



Skyworth Digital Holdings

Lifting PT to HK\$8.2 - Strong Feb sales on high-end TV demand

Skyworth is the largest branded TV maker in the China domestic market. Shares are up 22% in the past month (HSCEI down 0.6%) but we still see significant potential upside to our DCF based Dec 15 PT of HK\$8.2 (prev. HK\$7.0). Skyworth has a clear strategy to leverage its wide distribution network and strong rural brand name to roll out a number of new business streams and most of this potential is not yet reflected in the share price.

- Fantastic Feb sales just the beginning** - Skyworth reported 78% Y/Y unit sales growth in China which is a phenomenal achievement and best growth in at least a year. The increase in ASP of 2% was also much better than expected (ASP down 15% from Aug 14 to Jan 15) and is due to strong sales of larger and higher end TVs with above average margins. We continue to see more upside to the share price driven by a recovery in the TV business, rapid expansion into white goods and potential impact of new blockbuster businesses such as internet content and e-commerce fulfillment. Our new SOTP value is HK\$12.0 (previously HK\$9.0).
- Lifting net profits and PT.** We are lifting FY15E and FY16E sales by 1.2% and 2.5%, respectively, to reflect strong Feb 15 sales. We are lifting our FY15E and FY16E net profit by 0.6% and 7.9%, respectively, to reflect the higher sales. Our DCF-based Dec-14 share price target is lifted to HK\$8.2 (previously HK\$7.0) due to the earnings revisions.
- Price, valuation and risk.** Skyworth trades at 6.1 FY15 PE and 7.9x FY16E P/E. Our PT (Dec-15, DCF-derived; WACC: 12%; terminal growth of 3%) of HK\$8.2 implies a forward P/BV of 1.7x and forward P/E of 11.3x CY16E). Key risks to our PT are: the timing of the commencement of government incentive /subsidy schemes for TVs, and a higher cost of components cutting into margins.

Overweight

0751.HK, 751 HK

Price: HK\$5.50

▲ **Price Target: HK\$8.20**
Previous: HK\$7.00

China

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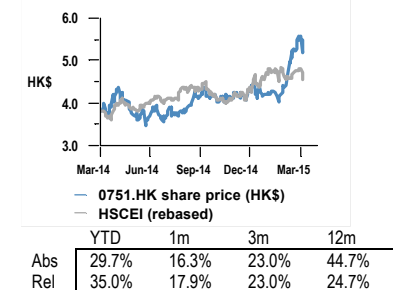
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Price Performance



Skyworth Digital Holdings (Reuters: 0751.HK, Bloomberg: 751 HK)

HK\$ in mn, year-end Mar	FY12A	FY13A	FY14A	FY15E	FY16E
Revenue (HK\$ mn)	28,137	37,824	39,480	41,642	48,088
Net Profit (HK\$ mn)	1,252	1,501	1,254	2,615	2,052
EPS (HK\$)	0.46	0.54	0.45	0.91	0.70
DPS (HK\$)	0.15	0.17	0.15	0.22	0.17
Revenue growth (%)	15.6%	34.4%	4.4%	5.5%	15.5%
EPS growth (%)	12.0%	17.4%	(18.0%)	103.8%	(23.0%)
ROCE	10.9%	12.0%	9.8%	10.7%	12.3%
ROE	16.1%	16.3%	12.1%	13.2%	15.1%
P/E (x)	11.9	10.1	12.3	6.1	7.9
P/BV (x)	1.8	1.5	1.4	1.2	1.1
EV/EBITDA (x)	6.6	5.8	5.7	4.2	3.7
Dividend Yield	2.6%	3.1%	2.7%	3.9%	3.0%

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

Company Data

Shares O/S (mn)	2,830
Market Cap (HK\$ mn)	15,565
Market Cap (\$ mn)	2,007
Price (HK\$)	5.50
Date Of Price	05 Mar 15
Free Float(%)	63.5%
3M - Avg daily vol (mn)	8.70
3M - Avg daily val (HK\$ mn)	41.68
3M - Avg daily val (\$ mn)	5.4
HSCEI	1,1597.77
Exchange Rate	7.76
Price Target End Date	31-Dec-15
Price Target (HK\$)	8.20

See page 14 for analyst certification and important disclosures, including non-US analyst disclosures.

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<p>Key catalysts for the stock price:</p> <ul style="list-style-type: none"> • New subsidies or incentives to stimulate appliance demand from the govt. • More sales from new white goods business • Higher proportion of sales through dedicated Skyworth retail outlets 	<p>Upside risks to our view:</p> <ul style="list-style-type: none"> • More demand for TVs as a result of the end of analog broadcasting in Dec 2015 • Higher demand for TVs and easier comparable numbers once consumers stop waiting for government incentives • More content related revenues from smart TVs 	<p>Downside risks to our view:</p> <ul style="list-style-type: none"> • Margins coming down as competition picks up from internet content providers selling cheap TVs • Margins on high end Ultra-High definition TVs come down as product matures • Poor sales for TVs as property market softens under a tight credit environment
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Key financial metrics	FY13	FY14	FY15E	FY16E
Revenues (LC)	37,824	39,480	41,642	48,088
Revenue growth (%)	-25.6%	4.4%	5.5%	15.5%
EBITDA (LC)	2,366	2,336	2,788	3,457
EBITDA margin (%)	6.3%	5.9%	6.7%	7.2%
Tax rate (%)	17%	16%	10%	15%
Net profit (LC)	1,501	1,254	2,615	2,052
EPS (LC)	0.544	0.446	0.909	0.699
EPS growth (%)	17.4%	82.0%	203.8%	77.0%
DPS (LC)	0.17	0.15	0.22	0.17
BVPS (LC)	3.56	3.82	4.44	4.89
Operating cash flow (LC mn)	(391)	3,900	3,383	1,886
Free cash flow (LC mn)	(894)	1,668	2,634	245
Interest cover (x)	18	14	17	21
Net margin (%)	4.0%	3.2%	6.3%	4.3%
Sales/assets (X)	1.47	1.29	1.23	1.29
Debt/equity (%)	56.7%	50.3%	42.1%	37.2%
Net debt/equity (%)	34.2%	23.6%	7.1%	10.8%
ROE (%)	16%	12%	13%	15%
Key model assumptions	FY13	FY14E	FY15E	FY16E
CRT (000 units sold)	490	212	0	0
LED (000 units sold)	8779	11108	12663	13676
LED (GPM %)	19%	19%	19%	19%

