TAIWAN

Silitech Technology

28 October 2008

3311 TT		Neutral
Stock price as of 27 Oct 08	NT$	69.00
12-month target	NT$	72.50
Upside/downside	%	+5.1
Valuation	NT$	74.00
- DCF (WACC 9.0%)		
GICS sector		technology hardware & equipment
Market cap	NT$m	11,825
30-day avg turnover	NT$m	41.0
Market cap	US$m	354
Number shares on issue	m	171.4

Investment fundamentals

Year end 31 Dec		2007A	2008E	2009E	2010E
Total revenue	m	8,906	9,512	9,954	11,223
Reported profit	m	1,289	1,163	1,036	1,183
Profit bonus exp	m	1,006	1,163	1,036	1,183
Bon exp/rep prof	%	22.0	0.0	0.0	0.0
Adjusted profit	m	1,289	1,163	1,036	1,183
EPS rep	NT$	7.85	6.89	6.05	6.90
EPS rep growth	%	19.6	-12.2	-12.2	14.1
EPS bonus exp	NT$	6.12	6.89	6.05	6.90
EPS bonus growth	%	61.9	12.5	-12.2	14.1
PE rep	x	8.8	10.0	11.4	10.0
PE bonus exp	x	11.3	10.0	11.4	10.0
Total DPS	NT$	3.81	3.84	4.00	5.00
Total div yield	%	5.5	5.6	5.8	7.2
ROA	%	20.9	14.0	13.1	13.9
ROE	%	34.0	26.0	21.1	22.2
EV/EBITDA	x	5.0	5.9	5.7	5.1
Net debt/equity	%	-32.8	-27.3	-29.2	-31.3
Price/book	x	2.7	2.5	2.3	2.1

3311 TT rel Taiex performance, & rec history

Source: Datastream, Macquarie Research, October 2008
(all figures in NT$ unless noted)

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Better 3Q08, but gloomier 2009

Event

- Silitech hosted an investor conference today to discuss its 3Q08 results and to update its 4Q08/2009 outlook.

Impact

- **Better-than-expected 3Q08 results:** Silitech reported 3Q08 net profits of NT$329m (down 3% YoY, up 19% QoQ) on sales of NT$2.5bn (up 15% YoY and 20% QoQ). Sales met the company's high-end guidance and beat Street expectations slightly due to share gains at Nokia, Samsung and in RIM orders. The gross margin stayed flat at 24.2% (vs expectations of a 0.5–1.0ppt increase), but operating profits were 5–10% above the consensus at NT$348m due to better opex control. Lastly, buoyed by an NT$64.5m forex gain, net profit beat the consensus by a wider margin of 20%+.
- **Positive 4Q08 guidance:** With 15 new handset keypad projects ready to enter mass production (vs 25 projects in 3Q08), Silitech expects 4Q08 sales to grow by 10–15% QoQ. Silitech seems to have stronger momentum in 4Q08, compared with 0–10% QoQ guidance from local handset component peers. Silitech expects its margin to remain stable, if not rise slightly, due to a better product mix (higher-end keypads) and production scale.
- **Cautious 2009 outlook:** Despite having better 4Q08 order visibility than its local peers, Silitech has the same caution about the 2009 outlook. Silitech expects the global handset volume to decline by 0–3% YoY. It does not provide 2009 sales guidance but thinks it can gain more order allocations from Nokia, Samsung and Sony Ericsson as it is currently involved with more projects with them. Considering the industry's market value contraction, we only model 4.6% revenue growth for Silitech for 2009, the lowest growth since its IPO.

Earnings revision

- We raised our 2008 EPS forecast by 9% to reflect the better 3Q08 results and 4Q08 guidance, but we trimmed our 2009 EPS forecast by 14% to reflect the weaker industry outlook.

Price catalyst

- 12-month price target: NT$72.50 based on a PER methodology.
- Catalyst: Weak global handset demand may cap share-price performance.

Action and recommendation

- **We maintain Neutral rating on Silitech.** We lowered our target price from NT$94 (14x 2009E EPS) to NT$72.5 (12x 2009E EPS). Given the weaker industry outlook ahead and the likely EPS decline in 2009, we expect Silitech's valuation to be de-rated.
- **When to revisit?** For the long run, we still like Silitech's leading industry position and superior technology. We think investors might revisit Silitech should there be better 1H09 order visibility and/or product diversification (into light-metal casings) that enables Silitech to gain more tier-one client orders.

