



Rating
Buy

Asia
China

Consumer

Company
Hengan Intl.

Reuters 1044.HK	Bloomberg 1044 HK	Exchange HKG	Ticker 1044
ADR Ticker HEGIY	ISIN US42551N1046		

Date
25 March 2015

Forecast Change

Price at 24 Mar 2015 (HKD)	87.50
Price target - 12mth (HKD)	95.10
52-week range (HKD)	93.35 - 76.35
HANG SENG INDEX	24,495

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Still the only necessity

Near-term safe haven + long-term potential; maintaining Buy

It seems to us that sanitary napkins are the only necessities in China, as demonstrated by Hengan's solid 2014 results. Looking ahead, we think Hengan has a proven track record of offering continuous novelty in products and branding, and we maintain our Buy recommendation, as we think lower input costs will allow the company more resources to invest in the baby diaper market and at a later stage the adult diaper market, both of which are still underpenetrated.

2014 NPAT grew by 5.2% yoy, beating Deutsche Bank estimate/consensus

Hengan's 2014 NPAT increased 5.2% yoy to HKD3,916m, 4.7%/4.3% higher than the Deutsche Bank estimate and market consensus. Revenue was up 12.5%, with GPM +1ppt to 46.1%. During the period, government grants increased 65% yoy to HKD667m (2013: HKD404m) and helped to offset the HKD132m exchange loss (2013: HKD279m exchange gain).

2015: more resources to invest in diapers and e-commerce

Management is comfortable with lower input costs in 2015 and plans to reinvest the cost benefit on diapers and e-commerce. The company broke up its all-in-one sales team by product into three teams focusing on each of its major categories; therefore, it can motivate each team with a specific sales target instead of a blended sales target.

2015-16E NPAT +3-5%; TP + 10%; maintaining Buy

We have revised up our 2015-16E NPAT forecast by 3-5%. Based on our new forecast and rolling over our DCF analysis by one year, we revised up our target price from HKD86 to HKD95.1, factoring in 3.9% RFR, 5.6% ERP, 1.0 beta, 3% TG and debt-free structure, equivalent to 24.8x 2015E PE. Our TP revision is higher than our NPAT revision, as with more resources (financial and management), we expect a higher success rate for its diapers in the longer term. We maintain our Buy recommendation. Key downside risks include irrational competition and slow diaper segment expansion.

Forecasts And Ratios

Year End Dec 31	2013A	2014A	2015E	2016E	2017E
Sales (HKDm)	21,186.4	23,830.8	27,113.8	32,094.7	37,316.0
Reported NPAT (HKDm)	3,721.0	3,915.8	4,688.6	5,653.3	6,589.3
Reported EPS FD (HKD)	3.09	3.12	3.72	4.47	5.20
DB EPS FD (HKD)	3.09	3.12	3.72	4.47	5.20
OLD DB EPS FD (HKD)	3.09	2.98	3.55	4.34	-
% Change	0.0%	4.8%	4.8%	3.1%	-
DB EPS growth (%)	8.0	1.1	19.2	20.1	16.3
PER (x)	27.3	26.3	23.5	19.6	16.8
DPS (net) (HKD)	1.85	2.00	2.39	2.88	3.36
Yield (net) (%)	2.2	2.4	2.7	3.3	3.8

Source: Deutsche Bank estimates, company data

¹ DB EPS is fully diluted and excludes non-recurring items

² Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close

Key changes

Price target	86.00 to 95.10	↑	10.6%
Sales (FYE)	28,056 to 27,114	↓	-3.4%
Op prof margin (FYE)	21.4 to 24.0	↑	12.6%
Net profit (FYE)	4,476.5 to 4,688.6	↑	4.7%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-2.2	9.7	6.4
HANG SENG INDEX	-1.0	4.9	12.1

Source: Deutsche Bank

Deutsche Bank AG/Hong Kong

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Model updated: 24 March 2015

Running the numbers

Asia

China

Consumer

Hengan Intl.

Reuters: 1044.HK

Bloomberg: 1044 HK

Buy

Price (24 Mar 15) HKD 87.50

Target Price HKD 95.10

52 Week range HKD 76.35 - 93.35

Market Cap (m) HKDm 107,135
USDm 13,814

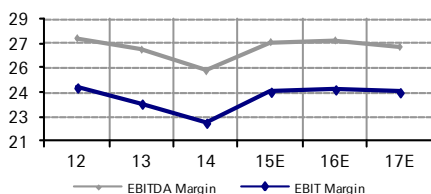
Company Profile

Hengan manufactures and sells personal hygiene products, including feminine napkins, baby diapers, and consumer tissue in China. The company's products are sold under brand names such as Anerle, Anle, and Hearttex.