Source: Company and J.P. Morgan estimates.

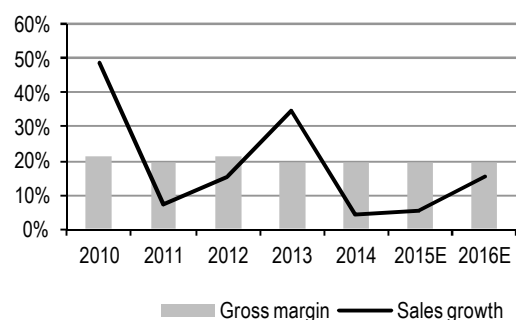
Sensitivity analysis	EBITDA		EPS	
Sensitivity to	FY14E	FY15E	FY14E	FY15E
Panel prices (5% drop)	14%	13%	27%	14%
Domestic LCD sales (5%)	9%	16%	17%	17%
1% change in GPM	13%	14%	21%	27%

Source: J.P. Morgan estimates.

Valuation and price target basis

Our Dec-15 price target is based on a DCF valuation that assumes a market risk premium of 6.0% and a risk-free rate of 4.2%. Our Beta is 1.3, and accordingly, we assume a WACC of 12.0%

Sales growth vs GPM trends



Source: Bloomberg, Company and J.P. Morgan estimates.

JPM vs. consensus, change in estimates

EPS (LC)	FY15E	FY16E
JPM old	0.531	0.648
JPM new	0.536	0.699
% chg	1%	8%
Consensus	0.601	0.618

Source: Bloomberg, J.P. Morgan estimates.

Peer comparison – Consumer electronic companies in China

Companies	Ticker	LC, (PT)	MCAP US\$mn	Vol US\$mn	1W chg	3M chg	CY13E P/E (x)	CY14E P/E(x)	13E ROE	13E PB	13E Yld (%)	13E ND/E (%)
SKYWORTH (OW)*	751 HK	5.50 (8.2)	2,088	8.8	3.4	28.0	12.2	7.2	14.8	1.8	2.5	23.9
TCL MULTIMEDIA (OW)*	1070 HK	4.41 (3.5)	742	3.2	(5.7)	35.2	(47.0)	23.5	19.9	1.0	5.7	(52.0)
HAIER ELECTRONIC (NC)	1169 HK	19.64	6,897	7.0	(2.9)	(4.5)	17.7	14.7	26.4	4.3	0.6	(70.3)
HISENSE ELEC-A (NC)	600060 CH	21.35	3,976	204.6	(2.2)	69.4	18.2	16.2	13.0	2.5	1.4	(15.1)
Average					(1.8)	32.0	0.3	15.4	18.5	2.4	2.2	(28.4)

Source: Bloomberg, J.P. Morgan estimates (*). Bloomberg estimates for NC companies. Share prices are as of Mar 05, 2015

Stronger than expected February sales

The Feb unit sales shows strong unit sales growth (up 78% Y/Y following up 39% Y/Y growth in Jan - the best month ever in unit sales). The strong sales in Feb is a good indication that sell through during CNY was quite good for Skyworth. Management mentioned strong orders coming from retailers after the holidays. March 2014 sales were quite strong and a tough comp period for March 2015 (and probably further away from CNY compared to March 2015 so normally meaning better sales) so we have factored in a 11% drop already in our estimates for March 2015.

Another key positive is that ASP in Feb14 increased by 2%Y/Y, the first increase in a year, which compares to a 15% decrease in ASP over the past six months (Aug 14 to Jan 15). We note that Skyworth has pushed out higher end new 4K TVs (20% of sales now) and also larger TVs during the holidays.

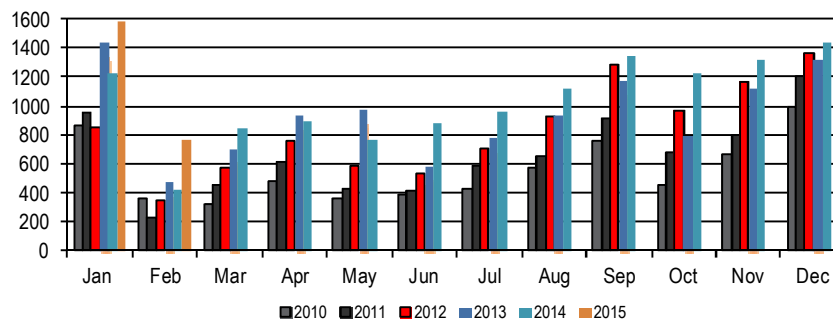
Overall, strong Jan and Feb domestic unit sales and better than expected ASP plus should be a positive for sentiment in Skyworth's TV business.

