

# Sunny Optical Technology (2382 HK)

 Target price: **HKD26.70** (from HKD21.50)

 Share price (10 May): **HKD24.00** | Up/downside: **+11.2%**

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**Outperform**  
 (unchanged)

## On track for a robust 2016

- Increasing adoption of dual-cam to provide ASP upsides for HCM
- Margin expansion continues on rising contribution from HLS and VLS
- Reiterate Outperform (2) with target price raised to HKD26.7

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**What's new:** We expect Sunny to record a robust 2016 due to its strong product mix and favourable industry trends ([2016: looking like another shining year](#)). Indeed, our supply chain research underpins our positive outlook Sunny has more project wins in the high-end handset camera module (HCM) category, while its handset lens set (HLS) and vehicle lens sets (VLS) are on track for strong volume growth this year. Outperform (2).

**What's the impact: HCM: gains high-end market share, benefiting from dual-cam trend.** As discussed in [Good time to revisit](#), we expect Sunny to gain market share in the high-end HCM segment. After a slow 1Q16, Sunny's strong HCM shipments of 19.4m in April, up 22% MoM and 22% YoY, echoes our positive stance. We expect the strong volume momentum to continue in the coming months, driven by the release of new models. In addition, following Huawei P9, our checks suggest Sunny has projects win for dual-cam models from top-tier China brands arriving in 2H16-1H17. Owing to the improving product mix and the rise in dual-cam adoption, we expect Sunny's HCM ASP to grow at 3-4% in 2016-17 from a decline of 3% in 2015.

**HLS: on track for solid growth despite a muted 1H16.** Owing to the product transition in major customers, we expect HLS shipments growth to slow to 12% YoY in 1H16 (vs. 115% YoY in 2H15), but resume with a strong 34% YoY in 2H16. We expect Sunny's HLS revenue to grow at 27-31% in 2016-17 and the gross-profit contribution to rise to 17-18% in 2016-17 from 15% in 2015.

**VLS: riding on ADAS trend through market-leading position** For VLS, Sunny's Jan-April shipments of 7.3m, up 57% YoY, ahead of our estimate of 40% YoY growth. Owing to Sunny's market-leading position and the rising adoption of advanced driver assistance systems (ADAS) in smart cars equipped with multiple cameras, we forecast Sunny's VLS revenue to grow by 45-50% in 2016-17.

**Solid earnings growth with gross margin uptrend.** Given the favorable product mix, improving production yield and ASP improvement from specs upgrades, we expect Sunny's gross margin to improve to 17.4% in 2016 and 17.9% in 2017 from 16.5% in 2015. We expect Sunny's earnings to grow by 44% YoY in 2016 and 25% YoY in 2017.

**What we recommend:** We raise 2016-2017E EPS by 6-7% to factor in more optimistic gross margin assumptions. We reaffirm Outperform (2) with the 12-month target price raised to HKD26.7 (from HKD21.5), based on a 21x PER (previous: 18x), near the high point of its past-3-year trading range of 9-22x, on our revised 2016E EPS, to factor in a better earnings growth outlook. Key risk: worse-than-expected competition in HCM and HLS.

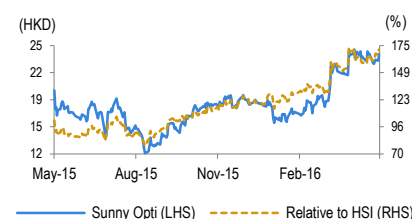
**How we differ:** We are more positive on Sunny's gross margin expansion, and as such our 2016-17E EPS are 6-7% above consensus.

### Forecast revisions (%)

Year to 31 Dec	16E	17E	18E
Revenue change	(0.5)	1.3	n.a.
Net profit change	6.6	7.4	n.a.
Core EPS (FD) change	6.6	7.4	n.a.