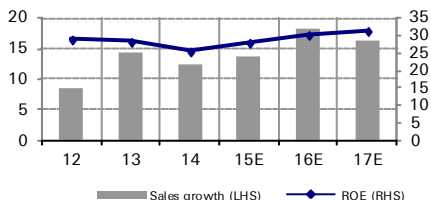
Price Performance



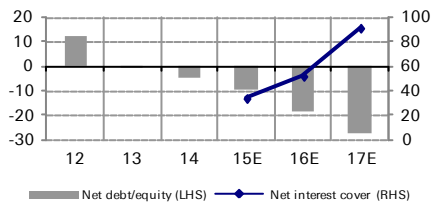
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

2012 2013 2014 2015E 2016E 2017E

Financial Summary

DB EPS (HKD)	2.86	3.09	3.12	3.72	4.47	5.20
Reported EPS (HKD)	2.86	3.09	3.12	3.72	4.47	5.20
DPS (HKD)	1.70	1.85	2.00	2.39	2.88	3.36
BVPS (HKD)	10.5	12.5	13.2	14.7	16.4	18.4
Weighted average shares (m)	1,229	1,231	1,227	1,227	1,227	1,227
Average market cap (HKDm)	90,827	103,664	100,718	107,135	107,135	107,135
Enterprise value (HKDm)	91,545	102,839	99,050	104,558	102,519	100,051

Valuation Metrics

P/E (DB) (x)	25.8	27.3	26.3	23.5	19.6	16.8
P/E (Reported) (x)	25.8	27.3	26.3	23.5	19.6	16.8
P/BV (x)	6.66	7.36	6.13	5.97	5.34	4.76
FCF Yield (%)	0.5	2.7	3.5	3.4	4.9	5.9
Dividend Yield (%)	2.3	2.2	2.4	2.7	3.3	3.8
EV/Sales (x)	4.9	4.9	4.2	3.9	3.2	2.7
EV/EBITDA (x)	18.1	18.2	16.4	14.2	11.7	10.0
EV/EBIT (x)	20.3	20.8	18.8	16.0	13.2	11.2

Income Statement (HKDm)

Sales revenue	18,524	21,186	23,831	27,114	32,095	37,316
Gross profit	8,315	9,560	10,988	13,168	15,308	17,763
EBITDA	5,064	5,642	6,030	7,347	8,730	10,002
Depreciation	561	703	755	828	966	1,041
Amortisation	0	0	0	0	0	0
EBIT	4,503	4,939	5,276	6,519	7,764	8,961
Net interest income/(expense)	36	76	67	-190	-148	-98
Associates/affiliates	0	0	0	0	0	0
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0	0
Profit before tax	4,539	5,015	5,343	6,329	7,616	8,864
Income tax expense	1,001	1,245	1,369	1,582	1,904	2,216
Minorities	19	50	58	58	58	58
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	3,519	3,721	3,916	4,689	5,653	6,589
DB adjustments (including dilution)	0	265	103	104	104	104
DB Net profit	3,519	3,986	4,019	4,792	5,757	6,693

Cash Flow (HKDm)

Cash flow from operations	2,936	3,984	5,329	5,051	6,907	7,448
Net Capex	-2,469	-1,201	-1,755	-1,355	-1,604	-1,119
Free cash flow	467	2,783	3,574	3,696	5,303	6,328
Equity raised/(bought back)	1	103	-1	0	0	0
Dividends paid	-1,847	-2,220	-2,271	-2,729	-3,206	-3,802
Net inc/(dec) in borrowings	4,013	8,226	1,095	0	0	0
Other investing/financing cash flows	-1,347	1,128	-665	0	0	0
Net cash flow	1,286	10,020	1,733	967	2,097	2,526
Change in working capital	-1,157	-380	783	-592	197	-272

Balance Sheet (HKDm)

