Deutsche Bank

15 December 2008

Motech Industries Inc

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

Synergies of vertical integration may deteriorate

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Weakening fundamentals; TP down to NT$55 from NT$94

Our recent channel checks suggest a sharper upstream polysilicon ASP decline due to weaker end demand and intensified oversupply. This has led downstream players (including Motech) to cut prices more aggressively. This implies Motech may face more margin pressure as AE Polysilicon's (over 10% stake owned by Motech) ramp-up in 2H09 may have less cost-reducing synergies for Motech. We cut our ESP forecasts by 27% for 2009 and 31% for 2010 and retain Hold.

More negative signs

Our surveys show that the spot polysilicon price has fallen to US$145-170 in Dec from US$180-200 in Nov, which is lower than our estimate of US$170-180. However, downstream solar cell/module makers are taking more aggressive pricing strategies in light of limited product differentiation and lackluster demand outlook. We believe this may partially offset the positive impact of Motech’s internal polysilicon production, which is scheduled to ramp-up in 2H09. We lower our GM forecast for Motech by 1.8ppt to 12.4% for 2009 and 1.4ppt for 2010.

Challenging 1Q09 outlook

We expect sales to decline 19% QoQ in 1Q09. However, we see downside risks to shipments and ASP in 1Q09 as the credit market is still tightening for solar system installations and the macro picture is turning more negative.

Valuation and risks; TP lowered to NT$55 based on 8x 2009E EPS

Our revised TP is based on 8x 2009E EPS, which is below the average of 20x in 2004-07. We believe this is merited by its earnings CAGR of -22% during 2009E-10E vs. 77% during 2004-07. In addition, a -22% 2009E-10E earnings CAGR is at the high end of the expected -46% to -22% for mid/downstream Asian solar companies under our coverage with the 7-8x TP PE multiple which we applied. Upside risks: better execution in reducing cost and stronger demand. Downside risks: slower pace in vertical integration and weaker demand (see p. 3).

Forecasts and ratios

Year End Dec 31	2006A	2007A	**2008E**	2009E	2010E
Sales (TWDm)	8,099.5	15,577.6	**23,982.3**	20,796.4	20,691.7
EBITDA (TWDm)	2,381.5	2,933.7	**3,618.6**	2,539.1	2,368.5
Reported NPAT (TWDm)	2,257.9	2,442.2	**2,586.6**	1,720.5	1,586.9
Reported EPS FD(TWD)	9.05	9.79	**10.37**	6.90	6.36
DB EPS FD(TWD)	6.07	7.28	**10.37**	6.90	6.36
OLD DB EPS FD(TWD)	6.07	7.28	**10.37**	9.42	9.17
% Change	0.0%	0.0%	**0.0%**	-26.8%	-30.7%
DB EPS growth (%)	86.8	19.8	**42.5**	-33.5	-7.8
PER (x)	61.2	46.2	**6.0**	9.1	9.8
EV/EBITDA (x)	25.5	18.8	**4.5**	6.1	6.0
DPS (net) (TWD)	8.50	7.00	**6.10**	4.25	3.75
Yield (net) (%)	2.3	2.1	**9.8**	6.8	6.0

Source: Deutsche Bank estimates, company data

[1] DB EPS is fully diluted and excludes non-recurring items
[2] 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

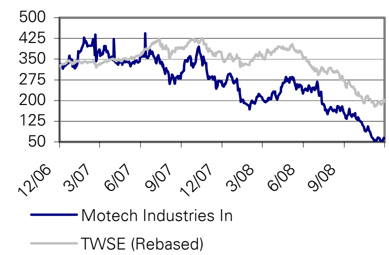
Hold

Price at 12 Dec 2008 (TWD)	**62.50**
Price target - 12mth (TWD)	**55.00**
52-week range (TWD)	**297.50 - 50.40**
TWSE	**4,481**

Key changes

Price target	94.00 to 55.00 ↓	**-41.5%**

Price/price relative



Performance (%)	1m	3m	12m
Absolute	*-15.9*	*-59.9*	*-76.9*
TWSE	*-2.9*	*-29.0*	*-47.2*

Stock data

Market cap (TWDm)	**15,592**
Market cap (USDm)	**468**
Shares outstanding (m)	**189.9**
Major shareholders	**Fu-Hien Cheng (8.53%)**
Free float (%)	**70**
Avg daily value traded (USDm)	**10.1**

Key indicators (FY1)

