

02 Apr 2013

|                        |      |
|------------------------|------|
| Close (NTD)            | 43.5 |
| 3M target price (NTD)  | 45.4 |
| 12M target price (NTD) | 45.4 |

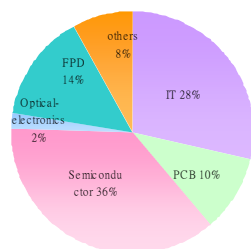
Last report date, rating, previous close

|            |         |       |
|------------|---------|-------|
| 3/25/2013  | BUY     | 42.1  |
| 1/22/2013  | BUY     | 39.45 |
| 11/16/2012 | NEUTRAL | 38.3  |

Company information

|                           |       |
|---------------------------|-------|
| Paid-in capital (NTD mn)  | 2,314 |
| Market cap (NTD bn)       | 10.1  |
| BVPS (NTD)                | 34.75 |
| FINI holding (%)          | 13.11 |
| Local fund holding (%)    | 0.06  |
| Major shareholders (%)    | 15.82 |
| Margin buying ('000 shrs) | 2,757 |

Product mix



Share performance relative to TAIEX



## Wah Lee (3010 TT)

**BUY**

**Penetration into biotech/medical business; core business to grow coupled with rising contribution from non-operating business**

### Key takeaways:

- 1Q13 revenue to beat expectation on booming shipment of FPD product and steady demand for solar product:** 1Q is typically the low season. However, JAN13 revenue recovered to NTD2.82bn on account of booming shipment of LCD timing control IC. Growth momentum of tablet and smartphone shipment resumed starting in MAR13. Therefore, the company's shipments of FPD (LCD timing control IC), engineering plastic, and PCB equipment are expected to rise in 1Q13. Topped with steady demand for solar product, 1Q13 revenue is estimated at NTD7.607bn (-2.76% QoQ and -1.65% YoY), exceeding our expectation. 1Q13 EPS is forecasted at NTD1.04.
- Growth momentum to resume for all product lines in FY13:**
  - Major growth drivers in FY13 is as follows: a) sustainable shipment of high-end plastic material applied in IT engineering; b) timing controller IC and driver IC shipments to 8.5G fabs in China after Wah Lee becomes a supplier of two major panel makers in Taiwan; c) FY13 revenue derived from touch panel controller IC is estimated to grow by >50% YoY.
  - Semiconductor segment: Wah Lee is an agent of JSR Corp's CMP slurry product. Having gained certification approval from **TSMC (2330TT)**, CMP slurry shipment commenced in small volume at present. Revenue contribution of CMP slurry is estimated to grow notably (to exceed NTD10mn per month) in FY14. The CMP slurry business is expected to become a key growth driver in FY13.
  - Green-energy segment: Shipment of optical-electronics and green energy related products is expected to improve in FY13. Furthermore, FY13 shipment of LiFePO<sub>4</sub> (Lithium iron phosphate) material is expected to increase in FY13. Wah Lee is the authorized distributor for **Tatung Fine Chemical's (4738 TT)** LiFePO<sub>4</sub> product.
- Wah Lee's non-operating income to grow in FY13:** Three subsidiaries of the Wah Lee Group are expected to go through IPO in FY13. Therefore, the company's earnings from non-operating investments are forecasted to exceed NTD500mn in FY13 from NTD420mn in FY12.
- Operation to bottom out; recommend BUY:** Wah Lee strives to penetrate into the biotech/medical market. In the short term, the company becomes the authorized distributor of pharmaceutical and chemical materials from Japan. In the mid/long term, the company is expected to penetrate into the markets of dietary supplement and medical equipment. FY12 unaudited net profit arrived at NTD981mn with EPS of NTD4.24 based on paid-in capital of NTD2.314bn. The company is estimated to distribute cash dividend of NTD2.5. FY13 EPS is forecasted at NTD5.04 given growth across all products line and rising contribution from non-operating business. Reiterate BUY with TP of NTD45.4.

