

LEVEL 7 ASSESSMENT SPECIFICATION

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Programme:	MBA		
Module:	Finance for Business Managers		
Module code:	HKBM7008	Contribution to Overall Module Assessment (%):	100%
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Assignment Title:	Assignment 1	Word count (or equivalent):	5,000 words
Submission deadline:	11 September 2023	Return date of provisional marks & written feedback:	10 October 2023

Executive Summary

This executive summary provides an overview of the assessment conducted on Fairwood Holdings Limited, a prominent fast-food company in Hong Kong. The assessment examines the company's financial performance, corporate governance practices, investment project appraisal, and financing and capital management with the action plan.

Fairwood Holdings Limited's significance lies in its strong market position and ability to adapt to changing market conditions. The assessment identifies areas for improvement and offers recommendations for sustainable growth.

Key areas covered in the assessment include analyzing financial performance, optimizing capital utilization, enhancing corporate governance practices, and exploring investment opportunities in the private nursing home sector. Recommendations focus on improving financial ratios, implementing effective cash management strategies, enhancing governance practices, and sourcing funding through private placement.

Overall, studying Fairwood Holdings Limited provides valuable insights into its financial strength, governance practices, and growth opportunities. Implementing the suggested improvements will strengthen the company's financial position and ensure long-term success in the fast-food industry.

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1. Introduction

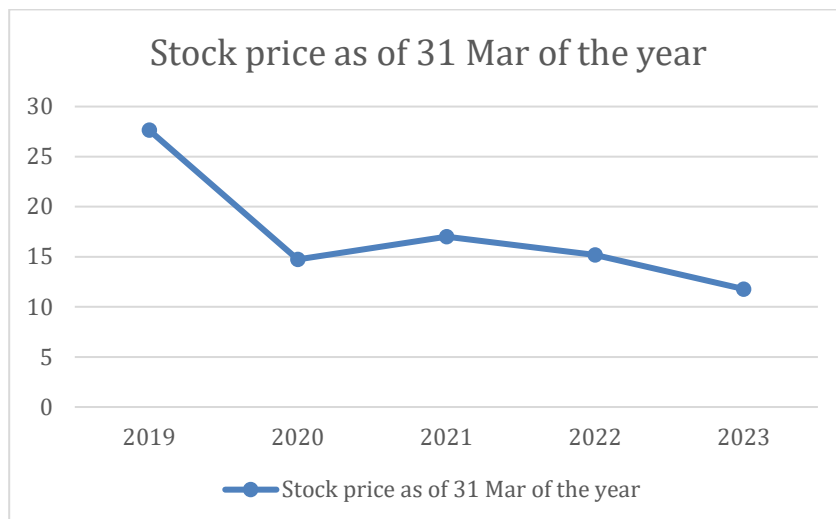
1.1 Company Background

Fairwood Holdings Limited, known as Fairwood (HKEX stock code: 52), is a prominent fast-food company based in Hong Kong. Established in 1972 by Mr. Lo Fong Seong and Mr. Lo Hoi Fook, Fairwood started as a single restaurant in Tsuen Wan and has since become a renowned fast food brand throughout Hong Kong (Fairwood Holdings Limited, 2022). Its main competitors are Café de Coral and Maxim's (Edigest, 2017).

Fairwood conducted its IPO on September 20, 1991, issuing 97.925 million shares at a price of HKD 1.18 per share, raising a total of HKD 116 million. The IPO was oversubscribed by 28.8 times, and employee subscriptions were fully taken up (ZKIZ Archives, 2019). However, the company faced challenges due to aggressive expansion plans, tight operating capital, and limitations imposed by joint ventures. The stock price initially rose but later declined, and the company reported losses. Fairwood made efforts to turn the situation around, including rights issues and the sale of unprofitable ventures. Since 2000, the company has shown improvement and outperformed its competitor, Café de Coral, in recent years.

Over the years, Fairwood has expanded its presence across the entire territory of Hong Kong, solidifying its status as a prominent player in the local market. As of August 2023, Fairwood Holdings Limited recorded a stock price of 10.9 Hong Kong dollars. The company's authorized share capital stands at 240,000,000 Hong Kong dollars, with issued and fully paid shares amounting to 129,533,000 Hong Kong dollars (Fairwood Holdings Limited, 2023, p.163).

Graph 1: The trend of the stock price from the last five years:



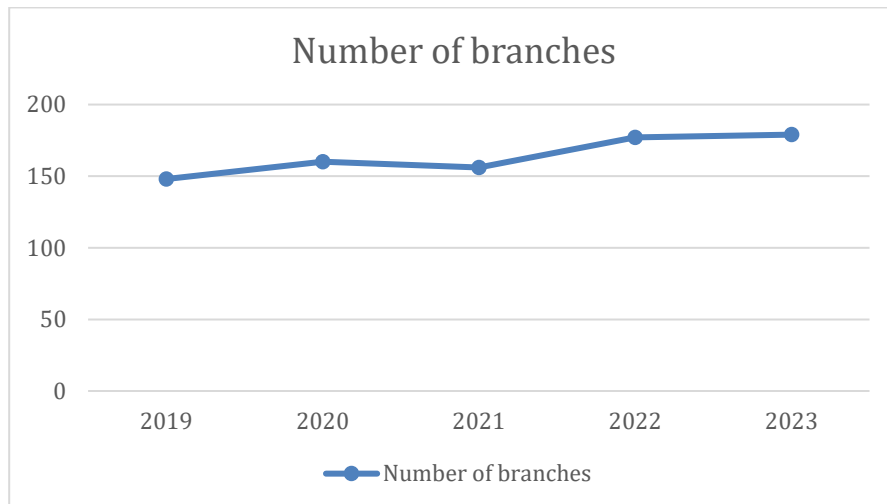
Source: Yahoo Finance

The main reason for the decrease in Fairwood's stock price is the pandemic and the economic downturn. This has resulted in a downturn in the catering industry, causing significant challenges for Fairwood as a local fast food leader. The company expects a considerable decline of approximately 70% in net profit for the current fiscal year compared to the previous year. Stringent social distancing measures, temporary restaurant closures, and city-wide lockdowns have adversely affected Fairwood's revenue and profitability (Ming Pao Finance, 2022).

1.2 Operating Business Overview

Fairwood primarily engages in the operation of a chain of restaurants. The company provides a range of dining options and services to its customers. Fairwood has established its presence in both Hong Kong and Mainland China, operating a total of 179 stores as of March 31, 2023. Out of these, 157 stores are located in Hong Kong, while 22 stores are situated in Mainland China. Furthermore, Fairwood operates a total of 10 specialty restaurants, including 3 ASAP, 4 Taiwan Bowl, and 3 The Leaf Kitchen (Fairwood Holdings Limited, 2023, p.19).

