

Xtep Intl (1368 HK)

Dallas Cai

+852 2135 0248

dallas.cai@oriental-patron.com.hk

Megan Jin

+852 2135 0209

megan.jin@oriental-patron.com.hk

Company Update

BUY

UNCHANGED

Close price: HK\$3.60

Target Price: HK\$5.34 (+48%)

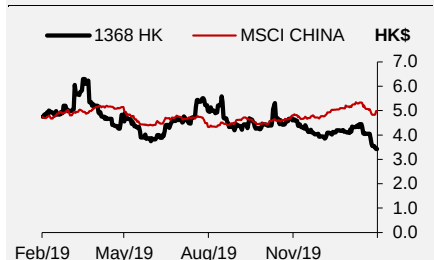
Prior TP: HK\$5.90

Key Data

HKEx code	1368 HK
12 Months High (HK\$)	6.74
12 Month Low (HK\$)	3.39
3M Avg Dail Vol. (mn)	6.13
Issue Share (mn)	2,512.45
Market Cap (HK\$mn)	9,044.80
Fiscal Year	31/12/2018
Major shareholder (s)	Ding Shuibao (54.16%)

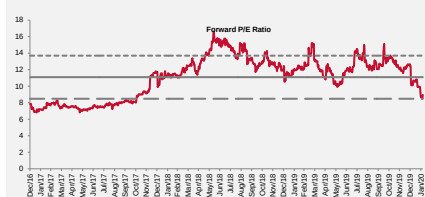
Source: Company data, Bloomberg, OP Research
Closing price as of 05/02/2020

Price Chart



	1mth	3mth	6mth
Absolute %	-15.9	-26.1	-31.4
Rel. MSCI CHINA %	-12.9	-28.8	-46.0

PE



Company Profile

Xtep International Holdings Ltd. designs, manufactures, and markets sportswear. The Company produces footwear, apparel, and accessories.

4Q19 retail in line with expectations

- Xtep announced 4Q19 retail performance with total sell-through up above 20% yoy and SSSG up LTS, in line with our expectations.
- We revise up our FY20E adj. net earnings by 3.8% to RMB837mn to factor in full consolidation of Palladium and K-Swiss.
- Maintain BUY with TP cut to HK\$5.34 from HK\$5.90 based on 14x FY20E P/E (vs previous 16x FY20E P/E) on lower visibility for 1H20E offline retail performance.

4Q19 in line with expectations. Xtep kept stable retail sell-through (incl. both online and offline) with above 20% yoy growth in 4Q19, vs around 20% in 3Q19. SSSG slightly improved to LTS, vs ~10% in 3Q19 and MTS in 4Q18. Retail discount level remained stable at 20~25% off, vs 22~25% off in 3Q19 and 20~25% off in 4Q18. Retail inventory turnover remained healthy at around 4 months, flattish YoY/MoM.

Revise up FY20E adj. net earnings by 3.8% to RMB837mn. We revise up FY20E revenue by 11.3% to RMB9,847mn from RMB8,845mn to factor in the consolidated K-Swiss and Palladium. Overall GPM is therefore dragged slightly to 42.9% from 43.6% due to dilution from new brands. We've also trimmed expected JV losses as the JV brands especially Saucony has been ready to make positive operating profit contribution with faster than expected distribution channel building. As a result, our FY20E diluted EPS is revised up by 3.8% to HK\$0.381.

Maintain BUY with TP cut to HK\$5.34. We maintain BUY on Xtep and cut our TP to HK\$5.34 from HK\$5.90 based on 14x FY20E P/E, vs previous 16x FY20E P/E on lower visibility for 1H20E retail performance. The coronavirus outbreak is expected to hit not only offline POS but also online platforms as ground logistics got significantly restricted. A clearer picture may be given during the result announcement in March and the 1Q20E operation update.

Risks: (1) Severer than expected impact from coronavirus on retail growth, (2) deflated consumer confidence due to slowing down macro economy, (3) execution risks in overseas expansion and the ramp-up of newly acquired brands.

