

Technology	Last Close	Target Price	Upside
	HK\$6.22	HK\$7.20↑	+16%

21 March 2018

O-Net Technologies (877 HK)

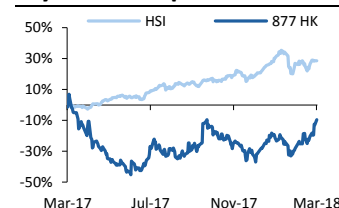
Solid growth continued as new businesses bear fruit

- ⊕ **Strong earnings growth; coating and industrial laser offset optical downturn:** Revenue grew 27% YoY to HK\$2.03bn (vs our estimates of HK\$1.94bn) with the beat from the growth of non-optical businesses such as coating and industrial laser. Coating saw strong growth in 2H17 as new capacity came online last year. Despite the sector downturn last year, the optical component business grew 15% YoY as solid demand continued for several of the company's key 100G products (amplifiers, isolators, AOC). Net profit grew 60% YoY to HK\$209m which was largely in line with the profit alert.
- ⊕ **Non-optical businesses to remain the bright spot:** While we expect recovery in the optical component industry this year as inventory digestion is largely over, we expect the non-optical side to again outperform. We expect the non-optical businesses (which include automation equipment, industrial laser, coating and LIDAR) combined to account for 25% of total revenue in 2018 (vs. 13%/21% in 2016/17). O-Net commented that the coating business is still under capacity constraint (company currently has around 40 coating machines). For the industrial laser business, the company will start to supply laser systems (rather than just laser components) which we believe could be a new growth driver.
- ⊕ **Raise estimates/TP:** We slightly raise our 2018-19 EPS estimates by 5%/3% on better-than-expected revenue outlook driven by growth from the industrial laser and smartphone surface coating businesses. Shares trade at 16x 2018E P/E, which is undemanding, in our view. Our new TP of HK\$7.20 is based on 17x average of 2018/19E EPS (previously HK\$6.50 on 18x 2018E P/E). Maintain **Buy**.

Stock Rating

BUY

1-year stock performance



Source: Bloomberg

Stock data

52w high (HK\$)	7.55
52w low (HK\$)	3.79
Market cap (HK\$ m)	4,975.10
Avg daily vol (m)	3.87
YTD change (%)	24.40
200d MA (HK\$)	5.04

Source: Bloomberg

Chris Yim

christopher.yim@bocomgroup.com
(852) 3766 1803

Xinhe Deng

xinhe.deng@bocomgroup.com
(852) 3766 1856

Financial highlights

Y/E 31 Dec	2015	2016	2017	2018E	2019E
Revenue (HK\$ m)	1,136	1,598	2,035	2,371	2,738
YoY growth (%)	37	41	27	17	15
Net profit (HK\$ m)	83	131	209	289	353
EPS (HK\$)	0.12	0.18	0.28	0.38	0.47
YoY growth (%)	100	50	56	36	22
Previous EPS (HK\$)				0.36	0.45
Change (%)				5	3
P/E (x)	51.8	34.6	22.2	16.3	13.4
BVPS (HK\$)	1.9	1.9	2.6	3.0	3.4
P/B (x)	3.2	3.2	2.4	2.1	1.8
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0

Source: Company data, BOCOM Int'l estimates

Figure 1: 2017 results beat our estimates on new business growth

2017 (HK\$ m)	Actual	Market	BOCOM
Revenue	2,035	2,063	1,941
GPM%	35.7	36.1	36.4
PTI	249	248	239
NP	209	203	197
EPS	0.28	0.27	0.26

Source: Company data, BOCOM Int'l estimates

Figure 2: We slightly raise our 2018-19 earnings forecasts

(HK\$ m)	2018E				2019E			
	Old	New	Change	Chg %	Old	New	Change	Chg %
Revenue	2,276	2,371	95	4	2,739	2,738	(0)	0
GPM (%)	36.8	36.4	-0.3*	-	36.6	36.4	-0.2*	-
OP	346	362	17	5	432	443	11	3
PTI	332	340	9	3	417	421	4	1
Net profit	278	289	11	4	345	353	8	2

