%	33%	25%	26%	2,123	-3%
GP margins	43.7%	44.7%	44.6%	42.5%					43.6%	
Other income & gains	143	53	138	170					73	135%
S & D expenses	(480)	(877)	(637)	(1,082)	25%	67%	33%	23%	(1,198)	-10%
S & D exp / sales	-17.6%	-24.0%	-19.0%	-22.4%					-24.6%	
Admin expenses	(264)	(359)	(281)	(625)	7%	-31%	7%	74%	(582)	7%
Admin exp / sales	-9.7%	-9.8%	-8.4%	-13.0%					-12.0%	
Other opex	0	0	0	0					0	
Operating profit (EBIT)	592	452	717	517	24%	84%	21%	14%	415	24%
OP margins	21.7%	12.4%	21.4%	10.7%					8.5%	
Other items	0	0	0	0					0	
Net finance income	(41)	(27)	(36)	(75)					(51)	46%
Net finance income / sales	-1.5%	-0.7%	-1.1%	-1.5%					-1.0%	
Profit after financing costs	551	426	681	442					364	
Associated coms	0	0	0	(2)					0	
Jointly controlled coms	0	0	0	0					0	
Pre-tax profit	551	426	681	440	18%	109%	24%	3%	364	21%
Tax	(175)	(131)	(218)	(172)					(122)	
Tax / sales	-6.4%	-3.6%	-6.5%	-3.6%					-2.5%	
Effective tax rate	-31.8%	-30.8%	-32.0%	-39.0%					-33.4%	
Minority interests	0	13	(0)	4					11	
Net profit att.	375	281	463	265	21%	188%	23%	-6%	232	14%
NP margins	13.7%	7.7%	13.8%	5.5%					4.8%	

Source: Company data, CMBIS estimates

Figure 8: Results preview - Full Year

Full yearly (RMB mn)	FY17	FY18	FY19	FY20E	FY18 YoY	FY19 YoY	FY20E YoY	FY19E CMBI	Actual vs CMBI
Revenue	5,113	6,383	8,183	8,307	25%	28%	2%	8,224	-1%
COGS	(2,869)	(3,555)	(4,632)	(4,739)				(4,604)	
Gross profit	2,244	2,828	3,550	3,568	26%	26%	1%	3,620	-2%
GP margins	43.9%	44.3%	43.4%	43.0%				44.0%	
Other income & gains	158	196	308	200				210	46%
S & D expenses	(911)	(1,357)	(1,718)	(1,789)	49%	27%	4%	(1,835)	-6%
S & D exp / sales	-17.8%	-21.3%	-21.0%	-21.5%				-22.3%	
Admin expenses	(767)	(622)	(906)	(901)	-19%	46%	-1%	(863)	5%
Admin exp / sales	-15.0%	-9.8%	-11.1%	-10.8%				-10.5%	
Other opex	0	0	0	0				0	
Operating profit (EBIT)	725	1,044	1,234	1,079	44%	18%	-13%	1,133	9%
OP margins	14.2%	16.4%	15.1%	13.0%				13.8%	
Other items	0	0	(2)	(18)				0	
Net finance income	(54)	(68)	(111)	(107)				(87)	27%
Net finance income / sales	-1.1%	-1.1%	-1.4%	-1.3%				-1.1%	
Profit after financing costs	671	976	1,121	953				1,045	
Associated coms	0	0	0	0				0	
Jointly controlled coms	0	0	0	0				0	
Pre-tax profit	671	976	1,121	953	46%	15%	-15%	1,045	7%
Tax	(224)	(306)	(390)	(324)				(340)	
Tax / sales	-4.4%	-4.8%	-4.8%	-3.9%				-4.1%	
Effective tax rate	-33.5%	-31.4%	-34.8%	-34.0%				-32.5%	
Minority interests	38	13	4	7				10	
Net profit att.	408	657	728	622	61%	11%	-14%	695	5%
NP margins	8.0%	10.3%	8.9%	7.5%				8.5%	

Source: Company data, CMBIS estimates

Earnings revision

Figure 9: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	8,307	9,505	10,514	9,780	10,923	n/a	-15.1%	-13.0%	n/a
Gross profit	3,568	4,103	4,536	4,264	4,782	n/a	-16.3%	-14.2%	n/a
EBIT	1,079	1,346	1,521	1,277	1,488	n/a	-15.5%	-9.5%	n/a
Reported Net profit	620	798	910	798	942	n/a	-22.3%	-15.2%	n/a
Diluted EPS (RMB)	0.249	0.320	0.365	0.320	0.378	n/a	-22.3%	-15.2%	n/a
Gross margin	43.0%	43.2%	43.1%	43.6%	43.8%	n/a	-0.6ppt	-0.6ppt	n/a
EBIT margin	13.0%	14.2%	14.5%	13.1%	13.6%	n/a	-0.1ppt	0.5ppt	n/a
Net profit att. margin	7.5%	8.4%	8.7%	8.2%	8.6%	n/a	-0.7ppt	-0.2ppt	n/a

