

Hong Kong

ADD (no change)

Consensus ratings*: Buy 50 Hold 0 Sell 1

Current price:	HK\$70.10
Target price:	HK\$113.0
Previous target:	HK\$120.0
Up/downside:	61.2%
CGI / Consensus:	29.3%
Reuters:	2331.HK
Bloomberg:	2331 HK
Market cap:	US\$23,414m
	HK\$183,513m
Average daily turnover:	US\$130.5m
	HK\$1,024m
Current shares o/s:	2,472m
Free float:	85.1%

*Source: Bloomberg

Key changes in this note

- FY22F EPS cut by 4.7%.
- FY23F EPS cut by 5.4%.
- FY24F EPS cut by 4.9%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.6	24.5	-18.9
Relative (%)	5.8	20.4	5

Major shareholders	% held
VIVA CHINA HOLDINGS LIMITED	14.9

Analyst(s)

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

Li Ning Company

Sales recovery since July

- Li Ning reported total revenue growth of 21.7% yoy to Rmb12.4bn in 1H22, in line with our expectation. Net profit grew 11.6% yoy to Rmb2,189m in 1H22, slightly lower than our expectation, due to a weaker gross margin.
- Management noted a sales recovery since July, and maintains its full-year guidance of 15–20% yoy sales growth with a net profit margin in the high teens.
- Reiterate Add, since we believe Li Ning still has large room to improve its store efficiency and margins in the long run. We lower our DCF-based TP to HK\$113 since we cut our FY22–24F EPS forecasts.

1H22 net profit slightly below expectation due to weaker GPM

Revenue grew 21.7% yoy in 1H22; wholesale, direct retail and online channels sales grew by 28.5%, 10.8% and 19.2%, respectively, yoy. The slower growth of the direct sales channel was a result of most of its stores being located in first-tier cities, which were more impacted by Covid. The GPM contracted by 5.9ppt yoy to 50.0% in 1H22, due to 1) a larger discount rate, 2) higher raw material costs, and 3) a smaller sales contribution from the direct sales and online channels, which have higher margins. But Li Ning improved control of expenses, reducing its distribution and admin expenses ratios by 0.8ppt and 0.1ppt, respectively, yoy to 27.3% and 4.2% in 1H22. Overall retail sell-through increased by 8% in 1H22. Channel inventory grew by the mid-forties in 1H22, due to larger sales size, low inventory levels last year, and the company's proactive increase in new products in the channels to prepare for a likely sales recovery in 3Q22F. Management said revenue has grown by the mid-teens yoy in 3Q22 to date.

Further efficiency improvement in 2H22F

Inventory turnover days remained healthy at 3.6 months in 1H22 vs. 3.1 and 3.9 months for 1H21 and FY21. The inventory structure also improved in 1H22, with new products within six months accounting for 88% vs. 83% in 1H21. Management expects the discount rate and inventory level to improve qoq in 3Q22F. The offline average label price increased by low-single-digits yoy in 1H22. Li Ning opened 240 stores in 1H22. The monthly store efficiency also improved by the mid-teens yoy in 1H22. Li Ning maintained its store opening plan for FY22F. The net increase in the Li Ning brand, China Li Ning, Li Ning Young and Li Ning 1990 stores will be 200–250, less than 50, 150–200 and 10–20, respectively. The speed of new store openings was a bit slow in 1H22, but it will speed this up in 2H22F (according to management in the analyst conference).

Functional products to drive growth

Li Ning facilitated its R&D investment in the past two years. The retail sell-through for running shoes and basketball products grew by 10% and 30%, respectively, yoy in 1H22, driven by strong growth of functional products. The new boom fiber shoes reached 2m pairs in 1H22, and management said (in the analyst conference) it will use this new technology in more product categories in FY22F. Li Ning Young also achieved strong growth in 1H22 with retail sell-through increasing by the mid-40s, the average label price up by the mid-teens, and monthly store efficiency growing by the mid-30s.

