

# FIT Hon Teng (6088 HK)

## NDR takeaways: Focus on Belkin/400G in 2020

**Summary.** We hosted NDR with FIT mgmt. this week, and investors are interested about 1) 400G progress, 2) Belkin's profitability, and 3) manufacturing transition to Vietnam. Overall, we expect a backend loaded 2H19E driven by new products in smart accessories/ connected home/ automotive, despite headwinds in PC/mobile/comm. We expect improving product mix to continue into 2H19E and operating leverage will kick in with cost synergy in Vietnam. Maintain BUY.

- **Double-digit growth revenue guidance on track.** We expect FY19E revenue growth to come from 1) Belkin integration (+200% YoY on full-year consolidation), contributing 23% of sales, 2) auto's strong growth of 80% YoY, 3) mobile decline of 7% YoY given loss of dongle partly offset by Huawei and iPhone share gain, 4) PC to decline 15% YoY on gaming product design changes, and 5) comm. decline of 6% YoY ahead of 5G and 400G ramp.
- **Comm: 400G optical module in 2020 and copper recovery in 2H19.** Following 1H19 decline of 3% YoY due to soft socket demands with servers (Dell/HP) destocking, mgmt. expected copper demand to recover in 2H19E, while challenges in optical will persist before 400G optical modules gain traction from datacenters in 4Q19. As one of two first-movers in 400G (another is InnoLight), FIT is well-prepared to ride on rising demand for high-performance computing of Amazon with mass production in 4Q19E.
- **Belkin: new roll-outs with improving profitability.** We forecast Belkin's integration will evolve as new growth driver and achieve 10% CAGR in FY19-21E, supported by 1) well-established product portfolio with new debuts, such as Wi-Fi 6 and audio products in 2H19E, 2) improving profitability with production ramp in Vietnam to boost 70%+ in-house manufacture (vs 40% before M&A), and 3) software applications on Linksys Velop platform with enhanced features (incl. security/motion sensing/health & wellness).
- **Automobile: actively seeking M&A and stepped-up R&D efforts.** After doubled revenue in 1H19, and mgmt. expects newly acquired biz, BMW's smart key and JV with Sharp, will continue to serve as major contributors of auto segment. Looking ahead, FIT will prioritize M&A opportunities for auto biz and will strengthen R&D to capture infotainment/ADAS opportunities.
- **Backend loaded 2H19E; Belkin/400G launch as catalysts.** We estimate 2H19 sales /NP growth of 9%/23% YoY. Trading at 9.2x FY20E P/E, the stock is attractive with 14% FY19-21E EPS CAGR. Our TP of HK\$ 3.77 is based on 11x FY20E P/E. Catalysts include Belkin/400G launches in 2H19E.

### Earnings Summary

| (YE 31 Dec)          | FY17A    | FY18A    | FY19E    | FY20E    | FY21E    |
|----------------------|----------|----------|----------|----------|----------|
| Revenue (US\$ mn)    | 3,399    | 4,006    | 4,408    | 4,900    | 5,464    |
| YoY growth (%)       | 18.0     | 17.9     | 10.0     | 11.2     | 11.5     |
| Net income (US\$ mn) | 180      | 234      | 258      | 294      | 332      |
| EPS (US\$ cents)     | 3.0      | 3.5      | 3.9      | 4.4      | 5.0      |
| YoY growth (%)       | (2.1)    | 18.8     | 10.1     | 14.1     | 13.0     |
| P/E (x)              | 13.8     | 11.6     | 10.5     | 9.2      | 8.2      |
| P/B (x)              | 1.3      | 1.4      | 1.3      | 1.1      | 1.0      |
| Yield (%)            | 1.6      | 2.2      | 2.1      | 2.4      | 2.7      |
| ROE (%)              | 10       | 12       | 12       | 12       | 13       |
| Net gearing (%)      | Net cash | Net cash | Net cash | Net cash | Net cash |

