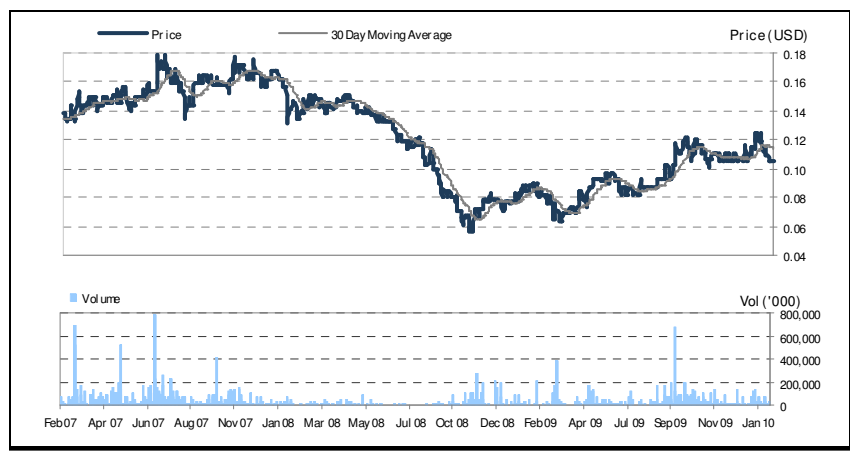


## Hotung Investment Holdings

Bloomberg: **HIH SP**Reuters: **HOTU.SI**Price: **USD0.11**Date: **February 22, 2010****GICS:** Financials/Asset Management & Custody Banks**Business Summary:** Hotung Investment Holdings' (Hotung) primary businesses are venture capital investment and fund management.**Country of Incorporation:** Bermuda**Head Office Location:** 10 Floor, 261 Sung Chiang Road, Taipei, Taiwan, R.O.C.**Place of Operations:** Taiwan**Website:** www.hotung.com.tw**IR Contact:** Frieda Tseng | frieda@equity.com.tw | 886-2-2500-6700**Analyst:** Lorraine Tan, CFA**Investment Highlights**

- With a history that dates back over 20 years, Hotung has since grown into one of the largest venture capital firms in Taiwan. Over the years, it has invested in more than 460 companies worldwide, taken more than 130 companies public in Asia and the U.S., and returned more than USD600 mln capital to its fund investors. 41.4%-associate Hotung International Co Ltd (HIC), meanwhile, is one of the largest venture capital investment managers in Taiwan.
- Hotung's prospects are largely tied to the outlook of the global economy, which we believe should be better in 2010. S&P Economists expect China to post GDP growth of 9.0%-9.5%, while Taiwan should see growth of 3.5%-4.0% on improving consumer confidence and a pickup in services and trading activity. The U.S., meanwhile, is expected to grow at a rate of 2.7%.
- We forecast an 18.9% growth in 2010 revenue, supported by an increase in the number of listings to 10 from seven in 2009 and bolstered primarily by the potential listing of MStar Semiconductor, presently the largest investment in Hotung's portfolio. We forecast a slower 8.8% growth in net profit on the back of marginally higher credit cost estimates.
- Hotung's balance sheet is strong, with a net cashpile of TWD2.09 bln as at end-September 2009. We expect ROEs to average 4.4%-4.7% in 2009-2010.

**Key Investment Risks**

- Earnings volatility.** Hotung's earnings performance is very much dictated by capital market activity as well as the economic health of the countries to which it is exposed. These factors influence issues such as the company's exit strategy and the value of its investments which lend to volatility in earnings. Reflecting this volatility is that the company reported losses in three of the past five years to 2008.
- Investment risk.** As a venture capitalist, Hotung's prospects are tied to the companies it invests in. Investment risk is high, given that the bulk of these companies are either in the start-up or expansion phase. Additionally, there may not be a liquid trading market for these companies which are typically unlisted. As most of Hotung's investments are in technology companies, there is also the risk of product obsolescence in a rapidly evolving environment.
- Economic and political risks.** Investment opportunities in China are dictated by ongoing political issues such as the liberalization of investment policies and cross-strait relations. In Taiwan, the rapidly maturing tech sector poses a risk to portfolio replenishment over the longer term while in the U.S., investment opportunities are presently constrained by the economic health of the country.

**Key Stock Statistics**

52-week Share Price Range (USD)	<b>0.06 - 0.13</b>
Avg Vol - 12 months ('000 shares)	<b>993.7</b>
Price Performance (%)	
- 1 month	<b>-8.7</b>
- 3 month	<b>-4.5</b>
- 12 month	<b>23.5</b>
No. of Outstanding Shares (mln)	<b>1,106.8</b>
Free Float (%)	<b>72.3</b>
Market Cap (USD mln)	<b>116.2</b>
Enterprise Value (USD mln)	<b>50.9</b>
Major Shareholders (%)	
Tai Lung Capital Inc.	<b>14.6</b>
Third Avenue Global Value (Master) Fund	<b>13.1</b>

**Per Share Data**

FY Dec.	2007	2008	2009E	2010E
Book Value (TWD)	7.29	5.68	6.78	6.41
Cash Flow (TWD)	0.37	-0.43	0.27	0.31
Reported Earnings (TWD)	0.37	-0.43	0.27	0.31
Dividend (TWD)	0.32	0.00	0.20	0.22
Payout Ratio (%)	86.4	0.0	70.0	70.0
PER (x)	9.1	NM	12.4	10.9
P/Cash Flow (x)	9.1	NM	12.4	10.9
P/Book Value (x)	0.5	0.6	0.5	0.5
Dividend Yield (%)	9.5	0.0	5.9	6.4
ROE (%)	5.2	-6.7	4.4	4.7
Net Gearing (%)	0.0	0.0	0.0	0.0

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**Background**

Incorporated in Bermuda on March 5, 1997, Hotung Investment Holdings Ltd (Hotung) is principally a venture capital firm whose history dates back to June 1987, when it was then known as Hotung Venture Capital Corp (Hotung VC).

