

EcoGreen: Better Days Ahead

Recommendation: BUY (unchanged)

China Chemicals

Price	HK\$2.38	Year to Net profit	EPS	EPS	P/E	P/B	EV/EBITDA	Yield	ROE	ROCE	N. Gear.	
Target price	HK\$3.12 (+31.1%)	Dec	RMBm	RMB	Δ %	x	x	x	%	%	%	
12 mth range	HK\$1.08-2.50	04A	61.4	0.156	na	15.3	3.1	14.8	0.8	30.2	17.6	Cash
Market cap.	US\$140.66m	05A	71.1	0.167	7.4	14.2	2.5	13.2	1.0	18.6	14.0	Cash
Daily t/o, 3 mth	US\$0.43m	06F	90.9	0.197	17.7	12.1	1.9	10.6	1.2	17.6	14.1	Cash
Free float %	54.7%	07F	120.0	0.260	32.2	9.1	1.6	8.0	1.6	18.5	16.2	Cash
Ticker	2341.HK/2341 HK	08F	159.8	0.347	33.1	6.9	1.3	5.9	2.3	20.5	17.2	Cash

Relative to Hang Seng Index (1 mth, 3 mth, 12 mth): +17.2%, +16.7%, +63.0%

Actual price changes (1 mth, 3 mth, 12 mth): +14.2%, +9.3%, +24.0%

Consensus EPS (06F-08F): HK\$0.186, HK\$0.194, HK\$0.239

Previous forecasts (06F-08F): HK\$90.9m (\$0.197), HK\$115.1m (\$0.250), HK\$154.7m (\$0.336)

Key points:

- FY12/06F results to be announced in mid April.
- Demand for its core product, Dihydromyrcenol, is rising.
- Better gross margin against the backdrop of the falling price of gum turpentine oil.
- New high-margin products to further enhance gross margin.
- Step up efforts to secure its raw material supply.
- To benefit from the growing strength of major clients such as IFF, Givaudan and Symrise.
- Earnings forecast lifted by 4.30% for FY12/07F and 3.30% for FY12/08F on improving margins.
- Target price increased to HK\$3.12 from HK\$2.50, equivalent to 12x FY12/07F P/E.

ASP increase. The average selling price (ASP) of its core product, dihydromyrcenol, increased around 8.4% YoY in RMB terms in 2006 due to stronger-than-expected demand.

Sales volume up. To meet the growing demand, EcoGreen has to outsource around 30.0% of its production of aroma chemicals, in addition to its current capacity of 16,000 tonnes. We expect its turnover to grow at least 28.5% YoY in FY12/07F and 39.2% in FY12/08F, when its Phase III operations come on stream.

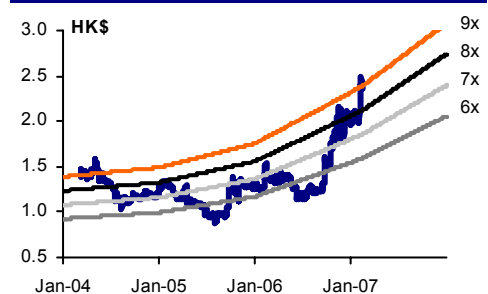
Gross margin expansion. The price of gum turpentine oil, the company's main raw material, dropped to RMB6,500 in December 2006 on the lower crude oil price and is expected to hover around RMB7,000, even if the crude price rises again. The gross margin is expected to widen by around 1.2% in FY12/07F.

New high-margin products. The company started to produce new food aroma chemicals on a trial basis in FY12/06 and will launch full-scale production by end of FY12/07. Their margins are estimated to be around 5.0% higher than those of personal care chemical products. Food aroma chemicals are expected to account for about 50.0% of the company's total turnover of aroma chemicals in the next few years.

Secure raw material supply. The company has set up a specialized raw material management team to secure its raw material supply and strengthen its upstream position. Currently, EcoGreen is estimated to be China's largest gum turpentine oil consumer.

IFF's strong results. International Fragrance and Flavours (IFF US, US\$48.45, NR), EcoGreen's largest client, reported strong 4Q FY12/06A results on 31 January 2007, with net profit up 215% at US\$48m and FY12/06A net profit was up by 17% to US\$226.5m, on the back of a surge in total turnover to US\$2.1b and the introduction

Chart 1: P/E bands



Source: SBI E2-Capital

of new high-margin products.

Symrise IPO debut. The share price of Symrise (SY1 GR, US\$19.75, NR) has increased 14.5% since its IPO on 11 Dec 2006 in Frankfurt. Symrise was the world's fourth largest flavor and fragrance companies in 2005 in terms of sales volume. With its stronger financial muscle, we expect Symrise to place more orders to EcoGreen.

Growth drivers. We believe future growth will be driven by the stronger-than-expected sales of food and beverage aroma chemical products, dihydromyrcenol market share gains, effective cost controls, production capacity expansion and gross margin expansion.

