

China / Hong Kong Company Update

Shenzhou International

Bloomberg: 2313 HK EQUITY | Reuters: 2313.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

27 Mar 2024

BUY

Last Traded Price (26 Mar 2024): HK\$65.80 (HSI : 16,618)
Price Target 12-mth: HK\$94.30 (43% upside) (Prev HK\$98.00)

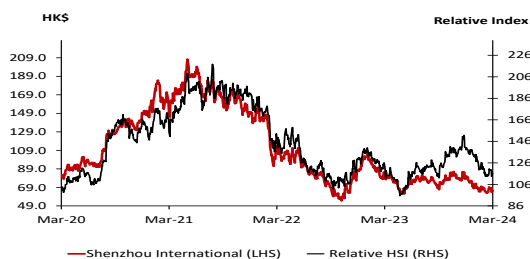
Analyst

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What's New

- 2023 results largely in line with expectations; payout higher at 60.3%
- 2024 guidance unchanged with topline to grow 12-15% y-o-y, driven by a recovery in sportswear and casual wear orders
- Maintain BUY, TP adjusted lower to HK\$94.3

Price Relative



Forecasts and Valuation

FY Dec (RMBm)	2022A	2023A	2024F	2025F
Turnover	27,781	24,970	28,122	31,133
EBITDA	5,366	5,095	6,107	7,025
Pre-tax Profit	5,262	4,996	5,874	6,838
Net Profit	4,563	4,557	5,227	6,017
Net Pft (Pre Ex) (core profit)	4,563	4,557	5,227	6,017
Net Profit Gth (Pre-ex) (%)	35.3	(0.1)	14.7	15.1
EPS (RMB)	3.04	3.03	3.48	4.00
EPS (HK\$)	3.29	3.29	3.77	4.34
Core EPS (RMB)	3.04	3.03	3.48	4.00
Core EPS (HK\$)	3.29	3.29	3.77	4.34
EPS Gth (%)	35.3	(0.1)	14.7	15.1
Core EPS Gth (%)	35.3	(0.1)	14.7	15.1
Diluted EPS (HK\$)	3.29	3.29	3.77	4.34
DPS (HK\$)	1.81	2.01	2.45	2.82
BV Per Share (HK\$)	22.18	23.71	25.49	27.55
PE (X)	20.0	20.0	17.5	15.2
CorePE (X)	20.0	20.0	17.5	15.2
P/Cash Flow (X)	19.7	16.1	18.0	15.2
P/Free CF (X)	26.6	21.9	27.0	22.1
EV/EBITDA (X)	16.2	17.0	14.1	12.1
Net Div Yield (%)	2.7	3.1	3.7	4.3
P/Book Value (X)	3.0	2.8	2.6	2.4
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE(%)	14.8	13.9	14.8	15.8
Earnings Rev (%)			1	n.a.
Consensus EPS (RMB)			3.72	4.39
Other Broker Recs:		B:42	S:0	H:1

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Actively driving growth

Investment Thesis

Largest integrated fabrics & garment manufacturer in China. As a key supplier for global brands including Nike, Uniqlo, Adidas, Puma, and more, Shenzhou Int'l (Shenzhou)'s diversified production bases in China and Asia, as well as its strong manufacturing capability in integrating fabric and garment production, should enable it to continue to gain market share, especially in the sportswear segment. We forecast the Group to achieve sales and earnings CAGR of 12% and 15% respectively in FY23-25E.

Downstream inventory levels still high but easing sequentially. We expect gradual restocking from the sportswear and casual wear categories in 2024. Sportswear revenue accounted for 72.2% of sales. Top 4 customers, comprising of Adidas, Nike, Puma and Uniqlo accounted for 79.6% of 2023 sales (2022: 82%)

FY24E earnings poised for rebound. We expect Shenzhou to record 12% topline recovery, driven by sportswear and casual wear orders. We expect GP margin to expand by 1.2ppt to reflect gradual improvement, driven by higher utilisation rates from overseas capacity.

Buy with target price of HK\$94.3. We raise our FY24E forecast by 1% on improving GP margin assumptions, but lower our TP to HK\$94.3, based on 26x FY26F PE (previously 28x), on sector derating, supported by >3.7% yield. The company's strategy is pivoting towards expanding its capacity in Southeast Asia, with new plants planned in Indonesia. This will enable the company to meet brand customers' requirements to diversify their sourcing needs.

