

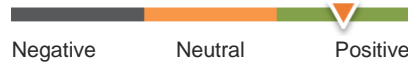
VIETNAM DAIRY PRODUCTS JSC (VNM) – UPDATE

Market Price VND108,500	Target Price VND155,600	Dividend Yield 4.2%	Rating ADD	Sector CONSUMER GOODS
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Outlook – Short term



Outlook – Long term



Valuation



21 February 2020

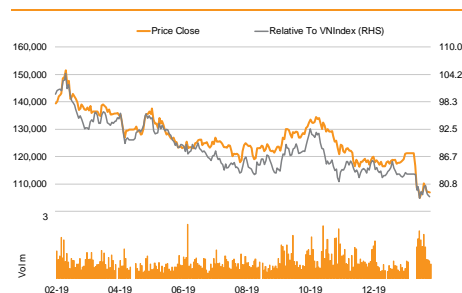
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Key changes in the report

- FY20F revenue and NP increased 3.8% and 2.9% respectively to reflect the consolidation of GTN's results.

Price performance



Source: VND RESEARCH

Key statistics

52w high (VND)	151,600
52w low (VND)	105,000
3m Avg daily volume (shares)	940,367
3m Avg daily value (VNDm)	109,380
Market cap (VNDbn)	186,676
Outstanding shares (m)	1,746
Free float (%)	33.0
TTM P/E (x)	19.5
Current P/B (x)	6.8

Ownership

SCIC	36.0%
F&N Dairy Investment Pte, Ltd	20.0%
Platinum Victory Pte Ltd	10.6%
Others	33.4%

Source: VND RESEARCH

Shelter from the storm

Solid topline growth across the board. VNM posted 4Q19 topline of VND14,239bn, up 9.5% yoy, bringing FY19 revenue to VND56,318bn (+7.1% yoy). In FY19, domestic sales grew 6.3% yoy given solid demand in both urban and rural areas, widening VNM's market share to 61.2% (+0.2% pts yoy). Besides, exports rose 14.8% yoy thanks to the recovery of Middle East market.

FY19 net profit largely in line with our expectation. Gross margin expanded 0.4% pts thanks to lower sugar price and lower milk powder price. However, higher effective corporate income tax (CIT) rate and lower other income together curbed the FY19F net profit growth. As a result, FY19 profit after tax edged up only 3.4% yoy to VND10,554bn.

We expect net profit to grow 13.4% yoy in average in FY20-21F. We expect VNM to register a FY20-21F revenue CAGR of 12.7% on the back of 1) a stable domestic dairy consumption growth of 8.0% p.a., 2) the consolidation of GTN's revenue after acquiring this company, and 3) 20% yoy growth of the export segment thanks to the recovery of Middle East market and new entrance to China.

Reiterate ADD with TP of VND155,600. VNM's share price has dropped 10.5% since 22nd Jan 2020 amid the overall market's concerns over the coronavirus outbreak. We see a minimal impact of Covid-19 on VNM's performance since then. We believe this is time to accumulate a high-quality stock with solid growth at cheap valuation. Our 12-month TP is based on an equal weighting of DCF approach (WACC 9.2%, cost of equity 14.1%, long-term growth 3.5%) and 24.6x FY20F P/E.

Re-rating catalysts include 1) stronger-than-expected domestic dairy consumption, and 2) higher-than-expected demand from the Middle East and China. Downside risks include 1) weaker-than-expected growth of domestic dairy demand, and 2) the price of milk material rising higher than expected.

Financial summary (VND)	12-18A	12-19A	12-20E	12-21E
Net revenue (bn)	52,562	56,318	64,955	71,492
Revenue growth	3.0%	7.1%	15.3%	10.1%
Gross margin	46.8%	47.2%	46.7%	47.1%
EBITDA margin	19.9%	19.5%	18.5%	18.6%
Net profit (bn)	10,184	10,527	12,064	13,448
Net profit growth	(0.7%)	3.4%	14.6%	11.5%
Adjusted EPS	5,295	5,485	6,234	6,949
BVPS	15,084	17,070	17,925	21,146
ROAE	41.4%	38.3%	40.2%	40.1%

