2019

Navigating Vietnam

Time to double down on quality

VNDIRECT WISDOM TO SUCCESS IN ALLIANCE WITH CGSCIMB

January 2019

STRATEGIST'S NOTE

In our **2018 strategy report** published at the start of last year, we highlighted the fact that Vietnam's 2017 stock market performance would be a tough act to follow. We expected the market to peak shortly after breaching the 1,100 point high-water mark largely due to a whole host of global factors which we categorized into the "predictable" (US Federal Reserve rate hikes) and the "black swans" (largely unknown, by definition, although we alluded to US-North Korea tensions and a hard landing in China's economy). Nonetheless, we reiterated our confidence in Vietnam's macro economy and consequent strength in corporate earnings. We saw continued strength in cyclical names with overweight ratings on the banking sector and flagged the textiles and fishery sectors based on their strong export prospects and the automotive sector for its recovery from a policy-induced trough in 2017. Finally, we alerted investors to the growing divergence between mid-cap and large cap valuations which we thought was unsustainable.

Fast-forward a year and we were right to be cautiously optimistic. The VN-Index peaked at 1,200 points, the Fed rate hikes triggered an era of equity market volatility and more than a handful of black swan risks surfaced including the US-China trade tensions and a disorderly Brexit. Meanwhile, Vietnam's economy continued to power on to register a decade-long high of 7.08% while corporate earnings across the listed universe are likely to have surged by around 25% in 2018, on a market capitalization-weighted basis. Banking and property led the pack in terms of stock price performance but the way investors dumped construction and materials stocks caught us by surprise given their cyclical nature. Meanwhile, our views on the textile, fishery and automotive sectors proved accurate. Finally, mid-cap and large cap valuations did converge again driven more by a large cap de-rating than by a mid-cap re-rating.

For 2019, the picture remains nuanced. We see growing headwinds for the global economy and lurking "black swan" risks. But the sharp correction in Vietnam's stock market has rendered valuations rather appealing in light of continued strong earnings growth. We also see a marked shift away from momentum-driven investing and into a focus on both growth and value. However, in an environment of heightened global uncertainty and an ageing economic upcycle and equity bull market, we believe a sharp re-rating of Vietnam's stock market is rather unlikely. Corporate earnings will decelerate this year from a high base last year but remain firmly in double-digit territory and this should carry the VN Index back towards the 1000 point psychological level. For all the bullishness out there on emerging markets, we rule out a miraculous resurrection of the bull market. However, value abounds and there has been no better time to double down on solid long-term bets on Vietnam's fantastic growth story.

Happy Investing!

Sincerely,

Anirban Lahiri

Head of Institutional Business & Head of Research

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EXECUTIVE SUMMARY

Vietnam's GDP acceleration and currency stability in 2018 made it a standout in a maturing global economic cycle. GDP grew by 7.08% last year on the back of a 13.0% expansion in industrial production, a 7.2% increase in consumption and a 13.0% surge in exports. Inflation remained contained despite estimated credit growth of 14.0% while the Dong depreciated by 2.2% versus the US$ in 2018, making it one of the most stable currencies in the region, facilitated by a trade surplus of US$7.0 billion and an estimated current account balance of US$7.1 billion at year end. This was against a backdrop of a sharp decline in frontier and EM currencies against the US$ and flat-lining global GDP growth of 3.7% in 2018.

US-China trade tensions and a slew of trade pacts have put Vietnam firmly on the global sourcing map. Vietnam has become the most favored offshored manufacturing and sourcing destination and the lynchpin of an ongoing "China plus one" sourcing diversification strategy for global branded goods producers, contract manufacturers and retailers. Vietnam's political stability, business-friendly policy regime, long coastline along one of the world's busiest shipping lanes and proximity to China's export manufacturing heartland make it an obvious winner from China's growing economic and trade isolation. This is reflected in the 9.1% surge in disbursed FDI in 2018 and crystallized by the 12.2% rise in total trade turnover in the year, driven by Vietnam's growing integration.

A slowing global economy, trade headwinds and a more hawkish monetary policy imply that Vietnam's GDP growth will decelerate to 6.6% this year. Vietnam will still be a standout economy, in our opinion. Emerging cluster effects in the export manufacturing sector are finally starting to materialize as evinced in Foxconn's ongoing discussions to build a handset manufacturing facility in Vietnam as well as the recent surge in textile and apparel export order books. We expect sustained strength in FDI inflows and low double digit export growth to support the current account and the currency, helping to cushion the impact of an orchestrated moderation in credit growth to touch 14-15% which will weigh on both consumption and domestic private sector investment. We expect a gentle 2.0% devaluation in the Dong this year, barring severe external shocks.

External risks are lurking in the shadows. A protracted US-China trade spat, a disorderly Brexit and a continued US government shutdown, combined with record high corporate debt levels in the US and the fading impact of fiscal stimulus, make the global economy fragile. Vietnam's growing trade integration makes it vulnerable to global demand shocks that might result from the above factors. A 1.2% fall in registered FDI into Vietnam in 2018 is testimony to the fact that trade tensions and policy uncertainty are already impacting the global capex cycle.

We expect the VN-Index to end the year at around 990 points, up 11% from 2018 year-end levels. We expect continued risk aversion to weigh on equity markets, globally. Vietnam's stock market correction in 2018 after a heady 2017 rally has catalyzed an ongoing transition from a momentum-driven investing strategy to a growth and value-based investing strategy. With the market trailing P/E having contracted to 15.5x, down from 21.9x at the 2018 peak and estimated 2018 market-cap weighted earnings growth of 25%, skittish foreign investors are likely to re-enter the market in force, albeit selectively. The market is currently trading at a forward P/E of just 13.3x based on 2019F earnings growth of 16.4%, per consensus forecasts implying a 44.9% PEG discount to the emerging and frontier market peer average. The VN-Index could breach the 1,000 point level, intra-year, if a US-China trade deal and Chinese fiscal stimulus materialize but the sentiment boost is likely to be transitory.

An upgrade to emerging market status is still two years away but a new securities law in the pipeline is likely to boost the perceived likelihood of MSCI EM inclusion. A new securities law, currently under legislation, is likely to shorten trade settlement times and improve information disclosure which will boost Vietnam's chances of an MSCI upgrade. This could trigger "front-running" in anticipation of an EM upgrade and constitutes upside to our base case index forecast.

We like earnings-driven stories for 2019 and advocate a shift away from cyclical names into more defensive stocks in the consumer and consumer-related, automotive and power sectors. Given intensifying competition in the consumer and retail space, we favor market or category leaders such as PNJ, MWG and QNS. We anticipate the nascent recovery in the automotive sector to gather steam and place VEA on our watch list. The leading parcel delivery company, VTP, provides broad exposure to the e-commerce and organized retail revolution. Within the cyclical space, we only like select banking and property names with good structural growth stories; among banks, we like MBB (for its growing retail lending exposure), VCB and ACB (for their leading deposit franchises, sound asset quality and healthy capital buffers). In the property sector we like NLG and also place VHM on our watch list due to their solid project pipelines, big pre-sales backlog and focus on real end-user demand. Finally, we think leading contractor CTD could benefit from strong industrial and non-residential construction growth and a huge

project pipeline stemming from Vincity affordable condo developments. PC1 and POW provide broad exposure to the power sector demand growth and liberalization stories.

We like textile and fishery exporters and industrial park developers as they are likely to be direct beneficiaries of US-China trade tensions and a slew of new trade pacts including the recently-implemented CPTPP. KBC and LHG are notable names in the industrial park space while STK, TCM and MSH are likely textile sector beneficiaries. In the fishery sector, VHC is well poised to capitalize on its giant scale and leadership in exporting to the US market while Chinese appetite for pangasius picks up, supported by trade tensions.

The Oil and Gas sector could see a sentiment makeover from a possible recovery in oil prices. We think oil prices have likely bottomed as OPEC supply cuts offset concerns of future demand weakness and given that China looks to be capitalizing on low prices to build up its strategic reserves. Energy security vulnerabilities could lead to an acceleration in exploration activity but territorial disputes cast a long shadow. We like downstream player PVT which will benefit from Vietnam's aggressive build-out in domestic refining capacity.

Anirban Lahiri – Head of Research

VIETNAM ECONOMY: POWERING AHEAD THROUGH BUILDING HEADWINDS

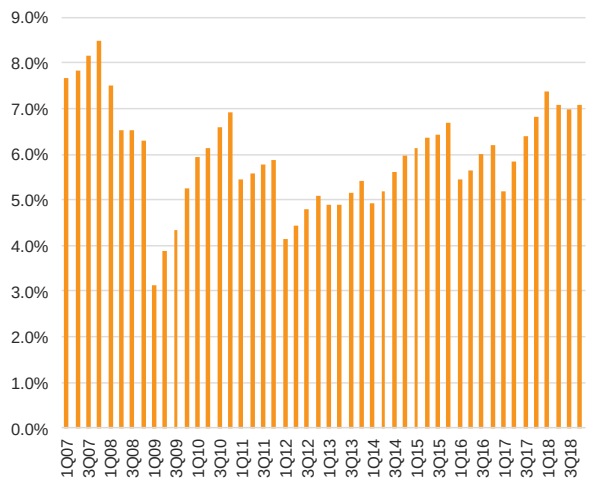
In this section, we present an overview of Vietnam's economic performance in 2018 and standing at the start of 2019. We go on to lay out our expectations for growth and inflation in the year ahead.

2018 REVIEW: ROBUST GROWTH AND MODERATE INFLATION

High and broad-based economic growth

Vietnam's economy grew 7.1% in 2018, the fastest pace in eleven years, surpassing both consensus forecasts and the government's target. Broad-based growth was attributed to 1) improving agriculture production (+3.8% yoy vs. 2.9% in 2017); 2) strong manufacturing expansion (+13.0% vs. 14.4% in 2017) despite increased global trade protectionism; 3) continued growth in the construction sector (9.2% vs. 8.7% in 2017); and 4) robust consumer spending (wholesale and retail sales rose 8.5% vs. 8.4% in 2017) thanks to sequential improvements in incomes coinciding with fairly benign inflation. Only the mining sector made a negative contribution to output growth (-3.1% yoy), led by continued declines in oil and gas production, but the contraction was milder than the 7.1% drop seen in 2017.

Figure 1: 2018 GDP growth marked an eleven year-high



Source: VNDIRECT, GSO

Figure 2: GDP growth was high broad-based (YTD as at end of each quarter)

ytd growth (%)	1Q18	2Q18	3Q18	4Q18
Real GDP	**7.38**	**7.08**	**6.98**	**7.08**
Agriculture	4.06	3.93	3.65	3.76
Mining	3.66	(0.14)	(1.97)	(3.11)
Manufacturing	12.82	12.39	12.65	12.98
Construction	5.54	7.42	8.46	9.16
Wholesale & Retail Sales	8.93	8.94	8.48	8.51
Transportation & Storage	7.28	7.59	7.55	7.85
Accomodation & Food	6.89	6.98	5.89	6.78
Financial services	7.17	7.58	7.85	8.21

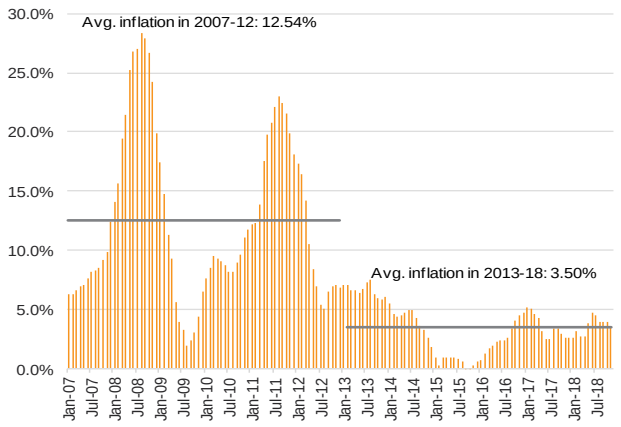
Source: VNDIRECT, GSO

Inflation dynamics changed but overall inflation rate remained contained due to government intervention

In 2018, the annual average CPI was 3.5% and core CPI was 1.5%, both of which were lower than our expectations and at around the same levels seen in the same period in 2017. The main difference versus last year was the higher contribution of food and fuel inflation in headline CPI, while in 2017, about half of the growth in inflation was due to the upward adjustment in prices of public services & goods. While there were concerns about an increase in food and fuel prices during 2018, these were allayed by the government's ability to cushion the rise in global prices of these commodities. Through draw-downs

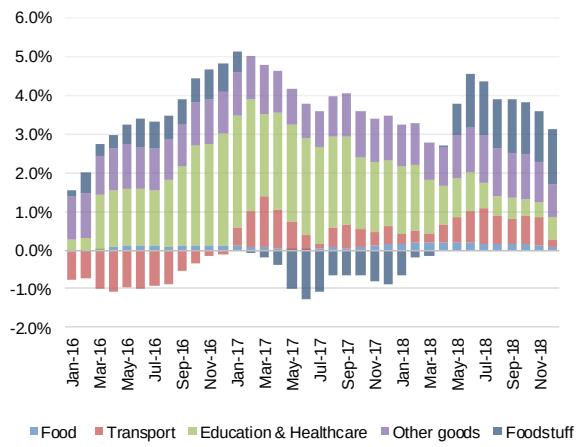
from the petrol price stabilisation fund and postponement of both power tariffs and environmental tax hikes, the government was able to keep the inflation rate under 4.0% in 2018. The government's efforts were also helped along by the sharp reversal in crude oil prices in the fourth quarter of 2018.

Figure 3: Inflation is hovering around the trailing five-year average level



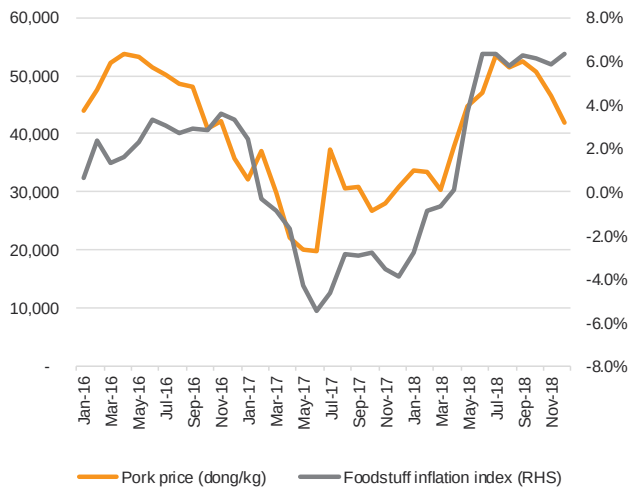
Source: VNDIRECT, GSO

Figure 4: Food and transport inflation contributed the most to 2018 headline CPI



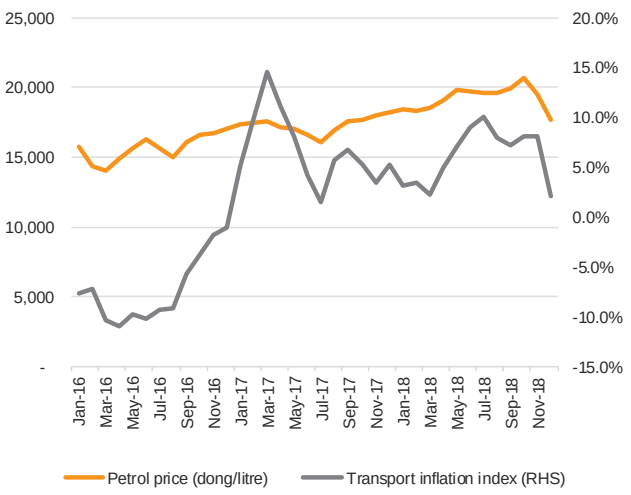
Source: VNDIRECT, GSO

Figure 5: Foodstuff inflation index vs. pork price



Source: VNDIRECT, GSO

Figure 6: Transport inflation index vs. petrol price



Source: VNDIRECT. GSO, MoIT

2019 OUTLOOK: VIETNAM'S GROWTH TO MODERATE

Global macro outlook: A synchronised slowdown is looming

Looking back over the past two years, the global economy has transitioned from robust and accelerating growth fuelled largely by low interest rates in 2017 to moderating growth and tighter liquidity in 2018. The US economy is expected to see a meaningful slowdown as the impact of fiscal stimulus fades away and developing economies will face more challenges due to uncertainty related to the US-China trade war. The Euro area and the UK have seen downward revisions in their economic prospects in 2019 with large Euro zone exporters like Germany seeing an economic contraction in the fourth quarter due to weakening demand in emerging economies and fears of a disorderly Brexit weighing on both European and UK investor sentiment.

