



Rating
Buy

Asia
China

Consumer
Alcohol & Tobacco

Company
Wuliangye Yibin

Reuters 000858.SZ Bloomberg 000858 CH Exchange SHZ Ticker 000858

Date
4 January 2018

Forecast Change

Price at 3 Jan 2018 (CNY)	80.90
Price target - 12mth (CNY)	98.00
52-week range (CNY)	82.15 - 35.45
Shenzhen Index	1,986

Don't leave the party too early; reiterating Buy

Entering secular growth cycle

After Wuliangye's 130% share price hike in past 12 month, market has increasing concerns on whether there is still upside. Our view is positive. We expect the company to enter a secular growth period in 2018-19, and its earnings to grow at 29% CAGR in 2018-20, driven by management's strong incentives for growth and expanding high end liquor market after Moutai raising price. We revise up our target price to Rmb98, implying 27x 2018 P/E. We reiterate Buy.

Management has strong incentive to drive sales and improve efficiency

During 1218 distributor meeting, Wuliangye management indicates to achieve gross sales of Rmb40bn in 2018 and Rmb60bn in 2020 (vs Rmb30bn in 2017E). Management will invest in channel penetration, brand building and products streamlining to drive sales growth. Helped by completion of management shares incentive schemes and strong support from Wuliangye group, we believe the company could achieve its target.

Moutai's price hike to release more market for Wuliangye

On Dec 29, Moutai announced to raise ex-factory price by 18% to Rmb969/bottle, and set retail price at Rmb1499/bottle. As a result, the ex-factory price gap of Moutai over Wuliangye expands from 10% to 30%. We believe Wuliangye is the biggest beneficiary of the price hike, helped by the expanding high end liquor market room released by Moutai.

We reiterate Buy; revising up TP to Rmb98

We are revising up our earnings forecast by 13%-42% for 2018-2020 to factor in a better volume growth, mix upgrade, and margin expansion, and revise up target price by 40% to Rmb98 based on DCF model. We are changing our valuation methodology from EV/EBITDA to DCF as we believe DCF model can incorporate long-term growth and solid cash flow. **Downside risk:** channel de-stocking in high-end liquor sector; food safety; worse than expected macro FAI slow down.

Valuation & Risks

Mark Yuan

Research Analyst
+852-2203 6181

Anne Ling

Research Analyst
+852-2203 6177

Key changes

TP	70.00 to 98.00	↑	40.0%
Sales (FYE)	26,123 to 26,475	↑	1.3%
Op prof margin (FYE)	45.1 to 44.7	↓	-0.9%
Net profit (FYE)	9,174.1 to 9,212.7	↑	0.4%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	23.9	41.2	133.4
Shenzhen Index	0.9	-2.7	-2.6

Source: Deutsche Bank

Key indicators (FY1)

ROE (%)	18.4
Net debt/equity (%)	-76.6
Book value/share (CNY)	13.93
Price/book (x)	5.8
Net interest cover (x)	-
Operating profit margin (%)	44.7

Source: Deutsche Bank

Deutsche Bank AG/Hong Kong

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Forecasts and ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
DB EPS FD (CNY)	1.63	1.79	2.43	3.25	4.16
OLD DB EPS FD (CNY)	1.63	1.79	2.42	2.89	3.31
% Change	0.0%	0.0%	0.4%	12.6%	25.6%
PER (x)	15.5	17.4	33.3	24.9	19.4

Source: Deutsche Bank estimates, company data



Internal driver: management has strong incentive to drive sales and improve efficiency

During 1218 distributor meeting held on December 18, 2017, Wuliangye management indicates to achieve gross sales of Rmb40bn in 2018 and Rmb60bn by the end of 13th five year plan (in 2020). This guidance implies 30% yoy growth in 2018 compared to Rmb30bn gross sales in 2017E. The company will enhance its channel, branding and products to achieve the target:

- In channel, to increase penetration in “a hundreds of city, a thousands of country, and ten thousands of stores”.
- In branding, to increase the marketing in all channels and enhance its leading position in aromatic liquor category.
- In products, to streamline the SKUs and focus in one main brand (the mainstream Wuliangye), and three products group targeting at super premium consumers, young consumers and international consumers.

