

FINAL TRANSCRIPT

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GRRF - Q1 2009 CHINA GRENTech CORP LTD Earnings Conference Call

Event Date/Time: May. 15. 2009 / 8:00AM ET

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GRENTech CORP LTD Earnings Conference Call

CORPORATE PARTICIPANTS

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China GrenTech - Director, CFO

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Adele Mao

Susquehanna International - Analyst

Charles John

Piper Jaffray - Analyst

PRESENTATION

Operator

Welcome to China GrenTech's 2009 First Quarter Results Conference Call. Statements made in this conference call regarding certain anticipated business prospects constitute forward-looking statements within the meaning of the Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are defined in the Private Securities Litigation Reform Act of 1995.

These statements are based upon GrenTech Management's current expectations and actual results could differ materially. Information regarding factors that could cause actual results to vary can be found in the Company's filings with the Securities and Exchange Commission at www.sec.gov. The Company undertakes no obligation to update or revise forward-looking statements to reflect subsequent events or changed assumptions or circumstances. Following management's opening comments, you will have the opportunity to ask questions. I would now like to turn the call over to the Company. Please go ahead.

Unidentified Company Representative

Thank you, operator, and thanks, everyone, for joining us on our first quarter 2009 results conference call. Joining me today are Rong Yu, Chief Financial Officer, Liping Mao, Director and Vice President of Wireless Coverage, Qi Wang, Vice President of RF business and Qingchang Liu, Vice President of Corporate Finance.

As we proceed through our remarks, we will refer to our results presentation, which can be downloaded from our website at www.grentech.com.cn in the investor section, under financials.

After the overview of our strategy on slide four, the slides pertaining to our first quarter 2009 performance start on slide six. Now let's begin with our wireless coverage business highlights on slide six. The chart on the right shows the first quarter is typically the weakest in terms of revenue, which is a direct result of telecommunications' operators expenditure patterns. However, large-scale 3G network construction was in full swing during the first quarter 2009 following the conclusion of the telecommunications industry restructuring and the issuance of 3G licenses by the PRC government.

This led to substantial growth in market demand for our products and services. As a result, our wireless coverage revenue in the first quarter of 2009 increased significantly, by 200%. Moving to our base station RF business highlights on slide seven, our base station RF revenue increased 565.8% in the first quarter, mainly because the first peak supply period for base station RF modules for 3G network construction in China's first-tier cities occurred during the first quarter of 2009.

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GREENTECH CORP LTD Earnings Conference Call

We expect continued strong demand over the coming quarters as the second peak supply period for base station RF modules for 3G network construction in the second-tier cities is about to begin. However, the next peak supply period will only start after the announcement of the results of base station procurement and tenure procedures, which have yet to be announced.

Therefore, we estimate that demand for base station RF modules in the second quarter of 2009 will be weaker than the first quarter of 2009, as Q2 will be between the peak supply periods. Now let's take a look at slide eight. As mentioned earlier, the first quarter is historically the weakest of the year.

The operating and net income typically experience losses. However, we are delighted to see that the demand pattern for this year has resulted in significant improvement in first-quarter results, demonstrated by the 200% increase in wireless coverage revenue and the 566% jump in base station RF revenue.

The improvement in seasonality is mainly attributable to the favorable market environment in the first quarter of 2009 and the growing contribution from the base station RF business, which contributed strongly.

In fact, base station RF revenue constituted 45% of the total revenue in the quarter, versus only 27% one year ago. Moving to slide nine, the positive operating income achieved this quarter is a result of economies of scale, realized through the substantial revenue increase, with bottom-line profits helped by higher interest income and significant improvement in foreign currency exchange loss. In addition, as announced in the prior quarter, we have committed to a number of initiatives to streamline our cost base and operations and have since divested two subsidiaries and reduced a number of the senior management and middle management positions.

