

# Your Money

Never mind the Macau fever, writes Andy Mantel, as he selects a rapidly expanding food processor and a manufacturer of telecoms gear for his China portfolio

## Looking for growth in agriculture

It is tempting to participate in the gambling frenzy that is currently taking place in the Hong Kong stock market. Almost every day in the past few weeks relatively small-cap companies have declared they are taking part in a Macau property or casino project in one form or another and subsequently their share prices have rocketed.

After yet another visit to Macau recently we are positive on its long-term potential. However, it is clear that much of the current fever grasping investors is a lot of hot air.

We are largely ignoring the Macau noise and instead focus on two companies with high-growth strategies in China and overseas but in different sectors.

China Green is a debt-free vegetable and fruit processor that stands out as one of the few growth companies in the private sector that has paid a final dividend to its investors. ZTE provides communications equipment in 50 countries and is set to list H shares in Hong Kong next month.

China Green, based in Fujian province, produces and supplies fresh, processed and pickled vegetables and fruits, primarily for Japanese customers. The diversified product range includes corn, peas, potatoes, cucumbers, carrots, pumpkin and lettuce.

The company operates four processing factories and leases 27 fruit and vegetable cultivation bases, a few of which are located in Zhejiang province. The most recent base was set up in Hubei province and the company also intends to grow asparagus, basil and mangoes in Thailand soon. It is exploring Jiangxi province too. The new bases fit into part of the company's strategy to complement domestic

shortages of vegetables and fruit to Japan during seasonal periods.

China Green is about a seventh the size of Chaoda Modern. Sales in the last fiscal year, to April 2004, were 375 million yuan and profit 146 million yuan, up 45 per cent and 25 per cent year on year, respectively. Fresh produce accounted for about 67 per cent of sales. Exports, mainly to Japan, accounted for about 67 per cent of sales. Products are also sent to Britain and the Philippines, while 33 per cent of sales are in China.

In the most recent year sales on the mainland grew 176 per cent from the year before, when the contribution to total turnover was only 18 per cent. The increase also had to do with lower exports during the Sars outbreak.

China Green listed on January and the stock appreciated more than 50 per cent on its first day. The retail portion of the placement was more than 1,500 times oversubscribed, a Hong Kong market record. The fund I manage, The China Mantou Fund, participated in the initial offering and has since acquired more shares.

China Green has been able to maintain stellar gross-profit margins despite the problems of other Chinese private firms in the past couple of years. Management says its high gross margins are due to the company's vertical integration, the mark-up on its export products and the low cost structure - farmhands earn US\$1.50 a day.

The company plans to maintain its high-growth strategy. With a market cap of about US\$120 million, China Green is trading at less than six times this year's earnings and has a return on equity of about 25 per cent.

### MANTEL'S CHOICE

	Price on recommendation	Friday price
China Resources	\$10.40	\$11.15
Qiao Xing Universal	US\$15.00	\$9.25
Telephone (Nasdaq short)	Feb 29	
Kwang Sung Electronics	\$1.76	\$1.02
Weichai Power	\$10.50	\$17.95
	Mar 28	
Jilin Chemical	\$1.68	\$2.65
GES	\$0.665	\$0.705
	May 28	
CNOOC	\$3.325	\$4.30
Zhenhai Refining	\$6.60	\$8.05
	Jul 16	
CIMC	\$11.88	\$15.00
Shanghai Petrochemical	\$2.75	\$2.925
	Aug 13	
Nanjing Panda	\$1.49	\$1.57
Guangdong Kelon	\$2.875	\$2.025
	Sep 24	
Huaneng Power	\$6.20	\$6.15
Guangdong Power	\$4.92	\$4.25
	Oct 22	
Tianjin Capital	\$2.275	\$2.75
Luoyang Glass	\$0.90	\$0.96
	Nov 26	
China Green	\$1.55	\$1.55
ZTE corp	-	-



"It is clear much of the current fever grasping investors is a lot of hot air"

billion yuan and profits 100 per cent to 724 million yuan.

After its initial listing in 1997, the company also floated shares in 2001. Since then the company has been seeking to list H shares in Hong Kong to facilitate the funding of its overseas expansion plans. The proposed Hong Kong listing met strong shareholder resistance because of the share dilution that would result by raising additional shares at significantly lower prices. An attempt to list the stock in Hong Kong was aborted last year.

ZTE also sells products in more than 50 countries. Overseas sales last year accounted for about 11.5 per cent of total turnover to about 1.98 billion yuan. In the first half of this year sales increased an additional 13.4 per cent from the year before, including a large contract to supply Brazil with handsets.

The company is set to list in Hong Kong on December 9. The shares are being sold at a valuation of about 13 times this year's earnings compared to about 19 times for its A shares. After the listing about 15 per cent of the floatation will be H shares, 32 per cent domestic A shares and 45 per cent will be held by the parent company.

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ZTE Corp is a leading provider of communications equipment in China. The company will design, build and install almost any type of advanced gear.

Product lines include wireless communications equipment, wireline switch and access equipment, optical and data equipment, handsets and software systems. It also provides services to run and maintain the equipment.

Domestic customers include telecom firms such as China Telecom, China Netcom, China Unicom and China Mobile. Last year ZTE was the largest domestic supplier of CDMA systems as well as PHS-based wireless local access systems and handsets in the wireless telecoms market according to contract value.

It was one of the top three providers of optical networking,

broadband access, circuit-switch products and telecommunications software systems.

