

China

ADD (no change)

Consensus ratings*: Buy 44 Hold 0 Sell 1

Current price:	Rmb173.5
Target price:	Rmb282.0
Previous target:	Rmb301.0
Up/downside:	62.5%
CGI / Consensus:	1.2%

Reuters:	601888.SS
Bloomberg:	601888 CH
Market cap:	US\$52,100m
	Rmb338,735m
Average daily turnover:	US\$315.8m
	Rmb2,031m

Current shares o/s:	1,952m
Free float:	25.6%

*Source: Bloomberg

Key changes in this note

- FY22F EPS cut by 17.5%.
- FY23F EPS cut by 16.7%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	6.5	-16	-42
Relative (%)	15.3	-1.3	-26.3

Major shareholders	% held
China National Travel Service Group	55.3

Analysts

Lei Yang

T (86) 21 6162 9676
E yanglei@chinastock.com.hk

Sun Feifei

T (86) 21 6888 8682
E sunfeifei@chinastock.com.hk

China Tourism Group Duty Free

Sustainable long-term leading position

- In FY21, sales grew by 29% yoy to Rmb67.67bn, and net profit rose by 57% yoy to Rmb9.65bn, in line with our expectations.
- Management said the Company achieved over 20% yoy growth in Jan and Feb for both sales and net profit, but the Omicron outbreak had a large effect on sales in Mar. Sales in 1Q22 fell by 7% yoy, and net profit dropped by 10% yoy, below our expectations.
- We now expect the Company's sales to grow by 10.6% in FY22F and net profit to decrease by 2.4% yoy, since we expect it to do more promotions during the Covid period to drive up sales.
- Reiterate Add with a new DCF-based TP of Rmb282.

Airport rental reductions benefit operating margin

In FY21, the Company's sales grew by 29% yoy to Rmb67.67bn, and net profit rose by 57% yoy to Rmb9.65bn, in line with our expectations. But the sales growth in 2H21 was dragged down by the pandemic rebound in 3Q21 (sales fell 3% yoy in 2H21 vs. an 84% yoy increase in 1H21). The Company's sales on Hainan Island grew by 57% yoy to Rmb47bn, and its sales contribution improved by 13% pts to 70% in FY21. Sales in the Shanghai and Beijing airports also declined by 9% yoy and 40% yoy to Rmb12.5bn and 1.9bn, respectively, in FY21, accounting for 21% of total sales. Owing to various promotions in the Hainan market in 4Q21, particularly for cosmetics products, with lower margins, the Company's overall gross margin declined by 7% pts to 33.7% in FY21. The Company's negotiations with airports resulted in Rmb3.1bn in rental reductions in FY21, so the sales and distribution expenses ratio declined by 11% pts to 5.7%. The Company's net profit margin improved by 2.6% pts to 14.3% in FY21.

Omicron will have a large impact on 2Q22F sales

Management said the Company achieved over 20% yoy growth in Jan and Feb, for both sales and net profit. However, the Omicron outbreak had a big impact on sales in Mar, leading to a 7% yoy 1Q22 sales decline. The Company's gross margin improved qoq to 34% in 1Q22, and management expects the overall GPM to gradually improve yoy in FY22 through product structure improvement. According to the Hainan government, owing to the current Omicron outbreak, the number of tourists visiting Hainan dropped by 36% yoy in Mar after 13% yoy growth in Feb. We expect Hainan's sales to be lackluster in 2Q22F and to rebound in 2H22F. We now expect the Company's sales to grow by 10.6% yoy in FY22F and net profit to decrease by 2.4% yoy.

Actively exploring long-term growth opportunities

The Company will attract more traffic volume to Hainan Island from areas unaffected by the pandemic. The phase one project of its logistics center, covering 50k sqm is complete, which will improve its shipment capacity on Hainan Island. In 2021, the Company successfully introduced 12 cosmetics brands, 30 shoe and apparel brands, 62 exclusive products, and 26 limited edition products to meet demand from young consumers. The Haikou International Duty-Free shopping mall will be opened on 30 Sep 2022, and so far, the Company has recruited over 500 brands. It now has 22m members in the WeChat app and aims to increase this to 26m in FY22F. Its member repurchase rate has increased significantly. The Company won duty-free operation rights for the Suifenhe railway port, Taiyuan airport and Quanzhou shipping port, and opened new duty-free stores in another four city airports in Chengdu, Qingdao, Ningbo and Yiwu. The Company also signed strategic agreements for downtown duty-free stores in Wuhan, Chendu, Xian, Tianjing and Huzhou. We expect the Company to maintain its leading position in China's duty-free market and to attract more traffic volume to Hainan Island.

