

Comtec Solar System Group (712.HK)

Differentiation leading better future!

Bloomberg | Reuters | POEMS

712.HK | 0712.HK | 712.HK

Industry: Clean Energy--PV

Phillip Securities Research Pte Ltd

26 March 2012

Report type: Result review and forecast

TP:\$1.57 CP:\$1.31 RATE:ACCUMULATE

Company Overview

Comtec Solar System Group is a manufacturer of PV silicon rods, silicon ingots and wafer, mainly engaged in the design, development, manufacture and sale of solar wafer. Comtec got stable performance during the period of industry recession and shows the considerable ability to against macro-economy risk.

Summary

Comtec's performance increased significantly during the report period, both of gross profit and net profit showed considerable growth. Although the whole industry is still in recession, Comtec's overall performance has been showing the momentum of bottoming out, and we estimate that the trend will be continue.

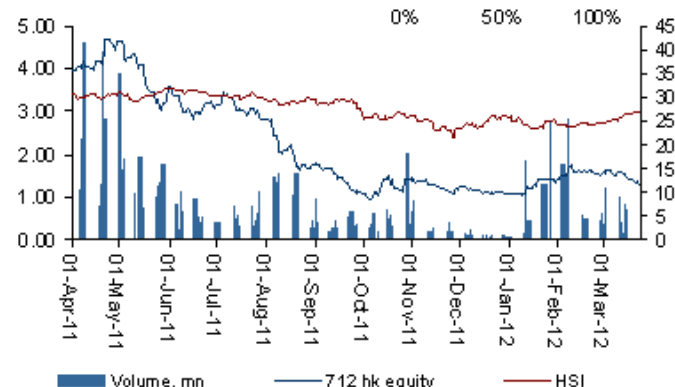
We believe that the effects of product renovation on performance increasing and avoiding excessive competition are obvious. Under the situation of fierce competition, the differentiation strategy could improve the competitive advantage of Comtec. As increase of proportion of new product, the performance will be improved constantly.

The product capacity will be increase in the first half of 2012. With stable customer base, the major part of product capacity could consume by them, plus the subsidiary from the government, Comtec could avoid loss even in the toughest time.

We estimate that the EPS of 2011 will be CNY 0.31, and considering the growth rate of Comtec, the EPS of 2012 could reach CNY 0.37 or HKD 0.45. The target price in the following 12 months is HKD 1.57 under 3.5x P/E we estimated. So the rating is "Accumulate".

Comtec

Rating	2.00	Accumulate
- Previous Rating	N/A	Not Rated
Target Price (HKD)	1.57	
- Previous Target Price (HKD)	N/A	
Closing Price (HKD)	1.31	
Expected Capital Gains (%)	18.0%	
Expected Dividend Yield (%)	0.0%	
Expected Total Return (%)	18.0%	
RawBeta (Past 2yrs weekly data)	1.50	
Market Cap. (HKD bn)	1,485	
Enterprise Value (HKD mn)	1,283	
52 week range (HKD)	0.94 - 4.8	
Closing Price in 52 week range		



Key Financial Summary

FYE	12/10	12/11E	12/12E	12/13E
Revenue (RMB mn)	1,021	1,328	1,527	1,756
Net Profit, adj. (RMB mn)	223	1,328	1,527	1,756
EPS, adj. (RMB)	0.21	0.31	0.37	0.43
P/E (X), adj.	5.0	3.4	2.9	2.5
BVPS (RMB)	1.33	2.26	2.56	2.82
P/B (X)	0.8	0.5	0.4	0.4
DPS (HKD)	0.00	0.00	0.00	0.00
Div. Yield (%)	0.0%	0.0%	0.0%	0.0%

Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

Valuation Method

DCF (WACC: 8.6%; terminal g: 1%)