Fig 1 3Q08 P&L review

(NT$ m)	3Q08E	2Q08	QoQ	2Q07	YoY	3Q08E (MacQ)	Difference %
Sales	2,508	2,090	20%	2,174	15%	2,404	4%
Gross Profit	608	503	21%	569	7%	600	1%
Operating Profit	348	213	63%	351	-1%	324	7%
No-op gain/loss	52	60	-13%	26	100%	2	2505%
Pretax Income	400	273	46%	377	6%	326	23%
Net Profits	329	275	19%	338	-3%	267	23%
EPS	1.95	1.63		2.06		1.58	23%
Margin Analysis							
Gross margin	24.2%	24.1%		26.2%		25.0%	
Operating margin	13.9%	10.2%		16.1%		13.5%	
Pretax margin	15.9%	13.1%		17.3%		13.6%	

Source: Macquarie Research, October 2008

Fig 2 Earnings revision

P/L Revision	2007	2008E		2009E		Change (%)	
(NT$ m)	Actual	Old	New	Old	New	2008E	2009E
Net sales	8,906	9,253	9,512	10,601	9,954	2.8	-6.1
Gross profits	2,405	2,318	2,334	2,667	2,355	0.7	-11.7
Operating expenses	786	1,083	1,056	1,198	1,085	-2.5	-9.4
Operating profit	1,619	1,235	1,278	1,469	1,270	3.5	-13.6
Non-op gain/loss	-8	63	140	5	-6	121.2	-227.4
Pretax profits	1,612	1,298	1,418	1,474	1,264	9.2	-14.3
Net profit	1,290	1,065	1,163	1,209	1,036	9.2	-14.3
EPS	7.9	6.3	6.9	7.1	6.0	9.2	-14.3
Key ratio (%)							
Sale growth	23.3	3.9	6.8	14.6	4.6		
Gross margin	27.0	25.0	24.5	25.2	23.7		
Net margin	14.5	11.5	12.2	11.4	10.4		

Source: Company data, Macquarie Research, October 2008

Fig 3 Quarterly financials and sales breakdown

(NT$ m)	FY2007	1Q08	2Q08	3Q08E	4Q08E	2008E	1Q09E	2Q09E	3Q09E	4Q09E	2009E
Sales	8,906	2,087	2,090	2,508	2,828	9,512	2,241	2,285	2,584	2,843	9,954
Gross profit	2,405	531	503	608	692	2,334	535	541	614	664	2,355
Operating profit	1,619	320	213	348	398	1,278	281	276	348	366	1,270
Non-op inc/exp	(8)	(2)	60	52	29	140	(1)	(1)	(1)	(1)	(6)
Pretax profit	1,612	318	273	400	427	1,418	279	274	346	364	1,264
Net income	1,290	219	275	329	340	1,163	237	233	270	296	1,036
EPS (NT$)	7.85	1.30	1.63	1.95	2.01	6.89	1.38	1.36	1.58	1.73	6.05
Wtd. avg. no. of shrs (m)	164	169	169	169	169	169	171	171	171	171	171
Key ratios (%)											
Gross margin	27.0%	25.5%	24.1%	24.2%	24.5%	24.5%	23.9%	23.7%	23.7%	23.4%	23.7%
Operating margin	18.2%	15.3%	10.2%	13.9%	14.1%	13.4%	12.5%	12.1%	13.5%	12.9%	12.8%
Pretax margin	18.1%	15.3%	13.1%	15.9%	15.1%	14.9%	12.5%	12.0%	13.4%	12.8%	12.7%
Effective tax rate	20.0%	31.3%	-0.9%	17.8%	20.4%	18.0%	15.0%	15.0%	22.0%	18.8%	18.0%
Sales BK (NT$ m)											
Keypad	7,146	1,745	1,745	2,189	2,502	8,181	1,927	1,947	2,208	2,502	8,584
Auto parts	1,359	257	250	215	215	937	228	251	276	254	1,008
Mg alloy parts	212	44	40	46	55	186	55	60	66	73	254
OA parts and others	188	41	54	58	56	209	31	28	35	44	137
Total	8,906	2,087	2,089	2,508	2,828	9,512	2,241	2,285	2,584	2,873	9,983
Sales breakdown (%)											
Keypad	80%	84%	84%	87%	88%	86%	86%	85%	85%	87%	86%
Auto parts	15%	12%	12%	9%	8%	10%	10%	11%	11%	9%	10%
Mg alloy parts	2%	2%	2%	2%	2%	2%	2%	3%	3%	3%	3%
OA parts and others	2%	2%	3%	2%	2%	2%	1%	1%	1%	2%	1%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Source: Company data, Macquarie Research, October 2008

