

Benefit from power grid investment

Not Rated

Financial summary

Year to Dec	06A	07A	08F	09F	10F
Turnover (RMBm)	600.4	808.5	1,103.2	1,469.2	1,898.5
Net Profit (RMBm)	151.7	212.9	257.8	313.5	383.5
EPS (RMB)	0.220	0.290	0.326	0.396	0.458
EPS Δ%		31.8	12.4	21.5	15.7
P/E (x)	8.9	6.8			
P/B (x)	2.36	1.31			
EV/EBITDA (x)	5.8	3.8			
Yield (%)	3.6	4.3			
ROE (%)	25.9	23.5			
ROCE (%)	19.0	17.6			
N. Gear. (%)	(22.5)	(37.5)			

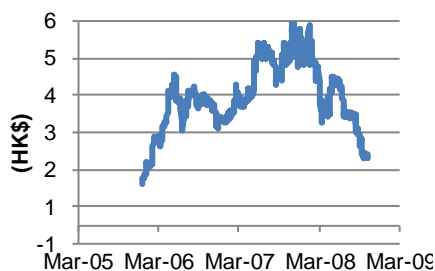
Source: Bloomberg

Price Performance

	1 mth	3 mth	12 mth
Relative to HSI (%)	+9.6	+83.7	+7.5
Actual price changes (%)	+1.6	+62.0	-43.2

	08F	09F	10F
Consensus EPS (RMB)	0.326	0.396	0.458
Previous forecasts (RMBm)	n.a.	n.a.	n.a.
Previous EPS (RMB)	n.a.	n.a.	n.a.

Price Chart


Norman Zhang

(852) 2533 3715

normanzhang@sbie2capital.com

public bids at provincial level. Our survey on 7 rounds of bidding in four provinces shows that procurement for data collection and related products went to 31 companies across the country, of which Wasion, Shenzhen Clou, Ningbo Sanxing, Jiangsu Linyang, Hangzhou Hualong, Holley Metre, Star Power and Wuzhou Minovo take the largest shares. We expect these industry leaders to be the major beneficiaries of SGCC and CSG's total ~RMB100b investment on data collection systems.

Ticker:	3393.HK	12 mth range:	HK\$0.70-4.25
Price:	HK\$1.96	Market cap:	US\$204.3m
Target:	n.a.	Daily t/o, 3 mth:	US\$0.5m
		Free float %:	33.9%

Key points:

- * RMB100bn investment on electricity data collection systems in the coming 2-3 years.
- * Competition confined within a few capable suppliers.
- * Estimated 5-10% market share.
- * Expecting considerable growth in FY12/09F – FY12/11F.
- * Existing capacity fully utilized.
- * New plant to double capacity in 2009.
- * Large working capital requirement to support top line.
- * Undemanding valuation with 5.3x one-year forward P/E.

Demand arising from grid construction. As part of China's RMB4.0tr stimulus package, State Grid Corporation of China (SGCC) plans to spend ~RMB80bn out of total RMB1.0t+ capex budget within the next three years (2009-2011) on building / upgrading its data collection system. We reckon that China Southern Power Grid (CSG) should have some similar plan with an estimated size of ~RMB20b. It is estimated that ~85% of these budgets will transfer into demand for equipment and related systems such as power metres, data collection terminals and power management software.

Table 1: Fixed assets investments from grid companies

(RMBbn)	06A	07A	08A	Future plan
SGCC	189.3	225.4	252.0	Over RMB1,000bn in 2-3 years
CSG	47.1	53.7	64.7	RMB102b in 2009 and RMB130b in 2010

Source: Companies data

Limited number of capable suppliers. In 2005, there were over 3,300 enterprises engaged in producing electrical instrument in China with a total capacity of 80m+ units (sets), including 60m power metres. Nevertheless, we believe only few of them are capable to obtain orders from the grid companies for their data collection systems. Entry barriers, in our view, stand on: 1) R&D facilities to upgrade / release products continuously; 2) system integration ability to provide solution instead of individual product; 3) proven track record and established relationship with grid companies. Normally SGCC and CSG procure equipment via