| (Unit: NTD mn)         | 2011    | 2012   | 2013F  | 4Q11    | 1Q12    | 2Q12   | 3Q12   | 4Q12    | 1Q13E  | 2Q13F  | 3Q13F  | 4Q13F  |
|------------------------|---------|--------|--------|---------|---------|--------|--------|---------|--------|--------|--------|--------|
| Sales                  | 31,225  | 31,545 | 33,443 | 7,011   | 7,734   | 8,279  | 7,709  | 7,822   | 7,607  | 8,215  | 9,037  | 8,585  |
| Gross profit           | 2,822   | 2,858  | 3,049  | 424     | 684     | 755    | 780    | 639     | 685    | 752    | 831    | 781    |
| Operating profit       | 940     | 834    | 992    | 36      | 233     | 228    | 241    | 133     | 193    | 236    | 293    | 270    |
| Net profit             | 952     | 981    | 1,167  | 25      | 241     | 221    | 295    | 224     | 240    | 277    | 338    | 311    |
| EPS (NTD)              | 4.12    | 4.24   | 5.04   | 0.11    | 1.04    | 0.95   | 1.27   | 0.97    | 1.04   | 1.20   | 1.46   | 1.35   |
| Gross margin (%)       | 9.04%   | 9.06%  | 9.12%  | 6.05%   | 8.85%   | 9.12%  | 10.11% | 8.17%   | 9.00%  | 9.15%  | 9.20%  | 9.10%  |
| Operating margin (%)   | 3.01%   | 2.65%  | 2.97%  | 0.51%   | 3.01%   | 2.75%  | 3.12%  | 1.70%   | 2.53%  | 2.88%  | 3.24%  | 3.14%  |
| Net margin (%)         | 3.05%   | 3.11%  | 3.49%  | 0.36%   | 3.12%   | 2.67%  | 3.82%  | 2.87%   | 3.16%  | 3.37%  | 3.74%  | 3.63%  |
| Sales YoY/QoQ (%)      | 15.55%  | 1.03%  | 6.02%  | -5.45%  | 10.31%  | 7.05%  | -6.88% | 1.47%   | -2.76% | 8.00%  | 10.00% | -5.00% |
| Net profit YoY/QoQ (%) | -32.45% | 3.03%  | 18.93% | -88.87% | 849.40% | -8.51% | 33.61% | -23.88% | 6.95%  | 15.45% | 22.08% | -7.98% |

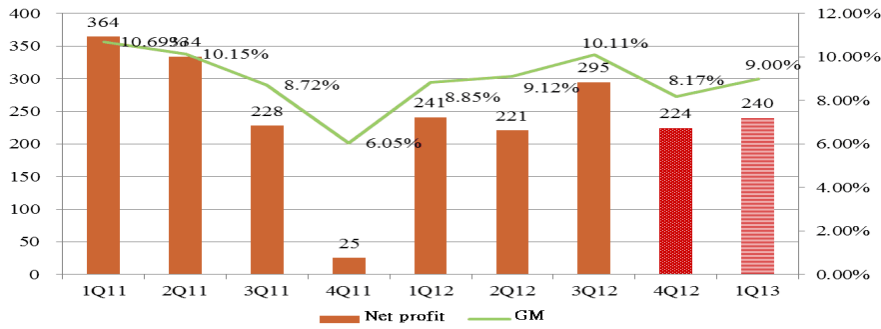
Source : TEJ; Capital Securities estimates

