

Growth from NB/Eee PCs and emerging markets



Reiterate Buy with lower PO of NT\$68.0

Asustek will host its analyst meeting on 30 Oct. We expect Asustek to meet the low-end of the Street's estimates (~NT\$7bn) for 3Q and guide 10% QoQ revenue growth with flat margins for 4Q. We cut our 2008/09 earnings by 2%/13% due to lower ASP/GP margin and higher Opex, despite improvement in the ODM business from 3Q08. We retain Buy with lower PO of NT\$68.0 (from NT\$84.7).

Mixed bag for 3Q08

With solid demand in China/Eastern Europe for NB/Eee PCs, Asustek's 3Q revenue increased 35% QoQ, surpassing its target of 30%. Our checks also suggest Pegatron could double its earnings due to robust revenue, improved efficiency and FX rate swings. However, we expect OPM to decline 70bp QoQ to 6.9% (vs its target of up 100-200bp), due to higher rebates/employee bonus.

NB/Eee PCs remain the growth driver for 2009

We expect Asustek to grow brand revenue by 15% YoY (vs 25% previously) for 2009, driven by both NB PCs (up 28% from 6mn in 08E) and Eee PCs (up 42% YoY from 5mn for 08E), despite a mild decline in motherboards. Asustek should benefit from the wave of Netbooks (as it is the pioneer) and its strong position in major emerging countries (ie, China/Russia), where demand remains strong.

Prefer Acer/Compal over Asustek

We like Acer given its pure brand model, position at the low-end segment and stronger procurement power. Compal offers great value/strong BS. However, Asustek might stand out again when we see its innovations deliver or/and further progress in the spin off. PO of NT\$68.0 is based upon our sum-of-parts valuation — 11x core EPS (NT\$58.0) plus 8x investment income (NT\$10.0) for 2009.

Estimates (Dec)

(NT\$)	2006A	2007A	2008E	2009E	2010E
Net Income (mn) Taiwan GAAP	21,742	30,458	27,084	27,331	28,656
EPS (Pre Bonus)	5.121	7.173	7.087	7.152	7.499
EPS (Post Bonus)	3.368	5.739	6.379	6.437	6.749
EPS Change (YoY)	8.6%	70.4%	11.2%	0.9%	4.8%
Dividend / Share	1.20	1.73	2.50	3.00	3.50
Free Cash Flow / Share	(2.33)	4.64	4.63	2.44	(1.77)

* Taiwan GAAP changed from Pre Bonus to Post Bonus earnings from 2008.

Valuation (Dec)

	2006A	2007A	2008E	2009E	2010E
P/E (Post Bonus)	15.62x	9.17x	8.25x	8.17x	7.79x
Dividend Yield	2.29%	3.29%	4.75%	5.70%	6.65%
Free Cash Flow Yield*	-4.43%	8.81%	8.81%	4.64%	-3.36%

* For full definitions of *iQmethod*SM measures, see page 10.

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Stock Data

Price	NT\$52.60
Price Objective	NT\$84.70 to NT\$68.00
Date Established	21-Oct-2008
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	NT\$48.35-NT\$105.48
Mrkt Val / Shares Out (mn)	US\$6,855 / 4,246.0
Average Daily Volume	32,760,450
ML Symbol / Exchange	AKCPF / TWO
Bloomberg / Reuters	2357 TT / 2357.TW
ROE (2008E)	14.3%
Net Dbt to Eqty (Dec-2007A)	-18.4%
Est. 5-Yr EPS / DPS Growth	10.0% / 20.0%
Free Float	70.0%



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Refer to important disclosures on page 11 to 12. Analyst Certification on Page 8. Price Objective Basis/Risk on page 8.

21 October 2008

iQprofileSM Asustek Computer Inc.

Key Income Statement Data (Dec)	2006A	2007A	2008E	2009E	2010E
(NT\$ Millions)					
Sales	560,235	755,361	774,375	848,237	934,298
Gross Profit	54,922	74,769	88,450	92,752	99,019
Sell General & Admin Expense	(34,569)	(46,098)	(64,440)	(62,516)	(63,532)
Operating Profit	20,353	28,672	24,010	30,236	35,486
Net Interest & Other Income	8,000	9,614	11,701	4,595	1,869
Associates	NA	NA	NA	NA	NA
Pretax Income	28,353	38,286	35,711	34,831	37,356
Tax (expense) / Benefit	(6,611)	(7,828)	(8,627)	(7,500)	(8,700)
Net Income (Adjusted)	21,742	30,458	27,084	27,331	28,656
Average Fully Diluted Shares Outstanding	4,246	4,246	4,246	4,246	4,246

