

### COMPANY UPDATE

## Li Ning Company (2331 HK)

Leading In The Revival Of Domestic Sports Brands

**We believe sportswear demand has been delayed by the spreading pandemic. Li Ning maintained its guidance of a high-teen to low-twenties sales growth in 2022. We believe Li Ning is leading in the revival of domestic sports brands. Its high-quality products backed by rising R&D abilities and high operational efficiency would continue to drive earnings growth ahead. Maintain BUY with a target price of HK\$96.00.**

### WHAT'S NEW

- **New store opening plan in 2022.** Li Ning Company (Li Ning) plans to open ~250 Li Ning mass product stores, 150-200 Li Ning Young stores, 10-20 Li Ning 1990 stores, and dozens (vs 93 in 2021) of China Li Ning stores in 2022. Moreover, it will open 300-400 (vs ~400 in 2021) large-sized (>300sqm) stores with high operational efficiency in 2022, which will be mainly in the shopping malls. It will continue to open the large-sized and high-efficient stores in the future.
- **Demand exists despite pandemic.** Despite the continued spread of the pandemic, Li Ning sees a relatively stable supply chain nationwide as the goods for April and May have already arrived for most of the stores while the goods for June have arrived for some stores. Unlike restaurant operations, we believe demand for sportswear would remain solid and be only delayed by the spreading pandemic.

### STOCK IMPACT

- **Best representative in revival of domestic sports brands.** Thanks to the fashion show held on the Tmall China Day during the New York Fashion Week in Feb 18, China Li Ning became the pioneer of the revival of domestic sports brands. We believe that: a) the company's abundant top-tier sports resources (eg China national sports teams, Wade), and b) its ability to expand crossover resources (eg Dunhuang Fashion week in the desert in Aug 20, and Fashion Music Festival in Dec 21) would allow the Li Ning brand to reach diverse segments of consumers and enlarge its customer base. Hence, this would strengthen brand recognition of Li Ning and its leading position among domestic sports brands.
- **Increasing R&D competence.** Beng (震) technology can offer 80% energy feedback, and Jiang (强) technology can provide a quick rebound and the protection to body joints during running. The two technologies are considered to be the first-class globally. Li Ning plans to expand the usage of Beng technology to mid-to-low tier running shoes, and other segments' products (eg basketball and training) in 2022. Its R&D cost saw a 24.6% 4-year CAGR in 2017-21, indicating the company's efforts in manufacturing high-quality products. We believe Li Ning's products would gain further recognition from customers and become more popular in the future.

### KEY FINANCIALS

Year to 31 Dec (HK\$m)	2020	2021	2022F	2023F	2024F
Net turnover	14,457	22,572	26,830	32,731	39,609
EBITDA	2,838	5,841	6,692	8,206	10,203
Operating profit	1,834	4,736	5,534	6,990	8,922
Net profit (rep./act.)	1,698	4,011	4,700	5,849	7,370
Net profit (adj.)	1,698	4,011	4,700	5,849	7,370
EPS (sen)	67.6	158.0	185.1	230.4	290.3
PE (x)	72.6	31.1	26.5	21.3	16.9
P/B (x)	14.1	6.1	5.2	4.4	3.7
EV/EBITDA (x)	39.9	19.4	16.9	13.8	11.1
Dividend yield (%)	0.4	0.9	1.1	1.4	1.7
Net margin (%)	11.7	17.8	17.5	17.9	18.6
Net debt/(cash) to equity (%)	(69.9)	(63.3)	(62.1)	(63.0)	(60.8)
Interest cover (x)	89.8	n.a.	n.a.	n.a.	n.a.
ROE (%)	21.5	26.9	20.6	21.8	23.1
Consensus net profit	-	-	4,768	5,921	7,326
UOBKH/Consensus (x)	-	-	0.99	0.99	1.01

Source: Li Ning, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	HK\$60.45
Target Price	HK\$96.00
Upside	+58.8%
(Previous TP:	HK\$113.42)

### COMPANY DESCRIPTION

Li Ning is one of the leading sportswear companies in China. It has the main brand Li Ning and other sub-brands, including China Li Ning, Li Ning Young, Li Ning 1990.

