

SIAM BROTHERS VIETNAM JSC (SBV)

Market Price VND48,000 **Target Price** VND56,052 **Dividend Yield** 9.3% **Rating** ADD **Sector** INDUSTRIALS

Outlook – Short term



Outlook – Long term



Valuation



24 October 2017

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We initiate on SBV with an ADD recommendation and a target price of VND56,052 based on the following factors: (1) SBV is the leading company in the marine rope and cordages niche market and has a great brand which gives it pricing power (2) Fishermen are shifting to offshore fishing, thereby boosting demand for higher quality rope products which SBV specializes in; and (3) a 40% jump in manufacturing capacity starting in 4Q will ease capacity constraints and lay the foundation for continued growth.

SBV is the leader in the niche market for marine ropes and cordage production with a market share of 36%, which is 2.5 times the market share of the number two market player, Penro.

SBV has pricing power as its brand is well known and synonymous with premium quality... SBV has a premium brand positioning at the higher end of the market and high brand recall among fishermen in Vietnam; management even claims the product is aspirational and a “status symbol” for fishermen and their families. The consequent pricing power is reflected in the fact that ASPs have increased by 3-4% annually on average over the past 3 years.

...and this will help it maintain industry-leading profitability. We expect gross and net margins of 41.8% and 21.2%, respectively in FY17 despite input price rises on the back of the oil price recovery.

The growing trend of fishermen shifting from near-shore to offshore fishing will expand SBV's core addressable market, by boosting demand for higher quality ropes. We estimate the number of offshore vessels could increase by 10% per year over the next 4 years.

The 40% capacity increase scheduled for FY17Q4 is a tangible earnings catalyst and will lay the foundation for SBV to capture the market growth over the next 2 years. We expect SBV's NPAT to surge by 15.7% in FY18, as capacity constraints are eased.

Strong cash flow generation supports generous dividend payout policy. We expect SBV to pay VND4,500 per share per year in the period FY17-18 (yield of 9.3%). According to the resolution of the EGM in October 2017, they will pay an advance cash dividend of VND1,500 per share and a 3:1 stock dividend in November 2017.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	49,200
52w low (VND)	38,222
3m Avg daily volume (shares)	39,870
3m Avg daily value (VND mn)	1,469
Market cap (VND bn)	985
Outstanding shares (m)	20.5
Free float (%)	34.7

Ownership

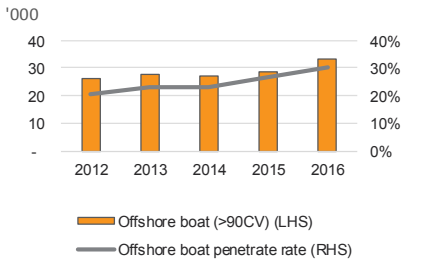
Thong Minh investment JSC (the founder's company)	65.37%
Vietnam Holding Limited	3.62%
Others	31.01%

Source: VNDIRECT

Financial summary (VND)	12-15A	12-16A	12-17E	12-18E
Net revenue (bn)	462	508	574	657
Revenue growth	23.6%	10.1%	13.0%	14.3%
Gross margin	33.9%	42.5%	41.8%	41.3%
EBITDA margin	16.4%	23.4%	26.6%	26.1%
Net profit (bn)	88	116	122	141
Net profit growth	105.5%	31.9%	4.9%	15.7%
Recurring profit growth	105.5%	31.9%	4.9%	15.7%
Basic EPS	4,290	5,656	5,936	6,870
Adjusted EPS	4,290	5,656	5,936	6,870
BVPS	10,778	20,932	22,343	24,464
ROAE	41.0%	35.7%	27.4%	29.4%

Source: VNDIRECT

Vietnam offshore vessel development



Source: VNDIRECT

Continuing shift to offshore fishing is inevitable

According to the General Statistics Office of Vietnam (GSO) and our own estimates, in the FY12-16 period, the number of offshore vessels grew at a CAGR of 6% per year. In fact, the offshore vessel count grew at a CAGR of 11% in the FY14-16 period, indicating that the trend is accelerating. The reasons for this are as follows: (1) Coastal and inshore fish stocks have become scarcer due to overfishing and so fishermen have to actively invest in offshore vessels to fish further out at sea (2) the Government's has offered preferential interest rate loans and higher loan-to-value (LTV) policy as incentives for fishermen to develop their offshore vessels (Decree 67/2014/NĐ-CP). Besides, in order to adapt to the Illegal, Unreported and Unregulated (IUU) Fishing regulations in place internationally, we think the Government will try to formalize the fishing industry through stricter licensing and incentives for fishermen to fish farther out at sea to avoid further depletion of near-shore fish stocks. In fact, in last August, Ministry of Agriculture & Rural Development (MARD) proposed some amendments to Decree 67 to the Government. In this proposal, they suggested that the Government directly fund 35% of the value of new vessels, rather than providing preferential loans. In the period FY14-16, the total number of large-capacity vessels (with engines above 90 CV) increased by 6,200 units, with 10% being built through the incentive program under Decree 67.

