

# Topsports INTL. (6110 HK)

## Profit in FY21 was in line with expectations, gradually recovered after the Xinjiang cotton incident

Hong Kong | Consumer (Sportswear) | Update Report

16 JUN 2021

### Investment summary

#### Profits in FY21 are in line with expectations, and costs are under controlled

Topsports INT'L announced on May 24 the company's annual results for the year ended February 28, 2021. The company's annual revenue was approximately CNY 36.01 billion, an increase of 6.9% Yoy (2020: CNY 33.69 billion), which was slightly lower than our previous expectation (previous expectation: CNY 37.37 billion), it was approximately 3.6% lower. The company's cost control during the period was adequate, and its OPM improved by 1.3 pcts Yoy, offsetting the slower revenue growth. The adjusted net profit for the year was CNY 2.77 billion, an increase of 16.4%, which was in line with our expectations (previously expected: CNY: 27.67) Billion). The company proposes to distribute 12 cents per share for the final period. Together with the interim dividend, the dividend payout ratio is approximately 54% (excluding special dividends). The annual dividend (including one special dividend) totals 64 cents per share.

#### Revenue recorded SD growth, strategically increasing the proportion of wholesale business

Topsports' annual revenue was 36.01 billion yuan, an increase of 6.9% Yoy. The company's revenue growth in 1H and 2H was -7% and +21%, respectively. Compared with the 2H19, revenue in 2H21 also increased with DD growth. In terms of business segment, the company's retail business revenue was CNY 30.73 billion, an increase of 5.4%, the wholesale business was CNY 4.95 billion, a Yoy increase of 17.3%, and joint operating expenses were CNY 240 million, a Yoy decrease of 9.8%. E-sports revenue was CNY 80 million yuan, an increase of 168.1%. During the period, the company's retail/wholesale/concessionaire fee income/e-sports revenue accounted for 85.3%/13.8%/0.7%/0.2%, and the wholesale business accounted for an increase of 1.3pcts, mainly due to the company's strategic increase in the proportion of approved business during the year. If divided by brand, the company's main source of revenue is the main brand, with revenue reaching CNY 31.42 billion, an increase of 6.6%, accounting for 87.3% of the revenue; while the revenue of other brands was CNY 4.27 billion, an increase of 9.3%.

In terms of profitability, the company's GPM decreased by about 1.3 pcts to 40.8% compared with last year, slightly lower than expected (previously expected: 41.6%), mainly due to the company's increased sales discounts to customers during the epidemic. The annual gross profit was CNY 146.8million. The company's cost control during the period was adequate, and the sales and distribution expense ratio and the administrative expense ratio were 26.8% and 3.5%, respectively, which improved compared to the same period last year (the same period last year: 28.6% and 4.2%). The decrease in sales and distribution expense ratio was mainly due to the decrease in staff costs and leasing costs as a percentage of revenue. In 1H21, due to the epidemic, the company received a certain amount of rent reduction and exemption. In 2H21, it has gradually returned to normal (1H/2H ratio changed Yoy: -1.8 ppts/+0.2 ppts). In terms of administrative expenses, it was mainly due to the one-off listing expenses (CNY 52 million) that were included in the same period last year, and no listing expenses were recorded this year.

### BUY (Upgrade)

CMP HKD 12.02

(Closing price as at 11 June)

TARGET HKD 15.34 (+27.62%)

#### COMPANY DATA

O/S SHARES (MN) :	6,201.22
MARKET CAP (HKD MN) :	75,035
52 - WK HI/LO (HKD):	13.78/8.32

#### SHARE HOLDING PATTERN, %

Belle Sports Limited	82.91
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#### PRICE VS. HSI



Source: Wind, Phillip Securities (HK) Research

#### Key Financial

CNY mn	FY20	FY21	FY22E	FY23E
Net Sales	33,690	36,009	41,040	45,429
Net Profit	2,303	2,770	3,235	3,528
EPS, CNY cent	40.88	44.67	52.17	56.89
P/E, x	24.99	22.87	19.58	17.96
BVPS, CNY	170.02	156.51	184.85	214.71
P/BV, x	6.01	6.53	5.53	4.76
DPS (HKD cent)	24.05	26.28	30.69	33.47
Div. Yield (%)	2.00	2.19	2.55	2.78

Source: Company reports, Phillip Securities Est.

