

Golden Eagle Retail Group
3308 HK

Target (HKD): **7.40 → 8.00**

Downside: **13.5%** 24 Mar price (HKD): **9.25**

- 1 Buy
- 2 Outperform
- 3 Hold
- 4 Underperform
- 5 Sell (unchanged)

Oversupply concerns remain

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- 2014 gross sales proceeds (GSP) dropped by 6% YoY; SSSG declined 5.5%
- Management guides for low-double-digit YoY GSP growth and low-single-digit SSSG for 2015
- Reiterating Sell (5) due to overly aggressive expansion plan in oversupplied Jiangsu

■ What's new

Golden Eagle held its analyst briefing on 24 March and updated analysts and investors on current operating trends, as well as the near-term industry outlook. It posted a 5.9% YoY decline in GSP, to CNY15.8bn, and a SSSG decline of 5.5% YoY, both largely due to expenses for its Nanjing Xinjiekou flagship store. Management said that excluding these one-off items, GSP would have declined by 2.4% YoY and SSSG would have come in at -1.8%. Management guides for low-double-digit YoY GSP growth and low-single-digit SSSG for 2015.

■ What's the impact

Earnings revision. We raise our 2015-16E core EPS by 7-16% in light of Golden Eagle's better-than-expected concessionaire-rate

improvements (up 40bps YoY to 18.2% in 2014), driven by its product mix. We also factor in a slight increase in rental expenses given that as at 31 March 2015, 40% of its GFA would remain leased, and management says this will rise to 46% by the end of 2015.

Highlights from analyst briefing.

We are cautious about management's optimism and aggressive expansion plans in the already oversupplied Jiangsu (where 10 of its 13 pipeline developments for 2015 onwards are based). Our concerns are also underpinned by the backdrop of a deteriorating retail environment in China. We believe that in a sluggish retail environment, having such a large development pipeline and hefty capex (2015E CNY1.6bn, 2016E+ CNY1.5bn per year), will place a large strain on the company's balance sheet, which, based on our forecasts, will see negative cash flows in 2015-17. Management also emphasised the development of its controllable merchandise mix (Wonderplace, Xess, etc.), and aims to grow the number of brands in this category from 47 to over 200 in the next 2-3 years. However, we note that its direct-sales margin fell by 50bps YoY to 17.8% in 2014, coming in below its concessionaire rate of 18.2%. Thus, we believe any shifts to more direct sales would be more margin-dilutive than accretive.

■ What we recommend

Given that we have raised our core EPS forecasts on the back of a better product mix, we raise our 12-month target price to HKD8.0 (formerly 6-month TP of HKD7.4), on an unchanged 2015E PER of 10x, the stock's past-2-year average. We also introduce our 2017 forecasts. We reiterate our Sell (5) rating as we

remain sceptical over management's plan, given its aggressive expansion pipeline. Due to the deteriorating macro backdrop, we believe there is more downside than upside for earnings revisions. Key risk: faster-than-expected sales growth in Mainland China.

■ How we differ

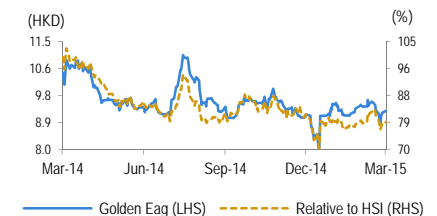
We believe the market is too optimistic about the company's private label initiatives and its plans to develop shopping malls. Accordingly, our 2015-17E EPS is slightly below consensus.

