

Fuji Catering



BUY (unchanged)

Lowering estimates to reflect weaker economy

Review. Top and bottom line increased 77.8% YoY and 27.2% YoY, respectively, to RMB1,387.3m and RMB250.2m in 1H FY03/09A.

- *Catering service* – revenue increased 52.7% YoY to RMB958.7m with operating profit up 41.2% to RMB309.4m. Daily output enlarged to 869,500 sets at end-Sep, up from 810,500 at end-Jun or 657,000 one year before. Operating margin, though squeezed 2.6pcp YoY to 32.3%, improved considerably QoQ in 2Q from 27.8% to 36.3%, thanks to a significant drop in operating expenses.
- *Chinese restaurants* – revenue increased 20.9% YoY to RMB151.7m with operating profit down 11.5% YoY to RMB26.9m. The company has 11 restaurants in Beijing, Shanghai and Suzhou. Four of them were closed for renovation and will re-open in Sep and Nov.
- *Theme restaurants* – revenue was RMB259.5m with RMB56.5m operating profit. With five new stores in 2Q, the total number reached 45 by end-Sep 08. The company served around 3.8m customers in 1H with average spending of RMB37 per head (1Q: 3.5m with RMB35 per head).
- *Convenience food and related business* – revenue dropped 35.0% YoY to RMB17.4m with RMB14.0m operating loss, reversing from RMB1.8m profit one year before. For 2Q, sales were a mere RMB6.0m, 47.8% lower than 1Q. The company explained this division is still in the infancy stage and that they are still in the process of refining this segment's positioning. Contributing to the revenue decline was that four of the total five convenience stores were affected by the re-design and decoration.

Outlook. The 1H results are in line with our previous forecast “*Top line still strong*” (dated 11 Sep). Nevertheless we expect the current economy slowdown to influence the company's operation in multiple aspects:

Bankrupt of manufacturing enterprises – though the company has not yet observed any apparent impact on its sales, the current slowdown in China's economy is nevertheless unfavorable towards the company. Although daily output at end-Sep was 869,500 sets (up 119,000 sets HoH from end-Mar) and ahead of our expectations, we are maintain our previous daily output forecast of 933,500 sets by end-FY03/09F, implying a decrease in the rate of growth to 64,000 sets in the final quarter. We have revised down revenue contribution in this segment by 4.4% in FY3/09F, 9.0% in FY3/10F and 11.4% in FY3/11F respectively.

China Consumer

Tue, 23 Dec 2008

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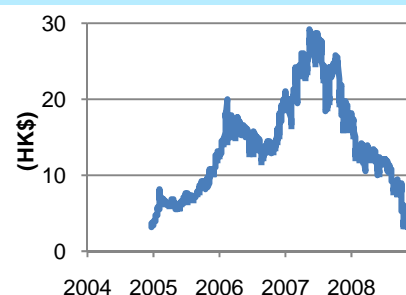
Stock data

Price	HK\$3.40
Target price	HK\$6.90 (+103%)
12 mth range	HK\$2.27-18.37
Market cap.	US\$233.2m
Daily t/o, 3 mth	US\$1.4m
Free float %	47.3%
Ticker	1175.HK/1175 HK

Financial summary

Year to Dec	07A	08A	09F	10F	11F
T/O (HK\$m)	1,199.41	915.62	830.33	413.94	022.9
NP(HK\$m)	348.1	411.0	503.9	569.2	641.7
EPS (HK\$m)	0.689	0.772	0.931	1.052	1.186
EPS Δ %	21.9	12.0	20.6	13.0	12.7
P/E (x)	4.5	4.0	3.3	2.9	2.6
P/B (x)	0.88	0.62	0.54	0.48	0.43
EV/EBITDA (x)	4.2	3.8	2.8	2.4	1.9
Yield (%)	6.1	7.1	7.2	7.8	8.5
ROE (%)	21.5	18.3	17.5	17.3	17.4
ROCE (%)	17.0	13.7	13.8	14.4	16.3
N. Gear. (%)	29.5	47.7	37.0	33.3	23.4

Price Chart



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Contraction of discretionary consumption – we expect consumer will reduce expenditures on outside dining to some extent during the current economic downturn, which should reduce demand at its restaurants. We have essentially left our estimates for the Chinese restaurant segment intact but have revised down revenue contribution from its theme restaurants by 2.2% in FY3/09F, 3.6% in FY3/10F and 6.8% in FY3/11F given the more discretionary nature of the latter line of business.

Convenience food segment unlikely to be major contributor near term – The loss from the convenience food segment was larger than expected. In our view, we think the management is still experimenting with the appropriate food selection mix, and market positioning. We do not have high expectations for the segment as we think it would take more time to scale up. Currently, our estimate is for the segment to breakeven in FY3/12F.

