

## High Tech Computer (HTC)

Cutting global smartphone forecast, HTC relatively robust for next 2 quarters on strong G1 backlog

- Cut PT, stay OW on good earnings visibility/ product launch:** We cut our PT from NT\$560 (Dec-09) to NT\$400 (Jun-09) to reflect our 6%/10%/14% EPS cut for FY08E-10E, and we lower our FY09E P/E multiple from 15x to 12x (8-20x historical range). Still, we expect HTC to outperform the index in the next two quarters due to 1) better earning visibility due to G1 backlog; 2) event-driven angle from new Google phones coming in 1H09 for multiple operators. Key risk is operator subsidy trend.
- Cutting global smartphone forecast, TCO brought back to focus:** We trim our Y/Y growth forecast for FY09/10 from 25%/50% to 15%/40%. Smartphone has been the “last man standing” among tech products, thanks to “killer application” in mobile broadband, and hefty operator subsidy. But subsidy is ultimately a financing scheme by operators; consumers still need to pay some US\$600 extra on a two-year total cost of ownership (TCO) basis. This has worked when consumers are certain about their income, but they may hesitate to commit such cash flow when confidence is hit hard. Operator data revenue already shows signs of deceleration for some quarters, and if that continues, it may hurt the operator subsidy budget for smartphone.
- HTC not feeling the pinch yet due to G1 backlog, but WM slowing:** Over the last few months, we spot order cuts by Apple and RIM in the supply chain. While G1 has almost doubled market expectations, HTC keeps 4Q08 revenue guidance at NT\$48B. We estimate Windows Mobile volume is flattish Q/Q vs. historical 4Q seasonality of ~30% Q/Q, suggesting HTC is somewhat affected by the downturn, but Y/Y growth in the next two quarters looks relatively robust thanks to strong G1 backlog.
- Right ingredients for strong rebound when market recovers:** In our view, HTC has the best state-of-the-art product in two of the four key smartphone operating systems, in a market that is still early in the product cycle. Trading at a single-digit P/E, it offers 10% cash dividend yield, with net cash at 20+% of total market cap. HTC is also taking advantage of current market turmoil to beef up its capability – we expect a small acquisition in handset industrial design in the coming months, which may help HTC compete more effectively with major brands in mainstream handset market in the long run.

Reuters: 2498.TW; Bloomberg: 2498 TT

NT\$ in billions, year-end Dec

	FY07	FY08E	FY09E	FY10E		FY07	FY08E	FY09E	FY10E		
Sales	118.6	153.2	152.4	186.5	Y/E BPS (NT\$)	75.8	77.2	85.0	90.3	52-Week range	NT\$274.5-682.3
Operating Profit	31.0	29.8	27.6	33.7	P/B (x)	4.0	3.9	3.5	3.3	Shares Outstg (Com)	755,394Mn
Pretax profit	32.2	31.1	28.8	35.1	ROE (%)	41.5	48.9	39.3	43.7	Free float	70%
MV of Employee Bonus	6.3	6.8	5.5	6.6	Cash Div (NT\$)	27.0	34.0	30.0	26.8	Avg daily volume	9.0Mn
Adj. Net Profit (New TW GAAP)	23.3	28.2	25.3	30.4	Cash Div Yield	9.0%	11.3%	10.0%	8.9%	Avg daily value	US\$137.3mn
Old TW GAAP net profit	28.9	35.5	30.2	36.1	Quarterly EPS (NT\$)	1Q	2Q	3Q	4Q	Dividend Yield (%)	11.3
New Taiwan GAAP EPS (NT\$)	31.5	37.7	33.4	39.4	EPS (FY08) E	9.3	8.9	9.4	10.2	Index	4,160.54
New Taiwan GAAP P/E (x)	9.6	8.0	9.0	7.6	EPS (FY09) E	7.6	6.6	8.9	10.3	Exchange rate	NT\$33.4/US\$1
Cash (NT\$B)	55.1	63.6	68.9	76.2	DCF value (12/2009)					Market cap	NT\$227B
Equity	56.1	57.7	64.4	69.5	Target Price (12/2009)					US\$6.8B	
										QFIL holding (%)	49.64

Source: Datastream, company, J.P. Morgan estimates. \*Retroactive adjustment for employee bonus expense is done for like-to-like comparison; price date 24 Nov 08

See page 8 for analyst certification and important disclosures, including non-US analyst disclosures.

