

Vietnam

ADD (no change)

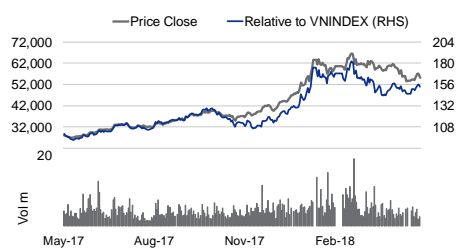
Consensus ratings*: Buy 9 Hold 1 Sell 0

Current price: VND55,200
 Target price: VND77,300
 Previous target: VND79,900
 Up/downside: 40.0%
 CGS-CIMB / Consensus: 1.5%

Reuters: HPG.HM
 Bloomberg: HPG VN
 Market cap: US\$3,677m
 VND83,731,368m
 Average daily turnover: US\$12.47m
 VND283,968m
 Current shares o/s: 1,517m
 Free float: 67.6%
 *Source: Bloomberg

Key changes in this note

➤ No changes.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	-9.2	-5.3	96.5
Relative (%)	4.9	-7.8	54.5

Major shareholders	% held
Tran Dinh Long	25.2
Vu Thi Hien	7.3
VOF Investment Limited	4.7

Analyst(s)



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Hoa Phat Group

Solid growth in 1Q18

- HPG's 1Q18 net profit rose 14.3% yoy, driven by higher sales volume and the continued growth momentum of steel prices.
- Gross margin declined to 22.8% in 1Q18, in line with our expectations.
- The company's galvanised steel plant has been operating since Apr 2018 and will be one of the key earnings growth drivers from 2H18F onwards, in our view.
- The first production line of Dung Quat Steel Complex project is expected to come on stream in 3Q18 with capacity of 600,000 tonnes per year.
- We lower our target price to VND77,300 per share (from VND80,000) due to a higher risk-free rate and recent market re-rating, but we reiterate our Add recommendation.

1Q18 growth was driven by higher volume and steel prices

HPG's construction steel volume grew by 7.2% yoy, while its steel pipe volume rose by 16.8% yoy. The company's revenue reached VND13,001bn, up 26.7% yoy and in line with our expectations. 1Q18 net profit rose 14.3% yoy, driven by higher sales volume and a 8.2% yoy rise in construction steel prices. 1Q18 earnings reached 23.5% of our full-year forecast (vs. 1Q17's earnings which accounted for 24.2% of FY17's net profit).

Construction volume growth was lower than our expectations

We continue to expect robust construction steel volume growth of 16.5% for FY18F, based on an acceleration in construction activity in the second half of the year. The volume growth momentum faltered due to the sluggish revival of public investment in 1Q. Although the authorities seem to be very aggressive in their intent to meet public investment disbursement targets for 2018, there could be some delays as the revised Public Investment Law 2015 has not been approved by the Vietnam National Assembly.

We expect stronger volume growth from 2H18F onwards

We project stronger volume growth from 2H18F onwards, driven by the initiation of: 1) the 400,000 tpa galvanised steel plant in Apr 2018; and 2) the first production line of Dung Quat Steel Complex project with a capacity of 600,000 tpa of construction steel in July 2017. The competition in Vietnam's steel industry has intensified due to slower demand growth. However, we believe that HPG's cost advantages and its strong position in the industry could help it capitalise on this anticipated acceleration in 2H18F.

Gross margins are still in line with full-year estimates

The company's gross margin fell to 22.8% in 1Q18, down 2.2 % pts qoq and 1.2 % pts yoy, on account of the absence of raw material savings vs. last year. In 1Q18, the steel price increased by 21.9% yoy; meanwhile, coking coal prices rose 19.8% yoy while iron ore plunged 16.4% yoy. Given that domestic construction steel demand has lost some growth momentum and raw materials prices have declined, we expect steel prices to move down towards the end of this year. We project full year gross margins of 22.0% for FY18F.

