

HOA PHAT GROUP JSC (HPG) – AGM NOTE

Market Price VND58,900	Target Price NA	Dividend Yield 0.00%	Rating NON RATED	Sector BASIC MATERIALS
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Outlook – Short term



Outlook – Long term



Valuation



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Hoa Phat Group (HPG) held its AGM last week. The company announced revenue and NPAT targets amounting to a CAGR of 29.4% and 23.3%, respectively over FY17-20. This growth will mainly be driven by its new Dung Quat Steel Complex project. While the current valuation is not cheap, we still see long-term upside in HPG.

Management announced robust targets for FY18-20 although the FY18 earnings guidance looks conservative. At the AGM, HPG announced its guidance for FY18. According to management, last year's net profit included the impact of around VND700bn worth of raw material savings which are one-off in nature. Therefore, it plans for its revenue to grow by 19.1% yoy (-VND55,000 bn) but is targeting flat earnings growth, with its NPAT projected to reach VND8,050 bn (+0.5% yoy). By 2020, the company targets net revenue of VND100 trillion and NPAT of VND15 trillion, equivalent to a CAGR of 29.4% and 23.3%, respectively for FY17-20. We think these targets are achievable and will mainly be driven by the new mega project (Dung Quat Steel Complex).

We expect steel prices to continue gather strength while input prices should stay subdued this year. As a result, margins could be higher than management as projected. Therefore, for FY18, we expect HPG to surpass its annual targets with forecasted revenue of VND60,064 bn (+30.1% yoy) and NPAT of VND9,448 bn (+18.0% yoy). We expect its FY18 EPS to reach VND5,791, translating to a forward P/E of 10.6x at current price.

Dung Quat Steel Complex project is well on track. According to the company, the first rolling line will come on-stream in Jul 2017. This rolling line will add 600,000 tonnes of construction steel (+23.2% increase in HPG's capacity) and begin to contribute to sales volume growth in the second half of this year. The second phase of the project kicked off in Aug 2017 and will commence production by 2019. The company aims to gain market share in central and northern Vietnam with this additional capacity of construction steel, while the remaining 25% of this steel will be exported. We also expect HPG to improve its profitability after the completion of phase 2, by using its HRC products to complete the integrated production chain for other value-added steel products (steel pipe and steel sheet).

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	66,700
52w low (VND)	26,682
3m Avg daily volume (shares)	5.72
3m Avg daily value (VNDmn)	339,501
Market cap (VNDbn)	93,134
Outstanding shares (m)	1,581
Free float (%)	3.0
TTM P/E	11.2
Current P/B	2.77

Ownership

Tran Dinh Long	25.2%
Vu Thi Hien	7.3%
VOF Investment Limited	4.7%
Others	62.80%

Source: VNDIRECT

Financial summary (VND)	12-15A	12-16A	12-17A	12-18E
Net revenue (bn)	27,453	33,283	46,162	60,064
Revenue growth		21.2%	38.7%	30.1%
Gross margin	20.4%	26.3%	23.1%	22.0%
EBITDA margin	20.3%	28.2%	24.5%	26.1%
Net profit (bn)	3,485	6,602	8,007	9,447
Net profit growth		89.4%	21.3%	18.0%
Recurring profit growth				
Basic EPS	4,755	7,833	5,278	6,227
Adjusted EPS	4,156	6,847	4,895	5,791
BVPS	19,706	23,425	21,282	27,073
ROAE		38.6%	30.8%	25.8%

Source: VNDIRECT

The new color galvanised steel factory will come on-stream in May 2018. Penetrating the galvanised steel segment will be a major milestone in HPG's development. We believe that this new product line has potential, as the company already entered the steel sheet segment last year via trading activity with sales volume of 200,000 tonnes realized in that year. HPG expects this steel sheet factory (400,000 tonnes/year) to contribute VND3,000 bn in revenues this year and VND9,000 bn, when running at full capacity, starting from 2019 onwards.

