

# Lenovo (992.HK) – Q3 FY13 Earnings Preview

## Technology Sector

28 January 2013

The company will report FQ3 earnings after the market close on January 30. Analyst earnings call January 30th at 5:30 pm HKT. Dial-in number +1 866 242 1388 (toll-free) for US investors or +852 2759 8661. <http://mms.pnasia.com/00992/20130130/live/investor/default.aspx>. Average surprise over the past 4 quarters has been +3% on sales and +10% on net profit, but surprises have narrowed in each successive quarter.

We are looking for quarterly revenues of **US\$9.25bn, +10%yoy** and net profits of **US\$190m, +23%yoy**. Product mix should lift GPMs from 11.4% in FQ311 to 12%. We expect operating margins to improve 29bps from a year earlier on improving profitability in Europe, Middle East Africa, smart phones and another solid quarter of controlling cost. Compared to consensus we are slightly above on revenues and +4.7% above on net profit.

Figure 1: Lenovo FQ3 Estimates

US\$m	Actual Q3 FY12	Actual Q4 FY12	Actual Q1 FY13	Actual Q2 FY13	SHKF Q3 FY13	Consensus Q3 FY13E
Revenues	8,372	7,496	8,010	8,673	<b>9,245</b>	<b>9,099</b>
yoy%	44.1%	53.6%	35.3%	11.4%	10.4%	8.7%
GPM%	11.40%	10.75%	11.97%	12.11%	<b>12.00%</b>	<b>11.90%</b>
Operating Profit	193	101	182	206	<b>240</b>	<b>237</b>
yoy%	55.3%	46.1%	47.7%	23.8%	24.2%	22.4%
OPM%	2.31%	1.35%	2.27%	2.37%	<b>2.60%</b>	<b>2.60%</b>
Net Profit	154	68	144	163	<b>190</b>	<b>181</b>
yoy%	54.9%	71.1%	32.8%	12.6%	23.1%	17.5%
NPM%	1.84%	0.90%	1.80%	1.88%	<b>2.06%</b>	<b>1.99%</b>
D. EPS (US\$/sh)	1.46	0.65	1.33	1.55	<b>1.80</b>	<b>1.74</b>
yoy%	48.9%	45.4%	23.1%	12.4%	23.0%	19.0%

Sources: Bloomberg and Sun Hung Kai Financial

**Lenovo's CFO disclosed publically that the company is now profitable in its mobile business unit.** This comes 1 to 2 quarters ahead of the schedule management provided at the last earnings call in November. Recent smartphone expansion in India, Russia, Vietnam and Indonesia has undoubtedly been very successful. Our own estimate had the company's mobile business becoming profitable in FY14 Q2 (Q3 this calendar year) in line with the firm's planned Wuhan mobile factory commencing operations.

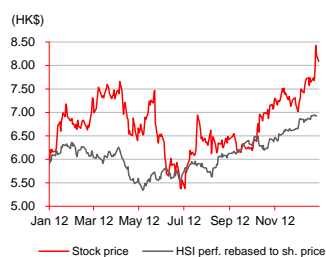
**Though we are optimistic about Lenovo's ability to execute on their non-PC businesses we remain conservative about its impact to the firm's P&L for FY13.** We note that tablet and mobile phones were less than 10% of overall revenues for Lenovo in the prior quarter. On the PC side, Q3 FY13 shipment growth for Lenovo was up 8%yoy according to IDC and Gartner research groups. PC growth globally has been down over 6%yoy. The company continued to outperform its peers.

We re-iterate our **3 Reasons to Buy**. 1) Upside on strength in China, growth in emerging markets and expansion into tablets and smart phones; 2) Increasing scale benefits: ability to leverage existing brand and channels on higher volumes across different products should translate into margin expansion; 3) Financials solid: US\$3.8bn in cash and little debt; strong FCF generation; dividend and share buyback friendly. Our rating and target price are under review.

**Target Price**  
12m Rating

**HK\$8.55**  
Buy (under review)  
5% upside

Lenovo – Price Chart



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**Figure 2: PC Vendor Comparables**

Ticker	Company	Last Price (LC)	Mkt Cap (US\$mm)	YTD %chg	P/E (x)		%	Estimates (%)	
					FY1	FY2	FY2 EPS Growth	Div Yield	Gross Margins
<b>992 HK</b>	<b>Lenovo</b>	<b>8.14</b>	<b>10,886</b>	<b>16.0</b>	<b>18.1</b>	<b>15.0</b>	<b>20.7</b>	<b>1.8</b>	<b>11.9</b>
HPQ US	HP	16.99	33,099	19.2	5.1	4.8	5.8	3.1	21.9
DELL US	Dell	13.16	22,862	29.8	7.7	8.0	-3.1	1.2	22.1
2353 TT	Acer	24.05	2,309	-4.6	24.7	18.7	32.1	1.1	10.3
2357 TT	Asus	339.00	8,643	3.8	11.5	10.8	6.1	4.8	12.8
AAPL US	Apple	439.88	413,064	-17.3	9.8	8.6	13.5	2.5	38.8
<b>Average</b>				<b>7.8</b>	<b>12.8</b>	<b>11.0</b>	<b>12.5</b>	<b>2.4</b>	<b>19.6</b>

Source: Bloomberg, Sun Hung Kai Financial



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