

Company Report

China Merchants Securities (HK)
Hong Kong Equity Research

AAC Technologies (2018 HK)

4Q14 miss on lower GPM; Mixed outlook in FY15E

- 4Q14 NP 15%/12% below our/consensus estimates; weaker GPM due to wage hike and ASP decline in acoustics business
- FY15E Outlook: more ASP/margin pressure in slowing acoustics; limited near-term visibility in mass adoption of haptics solutions
- Trimmed FY15-16E EPS by 9-11%; maintain NEUTRAL on mixed outlook and rich valuation of 16.4x FY15E P/E

4Q14 miss on both revenue and margins

AAC Tech reported 4Q14 net profit of RMB788mn (+31% YoY), below our/consensus estimates by 15%/12%; while 4Q14 revenue came in at RMB 3,340mn (+42% YoY; +50% QoQ), below our/consensus estimates by 7%/1%. We believe NP miss is due to weaker acoustic sales (-8% YoY) and lower GPM (-3ppt YoY), despite impressive non-acoustics (+100% YoY, 35% of 4Q sales; GPM 48%+). Mgmt stated 4Q14 GPM was impacted by higher labor costs and lower ASP of acoustics products.

FY15E: flattish GPM, weaker acoustics on pricing, more non-acoustics (30%+ sales mix)

Mgmt guided 1Q15E revenue decline 20% QoQ with margin similar to 4Q14. For long term, mgmt believes acoustics TAM for AAC is RMB9-10bn and expects YoY sales growth for acoustics in FY15E driven by higher speak-box adoption from Chinese customers (120-150 models in FY14) and Samsung's flagship models, while non-acoustics (haptics/RF), is guided to contribute 30% of FY15E sales (vs 22% in FY14). For FY15E, we remain conservative given slowing core acoustics segment with continued margin pressure, despite lower production cost in Vietnam plant and increasing mix from higher-margin non-acoustics.

Valuation/ Risks

We lower our FY15-16E EPS by 9-11% to reflect 4Q weakness, lower GPM, which offsets higher contribution from non-acoustics. Trading at 16.4x FY15E P/E, we maintain NEUTRAL rating with revised TP of HK\$44.2 based on 15x FY15E P/E (3-year hist. avg.), given low visibility of margins and new product ramp-up in FY15-16E. Upside risks include stronger iPhone6 demand and higher non-acoustics sales.

Financials

RMB mn	2013	2014E	2015E	2016E	2017E
Revenue	8,096	8,879	10,988	12,746	14,658
Growth	28.9%	9.7%	23.8%	16.0%	15.0%
Net profit	2,578	2,318	2,892	3,336	3,826
Growth	46.2%	-10.1%	24.8%	15.3%	14.7%
EPS (RMB)	2.10	1.89	2.36	2.72	3.12
DPS (RMB)	0.60	0.86	1.07	1.03	1.25
P/E (x)	18.4	20.4	16.4	14.2	12.4
P/B (x)	6.0	5.2	4.3	3.6	3.0
ROE	32.5%	25.2%	26.2%	25.6%	24.6%

Source: Company data, CMS (HK) estimates

Alex Ng
852-31896125
nglh@cmschina.com.hk

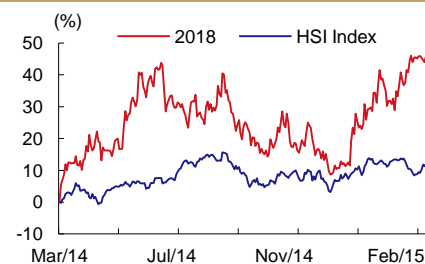
WHAT'S NEW

EPS and TP downgraded

NEUTRAL

Previous	NEUTRAL
Price	HK\$48.2
12-month Target Price (Potential upside/downside)	HK\$44.2 (-8%)
Previous	HK\$48.2

