



Rating  
**Buy**

Asia  
China

Consumer  
Alcohol & Tobacco

Company  
**Kweichow Moutai**

Reuters 600519.SS    Bloomberg 600519 CG    Exchange SHH    Ticker 600519

Date  
25 October 2017

## Forecast Change

Price at 25 Oct 2017 (CNY)	565.98
Price target - 12mth (CNY)	650.00
52-week range (CNY)	582.60 - 308.97
Shanghai Composite	3,388

## 3Q17 result strong beat; reiterating Buy

### Sales more than doubled in 3Q helped by increasing volume

Kweichow Moutai reported 3Q17 results with a **120% yoy sales increase** to RMB18.9bn and **140% yoy net profit increase** to RMB8.7bn. The sales growth was much higher than our forecast at 40% for 3Q, and tracks ahead of street's full year forecast at 27% yoy growth for FY17. Particularly, the strong sales growth is driven by:

- Around 70% yoy volume growth for mainstream Moutai (DB estimates).** To recap, Moutai indicated on August 28 that it supplied 6,200 tons of liquor (including 5,600 tons of "Feitian Moutai" and 600 tons of other SKUs) between August 15 and September 30, to meet the strong demand during National Holiday and Mid-Autumn Festival, implying 70% yoy growth.
- Strong growth of super premium Moutai.** We estimated that most of 600 tons of other SKU are super premium Moutai. This drives mix-upgrade for mainstream Moutai.
- Strong growth of mass market Moutai products.** According to news from Moutai website, mass market Moutai sales increased over 200% yoy in the first 9 months. This is a result of Moutai's "133" brand strategy (one core brand, three strategy brands - Huamao, Wangmao, Laimao, and three key brands - Hanjiang, Renjiu and Wangzi). Meanwhile, the number of domestic distributors increased by 634 YTD to 2,965, mainly for penetration of mass market Moutai.

### Net margin expanded 440bps yoy on operating leverage

Moutai's gross margin was stable at 75% in 3Q17, as the impact from lower margin mass-market products was offset by high margin customized Moutai. Selling expense ratio increased 20bps yoy to 3.2%, due to increasing A&P expense for its "133" brand strategy and "5+5" channel strategy (5 core markets and 5 potential markets). G&A expense ratio declined 480bps yoy, mainly helped by operating leverage.

### Increasing transparency in revenue recognition

Moutai booked most ex-factory shipments as revenue in 3Q17. This is different from market's and our expectation that it would allocate the shipments into sales and advances from customer accounts. Therefore, advances from customers

### Valuation & Risks

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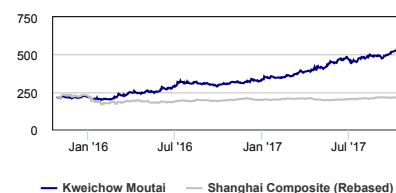
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#### Key changes

TP	610.00 to 650.00	↑	6.6%
Sales (FYE)	44,121 to 44,522	↑	0.9%
Op prof margin (FYE)	71.5 to 71.6	↑	0.2%
Net profit (FYE)	23,054.7 to 23,295.4	↑	1.0%

Source: Deutsche Bank

#### Price/price relative



Performance (%)	1m	3m	12m
Absolute	11.6	18.4	80.8
Shanghai Composite	1.4	4.5	8.2

Source: Deutsche Bank

#### Key indicators (FY1)

ROE (%)	29.0
Net debt/equity (%)	-85.6
Book value/share (CNY)	69.79
Price/book (x)	8.1
Net interest cover (x)	-
Operating profit margin (%)	71.6

Source: Deutsche Bank

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were stable at Rmb17bn on Sep 30 (vs Rmb18bn on June 30). This partly contributed to the results beat in 3Q. We believe this implies increasing transparency and improving cooperate governance for the company.