Source: Company data, CMBIS estimate

### BUY (Maintain)

|               |          |
|---------------|----------|
| Target Price  | HK\$3.77 |
| Up/Downside   | +19.3%   |
| Current Price | HK\$3.16 |

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#### Stock Data

|                          |           |
|--------------------------|-----------|
| Mkt. Cap. (HK\$mn)       | 21,400    |
| Avg. 3mths t/o (HK\$mn)  | 12.84     |
| 52W High/Low (HK\$)      | 5.05/2.97 |
| Total Issued Shares (mn) | 6,743.4   |

Source: Bloomberg

#### Shareholding Structure

|                        |        |
|------------------------|--------|
| Foxconn Far East Ltd   | 76.48% |
| Franklin Resources Inc | 2.03%  |
| Lu Sung-Ching          | 1.41%  |

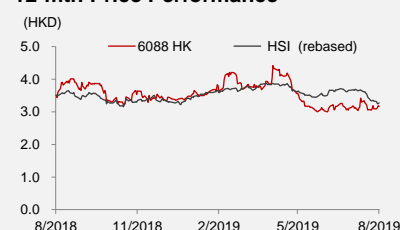
Source: HKEx

#### Share Performance

|       | Absolute | Relative |
|-------|----------|----------|
| 1-mth | 0.6%     | 12.7%    |
| 3-mth | -11.5%   | -1.9%    |
| 6-mth | -12.7%   | -4.5%    |

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

#### Auditor: Pricewaterhouse Coopers

#### Related Reports:

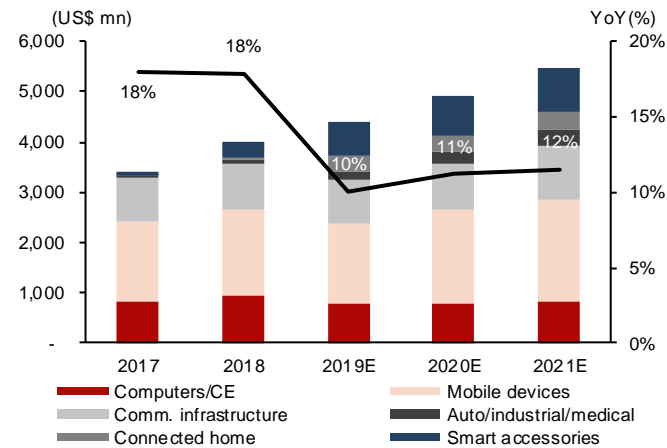
1. FIT (6088 HK, Buy) – Belkin/Vietnam synergy on track; Limited trade war impact – 14 Aug 2019
2. FIT (6088 HK, Buy) – 1H19 preview – 12 Aug 2019

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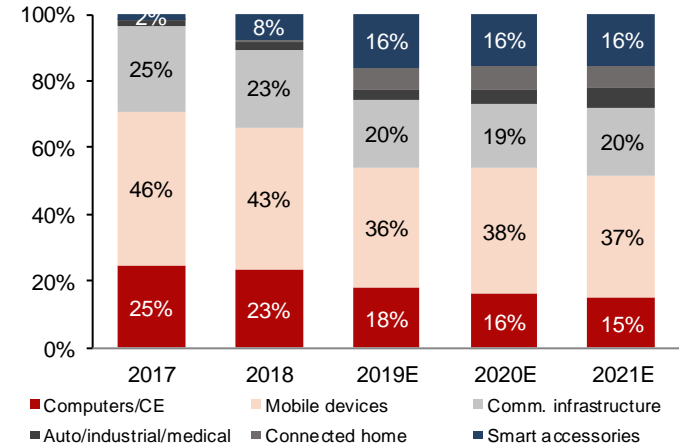
## Focus Charts