Key Risks

Key risks include macroeconomic headwinds, high inventory levels amongst apparel brand owners, unfavourable currency fluctuation, raw materials (such as cotton and polyester) cost fluctuation, and lastly, rise in trade tariffs between its trading partners.

At A Glance

Issued Capital (m shrs)	1,503
Mkt Cap (HKm/US\$m)	98,897 / 12,641
Major Shareholders (%)	
Keep Glory Limited	42.4
Free Float (%)	57.6
3m Avg. Daily Val. (US\$m)	31.8
GICS Industry: Consumer Discretionary / Consumer Durables & Apparel	

Shenzhou International

WHAT'S NEW

FY23 earnings in line

Shenzhou (2313.HK)'s FY23 net earnings declined marginally by 0.1% to Rmb4,557m, in line with market expectations. FY23 revenue dropped 10% to Rmb24,970m. Sportswear sales declined by 13.6% y-o-y, due to falling demand from sportswear products in the EU and US, followed by a decline in casual wear by 1.4%, while knitwear sales plunged 41.6% due to discontinuation of mask production in 2023, with some offset from lingerie wear products (+30.2% y-o-y). Despite slower revenue, GP margin expanded by 2.2ppts to 24.3% driven by gradual improvement in overseas factories with lower fixed operating cost per unit product. Effective tax rate dropped to 8.8% (2022: 13.3%), with the shift in production to overseas. The company declared a final DPS of HK\$1.08 (+27% y-o-y). With interim DPS of HK0.95/sh, total DPS for FY23 stood at HK2.03/sh, an increase of 6% y-o-y, with dividend payout higher at 60.3%, reverting to 2021 levels. (2022: c.56.2%).

By geography, Europe and US sales declined 19.1% and 20.4% respectively amounting to 20.1% and 15.6% of total sales, dragged by weaker sportswear demand. Followed by Japan and Other sales decline of 6.4% and 7.6% y-o-y respectively. Japan sales were dragged by a decline in casual wear procurement demand, and the suspension of sales of mask products. China domestic market recorded a 0.7% increase in sales, with sales contribution arising to 28.5% of total (2022: 25.5%), mainly driven by the increase in procurement demand for casual wear in the domestic market.

Rising overseas output. In 2023, garment output from overseas factories accounted for 53% of total output (2022: 46%). Of which, Cambodia garment output expanded by 4ppts to 26% in 2023. The average number of employees at the overseas bases accounted for 57% of the total in 2023 (2022: 52%). The company continues to improve its product range by providing accessories, and printing and embroidery services to overseas factories to improve deliveries and shorten the lead time.

The company maintained its earlier guidance of 12-15% topline growth in 2024, driven by order recovery for sportswear and

casual wear. The company noted that 1Q24 orderbook trend is largely positive without providing any details. Given there are concerns regarding the recent guidance from core and emerging customers, Nike and Lululemon, we have prudently adjusted our topline expectations to the lower end of the guidance. On the other hand, it is positive to note Lululemon has become an emerging customer, indicating Shenzhou's strength to take on new clients and gradual diversification in customer portfolio. We are still positive on the recovery in the sector, with largely healthy inventory levels across the brand operators as well as at the company level while short-lead times continue to favour the larger manufacturers. The company maintains its capex at between Rmb1.5-2bn, mainly targeting capacity expansion in Indonesia. In terms of workers by demographic basis, the company has added 3000 workers post CNY, giving a total of >40,000 workers in China (Ningbo & Anhui), with possibility to add another 2,000 later in the year. Cambodia has roughly 22k workers, while Vietnam has 95,000 workers with potential to increase this year. We raise our FY24E forecasts by 1% on adjustment on GP margin, and adjust our TP to HK\$94.3, based on 26x FY24F PE (previously 28x), on sector derating.

Company Background

Shenzhou International is China's largest vertically integrated knitwear manufacturer. The company is primarily engaged in the production of premium knitwear (sportswear, casual wear, and lingerie) on an Original Equipment Manufacturer (OEM) basis, with production facilities located in China, Vietnam, and Cambodia (total capacity of c.500m pieces/year of various knitwear). The company boasts of renowned clients such as Nike, Adidas, and Uniqlo.