We believe Wuliangye could achieve its sales growth target in 2018-20. The measures can transform it from a SOE company to a solid FMCG company with competitiveness in channels, branding and products. More important, Wuliangye’s management has strong incentives to achieve the target, given 1) the company’s management shares scheme has been approved by regulators and likely to be completed in 2018; 2) 2018 will be the first full year of operation since Mr Liu Shuguang, the Chairman of Wuliangye group, came on board.

Figure 1: Company guidance vs actual performance

Year	Company guidance	Actual/DB estimate
2013	15% yoy sales growth	9% yoy sales decline
2014	Positive growth in sales	15% yoy sales decline
2015	Flattish sales and PBT	3.1% yoy sales increase and 3.4% yoy PBT increase
2016	Sales is not lower than RMB23.8bn, yoy growth over 10%; PBT is targeted to be RMB8.8bn with a yoy growth of 10%	Sales of RMB24.5bn and PBT of RMB9.3bn
2017	Over 10% yoy growth in both sales and PBT	22% yoy sales increase and 36% yoy PBT increase
2018	To achieve sales of RMB40bn	Sales of RMB39.5bn
2020	To achieve sales of RMB60bn	Sales of RMB58.4bn

Source: Deutsche Bank, company annual report

Figure 2: Share scheme schedule

Date	Event
10/30/2015	Announced employee stock ownership plan
6/22/2016	Approved by general meeting
5/15/2017	Approved by China Securites Regulatory Commission
11/7/2017	Approved by China Securites Regulatory Commission to complete the private placement in next 6 months

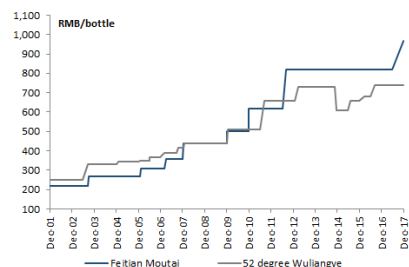
Source: Deutsche Bank, company announcement. Note: The scheme was supposed to be completed before 15 Nov 2017 according to the first approval. It was delayed and approved to be completed before 7 May 2018



External driver: Moutai's price hike to release more market room for Wuliangye

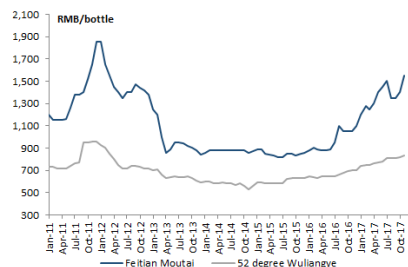
On Dec 29, Moutai announced to raise ex-factory price by 18% to Rmb969/bottle, and raise suggested retail price to Rmb1499/bottle (from Rmb1299/bottle). After the price adjustment, the ex-factory price gap of Moutai vs. Wuliangye expands from 10% to 30%, and suggested retail price gap expand from 18% to 36%.

Figure 3: Moutai and Wuliangye's ex-factory price



Source: Deutsche Bank, Wind

Figure 4: Moutai and Wuliangye's retail price



Source: Deutsche Bank, jianiang.cn

Moutai's price hike should result in increasing demand for Wuliangye. In the retail end, the expanding price gap will lead to part of private consumption (which is price sensitive) switching from Moutai to Wuliangye. Meanwhile, distributors will have less incentives to store up Moutai after price hike, and therefore left more cash flow for Wuliangye procurement. We forecast volume growth of premium Wuliangye to speed up helped by the expanding price gap.

Figure 5: Wuliangye's rebate policy

Date	Seasonal rebate	Annual rebate
Before Feb-13	10%-15%	1%-5%
Feb-13 to Dec-13	Rmb 70 per bottle	Depends on the performance
Jan-Apr 2014	Rmb 70 per bottle, market support	N/A
May-14 to Jul-15	Purchase two bottles at RMB609/bottle then could purchase one bottle at RMB509	N/A
Aug-15 to Mar 16	Rmb 40 per bottle, market support RMB30 per bottle	N/A
Mar-Jun 16	Rmb 30 per bottle	N/A
After Jul-16	No rebate	N/A

Source: Deutsche Bank



Key takeaways from 1218 distributor meeting

1. Targets Rmb60bn sales in 2020

- To increase gross sales from Rmb30bn in 2017 to Rmb40bn in 2018. The key drivers will be double digit volume growth in main stream Wuliangye, increasing sales from low-end Wuliangye (target to achieve Rmb10bn in 2018), and higher portion of high price Wuliangye.
- The listed-co: to achieve Rmb60bn sales by the end of 13th five year plan (2020), including Rmb40bn for main stream Wuliangye and Rmb20bn for low end Wuliangye.
- The group: to achieve Rmb100bn sales by 2020. Management also shows its confidence in achieving the target earlier than the plan. Liquor segment will accounts for 2/3 of the total sales.