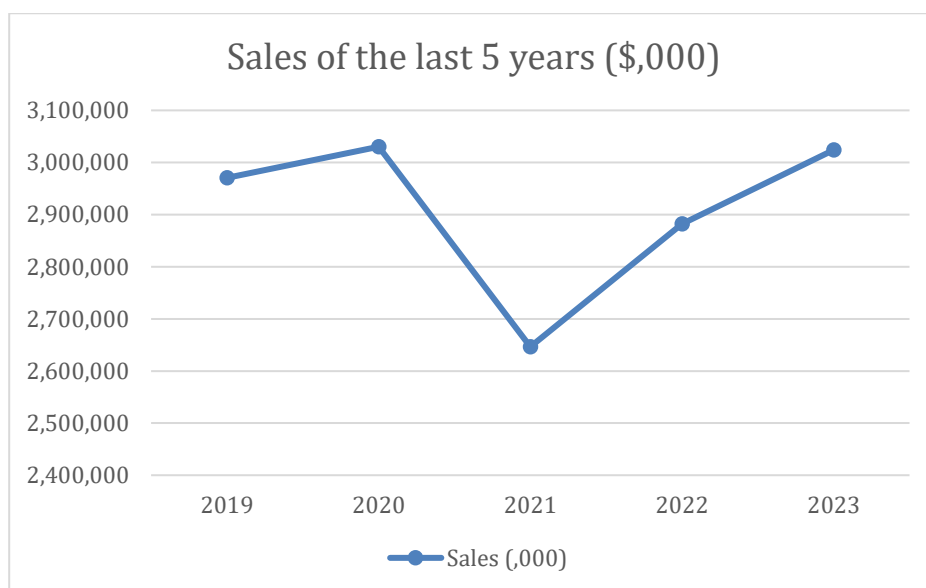
Graph 2: Number of branches in the past 5 years



Source: Fairwood Annual Reports

Fairwood's fast food restaurant chain in Hong Kong showed steady performance throughout the last fiscal year, improving as pandemic measures eased and the successful 50A campaign took place. Same Store Sales Growth (SSSG) increased by approximately 5%, accompanied by higher average spending per guest. While demand for takeout meals declined after COVID restrictions were lifted, it remains strong and accounts for around 36% of total sales. Specialty restaurants within the group experienced a slower recovery due to the significant impact of COVID-19 (Fairwood Holdings Limited, 2023, p.18).

Graph 3: Sales of the last 5 years:



Source: Fairwood Annual Reports

1.3 Today's Business Environment

Fairwood demonstrates robust financial strength as evidenced by its healthy financial situation and consistent cash flow. Its debt-free status shields it from the risks associated with fluctuating interest rates, which is particularly advantageous in a high-interest rate environment. The brand has established a reputable and trusted presence in Hong Kong, renowned for delivering not only value but also superior service tailored to customers' preferences. This positive brand reputation affords Fairwood the flexibility to set higher prices and make necessary adjustments as warranted.

Moreover, Fairwood employs a comprehensive cost-saving strategy that has yielded successful outcomes in the past and will persist in the future. Despite the challenges posed by the COVID-19 pandemic, Fairwood remains optimistic about its operations in Mainland China (Fairwood Holdings Limited, 2023, p.21). As COVID-19 restrictions ease and stores operate successfully, positive results are expected in the near future. However, the recovery of Fairwood's specialty restaurants may be protracted due to the enduring impact of COVID-19 on evening dining habits in Hong Kong. Consequently, Fairwood will closely monitor the mid-level dining scene and adapt its positioning accordingly. Furthermore, the company possesses available resources for targeted investments, if required.

Collectively, Fairwood's financial strength, debt-free status, brand reputation, and cost-saving strategies position it favorably in the marketplace as it adeptly navigates challenges and explores growth opportunities.

Although the performance declined in the first half of the year, Fairwood still maintained a high double-digit gross profit margin of 9.2%. Luo Hui Cheng's analysis suggests that there is upward pressure on operating costs, with significant increases in many areas this year. However, it is not expected to last too long. Taking labor costs as an example, they have been continuously rising in recent years, and Fairwood has been facing a shortage of manpower in the long term. They can only constantly think of improvement measures, such as optimizing the supply chain and striving to digitize internal processes to reduce manual labor. The goal is to achieve business growth without a proportional increase in manpower. (RTHK, 2022)

Fast food is considered a countercyclical stock in the traditional investment community. Fairwood Group is less affected by economic downturns, and they see potential for growth in the dinner segment. By providing high-value products at competitive prices, they can attract customers even during challenging economic times.

Table 1: SWOT Analysis of Fairwood:

Strengths: Strong Financial Position: Fairwood boasts a healthy financial situation and steady cash flow, providing a solid foundation for its operations. Debt-Free Status: Fairwood's lack of debt shields it from interest rate risks and ensures financial stability. Trusted Brand Reputation: Fairwood has established a reputable and respected brand in Hong Kong, known for offering value and delivering quality service that aligns with customer preferences. Pricing Flexibility: The positive brand reputation allows Fairwood to set higher prices and make price adjustments as needed, enhancing its profitability. Cost-Saving Strategy: Fairwood has a well-defined strategy for cost-saving and productivity enhancement, enabling efficient operations and maintaining profitability.	Weaknesses: Specialty Restaurant Recovery: The recovery of Fairwood's specialty restaurants may be slower due to the impact of COVID-19 restrictions on evening dining habits in Hong Kong. Reliance on Hong Kong Market: Fairwood's operations are primarily concentrated in Hong Kong, which may limit its geographical diversification and expose it to local market risks.
Opportunities: Mainland China Expansion: Fairwood's operations in Mainland China present an opportunity for growth and expansion, particularly as COVID-19 restrictions ease and successful store operations pave the way for positive results. Targeted Investment: Fairwood has the resources available to consider targeted investments, allowing it to pursue opportunities for growth and market positioning, especially in the evolving mid-level dining scene in Hong Kong.	Threats: Popularity for Two-dish mealboxes Economic Downturn: Fairwood may face challenges during downward economic cycles when consumers seek lower-cost dining options, increasing competition in the market. Food Ingredient and Labor Pressures and cost: The ongoing pressures associated with food ingredient costs and staff turnover could impact Fairwood's profitability and operational efficiency. COVID-19 Impact: The lingering effects of the COVID-19 pandemic, including potential

	future waves or new variants, could disrupt Fairwood's operations and customer demand, affecting its financial performance.
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Source : *from this research*

The fast food industry has surpassed its high-growth phase, but it still possesses the ability to withstand economic downturns. Additionally, centralized management costs give it an advantage over traditional tea restaurants. Fairwood is actively expanding its portfolio with new branded specialty restaurants and targeting the Greater Bay Area market, which still holds growth potential. With stable dividends and the anticipated recovery post-pandemic, as cross-border travel resumes, the company is expected to regain growth momentum. (RTHK, 2022)

1.4 Company Structure

Fairwood's company structure, as revealed in its annual report and ESG report for the fiscal year 2022-2023, consists of a Board comprising 3 Executive Directors and 4 Independent Non-executive Directors. The company also maintains three committees: the Audit Committee, responsible for financial oversight; the Remuneration Committee, which handles executive compensation matters; and the Nomination Committee, tasked with candidate selection for the Board and its committees. Total number of employees in Hong Kong is 4,681 (Fairwood Holdings Limited, 2023b, P.7).

