

**Analyst: Sabina Cheng**

## **Main Board Listing – Research**

361 度國際有限公司

**361 Degrees International Limited [Stock Code: 01361]**

**Sole Global Coordinator, Sole Bookrunner and Sole Sponsor** : Merrill Lynch International Merrill Lynch Far East Limited

**Joint Lead Managers** : Merrill Lynch Far East Limited CCB International Capital Limited

**PRC Domestic Financial Adviser** : Industrial Bank

**Sector** : Consumer

**Business** : A leading domestic sportswear enterprises in the PRC

<p><b>Total share offer:</b> <u>500,000,000</u> shares (25% of the enlarged share capital)</p> <p><b>Public Offer:</b> 50,000,000 shares (10%)</p> <p><b>Placing:</b> 450,000,000 shares (90%)</p>	<p><b><u>Business of 361 Degrees International (“361°”)</u></b></p> <p>Founded in 2003, 361° is now one of the leading domestic sportswear enterprises in the PRC. The company designs, develops, produces, markets and distributes sportswear products, including athletic footwear, apparel and accessories under its 361° trademark selling at more than 5,900 361° authorised retail outlets in 31 provinces and most major cities in the PRC.</p> <p>In 2008, the company was a top five domestic brand in terms of revenue, accounting for 4.2% of the total revenue of the PRC sportswear market and a top five brand in terms of the number of retail outlets in the PRC as of 31 March 2009.</p> <p>As of June 2009, the distribution network of 361° products consisted of 30 distributors who oversaw 3,173 authorised retailers. These authorised retailers owned and operated 5,925 361° authorised retail outlets, covering 31 provinces and more than 450 district-level cities, as well as more than 1,200 county-level cities in the PRC. The company’s production facilities are located in Jinjiang City, Fujian Province, the PRC. It operated 16 footwear production lines, with an aggregate annual production capacity of approximately 13.6 million pairs of footwear.</p>
<p><b>Price:</b> HK\$3.15 – HK\$4.35 per share</p> <p><b>Market Cap:</b> HK\$6.3 billion – HK\$8.7 billion</p> <p><b>Pro forma fully diluted FY09 P/E:</b> 10.0x – 13.9x</p> <p><b>Adjusted NTA per share:</b> HK\$1.09 – HK\$1.38</p> <p><b>Staffing:</b> 4,817 (as of 11<sup>th</sup> June 2009)</p>	
<p><b>HK Public Offer period:</b> 18<sup>th</sup> June 2009 – 23<sup>rd</sup> June 2009 noon</p> <p><b>Receiving bankers:</b> HSBC CCB (Asia)</p> <p><b>Hong Kong Share Registrar:</b> Computershare Hong Kong Investor Services Limited</p> <p><b>Listing date:</b> 30<sup>th</sup> June 2009</p>	

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### Shareholders after Listing (Assuming the over-allotment option is not exercised)

Dings International – owned by Mr Ding Wuhao, an executive Director and the president of 361 °	18.75%
Ming Rong International – owned by Mr Ding Huihuang, an executive Director and the chairman of 361 °	18.00%
Hui Rong International – owned by Mr Ding Huirong, an executive directors and vice president of 361 °	18.00%
Jian Tong Investments – owned by Mr Ding Jiangtong, father of Mr. Ding Huihuang and Ding Huirong	1.50%
Jia Wei Int'l – owned by Mr Wang Jiabi, an executive directors and a vice president of 361 °	9.375%
Jia Chen International – owned by Mr Wang Jiachen a vice general manager of 361 °	9.375%
Public shareholders	25.00%
	100.00%

### Use of Proceeds

Net proceeds from the offer are estimated to be HK\$1,741.2 million (based on an offer price of HK\$3.75, assuming the over-allotment option is not exercised)

	HK\$ million
For developing and increasing awareness of the company's brand awareness	677.3
For developing its facilities in Fujian Province, the PRC	560.7
For developing a distinct children's footwear and apparel sub-brand	156.7
For establishing a new product testing and research and development laboratory	104.5
For establishing an enterprise resource planning system	67.9
For working capital and other general corporate purposes	174.1

### Financial Highlights

	Year ended 30 <sup>th</sup> June			For the nine months ended 31 <sup>st</sup> March	
	2006 RMB '000	2007 RMB '000	2008 RMB '000	2008 RMB '000	2009 RMB '000
Revenue	262,923	373,346	1,317,069	853,651	2,423,679
Gross profit	27,058	76,923	348,028	202,359	791,325
Operating profit	12,237	29,331	202,543	116,322	442,601
<b>Profit for the year</b>	<b>11,006</b>	<b>22,911</b>	<b>178,973</b>	<b>102,656</b>	<b>364,205</b>
Gross profit margin	10.3%	20.6%	26.4%	23.7%	32.6%
Operating profit margin	4.7%	7.9%	15.4%	13.6%	18.3%
Net profit margin	4.2%	6.1%	13.6%	12.0%	15.0%



## **Strengths/Opportunities**

- ✓ **Improving performance within a short period of time with effective expansion and pricing strategies** The company reported a 681.2% rise in net profit to RMB178.973 million in FY2008 from RMB22.911 million in FY2007, driven by higher sales volume due to the continual expansion of its retail network and lower average selling price of its product lines.
- ✓ **Aggressive network expansion plan** As of end-March 2009, 361° had over 5,500 retail outlets, slightly behind its two industry leaders - Li Ning's (with 6,917 number of point of sale in FY2008) and Anta Sports (with 5,781 number of point of sale in FY2008). Its plan of adding 1,500 new outlets by the end of 2009 should help it grab more sales going forward.
- ✓ **Addition of new production facilities** Despite the company had the lowest gross profit margin (26.4%) among its peers like Li Ning (48.1%), Anta Sports (40.0%), China Dongxiang (58.5%) Xtep International (37.1%) in FY2008, it is expected that the company may improve its gross margin and net profit margin through business strategies like addition of new production facilities which can help control product quality as well as cost of production. New footwear facilities with two production lines and annual capacity of 1.7 million pairs of footwears will be completed by September 2009.

## **Weaknesses/Threats**

- × **The company currently derives nearly all the revenues from its single brand of 361° brand.**
- × **Small number of exclusive distributors** 361° relies on 30 exclusive distributors to sell its products to authorized retailers and ultimately consumers with the top five customers accounting for 47.5% of total revenues for the nine months ended March 2009 and the largest customer accounting for 17.0%.
- × **Negative operating cash flow (OCF) in past years** The company recorded negative OCF in the FY2006 and FY2007 partly due to cash outflow for the purchase of raw materials and outsourced products following the increase in sales volume. However, its peers all posted positive OCF over the same period, except Xtep International recorded a minor negative OCF in FY2006. Though there has been improvement on the company's OCF, its highest receivable-turnover-days among its peers implies that the company has higher inventory risk than its competitors.
- × **Keen competition from low-quality sport brands despite a fair valuation** Chinese sportswear companies are currently trading between 11.9x to 20.8x 2009 P/E (Li Ning:20.8x, Anta Sports:17.3x, China Dongxiang:15.3x, Xtep International:11.9x.). Given the similar scale of operation, valuation of 361° may be similar to Xtep International at around 11.0x to 14x 2009 earnings. Although the valuation of the offer price of the company is not demanding, keen competition from other sportswear companies especially those low-quality sport brands may reduce the pricing power of 361° products going forward.

## **Recommendation: Trading buy**



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