

## MARKET STRATEGY – AT THE FOREFRONT OF PUBLIC INVESTMENT HUSTLE

15 April 2020

- We believe public investment will accelerate earlier than expected in order to boost economic growth amid the slowdown of other growth engines.
- The North-South expressway projects will return to center stage in 2H20F.
- We believe the suppliers of construction materials, especially stone and asphalt, will directly benefit from the surging demand from these projects.
- Our top picks in this theme include: KSB, PLC and HPG.

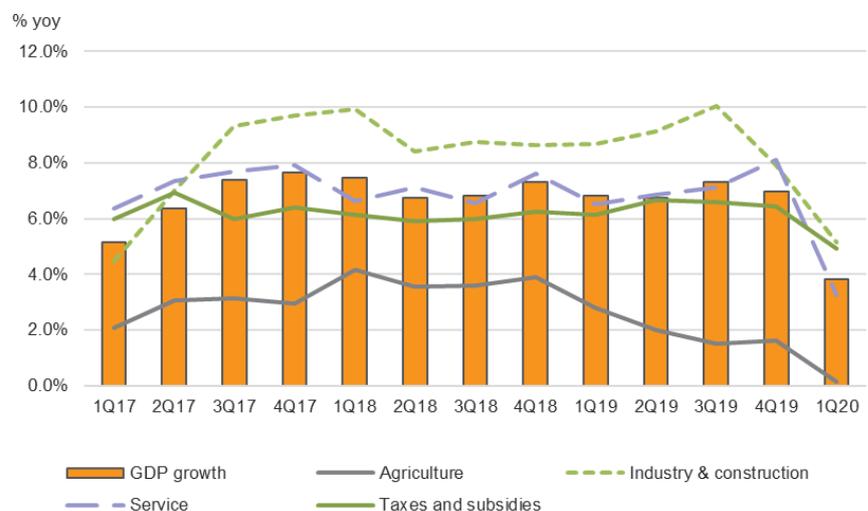
### Public investment will accelerate earlier than expected

#### All economic growth engines slowed in 1Q20

In our previous forecasts as at end-2019, we expected the visibility for new public investment would remain somewhat uncertain as the attention of key decision makers and government apparatus may be preoccupied by the 2021 leadership transition. Thus, the disbursement of public investment would be unlikely to accelerate until late-2020, in our view. However, the coronavirus outbreak (COVID-19) since Jan 2020 has changed the whole macroeconomic picture and casted a shadow over the economic growth outlook.

According to the General Statistics Office (GSO), Vietnam's economy witnessed the lowest 1Q growth in 11 years with only 3.82% yoy; sector growths plummeted across the board as a result of Covid-19 pandemic fallout.

Figure 1: 1Q20 real GDP growth at 10-year low, all sectors faced slower expansion



Source: GSO



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We expect Vietnam's GDP to grow 5.0% yoy in 2020F (vs. 7.1% in 2019), on the back of the industry and construction sector rising 5.6% yoy, the services sector expanding 5.3% yoy, and the agriculture sector edging up 2.0% yoy. We see all economic growth engines are teetering. Export faces higher pressure amid the subdued global demand due to the pandemic. Meanwhile, foreign direct investment (FDI) experienced a sharp decline in 1Q20 with only US\$8.6bn worth of registered FDI recorded (-20.9% yoy). Thus, we see public investment will be vital to drive the growth in 2020F.

### Fiscal policy still has room to expand for further improvement in public investment

The big gap between the data from the General Statistics Office (GSO) and the Ministry of Finance (MOF) in terms of actual expenditure on development investment in the past three years is worth noting. In 2019, GSO's preliminary data showed that public investment expenditure decreased by about 5.2% yoy and stood at only 57.5% of the annual plan. However, according to MOF, the estimated outturn of capital development expenditure was VND443.4tr, which is 3.3% higher than the annual plan; this number included the undisbursed amounts carried forward to 2020F. This signalled that the disbursement progress in public investment has still been sluggish and the actual budget deficit should be lower than the reported data.

