

## Our view

We upgrade Largan to BUY from Neutral, as better shipments for smartphones and new model launches should provide strong growth momentum in 2Q-3Q09F. We see VCM-related business and game console cameras to be key growth drivers beyond 2009F, contributing 15-17% of earnings in 2010-11F, up from 6% in 2009F.

## Anchor themes

- ⚓ We estimate that handset camera penetration was around 63% in 2008E and will reach 67% in 2009F. We think 3MP will replace 2MP as the mainstream resolution by end-2009F; by then, high-end handsets will gradually shift to 5MP-plus.
- ⚓ Handset vendors are increasingly sourcing components from Taiwan and China, amid mounting pressure to cut costs. The macro weakness, especially, should see handset vendors concentrate their component sourcing from tier-one makers, with more resilient financials and technology/cost leadership.

## Opening new markets

- Upgrade to BUY on rising sales for smartphones and new product potential
- A new market for Largan — auto-focus actuator
- New games, new opportunities
- Earnings revisions. Multiple catalysts are in place

### ① Upgrade to BUY on rising sales for smartphones and new product potential

We upgrade Largan to BUY from Neutral, with a revised price target of NT\$429 (18x 2010F EPS), from NT\$245, as: 1) we expect Largan's 2Q-3Q09F revenue to beat market expectation on better sales for smartphones and new model launches by its key customers, and; 2) with the ramp-up of Largan's voice coil motor (VCM, for auto-focus function) and the new application in game consoles, we look for the earnings contribution from new products (VCM assembly, in-house VCM, and game console camera) to reach to 15-17% of earnings in 2010-11F, from 0% in 2008 and 6% in 2009F. Although the stock price has pre-empted our assessment of emerging new growth drivers, we think that ongoing news flow will evidence our view that the stock's re-rating is far from finished.

- **Smartphone.** Largan's revenue growth is heating up in 2Q09F, thanks to the new model launches of smartphone customers (eg, Apple, RIM and HTC). In our previous forecast, we expected 2Q09F revenue to grow by 37% q-q (street-high estimate), based on our view that the launch of the new iPhone, which requires Largan to assemble purchased VCMs and its own lens together, would significantly boost Largan's top line. Now, we anticipate that better-than-expected orders of Apple's new iPhone and the

Closing price on 5 Jun	NT\$356.5
Price target	<b>NT\$429.0</b>
Upside/downside	20.3%
Difference from consensus	<b>48.4%</b>
FY10F net profit (NT\$m)	3,099
Difference from consensus	<b>13.4%</b>
Source: Nomura	

## Nomura vs consensus

Our FY10F bonus-adjusted earnings forecast is 13.4% above consensus, chiefly because of our higher earnings forecasts for new products.

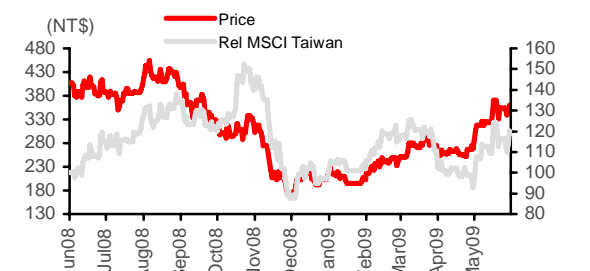
## Key financials & valuations

31 Dec (NT\$m)	FY08	FY09F	FY10F	FY11F
Revenue	7,478	7,380	8,750	9,458
Reported net profit	3,242	2,446	3,099	3,258
Normalised net profit	3,242	2,446	3,099	3,258
Normalised EPS (NT\$)	24.92	18.79	23.82	25.03
Norm. EPS growth (%)	24.3	(24.6)	26.7	5.1
Norm. P/E (x)	14.3	19.0	15.0	14.2
EV/EBITDA (x)	11.5	13.8	10.7	9.6
Price/book (x)	3.9	3.5	3.2	2.9
Dividend yield (%)	2.8	3.3	4.2	3.9
ROE (%)	29.4	19.5	22.3	21.3
Net debt/equity (%)		net cash	net cash	net cash

Earnings revisions			
Previous norm. net profit		2,354	2,607
Change from previous (%)		3.9	18.9
Previous norm. EPS (NT\$)		18.09	20.03

Source: Company, Nomura estimates

## Share price relative to MSCI Taiwan



	1m	3m	6m
Absolute (NT\$)	32.8	44.3	113.5
Absolute (US\$)	34.6	54.6	119.7
Relative to Index	29.7	3.5	57.7
Market cap (US\$m)			1,423
Estimated free float (%)			50.0
52-week range (NT\$)			453.9/167.0
3-mth avg daily turnover (US\$m)			27.32
Stock borrowability			Easy
Major shareholders (%)			
Chen Shih Ching			5.2
Chiang Tsui Ying			5.2

Source: Company, Nomura estimates

**Any authors named on this report are research analysts unless otherwise indicated. See the important disclosures and analyst certifications on pages 13 to 16.**

recovery of the top-tier handset customers will enable Largan's 2Q09F revenue to beat our previous forecast and grow by 47% q-q. This forecast represents the best sequential revenue growth momentum amid major Taiwan handset component makers that we cover. We expect the strength to last into 3Q09F, with sales revenue seen rising 28% q-q, driven by seasonal demand and continued smartphone growth.

- **VCM.** We look for growing opportunities from auto-focus (AF) actuators — a new business for Largan that has a total market value of about US\$300mn (roughly half the size of lens market) in 2009F. We expect this market value to grow at a CAGR of 25% over the 2008-11F period, in light of accelerating resolution migration to 3MP+ and the growth of smartphones. Largan should be able to leverage its strong customer relations and automation manufacturing expertise to earn extra assembly/testing fees from attaching lenses to VCMs (a kind of AF actuator). This should, in turn, pave the way for its in-house VCMs, which have a higher ASP and should have similar a gross margin to the lens units once ramping up. Largan started in-house VCM mass production in May; the ramp-up thus far has been smooth, and this lifts our confidence level regarding the company's potential with in-house VCMs. We expect VCM assembly and in-house VCMs to contribute a combined 9-11% earnings in 2010-11F, up from 5% in 2009F, and we only assume 3.5% and 4.5% global market share (8m and 13.5m units) for Largan in AF actuators in 2010F and 2011F, respectively. Any breakthrough in tier-one handset customers on in-house VCMs could offer upside to our forecasts.
- **New application game console.** We see game console as a new application field for smaller-sized cameras. Recently, a leading game console maker introduced a full-body motion-sensitive technology, which allows gamers to do what they want without holding on to any motion controller. The technology uses special cameras to detect the gamer's motion and is viewed as a revolutionary change in the gaming world. We think Largan, as a leading plastic lens maker, should be well-positioned to address this market. We expect this new application to contribute 5-6% of Largan's earnings in 2010F.

