

September 20, 2021 09:00 PM GMT

## China Jewelry

# Jewelry Demand Intact Amid China's Reset

Contrary to market concern, we believe jewelry consumers are mostly from the middle class, which is set to expand under Common Prosperity. Our recent AlphaWise survey suggests that consumers plan to increase jewelry spending in the short to medium term, mainly for personal use instead of gifting.

alphawise 



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# Jewelry Demand Intact Amid China's Reset

**Common Prosperity supports jewelry consumption growth in China, contrary to general capital market concerns.** Our China economist, Robin Xing, believes that the common prosperity initiative in China will take time, and aims to narrow the income gap within the country and expand the middle class. This is consistent with our investment thesis highlighted in China Consumer: Consumption 2030: At Your Service (27 Jan 2021). Luxury personal goods in China, including jewelry, are mainly purchased by the middle class, according to our latest AlphaWise survey and our conversations with jewelry retailers, as well as luxury shopping malls in the past 5-10 years.

## INDUSTRY VIEW

### China/Hong Kong Consumer | Asia Pacific

In-Line

### Encouraging AlphaWise survey results:

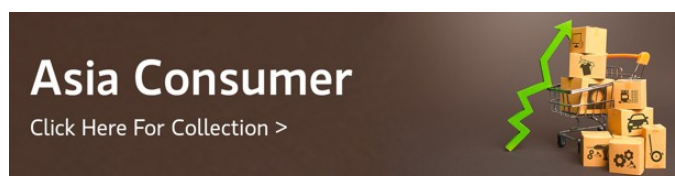
During July-August 2021, we surveyed 1,527 people in China who purchased jewelry in the last 12 months. Of those surveyed, 88% had household income of <Rmb40K/month (in other words, were middle class); 80-90% purchased jewelry for personal use (vs. 45-50% for gifting in 2014); and 80% were female, up from 52% in 2014. We believe this consumer profile is supportive of healthy and sustainable market growth.

**Growing jewelry spend in the next 3-5 years:** We surveyed 2,659 female consumers in China, including those who had not purchased any jewelry in the last 12 months. Among those surveyed, there were more plans to increase their spend on jewelry in the next 3-5 years. The purchase intention for jewelry was strongest among luxury categories. We see this as a positive sign that jewelry may gain consumers' wallet share in coming three years.

Exhibit 1: China jewelry stocks

Stock	Ticker	Rating	PT			Upside	F22 EPS		F23 EPS	
			NEW	Old	Chg		Chg	Chg		
CTS	002867.SZ	OW	25.0	24.0	4%	29%	2%	3%		
CTF	1929.HK	OW	18.5	17.5	6%	15%	-1%	5%		
LFX	600612.SS	UW	50.0	55.0	-9%	9%	-2%	5%		

Source: Morgan Stanley Research; Price as of 17th September 2021



**Local brands may gain further share in the next 12M:** We compared the number of respondents who plan to purchase jewelry in the next 12M with those that purchased jewelry in the preceding 12M. Among local brands, growth potential for CTS and CTF was 90% and 73%, respectively, while LFX was just 29%. Among foreign luxury brands, Cartier registered the highest growth potential at 74%. Among fashion brands, Pandora saw 42% growth potential.

**Stock implications - positive medium term earnings growth:** Our AlphaWise survey **gave us further confidence in the demand for luxury jewelry** in China over the medium term. Among Chinese jewelers, we **reiterate our OW ratings on CTS and CTF and raise our PTs accordingly**. We keep LFX UW due to its conservative strategy and high exposure in traditional pure gold products. We see **Richemont as the best proxy among European brands** with over 100% of group profit exposed to Cartier and Van Cleef. Among European fashion jewelry names, we see a **positive read-across for Pandora**, with the survey findings being supportive of a successful expansion in the region. Luxury shopping malls should also benefit with **HLP and CR Mix** having the highest exposure.

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# Investment Summary

In June 2021, we initiated coverage of the Chinese jewelry industry with a constructive outlook ([China/Hong Kong Jewelry Retailers: Industry initiation: Rare luxury proxy, led by local brands \(3 Jun 2021\)](#)). Since then, a common topic of discussion with investors has been about the sustainability of growth - whether local brands will lose market share to foreign brands or, going further, whether there will be a structural shift of luxury consumption to other product categories. In mid-August, the Chinese government [raised the notion of "common prosperity"](#), which has kick-started debate on whether there will be a prolonged shrinking in Chinese luxury/jewelry consumption.

We recently conducted an AlphaWise survey, which has given us greater confidence in our investment thesis. From July 26 to August 9, AlphaWise conducted an online survey of 5,453 individuals living in Tier 1-3 cities in China, 1,527 of which had purchased jewelry in the past 12 months or were intent on making a purchase in the next 12 months. We believe the market landscape has evolved and, given the rising importance of lower-tier cities, we expanded the sample coverage to include more cohorts living in lower-tier cities. We note that the sample skews towards younger, more affluent cohorts living in urban cities because of the online survey methodology. Median monthly household income of jewelry consumers in our AlphaWise survey was Rmb26K, which falls within the Rmb8-50K monthly household income range of the middle class.

**We compared the jewelry consumer profile to the survey conducted in 2014.** Of the jewelry consumers surveyed this year, 80-90% made purchases for personal own use, versus 45-50% of gifting demand in 2014. Of the total respondents, 80% were female in 2021, up from 52% in 2014. We believe the "anti-corruption" campaign of 2013-15 changed jewelry demand into more healthy and sustainable growth, as jewelry buyers nowadays are mostly the end-consumer.

**Consumers intend to increase their spend on jewelry in the near to medium term:** Of the 5.5K survey respondents, 2.7K were female, the key customer cohort for the luxury goods market in China, in our view. Of the female respondents, 9-17% of respondents planned to increase jewelry purchases (including foreign, local and fashion brands) and only 2-3% planned to reduce spending in the coming three to five years. Meanwhile, respondents plan to spend a largely similar amount on luxury bags/clothing. Of the 1.5K jewelry consumers, 24% plan to increase their spending on jewelry in the next 12 months, while 7% plan to reduce their jewelry consumption.

**Consumer perceptions about "buying local" support sustainable market share gains:** Consumer perceptions of local brands in terms of the top six jewelry purchase factors (product quality, design, fashion profile, product variety, materials used and value-for-money) are well-rounded, with above-average scores for each factor. This supports local brands capturing a majority of middle class demand, in our view. Meanwhile, foreign luxury brands and fashion brands rank top for unique designs and being fashionable, which are the top two purchase factors, though they are not considered value-for-money versus local brands.

**Stronger N12M purchase intent for local brands:** Compare with the L12M purchased ratio, N12M purchase intent for local brands (esp CTS and CTS) showed the highest growth potential at 50-60%. Among foreign luxury brands, purchase intent for Cartier was 50% higher than L12M purchase. Pandora purchase intent was 20% higher than L12M while Swarovski was neutral.

## Stock implications:

- **Chinese jewelry - we have further conviction in our OW on CTF and CTS:** We retain our constructive view on the Chinese jewelry market and continue to prefer Chow Tai Fook and Chow Tai Seng over Lao Feng Xiang. We raise 2023e EPS by 5% on average. We raise our price targets on CTF and CTS by 6% and 4%, respectively, and trim our price target on LFX by 9%. We keep LFX UW for its conservative strategy and high exposure in traditional pure gold products. Year to date, CTF stock has rallied ~60% ytd, outperformed Chinese consumer names (-13%) and MSCI China (-17%). We acknowledge potential short-term profit taking risk should there be any broader stock market volatility given strong stock performance ytd.
- **European luxury jewelry - reiterate OW ratings on LVMH and Richemont:** With over 100% of group profit generated by Cartier and Van Cleef, we see Richemont as the best vehicle to play the rise of luxury sales in China going forward. As for LVMH, while the group is less exposed to the category (c.10% of profits come from Bulgari and Tiffany), we have slightly higher upside to our target price (18% vs. 10% for Richemont).
- **European fashion jewelry - positive read-across for Pandora:** Whilst China only represents c.7% of Group sales for Pandora, the findings of our survey suggest that the brand has potential to expand further in the Chinese market and that management has a good chance of successfully boosting

sales in the region should the right strategy be put in place (one of the key debates on the stock).

- **HK/China property - positive for luxury retail malls like HLP and CR MixC:** Among HK/China stocks under coverage, Hang Lung Properties and CR MixC have the highest exposure to luxury retail malls. We expect HLP to continue its strong rental growth in China and see sustainable margin expansion. We expect CR MixC to deliver 52% earnings CAGR in 2020-23e, leveraging its key advantage in luxury shopping malls, and strong shopping mall pipelines.

**Risks to our call:** (1) Stock market volatility to have negative "wealth effect" on luxury/jewelry consumption; (2) potential for less extravagant consumption culture under recent regulation reset; and (3) short-video slowdown hence fewer advertisement and live commercial sales for jewelry products.

# China's common prosperity - implications for jewelry

Our China economist, Robin Xing, sees common prosperity as a long-term goal to be achieved via a gradual and flexible approach. It aims to narrow the income gap with an expansion of the middle class. **Contrary to common market concerns, we believe the luxury market is set to benefit from consumption growth from a more middle class**, who are the key consumer base according to our conversations with jewelry brands as well as luxury shopping malls in China in last 5-10 years.

We surveyed 1.5K people, who are mostly middle class, in China who purchased jewelry or intended to purchase jewelry in the next 12 months. Around **80-90% of respondents purchased jewelry for their own use in 2021**, as compared with 45-50% purchases for gifting in 2014. **Of respondents, 80% were female in 2021**, up from 52% in 2014. We see such a change in consumer profile supporting sustainable growth in jewelry consumption in China. Among the jewelry buyers, 24% plan to increase jewelry spending in the next 12 months and only 7% plan to reduce spending on jewelry.

We also surveyed 2.6K female consumers in China, including those who did not purchase jewelry, hence representing a broader consumer base. The survey suggested that **consumers still intended to increase spending in luxury personal goods in the coming 3-5 years**. Within that category, **incremental spending in jewelry is visibly stronger than other product categories** like bags and clothing. We see this as a positive sign of potential increase in wallet share for jewelry products.

**Risks to our call:** In the near-term, there could be a risk of luxury consumption slowdown due to the wealth effect amid general stock market volatility. Consumption sentiment may turn more "low-profile" culturally. So far, we are not aware of any regulation targeting luxury consumption directly.

## China's regulation reset and common prosperity - the top down view

**"Common prosperity" - why is that important to luxury consumption?** China's regulatory reset over the past 10 months reflects a shift in governance priorities from "growth first" to balancing growth and sustainability. As the "pro-growth" strategy over the past decades have led to higher inequality and social issues due to a lack of regulations on emerging sectors, the top leadership has emphasized "getting rich together" (common prosperity) as the new objective for the next stage of development in the midst of the CCP's 100-year anniversary (July 2021), and further elaborated on the "common prosperity" objective in mid-August 2021. It called for tackling social inequality and promoting social mobility with five tools – redistribution, social welfare, taxes, charity and inclusive education – and one target: to increase the middle-income group's share of the economy

However, this has led to market concerns about the income redistribution, which would dampen luxury consumption in China. The government clarified in late August 2021 that China does not aim for "absolute equality" nor mandatory wealth redistribution, and differentiated levels of income/wealth would still be a reality to preserve market incentives. Common prosperity is a long-term goal to be achieved via a gradual and flexible approach.

**View from our China economist:** Our China economist, Robin Xing, believes that the regulation reset and common prosperity are positive to overall consumption in the medium to long run, and will serve the purpose of rebalancing the rise in corporate power and the share of labor compensation. Meanwhile, household precautionary savings could be reduced with policy efforts in tackling the 'three big mountains' – escalating healthcare, education and housing costs, and a reduction in income inequality would enhance overall marginal propensity to consume, which tends to be higher for lower income groups than higher-income groups. This is consistent with our discussion earlier this year in China Consumption 2030: At Your Service (27 Jan 2021), where we forecast China's private consumption could more than double to about US\$13trn by 2030, matching the size of the US market now.

In terms of possible policy measures, Robin believes that the government will introduce: i) tax on inheritance and property; ii) wage adjustments linked to economic growth and inflation; iii) centralization of local land revenues for fiscal transfer to less-developed regions; iv) enhanced basic social security programs such as subsistence allowance, shelter, education and medical/elderly care; and v) economic and social incentives for firms and high-income individuals to perform charitable activities. That said, wealth tax appears unlikely in the near term due to its less predictable impact and diffi-

culties in implementation, and he does not expect a hike in personal income tax for middle and higher income groups, given the policy's purpose is to foster the rise of middle income groups (defined as annual household income at Rmb100K-500K) and an already elevated marginal tax rate of 45% for taxable income >Rmb1mn (in line with most EU economies).

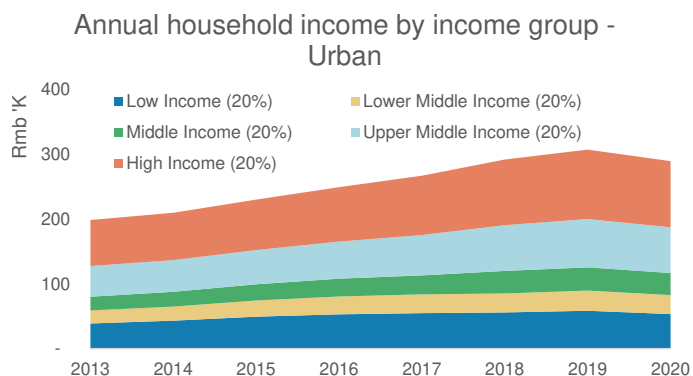
**Supportive for consumption, including luxury:** We expect consumption of luxury personal goods (including accessories, apparel, beauty and jewelry) to benefit as well, contrary to current concerns in the market. This is because the market for luxury personal goods is mostly contributed to by the middle class for their own consumption (instead of for business gifting, which was the case before the anti-grafting campaign pre-2015), as per our conversations with Chinese jewelry retailers and luxury retail malls operating on the Mainland for the past 10 years.

**We estimate that in 2020, 35-40% of Chinese households were classified as middle class** with household incomes of Rmb100-500K p.a. Within that, 45-50% of urban households and

~20% of rural households were middle class. **We estimate that the remaining households mostly had incomes below the middle-class threshold.** We estimate that 45-50% of urban households and 80-85% of rural households had household incomes <100K p.a.

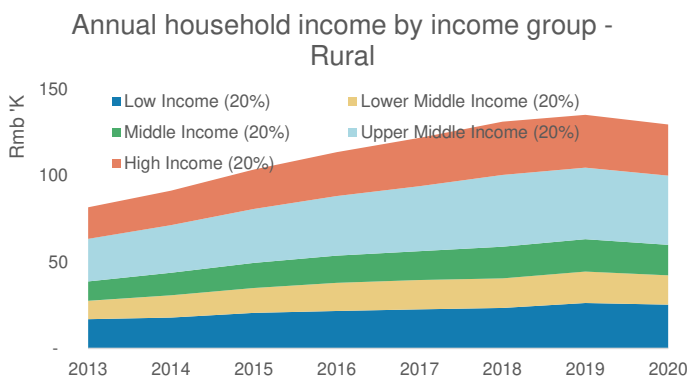
- Among urban households (Exhibit 2), we estimate that ~50% had household income of less than Rmb100K p.a. (the lower limit for middle class) in 2020. The average household income of the high income group (top 20% in terms of income) was Rmb240K p.a. in 2020, slightly lower than the mid-point of the middle class income range (Rmb100-500K p.a.).
- Among rural households (Exhibit 3), we estimate that ~80% of households were below the middle class line (< Rmb100K p.a.). The average household income of the high income group (top 20% in terms of income) was Rmb130K p.a. in 2020, slightly above the lower limit of middle class income definition.

**Exhibit 2:** Annual urban household income by income group in China, 2013-20



Source: NBS, Morgan Stanley Research

**Exhibit 3:** Annual rural household income by income group in China, 2013-20



Source: NBS, Morgan Stanley Research

**Rising middle class:** According to Euromonitor, 40% of Chinese households had annual household income of Rmb100-500K in 2020, up from 35% in 2017 and 15% in 2010. Meanwhile, the percentage of households with annual income <100K has fallen from 86% in 2010 to 58% in 2020. In 2020, only 2% of Chinese households had annual income over Rmb500K.

## AlphaWise survey results - encouraging

**The AlphaWise survey we conducted in July 2021 gives us further confidence in our investment thesis:** Two key takeaways were: 1) Jewelry consumers are now buying mostly for themselves, which suggests more sustainable growth; and 2) the majority of respondents said they intend to increase their spend on jewelry in the next 12 months as well as the next 3-5 years.