2. To invest in channels, brandings and products

- Channels: through “a hundreds of city, a thousands of country, and ten thousands of stores” program, increase its penetration in blank regions. By the end of 2017, it has built up 7000 core POS and 1000 Wuliangye specialty stores. It targets to increase to 8000 core POS and 1500 specialty stores in 2018.
- Branding: to increase investment in online marketing and interactions with consumers.
- Products: it will streamline the SKU portfolios and enhance the “1+3” system. The “1” refers to mainstream Wuliangye. The “3” categories include 1) super high end portfolios targeting in premium consumers, i.e. customized Wuliangye and Chinese zodiac Wuliangye; 2) the mild liquors targeting in younger consumers; and 3) international version of Wuliangye.

3. Selling expense ratio to stabilize and decline in next few years

- It will continue to implement comprehensive cost management. Through detail budget management and cost control, the management expects selling expense ratio to stabilize and decline in next few years

4. Positive in liquor industry trend in 2018.

- Management is optimistic and prudent in high end liquor sector, and believes it could be a bit more optimistic than prudent.
- The key industry driver will be consumers’ trading up, recovering macroeconomic, and increasing international demand from “one belt one road” program.
- Meanwhile, the high end liquor sector will continue to gain market share from low end sector on consumers’ trading up.



Revising up earnings 12-42% in 2018-20

For 2018, we forecast 31% sales growth, which is largely in line with management guidance, factoring 18% volume growth for mainstream products, 12% price increase from product mix, and 33% sales growth from low end mass products. Meanwhile, we expect Wuliangye's net margin to expand in 2018, helped by increasing portion of super premium products, lower channel subsidies and operating leverage.

For 2019-20E, we are revising up our earnings forecast by 26%-42% to factor in

- Higher sales volume of mainstream Wuliangye, helped by management's increasing investment in channel and branding; meanwhile, Moutai's price hike also expand high end liquor's market.
- Increasing sales from mass market SKUs, as the company will allocate more marketing resources to the categories.
- 6-10% annual price increase driven by mix upgrade and price hike

Figure 6: Sales and growth forecast

Sales	2014	2015	2016	2017E	2018E	2019E	2020E
Wuliangye	15,626	15,507	17,416	22,432	29,646	37,161	45,300
Volume (tons)	13,075	13,729	14,004	15,684	18,507	21,283	24,476
ASP (Rmb thousands/ton)	1,195	1,130	1,244	1,430	1,602	1,746	1,851
Mid-low end liquors	4,399	4,839	5,288	6,206	8,273	9,653	11,272
non-liquors	986	1,313	1,839	1,448	1,593	1,752	1,840
Total gross sales	21,011	21,659	24,544	30,086	39,512	48,567	58,412
YoY growth	2014	2015	2016	2017E	2018E	2019E	2020E
Wuliangye (mainstream)	-10%	-1%	12%	29%	32%	25%	22%
volume	-13%	5%	2%	12%	18%	15%	15%
ASP (Rmb thousands/ton)	-10%	-1%	12%	29%	32%	25%	22%
Mid-low end liquors	-31%	10%	9%	17%	33%	17%	17%
non-liquors	-3%	33%	40%	-21%	10%	10%	5%
Total gross sales	-15%	3%	13%	23%	31%	23%	20%

Source: company data; Deutsche Bank estimates

Figure 7: Earnings forecast change

RMBm	New			Old			Change		
	2018E	2019E	2020E	2018E	2019E	2020E	2018E	2019E	2020E
Gross sales	39,512	48,567	58,412	35,227	39,989	43,739	12.2%	21.5%	33.5%
Net sales	33,980	41,767	50,234	30,295	34,390	37,615	12.2%	21.5%	33.5%
Gross profit	24,538	30,980	37,754	21,714	24,725	27,038	13.0%	25.3%	39.6%
Core EBIT	15,982	20,455	25,497	14,085	16,059	17,559	13.5%	27.4%	45.2%
Net profit	12,338	15,799	19,657	10,961	12,583	13,821	12.6%	25.6%	42.2%
GPM	62.1%	63.8%	64.6%	61.6%	61.8%	61.8%	0.5%	2.0%	2.8%
EBITM	40.4%	42.1%	43.7%	40.0%	40.2%	40.1%	0.5%	2.0%	3.5%
NPM	31.2%	32.5%	33.7%	31.1%	31.5%	31.6%	0.1%	1.1%	2.1%

