

## Robust Demand for Green Food

## China F&B

**China Green (904 HK, HK\$7.16)**

**BUY (unchanged)**

### Target price: HK\$10.32 (+44.1%)

**Strong corn exports growth.** China's corn exports rose 55.2% YoY to 3.51m tones in the first five months of 2007 and are expected to reach 5.2m tones (up 40.0% YoY) by the end of 2007, according to China's Customs. In the first five months of 2007, China Green's (CG) corn exports rose more than 50.0% YoY and should account for more than 95.0% of its total vegetable exports in FY04/07F, according to our estimates.

**ASP hike expected.** CG's fully vertically integrated business model (own vegetables and fruit supply) gives it bargaining power to increase prices. In FY04/08F, the company expects its overall ASP to increase 4.0 – 8.0%.

**Capacity expansion.** Its non-fried noodle plant is currently working at full capacity. In the next 12 months, CG plans to add three to six production lines at its facility in Jiangxi province to quadruple its annual output to 132.0m packs, to meet growing demand.

**Gross margin to rebound.** The gross margin should reverse its two-year downtrend as contributions from the high-margin food and beverage segment (gross margin at 42.3% in FY04/06A) are expected to increase to around 46.0% in FY04/07F. We expect CG's gross margins to reach 51.6% in FY04/07F.

**New organic food plan.** CG plans to lease 20,000 mu (1,333.3 hectares) in Tianmen, Hubei province, and use it as an organic cultivation base, producing mainly for Japanese and domestic clients. CG will implement at their base with its first organic seasonal complementary cultivation model and use contemporary ecological principles and advanced technologies to ensure that its products meet organic standards. CG's first organic crops are expected in three years.

**Expanding beverage distribution.** The company currently has 60 beverage distributors in Fujian and Jiangxi. It plans to double the number and extend its network to Zhejiang, Jiangsu, Hunan and Hubei.

**Financials.** Its capex, estimated at around RMB444.0m in FY04/07F and RMB600.0m in FY04/08F, will be spent mainly on the Tianmen organic cultivation base and new production facilities in Jiangxi province. Cash on hand is estimated at over RMB900.0m, sufficient for the company's near-term expansion.

**Valuation.** Benefiting from strong demand for healthy green food and beverages, the company's turnover is expected to grow more than 30.0% annually in the next three years. Given its ROE of 26.9%, second highest among peers, and strong growth prospects, we reiterate our BUY call and target price of HK\$10.32.

**Major risks.** 1) RMB appreciation; 2) execution of capacity and downstream expansion; 3) execution of new product launches and 4) natural disasters.

**Table 1: Financial summary**

Year to	Net profit	EPS	EPS	P/E	P/B	EV/EBITDA	Yield	ROE	ROCE	N. Gearing
Apr	RMBm	HK\$	Δ %	X	X	x	%	%	%	%
05A	183.5	0.275	(8.3)	26.0	5.4	27.2	1.0	25.1	25.1	Cash
06A	271.3	0.373	35.6	19.2	4.6	20.9	1.4	26.9	23.4	Cash
07F	340.9	0.403	7.9	17.8	3.9	15.2	1.5	25.3	21.3	Cash
08F	450.0	0.505	25.4	14.2	3.9	10.3	1.9	28.2	24.4	Cash
09F	570.7	0.640	26.8	11.2	2.8	8.2	2.4	29.2	25.4	Cash

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**Table 2: F&B Peer comparison**

Company	Ticker	Currency	Price	Mkt Cap (US\$m)	Hist. P/E (x)	Fwd Yr. 1 P/E (x)	Fwd Yr. 2 P/E (x)	ROE (%)	FY07 PEG (x)
China Mengniu	2319 HK	HKD	26.95	4,916.3	49.4	39.0	29.8	27.3	1.3
Yili	600887 CH	RMB	31.16	2,113.2	44.5	39.8	33.9	14.1	6.6
Tingyi	322 HK	HKD	9.09	6,498.6	43.7	36.3	29.8	16.7	1.8
Groupe Danone	BN FP	EUR	59.0	41,493.9	23.9	21.5	18.9	24.4	1.8
Uni-President	1216 TT	TWD	33.90	3,360.8	33.4	18.7	17.3	8.0	na
Nissin Food	2897 JP	JPY	4,130	4,265.1	27.4	24.3	23.8	7.3	na
Kirin Brewery	2503 JP	JPY	1,843	14,700.0	32.2	33.9	31.7	5.4	na
<b>Average</b>					<b>36.4</b>	<b>30.5</b>	<b>26.5</b>	<b>17.7</b>	<b>2.9</b>

Source: Bloomberg & SBI E2-Capital