

Tianyi Fruit

Maximizing the value of an orange

to summarize...

- Tianyi's business model is to maximize the value of the orange.
- Tianyi's fresh orange was sold under the brand of "Shangguo" while the fresh orange sold has a higher value than the FCOJ sold.
- Tianyi is a leading domestic FCOJ manufacturer, its key clients include Coca-cola, Suntory, Wahaha and etc.
- Newly launched product, FCOJ fiber improved the profitable level and also locked its relations of Tianyi with its key clients
- Plan to expand its orange farm to 80,000 mu by 2013 and schedule to launch more new product.
- For 1H FY06/10A, Tianyi's revenue increased 11.4% YoY to RMB184.0m while the net profit (excl. the effect of biological asset) increased 60.8% YoY to RMB61.1m.
- Currently trading at 16.6x FY06/10 P/E and 11.7x FY06/11 P/E based on market consensus.

Company Background. Tianyi Fruit Holdings Limited (Tianyi) was founded in Quanzhou, Fujian Province in 1993. Tianyi is now a leading Frozen Concentrated Orange Juice (FCOJ) and fresh orange supplier in China. It also diversified its business to FCOJ fiber, Pulp and other tropical fruit juice. The company has 50,000 mu self-managed orange farm in Chongqing City and Fujian Province. The company was listed in HKEx main Board in July 2008.

Tianyi's business model maximized the value of the orange. Tianyi licensed 50,000 mu orange farms in Fujian and Chongqing, which are located in two of three major citrus plantation areas in China, to operate itself. Tianyi selects the high quality fresh oranges for selling on the fresh oranges market, which had been sold between RMB1.66/kg and RMB1.78/kg from July 2006 to June 2009, while the remaining oranges are used as raw materials for the production of FCOJ with FCOJ's ASP between RMB13.59/kg and RMB14.69/kg from July 2006 to June 2009. At the same time, Tianyi could also sell orange pulp, which is the remains of the orange after the orange juice has been press out. The orange pulp had been sold at between RMB4.83/kg and RMB6.15/kg from July 2006 to June 2009. On the customer side, Tianyi sells its fresh oranges to fresh fruit distributor and wholesaler directly. The FCOJ is sold to domestic orange juice manufacture. Tianyi has business relations with its 5 largest clients, including Coca-cola, Suntory, Wahaha, ranged from 7 to 12 years. 3 of its largest clients accounted for 38.0% of Tianyi's total FCOJ sales in FY06/09A.

"Shangguo" brand for fresh orange. Fresh orange sales revenue is one of the major revenue generators for Tianyi. Tianyi's fresh fruit has been sold under the brand of "Shangguo". The company sold 47,547 tonnes fresh fruit in 1H FY12/10A, accounting for 43% of Tianyi's total revenue. Tianyi normally choose high quality fresh oranges to sell to third-party distributor rather than making FCOJ because: 1) the ASP of fresh orange sold is 3.5x-4.0x higher than ASP of orange used for making FCOJ. The ASP of fresh orange sold is between RMB1.66/kg and RMB1.78/kg from July 2006 to June 2009 while the ASP of orange for making FCOJ is between RMB0.45/kg and RMB0.50/kg. 2) Tianyi normally used 12kg orange to make 1kg FCOJ. Based on this equivalence, the value of fresh orange sold is 44.6% to 46.6% higher than the value of FCOJ sold.

Ticker	756 HK
Rating	Not Rated
Price (HK\$)	2.26
Target Price (HK\$)	N.A.
12m Price Range (HK\$)	0.70-2.64
Market cap. (US\$m)	332.2
Daily t/o (US\$m)	0.3
Free float (%)	39.4

Financial summary

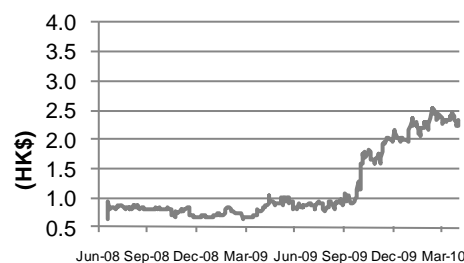
Year to June	08A	09A
Turnover (RMBm)	267.6	337.4
Net Profit (RMBm)	55.6	71.1
EPS (RMB)	0.055	0.071
P/E (x)	35.9	28.1
P/B (x)	7.5	4.4
EV/EBITDA (x)	17.6	17.4
Yield (%)	-	-
ROE (%)	24.8	47.2
ROCE (%)	39.9	29.0
N. Gear. (%)	cash	cash

Source: company data

	10F	11F	12F
Consensus EPS (RMB)	0.120	0.170	0.210
Previous earnings (RMBm)	-	-	-
Previous EPS (RMB)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	-4.8	-1.4	+101.8
Actual price changes (%)	-3.4	+1.3	+181.5



