

Comtec Solar

Satisfactory sales to healthy customer

to summarize...

- Comtec recorded core profit with 10%+ gross margin versus loss-making peers
- Healthy financial position with net-debt-to-equity ratio at 14.4%
- High contribution of n-type wafers up to 74.4% sales in 1H 2012A to SunPower
- Reasonably moderate customer concentration risk of current n-type sales
- Remain BUY. Target price lowered to HK\$1.44 on revised profit estimations

Comtec recorded interim core profit compared to loss-making peers. Comtec Solar announced interim results last Friday. The company recorded RMB456.2m for 1H FY12/12A, with RMB218.5m in Q1 and RMB237.7m in Q2. For the latest interim, gross margin was 12.5%. While there was loss on CB redemption, loss on new warrants, warrants cancellation and other one-off items, unadjusted and adjusted net profit for the period was -RMB121.1m and RMB44.9m. We attribute the higher-than-peers margin to sales of n-type wafers. For instance, Solargiga (0757 HK) reported a revenue of RMB485.0m for 1H FY12/12A with a gross loss of RMB21.9m after excluding one-off inventory write-down of RMB132.8m. Renesola (SOL US) achieved improving gross margin at 0.6% in Q2 excluding one-off items. In fact, both were having around 100% net debt-to-equity by the end of Jun 2012.

Table 1. 1H FY12/12A financial results

RMBm	1H 11A	2H 11A	Q1 12	Q2 12
Revenue	574.7	456.2	218.5	237.7
Gross profit	135.4	56.8	30.3	26.5
Loss on CB and warrants related	0	(151.2)	(170.1)	18.9
Loss on other one-off items	0	(14.8)	0	(14.8)
Reported net profit	101.6	(121.1)	(159.7)	38.6
Adjusted net profit	101.6	44.9	10.4	34.5
Gross margin	23.6%	12.5%	13.9%	11.1%
Adjusted net margin	17.7%	9.8%	4.8%	14.5%

Source: SBI E2-Capital

Healthy financial position with net-debt-to-equity ratio at 14.4%. By the end of Jun 2012, Comtec had RMB411.0m short-term bank loan, RMB20.7m long-term bank loan and RMB162.5m outstanding CB. With RMB135.8m pledged cash and RMB244.1m cash, net debt to equity ratio was low at 14.4%, in our view. On the other hand, inventory and total receivables were RMB278.7m and RMB264.3m by end of Jun 2012, equivalent to 127 days and 105 days. The figures were higher than that in 2011 partly due to increased sales volume to 218.6MW for 1H 12A from 109.4MW a year ago and increased sales to existing customers, in our view.

High contribution of n-type wafers up to 74.4% sales in 1H 2012A to SunPower. Comtec indicated that sales to the largest customer in Philippines with n-type wafers accounted for as much as 74.4% revenue for the period. The management believed that although customer concentration was higher than normal, it was their strategy to focus on limited number of customers with sound financial positions. According to our channel checks, the largest customer is SunPower (SPWR US), which has cell fabrication plants in Philippines currently under consolidation in its efforts to reduce manufacturing costs. We take closer look into SunPower financial performance to access Comtec's counterparty risk as well as customer concentration risk.

Ticker	0712 HK
Rating	BUY
Price (HK\$)	0.67
Target Price (HK\$)	1.44 (+115%)
12m Price Range (HK\$)	0.63 - 1.81
Market cap. (US\$m)	97.4
Daily t/o (US\$m)	0.11
Free float (%)	36.6

