

22 October 2008 | 10 pages

Motech Industries (6244.TWO)

 Estimate change
 Results

Sell: In-Line EBIT Margins in 3Q, but Faces Oversupply in 2009E

- Risks to margins** — Motech's 3Q operating margin (13%) was in-line with our forecasts, and EPS was up 51% QoQ to NT\$3.68 due to non-op FX gains. We expect 4Q revenue up 12% qoq as the company ramps up its Fab, but see growing risks to margins in 2009E due to concerns over market oversupply.
- Industry view** — We met with Motech, E-Ton, SAS and Wafer Works at the OTC conference. While TW solar companies have not felt the negative impact from the slowing macro economy, managements do worry about slower demand growth due to defaults by customers or cancellation on government subsidies.
- Results and outlook** — Motech 3Q08 revenue was NT\$6.7bn, +10% qoq and +63% yoy. Gross margin was 15.6%, slightly higher than CIR's 15% due to better product mix. It expects to meet its 2008 target output of 280MW and targets over 500MW output by end of 2009. Motech also plans to raise its long-term wafer supply contracts to 50% (from 30%) and lower its Spot Market exposure to 20% from 1/3 currently.
- Delay in AE Polysilicon** — Due to delay of the environmental evaluation, the company will delay ramp of AE Polysilicon to 3Q09 from 1Q09. AE Polysilicon will provide half of its capacity to Motech, ~900 tons or 90MW next year.
- Revising estimates** — We are revising our 2008E and 2009E EPS estimates to NT\$10.9 and NT\$13.5 respectively to reflect better 3Q results and margin contraction due to pricing pressure and oversupply in 2009E.

Sell/Medium Risk	3M
Price (21 Oct 08)	NT\$123.50
Target price	NT\$136.50
Expected share price return	10.5%
Expected dividend yield	6.5%
Expected total return	17.0%
Market Cap	NT\$30,814M
	US\$945M

Price Performance (RIC: 6244.TWO, BB: 6244 TT)



Motech – Statistical Abstract

Year to 31-Dec	Net profit NT\$mnn	EPS NT\$	EPS YoY	P/E (x)	P/B (x)	ROIC (%)	ROE (%)	I/B/E/S NT\$	% diff
2006A	2,258	10.8	13%	11	4.7	26%	56%		
2007A	2,442	9.9	-8%	13	2.3	16%	26%		
2008E	2,707	10.9	10%	11	2.1	17%	19%	10.3	6%
2009E	3,367	13.5	24%	9	2.0	17%	22%	14.7	-8%
2010E	3,127	12.6	-7%	10	1.8	14%	19%	16.6	-24%

Source: Company Reports and Citi Investment Research estimates

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See Appendix A-1 for Analyst Certification and important disclosures.

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Fiscal year end 31-Dec	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	11.5	12.5	11.4	9.1	9.8
EV/EBITDA adjusted (x)	12.7	9.2	6.5	5.7	5.8
P/BV (x)	4.7	2.3	2.1	2.0	1.8
Dividend yield (%)	0.0	0.0	5.7	6.5	6.5
Per Share Data (NT\$)					
EPS adjusted	10.77	9.87	10.87	13.52	12.55
EPS reported	10.77	9.87	10.87	13.52	12.55
BVPS	26.53	54.22	57.72	63.24	67.79
DPS	0.02	0.01	7.00	8.00	8.00
Profit & Loss (NT\$M)					
Net sales	8,099	15,578	25,299	35,041	40,919
Operating expenses	-5,922	-13,147	-22,199	-31,395	-37,535
EBIT	2,178	2,431	3,100	3,645	3,384
Net interest expense	-2	152	201	74	26
Non-operating/exceptionals	87	-124	-473	-60	-12
Pre-tax profit	2,263	2,459	2,828	3,659	3,399
Tax	-5	-17	-121	-293	-272
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	2,258	2,442	2,707	3,367	3,127
Adjusted earnings	2,258	2,442	2,707	3,367	3,127
Adjusted EBITDA	2,378	2,922	3,857	4,799	4,867
Growth Rates (%)					
Sales	88.2	92.3	62.4	38.5	16.8
EBIT adjusted	83.7	11.6	27.5	17.6	-7.2
EBITDA adjusted	78.6	22.9	32.0	24.4	1.4
EPS adjusted	13.4	-8.4	10.1	24.4	-7.1
Cash Flow (NT\$M)					
Operating cash flow	1,577	1,528	701	2,078	3,018
Depreciation/amortization	200	491	757	1,153	1,483
Net working capital	-873	-1,419	-2,763	-2,442	-1,592
Investing cash flow	-3,513	-3,387	-1,813	-1,514	-1,514
Capital expenditure	-1,788	-808	-1,800	-1,500	-1,500
Acquisitions/disposals	-1,724	-2,358	-13	-14	-14
Financing cash flow	3,246	5,781	-625	-1,993	-993
Borrowings	2,327	260	1,119	0	1,000
Dividends paid	-554	-346	-1,743	-1,993	-1,993
Change in cash	1,310	3,922	-1,736	-1,428	511
Balance Sheet (NT\$M)					
Total assets	9,050	17,573	20,413	22,551	25,171
Cash & cash equivalent	1,615	5,428	3,704	2,290	2,815
Accounts receivable	1,058	1,113	3,119	4,224	4,933
Net fixed assets	2,604	2,921	3,964	4,310	4,327
Total liabilities	3,491	4,160	6,037	6,801	8,286
Accounts payable	322	570	970	1,375	1,644
Total Debt	2,621	2,881	4,000	4,000	5,000
Shareholders' funds	5,560	13,413	14,377	15,751	16,885
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	29.4	18.8	15.2	13.7	11.9
ROE adjusted	56.0	25.7	19.5	22.3	19.2
ROIC adjusted	61.7	43.0	35.5	28.7	22.4
Net debt to equity	18.1	-19.0	2.1	10.9	12.9
Total debt to capital	32.0	17.7	21.8	20.3	22.8

