

Café de Coral

Bloomberg: 341 HK EQUITY | Reuters: 0341.HK

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DBS Group Research . Equity

16 Jun 2022

BUY

Last Traded Price (15 Jun 2022): HK\$11.78 (HSI : 21,308)
Price Target 12-mth: HK\$15.30 (30% upside) (Prev HK\$15.50)

Analyst

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What's New

- CdC net earnings in line with earlier profit warning, with positive surprise on final DPS of HK18cents.
- Gradual recovery since lockdowns eased in HK
- Over the next three years, CdC aims to lift HK profit margin from low single digit to high single digit, and more than double store numbers in PRC
- Proven track record to drive recovery post lockdowns; maintain BUY, TP at HK\$15.3

Poised for recovery again

Investment Thesis

Recovering from Omicron outbreak. Café de Coral's (CdC) operations in Hong Kong (HK) have been gradually recovering post the fifth wave of the COVID-19 pandemic. CdC's leading position remains unchanged, and its improved cost efficiency as well as its proactive strategy to boost takeaway and delivery sales should help partly offset the impact. Over the next three years, the group targets to drive its HK operational profit margin from a low single-digit percentage to a high single-digit percentage.

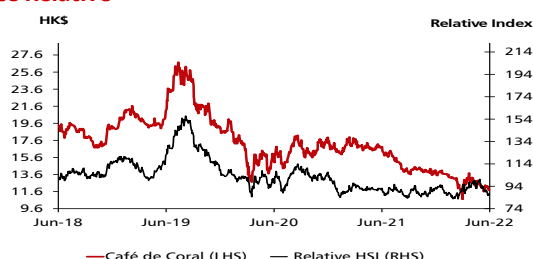
Well positioned to gain market share. The prolonged impact from the pandemic has accelerated market consolidation in the eating out industry, as weaker players are phased out. With a leading market position and strong financials, CdC should be on a strong footing to not just survive the challenging environment but to gain further market share.

China expansion to continue. The pandemic resurgence also impacted CdC's China business, with a slower pace of new store openings in FY22. The company aims to more than double its store count over the next three years, to 280 outlets (FY3/22: 136 outlets). China should remain a solid growth driver with store expansion projected to continue.

Valuation:

We adjust our earnings for FY23F upward by 2%. We adjust our TP mildly at HK\$15.3 on mild change in share base, premised on an unchanged 25x FY24F PE.

Price Relative



Forecasts and Valuation

FY Mar (HK\$m)	2021A	2022A	2023F	2024F
Turnover	6,714	7,509	8,061	8,671
EBITDA	839	508	656	916
Pre-tax Profit	391	51	205	450
Net Profit	359	21	162	356
Net Pft (Pre Ex) (core profit)	359	21	162	356
Net Profit Gth (Pre-ex) (%)	387.7	(94.1)	662.3	120.2
EPS (HK\$)	0.62	0.04	0.28	0.61
EPS Gth (%)	387.7	(94.1)	662.3	120.2
Diluted EPS (HK\$)	0.62	0.04	0.28	0.61
DPS (HK\$)	0.38	0.28	0.28	0.61
BV Per Share (HK\$)	5.23	4.86	4.78	5.12
PE (X)	19.0	321.6	42.2	19.2
P/Cash Flow (X)	4.0	6.6	5.7	4.9
P/Free CF (X)	4.8	11.2	8.9	7.1
EV/EBITDA (X)	7.1	12.4	8.4	5.6
Net Div Yield (%)	3.3	2.4	2.4	5.2
P/Book Value (X)	2.3	2.4	2.5	2.3
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	12.6	0.7	5.8	12.4
Earnings Rev (%)			2	Nil
Consensus EPS (HK\$)			1.01	1.11
Other Broker Recs:		B:6	S:0	H:0

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Where we differ:

Our earnings forecasts are below the market consensus, as we are more prudent about the normalisation pace – our current forecast assumes sales recovery in FY23.