ROE (%)	**18.6**
Net debt/equity (%)	**5.5**
Book value/share (TWD)	**57.76**
Price/book (x)	**1.08**
Net interest cover (x)	**–**
Operating profit margin (%)	**12.0**

Deutsche Bank AG/Hong Kong

Model updated:14 December 2008

Running the numbers

Asia

Taiwan, Province of China

Hardware & Equipment

Motech Industries Inc

Reuters: 6244.TWO Bloomberg: 6244 TT

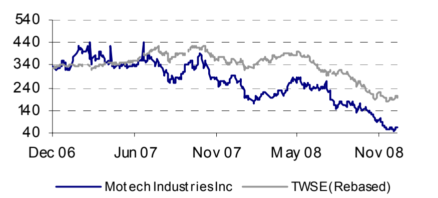
Hold

Price (12 Dec 08)	TWD 62.50
Target price	TWD 55.00
52-week Range	TWD 50.40 - 297.50
Market Cap (m)	TWDm 15,592 USDm 468

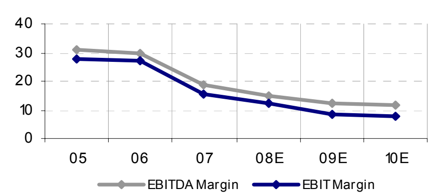
Company Profile

Founded in 1981, Motech Industries, Inc. (Motech) is 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.