Growth in developing countries is expected to slow, led by China, as the lagged effects of deleveraging and trade tensions weigh on consumption and business confidence. However, we think more policy easing could support China's private sector and infrastructure development, putting it on a gentle glideslope down to a lower trend rate of growth rather than precipitating a hard landing.

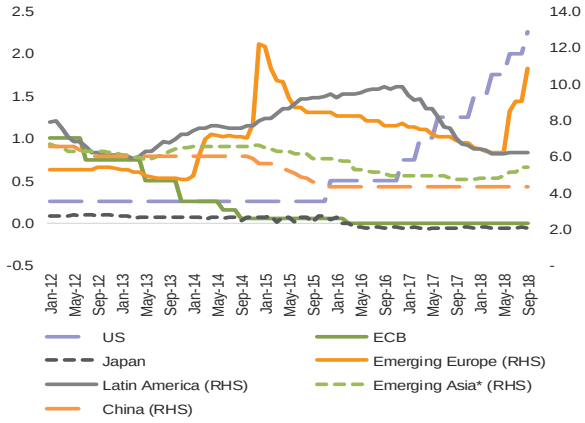
Figure 7: Expected slowdown in global growth in 2019-20F

Real GDP growth	2016	2017	2018F	2019F	2020F
US	1.6	2.2	2.9	2.6	1.9
Japan	1.0	1.7	1.0	1.0	0.4
Eurozone	1.9	2.4	1.9	1.6	1.5
Germany	2.2	2.2	1.7	1.6	1.5
France	1.1	2.2	1.6	1.6	1.5
Italy	1.1	1.6	1.0	0.9	0.9
Spain	3.2	3.0	2.5	2.2	1.9
UK	1.8	1.7	1.3	1.5	1.6
China	6.7	6.9	6.6	6.2	6.0
India**	8.2	7.1	7.5	7.3	7.5
Russia	(0.2)	1.5	1.7	1.5	1.7
Brazil	(3.3)	1.1	1.3	2.4	2.5
Developed markets	1.8	2.4	2.4	2.1	1.7
Emerging markets	4.5	5.1	5.1	4.9	5.1
World	3.3	3.7	3.7	3.6	3.3

Source: VNDIRECT, BLOOMBERG

** Bloomberg consensus fiscal year basis

Figure 8: Policy rates have generally increased across emerging markets since mid-2018



Source: VNDIRECT, IMF

The sharp increase for emerging Europe reflects the policy rate hikes in Turkey. Emerging Asia* excludes China.

Financial conditions have tightened in 2018 with rising interest rates, particularly in the US, triggering significant turbulence in emerging markets and reflected in currency depreciation against the US$ in many emerging countries, especially those with large and rising external imbalances or sizable foreign currency-denominated debt. The combination of weaker growth and the higher current rate environment will cloud prospects for emerging markets in 2019. However, with currencies having already devalued sharply across many emerging economies in 2018 and the recent dovish turn in the US Federal Reserve rate hike outlook, we expect the pressure on emerging market financial conditions from Fed tightening to ease during the course of the year. A temporary trade deal between the US and China presents additional upside to this base case view and could lead to a mild reacceleration of growth in the emerging world.

Vietnam macro outlook: Slightly Slower but Balanced Growth and Muted Inflation

Economic growth to ease in 2019 but stay high led by a strong expansion in industrial production and robust consumption

We expect growth to ease in 2019 after a strong performance in 2017-18. Our 2019 real GDP growth forecast is 6.6%, in line with consensus and near the low-end of the government's 6.6-6.8% target range for 2019. In our view, domestic demand is still a strong component of the growth equation with double-digit growth in retail and tourism industries and this should provide some buffer against uncertain global economic conditions.

A robust expansion in the manufacturing base is likely to continue for the following reasons: 1) In the previous three years, private investment grew at a stellar average rate of 15.0% per annum; we expect this new wave of investments to increase the productive capacity of the economy; 2) The imminent launch of foldable smartphones over 2019-2020 by leading smartphone makers and adoption of the 5G wireless network is expected to trigger a new upcycle in the smartphone industry and lift currently flagging demand. These significant technology breakthroughs in the smartphone industry developments have boosted registered FDI from Samsung and LG into Vietnam in 2017-18, which could support the growth of the FDI sector from 2019 onwards; 3) We believe that continued strong FDI inflows amid the US-China trade war could create opportunities for a further expansion of Vietnam's manufacturing base as regional supply chains are reconfigured to reduce dependence on China as a sourcing hub; this could be helped along by a slew of newly signed bilateral FTAs and the CPTPP trade pact.

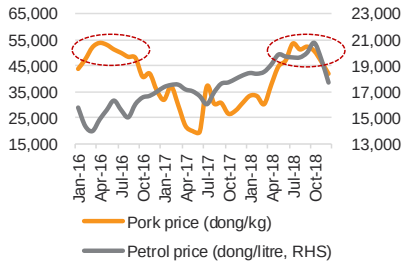
In 2019, we expect the government to focus more on the private sector and adopt a cautious monetary and fiscal policy in order to avoid undoing recent efforts at improving macro stability and cleaning up the banking system.

Figure 9: Macro forecasts

		2017	2018E	2019F	2019P
Real GDP growth	%yoy	6.8	7.1	6.6	6.8
Agriculture	%yoy	2.9	3.8	3.3	3.0
Mining	%yoy	-7.1	-3.1	-2.0	-4.4
Manufacturing	%yoy	14.4	13.0	10.2	12.1
Construction	%yoy	8.7	9.2	8.5	9.2
Wholesale & Retail Sales	%yoy	8.4	8.5	8.5	na
Exports	%yoy	21.6	13.0	12.0	8-10
Imports	%yoy	21.4	11.3	13.6	10.1
CPI (period average)	%yoy	3.5	3.5	3.9	< 4
Policy rate (period end)	%	6.3	6.3	6.3	na
Current account balance	% of GDP	2.7	3.0	2.5	na
Fiscal balance	% of GDP	-3.5	-3.0	-3.6	-3.6

Source: VNDIRECT | F: our forecast, P: government's plan

Figure 10: Food and fuel prices peaked in late 2018



Source: VNDIRECT, PLX

Inflation is expected to remain muted

In 2018, thanks to the government's consistent efforts to keep inflation under control and only a short-lived surge in oil prices in late-2018, there was only a slight pickup in inflation. Although we take into account the upward pressure from factors such as administered service price hikes (electricity, healthcare and education) and an increase in environmental tax on fuels, we think the continued near-term weakness in oil prices could render inflation manageable in 2019. Our base case assumes Brent oil prices will average around US$60-70/bbl in 2019, a level which does not portend a sharp rise in energy and transportation costs for Vietnam. Our forecast for 2019 headline inflation is 3.9%, slightly lower than Bloomberg's consensus of 4.0%. Risks to our base case include 1) a sharper-than-expected recovery in oil prices; and 2) a sharp depreciation of the dong, triggered by external risks.

Figure 11: What has driven inflation over the past five years?

	Headline CPI	Core CPI	Food prices	Fuel prices	Administered prices	Monetary policy
2013	6.6%	7.0%	↑	↑	↑	
2014	4.1%	1.9%		↓		
2015	0.6%	1.7%		↓		
2016	2.7%	1.9%			↑	↑*
2017	3.5%	1.3%			↑	
2018E	3.7%	1.5%	↑	↑		

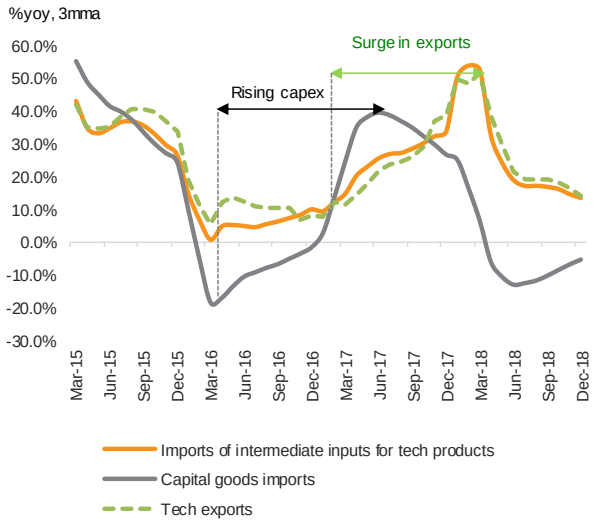
Source: VNDIRECT

* import-led inflation from the dong depreciation in 2015 only led to a marginal increase in 2016 headline CPI as commodity prices were favourable at that time.

Exports to moderate in line with a weakening in global demand

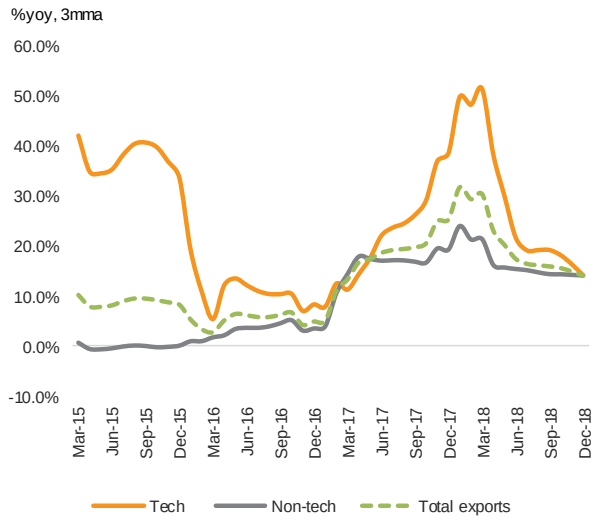
Despite escalating trade tensions, Vietnam's export growth remained strong in 2018 (+13.0% yoy). However, there was a slowdown from the 21.6% growth rate seen in 2017, largely due to a slowdown in tech exports. We note Vietnam's capital goods imports, which is highly correlated with the electronics export cycle, declined 3.2% yoy in 2018 (vs. a 21.0% increase in 2017). We think fixed capex momentum is likely to recover in 2019, helped in no small part by the relocation of export-oriented manufacturing capacity out of China, but there will be a lagged effect on export growth. Looking forward, we see more downside risks to export growth including lingering trade war tensions and a slowdown in global demand. Therefore, we expect export momentum to continue moderating somewhat into 2019. However, due to the strong relationship between exports and imports (Vietnam is a downstream player in key export categories such as electronics and machinery and therefore relies on imported components), we think the country could continue to maintain a trade surplus in 2019 (US$4.2bn vs. US$7.0bn in 2018). We also expect a current account surplus in 2019 (2.5% of GDP vs. an estimated 3.0% for 2018).

Figure 12: Fixed asset investment showing signs of a cyclical recovery from a trough seen in 2Q18



Source: VNDIRECT, CUSTOMS

Figure 13: Recent exports growth moderation was led by the tech segment



Source: VNDIRECT, CUSTOMS

Currency outlook: moderate depreciation envisioned in our base case assumption

We expect a moderate depreciation of the dong in 2019 (2.0% vs. 2.2% in 2018) as we believe that the value of the dong is ultimately driven by economic performance although there are many other factors that could affect the short-term supply-demand balance of the currency. Recall that during a tightening of global liquidity conditions in 2017-18, Vietnam, with its high export orientation and current account surplus, was relatively better placed than countries with low export orientation and current account deficits, such as India and Indonesia. In addition, we think Vietnamese exporters still have tariff advantages compared to Chinese exporters despite a sharp depreciation of the CNY driven by slowing growth and capital flight from China which have partially offset the disadvantage created by US tariffs.

In 2019, we estimate a narrowing in Vietnam's current account surplus to 2.5% of GDP from 3.0% in 2018 because of moderating export momentum. However, we also expect external funding pressures to ease largely due to a more dovish US Fed and this may help alleviate depreciation pressure on the dong. The government has also undertaken measures to control inflation and does not intend to devalue the dong in order to stimulate exports. Against this backdrop, we do not foresee a large-scale depreciation of the dong in 2019 under our base case scenario.

Figure 14: Factors that could impact the dong in 2019

Factors	Our rationale	Potential impact	Degree of impact
Domestic fundamentals	- We expect a current account surplus to be maintained in 2019 despite slower export growth. - Economic growth is expected to remain resilient with inflation under control. These factors could support the dong, in our view.	Positive	High
Global tightening of monetary conditions	- In the Dec 2018 meeting, the Fed lowered its rate projections to two hikes in 2019, signaling that US monetary policy may become less hawkish. Consequently, the US$ may weaken when the Fed decides to pause its tightening cycle.	Negative	Medium/Low
US-China trade war tensions	- We think the CNY has already devalued significantly in 2018 due to pressures from anticipated slowing growth, higher US tariffs on Chinese exports and capital flight from China, leaving less room for a further correction in 2019. - An escalation into a full-blown US-China trade war is not our base case assumption and we do not anticipate the Chinese authorities cutting policy rates aggressively and, hence, a further pronounced depreciation of the CNY looks unlikely implying that there will be less pressure on Vietnam to make competitive devaluations.	Negative	Medium
SBV's policy	- A new circular on foreign currency lending allows banks to extend USD-denominated loans to some borrowers in 2019. There could be a surge in US$ demand to meet the SBV's deadline for FX loans payment. However, we think the SBV may manage to control the exchange rate's volatility during this period.	Negative	Medium
	- The Vice Minister recently stressed that "the government has no intention to devalue the dong in order to stimulate exports" despite the fact that the dong appreciated by 3-4% against other Asian currencies in 2018.	Positive	Medium

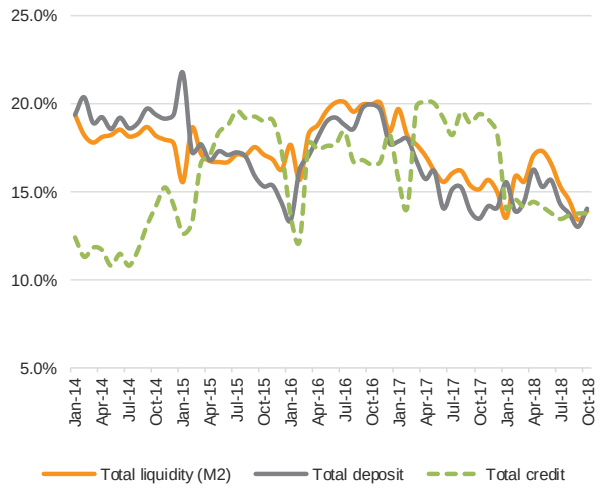
Source: VNDIRECT

Credit growth to continue moderating

In 2018, monetary policy remained accommodative, but credit conditions tightened in 2H2018. The SBV has strictly monitored the banking sector's credit growth target without exceptions and controlled lending to high-risk sectors (real estate and consumer finance). In addition, liquidity in the banking sector tightened markedly in the second half of the year with rising interbank rates given slower deposit growth and fierce competition for deposit mobilization. Amid tighter financing conditions, credit growth is estimated at 14.0% in 2019 vs. 18.2% in 2017, according to the SBV. We also expect credit growth to continue moderating into 2019, but expected the slowdown to be marginal as Vietnam remains a credit-fuelled economy and inflation seems to be contained for now.

