

# Want Want China (151.HK)

**Pushing innovations but not price deductions as the key to success while facing potential market challenges, entering new overseas market in Vietnam and ASEAN countries**

China | Consumer | Company report

17 December 2018

## Investment Summary

-In the first half of the year, revenue increased by 3.2% y.o.y to RMB 9.25 billion, which is lower than the guidance of the medium to high-single-digit growth given by the management team earlier. In accordance with the old accounting standards, revenue recorded a medium-single-digit growth. Milk drinks and rice crackers businesses performed not as expected. According to the management team, there were negative impacts of product price increase in Q2, as well as the company's shipment adjustment for rice crackers. In the 1H, the contribution of new products was less than expected, accounting for only 3% of total revenue. Earlier, the guidance was higher than low-single-digit growth of previous years.

According to management, the business performance in Q3 (July-September) was similar to that in Q2, maintaining a single-digit growth. The profit margin improved compared to Q2, mainly due to the improvement in product mix that was not fully reflected in Q2.

We expect top line growth in 2H of the year to be higher than 1H. As near the Lunar new year, rice crackers business is entering peak season, the management team is doing lots of preparation works. The milk beverage is expected to be better than the first half of the year, driven by new products and base factors. The company plans to focus on the promotions of New Year products including gift packs, "Lonely God" series and jellies to start off the busy peak season.

- In 1H, benefiting from the launch of high-margin new products, as well as the price decrease in sugar, palm oil and rice in raw materials, the gross profit margin increased by 1.1 ppt to 44.5%. We expect the sugar and carton to be flat in 2H compared with 1H, and the overall raw material pressure will be flat or down. The GPM for 2H and the full year is expected to be better than 1H.

In 1H, distribution costs increased by 12% y.o.y., and as a percentage of revenue increased by 1.3ppt to 15.6% as compared to that of the same period in the previous year. It was mainly due to an increase of advertising and promotion expenses as a percentage of revenue by 0.7ppt to 3.7%, as a result of the company's increased investment in promotion resources for new products and channels.

Want Want has invested in 3,000 vending machines this year, inside schools, office buildings and ect. in 34 cities. It is expected to increase to 10,000 to 20,000 vending machines in the next two years. If each machine's sales can reach RMB2,000 per month, the payback period is only about 9 months. The company will also extend its establishment in overseas market. The Vietnamese plant is expected to be put into operation in February to March in 2021. We expect this year's profit to resume growth, ending the declining trend in profits for four consecutive years since 2014. We give forecast P/E ratio 21.5 times, the corresponding target price HKD6.47. (current price as of December 13, 2018)

## Neutral

CMP HKD5.68

(Closing price at 13 December 2018)

TARGET HKD6.47 (+13.84%)

### COMPANY DATA

O/S SHARES (MN) :	12,449
MARKET CAP (HKDBN) :	70712
52 - WK HI/LO (HKD):	5.31/8.01

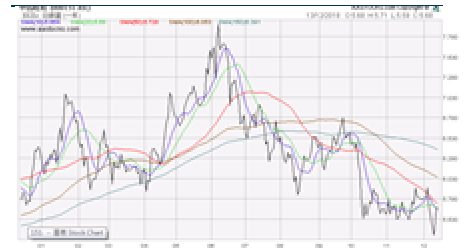
### SHARE HOLDING PATTERN , %

Director Tsai Eng Meng	50.59
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### PRICE PERFORMANCE , %

	1 個月	3 個月	1 年
Want Want	0	-13.15	-4.38
HSI	2.84	-1.81	-13.08

### RETURN VS. HSI



Source: Aastocks, Phillip Securities

### KEY FINANCIALS

RMB mn	FY16	FY17	FY18E	FY19E
<b>Net Sales</b>	19,017	20,275	21,288	22,246
<b>Net Profit</b>	3,337	3,116	3,293	3,506
<b>EPS, RMB</b>	0.26	0.25	0.26	0.28
<b>PER, x</b>	18.49	19.57	18.45	17.33
<b>BVPS, RMB</b>	0.97	1.17	1.28	1.39
<b>P/BV, x</b>	5.01	4.17	3.82	3.51
<b>ROE, %</b>	27.06%	21.29%	20.64%	20.20%

Source: Company, Phillip Securities Est.

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## Business Overview

### First half of the performance review

Revenue of rice crackers business declined by 0.7% y.o.y., mainly due to the sales order shipment adjustment in regions outside China which had a temporary negative impact on rice crackers export sales and the company's strategic decision to limit the low-margin sub-brand rice crackers sales from profitability consideration. However, it still achieved a single-digit growth in mainland China region. In terms of traditional channels and emerging e-commerce channels, it recorded growth too.

Revenue of dairy products and beverage increased by 2.8% y.o.y.. Revenue of "Hot-Kid milk", which accounted for over 90% of the segment's revenue, increased by 3.3% y.o.y. while sales through all channels, including traditional channels as well as the emerging channels, also achieved growth. The company actively cooperated with major e-commerce platforms and explored emerging retail methods. Revenue of dairy and beverages through e-commerce channels continued to maintain a doubling growth momentum. Through constantly investing resources in modern channels, and the success of differentiated strategy, led to a mid-single-digit growth. Sales through traditional channels made steady progress, particularly in second-and third-tier cities.

