

## COMPANY RESULTS

### Sunny Optical (2382 HK)

2022: Results In Line; Slow Recovery For Smartphone Business In 2023

Sunny Optical's 2022 net profit dropped 52% yoy to Rmb2,408m, at the upper end of profit warning. Product mix was better than expected, thanks to higher contributions from AR/VR and vehicle products, and resilient HCM ASP. As such, gross margin came in above our expectations and slightly below consensus expectation. Going forward, management remains confident in the AR/VR and vehicle businesses, but is conservative on the handset business. Maintain BUY. Target price: HK\$111.00.

#### 2022 RESULTS

Year to 31 Dec	2H21	1H22	2H22	yoy % chg	hoh % chg	2021	2022	yoy % chg
<b>Revenue (Rmbm)</b>	17,663	16,972	16,225	(8.1)	(4.4)	37,497	33,197	(11.5)
Optical component	4,432	4,399	5,069	14.4	15.2	8,776	9,468	7.9
Optoelectronic	13,026	12,371	10,955	(15.9)	(11.4)	28,334	23,326	(17.7)
Optical instrument	206	202	202	(1.9)	(0.1)	387	403	4.2
Gross profit	3,790	3,522	3,083	(18.7)	(12.5)	8,736	6,605	(24.4)
Net profit	2,300	1,358	1,050	(54.4)	(22.7)	4,988	2,408	(51.7)
<b>Margin (%)</b>								
Optical component	35.9	35.5	31.5	(4.4)	(4.0)	39.5	33.4	(6.1)
Optoelectronic	12.4	11.6	9.7	(2.7)	(1.9)	13.7	10.7	(3.0)
Optical instrument	49.9	44.6	40.0	(9.9)	(4.6)	45.1	42.0	(3.1)
<b>ASP (Rmb/unit)</b>								
Optical component	5.3	5.7	7.7	45.3	34.5	5.3	6.6	25.5
Optoelectronic	38.1	39.2	43.5	14.3	10.9	39.0	41.1	5.3

Source: Sunny Optical, UOB Kay Hian

#### RESULTS

- **2022 revenue declined 11.5% yoy to Rmb33.2b, above our and market expectations.** The vehicle as well as augmented reality and virtual reality (AR/VR) businesses were not far off our expectations, but the handset camera module (HCM) business turned out to be more resilient than expected. As such, revenue for the optoelectronic product segment was above our expectations at Rmb23.3b (-17.7% yoy). The optical component segment's revenue grew 7.9% yoy, primarily driven by the non-handset businesses, but the handset lens set (HLS) business should have plunged yoy, on the back of sharp ASP correction in 2H22.
- **By end market,** AR/VR product revenue grew 53% yoy to Rmb2,062m, and revenue for vehicle-related products grew 39% yoy to Rmb4,108m. Handset product revenue declined 21% yoy to Rmb23.3b.
- **2022 blended gross margin declined 3.4ppt yoy to 19.9%.** Gross margin came in 0.5 ppt above our expectations due to better-than-expected ASP. Optical component/optoelectronic products/optical instruments registered gross profit margin (GPM) of 33.4%/10.7%/42.0%, representing yoy GPM decline of 6.1ppt/3.0ppt/3.1ppt.

#### KEY FINANCIALS

Year to 31 Dec (Rmbm)	2021	2022	2023F	2024F	2025F
Net turnover	37,497	33,197	37,411	43,134	47,505
EBITDA	7,546	5,259	6,469	8,756	10,394
Operating profit	5,851	3,024	3,827	5,680	6,885
Net profit (rep./act.)	4,988	2,408	3,116	4,760	5,828
Net profit (adj.)	4,988	2,408	3,116	4,760	5,828
EPS (Fen)	455.9	220.1	284.9	435.2	532.9
PE (x)	17.6	36.5	28.2	18.5	15.1
P/B (x)	4.3	4.0	3.7	3.3	2.9
EV/EBITDA (x)	11.6	16.6	13.5	10.0	8.4
Dividend yield (%)	1.1	1.2	1.3	2.1	2.5
Net margin (%)	13.3	7.3	8.3	11.0	12.3
Net debt/(cash) to equity (%)	(0.4)	(3.4)	(4.7)	(21.1)	(32.5)
Interest cover (x)	32.8	18.0	21.0	28.5	33.8
ROE (%)	26.8	11.4	13.7	18.9	20.4
Consensus net profit	-	-	3,842	4,796	4,974
UOBKH/Consensus (x)	-	-	0.81	0.99	1.17

