

## Tontine Wines Group Ltd.

### Sweet, Sweet, Sweet!

to summarize...

- For 1H FY12/10A results, revenue came in at RMB288.9m, a 19% increase YoY while net profit came in at RMB89.9m, up 19% YoY. Gross margin for the period was 58.4%, up 1.8pcp. In line with expectations
- Tontine continues to focus on sales of sweet wine products. Sweet wines contributed 68.8%, increase from 68.2% in the 1H FY12/09A.
- Tontine plans to launch four new products in the sweet wine segment in this year to further strengthen their sweet wine portfolio.
- The group has undergone the second phased of capacity expansion, and the installation of production facility target to be completed by Q4 of this year.
- We revised our target price to HK\$2.28 (from HK\$2.38), Maintain BUY. The new target price represents 18.2x FY12/10F and 14.3x FY12/11F P/E.

**Interim results in line:** Tontine's 1H FY12/10A results were in line with expectations. Revenue was RMB288.9m, a 19% increase YoY while net profit came in at RMB89.9m, up 19% YoY. Gross margin for the period was 58.4%, up 1.8pcp. EPS decreased 8.8% to RMB0.052 (1H FY12/09A: RMB0.0057), due to increased in weighted average number of ordinary shares after the IPO in Nov 2009.

**Table 1. 1H FY12/10A results**

6 months to Dec	Turnover (RMBm)	Gross Profit (RMBm)	Gross margin (%)	Pre-tax profit (RMBm)	Tax rate (%)	Net profit (RMBm)
1H FY10	288.9	168.7	58.8	128.4	29.9	89.9
1H FY09	242.7	137.4	56.6	106.6	29.2	75.4
HoH(%)	19.0	22.7		20.0		19.2

Source: Company data

**Sweet wine continues to be the key driver:** Tontine continues to focus on sales of sweet wine products. Sweet wines contribute 68.8% of total sales in 1H FY12/10A, (up from 68.2% a year ago), with dry wine contributing the remaining 31.2%. Revenue from sweet wine represented 20.1% YoY growth to RMB198.8m with ASP increasing to RMB34.9 per tonne (1H FY12/09A: RMB29.3 per tonne). The significant increase in the average selling price of sweet wine products was the result of changing product mix to higher price product. Meanwhile, dry wine sales grew 16% YoY growth to RMB90.1m. ASP for this segment increased RMB0.8 to RMB28.6 per tonne.

**Margin improvement from higher selling price and stable cost:** Blended gross profit margin improved 1.8pcp YoY to 58.4%, driven by a combination of increasing in sales of high margin product and stable cost. Total raw material cost drop slightly from 74.1% to 73.2% of COGS.

**New developments and future plans:** Tontine has planned to launch four new products in the sweet wine segment in this year. The "Tontine Premium Blueberry Wine" was launched in January 2010 was well received by customer. Other product will be under label of the "Tontine Special Selection Ice Red", "Tontine Premium Ice Wine" and "Tontine Premium Rose Wine". The selling price on them will be targeting in the premium price range which is over RMB100. By introducing products in the premium price range allows them to attain a higher profit margin.

**Capacity increase:** Tontine will double their annual production capacity from 19,000 tonnes to 39,000 tonnes by the end of 2010. The group has undergone the second phase of capacity expansion, and the installation of production facility target to be complete by Q4 of this year.

Ticker	0389 HK
Rating	BUY(Unchanged)
Price (HK\$)	1.58
Target Price (HK\$)	2.28(+44%)
12m Price Range (HK\$)	1.25-2.05
Market cap. (US\$m)	357.2
Daily t/o (US\$m)	1.3
Free float (%)	53.0

#### Financial summary

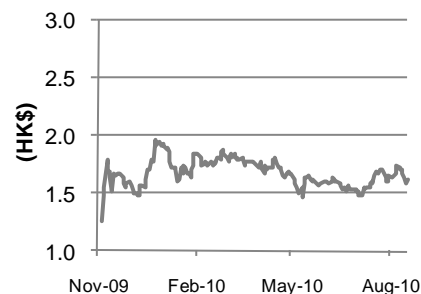
Year to Dec	08A	09A	10F	11F	12F
Turnover (RMBm)	486.7	584.3	704.0	866.7	998.0
Net Profit (RMBm)	136.8	174.1	214.8	273.0	323.9
EPS (RMB)	0.103	0.101	0.125	0.159	0.189
P/E (x)	17.0	17.4	14.1	11.1	9.3
P/B (x)	6.28	3.12	2.62	2.19	1.84
EV/EBITDA (x)	10.8	9.4	7.6	5.9	4.7
Yield (%)	-	1.4	1.8	2.3	2.7
ROE (%)	52.8	26.0	20.2	21.6	21.5
ROCE (%)	77.4	37.0	28.3	29.3	28.6
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Source: SBI/Bloomberg

	10F	11F	12F
Consensus EPS (RMB)	0.123	0.147	-
Previous earnings (RMBm)	212.2	272.0	-
Previous EPS (RMB)	0.124	0.158	-

#### Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	0.7	-5.4	-
Actual price changes (%)	-1.8	-1.8	-



Source: Bloomberg

#### SBI Research Team

(852) 2533 3700  
sbie2research@sbie2capital.com

The group also plans to develop a wines estate to produce premium range of estate bottle wine labeled under "Estate Bottled" from higher quality of grapes. The construction of Estate Wine will be commenced in second half of 2010 and complete by 2014. Construction of Wine Cellar will be completed by the end of 2010, cellar wine target to be launched by 2011.

