

Growth momentum intact

China Chemicals

EcoGreen (2341 HK, HK\$2.96)

BUY (unchanged)

Target price: HK\$3.77 (+27.4%)

Strong order books. The company is working at full capacity to meet its orders for 1Q FY12/07F, due to strong global demand for fast moving consumer goods. To fulfill further orders it may have to rely on outsourcing.

Secure supply. Its new JV will secure around 8,000 tonnes of turpentine oil a year, half of the company's estimated annual consumption of 16,000 tonnes.

ASP up 3-5.0% in 1Q. Strong global demand allowed the company to lift its overall ASP 3-5.0% for the orders received in 1Q FY12/07F.

Key growth drivers

New production expansion. The company bought a site in Fujian province in 2006 to develop a new plant of around 100,000 sqm for aroma chemicals and intermediate products. Phase III expansion of its current plant in Xiamen, which covers 40,000 sqm, will start trial production in 1H FY12/08, with an annual processing volume of botanic essential oils of up to 20,000 tonnes.

M&A targets sought. The company is actively identifying potential M&A targets. We believe there are many suitable candidates in the highly fragmented market.

New high-margin products. More new products such as butter, fruit flavors and food additives will be launched over the next three years, as indicated in the following roadmap. We expect them to significantly boost EcoGreen's profitability, as products such as F&B aroma chemicals enjoy higher gross margins than its existing products.

Valuation. Given the stronger-than-expected demand, we expect EcoGreen to achieve top line growth of about 30.0% in each of the next three years. To reflect the company's better-than-expected gross margin expansion, we revise our earnings forecast up 3.8% to HK\$124.6m for FY12/07F and 1.7% to HK\$162.5m for FY12/08F. Our new six-month target price of HK\$3.77, represents 14x FY12/07F P/E.

FY12/06 results recap. FY12/06A net profit increased 34.0% YoY to RMB94.5m, above market expectations. Turnover reached RMB533.0m, up 39.0%. A final dividend of HK\$0.023 per share was proposed, representing a 15% payout ratio.

Dihydromyrcenol up 56%. Accounting for 49% of EcoGreen's turnover, aroma chemicals surged 43% to RMB261.2m. Dihydromyrcenol grew 56% YoY in FY12/06A and contributed RMB83.9m to EcoGreen. Being the upstream market leader, EcoGreen was able to increase its ASP 10% in 2006.

Gross margin. Excluding the trading division, which has a profit margin of 9.9%, the overall blended gross

Table 1: Financial summary

Year to Dec	Net profit RMBm	EPS RMB	EPS Δ %	P/E X	P/B x	EV/EBITDA x	Yield %	ROE %	ROCE %	N. Gearing %
05A	71.1	0.154	na	19.2	2.9	12.0	0.8	18.6	7.0	Cash
06A	95.4	0.206	33.5	14.4	2.4	9.1	1.0	19.5	7.7	Cash
07F	124.6	0.269	30.6	11.0	2.1	7.1	1.4	21.4	8.7	Cash
08F	162.5	0.350	30.4	8.4	1.7	5.4	1.9	22.8	9.6	Cash
09F	210.4	0.454	29.5	6.5	1.4	3.9	2.5	24.3	10.4	Cash

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margin in FY12/06A decreased to 38.1% (40.3% in 2005) as the turpentine price was high at RMB8,000 per tonne in 2005. We expect the gross margin to improve in 2007 as the turpentine price started declining in 2H FY12/06A and currently stands at around RMB6,500 per tonne.

Table 2: FY12/06A results

Six months To Jun	Turnover RMBm	Gross profit RMBm	Gross margin (%)	Pre-tax profit RMBm	Tax rate (%)	Net profit RMBm	EPS RMB	DPS RMB
FY06	533.0	170.0	31.9	104.4	8.6	95.4	0.207	0.109
FY05	384.4	133.4	34.7	78.0	8.9	71.1	0.168	0.069
YoY (%)	38.7	27.4		33.9		34.2	23.2	57.9

Source: Company data