

China Green



Whisked by the milk storm

BUY (unchanged)

Involvement. We had a short discussion with the management recently regarding its involvement in the tainted milk scandal and potential impact. The company imports milk powder from New Zealand and uses it as raw material in producing corn milk, which accounted for 11.7% (RMB147.8m) of the total turnover in FY04/08A. Although no quality problem has been spotted yet, sales of corn milk in Oct declined as the scandal affected domestic food industry in general. The company expects a sales recovery next year.

Our view. As the company imports milk powder from New Zealand, we reckon its potential to be directly involved in this milk storm is low. For liquid milk, demand slashed over 70.0% at the sandal's outbreak in Sep and recovered to around 60.0 – 70.0% of previous normal level in Oct. We expect contraction in corn milk market to be more or less moderate.

Export business intact. Geographical expansion is the major driver for overseas business. The company is developing new markets, especially in Europe and Middle-East region.

Gains from the rural reform. We expect the rural reform to accelerate market consolidation. As a sizable player, CG is more capable to benefit from the trend and obtain market share from smaller players.

Forecast adjustments. We revise down our estimates of beverage sales for FY04/09F by 12.5% to RMB262.4m but hold the segmental growth assumption for years thereafter. Meanwhile, we raise our growth assumption for CG's domestic sales of fresh produce and processed food by 5.0pcc (fresh produce: 10.0% to 15.0%; processed products: 20.0% to 25.0%) for FY04/10F and FY04/11F to reflect the potential benefit from the rural reform. Overall we lower CG's earnings forecast by 5.6% to RMB486.2m in FY04/09F, 2.5% to RMB567.4m in FY04/10F and 1.7% to RMB688.8m in FY04/11F.

Valuation. Despite the cut in forecast, we maintain bullish on the counter, given its: 1) well position to benefit from China's rural reform; 2) overseas sales to be continuously driven by geographic expansion. Our target price is unchanged at HK\$8.17, which represents a forward P/E of 13.1x.

China Agriculture

Wed, 22 Oct 2008

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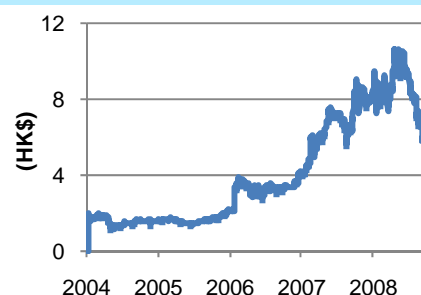
Stock data

Price	HK\$4.51
Target price	HK\$8.17(+81%)
12 mth range	HK\$4.04-11.30
Market cap.	US\$49.9m
Daily t/o, 3 mth	US\$1.3m
Free float %	49.6%
Ticker	904.HK/0904 HK

Financial summary

Year to Dec	06A	07A	08F	09F	10F
T?O (RMBm)	954.1	1,267.1	1,626.8	2,058.9	2,520.3
NP (RMBm)	346.0	471.0	486.2	567.4	688.8
EPS (RMB)	0.448	0.538	0.550	0.642	0.779
EPS Δ %	20.1	20.1	2.3	16.6	21.4
P/E (x)	8.9	7.4	7.2	6.2	5.1
P/B (x)	1.82	1.55	1.33	1.14	0.99
EV/EBITDA (x)	6.3	4.2	4.2	3.2	2.0
Yield (%)	2.4	3.2	4.0	4.9	5.8
ROE (%)	24.6	24.0	20.0	19.9	20.9
ROCE (%)	21.7	19.9	16.2	17.9	23.3
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Price Chart



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Table 1: P&L

Year to Apr (RMBm)	07A	08A	09F	10F	11F
Turnover	954.1	1,267.1	1,626.8	2,058.9	2,520.3
Cost of sales	(456.2)	(590.5)	(761.5)	(941.1)	(1,138.9)
Gross profit	497.9	676.6	865.2	1,117.8	1,381.4
Other revenue	23.8	58.3	58.9	40.0	36.0
Gain arising from changes in fair value less estimated point-of-sale costs of biological assets	15.2	19.9	23.7	29.0	34.8
Selling and distribution expenses	(92.9)	(125.2)	(194.8)	(261.9)	(302.7)
General and administrative expenses	(83.8)	(119.4)	(177.7)	(214.5)	(237.4)
Operating profit	360.1	510.3	575.3	710.3	912.0
Finance cost	(14.4)	(26.6)	(58.0)	(58.0)	(29.0)
Profit before taxation	345.8	483.7	517.3	652.2	883.0
Income tax	0.2	(12.8)	(31.0)	(84.8)	(194.3)
Net profit	346.0	471.0	486.2	567.4	688.8
EPS - basic (RMB)	0.448	0.538	0.550	0.642	0.779
EPS - diluted (RMB)	0.417	0.506	0.550	0.630	0.771

Source: Company data, SBI E2-Capital