

QUANG NGAI SUGAR JSC (QNS) - UPDATE

Market Price	Target Price	Dividend Yield	Rating	Sector
VND39,300	VND44,600	4.47%	HOLD	CONSUMER GOODS

Outlook – Short term



Outlook – Long term



Valuation



28 August 2018

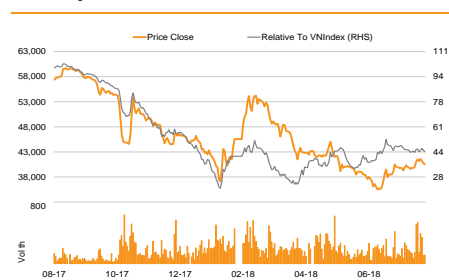
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Key changes in the report

- Increase FY18 net profit forecast by 5.4%
- Reduce target price by 18.5% post adjustment for stock dividend

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	59,685
52w low (VND)	35,500
3m Avg daily volume (shares)	189,981
3m Avg daily value (VNDmn)	7,521
Market cap (VNDbn)	11,556
Outstanding shares (m)	254
Free float (%)	80
TTM P/E (x)	10.7
Current P/B (x)	2.4

Ownership

Thanh Phat Trading Ltd.	15.8%
Foremost Worlwide Limited	5.2%
Võ Thanh Đàng	5.0%
Others	74.0%

Source: VNDIRECT

QNS booked 1H18 revenue of VND3,973bn and net profit of VND562bn. Results were disappointing due to weak revenue growth despite a massive increase in sugar sales volume. We downgrade our QNS outlook to Neutral due to intensifying competition in the soymilk segment and a negative market outlook for sugar prices in 2H18. We reduce our TP to VND44,600. Downgrade to HOLD.

Soymilk unable to recover due to intense competition. Soymilk sales decreased 5% yoy in 2Q18 following an 11% yoy drop in the previous quarter. We think one reason for this poor performance was the introduction of new products from competitors, especially walnut soymilk introduced by Vinamilk (VNM, HOSE) in March. We are concerned about QNS's ability to maintain its market share (86% in 2017) as the company has not announced any solid measures to counter increasing competition in the packaged soymilk segment.

Sugar production expansion mitigated price fall. Refined sugar (RS) ASP in 2Q18 plunged by 24.5% yoy and 11.3% YTD but sales in the segment still soared by 40.7% yoy due to an 85.6% increase in sales volume with the expanded An Khe plant running at full capacity. The Vietnam Sugar Association (VSSA) forecasts the domestic sugar price to continue sliding in 2H18. We are thus not optimistic about the outlook for the sugar segment.

Others segment sales supported by bioenergy but unlikely to contribute in second half. The launch of the biomass plant in 2Q18 added roughly VND100bn to the turnover of the "Others" segment, turning its revenue performance from slightly negative to positive. The biomass plant underwent a seasonally scheduled shut down in Jun 2018 and will not operate until the 2018-19 sugar harvesting season starts in late November. As such, its contribution to 2H18 results will be limited.

We reduce our topline forecast but lift our earnings forecast given lower-than-expected sales in sugar and soymilk but higher margins for these segments than previously expected. The two main segments of QNS saw improved gross margins in 2Q18 due to (1) a lower sugar cane input price for the RS operation, (2) one of QNS's soymilk plants was fully depreciated in 4Q2017. For FY2018, we expect topline growth of 2.6% and net profit growth of 10.0%.

Valuation not attractive due to absence of sustainable growth drivers. We reduce our target price to VND44,600/share and downgrade to HOLD due to (1) a negative outlook for the sugar segment given decreasing market sugar prices, (2) lack of effective countermeasures to rising soymilk competition.

Financial summary (VND)	12-15A	12-16A	12-17A	12-18E
Net revenue (bn)	7,785	6,972	7,633	7,830
Revenue growth	24.6%	(10.4%)	9.5%	2.6%
Gross margin	29.5%	32.6%	26.2%	26.9%
EBITDA margin	22.6%	27.8%	21.3%	23.8%
Net profit (bn)	1,230	1,410	1,027	1,130
Net profit growth	58.9%	14.6%	(27.2%)	10.0%
Basic EPS	11,556	10,646	5,797	4,919
FD EPS	5,112	5,689	4,062	4,447
BVPS	22,063	25,120	21,836	19,875
ROAE	56.6%	43.3%	24.5%	23.7%

