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Finanční analýza společnosti Lianhua Supermarket Holdings

Financial Analysis of the Lianhua Supermarket Holdings Company

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  2. Description of the financial analysis methodology
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List of Abbreviations  
Declaration of Utilization of Results from the Bachelor Thesis  
List of Annexes  
Annexes

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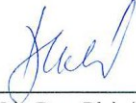
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**The declaration**

“Herewith I declare that I elaborated the entire thesis, including all annexes, independently.”

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# 1 Introduction

In the whole text, the financial statement of Lianhua Supermarket Holding Company Limited (“Lianhua Supermarket” or “Market”) will be introduced. According to analysis the annual reports from 2008 to 2012 of Lianhua, many important information will be shown. And after the processes of selecting, evaluating, calculating, we’ll know how this company works and which kind of policies has been made.

The main objective of the thesis is to assess Lianhua Supermarket’s present financial position. Knowing a company’s operations, expenses management and credit policies is a very important skill to investors and company’s managers.

Understanding the knowledge of financial tools is the first step to do. And most of the theories were found in *Financial Analysis Techniques*, written by Thomas R. Robinson, CFA. Normally different financial tools are used in different condition. Common-size analysis and financial ratios are introduced in this part. Common-size analysis includes horizontal analysis and vertical analysis. And financial ratios contain activity ratios, solvency ratios, liquidity ratios, profitability ratios and market ratios. More details about these methodologies will be explained in the second chapter.

Why choose Lianhua Supermarket as this study object? Firstly, it’s a Chinese company, and I worked there during my last summer holiday. So this company is easier to be analyzed. Secondly, Lianhua is the fourth supermarket in China, just behind Carrefour. There are three main segments of retail outlets in Lianhua’s operation, namely hypermarkets, supermarkets and convenience stores, catering for the diverse needs of consumers. In a sense, Lianhua Supermarket is more representative among Chinese supermarkets. More information like Lianhua’s history, main competitors, operation structures and stock prices will be showed clearly and deeply in the third part of this text.

When the balance sheet, the statement of cash flow, the income statement, the statement of shareholder’s equity and the financial environment have been known, it is time to use financial tools, including common-size analysis, financial ratio analysis, DuPont analysis and gradual analysis. These boring data from annual report will be transferred by financial

tools to a certain conclusion, and the reason of policies deciding or financial statement changing will also be explained. It's the fourth part of this thesis, and is also the main part.

Based on the analysis above, we can know whether Lianhua is valuable to be concerned and invested. The last chapter is conclusion. It's focused on the results and summaries of the study.



## 2 Description of the financial analysis methodology

Before all the investment decisions and recommendations, it is necessary to evaluate the company's financial reports, which include financial statements and other data. Influences from other companies and in different periods will also be considered. For example, if company A has liabilities of \$20,000, and company B has liabilities of \$300,000, is company A less risk? We cannot say "YES" or "NO" directly, it depends in part on the size of company and each company's industry. So we will use different financial tools in every different situation.

In this chapter, main theories are based on books *Corporate Finance: A Practical Approach*, written by Michelle R. Clayman, CFA and *Financial Analysis Techniques*, written by Thomas R. Robinson, CFA.

### 2.1 Common-size analysis

Common-size analysis mainly involves financial statements data and their changes over the time, in order to identify the trends and major differences. A common-size statement is mostly useful when one attempts to compare a company to similar companies of different size. It seems like that common analysis creates a ratio between every financial statement item and the base item. And the basic items are usually expressing as total assets or revenue. It is also called a one hundred percent statement. There are two types in common-size analysis, one is **horizontal common-size analysis**, and another is **vertical common-size analysis**.

#### **Horizontal analysis**

In horizontal common-size, people should analyze the evolution of financial statements data over the time or their changes with respect to a given period as a benchmark. In this case, each item on the income statement in a given year is compared to a base year, such as the prior year or some arbitrary starting year. So it's often also called "common-base-year analysis".

## **Vertical analysis**

It's normal to use vertical common-size analysis to analyze patterns in profitability, investments and financing.<sup>1</sup> According to this way, we can get changes in the proportions of selected benchmarks, such as total revenues, total assets, and total liabilities. What is one company's financial format? How is the company financing itself? What's the difference between one company with its competitors? All these question will be solved through vertical common-size analysis.

## **2.2 Financial ratio analysis**

Financial ratios are used to weigh and evaluate the operating performance of a company, by expressing one quantity in relation to another. It's a comparison of financial data in the form of financial ratios to exam the financial health of a company. And financial ratios are calculated using company's financial statement and market data. Meanwhile, the general economic cycle and company-specific should be also considered.

Ratio is an indicator of some parts of company's operation, which means that we can know what happened from the ratio, but cannot get the reason. Always, ratios will be influenced by differences in accounting policies across companies, so it's necessary to adjust financial data before. And not all ratios are needed; it's a meaningful way to select a relevant ratio or ratios to answer the research question.

We can separate 19 significant ratios into five primary categories; there are activity ratio, liquidity ratios, solvency ratios, profitability ratios and market ratios.

### **2.2.1 Activity Ratios**

Activity ratios measure how well a company uses its assets. And the ratios in this part may well explain why one company is able to use its assets more rapidly than another. All these ratios relate the balance sheet to the income statement, and their forms show as days of turnover and number of turnovers. Inventory turnover, receivables turnover, long-term

<sup>1</sup> From: Corporate Finance: A Practical Approach, Michelle R. Clayman, CFA, Chapter 7 Financial Statement Analysis, p.314

assets turnover and total assets turnover will be introduced here.

**Inventory turnover** is the ratio of cost of goods sold to inventory. It means how many times a year the company used up an average stock of goods. The equation for inventory turnover equals the cost of goods sold divided by the average inventory. Inventory turnover is also known as inventory turns, stockturn, stock turns, turns, and stock turnover.<sup>2</sup>

$$\text{Inventory Turnover} = \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}} \quad (2.1)$$

Because turnover is a large part of revenue, inventory turnover is very important to a company. If the ratio is higher, the inventory turnover is faster; inventory occupancy will be lower and more liquid. As for a low result, it always means overstocking, obsolescence, or deficiencies in the product line or marketing effort.<sup>3</sup> But in some times, a low rate may not be a bad thing, such as where higher inventory levels occur in anticipation of rapidly rising prices or expected market shortages. This matter is isolated, normally higher rate is better.

**Receivables turnover** is a measure of the liquidity of receivables, calculated as net credit sales divided by average net trade receivables. It also shows how long customers pay on average, during a time. It's useful in estimating one company's credit policy. A high ratio shows the company has a high speed in receiving, and the average receivable period is short. And a low ratio means the company may have bad debts.

$$\text{Receivable turnover} = \frac{\text{Turnover}}{\text{Average Receivables}} \quad (2.2)$$

If ratio is high, that relates that the company's extension of credit and collection of accounts receivable is efficient. A low ratio means the company should change its credit

<sup>2</sup> From Wikipedia – Inventory turnover: [http://en.wikipedia.org/wiki/Inventory\\_turnover](http://en.wikipedia.org/wiki/Inventory_turnover)

<sup>3</sup> From Legacy Associates- How to more effectively Convert Your Inventory into Cash; written by Terry Hill, [http://www.legacyai.com/Convert\\_Inventory.html](http://www.legacyai.com/Convert_Inventory.html)

policies in order to ensure the quickly collection of credit that is not earning interest for the company.

Payable turnover is a measure of the liquidity of payables. The ratio shows how fast a company pays off its creditors. According to this ratio, we can know a company's cash situation.

$$\text{Payable turnover} = \frac{\text{Turnover}}{\text{Average Payables}} \quad (2.3)$$

Normally, a higher ratio is worse, because high ratio means the time between purchase of goods and payment for them is short, so the payables are paid more quickly. And low payable turnover means company spends a long time in paying its supplier.

**Long-term assets** turnover measures whether a company uses its long-term assets efficiently.

$$\text{Long-term assets turnover} = \frac{\text{Revenue}}{\text{Average Long-term Assets}} \quad (2.4)$$

**Total assets turnover** seems more widely to be used, when compared with long-term assets. It measures the relationship of the firm's assets to sales. If other items are same, a higher turnover ratio is appropriate, because it indicates that a firm generates more sales and more cash flow from a given investment in assets.

$$\text{Total assets turnover} = \frac{\text{Revenue}}{\text{Total Assets}} \quad (2.5)$$

In some capital-intensive industries such as petroleum, maschinenbau and heavy manufacturing companies, total asset turnover ratio is typically less than one, while in retail and services companies it may be over ten. Company can increase the ratio according to reduce the price.

### 2.2.2 Liquidity Ratios

Liquidity ratio measures company's ability to deal with its immediate or short-term liabilities and obligations. Lenders and suppliers who provide products and services to the firm on credit should be more concerned about it. It's help for these people to estimate if a firm be worth to invest.

The **current ratio** is the primary measure of a company's liquidity. It defined as current assets divided by current liabilities.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Short-term Liabilities}} \quad (2.6)$$

We cannot say how high is appreciate of the ratio. It does not depend only on the type of the company, but it also depends on the costs and benefits. An example is that a current ratio of 1.0% is acceptable for a taxi company but may be not for a big steel firm. The more predictable a firm's cash flow, the lower the acceptable current ratio.

The **quick ratio** is similar to the current ratio, except that it excludes inventory, which is usually the least liquid current asset.

$$\text{Quick Ratio} = \frac{\text{Cash+Short-term Marketable Investments+Receivables}}{\text{Short-term Liabilities}} \quad (2.7)$$

If the result is low, it may have two reasons: it's not easy to sell so many types of inventory which are partially completed items, special-purpose items and so on; another reason is inventory is typically sold on credit, which means it becomes an account receivable before being transferred into cash.

### 2.2.3 Solvency Ratios

The solvency ratios measure company's ability to meets its long-term obligations, and

allow analyst to measure the prudence of the debt management policies of the firm. Solvency ratio relates a company's financial risk level. Compared with business risk, financial risk is arising from the company's obligation to meet required payments, such as the payment of promised interest and financial transactions that include company loans in risk of default.

Component-percentage solvency ratios mainly assess a company's debt level with its total assets and equity capital. Investor can decide whether the company on debt financing is safety or not. Component percentage is included in firm's value of capital, which represented by debt, stock, assets and other items.

The **debt-to-assets ratio** measures the assets financing with debt.

$$\text{Debt-to-assets ratio} = \frac{\text{Total Debt}}{\text{Total Assets}} \quad (2.8)$$

Investors are more risky with higher debt to assets ratios. On the same time, high debt to assets ratio may because of low borrowing capacity of a firm, which in turn will lower the firm's financial flexibility. Like all financial ratios, a company's debt ratio should be compared with their industry average or other competing firms. The debt ratio shows the structure of a company's assets which are financed through debt. If the ratio is less than 0.5, equity is the main way of assets financing. If the ratio is higher than 0.5, debt may be the main way of company's assets financing. Companies with high debt ratios are said to be "highly leveraged," not highly liquid as stated above. If creditors need repayment of debt, a company with a high debt ratio could be dangerous; it's hard to achieve this demand.

The **debt-to-equity ratio** measures both debt and equity among the firm's total capital. Debts here are usually in long-term.

$$\text{Debt-to-equity ratio} = \frac{\text{Total Debt}}{\text{Total Equity}} \quad (2.9)$$

Both creditors and investors concern on this formulation. Someone like banks especially notice this part of company, because that high debt to equity ratio means the risk they can't call in a loan.

The **financial leverage** also called the equity multiplier. It is measured as the ratio of total debt to total assets; "The greater the use of debt relative to equity in financing the company, the greater the financial leverage will be."<sup>4</sup>

$$\text{Financial leverage} = \frac{\text{Assets}}{\text{Equity}} \quad (2.10)$$

Another way to show how assets and equity relate to debt is coverage ratios. This type includes interest coverage, and fixed charge coverage.

The **interest coverage ratio** is also named time interest earned (TIE), it measures the number of times interest can be paid out of operate profit.

$$\text{Interest coverage ratio} = \frac{\text{EBIT}}{\text{Interest Payment}} \quad (2.11)$$

If a company's EBIT is \$200 and the interest is \$20, so the ratio is 10, and we can say that interest is covered 10 times. The more times earnings cover interest, the safer it is to lend more money to a company.

The **fixed charge coverage** relates fixed charges, or obligations, to the cash flow generated by the company. It measures how many times a company's earning before interest and taxes can cover the interest and lease payment.

<sup>4</sup> From: Corporate Finance: A Practical Approach, written by Michelle R. Clayman, CFA, , chapter7 Financial Statement Analysis, p. 330

$$\text{Fixed charge coverage} = \frac{\text{EBIT} + \text{Lease Payment}}{\text{Interest Payment} + \text{Lease Payment}} \quad (2.12)$$

Compared to the interest coverage ratio, it's same that a higher ratio implies stronger solvency, and gives investor a confidence to service its debts.

#### 2.2.4 Profitability Ratios

It's a very useful ability which generates profit on capital invested to a company's overall value and the value of the securities it issues. Profitability relates a company's competitive position in the market and the quality of management. And the profitability ratios measure the return during a period of time. The higher the profitability ratios, the better competitive position a company has.

**Operating profit margin** is a measurement of what proportion of a company's revenue is left over after paying for variable costs of production, such as wages, raw materials, etc. A healthy operating margin is required for a company to be able to pay for its fixed costs, such as interest on debt.

$$\text{Operating profit margin} = \frac{\text{Operate Profit}}{\text{Revernuess}} \quad (2.13)$$

Operating margin is usually increasing faster than it might be the result of the improvements in controlling operating costs. A decreasing operating profit margin will be an indicator of deteriorating control over operating costs.

**Net profit margin** is also called return on sales (ROS). This ratio is the lowest line in the common-size income statement. And manager can control the income statement of revenue, cost, and expense through this ratio.

$$\text{Net profit margin} = \frac{\text{Net Profit}}{\text{Revenues}} \quad (2.14)$$



**Return on assets** adds the effectiveness of asset management to ROS. ROA shows how a company uses assets to earn a profit. It measures what the company gets back, when the company has made the investment in assets.

$$\text{Return on assets (ROA)} = \frac{\text{Net Profit}}{\text{Total Assets}} \text{ or } \frac{\text{Operating Profit}}{\text{Assets}} \quad (2.15)$$

A company earns return on its equity capital, including minority equity, preferred equity, and common equity, it's appropriate to use **return on equity**. And this ratio is affected by the financial leverage of the company.

$$\text{Return on equity (ROE)} = \frac{\text{Net Profit}}{\text{Equity}} \quad (2.16)$$

If the company has plenty of debts, ROE will be higher than ROA in good times and lower in bad times. Assets equal to equity plus debt. So if there is little or nearly no debt, ROE and ROA are similar.

### 2.2.5 Market Ratios

Market ratio is a way to compare the company's value and the stock market price. So these ratios measure in the price of its stock. There are three market ratios will be introduced: EPS, P/E, divided payout ratio.