#### Research Analyst

**Timothy Chong (+ 852 22776515)**

timothychong@phillip.com.hk

### **Stores continue to be optimized, and the proportion of large stores continues to increase**

The company focuses on its own strategy and continues to prioritize and optimize stores. In terms of the number of stores, the company's direct-operated physical stores for the year decreased by 389 Yoy, with net closures of -239/-150 stores in the first and second half of the year, but the gross sales floor area increased by 4.1%. In terms of the size of stores, the proportion of large stores above 300 square meters continued to increase. As of February 28, 2021, the number of large stores above 300 square meters was 750, an increase of 138 Yoy, and the proportion increased by 2.1 ppts to 9.4%. The number of large stores opened in 1H21/2H21 was 37 and 101 respectively; the proportion of stores from 150 square meters to 300 square meters continued to increase; most of the closed stores were small stores below 150 square meters, a Yoy decrease of 540, and the proportion also decreased to 64.8%. The store changes show that the company has continued to optimize channel combing to provide customers with a high-quality offline experience, and store efficiency continues to improve.

### **Promote online and offline integration**

During the epidemic, the company continued to expand its online membership and provided diversified membership activities and services through global consumer reach. As of February 28, 2020, the company's cumulative registered members increased by 3.6 million quarterly to 40.9 million. In-store retail sales contributed by Q1/Q2/Q3/Q4 members accounted for 96.7%/97.3%/97.1%/95.3% of the total. The Topsports sports app has been online for more than a year. As of February 28, the number of users has exceeded 2.7 million to build a user community and increase customer stickiness. In the second half of the fiscal year, an online community "Tao Ker" will be added for members to share here. Exchange experiences and create an online sports lifestyle community. In the future, the company will focus on online and offline integration to achieve seamless interaction with consumers in physical and virtual scenarios, including increasing the coverage of store-based social programs and opening mobile cashier tools.

### **Follow-up to Xinjiang Cotton Incident**

After the incident, the company suffered a greater negative impact on sales in the first three weeks, and it has now begun to gradually recover. Sales in April recorded a positive growth Yoy in 2020, and sales during the May 1st period compared to the same period in 2019 have also returned to positive Growth, the company maintains its annual growth target. In the early stage of the incident, the company paid close attention to the development of the situation and terminal sales performance. Through the dynamic management of goods, discount control and store management, and the support of brand owners, the impact of the incident was reduced.

### **Valuation and investment advice**

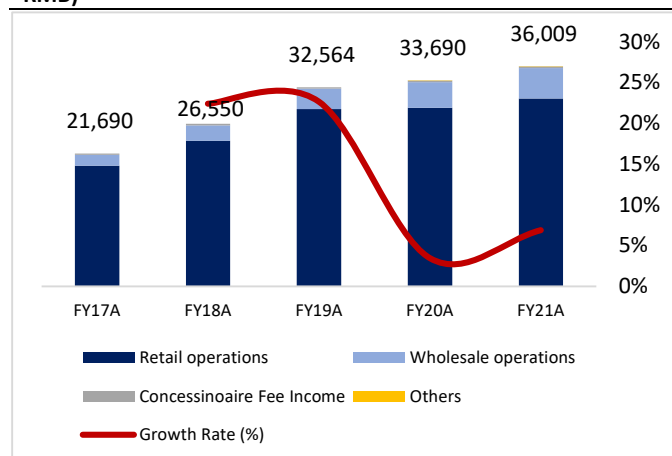
The company was affected by the epidemic last year and gradually recovered in the second half of the year. In terms of revenue, it recorded a MSD growth compared with the same period last year, which was lower than our previous expectations. However, the company's cost control during the period was adequate and the profit side was in line with our previous expectation. Affected by the Xinjiang cotton incident, it has a negative impact on the company's sales in the first quarter of this fiscal year, but it has gradually recovered recently. We lowered the company's revenue forecast in FY22 to CNY 41.04 billion (previous forecast: CNY 45.10 billion), raised the company's GPM to 41.9% (previously: 41.4%), and lowered the company's sales expense ratio and administrative expense ratio to 28.0% and 3.7% respectively (previously: 28.5% and 3.8%). The overall profit forecast is revised up by 4.0% to CNY 3.24 billion. Raise the target price to HKD 15.34, corresponding to the FY22E/FY23E P/E ratio of 25.0x/22.9x, and upgrade the rating to BUY.

