

## DAKLAK RUBBER INVESTMENT JSC (DRI - UPCOM) - UPDATE

**Market Price** VND11,500      **Target Price** VND17,700      **Dividend Yield** 4.4%      **Rating** ADD      **Sector** BASIC MATERIALS

### Outlook – Short term



### Outlook – Long term



### Valuation



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### Key changes in the report

- Higher tax expenses across entire horizon
- 8% increase in 2017F tapping volume

### Price performance



Source: VNDIRECT

### Key statistics

52w high (VND)	14,600
52w low (VND)	8,000
3m Avg daily volume (shares)	102,328
3m Avg daily value (VNDmn)	4,286
Market cap (VNDbn)	902
Outstanding shares (m)	73.9
Free float (%)	35

### Ownership

Dakruco	66.6%
Others	33.4%

Source: VNDIRECT

**We maintain our ADD rating for DRI given its attractive valuation and improving tapping volume and yields. However, we lower our target price by 17% as DRI's potential corporate tax obligation has led us to haircut our forecasted earnings. A planned listing on HOSE next year could be a positive price catalyst.**

**Conservative forecast on FY2018 output.** DRI plans to expand tapping area by 546 ha and improve tapping yields on the existing tapping area as the rubber trees are approaching the ideal tapping age (10-14<sup>th</sup> tapping year). However, our base case estimate for 2018 output is still 6% below the expected 2017 level as 2017 output so far has been unusually robust due to supportive weather conditions.

**Higher corporate tax obligation implies a 16-17% haircut to our 2017 and 2018 earnings forecast.** To reflect the possible increased in taxes imposed by the government on future earnings, we change our tax expense calculation to the higher of 1.0% on sales (per Laos tax regulation) or 15% on EBT (per Vietnam tax regulation) across our forecast horizon. It is estimated that this will reduce our FY2017 and FY2018 EAT by VND23billion each.

**Slow earnings growth in 2018 but stronger growth expected in 2019.** We estimate that DRI's 2018 ASP could increase by 5% from 2017 year-end level to VND35.2mn/tonne (+2%YoY). We also back-out the estimated disposal loss of VND35bn from the cashew nut plantation since DRI intends to keep the asset over the long-term. Accordingly, FY2018 EAT could be reported at VND142bn (+1.7% YoY) after accounting for the higher tax expense. In FY2019, 11% volume growth and 10% ASP growth should drive EAT growth of 33%.

**We reduce our target price by 17% to VND17,700/share** mainly due to the expected increase in the future tax burden. Nevertheless, the current cheap valuation (2017F PER of 5.9x) and the earnings recovery expected in 2019 convinces us to maintain an ADD rating on the stock. We also believe that market sentiment on the stock will improve post listing on the HOSE main bourse next year.

Financial summary (VND)	12-15A	12-16A	12-17E	12-18E
Net revenue (bn)	413	401	638	613
Revenue growth	41.4%	(2.9%)	59.1%	(3.8%)
Gross margin	21.4%	33.5%	43.6%	42.3%
EBITDA margin	14.9%	19.1%	40.4%	44.2%
Net profit (bn)	(1)	22	139	142
Net profit growth	(143.7%)		544.2%	1.7%
Recurring profit growth	(143.7%)		544.2%	1.7%
Basic EPS	(20)	296	1,904	1,936
Adjusted EPS	(20)	296	1,904	1,936
BVPS	10,555	10,147	11,051	11,487
ROAE	(0.2%)	2.9%	18.0%	17.2%

Source: VNDIRECT

### Higher income tax burden under double-taxation norms

As mentioned in our initiation report, DRI was originally liable to make annual tax payments of 1.6% (changed to 1.0% from 1 Jan 2017) on the annual rubber revenue in Laos (which is equivalent to 3-4% of our estimated FY2017 EBT). Since its commencement, DRI has not been required to pay taxes in Vietnam due to the parent's loss-making history. According to Circular 96/2015/TT-BTC and practices followed by peers, the incentive tax rate for rubber plantation income in Vietnam is generally 15% into perpetuity and could be lowered in certain circumstances. In fact, the document does not clearly state whether an off-shore rubber plantation, such as the ones operated by DRI are subject to the same tax rate. However, it appears now that under the double-taxation norms between Laos and Vietnam, rubber companies are expected to pay the higher of the following two in taxes: a) 15% on EBT and, b) 1.0% on revenue.