Financial Summary

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue (Rmbm)	52,597	67,676	74,835	95,648	116,325
Operating EBITDA (Rmbm)	10,107	15,103	14,688	20,278	26,386
Net Profit (Rmbm)	6,140	9,654	9,422	12,907	16,752
Core EPS (Rmb)	3.54	5.20	4.86	6.65	8.62
Core EPS Growth	59.8%	47.1%	(6.6%)	36.7%	29.6%
FD Core P/E (x)	49.04	33.34	35.68	26.10	20.13
DPS (Rmb)	1.00	1.50	1.46	2.01	2.60
Dividend Yield	0.58%	0.86%	0.84%	1.16%	1.50%
EV/EBITDA (x)	32.40	21.85	22.22	15.90	11.95
P/FCFE (x)	72.95	56.35	37.09	32.35	21.72
Net Gearing	(54.6%)	(37.2%)	(43.6%)	(46.5%)	(51.2%)
P/BV (x)	15.18	11.44	9.38	7.34	5.74
ROE	32.7%	39.1%	28.9%	31.6%	32.0%
% Change In Core EPS Estimates			(22.6%)	(21.4%)	
CGI/consensus EPS (x)			0.75	0.75	0.82

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Sustainable long-term leading position

Reiterate Add with a new DCF-based TP of Rmb282

We cut our EPS forecasts for FY22F–23F by 17.5% and 16.7%, respectively, to reflect our concern that the current Omicron situation will impact the Company's sales in 2Q22F and that the uncertainty about the travel policy relaxation will delay the tourism market recovery in the near term. However, we reiterate our Add rating for the Company because we believe that the recent pandemic outbreak is a temporary issue and that the Company's expansion on Hainan Island will become a significant revenue driver in the long term. The Company has also actively sought overseas expansion opportunities to expand in the Southeast Asia market. A potential catalyst is policy relaxation for downtown duty-free stores. A downside risk is unclear policy on Hainan's duty-free market from 2025 on.

Figure 1: CDF quarterly financial summary

(Rmb m)	1Q21	2Q21	3Q21	4Q21	1Q22	YoY	FY20	FY21	YoY
Revenue	18,134	17,392	13,973	18,177	16,782	-7%	52,597	67,676	29%
YoY(%)	137%	49%	-12%	4%	-7%		10%	29%	
Gross profit incl tax	6,577	6,044	4,029	4,303	5,218	-21%	20,293	20,954	3%
Other income	28	215	87	112	52	87%	230	441	92%
Sales and distribution expense	-1,773	-1,525	1,236	-1,800	-1,461	-18%	-8,847	-3,861	-56%
General administrative expense	-431	-447	-398	-974	-431	0%	-1,637	-2,250	37%
Operating profit	4,402	4,288	4,954	1,641	3,377	-23%	10,039	15,284	52%
Net profit	2,849	2,510	3,132	1,163	2,563	-10%	6,140	9,654	57%
YoY (%)	NA	139%	40%	-61%	-10%		33%	57%	
Margins						ppt chg			ppt chg
Gross profit margin excl: sales tax	39.1%	37.5%	31.3%	26.4%	34.0%	-5.1%	40.6%	33.7%	-7.0%
Sales tax	2.8%	2.8%	2.4%	2.8%	2.9%	0.1%	2.1%	2.7%	0.7%
Gross profit margin incl: sales tax	36.3%	34.8%	28.8%	23.7%	31.1%	-5.2%	38.6%	31.0%	-7.6%
S&D expense ratio	9.8%	8.8%	-8.8%	9.9%	8.7%	-1.1%	16.8%	5.7%	-11.1%
G&A expense ratio	2.4%	2.6%	2.9%	5.4%	2.6%	0.2%	3.1%	3.3%	0.2%
Operating profit margin (%)	24.3%	24.7%	35.5%	9.0%	20.1%	-4.1%	19.1%	22.6%	3.5%
Net profit margin (%)	15.7%	14.4%	22.4%	6.4%	15.3%	-0.4%	11.7%	14.3%	2.6%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Figure 2: Earnings revision