Key Risks to Our View:

Significant economic downturn, major resurgence of the pandemic, weakening/disruption in foot traffic, cost inflationary pressure, and food safety issues.

At A Glance

Issued Capital (m shrs)	586
Mkt Cap (HKm/US\$m)	6,900 / 879
Major Shareholders (%)	
Wandels Investment Ltd.	15.9
Lo (Hoi Kwong Sunny)	11.0
Mondrian Investment Partners Ltd.	7.0
Lo (Hoi Chun)	6.2
MMW Holding Corporation	5.4
Free Float (%)	54.5
3m Avg. Daily Val. (US\$m)	1.20
GICS Industry: Consumer Discretionary / Consumer Services	



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Café de Coral

WHAT'S NEW

FY3/22 results overview

FY3/22 results in line with earlier profit warning. Café de Coral (CdC)'s FY3/22 results show net earnings drop of 93.5% to HK\$21.2m (FY3/21: HK\$359.1m), in line with the earlier profit warning. 2HFY22 swung to a net loss of HK\$60m (2HFY21 net earnings were HK\$151.9m). Excluding COVID-related government subsidies, the net loss expanded to HK\$189.2m (2HFY21 net loss was HK\$176.5m). The group had reported steady recovery in the first three quarters, with sales returning to pre-pandemic levels by December. The outbreak of the fifth wave of the COVID-19 pandemic in HK and lockdown restrictions in Shenzhen and Zhuhai in Mar 22 brought about sales disruptions in the last quarter. Moreover, COVID-19 relief has substantially reduced to HK\$128m in FY3/22 (FY3/21: HK\$639m). Despite a contraction in earnings, the company has recommended a final DPS of HK18cents (FY3/21: HK28 cents), with its dividend payout ratio at 773.6%.

Sales disruptions in the last quarter. During the fifth wave of COVID-19, sales were seriously disrupted during February and March, resulting in a cumulative loss of 2,755 business days (c.17% of capacity). CdC targeted to drive full-day takeaway services in most CdC and Super Super Congee & Noodles outlets. HK sales growth slowed to 7% y-o-y in 2HFY22 (1HFY22: 20%); of which, QSR and casual dining sales rose 1% and 7%, respectively.

Partial lockdowns in Shenzhen and Zhuhai in Mar 22 had impacted 53 outlets in China, which were temporarily closed or only allowed to operate at limited capacity. China sales growth slowed to 2% in 2HFY22 (1HFY22: 20%), with a full-year same-store sales decline reported at 1%.

The gross profit margin expanded 1.7ppt to 7.3%, primarily lifted by business recovery in the first three quarters, offset by business disruptions in the last quarter. Raw material cost as a % of sales remained stable at 30.0% (FY3/21: 29.9%), staff cost contracted 1.1ppt to 34.1%, and rental costs contracted 1.1ppt to 11.6%.

Store openings disrupted, with more in the pipeline.

During the period, CdC had a gross opening of 12 outlets to 364 outlets in HK, and added 15 outlets in China, with 136 outlets as of Mar 22. The company reported 10/16 outlets in the pipeline for HK/China, respectively.

Steady financial position. The company's financial position remains healthy with net cash of HK\$506m as of Mar 22 (cash of HK\$1,586m and borrowings of HK\$1,080m) (Mar 21 net cash was HK\$893m).

Strategic three-year target. Café de Coral has established targets over the next three years. In Hong Kong, the group aims to unlock the potential of its revenue through improving profit margins from low to high single-digit percentages. This involves optimising operations and managing overheads. The group aims to brand its portfolio, refine its business model, increase investment in digital infrastructure, as well as strength its loyalty club membership programmes. In China, CdC aims to more than double its retail network to 280 stores (Mar-22: 136 outlets), whilst maintaining healthy profitability and service levels.