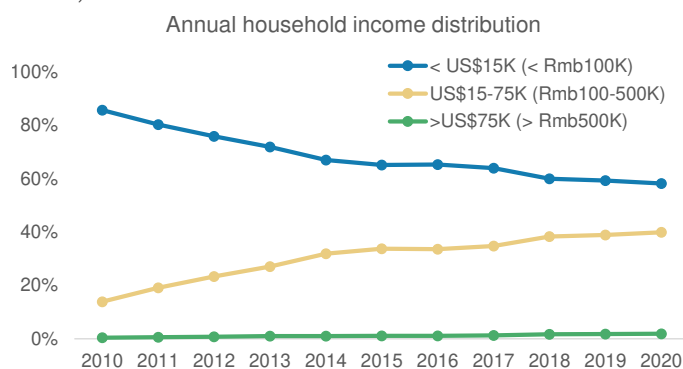
From July 26 to August 9, 2021, we surveyed 1,527 people that had either purchased jewelry in the past 12 months or intended to buy jewelry in the next 12 months. Because our survey used an online methodology, our sample skews younger and more affluent cohorts living in urban cities. The margin of error for findings on the total

sample is ±2.0% at a 90% confidence level; higher for subgroups. Wherever applicable the results are compared to previous surveys. We compared this survey with the AlphaWise survey we conducted in 2014 ([Hong Kong/China Discretionary: China Jewelry Brand Survey – Dissecting Chinese Consumers' Taste in Jewelry \(18 May 2015\)](#)).

We believe the market landscape has evolved since 2014 and, given the rising importance of lower-tier cities, we expanded the sample coverage to include more cohorts living in lower-tier cities (Exhibit 7). We believe this sample set represents a major consumer base and growth driver of the jewelry market in China.

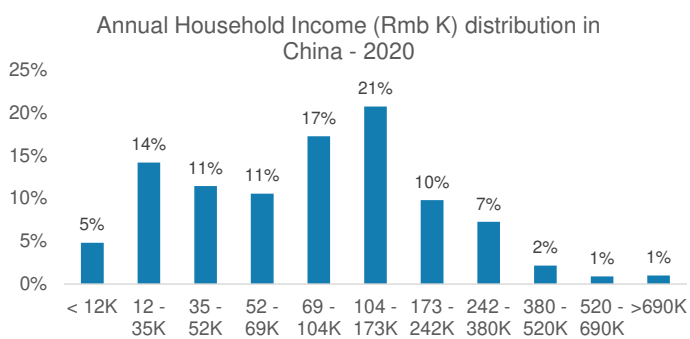
**Respondents had a middle class focus:** The survey respondents had an average household income of Rmb26K/month or Rmb310K/year in 2021. This is slightly below the mid-point of the middle class household income bracket of Rmb100-500K/year. Only 12% of survey respondents had household income over Rmb40K/month (Exhibit 6). The average household income of jewelry consumers increased by only 13% from our previous survey in 2014. This is much less than the 66% growth in China's per capita income during the period.

**Exhibit 4:** Annual household income distribution in China (urban + rural) 2010-20



Source: Euromonitor, Morgan Stanley Research

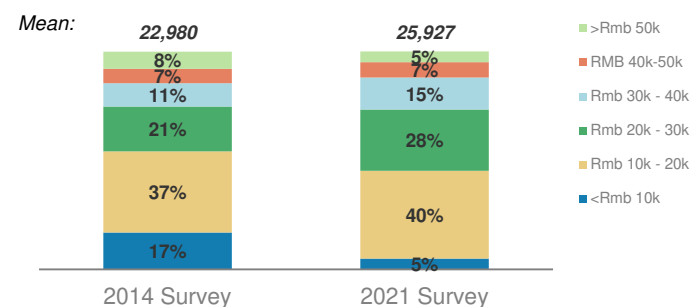
**Exhibit 5:** Annual household income distribution (urban + rural) in China 2020



Source: Euromonitor, Morgan Stanley Research

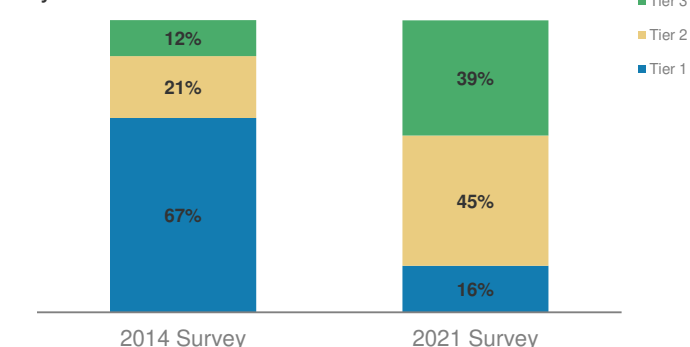
**Exhibit 6:** Monthly household income of jewelry consumers in China

### Monthly Household Income (by Total Jewelry Shopper)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 7:** Geographical distribution of jewelry consumers in China City Tier



Source: AlphaWise, Morgan Stanley Research



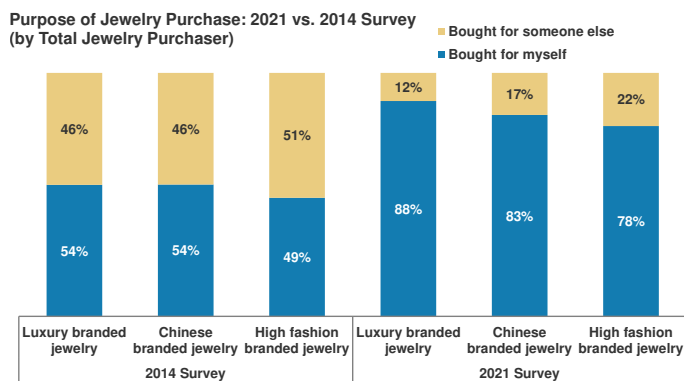
### Key change in consumer profile

Based on the survey results and our conversations with jewelry operators as well as luxury mall operators, we estimate that the middle class accounted for 80% of jewelry demand in China in 2020/21. Hence, we believe the study of their behavioral change would be key:

**Mostly self-consumption rather than gifting:** In our 2014 survey, 45-50% of survey respondents said they purchased jewelry for gifting. Whereas in 2021, gifting only accounted for 12-22% of demand (Exhibit 8). We believe this is largely due to the "anti-gifting" campaign conducted during 2013-15.

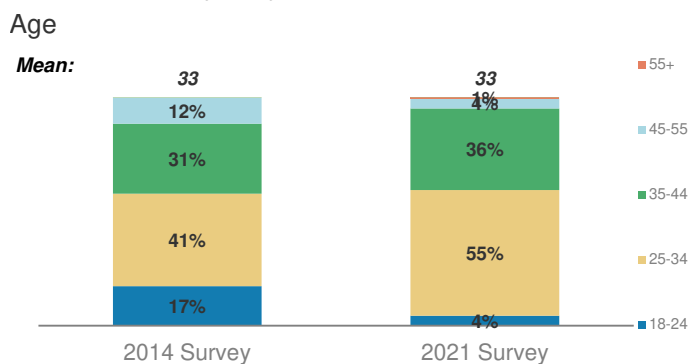
**More female buyers nowadays:** According to the survey, 80% of jewelry consumers were female, up from 52% in the 2014 survey (Exhibit 9). We attribute this to the rising incomes of females, and also more end-user/less "gifting" demand following the anti-gifting campaign.

**Exhibit 8:** Purpose of jewelry purchase - 2014 vs 2021



Source: AlphaWise, Morgan Stanley Research

**Exhibit 10:** Age of jewelry consumers in China



Source: AlphaWise, Morgan Stanley Research

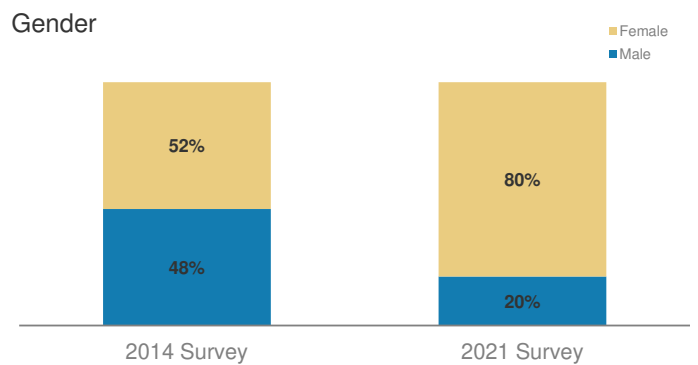
We see the change in the above consumer profile (more end-consumption and greater female focus) as supportive of sustainable growth in jewelry consumption in China.

**Millennials and Gen Z are key:** 55% of respondents who were jewelry consumers were aged 25-34 years while 36% of respondents were aged 35-44 years. The 45-55 year-old age group accounted for only 4% of respondents, down from 12% in the 2014 survey (Exhibit 10).

**Increasing purchase frequency:** In 2021, each consumer made 5.1 jewelry purchases L24M, up from 4.3 in the 2014 survey. Of survey respondents, 41% purchased an item of jewelry once every half year and 32% purchased once every three months.

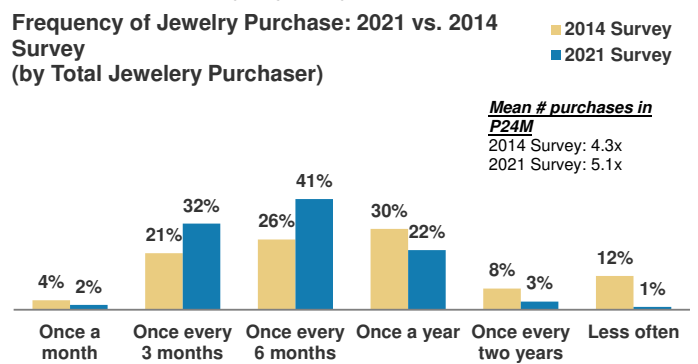
We believe the younger age cohort and increasing purchase frequency suggests a lower ticket value per purchase. This is supportive of fashion/affordable luxury consumption.

**Exhibit 9:** Gender of jewelry consumers in China



Source: AlphaWise, Morgan Stanley Research

**Exhibit 11:** Frequency of jewelry purchases: 2014 vs 2021



Source: AlphaWise, Morgan Stanley Research

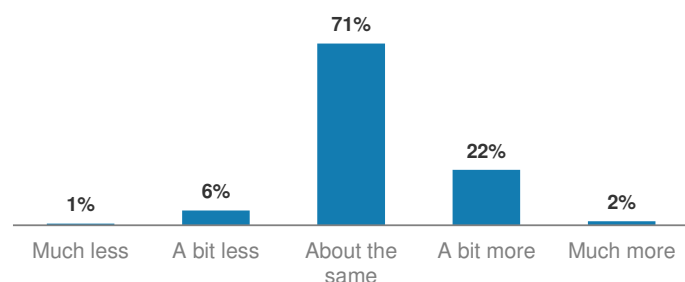
## Consumer purchase intentions

### Jewelry consumption: increased spending in the next 12 months

**Rising jewelry spend in N12M:** According to the survey results, the intent (among those who purchased jewelry in the last 12M or planned to purchase jewelry in the next 12 months) is to increase spending on jewelry in the next 12 months instead of reducing spending, with 24% saying 'higher spending' vs. 7% who said 'lower spending' (Exhibit 12). Consumers estimate their annual jewelry spend over the next 12 months will average at ~Rmb18,000, 10% higher than the level reported for the last 12 months, but 24% lower than the 2014 level (Exhibit 13). We believe this is related to "less gifting" and the growing fashion/affordable jewelry trend, both of which we discuss later in this report.

**Exhibit 12:** Expected change in jewelry spending in N12M - 2021 survey

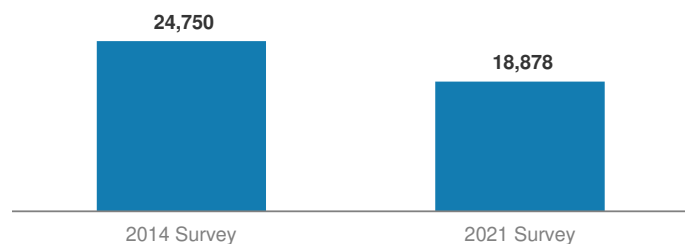
2021 Survey: Expected Change in Jewelry Spend over N12M (by Total Jewelry Purchaser)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 13:** Expectation of jewelry spending over N12M - 2014 vs 2021

Expectations on Spend over Next 12 Months (RMB): 2021 vs. 2014 Survey



Source: AlphaWise, Morgan Stanley Research

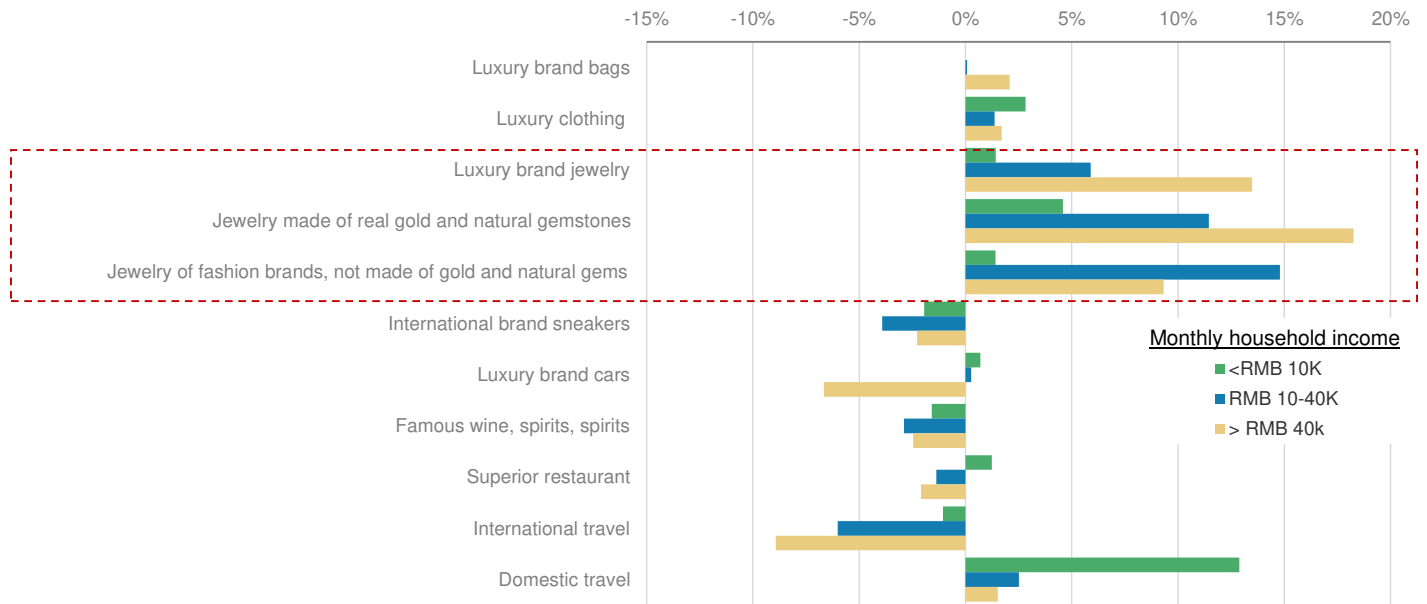
### Consumer plan to increase jewelry consumption in the coming 3-5 years:

Our conversations with investors, since our [Chinese jewelry stocks initiation in Jun-21](#), suggested that there were concerns about declining jewelry demand in 2021/22 after strong growth in 4Q20-1Q21. Some investors were concerned that demand would shift from local jewelry brands to foreign brands as household incomes rise.

Hence, we surveyed 5,453 consumers (including those who had and had not purchased jewelry in the last 12 months) in China about their plans to spend on luxury goods in the next 3-5 years. We analyzed the responses of the 2,659 female respondents (Exhibit 14), given their high exposure to the luxury goods market, including bags, clothing and jewelry. We see the broader sample as representing the general public, which includes non-jewelry/luxury consumers in the near-term:

- **There is a visible trend that consumers plan to increase their spending on jewelry more than on other categories.** The net spending intention (% increase less % decrease) for all luxury foreign jewelry brands (Cartier, Tiffany, Bulgari), local jewelry brand or real gold/gemstones products (Chow Tai Fook, Lao Feng Xiang) and fashion jewelry (Pandora, Swarovski) was higher than for other categories.
- **Middle class (monthly household income of Rmb10-40K) prefer local jewelry brands and fashion jewelry.** Meanwhile, high income individuals (monthly household income > Rmb40K) prefer foreign and local jewelry brands over fashion jewelry.
- Domestic travel intentions are strong, especially among the low income group (household income < Rmb10K).

