Deutsche Bank
Research

Rating
Hold

Asia
China

Consumer
Retail / Wholesale Trade

Company
Shanghai Jahwa

Reuters	Bloomberg	Exchange	Ticker
600315.SS	600315 CH	SHH	600315

Date
17 July 2018

Company Update

Price at 11 Jul 2018 (CNY)	38.17
Price target - 12mth (CNY)	39.22
52-week range (CNY)	46.34 - 29.83
Shanghai Composite	2,827

2Q18 preview ; maintaining Hold

Valuation & Risks
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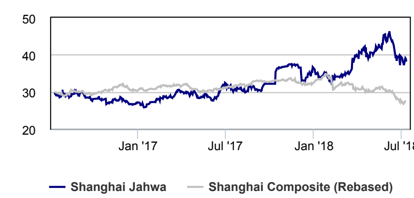
Jahwa to announce its interim results on 22 Aug 2018

We expect Jahwa's sales/NP will likely grow 40%/77% in 2Q18, this indicates 23%/56% growth for 1H sales/NP growth. 2Q18 has an easier comp due to ecommerce shortfall in 2Q17 as a result of business model transformation. We believe the recovery trend of its major brands has continued in 2Q18.

- **Herborist** is expected to see an acceleration in 2Q with single digit growth in volume in department store (50% of brand sales), in our view. The growth is mainly driven by new product launch in March and May. ASP also saw a solid growth. Major provinces including Henan, Shandong and Anhui led the growth. It also strictly controlled its retail discount thanks to a better channel control vs before. To recap, even newly launched products were sold at discount in old days. This situation has been largely changed according to the mgmt. As for its online business, it still needs to beef up its sales growth. To recap, most of its online sales come from its Tmall flagship store and it has changed from wholesale model to brand agency model. We believe management is still working on improving performance of its online operation, for example narrowing the ASP gap between its online and offline operations.
- **Liushen** saw solid growth (we believe mid single digit) in 2Q (high season for Liushen), partially thanks to several successful digital marketing campaigns such as Douyin.
- **Maxiam** also saw acceleration in sales growth in 2Q, thanks to a good performance in hypermarket/supermarkets. Its sun protection series has been selling well.
- **GF** has struggled with a negative growth in 1H18. It faces keen competition in the CS channel (key channel for GF) resulting in steeper promotions. Moreover, CS channel in general saw a slowdown ytd.
- **Giving**'s performance is within expectation in both mother's store and hypermarkets.
- It has ramped up all the network coverage (mainly mothers' store and online) for its newly acquired brand **TT**. It currently is focusing on increasing per store productivity.

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-12.5	-7.7	20.9
Shanghai Composite	-7.4	-11.9	-11.7

Source: Deutsche Bank

Key indicators (FY1)	
ROE (%)	9.8
Net debt/equity (%)	-12.5
Book value/share (CNY)	8.53
Price/book (x)	4.5
Net interest cover (x)	31.1
Operating profit margin (%)	9.2

Source: Deutsche Bank

New manufacturing capacity

It announced on 30 June that some of production lines (mainly non liquid products) has commenced operation since June, which indicates it will start to book D&A cost from June. According to the company's initial calculation, it expects the new manufacture will generate additional RMB25m D&A expense in 2018. We currently forecast full year D&A should increase 34% to RMB248, which accounts for 3.4% of 2018 sales (DBe) vs 2.9% in 2017.

In terms of industry landscape, Jahwa commented that:

- **Korean brands' growth momentum has tapered off significantly.** These days, the trend turns towards western brands and Japanese brands.
- As mentioned above, CS stores, which is one of the major channel for cosmetics products sales in lower tier cities **saw sales growth slowdown this year**. Instead, single brand store are getting more popular these days.
- There is still a **big gap between Tier 1/2 cities and lower tier cities** in terms of cosmetics consumption behaviour, e.g. brand recognition, channels, purchasing power. While local brands including Herborist are more popular in lower tier cities.

