

BUY

18 April 2005

Results in-line but GP under pressure

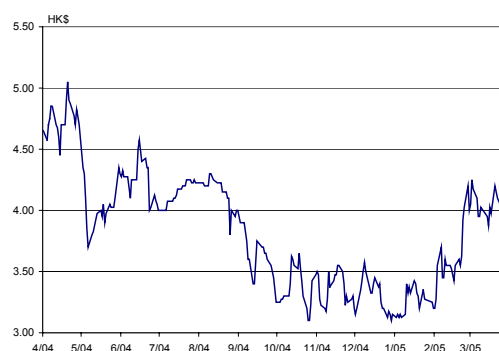
- **Net profit up 21%:** Turnover gained 36% to over HK\$1bn backed by strong growth from indoor solutions and export sales. Net profit stood at HK\$255mn, which is 6% lower to our expectation. During the year, sales from Unicom's CDMA grew by 135%. EPS for the year was 30.7 HK cents and a final dividend of 5 HK cents was declared, giving a full year payout ratio of 29.3%
- **GP margin trimmed due to price-cutting:** During 2H04, Comba lowered its selling price in order to maintain its market leadership in the PRC. As a result, Comba lost 3.4 percentage points in GP margin from 46.4% in FY03 to 43.0% in FY04. Going forward, we expect Comba's GP margin to hover around 40% before registering any significant sales on 3G products.
- **A lot more than 3G:** Instead of waiting for PRC's actions on 3G, Comba has been actively seeking for OEM and export opportunities to expand its business coverage and customer base. Engagements have been made with PRC's ZTE and Huawei as well as RFS and Alan Dick for international markets.
- **Earnings revisions:** We lower our profit forecast for FY05 and FY06 by 9% and 12%, respectively, to reflect the price cut for 2G products. Nevertheless, we are still expecting a good earnings growth of over 20% in the next few years as the contribution from new products kick in.
- **Target price revised to HK\$4.53 for 16% upside potential:** We believe the near-term share price catalyst remains to be the announcement of when to launch 3G in the PRC. However, given the lead-time required for tendering and installation, the window for recording significant profit contribution in FY05 diminishes over time. As such, we maintain our target price at 12x FY05 PER, which does not include any contribution from 3G.

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KEY DATA

<i>Sector</i>	<i>Telecom equipment</i>
<i>Share price</i>	<i>HK\$3.90</i>
<i>Stock code</i>	<i>2342</i>
<i>Shares O/S</i>	<i>832.73mn</i>
<i>Mkt. Cap</i>	<i>HK\$3,247mn</i>
<i>52wks High-Low</i>	<i>HK\$4.96-3.00</i>
<i>NAV per share</i>	<i>HK\$1.32</i>
<i>Major Shareholders</i>	<i>Fok Tung Ling (52.68%)</i> <i>Zhang Yue Jun (14.1%)</i>

Price Performance



Source: Bloomberg

Earnings Summary

YE: 31st Dec	FY03A	FY04A	FY05F	FY06F	FY07F
Turnover (HK\$'mn)	806.2	1,092.8	1,449.6	1,792.3	2,163.8
Growth (%)	39	36	33	24	21
Net profit (HK\$'mn)	211.2	255.1	314.5	392.8	472.4
Growth (%)	30	21	23	25	20
EPS (HK cents)	29.9	30.7	37.8	47.2	56.7
P/E (x)	13.0	12.7	10.3	8.3	6.9
DPS (HK cents)	5.0	9.0	11.0	14.0	14.0
Yield (%)	1.3	2.3	2.8	3.6	3.6

Source: company information, FSSL

Results comment

HK\$'mn	Year ended 31 December		Comments
	FY03	vs. FY04	
Turnover	806.2	1,092.8	Turnover up 35.5%, in-line with expectation. Sales from Unicom's CDMA went up by 135%. Export sales up
Cost of sales	<u>(432.0)</u>	<u>(623.3)</u>	
Gross profit	374.2	469.4	GP margin dropped by 3.4 percentage points due from price cuttings in 2G products
Other revenue	4.0	8.7	
Selling expenses	(42.4)	(69.4)	Increased to 6.4% of turnover from the 5.3% in FY03
Admin expenses	(98.3)	(136.6)	Up 39% largely attributable to the expanded sales and technical teams
Other operating expenses	<u>(10.8)</u>	<u>(8.3)</u>	
Operating profit	226.6	263.8	
Finance costs	<u>(5.5)</u>	<u>(9.5)</u>	Included HK\$2.2mn of factoring cost in FY04
Profit before tax	221.1	254.2	
Tax	<u>(15.9)</u>	<u>(6.0)</u>	Effective tax rate dropped to 2.4%
Profit after tax	205.2	248.2	
Minority interests	<u>5.9</u>	<u>6.9</u>	
Net profit	<u>211.1</u>	<u>255.1</u>	20.8% increase; about 6% below our expectation
Basic EPS (HK cents)	29.9	30.7	EPS up only 2.7% as Comba was only listed in July 2003
DPS (HK cents)	5.0	9.0	29.3% payout ratio

Source: company information, FSSL

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