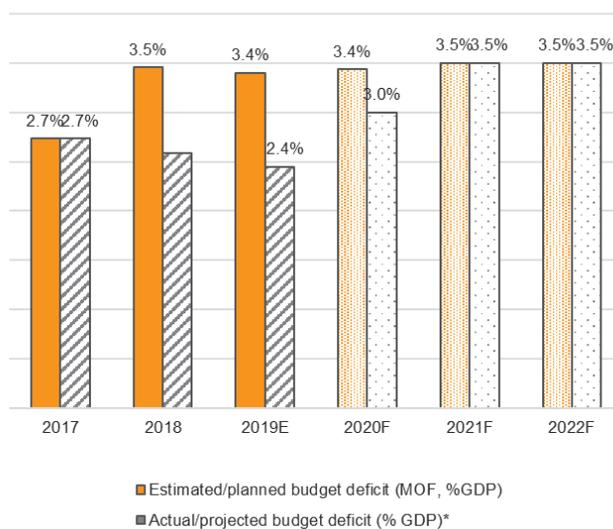
**Figure 2: Vietnam's State Budget Data (2017-2019E)**

Source	2017				2018			2019			
	MOF	GSO	MOF	MOF	MOF	GSO	MOF	MOF	GSO	MOF	
Type of data	Planned	Estimated	Estimated	Final accounts	Planned	Estimated	Estimated	Planned	Estimated	Estimated*	
Domestic revenue	990.3	871.1	1,032.2	1,039.2	1,099.3	1,012.3	1,148.7	1,173.5	1,146.2	1,195.5	
Oil revenue	38.3	43.5	49.6	49.6	35.9	59.4	66.0	44.6	53.3	46.8	
Trade revenue from im-ex activities	180.0	183.8	197.9	197.3	179.0	195.9	202.5	189.2	210.2	189.2	
<b>Total State Budget Revenue</b>	<b>1,212.2</b>	<b>1,104.0</b>	<b>1,287.6</b>	<b>1,293.6</b>	<b>1,319.2</b>	<b>1,272.5</b>	<b>1,424.9</b>	<b>1,411.3</b>	<b>1,414.3</b>	<b>1,457.3</b>	
Recurrent expenditure	896.3	862.6	906.0	881.7	940.7	874.5	954.1	1,042.8	927.9	999.5	
Capital development expenditure	357.2	259.5	365.5	372.8	399.7	260.2	411.3	429.3	246.7	443.4	
Interest	100.2	91.0	98.9	97.7	113.8	102.2	109.7	124.9	99.3	124.9	
<b>Total State Budget Expenditure</b>	<b>1,389.5</b>	<b>1,219.5</b>	<b>1,461.9</b>	<b>1,355.0</b>	<b>1,523.2</b>	<b>1,272.1</b>	<b>1,616.4</b>	<b>1,633.3</b>	<b>1,316.4</b>	<b>1,666.8</b>	
State Budget Surplus/Deficit	(177.4)	(115.5)	(174.3)	(61.4)	(204.0)	0.4	(191.5)	(222.0)	97.9	(209.5)	

Sources: VNDIRECT RESEARCH, GSO, MOF; \*: full-year estimation

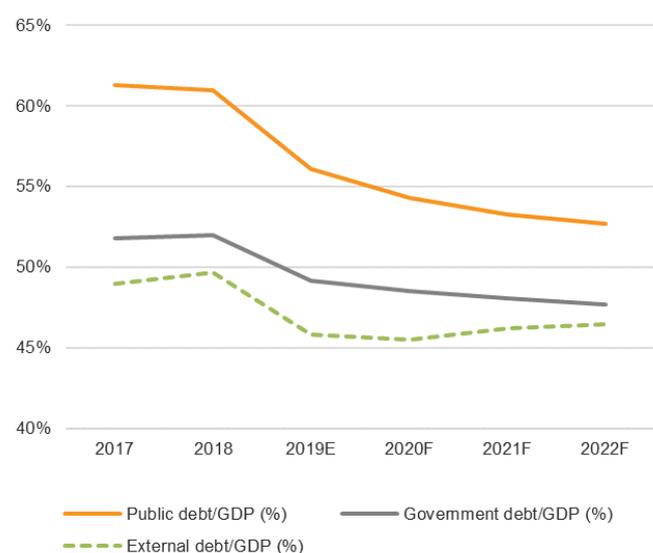
Additionally, the MOF reported that actual fiscal deficit declined from 3.5% of GDP to 2.7% of GDP in 2017, based on the slow disbursement of public investment; we project fiscal deficit at ~2.5% of GDP in 2018-19, which is lower than the preliminary estimate by the MOF. The lower fiscal deficit and robust economic growth have helped to reduce Vietnam's public debt from 61.3% of GDP in 2017 to an estimated 56.1% of GDP in 2019. According to the 2020-22F budget proposal, public debt will be reduced further to 52.7% of GDP in 2022F.

