

Aug 21, 2013
Company Note

Simmtech (036710.KQ)

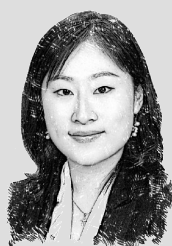
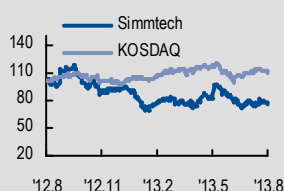
Buy (initiate)

TP W11,000 (initiate)
CP ('13/08/20) W8,360

Sector Semiconductor

Kospi 1,887.85
Kosdaq 537.57
Market cap (common) US\$240.13mn
Outstanding shares (common) 322,000
52W high ('13/07/18) W12,950
low ('12/17/12) W7,510
Dividend yield (2012) 1.94%
Foreign ownership 3.2%

Price trend



Analyst - Sophia Kim
822)768-7630, sophia.kim@wooriwm.com

RA - Soohyung Kim
822)768-7034, soohyung.kim@wooriwm.com

Preparing for growth of mid-end smartphone market

Initiate coverage at Buy with a target price of W11,000

- We initiate coverage on Simmtech with a Buy rating and target price of W11,000.
- Amid changes in demand being witnessed in the front-end industry, the company has carried out structural changes (ie, converted a production line) and begun supplying FC-CSP. Given these developments, we initiate coverage on Simmtech, forecasting that the play will register strong sales growth going forward.
- Our RIM-derived target price assumes a market risk premium of 7.0% and a beta of 1.3, with a COE of 14.2%. Possessing 32% upside to the firm's current share price, our target price is equivalent to a 2014F P/E of 10.8x.

To benefit from mid-end smartphone market growth: 1) PC module line converted to mobile substrate production line

- In 2Q13, Simmtech completed the conversion of part of its PC module PCB production line into a mobile package substrate line, raising its package substrate production capacity from 70,000m²/month to 82,000m²/month.
- The company also holds a 25% share of the global MCP market (the substrate is used for smartphone basebands, memory, and general chips).
- With smartphone shipments growing, the firm's MCP sales should continue to rise (MCP sales to climb 45% y-y in 2012, 47% y-y in 2013E, and 50% y-y in 2014F).

To benefit from mid-end smartphone market growth: 2) Begins supplying FC-CSP to Chinese smartphone chipmaker

- Simmtech has started supplying FC-CSP to a Chinese smartphone application processor (AP) chipmaker, with full-fledged sales growth likely to emerge from 4Q13. We predict that the company will announce 2013 and 2014 sales of W14bn and W35bn, respectively.
- With Chinese mid-end smartphone demand expected to increase sharply going forward, Chinese AP makers will likely diversify their vendors, creating an opportunity for Simmtech to expand its FC-CSP sales.

Earnings forecasts (IFRS non-consolidated basis)

(Units: Wbn, won, x, %)

	2012	2013E	2014F	2015F
Sales	631	550	631	725
Operating profit	46	-4	48	61
EBITDA	79	31	82	97
Net profit	25	-15	33	43
EPS	792	-471	1,022	1,340
P/E	13.0	N/A	8.2	6.2
P/B	1.5	1.4	1.2	1.0
EV/EBITDA	5.7	13.7	4.9	3.9
ROE	12.6	-7.4	15.9	18.1

Source: Woori I&S Research Center estimates

Initiate coverage on Simmtech with RIM-based target price of W11,000

**Target price
equivalent to 2014
P/E of 10.8x, offering
32% upside**

We initiate coverage on Simmtech, presenting a Buy recommendation and a target price of W11,000. Our RIM-derived target (assumes a market risk premium of 7.0%, a risk free rate of 4.0%, and beta of 1.3, with a COE of 13.1%) is equivalent to a 2014 P/E of 10.8x and a P/B of 1.6x, and offers 32% upside potential from the firm's current share price.

