

Analyst: Sam Ho

## Main Board Listing- Research

李寧有限公司

Li Ning Company Limited - [Stock Code: 2331]

Global Coordinator, Bookrunner, Lead Manager and Sponsor

: DBS Asia Capital

Sector : Sports-apparel

Business : Manufacture and sale of sports apparel and footwear in China

**Total share offer: 246,516,000 shares**  
(25% of the enlarged share capital)

**Placement:** 221,864,000 shares (90%)  
- 211,410,000 new shares  
- 10,454,000 sale shares

**IPO:** 24,652,000 shares (10%)

**Greenshoe:** 36,976,000 shares

**Price:** HK\$1.76-HK\$2.23 per share

**Market cap:** HK\$1,735 mln-HK\$2,199 mln

**Staffing:** 3,704

**Prospective 2004 P/E:** 15x-19x (fully-diluted)

**Adjusted NAV per share:** RMB0.81-RMB0.92

**Book opens:** 11<sup>th</sup> June 2004

**Book closes:** 18<sup>th</sup> June 2004

**IPO commences:** 15<sup>th</sup> June 2004

**IPO ends:** 18<sup>th</sup> June 2004

**Share registrar:** Computershare Hong Kong  
Investor Services

**Receiving bank:** Bank of China (Hong Kong)

**Listing date:** 28<sup>th</sup> June 2004

### Business of Li Ning

The Company is principally engaged in the design, manufacture and sale of sports apparel in China. Its products include sports footwear, apparel and accessories for sport and leisure use, primarily sold under the LI-NING brand, and the KAPPA brand, which is exclusively licensed to it for use in China and Macau.

It has established an extensive distributorship and retail network in China. As of 31/05/2004, it had over 200 distributors operating over 2,200 franchised retail outlets for the LI-NING and KAPPA brands in China, whilst there are also 110 retail stores and 199 concessions for the 2 brands directly under the Company in China. It also exports LI-NING products to Italy, Spain and Russia through its independent distributors.

The processing and manufacturing of the majority of its sports apparel and of all of its sports footwear and accessories are subcontracted to independent contract manufacturers in China. It manufactures a small portion of its sports apparel at its manufacturing facilities located in Sanshui, Guangdong province.

### Major Shareholders after Listing

(Assuming the over-allotment option is not exercised)

Mr Li Ning, chairman of the Company, and his family members	42.719%
Tetrad Ventures, which is wholly-owned by the Government of Singapore Investment Corporation	15.185%
Other founding shareholders	9.977%
Alpha Talent *	3.575%
CDH China Fund, L.P.	3.544%
	<u>75.000%</u>

\*- these shares are currently owned by Mr Li Ning through the employee share options scheme, whereby the senior management team can subscribe for the shares from Li 6 months after the listing

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### Use of Proceeds

Net proceeds from the offer are estimated to be HK\$440 million

(Assuming the over-allotment option is not exercised, and at an issue price of HK\$1.995 each, which is the mid-point of the indicative price range)

	HK\$ million
To expand and improve the coverage of distribution and retail network	100
To conduct brand promotions and marketing activities	110
To establish basic product research capabilities and set up an R&D centre in Hong Kong	15
To improve management information systems and logistics operations	35
To acquire and operate management rights or licences of other international brands in China	40
To establish a centralized operating headquarters in Beijing	60
To pursue other potential strategic acquisitions	40
To serve as general working capital	Balance

### Financial Highlights

	Year ended 31 <sup>st</sup> December		
	2003 RMB'000	2002 RMB'000	2001 RMB'000
Turnover			
Footwear	443,811	349,608	288,341
Apparel	658,649	500,131	385,425
Accessories	<u>173,764</u>	<u>108,266</u>	<u>61,169</u>
	<u>1,276,224</u>	<u>958,005</u>	<u>734,935</u>
Operating profit	119,109	103,347	65,201
Net profit	<u>93,960</u>	<u>66,889</u>	<u>49,620</u>
Dividend	65,772	23,970	17,182
EPS- basic	<u>RMB¢12.53</u>	<u>RMB¢8.92</u>	<u>RMB¢6.62</u>

### Breakdown of Sales by Brands and Types of Sales

	Year ended 31 <sup>st</sup> December		
	2003 RMB'000	2002 RMB'000	2001 RMB'000
Turnover			
LI-NING brand	1,236,166	944,269	734,935
KAPPA brand	<u>40,058</u>	<u>13,736</u>	-
	<u>1,276,224</u>	<u>958,005</u>	<u>734,935</u>

	Year ended 31 <sup>st</sup> December		
	2003 RMB'000	2002 RMB'000	2001 RMB'000
Turnover			
China market			
Distributor sales	995,067	750,715	567,388
Concession sales	132,699	115,564	99,697
Retail store sales	111,720	72,133	63,639
International markets	<u>36,738</u>	<u>19,593</u>	<u>4,211</u>
	<u>1,276,224</u>	<u>958,005</u>	<u>734,935</u>

**Strengths/ Opportunities**

- ✓ Retail sales of consumer goods in China grew at a CAGR of 10.3% from 1995 to 2002, along with the GDP CAGR growth of 8.3% in the same period. Demand for branded sports goods should at least rise at the pace of the overall economy going forward. In addition, the 2008 Beijing Olympic Games should also boost consumption and overall market growth.
- ✓ According to a research report of the Horizon Research Group, Adidas, Nike and LI-NING, in descending order, are the top 3 sports footwear brands in terms of overall brand equity in China in 2003.
- ✓ The Company had an extensive distribution network throughout the nation, comprising 2,200 franchised LI-NING & KAPPA retail outlets, 110 directly-managed LI-NING and KAPPA retail stores, as well as 199 directly-managed LI-NING and KAPPA concessions, as at 31/05/2004.
- ✓ The Company has abundant sponsorship resources as it is the official partner of the Chinese Olympic Committee. It is also the sponsor of the Chinese national teams in the Summer Olympic Games. Moreover, it is the regular sponsor of 4 national teams, namely Gymnastic Federation of France, Spanish women's basketball team, Russian Delegation at the 2001 Universiade and Gymnastic Federation of Spain.
- ✓ With shares priced at 2004E P/E of 15x-19x, valuation of Li Ning is fair, when compared with other retail-related peers Esprit (*stock code: 0330*)'s 2004E P/E of 22.1x, Giordano (*stock code: 0709*)'s 2004E P/E of 16.9x and Ports Design (*stock code: 0589*)'s 2004E P/E of 13.7x.

**Weaknesses/ Threats**

- × Competition in the sportswear industry is keen. There is a large number of local and international sports brands participating in China. The major competitors are Nike, Adidas, Anta, Doublestar and Kangwei. In general, international brands perform better in 1<sup>st</sup>-tier cities and some coastal cities while domestic brands are more competitive in 2<sup>nd</sup>-tier and 3<sup>rd</sup>-tier cities.
- × Being a leading sportswear brand in China, LI-NING, along with other foreign brands, has frequently become a victim of the counterfeit products. The poor quality of counterfeits would not only affect the Company's sales but also its brand reputation. However, the Company claimed that all its sub-contracted manufacturers and franchisees would help report counterfeit products.
- × The Company had a high inventory turnover of around 141-143 days, which was towards the high-end of the industry average (~100 days). Nevertheless, unlike fashion products, sports products usually have a longer shelf life.

**Recommendation: Hit and run**