The growth in the offshore vessel fleet is spurring demand for both more fishing rope and higher quality of rope as each offshore vessel, on average, usually consumes 3-fold the quantity of ropes used by an inshore vessel (Intage) and ropes used for offshore vessels need to be more "heavy-duty" in nature to resist greater wear-and-tear. This will directly benefit SBV which specializes in high performance ropes.

Real IP a source of lasting competitive advantage: SBV has inherited the trademark and secret rope production formula of the founding Sawatyanon Thai family

SBV uses a secret formula that gives its ropes unique properties and superior performance. These superior performance characteristics allow SBV to sell its products at a premium of 10-30% to similar products from competitors. According to the Company, their products score around 50% higher than competitor products on durability, adhesion, abrasion resistance and tensile strength.

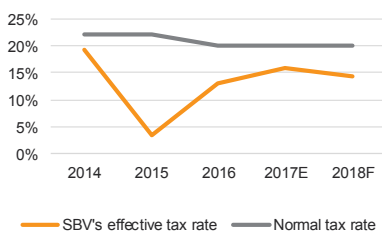
Even SBV's manufacturing equipment is customized to enhance product quality and production efficiency. These equipment modifications have been carried out by major shareholder Thong Minh Investment JSC, whose owner is SBV's Thai chairman, Veerapong Sawatyanon.

Increasing capacity by 40% from 4Q of this year will unlock further growth potential

Currently, the Company has 3 factories, with total capacity of 10,000 tons of finished products per year. Those factories have been operating at a reasonably high utilization 80% of designed capacity. In the last quarter of this year, the Company will commission the newly built fourth factory with a capacity of 4,000 tons/year in Long An built at a capex of VND110bn (USD4.8mn), including VND30bn (USD1.3mn) for the factory building and VND80bn (3.5USDmn) for equipment. We believe this factory will run at a capacity utilization of 80% by FY20 thanks to the continued growth in the offshore vessel fleet which will spur demand for heavy-duty ropes.

Also, this factory will enjoy a tax holiday over the period FY17-18 and about 10%, half of the normal tax rate, in the subsequent four years

SBV's tax rate



Source: VNDIRECT

(FY19-22), which will create significant tax savings for the company over the period.

VALUATION

Assumptions for estimating COE

	Assumed value
Beta	1.00
Risk free rate (based on 10-yr gov bond yield) (%)	5.50
Market risk premium (%)	9.84
COE (%)	15.34
Terminal growth rate (%)	2.50

Source: VNDIRECT

We apply a FCFE-level discounted cash flow analysis to come up with a fair value for SBV, with top-line growth being roughly in line with the development of the offshore vessel fleet in Vietnam. We assume a beta of 1.00 as there are no suitable peers and the Company has limited trading history. We also assume a terminal growth rate of 2.5% and apply a discount rate (COE) of 15.34%. Note that we use FCFE rather than FCFF for the DCF analysis as the company has a highly stable and predictable capital structure.

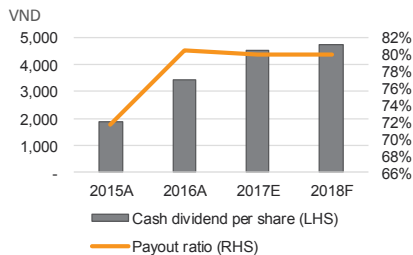
The summary of our valuation is as below:

Valuation (unit: bn. VND)

	2017F	2018F	2019F	2020F	2021F
Net profit	122	141	156	176	210
Net borrowing	-62	11	12	17	20
Non-cash expense (D&A)	25	35	38	44	56
Change in WC	6	32	34	49	56
Capex	-110	-24	-26	-140	-39
FCFE	-32	131	146	48	191
COE	15.3%	15.3%	15.3%	15.3%	15.3%
PV of next 5-yr cash flow	319				
PV of terminal value	830				
Total equity value	1,149				
No. of outstanding shares (million share)	20.50				
Price per share (VND)	56,052				

Source: VNDIRECT

Payout ratio in 2015-2018



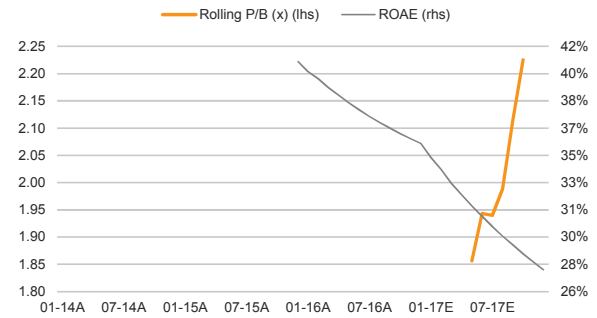
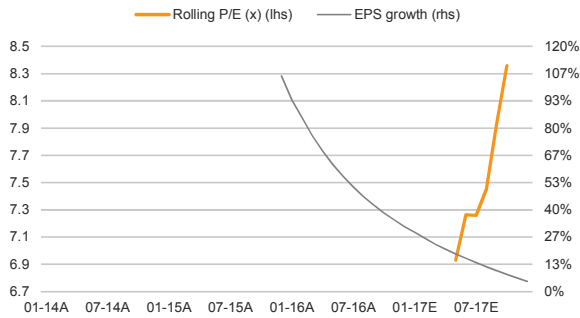
Source: VNDIRECT