**Figure 3: Budget deficit (2017-2022F)**



Sources: VNDIRECT RESEARCH, MOF, \* Final account from MOF and our estimations

**Figure 4: Public debt to GDP ratio has dropped in 2019E**



Sources: VNDIRECT RESEARCH, MOF

According to the 2020F Budget plan approved by the National Assembly in Nov 2019, expenditure for development investment is estimated at VND470.6bn (+6.1% yoy, ~6.9% of GDP). The government will boost its public investment expenditure by 8.2% in 2021-22F on top of the targeted 6.1% increase in 2020F. Net fiscal deficit will be allowed to widen to 3.5% of GDP in 2021-22F, expanding slightly from a projected 3.4% in 2020F. We expect that in the case the government manages to fully achieve 2020F guidance, it would contribute 0.42% pts to GDP growth this year.

The increase in public investment spending will focus on improving infrastructure conditions, particularly through a pipeline of mega projects.

**Figure 5: Major infrastructure projects in 2020-2026F**

Project	Total investment (VND bn)	Start	Completion
Metro 1 (Ben Thanh - Suoi Tien)	43,757	2012	4Q21
Metro 2 (Ben Thanh - Tham Luong)	47,800	2021	2026
HCM - Thu Dau Mot - Chon Thanh Highway	24,150		2021-25
HCM - Moc Bai Highway	10,668	2021	2026
Parallel Road for 50 Route	3,816		2021-25
Belt Road 2	6,500		2021-25
Belt Road 3	19,871		2022-25
Soai Rap Dredging Project (Phase 3)	8,977		2021-25
The water environment improvement Project (Phase 2)	11,282	2015	2021
Long Thanh International Airport	114,451	2021	2025
11 sub-projects of the eastern section of the North-South expressway	101,218	2020	2021-25

Sources: MINISTRY OF TRANSPORT

### Strong messages delivered by the government in recent days

The government is aggressively acting to accelerate the implementation of public investment. A decree on guiding the implementation of the amended Law on Public Investment has recently been issued on 6 Apr, which provides regulations on capital management, settlement and specific direction for individuals and organisations to prevent delays to public investment disbursement.

The Ministry of Transport requested the localities where 11 sub-projects of the North-South Expressway are implemented to focus on speeding up and handing over the ground in 2Q20F. Currently site clearance has been completed on 454km of the total 646km, or 70.3%. Meanwhile, Dong Nai province has now cleared 99% of the resettlement areas for Long Thanh airport project. The Prime Minister has instructed the province to disburse VND17,000bn of public investment this year to get the project started in 2021.

Disbursed state capital rose 16.4% yoy to VND59.5tr in 1Q20, equivalent to 13.2% of the full-year target (higher than the 11.2% rate seen in 1Q19). This is signaling that public investment will get back to center stage earlier than our expectation.

### PPP projects of the North-South Expressway will take the spotlight

On 7 Apr, the Prime Minister approved to change the financing format of eight sub-projects under the Eastern North-South Expressway project to public investment from public-private partnership (PPP), and assigned relevant ministries to quickly complete the adjustment procedures for submitting to the National Assembly. Therefore, all 11 sub-projects of the North-South expressway, which require a total investment of VND101.2tr, are now public investment projects.

Similarly, the My Thuan - Can Tho expressway will be converted to public investment project and will apply the same mechanism as the North-South expressway project.

With the financing format conversion, the government wants to get these projects started right in 3Q20F, instead of 1Q21F as we previously expected.

**Figure 6: 11 sub-projects of the Eastern section of the North-South expressway and My Thuan – Can Tho expressway**

Sub-projects under the PPP format will need to go through the procurement process which would last at least six months. In case of successful bidding, most of the investment will be funded by banks. This stage contains many risks as domestic banks are currently reducing the proportion of short-term capital used for medium- and long-term loans, especially restricting credit additions for infrastructure projects. Therefore, under this scheme, construction could only start in 1Q21F at the earliest.

