



Rating  
**Hold**

Asia  
China

Technology  
Hardware & Equipment

Company  
**O-Film**

Reuters 002456.SZ    Bloomberg 002456 CH    Exchange SHZ    Ticker 002456

Date  
22 August 2017

## Forecast Change

Price at 21 Aug 2017 (CNY)	20.35
Price target - 12mth (CNY)	20.50
52-week range (CNY)	20.35 - 12.65
Shenzhen Index	2,004

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## Dual cam driving growth

### Positive results/guidance, but fairly priced; Sunny is our top pick in CCM

O-Film delivered strong 2Q17 results and positive outlook for 2H17 and 2018, driven by dual-cam and rising contribution from Apple. We raise our target price to RMB20.5 but maintain Hold. Trading at 26x PER (0.8x PEG), we think it is fairly priced. In the CCM space, we prefer Sunny Optical to O-Film. Both companies enjoy a similar growth outlook (30%+ EPS CAGR for 2017-2020), largely driven by the same story (dual cam), but Sunny outperforms O-Film in EPS quality (positive free cash flows for Sunny since 2015 vs negative cash flows for O-Film since 2009) and ROE (48% vs 18% in 2017E).

### Strong 2Q17 results: ramp-up in dual cam and new Apple businesses

O-Film reported EPS of RMB0.16 (+125% YoY; +70% QoQ) and operating profit of RMB549mn (+124% QoQ; +54% YoY) on sales of RMB8.9bn (+44% QoQ; +31% YoY). Sales and operating profit came in 6% and 16% higher than our estimate, owing to rising contribution from Apple (touch panel for new iPads, as well as iPhone front cam via the acquisition of Sony's Guangzhou plant) and strong CCM business (sales up ~100% YoY, shipment up ~60%). Dual-cam shipment reached 10mn+ in 1H17 (mostly in 2Q17) from almost nil in 2H16, which helped in increasing ASP.

### 3Q17 outlook and key Q&As (page 3 for details)

O-Film expects 3Q17 net income to fall in the range of RMB400mn (+101% YoY) to RMB630mn (+216% YoY) with GPM up slightly, powered by the ramp-up in dual cam, a better product mix, and improving profitability from the newly acquired Guangzhou plant. On dual cam, O-Film has reiterated its 2017 shipment target of 50mn units (mainly for Chinese clients), and estimates the dual cam penetration on China smartphones is ~20% in 2017 and will exceed 40% in 2018. On the new business – automotive electronics – sales reached RMB128mn in 1H17. It has developed an ADAS solution (comprising 6 to 8 cameras and a central control unit) and sampled out to clients.

### Valuation and investment risks

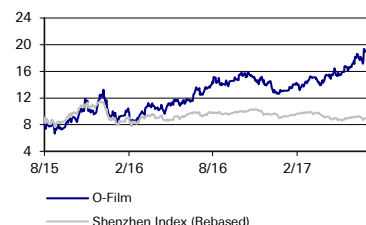
We raise 2017-19 EPS forecasts by 7%-22% (dual cam and Apple biz) and increase TP from RMB14.4 to RMB20.5, based on 26x 2018 EPS or 0.8x PEG (2017-2020 EPS CAGR of 33%). Earlier, our TP was based on 22x 2017 EPS, or 0.8x PEG (EPS CAGR of 28%). 0.8x PEG is in line with the trading average of regional tech peers. Risks: market-share losses, ASP erosion, and FX.

### Key changes

TP	14.40 to 20.50	↑	42.4%
Sales (FYE)	31,902 to 35,648	↑	11.7%
Op prof margin (FYE)	5.7 to 5.4	↓	-4.0%
Net profit (FYE)	1,496.5 to 1,598.2	↑	6.8%

Source: Deutsche Bank

### Price/price relative



Performance (%)	1m	3m	12m
Absolute	7.4	31.8	47.0
Shenzhen Index	3.8	3.4	-6.3

Source: Deutsche Bank

### Forecasts And Ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (CNYm)	18,456	26,746	35,648	44,274	50,893
DB EPS FD(CNY)	0.19	0.28	0.59	0.79	0.90
OLD DB EPS FD(CNY)	0.19	0.28	0.55	0.65	0.77
% Change	0.0%	0.0%	6.8%	21.8%	17.2%
DB EPS growth (%)	-38.0	48.5	113.1	33.9	14.3
PER (x)	59.6	44.2	34.6	25.8	22.6

