

Cafe De Coral (341 HK)

Turnaround is here but weaker than expected

We have updated with the management after its FY23 results last week and believe recovery is here but the pace could be slightly slower than expected (as SSSG in FY23 was just 1-2%, missed CMBI est. of 4%). While the management is still keeping their 3-year target (HSD pre-tax margin by FY25E), we are more prudent than them. We maintain BUY but cut TP to HK\$ 12.32, just because of the turnaround and relatively high dividend yield of 5%. The new TP is based on 23x FY3/25E (rolled over from 22x FY3/24E), slightly more than 1 s.d. over its 5 years average of 20x.

- The 3-year plan modified: more conservative in terms of timeline.** While the Company is still aiming for a HSD pre-tax margin by FY25E, management believes the likelihood is now lower, due to weaker-than-expected macro environment. We do think CDC will achieve the target, but could be one year later in FY26E, hence our pre-tax margin assumption for FY25E will now be cut from 5.0% to just 3.9%. On the store expansion in China, the Company's target of 280 stores by FY25E may be delayed, as the management will now focus more on the "success rate" of new stores. But since our estimates were already quite prudent, changes were little.
- Sales (and margins) recovery in HK market was slow, but the trend is still improving.** Recovery rate (vs FY19) of HK CDC's SSS in FY23 was at about 87%, where breakfast and lunch had better recovery than supper. Noted that the trend was picking up in Apr-May 2023 and we are now forecasting that to reach about 92%/ 95% in FY24E/ 25E, implying SSSG of 6%/ 4%. Comparing to pre-Covid level, the drop in EBIT margin for HK (7% in FY23 vs 12% in FY19) was mainly the result of surge in food and labour costs, while the rental expenses had been refined. Going forward, as SSS continue to improve, we do expect margins to recover, but that would be driven more by ASP increases (now at HK\$ 40.7, and may have a HK\$1-2 hike) and better menu mix (hence can more than offset the raw material costs inflation) and the operating leverage, while labour costs and rental expenses, as % of sale, could stay flattish. The surge in number of employees (by 1,000+) in FY23 was only due to the increased part-time staffs in the factory, hence that would not drive up costs significantly.
- Maintain BUY but cut TP to HK\$ 12.32.** We cut our net profit estimates by 35%-36% in FY24E-25E, to factor in the: 1) higher-than-expected other losses, 2) slower-than-expected SSSG and 3) the less-than-expected operating leverage. We maintain BUY but cut TP to HK\$ 12.32, based on 23x FY3/25E (rolled over from 22x FY3/24E). It is trading at 20x, at par with its 5 years average, not too demanding, in our view.

Earnings Summary

(YE 31 Mar)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue (HK\$ mn)	7,509	8,024	8,809	9,424	10,119
YoY growth (%)	11.8	6.9	9.8	7.0	7.4
Operating profit (HK\$ mn)	131	204	336	418	537
Net profit (HK\$ mn)	22.9	111.2	259.8	313.8	397.4
EPS (Reported) (HK\$)	0.04	0.19	0.44	0.54	0.68
YoY growth (%)	(94.1)	419.0	133.8	20.8	26.6
P/E (x)	291.0	56.1	24.0	19.9	15.7
P/B (x)	2.2	2.2	2.2	2.1	2.0
Yield (%)	2.7	3.6	4.2	5.0	6.4
ROE (%)	0.8	4.0	9.2	10.9	13.4

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$12.32
(Previous TP)	HK\$15.12)
Up/Downside	15.8%
Current Price	HK\$10.64

China Consumer Discretionary

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Stock Data

Mkt Cap (HK\$ mn)	6,021.0
Avg 3 mths t/o (HK\$ mn)	10.9
52w High/Low (HK\$)	15.18/9.10
Total Issued Shares (mn)	585.7

Source: FactSet

Shareholding Structure

Lo Tak Shing	16.1%
Lo Hoi Kwong	11.0%

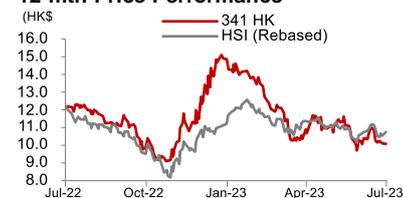
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-7.1%	-3.2%
3-mth	-15.5%	-9.8%
6-mth	-18.0%	-19.9%