VCMs and game console cameras are growth opportunities for Largan

## ② A new market for Largan — auto-focus actuator

According to iSuppli's forecast (see Exhibit 1), the share of 3MP in handset cameras will grow rapidly from 12% in 2008E to 25%/37% in 2009F/2010F, and the adoption of 5MP+ cameras in high-end phones is also ramping up. We believe the resolution upgrade, especially to 3MP and above, is a positive scenario for the AF function to penetrate the handset market, as higher-resolution cameras usually require an AF function to achieve desired image quality. Exhibit 4 shows that most 3MP+ camera phones go with an AF function.

Below are our forecasts and a background introduction for the AF actuator market.

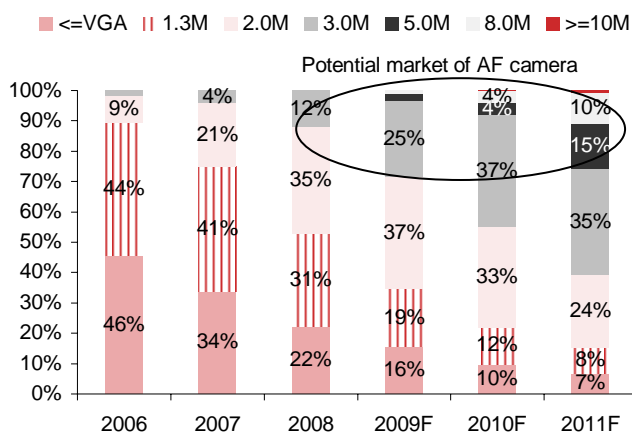
- **Market size:** The total market value of the handset AF actuators, in our estimate, will be about US\$300mn in 2009F. It is about half the size of the handset camera lens market, at US\$635mn. We think the AF actuator market is significant enough for Largan, not only because of its size, but also given the higher ASP (almost twice of the price of a lens unit) and comparable margin versus the lens products.
- **Growth:** We forecast the AF actuator market will grow at a CAGR of 45% in units and a CAGR of 25% in revenue in 2008-11F.
- **Penetration:** We expect the share of handsets with AF cameras will rise from 8% in 2008E to 15% in 2009F and 21% in 2010F, in light of the rising share of 3MP+ cameras.
- **Technology:** There are three kinds of AF actuator technologies — VCM, stepping motor, and piezoelectric motor. Current mainstream technology is VCM, as it has the advantages of smaller size, lower cost, better reliability and more mature

The AF actuator market carries higher ASPs and comparable margins than Largan's lens products

technology (see details in Exhibit 3). The entry barrier of the VCM market is high, however. Even if a maker can solve the design and patent issues, it is difficult to control the production yield rate, as the manufacturing is quite labour-intensive, requiring workers to assemble parts (eg, coil, spring, magnet, yoke and shells) under microscopes. It is easy to understand why this component is sold at a premium price and with a tight supply.

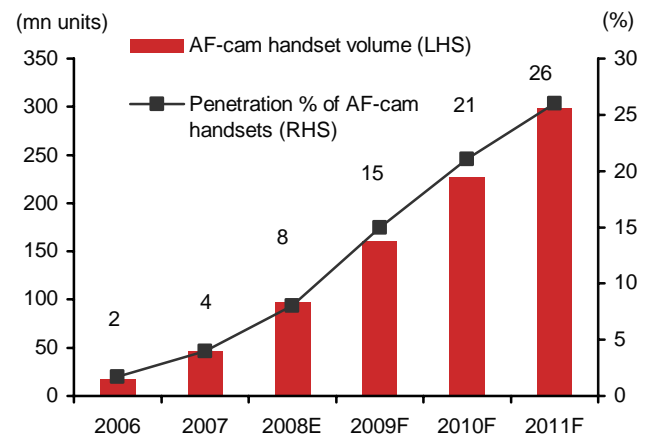
- **Competitive landscapes:** Given the high entry barriers, there are only a few leading players in the VCM market, including Sankyo, Shicoh, Mitsumi, TDK, LG Innotek and SEMCO. Sankyo and Shicoh are the leading players in this market, with a combined market share of around 60% currently.

Exhibit 1. Handset camera resolution mix



Source: iSuppli

Exhibit 2. AF-camera handset forecasts



Source: Nomura International (Hong Kong) Limited, Taipei Branch

Exhibit 3. Comparison of AF actuator technologies

	Voice coil motor	Piezoelectric motor	Stepping motor
Size	Smaller	Smaller	Larger
Cost	Lowest	Low	High
Auto-focus speed	10ms	3ms	100ms
Energy consumption (mJ)	2.4	0.7	21
Repeatability	Good	Poor	Average
Noise issue	No	No	Yes
Mass production	Easier	Not mature	Difficult