We believe these measures also enabled us to improve our operating efficiency and tighten cost controls, which in turn contributed to the improved bottom line this quarter. Next, let's go over the financials, beginning on slide 11. Benefiting from the substantial rollout of large-scale 3G network construction by the three telecommunications operators, our revenue in the first quarter of 2009 increased 299.6% year-over-year to RMB285.3 million, with wireless coverage revenue increased 200.9% year-over-year to RMB156.7 million and base station RF revenue increased 565.8% year-over-year to RMB128.6 million.

Gross profit increased 232.8% to RMB73.1 million. The gross margin was 25.6% in the first quarter, as compared to 30.8% in the corresponding period in 2008. The decrease in gross margin was due to a decline in wireless coverage equipment average selling price and increased revenue contribution from base station RF business. For the first time, we have achieved positive bottom-line results in the first quarter. Our operating income in Q1 was RMB11 million, as compared to an operating loss of RMB36.3 million in the first quarter of 2008.

Net income for first quarter 2009 was RMB6.3 million, as compared to a net loss of RMB41.5 million in the first quarter of 2008. Turning to our balance sheet on slide 12, cash, cash equivalents and cash timed deposits as of March 31st, 2009, decreased 41.2% to RMB244.4 million, mainly attributable to working capital outflow for raw materials and operating overhead.

Total accounts receivable as of March 31st, 2009, increased 12.2% to RMB1.436 billion, mainly because the majority of sales generated in the first quarter have yet to enter into their payment collection period. Inventories as of March 31st, 2009, increased 33% to RMB692.4 million. The increase was mainly due to the increase in raw material inventory in anticipation of the sales increase and the increase in finished goods, which were installed in customer sites but not yet recognized as revenue.

Moving to the business outlook on slide 14, in terms of wireless coverage business, 3G network construction in China's second-tier cities will begin shortly, so as construction in the first-tier cities in China is coming to an end -- therefore, we expect to see continued growth in market demand for wireless coverage, equipment and services. This will in turn drive further growth in our wireless coverage revenue in the second quarter of 2009 and beyond.

As for the base station RF business, we expect market demand for our base station RF modules to remain strong in the coming quarters as the 3G network construction is expected to roll out in the second-tier cities in China. However, as mentioned earlier,

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GRENTECH CORP LTD Earnings Conference Call

the next peak supply period for base station RF modules will only start after the announcement of the base station procurement tender results, which is currently in process and yet to be announced.

We expect the demand in second quarter of 2009, which will be between peak supply periods, to be weaker than that of the first quarter of 2009. Finally, I will turn to our guidance for the second quarter of 2009 on slide 15. We estimate that revenue for the second quarter of 2009 will range between RMB340 million to RMB380 million, representing a year-over-year increase of 83% to 104%. And, with that, we will be happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). And your first question comes from the line of Adele Mao with Susquehanna International. Please proceed.

Adele Mao - Susquehanna International - Analyst

Hi, my first question is related to the seasonality of your business this year, given that you've had a significant first quarter in light of your historical trends. How should we expect the seasonality to return in 2009, especially if you could comment on towards the end of the year, the fourth quarter where you historically would be booking a significant part of your revenue?

Unidentified Company Representative

Mr. Mao answered your question, Adele.

Liping Mao - China GrenTech - Director, VP

(interpreted) In terms of wireless coverage seasonality, this year is definitely much different than the past years, mainly because -- due to the telecommunication operators' expenditures in 3G network constructions. In Q1, we have very good growth. In Q2, we expect continued growth in wireless coverage revenue and in Q3 we foresee the trend will continue, but to forecast into Q4 at this point is a bit early, so I would have more information to give more -- to give estimates probably at the announcement of Q2 earnings.

Unidentified Company Representative

Ms. Yu answers your question in terms of RF business.