ZTE is the largest listed telecom equipment company in China's A-share market in terms of market capitalisation (22 billion yuan), revenue and net profits. Turnover in 2003 was about 17 billion yuan, with profits of one billion yuan. In the first half of this year, turnover jumped about 45 per cent to 10.2

## UPDATE

Your Money welcomes your ideas and contributions. Just e-mail us at [money@scmp.com](mailto:money@scmp.com)

### HANG SENG INDEX



A huge surge of foreign capital into the Hong Kong exchange is likely to maintain high liquidity levels and ensure the stock market remains in positive territory this week, dealers say.

Continuing fears of oil price rises may dampen sentiment and jitters are expected at the expiry of the November contract tomorrow.

The Hang Seng Index gained 107.35 points, or 0.7 per cent, over the past five trading days to end the week at 13,895.03. *AFP*

### DOW JONES INDUSTRIALS



Dollar weakness will move to the backburner this week as traders focus on economic data that will give clues to the health of the economy as the Christmas shopping season gets underway.

For the week the Dow Jones Industrials rose 0.62 per cent to 10,522.23, and Nasdaq rose 1.51 per cent to 2,101.97. The S&P 500 rose 1 per cent to 1,182.65.

Thursday will see the release of important monthly retail figures, followed by the US payrolls report on Friday. *AFP*

## NEW PRODUCTS

Pioneer Investments is launching three new funds designed to appeal to different needs.

The Global High Yield bond fund will invest in a range of US corporate, convertible and emerging-market debt. About 80 per cent of the fund will be invested in high-yield debt.

"The global sub-investment-grade debt market is one of the world's fastest growing asset classes and this growth trend is set to continue," a spokesman said.

The Euro Strategic Bond Fund is a fixed-income product designed to prosper in bull and bear markets. The fund can use both aggressive and defensive strategies, buying emerging-market debt or short-term government debt, for example. Pioneer says the risk profile of the fund will be adjusted to suit the interest-rate cycle. The aim of the fund is to provide consistent returns regardless of market conditions.

The European Quant Equity will use a strategy that selects stock on fundamentals using a unique in-house evaluation methodology. "This is one of the few quant-driven funds on offer to the retail investors in Hong Kong," Pioneer spokesman Edmund Lacin said.

"This approach allows us an innovative way to identify undervalued companies with good growth potential."

## EXCHANGE RATES

HK\$	Bid	Ask
E	14.7215	14.7240
SFr	6.8239	6.8254
*Y	7.5776	7.5786
S\$	4.7501	4.7523
A\$	6.1454	6.1480
C\$	6.6005	6.6027
Baht	0.1971	0.1972
NZ\$	5.5764	5.5818
*Won	0.74245	0.74245
M\$	2.0454	2.0454
NT\$	0.2416	0.2417
Euro	10.3343	10.3373
Peso	0.1382	0.1386
Yuan	0.9391	0.9393

Rates yesterday \*per 100 units Source: Bloomberg

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### Exhibition

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### MEET THE MANAGER

CHRIS OLIVER

Expect to hear a lot more talk about free cash flow from stock analysts in the next few years. The term refers to a simple accounting principle which says a lot about the dividend payout shareholders can expect, according to Fidelity Investments fund manager Lee Kong-chung.

Usually, investors look towards earnings as an indicator of a company's financial health. It is commonly thought the greater the company earnings, the more they will hand over in the form of half-yearly dividend cheques.

But that is a serious mistake, says Mr Lee. For one thing, earnings do not measure the amount of money a company will have to pitchfork back into the business in the form of capital reinvestment.

A computer chip company, for example, will have to spend a lot more to keep up with the latest product and manufacturing advancements than, say, a bank. In theory earnings for each company could be the same, but the computer company is likely to have a much smaller free cash flow after deductions for new capital investment. The bottom line: the bank has more cash.

"Free cash flow is a lot more important in driving the value of the business or the company," Mr Lee says. "If the company has to reinvest heavily, the earnings do not translate into free cash flows."

Low bank interest rates have increased demand for high dividend-yielding stocks. But investors are also paying attention because of an admirable track record.

When performance is averaged over bull and bear markets, Asian

**Lee Kong-shung believes Asian companies have some of the best prospects for increasing dividend payouts.**  
Photo: Martin Chan

## Free cash flow to be targeted for payouts

companies with the highest dividend yields have consistently outperformed companies with low dividend yields, according to Mr Lee. High dividend-yielding stocks are also less volatile, partly because shareholders are less likely to dump stock when it provides a steady income stream.

Fidelity is moving to fill the growing investor appetite for dividend-yielding stocks with a purpose-designed fund that focuses solely on Asian companies. It says the Asia Pacific Growth and Income Fund is designed to fill a gap in the market between guaranteed funds and volatile mutual funds.

"There are very few products positioned in the middle of the risk/return profile spectrum," says Mr Lee, who will manage the new fund.

The fund will focus on high-yield financial equities, which are expected to account for 37 per cent of holdings. Consumer discretionary stocks and industrials will each account for an additional 14 per cent of holdings. Hong Kong will be its single largest market with 26.6 per cent of total net assets, followed by Korea with 15.4 per cent and Taiwan with 13.3 per cent.

Mr Lee believes Asian companies have some of the best prospects for boosting dividend payouts. They have cut debt-to-equity ratios from 62.5 per cent in 1995 to less than 20 per cent on this year's estimates, meaning less cash will be used to service or retire debt. The free cash flow-to-sales ratio is trading at close to a 14-year high, and corporate leaders are more willing to return surplus cash to shareholders, with the dividend payout ratio rising from 36.7 per cent in 1995 to almost 41 per cent on this year's estimates.

The fund will carry an annual management fee of 1.5 per cent and launch on December 12.

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