



Data

Price (05/10/2011)	HK\$4.66
Issued shares	10,320.27mn
Market cap	HK\$48,092mn
52week high/low	HK\$5.72/3.9
3m ave.daily vol	38.246mn
Major shareholders:	
Legend Holdings Ltd (41.35%)	
Yuanqing Yang-CEO (9.18%)	

Stock Performance	1 wk	1 mth	3 mth	1 y
Absolute (%)	4.48	-8.63	-0.85	-3.52
Related to HSI (%)	11.13	10.97	27.71	24.70

	30d vol.	60d vol.	1y vol.
Lenovo	63.48	58.42	39.98
Hang Seng Index	35.62	32.93	20.71
Hang Seng Composite			
Index-IT index	44.57	38.59	28.25

Source: Bloomberg, ABCI Securities estimates

52 wk performance



Source: Bloomberg, ABCI Securities estimates

Report date: 06 Oct, 2011

Analyst:

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Lenovo Group (992) – Company Visit Note

Buy (12 month target HK\$5.78)

Investment Highlights

We believe that Lenovo will announce strong earning results in Q3 2011 and Q4 2011 due to strong shipment growth in the China market and other emerging markets. Lenovo is well positioned in emerging and developed markets by adopting diversified strategy. We expect the JV with NEC and the acquisition of Medion will help to increase global market share of Lenovo. Lenovo plans to speed up its mobile internet business, which will bring new growth momentum in the future. We recommend investors to accumulate the stock upon market correction.

Valuation

We initiate with BUY rating and set our 12month target price at HK\$ 5.78, which is based on a 18x FY 11PE and 13.96x FY 12PE.

Risk factors

Slow down in PC demand under a deceleration of global economy.
Supplier concentration risk.

Financial highlights

Yr to Mar31 (US\$ mn)	2011	2012F	2013F	2014F
Revenue	21,594	26,201	31,040	35,996
Chg (% yoy)	30.0%	21.3%	18.5%	16.0%
Gross profit	2,364	3,172	3,725	4,320
Chg (% yoy)	32.1%	34.2%	17.4%	16.0%
Net Income	273	425	548	665
Chg (% yoy)	111.2%	55.6%	29.0%	21.3%
Basic EPS(US cents)	2.84	4.12	5.31	6.44
Chg (% yoy)	100.0%	45.1%	29.0%	21.3%
Diluted EPS(US cents)	2.73	4.12	5.31	6.44
Chg (% yoy)	105.3%	50.9%	29.0%	21.3%
P/E	21.88	14.50	11.24	9.27
NBV(US cents)	18.08	21.90	27.22	33.66
P/B	3.30	2.73	2.20	1.77
DPS(US cents)	0.68	1.03	1.33	1.61
Dividend yield(%)	1.13%	1.72%	2.22%	2.70%
ROE(%)	14.89%	18.81%	19.53%	19.15%
ROA(%)	2.55%	3.29%	3.85%	3.56%

Source: Company data, ABCI Securities estimates @ Foreign exchange rate: HK\$/US\$: 7.8



Strong shipments growth ensure strong earning results in Q3 and Q4

We forecast sales will grow by 24.35% yoy and 24.64% yoy in Q3 2011 and Q4 2011 to US\$7,222.38mn and US\$6,081.81mn respectively due to strong PC shipment growth in the China market; EPS will grow by 17.80% yoy and 59.42% yoy respectively in Q3 2011 and Q4 2011 to US\$0.0121 and US\$0.007 respectively.

Chart 1: Global PC shipments(yoy growth)

