

## Q Tech Group | 1478.HK

### Recent setback provides good entry point

#### Fundamentals

#### ⚡ Robust 3Q16 shipment; Product mix continues to improve;

- Q Tech's 3Q16 shipment soared 82.4% Yoy to 48.7mn pieces, with 9M16 total shipment came in 122mn (83% of FY16E guidance). The robust figures continued to be driven by 70% Yoy shipment volume growth (~45.4mn and accounted for 93% of total shipment) and fingerprint recognition (up 237.4% Yoy, 3% of total shipment). The robust growth was led by 1.7x Yoy growth in  $\geq 8$ MP HCM shipment (~69% of total CCM volume vs. 43% in 3Q15). Top 5 clients accounted for ~86% of Q Tech's total CCM shipment in 1H16, with vivo & OPPO already contributed to 50% of company's total shipment.

- Management have revised up the monthly capacity by 15% to 23mn pieces/month (vs. previous guidance at 20mn pieces/month), which reflects strong demand for Q Tech's CCM. As first half shipment accounted for ~40% of full-year volume on average in 1H14 & 1H15, given the peak season in 2H16, the robust 9M16 shipment reaffirms our view that Q Tech would beat the 148mn shipment full-year target. (We maintain our estimates at 173mn, up 75.9% Yoy). We continue to see both the ASP and GPM to bottom out, on the grounds of increasing contribution from higher margin CCM ( $\geq 13$ MP HCM and dual cam) as well as the scaling up of fingerprint recognition in 2H16.

#### ⚡ Increasing dual cam and fingerprint recognition adoption amongst Chinese smartphone players

- We believe after the launch of iPhone 7 plus (with Wide+Tele backend dual cam), dual cam not only would become a standard spec. among flagship smartphones, but also began to penetrate into mid-end smartphones (RMB 1,000). Given the rising needs of selfies and relevant apps, as well as manufacturers' cost savings consideration, we believe RGB+RGB solution would be adopted in front cam by smartphone players in early stages. We expect Q Tech will continue to benefit from the rising trend of dual-cam adoption.

- Q-Tech shipped ~4.6mn units of fingerprint recognition modules in 9M16 which only accounted for 23% of FY16E guidance, however 3Q16 shipment grew by 2.4x QoQ and accounted 71% of the total shipment, which reflects the continuous ramp up of fingerprint recognition module. At 6kk/month production capacity in 1H16 and with further expansion to 10kk/month in FY16E, an average shipment of ~5.1kk/month in 4Q16 would still make management's FY16E guidance achievable, given the high seasonality demand, eg. The potential launch of Vivo X9 in November.

#### Catalysts

- ⚡ Faster than expected dual-cam adoption rate within Android camp
- ⚡ Successful entry into Huawei high-end smartphone supply chain
- ⚡ Announcement of dividend policy

#### Valuation

#### ⚡ Trading at FY17E 11.7x PE, turnaround & re-rating story continues

- We maintain Q Tech's FY16E/17E EPS unchanged. Though Q tech's stock price rocketed >20% since we issued the report on Oct 3, it is still trading at an undemanding FY17 11.7xPE (~40.3% discount to peers avg) and hence we believe Q Tech will continue to deserve a re-rating. We value Q-Tech's new TP at HK\$4.56 based on 13.5x FY17E PE (30% discount to peers avg.)

#### Short Term (6 Month)

Trading Buy

Trading Sell

**Current Price: HK\$3.96**

**Target price: HK\$4.56**

**Upside:15.1%**

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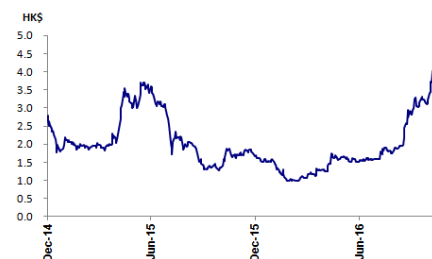
#### Trading data

52-Week Range (HK\$)	4.39/0.96
3 Mth Avg Daily Vol (m)	4.44
No. of Shares (m)	1,041.8
Market Cap (HK\$m)	4,125.4
Major Shareholders (%)	He Ning Ning (72.13%)
Auditors	KPMG
Result Due	FY16:Mar 2017