Source: Deutsche Bank estimates, company data



Model updated: 22 August 2017

Running the numbers

Asia  
 China  
 Hardware & Equipment

O-Film

Reuters: 002456.SZ Bloomberg: 002456.CH

Hold

Price (21 Aug 17) CNY 20.35  
 Target Price CNY 20.50  
 52 Week range CNY 12.65 - 20.35  
 Market Cap (m) CNYm 52,432  
 USDm 7,859

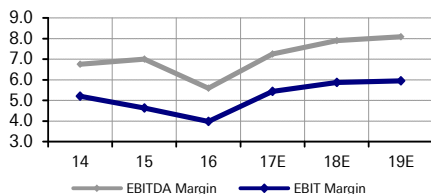
Company Profile

Established in 2001 and listed on Shenzhen stock exchange in 2010, O-Film ranks as the largest touch panel manufacturer in China with 15-20% global market share. The company also offers a wide range of handset component including handset camera module, fingerprint sensor, etc.

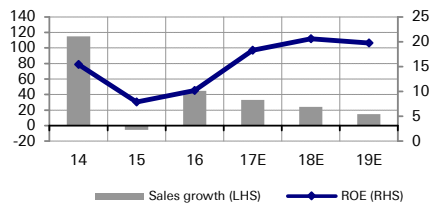
Price Performance



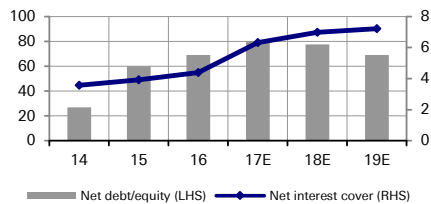
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

2014 2015 2016 2017E 2018E 2019E

Financial Summary

DB EPS (CNY)	0.30	0.19	0.28	0.59	0.79	0.90
Reported EPS (CNY)	0.30	0.19	0.28	0.59	0.79	0.90
DPS (CNY)	0.02	0.01	0.02	0.07	0.09	0.11
BVPS (CNY)	2.5	2.3	3.1	3.5	4.2	5.0
Weighted average shares (m)	2,406	2,572	2,602	2,716	2,716	2,716
Average market cap (CNYm)	21,525	28,494	31,802	52,432	52,432	52,432
Enterprise value (CNYm)	23,154	32,114	37,020	59,685	60,891	61,420

Valuation Metrics

P/E (DB) (x)	29.8	59.6	44.2	34.6	25.8	22.6
P/E (Reported) (x)	29.8	59.6	44.2	34.6	25.8	22.6
P/BV (x)	2.99	5.27	4.43	5.85	4.88	4.10
FCF Yield (%)	nm	nm	nm	nm	nm	nm
Dividend Yield (%)	0.2	0.1	0.2	0.3	0.5	0.5
EV/Sales (x)	1.2	1.7	1.4	1.7	1.4	1.2
EV/EBITDA (x)	17.5	24.8	24.7	23.1	17.4	14.9
EV/EBIT (x)	22.8	37.5	34.8	30.8	23.4	20.3

Income Statement (CNYm)

Sales revenue	19,514	18,456	26,746	35,648	44,274	50,893
Gross profit	2,666	2,767	3,502	5,044	6,395	7,349
EBITDA	1,319	1,293	1,496	2,584	3,495	4,117
Depreciation	273	363	432	645	892	1,090
Amortisation	32	75	0	0	0	0
EBIT	1,015	855	1,065	1,939	2,602	3,027
Net interest income/(expense)	-284	-218	-242	-307	-373	-420
Associates/affiliates	0	0	0	0	0	0
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	91	-108	-1	198	215	235
Profit before tax	823	530	822	1,831	2,444	2,842
Income tax expense	101	51	105	234	306	398
Minorities	0	0	-2	-2	-2	-2
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	722	478	719	1,598	2,141	2,446
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	722	478	719	1,598	2,141	2,446

Cash Flow (CNYm)

Cash flow from operations	-78	-393	186	1,621	1,623	2,464
Net Capex	-1,062	-1,168	-2,817	-3,135	-2,508	-2,633
Free cash flow	-1,140	-1,560	-2,631	-1,514	-885	-169
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-103	-72	-119	-192	-257	-294
Net inc/(dec) in borrowings	791	930	1,647	1,734	1,300	997
Other investing/financing cash flows	1,937	-359	830	-329	-64	-67
Net cash flow	1,484	-1,062	-274	-300	94	468
Change in working capital	-1,104	-1,309	-965	-622	-1,410	-1,072