Source: Deutsche Bank estimate

Figure 8: DB estimate vs consensus

RMBm	DBe			Consensus			Diff		
	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
Gross sales	30,086	39,512	48,567	29,735	36,139	43,172	1.2%	9.3%	12.5%
Net profit	9,213	12,338	15,799	8,970	11,319	13,834	2.7%	9.0%	14.2%

Source: Deutsche Bank estimate, Wind



Revising up target price to Rmb98; reiterating buy

Based on new earnings forecast, we are revising up target price by 40% to Rmb98 base on DCF model, factoring in 9.5% WACC (3.9% RFR, 5.6% ERP, 1.0 beta, debt-free structure) and a 2% terminal growth rate (in line with long term inflation rate). **We reiterate Buy on the stock.** Our target price implies 27x P/E with 29% earnings CAGR in 2018-20, we think this is reasonable given:

- Our target P/E is slightly lower than 30x 2018 P/E for China liquor sector;
- Wuliangye currently trades at 10% discount to Moutai's due to its weaker branding (Figure 11). Our target 27x P/E is also 10% discount compared to our 30x target P/E on Moutai.

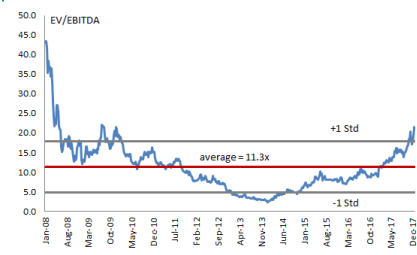
We are changing valuation methodology from EV/EBITDA to DCF approach, because 1) we believe DCF approach could incorporate Wuliangye's long-term growth, as we expect the company to maintain 20% earnings CAGR in 2017-20 helped by its investment in channels and brandings; 2) DCF approach could also incorporate Wuliangye's increasing cash flow generating capabilities; with increasing branding powers, Wuliangye's working capital is improving as it require increasing number of distributors to make advance payment before delivery. **Downside risk:** channel de-stocking in high-end liquor sector; food safety; worse than expected macro fixed asset investment slow down.

Figure 9: 1-year forward PE



Source: Deutsche Bank, Bloomberg Finance LP

Figure 10: EV/EBITDA



Source: Source: Deutsche Bank, Bloomberg Finance LP

Figure 11: Peer comp

Company	Ticker	Recom	Listing Curr	Price	Wkt Cap US\$m	PE (x)		PB (x)		EV/EBITDA		Div Yield (%)	
						Hist	FY1Y FY2Y	Hist	FY1Y FY2Y	Hist	FY1Y FY2Y	Hist	FY1Y FY2Y
Kweichow Moutai	600519.SS	Buy	CNY	715.86	138,337	20.7	34.2 28.0	5.8 9.9 8.3	12.1 21.9 17.4	2.5 1.6 1.9			
Wuliangye Yibin	000858.SZ	Buy	CNY	80.90	47,242	17.4	33.2 24.8	2.8 5.8 5.1	9.2 21.2 15.1	2.9 1.5 2.0			
Jiangsu Yanghe	002304.SZ	NR	CNY	115.25	26,718	18.2	25.7 21.6	4.1 5.9 5.1	12.0 18.5 15.7	1.8 2.0 2.4			
Luzhou Laojiao	000568.SZ	NR	CNY	66.40	14,962	24.0	37.5 28.3	4.2 7.3 6.5	17.2 26.0 19.5	1.4 1.4 2.1			
Xinghuacun Fen Wine	600809.SS	NR	CNY	56.67	7,548	35.8	47.7 32.0	4.6 9.1 7.6	19.7 28.1 20.0	1.0 1.1 1.6			
Anhui Gujing Distillery	000596.SZ	NR	CNY	68.44	4,723	27.6	31.7 25.1	4.1 5.4 4.6	17.8 17.8 14.8	0.9 1.0 1.2			
Anhui Yingjia Distillery	603198.SS	NR	CNY	17.76	2,186	25.4	19.9 17.4	4.4 3.5 3.2	16.6 14.2 12.6	3.4 N/A N/A			
Sichuan Swellfun	600779.SS	NR	CNY	46.30	3,480	41.5	64.5 36.9	6.4 13.4 10.5	30.4 41.7 24.8	1.0 0.7 1.1			
Tuopai Shede	600702.SS	NR	CNY	45.51	2,361	95.0	88.4 39.1	3.3 5.7 4.7	29.8 37.1 18.7	0.2 0.1 0.4			
Zhejiang Guyuelongshan	600059.SS	NR	CNY	9.38	1,167	68.3	50.4 42.6	2.1 1.9 1.9	34.0 28.0 25.7	1.1 0.9 1.1			
Jiugui Liquor	000799.SZ	NR	CNY	27.56	1,378	61.4	52.3 35.7	3.6 4.4 4.0	38.6 33.0 22.4	0.4 N/A N/A			
Xinjiang Yilite	600197.SS	NR	CNY	23.52	1,596	23.1	29.3 23.2	3.3 4.5 3.9	11.9 N/A N/A	1.1 1.1 1.2			
Average							38.2 42.9 29.5	4.0 6.4 5.4	20.8 26.1 18.8	1.5 1.1 1.5			