Price Performance



Source: Bigdata

%	1m	6m	12m
2018 HK	7.7	22.2	74.7
HSI	(1.4)	2.0	11.7

Industry: Hardware Technology

Hang Seng Index	24,528
HSCEI	11,969

Key Data

52-week range (HK\$)	34.9-54.85
Market cap (HK\$ mn)	59,251
Avg. daily volume ('000)	275.63
BVPS (HK\$)	6.46

Shareholdings Structure

Wu ChunYuan	21.40%
Capital Group	16.00%
ZhengMin Pan	18.93%
No. of shares outstanding (mn)	1228.0
Free float	18.20%

Related Research

1. AAC Tech (2018 HK) – 3Q14 below but impressive transition into non-acoustics - 10 Nov 14

Earnings revisions

Figure 1: Revenue assumptions

RMB mn	1Q14	2Q14	3Q14	4Q14	FY14	1Q15E	2Q15E	3Q15E	4Q15E	FY15E
Revenue										
Dynamic components	1,557	1,387	1,301	1,722	5,967	1,275	1,211	1,150	1,472	5,108
... YoY	-17%	-11%	-6%	32%		-26%	-5%	-5%	28%	
MEMS components	185	194	186	287	852	216	226	219	307	969
... YoY	-23%	4%	-4%	55%		-25%	5%	-3%	40%	
Non-acoustics	60	130	537	1,076	1,804	990	1,139	1,276	1,467	4,872
... YoY	N/A	116%	312%	101%		-8%	15%	12%	15%	
Other products	111	93	41	10	256	9	9	10	11	40
... YoY	27%	-16%	-56%	-76%		-15%	10%	10%	10%	
Revenue mix										
Dynamic components	84%	78%	63%	56%	67%	51%	47%	43%	45%	46%
MEMS components	10%	10%	9%	9%	10%	9%	9%	8%	9%	9%
Non-acoustics	3%	7%	26%	35%	20%	40%	44%	48%	45%	44%
Other products	3%	5%	2%	0%	3%	0%	0%	0%	0%	0%
Gross profit margin	40.2%	42.1%	42.3%	41.1%	41.4%	41.4%	42.1%	41.3%	40.7%	41.3%
Dynamic components	N/A	N/A	N/A	N/A	43.9%	42.5%	43.0%	42.0%	42.2%	42.4%
MEMS components	N/A	N/A	N/A	N/A	24.2%	24.0%	23.5%	23.5%	23.8%	23.7%
Non-acoustics	N/A	N/A	N/A	N/A	45.7%	44.0%	45.0%	44.0%	43.0%	43.9%
Other products	N/A	N/A	N/A	N/A	12.1%	11.0%	12.0%	12.0%	12.0%	11.8%

Source: Company, CMS (HK)

Figure 2: Earnings revisions

(RMB mn)	New		Old		Diff (%)	
	2015E	2016E	2015E	2016E	2015E	2016E
Revenue	10,988	12,746	11,846	13,979	-7%	-9%
Gross profit	4,541	5,264	5,047	5,969	-10%	-12%
Operating profit	3,098	3,556	3,400	4,012	-9%	-11%
Net profit	2,892	3,336	3,192	3,769	-9%	-11%
EPS (RMB)	2.36	2.72	2.60	3.07	-9%	-11%
Gross margin	41.3%	41.3%	42.6%	42.7%		
Operating margin	28.2%	27.9%	28.7%	28.7%		
Net Margin	26.3%	26.2%	26.9%	27.0%		

Source: CMS (HK), Bloomberg

Figure 3: CMS estimates vs Consensus

(RMB mn)	CMS (HK)			Consensus		Diff (%)	
	2015E	2016E	2017E	2015E	2016E	2015E	2016E
Revenue	10,988	12,746	14,658	11,092	12,718	-0.9%	0.2%
Gross profit	4,541	5,264	6,069	4,647	5,321	-2.3%	-1.1%
Operating profit	3,098	3,556	4,090	3,290	3,729	-5.8%	-4.6%
Net profit	2,892	3,336	3,826	3,040	3,497	-4.9%	-4.6%
EPS (RMB)	2.36	2.72	3.12	2.48	2.84	-5.0%	-4.5%
Gross margin	41.3%	41.3%	41.4%	41.9%	41.8%		
Operating margin	28.2%	27.9%	27.9%	29.7%	29.3%		
Net Margin	26.3%	26.2%	26.1%	27.4%	27.5%		