RIM valuation												(Units: Wbn, won)
	2013E	2014F	2015F	2016F	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F
Net profit	-15	33	43	51	59	69	80	91	105	121	139	160
Shareholder's equity	193	220	257	301	354	417	487	566	656	756	868	994
Forecast ROE (FROE)	-7.4%	15.9%	18.1%	18.2%	18.1%	17.9%	17.6%	17.4%	17.2%	17.1%	17.1%	17.2%
Spread (FROE-COE)	-20.5%	2.8%	5.0%	5.1%	5.0%	4.8%	4.5%	4.3%	4.1%	4.0%	4.0%	4.1%
Residual income	-42	6	12	14	16	19	20	22	25	28	33	38
Cost of equity (COE)	13.1%											
Beta	1.3											
Market risk premium (Rm-Rf)	7.0%											
Risk-free rate (Rf)	4.0%											
Beginning shareholder's equity	215											
PV of forecast period RI	57											
PV of continuing value	42											
Equity value (C+P)	314											
No. of shares (common, mn)	32,200											
		12M TP										
Fair price (C)		11,039										
Current price (C)		8,360										
Upside (-downside)		32.0%										
Implied P/B (x)		1.8										
Implied P/E (x)		21.0										

Note: RIM (Residual Income Model) is a cash flow approach that yields a fair shareholder value (value of equity) by adding shareholders' equity and present value of residual income (meaning income excluding cost of equity).

Value of equity = shareholders' equity + sum of present value of future residual income

*** Residual income (RI_t) = NP (t) – shareholders' equity (t-1) * cost of equity (t) = shareholders' equity (t-1) * (ROE_t - COE_t)**

Woori I&S uses RIM as our primary valuation model as RIM is an objective model that minimizes subjectivity of valuation indicators while producing same results as DDM (dividend discount model) and DCF.

Market risk premium assessment guidelines

	Mega cap	Large cap	Mid cap	Small cap
Criteria	Market cap of W10tn or higher + credit rating of 'AAA' or higher	Market cap of W1~10tn + credit rating of 'A0' or higher	Market cap of W200bn-1tn + credit rating of 'BBB+' or higher	Market cap of less than W200bn + credit rating of 'BBB-' or higher
Risk premium	5.2%	6.0%	7.0%	8.0%

* Risk free rate = 4.0% (standardized)

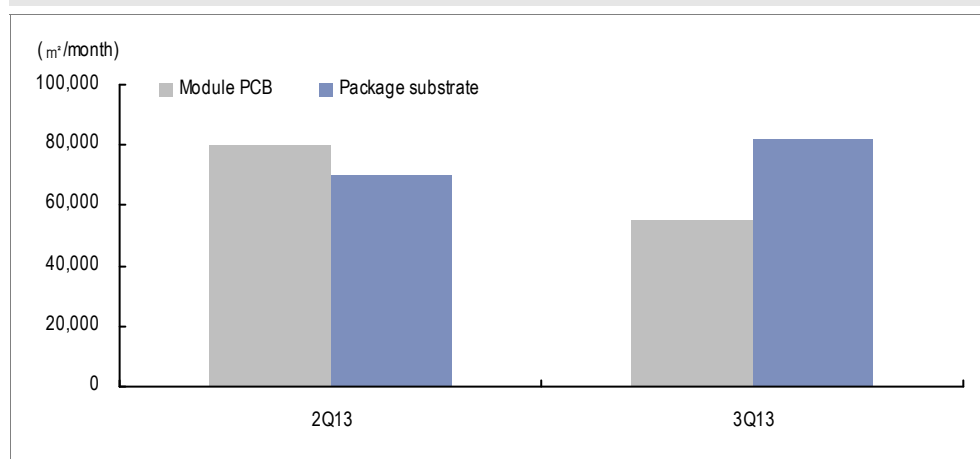
Completion of line conversion to boost mobile package sales growth

In 2Q13, Simmtech completed the conversion of part of its PC module PCB production line into a mobile package substrate line, raising its package substrate production capacity from 70,000m²/month to 82,000m²/month, and lowering its module PCB capacity from 80,000m²/month to 55,000m²/month. Although PC demand has continued to decline since 3Q12, smartphone demand should continue to accelerate (compared to demand for other IT products) despite the recent slowdown in high-end smartphone consumption. Accordingly, following its recent line conversion, we expect Simmtech's mobile-related sales (MCP, FC-CSP, CSP) to expand going forward.