Changes to our valuation and target price, we maintain an Add call

Due to the recent uptick in Vietnam G-bond yields, we lower our target price by 3.4% to VND77,300 based on an increase in our risk-free rate from 4.1% to 5.0%. We believe the sound 1Q18 earnings performance bodes well for HPG meeting our earnings projections for FY18F. The recent share price correction offers an attractive entry point, as we believe that this was mainly due to the recent sharp correction in Vietnam's stock market rather than any change in HPG's fundamentals. We maintain our Add recommendation.

Risks to our rating and re-rating catalysts

Some of the investment risks for HPG include: 1) a steep fall in steel prices; 2) sharp increases in raw material prices, leading to further gross margin contraction; 3) slower-than-expected demand volume growth which could also further pressure prices. Re-rating catalysts include low volume growth and sharp decline in steel prices.

Financial Summary	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
Revenue (VNDb)	33,283	46,162	60,064	78,313	88,810
Operating EBITDA (VNDb)	9,219	11,492	15,426	24,271	29,707
Net Profit (VNDb)	6,602	8,007	9,416	14,191	18,765
Core EPS (VND)	3,804	4,895	5,896	8,886	11,751
Core EPS Growth	89.4%	28.7%	20.5%	50.7%	32.2%
FD Core P/E (x)	14.51	11.28	9.36	6.21	4.70
DPS (VND)	0	0	0	1,000	2,000
Dividend Yield	0.00%	0.00%	0.00%	1.81%	3.62%
EV/EBITDA (x)	9.22	7.19	5.75	3.97	2.78
P/FCFE (x)	27.3	NA	118.0	NA	6.9
Net Gearing	6.1%	(3.8%)	11.9%	23.6%	(2.0%)
P/BV (x)	4.24	2.59	2.03	1.57	1.23
ROE	33.8%	28.5%	24.3%	28.6%	29.4%
% Change In Core EPS Estimates			0.001%	(0.044%)	(0.220%)
CIMB/consensus EPS (x)			1.03	1.16	1.02

