



Upgrade Earnings

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## Hong Kong Media

Reuters 2366.HK  
Bloomberg 2366 HK

### Priced on 22 May 2007

HK HSI @ 20,843.9

12M hi/lo HK\$4.15/1.87

12M price target HK\$4.50  
±% potential +12%  
Target set on 22 May 07

Shares in issue 512.5m  
Free float (est.) 45.8%

Market cap US\$263m

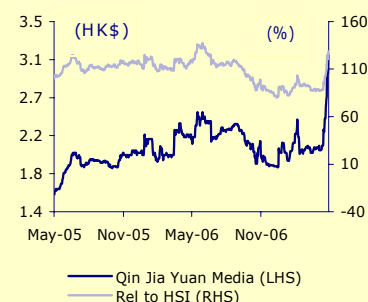
3M average daily volume  
HK\$5.3m (US\$0.7m)

### Major shareholders

Anita Leung / Philip Wong 35.2%  
Aegis plc 19.0%

### Stock performance (%)

	1M	3M	12M
Absolute	90.0	78.2	82.3
Relative	87.5	77.9	38.2
Abs (US\$)	89.8	77.9	80.7



Source: Bloomberg

www.cls.com

## Strong marketing: 4As

QJY Media, a HK based media related small cap, has acquired a PRC nationwide ad agency licence; and will be a beneficiary of the growing ad market in China - which we expect to take off with the '08 Beijing Olympics and the '10 Shanghai World Expo. After raising our earnings by 15-18%, valuations remain relatively attractive at only 11x CY08CL earnings, more than 50% discount to its peer group. This discount should narrow as the company executes on its plans in becoming a leader in the PRC media industry.

### Adding value: Acquisition of nationwide ad agent license

QJY has been awarded a nationwide advertising agency license; and for a consideration of HK\$38m, the company has acquired the advertising contracts owned by HA Group worth over HK\$100m (over a period of 5-10 years). Not only does this provide QJY Media with another revenue stream in China, the main benefit is that it could cut out the middleman - who normally keeps up to 15% of gross ad revenues. We have lifted FYSep08-09CL earnings by 15-18% to reflect the likely benefits.

### Advertising China

China's advertising market is one of the fastest growing in the world, with a 17% 2002-06 Cagr on booming consumer demand and advertisers' need to build national brands. With the *Beijing Olympics* in 2008 and *Shanghai World Expo* and *Guangzhou Asian Games* in 2010, we forecast ad-spend in China to grow at a Cagr of 18.3% from 07-09. Meanwhile China's low per-capita ad-spend highlights the long-term potential, especially given rising incomes.

### Attracting attention

QJY's share price has risen 90% in the past month; and has attracted greater levels of institutional interest following its better than expected interim FYSep07 results and an alliance with **NewsCorp's (NWS AU) Star TV** to explore the global Chinese TV drama market. CEO Dr Anita Leung presented at the CLSA Singapore CA Forum this week - with substantial client interest and a busy one-one meeting schedule.

### Attractive value vs peers

Based on our new forecasts, QJY now trades at 17.3x current year and 11.1x forward earnings (vs a historical PE average of 10x). Nevertheless, valuations remain cheap against the China media industry CY08 PE average of 28x. Our revised fair value of HK\$4.50/share is equivalent to 12x CY08CL earnings, approx one standard deviation above mean to reflect its growth prospects, but still at a substantial discount to peers, reflecting a smaller market cap and high execution risks.

