

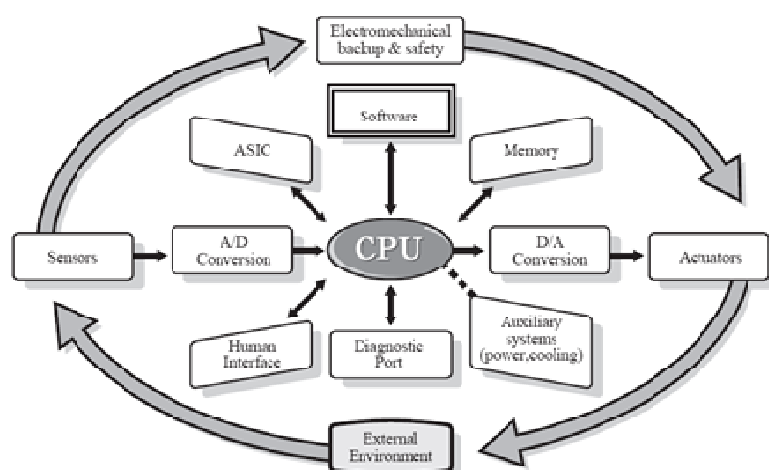
Intelligent machine

Key points:

- Robust EIP market
- China's leading player after Intel and Motorola
- Poised to capitalize on growth in the energy, railway and environment sectors in FY12/08F
- Overseas expansion accelerates
- Service outsourcing base being built in Jiangsu

Product overview. The embedded intelligent platform (EIP) is an industrial computer system designed to perform a particular task. It can be employed with other equipment to form an automation system. Cheaper and smaller than general industrial computer systems, EIP has been widely adopted despite its lower flexibility. The global EIP market increased 11.9% to near US\$59.3bn in 2007, according to Annual Research Report on China's EIP Market 2007-2008 by CCID Consulting (CCID).

Chart 1: Typical embedded system organization



Source: Company data

Robust demand. We expect China's industrialization drive to create huge demand for automation equipment, including EIP. Since EIPs are widely used in different areas, we believe the country's total fixed asset investment (FAI) is a good indicator for the demand. In 1-3Q 2008, China's urban FAI reached RMB9,987.1m, including RMB2,218.0m for equipment, up 32.6% YoY. With the recent RMB4.0tr stimulus package, we expect FAI to increase further in 2009 and 2010. According to CCID, China's EIP market expanded 15.3% in 2007 to RMB5.1bn and is anticipated to grow at a 13.2% CAGR from 2007 to 2012.

China Industrials

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Norman Zhang

(852) 2533 3715

normanzhang@sbie2capital.com

Stock data

Price	HK\$0.93
Target price	n.a.
12 mth range	HK\$0.68-2.15
Market cap.	US\$129.0m
Daily t/o, 3 mth	<US\$0.1m
Free float %	27.1%
Ticker	8285.HK/8285 HK

Financial summary

Year to Dec	05A	06A	07A
Turnover (RMBm)	233.4	278.6	602.6
Net Profit (RMBm)	45.1	82.0	154.4
EPS (RMB)	0.044	0.080	0.125
EPS Δ%		81.8	56.3
P/E (x)	18.7	10.2	6.5
P/B (x)	3.05	2.37	1.43
EV/EBITDA (x)	14.0	7.5	4.2
Yield (%)			
ROE (%)	15.5	24.6	31.0
ROCE (%)	49.7	73.3	47.3
N. Gear. (%)	Cash	Cash	Cash

Price Performance

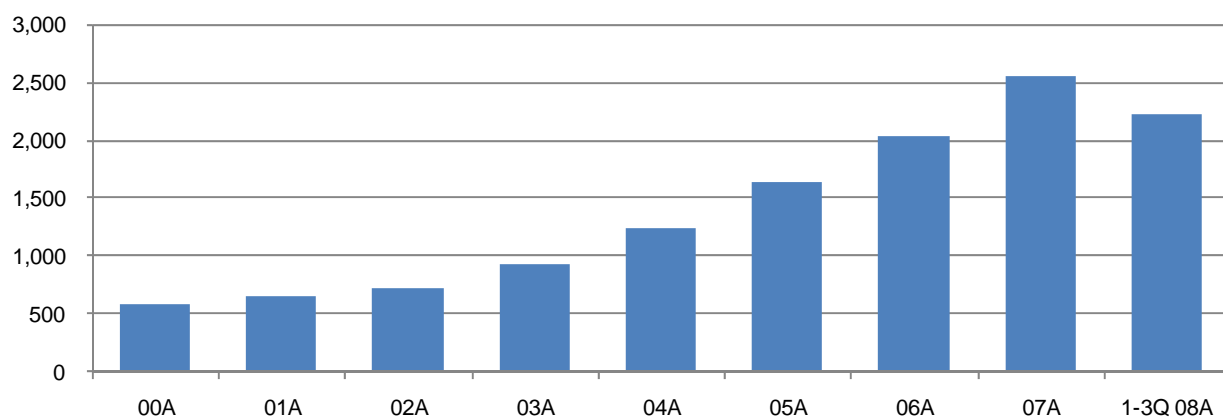
	1 mth	3 mth	12 mth
Relative to HSI (%)	-10.0	+39.7	-0.1
Actual price changes (%)	-3.1	-9.7	-50.5