Financial summary

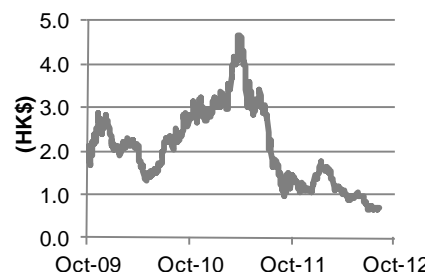
Year to Dec	10A	11A	12F	13F	14F
Turnover (RMBm)	1,021	1,017	990	1,300	1,656
Re.Net Profit (RMBm)	223	(46)	(82)	159	200
EPS (RMB)	0.210	(0.041)	(0.066)	0.129	0.163
P/E (x)	4.8	n.a.	n.a.	4.2	3.4
P/B (x)	0.7	0.7	0.4	0.4	0.3
EV/EBITDA (x)	3.1	9.1	8.5	2.3	1.9
Yield (%)	2.2	0.0	-1.2	2.4	3.0
ROE (%)	17.3	(2.9)	(5.1)	9.6	11.0
ROCE (%)	19.5	1.3	(1.9)	11.0	12.1
N. Gear. (%)	Cash	Cash	2.0	17.3	22.9

Source: SBI E2

	12F	13F	14F
Consensus EPS (RMB)	(0.02)	0.096	0.135
Previous earnings (RMBm)	60.2	201.9	240.1
Previous EPS (RMB)	0.049	0.164	0.196

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	(7.7)	(31.5)	(60.7)
Actual price changes (%)	(8.2)	(26.4)	(61.9)



Source: Bloomberg

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Reasonably moderate customer concentration risk of current n-type sales. As of RMB456m revenue in 1H FY12/12A, 74.6% was sales to SunPower, which accounted for almost all of Comtec n-type wafer sales. This heavy reliance on one particular customer may present high counterparty risk due to high customer concentration. Table 2 shows our quick assessment of SunPower financial position. By end of Jun 2012, SunPower had consolidated 2 fabrication plants in Philippines with capacity ramping-up from 680MW to 1,200MW in next 1 to 2 years. For the latest 6-month interim by Jun end by non-GAAP standard, revenue was US\$1,231m with improved gross margin of 13.9%. Operating income was US\$26.0m compared to loss-making in previous quarters. It was partly due to their effective cost reduction program upon plants consolidation. By end of Jun, their total debt (including CB and bank loans) was US\$835m with US\$376m cash on hands. As such, their net debt-to-equity ratio was still at satisfactory level of 39.5%. That said, as a major client of Comtec, we believe SunPower is to keep itself floating with certain profit and moderate financial health during this late stage of industry consolidation.

Table 2. Comtec reliance on SunPower in 1H 2012A and SunPower's key financial figures

	1H FY12/12A
<u>Comtec Solar</u>	
Total revenue	RMB456m
Revenue of n-type wafers	RMB340m
Revenue to SunPower in Philippines	RMB339m
<u>SunPower</u>	
Market capitalization	US\$721m
Capacity	Ramping-up from 680MW to 1,200MW
Total revenue (non-GAAP)	US\$1,231m
Gross margin (non-GAAP)	13.9%
Operating income (non-GAAP)	US\$26.0m
Total debt (CB plus bank loan)	US\$835m
Total cash (cash on hands plus pledged cash)	US\$376m
Net debt-to-equity ratio	39.5%

Source: SBI E2-Capital

Comtec outlook for 2H 2012F neutral-to-positive. Comtec has been outperforming its peers in latest quarters, and its outlook of 2H is generally neutral-to-positive, maintaining our view that it is bottoming-out in mid of the year. With potentially stable gross margin of 10% to 15% in 2H due to general price stability of polysilicon, there is potential for improvement in volume in 2H. While Comtec continued to emphasize on counterparty risk with limited number of customers in short-term, sales of n-type wafers may continue to support higher utilization of its 600MW capacity. With 100-120MW wafer sales in 1H, the number may go up to 200MW+ with 66%+ utilization. Furthermore, Sanyo (6764 JP) is another potential n-type customer for Comtec. Comtec targets to receive approval by the end of the year. According to our channel checks, Panasonic (6752 JP), parent company of Sanyo, planned to establish a new solar manufacturing plant of 300MW in Malaysia after Sanyo closing Californian solar facility earlier this March. Comtec may relocate or bargain purchase certain equipments in Malaysia or in China to meet the demand. Nevertheless, if everything goes smoothly it is only to be reflected in 2013F.