Source: Communication component magazine

## Exhibit 4. Latest introduced phones

Vendor	Model	Air interface	Camera resolution	Auto focus	Second camera	Launch time
Nokia	N97	3.5G	5M	Yes	Yes	2Q09
Nokia	N86	3.5G	8M	Yes	Yes	2Q09
Nokia	E75	3.5G	3.2M	Yes	Yes	1Q09
Nokia	E55	3.5G	3.2M	Yes	Yes	2Q09
Nokia	2720 fold	2G	1.3M	No	No	2Q09
Nokia	2730	2G	2M	No	No	2Q09
Nokia	6600i	3G	5M	Yes	Yes	3Q09
Nokia	6216	3G	2M	Yes	Yes	2Q09
Nokia	6710	3.5G	5M	Yes	Yes	3Q09
Nokia	6720	3.5G	5M	Yes	Yes	2Q09
Nokia	6730	3.5G	3.2M	Yes	Yes	2Q09
Nokia	7020	2G	2M	No	No	3Q09
Nokia	5800 (XpressMusic)	3.5G	3.2M	Yes	Yes	4Q08
Nokia	5370 (XpressMusic)	3.5G	3.2M	Yes	Yes	3Q09
Nokia	5330 (XpressMusic)	3G	3.2M	No	No	3Q09
Nokia	5030 (XpressRadio)	2.75G	No	No	No	2Q09
Samsung	A877 (Impression)	3.5G	3.2M	Yes	Yes	2Q09
Samsung	T919 (Behold)	3.5G	5M	Yes	Yes	4Q08
Samsung	T929 (Memoir)	3.5G	8M	Yes	No	1Q09
Samsung	S8300 (UltraTouch)	3.5G	8M	Yes	Yes	2Q09
Samsung	i637 (Jack)	3.5G	3.2M	No	No	2Q09
Samsung	i8910 (Omnia HD)	3.5G	8M	Yes	No	3Q09
Samsung	M7600 (Beat DJ)	3.5G	3M	Yes	No	2Q09
Samsung	M6710 (Beat Disc)	3.5G	3M	No	No	2Q09
Samsung	S30 (Instinct)	3G	2M	No	No	2Q09
Samsung	S7350 (Ultra S)	3.5G	5M	Yes	Yes	2Q09
Samsung	S7220 (Ultra B)	3.5G	5M	Yes	Yes	1Q09
Samsung	U490 (Trance)	3G	1.3M	No	No	2Q09
Samsung	U750 (Alias 2)	3G	2M	Yes	No	2Q09
Samsung	B5702 (Dous)	2.75G	3.2M	Yes	Yes	1Q09
Samsung	B2100/C5212/S3110	2.75G	1.3M	No	No	1Q09
Samsung	E2100B/E2210B/ C3010/ C3050	2.75G	0.3M	No	No	1Q09
Samsung	S3500	2.75G	2M	No	No	1Q09
LGE	KM900 (Arena)	3.5G	5M	Yes	Yes	2Q09
LGE	KC910i (Renoir)	3.5G	8M	Yes	Yes	4Q08
LGE	KP500 (Cookie)	2G	3.2M	No	No	4Q09
LGE	GM730	3.5G	5M	Yes	Yes	
LGE	KT770	3.5G	5M	Yes	Yes	
LGE	GC900 (Viewty 2)	3.5G	8M	Yes	Yes	1H09
LGE	GM310	3.5G	3M	Yes	No	
LGE	GB250	3.5G	1.3M	No	No	
LGE	GB220	2.75G	1.3M	No	No	1H09
Sony Ericsson	Idou	3.5G	12M	Yes	Yes	3Q09
Sony Ericsson	W995	3.5G	8M	Yes	Yes	2Q09
Sony Ericsson	C903	3.5G	5M	Yes	Yes	2Q09
Sony Ericsson	W395	2.75G	2M	No	No	1Q09
HTC	Diamond 2	3.5G	5M	Yes	Yes	2Q09
HTC	Touch Pro 2	3.5G	3.2M	Yes	Yes	2Q09
HTC	Magic	3.5G	3M	Yes	No	2Q09
RIM	Storm 9500	3.5G	3.2M	Yes	No	4Q08
RIM	Bold 9630	3.5G	2M	No	No	2Q09
RIM	Bold 9900	3.5G	3.2M	Yes	No	3Q09
Palm		Pre	3.5G	3.2M	No	2Q09

Source: Company data

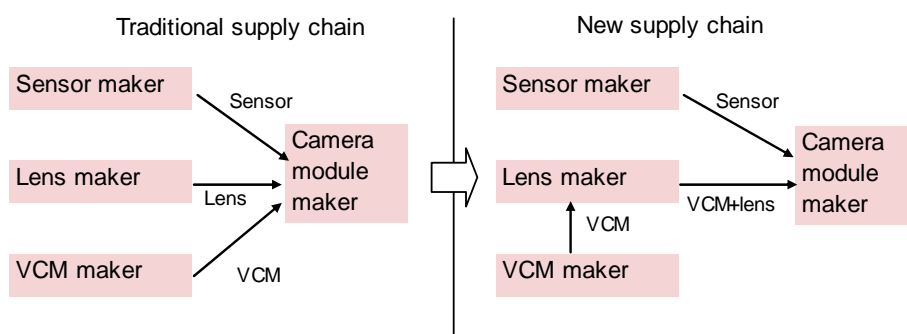
## Why Largan is able to address VCM market?

Largan has been developing its VCM technology for one to two years. We believe it is well-positioned to grow this business over the next two to three years, given the advantages below.

- **Strong capability in automation manufacturing:** In our view, Largan's leading position in the handset camera lens market resulted from its in-house automation manufacturing capability. Now, Largan wants to use this edge in VCM production. The company started mass production of its in-house VCMs in May 2009. Although automation is a new way to produce VCMs, the initial ramp-up has proceeded smoothly thus far. Previously, we were worried about yield rate; however, the good start boosts our confidence in Largan's VCM business, because this is a growing market and those with ready capability should be able to share in the growth. In addition, once volume reaches economies of scale, the automated manufacturing process can help Largan enjoy a margin premium and mass production advantages, relative to other VCM makers.
- **Synergy with its lens business:** VCM and lens are sharing the same customers — camera module makers and handset vendors. There are two supply chains (see Exhibit 5): 1) VCM makers can supply directly to camera module makers, or; 2) VCM makers ship to lens makers first, then lens makers assemble the VCM and lens together and supply to module makers (Apple and RIM use the latter flow). With the capability of both VCM and lens, Largan can provide a total solution (VCM+lens) to module makers.

**Largan can leverage existing capabilities to penetrate the VCM market**

### Exhibit 5. Evolution of handset camera module supply chain



Source: Nomura International (Hong Kong) Limited, Taipei Branch

## Growth driver for Largan in 2010-11F

We see two ways for Largan to benefit from the AF trend:

