

Tongda Group (698.HK)

Technical Advantages Facilitate Market Expansion

Hong Kong | TMT | Company report

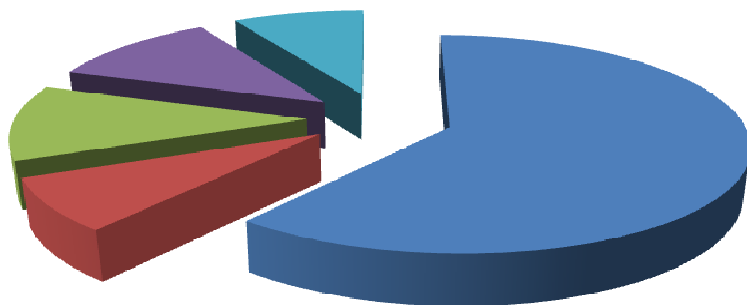
Technical Advantages Facilitate Market Expansion

Metal casing has become the major driving force for Tongda Group. Currently, few mobile phones produced in China use metal casing, accounting for only 10%. However, the newly released models more often use metal casing and the market will be in a rapid expansion. According to estimates, the proportion of Huawei mobile phones using metal casing will increase from 3% in 2014 to 20% in 2015 and 50% in 2016; that of Xiaomi mobile phones using metal casing will rise from 15% in 2015 and 25% in 2016. Also, mobile phones of other brands using metal casing are expected to soar from around 8 million in 2015 to 46 million in 2016, a five-time increase.

It is worth mentioning that metal casing will break into the market of mobile phones at RMB1,000. Tongda Group's technical advantage of "Composite Die-casting Technology + Nano Molding Technology (NMT) + CNC Processing" can half the time of metal casing production compared with that of competitors. Also, the overall yield of 70-80% also outperforms its peers. Meanwhile, the company's metal casing price around RMB100 is also half. Therefore, the company is more competitive in this market. Furthermore, the company will expand its CNC machine from the current 1700 sets to 2000-2300. As a result, the metal casing business will sustain the company's rapid growth, and its 28-30% gross profit margin will also enhance the profitability.

Sales breakdown in 1H15

■ Handset casings ■ Notebook computers ■ Electrical appliances
■ Ironware ■ Communication



Source: Company report, Phillip Securities (HK) Research

Brand Users Support Emerging Business Development

In the last decade, the diversified product mix of handsets, notebook computers and electrical appliances supported the stable growth of the Company's business. Presently, the company has already expanded business to the production of interior components for automobiles, which has been recognized by well-known clients. In addition to the existing clients such as Cisco, Decathlon, Ford and BYD, GM, Geely and Mazda have become the company's new clients since 2015. Despite the present small proportion of automotive interior components business, its market is huge with up to 30% of gross profit margin. We believe the business will become a new driver for the company.

5 February 2016

Buy (Maintain)

CMP: HKD 1.25
(Closing price as at 3 Feb 2016)
TARGET: HKD 1.64 (+31%)

COMPANY DATA

O/S SHARES (MN) :	5,726
MARKET CAP (HKDMN) :	7,158
52 - WK HI/LO (HKD):	1.75/1.00

SHARE HOLDING PATTERN , %

Wang Yanan :	41.40
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PRICE PERFORMANCE , %

	1M	3M	1Y
Tongda Group	-6.57	-17.95	23.08
HSI	4.69	-4.12	43.88

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

HKD mn	FY13	FY14	FY15E	FY16E
Net Sales	3627	4791	6301	7545
Net Profit	360	502	730	938
EPS, HKD	0.075	0.094	0.130	0.164
PER, x	16.7	13.3	9.6	7.6
BVPS, HKD	0.525	0.640	0.740	0.869
P/BV, x	2.4	2.0	1.7	1.4
ROE, %	15.2	16.9	18.6	20.6
Debt/Equity (%)	82.7	75.10	92.31	92.31

Source: Company reports, Phillip Securities Est.

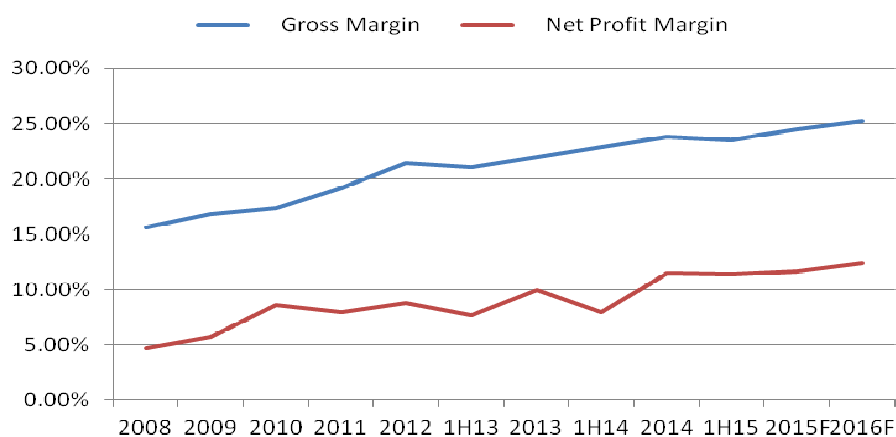
Research Analyst
Fan Guohe
(+ 86 21 51699400-110)
fanguohe@phillip.com.cn

Additionally, Tongda has been developing the rubber compression molding technology which can be used in the waterproof rubber band for smart phones and wearable devices. Moreover, Apple Inc. is likely to become the company's potential client. At present, this field is not fully competitive, and the gross profit margin can reach 30%. Once an agreement is concluded, the company's R&D strength will be further demonstrated, and the brand effect of the company will increase, laying groundwork for its further expansion. In the meantime, the agreement is also expected to contribute to performance growth of 1-3 percentage points.

