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China optical communication sector update

EQUITY: TECHNOLOGY

Transceiver Act, new fiber capacity, switch chip localization

Quick Note

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China's AI supply chain sector stocks experienced a significant correction on 28 Sept as investors are increasingly cautious before the golden week holidays, amid an uncertain geopolitical and macroeconomy environment, in our view. Moreover, we think two news events in the optical communication sector last week could lead to increased investor concerns: 1) the introduction of the "Chinese Optical Transceivers Act" by a bipartisan group of US senators, and 2) Hengtong Optic-Electric (600487 CH, Not rated)'s A-share private placement plan, which aims at expanding optical fiber capacity. On another note, the *Financial Times* reported last week (*news*) that the China State-owned Assets Supervision and Administration Commission (SASAC) has been surveying state-owned data centers' reliance on Broadcom (AVGO US, Not rated) switches, signaling an accelerated push for supply chain localization, in our view.

Despite these policy uncertainties, the underlying AI infra industry demand remains robust, in our view. Given the continued supply-demand gap in 1.6T optical transceivers and potential commercialisation of NPO (near-field packaging optics), we expect optical transceivers leaders (i.e. Innolight) to continue delivering solid fundamental performance. We recommend InnoLight (300308 CH / 3308 HK, Buy), YOFC (6869 HK, Buy), Shenzhen T&S Communication (300570 CH, Buy), and Unisplendour (000938 CH, Buy).

Optical Transceiver Act: limited impact as the scope only affects government business, but policy overhang remains

On 25 September, a bipartisan group of four US senators formally introduced the "Protecting National Security Systems from Chinese Optical Transceivers Act", which seeks to prohibit the procurement of Chinese manufactured optical transceivers, specifically naming InnoLight and Eoptolink (300502 CH, Not rated), for federal government national security systems (*news*). Currently, this legislation does not extend to the private sector (i.e., AI hyperscalers), which accounts for the vast majority of revenue for InnoLight and Eoptolink. Therefore, we think the direct commercial impact remains minimal for both the companies. However, the potential of adding Chinese companies to the "Covered List" remains as a long-term overhang, in our view. Given the current shortage of 1.6T optical transceivers and InnoLight's leading market position, we expect the company's fundamental performance to remain robust; as the recent stock weakness has largely priced in the FCC (Federal Communications Commission) restriction scenario, InnoLight remains as one of our top picks.

Optical fiber capacity expansion: the concern about oversupply likely overdone

On 25 Friday, Hengtong Optic-Electric proposed a private placement of up to 740 million A-shares to raise no more than CNY6.64bn, allocated across nine projects. Fiber-related investment projects include 800 tons / year new capacity of preforms, and 1,200 tons / year of high-end optical quartz materials (which can support further expansion of preforms capacity in future).

FiberHome (600498 CH, Not rated)'s private placement plan (up to CNY2.91bn) was announced on 11 July 2026, targeting to add 600 tons / year of preform capacity. Relative to the market demand gap driven by global AI infra construction, we think the capacity expansion plans from both the top-tier manufacturers are not aggressive, and the increased capacity is unlikely to trigger a reversal in the supply-demand structure in the near-term, in our view. However, Hengtong's announcement on 25 Sept could add to concerns about the potential oversupply in China's optical fiber market in the long-term. We remain positive on the near-term trading opportunities in YOFC and T&S Communication for their potential upside in global optical fiber / fiber connector markets.



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Fig. 1: Hengtong – capital application of raising funds related to the optics sector

Project name	Total investment amount (CNY mn)	Proposed amount of raised funds to be invested (CNY mn)	Details	Capacity planned
New-generation optical fiber R&D and production project	882.3	758.0	Build multi-core fiber optics, ultra-low loss multi-core fiber, polarization-maintaining fiber, air-core fiber, and multimode fiber specialty fiber production lines	800,000 fkm/year multi-core optical fibers; 100,000 fkm/year ultra-low loss multi-core fibers; 30,000 fkm/year polarization maintenance fibers; 100,000 fkm/year hollow-core optical fibers; and 2.5mn fkm/year multimode optical fibers
Inner Mongolia optics high-end optical new materials construction project	1040.8	862.0	Build production capacity for fiber optic preforms, along with supporting production capacity for high-purity quartz materials	800 tons/year of fiber preforms, 1,200 tons/year of high-end optical quartz materials, and 6mn fkm/year of optical fibers
Hengtong data intelligent communication project	813.9	281.0	Build high-density optical cable production lines for datacom scenarios	50mn fkm/year MPO cables

Source: Company data, Nomura research

Fig. 2: FiberHome – capital application of raising funds related to optics

Project name	Total investment amount (CNY mn)	Proposed amount of raised funds to be invested (CNY mn)	Details	Capacity planned
Multimode & Specialty Fiber Smart Manufacturing	1,047.7	942.2	Production lines cover multi-mode fibers, polarization-maintaining fibers, laser fibers, and other categories	2mn fkm/yr multimode fiber; 173,000 fkm/yr specialty fiber
Ultra-Large-Specification Fiber Preform Industrialization	547.8	528.1	Mainly used for the R&D and production of optical fiber preforms	600 tons/yr preform and 45 tons/yr core rod, using 0.3m x 3.5m spec
Thailand Fiber Industry Base	361.0	361.0	Construct fiber optic production base	20mn km/yr fiber output
Hollow-Core Fiber Key Performance R&D	281.2	281.2	Developing hollow-core optical fiber products with low latency, high bandwidth, and anti-interference characteristics	-

Source: Company data, Nomura research

Switch chip localization: still a long way to go but the trend is inevitable

Last week, a Financial Times news report highlighted the China SASAC's investigation into the usage of Broadcom chips in Chinese data centers (*news*), signaling a strong mandate to increase the localization rate of the supply chain, in our view. According to the news, the penetration rate of Broadcom switches among state-owned companies could be as high as 90% and Chinese regulators may be pushing Chinese companies to adopt more domestic switch chips. We think domestic switch chip players have made notable progress, but still trail global leaders by approximately 1-2 generations:

- HiSilicon (Unlisted): HiSilicon has achieved commercial deployment of 51.2T switch chips in the AIDC market, based on 112G SerDes and Huawei (Unlisted)'s proprietary UB protocol. Its switch chip has been integrated into CloudEngine XH9230-128DQ and CloudEngine 9866-128DQ switches.
- Centec Networks (688702 CH, Not rated): Centec's 25.6T switch chip (supporting 800G ports and UEC standards) was shipped to China's cloud service providers (CSPs) in 2026 and the company's 51.2T switch chip is still in R&D stage.

While Broadcom has been shipping 102.4T switch chip, Chinese players are still 1-2 generations behind, in our view. However, we think the localization trend is inevitable in China's networking switch & switch chip market. We believe Unisplendour, through its cooperation with Centec, is poised to benefit from this trend in the long run.