#### Company description

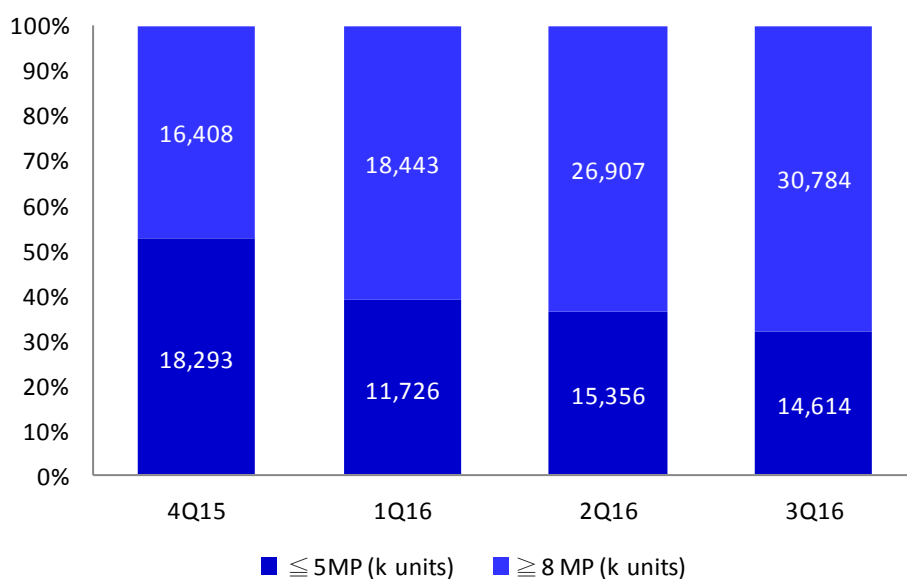
Established in 1997 and listed in HKEx in 2014, Q-tech is a leading PRC-based camera module manufacturer focusing on mid-to-high end camera module market for Chinese branded smart phone and tablet PC manufacturers. We were one of the first few manufacturers in China to use the COB (chip on board) and COF (chip on flex) assembly technologies in the manufacture of camera modules. Current customer portfolio includes leading Chinese smartphone players such as vivo, OPPO and Huawei etc

#### Price chart

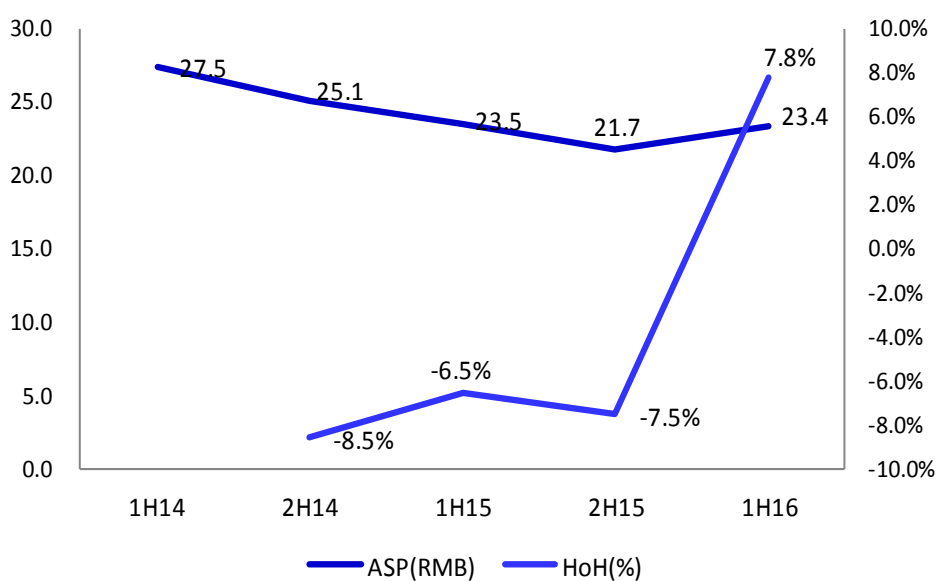


#### \* Note:

**FLASH NOTE represent short-term trading ideas by Cinda International Research which are distinguished from our normal coverage. The recommended stocks may not be continually followed.**

