

Fu Shou Yuan International

Company Visit Note

We visited Fu Shou Yuan International Ltd recently.

What does the company do?

Founded in 2004, FSY is the largest provider of death care services in the PRC in terms of revenue, with branches in nine provinces, including Shanghai, Chongqing and Xiamen. It operates two main businesses, burial and funeral services. In FY14, Fu Shou Yuan sold a total of 10,093 tombs and provided 12,692 funeral services.

What's new?

- FSY achieved 30% sales growth in 2014, more than double the growth of the overall market. The company has a strategy to limit sales of cemetery plots because the unit ASP is rising 10-15% each year.
- FSY sold 21k sqm of plots for 2014, but has over 1.56m of land available for immediate sale, with another 1.8m in land identified for future conversion to land that could be sold after payment of a government fee.
- FSY is an active market consolidator, making four acquisitions in 2014. The company plans to leverage off its national premium brand in order to acquire small individual operators and also manage third-party cemeteries.

Financials: FSY reported FY14 revenues of RMB795.1mn, up 30% y/y, with a GPM of 80% (80% in 1H13) and a net profit margin of 29% (27% in 1H13). The stock is trading at 18.13x FY15 P/E based on Bloomberg consensus estimates.

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Fu Shou Yuan Int'l (Reuters: 1448.HK, Bloomberg: 1448 HK), Historical financial data

Rmb m, year-end Dec	2010	2011	2012	2013	2014
Sales	350	421	480	612	795
% YoY growth	na	20%	14%	27%	30%
EBITDA	161	181	209	299	299
EBITDA margin	46%	43%	44%	49%	38%
Net profit	104	131	124	167	230
EPS	0.00	0.00	0.00	0.10	0.11
EPS growth (%)	na	n.a	n.a	n.a	n.a
DPS	0.00	0.00	0.00	0.00	0.02
EV/EBITDA (x)	44.0	38.2	33.1	22.4	17.3
P/E (x)	n.a	n.a	n.a	27.7	25.2
P/BV (x)	n.a	n.a	n.a	3.5	3.1

Source: Bloomberg

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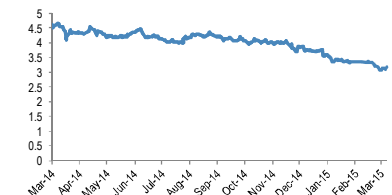
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1448 HK, Not Covered

HK\$3.07, 23 Mar 2015



Source: Bloomberg

One-year price performance

	1M	3M	12M
Absolute (%)	3	(9)	(25)
Relative (%) - HSCEI	3	(13)	(49)

Source: Bloomberg

Company data

52-wk range (HK\$)	2.95-4.59
Mkt cap. (HK\$ B)	7,076
Mkt cap. (US\$ MM)	907
Shares O/S (MM)	2,075.0
Free float (%)	23%
Avg. daily volume	1.5
Liquidity (HK\$ MM)	0.7
Exchange rate	6.30
Index	12,030
Year-end	Dec

Source: Bloomberg

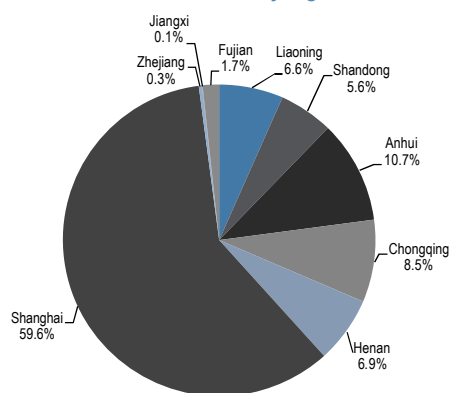
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Company Profile

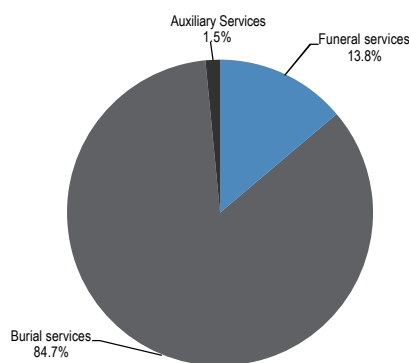
Founded in 2004, FSY is the largest provider of death care services in the PRC in terms of revenue and geographical coverage with branches in nine provinces, including Shanghai, Chongqing and Xiamen. It operates two main businesses, burial and funeral services. In FY14, Fu Shou Yuan sold a total of 10,093 tombs and provided 12,692 funeral services. Key shareholders include FSG Holdings (25.3%) and Chief Union Investment (23.3%).