**Figure 1: EPS projection based on tax treatments (VND/share)**

Tax rate	2017F	2018F	2019F
Exempted	2,153	2,194	2,942
10%	2,016	2,050	2,739
15%	1,904	1,936	2,587
20%	1,792	1,822	2,435

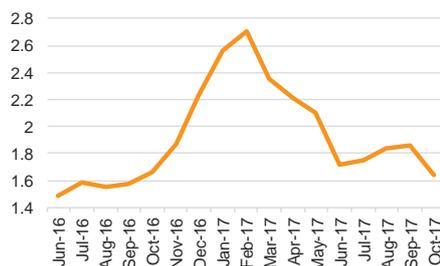
Source: VNDIRECT

Although DRI is waiting for a final decision from the Dak Lak tax office on the tax rate, our base case assumption is that that DRI could be bound to the Vietnam tax rate of 15% applied on EBT. We also deduct tax paid in Laos (1.0% on sales) from the tax payable in Vietnam based on the double taxation relief norms. It is worth nothing that parent company of DRI is operating in the tax jurisdiction as DRI's major shareholder (Dakruco) which is currently subject to a tax rate of 10% on rubber exploitation operations. DRI may possibly achieve this rate in its negotiation with the tax office in our best case scenario. The retroactive tax payable on past annual income is almost non-existent because the tax paid in Laos already surpasses the tax that would be owed if the new tax rate were applied retroactively.

### Output continues to outstrip the 2017 target

DRI's tapping volume reached 4,679 tonnes in 3Q 2017 (+14% YoY) and amounted to a YTD tapping volume growth of 25% YoY. DRI has exceeded its 9-month volume target by 25% and 4Q 2017 output could be outstanding thanks to the continuing favorable weather conditions. However, we remain conservative on 4Q 2017 output at 6,344 tonnes (+4.4% YoY). Total 2017 output is estimated at 18,573 tonnes (+26% YoY) with an average tapping yield of 2.4 tonnes/ha.

**Figure 2: Rubber price (US\$/kg)**



Source: VNDIRECT, SICOM

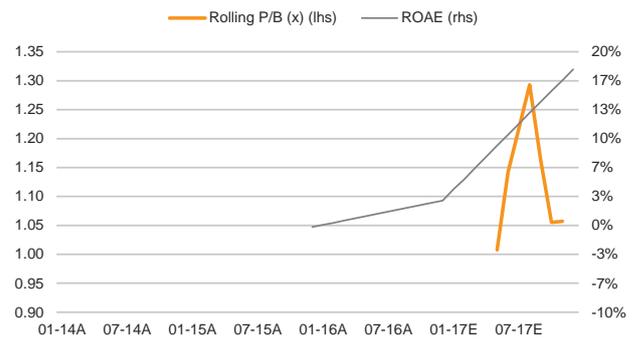
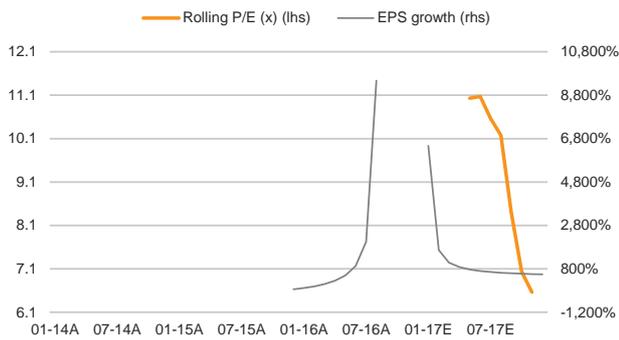
We believe the 4Q 2017 rubber ASP for DRI will remain stable at around VND33mn/tonne. DRI could record VND638bn in sales (+59% YoY) and VND241bn of operating profit (+115% YoY) from selling rubber in 2017. In 3Q 2017, DRI executed a VND22bn receivables write-off which was clarified in the latest audit report and led us to reduce our forecasted 2017 earnings. We also raise our 2017 CIT expense as mentioned above and estimate the 2017 EAT at VND139bn, 6 times higher than was realized last year.

**Figure 3: Forecast revision**

VNDbn	2017F			2018F			2019F		
	Old	New	%Δ	Old	New	%Δ	Old	New	%Δ
ASP (VNDmn/tonne)	33	35	5%	34	35	2%	38	39	2%
Tapped volume (tonne)	17,232	18,573	8%	17,186	17,186	0%	19,265	19,265	0%
Revenue	567	638	12%	595	613	3%	727	745	2%
Gross profit	240	278	16%	247	259	5%	306	318	4%
Operating EBIT	207	241	17%	212	224	5%	264	275	4%
EAT	154	139	-9%	125	142	14%	211	189	-10%
Adjusted EPS (VND)	2,098	1,904	-9%	1,704	1,936	14%	2,888	2,587	-10%