Shenzhou International

Interim Income Statement (RMBm)

FY Dec	2H2022	1H2023	2H2023	% chg yoy	% chg hoh
Revenue	14,189	11,562	13,408	(5.5)	16.0
Cost of Goods Sold	(11,128)	(8,967)	(9,943)	(10.7)	10.9
Gross Profit	3,060	2,595	3,465	13.2	33.5
Other Oper. (Exp)/Inc	(1,032)	(995)	(1,051)	1.8	5.6
Operating Profit	2,029	1,600	2,414	19.0	50.9
Other Non Opg (Exp)/Inc	412	558	(49)	nm	nm
Associates & JV Inc	(15)	11	2	nm	(78.4)
Net Interest (Exp)/Inc	68	180	279	313.2	55.6
Exceptional Gain/(Loss)	0	0	0	nm	nm
Pre-tax Profit	2,494	2,348	2,647	6.2	12.7
Tax	(298)	(222)	(217)	(27.3)	(2.2)
Minority Interest	1	0	0	nm	nm
Net Profit	2,196	2,127	2,430	10.7	14.3
Net profit bef Except.	2,196	2,127	2,430	10.7	14.3
EBITDA	2,785	2,295	2,800	0.5	22.0
Margins (%)					
Gross Margins	21.6	22.4	25.8		
Opg Profit Margins	14.3	13.8	18.0		
Net Profit Margins	15.5	18.4	18.1		

Source: Company, DBS HK

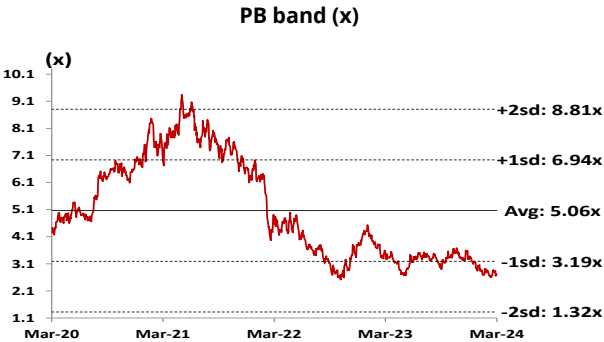
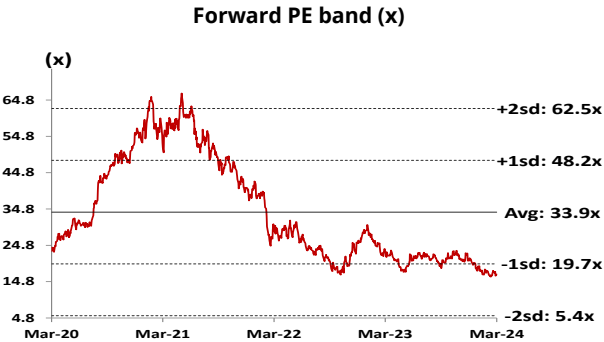
Income Statement (RMB m)

FY Dec	2022A	2023A	% cha vov
Revenue	27,781	24,970	(10.1)
Cost of Goods Sold	(21,656)	(18,910)	(12.7)
Gross Profit	6,126	6,060	(1.1)
Other Opng (Exp)/Inc	(2,159)	(2,045)	(5.2)
Operating Profit	3,967	4,014	1.2
Other Non Opg (Exp)/Inc	1,233	509	(58.7)
Associates & JV Inc	(21)	13	nm
Net Interest (Exp)/Inc	83	459	450.2
Exceptional Gain/(Loss)	0	0	nm
Pre-tax Profit	5,262	4,996	(5.1)
Tax	(699)	(438)	(37.3)
Minority Interest	0	0	nm
Net Profit	4,563	4,557	(0.1)
Net Profit before Except.	4,563	4,557	(0.1)
EBITDA	5,366	5,095	(5.0)
Margins & Ratio			
Gross Margins (%)	22.1	24.3	
Opg Profit Margin (%)	14.3	16.1	
Net Profit Margin (%)	16.4	18.3	

Source: Company, DBS HK

Shenzhou International

Historical PE and PB band



Source: Thomson Reuters, DBS HK

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Segmental Breakdown (RMB m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Revenues (RMB m)					
Sports wear	17,612	20,870	18,032	20,556	22,817
Casual wear	4,721	5,752	5,673	6,297	6,989
Lingerie wear	1,040	819	1,067	1,067	1,120
Other knitwear	472	341	199	203	207
Total	23,845	27,781	24,970	28,122	31,133

