



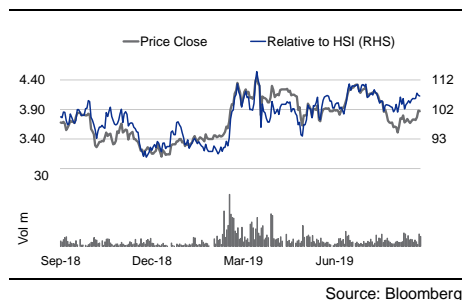
Hong Kong

ADD

Consensus ratings*:	Buy	Hold	Sell
Current price:			HK\$3.87
Target price:			HK\$4.70
Previous target:			N/A
Up/downside:			21.4%
CGI / Consensus:			na
Reuters:			
Bloomberg:		546 HK	
Market cap:		US\$1,256m	HK\$9,843m
Average daily turnover:		US\$1.14m	HK\$8.93m
Current shares o/s:		2,547m	
Free float:		42.7%	
*Source: Bloomberg			

Key changes in this note

➤ N/A



<b>Price performance</b>	1M	3M	12M
Absolute (%)	4.3	-1.3	5.2
Relative (%)	2.9	0.1	7.9

<b>Major shareholders</b>	% held
Li Xuechun, Chairman	46.3

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# Fufeng Group

## Strong MSG price in 2H19F

- Fufeng achieved core net profit growth of 94.5% yoy to Rmb613m in 1H19 because of a strong MSG price.
- We believe that the MSG market consolidation has been largely completed and that as the largest player, Fufeng should maintain a stable MSG price.
- Fufeng plans to construct railways in its two production plants to reduce costs in FY20F.
- We initiate coverage on Fufeng with an Add rating and a DCF-based target price of HK\$4.7. Its valuation of 7.44x FY19F and 6.44x FY20F PER looks attractive to us.

### Strong MSG price drove 1H19 results

Fufeng achieved sales growth of 16.5% yoy in 1H19 because of a strong MSG price. The MSG price was up by 22.7% yoy to Rmb7,161/t in 1H19, with sales volume dropping slightly by 8.3% YoY to 521kt. Xanthan gum maintained a flattish price yoy at Rmb14,898/t, with sales volume up by 12.5% yoy in 1H19. However, high-end amino acid sales fell by 3.9% yoy in 1H19 because the US tariff rate was increased to 25% from previously high single digits. Fufeng's GPM and OPM expanded by 4.7ppt and 3.6ppt YoY to 21.7% and 10.2% in 1H19, owing to the higher MSG price.

### MSG industry consolidation largely completed

We believe MSG market consolidation has been largely completed, and as the largest player, Fufeng should maintain a stable MSG price. We now expect Fufeng's MSG price to remain at Rmb7,019/t in 2H19F and its overall MSG GPM to expand by 4.3ppt yoy to 20.7% in FY19F. We forecast that Fufeng will achieve MSG sales volume of 1mt in FY19F, accounting for over 50% of China's MSG market share.

### Xanthan gum price remained stable

The global xanthan gum market was established in 1H19. We expect Fufeng's xanthan gum price to remain at Rmb14,923/t in 2H19F. However, we expect the xanthan gum segment GPM to contract by 5.0ppt YoY to 28% in FY19F because of increasing corn and coal prices. Corn and coal prices increased by 8.0% and 6.5% YoY in 1H19, and we expect these prices to remain stable in 2H19F.

### Measures to reduce costs

Fufeng plans to construct transportation facilities such as railways for raw materials and finished products for its Longjiang and Zhalantun plants to reduce costs. The railways will be completed in FY20F, which we expect to help save more than Rmb100m in coal costs and transportation expenses. We forecast that Fufeng's OPM will expand by 0.3ppt to 10.3% in FY20F.