Reiterate Add with a lower DCF-based TP of HK\$113

We reiterate our Add rating, since we believe it has large potential to further improve its store efficiency and margins in the long run. We cut our EPS forecasts for our FY22F–24F forecasts by 4.7–5.4% to reflect gross margin pressure. The key positive catalyst is higher-than-expected sales growth in 2H22F. The key risks are weaker consumption demand and a higher discount rate, which would impact margins. We derived our TP from DCF valuation with 7% WACC and 3% terminal growth rate.

Financial Summary	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue (Rmbm)	14,457	22,572	26,910	32,626	38,564
Operating EBITDA (Rmbm)	2,768	8,331	6,108	7,797	9,341
Net Profit (Rmbm)	1,698	6,577	4,410	5,442	6,548
Normalised EPS (Rmb)	0.70	2.65	1.75	2.14	2.55
Normalised EPS Growth	12%	281%	(34%)	22%	19%
FD Normalised P/E (x)	86.53	22.74	34.43	28.18	23.65
DPS (Rmb)	0.20	0.46	0.52	0.64	0.76
Dividend Yield	0.34%	0.76%	0.87%	1.06%	1.26%
EV/EBITDA (x)	50.12	16.01	21.62	16.52	13.31
P/FCFE (x)	82.95	NA	31.29	25.43	20.18
Net Gearing	(82.3%)	(69.6%)	(75.0%)	(80.3%)	(86.3%)
P/BV (x)	17.04	7.16	6.26	5.41	4.66
ROE	21.5%	44.2%	19.4%	20.6%	21.2%
% Change In Normalised EPS Estimates			(4.99%)	(5.66%)	(5.10%)
Normalised EPS/consensus EPS (x)			0.96	0.94	0.91

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Sales recovery since July

Figure 1: Li Ning financial summary

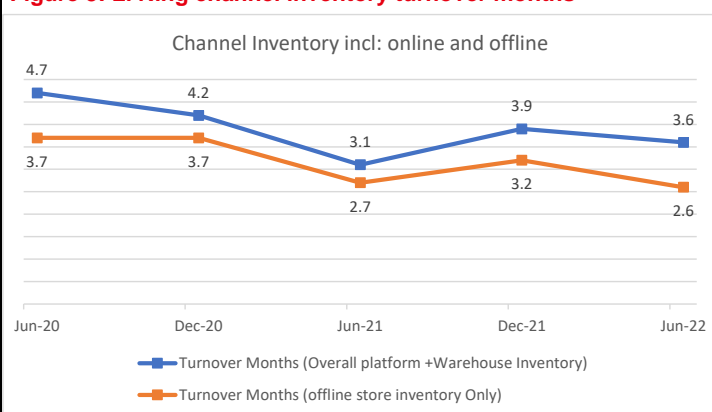
(RMB'000)	1H22	2H22F	FY22F
Revenues	12,408,665	14,501,557	26,910,222
yoy change	21.7%	17.2%	19.2%
Cost of Sales	-6,207,890	-7,496,713	-13,704,603
Gross Profit/loss	6,200,775	7,004,844	13,205,619
yoy change			88.5%
GPM	50.0%	48.3%	49.1%
yoy change			0.8%
Distribution Expenses	-3,382,990	-3,773,241	-7,156,231
Distribution expenses ratio	27.3%	26.0%	26.6%
Administrative Expenses	-518,104	-725,290	-1,243,394
Admin expenses ratio	4.2%	5.0%	4.6%
Reversal of impairment losses	7,341	8,341	15,682
Other Income and Other Gains-net	336,602	223,885	560,487
Operating Income (Loss)	2,643,624	2,722,857	5,366,481
yoy change			97.1%
OPM	21.3%	18.8%	19.9%
yoy change			1.2%
Share of Profit/loss of Investments	101,646	73,498	175,144
Finance Income	228,608	200,597	429,205
Finance Expenses	-54,877	-57,581	-112,458
Earnings before Taxes	2,919,001	2,939,371	5,858,372
EBT Margin	23.5%	20.3%	21.8%
Provision for Income Tax	-729,693	-718,726	-1,448,419
Effective tax rate	-25.00%	-24.45%	-24.72%
Net Income Attributable to Shareholders	2,189,308	2,220,645	4,409,953
yoy change	11.6%	8.4%	9.9%
NPM	17.6%	15.3%	16.4%
yoy change			-2.3%

