

## Truly International Holdings

### Riding on two wheels

to summarize...

- As a major supplier of small-size display module, the company serves mainly Chinese domestic mobile handset brands and owns 50%+ market share.
- Chinese handset brands did well last year and the momentum is likely to retain based on leading players' sales target this year.
- Consumption upgrade from feature phone to smartphone, triggered by maturity of Android system, may bring up demand for touch screen displays, which are much more expensive and profitable than conventional ones for display vendors.
- In a longer term, the company is looking at automobile display market, which is still controlled by Japanese players. The management expects revenue of this new business to over double this year to HK\$800m-1,000m, which will grow another 50% in FY12/12F.
- Accordingly, we derive our preliminary estimates that the company will achieve 20%+ top-line growth in both FY12/11F and FY12/12F. Gross margin will stay relatively stable. Thus, current valuation of 10x historical P/E seems unstretched. The valuation will decrease to 7.1x in FY12/11F and 4.2x in FY12/12F based on market consensus.

**A major supplier of handset display for Chinese brands.** As a major supplier of small-size display module, Truly International Holdings (TIH) serves mainly Chinese domestic mobile handset brands, which accounts for ~65% of the company's total revenue. According to the management, it has 50%+ market share for this specific business in China. Clients include almost all Chinese brands such as ZTE, Huawei, TCL, etc. Chinese handset brands did well last year and the momentum is expected to retain. According to our channel checks, for example, ZTE and Huawei plan to sell 80m and 60m handsets in 2011, respectively, which are 33% and 88% higher than last year. Meanwhile, TCL posted 37% volume growth in 1H and maintained full-year target at 50m, up 39% YoY.

**Stepping into touch screen era.** A major trend of mobile industry is the migration from feature phone to smartphone, boosted particularly by the penetration of Android system. As a result, demand for touch-screen display (TSD) has been increasing. Compared with conventional product, TSD carries higher ASP and gross margin and, therefore, favors display vendors in general. TIH shipped 3.5m TSD modules (out of total 75m) in 1H, which is expected to increase to 6-10m in 2H based on clients' feedback. Thus, a second TSD production line has been constructed, bringing total design capacity from 1.5m/month to 4.5m (yield rate: ~70%), and trial started at beginning-Aug.

**Table 1. Comparison of conventional display and TSD**

	Conventional display	TSD
ASP	~US\$4	US\$17-25 (3.8")
Gross margin	8-13%	12-20%

Source: compiled by SBI E2-Capital

**Ramping up automotive application.** Other than mobile handset, the company is looking at automobile display, e.g. dashboard, for long term development. The market currently is dominated by Japanese companies. Due to obvious cost advantage as well as the rising of China into the largest automotive market in the world, the management believes there is a well chance ahead. In fact, it has been qualified by all major auto brands except BMW and Mercedes. Automobile products accounted for ~5% (~HK\$380m) of the company's revenue in FY12/10A. Following delivery of orders in coming years, segmental revenue is anticipated to hit

Please refer to important disclosures at the end of this report

Ticker	0732 HK
Rating	Not Rated
Price (HK\$)	1.15
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	0.97-2.69
Market cap. (US\$m)	408.1
Daily t/o (US\$m)	1.7
Free float (%)	41.5

#### Financial summary

Year to Dec	08A	09A	10A
Turnover (HK\$m)	5,669	5,804	7,736
Net Profit (HK\$m)	261	307	315
EPS (HK\$)	0.100	0.118	0.115
P/E (x)	11.5	9.7	10.0
P/B (x)	0.9	0.9	0.8
EV/EBITDA (x)		5.5	4.6
Yield (%)	8.7	2.8	5.1
ROE (%)	8.0	8.8	8.0
ROCE (%)	5.7	6.2	5.5
N. Gear. (%)	44.2	44.3	35.8

Source: SBI E2-Capital

	11F	12F	13F
Consensus EPS (HK\$)	0.162	0.273	0.300
Previous earnings (HK\$m)	-	-	-
Previous EPS (HK\$)	-	-	-

#### Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	10.4	(13.3)	(36.4)
Actual price changes (%)	0.0	(26.3)	(40.9)



Source: Bloomberg

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HK\$800-1,000m this year and maintain 50% growth even in 2012.

**Growth story in our eyes.** Thereafter, we have our own growth picture towards TIH. Despite still prosperous feature phone market, we do not expect any significant capacity expansion in this area due to continuous margin pressure under keen competition. In short term, growth may mainly come from TSD. However, it should not be a surprise that TSD will also face a declining margin quickly following market maturity and intensifying competition. We expect then TIH will find momentum from automotive products. In addition, due to much longer lifespan of each car model compared with mobile phone, automotive business has better sales visibility and more stable gross margin.

**Preliminary forecasts.** In our preliminary calculations, the company may have 29% top-line growth in FY12/11F to HK\$10,011m. Gross profit will increase 25% to HK\$1,140m. The two figures will increase 24% and 27%, respectively, in FY12/12F to HK\$12,421m and HK\$1,446m. In the reported 1Q FY12/11A results, revenue went up 33% to HK\$2,120m, while gross profit 27% to HK\$270m and net profit 20% to HK\$122m.