Source: FactSet

12-mth Price Performance



Source: FactSet

- **We expect pace of recovery in China to be slower than that in HK, but the margin advantage could sustain.** Recovery rate (vs FY19) of Mainland CDC's SSS in FY23 was at around 92%, and the trend in Apr-May 2023 was kind of flattish, but still we are forecasting that to reach around 97%/ 100% in FY24E/ 25E, which is also implying 5%/ 3% SSSG. Noted that sales mix of breakfast were actually climbing healthily, to now about 20% of sales in China. From the costs side, we believe China's EBIT margin can still be better than that in HK by around 2ppt onwards, thanks to continual efficiency gains (greater digital sales and more food delivery robots were used) and reasonable decrease in rental expenses.
- **Store expansion plan becomes more conservative, but inline with our estimates.** Management is now forecasting about 20/ 25 gross openings in HK/ Mainland China in FY24E, while the net openings should be at about 5/ 20, which is slow in our view, but still inline with our previous estimates.
- **FY23 results recap: weak net profit but dividend surprised.** In FY23, sales increased by 7% to HK\$ 8.0 bn, inline with CMBI est., while net profit jumped by about 420% to HK\$ 110mn, inline with profit warning, but missing CMBI est. by roughly 50%. The weak results were a mixture of: 1) slower-than-expected SSSG, at 1-2% for CDC and Super congee (vs CMBI est. of 4%), 2) higher-than-expected impairment from store closures and fair value losses for investment property and 3) higher-than-expected finance costs. But there was still a positive, which is the higher-than-expected dividend (payout ratio at roughly 200%, vs CMBI est. of 70%).

Earnings revision

Figure 1: Earnings revision

HK\$ mn	New			Old			Diff (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Revenue	8,809	9,424	10,119	9,020	9,797	n/a	-2.3%	-3.8%	n/a
Gross profit	857	972	1,125	1,054	1,211	n/a	-18.7%	-19.8%	n/a
EBIT	336	418	537	540	657	n/a	-37.9%	-36.4%	n/a
Net profit att.	258	312	395	399	485	n/a	-35.3%	-35.8%	n/a
Diluted EPS (HK\$)	0.44	0.54	0.68	0.69	0.84	n/a	-35.4%	-35.9%	n/a
Gross margin	9.7%	10.3%	11.1%	11.7%	12.4%	n/a	-2ppt	-2.1ppt	n/a
EBIT margin	3.8%	4.4%	5.3%	6.0%	6.7%	n/a	-2.2ppt	-2.3ppt	n/a
Net profit att. margin	2.9%	3.3%	3.9%	4.4%	5.0%	n/a	-1.5ppt	-1.6ppt	n/a

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

HK\$ mn	CMBIGM			Consensus			Diff (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Revenue	8,809	9,424	10,119	8,846	9,722	10,475	-0.4%	-3.1%	-3.4%
Gross profit	857	972	1,125	1,017	1,205	1,320	-15.8%	-19.4%	-14.8%
EBIT	336	418	537	507	609	689	-33.9%	-31.3%	-22.0%
Net profit att.	258	312	395	263	319	309	-1.8%	-2.2%	27.7%
Diluted EPS (HK\$)	0.44	0.54	0.68	0.60	0.80	1.06	-26.1%	-33.0%	-36.0%
Gross margin	9.7%	10.3%	11.1%	11.5%	12.4%	12.6%	-1.8ppt	-2.1ppt	-1.5ppt
EBIT margin	3.8%	4.4%	5.3%	5.7%	6.3%	6.6%	-1.9ppt	-1.8ppt	-1.3ppt
Net profit att. margin	2.9%	3.3%	3.9%	3.0%	3.3%	3.0%	0ppt	0ppt	1ppt