Source: Deutsche Bank, Bloomberg Finance LP. Stock price is on 3 Jan 2018. We use DB estimates for those companies we covered and Bloomberg consensus for other companies.



Model updated: 03 January 2018

Running the numbers

Asia
China
Alcohol & Tobacco

Wuliangye Yibin

Reuters: 000858.SZ Bloomberg: 000858 CH

Buy

Price (3 Jan 18) CNY 80.90

Target Price CNY 98.00

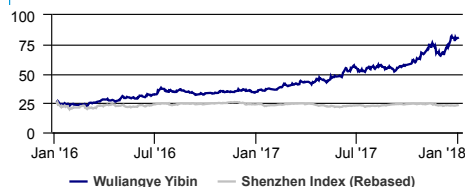
52 Week range CNY 35.45 - 82.15

Market cap (m) CNYm 307,094
USDm 47,232

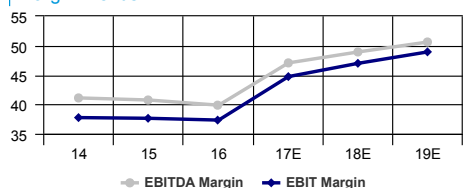
Company Profile

Wuliangye Yibin is China's leading local spirit brand/producer. Major brands under the company include "Wuliangye", "Wuliang Spring", "Wuliangchun" and "Jianzhuang".

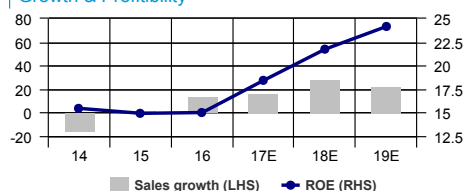
Price Performance



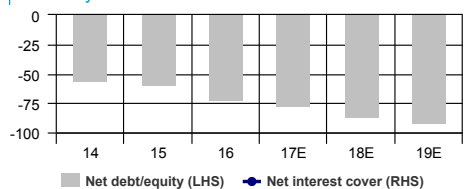
Margin Trends



Growth & Profitability



Solvency



Mark Yuan

+852 2203 6181

mark.yuan@db.com

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

Financial Summary

DB EPS (CNY)	1.54	1.63	1.79	2.43	3.25	4.16
Reported EPS (CNY)	1.54	1.63	1.79	2.43	3.25	4.16
DPS (CNY)	0.60	0.80	0.90	1.22	1.64	2.10
BVPS (CNY)	10.4	11.4	12.4	13.9	16.0	18.5
Weighted average shares (m)	3,796	3,796	3,796	3,796	3,796	3,796
Average market cap (CNYm)	65,945	95,934	117,781	307,094	307,094	307,094
Enterprise value (CNYm)	43,563	69,610	83,115	265,436	253,095	240,914