FY3/23 outlook. Disruptions to the restaurant sector brought about by the COVID-19 pandemic were unavoidable. The group has proven its ability to drive market consolidation and recovery post the lifting of lockdowns during the past few waves. We are positive about the group's medium-term prospects of returning to the pre-COVID level of profitability. We forecast earnings growth of 662%/120% in FY23E/24E, with TP at \$15.3/sh

Company Background

Established in 1968, Cafe de Coral (CdC) is the largest Chinese fast food operator in Hong Kong. The company was listed on the HK Stock Exchange in 1986. Apart from running fast food restaurants under the Cafe de Coral brand name, the company has been diversifying its brand portfolio in both quick-service restaurants and specialty restaurants with brands including Super Super Congee & Noodles, Oliver's Super Sandwiches, Mixian Sense, Spaghetti House, Shanghai Lao Lao, etc. The company also offers institutional catering services under Asia Pacific Catering.

Café de Coral

Interim Income Statement (HK\$m)

FY Mar	2H2021	1H2022	2H2022	% chg yoy	% chg hoh
Revenue	3,489	3,870	3,639	4.3	(6.0)
Cost of Goods Sold	(3,269)	(3,491)	(3,470)	6.1	(0.6)
Gross Profit	220	379	169	(23.1)	(55.4)
Other Oper. (Exp)/Inc	11	(242)	(175)	(1,683.6)	(27.7)
Operating Profit	231	137	(6)	(102.5)	(104.3)
Other Non Opg (Exp)/Inc	0	0	0	nm	nm
Associates & JV Inc	0	0	0	nm	nm
Net Interest (Exp)/Inc	(40)	(41)	(40)	1.5	2.6
Exceptional Gain/(Loss)	0	0	0	nm	nm
Pre-tax Profit	190	96	(46)	nm	nm
Tax	(38)	(14)	(14)	(63.9)	(5.0)
Minority Interest	(1)	(1)	(1)	(43.3)	11.9
Net Profit	152	81	(60)	nm	(173.9)
Net profit bef Except.	152	81	(60)	nm	(173.9)
EBITDA	411	322	187	(54.6)	(42.0)
Margins (%)					
Gross Margins	6.3	9.8	4.6		
Opg Profit Margins	6.6	3.5	(0.2)		
Net Profit Margins	4.4	2.1	(1.6)		

Source: Company, DBS HK

Income Statement (HK\$ m)

FY Mar	2021A	2022A	% chg vov
Revenue	6,714	7,509	11.8
Cost of Goods Sold	(6,339)	(6,961)	9.8
Gross Profit	375	548	46.0
Other Opg (Exp)/Inc	98	(417)	(523.4)
Operating Profit	474	131	(72.3)
Other Non Opg (Exp)/Inc	0	0	nm
Associates & JV Inc	0	0	nm
Net Interest (Exp)/Inc	(83)	(80)	3.2
Exceptional Gain/(Loss)	0	0	nm
Pre-tax Profit	391	51	(87.0)
Tax	(30)	(28)	(6.9)
Minority Interest	(1)	(2)	(15.2)
Net Profit	359	21	(94.1)
Net Profit before Except.	359	21	(94.1)
EBITDA	839	508	(39.4)
Margins & Ratio			
Gross Margins (%)	5.6	7.3	
Opg Profit Margin (%)	7.1	1.7	
Net Profit Margin (%)	5.3	0.3	

Source: Company, DBS HK

Café de Coral

Key Assumptions

FY Mar	2020A	2021A	2022A	2023F	2024F
Food cost as % of sales	28.4	29.9	30.0	29.3	28.8
Staff cost as % of sales	33.9	35.2	34.1	33.8	33.4
Rental cost as % of sales	13.1	12.7	11.6	11.6	11.6

Source: Company, DBS HK

Segmental Breakdown (HK\$ m)

FY Mar	2020A	2021A	2022A	2023F	2024F
Revenues (HK\$ m)					
Hong Kong	6,873	5,514	6,177	6,509	6,935
PRC	1,090	1,200	1,332	1,552	1,736
Total	7,963	6,714	7,509	8,061	8,671