Table 1: Detailed Statistics for Feb 2015

Unit sales (000)	14-Aug	14-Sep	14-Oct	14-Nov	14-Dec	15-Jan	16-Feb
Domestic							
Flat TV	838	1,001	713	912	1,103	1,284	514
Y/Y domestic LCD	8%	8%	10%	3%	9%	39%	78%
M/M total gth	26%	19%	-29%	28%	21%	16%	-60%
Y/Y flat panel	8%	8%	10%	3%	9%	39%	78%
Domestic ASP change	-17%	-11%	-20%	-11%	-8%	-7%	2%
Cloud	274	338	238	261	384	477	215
4K	112	148	95	130	197	257	47
4K + Cloud	386	486	333	391	580	733	262
3D + Cloud / Total	46%	49%	47%	43%	53%	57%	51%
Exports	287	344	513	411	333	299	244
Total Flat TV	1,125	1,345	1,226	1,323	1,436	1,583	758
Flat TV (Y/Y growth)	20%	15%	53%	18%	9%	29%	80%

Source: Company reports

Figure 1: Total TV Unit Sales



Source: Company reports

Buy on weakness due to industry jitters

We highlight some significant recent developments to reiterate our call that Skyworth is our top SMID-Cap pick. Firstly, we see Skyworth taking market share in the rural market from peers (especially TCLM) as it has a strong line-up of higher end TVs and the best high end brand in lower tier cities. The remarkable sales growth in Jan and Feb of this year of nearly 50% Y/Y (in aggregate) is much better than the industry on fast rural demand growth. Our positive view on Skyworth's TV operations is reinforced after our finds from meetings this week with TCLM during their post results road show

Strong Feb sales and rising ASP. We had expected Feb sales to be weaker than the previous year due to the fact that CNY occurred in Jan 2014 and in Feb 2015 meaning that there were more days in Feb 2014 that was not impacted by down days before and after the holidays. However, Skyworth still achieved 78% sales growth on the back of strong shipments before the holidays and quite robust orders after CNY as well. In addition the small 2% increase in ASP in February was a pleasant surprise as we had expected a drop of mid single digits. Our conversations with management is that the new high end models are selling well in Jan and Feb. These high end models tend to have GPM in the low 30s rather than high teens for average TVs.

We see upside to the industry and to Skyworth from any additional details regarding the upcoming TV and appliance energy savings subsidies (we expect a detailed announcement in March), which stipulates the start date as well as the overall budget. Currently, the subsidy reported by local press amounted to only approx. Rmb2.5bn for the 2015 subsidy for TVs, but we see risk that the budget can be considerably higher.

The non-TV business supports further upside, in our view. Our new sum of the parts valuation of HK\$12.0 shows that the TV business is currently valued at less than zero (actually at negative HK\$4 per share) at the current share price. This valuation does not factor in upside from the new air conditioning business or e-commerce fulfillment businesses, which can be substantial. Additionally, Skyworth is earning internet advertising and content revenue from its smart TVs and we see the large active subscriber base has the potential to be the largest and most valuable part of Skyworth longer term (but again valued at zero in our current SOTP).

Revising up SOTP value to HK\$12.0

In this section we calculate the value of Skyworth using sum of the parts methodology, which is updated from HK\$9.0 to HK\$12.0 per share or about 46% higher than the DCF based valuation where we look at the company as a whole, to reflect some recent changes in news and methodology. Firstly, the A-share set top box subsidiary, Skyworth Digital (000810 CH) has seen its share price increase by about 36% in the past month (Shenzhen Composite up 8% over this period) and we include the share price in our SOTP valuation (with a 20% discount). Secondly, we are moving the base earnings for the appliance business from FY14 to FY16 when determining the PE based valuation. We believe that this is more appropriate time period and also the new timeframe captures some of the contribution of the new air conditioning and air purification sales (not in 2014 estimates). Thirdly we have lifted

the PE multiple assumed for the TV business from 6x to 8x FY16PE which we believe is appropriate given the recent improvements in operations

Table 2: Estimation of Sum of the parts Value

	HK\$m	% NAV	Methodology
Cash	3,023		
Pledged deposits	1,572		
Investments	691		
Long term debt	(547)		
Short term debt	(5,156)		
Bills Receivables	10,061		
Bills Payables	(4,094)		
Cash receipt for land	1,470		Cash receipt net of taxes
Total monetary items	7,020	20%	Book value
Skyworth Digital technologies	8,136	23%	20% discount to shr price 15x FY16E PE multiple with
White goods	4877	14%	20% discount
Office buildings	5429	16%	Rmb 25k psm - 178k sm area
LCD JV	1404	4%	Book value with 20% discount
TV / modules / others	7,964	23%	8x PE multiple
Total SOTP value	34,828		
Shares	2,847		
Per share	12.0		

Source: Company reports

The key issues / assumptions that impact on the SOTP valuation are as follows:

- **Treatment of bills receivables / payables.** We have assumed that the net bills receivables less payables are monetary (near cash) items and have included these in the SOTP at book value. Essentially bills receivables are payments by customers for goods that have been delivered and guaranteed by major banks. Payment typically is made in cash in 3 to 6 months. As a check, we made sure that net working capital (excluding bills receivables and payables) is positive (receivables + inventories > payables) .
- **Head office buildings.** Skyworth has two large office buildings in Shenzhen (Nanshan Tech Park) which generate significant rental income. The new building is a 124,000 sm grade A office building that has recently generated rental income. The older building is 54,000 sm and has been generating some minor rental income for a number of years. We have assumed an average of Rmb25,000 psm which is the market price for comparable buildings in the area.
- **Multiples for non TV business.** We have assumed a 20% discount to the stake (290m shares) in A-share listed Skyworth Digital, which is a set top box maker that was spun off in ct 2014. The shares trade on the domestic A-share market with a current price of Rmb20.18. We have also assumed a 15x P/E for the white goods (mostly refrigerators) business, similar to HK listed peers.
- **Multiple for TV/Modules business.**– We use the TV and module assembly business for multiples, as historically these have been the core business, which are currently under a great deal of pressure (esp. the TV operations). We have

assumed a 8x PE multiple, which is a 23% discount to what Skyworth is currently trading at, and at the low end of PE multiples for industrial SMID-Caps.