Analyst

Phillip Research Team

+65 65311240

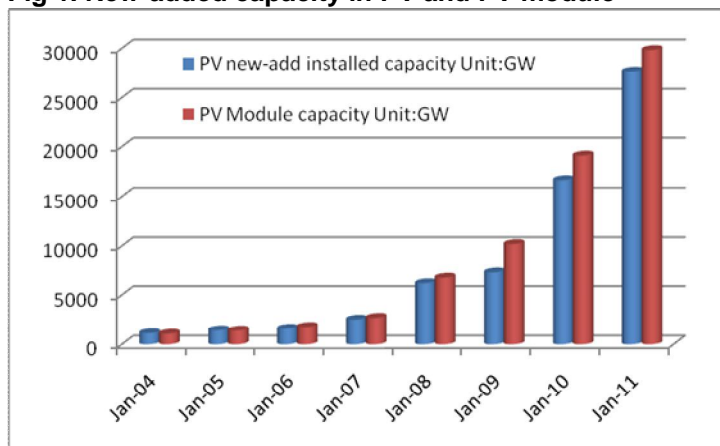
+65 63367607

research@phillip.com.sg

1. The differentiation in PV upstream companies

Overcapacity is a common problem faced by all upstream companies in PV industry. Although the global PV new-added installed capacity has been increasing as well as the demand of upstream products, the new-added capacity of PV cells and modules are also showed sharp increase in the past 2 years. By comparing the growth rate of the two parts, the absolute value of later one is far more than the former. So even the PV industry is recovering, the overcapacity will last for a relative long time. So we estimate that the operation environment for these upstream companies won't be better immediately and the situation of recession will last.

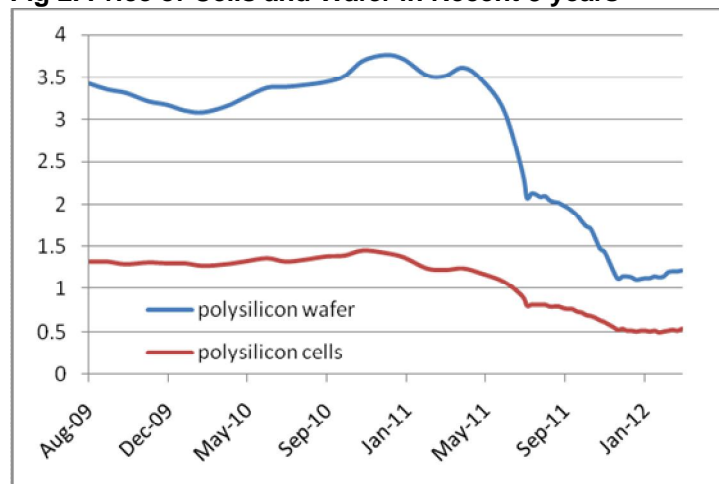
Fig 1. New-added capacity in PV and PV module



(Source: Bloomberg)

From the industry internal structure, the trend of differentiation in PV upstream companies is obvious. The reasons of this phenomenon are: 1) the fierce competition resulted from overcapacity compressed the profit margin, and made operation environment of some small-scale companies worse and worse, even to the edge of bankruptcy. Besides, the overcapacity compressed the price of most products, especially in the domestic market; the price of solar wafer is declined about 50% from 2009. 2) After a continuous decline, the price of polysilicon is stable at present, which means upstream companies may encounter the increase of cost in the future. Although the increase rate won't be too much, it will still make the market situation tougher. Generally speaking, the survival of the fittest in PV industry is inevitable definitely.

Fig 2. Price of Cells and Wafer in Recent 3 years



(Source: Bloomberg)

The nature of the PV industry is monopolistic competition, so firms in PV industry could get competitive advantage by following strategies: 1) the firm could use price war and scale advantage to increase market shares. But because of the reasons stated above, the possibility and space for price reduction is limited. 2) The firm could research and develop special product to avoid the competition in homogeneous product. Because the most product in PV industry is homogeneous and their conversion efficiency could be further improved, so the firm could provide higher conversion efficiency product could get priority in this industry reshuffle.