Source: Company data, CMBIGM estimates

Assumptions

Figure 3: Major assumptions

Major assumptions	FY22A	FY23A	FY24E	FY25E	FY26E
Sales by segment (HK\$ mn)					
HK QSR & Institutional Catering	4,751	5,259	6,348	6,898	7,330
HK Fast Casual & Casual Dining	622	771	848	932	1,026
Food Processing & Distribution	141	148	156	163	171
Mainland China	1,200	1,332	1,625	1,868	2,083
Total	6,714	7,509	8,975	9,862	10,610
Growth (%)					
HK QSR & Institutional Catering	-20%	11%	21%	9%	6%
HK Fast Casual & Casual Dining	-20%	24%	10%	10%	10%
Food Processing & Distribution	-9%	5%	5%	5%	5%
Mainland China	10%	11%	22%	15%	12%
Total	-16%	12%	20%	10%	8%
GP margin	5.6%	7.3%	11.6%	12.4%	12.7%
Costs breakdown					
Costs of raw materials	29.9%	30.0%	30.0%	29.8%	29.8%
Depreciation	5.2%	4.8%	4.3%	4.1%	4.0%
Operating lease rentals	13.2%	11.9%	11.0%	10.8%	10.9%
Employee benefit expenses	34.7%	34.0%	31.5%	31.6%	31.6%
OP margin	7.1%	1.7%	6.5%	6.7%	7.0%
Effective tax rate	7.7%	55.0%	16.0%	16.0%	16.0%
NP att. margins	5.3%	0.3%	4.4%	4.6%	4.9%
NP att. growth (%)	387.7%	-94.1%	1771.6%	14.6%	14.5%
Sales network by region					
HK QSR & Institutional Catering	292	301	306	311	316
HK Fast Casual Dining	60	63	68	73	78
Mainland China	122	136	156	176	201
Total	474	500	530	560	595
SSSG by segment					
HK Café de Coral	-14.0%	6.0%	14.0%	6.0%	4.0%
HK Super Super Congee & Noodles	-11.0%	13.0%	11.0%	4.0%	3.0%
Mainland China Café de Coral	2.0%	-1.0%	11.0%	5.0%	3.0%

