

JPM-pp1

Asia Pacific Equity Research

16 March 2015

Uni-President China Holdings Ltd (220 HK)

Neutral

Price: HK\$5.57

13 Mar 2015

Price Target: HK\$5.50

PT End Date: 31 Dec 2015

FY14 Preview - Reporting on 17 March 2015

Uni-President China is expected to report its FY14 result on 17 March, 2015 after market close. The company will hold its briefing around 2:30pm on 18 March, 2015, Hong Kong time.

- Beverage to be a drag in 2H while noodles profitability likely improved:** We expect UPC to report RMB6mn net profit in 2H14 vs a net loss of RMB5mn in 3Q14 and RMB355mn net profit in 1H14. 2H14 results are likely to show some improvement in noodles margin due to fewer promotions in the last two months of the year but we expect beverage margins to be under pressure due to weak sales. We however previously tweaked up our FY15 estimates by c5% as we modelled low PET costs to benefit the beverage segment slightly. Share price has corrected c15% (vs HIS +3%) since our last cut in estimates in Nov 2014, but the stock is still trading at demanding multiples in our view with 35x 15E and 24x 16E on our numbers which: i) already build in a very optimistic scenario for the new noodles product, and ii) better beverage margins with the help of low PET costs. We believe success of Gemian is still uncertain and even if successful as we have seen in the past, we are likely to see the major competitor coming up with a similar product, taking away some market share. We remain Neutral given strong earnings turnaround expected in FY15 which we think is in the price.
- 2H14 preview:** We expect sales to be down 1% y/y in 2H14 mainly dragged by the lackluster beverage segment (-6.3% y/y) while we expect noodles sales to be up 4% y/y. With the ASP increase and the removal of the free sausage campaign in 4Q we are looking for improvement in noodles gross margin in 2H14 but given weak beverages sales we expect to see beverage margins under pressure. We expect noodles margin recovery to be more notable in FY15 and start pulling up consolidated earnings. We expect UPC to report RMB6mn net profit in 2H14 vs a net loss of RMB5mn in 3Q14 and RMB355mn net profit in 1H14.
- Major issues to focus on during the results briefing:** 1) Sales momentum in beverages and new product introduction given that beverage segment is the key for UPC accounting for 60% of sales and more than 90% of earnings, 2) Performance of new Gemian noodles, 3) Promotion plans if any on both beverage and noodles.

Table 1: JPM's estimates for UPC's 2H14E and FY14E results

USDmn	2H13	2H14E	% chg y/y	FY13	FY14E	% chg y/y
Sales revenue	11,125	11,032	-0.8%	23,329	23,399	0.3%
COGS	(7,490)	(7,640)	2.0%	(15,549)	(15,987)	2.8%
Gross profit	3,635	3,392	-6.7%	7,780	7,412	-4.7%
Gross margin	32.7%	30.7%		33.3%	31.7%	
Other income	585	254	-56.6%	949	328	-65.5%
as % of sales	5.3%	2.3%		4.1%	1.4%	
Total operating expenses	(3,908)	(3,716)	-4.9%	(7,796)	(7,394)	-5.2%
as % of sales	-35.1%	-33.7%		-33.4%	-31.6%	
EBIT	312	-70	-122.4%	932	346	-62.9%
EBIT margin	2.8%	-0.6%		4.0%	1.5%	
Interest income	81	79	-2.2%	179	124	-31.0%
Interest expenses	-46	-120	157.9%	-84	-228	171.6%
Associates	40	119	195.7%	88	221	150.0%
Pretax profit	387	8	-97.9%	1,116	463	-58.5%
Tax	-45	-2	-96.3%	-200	-101	-49.5%
Effective tax rate	-11.7%	-20.8%		-17.9%	-21.8%	
Net profit	342	6	-98.1%	916	362	-60.5%
Net margin	3.1%	0.1%		3.9%	1.5%	

Source: Company reports. Source: Company data, Bloomberg and J.P. Morgan estimates.