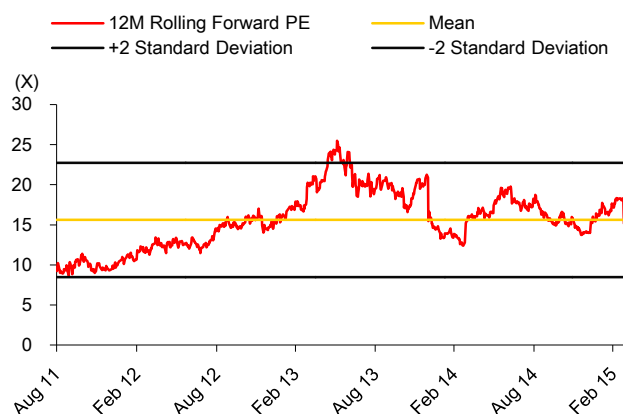
Source: Company, CMS (HK)

Valuation

Maintain NEUTRAL with revised TP of HK\$44.2 (9% downside)

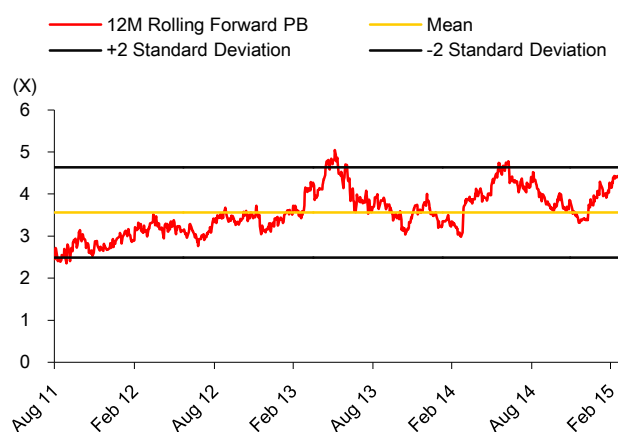
We revised our FY15-16E EPS estimates by 9-11% to reflect 4Q results, lower GPM but higher sales contribution from non-acoustics. We revised down our TP to HK\$44.2 based on 15x FY15E P/E (3-year historical average), and maintain our NEUTRAL rating given limited near-term visibility in margin and non-acoustics adoption. Upside risks include stronger iPhone6 demand and higher non-acoustics sales.

Figure 4: Forward P/E band



Source: Company, CMS (HK)

Figure 5: Forward P/B band



Source: Company, CMS (HK)

Peers Comparison

Figure 6: Sector valuation comparison

Company	Ticker	Rating	Mkt Cap (USD mn)	Current Price (HKD)	Target Price (HKD)	Upside (%)	P/E (x)		P/B (x)		ROE (%)	
							FY15E	FY16E	FY15E	FY16E	FY15E	FY16E
AAC Tech	2018 HK	Neutral	7,637	48.20	44.16	-8%	16.4	14.2	4.3	3.6	26%	26%
Sunny Optical	2382 HK	Neutral	2,050	14.48	16.21	12%	15.0	12.2	3.2	2.7	21%	21%
Truly Intl	732 HK	Buy	1,425	3.80	4.41	16%	7.8	6.5	1.3	1.1	16%	17%
BYD E	285 HK	N/A	2,582	8.88	N/A	N/A	10.8	8.9	1.4	1.3	14%	15%
FIH	2038 HK	N/A	4,121	4.10	N/A	N/A	17.6	15.5	1.0	0.9	6%	7%
Coolpad	2369 HK	Sell	782	1.41	1.05	-26%	11.8	10.8	1.6	1.4	13%	13%
TCL Comm	2618 HK	Buy	1,280	8.02	10.42	30%	6.9	6.1	1.7	1.5	27%	26%
ZTE	763 HK	N/A	11,455	17.28	N/A	N/A	14.1	12.5	1.7	1.5	13%	13%