**Table 2. Sales volume, ASP and revenue breakdown**

	1H 10A	1H 09A	YoY (%)	% of total
<b>Sweet wine</b>				
Vol (tonnes)	5,694	5,654	0.7	64.3
ASP(RMBk/t)	34.9	29.3	19.1	
Revenue (RMBm)	198.8	165.5	20.1	68.8
<b>Dry wine</b>				
Vol (tonnes)	3,154	2,774	13.7	35.6
ASP(RMBk/t)	28.6	27.8	2.9	
Revenue (RMBm)	90.1	77.2	16.7	31.1
<b>Total</b>				
Vol (tonnes)	8,848	8,428	4.9	100.0
ASP(RMBk/t)	32.7	28.8	13.5	
Revenue (RMBm)	288.9	242.7	19.0	100.0

Source: Company data

**Table 3. Cost structure breakdown**

	1H 10A(RMBm)	%	1H 09A(RMBm)	%	YoY (%)
<b>Raw material</b>					
Grape and grape juice	55.7	46.3	47.9	45.5	16.3
Yeast & others	4.3	3.6	4.0	3.8	7.5
Packaging	27.7	23	25.8	24.5	7.4
Others	.3	0.3	0.3	.3	(0)
<b>Subtotal</b>	<b>88.0</b>	<b>73.2</b>	<b>78.1</b>	<b>74.1</b>	<b>12.7</b>
<b>Others</b>					
Prod'n o/heads	3.4	2.8	3	2.8	13.3
Tax	28.9	24	24.3	23	19.0
<b>Subtotal</b>	<b>32.3</b>	<b>26.8</b>	<b>27.3</b>	<b>25.8</b>	<b>18.3</b>
<b>Total</b>	<b>120.2</b>	<b>100.0</b>	<b>105.3</b>	<b>100.0</b>	<b>14.2</b>

Source: Company data

**Valuation:** We revised our sales estimate to RMB704m for FY12/10F (from RMB709m) with 11.2% volume growth and 8.4% ASP growth for the full year. We estimate RMB866.7m for FY12/11F (from RMB874.5m) with 17.8% volume growth and 4.5% ASP growth. We estimate that the net profit would be RMB214.8m for FY12/10F (from RMB212.2m) and RMB273.0m for FY12/11F (from RMB272.0m). Our new DCF-derived target price is HK\$2.28 based on 2% terminal growth and 12% discount rate. Keep BUY. The new target price represents 18.2x FY12/10F and 14.3x FY12/11F P/E. The HK listed peers are currently trading at average 25.1x FY12/10F and 19.8x FY12/11F P/E based on market consensus.

**Table 4. Valuation comparison**

Company name	Ticker	Mkt cap (US\$m)	Last Price (Local)	His P/E (x)	1-Yr P/E (x)	2-Yr P/E (x)	PB (x)	Est ROE (%)
<b>HK-listed</b>								
China Food	506 HK	2026.3	5.66	35.4	27.5	20.9	2.83	10.7
Dynasty	828 HK	523.5	3.28	23.6	22.6	18.7	2.19	8.8
<i>Average</i>				29.5	25.1	19.8		
<b>China-Listed</b>								
Tongpu	600365 CH	245.0	13.65	-	-	-	12.4	-
CITIC Guoan Vine	600084 CH	887.8	8.85	-	-	45	7.37	-
Mogao	600543 CH	534.4	12.98	110.9	36.3	22.8	4.1	3.7
Changyu	000869 CH	5812.6	92.46	38.6	35	28.3	16.22	40.5
<i>Average</i>				52.1	30.4	27.1		
<i>Average*</i>						22.7		

\*exclude the Tongpu and CITIC Guoan Vine

Source: Bloomberg

Table 5. P &amp; L forecast

Year to Dec (RMBm)	08A	09A	10F	11F	12F
<b>Revenue</b>					
Sweet Wine	321.4	403.8	499.1	639.2	749.8
Dry Wine	165.3	180.5	204.9	227.5	248.2
	486.7	584.3	704.0	866.7	998.0
Cost of sales	(209.8)	(246.1)	(289.3)	(347.7)	(393.3)
<b>Gross profit</b>	276.9	338.2	414.7	519.0	604.6
Other income	0.2	1.7	6.0	8.7	12.0
Selling and distribution expenses	(53.5)	(67.9)	(96.2)	(128.6)	(151.0)
Administrative expenses	(9.8)	(13.3)	(17.6)	(19.9)	(22.0)
Other expenses	(13.0)	(9.0)	0.0	0.0	0.0
Finance costs	0.0	0.0	0.0	0.0	0.0
<b>Profit before tax</b>	200.9	249.7	306.9	379.2	443.7
Income tax expense	(64.1)	(75.6)	(92.1)	(106.2)	(119.8)
<b>Net profit</b>	136.8	174.1	214.8	273.0	323.9

Source: Company data, SBI E2-Capital

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Disclosure of interests: SBI E2-Capital Securities Limited was acted as the sole bookrunner and lead manager for the China Tontine Wines Group Limited (stock code: 389) in November 2009.

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**HOLD** : absolute return of -10% to +10% over the next six months

**SELL** : absolute downside of >10% over the next six months

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