

China
ADD

Consensus ratings*: Buy 40 Hold 1 Sell 1

Current price:	Rmb1,170
Target price:	Rmb1,328
Previous target:	Rmb1,328
Up/downside:	13.5%
CGI / Consensus:	12.7%

Reuters:	600519.SS
Bloomberg:	600519 CH
Market cap:	US\$207,569m
	Rmb1,469,751m
Average daily turnover:	US\$484.6m
	Rmb3,473m
Current shares o/s:	1,256m
Free float:	36.0%

*Source: Bloomberg

Key changes in this note

➤ No changes



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	6.5	20.9	75.4
Relative (%)	8.2	19.5	58.4

Major shareholders	% held
Kweichow Moutai Group	62.0

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Kweichow Moutai

Direct sales continue to increase

- Moutai's distribution channel changes are on track; the direct sales contribution improved to 7% in 3Q19 from 4.1% in 1H19.
- We expect the direct sales contribution to further increase in 4Q19F. We also forecast that FY19F net profit will grow 23% yoy.
- We expect Moutai to supply 1Q20 volume to the market ahead of schedule to maintain no further hikes in the current first-layer wholesaler price.
- Maintain Add with an unchanged DCF-based TP of Rmb1,328 (WACC:10%)

Modest sales growth in 3Q19, but net profit growth in line

Moutai's baijiu sales grew 14% yoy in 3Q19, a bit slower than the 18% yoy in 1H19. But net profit grew 17% yoy in 3Q19, driven by a continuous mix upgrade, an increase in direct sales, and better control of expenses. Moutai's 9M19 baijiu sales grew by 17% yoy to Rmb61bn, and its net profit was up by 23% yoy to Rmb30.5bn, in line with our expectations. Moutai's distribution network changes are still ongoing; for the domestic distributors channel, Moutai has cut 616 Moutai brand distributors year to date to 2,401 distributors; and the direct sales channel build-up is on track. The direct sales contribution improved to 7% in 3Q19 from 4.1% in 1H19. We expect Moutai to accelerate its supply volume to direct sales channels in 4Q19 and forecast that its FY19F net profit will grow 23% yoy.

Continually improving margin owing to a product structure upgrade

Moutai's 9M19 gross profit margin was 91.5%, up by 0.4%pts, due to a product structure upgrade. Its sales tax was down by 2%pts to 13%. The S&D expenses ratio fell by 1.2%pts to 4.3%, because of a decrease in the promotion of the Series brand. Moutai's net profit margin improved by 2.6%pts to 50% in 9M19. With direct sales improving and continuous upgrading of its product structure, we expect Moutai's profitability to further improve in FY20F.

Controlled price hikes to stimulate consumption

Moutai had direct sales of Rmb3.1bn in 9M19; its sales contribution improved to 5.1% in 9M19, from 4.1% in 1H19. In Sep 2019, Moutai increased its direct sales collaboration with hypermarket and ecommerce channels, supplying 600t of Moutai liquor to three hypermarkets – Wumart, Sun Art and China Resources – and 400t to two online platforms – Suning and Tmall. Moutai also announced the advance supply of 4Q19 volume to its distributors. These actions have had a positive impact in bringing down Moutai's first-tier wholesaler price in the distributors channel from a peak of Rmb2,700 per bottle to Rmb2200–2300 per bottle now. In 2020, Chinese New Year will be in Jan, slightly earlier than last year. To satisfy high customer demand and stabilize its wholesale price, we expect Moutai to execute its 1Q20 supply volume ahead of schedule, possibly in 4Q19, which will benefit its Q419F sales growth.

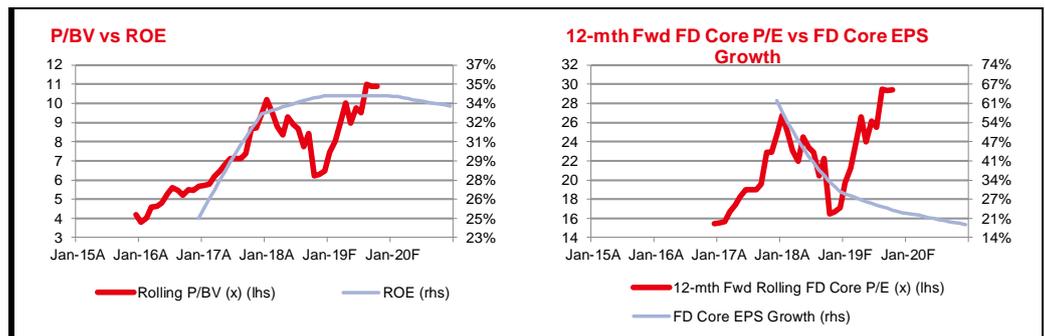
Maintain Add with an unchanged DCF-based TP of Rmb1,328