**Exhibit 1: Q Tech's  $\geq 8$ MP contributed ~69% of volume shipment in 3Q16 (vs. ~64% in 2Q16)**


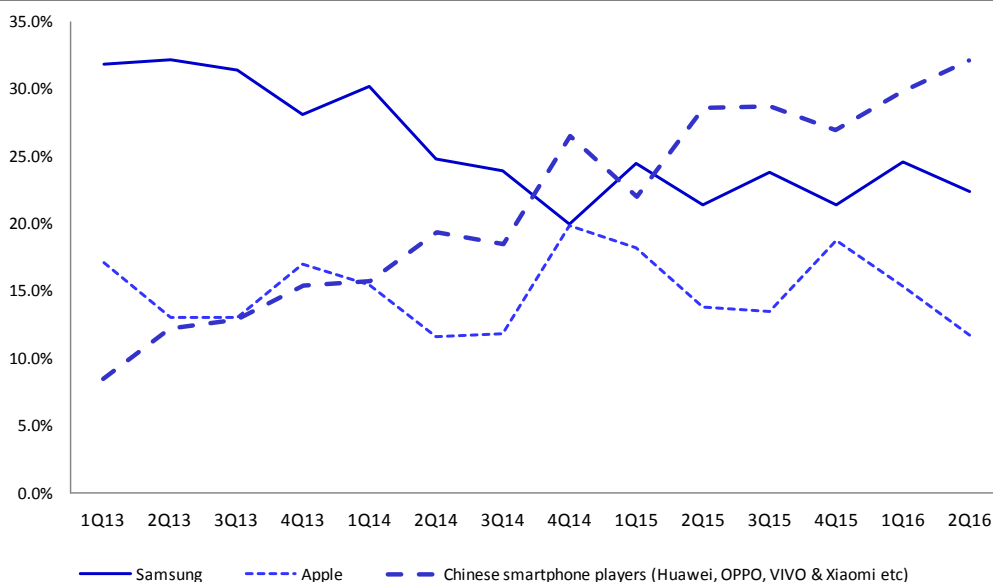
Source: Company data, CIRL

**Exhibit 2: Q Tech's CCM ASP sees signs of bottom out**


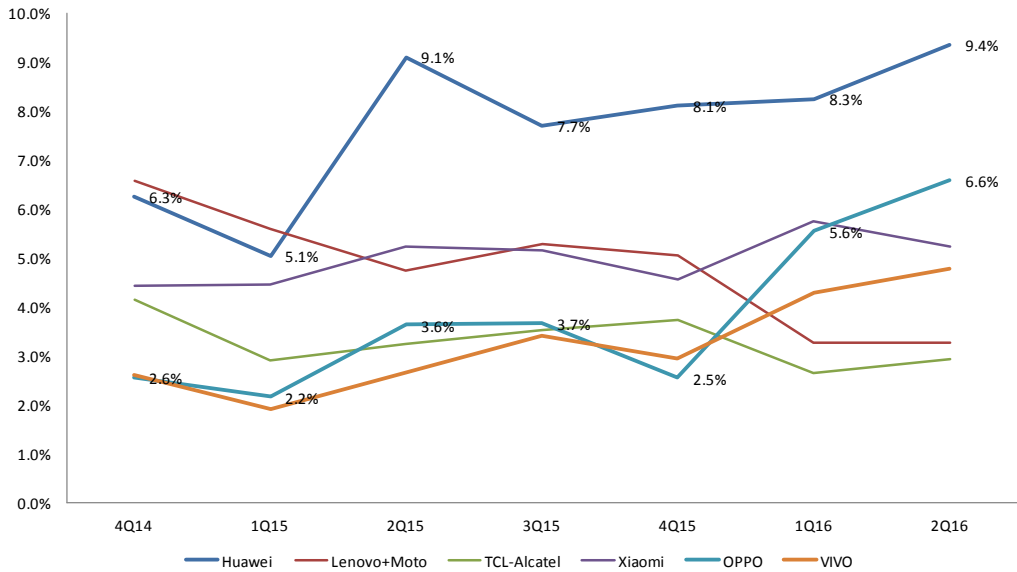
Source: Company data, CIRL

**Exhibit 3: Diversifying client mix for Q-tech**


Source: Company data