Source: Company, DBS HK

Income Statement (RMB m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Revenue	23,845	27,781	24,970	28,122	31,133
Cost of Goods Sold	(18,055)	(21,656)	(18,910)	(20,932)	(22,862)
Gross Profit	5,790	6,126	6,060	7,191	8,272
Other Opng (Exp)/Inc	(2,210)	(2,159)	(2,045)	(2,109)	(2,335)
Operating Profit	3,579	3,967	4,014	5,081	5,937
Other Non Opng (Exp)/Inc	124	1,233	509	514	520
Associates & JV Inc	7	(21)	13	13	13
Net Interest (Exp)/Inc	113	83	459	265	369
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	3,823	5,262	4,996	5,874	6,838
Tax	(452)	(699)	(438)	(646)	(821)
Minority Interest	0	0	0	0	(1)
Preference Dividend	0	0	0	0	0
Net Profit	3,372	4,563	4,557	5,227	6,017
Net Profit before Except.	3,372	4,563	4,557	5,227	6,017
EBITDA	4,736	5,366	5,095	6,107	7,025
Growth					
Revenue Gth (%)	3.5	16.5	(10.1)	12.6	10.7
EBITDA Gth (%)	(26.7)	13.3	(5.0)	19.9	15.0
Opg Profit Gth (%)	(33.8)	10.8	1.2	26.6	16.8
Net Profit Gth (%)	(34.0)	35.3	(0.1)	14.7	15.1
Margins & Ratio					
Gross Margins (%)	24.3	22.1	24.3	25.6	26.6
Opg Profit Margin (%)	15.0	14.3	16.1	18.1	19.1
Net Profit Margin (%)	14.1	16.4	18.3	18.6	19.3
ROAE (%)	12.1	14.8	13.9	14.8	15.8
ROA (%)	8.0	10.5	9.4	9.7	10.2
ROCE (%)	9.0	11.5	11.0	10.9	11.4
Div Payout Ratio (%)	60.1	54.9	61.2	65.0	65.0
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS HK

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Interim Income Statement (RMB m)

FY Dec	2H2021	1H2022	2H2022	1H2023	2H2023
Revenue	12,476	13,593	14,189	11,562	13,408
Cost of Goods Sold	(10,059)	(10,527)	(11,128)	(8,967)	(9,943)
Gross Profit	2,417	3,066	3,060	2,595	3,465
Other Oper. (Exp)/Inc	(1,183)	(1,127)	(1,032)	(995)	(1,051)
Operating Profit	1,235	1,938	2,029	1,600	2,414
Other Non Opg (Exp)/Inc	(4)	821	412	558	(49)
Associates & JV Inc	2	(7)	(15)	11	2
Net Interest (Exp)/Inc	60	16	68	180	279
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	1,293	2,768	2,494	2,348	2,647
Tax	(147)	(401)	(298)	(222)	(217)
Minority Interest	0	(1)	1	0	0
Net Profit	1,145	2,367	2,196	2,127	2,430
Net profit bef Except.	1,145	2,367	2,196	2,127	2,430
Growth					
Revenue Gth (%)	(2.5)	19.6	13.7	(14.9)	(5.5)
Opg Profit Gth (%)	(60.7)	(17.3)	64.3	(17.5)	19.0
Net Profit Gth (%)	(55.8)	6.3	91.7	(10.1)	10.7
Margins					
Gross Margins (%)	19.4	22.6	21.6	22.4	25.8
Opg Profit Margins (%)	9.9	14.3	14.3	13.8	18.0
Net Profit Margins (%)	9.2	17.4	15.5	18.4	18.1