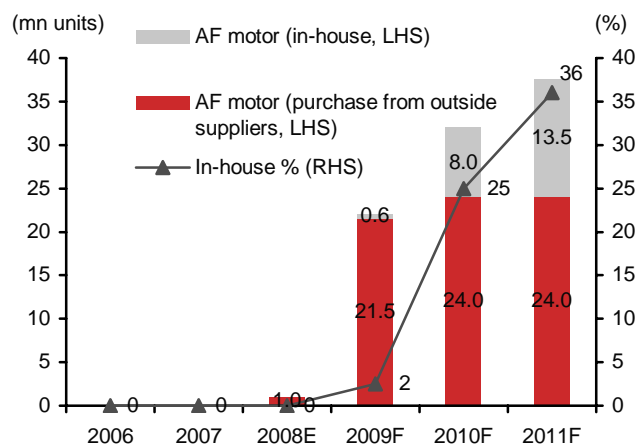
- **VCM+lens assembly.** Given the unstable yield rates of AF actuators and the difficulty in attaching lens units to AF actuators, camera module makers could suffer from yield rate risks, if they do all the assembly steps themselves. Now, some camera module makers or handset OEMs require lens makers to do the lens unit and VCM assembly, in order to reduce such risks. We believe Largan can charge extra fees from doing assembly and testing. Although the assembly margin is low, these would be incremental earnings for Largan.
- **In-house produced VCMs.** VCMs have a higher ASP and similar margin (if yield rate is fine and scale is ramped) versus lens units. As Largan is new to this field, the company started with smaller customers at the start. Given the lack of tier-one customers for VCMs at present, we only model 3.5% and 4.5% global market share for its in-house VCMs in 2010F and 2011F, respectively (see Exhibit 7). Any breakthrough on tier-one customers, however, could offer upside to our forecasts.

**VCM-related business will contribute 9-11% of earnings in 2010-11F, on our estimates**

We estimate that 19% of Largan's revenue in 2009F will come from VCMs, but its in-house produced VCMs would account for <1% of revenue, with the other 18% from reselling purchased VCMs and related assembly fees. The revenue contribution from in-house VCMs should ramp up to 5%/7% in 2010F/2011F, we expect, while the revenue from re-selling purchased VCMs should decline to 15%/12%, respectively (see Exhibit 9).

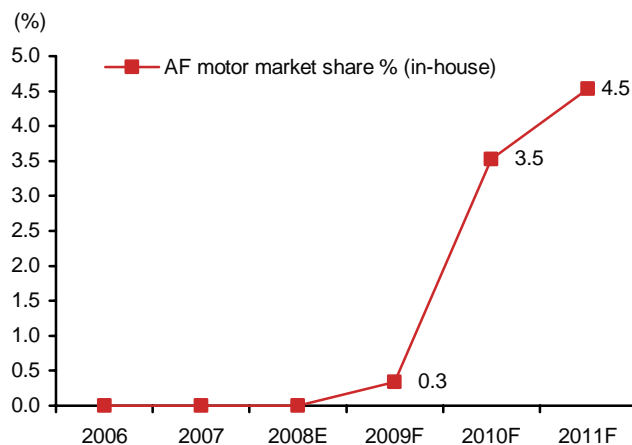
Overall, we forecast that VCM-related business will contribute 9-11% of Largan's earnings in 2010-11F.

**Exhibit 6. Largan: AF motor shipment forecasts**



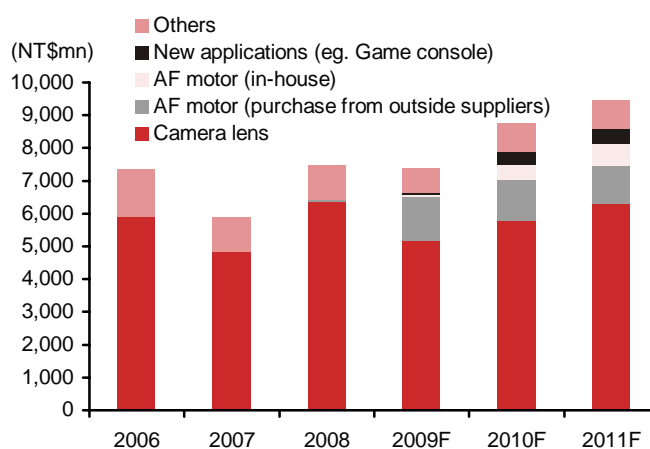
Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

**Exhibit 7. Largan: AF motor market share forecasts**



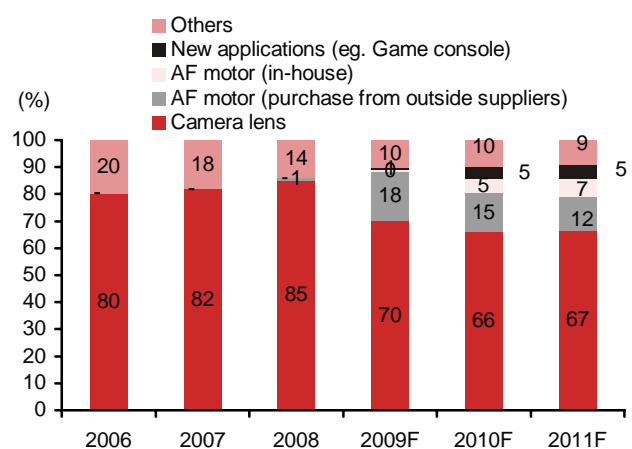
Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

**Exhibit 8. Largan: Sales breakdown**



Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

**Exhibit 9. Largan: Sales mix %**



Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

We present the sensitivity of Largan's FY10F EPS to its in-house VCM market share and gross margin in Exhibit 10. In our base case, we assume Largan to have 3.5% global market share (8m unit shipments) in 2010F. We then show that if Largan were to increase its market share to 5.5%/7.5% (12.5m/17m unit shipments), FY10F EPS would grow by 31.3%/35.9% (versus base case 26.7%). In our view, any penetration into tier-one customers could easily offer that volume (1-1.5m units per month).

**Exhibit 10. Sensitivity to in-house VCM market share (FY10F)**

	Base case			
In-house VCM market share (%)	1.5%	3.5%	5.5%	7.5%
In-house VCM shipment units (mn units)	3.4	7.9	12.5	17.0
FY10F EPS (NT\$)	22.9	23.8	24.7	25.5
FY10F EPS growth (%)	22.0	26.7	31.3	35.9
FY10F P/E (x)	15.5	15.0	14.4	14.0

