

Asia Taiwan

Technology Semiconductor &amp; Semiconductor Equipment

Deutsche Bank



10 November 2008

# Motech Industries Inc

Reuters: 6244.TWO Bloomberg: 6244 TT Exchange: TWO Ticker: 6244

## Deteriorating outlook; downgrade to Hold

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### Grim picture ahead

We cut our EPS forecast by 4% for 2008, 31% for 2009, and 54% for 2010 to factor in demand slowdown led by tightening loan standards and more margin contraction. We see demand is slowing with the growing unwillingness to lend money for the solar installation. Moreover, we believe low entry barriers and commoditized products will lead to sharp ASP/margin erosion when the solar industry is facing oversupply of polysilicon. We cut our TP from NT\$190 to NT\$94 and downgrade from Buy to Hold.

### Weaker 4Q08 and 1Q09

Our surveys show that Motech's customers are reducing orders for 4Q08 and 1Q09 due to the weakening end demand. We expect sales to decline 7-10% QoQ in 4Q08 and 18-20% in 1Q09 vs. our previous estimates of 3% and -1% growth, respectively. Recently order visibility continues to drop significantly, implying more downside risks to the end demand.

### 2009 looks more challenging

As the competitors can easily purchase polysilicon under oversupply and may cut price aggressively due to low capex/technology requirements and commoditized products in 2009, we expect the solar cell price to fall at a faster pace than the raw material price (polysilicon). We thus anticipate GM to fall to 14.2% in 2009 and 13.4% in 2010 from 15.4% in 2008.

### We lower our TP to NT\$94 from NT\$190; demand is an up/downside risk

Our revised TP is based on 10x 2009E EPS, which is below the 20x used in 2004-07. We believe this can be merited by its earnings CAGR of -6% during 2009-10 vs. 77% during 2004-07. Our revised TP also implies 1.5x 2009E PB as we apply a 16% discount to its fair PB based on 2009-10 ROE to reflect the downturn of the solar industry. Upside risks include better execution in cost reduction and stronger demand. Downside risks include slow ramp up in internal ingot/wafer capacity and weaker demand.

### Forecasts and ratios

Year End Dec 31	2006A	2007A	2008E	2009E	2010E
Sales (TWDm)	8,099.5	15,577.6	<b>23,982.3</b>	22,270.3	23,255.2
EBITDA (TWDm)	2,381.5	2,933.7	<b>3,618.6</b>	3,211.4	3,165.8
Reported NPAT (TWDm)	2,257.9	2,442.2	<b>2,586.6</b>	2,349.4	2,288.6
Reported EPS FD(TWD)	9.05	9.79	<b>10.37</b>	9.42	9.17
DB EPS FD(TWD)	6.07	7.28	<b>10.37</b>	9.42	9.17
DB EPS growth (%)	86.8	19.8	<b>42.5</b>	-9.2	-2.6
PER (x)	61.2	46.2	<b>8.9</b>	9.8	10.0
EV/EBITDA (x)	25.1	19.5	<b>6.4</b>	7.2	7.3
DPS (net) (TWD)	8.50	7.00	<b>6.50</b>	7.00	8.00
Yield (net) (%)	2.3	2.1	<b>7.0</b>	7.6	8.7

Source: Deutsche Bank estimates, company data

<sup>1</sup> DB EPS is fully diluted and excludes non-recurring items<sup>2</sup> Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close

### Forecast change

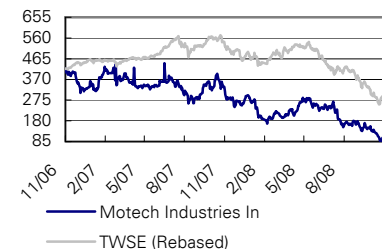
#### Hold

Price at 7 Nov 2008 (TWD)	<b>92.20</b>
Price target - 12mth (TWD)	<b>94.00</b>
52-week range (TWD)	<b>315.00 - 88.40</b>
TWSE	<b>4,742</b>