Fairwood operates through various Business Units(Fairwood Holdings Limited, 2023b, p.62), encompassing frontline Restaurant outlets, a central Office for administrative functions, a central kitchen for food preparation, and a Bakery production line for bakery items (Fairwood Holdings Limited, 2023c, p.11).

1.5 Peer Comparison

This study utilizes a comparative analysis approach to examine Tsui Wah Holdings Limited (HKEX stock code: 1314) and Café de Coral Holdings Limited (HKEX stock code: 341) in relation to Fairwood Holdings Limited, by using time-trend analysis and peer group analysis. These companies possess comparable attributes to Fairwood, including their business nature, market area, and market share. Notably, all three entities are prominent fast food chain stores in Hong Kong, as evidenced by the data presented in Table 2. Consequently, this study enables a comparative analysis of financial management practices across these three companies.

Table 2: Peer Analysis

Company Name (Stock number)	Fairwood Holdings Limited (HKEX stock code: 52)	Tsui Wah Holdings Limited (HKEX stock code: 1314)	Café de Coral Holdings Limited (HKEX stock code: 341)
Business Nature	fast food chain stores		
Market Value (HK\$) As of 31 Mar 2023 (\$,000)	\$ 1,526,134	\$ 3,457	\$ 6,091,322
PE ratio As of 31 Mar 2023	34	0.06	54.78
Market Area	Hong Kong and Mainland China	Hong Kong, Macau, Mainland China, and Singapore	Hong Kong and the Mainland China
Number of Store (from the annual report of 2023)	179	79	450

Source: Annual reports 2023 of three companies

2 Fairwood's Financial Analysis

Through an analysis of Fairwood's financial reports, this study examines various aspects of the company's financial structure, including repayment and realized capacity, operating capacity, profitability, growth capacity, market value, and share returns. A comparative study is conducted by juxtaposing Fairwood's performance in these six areas with the industrial average and two other companies within the same industry. The findings derived from the data, along with a comprehensive risk assessment, provide valuable insights and serve as points of reference for the financial statements.

2.1 Listed Company Bankruptcy index Z-score Analysis

The Z-score is a statistical measure developed by Edward Altman to assess the financial health and bankruptcy risk of a company. It combines multiple financial ratios to generate a single numeric value. The Z-score above 3 signifies low bankruptcy risk, while a score below 1.8 indicates high risk. The Z-score is commonly used by investors, creditors, and analysts to evaluate the financial stability of a company (Hayes, 2019).

Table 3: Z scores

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Z score	2.47	2.44	2.32	1.85	2.25
Interpretation	Grey Area	Grey Area	Grey Area	Almost high risk	Grey Area

The calculation of Z scores and the related factors please refer to appendix 1, Source : from this research

The Z-score of Fairwood has exhibited a declining trend, decreasing from 2.47 in 2021 to 2.32 in 2023. This decline indicates the presence of potential areas for improvement in order to further enhance the company's financial health. Based on the factors encompassed within the Z-score formula, Fairwood can focus on enhancing its working capital management, augmenting profitability through investments in lucrative new product lines, and reducing costs associated with raw materials and labor. By addressing these factors, Fairwood can potentially elevate its Z-score and strengthen its overall financial position.

2.2 Liquidity ratios

Table 4: Liquidity ratios

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Current Ratio	0.99	0.98	0.97	1.33	0.77
Quick Ratio	0.93	0.91	0.90	1.3	0.67
Cash Ratio	0.77	0.71	0.79	0.64	0.6

**the calculation please refer to appendix 1, Source : from this research*

Current Ratio = Current Assets / Current Liabilities

The current ratio is a widely used financial ratio that assesses a company's ability to meet its short-term obligations through its short-term assets (Fernando, 2023a). A ratio above 1 indicates a stronger liquidity position and a better capacity to cover short-term liabilities. However, Fairwood's current ratio has exhibited a decreasing trend over the past three years, declining from 0.99 in 2021 to 0.97 in 2023. This decline suggests a potential solvency issue, possibly due to an increased debt burden or a depletion of cash reserves.

Moreover, Fairwood's current liabilities have increased from \$782,322,000 in 2022 to \$817,224,000 in 2023. With a current ratio below 1.00, it indicates that the company's short-term liabilities exceed its short-term assets. To address this situation, Fairwood should consider increasing its short-term assets through strategies such as obtaining short-term loans with high return rates or accelerating revenue generation.

By boosting short-term assets, Fairwood can enhance its current ratio and improve its short-term debt-paying ability, thereby mitigating potential solvency concerns.

Quick Ratio = (Current Assets – Inventory) / Current Liabilities

The quick ratio is a financial metric that evaluates a company's short-term liquidity position by measuring its ability to fulfill short-term obligations using its most liquid assets. It is similar to the current ratio but excludes certain current assets, such as inventories, which may not be easily convertible into cash. (Seth, 2023) A quick ratio of 0.9, for instance, indicates that a company possesses \$0.9 of liquid assets for every \$1 of current liabilities, which is not enough.

In this comparison, Tsui Wah's quick ratio is 1.3, above 1, suggests a favorable ability to settle current liabilities, as its liquid assets surpass its short-term debt obligations. Conversely, Fairwood and Café de Coral exhibit a quick ratio well below 1, specifically at 0.45, indicating potential

challenges in meeting current obligations solely through quick assets. This assessment focuses solely on short-term financial health, disregarding factors such as profitability or income.

As a result, Tsui Wah appears to possess better short-term financial stability in terms of meeting its immediate debt requirements when compared to Fairwood and Café de Coral.

Cash ratio = Cash / Current Liabilities

The cash ratio evaluates a company's ability to repay short-term debt with cash and cash equivalents. It helps creditors determine the amount they would be willing to loan based on the company's available cash resources (Hayes, 2019a). Fairwood cash ratio is 0.79 which is the highest, mainly because of the cash on hand increased from \$557,102,000 in 2022 to \$646,758,000 in 2023.

2.3 Leverage Ratios

Table 5: Leverage Ratios

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Total Debt Ratio	68%	67%	70%	49%	61%
Debt-to-Equity (D/E) Ratio	2.15	2.19	2.38	0.95	1.57
Long Term Debt Ratio	110%	110%	118%	40%	57%
Equity Multiplier	3.15	3.27	3.38	1.95	2.57

**the calculation please refer to appendix 1 Source : from this research*

Total Debt Ratio = Total Liabilities / Total Assets

The debt ratio measures a company's leverage by dividing total debt by total assets. It shows the proportion of assets financed by debt. A ratio above 1.0 means higher debt than assets, while a ratio below 1.0 indicates higher assets than debt (Hayes, 2022b). Fairwood has the highest ratio at 70%, indicating significant reliance on debt and increased financial risk. However, borrowing for high-yield investments can be beneficial if returns outweigh the debt cost. Careful evaluation and risk management are essential to ensure the benefits outweigh the risks.