Source: Company, CMS (HK)

4Q14 Review: revenue/net profit missed due to weaker GPM

AAC Tech reported 4Q14 net profit of RMB788mn (+31%YoY), below our/consensus estimates by 15%/12%; while 4Q14 revenue came in at RMB 3,340 (+42% YoY; +50%QoQ), below our/consensus estimates by 7%/1%. We believe the miss is mainly due to weaker 4Q GPM of dynamic components despite impressive non-acoustics delivery (35% of 4Q sales, +100%YoY; GPM 48%+).

In terms of revenue breakdown by segment, dynamic components (56% of 4Q sales) declined 8%YoY, MEMS (9% of mix) up 20%YoY and non-acoustics (haptics/RF, 34% of mix) up 100%QoQ. We believe non-acoustics results are encouraging given 1) 4Q sales mix of 34% above guidance of 20%, and 2) GPM of 45.7% above company average (41.4%).

Figure 7: AAC's 4Q14 financial results

RMB mn	4Q13	1Q14	2Q14	3Q14	4Q14	CMS(HK)	Diff %	Consensus	Diff %
Revenue	2,182	1,854	1,862	2,064	3,099	3,340	-7%	3,145	-1%
Operating Profit	650	520	512	592	862	979	-12%	962	-10%
Net profit	604	487	493	550	788	927	-15%	899	-12%
EPS (RMB cents)	49.21	39.66	40.12	44.77	64.19	75.5	-15%	74.00	-13%
Margin (%)									
Gross Margin	42.8%	40.2%	42.1%	42.3%	41.1%	43.0%		42.4%	
Operating Margin	29.8%	28.0%	27.5%	28.7%	27.8%	29.3%		30.6%	
Net Margin	27.7%	26.3%	26.5%	26.6%	25.4%	27.8%		28.6%	
Growth (%)									
Revenue (YoY)	9.3%	-2.7%	-3.3%	-0.9%	42.0%	53.1%			
Revenue (QoQ)	4.7%	-15.0%	0.4%	10.9%	50.1%	38.0%			
Operating Profit	15.0%	-2.5%	-10.1%	-5.1%	32.7%	50.7%			
Net Profit	6.2%	-8.8%	-9.0%	-38.8%	30.5%	53.4%			

Source: Company, CMS (HK)

Financial Summary

Statement of financial position

RMB million	2013	2014	2015E	2016E	2017E
Current Assets	5,802	6,750	8,368	10,441	13,232
Cash & equivalents	2,354	1,603	2,805	4,630	6,372
Trading investments	0	0	0	0	0
Trade notes	0	0	0	0	0
Trade receivables	2,581	3,850	4,116	4,124	4,958
Other receivables	17	8	8	8	8
Inventories	832	1,267	1,418	1,657	1,873
Other current assets	19	22	22	22	22
Non-current assets	4,875	6,529	7,023	7,357	7,630
Investment property	0	0	0	0	0
PPE	3,969	5,285	5,779	6,113	6,387
Intangible assets	212	173	173	173	173
Other non-current assets	694	1,071	1,071	1,071	1,071
Total assets	10,677	13,279	15,391	17,798	20,863
Current Liabilities	2,679	4,001	4,283	4,677	5,196
Bank loans	905	1,418	1,418	1,418	1,418
Trade payables	1,617	2,388	2,635	3,001	3,488
Prepaid Accounts	0	0	0	0	0
Other liquid liabilities	154	195	229	258	290
Long term Liabilities	66	86	86	86	86
Loans	0	0	0	0	0
Others	52	75	75	75	75
Total Liabilities	2,745	4,088	4,369	4,763	5,283
Issued capital	100	100	100	100	100
Capital reserves	0	0	0	0	0
Reserves	7,776	9,038	10,878	12,901	15,459
NCI	56	54	44	34	22
Parents	7,876	9,138	10,978	13,000	15,558
Total equity and liabilities	10,677	13,279	15,391	17,798	20,863