**Exhibit 4: Chinese smartphone vendors' market share overtook Apple & Samsung since 2Q16**


Source: IDC, Strategy Analytics, Company data, CIRL

**Exhibit 5: Huawei continue to be market leader in Chinese smartphone camp while VIVO & OPPO picks**


Source: IDC,, Company data, CIRL

**Exhibit 6: Dual-cam adoption in Letv x Coolpad's Cool1 dual and Redmi Pro**

## COOL1 dual 真双摄 酷生态

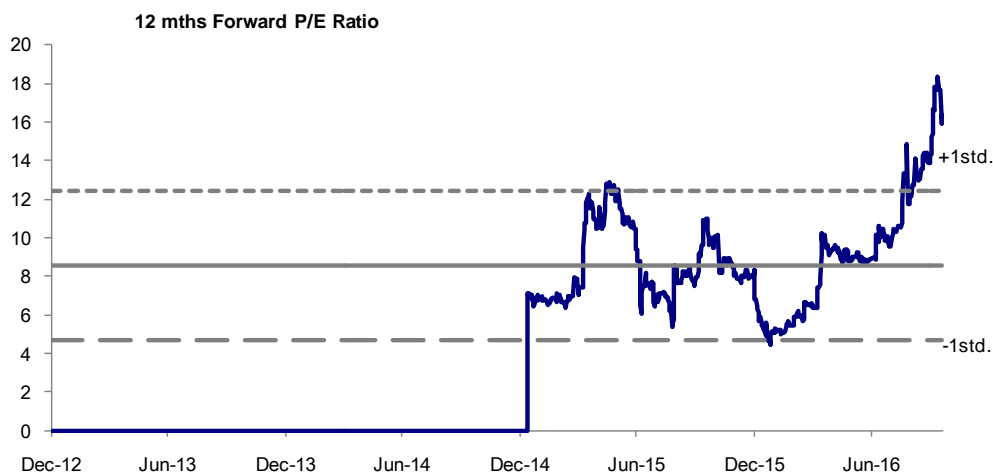
- 双1300万6P镜头
- MSM8976旗舰平台
- 4060mAh(typ)强续航
- 乐次元会员权益