Source: VND RESEARCH

2019 Recap: Higher tax rates obscure solid revenue growth recovery

Domestic sales recorded positive growth as demand recovered. Vietnam's dairy product consumption recovered strongly, rising 7.0% yoy in four biggest cities and 15.5% yoy in rural areas, according to Kantar World Panel. We believe the recovery was in place after domestic dairy producers strived to provide more innovative products and conducted more effective marketing strategy. VNM, as the market leader, launched 19 products (+26% yoy), the most remarkable ones were Organic Gold, a brand for organic infant formula and drinking milk, and the premium Yoko Gold infant formula, with all materials imported from Japan. As a result, domestic revenue in FY19 increased 6.3% yoy (versus 2.7% yoy in FY18) to VND47,555bn (accounting for 84.4% of total revenue).

Exports accelerated as traditional markets recovered. With the recovery of the Middle East market, VNM's exports bounced back 14.8% yoy in FY19, rising to VND5,175bn after a weak growth of 2.3% yoy in FY18. Export turnover contributed 9.2% to FY19 net revenue. It's notable that the checking process for China-bound official export permit is underway due to the large size of VNM's factories and milk farm system. We expect the permit to be available in 1H20F and China market will start contributing to VNM's export revenue from 2H20F.

Overseas revenue increased slightly, with mix performance of subsidiaries. Revenue of Angkor Milk, VNM's subsidiary in Cambodia, jumped 26.0% yoy in FY19 to VND1,211bn as its market share expanded to 13% from 10% previously. However, the California (U.S) subsidiary's revenue stayed flat at VND2,687bn (+0.5% yoy) due to weak performance of the local market. Overall, VNM's overseas subsidiaries reported 8.6% yoy increase in revenue in FY19, slightly higher than the previous year.

Increased CIT rate curbed net profit growth. FY19 tax rate stood at 17.5%, or 2.2% pts higher than FY18 after the incentive tax period enjoyed by several factories came to an end. Such a tax policy created a strong pressure on VNM's profit, having trimmed FY19 net margin by 0.7% pts to 18.7%. Therefore, FY19 profit after tax rose a modest 3.4% yoy to VND10,554bn.

Consolidation of GTNFoods had trivial impact on P&L numbers in FY19. VNM completed the acquisition of GTNFoods on 19 Dec 2019 by spending VND3,460bn for a 75% stake, and had its financial report consolidated in 4Q19. However, the move has yet to leave an impact on VNM's 4Q19 P&L given such short period of time. GTNFoods, a famous brand in Vietnam's FMCG sector, posted FY19 revenue and net profit of VND3,000bn and VND13bn, respectively. GTNFoods owns Moc Chau Milk brand, which claims 1.0%~1.5% domestic dairy market share and a large land bank of milk cow farms in Moc Chau highland in Vietnam's Northern region. We believe VNM aims for the large material area controlled by GTNFoods in order to develop high-quality milk farms, which is in line with its milk farm expansion strategy since 2014. In addition, we believe Moc Chau Milk is a decent brand for VNM to compete with TH Milk in the fresh drinking milk segment.