Plant restored following fire in February; operations to normalize from 3Q13

In 3Q12, reflecting changes in downstream industry conditions, the company decided to convert part of its module PCB line at the Cheongju plant #1 into a mobile package substrate line. However, the process took almost a year to complete due to a fire at the line in Feb 2013. Of note, Simmtech completed equipment installation for the converted line and secured customer approval for its new product offerings in Jun 2013. Although the firm's portion of variable costs rose due to increased outsourcing in 1Q13 and 2Q13 (following the fire), its variable costs should decline as operations normalize from 3Q13. As such, we expect Simmtech to turn to profit in 3Q13. Of note, the company recorded fire-related losses of W2.0bn in 1Q13, with further losses of W3.0bn expected to be booked in 3Q13.

Line conversion (module PCB → package substrate)



Source: Simmtech

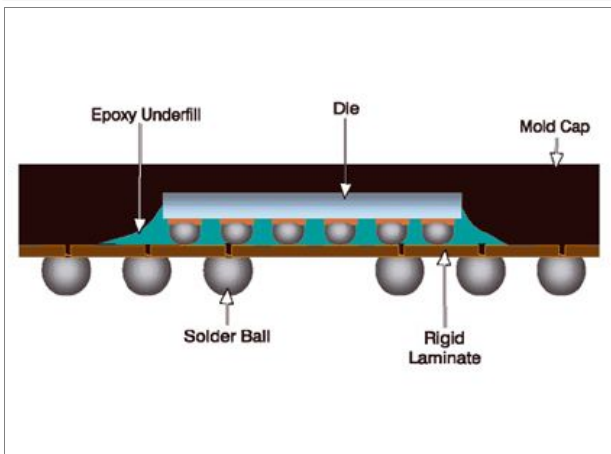
Begins supplying FC-CSP to Chinese AP makers

FC-CSP—a packaging substrate for mobile APs and basebands—is a high value-added product, costing 2~6 times more than MCP (substrate for general handset chips). Simmtech began mass-producing FC-CSP from 2013, and currently supplies FC-CSP (for a chip that combines dual-core APs and basebands) to Chinese chipmakers, which in turn produce chips for low- and mid-end smartphones. Simmtech is also developing FC-CSP for quad-core APs. In fact, we expect the company to gain product approval from Qualcomm by as early as end-2013, with supply likely to begin from 2014.

Strong low/mid-end smartphones sales to boost Simmtech's FC-CSP earnings

Currently, the global FC-CSP market is dominated by only a few players (including SEMCO (Korea), Ibiden (Japan), Unimicron, and Kinsus (Taiwan)). However, amid growing sales of low- and mid-end smartphones, demand is likely to rise for cheaper FC-CSP. In our view, as existing market leaders are unlikely to add low- and mid-end FC-CSP products to their portfolios (due to possible margin deterioration), we expect AP and baseband chipmakers to look for new FC-CSP vendors. In particular, we believe that Simmtech will benefit from new business opportunities thanks to its strong cost competitiveness and technological know-how.