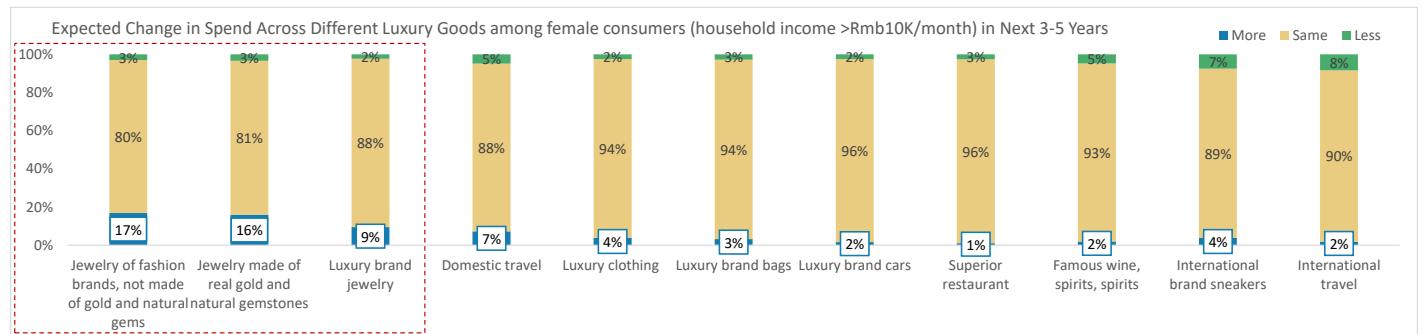
**Exhibit 14:** Net luxury spending in N3-5Y among female consumers among different household income groups in China  
 2021 Survey: Net Luxury Spending Shift Amongst Female Consumers in N3-5Y  
 (% Increase - % Decrease) (by Income Amongst Total Female Contactable Sample)



Source: AlphaWise, Morgan Stanley Research

Exhibit 15 shows the purchase intentions of female respondents with a monthly household income of >Rmb10K:

**Exhibit 15:** Expected change in spend across different luxury goods in N3-5Y among female consumers



Source: AlphaWise, Morgan Stanley Research

## Scenario assumptions

**Base case - slightly above private consumption growth:** We maintain our assumption that the jewelry market will grow at a 9% CAGR during 2019-30, which is slightly above our estimate for private consumption growth of a 7.9% CAGR during the period. The key drivers of consumption growth are growth in disposable income as well as the consumption premiumization trend. The AlphaWise survey results reaffirm our assumptions.

**Bull case - rapid expansion in the middle class supports strong jewelry demand:** In this scenario, the economies of lower tier cities develop rapidly and the urbanization trend accelerates. Jewelry brands penetrate further to lower tier cities, which supports revenue growth. We assume 15% market size CAGR during 2019-30 in this scenario.

**Bear case - less extravagant consumption dampens jewelry demand:** In this scenario, consumers may prefer to adopt a "less extravagant" style of living. Policy makers may impose direct policies to discourage jewelry demand, even though we see the direct policy risk as low. We assume 5% market size CAGR during 2019-30 in this scenario. Please see "Risks to our call" below for further elaboration.

## Risks to our call

In the context of [China's Regulatory Reset](#), we have yet to see any intent from policy makers to change industry practices for jewelry products or other luxury products. However, we highlight two potential downside risks below:

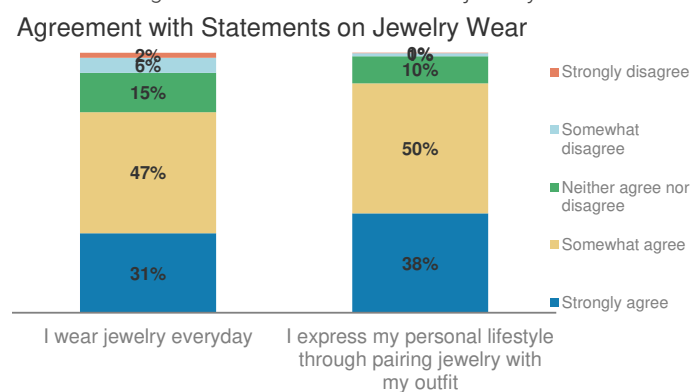
**(1) Stock market volatility may have a negative "wealth effect" on luxury and jewelry consumption**

**(2) Potential move away from extravagance:** The recent regulation reset and common prosperity direction may drive consumers to take a more "low-profile" view of luxury consumption to avoid being labeled as extravagant. In the survey, 88% of respondents said that they expressed their personal lifestyle via pairing jewelry with their outfit ([Exhibit 16](#)), and 54% of respondents said they either "always" or "frequently" post pictures on social media.

**(3) Slowdown in use of short-video platforms:** Jewelry brands, especially fashion and local brands, engaged KOLs (key opinion leaders) for promotions and also use live commerce as one of the sales channels. There have been some cleanup actions targeted at inappropriate content on short-video platforms since 2019. If these efforts were to increase, it could lead to slower user growth on these short-video platforms, their live commerce growth could slow down, affecting jewelry brands' business plans.

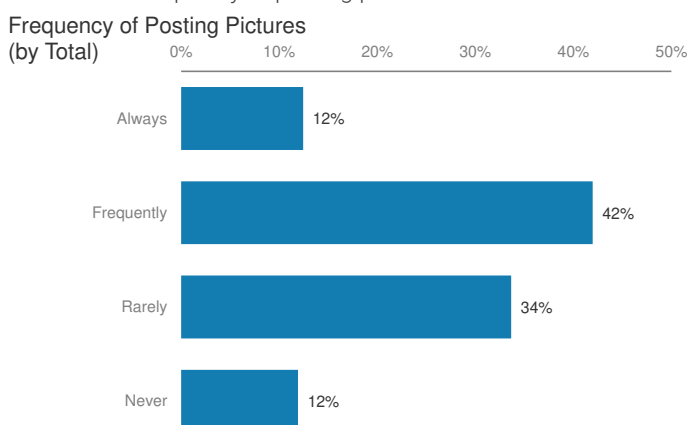
We note that Kuaishou, a short-video platform, tightened its monitoring of sales of "fake gold products" on its platform. While this could discourage some live commerce activities and potentially push out some small jewelry companies, we see this as an opportunity for large jewelry brands to gain market share.

**Exhibit 16:** Agreement with statements on jewelry wear



Source: AlphaWise, Morgan Stanley Research

**Exhibit 17:** Frequency of posting pictures 2021



Source: AlphaWise, Morgan Stanley Research

# Consumer preferences and brand momentum

The results of our AlphaWise survey suggested the potential for revenue growth (indicated by N12M purchase intentions over L12M purchase ratio), is slightly higher for local jewelry brands (especially CTS and CTF) than for foreign luxury brands. The potential for revenue growth appears to be lower for fashion brands on a high base.

Product quality remains the key factor for jewelry purchases, selected by ~70% of consumers in both the 2021 and 2014 surveys. Compared to 2014, consumers nowadays put *more focus on design, fashion element* and whether the *brand offers a wide range of products*, and are *less focused on value-for-money and product material*.

We analyzed consumers' perceptions of each brand for the top six purchase factors selected by >50% of jewelry consumers. Local brands are relatively all rounded with above-average score in all factors, even for the design/fashion element. Foreign luxury brands are aspirational with top scores in quality/design. Fashion brands are perceived as having a unique design and being fashionable, but score lower in product quality.

Compared with the 2014 survey, CTS ramped up the most in the consumer rankings in terms of product quality and design. Swarovski slipped the most in the consumer rankings for product quality but remained top in design and being fashionable.

## N12M purchase intention tracker - sales growth of local brands could outperform

We compare the purchase intentions for each brand for the coming 12 months as indicated by jewelry consumers, against the purchase patterns of the last 12 months (Exhibit 18), and measure the growth potential of each brand (Exhibit 19):

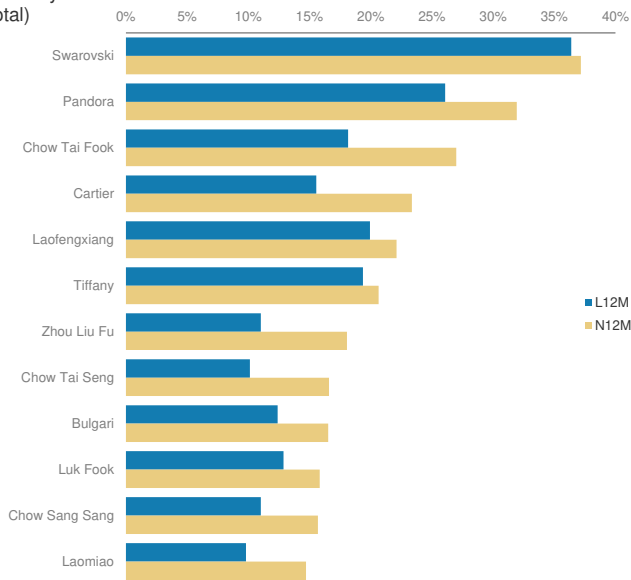
- Local jewelry brands stand out vs. foreign brands in terms of momentum growth potential in the coming 12 months: On average, the number of persons intent on buying the local brands we cover (CTF, LFX, CTS) in the coming 12 months are 64% higher than the purchased volume in the last 12 months. On average the purchase intentions for foreign luxury brands (Cartier, Bulgari and

Tiffany) is 51% higher than for L12M. Given the high base, the upcoming purchase intentions for fashion brands (Swarovski and Pandora) is only 30% higher than the L12M purchase volume.

- **Among local brands, Chow Tai Fook and Chow Tai Seng** saw the highest growth potential: Number of respondents that plan to buy CTS and CTF are 90% and 73% higher, respectively, than the L12M purchase volume. Lao Feng Xiang purchase intention was 29% higher than the last 12 months.
- **Among foreign brands, Cartier stands out:** Number of persons intending to purchase in N12M is 74% higher than L12M volume. Pandora purchase intent is 42% higher than L12M volume. Meanwhile, Swarovski and Tiffany purchase intention for N12M is only slightly higher than purchases in the L12M.

**Exhibit 18:** Jewelry purchased in L12M vs purchase intention in N12M

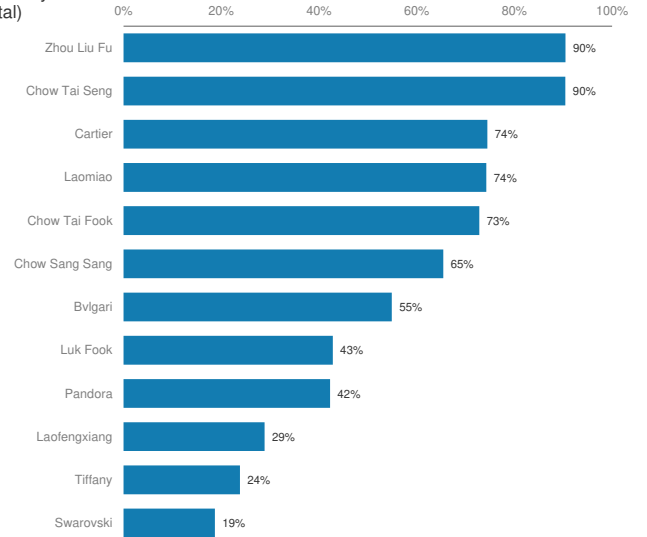
2021 Survey: Brand Purchased vs. Brand Intentions (by Total)



Source: AlphaWise, Morgan Stanley Research; \*L12M shoppers sample size = 1234; N12M shoppers sample size N = 1434

**Exhibit 19:** Jewelry purchase intention in N12M over L12M purchases

2021 Survey: Brand Growth Potentials (by Total)



Source: AlphaWise, Morgan Stanley Research

## Understanding consumer preferences

### Preference has changed - Growing preference of design and less on materials

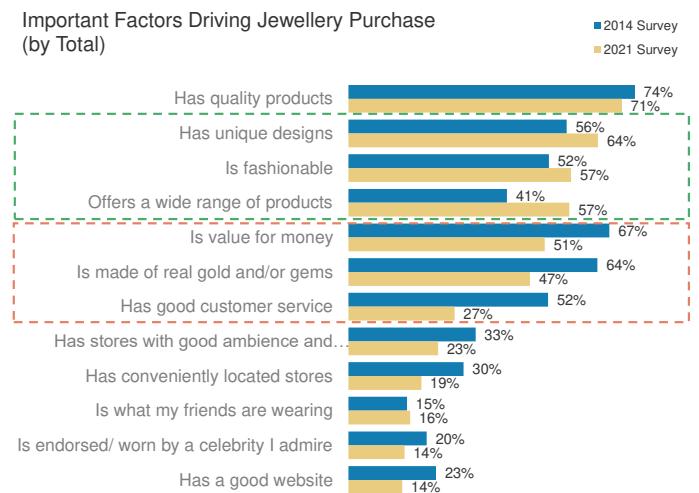
From our 2021 survey, key factors that drive jewelry purchases are: 1) product quality (71% of consumer selected as top 5 factors), 2) design (64% selection), 3) fashionable (57%), 4) wide range of products (57%), 5) value for money (51%), 6) made of real gold and gems (47%).

**Fashion jewelry on a rising trend:** We compared the key factors driving jewelry purchases as indicated by our 2014 and 2021 survey. Product quality remains the key factor for purchasing jewelry, selected by >70% of survey respondents in both 2014 and 2021. Yet the % of other factors has changed, indicating that consumers nowadays prefer fashion/design jewelry to traditional jewelry (Exhibit 20). Compared with the 2014 survey, jewelry consumers place more emphasis **on unique design, fashion elements** and whether the **brand offers a wide range of products**. At the same time, jewelry consumers nowadays are **less concerned about value-for-money, product materials** and **customer services**.

**Product material preferences have changed:** If we compare the survey responses from 2014 to 2021, among the products that were purchased in L12M by our survey respondents (Exhibit 21), the percentage of pure gold products declined from 79% to 44%, while just pearls declined from 29% to 11%, and natural gemstones declined from 54% to 31%. Meanwhile, the percentage of Karat-gold products increased from 13% in 2014 to 42% in 2021. We see this as a favorable trend for fashion jewelry over traditional gold products.

**Chinese jewelry consumers are open to purchasing different jewelry categories.** As per our AlphaWise survey, very few respondents stick to only one category of jewelry in China - 28% for Chinese brands, 11% for luxury brands and 7% for fashion brands. Most people will purchase different categories simultaneously to "mix and match".

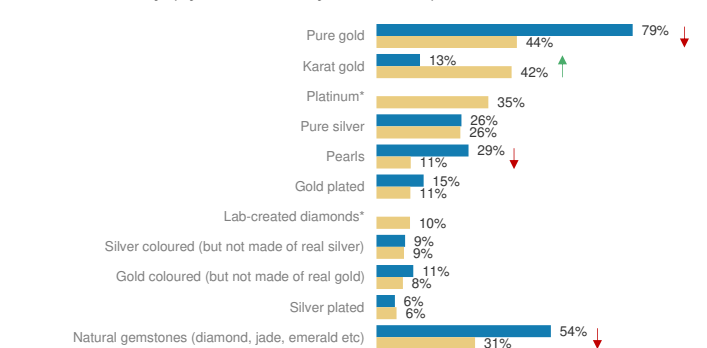
**Exhibit 20:** Important factors driving jewelry purchase



Source: AlphaWise, Morgan Stanley Research

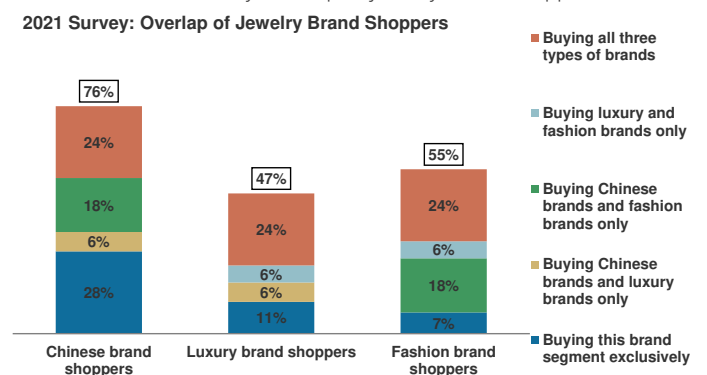
**Exhibit 21:** Materials made of jewelry purchased in L12M - 2021 vs 2014

Materials Made of the Jewelry Purchased in L12M: 2021 vs. 2014 Survey (by Total Jewelry Purchaser)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 22:** 2021 survey: overlap of jewelry brand shoppers



Source: AlphaWise, Morgan Stanley Research

### Consumer perceptions of individual brands

We analyzed consumers' perceptions of key jewelry brands across the top six purchase factors from our 2021 survey:

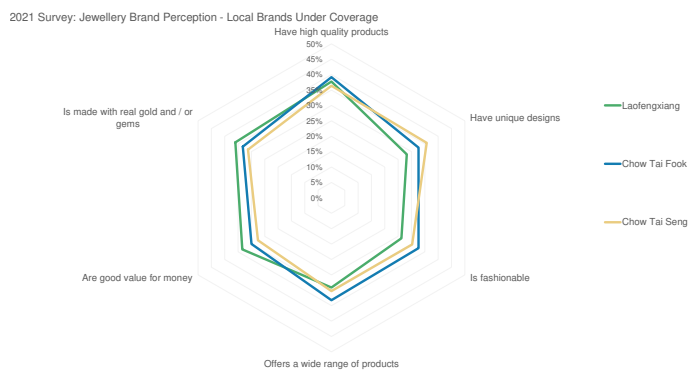
**Local brands (Exhibit 13) - balanced score card, CTF scores highest overall:** In general, the scores for local brands under coverage (CTF, LFX, CTS) were more "balanced" - around 30-40% of survey respondents agreed that these three brands offered each of the top six factors. CTF and LFX scored higher in product quality. CTF and CTS scored higher in "unique design", and "being fashionable". CTF scored higher in "product range".