Hotung VC was a venture capital company founded by: (i) Tai Lung Capital Inc (formerly known as Tai Lung Corp), (ii) Daiwa SMBC Ventures (formerly known as NIF SMBC Ventures) and (iii) Mega International Commercial Bank (formerly known as Chiao Tung Commercial Bank Co Ltd).

Venture capital activities aside, the Hotung group is also engaged in fund management operations via 41.4%-associate Hotung International Co Ltd (HIC), one of the largest venture capital investment managers in Taiwan.

HIC is also a value-added partner to Hotung's portfolio of companies, providing management and advisory services in respect of the group's investee companies. Shareholders of the remaining 59% stake in HIC include Tai Lung Capital, Daiwa SMBC Ventures, Mega International Commercial Bank, Feng Tay and Hotung's directors.

Prior to its listing in 1997, the group underwent a restructuring exercise which principally involved the delineation of business activity, with the transfer of Hotung VC's venture capital fund management contracts to HIC.

Hotung was listed on the Main Board of the Singapore Exchange on Aug. 11, 1997. It remains the first and only Taiwan venture capital firm listed on the Singapore Exchange. It currently has offices in Taipei, Shanghai and Silicon Valley.

Hotung's major direct shareholders are Tai Lung Capital with a 14.6% stake, Third Avenue Global Value (Master) Fund (13.1%), and Mega International Commercial Bank (5.4%).

Tai Lung Capital is the private investment vehicle of the Huang family, as represented by Mr Cheng-Wang Huang and Ms Tsui-Hui Huang on the Board of Directors. Third Avenue Global Value (Master) Fund is a fund managed by Third Avenue Management LLC, whose shareholders include various high net worth individuals and institutional clients.

**Board of Directors**

Name	Title	Date of Appointment
Isamu Sakakibara	Chairman, Joint Managing Director	January 2001
Tsui-Hui Huang	Joint Managing Director	August 2006
Cheng-Wang Huang	Non-Executive Director	July 1997
Fook Hong Lee	Non-Executive Director	July 1997
Chun-Chen Tsou	Non-Executive Director	July 1997
Tan Ng Chee	Non-Executive Director	August 2009
Kun-Sen Lu	Non-Executive Director	July 1997
Yang-Fu Kuo	Non-Executive Director	July 1997
Chin-Wei Chen	Non-Executive Director	July 1997
Chi-Chao Huang	Non-Executive Director	November 2007
Nelson Simon Meers	Non-Executive Director	April 2009
Koshiro Taniguchi	Non-Executive Director	April 2009

Source: Company data

At the group's helm is Isamu Sakakibara, who is Chairman and Joint Managing Director. Prior to joining Hotung, Mr. Sakakibara was attached to the Daiwa Securities Group for over 25 years. Mr. Sakakibara holds a B.A. in Economics from Sophia University, Tokyo, and a Master's degree in Economics from the University of Surrey, U.K.

Hotung's other Joint Managing Director is Ms. Tsui-Hui Huang. Ms Huang is also the President of HIC. She has over 20 years of experience in the financial services line. Ms. Huang graduated from National Taiwan University with a B.A. in Business and obtained her MBA degree from Cornell University, USA.

Hotung Group's founder is Mr Cheng-Wang Huang who today sits as a Non-Executive Director on the board, having retired as Chairman of the group in April 2006. His other businesses range from motorcycles to car tyre manufacturing, beverage, food and financials. He is the Chairman of Tai Lung Corp, Tai Ling Motor Co and Bridgestone Taiwan.

**Board Independence**

The Board of Directors comprises 12 members, of whom ten are non-executive directors. A point to note is that three family members sit on the board. Ms Tsui-Hui Huang is Mr Cheng-Wang Huang's daughter while her husband is Mr Chin-Wei Chen (Non-Executive Director). Nevertheless, the other eight non-executive directors are independent and provide for balanced representation, in our opinion.

The Audit Committee, Remuneration Committee and Nominating Committee comprise three members each, all of whom are non-executive. Mr Cheng-Wang Huang sits in all three committees, but the other directors on these committees are independent non-executive directors.

