Qian Hu full year FY02 net earnings rise 84% ro $6.5mn inline with expectations

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….expect more modest growth going forward of between 15-25%.

Synopsis : Better FY02 earnings already in stock price as Qian Hu was one of the better performing stocks in FY2002. There is still more upside to about $0.96 times with a target forward PER of 12 times FY03 earnings.

Qian Hu Corporation Ltd $ 0.81 Short term: BUY Long term: ACCUMULATE

FY02 results review

Mainboard listed, Qian Hu came inline with market expectations to deliver a full year net growth of 84% on the back of 52% increase in turnover from $41.2m in FY2001 to $62.7m in FY2002. However, sales turnover in the fourth quarter has been less than impressive with a negative sequential growth of –0.3%, a break away from the strong growth of 22% and 14.2% in the second and third quarter. To recap, Qian Hu has experienced a remarkable growth from the fish division in FY2002 which could be attributed to the addition of Taiwan as the new export market for dragon fish, coupled with the proliferation of retail outlets in various neighbourhoods and the commencement of in-house retail outlet in FY2001.

Nevertheless, this growth seems to have slowed down as indicated in the decline in sales revenue from the fish division, which dipped 10.2% sequentially in the last quarter. Adding to that, fish margins have also suffered a dip to single digit of 7% from 14.4% in the second quarter. But this is to be expected as the business matures.

Both accessories and plastics divisions registered flattish turnover with increases of 5.6% and 3.9% respectively for the quarter. Nevertheless, margins for the accessories division was maintained at 24.2%. Going forward, we expect this division to continue to contribute positively to the top and bottomline growth given that all its overseas subsidiaries are now fully operational. Plastic division, which is currently supplying 30% internally to its fish division and 70% externally, has seen a contraction in its contribution to turnover from 15% to 11%. Management has indicated the intention to dispose of this non-core business to focus on fish and fish related business in the long run.

Acquisition of Kim Kang Aquaculture Sdn Bhd

Also unveiled in the briefing was the agreement to acquire a 65% stake in a Malaysian fish breeding business, Kim Kang Aquaculture Sdn Bhd at a purchase price of approximately $7.68m. This will comprise a payment of S$5.6mn based on the NTA of Kim Kang and an additional sum of $2.1mn over its NTA only if Kim Kang can achieve earnings in 2003 is between M$1.9-3.0mn. This acquisition will be 50% funded from its cash reserves and the remaining half in the form of new shares to be allotted and issued to the Vendors at the price of 96 Singapore cents each.

Upon completion, the acquisition will enhance the group's ability to meet the increasing demand for Arowanas and allow the group to leverage on its established regional distribution network to optimise sales in these regional markets. Prior to this, sales of dragon fish accounted for approximately 10% of fish turnover with the other species accounting for less than 5%. Though this acquisition implies a further dilution of shareholders' interests, we are of the view that this newly added operation will drive the growth in sales of dragon fish, which could also suggest an expansion in margin given that dragon fish can command a higher selling price than the other fish species. Contribution from this acquisition to the bottomline in FY2003 is worked out to be approximately S$0.89m, which is equivalent to 13.5% of net earnings in FY2002. This gives an approximate acquisition PER of 11 times which is probably earnings neutral to slightly positive for Qian Hu.

Investment recommendation – still looking attractive maintain Buy

Meanwhile, the stock price has more than priced in the growth for this year, from a low of 33.5 cents in the beginning of FY2002. In the near term, it is unlikely that we will see a replication in performance of that in FY2002, which benefited from the low base effect. Notwithstanding this, we continue to like the business model which has proven to be fairly resilient during this difficult economic climate. We are looking at a more moderate growth in the range of 20% to 30% going ahead. This will translate into prospective PERs of about 10 times. Bearing in mind the excellent performance and its small market cap, we believe that Qian Hu should trade at a discount to the market PER and have therefore put a fair price at $0.96. We are therefore maintaining our BUY and Accumulate recommendations.