

## Company Report

### Xtep International (1368 HK)

#### Better-than-expected 2Q22 retail sales

- 2Q22 retail sales grew by mid-teens pts, better than expected
- Maintain FY22 revenue growth guidance at 25%-30% yoy
- Maintain BUY and raise TP to HKD16.0

#### 2Q22 retail sales growth ahead of expectations

Xtep announced that 2Q22 retail sales (incl. offline and online channels) grew by mid-teens pts yoy, compared to the 30%-35% yoy increase in 1Q22. The growth was ahead of expectations as COVID restrictions led to a low-single digit yoy decline in April, which was followed by c.10% yoy growth in May and 30%-35% yoy growth in June.

#### Exceptional growth in new brands

The growth in retail sales of Saucony grew by over 100% yoy in 2Q22 and is expected to grow by over 50% yoy for FY22E. Although affected by supply chain issues in 2Q22, the overseas demand for K-Swiss and Palladium products were very strong. Xtep expects K-Swiss and Palladium retail sales to grow by at least 30% yoy in FY22E.

#### Healthy discount and inventory in 2Q22

The retail discount level in 2Q22 was 25%-30%, compared to the 25% in 1Q22 and the 25%-30% in 1Q21 and the 20%-25% in 2Q21. We believe the higher discount levels in 2Q22 reflected both the COVID situation as well as the low base of comparison in 2Q21 where there was strong demand due to the Xinjiang cotton situation. The retail inventory level was c. 4.5 months, slightly higher than the 4 months in 1Q22 and the estimated 4.2 months in 2Q22. Given the current inventory level is healthy, barring any major COVID restrictions in 2H22, Xtep expects the discount levels to continue to narrow.

#### Maintain its FY22 guidance of 25% - 30% yoy growth

Xtep issued a positive earnings alert for 1H22 with net earnings growing at least 35% yoy. Assuming no more major COVID lockdowns in 2H22, mgmt. is confident that it can achieve its previous GMV and revenue growth guidance of over 25% yoy and 25%-30% yoy respectively.

#### Maintain BUY. New TP of HKD16

We tweak our FY22/23/24 EPS forecasts by -0.9%, +1.6% and +4.3% respectively. We also increase our target price from HKD14 to HKD16. Our new target price implies a PE of 26.4x on our next 12 months' forward EPS (previous 25x FY22 EPS), with an implied PEG of 0.9x. Maintain BUY. **Key catalysts:** Sooner-than-expected breakeven for new brands. **Key risks:** More large scale COVID lockdowns.

#### Financials

Year ended 31 Dec (RMB mn)	2020	2021	2022E	2023E	2024E
Revenue	8,172	10,013	12,772	16,340	20,676
yoy growth	-0.1%	22.5%	27.5%	27.9%	26.5%
Attributable net profit	513	908	1,160	1,522	1,950
Adj. EPS (RMB)	0.21	0.36	0.45	0.60	0.76
yoy growth	-31.6%	72.0%	27.7%	31.3%	28.1%
P/E	57.0x	33.1x	26.0x	19.8x	15.4x
ROE	7.2%	11.9%	14.1%	17.4%	20.2%
Net debt (cash)/ equity	-18.0%	-17.4%	-20.6%	-13.0%	-9.8%
Div yield	1.0%	1.8%	2.2%	2.9%	3.8%

Sources: Company data, CMS (HK) estimates; share price as of Jul 13, 2022

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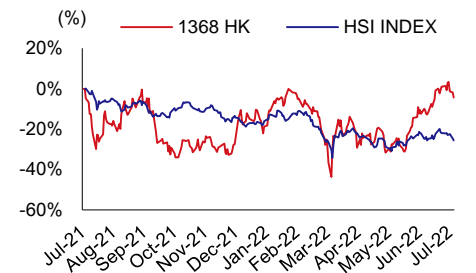
#### WHAT'S NEW

Xtep 2Q22 retail sales remained strong. Maintain BUY and lift TP to HKD 16.0

#### BUY

Previous	BUY
Price (Jul 13, 2022)	HKD 13.7
12-month Target Price (Potential up/downside)	HKD16.0 (+17.0%)
Previous	HKD14.0

#### Price Performance



Source: Bloomberg; share price as of Jul 13, 2022

%	1m	6m	12m
1368 HK	9.3	7.2	(3.0)
HSI	(1.3)	(14.9)	(25.6)