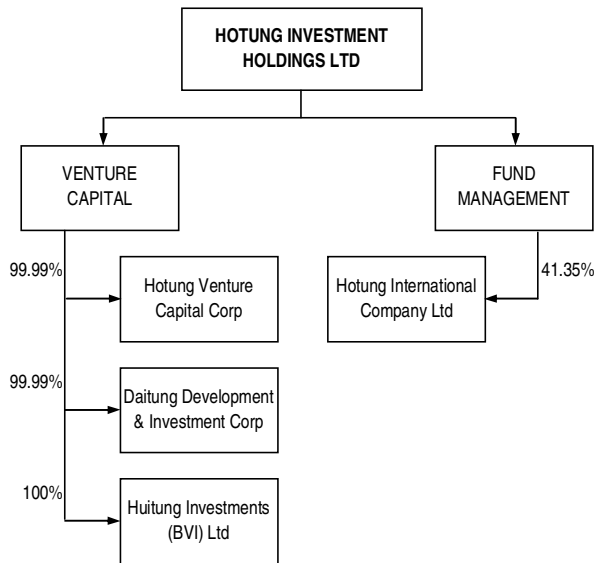
While we do have reservations over the Joint Managing Director positions, we understand that there is clear role separation in that Mr Sakakibara is officially the group's Chairman, while Ms Huang functions as Hotung's Chief Executive Officer. Both are involved in the group's daily operations.

**Key Management**

Name	Title	Date of Appointment
Tsui-Hui Huang	Chairwoman/President	April 2009/May 2005
Joseph Yu	Vice President, Taiwan Investments	March 2009
Cheng-Nan Chou	Vice President, Representative in China	February 2001
Steven Huang	Vice President, U.S. Investments	September 2007
George M.C. Huang	Associate Vice President, Head of Administration	February 2007
David Tso	Associate Vice President – Representative in China	July 2005
Vincent Jang	Associate Vice President – Taiwan Investments	February 2001

Source: Company data

## Corporate Structure



Source: Company data

## Key Subsidiaries & Associates

### Venture Capital Investment

In a move to integrate resources and to improve synergies, three of Hotung's venture capital subsidiaries were merged into one end-2008. Hotung Venture Capital Corp., Futung Venture Capital Corp. and Litung Venture Capital Corp. were amalgamated into a single entity known as Hotung Venture Capital Corp.

The streamlined venture capital division now has three subsidiaries: Hotung Venture Capital Corp (HVC), Daitung Development & Investment Corp. (Daitung) and Huitung Investments (BVI) Ltd (Huitung).

HVC houses the group's venture capital investments in Taiwan, while Huitung holds the group's investments in China/HK. Daitung is primarily involved in share trading. Investments outside Taiwan or China/HK may be undertaken by either HVC or Huitung.

### Fund Management Operations

Although Hotung has three venture capital companies, all investment decisions are made by 41.4%-owned Hotung International Company (HIC), which is the group's fund management and investment arm. HIC has staff strength of 34, 10 of whom are professional fund managers who oversee Hotung group's investment portfolio.

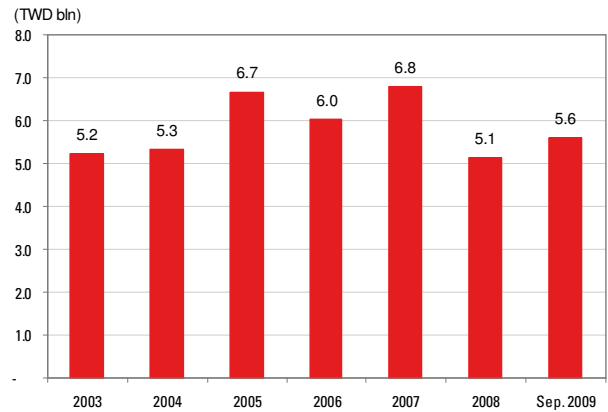
## Business Segments / Key Revenue Streams

### Venture Capital Investment

Over the past 20 years, Hotung has grown into one of the largest venture capital firms in Taiwan. During this period, it has invested in more than 460 companies worldwide, taken more than 130 companies public in Asia and the U.S., and returned more than USD600 mln capital to its fund investors.

The cumulative book value of Hotung's investments has typically averaged about TWD5 bln-TWD6 bln over the past six years and was TWD5.62 bln end-September 2009.

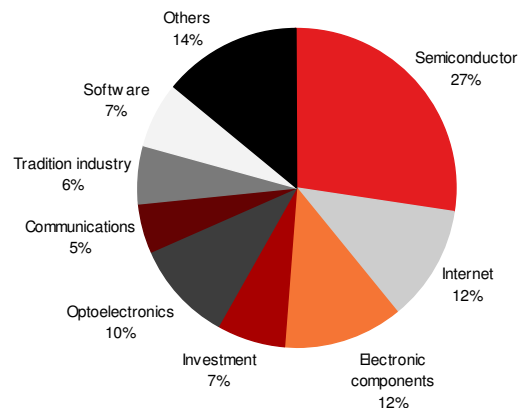
## Book Value of Investments (TWD bln)



Source: Company data

Hotung's investment portfolio as at end-September 2009 comprised 190 investee companies with a cumulative book value of TWD5.62 bln. Investments largely center on technology-based companies with key industry segments being semiconductors, internet, LCD and communications.

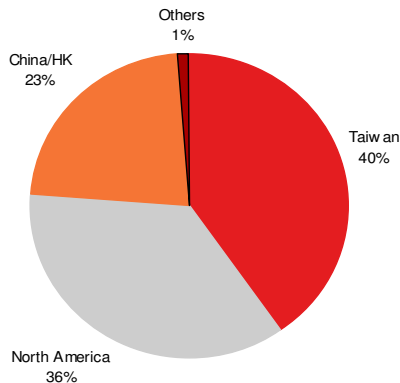
## Key Industry Exposure by Book Value (End-September 2009)



Source: Company data

With offices in Taipei, Shanghai and Silicon Valley, U.S., Hotung's investments are essentially concentrated in these countries. Nevertheless, the portfolio is more diversified now than before, with investments in Taiwan, the U.S. and China/Hong Kong accounting for a respective 40%, 36% and 23% of total NBV as at end-September 2009. In contrast, Taiwan investments accounted for a substantial 61% of total investments in 2003.

