Corporate Flash

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GDC: Uniqueness deserves premium

Recommendation: BUY (initiating coverage) — China Media

Price	HK$3.21
Target price	HK$4.30 (+34%)
12 mth range	HK$0.20-3.70
Market cap.	US$537.8m
Daily t/o, 3 mth	US$1.35m
Free float %	34.4%
Ticker	8271.HK/8271 HK

Year to Dec	Net profit HK$m	EPS HK$	EPS Δ %	P/E x	P/B x	EV/EBITDA x	Yield %	ROE %	ROCE %	N. Gear. %
05A	(76.4)	(0.095)	42.4	(33.7)	na	na	-	na	na	na
06A	(30.2)	(0.038)	60.4	(85.0)	na	na	-	na	na	na
07F	73.8	0.078	na	40.9	na	61.9	-	14.5	9.3	300.1
08F	159.4	0.122	55.5	26.3	50.4	17.9	-	20.0	14.0	73.4
09F	257.1	0.197	61.4	16.3	12.3	11.3	-	19.8	14.8	Cash

Relative to Hang Seng Index (1 mth, 3 mth, 12 mth): +11.3%, +60.2%, +704.1%
Actual price changes (1 mth, 3 mth, 12 mth): +20.0%, +82.3%, +1,037.9%

Key points:

- Strategic partnership with China Film Group will effectively make GDC the largest cinema network operator in China with around 75% market share.
- Potential growth of the Chinese cinema industry is often overlooked. Box office grew at a 3-year CAGR of 35.7% totaling RMB2.6b in 2006.
- Demographics of cinema goers suggest that it is a direct proxy to the China consumption story and emerging middle class consumers.
- GDC is a leading digital cinema server supplier with 16% market share worldwide and 68% in Asia. Supply issues of a larger competitor may potentially open up opportunities for GDC to gain further market share.
- Media plays that own a nationwide media distribution platform in China traditionally trade at a significant premium to comparables. Furthermore, the stock is a proxy to several emerging trends including: 1) growing box office in China; 2) emerging middle class consumers in China; 3) digitalisation of cinemas worldwide and 4) CG outsourcing trend to low cost countries such as China.
- We like GDC for the scarcity of its assets and unique synergistic combination of business segments. We initiate coverage with a BUY call and a target price of HK$4.30, representing 35.0x FY12/08F P/E. Comparables are presently trading at an average of 42.9x 1-year forward P/E on consensus basis.

Business model. Global Digital Creations (GDC) is a multimedia and animation services and solutions provider focusing on the global cinema industry. It is engaged in the following four main lines of business: 1) digital cinema network operator; 2) provision of digital cinema solutions; 3) computer generated (CG) content creation and 4) CG professional training. The company was listed on the GEM Board of HKEx in Aug 2003.

1) Digital cinema network operator

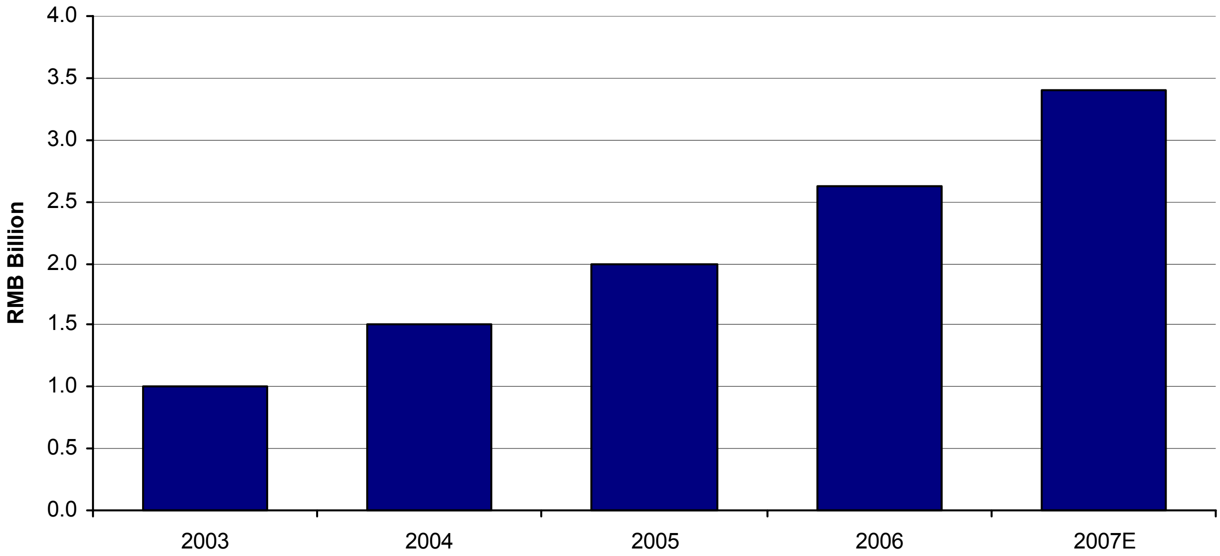
Strategic partnership with China Film Group to transform China's cinema industry. GDC will partner with China Film Group (CFG) to install, and operate digital cinema systems, based on the Hollywood-backed Digital Cinema Initiatives (DCI) standard, for the top 2,000 cinema screens in China in terms of revenue for a period of 10 years. Management estimates that the top 2,000 screens accounts for around 75% of box office receipts in China. GDC will provide network monitoring, content distribution management, technical support and maintenance services. The agreement is significant as CFG is China's biggest film production and distribution company and is wholly-owned by the State Administration of Radio Film and Television (SARFT). CFG has a tremendous amount of influence on China's cinema industry given that it has both administration and censorship powers as well as dominant distribution position. We estimate that CFG accounts for the distribution of over 70% of Chinese film titles and around 45% of foreign film titles in China.