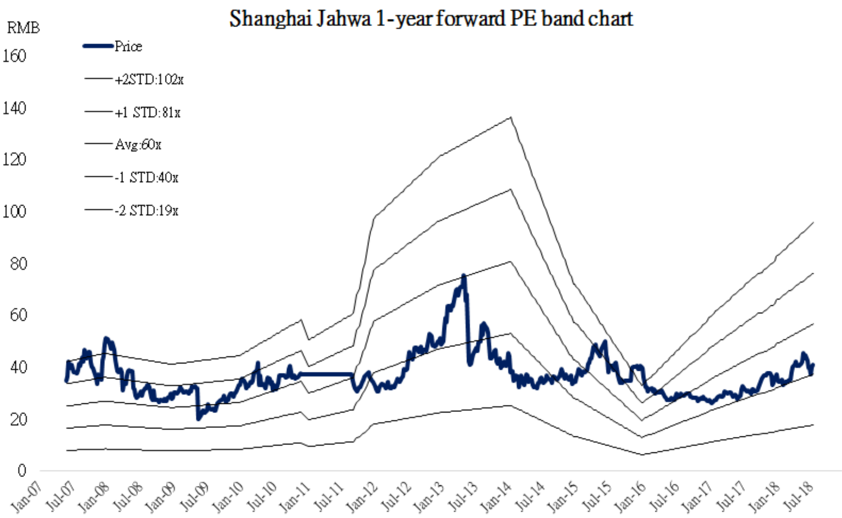
To recap, the company' share option intensive plan suggested it plans to achieve 23%/41% growth for sales/NP 2018 and 24%/29% three-year sales/NP CAGR from 2017-2020 according to the share option plan announced in Mar 2018. We forecast sales/NP should see 14%/40% growth in 2018. We maintain Hold recommendation.

Figure 1: Quarterly forecast

YE Dec RMBm P&L adjusted for model	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18e	3Q18e	4Q18e
Sales (net)	**1,527**	**1,510**	**1,212**	**1,018**	**1,325**	**1,299**	**1,230**	**907**	**1,844**	**1,817**	**1,752**	**1,951**
Sales yoy%	*-3.5%*	*-6.0%*	*-12.8%*	*-16.2%*	*-13.2%*	*-14.0%*	*1.5%*	*-10.9%*	*39.1%*	*39.8%*	*42.5%*	*115.1%*
COGS (ex dep)	(618)	(582)	(473)	(388)	(370)	(431)	(391)	(538)	(619)	(619)	(610)	(858)
Gross Profit	**909**	**928**	**738**	**630**	**955**	**868**	**838**	**369**	**1,225**	**1,197**	**1,142**	**1,093**
GP Margin %	*59.5%*	*61.5%*	*60.9%*	*61.9%*	*72.1%*	*66.8%*	*68.2%*	*40.7%*	*66.4%*	*65.9%*	*65.2%*	*56.0%*
GP yoy%	*-5.3%*	*-3.8%*	*-8.8%*	*-8.2%*	*5.0%*	*-6.4%*	*13.5%*	*-41.5%*	*28.3%*	*37.9%*	*36.3%*	*196.5%*
Other income/expense	(4)	17	2	45	11	16	23	7	24	10	(2)	23
Opex	(774)	(679)	(659)	(920)	(859)	(759)	(752)	(403)	(1,075)	(972)	(999)	(981)
EBIT	**132**	**266**	**81**	**(245)**	**107**	**126**	**108**	**(28)**	**174**	**235**	**142**	**135**
EBIT margin %	*8.6%*	*17.6%*	*6.7%*	*-24.1%*	*8.1%*	*9.7%*	*8.8%*	*-3.1%*	*9.4%*	*13.0%*	*8.1%*	*6.9%*
EBIT yoy%	*-23.7%*	*-44.6%*	*-37.2%*	*na*	*-18.7%*	*-52.5%*	*33.2%*	*na*	*na*	*na*	*na*	*na*
Finance cost (net)	9	29	9	22	10	9	8	(49)	(21)	(5)	(1)	5
Operating profit	**141**	**294**	**91**	**(224)**	**117**	**135**	**116**	**(77)**	**153**	**230**	**141**	**140**
Associate	7	0	(5)	(13)	4	(2)	(12)	20	29	5	4	(24)
Exceptionals	0	0	0	0	0	0	0	0	0	1	2	3
Pre-tax Profit	**148**	**294**	**85**	**(237)**	**121**	**134**	**104**	**(57)**	**182**	**236**	**147**	**119**
Taxation	(20)	(49)	(24)	19	(12)	(26)	(18)	(13)	(32)	(45)	(25)	(19)
Post Tax Profits	**127**	**245**	**61**	**(217)**	**108**	**108**	**86**	**(71)**	**151**	**191**	**122**	**100**
Minority Interests	-	-	-	-	-	-	-	-	-	-	-	-
Core NP	**127**	**245**	**61**	**(217)**	**108**	**108**	**86**	**(71)**	**151**	**191**	**122**	**100**
Core NP margin %	*8.3%*	*16.2%*	*5.0%*	*-21.4%*	*8.2%*	*8.3%*	*7.0%*	*-7.8%*	*8.2%*	*10.5%*	*6.9%*	*5.1%*
Core NP yoy%	*-32.9%*	*-45.7%*	*-59.2%*	*na*	*-15.0%*	*-55.9%*	*40.7%*	*na*	*39.2%*	*77.3%*	*41.7%*	*na*