We maintain our Add rating, because of strong earnings growth, driven by Moutai's channel reforms and a product mix upgrade. Moutai is currently trading at 34x FY19F, 1.7 s.d. above its historical average P/E of 19x since listing. Potential positive catalysts including a potential ex-factory price hike in 2020, and margin improvement from the increase in direct sales. Downside risks include a reduction in high-end baijiu consumption because of the worsening economic environment.

Financial Summary

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue (Rmbm)	58,218	73,639	84,775	98,351	112,040
Operating EBITDA (Rmbm)	39,992	52,506	63,821	75,531	87,662
Net Profit (Rmbm)	27,079	35,204	43,189	51,198	59,499
Core EPS (Rmb)	21.60	28.07	34.43	40.81	47.41
Core EPS Growth	61.8%	29.9%	22.7%	18.5%	16.2%
FD Core P/E (x)	54.16	41.68	33.98	28.67	24.68
DPS (Rmb)	11.00	14.54	17.84	21.14	24.57
Dividend Yield	0.94%	1.24%	1.52%	1.81%	2.10%
EV/EBITDA (x)	34.93	26.16	21.20	17.58	14.80
P/FCFE (x)	49.14	36.14	34.91	28.56	23.97
Net Gearing	(80.6%)	(85.7%)	(85.5%)	(86.1%)	(87.3%)
P/BV (x)	16.07	13.03	10.67	8.82	7.37
ROE	33.0%	34.5%	34.5%	33.7%	32.5%
% Change In Core EPS Estimates				1.00	0.99
CGI/consensus EPS (x)					0.99

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS

Profit & Loss

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Total Net Revenues	60,927	77,073	89,168	103,709	118,574
Gross Profit	46,583	59,261	70,358	82,870	95,619
Operating EBITDA	39,992	52,506	63,821	75,531	87,662
Depreciation And Amortisation	-1,108	-1,166	-1,224	-1,370	-1,516
Operating EBIT	38,884	51,339	62,597	74,161	86,146
Financial Income/(Expense)	56	4	0	0	0
Pretax Income/(Loss) from Assoc.	0	0	0	0	0
Non-Operating Income/(Expense)	-200	-515	-240	-240	-240
Profit Before Tax (pre-EI)	38,821	50,908	62,440	74,004	85,989
Exceptional Items					
Pre-tax Profit	38,740	50,828	62,357	73,921	85,906
Taxation	-9,734	-12,998	-15,946	-18,904	-21,968
Exceptional Income - post-tax					
Profit After Tax	29,006	37,830	46,411	55,017	63,937
Minority Interests	-1,927	-2,626	-3,222	-3,819	-4,438
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	27,079	35,204	43,189	51,198	59,499
Recurring Net Profit	27,140	35,263	43,251	51,260	59,561
Fully Diluted Recurring Net Profit	27,140	35,263	43,251	51,260	59,561

Cash Flow

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
EBITDA	39,992	52,506	63,821	75,531	87,662
Cash Flow from Invt. & Assoc.					
Change In Working Capital	-8,318	2,025	-2,734	-2,134	-2,146
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	-640	-12,254	-16,186	-19,144	-22,208
Net Interest (Paid)/Received	0	0	0	0	0
Tax Paid					
Cashflow From Operations	31,034	42,276	44,901	54,254	63,307
Capex	-1,125	-1,607	-2,800	-2,800	-2,000
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow					
Cash Flow From Investing	-1,125	-1,607	-2,800	-2,800	-2,000
Debt Raised/(repaid)					
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	-8,905	-16,441	-18,264	-22,406	-26,562
Preferred Dividends					
Other Financing Cashflow	6	0	0	0	0
Cash Flow From Financing	-8,899	-16,441	-18,264	-22,406	-26,562
Total Cash Generated	21,009	24,228	23,837	29,047	34,746
Free Cashflow To Equity	29,909	40,669	42,101	51,454	61,307
Free Cashflow To Firm	29,909	40,669	42,101	51,454	61,307