3+32G 锋芒金	4+32G 锋芒金	4+64G 锋芒金	4+64G 周笔畅版
¥1099	¥1499	¥1699	¥1818

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Source: Company data, CIRL

**Exhibit 8: Q Tech's 12 month Forward P/E Ratio**


Source: Bloomberg, CIRL

**Exhibit 7: Peers comparison**

	bloomberg code	Mkt Cap (HKD mn)	Price (HKD)	3M		PER (x)					Yield (%)				
				3M	YTD	FY13	FY14	FY15	FY16E	FY17E	FY13	FY14	FY15	FY16E	FY17E
<b>HK Listed Peers</b>															
LENOVO GROUP	992 HK	56,765	5.11	1.2	(35.1)	10.7	8.4	-56.8	13.0	10.1	3.1%	5.2%	4.6%	4.1%	3.8%
AAC TECHNOLOGIES	2018 HK	95,723	77.95	15.0	54.2	29.4	32.8	25.0	21.4	17.2	1.2%	1.6%	1.3%	1.7%	2.0%
SUNNY OPTICAL	2382 HK	43,825	39.95	39.7	124.2	74.7	59.4	48.4	32.4	24.8	0.4%	0.5%	0.6%	0.9%	1.2%
FIH MOBILE LTD	2038 HK	20,366	2.58	(5.5)	(7.6)	32.0	14.9	11.2	32.3	20.6	0.0%	2.6%	3.2%	3.5%	2.3%
BYD ELECTRONIC	285 HK	14,218	6.31	19.7	51.7	17.2	12.5	12.8	10.2	9.0	0.4%	0.0%	0.7%	1.6%	1.7%
TONGDA GROUP HLD	698 HK	10,683	1.86	26.5	35.8	24.9	19.7	14.8	11.1	9.3	1.2%	2.0%	2.2%	2.7%	3.3%
TCL COMM TECH HL	2618 HK	9,554	7.47	3.6	30.8	27.2	8.2	8.8	14.1	12.2	0.6%	4.5%	4.4%	2.9%	2.9%
TRULY INTL HLDGS	732 HK	9,506	3.27	(10.2)	75.8	5.7	8.5	11.2	10.5	9.1	6.7%	3.1%	2.7%	3.1%	3.3%
COOLPAD	2369 HK	7,243	1.44	10.8	(6.9)	17.4	12.1	2.7	-96.0	21.5	1.3%	0.0%	1.7%	0.2%	0.3%
TONGDA GROUP HLD	698 HK	10,683	1.86	26.5	35.8	24.9	19.7	14.8	11.1	9.3	1.2%	2.0%	2.2%	2.7%	3.3%
JU TENG INTL HDG	3336 HK	2,811	2.51	2.9	(32.0)	3.8	3.8	3.3	5.5	4.4	5.4%	6.0%	6.5%	4.4%	5.1%
VITAL MOBILE HOL	6133 HK	901	1.06	17.8	(1.9)	6.5	3.5	3.6	-	-	0.0%	4.9%	0.0%	0.0%	0.0%
SKY LIGHT HOLDIN	3882 HK	1,943	2.29	175.9	(8.4)	-	-	7.6	-	-	0.0%	5.8%	6.2%	0.0%	0.0%
COWELL	1415 HK	2,303	2.77	8.2	(14.0)	5.3	5.0	4.8	6.1	5.1	0.0%	0.0%	1.5%	0.5%	0.7%
WAI CHI HOLD	1305 HK	429	1.98	1.0	(46.2)	-	5.1	-10.4	-	-	0.0%	1.0%	0.0%	0.0%	0.0%
TK GROUP HOLDING	2283 HK	1,761	2.13	6.5	(3.2)	9.7	11.2	9.3	8.5	7.2	1.4%	4.7%	4.0%	5.5%	6.6%
KA SHUI INTL HLD	822 HK	474	0.53	(13.1)	(22.1)	7.8	6.1	-7.5	-	-	20.8%	0.0%	0.0%	0.0%	0.0%
SAS DRAGON HLDG	1184 HK	837	1.34	5.5	(10.1)	4.1	5.5	10.4	-	-	0.0%	5.2%	0.0%	0.0%	0.0%
