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HONG KONG RESEARCH**8th February 2007****Analyst: Kelvin Li****Main Board Listing – Research****China Huiyuan Juice Group Limited [Stock Code: 1886] 中國匯源果汁集團有限公司****Sole Global Coordinator, Sole** : UBS**Bookrunner and Sole Sponsor****Joint Lead Managers** : UBS

Guotai Junan Securities (Hong Kong) Limited

Sector : Food, Beverage & Tobacco**Business** : Production of fruit and vegetable juices in China

Total share offer: <u>400,000,000</u> shares (26.3%* of the enlarged share capital)	<u>Business of Huiyuan Juice</u> Huiyuan Juice (“the Company”) is the leading producer of fruit and vegetable juices in the PRC in terms of revenue and sales volume. Major products include fruit juice, vegetable juice, mixed fruit and vegetable juices and other beverages. Huiyuan’s products can be divided into 3 categories, namely 100% juices, nectars (25%-99% juices), juice drinks (<25% juice). In 2006, the Company grasped some 40% share on the Mainland’s 100% juice market, 37.6% in the nectar market and 6.4% in the PRC juice drinks market. Huiyuan’s production facilities are operated through 11 subsidiaries in China, with an aggregate annual production capacity of 1.46 million tons of juices and other beverages. As of 30 th Sept 2006, the Company has about 1,800 distributors across all provinces, autonomous regions and municipalities in China.
Public Offer: 40,000,000 shares (10%) Placing: 360,000,000 shares (90%) Greenshoe: 60,000,000 shares	
Price: HK\$4.80 – HK\$6.00 per share Market Capitalisation: HK\$7,505.9 million – HK\$9,129.8 million Pro-forma FY2006E P/E: 37.5x – 45.6x Adjusted NTA per share: HK\$1.99-HK\$2.58 Staffing: 5,213 (as of 30 th September 2006)	
HK Public Offer period: 8 th February 2007 – 13 th February 2007 noon Receiving bank: BOC (Hong Kong), Bank of Communications HK Share registrar: Computershare Hong Kong Investor Services Limited Listing date: 23 rd February 2007	

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

Mr. Zhu Xinli – executive director, chairman and founder of the Company	40.1%
Mr. Zhu Shenghua – son of Mr. Zhu Xinli	2.6%
Danone Asia (Singapore)	22.2%
Warburg Pincus	6.6%
Other bondholders – including Value Partners Investors and Development Partners Investors	2.0%
Mr. Lu Changqing – executive director and a joint company secretary of the Company	0.1%
Public shareholders – including shares belonging to 4 members of the Company's senior management team from the exercise of the options granted under the Pre-IPO Share Option Scheme	26.5%*
	100.0%

Remark (*): It is based on the 1,521,629,855 shares to be issued upon the completion of the Global Offering and exercise of the Danone Top-up Right, and assuming full conversion of the Convertible Bonds and full exercise of the options granted under the Pre-IPO Share Option Scheme at the high end of the indicative price range.

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Use of Proceeds

Net proceeds from the offer are estimated to be HK\$1,807.7 million – HK\$2,254.0 million.

(Assuming the over-allotment option is not exercised, and at an issue price of HK\$4.8-HK\$6.0 each)

	Offer price at HK\$4.8	Offer price at HK\$6.0
	HK\$ million	HK\$ million
To construct new manufacturing facilities	632.7	788.9
For expanding and upgrading Huiyuan's sales and distribution network and for marketing and promotional activities	632.7	788.9
To repay existing short-term debts	271.1	338.1
For equipment upgrade at Huiyuan's existing facilities	90.4	112.7
For general working capital	180.8	225.4

Financial Highlights

	Year ended 31 st December			9 months ended	
	2003	2004	2005	30 th Sep 2005	30 th Sep 2006
	RMB million	RMB million	RMB million	RMB million	RMB million
Sales	130.1	1,158.6	1,392.1	1,145.5	1,598.5
Gross profit	33.1	406.0	474.2	402.4	523.0
Operating profit	1.6	128.6	180.8	164.0	235.7
Attributable profit	-13.8	18.3	107.5	111.1	185.8
Gross margin	25.44%	35.04%	34.06%	35.13%	32.72%
Operating margin	1.23%	11.10%	12.99%	14.32%	14.75%
Net profit margin	-10.61%	1.58%	7.72%	9.70%	11.62%
	31/12/2003	31/12/2004	31/12/2005	30/06/2005	30/06/2006
Net debt to Equity	94%	82%	46%	N/A	45%