### Reiterating Buy with new target price at Rmb650

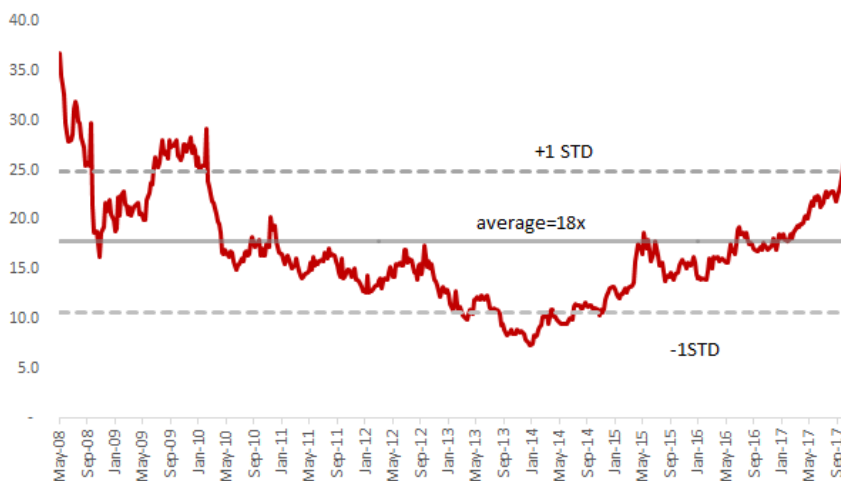
We are revising up our earnings forecast by 1-4% in 2017-19E, to factor in the better than expected sales growth. **We revise up our target price by 6% to Rmb650**, based on a DCF method (factoring in 9.5% WACC and a 2% TGR). The stock currently trades at 25x 2018 and 22x 2019 P/E with 26% earnings CAGR in 2017-19E. We expect street to revise up earnings forecasts and trigger further re-ratings. **We reiterate Buy**. Main downside risks: shorter-than-expected restocking cycle; government policy changes; food safety incidents.

Figure 1: Forecast change

RMBm	New			Old			Change		
	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
<b>Gross sales</b>	<b>54,251</b>	<b>66,938</b>	<b>76,082</b>	53,779	65,259	73,410	0.9%	2.6%	3.6%
Net Sales	44,522	55,048	62,424	44,121	53,636	60,963	0.9%	2.6%	2.4%
Gross profit	39,733	49,319	55,850	39,314	47,944	54,424	1.1%	2.9%	2.6%
EBIT	31,888	40,060	45,952	31,540	38,922	44,232	1.1%	2.9%	3.9%
<b>Net profit</b>	<b>23,295</b>	<b>29,141</b>	<b>33,575</b>	23,055	28,341	32,353	1.0%	2.8%	3.8%
GPM	73.2%	73.7%	73.4%	73.1%	73.5%	74.1%	0.1%	0.2%	-0.7%
EBITM	58.8%	59.8%	60.4%	58.6%	59.6%	60.3%	0.1%	0.2%	0.1%
<b>NPM</b>	<b>42.9%</b>	<b>43.5%</b>	<b>44.1%</b>	42.9%	43.4%	44.1%	0.1%	0.1%	0.1%

Source: Deutsche Bank

Figure 2: 1-year forward PE chart



Source: Deutsche Bank, Bloomberg



Model updated: 25 October 2017

### Running the numbers

Asia

China

Alcohol & Tobacco

### Kweichow Moutai

Reuters: 600519.SS Bloomberg: 600519 CG

### Buy

Price (25 Oct 17) CNY 566.0

Target Price CNY 650.0

52 Week range CNY 308.97 - 582.60

Market cap (m) CNYm 710,984  
USDm 107,136

### Company Profile

Kweichow Moutai is China's largest local spirit brand/producer by sales value.