Note: EPS estimate is based on paid-in capital of NTD2.314bn

### ■ Contribution from non-operating businesses to rise in FY13

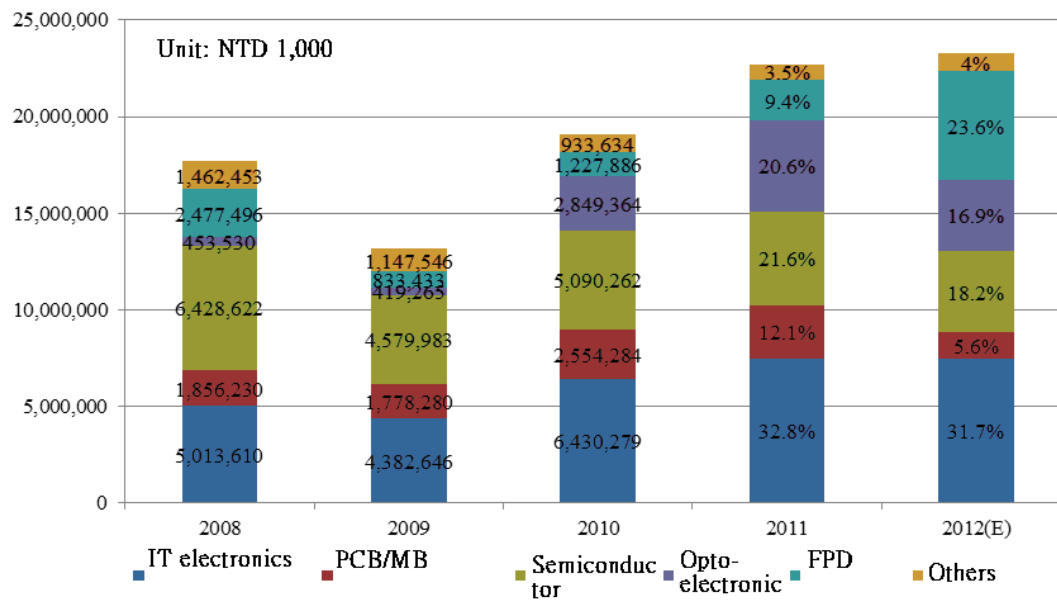
- (1) Three subsidiaries of the Wah Lee Group are expected to go through IPO in FY13. In particular, Wah Lee holds a stake in **Onano Industrial (6405 TT)**, a manufacturer of glass substrate thinning. **Chang Wah Electromaterials (8070 TT)** holds a stake in How Wei, a maker of electronic and communication components. **Wah Hong Industrial (8240 TT)** holds a stake in Jun Hong Optronics, a supplier of touch ITO film.
- (2) Onano Industrial was listed at Gre-Tai Securities Market in DEC12. Wah Lee currently has a 6% stake in Onano Industrial. Onano's FY12 EPS is estimated to exceed NTD10.0 on the back of strong demand for glass substrate thinning from optoelectronics product. Wah Lee's gain on disposal of Onano's stake is estimated at >NTD200mn.
- (3) How Wei is a supplier of power plug/socket. Revenue generated by handset and tablet related products accounts for >70% of its overall revenue while revenue derived from automobile components accounts for 30% of its overall revenue. How Wei has penetrated into Apple's supply chain. How Wei is expected to have its IPO listing in Taiwan in FY14.
- (4) Jun Hong Optronics is a supplier of touch ITO film. Jun Hong has two production lines of ITO film at the stage. Demand for high-end touch ITO film far exceeds supply of high-end ITO film. Jun Hong breaks even at present thanks to improved yield rate on collaboration with Japanese vendors.