Table 2: Revenue, Gross Profit and EBIT breakdown by product category

USDmn	2H13	2H14E	% chg y/y	FY13	FY14E	% chg y/y
Revenue Breakdown						
Beverage						
Instant noodles	6,890	6,459	-6.3%	15,152	14,551	-4.0%
Others	4,049	4,228	4.4%	7,826	8,168	4.4%

Total	186	344	85.3%	352	680	93.4%
	11,125	11,032	-0.8%	23,329	23,399	0.3%
Gross profit breakdown:						
Beverage						
Instant noodles	2,458	2,133	-13.2%	5,424	5,046	-7.0%
Others	1,137	1,203	5.8%	2,285	2,263	-1.0%
Total	40	56	42.1%	70	103	47.1%
	3,635	3,392	-6.7%	7,780	7,412	-4.7%
EBIT breakdown						
Beverage						
Instant noodles	98	-13	-112.9%	597	608	1.8%
Others	-82	19	-122.5%	-143	-98	-31.6%
Total	296	-76	-125.6%	478	-164	-134.3%
	312	-70	-122.4%	932	346	-62.9%
Gross margin breakdown						
Beverages						
Instant noodles	35.7%	33.0%		35.8%	34.7%	
Total	28.1%	28.5%		29.2%	27.7%	
	32.7%	30.7%		33.3%	31.7%	
EBIT margin breakdown						
Beverage						
Instant noodles	1.4%	-0.2%		3.9%	4.2%	
Total	-2.0%	0.4%		-1.8%	-1.2%	

Source: Company reports. Source: Company data, Bloomberg and J.P. Morgan estimates.

Investment Thesis

We recently tweaked up our FY15 estimates by c5% as we modelled low PET costs to benefit the beverage segment slightly. The share price has corrected c15% (vs HSI +3%) since Nov 2014, but the stock is still trading at demanding multiples in our view with 35x 15E and 24x 16E on our numbers which: i) already build in a very optimistic scenario for the new noodles product, and ii) better beverage margins with the help of low PET costs. We believe success of Gemian is still uncertain and even if successful as we have seen in the past, we are likely to see major competitors coming up with a similar product, taking away some market share. We remain Neutral given the strong earnings turnaround expected in FY15, which we think is in the price.

Valuation

Our Dec-15 PT of HK\$5.5 is based on P/E of 21x one year forward earnings, which is 1-standard deviation below the average P/E. The PT cut is mainly driven by multiple change.

Risks to Rating and Price Target

Key upside and downside risks to our rating and price target include: 1) the successful launch of new products, and 2) the promotional environment unexpectedly getting better/worse with competitors cutting back on promotions.

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<http://gps-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=1002710&shareClassServerId=4&chartDesignation=1&actionType=C>

Date	Rating	Share Price (HK\$)	Price Target (HK\$)
25-Mar-09	OW	2.42	3.50
21-Jun-09	N	3.94	3.50
28-Aug-09	N	4.45	4.70
01-Feb-10	N	4.73	5.00
27-Apr-10	UW	4.57	4.40
23-Aug-10	UW	4.48	4.00
07-Sep-11	N	4.36	4.50
12-Oct-11	N	4.34	4.20
19-Feb-12	N	4.78	4.00
05-Jun-12	UW	6.61	5.00
27-Aug-12	UW	7.46	5.80
10-Oct-12	UW	9.57	6.80
16-Jan-13	N	9.20	8.30
26-Mar-13	N	8.59	8.00
09-Aug-13	N	7.05	6.50
20-Mar-14	UW	7.86	4.00
26-Jul-14	UW	6.61	3.50
24-Sep-14	N	7.31	6.50
25-Nov-14	N	7.24	6.00
25-Feb-15	N	6.20	5.50

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Tsingtao Brewery - H (0168.HK), Uni-President China Holdings Ltd (0220.HK), Want Want China Holdings Ltd (0151.HK)

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