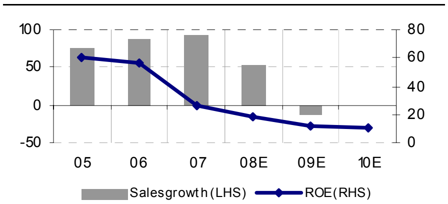
Price Performance



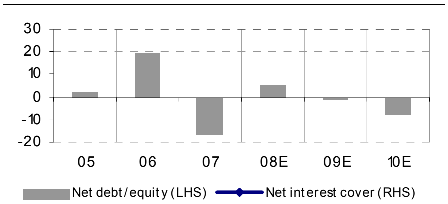
Margin Trends



Growth & Profitability



Solvency



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Fiscal year end 31-Dec	2005	2006	2007	2008E	2009E	2010E
Financial Summary						
DB EPS (TWD)	3.25	6.07	7.28	10.37	6.90	6.36
Reported EPS (TWD)	4.65	9.05	9.79	10.37	6.90	6.36
DPS (TWD)	4.36	8.50	7.00	6.10	4.25	3.75
BVPS (TWD)	10.0	22.3	53.8	57.8	58.9	68.1
Weighted average shares (m)	140	161	170	190	238	249
Average market cap (TWDm)	22,033	59,752	57,254	15,592	15,592	15,592
Enterprise value (TWDm)	22,087	60,809	55,010	16,379	15,477	14,320
Valuation Metrics						
P/E (DB) (x)	48.5	61.2	46.2	6.0	9.1	9.8
P/E (Reported) (x)	33.9	41.1	34.3	6.0	9.1	9.8
P/BV (x)	22.45	14.88	5.53	1.08	1.06	0.92
FCF Yield (%)	nm	nm	nm	nm	16.1	14.2
Dividend Yield (%)	2.8	2.3	2.1	9.8	6.8	6.0
EV/Sales (x)	5.1	7.5	3.5	0.7	0.7	0.7
EV/EBITDA (x)	16.6	25.5	18.8	4.5	6.1	6.0
EV/EBIT (x)	18.6	27.9	22.6	5.7	8.8	8.8
Income Statement (TWDm)						
Sales revenue	**4,304**	**8,099**	**15,578**	**23,982**	**20,796**	**20,692**
Gross profit	**1,572**	**2,684**	**3,493**	**4,451**	**3,359**	**3,219**
EBITDA	**1,334**	**2,382**	**2,934**	**3,619**	**2,539**	**2,369**
Depreciation	149	204	503	748	773	737
Amortisation	0	0	0	0	0	0
EBIT	**1,185**	**2,178**	**2,431**	**2,871**	**1,766**	**1,632**
Net interest income(expense)	-1	-2	152	49	74	75
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	-26	-27
Profit before tax	**1,167**	**2,263**	**2,459**	**2,656**	**1,814**	**1,680**
Income tax expense	7	5	17	72	105	118
Minorities	0	0	0	-3	-12	-25
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	**1,159**	**2,258**	**2,442**	**2,587**	**1,720**	**1,587**
DB adjustments (including dilution)	-348	-743	-626	0	0	0
DB Net profit	**811**	**1,515**	**1,816**	**2,587**	**1,720**	**1,587**
Cash Flow (TWDm)						
Cash flow from operations	**295**	**1,455**	**-813**	**1,718**	**3,037**	**2,541**
Net Capex	-465	-1,709	-858	-1,754	-630	-325
Free cash flow	**-170**	**-254**	**-1,671**	**-35**	**2,407**	**2,216**
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-135	-369	-1,383	-1,443	-1,520	-1,059
Net inc/(dec) in borrowings	175	2,291	309	1,368	-311	101
Other investing/financing cash flows	-56	-342	6,305	-1,246	0	0
Net cash flow	**-186**	**1,326**	**3,560**	**-1,356**	**575**	**1,258**
Change in working capital	*-1,113*	*-873*	*-1,419*	*-475*	*543*	*217*
Balance Sheet (TWDm)						
Cash and other liquid assets	239	1,565	5,125	3,769	4,344	5,603
Tangible fixed assets	1,016	2,604	2,921	4,029	3,962	5,318
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	10,735	10,168	9,873
Total assets	**3,234**	**9,050**	**17,573**	**20,674**	**20,615**	**22,934**
Interest bearing debt	294	2,621	2,881	4,556	4,230	4,331
Other liabilities	435	870	1,279	1,708	1,699	1,622
Total liabilities	**729**	**3,491**	**4,160**	**6,264**	**5,929**	**5,953**
Shareholders' equity	2,505	5,560	13,413	14,410	14,686	16,981
Minorities	0	0	0	0	0	0
Total shareholders' equity	**2,505**	**5,560**	**13,413**	**14,410**	**14,686**	**16,981**
Net debt	*55*	*1,056*	*-2,244*	*787*	*-115*	*-1,271*
Key Company Metrics						
Sales growth (%)	75.7	88.2	92.3	54.0	-13.3	-0.5
DB EPS growth (%)	86.5	86.8	19.8	42.5	-33.5	-7.8
EBITDA Margin (%)	31.0	29.4	18.8	15.1	12.2	11.4
EBIT Margin (%)	27.5	26.9	15.6	12.0	8.5	7.9
Payout ratio (%)	52.5	60.5	48.8	44.8	58.9	58.9
ROE (%)	60.3	56.0	25.7	18.6	11.8	10.0
Capex/sales (%)	10.8	21.1	5.5	7.3	3.0	1.6
Capex/depreciation (x)	3.1	8.4	1.7	2.3	0.8	0.4
Net debt/equity (%)	2.2	19.0	-16.7	5.5	-0.8	-7.5
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Bank estimates

Figure 1: Lowered earnings

	New		Previous		Diff. (%; New/Previous)	
NT$m	2009E	2010E	2009E	2010E	2009E	2010E
Net sales	20,796	20,692	22,270	23,255	-7%	-11%
Gross Profit	2,586	2,482	3,171	3,105	-18%	-20%
Operating Profit	1,766	1,632	2,401	2,350	-26%	-31%
PBT	1,814	1,680	2,483	2,434	-27%	-31%
PAT	1,720	1,587	2,349	2,289	-27%	-31%
EPS (NT$)	6.90	6.36	9.42	9.17	-27%	-31%
					Diff. (% pt)	
Gross Margin	12.4%	12.0%	14.2%	13.4%	-1.8%	-1.4%
Operating Margin	8.5%	7.9%	10.8%	10.1%	-2.3%	-2.2%
Net Margin	8.3%	7.7%	10.5%	9.8%	-2.3%	-2.2%

Source: Deutsche Bank estimates

Valuation and risks

Retain Hold

We foresee slowing demand and a growing unwillingness to lend money for solar system installations. Moreover, we believe low barriers to entry and commoditized products will lead to sharp ASP/margin erosion when polysilicon is oversupplied. This may lead the stock being range-bound over the next 6-12 months.

TP basis and risks

- **New TP of NT$55 (previously NT$94)** - Our revised TP is based on 8x 2009E EPS, which is below the 10x which we applied for our previous TP NT$94 and the average of 20x in 2004-07. We believe this is merited by its earnings CAGR of -22% for 2009E-10E, which is weaker than our previous forecast of -6% as well as 77% for 2004-07. In addition, this -22% earnings CAGR for 2009E-10E is at the high end of our expected -46% to -22% for the mid/downstream Asian solar companies under our coverage with the 7-8x TP PE multiple which we applied.

