

High growth on track

China Agriculture

Century Sunshine (8276 HK, HK\$4.71)

BUY (unchanged)

Target price: HK\$6.85 (+45%)

Interim results above expectations. The company reported a 136% jump in 1H FY12/06 net profit to RMB48.4m, above our forecast of RMB40m. Turnover increased 111% to RMB132.9m. The robust results were boosted by higher than expected net margin of 37.7% in 2Q06, compared with 34.2% in 1Q06 and 29.7% in 2Q05. The improvement in margins was due to an 8% decline in the in selling expenses and much smaller 55% increase in administrative expenses for period. An interim dividend of HK\$0.02 was declared (cf. RMB0.015 a year ago), representing a payout of 17.1%.

Robust sales. Thanks to strong market demand, sales volume surged 97% to 75,000 tonnes while price was raised for two of the products in May 06. The Nanchang Plant in Jiangxi commenced operation in May 2005 and added capacity of 100,000tpa to a total of 155,000tpa. Phase one of Yunxiao Plant in Fujian is expected to be completed by end-2006 and add another 200,000tpa by early 2007.

New products. The development of two new products – organic fertilizer for wind-protection trees and pesticide fertilizer is expected to be completed by end-2007.

Strong financials. The company is debt free and had net cash of HK\$215m as at end-Jun 06, equivalent to HK\$0.54 per share. Operating cash inflow amounted to RMB62.3m during the period.

Valuation and forecasts. We keep our forecasts unchanged but we have raised our target price to HK\$6.85 based on 10x FY12/08 P/E (from HK\$5.81) as both contribution from both two phases of Yunxiao Plant will start to kick in. Despite trading at a relatively high FY12/06 P/E, the visible high growth and scaleable business model do justify a premium valuation, not to mention that the PEG (FY12/06 P/E to 3-year EPS CAGR) only stands at 0.4x.

Table 1: Turnover by segment

Year to Dec (RMBm)	1Q05	2Q05	1H05	1Q06	2Q06	1H06
Microbial compound fertilizer	10.6	10.0	20.7	13.4	21.3	34.7
Organic tea fertilizer	8.6	4.6	13.2	9.3	5.4	14.7
Eucalypt tree organic fertilizer	-	5.6	5.6	17.0	24.0	41.1
Premium organic fertilizer	2.4	6.4	8.8	5.7	12.9	18.6
Organic compound fertilizer	4.0	7.7	11.7	3.8	14.0	17.8
Bio-pesticides	0.1	3.0	3.0	0.5	5.5	6.0
	25.7	37.2	62.9	49.8	83.1	132.9

Source: SBI E2-Capital and company data

Table 2: 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 %
04A	35.5	0.117	30.9	43.0	14.4	40.2	0.6	48.9	44.8	Cash
05A	71.4	0.217	86.6	22.5	6.2	16.5	1.1	33.7	34.0	Cash
06F	107.0	0.250	15.1	19.4	5.0	13.4	1.6	30.6	32.9	Cash
07F	200.2	0.468	87.1	10.4	3.7	7.0	3.1	43.7	48.9	Cash
08F	301.5	0.705	50.6	6.9	2.6	4.3	4.6	47.6	53.2	Cash