Table 2: Survey of bidding results*

Company	Bid won (times)	Products involved
Wasion	11	single- / three-phase power metre, management terminal
Ningbo Sanxing	8	single- / three-phase power metre
Shenzhen Clou	7	three-phase power metre, test device / calibrator, management terminal
Hangzhou Hualong	6	single- / three-phase power metre
Jiangsu Linyang	5	single-phase power metre
Star Power	5	Single- / three-phase power metre, test device / calibrator
Holley Metre	4	single-phase power metre
Wuzhou Minovo	4	single- / three-phase power metre
Others	40	
Total	90	

Source: compiled by SBI E2-Capital

Note: note: total 7 rounds of bidding in Shandong (4), Jiangxi (1), Guizhou (1) and Qinghai (1)

Power metre professional. Headquartered in Changsha, Hunan province, Wasion has three main business lines: single-phase power metre (for residential customers), three-phase power metre (for industrial users) and data collection terminals (incl. electricity management software). In IH FY12/08A, the three segments accounted for 51.7%, 23.1% and 25.2% of the total RMB345.5m revenue, respectively.

Est. 5-10% share of whole electricity data collection market. The management estimates it has 20-25% market share for multi-function three-phase power metre and ~5% for single-phase one. In our channel checking, Wasion was named 11 times out of total 90. We reckon the company should have 5-10% of entire electricity data collection market. In fact, the actual market share could be even larger, given that ~60% of investment on electricity data collection system is expected to go to power metres, which is Wasion's core product and on which its competitive strength relies.

Expanding capacity to host growth. Based on the potential investment from SGCC and CSG (~RMB100bn, 85% on equipment and software) and Wasion's estimated 5-10% market share, we calculate the company will have total sales of RMB4.25-8.50bn in the coming three years (2009-2011), implying an average of RMB1.4-2.8b. As existing production capacity has been fully utilized in 2008, the company is building a new manufacturing base ("Wasion Science and Technology Park"). Phase I construction has completed and operation commenced in Aug 2008, which will double its existing capacity in 2009. We think this expansion was necessary and should be sufficient to support the company's near term growth.

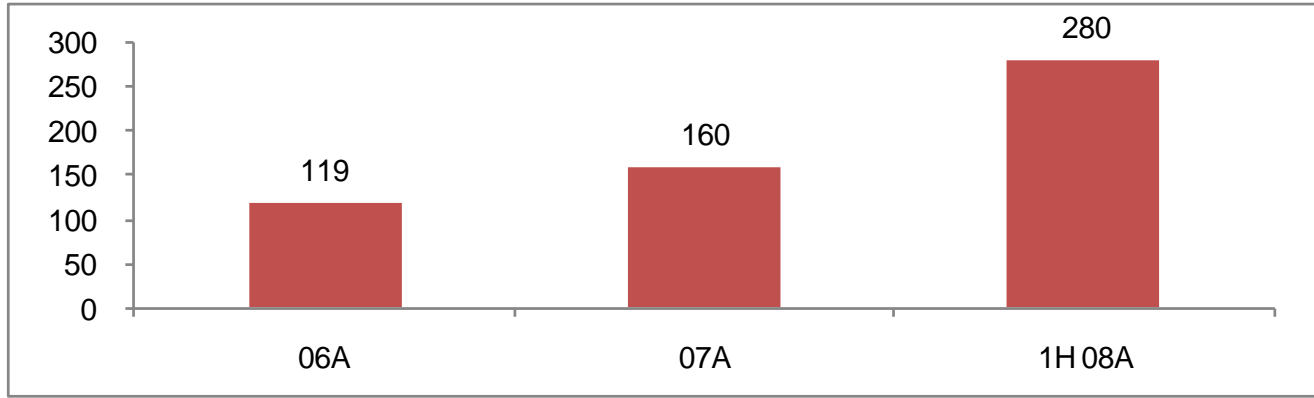
Table 3: Capacity expansion

Year to Dec (RMBm)	07A	08A	09F
Single-phase power metre	2,000.0	3,000.0	5,000.0
Three-phase power metre	600.0	900.0	2,000.0
Data collection terminal	80.0	120.0	500.0

