

Analyst: Sam Ho

Main Board Listing- Research

晶門科技

Solomon Systech (International) Limited - [Stock Code: 2878]

Global Coordinator, Sponsor and Sole Bookrunner : JP Morgan

Sector : Technology

Business : Design, development and sale of display IC solutions

Total share offer: 603,582,000 shares
(25% of the enlarged share capital)

Placement: 537,186,000 shares (89%)
- 264,116,360 sale shares
- 273,069,640 new shares

IPO: 66,396,000 shares (11%)

Greenshoe: 90,536,000 shares

Price: HK\$1.60-HK\$2.05 per share

Market cap. :
HK\$3,862.9 million-HK\$4,949.4 million

Staffing: 156

Historical 2003 P/E: 21.8x-28.0x (fully-diluted)

Adjusted NAV per share: HK\$0.32-HK\$0.38

IPO commences: 25th March 2004

IPO ends: 30th March 2004

Share registrar: Tricor Investor Services

Receiving bank: Standard Chartered Bank

Listing date: 8th April 2004

Business of Solomon Systech

The Company is an independent fabless semiconductor company specializing in the design, development and sale of proprietary IC solutions that enable sophisticated display applications such as cellular phones and handheld displays. It shipped more than 70 million display ICs in 2003, of which more than 95% were display ICs developed for use in cellular phones.

Leading cellular-phone brand owners, such as Motorola and Sony Ericsson, as well as display-module makers like ALPS Electric and RiTDisplay Corporation, uses its products. Its products are also critical components of consumer electronic products such as MP3 players and handhelds.

It outsourced the manufacturing process to wafer foundries as well as packaging and testing facilities. Meanwhile, its headquarters is in Hong Kong and it also has regional offices in the PRC, Singapore, Taiwan and the US, with authorized representatives and distributors in Europe, Japan, Korea, the PRC, Southeast Asia and Taiwan.

Major Shareholders after Listing

(Assuming the over-allotment option is not exercised)

Directors	8.1%
Senior management	3.6%
Other employees	3.1%
Trustee under share award plan	1.9%
Trustee under pre-IPO loyalty plan and pre-IPO stock reward scheme	6.0%
Cardio Investments Limited under pre-IPO share purchase and pre-IPO stock reward schemes	7.2%
CIDC Funds, a Taiwan-based venture-capital firm	21.4%
Extreme Performance Limited	5.1%
Customers	7.0%
Others	11.6%
	<u>75.0%</u>

This report has been prepared solely for information purposes and we are not soliciting any action based upon it. Neither this document nor its contents shall be construed as an offer, invitation, advertisement, inducement or representation of any kind or form whatsoever. The information is based upon information, which we consider reliable, but accuracy or completeness is not guaranteed. Opinions expressed herein are subject to change without notice. At time of this report, East Asia Securities Company Limited has no position in securities of the company or companies mentioned herein.

Use of Proceeds

Net proceeds from the offer are estimated to be HK\$589 million

(Assuming the over-allotment option is not exercised, and at an issue price of HK\$1.825 each, which is the mid-point of the indicative price range)

	In percentage
To carry out product R&D works	30%
To secure production capacity and testing equipment	30%
To expand its operational infrastructure	10%
To serve as general working capital	30%

Financial Highlights

	Year ended 31 st December		
	2003 US\$'000	2002 US\$'000	2001 US\$'000
Turnover			
Sales of IC products	<u>109,339</u>	<u>60,022</u>	<u>37,511</u>
Operating profit	27,723	8,238	3,181
Net profit	<u>22,685</u>	<u>6,778</u>	<u>2,653</u>
Dividend	-	6,122	-
EPS- basic	<u>US\$1.09</u>	<u>US\$0.33</u>	<u>US\$0.13</u>

Strengths

- ✓ The global cellular-phone market is large and is still growing rapidly. According to IDC, global shipments of cellular phones is expected to grow from 421.7 million units in 2002 to 657.7 million units in 2007, representing a CAGR of 9%. The demand growth should underpin the sales for Solomon's display IC products going forward.
- ✓ The Company received the ISO 9001 certification for design, development and sales of semiconductor products in 2000, which was then upgraded to an ISO 9001:2000 certification in 2002.
- ✓ Solomon enjoyed high margins during its track record period. Gross margin increased from 32.7% in 2001 to 42.1% in 2003 due to an increase in the overall sales volume and a rise in higher-value-added display ICs. Moreover, net margin was largely improved from 7.1% in 2001 to 20.7% in 2003 amid the effect of economies of scale.
- ✓ In March 2004, the Company has formed a joint venture with Quanta Group, which is the largest notebook-computer manufacturers in the world, as well as CIDC Funds. This will help Solomon develop and diversify into multiple display ICs for large-sized TFT-LCD panels.
- ✓ Valuation of Solomon Systech (2003 P/E: 21.8x-28x) is not cheap amid the current choppy market condition. However, the Company's prospective 2004E P/E should be around 11x-16x, which is comparable to other Taiwan-listed peers (average: P/E of 13x-15x).

Weaknesses

- × Competition in the display IC product market is intense as there are many contract manufacturers (which are owned by brand owners) and independent producers.
- × Currently, more than 95% of the Company's products are ultimately developed for use in cellular phones of a few brand owners (Motorola and Sony Ericsson). Should any of these brand owners cease to use its products in their cellular phones, its financial condition may be adversely affected. In fact, there are no long-term purchase commitments with its customers and its sales were made on the basis of individual purchase orders.

Recommendation: Hit & Run