Source: Company, DBS HK

Income Statement (HK\$ m)

FY Mar	2020A	2021A	2022A	2023F	2024F
Revenue	7,963	6,714	7,509	8,061	8,671
Cost of Goods Sold	(7,232)	(6,339)	(6,961)	(7,329)	(7,708)
Gross Profit	731	375	548	732	963
Other Opng (Exp)/Inc	(522)	98	(417)	(455)	(442)
Operating Profit	209	474	131	278	521
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(94)	(83)	(80)	(73)	(71)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	114	391	51	205	450
Tax	(40)	(30)	(28)	(42)	(92)
Minority Interest	(1)	(1)	(2)	(2)	(2)
Preference Dividend	0	0	0	0	0
Net Profit	74	359	21	162	356
EBITDA	581	839	508	656	916
Growth					
Revenue Gth (%)	(6.2)	(15.7)	11.8	7.4	7.6
EBITDA Gth (%)	(49.7)	44.4	(39.4)	29.1	39.6
Opg Profit Gth (%)	(73.9)	126.9	(72.3)	111.7	87.8
Net Profit Gth (%)	(87.1)	387.7	(94.1)	662.3	120.2
Margins & Ratio					
Gross Margins (%)	9.2	5.6	7.3	9.1	11.1
Opg Profit Margin (%)	2.6	7.1	1.7	3.4	6.0
Net Profit Margin (%)	0.9	5.3	0.3	2.0	4.1
ROAE (%)	2.5	12.6	0.7	5.8	12.4
ROA (%)	1.1	5.4	0.3	2.4	5.2
ROCE (%)	2.7	8.5	1.1	4.4	8.8
Div Payout Ratio (%)	151.1	62.0	773.1	100.0	100.0
Net Interest Cover (x)	2.2	5.7	1.6	3.8	7.3

Source: Company, DBS HK

Café de Coral

Interim Income Statement (HK\$ m)

FY Mar	2H2020	1H2021	2H2021	1H2022	2H2022
Revenue	3,699	3,226	3,489	3,870	3,639
Cost of Goods Sold	(3,468)	(3,087)	(3,269)	(3,491)	(3,470)
Gross Profit	232	138	220	379	169
Other Oper. (Exp)/Inc	(258)	87	11	(242)	(175)
Operating Profit	(27)	226	231	137	(6)
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(47)	(43)	(40)	(41)	(40)
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	(74)	183	190	96	(46)
Tax	(2)	(20)	(38)	(14)	(14)
Minority Interest	0	(1)	(1)	(1)	(1)
Net Profit	(76)	162	152	81	(60)
Net profit bef Except.	(76)	162	152	81	(60)
Growth					
Revenue Gth (%)	(13.9)	(24.3)	(5.7)	20.0	4.3
Opg Profit Gth (%)	(105.7)	(4.1)	(964.2)	(39.3)	(102.5)
Net Profit Gth (%)	N/A	8.4	N/A	(50.0)	N/A
Margins					
Gross Margins (%)	6.3	4.3	6.3	9.8	4.6
Opg Profit Margins (%)	(0.7)	7.0	6.6	3.5	(0.2)
Net Profit Margins (%)	(2.1)	5.0	4.4	2.1	(1.6)

Source: Company, DBS HK

Café de Coral

Balance Sheet (HK\$ m)

