

**Analyst: Anita Hwang**
**CHINA RESOURCES ENTERPRISE, LIMITED (華潤創業)**

Sector	: Conglomerates	Chairman	: Charles SONG Lin
HKSE Code	: 0291	Managing Director	: Chen Shulin
Market Price	: HK\$31.70 (05/09/2007)		
HSI	: 24,069.17 (05/09/2007)		
Shares Issued	: 2,378.012 million		
Market Cap.	: HK\$75,383 million		
52-week Hi / Lo	: HK\$34.80 / HK\$16.00		

**SUMMARY OF THE INTERIM RESULTS FOR THE SIX MONTHS ENDED 30<sup>TH</sup> JUNE 2007**
**Interim Results Highlights**

	1H07	1H06	Change
	HK\$ million	HK\$ million	
• Turnover	35,153	31,581	11.3%
• Profit before tax	1,780	1,601	11.2%
• Share of results of associates	162	151	7.3%
• <b>Profit attributable to shareholders</b>	<b>3,737</b>	<b>1,266</b>	<b>195.2%</b>
• EPS – Basic (HK\$)	1.58	0.55	187.3%
• Interim DPS (HK\$)	0.15	0.14	7.1%
• Special DPS (HK\$)	0.60	-	NA

• China Resources Enterprise (“CRE”) reported an attributable profit of HK\$3.737 billion for the six months ended 30th June 2007, up 195.2% when compared with the corresponding period last year. The sharp jump in earnings was mainly due to a disposal gain of HK\$2,393 million from the sale of non-core petroleum distribution operation in Hong Kong. EPS increased 187.3% y-o-y to HK\$1.58 whilst CRE declared an interim dividend of HK\$0.15 per share, up 7.1% from last year. A special dividend of HK\$0.60 per share was also declared.

• CRE recorded net revaluation gains in investment properties of HK\$274 million in 1H07 (vs. HK\$355 million in 1H06). Excluding the after-tax effect of revaluation of investment properties and major disposals, which led to aggregate gains of HK\$2,680 million in 1H07 and HK\$366 million in 1H06, CRE’s underlying unedited consolidated profit attributable to shareholders increased by 17.4% y-o-y to HK\$1.057 billion, which was in-line with market expectations

• As of 30<sup>th</sup> June 2007, consolidated net borrowings amounted to HK\$652 million (31/12/2006: HK\$1.78 billion) and net gearing ratio was 2.9% (31/12/2006: 9.3%).

• **Turnover breakdown:**

(HK\$ million)	1H07	%	1H06	%	Change
Retail	12,437	35.4%	9,910	31.4%	25.5%
Beverage	6,283	17.9%	4,345	13.8%	44.6%
Food processing and distribution	3,441	9.8%	2,889	9.1%	19.1%
Textile	2,318	6.6%	2,126	6.7%	9.0%
Investment Property	183	0.5%	171	0.5%	6.8%
Petroleum & related products distribution	10,610	30.2%	12,252	38.8%	-13.4%
Elimination of inter-segment transactions	(119)	-0.3%	(112)	-0.4%	6.4%
<b>Total</b>	<b>35,153</b>	<b>100.0%</b>	<b>31,581</b>	<b>100.0%</b>	<b>11.3%</b>

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- **Net profit breakdown (excluding revaluation gain and asset disposal):**

(HK\$ million)	1H07	%	1H06	%	Change
Retail	263	24.9%	147	16.4%	78.5%
Beverage	118	11.2%	76	8.5%	55.3%
Food processing and distribution	224	21.2%	214	23.8%	4.8%
Textile	66	6.2%	41	4.5%	62.0%
Investment Property	112	10.6%	114	12.7%	-1.7%
Petroleum & related products distribution	183	17.3%	217	24.1%	-15.7%
Investments & others	198	18.7%	191	21.2%	3.7%
Net corporate interest and expenses	(107)	-10.1%	(100)	-11.2%	6.6%
<b>Total</b>	<b>1,057</b>	<b>100.0%</b>	<b>900</b>	<b>100.0%</b>	<b>17.6%</b>