Weak share price due to CB repayment concerns. While Fuji's financial performance remains solid, a key concern of the investment community is its ability to repay the RMB479.8m CB in 2009 and RMB1.5b CB in 2010, especially in light of current tight credit conditions. To preserve cash, management has already indicated that they will temporarily suspend expansion plans at its new facilities in Beijing and Jiading. This should lower capex to RMB700.0m for FY12/09F and RMB400.0m for FY12/10F. In addition, management has already started negotiations with several prospective banks to obtain a credit facility of between RMB500.0-1,000.0m. A final option would be spin-off/dispose its theme restaurant business (Golden Hans) to raise funding to repay the CBs.

Our view on the CB repayment issue. Our view is while we think that the company is unlikely to have any trouble repaying the CB due in 2009, the repayment of its CB in 2010 would stretch its financial resources. Our current estimates suggest that the company will require around RMB1.2b in financing to meet its CB obligations. With respect to obtaining a bank facility, as most of Fuji's assets is plant and equipment, we think it may have difficulties in obtaining a facility in the region of RMB1,000.0m (though smaller loan facilities would still be possible). We are also reserved towards the theme restaurant spin-off/disposal option as we think that should market conditions remain extremely weak, it may not be able to raise sufficient cash. The most effective option for the company to address this issue would be through a combination of scaling down its capex over the next couple of years to preserve cash and simultaneously negotiate for a refinance of its CB. Assuming that China's economy (together with capital markets) would be begin to show signs of recovery by 2010, we think that Fuji should be in a position to navigate this situation.

Maintain BUY call, revise down target price to HK\$6.90. While we are still positive on Fuji's overall business outlook, we have incorporated the downward revisions in each of the company's segment as mentioned above. Our new net profit estimates are RMB503.9m for FY3/09F, RMB569.2m for FY3/10F and RMB641.7m for FY3/11F, representing a downward adjustment of 5.5%, 13.3% and 17.0% respectively. The downward revisions takes into account a weaker economic outlook and lower production capacity as company scales back capex investment. We maintain our BUY call on the counter, with a new DCF-derived target price of HK\$6.90 after factoring in a higher risk premium for the stock, resulting in a discount rate of HK\$19.0% (previously 13.5%). The new target price represents 5.8x FY3/10F P/E.