Source: VNDIRECT

## Valuation



### Income statement

(VNDbn)	12-16A	12-17E	12-18E
Net revenue	401	638	613
Cost of sales	(266)	(359)	(354)
Gen & admin expenses	(13)	(25)	(24)
Selling expenses	(9)	(12)	(12)
<b>Operating profit</b>	<b>112</b>	<b>241</b>	<b>224</b>
Operating EBITDA	112	296	286
<b>Depreciation and amortisation</b>	<b>0</b>	<b>(55)</b>	<b>(62)</b>
<b>Operating EBIT</b>	<b>112</b>	<b>241</b>	<b>224</b>
Interest income	5	0	0
Financial expense	(57)	(54)	(57)
Net other income	(31)	(23)	0
Income from associates & JVs	0	0	0
<b>Pre-tax profit</b>	<b>28</b>	<b>164</b>	<b>167</b>
Taxation	(6)	(25)	(25)
Minority interests	0	0	0
<b>Net profit</b>	<b>22</b>	<b>139</b>	<b>142</b>
Adj. net profit to ordinary	22	139	142
Ordinary dividends	0	(73)	(110)
<b>Retained earnings</b>	<b>22</b>	<b>66</b>	<b>32</b>

### Balance sheet

(VNDbn)	12-16A	12-17E	12-18E
Cash and equivalents	34	62	97
Short term investments	0	0	0
Accounts receivables	13	24	23
Inventories	26	35	34
Other current assets	11	11	11
<b>Total current assets</b>	<b>84</b>	<b>132</b>	<b>165</b>
Fixed assets	1,321	1,286	1,234
Total investments	0	0	0
Other long-term assets	14	14	14
<b>Total assets</b>	<b>1,418</b>	<b>1,432</b>	<b>1,413</b>
Short-term debt	206	198	197
Accounts payable	3	4	4
Other current liabilities	47	53	52
<b>Total current liabilities</b>	<b>256</b>	<b>254</b>	<b>253</b>
Total long-term debt	419	369	319
Other liabilities	0	0	0
Share capital	732	732	732
Retained earnings reserve	(27)	39	71
<b>Shareholders' equity</b>	<b>743</b>	<b>809</b>	<b>841</b>
Minority interests	0	0	0
<b>Total liabilities &amp; equity</b>	<b>1,418</b>	<b>1,432</b>	<b>1,413</b>

### Cash flow statement

(VNDbn)	12-16A	12-17E	12-18E
<b>Pretax profit</b>	<b>28</b>	<b>164</b>	<b>167</b>
Depreciation & amortisation	51	54	62
Tax paid	(8)	(25)	(25)
Other adjustments	31	0	0
<b>Change in working capital</b>	<b>5</b>	<b>(13)</b>	<b>1</b>
<b>Cash flow from operations</b>	<b>107</b>	<b>180</b>	<b>205</b>
Capex	(19)	(20)	(10)
Proceeds from assets sales	21	0	0
Others	0	0	0
Other non-current assets changes	0	0	0
<b>Cash flow from investing activities</b>	<b>2</b>	<b>(20)</b>	<b>(10)</b>
New share issuance	0	0	0
Shares buyback	0	0	0
Net borrowings	(89)	(58)	(51)
Other financing cash flow	0	0	0
Dividends paid	0	(73)	(110)
<b>Cash flow from financing activities</b>	<b>(89)</b>	<b>(131)</b>	<b>(160)</b>
Cash and equivalents at beginning of period	13	34	62
<b>Total cash generated</b>	<b>21</b>	<b>29</b>	<b>34</b>
Cash and equivalents at the end of period	34	62	97

### Key ratios

	12-16A	12-17E	12-18E
<b>Dupont</b>			
Net profit margin	5.4%	21.9%	23.1%
Asset turnover	0.27	0.45	0.43
ROAA	1.4%	9.8%	10.0%
Avg assets/avg equity	1.98	1.84	1.72
ROAE	2.9%	18.0%	17.2%
<b>Efficiency</b>			
Days account receivable	5.62	5.61	5.61
Days inventory	35.3	35.2	35.2
Days creditor	3.85	3.84	3.84
Fixed asset turnover	0.28	0.49	0.49
ROIC	1.6%	10.1%	10.4%
<b>Liquidity</b>			
Current ratio	0.33	0.52	0.65
Quick ratio	0.23	0.38	0.52
Cash ratio	0.13	0.25	0.38
Cash cycle	37.1	37.0	37.0
<b>Growth rate (yoy)</b>			
Revenue growth	(2.9%)	59.1%	(3.8%)
Operating profit growth	64.2%	115.4%	(7.3%)
Net profit growth		544.2%	1.7%
EPS growth		544.2%	1.7%
<b>Share value</b>			
Basic EPS (VND)	296	1,904	1,936
BVPS (VND)	10,147	11,051	11,487

Source: VNDIRECT

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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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