

# China Lilang (1234 HK)

## Likely bottomed out and supported by yield

We believe a bottom out and gradual improvement in FY22E is likely. Thanks to the extremely low valuation (6x 22E P/E and 12% FY22E yield) compared to 5 year-average of 8x P/E, we maintain BUY but lowered TP to HK\$ 4.94, based on 8x FY22E P/E (unchanged).

- FY21 results missed on the higher than expected inventory provision.** China Lilang's FY21 sales grew by 26% YoY to RMB 3.4bn, beating CMBI/BBG est. by 15%/ 7%, due to greater-than-expected sales from smart casual business (which has a model change from consignment into direct-to-retail) and resales of core brand's inventory repurchased from distributors in FY20. But FY21 net profit dropped by 16% YoY to RMB 468mn, missed CMBI/BBG est. by 24%/ 34%, due to: 1) greater-than-expected losses from smart casual and inventory resold with a lower margin and 2) unexpected inventory provisions of RMB 122mn for footwear and leather coats. However, if we adjust for provisions, GP margin would have improved to 45.5% (vs 44.9% in FY20) but NP margin will still have fallen to 16.9% (vs 20.8% in FY20).
- Retail sales growth accelerated in 1Q22E despite pandemic.** Management highlighted that retail sales growth was robust at low double-digit in Jan - Feb 2021, accelerated from MSD/ MSD to HSD in 4Q21/ 3Q21. But this trend was interrupted by COVID-19 outbreaks in Mar 2022 and about 100 - 150 stores (out of ~2,800 total stores) were closed temporarily.
- A prudent guidance and a likely turnaround in FY22E.** Management is targeting a 10% retail sales growth for FY22E and a 10%+ e-commerce sales growth, plus 50 - 150 new store openings (CMBI est. ~80/20 for LILANZ/ smart casual) in more high-end locations with larger sizes. We also expect store productivity to improve, as the distributors are more motivated under consignment model and inventory sharing will be more efficient.
- We believe NP margin will likely improve onwards gradually.** We are forecasting the NP margin to bottom out from 13.9% in FY21 to 15.7%/ 16.2%/ 17.5% in FY22E/ 23E/ 24E, because of: 1) absence of provisions in FY22E, 2) less inventory clearance sales on the e-commerce which as lower GP margin, 3) greater sales from consignment business and 4) smart casual business to turn profitable.
- Maintain BUY but cut TP to HK\$ 4.94.** We maintain BUY but lowered TP to HK\$ 4.94, based on 8x FY22E P/E (unchanged). The counter is cheap at 6x FY22E P/E and 12% FY22E yield. We cut our FY22E/ 23E net profit estimates by 21%/ 22% to factor in 1) inventory provisions, 2) higher sales but 3) lower GP margin and 4) higher operating expenses.

### Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	2,681	3,379	3,922	4,335	4,700
YoY growth (%)	(26.7)	26.1	16.1	10.5	8.4
Net income (RMB mn)	557	468	615	702	822
EPS (RMB)	0.465	0.390	0.513	0.585	0.683
YoY growth (%)	(31.4)	(16.1)	31.4	14.0	16.8
Consensus EPS (RMB)	n/a	n/a	0.622	0.718	0.815
P/E (x)	7.0	8.1	6.3	5.5	4.7
P/B (x)	1.1	1.0	1.0	0.9	0.9
Yield (%)	11.5	8.9	11.9	13.6	15.9
ROE (%)	15.4	12.8	16.3	17.6	19.5
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

### BUY (Maintain)

Target Price	HK\$4.94
(Previous TP)	HK\$6.27)
Up/Downside	+27.4%
Current Price	HK\$3.88

### China Apparel Sector

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#### Stock Data

Mkt Cap (HK\$ mn)	4,646
Avg 3 mths t/o (HK\$ mn)	2.17
52w High/Low (HK\$)	6.68/3.80
Total Issued Shares (mn)	1,197.5

Source: Bloomberg

#### Shareholding Structure

Mr Wang & Family	67.26%
Value Partners	1.13%
Free Float	31.61%

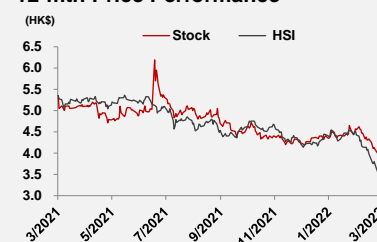
Source: Bloomberg, HKEx

#### Share Performance

	Absolute	Relative
1-mth	-10.3%	3.4%
3-mth	-3.3%	4.3%
6-mth	-12.8%	1.1%
12-mth	-24.9%	1.4%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