Figure 1: Comparison of financial results

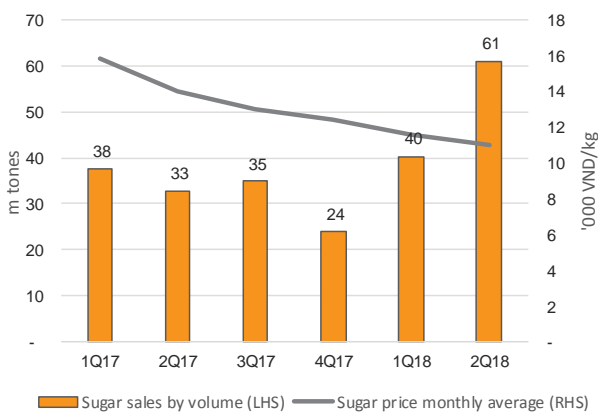
FYE (VNDbn)	2QFY18	yoy	1HFY18	yoy	vs. old forecast	vs. revised forecast	Comments
		chg		chg			
Net revenue	2,390	13.8%	3,999	1.5%	47.1%	51.1%	
<i>Sugar</i>	689	40.7%	1,173	7.5%	48.2%	54.1%	Due to sugar ASP lower -5% than our previous forecast despite higher than expected sales volume
<i>Soymilk</i>	1,095	-0.6%	1,754	-4.8%	39.7%	46.8%	Sale volume decrease due to higher competitions
<i>Others</i>	606	18.8%	1,072	6.7%	65.3%	56.1%	
Gross profit	656	25.4%	1,063	12.9%	52.1%	50.6%	
<i>Gross profit margin</i>	27.5%	+2.6% pts	26.6%	+2.7% pts			GPM improved with lower input price and lower depreciation expenses
<i>Selling expenses</i>	(175)	1.3%	(349)	5.5%	46.6%	48.8%	Mainly due to unexpected higher employee expense in 2Q18
<i>G&A expenses</i>	(53)	50.3%	(95)	38.2%	63.8%	63.4%	
Operating profit	428	35.8%	619	14.3%	54.1%	50.0%	
<i>Pre-tax profit</i>	421	23.9%	630	12.5%	53.3%	50.6%	
Net profit	374	39.7%	562	14.8%	52.4%	49.7%	

Source: VNDIRECT

1H2018 SUGAR REVENUE GREW; SOYMILK REVENUE FELL

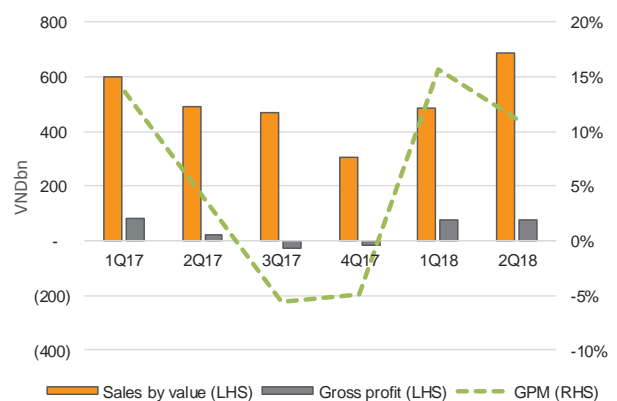
Sharp increase in production mitigated fall in market sugar price. The expanded An Khe sugar plant ran at full capacity in the 2017-18 season producing roughly 206m tonnes of RS sugar. The production was 47% higher than the same period last year. Such a huge jump in production helped the company manage growth in its sugar segment while factory-level sugar prices recorded in June 2018 fell 21% yoy according to *Agromonitor*. We estimate that the company sold about 101m tonnes of RS sugar in 1H18 (+44% yoy) and has about 105m tonnes left in inventory.

Figure 2: Sugar sales volume & Sugar price



Source: VNDIRECT

Figure 3: Sugar segment performance



Source: VNDIRECT

Lower sugar cane price helped improve sugar gross margin. QNS successfully adjusted down the purchase price for sugar cane from farmers by 20% in the crop season 2017-18 to manage the fall in refined sugar spot prices. The adjustment helped gross margin expand from 9% in 1H2017 to 13% in 1H2018. Gross profit surged 50% yoy to VND153bn in 1H2018 after a sharp decrease in 2H17.

Soymilk recorded negative growth for 2nd quarter in a row. This segment's growth rate was negative 5% in 1H18 (-1% yoy in 2Q18 and -11% yoy in 1Q18). The result was disappointing because QNS had just started operations in its 3rd soymilk factory in Binh Duong province,

raising total capacity to 390 m litres (+30%) in late Dec 2017. Lower sales of soymilk may be due to competition from Vinamilk's new walnut soymilk for the premium market since March 2018. The product has been warmly welcomed because walnut and soymilk are believed to be extremely good for women, especially expectant mothers.