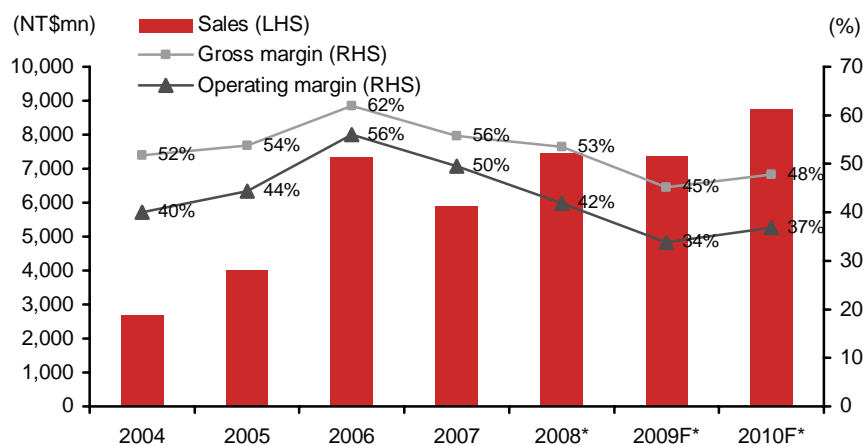
Source: Nomura International (Hong Kong) Limited, Taipei branch

## Margin decline? A reflection of product mix change

In our view, Largan's gross margin decline (from 53% in 2008 to 45% in FY09F) reflects a product mix change and low utilization in 1H09F. Both VCM assembly and in-house VCMs are new businesses for Largan. VCM assembly has a below-average margin, while in-house VCM, once reaching enough scale, should have an above-average margin. Assuming VCM+lens assembly grows rapidly in 2009F, the gross margin should decline with the ramp-up of assembly revenue. We expect the gross margin will gradually recover in 2H09F, however, and further trend up in FY10F, as the growth of in-house VCMs and the new game console applications should offset the margin pressure in its lens business and VCM assembly.

**A shift in product mix will pressure margins in FY09F**

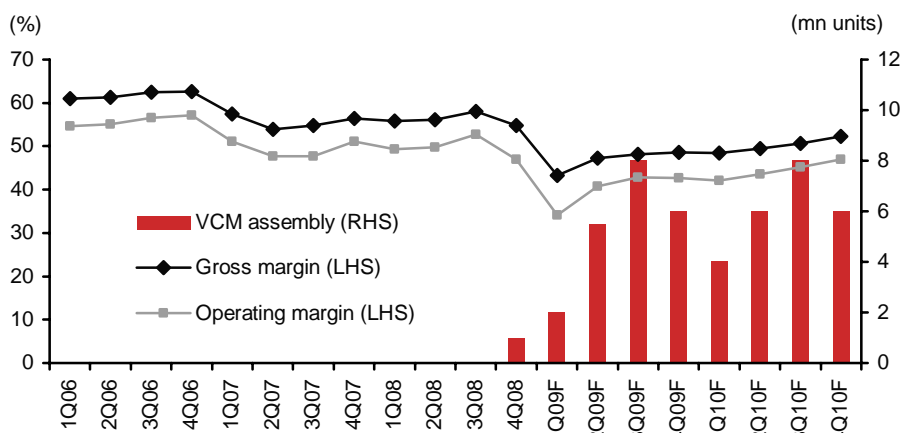
**Exhibit 11. Largan: sales and margin trends**



\* Employee bonus started to be expensed from 2008.

Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

**Exhibit 12. Largan: the increase in VCM assembly will lower margins (excluding bonus expenses)**



Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

### ③ New games, new opportunities

The application of small-sized cameras is broadening into game consoles, from traditional handset and NB/DT PC applications. Recently, a leading game console maker introduced a full-body motion-sensitive technology that allows gamers to do what they want without holding on to any motion controller. The technology uses special cameras to detect a gamer's motion and is viewed as a revolutionary change in the gaming world.

**As a leading plastic lens maker, Largan, has high potential to address this market, in our view**

According to IDC, the installed base of this game console maker was 28.4mn units at end-2008. IDC forecasts 12.0mn and 12.1mn unit shipments for that game console maker in 2009F and 2010F, respectively, up from 10.8mn units in 2008. As the full-body motion-sensitive technology can be used in both old and new game consoles of that maker, it can attract new buyers, as well as existing device owners. Compared to Nintendo Wii's shipments of 17mn and 25mn units in the second (2007) and third year (2008), respectively, after the launch in 2006, we see good potential for this project next year.

We think Largan, as a leading plastic lens maker, has high potential to address this market. We forecast Largan will ship 6mn game console cameras in 2010F, and this could contribute 5-6% of earnings in FY10F. Given that the formal launch timing remains uncertain, we have a sensitivity analysis for next year's volume in Exhibit 15.

### Exhibit 13. Full-body motion-sensitive device



Source: Company data

### Exhibit 14. Using your body to play games



Source: Company data

### Exhibit 15. Sensitivity to game console camera volume (FY10F)

			Base case		
Game console lens shipment units (mn units)	2.0	4.0	6.0	8.0	10.0
FY10F EPS (NT\$)	22.8	23.3	23.8	24.3	24.8
FY10F EPS growth (%)	21.3	24.0	26.7	29.5	32.1
FY10F P/E (x)	15.6	15.3	15.0	14.7	14.4

Source: Nomura International (Hong Kong) Limited, Taipei branch

### ④ Earnings revisions. Multiple catalysts are in place.

We are raising our earnings forecasts by 4% for FY09F and 18-24% for FY10-11F, chiefly reflecting the better-than-expected shipments on smartphones, ramp-up of VCM-related businesses and the new opportunity in game console applications. Our 12-month price target of NT\$429 is based on 18x FY10F EPS (from NT\$245, 13x 2Q09-1Q10F EPS). We raise our target P/E multiple from the lower-end (13x) of the historical trading range (10-40x), to the mid- to high-end (18x). Previously, we used the lower-end historical P/E 13x, as handset component peers were traded in 10-11x range for 2010F. Now, the peer average has been boosted to 13-14x for 2010F. We think the rising benefits from smartphones, the growth opportunity in VCMs and the potential in new game console applications could trigger a re-rating for Largan's share price. We upgrade Largan to BUY from Neutral.

Largan has long traded at a premium to other Asian handset component makers, because of its solid execution, quality management, strong balance sheet (no debt,

high cash) and leading position in handset lens units. However, compared to other optical lens makers and VCM makers in the region, Largan has better profitability and its P/E valuation is the lowest (see Exhibit 19).

