Sector note

07 Dec 2022

CONSTRUCTION & MATERIALS: BUILD RESILIENCE FOR THE TOUGH TIMES

- We believe public investment will back to centre stage in 2023F, partially offsetting the weakening residential property segment.
- Basic materials prices are on the mend which likely blow tailwind for a few industries among this sector.
- We like companies that might ride on upcoming infrastructure development. Our stock picks are HPG, C4G while PLC is on watchlist**.**

Public investment will back to centre stage in 2023F

According to our estimates, disbursement of public investment in 2023F could increase by 20-25% yoy. We have optimistic view on the infrastructure development into 2023F as the issues of stone shortage and high building material prices have mostly been addressed. Mega infrastructure projects in the near-term pipeline include twelve sub-projects of East North-South Expressway (NSE phase 2), Long Thanh Int'l Airport, Ring road 4 (Hanoi) and Ring road 3 (HCMC).

Chances for top construction players to win the large-scale projects

Since Sep 22, Ministry of Transport has been allowed to directly appoint contractors for NSE phase 2 which is expected to shorten the time of project implementation. Financial capability and construction experience are critical criteria for selecting contractors. We believe top players with strong track-record profiles, ie: VCG, HHV, C4G, etc. ... are likely to win the large portion of bidding packages. Additionally, we see 2023F could be a turnaround for construction stone and asphalt producers following the time lines of existing projects.

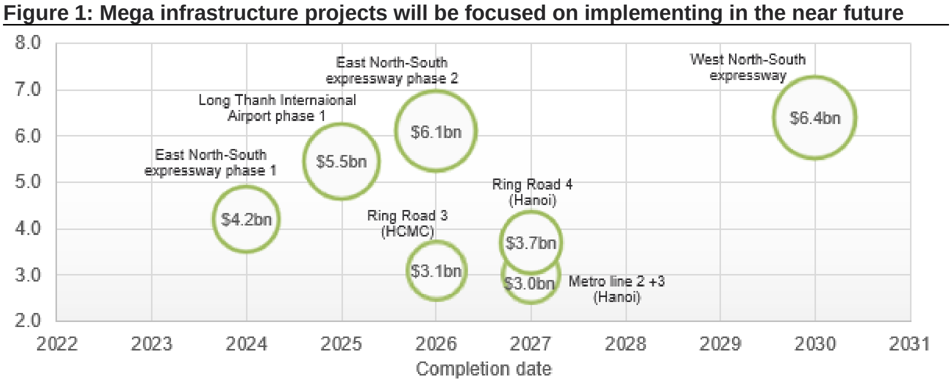
Headwinds persist with steel and cement industry

Vietnam's steel and cement manufacturers have struggled with declining global construction demand, elevated input materials and increasing supply gluts since 3Q22. Look into 2023F, the stagnant residential property will cast shadow over these segments. However, a few signals that could be frontal passages for wind change in late-23, include: easing basic materials prices (coking coal, steel scrap), the re-openings of Chinese might boost the demand, and the acceleration in infrastructure development might partially offset the residential construction.

Our stock picks are HPG, C4G while put PLC on watchlist

We prefer companies that ride on upcoming infrastructure development (**C4G, PLC**). For **HPG**, its current valuation is attractive with limited downside risks given its leading position in the Southeast Asian steel industry and healthy balance sheet to allow HPG to grab more market share during the industry downcycle. Downside risks include sluggish disbursement of public investment, higher-than-expected interest rates, commodities price upturn maintain.

Figure 1: Mega infrastructure projects will be focused on implementing in the near future



Source: VNDIRECT RESEARCH, COMPANY REPORTS

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Riding on the infrastructure development acceleration

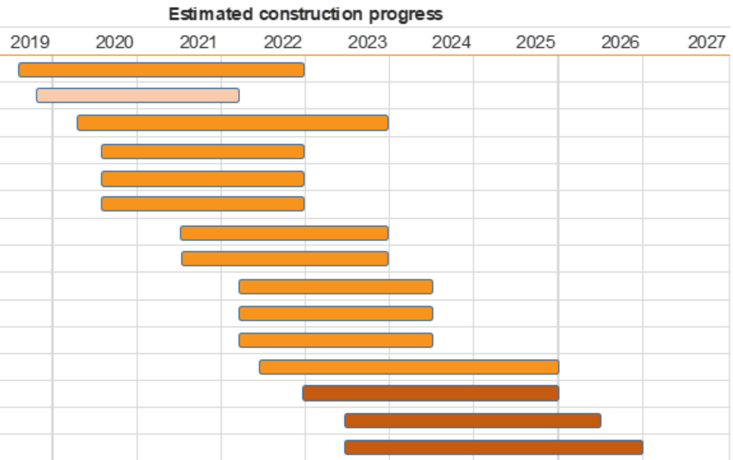
North-South Expressway (NSE) phase 2 in focus

In order to counter the slowdown of other growth engine, the government targets to push public investment in 2023F with VND793tr in disbursement pipeline (+34% versus 2022). We believe that the disbursement of public investment in 2023 could increase by 20-25% compared to the actual disbursement in 2022 thanks to (1) the bottleneck of construction stone shortage has been addressed as the government has licensed for new mines, (2) the prices of construction materials such as steel, cement, construction stone are gradually cooling down.

According to Ministry of Transport (MoT), key infrastructure projects will start construction in late-2022, including: East North-South expressway phase 2 (Dec 22); the passenger terminals and runways of Long Thanh Int'l Airport (Dec 22), Terminal 3 of Tan Son Nhat International Airport (Dec 22), Bien Hoa – Vung Tau expressway (Apr 23) and Khanh Hoa – Buon Ma Thuot expressway (Jun 23). Meanwhile, other eleven sub-projects at the North-South Expressway phase 1 will be completed within 2023-24F.

Figure 2: Many major transport infrastructure projects are expected to be completed in 2022-26F

Project		Total investment (VND bn)
Eleven sub-projects of East North-South expressway (Phase 1)	Cam Lo - La Son	7,700
	Cao Bo - Mai Son	1,600
	My Thuan 2 bridge	5,000
	Mai Son - Highway 45	12,920
	Vinh Hao - Phan Thiet	10,853
	Phan Thiet - Dau Giay	14,360
	Nghi Son - Dien Chau	8,380
	Highway 45 - Nghi Son	6,330
	Dien Chau - Bai Vot	13,340
	Nha Trang - Cam Lam	7,615
	Cam Lam - Vinh Hao	13,690
Long Thanh International Airport (Phase 1)		109,112
Twelve sub-projects of East North-South expressway (Phase 2)		146,990
Ring Road 3 (HCMC)		75,378
Ring Road 4 (Hanoi)		85,813
Total		**519,081**



Notes: Completed | Under construction | Not started yet

Source: VNDIRECT RESEARCH, MOT

Figure 3: North-South Expressway phase 2 is divided into 25 packages with size in range of VND3,000bn – VND8,000bn

Project	Length (km)	Bidding package	Package size (VND bn)
Bai Vot - Ham Nghi	35.3	XL-01	6,045
Ham Nghi - Vung Ang	54.2	11-XL	4,456
		12-XL	3,304
Vung Ang - Bung	56.1	XL-01	5,300
		XL-02	5,400
Bung - Van Ninh	50.0	XL-01	3,939
		XL-02	3,501
Van Ninh - Cam Lo	65.0	XL-01	3,361
		XL-02	3,480
Quang Ngai - Hoai Nhon	88.0	XL-01	3,800
		XL-02	4,500
		XL-03	6,400

Project	Length (km)	Bidding package	Package size (VND bn)
Hoai Nhon - Quy Nhon	70.1	11-XL	3,027
		12-XL	6,140
Quy Nhon - Chi Thanh	61.7	11-XL	3,690
		12-XL	3,055
		13-XL	6,241
Chi Thanh - Van Phong	48.0	XL-01	4,393
		XL-02	4,440
Van Phong - Nha Trang	83.4	XL-01	5,365
		XL-02	3,549
Can Tho - Hau Giang	37.7	XL-01	7,966
Hau Giang - Ca Mau	73.0	XL-01	7,256
		XL-02	3,835
		XL-03	3,334

Source: VNDIRECT RESEARCH, MOT

Direct appointment of contractors for NSE phase 2 will benefit some large players

In order to shorten the time of project implementation, the MoT will be authorized to appoint contractors for NSE phase 2 which will be applied since late-2022 to consultancy, technical infrastructure relocation, compensation for site clearance and re-settlement package deals. A list of criteria was set by MoT to ensure that the projects can be implemented in a transparent way. Top players with track-record profiles include Vinaconex (VCG VN, HOSE), Deo Ca Traffic Infrastructure Investment JSC (HHV VN, HOSE), CIENCO4 Group (C4G VN, UPCOM),… are likely to win the large portion of packages.