(Closing price as at 11 June)

**Risk**

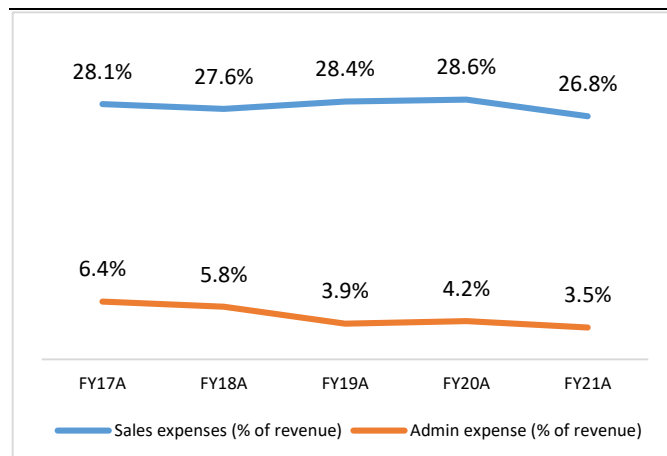
1) The impact of COVID-19 continues 2) The business relies on two major brands 3) The cash level is at a low level due to the dividend policy 4) Major brands are affected by the boycott

**Figure 1: The company's business revenue and growth (million RMB)**



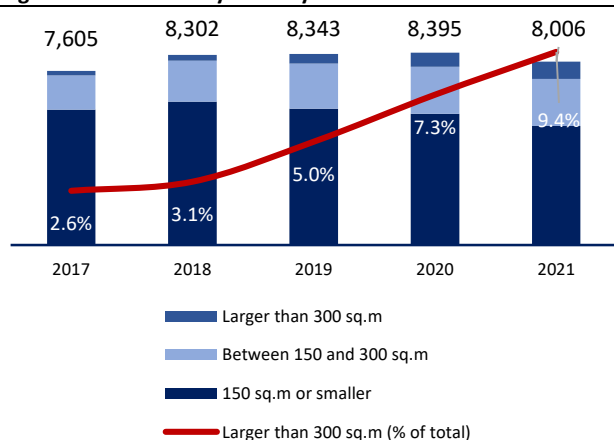
Source: Company, PSHK

**Figure 2: The company's period expenses to revenue ratio**



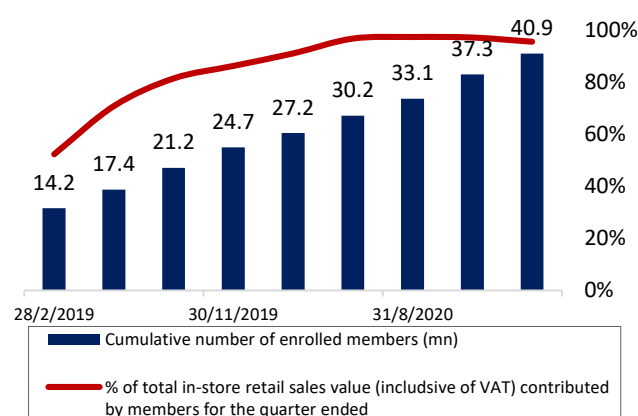
Source: Company, PSHK

**Figure 3: The number of company stores and the proportion of large stores increased year-on-year**



Source: Company, PSHK

**Figure 4: The number of registered members of the company and the proportion of sales contributed by members increased**



Source: Company, PSHK

## Financial

### Consolidated Statement of Profit or Loss

Feb Y/E, RMB mn	FY20	FY21	FY22E	FY23E	FY24E
Revenue	33,690	36,009	41,040	45,429	50,300
COGS	(19,503)	(21,328)	(23,780)	(26,400)	(29,318)
<b>Gross Profit</b>	<b>14,188</b>	<b>14,681</b>	<b>17,261</b>	<b>19,029</b>	<b>20,981</b>
Admin expense	(1,361)	(1,243)	(1,518)	(1,681)	(1,861)
S&D expense	(9,644)	(9,655)	(11,491)	(12,720)	(14,084)
Other operating gain/(loss)	172	206	190	190	190
<b>Operating Profit</b>	<b>3,355</b>	<b>3,989</b>	<b>4,441</b>	<b>4,818</b>	<b>5,226</b>
Net finance income	(217)	(139)	(69)	(51)	(30)
Listing ex	(52)	-	-	-	-
<b>Profit before tax</b>	<b>3,086</b>	<b>3,851</b>	<b>4,372</b>	<b>4,767</b>	<b>5,197</b>
Tax	(783)	(1,081)	(1,137)	(1,240)	(1,351)
NCI	-	-	-	-	-
<b>Profit for the year</b>	<b>2,303</b>	<b>2,770</b>	<b>3,235</b>	<b>3,528</b>	<b>3,846</b>
<b>EPS</b>	<b>40.88</b>	<b>44.67</b>	<b>52.17</b>	<b>56.89</b>	<b>62.01</b>