Source: Sunny Optical, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	HK\$91.70
Target Price	HK\$111.00
Upside	+21.0%
(Previous TP)	HK\$119.00)

#### COMPANY DESCRIPTION

Sunny Optical is engaged in the design, manufacturing and sales of optical and optical-related products. These products include glass/plastic lenses, lens sets, camera modules for mobile phones and digital cameras, microscopes and other analytical instrument.

#### STOCK DATA

GICS sector	Information Technology
Bloomberg ticker:	2382 HK
Shares issued (m):	1,097
Market cap (HK\$m):	100,581.1
Market cap (US\$m):	12,821.4
3-mth avg daily t'over (US\$m):	80.3
Price Performance (%)	

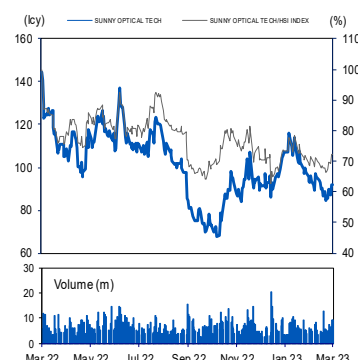
52-week high/low HK\$144.60/HK\$67.55

1mth	3mth	6mth	1yr	YTD
(2.0)	2.8	7.1	(33.4)	(1.2)

#### Major Shareholders

	%
Chairman and employees	38.4
-	-
-	-
FY23 NAV/Share (RMB)	21.74
FY23 Net Cash/Share (RMB)	1.01

#### PRICE CHART



Source: Bloomberg

#### ANALYST(S)

**Johnny Yum**  
+852 2236 6706  
johnny.yum@uobkayhian.com.hk

**Ariel Poh Yun Li**  
+603 2147 1986  
yunli@uobkayhian.com

- **2022 net profit dropped 51.7% yoy to Rmb2.4b**, falling at the upper end of the previous profit warning (-50% to -55% yoy). Apart from the sharp decline in the smartphone business, net profit was also impacted by a forex loss of Rmb353m from US\$-denominated bonds.
- **Operating expenses ratio surged 2.6ppt to 12.3%**. Management credited the expansion to increased R&D investment in AR/VR and vehicle-related products and increased remuneration of employees.

