

Consumer & Retail
 Food Products
 Equity – China

Want Want (151 HK)

Overweight

Target price (HKD)	11.30
Share price (HKD)	7.98
Potential return (%)	41.6

Note: Potential return equals the percentage difference between the current share price and the target price

Performance	1M	3M	12M
Absolute (%)	-12.1	-17.4	-30.5
Relative ^A (%)	-8.9	-21.9	-37.5

Index^A HANG SENG INDEX

RIC	0151.HK
Bloomberg	151 HK

Market cap (USDm)	13,553
Market cap (HKDm)	105,275

Enterprise value (USDm)	12916
Free float (%)	42

Note: (V) = volatile (please see disclosure appendix)

18 March 2015

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OW: Looking to sales and margin recovery

- ▶ **Despite weak 2H14 performance, we believe both sales and margins should see a recovery in coming quarters given healthy channel inventory and higher marketing efforts**
- ▶ **Significant decline in global milk powder costs and crude oil price should provide cost savings for higher A&P spend**
- ▶ **Maintain Overweight with an unchanged TP of HKD11.30**

Channel inventory and new products. Despite slightly weaker than expected 2014 results, management guided for a stabilization of channel inventory after the Chinese New Year holiday and a better margin outlook in 2015. We believe dairy beverage sales growth should start to recover in 2Q15 on the back of higher promotional efforts, new products offerings, and low comparison base. Similar to the strategy in 2014, Want Want has been placing higher emphasis on new product development, and we continue to believe the company's strategic focus on new products and channel efficiency could help drive sales growth and mitigate the product concentration risk in the long run. New products accounted for 5% of total sales in 2014, and we believe it could increase to around 7-8% in 2015 and 2016. Key new products to be launched this year include cold-chain puddings and yogurts (through the partnership with Morinaga Milk Industry Company), room-temperature yogurts, and fruit and vegetable juices.

Cost savings from lower input costs for higher A&P spend. We expect the group's net margin to improve by 1.8ppt in 2015 to 18.2%, and this is mainly due to the sharp decline in New Zealand milk powder prices (down 38% in 2H14), crude oil prices (down 50% in 2H14), and PET prices (down 20% in 2H14). A&P expenses increased by 0.7ppt to 3.7% of total sales in 2014, and we think it will increase to around 4% in 2015 given higher marketing efforts for both existing and new products. However, we believe the cost savings from input cost should be more than sufficient to offset the increase in A&P.

Results highlights. Want Want reported 10% decline in 2014 net profit to USD621m while revenue was down 1% to USD775m. The results were around 4% below our and consensus forecasts. Dairy revenue dropped 0.3% yoy and accounted for 53% of group revenue in 2014. Rice cracker revenue fell 11% yoy and represented 22% of total revenue. The decline in rice cracker business was mainly due to a later Chinese New Year this year, in which most of the orders were shifted to 1Q15. Snack food sales were up 7% yoy and account for 26% of group revenue. Want Want lowered its dividend payout to 51% from 67% in 2013, and we believe it could be due to lengthened inventory days and weaker cash flow. That said, we believe the company's free cash flow should recover strongly in 2015 given better inventory turnover, lower capex and margin recovery.

Financials & valuation

Financial statements

Year to	12/2013a	12/2014e	12/2015e	12/2016e
Profit & loss summary (USDm)				
Revenue	3,818	3,689	3,940	4,363
EBITDA	989	925	1,090	1,234
Depreciation & amortisation	-106	-126	-150	-167
Operating profit/EBIT	883	799	939	1,067
Net interest	49	60	64	65
PBT	934	861	1,005	1,133
HSBC PBT	934	861	1,005	1,133
Taxation	-247	-219	-261	-295
Net profit	687	642	744	840
HSBC net profit	687	642	744	840

Cash flow summary (USDm)

Cash flow from operations	955	681	965	883
Capex	-239	-370	-340	-250
Cash flow from investment	-273	-418	-388	-298
Dividends	-419	-430	-499	-563
Change in net debt	-306	167	-79	-23
FCF equity	686	343	657	665

Balance sheet summary (USDm)