Valuation Metrics

P/E (DB) (x)	11.3	15.5	17.4	33.3	24.9	19.4
P/E (Reported) (x)	11.3	15.5	17.4	33.3	24.9	19.4
P/BV (x)	2.07	2.39	2.78	5.81	5.07	4.38
FCF Yield (%)	0.6	6.6	9.7	3.4	5.5	6.0
Dividend Yield (%)	3.5	3.2	2.9	1.5	2.0	2.6
EV/Sales (x)	2.2	3.5	3.7	10.0	7.4	5.8
EV/EBITDA (x)	5.4	8.6	9.2	21.3	15.2	11.4
EV/EBIT (x)	5.9	9.3	9.9	22.4	15.8	11.8

Income Statement (CNYm)

Sales revenue	19,494	19,875	22,603	26,475	33,980	41,767
Gross profit	13,722	13,203	15,288	18,655	24,538	30,980
EBITDA	8,013	8,099	9,011	12,461	16,628	21,144
Depreciation	653	619	573	617	658	701
Amortisation	0	0	0	0	0	0
EBIT	7,360	7,480	8,438	11,844	15,970	20,443
Net interest income/(expense)	658	732	766	733	884	1,153
Associates/affiliates	14	34	33	33	33	33
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	-16	41	100	100	100	100
Profit before tax	8,016	8,287	9,337	12,711	16,988	21,730
Income tax expense	1,958	1,877	2,281	3,114	4,162	5,324
Minorities	223	234	272	384	487	607
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	5,835	6,176	6,785	9,213	12,338	15,799
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	5,835	6,176	6,785	9,213	12,338	15,799

Cash Flow (CNYm)

Cash flow from operations	795	6,691	11,697	10,829	17,502	19,021
Net Capex	-381	-394	-302	-420	-522	-627
Free cash flow	414	6,297	11,395	10,408	16,980	18,394
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-2,995	-2,457	-3,212	-3,416	-4,639	-6,213
Net inc/(dec) in borrowings	0	0	0	0	0	0
Other investing/financing cash flows	-800	103	159	0	0	0
Net cash flow	-3,381	3,942	8,342	6,992	12,341	12,181
Change in working capital	-6,004	-192	4,070	648	4,051	1,948

Balance Sheet (CNYm)

Cash and other liquid assets	22,382	26,324	34,666	41,658	53,999	66,180
Tangible fixed assets	6,061	5,902	5,724	5,532	5,402	5,336
Goodwill/intangible assets	423	413	404	393	380	364
Associates/investments	869	903	796	829	863	896
Other assets	16,674	19,004	20,584	21,409	21,058	22,610
Total assets	46,409	52,547	62,174	69,821	81,702	95,387
Interest bearing debt	0	0	0	0	0	0
Other liabilities	6,076	8,201	13,969	15,435	19,129	22,621
Total liabilities	6,076	8,201	13,969	15,435	19,129	22,621
Shareholders' equity	39,430	43,329	47,077	52,873	60,572	70,158
Minorities	903	1,016	1,129	1,513	2,000	2,607
Total shareholders' equity	40,333	44,345	48,206	54,386	62,573	72,766
Net debt	-22,382	-26,324	-34,666	-41,658	-53,999	-66,180

Key Company Metrics

Sales growth (%)	-14.8	2.0	13.7	17.1	28.3	22.9
DB EPS growth (%)	-26.9	5.8	9.9	35.8	33.9	28.0
EBITDA Margin (%)	41.1	40.7	39.9	47.1	48.9	50.6
EBIT Margin (%)	37.8	37.6	37.3	44.7	47.0	48.9
Payout ratio (%)	39.0	49.2	50.4	50.4	50.4	50.4
ROE (%)	15.5	14.9	15.0	18.4	21.8	24.2
Capex/sales (%)	2.1	2.0	1.4	1.6	1.5	1.5
Capex/depreciation (x)	0.6	0.6	0.5	0.7	0.8	0.9
Net debt/equity (%)	-55.5	-59.4	-71.9	-76.6	-86.3	-90.9
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Securities estimates



Appendix 1

Important Disclosures

*Other information available upon request

Disclosure checklist			
Company	Ticker	Recent price*	Disclosure
Wuliangye Yibin	000858.SZ	80.90 (CNY) 3 Jan 2018	NA

