

### COMPANY UPDATE

## Xtep International Holdings (1368 HK)

Sales Target Met And Inventories Normalised; Aiming For Double-digit Revenue Growth In 2024

The core Xtep brand recorded >30% retail sell-through growth in 4Q23, bringing the full-year sell-through growth to >20%, meeting the company's target. Although discounts deepened to about 30% mainly due to inventory clearance, inventory turnover returned to a healthy level. Management projects double-digit revenue growth in 2024. Maintain BUY but cut target price by 16% to HK\$8.00 to reflect the slower growth in 2023 and industry headwinds of destocking and rising competition.

### WHAT'S NEW

- Xtep International Holdings (Xtep) announced its 4Q23 operational updates.

### STOCK IMPACT

- 2023 sales target met; targeting double-digit revenue growth in 2024.** The core Xtep brand achieved >30% retail sell-through yoy growth in 4Q23, with offline performance surpassing that of online. This brought the full-year sell-through growth to >20% and met annual sales target. For 2024, management aims to lower the price band of the core Xtep brand by launching more value-for-money products (key focus on products within the price range of Rmb200-400 vs currently Rmb300-500), in order to brave the tepid consumption recovery and the intensifying competition in the mass market. Management targets the company to resume double-digit revenue growth in 2024, assuming that consumption recovery remains on track.
- Inventories back to normal by 4Q23.** Discounts deepened by low single-digit qoq to ~30% off (vs 25-30% off in 3Q23 and ~30% off in 4Q22), mainly due to inventory clearance. As of end-4Q23, inventory turnover had improved to 4-4.5 months (vs 4.5-5 months at end -3Q23), with new products (six months or less) accounting for >70%. Inventory value declined to Rmb1.8b (vs Rmb2.4b at end-2Q23), exceeding management's expectations.
- Expect Palladium to break even in 2024.** New brands performed well in 2023, with Saucony's and Merrell's sales doubling and K-Swiss' and Palladium's sales achieving mid-teens% growth globally. Management expects new brands to maintain the fast growth momentum in 2024, targeting 30-40% sales growth for Saucony and Merrell and double-digit sales growth for K-Swiss and Palladium. Furthermore, management expects Palladium China to achieve breakeven in 2024.

### KEY FINANCIALS

Year to 31 Dec (Rmbm)	2021	2022	2023F	2024F	2025F
Net turnover	10,013	12,930	14,508	16,377	18,448
EBITDA	1,550	1,688	1,923	2,178	2,497
Operating profit	1,396	1,464	1,670	1,915	2,224
Net profit (rep./act.)	908	922	1,050	1,224	1,430
Net profit (adj.)	908	922	1,050	1,224	1,430
EPS (Fen)	35.5	35.7	39.8	46.4	54.2
PE (x)	9.8	9.8	8.8	7.5	6.4
P/B (x)	1.1	1.1	1.0	0.9	0.9
EV/EBITDA (x)	5.2	4.8	4.2	3.7	3.3
Dividend yield (%)	0.1	0.1	0.1	0.1	0.1
Net margin (%)	9.1	7.1	7.2	7.5	7.7
Net debt/(cash) to equity (%)	(14.8)	0.6	(7.8)	(11.6)	(14.4)
Interest cover (x)	24.5	18.5	18.0	23.0	25.1
ROE (%)	11.9	11.1	12.0	13.0	14.1
Consensus net profit	-	-	1,073	1,307	1,564
UOBKH/Consensus (x)	-	-	0.98	0.94	0.91

Source: Xtep Int'l Holdings, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	HK\$3.81
Target Price	HK\$8.00
Upside	+110.0%
(Previous TP)	HK\$9.50

### COMPANY DESCRIPTION

Founded in 2001, Xtep is a leading international sporting goods company in China. While dedicated to the production of professional sports goods, Xtep insists on the unique positioning of sports fashion and provides consumers with sports goods with both individuality and cost performance through the differentiated marketing strategy of dual track of sports and entertainment.