Figure 4: Strict conditions in selecting contractors for the North-South expressway phase 2 project

5 groups of criteria for selecting contractors for the North-South expressway phase 2	1. The contractor must have a Class I qualification certificate for road works.
	2. The contractor must have experience in performing a technically similar contract.
	3. The contractor completed the bidding package with a value of at least 50% of the size of the package under consideration.
	4. Ensure financial capacity requirements.
	5. The average contractor's construction revenue in the last 3 years must be equivalent to the size of the package under consideration.

Source: VNDIRECT RESEARCH, MOT

Figure 5: Only a few Vietnamese contractors are capable of executing large-scale bidding packages

Package size (VND bn)	Number of contractors which have completed projects of equivalent size
350-500	18
500-1,000	16
1,000-1,500	7
> 1,500	7

Source: VNDIRECT RESEARCH, MOT

Figure 6: Companies have surpassed the previous strict conditions for winning the bid, thereby enabling them to continue participating in the next major infrastructure projects

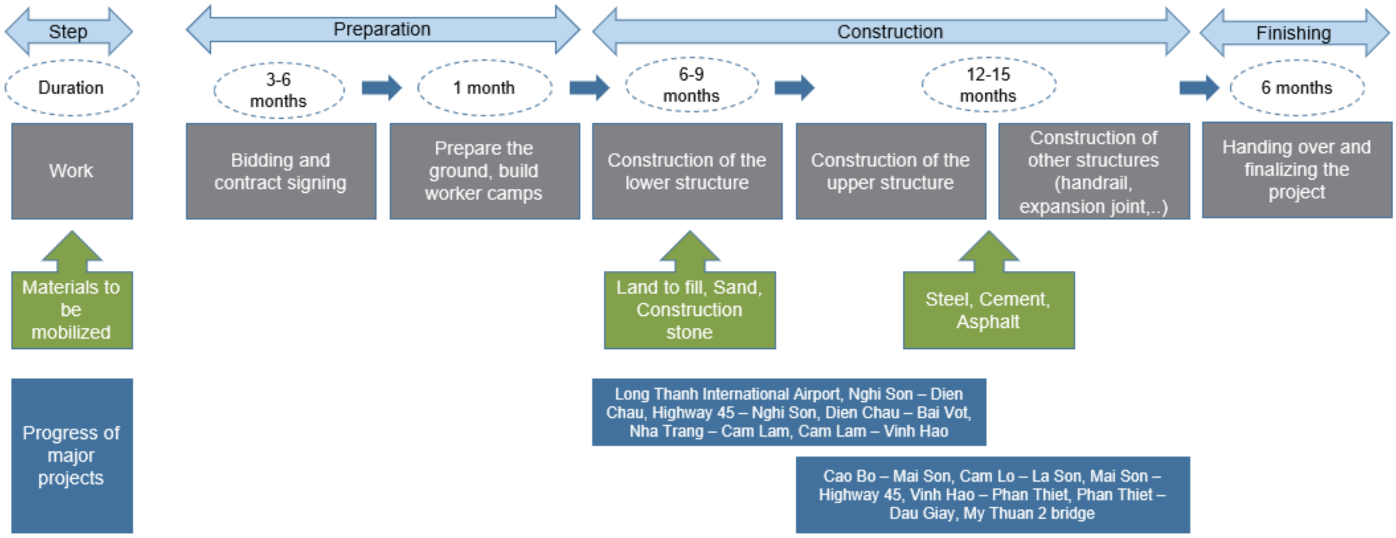
Company	Ticker	Time of establishment	Owner equity at the end of 3Q22 (VND bn)	Average revenue of construction segment in 2019-21 period (VND bn)	Outstanding projects participated: Project	Outstanding projects participated: Package size (VND bn)
Listed company						
Vietnam Construction And Import-Export JSC	VCG	1988	9,970	4,000	Package XL-14 at Mai Son - Highway 45 expressway (NSE 1)	1,573
					Package XL-04 at Vinh Hao - Phan Thiet expressway (NSE 1)	2,289
					Package XL-03 at Phan Thiet - Dau Giay expressway (NSE 1)	1,725
					Package XL-03 at Nghi Son - Dien Chau expressway (NSE 1)	886
					Package XL-03 at Highway 45 - Nghi Son expressway (NSE 1)	560
					Package XL-10 at Van Don - Mong Cai expressway	402
Lizen JSC	LCG	2001	2,553	2,226	Package XL-02 at Highway 45 - Nghi Son expressway (NSE 1)	350
					10 packages at Huu Nghi - Chi Lang expressway	1,207
					Van Don - Tien Yen expressway	602
					8 packages at Bac Giang - Lang Son expressway	1,532
Deo Ca Group JSC (the parent company of HHV)	HHV	1985	10,811	1,879	Package XL-12 at Mai Son - Highway 45 expressway (NSE 1)	672
					Package XL-01 at Nghi Son - Dien Chau expressway (NSE 1)	302
					Cam Lam - Vinh Hao expressway (NSE 1)	1,939
					Trung Luong - My Thuan expressway	3,287
					Package XL-08 at Cua Luc 3 bridge	647
					Package XL-08 at Cua Luc 1 bridge	567
CIENCO4 Group JSC	C4G	1982	2,455	1,435	Package XL-02 at Phan Thiet - Dau Giay expressway (NSE 1)	859
					Package XL-04 at Nghi Son - Dien Chau expressway (NSE 1)	455
					Package XL-02 at My Thuan - Can Tho expressway	296
					Dien Chau - Bai Vot expressway (NSE 1)	1,673
Dat Phuong Group JSC	DPG	2002	2,096	1,002	Package XL-01 at My Thuan 2 brigdge (NSE 1)	590
					Package XL-01 at Vinh Hao - Phan Thiet expressway (NSE 1)	400
					Package 1A at Tan Van - Nhon Trach highway	549
Vina2 Invest and Construction JSC	VC2	1989	693	630	Dien Chau - Bai Vot expressway (NSE 1)	1,673
Unlisted company (estimated financial figures)						
Son Hai Group JSC		1998	2,377	1,368	Package XL-01 at Nghi Son - Dien Chau expressway (NSE 1)	1,159
					Package XL-07 at Cam Lo - La Son expressway (NSE 1)	
					Package XL-10 at Mai Son - Highway 45 expressway (NSE 1)	
Truong Son Construction Corporation		1989	NA	3,373	Package XL-13 at Mai Son - Highway 45 expressway (NSE 1)	1,200
					Package XL-02 at My Thuan - Can Tho expressway	
					Package XL-02 at Cam Lo - La Son expressway (NSE 1)	
Phuong Thanh Traffic Construction and Investment JSC		1999	961	1,800	Package XL-02 at Phan Thiet - Dau Giay expressway (NSE 1)	911
					Package XL-R6B at Tien Yen - Mong Cai expressway	1,021
					Package XL-16 at Ha Long - Hai Phong expressway	700

Source: VNDIRECT RESEARCH, COMPANY REPORTS

Asphalt: timing for a profit growth turnaround

The Government urged all contractors of sub-projects at the NSE phase 1 to keep up with initial deadlines. We estimate about 361km/148km/128km of this expressway to be completed in 2022/23/24F, respectively. In addition, NSE phase 2 with 349km of expressway is also expected to be completed in the period of 2023-25F. As asphalt paving is the last-mile construction of road projects, we expect asphalt demand will increase since 4Q22.