Figure 1: Result comparison

VNDbn	4Q19	4Q18	%yoy chg	FY19	FY18	%yoy chg	2019F	% vs our FY19F forecast	Comment
Revenue	14.239	13.004	9,5%	56.318	52.562	7,1%	57.093	98,6%	
Domestics	11.735	10.850	8,2%	47.555	44.747	6,3%	47.866	99,3%	FY19 domestic ASP edged up 2% yoy and sales volume rose 4.3% yoy thanks for higher domestic dairy demand, especially in rural areas (+15% yoy, according to Kantar World Panel). In FY19, total market share edged up by 0.2% pts
Oversea subsidiaries	932	912	2,2%	3.588	3.305	8,6%	4.356	82,4%	Angkor Milk (Cambodia subsidiary) was the main contributor to VNM overseas subsidiaries' growth in FY19 thanks to its larger market share. Meanwhile, Drifwood Dairy revenue was flat in FY19 due to weak demand in California.
Export	1.572	1.242	26,6%	5.175	4.510	14,8%	4.871	106,3%	Export turnover accelerated in FY19 thanks to the recovery of Middle East market
Gross profit	6.680	6.163	8,4%	26.572	24.611	8,0%	26.748	99,3%	
GPM	46,9%	47,4%	-0,5% pts	47,2%	46,8%	0,4% pts	46,9%	0,3% pts	FY19 GPM gained 0.4% pts as the raw material cost as % of revenue eased 1.9% pts. Note that VNM's raw material cost in FY19 was up only 2.3% yoy when global whole milk powder price increased 4.5% yoy while other materials' prices were uncanged in the period.
Average global whole milk powder price (USD/Tonne)	3.213	2.680	19,9%	3.118	2.985	4,5%	3.050	102,2%	
SG&A	4.183	3.691	13,3%	14.390	13.399	7,4%	14.736	97,6%	
SG&A as % of revenue	29,4%	28,4%	1,0% pts	25,6%	25,5%	0,1% pts	25,8%	-0,3% pts	
EBIT	2.497	2.471	1,1%	12.182	11.212	8,7%	12.012	93,3%	
EBIT margin	17,5%	19,0%	-1,5% pts	21,6%	21,3%	0,3% pts	21,0%	0,3% pts	
Other profit	152	209	-27,3%	613	840	-27,0%	763	80%	
as % revenue	1,1%	1,6%	-0,5% pts	1,1%	1,6%	-0,5% pts	1,3%	-0,2% pts	
Pre-tax profit	2.649	2.680	-1,2%	12.796	12.052	6,2%	12.775	100,2%	
EBT margin	18,6%	20,6%	-2,0% pts	22,7%	22,9%	-0,2% pts	22,4%	0,3% pts	
Tax	473	396	19,4%	2.241	1.846	21,4%	2.084	107,5%	
Tax rate	17,8%	14,8%	3,1% pts	17,5%	15,3%	2,2% pts	16,3%	1,2% pts	VNM's CIT rate increased 2.2% pts yoy in FY19, after the tax incentive period enjoyed by some factories was over.
NPAT	2.151	2.269	-5,2%	10.554	10.206	3,4%	10.690	98,7%	
Net margin	15,1%	17,4%	-2,3% pts	18,7%	19,4%	-0,7% pts	18,7%	0,0% pts	
FD EPS (VND)	1.235	1.303	-5,2%	5.485	5.295	3,6%	5.415	98,7%	

Source: VNDIRECT

Net profit to post 13.4% CAGR in FY20-21F

Domestic revenue growth to accelerate in FY20-21F. We expect Vietnam's dairy consumption to maintain an average steady growth of 8.0% yoy in FY20-21F thanks to solid demand in rural areas. Revenue from the original Vinamilk brand is expected to ride the market trend, growing 8.5% yoy and 9.0% yoy, respectively, in FY20F and FY21F to reach VND59,806bn in FY21F. Besides, the consolidation of GTN will add a revenue of VND3,138bn in FY20F and VND3,565bn in FY21F. Therefore, overall domestic sales are expected to accelerate to 15.2% yoy in FY20F, and a further 9.2% yoy in FY21F, making it the main driver for VNM's total net revenue growth.

Exports to jump in FY20-21F. We expect VNM's exports to post a CAGR of 19.0% over the next two years as the Middle East market continues its recovery, while an official export licence to China will be available in 1H20F. Note that VNM received official export permit to China for condensed milk on 19 Feb 2020.

FY20F revenue and net profit forecast revised up by 3.8% and 2.9%, respectively, following GTNFoods consolidation. We expect GTNFoods to add roughly VND3,183bn and VND3,565bn to VNM's net revenue in FY20D and FY21D. GTNfood's consolidation will

reduce gross margin (GM) slightly in FY20F before improving from FY21F. GTN's GM stood at 15.8% in FY19, far below VNM's rate of 47.2% in the same period. As a result, we expect the consolidation will trim VNM's overall GM slightly to 46.6% in FY20F. However, we expect the company's overall GM to return to the level before the consolidation as the cost restructuring process of GTNfoods is expected to be complete from FY21F.