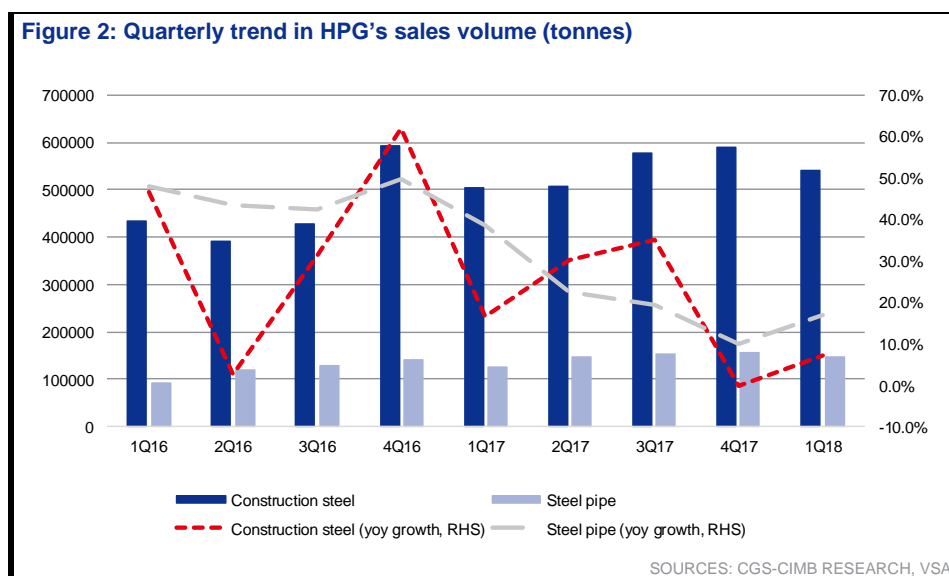
SOURCES: CGS-CIMB RESEARCH, HPG

Solid growth driven by increased volume and rising steel prices

Figure 1: Result comparison

FYE (VND bn)	1QFY18	1QFY17	yoy %		4QFY17		Prev. Comments
			chg	chg	chg	chg	
Revenue	13,001	10,265	26.7	12,745	2.0	60,064	Higher due to higher sales volume and steel prices
Operating costs	(9,738)	(7,541)	29.1	(9,345)	4.2	(44,638)	Higher due to higher iron ore and coking coal prices
EBITDA	3,263	2,724	19.8	3,400	(4.0)	15,426	
EBITDA margin (%)	25.1%	26.5%		26.7%		25.7%	Lower due to rising material costs
Dep. & amort.	(556)	(472)	17.8	(562)	(1.0)	(3,863)	
EBIT	2,707	2,252	20.2	2,839	(4.6)	11,563	
Financial expense	(172)	(112)	53.7	(146)	17.3	(744)	Higher due to higher debt
Financial & invt. Inc	63	74	(14.2)	46	38.1	142	
Other income	10	30	(67.4)	12	(16.7)	36	
Pretax profit	2,608	2,244	16.3	2,750	(5.1)	10,997	
Tax	(386)	(308)	25.4	(349)	10.5	(1,560)	
Tax rate (%)	14.8	13.7		12.7			
Minority interests	12	1	965	5	136	21	
Net profit	2,211	1,935	14.3	2,396	(7.7)	9,416	
EPS (VND)	1,385	1,179	17.4	1,483	(6.7)	5,896	

SOURCES: CGS-CIMB RESEARCH, HPG

Figure 2: Quarterly trend in HPG's sales volume (tonnes)


SOURCES: CGS-CIMB RESEARCH, VSA

Changes to our valuation and target price

Given that our market strategist believes that Vietnam's government bond yields might have bottomed out, we raised our risk-free rate assumption from 4.1% to 5.0%. Therefore, our cost of equity increases from 14.5% to 15.4% for FY18-22F and 17.0% for FY22F onwards. Our target price is calculated using an equal weighting of the DCF valuation and a target P/E multiple of 10.2x. We decreased our discounted cash flow-based target price to VND79,350 per share, down from VND84,314 per share, due to a 900 bps increase in the weighted average cost of capital. We maintain our target P/E multiple at 10.2x as our peer comparison does not include any suitable domestic company that is considered a close comparable with HPG and regional peer valuations have not changed materially since our initiation report on HPG. Due to the changes to our DCF valuation, our price target is lowered to VND77,300 per share, from VND80,000 per share.

Figure 3: HPG's cost of equity assumptions

	Old (%)	New (%)
Risk free rate	4.1	5.0
Market risk premium	10.1	10.1
Stock beta	1.03	1.03
Cost of equity, Ke	14.5	15.4
WACC	11.2	11.7

