

POWER GENERATION COMPANY NO. 3 (GENCO 3) – IPO RESULTS

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IPO information

IPO date	Feb 09, 2018
Initial price (VND/share)	24,600
Average successful bid price (VND/share)	24,802
Shares offered (shares)	267,051,900
% of current outstanding shares	12.8%
No of shares successfully sold (shares)	7,451,400
Structure	Primary
Asset valuation (VNDbn)	92,941
Book Value of Equity after revaluation (VNDbn)	26,108
Chartered Capital (VNDbn)	20,809

Key statistics

Market cap @ initial price(VNDbn)	51,190
EPS (VND)	127
ROE	2.3%
P/E (*)	193.7x
P/B (*)	4.5x

(*) Calculated based on initial price;
Genco 3's normalized TTM P/E is 19.4x

Expected ownership after full IPO process

Public	2.8%
Strategic investors	46.1%
ESOP	0.2%
State (EVN)	51.0%

The Genco 3 IPO auction on February 9th, 2018 was not well-received by investors. Given its high leverage and unfavorable short-term prospects, this should have come as no surprise. Nonetheless, we did a little post-mortem of the IPO to dig into the underlying results of the failure. With a series of recent unsuccessful SOE IPOs including that of Vietnam Rubber Group and Becamex, we think there are lessons to be learnt for investors looking to participate in the SOE divestment process.

Genco 3 only sold 2.8% of the total number of shares offered through the IPO. Only 7.5mn shares were sold through the IPO auction, at an average bid price of VND24,802/share. The remaining 10.1% will be offered to strategic investors after the IPO. Compared to PVPower, which is comparable in terms of its size and portfolio of multi-source power plants, Genco 3's IPO was met with far less enthusiasm.

In contrast, PVPower's IPO was successful. All of the shares offered were sold at an average price of VND14,938/share (3.7% higher than the initial price).

Despite its position as the largest power generation company in the country, Genco 3's IPO failed due to the following reasons:

- (1) At the initial price of VND24,600/share, Genco 3's P/E was much higher than its regional peers** and even higher than PVPower's IPO reference valuation which translated into a TTM P/E of 14.8x. Even after excluding the loss from revaluation of foreign currency debt, Genco 3's TTM P/E on normalized earnings was 19.4x (post-IPO share count).
- (2) High leverage and strong exposure to foreign currency debt concerned investors.** Based on its balance sheet as of 9M2017, Genco 3's debt/equity ratio was at 5.9x with 84% of total borrowings denominated in USD, JPY and CNY. Fluctuations in exchange rate cost the company VND2,369bn in 9M2017 in debt revaluation losses, depressing its net income and causing its TTM EPS to fall to only VND127/share. The volatility in earnings due to this forex exposure should warrant a valuation discount to peers, not a premium.
- (3) Unappealing to small shareholders due to less favourable prospects and lack of catalysts in the short run.** We expect Genco 3's financial situation to improve only after a few years, with the involvement of strategic investors. The restructuring of debt will be a long-drawn out process. PVPower and Genco 3 both have plans to increase capacity. However, we assess the development of two gas-based thermal power plants Nhon Trach 3&4 (1,500MW capacity in total, equivalent to 35.7% of current capacity) from PVPower to be more plausible than Genco's new expansion projects as they are already named on the revised Power Development Plan VII. Genco 3's solar power plants (Vinh Tan – Binh Thuan, Srepok 3, Ninh Phuoc 7) and LNG Long Son #1 expansion (amounting to 24.5% of current capacity) may be delayed further in terms of development timeline.

In summary, Genco 3 is a more suitable choice for strategic investors that can participate in and contribute to an improvement in the company's fundamentals over the long-term.

They key takeaway from Genco's IPO failure is that auctions of even landmark state assets can fail if the story is unclear and valuations are unreasonable. Some investors have been tempted to jump on the "big IPO" bandwagon by participating in auctions of large SOEs. A belief was building that a landmark SOE would attract plenty of interest in its IPO, irrespective of fundamentals as these companies tend to plan in monopolistic markets and are "too big to fail". However, the failed auctions of both the industrial park giant Becamex IDC and now Genco 3 have shattered that investment thesis. Investors steered clear of Becamex because of lack of disclosure on the company's land bank status and high leverage, despite the fact that Becamex is the biggest IP developer in Vietnam. Similarly, Genco 3's size and national strategic importance did not compensate for its high leverage and forex exposure. Both companies were priced at a significant premium to regional and domestic peers.

Investors are becoming far more discerning in their choice of IPOs and fundamentals do matter. Investors are unwilling to pay premiums for poorly managed assets, irrespective of size and national importance.

Recent IPO failures are more a function of "cherry-picking" rather than "IPO fatigue". In our 2018 strategy report issued at the beginning of this year, we warned of potential "IPO fatigue" during the latter part of the year as too much supply coincided with a deterioration in quality of IPOs. We think it is too early to conclude that this has set in already, given the strong reception of the PVPower and PVOil IPOs. It is just a sign that investors are going to "cherry pick" which IPOs they want to participate in. With IPOs of some of the best SOEs already behind us, selectivity is the key to making healthy returns on future SOE IPOs.

Figure 1: Peer Comparison

Company	Country	Market					
		Cap (bn US\$)	ROA (%)	ROE (%)	D/E (x)	TTM P/E (x)	P/B (x)
Tata Power Co Ltd	India	4.3	1.0	4.8	3.2	42.6	2.0
Adani Transmission Ltd	India	3.7	3.4	14.8	2.9	55.7	7.9
CESC Ltd	India	2.3	1.8	6.5	1.3	21.3	1.5
Torrent Power Ltd	India	2.1	2.1	6.4	1.3	31.4	2.0
Xinjiang Tianfu Energy CO-A	China	1.2	1.7	6.8	1.7	19.2	1.3
Henan Yuneng Holdings CO-A	China	1.0	0.0	0.1	1.3	n/a	1.0
Sichuan Guanggan AAA Public-A	China	0.8	3.2	7.5	0.4	20.3	1.5
Yunnan Wenshan Electric PO-A	China	0.7	8.6	14.0	0.3	19.1	2.6
Guangxi Guidong Electric-A	China	0.7	1.0	5.0	2.8	35.9	1.9
Leshan Electric Power CO-A	China	0.6	2.4	5.3	0.3	55.6	2.8
Sichuan Minjiang Hydro-A	China	0.6	2.4	5.6	0.9	60.4	3.3
PVPower	Vietnam	1.5 (*)	3.5	8.2	1.1	14.8 (*)	1.2 (*)
Genco 3	Vietnam	2.2 (*)	0.3	2.3 (**)	5.9	193.7 (*)	4.5 (*)
<i>Average</i>		1.5	4.7	13.2	1.6	33.0	2.3
<i>Median</i>		0.8	2.1	6.4	1.3	31.4	1.9

(*): Calculated using the initial price of VND24,600/share for Genco 3 and VND14,400/share for PVPower.

If the loss from revaluation of foreign debt was excluded, Genco 3's TTM P/E would be 19.4

(**): Calculated using the book value of equity on its balance sheet as of the end of 3Q2017

Source: VNDIRECT

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The survey result is as of the date appearing in the Corporate Governance Report of Thai Listed Companies. As a result, the survey result may be changed after that date. CIMBT does not confirm nor certify the accuracy of such survey result.

Score Range:	90 - 100	80 – 89	70 - 79	Below 70 or	No Survey Result
Description:	Excellent	Very Good	Good	N/A	

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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.

Country Ratings

Definition:

- Overweight An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
- Underweight An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

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