Figure 2: Our forecasts of VNM's FY2019-21F business results

VNDbn	2019	2020	2021	2022
Net revenue	56,318	64,955	71,492	78,693
% yoy	7.1%	15.3%	10.1%	9.2%
<i>Domestic</i>	6.3%	15.2%	9.2%	9.2%
<i>Export</i>	14.8%	20.0%	18.0%	18.0%
<i>Oversea subsidiaries</i>	8.6%	10.5%	9.9%	9.0%
Gross profit	26,572	30,352	33,682	37,360
Gross margin	47.2%	46.7%	47.1%	47.5%
SG&A	14,390	16,328	17,966	19,770
SG&A as % revenue	25.6%	25.1%	25.1%	25.1%
EBIT	12,182	14,024	15,716	17,590
EBIT margin	21.6%	21.6%	22.0%	22.4%
%yoy	8.7%	15.1%	12.1%	11.9%
Net profit	10,581	12,116	13,599	15,290
Net margin	18.8%	18.7%	19.0%	19.4%
%yoy	3.5%	14.5%	12.2%	12.4%
EPS diluted	5,485	6,261	7,027	7,901
EPS growth	3.6%	14.2%	12.2%	12.3%

Source: VNDIRECT RESEARCH

Valuation

Reiterate ADD with TP of VND155,600. Our 12-month TP is based on an equal weighting of DCF approach (WACC 9.2%, Cost of equity 14.1%, Long-term growth 3.5%) and 24.6x FY20F P/E. VNM is trading at TTM P/E of 19.5x, 20.9% lower than regional peer average and 19.7% below its two-year historical average P/E. Given its TTM ROE of 35.5% vs. the 12.9% regional average, we believe current valuation is compelling for a high-quality stock like VNM.

Re-rating catalysts include 1) stronger-than-expected rise of domestic dairy consumption, and 2) higher-than-expected demand in the Middle East and China. Downside risks include 1) a weaker-than-expected growth of domestic dairy demand, and 2) a higher-than-expected rise of material milk price.

Figure 3: Discounted Cash Flows - Future Cash Flows to Firm (FCFF)

Present value of Future Cash Flows to Firm (VNDbn)	106,173
Present value of Terminal value (VNDbn)	155,791
Enterprise Value (VNDbn)	261,964
Less: Net Debt Plus: Cash + ST investment (VNDbn)	9,626
Equity Value (VNDbn)	271,590
No. of Outstanding Share (m)	1,742
Equity Value Per Share (VND)	155,869
WACC	9.2%
Cost of Equity	4.1%
Long-term growth	3.5%

Source: VNDIRECT RESEARCH

Figure 4: Valuation: Multiples (P/E)

2020F NPAT attribute to common share holder (VNDbn)	10,905
2020F No. of outstanding share (m)	1,742
2020F EPS (VND)	6,261
Milk producers' average P/E (x)	24.6
Implied price 2020	153,327

Source: VNDIRECT RESEARCH

Figure 5: Valuation summary

Methodology	Price	Weight	Weighted price
FCFF	155,869	50%	77,935
P/E	153,987	50%	76,993
Average price			154,928
Target price			155,600

Source: VNDIRECT

Figure 6: Discounted Cash Flow model

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
	1	2	3	4	5	6	7	8	9	10
EBIT	14,024	15,716	17,590	20,370	21,609	22,917	24,297	25,753	27,288	28,906
Add: Depreciation	2,887	3,170	3,476	3,813	4,175	4,561	4,972	5,410	5,878	6,376
Less: Capital expenditure	(2,980)	(2,982)	(3,282)	(3,590)	(3,841)	(4,110)	(4,398)	(4,706)	(5,035)	(5,388)
Changes in Working Capital	(35)	(9)	(82)	729	(94)	195	(118)	664	(94)	(113)
Free Cash Flow (FCF)	13,896	15,895	17,703	21,322	21,849	23,562	24,752	27,121	28,037	29,781
Less: Taxes Paid	(2,654)	(2,958)	(3,322)	(3,849)	(4,097)	(4,321)	(4,582)	(4,859)	(5,153)	(5,461)
Free Cash Flows to Firm	11,242	12,937	14,380	17,473	17,751	19,241	20,170	22,262	22,883	24,320
Terminal Value										279,795
PV of FCFF	10,297	10,853	11,049	12,297	11,442	11,360	10,907	11,026	10,381	10,105
PV of Terminal Value										116,254

