

# Solargiga



Not Rated

## Sunshine in winter

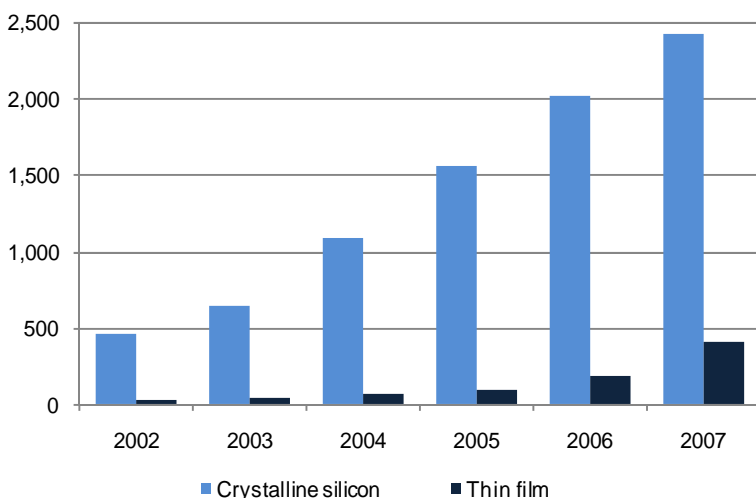
### Key points:

- Bright industry prospects.
- Increasing supply of polysilicon to reduce costs, potentially boosting demand for solar systems.
- China's second largest manufacturer of monocrystalline ingots - capacity to double to 400MW in 2009.
- Long-term supply contracts signed this year to secure polysilicon requirements in 2009.
- Substantial technology-related risks.

**Rapid development.** Solar energy is an attractive alternative to traditional fossil fuels. According to Solarbuzz, an independent international solar energy consultancy, global solar photovoltaic (PV) installations increased 62% in 2007 to 2,826MW. Despite the global economic slowdown and substantial drop in the oil price, we expect the solar industry to remain in good shape as governments will probably pump more money into renewable energy in a bid to stimulate the economy.

**Mainstream - crystalline silicon-based technology.** Two main technologies employed in the production of solar cells are defined by the choice of the semiconductor: 1) crystalline silicon in a wafer form (91.7% of the world's total PV cell output in 2006) or 2) thin films of other materials (8.3%). The former is a traditional light-absorbing semiconductor and can be divided into two sub-groups: monocrystalline (42.4%) and multicrystalline (49.3%). Monocrystalline silicon always has a higher conversion efficiency ratio than multicrystalline but is also more expensive. Thin film is cheaper but less efficient than crystalline silicone. The world's demand for thin film solar systems has been growing rapidly in recent years backed by the high polysilicon price.

Chart 1: World's solar PV installation by technology



Source: Solarbuzz

### China Industrials

Mon, 08 Dec 2008

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### Stock data

Price	HK\$1.83
Target price	n.a.
12 mth range	HK\$1.13-7.10
Market cap.	US\$397.6m
Daily t/o, 3 mth	US\$0.7m
Free float %	35.6%
Ticker	0757.HK/ 757 HK

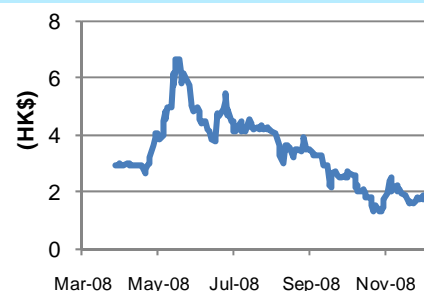
### Financial summary

Year to Dec	06A	07A
Turnover (RMBm)	413.3	1,015.5
Net Profit (RMBm)	109.7	292.2
EPS (RMB)	0.219	0.582
EPS %	165.5	165.5
P/E (x)	7.4	2.8
P/B (x)	1.79	4.33
EV/EBITDA (x)	14.2	7.1
Yield (%)		3.2
ROE (%)	72.5	71.1
ROCE (%)	230.3	216.3
N. Gear. (%)	Cash	Cash

