

# Xtep Int'l (1368 HK)

## Positive growth in Q3 retail sale-through, forecast updated Hong Kong | Consumer (Sportswear) | Update Report

11 November 2020

### Investment Summary

Xtep International's main brands recorded a MDS increase in retail sell-through in the Q3, and the discount level was flat QoQ, higher than normal. Inventory levels have improved on a quarterly basis, and retail inventory turnover has been shortened to approximately 5 months. Based on the operating data for the Q3, we adjusted our valuation model and lowered FY20E/FY21E earnings per share to RMB 19.11/29.74 cents respectively. Considering the development of other brands of the company and the development of national policies, the company raised its 12-month target price to \$3.68.

### The main brand recorded positive growth and outperformed its peers

Xtep announced the Q3 operating data of the Xtep main brand on October 16. The retail sales-through growth of the main brand recorded a MSD growth compared with the same period last year, which is in line with our expectations. Sales performance continued to improve QoQ. In 1Q20/2Q20, Xtep's main brand grew by a negative 20%-25%/negative LSD compared YoY, returning to a positive growth track. The performance in the Q3 is better than its peers. In terms of monthly breakdown of the third quarter, the sales of the main brand in July and August were basically flat/LSD growth compared YoY. Sales recorded a significant improvement in September, estimated to be about LDD growth. In terms of channels, both online and offline recorded positive growth, while online sales growth is better than offline.

Inventory levels continue to improve quarterly. The retail inventory turnover period in 3Q20 is about 5 months, which is an improvement from 5 to 5.5 months in 2Q20. The current company's main goal is still to reduce inventory levels. Regarding the discount level, the retail discount level of the main brand remained flat quarterly, maintaining at a rate of 30% to 35%, which is higher than the normal level of 20% to 25%. It is expected to return to normal levels in 1Q21. In Q1 this year, the company proposed to exchange Q1 products with Q3 products to ease the inventory pressure of the retailers. It is expected that the company will cooperate with online sales promotion activities such as "Double 11" in November for promotion.

### Other brands' overseas business affected

Affected by the epidemic, the company also lowered the full-year sales target of K-Swiss and Palladium from approximately RMB 900 million to approximately RMB 800 million, mainly due to the severe epidemic in Europe and the United States, and the brand's overseas business was more affected than expected. The brand is expected to postpone until next year and begin to record profits. Saucony and Merrell are expected to record 50 million in revenue for the year. The goal of opening stores throughout the year remains unchanged, 30-50 Saucony and Merrell; 30-50 Palladium.

### Valuation model update

The retail sales of the company's main brand in the third quarter were in line with our expectations, but the discount level has not improved. Therefore, we lower the full-year revenue expectation of Xtep's main brand from the original expectation and adjust to minus 5% from the same period last year. In terms of GPM, the GPM of the main brand has also been reduced from the original 40% by 1 pct to 39%. The main reasons include 1) the discount level is still high and 2) the proportion of online sales of the main brand has increased, and the fixed rate of online sales is higher than offline Low 3) The proportion of children's clothing sales increased, and the GPM of children's clothing was lower.  
(Closing price as at 9 November)

### Accumulate (downgrade)

CMP HKD 3.11

(Closing price as at 9 November)

TARGET HKD 3.43 (+10.3%)

### COMPANY DATA

O/S SHARES (MN) :	2,534.01
MARKET CAP (HKD MN) :	7,881
52 - WK HI/LO (HKD):	4.44/1.90

### SHARE HOLDING PATTERN, %

Ding Shui Po	54.30
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### PRICE VS. HSI



Source: Wind, Phillip Securities (HK) Research

### KEY FINANCIALS

CNY mn	FY18	FY19	FY20E	FY21E
Net Sales	6,383	8,183	8,241	9,427
Net Profit	657	728	452	704
EPS, CNY cent	30.19	30.72	17.86	27.79
P/E, x	9.27	9.11	15.67	10.07
BVPS, CNY	239.68	237.68	272.58	290.95
P/BV, x	0.85	0.99	0.97	1.04
DPS (HKD Cent)	20.0	20.0	11.90	18.53
Div. Yield (%)	6.43%	6.43%	3.83%	5.96%

Source: Company reports, Phillip Securities Est.

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## Valuation and Investment Recommendation

The impact of the epidemic on the company continues, but the sales and inventory levels of the main brands continue to improve quarterly, and perform better than other peers. Due to the impact of overseas business, other brands are expected to reduce revenue and record losses throughout the year. The goal of opening stores throughout the year is maintained. The four new brands have a large potential for growth in the Greater China region. In the future, the company will develop the brands in the form of direct operation, which is expected to increase the company's current GPM. Considering that the company's new brands currently have lower GPM, directly operated model can effectively increase the GPM of the new brand to 50-60%, with huge potential for future growth. It is estimated that the company's EPS for FY20E/FY21E is RMB 17.86/27.79 cents, giving the company a target price of \$3.43, which corresponds to a FY20E/FY21E market earnings ratio of 17.09x/11.00x.