Source: Company data, CMBIGM estimates

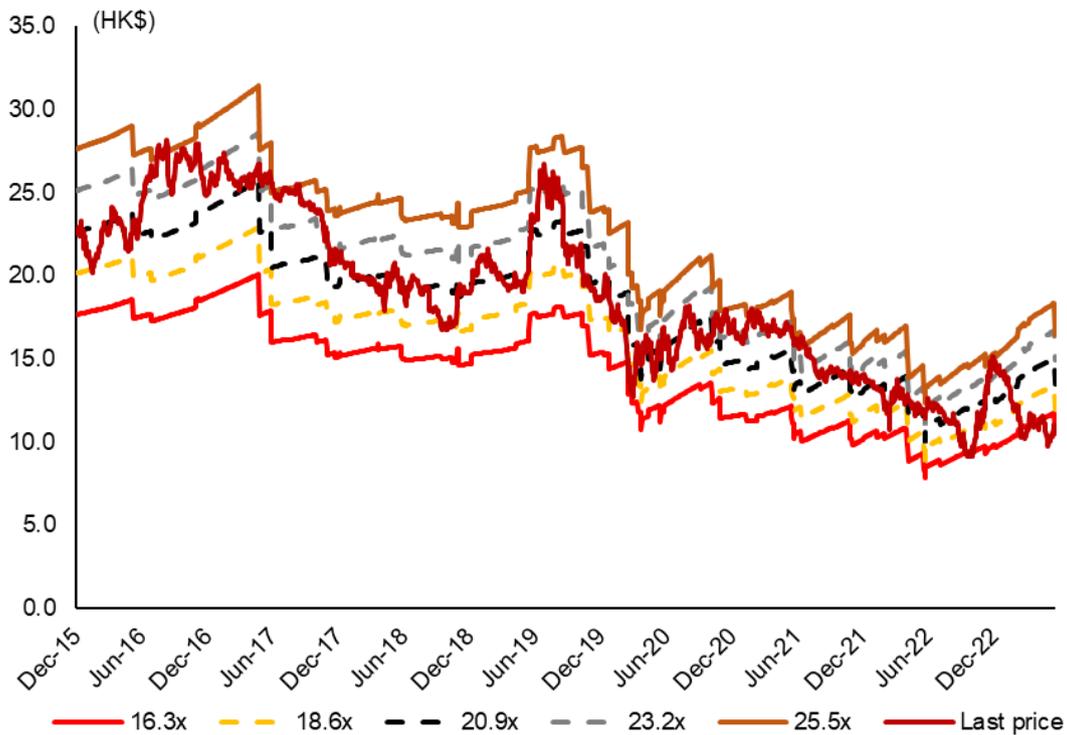
Valuation

Figure 4: Peers' valuation

Company	Ticker	Rating	12m TP (LC)	Price (LC)	Up/ Down- side	Mkt. Cap (HK\$ mn)	Year End	P/E (x)		P/B (x)	ROE (%)	3yrs PEG (x)	Yield (%)	YTD per. (%)
								FY1E	FY2E	FY1E	FY1E	FY1E	FY1E	FY1E
Leading Greater China Restaurants and Food Ingredients														
Cafe De Coral	341 HK	BUY	12.32	10.64	16%	6,232	Mar-23	24.0	19.8	2.2	2.1	3.9	0.5	4.2
Haidilao Int'l	6862 HK	BUY	21.62	17.74	22%	98,883	Dec-22	27.7	21.5	8.8	6.4	17.9	0.6	0.9
Jiumaojiu Int'l	9922 HK	BUY	19.70	13.18	49%	19,170	Dec-22	28.2	18.1	4.7	3.8	1.6	0.1	0.9
Helens	9869 HK	NR	n/a	8.06	n/a	10,211	Dec-22	23.1	13.8	4.2	3.3	(68.1)	(0.1)	0.2
XBXB Catering	520 HK	NR	n/a	3.94	n/a	4,280	Dec-22	13.6	8.5	2.3	2.0	(20.6)	(0.1)	2.4
Yihai Int'l	1579 HK	NR	n/a	18.02	n/a	18,681	Dec-22	18.8	16.1	3.3	2.9	18.3	1.3	1.6
Yum China	9987 HK	BUY	465.05	460.20	1%	192,134	Dec-22	27.1	22.6	3.4	3.0	9.3	0.6	0.9
Gourmet Master	2723 TT	NR	n/a	152.00	n/a	6,927	Dec-22	23.4	19.0	2.2	2.1	4.3	0.4	2.6
								Avg.	23.9	17.1	3.7	3.0	(4.8)	0.4
								Med.	24.0	18.1	3.3	2.9	3.9	0.4
														1.5
														0.9
International Restaurants and Food Ingredients														
Yum! Brands	YUM US	NR	n/a	138.58	n/a	303,754	Dec-22	27.1	23.4	n/a	n/a	n/a	2.0	1.7
McDonald's	MCD US	NR	n/a	293.70	n/a	1,678,075	Dec-22	26.6	24.3	n/a	n/a	n/a	1.7	2.1
Starbucks Corp	SBUX US	NR	n/a	101.87	n/a	913,926	Oct-22	29.7	24.9	n/a	n/a	n/a	1.6	2.1
Rest. Brands	QSR US	NR	n/a	76.43	n/a	268,083	Dec-22	24.6	22.6	8.8	7.9	41.7	5.5	2.9
Chipotle Mexican	CMG US	NR	n/a	2032.9	n/a	438,933	Dec-22	45.9	38.0	19.4	16.2	44.7	1.8	0.0
Darden Rest.	DRI US	NR	n/a	166.01	n/a	157,107	May-22	20.9	18.8	9.6	9.2	43.8	2.3	2.9
Domino's Pizza	DPZ US	NR	n/a	331.41	n/a	91,653	Jan-23	24.9	22.3	n/a	n/a	n/a	2.7	1.5
Wendy's Co	WEN US	NR	n/a	22.47	n/a	37,057	Jan-23	22.8	20.0	19.0	29.3	41.1	1.5	4.5
Shake Shack	SHAK US	NR	n/a	71.13	n/a	23,518	Dec-22	461.9	257.7	7.3	6.9	(3.9)	(2.4)	n/a
Wingstop	WING US	NR	n/a	188.17	n/a	44,132	Dec-22	88.2	76.0	n/a	n/a	n/a	4.6	0.4
Jollibee Foods	JFC PM	NR	n/a	240.00	n/a	37,832	Dec-22	31.7	25.8	3.3	3.1	9.9	1.8	1.2
								Avg.	73.1	50.4	11.2	12.1	29.6	2.1
								Med.	27.1	24.3	9.2	8.6	41.4	1.8
														1.9
H-shares Consumer Staples														
UPC	220 HK	NR	n/a	7.07	n/a	30,538	Dec-22	16.5	15.0	2.1	2.0	9.1	0.9	6.8
Tingyi	322 HK	NR	n/a	12.20	n/a	68,738	Dec-22	17.6	14.5	4.9	4.7	16.4	0.8	7.2
Want Want China	151 HK	NR	n/a	5.33	n/a	63,317	Mar-22	15.3	13.7	3.4	3.3	25.6	(42.7)	5.5
China Mengniu*	2319 HK	BUY	57.00	31.50	81%	124,441	Dec-22	18.3	15.8	2.5	2.2	13.8	1.3	1.6
Vitasoy	345 HK	NR	n/a	12.62	n/a	13,530	Mar-23	48.0	29.3	3.7	3.4	1.5	0.4	0.3
Nongfu Spring*	9633 HK	BUY	58.0	44.30	n/a	498,218	Dec-22	47.6	40.9	16.4	14.2	37.9	3.8	1.5
Tsingtao Brewery*	168 HK	BUY	86.00	70.00	23%	126,315	Dec-22	20.3	17.5	3.1	2.8	15.7	1.8	2.9
CR Beer*	291 HK	BUY	71.00	52.80	34%	171,293	Dec-22	28.9	24.0	5.1	4.6	16.9	1.5	1.4
Budweiser Brew*	1876 HK	BUY	28.00	21.70	29%	287,382	Dec-22	32.2	27.7	3.2	3.0	8.4	1.8	1.3
Dali Foods	3799 HK	NR	n/a	2.72	n/a	37,248	Dec-22	10.7	9.8	1.7	1.5	15.8	2.1	5.4
								Avg.	25.5	20.8	4.6	4.2	16.1	(2.8)
								Med.	19.3	16.6	3.3	3.2	15.8	1.4
														2.2