Source: Company data

External financing might be necessary. Cash conversion cycle was 160 days in FY12/07A (280 days in IH FY12/08A), which is mainly due to trade receivables from major customers (i.e. SGCC and CSG). Normally 90% payment is made within around 2-3 months after the final delivery. As revenue is recognized throughout the entire delivery period, which, in turn, is affected and largely determined by the production schedule, effective credit term is prolonged. However, associated default risk associated is low, given SGCC and CSG's state-owned background and special industry position. Wasion booked RMB1.2m impairment loss for bad and doubtful debt in FY12/07A (total receivables: RMB686.4m). Nevertheless, we believe working capital management is critical for top line expansion. Base on current length of cash conversion cycle, we reckon the company will probably need external resource in FY12/09F to fulfill its working capital requirement. At end-Jun 2008, it had RMB194.5m net debt.

Chart 1: Cash conversion cycle (days)



Source: Company data

20%+ growth in FY12/08F. The management guided 20%+ growth on both top and bottom lines for FY12/08F (1H: turnover up 18.4% and earnings up 12.4%), which we think is feasible with the newly added capacity released out in Aug. For FY12/09F, the company is looking for an accelerated growth of at least 30%+ in both top and bottom lines.

Undemanding valuation. We pick four A-share companies, Shenzhen Clou (002121 CH), Holley Metre (600097 CH), Star Power (000676 CH) and Wuzhou Minovo (600873 CH), to construct the peers group together with Wasion. Among the five parties, Wasion enjoys the highest gross margin, which should be largely attributed to its concentration on three-phase power metre. Both the company and Shenzhen Clou have a strong presence in power measurement and management area. The latter is trading at trading at 23.0x one-year forward P/E. Although we agree the investment-oriented high growth will exist only in coming 2-3 years and demand will soon resume its normal level thereafter, Wasion’s present value is nevertheless undemanding. A high single-digit P/E multiple might be more reasonable, in our view, justified by the expected earnings jump shortly.

Corporate governance. The company got listed in Dec 2005 via a public offering at HK\$1.13 per share. Substantial shareholders include Mr. Ji Wei (57.6%), the executive director, chairman and founder of the company, Temasek (5.2%) and Wasatch (5.0%).

Table 4: Peers comparison

Company	Ticker	Fiscal Yr-end	Revenue		Historical P/E (x)	1-Yr P/E (x)	2-Yr P/E (x)	
			(RMBm)	Gross margin (%)				
Wasion	3393	HK	12/2007	808.5	47.4	6.1	5.3	4.4
Star Power	000676	CH	12/2007	878.0	20.2	36.4	n.a.	n.a.
Shenzhen Clou	002121	CH	12/2007	344.5	39.1	34.4	23.0	14.2
Holley Metre	600097	CH	12/2007	213.7	20.1	478.4	n.a.	n.a.
Wuzhou Minovo	600873	CH	12/2007	690.5	22.1	57.8	n.a.	n.a.

Source: Company data

Table 5: P & L

Year to Dec (RMBm)	06A	07A	1H 07A	1H 08A
Turnover	600.4	808.5	291.7	345.5
Cost of sales	(323.2)	(425.1)	(157.2)	(186.9)
Gross profit	277.3	383.4	134.5	158.6
Other revenue	7.2	24.1	5.9	16.9
Administrative expenses	(53.8)	(70.5)	(36.2)	(45.6)
Selling expenses	(50.6)	(68.5)	(27.7)	(37.2)
Research and development expenses	(12.1)	(17.8)	(8.6)	(13.6)
Operating profit	167.9	250.6	67.9	79.1
Finance costs	(9.5)	(17.2)	(6.9)	(8.4)
Profit before taxation	158.4	233.4	61.0	70.7
Income tax expenses	(6.7)	(20.5)	(2.0)	(4.3)
Profit for the period	151.7	212.9	59.1	66.4
Attributable to:				
Equity holders of the Company	151.7	212.9	59.1	66.4
Minority interests				
EPS - Basic (RMB)	0.220	0.290	0.084	0.081
EPS - Diluted (RMB)	0.210	0.280	0.082	0.079
Proposed DPS (RMB)	0.070	0.084		

Source: Company data

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