**Foreign luxury brands (Exhibit 22) - aspirational:** The top three foreign luxury jewelry brands in terms of retail sales value in China (Cartier, Tiffany, Bulgari) all scored higher than local brands in terms

of product quality, design and being fashionable. Yet, they all scored lower than local brands in terms of value for money as well as made of real gold/gems. Of these three, Tiffany scored higher in terms of product quality and being fashionable, while Cartier and Bulgari scored higher for having a unique design.

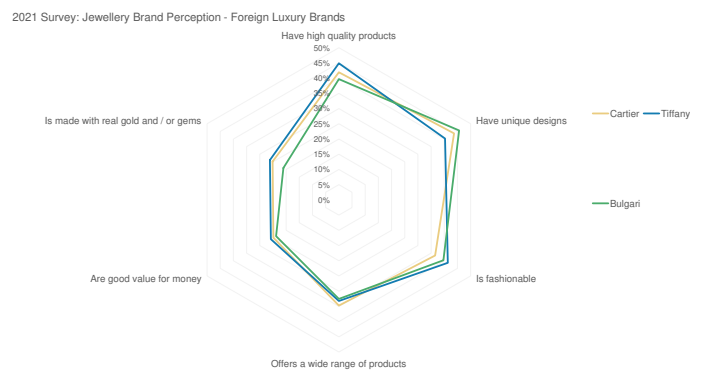
**Fashion jewelry brands (Exhibit 7) - unique design but only average in product quality and value-for-money:** Of no surprise, fashion jewelry brands (e.g. Swarovski, Pandora, APM Monaco) are perceived as having unique design and being fashionable, with scores even higher than foreign luxury brands. Yet, they generally scored average in terms of product quality and value-for-money, with these two score slightly lower than for local brands. Among fashion jewelry brands, Pandora scored highest in terms of design, and being fashionable, but scored lower in terms of product quality and product range.

**Exhibit 23:** Consumer perceptions of top 6 jewelry purchase factors - local brands



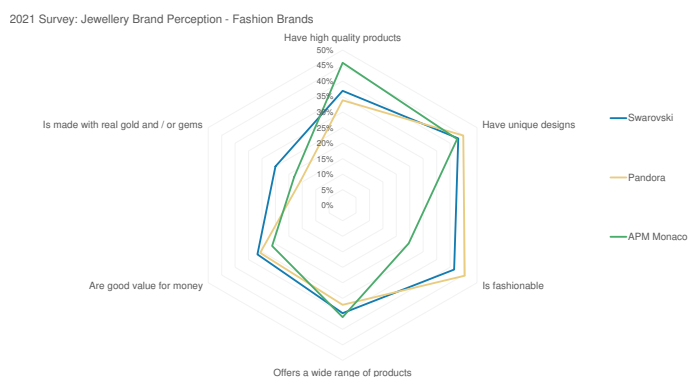
Source: AlphaWise, Morgan Stanley Research

**Exhibit 24:** Consumer perceptions of top 6 jewelry purchase factors - foreign luxury brands



Source: AlphaWise, Morgan Stanley Research

**Exhibit 25:** Consumer perceptions of top 6 jewelry purchase factors - fashion brands



Source: AlphaWise, Morgan Stanley Research



**Change in perception from 2014 to 2021:** We also compared the ranking of consumer perceptions among local and fashion brands of the top three factors, from 2014 to 2021:

- **Product quality (Exhibit 26):** The most visible change is that Swarovski's ranking slipped from No.1 in 2014 to No.4 in 2021. Pandora also slipped one place from No.6 in 2014 to No.7 in 2021. Rankings of local brands, CTF, LFX and CTS, all improved. This indicates that the local brands have developed a reputation among consumers during the period.
- **Design (Exhibit 27):** The most visible change is that the ranking for Chow Tai Seng jumped from No.7 in the 2014 survey to No.3 in the 2021 survey. Pandora and Swarovski remain the top two brands. Pandora replaced Swarovski as No.1 in terms of unique design among our selected brands.
- **Being fashionable (Exhibit 28):** Similar to consumer perceptions of design, Pandora and Swarovski continue to be perceived as the top two brands in terms of being fashionable, but Pandora replaced Swarovski as the No.1 fashionable jewelry brand among our selected brands.

**Exhibit 26:** Consumer perceptions of quality - Local brands and fashion brands 2021 vs 2014

High Quality	Rank 1	2	3	4	5	6	7	8	9	10
2021	CTF	LFX	LF	S	CTS	LM	P	CSS	ZLF	TSL
2014	S	CTF	LFX	CSS	3DG	P	CTS	TSL	LM	LF

Source: AlphaWise, Morgan Stanley Research; CTF: Chow Tai Fook; LFX: Liaofengxiang; CTS: Chow Tai Seng; CSS: Chow Sang Sang; LF: Luk Fook; TSL: Tse Sui Luen; LM: Laomiao; ZLF: Zhouliufu; P: Pandora, S: Swarovski,

**Exhibit 27:** Consumer perception of unique design - Local brands and fashion brands 2021 vs 2014

Unique Design	Rank 1	2	3	4	5	6	7	8	9	10
2021	P	S	CTS	CSS	LM	CTF	LF	ZLF	LFX	TSL
2014	S	P	3DG	TSL	CTF	CSS	CTS	LFX	LF	LM

Source: AlphaWise, Morgan Stanley Research; CTF: Chow Tai Fook; LFX: Liaofengxiang; CTS: Chow Tai Seng; CSS: Chow Sang Sang; LF: Luk Fook; TSL: Tse Sui Luen; LM: Laomiao; ZLF: Zhouliufu; P: Pandora, S: Swarovski,

**Exhibit 28:** Consumer perception of being fashionable - Local brands and fashion brands 2021 vs 2014

Fashionable	Rank 1	2	3	4	5	6	7	8	9	10
2021	P	S	ZLF	CTF	CSS	LF	CTS	LM	LFX	TSL
2014	S	P	3DG	CTF	TSL	CSS	CTS	LF	LFX	LM

Source: AlphaWise, Morgan Stanley Research; CTF: Chow Tai Fook; LFX: Liaofengxiang; CTS: Chow Tai Seng; CSS: Chow Sang Sang; LF: Luk Fook; TSL: Tse Sui Luen; LM: Laomiao; ZLF: Zhouliufu; P: Pandora, S: Swarovski,

# Implications for Chinese jewelry players

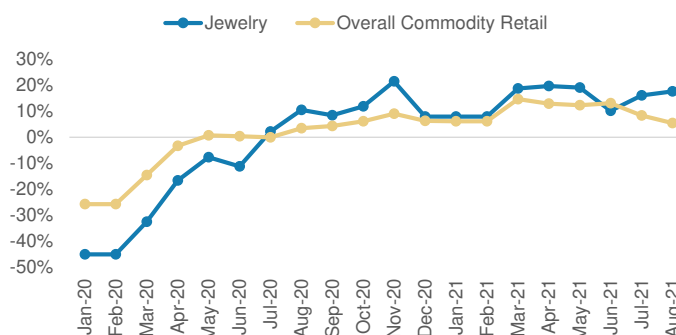
**We reiterate our Constructive view on Chinese Jewelry players following the encouraging results from our latest AlphaWise survey:** Our investment thesis, discussed in our [Jun-21 initiation report](#), is unchanged, we expect sustainable market growth, driven by fashion/affordable jewelry and local brands gaining market share. As discussed earlier in this report, our AlphaWise survey results show that consumers have a growing preference for product design/fashion trends rather than product materials. Purchase intentions for local brands are strong versus foreign brands.

**Local brands to gain market share as the middle class expands:** Consumer perceptions of local brands in terms of the top six jewelry purchase factors (product quality, design, fashionable, product variety, material and value-for-money) are well-rounded with an above-average score in each factor ([Exhibit 23](#)). This suggests local brands are set to capture a significant proportion of middle class demand, in our view. Meanwhile, local jewelry brands are expanding store networks and increasing penetration rates in lower-tier cities. This should support sustainable growth outperformance, in our view.

**Market is overly concerned about the notion of common prosperity:** Investors we have talked to over the past month are mostly concerned about the Chinese government's focus on the idea of common prosperity dampening demand for luxury goods, including jewelry. On the contrary, we are constructive on jewelry consumption because the market appeals to the middle class and is end-consumer focused.

**Jewelry retail sales growth continued to outperform:** Jewelry retail sales in Aug-21 were 18% higher than Sep-19, accelerating 10% in Jun-21 and 16% in Jul-21 ([Exhibit 29](#)). Meanwhile, overall retail sales growth in China has started to decelerate since Jun-21. Overall retail sales in Aug-21 were 5% higher than Aug-19, a slowdown from 13% in Jun-21 and 8% in Jul-21. Both Chow Tai Fook and Chow Sang Sang (not-covered) commented that jewelry demand remained healthy and sustainable sequentially. And leading jewelry brands' same-store-sales-growth is tracking stronger than the broader market.

**Exhibit 29:** China retail sales growth vs 2019  
China retail sales vs 2019



Source: NBS, Morgan Stanley Research

**We continue to prefer CTS and CTF to LFX:** CTS has a greater selection of high fashion jewelry and better online exposure than peers. We like CTF for its growing fashion/affordable jewelry offering and asset light strategy. LFX's strategy is more traditional, with high exposure to traditional gold products.

## What's changed

**Chow Tai Seng (002867.SZ):** We raise our 2023 EPS estimate by 3% to reflect our constructive view on jewelry market growth. Our target 2022 PE is unchanged at 17x and we raise our price target by 4% to Rmb25.

**Chow Tai Fook (1929.HK):** We raise our F23 EPS estimate by 5% as we gain more confidence on jewelry consumption growth in the medium term after the AlphaWise survey result. CTF is the market leader with increasing market share. We raise our price target by 6% to HK\$18.5. We roll forward our target P/E by six months to F23. We lower our target PE from 23x to 21x as the HK-China border reopening timeline has become more uncertain after China saw a resurgence in Covid-19 in July-August.

The stock is trading at 23x F22e and 18x F23 PE on MSe. This is 1.5SD and 1SD above average since 2016, which we see as supportive as the company is changing its business model by becoming more asset light with rapid franchise store expansion. We acknowledge potential short-term profit taking risk should there be any broader stock market volatility give strong stock performance ytd. Year to date, CTF stock price is up ~60%, the second best performer among our Chinese consumer coverage universe. On average, Chinese consumer stocks declined 13% ytd, and discretionary stocks on average are -9% ytd. MSCI China is -17% ytd.

**Laofengxiang (600612.SS):** We lower our 2021 EPS by 7% as margin compression in 2Q21 was more severe than expected. But we expect LFX to gradually improve margin from SG&A savings in 2022-23. Similar to CTF and CTS, we raise our 2023 EPS estimate for LFX by 5%. We lower our PT by 9% to Rmb50, and lower our target 2022 PE from 15x to 14x. This is to reflect weaker than expected cost management.

**Exhibit 30:** China jewelry stocks - what's changed

Stock	Ticker	Rating	PT			F21 EPS			F22 EPS			F23 EPS		
			NEW	Old	Chg	NEW	Old	Chg	NEW	Old	Chg	NEW	Old	Chg
CTS	002867.SZ	OW	25.0	24.0	4%	1.21	1.17 e	3%	1.45	1.43 e	2%	1.68	1.62 e	3%
CTF	1929.HK	OW	18.5	17.5	6%	0.60	0.60 e	0%	0.70	0.70 e	-1%	0.87	0.83 e	5%
LFX	600612.SS	UW	50.0	55.0	-9%	3.35	3.58 e	-7%	3.60	3.68 e	-2%	4.22	4.00 e	5%

Source: Morgan Stanley Research

# Implications for European luxury jewelry makers

One of the differences between the Chinese jewelry market and that of the West is the prevalence of jewelry purchases as a way to store wealth. Hence, historically, there has been a greater proportion of 24k gold (pure gold) pieces in total jewelry sales in China. That being said, our most recent survey provides further evidence to the idea that purchasing habits are changing, with a greater focus from millennials and Gen Z on design and branding, rather than on the material a given piece of jewelry is made of. In that context, we expect younger generations to gravitate towards Western luxury brands such as Cartier, Tiffany, Bulgari or Van Cleef & Arpels (VCA). Combined, these brands account for the vast majority of highly recognizable lines (e.g., Cartier Love or VCA's Alhambra), which we view as the key to success in jewelry sales ... particularly in the age of social media.

## European luxury players - Bulgari, Tiffany, Cartier, Van Cleef & Arpels

**Chinese nationals are a crucial cohort for European luxury jewelry brands.** Pre-Covid, we estimate that Chinese nationals accounted for c.48% of the sales for Bulgari, c.44% for Cartier, c.40% for Van Cleef & Arpels (VCA) and c.25% for Tiffany. According to a jewelry report by consulting firm McKinsey and fashion magazine, *Business of Fashion* (14 June 2021), the market for branded luxury jewelry (priced at US\$1,801-\$36,000) in Asia will grow at a 10%-14% CAGR (2019-2025), outgrowing the global market (which was set to grow at a

9%-13% CAGR, 2019-2025). We believe the Chinese market is the key driver behind Asia's outperformance.

**European luxury brands screen extremely well on key purchasing criteria.** As mentioned earlier in this report, the key purchasing criteria (KPC) among Chinese consumers are as follows: 1) product quality (71% of respondents selected this factor as a top five KPC), 2) design (64%), 3) fashionable (57%), 4) wide range of products (57%), 5) value for money (51%), and 6) made of real gold and gems (47%). As can be seen in Exhibit 31, European luxury brands dominate the rankings of the top three KPCs.

**Exhibit 31:** Screening on key purchasing criteria

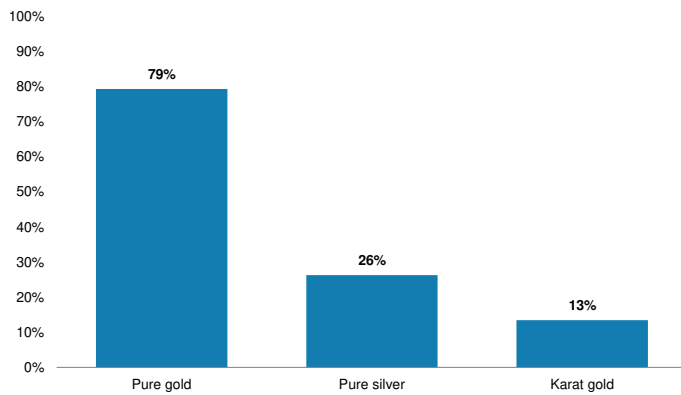
2021 Survey	High quality	Unique designs	Fashionable	Wide range of products	Value for money	Real gold/gems
Rank 1	Tiffany	Bulgari	Pandora	Zhou Liu Fu	Laomiao	Laofengxiang
Rank 2	Cartier	Pandora	Swarovski	Swarovski	Laofengxiang	Luk Fook
Rank 3	Bulgari	Cartier	Tiffany	Cartier	Swarovski	Chow Tai Fook
Rank 4	Chow Tai Fook	Swarovski	Bulgari	Chow Tai Fook	Chow Sang Sang	TSL
Rank 5	Laofengxiang	Tiffany	Cartier	Tiffany	Pandora	Laomiao
Rank 6	Luk Fook	Chow Tai Seng	Zhou Liu Fu	Luk Fook	Zhou Liu Fu	Chow Tai Seng
Rank 7	Swarovski	Chow Sang Sang	Chow Tai Fook	Bulgari	Chow Tai Fook	Chow Sang Sang
Rank 8	Chow Tai Seng	Laomiao	Chow Sang Sang	Pandora	Luk Fook	Zhou Liu Fu
Rank 9	Laomiao	Chow Tai Fook	Luk Fook	Chow Tai Seng	Chow Tai Seng	Tiffany
Rank 10	Pandora	Luk Fook	Chow Tai Seng	Chow Sang Sang	Tiffany	Cartier
Rank 11	Chow Sang Sang	Zhou Liu Fu	Laomiao	Laofengxiang	Cartier	Swarovski
Rank 12	Zhou Liu Fu	Laofengxiang	Laofengxiang	TSL	TSL	Bulgari
Rank 13	TSL	TSL	TSL	Laomiao	Bulgari	Pandora

Source: AlphaWise, Morgan Stanley Research

**Consumer preferences for the material that jewelry is made from has diverged from pure gold (24k gold) in China.** The key positive surprise from KPC ranking is the strong performance of European luxury brands in terms of "high quality" - Tiffany ranks first, followed by Cartier and Bulgari. Historically, the perceived quality of products had been associated with whether the product was made of pure gold. In our 2014 survey, pure gold was the dominant material that Chinese jewelry consumers preferred (see Exhibit 32). However, in the 2021 survey, only 44% of the jewelry purchased was made of pure gold. We had thought this was one of the biggest concerns for European luxury jewelry brands because pure gold jewelry had not been part of the European luxury jewelry brands' DNA as it had been

for the Chinese local brands'. However, while respondents to our survey who bought karat gold in the last 12 months increased by 28% from 2014 to 2021, those who bought pure gold fell by -36% over the same period (see Exhibit 33). That being said, gold is still the dominant material purchased by Chinese jewelry consumers. Of survey respondents, 44% said they purchased pure gold jewelry in the last 12 months vs. 42% for karat gold in 2021. In addition, 55% of respondents said they would purchase pure gold jewelry in the next 12 months vs. 41% for karat gold. All in all, we remain positive on European luxury jewelry brands due to higher acceptance rate of karat gold.