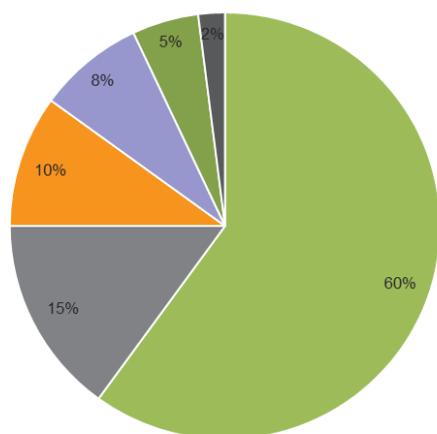
Expressway	Total investment (VNDbn)	Length of the route (km)	Starting time
Cao Bo - Mai Son	1,607	15	4Q19
Cam Lo - La Son	7,690	93	1Q20
My Thuan Bridge 2	5,003	7	1Q20
Mai Son – National Highway 45	12,918	63	3Q20
National Highway 45 – Nghi Son	6,333	43	3Q20
Phan Thiet - Dau Giay	14,359	99	3Q20
Dien Chau - Bai Vot	13,338	50	3Q20
Nha Trang - Cam Lam	5,058	29	3Q20
Cam Lam - Vinh Hao	13,687	91	3Q20
Vinh Hao - Phan Thiet	12,844	106	3Q20
Nghi Son - Dien Chau	8,381	50	3Q20
<b>Total</b>	<b>101,218</b>	<b>646</b>	
My Thuan - Can Tho	4,758	23	3Q20

Source: MINISTRY OF TRANSPORT

We estimate the cost structure of Vietnam’s infrastructure projects, based on 1) the calculation methodology for the construction cost specified in Circular No. 09/2019/TT-BXD (26 Dec 2019) of the Ministry of Construction; and 2) the cost structure of Vietnam’s expressway projects implemented in 2015-18. Details are presented in Figure 7 and Figure 8.

Under our base scenario, about 40% of public investment will be disbursed at My Thuan – Can Tho expressway and 11 North-South expressway projects in 2020F, and construction will require VND8.9tr worth of asphalt, VND7.6tr of steel and VND3.8tr of cement. Besides, we see construction stone supply will see the biggest impact as the demand from these projects is equivalent to 30-35% of the licensed mining capacity of listed companies in the construction area. In addition, to complete 100% of these projects, we expect the costs for asphalt, construction steel and cement to reach VND22.3tr, VND19.1tr and VND9.5tr, respectively.

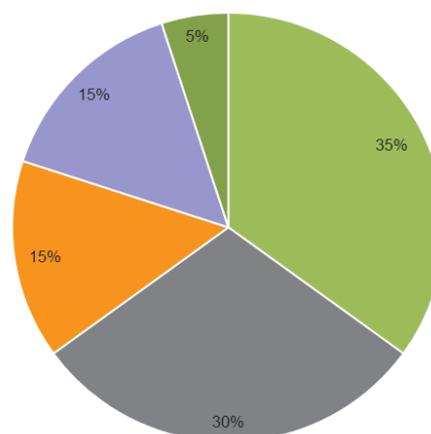
**Figure 7: Cost structure estimates for Vietnam’s expressway projects**



■ Materials ■ Equipment ■ Labor ■ Contingency ■ Compensation ■ Others

Source: VNDIRECT RESEARCH

**Figure 8: Construction material estimates for Vietnam’s expressway projects**



■ Asphalt ■ Construction steel ■ Construction stone ■ Cement ■ Others

Source: VNDIRECT RESEARCH

### We believe construction material sectors are broad plays in this theme

Figure 9: Summary of our assessment to derive the “highly potential” sub-sectors among the construction material industries, which could benefit from North-South Expressway projects

	Construction steel	Cement	Construction stone	Asphalt
How is the situation of supply and demand in the sector in 2019?				
How is the designed capacity expected to increase in 2020F?				
How is the distance of the supplier to the North-South expressway projects to be implemented in 2020F?				
How does the demand for raw materials from the North-South expressway projects compare to the production scale of the whole sector in 2020F?				
<b>Overall attractiveness rating</b>				
Notable stocks	HPG	HT1, BCC	KSB, DHA	PLC

NOTE: ● = “Highly favourable”; ○ = “Unfavourable”

Source: VNDIRECT RESEARCH

#### Construction stone: Highly favourable

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

The Ministry of Construction has asked 13 provinces where the expressways pass through to create favourable conditions for investors and construction contractors to exploit local raw materials, thereby reducing the time of construction and transport costs.