### Financials

Year to 30 Sep	05A	06A	07CL	08CL	09CL
Revenue (HK\$m)	106	125	188	320	384
Rev forecast change (%)			0	16.3	14.8
Net profit (HK\$m)	66	84	119	184	215
NP forecast change (%)			0	18.5	14.8
EPS (HK¢)	14.1	16.4	23.2	36.0	42.0
CL/consensus(2)(EPS%)	-	-	102	118	114
EPS (% YoY)	11.9	16.3	41.2	55.3	16.8
PEX (@HK\$4.01)	28.4	24.5	17.3	11.1	9.5
EV/Op Ebitda (x)	23.7	21.4	14.9	9.2	7.3
Dividend yield (%)	0.8	0.9	1.2	1.8	2.1
Net cash (HK\$m)	157	190	-	-	-

Source: CLSA Asia-Pacific Markets

**Key drivers**

Figure 1

**QJY – Key assumptions and drivers**

<b>FYE September</b>	<b>05A</b>	<b>06A</b>	<b>07CL</b>	<b>08CL</b>	<b>09CL</b>
Drama (episodes)	126	216	280	400	500
YoY%	117.2	71.4	29.6	42.9	25.0
<b>Ad/PR/Sponsorship revenues (HK\$m)</b>	<b>50</b>	<b>51</b>	<b>109</b>	<b>208</b>	<b>244</b>
YoY%	(2.5)	1.6	113.5	90.5	17.1
<i>Previous (HK\$m)</i>				163	194
EBIT margins (%)	66.3	68.0	66.9	68.8	71.4
Effective tax rate (%)	3.2	0.4	2.6	13.0	18.2
Payout ratio (%)	21.1	21.9	20.0	20.0	20.0

Source: CLSA Asia-Pacific Markets

**Adding value:**

**We have lifted our ad revenue/PR/sponsorship revenue forecasts**

**Attracting attention:**

**Leading TV drama producer**

**Looking to increase market share**

**Grand plans:**

**Looking to acquire ad rights for a provincial satellite channel**

**Broadcasting the story**

**Generating good feedback**

**Key takeaways from QJY presentation - Singapore CAF**

- ❑ QJY produces TV drama programs which it provides to TV channels in China for advertising rights.
- ❑ Production of programs of the Co increased from 126 in 2005 to 216 in 2006. Management forecast this will grow to 280 in 2007 and rise to 1,000 by 2010. That would lift QJY's market share for production of drama programs in China from 4% in 2006 to 20% by 2010.
- ❑ Management outlined medium-term goals. Phase 1 (2007-08): to establish business activity equivalent to running one provincial TV station, ie secure exclusive advertising rights for 1 satellite channel (which can broadcast nationally) and 6 ground channels (which broadcast within a given province).
- ❑ Phase 2 (2009 – 2010): to become one of the top 5 TV business players in the PRC, ie to have exclusive advertising rights for 3 satellite channels and 10 ground channels.
- ❑ Phase 3 (2010 – 2012): to become 2nd largest TV business player behind only CCTV – ie to have advertising rights for 6 satellite channels and 16 ground channels.
- ❑ Acquisition cost of a ground channel eg the one that QJY has already secured in Hubei in Feb-07 is RMB60m for 3 years, of which the annual charge of RMB20m is divided between RMB4m paid for 'underwriting' advertising income to the channel while RMB16m is for production of programs. For a national satellite channel, cost could be RMB300m per year, of which 1/3 is to 'underwriting' the advertising income to the TV channel, and 2/3 is the budget for production of programs. The payment is by instalments, but to meet targets, management does not rule out potential equity raising by the Co.
- ❑ Programs are produced by external production teams, key resource required by QJY are producers who determine the script and supervise editing of programs. QJY has 4 producers currently and expects by 2010 to have 7 which is estimated to be sufficient to produce 1,000 programs annually (CCTV has 10 producers). There are over a thousand production teams in China partly owing to liberalization of this sector by the government allowing people previously employed by government TV companies to work in the private sector.
- ❑ Management said they had to explain to HKEx why stock rose 30% today: the company announced strong interims (net profit rose 45%) on 10 May and has recently been on a road-show explaining their business model.
- ❑ Substantial interest from clients with good Q&A at the workshop presentation, with a busy schedule of one-one meetings as well for Anita Leung (CEO) who presented.

