

# A8 Digital Music



**BUY (unchanged)**

## Wireless sustains growth

### Key points:

- 3Q results show a solid growth in Tencent's and Sina's wireless businesses
- Sustained industry growth, stable operating policies and a healthy operating environment - key reasons behind the improvement
- Telecoms restructuring to benefit both companies in the long term
- Current operating environment will benefit leaders such as A8, whose wireless music products are key drivers to telcos' growth.
- A8's cash per share represents 94.6% of its share price, based on our 3Q projections. BUY, with a target price of HK\$2.60, representing 11.0x FY12/09F P/E.

**Update.** Tencent (700 HK, HK\$46.80) and Sina (SINA US) announced solid 3Q growth in their MVAS businesses. Tencent's MVAS revenue rose 93% YoY to RMB372m. Revenue of 2.5G products jumped 247% YoY to RMB71m and IVR 57% to RMB56m. Sina's revenue from mobile operations rose 63.3% YoY to US\$27m, due to: 1) sustained industry growth; 2) stabilization of operator policies; 3) favourable government regulations and 4) healthy business environment, the company said. It expects the industry's restructuring to improve the overall environment by spurring China Telecom (762 HK, HK\$2.85) and China Unicom (762 HK, HK\$9.81) to actively promote and enhance their value-added services (VAS).

**Our view.** We believe that the operating environment of China's telecom players is healthy and will benefit leaders such as A8. The company's UGC music offering is one of the key drivers of wireless VAS usage in China's mobile community and the latest comments from industry players give us confidence that A8 can meet our FY12/08F earnings forecast of RMB73.5m. We believe that its wireless music products may benefit from Chinese consumers' current "belt tightening", which is prompting a shift from discretionary spending to items/services that provide a high level of satisfaction at a relatively low price.

**Attractive price.** We view the current level as an attractive entry point for the counter. The company now has RMB290.0m in net cash at hand, based on our 3Q projections, representing 94.6% of its market value. We reiterate our BUY call on A8, with a target price of HK\$2.60, representing 11.0x FY12/09F P/E.

## China Technology

Fri, 14 Nov 2008

**Kennedy Tsang/Helena Qiu**

(852) 2533 3713/3709

[kennedytsang/helenaqiu@sbi2capital.com](mailto:kennedytsang/helenaqiu@sbi2capital.com)

### Stock data

Price	HK\$0.78
Target price	HK\$2.60(+233%)
12 mth range	HK\$0.68-2.67
Market cap.	US\$44.7m
Daily t/o, 3 mth	HK\$0.2m
Free float %	21.8%
Ticker	0800.HK/800 HK

### Financial summary

Year to Dec	06A	07A	08F	09F	10F
Turnover (RMBm)	260.1	278.1	650.5	815.2	952.1
Net profit (RMBm)	39.9	55.3	73.5	96.7	117.0
EPS (RMB)	0.089	0.124	0.165	0.217	0.262
EPS Δ %	(4.7)	38.7	33.0	31.6	21.0
P/E (x)	7.9	5.7	4.3	3.2	2.7
P/B (x)	2.5	1.7	0.6	0.5	0.4
EV/EBITDA (x)	3.7	2.9	0.8	1.2	0.2
Yield (%)	-	-	-	-	-
ROE (%)	38.4	36.2	21.9	17.9	18.0
ROCE (%)	45.7	38.6	27.1	21.4	21.4
N. Gear. (%)	cash	cash	Cash	Cash	Cash

### Price Performance

	1 mth	3 mth	12 mth
Relative to FSSTI (%)	+3.0	+2.5	-10.0
Actual price changes (%)	+3.5	+2.0	-8.5

	08F	09F	10F
Consensus EPS (RMB)	0.170	0.217	0.262
Previous forecasts (RMBm)	73.5	96.7	117.0
Previous EPS (RMB)	0.170	0.217	0.262