**Exhibit 1: Quarterly profit in FY11 and FY12 (Unit: NTD mn; %)**



Source: Company; Capital Securities

**Exhibit 2: Annual revenue during FY08-12**



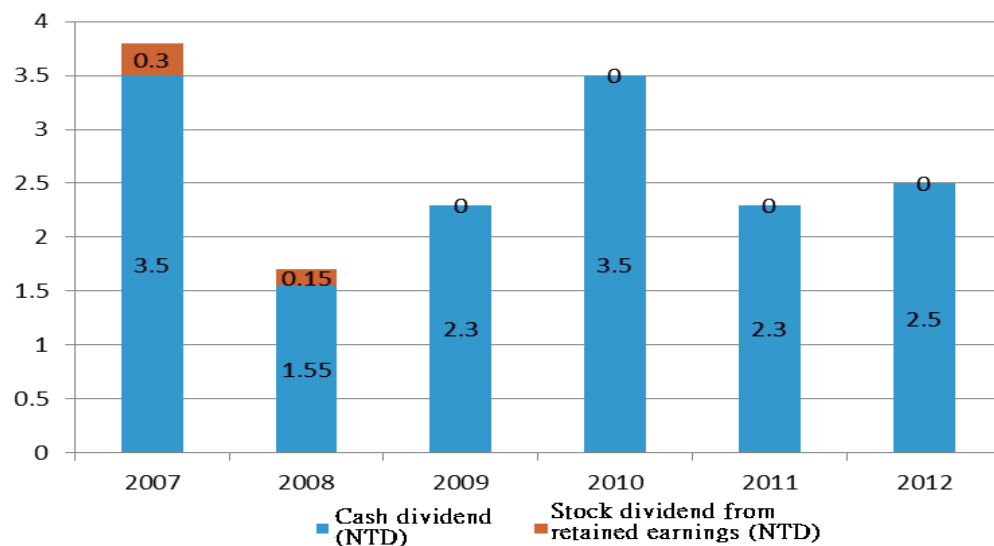
Source: Company; Capital Securities

**Exhibit 3: Wah Lee's penetration into the biotech business**

| Category                | Short term (within 1 year)  | Mid term (within 2 years)   | Long term (>2 years) |
|-------------------------|---|---|----------------------|
| Pharmaceutical business | Excipients (Japan)<br>Additive (Taiwan)   |   |                      |
| Biotech                 | Biochemical material (distributorship in discussion with Japanese suppliers)  |   |                      |
| Medical consumables     | Plastic material (Taiwan, in evaluation for distributorship)<br>Class 1 and Class 2 medical consumables (Taiwan)<br>Consumables for aesthetic medicine (Korea, in evaluation for distributorship) |   |                      |
| Medical consumables     | Medical equipment (Japan, in evaluation for distributorship)  | Surgery equipment (Japan)<br>Medical service project in China (Japan) |                      |
| Dietary supplement      | Dietary supplement (Taiwan)<br>Material and dietary supplement (Japan, in evaluation for distributorship)   |   |                      |

Source: Company; Capital Securities

**Exhibit 4: Dividends during FY07-12**



Source: TEJ; Capital Securities

**Balance sheet**

| (NTD mn)                                      | 2009          | 2010          | 2011          | 2012E         | 2013F         |
|---|---------------|---------------|---------------|---------------|---------------|
| <b>Assets</b>                                 | 15,026        | 17,491        | 18,890        | 19,828        | 22,547        |
| Current assets                                | 10,958        | 13,266        | 14,088        | 14,787        | 16,814        |
| Cash & cash equivalents                       | 2,087         | 1,552         | 2,112         | 2,217         | 2,521         |
| Accounts receivable                           | 5,602         | 7,303         | 7,793         | 7,873         | 8,346         |
| Inventories                                   | 2,456         | 3,425         | 3,229         | 3,261         | 3,455         |
| L/T investments                               | 2,739         | 2,957         | 3,486         | 3,486         | 3,486         |
| Fixed assets                                  | 916           | 903           | 898           | 1,433         | 1,933         |
| <b>Liabilities</b>                            | <b>7,784</b>  | <b>9,676</b>  | <b>10,781</b> | <b>11,317</b> | <b>12,868</b> |
| Current liabilities                           | 6,376         | 8,106         | 8,568         | 8,994         | 10,227        |
| Accounts payable                              | 3,511         | 4,513         | 4,334         | 4,377         | 4,638         |
| Long-term liabilities                         | 1,049         | 1,041         | 1,569         | 1,647         | 1,873         |
| Other liabilities                             | 359           | 529           | 644           | 676           | 768           |
| <b>Shareholders' equity</b>                   | <b>7,242</b>  | <b>7,814</b>  | <b>8,109</b>  | <b>8,512</b>  | <b>9,678</b>  |
| Share capital                                 | 2,344         | 2,314         | 2,314         | 2,314         | 2,314         |
| Retained earnings                             | 2,126         | 2,766         | 2,767         | 3,170         | 4,336         |
| <b>Liabilities &amp; shareholders' equity</b> | <b>15,026</b> | <b>17,491</b> | <b>18,890</b> | <b>19,828</b> | <b>22,547</b> |

