

JPM-pp1

Asia Pacific Equity Research

11 March 2015

Xtep International Holdings Limited (1368 HK)

Neutral

Price: HK\$2.59

10 Mar 2015

Price Target: HK\$3.50

PT End Date: 31 Dec 2015

FY14 result - reporting on 12 March 2015

Xtep will report its FY14 result on 12 March 2015 during the lunch break. The company will hold its briefing at 5:00pm Hong Kong time.

- **We expect Xtep to report FY14 NPAT of Rmb601m, slightly below FY13.** We expect the company to report sales growth of ~3% and 36bps of gross margin expansion. We expect Xtep to report FY14 EBIT of Rmb779m, down 2% y/y. We are forecasting ~14% EBIT growth in 2H14 due to sales growth, operating leverage and slightly lower A&P expenses. We expect Xtep to declare a final dividend of HK10cps.
- **Key Issues to look out for during the results briefing:** (1) Gross and EBIT Margins performance; (2) Any update with respect to trade fair data and SSSG; (3) Trade receivables and working capital metric, with the company's weak working capital metrics previously of concern.

Investment Thesis

Over recent months, both Xtep and sportswear companies in China have been reporting improving operational performance. We believe ongoing momentum will support the share price. Nevertheless, we remain cautious on sportswear names over the longer term, noting there is a risk that EBIT margins contract to be more in line with international peers. For Xtep more specifically, we note rising risk with respect to balance sheet metrics, which may be a negative leading indicator of future sales.

Valuation

Our price target of Dec-15 HK\$3.5 is based on P/E of ~10x our earnings forecasts for year ending Dec-16. Our target P/E is at a discount to the five-year average P/E of international peers (Adidas, Nike and Puma). We apply this discount to reflect:

- 1) advantages international peers have with respect to brand recognition; and
- 2) advantages international peers have with respect to scale in areas where fixed-cost investment is required.

Risks to Rating and Price Target

Upside risks to our price target include: 1) higher-than-expected improvement in sales; 2) significant improvement with respect to gross margins; and 3) a significant reduction of the competitive environment for sportswear in China.

Downside risks to our price target include: 1) significant downturn in the retail environment; 2) increase in the competitive environment for sportswear in China; 3) a significant loss of market share; 4) higher-than-expected sourcing costs; and 5) higher-than-expected capex expenditure.

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
08-Jul-08	OW	2.66	4.30
02-Sep-08	OW	2.23	4.50
13-Oct-08	OW	1.78	3.90
22-Jan-09	OW	1.66	2.50
01-Apr-09	OW	2.19	3.10
29-May-09	OW	3.66	4.70
07-Sep-09	OW	3.90	5.50
15-Jan-10	OW	5.40	6.35
29-Mar-10	OW	5.89	7.00
24-Aug-10	OW	6.00	7.10
29-Nov-10	OW	6.66	7.00
11-Jul-11	N	4.67	4.70
12-Oct-11	N	3.02	3.70
22-Feb-12	UW	3.03	2.60
02-Jul-12	UW	2.70	2.20
21-Aug-12	UW	2.94	2.30
15-Sep-12	UW	2.70	2.20
16-Jan-13	UW	3.53	2.30
16-Mar-13	UW	3.08	2.50
05-Apr-13	UW	3.10	2.40
24-Aug-13	UW	3.90	2.80
10-Jan-14	N	3.91	4.50
12-Mar-14	N	3.72	3.90
21-Aug-14	N	3.34	3.50

<http://gfd-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=1002421&shareClassServerId=4&chartDesignation=1&actionType=C>

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