Fiscal year end 31-Dec 2014 2015 2016 2017E 2018E 2019E

### Financial Summary

DB EPS (CNY)	12.22	12.34	13.31	18.54	23.20	26.73
Reported EPS (CNY)	12.22	12.34	13.31	18.54	23.20	26.73
DPS (CNY)	3.98	6.17	6.79	9.86	12.34	14.22
BVPS (CNY)	42.5	50.9	58.0	69.8	83.1	97.5
Weighted average shares (m)	1,256	1,256	1,256	1,256	1,256	1,256
Average market cap (CNYm)	169,335	256,416	346,172	710,984	710,984	710,984
Enterprise value (CNYm)	145,643	225,583	290,095	632,100	611,412	589,497

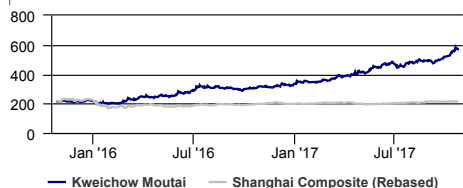
### Valuation Metrics

P/E (DB) (x)	11.0	16.5	20.7	30.5	24.4	21.2
P/E (Reported) (x)	11.0	16.5	20.7	30.5	24.4	21.2
P/BV (x)	4.05	4.28	5.76	8.11	6.81	5.80
FCF Yield (%)	4.8	6.0	10.5	4.4	4.7	5.3
Dividend Yield (%)	2.9	3.0	2.5	1.7	2.2	2.5
EV/Sales (x)	5.1	7.7	9.0	14.2	11.1	9.4
EV/EBITDA (x)	6.6	10.2	12.1	19.1	14.8	12.4
EV/EBIT (x)	6.8	10.6	12.6	19.8	15.3	12.8

### Income Statement (CNYm)

Sales revenue	28,785	29,210	32,353	44,522	55,048	62,424
Gross profit	26,446	26,672	28,943	39,733	49,319	55,850
EBITDA	22,146	22,223	23,997	33,095	41,423	47,471
Depreciation	753	848	934	1,207	1,363	1,519
Amortisation	0	0	0	0	0	0
EBIT	21,393	21,375	23,063	31,888	40,060	45,952
Net interest income(expense)	707	780	1,203	1,819	1,808	2,284
Associates/affiliates	0	0	0	0	0	0
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	-218	-153	-308	-217	-201	-228
Profit before tax	21,882	22,002	23,958	33,490	41,668	48,008
Income tax expense	5,613	5,547	6,027	8,707	10,667	12,290
Minorities	920	952	1,212	1,487	1,860	2,143
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	15,350	15,503	16,718	23,295	29,141	33,575
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	15,350	15,503	16,718	23,295	29,141	33,575

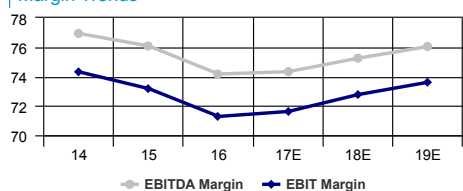
### Price Performance



### Cash Flow (CNYm)

Cash flow from operations	12,633	17,436	37,451	32,612	34,485	39,005
Net Capex	-4,431	-2,061	-1,019	-1,276	-1,406	-1,590
Free cash flow	8,201	15,375	36,432	31,335	33,080	37,415
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-5,122	-5,554	-8,351	-8,526	-12,391	-15,500
Net inc/(dec) in borrowings	1,246	1,948	4,811	11	11	11
Other investing/financing cash flows	105	65	6	-2	0	0
Net cash flow	4,430	11,834	32,899	22,818	20,699	21,925
Change in working capital	-4,480	471	19,162	6,001	2,121	1,768