Agreement signed. The agreement for the strategic partnership was announced in Nov 2006 and signed on 31 May 2007 via a signing ceremony between China Film Group and GDC's 51.49% majority stakeholder Shougang Grand (730 HK, HK$1.01, NR). Once Shougang has set up all necessary legal entities, the full rights will be transferred over to GDC. Given that GDC has an aggressive rollout schedule aimed at fully capturing the opportunities from 2008 Beijing Olympics, the company needed to rely on Shougang as its have both the expertise and connections to expedite quickly both the JV set up and required licenses. At present, we expect that the full rights will be transferred to GDC by Aug 2007.

GDC has emerged as the default supplier of digital cinema equipment in China. Similar to the overall movie industry, CFG has been trialing digital cinema systems in China since around 2002. From an initial 4 suppliers, it has now dwindled to 2 (one of which is GDC). With GDC now in a JV with CFG, the company has emerged as the defacto monopoly supplier of digital cinema systems on the Mainland. According to our channel checks, GDC has an estimated 90% market share in China.

Why cinema operations in China? The cinema industry in China is a market that offers tremendous growth, which is often overlooked. According to SARFT, China's box office has been growing at a 3-year CAGR of 35.7% totaling RMB2.6b in 2006, of which approximately 45% is from foreign films and 55% from domestic films. Despite having a population of over 1.3b, China's box office is only a fraction of the US$9.5b (RMB73.2b) recorded in the US in 2006, while India's box office for the first 6 months of 2007 was estimated at US$188m (RMB1.4b). China's box office is expected to grow at a rate of around 25-30% annually for the foreseeable future, faster than both the US and India. Interestingly, ticket price in China is not low. In general, ticket prices is around RMB60-80 compared to HK$50-70 in Hong Kong. This means that the cinema industry is a direct proxy to the China consumption story as well as the emergence of the Chinese middle class.

Chart 1: China cinema box office



Source: SARFT

Instant formation of high entry barrier. Given that GDC will control around 75% of China's cinema distribution market, the company will have first mover advantage and effectively become the monopoly player in the industry. The landmark agreement will instantly give GDC, access to: 1) film content; 2) operating scale and 3) distribution reach. Therefore, any would be competitor would face significant hurdles to enter the market. Moreover, as GDC is the market leader of the provision of digital cinema solutions in Asia (See section titled *"Provision of digital cinema solutions"* below), even in the event that a second license was issued to operate digital cinema networks on the Mainland, GDC will be in a position to constrain supply of digital equipment to the potential competitor and hence, restrict their growth and level of potential threat to GDC's cinema operation network.

Rapid rollout schedule of digital cinema equipment. GDC aims to install 700 sets of digital equipment by the end of this year, and the full 2,000 by end of Mar 2008. The company has commenced deployment since 1 Jul 2007, where they were able to take advantage of CEPA and receive exemption on the current 14.0% import duty on import of its digital cinema distribution servers into China. Based on our discussions with the management, GDC is scheduling to install 6 sets of systems in Jul, followed by 50 sets in Aug, and ramping up to 150 sets per month by Oct. Our channel checks suggests that this installation schedule is achievable given that it only takes 2 engineers around one day to install each set in an existing cinema complex. The time can be further accelerated if it is installed as part of a construction of a new cinema complex. Currently, the GDC has already signed agreements to install around two thirds of the targeted 700 screens for 2007. The signing of such agreements requires assistance from CFG to both approach and negotiate with the respective cinema operators. However, being a stakeholder in the JV, the interests have been aligned and we do not expect significant execution risks.

Partnership with leading visualization solutions provider Barco is a reflection of GDC's bargaining power. In Feb 2007, GDC entered into agreements with Barco, whereby Barco will provide: 1) development services and 2) supply DLP Cinema projectors for the development of GDC's integrated projection system for China and the rest of the world. The Belgium-based company is a world leader in display and visualization solutions, offering digital cinema solutions from digital mastering to premier quality feature film screenings. In the digital cinema market, Barco is one of only three licensees of the Texas Instruments DLP Cinema technology. GDC was able to secure such an agreement as it had bargaining power from its China digital cinema network operations as well as its leading position as a distributor of digital cinema servers worldwide. Moreover, one of Barco's main competitors, Christie, had at the time just secured a large order for supplying digital projectors in the US. Thus, Barco needs GDC's support to maintain their digital projector market share and to keep pace with Christie. To take advantage of the CEPA tax incentives, GDC's integrated projection system incorporates Barco's projectors into a single unit solution. Otherwise, the Barco projectors would be subject to import duties. The partnership is on an ongoing basis and GDC has already locked in the supply of the 700 sets of projectors for its China operations from Barco, so we do not expect component supply to hamper the digital cinema system project roll out in China.