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## Overweight

2498.TW, 2498 TT

Price: NT\$300.00

▼ Price Target: NT\$400.00  
Previous: NT\$560.00

### Taiwan

#### Computer Hardware

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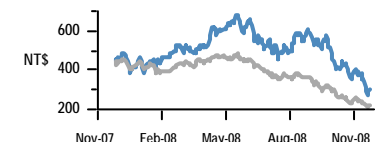
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#### Price Performance



	YTD	1m	3m	12m
ABS	-34.9%	-23.4%	-46.8%	-32.2%
REL	16.2%	-14.2%	-7.0%	19.0%

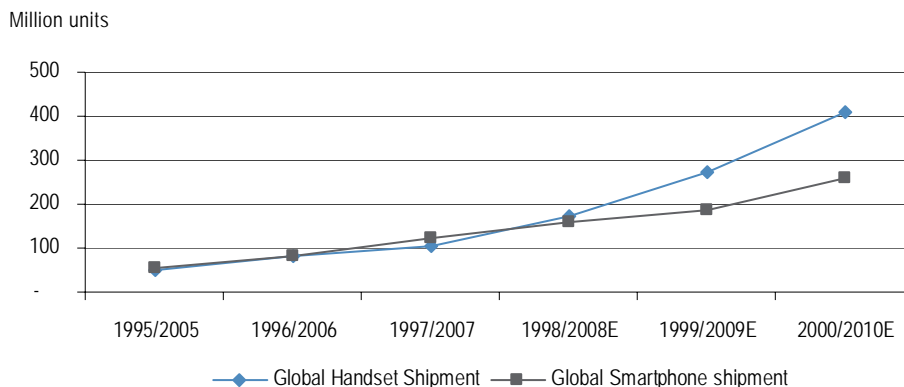
## Bringing down global smartphone unit estimates

If we look at the sequence of how different end markets have slowed in past quarters, it starts with “nice-to-have” type of products like GPS, digital photo frame, etc., back in Christmas last year, and followed by TV in 1Q09. Next to come was “cheaper good effect” for “need-to-have” type of products like PCs and handsets, and then volume also started to break down recently.

Smartphone has been the “last man standing” among tech products, thanks to “killer application” in mobile broadband and hefty subsidy by operators. Yet, subsidy is ultimately a financing scheme by operators, who recoup the investment in 18 to 24 months of data contracts. Overall, consumers still need to pay some US\$600 extra on a two-year total cost of ownership (TCO) basis – it works at times when consumers are certain about their jobs, but they may hesitate to commit such cash flow when confidence is hit hard as we see happening now.

We previously forecast smartphone unit growth at 25%/50% for 2009/2010, which already assumed a weak macro economy. However, as our economists now call for the worst global consumer recession since the 1980s, we further trim down our forecast to 15%/40% unit growth for 2009/2010. Back in 1999/2000, voice handset unit growth was 58%/51%, and over the past few years data has been lagging voice trends for 10 years, so our estimates represent a very substantial discount to the trend growth of data.

