

# Yangtze Optical Fibre and Cable (6869.HK)

**Comprehensive Technology and Complete Industry Chain Layout  
Help Consolidate the Leading Position**

**Hong Kong | TMT | Company report**

15 February 2016

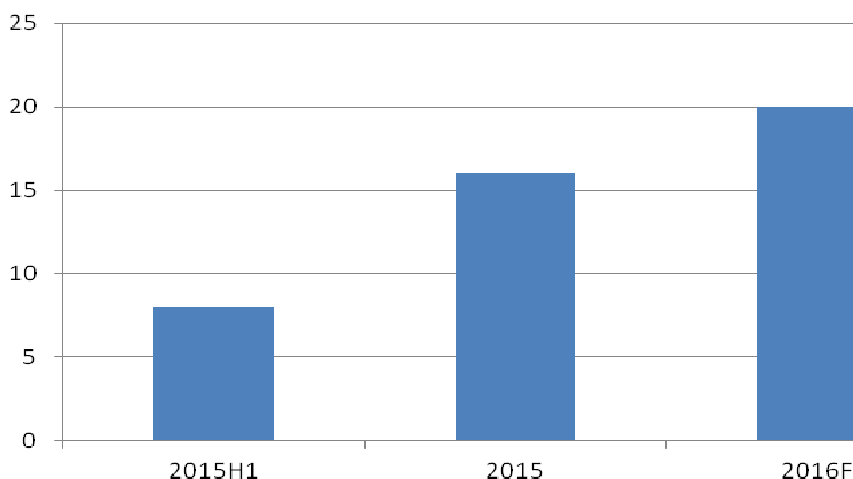
## Internet Construction Leads to Short Supply of Optical Fibre

Currently, the Chinese government actively invests RMB1.14 trillion in constructing high-speed Internet and will accelerate fibre-to-the-home (FTTH) in the coming three years. Therefore, the accelerated construction of 4G network and fixed-line broadband in mainland China and the rise of IDC, cloud computing and big data business will contribute to the increased demand for transmission network expansion. Also, the United States leads the global network transmission speed to upgrade from the current 10Gbps to 40-100Gbps. Overall, these will help maintain a heavy demand for optical fibre and cable, from which the company will benefit.

Presently, the optical fibre market has faced the predicament of short supply for the first time since FY2000. The optical fibres for tender and bid of China Mobile in 2015 to 2016 totalled 94.52 million km, a YoY increase of around 60%. Meanwhile, the tender price of all manufacturers basically grew by 5-10%. In this tender, the share of YOFC ranked the third, like 12.5% of tendered G.652D optical fibre. We believe that the company will still embrace the favorable situation of increase in both sales volume and price and that its performance will see further rapid growth.

In the meantime, in order to adapt to the national policy of "One Belt and One Road", the company plans to build a cable plant in Myanmar and Indonesia in 2015. At present, the company plans to open up opportunities of growth in Africa / South America and intends to build one million km/year of cable facilities in South Africa. The FTTH penetration rate in Africa, South America and other places is only 2.5%, resulting in vast space for development. Since optical fibre is fragile and inappropriate for transport, localized production is a more favorable choice. We believe that the strategy of YOFC will lead to its sustained growth in overseas contribution.

### Enlarged optical fibre cable capacity of YOFC (m fkm)



Source: Company reports, Phillip Securities (HK) Research

## Buy (Upgrade)

CMP: HKD 7.33  
(Closing price as at 11 Feb 2016)  
TARGET: HKD 10.00 (+36.4%)

### COMPANY DATA

O/S SHARES (MN) :	682
MARKET CAP (HKDMN) :	4,999
52 - WK HI/LO (HKD):	12.32/ 6.30

### SHARE HOLDING PATTERN, %

Draka Comteq B.V. :	28.12
China Huaxin Post & Telecommunication Economy Development Center	28.12

### PRICE PERFORMANCE, %

	1M	3M	1Y
YOFC	-15.02	-14.83	16.62
HSI	-6.95	0.82	38.46

### PRICE VS. HSI



Source: Phillip Securities (HK) Research

### KEY FINANCIALS

CNY mn	FY13	FY14	FY15E	FY16E
Net Sales	4826	5677	6347	7050
Net Profit	415	466	555	703
EPS, CNY	0.87	0.95	0.84	1.03
PER, x	7.1	6.5	7.4	6.0
BVPS, CNY	3.15	4.40	4.91	5.71
P/BV, x	2.0	1.4	1.3	1.1
ROE, %	25.5	21.6	17.8	19.5
Debt/Equity (%)	231.7	126.4	127.3	127.3

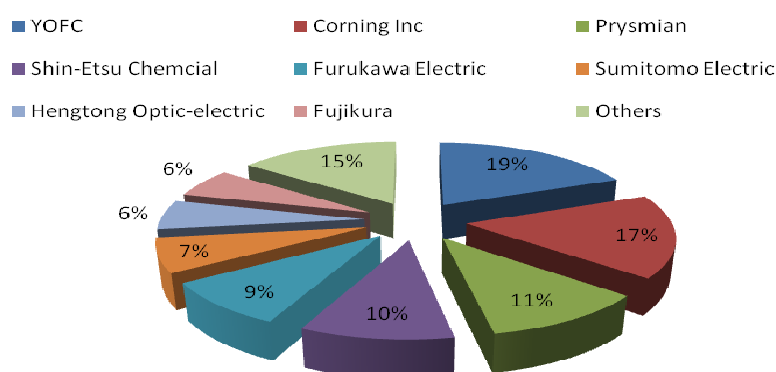
Source: Company reports, Phillip Securities Est.