Source: TEJ; Capital Securities

**Cash flow statement**

| (NTD mn)  | 2009         | 2010         | 2011         | 2012E        | 2013F        |
|---|--------------|--------------|--------------|--------------|--------------|
| <b>Operating cash flows</b>                     | 2,540        | -390         | 604          | 952          | 718          |
| Net income                                      | 810          | 1,410        | 952          | 981          | 1,167        |
| Depreciation & amortization                     | 107          | 106          | 103          | 103          | 164          |
| Increase in working capital                     | 1,105        | 578          | 359          | 794          | 794          |
| Other operating cash flows                      | 517          | -2,484       | -811         | -926         | -1,407       |
| <b>Investing cash flows</b>                     | -483         | -43          | -607         | -607         | -607         |
| Capital expenditures                            | -6           | 36           | -593         | -593         | -593         |
| Free cash flow                                  | 2,534        | -354         | 11           | 359          | 125          |
| Other investing cash flows                      | -477         | -79          | -14          | -14          | -14          |
| <b>Financing cash flows</b>                     | -1,478       | 28           | 422          | -241         | 193          |
| Dividends paid                                  | -352         | -532         | -810         | -578         | 0            |
| Other financing cash flows                      | -1,126       | 560          | 1,232        | 338          | 193          |
| <b>Increase in cash &amp; cash equivalents</b>  | <b>543</b>   | <b>-535</b>  | <b>560</b>   | <b>105</b>   | <b>304</b>   |
| <b>Cash &amp; cash equivalents - year begin</b> | <b>1,544</b> | <b>2,087</b> | <b>1,552</b> | <b>2,112</b> | <b>2,217</b> |
| <b>Cash &amp; cash equivalents - year end</b>   | <b>2,087</b> | <b>1,552</b> | <b>2,112</b> | <b>2,217</b> | <b>2,521</b> |

Source: TEJ; Capital Securities

**Income statement**

| (NTD mn)                | 2009         | 2010         | 2011         | 2012E        | 2013F        |
|-------------------------|--------------|--------------|--------------|--------------|--------------|
| <b>Revenue</b>          | 19,226       | 27,023       | 31,225       | 31,545       | 33,443       |
| Cost of sales           | 16,910       | 23,823       | 28,403       | 28,687       | 30,394       |
| <b>Gross profit</b>     | <b>2,316</b> | <b>3,200</b> | <b>2,822</b> | <b>2,858</b> | <b>3,049</b> |
| Operating expenses      | 1,639        | 2,028        | 1,882        | 2,023        | 2,057        |
| <b>Operating profit</b> | <b>677</b>   | <b>1,172</b> | <b>940</b>   | <b>834</b>   | <b>992</b>   |
| <b>EBITDA</b>           | <b>1,228</b> | <b>1,967</b> | <b>1,524</b> | <b>1,432</b> | <b>1,629</b> |
| Non-operating items     | 370          | 640          | 410          | 481          | 450          |
| Pre-tax profit          | 1,047        | 1,812        | 1,350        | 1,315        | 1,442        |
| Income taxes            | 237          | 402          | 398          | 334          | 275          |
| Net income              | 810          | 1,410        | 952          | 981          | 1,167        |
| Basic EPS (NTD)         | 3.50         | 6.09         | 4.12         | 4.24         | 5.04         |
| Diluted EPS (NTD)       | 3.50         | 6.09         | 4.12         | 4.24         | 5.04         |