Exhibit 1: Forecast and Valuation

Year to Dec (RMB mn)	FY17	FY18	FY19E	FY20E	FY21E
Revenue	5,113.4	6,383.2	7,722.4	9,847.1	11,102.1
Growth (%)	(5.2)	24.8	21.0	27.5	12.7
Adjusted net profit	529.0	577.3	667.0	837.2	1,010.3
Growth (%)	(22.7)	60.9	1.6	25.5	20.7
Diluted EPS (HK\$)	0.298	0.324	0.322	0.381	0.460
EPS growth (%)	0.3	9.0	(0.8)	18.6	20.7
Change to previous EPS (%)			0.0	3.8	
Consensus EPS (HK\$)			0.343	0.420	
ROE (%)	8.0	12.4	11.1	12.1	13.8
P/E (x)	12.1	11.1	10.7	9.0	7.5
P/B (x)	1.2	1.2	1.1	1.1	1.0
Yield (%)	4.1	5.8	5.6	6.7	8.1
DPS (HK\$)	0.140	0.200	0.193	0.229	0.276

Source: Bloomberg, OP Research

Exhibit 2: Earnings Revision

(RMB mn)	FY19E			FY20E			OP Comments
	New	Old	% Chg	New	Old	% Chg	
Revenue	7,722	7,722	0.0	9,847	8,845	11.3	Add in consolidated revenue
Gross profit	3,406	3,406	0.0	4,228	3,857	9.6	
Gross margin	44.1%	44.1%	0.0	42.9%	43.6%	(0.7)	
Opex	(2,466)	(2,466)	0.0	(3,012)	(2,631)	14.5	
EBIT	1,092	1,092	0.0	1,308	1,317	(0.7)	
Core Net Profit	706	706	0.0	837	806	3.8	Trimmed JV losses on faster-than-expected ramp-up of Saucony
Diluted EPS (HK\$)	0.322	0.322	0.0	0.381	0.367	3.8	

Source: OP Research

Exhibit 3: Retail sales and SSSG performance

Retail Sales Growth (yoy%)	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
Anta	+low teens	20~30 %	+mid teens	20~25 %	20~25 %	+low teens	+mid teens	+mid teens	+low teens	+mid teens	+mid teens	+ high teens
Li Ning	+HSD	+low teens	+LSD	+mid teens	+mid teens	+low teens	+mid teens	+ high teens	+low 20s	+low 20s	+low 30s	
Xtep	-	-	-	-	-	-	-	-	20%+	20%+	20%~	20%+
361 Degrees (Core brands offline)	-	+HSD	+HSD	+HSD	+HSD	+HSD	+MSD	flat	+LSD	+LSD	+LSD	+LSD

Same Store Sales Growth (yoy%)	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
Li Ning	flat	+ HSD	-LSD	+low teens	+low teens	+ HSD	+low teens	+mid teens	+mid teens	+mid teens	+ high teens	
Xtep	+ LSD	+ MSD	+ MSD	+ HSD	+low teens	+mid teens	+mid teens	+mid teens	+low teens	+low teens	10%~	+low teens

