



Rating
Hold

Asia
China

Consumer
Retail / Wholesale Trade

Company
Hengdeli Alert

Reuters 3389.HK	Bloomberg 3389 HK	Exchange HSI	Ticker 3389
ADR Ticker HENGY	ISIN US42551K1007		

Date
20 March 2015

Company Update

Price at 19 Mar 2015 (HKD)	1.38
Price target - 12mth (HKD)	1.35
52-week range (HKD)	1.53 - 1.21
HANG SENG INDEX	24,469

Anne Ling

Research Analyst
(+852) 2203 6177
anne.ling@db.com

Key takeaways from NDR

During the meetings, investors were interested in 1) principals' price adjustments; 2) the outlook for the watch business in Greater China; and 3) the impact of smartwatches (e.g., Apple Watch) on the traditional watch business.

No clear view on principals' price adjustments at the moment

Following Patek Philippe's price cuts of 5-20% and Chanel's price adjustments in Hong Kong, investors are concerned that more brands/principals will lower their watch prices, which could hurt Hengdeli's margin. Management commented that this could be true for old inventory (although there could be subsidies from principals), but that lower prices help attract more customers and drive sales. Management expects more clarity regarding price adjustments after the Basel conference, which kicks off 19 March.

Confident on growth of mid-range business in the PRC, but will not give up on high-end market in Hong Kong

- Management is confident regarding the mid-range watch business in mainland China due to the growth of the urban middle class. Consumption now comes from real demand by end-consumers, as opposed to gifting. Hengdeli will open 30-40 stores, mainly in Tier 3 and 4 cities, with capex of ~RMB100m.
- When asked if there will be store closures in Hong Kong, management said that it will not do so at this time as 1) the Hong Kong business is still profitable with controllable costs, as they are all located in shopping malls with turnover rent; 2) the Hong Kong market is still a key market for principals. Under the current adverse environment, they would be willing to take measures (e.g., larger sales rebates) to support Hengdeli; and 3) closures might give customers a negative impression. Also, Harvest Max, which targets tour groups, performs well.
- The company will try to reduce its inventory level, especially high-end watches. It targets 220 inventory days by 2015. In 2014, its inventory days were 227 (HK: 260-270 days, +50 days yoy; China: 160-170 days). Its inventory consists of 70%/30% mid-range/high-end watches.

Smartwatch impact is relatively limited to Swiss watches, management says

Regarding smartwatches, management commented that it focuses on functions and fast fashion (i.e., one year). However, Swiss watches focus on craftsmanship and their value is retained over time. Swiss watches and smartwatches do not compete against each other. That said, we believe all players (including the principals) are monitoring developments closely.

Stock data

Market cap (HKDm)	6,066
Market cap (USDm)	782
Shares outstanding (m)	4,396.0
Major shareholders	Mr. Zhang Yuping (35%)
Free float (%)	33
Avg daily value traded (USDm)	0.844

Source: Deutsche Bank

Key data

FYE 12/31	2014A	2015E	2016E
Sales (CNYm)	14,764	15,903	17,519
Net Profit (CNYm)	504.2	433.5	489.1
DB EPS (CNY)	0.11	0.09	0.10
PER (x)	10.0	12.2	10.8
Yield (net) (%)	2.2	2.5	2.8

Source: Deutsche Bank

Deutsche Bank AG/Hong Kong

The views expressed above accurately reflect the personal views of the authors about the subject companies and its(their) securities. The authors have not and will not receive any compensation for providing a specific recommendation or view. Deutsche Bank does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

FOR OTHER IMPORTANT DISCLOSURES PLEASE VISIT
<http://gm.db.com/ger/disclosure/Disclosure.eqsr?ricCode=3389.HK> MCI (P) 148/04/2014.