**China's advertising market is one of the fastest growing, with booming consumer demand and advertisers' need to build national brands**

**China's ad spend has grown at a Cagr of 17% from 2002-2006**

**China's ad-spend remains modest relative to GDP**

**China's low per-capita ad-spend highlights the long-term potential given rising incomes**

**Catalysts:**

**2008 Olympics**

**Increasing brand building efforts**

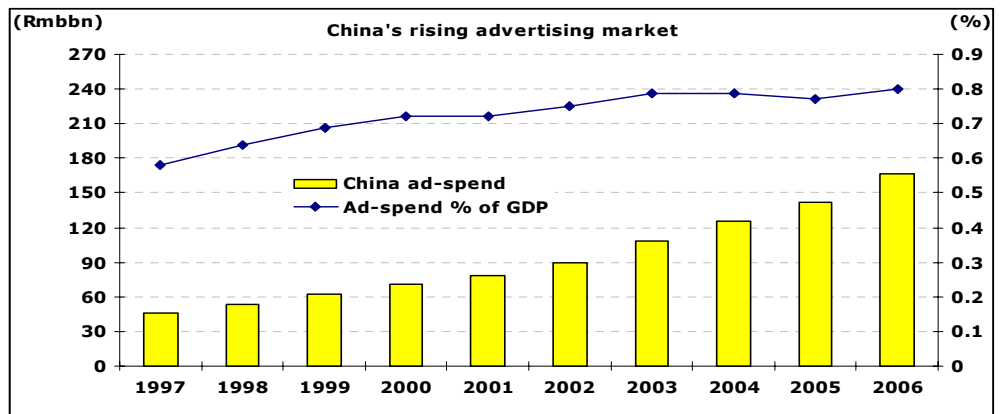
**Increasing pricing power**

**Advertising China**

China's advertising market is the world's fourth-largest at US\$21bn. It is also one of the fastest growing, with a 17% 2002-06 Cagr on booming consumer demand and advertisers' need to build national brands. With the Beijing Olympics in 2008 and Shanghai World Expo and Guangzhou Asian Games in 2010, we forecast ad-spend in China to grow at a Cagr of 18.3% from 07-09.

Figure 2

**China's rising advertising market**



Source: CEIC, CLSA Asia-Pacific Markets

China's advertising market remains modest relative to GDP at 0.8%, at the low-end of the 0.8-1.2% range for developed markets such as Europe and North America. China's ad-spend is not low for an emerging market as market competition is high and an increasing number of companies are trying to build nationwide brands. However, this trend is likely to accelerate as the spending power of Chinese consumers continues to increase and brand advertising becomes more targeted.

Moreover, China's per-average capita ad-spend is very low by global standards at only US\$16. Developed countries in Western Europe and North America have an average per-capita ad-spend of US\$230 and US\$540 respectively. China's low per-capita ad-spend highlights the long-term potential, especially given rising incomes, plus international and domestic corporate brand-building efforts.

We expect Chinese advertising revenue to continue growing at around 20% per annum over the next two years driven by the following factors:

- ❑ The 2008 Beijing Olympics will be a catalyst for the global advertising market, as well as China's. Typically ad growth spikes during the Olympics, and it will represent a golden opportunity for both domestic companies and multinationals to expand their brands in China.
- ❑ China's entry into the WTO and relaxation of foreign ownership limits across a wide range of industries has attracted more and more multinationals, to set up and expand their presence in China. Efforts to build brand recognition in China should continue to drive ad spend. For example, the opening of the banking services for foreign banks boosted ad spend in the financial sector by 33% last year. Domestic companies are also facing pressure to increase marketing given rising competition.
- ❑ CCTV's auction of its 2007 primetime ad-spot sales hit a record Rmb6.79bn, up 16%YoY. This was much higher than the 10%YoY increase last year, mainly driven by a 25% jump in bids from foreign brands and excitement around new ad products related to the Olympics.