Source: Daiwa forecasts

### Share price performance



12-month range	12.08-24.55
Market cap (USDbn)	3.32
3m avg daily turnover (USDm)	18.61
Shares outstanding (m)	1,074
Major shareholder	Sun Xu Ltd (38.4%)

### Financial summary (CNY)

Year to 31 Dec	16E	17E	18E
Revenue (m)	13,120	15,570	17,600
Operating profit (m)	1,215	1,532	1,897
Net profit (m)	1,096	1,366	1,677
Core EPS (fully-diluted)	1.020	1.271	1.561
EPS change (%)	43.9	24.6	22.8
Daiwa vs Cons. EPS (%)	6.3	6.8	n.a.
PER (x)	19.7	15.8	12.9
Dividend yield (%)	1.5	1.9	n.a.
DPS	0.306	0.381	n.a.
PBR (x)	4.6	3.8	3.1
EV/EBITDA (x)	13.3	10.2	7.9
ROE (%)	25.6	26.1	26.2

Source: FactSet, Daiwa forecasts

**Sunny Optical: revisions to revenue and earnings forecasts**

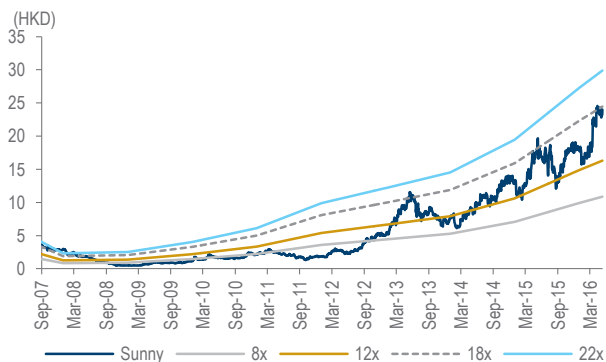
CNYm	Revised forecasts			Previous forecasts			Change		
	2016E	2017E	2018E	2016E	2017E	2018E	2016E	2017E	2018E
Revenues	13,120	15,570	17,600	13,180	15,370	n.a.	-0.5%	1.3%	n.a.
Gross profit	2,280	2,790	3,305	2,214	2,653	n.a.	3.0%	5.2%	n.a.
Op. profits	1,215	1,532	1,897	1,140	1,429	n.a.	6.6%	7.2%	n.a.
Pre-tax income	1,257	1,573	1,939	1,182	1,471	n.a.	6.3%	7.0%	n.a.
Net profit	1,096	1,366	1,677	1,028	1,272	n.a.	6.6%	7.4%	n.a.
EPS (CNY)	1.02	1.27	1.56	0.96	1.18	n.a.	6.6%	7.4%	n.a.
<b>Margins (%)</b>									
Gross margin	17.4%	17.9%	18.8%	16.8%	17.3%	n.a.			
Operating margin	9.3%	9.8%	10.8%	8.7%	9.3%	n.a.			
Pretax margin	9.6%	10.1%	11.0%	9.0%	9.6%	n.a.			
Net margin	8.4%	8.8%	9.5%	7.8%	8.3%	n.a.			

Source: Daiwa forecasts

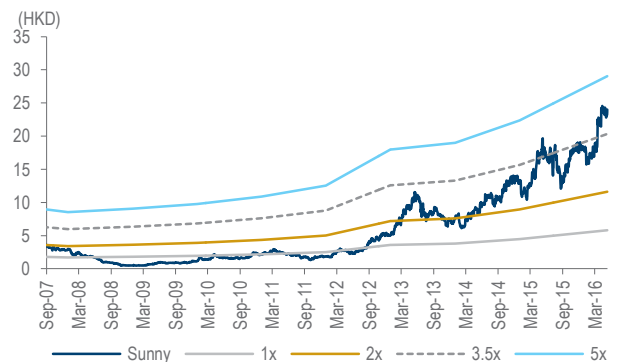
**Sunny Optical: semi-annual and annual P&L statement**