- **Cash to be received for property already sold.** In Oct 2013, a piece of land was sold in Shenzhen for a total consideration of HK\$2.1bn. The cash is scheduled to be received in FY15. We have included the cash receipt less any applicable taxes in the SOTP calculation. We understand that the company has other factories and plants that may be closed and sold for other uses (and presumably at a gain) but we have not included the value of these properties in this calculation.
- **Some upside to value that we don't factor in.** We have not factored in any SOTP value regarding the new air conditioning business, the new third party logistics business or any excess in market value for rental properties over the current book value in the accounts, leaving room for further upside.

Net profits revised up by 0.6% for FY15E and 8% for FY16E

Table 3: Earnings changes

(HK\$m)	----- New -----		----- Old -----		----- Change -----	
Year to Mar	FY15E	FY16E	FY15E	FY16E	FY15E	FY16E
Turnover	41,642	48,088	41,156	46,933	1.2%	2.5%
Gross profit	8,076	9,454	7,982	9,215	1.2%	2.6%
EBIT	2,207	2,783	2,187	2,600	0.9%	7.0%
Net profit	2,615	2,052	2,600	1,901	0.6%	7.9%
EPS (HKD)	0.91	0.70	0.90	0.65	0.6%	7.9%
Assumptions						
Gross margin	19.4%	19.7%	19.4%	19.6%	0.0%	0.0%

Source: J.P. Morgan estimates

We are lifting our FY15E and FY16E sales by 1.2% and 2.5%, respectively, to reflect the stronger than expected sales and ASP for February. The remarkable sales growth in Jan and Feb of this year of nearly 50% Y/Y (in aggregate) is much better than the industry on fast rural demand growth. ASP in Feb14 increased by 2%Y/Y, first increase in a year. We are lifting our FY15E and FY16E net profit by 0.6% and 7.9%, respectively, to reflect the higher sales.

Our DCF-based Dec-14 share price target is lifted to HK\$8.2 (previously HK\$7.0) due to the earnings revisions.

Valuation and share price analysis

DCF valuation

Our Dec-15 price target is based on a DCF valuation that assumes a market risk premium of 6.0% and a risk-free rate of 4.2% (yield on 10-year government notes in China). We assume a beta of 1.3. Our Beta is 1.3, and accordingly, we assume a WACC of 12.0%. We estimate free cash flow for Skyworth until 2020 and assume a terminal growth rate of 3.0%. The terminal growth is based on the annual growth rate expected in 2015 (the final year of the estimate period) subject to a minimum of 3% and a maximum of 6%, depending on the nature of the industry and the level of maturity in China.

Table 4: Base-case DCF analysis

HK\$ mn	2013	2014E	2015E	2016E	2017E	2018E	2019E	Terminal
Cash flow estimates								
Sales	37,824	39,480	41,642	48,088	56,193	65,578	73,608	83,105
EBIT	2,069	1,883	2,207	2,783	2,960	3,400	3,733	4,129
NOPAT	1,613	1,459	1,766	2,285	2,441	2,802	3,074	3,398
Capex, net	(950)	(2,079)	(1,948)	(1,772)	(1,867)	(1,359)	(1,400)	(930)
Depreciation	297	453	581	674	796	881	932	955
Change in working capital	(2,449)	1,896	862	(1,270)	(1,748)	(2,000)	(1,478)	(410)
Free CF (excl. non-core)	(1,489)	1,729	1,261	(82)	(377)	326	1,131	3,017
DCF Parameters								
Liabilities as a % of EV	0%	Assumptions						
WACC	12.0%	Terminal growth			3.0%			
		Risk-free rate			4.2%			
		Market risk			6.0%			
Enterprise NPV (10-16E)	19,027	Beta			1.30			
+ Net cash (debt), current	(961)	Cost of debt			6.2%			
- Minorities (Market value)	(641)							
+/- Other items	5,967	Implied exit P/E multiple (x)			11x			
= Equity value	23,392							
/ Number of shares (m)	2,847							
= Equity value per share (HK\$)	8.2							

Source Company data, J.P. Morgan estimates.

We also analyze the DCF price sensitivity to WACC, and the terminal multiple.

Table 5: Sensitivity analysis based on WACC and perpetual terminal growth rate

		Terminal growth rate						
		1.5%	2.0%	2.5%	3.0%	3.5%	4.0%	4.5%
WACC	10.5%	9.2	9.5	9.8	10.1	10.5	10.9	11.5
	11.0%	8.6	8.8	9.1	9.4	9.7	10.1	10.5
	11.5%	8.1	8.3	8.5	8.8	9	9.3	9.7
	12.0%	7.7	7.8	8	8.2	8.4	8.7	9
	12.5%	7.3	7.4	7.6	7.7	7.9	8.1	8.4
	13.0%	6.9	7	7.1	7.3	7.5	7.6	7.8
	13.5%	6.6	6.7	6.8	6.9	7	7.2	7.4

