

Focus on acquisitions

Hong Kong Industrials

AMVIG (2300 HK, HK\$5.80)

Not Rated

Company profile. Listed in 2004, AMVIG (previously named as Vision Grande) is a printer of cigarette packages and manufacturer of laminated paper for cigarette packages. The name stands for AMcor + VIsion Grande + World Grande, which has been perceived as a sign of integration success.

Internal sourcing. It produces laminated paper for its own use, which allows it to protect its profit margin and ensure the steady supply and quality of one its key cigarette packaging materials.

Table 1: Production facility

Location	Capacity (master cases*)
Beijing plant	300,000
Kuming plants	1,000,000
Nanjing plant	600,000
Qingdao plant	800,000
Shenzhen plant	400,000
Dongguan Plant	Expected to commence operation in last quarter of 2007

Source: SBI E2-Capital

* Master case = 2500 pack of cigarettes

Industry overview. With 1.9t sticks of cigarettes consumed every year (or c.1/3 of the global cigarette consumption), China is the world's largest tobacco market and is expected to grow 3-5% a year. Currently, tax payments from the tobacco industry exceed RMB300b annually. Given their importance to the country's tax revenue, all cigarette manufactures are owned and controlled by the Chinese government and the industry is closed to foreign investors, with production based on a quota system.

Market consolidation. The industry's reform in 2000 reduced the number of cigarette manufactures to 40 from 180 and further to around 10 over the next three to five years. The number of cigarette brands decreased to about 60 from more than 1,800. Market consolidation is accelerating and is expected to enter the cigarette packaging and printing sector.

Table 2: Interim results

Six months to Jun (HK\$m)	05A	06A	YoY
Turnover	173.6	404.1	132.8
Gross profit	66.2	110.5	66.9
Operating profit	37.8	66.7	76.5
Pre-tax profit	72.4	102.7	41.9
Net profit	69.4	90.1	29.8

Source: Company data

Table 3: Recent acquisitions

Date	Activity	Consideration
May-06	Successfully acquired the remaining 68.5% equity interest in World Grand and took full control of Kunming World Grand.	HK\$928.1m (HK\$439.5m in cash and HK\$488.6m in 69.8m new shares issued at HK\$7)
Feb-06	Successfully acquired Bellgate International, which owns 60% of Qingdao Leigh-Mardon and 83% of Beijing Leigh-Mardon cigarette package printing plants.	HK\$509m (121.2m new shares at HK\$4.20)

Source: SBI E2-Capital

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Rising ASP. The current ASP for a pack of cigarettes is RMB3 and is expected to rise to RMB6 in 2007 and RMB10 in 2008 respectively as the purchasing power in China increases and more smokers switch to higher-priced products with better brand names.

Table 4: Key customers

Key customers	% of turnover
Etsong Tobacco Group	25%
Hung Yun Tobacco Group	25%
Guangdong Tobacco Group	10%
Nanjing Cigarette Factory	10%
Baisha Tobacco Group	5%
Huaiyin Cigarette Factory	8%

Source: SBI E2-Capital

More acquisitions. With 8-9% of the market currently, AMVIG aims to boost its market share to 20-25% within three to five years through acquisitions. After two acquisitions last year, the company plans to acquire two companies this year, one in 1H07 and one in 2H07, to combat pricing pressure as a result of the market's rationalization.

Entry barriers and competitive advantage. Entry barriers in the tobacco industry are getting higher. A newcomer needs a printing licence and sufficient capital as well as good relations with large tobacco companies. AMVIG has long-established ties with some of China's largest tobacco companies. With Amcor as a substantial shareholder, AMVIG can share resources with the world's biggest packaging company in terms of technical know-how and management expertise (the current chairman of AMVIG is ex-managing director of Amcor Asia). Amcor's backing and strong reputation make AMVIG attractive to many big tobacco companies.

Valuation. The company currently has HK\$400m in net cash on hand, which it plans to use to fund more acquisitions. Its payout ratio is set at 40%. Currently, the counter is trading at c. 16.8x FY12/06F P/E, at a premium to its peer average of 12.8x FY12/06F P/E on a consensus basis.

Table 5: Peer comparison

Company name	Ticker	Year end	Market cap (US\$m)	P/E (x) 1-yr Fwd	P/E (x) 2-yr Fwd
AMVIG Holdings Limited	2300 HK	Dec	594.1	16.8	12.2
Kith Holdings Limited	1201 HK	Dec	137.1	na	na
Shanghai Asia Holdings Limited	SAHL SP	Dec	77.6	8.8	6.4
<i>Average</i>				12.8	9.3

Source: Bloomberg and SBI E2-Capital

Table 6: P&L

Year to Dec (HK\$m)	03A	04A	05A
Turnover	232.0	332.4	383.5
Cost of sales	(148.4)	(200.9)	(221.8)
Gross profit	83.6	131.5	161.7
EBITDA	63.1	100.0	120.3
Depre./amort.	(7.8)	(10.7)	(18.9)
EBIT	55.4	89.3	101.4
Net int. income/(exp.)	(8.7)	(9.0)	9.5
Exceptionals	na	na	na
Associations	47.9	38.3	76.1
Jointly-controlled entity	na	na	na
Pre-tax profit	94.5	118.6	186.9
Tax	(4.3)	(7.7)	(2.1)
Minority interests	na	(0.1)	(3.4)
Net profit	90.3	110.8	184.8
EPS (HK\$) – basic	0.282	0.290	0.381
DPS (HK\$)	na	0.052	0.085

Source: Company data