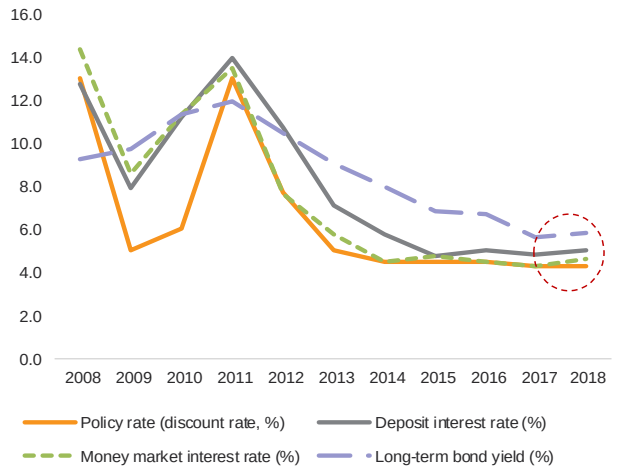
In terms of the domestic interest-rate trajectory, we expect the government's monetary policy stance to remain unchanged and we now expect policy rates to stay on hold at 4.25% and 6.25% (discount rate and refinancing rate respectively), versus earlier expectations of a 25-50bp hike. Indeed, the absence of inflationary pressures thanks to recent falling oil prices lead us to temper our policy rate hike expectations. However, we note that fund mobilisation interest rates increased slightly in 4Q18 in the banking system. This will result in higher borrowing costs, especially for high-risk sectors such as commercial real estate and consumer finance even if policy rates do not move up. For now, we think the divergence between market rates and policy rates is insignificant. We also believe the government and SBV would like to keep lending rates stable in order to support the domestic private sector and economic growth. Thus, we think a policy rate hike is not likely as long as inflation stays under control.

Figure 15: Credit conditions tightened in 2H2018



Source: VNDIRECT, SBV

Figure 16: A slight uptick in market interest rates in 2018 despite an unchanged policy rate



Source: VNDIRECT, EIU
Long-term bond yield: 10-year government bond yield

Figure 17: Vietnam's monetary policy cycle lags that of the broader region

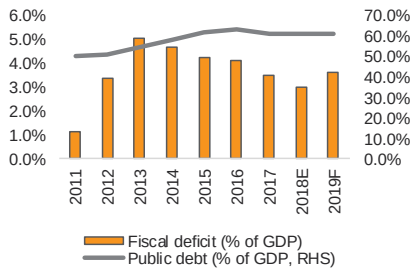
	Rate increase in 2018 (% bps)	Current policy rate (%)	Headline CPI (%)	Real interest rate (%)
China	-	4.35	2.20	2.15
Taiwan	-	1.38	0.31	1.07
Vietnam	-	4.25	3.46	0.79
Malaysia	0.25	3.25	0.20	3.05
South Korea	0.25	1.75	2.00	(0.25)
Thailand	0.25	1.75	0.94	0.81
India	0.50	6.50	2.33	4.17
Hongkong	0.61	2.25	2.60	(0.35)
Indonesia	1.75	6.00	3.23	2.77
Philippines	1.75	4.75	6.00	(1.25)

Source: VNDIRECT, BLOOMBERG

2018 was a turbulent year for many emerging market economies coping with heightened trade tensions, external financing constraints, capital outflows and currency depreciation. In Asia, the worst hit were countries running 'twin deficits' like India, Indonesia and Philippines, leading policymakers from these countries to shore up policy buffers with varying degrees of policy responses. Compared to other countries in Asia,

Vietnam is a lagging player in the global interest rate hike cycle and, given the strong growth momentum in the economy, we expect that monetary policy will be guided by the need to maintain the stability of the dong amid lingering external uncertainties. There the risks to our policy rate base case assumptions for 2019 are tilted to the upside.

Figure 18: Fiscal deficit has gradually shrunk thanks to fiscal consolidation

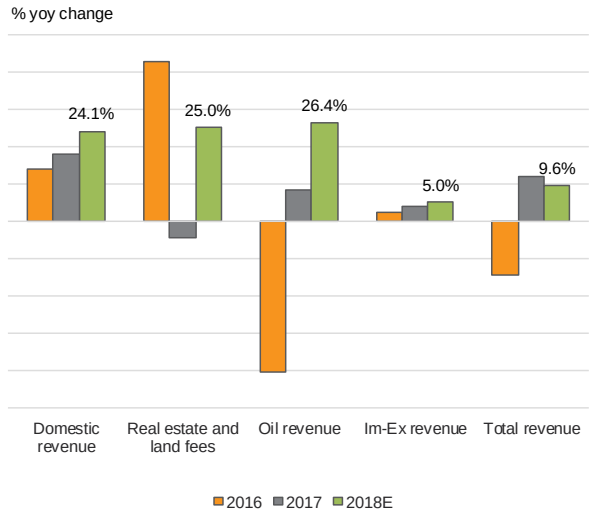


Source: VNDIRECT, GSO

We expect a cautious fiscal policy in the next two years

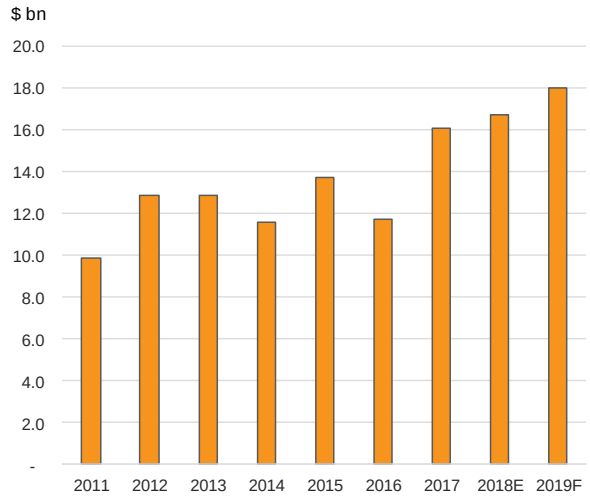
Based on preliminary data through Dec 2018, we estimate a budget deficit of about 3.0% of GDP in 2018, down from 3.5% in 2017. In 2018, improving revenue from the private sector and continued subdued public investment helped to contain public debt accumulation and ensured compliance with the debt limit of 65.0% of GDP. During the first 11 months of 2018, public investment spending only increased 6.7% yoy and reached 60.0% of the annual target. In our view, the continued contraction in public investment could undermine long-term economic growth and create more liabilities for the public sector. Given a narrowing of the budget deficit in the past two years we see room for cautious fiscal easing in 2019-20. We see the fiscal deficit widening from 3.0% of GDP in 2018 to 3.6% of GDP in 2019 (in line with the planned target of 3.6% of GDP).

Figure 19: Improving collection measures for domestic taxes and fees supported state budget revenue in 2018



Source: VNDIRECT, GSO

Figure 20: Public investment is expected to rise in 2019

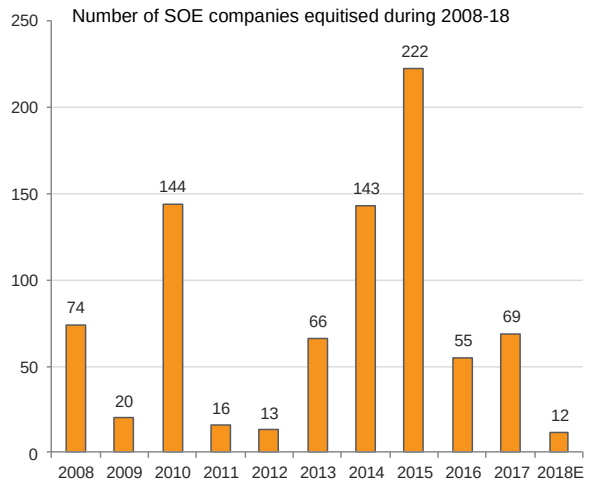


Source: VNDIRECT, GSO

SOE reform setbacks amid a national corruption crackdown

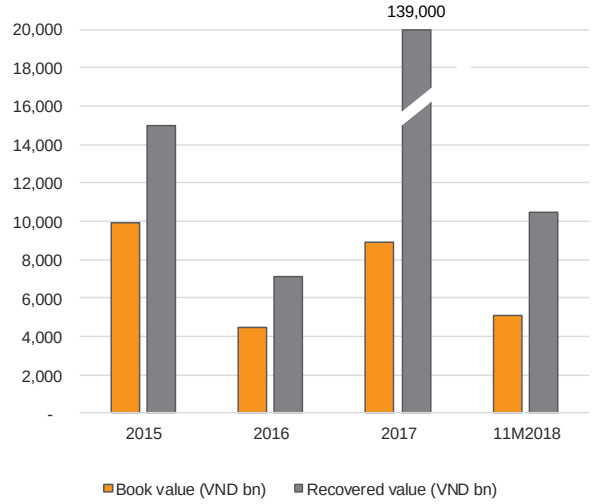
In 2018, the government did not meet its targets for SOE equitisation. Only 12 companies had completed the process as at the end of Nov 2018 versus a target of 85 companies planned for 2018. The divestment process was also sluggish with only 31 companies completing divestment versus the goal of 181 companies. Adding to challenges for SOE reforms such as complex ownership, and unclear financial and debt obligations, the valuation of land use rights became a prominent issue in the progress of SOE reforms in 2018. According to the Ministry of Finance, HCMC and Hanoi were expected to equitise 50 enterprises in 2018, but not a single firm from either city has been equitised until now. A greater scrutiny of state-owned land transferred to private companies has also created headwinds for the property market in Vietnam's big cities. With the ongoing anti-corruption campaign in the country, we expect IPO and divestment activities to slow in the near term. A slowdown in reforming the SOE sector could be a huge constraint for promoting the development of the domestic private sector, which we believe is a pivotal driver of economic growth going forward.

Figure 21: The SOE equitisation programme lost steam under stricter regulations and an ongoing corruption crackdown



Source: VNDIRECT, MOF

Figure 22: Collections from SOE divestments dropped after the large divestment of Vietnam's top brewer, Sabeco



Source: VNDIRECT, MOF

Risks tilted to the downside

In our view, the risks to Vietnam's economic outlook are titled to the downside, mainly stemming from external factors. The key global swing factors will be renewed strength in the US$ and a continuation along the rate hike trajectory, possible capital flight from risk assets due to rising global risk aversion and a full-blown escalation of the US-China trade war in our bear case. On the domestic front, overtly conservative fiscal policy and continued sluggishness in SOE reform could threaten longer-term productivity growth and the structural foundations of the economy. In addition, domestic credit conditions are key to watch. Delays in a continued tightening of monetary policy could lead to a build-up in inflationary pressures and consequently downside risks to growth, further down the road.

We see three key themes shaping the macro outlook in 2019:

Theme #1: Could US-China trade tensions benefit Vietnam? We think so, barring a further escalation of trade tensions.

Despite an escalation in US-China trade tensions during 2018, full-scale trade tensions have been scaled back since the last G20 summit. In the beginning of this year, the US President said there was progress towards a trade deal between the US and China, but denied considering lifting tariffs on Chinese imports. Therefore, we still expect a 30-40% chance of an escalation in the US tariff regime on US$200bn of Chinese goods from the existing 10% rate to 25% starting in Mar 2019 but we believe that the chances of an extension of the tariff universe to cover all Chinese goods exports to the US are rather low now given the cracks that are appearing in the global economy. In addition, we believe the US-China trade tensions are symptomatic of a protracted struggle between the incumbent superpower and an aspiring superpower rather than just a balance of trade issue. We therefore believe that concerns over a resurfacing of US-China trade tensions will linger through 2019 despite a possible trade deal in the first half of the year.

Figure 23: Recap of US-China trade war

US-led			
Date in effect	Tariff	Value of goods ($bn)	% of imports from China*
Jul 6 2018	25%	34	6.7%
Aug 23 2018	25%	16	3.2%
Sep 24 2018	10%	200	39.6%
China-led			
Date in effect	Tariff	Value of goods ($bn)	% of imports from US*
Jul 6 2018	25%	34	26.2%
Aug 23 2018	25%	16	12.3%
Sep 24 2018	5-10%	60	46.2%

Source: VNDIRECT
(*) Data in 2017

To the extent that a lasting trade resolution is unlikely to materialise in the immediate future, we believe Vietnam could benefit from trade diversion from China and the relocation of manufacturers away from China to avoid US tariffs. However, we adopt a cautious view as 1) when it comes to a trade war betwen the two biggest economies in the world, there are too many variables and interdependencies to be able to predict outcomes; 2) Vietnam has to compete with other countries to reap the to gain export market share from China. This will not be easy as the export potential for the country cannot be unlocked by the advantage of low labour costs alone. We expect the overall net impact on Vietnam to be positive if the current tariff regime is maintained (25% tariff on $250bn worth of Chinese exports to the US). But **Vietnam is likely to be negatively impacted by a slowdown in global trade and loss of business confidence in the event of a full-blown trade war. Also, if the current tariff regime stays in place for long, it could also trigger consumer price inflation in the US, raising the spectra of further interest rate hikes by the US Fed which could hurt emerging economies while also dampening appetite for equities as an asset class.**

In the short run, we see Vietnam benefitting from supply chain reconfiguration away from China. Among product categories subject to higher import tariffs from both countries, Vietnamese exports are well-placed as alternatives for Chinese-made goods. We expect top beneficiary export categories in Vietnam to include 1) fishery products; 2) headgear; 3) handbags; 4) furniture and 5) synthetic yarn and textile fabrics due to their high existing share of exports to the US relative to China which makes it easier to "nibble" away at Chinese market share by leveraging existing capabilities, track-record and client relationships.

Figure 24: Comparative advantage of Vietnam vs. other ASEAN countries

Country	Sector	Reason
Singapore	**High-tech**	- Singapore is not competitive in manufacturing due to its high operating costs and strong currency. - Manufacturing is focused on high value, low volume products or those that customers insist on doing in Singapore given its strong intellectual property protection regime.
Vietnam	**Textile, clothing & footwear**	- Vietnam has much lower labour costs than China and most ASEAN peers with sizable labour forces. - The country has been a major exporter of textile, apparel and footwear for well over a decade and therefore, has a strong skills base relative to other ASEAN countries.

	Electronics	- The country is shifting gear into electronics manufacturing, spurred by large anchor investments from Samsung and LG. - Vietnam's proximity to China's Pearl River Delta and long coastline make it easy to ship in components and parts which is a crucial advantage given the complex supply chains in this sector and China's position as a dominant supply hub.
Indonesia	**Food and beverage**	- Huge domestic market potential and well supported by productive agricultural sector and relatively predictable yields.
	Textile and clothing	- Low labour costs relative to China and a large labour force - Indonesia's textile exports contribute c.2% of the world textile demand, the second largest exporter after Vietnam in ASEAN implying a strong skills base. - Expertise in production of functional clothing (i.e. sports-wear) on top of basic clothing production ability.
	Automotive	- Indonesia has the largest automotive production capacity within ASEAN and was second only to Thailand in terms of auto exports in 2017.
	Plastics/ Rubbers	- Indonesia is the second largest natural rubber producer globally. Around 85% of Indonesia's rubber production is exported, while domestically sold rubber is mostly consumed by the automotive sector.
Thailand	**Automotive**	- Thailand has been the auto production hub in Southeast Asia over the past few decades as Thailand has a large domestic market and the government never had a national car brand development policy, thereby making way for global OEMs. - The Thai labour force is highly-skilled relative to most of ASEAN. - Strong presence of Japanese OEMs has also attracted many auto parts suppliers into the country, that have learnt to supply auto makers on a just-in-time basis. - Strong road, rail and port infrastructure helps reduce logistics costs.
	Electronics	- Strong automotive manufacturing ecosystem has created spillovers into electronics auto part manufacturing capabilities. - Thai electronic companies have ventured into making components for mobile phones and IT telecom equipment which also gives it an advantage in finished electronic goods production. Thailand is a major producer of consumer electrical appliances.
	Food and beverage	- Thailand is one of the largest food producers in the world due to a large agrarian base; the country has been a leading producer of processed food for years.
	Plastics/ Rubbers	- Thailand ranks as the largest rubber producer and exporter in the world. Complementing the natural rubber industry, Thailand is also growing its synthetic rubber segment by leveraging its robust petrochemicals production base. - Tyres are the number one rubber-based export from Thailand, with tyre producers accounting for roughly half of domestic rubber consumption given the country's large automotive manufacturing base. - Thailand has a large petrochemicals industry and is a regional leader in plastics production. Plastic packaging accounts for 48% of Thailand's raw plastic consumption, followed by 15% for its electronic sector, 14% for its construction sector and 8% for its automotive sector, according to ASEAN Briefing.
Malaysia	**Semiconductor**	- Malaysian semiconductor companies have built niche capabilities in assembly, packaging and testing of semiconductor chips. - Malaysian semiconductor companies have been the preferred partners/suppliers for foreign MNCs that are concerned over Intellectual Property (IP) infringement issues experienced with contract manufacturers in China. - The sector is supported by a strong ecosystem of local suppliers in Penang.
	Automotive	- Malaysia has a strong ecosystem of auto parts suppliers, many of which leverage its strong electronics parts and components manufacturing ecosystem.
	Plastics/ Rubbers	- Malaysia is the ASEAN region's top plastic export country. Its primary export destinations include Europe, China, Singapore, Japan and Thailand. - The Malaysian plastics market was estimated at US$3,305.4m, by revenue, in 2017 and is likely to expand at an estimated CAGR of 5.27%, during the forecast period 2018-2023, according to Mordor Intelligence.