The **EPS** is the amount of income earned during a period per share of common stock. The higher of the ratio, the greater of the profit created.

$$\text{Earning per share (EPS)} = \frac{\text{Net profit}}{\text{Number of shares outstanding}} \quad (2.17)$$

The **P/E** is the ratio of the price per share of common stock to the earnings per share.

The P/E ratio can use the reported earnings from the latest year (called a trailing P/E ) and employ an analyst's forecast of next year's earnings (called a forward P/E ).

$$\text{Price-to-earnings ratio (P/E)} = \frac{\text{Market Price Per Share}}{\text{EPS}} \quad (2.18)$$

The higher P/E is more profitable to a company. A high expected level of growth by the company will result in a high P/E. It is seemed as a proxy for assessing investors to generate cash flows in the future, so it must be used with caution. It's no meaningful of P/E, when a company's earning is zero or little.

**Dividend payout ratio** is the ratio of cash dividends paid to earnings for a given times.

$$\text{Dividend payout ratio} = \frac{\text{Dividends Paid}}{\text{Net Profit}} \quad (2.19)$$

### 2.3 Pyramidal decompositions and influence quantification

Pyramidal decomposition enables to analyze what leads to the value of financial ratio, such as which factors have impact on its value or evolution. This way is aimed at expressing selected ratio as a product of component ratios. One of the most famous formulations is DuPont analysis.

**DuPont analysis** separates ROE which expressing the basic ratio as a product of component ratios. It is named after an American company DuPont, which is the first one to use this formula. DuPont analysis identity breaks down return on equity into three components: net profit margin, assets turnover and financial leverage. And then we can get the result that what different aspects of performance influenced the company's profitability as measured by ROE. Management can also use this ratio to determine which parts they should main concentrate on to improve ROE. In a word, the DuPont equations express relationships between ratios that give insights into successful operation.

$$\text{ROE} = \frac{\text{Net profit}}{\text{Equity}} = \frac{\text{Net income}}{\text{Revenues}} \cdot \frac{\text{Revenues}}{\text{Total Assets}} \cdot \frac{\text{Total Assets}}{\text{Equity}} \quad (2.20)$$

Because of:

$$\frac{\text{Net income}}{\text{Revenues}} = \frac{\text{Net income}}{\text{EBT}} \cdot \frac{\text{EBT}}{\text{EBIT}} \cdot \frac{\text{EBIT}}{\text{Revenues}} \quad (2.21)$$

So:

$$\text{ROE} = \frac{\text{Net income}}{\text{EBT}} \cdot \frac{\text{EBT}}{\text{EBIT}} \cdot \frac{\text{EBIT}}{\text{Revenues}} \cdot \frac{\text{Revenues}}{\text{Total Assets}} \cdot \frac{\text{Total Assets}}{\text{Equity}} \quad (2.22)$$

ROE = Tax burden · Interest burden · EBIT margin · Assets turnover · Financial leverage

Certain types of retail operations, particularly stores, may have very low profit margins on sales, and relatively moderate leverage. But if they have very high turnover and sell plenty of their assets per year, the ROE of such firms may be higher. It depends on the performance of turnover. So in many times, retailers prefer to get more store sales rather than open a new store.

As for influence quantification, there are four methods: methods of gradual changes, methods of decomposition with surplus, logarithmic decomposition method and functional decomposition method. We can get the results of whose change have caused change in the basic ratio and which component ratios impacted to the change in basic ratio at most.

Method of gradual changes is the most common method, because of its simple calculation and useful results. This method is used to quantify how the change in component ratio impacts change in the basic ratio.

$$\begin{aligned} \Delta X_{a1} &= \Delta a_1 \cdot a_{2,0} \cdot a_{3,0} \\ \Delta X_{a2} &= a_{1,1} \cdot \Delta a_2 \cdot a_{3,0} \\ \Delta X_{a3} &= a_{1,1} \cdot a_{2,1} \cdot \Delta a_3 \end{aligned} \quad (2.23)$$

Symbols:

X - basic ratio

$\Delta X$ - absolute change in the basic ratio

A - component ratio

$\Delta$  absolute change in the component ratio

### 3 Overview of Lianhua Supermarket Holding company

The third chapter is focused on introducing Lianhua Supermarket, including its history, company structure, main competitors and its market share in China. According to this part, it will leave a general impression of Lianhua. And this also the first step for investors to decide whether to invest in this company. The main sources used in this chapter are annual report of Lianhua.<sup>5</sup>

#### 3.1 History of Lianhua Supermarket

Lianhua Commercial, the predecessor of Lianhua Supermarket, was established in Shanghai by United Trading, with a registered capital of CNY 12 million<sup>6</sup> and opened its first supermarket in Shanghai in September 1991. Chinese retail industry also started at this time, there were 94 supermarkets whose annual turnover is more than CNY 1200 million in 1991 in the whole China, and the number increased to 150 in 1992, as for 1995, it becomes 624. So the time in 1990s is a good period for retail company developing.<sup>7</sup>

Approached by Shanghai foreign investment committee, Lianhua Supermarket Company restructured to sino-foreign joint venture with the introduction of SIAMCL<sup>8</sup> and Mitsubishi Corporation as its shareholders and adopted the name Shanghai Lianhua in 1997.

At 1997 there were 230 stores of Lianhua, and their turnover reached to CNY 24 billion per year. Lianhua Supermarket didn't satisfy its current development situation, it decided to expand to other provinces in China.

In December 1999, in order to raise additional funds for the development of its directly operated hypermarket business and the establishment of a new distribution center, the registered capital of Lianhua was increased by CNY 180 million to approximately CNY 300 million. In May 2001, in order to raise additional funds to satisfy the requirements for the expansion of its retail network, the registered capital of Lianhua was further increase by CNY100 million to approximately CNY400 million. Lianhua was converted into a joint

<sup>5</sup> The annual reports of Lianhua can be founded in:

[http://www.lhok.com.cn/view.php?c=en\\_&MenuListDef=2&menuListId=20201](http://www.lhok.com.cn/view.php?c=en_&MenuListDef=2&menuListId=20201)

<sup>6</sup> CNY, also called RMB, is the official currency of China

<sup>7</sup> China retail industry's development trend, written by Qiong Yao, 2005,

<http://www.cnki.com.cn/Article/CJFDTotal-SYJJ200518007.htm>

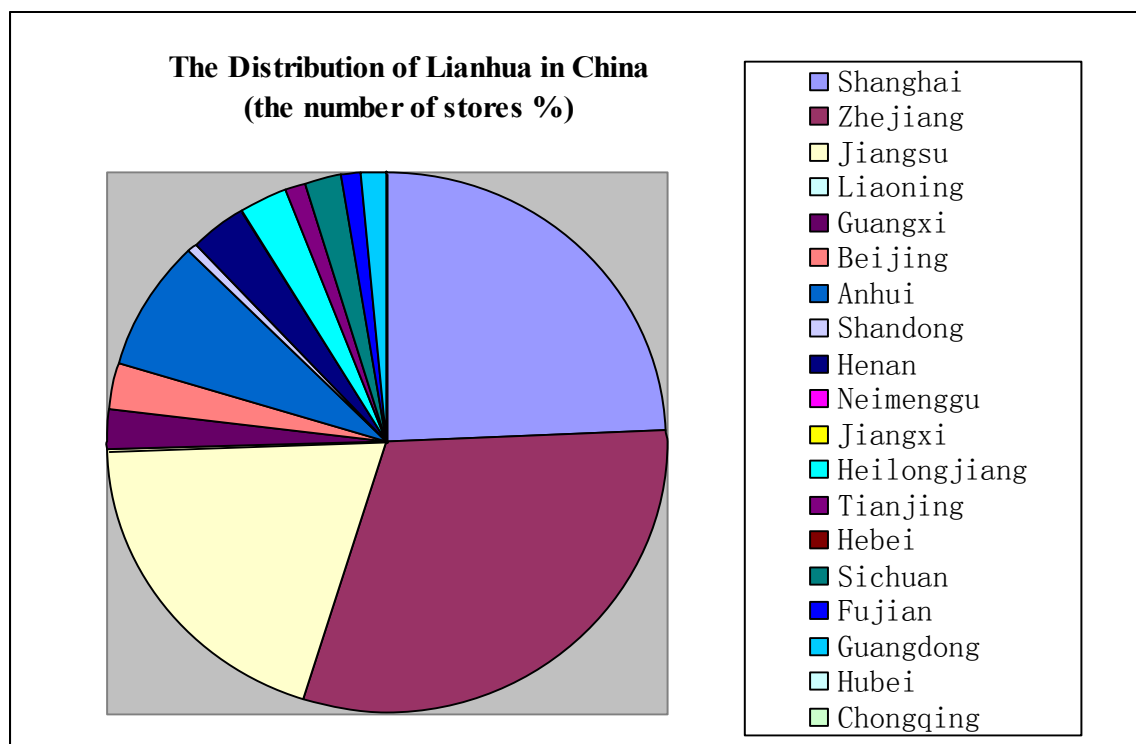
<sup>8</sup> SIAMCL is Shanghai Industrial Asset Management Company

stock limited company in late 2001.

At this time, the most glorious time of Lianhua is coming. From 2000 to 2002, Lianhua was the top of the league table of 100 Chinese retail and catering companies in three times, which was certificated by China General Chamber of Commerce and China Commercial Information Center.<sup>9</sup>

In the past 22 years, Lianhua has developed into a nationwide chain retail operator with a full range of retail segments, expanding through a combination of organic growth, franchises and merger and acquisitions. As at 31 December 2011, Lianhua Supermarket and its subsidiaries operated a total of 5,150 outlets (excluding those operated by the Company's associated companies) spanning 19 provinces and municipalities across the nation. With data from annex 1, figure 3.1 is made to show that approximately 85% of Lianhua's outlets located in the Eastern China area. Eastern China is Lianhua's birthland, and is also its main battlefield.

Figure 3.1 The Distribution of Lianhua in China



Source: Lianhua Annual Report 2011, p.3, author

<sup>9</sup> Data base of CCSFA  
<http://www.ccf.org.cn/viewCatalog.do?method=viewCatalog&catalogId=ff8080812e2b85c8012e2b9bc5800001>

The Company has kept its leading position in the fast moving consumer goods retail industry in China. And on 27 June 2003, Lianhua Supermarket was listed on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) as the first Chinese retail chain operators .

In 2011, in order to better adapt to market developments, satisfy various consumer needs and improve the operate structure, Lianhua started an e-commerce business and launched a shopping website on line named “Lhmart” in December. The new website adopted an “online + offline” business model, combining the advantages of physical outlet network resources to offer the options of home delivery or in-store pickup to meet the emerging need of online shopping.

Lianhua Supermarket became a Hong Kong Hang Seng Composite Index constituent stock in 2011 in recognition of its market capitalisation and trading volume, and was awarded “Listed Company of Best Growth Potential” of China Securities Golden Bauhinia Awards. (Annual Report 2011, p.14)

Figure 3.2 Lianhua Stock Prices



Source: finet.hk

From the figure 3.3, it’s clear that the stock price went down in 2008, and then had a

great increase from 2009 to 2011. At that time, it reached the top, and then went down sharply from 2011 to now. Because of inflation and stronger market competitions, rate of gross profit was decreased. At the same time, more and more hypermarket enlarged quickly resulted in the cost increasing.

### **3.2 Company structure**

Lianhua operates in three main retail segments – hypermarkets, supermarkets and convenience stores, in order to satisfy the different needs of consumers. These segments operate under the brand names of “Century Mart”, “Lianhua Supermarket”, “Hualian Supermarket” and “Lianhua Quik”, respectively. By the end of 2011, there were 152 hypermarkets, 669 supermarkets and 940 convenience stores in direct operation; and 2315 supermarkets and 1069 convenience stores in franchised operation.

**Centurymart hypermarkets** mainly cater to these consumers who want a “one-stop” shopping experience, and consumers can spend a long time with their friends or families shopping in hypermarket. Whatever they want, they can always find in centurymart. Besides basic services, consumers will find various ancillary services like bank, restaurant, medicine shop, laundry. Main characteristics of centurymart are large space, various products and full scale service. So consumers go there, not only for shopping, but also for enjoying their spare time.

**Lianhua supermarkets** usually located in urban areas with large need for daily necessities, such as residential areas and city centre. Normally old residential areas in China are not suitable for a new supermarket, because there must be many small old stores with a good number of loyal consumers. Besides, young people like move to new residential area, but elders prefer live in old residential area. These elders’ purchase powers are very low. Supermarkets have smaller store size than century hypermarkets, but bigger than quick convenience stores.

**Quik convenience stores** target consumers with the need for fast, efficient, convenient and 24-hour shopping services. These stores usually have small store size, but high product prices. That is because consumer who chooses quick convenience store must need primarily necessities products, such as drinks, foods. These stores trend to be located in



placed with high pedestrian flow, like airport, train station and so on. Quik convenience stores are usually open for 16 to 24 hours a day. ”

Like other companies, the highest level of Lihuan is General Meeting of Shareholders, and next is Supervisory Board and president & CEO. The president & CEO orders General Manager Office. And the GM office manages 22 departments, there are Ministry of Justice, Center for Strategic Studies, Security Department, General Accounting Department, Audit Department, Human Resource Department, Training Center, Information Center, Development Department, Management of Franchise Operation Department, Network Research Department, Project Management Department, Hypermarket Operation Department, Supermarket and Convenience Store Operation Department, Integrated Management Operation Department, Commodity Management Department, Import Department, Investment Service Center, Live and Fresh Produce Processing and Distribution Centre, Commercial Integrated Management Department, Distribution Centre and Asset Management Department.

Besides these divisions in the main company, Lianhua built many different subsidiary companies, including subsidiaries and associates companies. But all the subsidiary companies share the same information systems with the construction of a regional office information platform, which consisting of the OMS (Operation Management System), DMS (Distribution Management System), BMS (Business Management System), and FAS (Financial Assistant System). Information system integration ensures a unified flow in business, logistics, information and capital, achieving consistency, completeness and accuracy of data, and providing information sharing among headquarters, regional offices and outlets, enhancing its ability of outlet operations and information management and thus laying a solid foundation for further growth.( Annual Report 2011,p.27 )

### **3.3 Main competitors**

The table 3.1 shows the top 4 of fast moving consumer goods retail industries in China, in 2011. As it is evident, Lianhua was the second in 2011, the group sold CNY 6 807 630 million with 5221 stores. In the top 10, there are 4 foreign-founded companies: RT-Mart, Carrefour, Wal-Mart, and Tesco; and the top1, CR Vanguard and the seventh one NGS

Supermarket are state owned holding companies directly under the central government. Others in the top10 are Chinese holding companies like Lianhua.

