

361 Degrees (1361.HK)

Children`s Clothing and Overseas Business Become Highlights

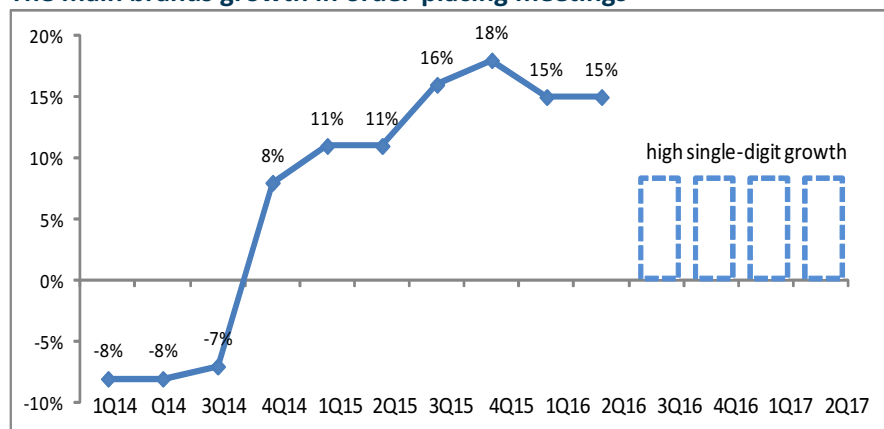
Hong Kong | Sport | Company report

21 December 2016

Sustained Spectacular Results in Order-Placing Meetings

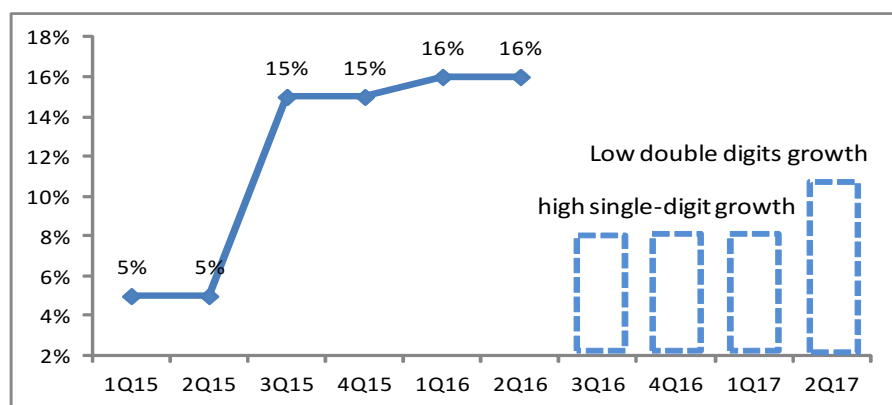
361 Degrees sustained spectacular results in order-placing meetings in autumn and winter of 2016 and spring and summer of 2017. The main brands of 361 Degrees achieved a high single-digit growth in each quarter, while the children`s clothing achieved a high single-digit + low double-digit growth. And the company`s growth rate of orders continued to take the lead among its counterparts listed on the Hong Kong Stock Exchange. Over the same period, ANTA Sports achieved a high single-digit + mid single-digit growth, while Xtep International achieved a high single-digit + low-to-mid single-digit growth. The company is expected to achieve great results in H2 this year and H1 next year, according to the excellent order results.

The main brands growth in order-placing meetings



Source: Company report, Phillip Securities(HK)Research

The children`s clothing growth in order-placing meetings



Source: Company report, Phillip Securities(HK)Research

Buy

CMP: HKD 3.07
(Closing price as at 19 Dec 2016)
TARGET: HKD 3.82 (24.4%)

COMPANY DATA

O/S SHARES (MN) :	2,068
MARKET CAP (HKDMN) :	6,347
52 - WK HI/LO (HKD):	3.24/1.89

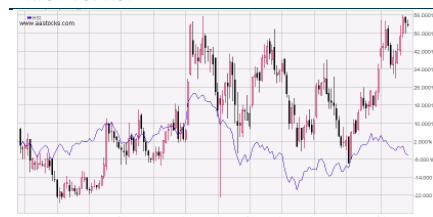
SHARE HOLDING PATTERN • %

Dings international co., LTD	18.27
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PRICE PERFORMANCE • %

	1-Month	3-Month	1-Year
361 Degrees	13.62	30.99	17.67
HSI	14.71	36.63	16.99

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

RMB mn	FY14	FY15	FY16E	FY17E
Revenue	3,906	4,459	5,032	5,641
Net Profit	398	518	569	650
P/E,x	11.2	8.5	10.0	8.7
EPS, RMB	0.19	0.25	0.27	0.31
P/B, x	0.9	0.8	1.0	0.9
BVPS, RMB	2.4	2.55	2.73	2.92
ROE, %	8.0	9.8	10.1	10.7

