

Comtec Solar

Bottoming out in mid of the year

to summarize...

- Japan embraced new FiT which should represents household IRR of 10%
- Demand from Japan, US, Germany and China should stabilize solar market
- Survivors such as Comtec should indirect benefit from bottoming out
- Q1 gross margin of Comtec was already better than peers at 13.9%
- Target price stays at HK\$2.02. Remain BUY

What's new? This weekend, Japan approved re-starting two nuclear reactors despite mass public opposition. At the same time, the government embraced the proposals put forward in April, offering PV system owners ¥42 (US\$0.53) per kWh from July this year in an uncapped manner, while wind energy will be subsidized at about half that of solar. Last year, Japan ranked sixth worldwide for solar installations, adding 1.3GW for a total capacity of 5GW. Japan's goal is to boost total renewable generation by 30GW+ over next decade to 12% of total generation.

Implication. A FiT of US\$0.53 per kWh in Japan is among the highest in the World, compared to Germany's latest reduction to US\$0.17-\$0.26 depending on size and ~RMB1 in China. Although Japan's solar system cost can be stunningly high at almost US\$6.3 per W compared to as low as US\$2.7 per W in Germany and US\$2.4 per W in China, with assumption of 20 years life with 4 sun-hours a day for 330 days a year, IRR for household in Japan can still be 10% under our estimation. According to Bloomberg New Energy Finance, solar system addition in Japan this year is expected to be 3.2 to 4.7GW compared to 1.3GW in 2011. Earlier this month, Solar Energy Industries Association and GTM Research raised a target for US in 2012F to 3.3GW. Together with 3.5GW target in Germany, the top 3 counties may contribute 10GW in 2012F with potential surprise from China. As discussed earlier, the effect of smaller Europe demand (Italy and German alone accounted for 50% installation of 24GW in 2011A) will be at least partly offset by rising US, Japan and China.

Table 1. Actual figures for FY12/11A and previous estimates

	Japan	China case1	China case2
FIT / reference tariff (US\$)	0.531	0.159	0.079
Life of PV project (years)	20	20	20
Number of sun hours a year (hours)	1320	1320	1320
System cost (US\$ per W)	6.300	2.381	1.190
IRR	10.7%	7.0%	7.0%

Source: SBI E2-Capital

Valuation. Japan market is largely closed to foreign manufacturers and developers today. Yet, the latest scheme apparently applies to all domestic and foreign players. The government claims to be primarily interested in fostering a flourishing renewable market with supporting domestic players such as Sharp (6753 JP), Panasonic (6752 JP), Kyocera (6971 JP) and Solar Frontier is a distant secondary concern. While Comtec can indirectly benefit from this FiT with apparently increasing module imports to 19% of Japan market in 2011A from 0% in 2008A on NPD Solarbuzz data, we remain cautious and earnings forecast for Comtec stay the same for now. The counter is currently trading at 17.4x and 5.2x P/E based on our profit forecast for FY12/12F and FY12/13F on fully diluted basis. Remain BUY with target price at HK\$2.02.

Ticker	0712 HK
Rating	BUY
Price (HK\$)	1.05
Target Price (HK\$)	2.02 (+92.4%)
12m Price Range (HK\$)	0.85 - 3.54
Market cap. (US\$m)	152.6
Daily t/o (US\$m)	0.24
Free float (%)	36.6

Financial summary

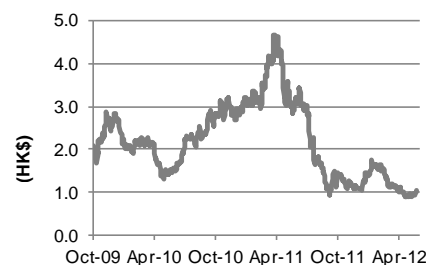
Year to Dec	10A	11A	12F	13F	14F
Turnover (RMBm)	1,021	1,017	790	1,258	1,494
Net Profit (RMBm)	223	(46)	60	202	240
EPS (RMB)	0.210	(0.041)	0.049	0.164	0.196
P/E (x)	4.8	n.a.	17.4	5.2	4.4
P/B (x)	0.7	0.7	0.6	0.5	0.5
EV/EBITDA (x)	3.1	9.1	2.1	1.6	1.5
Yield (%)	2.2	0.0	0.6	1.9	2.3
ROE (%)	17.3	(2.9)	3.7	12.0	12.7
ROCE (%)	19.5	1.3	7.2	17.0	16.3
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Source: SBI E2

	12F	13F	14F
Consensus EPS (RMB)	0.05	0.136	0.137
Previous earnings (RMBm)	56.2	199.8	240.1
Previous EPS (RMB)	0.046	0.163	0.196

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	13.9	(16.7)	(60.4)
Actual price changes (%)	16.7	(23.4)	(64.5)



Source: Bloomberg

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Q1 results. Comtec announced Q1 key data earlier late May. Revenue came at RMB218.5m with gross margin of 13.9%. While the company incurs other losses of RMB170.1m in relation to repurchase of CB and new warrants, reported net loss was RMB159.7m. That said, adjusted net profit for the quarter was RMB10.4m. While Q1 this year continued to be difficult for the whole solar industry, Comtec Solar in fact outperformed its peers with 13.9% gross margin compared to high single digit margin. In addition, revenue was high at RMB218.5m compared to our estimation of RMB311.1m for 1H this year. The management indicated that though they placed higher priority on counter-party risk control over sales target, strong demand from healthy customers especially for its n-type wafers contributed to relatively good ASP and volume for the last quarter. We maintain our profit forecast as follow.

Table 2. 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)
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

Table 3. Selected balance sheet items

RMB m	FY12/10A	FY12/11A	FY12/12F	FY12/13F	FY12/14F
Non-current assets	1,136	1,324	910	1,237	1,595
Property, plant and equipment	716	856	765	1,153	1,585
Other non-current assets	420	469	145	83	10
Current assets	777	1,330	1,059	976	885
Inventories	248	218	134	188	194
Trade and other receivables	155	214	144	215	235
Cash and cash equivalent	294	746	715	505	381
Other current assets	80	152	66	69	75
Non-current liability	4	484	136	142	144
CB	0	402	101	101	101
Other non-current liabilities	4	81	35	41	43
Current liabilities	397	517	239	297	343
Trade and other payables	194	199	138	193	198
Short-term bank loans	170	318	100	100	140
Other current liabilities	33	0	1	4	5
Total Equity	1,511	1,654	1,594	1,774	1,994

Source: SBI E2-Capital

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