

**Analyst: Sabina Cheng**

## Main Board Listing – Research

A8 Digital Music Holdings Limited [Stock Code:0800] A8電媒音樂控股有限公司
**Sponsor, Sole Bookrunner and Lead Manager** : SBI E2-Capital Securities Limited

**Sector** : Mobile entertainment services

**Business** : Producing and distributing wireless digital music and non-music contents in the PRC

<b>Total share offer:</b> * <u>91,000,000</u> shares <b>(20.66 % of the enlarged share capital)</b>  <b>Public Offer:</b> 9,100,000 shares (10%) <b>Placing:</b> 81,900,000 shares (90%) <i>* Comprising 80,000,000 New Shares and 11,000,000 Sale Shares</i>	<b><u>Business of A8 Digital Music</u></b>  The group is an integrated digital music company in PRC, promoting music and non-music content through the wireless network of mobile operators like China Mobile Group and China Unicom Group and on the Internet.  The music content distributed by the Group can be in form of the original independently produced music content and other music content. The original independently produced music content is uploaded by artists to the Group's own interactive Internet UGC platform (user generated contents), <a href="http://www.a8.com">www.a8.com</a> , while other music content is licensed from international and domestic record labels. As of 31 <sup>st</sup> Dec 2007, revenues derived from this business segment accounted for 69%.  Via SMS, MMS and WAP to the mobile phone subscribers, the Group also promotes the non-music content, which includes games, wallpapers, entertainment news and jokes. As of 31 <sup>st</sup> Dec 2007, revenues derived from this business segment accounted for 31%.  The Group will strengthen its distribution capacity by further developing A8Box as a new mobile multimedia platform, to further enhance its collectability of music contents through mergers and acquisitions and to integrate its business with the introduction of 3G mobile technology.
<b>Price:</b> HK\$1.66 - HK\$2.38 per share  <b>Market Cap:</b> HK\$ 731,402,640– HK\$ 1,048,199,600  <b>Pro forma FY2007E PER:</b> 12.2X – 17.4X  <b>Adjusted NTA per share:</b> HK\$0.68 – HK\$0.81  <b>Staffing:</b> 258 (as of 31 <sup>st</sup> March 2008)	
<b>HK Public Offer period:</b> 28 <sup>th</sup> May 2008 – 2 <sup>nd</sup> June 2008  <b>Receiving banks:</b> Standard Chartered Bank (HK) Limited ICBC (Asia) Limited  <b>Principal share registrar &amp; transfer office:</b> Butterfield Fund Services (Cayman) Limited  <b>Hong Kong branch share registrar &amp; transfer office:</b> Computershare Hong Kong Investor Services Limited  <b>Listing date:</b> 12 <sup>th</sup> June 2008	

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**Shareholding Structure after Listing** (Assuming the over-allotment option is not exercised)

Prime Century Technology Limited (52.61% owned by Ever Novel Holdings Limited)	40.78%
Ever Novel Holdings Limited (100% beneficially owned by a family trust set up by Mr. Liu Xiaosong-an executive Director, the chairman and CEO of the Group, for the benefit of his family members)	8.44%
Top Result Enterprises Limited (100% beneficially owned by Ms. Cui Jingtao through a company-the Success Profit Investments Limited, the spouse of Mr Li Wei, a non-executive Director of the Group)	11.04%
Others shareholders	19.08%
Public investors	20.66%
	<u>100.00</u>

**Use of Proceeds**

Net proceeds from the offer are estimated to be HK\$132.6 million (Assuming the over-allotment option is not exercised, and at an issue price of HK\$2.02 each, being the midpoint of the indicative price range)

	HK\$ million
For potential acquisition	48.5
For further developing A8Box	27.6
For integrating its business with the introduction of 3G mobile technology	20.8
For upgrading the interactive UGC platform, <a href="http://www.a8.com">www.a8.com</a>	12.6
For promoting the UGC platform	11.1
For promoting the original independently produced music content	11.1
As additional working capital	0.9

**Financial Highlights**

	Year ended 31st December		
	2005 RMB'000	2006 RMB'000	2007 RMB'000
Revenue	233,233	268,438	285,964
Gross profit	124,960	132,275	128,729
Operating profit	41,971	44,602	60,485
<b>Profits attributable to shareholders</b>	<b>40,997</b>	<b>39,288</b>	<b>55,237</b>
Gross margin	53.6%	49.3%	45.0%
Operating margin	18.0%	16.6%	21.2%
Net margin	17.6%	14.6%	19.3%

**Revenue Breakdown**

	Year ended 31 <sup>st</sup> December					
	2005		2006		2007	
	RMB'000	% of turnover	RMB'000	% of turnover	RMB'000	% of turnover
<b>Revenue</b>						
Music-related revenue						
-Ringtones	85,798	36.8	96,395	35.8	72,206	25.3
-RBTs (ring back tones)	13,260	5.7	42,086	15.7	89,498	31.3
-IVR Music	15,706	6.7	7,160	2.7	20,748	7.2
-Others	13,032	5.6	13,618	5.1	14,990	5.2
<b>Sub-total</b>	<b>127,796</b>	<b>54.8</b>	<b>159,259</b>	<b>59.3</b>	<b>197,442</b>	<b>69.0</b>
Non-music-related revenue	105,437	45.2	109,179	40.7	88,522	31.0
<b>Total</b>	<b>233,233</b>	<b>100.0</b>	<b>268,438</b>	<b>100.0</b>	<b>285,964</b>	<b>100.0</b>



## **Strengths/Opportunities**

- ✓ **One of the largest interactive Internet UGC platforms (user generated contents) in the PRC** A8 Digital Music has one of the largest interactive Internet UGC platforms for collection of original independently produced music content in the PRC.
- ✓ **Introduction of prepaid cards** The Group is trying to expand its settlement channels to prepaid cards, which is a channel currently used by other service providers. It can launch its own prepaid card and mobile phone subscribers could purchase the prepaid card at designated locations. This can help reduce the business risk of the company.
- ✓ **Award-winner for the business** The Group got many awards from 2005 onwards, including, “2006 China high-tech, High-growth Top 50 Enterprises” by Deloitte and “2007 Zero2IPO –Venture 50” by the Zero2IPO.

## **Weaknesses/Threats**

- × **Reliance on two major mobile operators** For the year ended 31 Dec 2007, A8 Digital Music derived about 86.3% of its revenue from its collaboration with the China Mobile Group and 13.4% of its revenue from its collaboration with the China Unicom Group.
- × **Specific licences and permits needed for conducting the business** The Group has applied for one of the licenses, from the General Administration of Press and Publication of the PRC for the approval of its Internet publishing business. Such approval has not yet been granted by the relevant authority and the Group ceased its electronic bulletin services in Apr 2008 and will not engage any third party agent to provide such services.
- × **Trade receivable turnover days highly driven by the mobile operator** The increase of the accounts receivable turnover days to 81.6 days for FY2007 from 50.4 days in FY2006, was mainly due to the change of the payment policy of the China Unicom Group in respect of which the amount due from such operator will be settled in a longer period after relevant services were rendered.

**Recommendation:     Trading Buy**



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