Source: Bloomberg

Research Team

SBI E2-Capital Securities Ltd.
(852) 2533 3700
sbie2research@sbie2capital.com

Table 1. fresh fruit sold and FCOJ sold

	July 2006-June 2007	July 2007-June 2008	July 2008-June 2009
Fresh oranges Sold(Tonnes)	60,775	64,561	56,734
Average price per kg (RMB)	1.77	1.78	1.66
FCOJ sold (Tonnes)	6,508	8,573	15,921
Average price per kg (RMB)	14.69	14.69	13.59

Source: Company data

China has imported majority of FCOJ. Around 75% FCOJ in China is imported mainly from Brazil and America because China does not have enough orange raw materials that are suitable for making FCOJ while Brazil and America has the advantage in FCOJ raw material. In 2009, China imported 44,464 tonnes FCOJ from Brazil and 1,455 tonnes from America based on market data. The current orange juice per capita consumption was only about 0.3 liter far below the world average consumption of 3 liters. However, increasing disposable income and improving nutrition awareness in China would encourage the demand for fresh orange juice, such as the popular of Coca-cola's fresh orange juice drink product-"Minute Maid 美汁源" orange juice product.

Tian Yi is the leading domestic FCOJ manufacturer. Tianyi accounted for 38.0% domestic FCOJ production in 2009. As a key domestic supplier, Tianyi is leveraging its advantage to: 1) supply to top beverage players in China, such as Coca-Cola China, Suntory, Wahaha, Pepsi China, and build up long term relations and trust with them; 2) secured domestic FCOJ raw material with 50,000 mu self-managed orange farms in Fujian and Chongqing. The company is also working closely with local government in orange farm expansion and the product development.

Diversified products improve the margin. Tianyi started a new product of FCOJ fiber in 2009. FCOJ fiber is a mixture of FCOJ with lower concentration rate and orange pulp sac, which was used for production of pulpy fruit juice and blended fruit juice. As FCOJ fiber has a shorter expiration period and higher requirement for storage, the new product further locked the relations of Tianyi with its key clients, such as Coca-cola, to improve its competitive advantage with overseas suppliers. In 1H FY06/10A, Tianyi sold 6,447 tonnes of FCOJ fiber with revenue of RMB44.1m. The gross margin of FCOJ fiber was 64.0% which is above the company average gross margin of 54.0%.

1H FY06/10A results. For 1H FY06/10A, Tianyi's revenue increased 11.4% YoY to RMB184.0m while the net profit increased 92.1% YoY to RMB91.7m. Our adjusted gross profit (excl. the effect of biological asset) increased 48.7% YoY to RMB99.4m while the net profit (excl. the effect of biological asset) increased 60.8% YoY to RMB61.1m. The sales growth was mainly drive by the growth in sales volume of fresh fruit and launch of FCOJ fiber while the high margin of FCOJ fiber improved the overall margin and net profit of the company.

Table 2. 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	184.0	99.4	54.0	71.4	12.1	61.1
1H FY09	165.2	66.9	40.5	53.6	29.0	38.0
YoY (%)	11.3	48.7		33.2		60.8

Source: Company data

Note: Gross profit and net profit excluded the biological asset

Table 3. 1H FY12/10A revenue breakdown

6 month ended to Dec (RMBm)	1H FY06/10			1H FY06/09			YoY (%)	
	Revenue	Gross profit	Margin(%)	Revenue	Gross profit	Margin(%)	Revenue	Gross profit
FCOJ	48.6	20.2	42.0	84.7	29.6	35.0	(42.6)	(31.8)
Fresh Fruit	79.8	32.7	41.0	64.0	23.7	37.0	24.7	38.0
FCOJ Fiber	44.1	28.2	64.0	-	-	-	-	-
Pulp	5.5			5.0	-	-	-	-
Others	6.5			11.5	-	-	-	-
Total	184.5	99.4	54.0	165.2	66.9	14.8	11.7	48.7

Source: Company data

Note: Gross profit and net profit excluded the biological asset

Expansion strategy. Tianyi's expansion will be mainly in two ways: 1) land and capacity expansion. Tianyi normally works with local government to discuss the terms and sign the lease contract with villager's committee. In 2009, the company leased orange farm of 20,000 mu in Kai County, which was located in one of three major Citrus Plantation Areas in China, to increase its operating land from 30,000mu to 50,000mu. At the same time, Tianyi built up 10,000 tonnes FCOJ production capacity in Kai County to match with its land expansion. Furthermore, Tianyi has already agreed with local government in Kai County for developing 20,000 mu quality plantable orange farms, which expect to have production in 3 years time. Also, Tianyi will further lease 10,000 mu land to have 80,000 mu leased orange farms by 2013. 2) Introducing new product. In 2009, Tianyi launched FCOJ fibers, which not only improved the profitable level but also locked the relations of Tianyi with its key clients. The company is scheduling to research and develop tropical fruit juice products in Hainan Island.