### Price Performance

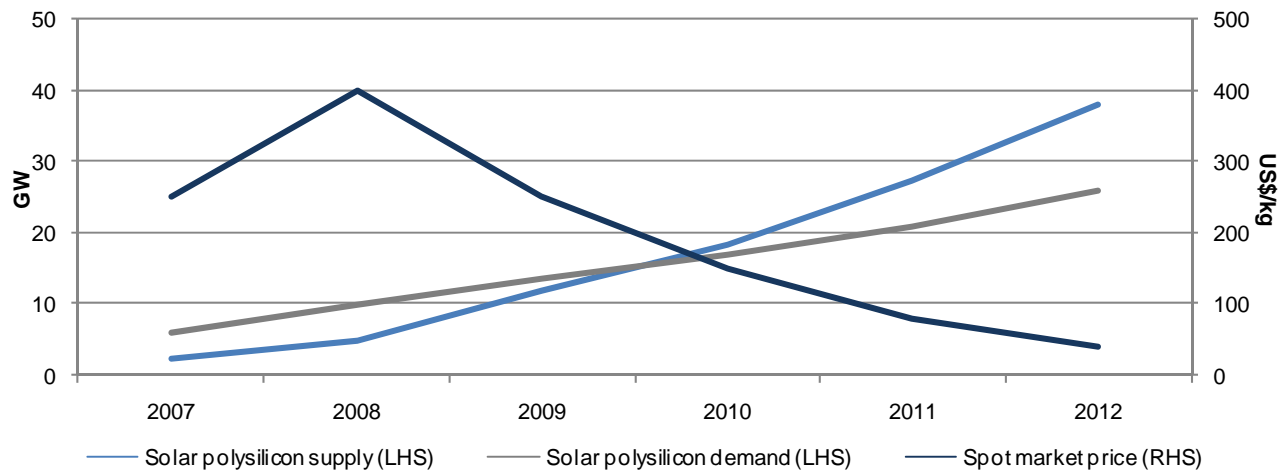
	1 mth	3 mth	12 mth
Relative to HSI (%)	-20.0	-23.0	n.a.
Actual price changes (%)	-16.4	-44.9	n.a.
	08F	09F	10F
Consensus EPS (RMB)	0.248	0.333	0.427
Previous forecasts (RMB)	n.a.	n.a.	n.a.
Previous EPS (RMB)	n.a.	n.a.	n.a.

### Price Chart



**New capacity to reduce polysilicon costs.** Polysilicon is the core raw material of crystalline silicon, which makes up 40-50% of finished solar module costs. Driven by the strong demand, its spot price has been rising significantly from US\$30/kg in 2004 to US\$400/kg this year. With new capacity globally, the polysilicon price is expected to decline gradually after 2008 (some supply shortages may still emerge in 2009), which should spur solar PV installation and encourage a consumption shift back to crystalline silicon products.

**Chart 2: Global supply/demand of solar polysilicon and price trend**



Source: Solarbuzz

**400MW capacity by 2010.** Solargiga is China's second largest manufacturer of monocrystalline silicon ingots, after Jinglong Group. Its major products include ingots and wafers. With plants in Jinzhou (main base) and Shanghai (for reclaiming polysilicon), it had 196 ingot pullers and 24 wire-saws by end-September with a capacity of 2,000 tonnes of ingots (equivalent to around 200MW light energy conversion capacity) and 48m pieces of wafers. The company plans to double its ingot capacity to 4,000 tonnes (equivalent to around 400MW light energy conversion capacity) by 2009 and increase wafer capacity to 150m pieces.

**Secured polysilicon supply in 2009.** The company signed several long-term contracts with polysilicon vendors this year to stabilize its raw material supply, which, in 2009, can satisfy around 35% of its total polysilicon requirement, with remaining 35% from the spot market and 30% from OEM clients. Contract length ranges at 5, 7 and ten years. Normally the contract price is considerably lower than the spot one (e.g. US\$90 contract price versus US\$300 spot in 2007). Hence we expect these long-term contracts to favor the company's gross margin in 2009. Although they will result in high procurement costs in the long term, against the backdrop of the declining polysilicon price, we believe that the impact will not be substantial, as long as the company maintains the pace of its capacity expansion.