Revenue of snack foods business increased 7.2% y.o.y. Sales of candies, its key products, achieved a double-digit growth, sales of beans, nuts and others (mainly jellies and biscuits) achieved a high-single-digit growth and sales of popsicles also enjoyed a high single-digit growth. The company launched a new popsicle product "Dongchi" during the period. It achieved revenue of over RMB100 million. "QQ gummy" achieved double-digit growth in all channels.

### Expand emerging channels and digital marketing

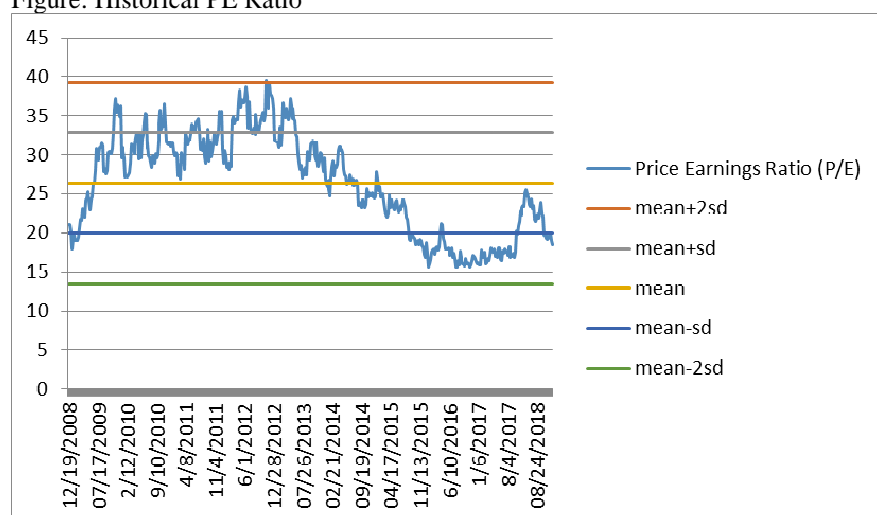
In 1H, revenue from traditional channel recorded a single-digit growth, while e-commerce channels maintained a doubling of growth, accounting for about 5% of total revenue. The development of maternity and other emerging channels was also in swift progress.

Want Want was named as one of the top three food and beverage brands by well-known short video social media called "Douyin". The company has carried out marketing activities towards brand rejuvenation and marketing customization in diversified forms to get closer to the young generation. After creating an online topic of "Want Want's New Products Release" on April Fools' Day, releasing serial products online including skincare products and apparels which aroused heated discussion on the internet. The jock materialized on 11th November. The products were promptly sold out after the launch.

## Investment Thesis & Valuation

We expect this year's profit to resume growth, ending the declining trend in profits for four consecutive years since 2014. We give forecast P/E ratio 21.5 times, the corresponding target price HKD6.47. Potential investment risks include revenue growth or channel expansion missing expectation, raw material cost with huge volatility. (current price as of December 13, 2018)

Figure: Historical PE Ratio



Source: Bloomberg, Phillip Securities

Figure: Peers Comparison

Company	Market Value(HKD,mm)	PE Ratio
Want Want China	70836	19.45
Mengniu Dairy	97602	34.35
Tingyi	58650	18.81
WH Group	92309	11.13
Dali Foods	78604	19.22
U-Presid China	29371	25.24
H&H	32846	31.40
Vitasoy	33427	47.18
Yihai	22090	68.97

Source: Bloomberg, Phillip Securities

## Financials

FYE	2016	2017	2018E	2019E	2020E
<b>Valuation Ratios</b>					
Price to Earnings (P/E)	18.49	19.57	18.45	17.33	16.35
Price to Book (P/B)	5.01	4.17	3.82	3.51	3.23
<b>Per Share Data (RMB)</b>					
EPS	0.26	0.25	0.26	0.28	0.30
Book Value Per Share	0.97	1.17	1.28	1.39	1.51
Dividend Per Share	0.12	0.20	0.16	0.17	0.18
<b>Growth (%)</b>					
Revenue	NA	6.61%	5.00%	4.50%	4.00%
Operating Income	NA	-7.38%	5.67%	6.45%	5.98%
Net Profit	NA	-6.62%	5.68%	6.46%	5.99%
<b>Margins (%)</b>					
Gross Profit Margin	47.19%	43.08%	45.08%	45.58%	46.08%
Operating Profit Margin	23.80%	20.68%	20.81%	21.20%	21.60%
Net Profit Margin	17.53%	15.34%	15.44%	15.73%	16.03%
<b>Key Ratios</b>					
ROE (%)	27.06%	21.29%	20.64%	20.20%	19.72%
ROA (%)	12.25%	11.66%	11.30%	11.06%	10.80%
<b>Income Statement (RMB,M)</b>					
<b>Revenue</b>	19,017	20,275	21,288	22,246	23,136
-Cost of Goods Sold	-10,044	-11,539	-11,692	-12,107	-12,475
<b>Gross Income</b>	8,973	8,735	9,597	10,140	10,661
-SG&A expenses	-5,016	-5,245	-5,720	-5,978	-6,217
<b>Operating Income</b>	4,526	4,192	4,430	4,716	4,998
<b>Pretax Income</b>	4,608	4,293	4,537	4,830	5,120
- Minority Interest	-3	-5	-6	-6	-6
<b>Net Profit</b>	3,334	3,110	3,287	3,499	3,709

Source: Company, Phillip Securities (HK) Research Estimates

Exchange rate (0.8810) is one year HKD/CNY forward contract price on 13<sup>th</sup> December from Wind

(Financial figures as at 13<sup>th</sup> December 2018)

**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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