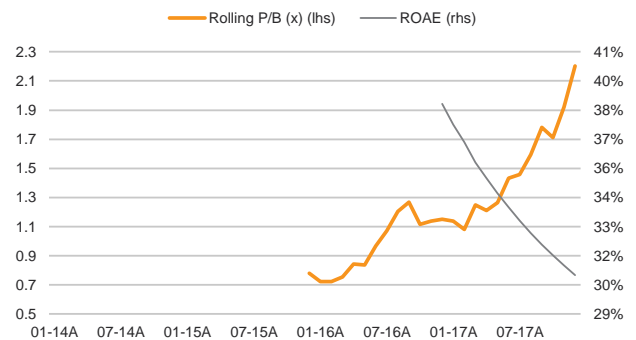
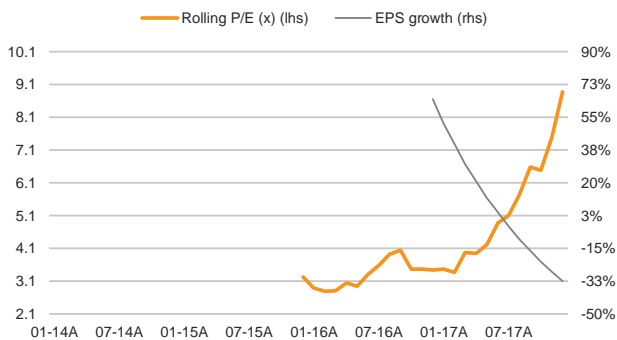
Margins narrowed in 1QFY18. At the AGM, the company announced that 1Q net revenue was approximately VND12 trillion, (+15.0% yoy) and NPAT was VND 2.0-2.1 trillion, (+3.4-8.6% yoy), including VND100 bn from its real estate project (Mandarin Garden 2). Although steel prices continued to increase in 1QFY18, margins still undershot our expectations because of high input price volatility.

The company will pay a 40% stock dividend for FY17 in Q2-Q3 this year. Total new share issuance is estimated at 606.8 million shares, expanding the charter capital to nearly US\$1 bn (VND21,239 bn). The company expects to pay a 30% dividend in FY18, and has not decided whether it will pay this in cash or stock, as it has to conserve cash for Dung Quat project's capex needs. HPG also plans to sell 206,327 treasury shares in the next few months. The guided selling price range is very wide (VND20,000-70,000/share).

Management displayed confidence in addressing shareholders' concerns about competition. According to management, HPG has the ability to compete with Formosa as it is more capital efficient, since capex per tonne is only about a third of that of Formosa. The company is also confident in its plans to build a complete vertically-integrated production chain which will add to its existing advantages of an expansive distribution network and dominant market share. In addition, the new tariff imposed by the Trump administration on steel imports into the US will not negatively impact HPG, as sales volume to the US market is negligible, only accounting for 1-2% of its total sales volume.

We believe HPG's stock still offers upside over a 12-18 month investment horizon. HPG is currently trading at a forward P/E of 10.6x (based on our EPS forecast), which is a 30% premium to its regional peers. The stock has seen some selling pressure recently in reaction to announcement of US tariffs and the expectation of declining margins in Q1. The 40% stock dividend and plan to sell treasury shares might also disappoint its shareholders. We see that the main drivers in FY18 are just the launch of the steel sheet operation and bookings from Mandarin Garden 2. However, the success of Dung Quat Steel project could be a strong catalyst for this stock over the long term as we expect the company's revenue and profitability to improve significantly in FY19 once production at this new factory ramps-up. We believe that its EPS could reach VND8,704, equivalent to a 2-year forward P/E of 6.8x.