Key Cash Flow Statement Data

Net Income (Reported)	21,742	30,458	27,084	27,331	28,656
Depreciation & Amortization	4,687	2,239	2,710	3,774	4,881
Change in Working Capital	(30,878)	(15,595)	19,705	7,939	(7,739)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	13,452	22,968	(1,927)	1,310	1,702
Cash Flow from Operations	9,003	40,069	47,572	40,354	27,500
Capital Expenditure	(18,897)	(20,383)	(27,896)	(30,000)	(35,000)
(Acquisition) / Disposal of Investments	(425)	(4,639)	(600)	(800)	(800)
Other Cash Inflow / (Outflow)	(1,313)	0	0	0	0
Cash Flow from Investing	(20,635)	(25,022)	(28,496)	(30,800)	(35,800)
Shares Issue / (Repurchase)	3,598	0	0	0	0
Cost of Dividends Paid	(3,848)	(8,910)	(9,667)	(10,692)	(12,345)
Cash Flow from Financing	13,268	(6,152)	(14,378)	(10,692)	(12,345)
Free Cash Flow	(9,894)	19,687	19,676	10,354	(7,500)
Net Debt	(26,417)	(33,443)	(44,161)	(43,021)	(22,144)
Change in Net Debt	4,268	(2,838)	(9,409)	1,137	20,646

Key Balance Sheet Data

Property, Plant & Equipment	52,199	63,177	87,980	113,788	143,446
Other Non-Current Assets	15,697	20,831	21,821	22,941	24,141
Trade Receivables	139,460	137,900	145,604	150,668	175,312
Cash & Equivalents	43,914	56,998	63,005	61,865	40,988
Other Current Assets	112,473	106,837	106,706	115,382	120,288
Total Assets	363,743	385,743	425,117	464,644	504,175
Long-Term Debt	12,750	16,389	13,111	13,111	13,111
Other Non-Current Liabilities	1,692	2,057	2,057	2,057	2,057
Short-Term Debt	4,747	7,166	5,733	5,733	5,733
Other Current Liabilities	201,395	178,829	205,498	228,386	251,606
Total Liabilities	220,584	204,441	226,399	249,287	272,507
Total Equity	143,162	181,301	198,718	215,357	231,668
Total Equity & Liabilities	363,746	385,742	425,117	464,645	504,175

iQmethodSM - Bus Performance*

Return On Capital Employed	11.4%	12.7%	8.8%	10.6%	11.4%
Return On Equity	17.2%	18.8%	14.3%	13.2%	12.8%
Operating Margin	3.6%	3.8%	3.1%	3.6%	3.8%
EBITDA Margin	4.5%	4.1%	3.5%	4.0%	4.3%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	0.4x	1.3x	1.8x	1.5x	1.0x
Asset Replacement Ratio	4.0x	9.1x	10.3x	7.9x	7.2x
Tax Rate (Reported)	23.3%	20.4%	24.2%	21.5%	23.3%
Net Debt-to-Equity Ratio	-18.5%	-18.4%	-22.2%	-20.0%	-9.6%
Interest Cover	45.4x	35.7x	NA	NA	NA

Key Metrics

Stock comp. adjusted ROIC	8.0%	11.1%	7.7%	9.8%	10.5%
Stock comp. adjusted ROE	12.0%	15.4%	12.8%	11.9%	11.5%
Stock comp. adjusted EPS	3.37	5.74	6.38	6.44	6.75
Stock comp. adjusted P/E	15.62x	9.17x	8.25x	8.17x	7.79x

* For full definitions of iQmethodSM measures, see page 10.

Company Description

Asustek Computer Inc. has expanded into notebook PCs, optical disk drivers, handsets & desktop PCs, in addition to its leading position in graphic cards & motherboards for desktop PCs. Asustek is the largest motherboard manufacturer, with about 30% of global share for both brand and key OEM customers - Intel, HP, & Dell. It has emerged as one of top 10 branded notebook PC names and supplies notebook PCs to Apple and Sony.

Investment Thesis

Our investment thesis includes a) strong growth for notebook PCs, b) leading position at emerging sub-NB PCs, c) Highly leveraged to fast-growing emerging regions-Russia/China, d) only 5pct of sales in the US, e) lower impacts from increase in labor costs in China and strength in currency (RMB/TWD), f) leading brand at motherboards/graphic cards with stable pricing, g) potential cost saving from new suppliers.