### Initiate with ADD

We initiate coverage on Fufeng with an Add rating and a DCF-based TP of HK\$4.7 (equivalent to 7.5x FY20F PER), since we expect the MSG price to remain strong in 2H19F. We believe that the MSG market consolidation has been largely completed, and that Fufeng should maintain stable MSG prices and margins. Fufeng is trading at 7.44x FY19F and 6.44x FY20F PER, which looks cheap to us, compared to its average historical forward PER of 7.9x for the past five years. Fufeng's dividend yield of 4.0% and 4.7% for FY19F and FY20F also looks attractive to us. A positive catalyst is stronger-than-expected MSG prices. Downside risk is higher-than-expected raw material prices.

Financial Summary	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue (Rmbm)	13,034	13,765	15,494	17,442	18,678
Operating EBITDA (Rmbm)	2,606	2,144	2,809	3,092	3,260
Net Profit (Rmbm)	1,382	1,708	1,208	1,395	1,493
Core EPS (Rmb)	0.54	0.14	0.47	0.55	0.59
Core EPS Growth	5%	(74%)	240%	15%	7%
FD Core P/E (x)	6.50	25.31	7.44	6.44	6.02
DPS (Rmb)	0.16	0.22	0.14	0.16	0.18
Dividend Yield	4.61%	6.16%	4.03%	4.66%	4.98%
EV/EBITDA (x)	4.04	5.06	3.72	3.01	2.45
P/FCFE (x)	NA	NA	8.02	6.00	5.16
Net Gearing	16.4%	16.8%	12.5%	2.6%	(7.2%)
P/BV (x)	0.95	0.82	0.77	0.71	0.65
ROE	17.0%	3.5%	10.7%	11.5%	11.3%
% Change In Core EPS Estimates					
CGI/consensus EPS (x)					

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

## Strong MSG price in 2H19F

**Figure 1: Fufeng's 1H19 and 2H19F P&L breakdown**

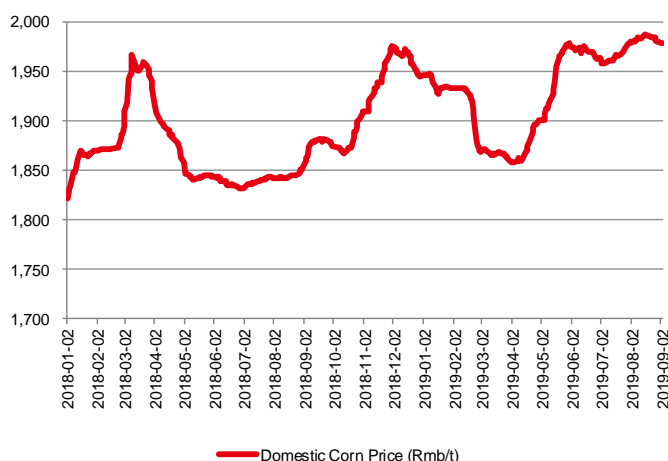
(Rmb m)	1H19	1H18	yoy	2H19F	2H18	yoy	FY19F	FY18	yoy
Total revenue	7,704	6,610	16.5%	7,790	7,154	8.9%	15,494	13,765	12.6%
Cost of sales	(6,030)	(5,489)	9.9%	(6,194)	(5,701)	8.6%	(12,224)	(11,190)	9.2%
Gross profit	1,673	1,121	49.2%	1,596	1,453	9.8%	3,269	2,575	27.0%
Gross margin	21.7%	17.0%	4.8ppt	20.5%	20.3%	0.2ppt	21.1%	18.7%	0.1ppt
Other operating income	153.514	131	17.0%	46	133	-64.9%	200	264	-24.2%
Distribution costs	(603)	(535)	12.6%	(555)	(507)	9.4%	(1,157)	(1,042)	11.1%
Distribution costs as % of net sales	7.8%	8.1%	0.0ppt	7.1%	7.1%	0.0ppt	7.5%	7.6%	0.0ppt
General and administrative expenses	(393)	(254)	54.8%	(332)	(404)	-17.8%	(726)	(659)	10.2%
G & A expenses as % of net sales	5.1%	3.8%	32.8%	4.3%	5.7%	-24.5%	4.7%	4.8%	-2.1%
Other operating expenses	(46)	(28)	63.7%	16	(27)	-162.0%	(30)	(55)	-45.4%
Operating profit	785	435	80.2%	772	648	19.1%	1,557	1,083	43.7%
Operating margin	10.2%	6.6%	3.6ppt	9.9%	9.1%	0.9ppt	10.0%	7.9%	27.7%
Interest income	40.546	1.911	nm	4.454	13.917	-68.0%	45	15.828	184.3%
Interest expenses	(118)	(71)	67.7%	27	(171)	-116.0%	(91)	(241)	-62.3%
Profit before tax	707	367	92.8%	804	491	63.7%	1,511	858	76.1%
Tax	(93)	(52)	79.7%	(209)	(314)	-33.4%	(302)	(366)	-17.4%
Net profit	614	315	94.9%	595	177	236.1%	1,208	492	145.7%
Net margin	8.0%	4.8%	3.2ppt	7.6%	2.5%	5.2ppt	7.8%	3.6%	1.2ppt