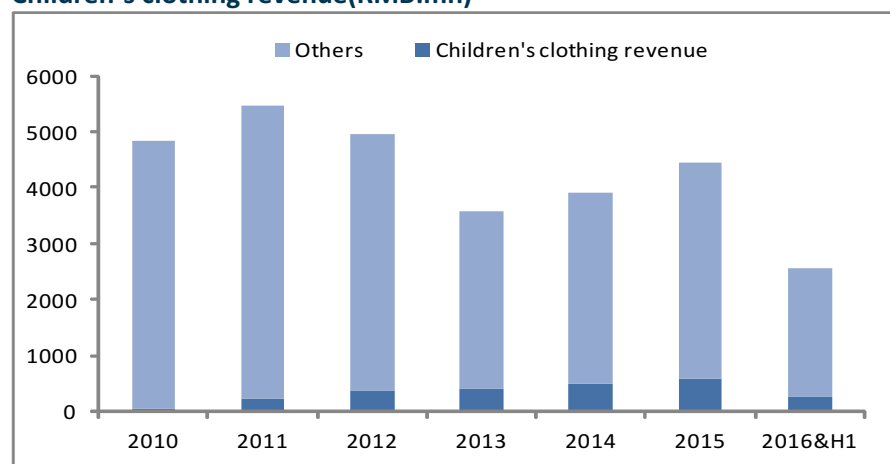
Source: Company reports, Phillip Securities Est.

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Rapid Growth in 361 Degrees Children`s Clothing Business

361 Degrees children`s clothing has experienced a rapid growth since its launch in 2010. In H1 2016, the revenue soared by 16.5% YoY to RMB272 million, and its proportion as a percentage of the total revenue increased to 10.7%. The department`s gross profit margin was partly benefited by the products of high gross profit margin ordered, whose proportion rocketed to 43.1%. Management said the gross profit margin of its department of children`s clothing would remain stable at roughly 41%, and its future revenue contribution would be further increased to 11% to 15%, thanks to the full implementation of the two-child policy and the upgrading of consumer spending.

Children`s clothing revenue(RMB:mn)



Source: Company report, Phillip Securities(HK)Research

361 Degrees Well-Poised for Overseas Business

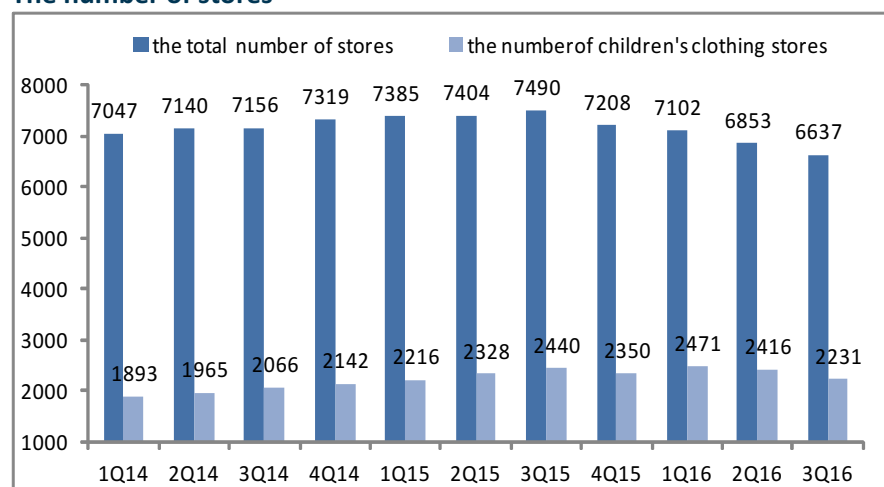
361 Degrees overseas business mainly focuses on high-end, differentiation-based functional products. Not only is product performance comparable to world-renowned brands, but the prices are impressive as well. Many series of products, such as Sensation, STRATA, KgM2 and SPIRE, have won good feedback international for their excellent performance. The company will continue to improve the R&D and features of products. In H1 2016 the revenue from overseas business rocketed by 120% YoY to RMB45.2 million, accounting for 1.7% of the total revenue. Thanks to the successful sponsorship of Rio 2016 Olympic Games and Paralympic Games, a significant increase in brand awareness and the rapid expansion of overseas sales outlets are expected to bring considerable revenue to the company, contributing to 2% of the total revenue of the year and around 4% of the year after and beginning to contribute to the company`s profits.

Stepping Up Efforts to Boost Operation Efficiency and E-Commerce Growth

In terms of offline stores, the company will continue to optimize the number of stores, and improve their operation efficiency. As of Q3 2016, the number of offline stores of 361 Degrees has been reduced to 6,637, of which around 67% locate in third-tier or below cities, and the company will maintain an ideal size of around 6,500. Its number of children`s clothing stores, is 2,231. In Q3 2016, the sales growth rate of main-brand offline stores and children`s clothing stores remained at a high level of 7.3% and 7.3% YoY, respectively, reflecting the strong competitiveness of corresponding products. At present, the average sales volume reached around

RMB1.5 to 2.5 million per store, and it is expected to be increased to RMB2.5-3 million.