Stock Data

Price to Book Value 1.1x

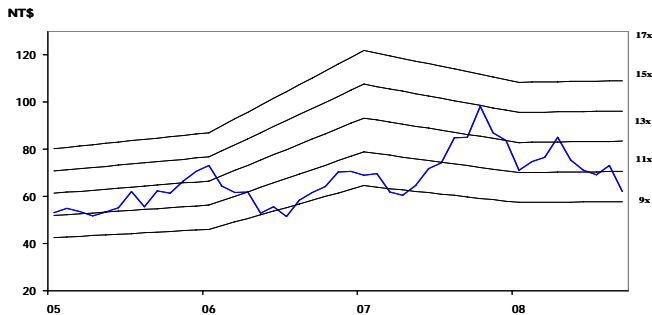
Buy reiterated with lower PO

We cut our 2008/09 earnings by 2%/13% due to lower ASP/GP margin and higher Opex, despite improvement in ODM business from 3Q08. Our new PO of NT\$68.0, down from NT\$84.7, is based upon our sum-of-parts valuation — 11x core EPS (NT\$58.0) plus 8x investment income (NT\$10.0) for 2009.

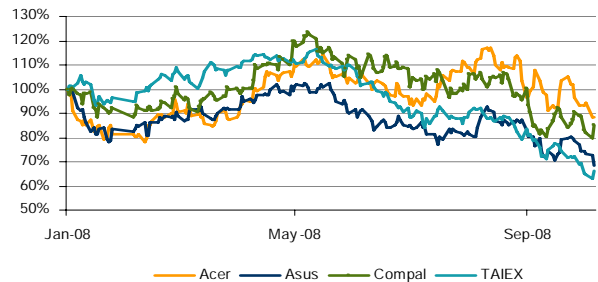
Table 1: Asustek- Reducing estimates for 2008/9

NT\$m	New		Diff.		YoY 2009E	Old	
	2008E	2009E	2008E	2009E		2008E	2009E
Sales	285,212	328,983	-2%	-9%	15%	291,193	363,021
Gross Profit	62,419	67,505	-5%	-14%	8%	65,409	78,566
Operating expense	(40,130)	(44,093)	2%	-6%	10%	(39,433)	(47,037)
Operating Profit	22,289	23,411	-14%	-26%	5%	25,976	31,529
Non-Op	10,791	10,540	8%	16%	-2%	9,970	9,103
Investment Income	5,618	6,150	36%	41%	9%	4,118	4,350
Others	5,173	4,390	-12%	-8%	-15%	5,852	4,753
Pre-tax Profit	33,079	33,951	-8%	-16%	3%	35,946	40,632
Net Profit	27,084	27,331	-2%	-13%	1%	27,658	31,507
EPS (NT\$)	6.38	6.44				6.51	7.42
GPM	21.9%	20.5%				22.5%	21.6%
Opex	-14.1%	-13.4%				-13.5%	-13.0%
OPM	7.8%	7.1%				8.9%	8.7%
Pre-tax Margin	11.6%	10.3%				12.3%	11.2%
Net margin	9.5%	8.3%				9.5%	8.7%
Tax Rate	-18.1%	-19.5%				-23.1%	-22.5%

Source: Merrill Lynch estimates

Chart 1: Asustek- Forward Taiwan-GAAP PE


Source: Merrill Lynch estimates

Chart 2: Asustek: Inline performance vs Taiex


Source: Bloomberg

Table 2: Asustek-valuation comparison

	ML Symbol	ML Rating	Price 20-Oct-08	Mkt Cap (US\$m)	EPS (Local)		EPG		PER(x)		ROE (%)		Cash Yield	Price YTD
					2008E	2009E	2008E	2009E	2008E	2009E	2008E	2009E		
HTC	HTCCF	C-2-7 Neutral	435.0	10,594	40.88	49.58	7%	21%	10.6	8.8	51%	55%	6%	1%
Acer	ASIYF	C-1-7 Buy	47.6	3,799	4.95	5.36	-2%	8%	9.6	8.9	16%	17%	7%	-18%
Asustek	AKCPF	C-1-7 Buy	52.6	7,205	6.38	6.44	-11%	1%	8.2	8.2	14%	13%	3%	-46%
Compal	CMLPF	C-1-7 Buy	22.6	2,866	3.32	3.69	-4%	11%	6.8	6.1	16%	17%	11%	-36%
Wistron	WICOF	C-2-7 Neutral	31.8	1,553	4.80	5.50	10%	15%	6.6	5.8	21%	22%	8%	-47%
Hon Hai	HNHAF	C-2-7 Neutral	84.0	20,090	8.91	10.96	-15%	23%	9.4	7.7	16%	18%	3%	-58%
Lenovo	LNVEF	C-2-7 Neutral	HK\$2.6	2,918	0.35	0.39	-7%	11%	7.3	6.6	26%	25%		-63%
Dell	DELL	C-1-9 Buy	US\$13.4	28,565	1.37	1.45	20%	6%	9.8	9.2	74%	79%		-45%
HPQ	HPQ	B-1-7 Buy	US\$41.0	108,882	3.62	4.30	24%	19%	11.3	9.5	29%	36%		-18%

Source: Bloomberg, Merrill Lynch estimates

Mixed bag for 3Q08

With solid demand in China/Eastern Europe for NB/Eee PCs, Asustek's 3Q revenue increased 35% QoQ, ahead of its target of 30%. The upside came from stronger shipments across all NB PCs, Eee PCs and even motherboards in September.