Financial Summary

Year to Dec	FY17	FY18	FY19E	FY20E	FY21E
Income Statement (RMB mn)					
Xtep core brands	5,113	6,383	7,722	8,677	9,698
Acquired brands	0	0	0	1,170	1,404
Turnover	5,113	6,383	7,722	9,847	11,102
YoY%	(5.2)	24.8	21.0	27.5	12.7
COGS	(2,869)	(3,555)	(4,317)	(5,619)	(6,312)
Gross profit	2,244	2,828	3,406	4,228	4,790
Gross margin	43.9%	44.3%	44.1%	42.9%	43.1%
Other income	158	196	152	92	92
Selling & distribution	(911)	(1,357)	(1,677)	(1,995)	(2,180)
Admin	(623)	(456)	(511)	(594)	(664)
R&D	(143)	(166)	(178)	(246)	(255)
Other opex	0	0	(100)	(177)	(133)
Total opex	(1,678)	(1,980)	(2,466)	(3,012)	(3,233)
Operating profit (EBIT)	725	1,044	1,092	1,308	1,649
Operating margin	14.2%	16.4%	14.1%	13.3%	14.9%
Provisions	0	0	0	0	0
Interest Income	52	72	62	57	58
Finance costs	(106)	(141)	(144)	(144)	(144)
Profit after financing costs	671	976	1,010	1,221	1,564
Associated companies & JVs	0	0	(20)	(30)	(100)
Pre-tax profit	671	976	990	1,191	1,464
Tax	(224)	(306)	(313)	(342)	(438)
Minority interests	(38)	(13)	(10)	(12)	(16)
Profit from discontinued operations	0	0	0	0	0
Net profit	408	657	667	837	1,010
YoY%	(23)	61	2	26	21
Adjusted net profit	529	577	706	837	1,010
YoY%	0	9	22	19	21
Adjusted net margin	10.3%	9.0%	9.1%	8.5%	9.1%
EBITDA	783	1,126	1,160	1,384	1,734
EBITDA margin	15.3%	17.6%	15.0%	14.1%	15.6%
EPS (RMB)	0.184	0.295	0.264	0.332	0.400
YoY%	0	9	(1)	19	21
DPS (HK\$)	0.140	0.200	0.193	0.229	0.276
Year to Dec	FY17	FY18	FY19E	FY20E	FY21E
Cash Flow (RMB mn)					
EBITDA	783	1,126	1,160	1,384	1,734
Chg in working cap	(119)	(513)	(207)	(430)	(450)
Others	205	(94)	0	0	0
Operating cash	868	518	953	954	1,284
Interest received	(51)	(55)	62	57	58
Tax	(259)	(309)	(54)	(313)	(342)
Net cash from operations	558	154	960	698	1,001
Capex	(123)	(72)	(88)	(112)	(126)
Investments	(75)	(81)	(2,000)	0	0
Change in short-term bank deposits	447	(234)	0	0	0
Sales of assets	63	83	0	0	0
Interests received	0	0	0	0	0
Others	(37)	24	0	0	0
Investing cash	275	(281)	(2,088)	(112)	(126)
FCF	833	(127)	(1,127)	586	875
Issue of shares	7	59	1,178	0	0
Buy-back	0	(89)	0	0	0
Minority interests	0	(4)	0	0	0
Dividends paid	(271)	(459)	(461)	(470)	(564)
Net change in bank loans	421	(10)	0	0	0
Others	(3)	(7)	(144)	(144)	(144)
Financing cash	154	(511)	573	(614)	(708)
Net change in cash	987	(637)	(554)	(28)	167
Exchange rate or other Adj	(1)	1	0	0	0
Opening cash	2,847	3,832	3,196	2,642	2,614
Closing cash	3,832	3,196	2,642	2,614	2,781