Figure 1: Global handset shipment: Data lags voice by 10 years

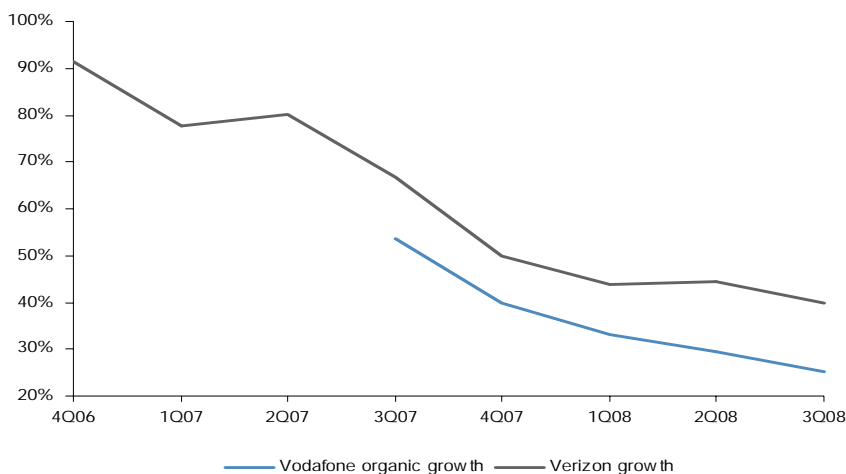


Source: Nokia, J.P. Morgan estimates.

## Data revenue showing signs of deceleration, operator subsidy budget may get hurt

Data revenue may not move exactly in line with smartphone volume, as there are two moving parts in data -- ARPU change and subscriber growth. Still, it likely matters to smartphone, as subsidy budget is likely a fraction of data revenue. If operators have to cut data plan to stimulate demand, it is likely that subsidy per phone would be reduced as well, unless they are willing to reduce the near-term profit for longer-term reasons.

Figure 2: Operators: Data revenue Y/Y growth



Source: Company data

### HTC – Not hurt by current turmoil? Probably more accurate to say it is offset by strong G1 launch, so far

HTC President Peter Chou upped the year-end G1 shipment target to 1mn during a recent public event (vs. market expectations of some 500-600k), yet maintained 4Q08 revenue guidance at 20-30% Q/Q growth. G1 is accounting for close to 20-25% of 4Q wireless volume, implying rather flattish Windows Mobile volume.

With the exception of 4Q06 (up 13% Q/Q) which is partially hurt by ODM share loss, HTC recorded over 30% Q/Q revenue growth in most other 4Qs in the past, due to heavy tilt in Europe seasonality. G1 cannibalization effect should be limited at this point given it is only available at a single operator at this stage, even though there might still be some waiting element for Google phone. The muted Windows Mobile shipment therefore does seem to be affected by the weak macro, just like the order cut news we hear at Apple and RIM.

Still, in aggregate, we believe HTC should have relatively good visibility in the coming two quarters, until G1 shortage is resolved. We might see HTC top line growth moving more in line with industry growth by 2Q09.

### Earnings estimate changes

- Our shipment cut largely reflects slower global smartphone growth. We also assume faster Google phone share gain at the expense of Windows Mobile.
- We are not changing like-to-like margin assumption, though higher mix in G1 would mean weaker margin in next two quarters.
- We have previously mixed up the 4Q08 employee bonus guidance. Post clarification with the company, our understanding is that NT\$616MM is not the full amount of employee bonus, but rather a one-off additional amount on top of the regular 18% net profit after tax dilution.

Table 1: Earnings change table

NT\$ in millions

	3Q08 Actual	4Q08 Revised	Previous Estimate	Chg	FY08 Revised	Previous Estimate	Chg	FY09 Revised	Previous Estimate	Chg
Revenue	37,859	48,026	47,989	0.1%	153,208	153,171	0.0%	152,445	168,479	-9.5%
Gross profit	12,931	14,371	14,548	-1.2%	50,915	51,093	-0.3%	45,828	50,996	-10.1%
Gross margin (%)	34.2%	29.9%	30.3%	-39 bps	33.2%	33.4%	-12 bps	30.1%	30.3%	-21 bps
Operating profit	7,227	8,156	8,310	-1.9%	29,755	29,909	-0.5%	27,607	30,842	-10.5%
Operating margin (%)	19%	17%	17%	-33 bps	19%	19.5%	-11 bps	18%	18.3%	-20 bps
Pre-tax profit	7,701	8,461	8,615	-1.8%	31,113	31,267	-0.5%	28,819	32,093	-10.2%
Net profit (reported)	6,985	7,674	7,814	-1.8%	28,219	28,359	-0.5%	25,315	28,154	-10.1%
Net profit (excl. bonus)	8,335	9,839	10,006	-1.7%	35,464	35,631	-0.5%	30,165	33,533	-10.0%
New TW GAAP EPS	9.4	10.2	10.3	-1.8%	37.7	37.9	-0.5%	33.4	37.1	-10.1%
ODM (000's)	442	576	612	-5.9%	1,408	1,444	-2.5%	1,849	2,010	-8.0%
OBM - Windows Mobile	2,608	2,592	2,958	-12.4%	9,977	10,343	-3.5%	7,839	9,039	-13.3%
OBM - Google phone	0	960	510	88.2%	960	510	88.2%	4,834	4,997	-3.3%
Total wireless shipment	3,050	4,128	4,080	1.2%	12,344	12,296	0.4%	14,522	16,046	-9.5%
Global smartphone shipments	44,200	48,000	51,000	-5.9%	160,800	160,800	0.0%	184,920	201,000	-8.0%
Blended ASP (US\$)	376	356	359	-1.0%	348	349	-0.3%	324	325	-0.4%

