

Plover Bay Technologies – Business update & Forecast revision

BUY

Minimal impact from the US-China trade war

TMT

Plover Bay Technologies (Plover Bay) made a conference call regarding the possible impact of US tariff. The management confirms that the trade war should have minimal effect to the company's results, and the company has prepared several plans to handle the new tariff. We have also revised our forecast as the strong momentum in 4Q17 did not extend into 1H18 as originally expected. We reiterate our BUY rating on Plover Bay with a new TP of HKD2.57 based on a 20x FY19E PER, or 27x FY18E PER for 155% upside potential.

Products are potentially included in the latest tariff list – The US Trade Representative (USTR) announced a new tariff list on 10 July 18, proposing to impose a tariff of 10% on an additional US\$200bn of Chinese imports. In which, a product description of “Machines for the reception, conversion and transmission or regeneration of voice, images or other data, including switching and routing appa (HTSUS Subheading: 8517.62.00)” was included in the list. As the major product of Plover Bay is SD-router, which the function meets the description above, the management believes its products are potentially affected by the new tariff.

Only low-end products are manufactured in China – Plover Bay has been outsourcing its manufacturing to Taiwanese EMS providers for better IP protection. However, some of the low end products are made by their factories in the Mainland China and part of those were included in the tariff list. In fact, Plover Bay can transfer all the manufacturing process to Taiwan if necessary.

Well-prepared plans to handle the new tariff – The new tariff is expected to be effective on 30 Aug, the company will shift all the manufacturing process of the low-end product that shipped to the US, from Mainland China to Taiwan, in order to avoid the tariff. As a result, only low-end products for non US-market would be produced in China. The Taiwan EMS providers should be able to pick up those shifted orders in Sep or Oct this year, while the company's inventory can fulfill the demand in between. According to the management, the manufacturing costs in China and Taiwan are nearly the same. In FY17, 57.4% of the company's revenue was generated from North America and those customers tend to buy some high-end models. In addition, Plover Bay's product prices are relatively lower than its competitors even after the tariff.

Recommendation

Ticker	1523 HK
Rating	BUY
Last Close	HKD1.01
Target Price	HKD2.57
Previous Target	HKD2.85
Up/(Down)side	154.9%
Previous Rating	BUY

Share Information

52-week range (HKD)	0.98 – 2.40
ADT (3M) (HKD'mn)	0.99
Market Cap. (HKD'mn)	1,027.0
Shares outstanding ('mn)	1,016.8
Free float (%)	25.53
SH-HK Connect	No
SZ-HK Connect	No

Major Shareholders

Mr. Chan Wing Hong Alex	74.47%
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Share Price Performance



Source: Bloomberg

Key Financials – Fiscal Year Ended December 31

(USD'000)	FY16	FY17	FY18E	FY19E	FY20E
Revenue	28,358	37,132	48,132	61,413	77,689
Growth	29.7%	30.9%	29.6%	27.6%	26.5%
Operating profit	6,675	10,629	14,776	20,142	25,688
Growth	61.2%	59.2%	39.0%	36.3%	27.5%
Net profit	5,240	8,754	12,338	16,819	22,033
Growth	56.1%	67.1%	40.9%	36.3%	31.0%
			CAGR FY18E-20E		33.6%
EPS (US cents)	0.52	0.87	1.21	1.65	2.17
PER (x)	25.1	14.9	10.7	7.8	6.0
PBR (x)	5.4	4.6	4.1	3.5	2.9
Dividend Yield (%)	3.6%	6.0%	7.0%	9.6%	12.5%

Source: Company data, Oceanwide Securities

Tsz Wang Poon

☎: +852 2971 5432

✉: edwin.poon@oceanwidefinancial.com

Howard Wong

☎: +852 2971 5435

✉: howard.wong@oceanwidefinancial.com

New vs Original Estimates

USD'mn	FY18E			FY19E			FY20E		
	Original	New	Change	Original	New	Change	Original	New	Change
Revenue	53.6	48.1	-10.3%	72.9	61.4	-15.8%	94.8	77.7	-18.1%
GPM	63.4%	61.7%	-1.7 ppt	64.0%	61.7%	-2.29 ppt	64.8%	61.8%	-3.04 ppt
Operating Profit	15.8	14.8	-6.6%	22.2	20.1	-9.2%	29.0	26.4	-9.2%
Net Profit	13.2	12.3	-6.6%	18.5	16.8	-9.2%	24.3	22.0	-9.2%
NPM	24.6%	25.6%	1.0 ppt	25.4%	27.4%	1.99 ppt	25.6%	28.4%	2.78 ppt

Source: Oceanwide Securities

Thanks to the increasing global awareness of SD-WAN technologies, the market demand for high performance internet connectivity is strong. As the strong momentum in 4Q17 did not carry into 1H18, we have lowered the top-line forecasts in our model by 10.3%, 15.8% and 18.1%, for FY18E-20E, respectively. However, we still maintain a positive view on the company given the strong market potential of the connectivity and the IoT segments.