Source: VNDIRECT

Figure 25: Market share of Vietnam vs. China in exports to the US in the $250bn list and our predicted Vietnamese export beneficiaries by product category

Category	China's market share	Vietnam's market share	VN market share relative to China	Key beneficiary product lines
Footwear/Headgear	63.9%	10.2%	0.16	Headgear
Raw hides, skins, leather & furs	54.7%	8.6%	0.16	Handbag
Metals	34.9%	1.3%	0.04	Stranded wire, cable
Miscellaneous	34.8%	4.9%	0.14	Furniture
Wood & wood products	32.6%	1.7%	0.05	Cartons, boxes, plywood
Textiles	30.9%	2.8%	0.09	Synthetic yarn, textile fabrics
Stone/Glass	25.6%	1.0%	0.04	Cement, glass
Machinery/Electrical	23.9%	1.5%	0.06	Electronic products
Chemicals & Allied industries	18.6%	0.4%	0.02	Insignificant
Plastics/Rubbers	17.2%	1.3%	0.07	Tyre
Transportation	14.0%	0.4%	0.03	Motor vehicles
Animal & Animal products	13.8%	7.9%	0.57	Fishery
Foodstuffs	7.1%	2.7%	0.38	Prepared fishery, fruits
Vegetable products	6.8%	11.6%	1.00	Not really substitutes
Mineral products	0.2%	0.1%	0.50	Insignificant

Source: VNDIRECT, USTR, TRADEMAP

Red boxes indicate the categories in which Vietnam exporters will benefit the most.

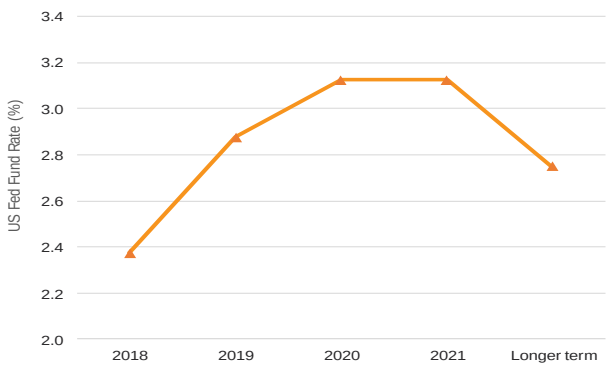
According to a recent survey conducted by AmCham China, 18.3% of the respondents (over 430 companies) indicated that they were considering the relocation of some or all of their manufacturing out of China. Among those who indicated that they were considering relocating, the top destinations were Southeast Asia (18.5%) and South Asia (6.3%). Indeed, according to media reports, touring activities in Vietnam industrial parks have intensified since Sep 2018, when the latest round of US tariffs took effect. We think US tariffs on Chinese goods could boost the current wave of already robust FDI flows into Vietnam. We also expect low value manufacturers (furniture, shoes, textiles and low-tech products) will be the quickest to migrate while higher value-added manufacturing (machinery, IT, and transportation) will likely take many years to relocate due to China's extensive supplier ecosystem and dense supply chain dependencies.

In addition, limited infrastructure, an unskilled labour force and a lack of an established industrial and supplier ecosystem are still major constraints that could discourage investors from continuing to relocate their manufacturing facilities from China to Vietnam.

Theme #2: External pressures from Fed rate hikes should abate but China's slowdown could pose headwinds to exports

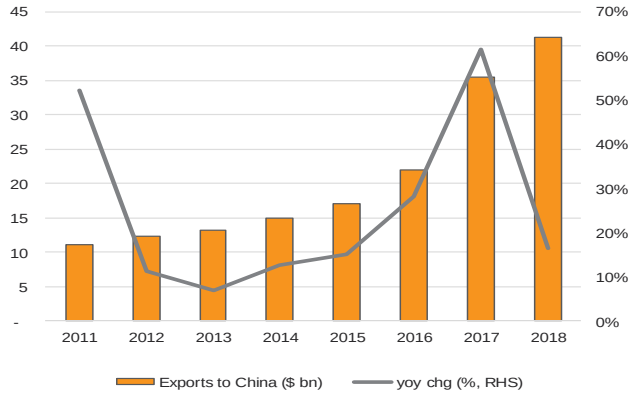
Since 2015, emerging countries including Vietnam have reeled under the impact of the Fed's balance sheet normalisation and the repatriation of funds to the US. However, in the latest meeting, Fed policy makers signaled an inflection point in the US rate hike path due to a slowdown in global growth, tightened global financial conditions and moderating impacts of the fiscal stimulus in the US. According to the most updated Fed dot plot, there will be only another two rate hikes in 2019 and one in 2020. Because of this dovish turn in Fed expectations, we take a view that global tightening pressures could ease in 2019. In addition, the US Dollar is expected to weaken with moderating US growth and a maturing Fed tightening process.

Figure 26: US Fed rate expectations: Two in 2019 and one in 2020



Source: VNDIRECT, BLOOMBERG

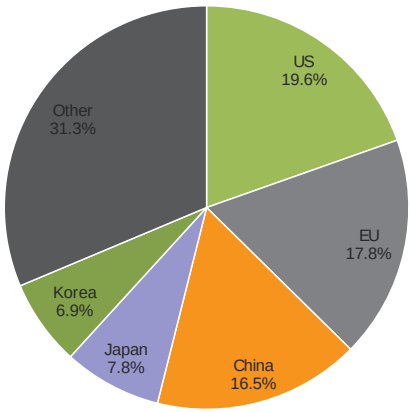
Figure 27: Vietnam's export growth to China moderated in 2018 but remained in double-digit territory



Source: VNDIRECT, CUSTOMS

China's slowdown is another concern for Vietnam's economy. However, we think China will continue on its path of a soft landing for its economy. The country still has room for policy easing to support the private sector and infrastructure development in order to offset the negative impact from trade tensions. Therefore, a soft landing is more likely than not. However, China's slowdown could well continue and will weight on Vietnam's export growth, in our view.

Figure 28: China ranked 3rd among Vietnam's top export markets in 2018



Source: VNDIRECT, GSO

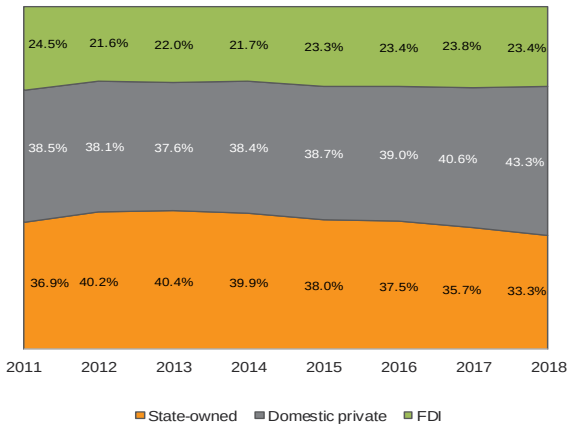
Despite CNY volatility during 2018, the SBV managed to keep the dong on a gentle glide slope, helped by the following factors: 1) Vietnam's strong fundamentals with robust growth and controlled inflation; and 2) the country is considered a net beneficiary of US-China trade tensions. We think the CNY has already seen a sizeable adjustment in 2018 due to pressures from anticipated slowing growth and higher US tariffs towards China exports. Therefore, we do not foresee a large-scale depreciation of the dong in 2019.

Even though Vietnam's export growth could slow due to slowing Chinese demand, we believe that the impact of this on the current account will by partially offset by strong FDI inflows from factory relocation out of China. Therefore, we do not envision the slowdown in export growth to pose a major threat to dong stability.

Theme #3: Could the domestic private sector become the next economic growth engine? Perhaps but don't expect miracles.

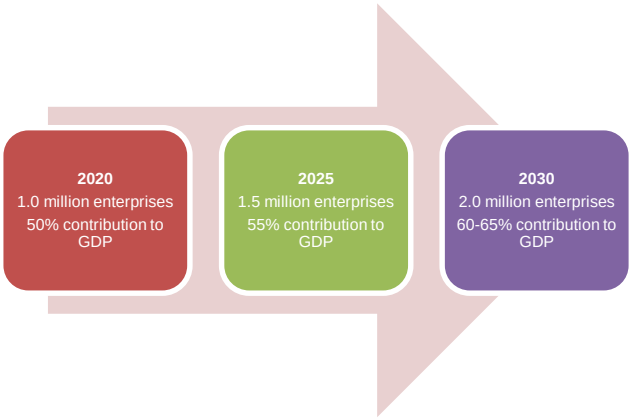
During the last few years, the FDI sector increased its contribution to Vietnam's GDP at the expense of the domestic private sector. In recognition of Vietnam's growing reliance on FDI to drive economic growth in recent years, the government is trying to strengthen the domestic private sector in pursuit of a more balanced economic growth model. Indeed, the private sector has been receiving more attention than ever from the government. The government has 1) reduced business rules and regulations; 2) made commitments to develop a pro-private sector business environment with the aim of boosting private sector contributions to GDP. The government wants the domestic private sector to contribute half of Vietnam's GDP by 2020, up from 43% in 2017. In our view, the recent pick-up in private investment, aided by supportive policies, could boost economic growth. In 2016-18, private investment grew at an average of 15.0% per annum, while State investment growth grew by only 6.0% per annum. FDI investment growth over 2016-18 slowed to an average of 10.9% per annum vs. 13.4% during 2013-15.

Figure 29: Share of domestic private investment has gradually risen in recent years



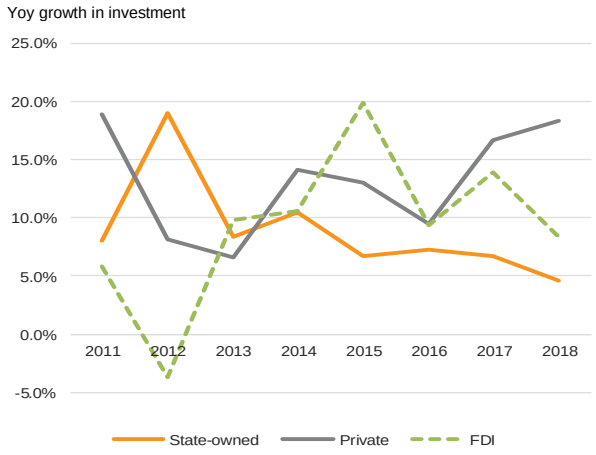
Source: VNDIRECT, GSO

Figure 30: The government's objectives for the domestic private sector



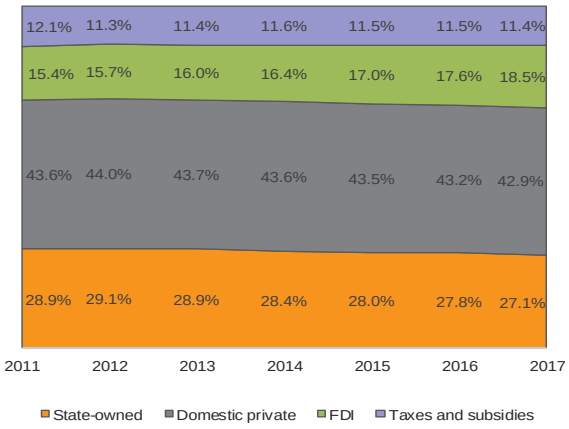
Source: VNDIRECT, GSO

Figure 31: Rising domestic private sector investment during 2016-18



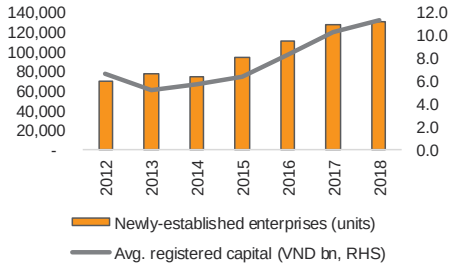
Source: VNDIRECT, GSO

Figure 32: The FDI sector has continuously gained share in Vietnam's GDP mix in recent years



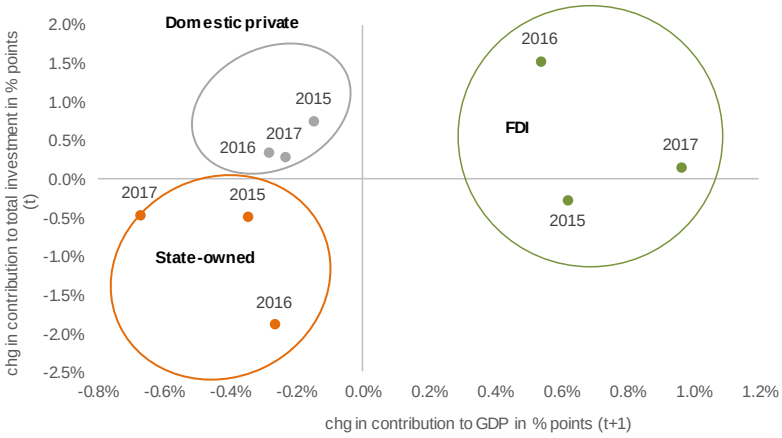
Source: VNDIRECT, GSO

Figure 33: A significant increase in the number of registered private businesses



Source: VNDIRECT, GSO

Figure 34: Even though domestic private investment is increasing its share in total investment, its contribution to GDP is falling



Source: VNDIRECT, GSO

Despite a recent boost from private investment, we believe it will take many years to reach the first milestone in this area that the government targets to achieve by 2020 (1 million enterprises and raising private sector contribution to 50% of GDP). Under our base case scenario, the private sector would have to grow at an average of 16.1% per annum in 2019-20 to achieve the second milestone laid out by the government. We believe that this is an unrealistic expectation in light of the growth of around 6.0% seen during the past five years.

Despite a dramatic increase in the number of newly-established private businesses, most of them registered to operate in relatively low productivity sectors such as commerce, services and construction, not manufacturing. These private sector developments, as such, imply that the private sector will have less significant an impact on future economic growth. In addition, we see sluggish public investment and recent setbacks in SOE reforms as further constraints for promoting the development of the domestic private sector.

In general, we see a more favourable business environment emerging for domestic private companies rather than a miraculous transformation of this sector which will turbo-charge economic growth. We already see improving management quality at a few, large private companies (top VN500 or large-cap listed companies) which is an indication that a phased and gradual improvement of the domestic private sector is already underway. With the newfound policy support, these companies could become major engines of economic growth in the future, thereby reducing Vietnam's outsized reliance on FDI.

STOCK MARKET 2018 REVIEW: A BASS TONE AFTER HIGH NOTES

VN-INDEX could not cling on to its gains in early 2018 amid growing uncertainties in global financial markets.

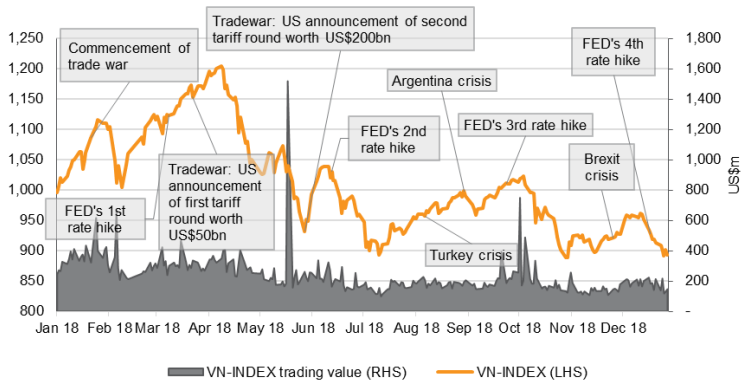
Note: All pricing data in this section is as of 28 Dec 2018 unless otherwise noted.