### Key Financial Data

Feb Y/E	FY20	FY21	FY22E	FY23E	FY24E
<b>Valuation Ratio</b>					
P/E ratio, x	24.99	22.87	19.58	17.96	16.48
P/B ratio, x	6.01	6.53	5.53	4.76	4.13
Dividend Yield, %	2.00	2.19	2.55	2.78	3.03

### Per share data (RMB cent)

EPS	40.88	44.67	52.17	56.89	62.01
BVPS	170.02	156.51	184.85	214.71	247.26
DPS (HKD cent)	24.05	26.28	30.69	33.47	36.48

### Growth & Margin

<b>Growth</b>					
Revenue Growth	3%	7%	14%	11%	11%
Operating Profit Growth	3%	19%	11%	9%	8%
Net Profit Growth	5%	20%	17%	9%	9%
<b>Margin</b>					
Gross Profit Margin	42%	41%	42%	42%	42%
Operating Profit Margin	10%	11%	11%	11%	10%
Net Profit Margin	7%	8%	8%	8%	8%

### Key Ratios

ROE	22%	29%	28%	26%	25%
ROA	10%	16%	17%	16%	16%

(Closing price as at 11 June)

Source: Phillip Securities Research

### Consolidated Statement of Financial Position

Feb Y/E, RMB mn	FY20	FY21	FY22E	FY23E	FY24E
<b>Non Current Asset</b>					
PPE	1,154	1,020	1,209	1,434	1,701
Right-of-use asset	3,909	3,625	3,625	3,625	3,625
LT investment	256	266	266	266	266
Other	1,341	2,356	2,356	2,356	2,356
<b>Total Non Current Assets</b>	<b>6,659</b>	<b>7,266</b>	<b>7,456</b>	<b>7,681</b>	<b>7,947</b>
<b>Current Asset</b>					
T/R	1,487	2,177	2,474	2,738	3,032
Inventories	6,649	6,211	6,515	7,233	8,032
Restricted Bank deposits	3,595	-	-	-	-
Cash and cash equivalents	2,824	1,229	2,140	3,201	4,318
Others	822	823	823	823	823
<b>Total Current Assets</b>	<b>15,376</b>	<b>10,440</b>	<b>11,952</b>	<b>13,995</b>	<b>16,205</b>
<b>Total Assets</b>	<b>22,035</b>	<b>17,706</b>	<b>19,407</b>	<b>21,675</b>	<b>24,153</b>
<b>Non Current Liabilities</b>					
Loan	-	-	-	-	-
Deferred tax liabilities	73	246	246	246	246
Others	2,520	2,329	2,329	2,329	2,329
<b>Total Non Current Liabilities</b>	<b>2,593</b>	<b>2,575</b>	<b>2,575</b>	<b>2,575</b>	<b>2,575</b>
<b>Current Liabilities</b>					
Loan	2,400	1,337	1,337	1,337	1,337
T/P	1,106	445	1,042	1,157	1,285
B/P	1,593	1,516	1,853	2,052	2,272
Others	3,800	2,127	1,137	1,240	1,351
<b>Total Current Liabilities</b>	<b>8,899</b>	<b>5,426</b>	<b>5,370</b>	<b>5,786</b>	<b>6,245</b>
<b>Equity</b>					
Share capital	0	0	0	0	0
Reserve	10,543	9,706	11,463	13,315	15,333
<b>Total Equity</b>	<b>10,543</b>	<b>9,706</b>	<b>11,463</b>	<b>13,315</b>	<b>15,333</b>
<b>Total Liabilities and Equity</b>	<b>22,035</b>	<b>17,706</b>	<b>19,407</b>	<b>21,675</b>	<b>24,153</b>

### Consolidated Statement of Cash Flow

Feb Y/E, RMB mn	FY20	FY21	FY22E	FY23E	FY24E
<b>EBITDA</b>	<b>5,831</b>	<b>5,062</b>	<b>5,389</b>	<b>5,943</b>	<b>6,560</b>
Chg in working cap	1,056	593	(986)	(669)	(745)
Others	89	-	-	-	-
Tax	(528)	(950)	(807)	(1,137)	(1,240)
<b>CFO</b>	<b>6,448</b>	<b>4,706</b>	<b>3,596</b>	<b>4,137</b>	<b>4,575</b>
Capex	(702)	(637)	(1,138)	(1,349)	(1,600)
Others	(3,594)	2,735	25	43	64
<b>CFI</b>	<b>(4,297)</b>	<b>2,098</b>	<b>(1,113)</b>	<b>(1,307)</b>	<b>(1,536)</b>
Issue of Shares	7,076	-	-	-	-
Dividends paid	(744)	(3,659)	(1,478)	(1,676)	(1,828)
Others	(6,056)	(4,740)	(94)	(94)	(94)
<b>CFF</b>	<b>276</b>	<b>(8,398)</b>	<b>(1,572)</b>	<b>(1,770)</b>	<b>(1,921)</b>
<b>Net Change in Cash</b>	<b>2,427</b>	<b>(1,595)</b>	<b>911</b>	<b>1,061</b>	<b>1,118</b>
Foreign exchange	(53)	-	-	-	-
<b>Cash and CE at Y/E</b>	<b>1,284</b>	<b>3,171</b>	<b>4,291</b>	<b>5,834</b>	<b>7,937</b>