Balance Sheet (CNYm)

Cash and other liquid assets	2,730	1,669	1,395	1,095	1,189	1,657
Tangible fixed assets	3,917	4,492	6,764	9,254	10,869	12,413
Goodwill/intangible assets	0	0	0	0	0	0
Associates/investments	0	0	322	322	322	322
Other assets	7,773	9,907	14,954	18,257	22,326	25,482
Total assets	14,420	16,068	23,434	28,927	34,706	39,873
Interest bearing debt	4,359	5,289	6,935	8,669	9,969	10,966
Other liabilities	3,987	4,739	8,458	10,811	13,406	15,424
Total liabilities	8,346	10,028	15,394	19,480	23,375	26,390
Shareholders' equity	6,074	6,040	8,041	9,447	11,331	13,483
Minorities	0	0	0	0	0	0
Total shareholders' equity	6,074	6,040	8,041	9,447	11,331	13,483
Net debt	1,629	3,620	5,540	7,574	8,780	9,309

Key Company Metrics

Sales growth (%)	114.8	-5.4	44.9	33.3	24.2	15.0
DB EPS growth (%)	20.3	-38.0	48.5	113.1	33.9	14.3
EBITDA Margin (%)	6.8	7.0	5.6	7.2	7.9	8.1
EBIT Margin (%)	5.2	4.6	4.0	5.4	5.9	5.9
Payout ratio (%)	5.7	6.0	6.6	12.0	12.0	12.0
ROE (%)	15.5	7.9	10.2	18.3	20.6	19.7
Capex/sales (%)	5.4	6.3	10.5	8.8	5.7	5.2
Capex/depreciation (x)	3.5	2.7	6.5	4.9	2.8	2.4
Net debt/equity (%)	26.8	59.9	68.9	80.2	77.5	69.0
Net interest cover (x)	3.6	3.9	4.4	6.3	7.0	7.2

Source: Company data, Deutsche Bank estimates



# Business update

## 2Q17 results recap

### Strong results, powered by dual cam and new Apple businesses

O-Film reported EPS of RMB0.16 (+125% YoY; +70% QoQ) and operating profit of RMB549mn (+124% QoQ; +54% YoY) on sales of RMB8.9bn (+44% QoQ; +31% YoY). Sales and operating profit came in 6% and 16% higher than our estimate, owing to rising contribution from Apple (touch panel for new iPads, as well as iPhone front cam via the acquisition of Sony's Guangzhou plant) and strong CCM business (sales up ~100% YoY, shipment up ~60%).

Figure 1: 2Q17 P&L snapshot

	2Q17	1Q17	QoQ	2Q16	YoY	2Q17 DBe	% of diff
Sales	8,928	6,193	44.2%	6,797	31.4%	8,416	6.1%
Gross profits	1,086	742	46.4%	806	34.7%	1,001	8.5%
Op. profits	549	245	123.8%	356	54.2%	475	15.6%
Non-op	(26)	(23)	15.7%	(62)	-57.2%	(34)	-23.4%
Pre-tax income	523	223	134.8%	294	77.6%	441	18.6%
Net profit	430	191	125.4%	243	76.8%	396	8.3%
EPS (RMB)	0.16	0.07	125.4%	0.09	69.5%	0.15	8.3%
<b>Margin analysis</b>							
Gross margin	12.2%	12.0%		11.9%		11.9%	
Operating margin	6.1%	4.0%		5.2%		5.6%	
Net margin	4.8%	3.1%		3.6%		4.7%	

Source: Deutsche Bank estimates, company data

### Update on three major business lines

On the CCM (compact camera module) business (~45% of 2017 sales), O-Film attributed its outperformance to 1) dual-cam shipment of 10mn in 1H17 (mostly in 2Q17), accounting for high-single digit percentage of total CCM shipments in 2Q17, up from low single digit in 1Q17; 2) continued market share gain; and 3) ASP increase due to spec upgrades and rising dual-cam contribution.