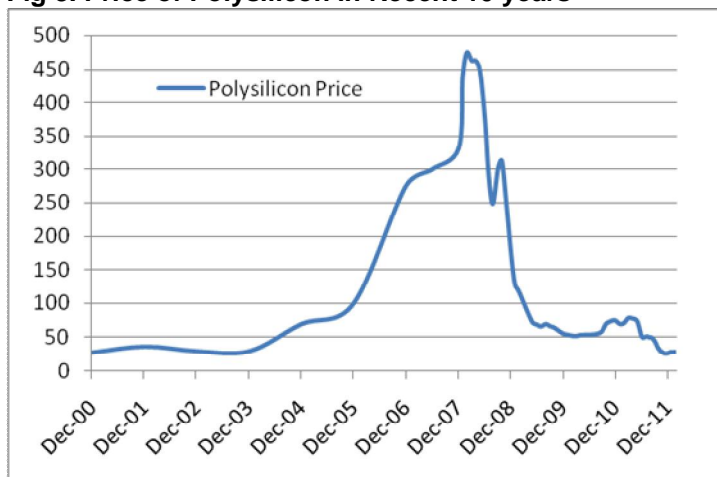
2. Comtec's Operation Analysis

The operation structure of Comtec is single; its most revenue is from the production and sale of solar wafer. Its main products are P-type single-crystal silicon wafer and the size of most products is 156mm. The revenue from this product took 80.6% of the total revenue. And growth in revenue is attributing to the sale growth, as product price declined 3% to 9% in the same period.

Comtec's performance could maintain in a stable position and avoided loss in the fierce competition, we estimate that the main reasons are following:

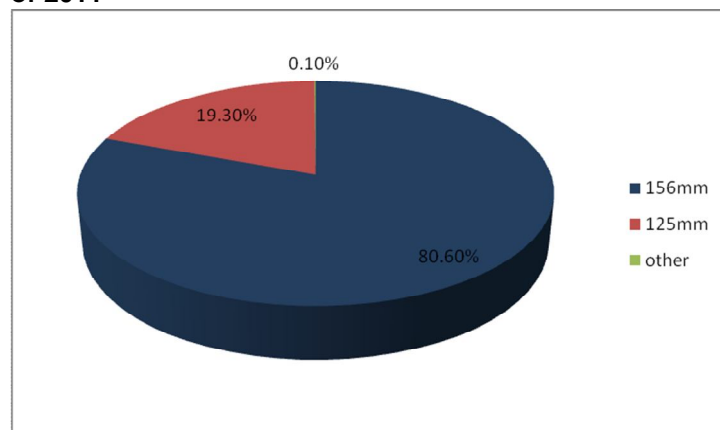
- 1). The reasonable control of cost. The price of Polysilicon is increased in report period, the increase rate is 18.8%, it's a negative change for the Comtec's cost control, but the company still could keeps the cost at a relative lower level by improving manufacture and management efficiency. In the future, the economies of scale and improvement of production efficiency could offset the negative effect from the price increase of raw materials.

Fig 3. Price of Polysilicon in Recent 10 years



(Source: Bloomberg)

Fig 4. Revenue Proportion of Comtec in the first half of 2011



(Source: Company reports)

2).The customer base of Comtec is relative stable. According to information of 2011 interim report, the large part of revenue is generated by the big five customers who have long cooperation relationship with Comtec. So even the market situation is tough, the sale of Comtec could keeps in a stable position. Additionally, the inventory level of semi-products and products didn't changed in the past several years, also means the sales channel is fine. So this point is very favorable for the future development of Comtec. But there's something need to be note, for the concentration degree of customer is relative high, the bargaining power of the company may be limited, the negative effect from this aspect need to follow closely.

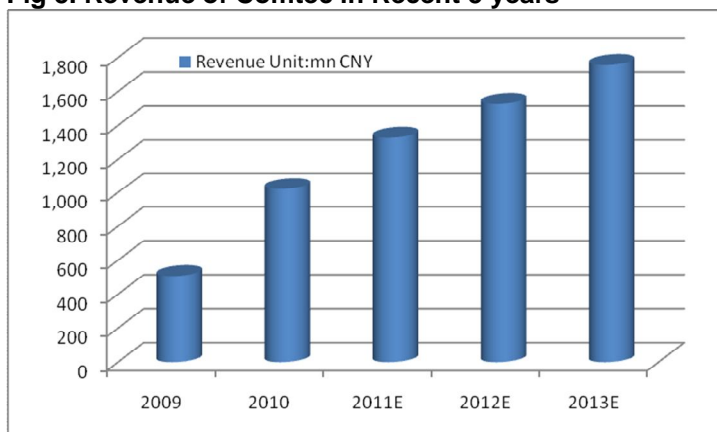
3). Comtec's research and development of new product got significant achievement, according to company's disclosure, the super Monocrystalline silicon wafer is already put into production. The conversion efficiency of this product is 20% higher than the current solar wafer and according to the feedback of market and customers, the demand and sale of super wafer is good. The company is planning to expand market by promote the super wafer as main product, and the proportion of super wafer in all sales will increase to 50% in the future. Product differentiation is extremely beneficial to the company's development, because the differentiated product could attract more market concerns. Besides, in the upstream companies of PV industry, Comtec's fame is relative high and had been named as world top 10 solar wafers manufacturers. The brand premium is also very important for the future development.