Source: J.P. Morgan estimates, Company data. \*3Q08 actual shipments derived through calculations from company reported data.

## Cut price target, still better earnings visibility and event driven angle makes HTC a relative outperformer

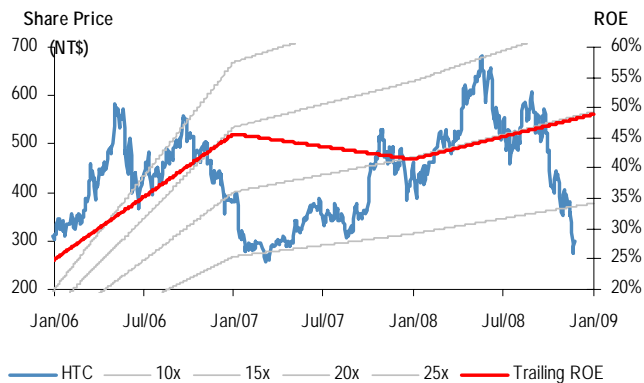
We cut our PT from NT\$560 (Dec-09) to NT\$400 (Jun-09), to reflect 6%/10%/14% EPS cut for FY08E-10E, and a lower FY09 P/E multiple from 15x to 12x (vs. historical range of 8-20x). Still, we expect HTC to outperform the index in next two quarters. Besides better earnings visibility due to G1 backlog, we also see event-driven angle from new Google phones coming up in 1H09 for multiple operators, while we expect its Korean/Taiwan peers to fail to launch on time. Back in Touch, Diamond and G1, HTC stock rallied some 30+% 2 months ahead of the new product launch.

Figure 1: How HTC share price reacted to its own product launch and company news



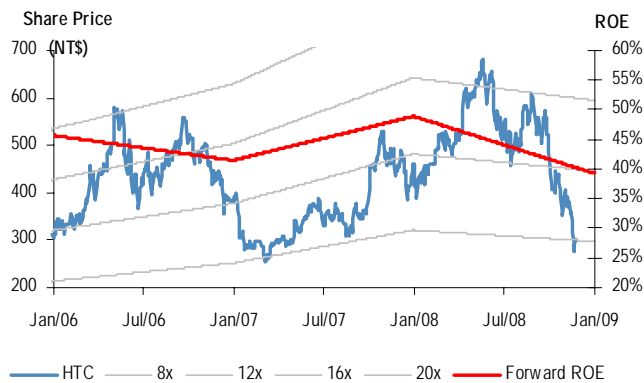
Source: Datastream, J.P. Morgan.

Figure 3: Trailing P/E band (New Taiwan GAAP)



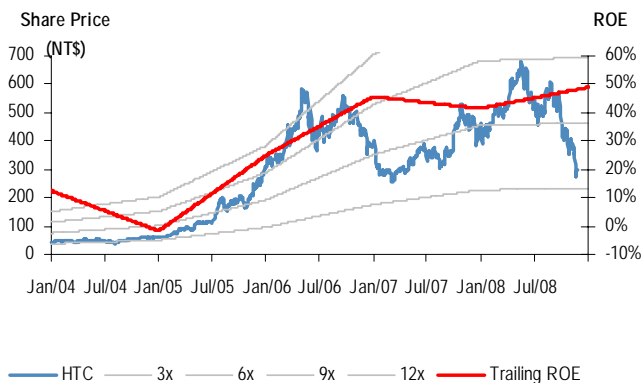
Source: J.P. Morgan.