Our checks also suggest Pegatron could double its earnings due to robust revenue, improved efficiency and FX rate swings. However, we expect OPM to decline 70bp QoQ to 6.9% (vs its target of up 100-200bp), due to higher promotion fees/employee bonus.

Looking ahead, Asustek expects 4Q revenue to grow QoQ (~10% level) due to sequential growth from both NB PCs and Eee PCs, despite flat motherboards.

Table 3: Assutek: Sep/3Q results vs target

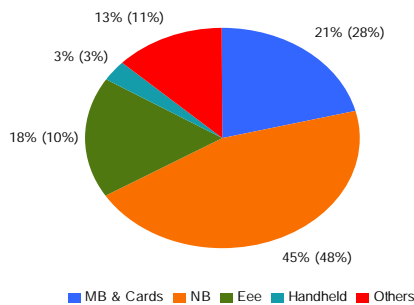
	Sep	MoM	Actual in 3Q	QoQ	Target
NB PCs	0.7mn	30%	1.7mn	40%	1.5-1.8mn
Motherboards		>10%		20%	
Eee PCs	0.6-0.7mn	>20%	1.6mn+	70%	1.5-1.8mn
Sales	NT\$30.3bn	17%	NT\$78.3bn	35%	30%

Source: Asustek

NB/Eee PCs remain the growth driver for 2009

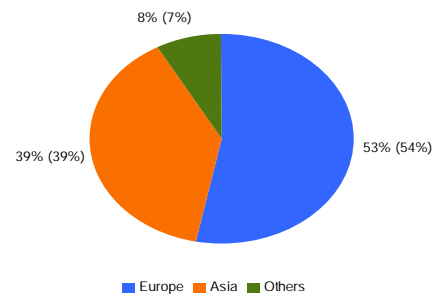
We expect Asustek to grow brand revenue by 15% YoY (vs 25% prev.) for 2009, driven by both NB PCs (up 28% from 6mn in 08E) and Eee PCs (up 42% YoY from 5mn for 08E), despite a mild decline in motherboards. Asustek should benefit from the wave of Netbooks (as it is the pioneer) and its strong position in major emerging countries (ie, China/Russia), where demand remains strong.

Chart 3: Asustek: sales breakdown by product for 2Q08 (1Q)



Source: Asustek

Chart 4: Asustek: sales breakdown by region for 2Q08 (1Q)



Source: Asustek

Pegatron to recover in 2H08

Pegatron's management expects 4Q revenue to be flattish QoQ from NT\$146.6bn in 3Q (See Chart 5), due to a high base for 3Q (up 45% QoQ) and sequential decline for DT PC/motherboards, despite a moderate increase of notebook PCs. Therefore, Pegatron could reach the low-end of its revenue target of NT\$500-500bn for 2009. In addition, Pegatron indicated that 3Q earnings could improve to NT\$2bn level (OPM of 1.0-1.5%, in our estimation), up over 100% QoQ, due to strong revenue, lower inventory write-down, swing on FX rate and improved efficiency.

Looking ahead, Pegatron expects revenue for 2009 to grow 30% YoY, largely driven by strong growth of NB PCs (from Asustek and Toshiba; close to 9mn for 2008E) and consumer devices (likely game consoles from Nintendo or even for Apple's iPhone). Its OPM target of 2.0% seems stretched given its delivery for 2008 and diversified product lines (See Chart 6). In Taiwan, the top 3 NB PC ODMs enjoy OPM of 2-3% while Hon Hai's OPM could be higher at 4-5% given its higher in-house components.

Adding new customers

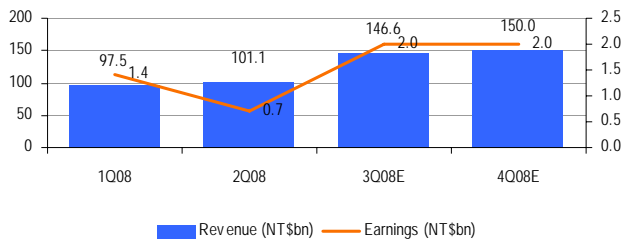
Pegatron's parent (Asustek) is the largest customer and accounts for about 50% of revenue in 2008 and 70% of NB PC shipments. Other major customers include HP for consumer DT PCs and Sony for PS3s. Orders (including NB PCs and barebone DT PCs) from Dell have decreased, partially offset by increased orders from HP, due to lower profitability and Dell's concerns on conflict of interest.