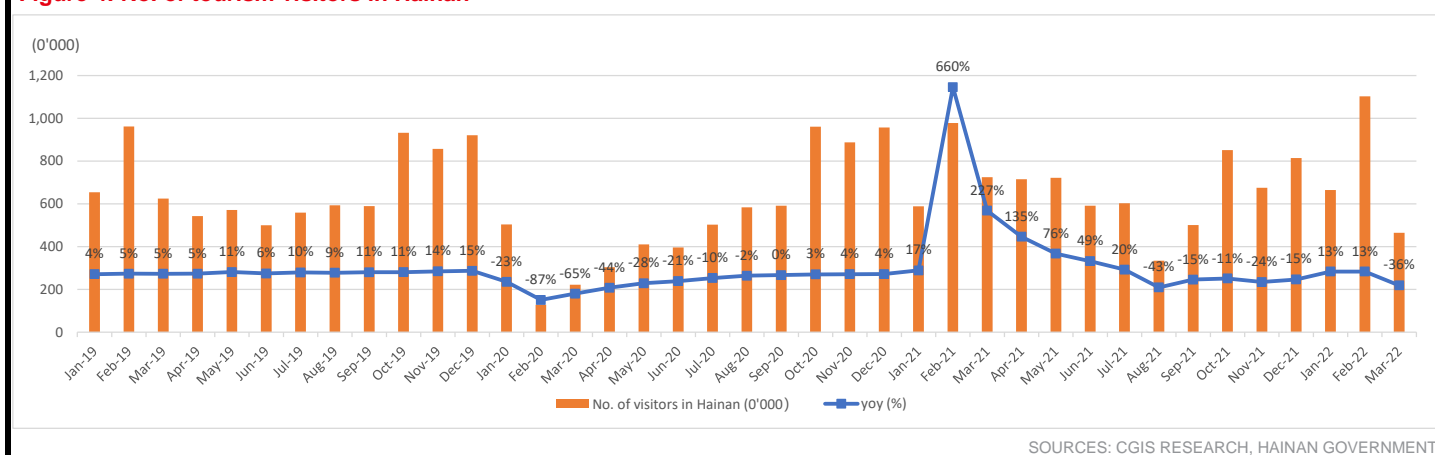
(Rmb m)	FY22F			FY23F			FY24F
	Old	New	% change	Old	New	% change	New
Revenue	80,897	74,835	-7.5%	102,961	95,648	-7.1%	116,325
yoy growth	20%	11%	-9.0%	27%	28%	0.5%	22%
Gross profit	25,868	23,544	-9.0%	33,747	30,858	-8.6%	38,460
GPM	32.0%	31.5%	-0.5%	32.8%	32.3%	-0.5%	33.1%
Operating profit	16,755	14,396	-14.1%	22,711	19,739	-13.1%	25,635
Reported net profit	11,416	9,422	-17.5%	15,504	12,907	-16.7%	16,752
yoy growth	19.0%	-2.4%	-21.4%	35.8%	37.0%	1.2%	29.8%

SOURCES: CGIS RESEARCH

Figure 3: Duty-free sales in Hainan since the policy stimulus in July 2020

Period	Duty free sales (Rmb, 0'000)	No. of actual duty free shoppers (0'000)	Ticket size (Rmb)
3Q20	860,576	129	6,670
4Q20	1,137,974	170	6,684
1Q21	1,357,113	179	7,598
2Q21	1,319,583	204	6,477
3Q21	877,746	131	6,714
4Q21	1,392,521	158	8,791
1Q22	1,471,554	176	8,372