PANASIALUM HOLDI	2078 HK	1,032	0.86	0.0	0.0	4.5	-	4.5	-	-	5.5%	23.3%	0.0%	0.0%	0.0%
SCUD GROUP LTD	1399 HK	1,134	1.04	0.0	0.0	22.2	-	22.2	-	-	0.0%	1.0%	0.0%	0.0%	0.0%
SIM TECH GROUP	2000 HK	831	0.33	0.0	(27.0)	-3.5	34.6	12.8	-	-	0.0%	0.0%	0.0%	0.0%	0.0%
WILLAS-ARRAY ELE	854 HK	282	3.74	5.4	(16.9)	6.1	9.6	-3.9	-	-	7.8%	1.7%	0.0%	0.0%	0.0%
<b>Average</b>		<b>13,332</b>		<b>15.3</b>	<b>8.1</b>	<b>17.6</b>	<b>14.8</b>	<b>12.7</b>	<b>14.7</b>	<b>12.3</b>	<b>4.1%</b>	<b>4.4%</b>	<b>3.0%</b>	<b>2.6%</b>	<b>2.8%</b>
<b>Q TECHNOLOGY GRO</b>	<b>1478 HK</b>	<b>4,125</b>	<b>3.96</b>	<b>109.5</b>	<b>149.1</b>	<b>19.4</b>	<b>9.9</b>	<b>33.1</b>	<b>18.2</b>	<b>11.7</b>	<b>0.0%</b>	<b>1.2%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>
<b>Camera module/fingerprint module peers</b>															
TRULY INTL HLDGS	732 HK	9,506	3.27	(10.2)	75.8	5.7	11.2	12.4	10.5	9.1	6.7%	3.0%	2.7%	3.1%	3.3%
SUNNY OPTICAL	2382 HK	43,825	39.95	39.7	124.2	45.7	45.7	48.4	32.4	24.8	0.4%	0.5%	0.6%	0.9%	1.2%
LITE-ON TECHNOLO	2301 TT	26,470	11.32	(5.6)	45.0	11.5	15.0	15.5	12.8	11.8	5.6%	4.7%	4.4%	5.1%	5.7%
ADVANCED SEMICON	2311 TT	75,223	9.49	4.3	1.4	17.4	15.2	14.1	14.3	12.3	2.9%	4.0%	5.6%	4.5%	4.8%
PRIMAX ELECTRONI	4915 TT	4,977	11.27	6.4	9.3	27.8	11.4	11.7	10.1	8.8	1.8%	3.5%	4.8%	5.5%	6.5%
LG INNOTEK CO LT	011070 KS	12,648	534.45	(13.8)	(21.5)	97.8	19.4	15.4	-1,595.4	12.5	0.3%	0.4%	0.4%	0.4%	0.5%
CRUCIALTEC CO LT	114120 KS	1,813	63.54	(11.2)	(41.5)	-9.1	26.6	319.3	17.2	12.5	0.0%	0.0%	0.0%	0.0%	0.0%
HUIZHOU SPEED -A	300322 CH	9,017	22.13	(2.6)	(1.5)	185.7	-69.0	-90.7	78.2	51.2	0.0%	0.0%	0.4%	0.0%	0.0%
SHENZHEN O-FIL-A	002456 CH	44,516	42.41	8.0	18.6	53.8	74.7	68.3	42.1	29.7	0.4%	0.6%	0.3%	0.3%	0.5%
<b>Average</b>		<b>25,333</b>		<b>1.7</b>	<b>23.3</b>	<b>55.7</b>	<b>27.4</b>	<b>63.1</b>	<b>27.2</b>	<b>19.2</b>	<b>2.2%</b>	<b>2.6%</b>	<b>2.6%</b>	<b>3.2%</b>	<b>3.6%</b>
<b>Q TECHNOLOGY GRO</b>	<b>1478 HK</b>	<b>4,125</b>	<b>3.96</b>	<b>109.5</b>	<b>149.1</b>	<b>19.4</b>	<b>9.9</b>	<b>33.1</b>	<b>18.2</b>	<b>11.7</b>	<b>0.0%</b>	<b>1.2%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>