SOURCES: CGIS RESEARCH ESTIMATES, COMPANY DATA, BLOOMBERG

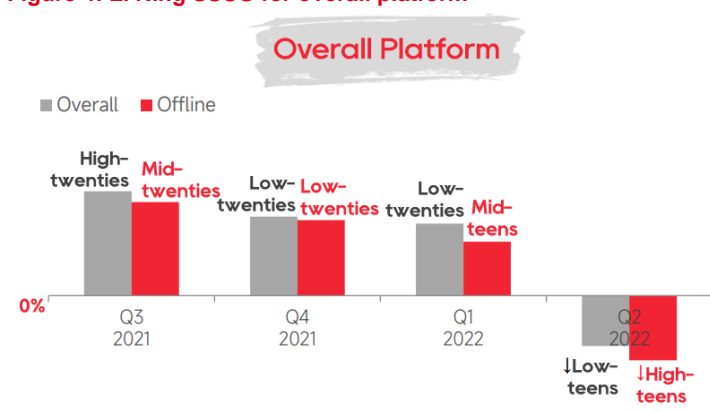
Figure 2: Earnings revision

FYE Dec (Rmb m)	FY22F			FY23F			FY24F		
	Old	New	% change	Old	New	% change	Old	New	% change
Revenue	26,910.2	26,910.2	0.0%	32,625.5	32,625.5	0.0%	38,564.0	38,564.0	0.0%
Gross margin	52.2%	49.1%	-3.1 pts	52.7%	50.4%	-2.3 pts	53.0%	50.9%	-2.1 pts
Operating margin	21.9%	19.9%	-2.0 pts	22.4%	21.2%	-1.2 pts	22.7%	21.5%	-1.2 pts
Net profit	4,626.0	4,410.0	-4.7%	5,752.8	5,442.2	-5.4%	6,884.4	6,548.1	-4.9%
Net profit margin	17.2%	16.4%	-0.8 pts	17.6%	16.7%	-0.9 pts	17.9%	17.0%	-0.9 pts

SOURCES: CGIS RESEARCH ESTIMATES, COMPANY DATA

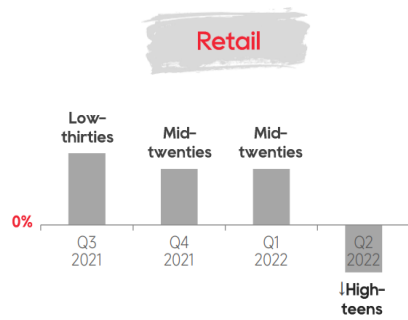
Figure 3: Li Ning channel inventory turnover months


SOURCES: CGIS RESEARCH, COMPANY DATA

Figure 4: Li Ning SSSG for overall platform


SOURCES: CGIS RESEARCH, COMPANY DATA

Figure 5: Lining SSSG for retail



SOURCES: CGIS RESEARCH, COMPANY DATA,

Figure 6: Lining SSSG for wholesale



SOURCES: CGIS RESEARCH, COMPANY DATA

Figure 7: Lining SSSG for e-commerce



SOURCES: CGIS RESEARCH, COMPANY DATA

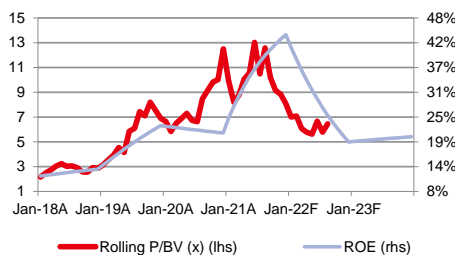
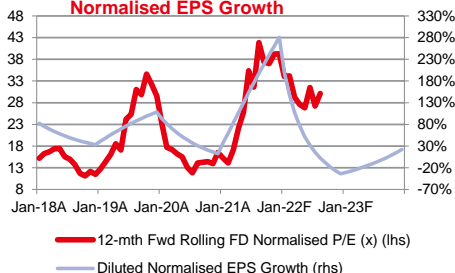
We reiterate our Add rating, since we believe it has large potential to further improve its store efficiency and margins in the long run. We cut our EPS forecasts for our FY22F–24F forecasts by 4.7–5.4% to reflect gross margin pressure. The key positive catalyst is higher-than-expected sales growth in 2H22F. The key risks are weaker consumption demand and a higher discount rate, which would impact margins. We derived our TP from DCF valuation with 9.7% WACC and 3% terminal growth rate (Rf: 3%, beta: 1, cost of equity: 10.5%, tax rate: 27%).

