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Main Board H-share Listing – Research

四川新華文軒連鎖股份有限公司

Sichuan Xinhua Winshare Chainstore Co., Ltd. [Stock Code: 0811]

Sole Global Co-ordinator, Bookrunner, Sponsor and Lead Manager : BOCI Asia Limited

Sector : Retailing

Business : Distribution of textbooks & supplementary materials, operation of book & audio-visual products retail outlets and provision of ancillary services to publishers

Total H share offer: <u>369,400,000</u> H shares (33.5% of the enlarged share capital) Public Offer: 36,940,000 shares (10%) Placing: 332,460,000 shares (90%) Greenshoe: 55,410,000 shares	<u>Business of Sichuan Xinhua Winshare</u> Sichuan Xinhua Winshare ("Winshare") engages in 3 lines of businesses, namely, (i) operation of retail outlets for books and audio-visual projects; (ii) distribution of textbooks and supplementary materials; and (iii) provision of ancillary support and services to book publishers. Currently, Winshare is the sole distributor of non-government-subsidised textbooks and the general (equivalent to sole and exclusive) supplier of government-subsidised textbooks to primary and secondary schools, as well as a major distributor of supplementary education materials to students in Sichuan Province. Being the largest retail bookstore chain in Sichuan Province, the PRC, Winshare has 193 outlets, with total GFA of 111,086 m ² , comprising 2 chains under the self-developed brands " <i>WenXuan</i> " ("文軒") and " <i>Times Xinhua</i> " ("時代新華"). <i>WenXuan</i> sells a wide variety of books of general interest while <i>Times Xinhua</i> specialises in audio-visual products. Of the 193 outlets (182 self-operated stores and 11 franchise stores), 181 are <i>WenXuan</i> outlets and 10 are <i>Times Xinhua</i> stores locating in Sichuan Province while the remaining 2 are <i>WenXuan</i> outlets in Xi'an (Xi'an Book City "西安書城") and Chongqing (Chongqing Bookstore "重慶書店"), both under the " <i>Xinhua WenXuan</i> " ("新華文軒") brand.
Price: HK\$4.50 – HK\$5.80 per H share H-share Market Cap: HK\$1,662 million – HK\$2,143 million Historical fully-diluted 2006 P/E: 16.4x – 21.1x Adjusted NTA per share: HK\$2.50 – HK\$2.91 Staffing: 5,728 (as of 31 st December 2006)	
Bookbuilding Period: 14 th May 2007 – 22 nd May 2007 HK Public Offer period: 16 th May 2007 – 21 st May 2007 noon Receiving bank: Bank of China (Hong Kong) Share registrar: Computershare Hong Kong Investor Services Limited Listing date: 30 th May 2007	

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

Sichuan Xinhua Publishing Group	54.028%
Chengdu Hua Sheng Group (90% owned by Mr. Wu Qing, a non-executive director of the Company)	4.837%
Sichuan Publication Group	2.201%
Sichuan Daily Newspaper Group	0.858%
Sichuan Youth and Children	0.629%
Liaoning Publication Group	0.600%
The National Council for Social Security Fund of the PRC	3.350%
Public shareholders	33.497%
	<u>100.000%</u>

Use of Proceeds

Net proceeds from the offer are estimated to be HK\$2,011.9 million (Assuming the over-allotment option is not exercised, and at an issue price of HK\$5.80 each, being the top end of the indicative price range)

	HK\$ million
For the expansion of retail network	568.1
For the strengthening of existing distribution network within Sichuan Province and the expansion of distribution network outside Sichuan Province	688.8
For the establishment of a nationwide wholesale network	86.1
For the enhancement of diversity of co-operative products by way of co-operation with or acquisition of publishing entities related to ancillary support and services business as well as development of co-operative products	172.2
For the establishment of regional logistics centres which, collectively, will form a national logistics network to support the Zhongpan operation	344.4
For the development of Enterprise Resource Planning (ERP) information system	51.7
For general working capital	100.6