Source: Company data, CMBIS estimates

Figure 10: CMBI estimates vs consensus

RMB mn	CMBI			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	8,307	9,505	10,514	9,695	11,043	n/a	-14.3%	-13.9%	n/a
Gross profit	3,568	4,103	4,536	4,220	4,844	n/a	-15.4%	-15.3%	n/a
EBIT	1,079	1,346	1,521	1,318	1,559	n/a	-18.1%	-13.6%	n/a
Net profit att.	620	798	910	878	1,047	n/a	-29.4%	-23.8%	n/a
Diluted EPS (RMB)	0.249	0.320	0.365	0.355	0.433	n/a	-29.9%	-25.9%	n/a
Gross margin	43.0%	43.2%	43.1%	43.5%	43.9%	n/a	-0.6ppt	-0.7ppt	n/a
EBIT margin	13.0%	14.2%	14.5%	13.6%	14.1%	n/a	-0.6ppt	0ppt	n/a
Net profit att. margin	7.5%	8.4%	8.7%	9.1%	9.5%	n/a	-1.6ppt	-1.1ppt	n/a

Source: Company data, CMBIS estimates

Valuation

Figure 11: Peers valuation table

			12m TP	Price	Up/ Down-	Mkt. Cap	Year	P/E (x)		P/B (x)		ROE (%)	3yrs PEG (x)	Yield (%)
Company	Ticker	Rating	(LC)	(LC)	side	(HK\$mn)	End	FY1E	FY2E	FY1E	FY2E	FY1E	FY1E	FY1E
H shares Sportswear														
Xtep Intl*	1368 HK	BUY	2.90	2.32	25.2%	5,829	Dec-18	6.6	8.0	0.8	0.8	12.2	1.9	7.5
Anta Sports	2020 HK	BUY	91.46	47.20	93.8%	127,532	Dec-18	20.9	16.8	5.9	4.8	28.6	0.8	1.8
Li Ning	2331 HK	BUY	24.43	16.36	49.3%	40,156	Dec-18	24.9	22.5	5.0	4.2	20.9	0.6	1.3
361 Degrees	1361 HK	NR	n/a	1.19	n/a	2,460	Dec-19	4.6	4.2	0.3	0.3	5.5	0.4	9.5
Topsports	6110 HK	NR	n/a	7.32	n/a	45,393	Feb-19	15.7	13.4	4.5	3.4	76.8	0.0	3.6
Pou Sheng	3813 HK	NR	n/a	1.42	n/a	7,606	Dec-18	8.4	9.1	0.9	0.8	9.6	0.3	2.1
China DX	3818 HK	NR	n/a	0.65	n/a	3,826	Mar-19	5.7	5.9	0.3	0.3	n/a	0.0	12.7
Avg.								12.4	11.4	2.5	2.1	25.6	0.6	5.5
Med.								8.4	9.1	0.9	0.8	16.5	0.4	3.6
International Sportswear														
Nike Inc	NKE US	NR	n/a	61.79	n/a	747,358	May-19	22.0	18.6	11.7	11.5	50.6	1.5	1.5
Adidas	ADS GY	NR	n/a	166.92	n/a	282,491	Dec-19	18.2	14.8	4.4	3.8	30.0	2.5	2.4
Puma	PUM GY	NR	n/a	42.14	n/a	53,670	Dec-19	20.7	16.7	3.0	2.7	14.7	1.1	1.4
Under Armour	UAA US	NR	n/a	8.34	n/a	27,632	Dec-19	71.3	28.0	1.7	1.6	4.4	2.0	0.0
Lululemon	LULU US	NR	n/a	133.61	n/a	135,213	Feb-19	27.3	23.3	9.2	7.3	37.1	1.2	0.0
Skechers	SKX US	NR	n/a	17.50	n/a	21,327	Dec-19	7.1	6.1	1.0	0.9	15.9	0.7	0.0
Vf Corp	VFC US	NR	n/a	53.72	n/a	164,679	Mar-20	16.5	14.7	4.6	4.3	29.1	1.9	3.5
Columbia	COLM US	NR	n/a	53.17	n/a	27,837	Dec-19	11.4	10.3	1.7	1.4	18.8	7.5	2.0
Wolverine	WWW US	NR	n/a	13.37	n/a	8,508	Dec-19	5.7	5.2	1.2	1.0	14.4	0.3	3.0
Mizuno Corp	8022 JP	NR	n/a	1544.00	n/a	2,953	Mar-19	6.7	6.0	0.4	0.4	6.6	1.2	3.2
Asics Corp	7936 JP	NR	n/a	787.00	n/a	10,751	Dec-19	18.6	13.0	0.9	0.8	4.5	0.9	3.6
Avg.								20.5	14.2	3.6	3.3	20.5	1.9	1.9
Med.								18.2	14.7	1.7	1.6	15.9	1.2	2.0