Debt-to-Equity (D/E) Ratio = Total Liabilities / Total Shareholders' Equity

The debt-to-equity (D/E) ratio measures a company's financial leverage by comparing total liabilities to shareholder equity. It indicates the reliance on debt financing and varies by industry. A higher D/E ratio suggests more risk, while a low ratio may indicate underutilization of debt for expansion. Investors often focus on long-term debt for a more accurate assessment of risk (Fernando, 2023b).

Long Term Debt Ratio = Long Term Liabilities / Total Equities

The long-term debt-to-total-assets ratio measures the proportion of a company's assets financed by long-term debt. It indicates the company's long-term financial position and its ability to meet loan obligations. The ratio result reflects the percentage of assets that would need to be liquidated to repay long-term debt, and tracking it over time reveals trends in financing choices and debt repayment capability (Kenton, 2020). Fairwood exhibits the highest long-term debt ratio at 118%, while the ratios for the other two competitors stand at 40% and 57% respectively. The elevated long-term debt ratio of Fairwood may be attributed to the inclusion of "Provisions" within their Non-Current Liabilities (Fairwood Holdings Limited, 2023d, p.83), amounting to HK\$47,450,000.

2.4 Coverage Ratios

Table 6: Coverage Ratios

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Times Interest Earned	4.76	2.48	2.63	4.27	2.46
Cash Coverage	19.53	17.89	17.73	16.34	14.41

**the calculation please refer to appendix 1 Source : from this research*

Times Interest Earned=EBIT / Interest

This ratio is to measure the ability of the company income to pay the interest expense, a good TIE ratio is at least 2 or 3, especially in economic times when EBIT can fall due to revenue drops and cost inflation effects, and interest expense rises on variable rate debt as the Fed raises rates (Chen, 2022b). Fairwood's ratio dropped from 4.76 to 2.63, possibly due to the pandemic and decreased profitability. To improve their financial performance, Fairwood should consider making strategic investments to expand their product line, aiming to generate higher profits.

$$\text{Cash Coverage} = (\text{EBIT} + \text{Depreciation} + \text{Amortization}) / \text{Interest}$$

It is similar to the Times Interest Earned ratio but incorporates the inclusion of Depreciation and Amortization, showing a decreasing trend. The same recommendation applies.

2.5 Inventory Ratios

Table 7: Inventory Ratios

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Inventory Turnover	50.40	46.43	49.75	26.55	27.29
Days' Sales in Inventory	7.24	7.86	7.34	13.75	13.37

**the calculation please refer to appendix 1 Source : from this research*

$$\text{Inventory Turnover} = \text{Cost of Good Sold} / \text{Inventory}$$

Inventory turnover is a financial metric that measures how quickly a company sells and replaces its inventory. It is calculated by dividing the cost of goods sold by the average inventory. A high turnover indicates efficient inventory management, while a low turnover suggests slow sales or excess inventory (Fernando, 2023c). Fairwood have the strongest ratios regarding inventory management.

2.6 Receivables Ratios

Table 8: Receivables Ratios

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Receivables Turnover (times)	26.53	19.92	33.59	203.22	58.13
Average Collection Period (days)	13.76	18.32	10.87	1.80	6.28

**the calculation please refer to appendix 1 Source : from this research*

$$\text{Receivables Turnover} = \text{Sales} / \text{Account Receivable}$$

Receivables turnover is a financial ratio that measures how quickly a company collects its accounts receivable. It is calculated by dividing net credit sales by average accounts receivable. A higher ratio indicates efficient collection, while a lower ratio suggests potential issues with credit

management or delayed payments. Comparing the ratio to industry peers or historical performance provides valuable insights (Murphy, 2023). Fairwood is shortening the average collection period, yet it remains the longest among the comparison.

2.7 Operating Period and Cash Period

Table 9: Operating Period and Cash Period

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Operating Period	21.00	26.18	18.20	15.55	19.65
Cash Period	-35.63	-21.09	-34.62	-29.00	8.39
Total Asset Turnover	1.08	1.23	1.31	0.81	1.12

**the calculation please refer to appendix 1 Source : from this research*

Operating Period = Inventory Period + Collection Period

Fairwood's operating period is 18.2 days and the cash period is -34.6 days. Fairwood's negative cash period indicates that they collect cash from customers before needing to pay suppliers, resulting in a shorter cash conversion cycle. This provides them with more liquidity and potentially reduces the need for external financing (Deegan, 2021).

Total Asset Turnover = Sales / Total Assets

Total Asset Turnover is a ratio that measures a company's efficiency in generating sales from its total assets. It is calculated by dividing net sales by average total assets. A higher ratio indicates better asset utilization and revenue generation (Hayes, 2022a). Fairwood have the higher ratio among this comparison.

2.8 Profitability

Table 10: Profitability

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Gross Profit Margin	12%	8%	8%	73%	9%
Net Profit Margin	7%	3%	1%	7%	1%
EBITDA Margin	25%	22%	20%	30%	18%
Return on Assets (ROA after tax)	8%	3%	2%	5%	2%
Return on Equity (ROE after tax)	24%	11%	7%	10%	4%

**the calculation please refer to appendix 1 Source : from this research*

Gross Profit Margin = (Sales – Cost of goods sold) / Sales

Net Profit Margin = Net Income after tax / Sales

EBITDA Margin = EBITDA / Sales

These 3 ratio are measures the profitability of a company's core operations. A higher margin indicates better profitability, while a lower margin suggests higher production costs or pricing pressures (Bloomenthal,2021). Fairwood and Café de Coral have similar ratios. However, Fairwood's margin has been decreasing, indicating a need for investment in new product lines to boost profitability. Tsui Wah's surprisingly high ratios may be due to the inclusion of costs in the balance sheet, obscuring the true extent of expenses.

Return on Assets (ROA after tax) = Net Income after Tax / Total Assets

Return on Equity (ROE after tax) = Net Income after Tax / Total Equity

ROA after tax is a ratio that measures a company's profitability in relation to its total assets, accounting for taxes. It is calculated by dividing net income by average total assets. A higher ratio indicates better profitability and efficient asset utilization (Kenton, 2021)

ROE after tax is a ratio that measures a company's profitability in relation to its shareholders' equity, considering taxes. It is calculated by dividing net income by average shareholders' equity. A higher ratio indicates better profitability and efficient use of equity. (Fernando, 2023d)

The decreasing trends observed in these two return ratios suggest that Fairwood should consider investing in new high-profitability projects to achieve higher returns.