The VNDINDEX succumbed to growing risk-off sentiment in global equity markets in 2018. After being the world's best performer in 1Q2018 with a 19.3% increase, and recording a historical peak in early April, the VN-INDEX rapidly lost momentum and became one of the world's worst performers in 2Q18 with a 19.7% fall.

Figure 35: VN-INDEX 2018: Retreated after making new historical peak

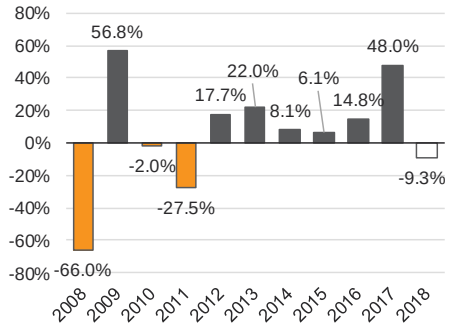
Source: VNDIRECT, Bloomberg

Figure 36: VN-INDEX 2018 performance



Source: VNDIRECT

Figure 37: The VN-INDEX ended 2018 at 892.5 pts to record the first negative annual performance since 2011

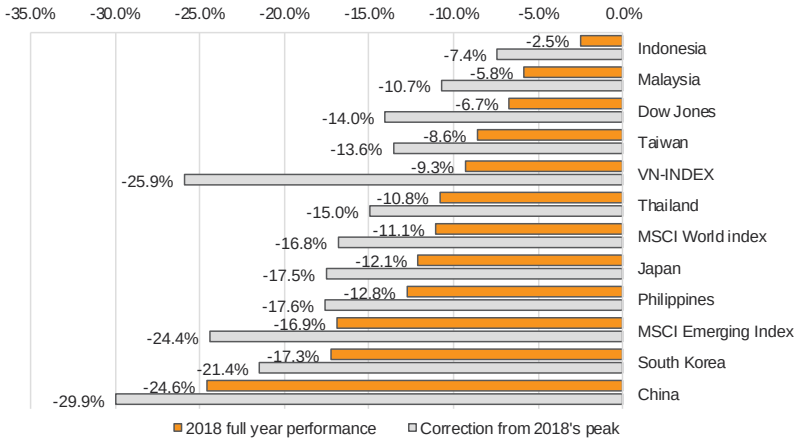


Source: VNDIRECT

We attribute the big correction in the VN-INDEX in 2Q18 to the following main factors:

- The surge in the VN-INDEX in 1Q18 was not really matched by earnings growth. The VN-INDEX TTM P/E touched 21.9x at the peak of the index, marking a huge expansion from the 14.0-16.0x levels seen in the 2016-2017 period.
- Global equity markets saw big corrections, led by the sharp reversal in the US market which was largely fuelled by escalating US-China trade tensions and a series of rate hikes by the US Federal Reserve.

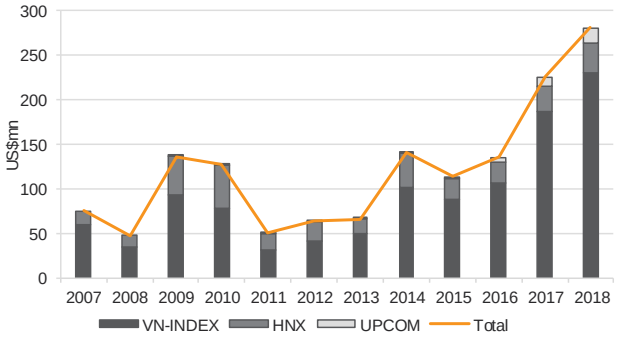
Figure 38: VN-INDEX was a relative outperformer on a full year basis, despite seeing one of the strongest corrections from 2018 peak levels



Source: Bloomberg

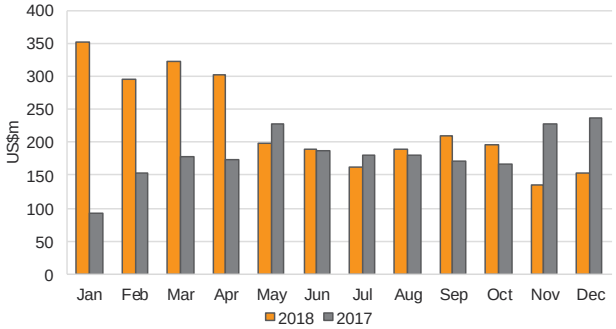
Growing risk aversion on mounting uncertainty and sharp market declines in 2Q18 spurred a retreat in liquidity. We saw no significant flows re-entering the stock market even during the short up-trend in 3Q18 and 4Q18. We think the correction in 2Q18 was unavoidable given frothy valuations and rising global risks but the poor performance in the second half of 2018 was not aligned with the strong fundamentals of the Vietnamese economy which recorded the highest GDP growth rate in a decade (7.08%) even as inflation remained subdued and the currency was stable. Even though 2018 ADTV recorded a 27.6% increase versus 2017, 4Q2018 ADTV decreased 28.9% compared with 4Q2017.

Figure 39: Market Liquidity surged in 1Q18



Source: VNDIRECT

Figure 40: Liquidity retreated dramatically starting in May 2018

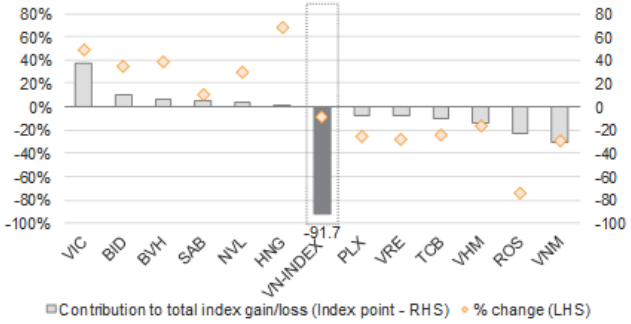


Source: VNDIRECT

Market diverged in the first half of 2018, but dispersion across tiers narrowed in the second half of the year. Leading up to the VN-INDEX hitting its 1,200-peak, VN30 stocks far outperformed mid-caps and small-caps but subsequently corrected much more sharply than the rest of the market. At Dec 2018, VN30 had still outperformed the rest of the market on an annual return basis but by a narrower margin.

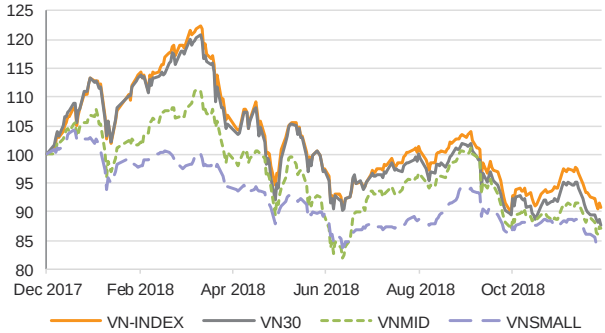
Even though VIC contributed over 37.4pts to the VN-INDEX, the top seven laggards wiped away 94.0pts and dragged the index down 91.7pts (-9.3%) for the full year 2018. At 28 Dec 2018, 253 stocks on HOSE (67% of the total listed universe) had recorded negative returns. Even newly-listed tickers failed to reignite investor appetite and featured heavily in the list of top laggards. Of the top 10 laggards in the VN-INDEX in 2018, three stocks were listed in 2018 (VHM, TCB, HDB) and three others were listed in 2017 (VRE, PLX, VPB).

Figure 41: VN-INDEX's top movers and laggards - VIC was the major pillar of the index in 2018



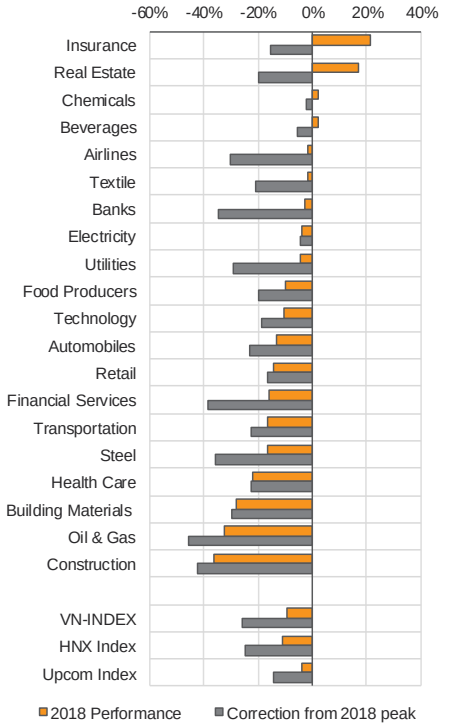
Source: Bloomberg

Figure 42: Market diverged by tier in 1H18 but re-converged in the second half of the year



Source: FiinPro

Figure 43: Most sectors saw strong corrections from the 2018 peak, theoretically entering bearish zones



Source: FiinPro

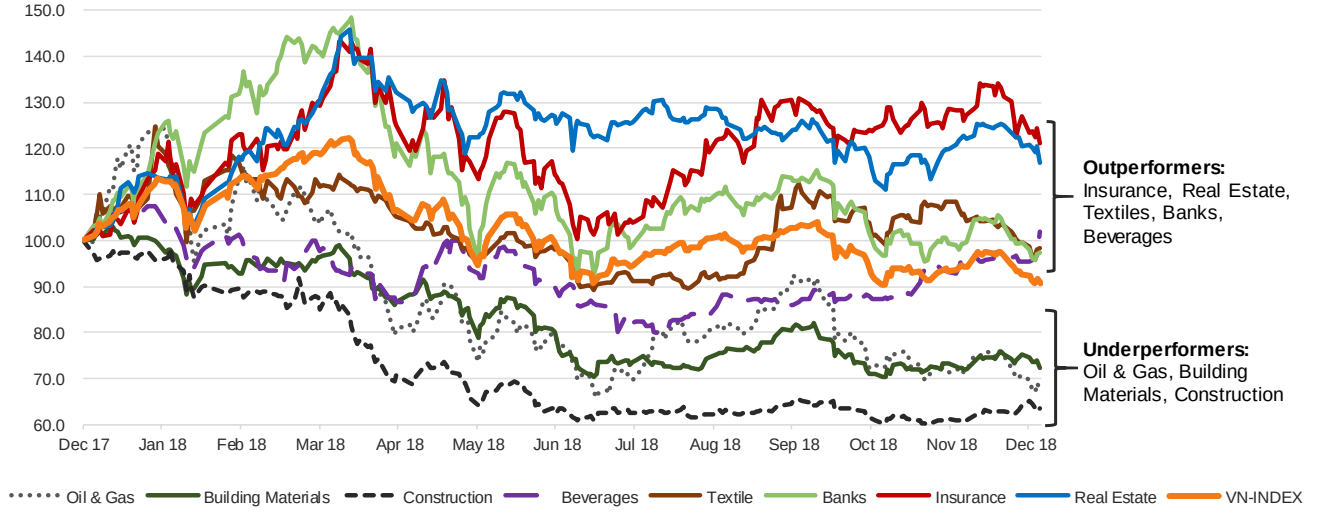
The VN-INDEX reversal was quite broad-based from a sectoral perspective but some sectors still saw positive full year returns. 2018 could be seen as a revenue-booking period for real estate companies as they delivered apartments/products sold 1-2 years ago. However, the sector's performance was mainly driven by VIC (+49.2%), while some major real estate stocks saw price falls (VHM: -17.0%, VRE: -27.5%). The insurance sector was the top performer this year, and just like real estate, the insurance sector index is not representative of the industry but the largest insurance company BVH was a stellar performer (+38.1%). BVH's surge in 2018 is somehow hard to explain as its bottom line dropped 85.7% yoy in 9M18 dragged down by a fall in investment income due to stock market weakness.

Concerns over the slowdown in new real estate projects made construction and building material stocks among the worst performers in 2018. However, the deep decline of the construction index was partly due to outlier ROS, which dropped 74.4% in 2018. Meanwhile, despite the average oil price surging over 30% yoy, the oil & gas sector ended the year down sharply due to the sharp fall in newly listed downstream oil and gas stocks (BSR: -56.0%; OIL: -32.6%).

Key Gainers and Losers in 2018:

- **Insurance sector key gainer:** BVH (38.1%)
  Insurance sector key losers: BMI (-41.7%), BIC (-27.8%)
- **Real estate sector key gainers:** VIC (49.2%), NVL (29.2%), DXG (24.8%)
  Real estate sector key losers: VRE (-27.5%), DIG (-20.2%)
- **Bank sector key gainers:** BID (32.0%)
  Bank sector key losers: VPB (-21.3%), CTG (-20.2%)
- **Building material sector key gainers:** NNC (20.1%), FCM (18.2%)
  Building material sector key losers: VCS (-39.6%), VGC (-27.2%), BMP (-35.5%)
- **Oil & Gas sector key gainers:** PGS (28.2%), PGD (8.7%)
  Oil & Gas sector key losers: BSR (-56.0%), OIL (-32.6%), PVD (-37.5%)
- **Construction sector key gainers:** VCP (72.5%), DPG (58.7%)
  Construction sector key losers: ROS (-74.4%), HBC (-40.5%), CTD (-27.7%)

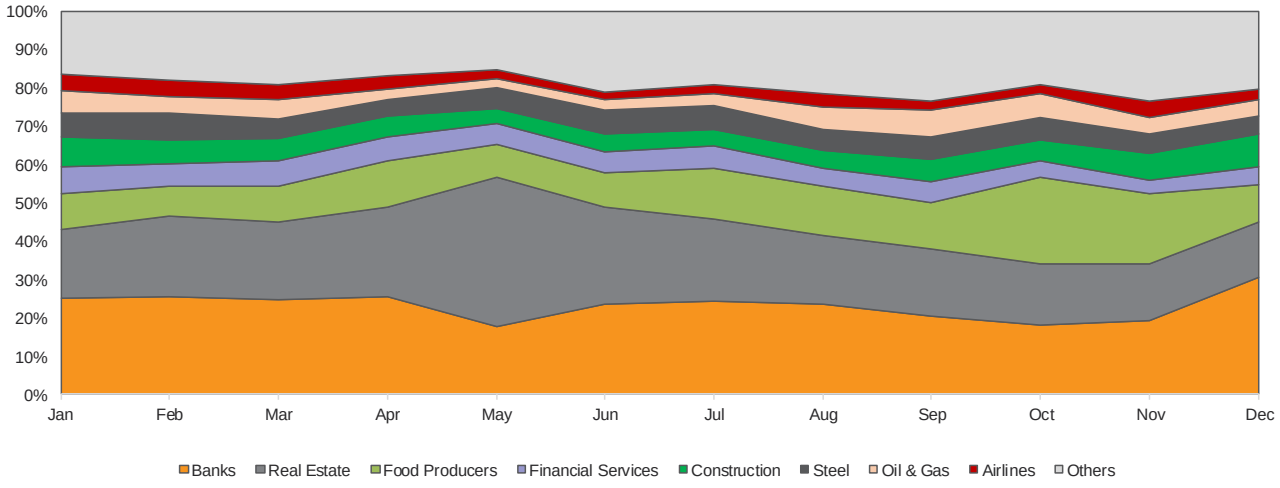
Figure 44: Top outperforming and underperforming sectors in 2018



Source: VNDIRECT, FiinPro

With the retreat of ROS, construction lost its sizable contribution to total market ADTV seen in 2017, leaving the Banks, Real Estate and Food producers as the top 3 traded sectors with over 50% collective contribution to total market trading value.

Figure 45: Trading value share by sector (monthly, 2018): Money chased Banks, Real Estate and Food producer stocks.

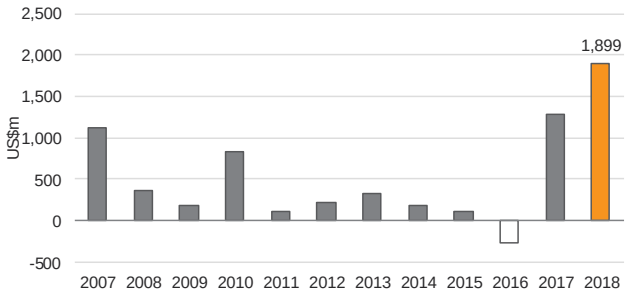


Source: VNDIRECT

Foreign investors net sold via the matching method, but still net bought overall in 2018, focusing on deals or put-through transactions of newly-listed stocks.