Figure 4: Forward P/E band (New Taiwan GAAP)



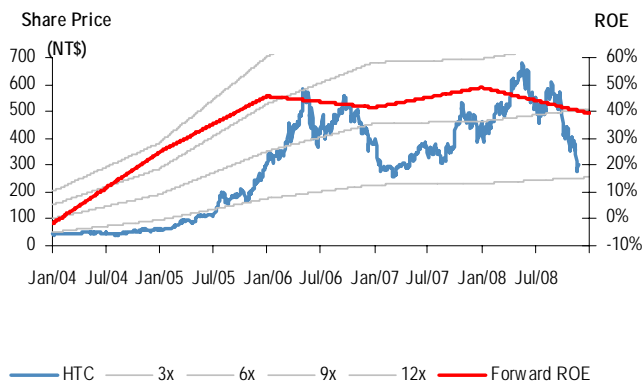
Source: J.P. Morgan.

Figure 5: Trailing P/B band



Source: J.P. Morgan.

Figure 6: Forward P/B band



Source: J.P. Morgan.

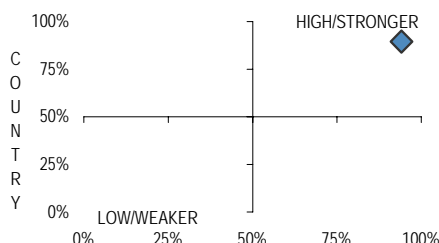
All Data As Of 24-Nov-08

## Q-Snapshot: HTC Corp.

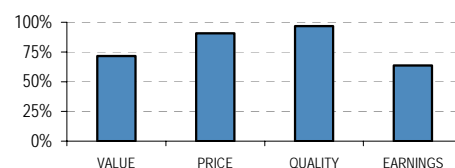
Quant Return Drivers (a Score >50% indicates company ranks 'above average')

Score 0% (worst) to 100% (best)	vs Country	vs Industry	Raw Value
<b>Value</b>			
P/E Vs Market (12mth fwd EPS)	67%	80%	0.6x
P/E Vs Sector (12mth fwd EPS)	70%	83%	0.5x
EPS Growth (forecast)	70%	64%	1.7%
<b>Value Score</b>	<b>72%</b>	<b>82%</b>	
<b>Price Momentum</b>			
12 Month Price Momentum	83%	86%	-33.8%
1 Month Price Reversion	75%	78%	-33.3%
<b>Momentum Score</b>	<b>91%</b>	<b>93%</b>	
<b>Quality</b>			
Return On Equity (forecast)	97%	98%	48.5%
Earnings Risk (Variation in Consensus)	69%	71%	0.09
<b>Quality Score</b>	<b>97%</b>	<b>98%</b>	
<b>Earnings &amp; Sentiment</b>			
Earnings Momentum 3mth (risk adjusted)	75%	77%	-43.1
1 Mth Change in Avg Recom.	13%	49%	0.00
Net Revisions FY2 EPS	57%	57%	-83%
<b>Earnings &amp; Sentiment Score</b>	<b>64%</b>	<b>66%</b>	
<b>COMPOSITE Q-SCORE* (0% To 100%)</b>	<b>89%</b>	<b>94%</b>	

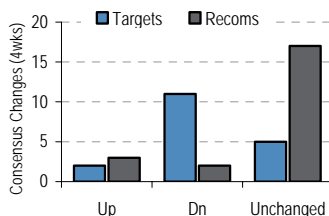
### J.P. Morgan Composite Q-Score



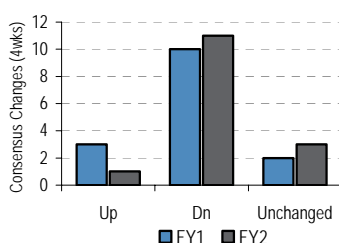
### INDUSTRY Quant Return Drivers Summary (vs Country)