Cash and other liquid assets	9,544	19,564	21,297	22,264	24,361	26,888
Tangible fixed assets	9,439	10,413	10,849	11,376	12,013	12,092
Goodwill/intangible assets	0	0	0	0	0	0
Associates/investments	1,301	1,105	1,351	1,351	1,351	1,351
Other assets	8,920	9,108	9,080	10,186	10,768	11,858
Total assets	29,205	40,190	42,577	45,177	48,494	52,189
Interest bearing debt	11,233	19,459	20,555	20,555	20,555	20,555
Other liabilities	4,731	5,044	5,367	6,154	7,299	8,470
Total liabilities	15,964	24,503	25,922	26,709	27,853	29,024
Shareholders' equity	12,911	15,302	16,230	17,984	20,099	22,564
Minorities	330	385	425	484	542	600
Total shareholders' equity	13,241	15,687	16,655	18,467	20,641	23,164
Net debt	1,689	-105	-742	-1,709	-3,807	-6,333

Key Company Metrics

Sales growth (%)	8.6	14.4	12.5	13.8	18.4	16.3
DB EPS growth (%)	32.7	8.0	1.1	19.2	20.1	16.3
EBITDA Margin (%)	27.3	26.6	25.3	27.1	27.2	26.8
EBIT Margin (%)	24.3	23.3	22.1	24.0	24.2	24.0
Payout ratio (%)	59.4	61.3	62.6	62.6	62.6	62.6
ROE (%)	28.9	28.3	25.5	28.0	30.2	31.4
Capex/sales (%)	13.3	5.7	7.4	5.0	5.0	3.0
Capex/depreciation (x)	4.4	1.7	2.3	1.6	1.7	1.1
Net debt/equity (%)	12.8	-0.7	-4.5	-9.3	-18.4	-27.3
Net interest cover (x)	nm	nm	nm	34.3	52.4	91.9

Source: Company data, Deutsche Bank estimates

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Nothing new, it just delivered

2015 management guidance and outlook

Management is comfortable with lower input costs in 2015 and plans to reinvest the cost benefit on diapers and e-commerce. It broke up its all-in-one sales team by product into three teams focusing on each of its major categories; therefore, it can motivate each team with a specific sales target instead of a blended sales target. With more resources (financial and management), we expect a higher success rate for its diapers.

From all-in-one to three kingdoms

For the first time in its history, Hengan will run three sales teams for its three major products. The restructuring was completed at the end of 2014, with total salesforce and staff cost unchanged. Management aims at creating internal competition to stimulate productivity and innovation, and each team will have a specific sales target. Before that, the all-in-one sales team had a blended sales target, which was therefore biased toward the best selling products. Thus far, the distributors are positive toward the change.

Tissue: a balance between market share and profitability this year

Hengan will seek a balance between market share and profitability this year. In 2H14, the company focused on profitability and lost some market share. While overcapacity still lingers, Hengan will focus on product differentiation and has no intention of selling/developing any loss-making products. It introduced a new high-end series, Ultrasoft, to the market in late 2014/early 2015.

Sanitary napkins: longer and/or thinner

Management saw its weakness in the overnight-use market, and the company will launch a 42cm-sanitary napkin this year. Management expects more online sales, as it has seen encouraging online sales performance since 2014. Earlier, management said the sanitary napkins market in China still supports premiumization, and the company still sees room for market share expansion, as the market is still fragmented. According to management, its new ultra-thin product (introduced in 2014) made a GPM of over 70%.

Channel development is the focus for diapers

Management targets strong growth for diapers. To recall, the company targeted for strong growth in 2013 and 2014 but failed. This year, Hengan will reinvest the savings from lower input costs on channel development, including both baby stores and e-commerce. Baby stores and e-commerce are the two major channels for diaper sales. The company told us in our Beijing conference that its target is to cover 27,000 baby stores in 2015, down from 30,000-35,000, as certain baby stores require an expensive listing fee, and Hengan therefore dropped them off the target list. Comparing to last year, we think management has become more open in terms of dealing with e-commerce challenges/opportunities. The company will use both a self-operated platform as well as a third-party platform, and it has not changed its target on developing a sound O2O model.



2015-16E NPAT forecast revisions and TP change

Hengan started to enjoy the cost benefit from lower crude oil from November 2014. We have revised up our 2015-16E NPAT forecast by 3-5%. Based on our new forecast and rolling over our DCF analysis by one year, we revised up our target price from HKD86 to HKD95.1, factoring in 3.9% RFR, 5.6% ERP, 1.0 beta, 3% TG and debt-free structure, equivalent to 24.8x 2015E PE, which is not demanding compared to the global peer average of 31.3x FY15E PE.

