

Nongfu Spring (9633 HK)

Effective product diversification strategy to sustain revenue growth

- Overall revenue growth outlook improves on strong headline revenue growth a in 1H23
- The Group's product diversification strategy led to strong beverage product revenue growth and increasing revenue contribution of tea beverage products in 1H23
- Margin will continue to rise as cost-control measures would offset the negative impacts of high raw material costs in FY23E
- Maintain **BUY**; current TP represents 54.89x/46.96x 23E/24E P/E, or 21.09x/16.28x 23E/24E P/B

Growth outlook improves. 1H23 revenue grew 23.3% YoY. By product segment, revenue from tea beverages, juice beverages, and functional beverages jumped 59.9% YoY, 32.2% YoY, and 21.5% YoY; meanwhile, revenue from packaged drinking water products grew 11.7% YoY. The strong revenue growth can be attributed to the resumption of outdoor activities post-pandemic, increasing health consciousness among consumers, and the ability to effectively promote products through various marketing campaigns. In addition the strong revenue growth of beverages products shows the Group's product diversification strategy has achieved initial success; revenue contribution of tea beverage products rose from 20.8% in FY22 to 25.8% in 1H23. Despite that uncertain consumer market outlook remains in 2H23 and low base effect arisen from 2H22 will be less prominent, based on 1H23 performance, we raise FY23E revenue growth to 19.0% YoY. FY23E revenue growth of packaged drinking water, tea beverages, juice beverages, and functional beverages are estimated at 11.4% YoY, 44.1% YoY, 15.6% YoY, and 19.0% YoY. FY22-25E revenue CAGR is projected at 17.8%.

Margins to be affected by raw material costs. Rising price of PET caused by increased oil price led to some cost pressure in 1H23 but margin profile continued to improve during the period, with GPM and NPM (to shareholders of the Company) increasing from 59.3% and 27.8% in 1H22 to 60.2% and 28.2% in 1H23. We believe the rising raw material costs amid inflation will pressure margins, but the Group's proven ability to control cost would offset the negative impact. We project FY23E GPM and NPM (to shareholders of the Company) to be 58.2% and 26.0% in FY23E.

Maintain BUY; TP at HK\$ 53.8. Maintain **BUY** on the Group's strong ability to generate growth and the continued expansion of beverage products. We raise our DCF-derived TP to reflect the increase in our revenue and profit projections. Current TP represents 54.89x/46.96x 23E/24E P/E, or 21.09x/16.28x 23E/24E P/B.

Risk factors: 1) Macroeconomic risk; 2) Commodity price risk; 3) Regulation risk; 4) Food safety risk; 5) Limitation of water sources; 6) Product concentration risk; 7) Changing consumer taste in China; 8) Fluctuation of EPS growth.

Results and Valuation

FY ended Dec 31	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	29,696	33,239	39,567	46,286	54,399
Chg (YoY %)	29.8	11.9	19.0	17.0	17.5
Net Profit – to shareholders of the Company (RMB mn)	7,162	8,495	10,279	12,015	14,177
Chg (% YoY)	35.7	18.6	21.0	16.9	18.0
Basic EPS (RMB)	0.64	0.76	0.91	1.07	1.26
Chg (YoY %)	33.3	18.8	20.3	16.9	18.0
P/E (x)	63.87	53.78	44.72	38.26	32.43
BVPS (RMB)	1.84	2.14	2.38	3.08	3.92
P/B (x)	22.16	19.09	17.18	13.26	10.44
Dividends (RMB)	0.45	0.68	0.37	0.43	0.50
Dividend yield	1.1	1.7	0.9	1.0	1.2
ROAA (%)	24.4	23.5	22.5	22.0	21.4
ROAE (%)	39.5	37.9	40.4	39.1	36.0

Source(s): The Group, ABCI Securities estimates

Company Report

Sep 7, 2023

Rating: BUY

TP: HK\$ 53.8

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Share price (HK\$)	43.85
52WK H/L (HK\$)	48.65/38
Est. share price return	22.7%
Est. dividend yield	0.9%
Est. total returns	23.6%
Previous report date	Apr 4, 2023
Previous rating/TP	BUY/HK\$52.3

Source(s): Bloomberg, ABCI Securities estimates

Key data

Issued H-shares (bn)	5.03
Total issued shares (bn)	11.25
H-share mkt cap (HK\$ bn)	220.8
Total mkt cap (HK\$ bn)	493.2
3-mth avg. ADT (HK\$ mn)	125.8
Shareholding (%)	
Zhong Shanshan	65.0