Source: Bloomberg, CMBIS estimates, * Period FY1 and FY2 for Xtep are referring to FY19 and FY20E as it had just issued its annual result

Assumptions

Figure 12: Xtep's key assumptions

Major assumptions	FY18A	FY19A	FY20E	FY21E	FY22E
Sales by segment (RMB mn)					
Shoes	3,925	4,653	4,653	5,242	5,749
Apparels	2,327	3,344	3,478	4,069	4,558
Accessories	131	185	176	194	207
Total	6,383	8,183	8,307	9,505	10,514
Sales by segment growth (%)					
Shoes	20.5%	18.6%	0.0%	12.7%	9.7%
Apparels	32.2%	43.7%	4.0%	17.0%	12.0%
Accessories	36.6%	41.0%	-5.0%	10.0%	7.0%
Total	24.8%	28.2%	1.5%	14.4%	10.6%
Sales by segment (RMB mn)					
Mass market	6,383	7,707	7,102	7,961	8,681
Athleisure	0	466	1,152	1,310	1,509
Professional sports	0	10	53	234	323
Total	6,383	8,183	8,307	9,505	10,514
Sales by segment growth (YoY)					
Mass market	24.8%	20.7%	-7.8%	12.1%	9.1%
Athleisure	n/a	n/a	147.3%	13.7%	15.2%
Professional sports	n/a	n/a	421.3%	345.4%	37.8%
Total	24.8%	28.2%	1.5%	14.4%	10.6%
Sales network					
Xtep	5,580	5,279	5,279	5,437	5,600
Xtep kids	450	850	850	893	982
Oversea stores	200	250	250	250	300
Total	6,230	6,379	6,379	6,580	6,882
GP margins	44.3%	43.4%	43.0%	43.2%	43.1%
Opex breakdown					
A&P / sales	15.2%	14.4%	14.1%	13.8%	13.4%
Staff costs/ sales	11.6%	11.0%	11.7%	11.2%	11.2%
R&D / sales	2.6%	2.4%	2.6%	2.6%	2.5%
D&A / sales	1.4%	1.7%	1.4%	1.3%	1.3%
Provisions (write backs) / sales	-0.8%	-0.9%	0.2%	0.0%	0.0%
Rental / sales	0.3%	0.1%	0.8%	1.0%	1.2%
Selling & distribution costs / sales	21.3%	21.0%	21.5%	21.3%	21.1%
Admin expenses / sales	9.8%	11.1%	10.8%	10.0%	9.7%
Total	31.0%	32.1%	32.4%	31.3%	30.8%
OP margins	16.4%	15.1%	13.0%	14.2%	14.5%
Effective tax rate	31.4%	34.8%	34.0%	33.0%	32.0%
Net profit att. margins	10.3%	8.9%	7.5%	8.6%	9.2%
Net profit att. growth (%)	60.9%	10.8%	-14.5%	30.9%	18.4%

Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	6,383	8,183	8,307	9,505	10,514
Footwear	3,925	4,653	4,653	5,242	5,749
Apparel	2,327	3,344	3,478	4,069	4,558
Accessories	131	185	176	194	207
Cost of goods sold	(3,555)	(4,632)	(4,739)	(5,403)	(5,977)
Gross profit	2,828	3,550	3,568	4,103	4,536
Other income	196	308	200	215	222
Operating expenses	(1,980)	(2,625)	(2,690)	(2,971)	(3,237)
D & A	(8)	(141)	(267)	(272)	(276)
Staff costs	(738)	(901)	(970)	(1,060)	(1,177)
S & D costs (ex-staff, D&A)	(623)	(823)	(825)	(967)	(1,048)
Admin exp. (ex-staff, D&A)	(611)	(760)	(628)	(672)	(736)
Other operating expenses	-	-	-	-	-
EBIT	1,044	1,234	1,079	1,346	1,521
Finance costs, net	(68)	(111)	(107)	(101)	(97)
JVs & associates	-	(2)	(18)	(16)	10
Exceptional	-	-	-	-	-
Pre-tax profit	976	1,121	953	1,229	1,433
Income tax	(306)	(390)	(324)	(406)	(459)
Less: Minority interests	13	4	7	9	10
Net profit	657	728	622	815	965