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Motech – Earnings Revisions

Year to 31-Dec	Net Profit (NT\$ mn)		Diluted EPS		
	Old	New	Old	New	% Chg
2008E	2,612	2,707	10.49	10.87	3.6%
2009E	3,576	3,367	14.36	13.52	-5.9%
2010E	3,204	3,127	12.87	12.55	-2.4%

Source: Citi Investment Research estimates

Figure 1. Motech – Quarterly Income Statement (2006-2010E, NT\$ in Millions)

NT\$ in mn	2007					2008E					2009E					2010E					
	FYE '06	1Q	2Q	3Q	4Q	FYE '07	1Q	2Q	3Q	4QE	FYE '08	1Q	2Q	3Q	4Q	FYE '09	1Q	2Q	3Q	4Q	FYE '10
NET REVENUES	8,099	3,308	3,676	4,132	4,462	15,578	4,902	6,096	6,736	7,564	25,299	7,727	8,695	9,428	9,191	35,041	9,156	10,130	10,732	10,900	40,919
Total cost of good sold	(5,619)	(2,500)	(3,000)	(3,407)	(3,680)	(12,587)	(4,086)	(5,221)	(5,685)	(6,419)	(21,412)	(6,591)	(7,472)	(8,233)	(8,063)	(30,359)	(7,962)	(8,969)	(9,595)	(9,770)	(36,296)
GROSS PROFIT	2,480	808	676	725	782	2,991	816	876	1,051	1,145	3,887	1,136	1,222	1,195	1,128	4,682	1,194	1,161	1,137	1,131	4,623
R&D	(45)	(25)	(30)	(67)	(70)	(192)	(63)	(88)	(119)	(103)	(372)	(107)	(131)	(133)	(141)	(512)	(92)	(203)	(107)	(218)	(619)
SG&A	(258)	(80)	(84)	(97)	(107)	(368)	(92)	(144)	(84)	(95)	(415)	(99)	(146)	(123)	(157)	(524)	(92)	(203)	(107)	(218)	(619)
Operating expenses	(303)	(105)	(114)	(164)	(177)	(560)	(155)	(232)	(203)	(198)	(788)	(206)	(276)	(256)	(298)	(1,036)	(183)	(405)	(215)	(436)	(1,239)
OPERATING INCOME	2,178	703	562	561	605	2,431	661	644	848	947	3,100	930	946	938	831	3,645	1,011	756	922	695	3,384
Int&other inc/(exp)	85	63	(59)	43	(20)	28	(416)	(17)	127	34	(271)	(6)	1	12	6	14	(6)	1	13	6	15
PRETAX INCOME	2,263	766	503	604	585	2,459	245	627	975	981	2,828	924	947	951	837	3,659	1,005	757	936	701	3,399
Taxes credit (exp)	(5)	-	18	(61)	27	(17)	24	(18)	(59)	(69)	(121)	(74)	(76)	(76)	(67)	(293)	(80)	(61)	(75)	(56)	(272)
NET INCOME	2,258	766	521	543	612	2,442	269	608	917	913	2,707	850	872	875	770	3,367	925	696	861	645	3,127
Earnings per share	10.77	3.10	2.11	2.20	2.47	9.87	1.08	2.44	3.68	3.66	10.87	3.41	3.50	3.51	3.09	13.52	3.71	2.80	3.46	2.59	12.55
Fully diluted shares (mn)	210	247	247	247	247	247	249	249	249	249	249	249	249	249	249	249	249	249	249	249	249
Operating Ratios																					
Gross margins	31%	24%	18%	18%	18%	19%	17%	14%	16%	15%	15%	15%	14%	13%	12%	13%	13%	11%	11%	10%	11%
R&D	-1%	-1%	-1%	-2%	-2%	-1%	-1%	-2%	-2%	-1%	-1%	-1%	-2%	-1%	-2%	-1%	-1%	-2%	-1%	-2%	-2%
SG&A	-3%	-2%	-2%	-2%	-2%	-2%	-2%	-1%	-1%	-1%	-2%	-1%	-2%	-1%	-2%	-1%	-1%	-2%	-1%	-2%	-2%
Operating margin	27%	21%	15%	14%	14%	16%	13%	11%	13%	13%	12%	12%	11%	10%	9%	10%	11%	7%	9%	6%	8%
Pre-tax margin	28%	23%	14%	15%	13%	16%	5%	10%	14%	13%	11%	12%	11%	10%	9%	10%	11%	7%	9%	6%	8%
Net margin	28%	23%	14%	13%	14%	16%	5%	10%	14%	12%	11%	11%	10%	9%	8%	10%	10%	7%	8%	6%	8%
Year-to-Year %																					
Net revenues	88%	366%	75%	86%	45%	92%	48%	66%	63%	70%	62%	58%	43%	40%	22%	39%	18%	17%	14%	19%	17%
Gross profit	74%	630%	-3%	5%	-20%	21%	1%	29%	45%	46%	30%	39%	40%	14%	-1%	20%	5%	-5%	-5%	0%	-1%
Operating income	84%	1055%	-10%	-9%	-31%	12%	-6%	15%	51%	56%	27%	41%	47%	11%	-12%	18%	9%	-20%	-2%	-16%	-7%
Pretax income	94%	1428%	-21%	-13%	-33%	9%	-68%	25%	61%	68%	15%	277%	51%	-3%	-15%	29%	9%	-20%	-2%	-16%	-7%
Net income	95%	1428%	-18%	-22%	-30%	8%	-65%	17%	69%	49%	11%	216%	43%	-5%	-16%	24%	9%	-20%	-2%	-16%	-7%
Qtr-to-Qtr %																					
Net revenues		7%	11%	12%	8%		10%	24%	10%	12%		2%	13%	8%	-3%		0%	11%	6%	2%	
Gross profit		-18%	-16%	7%	8%		4%	7%	20%	9%		-1%	8%	-2%	-6%		6%	-3%	-2%	-1%	
Operating income		-20%	-20%	0%	8%		9%	-3%	32%	12%		-2%	2%	-1%	-11%		22%	-25%	22%	-25%	
Net income		-12%	-32%	4%	13%		-56%	126%	51%	0%		-7%	3%	0%	-12%		20%	-25%	24%	-25%	