CFPS (HK\$)	0.314	0.087	0.438	0.318	0.456

Source: Company, OP Research

Year to Dec	FY17	FY18	FY19E	FY20E	FY21E
Ratios					
Gross margin (%)	43.9	44.3	44.1	42.9	43.1
Operating margin (%)	14.2	16.4	14.1	13.3	14.9
Net margin (%)	8.0	10.3	8.6	8.5	9.1
Selling & dist'n exp/Sales (%)	17.8	21.3	21.7	20.3	19.6
Admin exp/Sales (%)	12.2	7.2	6.6	6.0	6.0
Salaries/Sales (%)	12.1	11.6	11.4	10.4	10.3
A&P/Sales (%)	12.9	15.2	16.2	15.5	15.0
R&D/Sales (%)	2.8	2.6	2.3	2.5	2.3
Payout ratio (%)	101.4	59.5	60.0	60.0	60.0
Effective tax (%)	33.5	31.4	31.0	28.0	28.0
Total debt/equity (%)	35.4	36.5	29.0	27.5	25.8
Net debt/equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Current ratio (x)	3.2	2.5	2.1	2.0	2.0
Quick ratio (x)	2.9	2.2	1.9	1.8	1.8
Inventory T/O (days)	91	86	86	86	86
AR T/O (days)	129	121	120	117	115
AP T/O (days)	131	90	90	90	90
Cash conversion cycle (days)	90	117	116	113	111
Asset turnover (x)	0.6	0.7	0.8	0.8	0.9
Financial leverage (x)	1.7	1.7	1.7	1.7	1.7
EBIT margin (%)	14.2	16.4	14.1	13.3	14.9
Interest burden (x)	0.9	0.9	0.9	0.9	0.9
Tax burden (x)	0.6	0.7	0.7	0.7	0.7
Return on equity (%)	8.0	12.4	11.1	12.1	13.8
ROIC (%)	19.9	26.2	19.0	18.4	21.7
Year to Dec	FY17	FY18	FY19E	FY20E	FY21E
Balance Sheet (RMB mn)					
Fixed assets	686	677	698	736	779
Intangible assets & goodwill	8	8	6	4	3
Associated companies & JVs	0	0	(20)	(50)	(150)
Long-term investments	267	339	2,339	2,339	2,339
Other non-current assets	92	114	114	114	114
Non-current assets	1,052	1,139	3,138	3,144	3,085
Inventories	718	836	836	1,015	1,321
AR	1,807	2,115	2,539	3,156	3,498
Prepayments & deposits	572	727	880	1,122	1,265
Other current assets	953	1,186	1,186	1,186	1,186
Cash	3,832	3,196	2,642	2,614	2,781
Current assets	7,882	8,060	8,082	9,093	10,050
AP	1,028	879	1,067	1,389	1,560
Tax	66	54	313	342	438
Accruals & other payables	565	861	1,042	1,329	1,498
Bank loans & leases	831	1,483	1,483	1,483	1,483
CB & othe debts	0	0	0	0	0
Other current liabilities	0	1	1	1	1
Current liabilities	2,489	3,278	3,905	4,543	4,980
Bank loans & leases	1,019	461	461	461	461
CB & othe debts	0	0	0	0	0
Deferred tax & others	97	129	129	129	129
MI	108	5	14	26	42
Non-current liabilities	1,224	595	604	616	632
Total net assets	5,221	5,326	6,711	7,078	7,524
Shareholder's equity	5,221	5,326	6,711	7,078	7,524
Share capital	20	20	20	20	20
Reserves	5,201	5,306	6,691	7,058	7,504
BVPS (HK\$)	2.94	2.97	3.09	3.26	3.46
Total debts	1,850	1,944	1,944	1,944	1,944
Net cash/(debts)	2,934	2,438	1,884	1,856	2,023

