

AMD/ATI tie up brings long term opportunities

China Electronics

VST Holdings (856 HK, HK\$1.26)

Not Rated

AMD acquires ATI. On 24 Jul 2007, AMD announced to acquire ATI for US\$5.4b in cash and stock. ATI is the world's largest supplier of graphic processor units (GPUs) and also manufactures chipsets. AMD is a key vendor of VST and accounted for 24% of the company's revenues in FY3/06. The deal provides VST with a number of opportunities, but we believe that these benefits may take time to realize.

Opportunities abound for VST....

- ❑ Distribution of GPUs can potentially strengthen VST's already broad portfolio. With increasing PC penetration and the growing online gaming community in China, there is demand for high-end GPUs in the do-it-yourself (DIY) PC and server markets.
- ❑ The acquisition will enable AMD to accelerate its entry into the chipset market. VST, being AMD's largest distributor in China, is in a good position to gain distributorship for any new chipset products.
- ❑ VST has previously indicated that it intend to extend into the digital TV market. ATI is a top chip supplier to both the high-end/mainstream handset and digital TV end-markets, with customers such as Qualcomm, Motorola, Sony, LG and Samsung. Though we expect VST to have already established presence in China's digital TV market by the time the deal closes, VST can leverage on ATI's high-end products to differentiate itself from other competitors.

Realizing these opportunities will take time....

- ❑ The acquisition deal is expected to close in 4Q 2006.
- ❑ At present, ATI is likely to have its own distribution network in China. It would take some time to consolidate the distribution network and phase out some of the smaller distributors.
- ❑ AMD's chipset products may take some time to develop. Street estimates that a large proportion of ATI's chipset business is currently tied up with Intel while AMD traditionally has aligned itself with Nvidia. The technology partnership realignment would require a certain amount of lead time.

Summary. In all, we expect that VST can benefit from AMD's acquisition with ATI. Securing distributorship of GPUs/chipsets can enhance the company's relationship with AMD. ATI's products are generally high-end, which may provide scope for margin expansion once the distributorship of the new products gain scale. However, material effects to VST in the short-term is limited as the potential benefits of filtering down the value chain will be a lengthy process, 2H FY3/08 at the earliest in our view. Lead time associated includes 1) closing the acquisition deal, 2) roll-out of new integrated products and 3) distribution network consolidation and realignment in China. We maintain our FY3/07F profit forecast of HK\$138.7m (fully diluted EPS: HK\$0.155). The counter is currently trading at 8.1x fully diluted FY3/07F P/E.