Source: Company Reports and Citi Investment Research estimates

Motech Industries

Company description

Established in 1981 as an electronic meter test and measurement equipment manufacturer, Motech began producing solar cells in 1999 at the Tainan Science Industrial Park. In 2005, it had output of 60MW, or a 3% global market share, and was ranked #9 globally with 95% of sales from solar cells.

Investment strategy

We rate Motech shares Sell / Medium Risk (3M) with TP of NT\$136.5. We are negative on the solar sector in Taiwan, as we view the risk/reward profile as no longer attractive. With more uncertainties evolving the magnitude of subsidy reduction, while supply of poly-si is loosening in the spot market, both share prices and earnings forecasts could be vulnerable. We view the likelihood of further upward estimate revisions as low.

Valuation

Our target price of NT\$136.5 is based on 9-10x 2009E earnings, in line with our valuation multiple for peer Gintech. The multiple also reflects the global sector re-valuation and the potential for much slower growth due to difficulty in financing in current environment. Although Motech may continue to see strong CAGR in the next three years, we believe a cautious valuation multiple is warranted given the rapid drop in economic confidence may lead to a slower take-up in the solar sector in the near-term. From a book value perspective, our target multiple equates 2.1-2.3X P/B, also in line with our target for peer Gintech.

Risks

We rate Motech shares Medium Risk based on our quantitative risk-rating system, which tracks 260-day historical share-price volatility. Upside risks that could cause the shares to exceed our target price include: 1) a renewal of favorable subsidy program; 2) new competitors cannot ramp up smoothly due to a lack of economies of scale and other factors. Downside risks include: 1) polysilicon price falling more than expected; 2) reliance on a few material suppliers; 3) competition in solar cell is intensifying; 4) cancellation of government subsidy will impact global demand for PV cells.

Gintech Energy (3514.TW; NT\$143.00; 2M)

Valuation

Our target price of NT\$172 equates to 9-10x 2009E earnings. Due to Gintech's smaller scale, shorter operating history, and less diversified supply sources, our target assumes a 50% discount to our target multiple for market leader Q-Cells. Our target price is also equivalent to a P/BV of 2.3-2.5x to reflect ongoing risks on margins and slower demand growth amid global economic slowdown. The P/BV multiple is particularly relevant given the challenges in fund raising in current environment may hamper near-term growth prospects, and see its stock likely to remain near its trough book valuation.