(Closing price as of November 9th)

## Peer Comparison

Company	Ticker	CMP	Mkt Cap.	P/E				P/B			
				TTM	2019	2020	2021	TTM	2019	2020	2021
('mn HKD)											
ANTA SPORTS	2020 hk equity	100.80	272,496	51.1x	41.9x	44.1x	29.5x	10.8x	11.7x	9.8x	7.9x
SHENZHOU INTL	2313 hk equity	140.50	211,203	34.6x	34.6x	34.1x	28.5x	6.8x	7.2x	6.4x	5.7x
LI NING	2331 hk equity	45.45	113,113	67.7x	64.7x	59.7x	43.7x	12.5x	13.1x	11.3x	9.4x
TOPSPORTS	6110 hk equity	11.28	69,950	23.5x	-	23.0x	24.3x	5.6x	-	5.9x	5.6x
YUE YUEN IND	551 hk equity	14.04	22,635	-	9.4x	-	11.8x	0.8x	0.7x	0.7x	0.7x
POU SHENG INT'L	3813 hk equity	1.83	9,803	19.6x	10.2x	21.0x	7.9x	1.1x	1.1x	1.0x	0.9x
XTEP INT'L	1368 hk equity	3.11	7,881	12.6x	8.9x	13.1x	9.4x	1.0x	1.0x	0.9x	0.9x
CHINA DONGXIANG	3818 hk equity	0.90	5,298	12.2x	-	7.0x	10.2x	0.4x	-	-	0.4x
361 DEGREES	1361 hk equity	0.93	1,923	4.5x	3.7x	4.1x	3.7x	0.2x	0.3x	0.3x	0.2x
			Mean	28.2x	24.8x	25.8x	18.8x	4.4x	5.0x	4.5x	3.5x
			Median	21.5x	10.2x	22.0x	11.8x	1.1x	1.1x	3.5x	0.9x

Source : Bloomberg, Phillip Securities Research

FYE DEC	FY18	FY19	FY20E	FY21E	FY22E
<b>Valuation Ratio</b>					
P/E ratio	9.27	9.11	15.67	10.07	7.52
P/B ratio	0.85	0.99	0.97	1.04	1.13
Dividend Yield (%)	6.43%	6.43%	3.83%	5.96%	7.97%
<b>Per share data (RMB)</b>					
EPS (cent)	30.19	30.72	17.86	27.79	37.20
BVPS (cent)	237.63	277.03	272.58	290.95	316.12
DPS (HKD cent)	20.00	20.00	11.90	18.53	24.80
<b>Growth &amp; Margin</b>					
<b>Growth</b>					
Revenue	24.8%	28.2%	0.7%	14.4%	27.2%
Operating income	44.1%	18.2%	-32.0%	47.9%	35.4%
Net income	60.9%	10.8%	-37.8%	55.7%	33.8%
<b>Margins</b>					
Gross Profit Margin	44.3%	43.4%	39.1%	41.4%	42.6%
Operating profit Margin	16.4%	15.1%	10.2%	13.2%	14.0%
Net Profit Margin	10.3%	8.9%	5.5%	7.5%	7.9%
<b>Key Ratios</b>					
ROE	12%	10%	7%	10%	12%
ROA	7%	6%	4%	5%	7%

(Closing price as of November 9th)

Source : PSHK

## Financials

### Income Statement (CNY\$ mn)

	FY18A	FY19A	FY20E	FY21E	FY22E
Mass Market	6,383	7,707	7,398	8,138	9,359
Athleisure	-	466	792	1,188	2,376
Professional Sports	-	10	51	101	253
Revenue	6,383	8,183	8,241	9,427	11,988
Growth (%) YoY	25%	28%	1%	14%	27%
COGS	(3,555)	(4,632)	(5,019)	(5,527)	(6,883)
Gross Profit	2,828	3,550	3,222	3,900	5,105
Gross margin (%)	44%	43%	39%	41%	43%
other income	196	308	254	151	149
Selling & distribution	(1,357)	(1,718)	(1,731)	(1,885)	(2,398)
Admin	(622)	(906)	(907)	(924)	(1,175)
-	-	-	-	-	-
Total opex	(1,980)	(2,625)	(2,637)	(2,809)	(3,572)
Operating income (EBIT)	1,044	1,234	840	1,242	1,681
Operating Margin(%)	16%	15%	10%	13%	14%
Finance income	72	29	48	50	51
Finance costs	(128)	(130)	(184)	(184)	(184)
Pre-tax profit	976	1,121	704	1,108	1,549
Tax	(306)	(390)	(232)	(366)	(511)
Minority interest	(0)	(0)	(0)	(0)	(0)
Net profit	657	728	452	704	943
Net margin(%)	10.3%	8.9%	5.5%	7.5%	7.9%
EPS (CNY\$ cent)	30.19	30.72	17.86	27.79	37.20