Source: Bloomberg, CMBIGM estimates, *covered by Joseph Wong

Figure 5: Forward 12M P/E valuation band



Source: Bloomberg, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar (HK\$ mn)						
Revenue	6,714	7,509	8,024	8,809	9,424	10,119
Cost of goods sold	(6,339)	(6,961)	(7,321)	(7,952)	(8,453)	(8,994)
Gross profit	375	548	703	857	972	1,125
Operating expenses	98	(417)	(499)	(521)	(553)	(588)
Admin expense	(463)	(459)	(486)	(508)	(540)	(574)
Others	561	42	(13)	(14)	(14)	(14)
Operating profit	474	131	204	336	418	537
Share of (losses)/profits of associates/JV	0	0	0	0	0	0
EBITDA	825	493	582	755	869	1,022
Depreciation	(351)	(362)	(378)	(416)	(448)	(482)
Depreciation of ROU assets	(14)	(14)	(14)	(14)	(14)	(14)
Other amortisation	(0)	(0)	(0)	(3)	(3)	(3)
Interest income	(83)	(80)	(60)	(30)	(49)	(70)
Pre-tax profit	391	51	144	306	369	467
Income tax	(30)	(28)	(33)	(46)	(55)	(70)
Minority interest	1	2	1	2	2	3
Net profit	361	23	111	260	314	397
BALANCE SHEET	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar (HK\$ mn)						
Current assets	2,516	2,152	2,050	2,055	2,040	2,047
Cash & equivalents	2,073	1,586	1,510	1,515	1,465	1,434
Account receivables	103	200	154	121	129	139
Inventories	235	304	319	347	369	392
Prepayment	51	55	59	65	69	74
ST bank deposits	21	0	0	0	0	0
Financial assets at FVTPL	0	0	0	0	0	0
Other current assets	33	8	8	8	8	8
Non-current assets	4,639	4,720	4,844	4,991	5,146	5,314
PP&E	1,519	1,586	1,702	1,852	2,010	2,180
Deferred income tax	71	68	10	10	10	10
Intangibles	1	1	2	2	1	1
Other non-current assets	3,048	3,065	3,130	3,128	3,125	3,123
Total assets	7,155	6,872	6,894	7,046	7,186	7,360
Current liabilities	1,688	1,726	1,782	1,868	1,936	2,012
Account payables	178	167	176	191	203	216
Tax payable	8	14	14	14	14	14
Other current liabilities	1,502	1,544	1,591	1,662	1,718	1,782
Non-current liabilities	2,432	2,319	2,319	2,319	2,319	2,319
Other non-current liabilities	2,432	2,319	2,319	2,319	2,319	2,319
Total liabilities	4,120	4,045	4,101	4,188	4,256	4,332
Share capital	59	59	59	59	59	59
Capital surplus	621	621	621	621	621	621
Retained earnings	1,982	1,755	1,701	1,738	1,780	1,845
Other reserves	368	384	404	430	458	489
Total shareholders equity	3,029	2,819	2,785	2,848	2,918	3,014
Minority interest	6	8	8	10	12	15
Total equity and liabilities	7,155	6,872	6,894	7,046	7,186	7,360