We believe that the quarries of listed companies located near expressway projects will be prioritised for the supply given the advantages and product quality of these large companies.

Figure 10: Quarries of listed construction stone companies

Company	Quarry	District	Province	Licensed mining capacity (m3/year)	Exploitation period
KSB	Tan Dong Hiep (*)	Di An	Binh Duong	2,341,858	Dec-19
	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 Dong Hiep (*)	Di An	Binh Duong	762,738	Dec-19
	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	Nui Nho (*)	Di An	Binh Duong	2,000,000	Dec-19
	Mui Tau	Tan Lap	Binh Phuoc	1,000,000	Jan-42
VLB	Thach Phu 1	Vinh Cuu	Dong Nai	1,800,000	Feb-23
	Thien Tan 2	Vinh Cuu	Dong Nai	1,800,000	N/A
	Solku 2	Thong Nhat	Dong Nai	400,000	N/A
DND	Tan Cang 1	Bien Hoa	Dong Nai	1,500,000	N/A
	Tan Cang 5	Bien Hoa	Dong Nai	1,000,000	Jan-23
	Thien Tan	Vinh Cuu	Dong Nai	354,000	Jan-26
CTI	Tan Cang 8	Bien Hoa	Dong Nai	1,000,000	Dec-35

(\*) Clusters have expired, but can still be exploited in the reconstituted period for 1-2 years

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

Source: VNDIRECT RESEARCH, COMPANY REPORTS

Four quarry clusters (including: Solku, Thien Tan, Thach Phu and Tan Cang) in Dong Nai province are in favourable locations to provide construction stone for Phan Thiet - Dau Giay expressway project - the prioritized one among 11 North-South expressway projects.

In addition, the My Thuan-Can Tho expressway project will also have to source stones from mines in the southeast region, due to the negligible stone reserves in the Mekong Delta region (details in Figure 11). Especially, due to the soft ground of the delta, this expressway project will need more stone than other areas.

**Figure 11: Negligible construction stone reserves in the Mekong Delta region**



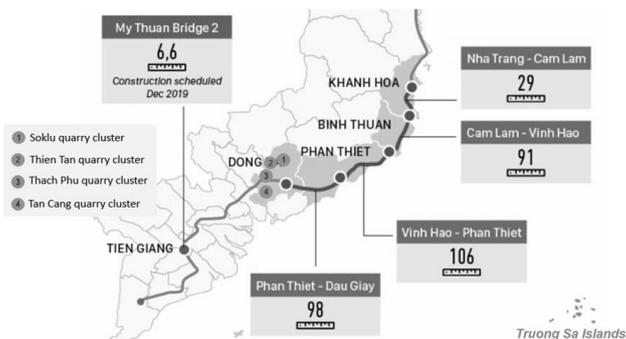
Source: VNDIRECT RESEARCH, DEPARTMENT OF SURVEYING & MAPPING

The two projects will need 6-7m tonnes of construction stone, equivalent to 30-35% of the licensed mining capacity of listed companies, according to our estimates.

KSB's two quarries (Bai Giang and Go Truong) are also conveniently located to supply stone to the expressway projects in the provinces of Nghe An and Thanh Hoa.