Figure 1: FIT revenue trend forecast



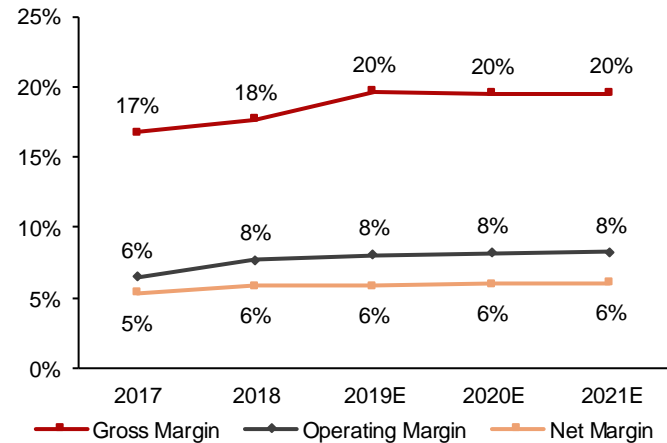
Source: Company data, CMBIS estimates

Figure 2: FIT revenue mix forecast



Source: Company data, CMBIS estimates

Figure 3: FIT margin trend forecast



Source: Company data, CMBIS estimates

Figure 4: Short-term/long-term strategy



Source: Company data, CMBIS estimates





Figure 5: Belkin's connected things products



Source: Company data, CMBIS

Figure 6: Optical modules portfolio

### Solutions for Optical Network Connectivity

|                                 |                                                                                       |          |                                       |                                      |                        |
|---------------------------------|---------------------------------------------------------------------------------------|----------|---------------------------------------|--------------------------------------|------------------------|
| <b>DATA CENTER / ENTERPRISE</b> |  | \$3,659M | 10G   40G   100G<br>SAN: 8G, 16G, 32G | 200G   400G   800G<br>SAN: 64G, 128G | GAGR (2019-2023) = 15% |
| <b>SWITCH / ROUTER</b>          |  | \$1,607M | 1G   10G   25G   40G   100G           | 50G   400G   800G                    | GAGR (2019-2023) = 12% |
| <b>CAMPUS / METRO</b>           |  | \$1,053M | 10G   40G   100G                      | 200G   400G   800G                   | GAGR (2019-2023) = 10% |
| <b>WIRELESS</b>                 |  | \$355M   | 3G   6G   9.8G                        | 25G   50G   100G                     | GAGR (2019-2023) = 21% |