Statement of cash flows

RMB million	2013	2014	2015E	2016E	2017E
CF from OA	2,548	902	3,269	4,052	3,924
Net profit	2,578	2,318	2,892	3,336	3,826
D&A	452	506	506	566	626
Finance costs	11	14	14	14	14
Investment income	(12)	0	0	0	0
Changes of WC	(258)	(906)	(169)	117	(561)
Others	(264)	(254)	(304)	(361)	(416)
CF from IA	(716)	(900)	(1,000)	(900)	(900)
Capital expenditure	(707)	(900)	(1,000)	(900)	(900)
Other investments	(9)	0	0	0	0
CF from FA	(775)	(754)	(1,066)	(1,327)	(1,281)
Borrowings	(21)	0	0	0	0
Share capital	0	0	0	0	0
Changes of reserves	0	0	0	0	0
Dividends	(740)	(740)	(1,052)	(1,313)	(1,268)
Others	(14)	(14)	(14)	(14)	(14)
Net cash flow	1,057	(752)	1,203	1,825	1,742

Source: Company, CMS(HK)

Statement of comprehensive income

RMB million	2013	2014	2015E	2016E	2017E
Revenues	8,096	8,879	10,988	12,746	14,658
Cost of sales	(4,637)	(5,201)	(6,447)	(7,482)	(8,590)
Selling exp	(182)	(199)	(242)	(293)	(352)
Admin exp	(349)	(338)	(406)	(459)	(528)
Op expenses	(1,083)	(1,193)	(1,444)	(1,708)	(1,979)
Op Profit	2,376	2,485	3,098	3,556	4,090
Financial costs	(11)	(14)	(14)	(14)	(14)
Impairments	0	0	0	0	0
FV changes	(0)	0	0	0	0
Inv income	12	(1)	(1)	(1)	(1)
Non-op inc	136	110	139	174	186
Non-op exp	0	0	0	0	0
PBT	2,835	2,581	3,221	3,715	4,261
Taxes	(263)	(270)	(338)	(390)	(447)
Net Profit	2,571	2,310	2,883	3,325	3,814
NCI	(6)	(7)	(9)	(10)	(12)
Parents	2,578	2,318	2,892	3,336	3,826
EPS (RMB)	2.10	1.89	2.36	2.72	3.12

Ratios

	2013	2014	2015E	2016E	2017E
YoY growth rate					
Revenue	28.9%	9.7%	23.8%	16.0%	15.0%
Op profit	28.5%	4.6%	24.6%	14.8%	15.0%
Net profit	46.2%	-10.1%	24.8%	15.3%	14.7%
Profitability					
Gross margin	42.7%	41.4%	41.3%	41.3%	41.4%
NP margin	31.8%	26.1%	26.3%	26.2%	26.1%
ROE	32.5%	25.2%	26.2%	25.6%	24.6%
ROIC	43.1%	30.7%	31.6%	34.9%	38.1%
Liquidity					
D/A	8.5%	10.7%	9.2%	8.0%	6.8%
ND/A	-13.6%	-1.4%	-9.0%	-18.0%	-23.7%
Liquid ratio	2.2	1.7	2.0	2.2	2.5
Quick ratio	1.9	1.4	1.6	1.9	2.2
Operating efficiency					
Asset turnover	1.4	1.3	1.3	1.2	1.1
Inventory turnover	5.6	4.1	4.5	4.5	4.6
AR turnover	3.1	2.3	2.7	3.1	3.0
AP turnover	1.8	1.4	1.6	1.8	1.7
Per share ratios(RMB)					
PE	2.10	1.89	2.36	2.72	3.12
PCF	2.07	0.73	2.66	3.30	3.20
PB	6.46	7.49	8.98	10.61	12.69
DPS	0.60	0.86	1.07	1.03	1.25
Valuation ratios					
PE	18.4	20.4	16.4	14.2	12.4
PB	6.0	5.2	4.3	3.6	3.0
EV/EBITDA	16.7	18.6	15.1	12.6	10.6

