Qian Hu

Reuters: QIAN.SI
Bloomberg: QIAN SP

Sector: Commerce

Price S$0.805

recommendation :
Maintain **Market Perform**

Y/E 31-Dec	2001A	2002A	2003F	2004F	2005F
Net Profit (S$m)	3.6	6.5	7.9	9.5	10.2
EPS (cts)	3.9	6.6	7.5	8.9	9.5
EPS Growth (%)	*-22*	*+70*	*+13*	*+18*	*+8*
Consensus EPS	-	-	7.5	8.5	-
PER (x) @ S$0.805	20.6	12.1	10.7	9.1	8.4
NTA (S$)	0.21	0.27	0.32	0.39	0.47

Performance (%)	1mth	3mth	12mth		
Absolute	+10	+13	-	Market Capitalisation :	S$83m
Relative against STI	+7	+19	-	Issued shares :	103m
				30-day avg daily vol ('000) :	477

FY02 results were marginally above consensus

Qian Hu's full year net profit of $6.5m was 6.5% above consensus, but in line with our forecast. Outlook for Qian Hu remains good and management expects to maintain a healthy growth in turnover and overall profitability in FY03. Overseas operations will be growth drivers. The latest acquisition of a 65% stake in a Malaysian Dragon Fish breeder should be bottomline enhancing and the profit guarantees are projected to boost Qian Hu's FY03-FY04 net profit by 8.3% and 10.3%, respectively. We are raising our FY03 profit forecast by 2.6% to $7.9m and FY04 by 14.5% to $9.5m, giving earnings CAGR of 12.6% for FY03-FY05. At $0.805, Qian Hu's FY03-FY04 PERs of 10.7x and 9.1x are near its historical PER average of 10x. Its premium valuation over its closest Malaysian peer, Xian Leng has reflected Qian Hu's outperformance and its broader earnings profile. At PEG ratio of 0.85x, we continue to rate Qian Hu as a MARKET PERFORM.

FY02 results were marginally above consensus. Full year net profit of $6.5m was 6.5% above consensus, but in line with our forecast. The stellar 84% YoY increase in net profit to S$6.5m for the year ended 31 Dec 2002 was brought about by a 52% turnover growth to S$62.7m and a 2.4%-point improvement in EBITDA margin to 16.3%. Continued sales growth and the improved operational efficiency, especially of its overseas divisions, have contributed to the strong FY02 performance.

Accessories were the largest contributor. Accessories contributed to 51% of total turnover (FY01: 40%) and 73% of the operating profit before taxation (FY01: 49%). The 172.8% increase in the division's pre-tax profit was mainly due to increase in sales and profit margin, particularly of its overseas operations. Overseas operations (including Wan Jiang, which became a subsidiary in the 4QFY02) contributed approximately 65% of the increase in accessories turnover. Improved efficiency has also raised the division's profit margin by 0.3%-point to 16%.

The ornamental fish division posted 27.6% turnover growth and 16.9% operating profit before taxation growth. This was due to the growing numbers of local fish retail outlets and visitors patronising in-house retail outlets. Export sales to China also showed positive growth. The subsidiary in Thailand (dealing with fish) and the newly set-up fish division in Malaysia, which commenced operations in Jan 2002, have also contributed positively to the turnover of ornamental fishes in FY02. With the import deregulation in Taiwan,

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sales of Dragon Fish to Taiwan accounted for approximately 23% of the increase in ornamental fish sales.

Plastic business suffered from market competition, high operating costs and also dragged by losses incurred by a subsidiary in China. The division posted a 51.3% decline in profit to S$0.3m.

Geographically, all market regions showed double-digit growth in turnover. Singapore accounted for 55% of total turnover and 53% of total operating profit before taxation. Turnover from Singapore grew 39% YoY as a result of improved sales of fish and aquarium accessories to local retailers and sales generated from in-house retail outlets. The second largest turnover contributor was Asia, which also posted the strongest YoY turnover growth of 93% to S$22m or 35.2% to total turnover.