### STOCK DATA

GICS sector	Consumer Discretionary
Bloomberg ticker:	1368 HK
Shares issued (m):	2,641.5
Market cap (HK\$m):	10,064.0
Market cap (US\$m):	1,287.9
3-mth avg daily t'over (US\$m):	8.0

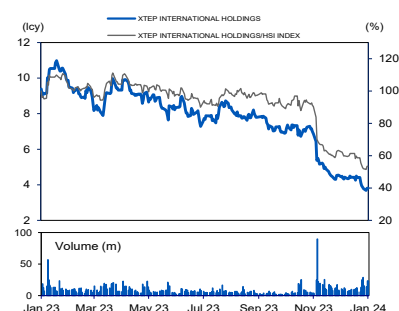
### Price Performance (%)

52-week high/low	HK\$10.98/HK\$3.68			
<b>1mth</b>	<b>3mth</b>	<b>6mth</b>	<b>1yr</b>	<b>YTD</b>
(16.3)	(44.8)	(47.7)	(59.9)	(13.6)

### Major Shareholders

	%
Success group corporation limited	46.65
FY24 NAV/Share (Rmb)	3.70
FY24 Net Cash/Share (Rmb)	0.43

### PRICE CHART



Source: Bloomberg

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### EARNINGS REVISION/RISK

- **Cut 2023-24 earnings by 10%/7%.** For 2023, we maintain our revenue estimate unchanged. We cut our gross margin estimate by 0.7ppt to reflect the deepened discounts due to inventory clearance, and raise our SG&A estimate by 0.5ppt to reflect the higher A&P fees due to the intensifying industry competition. Thus, our earnings estimate is cut by 10%. For 2024, we also maintain our revenue estimate unchanged, but cut our gross margin estimate by 0.5ppt to reflect the ongoing industry deepening discounts and the lowered price band. We also raise our SG&A estimate by 0.4ppt to reflect the higher A&P fees due to the Olympics. Thus, our earnings estimate is cut by 7%.
- **Risks include:** a) lower-than-expected sales recovery; and b) higher A&P expenses.

### VALUATION/RECOMMENDATION

- **Maintain BUY; cut target price by 16% to HK\$8.00.** Given the current sportswear industry's ongoing destocking in the short term, we revise up Xtep's WACC to 13.0% from 10.5% to reflect the industry's higher risk premium, and we roll over the target price to 2024. Our new target price is HK\$8.00, 16% lower than the previous target price. The stock currently trades at 7.5x 2024F PE.

### XTEP RETAIL SELL-THROUGH GROWTH RATE (YOY)

	Retail Sell-through Growth	Retail Discount (% off)	Retail Inventory Turnover
1Q21	(+) Mid-fifties	25-30%	4.5 months
2Q21	(+) 30-35%	20-25%	4 months
3Q21	(+) Mid-teens	20-25%	4 months
4Q21	(+) 20-25%	20-25%	4 months
1Q22	(+) 30-35%	~ 25%	4 months
2Q22	(+) Mid-teens	25-30%	-4.5 months
3Q22	(+) 20-25%	25-30%	4.5-5 months
4Q22	(-) High-SD	~ 30%	-5.5 months
1Q23	(+) ~ 20%	25-30%	<5 months
2Q23	(+) High-teens	~ 25%	<5 months
3Q23	(+) High-teens	25-30%	4.5-5 months
4Q23	(+) >30%	~ 30%	4-4.5 months

Source: Xtep, UOB Kay Hian

### DCF VALUATION

Rmbm	2024F	2025F	2026F	2027F	2028F	2029F	2030F	2031F	2032F	2033F	2034F
EBIT	1,903	2,212	2,512	2,764	3,053	3,356	3,687	4,049	4,445	4,878	5,351
D&A	263	273	278	277	276	273	265	251	234	219	205
Capex	-346	-346	-270	-270	-270	-200	-200	-100	-100	-100	-100
W.C. change	-177	-340	-461	-566	-621	-248	-697	-407	-796	-871	-953
FCFF	1,015	1,069	1,229	1,293	1,431	2,073	1,839	2,458	2,317	2,517	2,738
NPV of FCFF	1,015	946	962	896	877	1,124	882	1,043	870	836	805
PV of terminal value	7,443										
Enterprise value	17,698										
Net debt	-1,131										
MI	40										
<b>Equity value</b>	<b>18,789</b>										
# of shares O/S (in m)	2,637										
Value per share (Rmb)	7.10										
<b>Value per share (HK\$)</b>	<b>8.00</b>										