Based on the above, the fair value for SBV share price is VND56,052, equivalent to a PER of 8.1x, based on FY18 forecasted EPS.

SBV has historically paid a high cash dividend, at a payout ratio of 70-80% in the period of FY15-16. We estimate that the company could pay out VND4,500 per share per year as cash dividend in 2017 and 2018,

According to the resolution of the EGM, which was held in October 2017, they will pay an advance cash dividend of VND1,500 per share and a 3:1 stock dividend this November.

Valuation



Income statements

(VNDbn)	12-16A	12-17E	12-18E
Net revenue	508	574	657
Cost of sales	(292)	(334)	(385)
Gen & admin expenses	(47)	(54)	(61)
Selling expenses	(30)	(34)	(39)
Operating profit	139	153	171
Operating EBITDA	115	128	136
Depreciation and amortisation	23	25	35
Operating EBIT	139	153	171
Interest income	4	4	4
Financial expense	(12)	(11)	(10)
Net other income	2	0	0
Income from associates & JVs	2	0	0
Pre-tax profit	134	145	165
Taxation	(18)	(23)	(24)
Minority interests	0	0	0
Net profit	116	122	141
Adj. net profit to ordinary	116	122	141
Ordinary dividends	(71)	(93)	(98)
Retained earnings	45	29	44

Balance sheets

(VNDbn)	12-16A	12-17E	12-18E
Cash and equivalents	202	76	107
Short term investments	5	5	5
Accounts receivables	203	207	237
Inventories	42	48	55
Other current assets	17	19	22
Total current assets	469	355	426
Fixed assets	101	188	179
Total investments	0	0	0
Other long-term assets	47	47	47
Total assets	617	590	652
Short-term debt	133	77	89
Accounts payable	11	13	15
Other current liabilities	36	40	46
Total current liabilities	180	131	149
Total long-term debt	7	0	0
Other liabilities	0	0	0
Share capital	205	205	205
Retained earnings reserve	116	145	188
Shareholders' equity	430	459	502
Minority interests	0	0	0
Total liabilities & equity	617	590	652

Cash flow statement

(VNDbn)	12-16A	12-17E	12-18E
Pretax profit	134	145	165
Depreciation & amortisation	23	25	35
Tax paid	(15)	(23)	(24)
Other adjustments	27	0	0
Change in working capital	(78)	(6)	(32)
Cash flow from operations	91	141	144
Capex	(43)	(110)	(24)
Proceeds from assets sales	20	0	0
Others	6	(2)	(2)
Other non-current assets changes	0	0	0
Cash flow from investing activities	(16)	(112)	(26)
New share issuance	136	0	0
Shares buyback	0	0	0
Net borrowings	16	(62)	11
Other financing cash flow	(11)	0	0
Dividends paid	(71)	(93)	(98)
Cash flow from financing activities	69	(155)	(86)
Cash and equivalents at beginning of period	58	202	76
Total cash generated	144	(126)	32
Cash and equivalents at the end of period	202	76	107

Key ratios

	12-16A	12-17E	12-18E
Dupont			
Net profit margin	22.9%	21.2%	21.5%
Asset turnover	0.95	0.95	1.06
ROAA	21.8%	20.2%	22.7%
Avg assets/avg equity	1.64	1.36	1.29
ROAE	35.7%	27.4%	29.4%
Efficiency			
Days account receivable	106	91	91
Days inventory	52.1	52.0	52.0
Days creditor	14.2	14.0	13.9
Fixed asset turnover	4.97	3.98	3.58
ROIC	20.4%	22.7%	23.9%
Liquidity			
Current ratio	2.61	2.72	2.85
Quick ratio	2.37	2.35	2.48
Cash ratio	1.15	0.62	0.75
Cash cycle	144	129	129
Growth rate (yoy)			
Revenue growth	10.1%	13.0%	14.3%
Operating profit growth	46.4%	10.1%	12.2%
Net profit growth	31.9%	4.9%	15.7%
EPS growth	31.9%	4.9%	15.7%
Share value			
Basic EPS (VND)	5,656	5,936	6,870
BVPS (VND)	20,932	22,343	24,464

Source: VNDIRECT

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Definition:

- Add The stock's total return is expected to exceed 15% 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 -10% or more 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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