Table 3.1 Top 4 Fast Moving Consumer Goods Retail Industries in China in 2011<sup>10</sup>

Rank	Company	2011 Retail Sales(Million)	Number of Stores
1	CR Vanguard	8270000	3977
2	Lianhua	6807630	5221
3	RT-MART	6156700	185
4	Carrefour China	4519581	203

Source:CCFA-China Chain Store & Franchise Association

### **CR Vanguard**

CR Vanguard also named China Resources Vanguard Co.Ltd, is a multi-business holding enterprise group registered and operating in Hong Kong. Its parent company's predecessor was Liow & Company established in Hong Kong in 1938 and was renamed China Resources Company in 1948, which is one of the global top 500 companies now. Its supervision was transferred from the General Office of CPC Central Committee to the Central Ministry of Trade (the present Ministry of Commerce) in 1952 and to the State-owned Assets Supervision and Administration Commission in 2003 when it was listed as a key state-owned enterprise. After then, it developed very quickly.<sup>11</sup>

Compared with Lianhua, CR pays more attention to high consumption group. The Group owns various well-known brands including Vanguard, Suguo, Fun2, Chinese Arts & Crafts, CRare, Ole, blt, V>nGO, Voi\_la!, VIVO, Pacific Coffee, etc. There are not only supermarkets and hypermarkets like Vanguard and Suguo, but also many special stores; for example, CRare is medicine store, VIVO main for fitness product.

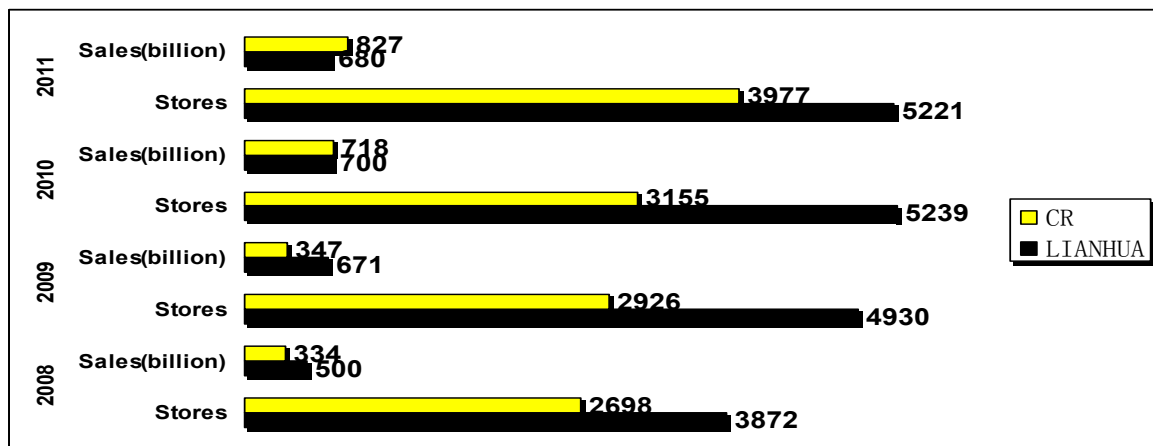
Table 3.1 Comparison between Lianhua and CR sales and stores from 2008 to 2011 (Currency in millions of CNY)

<sup>10</sup> From: [http://www.cdfa.org.cn/pages/upload/up\\_fj/pR7p0yq9h7Ym1337150553850.pdf](http://www.cdfa.org.cn/pages/upload/up_fj/pR7p0yq9h7Ym1337150553850.pdf)

<sup>11</sup> Source from official website of CR: <http://www.crc.com.cn/aboutus/about/>

	2008		2009		2010		2011	
	Stores	Sales	Stores	Sales	Stores	Sales	Stores	Sales
LIANH								
UA	3872	500	4930	671	5239	700	5221	680
CR	2698	334	2926	347	3155	718	3977	827

Figure 3.3 Comparison between Lianhua and CR sales and stores from 2008 to 2011



Source:CCFA-China Chain Store & Franchise Association, author

From the table and figure above, it's clear that although the number of CR stores is lower than Lianhua, the turnover still be higher. When Lianhua had 3872 stores in 2008, CR just had 2698 stores, so the turnover in Lianhua is higher than CR. But after 2010, influenced by the global financial crisis, Lianhua sales growth became slowly, while government supported the development of CR. And CR sales CNY 827 billion in 2011 with 3977 stores, while Lianhua sales CNY 680 billion with 5221 stores. In some times, number of stores doesn't represent turnover.

### Carrefour China

After China took the Reform and Opening policy in 1978, Chinese market was opened, and more and more foreign companies came to China. Considering these four foreign-founded companies in the top 10 fast moving consumer goods retail industries in China, RT-Mart is from Taiwan, Carrefour is from France, Wal-Mart is from American and Tesco is from British. Carrefour China developed better than others these years.

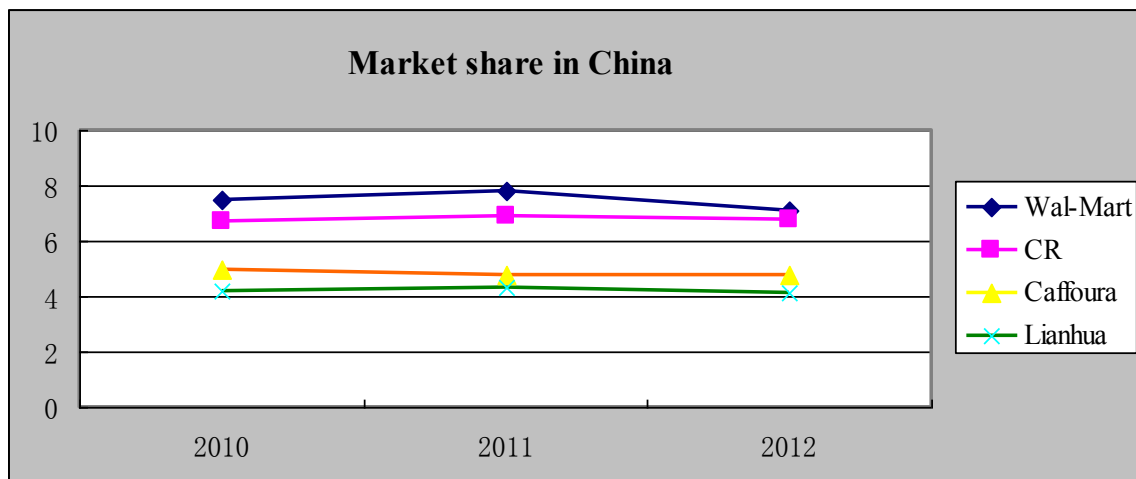
Carrefour China started its first store in 1995 in Shanghai. And it cooperated with Lianhua to built a joint venture, Shanghai Lianjia Supermarket in 1996 in order to get more preferential policies. Lianhua and Carrefour are not only competitors, but also partners. Carrefour needed Lianhua's help to open Chinese market, and Lianhua studied many valuable manager's and operation's experience from Carrefour. For example, suppliers should pay a fixed fee to get access permission of Carrefour, while some supermarkets like Wal-Mart doesn't have this rule. Carrefour focused on the number of stores, it has a high speed in enlarging scale, and Lianhua is same. But Carrefour doesn't has its own distribution center, while Lianhua has.

Table 3.2 Market Share in China<sup>12</sup>

Rank	Company	2010	2011	2012
4	Wal-Mart	7.5	7.8	7.1
7	CR	6.7	6.9	6.8
8	Carrefour	5	4.8	4.8
9	Lianhua	4.2	4.3	4.1

(Source from Kantar Worldpanel, Jian Yu, 21/02/2013)

Figure 3.4 Market share in China



Source from Kantar Worldpanel,author

From table 3.2 and figure 3.4, we can see that market share of Wal-Mart is the highest among CR, Carrefour and Lianhua, and Lianhua's market share is the lowest. Market share

<sup>12</sup> Data from Kantar Worldpanel: <http://www.kantarworldpanel.com/cn/news/news-articles/12Q4-Retail-Press-Release>

of Lianhua, CR and Wal-Mart increased in 2010, but decreased from 2011 to 2012. This change proves the fierce competition in the retail market.

## 4 Financial analysis of Lianhua Supermarket Holding company

This chapter is the main part of this thesis. When the basic information has already been known, it's time to analyze Lianhua's statement from 2007 to 2011, with common-size analysis, ratio analysis and DuPont analysis. This chapter's objective is focused on estimate how Lianhua is operating, financing and managing. All data in this chapter is from Lianhua's annual reports. The calculations are based on financial statements of the company which are available in annexes (Annex 2, 3 and 4)

### 4.1 Common-size analysis

In chapter 2, it's said that there are two way in common-size analysis, one is vertical common-size analysis, and another one is horizontal common-size analysis. Now we can analyze Lianhua's balance sheets and income statements from 2007 to 2011.

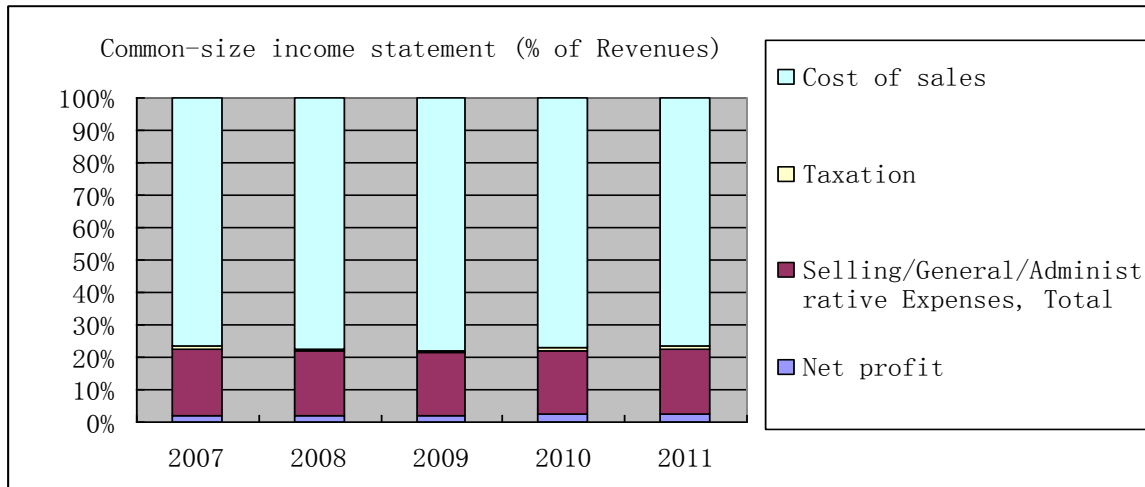
#### 4.1.1 Vertical common-size analysis

Firstly, we start with vertical-common size analysis. We choose revenues as basic item in income statement and choose total assets as basic item in balance sheet. And then, we can see composition of revenues and assets respectively.

Table 4.1 Vertical common-size analysis of income statement (% of revenues)

	2007	2008	2009	2010	2011
Revenues	100.00%	100.00%	100.00%	100.00%	100.00%
Cost of sales	76.72%	77.57%	77.86%	77.01%	76.55%
Gross profit	23.28%	22.43%	22.14%	22.99%	23.45%
Selling/General/Administrative Expenses, Total	20.43%	19.86%	19.17%	19.70%	20.29%
Profit before taxation	2.85%	2.57%	2.97%	3.30%	3.16%
Taxation	1.00%	0.57%	0.78%	0.84%	0.84%
Net profit	1.86%	2.00%	2.20%	2.45%	2.32%

Figure 4.1 Vertical common-size analysis of income statement



From table 4.1 and figure 4.1, it's clear that cost of sales is the largest part of revenues, and expenses also occupy large proportion. When cost of sales increased from 2007 to 2009 as a percentage of revenues, the expenses decreased at the same time. And when cost of sales decreased from 2009 to 2011 as a percentage of revenues, the expenses increase from 19.17% to 20.29% of revenues. It's very easy to understand, firstly because recent years, employees' salaries are higher and higher. From 2010, many cities in China improved the lowest level of citizens' wage. For example, in Shanghai the lowest income level increased 16.7% in 2010, and until 2011 the lowest wage level was adjusted in 24 provinces nationwide with an average growth of 22%. Secondly, with more and more stores opening, there are more administrative expenses like rental costs and employees salaries should be paid. So the total expenses have been increasing. Even though the costs of sales are increasing, the increasing rate wouldn't catch up with expenses, so the proportion in revenues is decreasing.

The net profit also increased quickly relative to revenue. On the one hand, in 2011 gross domestic product (GDP) in China reached CNY 47 156.4 billion, representing an increase of 9.2% over 2010 at comparable prices according to the National Bureau of Statistics of China. The Chinese government continued to launch various measures to stimulate consumption, which played a more important role in economic growth and fostered further development of the retail industry. And on the other hand, the income of urban and rural

residents grew steadily. Total annual income per capita of urban resident amounted to CNY 23 979 and income of rural residents grew faster than that of urban residents with net annual income per capita amounting to CNY 6977. People have more money and then the purchase power will be increasing.

The next part of this chapter is focused on the brief analysis of turnovers generated by various types of stores. Based on company's annual reports, the percentages relative to the overall turnover have been calculated and demonstrated in the chart.