Exhibit 4: Peer Group Comparison

Company	Ticker	Price	Mkt cap (US\$m)	3-mth avg t/o (US\$m)	PER			EPS			3-Yr EPS Cagr (%)	Div yld		P/B		EV/		Net gearing Hist (%)	Gross margin Hist (%)	Net margin Hist (%)	ROE Hist (%)	ROE FY1 (%)	Sh px 1-mth %	Sh px 3-mth %
					Hist (x)	FY1 (x)	FY2 (x)	FY1 YoY%	FY2 YoY%	FY2 Cagr (%)		Hist (%)	FY1 (%)	Hist (x)	FY1 (x)	Hist (%)	Cur Yr							
Xtep Intl	1368 HK	3.60	1,165	3.3	11.1	10.7	9.0	(0.8)	18.6	21.1	0.5	5.6	5.6	1.2	1.1	5.0	5.8	Net cash	44.3	10.3	12.4	11.1	(12.2)	(21.7)
HSI		26,786.74			10.5	10.2	9.5	2.3	8.3	8.4	1.22	3.7	4.0	1.17	1.08						11.1	10.6	(5.9)	(3.2)
HSCEI		10,493.85			8.3	8.0	7.3	3.7	9.2	3.5	2.29	3.6	4.2	1.12	0.99						13.6	12.4	(6.8)	(3.5)
CSI300		3,828.53			13.6	11.1	9.9	22.0	12.5			2.2	2.8	1.8	1.5						12.9	13.6	(7.6)	(4.4)
Domestic peers																								
Adjusted sector avg*					31.5	18.6	15.1	44.8	26.5	29.6	0.8	2.8	4.5	2.2	3.0	12.7	10.6	6.6	43.1	7.8	14.3	10.6	(8.0)	(15.4)
361 Degrees	1361 HK	1.22	325	0.3	7.5	4.9	4.2	52.4	16.1	24.0	0.2	7.6	8.8	0.4	0.4	(0.8)	(0.7)	0.0	40.6	5.9	5.5	7.8	(12.2)	(25.6)
Anta Sports Prod	2020 HK	68.80	23,941	56.6	40.6	30.8	23.1	31.8	33.5	29.9	1.0	0.9	1.2	9.3	8.5	28.0	19.2	0.0	52.6	17.0	28.6	30.2	(0.9)	(11.9)
Li Ning Co Ltd	2331 HK	23.40	7,397	32.7	71.2	35.5	29.6	100.8	19.7	45.8	0.8	0.4	0.9	7.5	7.2	40.3	25.8	0.0	48.1	6.8	20.9	21.2	(0.2)	(9.5)
Pou Sheng Intl	3813 HK	2.24	1,545	1.0	19.4	13.2	9.9	47.3	33.3	33.8	0.4	1.1	1.4	1.5	1.4	10.7	7.1	39.8	33.5	2.4	9.6	10.3	(7.1)	(23.5)
China Dongxiang	3818 HK	0.81	614	0.5	N/A	7.1	8.1	N/A	(12.6)	N/A	N/A	5.6	10.3	0.4	0.4	N/A	1.3	0.0	N/A	N/A	N/A	5.8	(6.9)	(8.2)
Annil Co Ltd-A	002875 CH	13.15	247	7.0	18.7	20.4	15.7	(8.5)	29.9	14.5	1.4	1.2	N/A	2.0	1.8	15.1	10.8	0.0	55.3	6.9	6.9	7.5	(20.7)	(21.0)
Guirenniao Co-A	603555 CH	3.44	309	12.7	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	1.4	1.5	(17.1)	N/A	146.8	28.7	(24.4)	(46.6)	(8.9)	(41.5)	(8.3)
International peers																								
Adjusted sector avg*					50.2	43.3	35.4	26.8	21.1	20.5	1.96	0.8	0.6	10.90	10.87	35.9	23.2	0.0	49.0	7.2	27.0	27.7	1.7	13.9
Nike Inc -Cl B	NKE US	101.38	157,886	578.6	39.8	33.5	29.0	18.6	15.6	17.0	2.0	0.9	0.9	16.9	18.7	29.5	25.8	0.0	44.7	10.3	50.6	49.4	(0.5)	12.8
Under Armour-A	UAA US	20.79	8,805	102.6	N/A	60.6	44.6	N/A	35.9	(280.7)	N/A	N/A	0.0	4.4	4.3	61.8	22.8	8.5	45.1	(0.9)	5.4	7.3	(4.9)	16.1
Lululemon Ath	LULU US	247.99	32,312	426.9	68.3	50.8	42.9	34.4	18.4	23.6	2.2	N/A	0.0	19.6	17.6	39.1	31.4	0.0	55.2	14.7	37.1	38.1	6.6	27.6
Adidas Ag	ADS GR	289.15	63,995	156.0	34.3	29.6	26.4	15.7	12.3	13.6	2.2	1.2	1.3	8.0	8.0	21.1	16.7	0.0	51.9	7.8	28.2	29.0	(0.6)	3.0
Puma Se	PUM GR	73.20	12,192	24.3	58.4	42.2	34.3	38.4	23.0	27.8	1.5	0.5	0.7	5.6	5.8	27.8	19.3	0.0	48.4	4.0	14.0	14.5	8.0	9.7