Forecast revisions (%)

| Year to 31 Dec | 15E | 16E | 17E |
|----------------------|-----|------|------|
| Revenue change | 9.6 | 20.6 | n.a. |
| Net profit change | 2.8 | 10.7 | n.a. |
| Core EPS (FD) change | 7.3 | 15.5 | n.a. |

Source: Daiwa forecasts

Share price performance



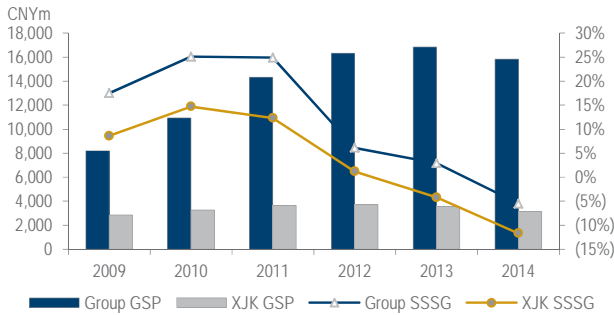
| | |
|------------------------------|-----------------------------------|
| 12-month range | 8.07-11.06 |
| Market cap (USDbn) | 2.15 |
| 3m avg daily turnover (USDm) | 3.62 |
| Shares outstanding (m) | 1,807 |
| Major shareholder | Mr. Roger Wang and family (74.8%) |

Financial summary (CNY)

| Year to 31 Dec | 15E | 16E | 17E |
|--------------------------|-------|-------|-------|
| Revenue (m) | 4,124 | 4,665 | 5,028 |
| Operating profit (m) | 1,493 | 1,638 | 1,733 |
| Net profit (m) | 1,152 | 1,198 | 1,203 |
| Core EPS (fully-diluted) | 0.635 | 0.661 | 0.663 |
| EPS change (%) | 6.7 | 4.0 | 0.4 |
| Daiwa vs Cons. EPS (%) | (0.7) | (3.3) | (2.5) |
| PER (x) | 11.7 | 11.2 | 11.2 |
| Dividend yield (%) | 3.4 | 3.6 | 3.6 |
| DPS | 0.254 | 0.264 | 0.265 |
| PBR (x) | 2.2 | 2.0 | 1.8 |
| EV/EBITDA (x) | 9.8 | 8.9 | 8.4 |
| ROE (%) | 20.0 | 18.5 | 16.7 |

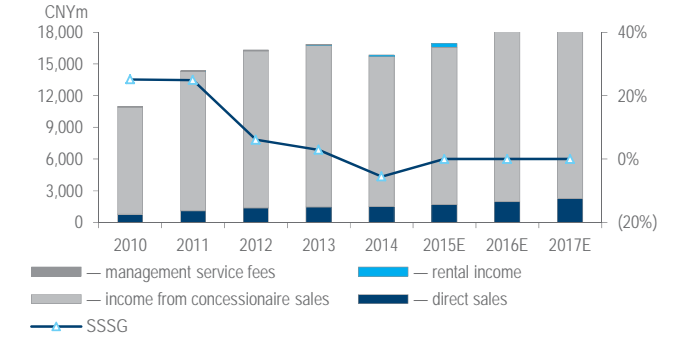
Source: FactSet, Daiwa forecasts

■ Golden Eagle: Group and flagship GSP and SSSG



Source: Company

■ Golden Eagle: Revenue breakdown by segment



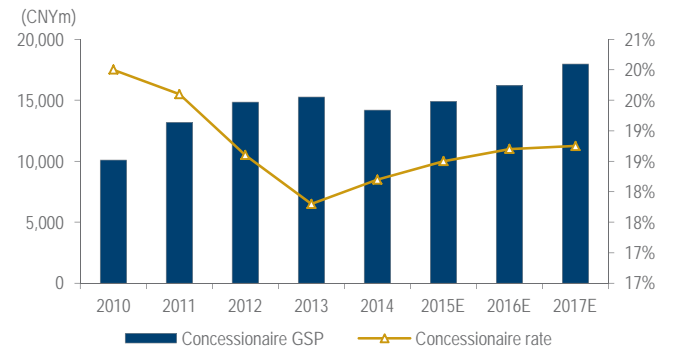
Source: Company, Daiwa forecasts

■ Golden Eagle: Development pipeline (2015 onwards)