Source: Bloomberg, CIRL

**Exhibit 8: Financial statement**
**Income statement**

Year to Dec (RMB mn)	FY13A	FY14A	FY15A	FY16E	FY17E
<b>Revenue</b>	<b>1,411</b>	<b>2,161</b>	<b>2,202</b>	<b>3,957</b>	<b>6,102</b>
Gross profit (reported)	234	353	241	372	604
<b>EBITDA</b>	<b>207</b>	<b>294</b>	<b>167</b>	<b>290</b>	<b>455</b>
Depreciation	15	31	42	57	81
<b>EBIT</b>	<b>192</b>	<b>262</b>	<b>125</b>	<b>231</b>	<b>370</b>
Net interest income (exp.)	(9)	(23)	(10)	(18)	(28)
Associates	5	0	0	0	0
Exceptionals/others	0	0	0	0	0
<b>Profit before tax</b>	<b>188</b>	<b>239</b>	<b>115</b>	<b>213</b>	<b>342</b>
Tax expenses	(25)	(44)	(13)	(24)	(38)
Minority interest	0	0	0	0	0
<b>Net profit</b>	<b>163</b>	<b>196</b>	<b>102</b>	<b>190</b>	<b>304</b>
Dividends	0	41	0	0	0

**Balance sheet**

Year to Dec (RMB mn)	FY13A	FY14A	FY15A	FY16E	FY17E
Cash & equiv	51	803	428	375	256
Trade receivables	872	873	889	1,385	2,136
Other receivables	0	0	0	0	0
Inventories	129	142	209	382	586
Other current assets	416	125	11	11	11
Fixed assets	270	336	421	512	577
Intangible assets	0	0	1	2	3
Investment, associates etc	24	24	32	32	32
<b>Total assets</b>	<b>1,762</b>	<b>2,303</b>	<b>1,991</b>	<b>2,698</b>	<b>3,601</b>
Account payables	904	445	622	1,137	1,743
Other payables	0	0	0	0	0
Short-term debt	428	713	142	146	137
Other current liabs	15	12	2	2	2
Long-term debts	146	0	0	0	0
Deferred tax and others	0	8	2	2	2
Other long-term liabs	0	1	5	5	5
<b>Total liabilities</b>	<b>1,494</b>	<b>1,178</b>	<b>773</b>	<b>1,291</b>	<b>1,890</b>
Share capital	0	8	8	8	8
Reserves	269	1,116	1,209	1,399	1,703
<b>Shareholders' equity</b>	<b>269</b>	<b>1,124</b>	<b>1,218</b>	<b>1,407</b>	<b>1,711</b>
Minorities	0	0	0	0	0
<b>Total equity</b>	<b>269</b>	<b>1,124</b>	<b>1,218</b>	<b>1,407</b>	<b>1,711</b>
Net cash (debt)	(523)	90	286	229	119

**Cash flow**

Year to Dec (RMB mn)	FY13A	FY14A	FY15A	FY16E	FY17E
Pre-tax profit	188	239	115	213	342
Taxes paid	(25)	(44)	(13)	(24)	(38)
Depreciation	(15)	(31)	(42)	(57)	(81)
Associates	(5)	0	0	0	0
CFO bef. WC change	143	165	60	133	223
Change in working cap	(337)	(473)	93	(155)	(348)
<b>Cashflow from operation</b>	<b>(194)</b>	<b>(308)</b>	<b>153</b>	<b>(22)</b>	<b>(125)</b>
CAPEX	(152)	(98)	(132)	(150)	(150)
<b>Free cash flow</b>	<b>(346)</b>	<b>(406)</b>	<b>21</b>	<b>(172)</b>	<b>(275)</b>
Dividends	0	41	0	0	0
Balance sheet adj.	(172)	979	174	115	165
Shares issued	0	0	0	0	0
Others	0	0	0	0	0
<b>Net cash flow</b>	<b>(518)</b>	<b>613</b>	<b>195</b>	<b>(57)</b>	<b>(110)</b>
Net cash (debt) start	(4)	(523)	90	286	229
Net cash (debt) at year-end	(523)	90	286	229	119

**Ratios**

Year to Dec	FY13A	FY14A	FY15A	FY16E	FY17E
<b>Growth rate (%)</b>					
Revenue	121.2	53.2	1.9	79.7	54.2
EBITDA	195.6	41.6	(43.1)	73.6	56.8
EBIT	233.9	36.6	(52.5)	85.5	59.9
Net profit	222.9	19.8	(47.8)	86.0	60.4
Fully diluted EPS	223.3%	94.6%	-68.3%	86.0%	60.4%
<b>Margins (%)</b>					
Gross margin (reported)	16.6	16.3	10.9	9.4	9.9
EBITDA	14.7	13.6	7.6	7.3	7.5
EBIT	13.6	12.1	5.7	5.8	6.1
Net margin	11.6	9.0	4.6	4.8	5.0
<b>Other ratios</b>					
ROE (%)	60.7	17.4	8.4	13.5	17.8
ROA (%)	9.3	8.5	5.1	7.0	8.4
Net gearing (%)	194.6	(8.0)	(23.5)	(16.3)	(6.9)
Interest coverage (x)	21.3	11.3	12.5	12.9	13.4
Receivables days	225.6	147.4	147.3	127.8	127.8
Payables days	280.6	89.8	115.7	115.7	115.7
Inventory days	40.1	28.6	38.9	38.9	38.9
Effective tax rate (%)	13.7	18.2	11.1	11.1	11.1

Source: Company data, CIRL estimates

## Rating Policy

	Rating	Definition
<b>Stock Rating</b>	Buy	Outperform HSI by 15%
	Neutral	Between -15% ~ 15% of the HSI
	Sell	Underperform HSI by -15%
<b>Sector Rating</b>	Accumulate	Outperform HSI by 10%
	Neutral	Between -10% ~ 10% of the HSI
	Reduce	Underperform HSI by -10%

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## Analyst Certification

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