Source: Company data, BOCOM Int'l estimates *ppt

Figure 3: O-Net earnings forecast

HK\$ m	1H16	2H16	1H17	2H17	1H18E	2H18E	1H19E	2H19E	2015	2016	2017	2018E	2019E
Revenue	746	852	881	1,154	1,048	1,324	1,226	1,512	1,136	1,598	2,035	2,371	2,738
YoY%	43	39	18	35	19	15	17	14	37	41	27	17	15
Optical Network	674	724	725	876	824	982	931	1,094	975	1,398	1,601	1,806	2,025
YoY%	50	38	8	21	14	12	13	11	0	43	15	13	12
Other Businesses	73	128	149	269	224	342	295	418	161	201	434	591	758
YoY%	-1	47	106	110	50	27	32	22	0	25	116	36	28
COGS	509	520	563	746	665	842	781	960	773	1,029	1,309	1,507	1,741
% of sales	68	61	64	65	64	64	64	64	68	64	64	64	64
Gross Profit	238	332	318	409	382	482	445	552	363	570	727	864	997
GPM%	31.8	39.0	36.1	35.4	36.5	36.4	36.3	36.5	31.9	35.6	35.7	36.4	36.4
OPEX	176	232	216	238	230	271	258	296	282	407	454	502	554
% of sales	23.5	27.2	24.5	20.6	22.0	20.5	21.0	19.6	24.8	25.5	22.3	21.2	20.2
Operating Profit	62	100	102	171	152	210	188	255	81	162	273	362	443
OM%	8.3	11.8	11.6	14.8	14.5	15.9	15.3	16.9	7.1	10.1	13.4	15.3	16.2
Pretax Profit	53	101	89	161	140	200	176	245	82	154	249	340	421
Taxes (benefit)	9	17	17	26	22	32	30	42	3	26	43	54	72
Net Profit	45	86	74	135	121	168	149	204	83	131	209	289	353
EPS (HK\$)	0.06	0.12	0.10	0.18	0.16	0.22	0.19	0.27	0.12	0.18	0.28	0.38	0.47
EPS growth%	50	50	67	50	56	25	24	21	100	50	56	36	22
Revenue breakdown %													
Optical Network	90	85	83	76	79	74	76	72	86	87	79	75	73
Other Businesses	10	15	17	24	21	26	24	28	14	13	21	25	27
Total	100	100	100	100	100	100	100	100	100	100	100	100	100

Source: Company data, BOCOM Int'l estimates

21 March 2018

O-Net Technologies (877 HK)



Financial Statements

Income statement (HK\$ m)					
Y/E 31 Dec	2015	2016	2017	2018E	2019E
Revenue	1,136	1,598	2,035	2,371	2,738
COGS	773	1,029	1,309	1,507	1,741
Gross Profit	363	570	727	864	997
OPEX	282	407	454	502	554
OP	81	162	273	362	443
Net interest expense	4	(6)	(24)	(22)	(22)
Equity Method	(3)	(1)	(0)	-	-
Others	-	-	-	-	-
Non-OP income	1	(8)	(24)	(22)	(22)
Pre-tax income	82	154	249	340	421
Tax	3	26	43	54	72
Net income (before minority)	79	129	206	286	350
Minority interest	(3)	(2)	(3)	(3)	(3)
Net income	83	131	209	289	353
EPS	0.12	0.18	0.28	0.38	0.47

Balance sheet (HK\$ m)					
As of 31 Dec	2015	2016	2017	2018E	2019E
Cash & cash equiv.	134	169	321	469	725
Marketable Securities	41	364	106	106	106
Account Receivables	509	647	975	1,128	1,294
Inventory	228	270	378	440	508
Others	2	37	2	2	2
Current Assets	914	1,487	1,781	2,145	2,635
Land/CIP	26	24	25	25	25
PP&E, net	699	702	916	931	901
Investment securities	-	-	-	-	-
Interest bearing asset	14	15	-	-	-
Intangible asset	65	88	83	83	83
Other fixed assets	55	170	300	278	257
Total Assets	1,773	2,487	3,104	3,461	3,900
Accounts payable	341	290	367	427	494
Short-term debt	74	684	654	654	654
Others	7	21	33	33	33
Current Liabilities	422	995	1,053	1,114	1,180
Long term debt	-	-	-	-	-
Others	16	63	18	26	46
Total Liabilities	438	1,058	1,071	1,139	1,226
Common stock	7	7	8	8	8
Retained earnings	539	669	878	1,167	1,519
Share premium	784	745	1,100	1,100	1,100
Shareholder equity	1,330	1,421	2,031	2,320	2,673
Minority interest	5	8	2	2	2
Total liabilities and equity	1,773	2,487	3,104	3,461	3,900