Figure 1: Revenue breakdown by region



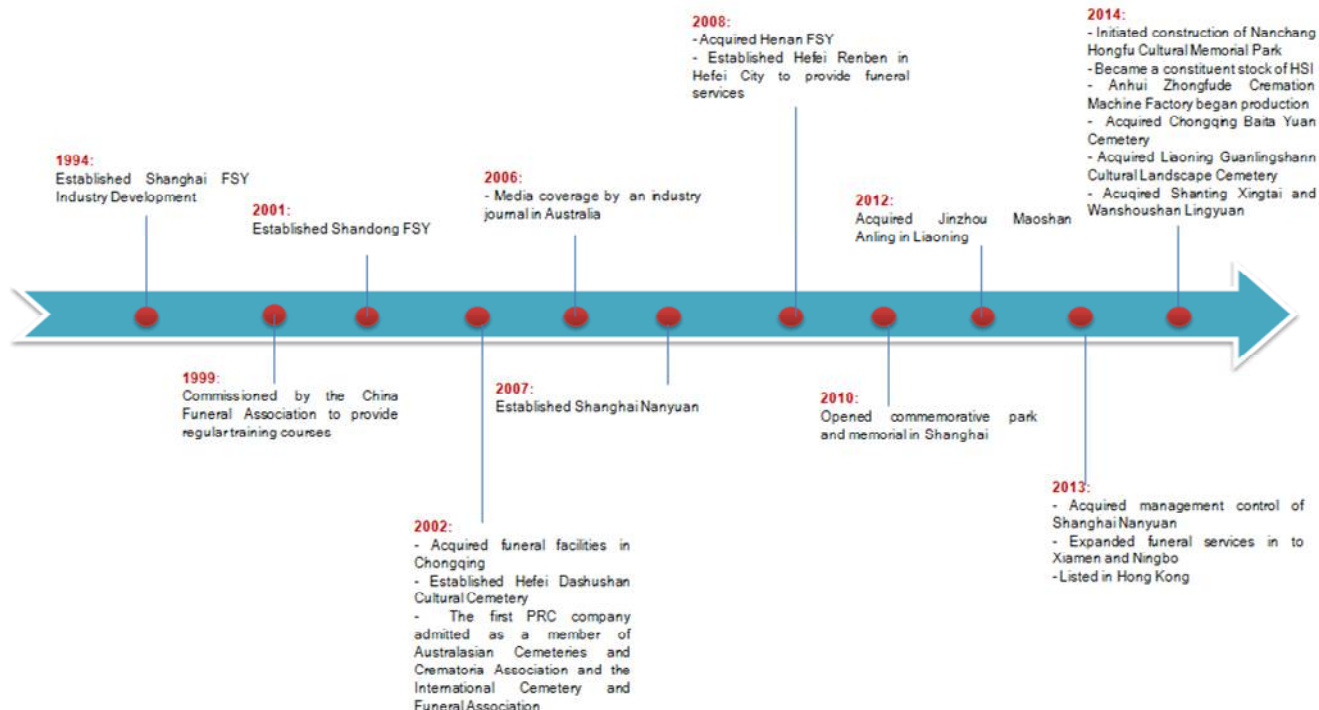
Source: Company data

Figure 2: Revenue breakdown by service



Source: Company data

Figure 3: Company key milestones



Source: Company reports

FSY has achieved many awards in industry, such as Famous Trademark of Shanghai, Top 10 Most Valuable Asian Brands, Provincial Demonstration Unit for Death Care Services Reform in Shanghai, etc.

Shanghai Fu Shou Yuan enjoys a convenient location. It is only a 20 minute drive from Shanghai Hong Qiao Airport.