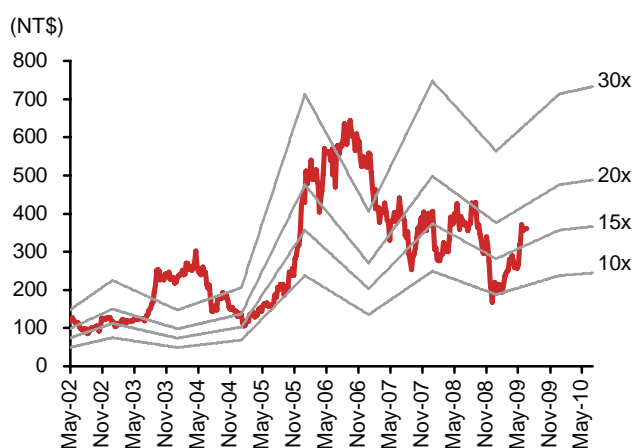
**Risks to price target:** Key risks to our price target include the following: 1) weaker-than-expected global demand; 2) increased competition from other lens makers or in-house capacity of camera module makers; 3) ASP erosion; 4) smaller-than-forecast earnings contribution from new products; and 5) faster-than-expected progress on competitive technology, such as wafer-level optics.

### Exhibit 16. Largan: earnings revisions

(NT\$m)	New forecasts			Old forecasts			Difference (%)		
	FY09F	FY10F	FY11F	FY09F	FY10F	FY11F	FY09F	FY10F	FY11F
Revenue	7,380	8,750	9,458	6,860	7,649	7,978	7.6	14.4	18.5
Gross profit	3,335	4,184	4,394	3,147	3,602	3,654	6.0	16.1	20.3
Operating profit	2,497	3,221	3,394	2,323	2,713	2,746	7.5	18.7	23.6
Pre-tax profit	2,576	3,309	3,482	2,482	2,801	2,834	3.8	18.1	22.9
Net profit	2,446	3,099	3,258	2,354	2,607	2,629	3.9	18.9	23.9
EPS (NT\$)	18.8	23.8	25.0	18.1	20.0	20			
<b>Margin (%)</b>									
Gross margin	45.2	47.8	46.5	45.9	47.1	45.8	(0.7)	0.7	0.7
Operating margin	33.8	36.8	35.9	33.9	35.5	34.4	(0.0)	1.3	1.5
Pre-tax margin	34.9	37.8	36.8	36.2	36.6	35.5	(1.3)	1.2	1.3
Net margin	33.1	35.4	34.4	34.3	34.1	33.0	(1.2)	1.3	1.5

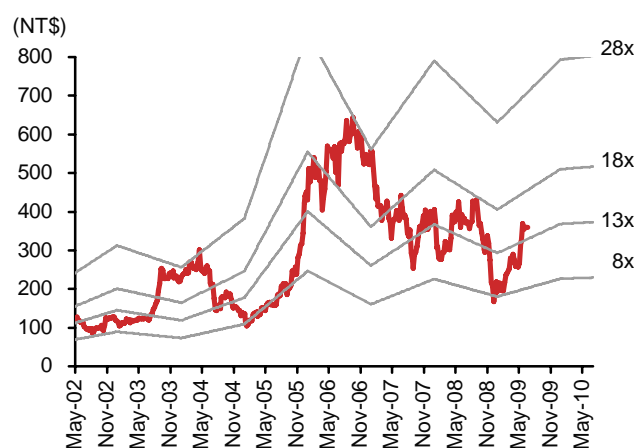
Source: Company data, Nomura International (Hong Kong) Limited, Taipei Branch

### Exhibit 17. Largan: P/E bands (bonus-adjusted)



Source: TEJ, Nomura International (Hong Kong) Limited, Taipei Branch

### Exhibit 18. Largan: P/E bands (non bonus-adjusted)



Source: TEJ, Nomura International (Hong Kong) Limited, Taipei Branch

## Exhibit 19. Handset component and optical peers: valuation comparison

Code	Company	Price (5-Jun)	Nomura Rating	Price Target	P/E (x)			P/BV (x)			ROE (%)		
					FY08F	FY09F	FY10F	FY08F	FY09F	FY10F	FY08F	FY09F	FY10F
<b>Handset Component</b>													
3008 TT	Largan	356.50	BUY	429.0	14.3	19.0	15.0	3.9	3.5	3.2	29.4	19.5	22.3
2439 TT	Merry	35.85	REDUCE	19.7	10.1	18.2	14.6	1.3	1.3	1.3	12.6	7.2	8.9
3311 TT	Silitech	71.00	NEUTRAL	66.6	10.8	13.9	12.6	2.7	2.5	2.2	25.5	18.6	18.5
2301 TT	Lite-On	28.75	NEUTRAL	28.4	14.4	12.4	10.9	1.1	1.0	1.0	7.5	8.8	9.4
3037 TT	Unimicron	27.00	NEUTRAL	22.2	12.0	21.7	12.9	1.0	1.0	0.9	8.6	4.7	7.5
3044 TT	Tripod	60.90	BUY	62.5	9.9	14.0	10.9	1.8	1.7	1.5	19.3	12.3	14.5
2018 HK	AAC Acoustic	6.54	BUY	6.26	12.0	14.0	12.2	2.3	2.0	1.8	20.8	15.4	15.7
1211 HK	BYD	33.35	REDUCE	24.50	59.0	34.9	27.2	5.3	4.3	3.7	9.3	14.0	14.7
HIP SP	Hi-P	0.72	NEUTRAL	0.32	4.2	6.5	5.0	0.8	0.7	0.6	20.0	11.2	13.1
<b>Handset component peers average</b>					<b>16.3</b>	<b>17.2</b>	<b>13.5</b>	<b>2.3</b>	<b>2.0</b>	<b>1.8</b>	<b>17.0</b>	<b>12.4</b>	<b>13.9</b>
<b>Optical</b>													
3008 TT	Largan	356.50	BUY	429.0	14.3	19.0	15.0	3.9	3.5	3.2	29.4	19.5	22.3
3406 TT	Genius	50.00	Not rated	na	na	na	na	1.2	1.3	na	(19.5)	na	na
7741 JP	Hoya	2,060.0	BUY	2,042.0	35.5	31.0	17.5	2.7	2.6	2.4	7.4	8.4	13.9
7752 JP	Ricoh	1,339.0	BUY	1,550.0	148.8	48.5	22.6	1.0	1.0	1.0	0.7	2.0	4.2
6961 JP	Enplas	961.0	Not rated	na	na	na	na	0.5	na	na	(21.6)	na	na
4902 JP	Konica- Minolta	1,077	BUY	1,200.0	37.7	27.2	16.3	1.4	1.4	1.3	3.7	5.0	7.8
085660 KS	Diostech	12,700	Not rated	na	40.3	na	na	3.8	na	na	7.8	na	na
<b>Optical peers average</b>					<b>55.3</b>	<b>31.4</b>	<b>17.8</b>	<b>2.1</b>	<b>2.0</b>	<b>2.0</b>	<b>1.1</b>	<b>8.7</b>	<b>12.1</b>
<b>VCM</b>													
011070 KS	LG Innotek	124,500.0	Not rated	na	22.4	25.0	18.9	3.0	2.9	2.6	15.1	11.5	13.5
6667 JP	Shicoh	42,800.0	Not rated	na	na	na	na	1.0	na	na	(60.6)	na	na
7757 JP	Nidec Sankyo	467.0	Not rated	na	47.6	na	na	1.2	na	na	2.5	na	na
<b>VCM peers average</b>					<b>35.0</b>	<b>25.0</b>	<b>18.9</b>	<b>1.7</b>	<b>2.9</b>	<b>2.6</b>	<b>(14.3)</b>	<b>11.5</b>	<b>13.5</b>