| Upcoming new stores | Owned / Leased | Year | |
|-------------------------------|------------------|----------------|------------------|
| | | 2015 | 2016 |
| Jiangning, Nanjing | Leased | 144,710 | |
| Ma'anshan, Anhui | Leased | 87,568 | |
| Xinjiekou Block B, Additional | Managed | 23,800 | |
| Wujiang, Jiangsu | Owned | 57,800 | |
| Suzhou2, Jiangsu | Owned | | 176,764 |
| Danyang Additional, Jiangsu | Leased | 58,100 | |
| Changzhou3, Jiangsu | Leased | 60,000 | |
| Chuzhou, Anhui | Managed | 50,000 | |
| Hexi, Nanjing | Owned/Managed | 274,000 | |
| Xianlin Additional, Nanjing | Owned | 150,100 | |
| Xuzhou Additiona, Jiangsu | Owned/Managed | 58,800 | |
| Jiangdu, Yangzhou (JV) | Owned | | 250,000 |
| Xi'an 3, Shaanxi | Leased | | 62,500 |
| Total | 1,454,142 | 313,878 | 1,140,264 |
| % Year End GFA Increase | | 21% | 62% |
| % of Owned Property (GFA) | | 54% | 60% |
| Estimated Capex (RMBbn) | | 1.6 | 2 |

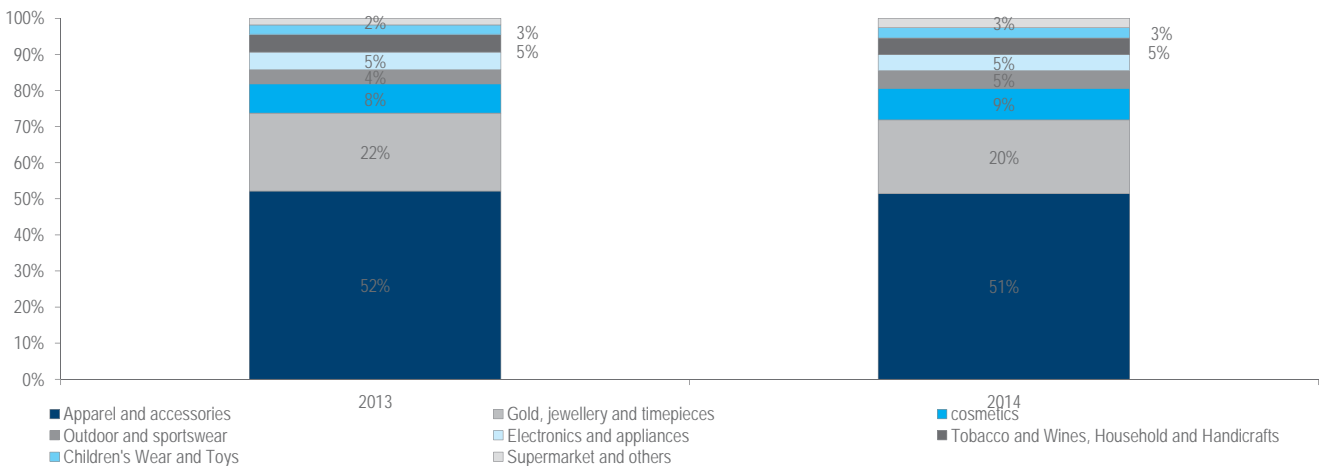
Source: Company

■ Golden Eagle: Concession sales growth and rates



Source: Company, Daiwa forecasts

■ Golden Eagle: GSP breakdown by product category



Source: Company

Financial summary

■ Key assumptions

| Year to 31 Dec | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E | 2017E |
|---------------------|------|------|------|------|-------|-------|-------|-------|
| GSP YoY growth (%) | 33.7 | 31.0 | 13.8 | 3.1 | (5.9) | 6.8 | 9.1 | 4.6 |
| Concession Rate (%) | 20.0 | 19.6 | 18.6 | 17.8 | 18.2 | 18.5 | 18.7 | 18.8 |
| Combined GPm (%) | 20.2 | 19.6 | 18.5 | 17.8 | 18.2 | 18.2 | 18.2 | 18.2 |