## Key Geographical Exposure by Book Value (End-September 2009)



Source: Company data

## Investment Guideline

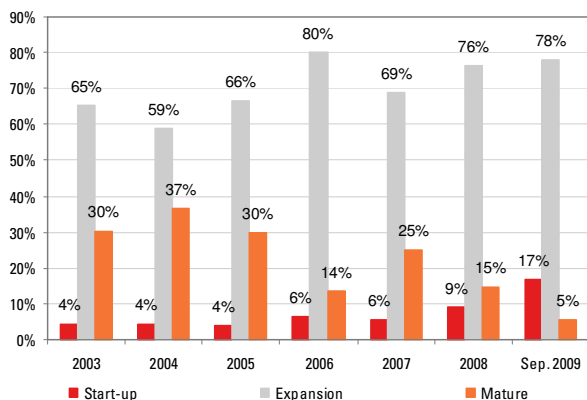
In assessing which companies to invest in, some of Hotung's main criteria are that the company must: (i) be well-positioned in the industry with cutting-edge technology to offer; (ii) keep transparent financial statements; and (iii) have a clear exit strategy.

Hotung adheres to an investment limit of TWD300 mln for a single company and typically caps its shareholding at less than 20%, should it invest in the ordinary shares of a company.

Investee companies are classified into three phases: (i) start-up, (ii) expansion and (iii) mature. Companies in the expansion phase are broadly those that already have a product to offer and are in a fund-raising mode to commercialize the product. These companies are roughly two to four years away from potential listing. Companies in the mature phase are those that are normally ready for listing within the next six months to a year.

Companies in the expansion phase typically account for the bulk of the investments, making up 78% of the value of Hotung's entire portfolio end-September 2009. Companies in the mature phase accounted for 5% of total while those in the start-up phase jumped to 17% of total investments end-September 2009.

## Life Cycle of Investments



Source: Company data

Hotung typically takes an active role in its investee companies with board representation as well. With a wide spectrum of companies under its management, Hotung attempts to value-add wherever possible by bringing together companies that offer synergistic benefits.

## Exit Strategy

In accordance with the objectives of venture capitalism, the strategy is to groom investee companies with the ultimate aim of realizing the value of these investments, be it through trade sales or listings. Since its inception, Hotung has taken 140 companies to listing across various stock markets.

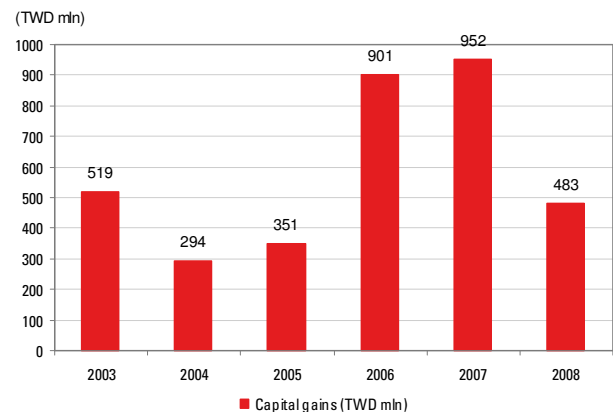
## IPO Record (Cumulative Since 1988)

	2005	2006	2007	2008	2009
TWSE	39	42	43	45	50
Taiwan OTC	50	51	54	54	55
USA Nasdaq & M&A	18	20	23	23	23
UK AIM / OFEX	2	2	2	2	2
Toronto TSE	1	1	1	1	1
Singapore	1	1	1	1	1
Hong Kong GEM	5	6	7	7	8
<b>Total</b>	<b>116</b>	<b>123</b>	<b>131</b>	<b>133</b>	<b>140</b>

Source: Company data

Hotung strives for a benchmark 20% return on investment (ROI) and it typically divests its shareholdings fully in order to realize capital gains. From 2003-2008, Hotung has realized about TWD3.5 bln worth of capital gains, with 2006 and 2007 being bumper years for the group.

## Capital Gains (2003-2008)



Source: Company data

## Fund Management Operations

Fund management operations are undertaken by 41.4% associate HIC, which presently has ten professional fund managers overseeing Hotung group's investment portfolio. HIC manages both in-house and third-party funds, with a cumulative value of TWD7.3 bln as at end-September 2009.

The in-house funds, of which there are three with a total value of TWD6.3 bln, are open-end funds that invest in both listed and unlisted (primarily start-up) companies. Presently, the company manages three third-party funds to the tune of TWD1.05 bln, all of which are closed-end.

**Third-Party Funds Under Management**

Fund	Size (TWD mln)	Duration
Shentung VC	650	To early-2011
Kuangtung VC	200	To mid-2010
Chang Feng Investment	200	To mid-2015
<b>Total</b>	<b>1,050</b>	

Source: Company data

Management fees for both in-house and third-party funds range from 2%-2.5% annually, while a performance fee is also levied on the returns generated.