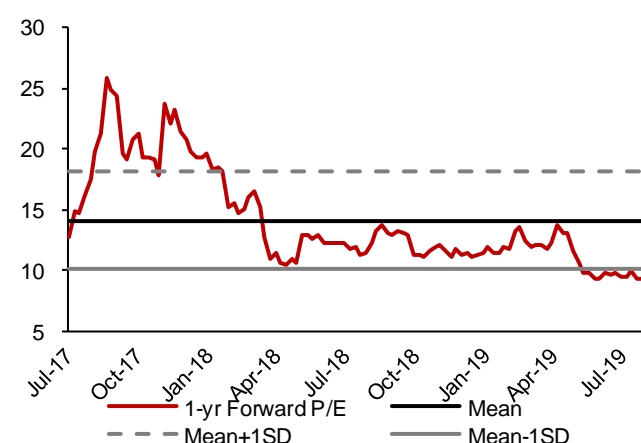
Source: Company data, CMBIS

Figure 7: Peers' valuation

| Company                     | Ticker    | Rating | Market US\$(mn) | Price (LC) | TP (LC) | Up/-side | P/E (x)     |             | P/B (x)    |            | ROE (%)     |             |
|-----------------------------|-----------|--------|-----------------|------------|---------|----------|-------------|-------------|------------|------------|-------------|-------------|
|                             |           |        |                 |            |         |          | FY19E       | FY20E       | FY19E      | FY20E      | FY19E       | FY20E       |
| <b>Global connectors</b>    |           |        |                 |            |         |          |             |             |            |            |             |             |
| TE                          | TEL US    | NR     | 29,559          | 87.99      | NA      | NA       | 15.9        | 15.2        | 2.8        | 2.7        | 17.5        | 17.5        |
| Amphenol                    | APH US    | NR     | 25,363          | 85.27      | NA      | NA       | 23.8        | 21.5        | 6.4        | 5.5        | 26.4        | 26.2        |
| Delphi                      | DLPH US   | NR     | 1,227           | 14.08      | NA      | NA       | 5.1         | 4.5         | 2.7        | 1.9        | 57.1        | 46.5        |
| Finisar                     | FNSR US   | NR     | 2,680           | 22.36      | NA      | NA       | 23.8        | 18.7        | 1.6        | 1.5        | 7.1         | 8.0         |
| Fabrinet                    | FN US     | NR     | 1,940           | 52.66      | NA      | NA       | 14.1        | 13.3        | 2.4        | -          | 17.4        | 15.8        |
| Aviat                       | 6807 JP   | NR     | 1,233           | 1418.00    | NA      | NA       | 10.1        | 11.2        | 1.0        | 0.9        | 10.4        | 8.5         |
| Hirose                      | 6806 JP   | NR     | 4,233           | 11710.00   | NA      | NA       | 23.0        | 24.3        | 1.4        | 1.4        | 6.1         | 5.7         |
| Luxshare                    | 002475 CH | NR     | 17,994          | 23.65      | NA      | NA       | 30.9        | 23.4        | 6.2        | 5.0        | 20.9        | 22.5        |
| Cheng Uei                   | 2392 TT   | NR     | 516             | 31.60      | NA      | NA       | -           | -           | -          | -          | -           | -           |
| Foxconn                     | 2354 TT   | NR     | 2,769           | 61.40      | NA      | NA       | 10.2        | 9.7         | 0.7        | 0.7        | 8.0         | 7.9         |
| Hon Hai                     | 2317 TT   | NR     | 31,645          | 71.60      | NA      | NA       | 8.9         | 8.8         | 0.8        | 0.7        | 8.7         | 8.6         |
| <b>Average</b>              |           |        |                 |            |         |          | <b>16.6</b> | <b>15.1</b> | <b>2.6</b> | <b>2.3</b> | <b>18.0</b> | <b>16.7</b> |
| <b>HK-listed components</b> |           |        |                 |            |         |          |             |             |            |            |             |             |
| FIT Hon Teng                | 6088 HK   | Buy    | 2,729           | 3.16       | 3.77    | 19%      | 10.5        | 9.2         | 1.3        | 1.1        | 12.1        | 12.2        |
| AAC Tech                    | 2018 HK   | Sell   | 5,556           | 36.05      | 43.3    | 20%      | 15.0        | 12.6        | 2.2        | 2.2        | 15.0        | 17.8        |
| Sunny Optical               | 2382 HK   | Buy    | 13,346          | 95.40      | 114.0   | 19%      | 27.3        | 19.8        | 7.9        | 6.2        | 28.8        | 31.2        |
| Tongda                      | 698 HK    | Buy    | 401             | 0.49       | 0.8     | 57%      | 3.8         | 3.2         | 0.4        | 0.4        | 11.7        | 12.8        |
| BYDE                        | 285 HK    | Hold   | 3,351           | 11.66      | 11.8    | 1%       | 11.2        | 9.9         | 1.3        | 1.2        | 12.0        | 12.3        |
| Q tech                      | 1478 HK   | Buy    | 1,090           | 7.48       | 9.5     | 27%      | 18.4        | 14.2        | 3.0        | 2.6        | 16.4        | 18.0        |
| TK Group                    | 2283 HK   | Buy    | 293             | 2.76       | 4.5     | 63%      | 6.0         | 5.0         | 1.8        | 1.8        | 29.7        | 35.7        |
| FIH                         | 2038 HK   | NR     | 974             | 0.93       | NA      | NA       | -           | -           | -          | -          | -           | -           |
| Truly                       | 732 HK    | NR     | 399             | 0.95       | NA      | NA       | 4.1         | 4.2         | 0.4        | 0.3        | 5.1         | 8.3         |
| SMIC                        | 981 HK    | NR     | 5,348           | 8.30       | NA      | NA       | 66.2        | 52.9        | 0.9        | 0.9        | 1.2         | 1.6         |
| YOFC                        | 6869 HK   | NR     | 2,420           | 12.86      | NA      | NA       | 10.4        | 9.1         | 1.0        | 1.0        | 10.2        | 9.6         |
| O-NET                       | 877 HK    | NR     | 398             | 3.80       | NA      | NA       | 9.6         | 8.1         | 1.2        | 1.0        | 12.5        | 13.3        |
| Ju Teng                     | 3336 HK   | NR     | 250             | 1.68       | NA      | NA       | 6.8         | 4.5         | 0.3        | 0.3        | 4.4         | 6.5         |
| Cowell                      | 1415 HK   | NR     | 134             | 1.26       | NA      | NA       | 8.9         | 6.2         | 0.4        | 0.4        | 5.8         | 5.8         |
| <b>Average</b>              |           |        |                 |            |         |          | <b>15.2</b> | <b>12.2</b> | <b>1.7</b> | <b>1.5</b> | <b>12.7</b> | <b>14.2</b> |