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## Comprehensive Technology and Complete Industry Chain Help Consolidate the Leading Position

In the profit structure of optical fibre industry chain, preform accounts for about 70%, being most profitable. At present, YOFC not only owns the largest capacity in this field, but is the only enterprise mastering PCVD, VAD and OVD technologies in the world. So by integrating the advantages of these three technologies, its manufacturing of cladding and mandrel has been globally cutting-edge. Furthermore, the company will expand the capacity of Hubei Qianjiang with Phase I capacity reaching 500 tonnes. As a result, the company will continue to consolidate its leading position in the domain of the preform and increase its self-sufficiency rate to enhance profitability.

### Global market share of optical fibre preforms



Source: Company reports, Phillip Securities (HK) Research

Meanwhile, the company also starts the whole industry chain layout. Downstream, the fibre coating project was officially approved, and also, the company broke into the field of integrated cabling. Currently, the domestic high-end market of data centre cabling is monopolized by imported brands with over 40% of gross margin. But in the era of big data, this demand will be immense. Upstream, the company carries the layout of key raw materials such as silicon tetrachloride and germanium tetrachloride. Overall, the company will be the one with the longest industry chain in the industry of optical fibre and cable in the globe and will keep consolidating its leading position.

### Industry Leader but Undervalued

In spite of the overall excess capacity in the cable industry, the short supply of optical fibre preform and accelerated construction of "Broadband China" and "FTTH" in mainland China will significantly improve the supply and demand situation. As an industry leader, the company is equipped with technical and profitable advantages, so its sales growth is worth expecting. We take 10 times as the PE ratio valuation of EPS in 2015 and the target price can reach 10 HKD, with the "Buy" rating. (Closing price as at 11 Feb 2016)

### Risk

The capital expenditure of operators' fixed-line broadband falls short of expectation. Intense competition results in the decline in profitability.

## Financials

FYE	2012	2013	2014	2015F	2016F
<b>Valuation Ratios</b>					
Price Earnings	8.1x	7.1x	6.5x	7.4x	6.0x
Price to Book	1.7x	2.0x	1.4x	1.3x	1.1x
Dividend Yield	0.0%	0.0%	2.7%	3.1%	3.7%
<b>Per share data(RMB)</b>					
EPS Adjusted	0.76	0.87	0.95	0.84	1.03
Book Value Per Share	3.65	3.15	4.40	4.91	5.71
Dividends Per Share	0.00	0.00	0.17	0.19	0.23
<b>Growth &amp; Margin</b>					
Revenue growth	14.4%	1.0%	17.6%	11.8%	11.1%
Gross Profit growth	19.0%	15.4%	6.9%	15.5%	19.5%
Net Profit growth	6.1%	13.8%	12.4%	19.1%	26.6%
<b>Profitability Ratios</b>					
Gross Margin	18.5%	21.1%	19.2%	19.8%	21.3%
Net Profit Margin	7.6%	8.6%	8.2%	8.7%	10.0%
Dividend Payout Ratio %	0.0%	0.0%	22.8%	22.6%	22.3%
<b>Key Ratios</b>					
Return on Assets	9.7%	9.2%	8.0%	7.8%	8.6%
Return on Equity	22.1%	25.5%	21.6%	17.8%	19.5%
Effective Tax Rate	9.0%	11.7%	13.2%	12.5%	12.5%
Liability ratio	56.3%	69.9%	55.8%	56.0%	56.0%
<b>Income Statement(RMB: mn)</b>					
<b>Revenue</b>	<b>4,778</b>	<b>4,826</b>	<b>5,677</b>	<b>6,347</b>	<b>7,050</b>
- Cost of Goods Sold	3,896	3,808	4,589	5,090	5,548
<b>Gross Income</b>	<b>882</b>	<b>1,018</b>	<b>1,088</b>	<b>1,257</b>	<b>1,502</b>
- Selling, General & Admin Expenses	528	549	565	635	705
<b>Operating Income</b>	<b>378</b>	<b>491</b>	<b>553</b>	<b>1,297</b>	<b>1,542</b>
- Interest Expense	62	40	67	75	81
<b>Pretax Income</b>	<b>401</b>	<b>470</b>	<b>535</b>	<b>632</b>	<b>800</b>
- Income Tax Expense	36	55	71	79	100
<b>Income Before XO Items</b>	<b>365</b>	<b>415</b>	<b>464</b>	<b>553</b>	<b>700</b>
<b>Net Profit</b>	<b>365</b>	<b>415</b>	<b>466</b>	<b>555</b>	<b>703</b>

Source: Company, Phillip Securities (HK) Research Estimates  
(Financial figures as at 11 Feb 2016)

**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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