### STOCK IMPACT

- **2023 shipment guidance.** Vehicle lens sets (VLS) are expected to register 15% yoy shipment growth, and HLS and HCM are both expected to register 5% yoy shipment growth. AR/VR is expected to register a 30% yoy growth in revenue, while vehicle camera module revenue is expected to double from Rmb1b in 2023.
- **Spec upgrade trend resumption in 2H23.** Management is expecting the smartphone business to recover from 3Q23, as some Android 4OEMs have increased their orders recently, with a higher interest in spec upgrades for 2H23 launches. That said, management warned that the ASP of HLS and HCM should remain under pressure in 1H23, given a relatively higher base, while end-demand has yet to recover.
- **Robust growth of vehicle-related products to partly offset sluggish handset-related component shipment.** As of 2022, vehicle-related products' contribution to revenue surged to 12.4%, vs 7.9% in 2021. The vehicle business should remain Sunny Optical's key growth driver through 2023, as we now expect the contribution to surge to 14.9% by 2023 on the back of a 36% yoy growth. The vehicle business will be primarily driven by product upgrades, new project wins, as well as robust growth in the vehicle camera module business.
- **2023 ASP likely under pressure; margin guidance below our expectations.** Management provided conservative margin guidance on handset-related components. HLS and HCM margins remain at similar levels vs 2H22 at 20-25% and 5-8% respectively. For VLS, management guided a stable margin of 40%, hoping for flat yoy growth in ASP and GPM. As such, we change our margins assumption for optical components and optoelectronic products by -5.0ppt/-2.7ppt to 31.0%/37.0% and flat/-0.2ppt to 10.0%/11.0% in 2023-24. We are expecting the growth of high-margin emerging businesses (AR/VR/vehicle) to partially offset the weak smartphone business. We are also slightly more optimistic on the smartphone business compared to management's guidance, as we believe the smartphone supply chain is now overly conservative after the big expectations miss in 2H22.
- For the handset business, we are now expecting a mild 5% yoy growth, primarily driven by a stabilising ASP, and mild shipment growth.
- **Capex will reach Rmb3.5b in 2023, vs Rmb3.1b in 2022.** Rmb1.3b will be invested in AR/VR and vehicle-related products, and Rmb800m will be invested in HLS for its major US client. Rmb800m will be spent on its Vietnam plant, and Rmb600m will be used in vertical integration (lens+actuator+module) of HCM.

### EARNINGS REVISION/RISKS

- We fine-tune our 2023-24F earnings estimates by -8.2%/-7.1% to Rmb3,116m /Rmb4,760m and introduce our 2025F earnings at Rmb5,828m. We have factored in assumptions of: a) higher ASP led by better product mix, b) lower shipment growth in HLS, VLS and HCM, c) lower margin for optical components, and d) higher operating expenses.

### VALUATION/RECOMMENDATION

- **Maintain BUY and trim target price to HK\$111.00**, based on lower 2023 earnings estimates. Our target price is now pegged to 34.2x 2023F PE, still based on the five-year average historical mean.

### CATALYSTS

- Recovery of shipment data as smartphone OEMs start to restock in 2Q23.

### OLD ASSUMPTIONS TABLE

(Rmbm)	2023F	2024F	2025F
Shipment (m units)			
Optical Components	1566	1815	NA
Optoelectronic products	608	733	NA
ASP (Rmb)			
Optical Components	5.6	5.8	NA
Optoelectronic products	40.6	41.7	NA
Margin (%)			
Optical Components	36.0	39.9	NA
Optoelectronic products	10.0	11.2	NA
EBIT (Rmbm)	4,052	6,008	NA
Net Profit (Rmbm)	3,393	5,124	NA

Source: Sunny Optical, UOB Kay Hian

### NEW ASSUMPTIONS TABLE

(Rmbm)	2023F	2024F	2025F
Shipment (m units)			
Optical Components	1,527	1,760	1,957
Optoelectronic products	609	681	732
ASP (Rmb)			
Optical Components	7.0	7.2	7.6
Optoelectronic products	43.2	44.0	44.0
Margin (%)			
Optical Components	31.0	37.0	38.0
Optoelectronic products	10.0	11.0	11.5
EBIT (Rmbm)	3,827	5,680	6,885
Net Profit (Rmbm)	3,116	4,760	5,828

Source: Sunny Optical, UOB Kay Hian

### CHANGES TO ASSUMPTIONS TABLE (%)

(Rmbm)	2023F	2024F	2025F
Shipment (%)			
Optical Components	-2.5	-3.0	NA
Optoelectronic products	0.3	-7.0	NA
ASP (%)			
Optical Components	24.3	24.9	NA
Optoelectronic products	6.2	5.5	NA
Margin (ppt)			
Optical Components	-5.0	-2.9	NA
Optoelectronic products	0.0	-0.2	NA
EBIT (%)	-5.6	-5.5	NA
Net Profit (%)	-8.2	-7.1	NA