Additionally, Comtec's capacity is still increasing. During the report period, the construction of new production base is finished and planned to put into operation in 2012. The whole capacity of the company will reach 1400 GW per year. Although overcapacity is still exist and America already proposed anti-dumping proceeding for the solar wafers produced in China, the Comtec's customers are mainly located in mainland and Taiwan area, so the negative effect is limited. We believe that with the slow industry recovery and stable increase in demand of large customers, the performance of Comtec will be improved gradually.

3. Financial Report Analysis

During the report period, the revenue is increased approximately 33.9% to the same period of 2010, to 574 million RMB. From the structure of income, the increase in income is attributing to the increase in sale, and the innovation of product also made contribution to it. The gross profit rate and net profit rate are improved in report period, specifically the gross profit rate increased 0.8% to 23.6% and the net profit rate increased 1.7% to 17.5%. The growth in profit rate is attributed to the price fluctuation of raw material and improvement of production efficiency. Although comparing with peak figures in 2007 and 2008, the gap is still huge; the premium from product and brand is significantly obvious when compared to industry average level. We estimate that when the cost already arrived at the bottom and product price is hard to promote in relative short time, the company profit margins will be remain in the current level.

Fig 5. Revenue of Comtec in Recent 5 years



(Sources: Company reports, Phillip Securities estimate)

Another important issue is the sharp increase of inventory. From the absolute value, the inventory increased 174.16% approximately comparing to the level in 2009 and inventory turnover and other financial indicators relate to inventory are all showed negative changes. The inventory turnover of Comtec is 3.97, far less than the industry average level, about 8 to 12. But the inventory structure is more important than figure itself, as we mentioned above, raw material takes a large part of inventory, nearly 85%. If the price of polysilicon increase in the future, with the expansion of capacity, the inventory level will decrease and return to the reasonable range.

Form 1. Key Financial Data Comparison

Code	ROA	ROE	P/B	Market Value	P/E	Income	EPS
916	3.63	11.12	1.65	50234.66	15.54	18268.23	0.41
750	15.12	23.18	1.57	2149.84	7.58	2046.15	0.51
958	2.41	12.31	1.17	16248.99	11.19	3849.89	0.17
757	7.60	15.40	0.67	1861.00	4.62	2740.99	0.17
658	7.34	18.66	0.66	6050.58	4.22	8758.51	0.97
712	12.06	16.99	0.64	1485.40	4.63	1369.36	0.27
155	-27.56	-30.23	0.55	507.67		174.23	-0.03
2468			0.43	1584.68		2006.36	-0.25
1165	14.08	32.66		577.20	4.36	715.08	0.08
8128				867.43	37.84	249.55	0.01

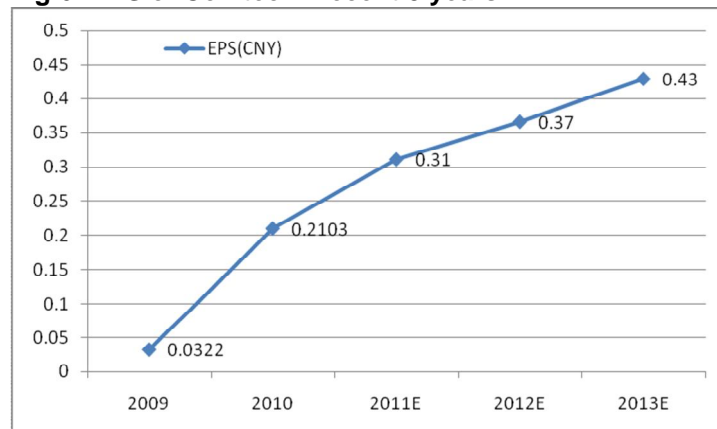
(Source: Bloomberg)

4. Valuation

According to the interim report of 2011, the EPS increased approximately 34.6% comparing the same period of 2010 to CNY0.08. And the company's sales volume and sales growth is about 28.3% and 33.9%. Because the operation condition of Comtec is stable in recent years, we estimate that the EPS growth will be