Note: For method and risk pertaining to price targets, please see the last published Nomura report on each company.

Source: Bloomberg, Nomura International (Hong Kong) Limited

# Financial statements

Income statement (NT\$m)					
Year-end 31 Dec	FY07	FY08	FY09F	FY10F	FY11F
<b>Revenue</b>	5,882	7,478	7,380	8,750	9,458
Cost of goods sold	(2,604)	(3,481)	(4,044)	(4,566)	(5,064)
<b>Gross profit</b>	<b>3,278</b>	<b>3,997</b>	<b>3,335</b>	<b>4,184</b>	<b>4,394</b>
SG&A	(361)	(869)	(838)	(963)	(999)
Employee share expense	-	-	-	-	-
<b>Operating profit</b>	<b>2,917</b>	<b>3,129</b>	<b>2,497</b>	<b>3,221</b>	<b>3,394</b>
<b>EBITDA</b>	<b>3,468</b>	<b>3,694</b>	<b>3,115</b>	<b>3,961</b>	<b>4,294</b>
Depreciation	(551)	(565)	(618)	(740)	(900)
Amortisation	-	-	-	-	-
<b>EBIT</b>	<b>2,917</b>	<b>3,129</b>	<b>2,497</b>	<b>3,221</b>	<b>3,394</b>
Net interest expense	48	56	44	48	48
Associates & JCEs	15	60	52	40	40
Other income	22	94	(17)	-	-
<b>Earnings before tax</b>	<b>3,002</b>	<b>3,338</b>	<b>2,576</b>	<b>3,309</b>	<b>3,482</b>
Income tax	(432)	(96)	(130)	(209)	(224)
<b>Net profit after tax</b>	<b>2,570</b>	<b>3,242</b>	<b>2,446</b>	<b>3,099</b>	<b>3,258</b>
Minority interests	-	-	-	-	-
Other items	-	-	-	-	-
Preferred dividends	-	-	-	-	-
<b>Normalised NPAT</b>	<b>2,570</b>	<b>3,242</b>	<b>2,446</b>	<b>3,099</b>	<b>3,258</b>
Extraordinary items	-	-	-	-	-
<b>Reported NPAT</b>	<b>2,570</b>	<b>3,242</b>	<b>2,446</b>	<b>3,099</b>	<b>3,258</b>
Dividends	(1,232)	(1,301)	(1,541)	(1,953)	(1,792)
<b>Transfer to reserves</b>	<b>1,338</b>	<b>1,941</b>	<b>905</b>	<b>1,147</b>	<b>1,466</b>

We re-allocate 30% of employee bonus expenses to COGS and 70% to operating expenses in FY09-11F

## Valuation and ratio analysis

FD normalised P/E (x)	17.8	14.3	19.0	15.0	14.2
FD normalised P/E at price target (x)	21.4	17.2	22.8	18.0	17.1
Reported P/E (x)	17.8	14.3	19.0	15.0	14.2
Dividend yield (%)	2.7	2.8	3.3	4.2	3.9
Price/cashflow (x)	12.6	10.4	19.7	13.3	11.5
Price/book (x)	4.4	3.9	3.5	3.2	2.9
EV/EBITDA (x)	12.7	11.5	13.8	10.7	9.6
EV/EBIT (x)	15.1	13.5	17.1	13.1	12.1
Gross margin (%)	55.7	53.5	45.2	47.8	46.5
EBITDA margin (%)	59.0	49.4	42.2	45.3	45.4
EBIT margin (%)	49.6	41.8	33.8	36.8	35.9
Net margin (%)	43.7	43.4	33.1	35.4	34.4
Effective tax rate (%)	14.4	2.9	5.1	6.3	6.4
Dividend payout (%)	47.9	40.1	63.0	63.0	55.0
Capex to sales (%)	12.2	18.6	8.8	11.4	10.6
Capex to depreciation (x)	1.3	2.5	1.1	1.4	1.1
ROE (%)	26.7	29.4	19.5	22.3	21.3
ROA (pretax %)	31.8	33.4	23.5	27.3	27.5

Top-line slowdown in FY09F

## Growth (%)

Revenue	(19.9)	27.1	(1.3)	18.6	8.1
EBITDA	(25.0)	6.5	(15.7)	27.1	8.4
EBIT	(29.1)	7.3	(20.2)	29.0	5.4
Normalised EPS	(35.0)	24.3	(24.6)	26.7	5.1
Normalised FDEPS	(35.0)	24.3	(24.6)	26.7	5.1

## Per share

Reported EPS (NT\$)	20.0	24.9	18.8	23.8	25.0
Norm EPS (NT\$)	20.0	24.9	18.8	23.8	25.0
Fully diluted norm EPS (NT\$)	20.0	24.9	18.8	23.8	25.0
Book value per share (NT\$)	80.5	91.7	100.6	112.6	122.6
DPS (NT\$)	9.8	10.0	11.8	15.0	13.8