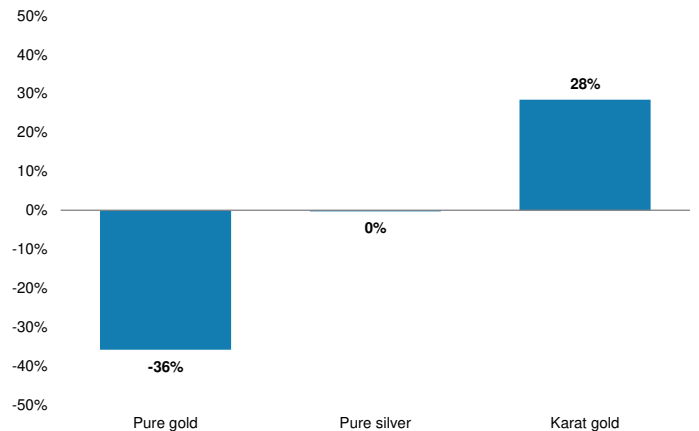
**Exhibit 32:** Jewelry materials purchased by Chinese consumers in LTM, 2014



Source: AlphaWise, Morgan Stanley Research

Note: Respondents were asked the materials of the jewellery they bought in LTM. For example, 79% of the respondents purchased pure gold jewellery in LTM as per our 2014 survey.

**Exhibit 33:** Jewelry materials purchased in LTM (2014 vs. 2021)

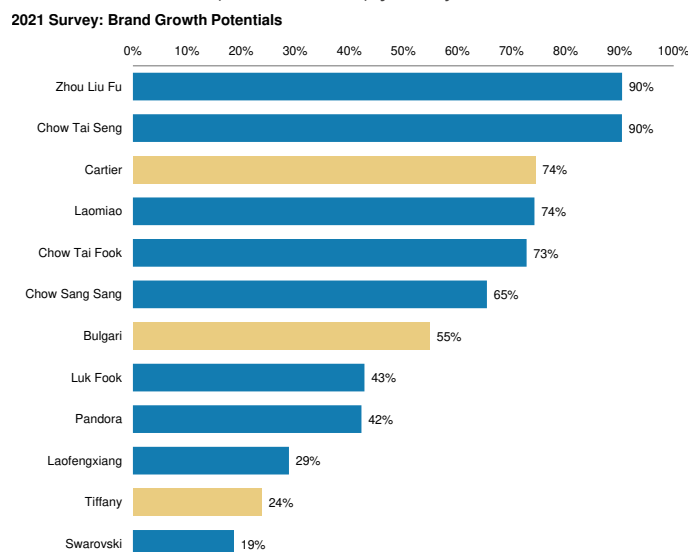


Source: AlphaWise, Morgan Stanley Research

**Brand momentum continues to be strong for European luxury names.** Out of the four European luxury brands, three brands were among the top 15 brands with the largest growth potential - Cartier, Bulgari and Tiffany. Crucially, Cartier is the number three in terms of growth potential. This, in our view, can be credited to Cartier's continuous efforts to rejuvenate its brand and investment in the China market. As mentioned above, millennials and GenZ are the key in China's jewelry market, accounting for 91% of consumers, as per our

AlphaWise survey. Mr Vigneron, CEO of Cartier, stated in an interview given at Auditorium in SIHH in January 2018 that "Cartier makes 43% of its sales from under-35s. In Asia, it's more than half" (see more from Richemont: An Introductory Guide). As per our survey, almost 70% of the Jewelry consumers had heard of the Cartier brand (see Exhibit 35). The four European luxury brands are among the top 15 most known brands in China, which we believe bodes well for their brand momentum going forward.

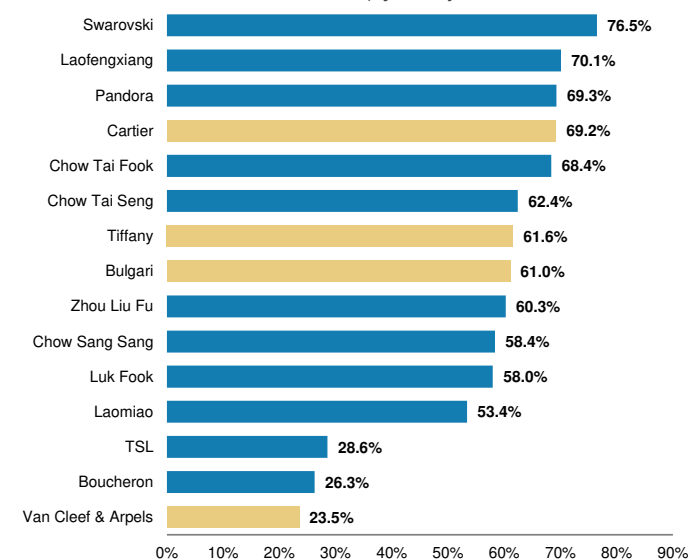
**Exhibit 34:** Growth potential of top jewelry brands in China, 2021



Source: AlphaWise, Morgan Stanley Research

Note: Growth potential is calculated as "purchase in NTM" / "purchase in LTM" - 1. We highlighted the European luxury brands in yellow. There was only 1% of the respondents in our sample purchased Van Cleef in the past year and it ranks the 17th by growth potential.

**Exhibit 35:** Brand awareness of top jewelry brands in China, 2021



Source: AlphaWise, Morgan Stanley Research

Note: Brand awareness is gauged by the percentage of respondents who have heard of the brand. For instance, 69.2% of the respondents said that they heard of Cartier as per our 2021 survey.

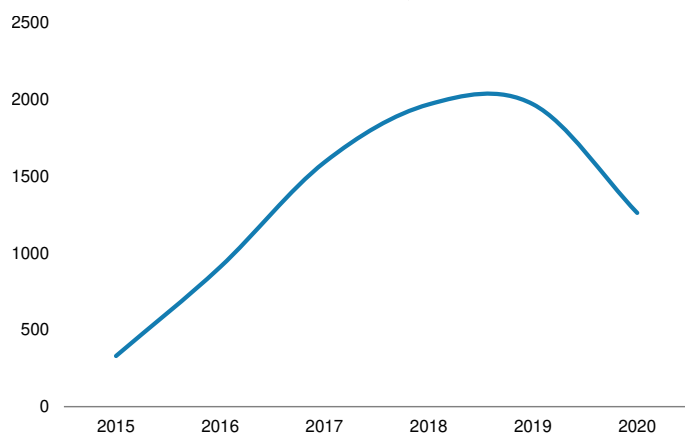
# Implications for European fashion jewelry players

## European fashion player – Pandora

**Pandora has historically struggled to gain traction in the Chinese market.** Pandora officially entered the Chinese market in 2015. After a first period of expansion through store openings, the brand's LFL quickly turned negative and the brand failed to gain meaningful traction among consumers, despite the strong potential offered by the Chinese market. China accounts only for c.6-7% of the Group's sales

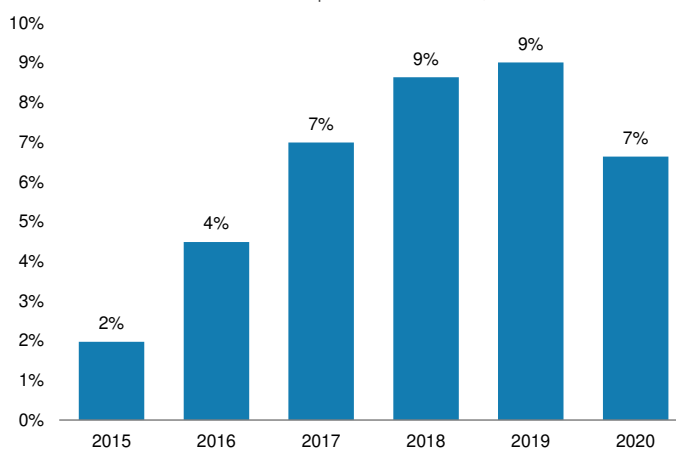
as of today (compared to 20-40% for luxury names). Whilst historically many western fashion brands failed to conquer the Chinese market due to the uniqueness of consumer preferences (such as a strong preference for gold over silver), Pandora's issue was mostly company-specific and due to a poor positioning and limited marketing investment, as per feedback from the company's new management team.

**Exhibit 36:** Pandora: revenue in China, 2015-20



Source: Company data, Morgan Stanley Research

**Exhibit 37:** Pandora: sales exposure to China, 2015-20



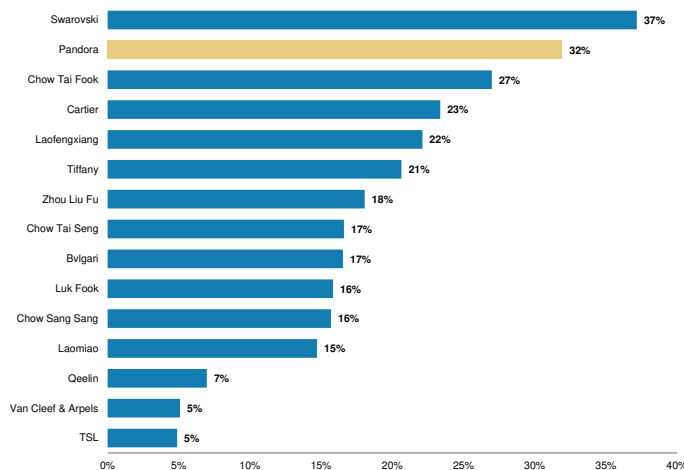
Source: Company data, Morgan Stanley Research

**China, however, is now seen as one of the most promising markets for Pandora.** After a change in management, Pandora launched a new global transformation plan (Phoenix). As part of this new strategic plan, management now aims to address the issues and re-establish Pandora's presence in the Chinese market, targeting to triple sales over the long term to c. DKK6bn (equalling c.€800m) in a market worth DKK680bn as of today. Whilst the company is convinced that Pandora's global brand attributes and core proposition are relevant to the Chinese consumer, the market so far has remained partly skeptical on this turnaround given its unproven track record.

**Our AlphaWise survey suggests that the brand has potential in the Chinese market.** We were positively surprised by the results of this survey. Based on our findings, Pandora is already enjoying strong

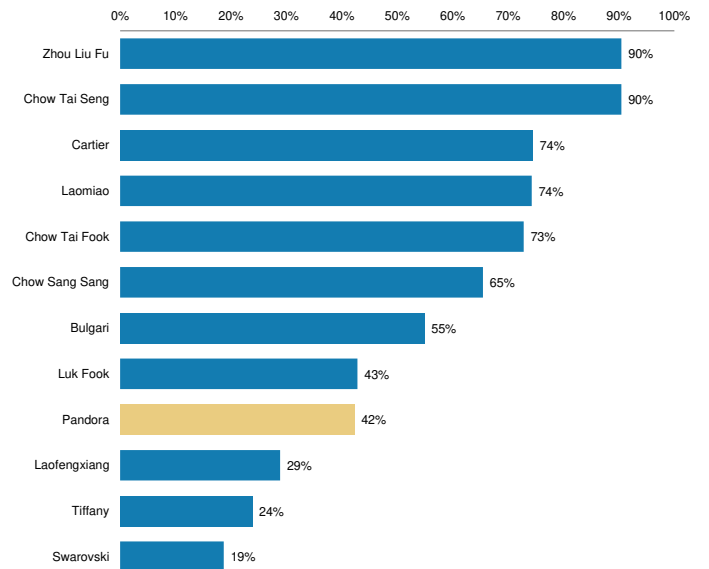
brand awareness (Exhibit 42) and good purchasing intentions, suggesting a relatively solid starting point for the ongoing turnaround. As illustrated in Exhibit 38, Pandora is the second brand that is most likely to be purchased by our sample over the next 12 months, with very high growth potential (see Exhibit 39). The brand is also the second favorite (see Exhibit 40) and second most often purchased (see Exhibit 41) brand in our sample. Interestingly, it is also the most frequently bought online (Exhibit 43). Finally, that Chinese are buying jewelry more frequently than before (every 3 months or every 6 months, as per Exhibit 45) and diversifying their purchases away from pure gold (Exhibit 44) are both very positive trends for a brand like Pandora. Therefore, all in all, our findings are supportive of brand improvement in the region and suggest that management has a good chance of success should the right strategy be put in place.

**Exhibit 38:** Brand mostly likely to be purchased in the NTM, 2021



Source: AlphaWise, Morgan Stanley Research  
 Note: The sample was asked to choose the brands that they are most likely to purchase in NTM, e.g., 32% of the sample said they would mostly likely buy Pandora in NTM.

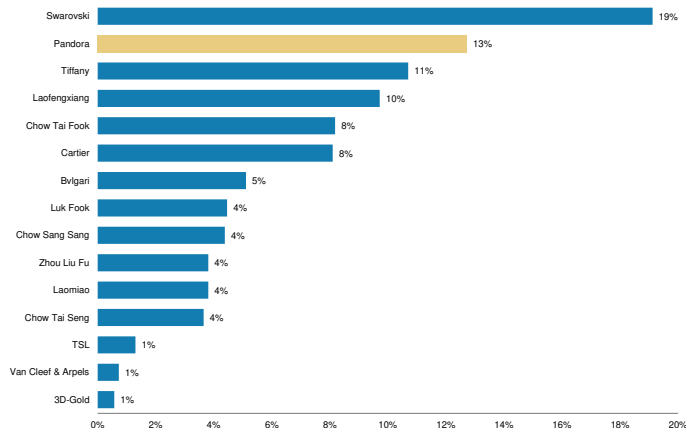
**Exhibit 39:** Top jewelry brands with the highest growth potential in the NTM, 2021



Source: AlphaWise, Morgan Stanley Research  
 Note: Growth potential is calculated as "purchase in NTM" / "purchase in LTM" - 1.