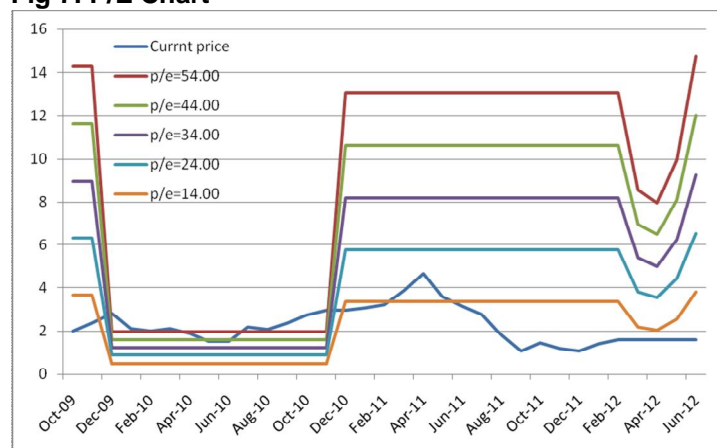
20% per year, so the EPS of 2011 and 2012 are CNY 0.31 and CNY 0.37 separately. Considering the market situation, the target price is HKD 1.57 under 3.5x P/E we estimated, the rating is Accumulated.

Fig 6: EPS of Comtec in recent 5 years



(Sources: Company reports, Phillip Securities estimate)

Fig 7: P/E Chart



(Source: Bloomberg)

5. Risk

- Price of polysilicon will increase in the future.
- Demand of downstream companies and relevant product price remain in low level.
- Macro-economy risk increases.

Key Assumption:
HKD 1= CNY 0.81

Financial Data

Income Statement

Unit: Million CNY	2009	2010	2011E	2012E	2013E
Revenue	506.88	1021.37	1327.78	1526.95	1756.10
Cost	(451.76)	(690.79)	898.03	1014.77	1146.69
Gross Profit	55.12	330.59	429.75	512.18	609.41
Other Income	4.85	26.57	29.23	32.15	35.36
Selling and Distrib	(2.22)	(1.79)	(2.15)	(2.58)	(2.84)
Administrative Exp	(18.19)	(75.76)	(37.54)	(48.81)	(63.45)
Other Expenses	3.41	-	3.75	4.13	4.54
Finance Cost	(6.67)	(7.40)	(8.14)	(8.95)	(9.85)
Operation Profit	31.33	263.09	414.90	488.12	573.17
Tax	(6.39)	(40.15)	(62.24)	(73.22)	(85.98)
Minority Interest	0.00	0.00	0.00	0.00	0.00
Net profit	24.94	222.94	352.67	414.90	487.19
Shareholder equit	24.94	222.94	352.67	414.90	487.19
Depreciation	26.94	55.42	72.05	86.46	95.11
EBITDA	58.27	318.51	486.95	574.58	668.28

Balance Sheet

Unit: Million CNY	2009	2010	2011E	2012E	2013E
Current Asset	742.95	776.59	1553.17	1679.86	1847.84
Non-Current Asse	667.72	1135.81	1454.24	1708.49	1879.34
Asset	1410.68	1912.39	3007.41	3388.35	3727.18
Current Liability	345.28	396.59	436.25	479.88	527.87
Non-Current Liabil	3.77	4.46	5.35	6.42	7.70
Liability	349.05	401.05	441.60	486.29	535.57
Equity	1061.63	1511.34	2565.81	2902.05	3191.61
Shares	1031.74	1133.63	1133.63	1133.63	1133.63
Dividend(CNY)	0.0073	0.00	0.00	0.00	0.00
EPS(CNY)	0.0322	0.2103	0.31	0.37	0.43
BookValue per sh	1.029	1.3332	2.26	2.56	2.82
ROA(%)	1.77%	11.66%	11.73%	12.24%	13.07%
ROE(%)	2.35%	14.75%	13.74%	14.30%	15.26%
P/E(x)	32.95	5.05	3.41	2.90	2.47
P/B(x)	1.03	0.80	0.47	0.41	0.38

(Sources: Company reports, Phillip Securities estimate)

Important Information

This publication is prepared by Phillip Securities Research Pte Ltd., 250 North Bridge Road, #06-00, Raffles City Tower, Singapore 179101 (Registration Number: 198803136N), which is regulated by the Monetary Authority of Singapore ("Phillip Securities Research"). By receiving or reading this publication, you agree to be bound by the terms and limitations set out below.