Source: Xtep, UOB Kay Hian

### PROFIT & LOSS

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Net turnover	12,930.4	14,508.4	16,376.8	18,448.2
EBITDA	1,688.3	1,922.6	2,178.4	2,496.9
Deprec. & amort.	224.0	252.3	263.1	272.6
EBIT	1,464.3	1,670.3	1,915.4	2,224.3
Associate contributions	(12.1)	(12.0)	(12.0)	(12.0)
Net interest income/(expense)	(91.2)	(106.9)	(94.8)	(99.6)
Pre-tax profit	1,361.0	1,551.4	1,808.5	2,112.7
Tax	(448.7)	(511.8)	(596.6)	(697.0)
Minorities	9.4	10.6	12.0	14.0
Net profit	921.7	1,050.2	1,223.9	1,429.7
Net profit (adj.)	921.7	1,050.2	1,223.9	1,429.7

### CASH FLOW

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Operating	571.8	1,056.7	1,297.9	1,348.4
Pre-tax profit	11,355.0	1,551.4	1,808.5	2,112.7
Tax	(524.0)	(511.8)	(596.6)	(697.0)
Deprec. & amort.	239.4	252.3	263.1	272.6
Working capital changes	(678.2)	(235.2)	(177.1)	(340.0)
Non-cash items	43.9	0.0	0.0	0.0
Other operating cashflows	(9,864.3)	0.0	0.0	0.0
Investing	(872.6)	159.8	(346.0)	(346.0)
Capex (growth)	(365.0)	(200.0)	(200.0)	(200.0)
Investments	(4.7)	354.3	(146.0)	(146.0)
Proceeds from sale of assets	(458.9)	0.0	0.0	0.0
Others	(44.1)	5.4	0.0	0.0
Financing	(236.1)	(1,299.6)	(284.3)	(426.5)
Dividend payments	(550.4)	(460.8)	(525.1)	(611.9)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	364.1	1,500.0	1,500.0	1,500.0
Loan repayment	0.0	(2,338.8)	(1,259.2)	(1,314.6)
Others/interest paid	(49.9)	0.0	0.0	0.0
Net cash inflow (outflow)	(536.9)	(83.1)	667.6	575.9
Beginning cash & cash equivalent	3,929.8	3,414.2	3,331.0	3,998.6
Changes due to forex impact	21.2	0.0	0.0	0.0
Ending cash & cash equivalent	3,414.2	3,331.0	3,998.6	4,574.5

### BALANCE SHEET

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Fixed assets	1,367.5	1,424.6	1,475.7	1,521.4
Other LT assets	2,787.7	3,052.0	3,083.8	3,111.5
Cash/ST investment	3,414.2	3,331.0	3,998.6	4,574.5
Other current assets	8,922.0	9,178.1	9,952.9	10,949.1
<b>Total assets</b>	<b>16,491.4</b>	<b>16,985.7</b>	<b>18,511.0</b>	<b>20,156.5</b>
ST debt	2,338.8	1,259.2	1,314.6	1,357.2
Other current liabilities	4,305.6	4,832.2	5,430.0	6,086.2
LT debt	1,127.1	1,367.8	1,553.2	1,696.0
Other LT liabilities	415.0	415.0	415.0	415.0
Shareholders' equity	8,470.1	9,059.4	9,758.2	10,576.1
Minority interest	(165.1)	51.9	40.0	26.0
<b>Total liabilities &amp; equity</b>	<b>16,491.4</b>	<b>16,985.7</b>	<b>18,511.0</b>	<b>20,156.5</b>

### KEY METRICS

Year to 31 Dec (%)	2022	2023F	2024F	2025F
<b>Profitability</b>				
EBITDA margin	13.1	13.3	13.3	13.5
Pre-tax margin	10.5	10.7	11.0	11.5
Net margin	7.1	7.2	7.5	7.7
ROA	5.9	6.3	6.9	7.4
ROE	11.1	12.0	13.0	14.1
<b>Growth</b>				
Turnover	29.1	12.2	12.9	12.6
EBITDA	8.9	13.9	13.3	14.6
Pre-tax profit	5.8	14.0	16.6	16.8
Net profit	1.5	13.9	16.5	16.8
Net profit (adj.)	1.5	13.9	16.5	16.8
EPS	0.6	11.5	16.5	16.8
<b>Leverage</b>				
Debt to total capital	29.4	22.4	22.6	22.4
Debt to equity	40.9	29.0	29.4	28.9
Net debt/(cash) to equity	0.6	(7.8)	(11.6)	(14.4)
Interest cover (x)	18.5	18.0	23.0	25.1

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