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HONG KONG RESEARCH
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Analyst: Kelvin Li

Main Board Listing – Research

神冠控股(集團)有限公司
Shenguan Holdings (Group) Limited [Stock Code: 00829]

Sole Global Coordinator	:	Macquarie Capital	
Joint Bookrunners, Joint Lead Managers and Joint Sponsors	:	Macquarie Capital	China Merchants Securities

Sector : Food, Beverage & Tabacco
Business : Manufacture of edible collagen sausage casing products

Total share offer: *400,000,000* shares
(25% of the enlarged share capital)

Public Offer: *40,000,000* shares (10%)
Placing: *360,000,000* shares (90%)
Greenshoe: *60,000,000* shares

Price: HK$2.10 – HK$3.10 per share

Market Cap: HK$3.36 billion – HK$4.96 billion

Pro forma fully diluted FY09E P/E: 10.6x – 15.6x

Company guidance on FY09E net profit:
not less than RMB279 million

Adjusted NTA per share: HK$0.59 – HK$0.83

Staffing: 1,750 (as of 23rd September 2009)

HK Public Offer period:
30th September 2009 – 6th October 2009 noon

Receiving bank: Standard Chartered (HK)

Share registrar: Tricor Investor Services Ltd.

Listing date: 13th October 2009

Business of Shenguan Holdings

The Group is mainly engaged in the manufacture and sale of edible collagen sausage casing products in the Mainland. According to China Meat Association, the Group has been the largest manufacturer of edible collagen sausage casing products in the country from 2006 to 2008.

The Group's products are artificial sausage casings, made from cattle's inner skins and other auxiliary materials. The products can be classified into two main categories, namely Western-style sausage casings and Chinese-style sausage casings. The Group produces a comprehensive range of edible collagen sausage casing products under its "Shenguan" brand name, with different diameters (ranging from 16mm to 50mm) and thickness. The Group is also able to produce sausage casings in accordance with specific requirements and standards of its clients.

The Group currently operates two production bases in Wuzhou (梧州), Guangxi (廣西) province, with a total of 106 production lines and an aggregate annual output capacity of 2.417 billion metres of collagen sausage casings.

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

Rich Top Future – 65.45% owned by Chairman Ms. Zhou Yaxian, 20.84% by Mr. Low Jee Keong (a non-executive director) and 13.71% by Mr. Wei Cheng (a director of subsidiary Wuzhou Shenguan).	63.16%
Xian Sheng – 100% owned by Chairman Ms. Zhou Yaxian.	7.75%
Wealthy Safe – 100% owned by Mr. Low Jee Keong	2.47%
Cheng Sheng – 100% owned by Mr. Wei Cheng	1.62%
Public shareholders*	25.00%
	100.00%

Remark: (*) China Life Insurance (Overseas) Co. Ltd., wholly owned by China Life (HKEx: 02628)'s parent company, will act as a Cornerstone Investor in the Global Offering, subscribing US$12 million worth of the offer shares or about 2.24% of the enlarged share capital (assuming an issue price of HK$2.60 and the over-allotment option is not exercised) with a lock-up period of six months.

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Use of Proceeds

Net proceeds from the offer are estimated to be HK$966.4 million *(based on an offer price of HK$2.60, being the mid-point of the indicative price range and assuming the over-allotment option is not exercised)*

	HK$ million
For the development and expansion of production facilities in Wuzhou.	586.7
For the expansion of research and development capabilities and development of new products.	34.1
For the acquisition of new land sites.	79.6
For the repayment of bank loans	151.2
For the repayment of the outstanding amount due to Hong Kong Shenguan (owned by Chairman Ms. Zhou), C.T. Company (a marketing agent in South Africa) and Exceltech (owned by non-executive director Mr. Low Jee Keong)	18.2
General working capital.	96.6

Financial Highlights

	Year ended 31st Dec			6 months ended	
	2006	2007	2008	30th Jun 2008	30th Jun 2009
	RMB million	RMB million	RMB million	RMB million	RMB million
Turnover	178.3	259.3	454.1	194.5	317.2
Gross profit	102.6	136.2	250.1	109.7	196.4
Operating profit	87.3	116.1	222.5	97.0	167.0
Profit attributable to shareholders	**84.8**	**120.9**	**172.9**	**77.5**	**129.1**
Gross profit margin	*57.6%*	*52.5%*	*55.1%*	*56.4%*	*61.9%*
Operating profit margin	*48.9%*	*44.8%*	*49.0%*	*49.9%*	*52.6%*
Net profit margin	*47.6%*	*46.6%*	*38.1%*	*39.9%*	*40.7%*
	31/12/2006	**31/12/2007**	**31/12/2008**	**30/6/2008**	**30/6/2009**
Net debt to Equity	Net cash	25.0%	Net cash	N/A	14.6%

Strengths/Opportunities

- ✓ Thanks to solid economic growth and rising standard of living in the Mainland, the retail sales volume of processed meat products (including sausages) saw healthy growth with a CAGR of 12.7% during 2003-2008. For sausage alone, the retail sales volume grew at a CAGR of 14.3% during 2003-2008.
- ✓ Food safety is drawing much consumer attentions nowadays. With a high standard of quality control, the Group has established strong client relationship with well-known food processors like Yurun Group. For instance, the Group is accredited with ISO 9001:2000 Quality Management System and HACCP (regulated by the US Department of Agriculture) standards. Besides, the Group's products are also registered with the US Food and Drug Administration (FDA) for exports to the country.
- ✓ The Group plans to double its production capacity by lifting the number of production lines to 116 by the end of 2009 from 56 a year ago (76 by the end 1H09 and 106 by 23rd Sep 2009) to meet its client demand. In 2010, the Group plans to further boost its capacity by adding another 50 production lines or more than 40% to a total of 166 by the year-end. The aggressive expansion will help fuel the Group's growth momentum in the next couple of years.

Weaknesses/Threats

- × The Group has a high degree of customer base concentration, with the top five customers accounting for more than 60% of total revenue during the first half of 2009.
- × Shenguan's production facilities have been operating at nearly full capacity during the first half of 2009. In order to expand its business scale, the Group plans to increase the number of production lines by nearly two-fold to 166 by the end of 2010 from 56 as at the end of 2008. Nonetheless, there is no guarantee for the Group to fill up the planned new capacity with new orders and continue to operate at nearly full capacity.

Recommendation: Neutral

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