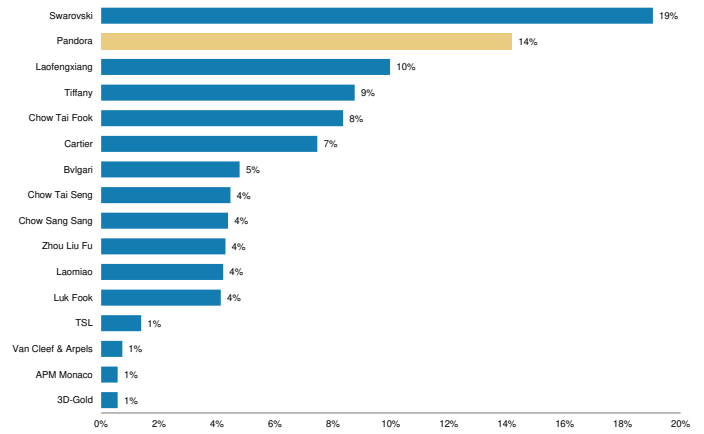


**Exhibit 40:** Most favorite brand of Chinese jewelry consumers, 2021



Source: AlphaWise, Morgan Stanley Research

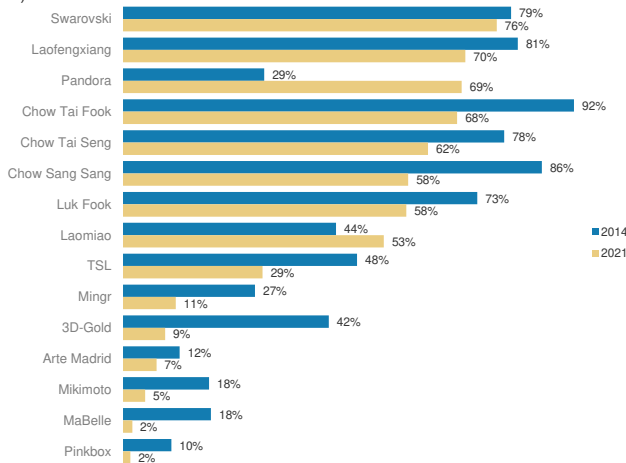
**Exhibit 41:** Most often purchased brand of Chinese jewelry consumers, 2021



Source: AlphaWise, Morgan Stanley Research

**Exhibit 42:** Brand awareness ranking, 2021 vs. 2014

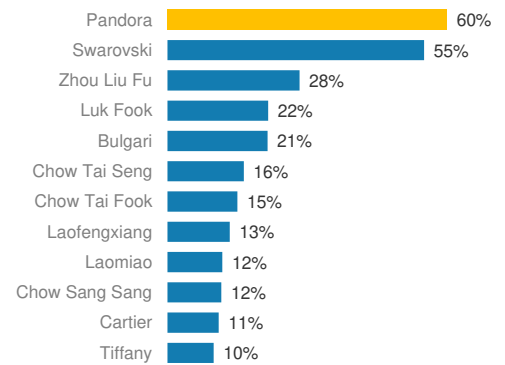
Jewellery Brand Awareness: 2021 vs. 2014 Survey (by Total)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 43:** Brands most frequently bought online, 2021

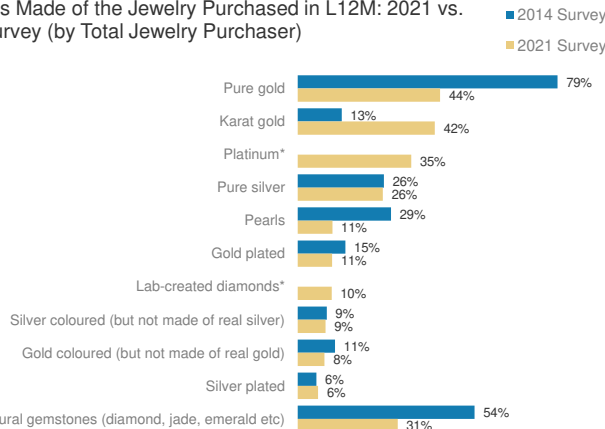
2021 Survey: Branded Jewelry Bought Online in L12M (by Most Often Brand Purchaser)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 44:** Materials of the jewelry purchased, 2021 vs. 2014

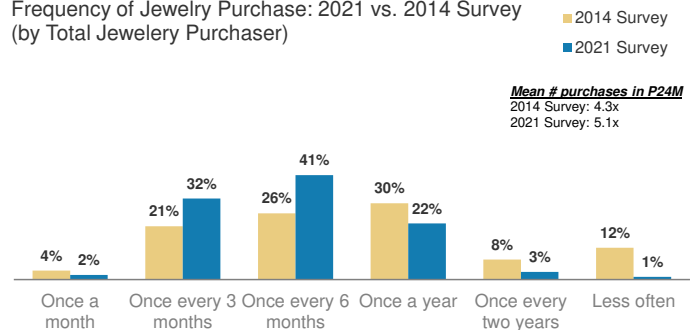
Materials Made of the Jewelry Purchased in L12M: 2021 vs. 2014 Survey (by Total Jewelry Purchaser)



Source: AlphaWise, Morgan Stanley Research

**Exhibit 45:** Frequency of jewelry purchase, 2021 vs. 2014

Frequency of Jewelry Purchase: 2021 vs. 2014 Survey (by Total Jewelry Purchaser)



Source: AlphaWise, Morgan Stanley Research

# Implications for luxury retail landlords and property management

Luxury malls in mainland China are mostly operated by HK property companies, except MixC, which is owned and operated by CR Land. We highlight two names with the highest exposure to luxury retail malls in China: Hang Lung Properties (0101.HK, OW, covered by Praveen Choudhary) and China Resources Mixc Lifestyle Services (1209.HK, OW, covered by Chloe Liu).

**Reiterate OW on Hang Lung Properties (0101.HK):** HLP owns and operates luxury shopping malls in Shanghai and five tier 2 cities in China. Among HK property names in our coverage universe, HLP has the highest exposure to retail rental income (39% of GAV) in China, and is set to benefit the most from the discretionary retail sales boom.

HLP generates more than 65% of its rental revenue from China. Within its China rental portfolio, 86% comes from luxury malls while 14% from lifestyle malls, 64% from Shanghai and 36% from tier 2 cities. As shown in [Exhibit 46](#), luxury malls in Shanghai, Shenyang

and Wuxi outperformed lifestyle malls by growing retail sales by 65-190% YoY in 1H21 (or double-digit growth vs. the high base in 2H20). The growth in retail sales translates into retail income growth via the collection of turnover rent or positive rental reversion for HLP. Luxury mall rental income grew 46% YoY in 1H21, compared to 3% for lifestyle malls.

We are also positive on rising rental income from tier 2 malls, which have been adding luxury content. Operating leverage should drive sustainable operating margin expansion. We estimate the EBIT margin for tier 2 cities' malls was just 50% in 2020, which is much lower than 90% for the two malls in Shanghai.

The stock is trading at 50% discount to NAV (1 SD below LT average) and a 4.5% 2021e dividend yield. The company raised interim DPS in 1H21, the first time in 11 years as a result of strong China rental growth.

**Exhibit 46:** HLP's mall retail sales and income performance in 1H21

City	Type	Malls	Retail sales YoY			Retail income YoY (in RMB)			
			1H20	2020	1H21	1H20	2H20	2020	1H21
Shanghai	Luxury	Grand Gateway 66	+7%	+42%	+116%	+15%	+16%	+15%	+25%
Shanghai	Luxury	Plaza 66	+17%	+60%	+101%	+9%	+57%	+34%	+56%
Shenyang	Lifestyle	Palace 66	-34%	-15%	+51%	-11%	-9%	-10%	+6%
Shenyang	Luxury	Forum 66	-14%	+9%	+65%	-14%	+2%	-6%	+19%
Jinan	Lifestyle	Parc 66	-34%	-18%	+48%	-6%	-9%	-8%	+1%
Wuxi	Luxury	Center 66	+13%	+72%	+190%	+6%	+52%	+30%	+71%
Tianjin	Lifestyle	Riverside 66	-40%	-23%	+79%	-14%	-5%	-10%	+2%
Dalian	Luxury*	Olympia 66	-27%	-18%	+80%	-9%	-12%	-11%	+0%

\*Olympia 66 is undergoing a transformation into a luxury mall

Source: Company data, Morgan Stanley Research

**Exhibit 47:** HLP's tenant mix as of Jun-21

City	Type	Malls	Jewelry & Others as % of GFA	Fashion & accessories as % of GFA
Shanghai	Luxury	Grand Gateway 66	19%	47%
Shanghai	Luxury	Plaza 66	14%	66%
Shenyang	Lifestyle	Palace 66	18%	46%
Shenyang	Luxury	Forum 66	33%	21%
Jinan	Lifestyle	Parc 66	22%	39%
Wuxi	Luxury	Center 66	25%	26%
Tianjin	Lifestyle	Riverside 66	26%	31%
Dalian	Luxury*	Olympia 66	28%	22%

Source: Company data, Morgan Stanley Research.

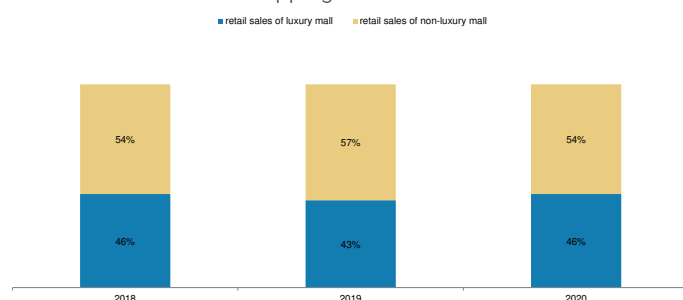
**Reiterate OW on CR Mixc (1209.HK):** CR Mixc is a shopping mall operator in China (it is a subsidiary of CR Land, the shopping mall owner), and is ranked in the top five in China for number of shopping malls in operation, and first for luxury malls. At end 2020, CR Mixc had 62 shopping malls under management, of which eight were luxury malls (Shenzhen Mixc, Shenzhen Bay Mixc, Hangzhou Mixc, Shenyang Mixc, Nanning Mixc, Tianjin Mixc, Xiamen Mixc, Chongqing Mixc), contributing 46% of CR Land's total retail sales in 2020, up from 43% in 2019.

Luxury malls have outperformed non-luxury malls since 1H20, with retail sales quickly rebounding. In 1H21, luxury mall retail sales increased by 89% y-y, including: Shenzhen Bay Mixc up 225% y-y, Chongqing Mixc up 110% y-y, Hangzhou Mixc up 108% y-y, and Tianjin Mixc up 105% y-y.

Most of CR Mixc's malls are in prime locations in tier 1 and tier 2 cities, with consistently strong operational performance; annual rental income and retail sales growth is usually 25-30%, and same-store sales growth has been as high as 10-15% over the past few years. Besides charging a basic property management fee, CR Mixc can charge (depending on the property management contract) a commercial operational services fee, at 4-5% of rental + 8-10% of EBITDA, and, given most of its rentals are linked with retail sales, CR Mixc can enjoy periods of rising retail sales. We forecast 30% annual growth in shopping mall revenue through 2023, with 104 malls in operation in 2023, up from 62 in 2020.

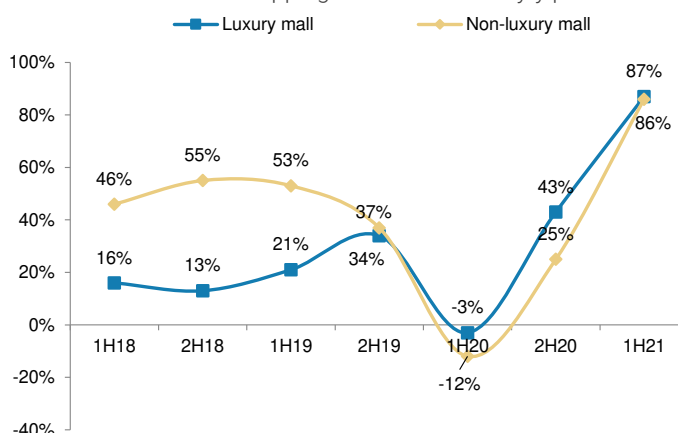
CR Mixc is one of our top picks in China's property management sector, given its strong parent developer with an SOE background, solid earnings growth (52% earnings CAGR in 2020-23) and stable gross margin outlook.

**Exhibit 48:** CR Land: Shopping mall retail sales breakdown



Source: CR Land, Morgan Stanley Research.

**Exhibit 49:** CR Land: shopping malls retail sales y-y performance



Source: CR Land, Morgan Stanley Research.

**Exhibit 50:** Major luxury malls in major tier 1&2 cities

City	一二线城市代表性轻奢商场	Major luxury malls in major tier 1&2 cities
Beijing	北京SKP、北京国贸商场、北京金融街购物中心、北京王府中环、老佛爷百货、北京银泰INO1、北京银泰IN88、北京太古里	Beijing SKP, China World Mall, Beijing Seasons Place, Beijing WF Central, Galeries Lafayette, Beijing Yintai Centre IN01, Beijing Yintai Centre IN88, Beijing Taikoo Li
Shanghai	恒隆广场、上海国金中心、港汇恒隆、环贸IAP M、尚嘉中心	Shanghai Hang Lung Plaza, Shanghai IFC, Shanghai Grand Gateway 66, Shanghai ICC, L'Avenue
Chengdu	成都太古里、成都IFS、成都仁恒置地广场	Chengdu Taikoo Li, Chengdu IFS, Chengdu Yanlord Land
Chongqing	重庆万象城、重庆星光68、重庆IFS、重庆WFC、重庆时代广场	Chongqing Mixc, Chongqing Starlight 68, Chongqing IFS, Chongqing WFC, Chongqing Times Square
Hangzhou	杭州大厦、杭州万象城、湖滨银泰in77A座、恒隆广场（在建）、SKP（在建）	Hangzhou Tower, Hangzhou Mixc, Hubin Yintai IN77A, Hang Lung Plaza (under construction), SKP (under construction)
Guangzhou	广州太古汇、丽柏广场	Guangzhou Taikoo Hui, La Perle Square
Shenzhen	深圳万象城、深圳湾万象城	Shenzhen Mixc, Shenzhen Bay Mixc

Source: Morgan Stanley Research.

# Financials - China Jewelry

**Exhibit 51:** Chow Tai Fook financial summary

HK\$'mn; YE March	2021	2022E	2023E	2024E	HK\$'mn; YE March	2021	2022E	2023E	2024E
<b>Income Statement</b>					<b>Cash Flow Statement</b>				
Revenue	70,164	83,854	96,665	108,653	Profit after tax	6,176	7,136	8,926	10,136
Cost of Goods Sold	(50,089)	(60,727)	(69,277)	(77,871)	Depreciation & Amortization	1,086	1,195	1,277	1,361
<b>Gross Profit</b>	<b>20,075</b>	<b>23,127</b>	<b>27,388</b>	<b>30,782</b>	Other Non-Cash Items	2,915	219	254	266
Selling and distribution expenses	(8,635)	(10,062)	(11,600)	(12,495)	Change in Net Working Capital	300	(7,011)	(5,574)	(5,524)
General and administrative expenses	(3,214)	(3,303)	(3,605)	(4,499)	<b>Operating Cash Flow</b>	<b>10,476</b>	<b>1,539</b>	<b>4,883</b>	<b>6,238</b>
<b>Operating Income - b/f Other Inc/Exp</b>	<b>8,226</b>	<b>9,762</b>	<b>12,183</b>	<b>13,788</b>	Capital Expenditure	(839)	(856)	(873)	(891)
Other Income (Expense) - Net	463	167	216	268	Other	147	0	0	0
<b>EBIT</b>	<b>8,689</b>	<b>9,928</b>	<b>12,399</b>	<b>14,056</b>	<b>Net Cash Used in Investing Activities</b>	<b>(693)</b>	<b>(856)</b>	<b>(873)</b>	<b>(891)</b>
Net Interest Income (Expense)	(295)	(219)	(254)	(266)	Loans Borrowed/ Repaid	3,344	0	0	0
<b>Income Before Tax</b>	<b>8,395</b>	<b>9,709</b>	<b>12,144</b>	<b>13,790</b>	Share Repurchase/ Issue	(337)	0	0	0
Tax	(2,219)	(2,573)	(3,218)	(3,654)	Dividends - Minoritry & Ordinary	(1,809)	0	0	0
Minority Interest	(150)	(173)	(216)	(246)	Other	(12,385)	(4,219)	(5,129)	(6,362)
<b>Net Income</b>	<b>6,026</b>	<b>6,963</b>	<b>8,710</b>	<b>9,890</b>	<b>Net Cash Flow from Financing</b>	<b>(11,188)</b>	<b>(4,219)</b>	<b>(5,129)</b>	<b>(6,362)</b>
Shares Outstanding (mn)	10,000	10,000	10,000	10,000	<b>Change in Cash</b>	<b>(1,404)</b>	<b>(3,536)</b>	<b>(1,119)</b>	<b>(1,015)</b>
<b>MW EPS</b>	<b>0.60</b>	<b>0.70</b>	<b>0.87</b>	<b>0.99</b>	Effect of FX	217	0	0	0
Total dividend payout ratio	66.4%	70.0%	70.0%	70.0%	<b>Prior Yr Balance</b>	<b>7,219</b>	<b>6,032</b>	<b>2,496</b>	<b>1,377</b>
Effective Tax Rate	26.4%	26.5%	26.5%	26.5%	<b>Ending Balance</b>	<b>6,032</b>	<b>2,496</b>	<b>1,377</b>	<b>362</b>
<b>Total POS (# of stores)</b>	<b>4,597</b>	<b>5,271</b>	<b>5,666</b>	<b>6,166</b>					
Mainland China	4445	5125	5525	6025					
HK, Macau and Others	152	146	141	141					
<b>SSSG (%)</b>									
Mainland China	32%	7%	5%	7%					
HK, Macau and Others	-39%	-41%	35%	25%					
HK\$'mn; YE March	2021	2022E	2023E	2024E	HK\$'mn; YE March	2021	2022E	2023E	2024E
<b>Balance Sheet</b>					<b>Ratio Analysis</b>				
Cash & Cash Equivalent	6,032	2,496	1,377	362	<b>YoY Change</b>				
Trade and Other Receivables	6,189	7,360	8,484	9,535	Revenue	23.6%	19.5%	15.3%	12.4%
Inventories	43,011	46,585	51,246	57,603	Gross Profit	24.7%	15.2%	18.4%	12.4%
Other Current Assets	10	10	10	10	Operating Profit (B/f Other Inc/Exp)	81.2%	18.7%	24.8%	13.2%
<b>Total Current Assets</b>	<b>55,243</b>	<b>56,452</b>	<b>61,117</b>	<b>67,511</b>	Operating Income	85.4%	14.3%	24.9%	13.4%
PP&E	4,615	4,338	3,995	3,586	EBITDA	70.9%	13.8%	22.9%	12.7%
Construction-In-Progress	158	108	59	9	Net Income	107.7%	15.5%	25.1%	13.6%
Intangible assets and goodwill	24	24	24	24	<b>Margins</b>				
Other Long Term Assets	4,269	4,257	4,245	4,233	Gross Margin	28.6%	27.6%	28.3%	28.3%
<b>Total Non-current Assets</b>	<b>9,065</b>	<b>8,727</b>	<b>8,323</b>	<b>7,852</b>	Opex/ Sales	16.9%	15.9%	15.7%	15.6%
<b>Total Assets</b>	<b>64,308</b>	<b>65,178</b>	<b>69,440</b>	<b>75,363</b>	Operating Margin (B/f Other Inc/ Exp)	11.7%	11.6%	12.6%	12.7%
Short Term Loans	10,344	10,344	10,344	10,344	Operating/EBIT Margin	12.4%	11.8%	12.8%	12.9%
Trade and Other Payables	17,962	15,696	15,906	17,789	EBITDA Margin	13.9%	13.3%	14.1%	14.2%
Other Current Liabilities	836	836	836	836	Net Margin	8.6%	8.3%	9.0%	9.1%
<b>Total Current Liabilities</b>	<b>29,142</b>	<b>26,876</b>	<b>27,086</b>	<b>28,970</b>	<b>Returns</b>				
Long Term Debt	1,799	1,799	1,799	1,799	ROE	20%	21%	23%	24%
Other Long Term Liabilities	1,800	1,800	1,800	1,800	ROA	9%	11%	13%	13%
<b>Total Non-current Liabilities</b>	<b>3,598</b>	<b>3,598</b>	<b>3,598</b>	<b>3,598</b>	<b>Efficiency</b>				
<b>Total Liabilities</b>	<b>32,741</b>	<b>30,474</b>	<b>30,685</b>	<b>32,568</b>	Day's Receivables - EOP	30	32	32	32
Share capital	10,000	10,000	10,000	10,000	Day's Inventory - EOP	312	280	270	270
Reserves	20,767	23,731	27,566	31,359	Day's Payables - EOP	108	90	80	80
Minority Interest	801	973	1,190	1,436	<b>Gearing</b>				
<b>Total Stockholders' Equity</b>	<b>31,568</b>	<b>34,704</b>	<b>38,756</b>	<b>42,795</b>	Current Ratio	1.90	2.10	2.26	2.33
<b>Total Liabilities &amp; SE</b>	<b>64,308</b>	<b>65,178</b>	<b>69,440</b>	<b>75,363</b>	Net Debt to Equity	19%	28%	28%	28%