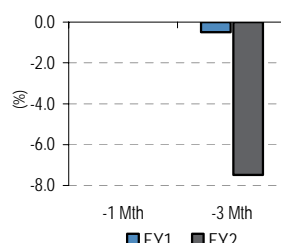
### Targets & Recommendations\*\*



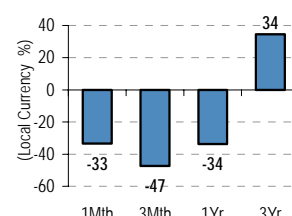
### EPS Revisions\*\*



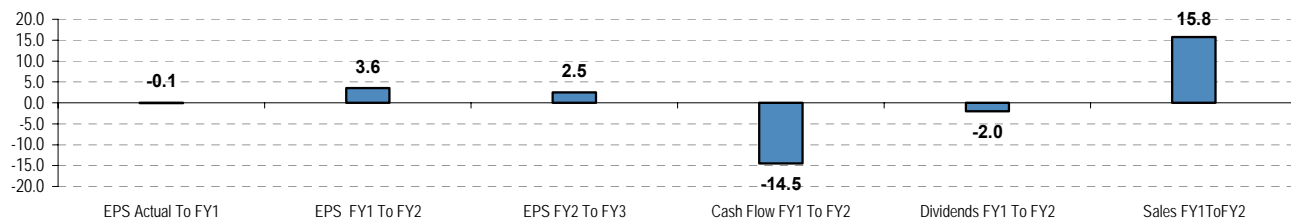
### EPS Momentum (%)



### Historical Total Return (%)



### Consensus Growth Outlook (%)



### Closest in Country by Size (Consensus. ADV = average daily value traded in US\$m over the last 3 mths)

Code	Name	Industry	USD MCAP	ADV	PE FY1	Q-Score*
2317-TW	Hon Hai Precision Industry Co. Ltd.	Computer Peripherals	12,809	119.27	6.4	45%
2882-TW	Cathay Financial Holding Co. Ltd.	Financial Conglomerates	8,831	48.47	44.9	20%
1303-TW	Nan Ya Plastics Corp.	Chemicals: Specialty	8,787	14.16	11.0	11%
2002-TW	China Steel Corp.	Steel	8,124	47.43	5.8	31%
1326-TW	Formosa Chemicals & Fibre Corp.	Chemicals: Major Diversified	7,602	11.83	8.7	26%
<b>2498-TW</b>	<b>HTC Corp.</b>	<b>Telecommunications Equipment</b>	<b>6,559</b>	<b>127.22</b>	<b>7.5</b>	<b>89%</b>
2454-TW	MediaTek Inc.	Semiconductors	6,411	91.99	9.5	68%
2409-TW	AU Optronics Corp.	Electronic Equipment/Instruments	5,029	60.83	4.1	5%
2357-TW	ASUSTeK Computer Inc.	Computer Processing Hardware	4,379	47.56	5.7	50%
3045-TW	Taiwan Mobile Co. Ltd.	Wireless Telecommunications	4,340	11.79	10.8	91%
2881-TW	Fubon Financial Holding Co. Ltd.	Financial Conglomerates	4,194	17.86	11.2	44%

Source: Factset, Thomson and J.P. Morgan Quantitative Research. For an explanation of the Q-Snapshot, please visit <http://jpmorgan.hk.acrobat.com/qsnapshot/>  
Q-Snapshots are a product of J.P. Morgan's Global Quantitative Analysis team and provide quantitative metrics summarized in an overall company 'Q-Score.'  
Q-Snapshots are based on consensus data and should not be considered as having a direct relationship with the J.P. Morgan analysts' recommendation.  
\* The Composite Q-Score is calculated by weighting and combining the 10 Quant return drivers shown. The higher the Q-Score the higher the one month expected return. On a 14 Year back-test the stocks with the highest Q-Scores have been shown (on average) to significantly outperform those stocks with the lowest Q-Scores in this universe. \*\* The number of up, down and unchanged target prices, recommendations or EPS forecasts that make up consensus.