Figure 7: Progress of key transport infrastructure projects



Source: VNDIRECT RESEARCH

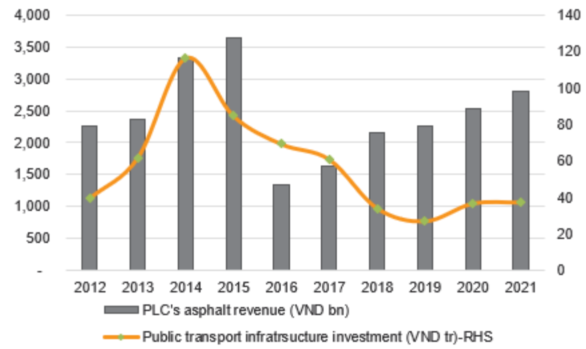
Due to the lack of statistics on Vietnam's asphalt industry, we compare industry sales volume growth based on Petrolimex Petrochemical Corporation – JSC (PLC VN, HNX), which maintained about 30% of domestic asphalt market share in FY15-21, according to PLC. PLC's asphalt revenue jumped during FY2014-15, when the disbursement of public transportation investment rose strongly. Low infrastructure spending in FY16-19 was attributed to a strained government budget and cooling private investment in BOT projects, resulting in a ~50% decline in PLC's asphalt revenues vs. FY2014-15.

Figure 8: Key asphalt manufactures in Vietnam

Company	Capacity (tonnes)	Number of factory	Market share in 2020	Asphalt products offered 60/70	MC	Emulsions	Polymer
PLC	400,000	7	30%	x	x	x	x
ADCo	150,000	4	22%	x		x	x
ICT	120,000	3	15-20%	x		x	x
Transmeco	~ 100,000	2	N/A	x	x	x	x

Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 9: PLC's asphalt revenue jumped during FY2014-15, when the disbursement of public transportation investment rose strongly



Source: VNDIRECT RESEARCH, COMPANY REPORTS

We believe PLC is well positioned to win contracts thanks to (1) its strong warehouse network and its market-leading capacity, and (2) PLC's long-standing relationships with SOEs and a good track record in contract execution.

Construction stone: Eye on Long Thanh Int'l Airport

Due to the industry characteristics, transportation costs often account for a large proportion of construction stone costs. Depending on the distance and type of transportation, the price of stone delivered to a work site may be double the gate price at the mine.

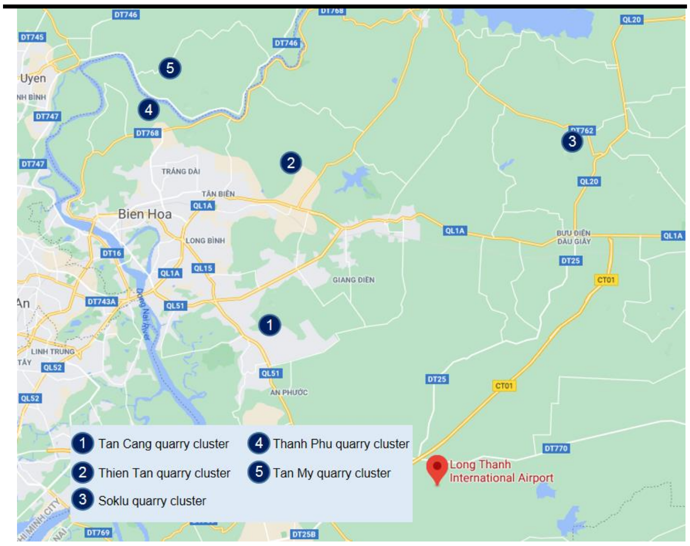
Long Thanh international airport project recently started to build the foundation will be the main growth driver of construction stone demand in the Vietnam Southeast region. We believe that the quarries of companies located near major projects will be prioritised for the supply given the advantages and product quality of these large companies.

Meanwhile, we believe that the licensing of construction stone quarries is facing difficulties in both extending the mining time, increasing the mining capacity and especially in exploiting new quarries due to (1) the opposition of local people when the quarries are causing a lot of negative impacts on the environment and (2) most of the old quarries (with the expiry of the mining life) have not yet carried out the closing procedures mine as committed.

Thus, we believe that listed construction stone enterprises that own many quarries with long exploitation periods, large mining capacity will have many advantages compared to their competitors and will benefit mainly from the Vietnam's huge demand for infrastructure construction in FY22-30F.

We believe listed stone companies that own high quality quarries at favourable locations will supply stone to LTIA, especially the Tan Cang and Thien Tan quarry cluster (owned by KSB, DHA, VLB and DND). We believe this mega project will drive the earnings of construction stone companies in 2023-24F.

Figure 10: Locations of construction stone quarries and LTIA



Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 11: Quarries of listed construction stone companies

Company	Quarry	District	Province	Licensed mining capacity (m3/year)	Exploitation period
KSB	Tan My	Bac Tan Uyen	Binh Duong	1,500,000	Aug-29
	Phuoc Vinh	Phu Giao	Binh Duong	1,200,000	Jan-23
	Thien Tan 7	Vinh Cuu	Dong Nai	280,000	Jan-35
	Go Truong	Tinh Gia	Thanh Hoa	180,000	Jan-45
	Bai Giang	Nghi Loc	Nghe An	150,000	Aug-43
C32	Tan My (*)	Bac Tan Uyen	Binh Duong	1,000,000	Dec-25
DHA	Thach Phu 2	Vinh Cuu	Dong Nai	818,000	Sep-26
	Tan Cang 3	Bien Hoa	Dong Nai	490,000	Mar-37
	Nui Gio	Hon Quan	Binh Phuoc	300,000	Aug-38
NNC	Mui Tau	Tan Lap	Binh Phuoc	1,000,000	Jan-42
VLB	Thach Phu 1	Vinh Cuu	Dong Nai	1,800,000	Jul-42
	Thien Tan 2	Vinh Cuu	Dong Nai	1,500,000	Jun-38
	Solku 2	Thong Nhat	Dong Nai	400,000	Jan-26
	Solku 5	Thong Nhat	Dong Nai	500,000	Jun-25
	Tan Cang 1	Bien Hoa	Dong Nai	1,500,000	Dec-39
DND	Tan Cang 5	Bien Hoa	Dong Nai	1,000,000	Jan-23
	Thien Tan	Vinh Cuu	Dong Nai	354,000	Jan-26
CTI	Xuan Hoa	Xuan Loc	Dong Nai	750,000	Jan-30
	Thien Tan 10	Bien Hoa	Dong Nai	2,000,000	Dec-33

(*) Tan My mine is owned by Mien Dong (HOSE: MDG) – C32's associated company

Source: VNDIRECT RESEARCH, COMPANY REPORTS

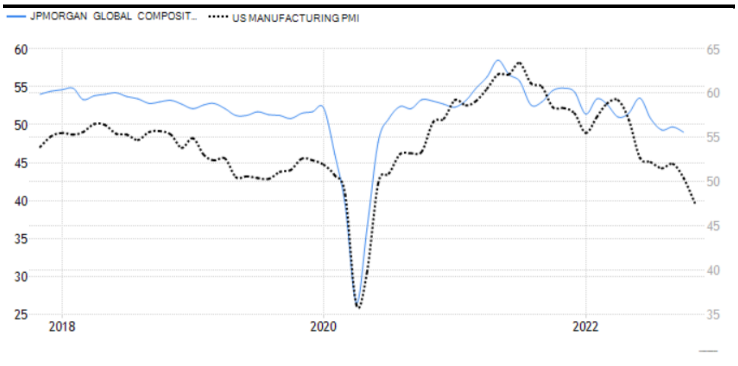
Exports dip on weakening global demand

Global industrial production is declining

In Oct 22, the JPMorgan Global Manufacturing PMI — a broad measure of current conditions in the global manufacturing sector — reached its lowest level (49.4) in over two years. This included a further weakening in new orders, and signals a likely contraction of industrial activity and steel output in the near term.