Source(s): Bloomberg, HKEX

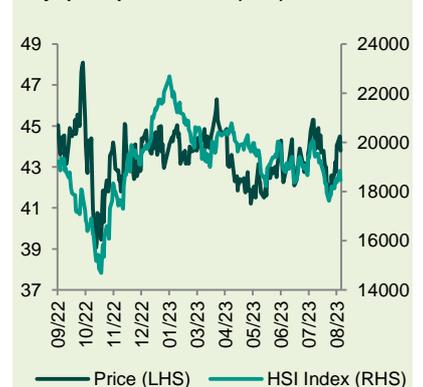
Price performance (%)

	Absolute	Relative*
1-mth	(1.02)	4.56
3-mth	2.21	5.66
6-mth	0.11	10.41

* Relative to HSI

Source(s): Bloomberg

1-yr price performance (HK\$)



Source(s): Bloomberg, ABCI Securities

Note: Market data as of Sep 6, 2023

RMB/HKD: 1.0728



Exhibit 1: Changes in assumptions, projections, and valuations

FY ends at Dec 31	Current report		Previous report		Rationale
	FY23E	FY24E	FY23E	FY24E	
Assumptions					
D/E (%)	14.7	10.5	7.0	4.7	Adjusted based on 1H23 company release
D/A (%)	7.6	6.4	4.8	3.1	
Tax rate (%)	23.3	23.3	23.3	23.3	
Valuations					
TP (HK\$)	53.8		52.3		Higher TP due to higher revenue and profit projections
P/E (x)	54.89	46.96	56.22	46.30	
P/B (x)	21.09	16.28	17.45	14.23	

Note: Previous report was published on Apr 4, 2023

Source(s): The Group, ABCI Securities estimates

Exhibit 2: Changes in major forecasts

As of Dec 31	Current report			Previous report			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue (RMB mn)	39,567	46,286	54,399	38,944	45,895	54,371	1.6	0.9	0.1
Net profit (to shareholders of the Company) (RMB mn)	10,279	12,015	14,177	9,188	11,157	13,584	11.9	7.7	4.4
EPS (RMB)	0.91	1.07	1.26	0.82	0.99	1.21	11.9	7.7	4.4

Source(s): ABCI Securities estimates



Financial statement of the Group

Consolidated income statement

FY ends at Dec 31 (RMB mn, except for per share figures)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	29,696	33,239	39,567	46,286	54,399
Packaged drinking water products	17,058	18,263	20,340	22,458	24,709
Tea beverage products	4,579	6,906	9,952	13,211	17,476
Functional beverage products	3,695	3,838	4,435	5,125	5,914
Juice beverage products	2,614	2,879	3,427	4,028	4,777
Other products	1,750	1,354	1,413	1,465	1,523
Cost of sales	(12,040)	(14,144)	(16,523)	(19,210)	(22,403)
Gross profit	17,656	19,095	23,044	27,077	31,996
Selling expenses	(7,233)	(7,821)	(9,549)	(11,212)	(13,296)
Admin expenses	(1,751)	(1,835)	(2,111)	(2,481)	(2,929)
Others net income/gain	735	1,687	2,089	2,375	2,781
Net finance costs	(53)	(76)	(77)	(98)	(87)
Pretax profit	9,354	11,050	13,396	15,661	18,465
Tax	(2,193)	(2,555)	(3,117)	(3,645)	(4,288)
Net profit	7,162	8,495	10,279	12,015	14,177
- Owners	7,162	8,495	10,279	12,015	14,177
- MI	0	0	0	0	0
Dividend	5,061	7,648	4,112	4,806	5,671
EPS (RMB)					
- Basic	0.64	0.76	0.91	1.07	1.26
- Diluted	0.64	0.76	0.91	1.07	1.26
DPS (RMB)	0.45	0.68	0.37	0.43	0.50

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Consolidated balance sheet

FY ends at Dec 31 (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Bank balances and cash	14,784	15,211	25,432	28,262	42,894
Prepayments, other receivables and other assets	558	560	590	716	842
Trade and bills receivables	476	479	645	677	873
Inventories	1,809	2,108	2,374	2,892	3,218
Others	208	3	0	0	0
Current assets	17,836	18,361	29,042	32,547	47,826
PP&E	12,800	15,398	17,009	18,456	20,934
Right-of-use assets	724	853	948	1,032	1,166
Intangible assets	65	58	76	82	89
Others	1,471	4,584	4,988	4,808	5,254
Non-current assets	15,060	20,893	23,021	24,378	27,442
Total assets	32,896	39,255	52,062	56,925	75,269
Trade and bills payables	1,153	1,425	1,825	2,179	2,496
Other payables and accruals	4,488	6,506	13,521	9,981	17,300
Contract liabilities	2,351	2,677	3,379	3,664	4,638
ST bank borrowing	2,500	2,425	3,802	3,498	3,148
Others	1,097	1,568	2,139	2,311	2,840
Current liabilities	11,589	14,601	24,666	21,633	30,421
Deferred income	265	291	302	315	333
Deferred tax liabilities	258	247	279	255	421
Lease liabilities	43	31	54	58	58
Non-current liabilities	566	569	635	627	812
Shareholders' equity	20,742	24,084	26,761	34,665	44,036
MI	0	0	0	0	0
Total equity	20,742	24,084	26,761	34,665	44,036
Total liabilities and equity	32,896	39,255	52,062	56,925	75,269