Rong Yu - China GrenTech - Director, CFO

(interpreted) For Q1, the growth is obviously very good, and Q1 definitely is going to be the peak growth for the year. For the coming quarters, the growth will be relatively stable, and at the end of Q2 we probably will be able to give more direction in terms of RF revenue. In terms of overall revenue growth, regardless of wireless coverage or RF business, overall the revenue in full-year '09 is definitely going to have good growth, compared to full-year '08.

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GREENTECH CORP LTD Earnings Conference Call

Adele Mao - *Susquehanna International - Analyst*

Okay, when you talk about the stable growth for the RF business, are you referring to year-over-year or sequentially?

Rong Yu - *China GrenTech - Director, CFO*

(interpreted) For RF revenue, overall, for full year '09, it's going to definitely have a good growth compared to '08. In terms of quarter-over-quarter, the next three quarters have -- the growth in the next few quarters, the year-over-year growth, will be relatively, let's say, stable or flat compared to the year-over-year growth achieved in Q1. In terms of quarter-over-quarter growth, the next three quarters won't be -- the growth won't be as big as the first quarter.

Adele Mao - *Susquehanna International - Analyst*

I see, okay. Could you -- just related to that, your RF product is 40% of your revenue in the first quarter. What's your expectation for the revenue mix for the full year and how do you see this impacting your gross margin?

Rong Yu - *China GrenTech - Director, CFO*

(interpreted) In the first quarter, RF revenue contributed a bit higher to the total revenue, but for the full year '09, the RF revenue contribution will be pretty much in line with the '08 level. Excluding extraordinary items, last year, the RF gross margin was 16.6%. For this year, due to scalability, we foresee the gross margin will be about this level and have room for improvement.

Adele Mao - *Susquehanna International - Analyst*

Okay, thanks for the details. Just lastly, on the accounts receivable front, it looks like the balance has gone further up this quarter. Could you update us regarding your effort in controlling or potentially lowering your account receivable balance, given that you have substantial working capital tied up there? What are the credit facilities that you have available to help you facilitate the cash needed to deliver your growth in 2009?

Rong Yu - *China GrenTech - Director, CFO*

(interpreted) Last year, the account receivable was around 1.28 billion. This year, there's a slight increase in the account receivable in relation to the tremendous growth in the top-line revenue. It's mainly because part of the sales in Q1 have not entered the collection, their payment collection period.

Account receivable situation will definitely improve in 2009. After we implement the stringent cost controls -- after the big increase in the total revenue, we will -- the speed of growth in accounts receivable will definitely be lower than the speed of growth in the top-line revenue.

We have implemented several measures in terms of improving the accounts receivable situation. In terms of new orders, we will focus on developing more on the RF side, because the collection period for RF business is only around 100 days. And in terms of wireless coverage, we will pay more attention in selecting good orders and orders with better payment terms. In terms of historical accounts receivable, we'll continue to speed up the collection time and also at the same time we'll offer discounts to further speed up collection.

In terms of working capital, on one hand, as we speed up collections for accounts receivable, that will help. And, also, on the other hand, we will have bank loans to support for working capital. Right now, we have available bank loans about RMB1.2

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GRENTech CORP LTD Earnings Conference Call

billion, and over this, we have RMB0.6 billion already used, so the remaining are still available. And in the future there's also room to increase bank loans.

Adele Mao - *Susquehanna International - Analyst*

Okay, thanks very much.

Operator

(Operator Instructions). And your next question comes from the line of Charles John with Piper Jaffray. Please proceed.

Charles John - *Piper Jaffray - Analyst*

Thanks for taking my question, guys. Just a follow-up question on the wireless coverage division. Like you had talked about the RF division, can you give us some targets for your 2009 growth and also the gross margin impact?

Unidentified Company Representative

(interpreted) For wireless coverage revenue in Q1, well now there's a significant increase. According to orders, for Q2, we still foresee a big increase in wireless coverage revenue. In terms of Q3, as of now, we can see that the growing trend will continue.

In terms of full year 2009, like I said before, probably toward the time when we announced the Q2 results, we will be able to provide more clear direction. One thing for sure is that overall for 2009 the revenue is definitely -- will definitely have a good growth compared to 2008.