#### Sector: Consumer

Hang Seng Index (Jul 13, 2022)	20,798
HSCEI (Jul 13, 2022)	7,146

#### Key Data

52-week range (HKD)	8.08 - 14.98
Market cap (HKD mn)	36,045
Avg. daily volume (mn)	10.34
BVPS (RMB)	3.11

#### Shareholding Structure

Group Success Investments Ltd	50.0%
Ding Shui Po	2.3%
Free float	47.7%

Source: Bloomberg

#### Related Research

1. China Sportswear Sector - 2H22 Outlook: Sales should rebound; FY22 growth may still be met (OVERWEIGHT) (July 5, 2022)
2. Xtep International (1368 HK) - Retail sales rebound yoy in May and June (BUY) (Jun 14, 2022)

Figure 1: Xtep historical retail sales growth summary

	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22
Retail sell-through growth (%)	20%+	20%+	20%	20%+	-	-LSD	+5%	+5%-10%	+55%	+30%-35%	+15%	+20%-25%	+30-35%	+mid-teens
Retail discount	25%	20%-25%	22%-25%	20%-25%	30%-35%	30%-35%	30%-35%	30%-35%	25%-30%	20%-25%	20%-25%	20%-25%	c. 25%	25%-30%
Retail inventory turnover (months)	4.0	4.0	4.0	4.0	5.5	5.0-5.5	5.0	< 5.0	4.5	3.5-4.0	4.0	4.0	4.0	4.5

Sources: Company data, CMS (HK)

Figure 2: Key assumptions adjustment

Unit: RMB mn	2022E			2023E			2024E		
	Original	New	diff %	Original	New	diff %	Original	New	diff %
<b>Revenue</b>	<b>13,013</b>	<b>12,772</b>	<b>-1.9%</b>	<b>16,656</b>	<b>16,340</b>	<b>-1.9%</b>	<b>21,088</b>	<b>20,676</b>	<b>-2.0%</b>
Mass market (Xtep)	11,359	11,110	-2.2%	14,426	14,109	-2.2%	18,032	17,636	-2.2%
Athleisure (K-swiss, Palladium)	1,237	1,271	2.8%	1,546	1,589	2.8%	1,932	1,987	2.8%
Professional sports (Saucony, Merrell)	417	391	-6.3%	684	641	-6.3%	1,123	1,053	-6.2%
<b>GPM</b>	<b>41.9%</b>	<b>42.0%</b>	<b>0.0ppt</b>	<b>42.1%</b>	<b>42.1%</b>	<b>0.0ppt</b>	<b>42.2%</b>	<b>42.2%</b>	<b>0.0ppt</b>
Mass market (Xtep)	41.7%	41.7%	0.0ppt	41.9%	41.9%	0.0ppt	42.1%	42.1%	0.0ppt
Athleisure (K-swiss, Palladium)	44.7%	44.7%	0.0ppt	44.9%	44.9%	0.0ppt	44.1%	44.1%	0.0ppt
Professional sports (Saucony, Merrell)	40.6%	40.6%	0.1ppt	40.8%	40.8%	0.1ppt	41.0%	41.1%	0.1ppt
<b>OPM</b>	<b>13.3%</b>	<b>13.9%</b>	<b>0.6ppt</b>	<b>13.2%</b>	<b>14.1%</b>	<b>0.9ppt</b>	<b>12.9%</b>	<b>14.2%</b>	<b>1.3ppt</b>
<b>Attributable net profit</b>	<b>1,170</b>	<b>1,160</b>	<b>-0.9%</b>	<b>1,499</b>	<b>1,522</b>	<b>1.6%</b>	<b>1,869</b>	<b>1,950</b>	<b>4.3%</b>
NPM	9.0%	9.1%	0.1ppt	9.0%	9.3%	0.3ppt	8.9%	9.4%	0.6ppt
<b>Diluted EPS (RMB)</b>	<b>0.46</b>	<b>0.45</b>	<b>-0.9%</b>	<b>0.59</b>	<b>0.60</b>	<b>1.6%</b>	<b>0.73</b>	<b>0.76</b>	<b>4.3%</b>