SOURCES: CGIS RESEARCH, COMPANY DATA

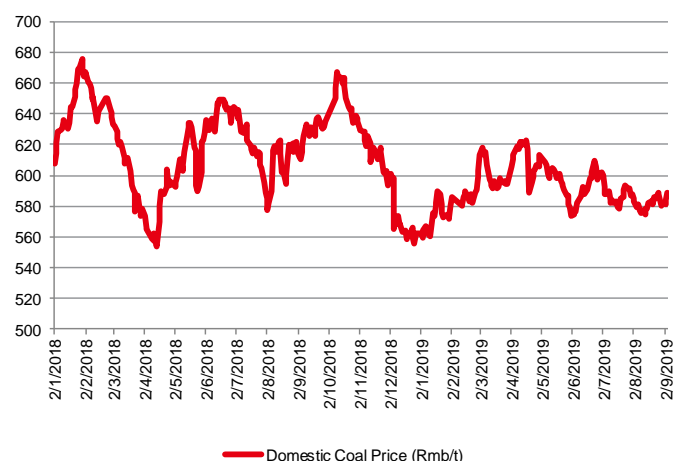
**Figure 2: Fufeng's major products prices**

Rmb/t	1H19	2H19F	FY19F	hoh
MSG	7,161	7,019	7,090	-2.0%
Xanthan gum	14,898	14,923	14,910	0.2%
Threonine	6,978	7,001	6,989	0.3%
Starch Sweetener	2,432	2,500	2,466	2.8%

SOURCES: CGIS RESEARCH, COMPANY DATA

**Figure 3: Domestic Corn Price (Rmb/t)**


SOURCES: CGIS RESEARCH, WIND INFO

**Figure 4: Domestic Coal Price (Rmb/t)**


SOURCES: CGIS RESEARCH, WIND INFO

**Figure 5: DCF valuation**

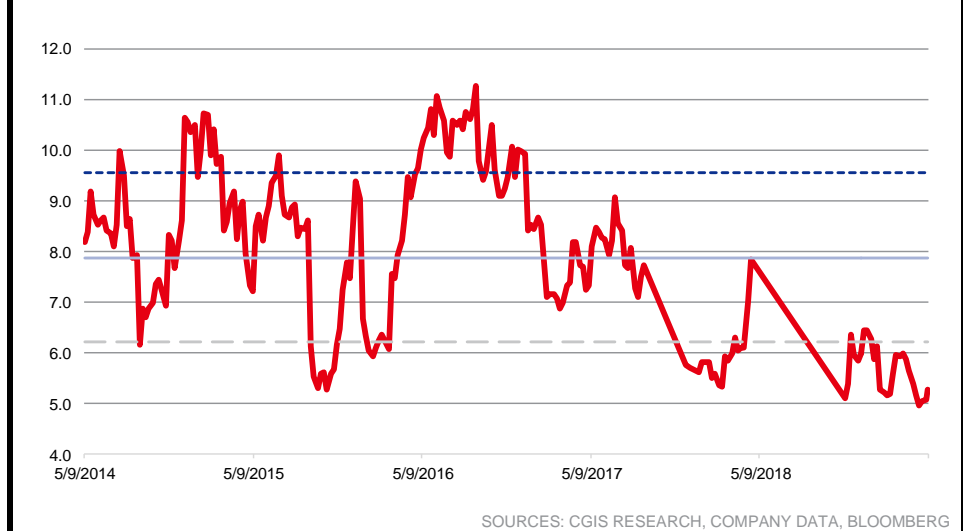
DCF Valuation	HK\$ m
Value of Phase 1: Explicit	8,167.6
Value of Phase 2: Value Driver	3,275.2
Value of Phase 3: Fade	1,492.3
Terminal Value	1,008.5
Enterprise Value	13,943.6
Less: Net Debt	1,939.6
Equity Value	12,004.0
No. Shares (millions)	2,546.7
Per Share Equity Value (HKD)	4.7