Pegatron indicated that it ramped up new consumer NB PC models for Lenovo from 3Q08 and regained orders from Toshiba from 1H09, given its strength in industrial design (similar to Wistron) and decent execution. However, at the same time, our checks suggest that Asustek has offered new contracts to other suppliers, such as Hon Hai for NB PCs, Flextronics for DT PCs/motherboards and Quanta for all-in-one LCD PCs from 1Q2009.

Slow pace in changing shareholding structure

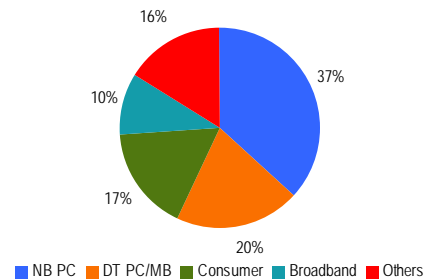
Management reiterates its listing timetable — within three years — by reducing Asustek's holding to below 70%. However, the divesture pace has been slower than expected, due to weaker profitability and tougher equity market. Asustek's stake of 100% will be slightly diluted in 2008 only due to employee stock bonus. In addition, Pegatron claims that itself, rather than Asustek, has the autonomy to decide which investors it wants to bring in. The company stated that it prefers to bring in financial investors (The company denied the speculation on potential alliance with Hon Hai).

Chart 5: Pegatron- Quarterly revenue and earnings for 2008E



Source: Pegatron, Merrill Lynch estimates

Chart 6: Pegatron- revenue mix by product for 2008



Source: Pegatron, Merrill Lynch estimates

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Table 4: Asustek- Consolidated quarterly Income Statement for brand

NT\$m	1Q08	2Q08	3Q08E	4Q08E	1Q09E	2Q09E	3Q09E	4Q09E	2008E	2009E	2010E
Sales	62,967	58,062	78,304	85,879	71,095	72,018	86,582	99,288	285,212	328,983	383,068
Cost of Sales	(49,441)	(44,617)	(60,994)	(67,742)	(56,324)	(57,739)	(68,752)	(78,664)	(222,793)	(261,479)	(309,590)
Gross Profit	13,527	13,445	17,311	18,137	14,771	14,279	17,830	20,624	62,419	67,505	73,478
Promotion	(4,471)	(6,795)	(8,770)	(9,103)	(6,967)	(7,778)	(8,225)	(9,333)	(29,139)	(32,304)	(35,817)
ADM	(693)	(627)	(830)	(927)	(754)	(749)	(883)	(993)	(3,077)	(3,379)	(3,754)
R&D Exp	(1,699)	(1,626)	(2,271)	(2,319)	(1,848)	(1,872)	(2,208)	(2,482)	(7,914)	(8,411)	(9,194)
Operating Expense	(6,862)	(9,048)	(11,871)	(12,349)	(9,569)	(10,399)	(11,316)	(12,808)	(40,130)	(44,093)	(48,765)
Operating Profit	6,664	4,397	5,440	5,787	5,202	3,880	6,514	7,816	22,289	23,411	24,713
Non-operating Income	2,770	2,220	2,800	3,000	2,610	2,260	2,660	3,010	10,791	10,540	11,560
Net Interest Income	108	9	50	50	60	60	60	60	217	240	260
Investment Income	838	980	2,000	1,800	1,550	1,350	1,550	1,700	5,618	6,150	6,700
Exchange Gain	(137)	180	(250)						(207)	0	
Others	1,961	1,051	1,000	1,150	1,000	850	1,050	1,250	5,162	4,150	4,600
Pre-tax Profit	9,435	6,617	8,240	8,787	7,812	6,140	9,174	10,826	33,079	33,951	36,273
Tax Expense	(2,205)	(973)	(1,236)	(1,582)	(1,523)	(1,197)	(1,789)	(2,111)	(5,996)	(6,621)	(7,617)
Net Profit	7,230	5,644	7,004	7,206	6,289	4,943	7,385	8,715	27,084	27,331	28,656
EPS	1.70	1.33	1.65	1.70	1.48	1.16	1.74	2.05	6.38	6.44	6.75
Ratio											
Gross Margin	21.5%	23.2%	22.1%	21.1%	20.8%	19.8%	20.6%	20.8%	21.9%	20.5%	19.2%
Operating Expense	-10.9%	-15.6%	-15.2%	-14.4%	-13.5%	-14.4%	-13.1%	-12.9%	-14.1%	-13.4%	-12.7%
Operating Margin	10.6%	7.6%	6.9%	6.7%	7.3%	5.4%	7.5%	7.9%	7.8%	7.1%	6.5%
Pre-tax Margin	15.0%	11.4%	10.5%	10.2%	11.0%	8.5%	10.6%	10.9%	11.6%	10.3%	9.5%
Net Margin	11.5%	9.7%	8.9%	8.4%	8.8%	6.9%	8.5%	8.8%	9.5%	8.3%	7.5%
Tax Rate	-23.4%	-14.7%	-15.0%	-18.0%	-19.5%	-19.5%	-19.5%	-19.5%	-18.1%	-19.5%	-21.0%
Sequential Growth											
Sales		-8%	35%	10%	-17%	1%	20%	15%		15%	16%
Cost of Sales		-10%	37%	11%	-17%	3%	19%	14%		17%	18%
Gross Profit		-1%	29%	5%	-19%	-3%	25%	16%		8%	9%
Operating Expense		32%	31%	4%	-23%	9%	9%	13%		10%	11%
Operating Profit		-34%	24%	6%	-10%	-25%	68%	20%		5%	6%
Non-operating Income		-20%	26%	7%	-13%	-13%	18%	13%		-2%	10%
Pre-tax Profit		-30%	25%	7%	-11%	-21%	49%	18%		3%	7%
Tax Expense		-56%	27%	28%	-4%	-21%	49%	18%		10%	15%
Net Profit		-22%	24%	3%	-13%	-21%	49%	18%	-2%	1%	5%