On the FPM (fingerprint module) business (~20% of sales), O-Film shipped about 100mn units in 1H17 (up ~50% YoY). Sales grew only 16% YoY due to a sharp ASP decline (as a result of product mix and price competition). However, O-Film managed to improve gross margin to 12%+ (vs 10% in 1H17).

On the cash cow – touch panel business (~33% of 2017 sales), this product line posted 6% YoY growth in 1H17, mainly driven by the commencement of shipments for new client Apple (touch panels for 9.7" new iPad).

## 3Q17 outlook and key Q&As

### Strong results, powered by dual cam and new Apple businesses

O-Film expects 3Q17 net income to fall in the range of RMB400mn (+101% YoY) to RMB630mn (+216% YoY) with GPM up slightly, powered by the



continued ramp-up in dual cam, better product mix, and improving profitability from the newly acquired Guangzhou plant (for the iPhone front camera).

On dual cam, O-Film has reiterated its 2017 shipment target of 50mn units (mainly for Chinese clients). O-Film is positive about the dual-cam outlook, and estimates dual-cam penetration for China smartphones to reach ~20% in 2017 and exceed 40% in 2018. In the long term, O-Film believes dual cam will be a standard spec even for mid/low-end smartphones (to improve image quality, reduce thickness of the device or enable basic AR features).

#### Other key Q&As

- **On automotive electronics:** O-Film highlighted that sales reached RMB128mn in 1H17 (vs almost nil in 1H16). This business line covers three types of products: 1) Human Machine Interface (touch panels for the display), 2) ADAS (cameras), and 3) electronic control units (sensors, power management, ADAS control, etc.).
- **On ADAS solution:** O-Film has developed a total solution product for the ADAS application and sampled out to clients. It comprises 6 to 8 cameras and a central control unit. ASP will be more than RMB1,500.
- **On ultrasonic FPM (finger print module):** O-Film's ultrasonic FPM (based on Qualcomm solution) has been qualified by Vivo's flagship device. Shipments could start late 2017 or early 2018.
- **On Optical FPM technology:** At this moment, this technology is relatively immature (in terms of mass production possibility), compared with the ultrasonic- or capacitive-type solutions. However, O-Film will keep working on this, as clients are still interested in this.
- **On ITO film for Apple's iPhone or iPad:** This product has been dominated by a Japanese competitor (Nissha Printing) over the past decade. O-Film has been working with Apple on this (in order to be a second source). O-Film believes it has good chance to get this business in 2018.
- **On the small-form-factor front camera:** Due to the emerging trend of the "full display" design, the space reserved for the front camera will be significantly reduced. O-Film sees a high interest in this type of product from Chinese smartphone OEMs. O-Film already has this type of product and will ship to clients by 4Q17. ASP could be 20% higher, compared with the conventional products.



# Recommendation and risks

## Maintain Hold rating, but raise TP to RMB20.5

We raise 2017-19 EPS forecasts by 7%-22% (dual cam and Apple biz). In light of higher EPS forecasts on top of a stronger growth outlook (2017-2020 EPS CAGR of 33% now vs previous estimate of 28%), we revise up TP from RMB14.4 to RMB20.5, based on 26x 2018 EPS or 0.8x PEG. Our prior TP was based on 22x 2017 EPS, also 0.8x PEG. 0.8x PEG is in line with the trading average of regional tech peers.

### Sunny as the top Buy in CCM

Despite strong 2Q17 results and positive outlook, we maintain Hold Rating on O-Film. Trading at 26x PER (0.8x PEG), we think it is fairly priced. In CCM space, we prefer Sunny Optical (Buy, CP- HKD 106.6) to O-Film.

Both companies enjoy a similar growth outlook (30%+ EPS CAGR for 2017-2020) largely driven by the same story (dual cam), but Sunny outperforms O-Film in EPS quality (positive free cash flows for Sunny since 2015 vs negative cash flows for O-Film since 2009) and ROE (Sunny's 48% vs O-Film 18% in 2017E).

### Investment risks

Downside/upside risks to our neutral calls include 1) market-share losses/gains with Chinese clients, 2) ASP erosion/increase (due to price competition or spec upgrades), and 3) forex fluctuation.