### Price Chart

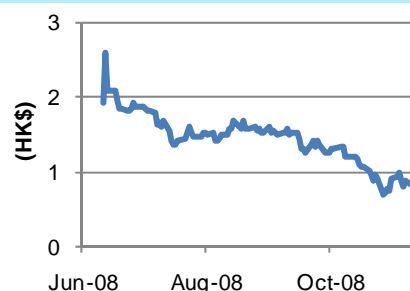


Table 1: Summary P&amp;L

Year to Dec (RMBm)	06A	07A	08F	09F	10F
Revenue					
Music-related	159.3	197.5	496.5	649.5	780.8
Non music related	109.2	88.5	165.4	180.0	188.0
	268.4	286.0	661.9	829.5	968.8
Business tax	(8.3)	(7.9)	(11.4)	(14.3)	(16.7)
Net revenue	260.1	278.1	650.5	815.2	952.1
Cost of services	(127.8)	(149.4)	(388.1)	(496.8)	(595.4)
Gross profit	132.3	128.7	262.4	318.4	356.6
Other income/gains, net	9.7	20.2	4.6	4.9	5.5
Gain from disposal of JCE	-	5.7	-	-	-
Selling & marketing expenses	(67.8)	(67.1)	(120.0)	(149.1)	(165.4)
Administration expenses	(22.4)	(21.7)	(31.2)	(37.2)	(41.3)
Other expenses	(2.8)	(0.1)	(21.5)	(16.5)	(10.6)
Finance costs	(5.0)	(4.9)	(3.8)	(2.0)	(2.0)
Profit/loss from JV	0.6	(0.3)	-	-	-
Tax	(5.3)	(5.2)	(15.1)	(20.1)	(24.3)
Profit after tax	39.3	55.2	75.4	98.4	118.5
Minority interest	0.6	0	(1.9)	(1.7)	(1.5)
Net profit	39.9	55.3	73.5	96.7	117.0

Source: Company data

Disclosure of interest: SBI E2-Capital Securities Limited acted as the sole bookrunner, lead manager and underwriter for the A8 Digital Music Holdings Limited in June 2008.

SBI E2-Capital is a dedicated small/mid cap investment banking/ stockbrokerage house. Find our research on: [sbie2capital.com](http://sbie2capital.com), [thomsononeanalytics.com](http://thomsononeanalytics.com), [factset.com](http://factset.com) and [multex.com](http://multex.com)

**SBI E2-Capital stock ratings:**

**STRONG BUY** : absolute upside of >50% over the next three months

**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

Investors should assume that SBI E2-Capital is seeking or will seek investment banking or other related businesses with the companies in this report.

**Analyst certification:** The views expressed in this report accurately reflect the analyst's personal views of the subject securities and that the analyst has not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

**Disclaimer:** This research report is not an offer to sell or the solicitation of an offer to buy or subscribe for any securities. The securities referred to in this report may not be eligible for sale in some jurisdictions. The information contained in this report has been compiled by the Research Department of SBI E2-Capital Securities Limited ('SBI E2-Capital') from sources that it believes to be reliable but no representation, warranty or guarantee is made or given by SBI E2-Capital or any other person as to its accuracy or completeness. All opinions and estimates expressed in this report are (unless otherwise indicated) entirely those of SBI E2-Capital as of the date of this report only and are subject to change without notice. Neither SBI E2-Capital nor any other person, accepts any liability whatsoever for any loss howsoever arising from any use of this report or its contents or otherwise arising in connection therewith. Each recipient of this report shall be solely responsible for making its own independent investigation of the business, financial condition and prospects of the companies referred to in this report. SBI E2-Capital and their respective officers, directors and employees, including persons involved in the preparation or issuance of this report, may from time to time (1) have positions in, and buy or sell, the securities of companies referred to in this report (or related investments); (2) have a consulting, investment banking or broking relationship with any company referred to in this report; and (3) to the extent permitted under applicable law, have acted upon or used the information contained or referred to in this report including effecting transactions for their own account in an investment (or related investment) in respect of any company referred to in this report, prior to or immediately following its publication. This report may not have been distributed to all recipients at the same time. This report is issued only for the information of and may only be distributed to professional investors and dealers in securities and must not be copied, published, reproduced or redistributed (in whole or in part) by any recipient for any purpose. This report is distributed in Hong Kong by SBI E2-Capital. Any recipient of this report who requires further information regarding any securities referred to in this report should contact the relevant office of SBI E2-Capital located in such recipient's home jurisdiction.

Copyright © SBI E2-Capital Securities Limited 2008. All rights reserved.