Figure 1: 2015-16E NPAT revisions

(HKDm)	New		Old		Change	
	2015E	2016E	2015E	2016E	2015E	2016E
Sales	27,114	32,095	28,056	33,247	-3.4%	-3.5%
GPM	48.6%	47.7%	44.5%	44.3%	4.1%	3.4%
EBITM	24.0%	24.2%	21.4%	22.0%	2.7%	2.2%
NPAT	4,689	5,653	4,477	5,488	4.7%	3.0%

Source: Deutsche Bank estimates

Figure 2: Personal care peer group comparison

	Code	Listing curr	Rec	Price		Mkt cap	PE (x)	
				Local curr	Local curr		USDm	FY15E
HK-listed								
Vinda	3331 HK Equity	HKD	NR	12.5	NA	1,609	18.9	15.9
PRC-listed								
Shanghai Jahwa	600315 CH Equity	CNY	NR	42.98	NA	4,658	22.9	21.6
C&S Paper	002511 CH Equity	CNY	NR	12.92	NA	845	55.5	41.0
Asia (ex-HK, CHN) listed								
Hindustan Unilever	HUVR IN Equity	INR	Buy	890	1000.0	30,756	45.8	38.4
Kao Corp	4452 JT Equity	JPY	NR	6016	NA	25,331	32.9	27.8
Unilever Indonesia Tbk Pt	UNVR IJ Equity	IDR	Hold	38900	NA	22,923	50.5	45.2
Unicharm	8113 JT Equity	JPY	NR	3239	NA	16,799	39.8	34.3
LG Household & Health Care	051900 KS Equity	KRW	NR	760000	NA	10,732	29.3	25.1
Dabur India	DABUR IN Equity	INR	Hold	266	260.0	7,501	43.3	34.5
Emami Ltd	HMN IN Equity	INR	NR	983.2	NA	3,576	47.4	38.6
Procter & Gamble Hygiene	PG IN Equity	INR	NR	7249.4	NA	3,771	N/A	N/A
Gillette India Ltd	GILL IN Equity	INR	NR	4859.4	NA	2,537	N/A	N/A
Rest of world								
P&G	PG US Equity	USD	Buy	84.86	96.0	229,364	21.4	19.6
Unilever Plc	ULVR LN Equity	GBP	Buy	2905	2950.0	130,354	21.2	19.9
Colgate-Palmolive Co	CL US Equity	USD	NR	70.35	NA	63,804	23.5	21.5
Kimberly Clark	KMB US Equity	USD	Hold	108.99	112.0	40,019	17.6	NA
Svenska Cellulosa	SCAB SS Equity	SEK	NR	206.5	NA	17,100	17.3	16.2
Kimberly-Clark Mexico	KIMBERA MM Equity	MXN	Hold	30.6	30.0	6,296	26.3	22.8
Paul Hartmann	PHH2 GR Equity	EUR	NR	339	NA	1,322	N/A	N/A
Clearwater Paper	CLW US Equity	USD	NR	64.5	NA	1,236	18.2	12.3
Average							31.3	27.2

Source: Deutsche Bank estimates; Bloomberg Finance LP

We estimate petrochem-related and packaging materials to account for 33% of Hengan's 2015E COGS, and for every 2% change in the related cost from our forecast, Hengan's NPAT will be revised up/down by 1.5%. In 2009, when crude oil prices corrected sharply, Hengan's sanitary napkins and diapers recorded a 3.2ppt and 5.8ppt gain in GPM, respectively, which was also a



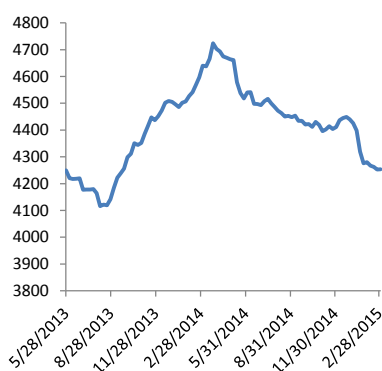
result of product mix improvement. Assuming all such gain was purely due to lower input cost, the contribution to its 2009 NPAT would have been 8%.