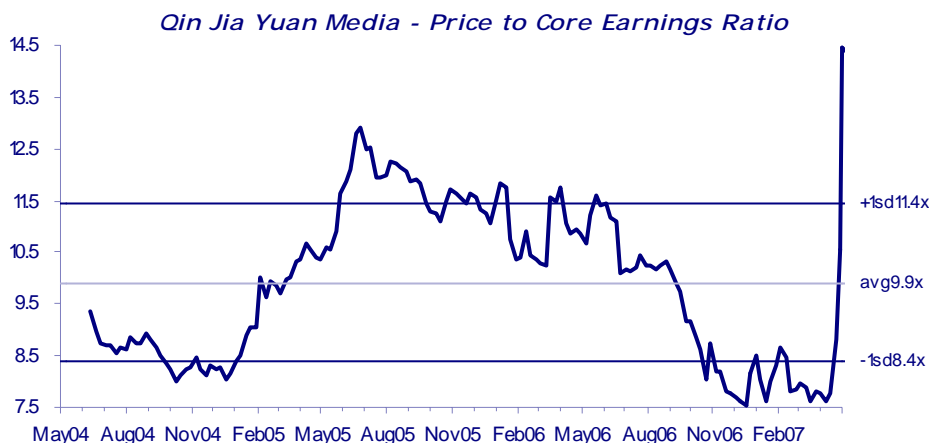
Following a sharp rise, QJY is now trading on 17.3x current year and 11.1x forward earnings (vs a historical PE average of 10x)

However valuations remain cheap against its China media sector peers (which are trading at an average of 28.3x CY08F earnings)

We have lifted our fair value target to **HK\$4.50/share** from **HK\$3.66/share**

Figure 3

**QJY – Historical PE valuations**

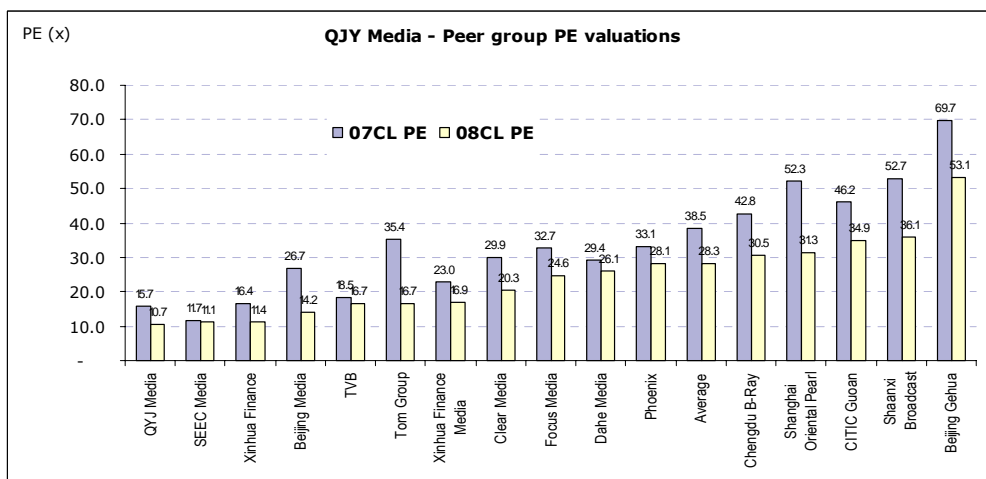


Source: CLSA Evalu@tor

Source: CLSA Asia-Pacific Markets

Figure 4

**QJY – Peer group P/E comparisons**



Source: CLSA Asia-Pacific Markets / Bloomberg / IBES

**Recommendation history - Qin Jia Yuan Media Services 2366 HK**

Date	Rec level	Closing price	Target
22 May 2007	N-R	3.13	4.50
10 May 2007	N-R	2.28	3.66
20 February 2007	N-R	2.16	3.36
16 May 2006	N-R	2.23	3.28

Source: CLSA Asia-Pacific Markets

**Key to CLSA investment rankings:** BUY = Expected to outperform the local market by >10%; O-PF = Expected to outperform the local market by 0-10%; U-PF = Expected to underperform the local market by 0-10%; SELL = Expected to underperform the local market by >10%. Performance is defined as 12-month total return (including dividends).

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Note: In the interests of timeliness, this document has not been edited.

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