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Hard questions raised as Fu Ji Catering goes for soft option

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On Monday morning, mainland firm Fu Ji Food and Catering Services Holdings' Hong Kong-traded shares were worth HK$7.60 each. That afternoon, the company voluntarily placed itself in provisional liquidation, saying it could not afford to repay its convertible bondholders, who are owed just over HK$2 billion.

If Fu Ji, which fed thousands at last year's Beijing Olympics and was set to serve the noodles and sandwiches at the coming East Asian Games, is wound up, shareholders are likely to see their entire investments wiped out. But investors had no idea the caterer was heading for liquidation. When Fu Ji last released accounts, it looked healthy and solvent.

It has a HK$550 million convertible bond payment due on November 9. So did it pull the plug to avoid its financial commitments?

An official at Fu Ji's Shanghai headquarters told the South China Morning Post on Tuesday: 'We think the game of financing is too complicated for us. We just want to quit it by liquidation.'

Fu Ji has still not published its 2008-09 financial statements. Its shares were suspended in July.

However, for the six months to September last year, it reported a 272 million yuan (HK$308.69 million) net profit and said its assets were worth more than its liabilities.

Fu Ji's provisional liquidator, Derek Lai Kar-yan of Deloitte Touche Tohmatsu, says the caterer - whose Chinese name means 'Lucky Shop' - really is bust. He says Fu Ji has assets worth HK$3 billion but it does not have enough cash to meet its financial obligations.

'From the cash-flow perspective, the group is insolvent,' Lai says.

Fu Ji's assets, which are mostly buildings under construction, can take a while to sell.

Some of Fu Ji's bondholders are privately slamming the firm for not attempting a financial restructuring before entering provisional liquidation. At least 12 of the about 100 bond investors have formed an action group to try to drag Fu Ji out of the insolvency process.

They say the caterer can still potentially stay afloat by asking convertible bondholders for more time to pay them, trying to raise cash through a stock market rights issue or asking its banks for fresh loans. These options will be a lot better for Fu Ji's beleaguered shareholders, too.

When firms go into liquidation, banks that have claims over assets, including mortgages on properties, get the lion's share of proceeds from asset sales. Bondholders, who are unsecured creditors, are next in line for a payout. Shareholders are usually left empty-handed.

Mainland aluminium extruder Asia Aluminum Holdings was wound up in July. Its adviser, Ferrier Hodgson, sold the firm to members of its management team. The company's banks got most of their money back.

The bondholders lost 80 to 99 per cent of their money, depending on which class of bond they held.

Asia Aluminum spent months negotiating with its lenders before winding itself up. But Fu Ji did not consult bondholders before it petitioned the court to enter provisional liquidation, it is claimed.

'Creditors were denied the opportunity [by Fu Ji] to explore other options,' one Fu Ji bondholder said. 'Fu Ji could look at many financial restructuring options.'

Shareholder activist David Webb said Fu Ji might have opted for the move to escape its financial liabilities. He added that such corporate behaviour was becoming a worrying trend in Hong Kong.

'Companies, led by their management, are abusing the liquidation process as a means to run away from minority shareholders and creditors,' he said.

'Unless the Securities and Futures Commission intervenes to oppose the winding-up petition and the appointment of provisional liquidators, they have a clear run at it.'

Webb is campaigning for the SFC to intervene in provisional liquidations that seem unnecessary.

He lost money after a firm that he believes was solvent voluntarily wound itself up.

Webb owned shares in Norstar Founders, a mainland car-parts manufacturer, which reported net cash of 1.28 billion yuan for the six months to September last year and net assets of HK$3.12 per share.

In February, Norstar chairman Lilly Huang convinced the High Court to put the firm into provisional liquidation. Norstar had made a wrong-way bet on accumulators and owed 39 million yuan on that contract. It had also been sued by a supplier for 326 million yuan.

However, according to Webb, the company should have had 753 million yuan of spare cash after these liabilities.

Lai has the same court-appointed role at Norstar. Deloitte is now selling the car-parts firm to state-owned Beijing West, which is connected to Norstar's management.

Half of Beijing West is owned by a vehicle called Baoan Investment Development. Zhou Xiaochun, the son of Norstar chief executive Zhou Tianbao, owns 20 per cent of Baoan Investment.

Lai said the family relationship was insignificant because the younger Zhou's shareholding represented just 4.8 per cent of Norstar.

Webb wrote to the SFC in April asking it to intervene in the Norstar case. The SFC declined to comment.

Another Hong Kong-traded mainland firm, food processor First Natural Foods, plunged unexpectedly into provisional liquidation in January. For the six months to September last year, First Natural had 438 million yuan net cash. Like Norstar, it had tripped up on derivatives.

Ernst & Young, First Natural's provisional liquidator, declined to comment.

Ricky Tam, the head of the Hong Kong Institute of Investors, also wants the SFC to make it harder for locally listed firms to enter provisional liquidation by intervening in cases.

'Hong Kong is sending a very bad signal here,' Tam said.

'Companies that have enough money or other options are going into liquidation ... The mainland has tougher regulators.'