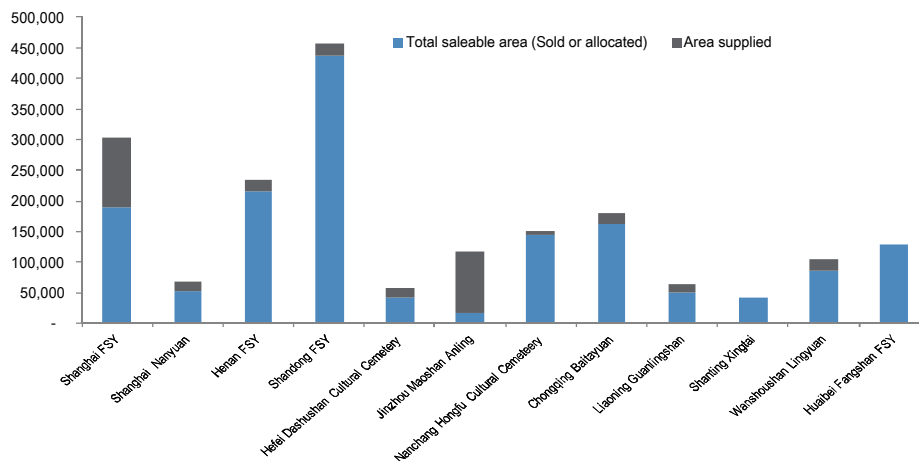
Figure 4: Shanghai FSY and associated constructions



Source: Company reports

Apart from Shanghai, FSY has continued to focus on product development and brand building over past years and it has grown its business via expansion and acquisitions. The company has ample landbank to support future business development for at least the next 20 years, according to management. As of Dec 31, 2014, the company supplied 20,691 sq.m of land and had an aggregate saleable area of 3,489,384 sq.m remaining (including an area of 1,566,604 sq.m with land use right certificates) to support development.

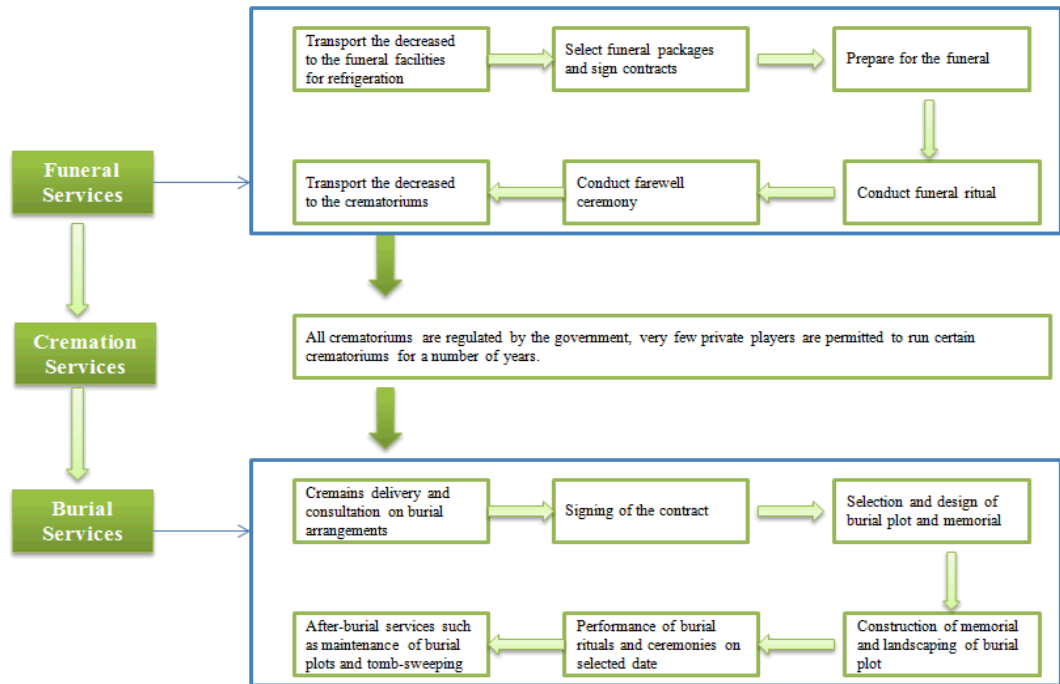
Figure 5: Saleable and taken up area by cemeteries



Source: Company data

FSY is one of the largest providers in China offering full vertically integrated death care services, from funeral services to cremation and burial services. Usually all crematoriums are regulated by the government and very few private players are permitted to carry out such business. Thanks to the 60% equity acquisition of Chongqing Baita Yuan in 2014, the only private crematorium provider approved by the government, FSY successfully managed to enter this business.