Sales Volume Breakdown

	Year ended 31 st December						9 months ended			
	2003		2004		2005		30 th Sep 2005		30 th Sep 2006	
	Tons	%	Tons	%	Tons	%	Tons	%	Tons	%
100% Juice	5,367	16	40,588	12	55,091	12	40,715	11	52,456	10
Nectars	14,797	45	169,261	48	170,034	39	128,748	36	215,935	42
Juice drinks	12,847	39	142,685	40	214,723	49	189,766	53	244,437	48
Total	33,011	100	352,534	100	439,848	100	359,229	100	512,828	100

Average Selling Price of Huiyuan's Products

	Year ended 31 st December						9 months ended 30 th September		
	2003	2004	2003-2004		2005	2004-2005	2005	2006	Y-O-Y
	RMB/ton	RMB/ton	% CHG		RMB/ton	% CHG	RMB/ton	RMB/ton	% CHG
100% Juice	6,073	5,463	-10.0		5,439	-0.4	5,593	5,665	+1.3
Nectars	3,299	2,759	-16.4		2,861	+3.7	2,868	3,046	+6.2
Juice drinks	3,192	2,358	-26.1		2,219	-5.9	2,269	2,271	+0.1

**Strengths/Opportunities**

- ✓ Thanks to the fast growing Chinese economy and rising concerns over health issues, the demand for fruit and vegetable juices on the Mainland has been growing rapidly. According to statistics from *Euromonitor International*, sales volume of fruit and vegetable juices grew at a CAGR of 19.9% during 2000-2005, compared with a 14.4% CAGR in bottled water sales and 25.4% in that of ready-to-drink tea products. Besides, the statistics showed that the growth rate of fruit and vegetable juices was the highest among major drinking products during 2003-2005.
- ✓ Market penetration in respect of fruit and vegetable juice in China is still low and strong growth potential is expected. The annual consumption of fruit and vegetable juices per capita in the Mainland is just about 3.4 litres in 2005, compared with Russia's 16.5 litres and Mexico's 12.5 litres. It is expected that the off-trade sales of fruit and vegetable juices in the Mainland should grow from RMB40.5 billion in 2005 to RMB67.1 billion in 2010, representing a CAGR of 10.6%.
- ✓ According to data from *AC Nielsen*, Huiyuan is a market leader in terms of revenue in the 100% juices and the nectars markets of China. For the first 9 months of 2006, Huiyuan ranked 1st in the Mainland's 100% juices market in terms of revenue with a 36.1% share and also 1st in the nectars market with a 37.3% share.
- ✓ Huiyuan has about 1,800 distributors across all Mainland provinces, autonomous regions and municipalities. This extensive sales network should help promote the Group's products efficiently and should ensure effective marketing effort with distributors' local knowledge about consumers.

Weaknesses/Threats

- × Juice drinks (<25% juice) was the fastest growing and largest segment in China's juice and vegetable juices market in terms of revenue. At the moment, Huiyuan just grasped a small market share of 6.4% and ranked 4th in the industry during the first 9 months in 2006, while the top three players snatched more than 75% of market share during the same period. Owing to its small size in the market segment, Huiyuan experienced severe rivalry and saw sluggish movement in the average selling price of its juice drinks over the past 3 years.
- × According to the listing documents, Huiyuan is expected to post a net profit of RMB222 million in 2006 and RMB300 million in 2007, representing 34x-41X FY2006E pro-forma P/E and 25x-30x FY2007E P/E at the indicative price range. Huiyuan's valuation is in line with other Mainland beverage plays like Mengniu Dairy (HKEx: 2319) and Tingyi (HKEx: 0322) with FY2007E P/E at 35x and 33x, respectively. However, we see bargains in other domestic juice manufacturers like China Haisheng Juice (HKEx: 0359) and Yantai North Andre Juice (HKEx: 8259) with 2007 prospective price-earnings multiple ranging from 11x to 15x.

Recommendation: Trading Buy



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