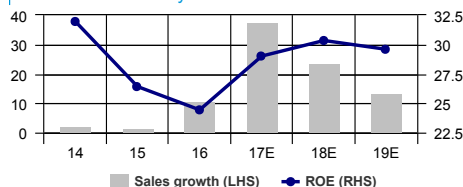
### Margin Trends



### Balance Sheet (CNYm)

Cash and other liquid assets	27,711	36,801	66,855	89,673	110,372	132,298
Tangible fixed assets	13,798	16,312	17,199	17,332	17,436	17,569
Goodwill/intangible assets	3,583	3,582	3,532	3,481	3,430	3,380
Associates/investments	64	29	29	29	29	29
Other assets	20,718	29,577	25,320	27,827	32,807	36,916
Total assets	65,873	86,301	112,935	138,342	164,074	190,191
Interest bearing debt	4,019	5,967	10,779	10,790	10,800	10,811
Other liabilities	6,543	14,100	26,257	35,397	42,509	48,398
Total liabilities	10,562	20,067	37,036	46,186	53,310	59,209
Shareholders' equity	53,430	63,926	72,894	87,664	104,413	122,488
Minorities	1,881	2,308	3,004	4,491	6,351	8,494
Total shareholders' equity	55,312	66,234	75,899	92,155	110,765	130,982
Net debt	-23,692	-30,833	-56,076	-78,884	-99,572	-121,487

### Growth & Profitability



### Key Company Metrics

Sales growth (%)	2.3	1.5	10.8	37.6	23.6	13.4
DB EPS growth (%)	1.4	1.0	7.8	39.3	25.1	15.2
EBITDA Margin (%)	76.9	76.1	74.2	74.3	75.3	76.0
EBIT Margin (%)	74.3	73.2	71.3	71.6	72.8	73.6
Payout ratio (%)	32.5	50.0	51.0	53.2	53.2	53.2
ROE (%)	32.0	26.4	24.4	29.0	30.3	29.6
Capex/sales (%)	15.4	7.1	3.2	2.9	2.6	2.5
Capex/depreciation (x)	5.9	2.4	1.1	1.1	1.0	1.0
Net debt/equity (%)	-42.8	-46.6	-73.9	-85.6	-89.9	-92.8
Net interest cover (x)	nm	nm	nm	nm	nm	nm

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Source: Company data, Deutsche Securities estimates



# Appendix 1

## Important Disclosures

\*Other information available upon request

Disclosure checklist			
Company	Ticker	Recent price*	Disclosure
Kweichow Moutai	600519.SS	565.98 (CNY) 25 Oct 2017	NA

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## Historical recommendations and target price. Kweichow Moutai (600519.SS)

(as of 10/25/2017)



### Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

\*\* Analyst is no longer at Deutsche Bank

1.	01/07/2016	Buy, Target Price Change CNY 267,00	Winnie Mak**	4.	06/22/2017	Buy, Target Price Change CNY 550,00	Mark Yuan
2.	09/19/2016	Buy, Target Price Change CNY 385,00	Charlie Chen**	5.	10/06/2017	Buy, Target Price Change CNY 610,00	Mark Yuan
3.	01/18/2017	Buy, Target Price Change CNY 410,00	Charlie Chen**				



### Equity Rating Key

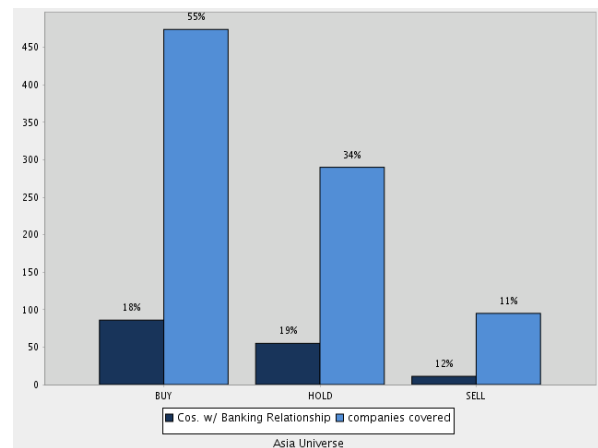
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**Sell:** Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock.

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