The group also provides advisory and management services to Daiwa SMBC Capital Co., Ltd. (DS Cap) (formerly NIF SMBC Ventures Co., Ltd) which manages a variety of funds, a portion of which is farmed out to HIC. Funds managed for DS Cap presently total about TWD270 mln.

**Top 10 Investments**

Hotung's top 20 investments as at end-September 2009 totaled TWD2.73 bln in terms of net book value (NBV), accounting for 49% of its total investments of TWD5.62 bln in 190 companies. The top ten companies by NBV are summarised below, all of which are in an expansion phase:

**Top 10 Investments by NBV (End-September 2009)**

Company	NBV (TWD mln)	Industry	Location
MStar Semiconductor	767	Semicon	Taiwan
Summit Microelectronics	162	Semicon	US
Amphastar Pharmaceuticals	160	Life Science	US
Canmake Business	137	Traditional Industry	PRC/HK
E2Open	129	Software	US
Force10 Networks	120	Internet	US
New Egg	116	Internet	US
BitAuto	113	Media	Taiwan
Great Team	109	Semicon	PRC/HK
Fair Friend	100	Precision machinery	Taiwan

Source: Company data

- **MStar Semiconductor.** Headquartered in Hsinchu (ChuPei), Taiwan, MStar is an Integrated Circuit (IC) design house dedicated to providing mixed-mode IC technologies. Products on offer include high-performance display IC products and complete technology solutions in both analog and digital designs for mixed mode ASIC services.
- **Summit Microelectronics.** Founded in January 1997, Summit is a fabless semiconductor company that specializes in the design and manufacture of ICs that incorporate both analog and digital technologies. It is said to be a leader in flexible, highly integrated power management solutions.
- **Amphastar Pharmaceuticals** is a generic and specialty pharmaceutical company that is engaged in the R&D, manufacture

and marketing of generic and proprietary pharmaceuticals, innovative delivery systems and active pharmaceutical ingredients.

- **Canmake Business** is a China-based manufacturer and exporter of furniture, bags, food covers and mosquito nets. It also manufactures galvanized products such as watering cans and flower pots.
- **E2Open** was founded in 2000. It is said to be a pioneer and leader in SaaS-based demand-supply network solutions that assist companies in establishing leaner, more flexible demand-supply networks.
- **Force10 Networks** is a U.S. company that develops and markets high density 10 gigabit and 100 gigabit Ethernet network infrastructure equipment. With offices in North America, Europe, and the Asia Pacific region, its clients include corporate, educational and governmental enterprises.
- **NewEgg Inc** is an online retailer of computer hardware and software. It is said to be the second largest online-only retailer in the U.S. via its website www.newegg.com.
- **BitAuto** is a leading auto media group in China. Focusing on the auto industry, BitAuto has created a solidified multi-media platform embodying five specific media: internet, radio, TV, newspaper and magazine, providing information to more than 95% of the auto users in China.
- **Great Team.** A China-based company founded in June 2001, Great Team is a company involved in the assembly and test of power management integrated circuits.
- **Fair Friend Enterprise.** Based in Taiwan, Fair Friend is a precision machinery company that produces products such as machine tools, pneumatic tools, bearing housings and pulleys, construction machinery, power tools, home improvement hardware and accessories, parking garage equipment, passenger & cargo elevators as well as forklift trucks.

**Industry Landscape**

According to the Taiwan Venture Capital Association (TVCA), Taiwan's venture capital (VC) industry took shape in 1982, with the introduction of Silicon Valley's VC system into the country, and the first VC company was established in 1984. The local VC industry flourished from 1995-2000 alongside the rapid development of Taiwan's technology industry, but moderated thereafter.

Based on TVCA statistics up to end-2007, the number of venture funds increased marginally by two to 272. Capital under management, however, declined for the second year running, to TWD162 bln from a peak of TWD189 bln in 2005. The industry consolidated with the reduction in the number of venture fund management companies to 88 in 2007 from a peak of 105 in 2005. Positively though, the total amount invested by the industry rose further to TWD224 bln in 2007 from TWD204 bln in 2006.

**Venture Capital Industry Taiwan**

	2002	2003	2004	2005	2006	2007
Total venture funds	217	240	259	268	270	272
Total funds size (TWD bln)	151	172	185	189	177	162
No. of venture fund mgt firms	86	93	101	105	101	88
Total amt invested (TWD bln)	145	162	177	188	204	224

Source: TVCA

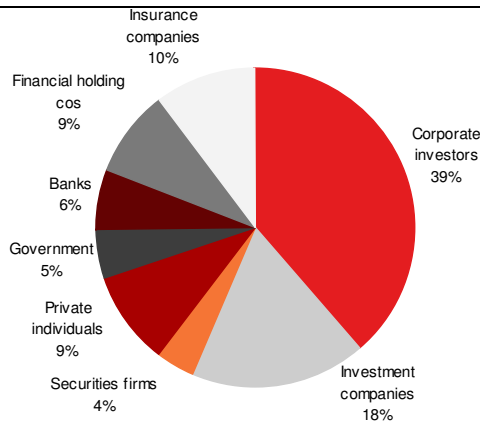
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Corporates comprise the largest portion of investors in Taiwan's venture capital industry, followed by investment companies and insurance companies.