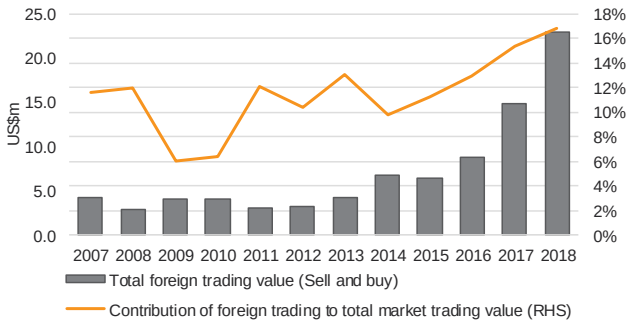
Despite a new record in terms of net buying value in 2018 worth VND1.9bn and increased contribution to overall market trading value, foreign capital was not the engine for the market unlike in 2017. New capital inflows mainly focused on deal-related and put-through transactions which saw net buying worth US$2.6bn (versus net sold value of US$0.7bn on HOSE via order matching method), resulting in an overall net bought position worth U$1.9bn. As of Dec 28, 2018, foreign investors net sold on 155 out of 247 trading days (63%), putting significant pressure on the stock market.

Figure 46: Foreign investors set a record high in net bought value in 2018 (total across 3 exchanges)



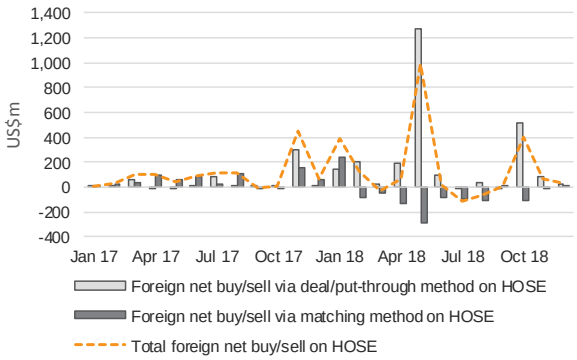
Source: VNDIRECT

Figure 47: Foreign investors contributed more to total market trading value than at any point in the past eleven years



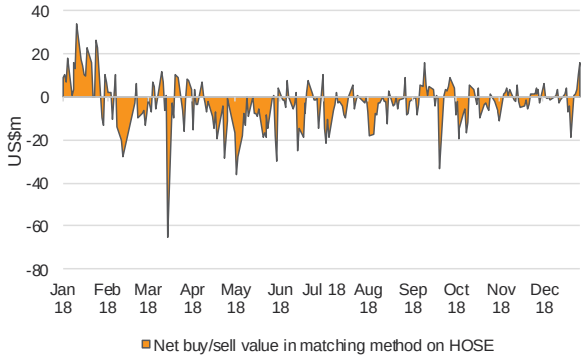
Source: VNDIRECT

Figure 48: Monthly net buy/sell value on HOSE: Foreign net buys in 2018 were mainly via deal/put-through method



Source: FiinPro

Figure 49: Foreigners net sold during most of 2018 via the order matching method



Source: FiinPro

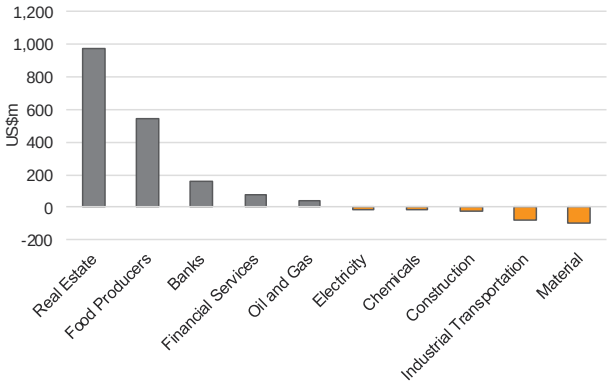
Real estate and food producers were the favourite sectors of foreign investors in 2018 driven largely significant transactions by VHM, VRE, NVL and MSN. On the other hand, construction, transportation and materials were among the top three top foreign net sold sectors as foreigners retreated selectively from cyclical names that were in favor in 2017 (VJC, CTD, HPG, VGC).

Figure 50: Net buying value via deal/put-through of foreign investors in 2018 (data as of Dec 18, 2018)

	Ticker	Net buy/sell value (US$m)
1	VHM	1,240
2	MSN	635
3	VRE	206
4	NVL	147
5	YEG	106
6	HDB	103
7	E1VFVN30	62
8	VIS	56
9	HPG	23
10	VJC	21

Source: FiinPro

Figure 51: Top five foreign net bought and net sold sectors: Net flow (US$m)



Source: VNDIRECT

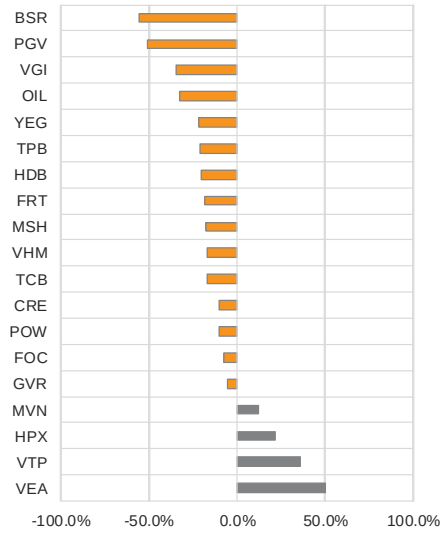
Figure 52: Top net bought/net sold stocks in 2018: Foreign trading activity focused on newly listed names (US$m)

		Net buy	Value buy	Value Sell			Net buy	Value buy	Value Sell
1	VHM	1,129	1,600	470	1	VIC	-434	723	1,157
2	MSN	578	1,230	652	2	VJC	-109	258	367
3	VRE	167	726	559	3	HPG	-85	711	796
4	YEG	112	127	15	4	VNM	-69	1,210	1,279
5	HDB	101	399	297	5	BSR	-60	18	78
6	DXG	68	191	123	6	VGC	-47	46	94
7	VIS	57	58	1	7	VCG	-38	16	54
8	NVL	54	231	177	8	MPC	-21	5	26
9	SSI	48	265	217	9	VCB	-17	355	371
10	FRT	47	68	22	10	CTD	-16	102	117
11	VEA	41	65	24	11	CTG	-16	53	69
12	SCS	41	64	23	12	HSG	-15	51	66
13	POW	39	84	45	13	KBC	-14	51	65
14	STB	38	86	48	14	DIG	-13	26	39
15	BID	35	160	126	15	GTN	-13	2	15
16	KDH	25	57	32	16	TAG	-12	0	12
17	VTP	25	25	1	17	IDC	-11	0	11
18	QNS	24	31	7	18	HDG	-9	5	14
19	BVH	24	140	117	19	HAG	-8	9	18
20	PLX	22	93	71	20	VFG	-8	0	9

New ly-listed in 2018

Source: VNDIRECT

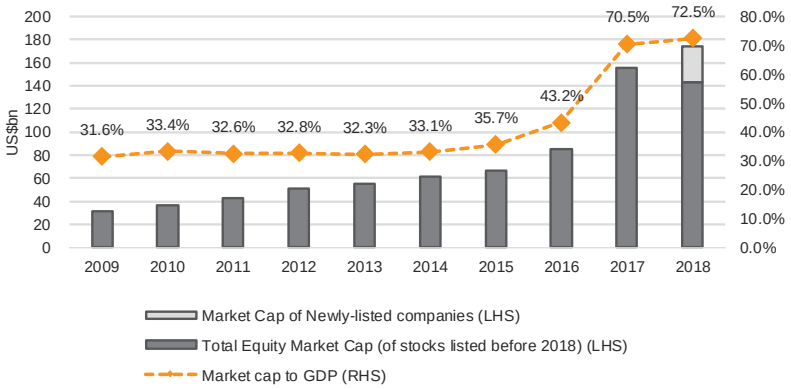
Figure 53: Performance of notable stocks since listing in 2018



Source: VNDIRECT

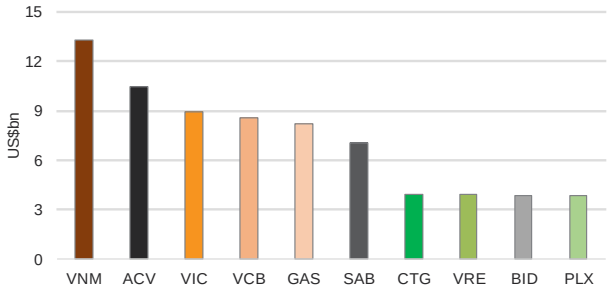
Unglamorous debuts of newly-listed stocks. Total equity market cap grew 12.1% in 2018 and reached 72.5% of GDP. Newly-listed stocks in 2018 contributed 19.8% points of market cap growth while the negative performance of legacy stocks took 7.7% points away from market cap in 2018. Following 2017 results, the market was expecting another stellar year for newcomers, with a number of notable new listings such as VHM, TCB, VEA, HDB, and PetroVietnam's triad BSR, OIL, POW. However, the lacklustre stock market rendered the debuts of newly-listed stocks unimpressive although select listings saw huge transaction values such as VHM (US$1.2bn), YEG (US$102.4m) and HDB (US$53.8m).

Figure 54: Vietnam's total stock market capitalization reached 72.5% GDP



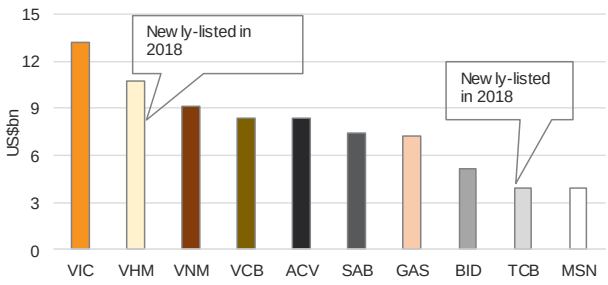
Source: VNDIRECT, GSO, FiinPro

Figure 55: Top 10 companies by market cap as of Dec-2017



Source: VNDIRECT, FiinPro

Figure 56: Top 10 companies by market cap as of Dec-2018

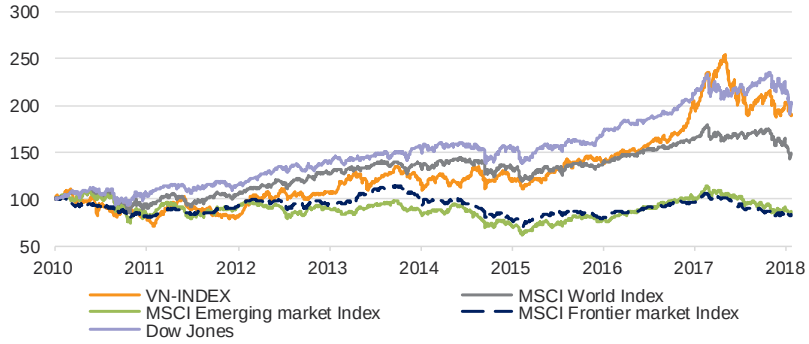


Source: VNDIRECT, FiinPro

STOCK MARKET OUTLOOK: TIME TO ROTATE INTO MORE HIGH QUALITY AND DEFENSIVE NAMES

Vietnam's stock market will continue to face challenges from both "black swan" events and a maturing global business cycle.

Figure 57: Global equity markets have enjoyed a 10 year-long uptrend



Source: Bloomberg

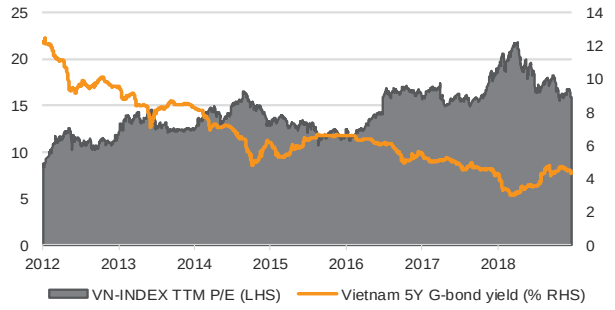
Trade tensions between the US and China marked a "black swan" event that very few expected in 2017 and which kick-started a global sell-off in February. Combined with four rate hikes by the US Fed, the trade war became a psychological burden on the global stock market and materially changed the view of investors on the world economic outlook. **To us, this goes to show that in a late-cycle economic and late-stage equity bull market, investor sentiment is highly exposed to negative shocks created by all manner of black swan events. Investors should therefore prepare for heightened volatility and overreaction to any negative news flow on the economy or geopolitical events in 2019.**

Valuation multiples may contract further due to global challenges but positive earnings growth will provide some cushion

We expect the VN-INDEX P/E to stay under pressure in 2019 due to the following factors:

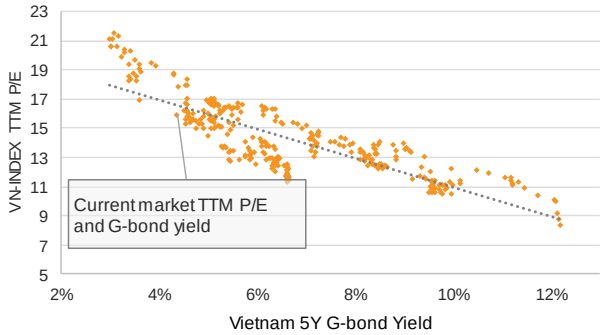
- Foreign capital flows withdrawing from emerging markets and seeking safe havens due to possible future Fed rate hikes and a worsening global economic environment;
- Vietnam's domestic bond yields may increase in 2019, albeit marginally, which will increase equity discount rates

Figure 58: VN-INDEX TTM P/E and Vietnam G-bond yield 2012-2018



Source: Bloomberg

Figure 59: Historical relationship between the VN-INDEX TTM P/E and Vietnam 5Y G-bond yield

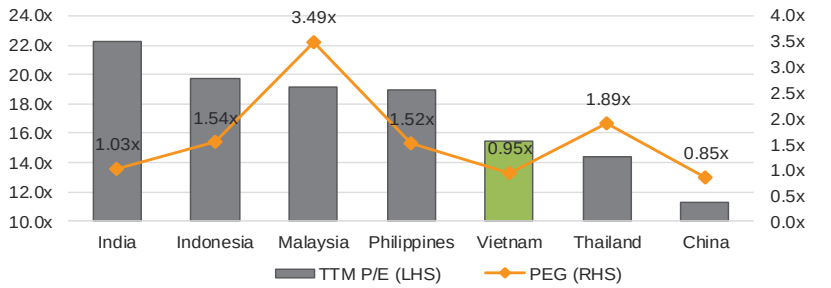


Source: Bloomberg, VNDIRECT

On Dec 28, 2018 the VN-INDEX was trading at a TTM P/E of 15.5x (a 29.4% discount to the TTM P/E when the VN-INDEX peaked at 1,200 points in the first quarter), which looks cheap on the basis of estimated market capitalization-weighted earnings growth of 25% across the HOSE listed universe in 2018 per Bloomberg consensus.

Corporate earnings growth across the VN-INDEX universe is expected to slow in 2019, but still forecasted to touch a robust 16.4% (on a market capitalization-weighted basis) per consensus which implies that the VN-INDEX is trading at a very reasonable level on a PEG basis.

Figure 60: TTM P/E and PEG of Vietnam and regional peers



PEG calculated by consensus 2019 earnings forecast

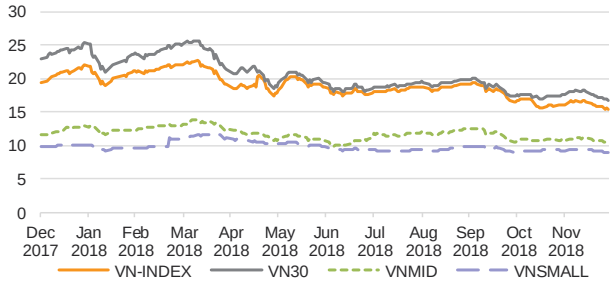
Source: Bloomberg

Overall, we expect a TTM P/E contraction of around 5% to touch 14.7x which, juxtaposed against a 16.4% rise in market cap-weighted earnings during the year should translate into an approximate 11% rise in the index to touch 990 points towards year end 2019. However, the index could breach this level in the first half of 2019 on possible news of a trade war deal and Chinese fiscal stimulus but optimism is unlikely to last into the second half due to a continued economic slowdown in the US and, possibly, in China as well.