Fig 4 Valuation comparison table

Company	Ticker	Price (lc) 28/10/08	MACQ Rating	Mkt cap (US$ m)	EPS (lc) 2007	EPS (lc) 2008E	EPS (lc) 2009E	PER (x) 2007	PER (x) 2008E	PER (x) 2009E	EPS growth (%) 2007	EPS growth (%) 2008E	EPS growth (%) 2009E
Local peers													
Largan	3008 TT	307.5	N	1,197	21.0	25.1	29.2	14.7	12.2	10.5	-32.3	19.8	16.3
Merry	2439 TT	27.9	OP	133	5.7	4.5	6.4	4.9	6.2	4.4	18.2	-20.0	41.6
Silitech	3311 TT	69	N	354	7.9	6.9	6.1	8.8	10.0	11.4	19.6	-12.2	-12.2
Ichia	2402 TT	10.3	UP	104	1.1	1.6	2.0	9.4	6.3	5.2	-61.2	49.7	20.4
ChengUei	2392 TT	46.25	UP	605	5.1	5.0	5.8	9.0	9.3	8.0	-12.1	-2.5	15.8
Catcher	2474 TT	78	N	1,399	13.4	8.5	10.8	5.8	9.1	7.2	6.6	-36.1	26.2
Foxconn Tech	2354 TT	71.2	UP	1,805	10.9	7.7	9.2	6.5	9.3	7.7	42.1	-29.7	20.3
Average					**-**	**-**	**-**	**8.5**	**8.9**	**7.8**	**-2.7**	**-4.4**	**18.4**
Global peers													
AAC Acoustic	2018 HK	3.03	OP	480	0.4	0.6	0.7	6.9	4.9	4.1	-3.6	39.3	21.2
BYD Elec.	0285 HK	2.4	NR	698	0.6	0.6	0.7	4.1	4.2	3.4	55.3	-3.9	24.2
KH Vatec	060720 KS	10600	N	58	-452	2,606	2,479	na	4.1	4.3	na	na	-4.9
Intops	049070 KS	11800	NR	69	4,608	4,445	4,996	2.6	2.7	2.4	-3.9	-3.5	12.4
Hi-P	HIP SG	0.325	OP	191	6.7	7.6	9.8	0.0	0.0	0.0	4.1	13.5	28.4
Balda	BAD GR	0.249	NR	17	-1.5	0.0	0.2	na	31.1	1.1	na	na	2,750.0
Average					**-**	**-**	**-**	**3.4**	**7.8**	**2.5**	**13.0**	**11.3**	**471.9**