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS... cont'd
Balance Sheet

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Total Cash And Equivalents	87,869	112,075	135,912	164,959	199,705
Total Debtors	2,285	2,140	2,301	2,458	2,626
Inventories	22,057	23,507	26,228	30,428	34,663
Total Other Current Assets	38	140	140	140	140
Total Current Assets	112,249	137,862	164,581	197,985	237,134
Fixed Assets	15,244	15,249	16,907	18,420	18,987
Total Investments	62	65	65	65	65
Intangible Assets	3,459	3,499	3,416	3,333	3,250
Total Other Non-Current Assets	3,596	3,172	3,172	3,172	3,172
Total Non-current Assets	22,361	21,985	23,561	24,991	25,475
Short-term Debt	10,463	11,473	11,473	11,473	11,473
Current Portion of Long-Term Debt					
Total Creditors	28,112	30,965	31,113	33,336	35,594
Other Current Liabilities					
Total Current Liabilities	38,575	42,438	42,586	44,809	47,067
Total Long-term Debt					
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	16	0	0	0	0
Total Non-current Liabilities	16	0	0	0	0
Total Provisions	0	0	0	0	0
Total Liabilities	38,590	42,438	42,586	44,809	47,067
Shareholders' Equity	91,452	112,839	137,764	166,556	199,493
Minority Interests	4,568	4,570	7,792	11,611	16,049
Total Equity	96,020	117,408	145,555	178,166	215,542

Key Ratios

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue Growth	49.8%	26.5%	15.1%	16.0%	13.9%
Operating EBITDA Growth	58.9%	31.3%	21.6%	18.3%	16.1%
Operating EBITDA Margin	68.7%	71.3%	75.3%	76.8%	78.2%
Net Cash Per Share (Rmb)	61.6	80.1	99.1	122.2	149.8
BVPS (Rmb)	72.8	89.8	109.7	132.6	158.8
Gross Interest Cover	N/A	N/A	N/A	N/A	N/A
Effective Tax Rate	25.1%	25.6%	25.6%	25.6%	25.6%
Net Dividend Payout Ratio	50.9%	51.8%	51.8%	51.8%	51.8%
Accounts Receivables Days	6.39	4.42	3.43	4.13	4.15
Inventory Days	543.0	466.9	482.5	497.5	517.5
Accounts Payables Days	25.86	22.24	20.82	16.91	15.30
ROIC (%)	197%	277%	374%	353%	350%
ROCE (%)	40.4%	43.7%	43.8%	42.8%	41.4%
Return On Average Assets	23.5%	25.7%	26.7%	26.8%	26.4%

Key Drivers

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
ASP (% chg, main prod./serv.)	8.3%	16.3%	5.0%	4.8%	3.2%
Unit sales grth (% , main prod./serv.)	31.8%	7.5%	7.4%	7.8%	8.7%
Util. rate (% , main prod./serv.)	N/A	N/A	N/A	N/A	N/A
ASP (% chg, 2ndary prod./serv.)	27.4%	40.5%	30.0%	30.0%	20.0%
Unit sales grth (% ,2ndary prod/serv)	113.2%	-0.4%	3.0%	5.0%	3.0%
Util. rate (% , 2ndary prod/serv)	N/A	N/A	N/A	N/A	N/A
ASP (% chg, tertiary prod/serv)	N/A	N/A	N/A	N/A	N/A
Unit sales grth (% ,tertiary prod/serv)	N/A	N/A	N/A	N/A	N/A
Util. rate (% , tertiary prod/serv)	N/A	N/A	N/A	N/A	N/A
Unit raw mat ASP (%chg,main)	N/A	N/A	N/A	N/A	N/A
Total Export Sales Growth (%)	N/A	N/A	N/A	N/A	N/A
Export Sales/total Sales (%)	N/A	N/A	N/A	N/A	N/A

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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We are transferring the rating mechanism from "BUY, SELL, HOLD" to "ADD, REDUCE, HOLD". Please refer to the definitions below.

Explanation on Equity Ratings (Existing mechanism (will be replaced by new mechanism by 01/09/19))

BUY : share price will increase by >20% within 12 months in absolute terms

SELL : share price will decrease by >20% within 12 months in absolute terms

HOLD : no clear catalyst, and downgraded from BUY pending clearer signal to reinstate BUY or further downgrade to outright SELL

Explanation on Equity Ratings (New mechanism)

ADD : The stock's total return is expected to exceed 10% over the next 12 months.

REDUCE : The stock's total return is expected to fall below 0% or more over the next 12 months.

HOLD : The stock's total return is expected to be between 0% and positive 10% over the next 12 months.

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