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates



Consolidated cash flow statement

FY ends at Dec 31 (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Profit before tax	9,354	11,050	13,396	15,661	18,465
Depreciation and amortization	2,378	2,487	2,958	3,566	4,809
Change in working capital	1,686	1,409	7,655	(3,577)	7,962
Others	(2,018)	(2,905)	(3,186)	(3,882)	(4,619)
Cash flow from operating activities	11,400	12,042	20,822	11,768	26,618
Change of P&E and right-of-use assets	(2,461)	(4,270)	(4,098)	(4,112)	(6,140)
Change in intangible assets	(15)	(2)	(18)	(6)	(7)
Others	(2,839)	(5,154)	(3,800)	(2,375)	(8,005)
Cash flow from investing activities	(5,316)	(9,426)	(7,916)	(6,492)	(14,152)
Change in borrowing	86	(75)	(304)	(350)	(630)
Net proceeds from IPO	0	0	0	0	0
Others	(1,980)	(5,295)	(6,056)	(4,501)	(5,103)
Cash flow from financing activities	(1,893)	(5,370)	(6,360)	(4,851)	(5,733)
Net change in cash	4,191	(2,755)	6,546	424	6,733
ForEx Impact	(59)	388	(171)	(9)	(153)
Cash and cash equivalent - end	10,188	7,821	14,196	14,611	21,192

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Key operating and financial ratios

FY ends at Dec 31	FY21A	FY22A	FY23E	FY24E	FY25E
Growth (YoY %)					
Revenue	29.8	11.9	19.0	17.0	17.5
Packaged drinking water products	22.1	7.1	11.4	10.4	10.0
Tea beverage products	48.3	50.8	44.1	32.8	32.3
Functional beverage products	32.3	3.9	15.6	15.5	15.4
Juice beverage products	32.2	10.1	19.0	17.5	18.6
Others	66.0	(22.6)	4.3	3.7	4.0
Gross profit	30.7	8.2	20.7	17.5	18.2
Pretax profit	33.9	18.1	21.2	16.9	17.9
Net profit (to shareholders of the Company)	35.7	18.6	21.0	16.9	18.0
Profitability ratios (%)					
GPM	59.5	57.4	58.2	58.5	58.8
Pretax margin	31.5	33.2	33.9	33.8	33.9
NPM (to shareholders of the Company)	24.1	25.6	26.0	26.0	26.1
Return ratios (%)					
ROAA	24.4	23.5	22.5	22.0	21.4
ROAE	39.5	37.9	40.4	39.1	36.0
Liquidity ratio (x)					
Current ratio	1.5	1.3	1.2	1.5	1.6
Quick ratio	1.4	1.1	1.1	1.4	1.5
Cash ratio	1.3	1.0	1.0	1.3	1.4
Working capital turnover (days)					
Receivable turnover	5	5	5	5	5
Inventory turnover	55	51	50	50	50
Payable turnover	31	33	36	38	38
Cash conversion cycle	29	23	19	17	17
Leverage ratios (%)					
Total debt to Equity	12.5	10.5	14.7	10.5	7.5
Total debt to Total assets	7.9	6.4	7.6	6.4	4.4
Net debt/(cash) to Equity	(58.8)	(52.7)	(80.3)	(71.0)	(89.9)
Net debt/(cash) to Total assets	(37.1)	(32.3)	(41.3)	(43.3)	(52.6)

Source(s): The Group, ABCI Securities estimates



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Rating	Definition
Buy	Stock return rate \geq Market return rate ($\sim 9\%$)
Hold	- Market return rate ($\sim 9\%$) \leq Stock return rate $<$ Market return rate ($\sim 9\%$)
Sell	Stock return $<$ - Market return ($\sim 9\%$)

Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months

Market return rate: average market return rate since 2006 (HSI total return index 2006-22 averaged at 8.4%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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