Figure 8: DCF valuation

(Rmb m)	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E	2032E
EBIT	5,366	6,907	8,296	9,540	10,971	12,617	14,510	16,686	19,189	22,067	25,378
Add: Depreciation & amortization	741	890	1,045	1,098	1,153	1,210	1,271	1,334	1,401	1,471	1,545
Less: Tax	1,448	1,787	2,151	2,575	2,961	3,405	3,916	4,504	5,179	5,956	6,849
Less: Capex	(985)	(985)	(985)	(1,015)	(1,045)	(1,076)	(1,109)	(1,142)	(1,176)	(1,211)	(1,248)
Less: Net change in working capital	(890)	(492)	(877)	(921)	(967)	(1,016)	(1,066)	(1,120)	(1,176)	(1,235)	(1,296)
Unlevered FCF	4,564	5,517	7,083	9,999	11,175	12,514	14,039	15,779	17,763	20,028	22,617
Terminal value											349,306
DCF	4,564	5,030	5,889	7,581	7,725	7,888	8,069	8,269	8,489	8,728	8,987
			Assumptions								
PV for the forecasted period			81,219			Risk-free Rate of Return			3.0%		
PV for the terminal value			138,793			Equity Risk Premium			7.5%		
Enterprise Value			220,012			Company Beta			1		
Minus: Net debt + Minority interest			(18,330)			Cost of Equity			10.5%		
NPV to equity shareholders			238,342			Pre-tax Cost of Debt			3.0%		
Divided by: # of shares outstanding (m)			2,530			Tax Rate			27%		
NPV per share to equity shareholders (Rmb)			94.2			After-tax Cost of Debt			2.2%		
CNY/HKD			0.83			Target debt to total capital			10.0%		
NPV per share to equity shareholders (HKD)			113.0			WACC			9.7%		
						Terminal growth ("g")			3.0%		

SOURCES: CGIS RESEARCH ESTIMATES, COMPANY DATA, BLOOMBERG

BY THE NUMBERS

P/BV vs ROE

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


Profit & Loss

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Net Revenues	14,457	22,572	26,910	32,626	38,564
Gross Profit	7,094	11,969	13,206	16,432	19,618
Operating EBITDA	2,768	8,331	6,108	7,797	9,341
Depreciation And Amortisation	(572)	(628)	(741)	(890)	(1,045)
Operating EBIT	2,196	7,703	5,366	6,907	8,296
Financial Income/(Expense)	(32)	33	317	130	191
Pretax Income/(Loss) from Assoc.	83	159	175	193	212
Non-Operating Income/(Expense)	0	0	0	0	0
Profit Before Tax (pre-EI)	2,248	7,895	5,858	7,230	8,699
Exceptional Items					
Pre-tax Profit	2,248	7,895	5,858	7,230	8,699
Taxation	(549)	(1,317)	(1,448)	(1,787)	(2,151)
Exceptional Income - post-tax					
Profit After Tax	1,698	6,577	4,410	5,442	6,548
Minority Interests	0	0	0	0	0
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Preference Dividends (Australia)					
Net Profit	1,698	6,577	4,410	5,442	6,548
Normalised Net Profit	1,698	6,577	4,410	5,442	6,548
Fully Diluted Normalised Profit	1,698	6,577	4,410	5,442	6,548