Source: Company, DBS HK

Shenzhou International

Balance Sheet (RMB m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Net Fixed Assets	11,130	11,594	10,931	11,634	12,455
Invt in Associates & JVs	601	574	13	13	13
Other LT Assets	3,892	5,161	9,187	9,146	9,105
Cash & ST Invt	12,215	13,725	16,872	20,033	23,534
Inventory	6,636	6,261	6,125	7,326	8,002
Debtors	3,502	5,005	5,024	5,067	5,609
Other Current Assets	4,158	1,174	459	459	459
Total Assets	42,132	43,493	48,611	53,678	59,177
ST Debt	10,212	7,198	10,204	10,204	10,204
Creditors	1,387	932	1,198	1,256	1,372
Other Current Liab	1,934	2,130	1,982	1,982	1,982
LT Debt	483	2,087	2,011	4,544	7,078
Other LT Liabilities	333	381	349	349	349
Shareholder's Equity	27,771	30,753	32,867	35,342	38,192
Minority Interests	12	13	0	0	1
Total Cap. & Liab.	42,132	43,493	48,611	53,678	59,177
Non-Cash Wkg. Capital	10,975	9,378	8,427	9,614	10,716
Net Cash/(Debt)	1,519	4,440	4,657	5,285	6,252
Debtors Turn (avg days)	53.6	65.8	73.4	65.8	65.8
Creditors Turn (avg days)	29.9	16.8	24.5	23.0	23.0
Inventory Turn (avg days)	143.3	112.8	125.4	134.3	134.1
Asset Turnover (x)	0.6	0.6	0.5	0.5	0.5
Current Ratio (x)	2.0	2.6	2.1	2.4	2.8
Quick Ratio (x)	1.2	1.8	1.6	1.9	2.1
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	19.9	12.9	12.3	11.4	10.8
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

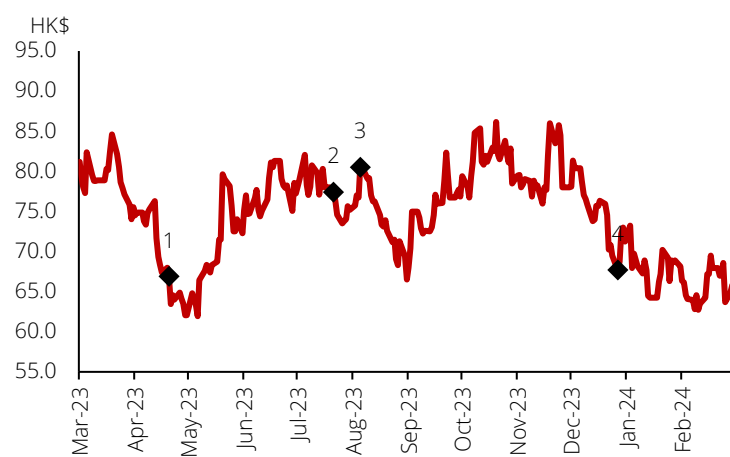
Cash Flow Statement (RMB m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Pre-Tax Profit	3,823	5,262	4,996	5,874	6,838
Dep. & Amort.	1,156	1,399	1,081	1,026	1,088
Tax Paid	(282)	(508)	(438)	(646)	(821)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	2	0	0	0	0
Chg in Wkg.Cap.	(831)	(1,584)	384	(1,187)	(1,102)
Other Operating CF	(274)	59	(359)	0	0
Net Operating CF	3,594	4,628	5,663	5,067	6,004
Capital Exp.(net)	(2,130)	(1,202)	(1,498)	(1,687)	(1,868)
Other Invt.(net)	(3,886)	1,742	0	0	0
Invt in Assoc. & JV	7	5	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(400)	(917)	0	0	0
Net Investing CF	(6,410)	(371)	(1,498)	(1,687)	(1,868)
Div Paid	(2,718)	(2,063)	(2,472)	(2,752)	(3,168)
Chg in Gross Debt	4,061	(1,823)	2,534	2,534	2,534
Capital Issues	0	0	0	0	0
Other Financing CF	(24)	(29)	0	0	0
Net Financing CF	1,320	(3,915)	62	(219)	(634)
Currency Adjustments	0	0	0	0	0
Chg in Cash	(1,496)	342	4,227	3,161	3,501
Opg CFPS (RMB)	2.94	4.13	3.51	4.16	4.73
Free CFPS (RMB)	0.97	2.28	2.77	2.25	2.75

Source: Company, DBS HK

Shenzhou International

Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	Target Price	Rating
1	16-May-23	HK\$68.00	HK\$82.60	BUY
2	16-Aug-23	HK\$77.55	HK\$102.50	BUY
3	31-Aug-23	HK\$76.75	HK\$100.00	BUY
4	22-Jan-24	HK\$69.50	HK\$98.00	BUY

Source: DBS HK

Analyst: Alison Fok

Mavis Hui

Shenzhou International

DBS Group Research recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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