In terms of gross profit margin, we can divide it into two different sections. One is in terms of equipment sales. The other is in terms of our integration services. For integration services, we will see that gross profit margin is -- there is improvement compared to '08, but in terms of equipment sales, we continue to see the pricing pressure. But based on this year, the operator's procurement process that we see, they place more emphasis on suppliers' technology and overall strength, rather than lesser emphasis on the pricing competitiveness.

So we think for '09, overall, the gross margin should be pretty much in line with the '08 level. Even if there is a decrease, it will only be a slight decrease.

Charles John - *Piper Jaffray - Analyst*

Okay, great, thanks. And just in terms of these tenders which are coming through right now, could you give some color on how long this process is going to take, and you talk about the next peak in the supply being after these tenders are going to get completed.

Could you maybe explain to us how GrenTech is positioned with these tenders and how long this process takes. Should we expect the big uptick in Q4, or is it going to be 2010?

Unidentified Company Representative

Mr. Qi Wang answered your question.

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GRENTech CORP LTD Earnings Conference Call

Qi Wang - *China GrenTech - VP*

(interpreted) For China Mobile, the TD phase three tender, the results will come out somewhere toward the end of this month. And our RF business, our RF section, we will provide -- we will supply for the two base station manufacturers for the TD base station manufacturers for the RRU products.

Overall, the supply for TD, there is an increase compared to last year. And the next tender for China Unicom WCDMA network, I think the result will come out somewhere in the second half of the year. Overall, the construction and the tender plan is not very clear. It lacks visibility at this point. We think at the announcement of Q2 earnings, we will probably be able to provide more clear -- more information at that time.

Charles John - *Piper Jaffray - Analyst*

Okay, great, and in terms of the operating margin levels in the model, you have done a pretty good job in just cutting OpEx overall. How should we think of 2009? Where are you guys going to take out costs from in the next several quarters and how should we think of 2009 in terms of your OpEx to overall sales ratio?

Rong Yu - *China GrenTech - Director, CFO*

(interpreted) In 2009, not only the revenue will have very good growth, also in terms of major expense items, we also expect to see great improvements.

I cannot really give you specific numbers. However, I can give you some directions. In terms of RF -- in terms of R&D expenses as percentage of revenue, I'm pretty confident that it won't exceed the '08 level. There are two reasons for the R&D expenses improvement. One is that after our initial investment in the 3G products and right now that part becomes into the stable period, so we expect the R&D expense to be less.

And the second reason is we have greatly improved efficiency of using -- efficiency in using funds. So that also improved the R&D expenses. In terms of sales and marketing expenses, we'll continue to strengthen our efforts to control this expense. In 2009, one factor is the economy of scale as the quantity -- as the revenue increases will help the sales and marketing -- help to improve the sales and marketing expenses. In terms of actual number for 2009, it will be increased compared to 2008, but in terms of percentage to revenue, definitely we'll see good improvement there.

In terms of general and administration expenses, as we mentioned, we have reduced the senior management and middle management positions, so that will help us control these expenses. For last year, excluding extraordinary items, the G&A cost was \$68 million. For '09, definitely it won't exceed this number.

Overall, for '09, the conclusion is the revenue will have very good growth. For gross profit margin, it will be slightly lower, and in terms of expenses we expect to be well under control.

Charles John - *Piper Jaffray - Analyst*

Okay, perfect. Thank you very much, and good luck.

Unidentified Company Representative

Thank you.

May. 15. 2009 / 8:00AM, GRRF - Q1 2009 CHINA GREENTECH CORP LTD Earnings Conference Call

Operator

At this time, we have no more questions. I would like to turn the call back over to the Company for any closing remarks.

Unidentified Company Representative

Thank you for joining us today. We look forward to updating you on our progress.

Operator

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Enjoy the rest of your day.

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