Market trends in 2019: We foresee a flight to quality.

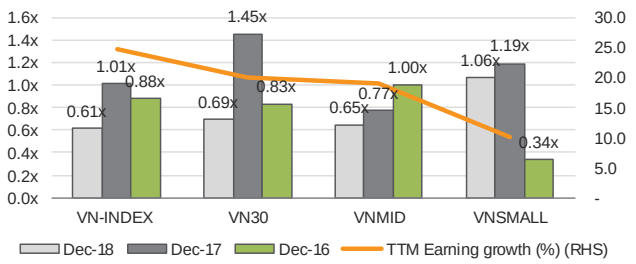
- Money will focus less on new listings and more on high quality companies with leading industry positions and healthy balance sheets.
- Investors will partially rotate into more defensive sectors such as electricity, consumer staples or companies with high cash dividend yields.
- The positive export story may continue with tailwinds from Free Trade Agreements (FTAs) and the US-China trade war drawing investors to Fishery, Textiles, Agribusiness, Industrial Parks and Logistics stocks.
- Midcaps may be selectively targeted. Although market breadth typically narrows in aging bull markets and flows concentrate on larger, blue chip and more liquid names, we believe that the end of a "momentum-driven" trading strategy will spur interest in bottoms-up stories. This could work to the benefit of high quality midcaps which have so far been relatively ignored and trading at attractive valuations, particularly in light of solid earnings growth.

Figure 61: TTM P/E of VN-INDEX by tier



Source: VNDIRECT, FiinPro

Figure 62: PEG of VN-INDEX by tier



PEG calculated based on TTM earnings growth.

Source: VNDIRECT, FiinPro

VIETNAM OFFERS SUPERIOR PROSPECTS TO MSCI FRONTIER MARKETS AND SMALLER EMERGING MARKETS (EM)

Vietnam is positioned to enter MSCI Emerging Markets with a respectable standing over the medium term, and to continue improving its frontier market status in the interim. Given that an emerging market upgrade for Vietnam is still at least two years away, we see greater value in focusing on the short term perks as Vietnam ascends the MSCI Frontier Markets league table which will result in increased attention from both frontier and emerging market investors.

Vietnam has multiple advantages compared to other smaller emerging markets. Vietnam's delayed EM upgrade can actually be beneficial in the next couple of years, as it can be considered a superior alternative to most frontier markets and even some small emerging markets:

- **Superior Liquidity**: Vietnam's liquidity is still superior to other smaller emerging markets such as Egypt and Pakistan (circa US$25-50m ADTV), though it is still lagging behind some of its Asian emerging market peers such as Malaysia and Thailand. The smaller weighting of markets such as Egypt and Pakistan, for example, has resulted in select EM fund managers choosing to ignore these markets (only 3-5 MSCI EM constituents), while Vietnam has seen liquidity nearly double in the past two years.
- **Pakistan as a failed case study**: The removal of two Pakistan MSCI EM constituents' further attests to the downside risks of entering the MSCI Emerging markets as a smaller player, as its weight in MSCI EM will now drop further to 0.03-0.04%. As we mentioned in our **Navigating 2018**, we believe that Vietnam's delayed EM upgrade will prove to be beneficial for the market, as Vietnam has the potential to become the largest constituent in MSCI Frontier Markets and to later enter MSCI EM as a larger player than it would if it were upgraded this year.
- Most notably, Vietnam is moving forward with the EM upgrade process, and is currently being reviewed by FTSE. Further critical areas for improvement include information disclosure and further FOL removal. However, radical improvements in these areas cannot be counted upon, in our view as other markets such as Argentina have been upgraded despite not meeting some of these criteria. We are awaiting further clarity from FTSE and MSCI in June 2019 regarding Vietnam's EM upgrade and see its status as a frontier giant to be an extremely beneficial attribute in its candidacy for an EM upgrade.
- Vietnam has comparatively favourable macro characteristics, which will result in investors increasing exposure when Vietnam does enter the EM club (unlike the case for Pakistan which saw its upgrade to EM coincide with a deterioration in its macroeconomic fundamentals). Argentina received increased attention from EM investors in previous years, though it was still a frontier market, simply because its weighting in MSCI Frontier Markets increased. For Vietnam, the case is much stronger given that its weighting in MSCI Frontier Markets will be similar to Argentina's in the past, while the macro picture of Vietnam is much more robust than it was in Argentina's case.

Figure 63: MSCI frontier index composition by country: 2018 YE versus 2017 YE

Countries	Dec 17	Countries	Dec 18
Argentina	23.2%	Kuwait	24.1%
Kuwait	15.8%	Argentina	16.9%
Vietnam	**14.3%**	**Vietnam**	**16.9%**
Morocco	7.8%	Morocco	7.2%
Nigeria	7.6%	Bangladesh	6.5%
Others	31.3%	Others	28.5%

Source: MSCI

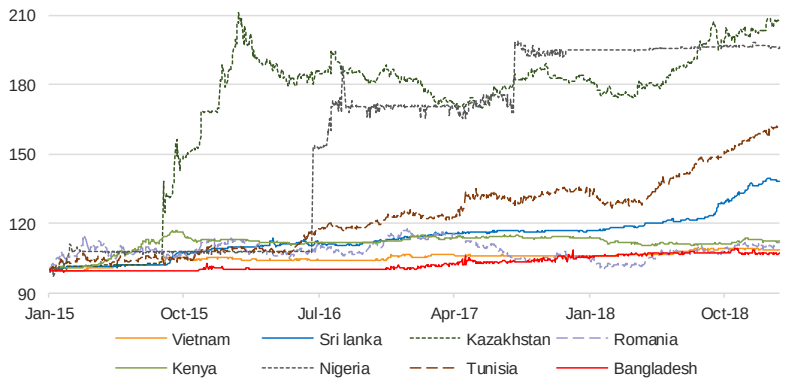
Overall, we are optimistic about Vietnam's stronger weighting in MSCI Frontier Markets, and see this as a case for further foreign inflows, at a time when other frontier and smaller emerging markets such as Kenya, Sri Lanka, and Pakistan have been

struggling with growing political and economic risks. Vietnam is therefore poised to benefit strongly in the coming years as it continues maturing to the point at which it is able to exit "frontier market purgatory". Its economic development, coupled with rising liquidity will also make its future entry into MSCI Emerging Markets more favourable. Moreover, there is also a clear precedent of frontier-focused funds choosing to hold onto positions in emerging markets when their holdings are upgraded. For example, frontier funds still held positions in Pakistan when it was upgraded to EM status. This trend will bode well for Vietnam when it is upgraded. We expect positive developments even in the absence of an MSCI EM upgrade.

Vietnam's sovereign equity valuation premium underpinned by favourable macro, stable politics, and superior liquidity relative to frontier peers.

The "macro-political stability premium": Vietnam's current favourable economic standing has resulted in its currency holding up, while other frontier and emerging market currencies depreciated sharply this year. This phenomenon is very similar to what occurred in 2015, when a plethora of FM/EM currencies depreciated, while Vietnam's currency stayed resilient due to its strong macro fundamentals.

Figure 64: Vietnam's currency relative to frontier peer currencies, versus the US Dollar (base year = 2015)



Source: Bloomberg

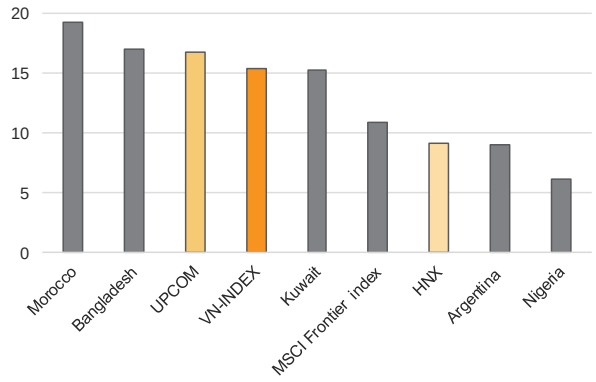
Vietnam's favourable external debt levels, although high, have not dented market sentiment, given that much of this includes concessional or Official Development Assistance (ODA) loans. The IMF considers Vietnam's FX import cover to be adequate, and it is also imperative to note that a large amount of Vietnam's imports are components for products it exports (i.e. electronics), which makes it less vulnerable to a balance of payments crisis. Vietnam is one of a few MSCI Frontier Markets that has a current account surplus, and it will easily sustain this advantage moving forward driven by its robust export growth. Another positive point to note is that Vietnam has established itself as a politically stable FDI destination, while risks with political transition can be seen in Asian frontier markets such as Sri Lanka and Pakistan. Investors searching for a politically stable and low cost manufacturing destination can clearly see Vietnam's success in drawing manufacturers to the country, while other frontier markets have a less reputable image or are behind Vietnam in terms of export diversification and sophistication. We also see the stock market being further supported by Vietnam's relatively strong and broad-based economic growth. Vietnam's increasingly diversified export mix should support longer-term, sustainable growth, while other frontier markets such as Sri Lanka and Bangladesh face the issue of having

comparatively lower export diversification with a focus on labor cost arbitrage.

The liquidity premium: Vietnam's superior liquidity compared to other frontier markets and smaller emerging markets warrants a premium, as the market has now become easier for institutional investors to access. Vietnam's liquidity surpasses a large number of emerging markets, such as the Philippines, Egypt, Peru, and Pakistan, and is also more than 20x higher than other frontier markets such as Sri Lanka, Romania, and Kenya. Therefore, we think that it is most appropriate to compare the valuations in the small/mid cap space or other indexes such as the HNX (around 9x P/E) to that in other frontier markets when making a country-level peer comparison. When using this method, it can actually be said that Vietnam trades at a discount to some of these frontier markets, rather than a premium.

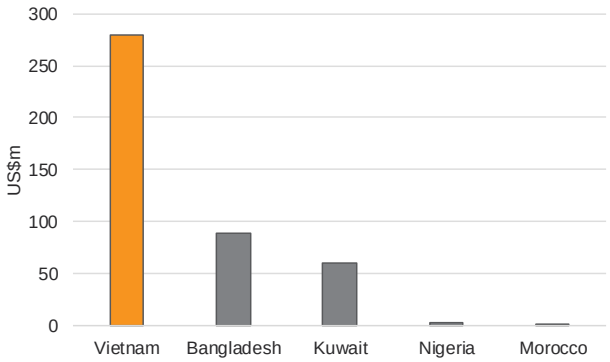
Most frontier markets are inferior to Vietnam, but Bangladesh is a notable rival

Figure 65: TTM P/E of Vietnam's main indices and other frontier markets



Source: Bloomberg, FiinPro

Figure 66: 1M ADTV of Vietnam and other frontier markets in Dec-2018



Source: Exchanges' websites,

Vietnam's PMI has remained above 50 since 2016, following several dips below 50 seen during 2014-2015. This PMI reading has also been one of the highest among other ASEAN peers in recent months. This reflects the success of its export diversification efforts since 2016, and the fact that it has still been able to sustain its textile export growth despite strong competition from other countries such as Bangladesh. The outlook for Vietnam's economy on the back of the US-China trade war is much clearer, as compared to 2016, as Vietnam is clearly being seen as a beneficiary of this development at the expense of China.

One key risk to monitor is the continued rise of Bangladesh's textile and garments export sector, as this country of around 166 million is easily positioned to rival Vietnam in terms of textile products given its comparatively lower wages and its existing dominant position in this industry. Garment workers in Bangladesh only make around $56/month, compared to around $200/month in Vietnam. Vietnam is no longer wage competitive with other frontier market textile exporters, thought its strong global position for textile exports trounces other frontier competitors such as Laos, Sri Lanka, Cambodia, and Myanmar. **Vietnam's continued export success will rest upon in its ability to be wage competitive with other emerging markets and on its ability to continue moving up the value chain into more sophisticated export categories.**

Figure 67: Vietnam versus Bangladesh: How the two frontier giants stack up

	Vietnam	Bangladesh
Population 2018 (m)	94.7	166.4
GDP FY18 (US$bn)	240	286
GDP growth FY18	7.08%	7.86%
GDP per capita (US$)	2,535	1,718
Total exports value FY18 (US$bn)	244	41
Stock market capitalization	174	80
Stock market ADTV (US$m)	280	88
TTM coporate earning growth	25.0%	11.7%

Source: Bloomberg, Official information websites, GSO

Within the frontier space, Bangladesh poses the greatest risk to Vietnam given its higher textile export market share, lower wages, and long term ability to be competitive in areas such as pharmaceutical manufacturing and ICT. While Vietnam and Bangladesh are both positioned to benefit from the US-China trade war, Vietnam can be seen as a bigger beneficiary due to its faster export diversification progress and geographical proximity to China.

Within the frontier asset class, the recognition of Bangladesh's potential – and given the country's population size advantage over Vietnam – could also mean that the Bangladesh equity markets could increasingly compete for foreign capital flows versus Vietnam.

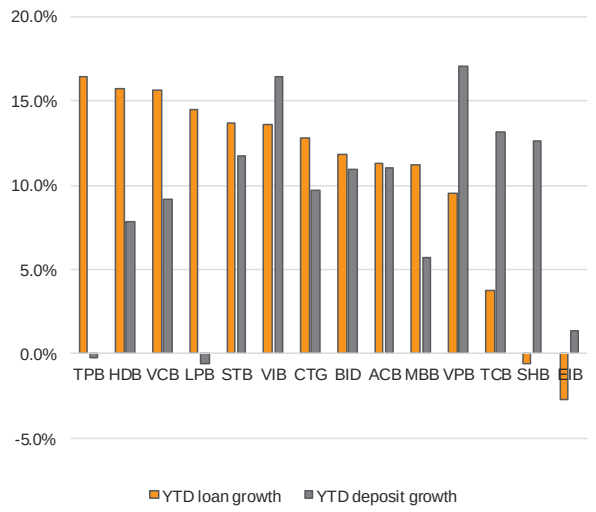
BANKING: NEUTRAL OUTLOOK ON THE BACK OF TIGHTENING MONETARY POLICY

2018 wrap-up: Loan growth below expectations but profits surge

Credit growth decelerating from recent years' rapid pace

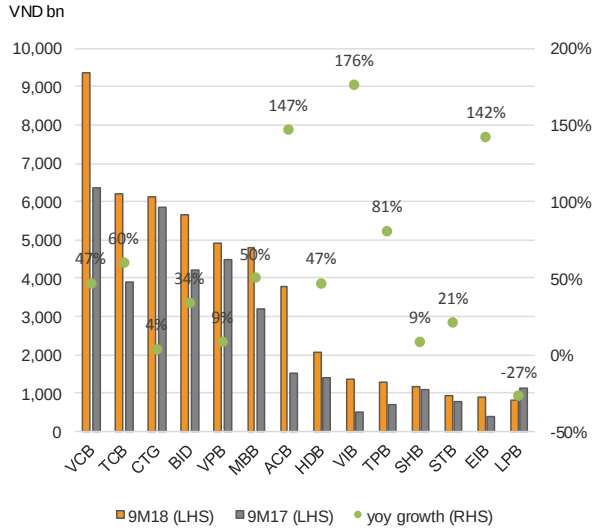
In the beginning of 2018, State Bank of Vietnam (SBV) capped local banks' credit growth at 14%, while setting a 17% common growth target for the whole banking system. System-wide credit growth expanded by 14% at 2018-end, which was the lowest growth rate in the past four years. With GDP growth in Vietnam reaching 7.1% in 2018, the fastest pace in eleven years, SBV has shifted its focus to curbing inflation, which was 3.54% in 2018, below the government target of 4% but within "striking" distance of the target. Under a directive issued in Aug 2018, the SBV refused to lift credit growth limits it imposed on individual banks for the year, even though some banks (eg: LPB, VCB, HDB, TPB) were approaching the full-year credit growth quota. Among those banks, LPB had to revise down its FY18 business targets as the bank was not allowed to expand its credit growth room as had been expected by management.