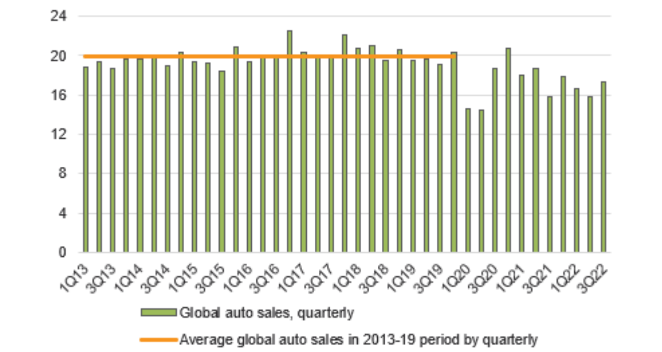
The automotive sector — which typically accounts for around 10-15% of the global total steel consumption - has continued to face disruptions, with COVID-related supply chain shortages further aggravated by fallout from the Russian invasion of Ukraine, and recent outbreaks of the pandemic in China. This led to global auto sales in 2022 being significantly below the 2013-19 average. The weakening global outlook in recent months has also seen a marked drop in steel prices across major markets, particularly flat products such as hot rolled coil (HRC).

Figure 12: Both global manufacturing PMI and US Industrial production sink to the 2-year by Oct 2022



Source: VNDIRECT RESEARCH, TRADING ECONOMICS

Figure 13: Global auto sales in 2022 remain significantly below the 2013-19 average (m autos)



Source: VNDIRECT RESEARCH, BLOOMBERG

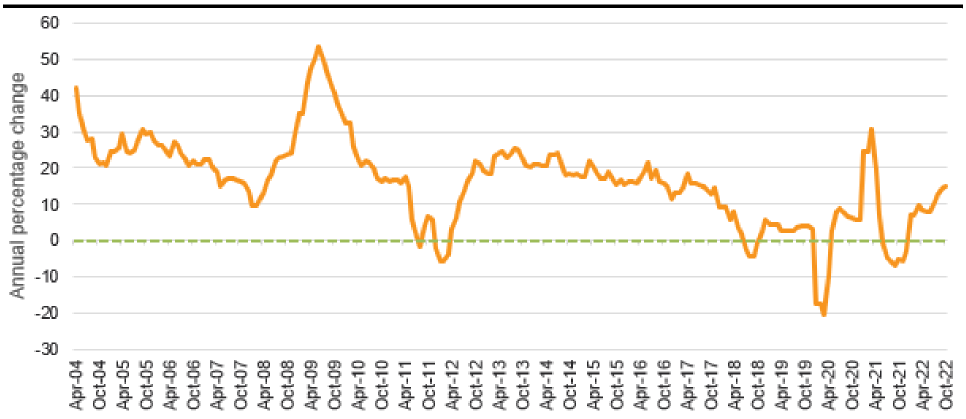
China's construction material demand growth falters amid Covid-19 outbreaks and property sector weakness

The fall in China's construction material demand so far in 2022 reflects renewed Covid-19 lockdowns across many cities from 2Q22 and significant weakness in China's residential property sector.

China's real estate sector has continued to weaken throughout 2022-1Q23F. Housing starts in the year-to-Aug were down 37% yoy, while new home sales over the same period were down 21% yoy. In Aug 22, home prices (China's 70 large and medium-sized cities index) also fell for a 12th straight month.

Infrastructure investment has seen a significant ramp up so far in 2022, with more than 90% of this year's quota of local government special purpose bonds (US$500bn) already allocated in 1H22. In Oct, China's infrastructure investment (3 months average) was around 15% higher yoy. This spending is expected to boost construction activity in the 4Q22 and into 2023. However, it is unclear if the stimulus will fully offset continued weakness in China's property sector.

Figure 14: China's infrastructure investment was around 15% higher yoy in Oct 2022

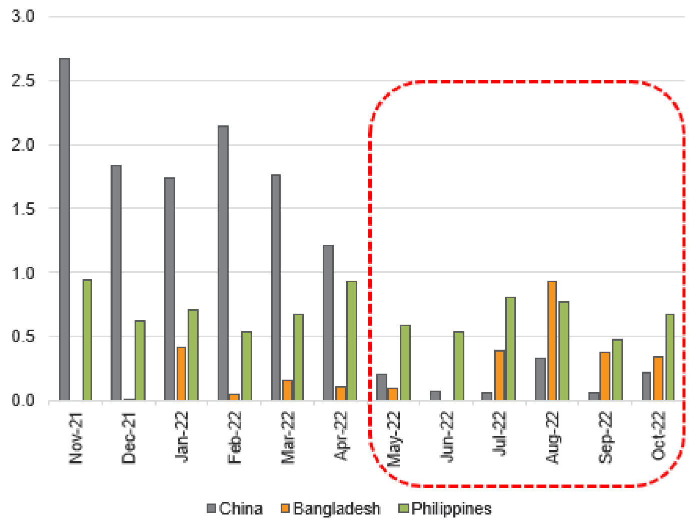


Source: VNDIRECT RESEARCH, BLOOMBERG

Headwind persist for both steel and cement exports till 2H23F

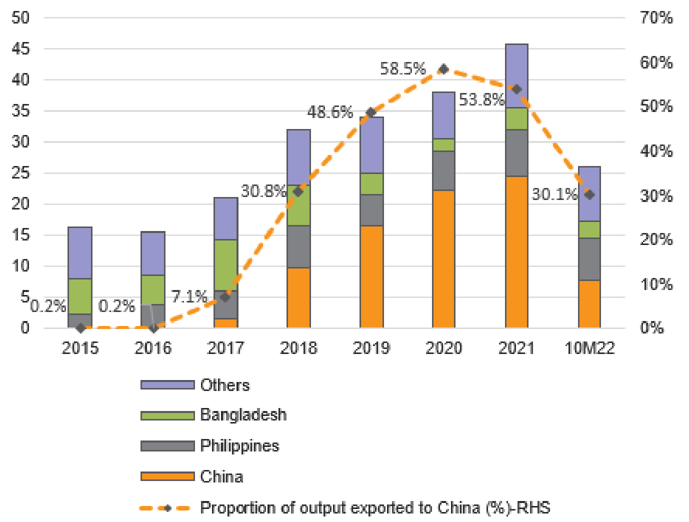
According to the General Department of Vietnam Customs, China is the largest export market of Vietnam's cement since 2018 and accounts for 54% of total export volume in 2021. Thus, Vietnam's cement exporters struggled since May 2022 due to weak construction demand in China as a result of China's zero Covid-19 policy and the cooling real estate market. In 10M22, Vietnam's cement export volume fell significantly 30% yoy, reaching only 26m tonnes.