SOURCES: CGS-CIMB RESEARCH

Figure 4: Regional sector comparison

Company	Bloomberg Ticker	Recom.	Closing price	Target price	Market cap (US\$ m)	ROE (%)		P/BV (x)		P/E (x)	
			(local curr.)	(local curr.)		CY18F	CY19F	CY18F	CY19F	CY18F	CY19F
JSW Steel	JSTL IN	Reduce	319.6	222.0	11,474	14.0	14.3	2.9	2.5	16.9	13.4
Tata Steel	TATA IN	Reduce	594.2	460.0	9,952	14.0	10.8	1.4	1.2	9.3	8.0
NMDC	NMDC IN	Add	116.3	162.0	5,704	16.0	16.0	1.6	1.5	9.7	9.2
Shanxi Taigang Stainless-A	000825 CH	Not rated	6.0	na	5,373	14.7	15.7	1.1	1.0	7.6	6.4
Maanshan Iron & Steel-A	600808 CH	Add	3.8	4.7	4,418	15.3	16.8	1.1	1.0	7.0	6.8
Hunan Valin Steel Co Ltd -A	000932 CH	Add	8.2	13.7	3,911	26.4	31.8	1.7	1.3	5.4	5.1
Sansteel Minguang Co Ltd -A	002110 CH	Not rated	18.3	na	3,828	26.3	30.1	1.8	1.4	5.7	5.2
Nanjing Iron & Steel Co-A	600282 CH	Not rated	4.5	na	3,271	20.0	23.7	1.4	1.2	5.8	5.5
Xinyu Iron & Steel Co Ltd-A	600782 CH	Not rated	5.8	na	2,988	18.9	21.6	1.2	1.0	5.6	5.3
Xinxing Ductile Iron Pipes-A	000778 CH	Not rated	4.7	na	2,923	6.9	6.5	0.9	0.9	13.7	12.3
Sgis Songshan Co Ltd-A	000717 CH	Not rated	7.0	na	2,655	39.0	55.2	2.8	1.8	5.7	5.5
<i>Average regional peers</i>						19.2	22.0	1.6	1.3	8.4	7.5
<i>Median regional peers</i>						16.0	16.8	1.4	1.2	7.0	6.4
Hoa Phat Group JSC	HPG VN	Add	55,200	77,300	3,600	24.3	28.6	2.0	1.6	9.4	6.2

NOTE: AS OF 10 APR 2018

SOURCES: CGS-CIMB RESEARCH, BLOOMBERG

Industry conditions became less favourable for HPG

Construction steel lost some growth momentum ►

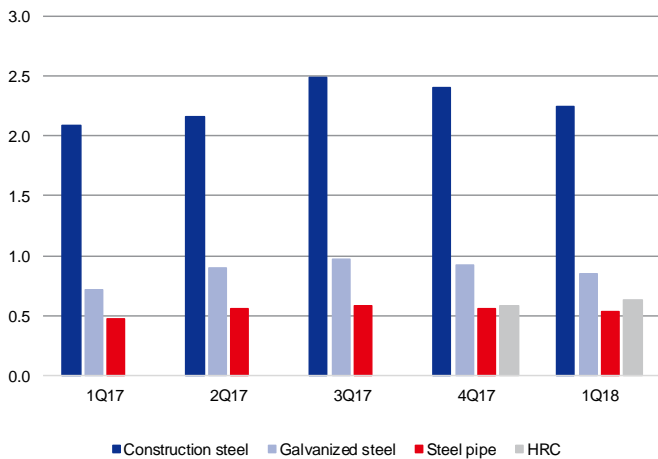
In 1Q18, the total sales volume of Vietnam's steel industry reached 5.7m tonnes (+29.0% yoy) according to the official data released by Vietnam Steel Association (VSA). Finished steel consumption, excluding HRC sales volume, grew 11.0% yoy, driven by the strong growth of flat steel products (galvanised steel and steel pipes). The industry's construction steel volume growth was much lower than the industry's growth, rising by 7.6% yoy due to the continued stagnant growth of public investment disbursement. Meanwhile, the sales volume of steel pipes and galvanised steel products remained strong with growth of 13.2% yoy and 19.5% yoy, respectively in 1Q18.

There was a radical change in the domestic steel market as the import volume fell sharply in 1Q18 (-25.4% yoy in terms of volume and -6.9% yoy in terms of value). In our view, the ramp-up of Formosa's plant in 2Q17 and the anti-dumping duties on imported steel products resulted in the declining competitiveness of imported product.