P & L (RMBm)						Cash Flow (RMBm)					
	07A	08A	09F	10F	11F		07A	08A	09F	10F	11F
Year to Mar						Year to Mar					
Turnover	1,199.4	1,915.6	2,830.3	3,413.9	4,022.9	EBIT	410.5	553.4	733.4	836.8	967.1
% chg	50.5	59.7	47.8	20.6	17.8	Depre./amort.	94.4	154.5	226.4	286.0	354.5
Gross profit	695.4	1,127.8	1,646.7	1,992.9	2,330.4	Net int. paid	2.6	(0.3)	17.0	(9.3)	(101.8)
EBITDA	504.9	707.8	959.8	1,122.9	1,321.6	Tax paid	(34.4)	(35.2)	(61.9)	(113.3)	(146.3)
Depre./amort.	(94.4)	(154.5)	(226.4)	(286.0)	(354.5)	Dividends received					
EBIT	410.5	553.4	733.4	836.8	967.1	Gross cashflow	473.1	672.3	914.9	1,000.2	1,073.5
Net int. income/(exp.)	(26.8)	(77.6)	(84.0)	(87.4)	(101.8)	Chgs. in working cap.	(1.6)	(134.6)	12.1	2.7	10.7
Exceptionals						Operating cashflow	471.5	537.8	927.0	1,002.9	1,084.2
Associates						Capex	(1,015.9)	(1,658.0)	(725.2)	(820.4)	(576.2)
Jointly-controlled entit.						Free cashflow	(544.5)	(1,120.2)	201.8	182.5	508.0
Pre-tax profit	383.8	475.8	649.4	749.5	865.3	Dividends paid	(90.1)	(111.9)	(120.7)	(130.1)	(142.5)
Tax	(35.7)	(49.5)	(106.5)	(137.9)	(176.5)	Net distribution to MI					
Minority interests	0.0	(15.4)	(39.0)	(42.4)	(47.1)	Investments					
Net profit	348.1	411.0	503.9	569.2	641.7	Disposals					
% chg	38.5	18.1	22.6	13.0	12.7	New shares	0.0	4.5	0.0	0.0	0.0
Dividends	(104.6)	(120.3)	(119.8)	(134.1)	(143.7)	Others	62.1	610.2	(101.0)	(89.6)	(125.4)
Retained earnings	243.5	290.7	384.2	435.1	498.0	Net cashflow	(572.5)	(617.5)	(19.9)	(37.1)	240.1
EPS (RMB) - Basic	0.689	0.772	0.931	1.052	1.186	Net (debt)/cash - Beg.	94.9	(477.7)	(1,095.1)	(1,115.0)	(1,152.2)
EPS (RMB) - F.D.	0.689	0.772	0.931	1.052	1.186	Net (debt)/cash - End.	(477.7)	(1,095.1)	(1,115.0)	(1,152.2)	(912.1)
DPS (HK\$)	0.206	0.241	0.245	0.264	0.290	Interim Results (RMBm)					
No. sh.s o/s (m) - W.A.	504.9	532.6	541.3	541.3	541.3	Six months to Sep					
No. sh.s o/s (m) - Y.E.	510.3	541.3	541.3	541.3	541.3	Turnover	323.7	534.8	780.2		
No. sh.s o/s (m) - F.D.	505.1	532.6	541.3	541.3	541.3	% chg		65.2	45.9		
Margins (%)						Profit from operations	137.2	198.7	249.8		
Gross	58.0	58.9	58.2	58.4	57.9	Interest expenses	(4.5)	(10.1)	(35.7)		
EBITDA	42.1	37.0	33.9	32.9	32.9	Associates					
EBIT	34.2	28.9	25.9	24.5	24.0	Jointly-controlled entit.					
Pre-tax	32.0	24.8	22.9	22.0	21.5	Pre-tax profit	132.8	188.6	214.1		
Net	29.0	21.5	17.8	16.7	16.0	Tax	(18.6)	(16.4)	(17.3)		
						Minority interests					
						Net profit	114.1	172.2	196.8		
						% chg		50.8	14.3		
						EPS (RMB) - Basic	0.267	0.342	0.376		
						DPS (HK\$)					
Balance Sheet (RMBm)						Shareholding Structure					
	07A	08A	09F	10F	11F					Shares o/s (m)	%
Year to Mar											
Fixed assets	2,042.6	3,190.9	3,712.2	3,898.7	4,044.7					285.0	52.7
Intangible assets	197.5	795.8	908.4	976.3	1,046.0					33.4	6.2
Other LT assets	80.7	301.1	166.0	104.0	110.0					32.9	6.1
Cash	819.2	1,093.9	1,300.6	1,173.2	787.9					32.4	6.0
Accounts receivable	31.1	53.8	79.5	95.9	113.0					28.5	5.3
Other receivables	46.0	193.1	285.4	344.2	405.6					129.1	23.9
Inventories	27.8	88.7	133.3	160.0	190.6					541.3	100.0
Due from related co.s											
Other current assets											
Total assets	3,244.9	5,717.3	6,585.3	6,752.4	6,697.8						
Accounts payable	(21.5)	(126.2)	(189.6)	(227.6)	(271.1)	Background					
Other payable	(110.8)	(221.3)	(332.5)	(399.2)	(475.5)	Headquartered in Shanghai, Fu Ji Food and Catering Services mainly provides catering service to industrial clients in China. It is one of the largest professional catering service company with daily capacity exceeding 1m sets of meal in 2008. The company is also engaged in operation of Chinese restaurants, theme restaurants and sales of convenient food.					
Tax payable	(23.4)	(38.6)	(83.2)	(107.7)	(137.8)	Key Ratios					
Due to related co.s						07A	08A	09F	10F	11F	
ST debts	(319.5)	(269.0)	(400.0)	(400.0)	(700.0)	Net gearing (%)	29.5	47.7	37.0	33.3	23.4
Other current liab.	0.0	0.0	(341.9)	0.0	0.0	Net ROE (%)	21.5	18.3	17.5	17.3	17.4
LT debts	(977.3)	(1,920.0)	(2,015.6)	(1,925.4)	(1,000.0)	EBIT ROCE (%)	17.0	13.7	13.8	14.4	16.3
Other LT liabilities	0.0	(341.9)	0.0	0.0	0.0	Dividend payout (%)	30.0	29.3	23.8	23.6	22.4
Total liabilities	(1,452.5)	(2,917.0)	(3,362.8)	(3,059.9)	(2,584.5)	Effective tax rate (%)	9.3	10.4	16.4	18.4	20.4
Share capital	5.4	5.7	5.7	5.7	5.7	Net interest coverage (x)	15.3	7.1	8.7	9.6	9.5
Reserves	1,787.0	2,688.9	3,072.1	3,499.7	3,873.6	A/R turnover (days)	8.5	8.1	8.6	9.4	9.5
Shareholders' funds	1,792.4	2,694.6	3,077.8	3,505.4	3,879.2	A/P turnover (days)	4.7	14.1	20.4	22.3	22.6
Minority interest	-	105.7	144.7	187.1	234.1	Stock turnover (days)	15.6	27.0	34.2	37.7	37.8
Total	1,792.4	2,800.3	3,222.5	3,692.5	4,113.4						
Capital employed	3,089.2	4,989.3	5,638.1	6,017.9	5,813.4						
Net (debt)/cash	(477.7)	(1,095.1)	(1,115.0)	(1,152.2)	(912.1)						