Figure 15: Vietnam's cement and clinker exports to China fall significantly since May 2022 (m tonnes)



Source: VNDIRECT RESEARCH, GENERAL DEPARTMENT OF VN CUSTOMS

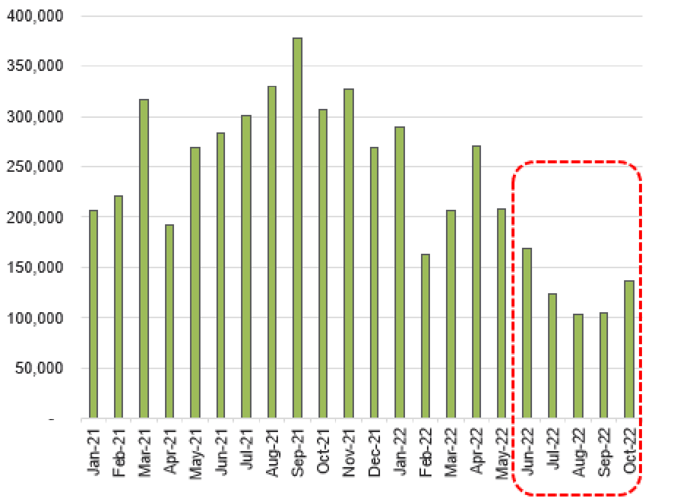
Figure 16: Vietnam's cement depends on exporting to the Chinese market (m tonnes)



Source: VNDIRECT RESEARCH, GENERAL DEPARTMENT OF VN CUSTOMS

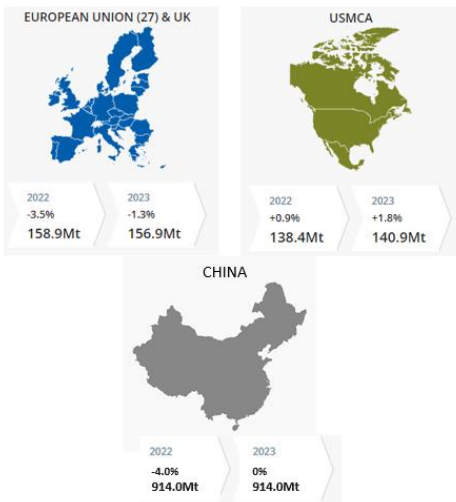
Weak construction demand was also recorded in Vietnam's main steel export markets - the EU and U.S. since May 2022, due to (1) high inflation causing a decrease in real estate demand and (2) critical raw material & energy shortages caused industrial production to decline. In 10M22, Vietnam's galvanised steel export volume decreased by 37% yoy.

Figure 17: In 10M22, export of galvanised steel decreased by 37% yoy (tonnes)



Source: VNDIRECT RESEARCH, VSA

Figure 18: The World Steel Association (WSA) forecasts steel demand in Europe to decrease by 1.3% yoy in 2023, while steel demand in China is almost unchanged



Source: VNDIRECT RESEARCH, WSA

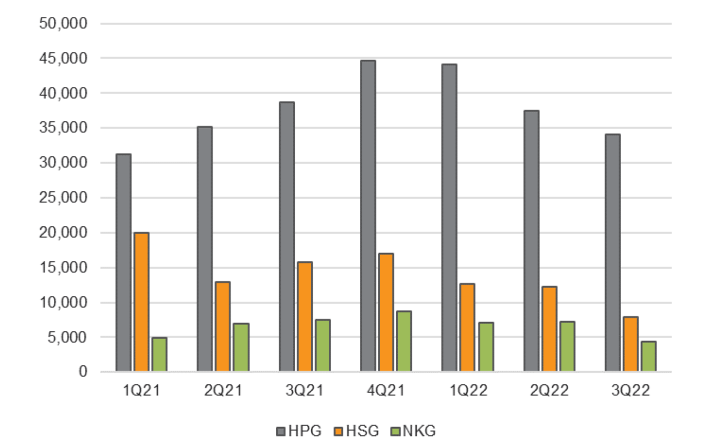
We believe steel and cement exports will still face difficulties in the coming months before the situation improves in 2H23F. This expectation is thanks to (1) stimulus-related infrastructure projects, recent social distancing orders showing signs of easing and real estate sector bailouts gradually taking effect in China, and (2) a recovery in global industrial production as energy shortages gradually cooled down.

Steel sector: Times is getting harder for domestic steel makers

Sluggish performance of steel maker in 2022

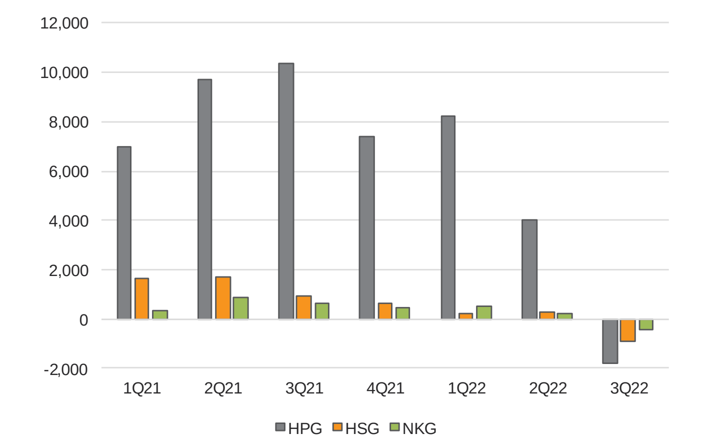
Steel companies all recorded dismal business results in 3Q22. Revenue of the three largest listed steel companies in 3Q22 (including HPG, HSG, NKG) decreased by 25% yoy and 18% qoq due to weak steel demand causing both sales volume and selling price to decline. In addition, high input prices (including coking coal and hot rolled coin), rising interest rates and weakening VND have caused many steel businesses to record net losses in 3Q22. Notably, the largest steel producer in Vietnam - HPG with the advantage economies of scale also had a loss of VND1,776bn in 3Q22, the first loss since 4Q08.

Figure 19: Revenue of the three largest listed steel companies in 3Q22 decreased by 25% yoy and 18% qoq (VND bn)



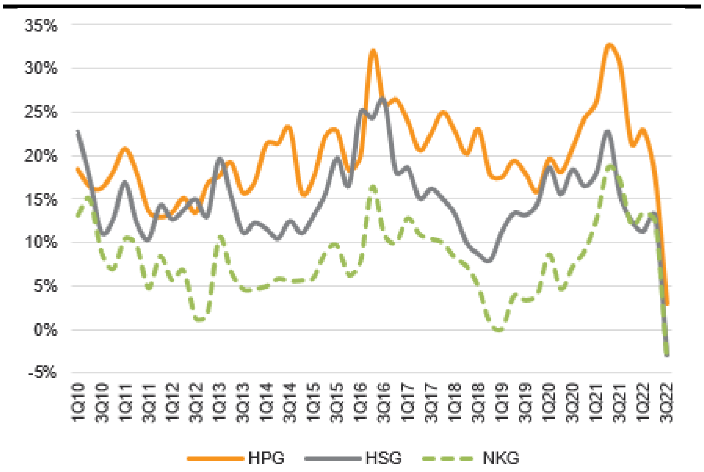
Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 20: Major listed steel companies recorded net profit loss in 3Q22, the first loss seen since 2019 (VND bn)



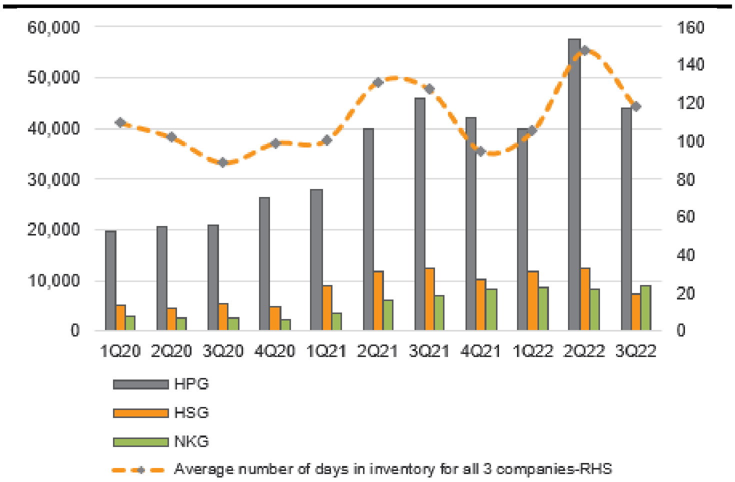
Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 21: GM of Vietnamese's major steel companies in 3Q22 was the lowest since listing



Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 22: At the end of 3Q22, steel companies inventory decreased significantly compared to the previous quarter (VND bn)



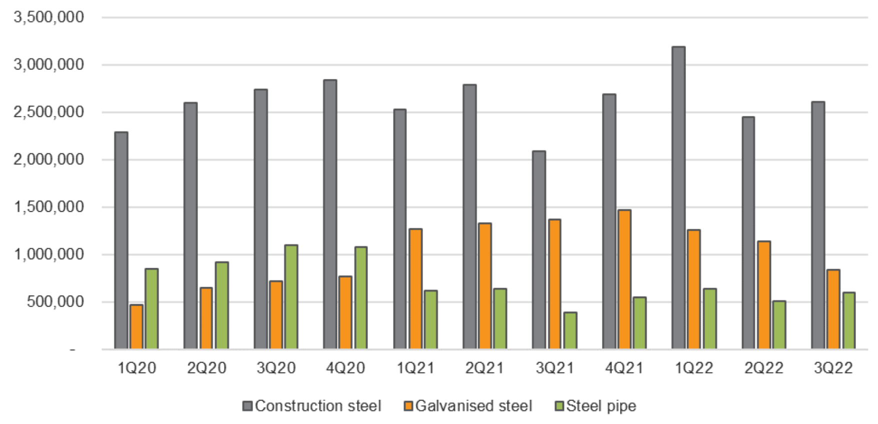
Source: VNDIRECT RESEARCH, COMPANY REPORTS

Despite steel selling price continuously decreased in Oct-Nov, we expect gross margin (GM) of steel companies is expected to recover from 4Q22 as cheaper input costs will materialise. We understand that steel companies have reduced their inventory levels to around two to three months in 4Q22 from four to five months as of end-June this year. This would reduce the risk of any bookings from the inventory provisioning. Meanwhile, spot prices of input materials (including coking coal, steel scrap and iron ore) also have returned to normal levels. Thus, we believe that earnings will bottom out soon for steel companies. Yet, the speed of recovery is quite slow at the moment due to weak demand.

Stagnant residential property will drag down domestic steel demand

Global steel prices across product categories continued to decline in 3Q22 amid weak global demand on fears of a global economic slowdown and lockdown extension in China. In Vietnam, total steel volume (including construction steel, steel pipes and galvanised steel) still increased by 5% yoy to 4.05m tonnes in 3Q22 from low base 3Q21, according to Vietnam Steel Association (VSA). We note that in 3Q21, Vietnam applied strict lockdown measures which massively impacted domestic steel demand. Compared to the same period in 2020, Vietnam's total steel sales volume in 3Q22 decreased by 11%.

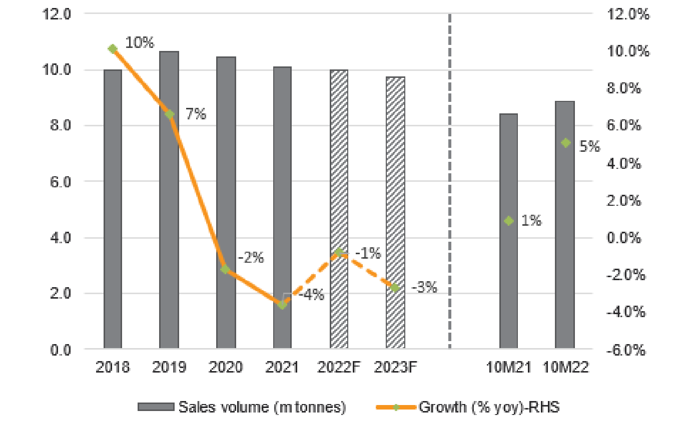
Figure 23: Vietnam's steel sales volume by quarter (tonnes)



Source: VNDIRECT RESEARCH, VSA

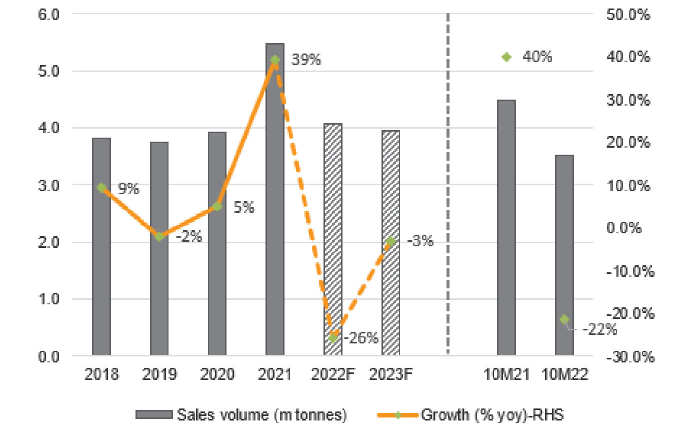
Vietnam's residential property market has cooled down since 2Q22 following some tycoon arrests due to corporate bonds issuance violations, limited credit room for property and rising lending rates to dent the housing demand. Domestic steel industry is also been hit by other headwinds: (1) high input (including coking coal and steel scrap) prices and (2) persistent inflationary pressures had financial conditions tighten across a number of major economies, casting a shadow for global growth prospects. As a result, global steel demand declined, causing difficulties for the export activities of Vietnamese steel companies. Although public investment disbursement is expected to accelerate in the coming quarters, we forecast total domestic steel demand to decline single digits in 2023F. In which, we expect Vietnam's construction steel/galvanised steel sales volume to decrease by 3% yoy in 2023F.

Figure 24: Vietnam's construction steel sales volume will continue to grow negative in 2022-23F



Source: VNDIRECT RESEARCH, VSA

Figure 25: Vietnam's galvanised steel sales volume growth in 2023F will decrease by 3% yoy to the equivalent level of 2020



Source: VNDIRECT RESEARCH, VSA

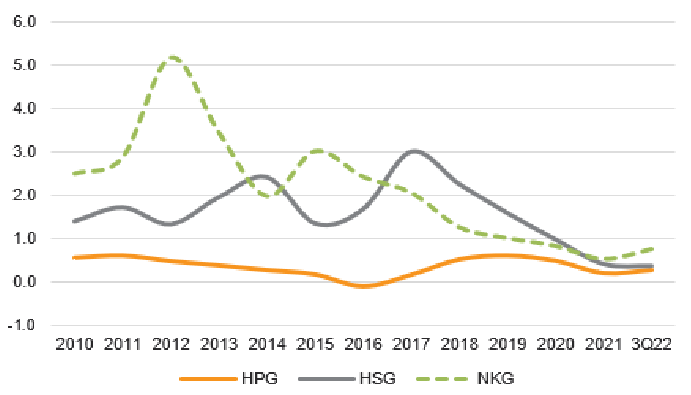
Since late-Sep, several production cuts have been announced: (1) Pomina Steel Corporation (POM VN, HOSE) has announced the closure of its blast furnace - POM 2 factory since 25 Sep 2022; (2) Southern Steel Company Limited has reduced the workload and production output during 4Q22, (3) other galvanised steel makers have partially halted their production and (4) HPG plans to close two blast furnaces (out of three) in its Hai Duong factory and two blast furnaces (out of four) at Dung Quat Steel Complex (DQSC) in Nov 2022. If demand continues to fall further towards the end of the year, HPG would consider shutting down one more (the fifth blast furnace) in Dec 2022. With massive shutdown plans for five out of seven blast furnaces at two steel complexes, this sends a negative message regarding HPG management's view on steel demand in the short-term (maybe till the end of 2022 and 1Q23F).