<b>Table 2. Preliminary forecasts</b>			
<b>Year to Dec (HK\$ m)</b>	<b>10A</b>	<b>11F</b>	<b>12F</b>
<b>Turnover</b>	7,735.7	10,011.3	12,421.1
Mobile handset	5,028.2	6,085.4	7,437.4
Conventional display	5,028.2	4,525.4	3,927.4
TSD		1,560.0	3,510.0
Automotive	386.8	908.9	1,363.4
Others	2,320.7	3,016.9	3,620.3
<b>Growth</b>	33.3%	29.4%	24.1%
Mobile handset		21.0%	22.2%
Conventional display			
TSD			
Automotive		135.0%	50.0%
Others		30.0%	20.0%
<b>Shipment volume (m)</b>			
Mobile handset	140.0	150.0	160.0
Conventional display		140.0	135.0
TSD		10.0	25.0
<b>ASP (HK\$)</b>			
Mobile handset	35.9	40.6	46.5
Conventional display	35.9	32.3	29.1
TSD		156.0	140.4
<b>Gross profit</b>	910.6	1,140.2	1,446.2
Mobile handset	502.8	549.2	696.1
Conventional display	502.8	362.0	274.9
TSD		187.2	421.2
Automotive	58.0	136.3	204.5
Others	349.7	454.7	545.6
<b>Gross margin</b>	11.8%	11.4%	11.6%
Mobile handset	10.0%	9.0%	9.4%
Conventional display	10.0%	8.0%	7.0%
TSD		12.0%	12.0%
Automotive	15.0%	15.0%	15.0%
Others	15.1%	15.1%	15.1%

Source: Company data

**Valuation.** Based on the growth picture, which can translate into 20+% top-line growth in coming two years and potential margin enhancement in FY12/12F in our preliminary forecasts, we think the counter's current valuation at 10x historical earnings is unstretched. The street expects the P/E multiple to decline to 7.1x in FY12/11F and 4.2x in FY12/12F.

**Risks.** Major risk should come from the market side.

**Table 3. Key financials**

Year to Dec (HK\$ m)	08A	09A	10A
Revenue	5,669.3	5,804.2	7,735.7
Gross profit	696.0	828.1	910.6
Operating profit	406.1	455.1	532.6
EBITDA	823.5	831.6	992.8
Net profit	261.1	307.3	315.0
EPS (HK\$)	0.100	0.118	0.115
Fixed assets	4,223.0	4,177.7	4,228.9
Inventories	708.3	692.9	748.9
Receivables	649.7	1,044.5	1,853.8
Payables	1,103.7	1,050.3	1,566.8
Cash	687.4	503.1	851.9
Short-term debt	2,100.8	2,030.7	1,655.0
Long-term debt	20.6	14.8	610.2
Shareholders' fund	3,246.0	3,484.0	3,950.4
Total equity	3,246.1	3,484.1	3,950.4
Net cash from operating activities	1,051.0	353.3	518.4
Net cash used in investing activities	(1,325.4)	(331.5)	(469.9)
Net cash from financing activities	399.2	(206.2)	298.7
Net change in cash and cash equivalents	124.8	(184.4)	347.1

Source: Company data

**Table 4. P&L**

Year to Dec (HK\$ m)	08A	09A	10A
Turnover	5,669.3	5,804.2	7,735.7
Cost of sales	(4,973.3)	(4,976.1)	(6,825.1)
Gross profit	696.0	828.1	910.6
Other income	86.5	25.6	37.9
Other gains and losses	(45.1)	(101.8)	(36.8)
Administrative expenses	(190.9)	(186.5)	(231.7)
Distribution and selling expenses	(140.4)	(110.3)	(147.5)
Profit from operations	406.1	455.1	532.6
Finance costs	(67.0)	(46.6)	(43.4)
Profit before taxation	339.1	408.4	489.2
Income tax expenses	(77.9)	(101.1)	(174.2)
Profit for the period	261.1	307.3	315.0
Attributable to:			
Shareholders of the Company	261.1	307.3	315.0
Minority interests			
EPS - Basic (HK\$)	0.100	0.118	0.115
EPS - Diluted (HK\$)	0.100	0.118	0.115
Proposed DPS (HK\$)	0.100	0.033	0.058
Proposed dividend	260.0	85.1	161.0

Source: Company data

**Table 5. Shareholding structure (after exercise of all equity instruments)**

Shareholders	Interest
Lam Wai Wah & Chung King Yee	44.41%
Chan Kin Sun & Cheng Kwan Ying	7.70%
Others	47.89%
Total	100.0%

Source: HKEx

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**BUY** : absolute upside of >10% over the next six months

**HOLD** : absolute return of -10% to +10% over the next six months

**SELL** : absolute downside of >10% over the next six months

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