2.9 Market Value

Table 11: Market Value

Company	Fairwood			Tsui Wah	Café de Coral
Year	2021	2022	2023	2023	2023
Market Capitalisation (\$,000)	\$2,204,652	\$1,968,902	\$1,526,134	\$3,457	\$6,091,322
PE ratio	11.58	26.24	34.00	0.06	54.78
Market-to-book ratio	2.83	2.76	2.24	0.01	2.18

**the calculation please refer to appendix 1. Source : from this research and the PE ratios are from FUTU*

Market Capitalisation = Price per share * Number of shares

Market Capitalization is calculated by multiplying the price per share by the number of shares outstanding. It represents the total value of a company's equity in the market and is used to assess its size and value. (Fernando, 2022) The declining trend in Fairwood's market capitalization can be attributed to a decrease in profitability and the economic downturn, leading to shareholder concerns regarding the company's future prospects. To address this issue, Fairwood should consider investing in a high-profitability project, such as an elderly caring service. This strategic move not only has the potential to enhance profitability but also improves Fairwood's social perception and reputation. By expanding its operations into the elderly care sector, Fairwood can garner positive attention and potentially restore investor confidence.

PE ratio = Price per share / Earnings per share

The P/E ratio is a financial metric calculated by dividing the price per share by the earnings per share. It is used to assess the relative value of a company's stock. A higher P/E ratio suggests higher market expectations, while a lower ratio may indicate potential undervaluation (Picardo, 2019).

Market-to-book ratio = Market Value Per Share / Book Value Per Share

The Market-to-Book ratio (M/B ratio) compares the market value of a company to its book value. A higher ratio suggests positive market sentiment and potential growth expectations, while a lower

ratio may indicate undervaluation or lower growth prospects (Kenton, 2019). Fairwood should strive to cultivate a more positive market sentiment by engaging in CSR or ESG campaigns.

3 Fairwood's Corporate Governance Assessment

Based on the financial assessment analysis conducted in Chapter 2, it is evident that Fairwood is experiencing a decline in profitability, increasing costs, and the potential for expanding its current business in Hong Kong is limited. Consequently, it becomes imperative for Fairwood to explore the governance structure and assess any risks pertaining to its internal control and risk management.

The presence of an Executive Director alongside Independent Non-executive Directors in the Nomination Committee may raise concerns regarding objectivity and independence. To enhance corporate governance practices, it is recommended to reassess the composition of the Nomination Committee by eliminating the representation of Executive Directors and prioritizing the inclusion of Independent Non-executive Directors. The decision to involve an Executive Director in the nomination committee should be cautiously deliberated, considering the company's specific circumstances and corporate governance guidelines. While the participation of an Executive Director can offer valuable insights, it is crucial to maintain a balance in their involvement to uphold independence and objectivity. Discussions pertaining to Executive Director performance and succession planning may necessitate their exclusion (KPMG Board Leadership Centre, 2022). Ultimately, a comprehensive evaluation is required to ensure the effectiveness of the nomination process.

In order to fulfill their responsibilities as committee and board members, it is crucial to offer guidance and advice to the team rather than expressing uncertainty about future plans to investors and the public (Eisenstein, 2019). The statement in Fairwood's ESG report mentioning that the Group is contemplating new ways to enhance environmental sustainability and social responsibility falls short of providing concrete plans and strategies (Fairwood Holdings Limited, 2023b, p. 65). Given the prominence of ESG considerations in the market, it would be more appropriate for committee and board members to present well-defined plans, thereby demonstrating a stronger commitment to sustainability and responsible practices. As stakeholders or investors, it is important to seek specific details and evidence regarding Fairwood's initiatives and progress in environmental stewardship and social responsibility. Transparent disclosure and concrete information would facilitate a better understanding of Fairwood's dedication to sustainability and its potential for long-term growth. Enhancing these aspects could foster a more positive market sentiment, leading to improved market capitalization and brand image.

Table 12: Suggestions to Fairwood regarding its governance

Nomination Committee	Reassess the composition of the Nomination Committee by reducing or eliminating the representation of Executive Directors and emphasizing the inclusion of Independent Non-executive Directors. This will enhance the committee's independence and impartiality in the board nomination process.
Board Refreshment	Consider periodically refreshing the composition of the Board of Directors by appointing new members with diverse backgrounds and expertise. This can bring in fresh perspectives and ensure the board remains dynamic and adaptable to changing market conditions and stakeholder expectations (III and Neal, 2020). Joining new members with relevant expertise and experience in compensation and benefits can provide valuable insights and impartial recommendations, ensuring fairness and alignment with industry practices.
Stakeholder Engagement	Establish effective mechanisms for engaging with stakeholders, including customers, employees, shareholders, and the local community. Regular dialogue and feedback mechanisms can help understand stakeholder expectations, address concerns, and foster trust and transparency (Fleischer, 2009).
Training and Development	Invest in ongoing training and development programs for board members and employees to enhance their understanding of corporate governance, ethics, and sustainability. This will promote best practices, foster a culture of compliance, and encourage responsible decision-making.

Source: from this research

By incorporating new board members and external experts into the governance structure, Fairwood can benefit from a broader range of perspectives and knowledge. This can contribute to more robust decision-making processes, improved governance practices, and enhanced stakeholder confidence.

4 Investment Project Appraisal

Based on a careful assessment of Fairwood's financial ratios, it is recommended that the company consider investing in a new project and introducing a new product line: delivering soft meals to private nursing homes (as public nursing homes typically have in-house kitchens). This initiative can be initiated as a pilot program and, if successful, may expand to provide household services.

The aging society indicates a foreseeable increase in demand (Hong Kong Census and Statistics Department, 2017), supported by the HKCSS report, which highlights a specific demand for soft meals in society (The Hong Kong Council of Social Service, 2019).

By being a first mover in this business segment, Fairwood can gain a significant competitive advantage as there are currently no competitors operating in this space. Being the first company to deliver soft meals to private nursing homes, Fairwood can leverage the first mover advantage. This allows them to establish brand recognition, build customer loyalty, set industry standards, and secure key partnerships before competitors enter the market (Tarver, 2020).

This endeavor also demonstrates Fairwood's commitment to caring for the elderly, making it a potential signature campaign for their environmental, social, and governance (ESG) initiatives. This not only enhances positive market sentiment but also strengthens the company's brand image.

Furthermore, the initial investment cost for this project is relatively low, allowing Fairwood to preserve its financial advantage and maintain its debt-free status.

Fairwood should use financial ratios like Net Present Value (NPV) to assess the investment in delivering soft meals to private nursing homes. NPV considers the project's cash flows and compares them to the initial investment. Other ratios like ROI, Payback Period, and IRR can provide additional insights. This analysis will help Fairwood make informed decisions about the project's feasibility and potential profitability, ensuring financial stability and growth.