Figure 3: 2015-16E NPAT sensitivity to petrochem/packaging cost change

	2015E		2016E	
	HKDm	Dev from base case	HKDm	Dev from base case
6%	(206)	-4.4%	(254)	-4.5%
4%	(138)	-2.9%	(169)	-3.0%
2%	(69)	-1.5%	(85)	-1.5%
Base case NPAT	4688.6		5653.3	
-2%	69	1.5%	85	1.5%
-4%	138	2.9%	169	3.0%
-6%	206	4.4%	254	4.5%

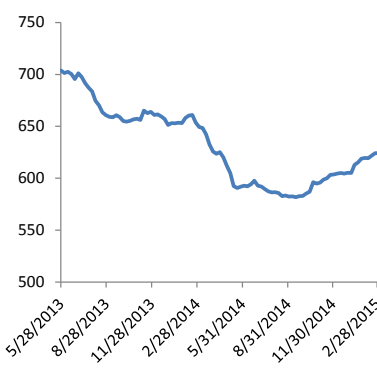
Source: Deutsche Bank estimates

Figure 4: China NBSK (long fibre; RMB/tonne)



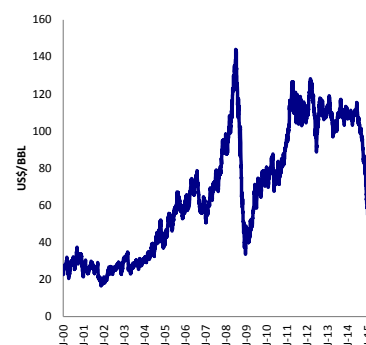
Source: Bloomberg Finance LP

Figure 5: China BHKP (short fibre; USD/tonne)



Source: Bloomberg Finance LP

Figure 6: Crude oil-Brent dated FOB USD/BBL



Source: Datastream

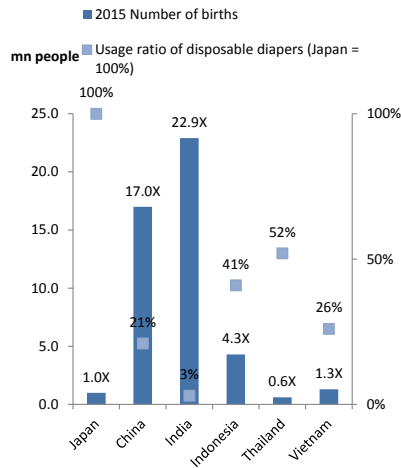
Near-term safe haven + long-term potential; maintaining Buy

It seems to us that sanitary napkins are the only necessities in China, as demonstrated by Hengan's solid 2014 results. In 1Q15, Hengan is not in F&B and therefore is immune from the F&B weakness due to ongoing destocking (refer to the Deutsche Bank report, "Destocking still lingering, need new products and channels to reconnect", published on 27 February 2015). In addition, it has started enjoying benefits of lower input costs since late 2014.

Looking ahead, we think Hengan has a proven track record of offering continuous novelty in products and branding, and we maintain our Buy recommendation, as we think lower input costs will allow the company more resources to invest in the baby diaper market and at a later stage the adult diaper market, both of which are still underpenetrated. Key downside risks include irrational competition and slow diaper segment expansion.