Profit sharing with CFG and cinema operator. GDC will undertake the cinema network operations through a profit sharing agreement with CFG and the cinema operator. Currently in the industry, box office receipts are split as to 50% cinema operator, 30% production house and 20% distributor (CFG). GDC will take a cut of the receipts from both the cinema operator and the distributor. After deducting administration costs to CFG, we estimate that GDC can capture around RMB0.08 per Renminbi of box office receipt. Once the business is fully ramped up, we estimate that gross margins could be in the region of 50%. In our view, the business model is extremely lean. Marketing costs are minimal, while G&A costs can also be relatively well controlled given that monitoring and distribution of content can be more centralized with the aid of the digital distribution system. To minimize technology switching costs, and avoid resistance from cinema operators, the company plans to "finance" transition to digital cinema by installing the system up-front and receiving payment through the profit sharing arrangement. The cost of the server equipment will be amortised over a 10-year period.

Table 1: GDC's cinema operations profit sharing model

Description	% of box office receipt	RMB
Box Office Receipt		1.00
Cinema	50.0%	0.50
Producer	30.0%	0.30
Distributor (CFG)	20.0%	0.20
GDC proportion of cinema (10.0% of cinema share)	5.0%	0.05
GDC proportion of distributor (CFG) (25.0% of distributor share)	5.0%	0.05
Administration costs to cinema (5.0%) and distributor (CFG) (30.0%)		(0.02)
GDC revenue	**8.3%**	**0.08**

Source: Company data, SBI E2-Capital

Digital cinema is a platform for greater potential. We see the digital cinema network as a platform, whose value can be further unlocked. The "off site" screening of the 2006 World Cup in Germany was an unexpected success, allowing people without access to stadium tickets to participate in the event. We believe that going forward, the Chinese government may explore the possible use of the digital cinema platform for the re-broadcasting of nationwide and cultural events to the general community.

Ad spend on cinema media platform is significantly underdeveloped, but has tremendous opportunities. Traditionally, advertising revenues from the cinema is underdeveloped at around 0.4% of worldwide ad spend in 2005 and significantly trails other medium. In our view, this is primarily due to the archaic and inflexible distribution system and the difficulties associated with coordinating the broadcasting of advertising. The lack of a proper infrastructure means that advertising clients have a hard time finding the appropriate distribution channels. Note that on other media platforms such as newspaper and magazines, advertising revenues typically account for around 70.0-80.0% of overall revenues. This metric is even higher, at 90.0%+ on platforms such as the Internet and TV. Despite the nascent situation, the advantages that cinema in-screen advertising offers is intriguing. The nature of the cinema essentially locks movie goers into a captive environment and audience are often focus on the advertising message with minimal interruptions. This leads to a reach rate upwards of 90.0%. In addition, China's movie going population are young consumers that are well educated with higher income. This is often the target audience of many fast moving consumer goods (FMCG) and luxury good products. GDC has the technological expertise and channels to capture emerging advertising opportunities and we believe that the company will look to break into this revenue stream once the cinema network is established.

Table 2: 2005 worldwide ad spend by media

Media type	Ad spend (US$m)	Percentage of total
Cinema	1,697	0.4%
Internet	18,712	4.7%
Outdoor	21,769	5.4%
Radio	34,348	8.6%
Magazine	52,992	13.3%
Newspaper	119,171	29.8%
TV	151187	37.8%
Total	**399,876**	**100.0%**

Source: Zenith Optimedia

Table 3: Characteristics of China's movie going population

Characteristics	Remarks
High income earners	73% of China's movie goers annual income is above US$3,000, well above the GDP per capital of around US$1,700
Young age	Average age of China's movie goers is 29.2. 82.6% between 18-40 years old.
Well educated	67% with university degrees, 92.3% are high school graduates or above
Highly concentrated	6,546m shows sessions and 1.43b movie goers in China in 2005

Source: Company data

2) Provision of digital cinema solutions

Leading solutions provider of digital cinema technology. The company is a leading provider of digital cinema distribution technology in the world through 56.25%-owned subsidiary GDC Technology. The subsidiary has R&D and marketing facilities in Singapore, Hong Kong, China and the US. Digital cinema distribution entails the centralized distribution of digital content from a remote server to cinemas equipped with processing servers and customized digital projectors. The content can be distributed via physical hard drives, satellite and/or the Internet. GDC's digital distribution standard is developed as part of the Digital Cinema Initiatives (DCI), a consortium of Hollywood studios and vendors including: *Buena Vista Group (Disney)*, *20th Century Fox*, *MGM*, *Paramount Pictures*, *Sony Pictures Entertainment* amongst others. The standard has been earmarked as the defacto standard on which all next generation cinema will be based on. GDC is already one of the world's leading providers and has a technology edge as it was: 1) World's first server provider to upgrade to DCI MXF format (Jul 2005) and 2) one of only three digital cinema equipment providers to meet full DCI compliance (Mar 2007).