Table 4.2 Percentages of turnovers (%)

	2007	2008	2009	2010	2011
Turnover	100.00	100.00	100.00	100.00	100.00
Hypermarkets	54.44	51.22	54.29	56.28	58.44
Supermarkets	36.27	41.27	38.80	36.41	34.95
Convenience stores	8.43	6.85	6.47	6.74	6.30
Other businesses	0.86	0.66	0.44	0.57	0.31

Figure 4.2 Percentages of turnovers (%)

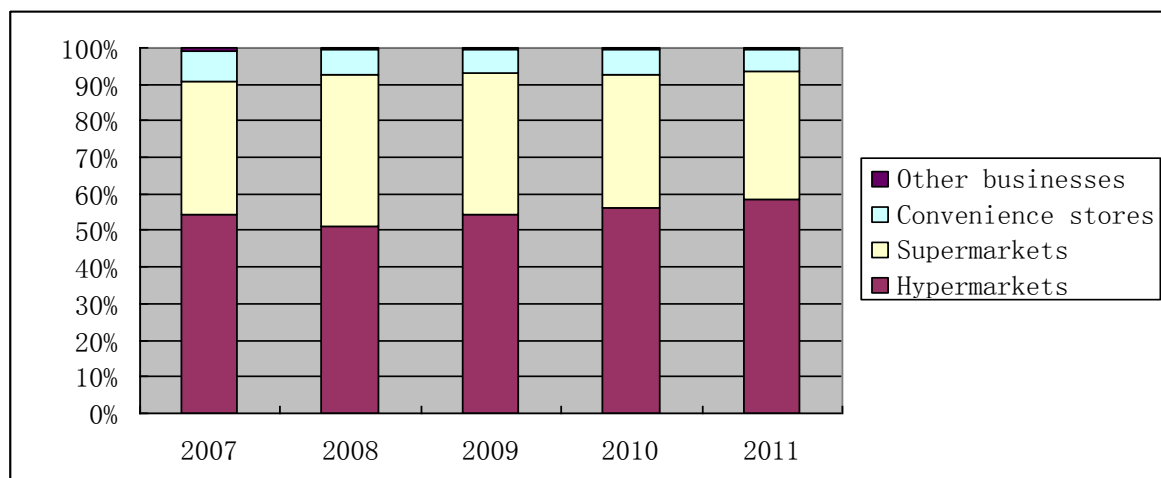
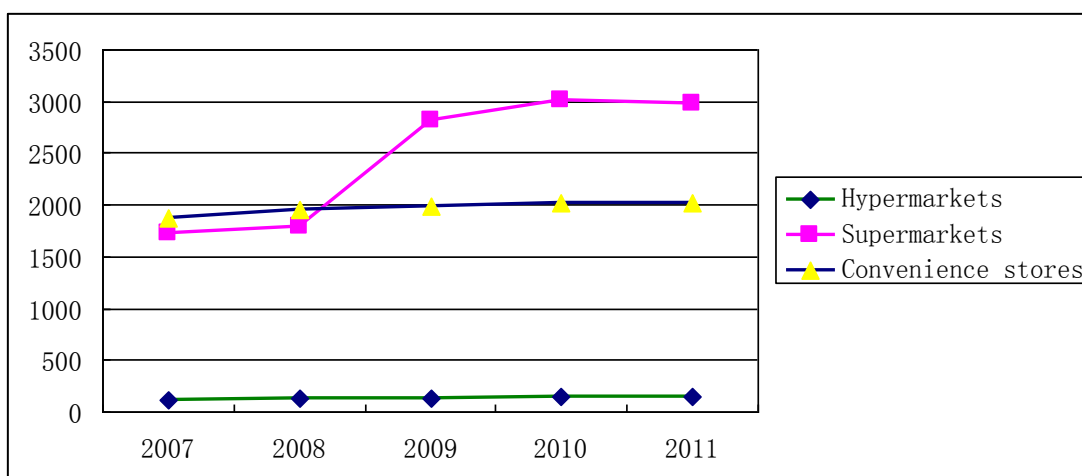


Figure 4.3 Number of stores





According to table and figure 4.2, it shows that hypermarket's turnover is the highest, the turnover is even more than half of the total turnover but the number of hypermarkets is the lowest. Supermarkets are the second even though the number of supermarkets is the largest after 2008. Lianhua puts hypermarket as they emphasis object of profit and supermarket is their main object. In order to suffer the financial crisis, Lianhua's number of supermarkets rose from 1788 to 2818. More networks shared the main risk. But because of the weak profit and fierce competition, Lianhua had to close 30 supermarkets in 2011.

Table 4.3 Vertical Common-size analysis in assets (% of total assets)

	2007	2008	2009	2010	2011
Cash and Cash equivalents	43.51	24.28	27.19	30.25	27.40
Total Receivables	5.47	4.87	3.65	3.94	4.83
Total Inventory	16.69	16.57	15.95	15.10	16.84
Prepaid Expenses	0.00	23.60	15.11	12.36	8.43
Other Current Assets, Total	2.05	1.77	4.61	4.06	1.89
<b>Total Current Assets</b>	<b>67.72</b>	<b>71.09</b>	<b>66.50</b>	<b>65.72</b>	<b>59.39</b>
Property/Plant/Equipment, Total	22.38	18.37	19.66	15.62	16.43
Intangibles, Net	1.68	1.34	1.19	0.96	0.92
Long Term Investments	7.59	8.53	10.90	16.32	21.78

Note Receivable - Long Term	0.39	0.48	1.58	1.24	1.36
Other Long Term Assets	0.24	0.19	0.17	0.13	0.11
<b>Total Non-Current Assets</b>	<b>32.28</b>	<b>28.91</b>	<b>33.50</b>	<b>34.28</b>	<b>40.61</b>
<b>Total Assets</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

Figure 4.4 Vertical Common-size analysis in assets (% of total assets)

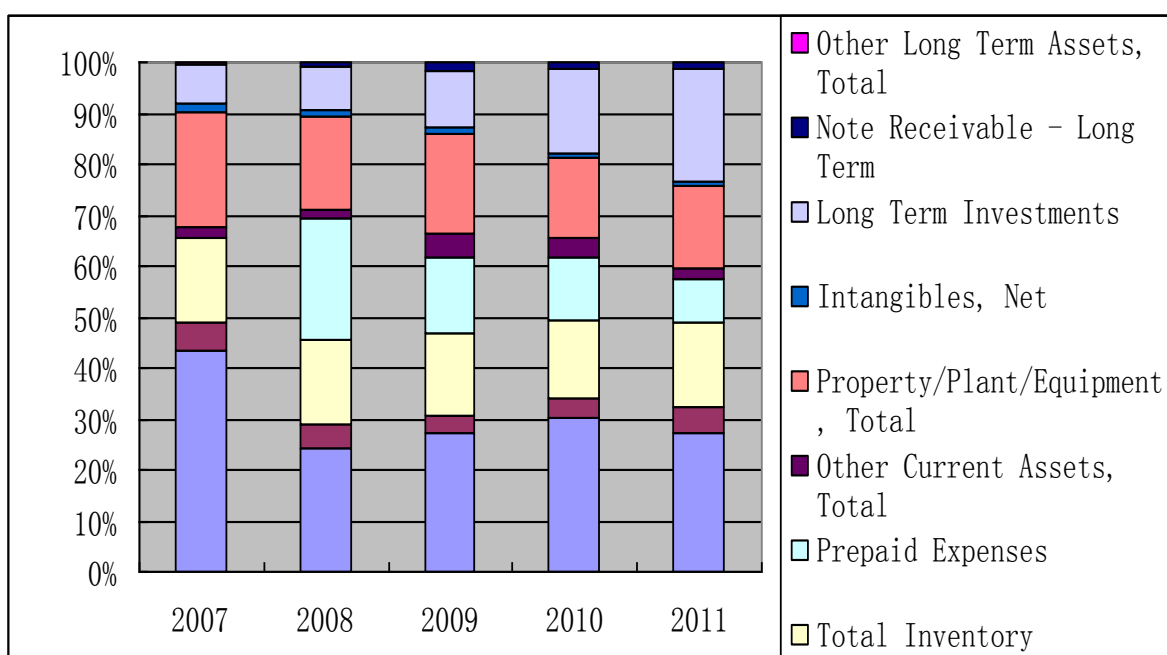


Table 4.3 and figure 4.4 represent how Lianhua's investments have changed from 2007 to 2011. It's obviously that cash and cash equivalents occupy a large proportion of total assets. It's just a special characteristic in retail industry with positive and quickly cash flow. When cash ratio is higher, the capital return comes faster. If company gets capital return on time, it can re-invest, and get more profit. But cash and cash equivalents' proportion had a sharply decrease in 2008 because of the financial crisis. In these years, the proportion has been increasing slowly.

The proportion of total property, plant and equipment and prepaid expenses also decrease evidently, while there is an increase in the long-term investment. It also reveals that Lianhua has opened many new outlets recent years, and we can't deny that the price is

rising unsustainably especially in rental price.

Inventory also plays an important role in retail industry. In 2007, Lianhua's total inventory was 16.69% relative to total assets, and then it went to fall till 2010. And in 2011, it raised again. Enough inventories can satisfy consumer's demand, but too much inventory will block capital turnover. Since the operation and scale of the sales are expanding rapidly in 2011, Lianhua's exception of turnover is higher than the real turnover, so the inventory relative to total assets is higher.

Table4.4 Vertical Common-size of equity and liabilities (% of total equity and liabilities)

	2007	2008	2009	2010	2011
Share capital	5.39	4.54	4.0	3.37	5.51
Reserves	14.01	13.64	11.94	12.32	10.80
Equity attributable to owners of the Company	19.40	18.18	15.98	15.69	16.31
Non-controlling interests	3.05	2.92	3.01	1.78	1.51
<b>Total equity</b>	22.45	21.10	18.99	17.48	17.83
Deferred tax liabilities	0.61	0.39	0.33	0.27	0.23
Trade payables	0.00	0.00	0.00	0.00	0.01
Bank borrowing	9.65	11.24	11.50	11.25	10.85
Other payables and accruals	9.65	11.24	11.50	11.25	10.85
Coupon liabilities	41.43	43.33	45.04	47.19	48.03
Deferred income	0.00	0.00	0.20	0.12	0.08
Taxation payable	0.71	0.41	0.60	0.58	0.80
<b>Total liabilities</b>	77.55	78.90	81.01	82.52	82.17
<b>Total equity and liabilities</b>	100.00	100.00	100.00	100.00	100.00

Figure 4.5 Vertical Common-size of equity and liabilities (% of total equity and liabilities)

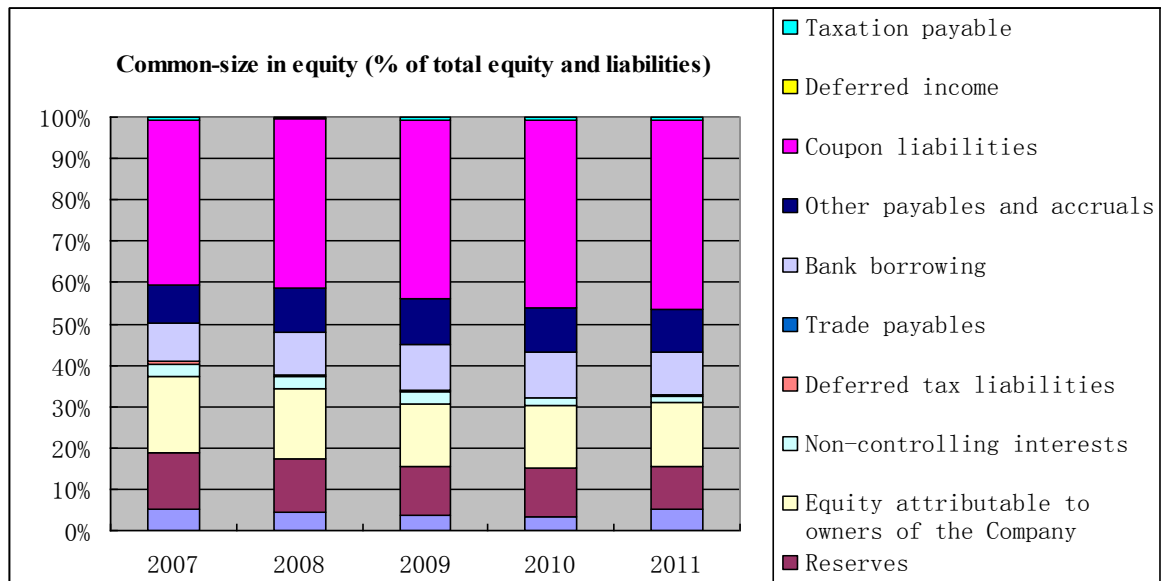


Figure 4.5 and table 4.4 represent the proportion of total equity and liabilities. The proportion of Coupon liabilities is the highest. This item is very different to others, because it includes value card. Value card of Lianhua is named Lianhua OK card. This OK card is used for purchase, and it can totally replace cash. From 2002, Lianhua cooperated with many other companies, and sold their OK card to these companies as their employees' welfare. When these companies' staff had the OK card, of cause they prefer to purchase in Lianhua, or not other supermarket like Wal-Mart, Carrefour and so on. This card's cost equals to zero for company, but has huge return.

The reserves and share capital are contained in equity attributable to owners of the company. It's the second part of total liabilities and equity. Because of the positive trend in Lianhua's development, the capital share increased from 622 million to 1119.6 million.

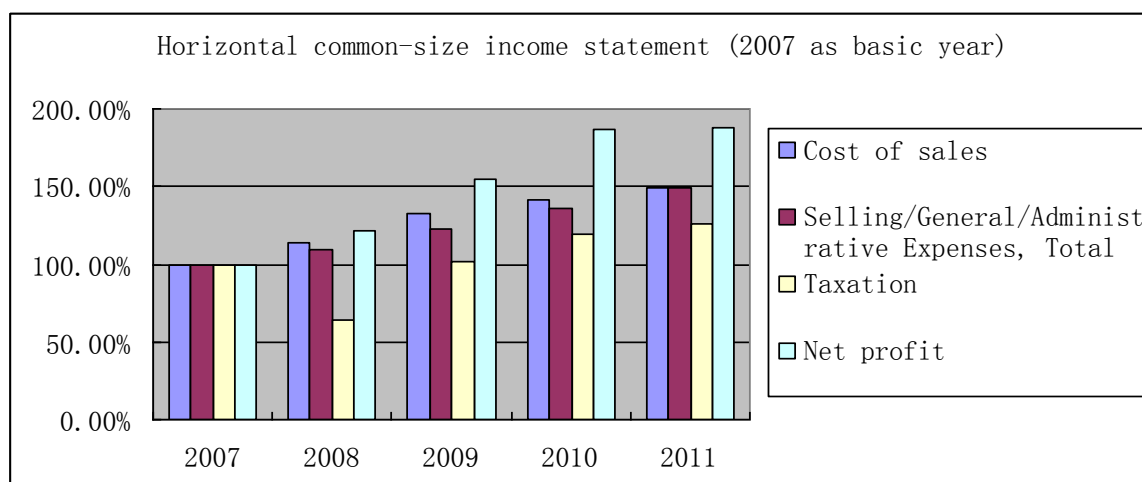
#### 4.1.2 Horizontal common-size analysis

Compared with vertical common-size analysis, horizontal common-size analysis focuses more on every year's difference. When each item's proportion in the basic item is clear, it's time to analyze how they changed over a period time.