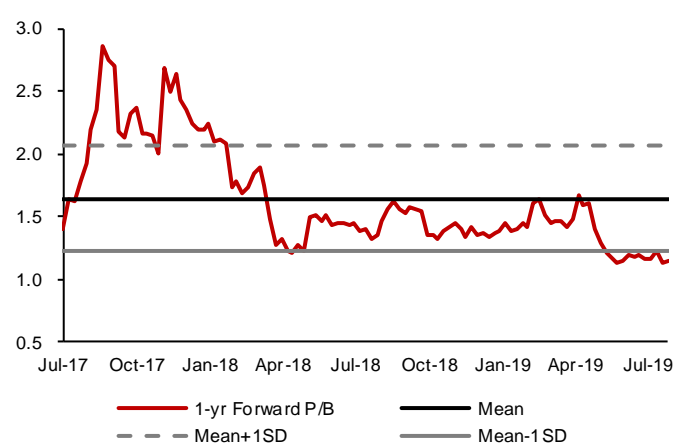
Source: Bloomberg, CMBIS

Figure 8: 12M forward P/E band



Source: Company data, CMBIS

Figure 9: 12M forward P/B band



Source: Company data, CMBIS

## Financial Summary

### Income statement

| YE 31 Dec (US\$ mn)      | FY17A      | FY18A      | FY19E      | FY20E      | FY21E      |
|--------------------------|------------|------------|------------|------------|------------|
| <b>Revenue</b>           | 3,399      | 4,006      | 4,408      | 4,900      | 5,464      |
| COGS                     | (2,829)    | (3,298)    | (3,541)    | (3,944)    | (4,395)    |
| <b>Gross profit</b>      | 569        | 708        | 867        | 956        | 1,068      |
| Selling and marketing    | (83)       | (85)       | (123)      | (137)      | (153)      |
| Administrative           | (81)       | (126)      | (163)      | (171)      | (191)      |
| R&D                      | (190)      | (227)      | (260)      | (284)      | (317)      |
| Other gain/(loss)        | 4          | 41         | 35         | 39         | 44         |
| <b>Operating profit</b>  | <b>220</b> | <b>309</b> | <b>356</b> | <b>402</b> | <b>451</b> |
| Financial cost           | 5          | 3          | (12)       | (10)       | (8)        |
| Share associate's profit | (0)        | (0)        | (0)        | (0)        | (0)        |
| <b>Pre-tax profit</b>    | <b>225</b> | <b>311</b> | <b>343</b> | <b>392</b> | <b>443</b> |
| Tax                      | (44)       | (79)       | (86)       | (98)       | (111)      |
| Minority interest        | (0)        | (1)        | 0          | 0          | 0          |
| <b>Net profit</b>        | <b>180</b> | <b>234</b> | <b>258</b> | <b>294</b> | <b>332</b> |