This publication has been provided to you for personal use only and shall not be reproduced, distributed or published by you in whole or in part, for any purpose. If you have received this document by mistake, please delete or destroy it, and notify the sender immediately. Phillip Securities Research shall not be liable for any direct or consequential loss arising from any use of material contained in this publication.

The information contained in this publication has been obtained from public sources, which Phillip Securities Research has no reason to believe are unreliable and any analysis, forecasts, projections, expectations and opinions (collectively, the "Research") contained in this publication are based on such information and are expressions of belief of the individual author or the indicated source (as applicable) only. Phillip Securities Research has not verified this information and no representation or warranty, express or implied, is made that such information or Research is accurate, complete, appropriate or verified or should be relied upon as such. Any such information or Research contained in this publication is subject to change, and Phillip Securities Research shall not have any responsibility to maintain or update the information or Research made available or to supply any corrections, updates or releases in connection therewith. In no event will Phillip Securities Research or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, (i) be liable in any manner whatsoever for any consequences (including but not limited to any special, direct, indirect, incidental or consequential losses, loss of profits and damages) of any reliance or usage of this publication or (ii) accept any legal responsibility from any person who receives this publication, even if it has been advised of the possibility of such damages. You must make the final investment decision and accept all responsibility for your investment decision, including, but not limited to your reliance on the information, data and/or other materials presented in this publication.

Any opinions, forecasts, assumptions, estimates, valuations and prices contained in this material are as of the date indicated and are subject to change at any time without prior notice.

Past performance of any product referred to in this publication is not indicative of future results.

This report does not constitute, and should not be used as a substitute for, tax, legal or investment advice. This publication should not be relied upon exclusively or as authoritative, without further being subject to the recipient's own independent verification and exercise of judgment. The fact that this publication has been made available constitutes neither a recommendation to enter into a particular transaction, nor a representation that any product described in this material is suitable or appropriate for the recipient. Recipients should be aware that many of the products, which may be described in this publication involve significant risks and may not be suitable for all investors, and that any decision to enter into transactions involving such products should not be made, unless all such risks are understood and an independent determination has been made that such transactions would be appropriate. Any discussion of the risks contained herein with respect to any product should not be considered to be a disclosure of all risks or a complete discussion of such risks.

Nothing in this report shall be construed to be an offer or solicitation for the purchase or sale of any product. Any decision to purchase any product mentioned in this research should take into account existing public information, including any registered prospectus in respect of such product.

Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, may provide an array of financial services to a large number of corporations in Singapore and worldwide, including but not limited to commercial / investment banking activities (including sponsorship, financial advisory or underwriting activities), brokerage or securities trading activities. Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, may have participated in or invested in transactions with the issuer(s) of the securities mentioned in this publication, and may have performed services for or solicited business from such issuers. Additionally, Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the

preparation or issuance of this report, may have provided advice or investment services to such companies and investments or related investments, as may be mentioned in this publication.

Phillip Securities Research or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report may, from time to time maintain a long or short position in securities referred to herein, or in related futures or options, purchase or sell, make a market in, or engage in any other transaction involving such securities, and earn brokerage or other compensation in respect of the foregoing. Investments will be denominated in various currencies including US dollars and Euro and thus will be subject to any fluctuation in exchange rates between US dollars and Euro or foreign currencies and the currency of your own jurisdiction. Such fluctuations may have an adverse effect on the value, price or income return of the investment.

To the extent permitted by law, Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, may at any time engage in any of the above activities as set out above or otherwise hold an interest, whether material or not, in respect of companies and investments or related investments, which may be mentioned in this publication. Accordingly, information may be available to Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, which is not reflected in this material, and Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, may, to the extent permitted by law, have acted upon or used the information prior to or immediately following its publication. Phillip Securities Research, or persons associated with or connected to Phillip Securities Research, including but not limited to its officers, directors, employees or persons involved in the preparation or issuance of this report, may have issued other material that is inconsistent with, or reach different conclusions from, the contents of this material.