A first and final dividend of 6% gross per share and a 6% special dividend have been proposed and if approved, will be paid on 10 Apr 2003. This translates into a total gross yield of 1.5%.

Outlook remains good. Management guidance is for the company to maintain a healthy growth in turnover and overall profitability in FY03 with its overseas operations being the growth drivers. The regional distribution network, set up in the last two years, should see improving operational efficiency in the coming years. However, management's view is that the overseas markets are still young and it will take another 5-10 years to reach optimal efficiency and to achieve sufficient market breadth. Marketing plans will be set up to boost the sales of accessories in Thailand and China. In Taiwan, contribution from the pet food business is not significant, but there are plans to capitalise on its growing contacts and business relationships to promote the sales of ornamental fishes and to take advantage of the import deregulation of ornamental fishes in Taiwan. In the domestic market, the focus will remain on expanding and penetrating distribution network to reach more local retailers and supermarkets.

Latest acquisition in Malaysia. Qian Hu has also announced that it has signed a definitive agreement to acquire a 65% stake in Kim Kang, a Dragon Fish breeder in Batu Pahat, Malaysia for a total purchase consideration of S$7.7m. The pricing includes goodwill of about $3.2m in consideration of Kim Kang's more than ten years business track record in breeding and trading Arowanas. Of the consideration, 50% will be in cash funded by its cash reserves of $7.8m and the remaining 50% will be via the issuance of an estimated 4m new Qian Hu shares at $0.96 a piece. This issue price is at a 19.3% premium to Qian Hu's last done price. The acquisition is subject to the completion of all legal and financial due diligence on Kim Kang as well as relevant regulatory and government approvals.

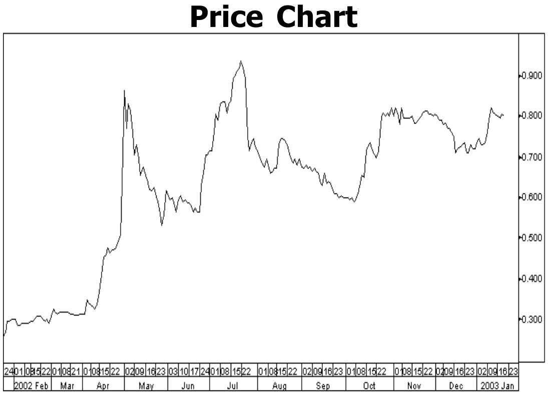
Pricing of the acquisition. The total consideration of $7.7m is 8.7x of the FY03 pre-tax profit (PBT) of RM1.95m (based on 65% stake) guaranteed by the vendors and 6.5x of FY04 guarantee profit of RM2.6m. This is comparable to Qian Hu's current valuation of 8.2x of our projected FY03 PBT prior to the acquisition. The P/NTA ratio of 1.36x based on Kim Kang's FY02 NTA of RM19m is lower than Qian Hu's prevailing ratio of 2.9x. The profit guarantees of RM3m for FY03 and RM4m for FY04 from Kim Kang is projected to boost Qian Hu's FY03-FY04 net profit by $0.6m (or +8.3%) and $0.9m (or 10.3%), respectively.

FY03-FY04 earnings upgraded by 3% and 14%. We are revising upward our FY03 profit forecast by 2.6% to $7.9m and our FY04 forecast by 14.5% to $9.5m to reflect this latest acquisition and we have assumed that the acquisition of Kim Kang will be completed in mid-FY03. FY05 net profit is projected at $10.2m, giving earnings CAGR of 12.6% for FY03-FY05.

Valuation. At $0.805, Qian Hu is trading at FY03-FY05 PERs of 10.7x, 9.1x and 8.4x, near its historical PER average of 10x. Qian Hu's FY03 PER of 10.7x and P/NTA of 2.4x are at premiums to its closest Malaysian peer, Xian Leng (at 9.9x and 1.4x, respectively). We believe this premium is reflective of Qian Hu's outperformance and its broader earnings profile. At PEG ratio of 0.85x, we continue to rate Qian Hu as a **MARKET PERFORM**.

Technical: Prefer to accumulate near 74 cents.

Price Chart



Qian Hu vs STI