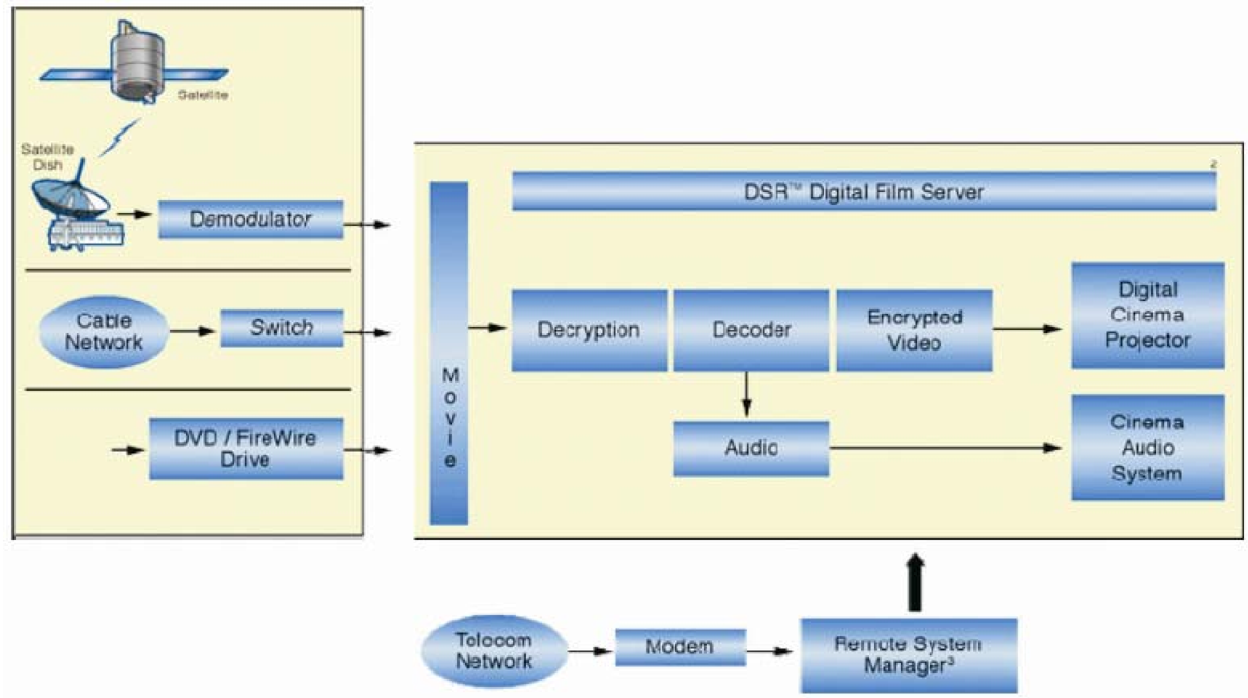
DCI paving way for global transition to digital cinema. The DCI standard has taken several years to develop and was formally released in Apr 2007. The cinema industry has been traditionally slow to make its transition to digital and the release of the standard is a major milestone given that it solidified the industry's commitment. The cinema industry still derives the bulk of their revenues from box office receipts and the roll out of next generation digital cinema will provide a platform for production houses and cinema operators to diversify their revenue streams, introduce more flexible scheduling (based on demand) and improve distribution security. Moreover, with vendor/production interests aligned, we are unlikely to see a standards war that is occurring in the next generation DVD space.

Table 4: Digital cinema advantages

Digital cinema advantages
Viewer advantages
- Better picture and sound quality (same clarity from first to last screening)
Distributor/producer advantages
- Better control of content distribution
- More flexible management of content and advertising
- Increased protection of IPR through advanced encryption
- Enables small producers to distribute their content effectively
- Lower cost of print production and content distribution
Theatre operator advantages
- Allows theatres to show more content than just movies
- Increased operating efficiency for chain operators and improves scalability

Source: Company data and SBI E2-Capital

Chart 2: Digital cinema architecture



Source: Company data and SBI E2-Capital

Already an established brand overseas, with significant market share. GDC's current installed base in North America presently includes the famous Graumans Chinese Theatre in Los Angeles, as well as Mann Glendale Market Place and Pacific Sherman Oaks cinema complexes in the US. The company's systems are also installed in various cinema complexes in Korea, Netherlands, Hong Kong, Singapore and India. According to "www.dcinematoday.com" and several manufacturers' websites, the company is the second largest provider, with a 16% global market share in digital cinema servers, while in Asia, it is the largest provider with a 68% market share. We note however, that the largest provider Doremi, has only one single customer (in the US) and has only been in the industry for just over one year. Meanwhile, several smaller players have since exited the market. In our view, this would open up opportunities for GDC to further extend their market share going forward. There is presently an installed base of over 550 digital servers globally.

Table 5: GDC's cinema operations profit sharing model

Worldwide	Market share (%)	Asia	Market share (%)
Doremi	55	GDC	68
GDC	16	Quvis	20
Quvis	9	Avica	7
XDC	9	XDC	3
Dolby	6	Dolby	2
Avica	4	Kodak	0
Kodak	1	Doremi	0
Total	100	Total	100

Note: Quvis, Avica and XDC have since exited market

Source: Company data, SBI E2-Capital

Digital cinema standard can deter piracy. The digital cinema solution offered by GDC can deter piracy. The measures include: 1) coding encryption; 2) forensic marking and 3) control on number of times the movie is played and the period for which it can be played. Furthermore, it is our understanding that the refresh rate of the screen is slightly different from standard consumer video equipment, which means that any pirated material will suffer from a significant deterioration in quality. With China facing increasing pressure from the global community to address piracy and international property rights, solutions such as those offered by GDC will be received favouably.