**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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**Contact Information (Regional Member Companies)**
**SINGAPORE**
**Phillip Securities Pte Ltd**

250 North Bridge Road, #06-00 Raffles City Tower,  
Singapore 179101

Tel : (65) 6533 6001 Fax: (65) 6535 3834

[www.phillip.com.sg](http://www.phillip.com.sg)

**INDONESIA**
**PT Phillip Securities Indonesia**

ANZ Tower Level 23B, Jl Jend Sudirman Kav 33A,  
Jakarta 10220, Indonesia

Tel (62) 21 5790 0800 Fax: (62) 21 5790 0809

[www.phillip.co.id](http://www.phillip.co.id)

**THAILAND**
**Phillip Securities (Thailand) Public Co. Ltd.**

15th Floor, Vorawat Building, 849 Silom Road,  
Silom, Bangrak, Bangkok 10500 Thailand

Tel (66) 2 2268 0999 Fax: (66) 2 2268 0921

[www.phillip.co.th](http://www.phillip.co.th)

**UNITED STATES**
**Phillip Futures Inc.**

141 W Jackson Blvd Ste 3050

The Chicago Board of Trade Building

Chicago, IL 60604 USA

Tel (1) 312 356 9000 Fax: (1) 312 356 9005

**MALAYSIA**
**Phillip Capital Management Sdn Bhd**

B-3-6 Block B Level 3, Megan Avenue II,  
No. 12, Jalan Yap Kwan Seng, 50450 Kuala Lumpur

Tel (60) 3 2162 8841 Fax (60) 3 2166 5099

[www.poems.com.my](http://www.poems.com.my)

**CHINA**
**Phillip Financial Advisory (Shanghai) Co. Ltd.**

No 436 Heng Feng Road, Green Tech Tower Unit 604  
Shanghai 200 070

Tel (86) 21 5169 9400 Fax: (86) 21 6091 1155

[www.phillip.com.cn](http://www.phillip.com.cn)

**FRANCE**
**King & Shaxson Capital Ltd.**

3rd Floor, 35 Rue de la Bienfaisance  
75008 Paris France

Tel (33) 1 4563 3100 Fax : (33) 1 4563 6017

[www.kingandshaxson.com](http://www.kingandshaxson.com)

**AUSTRALIA**
**PhillipCapital Australia**

L Level 10, 330 Collins Street

Melbourne VIC 3000 Australia

Tel: (61) 3 9618 8238 Fax: (61) 3 9200 2277

[www.phillipcapital.com.au](http://www.phillipcapital.com.au)

**HONG KONG**
**Phillip Securities (HK) Ltd**

11/F United Centre 95 Queensway Hong Kong

Tel (852) 2277 6600 Fax: (852) 2868 5307

[www.phillip.com.hk](http://www.phillip.com.hk)

**JAPAN**
**Phillip Securities Japan, Ltd**

4-2 Nihonbashi Kabutocho, Chuo-ku  
Tokyo 103-0026

Tel: (81) 3 3666 2101 Fax: (81) 3 3664 0141

[www.phillip.co.jp](http://www.phillip.co.jp)

**INDIA**
**PhillipCapital (India) Private Limited**

No. 1, 18th Floor, Urmi Estate, 95 Ganpatrao Kadam Marg,  
Lower Parel West, Mumbai 400013

Tel: (9122) 2300 2999 Fax: (9122) 6667 9955

[www.phillipcapital.in](http://www.phillipcapital.in)

**UNITED KINGDOM**
**King & Shaxson Ltd.**

6th Floor, Candlewick House, 120 Cannon Street  
London, EC4N 6AS

Tel (44) 20 7929 5300 Fax: (44) 20 7283 6835

[www.kingandshaxson.com](http://www.kingandshaxson.com)

**SRI LANKA**
**Asha Phillip Securities Limited**

Level 4, Millennium House, 46/58 Navam Mawatha,  
Colombo 2, Sri Lanka

Tel: (94) 11 2429 100 Fax: (94) 11 2429 199

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