

Tongda Group

LED TV light guide plate business to contribute in 2011

to summarize...

- Top line rose 30% YoY in FY12/10A to HK\$2,348m. Mobile handset sub-segment performed especially well thanks to the strong growth of key clients.
- Gross margin has been improved continuously after the financial crisis. It increased 0.6 pcp in FY12/10A to 17.4%.
- Although account receivables accumulated a bit faster than top line growth, majority is within general three-month credit period.
- New LED TV light guide plate business went well with unchanged output guidance of 6m pieces for FY12/11F.
- The results are better than we expected. We adjusted our preliminary forecasts and expect FY12/11F earnings to be HK\$270m. Thus, the counter is trading at 7.3 one-year forward P/E.

Top line driven by demand from mobile handset sector. Revenue increased 30% in FY12/10A to HK\$2,348m or 17% in 2H to HK\$1,309m. Although iron parts division and communication facilities and others division recorded sales retreat in 2H, the core electrical fittings segment retained a satisfactory 28% growth with push mainly from mobile handset sub-segment, whose turnover picked up 73% to HK\$577m (full year: up 51% YoY to HK\$951m). As a strategic partner of ZTE (0763 HK) and Huawei (the two names account for ~30% of the segmental revenue), TDG definitely benefited from the latter two' supreme shipment growth last year (ZTE: 77% YoY; Huawei: 80% YoY). Such effect may last into 2011, because ZTE and Huawei, according to our check, are anticipated to maintain their strong performance with handset shipment growth guided at 33% and 40%, respectively.

Table 1. Sales in FY12/10A

Year to Dec (HK\$m)	1H 10A	YoY growth	2H 10A	YoY growth	10A	YoY growth
Revenue	1,039.5	53.3%	1,308.8	16.6%	2,348.3	30.4%
Electrical fittings	794.4	72.2%	1,082.2	28.2%	1,876.7	43.7%
Handsets	374.0	25.9%	576.7	73.2%	950.7	50.9%
Electrical appliances	230.0	144.7%	372.4	6.1%	602.4	35.4%
Notebooks	174.0	163.6%	147.5	-7.2%	321.5	42.9%
Ironware parts	167.2	2.3%	163.0	-6.7%	330.2	-2.4%
Communication facilities and others	77.9	46.1%	65.6	-36.4%	143.4	-8.3%

Source: Company data

Gross margin improved steadily. Gross margin dipped 1.3 pcps HoH in 2H to 16.8% largely due to seasonality but improved 0.1 pcp YoY. On a full-year basis, it widened 0.6 pcp to 17.4%. Although it is still far below the pre-financial crisis level (1H FY12/07A: 27%), a continuous improvement has been since 2H FY12/07A amid the backdrop of gradually recovering economy. Further margin enhancement is possible backed by enlarging operating scale and strengthening demand, though we cautiously assume a flat gross margin trend for FY12/11F in our preliminary estimates.

97% up in bottom line. Operating expenses was well controlled at 6.9% of total turnover in 2H, versus 8.8% in 1H. Meanwhile, other income, surprisingly, increased from HK\$9.8m to HK\$27m, of which HK\$7.9m came from foreign exchange differences (1H: HK\$1.1m). Effective tax rate also dropped from 16% to 13%. Thus, 2H net profit increased significantly from HK\$81m in 1H to HK\$120m, bringing the full-year figure to HK\$201m, nearly doubled from HK\$102m last year and 16%

Ticker	0698 HK
Rating	Not Rated
Price (HK\$)	0.425
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	0.255-0.530
Market cap. (US\$m)	254.6
Daily t/o (US\$m)	1.1
Free float (%)	46.8