Digital cinema servers a US$3.0b addressable market. Based on information from independent industry researchers Digital Cinema Report and Scenic Wonders Inc, there are presently around 200,000 first run screens worldwide, representing an addressable market for digital cinema servers of around US$3.0b. We estimate that the upgrade process will take around 6-7 years to complete.

Digital cinema servers a US$3.0b addressable market. Given its strong market share, GDC will also be able to benefit from the worldwide transition of digital cinema server systems. Based on information from independent industry researchers Digital Cinema Report and Scenic Wonders Inc, there are presently around 200,000 first run screens worldwide, representing an addressable market for digital cinema servers of around US$3.0b. We estimate that the upgrade process will take around 6-7 years to complete. Meanwhile in China, digital cinema screens are projected to surge from 186 in 2005 to 2,500 in 2009 and 7,000 in 2015. Management aims to sell on average 2,000-4,000 sets/year of digital cinema solutions or servers commencing FY12/08F. ASP for the solutions ranges from US$12,000 (server) to US$65,000 (integrated solutions). We expect this segment to form a steady cash cow for the company once the worldwide switching process reaches overdrive and estimate that the company would be able to derive around HK$700.0-1,000.0m in revenues from FY12/08F onwards. Management has already prepared for the production ramp up by setting up assembly facilities in both Hong Kong and Shenzhen. GDC will procure the component parts and conduct the core-assembly of the solution in-house. The company is currently in talks with several large scale cinema chains in the US to roll-out their solutions.

Stumbles by main competitor may further open up opportunities for GDC. As mentioned previously, Doremi is GDC's main competitor in the digital cinema servers arena. Despite possessing more market share, the company only has one contract, that being an installation contract with US-based AccessIT, to roll out digital cinema servers in the US. However, Doremi's limited time in this industry may be starting to show as our checks suggest that they may be facing supply issues and unable to meet the demands of AccessIT. This stumble by Doremi may potentially open the door for GDC to further gain ground on its rival.

3) CG content creation

GDC already a leader in CG animation in China. GDC's fully owned subsidiary, IDMT, is already a leading CG animation developer in China. Last year, the company released China's first full length CG animation film "Thru the Moebius Strip", while its "Legend of Shangri-la (Peach Blossom Valley)" was a first place winner at Tokyo Broadcasting System's DigiCon 6+2 Gold Award. Typically, the script, director and voice-overs for the animation feature are sourced from overseas while the animation is produced in China. The company has a 300 strong animation team based in Shenzhen.

Outsourcing for North American-based animation film studios. The company is presently conducting outsourcing work for several North American-based animation film studios. According to the management, they have approximately HK$60.0m contracts on hand for the remainder for FY12/07F. To further leverage the strength of their cinema network in China, GDC is presently in talks with the animation studios to secure the cinema distribution rights in China for those OEM contracts that are currently in hand. After only 5 CG film releases in 2005, this number swelled to 13 in 2006. For the first six months of 2007, 6 CG films have already been released. With increasing competition among CG animation films, we expect the Hollywood studios to increasingly outsource parts of their film production to low cost centres such as China and demand for services offered by GDC to increase. However, we continue to expect revenue stream in this segment to be lumpy going forward, given that OEM contracts are typically one-off and that the company is still working on developing a stable pipeline of CG animation projects.

4) CG training

Training centres both a funnel for talent and profit centre. Together with CG creation, GDC's subsidiary IDMT also runs a series of training centres. At present, the company has 2 self-operated centres, located in Shenzhen and Shanghai, while operating another four centres under a franchise model. The flagship centres in Shenzhen and Shanghai has been established for around 9 years, and leveraging the IDMT brand name, has built up a leading reputation in the industry. The training centres typically charges around RMB28,000-33,000 for a nine month programme, which are amongst the highest in the industry. In our view, GDC can command above industry training fees given that: 1) students showing good potential can gain employment with IDMT after the completion of the training course; 2) the training course uses both software and training material that are commonly adopted by major Hollywood studios and 3) the strong brand name and reputation of IDMT. Thus, the training centre both acts as a talent pool for IDMT, ensuring that they continue to attract the best animators, as well as a self sustaining profit centre. Though there are other training programmes available on the market, the quality and reputation of the programme, as well as the opportunity to gain employment with one of China's largest CG animation companies, will allow the training centre to sufficiently differentiate from its competitors.

Chinese government encouraging the development of CG industry. The CG industry is an area of focus for the Chinese government as it seeks encourage the development of service based industries on the Mainland. The government is actively promoting the development of the CG industry in China by encouraging: 1) foreign investment; 2) training of high-end talent and 3) developing a complete value chain. We expect these initiatives to significantly drive up demand for CG animators going forward. Demand for animators significantly outstrips supply. According to a survey by China Television Artist Association, there were around 7,000-10,000 animation artists in China in the middle of 2006, while demand is estimated at around 150,000. Furthermore, the CG industry represents alternative training for Chinese youths who are not able to gain tertiary education. According to the Vice President of the Ministry of Education, China's university entry rate was around 23% in 2006. While this percentage is expected to increase going forward, demand for alternative forms of post-high school training, such as CG animation, is expected to remain high.