FC-CSP structure



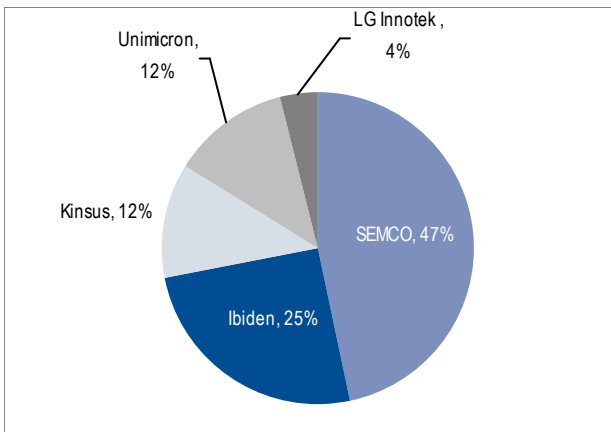
Source: Simmtech

Substrates used for different smartphone parts



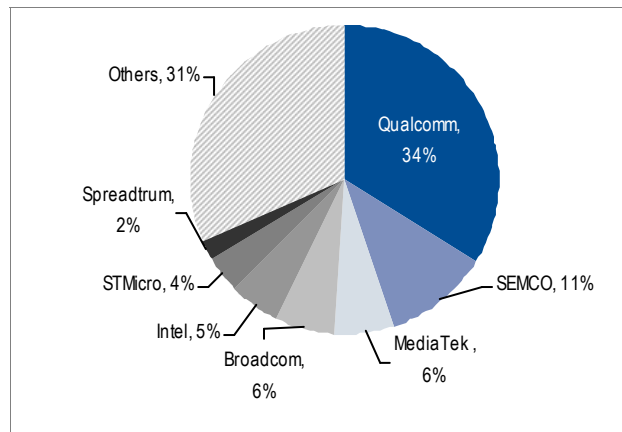
Source: SEMCO

FC-CSP market share, by company (as of end-2012)



Source: Woori I&S Research Center

Handset chip market share, by company

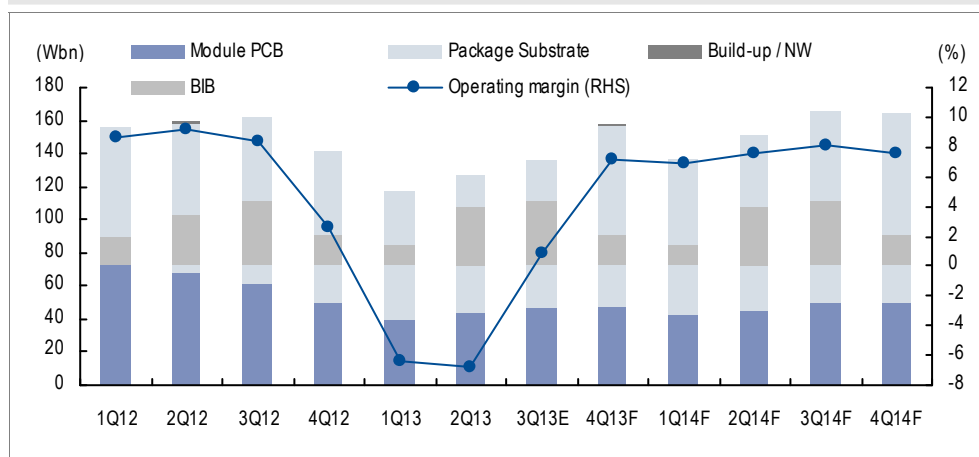


Note: Handset chips include baseband, RF, AP and multi-media chips
Source: Gartner

To register operating profit in 3Q13 on normalizing operations

After registering sound earnings over 2007~2011 (including double-digit operating margins), Simmtech posted an operating margin of 2.6% in 4Q12, followed by operating losses in 1Q13 and 2Q13. In particular, due to reduced utilization at the module PCB line (stemming from the larger-than-anticipated drop in PC demand in 4Q12), fixed costs weighed heavily on the firm's earnings. In addition, the company incurred outsourcing production costs and a contraction in orders over 1Q13~2Q13 due to the fire in February. However, upon the normalization of production from July, we expect Simmtech to return to profit in 3Q13. Specifically, we forecast 3Q13 sales of W140.8bn (up 8% q-q) and operating profit of W1.2bn (TTP q-q).