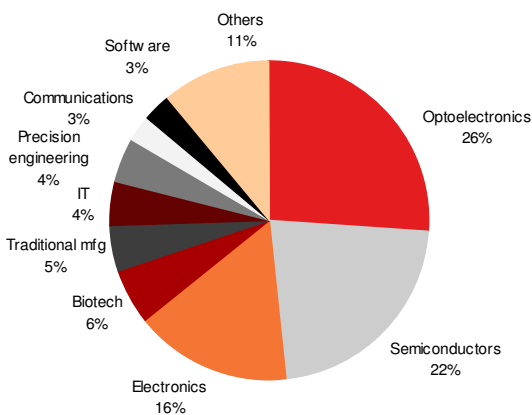
## Taiwan's VC Industry Shareholders (2007)



Source: TVCA

New investments totaled TWD20.6 bln in 2007 and the bulk of these funds were channeled to the optoelectronics, semiconductor and electronics industries, which absorbed a cumulative 64% of the funds in 2007.

## 2007 New VC Investments by Industry (TWD20.6 bln)

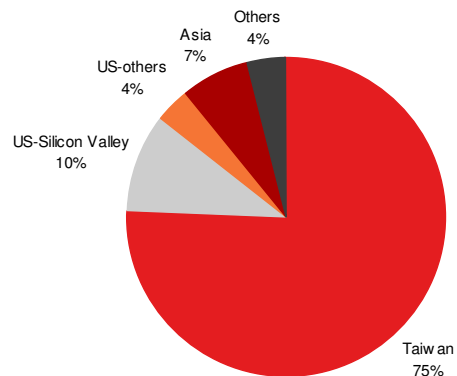


Source: TVCA

Companies in the expansion phase accounted for 46.5% of total new investments in 2007, followed by companies in the start-up phase at 23.1%. Companies in the mature phase followed closely behind in third place, accounting for 22.9% of total new investments.

Meanwhile on a geographical basis, venture capital companies had, not surprisingly, allocated 75% of their 2007 resources to companies in Taiwan, with the U.S. being the alternative investment destination.

## 2007 New VC Investments by Destination (TWD20.6 bln)



Source: TVCA

## Economic Outlook

Hotung's prospects are largely tied to the outlook of the global economy which we believe should be better in 2010, with most countries technically out of recession. Hence, Asian GDP growth should return to more "normal" levels in 2010, albeit not back to the 2007 growth rate, due to slower growth in the U.S..

Positively, the U.S. economy is taking a turn for the better and S&P Economists expect the U.S. to expand by 2.7% in 2010. While a recovery is in the making, high unemployment rates (forecast at 10% in 2010) remain a constraint to consumer spending, which is expected to grow by 2.1% in 2010.

We expect China to post GDP growth of 9.0%-9.5% in 2010, boosted in part by the ongoing implementation of previously planned infrastructure projects and the low 1H09 base effect. Hong Kong and Taiwan should each see growth of 3.5%-4.0% on improving consumer confidence and a pickup in services and trading activity.

Interest rates and inflation should both remain benign in 2010, given our base case scenario for a slow U.S. economic recovery. Inflation is expected to rise from the current low levels but remain manageable. As central banks commit to a neutral policy stance, some tightening will likely occur eventually and we see interest rates rising by 20 bps-100 bps in Asia in 2010, with moves up to intensify in 2H10.

## Semiconductors

S&P Equity Research has a positive fundamental outlook on the semiconductor industry for the next 12 months. For 2010, we foresee sales growth of 10%. Considering recent notes from S&P Economics and market and industry researchers, and chipmakers' earnings reports, we see increasing unit shipments for key end-markets, such as computers, cell phones and other consumer electronics, that comprise a large percentage of the semiconductor industry's demand.

Chipmakers have managed production in an effort to keep supply in line with anticipated demand, and their customers have kept a watchful eye on inventory as well. As a result, inventory appears to be at healthy levels, and the industry has been undergoing an undersupply situation due to the depleted inventory at customer sites and in the distribution channel. As inventory levels are replenished, we believe improving economic conditions will contribute to better end-market demand, supporting further sales growth.

As the industry's plant utilization rates recover, we think chipmakers will post wider margins due to more favorable operating leverage. Chipmakers have cut variable and fixed costs, and as production rises with increasing demand, we see the industry achieving higher profitability and stronger earnings power at lower sales levels.

In the long term, we believe sales growth will decelerate and converge with that of GDP. We see more tempered variability in margins, leading to more stable profits and less risk. Also, with semiconductor companies increasingly utilizing third-party foundries, we believe this shift to fabless or fab-lite manufacturing will contribute to more flexible cost structures and less margin variability.

### Internet Retail

According to estimates from technology research firm IDC, there were some 1.4 bln Internet users around the world, including 247 mln in the U.S., as of roughly the end of 2008. To offer some perspective, the size of the worldwide population of Internet users is comparable to the population of India (estimated to be 1.3 bln as of early 2009, according to the U.S. Central Intelligence Agency), and the size of the U.S. population of Internet users is comparable to the population of Indonesia (240 mln).

Our fundamental outlook for the Internet retail sub-industry is neutral. Despite the favorable growth prospects we see for online retail sales, we are cautious on the group, as ongoing price reductions in response to increasing competition, notable shipping costs (reflecting high fuel prices and free shipping offers), and increasing marketing expenses are a concern to us.

Forrester Research projects that U.S. eCommerce sales will increase to USD229.1 bln in 2013 from USD141.3 bln in 2008, a compound annual growth rate (CAGR) of 10%.