Intangible fixed assets	27	27	27	27
Tangible fixed assets	1,401	1,725	1,996	2,160
Current assets	2,911	2,903	2,883	3,022
Cash & others	2,060	1,993	2,073	2,096
Total assets	4,348	4,665	4,916	5,219
Operating liabilities	1,125	1,131	1,137	1,163
Gross debt	1,258	1,358	1,358	1,358
Net debt	-802	-636	-715	-738
Shareholders funds	1,943	2,155	2,401	2,678
Invested capital	1,154	1,531	1,698	1,952

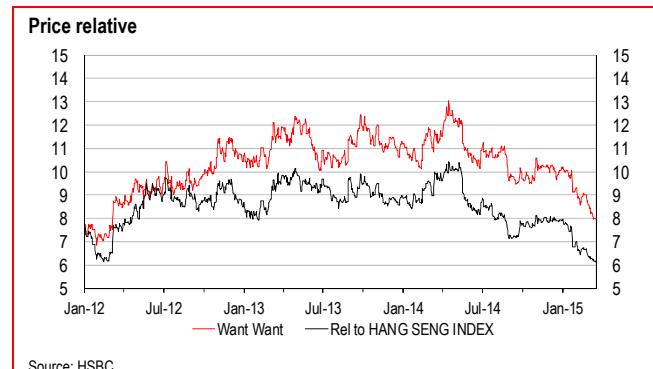
Ratio, growth and per share analysis

Year to	12/2013a	12/2014e	12/2015e	12/2016e
Y-o-y % change				
Revenue	13.7	-3.4	6.8	10.7
EBITDA	23.9	-6.4	17.8	13.3
Operating profit	24.3	-9.5	17.6	13.6
PBT	24.7	-7.8	16.7	12.8
HSBC EPS	24.1	-6.6	16.0	12.8
Ratios (%)				
Revenue/IC (x)	3.4	2.7	2.4	2.4
ROIC	57.3	44.3	43.1	43.3
ROE	38.8	31.3	32.7	33.1
ROA	17.9	14.5	15.8	16.8
EBITDA margin	25.9	25.1	27.6	28.3
Operating profit margin	23.1	21.7	23.8	24.5
EBITDA/net interest (x)				
Net debt/equity	-41.1	-29.4	-29.7	-27.5
Net debt/EBITDA (x)	-0.8	-0.7	-0.7	-0.6
CF from operations/net debt				
Per share data (USD)				
EPS reported (fully diluted)	0.05	0.05	0.06	0.06
HSBC EPS (fully diluted)	0.05	0.05	0.06	0.06
DPS	0.03	0.03	0.04	0.04
Book value	0.15	0.16	0.18	0.20

Valuation data

Year to	12/2013a	12/2014e	12/2015e	12/2016e
EV/sales	3.3	3.5	3.3	2.9
EV/EBITDA	12.9	14.0	11.8	10.4
EV/IC	11.1	8.4	7.6	6.6
PE*	19.8	21.2	18.3	16.2
P/Book value	7.0	6.3	5.7	5.1
FCF yield (%)	5.1	2.5	4.8	4.9
Dividend yield (%)	3.4	3.2	3.7	4.1

Note: * = Based on HSBC EPS (fully diluted)



Note: price at close of 17 Mar 2015

Valuation and risks

We continue to use DCF to value Want Want, as its strong brand positioning and large distribution network allow it to generate steady cash flows and potential returns over the long run. Our target price for Want Want is HKD11.30, and it is derived from a WACC of 7.6%, which include a beta of 0.8, a risk-free rate of 3.5%, and a market risk premium of 5.5%.

Under our research model, for stocks without a volatility indicator the Neutral band is 5ppts above and below the hurdle rate for Hong Kong listed stocks of 8.5%. Our target price implies a potential return of 41.6%, above the Neutral band; therefore, we reiterate our Overweight rating. Potential return equals the percentage difference between the current share price and target price, including the forecast dividend yield when indicated.

Key downside risks

Key downside risks: 1) a sooner-than-expected rebound in milk powder costs; 2) rising competition leading to higher ASP spending; 3) disappointing new product launches; and 4) slower-than-expected improvements in sales channels and productivity.