Table 4.5 Horizontal common-size analysis of income statement (2007 as basic year)

	2007	2008	2009	2010	2011
Revenues	100.00	112.46	130.75	141.12	150.05
Cost of sales	100.00	113.71	132.68	141.64	149.72
Gross profit	100.00	108.34	124.36	139.39	151.14
Selling/General/Administrative Expenses, Total	100.00	109.32	122.70	136.09	149.07
Profit before taxation	100.00	101.30	136.27	162.96	166.02
Taxation	100.00	63.89	101.77	118.94	126.10
Net profit	100.00	121.43	154.84	186.64	187.49

Figure 4.6 Horizontal common-size analysis of income statements (2007 as basic year)



The horizontal common-size analysis of income statement is provided in table 4.5 and figure 4.6. Net profit has a great increase from 2007 to 2011. Because of the macro-environment of economic slowdown and consumption's shrinking as the results of the financial crisis, the state took the policy of "subsidizing farmers' purchase of electrical appliances" and supporting "supermarkets' move to open outlets in rural areas" under the "marketing project for ten thousand villages and a thousand rural areas".<sup>13</sup> Lianhua grasped this opportunity to develop its business in the second and third tier market. The balance and scale distribution reduced the negative influence of Lianhua. At the same time,

<sup>13</sup> From annual report 2008, p.23

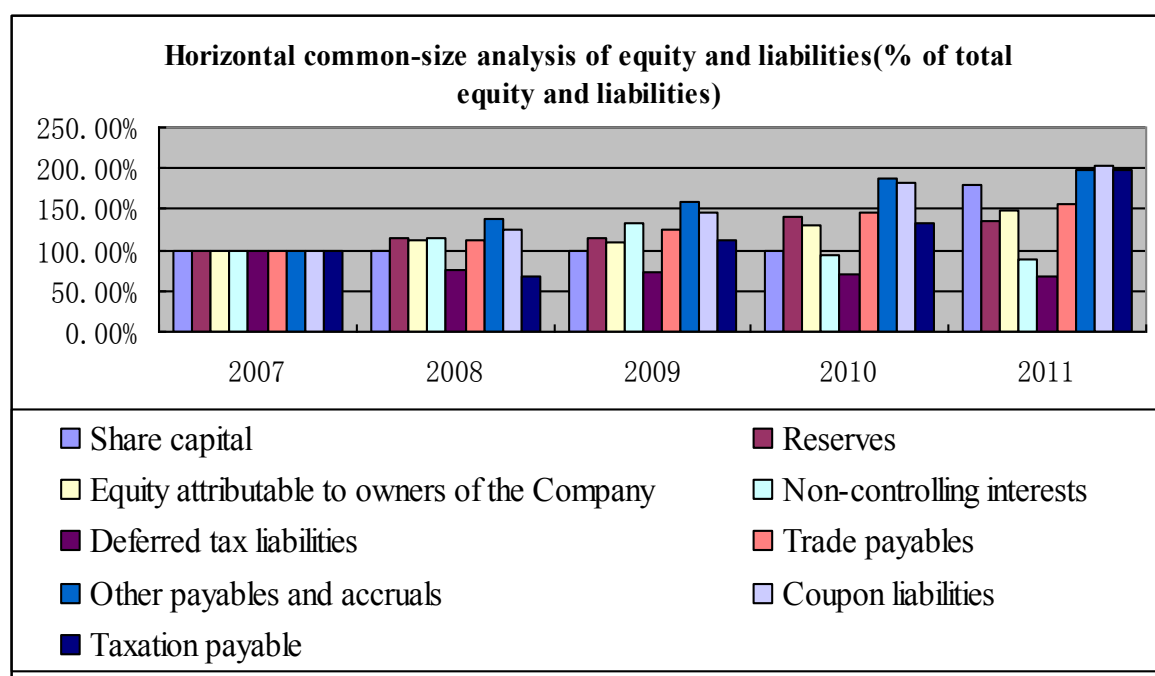
expenses and cost of sales also increased. The reason was explained above.

In 2008, there was an obviously decrease of taxation. And that was because of the new corporation law. In the past, business income tax rate was 33%, but since 2008 it is just 25%. Even though the profit was increasing, the taxation went down yet,

Table 4.6 Horizontal common-size analysis of equity and liabilities(% of total equity and liabilities)

	2007	2008	2009	2010	2011
Share capital	100.00	100.00	100.00	100.0%	180.00
Reserves	100.00	115.55	113.87	140.62	135.71
Equity attributable to owners of the Company	100.00	111.23	110.02	129.33	148.01
Non-controlling interests	100.00	113.73	132.11	93.54	87.47
<b>Total equity</b>	100.00	111.57	113.02	124.47	139.79
Deferred tax liabilities	100.00	76.23	73.29	70.36	67.42
Trade payables	100.00	111.04	123.93	146.96	155.15
Other payables and accruals	100.00	138.29	159.26	186.38	197.98
Coupon liabilities	100.00	124.15	145.20	182.06	203.99
Taxation payable	100.00	68.01	113.00	131.70	198.02
<b>Total liabilities</b>	100.00	120.77	139.53	170.11	186.47
<b>Total equity and liabilities</b>	100.00	118.70	133.58	159.87	175.99

Figure 4.7 Horizontal common-size analysis of equity and liabilities(% of total equity and liabilities)



In above table and figure, coupon liabilities increased quickly because of its huge benefits, and until 2011 it rose to 203.99% compared with 2007. Share capital was equal from 2007 to 2010, but in 2011 it increased to 180% in order to better development. In 23 June 2011, shareholders of Lianhua decided to increase the registered share share capital from CNY 622 billion to CNY 1 119.6 billion.<sup>14</sup>

Deferred tax liabilities reduced and it's also a normal change. Deferred tax assets relate to certain tax losses and deductible temporary differences.

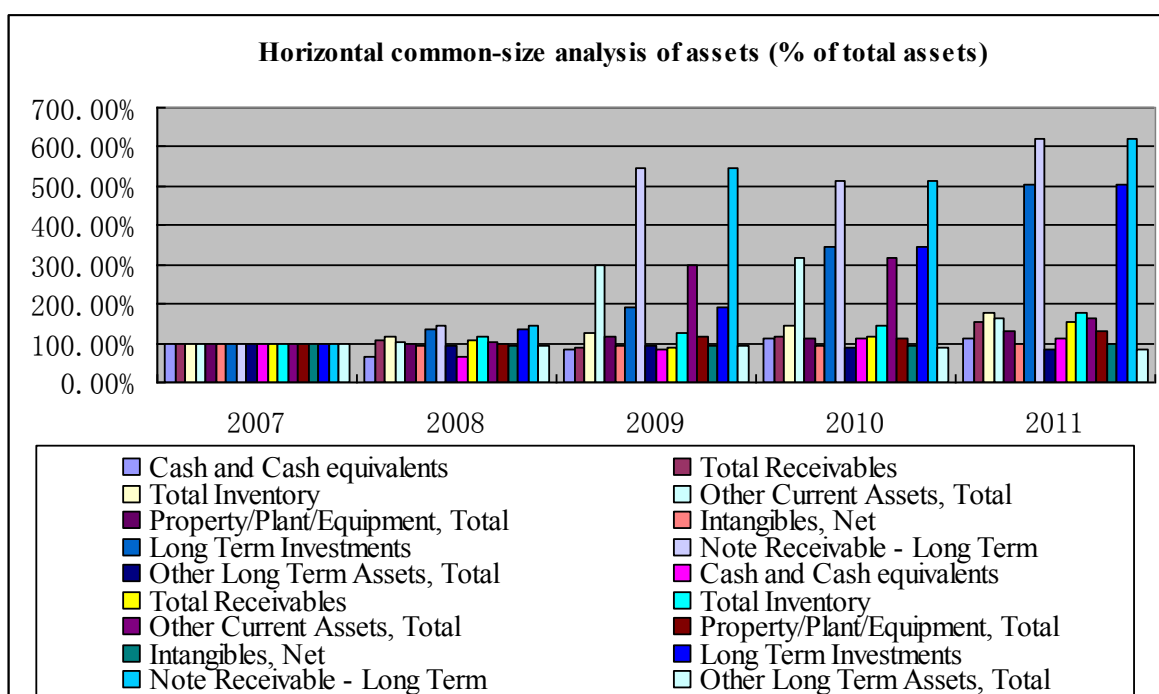
Table 4.7 Horizontal common-size analysis of assets (% of total assets)

	2007	2008	2009	2010	2011
Cash and Cash equivalents	100.00	66.23	83.47	111.13	110.83
Total Receivables	100.00	105.71	89.06	115.23	155.57
Total Inventory	100.00	117.87	127.67	144.68	177.57
Other Current Assets, Total	100.00	102.66	300.59	317.18	162.07
Total Current Assets	100.00	124.62	131.19	155.15	154.36
Property/Plant/Equipment, Total	100.00	97.42	117.34	111.61	129.22

<sup>14</sup> From annual report 2011, p.45

Intangibles, Net	100.00	94.78	94.83	91.58	96.35
Long Term Investments	100.00	133.39	191.78	343.66	504.92
Note Receivable - Long Term	100.00	146.04	544.28	513.86	619.99
Other Long Term Assets, Total	100.00	94.60	91.56	87.36	81.97
Total Non-Current Assets	100.00	106.30	138.60	169.77	221.38
Total Assets	100.00	118.70	133.58	159.87	175.99

Figure 4.8 Horizontal common-size analysis of assets (% of total assets)



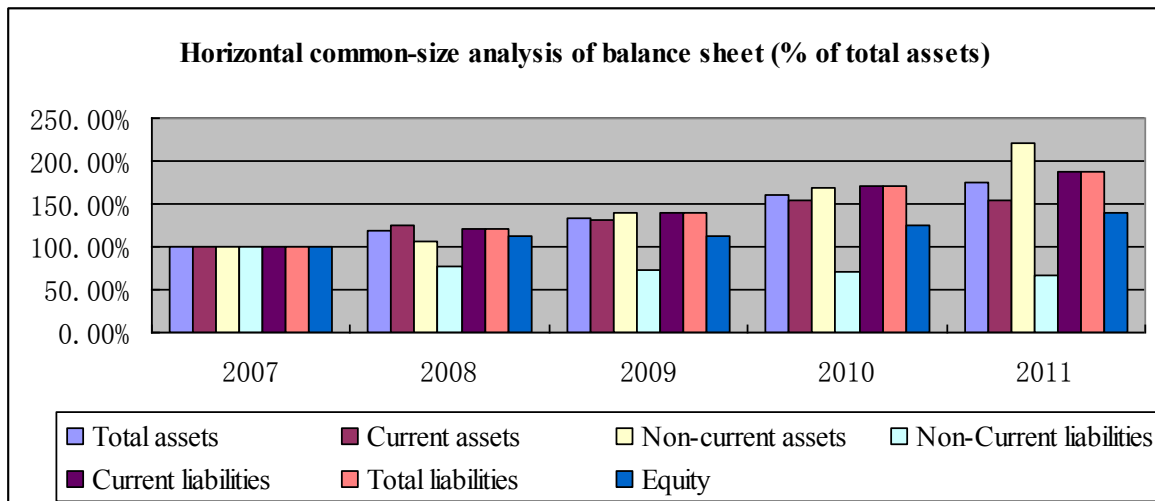
Note receivable changes very fast from 2008 to 2011, and in 2011 it came to 619.99% of 2007. Because in 2007 and 2008, there was no receivable of prepaid rental, but in 2009 this item gained CNY 138 481 million. Long-term investment also raised to 504.92% in 2011. Higher long-term investment means Lianhua can have more number of stores and more population of staff. Meanwhile, intangible liabilities, property, plant, and equipment expenses, cash and cash equivalents have an obviously decrease in 2008.



Table 4.7 Horizontal common-size analysis of balance sheet (% of total assets)

	2007	2008	2009	2010	2011
Total assets	100.00	118.70	133.5	159.87	175.99
Current assets	100.00	124.62	131.19	155.15	154.36
Non-current assets	100.00	106.30	138.60	169.77	221.38
Non-current liabilities	100.00	76.23	73.29	70.36	67.42
Current liabilities	100.00	121.12	140.05	170.90	187.41
Total liabilities	100.00	120.77	139.53	170.11	186.47
Equity	100.00	111.57	113.02	124.47	139.79

Figure 4.9 Horizontal common-size analysis of balance sheet (% of total assets)



Non-current assets increased fastest from 2007 to 2011, especially in 2011. The reason is that there were 9 new hypermarkets opened. Managers in Lianhua though their company has bright look in the future. And there are frequent food safety incidents in 2011. Facing these challenges, Lianhua built a multi-level inspection system to eliminate fake and shoddy goods. Total assets, current assets, current liabilities, total liabilities and equity are

also constantly increasing in these years. Specifically, the proportion of non-current liabilities is little, so the growth in current liabilities and total liabilities seems same. Besides, non-current liabilities constantly go down during these five years.

## 4.2 Financial ratio analysis

After these visual views from common-size analysis within income statement and balance sheet, it's time to have more professional and detailed opinions. Lianhua's operating, financing and debts statement will be introduced with activity ratio, liquidity ratios, solvency ratios and profitability ratios.

### 4.2.1 Activity Ratios

Table 4.8 Inventory turnover ratio

	2007	2008	2009	2010	2011
Turnover	18086857	20702441	24017720	25905344	27520176
Inventory	1926462	2270696	2459506	2787111	3420822
<b>Inventory turnover ratio</b>	<b>9.39</b>	<b>9.12</b>	<b>9.77</b>	<b>9.29</b>	<b>8.04</b>

Figure 4.9 Inventory turnover ratio



Inventory turnover ratio is very important for companies, especially for retail industries. Retailers buy commodities from middle men, wholesalers or producers. If a retail company has enough inventory, it can satisfy different and plenty consumption demand. And it can also provide enough goods for consumer choosing. This ratio can be calculated

with formula 2.1, and the results were shown in table 4.8.

Lianhua’s inventory turnover ratio is not simply decreasing or decreasing. Its ratio had a slightly increase in 2007, and then raised in 2008, but decreased from 2009 to 2011. In 2011, each item of Lianhua’s inventory was sold out 4.08 times per year. Although turnover is continue rising during these five years, but the inventory’s growth is faster. Holding too much inventory is not good for a retail company. High level of inventory will lead to more operating working capital, and that means the cash flow will be reduced. As Ehrhardt (2011, p.92) said, “low inventory turnover ratio makes us wonder whether the firm is actually holding obsolete goods not worth their stated value.”

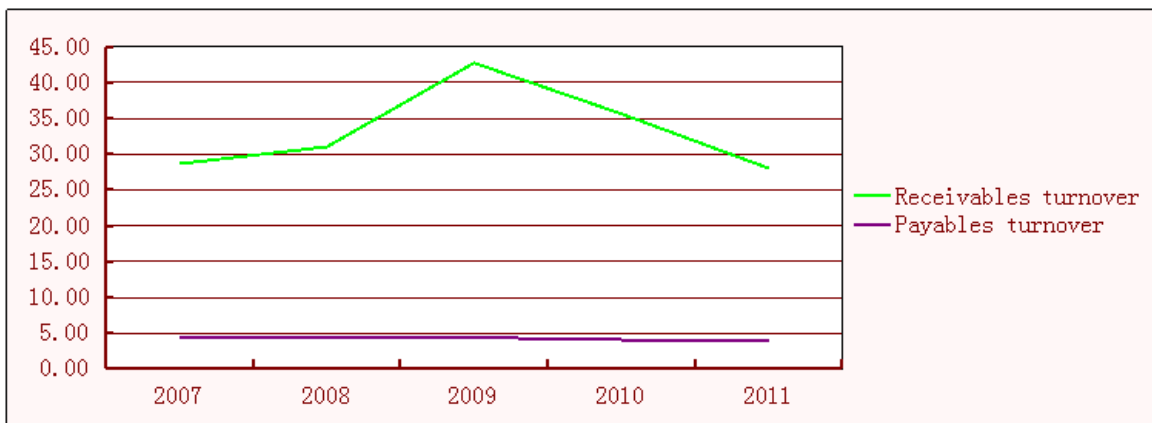
In recent years, there are more and more retail companies. As for Lianhua, its competitors always open new stores nearby it. It’s not easy to continue profit. A real example is that in 2011, Lianhua had no choice but to close 9 supermarkets in north China. Nearly each Wu-mart opposites to one Lianhua.