Rising interest rates weighed on borrowing costs

All steel companies have net debt and most of it is short-term. Therefore, in a raising interest rate environment, interest expenses will increase. However, the net debt/equity levels look better than FY10-19 levels (above 1.5x).

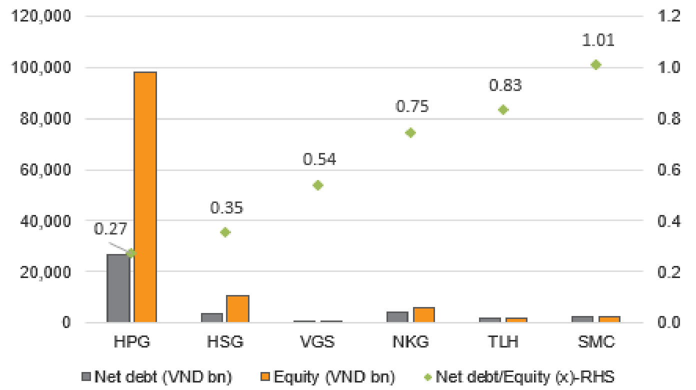
In fact, as of end of Sep-22, HPG has the highest net debt position of VND26,589bn, but net debt/equity was low at just 0.27x. In addition, NKG and HSG also reduced their debt positions over time, and net debt/equity levels for both was in the range of 0.35x to 0.75x as of the end of Sep-22. We note that most debt is short-term to support working capital. With the effort to reduce its inventory in 4Q22, we believe that debt will continue to decline further in 1Q23F.

Figure 26: At the end of 3Q22, Net Debt/Equity ratio of steel companies is still healthier than the 2010-19 period



Source: VNDIRECT RESEARCH, COMPANY REPORTS

Figure 27: HPG has the largest net debt position as of end-3Q22, but net debt/equity is lowest at 0.27x



Source: VNDIRECT RESEARCH, COMPANY REPORTS

When will the positive signal of the steel industry come?

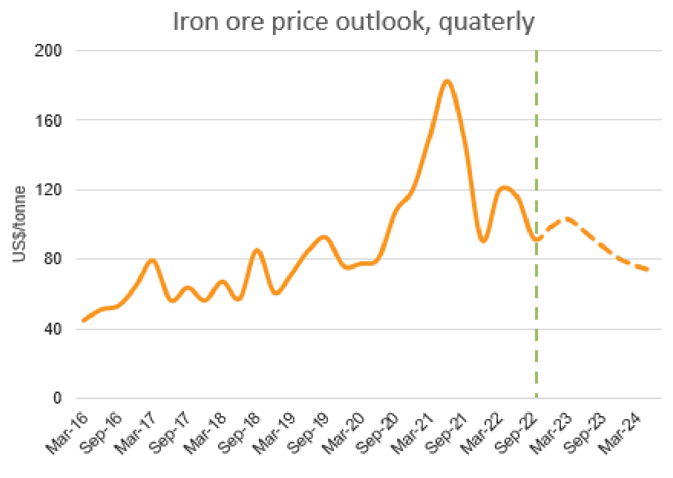
We see a few signals that could be frontal passages for wind change: (1) coking coal prices is forecasted to ease from an average US$420/tonne in FY22F to US$258-220/tonne in FY23-24F as supply conditions normalize; iron ore prices is expected to decline toward longer-run levels from an average US$110/tonne in FY22F to US$90-70/tonne in FY23-24F as weaker demand and more supply; (2) the reopening of Chinese economy will reboot the global steel demand, and (3) the acceleration in Vietnam's infrastructure development will drive up the demand, partially offset the stagnant residential property market.

Weaker demand and more supply to push iron ore prices lower to FY24F

Iron ore prices have fallen by around 45% to US$80/tonne from the peak in Apr 2022. Combined with growing global recessionary fears, new COVID-19 outbreaks and weakness in China's housing sector, have dampened world steel and iron ore demand in recent months.

Over the rest of the outlook period, iron ore prices are projected to decline toward (lower) longer-run levels. This follows more modest growth in blast-furnace steelmaking (compared with the past decade) from major producers such as the EU, US and China, as the world undergoes a transition to a low emissions environment. Slower growth in blast furnace steelmaking capacity will also take place alongside growing supply from Australia and Brazil. Growing global recessionary fears present further downside risks to iron ore prices over this period.

According to Australian Department of Industry, Science, Energy and Resources (DISR) estimates, the FY22F average iron ore price is forecasted to reach US$110/tonne (-29.5% yoy), the benchmark iron ore price is projected to average US$90/tonne in FY23F and around US$70/tonne in FY24F.

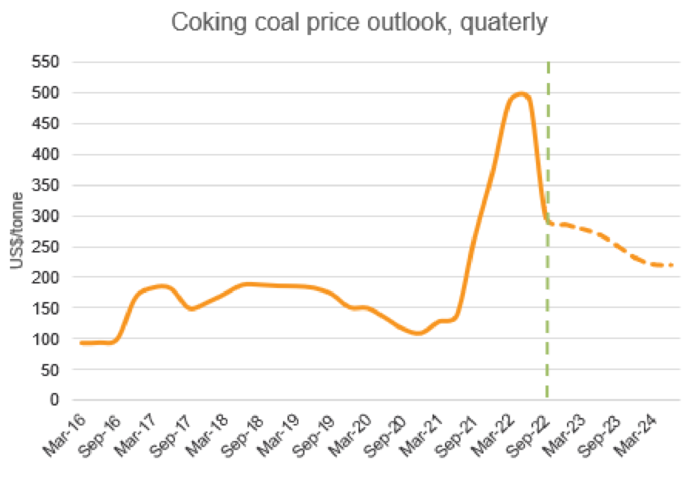


Source: DISR FORECASTS

Coking coal prices are expected to ease gradually

Coking coal prices fell sharply between late May and early July, before recovering slightly. Supply continues to face disruptions from floods in Australia and other weather events, but the fall in demand has allowed market tightness to ease nonetheless. High global energy prices are likely to act as an ongoing curb on steelmaking, especially in China and Europe — where gas shortages are likely to force some moderation in overall energy use over the winter.

DISR forecasts coking coal to ease from an average US$420/tonne in FY22F, but is expected to fall by almost half as supply conditions normalise. Prices are ultimately expected to reach around US$220/ tonne by FY24F.