FY Mar	2020A	2021A	2022A	2023F	2024F
Net Fixed Assets	2,194	2,062	2,101	2,117	2,117
Invt in Associates & JVs	0	0	0	0	0
Other LT Assets	3,152	2,577	2,619	2,078	1,919
Cash & ST Invt	347	2,094	1,586	1,918	2,270
Inventory	261	235	304	326	351
Debtors	167	103	200	214	230
Other Current Assets	101	84	63	67	71
Total Assets	6,221	7,155	6,872	6,721	6,959
ST Debt	0	180	180	180	180
Creditors	172	178	167	180	193
Other Current Liab	1,443	1,330	1,379	1,862	1,990
LT Debt	0	999	900	400	400
Other LT Liabilities	1,934	1,433	1,420	1,320	1,220
Shareholder's Equity	2,667	3,029	2,819	2,770	2,964
Minority Interests	5	6	8	9	11
Total Cap. & Liab.	6,221	7,155	6,872	6,721	6,959
Non-Cash Wkg. Capital	(1,088)	(1,086)	(980)	(1,435)	(1,531)
Net Cash/(Debt)	347	914	506	1,339	1,691
Debtors Turn (avg days)	7.6	7.3	7.3	9.4	9.4
Creditors Turn (avg days)	10.4	10.7	9.6	9.1	9.3
Inventory Turn (avg days)	13.4	15.1	14.9	16.5	16.9
Asset Turnover (x)	1.2	1.0	1.1	1.2	1.3
Current Ratio (x)	0.5	1.5	1.2	1.1	1.2
Quick Ratio (x)	0.3	1.3	1.0	1.0	1.1
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	N/A	23.4	38.9	72.5	72.5
Z-Score (X)	3.4	3.6	3.6	3.6	NA

Source: Company, DBS HK

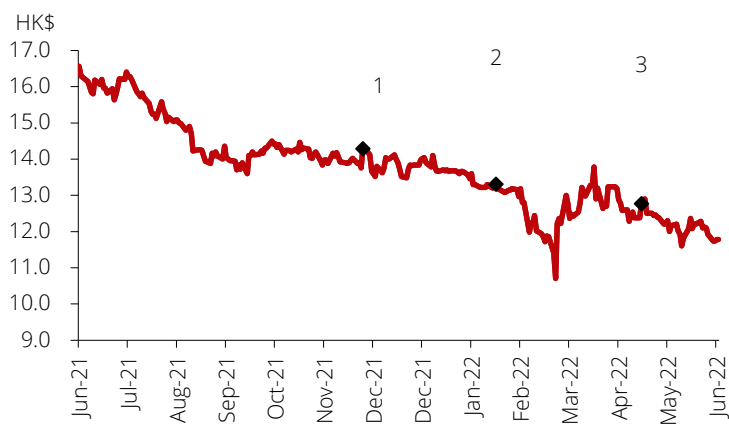
Cash Flow Statement (HK\$ m)

FY Mar	2020A	2021A	2022A	2023F	2024F
Pre-Tax Profit	114	391	51	205	450
Dep. & Amort.	1,234	1,099	968	894	854
Tax Paid	(112)	(29)	(30)	(28)	(42)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	34	241	(53)	104	105
Other Operating CF	175	4	92	13	11
Net Operating CF	1,445	1,705	1,028	1,189	1,378
Capital Exp.(net)	(501)	(276)	(420)	(420)	(420)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	18	11	1	0	0
Net Investing CF	(483)	(265)	(419)	(420)	(420)
Div Paid	(488)	(58)	(223)	(210)	(162)
Chg in Gross Debt	0	1,179	(100)	(500)	0
Capital Issues	(37)	(25)	0	(1)	0
Other Financing CF	(936)	(808)	(938)	(860)	(857)
Net Financing CF	(1,461)	288	(1,260)	(1,570)	(1,019)
Currency Adjustments	(12)	20	143	1,134	413
Chg in Cash	(511)	1,747	(508)	333	352
Opg CFPS (HK\$)	2.43	2.53	1.87	1.87	2.20
Free CFPS (HK\$)	1.63	2.46	1.05	1.33	1.65

Source: Company, DBS HK

Café de Coral

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	25-Nov-21	HK\$13.76	HK\$18.00	Buy
2:	9-Feb-22	HK\$13.20	HK\$15.50	Buy
3:	3-May-22	HK\$12.38	HK\$15.50	Buy

Source: DBS HK

Analyst: Alison Fok

Alice Hui

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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