#### Key changes

Rating	Buy to Hold	↓
Price target	190.00 to 94.00	<b>-50.5%</b>
Sales (FYE)	24,699 to 23,982	<b>-2.9%</b>
Op prof margin (FYE)	11.8 to 12.0	<b>1.1%</b>
Net profit (FYE)	2,686.1 to 2,586.6	<b>-3.7%</b>

#### Price/price relative



Performance (%)	1m	3m	12m
Absolute	-40.5	-41.5	-72.6
TWSE	-14.2	-32.5	-49.0

#### Stock data

Market cap (TWDm)	<b>23,001</b>
Market cap (USDm)	<b>701</b>
Shares outstanding (m)	<b>189.9</b>
Major shareholders	<b>Fu-Hien Cheng (8.53%)</b>
Free float (%)	<b>70</b>
Avg daily value traded (USDm)	<b>11.3</b>

#### Key indicators (FY1)

ROE (%)	<b>18.9</b>
Net debt/equity (%)	<b>5.7</b>
Book value/share (TWD)	<b>55.75</b>
Price/book (x)	<b>1.65</b>
Net interest cover (x)	<b>-</b>
Operating profit margin (%)	<b>12.0</b>

Deutsche Bank AG/Hong Kong

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Model updated:09 November 2008

**Running the numbers****Asia****Taiwan****Hardware & Equipment****Motech Industries Inc**

Reuters: 6244.TWO

Bloomberg: 6244 TT

**Hold**

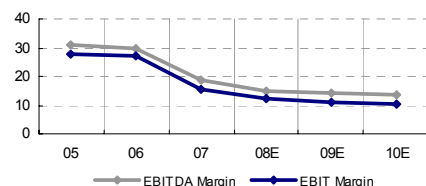
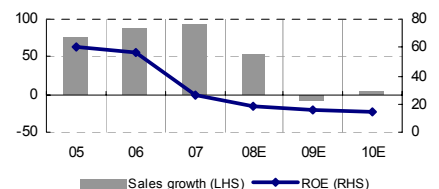
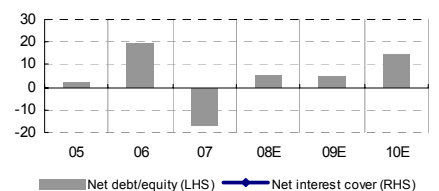
Price (7 Nov 08) TWD 92.20

Target price TWD 94.00

52-week Range TWD 88.40 - 315.00

Market Cap (m) TWDm 23,001  
USDm 701**Company Profile**

Founded in 1981, Motech Industries, Inc. (Motech) focused on designing, manufacturing, marketing, and servicing high-end test and measurement instruments. In 1998, the company set up solar energy division as the pioneer in Taiwan for manufacturing single and multi-crystalline silicon solar cells. The company is the largest supplier in Taiwan and has become one of the top 10 suppliers in the world.

**Price Performance****Margin Trends****Growth & Profitability****Solvency****Michael Chou**

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Fiscal year end 31-Dec

**Financial Summary**

	2005	2006	2007	2008E	2009E	2010E
DB EPS (TWD)	3.25	6.07	7.28	10.37	9.42	9.17
Reported EPS (TWD)	4.65	9.05	9.79	10.37	9.42	9.17
DPS (TWD)	4.36	8.50	7.00	6.50	7.00	8.00
BVPS (TWD)	10.0	22.3	53.8	55.7	60.8	63.3

Weighted average shares (m)	140	161	170	190	238	249
Average market cap (TWDm)	22,033	59,752	57,254	23,001	23,001	23,001
Enterprise value (TWDm)	22,033	59,752	57,254	23,001	23,001	23,001