Figure 2: Earnings forecast revisions

P/L Revision (RMBm)	2016	2017E		2018E		2019E		% of change		
	(Actual)	Old	New	Old	New	Old	New	2017E	2018E	2019E
Net sales	26,746	31,902	35,648	36,102	44,274	39,000	50,893	11.7	22.6	30.5
Gross profit	3,070	4,073	4,399	4,591	5,502	4,822	6,258	8.0	19.9	29.8
Operating expense	2,005	2,265	2,460	2,462	2,900	2,613	3,232	8.6	17.8	23.7
Operating profit	1,065	1,808	1,939	2,129	2,602	2,209	3,027	7.2	22.3	37.0
Non-op gain/loss	-243	-94	-109	-122	-158	173	-185	15.2	29.3	NM
Pre-tax profit	822	1,714	1,831	2,006	2,444	2,382	2,842	6.8	21.8	19.3
Net profit	719	1,496	1,598	1,758	2,141	2,086	2,446	6.8	21.8	17.2
EPS (RMB)	0.6	0.55	0.59	0.65	0.79	0.77	0.90	6.8	21.8	17.2
Key ratio (%)										
Sales growth	44.9	19.3	33.3	13.2	24.2	8.0	15.0			
Gross margin	11.5	12.8	12.3	12.7	12.4	12.4	12.3			
Operating Margin	4.0	5.7	5.4	5.9	5.9	5.7	5.9			
Net margin	2.7	4.7	4.5	4.9	4.8	5.3	4.8			

Source: Deutsche Bank estimates, company data



Figure 3: 2017E EPS sensitivity

2017E EPS		% change of ASP Assumption								
		-12.00%	-9.00%	-6.00%	-3.00%	0.00%	3.00%	6.00%	9.00%	12.00%
% Change of Gross margin assumption	10.3%	0.25	0.27	0.30	0.33	0.36	0.39	0.42	0.44	0.47
	10.8%	0.30	0.33	0.36	0.39	0.42	0.45	0.48	0.51	0.54
	11.3%	0.35	0.38	0.41	0.44	0.47	0.51	0.54	0.57	0.60
	11.8%	0.40	0.43	0.46	0.50	0.53	0.56	0.60	0.63	0.67
	12.3%	0.45	0.48	0.52	0.55	0.59	0.62	0.66	0.69	0.73
	12.8%	0.50	0.53	0.57	0.61	0.65	0.68	0.72	0.76	0.79
	13.3%	0.55	0.59	0.63	0.66	0.70	0.74	0.78	0.82	0.86
	13.8%	0.60	0.64	0.68	0.72	0.76	0.80	0.84	0.88	0.92
	14.3%	0.65	0.69	0.73	0.78	0.82	0.86	0.90	0.94	0.99

Source: Deutsche Bank estimates

Figure 4: 2018E EPS sensitivity

2018E EPS		% change of ASP Assumption								
		-12.00%	-9.00%	-6.00%	-3.00%	0.00%	3.00%	6.00%	9.00%	12.00%
% Change of Gross margin assumption	10.3%	0.36	0.39	0.43	0.47	0.50	0.54	0.58	0.61	0.65
	10.8%	0.42	0.46	0.50	0.54	0.57	0.61	0.65	0.69	0.73
	11.3%	0.48	0.52	0.56	0.60	0.65	0.69	0.73	0.77	0.81
	11.8%	0.55	0.59	0.63	0.67	0.72	0.76	0.80	0.84	0.89
	12.3%	0.61	0.65	0.70	0.74	0.79	0.83	0.88	0.92	0.97
	12.8%	0.67	0.72	0.77	0.81	0.86	0.91	0.95	1.00	1.05
	13.3%	0.73	0.78	0.83	0.88	0.93	0.98	1.03	1.08	1.13
	13.8%	0.80	0.85	0.90	0.95	1.00	1.05	1.10	1.16	1.21
	14.3%	0.86	0.91	0.97	1.02	1.07	1.13	1.18	1.23	1.29