Financial summary

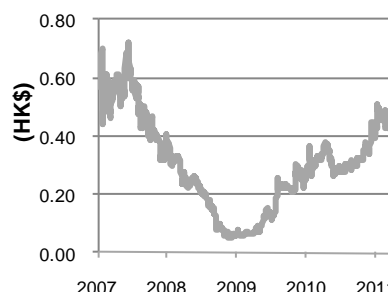
Year to Dec	08A	09A	10A
Turnover (HK\$m)	1,394	1,800	2,348
Net Profit (HK\$m)	65	102	201
EPS (HK\$)	0.016	0.025	0.045
P/E (x)	25.9	16.9	9.4
P/B (x)	1.44	1.27	1.05
EV/EBITDA (x)	12.8	9.4	6.1
Yield (%)	1.4	2.0	2.6
ROE (%)	5.6	8.1	13.6
ROCE (%)	6.5	7.7	11.8
N. Gear. (%)	15.1	6.5	12.7

Source: SBI E2-Capital

	11F	12F	13F
Consensus EPS (HK\$)	0.53	0.060	n.a.
Previous earnings (HK\$m)	-	-	-
Previous EPS (HK\$)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	(3.4)	+5.7	+27.4
Actual price changes (%)	(7.6)	+3.7	+32.8



Source: Bloomberg

Norman Zhang, CFA

(852) 2533 3723

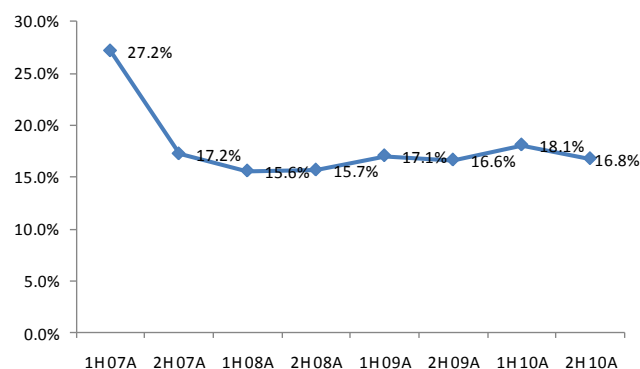
normanzhang@sbie2capital.com

higher than our previous forecast of HK\$174m.

AR piled up. Apart from the encouraging earnings figures, we noticed the increase in account receivables from HK\$631m in FY12/09A to HK\$1,020m this year. According to the management, AR piled up due to sales expansion. As majority of the AR (HK\$906m) is within general three-month credit period, we reckon associated bad debt risk is low. Cash reserved (incl. cash balance, restricted cash and pledged cash) dropped by HK\$18m. Other than working capital requirement, cash flew out for expanding capacity during the period.

Guidance unchanged for TDO. There is no special update on TDO, the 55:45 JV with Matsushita Shokai engaged in production of LED TV light guide plate. The management re-iterated its 2011 output target of ~6m pieces. According to our last site visit in Jan, operation launched already. Actual output in Jan/Feb was 200,000-300,000 pieces/month, which is ramping up gradually. The 6m pieces target so far seems achievable and we will monitor the monthly output number closely. As discussed in our early reports, the TDO will be a significant earnings factor. Based on an output of 6m pieces, potential earnings contribution to the listco can be HK\$53m.

Chart 1. Breakdown of electrical fittings segment 1H FY12/10A



Source: Company data

Table 2. TDO FY12/11F estimates and sensitivity test

Gross margin assumption (%)	20.0	22.5	25.0	27.5	30.0
Sales volume (pieces m)	6.0	6.0	6.0	6.0	6.0
ASP (US\$/piece)	20.0	20.0	20.0	20.0	20.0
Revenue (HK\$m)	936.0	936.0	936.0	936.0	936.0
Gross profit (HK\$m)	187.2	210.6	234.0	257.4	280.8
Net profit (HK\$m)	96.9	120.3	143.7	167.1	190.5
Profit attributable to TDG (HK\$m)	53.3	66.2	79.0	91.9	104.8

Source: SBI E2-Capital

Preliminary estimates revised up. We fine-tuned our assumptions in calculating TDG's FY12/11F earnings. Growth of mobile handset sub-segment has been revised from 5% to 30%, in line with ZTE and Huawei's growth guidance. Meanwhile, communication facilities and others segment is expected to have zero growth from previous 10%. Thereafter, our new calculations suggest TDG may 16% growth in its top line in FY12/11F to HK\$2,728m and net profit will increase 10% to HK\$220m (mainly due to less contribution from other income item). Combining contribution from TDO, TDG's overall FY12/11F earnings may reach HK\$274m, up 36% YoY, which puts the counter at an undemanding P/E of 7.3X.