Table 13: Basic information and assumptions of the investment plan

Basic information	(HK\$,000)	Assumptions and Remarks
Equipment cost (Blender)	(103.68)	The blenders, which cost HK\$8,640 each (purchased from Taobao), are required in a quantity of 12 to meet the demand
Equipment cost (Sally Robot for packing soft meals)	(2,880)	The robot cost HK\$240,000 each (Guszkowski, 2022). Need 12 in order to meet the demand.
Lorry Cost	(2,099)	Lorry for delivering services. One new lorry cost \$350,000 (MoneyHero, 2022). Need 6 for 3 main districts in Hong Kong.
Initial Cost	(5,083)	
Estimated total Sales (year)	25,498.9	In Hong Kong, there are 618 privately listed nursing homes, collectively offering a total of 69,854 spots (Social Welfare Development, 2023). As per the International Dysphagia Diet Standardization Initiative (IDDSI), the classification of food textures comprises 7 levels (SIK SIK YUEN, 2019). Soft meals predominantly cater to Level 4, characterized by pureed foods possessing a smooth and cohesive texture. Additionally, Level 5 is also accommodated, encompassing minced or chopped foods that are soft and easily masticated. These specific texture levels are specifically targeted within soft meals to accommodate individuals with swallowing difficulties. $=69854/7*2=4990$ elderly=potential demand in the market Each day 2 meals, lunch and dinner. $4990 \text{ elderly} * 2 \text{ meals} = 9980$= demand per each day There are 4 main soft meals providers in Hong Kong (耆跡軟遠 ProblemSofting, 2020),safely assume Fairwood can have 50% of the 1/5 market when competing with 4 main and other competitors

		$=9980/5=1,996$ meals per day Average sales price of 1 prepack soft meal: \$70 (樂齡網, 2023) $1996 \text{ meals} * \$70 = \$139,720$ (sales daily) $\$139,720 * 365 = \$50,997,800$ $\$50,997,800 * 50\% = \$25,498,900$ The first year calculation of sales (HK\$,000): 25,498.9
Sales Growth rate (%)	6.9%	Growth rate from 2021 to 2022 = 8.9% Growth rate from 2022 to 2023= 4.9% Take average of these two %=6.9%
EBITDA %	18.58%	EBITDA from 2023
Depreciation	33 % for equipment 15 % for lorry	From 2022-23 Fairwood's annual report and Fairwood is adopting straight-line basis for calculating depreciation (Fairwood Holdings Limited, 2023, p.23)
Tax	16.5%	(香港政府一站通, 2023)

Source : from this research

Table 14: Projected Sales revenue and related numbers

Sales Growth	6.9%					
Year		1	2	3	4	5
Sales		25,498.9	27,258.3	29,139.1	31,149.7	33,299.1
EBITDA	18.58%	4,737.70	5,064.60	5,414.05	5,787.62	6,186.97
Equipment cost (blender)	Depre rate: 33% straight-line basis	34.21	34.21	34.21	34.21	34.21
Equipment cost (sally robot)	Depre rate: 33%	950.40	950.40	950.40	950.40	950.40
Equipment cost (lorry)	Depre rate: 15%	314.82	314.82	314.82	314.82	314.82
Total depreciation		1,299.44	1,299.44	1,299.44	1,299.44	1,299.44
EBIT		3,438.26	3,765.16	4,114.62	4,488.19	4,887.53
Tax	Tax rate: 16.5%	567.31	621.25	678.91	740.55	806.44
Profit		2,870.95	3,143.91	3,435.70	3,747.63	4,081.09
EBITDA		4,737.70	5,064.60	5,414.05	5,787.62	6,186.97
Expenditure 1	Salary of Dietitian*	(1,378.92)	(1,434.08)	(1,491.44)	(1,551.10)	(1,613.14)
Expenditure 2	Salary of Speech therapist**	(1,445.16)	(1,502.97)	(1,563.09)	(1,625.61)	(1,690.63)
Maintenance	1.5 % of the sales, reference to 2023	(382.48)	(382.48)	(382.48)	(382.48)	(382.48)
Tax		(567.31)	(621.25)	(678.91)	(740.55)	(806.44)
Cashflow		963.82	1,123.82	1,298.13	1,487.88	1,694.27

* the average salary of a dietitian in Hong Kong is HK\$57,455, with an annual salary adjustment of 4% (香港公務員資訊網, 2023)

** the average salary of a speech therapist in Hong Kong is HK\$60,215, with an annual salary adjustment of 4% (indeed, 2023)

Source : from this research, calculation and related numbers please refer to appendix 2

Table 15: Cashflow and NPV

Year	Cashflow in/(out)	PV of cashflow	CUM Cashflow	Profit
0	(5,083)	(5,083)	(5,083)	
1	963.8	945	(4,119)	3,116.2
2	1,123.8	1,080	(2,995)	3,389.7
3	1,298.1	1,223	(1,697)	3,682.1
4	1,487.9	1,375	(209)	3,994.6
5	1,694.3	1,535	1,485	4,328.8

Source : from this research, calculation and related numbers please refer to appendix 3

Table 16: Evaluation methods

Method	Estimated result
Method 1 NPV	1,074.48
Method 2 PBP	4 year 1months
Method 3 IRR	8.3%
Method 4 PI	1.21
Method 5 ARR	72.8%

Source : from this research, calculation and related numbers please refer to appendix 3

Net Present Value: Net Present Value (NPV) is a financial metric that assesses the profitability of an investment by calculating the present value of expected cash flows. A positive NPV indicates a profitable investment, while a negative NPV suggests it may not be viable (Fernando, 2023d). As mentioned, this project will result in a positive NPV of HK\$1,074,480, indicating that Fairwood will earn more profit. The Net Present Value (NPV) method has limitations. It relies on accurate cash flow and discount rate estimations, does not consider the scale of investment, assumes discrete time intervals, neglects non-financial factors, and assumes a constant discount rate.

The payback period represents the time needed for an investment to recover its initial cost (Kagan, 2023). In the food and beverage industry, payback periods of 4 years are considered cost-effective (Bhadbhade & Patel, 2020). With a payback period of 4 years and 1 months, this project is both cost-effective and ideal. Limitations of the Payback Period method include its disregard for the time value of money, exclusion of cash flows beyond the payback period, failure to measure profitability directly, overlooking cash flow timing, subjective decision-making, and limited focus on recovering the initial investment.

The Internal Rate of Return (IRR) is a financial metric that assesses investment profitability by determining the discount rate at which cash flows reach zero NPV. It helps compare investment opportunities and indicates the expected rate of return (Fernando, 2023f). An IRR of 8.3% indicates a higher expected rate of return for the project or investment than ROA of fairwood.

Profitability Index (PI) compares the present value of cash inflows to the initial investment. A PI greater than 1 suggests potential profitability, while a PI less than 1 indicates a potential loss. It aids in evaluating investment options (Chen, 2022a). PI of this project is 1.21, it means potential profitability.

Accounting Rate of Return (ARR) is a financial metric used to assess investment profitability based on average annual accounting profit and initial investment, higher ARR indicates greater profitability (Murphy, 2022).

ARR is a non-discounted cash flow formula that doesn't consider the time value of money. IRR, on the other hand, is a discounted cash flow formula that incorporates the present value of future cash flows, accounting for the time value of money. Due to its consideration of the time value of money, the IRR is a more realistic measure of investment profitability and should be given greater consideration.

