

## POWER CONSTRUCTION JSC NO.1 (PC1) - UPDATE

<b>Market Price</b> VND24,850	<b>Target Price</b> VND28,400	<b>Dividend Yield</b> 0.0%	<b>Rating</b> ADD	<b>Sector</b> INDUSTRIALS
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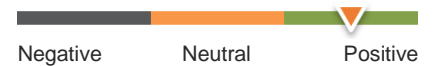
### Outlook – Short term



### Outlook – Long term



### Valuation



18 February 2019

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**PC1's 4Q18 net profit was disappointing despite a strong recovery in the M&E segment. We are Neutral in the short-term because of an expected earnings slowdown in 2019 but are positive over the long-term based on a series of new projects in both the real estate and hydro segments as well as a potential rise in M&E contracting volume. Maintain Add with a TP of VND28,400.**

### Price performance



Source: VNDIRECT

### Key statistics

52w high (VND)	30,435
52w low (VND)	20,600
3m Avg daily volume (shares)	188,902
3m Avg daily value (VNDmn)	4,393
Market cap (VNDbn)	3,299
Outstanding shares (m)	133
Free float (%)	71
TTM P/E (x)	7.1
Current P/B (x)	1.1

### Ownership

Trinh Van Tuan	17.7%
Vietnam Enterprise Investments Ltd.	11.1%
Vietnam Holding Limited	4.1%
Others	67.1%

Source: VNDIRECT

**4Q18 results: strong sales execution but margins disappointed.** In 4Q18, PC1 reported net revenue of VND1,507.2bn (+75.4% yoy) thanks to the recovery of the M&E business with a surge in the grid erection and installation segment (+65.2% yoy). However, net profit only reached VND50.9bn (-10.7% yoy) due to sharp gross margin contraction. In 4Q18, blended gross margin (GM) declined to 10.3%, down from 13.6% in the same period of 2017. This drop was due to continued margin erosion in the M&E segment and negative GM of the real estate segment due to the booking of land use rights costs for the My Dinh Plaza 2 project.

**Full-year profit was slightly weaker than expected.** In FY18, the company achieved revenue of VND5,085bn (+60.9% yoy) and net profit of VND462bn (+95.1% yoy). While topline was in line with our estimate, net profit was 7.5% below our estimate, mostly due to a one-off payment for My Dinh Plaza 2 project's land use rights.

**Strong order book to start the new year.** In 2019, management expects growth in the grid erection and installation segment with a strong order backlog of VND2,829bn at the beginning of 2019, much higher than that of last year (VND1,300bn). The backlog in the steel pole production sub-segment of the the industrial manufacturing segment was also robust thanks to contract wins from the third national transmission line project. We forecast a 32.1% increase in revenue from the grid erection and installation and steel pole segments in 2019. However, we brace for a further possible deterioration in gross margin of these segments, which could drag on PC1's earnings growth.

**Earnings likely to drop in 2019F but we expect a recovery in 2020-21F.** The company management targets to achieve revenue of VND6,229bn and net profit of VND436bn in FY19. In our view, these targets are overly-ambitious due to chronic issues in M&E project execution and limited ability to complete a huge workload in a short time. We estimate 2019 revenue to be flattish at VND5,095bn and net profit to reach VND400bn (-13.5% yoy). However, we expect earnings to recover in 2020-21F thanks to 1) the launch of new real estate projects (Thanh Xuan (Q1/2020), Vinh Hung (Q2/2021); 2) new hydropower plants coming onstream (Mong An (Q3/2019), Bao Lac B (Q4/2019) and Song Nhiem (Q3/2020); 3) a surge in M&E contract wins due to the need to upgrade the national transmission grid.

Financial summary (VND)	12-16A	12-17A	12-18A	12-19E
Net revenue (bn)	3,008	3,161	5,085	5,095
Revenue growth	(3.0%)	5.1%	60.9%	0.2%
Gross margin	17.5%	15.2%	16.9%	15.0%
EBITDA margin	15.2%	16.3%	17.1%	16.6%
Net profit (bn)	305	237	462	400
Net profit growth	24.1%	(22.3%)	95.1%	(13.5%)
Recurring profit growth	24.1%	(22.3%)	95.1%	(13.5%)
Basic EPS	2,295	1,782	3,478	3,010
Adjusted EPS	2,125	1,644	3,478	2,859
BVPS	16,952	20,215	23,454	25,978
ROAE	18.7%	10.2%	15.9%	12.2%