**Valuation Metrics**

P/E (DB) (x)	48.5	61.2	46.2	8.9	9.8	10.0
P/E (Reported) (x)	33.9	41.1	34.3	8.9	9.8	10.0
P/BV (x)	22.45	14.88	5.53	1.65	1.52	1.46
FCF Yield (%)	nm	nm	nm	0.1	8.7	1.7
Dividend Yield (%)	2.8	2.3	2.1	7.0	7.6	8.7
EV/Sales (x)	5.1	7.4	3.7	1.0	1.0	1.0
EV/EBITDA (x)	16.5	25.1	19.5	6.4	7.2	7.3
EV/EBIT (x)	18.6	27.4	23.6	8.0	9.6	9.8

**Income Statement (TWDm)**

<b>Sales revenue</b>	<b>4,304</b>	<b>8,099</b>	<b>15,573</b>	<b>23,982</b>	<b>22,270</b>	<b>23,255</b>
<b>Gross profit</b>	<b>1,572</b>	<b>2,684</b>	<b>3,493</b>	<b>4,451</b>	<b>3,981</b>	<b>3,921</b>
<b>EBITDA</b>	<b>1,334</b>	<b>2,382</b>	<b>2,934</b>	<b>3,619</b>	<b>3,211</b>	<b>3,166</b>
Depreciation	149	204	503	748	810	816
Amortisation	0	0	0	0	0	0
<b>EBIT</b>	<b>1,185</b>	<b>2,178</b>	<b>2,431</b>	<b>2,871</b>	<b>2,401</b>	<b>2,350</b>
Net interest income/(expense)	-1	-2	152	49	112	117
Associates/affiliates	0	0	0	0	0	0
Exceptionals/extraordinaries	0	0	0	0	0	0
Other pre-tax income/(expense)	-17	87	-124	-264	-30	-33
<b>Profit before tax</b>	<b>1,167</b>	<b>2,263</b>	<b>2,459</b>	<b>2,656</b>	<b>2,483</b>	<b>2,434</b>
Income tax expense	7	5	17	72	145	170
Minorities	0	0	0	-3	-12	-25
Other post-tax income/(expense)	0	0	0	0	0	0
<b>Net profit</b>	<b>1,159</b>	<b>2,258</b>	<b>2,442</b>	<b>2,587</b>	<b>2,349</b>	<b>2,289</b>
DB adjustments (including dilution)	-348	-743	-626	0	0	0
<b>DB Net profit</b>	<b>811</b>	<b>1,515</b>	<b>1,816</b>	<b>2,587</b>	<b>2,349</b>	<b>2,289</b>

**Cash Flow (TWDm)**

<b>Cash flow from operations</b>	<b>295</b>	<b>1,455</b>	<b>-813</b>	<b>1,770</b>	<b>3,672</b>	<b>2,942</b>
Net Capex	-465	-1,709	-858	-1,754	-1,750	-2,550
<b>Free cash flow</b>	<b>-170</b>	<b>-254</b>	<b>-1,671</b>	<b>16</b>	<b>1,922</b>	<b>392</b>
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-135	-369	-1,383	-1,443	-1,620	-1,744
Net inc/(dec) in borrowings	175	2,291	309	1,368	-311	101
Other investing/financing cash flows	-56	-342	6,305	-1,304	-232	-232
<b>Net cash flow</b>	<b>-186</b>	<b>1,326</b>	<b>3,560</b>	<b>-1,363</b>	<b>-241</b>	<b>-1,484</b>
Change in working capital	-1,113	-873	-1,419	-424	512	-163

**Balance Sheet (TWDm)**

Cash and other liquid assets	239	1,565	5,125	3,762	3,522	2,038
Tangible fixed assets	1,016	2,604	2,921	4,029	4,915	6,642
Goodwill/intangible assets	0	0	0	0	0	0
Associates/investments	152	149	609	2,140	2,140	2,140
Other assets	1,826	4,733	8,919	10,162	10,458	11,004
<b>Total assets</b>	<b>3,234</b>	<b>9,050</b>	<b>17,573</b>	<b>20,094</b>	<b>21,036</b>	<b>21,825</b>
Interest bearing debt	294	2,621	2,881	4,556	4,230	4,331
Other liabilities	435	870	1,279	1,631	1,635	1,700
<b>Total liabilities</b>	<b>729</b>	<b>3,491</b>	<b>4,160</b>	<b>6,187</b>	<b>5,865</b>	<b>6,031</b>
Shareholders' equity	2,505	5,560	13,413	13,907	15,171	15,794
Minorities	0	0	0	0	0	0
<b>Total shareholders' equity</b>	<b>2,505</b>	<b>5,560</b>	<b>13,413</b>	<b>13,907</b>	<b>15,171</b>	<b>15,794</b>
<b>Net debt</b>	<b>55</b>	<b>1,056</b>	<b>-2,244</b>	<b>794</b>	<b>708</b>	<b>2,293</b>