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

Price Chart



Chart 2: China's FAI in equipment in urban areas (RMBbn)



Source: the National Bureau of Statistics

EVOC's strengths. EVOC is China's leading EIP supplier with 6.3% of the market in 2006, after Intel (27.4%) and Motorola (17.1%). We believe its major competitive advantages include:

- Strong brand equity – reliability and stability are important in an automation system. Customers prefer familiar and well-known brands.
- Extensive product portfolio – the company has over 300 modules, which can be used to construct different system tailored to customer needs.

1-3Q results. Turnover increased 149.9% to RMB771.2m in 1-3Q FY12/08A. The gross margin narrowed from 42.8% to 26.8% so that net profit increased only 33.4% to RMB101.3m. Instead of pure EIPs, the company started offering total solutions to some clients, incurring extra costs due to sourcing components from outside (booked under other items in revenue with the gross margin of 6.0%). Excluding this, turnover rose 51.9% to RMB469.0m, while the gross margin narrowed slightly to 38.1%, based on our calculation. In 3Q, top line rose 128.4% to RMB351.8m. The slowdown was mainly due to lower contribution from the component sourcing / reselling operation. Bottom line maintained growth at 34.3% to reach RMB59.0m.

Outlook. The company has a diversified client base from sectors such as automation equipment, finance, system integration, etc. In addition to its organic market expansion, we expect extra growth from the energy, railway and environment sectors, as the company is:

- qualified supplier of EIPs used in IC card systems of gas stations - oil companies began intelligitizing gas stations in 2003. With China's 100,000 gas stations, we estimate total demand for EIPs at RMB1.4bn (every station needs two EIPs with the ASP of RMB7,000 each).
- major supplier of automatic fair collection, anti-collision and other control systems for subways in Beijing, Guangzhou and Shenzhen - sales from this segment will double in 2008 from the 2007 level of RMB43.1m, according to the management.
- supplier of some environmental protection products such as systems to monitor lake pollution - management expects some major growth in this division in 2008.

Overseas expansion. EVOC entered the overseas market in 2H FY12/07 via local agents. Overseas revenue, mainly from the US and Germany, represented around 5.0% of the total in FY12/07A. With its expansion in Russia, India and other countries, the management expects overseas business to ramp up rapidly.

Other plans. In Sep 2007, EVOC acquired 51.0% in Jiang Nan Da Shi Jie (JNDSJ) for RMB717.9m via a connected transaction. JNDSJ owns 518,564sqm of land in Wuxi where it is building a service outsourcing base with support from the local government. Phase I, which will be put into operation by end-2008, will also house the company's research centre and some production facilities. Most facilities will be leased to third parties (mainly service outsourcing companies).

Corporate governance. The company was listed on the Hong Kong Stock Exchange in 2003. Mr. Chen Zhilie is its controlling shareholder with a 68.2% stake.

Valuation. The counter is trading at 6.5x P/E historically. It had a minor net debt of RMB29.9m at end-Jun 2008.

Table 1: P&L

Year to Dec (RMBm)	05A	06A	07A	1-3Q 07A	1-3Q 08A
Turnover	233.4	278.6	602.6	308.6	771.2
Cost of sales	(143.0)	(162.8)	(371.0)	(176.5)	(564.5)
Gross profit	90.5	115.8	231.7	132.1	206.7
Other income	14.8	23.4	19.9	11.8	39.1
Valuation gains on investment properties		27.6	0.0	0.0	
Selling and distribution costs	(21.7)	(23.0)	(39.9)	(25.7)	(39.3)
Administrative expenses	(11.0)	(9.8)	(30.3)	(14.5)	(33.5)
Other operating expenses	(23.9)	(20.3)	(36.9)	(20.0)	(38.4)
Finance costs	(0.1)	(0.0)	(12.2)	(3.9)	(33.2)
Profit before taxation	48.5	86.0	159.8	79.8	101.3
Income tax	(3.4)	(4.0)	(5.4)	(3.8)	(8.5)
Profit for the period	45.1	82.0	154.4	76.0	92.8
Attributable to:					
Equity holders for the company	45.1	82.0	154.4	76.0	101.3
Minority interest		(0.0)	0.0	0.0	(8.5)
EPS - Basic (RMB)	0.044	0.080	0.125	0.062	0.075

Source: Company data

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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

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