

Competitor supplied poisoned food

China F&B

Fu Ji Catering (1175 HK, HK\$13.50)

BUY (unchanged)

Target price: HK\$19.0 (+40.7)

According to the Chinese media, around 180 employees from Shenzhen's Foxconn (2038, HK25.1, NR) suffered from food poison after eating some vegetables from a Taiwanese restaurant (the third largest supplier, one of the Fu Ji's key competitors).

There are around 13 catering suppliers for Shenzhen's Foxconn. Fu Ji is the largest supplier while the above-mentioned Taiwanese supplier is believed to be around the third largest.

Yesterday, Fu Ji's share price dropped 5.5% to HK\$13.5 against the general uptrend of major China consumption stocks.

We consider this is a good opportunity to accumulate the shares for the following reasons:

- After the event, we expect Foxconn will quicken the process to streamline the number of suppliers and Fu Ji may acquire more orders.
- Fu Ji maintains a high level of safety standard by adopting automatic food processing while some smaller competitors still stick to manual food processing.
- Fu Ji has its own sourcing and processing centers to control the food safety standard.

ASP expected to rebound. In 2Q FY03/07, the company signed some new MNC clients and industrial zone clients with higher ASP. ASP is expected to rebound back to RMB6.0 level as a result. The newly acquired clients are mainly American and European companies based in Songjiang, countryside of Greater Shanghai region. They are willing to pay higher ASP for higher quality food. We estimate the ASP should be around RMB7.0-8.0 per meal for these new westerners.

SIPC lifts margins. Four sourcing and processing centers (SIPC) commenced operations so far this year. Direct sourcing from the farmers is expected to help further stabilize its margins. The recruitment for middle management has come to the final stage that the pressure with increasing staff costs should start to slow down by 2Q FY03/07.

Valuation. The counter is currently trading at attractive 17.8x FY03/07F and 12.5x FY03/08F P/E and a 0.4x PEG while its major competitors like Compass (CPG LN) and Sodexo (SWFP) are trading at 2.4x and 1.6x PEG. We maintain our BUY call because of its attractive valuation and increasing economies of scale.

Table 1: Financial summary

Year to	Net profit	EPS	EPS	P/E	P/B	EV/EBITDA	Yield	ROE	ROCE	N. Gearing
Mar	RMBm	RMB	Δ %	x	X	X	%	%	%	%
04A	82.6	-	-	-	-	-	-	-	-	-
05A	165.4	0.462	-	30.1	6.8	18.7	0.3	38.9	40.7	Cash
06A	251.4	0.488	5.6	28.5	5.0	16.6	1.1	23.7	24.6	Cash
07F	402.1	0.780	59.7	17.8	3.9	11.3	1.7	24.4	25.8	Cash
08F	570.0	1.108	42.1	12.5	3.1	7.2	2.4	27.3	27.2	Cash

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