### Cash flow summary

| YE 31 Dec (US\$ mn)                | FY17A       | FY18A        | FY19E        | FY20E        | FY21E        |
|------------------------------------|-------------|--------------|--------------|--------------|--------------|
| <b>Profit before taxation</b>      | 225         | 311          | 343          | 392          | 443          |
| Depreciation                       | 184         | 201          | 204          | 221          | 239          |
| Change in working capital          | (223)       | 248          | (415)        | 293          | (445)        |
| Others                             | (29)        | (64)         | (74)         | (88)         | (102)        |
| <b>Net cash from operating</b>     | <b>156</b>  | <b>697</b>   | <b>59</b>    | <b>818</b>   | <b>134</b>   |
| Capex                              | (111)       | (110)        | (180)        | (180)        | (180)        |
| Other                              | 59          | (837)        | 18           | 20           | 22           |
| <b>Net cash from investing</b>     | <b>(52)</b> | <b>(947)</b> | <b>(162)</b> | <b>(160)</b> | <b>(158)</b> |
| Net borrowings                     | (119)       | 694          | 85           | 115          | 129          |
| Dividend paid                      | (41)        | (47)         | (57)         | (65)         | (73)         |
| Share issuing                      | 375         | (72)         | (30)         | (30)         | (30)         |
| Other                              | 215         | 575          | (2)          | 20           | 26           |
| <b>Net cash from financing</b>     | <b>215</b>  | <b>575</b>   | <b>(2)</b>   | <b>20</b>    | <b>26</b>    |
| <b>Net change in cash</b>          | 319         | 325          | (105)        | 678          | 2            |
| Cash at beginning of the year      | 415         | 768          | 1,065        | 960          | 1,638        |
| Exchange difference                | 34          | (27)         |              |              |              |
| <b>Cash at the end of the year</b> | <b>768</b>  | <b>1,065</b> | <b>960</b>   | <b>1,638</b> | <b>1,640</b> |

### Balance sheet

| YE 31 Dec (US\$ mn)                 | FY17A        | FY18A        | FY19E        | FY20E        | FY21E        |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|
| <b>Current assets</b>               | <b>2,412</b> | <b>2,753</b> | <b>2,964</b> | <b>3,708</b> | <b>4,087</b> |
| Cash & equivalents                  | 768          | 1,065        | 960          | 1,638        | 1,640        |
| Account receivables                 | 993          | 935          | 1,187        | 1,172        | 1,458        |
| Inventories                         | 528          | 650          | 715          | 795          | 886          |
| Short-term bank deposits            | 49           | 6            | 6            | 6            | 6            |
| <b>Non-current assets</b>           | <b>769</b>   | <b>1,557</b> | <b>1,533</b> | <b>1,492</b> | <b>1,433</b> |
| PPE                                 | 676          | 599          | 575          | 534          | 476          |
| Intangibles                         | 14           | 791          | 791          | 791          | 791          |
| Interests in associates             | 7            | 6            | 6            | 6            | 6            |
| Deferred income tax                 | 28           | 109          | 109          | 109          | 109          |
| Other non-current assets            | 44           | 52           | 52           | 52           | 52           |
| <b>Total assets</b>                 | <b>3,181</b> | <b>4,310</b> | <b>4,497</b> | <b>5,199</b> | <b>5,520</b> |
| <b>Current liabilities</b>          | <b>1,277</b> | <b>2,269</b> | <b>2,256</b> | <b>2,728</b> | <b>2,791</b> |
| ST borrowings                       | 296          | 989          | 1,074        | 1,189        | 1,318        |
| Account payables                    | 936          | 1,191        | 1,093        | 1,451        | 1,384        |
| Tax payable                         | 45           | 83           | 83           | 83           | 83           |
| Other current liabilities           | 0            | 6.025        | 6.025        | 6.025        | 6.025        |
| <b>Non-current liabilities</b>      | <b>10</b>    | <b>93</b>    | <b>93</b>    | <b>93</b>    | <b>93</b>    |
| Other payables                      | 9            | 18           | 18           | 18           | 18           |
| Deferred tax liability              | 1            | 75           | 75           | 75           | 75           |
| <b>Total liabilities</b>            | <b>1,287</b> | <b>2,362</b> | <b>2,349</b> | <b>2,822</b> | <b>2,884</b> |
| Share capital                       | 132          | 132          | 132          | 132          | 132          |
| Reserves                            | 1,762        | 1,875        | 2,076        | 2,305        | 2,564        |
| Non-controlling interests           | 0            | 13           | 13           | 13           | 13           |
| <b>Shareholders' equity</b>         | <b>1,894</b> | <b>1,947</b> | <b>2,148</b> | <b>2,377</b> | <b>2,636</b> |
| <b>Total equity and liabilities</b> | <b>3,181</b> | <b>4,310</b> | <b>4,497</b> | <b>5,199</b> | <b>5,520</b> |