Source: Bloomberg, Macquarie Research, October 2008

Fig 5 Valuation comparison table

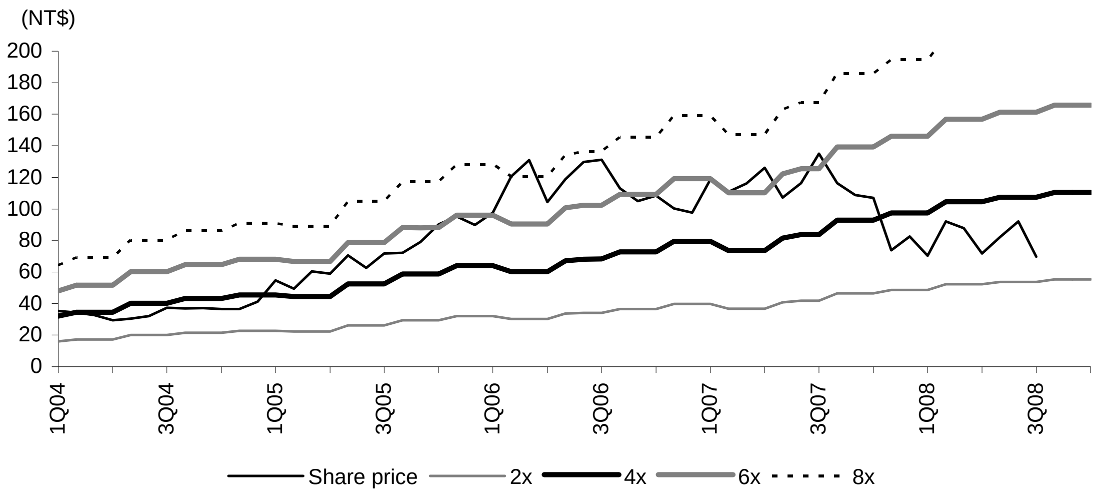
Company	Ticker	ROE(%) 2007	ROE(%) 2008E	ROE(%) 2009E	BVPS (lc) 2007	BVPS (lc) 2008E	BVPS (lc) 2009E	PBR (x) 2007	PBR (x) 2008E	PBR (x) 2009E	EV/EBITDA (x) 2007	EV/EBITDA (x) 2008E	EV/EBITDA (x) 2009E
Local peers													
Largan	3008 TT	28.1	31.0	30.3	74.0	87.9	105.1	4.2	3.5	2.9	10.6	8.3	6.6
Merry	2439 TT	20.9	15.7	20.7	28.7	28.9	32.9	1.0	1.0	0.8	4.0	5.1	3.9
Silitech	3311 TT	34.0	26.0	21.1	25.4	27.6	29.7	2.7	2.5	2.3	5.0	5.9	5.7
Ichia	2402 TT	5.7	8.1	9.2	19.2	20.9	22.0	0.5	0.5	0.5	4.5	2.5	1.9
ChengUei	2392 TT	13.1	11.2	11.8	41.5	47.1	50.9	1.1	1.0	0.9	5.7	5.2	4.5
Catcher	2474 TT	31.7	16.9	18.6	47.9	53.4	62.7	1.6	1.5	1.2	5.0	6.3	4.8
Foxconn Tech	2354 TT	24.4	11.0	13.5	59.1	64.6	72.1	1.2	1.1	1.0	7.4	7.5	6.2
Average		**22.6**	**17.1**	**17.9**	**-**	**-**	**-**	**1.8**	**1.6**	**1.4**	**6.0**	**5.8**	**4.8**
Global peers													
AAC Acoustic	2018 HK	23.4	25.8	24.3	2.1	2.7	3.4	1.5	1.1	0.9	8.9	5.3	3.7
BYD Elec.	0285 HK	na	23.7	18.9	na	2.9	3.5	na	0.8	0.7	1.8	2.3	1.7
KH Vatec	060720 KS	-4.6	28.0	20.9	8,419	10,668	13,005	1.3	1.0	0.8	12.3	4.5	4.2
Intops	049070 KS	21.1	17.9	17.4	23,771	27,549	31,336	0.5	0.4	0.4	0.9	1.9	1.7
Hi-P	HIP SG	14.1	14.1	16.0	0.5	0.6	0.7	0.6	0.6	0.5	2.8	2.3	1.5
Balda	BAD GR	-48.4	-3.6	2.6	2.7	2.8	2.9	0.1	0.1	0.1	3.8	4.3	3.9
Average		**1.1**	**17.7**	**16.7**	**-**	**-**	**-**	**0.8**	**0.7**	**0.6**	**5.1**	**3.4**	**2.8**

Source: Bloomberg, Macquarie Research, October 2008

Fig 6 PER band - annual

Source: Bloomberg, Macquarie Research, October 2008

Fig 7 P/BV- annual



Source: Bloomberg, Macquarie Research, October 2008

Silitech Technology (3311 TT, Neutral, Target price: NT$72.50)