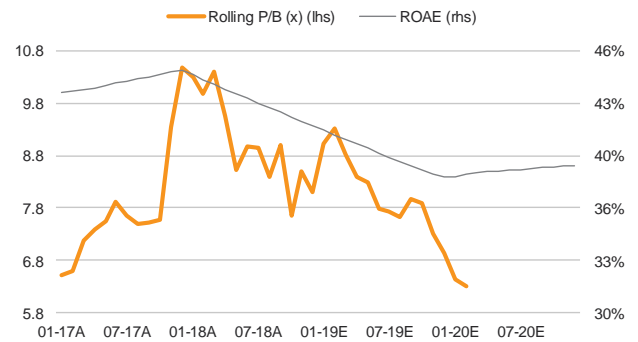
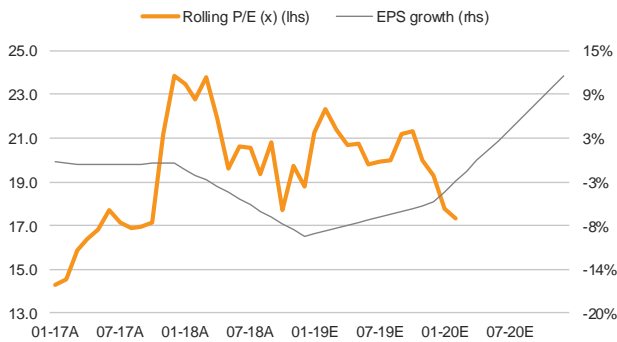
Source: VNDIRECT RESEARCH

Figure 7: Peer comparison (Data as of 17th Feb 2020)

Dairy producer	Bloomberg code	Recom.	Target price (VND)	Market cap (US\$m)	EPS growth (%)		P/E (x)		P/B (x)		ROE (%)		ROA (%)		D/E(x)
					FY19F	FY20F	FY19F	FY20F	FY19F	FY20F	FY19F	FY20F	FY19F	FY20F	
Inner Mongolia Yili	600887 CH	NR	N/a	25.935	19,2%	8,5%	25,7	23,7	7,2	5,4	27,7%	23,2%	14,3%	13,3%	0,2
China Mengniu Dairy	2319 HK	NR	N/a	15.074	32,8%	-4,3%	29,4	23,3	3,9	3,3	14,2%	14,6%	5,2%	6,3%	0,4
Meiji Holdings	2269 JP	NR	N/a	9.860	-12,7%	8,6%	19,6	15,7	1,9	1,8	9,7%	12,2%	5,9%	6,5%	0,2
Yakult Honsha Co	2267 JP	NR	N/a	8.368	15,9%	7,7%	23,7	23,1	2,3	2,2	9,9%	10,1%	5,7%	6,8%	0,3
Bright Dairy	600597 CH	NR	N/a	1.971	20,0%	12,0%	35,4	26,5	2,5	2,3	7,2%	9,1%	2,2%	3,9%	0,7
Morinaga Milk Industries	2264 JP	NR	N/a	1.931	18,9%	41,9%	13,8	10,5	1,2	1,1	8,8%	11,2%	3,4%	5,3%	0,6
Average				10.523	15,7%	12,4%	24,6	20,5	3,2	2,7	12,9%	13,4%	6,1%	7,0%	0,4
Median				9.114	19,1%	8,5%	24,7	23,2	2,4	2,3	9,8%	11,7%	5,5%	6,4%	0,4
Vietnam Dairy Products	VNM VN	ADD	155.600	7.985	3,6%	14,2%	19,5	24,8	6,8	8,7	35,5%	38,9%	25,8%	24,7%	0,2