- Net profit of **retail** business, which comprises supermarkets, retail stores in Hong Kong and brand-fashion distribution in China, rose by 78.5% y-o-y to HK\$263 million. The growth was underpinned by organic growth in the supermarket operation.
  - **Supermarket** operation saw a 26.2% y-o-y increase in turnover to HK\$11.2 billion and a 68.9% y-o-y increase in profit contribution to HK\$201 million. Overall same store growth for 1H07 was 8.2%, in particular a 9.0% increase was achieved for the stores in the Mainland. EBITDA for 1H07 amounted to HK\$525 million, representing a 20.4% y-o-y growth.
  - **Brand-fashion distribution** in China reported turnover and attributable profit for 1H07 of HK\$876 million and HK\$48 million respectively, representing a corresponding y-o-y increase of 20.5% and 269.2%.
  - **Other retail stores** Turnover and attributable profit of the other retail stores segment for 1H07 were HK\$378 million and HK\$24 million respectively, representing a corresponding y-o-y increase of 17.0% and 60.0% respectively. The store network consisted of 5 Chinese Arts & Crafts stores in Hong Kong and 38 CR Care stores in Hong Kong and the Mainland as at the end of 1H07.
- Profit contribution from the **beverage** business rose by 55.3% y-o-y to HK\$118 million. Beer sales volume grew 36.6% y-o-y to 3.336 million kilolitres, representing a domestic market share of about 17.8% (2006: 15.1%). Overall average selling price increased 2% y-o-y (in RMB) and overall gross margin remained steady. National brand "SNOW" recorded a sales volume of 2.377 million kilolitres, representing an impressive growth of 82.0% y-o-y in volume. Net margin increased to 1.88% during 1H07 from 1.75% in 1H06.
- The **food processing and distribution** business saw a net profit growth of 4.8% y-o-y to HK\$224 million. Despite the shortage of livestock and price volatility, foodstuff distribution reported an 8% rise in operating profit boosted by the higher contribution from the frozen food and assorted food distribution. Sales volume growth under the marine fishing and aquatic products processing operation was 26.0% y-o-y.
- The **textile** business reported a net profit of HK\$66 million (1H06: HK\$41 million). The sharp y-o-y increase was due to the one-off worker compensation in 1H06. Sales volume of **cotton yarns** increased 9% y-o-y to 31,884 tonnes whilst sales of **fabrics** dropped by 15% y-o-y to 93 million meters. Average selling price of yarns and fabrics rose 5% and 6% y-o-y respectively on technology upgrade. Earnings contribution from the **garment** division increased by 29% y-o-y with a 37% increase in sales volume.
- Net profit of the **investment property** business fell by 19.6% y-o-y to HK\$386 million while turnover for 1H07 was HK\$183 million, representing an increase of 6.8% over 1H06. Excluding net-of-tax revaluation surplus and disposal gains of certain non-core investment properties aggregating some HK\$274 million (1H06: HK\$366 million), attributable profit of the division decreased by 1.7% y-o-y to HK\$112 million. Gross rental income increased by 8% y-o-y to HK\$182 million on the back of a 2.0% increase in average retail rent.

- Turnover and attributable profit of the **petroleum and related products distribution** division for 1H07 amounted to HK\$10.61 billion and HK\$2.576 billion respectively. Excluding a gain of HK\$2.393 billion from the disposal of the entire interest in petroleum distribution business in HK, the attributable profits for 1H07 was actually decreased by 15.7% y-o-y to HK\$183 million.
- CRE has a 10% interest in HIT Investments and Hutchison Ports Yantian investments, which together made a net profit of HK\$198 million in 1H07, up 3.7% y-o-y.

### **Outlook & Prospect**

- **PRC supermarket business** CRE's parent company now operates all the previous Home World stores under the "CR Vanguard" brand. Stores in Tianjin and Xi'an performed well with market share of about 30% in Tianjin (20 stores). Stores in other Northeastern provinces have not been performing well. Management maintained the view to inject profitable stores into CRE and it could take some 12-18 months to turnaround a fair proportion of stores into profitable. Hence, the asset injection concept may not realize until mid of next year the earliest. Meanwhile, strong same store growth is expected in the existing supermarkets operations.
- **Brewery business** With a target to achieve a capacity of 11 million kiloliters by the end of FY09, CRE continued acquisitions of breweries. The latest ones in August included 4 breweries, 2 in Liaoning Province and 1 in each of Anhui and Hunan Provinces for a total investment of RMB596 million. This will increase CRE's total beer production capacity in China by 0.5 million kiloliters to 9.0 million kiloliters. In 1H07, the averaged 2% increase in cost per kiloliter was passed through into similar increase in the average selling price. Going forward, barley cost is expected to stay high and this remains the biggest overhang of CRE. Meanwhile, new breweries will drag on the segment's profitability as new breweries typically take 2-3 years to be profitable. However, organic growth among the existing breweries remains strong (1H07: 50% y-o-y). As the capacity is on track to approach the target of 11 million kiloliters, the focus will now shift from acquisition to improving profitability.
- **Food processing and distribution** In 2Q07, the shortage of supply of livestock in the Mainland put pressure on cost and lowered the attributable profit of the livestock distribution business. The operating environment is expected to be challenging as Guangnan Hong is going to be the second agent to import live pigs from the Mainland to Hong Kong. Management said they are still assessing the impact, while we expect some import business from Ng Fung Hong would be taken away by Guangnan Hong next year.
- **Divestment of non-core assets** CRE maintains the vision to become a true retail / consumer player and to divest non-core investments in HIT and possibly textile business back to its parent company. However, no timetable is revealed and those divestments are not expected to be materialized in the near-term.
- **Valuation on the high side** The counter has surged about 45% year-to-date and is trading at 33X FY08E PER. Although the expansion of retail network and robust growth in sales and capacity of brewery business make the counter attractive on a longer-term perspective, the current valuation already caught up with other consumer plays after re-rating. We are "Neutral" on the counter.

## **Recommendation: Neutral**



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