Source: Company data, BOCOM Int'l estimates

Cash flow statement (HK\$ m)					
Y/E 31 Dec	2015	2016	2017E	2018E	2019E
Profit before tax	82	154	249	340	421
Depreciation/Amortization	60	62	79	85	130
Changes in working capital	(5)	(304)	(391)	(201)	(220)
Forex gain/loss	-	-	-	-	-
Others	(9)	28	44	44	44
Cash flow from operations	128	(60)	(18)	269	376
Capex	(153)	(115)	(247)	(100)	(100)
Sales of tangible assets	6	18	-	-	-
Investments	64	23	258	-	-
Others	(33)	(482)	(20)	(20)	(20)
Cash flow from investing	(116)	(555)	(8)	(120)	(120)
Dividends paid	-	-	-	-	-
New share issued	(3)	-	262	-	-
Debt issuance/(repayment)	74	639	(84)	-	-
Other	(10)	18	-	-	-
Cash flow from financing	61	657	178	-	-
Other	(8)	(7)	-	-	-
Net cash flow	64	35	151	149	256
Cash at beginning	70	134	169	321	469
Cash at end	134	169	321	469	725

Financial ratios					
Y/E 31 Dec	2015	2016	2017	2018E	2019E
GPM%	31.9	35.6	35.7	36.4	36.4
OM%	7.1	10.1	13.4	15.3	16.2
EPS growth%	100.0	50.0	55.6	35.9	22.2
P/E (x)	51.8	34.6	22.2	16.3	13.4
P/B (x)	3.2	3.2	2.4	2.1	1.8
P/S (x)	0.5	0.4	0.3	0.3	0.2
EV/EBITDA (x)	29.9	22.8	14.8	11.3	8.4
Dividend yield%	0.0	0.0	0.0	0.0	0.0
Net debt/equity	(0.0)	0.4	0.2	0.1	(0.0)
ROE%	6.2	9.5	12.1	13.3	14.1
ROA%	4.8	6.0	7.4	8.7	9.5
ROIC%	5.8	7.3	8.6	10.1	11.1

21 March 2018

O-Net Technologies (877 HK)



BOCOM International

10/F, Man Yee Building, 68 Des Voeux Road Central, Central, Hong Kong

Main: (852) 3766 1899 Fax: (852) 2107 4662

Rating System

Analyst Stock Ratings:

Buy: The stock's total return is expected to **exceed** that of the corresponding industry over the next 12 months.

Neutral: The stock's total return is expected to be **in line with** that of the corresponding industry over the next 12 months.

Sell: The stock's total return is expected to be **below** that of the corresponding industry over the next 12 months.

Not-Rated: The analyst **does not have conviction** regarding the outlook of the stock's total return relative to that of the corresponding industry over the next 12 months.

Analyst Industry Views:

Outperform: The analyst expects the industry coverage universe to be **attractive** relative to the relevant broad market benchmark over the next 12 months.

Market perform: The analyst expects the industry coverage universe to be **in line with** the relevant broad market benchmark over the next 12 months.

Underperform: The analyst expects the industry coverage universe to be **unattractive** relative to the relevant broad market benchmark over the next 12 months.

Broad market benchmark for Hong Kong is **the Hang Seng Composite Index**, for China A-shares is the **MSCI China A Index**, for US-listed Chinese companies is **S&P US Listed China 50 (USD) Index**.

Analyst certification

The authors of this report, hereby declare that: (i) all of the views expressed in this report accurately reflect their personal views about any and all of the subject securities or issuers; and (ii) no part of any of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this report; (iii) no insider information/ non-public price-sensitive information in relation to the subject securities or issuers which may influence the recommendations were being received by the authors.

The authors of this report further confirm that (i) neither they nor their respective associates (as defined in the Code of Conduct issued by the Hong Kong Securities and Futures Commission) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of the report; (ii) neither they nor their respective associates serve as an officer of any of the Hong Kong listed companies covered in this report; and (iii) neither they nor their respective associates have any financial interests in the stock(s) covered in this report except for one coverage analyst who is holding shares of Shimao Property Holdings Limited.