(CNYm)	2015		2016E		2015	2016E	2017E
	1H	2H	1HE	2HE			
<b>Net sales</b>	<b>4,651</b>	<b>6,045</b>	<b>5,389</b>	<b>7,731</b>	<b>10,696</b>	<b>13,120</b>	<b>15,570</b>
COGS	3,929	5,004	4,484	6,356	8,933	10,840	12,780
<b>Gross profit</b>	<b>722</b>	<b>1,041</b>	<b>905</b>	<b>1,375</b>	<b>1,763</b>	<b>2,280</b>	<b>2,790</b>
Operating costs	398	456	442	623	854	1,065	1,258
<b>Operating profit</b>	<b>324</b>	<b>586</b>	<b>463</b>	<b>752</b>	<b>909</b>	<b>1,215</b>	<b>1,532</b>
Pre-tax income	349	513	478	779	862	1,257	1,573
<b>Net income</b>	<b>308</b>	<b>454</b>	<b>416</b>	<b>680</b>	<b>762</b>	<b>1,096</b>	<b>1,366</b>
<b>Net EPS (CNY)</b>	<b>0.29</b>	<b>0.42</b>	<b>0.39</b>	<b>0.63</b>	<b>0.71</b>	<b>1.02</b>	<b>1.27</b>
<b>Operating ratios</b>							
Gross margin	15.5%	17.2%	16.8%	17.8%	16.5%	17.4%	17.9%
Operating margin	7.0%	9.7%	8.6%	9.7%	8.5%	9.3%	9.8%
Pre-tax margin	7.5%	8.5%	8.9%	10.1%	8.1%	9.6%	10.1%
Net margin	6.6%	7.5%	7.7%	8.8%	7.1%	8.4%	8.8%
<b>YoY (%)</b>							
Net revenue	21%	32%	16%	28%	27%	23%	19%
Gross profit	29%	43%	25%	32%	37%	29%	22%
Operating income	20%	90%	43%	28%	58%	34%	26%
Pre-tax income	16%	54%	37%	52%	36%	46%	25%
Net income	20%	47%	35%	50%	35%	44%	25%
<b>HoH (%)</b>							
Net revenue	1%	30%	-11%	43%			
Gross profit	-1%	44%	-13%	52%			
Operating income	5%	81%	-21%	62%			
Pre-tax income	5%	47%	-7%	63%			
Net income	-1%	48%	-8%	63%			

Source: Company, Daiwa forecasts

**Sunny Optical: 1-year-forward PER**


Source: Bloomberg, Daiwa forecasts

**Sunny Optical: 1-year-forward PBR**


Source: Bloomberg, Daiwa forecasts

## Financial summary

### Key assumptions

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Handset CCM shipment (m units)	70	97	133	187	228	266	305	329
Blended ASP of handset CCM (USD)	2.38	3.78	4.98	5.68	5.51	5.71	5.95	6.13
Vehicle lens shipment (m units)	0	0	8	11	17	24	34	48
Handset lens shipment - external + internal (m units)	32	36	26	75	302	376	464	553

### Profit and loss (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Handset CCM Revenues	1,069	2,307	4,157	6,576	7,785	9,419	11,266	12,515
Vehicle Lens Revenues	100	167	291	421	651	985	1,453	2,106
Other Revenue	1,329	1,510	1,365	1,429	2,260	2,716	2,851	2,979
<b>Total Revenue</b>	<b>2,499</b>	<b>3,984</b>	<b>5,813</b>	<b>8,426</b>	<b>10,696</b>	<b>13,120</b>	<b>15,570</b>	<b>17,600</b>
Other income	0	0	0	0	0	0	0	0
COGS	(1,976)	(3,243)	(4,846)	(7,137)	(8,933)	(10,840)	(12,780)	(14,295)
SG&A	(182)	(214)	(254)	(482)	(597)	(745)	(850)	(952)
Other op.expenses	(131)	(163)	(251)	(231)	(257)	(320)	(408)	(456)
<b>Operating profit</b>	<b>210</b>	<b>363</b>	<b>462</b>	<b>577</b>	<b>909</b>	<b>1,215</b>	<b>1,532</b>	<b>1,897</b>
Net-interest inc./(exp.)	(3)	(3)	(7)	(14)	(16)	(21)	(22)	(22)
Assoc/forex/extraord./others	33	37	49	71	(31)	65	65	65
<b>Pre-tax profit</b>	<b>240</b>	<b>397</b>	<b>504</b>	<b>634</b>	<b>862</b>	<b>1,259</b>	<b>1,575</b>	<b>1,941</b>
Tax	(38)	(58)	(64)	(73)	(99)	(161)	(208)	(262)
Min. int./pref. div./others	14	7	(0)	5	(2)	(2)	(2)	(2)
<b>Net profit (reported)</b>	<b>215</b>	<b>346</b>	<b>440</b>	<b>566</b>	<b>762</b>	<b>1,096</b>	<b>1,366</b>	<b>1,677</b>
<b>Net profit (adjusted)</b>	<b>215</b>	<b>346</b>	<b>440</b>	<b>566</b>	<b>762</b>	<b>1,096</b>	<b>1,366</b>	<b>1,677</b>
<b>EPS (reported)(CNY)</b>	<b>0.223</b>	<b>0.360</b>	<b>0.443</b>	<b>0.529</b>	<b>0.709</b>	<b>1.020</b>	<b>1.271</b>	<b>1.561</b>
<b>EPS (adjusted)(CNY)</b>	<b>0.223</b>	<b>0.360</b>	<b>0.443</b>	<b>0.529</b>	<b>0.709</b>	<b>1.020</b>	<b>1.271</b>	<b>1.561</b>
<b>EPS (adjusted fully-diluted)(CNY)</b>	<b>0.223</b>	<b>0.360</b>	<b>0.443</b>	<b>0.529</b>	<b>0.709</b>	<b>1.020</b>	<b>1.271</b>	<b>1.561</b>
<b>DPS (CNY)</b>	<b>0.071</b>	<b>0.105</b>	<b>0.121</b>	<b>0.155</b>	<b>0.208</b>	<b>0.306</b>	<b>0.381</b>	<b>n.a.</b>
<b>EBIT</b>	<b>210</b>	<b>363</b>	<b>462</b>	<b>577</b>	<b>909</b>	<b>1,215</b>	<b>1,532</b>	<b>1,897</b>
<b>EBITDA</b>	<b>298</b>	<b>472</b>	<b>609</b>	<b>792</b>	<b>1,155</b>	<b>1,527</b>	<b>1,932</b>	<b>2,351</b>