In terms of GPM, as the company may adopt a more aggressive pricing strategy for large contracts or new market segments, we have trimmed our overall GPM for FY18E-20E to between 61 and 62%. With its stringent cost control measures, we believe that the company will have better economies of scale in the future, when its NPM will jump from 25.6% in FY18E to 28.4% in FY20E. Based on our new estimates, we expect the company to register a 33.6% CAGR in net profit in FY18E-20E.

Financial Statements

Income Statement (USD'000)						Cashflow Statement (USD'000)					
	2016	2017	2018E	2019E	2020E		2016	2017	2018E	2019E	2020E
Revenue	28,358	37,132	48,132	61,413	77,689	Operating cashflow					
Cost of goods sold	(10,413)	(14,157)	(18,447)	(23,515)	(29,694)	EBITDA	7,641	12,177	16,201	22,087	29,042
Gross profit	17,945	22,975	29,685	37,898	47,995	Tax paid	(346)	(2,547)	(2,438)	(3,323)	(4,354)
Other income and gains, net	104	463	300	300	300	Operating cashflow before W/C	7,295	9,630	13,763	18,763	24,688
Operating expenses	(11,351)	(12,783)	(15,210)	(18,055)	(21,908)	Change in working capital	(2,875)	(6,821)	562	(2,829)	(2,446)
EBIT	6,698	10,655	14,776	20,142	26,387	Cash flow from operations	4,420	2,809	14,324	15,934	22,241
Finance costs	(23)	(26)	-	-	-	Investing activities					
Profit before tax	6,675	10,629	14,776	20,142	26,387	Capex	(937)	(8,936)	(1,716)	(2,342)	(3,198)
Income tax expense	(1,435)	(1,875)	(2,438)	(3,323)	(4,354)	Others	-	-	-	-	-
Profit after tax	5,240	8,754	12,338	16,819	22,033	Cash flow from investing activities	(937)	(8,936)	(1,716)	(2,342)	(3,198)
Minority interest	-	-	-	-	-	Financing activities					
Attributable profit to shareholders	5,240	8,754	12,338	16,819	22,033	Bank loan movement	(920)	1,643	(1,944)	-	-
						Dividend paid	(3,228)	(5,824)	(9,177)	(10,924)	(14,561)
						Interest paid	(23)	(26)	-	-	-
						Issue/(Buyback) Shares	16,111	-	-	-	-
						Others	(2,286)	887	-	-	-
						Cash flow from financing activities	9,654	(3,320)	(11,121)	(10,924)	(14,561)
						Net increase/decrease in cash and cash equivalents	13,137	(9,447)	1,487	2,668	4,482
						Cash and cash equivalents at beginning of the Year	6,062	19,193	16,747	18,234	20,902
						Non Pledged time deposit	-	7,115	-	-	-
						Effect of foreign exchange rate	(6)	(114)	-	-	-
						Cash and cash equivalents at end of the Year	19,193	16,747	18,234	20,902	25,384
Per Share Items (US cents)						Ratio Analysis					
	2016	2017	2018E	2019E	2020E		2016	2017	2018E	2019E	2020E
EPS	0.52	0.87	1.21	1.65	2.17	Growth (YoY%)					
Diluted EPS	0.52	0.87	1.21	1.65	2.17	Revenue	29.7%	30.9%	29.6%	27.6%	26.5%
DPS (HK cents)	3.66	6.08	7.09	9.67	12.67	EBIT	61.7%	59.1%	38.7%	36.3%	31.0%
BVPS	2.42	2.83	3.14	3.72	4.45	Net profit	56.1%	67.1%	40.9%	36.3%	31.0%
						Diluted EPS	56.1%	68.8%	39.5%	36.3%	31.0%
						Margins					
						Gross profit margin	63.3%	61.9%	61.7%	61.7%	61.8%
						EBIT margin	23.6%	28.7%	30.7%	32.8%	34.0%
						Net profit margin	18.5%	23.6%	25.6%	27.4%	28.4%
						Other ratios					
						Sales/ avg. assets	118.5%	101.7%	117.2%	135.5%	147.0%
						Return on average assets	21.9%	24.0%	30.0%	37.1%	41.7%
						Return on average equity	33.4%	33.0%	40.7%	48.3%	53.0%
						ROIC	21.3%	28.5%	38.7%	44.5%	48.7%
						Dividend payout ratio	91.1%	89.6%	75.0%	75.0%	75.0%
						Valuation measures					
						PSR (x)	4.7	3.6	2.8	2.2	1.7
						PER (x)	25.4	15.0	10.8	7.9	6.0
						PBR (x)	5.5	4.6	4.2	3.5	2.9
						Dividend yield	3.6%	6.0%	7.0%	9.6%	12.5%
Balance Sheet (USD'000)						Key Ratios					
	2016	2017	2018E	2019E	2020E		2016	2017	2018E	2019E	2020E
Non-current assets						Debt to equity	1.3%	6.8%	-	-	-
PPE	694	1,995	2,188	2,448	2,800	Net debt to equity	-	-	-	-	-
Intangible assets	383	661	759	896	1,088	Capex/ Sales	3.3%	24.1%	3.6%	3.8%	4.1%
Others	106	22	22	22	22	Current ratio (x)	4.3	3.6	4.6	4.6	5.2
Total non-current assets	1,183	2,678	2,969	3,366	3,910	Quick ratio (x)	2.61	1.59	2.18	2.10	2.52
Current assets						Interest coverage (x)	332	468	-	-	-
Inventories	6,678	11,629	11,619	14,151	15,136	Days inventory (days)	190	236	230	200	180
Trade receivables	5,315	9,476	8,718	10,610	12,169	Days receivable (days)	161	191	180	150	140
Pledged bank balances	129	-	-	-	-	Days payable (days)	51	58	50	50	50
Cash and cash equivalents	19,193	16,747	18,234	20,902	25,384	Cash conversion cycle (days)	299	368	360	300	270
Others	-	29	29	29	29						
Total current assets	31,315	37,881	38,600	45,692	52,718						
Total assets	32,498	40,559	41,569	49,058	56,628						
Current liabilities											
Trade payables	1,884	2,630	2,424	4,019	4,117						
Deferred revenue	3,551	5,036	5,036	5,036	5,036						
Bank borrowings	318	1,944	-	-	-						
Tax liabilities	1,589	919	919	919	919						
Others	-	-	-	-	-						
Total current liabilities	7,342	10,529	8,379	9,974	10,072						
Non-current liabilities											
Deferred tax liabilities	56	95	95	95	95						
Deferred revenue	854	1,185	1,185	1,185	1,185						
Total non-current liabilities	910	1,280	1,280	1,280	1,280						
Total liabilities	1,820	2,560	2,560	2,560	2,560						
Shareholders' equity											
Share capital	1,288	1,307	1,307	1,307	1,307						
Reserves	22,958	27,443	30,603	36,498	43,969						
Total shareholders' equity	24,246	28,750	31,910	37,805	45,276						
Minority interest	-	-	-	-	-						
Total equity	24,246	28,750	31,910	37,805	45,276						