Sources: Company data, CMS (HK) estimates

Figure 3: Target price and valuation table

Valuation - Xtep			
Stock price (HKD)	13.7		
HKD to RMB	0.86		
Price date	13/7/2022		
	FY22E	FY23E	FY24E
Year difference	1.0	2.0	3.0
EPS (RMB)	0.45	0.60	0.76
P/E	26.0x	19.8x	15.4x
EPS CAGR since FY21	27.7%	29.5%	29.0%
PEG	0.9x	0.7x	0.5x
<b>Target PE</b>	<b>26.4x</b>		
12-month fwd EPS, yoy growth	28.7%		
<b>Implied PEG</b>	<b>0.9x</b>		
12-month fwd EPS (RMB)	0.52		
<b>Target Price (HKD)</b>	<b>16.0</b>		
<b>Upside</b>	<b>17.0%</b>		
22E Div yield	2.2%		
<b>Total return</b>	<b>19.2%</b>		

Sources: Company data, Bloomberg, CMS (HK) estimates

## Financial statement

### Balance Sheet

RMB mn	2020	2021	2022E	2023E	2024E
PP&E	796	1,119	1,379	1,610	1,809
Right of use assets	429	668	672	676	680
Goodwill	787	756	756	756	756
Investment in associate/JV	34	144	132	156	180
Other non-current assets	1,498	1,496	1,490	1,483	1,476
<b>Non-current assets</b>	<b>3,544</b>	<b>4,183</b>	<b>4,430</b>	<b>4,681</b>	<b>4,902</b>
Inventories	975	1,497	1,580	2,016	2,549
Receivables and prepayments	4,143	4,972	5,603	7,159	9,051
Financial assets at FVTPL	0	0	0	0	0
Deposits	0	0	0	0	0
Bank Balances and Cash	3,472	3,930	4,278	3,721	3,538
Other current assets	437	33	33	33	33
<b>Current assets</b>	<b>9,027</b>	<b>10,432</b>	<b>11,494</b>	<b>12,929</b>	<b>15,171</b>
<b>Total assets</b>	<b>12,572</b>	<b>14,615</b>	<b>15,924</b>	<b>17,610</b>	<b>20,073</b>
Account Payable	1,479	2,352	2,356	3,005	3,801
Due to Related Parties	0	0	0	0	0
Bank Borrowings	642	405	405	405	405
Other current liabilities	1,213	1,296	1,668	2,071	2,565
<b>Current liabilities</b>	<b>3,334</b>	<b>4,053</b>	<b>4,430</b>	<b>5,482</b>	<b>6,771</b>
Deferred Tax Liabilities	237	253	253	253	253
Lease Liabilities	131	102	123	123	123
Bank Borrowing	1,516	2,133	2,133	2,133	2,133
Other Borrowing	-	-	-	-	-
Provision and other liabilities	55	92	531	542	557
<b>Non-current liabilities</b>	<b>1,939</b>	<b>2,580</b>	<b>3,040</b>	<b>3,052</b>	<b>3,066</b>
<b>Total liabilities</b>	<b>5,273</b>	<b>6,633</b>	<b>7,470</b>	<b>8,534</b>	<b>9,837</b>
Share Capital	22	23	23	23	23
Reserves	7,201	7,906	8,390	9,025	10,196
Non-controlling interests	75	53	41	28	17
<b>Total equity</b>	<b>7,299</b>	<b>7,982</b>	<b>8,453</b>	<b>9,076</b>	<b>10,236</b>
<b>Total equity and liabilities</b>	<b>12,572</b>	<b>14,615</b>	<b>15,924</b>	<b>17,610</b>	<b>20,073</b>

### Cashflow

RMB mn	2020	2021	2022E	2023E	2024E
Profit before tax	762	1,287	1,666	2,193	2,816
Finance Costs	112	90	68	66	73
Shares of profit of associate/JV	0	0	11	-24	-24
D&A	166	169	192	222	253
Changes in OWC	-320	-447	-292	-928	-1,122
Others	29	-16	413	0	0
Income tax paid and others	-429	-382	-522	-683	-878
<b>CF from operating activities</b>	<b>320</b>	<b>701</b>	<b>1,536</b>	<b>847</b>	<b>1,118</b>
Capital expenditure	-207	-414	-400	-400	-400
Investments	-4	-3	0	0	0
Others	784	89	-12	-10	-16
<b>CF from investing activities</b>	<b>573</b>	<b>-329</b>	<b>-412</b>	<b>-410</b>	<b>-416</b>
Dividend paid	-279	-356	-676	-887	-778
Equity financing	0	823	0	0	0
Debt financing (repaid)	-77	-339	0	0	0
Others	-25	-31	-101	-107	-107
<b>CF from financing activities</b>	<b>-380</b>	<b>96</b>	<b>-777</b>	<b>-994</b>	<b>-885</b>
<b>Net cash flow</b>	<b>513</b>	<b>469</b>	<b>348</b>	<b>-556</b>	<b>-183</b>