■ Profit and loss (CNYm)

| Year to 31 Dec | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E | 2017E |
|-----------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Concession Income | 1,729 | 2,204 | 2,363 | 2,320 | 2,213 | 2,358 | 2,571 | 2,665 |
| Direct Sales Income | 676 | 957 | 1,172 | 1,245 | 1,271 | 1,447 | 1,658 | 1,816 |
| Other Revenue | 45 | 55 | 88 | 95 | 142 | 319 | 436 | 547 |
| Total Revenue | 2,450 | 3,217 | 3,623 | 3,660 | 3,625 | 4,124 | 4,665 | 5,028 |
| Other income | 111 | 138 | 211 | 233 | 285 | 348 | 425 | 519 |
| COGS | (525) | (764) | (964) | (1,017) | (1,045) | (1,186) | (1,359) | (1,489) |
| SG&A | (311) | (431) | (519) | (546) | (616) | (724) | (877) | (956) |
| Other op.expenses | (479) | (627) | (794) | (815) | (926) | (1,068) | (1,214) | (1,369) |
| Operating profit | 1,246 | 1,533 | 1,557 | 1,515 | 1,323 | 1,493 | 1,638 | 1,733 |
| Net-interest inc./(exp.) | 33 | 73 | 68 | 80 | 100 | 100 | 100 | 100 |
| Assoc/forex/extraord./others | 18 | 19 | 23 | 113 | 115 | 115 | 115 | 115 |
| Pre-tax profit | 1,297 | 1,626 | 1,648 | 1,708 | 1,538 | 1,708 | 1,854 | 1,948 |
| Tax | (337) | (414) | (430) | (473) | (458) | (556) | (655) | (745) |
| Min. int./pref. div./others | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net profit (reported) | 959 | 1,212 | 1,217 | 1,235 | 1,080 | 1,152 | 1,198 | 1,203 |
| Net profit (adjusted) | 959 | 1,212 | 1,217 | 1,235 | 1,080 | 1,152 | 1,198 | 1,203 |
| EPS (reported)(CNY) | 0.494 | 0.623 | 0.629 | 0.655 | 0.598 | 0.638 | 0.663 | 0.666 |
| EPS (adjusted)(CNY) | 0.494 | 0.623 | 0.629 | 0.655 | 0.598 | 0.638 | 0.663 | 0.666 |
| EPS (adjusted fully-diluted)(CNY) | 0.489 | 0.618 | 0.625 | 0.652 | 0.596 | 0.635 | 0.661 | 0.663 |
| DPS (CNY) | 0.148 | 0.186 | 0.187 | 0.202 | 0.238 | 0.254 | 0.264 | 0.265 |
| EBIT | 1,246 | 1,533 | 1,557 | 1,515 | 1,323 | 1,493 | 1,638 | 1,733 |
| EBITDA | 1,364 | 1,672 | 1,738 | 1,710 | 1,557 | 1,790 | 1,992 | 2,142 |

■ Cash flow (CNYm)