Table 4.9 Receivables turnover and Payable turnover

	2007	2008	2009	2010	2011
Turnover	18,086,857	20,702,441	24,017,720	25,905,344	27,520,176
Receivables	631,129	667,192	562,059	727,222	981,856
<b>Receivables turnover</b>	<b>28.65</b>	<b>31.02</b>	<b>42.73</b>	<b>35.62</b>	<b>28.02</b>
Payables	4099058	4819890	5464325	6342506	6871478
<b>Payables turnover</b>	<b>4.41</b>	<b>4.30</b>	<b>4.40</b>	<b>4.08</b>	<b>4.00</b>

Formula 2.2 and 2.3 are used here to calculate receivables turnover and payable turnover. Because in these two ratio, one is to indicate how many times a company collects receivables in a period time, and another one is to indicate how many times a company pays off its suppliers. We can see the results in table 4.9, and the figure below will show more clearly.

Figure 4.10 Receivables turnover and Payable turnover



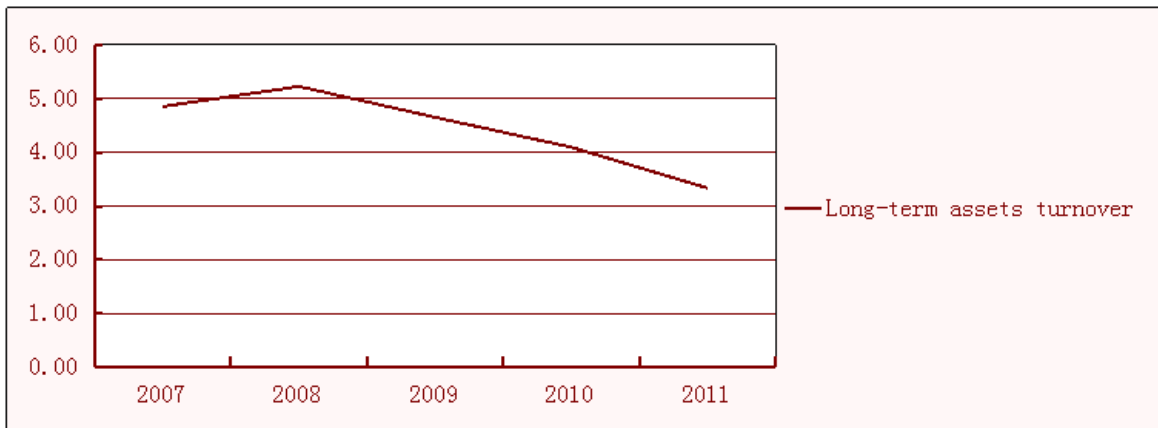
We can see that receivables turnover ratio increased gently in 2007, and growth rate was higher in 2008, but from 2009 it came down sharply. This ratio of Lianhua is between 25 and 45. It is relatively a high level. That implies Lianhua operates on a cash basis and its extension of credit and collection of accounts receivable is efficient.

At the same time, payable turnover had gentle decrease during these years, except the growth in 2008. This ratio changed between 4 to 5, and that means Lianhua a good ability to efficiently pay off supplier for purchases. Thanks to the complete information systems and its own distribution center, Lianhua did a good job in both collecting receivables and paying off suppliers.

Table 4.10 Long-term assets turnover

	2007	2008	2009	2010	2011
Revenues	18086857	20702441	24017720	25905344	27520176
Long-term Assets	3726166	3960927	5164460	6326007	8249016
<b>Long-term assets turnover</b>	<b>4.85</b>	<b>5.23</b>	<b>4.65</b>	<b>4.10</b>	<b>3.34</b>

Figure 4.11 Long-term assets turnover



From the table and figure above, it shows that long-term assets turnover increased in 2007, but decreased from 2008 to 2011. The results is calculated by formula 2.4. All ratios during these five years are higher than 3 and lower than 6. We can say that after financial crisis in 2008, Lianhua's power of controlling long-term assets has been higher and higher. From the vertical common-size analysis in total assets before (figure 4.4), we can get that in long-term assets, long-term investment occupies the largest proportion and also has the fastest speed in growth. That also indicates that Lianhua expands very quickly in recent years.

Table 4.11 Total assets turnover

	2007	2008	2009	2010	2011
Revenues	18086857	20702441	24017720	25905344	27520176
Total Assets	11542454	13701336	15418396	18452840	20313931
<b>Total assets turnover</b>	<b>1.57</b>	<b>1.51</b>	<b>1.56</b>	<b>1.40</b>	<b>1.35</b>
<b>Industry average</b>	<b>1.64</b>	<b>1.64</b>	<b>1.59</b>	<b>1.60</b>	<b>1.56</b>

Figure 4.12 Total assets turnover



Total assets turnover is calculated by formula 2.5, and the result is between 1.3 and 1.6. As a whole, it trend to decrease, but there was an increase in 2008. We can compare Lianhua's total assets turnover to industry average in China<sup>15</sup>. Industry average is more stable and higher than Lianhua' ratio, and its variation trend is different from Lianhua. Normally, industry average increased while Lianhua's ratio decreased, except in 2011, both of them went down. So Lianhua's profit ability has been weaker and weaker.

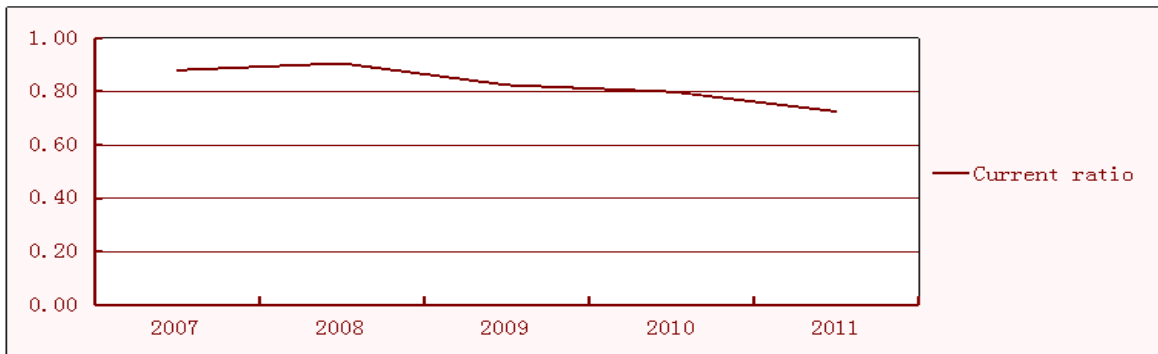
#### 4.2.2 Liquidity ratios

Table 4.12 current ratios

	2007	2008	2009	2010	2011
Current assets	7,816,288	9,740,409	10,253,936	12,126,833	12,064,915
Short-term liabilities	8,881,596	10,757,320	12,438,947	15,178,721	16,645,024
<b>Current ratio</b>	<b>0.88</b>	<b>0.91</b>	<b>0.82</b>	<b>0.80</b>	<b>0.72</b>

Figure 4.13 current ratio

<sup>15</sup> Data of industry average are from China Statistical Yearbook

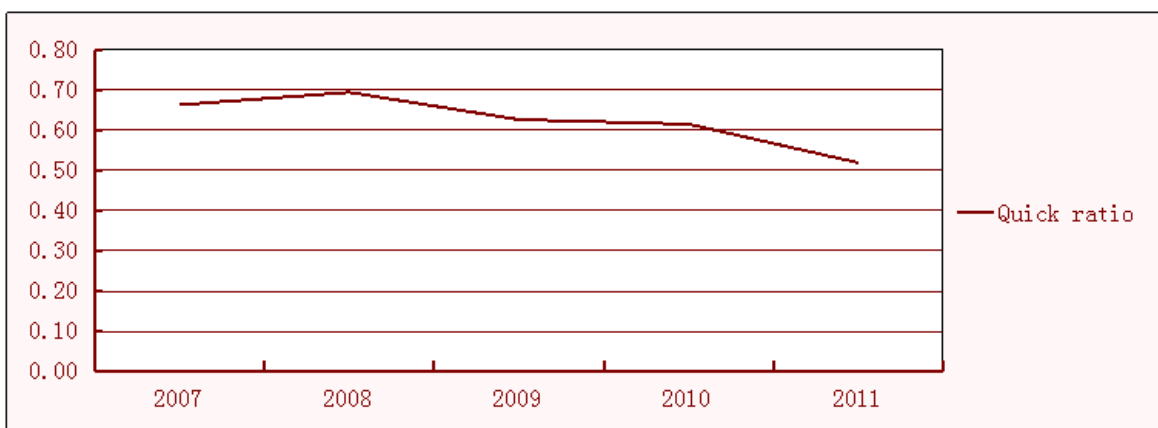


Formula 2.6 is used here. The current ratio trends decrease during five years, but there still an increase in 2008. Lianhua didn't have enough recourse to pay its debts in recent years, the debt-paying ability is poor and cost of debt is high, so Lianhua has no choice except get more current liabilities. As a result, short-term obligations occupied large proportion. It is said that generally current ratio equals to 2 is properly, but in Lianhua the highest level is lower than 1. It is evident that there is a liquidity problem.

Table 4.13 Quick ratio

	2007	2008	2009	2010	2011
Current assets	5,889,826	7,469,713	7,794,430	9,339,722	8,644,093
Inventories	8,881,596	10,757,320	12,438,947	15,178,721	16,645,024
<b>Quick ratio</b>	<b>0.66</b>	<b>0.69</b>	<b>0.63</b>	<b>0.62</b>	<b>0.52</b>

Figure 4.14 Quick ratio



The results in table 4.13 are calculated by formula 2.7 and its change trend is same to current ratio. The only difference is that in quick ratio doesn't contain inventory. And the

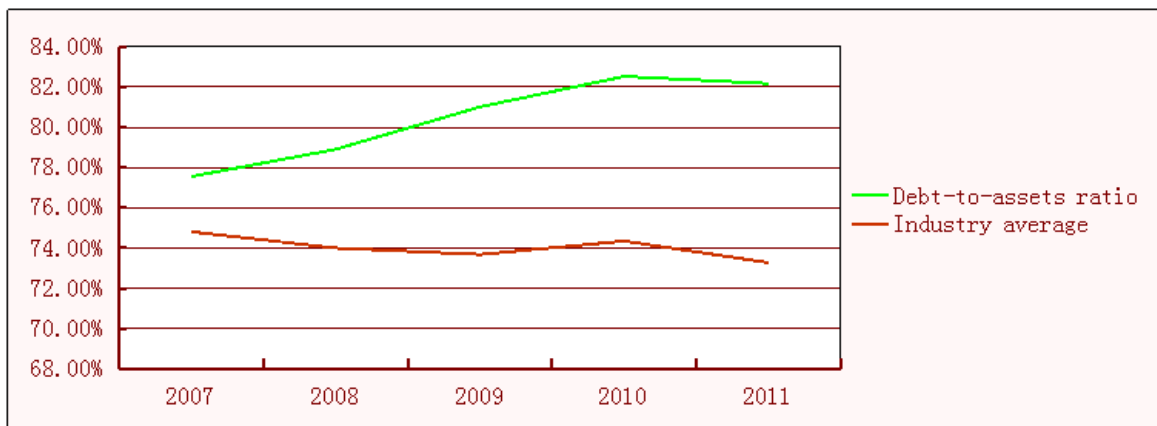
normal quick ratio is 1<sup>16</sup>. Obviously, Lianhua's quick ratio is lower than 1. This result also proves that Lianhua has poor ability to pay off short-term obligations. And a liquid asset transfers slowly to cash.

### 4.2.3 Solvency ratios

Table 4.14 Debt-to-assets ratio

	2007	2008	2009	2010	2011
Total debts	8,951,693	10,810,752	12,490,322	15,228,039	16,692,285
Total assets	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
<b>Debt-to-assets ratio</b>	<b>77.55%</b>	<b>78.90%</b>	<b>81.01%</b>	<b>82.52%</b>	<b>82.17%</b>
<b>Industry average</b>	<b>74.82%</b>	<b>74.01%</b>	<b>73.69%</b>	<b>74.35%</b>	<b>73.28%</b>

Figure 4.15 Debt-to-assets ratio



The results in table 4.14 is calculated by formula 2.8, it increased from 2007 to 2010, but went down from 2010 to 2011. We can compare debt-to-assets ratio of Lianhua with the industry average, and see the result from figure 4.15 that there is large distance between the green and yellow line.

This result is influenced by Lianhua's coupon liabilities. Compared with 2007, coupon

<sup>16</sup> From Wikipedia-Quick ratio: [http://en.wikipedia.org/wiki/Quick\\_ratio](http://en.wikipedia.org/wiki/Quick_ratio)

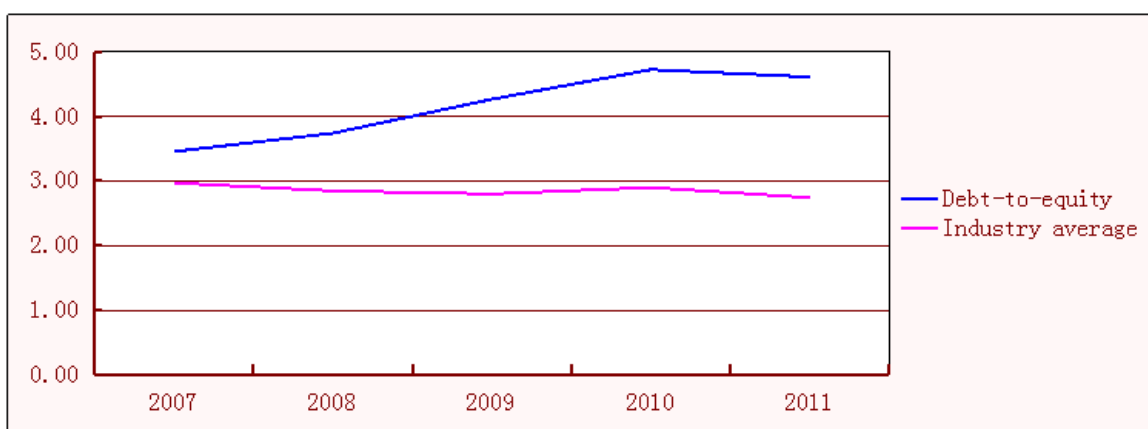


liabilities grew 103.99% in 2011. Total assets grew more quickly than total debts. For creditors, lower debt to assets ratio is better, because the company's solvency is guaranteed; but for shareholders, higher debt to assets ratio means the profit they get enlarged. In order to expand the scale and finance money into stores' development, Lianhua borrowed CNY 2 billion from bank in 2011. Lianhua's debt to assets ratio exceeded 80%, it is a bad news for creditors. Once Lianhua goes broke, creditors may suffer losses.