## HTC: Summary of financials

NT\$ in millions, year-end December

Profit and Loss statement					Cash flow statement				
	FY07	FY08E	FY09E	FY10E		FY07	FY08E	FY09E	FY10E
Revenues	118,581	153,208	152,445	186,489	Net Income	28,939	28,219	25,315	30,356
% change Y/Y	11.7	29.2	-0.5	22.3	Depreciation and Amortization	681	707	1,185	1,489
Gross Margin (%)	34.3	33.2	30.1	29.5	Change in working capital	10,256	9,789	-806	3,150
EBITDA	31,705	30,461	28,792	35,180	Net Cash from Operations	39,876	38,715	25,694	34,994
% change Y/Y	15.9	-3.9	-5.5	22.2	Cash Flow from Investing	-	-	-	-
EBITDA Margin (%)	26.7	19.9	18.9	18.9	Purchase of Property, Plant & Equipment	(1,488)	(1,192)	(1,800)	(2,400)
EBIT	31,024	29,755	27,607	33,691	Purchase/Sale of Other LT assets	(208)	(679)	-	-
% change Y/Y	16.1	-4.1	-7.2	22.0	Purchase/Sale of Investments	(2,075)	(1,704)	-	-
EBIT Margin (%)	26.2	19.4	18.1	18.1	Net Cash from Investing Activities	(3,770)	(3,575)	(1,800)	(2,400)
Net Interest	761	1,362	1,212	1,380	Cash Flow from Financing	-	-	-	-
Earnings before tax	32,151	31,113	28,819	35,071	Issuance/Repayment of Debt	-	-	-	-
% change Y/Y	18.5	-3.2	-7.4	21.7	Change in other LT liabilities	(0)	6	-	-
Tax	3,212	2,894	3,504	4,716	Change in Common Equity - net	4,097	(2,622)	5,487	-
as % of EBT	10.0	9.3	12.2	13.4	Payment of Cash Dividends	(19,487)	(22,662)	(22,575)	(22,784)
Net Income (Reported)	28,939	28,219	25,315	30,356	Other Financing Charges, Net	(46)	(1,300)	(1,500)	(2,500)
% change Y/Y	14.4	-2.5	-10.3	19.9	Net Cash from Financing Activities	(15,435)	(26,577)	(18,588)	(25,284)
Net Income (Adjusted)	23,260	28,219	25,315	30,356	Net Change in Cash and Cash Equivalents	20,672	8,563	5,306	7,310
% change Y/Y	19.6	21.3	-10.3	19.9	Cash at Beginning of Period	34,397	55,069	63,632	68,938
Shares Outstanding	739	748	758	770					
EPS (reported)	39.1	37.7	33.4	39.4					
% change Y/Y	12.5	21.2	-16.1	17.9					
EPS (adjusted)	31.5	37.7	33.4	39.4					
% change Y/Y	17.7	20.0	-11.6	18.1					
Balance sheet					Ratio Analysis				
	FY07	FY08E	FY09E	FY10E	%	FY07	FY08E	FY09E	FY10E
Cash and cash equivalents	55,069	63,632	68,938	76,248	EBITDA margin	26.7	19.9	18.9	18.9
Accounts receivable	19,484	27,314	26,170	30,492	Operating margin	26.2	19.4	18.1	18.1
Inventories	6,119	9,991	9,573	11,154	Net profit margin	19.6	18.4	16.6	16.3
Others	2,501	2,230	2,230	2,230	SG&A/sales	5.0	6.1	5.7	5.4
Current assets	83,173	103,167	106,911	120,123					
LT investments	2,899	4,603	4,603	4,603	Sales per share growth	9.9	27.8	(1.9)	20.5
Net fixed assets	3,716	4,201	4,816	5,728	Sales growth	11.7	29.2	(0.5)	22.3
Total assets	90,445	113,307	117,666	131,790	Net profit growth (adjusted)	19.6	21.3	-10.3	19.9
					Net profit growth (reported)	14.4	-2.5	-10.3	19.9
Liabilities					EPS growth (adjusted)	17.7	20.0	-11.6	18.1
ST loans	-	-	-	-	EPS growth (reported)	12.5	21.2	-16.1	17.9
Payables	22,020	25,657	24,542	28,858	Interest coverage (x)	NM	217,580	NM	NM
Others	12,348	29,932	28,679	33,414	Net debt to total capital	Net Cash	Net Cash	Net Cash	Net Cash
Total current liabilities	34,368	55,588	53,221	62,272	Net debt to equity	Net Cash	Net Cash	Net Cash	Net Cash
Long term debt	-	-	-	-	Sales/assets	131.1	135.2	129.6	141.5
Other liabilities	1	6	6	6	Assets/equity	161.3	196.3	182.6	189.6
Total liabilities	34,369	55,595	53,227	62,279	ROE	41.5	48.9	39.3	43.7
Shareholders' equity	56,076	57,712	64,439	69,511	ROCE	41.5	48.9	39.3	43.3
BVPS	75.8	77.2	85.0	90.3					