Source: VNDIRECT

Figure 1: 4Q18 Results review

FYE (VND bn)	4QFY18	yoy	FY18	yoy	vs. our forecast	Comments
		chg		chg		
<b>Net revenue</b>	<b>1,507.2</b>	<b>75.4%</b>	<b>5,085.5</b>	<b>60.9%</b>	<b>98.4%</b>	In line with our expectations
<i>Industrial manufacturing</i>	521.1	18.0%	1,753.3	59.5%		Surge in trading activities and recovery of steel pole production business in 4Q
<i>Grid erection &amp; installation</i>	727.2	65.2%	1,730.2	32.8%		Recovered in 4Q as expected
<i>Real estate</i>	106.0	2918.4%	968.6	7170.4%		Recognition of revenue from My Dinh Plaza 2
<i>Hydropower</i>	130.0	51.2%	559.4	100.2%		Contribution of new hydropower plants
<i>Other</i>	23.0	-15.5%	74.0	10.1%		
<b>Gross profit</b>	<b>155.9</b>	<b>35.6%</b>	<b>859.3</b>	<b>78.6%</b>	<b>95.2%</b>	Lower than our expectations
<i>Gross profit margin</i>	10.3%	-3.3% pts	16.9%	1.7% pts		Lower than our forecast (17.5% due to a sharp deterioration in 4Q gross margin)
Selling expenses	6.7	na*	54.2	na*		
G&A expenses	54.6	26.3%	159.9	12.1%	<b>98.7%</b>	In line with our expectations, a surge in G&A expenses was mainly driven by a rise in labor expenses
<b>Operating profit</b>	<b>94.6</b>	<b>9.6%</b>	<b>645.2</b>	<b>81.7%</b>	<b>94.1%</b>	
<b>Financial expenses</b>	<b>33.8</b>	<b>-3.4%</b>	<b>117.0</b>	<b>26.5%</b>	<b>107.5%</b>	Higher than our expectations due to higher interest rate for short-term borrowings
<b>Gain/loss from JVs</b>	<b>1.1</b>	<b>-88.5%</b>	<b>4.7</b>	<b>696.9%</b>	<b>97.7%</b>	In 4Q18, there was a sharp decline in Cao Bang Steel's earnings (PC1's affiliate) due to decreasing steel prices and rising raw material prices
<b>Net profit</b>	<b>50.9</b>	<b>-9.6%</b>	<b>461.8</b>	<b>95.1%</b>	<b>92.5%</b>	Lower than our expectations because of unexpected weak earnings in 4Q
<b>EPS (dong/share)</b>	<b>383</b>	<b>-9.6%</b>	<b>3,478</b>	<b>95.1%</b>	<b>92.5%</b>	

Source: PC1, VNDIRECT

(\*): There was a huge reversal of provision for insurance expenses in 2017, leading to a positive value of selling expense.

## VALUATION

My Dinh Plaza 2 project contributed 29.0% of PC1's gross profit in 2018, leading to a surge in PC1's net profit. In 2019F, we project a 13.5% decline in PC1's net profit because: 1) we assume most revenue from PC1's new real estate projects will be booked in 2020-21F and 2) the recovery in the grid erection and steel pole production will not be sufficient to offset a significant drop in profit booking from the real estate segment.

We used the SOTP valuation method based on PC1's 2019F outlook to arrive at the target price of VND28,400. Our ADD rating is underpinned by several factors: 1) a drop in the real estate segment in 2019F is broadly expected and not alarming given the inherent volatility in revenue booking in this segment as it is not yet a core business of the company; 2) a recovery in the grid erection and installation segments on the back of a strong order backlog; 3) stable cash flow from hydropower segment which will see further capacity addition post-2019.

Downside risks to our call include: 1) lower-than-expected revenue growth of the grid erection and installation segment as well as steel pole production segment; and 2) lower-than-expected margins. Key upside catalysts are: 1) Sooner-than-expected launch of the Thanh Xuan project; 2) stronger-than-expected revenue execution in the company's M&E segment.

Figure 2: SOTP valuation estimate

Segment	Value (VND bn)	% of total	Valuation methodology
M&E & Industrial manufacturing	1,028.5	27.3%	Target P/E of 6x
Real estate development	178.2	4.7%	NAV, discount rate of 16%
Real estate investment	30.8	0.8%	DCF, discount rate of 16%, terminal growth rate: 0%
Hydropower	2,439.9	64.7%	DCF, discount rate of 8.5%, terminal growth rate: 1%
Other	92.6	2.5%	Book value
<b>Total</b>	<b>3,770.0</b>		
No of shares outstanding (shares)	132,769,862		
<b>Target price (VND/share)</b>	<b>28,400</b>		