Figure 4: Vinamilk's new walnut soymilk product – Launched in March 2018



Source: VNDIRECT

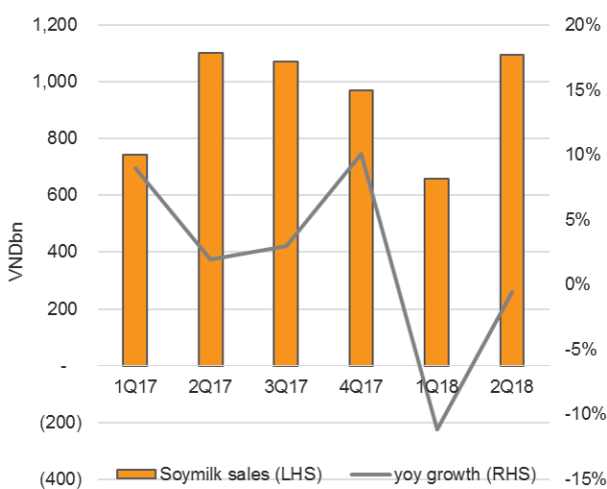
Figure 5: Soymilk brands in Vietnam

Brand	Fami	Vinasoy	VNM original	VNM walnut	Nuti	Soy SecretZ	Vitasoy
Producer	Vinasoy	Vinasoy	Vinamilk	Vinamilk	Nutifoods	Dutch Mill	Vitasoy
	Vietnam	Vietnam	Vietnam	Vietnam	Vietnam	Thailand	Vietnam
Retail price (VND/ml)	24	26	21	33	20	49	na

Source: VNDIRECT

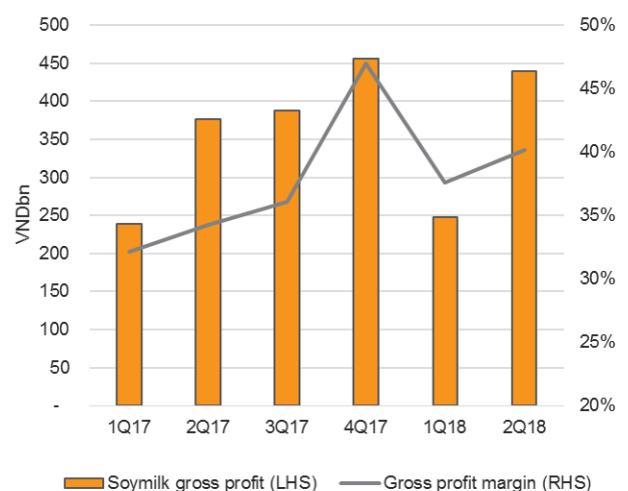
Improved margin, supported by lower depreciation and raw material price, helped partly offset effect of poor soymilk sales. Lower depreciation helped COGS decrease 4.6% yoy in 1H18. In addition, the fall in sugar prices more than offset the rise in soybean prices, resulting in a net reduction in COGS of 1.2% yoy. As a result, soymilk segment gross margin rose to 39.2% (+4.8%pts from 1H17), helping the segment achieve gross profit of VND687bn (+12% yoy) despite a reduction in sales.

Figure 6: Quarterly soymilk sales by value



SOURCE: VNDIRECT

Figure 7: Soymilk gross profit quarterly



SOURCE: VNDIRECT

2018F OUTLOOK

We reduce our 2018 revenue forecast but raise our net profit forecast. Our revised projection is based on the following assumptions: (1) Sugar sales volume rises 50% yoy in 2H18, leading to an increase in sugar sales by value despite a possible 9% further decrease in the average market sugar price in the period, compared

to the average price recorded in 1H18. (2) Soymilk market share in 2H18 decreases slightly as the company has not developed effective measures to counter increased competition; we note that the company will continue benefiting from lower sugar prices; (3) Sales in the Others segment will remain on an even keel from last year and the biomass plant will contribute limited revenue to total Group revenue. This is because the plant was shut down in June 2018 and will only resume operations in late November when the 2018-19 sugar season begins.