#### Auditor: KPMG

#### Related Reports

- China Lilang (1234 HK, BUY) – A transition year but with attractive yield - 24 Aug 2021
- China Lilang (1234 HK, BUY) – A prudent retail sales target but attractive yield - 19 Mar 2021
- China Lilang (1234 HK, BUY) – Positive growth resumed and attractive yield - 20 Aug 2020

## Earnings revision

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	3,922	4,335	4,700	3,421	3,763	n/a	14.7%	15.2%	n/a
Gross profit	1,818	2,063	2,264	1,662	1,858	n/a	9.4%	11.0%	n/a
EBIT	737	870	1,024	917	1,058	n/a	-19.7%	-17.7%	n/a
Net profit att.	615	702	822	782	901	n/a	-21.3%	-22.1%	n/a
Diluted EPS (RMB)	0.513	0.585	0.683	0.650	0.749	n/a	-21.1%	-21.9%	n/a
Gross margin	46.4%	47.6%	48.2%	48.6%	49.4%	n/a	-2.2ppt	-1.8ppt	n/a
EBIT margin	18.8%	20.1%	21.8%	26.8%	28.1%	n/a	-8ppt	-8ppt	n/a
Net profit att. margin	15.7%	16.2%	17.5%	22.8%	24.0%	n/a	-7.2ppt	-7.8ppt	n/a

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB mn	CMBIS			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	3,922	4,335	4,700	3,567	3,763	n/a	10.0%	15.2%	n/a
Gross profit	1,818	2,063	2,264	1,733	1,859	n/a	4.9%	11.0%	n/a
EBIT	737	870	1,024	941	1,058	n/a	-21.7%	-17.8%	n/a
Net profit att.	615	702	822	778	901	n/a	-21.0%	-22.0%	n/a
Diluted EPS (RMB)	0.513	0.585	0.683	0.653	0.750	n/a	-21.4%	-22.0%	n/a
Gross margin	46.4%	47.6%	48.2%	48.6%	49.4%	n/a	-2.2ppt	-1.8ppt	n/a
EBIT margin	18.8%	20.1%	21.8%	26.4%	28.1%	n/a	-7.6ppt	-8ppt	n/a
Net profit att. margin	15.7%	16.2%	17.5%	21.8%	23.9%	n/a	-6.1ppt	-7.7ppt	n/a