Source: Company data, Oceanwide Securities

Rating Definitions	Disclaimer and Risk Statement
BUY We expect the stock to have a total return of > 15% over the next 12 months	This document is published by Oceanwide Securities Company Limited ("Oceanwide Securities"), a licensed corporation (central entity number AAC577) regulated by the Securities and Futures Commission in Hong Kong. This document is for distribution in Hong Kong only to persons who are "Professional Investors" as defined in Part 1 of Schedule 1 of Securities and Futures Ordinance (Cap 571) of Hong Kong and any rules made thereunder. This document is not intended for distribution to or use by, any person or entity who is a citizen or resident of any jurisdiction where such distribution or use would be contrary to applicable law or regulation within such jurisdiction. This document does not constitute an offer or a solicitation of an offer to buy or sell any securities. This document is circulated to addresses solely and may not be reproduced or redistributed to any other person or published, in whole or in part, for any purpose. The research is based on information obtained from sources believed to be reliable, but Oceanwide Securities does not make any representation or warranty as to its accuracy, completeness or correctness. Opinions expressed are subject to change without prior notice. Any recommendation does not have regard to specific investment objectives, financial situation and particular needs of any specific addressee. Oceanwide Securities accepts no liability whatsoever for any direct or consequential loss arising from any use of this document. Oceanwide Securities and its affiliates as well as persons associated with any of them from time to time may or may not have interests in the securities mentioned in this document. The prices of securities may move up or down, and past performance is not an indication of future performance. Investors shall consider seeking separate legal or financial advice before making investment decisions.
HOLD We expect the stock to have a total return of < 15% and >-15% over the next 12 months	
SELL We expect the stock to have a total return of < -15% over the next 12 months	
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