5 Financing and Capital Management

The new project of Fairwood requires an initial cost of HK\$ 5,082,504, which represents approximately 0.22% of the total assets and 0.17% of last fiscal year's sales revenue.

Table 17: Initial cost compare with total assets and 2022-2023's revenue

Initial cost of the project	Total Assets	Initial cost / Total Assets	2022-2023 Sales Revenue	Initial cost / 2022-2023 Sales Revenue
HK\$ 5,082,504	HK\$ 2,302,545,000	0.22%	HK\$ 3,024,152,000	0.17%

Source : from this research

Although the percentage is relatively small, the liquidity ratios indicate some concerns. The current ratio stands at 0.97, the quick ratio at 0.9, and the cash ratio at 0.79. A healthy finance position for the company typically entails a cash ratio should be equal to or greater than 1 (Hayes, 2019b).

Therefore, it would be advisable to explore alternative financing programs to raise the initial project cost, rather than relying on the revenue from the previous year. This approach would prevent further decline in the liquidity ratios. Below will analyse various financing program.

Table 18: Financing programs pros and cons

Source	Methods	Pros:	Cons:
Internal Source	Retained Earnings:	● No additional cost or interest associated with using retained earnings. ● Provides flexibility and control over the allocation of funds. ● Demonstrates financial stability and confidence to external stakeholders.	● May limit dividend payments to shareholders. ● Availability of retained earnings depends on profitability. ● Can restrict immediate distribution of profits to shareholders.
Internal Source	Working Capital Management	● Optimizing working capital improves cash flow and liquidity. ● Reduces the need for external financing.	● Requires effective management and monitoring of cash conversion cycle.

		● Enhances operational efficiency and profitability.	● May require adjustments to inventory levels, affecting supply chain management. ● Over-optimization of working capital may impact customer or supplier relationships.
Internal Source	Cost Reduction Initiatives	● Generates internal funds without relying on external sources. ● Increases profitability and enhances cost efficiency. ● Creates a culture of continuous improvement within the organization.	● Cost reduction measures may require upfront investments. ● Potential resistance from employees due to changes in processes or job roles. ● Cost-cutting may negatively impact quality or customer satisfaction if not managed properly.
Internal Source	Sale of Assets	● Provides immediate funds for growth initiatives. ● Liquidates underutilized assets and improves efficiency. ● Enables a strategic focus on core business activities.	● Loss of long-term revenue or asset value. ● May disrupt ongoing operations or require adjustments to business strategies. ● Selling assets at unfavorable market conditions may result in lower returns.
External Source	Equity Financing/Shares	● Provides additional capital without incurring debt.	● Dilution of ownership and control for existing shareholders.

		● Shares the financial risk and burden with new shareholders. ● Can bring in expertise and strategic partnerships.	● Increased reporting and disclosure requirements. ● Potential conflicts among shareholders regarding decision-making and company direction.
External Source	Debentures	● Enables companies to raise long-term capital. ● Fixed interest payments provide predictability. ● No dilution of ownership for existing shareholders. ● Flexibility in terms and customization options. ● Diversifies the investor base.	● Creates debt obligations and strain on cash flow. ● Involves regular interest payments, increasing the cost of capital. ● Collateral may be required, limiting flexibility. ● Can impact credit rating and borrowing capacity. ● Interest rates influenced by market conditions.
External Source	Bank Loans	● Quick access to funds for immediate financing needs. ● Flexible repayment options based on the company's cash flow. ● Can be secured or unsecured, depending on the terms and collateral provided	● Interest payments increase the cost of capital. ● Loan approval may be subject to strict criteria and creditworthiness. ● Short-term nature may require frequent refinancing or renewal.

			● Lack of friend banks to offer low interest rate loans ● High interest rate in 2023
External Source	Overdraft Facilities	● Provides flexibility in managing short-term cash flow fluctuations. ● Allows access to funds as needed, reducing the need for constant borrowing. ● Interest is charged only on the amount utilized.	● Higher interest rates compared to traditional loans. ● Over-reliance on overdraft facilities may indicate financial instability. ● Banks can demand repayment or change terms at any time.
External Source	Trade Credit	● Convenient financing option as it involves deferring payment to suppliers. ● Helps in managing short-term cash flow mismatches. ● Can be negotiated for favorable terms with trusted suppliers.	● Limited by the credit terms offered by suppliers. ● Over-reliance on trade credit may strain supplier relationships. ● Potential impact on creditworthiness if payment terms are not honored.

(GoCardless, 2020)

After evaluating the circumstances surrounding Fairwood, it is recommended that the company considers issuing shares through a private placement offering to a targeted group comprised of ESG experts and investors who share the company's values (GANTI, 2019). This approach would enable Fairwood to secure additional capital for the new project while also benefiting from the insights and contributions of these shareholders in the future development of its ESG planning. It is confident enough as the PE ratio is increasing for the past 3 years.

The determination of share prices would be based on negotiations with the target group and consideration of prevailing market conditions. Once the shares are successfully sold, Fairwood can

actively engage the ESG experts who have become shareholders, seeking their input, expertise, and advice in formulating and executing the company's ESG strategy. Leveraging their knowledge and experience in the field, these experts can offer valuable insights, guidance, and recommendations.