Source: Nomura estimates

<b>Cashflow (NT\$mn)</b>					
<b>Year-end 31 Dec</b>	<b>FY07</b>	<b>FY08</b>	<b>FY09F</b>	<b>FY10F</b>	<b>FY11F</b>
EBITDA	3,468	3,694	3,115	3,961	4,294
Change in working capital	510	711	(703)	(242)	(15)
Other operating cashflow	(360)	40	(55)	(220)	(262)
<b>Cashflow from operations</b>	<b>3,619</b>	<b>4,444</b>	<b>2,357</b>	<b>3,499</b>	<b>4,017</b>
Capital expenditure	(720)	(1,393)	(650)	(1,000)	(1,000)
<b>Free cashflow</b>	<b>2,899</b>	<b>3,051</b>	<b>1,708</b>	<b>2,499</b>	<b>3,017</b>
Reduction in investments	206	(405)	(1,060)	(40)	(40)
Net acquisitions	-	-	-	-	-
Reduction in other LT assets	4	(16)	(22)	(59)	(86)
Addition in other LT liabilities	9	7	3	0	0
Adjustments	(1)	(67)	83	98	126
<b>Cashflow after investing acts</b>	<b>3,117</b>	<b>2,571</b>	<b>712</b>	<b>2,499</b>	<b>3,017</b>
Cash dividends	(1,383)	(1,232)	(1,301)	(1,541)	(1,953)
Equity issue	-	-	-	-	-
Debt issue	(239)	87	(68)	-	-
Convertible debt issue	-	-	-	-	-
Others	(220)	(86)	0	-	-
<b>Cashflow from financial acts</b>	<b>(1,842)</b>	<b>(1,232)</b>	<b>(1,369)</b>	<b>(1,541)</b>	<b>(1,953)</b>
<b>Net cashflow</b>	<b>1,275</b>	<b>1,339</b>	<b>(657)</b>	<b>958</b>	<b>1,064</b>
Beginning cash	903	2,178	3,517	2,860	3,818
Ending cash	2,178	3,517	2,860	3,818	4,882
Ending net debt	(2,153)	(3,406)	(2,817)	(3,775)	(4,839)

Source: Nomura estimates

<b>Balance sheet (NT\$mn)</b>					
<b>As at 31 Dec</b>	<b>FY07</b>	<b>FY08</b>	<b>FY09F</b>	<b>FY10F</b>	<b>FY11F</b>
Cash & equivalents	2,178	3,517	2,860	3,818	4,882
Marketable securities	2,038	2,388	3,406	3,406	3,406
Accounts receivable	1,782	1,494	1,779	2,087	2,129
Inventories	620	625	742	812	880
Other current assets	97	234	240	240	240
<b>Total current assets</b>	<b>6,715</b>	<b>8,257</b>	<b>9,026</b>	<b>10,364</b>	<b>11,537</b>
LT investments	205	261	302	342	382
Fixed assets	4,163	5,018	4,987	5,247	5,347
Goodwill	-	-	-	-	-
Other intangible assets	-	-	-	-	-
Other LT assets	89	105	127	186	272
<b>Total assets</b>	<b>11,172</b>	<b>13,640</b>	<b>14,442</b>	<b>16,139</b>	<b>17,539</b>
Short-term debt	24	111	43	43	43
Accounts payable	401	1,097	998	1,135	1,229
Other current liabilities	586	455	259	259	259
<b>Total current liabilities</b>	<b>1,012</b>	<b>1,662</b>	<b>1,300</b>	<b>1,437</b>	<b>1,531</b>
Long-term debt	-	-	-	-	-
Convertible debt	-	-	-	-	-
Other LT liabilities	40	47	50	50	51
<b>Total liabilities</b>	<b>1,051</b>	<b>1,709</b>	<b>1,350</b>	<b>1,487</b>	<b>1,582</b>
Minority interest	-	-	-	-	-
Preferred stock	-	-	-	-	-
Common stock	1,257	1,301	1,301	1,301	1,301
Retained earnings	6,651	8,254	9,409	10,967	12,272
Proposed dividends	-	-	-	-	-
Other equity and reserves	2,213	2,376	2,383	2,383	2,383
<b>Total shareholders' equity</b>	<b>10,121</b>	<b>11,931</b>	<b>13,093</b>	<b>14,651</b>	<b>15,956</b>
<b>Total equity &amp; liabilities</b>	<b>11,172</b>	<b>13,640</b>	<b>14,442</b>	<b>16,139</b>	<b>17,539</b>

Cash-rich

No long-term debt  
on Largan's books**Liquidity (x)**

Current ratio	6.64	4.97	6.94	7.21	7.53
Interest cover	na	na	na	na	na

**Leverage**

Net debt/EBITDA (x)	net cash	net cash	net cash	net cash	net cash
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash

**Activity (days)**

Days receivable	119.7	80.2	80.9	80.6	81.4
Days inventory	89.9	65.5	61.7	62.1	61.0
Days payable	55.1	78.8	94.5	85.2	85.2
Cash cycle	154.5	66.8	48.1	57.5	57.2

Source: Nomura estimates

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Issuer	Ticker	Price (as at last close)	Closing Price Date	Rating	Disclosures
Largan Precision	3008 TT	356.50 TWD	05 Jun 2009	Neutral	

## Previous Ratings

Issuer	Previous Rating	Date of change
Largan Precision	No Rating	05 Sep 2008

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Stocks:

- A rating of "1", or "**Buy**", indicates that the analyst expects the stock to outperform the Benchmark over the next 12 months.
- A rating of "2", or "**Neutral**", indicates that the analyst expects the stock to perform in line with the Benchmark over the next 12 months.
- A rating of "3", or "**Reduce**", indicates that the analyst expects the stock to underperform the Benchmark over the next 12 months.
- A rating of "**RS-Rating Suspended**", " indicates that the rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the company.

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- A rating of "3", or "**Neutral**", indicates that the analyst expects the stock to either outperform or underperform the Benchmark by less than 5% over the next six months.
- A rating of "4", or "**Reduce**", indicates that the analyst expects the stock to underperform the Benchmark by 5% or more but less than 15% over the next six months.
- A rating of "5", or "**Sell**", indicates that the analyst expects the stock to underperform the Benchmark by 15% or more over the next six months.
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A "**Neutral**" stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next six months.

A "**Bearish**" stance, indicates that the analyst expects the sector to underperform the Benchmark during the next six months.

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- A "**Strong buy**" recommendation indicates that upside is more than 20%.
- A "**Buy**" recommendation indicates that upside is between 10% and 20%.
- A "**Neutral**" recommendation indicates that upside or downside is less than 10%.
- A "**Reduce**" recommendation indicates that downside is between 10% and 20%.
- A "**Sell**" recommendation indicates that downside is more than 20%.

### Sectors:

A "**Bullish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a positive absolute recommendation.

A "**Neutral**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a neutral absolute recommendation.

A "**Bearish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a negative absolute recommendation.

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