### Profit & Loss Statement

RMB mn	2020	2021	2022E	2023E	2024E
<b>Revenue</b>	<b>8,172</b>	<b>10,013</b>	<b>12,772</b>	<b>16,340</b>	<b>20,676</b>
Cost of Sales	-4,973	-5,835	-7,414	-9,454	-11,945
<b>Gross profits</b>	<b>3,198</b>	<b>4,178</b>	<b>5,358</b>	<b>6,885</b>	<b>8,731</b>
Selling expenses	-1,537	-1,891	-2,412	-3,085	-3,904
General & Admin exp	-1,050	-1,189	-1,515	-1,938	-2,452
Others	307	299	349	444	560
<b>Operating profits</b>	<b>918</b>	<b>1,396</b>	<b>1,780</b>	<b>2,306</b>	<b>2,935</b>
D&A	-166	-169	-192	-222	-253
<b>EBITDA</b>	<b>1,084</b>	<b>1,566</b>	<b>1,972</b>	<b>2,528</b>	<b>3,188</b>
Finance costs	-140	-63	-68	-66	-73
Other income/expenses	-17	-46	-46	-46	-46
<b>Profit before tax</b>	<b>762</b>	<b>1,287</b>	<b>1,666</b>	<b>2,193</b>	<b>2,816</b>
Income tax expense	-257	-397	-519	-683	-878
<b>Net profit</b>	<b>505</b>	<b>889</b>	<b>1,147</b>	<b>1,510</b>	<b>1,938</b>
Non-controlling interest	8	19	13	12	12
<b>Attributable net profit</b>	<b>513</b>	<b>908</b>	<b>1,160</b>	<b>1,522</b>	<b>1,950</b>
Diluted EPS (RMB)	0.21	0.36	0.45	0.60	0.76
Div. per share (RMB)	0.12	0.21	0.26	0.35	0.44

### Financial

	2020	2021	2022E	2023E	2024E
<b>yoY growth rate</b>					
Revenue	-0.1%	22.5%	27.5%	27.9%	26.5%
Gross Profit	-9.9%	30.6%	28.3%	28.5%	26.8%
Operating profit	-25.6%	52.1%	27.5%	29.5%	27.3%
Net profit	-29.5%	77.1%	27.7%	31.3%	28.1%
EPS	-31.6%	72.0%	27.7%	31.3%	28.1%
<b>Profitability</b>					
Gross margin	39.1%	41.7%	42.0%	42.1%	42.2%
Operating margin	11.2%	13.9%	13.9%	14.1%	14.2%
Net margin	6.3%	9.1%	9.1%	9.3%	9.4%
<b>Liquidity</b>					
AR days	137.3	123.3	105.3	97.8	98.2
Inventory days	74.2	77.3	75.8	69.4	69.7
AP days	106.4	119.8	115.9	103.5	104.0
Cash conversion cycle	105.1	80.8	65.2	63.7	64.0
<b>Cash flow &amp; leverage</b>					
Free cash low (RMB mn)	217	279	694	450	719
Net debt to equity	-18.0%	-17.4%	-20.6%	-13.0%	-9.8%
Dividend payout ratio	60.0%	58.1%	58.3%	58.3%	58.3%
Dividend yield	1.0%	1.8%	2.2%	2.9%	3.8%
<b>Return analysis</b>					
ROE	7.2%	11.9%	14.1%	17.4%	20.2%
Asset turnover	0.7	0.7	0.8	1.0	1.1
Net margin	6.3%	9.1%	9.1%	9.3%	9.4%
Financial leverage	1.7	1.8	1.9	1.9	2.0
ROA	4.1%	6.7%	7.6%	9.1%	10.3%
<b>Valuation ratios</b>					
P/E	57.0x	33.1x	26.0x	19.8x	15.4x
P/B	4.4x	4.0x	3.8x	3.5x	3.1x

Sources: Company data, CMS (HK) estimates

## Investment Ratings

Industry Rating	Definition
OVERWEIGHT	Expect sector to outperform the market over the next 12 months
NEUTRAL	Expect sector to perform in-line with the market over the next 12 months
UNDERWEIGHT	Expect sector to underperform the market over the next 12 months

Company Rating	Definition
BUY	Expect stock to generate 10%+ return over the next 12 months
NEUTRAL	Expect stock to generate +10% to -10% over the next 12 months
SELL	Expect stock to generate loss of 10%+ over the next 12 months

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