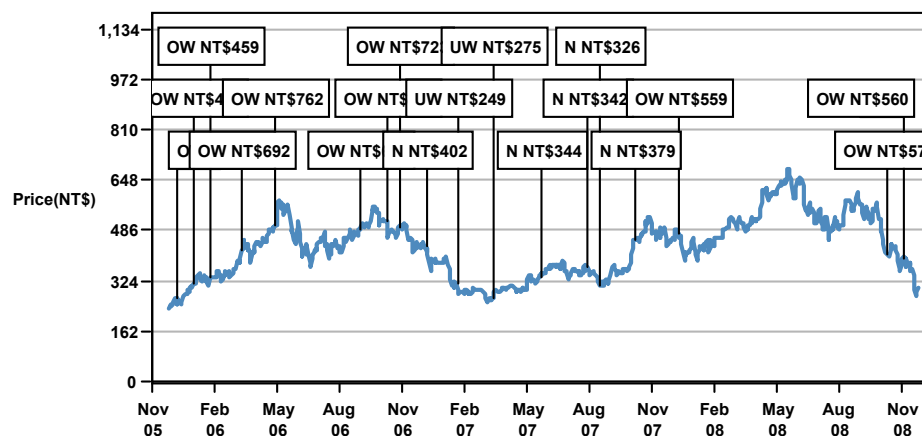
Source: J.P. Morgan estimates, Company data.

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**Important Disclosures**

**High Tech Computer (HTC) (2498.TW) Price Chart**



Date	Rating	Share Price (NT\$)	Price Target (NT\$)
06-Dec-05	OW	270.22	341.00
02-Jan-06	OW	312.62	433.00
26-Jan-06	OW	334.81	459.00
13-Mar-06	OW	422.58	692.00
29-Apr-06	OW	502.96	762.00
01-Sep-06	OW	491.12	686.00
11-Oct-06	OW	515.98	689.00
30-Oct-06	OW	492.90	723.00
07-Dec-06	N	436.09	402.00
22-Jan-07	UW	313.61	249.00
15-Mar-07	UW	266.27	275.00
23-May-07	N	337.87	344.00
29-Jul-07	N	366.86	342.00
17-Aug-07	N	306.92	326.00
08-Oct-07	N	457.69	379.00
10-Dec-07	OW	472.31	559.00
09-Oct-08	OW	408.00	570.00
03-Nov-08	OW	393.50	560.00

Source: Reuters and J.P. Morgan; price data adjusted for stock splits and dividends.  
 This chart shows J.P. Morgan’s continuing coverage of this stock; the current analyst may or may not have covered it over the entire period.  
 J.P. Morgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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Coverage Universe: **Bhavin Shah:** Advanced Semiconductor Engineering (ASE) (2311.TW), Chartered Semiconductor (Singapore) (CSMF.SI), Chartered Semiconductor (US) (CHRT), High Tech Computer (HTC) (2498.TW), SPIL (Siliconware Precision Industries) (2325.TW), TSMC (2330.TW), UMC (2303.TW)

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
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IB clients*	53%	51%	43%
JPMSI Equity Research Coverage	40%	48%	12%
IB clients*	76%	70%	59%

\*Percentage of investment banking clients in each rating category.

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