Table 3. Adjustments of preliminary estimates

Year to Dec (HK\$m)	Old	YoY growth	NEW	YoY growth (%)
	11F		11F	
Revenue (excl. TDO)	2,328.3	7.7%	2,727.9	16.2%
Electrical fittings	1,787.4	9.1%	2,254.3	20.1%
Handsets	777.7	10.0%	1,235.9	30.0%
Electrical appliances	610.1	5.0%	632.6	5.0%
Notebooks	399.6	20.0%	385.8	20.0%
Ironware parts	341.8	0.0%	330.2	0.0%
Communication facilities and others	199.1	10.0%	143.4	0.0%
		Margin		Margin
Gross profit (excl. TDO)	421.3	18.1%	473.4	17.4%
Operating profit (excl. TDO)	249.1	10.7%	289.3	10.6%
Net profit (excl. TDO)	191.9	8.2%	220.3	8.1%
Contribution from TDO	50.4		53.3	
Total net profit	242.3		273.6	

Source: SBI E2-Capital

Table 4. P&L

Year to Dec (HK\$m)	08A	09A	10A
Revenue	1,393.8	1,800.3	2,348.3
Gross profit	217.9	302.4	407.6
Operating profit	111.1	151.6	262.1
Net profit	65.3	102.1	200.9
EBITDA	172.0	233.3	360.7
Fixed assets	752.8	822.3	957.0
Inventories	305.9	369.2	472.2
Receivables	690.2	706.1	1,132.5
Payables	360.3	492.4	748.0
Cash	199.0	257.5	240.3
Short-term debt	170.9	248.2	282.4
Long-term debt	211.2	99.1	169.8
Shareholders' fund	1,181.7	1,333.5	1,616.0
Total equity	1,215.3	1,380.8	1,662.5
Net cash from operating activities	47.7	259.8	n.a.
Net cash used in investing activities	(266.2)	(130.2)	n.a.
Net cash from financing activities	221.7	(51.7)	n.a.
Net change in cash and cash equivalents	3.2	77.9	n.a.

Source: Company data

Table 5. 1H results highlight

Year to Dec (HK\$m)	08A	09A	10A
Revenue	1,393.8	1,800.3	2,348.3
Cost of sales	(1,175.9)	(1,497.9)	(1,940.7)
Gross profit	217.9	302.4	407.6
Other income and gain, net	52.4	25.0	36.5
Selling and distribution costs	(39.0)	(49.0)	(53.1)
Administrative expenses	(97.6)	(108.1)	(122.8)
Change in fair value of warrants	0.0	0.0	0.0
Other expenses, net	(22.5)	(18.6)	(6.0)
Profit from operations	111.1	151.6	262.1
Finance costs	(27.3)	(16.7)	(20.3)
Share of profits and losses of	0.0	0.0	0.0
Associates	2.7	3.1	2.6
A jointly-controlled entity	3.6	0.0	0.0
Profit before tax	90.1	138.1	244.5
Income tax	(18.7)	(24.2)	(34.2)
Profit for the period	71.3	113.8	210.2
Attributable to:	0.0	0.0	0.0
Owners of the Company	65.3	102.1	200.9
Minority interests	6.0	11.7	9.3
EPS - Basic (HK\$)	0.016	0.025	0.045
EPS - Diluted (HK\$)	0.016	0.025	0.043

Source: Company data

Table 6. Shareholding structure

Shareholders	Interest (%)
Wong Brothers	53.19
Others	46.81

Source: Bloomberg

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