Valuation. Thanks to its high-end products and ASP growth, we expect it to achieve top line growth of about 33.0% in the next three years. To reflect the company's better-than-expected gross margin expansion and strong market demand, we revise our earnings forecast up 4.3% to HK\$120.0m for FY12/07F and 3.3% to HK\$159.8m for FY12/08F. Our new target price of HK\$3.12, represents 12x FY12/07F P/E.

Table 1 : Peers along the food chain

Company	Industry position [#]	Ticker	Currency	Price	Hist. P/E (x)	Fwd Yr 1 P/E (x)	Fwd Yr 2 P/E (x)	Hist. ROE (%)
EcoGreen	a	2341HK	HKD	2.38	14.2	12.1	9.1	18.6
Produits Chimiques Auxiliair	a	PCA FP	EUR	5.52	na	69.0	15.6	(5.8)
Rhodia SA	a	RHA FP	EUR	2.83	na	26.7	15.8	na
Dynaction SA	a	DYT FP	EUR	14.22	na	33.0	14.5	(15.2)
Lyondell Chemicals	a	LYO US	USD	30.41	9.3	8.3	8.8	21.8
International Flavors & Fragrances	b	IFF US	USD	48.45	20.1	19.9	18.3	24.6
Givaudan	b	GIVN VX	CHF	1122	17.3	18.0	18.0	16.9
T Hasegawa	b	4958 JP	JPY	1828	20.3	20.9	19.5	6.4
Takasgo	b	4914 JP	JPY	605	18.2	18.8	21.0	5.4
Huabao	b	336 HK	HKD	4.70	na	27.5	21.2	na
China Flavors & Fragrances	b	3318 HK	HKD	3.50	17.4	18.8	15.7	37.5
P&G	c	PG US	USD	64.16	22.8	21.2	18.5	21.8
Tingyi	c	322 HK	HKD	8.53	49.7	40.5	32.2	14.8
China Mengniu	c	2319 HK	HKD	23.10	63.3	51.3	39.6	21.3
Hengan	c	1044 HK	HKD	21.05	50.5	35.5	26.1	20.4
Average					27.6	28.1	19.6	14.5

[#] a: upstream producers; b: midstream producers (flavors & fragrances companies); c: downstream producers (consumer goods manufacturers)

Source: SBI E2-Capital & Bloomberg

Table 2 : Top Ten Flavor and Fragrance Companies

Company	Turnover (US\$m)	Estimated Market Share (%)
Givaudan	2,108.9	13.2
International Flavor and Fragrance	1,993.4	12.4
Firmenich	na	9.8
Symrise	1,360.2	8.5
ICI	963.4	6.0
Takasago	898.3	5.6
Sensient Technologies	516.4	3.2
T. Hasegawa	405.7	2.5
Mane SA	311.4	1.9
Danisco	279.4	1.7