Source: Company data, Morgan Stanley Research (E) estimates

## Exhibit 52: Chow Tai Seng financial summary

Rmb'mn; YE December	2020	2021E	2022E	2023E	Rmb'mn; YE December	2020	2021E	2022E	2023E
<b>Income Statement</b>					<b>Cash Flow Statement</b>				
Revenue	5,084	6,565	7,729	8,891	Profit after tax	1,013	1,315	1,577	1,819
Cost of Goods Sold	(2,998)	(3,889)	(4,568)	(5,241)	Depreciation & Amortization	13	26	33	40
<b>Gross Profit</b>	<b>2,086</b>	<b>2,676</b>	<b>3,161</b>	<b>3,650</b>	Other Non-Cash Items	57	0	(0)	0
Business Tax	(69)	(89)	(105)	(121)	Change in Net Working Capital	278	(725)	(490)	(486)
Selling expenses	(668)	(788)	(889)	(1,022)	<b>Operating Cash Flow</b>	<b>1,361</b>	<b>616</b>	<b>1,120</b>	<b>1,373</b>
General & admin expenses	(111)	(164)	(193)	(222)	Capital Expenditure	(137)	(137)	(137)	(137)
<b>Operating Income - b/f Other Inc/Exp</b>	<b>1,237</b>	<b>1,634</b>	<b>1,974</b>	<b>2,284</b>	Other	(501)	278	0	0
Other Income (Expense) - Net	63	60	57	55	<b>Net Cash Used in Investing Activities</b>	<b>(638)</b>	<b>141</b>	<b>(137)</b>	<b>(137)</b>
<b>Operating Income</b>	<b>1,300</b>	<b>1,694</b>	<b>2,031</b>	<b>2,339</b>	Loans Borrowed/ Repaid	0	0	0	0
Net Interest Income (Expense)	23	19	25	32	Share Repurchase/ Issue	0	0	0	0
<b>Income Before Tax</b>	<b>1,324</b>	<b>1,713</b>	<b>2,056</b>	<b>2,371</b>	Dividends - Minority & Ordinary	(336)	(438)	(569)	(683)
Provision for Income Tax	(310)	(399)	(478)	(552)	Other	(0)	0	0	0
Minority Interest	(0)	0	0	0	<b>Net Cash Flow from Financing</b>	<b>(336)</b>	<b>(438)</b>	<b>(569)</b>	<b>(683)</b>
<b>Net Income</b>	<b>1,013</b>	<b>1,315</b>	<b>1,577</b>	<b>1,819</b>	<b>Change in Cash</b>	<b>387</b>	<b>318</b>	<b>414</b>	<b>554</b>
Shares Outstanding (mn)	1,086	1,086	1,086	1,086	Effect of FX	(0)	0	0	0
<b>MW EPS</b>	<b>0.93</b>	<b>1.21</b>	<b>1.45</b>	<b>1.68</b>	<b>Prior Yr Balance</b>	<b>1,294</b>	<b>1,680</b>	<b>1,998</b>	<b>2,412</b>
Payout Ratio	43.3%	43.3%	43.3%	43.3%	<b>Ending Balance</b>	<b>1,680</b>	<b>1,998</b>	<b>2,412</b>	<b>2,966</b>
Effective Tax Rate	23.3%	23.3%	23.3%	23.3%					
<b>Total POS (# of stores)</b>	<b>3,375</b>	<b>4,011</b>	<b>4,189</b>	<b>4,439</b>					
Self-operated	302	278	249	249					
Franchise	3073	3733	3940	4190					
Rmb'mn; YE December	2020	2021E	2022E	2023E	Rmb'mn; YE December	2020	2021E	2022E	2023E
<b>Balance Sheet</b>					<b>Ratio Analysis</b>				
Cash & Cash Equivalent	1,680	1,998	2,412	2,966	<b>YoY Change</b>				
Trade and Other Receivables	157	163	192	221	Revenue	-6.5%	29.1%	17.7%	15.0%
Inventories	2,391	3,235	3,801	4,361	Gross Profit	6.6%	28.3%	18.1%	15.5%
Other Current Assets	530	542	547	551	Operating Profit (B/f Other Inc/Exp)	4.9%	32.1%	20.8%	15.7%
<b>Total Current Assets</b>	<b>4,759</b>	<b>5,939</b>	<b>6,952</b>	<b>8,099</b>	Operating Income	0.1%	30.3%	19.9%	15.1%
PP&E	23	70	112	149	EBITDA	-0.5%	30.9%	20.0%	15.3%
Construction-In-Progress	305	27	27	27	Net Income	2.2%	29.7%	20.0%	15.3%
Intangible assets and goodwill	427	491	553	613	<b>Margins</b>				
Other Long Term Assets	1,142	1,142	1,142	1,142	Gross Margin	41.0%	40.8%	40.9%	41.0%
<b>Total Non-current Assets</b>	<b>1,897</b>	<b>1,731</b>	<b>1,834</b>	<b>1,931</b>	Opex/ Sales	15.3%	14.5%	14.0%	14.0%
<b>Total Assets</b>	<b>6,656</b>	<b>7,669</b>	<b>8,786</b>	<b>10,030</b>	Operating Margin (B/f Other Inc/ Exp)	24.3%	24.9%	25.5%	25.7%
Short Term Loans	0	0	0	0	Operating/EBIT Margin	25.6%	25.8%	26.3%	26.3%
Trade and Other Payables	423	507	595	683	EBITDA Margin	25.8%	26.2%	26.7%	26.8%
Advance collection	48	105	124	142	Net Margin	19.9%	20.0%	20.4%	20.5%
Other Current Liabilities	769	765	766	767	<b>Returns</b>				
<b>Total Current Liabilities</b>	<b>1,239</b>	<b>1,377</b>	<b>1,485</b>	<b>1,593</b>	ROE	19%	21%	22%	22%
Long Term Debt	0	0	0	0	ROA	15%	17%	18%	18%
Other Long Term Liabilities	26	26	26	26	<b>Efficiency</b>				
<b>Total Non-current Liabilities</b>	<b>26</b>	<b>26</b>	<b>26</b>	<b>26</b>	Day's Receivables - EOP	10	10	10	10
<b>Total Liabilities</b>	<b>1,266</b>	<b>1,403</b>	<b>1,511</b>	<b>1,619</b>	Day's Inventory - EOP	304	304	304	304
Common Stock	731	731	731	731	Day's Payables - EOP	53	53	53	53
Reserves	1,932	1,932	1,932	1,932	<b>Gearing</b>				
Retained Earnings/ (Accumulated Deficit)	2,723	3,599	4,607	5,744	Current Ratio	3.84	4.31	4.68	5.08
Minority Interest	5	4	4	4	Net Debt to Equity	-28%	-29%	-31%	-33%
<b>Total Stockholders' Equity</b>	<b>5,390</b>	<b>6,266</b>	<b>7,274</b>	<b>8,411</b>					
<b>Total Liabilities &amp; SE</b>	<b>6,656</b>	<b>7,669</b>	<b>8,786</b>	<b>10,030</b>					

Source: Company data, Morgan Stanley Research (E) estimates

## Exhibit 53: Lao Feng Xiang financial summary

Rmb'mn; YE December	2020	2021E	2022E	2023E	Rmb'mn; YE December	2020	2021E	2022E	2023E
<b>Income Statement</b>					<b>Cash Flow Statement</b>				
<b>Revenue</b>	<b>51,722</b>	<b>57,521</b>	<b>62,401</b>	<b>69,484</b>	Profit after tax	2,072	2,277	2,448	2,867
Jewelry	38,079	42,973	47,132	53,457	Depreciation & Amortization	45	48	50	52
Gold trading	13,015	14,317	15,033	15,784	Other Non-Cash Items	305	314	314	314
Trading	136	143	146	149	Change in Net Working Capital	(74)	(1,303)	(1,046)	(1,503)
Crafts	84	88	91	93	<b>Operating Cash Flow</b>	<b>2,348</b>	<b>1,336</b>	<b>1,766</b>	<b>1,730</b>
Pencil and others	270	310	326	332	Capital Expenditure	(37)	(37)	(37)	(37)
Others	138	550	826	1,239	Other	169	0	0	0
Cost of Goods Sold	(47,489)	(53,090)	(57,519)	(63,884)	<b>Net Cash Used in Investing Activities</b>	<b>133</b>	<b>(37)</b>	<b>(37)</b>	<b>(37)</b>
<b>Gross Profit</b>	<b>4,233</b>	<b>4,431</b>	<b>4,882</b>	<b>5,600</b>	Loans Borrowed/ Repaid	86	0	0	0
Business Tax	(142)	(158)	(171)	(190)	Share Repurchase/ Issue	25	0	0	0
Selling expenses	(688)	(748)	(624)	(695)	Dividends - Nonotriy & Ordinary	(1,221)	(654)	(876)	(941)
General & admin expenses	(447)	(497)	(539)	(601)	Other	(96)	(314)	(314)	(314)
<b>Operating Income - b/f Other Inc/Exp</b>	<b>2,956</b>	<b>3,029</b>	<b>3,548</b>	<b>4,114</b>	<b>Net Cash Flow from Financing</b>	<b>(1,207)</b>	<b>(968)</b>	<b>(1,190)</b>	<b>(1,256)</b>
Other Income (Expense) - Net	128	333	42	41	<b>Change in Cash</b>	<b>1,273</b>	<b>331</b>	<b>539</b>	<b>438</b>
<b>Operating Income</b>	<b>3,084</b>	<b>3,362</b>	<b>3,589</b>	<b>4,155</b>	Effect of FX	11	0	0	0
Net Interest Income (Expense)	(289)	(260)	(255)	(249)	<b>Prior Yr Balance</b>	<b>4,310</b>	<b>5,594</b>	<b>5,925</b>	<b>6,465</b>
<b>Income Before Tax</b>	<b>2,794</b>	<b>3,102</b>	<b>3,334</b>	<b>3,906</b>	<b>Ending Balance</b>	<b>5,594</b>	<b>5,925</b>	<b>6,465</b>	<b>6,903</b>
Provision for Income Tax	(722)	(825)	(886)	(1,038)					
Minority Interest	(486)	(525)	(565)	(661)					
<b>Net Income</b>	<b>1,586</b>	<b>1,752</b>	<b>1,883</b>	<b>2,206</b>					
Shares Outstanding (mn)	523	523	523	523					
<b>MW EPS</b>	<b>3.03</b>	<b>3.35</b>	<b>3.60</b>	<b>4.22</b>					
Payout Ratio	50.0%	50.0%	50.0%	50.0%					
Effective Tax Rate	26.6%	26.6%	26.6%	26.6%					
<b>Total POS (# of stores)</b>	<b>4450</b>	<b>4850</b>	<b>5150</b>	<b>5450</b>					
Franchise	4270	4670	4970	5270					
Self-operate	180	180	180	180					
Rmb'mn; YE December	2020	2021E	2022E	2023E	Rmb'mn; YE December	2020	2021E	2022E	2023E
<b>Balance Sheet</b>					<b>Ratio Analysis</b>				
Cash & Cash Equivalent	5,605	5,936	6,475	6,914	<b>YoY Change</b>				
Trade and Other Receivables	175	323	351	390	Revenue	4.2%	11.2%	8.5%	11.3%
Inventories	11,882	13,017	14,103	15,663	Gross Profit	0.7%	4.7%	10.2%	14.7%
Other Current Assets	1,090	1,087	1,092	1,098	Operating Profit (B/f Other Inc/Exp)	6.5%	2.4%	17.1%	16.0%
<b>Total Current Assets</b>	<b>18,752</b>	<b>20,363</b>	<b>22,021</b>	<b>24,066</b>	Operating Income	12.3%	9.0%	6.8%	15.7%
PP&E	359	363	355	344	EBITDA	12.0%	9.0%	6.8%	15.6%
Construction-In-Progress	18	7	7	7	Net Income	12.6%	10.5%	7.5%	17.1%
Intangible assets and goodwill	89	84	79	75	<b>Margins</b>				
Other Long Term Assets	345	345	345	345	Gross Margin	8.2%	7.7%	7.8%	8.1%
<b>Total Non-current Assets</b>	<b>812</b>	<b>800</b>	<b>787</b>	<b>771</b>	Opex/ Sales	2.2%	2.2%	1.9%	1.9%
<b>Total Assets</b>	<b>19,563</b>	<b>21,164</b>	<b>22,807</b>	<b>24,837</b>	Operating Margin (B/f Other Inc/ Exp)	5.7%	5.3%	5.7%	5.9%
Short Term Loans	6,251	6,251	6,251	6,251	Operating/EBIT Margin	6.0%	5.8%	5.8%	6.0%
Trade and Other Payables	480	561	608	675	EBITDA Margin	6.0%	5.9%	5.8%	6.1%
Advance collection	5	76	83	92	Net Margin	3.1%	3.0%	3.0%	3.2%
Other Current Liabilities	2,434	2,259	2,278	2,305	<b>Returns</b>				
<b>Total Current Liabilities</b>	<b>9,170</b>	<b>9,147</b>	<b>9,219</b>	<b>9,322</b>	ROE	20%	19%	19%	19%
Long Term Debt	900	900	900	900	ROA	8%	8%	8%	9%
Other Long Term Liabilities	79	79	79	79	<b>Efficiency</b>				
<b>Total Non-current Liabilities</b>	<b>979</b>	<b>979</b>	<b>979</b>	<b>979</b>	Day's Receivables - EOP	2	2	2	2
<b>Total Liabilities</b>	<b>10,149</b>	<b>10,126</b>	<b>10,198</b>	<b>10,302</b>	Day's Inventory - EOP	89	89	89	89
Common Stock	523	523	523	523	Day's Payables - EOP	4	4	4	4
Reserves	805	805	805	805	<b>Gearing</b>				
Retained Earnings/ (Accumulated Deficit)	6,637	7,735	8,742	10,006	Current Ratio	2.04	2.23	2.39	2.58
Minority Interest	1,450	1,975	2,540	3,201	Net Debt to Equity	17%	11%	6%	2%
<b>Total Stockholders' Equity</b>	<b>9,414</b>	<b>11,038</b>	<b>12,610</b>	<b>14,535</b>					
<b>Total Liabilities &amp; SE</b>	<b>19,563</b>	<b>21,164</b>	<b>22,807</b>	<b>24,837</b>					

Source: Company data, Morgan Stanley Research (E) estimates

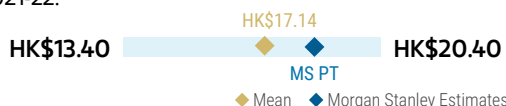
## Risk Reward – Chow Tai Fook Jewellery Group Ltd (1929.HK)

More fashion jewelry and asset-light model to drive growth acceleration

### PRICE TARGET HK\$18.50

We use a P/E-based valuation, consistent with the rest of our consumer discretionary coverage. Our price target is based on 21x forward 12 months P/E, close to its historical peak. We see CTF as key beneficiary of structural growth of China's jewelry market. Its wide product range supports more sustainable growth than peers. HK-China border reopening is set to support growth and valuation in 2021-22.