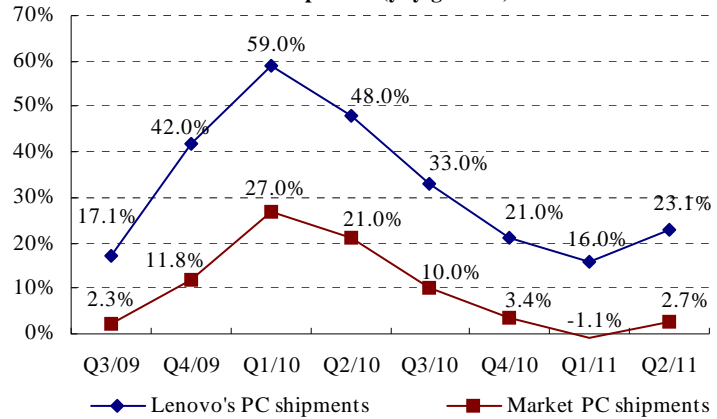
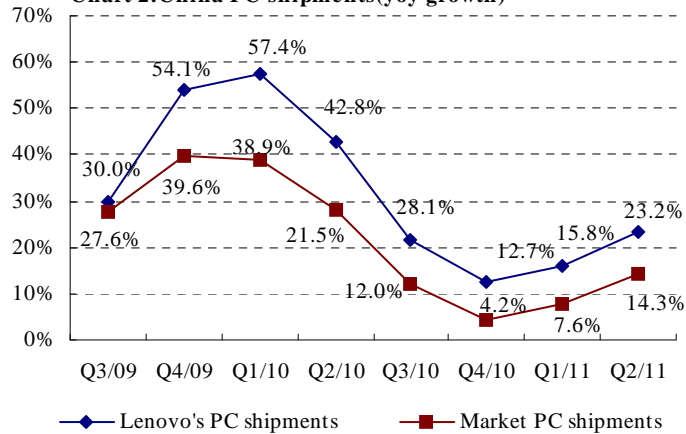


Chart 2: China PC shipments(yoy growth)



Source: Company data, ABCI Securities estimates

Lenovo achieved 23.1% yoy global shipment growth in Q2 2011, which is outperformed the overall PC shipment growth of 2.7% (Chart1). The stronger-than-market growth is due to its strong shipment growth in the China market (Chart2). Management guided that PC shipment growth remained strong for July and August. As we tracked the new broadband subscriber data from China Telecom and China Unicom, which are the two top telecom-operators in China, the July and August new broadband subscriber growth maintained at high level, which indicated strong PC online demand in China ahead. Lenovo, as a leading PC producer that account for 31.7% market share in China, is expected to maintain its strong sales growth and outpace its international peers going forward.



Chart 3: Monthly new broadband subscriber(mn)

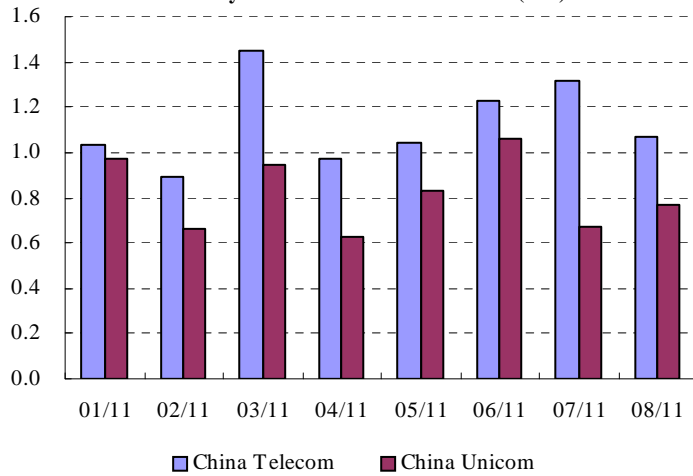
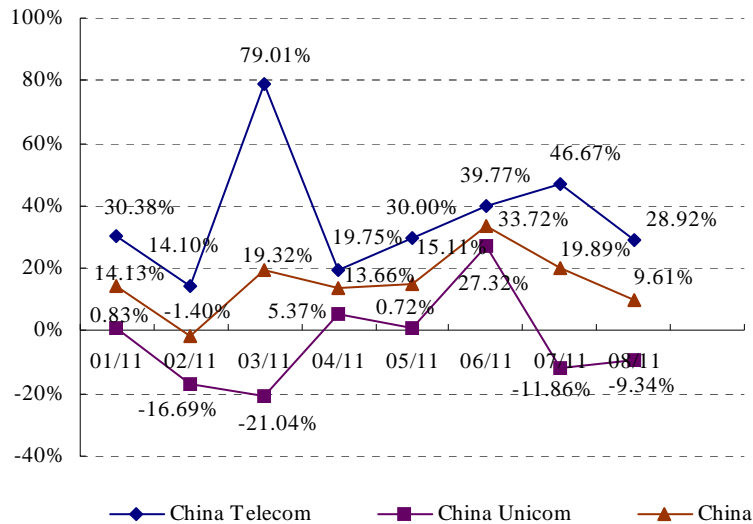


