

JPM-pp1

Asia Pacific Equity Research

30 March 2015

BYD Electronic International (285 HK)

Neutral

Price: HK\$8.61

27 Mar 2015

Price Target: HK\$10.00

PT End Date: 30 Jun 2015

2H14 earnings first take

BYD-E's 2H14 earnings missed consensus by ~40% (actual Rmb312 vs the street at Rmb514) on a disappointing GM and an R&D hike, confirming our previous expectation on [March 2nd](#) and our cautious view on BYD-E. We expect the market to respond negatively on March 30. We leave our estimates unchanged, pending further review post the analyst briefing on March 30.

- **2H14 earnings miss on low margins:** 2H revenue came in slightly better than expected, but GM margin came in disappointingly at 9.7%, 1.8ppt lower than street estimates and 1.9ppt lower than 1H14. We believe the margin weakness is likely associated with the ramp-up costs with the new platform (~5K CNC machines) for Samsung on metal casing. R&D expenses also witnessed a big hike in 2H14 (+60% H/H or +56% Y/Y), highlighting the sharp learning curve on metal casing for multiple brands.

Table 1: BYD-E 2H14 earnings comparison – actual vs. JPMe vs. consensus

Rmb mn, except per share data	2H14				2H13		1H14		
	Actual	JPMe	Variance	Consensus	Variance	Y/Y	Actual	H/H	
Sales	10,728	9,986	7.4%	10,491	2.3%	8,462	26.8%	9,104	17.8%
Gross profit	1,044	1,118	-6.6%	1,212	-13.8%	852	22.6%	1,061	-1.5%
Operating profit	421	690	-39.1%	572	-26.4%	432	-2.6%	642	-34.5%
PBT	357	699	-48.9%			395	-9.5%	655	-45.4%
Net income	312	616	-49.3%	514	-39.3%	332	-5.9%	590	-47.1%
EPS (Rmb)	0.14	0.27	-49.3%			0.15	-5.9%	0.26	-47.1%
Gross Margin	9.7%	11.2%	-146 bps	11.6%	-182 bps	10.1%	-34 bps	11.7%	-192 bps
Operating Margin	3.9%	6.9%	-299 bps	5.4%	-153 bps	5.1%	-118 bps	7.1%	-314 bps
Net Margin	2.9%	6.2%	-326 bps	4.9%	-199 bps	3.9%	-101 bps	6.5%	-357 bps

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

Investment Thesis

BYD Electronic International (285 HK) is a handset component (including casing, mould/keypads and battery chargers) maker and EMS/ODM service provider for handset OEMs such as Nokia, Huawei and HTC. It sells components and provides assembly services for handset makers.

BYD-E is a prime beneficiary of second-tier smartphone vendors (HTC, OPPO) adopting metal casing for their handsets, which helps offset the decline in sales of plastic casing to Nokia and Huawei. We believe the next major catalyst for BYD-E's share price will be Samsung's allocation of metal casing orders to BYD-E. With Samsung's metal casing qualification process still ongoing, we do not think the likelihood of BYD-E's winning Samsung's metal casing orders in the near term is high.

Valuation

Our Jun-15 PT is HK\$10 based on a valuation multiple of 13x; 13x is close to the high-end of the historical trading range, which we think is justified given new breakthroughs in metal casing customers.

Risks to Rating and Price Target

Key upside risks include a higher adoption rate for metal casings and strong demand for customers' gadgets. Key downside risks include declining feature phone orders from Nokia and a "winning business first" mentality, potentially leading to loss-making contracts from time to time.

Technology - Hardware

AC

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
28-Apr-10	N	5.69	5.90
23-Aug-10	N	4.18	4.60
23-Dec-11	N	2.26	--
24-Apr-13	OW	3.15	6.00
16-May-13	OW	4.25	6.60
09-Jan-14	N	4.28	5.00
17-Jun-14	N	5.99	5.80
25-Aug-14	N	6.94	6.90
02-Oct-14	N	9.00	10.00

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