Increase of Shareholder Equity Holdings that Highlight Confidence in Development

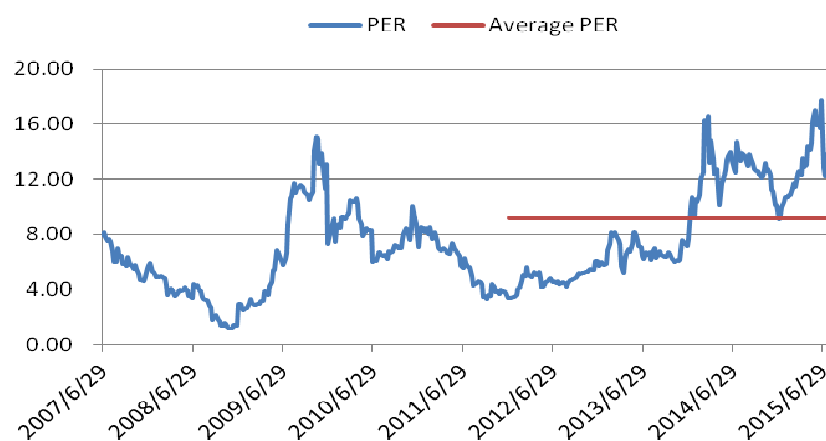
Since the end of last year, Wang Yanan, the actual controller of the company has increased his holdings from 40.92% to 41.4%. And the acquisition price has dropped from the previous HK\$1.4 to the current HK\$1.25. This demonstrates his confidence in the company's development. We believe that Tongda Group equips itself with the core competitive technologies in all segments that constantly win the recognition of well-known clients. Also, the new businesses such as metal casing will not only support the Company's growth, but will improve its profitability as well. We grant it 10x P/E corresponding to 2016 EPS and the price target is HK\$ 1.64, with the "Buy" rating maintained. (Closing price as at 3 Feb 2016)

Improved earning capabilities



Source: Company report, Phillip Securities (HK) Research

Historical P/E valuation



Source: Company report, Phillip Securities (HK) Research

Risk

Intense competition in the smart phone market that will result in price wars;
The new capacity cannot be put into production as expected.

Financials

Periodicity:	2012	2013	2014	2015F	2016F
Valuation Ratios					
Price Earnings	19.5x	16.7x	13.3x	9.6x	7.6x
Price to Book	2.8x	2.4x	2.0x	1.7x	1.4x
Dividend Yield	1.6%	2.0%	1.6%	2.4%	2.8%
Per share data(HK\$)					
EPS Adjusted	0.064	0.075	0.094	0.130	0.164
Book Value Per Share	0.441	0.525	0.640	0.740	0.869
Dividends Per Share	0.020	0.025	0.020	0.030	0.035
Growth & Margin					
Revenue growth	8.29%	6.42%	32.09%	31.52%	19.75%
Gross profit growth	20.70%	9.22%	43.36%	34.94%	23.17%
Net profit growth	19.85%	20.00%	39.44%	45.45%	28.45%
Gross Margin	21.4%	22.0%	23.9%	24.5%	25.2%
Operating Margin	13.1%	12.9%	14.5%	15.5%	16.2%
Net Profit Margin	8.8%	9.9%	10.5%	11.6%	12.4%
Dividend Payout Ratio %	31.8%	33.5%	21.2%	23.0%	21.4%
Key ratios					
Return on Assets	7.6%	8.1%	10.0%	10.1%	10.7%
Return on Equity	15.2%	15.2%	16.9%	18.6%	20.6%
Liability ratio	47.84%	45.27%	42.89%	48.00%	48.00%
Effective Tax Rate	16.8%	11.1%	14.6%	13.0%	13.0%
Income Statement(HK\$: mn)					
Revenue	3,408	3,627	4,791	6,301	7,545
- Cost of Goods Sold	2,677	2,829	3,648	4,757	5,644
Gross Income	731	798	1,144	1,544	1,901
- Selling, General & Admin Expenses	295	357	450	599	717
Operating Income	448	468	694	975	1,222
- Interest Expense	49	52	57	55	52
Pretax Income	401	415	642	915	1,175
- Income Tax Expense	67	46	94	119	153
Income Before XO Items	334	369	548	796	1,022
- Minority Interests	34	9	46	66	84
Net Profit	300	360	502	730	938

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 3 Feb 2015)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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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 12, 15 William Street,
Melbourne, Victoria 3000, Australia
Tel (613) 96188238
Fax (613) 92002272
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 436 Hengfeng Road,
Greentech Unit 604,
Postal code 200070
Tel (86-21) 51699400
Fax (86-21) 63532643
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