Source: www.leffingwell.com

P & L (RMBm)	04A	05A	06F	07F	08F
Year to Dec					
Turnover	276.5	384.4	510.7	656.2	913.6
% chg	23.9	39.0	32.8	28.5	39.2
Gross profit	114.4	133.4	163.9	218.5	306.0
EBITDA	79.9	93.5	121.5	161.6	218.3
Depre./amort.	(7.2)	(8.6)	(13.8)	(19.0)	(24.0)
EBIT	72.7	84.9	107.7	142.6	194.3
Net int. income/(exp.)	(6.0)	(6.9)	(8.3)	(11.2)	(15.8)
Exceptionals	-	-	-	-	-
Associates	-	-	-	-	-
Jointly-controlled entit.	-	-	-	-	-
Pre-tax profit	66.6	78.0	99.4	131.4	178.5
Tax	(5.2)	(6.9)	(8.5)	(11.4)	(18.7)
Minority interests	-	-	-	-	-
Net profit	61.4	71.1	90.9	120.0	159.8
% chg	12.2	15.8	28.0	32.0	33.1
Dividends	(7.7)	(9.6)	(12.7)	(18.0)	(25.6)
Retained earnings	53.7	61.4	78.2	102.0	134.2
EPS (RMB) - Basic	0.156	0.167	0.197	0.260	0.347
EPS (RMB) - F.D.	0.148	0.154	0.197	0.260	0.347
DPS (RMB)	0.019	0.023	0.028	0.039	0.055
No. sh.s o/s (m) - W.A.	393.6	424.3	461.0	461.0	461.0
No. sh.s o/s (m) - Y.E.	415.0	461.0	461.0	461.0	461.0
No. sh.s o/s (m) - F.D.	415.0	461.0	461.0	461.0	461.0
Margins (%)					
Gross	41.4	34.7	32.1	33.3	33.5
EBITDA	28.9	24.3	23.8	24.6	23.9
EBIT	26.3	22.1	21.1	21.7	21.3
Pre-tax	24.1	20.3	19.5	20.0	19.5
Net	22.2	18.5	17.8	18.3	17.5
Balance Sheet (RMBm)	04A	05A	06F	07F	08F
Year to Dec					
Fixed assets	119.4	184.1	270.3	351.3	427.3
Intangible assets	22.0	27.7	27.8	32.6	35.8
Other LT assets	0.4	0.4	0.4	0.4	0.4
Cash	208.7	260.8	322.8	334.8	354.8
Accounts receivable	67.2	101.8	130.0	160.0	220.0
Other receivables	16.8	40.6	32.0	43.2	49.0
Inventories	19.5	33.3	54.0	70.0	95.0
Due from related co.s	-	-	-	-	-
Other current assets	31.8	0.3	3.1	3.1	3.1
Total assets	485.8	648.9	840.4	995.4	1,185.5
Accounts payable	(15.2)	(48.1)	(57.7)	(69.2)	(83.0)
Other payable	(19.0)	(30.6)	(55.5)	(74.1)	(90.2)
Tax payable	(1.2)	(2.4)	(3.0)	(4.0)	(6.5)
Due to related co.s	-	-	-	-	-
ST debts	(122.6)	(117.8)	(118.0)	(120.0)	(122.0)
Other current liab.	(1.9)	(0.3)	(0.6)	(0.6)	(0.6)
LT debts	(5.0)	(5.0)	(14.8)	(19.8)	(34.8)
Other LT liabilities	(0.1)	(0.0)	(0.2)	(0.2)	(0.2)
Total liabilities	(165.1)	(204.2)	(249.8)	(287.8)	(337.4)
Share capital	44.0	48.8	48.8	48.8	48.8
Reserves	276.5	396.0	541.7	658.5	799.2
Shareholders' funds	320.5	444.8	590.4	707.3	848.0
Minority interest	0.3	0.2	0.2	0.2	0.2
Total	320.8	445.0	590.7	707.5	848.2
Capital employed	448.4	567.8	723.5	847.3	1,005.0
Net (debt)/cash	81.1	138.0	190.0	195.0	198.0
Cash Flow (RMBm)	04A	05A	06F	07F	08F
Year to Dec					
EBIT	72.7	84.9	107.7	142.6	194.3
Depre./amort.	7.2	8.6	13.8	19.0	24.0
Net int. paid	(6.0)	(6.9)	(8.3)	(11.2)	(15.8)
Tax paid	(4.0)	(5.8)	(6.9)	(8.5)	(11.4)
Others	3.5	2.0	18.6	16.4	35.1
Gross cashflow	73.4	82.9	124.9	158.3	226.1
Chgs. in working cap.	(0.1)	(27.6)	(5.8)	(27.1)	(60.8)
Operating cashflow	73.3	55.3	119.1	131.2	165.3
Capex	(34.8)	(70.6)	(70.0)	(133.5)	(142.1)
Free cashflow	38.5	(15.3)	49.1	(2.3)	23.2
Dividends paid	-	(11.5)	(12.0)	(13.5)	(19.0)
Net distribution to MI	0.3	-	-	-	-
Investments	-	(0.3)	-	-	-
Disposals	-	-	-	-	-
New shares	168.2	61.8	-	-	-
Others	(58.7)	22.2	14.9	20.8	(1.2)
Net cashflow	148.3	56.8	52.0	5.0	3.0
Net (debt)/cash - Beg.	(67.1)	81.1	138.0	190.0	195.0
Net (debt)/cash - End.	81.1	138.0	190.0	195.0	198.0
Interim Results (RMBm)	04A	05A	06A		
Six months to Jun					
Turnover	127.8	171.0	253.5		
% chg	37.1	33.9	48.2		
Profit from operations	38.7	42.5	54.1		
Interest expenses	(4.1)	(3.4)	(3.3)		
Associates	-	-	-		
Jointly-controlled entit.	-	-	-		
Pre-tax profit	34.6	39.1	50.8		
Tax	(2.5)	(3.4)	(4.3)		
Minority interests	-	(0.0)	0.0		
Net profit	32.0	35.7	46.5		
% chg	62.7	11.4	30.3		
EPS (RMB\$) - Basic	0.086	0.094	0.100		
DPS (RMB\$)	-	0.008	0.008		
Shareholding Structure					
			Shares o/s (m)	%	
Mr. Yang Yirong			193.2	41.9	
Keywise			51.3	11.1	
Value Partners			36.8	8.0	
Senior management			15.7	3.4	
Public			164.0	35.6	
Total			461.0	100.0	
Background					
Ecogreen is engaged in the production, research and distribution fine chemical products of functional ingredients and intermediates for application in pharmaceutical industry, healthcare industry and personal care and personal care industry.					
Key Ratios	04A	05A	06F	07F	08F
Net gearing (%)	Cash	Cash	Cash	Cash	Cash
Net ROE (%)	30.2	18.6	17.6	18.5	20.5
EBIT ROCE (%)	20.8	16.7	16.7	18.2	21.0
Dividend payout (%)	12.5	13.6	14.0	15.0	16.0
Effective tax rate (%)	7.9	8.9	8.6	8.7	10.5
Net interest coverage (x)	12.1	12.3	13.0	12.7	12.3
A/R turnover (days)	88.8	96.6	92.9	89.0	87.9
A/P turnover (days)	34.2	69.9	60.7	57.7	49.9
Stock turnover (days)	43.9	48.4	56.8	58.4	57.1

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