GDC looking to ramp up training centres. Recognising this demand for training services, GDC will be looking to set up more training centres. The company set up 4 centres under a franchise model in mid 2006, but its strategy will be to establish more self operated training centres going forward. Management indicates that self operated centres are preferred as they have better control over the quality of the courses and the overall learning environment.

Earning and valuation

FY12/06A and 1Q FY12/07A results. For FY12/06A, GDC recorded a HK$30.2m net loss on a turnover of HK$54.9m. The bulk of the turnover was derived from its CG animation business, amounting to HK$30.4m, with the release of "Thru the Moebius Strip". In 1Q FY12/07A, revenue increased 128.1% YoY to HK$19.7m. Digital cinema solution sales contributed HK$8.6m (43.7%), CG creation HK$8.4m (42.5%) and training fees HK$2.2m (11.1%). At present, we are not expecting digital solutions sales to ramp up until 3Q FY12/07 as the company only launched its integrated solution at the end of 2Q FY12/07. Boosted by a one-off gain of HK$40.3m for the 27.0% disposal of subsidiary GDC Technology to Li Ka-shing, net profit came in at HK$45.1m, reversing a net loss of HK$10.2m a year ago.

FY12/07F and FY12/08F estimates. We expect a turnaround in FY12/07 followed by an explosive FY12/08 as both its digital cinema network operations and sales of digital cinema production reach critical mass. We estimate FY12/07F and FY12/08F net profit to come in HK$33.5m (excluding the HK$40.3m one-off gain) and HK$159.4m respectively, on a turnover of HK$523.56m and HK$1,029.3m. For FY12/07F, we expect sales of digital solutions to be the main top line contributor with around HK$429.8m. However, for FY12/08F we see cinema network operation to deliver around HK$200.9m and solutions sales of around HK$748.4m. Note that our preliminary estimates do not include any contribution from cinema advertising, which we expect will boost top line as well as margins.

Table 6: Revenue breakdown

Year to Dec (HK$m)	05A	06A	07F	08F	09F
Cinema network operation	-	-	28.1	191.8	342.5
Sale of digital solutions	19.1	12.8	429.8	748.4	809.9
CG creation	19.1	27.4	54.6	73.7	92.1
CG training	7.2	9.1	11.0	15.4	20.0
Receipts from distribution of digital motion pictures	-	2.9	-	-	-
Technical service income	0.9	2.2	-	-	-
Rental income from equipment leasing	0.1	0.4	-	-	-
Turnover	32.2	54.9	523.5	1,029.3	1,264.6
% chg		*70.5*	*853.6*	*96.7*	*22.9*

Source: SBI E2-Capital

Initiate coverage with BUY call, target price HK$4.30. GDC is one a handful of media plays that owns a nationwide media distribution platform. Others being Phoenix TV (8002 HK, HK$1.91, NR) and TOM Group (2383 HK, HK$0.85, NR). Given the scarcity of these assets, these media plays traditionally trade at a significant premium. With GDC's other synergistic business segments, the company can tap several emerging trends and industries including: 1) growing box office in China; 2) emerging middle class consumers in China; 3) worldwide roll out of digital cinema systems and 4) increasing CG outsourcing by North American studios to low cost countries such as China. This unique combination of assets deserves a valuation premium in our view. We initiate coverage on GDC with a target price of HK$4.30, representing 35.0x FY12/08F P/E (fully diluted including the top up placing shares). Relative to other China related media plays, the company is undervalued currently trading at 26.3x FY12/08F P/E (fully diluted). We are expecting further re-rating catalysts as the rollout of its China cinema operation network takes shape and as the investment community increases its investing focuses on the media sector leading up to the 2008 Beijing Olympics.

Corporate governance issues. Shougang Grand is the largest shareholder with a 51.5% stake in the company. Other substantial shareholders include Keywise Capital (7.7%), Credit Suisse (3.3%) and Li Kashing (3.1%), while public shareholders account for around 45.4%. The company was listed on the GEM Board in 2003. Deloitte has been GDC's auditor since Mar 2005. Prior to this, the auditor was PricewaterhouseCoopers.

Corporate actions. The company has undertaken a number of corporate actions in 2007. These include: 1) the top up placing of 120m shares and the subscription of 100m new shares by Shougang Grand at HK$0.54 on 16 Mar 2007; 2) the placing of 30m shares by largest Shougang Grand at HK$1.20 on 30 Mar 2007; 3) top up placing of 105m shares at HK$1.61 per share at 2 May 2007 and 4) top up placing of 72m shares at HK$2.70 on 4 Jul 2007.

Risks. 1) delays to rollout of digital cinema network in China; 2) price competition in digital cinema servers worldwide; 3) new entrants in the digital cinema server business; 4) supply constraints from suppliers such as Barco;5) access to capital to fund network rollout and 6) low liquidity in trading of the stock.