### STOCK DATA

GICS sector	Consumer Discretionary
Bloomberg ticker:	2331 HK
Shares issued (m):	2,616.8
Market cap (HK\$m):	158,188.3
Market cap (US\$m):	20,182.2
3-mth avg daily t'over (US\$m):	165.5

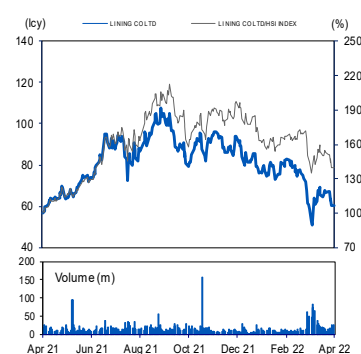
### Price Performance (%)

52-week high/low	HK\$107.70/HK\$50.95			
<b>1mth</b>	<b>3mth</b>	<b>6mth</b>	<b>1yr</b>	<b>YTD</b>
(10.9)	(20.4)	(25.3)	9.1	(29.2)

### Major Shareholders

	<b>%</b>
Viva China Holdings Limited	10.36
FY22 NAV/Share (Rmb)	9.40
FY22 Net Cash/Share (Rmb)	5.83

### PRICE CHART



Source: Bloomberg

### ANALYST(S)

**Shen Zhifeng**  
+8621 5404 7225 ext.811  
zhifeng@uobkayhian.com

**Ng Jo Yee**  
+603 2147 1984  
joyee@uobkayhian.com

- Effective channel restructure.** Li Ning started its channel restructure in 2012 and targeted to lift retail sales efficiency and achieve high-quality growth. In recent years, its efforts were mainly focused on: a) opening efficient and large-sized stores in the core cities (especially the Tier 1 & 2 cities), and closing the underperforming or loss-making stores; b) upgrading the decoration of stores that were opened before 2019 to improve consumers' purchase experiences; c) raising the franchised stores' operational efficiency based on experiences gleaned from self-operated stores; d) replicating the standardised operational model of high operational efficiency stores in all other stores. Hence, the proportion of stores in Tier 1 & 2 cities and in Tier 3 & 4 cities increased 10ppt and 3ppt respectively, and the proportion of stores in shopping malls hiked more than 15ppt as of end-21, compared with end-19. Its overall annual per store sales surged more than 60% in 2021, and the large stores' annual per store sales reached Rmb7.2m in 2021, higher than Rmb4.2m for self-operated stores and Rmb2.1m for franchised stores. Also, Li Ning will decide the sell-in plan based on the sell-through situations, which we think would lower the risks from high inventory.
- Rising direct sales with strong online sales expansion.** The share of sales revenue from franchised distributors continuously dropped to 48.1% in 2021 from 79.0% in 2011. However, its online sales recorded 55.6% 7-year CAGR in 2014-21, accounting for 28.4% of total revenue in 2021 from 4.9% in 2014. The number of online members reached 40m as of end-21, and their sales contributions increased by low-teens in 2021. In addition, the number of low-efficiency online wholesale stores declined by mid-forties in 2021. With Li Ning's effective e-commerce strategies (eg the omni-channel inventory and resources sharing), we believe its online sales would continue to grow fast in the future. The company guided for online sales to grow 20% per year in the next few years.
- Solid sales expansion with multiple drivers.** Li Ning achieved a 26.3% 4-year revenue CAGR in 2017-21, and guided for a high-teen to low-twenties top-line growth and a high-teen net profit margin for 2022. It achieved high-thirties to low-forties offline sales growth in some cities before the resurgence of the pandemic in Mar 22. It also expects a mid-single-digit revenue growth in 2Q22 despite the high base in 2Q21. The company stated that Li Ning mass products (offline) would contribute a mid-to-high single-digit in the total revenue growth in 2022, while China Li Ning and Li Ning Young would likely see 40-60% sales growth and a mid-single-digit revenue growth in 2022. With a clear and firm long-term strategy, we expect China LN and LN Young to continue the fast expansion and contribute more in the top line growth in the future.
- Expecting stable gross margins ahead.** Although the company guided a 1% drop in gross margin in 2022 given the high material costs, we reckon that Li Ning would likely see a margin recovery after 2022 thanks to its brand elevation and high operational efficiency. The potential improvement in new products' sell-out rate, retail discount rate, and the delivery discount and rebate rate to distributors would improve gross margin.
- Stable supply chain.** Li Ning's production capacity hiked 50% in 2021. It is lifting the share of orders to the core suppliers. Its top three suppliers' capacity accounted for 45% of total capacity as of end-21. We think the top suppliers would facilitate flexible production for Li Ning. Li Ning has also planned its logistics in the next 3-5 years to further lift its operational efficiency and customers' purchase experiences.

### EARNINGS REVISION/RISK

- Earnings forecasts.** We estimate 17.2%/24.4%/26.0% earnings growth for 2022/23/24.
- Risks.** a) Continuous spread of pandemic, b) costs of materials remaining high.

### VALUATION/RECOMMENDATION

- Maintain BUY with a target price of HK\$96.00.** We believe Li Ning brand is the leader in the revival of domestic sportswear brands. Its increasing R&D capabilities and operational efficiency would further strengthen Li Ning's brand power in customers' minds. Maintain BUY. Our target price implies 45.5x 2022F PE and 36.6x 2023F PE.