#### Consensus Price Target Distribution



Source: Thomson Reuters, Morgan Stanley Research

### RISK REWARD CHART



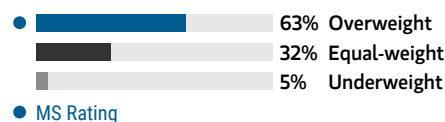
Key: — Historical Stock Performance ● Current Stock Price ◆ Price Target

Source: Thomson Reuters, Morgan Stanley Research

### OVERWEIGHT THESIS

- We are constructive on the structural growth of the jewelry market in China, consumption upgrade and premiumization trends.
- Domestic brands to benefit more than international brands on Chinese consumers' rising preference for local products and design.
- Switch of business focus to more affordable luxury offerings and growing franchise store exposure should drive market share gain.
- Key beneficiary of potential HK-China border reopening in 2021-22e.

#### Consensus Rating Distribution



Source: Thomson Reuters, Morgan Stanley Research

#### Risk Reward Themes

Pricing Power: *Positive*  
Self-help: *Positive*  
Market Share: *Positive*

View descriptions of Risk Rewards Themes [here](#)

#### BULL CASE

HK\$26.00

25x 12-month forward P/E

**Rapid middle class expansion and disposable income growth:** We assume CTF's FY22/23/24e EPS are 10%/20%/25% higher than our base case assumptions. This implies 27%, 36% and 18% yoy EPS growth in FY22e, FY23e and FY24e. As market sentiment is positive under this scenario, we assign a 25x target P/E to our bull case (3SD above average since 2016).

#### BASE CASE

HK\$18.50

21x 12-month forward PE

**Rising middle class supports jewelry market growth:** We expect CTF EPS to grow 16%, 25% and 14% in FY22, FY23 and FY24.

#### BEAR CASE

HK\$9.00

13x 12-month forward P/E

**Economic growth slowdown together with less extravagant spending trend:** We assume CTF's FY22/23/24e EPS are 10%/20%/25% lower than our base case assumptions. This implies 4%, 11% and 6% yoy EPS growth in FY22e, FY23e and FY24e. As market sentiment is negative under this scenario, we assign a 13x target P/E to our bear case (1SD below average since 2016).

## Risk Reward – Chow Tai Fook Jewellery Group Ltd (1929.HK)

### KEY EARNINGS INPUTS

Drivers	2021	2022e	2023e	2024e
SSSG - China (%)	31.9	7.0	5.0	7.0
SSSG - HK (%)	(41.3)	35.0	25.0	15.0

### CATALYST CALENDAR

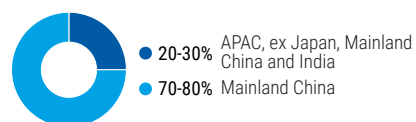
Date	Event
27 Sep 2021	Chow Tai Fook Jewellery Group Virtual Investor Day 2021

Source: Thomson Reuters, Morgan Stanley

### INVESTMENT DRIVERS

- Among Chinese consumers, continuous consumption upgrade and premiumization
- Rising affordable luxury market
- Market share gain from stores opening and same-store-sales growth in China
- HK-China border reopening

### GLOBAL REVENUE EXPOSURE



Source: Morgan Stanley Research Estimate  
View explanation of regional hierarchies [here](#)

### MS ALPHA MODELS

1/5  
MOST

3 Month  
Horizon

Source: Thomson Reuters, FactSet, Morgan Stanley Research; 1 is the highest favored Quintile and 5 is the least favored Quintile

### RISKS TO PT/RATING

#### RISKS TO UPSIDE

- Faster-than-expected network expansion and same-store sales growth in China/HK
- Gold price rally to drive margin expansion
- Strong sales growth at online/omnichannels

#### RISKS TO DOWNSIDE

- Macro slowdown and decline in disposable income
- Intense competition in affordable luxury given low entry barrier
- Luxury consumption returns to overseas when international travel normalizes after COVID-19

### OWNERSHIP POSITIONING

Inst. Owners, % Active 65.2%

Source: Thomson Reuters, Morgan Stanley Research

### MS ESTIMATES VS. CONSENSUS

FY Mar 2022e

**Sales / Revenue** (HK\$, mn) 81,424 **83,854** 95,326  
84,227

**Net income** (HK\$, mn) 6,287 **6,963** 8,886  
6,872

**EPS** (HK\$) 0.60 **0.70** 0.89  
0.68

◆ Mean ◆ Morgan Stanley Estimates

Source: Thomson Reuters, Morgan Stanley Research



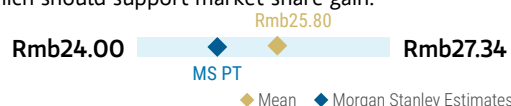
## Risk Reward – Chow Tai Seng Jewellery Co Ltd (002867.SZ)

Affordable luxury to drive growth acceleration and market share gain

### PRICE TARGET Rmb25.00

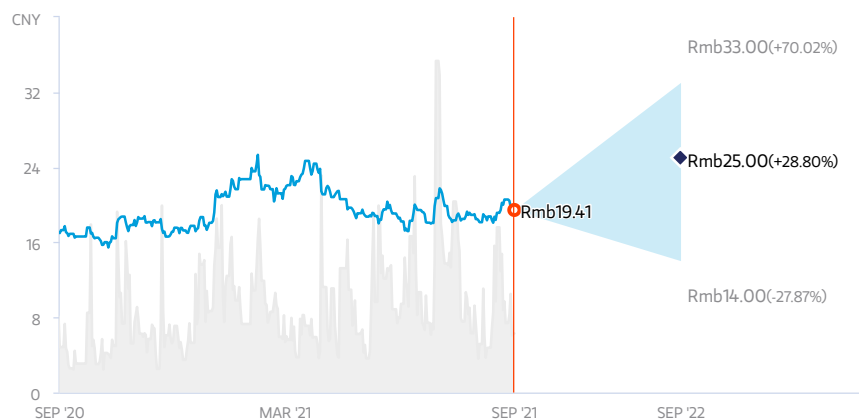
We use a P/E-based valuation, consistent with the rest of our consumer discretionary coverage. Our price target is based on a 2022P/E of 17x. Our target P/E is slightly below +1SD average since its listing in 2017. We are constructive on the jewelry market given consumption upgrade and premiumization trends during 2020-30. CTS is focused on affordable luxury and online channels, which should support market share gain.

#### Consensus Price Target Distribution



Source: Thomson Reuters, Morgan Stanley Research

### RISK REWARD CHART



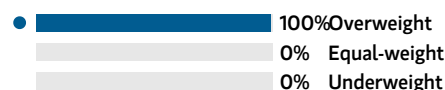
Key: — Historical Stock Performance ● Current Stock Price ◆ Price Target

Source: Thomson Reuters, Morgan Stanley Research

### OVERWEIGHT THESIS

- We are constructive on the structural growth of the jewelry market in China given consumption upgrade and premiumization trends.
- Domestic brands to benefit more than international brands on Chinese consumers' rising preference for local products and design.
- CTS is one of China's top-five jewelry retailers, with a focus in affordable luxury, lower-tier cities and online channels, which should drive better-than-market growth.
- Asset-light model drives higher-than-peer net margins.

#### Consensus Rating Distribution



● MS Rating

Source: Thomson Reuters, Morgan Stanley Research

#### Risk Reward Themes

Pricing Power: *Positive*  
Market Share: *Positive*

View descriptions of Risk Rewards Themes [here](#)

#### BULL CASE

Rmb33.00

19x 2022e bull PE

**Rapid middle class expansion and fast growing fashion jewelry demand:**We assume CTS's 2021/22e EPS are 10%/20% higher than our base case assumptions. This implies 43% and 31% yoy EPS growth in 2021e and 2022e. As market sentiment is positive under this scenario, we assign a 19x target P/E to our bull case (1.5SD above average since 2018).

#### BASE CASE

Rmb25.00

17x 2022 base PE

**Rising middle class supports jewelry market growth:** We expect CTS EPS to grow 30% and 20% in 2021 and 2022.

#### BEAR CASE

Rmb14.00

12x 2022e bear PE

**Growth slowdown in lower-tier cities and online sales:**We assume CTS's 2021/22e EPS are 10%/20% lower than our base case assumptions. This implies 17% and 7% yoy EPS growth in 2021e and 2022e. As market sentiment is negative under this scenario, we assign a 12x target P/E to our bear case (1SD below average since 2018).

## Risk Reward – Chow Tai Seng Jewellery Co Ltd (002867.SZ)

### KEY EARNINGS INPUTS

Drivers	2020	2021e	2022e	2023e
Per self-operate store revenue growth (%)	(24.3)	37.7	12.1	8.5
Per franchisee store revenue growth (%)	(21.0)	25.9	12.5	8.6
Gross margin (%)	41.0	40.8	40.9	41.0

### INVESTMENT DRIVERS

- Among Chinese consumers, continuous consumption upgrade and premiumization
- Rising affordable luxury market
- Market share gain from stores opening and same-store sales growth in China
- Margin expansion from brand building and operating leverage

### GLOBAL REVENUE EXPOSURE



● 100% Mainland China

Source: Morgan Stanley Research Estimate  
View explanation of regional hierarchies [here](#)

### RISKS TO PT/RATING

#### RISKS TO UPSIDE

- Faster-than-expected network expansion and same-store sales growth in China
- Overseas network expansion
- Strong ASP growth, hence margin expansion due to strong brand building

#### RISKS TO DOWNSIDE

- Macro slowdown and decline in disposable income
- Intense competition in affordable luxury given low entry barrier
- Luxury consumption returns to overseas when international travel normalizes after covid

### OWNERSHIP POSITIONING

Inst. Owners, % Active 98%

Source: Thomson Reuters, Morgan Stanley Research

### MS ESTIMATES VS. CONSENSUS

FY Dec 2021e

**Sales / Revenue** (Rmb, mn) 5,787 7,478

**Net income** (Rmb, mn) 1,213 1,434

**EPS** (Rmb) 1.11 1.31

◆ Mean ◆ Morgan Stanley Estimates

Source: Thomson Reuters, Morgan Stanley Research

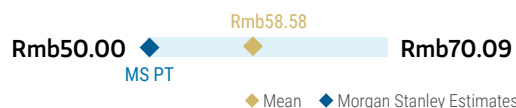
## Risk Reward – Lao Feng Xiang Co Ltd (600612.SS)

Conservative strategy could risk market share loss amid improving macro trends

### PRICE TARGET Rmb50.00

We use a P/E-based valuation, consistent with the rest of our consumer discretionary coverage. Our price target is based on a 2022P/E of 14x. Our target P/E is similar to its average P/E since 2016. We are constructive on the jewelry market given consumption upgrade and premiumization trends during 2020-30. Yet we are concerned that LFX's conservative strategy and traditional high-end focus could translate into market share losses, medium term.

#### Consensus Price Target Distribution



Source: Thomson Reuters, Morgan Stanley Research

### RISK REWARD CHART



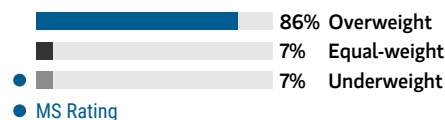
Key: — Historical Stock Performance ● Current Stock Price ◆ Price Target

Source: Thomson Reuters, Morgan Stanley Research

### UNDERWEIGHT THESIS

- We are concerned about the company's conservative strategy, with its focus on traditional high-end jewelry and offline channels. This might risk the loss of market share, as peers are ramping up fashion/affordable luxury and online channels.
- Gross margin for jewelry sales was just ~10%, and net margin was just ~3%, during 2018-20, much lower than peers.
- Risk of declining sales demand and margin pressure when the gold price is expected to decline in 2021-22e. The company has an est. 80% of gold product sales, highest among HK/China jewelry stocks.
- Valuation at 14x is lower than its average P/E since 2016, but appears to be rich given the risk of slowing demand and potential market share loss.

#### Consensus Rating Distribution



Source: Thomson Reuters, Morgan Stanley Research

#### Risk Reward Themes

Disruption: *Negative*  
Market Share: *Negative*

View descriptions of Risk Rewards Themes [here](#)

#### BULL CASE

Rmb82.00

19x 2022e bull case EPS

**Rapid middle class expansion and preference of local jewelry brands:** We assume LFX's 2021/22e EPS are 10%/20% higher than our base case assumptions. This implies 22% and 17% yoy EPS growth in 2021e and 2022e. As market sentiment is positive under this scenario, we assign a 19x target P/E to our bull case.

#### BASE CASE

Rmb50.00

14x 2022e base EPS

**Rising middle class supports jewelry market growth:** We expect LFX EPS to grow 10% and 7% in 2021 and 2022.

#### BEAR CASE

Rmb35.00

12x 2022e bear case EPS

**Less extravagant spending trend and reducing preference on traditional gold jewelry:** We assume LFX's 2021/22e EPS are 10%/20% lower than our base case assumptions. This implies -1% and -4% yoy EPS change in 2021e and 2022e. As market sentiment is negative under this scenario, we assign a 12x target P/E to our bear case.

## Risk Reward – Lao Feng Xiang Co Ltd (600612.SS)

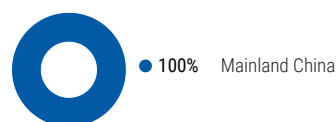
### KEY EARNINGS INPUTS

Drivers	2020	2021e	2022e	2023e
Jewelry revenue per store yoy (%)	(10.2)	8.0	2.0	7.0
Jewelry sales gross margin (%)	10.1	10.0	10.0	10.0

### INVESTMENT DRIVERS

- Among Chinese consumers, continuous consumption upgrade and premiumization
- Stores opening and same-store sales growth in China
- Gold product demand, partly affected by gold price

### GLOBAL REVENUE EXPOSURE



Source: Morgan Stanley Research Estimate  
View explanation of regional hierarchies [here](#)

### MS ALPHA MODELS

1/5  
MOST  
3 Month  
Horizon

Source: Thomson Reuters, FactSet, Morgan Stanley Research; 1 is the highest favored Quintile and 5 is the least favored Quintile

### RISKS TO PT/RATING

#### RISKS TO UPSIDE

- Rising gold demand - LFX has high exposure in gold product sales
- Faster-than-expected network expansion and same-store sales growth in China
- Overseas network expansion

#### RISKS TO DOWNSIDE

- Macro slowdown and decline in disposable income
- Luxury consumption returns to overseas when international travel normalizes after COVID-19
- Market share loss due to intense competition from both domestic and foreign brands

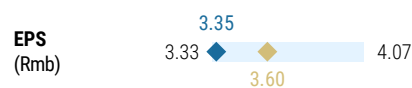
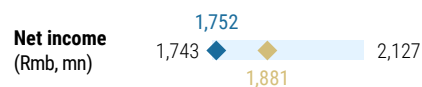
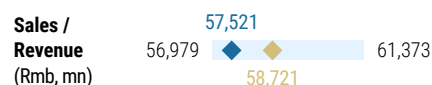
### OWNERSHIP POSITIONING

Inst. Owners, % Active 96.8%

Source: Thomson Reuters, Morgan Stanley Research

### MS ESTIMATES VS. CONSENSUS

FY Dec 2021e



◆ Mean ◆ Morgan Stanley Estimates

Source: Thomson Reuters, Morgan Stanley Research

# Morgan Stanley

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