Chart 4: Monthly new broadband subscriber yoy growth(%)



Source: Company data, ABCI Securities estimates

Increasing market share ensure Lenovo to achieve higher margin

In Q2 2011, China has exceeded United States to become the largest PC market which represented 22% of the global PC unit shipments compared to the US at 21%. In addition, Lenovo has overtaken Acer to become the No.3 PC vendor in the world with 22.9% yoy and 25.7% qoq shipment growth (Figure1). We believe Lenovo will surpass Dell as the second-largest PC maker in coming quarters. As HP announced that it plans to spin off its PC business, which could lead HP losing market share to its competitors, including Lenovo. The increasing market share will help Lenovo to achieve scale of economy in sourcing, production and distribution. Subsequently, bargain powers of Lenovo against its suppliers and distributors will further increase. We expect the operating margin of Lenovo will up to 2.4% in next two years (Chart6).



Chart 5 Lenovo global market share (%)

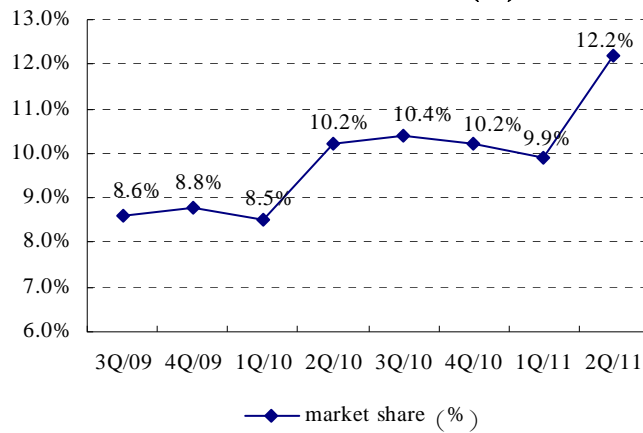
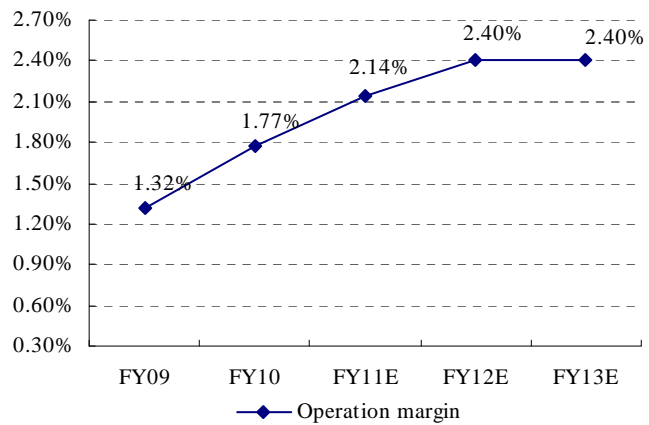


Chart 6: Operation margin (%)



Source: Company data, ABCI Securities estimates

Figure1: Q2/2011 Worldwide PC shipments

Rank	Vendor	2Q/11shipment	Market share	yoy growth(%)	qoq growth(%)
1	HP	15,263	18.0%	3.0%	0.5%
2	Dell	10,927	12.9%	2.8%	6.3%
3	Lenovo	10,276	12.2%	22.9%	25.7%
4	Acer	9,160	10.9%	-10.1%	1.3%
5	Asus	4,468	5.3%	6.0%	-
	All vendor	84,413	100.0%	2.6%	4.8%