Source: Merrill Lynch estimates

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Table 5: Asustek- Consolidated Quarterly Income Statement (bonus-adjusted from 1Q08)

NT\$m	1Q08A	2Q08A	3Q08E	4Q08E	1Q09E	2Q09E	3Q09E	4Q09E	2007A	2008E	2009E	2010E
Sales	176,649	169,051	202,874	225,801	189,017	180,184	217,473	261,563	755,361	774,375	848,237	934,298
Cost of Sales	(157,146)	(149,682)	(178,631)	(200,466)	(168,412)	(161,275)	(193,519)	(232,279)	(680,592)	(685,924)	(755,485)	(835,279)
Gross Profit	19,503	19,369	24,244	25,335	20,605	18,910	23,954	29,284	74,769	88,450	92,752	99,019
Promotion	(7,124)	(9,775)	(11,767)	(12,193)	(8,128)	(9,009)	(10,004)	(11,509)	(29,708)	(40,860)	(38,649)	(38,306)
ADM	(2,256)	(2,420)	(2,678)	(2,890)	(2,363)	(2,198)	(2,610)	(3,086)	(7,288)	(10,244)	(10,257)	(10,651)
R&D Exp	(2,894)	(2,885)	(3,652)	(3,906)	(3,062)	(2,883)	(3,480)	(4,185)	(9,102)	(13,337)	(13,610)	(14,575)
Operating Expense	(12,274)	(15,080)	(18,096)	(18,990)	(13,553)	(14,090)	(16,093)	(18,780)	(46,098)	(64,440)	(62,516)	(63,532)
Operating Profit	7,229	4,289	6,147	6,345	7,052	4,819	7,861	10,503	28,672	24,010	30,236	35,486
Non-operating Income	3,498	2,816	2,587	2,801	916	1,623	1,594	462	9,912	11,701	4,595	1,869
Net Interest Income	131	177	140	160	160	150	160	180	832	608	650	700
Investment Income	107	2	25	25	30	30	30	30	423	159	120	150
Disposal Gain	2	150	30	50	50	50	50	50	(177)	232	200	250
Exchange Gain	792	1,605	800						4,359	3,197	0	
Others	2,466	882	1,592	2,566	676	1,393	1,354	202	4,475	7,505	3,625	769
Pre-tax Profit	10,727	7,104	8,734	9,146	7,969	6,443	9,455	10,965	38,583	35,711	34,831	37,356
Tax Expense	(2,785)	(1,060)	(1,250)	(1,400)	(1,200)	(1,000)	(1,500)	(1,600)	(7,828)	(6,494)	(5,300)	(6,300)
Minority Interest	(712)	(401)	(480)	(540)	(480)	(500)	(570)	(650)	(3,132)	(2,133)	(2,200)	(2,400)
Net Profit	7,230	5,644	7,004	7,206	6,289	4,943	7,385	8,715	27,624	27,084	27,331	28,656
EPS	1.70	1.33	1.65	1.70	1.48	1.16	1.74	2.05	6.51	6.38	6.44	6.75
Ratio												
Gross Margin	11.0%	11.5%	12.0%	11.2%	10.9%	10.5%	11.0%	11.2%	9.9%	11.4%	10.9%	10.6%
Operating Expense	-6.9%	-8.9%	-8.9%	-8.4%	-7.2%	-7.8%	-7.4%	-7.2%	-6.1%	-8.3%	-7.4%	-6.8%
Operating Margin	4.1%	2.5%	3.0%	2.8%	3.7%	2.7%	3.6%	4.0%	3.8%	3.1%	3.6%	3.8%
Pre-tax Margin	6.1%	4.2%	4.3%	4.1%	4.2%	3.6%	4.3%	4.2%	5.1%	4.6%	4.1%	4.0%
Net Margin	4.1%	3.3%	3.5%	3.2%	3.3%	2.7%	3.4%	3.3%	3.7%	3.5%	3.2%	3.1%
Tax Rate	-26.0%	-14.9%	-14.3%	-15.3%	-15.1%	-15.5%	-15.9%	-14.6%	-20.3%	-18.2%	-15.2%	-16.9%
Sequential Growth												
Sales	-19%	-4%	20%	11%	-16%	-5%	21%	20%	35%	3%	10%	10%
Cost of Sales	-20%	-5%	19%	12%	-16%	-4%	20%	20%	35%	1%	10%	11%
Gross Profit	-16%	-1%	25%	5%	-19%	-8%	27%	22%	36%	18%	5%	7%
Operating Expense	-21%	23%	20%	5%	-29%	4%	14%	17%	33%	40%	-3%	2%
Operating Profit	-8%	-41%	43%	3%	11%	-32%	63%	34%	41%	-16%	26%	17%
Non-operating Income	17%	-19%	-8%	8%	-67%	77%	-2%	-71%	24%	18%	-61%	-59%
Pre-tax Profit	-1%	-34%	23%	5%	-13%	-19%	47%	16%	36%	-7%	-2%	7%
Tax Expense	3%	-62%	18%	12%	-14%	-17%	50%	7%	18%	-17%	-18%	19%
Net Profit	9%	-22%	24%	3%	-13%	-21%	49%	18%	44%	-2%	1%	5%
EPS	9%	-22%	24%	3%	-13%	-21%	49%	18%	44%	-2%	1%	5%