### PROFIT & LOSS

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
Net turnover	22,572.3	26,830.3	32,730.7	39,608.8
EBITDA	5,840.6	6,691.8	8,206.4	10,203.2
Deprec. & amort.	1,104.6	1,157.9	1,216.5	1,281.0
EBIT	4,736.0	5,533.9	6,989.8	8,922.1
Total other non-operating income	326.3	326.3	326.3	326.3
Associate contributions	159.2	170.0	172.0	175.0
Net interest income/(expense)	32.6	133.4	187.1	249.1
<b>Pre-tax profit</b>	<b>5,328.2</b>	<b>6,163.6</b>	<b>7,675.3</b>	<b>9,672.5</b>
Tax	(1,317.3)	(1,463.9)	(1,826.7)	(2,302.1)
Minorities	0.0	0.0	0.0	0.0
<b>Net profit</b>	<b>4,010.9</b>	<b>4,699.8</b>	<b>5,848.6</b>	<b>7,370.5</b>
Net profit (adj.)	4,010.9	4,699.8	5,848.6	7,370.5

### BALANCE SHEET

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
Fixed assets	1,625.9	1,692.0	1,758.1	1,824.2
Other LT assets	9,977.1	10,108.8	10,253.9	10,413.6
Cash/ST investment	14,744.9	16,660.1	19,698.6	22,471.0
Other current assets	3,927.0	6,116.8	7,291.7	10,304.1
<b>Total assets</b>	<b>30,274.8</b>	<b>34,577.7</b>	<b>39,002.3</b>	<b>45,012.8</b>
ST debt	417.1	417.1	417.1	417.1
Other current liabilities	7,286.8	8,093.1	8,079.1	8,473.8
LT debt	977.5	977.5	977.5	977.5
Other LT liabilities	489.4	489.4	489.4	489.4
Shareholders' equity	21,101.5	24,598.1	29,036.7	34,652.6
Minority interest	2.6	2.6	2.6	2.6
<b>Total liabilities &amp; equity</b>	<b>30,274.8</b>	<b>34,577.7</b>	<b>39,002.3</b>	<b>45,012.8</b>

### CASH FLOW

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
Operating	4,707.6	3,754.5	5,084.4	5,162.9
Pre-tax profit	5,328.2	6,163.6	7,675.3	9,672.5
Tax	(1,317.3)	(1,463.9)	(1,826.7)	(2,302.1)
Deprec. & amort.	571.5	571.5	571.5	571.5
Working capital changes	558.0	(1,383.5)	(1,189.0)	(2,617.7)
Non-cash items	(266.8)	(133.3)	(146.6)	(161.3)
Other operating cashflows	(166.0)	0.0	0.0	0.0
<b>Investing</b>	<b>3,085.9</b>	<b>(636.0)</b>	<b>(636.0)</b>	<b>(636.0)</b>
Capex (growth)	(1,094.7)	(600.0)	(600.0)	(600.0)
Investments	(30.7)	(36.0)	(36.0)	(36.0)
Proceeds from sale of assets	0.0	0.0	0.0	0.0
Others	4,211.3	0.0	0.0	0.0
<b>Financing</b>	<b>(235.6)</b>	<b>(1,203.3)</b>	<b>(1,409.9)</b>	<b>(1,754.6)</b>
Dividend payments	(509.5)	(1,203.3)	(1,409.9)	(1,754.6)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	0.0	0.0	0.0	0.0
Loan repayment	0.0	0.0	0.0	0.0
Others/interest paid	273.9	0.0	0.0	0.0
<b>Net cash inflow (outflow)</b>	<b>7,557.9</b>	<b>1,915.2</b>	<b>3,038.5</b>	<b>2,772.4</b>
Beginning cash & cash equivalent	7,187.0	14,744.9	16,660.1	19,698.6
Changes due to forex impact	0.0	0.0	0.0	0.0
<b>Ending cash &amp; cash equivalent</b>	<b>14,744.9</b>	<b>16,660.1</b>	<b>19,698.6</b>	<b>22,471.0</b>

### KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Profitability</b>				
EBITDA margin	25.9	24.9	25.1	25.8
Pre-tax margin	23.6	23.0	23.4	24.4
Net margin	17.8	17.5	17.9	18.6
ROA	17.9	14.5	15.9	17.5
ROE	26.9	20.6	21.8	23.1
<b>Growth</b>				
Turnover	56.1	18.9	22.0	21.0
EBITDA	105.8	14.6	22.6	24.3
Pre-tax profit	137.0	15.7	24.5	26.0
Net profit	136.1	17.2	24.4	26.0
Net profit (adj.)	136.1	17.2	24.4	26.0
EPS	133.6	17.2	24.4	26.0
<b>Leverage</b>				
Debt to total capital	6.2	5.4	4.6	3.9
Debt to equity	6.6	5.7	4.8	4.0
Net debt/(cash) to equity	(63.3)	(62.1)	(63.0)	(60.8)
Interest cover (x)	n.a.	n.a.	n.a.	n.a.

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