Source : IDC, ABCI Securities estimates

Well positioned in emerging and matured markets

China market: In Q2 2011, Lenovo gained 31.7% market share in China, which represented 2.3% yoy and 4% qoq growth. Total sales in China reached US\$2,840 million, accounting for 47.9% of total sales of the group. Total operating profit in China accounts for 70% of total operating profit of the group. Lenovo has divided China into two market segments: 1) Matured market, which includes tier 1 to



tier 3 cities; 2) Emerging market, which include tier 4 to tier 6 cities. Emerging market is expected to achieve double digit growth vs single digit growth in matured market as PC penetration in emerging cities are much lower than matured markets. Lenovo has the edges in branding recognition and provides better after-sale service. It also well positioned in these two market segments and has close relationship with big retailers such as Gome and Sunning. We believe Lenovo will further displace some small local brands and grab more market share.

Emerging markets (excluding China): Lenovo’s emerging markets share reached 6.9% in Q2 2011 and it has already captured 10.8% market shares in India. Market forecasts India shipment will grow by 12.7% yoy and 14% yoy for 2011 and 2012.(Figure 2). Four (including HK/Taiwan/Korea, Asean, India and Rucis) out of seven (including HK/Taiwan/Korea, Asean, India, Rucis, Middle East, Eastern-Europe/Turkey, LA/Brazil) emerging markets are above break-even points so far and we expect more emerging markets will become profitable by the end of this year or early next year.

Matured markets: Currently, Lenovo concentrated on commercial PC business in matured markets as consumer PC is facing fierce competition from media tablet and other competing devices. Matured markets sales accounted for 34.6% of total sales, among which 85% of its sales is concentrated on commercial PC business and 15% is from its consumer PC business. Lenovo provides tailor-made service to its corporate clients. As we expect that corporate PC replacement cycle can further last 5-6 quarters, we believe Lenovo will maintain a sustainable growth in commercial PC business in the coming 2 years.

Chart 7: Lenovo Geographical sales breakdown

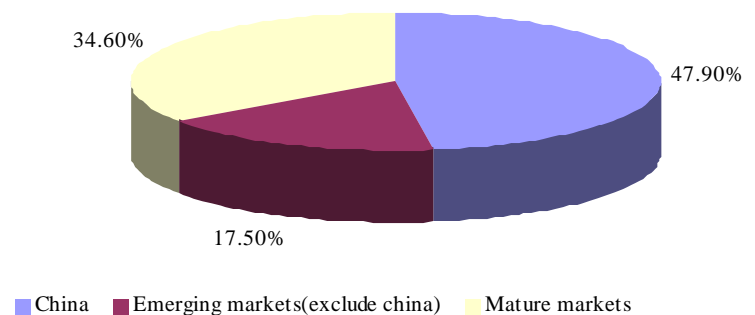


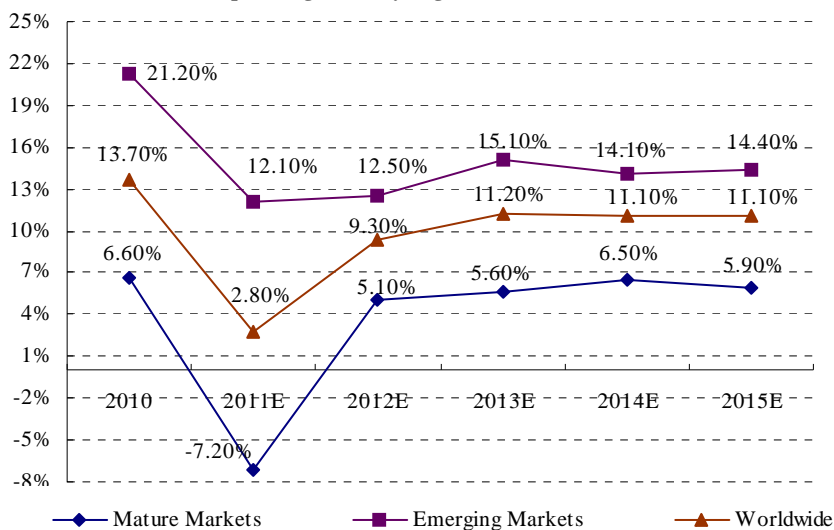
Figure 2: India PC market shipments(mn units): Forecast for 2011 and 2012