Financial Highlights

	Year ended 31 st December		
	2004 RMB million	2005 RMB million	2006 RMB million
Revenues	2,084.8	2,262.6	2,217.6
Gross profit	790.5	820.4	850.1
Operating profit	304.2	343.8	299.9
Net profit	202.3	273.7	302.8
Gross margin	37.9%	36.3%	38.3%
Operating margin	14.6%	15.2%	13.5%
Net margin	9.7%	12.1%	13.7%

Revenue Breakdown (% of Total Revenues) and Gross Margin

	Revenue Breakdown			Gross Margin		
	Year ended 31 st December			Year ended 31 st December		
	2004	2005	2006	2004	2005	2006
Textbooks	50.3%	50.3%	49.9%	31.5%	32.2%	33.7%
Supplementary materials	32.8%	32.8%	33.3%	49.6%	43.9%	49.2%
Distribution	83.1%	83.1%	83.2%	38.6%	36.9%	39.2%
Retailing	14.5%	14.5%	14.1%	35.1%	33.6%	33.3%
Others*	2.4%	2.4%	2.6%	27.2%	28.6%	20.1%
Total	100.0%	100.0%	100.0%	37.9%	36.3%	38.3%

Remark (*): Including inter-segment

Strengths/Opportunities

- ✓ According to China Statistical Data Collection of Press and Publication 2006, Sichuan Province, in which Winshare has the dominant leadership position, was ranked the 4th top book-selling province in 2005 in terms of total net sales of RMB2,547.2 million, representing approximately 5.2% of the national total.
- ✓ As a member of the Xinhua Bookstores family, it enjoys the benefits of a reputable brand name with a long history. Its self-developed brands – *WenXuan* and *Times Xinhua* – are well recognised in Sichuan Province. In addition, Winshare has a strong balance sheet, with net cash of RMB858 million as of 31st December 2006 and RMB785 million as of 31st March 2007. Given its solid brand name and strong cash flow, Winshare is well positioned to expand outside Sichuan Province and to become a beneficiary of the consolidation of the book retailing market in China.
- ✓ Winshare intends to pay out approximately 15%-30% of its net profit as dividends.
- ✓ There is no real direct comparables as Winshare will be the first Chinese book distributor & retailer to be listed in Hong Kong. To be priced at 16.4x-21.1x FY2006 P/E, Winshare's valuation looks cheap when comparing with its Shanghai-listed A-share cousin Shanghai Xinhua Media (stock code: 600825.SS), which is trading at 531x FY2006 P/E or 93.7x FY2007E P/E. However, it should be noted that the premium valuation tagged on Shanghai Xinhua Media, as on other A shares, is partly liquidity-driven and due to its more retail-focused business model.

Weaknesses/Threats

- × For the textbook distribution business, Winshare currently has no competitors in respect of non-government-subsidised textbooks and government-subsidised textbooks for primary & lower secondary schools in Sichuan Province given its exclusive distribution rights won through tenders in these 2 sub-segments that will expire after the spring term 2008 and autumn term 2007 respectively. Meanwhile, Winshare's sole distributorship for non-government-subsidised textbooks for upper secondary schools in Sichuan Province is not covered by the public tender process. However, should Winshare fail to renew the sole distributorship rights and/or the government extend the tender system to upper secondary school textbooks, its textbook distribution business, which accounted for 53.3% of its total revenues for FY2006, and hence its overall operation results will be negatively affected.
- × Currently, Winshare's business is substantially derived from one single geographical area – Sichuan Province, although it has plans to extend its reach to other provinces in China.
- × Major threat to Winshare's retail business is the entry of foreign players who are financially stronger and are more sophisticated in marketing, management and risk control. These international players can offer a broader range of products and services to their customers that may not be matched by Winshare.
- × Being a threat to all booksellers worldwide, increased use of online book shopping and e-books may dampen sales of printed books at Winshare's retail outlets.

Recommendation: Neutral

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