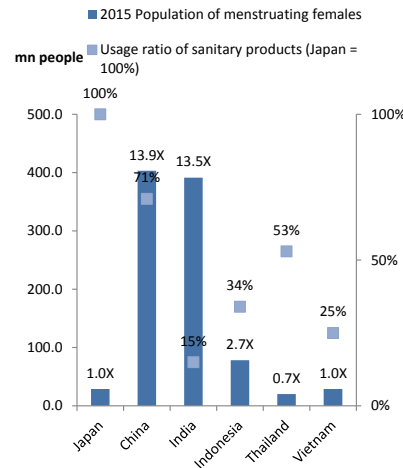


Figure 7: Number of births and usage of diapers



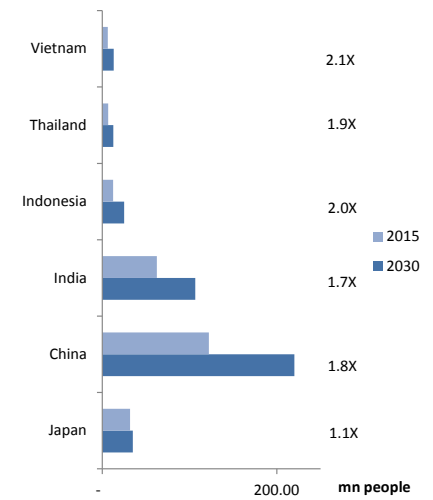
Source: Unicharm

Figure 8: Number of menstruating females and usage of sanitary products



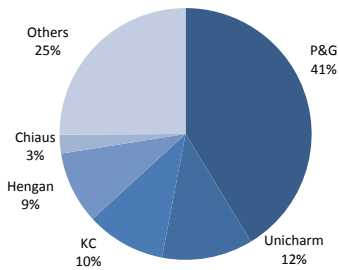
Source: Unicharm

Figure 9: 2030/2015 number of elderly



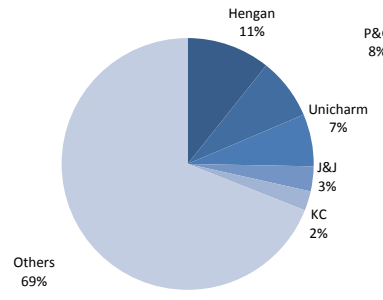
Source: Unicharm

Figure 10: China diaper market share breakdown (2013)



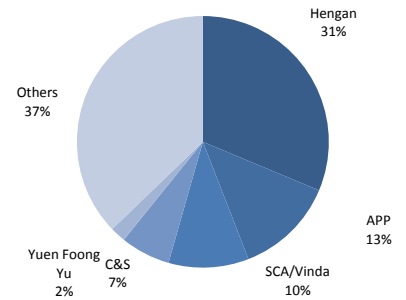
Source: Euromonitor

Figure 11: China sanitary protection market share breakdown (2013)



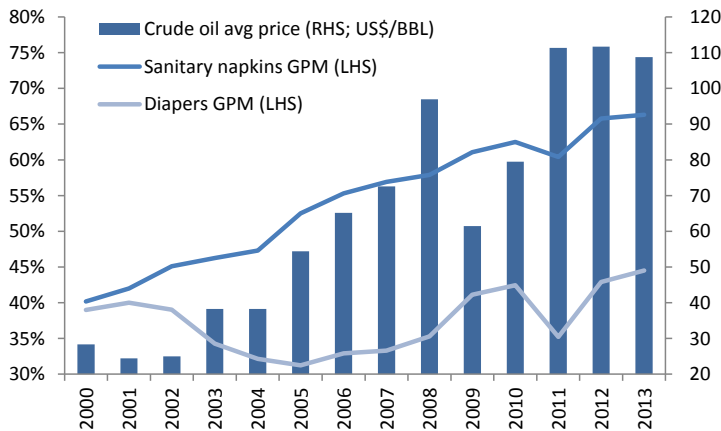
Source: Euromonitor

Figure 12: China tissue market share breakdown (2013)



Source: Euromonitor

Figure 13: Hengam GPM vs. crude oil price



Source: Datastream, company data, Deutsche Bank



Input-cost benefit is one-off

We think input cost-driven growth is a one-off, benefiting inefficient players and undermining branding and management capabilities, making the stock a derivative to commodity trends. To illustrate, Hengan's diapers are vulnerable to fluctuations in the price of raw materials, but its sanitary napkins are relatively not as sensitive to raw material cost changes given its brand value.

2015: energize the babies

We expect Hengan to reinvest the input cost benefit in branding and network expansion of its baby diapers, therefore absorbing part of the gain. This will help to make diapers its new growth engine. We also found Hengan expanding online diaper sales from our earlier channel check with online distributors.

2016: from baby to adult

According to Unicharm, China's elderly population in 2030 will be 1.8x that of 2015 (i.e., a c.4% CAGR over the period). Hengan's Elderjoy is currently the most popular adult diaper brand in China, according to the China National Household Paper Industry Association (CNHPIA). Hengan's adult diaper sales grew rapidly but accounted for less than 1% of its total sales. Management believes that it will be a key growth area in the future when consumption habits change. It has set up a specialized team to prepare for that and is expanding its distribution network to hospitals and homes for the elderly.

The penetration of adult incontinence is unknown, but in 2013, domestic consumption increased 41% yoy. China's aging population is inevitably growing, but according to CNHPIA, the international threshold for development of a sustainable adult incontinence market is USD8,000 per capita GDP, compared to China's USD6,767 in 2013. Based on our forecasts, China's per capita GDP will hit USD8,000 in 2016 (i.e., affordability should support sustainable adult incontinence market growth by then). However, consumer education is greatly needed to narrow the cultural gap for growing product usage. According to Price Hanna Consultants, the global market consumed 33.3bn pieces of adult care products, compared to 301.3bn pieces of feminine care products and 156.5bn baby care products. We estimate the global adult incontinence market is c.60% the size of the global feminine care market, which is c.60% the size of the baby diaper market.