Valuation



Balance sheet

(VNDbn)	12-16A	12-17A	12-18E
Cash and equivalents	4,559	4,265	6,872
Short term investments	694	9,937	937
Accounts receivables	2,395	6,555	5,823
Inventories	10,247	11,769	15,440
Other current assets	289	552	663
Total current assets	18,183	33,077	29,734
Fixed assets	13,778	17,924	41,841
Total investments	126	740	17
Other long-term assets	1,139	1,281	1,320
Total assets	33,227	53,022	72,912
Short-term debt	5,488	11,329	13,949
Accounts payable	6,097	6,487	9,845
Other current liabilities	0	0	(0)
Total current liabilities	11,585	17,815	23,794
Total long-term debt	972	1,651	6,605
Other liabilities	819	1,158	1,330
Share capital	8,429	15,171	15,171
Retained earnings reserve	9,486	13,397	22,183
Shareholders' equity	19,745	32,287	41,072
Minority interests	106	111	111
Total liabilities & equity	33,227	53,022	72,912

Income statement

(VNDbn)	12-16A	12-17A	12-18E
Net revenue	33,283	46,162	60,064
Cost of sales	(24,533)	(35,487)	(46,880)
Gen & admin expenses	(405)	(409)	(721)
Selling expenses	(490)	(643)	(901)
Operating profit	7,856	9,622	11,563
Operating EBITDA	9,530	11,637	16,228
Depreciation and amortisation	(1,674)	(2,015)	(4,665)
Operating EBIT	7,856	9,622	11,563
Interest income	197	186	217
Financial expense	(368)	(556)	(795)
Net other income	17	36	36
Income from associates & JVs	(1)	(0)	(0)
Pre-tax profit	7,702	9,288	11,021
Taxation	(1,096)	(1,274)	(1,563)
Minority interests	(4)	(8)	(11)
Net profit	6,602	8,007	9,447
Adj. net profit to ordinary	6,602	8,007	9,447
Ordinary dividends			
Retained earnings	6,602	8,007	9,447

Cash flow statement

(VNDbn)	12-16A	12-17A	12-18E
Pretax profit	7,702	9,288	11,021
Depreciation & amortisation	1,363	1,870	4,665
Tax paid	(1,096)	(1,274)	(1,563)
Other adjustments	422	1,717	0
Change in working capital	(1,572)	(5,546)	309
Cash flow from operations	6,819	6,056	14,432
Capex	(5,832)	(2,361)	(23,466)
Proceeds from assets sales	8	9	0
Others	88	(9,181)	(0)
Other non-current assets changes	2,608	(6,390)	0
Cash flow from investing activities	(3,128)	(17,923)	(23,466)
New share issuance	1,099	6,742	0
Shares buyback	(0)	(1)	(0)
Net borrowings	(395)	6,520	(2,333)
Other financing cash flow	(2,208)	(1,687)	13,967
Dividends paid	0	0	0
Cash flow from financing activities	(1,505)	11,574	11,633
Cash & equivalents at beginning of period	2,373	4,559	4,265
Total cash generated	2,186	(294)	2,600
Cash & equivalents at the end of period	4,559	4,265	6,864

Key ratios

	12-16A	12-17A	12-18E
Dupont			
Net profit margin	19.8%	17.3%	15.7%
Asset turnover	1.13	1.07	0.95
ROAA	22.5%	18.6%	15.0%
Avg assets/avg equity	1.72	1.66	1.72
ROAE	38.6%	30.8%	25.8%
Efficiency			
Days account receivable	17.0	15.8	19.9
Days inventory	153	121	120
Days creditor	91.0	66.7	76.7
Fixed asset turnover	2.53	2.91	2.01
ROIC	25.1%	17.6%	15.3%
Liquidity			
Current ratio	1.57	1.86	1.25
Quick ratio	0.68	1.20	0.60
Cash ratio	0.45	0.80	0.33
Cash cycle	78.9	70.1	63.4
Growth rate (yoy)			
Revenue growth	21.2%	38.7%	30.1%
Operating profit growth	78.2%	22.5%	20.2%
Net profit growth	89.4%	21.3%	18.0%
EPS growth	64.7%	(32.6%)	18.0%
Share value			
Basic EPS (VND)	7,833	5,278	6,227
BVPS (VND)	23,425	21,282	27,073

Source: VNDIRECT

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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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