CASH FLOW	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar (HK\$ mn)						
Operating						
Profit before taxation	391	51	144	306	369	467
Depreciation & amortization	1,099	1,110	378	419	451	484
Tax paid	(29)	9	(33)	(46)	(55)	(70)
Change in working capital	70	(166)	82	86	33	38
Others	162	160	95	61	82	105
Net cash from operations	1,693	1,164	666	827	880	1,025
Investing						
Capital expenditure	(278)	(492)	(525)	(577)	(617)	(662)
Acquisition of subsidiaries/ investments	0	0	0	0	0	0
Net proceeds from disposal of short-term investments	0	0	0	0	0	0
Others	5	36	808	837	817	796
Net cash from investing	(273)	(456)	283	260	200	134
Financing						
Dividend paid	(58)	(221)	(164)	(221)	(270)	(330)
Net borrowings	1,179	(100)	0	0	0	0
Proceeds from share issues	0	0	0	0	0	0
Share repurchases	(25)	(26)	0	0	0	0
Others	(808)	(860)	(860)	(860)	(860)	(860)
Net cash from financing	288	(1,207)	(1,024)	(1,081)	(1,130)	(1,190)
Net change in cash						
Cash at the beginning of the year	345	2,073	1,586	1,510	1,515	1,465
Exchange difference	20	11	0	0	0	0
Others	1,708	(498)	(76)	5	(50)	(32)
Cash at the end of the year	2,073	1,586	1,510	1,515	1,465	1,434
GROWTH	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar						
Revenue	(15.7%)	11.8%	6.9%	9.8%	7.0%	7.4%
Gross profit	(48.7%)	46.0%	28.3%	21.9%	13.4%	15.8%
Operating profit	126.9%	(72.3%)	55.4%	64.6%	24.7%	28.5%
EBITDA	45.5%	(40.2%)	18.0%	29.7%	15.1%	17.6%
Net profit	384.7%	(93.7%)	386.6%	133.6%	20.8%	26.6%
PROFITABILITY	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar						
Gross profit margin	5.6%	7.3%	8.8%	9.7%	10.3%	11.1%
Operating margin	7.1%	1.7%	2.5%	3.8%	4.4%	5.3%
EBITDA margin	12.3%	6.6%	7.3%	8.6%	9.2%	10.1%
Return on equity (ROE)	12.7%	0.8%	4.0%	9.2%	10.9%	13.4%
GEARING/LIQUIDITY/ACTIVITIES	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar						
Current ratio (x)	1.5	1.2	1.2	1.1	1.1	1.0
Receivable turnover days	5.6	9.7	7.0	5.0	5.0	5.0
Inventory turnover days	13.5	15.9	15.9	15.9	15.9	15.9
Payable turnover days	10.3	8.8	8.8	8.8	8.8	8.8
VALUATION	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Mar						
P/E	17.2	291.0	56.1	24.0	19.9	15.7
P/E (diluted)	17.2	291.0	56.1	24.0	19.9	15.7
P/B	2.0	2.2	2.2	2.2	2.1	2.0
P/CFPS	5.6	7.3	10.4	7.1	6.7	5.8
Div yield (%)	3.6	2.7	3.6	4.2	5.0	6.4

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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