Source: VNDIRECT RESEARCH, Bloomberg

Valuation



Income statement

(VNDbn)	12-19A	12-20E	12-21E
Net revenue	56,318	64,955	71,492
Cost of sales	(29,746)	(34,603)	(37,810)
Gen & admin expenses	(1,396)	(1,709)	(1,883)
Selling expenses	(12,993)	(14,619)	(16,083)
Operating profit	12,182	14,024	15,716
Operating EBITDA	10,234	11,137	12,547
Depreciation and amortisation	1,948	2,887	3,170
Operating EBIT	12,182	14,024	15,716
Interest income	807	928	855
Financial expense	(187)	(232)	(162)
Net other income	(1)	(2)	(2)
Income from associates & JVs	(6)	25	27
Pre-tax profit	12,796	14,744	16,434
Tax expense	(2,241)	(2,654)	(2,958)
Minority interest	(27)	(26)	(29)
Net profit	10,527	12,064	13,448
Adj. net profit to ordinary	10,527	12,064	13,448
Ordinary dividends	(7,838)	(7,838)	(7,838)
Retained earnings	2,690	4,227	5,610

Balance sheet

(VNDbn)	12-19A	12-20E	12-21E
Cash and equivalents	2,665	5,996	9,896
Short term investments	12,436	8,769	10,009
Accounts receivables	4,442	5,711	6,286
Inventories	4,983	6,616	7,175
Other current assets	134	245	269
Total current assets	24,660	27,337	33,634
Fixed assets	15,837	14,715	14,435
Total investments	1,100	897	1,196
Other long-term assets	3,133	3,177	3,028
Total assets	44,731	46,127	52,293
Short-term debt	5,351	1,372	1,504
Accounts payable	3,648	4,208	4,631
Other current liabilities	5,443	7,751	8,452
Total current liabilities	14,443	13,331	14,588
Total long-term debt	123	91	29
Other liabilities	434	1,484	846
Share capital	17,417	17,417	17,417
Retained earnings reserve	7,875	10,896	15,161
Shareholders' equity	29,240	30,730	36,340
Minority interest	491	490	490
Total liabilities & equity	44,731	46,127	52,293

Cash flow statement

(VNDbn)	12-19A	12-20E	12-21E
Pretax profit	12,796	14,838	16,677
Depreciation & amortisation	2,016	3,182	3,629
Tax paid	(2,034)	(2,671)	(3,002)
Other adjustments	(556)	(757)	(879)
Change in working capital	(808)	(15)	23
Cash flow from operations	11,414	14,578	16,448
Capex	(2,158)	(4,280)	(4,054)
Proceeds from assets sales	114	59	74
Others	(5,370)	(352)	(1,606)
Other non-current assets changes	666	(268)	(98)
Cash flow from investing activities	(6,748)	(4,841)	(5,684)
New share issuance	128	0	0
Shares buyback	(1)	1	0
Net borrowings	4,194	(1,424)	(2,518)
Other financing cash flow	(8)	0	0
Dividends paid	(7,836)	(7,838)	(7,838)
Cash flow from financing activities	(3,524)	(9,260)	(10,355)
Cash and equivalents at beginning of period	1,523	2,665	3,142
Total cash generated	1,143	477	409
Cash and equivalents at the end of period	2,665	3,142	3,551

Key ratios

	12-19A	12-20E	12-21E
Dupont			
Net profit margin	18.7%	18.6%	18.8%
Asset turnover	1.37	1.43	1.45
ROAA	25.6%	26.6%	27.3%
Avg assets/avg equity	1.49	1.52	1.47
ROAE	38.3%	40.2%	40.1%
Efficiency			
Days account receivable	22.5	23.5	23.5
Days inventory	61.1	70.0	69.3
Days creditor	44.8	44.5	44.7
Fixed asset turnover	3.75	4.25	4.91
ROIC	29.9%	36.9%	35.1%
Liquidity			
Current ratio	1.7	2.1	2.3
Quick ratio	1.4	1.6	1.8
Cash ratio	1.0	1.1	1.4
Cash cycle	38.9	49.0	48.0
Growth rate (yoy)			
Revenue growth	7.1%	15.3%	10.1%
Operating profit growth	8.7%	15.1%	12.1%
Net profit growth	3.4%	14.6%	11.5%
FD EPS growth	3.4%	14.6%	11.5%

Source: VND RESEARCH

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RECOMMENDATION FRAMEWORK

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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