Source: J.P. Morgan estimates

Table 6: SD – Revenue mix

HK\$ mn, year-end March	2013	2014	2015E
LCD	5,481	-	-
YoY	-34.2%	-100.0%	#DIV/0!
% of total	14.5%	0.0%	0.0%
CRT	218	85	-
YoY	-62.9%	-61.0%	-100.0%
% of total	0.6%	0.2%	0.0%
LED	24,555	29,205	29,132
YoY	63.4%	18.9%	-0.2%
% of total	64.9%	74.0%	70.0%
Set top box	3,906	4,162	4,523
YoY	19.4%	6.6%	8.7%
% of total	10.3%	10.5%	10.9%
Others	1691	2532	3748.5
YoY	#DIV/0!	49.7%	48.0%
% of total	4.5%	6.4%	9.0%
Total	37,824	39,480	41,642
YoY	34.4%	4.4%	5.5%

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

Table 7: SD – P&L statement

HK\$ mn, year-end March	2012	2013	2014	2015E	2016E
Total Revenues	28,137	37,824	39,480	41,642	48,088
YoY change (%)	15.6%	34.4%	4.4%	5.5%	15.5%
Cost of Goods Sold	(22,181)	(30,418)	(31,851)	(33,566)	(38,634)
YoY change (%)	12.7%	37.1%	4.7%	5.4%	15.1%
Gross Profit	5,956	7,406	7,629	8,076	9,454
YoY change (%)	27.7%	24.3%	3.0%	5.9%	17.1%
Gross Margin	21.2%	19.6%	19.3%	19.4%	19.7%
SGA	(4,765)	(5,942)	(6,570)	(6,868)	(7,748)
YoY change (%)	31.4%	24.7%	10.6%	4.5%	12.8%
Other Income/(Expenses)	444	605	824	1,000	1,077
Operating profit	1,635	2,069	1,883	2,207	2,783
EBITDA	1,879	2,366	2,336	2,788	3,457
EBITDA margin	6.7%	6.3%	5.9%	6.7%	7.2%
Depreciation & Amortization	(245)	(297)	(453)	(581)	(674)
YoY change (%)	22.5%	21.3%	52.5%	28.4%	16.1%
EBIT	1,723	2,069	1,883	2,207	2,783
EBIT margin	6.1%	5.5%	4.8%	5.3%	5.8%
Net Interest Expense	(177)	(133)	(163)	(162)	(162)
Exceptional item	0	0	0	1,060	0
Associates	30	(10)	(20)	0	42
Gains/losses	0	0	0	0	0
Net Income Before Taxes	1,576	1,926	1,700	3,105	2,662
YoY change (%)	11.2%	22.2%	-11.7%	82.6%	-14.3%
Tax	(308)	(332)	(267)	(301)	(391)
Effective Tax rate	19.5%	17.2%	15.7%	14.7%	14.7%
Minority Interests	(16)	(93)	(179)	(189)	(218)
Net Income	1,252	1,501	1,254	2,615	2,052
YoY change (%)	14.1%	19.9%	-16.5%	108.5%	-21.5%
Net margin	4.3%	4.0%	3.2%	6.3%	4.2%

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

Table 8: Interim estimates

HK\$ mn, year-end March	1H13	2H13	1H14	2H14	1H15	2H15E
Total Revenues	16,389	21,435	20,022	19,458	18,478	23,164
Gross Profit	3,301	4,105	3,833	3,796	3,612	4,464
EBIT	844	1,225	1,056	827	1,184	1,023
Net Income Before Taxes	774	1,152	973	727	1,099	2,006
Net Income	618	883	719	535	824	1,791
Diluted EPS (HK\$)	0.224	0.32	0.256	0.19	0.291	0.62
Ratios						
Revenue split	43.3%	56.7%	50.7%	49.3%	44.4%	55.6%
GPM	20.1%	19.2%	19.1%	19.5%	19.5%	19.3%
EBIT margin	5.1%	5.7%	5.3%	4.3%	6.4%	4.4%
NPM	3.8%	4.1%	3.6%	2.7%	4.5%	7.7%
YoY						
Revenue	25.4%	42.3%	22.2%	-9.2%	-7.7%	19.0%
GP	19.1%	28.9%	16.1%	-7.5%	-5.8%	17.6%
EBIT	22.7%	18.4%	25.1%	-32.5%	12.1%	23.7%
NP	34.1%	11.6%	16.3%	-39.4%	14.6%	234.8%

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

Table 9: SD – Balance sheet

HK\$ mn, year-end March	2012	2013	2014	2015E	2016E
Cash and Cash Equivalents	2,164	2,301	3,023	4,742	4,047
Inventories	3,151	5,109	4,188	4,417	5,101
Accounts receivable	11,623	15,986	15,848	16,716	19,303
Other Current Assets	2,002	1,237	3,121	3,566	3,895
Total Current Assets	18,940	24,633	26,180	29,441	32,346
Intangible Assets	0	0	0	0	0
Property and Equipment, Net	2,328	3,192	4,436	5,392	6,477
Other Assets	956	1,238	1,528	468	476
Non-Current assets	3,284	4,430	5,964	5,860	6,954
Total Assets	22,224	29,063	32,144	35,301	39,299
Accounts Payable	7,107	9,586	9,241	9,747	11,256
Other Accrued Expenses	1,248	2,321	4,979	5,409	6,022
Taxes Payable	198	190	125	159	249
ST and current LT debts	3,568	5,581	5,156	5,156	5,156
Total Current Liabilities	12,121	17,678	19,501	20,471	22,683
Long-term Debt	715	225	547	547	547
Other Noncurrent Liability	720	924	748	748	748
Noncurrent liabilities	1,435	1,149	1,295	1,295	1,295
Total Liabilities	13,556	18,827	20,796	21,766	23,978
Share capital	269	280	283	283	283
Reserves and Surplus	8,200	9,689	10,539	12,537	14,105
Total Shareholders' Equity	8,469	9,969	10,822	12,820	14,388
Minority Interest	199	267	526	715	933
Total Shareholders' Equity	8,668	10,236	11,348	13,535	15,321
Total Liabilities and Equity	22,224	29,063	32,144	35,301	39,299