Corporate governance. Mr. Sin Ke is the CEO and founder of the company. Before starting Tianyi in 1993, Mr. Sin had 12 year experience in sales, manufacturing, and administration of beverage, health products and pharmaceutical products. Currently, Mr. Sin and his family hold 55.4% of the listco; Dr. Shi Zheng Rong had 5.2% share and other public shareholders had 39.4%.

Risks. We think the company is subject to the following risks: 1) Fresh Orange and FCOJ price fluctuation; 2) Natural disasters; 3) government regulation change.

Valuation. The counter is currently trading at 16.6x FY06/10 and 11.7x FY06/11 P/E based on market consensus. The other agriculture upstream player, China Green (904 HK), is now trading at 14.7x FY04/10F P/E and 12.0x FY04/11F P/E based on market consensus. The downstream player, Huiyuan (1886 HK), is now trading at 33.5x FY12/10F P/E and 27.0x FY12/11F P/E based on market consensus.

Table 4. P & L				
Year to June (HK\$m)	08A	09A	1H09A	1H10A
Turnover	267.6	337.4	165.2	184.0
Cost of sales	(196.3)	(252.8)	(129.0)	(127.0)
Gross profit	71.3	84.5	36.2	57.0
Gain from changes in fair value of biological assets less estimated point-of-sale costs	44.0	44.4	44.4	77.1
Other income	1.4	1.9	1.9	1.8
distribution expenses	(5.9)	(8.3)	(4.3)	(11.7)
Administrative expenses	(6.7)	(21.8)	(11.0)	(17.9)
Other expenses	(0.3)	(0.1)	(0.1)	(0.3)
Profit from Operation	103.7	100.6	67.1	106.1
Finance costs	(3.0)	1.2	0.1	0.1
Profit before taxation	100.7	101.8	67.2	106.1
Taxation	(27.9)	(30.7)	(19.5)	(12.8)
MI	(7.1)	0.0	0.0	(1.7)
Net profit	65.8	71.1	47.7	91.7

Source: Company data

SBI E2-Capital is a dedicated small/mid cap investment banking/ stockbrokerage house. Find our research on: sbie2capital.com, thomsononeanalytics.com, factset.com and multex.com

SBI E2-Capital stock ratings:

STRONG BUY : absolute upside of >50% over the next three months

BUY : absolute upside of >10% over the next six months

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

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

Investors should assume that SBI E2-Capital is seeking or will seek investment banking or other related businesses with the companies in this report.

Analyst certification: The views expressed in this report accurately reflect the analyst's personal views of the subject securities and that the analyst has not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

Disclaimer: This research report is not an offer to sell or the solicitation of an offer to buy or subscribe for any securities. The securities referred to in this report may not be eligible for sale in some jurisdictions. The information contained in this report has been compiled by the Research Department of SBI E2-Capital Securities Limited ('SBI E2-Capital') from sources that it believes to be reliable but no representation, warranty or guarantee is made or given by SBI E2-Capital or any other person as to its accuracy or completeness. All opinions and estimates expressed in this report are (unless otherwise indicated) entirely those of SBI E2-Capital as of the date of this report only and are subject to change without notice. Neither SBI E2-Capital nor any other person, accepts any liability whatsoever for any loss howsoever arising from any use of this report or its contents or otherwise arising in connection therewith. Each recipient of this report shall be solely responsible for making its own independent investigation of the business, financial condition and prospects of the companies referred to in this report. SBI E2-Capital and their respective officers, directors and employees, including persons involved in the preparation or issuance of this report, may from time to time (1) have positions in, and buy or sell, the securities of companies referred to in this report (or related investments); (2) have a consulting, investment banking or broking relationship with any company referred to in this report; and (3) to the extent permitted under applicable law, have acted upon or used the information contained or referred to in this report including effecting transactions for their own account in an investment (or related investment) in respect of any company referred to in this report, prior to or immediately following its publication. This report may not have been distributed to all recipients at the same time. This report is issued only for the information of and may only be distributed to professional investors and dealers in securities and must not be copied, published, reproduced or redistributed (in whole or in part) by any recipient for any purpose. This report is distributed in Hong Kong by SBI E2-Capital. Any recipient of this report who requires further information regarding any securities referred to in this report should contact the relevant office of SBI E2-Capital located in such recipient's home jurisdiction.

Copyright © SBI E2-Capital Securities Limited 2008. All rights reserved.