### Cash Flow Statement (CNY\$ mn)

	FY18A	FY19A	FY20E	FY21E	FY22E
Operating cash flow					
EBITDA	1,136	1,370	1,092	1,470	1,894
Chg in working cap	(568)	(64)	416	(311)	(664)
Others	(105)	(194)	(136)	(134)	(133)
Cash from operating	463	1,112	1,372	1,025	1,097
Tax	(309)	(334)	(116)	(232)	(366)
<b>Net Cash from operation</b>	154	778	1,256	793	732
Capex	(154)	(100)	(99)	(105)	(108)
Acquisition	-	(1,691)	-	-	-
Placement of structured bank depo	(85)	(3,415)	-	-	-
Others	735	202	150	117	133
Cash from investing	(281)	(2,045)	(99)	(105)	(108)
FCF	(127)	(1,267)	1,157	688	624
Financing cash flow					
Issue of Shares	0	30	-	-	-
Dividends paid	(0)	(436)	(525)	(277)	(400)
Others	(570)	265	(1,532)	(1,717)	(2,064)
Cash from financing	(511)	1,039	(572)	(324)	(447)
<b>Net increase (decrease) in cash</b>	<b>(637)</b>	<b>(227)</b>	<b>586</b>	<b>364</b>	<b>177</b>
Exchange rate or other adj	1	1	-	-	-
Opening cash balance	3,832	3,196	2,970	3,555	3,920
<b>Closing cash balance</b>	<b>3,196</b>	<b>2,970</b>	<b>3,555</b>	<b>3,920</b>	<b>4,097</b>
<b>CFPS (CNY\$)</b>	<b>0.18</b>	<b>0.44</b>	<b>0.54</b>	<b>0.36</b>	<b>0.38</b>

**Balance Sheet (CNY\$ mn)**

	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Non-current assets</b>					
Property & Equipment	641	662	675	692	710
LT investment and Receivables	37	73	73	73	73
Other Long Term Asset	461	2,322	2,206	2,115	2,041
<b>Total non-current assets</b>	<b>1,139</b>	<b>3,057</b>	<b>2,953</b>	<b>2,880</b>	<b>2,825</b>
<b>Current assets</b>					
Restricted Bank deposits	1,953	2,596	2,258	2,583	3,284
Trade Receivable	1,953	2,596	2,258	2,583	3,284
Inventory	836	1,046	1,100	1,212	1,509
Cash	3,196	2,970	3,555	3,920	4,097
Other Short Term Asset	1,913	2,340	2,340	2,340	2,340
<b>Total current asset</b>	<b>8,060</b>	<b>9,266</b>	<b>9,253</b>	<b>10,054</b>	<b>11,230</b>
<b>Total Assets</b>	<b>9,199</b>	<b>12,323</b>	<b>12,207</b>	<b>12,934</b>	<b>14,055</b>
<b>Liabilities</b>					
<b>Current Liabilities</b>					
Trade Payable	879	1,420	1,237	1,363	1,697
Bill Payable	861	981	981	981	981
Bank and other borrowing	1,483	1,086	1,086	1,086	1,086
Tax payable	55	116	232	366	511
Leasing liabilities	-	69	69	69	69
	3,278	3,671	3,605	3,864	4,344
<b>Non-current Liabilities</b>					
Debt	483	1,304	1,304	1,304	1,304
Deferred tax liabilities	107	280	280	280	280
Operating lease	-	107	110	113	116
	590	1,691	1,694	1,697	1,700
<b>Total Liabilities</b>	<b>3,868</b>	<b>5,362</b>	<b>5,300</b>	<b>5,562</b>	<b>6,044</b>
<b>Shareholder's Equity</b>					
Equity Capital	20	22	22	22	22
Reserve	5,306	6,868	6,796	7,224	7,767
Non-controlling interest	5	70	89	127	222
<b>Shareholder's Equity</b>	<b>5,331</b>	<b>6,960</b>	<b>6,907</b>	<b>7,373</b>	<b>8,010</b>
<b>Total Liabilities &amp; Shareholder's Eq</b>	<b>9,199</b>	<b>12,323</b>	<b>12,207</b>	<b>12,934</b>	<b>14,055</b>

source : PSHK

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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 ± 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

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