Source: TEJ; Capital Securities

**Ratio analysis**

| (NTD mn)                             | 2009   | 2010   | 2011   | 2012F  | 2013F  |
|--------------------------------------|--------|--------|--------|--------|--------|
| <b>Growth analysis (%)</b>           |        |        |        |        |        |
| Revenue                              | -20.8% | 40.6%  | 15.5%  | 1.0%   | 6.0%   |
| Gross profit                         | -22.6% | 38.2%  | -11.8% | 1.3%   | 6.7%   |
| Operating profit                     | -35.9% | 73.1%  | -19.8% | -11.2% | 18.9%  |
| Net income                           | 9.3%   | 74.0%  | -32.4% | 3.0%   | 18.9%  |
| <b>Profitability analysis (%)</b>    |        |        |        |        |        |
| Gross margin                         | 12.1%  | 11.8%  | 9.0%   | 9.1%   | 9.1%   |
| EBITDA margin                        | 6.4%   | 7.3%   | 4.9%   | 4.5%   | 4.9%   |
| Operating margin                     | 3.5%   | 4.3%   | 3.0%   | 2.6%   | 3.0%   |
| Net margin                           | 4.2%   | 5.2%   | 3.0%   | 3.1%   | 3.5%   |
| Return on asset                      | 6.2%   | 9.3%   | 5.9%   | 5.1%   | 5.5%   |
| Return on equity                     | 12.2%  | 19.5%  | 12.7%  | 11.8%  | 12.8%  |
| <b>Debt &amp; liquidity analysis</b> |        |        |        |        |        |
| Debt ratio                           | 51.8%  | 55.3%  | 57.1%  | 57.1%  | 57.1%  |
| Debt-to-equity ratio                 | 107.5% | 123.8% | 133.0% | 133.0% | 133.0% |
| Current ratio                        | 171.9% | 163.7% | 164.4% | 164.4% | 164.4% |
| <b>Activity analysis</b>             |        |        |        |        |        |
| Inventory days                       | 64.8   | 45.1   | 42.8   | 41.3   | 40.3   |
| Accounts receivable days             | 99.4   | 87.2   | 88.2   | 90.6   | 88.5   |