| Year to 31 Dec | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E | 2017E |
|----------------------------------|----------------|----------------|----------------|----------------|--------------|----------------|----------------|----------------|
| Profit before tax | 1,297 | 1,626 | 1,648 | 1,708 | 1,538 | 1,708 | 1,854 | 1,948 |
| Depreciation and amortisation | 119 | 139 | 181 | 194 | 228 | 297 | 354 | 410 |
| Tax paid | (280) | (362) | (477) | (470) | (470) | (556) | (655) | (745) |
| Change in working capital | 797 | 744 | 193 | (32) | 34 | 183 | 198 | 133 |
| Other operational CF items | (18) | (72) | (57) | (151) | (607) | (0) | (0) | (0) |
| Cash flow from operations | 1,914 | 2,074 | 1,488 | 1,250 | 722 | 1,632 | 1,750 | 1,745 |
| Capex | (1,147) | (985) | (1,033) | (328) | (1,062) | (1,600) | (1,500) | (1,500) |
| Net (acquisitions)/disposals | (1,211) | (1,539) | (769) | (2,051) | 0 | 0 | 0 | 0 |
| Other investing CF items | 269 | (159) | 83 | 1 | 608 | 0 | 0 | 0 |
| Cash flow from investing | (2,089) | (2,683) | (1,720) | (2,378) | (454) | (1,600) | (1,500) | (1,500) |
| Change in debt | 189 | 1,059 | 1,771 | 1,410 | 1,002 | 0 | 0 | 0 |
| Net share issues/(repurchases) | (8) | (25) | (196) | (944) | (416) | 0 | 0 | 0 |
| Dividends paid | (208) | (290) | (367) | (353) | (522) | (461) | (479) | (481) |
| Other financing CF items | 0 | (1) | (90) | (172) | (179) | 0 | 0 | 0 |
| Cash flow from financing | (27) | 744 | 1,119 | (58) | (114) | (461) | (479) | (481) |
| Forex effect/others | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Change in cash | (202) | 134 | 887 | (1,186) | 154 | (429) | (229) | (236) |
| Free cash flow | 767 | 1,089 | 455 | 922 | (340) | 32 | 250 | 245 |

Source: FactSet, Daiwa forecasts

Financial summary continued ...

■ Balance sheet (CNYm)

| As at 31 Dec | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E | 2017E |
|---------------------------------------|--------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Cash & short-term investment | 1,819 | 1,953 | 2,840 | 1,666 | 1,820 | 1,390 | 1,161 | 926 |
| Inventory | 213 | 304 | 399 | 355 | 439 | 500 | 565 | 609 |
| Accounts receivable | 211 | 248 | 387 | 408 | 484 | 550 | 622 | 671 |
| Other current assets | 954 | 1,877 | 2,387 | 4,351 | 3,662 | 3,662 | 3,662 | 3,662 |
| Total current assets | 3,197 | 4,383 | 6,013 | 6,779 | 6,405 | 6,102 | 6,011 | 5,868 |
| Fixed assets | 2,722 | 3,906 | 4,025 | 4,047 | 5,933 | 7,236 | 8,382 | 9,473 |
| Goodwill & intangibles | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other non-current assets | 2,061 | 3,053 | 3,748 | 4,278 | 4,180 | 4,180 | 4,180 | 4,180 |
| Total assets | 7,979 | 11,343 | 13,787 | 15,104 | 16,518 | 17,519 | 18,573 | 19,520 |
| Short-term debt | 458 | 1,484 | 1,079 | 0 | 3,116 | 3,116 | 3,116 | 3,116 |
| Accounts payable | 1,719 | 2,063 | 2,085 | 2,055 | 2,249 | 2,559 | 2,894 | 3,120 |
| Other current liabilities | 2,027 | 3,101 | 3,043 | 3,178 | 3,159 | 3,159 | 3,159 | 3,159 |
| Total current liabilities | 4,204 | 6,648 | 6,207 | 5,233 | 8,525 | 8,835 | 9,170 | 9,396 |
| Long-term debt | 0 | 0 | 2,132 | 4,494 | 2,420 | 2,420 | 2,420 | 2,420 |
| Other non-current liabilities | 95 | 125 | 150 | 130 | 157 | 157 | 157 | 157 |
| Total liabilities | 4,299 | 6,773 | 8,489 | 9,858 | 11,102 | 11,412 | 11,747 | 11,973 |
| Share capital | 197 | 198 | 197 | 189 | 185 | 185 | 185 | 185 |
| Reserves/R.E./others | 3,483 | 4,369 | 5,098 | 5,055 | 5,225 | 5,917 | 6,636 | 7,358 |
| Shareholders' equity | 3,680 | 4,567 | 5,295 | 5,244 | 5,411 | 6,102 | 6,821 | 7,543 |
| Minority interests | 0 | 3 | 3 | 2 | 5 | 5 | 5 | 5 |
| Total equity & liabilities | 7,979 | 11,343 | 13,787 | 15,104 | 16,518 | 17,519 | 18,573 | 19,520 |
| EV | 12,034 | 12,929 | 13,768 | 16,225 | 17,116 | 17,545 | 17,774 | 18,010 |
| Net debt/(cash) | (1,361) | (469) | 370 | 2,828 | 3,716 | 4,146 | 4,375 | 4,611 |
| BVPS (CNY) | 1.895 | 2.349 | 2.734 | 2.784 | 2.995 | 3.378 | 3.775 | 4.175 |