The number of stores



Source: Company report, Phillip Securities(HK)Research

The sales growth rate of main-brand offline stores and children's clothing stores

	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16
The main brand	1.8%	2.8%	4.7%	5.5%	6.3%	7.2%	8.1%	7.9%	7.2%	7.0%	7.3%
The children's bra	2.8%	3.1%	5.0%	6.3%	7.0%	8.0%	8.4%	8.2%	7.5%	7.3%	7.3%

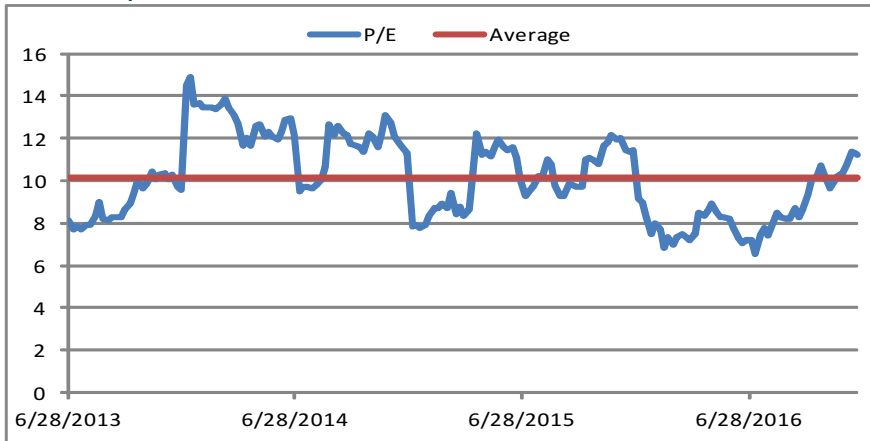
Source: Company report, Phillip Securities(HK)Research

In terms of online e-commerce, the company will increase the proportion of special products and speed up the development of its channels. In H1 2016 the sales volume of online special products reached RMB166 million, accounting for 6.5% of the total revenue. Currently, the online special product only makes up around 50% of the total sales, and the rest comes from offline store inventory. With the decreased inventory in offline stores, the proportion of online special products will soar to roughly 80%, which is expected to boost the revenue contribution from e-commerce to around 10% to 15%.

Valuation and Rating

Benefited from the favorable policies and increased sports consumer demand, the company's industry outlook is relatively optimistic. Considering the company's improved operation efficiency and potential growth in overseas business, and the rapid growth in children's clothing business and e-commerce, we give an estimation of 11x EPS in 2017 and the target price is HKD3.82. Also, the "Buy" rating is maintained. (Closing price as at 19 Dec 2016)

Historical P/E Valuation



Source: Bloomberg, Phillip Securities(HK)Research

Risk Warnings

- Macroeconomic downturn and inventory backlog;
- Market demand release below expectations;
- Results of overseas business expansion below expectations;

Financials

FYE	FY13	FY14	FY15	FY16E	FY17E
Valuation Ratios					
Price Earnings(P/E)	27.5	14.4	11.0	10.0	8.7
Price to Book(P/B)	1.2	1.1	1.1	1.0	0.9
Per share data(RMB)					
EPS,Adjusted	0.10	0.19	0.25	0.27	0.31
Book Value Per Share	2.26	2.40	2.55	2.73	2.92
Dividends Per Share	0.11	0.08	0.10	0.14	0.15
Growth & Margins(%)					
Growth					
Revenue	-27.6%	9.0%	14.2%	12.8%	12.1%
Operating income	-64.9%	124.5%	19.5%	16.7%	11.8%
Net profit	-70.2%	88.6%	30.2%	9.8%	14.3%
Margins					
Gross profit margin	39.5%	40.9%	40.9%	41.4%	41.6%
Operating profit margin	8.2%	16.9%	17.7%	18.3%	18.3%
Net income margin	5.9%	10.2%	11.6%	11.3%	11.5%
Key Ratios					
ROE(%)	4.5%	8.0%	9.8%	10.1%	10.7%
ROA(%)	2.9%	5.1%	6.0%	5.9%	6.2%
Income Statement(RMB mn)					
Revenue	3,583	3,906	4,459	5,032	5,641
- Cost of Goods Sold	2,166	2,309	2,636	2,949	3,294
Gross Income	1,417	1,597	1,823	2,083	2,346
- Operating Expenses	1,154	973	1,090	1,182	1,337
Operating Income	294	660	789	921	1,030
- Net Non-Operating Losses (Gains)	52	(16)	56	(40)	(22)
Pretax Income	315	607	789	861	988
- Income Tax Expense	100	202	260	284	326
Net profit	211	398	518	569	650

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 19 Dec 2016)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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