Source: Deutsche Bank, Company data

Figure 2: One year forward PE band



Source: Company data, Bloomberg Finance LP, closing price as of 17 July 2018

Forecasts and ratios

Year End Dec 31	2016A	2017A	2018E	2019E	2020E
Sales (CNYm)	5,266.3	6,430.6	7,305.8	8,350.6	9,681.1
EBITDA (CNYm)	372.8	672.7	918.8	1,084.4	1,245.6
Reported NPAT (CNYm)	216.0	389.8	543.7	701.3	823.7
Reported EPS FD(CNY)	0.32	0.58	0.81	1.04	1.22
DB EPS FD(CNY)	0.32	0.58	0.81	1.04	1.22
DB EPS growth (%)	-90.2	81.2	39.2	28.9	17.5
PER (x)	91.0	53.6	47.3	36.7	31.2
EV/EBITDA (x)	42.8	25.1	23.0	18.9	15.8
DPS (net) (CNY)	0.10	0.18	0.25	0.32	0.48
Yield (net) (%)	0.3	0.6	0.7	0.8	1.3

Source: Deutsche Bank estimates, company data

Appendix 1

Important Disclosures

*Other information available upon request

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Company	Ticker	Recent price*	Disclosure
Shanghai Jahwa	600315.SS	40.51 (CNY) 16 Jul 2018	NA

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Historical recommendations and target price. Shanghai Jahwa (600315.SS)

(as of 07/11/2018)

1. 08/16/2016 Hold, Target Price Change CNY 24.70 Anne Ling
2. 03/24/2017 Hold, Target Price Change CNY 31.60 Anne Ling
3. 06/28/2017 Hold, Target Price Change CNY 32.30 Anne Ling
4. 08/16/2017 Hold, Target Price Change CNY 30.04 Anne Ling
5. 03/22/2018 Hold, Target Price Change CNY 39.22 Anne Ling

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Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock.
Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

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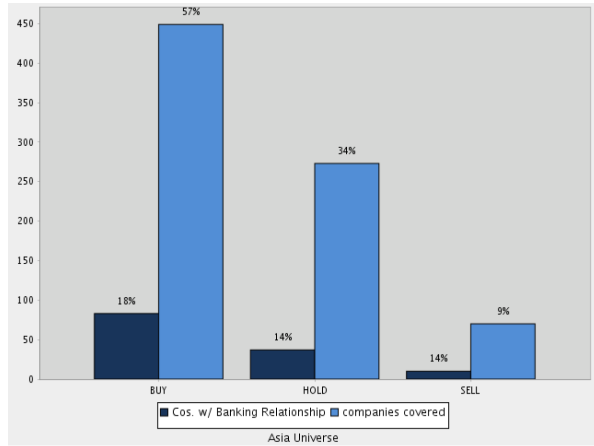

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