

Acquisition of second forest

Asia Resources

China ASEAN Res (8186 HK, HK\$0.43) STRONG BUY (unchanged)

Target price: HK\$2.09 (+386.0%)

Option to acquire three forests in Cambodia. Under the agreement to acquire the first forest, vendors Zhang Zhenzhong, Pen Sophal and Zhang Jie have granted China ASEAN Resources an option to acquire from them all the issued capital in the companies, which hold land use rights and exploitation rights to three other forests in Cambodia. Under the deal (valid from October 2007 to October 2010), the company shall pay Mr. Zhang Zhenzhong a premium of HK\$30.0m in cash if the option is exercised. After that no more call option premiums will be payable by the group to Mr. Zhang.

Proposed acquisition. The company said that it had partially exercised the option and entered into a non-legally binding MOU on 14 November to acquire Agri-Industrial Crop, an investment company incorporated in Cambodia, which holds land use rights to a 10,000 hectare forest adjacent to its own forest in Kratie province, Cambodia. Agri-Industrial Crop will obtain from the Cambodian government the right to explore its forest for 70 years after paying all relevant premiums and government taxes, duties and expenses. A refundable deposit of HK\$15.0m shall be payable by the group to the vendors within 10 business days from the date of the MOU. Further details are yet to be disclosed.

The target. The forest is adjacent to the group's forest in Kratie province, Cambodia and covers about 10,000.0 hectares, with similar vegetation as the group's forest and timber reserves of about 3.0m m³.

Bridging the gap. We originally expected the company's earnings to fall 77.8% YoY in FY12/12F because of its shrinking timber resources and still immature latex operations. Between FY12/12F and FY12/13F, we expected earnings growth to be sluggish but to pick up in FY12/14F when latex production gets in full swing. The latest move should help the company to bridge the earnings gap between FY12/12F and FY12/14F. Due to the proximity of the two forests, the deal will benefit the company in terms of economies of scale, log transport and latex production potential. It will also strengthen its position in Cambodia's natural resources industry.

Two-fold valuation boost. BMI Appraisals valued the group's forest at US\$360.0m. We put it at US\$703.4m. Since the company's forest is similar to the target forest, China ASEAN Resources' intrinsic value should double upon the completion of the acquisition. Based on a simple P/E multiple approach, the company is attractively valued at P/E of 2.9x for FY12/08F, representing an substantial discount to the peer group's average one-year forward P/E of 24.3x. STRONG BUY call reiterated.

Table 1: Financial summary

Year to	Net profit	EPS	EPS	P/E	P/B	EV/EBITDA	Yield	ROE	ROCE	N. Gearing
Mar	HK\$m	HK\$	Δ %	x	x	x	%	%	%	%
05A	(2.2)	(0.003)	na	na	3.0	283.2	na	(1.8)	na	Cash
06A	(29.4)	(0.035)	na	na	3.8	na	na	(27.3)	na	Cash
07F	(6.2)	(0.005)	na	na	3.0	na	na	(3.7)	na	Cash
08F	249.4	0.146	na	2.9	1.5	2.2	na	67.6	43.2	Cash
09F	341.6	0.200	36.9	2.1	0.9	1.6	na	50.9	37.2	Cash

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Table 2: Peer group comparisons

Ticker	Year End	Currency	Price	Market Cap (US\$m)	P/E (x)	
					1-yr forward	2-yr forward
TAH MK	Dec	MYR	6.8	431.1	11.1	9.2
JT MK	Apr	MYR	3.3	279.1	13.1	10.8
WTKH MK	Dec	MYR	2.2	291.1	11.5	9.6
EVF MK	Dec	MYR	1.7	248.5	7.8	6.0
TWF-U CN	Dec	CAD	14.1	1,140.5	12.4	8.9
TRE CN	Dec	CAD	22.0	4,160.4	21.5	17.4
WY US	Dec	USD	73.1	15,431.8	45.1	31.3
IP US	Dec	USD	34.5	14,766.5	15.8	12.5
RYN US	Dec	USD	47.2	3,686.0	20.5	22.4
PCL US	Dec	USD	44.0	7,583.6	32.3	29.9
FBU NZ	Jun	NZD	11.6	4,422.6	12.4	10.9
GNS AU	Jun	AUD	3.7	1,333.3	16.1	15.1
UPM1V FH	Dec	EUR	14.6	11,328.4	15.1	14.2
3938 HK	Jun	HKD	2.4	1,296.0	16.7	15.1
<i>Average</i>					24.3	19.6

Source: Bloomberg

Disclosure of interests: SBI E2-Capital Securities Ltd. acted as the Sole Bookrunner and Joint Placing Agent for China ASEAN Resources (233m Top-up shares and 167m new shares at HK\$0.60) on Jul, 2007.