2014 review

Hengan reported 5.2% yoy growth in NPAT to HKD3.9bn, with a revenue increase of 12.5% and EBITM of 22.1% (2013: 23.3%). In 2H14, revenue was up 9% as a combined result of slow tissue and diapers sales and RMB depreciation, offset by product mix improvement and lower input cost (both pulp and petrochem-related raw materials); EBITM gained 0.7 ppt yoy, and as a result, NPAT was up 15%.



Figure 14: 1H vs. 2H results highlights

	1H13	2H13	1H14	2H14	1H14	2H14
Sales (HK\$m)						
Sanitary napkins	2,860	3,113	3,586	3,842	25.4%	23.4%
Disposable diapers	1,432	1,506	1,546	1,549	8.0%	2.8%
Tissue paper	5,065	5,139	5,638	5,219	11.3%	1.6%
Food & snack products	932	673	947	588	1.6%	-12.6%
Skincare and others	126	341	381	535	202.4%	57.1%
Total	10,415	10,771	12,098	11,733	16.2%	8.9%
Gross profit	4,711	4,848	5,434	5,554	15.3%	14.6%
Blended GPM	45.2%	45.0%	44.9%	47.3%	-0.3%	2.3%
GPM by category						
Sanitary napkins	65.1%	67.4%	66.9%	70.0%	1.8%	2.6%
Disposable diapers	43.5%	45.4%	44.2%	46.4%	0.7%	1.0%
Tissue paper	34.9%	33.3%	33.2%	35.9%	-1.7%	2.6%
Others	43.3%	35.0%	36.1%	24.3%	-7.2%	-10.7%
EBIT	2,356	2,584	2,376	2,900	0.8%	12.2%
EBITM	22.6%	24.0%	19.6%	24.7%	-3.0%	0.7%
Net Profit	1,859	1,862	1,775	2,141	-4.5%	15.0%

Source: Deutsche Bank, company data

Figure 15: Sales growth by volume and ASP and GPM growth

(HK\$m)	2013		2014		YoY change			
	Sales	GPM	Sales	GPM	Sales	Volume	ASP	GPM
Tissue paper	10,204.0	34.1%	10,857.3	34.5%	6.4%	8.3%	-1.90%	0.4%
Sanitary napkins	5,972.7	66.3%	7,427.7	68.5%	24.4%	17.8%	6.60%	2.2%
Disposable diapers	2,938.2	44.5%	3,094.6	45.3%	5.3%	-4.2%	9.50%	0.8%
Food and snacks	1,604.7	42.3%	1,534.7	42.4%	-4.4%	na	na	0.1%
Others	466.8	na	916.4	na	96.3%	na	na	na
Overall	21,186.4	45.1%	23,830.8	46.10%	12.5%	na	na	1.0%

Source: Deutsche Bank, company data

Sanitary napkins: 2014 sanitary napkin sales increased 24.4% yoy to HKD7.4bn, accounting for 31.2% of total revenue (2013: 28.2%). GPM on a full-year basis improved 2.2 ppt to 68.5%. Going forward, the company will focus on optimizing product mix by increasing mid-/high-end product sales.

Tissue: 2H14 saw stagnant top-line growth, but thanks to lower pulp cost and as Hengan did not offer additional discounts in 2H14, management saw GPM improvement. To stimulate demand, Hengan launched a new tissue series, and to shorten reaction time to market changes, Hengan set up a new tissue sales team (previously, one single sales team covered all three categories) to take responsibility for driving tissue sales. On a full-year basis, revenue from tissue sales was up 6.4% to HKD10.9bn in 2014, representing 45.6% of the total (2013:48.2%). GPM remained fairly stable at 35.4%, 0.4ppt higher than 2013. The company plans to increase capacity based on market conditions in the future.

Diaper: The major sales growth driver remained the mid-/high-end diapers (one-third of 1H14 diaper sales) but was offset by a decline in low-end diapers (20% of 1H14 diaper sales). Hengan now covers 20,000 baby stores (June 2014: over 13,000). Sales through e-commerce and baby stores now account



for only 10% of its diaper sales, and it aims at catching up with the market (45%) in the long term. The total revenue from diapers was up 5.3% to approximately HKD3.1bn, which represented 13% of overall revenue (2013: 13.9%). GPM on a full-year base improved 0.8 ppt to 45.3%, benefiting from product mix optimization and a drop of raw material cost since 4Q14.