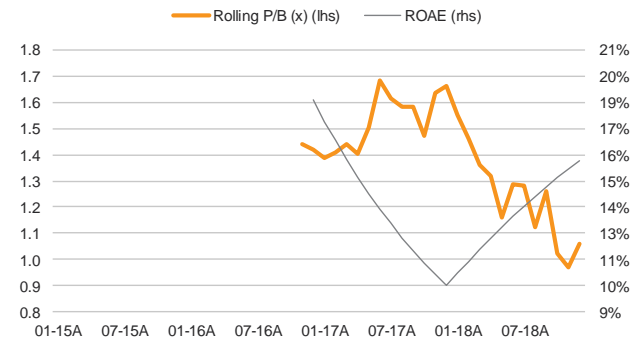
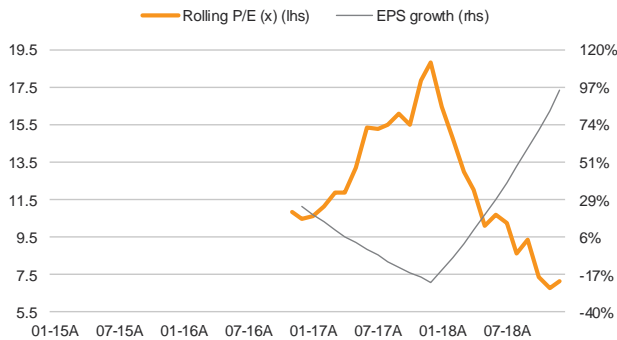
Source: VNDIRECT

Figure 3: Peer comparison

Ticker	Market cap	TTM NPAT growth	TTM EPS growth	ROA	ROE	Net D/E	P/E	P/B	EV/EBITDA
	(US\$ m)	(%)	(%)	(%)	(%)	(%)	(x)	(x)	(x)
<b>Speciality Construction</b>									
TV2 VN Equity	65.3	4.6	6.4	11.9	37.4	(142.6)	6.8	2.2	2.0
VNE VN Equity	14.9	36.1	48.1	5.5	9.1	3.3	4.1	0.4	na
SC5 VN Equity	15.6	(33.8)	(33.8)	2.0	11.4	19.7	9.1	1.0	5.2
TV3 VN Equity	13.3	68.2	98.2	8.2	23.4	(84.9)	20.6	3.0	7.5
SJE VN Equity	15.8	(57.8)	(58.6)	1.9	7.4	129.9	12.2	0.9	8.4
TV4 VN Equity	12.1	0.9	(6.8)	9.5	13.8	(30.5)	11.1	1.5	11.3
<i>Average</i>	<i>22.8</i>	<i>3.0</i>	<i>8.9</i>	<i>6.5</i>	<i>17.1</i>	<i>(17.5)</i>	<i>10.6</i>	<i>1.5</i>	<i>6.9</i>
<i>Median</i>	<i>15.2</i>	<i>2.7</i>	<i>(0.2)</i>	<i>6.9</i>	<i>12.6</i>	<i>(13.6)</i>	<i>10.1</i>	<i>1.3</i>	<i>7.5</i>
<b>Hydropower</b>									
SHP VN Equity	92.9	1.8	(3.8)	7.9	13.9	72.0	12.7	1.7	6.3
SJD VN Equity	64.2	(0.7)	(0.7)	13.3	18.7	9.5	7.7	1.5	4.9
VPD VN Equity	70.7	5.3	5.3	6.1	14.0	-	9.6	1.4	5.6
SEB VN Equity	42.8	(32.1)	(32.1)	12.4	27.2	49.9	9.8	2.5	7.7
ISH VN Equity	30.8	274.1	321.3	8.4	13.6	41.7	10.2	1.3	5.1
GHC VN Equity	27.7	66.0	66.0	29.5	34.3	(37.7)	5.9	1.9	4.3
DRL VN Equity	20.8	(18.1)	(17.3)	36.0	36.7	(59.0)	9.8	3.8	6.8
HJS VN Equity	20.7	(0.8)	(0.9)	10.2	15.7	3.0	10.5	1.6	5.8
PIC VN Equity	16.2	(29.2)	(31.2)	5.0	8.4	52.7	13.0	1.1	8.1
<i>Average</i>	<i>43.0</i>	<i>41.4</i>	<i>45.5</i>	<i>13.7</i>	<i>19.9</i>	<i>22.0</i>	<i>9.9</i>	<i>1.9</i>	<i>5.9</i>
<i>Median</i>	<i>30.8</i>	<i>0.6</i>	<i>(0.8)</i>	<i>9.3</i>	<i>16.1</i>	<i>25.6</i>	<i>9.8</i>	<i>1.6</i>	<i>5.7</i>
<b>PC1 VN Equity</b>	<b>142.2</b>	<b>95.1</b>	<b>95.1</b>	<b>7.2</b>	<b>16.0</b>	<b>36.0</b>	<b>7.1</b>	<b>1.1</b>	<b>5.8</b>