Investment Ratings

Rating	Definition
BUY	Expected to outperform the market index by >10% over the next 12 months
NEUTRAL	Expected to outperform or underperform the market index by 10% or less over the next 12 months
SELL	Expected to underperform the market index by >10% over the next 12 months

Analyst Disclosure

The analysts primarily responsible for the preparation of all or part of the research report contained herein hereby certify that: (i) the views expressed in this research report accurately reflect the personal views of each such analyst about the subject securities and issuers; and (ii) no part of the analyst's compensation was, is, or will be directly or indirectly, related to the specific recommendations or views expressed in this research report.

Regulatory Disclosure

Please refer to the important disclosures on our website <http://www.newone.com.hk/cmshk/en/disclosure.html>.

Disclaimer

This document is prepared by China Merchants Securities (HK) Co., Limited ("CMS HK"). CMS HK is a licensed corporation to carry on Type 1 (dealing in securities), Type 2 (dealing in futures), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities under the Securities and Futures Ordinance (Chapter 571). This document is for information purpose only. Neither the information nor opinion expressed shall be construed, expressly or impliedly, as an advice, offer or solicitation of an offer, invitation, advertisement, inducement, recommendation or representation of any kind or form whatsoever to buy or sell any security, financial instrument or any investment or other specific product. The securities, instruments or strategies discussed in this document may not be suitable for all investors, and certain investors may not be eligible to participate in some or all of them. Certain services and products are subject to legal restrictions and cannot be offered worldwide on an unrestricted basis and/or may not be eligible for sale to all investors. CMS HK is not registered as a broker-dealer in the United States and its products and services are not available to U.S. persons except as permitted under SEC Rule 15a-6.

The information and opinions, and associated estimates and forecasts, contained herein have been obtained from or are based on sources believed to be reliable. CMS HK, its holding or affiliated companies, or any of its or their directors, officers or employees ("CMS Group") do not represent or warrant, expressly or impliedly, that it is accurate, correct or complete and it should not be relied upon. CMS Group will not accept any responsibility or liability whatsoever for any use of or reliance upon this document or any of the content thereof. The contents and information in this document are only current as of the date of their publication and will be subject to change without prior notice. Past performance is not indicative of future performance. Estimates of future performance are based on assumptions that may not be realized. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. Opinions expressed herein may differ or be contrary to those expressed by other business divisions or other members of CMS Group as a result of using different assumptions and/or criteria.

This document has been prepared without regard to the individual financial circumstances and investment objectives of the persons who receive it. Use of any information herein shall be at the sole discretion and risk of the user. Investors are advised to independently evaluate particular investments and strategies, take financial and/or tax advice as to the implications (including tax) of investing in any of the securities or products mentioned in this document, and make their own investment decisions without relying on this publication.

CMS Group may have a long or short position, make markets, act as principal or agent, or engage in transactions in securities of companies referred to in this document and may also perform or seek to perform investment banking services or provide advisory or other services for those companies. This document is for the use of intended recipients only and this document may not be reproduced, distributed or published in whole or in part for any purpose without the prior consent of CMS Group. CMS Group will not be liable for any claims or lawsuits from any third parties arising from the use or distribution of this document. This document is for distribution only under such circumstances as may be permitted by applicable law. This document is not directed at you if CMS Group is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. In particular, this document is only made available to certain US persons to whom CMS Group is permitted to make available according to US securities laws, but cannot otherwise be made available, distributed or transmitted, whether directly or indirectly, into the US or to any US person. This document also cannot be distributed or transmitted, whether directly or indirectly, into Japan and Canada and not to the general public in the People's Republic of China (for the purpose of this document, excluding Hong Kong, Macau and Taiwan).

Hong Kong

China Merchants Securities (HK) Co., Ltd.

Address: 48/F, One Exchange Square, Central, Hong Kong

Tel: +852 3189 6888 Fax: +852 3101 0828