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China Communications Infrastructure

Quick Thoughts on Potential FCC Restrictions on 3.2T Optical Modules

CITI'S TAKE

During our recent investor discussions, we observed heightened investor focus on the FCC's potential future restrictions on high-end optical module imports into the US. Investors asked about potential FCC restrictions on the origin of core component value in next-generation 3.2T modules; the most negatively impacted companies would be those with exposure to critical components such as optical chips given the BOM requirement for US content. If US-original value share is required, the room for gross margin improvement may be limited. But it is also positive for leading module makers that 3.2T migration will continue in 2028. And the leaders, such as **Innolight**, would benefit given its advancement in technology preparation, efficient production ramp and comprehensive supply chain support (including DSP, optical chips, PD, etc.).

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Investors discussed a possible FCC regulated framework that could impose requirements that a certain level of industrial value in an optical module must originate from the US. It is possible that DSP, photodiode (PD), optical chips (EML, CW laser) components could be required to be US or US-partner originated; we believe electrical and optical chips and module in the optical transceiver accounts for c.70% of BOM. Currently DSPs are basically from US vendors but made in Taiwan, some optical chips are from US and Taiwan while the majority of PD chips are made in Taiwan and US.

Current Policy and Regulatory Status: No enacted FCC rule currently restricts Chinese optical module exports to the US; Innolight, Eoptolink, and DSBJ are not on the FCC Covered List as of today.

3.2T Volume Ramp: we forecast 3.2T optical transceiver shipments commencing from a small shipment in 2027E and ramping up in 2028E. We see the major financial impact on potential 3.2T restriction will only come in after 2027. We forecast 31% / 4% of Innolight/ Eoptolink revenue in 2028 from 3.2T optical transceiver. Yet, we do not know if NPO will be included; we see many industry activities happening this year, and sampling to start in 3Q/4Q26. As for Innolight, it also received NPO orders from customers for 2027 shipment; we believe the products could possibly get FCC approval before restrictions.

See Appendix A-1 for Analyst Certification, Important Disclosures and Research Analyst Affiliations

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Dongshan Precision

(002384.SZ; Rmb167.4; 1; 30 Sep 26; 15:00)

Valuation

We use SOTP methodology to derive our TP of Rmb282. We apply (1) 15x 26E P/E to DSBJ's original biz (past 5-year average); (2) 15x 27E P/E to the optical transceiver biz, in-line with the optical transceiver names average fwd P/E; (3) 50x 27E P/E to the optical chip biz, in-line with the optical chip names' average fwd P/E; (4) 20x to the 27E AI-PCB biz, in-line with PCB names' average fwd P/E.

Risks

Key downside risks that could impede the stock from reaching our TP include: (1) slower-than-expected progress in modules FPC and share gain from overseas peers; (2) slower-than-expected Tesla business growth due to fierce competition in the China NEV market; (3) continued optoelectronic business loss due to weak demand and intensified competition; (4) increasing materials costs; and (5) US-China geopolitical risk.

Eoptolink Technology

(300502.SZ; Rmb389.0; 1; 30 Sep 26; 15:00)

Valuation

Our target price for Eoptolink of Rmb701 is based on 20.0x FY27E, set at -0.5SD the 5-year historical mean to reflect a strong 800G/1.6T cycle, ASIC and Scale-Up Opportunity at CSP customers on the one hand and CPO cannibalization at its key customer Nvidia on the other.

Risks

Downside risks that could impede the stock from reaching our target price include: 1) slower-than-expected data center investments, 2) lower-than-expected optical network capex by telcos and corporates/governments in China, 3) margin pressures due to price competition, 4) slower-than-expected expansion of new customers, 5) China-US tech disputes and 6) faster-than-expected CPO deployment.

Innolight

(3308.HK; HK$1072.0; 1; 02 Oct 26; 16:10)

Valuation

Our target price for Innolight H-shares of HK$1,524 is based on 16.2x FY27E forward PE, set 1SD below Innolight A-share's three-year historical mean, reflecting the sector-wide overhang on FCC rules impact. That target P/E is also equivalent to a very slight premium to the direct peers' current trading average, and we believe is reasonable in the context of 129%/149% forecast three-year revenue/earnings CAGR. It also is in sync with our valuation approach to Eoptolink, which is likewise set at a discount to historical mean.

Risks

Our quant risk-rating screen suggests a High Risk flag for the H-shares given their short trading history (listed July 2026); however, we think a High Risk flag is not appropriate given the shares already have a lengthy trading history in the Shenzhen market, and also given the company's scale and track record. Downside risks that could impede the shares from reaching our target price include high customer concentration; intense competition; market demand cyclicality; technology risks; supply chain and manufacturing risks; and geopolitical and trade risks. Specific risks include1) slower-than-expected AIDC investments; 2) weaker-than-expected telecoms market expansion; 3) margin pressures due to price competition; and 4) China-US tech disputes intensifying.

