

22 April 2014 | Sector update

## Semiconductor sector China to fuel demand for 4G smartphones

**Maintain POSITIVE**

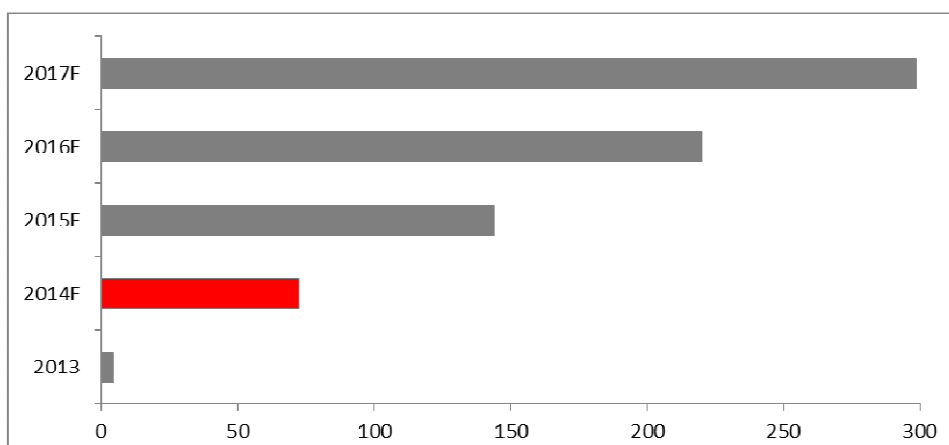
- TSMC's stellar 1Q14 performance underpinned by active global smartphone market.
- The launch of 4G services in China is expected to boost demand for 4G smartphones.
- Local Chinese phone vendors are working against time to expedite new 4G smartphones launches to compete with Samsung and Apple.
- Malaysia's technology companies involved in the smartphone value chain could experience positive spill-over effects.

**Positive 1Q14 performance by TSMC...** Taiwan Semiconductor Manufacturing Company (TSMC), the biggest dedicated independent semiconductor foundry in the world and an industry bellwether, announced a stellar 1Q14 results over the weekend. The numbers were strong and even outperformed its internal expectations. Profit grew by +21%yoy to TWD47.9b, attributable to higher revenue contribution of TWD148.2b (+11.6%yoy). Demand for its 40/45nm wafers and below continue to rise. Operating profit margin also expanded by +1.9ppts to 35.4%, partly due to higher capacity utilisation.

**...to be reflective of 2014 outlook.** TSMC guided that 2Q14 revenue could grow by more than +20%mom, ranging between TWD180b to TWD183b. Subsequently, operating profit margin is expected to expand, registering numbers within the range of 36.5%-38.5%. Moving forward into the medium term, TSMC's production capacity has been booked through to the end of 3Q14, as quoted by media sources. This is mainly attributable to orders from handset solution and PC chip vendors. China's demand for smartphone is also expected to be strong due to the growth in 4G take-up rates in China.

**4G smartphone boom in China.** In the first two months of 2014, both Samsung and Apple commanded approximately 85% of China's 4G LTE smartphone market. In an attempt to regain better market share and sales footing in the growing smartphone market, local vendors such as Coolpad, Huawei, ZTE and Lenovo are expediting the launch of their respective 4G LTE smartphones. The influx of new 4G smartphones will depress prices, making these gadgets more affordable to the masses. China's domestic 4G smartphone market is set to grow by 1473% to 72.4m units this year, in comparison 4.4m units last years. By 2017, the market is expected to reach closer to 300m units.

**Chart 1: Demand of 4G smartphone in China (in millions)**



Source: IHS

**Maintain POSITIVE.** The intense 4G competition in China could act as a catalyst to further boost the Malaysian semiconductor industry. This could lead to continuous demand for high-value components and parts for the manufacturing of 4G smartphones. In this respect, high capex spending, especially in the area of research and development, is vital to ensure that local manufacturers continuously innovate on new products to meet global demand. Having manufacturing presence in China could serve as an added advantage to gain better market access. We opine that companies such as Unisem and MPI which have manufacturing facilities in Chengdu and Suzhou respectively, could be one of the main beneficiaries. With the upbeat demand of smartphones, we reiterate our bullish stance on the industry. On a separate note, we expect demand of wearable devices to gain traction as developers are competing to launch new and better versions of wearable devices.



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### MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

#### STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

#### SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.