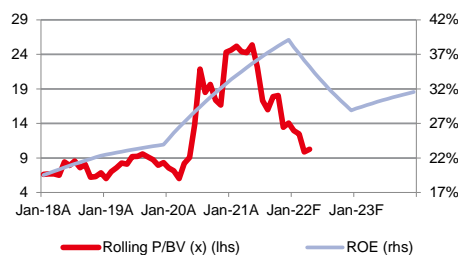
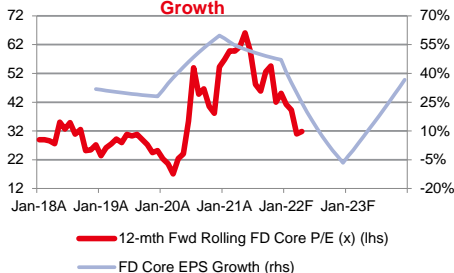
SOURCES: CGIS RESEARCH, HAINAN CUSTOMS, DEPARTMENT OF COMMERCE OF HAINAN PROVINCE

Figure 4: No. of tourism visitors in Hainan

Figure 5: DCF valuation

(Rmb, m)	FY22F	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F
Operating EBIT	14,396	19,739	25,635	30,219	36,148	42,878	50,003	57,813	66,264	74,626
Taxes	-2,378	-3,258	-4,229	-4,975	-5,951	-7,059	-8,232	-9,518	-10,909	-12,286
EBIT, tax-affected	12,018	16,481	21,407	25,244	30,197	35,819	41,771	48,295	55,355	62,340
Add: Depreciation & amortisation	291	539	751	835	915	986	1,034	1,061	938	1,057
Add Changes in Working capital	274	-3,599	-3,611	-4,356	-5,210	-6,180	-7,207	-8,333	-9,551	-10,756
Less Capital Expenditure	-3,500	-3,000	-3,000	-3,000	-2,100	-2,037	-1,976	-1,917	-1,859	-1,803
Free Cash Flow to firm	9,083	10,421	15,546	18,724	23,802	28,588	33,622	39,107	44,884	50,837
Key assumptions										
NPV of FY22-26 cash flow	56,802	Company average beta		1.0						
NPV of FY27-31 cash flow	100,163	Risk free rate		3%						
NPV of Terminal Value	382,646	Risk premium		5%						
Enterprise Value	539,611	Cost of equity		9%						
Add Net cash/(Net Debt)	16,445	Cost of Debt		4%						
Less Minority	-5,173	Debt %		0%						
Equity value of firm	550,883	Tax rate		26%						
Share outstanding (m)	1,952	WACC		9%						
Target price (Rmb)	282	Terminal growth rate		3%						

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS

P/BV vs ROE

12-mth Fwd FD Core P/E vs FD Core EPS Growth


Profit & Loss

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Net Revenues	52,597	67,676	74,835	95,648	116,325
Gross Profit	20,293	20,954	23,544	30,858	38,460
Operating EBITDA	10,107	15,103	14,688	20,278	26,386
Depreciation And Amortisation	-1,189	-782	-291	-539	-751
Operating EBIT	8,919	14,321	14,396	19,739	25,635
Financial Income/(Expense)	545	43	50	50	50
Pretax Income/(Loss) from Assoc.	0	0	0	0	0
Non-Operating Income/(Expense)	208	438	0	0	0
Profit Before Tax (pre-EI)	10,684	15,408	14,533	19,876	25,772
Exceptional Items	0	0	0	0	0
Pre-tax Profit	9,672	14,801	14,446	19,789	25,685
Taxation	-2,335	-2,437	-2,378	-3,258	-4,229
Exceptional Income - post-tax					
Profit After Tax	7,337	12,365	12,068	16,531	21,457
Minority Interests	-1,197	-2,711	-2,646	-3,624	-4,704
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	6,140	9,654	9,422	12,907	16,752
Recurring Net Profit	6,907	10,160	9,494	12,979	16,825
Fully Diluted Recurring Net Profit	6,907	10,160	9,494	12,979	16,825