	2010	2011	yoy growth(%)	2012	yoy Growth(%)
Total Desktop PC	6.13	6.74	10.00%	7.54	11.90%
Total Portable PC	3.76	4.41	17.30%	5.17	17.20%
Total PC	9.89	11.15	12.70%	12.71	14.00%

Source: Cybermedia Research



Chart 8: PC shipment growth by region, 2010-2015



Source: IDC data, ABCI Securities estimates

Rapid expansion map

Lenovo has set up a JV with NEC(the No.1 PC producer in Japan), and total market share in Japan would have reached 25% by end of 2010 on pro-forma basis. The JV will help Lenovo to expand its Japan market share to 30%. NEC has achieved US\$2220million sales in 2010.

Lenovo announced completion of the acquisition of Medion in July 2011. Medion is the PC and mobile devices producer which has sales network in Germany and Western Europe. We expect Medion to strengthen Lenovo’s distribution network in Europe.

Lenovo also has announced to set up a JV with Compal Electronics, which is the second largest OEM PC maker in the world. We think the JV will bring in synergy effect in cost saving in production.

Speed up mobile internet business

We see rapid development of PC related consumer electronics business in recent years due to strong demand for mobile-internet. Lenovo followed Apple and Samsung to enter into this market through launch its tablets and 3G phones with limiting investing risk as the same types of products have already tested by the first mover. Lenovo’s total mobile handset unit shipments recorded 33.7% yoy growth for 2Q 2011 .We believe mobile internet business will bring new growth momentum as the industry enters a fast-growing era.

Valuation

Lenovo is now trading at 14.50x FY11 PE and 11.24x FY 12PE which is higher than its international peers. As we see Hang Seng Composite IT Index is trading at 17.22x FY11PE, given Lenovo’s high concentration on fast growing markets and continuous rapid expansion, we believe it should trade at a premium with sector



average. We initiate with BUY rating and set 12M target price at HK\$ 5.78, based on 18x FY 11PE and 13.96x FY 12PE.

Figure 3: Comparables

	Price	Market cap(US \$mn)	FY 11 PE	FY 12 PE	FY 11 PB	ROE	ROA
Lenovo	HKD 4.66	6165.70	14.50	11.24	2.73	14.89%	2.55%
Taiwan							
Acer	TWD 33.65	3004.01	-	19.13	1.05	16.13%	5.39%
Asus	TWD 208	5092.20	9.73	8.67	1.38	15.55%	9.83%
US							
HP	USD 23.86	47410.00	10.91	9.03	1.39	21.66%	7.04%
Dell	USD 15.38	28060.00	7.63	7.77	3.07	33.93%	6.83%
Apple	USD 378.25	350670.00	13.60	11.51	4.86	29.32%	18.64%

Source: Bloomberg, ABCI Securities estimates @ Foreign exchange rate: HK\$/US\$:7.8; TWD/US\$:30.6

Risk factors

Slow down in PC demand under a deceleration of global economy

IMF revised down the real GDP growth forecast of the advanced economies(including US, Eurozone, UK, Japan and Canada) for 2011 and 2012. IMF also revised down the GDP growth forecast of China for 2011 and 2012. The expected slowdown of economies in Lenovo's market will reduce the demand of its products subsequently.

Supplier concentration risk

As disclosed in Lenovo's latest annual report, purchases from the largest supplier accounted for 26% of the Group's total purchase and it may cause high concentration risk.