SOURCES: CGS-CIMB RESEARCH

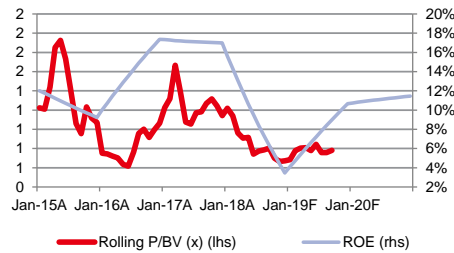
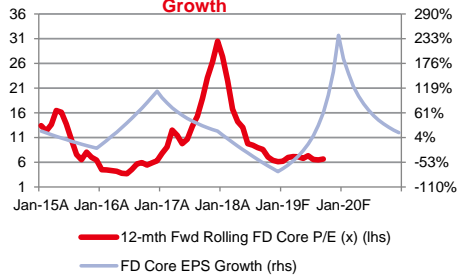
**Figure 6: WACC**

	(%)
<b>Cost of equity</b>	<b>10.1%</b>
Risk free	3.5%
Market risk premium	7.0%
Beta	0.94
<b>Cost of debt</b>	<b>4.3%</b>
Kd (after tax)	3.2%
Target Debt / (Debt + Equity)	15.0%
Target Equity / (Debt + Equity)	85.0%
<b>WACC</b>	<b>9.1%</b>

SOURCES: CGS-CIMB RESEARCH

**Figure 7: Forward PER band of Fufeng**


SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

**BY THE NUMBERS**
**P/BV vs ROE**

**12-mth Fwd FD Core P/E vs FD Core EPS Growth**

**Profit & Loss**

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
<b>Total Net Revenues</b>	<b>13,034</b>	<b>13,765</b>	<b>15,494</b>	<b>17,442</b>	<b>18,678</b>
<b>Gross Profit</b>	<b>2,979</b>	<b>2,575</b>	<b>3,269</b>	<b>3,785</b>	<b>3,980</b>
<b>Operating EBITDA</b>	<b>2,606</b>	<b>2,144</b>	<b>2,809</b>	<b>3,092</b>	<b>3,260</b>
Depreciation And Amortisation	(892)	(1,198)	(1,253)	(1,302)	(1,348)
<b>Operating EBIT</b>	<b>1,715</b>	<b>946</b>	<b>1,557</b>	<b>1,790</b>	<b>1,912</b>
Financial Income/(Expense)	(63)	(226)	(46)	(46)	(46)
Pretax Income/(Loss) from Assoc.	1	0	0	0	0
Non-Operating Income/(Expense)	0	0	0	0	0
<b>Profit Before Tax (pre-EI)</b>	<b>1,653</b>	<b>721</b>	<b>1,511</b>	<b>1,744</b>	<b>1,866</b>
Exceptional Items					
<b>Pre-tax Profit</b>	<b>1,653</b>	<b>721</b>	<b>1,511</b>	<b>1,744</b>	<b>1,866</b>
Taxation	(270)	(366)	(302)	(349)	(373)
Exceptional Income - post-tax	0	1,353	0	0	0
<b>Profit After Tax</b>	<b>1,382</b>	<b>1,708</b>	<b>1,208</b>	<b>1,395</b>	<b>1,493</b>
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
<b>Net Profit</b>	<b>1,382</b>	<b>1,708</b>	<b>1,208</b>	<b>1,395</b>	<b>1,493</b>
Recurring Net Profit	1,382	355	1,208	1,395	1,493
<b>Fully Diluted Recurring Net Profit</b>	<b>1,382</b>	<b>355</b>	<b>1,208</b>	<b>1,395</b>	<b>1,493</b>