Quarterly sales and operating margin forecasts



Source: Simmtech, Woori I&S Research Center estimates

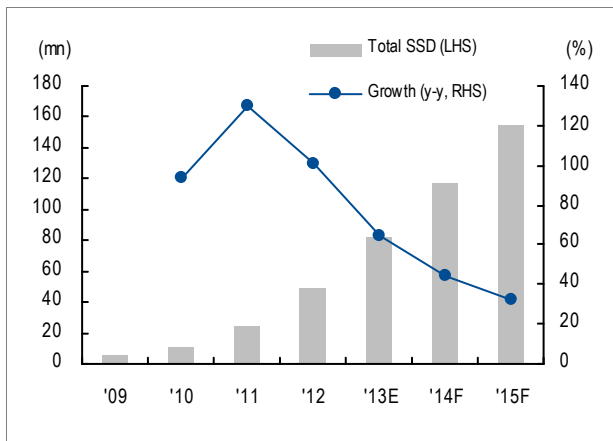
Quarterly earnings forecasts, by product

(Units: Wbn, %)

Sales	Application	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13E	4Q13F	2012	2013E	2014F
Module PCB		76.0	67.8	62.0	49.0	40.4	43.0	46.7	46.9	254.8	177.0	186.1
DDR3 Module	PC	37.6	37.9	35.5	24.5	21.1	22.9	26.5	25.5	135.5	95.9	89.8
RDIMM	Server	26.5	18.3	15.6	14.1	11.9	13.3	12.5	12.7	74.5	50.4	58.0
Package Substrate		80.1	90.9	99.6	92.1	76.2	83.6	89.5	110.6	362.7	359.8	431.0
DDR3 BOC	PC/Server	36.0	33.6	33.8	22.1	21.9	22.9	26.1	23.4	125.5	94.3	76.1
FMC	Mobile	15.9	13.8	12.3	12.6	6.6	7.7	8.6	12.0	54.6	34.9	31.4
MCP	Mobile	14.9	22.4	30.7	38.4	31.0	35.1	38.4	51.8	106.4	156.3	233.8
FC-CSP	Mobile	0.4	0.6	1.2	0.8	0.8	2.0	3.8	7.6	3.0	14.2	35.4
Build-up/NW	Mobile	0.3	0.3	0.3	0.5	0.5	0.4	0.3	0.5	1.4	1.7	1.7
BIB	DRAM test	1.9	3.4	4.4	2.1	1.4	3.9	4.4	2.1	11.8	11.8	11.8
Operating profit		13.6	15.0	13.9	3.8	-7.6	-8.8	1.2	11.4	46.3	-3.9	47.9
Operating margin		8.6	9.2	8.4	2.6	-6.4	-6.7	0.8	7.1	7.3	-0.7	7.6

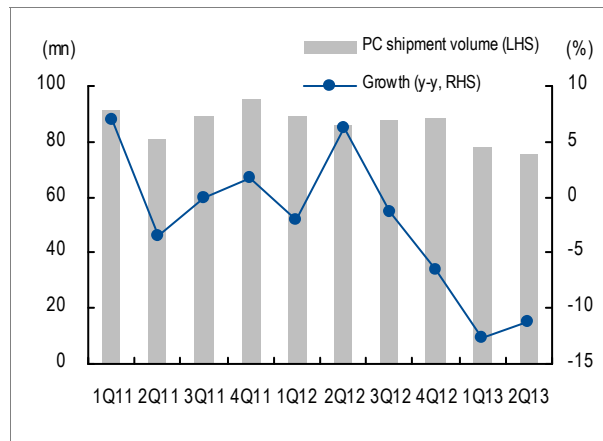
Source: Simmtech, Woori I&S Research Center estimates