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

Table 10: SD – Cash flow statement

HK\$ mn, year-end March	2012	2013	2014	2015E	2016E
EBIT	1,723	2,069	1,883	2,207	2,783
Depreciation and Amortization	245	297	453	581	674
Working Capital Changes	(348)	(2,449)	1,896	862	(1,270)
Tax Paid	(244)	(308)	(332)	(267)	(301)
Cash Flow From Operations	1,376	(524)	3,737	3,221	1,724
Capital expenditures	(720)	(950)	(2,079)	(1,948)	(1,772)
Investments and others	(408)	286	(390)	966	(97)
Net Interest	(177)	(133)	(163)	(162)	(162)
Cash Flow from Investing	(1,305)	(328)	(2,858)	(17)	(1,965)
Free Cash Flow	71	(1,137)	1,268	2,238	(145)
Dividends	(199)	(177)	(443)	(519)	(551)
Common issue	0	0	0	0	0
Debt	(322)	1,727	(103)	0	0
Other Financing	0	(309)	0	0	0
Cash Flow from financing	(521)	1,241	(546)	(519)	(551)
Change in cash	(450)	104	722	1,719	(695)
Cash beginning	2,524	2,164	2,301	3,023	4,742
Foreign exchange changes	90	33	0	0	0
Cash at end	2,164	2,301	3,023	4,742	4,047

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

Investment Thesis, Valuation and Risks

Skyworth Digital Holdings *(Overweight; Price Target: HK\$8.20)*

Investment Thesis

Skyworth is China's largest flat-panel TV brand by unit sales and is a leader in the fast-growing rural market. We believe that the flat panel TV market in China is entering a favourable period of growth and margin expansion due to the migration of 3D TVs into the mass market. There may be lower marketing expenses as a proportion of sales revenues as the company improves its distribution network with newly introduced specialty stores. We see Skyworth taking market share in the rural market from peers (especially TCLM) as Skyworth has a strong line-up of higher end TVs and the best high end brand in lower tier cities.

Valuation

Our Dec-15 price target is based on a DCF valuation that assumes a market risk premium of 6.0% and a risk-free rate of 4.2% (yield on ten-year government notes in China). We assume a beta of 1.3, and accordingly, we assume a WACC of 12.0%.

Risks to Rating and Price Target

Key risks to our rating and price target include the higher cost of components and higher-than-expected selling expenses that could cut into margins.

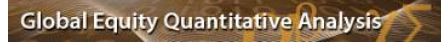
Skyworth Digital Holdings: Summary of Financials

Income Statement						Cash flow statement					
HK\$ in millions, year end Mar	FY13	FY14	FY15E	FY16E	FY17E	HK\$ in millions, year end Mar	FY13	FY14	FY15E	FY16E	FY17E
Revenues	37,824	39,480	41,642	48,088	56,193	EBIT	2,069	1,883	2,207	2,783	2,960
% change Y/Y	34.4%	4.4%	5.5%	15.5%	16.9%	Depr. & amortization	297	453	581	674	796
Gross Profit	7,406	7,629	8,076	9,454	10,846	Change in working capital	(2,449)	1,896	862	(1,270)	(1,748)
% change Y/Y	24.3%	3.0%	5.9%	17.1%	14.7%	Taxes	(308)	(332)	(267)	(301)	(391)
EBITDA	2,366	2,336	2,788	3,457	3,756	Cash flow from operations	(391)	3,900	3,383	1,886	1,617
% change Y/Y	25.9%	(1.3%)	19.4%	24.0%	8.7%	Capex	(613)	(2,079)	(1,948)	(1,772)	(1,867)
EBIT	2,069	1,883	2,207	2,783	2,960	Net Interest	(133)	(163)	(162)	(162)	(162)
% change Y/Y	26.6%	(9.0%)	17.2%	26.1%	6.4%	Other	0	(100)	(94)	(88)	(84)
EBIT Margin	5.5%	4.8%	5.3%	5.8%	5.3%	Free cash flow	(894)	1,668	2,634	245	(129)
Net Interest	(133)	(163)	(162)	(162)	(162)	Equity raised/(repaid)	0	0	0	0	0
Earnings before tax	1,926	1,700	3,105	2,662	2,884	Debt raised/(repaid)	1,727	(103)	0	0	0
% change Y/Y	22.2%	(11.7%)	82.6%	(14.3%)	8.4%	Other	(309)	0	0	0	0
Tax	(332)	(267)	(301)	(391)	(424)	Dividends paid	(177)	(443)	(519)	(551)	(502)
as % of EBT	17.2%	15.7%	9.7%	14.7%	14.7%	Beginning cash	2,164	2,301	3,023	4,742	4,047
Net income (reported)	1,501	1,254	2,615	2,052	2,206	Ending cash	2,301	3,023	4,742	4,047	3,031
% change Y/Y	19.9%	(16.5%)	108.5%	(21.5%)	7.5%	DPS	0.17	0.15	0.22	0.17	0.17
Shares outstanding	2,761	2,813	2,878	2,935	2,994						
EPS (reported)	0.54	0.45	0.91	0.70	0.74						
% change Y/Y	17.4%	(18.0%)	103.8%	(23.0%)	5.4%						
Balance sheet						Ratio Analysis					
HK\$ in millions, year end Mar	FY13	FY14	FY15E	FY16E	FY17E	HK\$ in millions, year end Mar	FY13	FY14	FY15E	FY16E	FY17E
Cash and cash equivalents	2,301	3,023	4,742	4,047	3,031	Gross margin	19.6%	19.3%	19.4%	19.7%	19.3%
Accounts receivable	15,986	15,848	16,716	19,303	22,557	EBITDA margin	6.3%	5.9%	6.7%	7.2%	6.7%
Inventories	5,109	4,188	4,417	5,101	5,961	Operating margin	5.5%	4.8%	5.3%	5.8%	5.3%
Others	1,237	3,121	3,566	3,895	4,294	Net margin	4.0%	3.2%	3.7%	4.3%	3.9%
Current assets	24,633	26,180	29,441	32,346	35,843	Sales per share growth	31.7%	2.4%	3.1%	13.2%	14.6%
LT investments	1,238	1,528	468	476	494	Sales growth	34.4%	4.4%	5.5%	15.5%	16.9%
Net fixed assets	3,192	4,436	5,392	6,477	7,534	Net profit growth	19.9%	(16.5%)	108.5%	(21.5%)	7.5%
Total Assets	29,063	32,144	35,301	39,299	43,870	EPS growth	17.4%	(18.0%)	103.8%	(23.0%)	5.4%
Liabilities						Interest coverage (x)	17.8	14.3	17.2	21.3	23.1
Short-term loans	5,581	5,156	5,156	5,156	5,156	Net debt to equity	34.2%	23.6%	7.1%	10.8%	15.5%
Payables	9,586	9,241	9,747	11,256	13,153	Working Capital to Sales	0.2	0.2	0.2	0.2	0.2
Others	2,511	5,104	5,568	6,271	7,005	Sales/assets	1.5	1.3	1.2	1.3	1.4
Total current liabilities	17,678	19,501	20,471	22,683	25,314	Assets/equity	2.8	2.9	2.9	2.7	2.7
Long-term debt	225	547	547	547	547	ROE	16.3%	12.1%	13.2%	15.1%	14.5%
Other liabilities	924	748	748	748	748	ROCE	12.0%	9.8%	10.7%	12.3%	12.1%
Total Liabilities	18,827	20,796	21,766	23,978	26,609						
Shareholders' equity	10,236	11,348	13,535	15,321	17,261						
BVPS	3.56	3.82	4.44	4.89	5.35						