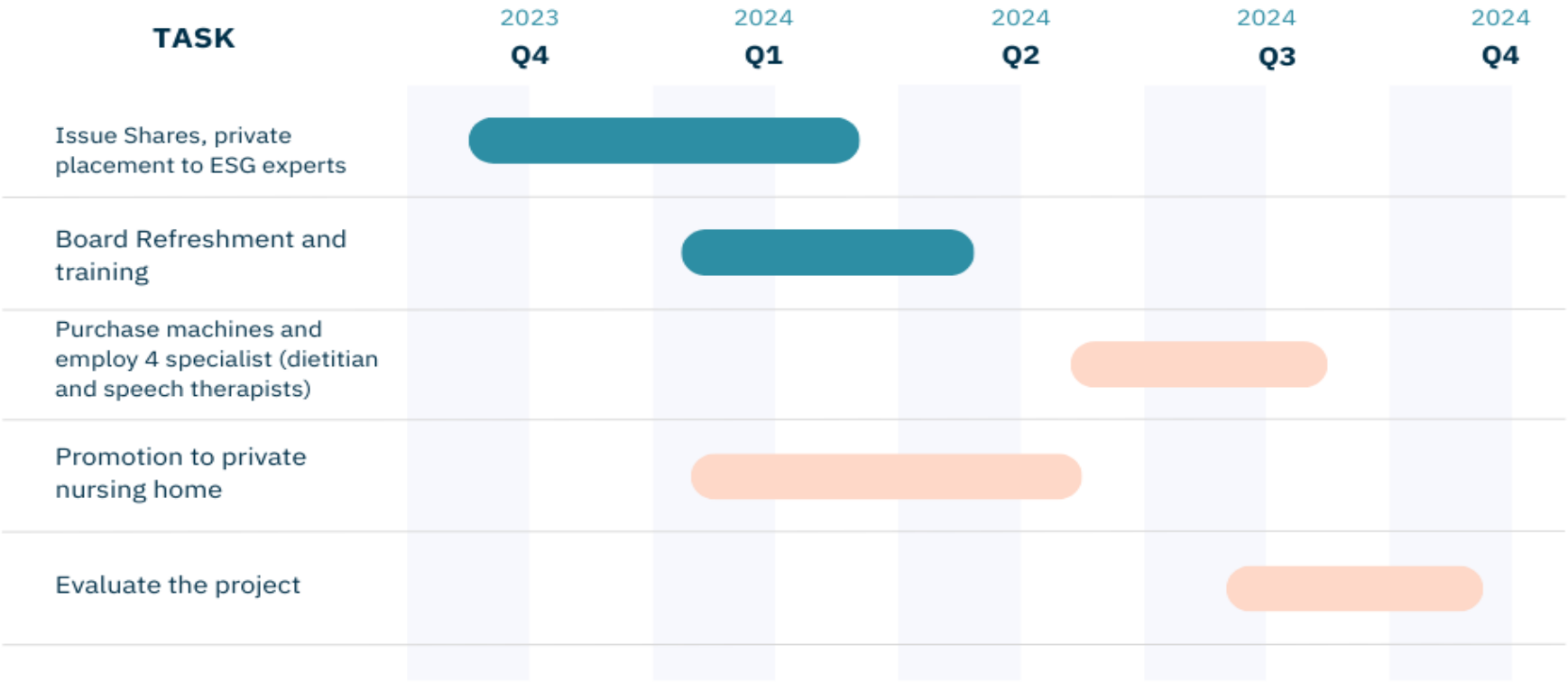
By involving these experts in the decision-making process, Fairwood can effectively enhance its ESG performance, align its practices with industry best practices, and ensure the effectiveness and impact of its initiatives. Moreover, the presence of ESG experts as shareholders would serve as a tangible demonstration of the company's commitment to sustainability and responsible business practices, reinforcing its reputation among stakeholders, including investors, customers, and the broader community.

6 Schedule

Fairwood New Project

Delivering soft meals to private nursing homes

GANTT CHART



7 Conclusion

In conclusion, Fairwood Holdings Limited exhibits a relatively healthy financial status compared to its competitors; however, there are areas that require improvement. Cost control measures should be implemented to increase profitability and improve key financial ratios, aiming to achieve a Z-score of at least 3. Additionally, enhancing liquidity ratios can be achieved by increasing cash reserves through financing programs. Implementing a proactive payment reminder system to debtors can effectively expedite the collection of outstanding payments.

To foster further growth, Fairwood should consider investing in a profitable new project, such as the development and launch of a new product line catering to the needs of private nursing homes. This initiative aligns with the demands of an aging population and serves as an opportunity to enhance the company's reputation, generate positive market sentiment, and improve its brand image, particularly in terms of displaying care for the elderly and social responsibility. Initial funding for this venture can be obtained through issuing shares with private placement to ESG-focused investors, simultaneously sourcing capital and gaining valuable insights from these stakeholders.

Moreover, Fairwood should prioritize enhancing corporate governance practices to ensure transparency, accountability, and compliance with regulations. Initiatives such as Board Refreshment and Training and Development programs can stimulate innovation and bring fresh perspectives to the company. Additionally, dedicating more effort to stakeholder engagement will strengthen relationships with key stakeholders, fostering mutual understanding and collaboration.

By implementing these recommended improvements, Fairwood can further enhance its financial performance, reputation, and corporate governance practices. These measures will position the company for sustained growth and success in the competitive fast-food industry.

(4934 words)

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11 Appendices

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Appendix 5: Fairwood Annual report 2022-23

Appendix 6: Fairwood Annual report 2021-22

Appendix 7: Fairwood Annual report 2020-21

Appendix 8: Tsuiwah Annual report 2022-23

Appendix 9: Café de carol Annual report 2022-23

Appendix 1: Calculation of the ratios of 3 companies

[illegible]

Appendix 2: Calculation for new investment project for Fairwood

	(\$1K)		HKD					
12	Equipment cost	Blender	(103.680)					0.22%
12	Equipment cost	Sally robot	(2,880.000)					
	Lorry		(2,098.824)				5,082,504	
	Initial cost		(5,082.504)			\$2,302,545	2,302,545,000	
	Total Sales		25,498.90	50.0%				
			100%					
			-					
	Direct		25,498.9					
	Total		25,498.9					
	Sales Growth		6.9%					
	Yr		1	2	3	4	5	
	Sales		25,498.9	27,258.3	29,139.1	31,149.7	33,299.1	
	EBITDA	18.58%	4,737.70	5,064.60	5,414.05	5,787.62	6,186.97	
	Depr	straight line depr mthd						
	Equipment cost	33%	34.21	34.21	34.21	34.21	34.21	
	Equipment cost	33%	950.40	950.40	950.40	950.40	950.40	
	Lorry	15%	314.82	314.82	314.82	314.82	314.82	
	Total Depr		1,299.44	1,299.44	1,299.44	1,299.44	1,299.44	
	EBIT		3,438.26	3,765.16	4,114.62	4,488.19	4,887.53	
	Tax	16.5%	567.31	621.25	678.91	740.55	806.44	
	Profit		2,870.95	3,143.91	3,435.70	3,747.63	4,081.09	
	EBITDA		4,737.70	5,064.60	5,414.05	5,787.62	6,186.97	
4%	Expenditure 1	Sal	(1,378.92)	(1,434.08)	(1,491.44)	(1,551.10)	(1,613.14)	
	Expenditure 2	Sal	(1,445.16)	(1,502.97)	(1,563.09)	(1,625.61)	(1,690.63)	
	Maintence	1.50%	(382.48)	(382.48)	(382.48)	(382.48)	(382.48)	
	Tax		(567.31)	(621.25)	(678.91)	(740.55)	(806.44)	
	Cashflow		963.82	1,123.82	1,298.13	1,487.88	1,694.27	

Appendix 3: NPV assessment methods and ratios for new project

Yr	Cashflow in/(out)	PV of cashflow	CUM Cashflow	Profit		ROA	2.0%	
0	(5,083.0)	(5,083.0)	(5,083.0)			Growth rate		
1	963.8	945	(4,119)	3,116.2		Payback period calculation:		
2	1,123.8	1,080	(2,995)	3,389.7		141.1891667	-68.1608	1
3	1,298.1	1,223	(1,697)	3,682.1			73.02833	2
4	1,487.9	1,375	(209)	3,994.6			214.2175	3
5	1,694.3	1,535	1,485	4,328.8			355.4067	4
Method 1 NPV	1,074.48	1,074.48					496.5958	5
Method 2 PBP	4 year 1months						637.785	6
Method 3 IRR	8.3%						778.9742	7
Method 4 PI	1.21						920.1633	8
Method 5 ARR	72.8%						1061.353	9
							1202.542	10
							1343.731	11