Domestic steel prices are likely to head lower ►

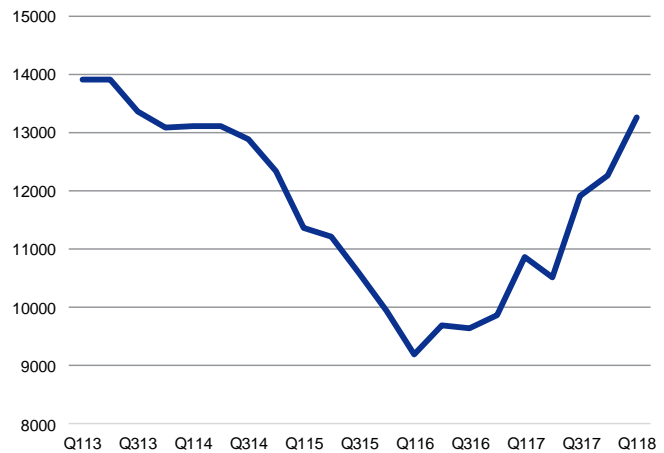
According to the VSA, following an 18.6% yoy rise in the steel price in 2017, the domestic steel price continued to maintain its growth momentum in 1Q18 with an increase of 8.2% qoq. However, there has been a slight decline since the beginning of 2Q18 following the global steel prices' trend. Compared with the end of 2017, domestic steel price still rose by around 6.0% YTD. We project HPG's ASP will continue to rise in FY18F but at a slower pace than the previous year. Given that domestic construction steel demand has lost some growth momentum and raw materials prices have declined, we expect steel prices to move down towards the end of this year. Our ASP's growth assumption remains unchanged at 7.0% yoy.

Figure 5: Sales volume by product (m tonnes, 1Q17-1Q18)



SOURCES: CGS-CIMB RESEARCH, VSA
No available data for HRC's sales volume in 1Q17-3Q17 period

Figure 6: Trend of steel price (rebar, VND per kg, 1Q13-1Q18)



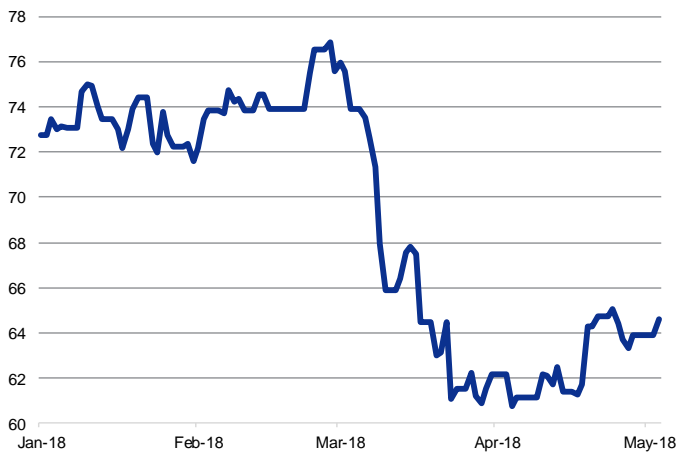
SOURCES: CGS-CIMB RESEARCH, VSA

Weaker raw material prices due to steel demand concerns ➤

Global steel demand concerns have weighed on both iron ore and coking coal prices since the end of Mar 18. The spot price for benchmark 62% iron ore fines had tumbled 11.2% to \$64.6 a tonne as at 03 May 18, compared with the end of 2017. Following an increase of 14.8% qoq in 1Q18, the spot price of JM25 coking coal decreased to US\$178.2 a tonne as of 03 May 18, a 6.8% decrease compared with the end of 2017.

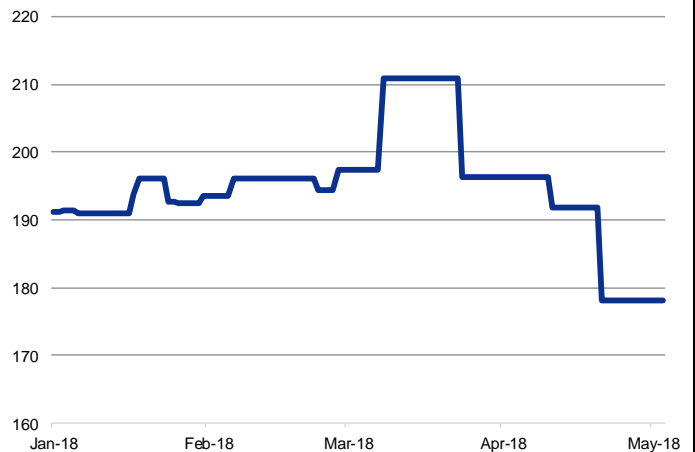
In our view, the continued softness in raw material input prices should support HPG's margins in 2018.