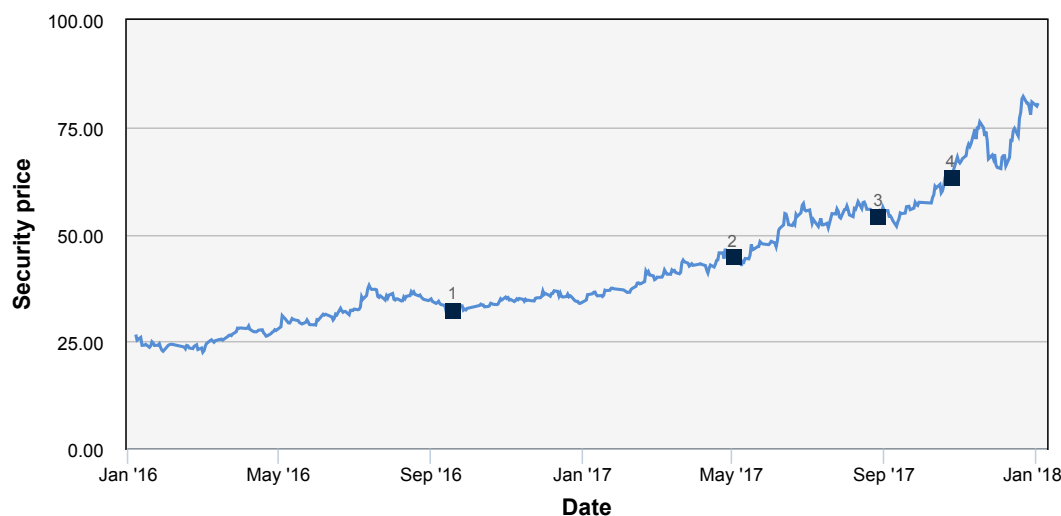
*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <http://gm.db.com/ger/disclosure/DisclosureDirectory.eqr>. Aside from within this report, important conflict disclosures can also be found at <https://gm.db.com/equities> under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

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Historical recommendations and target price. Wuliangye Yibin (000858.SZ)

(as of 01/03/2018)



Current Recommendations

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

** Analyst is no longer at Deutsche Bank

1.	09/19/2016	Buy, Target Price Change CNY 46,30	Charlie Chen**	3.	08/28/2017	Buy, Target Price Change CNY 62,00	Mark Yuan
2.	05/03/2017	Buy, Target Price Change CNY 55,00	Charlie Chen**	4.	10/26/2017	Buy, Target Price Change CNY 70,00	Mark Yuan



Equity Rating Key

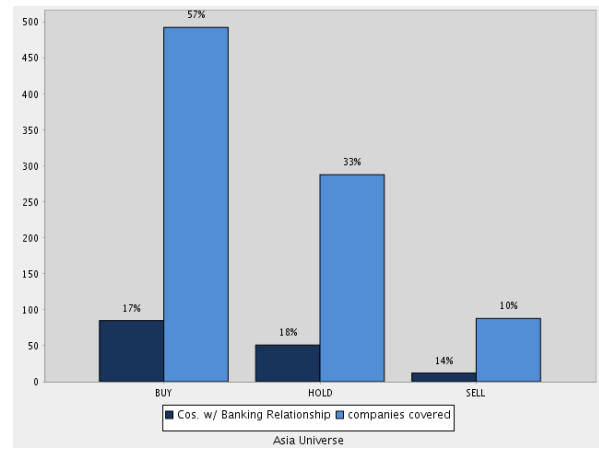
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Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock.

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David Folkerts-Landau

Group Chief Economist and Global Head of Research

Raj Hindocha
Global Chief Operating Officer
Research

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Deutsche Bank AG

Deutsche Bank Place
Level 16
Corner of Hunter & Phillip Streets
Sydney, NSW 2000
Australia
Tel: (61) 2 8258 1234

Deutsche Bank AG

Mainzer Landstrasse 11-17
60329 Frankfurt am Main
Germany
Tel: (49) 69 910 00

Deutsche Bank AG

Filiale Hongkong
International Commerce Centre,
1 Austin Road West, Kowloon,
Hong Kong
Tel: (852) 2203 8888

Deutsche Securities Inc.

2-11-1 Nagatacho
Sanno Park Tower
Chiyoda-ku, Tokyo 100-6171
Japan
Tel: (81) 3 5156 6770

Deutsche Bank AG London

1 Great Winchester Street
London EC2N 2EQ
United Kingdom
Tel: (44) 20 7545 8000

Deutsche Bank Securities Inc.

60 Wall Street
New York, NY 10005
United States of America
Tel: (1) 212 250 2500