Table 7: P&L

Year to Dec (HK$m)	05A	06A	07F	08F	09F
Turnover	32.2	54.9	523.5	1,029.3	1,264.6
Cost of sales	(34.8)	(30.1)	(361.7)	(648.8)	(771.9)
Allowance for production work in progress	(24.7)	-	-	-	-
Gross profit	(27.4)	24.8	161.8	380.5	492.7
Other income and gains	0.6	1.1	12.0	15.0	16.5
Selling and distribution costs	(2.0)	(6.5)	(57.0)	(107.9)	(113.0)
Administrative expenses	(37.4)	(38.4)	(42.1)	(58.1)	(60.9)
Impairment losses recognized in respect of PPE	(2.4)	-	-	-	-
Finance costs	(7.7)	(13.1)	(11.0)	(13.2)	(15.8)
Exceptionals	-	1.8	40.3	-	-
Profit/(loss) before taxation	(76.2)	(30.2)	103.9	216.3	319.4
Taxation	(0.2)	-	(10.5)	(23.3)	(28.8)
Profit/(loss) after tax	(76.4)	(30.2)	93.4	193.1	290.6
Minority interests	-	-	(19.6)	(33.7)	(33.5)
Profit/(loss) attributable to shareholders	(76.4)	(30.2)	73.8	159.4	257.1
% chg	*41.8*	*60.5*	-	*116.0*	*61.3*
Dividends	-	-	-	-	-

Source: Company data

Table 8: Peer comparison

Company name	Ticker	Market Cap (US$m)	Last Price (Local)	P/E (x) Historical	Current	1-yr Fwd	ROE (%)
New Media							
Tencent	700 HK	8,183.4	35.85	57.9	47.9	33.9	32.0
Sina	SINA US	305.4	44.96	59.9	46.2	32.8	11.3
Sohu	SOHU US	1,136.6	32.14	47.5	40.9	27.0	18.1
Focus Media	FMCN US	4,639.5	44.45	47.3	30.5	22.4	16.6
Average				*53.1*	*41.4*	*29.0*	*19.5*
Media							
Phoenix TV	8002 HK	1,194.8	1.91	41.9	41.1	36.3	19.7
TOM Group	2383 HK	418.1	0.85	102.4	168.0	49.4	1.1
Average				*72.2*	*104.5*	*42.9*	*10.4*
GDC	8271 HK	539.7	3.21	n/a	51.0*	26.3*	n/a

*Note: " * " based on fully diluted EPS*

Source: SBI E2-Capital

Disclosure of interests: SBI E2-Capital Securities Ltd. acted as the sole bookrunner and placing agent for the GDC top-up placement of 72.0m shares at HK$2.70 per share on 4 July 2007.

P & L (HK$m)	05A	06A	07F	08F	09F
Year to Dec					
Turnover	**32.2**	**54.9**	**523.5**	**1,029.3**	**1,264.6**
% chg	*(32.9)*	*70.6*	*853.2*	*96.6*	*22.9*
Gross profit	(27.4)	24.8	161.8	380.5	492.7
EBITDA	(62.6)	(15.0)	71.7	256.7	389.0
Depre./amort.	(4.3)	(5.1)	(9.1)	(42.1)	(70.2)
EBIT	(66.8)	(20.1)	62.6	214.5	318.8
Net int. income/(exp.)	(7.0)	(12.0)	1.0	1.8	0.7
Exceptionals	(2.4)	1.8	40.3	-	-
Associates	-	-	-	-	-
Jointly-controlled entit.	-	-	-	-	-
Pre-tax profit	**(76.2)**	**(30.2)**	**103.9**	**216.3**	**319.4**
Tax	(0.2)	-	(10.5)	(23.3)	(28.8)
Minority interests	-	-	(19.6)	(33.7)	(33.5)
Net profit	**(76.4)**	**(30.2)**	**73.8**	**159.4**	**257.1**
% chg	*(41.8)*	*(60.4)*	*n/a*	*116.0*	*61.4*
Dividends	-	-	-	-	-
Retained earnings	(76.4)	(30.2)	73.8	159.4	257.1
EPS (HK$) - Basic	(0.095)	(0.038)	0.078	0.122	0.197
EPS (HK$) - F.D.	(0.095)	(0.038)	0.063	0.122	0.197
DPS (HK$)	-	-	-	-	-
No. sh.s o/s (m) - W.A.	793.2	800.8	800.8	941.0	1,306.9
No. sh.s o/s (m) - Y.E.	800.8	800.8	800.8	1,306.9	1,306.9
No. sh.s o/s (m) - F.D.	793.2	800.8	800.8	1,176.2	1,306.9
Margins (%)					
Gross	*(85.0)*	*45.1*	*30.9*	*37.0*	*39.0*
EBITDA	*(194.3)*	*(27.3)*	*13.7*	*24.9*	*30.8*
EBIT	*(207.6)*	*(36.5)*	*12.0*	*20.8*	*25.2*
Pre-tax	*(236.7)*	*(55.1)*	*19.9*	*21.0*	*25.3*
Net	*(237.2)*	*(55.1)*	*14.1*	*15.5*	*20.3*