Figure 6: Basic process for China's death care services industry

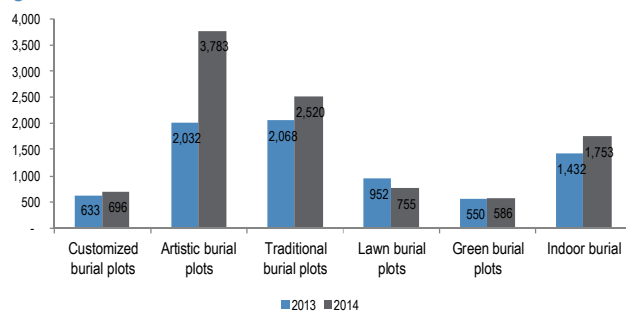


Source: Company reports

Burial Services (84.7% of FY14 revenue)

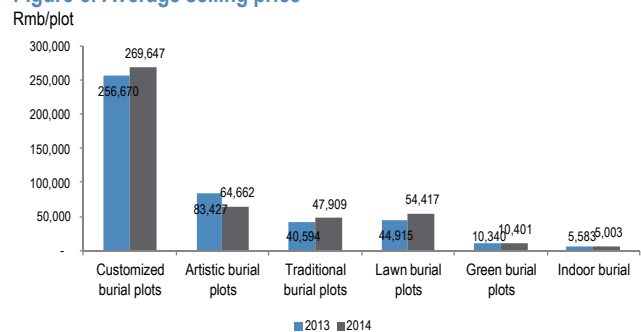
The burial services include a range of customization options, such as selection of a particular landscape, different style of plots, etc. and FSY generates revenue mainly from sales of plots. There are six types of burial plots in FSY. Customized and artistic burial plots are the primary revenue drivers with relatively higher ASPs.

Figure 7: Number of units









Source: Company data

Figure 8: Average selling price



Source: Company data

Figure 9: Six types of burial plots

Type of burial plots	Selected plots	Type of burial plots	Selected plots
Customized burial plot		Lawn burial plot	
Artistic burial plot		Traditional burial plot	
Green burial plot		Indoor burial plot	

Source: Company website

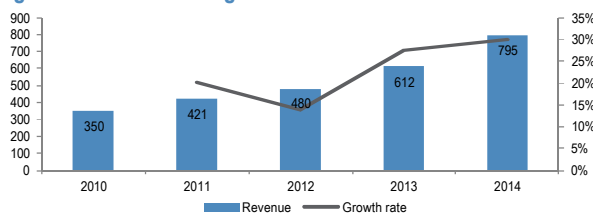
Funeral Services (13.8% of FY14 revenue)

FSY generates revenue from planning, organizing and conducting funerals. The whole process may include transportation to the funeral facilities, performance of religious rituals and ceremonies, etc.

Business Overview

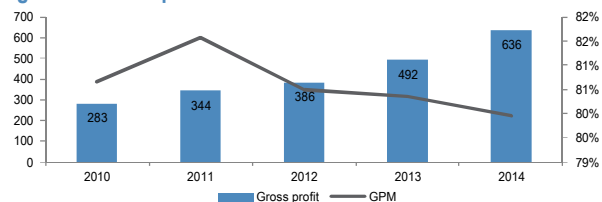
FSY delivered a strong and solid performance in FY14. The top line achieved 30% y/y growth to RMB795mn thanks to 28.5% y/y growth in burial services and a 24.5% y/y increase in funeral services via expansion and acquisitions. Auxiliary services are a new revenue driver, which reported RMB11.9mn in FY14. The cost of services increased by 32.5% in 2014 to RMB159mn due to a 27.0% increase for burial services, a 16.9% increase for funeral services, and a 100% increase for auxiliary services. Gross profit reported 28.9% y/y growth to RMB634mn due to its premium marketing position, pricing power and strong cost control. GPM is still stable at around 80% (burial services at 82.2%, funeral services at 72.7% and auxiliary services at 20.7%). Net profit reported a 37.7% y/y rise to RMB230mn, thanks to strong revenue growth in existing business as well as lower effective corporate income tax, which well offset the increase in operating expenses.

