

Analyst: Anita Hwang

Main Board Listing – Research
Jiahua Stores Holdings Limited [Stock Code: 0602] (佳華百貨控股有限公司)

Sponsor : Taifook Capital Ltd
Sole bookrunner and lead manager : Taifook Securities Co. Ltd
Sector : Retailing
Business : Operation of retail stores

<p> Total share offer: <u>250,000,000</u> shares (25 % of the enlarged share capital) Public Offer: 25,000,000 shares (10%) Placing: 225,000,000 shares (90%) Greenshoe: 37,500,000 shares Price: HK\$0.87 – HK\$1.04 per share Market Cap: HK\$870 – HK\$1,040 million FY06 PER: 15.0X – 18.0X Adjusted NTA per share: RMB0.24 – RMB0.29 Staffing: 2,638 </p>	<p> <u>Business of Jiahua Stores (Jiahua)</u> Jiahua Stores (Jiahua) operates 8 large-scale retail stores, 7 of which are located in the Baoan (寶安) District in Shenzhen and the remaining one in Dongguan. Each store is operated in the form of department store plus supermarket. The retail stores are operated under the trade name of “佳華商場”. The first store was opened in 1997 and Jiahua now operates total gross floor area of 57,539 sq. m. for the supermarket section and 76,933 sq. m. for the department store section. Jiahua positions the retail stores at the mid-tier of the market segment with the strategy to attract customers into large-scale supermarkets for daily necessities and in turn create traffic flow in the department store sections. Sales from the retail stores are divided into direct sales and concessionaire sales. Merchandises in the department stores are sold mainly through concessionaire sales while the merchandises in the supermarkets are sold mainly through direct sales. </p>
<p> HK Public Offer period: 8th May 07 – 11th May 07 noon Receiving bank: The Bank of East Asia Ltd. Share registrar: Tricor Investor Services Limited Listing date: 21st May 2007 </p>	

Major Shareholders after Listing (Assuming the over-allotment option is not exercised)

Mr. Zhuang Lu Kun, the founder, Chairman & executive director	60.75%
	60.75%

*Cornerstone investors:

General Motors Investment Management Corporation (GMIMC) and the China Development Capital Partnership Master Fund (CDCPMF) have agreed to purchase an aggregate of 30,000,000 shares, representing 3% the enlarged share capital or 12% of the Offer Shares. Martin Currie Investment Management Limited, an active equity manager based in the UK, acts as manager for GMIMC and CDCPMF. The lock-up period will be 12 months following the listing date.

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**Use of Proceeds**

Net proceeds from the offer are estimated to be HK\$216 million. *(Being the mid-point of the offer price range [HK\$0.955 per share] and assuming the over-allotment option is not exercised)*

	HK\$ million
For the establishment of new retail stores in the Guangdong province	100
For acquisition of retail stores	63
For the establishment of procurement centre and the upgrade of the MIS to complement the retail chain business	38
For promotion of brand image	6
For general working capital	9

Financial Highlights

(RMB million)	Year ended 31 Dec		
	2004	2005	2006
Revenue	581.95	546.17	630.62
Gross profit	123.37	132.90	146.57
Operating profit	50.81	66.50	65.58
Net profit	49.98	56.54	56.91
Gross margin	21.2%	24.3%	23.2%
Operating margin	8.7%	12.2%	10.4%
Net margin	8.6%	10.4%	9.0%

Revenue Breakdown by business activities (% of Total revenue)

	2004		2005		2006	
	RMB million	%	RMB million	%	RMB million	%
Direct sales	523.2	89.9	507.8	88.1	547.0	86.7
Commissions from concessionaire sales	45.9	7.9	55.8	9.7	68.4	10.9
Rental income from leasing of shop premises	12.8	2.2	12.6	2.2	15.2	2.4
Total revenue	582.0	100.0	576.2	100.0	630.6	100.0

Strengths/Opportunities

- ✓ Jiahua has strong presence in Baoan District in Shenzhen. A recognized brand in Shenzhen should help the company's expansion strategy.
- ✓ Based on Jiahua's historic FY06 PER of 15.0X – 18.0X, valuation seems cheaper than its peers. Peers engaged in supermarket operation, such as Lianhua (0980.HK) and Beijing Jingkelong (8245.HK) trade at FY07E PER of 21X – 24X. Peers engaged in department store operation, such as Parkson (3368.HK) and Golden Eagle (3308.HK), trade at 34X-46X FY07E PER. However, valuation discount to its peers reflects the relatively small scale of Jiahua's operations and small local coverage of its network.

Weaknesses/Threats

- × Competition is very intense in China's retail industry. Jiahua lacks the economy of scale that other large domestic and international retail businesses command. Although household consumption is growing in China, retailers have experienced heightened competition in recent years and margin erosion is seen in some smaller players.
- × Three of the eight stores started operation for less than a year (they were opened during Aug 2006 to Jan 2007). On average, Jiahua added a new store every 1-2 years in the past. How well Jiahua can manage rapid expansion is yet to be tested.

Recommendation: Neutral



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