Source: Company data, CMBIGM estimates

## Valuation

Figure 3: Peers' valuation

Company	Ticker	Rating	12m TP (LC)	Price (LC)	Up/Down-side	Mkt. Cap (HK\$m)	Year End	P/E (x)		P/B (x)		ROE (%)	3yrs PEG (x)	Yield (%)	
								FY1E	FY2E	FY1E	FY2E	FY1E	FY1E	FY1E	
<b>H shares Apparel</b>															
China Lilang	1234 HK	BUY	4.94	3.88	27%	4,646	Dec-21	6.3	5.5	0.9	0.9	12.8	0.3	11.9	
Bosideng Int'l	3998 HK	BUY	5.31	3.59	48%	39,079	Mar-21	14.3	11.8	2.6	2.3	17.5	0.6	5.0	
Jnby Design	3306 HK	BUY	14.51	9.27	57%	4,809	Jun-21	6.1	5.3	2.1	2.0	37.1	0.6	11.1	
Cosmo Lady	2298 HK	NR	n/a	0.44	n/a	979	Dec-20	n/a	7.5	0.4	0.3	1.2	0.0	1.7	
Giordano	709 HK	NR	n/a	1.56	n/a	2,463	Dec-21	13.0	9.8	n/a	n/a	7.8	0.8	7.7	
Koradior	3709 HK	NR	n/a	11.70	n/a	8,237	Dec-20	10.7	8.6	1.7	1.5	17.2	0.4	4.6	
Esprit Holdings	330 HK	NR	n/a	0.86	n/a	2,435	Dec-20	n/a	n/a	n/a	n/a	(62.7)	0.0	n/a	
La Chapelle	6116 HK	NR	n/a	0.39	n/a	627	Dec-20	n/a	n/a	n/a	n/a	n/a	0.0	n/a	
Bauhaus Intl	483 HK	NR	n/a	0.53	n/a	195	Mar-21	n/a	n/a	n/a	n/a	53.5	0.0	n/a	
								<b>Avg.</b>	<b>10.1</b>	<b>8.1</b>	<b>1.5</b>	<b>1.4</b>	<b>10.5</b>	<b>0.3</b>	<b>7.0</b>
								<b>Med.</b>	<b>10.7</b>	<b>8.0</b>	<b>1.7</b>	<b>1.5</b>	<b>15.0</b>	<b>0.3</b>	<b>6.3</b>
<b>A-shares Apparel</b>															
Ningbo Peacebird	603877 CH	NR	n/a	21.35	n/a	12,518	Dec-20	11.1	9.2	2.3	2.0	25.1	0.4	4.7	
Joeone Co Ltd	601566 CH	NR	n/a	10.44	n/a	7,378	Dec-20	24.0	16.6	1.4	1.3	3.6	3.6	3.8	
Fujian Septwolves	002029 CH	NR	n/a	5.24	n/a	4,870	Dec-20	15.9	12.1	0.6	0.6	4.1	0.7	2.3	
Hla Corp Ltd	600398 CH	NR	n/a	5.46	n/a	29,007	Dec-20	8.2	7.0	1.5	1.4	18.2	0.2	11.5	
Jiangsu Hongdou	600400 CH	NR	n/a	3.16	n/a	8,950	Dec-20	59.6	47.2	2.1	2.1	2.7	4.0	n/a	
Lancy Co Ltd	002612 CH	NR	n/a	24.09	n/a	13,109	Dec-20	43.2	31.1	3.4	3.0	8.4	0.8	n/a	
Shenzhen Huijie	002763 CH	NR	n/a	8.77	n/a	4,423	Dec-20	n/a	n/a	n/a	n/a	15.7	0.0	n/a	
Ellassay Fashion	603808 CH	NR	n/a	12.20	n/a	5,538	Dec-20	12.8	10.7	1.6	1.5	14.0	4.1	3.3	
Bobaoon Co	002776 CH	NR	n/a	2.91	n/a	1,925	Dec-20	n/a	n/a	n/a	n/a	(22.0)	0.0	n/a	
								<b>Avg.</b>	<b>25.0</b>	<b>19.1</b>	<b>1.8</b>	<b>1.7</b>	<b>7.7</b>	<b>1.6</b>	<b>5.1</b>
								<b>Med.</b>	<b>15.9</b>	<b>12.1</b>	<b>1.6</b>	<b>1.5</b>	<b>8.4</b>	<b>0.7</b>	<b>3.8</b>
<b>International Apparel</b>															
Hugo Boss	BOSS GR	NR	n/a	48.62	n/a	29,615	Dec-21	19.5	15.4	3.1	2.7	16.7	0.9	2.1	
Ted Baker	TED LN	NR	n/a	115.60	n/a	2,202	Jan-21	n/a	128.4	n/a	n/a	(21.7)	0.0	0.0	
Next	NXT LN	NR	n/a	6528.00	n/a	89,094	Jan-21	12.4	11.8	7.9	6.7	88.3	0.3	3.8	
Hennes & Mauritz	HMB SS	NR	n/a	141.92	n/a	195,193	Nov-21	17.4	15.0	3.8	3.6	15.1	1.3	5.4	
Industria De Diseno	ITX SM	NR	n/a	20.88	n/a	563,036	Jan-22	18.0	16.3	4.0	3.9	21.4	2.4	5.2	
Ovs Spa	OVS IM	NR	n/a	1.96	n/a	4,933	Jan-21	10.7	9.0	0.6	0.6	16.9	0.6	0.0	
Pvh Corp	PVH US	NR	n/a	83.73	n/a	45,840	Jan-21	9.0	8.4	1.2	1.0	10.2	(0.0)	0.1	
Vf Corp	VFC US	NR	n/a	57.49	n/a	174,917	Apr-21	17.9	15.9	6.6	6.1	41.1	0.3	3.4	
Marks & Spencer	MKS LN	NR	n/a	165.10	n/a	33,369	Apr-21	7.9	8.9	1.3	1.2	1.1	(0.0)	0.6	
								<b>Avg.</b>	<b>14.1</b>	<b>25.5</b>	<b>3.5</b>	<b>3.2</b>	<b>21.0</b>	<b>0.6</b>	<b>2.3</b>
								<b>Med.</b>	<b>14.9</b>	<b>15.0</b>	<b>3.4</b>	<b>3.2</b>	<b>16.7</b>	<b>0.3</b>	<b>2.1</b>