  Our TP also implies 0.9x 2009E PB, which is a 28% discount to its fair PB based on a 2009E-10E average ROE of 11%, a 9.3% cost of equity, and a terminal growth rate of 3%. Our 3% terminal growth rate reflects a 2% long-term solar industry growth rate and a 1% inflation rate.

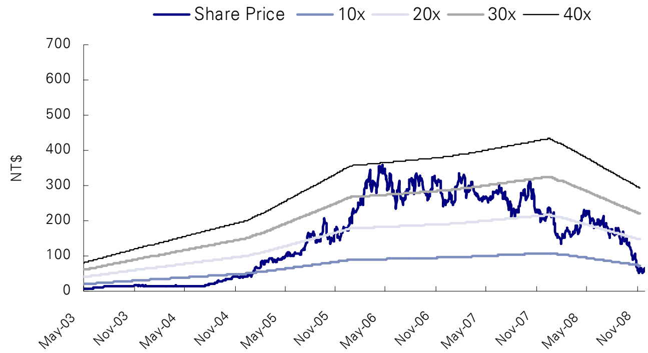
- **Upside risks include better execution in reducing cost and stronger demand -** If the company can significantly lower the portion of contracted polysilicon, this could result in upside to our margin estimates. Better-than-expected demand could also lead us to adjust our ASP and shipment assumptions.

- **Downside risks are a slower pace in vertical integration and weaker demand –** AE Polysilicon plans to supply polysilicon to Motech in 2H09. If AE Polysilicon delays its mass production schedule into 1H10, this may trigger more downward revisions to our margin estimates for 2009 and 2010. In addition, weaker-than-expected demand may cause more downside risks to our ASP/shipment assumptions.

TP sensitivity analysis

Our TP of NT$55 assumes a sales decline of 13% and a gross margin of 12.4% 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$1.18-1.38. This could cause our valuation to expand by NT$10-12. For instance, we derive a valuation of NT$77 based on a 3% sales decline (10ppt above our base case) and a 14.4% gross margin (2ppt above our base case) for 2009. In contrast, if we assume a sales decline of 23% (10ppt below our base case) and a 10.4% gross margin (2ppt below our base case) for 2009, we derive a valuation of NT$35.

Figure 2: Motech's forward PE band



Source: TEJ; Deutsche Bank estimates

Figure 3: Motech's sensitivity analysis of TP

		2009 sales growth (%)				
		-23%	-18%	-13%	-8%	-3%
2009 gross margin (%)	10.4%	35	38	40	43	47
	11.4%	42	45	48	51	55
	12.4%	48	52	55	58	62
	13.4%	55	59	62	65	69
	14.4%	63	67	70	73	77

Source: Deutsche Bank estimates

Figure 4: Earnings model for Motech – US GAAP

NT$mn	1Q08	2Q08	3Q08	4Q08E	2008E	1Q09E	2Q09E	3Q09E	4Q09E	2009E
Net Sales	4,902	6,096	6,736	6,248	23,982	5,054	5,048	5,265	5,429	20,796
Gross Profit	816	876	1,049	962	3,703	693	623	614	655	2,586
Operating Profit	661	644	848	718	2,871	486	413	413	453	1,766
PBT	245	627	961	823	2,656	501	425	423	464	1,814
Tax	24	(18)	(45)	(33)	(72)	(25)	(23)	(25)	(32)	(105)
PAT	269	608	916	793	2,587	479	405	401	436	1,720
EPS (NT$)	1.08	2.44	3.67	3.18	10.37	1.92	1.62	1.61	1.75	6.90
Margin (%)										
Gross Margin	16.6%	14.4%	15.6%	15.4%	15.4%	13.7%	12.3%	11.7%	12.1%	12.4%
Operating Margin	13.5%	10.6%	12.6%	11.5%	12.0%	9.6%	8.2%	7.8%	8.3%	8.5%
Net Margin	5.5%	10.0%	13.6%	12.7%	10.8%	9.5%	8.0%	7.6%	8.0%	8.3%
Growth (%)										
Sales YoY	100%	83%	17%	39%	49%	20%	21%	-1%	-16%	3%
PAT YoY	-53%	57%	127%	75%	42%	78%	-33%	-56%	-45%	-33%
Sales QoQ	11%	28%	9%	-7%		-18%	1%	5%	3%	
PAT QoQ	-50%	126%	50%	-13%		-40%	-15%	-1%	9%	