**Key Company Metrics**

Sales growth (%)	75.7	88.2	92.3	54.0	-7.1	4.4
DB EPS growth (%)	86.5	86.8	19.8	42.5	-9.2	-2.6
EBITDA Margin (%)	31.0	29.4	18.8	15.1	14.4	13.6
EBIT Margin (%)	27.5	26.9	15.6	12.0	10.8	10.1
Payout ratio (%)	52.5	60.5	48.8	47.7	71.0	87.1
ROE (%)	60.3	56.0	25.7	18.9	16.2	14.8
Capex/sales (%)	10.8	21.1	5.5	7.3	7.9	11.0
Capex/depreciation (x)	3.1	8.4	1.7	2.3	2.2	3.1
Net debt/equity (%)	2.2	19.0	-16.7	5.7	4.7	14.5
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Bank estimates

**Figure 1: Earnings downward revisions**

NT\$m	New			Previous			Diff. (%; New/Previous)		
	2008E	2009E	2010E	2008E	2009E	2010E	2008E	2009E	2010E
Net sales	23,982	22,270	23,255	24,699	28,988	38,628	-3%	-23%	-40%
Gross Profit	3,703	3,171	3,105	3,815	4,554	6,512	-3%	-30%	-52%
Operating Profit	2,871	2,401	2,350	2,923	3,514	5,232	-2%	-32%	-55%
PBT	2,656	2,483	2,434	2,730	3,590	5,316	-3%	-31%	-54%
PAT	2,587	2,349	2,289	2,686	3,395	4,969	-4%	-31%	-54%
EPS (NT\$)	10.37	9.42	9.17	10.77	13.61	19.92	-4%	-31%	-54%
								<b>Diff. (% pt)</b>	
Gross Margin	15.4%	14.2%	13.4%	15.4%	15.7%	16.9%	0.0%	-1.5%	-3.5%
Operating Margin	12.0%	10.8%	10.1%	11.8%	12.1%	13.5%	0.1%	-1.3%	-3.4%
Net Margin	10.8%	10.5%	9.8%	10.9%	11.7%	12.9%	-0.1%	-1.2%	-3.0%

Source: Deutsche Bank estimates

## Valuation and Risks

### TP and demand is the main up/downside risks

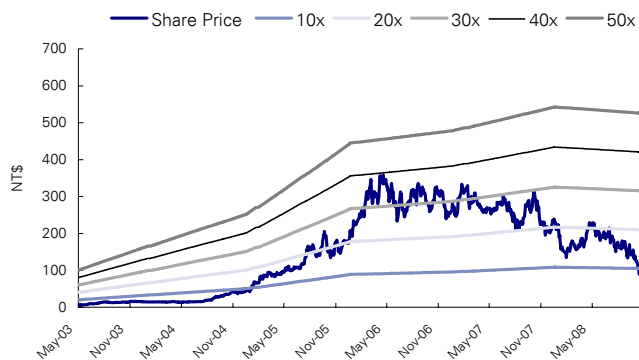
Our TP is based on 10x 2009E EPS, which is below the 20x used in 2004-07. We believe this can be merited by its earnings CAGR of -6% during 2009-10 vs. 77% during 2004-07. This TP PE multiple of 10x 2009E EPS is also higher than 7-9x for its peers as we factor in higher earnings CAGR compared with its peers. Our revised TP also implies 1.5x 2009E PB as we apply a 16% discount to its fair PB based on 2009-10 ROE to reflect the downturn of the solar industry.