Disclosure of relevant business relationships

BOCOM International Securities Limited, and/or its associated companies, has investment banking relationship with Bank of Communications, Guolian Securities Co. Ltd., Bank of Zhengzhou Co. Ltd., Human Health Holdings Limited, COFCO Meat Holdings Limited, Hebei Yichen Industrial Group Corporation Limited, China Aircraft Leasing Group Holdings Limited, Orient Securities Company Limited, Wuxi Construction and Development Investment Co. China Development Bank Financial Leasing Co., Ltd, Phoenix Healthcare Group Co. Ltd, Everbright Securities Company Limited, China First Capital Group Limited, Jiayuan International Group Limited, Luzhou Xinglu Water (Group) Co., Ltd., Postal Savings Bank of China Co., Ltd., China Merchants Securities Co., Limited, Shandong International Trust Co., Ltd, Guangdong Kanghua Healthcare Co., Ltd CSC Financial Co., Ltd, BOCOM International Holdings Company Limited, HPC Holdings Limited, Guotai Junan Securities Co., Ltd, Zhongyuan Bank Co., Ltd, Sichuan Energy Investment Development Co., Ltd and Light Year Holdings Limited within the preceding 12 months.

BOCOM International Global Investment Limited currently holds more than 1% of the equity securities of Orient Securities Company Limited.

BOCOM International Global Investment Limited currently holds more than 1% of the equity securities of Everbright Securities Company Limited.

BOCOM International Global Investment Limited currently holds more than 1% of the equity securities of Guolian Securities Co., Ltd.

BOCOM International Global Investment Limited currently holds more than 1% of the equity securities of Guotai Junan Securities Co., Ltd.

BOCOM International Prosperity Investment Limited currently holds more than 1% of the equity securities of China YuHua Education Corporation Ltd.

Disclaimer

By accepting this report (which includes any attachment hereto), the recipient hereof represents and warrants that he is entitled to receive such report in accordance with the restrictions set forth below and agrees to be bound by the limitations contained herein. Any failure to comply with these limitations may constitute a violation of law.

This report is strictly confidential and is for private circulation only to clients of BOCOM International Securities Ltd. This report is being supplied to you strictly on the basis that it will remain confidential. No part of this report may be (i) copied, photocopied, duplicated, stored or reproduced in any form by any means or (ii) redistributed or passed on, directly or indirectly, to any other person in whole or in part, for any purpose without the prior written consent of BOCOM International Securities Ltd.

BOCOM International Securities Ltd, its affiliates and related companies, their directors, associates, connected parties and/or employees may own or have positions in securities of the company(ies) covered in this report or any securities related thereto and may from time to time add to or dispose of, or may be interested in, any such securities. Further, BOCOM International Securities Ltd, its affiliates and its related companies may do and seek to do business with the company(ies) covered in this report and may from time to time act as market maker or have assumed an underwriting commitment in securities of such company(ies), may sell them to or buy them from customers on a principal basis and may also perform or seek to perform investment banking, advisory, underwriting, financing or other services for or relating to such company(ies) as well as solicit such investment, advisory, financing or other services from any entity mentioned in this report. In reviewing this report, an investor should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest.

The information contained in this report is prepared from data and sources believed to be correct and reliable at the time of issue of this report. This report does not purport to contain all the information that a prospective investor may require and may be subject to late delivery, interruption and interception. BOCOM International Securities Ltd does not make any guarantee, representation or warranty, express or implied, as to the adequacy, accuracy, completeness, reliability or fairness of any such information and opinion contained in this report and accordingly, neither BOCOM International Securities Ltd nor any of its affiliates nor its related persons shall be liable in any manner whatsoever for any consequences (including but not limited to any direct, indirect or consequential losses, loss of profits and damages) of any reliance thereon or usage thereof.

This report is general in nature and has been prepared for information purposes only. It is intended for circulation amongst BOCOM International Securities Ltd's clients generally and does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may receive this report. The information and opinions in this report are not and should not be construed or considered as an offer, recommendation or solicitation to buy or sell the subject securities, related investments or other financial instruments thereof.

The views, recommendations, advice and opinions in this report may not necessarily reflect those of BOCOM International Securities Ltd or any of its affiliates, and are subject to change without notice. BOCOM International Securities Ltd has no obligation to update its opinion or the information in this report.

Investors are advised to make their own independent evaluation of the information contained in this research report, consider their own individual investment objectives, financial situation and particular needs and consult their own professional and financial advisers as to the legal, business, financial, tax and other aspects before participating in any transaction in respect of the securities of company(ies) covered in this report. The securities of such company(ies) may not be eligible for sale in all jurisdictions or to all categories of investors.

This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to any law, regulation, rule or other registration or licensing requirement.

BOCOM International Securities Ltd is a subsidiary of Bank of Communications Co Ltd.