Lenovo Quarterly Earnings Model

Yr to Mar31 (US\$ mn)	2012F				2010	2011	2012F	2013F	2014F
	Q1	Q2	Q3	Q4					
Sales	5,919.92	6,976.41	7,222.38	6,081.81	16,604.82	21,594.37	26,200.51	31,040.25	35,996.38
Gross profit	738.50	837.17	866.69	729.82	1,789.59	2,363.95	3,172.17	3,724.83	4,319.57
Operating profit	123.06	164.17	172.78	102.45	218.69	382.22	562.48	744.97	863.91
PBT	123.49	158.34	166.95	96.52	176.30	357.75	545.31	731.16	886.80
Net profit	108.80	118.76	125.21	72.39	129.37	273.24	425.16	548.37	665.10
Basic EPS(US cents)	1.11	1.15	1.21	0.70	1.42	2.84	4.12	5.31	6.44
Ratio(%)									
Gross Margin	12.47%	12.00%	12.00%	12.00%	10.78%	10.95%	12.11%	12.00%	12.00%
Operation Margin	2.08%	2.35%	2.39%	1.68%	1.32%	1.77%	2.15%	2.40%	2.40%
Net Margin	1.84%	1.70%	1.73%	1.19%	0.78%	1.27%	1.62%	1.77%	1.85%
E/R Ratio	10.40%	9.65%	9.61%	10.32%	9.46%	9.18%	9.96%	9.60%	9.60%
Q/Q Growth(%)									
Revenue	21.33%	17.85%	3.53%	-15.79%	n.a	n.a	n.a	n.a	n.a
Gross profit	23.17%	13.36%	3.53%	-15.79%	n.a	n.a	n.a	n.a	n.a
Operating profit	77.25%	33.41%	5.24%	-40.70%	n.a	n.a	n.a	n.a	n.a
Net profit	158.18%	9.16%	5.44%	-42.18%	n.a	n.a	n.a	n.a	n.a
EPS	152.27%	3.67%	5.44%	-42.18%	n.a	n.a	n.a	n.a	n.a
Y/Y Growth(%)									
Revenue	15.02%	21.12%	24.35%	24.64%	11.44%	30.05%	21.33%	18.47%	15.97%
Gross profit	41.21%	41.18%	33.67%	21.72%	-26.95%	32.09%	34.19%	17.42%	15.97%
Operating profit	51.36%	53.58%	38.68%	47.56%	-56.18%	74.78%	47.16%	32.44%	15.97%
Net profit	98.31%	55.06%	25.65%	71.80%	-72.19%	111.21%	55.60%	28.98%	21.29%
EPS	94.74%	42.07%	17.80%	59.42%	-73.16%	100.00%	45.06%	28.98%	21.29%

Source: Company data, ABCI Securities estimates



Lenovo:Financial Summary

Income statement

Yr to Mar31 (US\$ mn)	2010	2011	2012F	2013F	2014F
Sales	16,604.82	21,594.37	26,200.51	31,040.25	35,996.38
Cost of sales	(14,815.22)	(19,230.42)	(23,028.34)	(27,315.42)	(31,676.82)
Gross profit	1,789.59	2,363.95	3,172.17	3,724.83	4,319.57
Other income	83.13	0.42	0.00	0.00	0.00
Selling and distribution expense	(839.39)	(1,038.46)	(1,495.39)	(1,738.25)	(2,015.80)
Admin expense	(566.25)	(719.71)	(782.13)	(931.21)	(1,079.89)
R&D expense	(214.34)	(303.41)	(317.52)	(310.40)	(359.96)
Other operating(expense)/income	(34.06)	79.43	(14.65)	0.00	0.00
EBITDA	395.48	558.36	708.62	885.37	999.26
Depreciation & amortization	176.79	176.14	146.15	140.41	135.35
EBIT	218.69	382.22	562.48	744.97	863.91
Interest income	20.38	24.93	33.72	36.71	73.41
Interest cost	(62.88)	(49.18)	(50.58)	(50.52)	(50.52)
Share of (losses)/profits of associates	0.12	(0.23)	(0.31)	0.00	0.00
PBT	176.30	357.75	545.31	731.16	886.80
Taxation	(46.94)	(84.52)	(120.15)	(182.79)	(221.70)
Net Income	129.37	273.24	425.16	548.37	665.10
Basic EPS(cent)	1.42	2.84	4.12	5.31	6.44
Diluted EPS(cent)	1.33	2.73	4.12	5.31	6.44
Dividend	35.58	68.73	106.29	137.09	166.28
DPS(US\$)	0.00	0.68	1.03	1.33	1.61
Dividend payout ration(%)	27%	25%	25%	25%	25%