Cash Flow

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
EBITDA	10,107	15,103	14,688	20,278	26,386
Cash Flow from Invt. & Assoc.					
Change In Working Capital	200	-6,494	274	-3,599	-3,611
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	-2,105	-280	-2,328	-3,208	-4,179
Net Interest (Paid)/Received	0	0	0	0	0
Tax Paid					
Cashflow From Operations	8,202	8,329	12,633	13,471	18,596
Capex	-2,775	-2,216	-3,500	-3,000	-3,000
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	-1,039	-101	0	0	0
Cash Flow From Investing	-3,814	-2,318	-3,500	-3,000	-3,000
Debt Raised/(repaid)	255	0	0	0	0
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid					
Preferred Dividends	-1,658	-3,431	-2,929	-2,858	-3,916
Other Financing Cashflow	477	-38	0	0	0
Cash Flow From Financing	-927	-3,469	-2,929	-2,858	-3,916
Total Cash Generated	3,462	2,543	6,204	7,613	11,681
Free Cashflow To Equity	4,643	6,011	9,133	10,471	15,596
Free Cashflow To Firm	4,388	6,011	9,133	10,471	15,596

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS... cont'd
Balance Sheet

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Cash And Equivalents	14,706	16,856	23,061	30,673	42,354
Total Debtors	1,532	1,961	1,968	2,091	2,211
Inventories	14,733	19,725	19,051	24,350	29,614
Total Other Current Assets	0	0	0	0	0
Total Current Assets	30,971	38,542	44,080	57,114	74,179
Fixed Assets	1,591	1,843	5,138	7,686	10,022
Total Investments	3,305	5,078	5,078	5,078	5,078
Intangible Assets	3,271	3,224	3,137	3,051	2,964
Total Other Non-Current Assets	2,781	6,787	6,787	6,787	6,787
Total Non-current Assets	10,948	16,932	20,140	22,602	24,851
Short-term Debt	417	411	411	411	411
Current Portion of Long-Term Debt					
Total Creditors	9,322	12,394	12,002	13,825	15,598
Other Current Liabilities	5,922	4,330	4,330	4,330	4,330
Total Current Liabilities	15,661	17,136	16,743	18,567	20,340
Total Long-term Debt	0	0	0	0	0
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	79	3,546	3,546	3,546	3,546
Total Non-current Liabilities	79	3,546	3,546	3,546	3,546
Total Provisions	0	0	0	0	0
Total Liabilities	15,741	20,682	20,290	22,113	23,886
Shareholders' Equity	22,308	29,619	36,112	46,160	58,997
Minority Interests	3,871	5,173	7,818	11,443	16,147
Total Equity	26,179	34,791	43,930	57,603	75,144

Key Ratios

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue Growth	9.7%	28.7%	10.6%	27.8%	21.6%
Operating EBITDA Growth	49.5%	49.4%	(2.7%)	38.1%	30.1%
Operating EBITDA Margin	19.2%	22.3%	19.6%	21.2%	22.7%
Net Cash Per Share (Rmb)	7.32	6.64	9.81	13.71	19.70
BVPS (Rmb)	11.43	15.17	18.50	23.64	30.22
Gross Interest Cover	N/A	N/A	N/A	N/A	N/A
Effective Tax Rate	24.1%	16.5%	16.5%	16.5%	16.5%
Net Dividend Payout Ratio	27.3%	28.5%	30.1%	30.1%	30.2%
Accounts Receivables Days	3.23	0.63	0.57	0.56	0.58
Inventory Days	129.1	134.6	138.0	122.3	126.8
Accounts Payables Days	44.55	39.87	40.85	35.69	36.58
ROIC (%)	110%	172%	86%	100%	100%
ROCE (%)	43.6%	47.2%	33.6%	36.4%	36.7%
Return On Average Assets	21.5%	26.5%	20.2%	23.0%	24.0%

Key Drivers

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Airport duty free sales growth (%)	-37.5%	-10.2%	-8.4%	16.5%	19.3%
Hainan offshore sales growth (%)	186.3%	57.2%	18.8%	31.9%	22.5%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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619 companies under coverage for quarter ended on 31 Dec 2021		
	Rating Distribution (%)	Investment Banking clients (%)
Add	71.1%	1.5%
Hold	21.8%	0.0%
Reduce	7.1%	0.0%

Spitzer Chart for stock being researched (2 year data)

China Tourism Group Duty Free (601888 CH)

RECOMMENDATION FRAMEWORK

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