Want Want - 2014 results summary

Year to Dec 31 (USDm)	2013	2014	% Chg	1H14	% Chg	2H14	% Chg
Sales	3,818	3,775	-1%	1,853	6%	1,923	-7%
COGS	(2,232)	(2,256)	1%	(1,105)	7%	(1,151)	-4%
Gross profit	1,586	1,519	-4%	747	3%	772	-10%
Distribution costs	(455)	(487)	7%	(238)	8%	(249)	6%
Admin costs	(326)	(329)	1%	(155)	5%	(174)	-2%
Other income	70	73	5%	43	27%	30	-17%
Other gains/(losses), net	9	1	-94%	(2)	n/a	2	n/a
EBIT	883	777	-12%	395	-1%	382	-21%
Finance income	66	77	17%	44	51%	33	-10%
Finance costs	(17)	(23)	39%	(12)	73%	(11)	14%
Share of profit of associates	2	(1)	-134%	(0)	n/a	(0)	n/a
PBT	934	830	-11%	426	2%	403	-21%
Tax	(247)	(210)	-15%	(108)	-4%	(102)	-24%
Minority	1	1	31%	0	n/a	0	n/a
Net profit	687	621	-10%	318	4%	302	-20%
Margins and key ratios							
Gross Margin	41.5%	40.2%	-1.3ppt	40.3%	-0.9 ppt	40.2%	-1.6 ppt
EBITDA Margin	25.9%	23.8%	-2.1 ppt	24.6%	-0.8 ppt	23.1%	-3.2 ppt
EBIT Margin	23.1%	20.6%	-2.6 ppt	21.3%	-1.3 ppt	19.9%	-3.7 ppt
PBT Margin	24.5%	22.0%	-2.5 ppt	23.0%	-0.9 ppt	21.0%	-3.9 ppt
Net Margin	18.0%	16.4%	-1.6 ppt	17.2%	-0.3 ppt	15.7%	-2.7 ppt
Distribution costs as % of sales	11.9%	12.9%	+1.0ppt	12.8%	0.3 ppt	12.9%	+1.5 ppt
Admin expense as % of sales	8.5%	8.7%	+0.2ppt	8.4%	-0.1 ppt	9.0%	+0.4 ppt
Effective tax rate	26.5%	25.3%	-1.1ppt	25.4%	-1.4 ppt	25.2%	-1.0 ppt

Source: Company data, HSBC

Disclosure appendix

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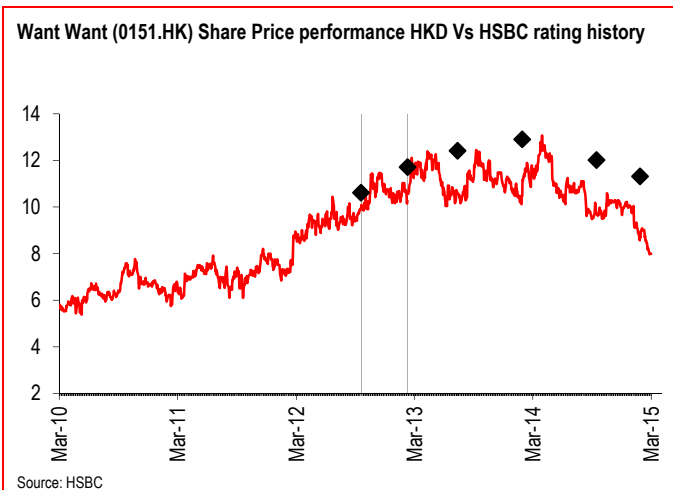
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Underweight (Sell)	20%	(20% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities



Recommendation & price target history

From	To	Date
N/A	Neutral	03 October 2012
Neutral	Overweight	24 February 2013
Target Price	Value	Date
Price 1	10.60	03 October 2012
Price 2	11.70	24 February 2013
Price 3	12.40	28 July 2013
Price 4	12.90	12 February 2014
Price 5	12.00	29 September 2014
Price 6	11.30	11 February 2015

Source: HSBC

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Company	Ticker	Recent price	Price Date	Disclosure
WANT WANT	0151.HK	7.98	17-Mar-2015	4, 7

Source: HSBC

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