Figure 8: Earnings revision

FYE (VNDbn)	2017A		2018F		Comments
		Old	New	%change	
Net revenue	7,633	8,489	7,830	-7.8%	Assume -8% lower sugar ASP. Soymilk sales forecast to decrease 15% with poor performance in 1H18
Net revenue growth	9.5%	11.2%	2.6%	-8.6% pts	
Gross profit	1,996	2,043	2,104	3.0%	
Gross profit margin	26.2%	24.1%	26.9%	-2.8% pts	Higher GM due to lower input price and lower depreciation
EBIT	1,153	1,145	1,239	8.2%	
EBT	1,138	1,182	1,245	5.3%	
Net profit	1,027	1,072	1,130	5.4%	
EPS (VND)	5,399	4,668	4,919	5.4%	

Source: VNDIRECT

VALUATION

Our target price for QNS is VND44,600/share implying a 13.4% upside. We apply target P/E for the soymilk, sugar segment and other segment of 10.9x, 11.0x and 9.0x, equal to the peer average trailing P/E. We downgrade to a HOLD recommendation.

Figure 9: SOTP valuation

	%EBT	EBT FY2018	Tax rate	NPAT FY18	Target P/E (x)	Target price (VND)
Soymilk	70%	870	12%	770	10.9	31,277
Sugar	13%	168	3%	163	11.0	6,640
Others	17%	208	5%	198	9.0	6,642
				Target price		44,560

Source: VNDIRECT

Figure 10: Peer comparison (Data as 15 Aug 2018)

Company	Country	Market cap (US\$ m)	TTM NPAT growth (%)	TTM EPS growth (%)	ROA (%)	ROE (%)	D/E (x)	TTM P/E (x)	P/B (x)
Soymilk									
VNM	Vietnam	10,119.1	-2.4%	-2.5%	28.5%	38.9%	0.4x	23.7x	8.9x
VCF	Vietnam	187.3	14.4%	14.4%	24.7%	50.4%	0.7x	6.8x	4.0x
SKH	Vietnam	30.0	56.8%	na	na	na	na	4.8x	1.9x
SKV	Vietnam	23.9	16.2%	1.6%	na	na	na	8.3x	2.2x
Average								10.9x	
Sugar									
SBT	Vietnam	415.9	14.0%	28.1%	3.0%	8.0%	1.9x	17.3x	1.7x
SLS	Vietnam	27.5	-16.6%	-16.6%	9.8%	26.4%	1.9x	5.4x	1.3x
KTS	Vietnam	4.0	7.1%	7.1%	2.2%	6.0%	2.3x	10.1x	0.6x
Average								11.0x	
Others									
<u>Beers</u>									
BSP	Vietnam	10.8	-8.9%	-8.9%	12.1%	19.0%	0.6x	5.5x	1.1x
HAT	Vietnam	4.7	19.2%	19.2%	21.8%	58.1%	2.4x	3.1x	2.0x
THB	Vietnam	6.5	-22.5%	-22.5%	2.4%	4.3%	1.4x	18.4x	0.9x
<u>Mineral water</u>									
QHW	Vietnam	7.5		-3.9%				5.4x	1.3x
<u>Electricity</u>									
HJS	Vietnam	20.6	12.2%	12.2%	9.4%	15.2%	0.7x	10.7x	1.7x
QPH	Vietnam	12.4	3.2%	8.9%	9.4%	14.1%	0.5x	7.0x	
<u>Confectionery</u>									
BBC	Vietnam	53.5	0.2%	-2.1%	9.0%	11.8%	0.3x	13.0x	1.5x
Average								9.0x	
QNS		508.4	10.8%	-7.9%	14.7%	23.8%	0.7x	10.7x	2.4x

Source: VNDIRECT, FiiPro

Valuation

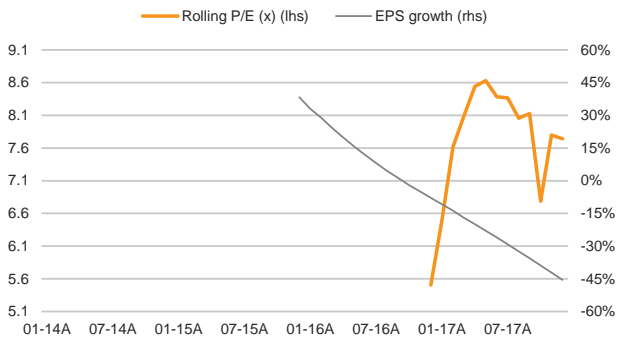
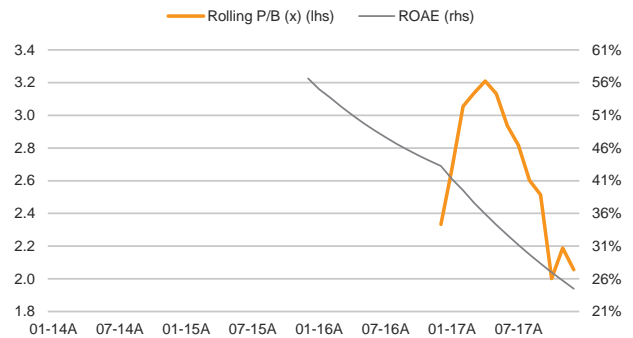