Source: Deutsche Bank estimates

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Motech Industries Inc	6244.TWO	62.50 (TWD) 12 Dec 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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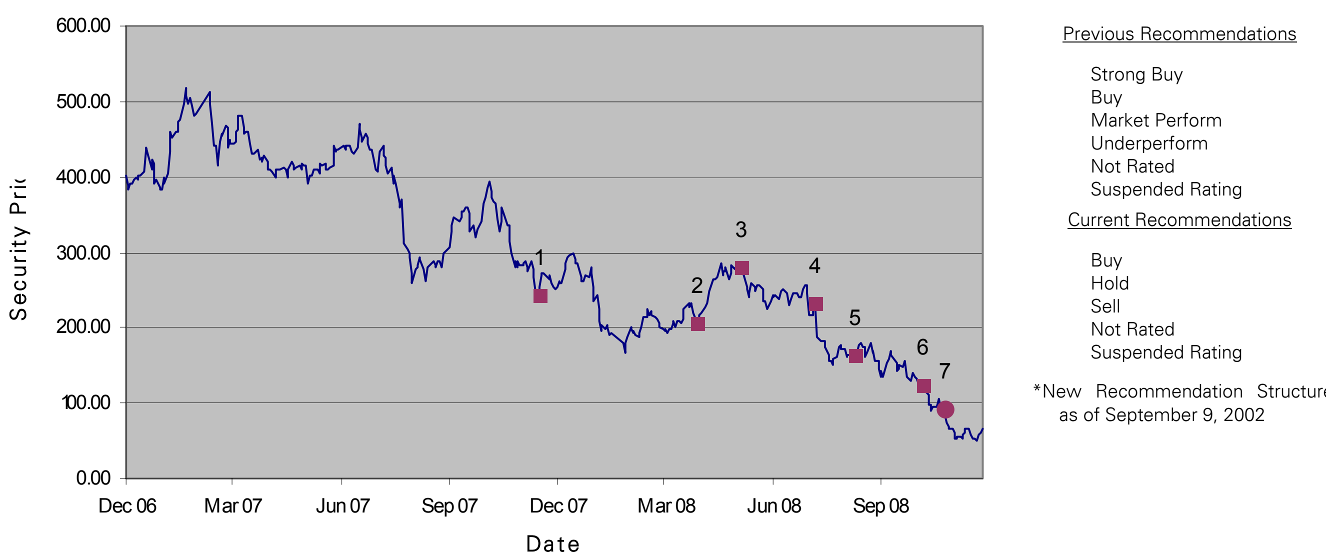
Historical recommendations and target price: Motech Industries Inc (6244.TWO)

(as of 12/12/2008)



1.	2/12/2007:	Buy, Target Price Change TWD297.00	5.	26/8/2008:	Buy, Target Price Change TWD250.00
2.	14/4/2008:	Buy, Target Price Change TWD275.00	6.	22/10/2008:	Buy, Target Price Change TWD190.00
3.	21/5/2008:	Buy, Target Price Change TWD320.00	7.	10/11/2008:	Downgrade to Hold, Target Price Change TWD94.00
4.	24/7/2008:	Buy, Target Price Change TWD267.00			

Equity rating key

Buy: Based on a current 12- month view of total share-holder 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 share-holder return, we recommend that investors sell the stock
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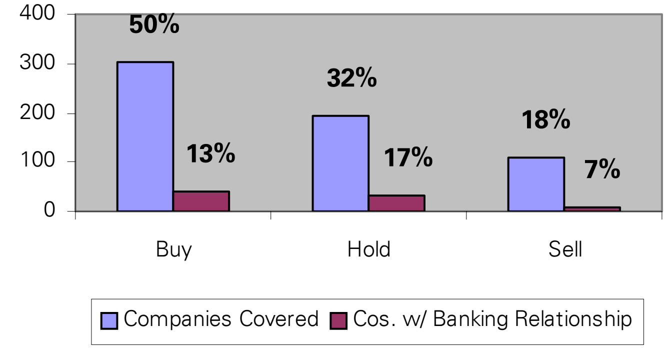
Notes:
1. Newly issued research recommendations and target prices always supersede previously published research.
2. Ratings definitions prior to 27 January, 2007 were:
   Buy: Expected total return (including dividends) of 10% or more over a 12-month period
   Hold: Expected total return (including 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

Equity rating dispersion and banking relationships



Asia-Pacific Universe

Regulatory Disclosures

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