Source: Bloomberg, CMBIGM estimates

## Assumptions

Figure 4: China Lilang's key assumptions

Major assumptions	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Sales by segment (RMB mn)</b>					
LILANZ	2,215	2,737	3,248	3,593	3,899
Smart Casual	483	642	674	742	801
Total	2,698	3,379	3,922	4,335	4,700
<b>Sales by segment growth (%)</b>					
LILANZ	-32.1%	23.6%	18.6%	10.6%	8.5%
Smart Casual	21.3%	32.9%	5.0%	10.0%	8.0%
Total	-26.3%	25.3%	16.1%	10.5%	8.4%
<b>Sales network by segment</b>					
LILANZ	2,466	2,443	2,523	2,603	2,683
Smart Casual	295	290	307	317	327
Total	2,761	2,733	2,830	2,920	3,010
<b>Sales network by segment growth (%)</b>					
LILANZ	-2.3%	-0.9%	3.3%	3.2%	3.1%
Smart Casual	1.7%	-1.7%	5.9%	3.3%	3.2%
Total	-1.9%	-1.0%	3.5%	3.2%	3.1%
<b>Trade fair sales growth (%)</b>					
Spring Summer	-40.0%	20.0%	13.0%	10.0%	0.0%
Fall	-10.0%	15.0%	11.5%	10.0%	0.0%
Winter	-5.0%	10.0%	16.5%	10.0%	0.0%
GP margins by segment	44.9%	41.9%	46.4%	47.6%	48.2%
<b>Opex breakdown</b>					
Staff costs	2.1%	3.3%	3.9%	3.8%	3.8%
D & A	1.1%	3.0%	3.5%	3.7%	3.8%
R & D	4.5%	3.8%	4.5%	4.5%	4.5%
Provision ( write back )	0.0%	0.0%	0.0%	0.0%	0.0%
A & P	10.3%	8.9%	10.0%	10.5%	10.5%
Selling & distribution costs / sales	18.3%	23.5%	23.6%	23.7%	22.9%
Admin expenses / sales	4.0%	5.1%	4.8%	4.8%	4.7%
<b>OP margins</b>	<b>24.3%</b>	<b>15.8%</b>	<b>18.8%</b>	<b>20.1%</b>	<b>21.8%</b>
Effective tax rate	19.8%	16.6%	19.0%	21.0%	21.0%
<b>NP att. margins</b>	<b>20.8%</b>	<b>13.9%</b>	<b>15.7%</b>	<b>16.2%</b>	<b>17.5%</b>
<b>NP att. growth (%)</b>	<b>-31.4%</b>	<b>-16.0%</b>	<b>31.3%</b>	<b>14.2%</b>	<b>17.1%</b>

Source: Company data, CMBIGM estimates

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Revenue</b>	<b>2,698</b>	<b>3,379</b>	<b>3,922</b>	<b>4,335</b>	<b>4,700</b>
LILANZ	2,215	2,737	3,248	3,593	3,899
L2	-	-	-	-	-
Smart Casual	483	642	674	742	801
<b>Cost of goods sold</b>	<b>(1,477)</b>	<b>(1,964)</b>	<b>(2,104)</b>	<b>(2,271)</b>	<b>(2,436)</b>
<b>Gross profit</b>	<b>1,221</b>	<b>1,415</b>	<b>1,818</b>	<b>2,063</b>	<b>2,264</b>
<b>Other income</b>	<b>106</b>	<b>89</b>	<b>55</b>	<b>69</b>	<b>85</b>
<b>Operating expenses</b>	<b>(658)</b>	<b>(971)</b>	<b>(1,136)</b>	<b>(1,263)</b>	<b>(1,325)</b>
D & A	(22)	(52)	(81)	(90)	(78)
Staff costs	(62)	(81)	(93)	(103)	(111)
S & D costs (ex-staff,	(452)	(743)	(863)	(959)	(1,003)
Admin exp. (ex-staff,	(63)	(91)	(76)	(85)	(105)
Other operating	(58)	(5)	(24)	(26)	(28)
<b>EBIT</b>	<b>669</b>	<b>533</b>	<b>737</b>	<b>870</b>	<b>1,024</b>
Finance costs, net	43	28	22	19	17
JVs & associates	-	-	-	-	-
Exceptional	-	-	-	-	-
<b>Pre-tax profit</b>	<b>712</b>	<b>561</b>	<b>759</b>	<b>889</b>	<b>1,041</b>
Income tax	(138)	(93)	(144)	(187)	(219)
Less: Minority interests	0	0	0	0	0
<b>Net profit</b>	<b>574</b>	<b>468</b>	<b>615</b>	<b>702</b>	<b>822</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>EBIT</b>	<b>669</b>	<b>533</b>	<b>737</b>	<b>870</b>	<b>1,024</b>
D & A	31	100	161	179	155
Change in working capital	175	(69)	(238)	(114)	(100)
Income tax paid	(155)	(100)	(144)	(187)	(219)
Others	53	135	31	27	25
<b>Net cash from operating</b>	<b>773</b>	<b>599</b>	<b>545</b>	<b>775</b>	<b>885</b>
Capex & investments	(225)	(302)	(351)	(388)	(420)
Associated companies	-	-	-	-	-
Interest received	45	34	-	-	-
Others	(11)	(12)	-	-	-
<b>Net cash from investing</b>	<b>(191)</b>	<b>(280)</b>	<b>(351)</b>	<b>(388)</b>	<b>(420)</b>
Equity raised	-	-	-	-	-
Net change in bank loans	-	73	-	-	-
Dividend paid	(521)	(446)	(403)	(497)	(575)
Others	(69)	(109)	(8)	(8)	(8)
<b>Net cash from financing</b>	<b>(590)</b>	<b>(483)</b>	<b>(411)</b>	<b>(505)</b>	<b>(583)</b>
<b>Net change in cash</b>	<b>(8)</b>	<b>(164)</b>	<b>(216)</b>	<b>(117)</b>	<b>(119)</b>
Beginning cash balance	1,751	1,739	1,572	1,356	1,238
Exchange difference	(4)	(3)	-	-	-
<b>Cash at the end of the year</b>	<b>1,739</b>	<b>1,572</b>	<b>1,356</b>	<b>1,238</b>	<b>1,119</b>

### Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Non-current assets</b>	<b>1,394</b>	<b>1,735</b>	<b>1,925</b>	<b>2,134</b>	<b>2,399</b>
Fixed asset	924	1,200	1,392	1,602	1,870
Intangible assets &	130	126	124	122	120
Prepaid lease payments	3	21	21	21	21
Interest in joint ventures	-	-	-	-	-
Other non-current assets	337	389	389	389	389
<b>Current assets</b>	<b>3,618</b>	<b>3,273</b>	<b>3,357</b>	<b>3,428</b>	<b>3,482</b>
Cash and cash equivalents	1,739	1,572	1,356	1,238	1,119
Inventories	667	894	807	871	934
Trade and other	1,210	795	1,182	1,306	1,416
Prepayments	-	-	-	-	-
Other current assets	2	12	12	12	12
<b>Current liabilities</b>	<b>1,288</b>	<b>1,261</b>	<b>1,323</b>	<b>1,397</b>	<b>1,470</b>
Bank loans	37	119	119	119	119
Trade payables	1,036	870	932	1,006	1,079
Accruals & other payables	-	-	-	-	-
Tax payables	152	175	175	175	175
Others	62	98	98	98	98
<b>Non-current liabilities</b>	<b>70</b>	<b>73</b>	<b>73</b>	<b>73</b>	<b>73</b>
Bank loans	-	-	-	-	-
Deferred income	-	-	-	-	-
Deferred tax	8	9	9	9	9
Others	62	64	64	64	64
<b>Minority Interest</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total net assets</b>	<b>3,654</b>	<b>3,673</b>	<b>3,886</b>	<b>4,092</b>	<b>4,339</b>
<b>Shareholders' equity</b>	<b>3,654</b>	<b>3,673</b>	<b>3,886</b>	<b>4,092</b>	<b>4,339</b>

### Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Sales mix (%)</b>					
LILANZ	82.1	81.0	82.8	82.9	83.0
L2	-	-	-	-	-
Smart Casual	17.9	19.0	17.2	17.1	17.0
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>P&amp;L ratios (%)</b>					
Gross margin	44.9	41.9	46.4	47.6	48.2
Operating margin	24.3	15.8	18.8	20.1	21.8
Pre-tax margin	25.9	16.6	19.4	20.5	22.1
Net margin	20.8	13.9	15.7	16.2	17.5
Effective tax rate	19.8	16.6	19.0	21.0	21.0
<b>Balance sheet ratios</b>					
Current ratio (x)	2.8	2.6	2.5	2.5	2.4
Quick ratio (x)	2.3	1.9	1.9	1.8	1.7
Cash ratio (x)	1.4	1.2	1.0	0.9	0.8
Inventory turnover days	165	166	140	140	140
Trade receivables days	165	86	110	110	110
Trade payables days	256	162	162	162	162
Total debt / total equity ratio (%)	3	6	6	5	5
Net debt / equity ratio (%)	Net cash	Net cash	Net cash	Net cash	Net cash
<b>Returns (%)</b>					
ROE	15.7	12.7	15.8	17.2	19.0
ROA	11.5	9.3	11.6	12.6	14.0
<b>Per share</b>					
EPS (RMB)	0.47	0.39	0.51	0.58	0.68
DPS (RMB)	0.38	0.28	0.38	0.44	0.51
BVPS (RMB)	3.05	3.07	3.24	3.40	3.60

Source: Company data, CMBIGM estimates

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