Source: Merrill Lynch estimates

Price objective basis & risk

Asustek (AKCPF)

PO of NT\$68.0 is based upon our sum-of-parts valuation -11x core EPS (NT\$58.0) plus 8x investment income (NT\$10.0) for 2009. 11x for its brand business is comparable with other brand companies in Taiwan (Acer and HTC). In addition, 8x for investment income (mainly ODM) is also comparable with the target multiple for other NB PC ODMs. We believe Asustek deserves a premium over PC ODMs in Taiwan, given its brand. We believe its ongoing restructuring might unlock more hidden value and reduce potential conflict of interest, which should be a positive for its valuations. Risks: Slowdown in PC demand, potential conflict of interest between brand and ODM businesses, demand and profitability from Eee PCs.

Analyst Certification

I, Tony Tseng, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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21 October 2008

APR - Technology Hardware Coverage Cluster

Investment rating	Company	ML ticker	Bloomberg symbol	Analyst
BUY				
	Acer, Inc	ASIYF	2353 TT	Tony Tseng, CFA
	Asustek	AKCPF	2357 TT	Tony Tseng, CFA
	BYD	BYDDF	1211 HK	Daniel Kim, CFA
	Catcher Tech	CHERF	2474 TT	Tony Tseng, CFA
	Cheil Industries	CLFUF	001300 KS	Simon Dong-je Woo, CFA
	Chicony Elect	CCNYF	2385 TT	Tina Chang, CFA
	Compal Electron	CMLPF	2324 TT	Tina Chang, CFA
	Coretronic	CCOCF	5371 TT	Jeffrey Su
	Delta Elect	DLTEF	2308 TT	Jeffrey Su
	Foxconn Tech	FXTCF	2354 TT	Tony Tseng, CFA
	InnoLux	INXDF	3481 TT	Jeffrey Su
	Ju Teng Intl	JUTGF	3336 HK	Ronnie Ho
	Kingboard	KBDCF	148 HK	Ronnie Ho
	Largan Precision	LGANF	3008 TT	Laura Chen
	LG Electronics	LGEAF	066570 KS	Daniel Kim, CFA
	Samsung Techwin	SGTWF	012450 KS	Simon Dong-je Woo, CFA
	Shin Zu Shing	SZUSF	3376 TT	Tina Chang, CFA
	Simplo Tech	SPLOF	6121 TT	Tina Chang, CFA
	SSCP CO LTD	SSCPF	071660 KS	Daniel Kim, CFA
	TPV	TPVTF	903 HK	Daniel Kim, CFA
	Venture Corp.	VEMLF	VMS SP	Ronnie Ho
NEUTRAL				
	AU Optronics	AUO	AUO US	Jeffrey Su
	AU Optronics	AUOPF	2409 TT	Jeffrey Su