### Key ratios

| YE 31 Dec                          | FY17A    | FY18A    | FY19E    | FY20E    | FY21E    |
|------------------------------------|----------|----------|----------|----------|----------|
| <b>Sales mix (%)</b>               |          |          |          |          |          |
| Consumer electronics               | 25       | 23       | 18       | 16       | 15       |
| Mobile devices                     | 46       | 43       | 36       | 38       | 37       |
| Comm. infrastructure               | 25       | 23       | 20       | 19       | 20       |
| Auto, industrial and medical       | 2        | 2        | 3        | 4        | 6        |
| Connected home                     | 0        | 1        | 7        | 7        | 7        |
| Smart accessories                  | 2        | 8        | 16       | 16       | 16       |
| <b>Growth (%)</b>                  |          |          |          |          |          |
| Revenue                            | 18.0     | 17.9     | 10.0     | 11.2     | 11.5     |
| Gross profit                       | 16.1     | 24.3     | 22.4     | 10.3     | 11.8     |
| Operating profit                   | 4.7      | 40.4     | 15.3     | 13.1     | 12.1     |
| Net profit                         | 7.1      | 29.6     | 10.1     | 14.1     | 13.0     |
| <b>Profit &amp; loss ratio (%)</b> |          |          |          |          |          |
| Gross margin                       | 16.8     | 17.7     | 19.7     | 19.5     | 19.6     |
| Operating margin                   | 6.5      | 7.7      | 8.1      | 8.2      | 8.3      |
| Net profit margin                  | 5.3      | 5.8      | 5.8      | 6.0      | 6.1      |
| <b>Balance sheet ratio</b>         |          |          |          |          |          |
| Net debt/total equity (x)          | Net cash | Net cash | Net cash | Net cash | Net cash |
| Current ratio (x)                  | 1.9      | 1.2      | 1.3      | 1.4      | 1.5      |
| Receivable turnover days           | 107      | 85       | 98       | 87       | 97       |
| Inventory turnover days            | 68       | 72       | 74       | 74       | 74       |
| Payable turnover days              | 121      | 132      | 113      | 134      | 115      |
| <b>Profitability (%)</b>           |          |          |          |          |          |
| ROE                                | 9.5      | 12.0     | 12.0     | 12.4     | 12.6     |
| ROA                                | 5.7      | 5.4      | 5.7      | 5.7      | 6.0      |
| <b>Per share data (US\$ cents)</b> |          |          |          |          |          |
| EPS                                | 2.95     | 3.50     | 3.86     | 4.40     | 4.97     |
| DPS                                | 0.66     | 0.90     | 0.85     | 0.97     | 1.09     |

Source: Company data, CMBIS estimates

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**BUY** : Stock with potential return of over 15% over next 12 months  
**HOLD** : Stock with potential return of +15% to -10% over next 12 months  
**SELL** : Stock with potential loss of over 10% over next 12 months  
**NOT RATED** : Stock is not rated by CMBIS

**OUTPERFORM** : Industry expected to outperform the relevant broad market benchmark over next 12 months  
**MARKET-PERFORM** : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months  
**UNDERPERFORM** : Industry expected to underperform the relevant broad market benchmark over next 12 months

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