China was a growth driver for Kao (4452 JT, NR) in 2014, mainly through sales of Merries baby diapers (launched in 2013) targeting the middle class segment. Unicharm (UC, 8113 JT, NR) reported 10% diaper sales growth in China, partly due to a 66% yoy increase in import diaper sales. Kimberly Clark's (KMB US, Hold) diaper organic sales rose 25% in China in 2014. According to UC, imports accounted for 11% of China's total diaper industry sales in 2014 (2010: 8%), and diaper sales through the e-commerce channel increased to 32% of the total in 2014 from 14% in 2011. Hengan was clearly a laggard in 2014, and we think it is largely attributable to its poor distribution network and inadequate marketing effort.

Figure 16: Hengan sales growth vs. market and peers' China sales (2014)

Yoy change	Market	Hengan	Unicharm	Kimberly Clark
Diaper	6%	5%	10%	25%
Diaper through ecommerce	25%	NA	74%	NA
Import diaper sales	NA	NA	66%	NA
Sanitary napkins	NA	24%	21%	NA

Source: Company data

Figure 17: China baby diaper sales by channel mix

	2011	2014
Ecommerce	14%	32%
Baby stores	26%	31%
Traditional	32%	21%
Modern	29%	18%

Source: Unicharm

Figure 18: China baby diaper sales by product mix

	2010	2014
Pants	1%	14%
Imports	8%	11%
Premium	3%	13%
Standard	49%	40%
Economy	26%	17%
Pad	13%	5%

Source: Unicharm



Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Hengan Intl.	1044.HK	87.50 (HKD) 24 Mar 15	14

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

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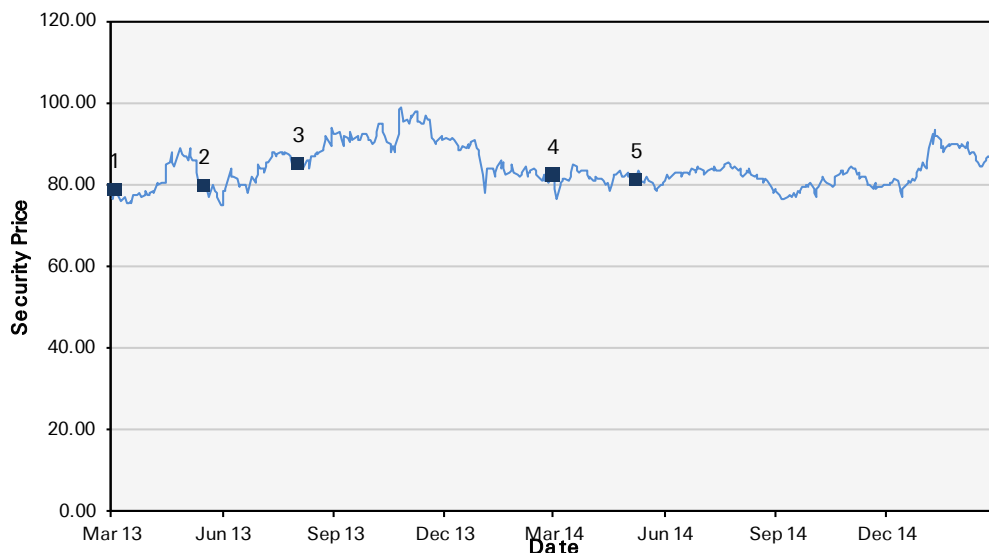
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Historical recommendations and target price: Hengan Intl. (1044.HK)

(as of 3/24/2015)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

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1.	28/03/2013:	Buy, Target Price Change HKD84.49	4.	25/03/2014:	Buy, Target Price Change HKD90.00
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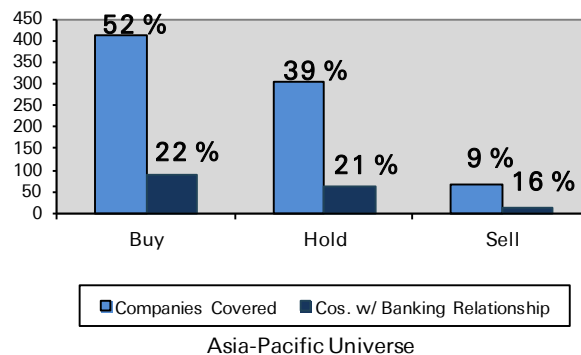
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