	Foxconn Intl Hld	FXCNF	2038 HK	Tony Tseng, CFA
	Hon Hai Prec.	HNHAF	2317 TT	Tony Tseng, CFA
	HTC Corp.	HTCCF	2498 TT	Tony Tseng, CFA
	Inventec	IVCJF	2356 TT	Tina Chang, CFA
	Inventec Applian	IVAPF	3367 TT	Tina Chang, CFA
	Lenovo Group	LNVGF	992 HK	Daniel Kim, CFA
	Lenovo Group	LNVGY	LNVGY US	Daniel Kim, CFA
	Qisda Corp	BNQCF	2352 TT	Jeffrey Su
	Radiant	ROPTF	6176 TT	Jeffrey Su
	Silitech	SLKCF	3311 TT	Laura Chen
	Wistron	WICOF	3231 TT	Tony Tseng, CFA
	Yageo Corp	YGEQF	2327 TT	Ronnie Ho
UNDERPERFORM				
	Alpha Networks I	AHNWF	3380 TT	Laura Chen
	Chi Mei Opto	CMEOF	3009 TT	Jeffrey Su
	Compal Comm	CPCMF	8078 TT	Laura Chen
	Epistar Corp	EPIPF	2448 TT	Jeffrey Su
	Everlight Elec	EVLEF	2393 TT	Jeffrey Su
	Gemtek Technolog	GTKTF	4906 TT	Laura Chen
	LG Display Co., Ltd.	LPHLF	034220 KS	Daniel Kim, CFA
	LG Display Co., Ltd.-A	LPL	LPL US	Daniel Kim, CFA
	Lite-On Tech	LOTZF	2301 TT	Jeffrey Su
	Merry Electron	MMECF	2439 TT	Laura Chen
	Mitac Intl	MTCXF	2315 TT	Tina Chang, CFA
	Quanta Computer	QUCPF	2382 TT	Tony Tseng, CFA
	Samsung Elec M	SSEMF	009150 KS	Daniel Kim, CFA
	Samsung SDI	SSDIF	006400 KS	Daniel Kim, CFA
	Seoul Semicon	SLSOF	046890 KS	Simon Dong-je Woo, CFA
	Unisteel Tech	UNSGF	USTL SP	Ronnie Ho
	Wellypower	XTTWF	3080 TT	Jeffrey Su
	ZTE Corp - H	ZTCOF	763 HK	Ronnie Ho

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

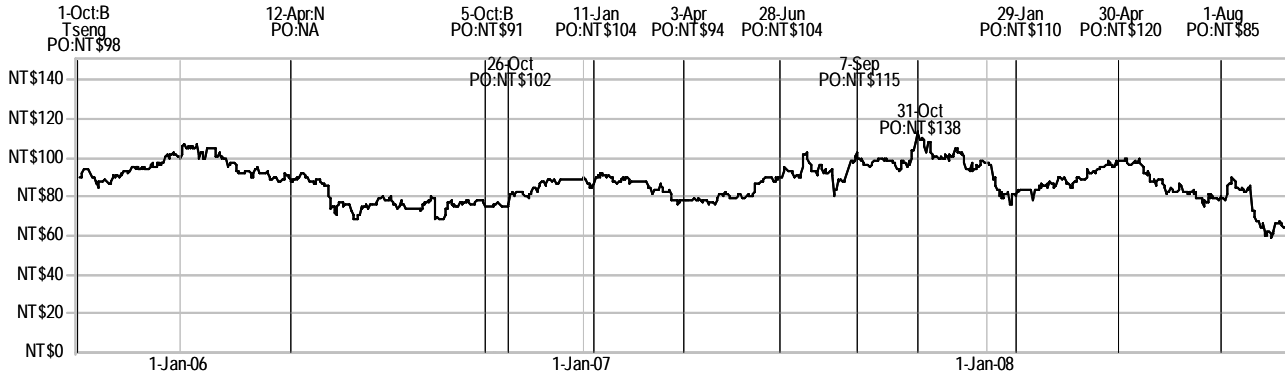
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B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of September 30, 2008 or such later date as indicated.

Investment Rating Distribution: Electronics Group (as of 01 Oct 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	42	40.00%	Buy	8	20.51%
Neutral	32	30.48%	Neutral	3	11.11%
Sell	31	29.52%	Sell	2	7.41%

Investment Rating Distribution: Global Group (as of 01 Oct 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1647	45.31%	Buy	429	28.83%
Neutral	858	23.60%	Neutral	240	31.41%
Sell	1130	31.09%	Sell	227	22.02%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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