Source: Company reports and J.P. Morgan estimates.

JPM Q-Profile

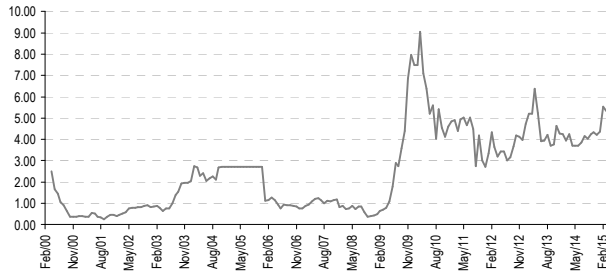
Skyworth Digital Holdings Limited (HONG KONG / Consumer Discretionary)
 As Of: 04-Mar-2015



Quant_Strategy@jpmorgan.com

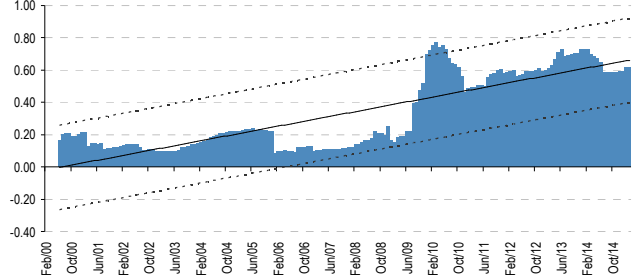
Local Share Price

Current: **5.34**



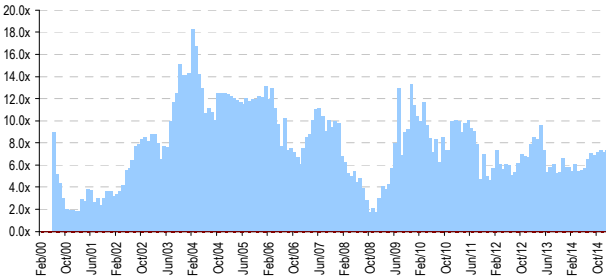
12 Mth Forward EPS

Current: **0.62**



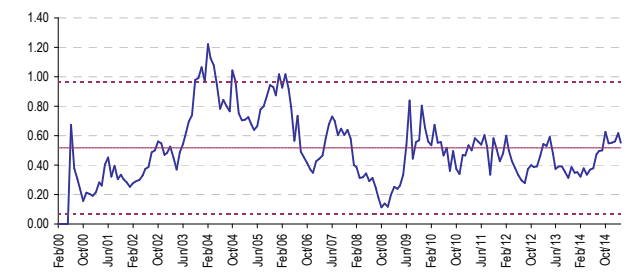
PE (1Yr Forward)