Figure 10: Revenue and growth rate



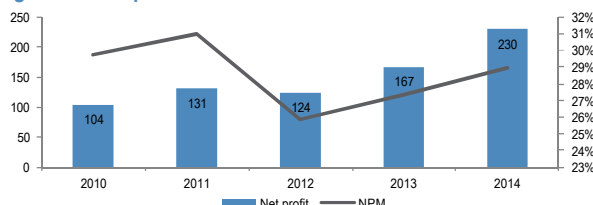
Source: Company reports

Figure 11: Gross profit and GPM



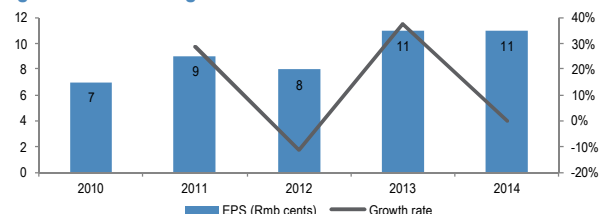
Source: Company reports

Figure 12: Net profit and NPM



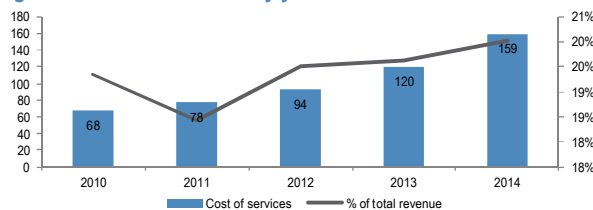
Source: Company reports

Figure 13: EPS and growth rate



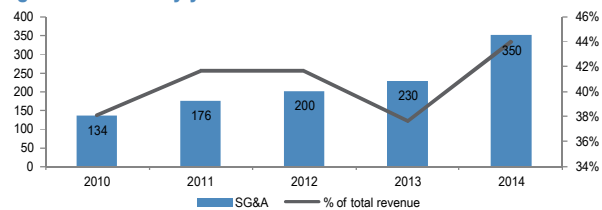
Source: Company reports

Figure 14: Cost of services by year



Source: Company reports

Figure 15: SG&A by year



Source: Company reports

Table 4: Company annual result

Annual Result (RMB mn)	FY14	FY13	Growth
Total Revenues	795	612	29.9%
Gross Profit	634	492	28.9%
EBIT	345	266	29.8%
Net Income Before Taxes	341	260	31.2%
Net Income	230	167	37.7%
Diluted EPS (RMB cent)	11	11	0.0%

Source: Company data

Business Outlook

- Stable high margins.** The company has been achieving a high level of GPM near 80% and EBIT margin from 40-50% due to a high proportion of revenues related to cemetery plot sales. Most of the land is held at cost and sold at a current price which has been rising at nearly 10% a year. This results in a high GPM for plot sales and ancillary sales related to plot maintenance and funeral services tend to be quite high margin as well. This healthy level of margins is expected by management to continue as demand is strong and competition is limited in most markets.

- **High growth is by design.** While the 30% annual sales growth CAGR over the past few years is impressive in many other industries, FSY is actually actively curtailing the number of plots that it sells in order to benefit from selling plots at a higher price in future. The company believes there is strong underlying demand and that allows them to be able to grow consistently at around 30% a year.
- **Large land bank still expanding.** The company has sufficient landbank (with government certificates for immediate sales) to satisfy over 60 years of sales (at 2014 levels) and is still looking to expand this landbank through expansion of existing sites (and payment of a fee to the government), buying competing cemeteries or starting new cemeteries.
- **Predictable maintenance fees.** About 12% of 2014 sales are related to maintenance fees that existing customers pay to maintain their plots. These sales are recurrent and predictable and are growing each year as FSY sells more plots.
- **More service related income targeted.** FSY is also looking to manage third-party cemeteries for a management fee as well as lift the proportion of its sales for ancillary funeral services.