Table 4.15 Debt to equity

	2007	2008	2009	2010	2011
Total Debts	8,951,693	10,810,752	12,490,322	15,228,039	16,692,285
Total Equity	2,590,761	2,890,584	2,928,074	3,224,801	3,621,646
<b>Debt-to-equity</b>	<b>3.46</b>	<b>3.74</b>	<b>4.27</b>	<b>4.72</b>	<b>4.61</b>
<b>Industry average</b>	<b>2.97</b>	<b>2.85</b>	<b>2.80</b>	<b>2.90</b>	<b>2.74</b>

Figure 4.16 Debt to equity



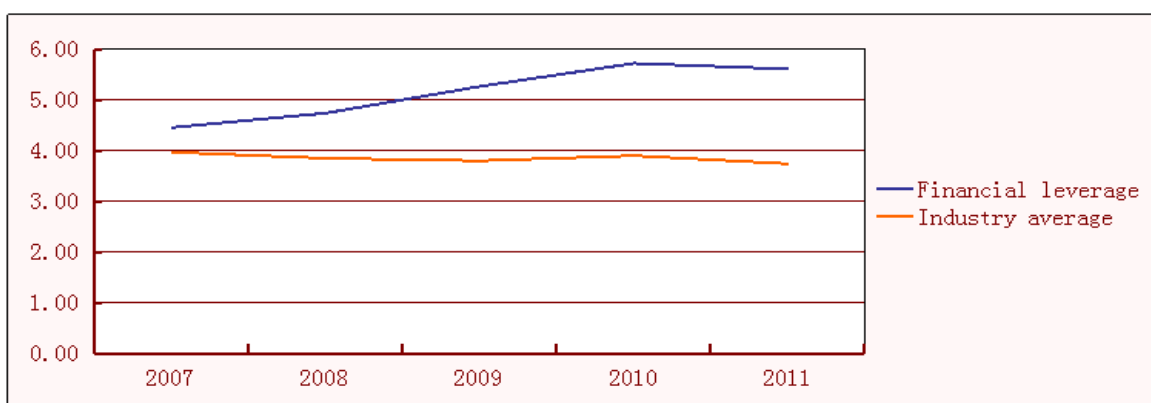
Using formula 2.9, the debt to equity is shown in table 4.15. It's also constantly increased from 2007 to 2008, but in 2011 dropped from 4.72 to 4.61. As for industry average, the ratio is more stable and lower than Lianhua's.

This result reflects that Lianhua's liabilities are more than equity result in a weak financial foundation. Lianhua realized this serious problem and tried to improve. In recent years, it seems better, especially in 2011, share capital was added to CNY 1 119 600 million, and the total equity had a positive change.

Table 4.16 Financial leverage

	2007	2008	2009	2010	2011
Assets	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
Equity	2,590,761	2,890,584	2,928,074	3,224,801	3,621,646
<b>financial leverage</b>	<b>4.46</b>	<b>4.74</b>	<b>5.27</b>	<b>5.72</b>	<b>5.61</b>
<b>Industry average</b>	<b>3.97</b>	<b>3.85</b>	<b>3.80</b>	<b>3.90</b>	<b>3.74</b>

Figure 4.17 Financial leverage



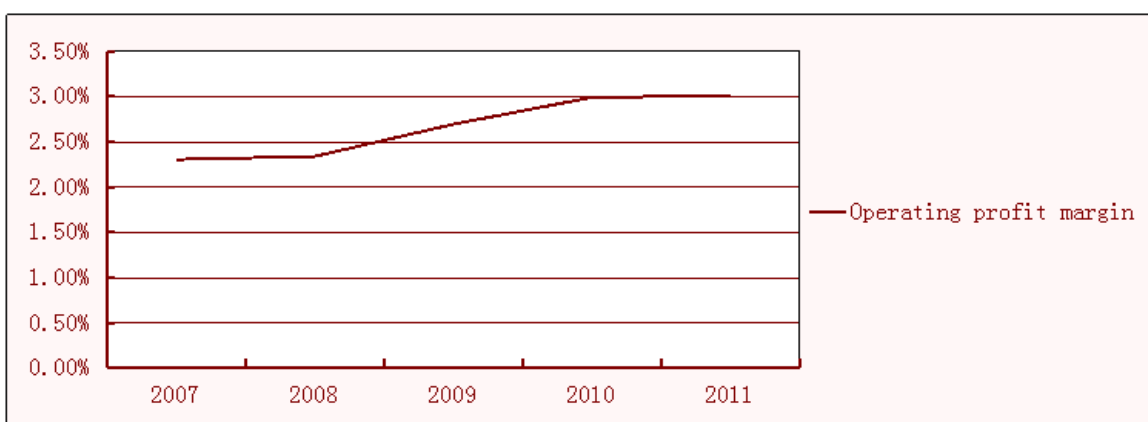
Financial leverage has been continually increasing from 4.46 to 5.61 during these years. The results are calculated by formula 2.10. Industry average is still lower than Lianhua's financial leverage. Great increase in assets leads to Lianhua's high financial leverage. It shows that Lianhua has enough sales revenue to cover the interest payments. We can also see how quickly does Lianhua expand. Both Lianhua and industry average financial leverage decreased from 2010 to 2011, that was because of the fierce market competition, so the the growth speed of assets in both Lianhua and industry average has been slower.

#### 4.24 Profitability ratios

Table 4.17 Operating profit margin

	2007	2008	2009	2010	2011
EBIT	417,294	484,641	647,573	775,202	829,373
Revenues	18,086,857	20,702,441	24,017,720	25,905,344	27,520,176
<b>Operating profit margin</b>	<b>2.31%</b>	<b>2.34%</b>	<b>2.70%</b>	<b>2.99%</b>	<b>3.01%</b>

Figure 4.18 Operating profit margin

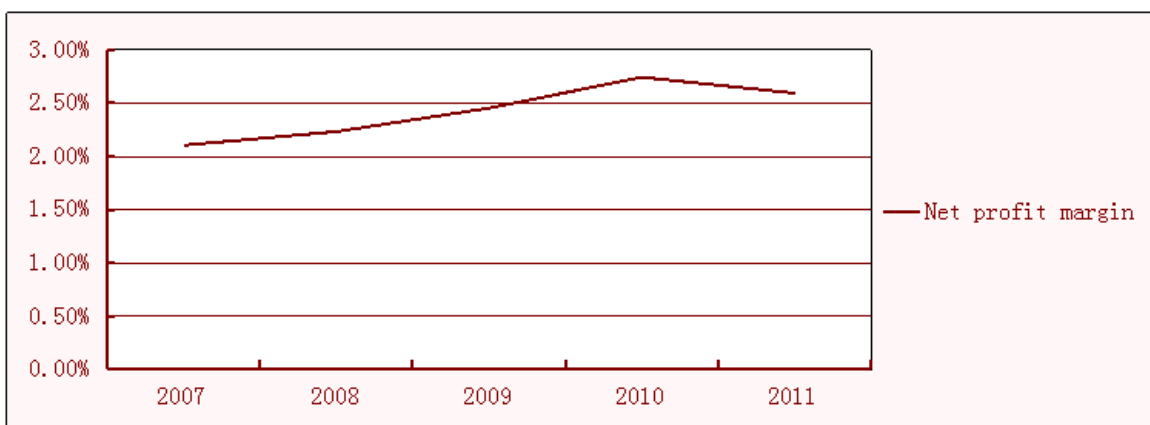


Formula 2.13 has been used for operating profit ratio. It constantly grew from 2.31% to 3.01% during these five years. Because of the high level of cost, even though operating profit grows fast, the margin is still not high. Along with rental price raising and company enlarging, Lianhua generated a higher level of revenues to pay for operating expenses, but due to the prominent effect of continuous improvement in operation and the excellent performance of new outlets sales quantity and turnover also increased. The margin's growth in 2008 is the highest, and the reason is Lianhua started to build its own fresh produce production bases and launched its own logistics delivery system to replace some third party delivery services. And these bases reduced large of logistics cost in last few years.

Table 4.18 Net profit margin

	2007	2008	2009	2010	2011
Net profit	380,649	462,230	589,383	710,432	713,693
Revenues	18086857	20702441	24017720	25905344	27520176
<b>Net profit margin</b>	<b>2.10%</b>	<b>2.23%</b>	<b>2.45%</b>	<b>2.74%</b>	<b>2.59%</b>

Figure 4.19 Net profit margin



Formula 2.14 has been used for net profit margin. From 2007 to 2010, Lianhua's net profit margin kept increasing but decreased in 2011. It's said above that in 2008, China took new enterprise income tax low, and income tax rate is reduced. So the net profit margin grew more quickly than before. But due to costs' increase, the margin reduced in 2011. As a whole, Lianhua is profitability and effectiveness of the cost contral measure.

Table 4.19 Return on assets

	2007	2008	2009	2010	2011
Net profit	380,649	462,230	589,383	710,432	713,693
Total assets	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
<b>Return on assets</b>	<b>3.30%</b>	<b>3.37%</b>	<b>3.82%</b>	<b>3.85%</b>	<b>3.51%</b>

Figure 4.20 Return on assets



Return on assets is calculated by formula 2.15. There is a gentle fluctuation in figure

4.20. It increased from 2007 to 2010, and had great growth in 2008, but decreased in 2011. This change is due to Lianhua's high interest costs which resulting from its above-average use of debts. In general, Lianhua's ROA is higher than 3% but lower than 4%, it proves that Lianhua did a good job to transfer its investment into profit.

Table 4.20 Return on equity

	2007	2008	2009	2010	2011
Net profit	380,649	462,230	589,383	710,432	713,693
Equity	2,590,761	2,890,584	2,928,074	3,224,801	3,621,646
<b>return on equity</b>	<b>14.69%</b>	<b>15.99%</b>	<b>20.13%</b>	<b>22.03%</b>	<b>19.71%</b>

Figure 4.21 Return on equity



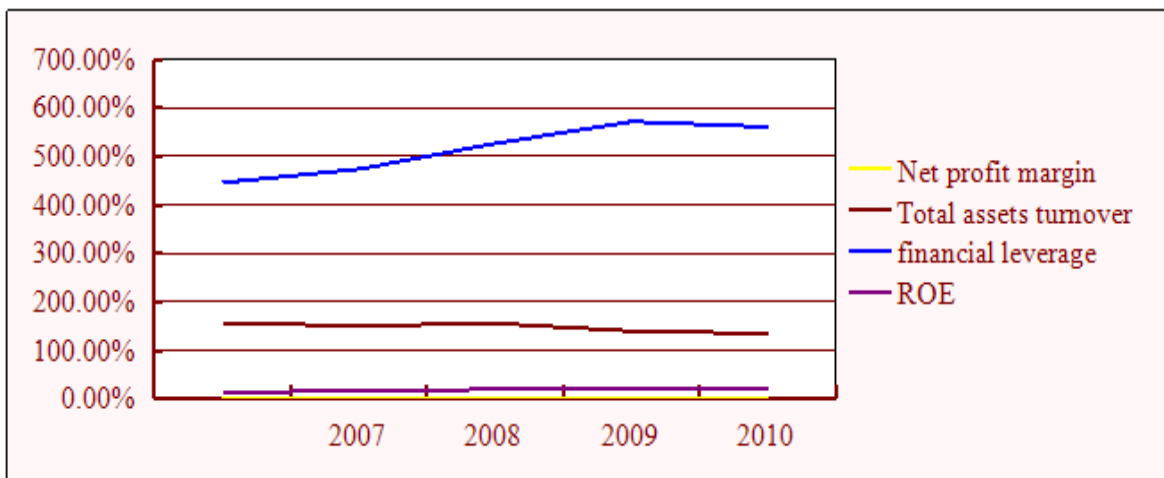
Formula 2.16 is used here, and results are shown in table 4.20. Lianhua's return on equity trended increase from 2007 to 2010, and decrease in 2011. During these five years, the highest ratio is 22.03% in 2010, and the lowest one is 14.69% in 2007. This increase is mainly related to the great growth of gross profit. Lianhua tried to improve itself profitability. And more details will be introduced later.

### 4.3 DuPont analysis

Table 4.20 DuPont analysis

	2007	2008	2009	2010	2011
Net profit	380,649	462,230	589,383	710,432	713,693
Revenues	18,086,857	20,702,441	24,017,720	25,905,344	27,520,176
<b>Net profit margin</b>	<b>2.10%</b>	<b>2.23%</b>	<b>2.45%</b>	<b>2.74%</b>	<b>2.59%</b>
Total Assets	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
<b>Total assets turnover</b>	<b>1.57</b>	<b>1.51</b>	<b>1.56</b>	<b>1.40</b>	<b>1.35</b>
Equity	2,590,761	2,890,584	2,928,074	3,224,801	3,621,646
<b>financial leverage</b>	<b>4.46</b>	<b>4.74</b>	<b>5.27</b>	<b>5.72</b>	<b>5.61</b>
<b>ROE</b>	<b>14.69%</b>	<b>15.99%</b>	<b>20.13%</b>	<b>22.03%</b>	<b>19.71%</b>

Figure 4.22 Description of ROE



DuPont analysis is calculated by formula 2.20. From the table 4.20, Lianhua's profitability, asset efficiency, and use of debt are connected. It's clear from figure 4.22 that financial leverage is main component and net profit margin just occupies a little part. Even if total assets turnover has been declining these years, financial leverage and net profit are in sustainable growth, so ROE is increase.

Too much costs and expenses are Lianhua's worst shortcoming, meanwhile the number

of stores is its main advantage. Although Lianhua had 5150 stores in 2008, there are just 1768 stores belong to direct operation, and other 3382 stores is franchised operation. It is inevitably to have some lack in the management. How to operate the whole group more efficiently is an urgent problem for Lianhua now.

#### 4.4 Analysis of gradual changes

In order to know how each component effects ROE, we will use analysis of gradual changes. Firstly, we should calculate gradual changes of net profit margin, total assets turnover, and financial leverage with the formula 2.23.

Table 4.21 Gradual change from 2007 to 2008

	a <sub>2007</sub>	a <sub>2008</sub>	Δ a	Δ x	order
a <sub>1</sub> =EAT/Rev	2.10%	2.23%	0.13%	0.89%	2
a <sub>2</sub> =Rev/Assets	1.57	1.51	-0.06	-0.56%	3
a <sub>3</sub> =Assets/Equit					
y	4.46	4.74	0.28	0.96%	1
SUM	X	X	X	1.30%	X

From table 4.21, it very obviously that from 2007 to 2008, total assets turnover has been decreasing by 6% , but net profit margin and financial leverage respectively grew by 0.13% and 28%. According to calculation, we can see from the table that financial leverage had the deepest influence in ROE, and the second one is net profit margin. As for total assets turnover, its gradual change was lower than zero.

Table 4.22 Gradual change from 2008 to 2009

	a <sub>2008</sub>	a <sub>2009</sub>	Δ a	Δ x	order
a <sub>1</sub> =EAT/Rev	2.23%	2.45%	0.22%	1.58%	2
a <sub>2</sub> =Rev/Assets	1.51	1.56	0.05	0.54%	3
a <sub>3</sub> =Assets/Equit					
y	4.74	5.27	0.53	2.01%	1
SUM	X	X	X	4.14%	X

From table 4.22, it is shown that the situation from 2008 to 2009 was better than which

was from 2007 to 2008. Because total assets turnover has a positive change. Financial leverage still had a deepest impact on ROE, net profit margin was the second one, and the lowest impact was from total assets turnover.