Current: **8.7x**



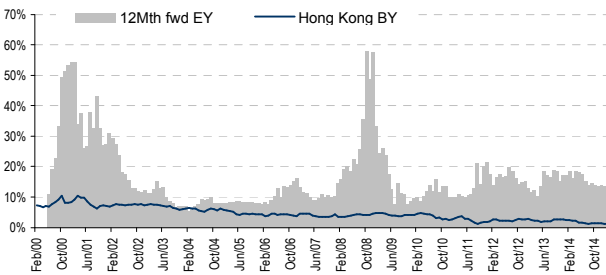
P/E Relative to Hong Kong Index

Current: **0.55**



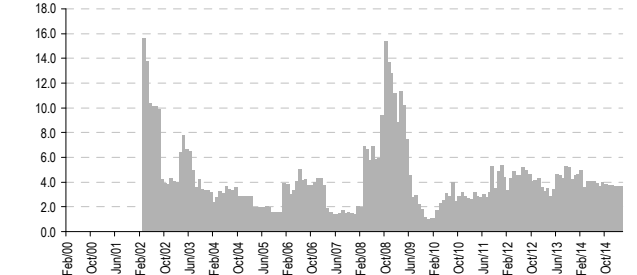
Earnings Yield (& Local Bond Yield)

Current: **12%**



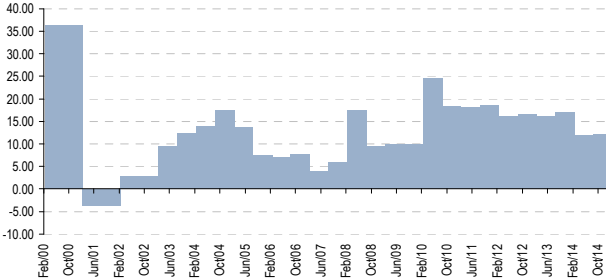
Dividend Yield (Trailing)

Current: **3.65**



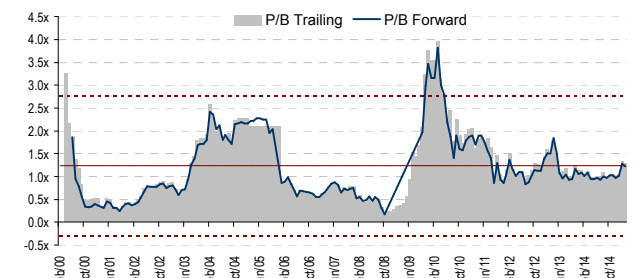
ROE (Trailing)

Current: **12.19**



Price/Book (Value)

Current: **1.3x**



Summary

Skyworth Digital Holdings Limited		HONG KONG		TICKER 751 HK		As Of: 4-Mar-15					
Consumer Discretionary						Local Price: 5.34					
						EPS: 0.62					
12mth Forward PE	Latest 8.67x	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
P/BV (Trailing)	1.28	0.20	3.96	1.02	1.24	2.77	-0.28	-84%	210%	-20%	-3%
Dividend Yield (Trailing)	3.65x	0.00	15.69	3.46	3.73	9.60	-2.14	-100%	330%	-5%	2%
ROE (Trailing)	12.19	-3.68	36.45	12.19	12.94	31.00	-5.12	-130%	199%	0%	6%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, JPMorgan Quantitative & Derivative Strategy

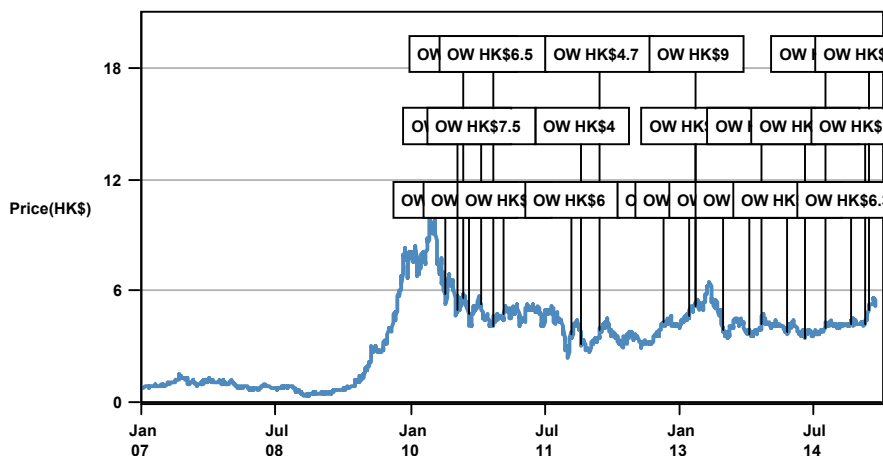
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Skyworth Digital Holdings (0751.HK, 751 HK) Price Chart



Date	Rating	Share Price (HK\$)	Price Target (HK\$)
19-May-10	OW	5.78	10.00
06-Jul-10	OW	4.92	8.40
03-Aug-10	OW	5.61	9.20
27-Aug-10	OW	4.69	8.00
13-Oct-10	OW	5.28	7.50
01-Dec-10	OW	4.10	6.50
17-Jan-11	OW	4.70	7.00
18-Oct-11	OW	3.68	6.00
25-Nov-11	OW	3.17	4.00
09-Feb-12	OW	3.86	4.70
24-Oct-12	OW	4.26	6.00
07-Feb-13	OW	4.60	6.70
04-Mar-13	OW	5.16	7.90
08-Mar-13	OW	5.33	9.00
27-Jun-13	OW	3.89	7.50
11-Oct-13	OW	3.69	6.70
26-Nov-13	OW	4.19	6.80
11-Mar-14	OW	3.80	5.60
23-May-14	OW	3.49	4.70
15-Aug-14	OW	4.00	5.60
25-Nov-14	OW	4.23	6.30
26-Jan-15	OW	4.23	6.50
09-Feb-15	OW	4.97	7.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage May 19, 2010.

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IB clients*	56%	49%	33%
JPMS Equity Research Coverage	45%	48%	7%
IB clients*	75%	67%	52%

*Percentage of investment banking clients in each rating category.

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