### Cash flow (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Profit before tax	240	397	504	634	862	1,259	1,575	1,941
Depreciation and amortisation	88	109	147	215	246	312	400	454
Tax paid	(38)	(58)	(64)	(73)	(99)	(161)	(208)	(262)
Change in working capital	(264)	(169)	55	(898)	609	(650)	(310)	(273)
Other operational CF items	14	7	(0)	5	(2)	(2)	(2)	(2)
<b>Cash flow from operations</b>	<b>40</b>	<b>286</b>	<b>643</b>	<b>(117)</b>	<b>1,616</b>	<b>758</b>	<b>1,455</b>	<b>1,858</b>
Capex	(112)	(265)	(286)	(465)	(351)	(650)	(400)	(400)
Net (acquisitions)/disposals	1	13	1	(62)	(64)	0	0	0
Other investing CF items	0	(38)	(26)	(178)	(60)	60	0	0
<b>Cash flow from investing</b>	<b>(111)</b>	<b>(291)</b>	<b>(311)</b>	<b>(705)</b>	<b>(475)</b>	<b>(590)</b>	<b>(400)</b>	<b>(400)</b>
Change in debt	(35)	34	392	56	167	(5)	0	0
Net share issues/(repurchases)	0	0	0	0	0	0	0	0
Dividends paid	(43)	(69)	(101)	(120)	(166)	(223)	(329)	(410)
Other financing CF items	(20)	(27)	589	(55)	(2)	0	0	0
<b>Cash flow from financing</b>	<b>(97)</b>	<b>(61)</b>	<b>879</b>	<b>(120)</b>	<b>(0)</b>	<b>(229)</b>	<b>(329)</b>	<b>(410)</b>
Forex effect/others	0	0	0	0	0	0	0	0
<b>Change in cash</b>	<b>(169)</b>	<b>(66)</b>	<b>1,211</b>	<b>(942)</b>	<b>1,141</b>	<b>(60)</b>	<b>726</b>	<b>1,048</b>
Free cash flow	(73)	20	357	(582)	1,265	108	1,055	1,458