**Cash Flow**

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
<b>EBITDA</b>	<b>2,606</b>	<b>2,144</b>	<b>2,809</b>	<b>3,092</b>	<b>3,260</b>
Cash Flow from Inv. & Assoc.					
Change In Working Capital	(987)	(257)	322	(313)	(218)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(82)	(31)	0	0	1
Net Interest (Paid)/Received	(84)	(137)	(91)	(91)	(91)
Tax Paid	(251)	(210)	(302)	(349)	(373)
<b>Cashflow From Operations</b>	<b>1,202</b>	<b>1,510</b>	<b>2,738</b>	<b>2,339</b>	<b>2,579</b>
Capex	(1,985)	(1,717)	(875)	(875)	(875)
Disposals Of FAs/subsidiaries	8	156	0	0	1
Acq. Of Subsidiaries/investments	97	(163)	0	0	1
Other Investing Cashflow	3	(104)	35	35	35
<b>Cash Flow From Investing</b>	<b>(1,876)</b>	<b>(1,828)</b>	<b>(840)</b>	<b>(840)</b>	<b>(838)</b>
Debt Raised/(repaid)	(177)	(397)	(778)	0	1
Proceeds From Issue Of Shares	679	0	0	0	0
Shares Repurchased					
Dividends Paid	(368)	(320)	(554)	(363)	(419)
Preferred Dividends					
Other Financing Cashflow	0	2,350	0	0	0
<b>Cash Flow From Financing</b>	<b>134</b>	<b>1,634</b>	<b>(1,331)</b>	<b>(363)</b>	<b>(418)</b>
Total Cash Generated	(540)	1,315	567	1,137	1,323
<b>Free Cashflow To Equity</b>	<b>(851)</b>	<b>(715)</b>	<b>1,120</b>	<b>1,499</b>	<b>1,742</b>
<b>Free Cashflow To Firm</b>	<b>(590)</b>	<b>(182)</b>	<b>1,989</b>	<b>1,590</b>	<b>1,832</b>

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

**BY THE NUMBERS... cont'd**
**Balance Sheet**

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Total Cash And Equivalents	419	2,690	2,302	3,438	4,762
Total Debtors	489	611	509	573	614
Inventories	3,230	3,262	3,014	3,368	3,624
Total Other Current Assets	969	2,429	2,560	2,690	2,796
<b>Total Current Assets</b>	<b>5,107</b>	<b>8,993</b>	<b>8,385</b>	<b>10,069</b>	<b>11,796</b>
Fixed Assets	9,234	10,310	10,296	9,887	9,428
Total Investments	0	0	0	0	0
Intangible Assets	9	18	31	31	31
Total Other Non-Current Assets	1,608	999	1,601	1,594	1,585
<b>Total Non-current Assets</b>	<b>10,851</b>	<b>11,327</b>	<b>11,928</b>	<b>11,511</b>	<b>11,044</b>
Short-term Debt	1,411	2,025	1,277	1,277	1,277
Current Portion of Long-Term Debt					
Total Creditors	1,451	1,512	1,680	1,915	2,101
Other Current Liabilities	2,345	2,471	2,407	2,407	2,407
<b>Total Current Liabilities</b>	<b>5,208</b>	<b>6,008</b>	<b>5,364</b>	<b>5,598</b>	<b>5,784</b>
Total Long-term Debt	560	2,517	2,487	2,487	2,487
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	739	803	803	803	803
<b>Total Non-current Liabilities</b>	<b>1,299</b>	<b>3,320</b>	<b>3,290</b>	<b>3,290</b>	<b>3,290</b>
Total Provisions	0	0	0	0	0
<b>Total Liabilities</b>	<b>6,506</b>	<b>9,328</b>	<b>8,654</b>	<b>8,888</b>	<b>9,074</b>
Shareholders' Equity	9,460	11,004	11,659	12,692	13,767
Minority Interests	0	0	0	0	0
<b>Total Equity</b>	<b>9,460</b>	<b>11,004</b>	<b>11,659</b>	<b>12,692</b>	<b>13,767</b>