Figure 11: Key ratios



Source: VNDIRECT

Income statement

(VNDbn)	12-16A	12-17A	12-18E
Net revenue	6,972	7,633	7,830
Cost of sales	(4,697)	(5,637)	(5,726)
Gen & admin expenses	(44)	(146)	(150)
Selling expenses	(715)	(697)	(715)
Operating profit	1,516	1,153	1,239
Operating EBITDA	1,840	1,567	1,787
Depreciation and amortisation	(324)	(414)	(548)
Operating EBIT	1,516	1,153	1,239
Interest income	73	38	53
Financial expense	(77)	(78)	(74)
Net other income	31	26	27
Income from associates & JVs	0	0	0
Pre-tax profit	1,543	1,138	1,245
Tax expense	(133)	(112)	(115)
Minority interest	0	0	0
Net profit	1,410	1,027	1,130
Adj. net profit to ordinary	1,410	1,027	1,130
Ordinary dividends	(402)	(366)	(414)
Retained earnings	1,008	661	715

Balance sheet

(VNDbn)	12-16A	12-17A	12-18E
Cash and equivalents	137	528	503
Short term investments	555	751	951
Accounts receivables	395	289	389
Inventories	519	320	405
Other current assets	170	19	209
Total current assets	1,775	1,907	2,457
Fixed assets	4,120	4,852	4,980
Total investments	0	0	0
Other long-term assets	229	240	175
Total assets	6,124	6,999	7,611
Short-term debt	1,178	1,404	1,292
Accounts payable	475	540	575
Other current liabilities	315	401	554
Total current liabilities	1,968	2,345	2,421
Total long-term debt	213	145	79
Other liabilities	32	27	62
Share capital	1,875	2,438	2,926
Retained earnings reserve	2,198	2,135	2,135
Shareholders' equity	3,911	4,482	5,049
Minority interest	0	0	0
Total liabilities & equity	6,124	6,999	7,611

Cash flow statement

(VNDbn)	12-16A	12-17A	12-18E
Pretax profit	1,543	1,138	1,245
Depreciation & amortisation	324	414	548
Tax paid	(137)	(116)	(115)
Other adjustments	(73)	57	6
Change in working capital	(497)	131	(269)
Cash flow from operations	1,160	1,625	1,415
Capex	(2,121)	(874)	(676)
Proceeds from assets sales	0	0	0
Others	626	(196)	(200)
Other non-current assets changes	61	19	65
Cash flow from investing activities	(1,435)	(1,051)	(811)
New share issuance	103	(0)	0
Shares buyback	0	0	0
Net borrowings	(417)	158	(180)
Other financing cash flow	0	(0)	(35)
Dividends paid	(284)	(339)	(414)
Cash flow from financing activities	(598)	(182)	(629)
Cash and equivalents at beginning of period	1,009	137	528
Total cash generated	(872)	391	(25)
Cash and equivalents at the end of period	136	528	503

Key ratios

	12-16A	12-17A	12-18E
Dupont			
Net profit margin	20.2%	13.5%	14.4%
Asset turnover	1.23	1.16	1.07
ROAA	25.0%	15.6%	15.5%
Avg assets/avg equity	1.73	1.56	1.53
ROAE	43.3%	24.5%	23.7%
Efficiency			
Days account receivable	1.14	1.04	1.01
Days inventory	40.4	20.7	25.8
Days creditor	37.0	34.9	36.6
Fixed asset turnover	2.38	1.70	1.59
ROIC	26.6%	17.0%	17.6%
Liquidity			
Current ratio	0.90	0.81	1.01
Quick ratio	0.64	0.68	0.85
Cash ratio	0.35	0.55	0.60
Cash cycle	4.5	(13.2)	(9.8)
Growth rate (yoy)			
Revenue growth	(10.4%)	9.5%	2.6%
Operating profit growth	13.7%	(24.0%)	7.4%
Net profit growth	14.6%	(27.2%)	10.0%
EPS growth	11.3%	(28.6%)	9.5%
Share value			
FD EPS (VND)	5,689	4,062	4,447
BVPS (VND)	25,120	21,836	19,875

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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Definition:

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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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