Figure 7: Iron ore price (US\$/tonne, Jan-18 to May-18)



SOURCES: CGS-CIMB RESEARCH, BLOOMBERG

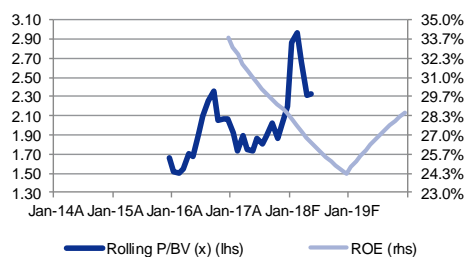
Figure 8: Coking coal price (US\$/tonne, Jan-18 to May-18)



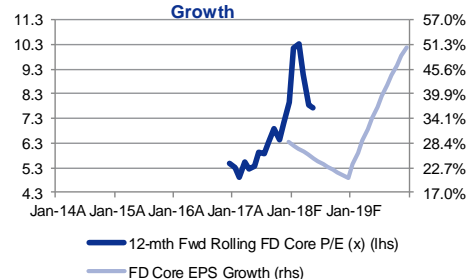
SOURCES: CGS-CIMB RESEARCH, BLOOMBERG

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Core P/E vs FD Core EPS Growth



Profit & Loss

(VNDb)	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
Total Net Revenues	33,283	46,162	60,064	78,313	88,810
Gross Profit	8,751	10,674	13,184	19,403	24,786
Operating EBITDA	9,219	11,492	15,426	24,271	29,707
Depreciation And Amortisation	(1,363)	(1,870)	(3,863)	(6,958)	(7,297)
Operating EBIT	7,856	9,622	11,563	17,313	22,410
Financial Income/(Expense)	(171)	(370)	(602)	(793)	(553)
Pretax Income/(Loss) from Assoc.	0	0	0	0	0
Non-Operating Income/(Expense)	17	36	36	36	36
Profit Before Tax (pre-EI)	7,702	9,288	10,997	16,556	21,893
Exceptional Items					
Pre-tax Profit	7,702	9,288	10,997	16,556	21,893
Taxation	(1,096)	(1,274)	(1,560)	(2,349)	(3,106)
Exceptional Income - post-tax					
Profit After Tax	6,606	8,015	9,437	14,207	18,787
Minority Interests	(4)	(8)	(21)	(17)	(22)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	6,602	8,007	9,416	14,191	18,765
Recurring Net Profit	5,771	7,426	8,945	13,481	17,827
Fully Diluted Recurring Net Profit	5,771	7,426	8,945	13,481	17,827

Cash Flow

(VNDb)	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
EBITDA	9,219	11,492	15,426	24,271	29,707
Cash Flow from Inv. & Assoc.					
Change In Working Capital	(1,572)	(5,546)	1,091	(5,972)	(2,407)
(Incr)/Decr in Total Provisions	(126)	(5)	0	0	0
Other Non-Cash (Income)/Expense	181	24	0	0	0
Other Operating Cashflow	368	1,701	0	0	0
Net Interest (Paid)/Received	(154)	(333)	(566)	(757)	(517)
Tax Paid	(1,096)	(1,274)	(1,560)	(2,349)	(3,106)
Cashflow From Operations	6,819	6,058	14,391	15,193	23,677
Capex	(5,832)	(2,361)	(15,766)	(29,762)	(3,315)
Disposals Of FAs/subsidiaries	8	9	0	0	0
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	2,696	(15,574)	2,000	7,000	0
Cash Flow From Investing	(3,128)	(17,926)	(13,765)	(22,762)	(3,314)
Debt Raised/(repaid)	(629)	5,840	84	1,167	(8,250)
Proceeds From Issue Of Shares	1,099	6,742	0	0	0
Shares Repurchased	(0)	(1)			
Dividends Paid	0	0	0	(1,517)	(3,034)
Preferred Dividends					
Other Financing Cashflow	(2,208)	(1,687)	(168)	(470)	(458)
Cash Flow From Financing	(1,738)	10,894	(84)	(820)	(11,741)
Total Cash Generated	1,953	(973)	542	(8,389)	8,621
Free Cashflow To Equity	3,062	(6,027)	710	(6,401)	12,113
Free Cashflow To Firm	3,845	(11,534)	1,192	(6,811)	20,880

