

Analyst: Stanley Lau

## **Main Board H-share Listing - Research**

彩虹集團電子股份有限公司

IRICO Group Electronics Company Limited [Stock Code: 0438]
**Global Coordinator, Bookrunner,  
Lead Manager and Sponsor**

: China International Capital Corporation Limited  
(CICC)

**Sector** : Consumer discretionary

**Business** : Manufacturing of Colour Picture Tube (CPT) - a major component of television set

<b>Total share offer:</b> <u>485,294,000</u> H shares (25% of the enlarged share capital)  <b>Public Offer:</b> 48,530,000 H shares (10%) <b>Placing:</b> 436,764,000 H shares (90%)  <b>Greenshoe:</b> 72,780,000 H shares (15%)	<b><u>Business of IRICO</u></b>  IRICO is the largest CPT (Colour Picture Tube) manufacturer in China and one of the world's major CPT and CPT component manufacturers. It has the longest operating history among all Chinese CPT manufacturers, with over 20 years of experience in CPT production.  The CPT is the core component of a CRT (Cathode Ray Tube) television set, accounting for about 50% of the aggregate cost of all of the components of a CRT television set. The company manufactures small, medium and large sized CPTs 14" to 29" in size and a majority of CPT components, including glass bulbs, electron guns, deflection yokes, shadow masks and their frames as well as phosphor and frit.  IRICO's CPT production lines are located in Xianyang, Shaanxi Province. IRICO was ranked 1 <sup>st</sup> among vacuum electronic appliances enterprises in the China Electronics Industry Yearbook 2003 in categories including production and sales volumes, total output, sales revenues and export revenues for that year. The company was also ranked 22 <sup>nd</sup> among the Top Hundred Electronics and Information Technology Enterprises in terms of sales revenues in 2003 by the Ministry of Information Industry of the PRC.
<b>Price:</b> HK\$1.51 – HK\$1.73 per share <b>Market Cap.:</b> HK\$733 million – HK\$840 million  <b>Forecast FY2004 P/E:</b> 8.4x – 9.6x (pro forma) <b>Adjusted NTA per share:</b> HK\$1.25 – HK\$1.29 <b>Staffing:</b> 19,102	
<b>HK Public Offer period:</b> 8 <sup>th</sup> December 2004 - 13 <sup>th</sup> December 2004  <b>Receiving bank:</b> The Bank of East Asia  <b>Share registrar:</b> Computershare Hong Kong Investor Service Limited  <b>Listing date:</b> 20 <sup>th</sup> December 2004	

### **Major Shareholders after Listing** (Assuming the over-allotment option is not exercised)

The Group Corporation - parent company of IRICO

75.00%

75.00%

### Use of Proceeds

Net proceeds from the offer are estimated to be HK\$651 million

(Assuming the over-allotment option is not exercised, and at an issue price of HK\$1.62 each, which is the mid-point of the indicative price range)

	HK\$ million
To fund part of the investment cost for the construction of the production plant of high definition CPT of over 30" (the K Line with total investment cost of some HK\$613 million)	157
To repay the loan from its parent company - Group Corporation re. the production plant of high definition CPT of over 30"	157
To fund part of the total capital expenditures for the construction of production lines for key CPT components, including shadow masks, electron guns, large metal components and frames	162
Research and development of CPTs, CPT components and new display devices	94
Fund part of the working capital requirements of new projects (for the manufacture of 21" and 25" CPTs and components)	75
General working capital	6

### Financial Highlights

	Year ended 31 <sup>st</sup> December			6 months ended
	2001	2002	2003	30 <sup>th</sup> June 2004
	RMB in million	RMB in million	RMB in million	RMB in million
Revenue	3,293	3,999	4,270	2,419
Operating profit / (loss)	258	592	680	389
Net profit / (loss)	74	277	316	184
EPS – Basic*	RMB0.049	RMB0.185	RMB0.211	RMB0.123

\*There were 1,500,000,000 shares outstanding (100% owned by the Group Corporation)

### Breakdown of Revenue by Product Types

	Year ended 31 <sup>st</sup> December						6 months ended	
	2001		2002		2003		30 <sup>th</sup> June 2004	
	RMB in million	%	RMB in million	%	RMB in million	%	RMB in million	%
Small-sized CPT	728	22	880	22	700	16	347	14
Medium-sized CPT	2,051	62	2,503	63	2,881	68	1,833	76
Large-size CPT	373	12	341	8	307	7	23	1
CPT components and materials	141	4	275	7	382	9	216	9
Revenue	<u>3,293</u>	100	<u>3,999</u>	100	<u>4,270</u>	100	<u>2,419</u>	100

### Strengths/Opportunities

- ✓ The development of the rural market in China should drive demand growth for CRT television sets and hence CPTs.
- ✓ China's CRT television set exports should continue to grow in the coming years as China still has a low cost advantage in manufacturing.
- ✓ IRICO has the largest CPT production capacity and aggregate CPT component production capacity in the CPT industry in China. The company enjoys good economies of scale and lower production cost compared with other CPT manufacturers in China.
- ✓ The valuation of IRICO at 8.4x-9.6x FY2004 P/E is not demanding.



**Weaknesses/Threats**

- × General competition in the production of CPTs is intense and is characterized by rapid technological advances, price declines and competition from domestic and international competitors.
- × The selling prices of colour television sets have been declining over the past years due to over-production. As the CPT industry is the upstream industry of the colour television set industry, the selling prices of CPTs also declined. There is no evident that the declining trend has stabilized.
- × The high-end television sets like LCD and PDP are currently at the beginning of a fast growing period. With further upgrades in their technologies and improvement in their functions, as well as a decline in their prices, consumers would be more inclined to these new display devices. The gain in popularity of high-end devices would affect the sales volumes and gross profit margins of the traditional CRT television set industry as well as those of CPT manufacturers.
- × The concern about the IRICO's prospect has grown since its 2<sup>nd</sup>-largest client Skyworth Digital Holdings' (stock code: 0751) chairman and other officials were arrested by the Independent Commission Against Corruption on charges of misappropriation of company funds. IRICO has announced to make a provision of 18.8 million yuan to cover accounts receivables and inventory consigned with Skyworth Digital, which trimmed its 2004 profit forecast by 4% to 365.7 million yuan.

**Recommendation:    Caveat Emptor**