From a macroeconomic viewpoint, personal spending remains the primary driver. Standard & Poor's projects U.S. personal spending will increase 2.1% in 2010. While wage growth is expected to increase modestly, S&P projects U.S. unemployment rate will average 10% in 2010. From an industry perspective, we think online merchants often offer a strong combination of convenience, selection, information and value compared to offline competitors.

### Electronic Components

We have a neutral outlook for the electronic components sub-industry. We believe the revenue growth outlook at component companies will remain challenging into early 2010. Our outlook reflects our view that distributors, electronic manufacturing service (EMS) companies, and original equipment manufacturers (OEM) are restocking inventory levels in anticipation of a gradual economic recovery. In addition, we think the Chinese stimulus plan is driving demand in Asia. We still foresee weak consumer spending, high levels of unemployment, and a restrained housing environment in the important U.S. and European markets, but think the worst of the downturn has passed.

We foresee average price declines in line with historical levels and higher capacity utilization rates, reflecting what we see as challenging end-market demand. Many companies are now extending or completing restructuring initiatives, which we think signals better control of operating expenses. In our opinion, companies are striving for better supply-demand balance, and we see them cutting capacity or eliminating low margin product lines.

However, we believe commodities and raw material costs have increased somewhat in anticipation of a gradual economic recovery. As a result, we think this has introduced some cost uncertainty.

We see favorable longer-term growth for the industry. Segments that show promise over the next three years, in our view, include mobile handsets, devices and computing, and medical devices.

Geographically, we expect Asia to outpace the rest of the world in growth, followed by the Middle East, Africa, and Latin America. We expect weakness in North America and Europe. Product mix, volumes and operating expense structures play a large part in determining profitable growth among companies in this industry.

### Growth Strategy

Over the past few years up to 2007, Hotung had typically invested in about 20 new companies a year. On an annual basis, it has typically spent about TWD1 bln on average, on both new investments and follow-on investments in existing investee companies.

Investments hit a peak in 2007 at TWD1.6 bln but were scaled back to TWD1.1 bln in 2008 with the onset of the financial crisis. Management maintained its cautious stance into 2009 and by September 2009, it had only invested in seven new companies, with total investments declining substantially to just TWD348 mln.

### New and Follow-On Investments

	New companies	New invt. (TWD mln)	Follow-on companies	Follow-on invt. (TWD mln)	Total invt. (TWD mln)
2003	19	629	16	136	764
2004	23	797	16	159	956
2005	21	1,005	12	188	1,193
2006	21	1,027	11	122	1,149
2007	23	1,404	17	190	1,593
2008	15	805	13	318	1,123
Sep. 09	7	248	11	100	348

Source: Company data

With a cash hoard of TWD2.09 bln as at end-September 2009, Hotung is in a strong financial position to expand its portfolio once more. In the near term, the focus will be on opportunities in China and Taiwan. Management remains cautious of investments in the U.S. and will look to some stabilization in its economic environment before investing further in U.S.-based companies. On a sectoral basis, green energy is an industry that management hopes to invest in. Other industries earmarked for future investments include:

### Targeted Industries

Optoelectronics	Telematics
Wireless communications	New materials
Digital content	New energy resources
IC design	Consumption related industries
Broadband network transmission & reception equipment	

Source: Company data

**SWOT Analysis****Strengths**

- A wealth of experience in the VC field, with its history as a venture capitalist dating back over 20 years.
- Prudent management and strong balance sheet, with a net cash pile of TWD2.09 bln as at end-September 2009.
- Streamlining of the group over the years has resulted in a leaner structure and better resource utilization.

**Weaknesses**

- Hotung's earnings are volatile, as they are tied to the performance of global capital markets and economies.
- ROEs have traditionally been low, due in part to the group's large holding of idle low-yielding cash.
- Staff constraints could be an obstacle to Hotung aggressively expanding its investment portfolio in the near term.

**Opportunities**

- China presents venture capitalists with much potential, given the size of the market and the rapid rate of economic advancement, aided further by improving bilateral ties.
- Competition in Taiwan has eased as a result of the crisis and presents cash-rich VCs such as Hotung the opportunity to expand market share.

**Threats**

- The maturity of the tech industry in Taiwan coupled with the emergence of large technology companies as alternative financiers, are factors that challenge existing VC companies in Taiwan.
- Weaker-than-expected economic recovery would negatively impact the financial performance of investee companies.
- Rapidly evolving technology and fierce competition could render products of investee companies obsolete, while the risk of start-up failures remains high.

**Recent Key Developments**

There have been no major corporate developments over the past 12 months.

**Management Guidance**

Management guides that in terms of new listings, it is looking at 10 IPOs in 2010 and 12 IPOs in 2011. This compares against seven IPOs in 2009, comprising one listing on the Hong Kong Stock Exchange, five on the Taiwan Stock Exchange and one on the Taiwan OTC market.

**Earnings Outlook**

In the nine months to September 2009, Hotung reported revenue of TWD662.7 mln, up 10% YoY. While commission and interest income declined YoY, revenue was bolstered by higher investment gains.

Investment gains arose primarily from the listing of six companies during the period and two U.S. trade sales. Coupled with lower allowance for impairment losses of TWD304 mln (-19% YoY), 9M09 net profit jumped to TWD306 mln from TWD60 mln in 9M08.