The information, tools and material presented herein are not directed, intended for distribution to or use by, any person or entity in any jurisdiction or country where such distribution, publication, availability or use would be contrary to the applicable law or regulation or which would subject Phillip Securities Research to any registration or licensing or other requirement, or penalty for contravention of such requirements within such jurisdiction.

Section 27 of the Financial Advisers Act (Cap. 110) of Singapore and the MAS Notice on Recommendations on Investment Products (FAA-N01) do not apply in respect of this publication.

This material is intended for general circulation only and does not take into account the specific investment objectives, financial situation or particular needs of any particular person. The products mentioned in this material may not be suitable for all investors and a person receiving or reading this material should seek advice from a professional and financial adviser regarding the legal, business, financial, tax and other aspects including the suitability of such products, taking into account the specific investment objectives, financial situation or particular needs of that person, before making a commitment to invest in any of such products.

Please contact Phillip Securities Research at [65 65311240] in respect of any matters arising from, or in connection with, this document.

This report is only for the purpose of distribution in Singapore.

Contact Information (Singapore Research Team)

Chan Wai Chee
CEO, Research
Special Opportunities
+65 6531 1231
yebo@phillip.com.sg

Magdalene Choong
Investment Analyst
SG & US Financials, Gaming
+65 6531 1791
magdalenechoongss@phillip.com.sg

Nicholas Low, CFA
Investment Analyst
Commodities, Offshore & Marine
+65 6531 1535
nicholaslowkc@phillip.com.sg

Ken Ang
Investment Analyst
Financials
+65 6531 1793
kenangwy@phillip.com.sg

Lee Kok Joo, CFA
Head of Research
S-Chips, Strategy
+65 6531 1685
leekj@phillip.com.sg

Go Choon Koay, Bryan
Investment Analyst
Property
+65 6531 1792
gock@phillip.com.sg

Travis Seah
Investment Analyst
REITS
+65 6531 1229
travisseahhk@phillip.com.sg

Joshua Tan
Strategist
+65 6531 1249
joshuatan@phillip.com.sg

Derrick Heng
Investment Analyst
Transportation, Telecom.
+65 6531 1221
derrickhengch@phillip.com.sg

Peter Lee
Research Assistant
General Enquiries
+65 6531 1240 (Phone)
+65 6336 7607 (Fax)
research@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE

Phillip Securities Pte Ltd
Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel : (65) 6533 6001
Fax : (65) 6535 6631
Website: www.poems.com.sg

HONG KONG

Phillip Securities (HK) Ltd
Exchange Participant of the Stock Exchange of Hong Kong
11/F United Centre 95 Queensway
Hong Kong
Tel (852) 22776600
Fax (852) 28685307
Websites: www.phillip.com.hk

INDONESIA

PT Phillip Securities Indonesia
ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel (62-21) 57900800
Fax (62-21) 57900809
Website: www.phillip.co.id

THAILAND

Phillip Securities (Thailand) Public Co. Ltd
15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel (66-2) 6351700 / 22680999
Fax (66-2) 22680921
Website www.phillip.co.th

UNITED KINGDOM

King & Shaxson Capital Limited
6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel (44-20) 7426 5950
Fax (44-20) 7626 1757
Website: www.kingandshaxson.com

AUSTRALIA

PhillipCapital Australia
Level 37, 530 Collins Street,
Melbourne, Victoria 3000, Australia
Tel (613) 96298380
Fax (613) 96148309
Website: www.phillipcapital.com.au

MALAYSIA

Phillip Capital Management Sdn Bhd
B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel (603) 21628841
Fax (603) 21665099
Website: www.poems.com.my

JAPAN

PhillipCapital Japan K.K.
Nagata-cho Bldg.,
8F, 2-4-3 Nagata-cho,
Chiyoda-ku, Tokyo 100-0014
Tel (81-3) 35953631
Fax (81-3) 35953630
Website: www.phillip.co.jp

CHINA

Phillip Financial Advisory (Shanghai) Co. Ltd
No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel (86-21) 51699200
Fax (86-21) 63512940
Website: www.phillip.com.cn

FRANCE

King & Shaxson Capital Limited
3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel (33-1) 45633100
Fax (33-1) 45636017
Website: www.kingandshaxson.com

UNITED STATES

Phillip Futures Inc
141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1.312.356.9000
Fax +1.312.356.9005