Cash flow summary

YE Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
EBIT	1,044	1,234	1,079	1,346	1,521
D & A	60	185	317	330	341
Change in working capital	(513)	36	335	(296)	(247)
Income tax paid	(309)	(334)	(324)	(406)	(459)
Others	(128)	(343)	(106)	(116)	(151)
Net cash from operating	154	778	1,301	860	1,005
Capex & investments	(72)	(97)	(208)	(143)	(158)
Associated companies	(1)	(35)	-	-	-
Interest received	-	-	-	-	-
Others	(208)	(1,913)	-	-	-
Net cash from investing	(281)	(2,045)	(208)	(143)	(158)
Equity raised	(31)	1,187	-	-	-
Net change in bank loans	(10)	386	-	-	-
Dividend paid	(459)	(436)	(397)	(439)	(521)
Others	(11)	(98)	-	-	-
Net cash from financing	(511)	1,039	(397)	(439)	(521)
Net change in cash	(637)	(227)	697	278	326
Beginning cash balance	3,832	3,196	2,970	3,666	3,945
Exchange difference	1	1	-	-	-
Cash at the end of the year	3,196	2,970	3,666	3,944	4,271

Balance sheet

YE Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	1,139	3,057	2,929	2,725	2,551
Fixed asset	641	662	791	844	902
Intangible assets & goodwill	105	1,738	1,499	1,258	1,017
Prepaid lease payments	279	104	104	104	104
Interest in joint ventures	114	197	179	162	172
Other non-current assets	-	356	356	356	356
Current assets	8,060	9,266	9,675	10,596	11,467
Cash and cash equivalents	3,196	2,970	3,666	3,945	4,271
Inventories	836	1,046	1,039	1,184	1,310
Trade and other receivables	2,115	2,910	2,617	2,995	3,313
Prepayments	727	818	830	950	1,051
Other current assets	1,186	1,522	1,522	1,522	1,522
Current liabilities	3,278	3,671	3,719	4,066	4,363
Bank loans	1,483	1,086	1,086	1,086	1,086
Trade payables	879	1,420	1,452	1,656	1,832
Accruals & other payables	861	981	996	1,139	1,260
Tax payables	54	115	115	115	115
Others	1	69	69	69	69
Non-current liabilities	590	1,691	1,691	1,691	1,691
Bank loans	461	1,269	1,269	1,269	1,269
Deferred income	-	-	-	-	-
Deferred tax	107	280	280	280	280
Others	22	142	142	142	142
Minority Interest	-	-	7	15	25
Total net assets	5,331	6,960	7,187	7,548	7,938
Shareholders' equity	5,331	6,960	7,185	7,554	7,974

Key ratios

YE Dec 31	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Footwear	61.5	56.9	56.0	55.2	54.7
Apparel	36.5	40.9	41.9	42.8	43.4
Accessories	2.1	2.3	2.1	2.0	2.0
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross margin	44.3	43.4	43.0	43.2	43.1
Operating margin	16.4	15.1	13.0	14.2	14.5
Pre-tax margin	15.3	13.7	11.5	12.9	13.6
Net margin	10.3	8.9	7.5	8.4	8.7
Effective tax rate	31.4	34.7	33.4	32.6	32.2
Balance sheet ratios					
Current ratio (x)	2.5	2.5	2.6	2.6	2.6
Quick ratio (x)	2.2	2.2	2.3	2.3	2.3
Cash ratio (x)	1.0	0.8	1.0	1.0	1.0
Inventory turnover days	86	82	80	80	80
Trade receivables days	121	130	115	115	115
Trade payables days	90	112	112	112	112
Total debt / total equity ratio (%)	36	34	33	31	30
Net debt / equity ratio (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Returns (%)					
ROE	12.3	10.5	8.7	10.8	12.1
ROA	7.1	5.9	4.9	6.1	6.9
Per share					
EPS (RMB)	0.30	0.30	0.25	0.32	0.37
DPS (RMB)	0.18	0.18	0.15	0.20	0.23
BVPS (RMB)	2.40	2.79	2.88	3.03	3.20

Source: Company data, CMBIS estimates

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