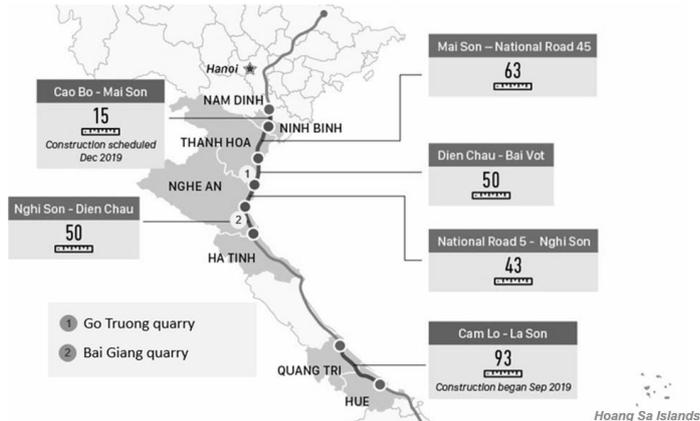
We believe **KSB** and **DHA** are two best players in the construction stone sector, as they own many quarries in convenient locations, with large mining capacity and long mining time horizon. KSB is also aiming to M&A with Bien Hoa Building Materials Production And Construction (UpCom: VLB) (expected in 2Q20F), thereby becoming the Vietnam's largest stone miner, raising its capacity to 8.8m tonnes of construction stone p.a. Meanwhile, DHA is among the companies with the highest profit margins in the industry, who also maintains a positive profit growth in recent years, has no debt and maintains regular dividend payments.

Figure 12: Locations of construction stone quarries and the southern section of the North-South expressway



Source: VNDIRECT RESEARCH, MOT, VNEXPRESS

Figure 13: Locations of construction stone quarries and the northern section of the North-South expressway



Source: VNDIRECT RESEARCH, MOT, VNEXPRESS

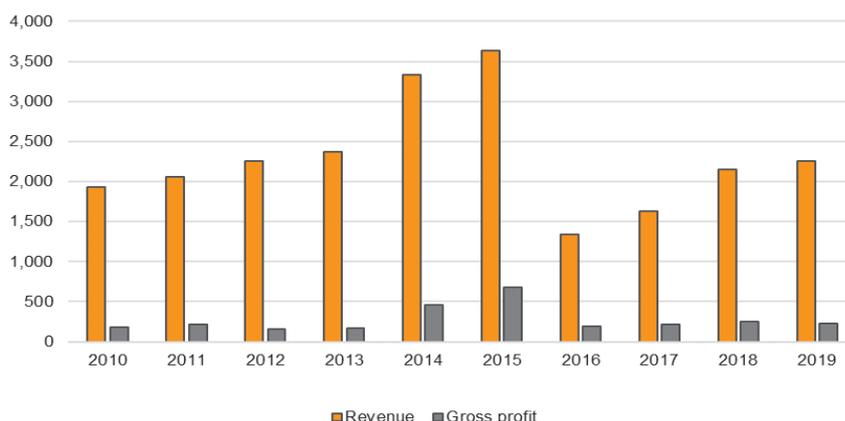
### Asphalt: Highly favourable

We believe that the business results of companies in this industry will greatly benefit from the disbursement of government infrastructure projects. In addition, lower oil prices could translate into higher margins for asphalt companies in 2020F.

Investors should keep an eye on **PLC**, a subsidiary of Petrolimex Group (HOSE: PLX), which is the only listed asphalt company and currently accounting for about 30% of the domestic market share of the material.

PLC's asphalt revenue reached a high level during FY2014-15, when disbursement of public transportation investment grew strongly. Low infrastructure spending in FY2016-19 was attributed to a strained government budget and cooling private investment in BOT projects, resulting in a ~50% decline in PLC's asphalt revenues from those in FY2014-15.

Figure 14: PLC's asphalt revenue and gross profit in FY2010-19 (VNDbn)



Source: VNDIRECT RESEARCH, COMPANY REPORT

### Construction steel: Favourable

Vietnam's construction steel industry is currently facing oversupply, and the whole industry operated at about 80% of its designed capacity at end-2019.

Most of the input materials for the steel industry (iron ore, coking coal, scrap steel) are imported. Therefore, when exporting countries impose lockdowns due to the Covid-19 pandemic, companies in the industry face the risk of unstable supply. However, many other countries can supply these raw

materials, thus Vietnamese companies can redirect their imports. In addition, they always have contingency plans, involving the stockup of raw materials for three to six months to ensure smooth operation.

We estimate the 11 North-South Expressway projects starting construction in 3Q20F will add about 6.2% to current construction steel demand. The additional demand will thus slightly reduce the competitive pressure in the industry, especially when capacity is expected to increase approx. 15% this year, according to our estimates.