**Key Ratios**

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue Growth	10.4%	5.6%	12.6%	12.6%	7.1%
Operating EBITDA Growth	10.3%	(17.7%)	31.0%	10.1%	5.4%
Operating EBITDA Margin	20.0%	15.6%	18.1%	17.7%	17.5%
Net Cash Per Share (Rmb)	(0.61)	(0.73)	(0.57)	(0.13)	0.39
BVPS (Rmb)	3.71	4.32	4.58	4.98	5.41
Gross Interest Cover	15.71	3.92	17.10	19.67	21.01
Effective Tax Rate	16.4%	50.7%	20.0%	20.0%	20.0%
Net Dividend Payout Ratio	30%	156%	30%	30%	30%
Accounts Receivables Days	12.28	14.59	13.20	11.36	11.60
Inventory Days	103.7	105.9	93.7	85.5	86.8
Accounts Payables Days	48.39	48.33	47.66	48.17	49.86
ROIC (%)	14.8%	4.6%	9.1%	10.3%	11.1%
ROCE (%)	16.5%	7.1%	10.3%	11.5%	11.5%
Return On Average Assets	9.44%	2.67%	6.13%	6.84%	6.89%

**Key Drivers**

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
ASP (% chg, main prod./serv.)	8.5%	-1.7%	6.2%	3.8%	5.2%
Unit sales grth (% , main prod./serv.)	-3.1%	12.3%	7.5%	0.4%	7.0%
Util. rate (% , main prod./serv.)	N/A	N/A	N/A	N/A	N/A
ASP (% chg, 2ndary prod./serv.)	N/A	N/A	N/A	N/A	N/A
Unit sales grth (% , 2ndary prod./serv.)	N/A	N/A	N/A	N/A	N/A
Util. rate (% , 2ndary prod./serv.)	N/A	N/A	N/A	N/A	N/A
ASP (% chg, tertiary prod./serv.)	N/A	N/A	N/A	N/A	N/A
Unit sales grth (% , tertiary prod./serv.)	N/A	N/A	N/A	N/A	N/A
Util. rate (% , tertiary prod./serv.)	N/A	N/A	N/A	N/A	N/A
Unit raw mat ASP (%chg,main)	N/A	N/A	N/A	N/A	N/A
Total Export Sales Growth (%)	N/A	N/A	N/A	N/A	N/A
Export Sales/total Sales (%)	N/A	N/A	N/A	N/A	N/A

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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We are transferring the rating mechanism from "BUY, SELL, HOLD" to "ADD, REDUCE, HOLD". Please refer to the definitions below.

**Explanation on Equity Ratings (Existing mechanism (will be replaced by new mechanism by 01/09/19))**

BUY : share price will increase by >20% within 12 months in absolute terms

SELL : share price will decrease by >20% within 12 months in absolute terms

HOLD : no clear catalyst, and downgraded from BUY pending clearer signal to reinstate BUY or further downgrade to outright SELL

**Explanation on Equity Ratings (New mechanism)**

ADD : The stock's total return is expected to exceed 10% over the next 12 months.

REDUCE : The stock's total return is expected to fall below 0% or more over the next 12 months.

HOLD : The stock's total return is expected to be between 0% and positive 10% over the next 12 months.

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