Global SSD demand forecast



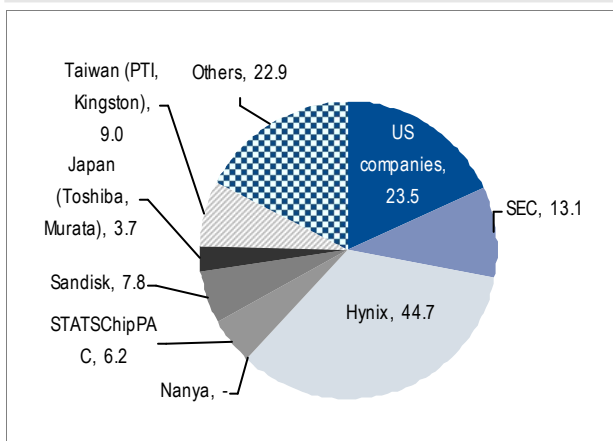
Source: Gartner

Quarterly PC shipment forecast



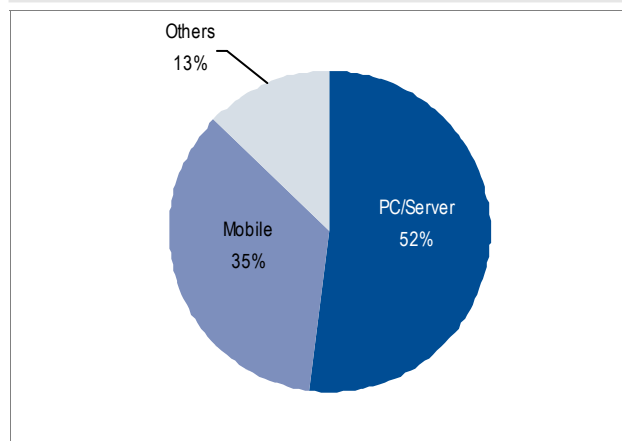
Source: Gartner

Sales breakdown, by client (2Q13)



Source: Gartner, Woori I&S Research Center estimates

Sales breakdown, by application(2Q13)



Source: Simmtech, Woori I&S Research Center estimates

STATEMENT OF COMPREHENSIVE INCOME

(Wbn)	2012/12A	2013/12E	2014/12F	2015/12F
Sales	631	550	631	725
Growth (%)	3.0	-12.7	14.6	15.0
COGS	544	519	543	619
Gross Profit	86	31	88	106
Gross margin (%)	13.7	5.7	13.9	14.7
SG&A	40	35	40	46
Operating Income	46	-4	48	61
Growth (%)	-26.0	TTL	TTP	26.9
Operating margin (%)	7.3	-0.7	7.6	8.4
EBITDA	79	31	82	97
Non-Operating Profits	-13	-11	-6	-6
Financial Income(Costs)	-5	-6	-6	-6
Other Non-Operating Profits	-6	-5	0	0
Gains(Losses) in Associates, Subsidiaries and JVs	-3	0	0	0
Pre-tax Profit from Cont. Op.	33	-15	42	55
Income Taxes	8	0	9	11
Profit from Continuing Op.	25	-15	33	43
Net Profit	25	-15	33	43
Growth (%)	-41.5	TTL	TTP	31.0
Net margin (%)	3.9	-2.8	5.2	5.9
Net Profit of Parent	25	-15	33	43
Net Profit to Non-Controlling	0	0	0	0
Other Comprehensive Income	0	0	0	0
Total Comprehensive Income	25	-15	33	43