■ Key ratios (%)

| Year to 31 Dec | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E | 2017E |
|--------------------------------|-------|------|------|-------|--------|-------|-------|-------|
| Sales (YoY) | 32.4 | 31.3 | 12.6 | 1.0 | (0.9) | 13.8 | 13.1 | 7.8 |
| EBITDA (YoY) | 29.1 | 22.6 | 3.9 | (1.6) | (8.9) | 14.9 | 11.3 | 7.5 |
| Operating profit (YoY) | 30.0 | 23.1 | 1.5 | (2.7) | (12.7) | 12.9 | 9.7 | 5.7 |
| Net profit (YoY) | 282.3 | 26.3 | 0.4 | 1.4 | (12.5) | 6.7 | 4.0 | 0.4 |
| Core EPS (fully-diluted) (YoY) | 259.8 | 26.3 | 1.2 | 4.4 | (8.7) | 6.7 | 4.0 | 0.4 |
| Gross-profit margin | 78.6 | 76.3 | 73.4 | 72.2 | 71.2 | 71.2 | 70.9 | 70.4 |
| EBITDA margin | 55.7 | 52.0 | 48.0 | 46.7 | 43.0 | 43.4 | 42.7 | 42.6 |
| Operating-profit margin | 50.8 | 47.7 | 43.0 | 41.4 | 36.5 | 36.2 | 35.1 | 34.5 |
| Net profit margin | 39.1 | 37.7 | 33.6 | 33.7 | 29.8 | 27.9 | 25.7 | 23.9 |
| ROAE | 29.1 | 29.4 | 24.7 | 23.4 | 20.3 | 20.0 | 18.5 | 16.7 |
| ROAA | 13.7 | 12.5 | 9.7 | 8.5 | 6.8 | 6.8 | 6.6 | 6.3 |
| ROCE | 34.0 | 30.1 | 21.4 | 16.6 | 12.8 | 13.2 | 13.7 | 13.6 |
| ROIC | 52.9 | 35.6 | 23.5 | 15.9 | 10.8 | 10.4 | 9.9 | 9.2 |
| Net debt to equity | n.a. | n.a. | 7.0 | 53.9 | 68.7 | 67.9 | 64.1 | 61.1 |
| Effective tax rate | 26.0 | 25.5 | 26.1 | 27.7 | 29.8 | 32.5 | 35.3 | 38.3 |
| Accounts receivable (days) | 23.7 | 26.1 | 32.0 | 39.6 | 44.9 | 45.7 | 45.9 | 46.9 |
| Current ratio (x) | 0.8 | 0.7 | 1.0 | 1.3 | 0.8 | 0.7 | 0.7 | 0.6 |
| Net interest cover (x) | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Net dividend payout | 30.1 | 29.9 | 29.7 | 30.8 | 39.8 | 39.8 | 39.8 | 39.8 |
| Free cash flow yield | 5.7 | 8.1 | 3.4 | 6.9 | n.a. | 0.2 | 1.9 | 1.8 |

Source: FactSet, Daiwa forecasts

■ Company profile

Golden Eagle Retail Group Limited is principally engaged in the development and operation of stylish department stores in The People's Republic of China (PRC) with a focus on Jiangsu province. Nanjing Xinjiekou Store is the company's flagship store. The company was listed on the Hong Kong Stock Exchange on 21 March 2006.

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