Upside risks include better execution in reducing cost and stronger demand. If the company can significantly lower the portion of contracted polysilicon, this should result in upside to our margin estimates. Better-than-expected demand can lead us to adjust our ASP and shipment assumptions. Downside risks include slow ramp up in internal ingot/wafer capacity and weaker demand, which may cause more margin/shipment downside.

### TP sensitivity analysis

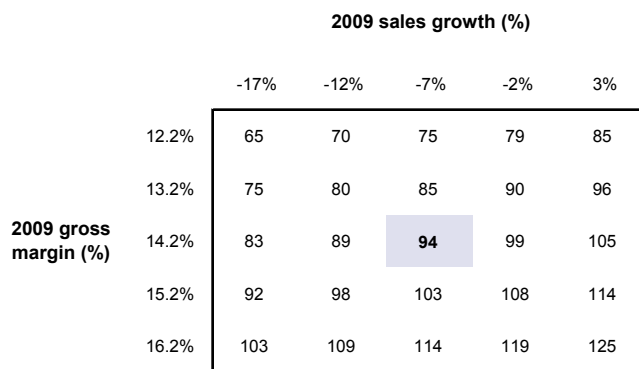
Our TP of NT\$94 assumes sales decline of 7% and a gross margin of 14.2% in 2009. Our analysis shows that every incremental increase of 5ppt in sales and 1ppt in gross margin can generate an additional EPS of NT\$1.36-1.56. This can cause our valuation to expand by NT\$14-17. For instance, we can derive a valuation of NT\$125 based on 3% sales growth (10ppt above our base case) and a 16.2% gross margin (2ppt above our base case) for 2009. In contrast, if we assume sales decline of 17% (10ppt below our base case) and 12.2% gross margin (2ppt below our base case) for 2009, we can derive a valuation of NT\$65.

**Figure 2: Forward PE band for Motech – US GAAP**



Source: Deutsche Bank estimates, company data

**Figure 3: TP sensitivity for Motech**



Source: Deutsche Bank estimates

**Figure 4: Earnings model for Motech – US GAAP**

NT\$m	1Q08	2Q08	3Q08	4Q08E	2008E	1Q09E	2Q09E	3Q09E	4Q09E	2009E
Net Sales	4,902	6,096	6,736	6,248	23,982	5,100	5,343	5,909	5,918	22,270
Gross Profit	816	876	1,049	962	3,703	777	754	785	855	3,171
Operating Profit	661	644	848	718	2,871	598	567	582	654	2,401
PBT	245	627	961	823	2,656	621	589	601	671	2,483
Tax	24	(18)	(45)	(33)	(72)	(31)	(32)	(36)	(46)	(145)
PAT	269	608	916	793	2,587	593	559	568	629	2,349
EPS (NT\$)	1.08	2.44	3.67	3.18	10.37	2.38	2.24	2.28	2.52	9.42
<b>Margin (%)</b>										
Gross Margin	16.6%	14.4%	15.6%	15.4%	15.4%	15.2%	14.1%	13.3%	14.4%	14.2%
Operating Margin	13.5%	10.6%	12.6%	11.5%	12.0%	11.7%	10.6%	9.8%	11.1%	10.8%
Net Margin	5.5%	10.0%	13.6%	12.7%	10.8%	11.6%	10.5%	9.6%	10.6%	10.5%
<b>Growth (%)</b>										
Sales YoY	100%	83%	17%	39%	49%	19%	25%	9%	-11%	8%
PAT YoY	-53%	57%	127%	75%	42%	121%	-8%	-38%	-21%	-9%
Sales QoQ	11%	28%	9%	-7%		-18%	6%	12%	-1%	
PAT QoQ	-50%	126%	50%	-13%		-26%	-6%	2%	11%	