Risks

We assign a Medium Risk rating to Gintech shares as the company has secured nearly 100% of its raw materials supplies in 2008 (vs. industry average of 50-70%), and therefore we see little risks to our shipments forecast in the near- to medium-term. The Medium Risk rating for Gintech is also fairly consistent with that assigned to other supply-chain players under our global coverage.

Risks that could prevent the stock from reaching our target price include: 1) polysilicon price falling more than expected; 2) reliance on a few material suppliers; 3) competition in solar cells is intensifying; and 4) cancellation of government subsidy will impact global demand for PV cells. Conversely, upside risks to our target price include: 1) a renewal of favorable subsidy program; and 2) new competitors fail to ramp up smoothly due to lack of economies of scale.

Appendix A-1

Analyst Certification

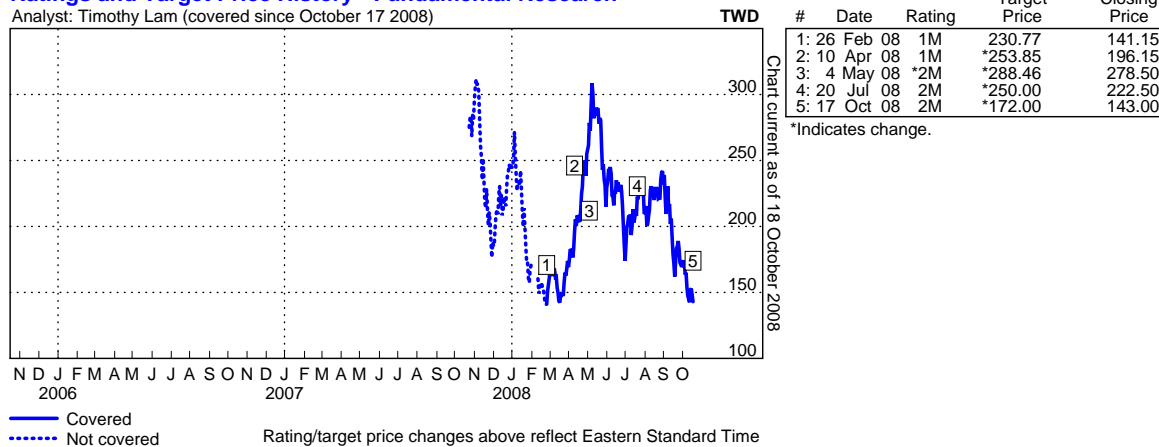
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Gintech Energy (3514.TW)

Ratings and Target Price History - Fundamental Research

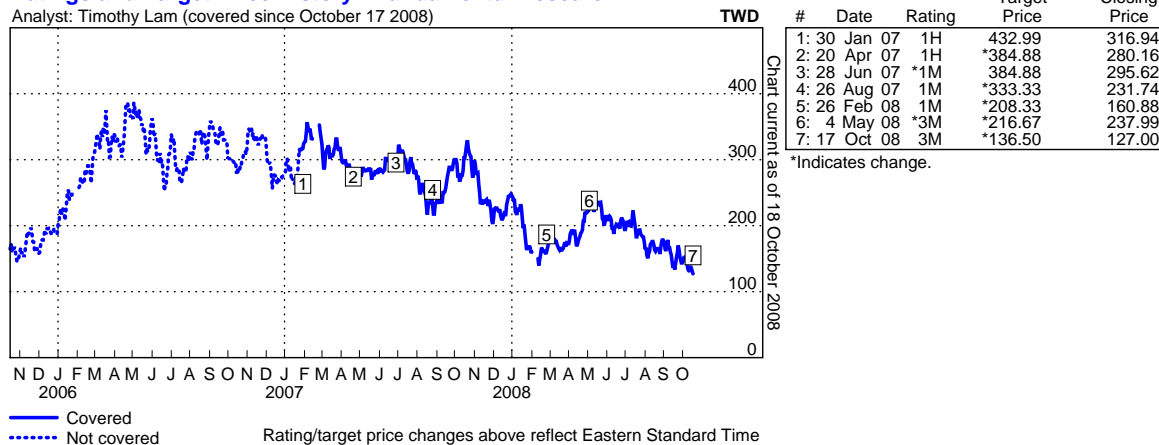
Analyst: Timothy Lam (covered since October 17 2008)



Motech Industries (6244.TWO)

Ratings and Target Price History - Fundamental Research

Analyst: Timothy Lam (covered since October 17 2008)



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Motech Industries (6244.TWO)

22 October 2008

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