We expect revenue in 4Q09 to be supported by the listing of one other company, Coxon Precise Industrial (3607 TT, TWD81.30, Not Ranked), during the quarter as well as further investment gains as a result of buoyant capital markets. Partially mitigating this effect is our expectation of some impairment provisions on two or three of Hotung's U.S. investments.

Looking forward to 2010, we expect earnings to be supported by an increase in the number of listings to 10 from seven in 2009. While we expect capital markets to be robust, we are of the view that there could be greater market volatility this year and that listing gains are unlikely to be as sharp as they were in 2009. We also estimate lower trading gains in 2010.

Overall, however, we forecast an 18.9% growth in 2010 revenue, bolstered primarily by the potential listing of MStar Semiconductor, which is presently the largest investment in Hotung's portfolio. This investment carried a value of TWD767 mln end-September 2009 vs. TWD170 mln end-December 2008. We forecast a slower 8.8% growth in net profit on the back of marginally higher credit cost estimates.

Up to September 2009, Hotung had invested just about TWD348 mln comprising TWD248 mln in seven new companies and TWD100 mln in follow-on investments. This represents a significant decline over the TWD1.12 bln invested in 2008. With improved economic fundamentals, we expect the group to ratchet investments back up closer to the historical levels of around TWD1 bln.

As we expect Hotung to be profitable in 2009 and 2010, we have imputed dividend payments in both years, with an assumed payout ratio of 70%. We expect ROEs to average 4.4%-4.7% in 2009-2010.

**Peer Comparison**

	Hotung	Korea Tech	Nexus	Hanmi	Hallim
Year end:	Dec 08	Dec 08	Dec 08	Dec 08	Dec 08
Bloomberg code:	HIH SP	019550 KS	019430 KS	021080 KS	021060 KS
Currency	USD	KRW	KRW	KRW	KRW
Share price @ 19.2.10	0.11	895	425	565	700
Mkt. Cap (USD mln)	116	79	29	20	16
PER Historical (x)	NM	NM	NM	NM	NM
P/NTA Historical (x)	0.6	0.6	0.4	0.7	1.9
<b>Latest FY</b>	Dec 08	Dec 08	Dec 08	Dec 08	Dec 08
Currency	TWD mln	KRW mln	KRW mln	KRW mln	KRW mln
Revenue	654	22,198	4,910	69,130	37,210
Pre-Tax Profit, as reported	-525	-17,950	-11,195	-10,623	-2,033
Net Profit, as reported	-539	-13,838	-11,195	-4,227	-2,467

Source: Capital IQ, Company data

**Profit & Loss**

FY Dec. / TWD mln	2007	2008	2009E	2010E
Reported Revenue	1,086.3	654.2	745.3	886.2
Reported Operating Profit	479.1	-539.3	307.8	337.6
Depreciation & Amortization	0.0	0.0	0.0	0.0
Net interest Income / (Expense)	49.1	38.2	10.1	33.7
Reported Pre-tax Profit	497.2	-525.4	322.4	353.4
Effective Tax Rate (%)	6.3	NM	2.1	2.8
Reported Net profit	465.8	-538.7	315.7	343.5
Reported Operating Margin (%)	44.1	-82.4	41.3	38.1
Reported Pre-tax Margin (%)	45.8	-80.3	43.3	39.9
Reported Net Margin (%)	42.9	-82.3	42.4	38.8

Source: Company data, S&amp;P Equity Research

**Balance Sheet**

FY Dec. / TWD mln	2007	2008
Total Assets	9,513.0	7,060.7
Fixed Assets	0.0	0.0
Current Assets	2,547.7	1,797.3
Other LT Assets	6,965.2	5,263.4
Current Liabilities	115.4	88.5
LT Liabilities	239.7	18.2
Share Capital	6,285.2	6,121.3
Shareholders' Funds	9,157.9	6,954.0

Source: Company data, S&amp;P Equity Research

**Cash Flow**

FY Dec. / TWD mln	2007	2008	2009E	2010E
Operating Cash Flow	-210.6	48.2	-56.5	69.5
Investing Cash Flow	258.5	-168.1	818.9	-527.5
Financing Cash Flow	-359.0	-479.9	-571.7	-236.0
Net Cash Flow	-311.1	-599.8	190.8	-694.0
Ending Cash	2,283.2	1,683.5	1,874.2	1,180.2
Capex	NA	NA	NA	NA

Source: Company data, S&amp;P Equity Research

**Material Disclosures Including Interested Party Transactions**

Nil.

**New Issues & Placements**

There are no new issues or placements. The group, nevertheless, has an active share buyback program. In 2008, Hotung repurchased and canceled 32.77 mln shares, which it bought for a total consideration of USD2.48 mln. In 2009, it repurchased 117.43 mln shares for USD10.6 mln.

**Dividend Policy**

Management does not have a pre-determined dividend policy and historical payments have been erratic, due to loss-making situations. The company paid cash dividends annually from its incorporation in 1997 to 2001. No dividends were paid between 2002 and 2005 when the group incurred losses/low profits. 2006 and 2007 saw a dividend payout of more than 60% each year on the back of sizeable earnings. Dividend payments ceased again in 2008 when the group returned to the red.

As a company registered in Bermuda, Hotung faces restrictions in relation to the quantum of its cash dividends, for there are pre-determined solvency requirements to be complied with.

**Auditors' History**

2002-present: Deloitte & Touche LLP (Public Accountants & Certified Public Accountants).

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