Quarterly Results		3Q/08A	4Q/08E	1Q/09E	2Q/09E
Revenue	**m**	**2,508**	**2,828**	**2,241**	**2,285**
Gross Profit	**m**	**608**	**692**	**535**	**541**
Operating Expenses	m	-260	-294	-255	-266
Operating Income	**m**	**348**	**398**	**281**	**276**
Net Non-operating income	m	13	116	-1	-1
Pre-Tax Income	**m**	**360**	**514**	**279**	**274**
Tax Expense	m	-71	-87	-42	-41
Exceptionals	m	0	0	0	0
Minority Interests	m	0	0	0	0
Reported Earnings	**m**	**289**	**427**	**237**	**233**
Reported Earnings (bonus exp)	m	289	427	237	233
Bonus exp / Reported Earnings	%	0.0	0.0	0.0	0.0
Adjusted Earnings	**m**	**289**	**427**	**237**	**233**
EBITDA	**m**	**458**	**563**	**420**	**415**
EPS (rep)	NT$	1.71	2.53	1.38	1.36
EPS pcp growth (rep)	%	-20.0	20.5	6.8	0.7
EPS (rep bonus exp)	NT$	1.71	2.53	1.38	1.36
EPS pcp growth (rep bonus exp)	%	2.5	54.4	6.8	0.7
EPS (adj)	NT$	1.71	2.53	1.38	1.36
EPS pcp growth (adj)	%	-20.0	17.0	6.8	0.7
Revenue pcp growth	%	10.7	12.3	7.4	9.4
Operating Income pcp growth	%	-19.9	-14.0	-12.4	29.6
Reported Earnings pcp growth	%	-17.8	23.8	8.5	2.3
Gross Profit Margin	%	24.2	24.5	23.9	23.7
Operating Income Margin	%	13.9	14.1	12.5	12.1
Reported Earnings Margin	%	11.5	15.1	10.6	10.2
EBITDA Margin	%	18.3	19.9	18.7	18.2

Profit and Loss Ratios		2007A	2008E	2009E	2010E
Revenue Growth	%	23.3	6.8	4.6	12.8
Gross Profit Growth	%	24.6	-3.0	0.9	11.6
Operating Income Growth	%	31.5	-21.1	-0.6	13.2
Reported Earnings Growth	%	22.8	-9.8	-10.9	14.1
EBITDA Growth	%	32.0	-13.4	3.0	13.5
Gross Profit Margin	%	27.0	24.5	23.7	23.4
Operating Income Margin	%	18.2	13.4	12.8	12.8
Reported Earnings Margin	%	14.5	12.2	10.4	10.5
EBITDA Margin	%	23.0	18.7	18.4	18.5
Payout Ratio	%	48.5	55.8	66.1	72.5
EV/EBITDA	x	5.0	5.9	5.7	5.1
EV/EBIT	x	6.3	8.1	8.3	7.3
Balance Sheet Ratios					
ROE	%	34.0	26.0	21.1	22.2
ROA	%	20.9	14.0	13.1	13.9
ROIC	%	58.4	36.9	30.3	32.8
Net Debt/Equity	%	-32.8	-27.3	-29.2	-31.3
Interest Cover	x	28.7	20.5	22.2	27.0
Price/Book	x	2.7	2.5	2.3	2.1
Book Value per Share	NT$	25.4	27.6	29.7	32.6

Profit & Loss		2007A	2008E	2009E	2010E
Revenue	**m**	**8,906**	**9,512**	**9,954**	**11,223**
Gross Profit	**m**	**2,405**	**2,334**	**2,355**	**2,627**
Operating Expenses	m	-786	-1,056	-1,085	-1,190
Operating Income	**m**	**1,619**	**1,278**	**1,270**	**1,438**
Net Non-operating income	m	-8	140	-6	4
Pre-Tax Income	**m**	**1,612**	**1,418**	**1,264**	**1,442**
Tax Expense	m	-323	-255	-227	-260
Exceptionals	m	0	0	0	0
Minority Interests	m	0	0	0	0
Reported Earnings	**m**	**1,289**	**1,163**	**1,036**	**1,183**
Reported Earnings (bonus exp)	m	1,006	1,163	1,036	1,183
Bonus exp / Reported Earnings	%	22.0	0.0	0.0	0.0
Adjusted Earnings	**m**	**1,289**	**1,163**	**1,036**	**1,183**
EBITDA	**m**	**2,048**	**1,774**	**1,827**	**2,073**
EPS (rep)	NT$	7.85	6.89	6.05	6.90
EPS growth (rep)	%	19.6	-12.2	-12.2	14.1
EPS (rep bonus exp)	NT$	6.12	6.89	6.05	6.90
EPS growth (rep bonus exp)	%	61.9	12.5	-12.2	14.1
EPS (adj)	NT$	7.85	6.89	6.05	6.90
EPS growth (adj)	%	19.6	-12.2	-12.2	14.1
PE (rep)	x	8.8	10.0	11.4	10.0
PE (rep bonus adj)	x	11.3	10.0	11.4	10.0
PE (adj)	x	8.8	10.0	11.4	10.0
Total DPS	NT$	3.81	3.84	4.00	5.00
Total Div Yield	%	5.5	5.6	5.8	7.2
Weighted Average Shares	m	164.3	168.8	171.4	171.4
Period End Shares	m	166.6	171.4	171.4	171.4