We prefer **HPG** in this sector. We believe Dung Quat Steel Complex (DQSC) will be a game changer for HPG and the entire domestic steel market. When the two phases of Dung Quat Steel Complex are completed, HPG will shorten the delivery time to Vietnam’s southern region to three days from seven days, which could help the company achieve its 35-40% market share target in the Southern region (from 13.8% in 2019).

**Cement: Low favourable**

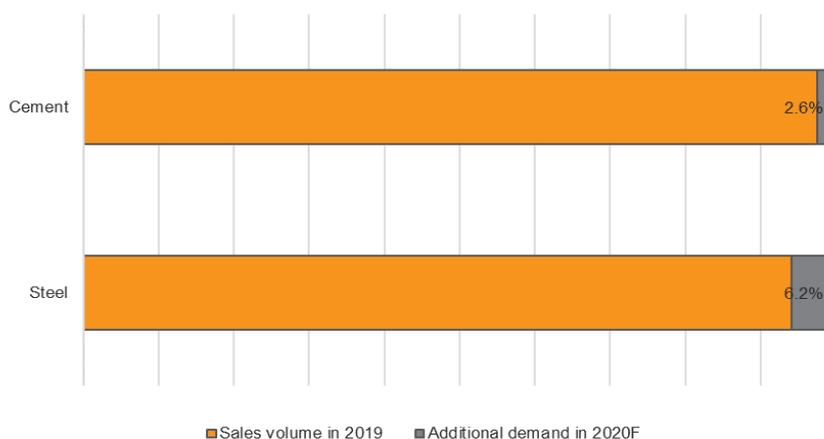
After a period of massive expansion, Vietnam's cement industry started to face oversupply from 2009, resulting in increasing competition in the industry. In 2018, Vietnam officially became the world's No. 1 cement exporter.

According to the Vietnam Cement Association (VNCA), Vietnam’s cement sales volume reached 99m tonnes in 2019, of which nearly 65m tonnes were domestic consumption, while 34m tonnes (equivalent to 34% of total sales volume) were exported.

We estimate the 11 North-South Expressway projects starting construction in 3Q20F will add only ~2.6% to current cement demand. Other projects in the government's 2020F public investment disbursement plan will further support the demand. However, we assess that this positive impact will not be too big a push for the industry, especially when two major export markets, the Philippines and Bangladesh (accounting for a combined 25.9% of Vietnam’s export volume and making up 8.8% of total sales volume in FY19) have started imposing self-defence tariffs from 2H19.

We prefer **HT1** and **BCC** for the consistent improvement of their core business results on the back of healthy sales volume growth, lower interest expenses and FX risks. Specifically, HT1 is the largest cement manufacturer in the Southern region, owning the majority of local limestone mines (which is scarce in the region).

**Figure 15: Estimated additional demand for materials from six expressway projects to be implemented in 2020F**



Source: VNDIRECT RESEARCH, VSA, VNCA

**Figure 16: Financial ratios of mentioned companies (Data as at 14 Apr 2020)**

Company Name	Ticker	Share price (VND)	Market Cap (US\$ m)	FY19 revenue growth (%)	FY19 NPAT growth (%)	Dividend yield (%)	FY19 ROE (%)	FY19 ROA (%)	TTM P/E (x)	Current P/B (x)
Hoa Phat Group JSC	HPG VN	19,950	2,374.3	14.0%	-11.9%	0.0%	17.0%	8.4%	7.3	1.2
Ha Tien 1 Cement JSC	HT1 VN	12,100	199.0	5.5%	15.5%	0.0%	14.1%	7.1%	6.2	0.9
Bim Son Cement JSC	BCC VN	6,400	31.3	4.0%	39.4%	0.0%	6.7%	2.9%	5.4	0.3
Binh Duong Mineral & Construction JSC	KSB VN	14,650	33.8	12.4%	0.9%	0.0%	28.6%	9.6%	2.5	0.6
Hoa An JSC	DHA VN	27,800	17.6	11.3%	1.5%	12.6%	17.6%	16.1%	6.2	1.1
Petrolimex Petrochemical Corp - JSC	PLC VN	12,800	44.6	-4.3%	-4.1%	12.5%	11.0%	3.1%	7.1	0.8

Source: VNDIRECT RESEARCH, BLOOMBERG

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### 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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