Cash Flow

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
EBITDA	2,768	8,331	6,108	7,797	9,341
Cash Flow from Inv. & Assoc.					
Change In Working Capital	551	2,636	890	492	877
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	116	19	(317)	(75)	(83)
Other Operating Cashflow	(16)	(3,891)	449	377	396
Net Interest (Paid)/Received	(66)	(112)	(112)	(112)	(112)
Tax Paid	(589)	(456)	(1,448)	(1,787)	(2,151)
Cashflow From Operations	2,763	6,525	5,568	6,691	8,269
Capex	(647)	(1,028)	(985)	(985)	(985)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(345)	(5,511)	269	324	393
Cash Flow From Investing	(992)	(6,539)	(716)	(661)	(592)
Debt Raised/(repaid)	0	0	0	0	0
Proceeds From Issue Of Shares	189	8,612	0	0	0
Shares Repurchased					
Dividends Paid	0	0	0	0	0
Preferred Dividends					
Other Financing Cashflow	(703)	(1,016)	(1,264)	(1,435)	(1,745)
Cash Flow From Financing	(513)	7,596	(1,264)	(1,435)	(1,745)
Total Cash Generated	1,258	7,583	3,588	4,595	5,932
Free Cashflow To Equity	1,772	(13)	4,852	6,031	7,677
Free Cashflow To Firm	1,838	99	4,965	6,143	7,790

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	7,187	14,745	18,333	22,928	28,860
Total Debtors	1,243	1,752	1,925	2,491	2,720
Inventories	1,346	1,773	2,258	2,505	3,067
Total Other Current Assets	1	402	402	402	402
Total Current Assets	9,777	18,672	22,918	28,326	35,049
Fixed Assets	1,065	1,626	1,908	2,041	2,019
Total Investments	1,101	1,437	1,538	1,648	1,770
Intangible Assets	191	188	147	106	65
Total Other Non-Current Assets	2,460	8,353	8,425	8,610	8,807
Total Non-current Assets	4,817	11,603	12,018	12,406	12,662
Short-term Debt	39	50	50	50	50
Current Portion of Long-Term Debt	0	0	0	0	0
Total Creditors	3,737	5,633	6,863	8,093	9,679
Other Current Liabilities	1,239	2,021	2,151	2,487	2,848
Total Current Liabilities	5,015	7,704	9,064	10,631	12,577
Total Long-term Debt	0	0	0	0	0
Hybrid Debt - Debt Component	0	0	0	0	0
Total Other Non-Current Liabilities	787	1,040	1,040	1,040	1,040
Total Non-current Liabilities	787	1,040	1,040	1,040	1,040
Total Provisions	103	427	469	579	697
Total Liabilities	5,904	9,171	10,573	12,250	14,314
Shareholders' Equity	8,687	21,102	24,360	28,479	33,395
Minority Interests	3	3	3	3	3
Total Equity	8,689	21,104	24,362	28,482	33,397

Key Ratios					
	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue Growth	4.2%	56.1%	19.2%	21.2%	18.2%
Operating EBITDA Growth	38%	201%	(27%)	28%	20%
Operating EBITDA Margin	19.1%	36.9%	22.7%	23.9%	24.2%
Net Cash Per Share (Rmb)	2.91	5.87	7.23	8.95	11.16
BVPS (Rmb)	3.54	8.42	9.63	11.14	12.94
Gross Interest Cover	33.15	68.49	47.72	61.42	73.77
Effective Tax Rate	24.4%	16.7%	24.7%	24.7%	24.7%
Net Dividend Payout Ratio	29.8%	17.3%	29.3%	29.0%	28.7%
Accounts Receivables Days	17.03	12.63	13.35	13.11	13.10
Inventory Days	68.42	53.67	53.67	53.67	53.82
Accounts Payables Days	64.01	48.65	48.65	48.65	48.78
ROIC (%)	260%	579%	83%	114%	149%
ROCE (%)	27.8%	51.6%	24.9%	26.5%	27.2%
Return On Average Assets	12.7%	29.2%	12.6%	14.0%	14.4%

Key Drivers					
	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total number of stores	6,933.0	7,137.0	7,437.0	7,737.0	8,037.0
Overall SSSG (%)	4.2%	56.1%	19.2%	21.2%	18.2%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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643 companies under coverage for quarter ended on 30 Jun 2022		
	Rating Distribution (%)	Investment Banking clients (%)
Add	68.4%	0.8%
Hold	24.6%	0.0%
Reduce	7.0%	0.2%

Spitzer Chart for stock being researched (2 year data)

Li Ning Company (2331 HK)

— Price Close



RECOMMENDATION FRAMEWORK

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