SOURCES: VND, COMPANY REPORTS

BY THE NUMBERS... cont'd

Balance Sheet

(VNDb)	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
Total Cash And Equivalents	5,252	14,201	13,111	8,481	15,439
Total Debtors	2,395	6,555	3,604	7,440	8,881
Inventories	10,247	11,769	15,470	19,440	21,128
Total Other Current Assets	289	552	663	994	1,193
Total Current Assets	18,183	33,077	32,848	36,355	46,641
Fixed Assets	13,846	18,652	34,942	49,047	47,913
Total Investments	79	17	17	17	16
Intangible Assets	257	240	234	229	224
Total Other Non-Current Assets	862	1,035	1,087	1,141	1,198
Total Non-current Assets	15,044	19,945	36,280	50,434	49,352
Short-term Debt	5,488	11,329	11,412	14,096	8,881
Current Portion of Long-Term Debt					
Total Creditors	6,097	6,487	8,438	10,604	11,524
Other Current Liabilities					
Total Current Liabilities	11,585	17,815	19,851	24,700	20,405
Total Long-term Debt	972	1,651	6,605	6,982	5,230
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	819	1,158	1,327	1,798	2,256
Total Non-current Liabilities	1,791	2,809	7,933	8,780	7,485
Total Provisions	0	0	0	0	0
Total Liabilities	13,376	20,624	27,783	33,480	27,891
Shareholders' Equity	19,745	32,287	41,234	53,198	67,991
Minority Interests	106	111	111	111	111
Total Equity	19,850	32,398	41,345	53,309	68,102

Key Ratios

	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
Revenue Growth	21.2%	38.7%	30.1%	30.4%	13.4%
Operating EBITDA Growth	66.4%	24.7%	34.2%	57.3%	22.4%
Operating EBITDA Margin	27.7%	24.9%	25.7%	31.0%	33.4%
Net Cash Per Share (VND)	(796)	805	(3,234)	(8,304)	876
BVPS (VND)	13,015	21,282	27,180	35,066	44,817
Gross Interest Cover	28.06	20.06	15.55	17.56	25.27
Effective Tax Rate	14.2%	13.7%	14.2%	14.2%	14.2%
Net Dividend Payout Ratio	NA	NA	NA	10.7%	16.2%
Accounts Receivables Days	22.01	35.38	30.87	25.74	33.63
Inventory Days	128.2	113.2	106.0	108.2	116.0
Accounts Payables Days	71.79	64.71	58.10	58.99	63.25
ROIC (%)	41.9%	44.1%	35.8%	36.4%	33.1%
ROCE (%)	33.6%	27.1%	22.4%	26.2%	29.0%
Return On Average Assets	23.1%	19.4%	16.4%	19.2%	21.2%

Key Drivers

	Dec-16A	Dec-17A	Dec-18F	Dec-19F	Dec-20F
ASP (% Change)	-10.9%	9.7%	7.0%	5.0%	0.0%
Unit Sales Growth (%)	51.1%	21.1%	22.8%	31.6%	13.2%
Utilisation Rate (%)	91.0%	106.4%	95.9%	60.9%	84.8%

SOURCES: VND, COMPANY REPORTS

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