Source: Sunny Optical, UOB Kay Hian

**PROFIT & LOSS**

Year to 31 Dec (RMBm)	2022	2023F	2024F	2025F
Net turnover	33,197	37,411	43,134	47,505
EBITDA	5,259	6,469	8,756	10,394
Deprec. & amort.	2,235	2,642	3,075	3,509
EBIT	3,024	3,827	5,680	6,885
Associate contributions	(6)	(6)	(6)	(6)
Net interest income/(expense)	(293)	(308)	(308)	(308)
Pre-tax profit	2,715	3,513	5,367	6,572
Tax	(241)	(312)	(476)	(583)
Minorities	(66)	(86)	(131)	(161)
Net profit	2,408	3,116	4,760	5,828
Net profit (adj.)	2,408	3,116	4,760	5,828

**BALANCE SHEET**

Year to 31 Dec (RMBm)	2022	2023F	2024F	2025F
Fixed assets	10,120	9,501	9,656	9,377
Other LT assets	2,236	2,372	2,557	2,698
Cash/ST investment	7,033	7,397	11,931	16,163
Other current assets	23,612	26,807	27,071	28,189
<b>Total assets</b>	<b>43,001</b>	<b>46,077</b>	<b>51,215</b>	<b>56,427</b>
ST debt	6,168	6,168	6,168	6,168
Other current liabilities	13,169	14,423	16,463	17,950
LT debt	123	123	123	123
Other LT liabilities	1,359	1,249	1,396	1,508
Shareholders' equity	21,838	23,770	26,721	30,335
Minority interest	344	344	344	344
<b>Total liabilities &amp; equity</b>	<b>43,001</b>	<b>46,077</b>	<b>51,215</b>	<b>56,427</b>

**CASH FLOW**

Year to 31 Dec (RMBm)	2022	2023F	2024F	2025F
Operating	7,377	4,722	8,536	8,851
Pre-tax profit	2,715	3,513	5,367	6,572
Tax	(627)	(312)	(476)	(583)
Deprec. & amort.	2,235	2,642	3,075	3,509
Associates	6	6	6	6
Working capital changes	3,714	(1,171)	601	(611)
Other operating cashflows	(665)	43	(37)	(42)
Investing	(3,834)	(4,124)	(3,633)	(3,623)
Capex (growth)	(3,114)	(3,500)	(3,000)	(3,000)
Investments	1	(25)	(35)	(26)
Proceeds from sale of assets	0	0	0	0
Others	(721)	(599)	(598)	(597)
Financing	(2,159)	(277)	(414)	(1,038)
Dividend payments	(974)	(1,048)	(1,184)	(1,809)
Issue of shares	0	0	0	0
Proceeds from borrowings	764	764	764	764
Loan repayment	0	0	0	0
Others/interest paid	(1,949)	6	6	6
Net cash inflow (outflow)	1,384	320	4,490	4,189
Beginning cash & cash equivalent	5,605	7,033	7,397	11,931
Changes due to forex impact	44	44	44	44
Ending cash & cash equivalent	7,033	7,397	11,931	16,163

**KEY METRICS**

Year to 31 Dec (%)	2023	2023F	2024F	2025F
<b>Profitability</b>				
EBITDA margin	15.8	17.3	20.3	21.9
Pre-tax margin	8.2	9.4	12.4	13.8
Net margin	7.3	8.3	11.0	12.3
ROA	5.9	7.0	9.8	10.8
ROE	11.4	13.7	18.9	20.4
<b>Growth</b>				
Turnover	(11.5)	12.7	15.3	10.1
EBITDA	(30.3)	23.0	35.4	18.7
Pre-tax profit	(51.8)	29.4	52.8	22.4
Net profit	(51.7)	29.4	52.8	22.4
Net profit (adj.)	(51.7)	29.4	52.8	22.4
EPS	(51.7)	29.4	52.8	22.4
<b>Leverage</b>				
Debt to total capital	22.1	20.7	18.9	17.0
Debt to equity	28.8	26.5	23.5	20.7
Net debt/(cash) to equity	(3.4)	(4.7)	(21.1)	(32.5)
Interest cover (x)	18.0	21.0	28.5	33.8

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