Source: TEJ; Capital Securities

**Quarterly income statement**

| (NTD mn)                    | 1Q11   | 2Q11    | 3Q11    | 4Q11    | 1Q12    | 2Q12    | 3Q12   | 4Q12    | 1Q13E   | 2Q13F  | 3Q13F  | 4Q13F   |
|-----------------------------|--------|---------|---------|---------|---------|---------|--------|---------|---------|--------|--------|---------|
| Sales                       | 8,588  | 8,210   | 7,415   | 7,011   | 7,734   | 8,279   | 7,709  | 7,822   | 7,607   | 8,215  | 9,037  | 8,585   |
| Gross profit                | 918    | 833     | 647     | 424     | 684     | 755     | 780    | 639     | 685     | 752    | 831    | 781     |
| Operating expenses          | 517    | 487     | 490     | 388     | 452     | 527     | 539    | 506     | 492     | 515    | 538    | 512     |
| Operating profit            | 401    | 346     | 156     | 36      | 233     | 228     | 241    | 133     | 193     | 236    | 293    | 270     |
| Non-operating income        | 140    | 162     | 170     | 40      | 112     | 121     | 186    | 184     | 120     | 120    | 140    | 130     |
| Non-operating expenses      | 19     | 21      | 34      | 27      | 37      | 28      | 40     | 17      | 20      | 10     | 10     | 20      |
| Pre-tax profit              | 522    | 487     | 293     | 48      | 307     | 321     | 387    | 300     | 293     | 346    | 423    | 380     |
| Net profit                  | 364    | 334     | 228     | 25      | 241     | 221     | 295    | 224     | 240     | 277    | 338    | 311     |
| Paid-in capital             | 231    | 231     | 231     | 231     | 231     | 231     | 231    | 231     | 231     | 231    | 231    | 231     |
| EPS (NTD)                   | 1.57   | 1.44    | 0.99    | 0.11    | 1.04    | 0.95    | 1.27   | 0.97    | 1.04    | 1.20   | 1.46   | 1.35    |
| <b>Operating efficiency</b> |        |         |         |         |         |         |        |         |         |        |        |         |
| Gross margin (%)            | 10.69% | 10.15%  | 8.72%   | 6.05%   | 8.85%   | 9.12%   | 10.11% | 8.17%   | 9.00%   | 9.15%  | 9.20%  | 9.10%   |
| Operating margin (%)        | 4.67%  | 4.22%   | 2.11%   | 0.51%   | 3.01%   | 2.75%   | 3.12%  | 1.70%   | 2.53%   | 2.88%  | 3.24%  | 3.14%   |
| Net margin (%)              | 4.24%  | 4.07%   | 3.08%   | 0.36%   | 3.12%   | 2.67%   | 3.82%  | 2.87%   | 3.16%   | 3.37%  | 3.74%  | 3.63%   |
| <b>QoQ (%)</b>              |        |         |         |         |         |         |        |         |         |        |        |         |
| Sales                       | 20.67% | -4.41%  | -9.68%  | -5.45%  | 10.31%  | 7.05%   | -6.88% | 1.47%   | -2.76%  | 8.00%  | 10.00% | -5.00%  |
| Operating profit            | 94.91% | -13.76% | -54.78% | -76.96% | 545.10% | -2.03%  | 5.58%  | -44.57% | 44.52%  | 22.66% | 23.90% | -7.93%  |
| Pre-tax profit              | 90.32% | -6.73%  | -39.81% | -83.47% | 534.85% | 4.41%   | 20.44% | -22.35% | -2.50%  | 18.34% | 22.08% | -10.22% |
| Net profit                  | 73.76% | -8.25%  | -31.70% | -88.87% | 849.40% | -8.51%  | 33.61% | -23.88% | 6.95%   | 15.45% | 22.08% | -7.98%  |
| <b>YoY (%)</b>              |        |         |         |         |         |         |        |         |         |        |        |         |
| Sales                       | 43.50% | 17.69%  | 6.76%   | -1.49%  | -9.95%  | 0.85%   | 3.97%  | 11.57%  | -1.65%  | -0.77% | 17.22% | 9.75%   |
| Operating profit            | 48.53% | -5.18%  | -52.78% | -82.49% | -42.04% | -34.15% | 53.74% | 269.87% | -17.14% | 3.75%  | 21.75% | 102.22% |
| Pre-tax profit              | 12.99% | -2.47%  | -49.17% | -82.34% | -41.09% | -34.06% | 31.95% | 519.90% | -4.80%  | 7.90%  | 9.37%  | 26.46%  |
| Net profit                  | -0.34% | -11.11% | -50.20% | -87.88% | -33.79% | -33.98% | 29.16% | 783.41% | -0.48%  | 25.59% | 14.75% | 38.72%  |

Source: TEJ; Capital Securities

| <b>STOCK RATING</b>   |
|---|
| <b>STRONG BUY</b><br>Based on the last closing price prior to our initial STRONG BUY recommendation, our 3-month target price implies upside exceeding or equal to 35%.   |
| <b>BUY</b><br>Based on the last closing price prior to our initial BUY recommendation, our 3-month target price implies upside between 15% and 35%.   |
| <b>NEUTRAL</b><br>We are unable to issue investment recommendation based on the company's current fundamentals. We expect the share price to consolidate in the near term and recommend investors to look for a better entry point. |

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