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Table 3: Quarterly results

Year to Dec (RMBm)	1Q04	2Q04	1H04	3Q04	4Q04	1Q05	2Q05	1H05	3Q05	4Q05	1Q06	2Q06	1H06
Turnover	17.6	17.0	34.6	28.2	31.2	25.7	37.2	62.9	54.9	73.1	49.8	83.1	132.9
Cost of sales	(8.0)	(7.4)	(15.4)	(12.0)	(14.0)	(10.7)	(18.8)	(29.5)	(26.7)	(37.2)	(24.9)	(42.2)	(67.1)
Gross Profit	9.6	9.6	19.2	16.2	17.2	15.1	18.4	33.5	28.2	35.9	24.9	40.9	65.8
Other revenue	0.0	0.0	0.0	0.1	0.2	0.3	0.1	0.4	0.1	0.0	0.7	1.3	2.1
Distribution and selling expenses	(0.6)	(0.7)	(1.3)	(1.1)	(1.0)	(0.9)	(1.9)	(2.8)	(2.2)	(1.7)	(1.1)	(1.5)	(2.6)
General and admin. expenses	(1.2)	(1.2)	(2.4)	(1.8)	(3.7)	(3.2)	(3.5)	(6.7)	(4.3)	(2.0)	(5.1)	(5.9)	(10.9)
Research and development costs	(1.1)	(3.4)	(4.5)	(1.5)	(0.2)	(0.0)	(0.3)	(0.3)	(0.7)	0.0	0.0	0.0	0.0
Operating profit	6.7	4.3	11.0	11.9	12.6	11.2	12.9	24.1	21.1	32.3	19.5	35.0	54.4
Finance costs	(0.1)	(0.0)	(0.1)	(0.0)	(0.0)	(0.1)	(0.4)	(0.5)	(0.4)	(0.1)	(0.2)	(0.0)	(0.2)
Profit before taxation	6.6	4.3	10.9	11.9	12.6	11.1	12.5	23.5	20.6	32.2	19.2	34.9	54.2
Taxation	(0.0)	0.0	(0.0)	0.0	0.0	(1.6)	(1.4)	(3.1)	(0.9)	(1.0)	(2.2)	(3.6)	(5.8)
Profit after tax	6.6	4.3	10.9	11.9	12.6	9.4	11.1	20.5	19.7	31.2	17.0	31.3	48.4
Minority interest	(0.0)	(0.0)	(0.0)	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit	6.6	4.3	10.9	11.9	12.6	9.4	11.1	20.5	19.7	31.2	17.0	31.3	48.4
Dividends								(5.1)					(8.3)
DPS (HK\$)								0.015					0.02
<i>Gross margin</i>	55.5	57.5	55.3	58.6	49.5	53.2	51.3	55.5	57.5	49.1	49.9	49.3	49.5
<i>Pre-tax margin</i>	31.5	42.3	40.5	43.0	33.5	37.4	37.5	31.5	42.3	44.0	38.6	42.0	40.8
<i>Net margin</i>	31.5	42.3	40.5	36.6	29.7	32.5	35.9	31.5	42.3	42.7	34.2	37.7	36.4

Source: SBI E2-Capital and company data

Table 4: Earnings model

Year to Dec (RMBm)	02A	03A	04A	05A	06F	07F	08F
Turnover							
Microbial compound fertilizers	18.1	23.6	43.7	54.0	76.1	149.1	225.0
Organic tea fertilizers	14.2	17.4	24.3	27.3	41.2	80.7	121.8
Organic compound fertilizers	9.2	12.3	21.4	22.6	30.0	62.9	95.0
Premium organic fertilizers	1.1	2.2	4.4	36.7	59.2	122.6	185.0
Eucalypt tree organic fertilizers	0.0	0.0	0.0	44.9	66.0	130.8	199.3
Bio-pesticides	0.0	0.0	0.0	5.5	28.5	33.0	39.0
	42.6	55.5	93.9	191.0	301.0	579.0	865.0
<i>% change</i>		30.1	69.3	103.4	57.6	92.4	49.4
Cost of sales	(19.2)	(24.4)	(41.3)	(93.4)	(148.8)	(295.9)	(447.2)
Gross Profit	23.5	31.1	52.6	97.6	152.2	283.0	417.8
Other revenue	0.0	0.0	0.3	0.5	3.7	3.6	5.6
Distribution and selling expenses	(3.2)	(3.1)	(3.4)	(6.7)	(9.4)	(17.8)	(24.9)
General and administrative expenses	(2.7)	(4.3)	(7.9)	(13.0)	(18.3)	(34.7)	(48.6)
Research and development costs	(4.1)	(2.1)	(6.1)	(1.0)	(6.0)	(6.6)	(7.3)
Operating profit	13.4	21.5	35.6	77.4	122.2	227.5	342.6
Finance costs	(0.2)	(0.3)	(0.1)	(1.0)	(0.6)	0.0	0.0
Profit before tax	13.2	21.2	35.4	76.4	121.6	227.5	342.6
Taxation	(0.0)	(0.0)	0.0	(5.0)	(14.6)	(27.3)	(41.1)
Profit after tax	13.2	21.2	35.4	71.4	107.0	200.2	301.5
Minority interest	0.2	0.2	0.0	0.0	0.0	0.0	0.0
Net profit	13.4	21.4	35.5	71.4	107.0	200.2	301.5
<i>% change</i>		59.2	66.0	101.3	50.0	87.1	50.6
Dividends	-	-	(10.2)	(19.6)	(31.1)	(60.1)	(90.5)

Source: SBI E2-Capital

Disclosure of interests: SBI E2-Capital Securities Ltd. acted as one of the two placing agents for the Century Sunshine top-up placement (56.5m new shares at HK\$2.2 each) on Dec 16, 2005.