Source: FactSet, Daiwa forecasts

## Financial summary continued ...

### Balance sheet (CNYm)

As at 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Cash & short-term investment	681	614	1,826	884	2,025	1,964	2,690	3,739
Inventory	472	748	768	896	897	1,141	1,345	1,505
Accounts receivable	627	901	1,172	2,388	3,003	3,415	4,052	4,581
Other current assets	42	4	1	36	93	52	62	70
<b>Total current assets</b>	<b>1,822</b>	<b>2,267</b>	<b>3,766</b>	<b>4,204</b>	<b>6,017</b>	<b>6,573</b>	<b>8,150</b>	<b>9,894</b>
Fixed assets	489	646	785	1,035	1,141	1,479	1,479	1,425
Goodwill & intangibles	0	0	0	0	0	0	0	0
Other non-current assets	64	89	114	354	478	418	418	418
<b>Total assets</b>	<b>2,375</b>	<b>3,002</b>	<b>4,665</b>	<b>5,594</b>	<b>7,636</b>	<b>8,470</b>	<b>10,048</b>	<b>11,738</b>
Short-term debt	62	103	489	522	683	684	684	684
Accounts payable	599	939	1,257	1,744	2,914	2,970	3,501	3,916
Other current liabilities	9	11	36	31	142	52	62	70
<b>Total current liabilities</b>	<b>671</b>	<b>1,052</b>	<b>1,782</b>	<b>2,297</b>	<b>3,739</b>	<b>3,706</b>	<b>4,248</b>	<b>4,671</b>
Long-term debt	17	0	18	36	33	36	36	36
Other non-current liabilities	7	18	6	11	19	10	10	10
<b>Total liabilities</b>	<b>694</b>	<b>1,070</b>	<b>1,805</b>	<b>2,343</b>	<b>3,791</b>	<b>3,752</b>	<b>4,294</b>	<b>4,717</b>
Share capital	98	98	105	105	105	105	105	105
Reserves/R.E./others	1,584	1,834	2,755	3,145	3,740	4,612	5,649	6,916
<b>Shareholders' equity</b>	<b>1,681</b>	<b>1,932</b>	<b>2,860</b>	<b>3,251</b>	<b>3,845</b>	<b>4,717</b>	<b>5,754</b>	<b>7,021</b>
Minority interests	0	0	0	0	0	0	0	0
<b>Total equity &amp; liabilities</b>	<b>2,375</b>	<b>3,002</b>	<b>4,665</b>	<b>5,594</b>	<b>7,636</b>	<b>8,470</b>	<b>10,048</b>	<b>11,738</b>
EV	21,011	21,100	20,293	21,285	20,303	20,368	19,641	18,593
<b>Net debt/(cash)</b>	<b>(601)</b>	<b>(512)</b>	<b>(1,319)</b>	<b>(327)</b>	<b>(1,309)</b>	<b>(1,244)</b>	<b>(1,970)</b>	<b>(3,019)</b>
<b>BVPS (CNY)</b>	<b>1.741</b>	<b>2.007</b>	<b>2.876</b>	<b>3.038</b>	<b>3.579</b>	<b>4.391</b>	<b>5.356</b>	<b>6.536</b>

### Key ratios (%)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Sales (YoY)	37.4	59.5	45.9	45.0	26.9	22.7	18.7	13.0
EBITDA (YoY)	30.3	58.1	29.1	30.0	45.9	32.2	26.5	21.7
Operating profit (YoY)	48.0	73.0	27.1	24.9	57.6	33.6	26.1	23.8
Net profit (YoY)	49.7	60.8	27.2	28.5	34.5	43.9	24.6	22.8
Core EPS (fully-diluted) (YoY)	51.7	61.3	23.1	19.4	34.0	43.9	24.6	22.8
Gross-profit margin	20.9	18.6	16.6	15.3	16.5	17.4	17.9	18.8
EBITDA margin	11.9	11.8	10.5	9.4	10.8	11.6	12.4	13.4
Operating-profit margin	8.4	9.1	7.9	6.8	8.5	9.3	9.8	10.8
Net profit margin	8.6	8.7	7.6	6.7	7.1	8.4	8.8	9.5
ROAE	13.4	19.2	18.4	18.5	21.5	25.6	26.1	26.2
ROAA	9.7	12.9	11.5	11.0	11.5	13.6	14.7	15.4
ROCE	12.3	19.1	17.1	16.1	21.7	24.3	25.7	26.7
ROIC	18.9	24.8	27.3	22.9	29.5	35.3	36.7	42.2
Net debt to equity	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Effective tax rate	15.8	14.7	12.6	11.5	11.5	12.8	13.2	13.5
Accounts receivable (days)	79.0	70.0	65.1	77.1	92.0	89.3	87.5	89.5
Current ratio (x)	2.7	2.2	2.1	1.8	1.6	1.8	1.9	2.1
Net interest cover (x)	70.4	115.7	70.0	41.3	56.8	58.3	70.9	87.8
Net dividend payout	31.8	29.2	27.3	29.3	29.3	30.0	30.0	n.a.
Free cash flow yield	n.a.	0.1	1.7	n.a.	5.9	0.5	4.9	6.7

Source: FactSet, Daiwa forecasts

## Company profile

Founded in 1984, Sunny Optical is the leading optical component manufacturer in the China technology supply chain. It develops and provides optical-related products with various applications, including instruments, components and opto-electronic modules. The company's major customers include leading China smartphone brand name makers Huawei, Lenovo and OPPO.

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## Japan

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#### Disclosure of investment ratings

Rating	Percentage of total
Buy*	66.9%
Hold**	19.7%
Sell***	13.5%

Source: Daiwa

Notes: data is for single-branded Daiwa research in Asia (ex Japan) and correct as of 31 March 2016.

\* comprised of Daiwa's Buy and Outperform ratings.

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