

Impressive results

China Industrials

Nine Dragons (2689 HK, HK\$8.88)

Not Rated

Results summary. FY6/06 revenue jumped 63.8% to a record high of RMB7.90b. Gross profit rose by 144.7% to RMB1.86b, with gross margin increasing from 15.8% to 23.5%. Net profit grew by 340.4% to RMB1.40b and basic EPS climbed from RMB0.10 to RMB0.41. A final dividend per share of RMB2.30cents (equivalent to approximate HK\$2.26 cents) was proposed.

Increasing number of machines. The company will increase the number of machines in 2007/08 due to several reasons. The consumption of containerboard products continues to exceed domestic production and more international customers recognize the company because it does not just offer cheaper prices but also better quality products. Several competitors have closed down their factories due to incompetence business model, bad quality products and failure to meet strict regulation enforced by the government, leading to a shortage in supply.

Tapping into international market. This year, the company has successfully expanded its business to the worldwide market at a faster pace than before. The export rate has increased to 10% compared to 3% last year. The company wanted to expand its business to overseas because overseas market offers better selling price than the local market. So the company seeks to increase its exports to tap selected international market such as America, Europe and Middle East.

Outperformed the market. Nine Dragons is the largest producer in China, so it is able to enjoy better economies of scale and greater bargaining power. It uses imported machinery of advanced technology whereas other manufacturers use local made machinery of inferior technology. The company has well-established brand name and reputation. Other competitors can only compete at prices but have limited room to go further down due to cost pressure. Note that the company is able to price its products at premium.

Future plans and strategies. The company plans to further expand its capacity by speeding up the CAPEX plans and increase annual production capacity by June 2007. It will increase the usage of recovered paper in production in the future. Besides that, the company considers to extend its presence in inland regions such as the Central-Western and Northern China as the manufacturing industries in these regions become more active. The company wants to focus on developing upstream and wood pulp business and it will implement stringent cost control though internal R&D. The management expects 4 new paper machines will start production before the end of 2008.