Source: Deutsche Bank estimates, company data

# Appendix 1

## Important Disclosures

Additional information available upon request

### Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Motech Industries Inc	6244.TWO	92.20 (TWD) 7 Nov 08	NA

\*Prices are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

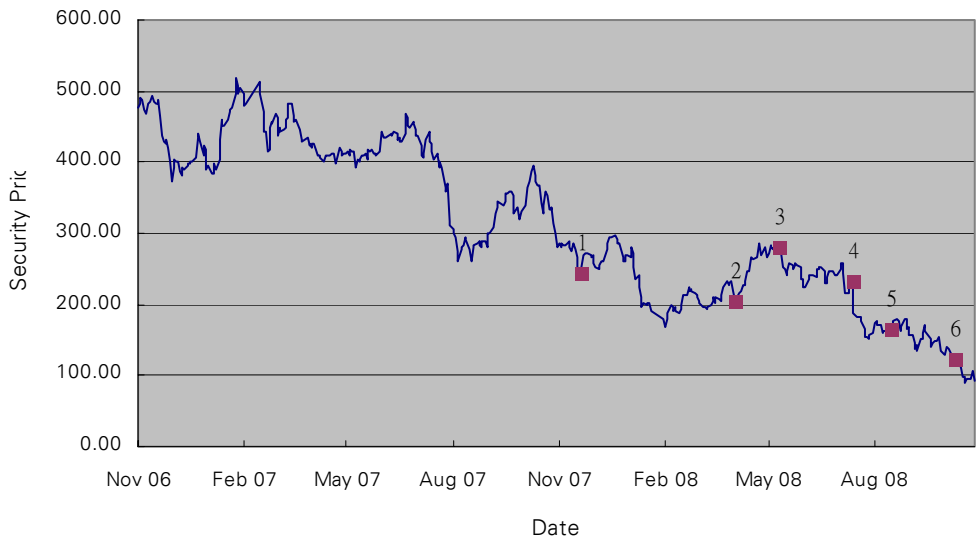
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### Historical recommendations and target price: Motech Industries Inc (6244.TWO)

(as of 11/7/2008)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

\*New Recommendation Structure as of September 9, 2002

1. 2/12/2007:	Buy, Target Price Change TWD297.00	4. 24/7/2008:	Buy, Target Price Change TWD267.00
2. 14/4/2008:	Buy, Target Price Change TWD275.00	5. 26/8/2008:	Buy, Target Price Change TWD250.00
3. 21/5/2008:	Buy, Target Price Change TWD320.00	6. 22/10/2008:	Buy, Target Price Change TWD190.00

Equity rating key

Equity rating dispersion and banking relationships

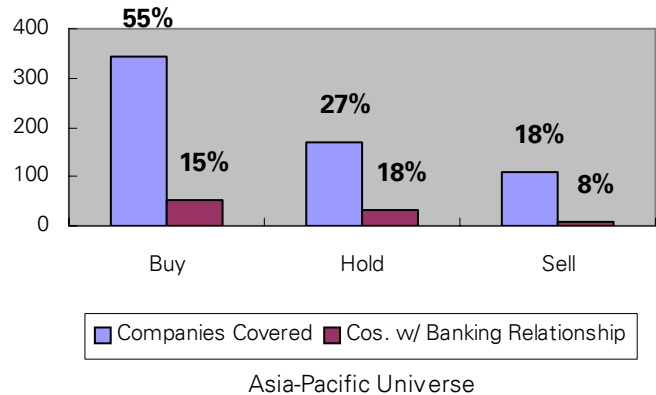
**Buy:** Based on a current 12-month view of total shareholder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

**Sell:** Based on a current 12-month view of total shareholder return, we recommend that investors sell the stock

**Hold:** We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

**Notes:**

1. Newly issued research recommendations and target prices always supersede previously published research.
2. Ratings definitions prior to 27 January, 2007 were:
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  - Hold: Expected total return (including dividends) between -10% and 10% over a 12-month period
  - Sell: Expected total return (including dividends) of -10% or worse over a 12-month period



## Regulatory Disclosures

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