Financials

As of Dec 31, 2014, the company had total interest-bearing borrowings of RMB35mn which are wholly repayable within one year. The group's net gearing ratio was 4.3% in FY14 thanks to its good operating cash generating capability. The company's cash and cash equivalents amounted to RMB1,296.8mn, which comes primarily from net proceeds of the global offering of new shares. Its capex for FY14 was RMB111.6mn (RMB74.5mn as of Dec 31, 2013). The stock is trading at 18.13x FY15 P/E based on Bloomberg consensus estimates.

Fu Shou Yuan Int'l: Historical financial summary

Income statement

Rmb in millions, year-end December

	2,012	2,013	2,014
Revenue	480	612	795
% change Y/Y	14%	27%	30%
Gross margin (%)	80%	80%	0%
EBITDA	209	299	299
% change Y/Y	15%	43%	0%
EBITDA margin (%)	44%	49%	38%
EBIT	189	271	286
% change Y/Y	13%	43%	5%
EBIT margin (%)	39%	44%	36%
Net interest	11	5	4
Earnings before tax	195	260	341
% change Y/Y	0	0	0
Tax	56	70	56
as % of EBT	30%	26%	20%
Net income (reported)	124	167	-
% change Y/Y	6%	60%	-100%
Shares O/S (MM)	-	1,521	-
EPS (LC)	-	0.11	0.11

Source: Company reports

Cash flow statement

Rmb in millions, year-end December

	2,012	2,013	2,014
Net income	124	167	230
Depreciation & Amort.	20	28	28
Change in working capital	(1)	(76)	(76)
Taxes	56	70	56
Net interest	4	(3)	-
Cash flow from operations	193	154	154
Capex	(23)	(75)	(75)
Others	(12)	29	29
Cash flow from investing	(33)	(39)	(39)
Equity raised/(repaid)	-	1,216	1,216
Debt raised/(repaid)	1	(16)	(16)
Other	(17)	(26)	(26)
Dividends	(78)	(32)	-
Cash flow from financing	(94)	1,142	1,142
Beginning cash	222	287	-
Change in cash Flow	65	1,257	1,257
Ending cash	287	1,544	-
DPS (LC)	-	-	0.02

Source: Company reports

Balance sheet

Rmb in millions, year-end December

	2,012	2,013	2,014
Cash and cash equivalents	287	1,544	1,297
Accounts receivable	-	-	-
Inventories	111	183	216
Others	51	21	20
Current assets	449	1,748	-
LT investments	18	20	24
Net fixed assets	122	188	284
Total assets	1,035	2,468	2,935
Liabilities			
ST loans	51	39	35
Payables	43	51	92
Others	316	422	324
Total current liabilities	409	512	-
Long-term debt	49	38	-
Other liabilities	196	173	272
Total liabilities	654	723	-
Shareholders' equity	381	1,745	2,212
BVPS (LC)	-	0.79	-

Source: Company reports

Ratio analysis

%, year-end December

	2,012	2,013	2,014
EBITDA margin	43.6	48.8	37.6
Operating margin	39.5	44.3	36.0
Net profit margin	25.9	27.3	0.0
Opex/sales	41.7	37.6	44.0
Sales growth	13.9	27.5	30.0
Net profit growth	6.4	59.5	(100.0)
Sales per share growth	-	-	-
EPS growth	-	-	0.0
Interest coverage (x)	19.3	56.6	81.2
Gross debt to equity	41.0	4.9	-
Net debt to equity	(49.1)	(84.1)	(57.0)
Sales/assets	46.4	24.8	27.1
ROCE	98.7	24.5	20.7
Assets/equity (x)	425.9	156.2	-
ROA	13.2	9.5	8.5
ROE	98.7	24.5	20.7
Dividend payout ratio	-	0%	0%

Source: Company report

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