Growth&Margin(%)	2010	2011	2012F	2013F	2014F
Sales growth	11.44%	30.05%	21.33%	18.47%	15.97%
EBIT growth	-56.18%	74.78%	47.16%	32.44%	15.97%
Net income growth	-72.19%	111.21%	55.60%	28.98%	21.29%
EPS growth	-73.16%	100.00%	45.06%	28.98%	21.29%
Gross margin	10.78%	10.95%	12.11%	12.00%	12.00%
EBIT margin	1.32%	1.77%	2.15%	2.40%	2.40%

Source:Company data,ABCI Securities estimates



Balance sheet

As of Mar31 (US\$ mn)	2010	2011	2012F	2013F	2014F
Cash and cash equivalents	2,439.00	2,996.66	4,058.23	4,478.46	5,079.98
Account receivables	1,407.81	1,760.57	1,926.51	2,282.37	2,646.79
Inventories	878.89	803.70	1,010.02	1,198.04	1,389.33
Others	1,509.92	2,375.53	3,276.80	3,716.25	7,095.56
Total current assets	6,235.61	7,936.46	10,271.55	11,675.13	16,211.67
property, plant and equip	248.26	209.42	200.56	194.20	189.62
Intangible assets	2,066.34	2,134.45	2,040.54	1,950.75	1,864.92
Others	405.72	425.61	426.00	426.00	426.00
Total asset	8,955.93	10,705.94	12,938.65	14,246.08	18,692.21
Short-term bank loans	64.71	71.56	61.47	61.47	61.47
Account payables	3,235.85	2,278.80	3,289.76	3,902.20	4,525.26
Current portion of non-current liabilities	437.36	449.71	461.75	460.00	460.00
Others	2,681.44	5,232.58	5,990.26	6,138.63	9,296.60
Total current liabilities	6,419.35	8,032.65	9,803.24	10,562.30	14,343.33
Non-current liabilities:	930.56	838.39	875.35	875.35	875.35
Total liabilities	7,349.91	8,871.04	10,678.59	11,437.65	15,218.68
Total equity	1,606.02	1,834.90	2,260.06	2,808.43	3,473.53
BVPS(\$)	16.50	18.08	21.90	27.22	33.66

Ratios	2011	2012F	2013F	2014F
ROE(%)	14.89%	18.81%	19.53%	19.15%
ROA(%)	2.55%	3.29%	3.85%	3.56%
Inventory days	15.97	14.37	14.75	14.91
Receivables days	26.78	25.68	24.75	24.99
Payable days	52.34	44.13	48.05	48.55
Net debt/equity(%)	(89.21)	(117.68)	(109.73)	(106.04)

Valuation	2011	2012F	2013F	2014F
P/E	21.88	14.50	11.24	9.27
P/B	3.30	2.73	2.20	1.77
Dividend yield(%)	1.13%	1.72%	2.22%	2.70%

Source: Company data, ABCI Securities estimates



Cash flow statement

Yr to Mar31 (US\$ mn)	2010	2011	2012F	2013F	2014F
Net income	129.37	273.24	425.16	548.37	665.10
D&A add-back	176.79	176.14	146.15	140.41	135.35
Minorities interest add-back	0.00	0.00	0.00	0.00	0.00
Change in working capital	433.72	(1,234.63)	638.71	68.55	67.35
Other operating cash flow	94.87	1,750.51	0.00	0.00	0.00
Cash flow from operations	834.75	965.25	1,210.02	757.32	867.80
Acquisition	(106.70)	0.00	(210.00)	(200.00)	(100.00)
Others	(148.35)	65.52	0.00	0.00	0.00
Cash flow from investing	(255.06)	65.52	(210.00)	(200.00)	(100.00)
Dividend paid	(11.90)	(87.87)	(106.29)	(137.09)	(166.28)
issue shares	0.00	0.00	210.00	0.00	0.00
Cash flow from financing	(217.14)	(372.51)	103.71	(137.09)	(166.28)
Net change in cash	375.00	716.30	1,103.73	420.23	601.52
Beginning cash	1,863.00	2,238.20	2,954.50	4,058.23	4,478.46
Ending cash	2,238.00	2,954.50	4,058.23	4,478.46	5,079.98

Source: Company data, ABCI Securities estimates



Disclosures

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