VALUATION INDEX

	2012/12A	2013/12E	2014/12F	2015/12F
Price/Earning (X)	13.0	N/A	8.2	6.2
PER (High,X)	19.7	N/A	10.9	8.3
PER (Low,X)	11.8	N/A	7.2	5.5
Price/ Book Value (X)	1.5	1.4	1.2	1.0
PBR (High,X)	2.3	1.8	1.6	1.4
PBR (Low,X)	1.4	1.2	1.1	0.9
Price/ Gross Cash Flow (X)	3.7	10.4	3.3	2.8
Price/ Sales (X)	0.5	0.5	0.4	0.4
PER/ EPS growth (X)	0.7	N/A	0.4	0.4
PER/ EBITPS growth (X)	1.6	N/A	0.4	0.4
PER/ EBITDAPS growth (X)	2.3	N/A	0.7	0.6
EV/ EBITDA (X)	5.7	13.7	4.9	3.9
EV/ EBIT (X)	9.8	N/A	8.3	6.3
Enterprise Value (Wbn)	451	424	399	381
EPS CAGR (3-Yr) (%)	19.1	-249.5	21.7	17.0
EBITPS CAGR (3-Yr) (%)	8.2	-362.7	19.1	15.3
EBITDAPS CAGR (3-Yr) (%)	5.7	50.7	12.2	11.1
EBITPS (W)	1,494	-121	1,491	1,892
EBITDAPS (W)	2,558	959	2,548	3,022
Fully diluted EPS (W)	792	-471	1,022	1,340
BVPS (W)	6,676	6,006	6,829	7,970
CFPS (W)	2,776	804	2,548	3,022
Sales PS (W)	20,361	17,091	19,583	22,520
DPS (W)	200	200	200	200

CASH FLOW STATEMENT

(Wbn)	2012/12A	2013/12E	2014/12F	2015/12F
Operating Cash Flow	70	20	67	79
Net Profit	25	-15	33	43
Depreciation&Amortization	33	35	34	36
+ Loss(Gains) from Subs	0	0	0	0
+ FC translation loss(profit)	0	0	0	0
+ Losses(Gains) on Disposal of Assets	1	0	0	0
Gross Cash Flow	86	26	82	97
- Incr. (Decr.) in WC	-6	0	0	0
Investing Cash Flow	-64	-49	-35	-56
+ Decr. In Tangible Assets	0	0	0	0
- Incr. In Tangible Assets(CAPEX)	-62	-30	-30	-50
+ Disp.(Acq.) of Inv. Assets	2	5	-5	-6
Free Cash Flow	8	-10	37	29
Net Cash Flow	6	-29	32	24
Financing Cash Flow	31	-14	2	3
Equity Financing	21	0	0	0
Debt Financing	10	-14	2	3
Incr.(Decr.) in Cash	37	-44	34	27
Ending Cash and Cash Equivalents	52	9	42	69
Net Debt (Cash)	120	155	129	112

RIM & EVA

	2012/12A	2013/12E	2014/12F	2015/12F
RIM				
Spread (FROE-COE) (%)	-0.4	-21.3	2.8	5.0
Residual Income	-0.9	-41.9	5.8	11.9
12M RIM Target Price (W)	11,039			
EVA				
Invested Capital	279.3	294.4	292.1	307.7
NOPAT	39.1	-5.9	37.9	48.1
ROIC (%)	14.3	-2.0	12.9	16.1
ROIC - WACC (%)	7.3	-9.9	5.7	8.7
EVA	20.2	-29.2	16.7	26.6
DCF				
EBIT	46.3	-3.9	48.0	60.9
+ Depreciation/Amortization	33	35	34	36
- CAPEX	-62.2	-30.0	-30.0	-50.0
- Incr. (Decr.) in Working Capital	1.0	1.7	-1.7	-2.0
Free Cash Flow for Firm	4.3	-0.8	43.7	36.5
WACC				
Cost of Debt (Tax Adj.)	2.5	3.5	2.7	2.8
Cost of Equity (COE)	13.1	13.9	13.1	13.1
WACC (%)	7.0	7.9	7.2	7.4