Target price further lowered to HK\$1.44 from HK\$2.02 partly on reduced earnings from 2013F onwards. Despite profitability and sustainability of Comtec, solar industry consolidation due to decrease in ASP is complicated with trade wars among major countries. While we continue to believe that at least Comtec is bottoming out in mid of the year, the prolonged consolidation does not provide quick recovery and slightly revise down our estimation from 2013F onwards. The counter is currently trading at 0.40x P/B based on RMB1,572m net equity FY12/12F. We revise our Target Price to HK\$1.44 from HK\$2.02 on lowered profit forecast in the next 2 years based on 14.9x and 8.4x P/E for FY12/12F and FY12/13F based on adjusted net profit of RMB84.8m and RMB158.9m respectively. Remained BUY.

Table 3. Revised selected key operational data on half-yearly basis

	1H FY12/11A	2H FY12/11A	1H FY12/12F	2H 12/12F
Nameplate capacity MW	600	600	600	600
Shipment MW	109	113	135	220
Revenue (RMBm)	575	442	456	534
Overall gross margin	24%	-10%	12.5%	17.6%
Overall net margin	18%	-33%	-27%	8%
Net profit (RMBm)	101.6	(147.9)	(121.1)	44.4
EPS (RMB)	0.090	(0.130)	(0.107)	0.039
Adjusted net profit (RMBm)	101.6	(12.5)	44.9	44.4

Source: SBI E2-Capital

Table 4. Profit and loss forecast (Full-year)

RMB m	FY12/10A	FY12/11A	FY12/12F	FY12/13F	FY12/14F
Revenue	1,021.4	1,016.7	790.4	1,257.6	1,493.6
Cost of sales	(690.8)	(924.3)	(670.5)	(938.8)	(1,111.2)
Gross profit / loss	330.6	92.5	119.9	318.8	382.5
Other income	26.6	40.1	0.0	0.0	0.0
Other expenses	(9.1)	(61.4)	0.0	0.0	0.0
Selling and distribution expenses	(1.8)	(1.8)	(1.6)	(2.5)	(3.0)
Administrative expenses	(75.8)	(48.7)	(39.5)	(62.9)	(74.7)
EBIT	270.5	20.6	78.8	253.4	304.8
Finance Costs	(7.4)	(38.6)	(5.8)	(8.6)	(13.7)
EBT	263.1	(18.0)	73.0	244.8	291.1
Income tax expenses	(40.2)	(28.3)	(12.8)	(42.8)	(50.9)
Reported profit for the year	222.9	(46.3)	60.2	201.9	240.1
Reported EPS (RMB)	0.210	(0.041)	0.049	0.164	0.196
Adjusted net profit	222.9	155.1	89.4	158.9	199.8

Table 5. Selected balance sheet items

RMB m	FY12/10A	FY12/11A	FY12/12F	FY12/13F	FY12/14F
Non-current assets	1,136	1,324	1,206	1,593	1,910
Property, plant and equipment	716	856	763	1,150	1,468
Other non-current assets	420	469	442	442	442
Current assets	777	1,330	949	861	941
Inventories	248	218	253	290	325
Trade and other receivables	155	214	271	303	329
Cash and cash equivalent	294	746	313	158	176
Other current assets	80	152	111	111	111
Non-current liability	4	484	164	177	190
CB	0	402	122	134	148
Other non-current liabilities	4	81	42	42	42
Current liabilities	397	517	413	541	749
Trade and other payables	194	199	213	241	299
Short-term bank loans	170	318	200	300	450
Other current liabilities	33	0	0	0	0
Total Equity	1,511	1,654	1,577	1,736	1,912

Source: SBI E2-Capital

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