

WEDNESDAY, 18 JULY 2012

Field Notes

**JOLLIBEE FOODS CORPORATION (JFC)
Chinese business facing challenges**

- Challenges in China.** Jollibee has 354 stores in China, representing 14% of JFC's total store network. JFC said that it is currently encountering difficulties in growing same store sales and increasing profitability. Same store sales, which measure sales of stores open for more than one year, was flat to negative during the 1Q12. According to JFC, sales were negatively affected by scandals concerning the product quality of its competitors (quality of soup base and milk tea products) as sentiment for their products was also negatively affected. Management also admitted that it is encountering difficulties in competing with global brands such as KFC, Pizza Hut and McDonalds which have a larger size in terms of store network and marketing budget.

Due to the said challenges, JFC's goal of having the international business account for 50% of sales will most likely be delayed from 2013 to 2016. Unfortunately, this would mean that it would take longer for its Chinese operations to contribute to the bottomline and drive earnings growth. JFC's entire China business, including head office and commissary, is still operating at a loss. The company expects to breakeven by 500 stores, which means that it will have to grow its store network by 41.2% from its current level.

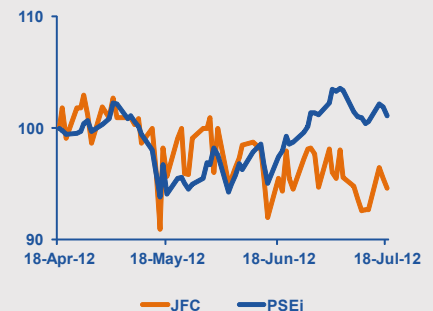
- Domestic business carrying the load.** On the positive side, domestic sales continued to be strong. Although the number of restaurants of major brands – Chow King, Greenwich, and Red Ribbon – declined during 1Q12, same store sales still grew by high single-digit level. Management said the decline in the number of stores was largely due to the closure of unprofitable locations. Domestic system-wide sales, which include both company and franchise owned sales, is still expected to carry the load contributing 82% of the total system-wide sales as of the 1Q12.
- Focus on growth instead of margins.** JFC also said that it is adopting a different strategy to grow profitability. Commodity prices are falling globally. However, instead of pocketing the savings, JFC is reducing the price of some of its products and passing on the cost savings to its customers. JFC said that the resulting growth in sales and profits will more than offsets the drop in margins resulting from this strategy.
- Planning global expansion.** Although Jollibee already has an exposure in China, Vietnam, Middle East, and the US, it also wants to establish a presence in key growth markets such as India, and Indonesia. JFC is looking for a partners or acquisition targets that will give it access to these markets.

Forecast Summary (PhpMil)

Year to December 31 (Php Mil)	2010	2011	2012E	2013E
Revenues	47,958	53,372	72,562	79,951
% change y/y	9.3	11.3	36.0	10.2
Gross Profit	9,569	10,117	13,560	15,316
%change y/y	18.0	5.7	34.0	12.9
Gross Profit Margin (%)	20.0	19.0	18.7	19.2
Operating Income	3,301	3,599	4,609	5,685
%change y/y	22.8	9.0	28.1	23.3
Operating Margin (%)	6.9	6.7	6.4	7.1
Net Income	2,665	3,198	3,779	4,671
%change y/y	14.9	20.5	14.6	8.4
Net Margin (%)	5.6	6.0	5.2	5.8
EPS (in Php)	2.58	3.08	3.71	4.58
%change y/y	14.6	19.2	16.3	8.4
RELATIVE VALUE				
P/E(X)	40.4	33.9	28.1	22.8
P/BV(X)	6.6	6.3	5.5	4.9
ROE(%)	16.4	18.5	19.2	20.9
Dividend Yield (%)	0.8	2.4	1.1	1.2

*Source: JFC, Citiseconline estimates
SHARE DATA

Rating	HOLD
Ticker	JFC
Fair Value (Php)	107.50
Current Price	104.10
Upside (%)	3.27

SHARE PRICE MOVEMENT

ABSOLUTE PERFORMANCE

	1M	3M	YTD
JFC	-0.86	-5.36	15.09
PSEI	3.84	1.13	19.96

MARKET DATA

Market Cap	108,552.05Mil
Outstanding Shares	1,038.51Mil
52 Wk Range	80.00 - 120.00
3Mo Ave Daily T/O	42.10Mil

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Challenges in China

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Reviewing forecast

We are reviewing our forecast on JFC in light of the recent challenges posed by China. We reiterate our HOLD rating on JFC with a FV estimate of Php107.5/sh. We believe the stock is fairly valued trading at 28.3X FY 12 P/E.

INVESTMENT RATING DEFINITIONS

BUY	HOLD	SELL
Over the next six to twelve months, we expect the share price to increase by 15% or more.	Over the next six to twelve months, we expect the share price move within a range of +/- 15%.	Over the next six to twelve months, we expect the share price to decline by more than 15%.

TOP PICK DEFINITION

A stock that is included in our "Top Pick" list has to meet the following criteria: 1.) It must belong to a sector with neutral to positive outlook; 2.) It must have double digit earnings growth for the current and the succeeding fiscal year; 3.) Its share price appreciation potential must be above 15% as of the date it was included in the list; and 4.) It must have an upward intermediate term trend.

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