**Background.** Solargiga was established in 2000. In 2006, the company introduced Taiwan-based WWX as a strategic investor. WWX is a world's leading semiconductor manufacturer, raking seventh in wafer sales in 2006. After acquiring Youhua through a connected transaction in 2006, Solargiga listed in Hong Kong in Mar 2008 via a global offering of 338.1m shares, including 84.5m sale shares, at HK\$2.92 each. Substantial shareholders now include Tan Wenhua (30.7%), WWX (21.2%), SEC (8.6%), Chong Kin Ngai (8.0%) and Jean Salata (7.0%). In 1-3Q FY12/08A, the company's turnover increased 35.9% to RMB1,199.7m on a pro-forma basis while net profit rose 59.3% to RMB318.1m, excluding RMB11.6m one-off listing expenses.

**Our view and valuation.** We think the company's growth will be driven mainly by the industry's strong organic momentum. The maturing market will attract more players pushing down profit margins. The company might need to continuously invest in capacity to maintain its earnings growth. It had RMB575.0m cash (net: RMB542.0) at end-June. The counter now is trading at 6.6x one-year P/E, versus average 5.3x of its international peers.

**Major risks.** One of major risks, in our view, is associated with the technical side. A new technology might significantly change the industry's landscape. Also, any change in China's tax policy might affect the company's profitability. The company currently enjoys a 5.0% VAT rebate on its wafer exports.

Table 1: Peers comparison

Company name	Ticker	Fiscal Year end	Mkt Cap (US\$m)	His P/E(x)	Curr-Yr Fwd P/E(x)	Nxt-Yr Fwd P/E(x)	ROE (%)
<b>Ingot and wafer</b>							
Solargiga	757 HK	12/2007	397.6	2.8	6.6	4.9	71.2
SAS	5483 TT	12/2007	346.0	6.0	5.4	5.2	32.6
LDK Solar	LDK US	12/2007	1,554.6	5.0	5.2	3.8	38.4
<b>Solar products</b>							
E-TON Solar	3452 TT	12/2007	246.3	8.2	4.9	4.5	27.4
Motech	6244 TT	12/2007	400.8	5.2	5.2	5.0	25.7
SolarWorld	SWV GR	12/2007	1,865.8	n.a.	9.1	8.0	17.6
Suntech	STP US	12/2007	1,308.5	6.3	8.0	7.8	22.2
Trina Solar	TSL US	12/2007	249.3	2.8	2.9	3.6	13.6
JA Solar	JASO US	12/2007	545.6	9.4	7.8	4.7	18.4
Canadian Solar	CSIQ US	12/2007	170.3	2.9	2.8	4.0	(0.6)
Evergreen Solar	ESLR US	12/2007	407.2	247.0	n.a.	10.2	(6.8)
Fuelcell	FCEL US	10/2007	270.2	n.a.	n.a.	n.a.	(61.2)
ECD	ENER US	06/2008	1,130.2	26.9	12.8	8.3	0.7
Solarfun	SOLF US	12/2007	252.4	7.5	10.9	13.7	8.6
Sunpower – A	SPWRA US	12/2007	2,460.1	36.7	15.3	11.3	1.4

Source: Bloomberg

Table 2: P&amp;L

Year to Dec (RMBm)	05A	06A	07A	1-3Q 06A	1-3Q 07A	1-3Q 08A
Revenue	173.7	413.3	1,015.5	277.7	715.4	1,199.7
Cost of sales	(104.8)	(244.2)	(692.4)	(161.6)	(514.4)	
Gross profit	68.9	169.1	323.1	116.1	201.0	
Other revenue	2.6	5.5	81.6	1.3	79.0	
Other net loss	(0.5)	(1.2)	(8.4)	(0.6)	(3.8)	
Selling and distribution expenses	(0.9)	(2.1)	(4.4)	(1.3)	(2.8)	
Administrative expenses	(7.3)	(15.2)	(47.6)	(10.6)	(23.9)	
Profit from operation	62.8	156.0	344.2	104.9	249.4	449.2
Finance costs	(2.4)	(3.9)	(7.6)	(3.5)	(5.4)	
Profit before taxation	60.4	152.2	336.6	101.4	244.0	
Income tax	(3.4)	(4.0)	(20.6)	(2.6)	(8.4)	
Profit for the period	57.0	148.1	316.0	98.8	235.6	
Attributable to:						
Equity holders of the Company	41.3	109.7	292.2	72.5	211.3	318.1 *
Minority interests	15.7	38.4	23.8	26.3	24.2	
EPS - Basic (RMB)	0.083	0.219	0.582	0.145	0.423	

Source: Company data

Note: \* excluding one-off listing expenses of around RMB11.6m.

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