Table 4.23 Gradual change from 2009 to 2010

	a <sub>2009</sub>	a <sub>2010</sub>	△a	△x	order
a <sub>1</sub> =EAT/Rev	2.45%	2.74%	0.29%	2.37%	2
a <sub>2</sub> =Rev/Assets	1.56	1.40	-0.15	-2.22%	3
a <sub>3</sub> =Assets/Equity	5.27	5.72	0.45	1.76%	1
SUM	X	X	X	1.90%	X

In table 4.23, total assets turnover has been decreasing again from 2009 to 2010. The growth rate of net profit margin was higher than 2008, while the growth rate of financial leverage went down. Whatever, financial leverage still had the most contribution to ROE, and total assets turnover had the least because of its negative gradual change. The total gradual change decreased from 4.14% to 1.90%.

Table 4.24 Gradual change from 2010 to 2011

	a <sub>2010</sub>	a <sub>2011</sub>	△a	△x	order
a <sub>1</sub> =EAT/Rev	2.74%	2.59%	-0.15%	-1.20%	3
a <sub>2</sub> =Rev/Assets	1.40	1.35	-4.91%	-0.73%	2
a <sub>3</sub> =Assets/Equity	5.72	5.61	-11.31%	-0.40%	1
SUM	X	X	X	-2.32%	X

From table 4.24, we can see that net profit margin, total assets turnover and financial leverage have been decreasing from 2010 to 2011. Financial leverage had the deepest impact on ROE, the second one is total assets turnover, and the last one is net profit margin. All these gradual changes were negative.

In a word, financial leverage has the deepest impact on Lianhua. Company should pay more attention to keep this ratio stable. At the same time, Lianhua should also adjust its assets structure and consider more in expansion, so that its total assets turnover has a positive impact on ROE.



## 5 Conclusion

Lianhua is named as “a leader of fast moving consumer goods chain companies in China”, but after so much calculation and analysis, the truth of this honorary title will be hesitated. It is undeniable that Lianhua really had a glorious past, when it became the top one of 100 Chinese retail and catering companies in three times. And it is also a great achievement to develop the company from just one stores in 1991 to 5150 outlets in 2011. Total revenues and number of stores has been increasing these years. Lianhua became nationwide well-know.

Everything looks excellent, but from common-size analysis of income statement, cost of sales and expenses consist large part of total revenues, and their growth speed is very fast. As we all know, scale expanding will lead to increase of costs. Lianhua is not good at reduce the costs. Even if total turnover grows fast, net profit would have negative influence affected by costs. But every coin has two sides, in the other hand, employees in Lianhua have higher salary than in other supermarkets. So people prefer to work in Lianhua, and they also suggest their families or friends shop in Lianhua.

Compared with income sheet, we can see that total inventory was 16.69% of total assets in balance sheet in 2011 and the proportion has been increasing in recent years. At the same time, the current assets occupied 59.39% of total assets and has kept decreasing. The retail industry’s average proportion of inventory and current assets are 16.87% and 60.14% respectively. Enough turnover ensures various consumer demand.

As for financial ratios, they were separated into 4 parts; activity ratios, liquidity ratios, solvency ratios and profitability ratios. Activity ratios are aimed to measure how well a company uses its assets. It is obviously that activity ratios have been decreasing from 2007 to 2011. Lianhua’s ability to transfer products to cash or sales is lower and lower.

Liquidity ratio measures company’s ability to deal with its immediate or short-term liabilities and obligations. Two ratios were used in the part of liquidity ratios. There are current ratio and quick ratio. Both ratios decreased from 2007 to 2009, and both ratios were below the normal index. So there must be some serious problems in liquidity.

The solvency ratios measure company's ability to meet its long-term obligations, and allow analysts to measure the prudence of the debt management policies of the firm. There were three ratios introduced in solvency ratios. Because of the high level of coupon liability, total debts is high as well. Coupon liability was 41.43% of total equity and liabilities in 2007, and in 2011 it grew to 48.03% of total equity and liabilities. Debt-to-assets ratio was 77.55% in 2007, and in 2011 is 82.17%. Debt-to-assets ratio of Lianhua is mainly influenced by coupon liabilities. Debt-to-equity ratio was not very high, but it has been increasing in these five years. Financial leverage has been continually increasing from 4.46 to 5.61. It seems like Lianhua paid more attention to its enlargement, but ignored the debts and liquidity.

Profitability ratios relate a company's competitive position in the market and the quality of management. There were four ratios used in the text, and all of them are decreasing. That means Lianhua has a good competitive position.

From the whole text, Lianhua's advantage in market competition is the number of outlets. Lianhua is good at studying others' experience. It built fresh production bases and distribution centers, in order to satisfy consumers' demand and reduce costs; the first one is studied from Carrefour and the second one is studied from Wal-Mart. Lianhua still has a long way to go, and there is no chance to develop overseas business in a short time.

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[http://www.finet.hk/mainsite/chart.php?lang=TC&MainType=stock&code=00980&index\\_code=HSI&CompareType=none&c\\_code=&c\\_index\\_code=HSI&ChartType=line&ChartPeriodOption=0&TimeSpan=TIME07&ChartPeriod2=daily&Start\\_Year=&Start\\_Month=&Start\\_Day=&End\\_Year=&End\\_Month=&End\\_Day=&UpperFunction=mov&m1en\\_a=0&m1en\\_b=0&m1en\\_c=0&blen=&sd=&LowerFunction=none&rsi=&mon\\_len=&macdlen1=&macdlen2=&macdAvg=&k=&d=&draw=%E7%B9%AA%E5%9C%96](http://www.finet.hk/mainsite/chart.php?lang=TC&MainType=stock&code=00980&index_code=HSI&CompareType=none&c_code=&c_index_code=HSI&ChartType=line&ChartPeriodOption=0&TimeSpan=TIME07&ChartPeriod2=daily&Start_Year=&Start_Month=&Start_Day=&End_Year=&End_Month=&End_Day=&UpperFunction=mov&m1en_a=0&m1en_b=0&m1en_c=0&blen=&sd=&LowerFunction=none&rsi=&mon_len=&macdlen1=&macdlen2=&macdAvg=&k=&d=&draw=%E7%B9%AA%E5%9C%96)

## **List of Abbreviations**

TIE	Time interest earned
ROS	Return on sales
ROA	Return on assets
ROE	Return on equity
EBIT	Earning before interest and tax
EPS	Earning per share
P/E	Price-to-earnings ratio
Rev	Revenue

### **Declaration of Utilization of Results from a Bachelor Thesis**

Herewith I declare that

- I am informed that Act No. 121/2000 Coll. – the Copyright Act, in particular, Section 35
- Utilization of the Work as a Part of Civil and Religious Ceremonies, as a Part of School Performances and the Utilization of a School Work – and Section 60 – School Work, fully applies to my diploma (bachelor) thesis;
- I take account of the VSB – Technical University of Ostrava (hereinafter as VSB-TUO) having the right to utilize the diploma (bachelor) thesis (under Section 35(3)) unprofitably and for own use ;
- I agree that the diploma (bachelor) thesis shall be archived in the electronic form in VSB-TUO's Central Library and one copy shall be kept by the supervisor of the diploma (bachelor) thesis. I agree that the bibliographic information about the diploma (bachelor) thesis shall be published in VSB-TUO's information system;
- It was agreed that, in case of VSB-TUO's interest, I shall enter into a license agreement with VSB-TUO, granting the authorization to utilize the work in the scope of Section 12(4) of the Copyright Act;
- It was agreed that I may utilize my work, the diploma (bachelor) thesis, or provide a license to utilize it only with the consent of VSB-TUO, which is entitled, in such a case, to claim an adequate contribution from me to cover the cost expended by VSB-TUO for producing the work (up to its real amount).

Ostrava dated 1.May.2013

.....*Junyan Guo*.....

Junyan Guo

## **List of Annexes**

Annex 1 : The Distribution of Lianhua in China in 2011

Annex 2 : Income statement of Lianhua

Annex 3 : Balance sheet of Lianhua

Annex 4 : Basic Conditions of Retail of Supermarkets in China

Annex 1 The distribution of Lianhua in China in 2011

The distribution of Lianhua in China				
	Hypermarkets	Supermarkets	Convenience stores	SUM
Shanghai	37	1925	1258	3220
Zhejiang	46	261	242	549
Jiangsu	30	464	4	498
Liaoning	0	0	339	339
Guangxi	4	197	0	201
Beijing	4	1	171	176
Anhui	12	74	0	86
Shandong	1	22	0	23
Henan	5	14	0	19
Neimenggu	0	12	0	12
Jiangxi	0	6	0	6
Heilongjiang	4	0	0	4
Tianjing	2	1	0	3
Hebei	0	3	0	3
Sichuan	3	0	0	3
Fujian	2	0	0	2
Guangdong	2	0	0	2
Hubei	0	1	0	1
Chongqing	0	1	0	1



Annex 2 : Income statement of Lianhua (Currency in millions of CNY)

ITEMS	2007	2008	2009	2010	2011
Turnover	18,086,857	23,253,764	24,017,720	25,905,344	27,520,176
Cost of sales	15,738,221	20,232,932	20,881,677	22,292,378	23,563,736
Gross profit	2,348,636	3,020,832	3,136,043	3,612,966	3,956,440
Other revenue	1,619,536	2,083,763	2,280,322	2,417,087	2,523,310
Other income	638,132	354,319	372,517	447,601	595,704
Selling and distribution expenses	3,462,317	4,316,946	4,558,202	4,976,611	5,498,318
Administrative expenses	363,519	548,806	560,117	648,208	672,614
Other operating expenses	363,174	94,933	16,667	77,633	75,100
Finance costs	1,133	13,588	6,323	0	49
Operating profit	417,294	484,641	647,573	775,202	829,373
Share of profits of associates	130,475	149,482	150,240	178,826	142,578
Profit before taxation	585,454	634,123	797,813	954,028	971,951
Taxation	204,805	145,646	208,430	243,596	258,258
Profit and total comprehensive income for the year	380,649	488,477	589,383	710,432	713,693
Profit and total comprehensive income for the year attributable to:					
Owners of the Company	268,301	412,489	506,802	622,415	626,726
Non-controlling	112,348	75,988	82,581	88,017	86,967

interests					
	380,649	488,477	589,383	710,432	713,693
Earnings per share – basic and diluted	CNY0.43	CNY0.66	CNY0.81	CNY0.56	CNY0.56

## Annex 3 (Currency in millions of CNY)

ITEMS	2007	2008	2009	2010	2011
Non-current assets					
Property, plant and equipment	2,583,134	2,516,387	3,031,153	2,883,016	3,337,975
Construction in progress	171,561	153,088	86,921	220,730	67,765
Land use rights	284,429	309,519	254,717	249,419	304,559
Intangible assets	193,941	183,816	183,917	177,615	186,863
Deposit for acquisition of property, plant and equipment	0	0	0	0	300,000
Interests in associates	394,051	437,223	449,885	503,567	517,087
Available-for-sale financial assets	26,158	30,158	31,271	167,158	252,808
Held-to-maturity financial assets	0	8,800	377,615	377,295	238,365
Term deposits					
– restricted	0	0	0	293,000	1,893,500
– unrestricted	0	230,000	480,000	1,200,000	850,000
Prepaid rental	0	0	138,481	108,193	134,750
Deferred tax assets	44,672	65,239	104,661	121,360	142,213
Other non-current assets	28,220	26,697	25,839	24,654	23,131
	3,726,166	3,960,927	5,164,460	6,326,007	8,249,016
Current assets					

Inventories	1,926,462	2,270,696	2,459,506	2,787,111	3,420,822
Trade receivables	34,633	37,551	74,302	117,672	86,056
Deposits, prepayments and other receivables	596,462	629,109	487,723	601,429	884,861
Amounts due from fellow subsidiaries	0	0	0	8,092	10,810
Amounts due from associates	34	532	34	29	129
Available-for-sale financial assets	120,000	215,000	610,900	500,000	237,975
Held-to-maturity financial assets	0	0	97,873	45,777	145,191
Financial assets at fair value through profit or loss	116,420	27,706	1,874	204,089	0
Term deposits					
– restricted		649,000	1,219,800	1,621,400	1,087,700
– unrestricted		2,584,500	1,110,000	660,000	625,000
Cash and cash equivalents	5,022,277	3,326,315	4,191,924	5,581,234	5,566,371
	7,816,288	9,740,409	10,253,936	12,126,833	12,064,915
Total assets	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
Capital and reserves					
Share capital	622,000	622,000	622,000	622,000	1,119,600
Reserves	1616941	1,868,442	1,841,284	2,273,700	2,194,309
Equity attributable to owners of the	2,238,941	2,490,442	2,463,284	2,895,700	3,313,909

Company					
Non-controlling interests	351,820	400,142	464,790	329,101	307,737
Total equity	2,590,761	2,890,584	2,928,074	3,224,801	3,621,646
Non-current liabilities					
Deferred tax liabilities	70,097	53,432	51,375	49,318	47,261
Current liabilities					
Trade payables	2,815,286	3,130,020	3,490,098	4,156,708	4,419,446
Bank borrowing				-	2000
Other payables and accruals	1,113,454	1,539,754	1,773,257	1,871,658	2,204,370
Dividend payable to non-controlling interest of subsidiaries	0	0	0	203,569	0
Coupon liabilities	4,782,538	5,937,430	6,944,234	8,707,200	9,756,029
Deferred income	0	0	30,388	21,260	15,517
Amounts due to associates	7,865	24,681	4,791	5,399	13,014
Amount due to ultimate holding company	39,000	39,000	10,023	0	0
Amounts due to fellow subsidiaries	41,632	30,788	93,696	105,172	72,630
Taxation payable	81,821	55,647	92,460	107,755	162,018
	8,881,596	10,757,320	12,438,947	15,178,721	16,645,024
Total liabilities	8,951,693	10,810,752	12,490,322	15,228,039	16,692,285

Total equity and liabilities	11,542,454	13,701,336	15,418,396	18,452,840	20,313,931
Net current liabilities	-1,065,308	-1,016,911	-2,185,011	3,051,888	4,580,109
Total assets less current liabilities	2,660,858	2,944,016	2,979,449	3,274,119	3,668,907

#### Annex 4: Basic Conditions of Retail of Supermarkets in China

(Currency in billions of CNY)

	2007.00	2008.00	2009.00	2010.00	2011.00
Assets	5124.29	6236.49	7148.15	8746.71	10489.76
Working Capitals	2844.08	3509.66	4083.32	5269.94	6308.65
Fixed Assets	1938.21	2206.86	1747.43	1908.56	2230.87
Liabilities	3833.80	4615.56	5267.62	6503.40	7687.03
Equities	1290.49	1620.93	1880.53	2243.32	2803.33
Inventory	884.56	1251.61	1211.50	1486.18	1769.77
Revenue	8390.31	10250.39	11337.06	14037.61	16383.36
Cost	7165.19	8612.03	9697.44	12008.53	14020.30
Taxes	38.53	83.71	81.18	97.68	125.57
Profits	1041.82	1487.29	1483.03	1834.78	2237.49
Total Sales	6099.21	11930.72	13164.19	27385.40	10733.72
Number of Stores	47629.00	48020.00	56568.00	176792.00	195779.00