Source: VNDIRECT

**Valuation**



**Income statement**

(VNDbn)	12-17A	12-18A	12-19E
Net revenue	3,161	5,085	5,095
Cost of sales	(2,679)	(4,226)	(4,333)
Gen & admin expenses	(126)	(160)	(153)
Selling expenses	0	(54)	(10)
<b>Operating profit</b>	<b>355</b>	<b>645</b>	<b>599</b>
Operating EBITDA	470	800	781
<b>Depreciation and amortisation</b>	<b>(115)</b>	<b>(155)</b>	<b>(182)</b>
<b>Operating EBIT</b>	<b>355</b>	<b>645</b>	<b>599</b>
Interest income	11	26	22
Financial expense	(103)	(143)	(176)
Net other income	40	40	40
Income from associates & JVs	1	5	5
<b>Pre-tax profit</b>	<b>303</b>	<b>573</b>	<b>490</b>
Tax expense	(47)	(87)	(64)
Minority interest	(20)	(25)	(27)
<b>Net profit</b>	<b>237</b>	<b>462</b>	<b>400</b>
Adj. net profit to ordinary	237	462	400
Ordinary dividends			
<b>Retained earnings</b>	<b>237</b>	<b>462</b>	<b>400</b>

**Balance sheet**

(VNDbn)	12-17A	12-18A	12-19E
Cash and equivalents	567	741	1,006
Short term investments	100	50	50
Accounts receivables	1,302	1,633	1,636
Inventories	1,085	759	1,128
Other current assets	38	46	49
<b>Total current assets</b>	<b>3,092</b>	<b>3,229</b>	<b>3,868</b>
Fixed assets	2,816	2,969	3,923
Total investments	91	99	97
Other long-term assets	213	360	359
<b>Total assets</b>	<b>6,212</b>	<b>6,657</b>	<b>8,247</b>
Short-term debt	294	416	651
Accounts payable	794	816	1,068
Other current liabilities	745	574	577
<b>Total current liabilities</b>	<b>1,833</b>	<b>1,805</b>	<b>2,296</b>
Total long-term debt	1,527	1,554	2,318
Other liabilities	40	24	25
Share capital	1,155	1,328	1,328
Retained earnings reserve	716	920	1,239
<b>Shareholders' equity</b>	<b>2,684</b>	<b>3,114</b>	<b>3,449</b>
Minority interest	128	159	159
<b>Total liabilities &amp; equity</b>	<b>6,212</b>	<b>6,657</b>	<b>8,247</b>

**Cash flow statement**

(VNDbn)	12-17A	12-18A	12-19E
<b>Pretax profit</b>	<b>303</b>	<b>573</b>	<b>490</b>
Depreciation & amortisation	115	155	182
Tax paid	(63)	(66)	(64)
Other adjustments	22	23	(64)
<b>Change in working capital</b>	<b>(558)</b>	<b>(179)</b>	<b>(95)</b>
<b>Cash flow from operations</b>	<b>(181)</b>	<b>506</b>	<b>449</b>
Capex	(821)	(521)	(1,130)
Proceeds from assets sales	2	3	0
Others	(76)	30	1
Other non-current assets changes	0	0	0
<b>Cash flow from investing activities</b>	<b>(895)</b>	<b>(487)</b>	<b>(1,129)</b>
New share issuance	519	17	0
Shares buyback	(0)	0	0
Net borrowings	705	149	964
Other financing cash flow	0	(0)	(11)
Dividends paid	0	(10)	(10)
<b>Cash flow from financing activities</b>	<b>1,224</b>	<b>156</b>	<b>944</b>
Cash and equivalents at beginning of period	419	567	741
<b>Total cash generated</b>	<b>148</b>	<b>174</b>	<b>264</b>
Cash and equivalents at the end of period	567	741	1,006

**Key ratios**

	12-17A	12-18A	12-19E
<b>Dupont</b>			
Net profit margin	7.5%	9.1%	7.8%
Asset turnover	0.59	0.79	0.68
ROAA	4.4%	7.2%	5.4%
Avg assets/avg equity	2.31	2.22	2.27
ROAE	10.2%	15.9%	12.2%
<b>Efficiency</b>			
Days account receivable	101	79	77
Days inventory	148	66	95
Days creditor	108	70	90
Fixed asset turnover	1.28	1.76	1.48
ROIC	5.1%	8.8%	6.1%
<b>Liquidity</b>			
Current ratio	1.69	1.79	1.68
Quick ratio	1.09	1.37	1.19
Cash ratio	0.36	0.44	0.46
Cash cycle	141	74	82
<b>Growth rate (yoy)</b>			
Revenue growth	5.1%	60.9%	0.2%
Operating profit growth	(10.6%)	81.7%	(7.1%)
Net profit growth	(22.3%)	95.1%	(13.5%)
EPS growth	(22.3%)	95.1%	(13.5%)
<b>Share value</b>			
Basic EPS (VND)	1,782	3,478	3,010
BVPS (VND)	20,215	23,454	25,978

Source: VNDIRECT

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- 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.*

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- 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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