Balance Sheet (HK$m)	05A	06A	07F	08F	09F
Year to Dec					
Fixed assets	6.3	4.9	214.2	577.6	663.4
Intangible assets	-	-	-	-	-
Other LT assets	-	-	-	-	-
Cash	20.1	8.6	19.1	10.6	97.4
Accounts receivable	3.7	6.1	78.5	123.5	151.7
Other receivables	2.1	3.7	26.2	36.0	44.3
Inventories	1.2	2.5	36.2	64.9	77.2
Due from related co.s	-	-	-	-	-
Other current assets	-	-	-	-	-
Total assets	**33.4**	**25.7**	**374.2**	**812.7**	**1,034.0**
Accounts payable	(1.1)	(2.8)	(72.3)	(113.5)	(135.1)
Other payable	(23.6)	(29.3)	(27.1)	(48.7)	(57.9)
Tax payable	-	-	(1.1)	(2.3)	(2.9)
Due to related co.s	(7.6)	(4.1)	(54.3)	(81.1)	(96.5)
ST debts	(105.4)	(31.0)	(15.5)	(20.1)	(24.2)
Other current liab.	(21.5)	(20.8)	(10.0)	(10.0)	(10.0)
LT debts	(1.9)	(92.7)	(250.0)	(400.0)	(280.0)
Other LT liabilities	(1.5)	(0.5)	(0.5)	(0.5)	(0.5)
Total liabilities	**(162.5)**	**(181.2)**	**(430.7)**	**(676.2)**	**(607.0)**
Share capital	8.0	8.0	13.1	13.1	13.1
Reserves	(136.2)	(163.0)	(89.3)	70.1	327.3
Shareholders' funds	**(128.2)**	**(155.0)**	**(76.2)**	**83.2**	**340.3**
Minority interest	-	-	19.6	53.3	86.8
Total	**(128.2)**	**(155.0)**	**(56.6)**	**136.5**	**427.1**
Capital employed	(20.9)	(31.4)	208.9	556.6	731.2
Net (debt)/cash	(87.1)	(115.1)	(246.4)	(409.5)	(206.8)

Cash Flow (HK$m)	05A	06A	07F	08F	09F
Year to Dec					
EBIT	(66.8)	(20.1)	62.6	214.5	318.8
Depre./amort.	4.3	5.1	9.1	42.1	70.2
Net int. paid	(7.0)	(12.0)	1.0	1.8	0.7
Tax paid	(0.2)	-	(10.5)	(23.3)	(28.8)
Others	36.3	18.0	14.0	18.0	22.0
Gross cashflow	**(33.4)**	**(8.9)**	**76.2**	**253.2**	**382.8**
Chgs. in working cap.	27.8	0.6	(61.3)	(20.8)	(18.0)
Operating cashflow	**(5.7)**	**(8.3)**	**15.9**	**232.3**	**364.8**
Capex	(0.4)	(2.1)	(218.4)	(405.6)	(156.0)
Free cashflow	**(6.1)**	**(10.4)**	**(202.5)**	**(173.3)**	**208.8**
Dividends paid	-	-	-	-	-
Net distribution to MI	-	-	(19.6)	(33.7)	(33.5)
Investments	(14.5)	-	-	-	-
Disposals	0.1	2.3	3.0	5.0	5.0
New shares	-	-	447.0	-	-
Others	9.9	(19.8)	(359.2)	38.8	22.4
Net cashflow	**(10.5)**	**(27.9)**	**(131.3)**	**(163.1)**	**202.7**
Net (debt)/cash - Beg.	(76.6)	(87.1)	(115.1)	(246.4)	(409.5)
Net (debt)/cash - End.	(87.1)	(115.1)	(246.4)	(409.5)	(206.8)

Interim Results (HK$m)	05A	06A
Six months to Jun		
Turnover	**10.3**	**18.3**
% chg	*n/a*	*77.5*
Profit from operations	(17.3)	(12.7)
Interest expenses	(3.4)	(6.2)
Associates	-	-
Jointly-controlled entit.	-	-
Pre-tax profit	**(20.7)**	**(18.8)**
Tax	(0.4)	-
Minority interests	-	-
Net profit	**(21.1)**	**(18.8)**
% chg	*n/a*	*n/a*
EPS (HK$) - Basic	(0.026)	(0.024)
DPS (HK$)	-	-

Shareholding Structure	Shares o/s (m)	%
Shougang Grand	656.8	51.5
Keywise Capital	97.8	7.7
Credit Suisse	41.7	3.3
Publiic	479.3	37.6
Total	**1,275.6**	**100.0**

Background

SGDC is a multimedia and animation services and solutions provider focusing on the global cinema industry. It is engaged in 1) digital cinema network operator in China; 2) provision of digital cinema solutiosn; 3) CG content creation and 4) CG professional training

Key Ratios	05A	06A	07F	08F	09F
Net gearing (%)	na	na	na	300.1	73.4
Net ROE (%)	na	na	na	4,565.5	121.4
EBIT ROCE (%)	na	na	70.6	56.1	49.5
Dividend payout (%)	-	-	-	-	-
Effective tax rate (%)	-	-	10.1	10.8	9.0
Net interest coverage (x)	na	na	na	na	na
A/R turnover (days)	122.9	32.4	29.5	35.8	39.7
A/P turnover (days)	68.5	13.0	26.2	33.0	35.9
Stock turnover (days)	20.5	22.0	19.5	28.4	33.6