Source: DISR FORECASTS

Our stock picks are HPG, C4G while put PLC on watchlist

Figure 28: Investment ideas

No	Ticker	1-year TP (VND/share)	Rating	Investment thesis
1	STOCK PICK HPG	20,900	ADD	HPG is traded at 8.1x FY22F P/E and 6.5x FY23F P/E, not very attractive for short-term investment amid sector downtrend. We have no idea about the inflection point of steel manufacturing segment however we still favor HPG for long-term investment: (1) the leading position in the Southeast Asian steel industry will help HPG to ride on the surge of domestic demand for both civil and transport infrastructure construction; (2) the company's healthy balance sheet with cash-rich will help HPG to grab more market share during the industry downcycle; and (3) Dung Quat Steel Complex 2 (DQSC 2) to bring the HPG's crude steel production capacity by 66% from now to 14.6m tonnes per annum from 2025F onwards. Besides, hot rolled coil (HRC) - the main output product of DQSC 2, is still facing a shortage of supply in the domestic market and depends on imports, thus not putting pressure on HPG's steel oversupply in 2025-30F, in our view.
2	STOCK PICK C4G	13,200	ADD	In infrastructure construction industry, we see that **C4G** is a bright candidate thanks to: (1) it's leading position in transport infrastructure construction in Vietnam; C4G has gradually become "familiar" with large-scale and highly technical projects such as North-South expressway, airport runway, sea bridge... thereby which it has many advantages to continue participating in the next major infrastructure projects in the 2023-25F period; (2) After the issuance to existing shareholders in Jan 2022, C4G's equity at the end of 3Q22 increased by 90% compared to the beginning of the year, which will help C4G significantly improve its financial capacity; and (3) C4G owns many potential assets in real estate projects and is planning to develop such as Cau Cau tourist area, Nghi Hai ecological food court, building at 29 Quang Trung (Nghe An) and 136 Le Van Duyet (HCMC), ...
3	PLC	23,000	ADD	The Government requested all sub-projects at the North-South Expressway not to be delayed; thus, this expressway will have to complete by 361km/148km/128km in 2022/23/24F, respectively. In addition, NSE phase 2 with 349km of expressway is also expected to be completed in the period of 2023-25. As asphalt paving usually takes place in the later stages of road-building projects, we expect asphalt companies to benefit more in 4Q22-23F. We believe PLC is well positioned to win contracts thanks to (1) its strong warehouse network and its market-leading capacity, and (2) PLC's long-standing relationships with SOEs and a good track record in contract execution.
4	FCN	NA	NA	FCN is one of the largest local players in heavy construction with deep expertise in foundation. The company is expected to benefit from a strong wave of public investment disbursement. High raw material prices weighed on the gross margin of construction companies in 2022, the situation will improve in 2023F when input prices gradually decrease. FCN aims to offload its stake of Vinh Hao 6 solar power plant and Quoc Vinh – Soc Trang wind power plant in 4Q22-23F. If successful, the two divestment deals will bring about VND150bn to FCN's net profit over FY22-23F, based on our estimate.

Source: VNDIRECT RESEARCH

Figure 29: FY22-24F earnings forecasts of stocks under coverage

	HPG			C4G			PLC		
	2022F	2023F	2024F	2022F	2023F	2024F	2022F	2023F	2024F
Revenue (VNDbn)	143,541	145,880	160,144	3,270	3,389	3,889	8,358	8,070	7,797
% growth	*-4.1%*	*1.6%*	*9.8%*	*73.5%*	*3.6%*	*14.7%*	*21.7%*	*-3.4%*	*-3.4%*
Gross margin (%)	*14.0%*	*14.6%*	*15.8%*	*12.3%*	*11.8%*	*12.7%*	*11.6%*	*11.9%*	*12.3%*
EBITDA margin (%)	*13.2%*	*15.4%*	*17.1%*	*14.0%*	*14.0%*	*15.0%*	*3.6%*	*4.1%*	*4.7%*
Net profit (VNDbn)	11,213	13,869	16,619	165	169	196	156	173	191
% growth	*-67.5%*	*23.7%*	*19.8%*	*166.5%*	*2.2%*	*15.8%*	*-10.4%*	*10.8%*	*10.3%*
EPS (VND/share)	1,832	2,265	2,702	733	750	869	1,889	2,093	2,309
BVPS (VND/share)	16,985	18,881	21,307	11,104	11,563	12,156	18,480	18,922	19,595
Net cash/share (VND/share)	-6,001	-7,706	-8,562	-13,184	-14,917	-14,445	-4,750	-4,514	-4,993
D/E	0.47	0.47	0.40	1.40	1.49	1.38	0.98	0.96	0.93
Dividend yield (%)	3.3%	3.3%	3.3%	0.0%	3.9%	3.9%	8.9%	8.9%	8.9%
ROAE (%)	11.8%	13.3%	14.2%	8.9%	6.6%	7.3%	10.9%	11.5%	12.3%
ROAA (%)	6.2%	7.0%	7.5%	2.0%	1.9%	2.1%	3.2%	3.4%	3.7%

Sources: VNDIRECT RESEARCH

Figure 30: Construction & Materials sector comparison

Company	Ticker	Price	TP	Recom.	Mkt cap	P/E (x)		3-year EPS	P/B (x)		EV/EBITDA (x)		ROE (%)	
		LC$	LC$		US$ m	TTM	FY22F	CAGR (%)	Current	FY22F	TTM	FY22F	TTM	FY22F
Steel														
Hoa Phat Group JSC	HPG VN	18,700	20,900	Add	4,533	7.0	10.2	68.3	1.1	1.1	7.3	7.4	17.0	11.8
Hoa Sen Group	HSG VN	12,000	na	na	299	27.4	2.9	177.0	0.7	0.4	6.4	4.6	2.2	7.0
Nam Kim Steel JSC	NKG VN	12,100	na	na	133	4.3	na	391.1	0.6	0.6	2.1	10.9	13.5	(1.0)
Average						*12.9*	*6.6*	*212.2*	*0.8*	*0.7*	*5.3*	*7.6*	*10.9*	*5.9*
Median						*7.0*	*6.6*	*177.0*	*0.7*	*0.6*	*6.4*	*7.4*	*13.5*	*7.0*
Cement														
Ha Tien 1 Cement JSC	HT1 VN	10,100	na	na	160.7	15.5	15.8	(7.4)	0.8	0.7	4.7	4.8	4.7	5.0
Bim Son Cement JSC	BCC VN	8,200	na	na	42.1	12.7	na	(1.4)	0.5	na	3.5	na	3.5	na
But Son Cement JSC	BTS VN	6,400	na	na	33.0	9.7	na	139.6	0.5	na	5.0	na	5.6	na
Average						*12.6*	*15.8*	*43.6*	*0.6*	*0.7*	*4.4*	*4.8*	*4.6*	*5.0*
Median						*12.7*	*15.8*	*(1.4)*	*0.5*	*0.7*	*4.7*	*4.8*	*4.7*	*5.0*
Construction stone														
Binh Duong Minerals & Construction JSC	KSB VN	15,800	na	na	50.3	6.4	na	(8.9)	0.6	na	4.6	na	10.1	na
Nui Nho Stone JSC	NNC VN	17,700	na	na	16.2	21.3	na	(32.1)	1.2	na	50.8	na	3.9	na
Hoa An JSC	DHA VN	30,400	na	na	18.7	6.0	na	11.7	1.0	na	2.3	na	14.2	na
Average						*11.3*	*na*	*(9.8)*	*1.0*	*na*	*19.2*	*na*	*9.4*	*na*
Median						*6.4*	*na*	*(8.9)*	*1.0*	*na*	*4.6*	*na*	*10.1*	*na*
Asphalt														
Petrolimex Petrochemical JSC	PLC VN	19,700	23,000	Add	66.4	11.5	10.4	6.5	1.2	1.0	8.0	8.5	10.3	10.9
Infrastructure construction														
Vietnam Construction and Import-Export JSC	VCG VN	16,700	na	na	338.3	6.0	10.8	37.0	1.2	na	21.3	23.4	5.1	11.0
Dat Phuong Group JSC	DPG VN	29,550	na	na	77.6	5.0	na	38.8	1.2	na	5.0	na	26.3	na
Deo Ca Trafic Infrastructure Investment JSC	HHV VN	8,680	na	na	193.5	8.4	na	123.8	0.3	na	21.6	na	4.2	na
CIENCO4 Group JSC	C4G VN	8,800	13,200	Add	82.4	22.0	12.0	(20.9)	1.1	0.8	12.4	14.0	5.5	8.9
FECON Corp	FCN VN	8,640	na	na	56.7	106.0	13.6	(32.2)	0.5	0.5	12.4	13.5	0.2	4.0
Average						*29.5*	*12.1*	*29.3*	*0.9*	*0.6*	*14.5*	*17.0*	*8.2*	*8.0*
Median						*8.4*	*12.0*	*37.0*	*1.1*	*0.6*	*12.4*	*14.0*	*5.1*	*8.9*

Sources: VNDIRECT RESEARCH, BLOOMBERG, DATA AS OF 07 Dec 2022

DISCLAIMER

RECOMMENDATION FRAMEWORK

Stock Ratings	Definition:
Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings	Definition:
Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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