Cashflow Analysis		2007A	2008E	2009E	2010E
Reported Earnings	**m**	**1,289**	**1,163**	**1,036**	**1,183**
Depreciation & Amortisation	m	429	496	557	635
Chgs in Working Cap	m	411	-528	-9	-63
Other	m	5	0	11	10
Operating Cashflow	**m**	**2,133**	**1,131**	**1,595**	**1,765**
Acquisitions	m	3	-45	-19	-18
Capex	m	-1,363	-417	-652	-752
Asset Sales	m	0	0	0	0
Other	m	-189	-15	-53	-53
Investing Cashflow	**m**	**-1,549**	**-477**	**-724**	**-823**
Dividend (Ordinary)	m	-504	-656	-686	-686
Equity Raised	m	83	0	0	0
Debt Movements	m	840	-206	-113	-25
Other	m	0	0	0	0
Financing Cashflow	**m**	**419**	**-861**	**-798**	**-710**
Net Chg in Cash/Debt	**m**	**1,002**	**-208**	**73**	**232**
Free Cashflow	m	770	714	943	1,013
FCF per Share	NT$	4.69	4.23	5.50	5.91
P/FCF	x	14.7	16.3	12.5	11.7

Balance Sheet		2007A	2008E	2009E	2010E
Cash	m	3,020	2,812	2,884	3,116
Receivables	m	1,978	2,606	2,727	3,075
Inventories	m	381	653	691	781
Investments	m	29	74	82	90
Fixed Assets	m	2,990	2,966	3,111	3,278
Intangibles	m	36	0	0	0
Other Assets	m	340	379	397	442
Total Assets	**m**	**8,774**	**9,490**	**9,892**	**10,783**
Payables	m	1,647	1,868	1,978	2,237
Short Term Debt	m	399	532	490	479
Long Term Debt	m	1,233	988	910	890
Provisions	m	0	0	0	0
Other Liabilities	m	1,269	1,368	1,430	1,596
Total Liabilities	**m**	**4,549**	**4,757**	**4,809**	**5,202**
Total S/H Equity	**m**	**4,226**	**4,733**	**5,083**	**5,580**
Total Liab & S/H Funds	**m**	**8,774**	**9,490**	**9,892**	**10,783**

All figures in NT$ unless noted.
Source: Macquarie Research, October 2008

Important disclosures:

Recommendation definitions

Macquarie - Australia/New Zealand
Outperform – return >5% in excess of benchmark return (>2.5% in excess for listed property trusts)
Neutral – return within 5% of benchmark return (within 2.5% for listed property trusts)
Underperform – return >5% below benchmark return (>2.5% below for listed property trusts)

Macquarie – Asia/Europe
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie First South - South Africa
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Canada
Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

Macquarie - USA
Outperform (Buy) – return >5% in excess of benchmark return
Neutral (Hold) – return within 5% of benchmark return
Underperform (Sell)– return >5% below benchmark return

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to Australian/NZ/Canada stocks only

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 September 2008

	AU/NZ	Asia	RSA	USA	CA	EUR
Outperform	43.17%	61.57%	63.08%	53.60%	71.54%	43.00%
Neutral	41.37%	16.43%	30.77%	37.60%	24.61%	48.00%
Underperform	15.47%	22.00%	6.15%	8.80%	3.85%	9.00%

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