Source: Deutsche Bank estimates



Figure 5: Quarterly P&L highlights

(RMB mn)	1Q17	2Q17	3Q17E	4Q17E	2017E	1Q18E	2Q18E	3Q18E	4Q18E	2018E
Sales	6,193	8,928	9,850	10,677	35,648	9,321	10,097	11,619	13,238	44,274
Gross profit	742	1,086	1,227	1,344	4,399	1,128	1,232	1,467	1,675	5,502
Operating profit	245	549	587	558	1,939	447	551	713	892	2,602
Non-operating item	-23	-26	-28	-31	-109	-40	-40	-40	-40	-158
Pre-tax income	223	523	559	526	1,831	407	511	673	853	2,444
Net profit	191	430	492	486	1,598	358	409	592	781	2,141
EPS (RMB)	0.07	0.16	0.18	0.18	0.59	0.13	0.15	0.22	0.29	0.79
<b>Margin Analysis (%)</b>										
Gross margin	12.0	12.2	12.5	12.6	12.3	12.1	12.2	12.6	12.7	12.4
Operating margin	4.0	6.1	6.0	5.2	5.4	4.8	5.5	6.1	6.7	5.9
Pre-tax margin	3.6	5.9	5.7	4.9	5.1	4.4	5.1	5.8	6.4	5.5
Tax rate	14.4	17.8	12.0	7.6	12.7	12.0	20.0	12.0	8.4	12.4
<b>YoY growth (%)</b>										
Sales	47.1	31.4	23.3	37.8	33.3	50.5	13.1	18.0	24.0	24.2
Gross profit	49.5	34.7	56.7	36.5	43.3	52.0	13.4	19.6	24.7	25.1
Operating profit	69.3	54.2	82.7	197.7	82.2	82.0	0.3	21.4	59.9	34.2
Pre-tax profit	52.2	77.6	113.5	340.1	122.7	82.9	-2.2	20.4	62.0	33.5
Net profit	52.8	76.8	147.0	219.7	122.3	88.0	-4.8	20.4	60.6	33.9
<b>QoQ growth (%)</b>										
Sales	-20.1	44.2	10.3	8.4		-12.7	8.3	15.1	13.9	
Gross profit	-24.6	46.4	12.9	9.5		-16.0	9.2	19.0	14.2	
Operating profit	30.9	123.8	6.9	-4.9		-20.0	23.4	29.4	25.2	
Pre-tax profit	86.0	134.8	7.0	-5.8		-22.7	25.6	31.7	26.7	
Net profit	25.3	125.4	14.5	-1.2		-26.3	14.2	44.8	31.8	
<b>Sales breakdown</b>										
Touch panel	37.5%	33.3%	31.5%	32.2%	33.2%	30.6%	31.1%	29.3%	28.6%	29.8%
Handset CCM	40.0%	46.6%	47.4%	47.3%	45.9%	49.4%	52.7%	54.5%	55.6%	53.3%
Fingerprint sensor	20.9%	18.6%	18.4%	17.5%	18.6%	16.7%	12.8%	12.9%	12.6%	13.6%
Others	1.6%	1.6%	2.6%	3.0%	2.3%	3.4%	3.4%	3.3%	3.2%	3.3%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Deutsche Bank estimates, company data



# Appendix 1

## Important Disclosures

\*Other information available upon request

### Disclosure checklist

Company	Ticker	Recent price*	Disclosure
O-Film	002456.SZ	20.35 (CNY) 21 Aug 17	NA

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### Historical recommendations and target price: O-Film (002456.SZ)

(as of 8/21/2017)



1.	01/10/2015:	Upgrade to Hold, Target Price Change CNY18.00	Birdy Lu	4.	23/11/2016:	Hold, Target Price Change CNY33.00	Birdy Lu
2.	22/06/2016:	Hold, Target Price Change CNY28.00	Birdy Lu	5.	25/04/2017:	Hold, Target Price Change CNY36.00	Birdy Lu
3.	23/08/2016:	Hold, Target Price Change CNY31.80	Birdy Lu	6.	14/08/2017:	Hold, Target Price Change CNY14.40	Janice Cheng





### Equity rating key

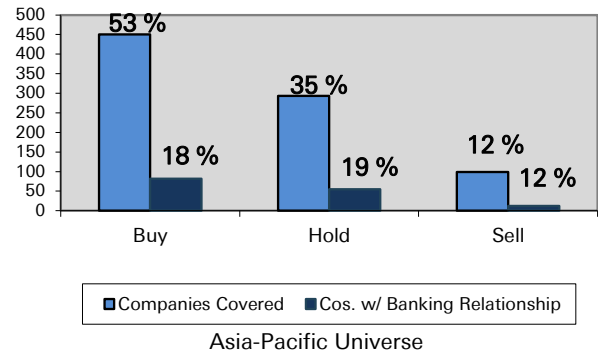
**Buy:** Based on a current 12-month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

**Sell:** Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock

**Hold:** We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

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