* Outliners and "N/A" entries are in red and excl. from the calculation of averages

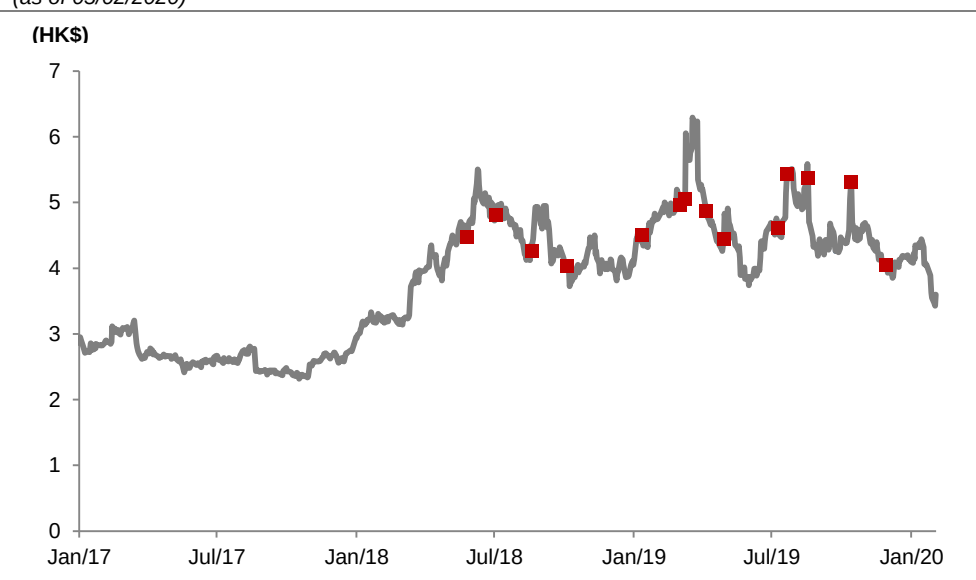
Source: Bloomberg, OP Research

Our recent reports

Date	Company / Sector	Stock Code	Title	Rating	Analyst
17/01/2020	Edvantage Group	382	FY20/21E saw a good start	BUY	Yuji Fung/Dallas Cai
17/01/2020	361 Degrees Intl	1361	4Q19 retail sales on track	BUY	Megan Jin
15/01/2020	Anta Sports	2020	Issuance of CB to optimize financial structure	BUY	Dallas Cai/Megan Jin
10/01/2020	Sunny Optical	2382	2019 shipment targets met - as expected	BUY	Yuji Fung/Dallas Cai
08/01/2020	Q Tech	1478	2019 full year shipments meet OP targets	BUY	Yuji Fung/Dallas Cai
31/12/2019	GT Service	2869	Introducing Longfor as 3rd largest shareholder	BUY	Dallas Cai/Yuji Fung
20/12/2019	Q Tech	1478	Top-up placement for CCM capacity expansion	BUY	Yuji Fung/Dallas Cai
17/12/2019	Aidigong	286	Transforming into a leading postpartum care player in China	NR	Yuji Fung
13/12/2019	Anta Sports	2020	Revealing higher visibility of post-M&A roadmap	BUY	Dallas Cai/Megan Jin
10/12/2019	Sunny Optical	2382	November saw strong HCM shipment growth	BUY	Yuji Fung/Dallas Cai
10/12/2019	Q Tech	1478	November shipments maintain full steam	BUY	Yuji Fung/Dallas Cai
03/12/2019	Xtep Intl	1368	Update on winter sales and new brand	BUY	Dallas Cai/Megan Jin
28/11/2019	Edvantage Group	382	Advantageous Educator in Greater Bay Area	BUY	Yuji Fung/Dallas Cai
14/11/2019	Ausnutria Dairy	1717	3Q results up to expectations	BUY	Dallas Cai/Megan Jin
14/11/2019	Anta Sports	2020	Dispose 5% of Amer for introduction of experienced investors	BUY	Dallas Cai/Megan Jin
11/11/2019	Sunny Optical	2382	October shipments in line with expectations	BUY	Yuji Fung/Dallas Cai
11/11/2019	Q Tech	1478	Another month of robust growth in October	BUY	Yuji Fung/Dallas Cai
30/10/2019	CH Display OPT	334	More shifting to processing mode in 3Q19	HOLD	Yuji Fung/Dallas Cai
22/10/2019	Li-Ning	2331	3Q19 saw solid retail performance	BUY	Dallas Cai/Megan Jin
21/10/2019	Q Tech	1478	Upgrade on diversified global footprint	BUY	Yuji Fung/Dallas Cai
18/10/2019	Xtep Intl	1368	3Q19 operations in line	BUY	Dallas Cai/Megan Jin
17/10/2019	Anta Sports	2020	3Q19 retail performance up to expectations	BUY	Dallas Cai/Megan Jin
17/10/2019	361 Degrees Intl	1361	3Q19 operations in line with expectations	BUY	Megan Jin
14/10/2019	Sunny Optical	2382	Another month of robust HLS growth	BUY	Yuji Fung/Dallas Cai
11/10/2019	Q Tech	1478	September saw robust shipment growth momentum	BUY	Yuji Fung/Dallas Cai
02/10/2019	China Prop Mgmt	-	Clear vision of promising secular growth	BUY	Dallas Cai/Yuji Fung
11/09/2019	Q Tech	1478	August saw product mix improving on track	BUY	Yuji Fung/Dallas Cai

Historical recommendations and target price: Xtep (1368 HK)

(as of 05/02/2020)



Date	Rating	TP (HK\$)	Close (HK\$)	Date	Rating	TP (HK\$)	Close (HK\$)
1 15 Jan 2019	BUY	5.70	4.62	6 15 Jul 2019	BUY	5.60	4.74
2 06 Mar 2019	BUY	5.70	5.27	7 24 Jul 2019	BUY	6.40	5.59
3 13 Mar 2019	BUY	6.50	5.30	8 21 Aug 2019	BUY	6.50	5.52
4 09 Apr 2019	BUY	5.70	5.11	9 18 Oct 2019	BUY	6.50	5.31
5 03 May 2019	BUY	5.70	4.67	10 03 Dec 2019	BUY	5.90	4.04

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Buy (B)	We expect this stock outperform the relevant benchmark greater than 15% over the next 12 months.
Hold (H)	We expect this stock to perform in line with the relevant benchmark over the next 12 months.
Sell (S)	We expect this stock to underperform the relevant benchmark greater than 15% over the next 12 month.
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CONTACT

27/F, Two Exchange Square,

8 Connaught Place, Central, Hong Kong

www.oriental-patron.com.hk

dallas.cai@oriental-patron.com.hk

Tel: (852) 2135 0248

Fax: (852) 2135 0295