STATEMENT OF FINANCIAL POSITION

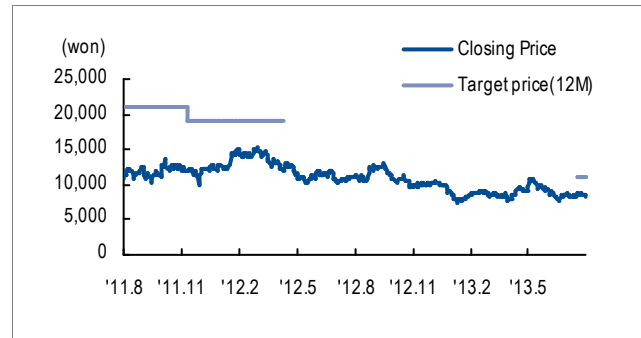
(Wbn)	2012/12A	2013/12E	2014/12F	2015/12F
Cash and Cash Equivalents	52	9	42	69
Accounts Receivables	43	38	43	50
Total Current Assets	191	133	182	226
Tangible Assets	239	235	232	246
Investment Assets	38	33	38	43
Non-Current Assets	312	326	327	346
Assets	503	459	508	572
Short-Term Debt	64	55	64	73
Account Payables	46	40	46	53
Current Liabilities	168	146	168	193
Long-Term Debt	108	108	108	108
Long-Term Allowance	11	9	11	12
Non-Current Liabilities	121	119	121	123
Liabilities	288	266	289	316
Capital Stock	16	16	16	16
Capital Surplus	102	102	102	102
Retained Earnings	98	76	102	139
Non-Controlling Interests Equity	0	0	0	0
Shareholders' Equity	215	193	220	257

PROFITABILITY & STABILITY

	2012/12A	2013/12E	2014/12F	2015/12F
ROE (%)	12.6	-7.4	15.9	18.1
ROA (%)	5.2	-3.2	6.8	8.0
ROIC (%)	14.3	-2.0	12.9	16.1
EBITDA/ equity (%)	36.9	16.0	37.3	37.9
EBITDA/ asset (%)	15.7	6.7	16.1	17.0
Dividend Yield (%)	1.9	2.4	2.4	2.4
Payout Ratio (%)	26.1	-42.2	19.5	14.8
Total Cash Dividend (Wbn)	6	6	6	6
Cash DPS (W)	200	200	200	200
Net debt(cash)/ equity (%)	55.7	80.2	58.8	43.7
Debt/ equity (%)	134.1	137.4	131.2	123.0
Net interest exp/ sales (%)	1.0	1.2	1.1	1.0
Interest coverage (X)	7.0	-0.6	7.2	8.7
Current Ratio (%)	114.1	90.9	108.4	117.3
Quick Ratio (%)	69.8	46.7	64.1	73.0
Total shares (mn)	32	32	32	32
Par value (W)	500	500	500	500
Share price (W)	10,300	8,360	8,360	8,360
Market Cap (Wbn)	332	269	269	269

Rating and target price update

Company	Code	Date	Rating	Target price
Simmtech	036710.KQ	2013.08.21	Buy	W11,000(12M)
		2013.08.21		Coverage initiated
		2011.12.01	Buy	W19,000(12M)



Woori Investment & Securities stock ratings

1. Period: Uniform 12-month
2. Rating System: Based on a stock's absolute return from the date of publication
 - Strong Buy: high conviction Buy rated stocks
 - Buy: greater than +15%
 - Hold: 0% and +15%
 - Reduce: less than 0%

Compliance notice

- Woori I&S does not have a stake greater than or equal to 1% in Simmtech as of the preparation date.
- Woori I&S has not provided this material to any institutional investor or other third party in advance.
- The analyst and his/her spouse do not own any securities of Simmtech as of the preparation date.
- This report correctly reflects the analyst's opinion and was written without any external influence or intervention.

Disclosures

The research is based on current public information that Woori I&S considers reliable, but Woori I&S does not represent it as accurate or complete and it should not be relied on as such. Furthermore, the research does not take into account particular investment objectives, financial situations or individual client needs, and Woori I&S is in no way legally responsible for future returns or loss of original capital. All materials in this report are the intellectual property of Woori I&S. Copying, distributing, transmitting, transforming or lending of this material without Woori I&S' consent is prohibited.