Figure 68: 9M18 loan & deposit YTD growth among banks



Source: VNDIRECT, Banks

Figure 69: Many banks posted robust net profit growth in 9M18



Source: VNDIRECT, Banks

Robust earnings growth on the back of Net interest margin (NIM) expansion and improving Cost-to-income ratio (CIR)

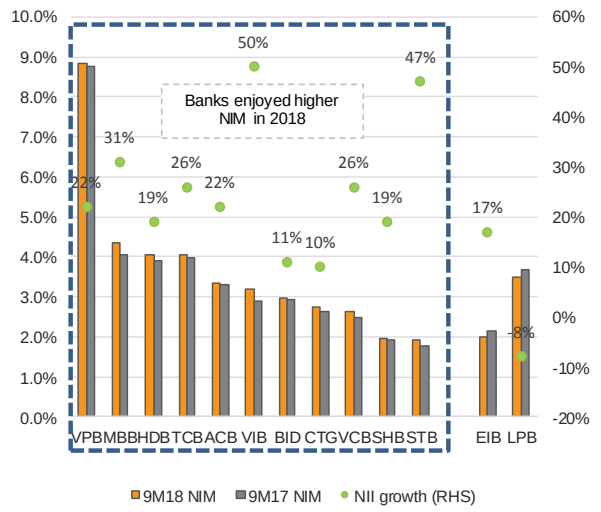
We estimate that the top-14 listed banks posted a robust increase of 39.0% yoy in aggregate net profit for 9MFY18. Aggregate Net interest income (NII) grew by 20% yoy as moderating loan growth was offset by a 30bps NIM expansion (3.5% in 9MFY18 vs. 3.2% in 9MFY17). NIM among top-14 listed banks have gradually expanded over time, reflecting a changing asset mix towards higher yielding individual and Small and Medium Enterprise (SMEs) segments.

9MFY18 aggregate fee income of top-14 listed banks also enjoyed strong growth of 27.0% yoy, albeit from a low base, as banks in 2018 started to hike their service fees (cash withdrawals, internet banking, money transfer etc.) as well as diversify their income sources through new businesses like bancassurance. However, fee income contribution still has plenty of room to grow as it only contributed

around 9.2% to banks' total operating income in the first nine months of the year.

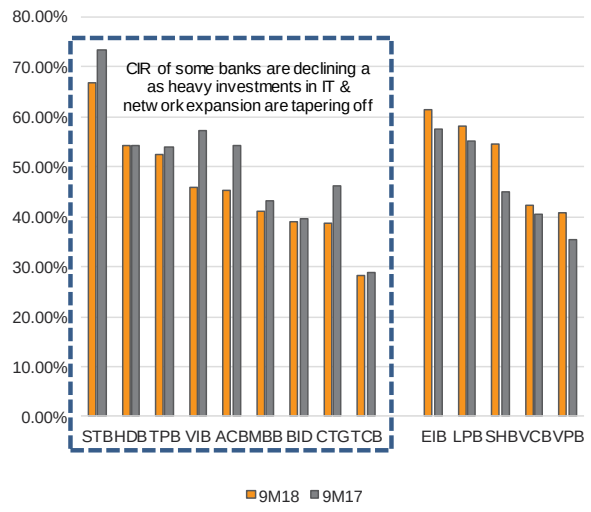
Aggregate CIR of top-14 listed banks continued to fall from 43.3% in 9MFY17 to 40.9% in 9MFY18 with better cost control and strong top-line growth driven by interest and fee income which boosted operating leverage. We believe Vietnam banks' heavy legacy investments in IT and network expansion are tapering off. We view this recent plunge in the CIR as the twin impact of a normalisation of IT investments and the pay-off from recent IT investments in terms of lifting operating efficiency.

Figure 70: NIM & NII growth by bank



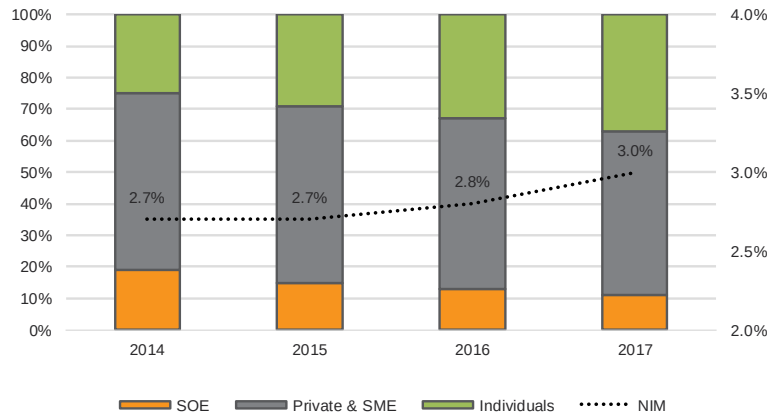
Source: VNDIRECT, Banks

Figure 71: CIR by bank



Source: VNDIRECT, Banks

Figure 72: Systemwide NIM has gradually expanded with a change in lending mix

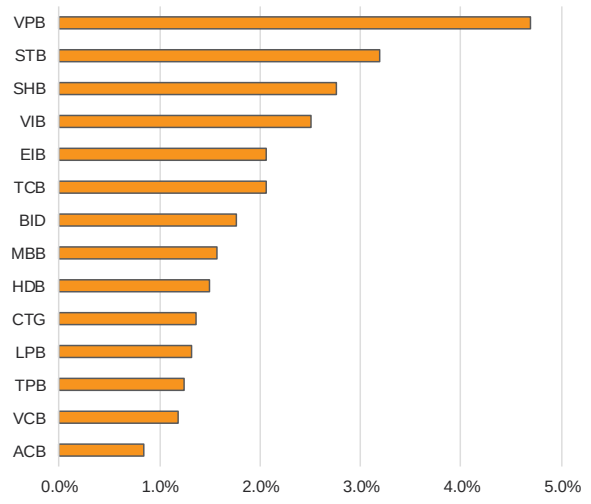


Source: SBV, VNDIRECT

Asset quality remained stable while the tail-end of a heavy provisioning cycle boosted loan loss buffers

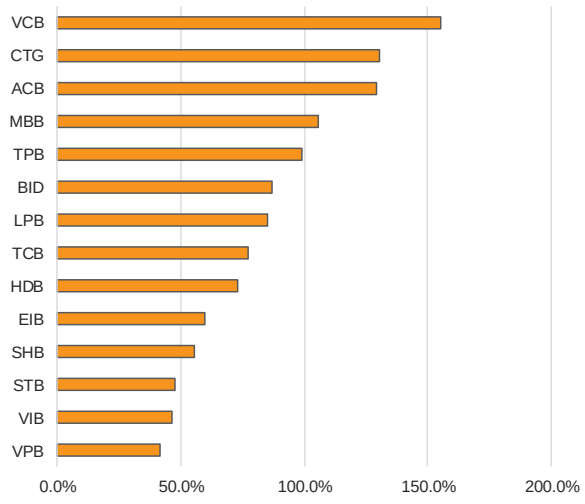
According to the recent report of the National Finance Supervisory Committee (NFSC), the system-wide NPL ratio is estimated to be contained at 2.4% by FY18-end, slightly lower than FY17's 2.5% level. Meanwhile, system-wide loan loss coverage ratio (LLR) improved to 78.2% at FY18-end from 65.4% at FY17-end.

Figure 73: NPL ratio among banks by end-Sep FY18



Source: VNDIRECT, Banks

Figure 74: LLR among banks by end-Sep FY18



Source: VNDIRECT, Banks

Figure 75: Aggregate top-14 listed banks' 9MFY18 results summary

	9MFY18	9MFY17	*change yoy*		9MFY18	9MFY17	*change yoy*
NP yoy growth	39.0%	30.1%	*8.9%*	NIM	3.5%	3.3%	*0.2%*
NII yoy growth	19.7%	15.0%	*4.7%*	CIR	40.9%	43.3%	*-2.4%*
NII/TOI	76.9%	79.2%	*-2.3%*	Annualized credit cost	1.37%	1.43%	*-0.06%*
Loan yoy growth	16.8%	20.0%	*-3.2%*	LLR	78.0%	65.0%	*13.0%*
Deposit yoy growth	13.8%	15.0%	*-1.2%*	NPL	1.8%	1.7%	*0.1%*

Note: 14 listed banks accounted for 63.4% of system commercial banks' total asset.

Source: VNDIRECT, Banks

2019 OUTLOOK: GROWTH TO MODERATE FROM A CYCLICAL PEAK

Credit growth expected to cool in 2019 but there is still ample room for retail lending expansion

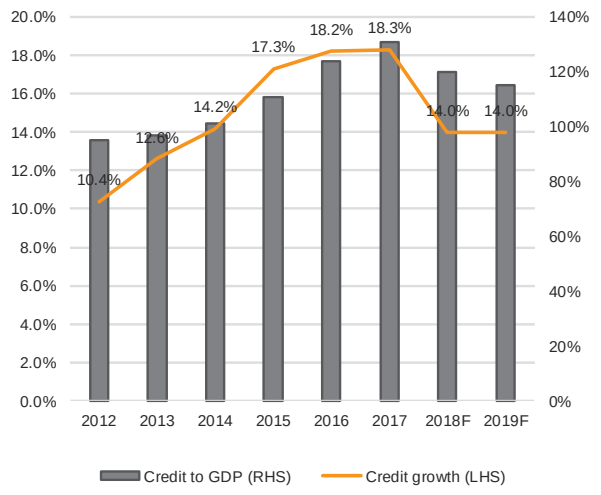
We expect Vietnam might be able to pursue 14% - 15% credit growth during 2019-2020 based on the following factors:

- Inflation in Vietnam has picked up again, with the Consumer Price Index (CPI) inflation accelerating by 3.6% in 9M2018 from 3.5% in 2017. Policymakers managed to contain inflation below the "comfort level" of 4% thanks to postponements in the planned power price and environmental tax hikes, a tightening of credit growth and helped in no small measure by the recent slump in oil prices. With GDP growth for 2018 having accelerated to breach the 7% level, we believe that inflation control will be the government's priority in 2019.
- The credit supply in 2019 will also be restricted due to the central bank's new regulations which call for an increase in the risk weighting of real estate loans in the banking system from the current 200% to 250% from early next year. A regulation on reducing the proportion of short-term funds to medium and long-term loans outstanding at banks from the current 45% to 40% from the beginning of 2019 will also impact liquidity.
- We observed that all central banks in the ASEAN-4 group of countries started to tighten their respective monetary policies in

2019, in the light of tighter global financial conditions spurred by Fed rate hikes and a reversal of Quantitative Easing (QE) and consequent US dollar strength.

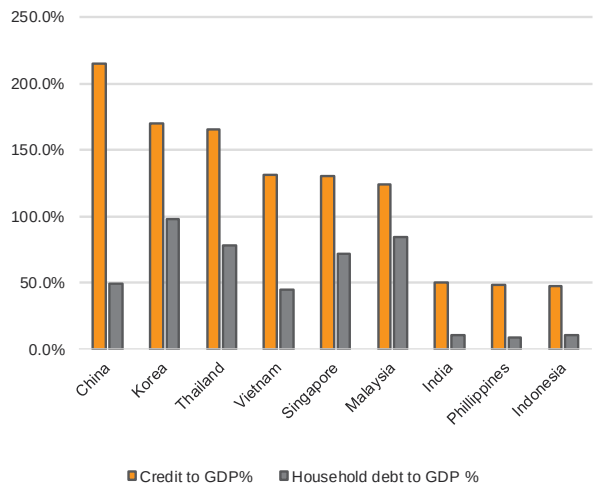
- Credit penetration of Vietnam is high relative to other economies.

Figure 76: Credit growth started to slow down in 2018



Source: SBV,VNDIRECT

Figure 77: Regional credit penetration as of end-2017

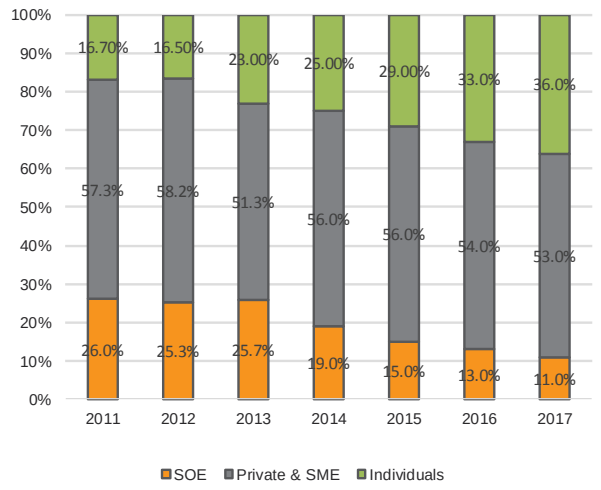


Note: Credit to GDP of India, Malaysia are as of 2016)
Source: CEIC, World Bank,VNDIRECT

However retail lending still has room for growth

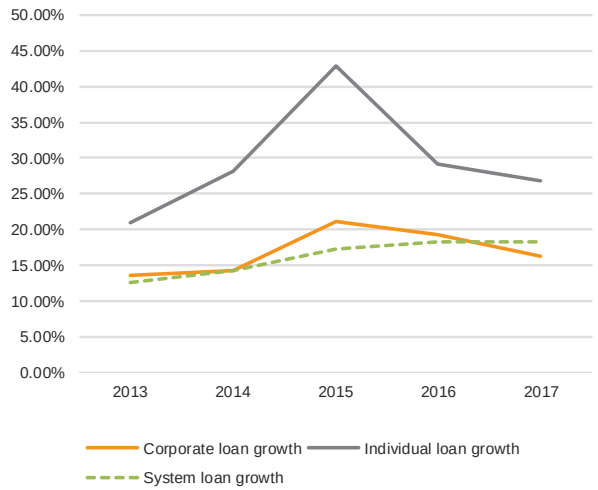
One positive change from the previous lending boom is that credit demand now is fuelled by households and private corporates, including SMEs, whereas in the past, a significant portion of the new credit went to the real estate and State-Owned Enterprise (SOE) sectors. The share of total credit to SOEs decreased sharply to 11% in FY17 from 25-26% in FY11-13. We believe this has been greatly aided also by the progress on privatisation as several SOEs have equitised and are now classified as private companies. However, the strong rise in lending to individuals has clearly been an important driver for system-wide loan growth and the aforementioned change in system-wide lending mix.

Figure 78: Credit allocation by type of borrower



Source: VNDIRECT, Banks

Figure 79: Individual lending has been a key driver of system-wide loan growth



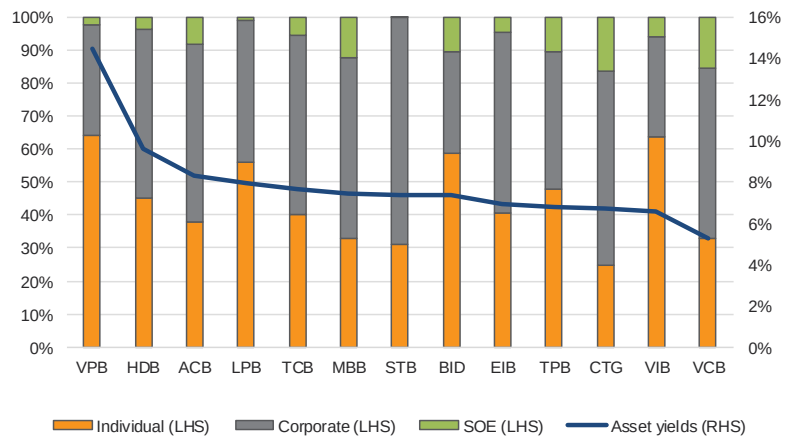
Source: VNDIRECT, Banks

Retail banking in Vietnam (defined to include lending to individuals and SMEs) only took-off in 2015, and in this early stage of retail banking evolution, banks are differentiating themselves by launching more sophisticated products such as cash and liquidity management tools for SMEs or innovative wealth management products incorporating new asset classes. We believe, in the near future, banks will have opportunities to cross-sell more fee-based products such as bancassurance and credit cards to their existing retail customer base.

We still see room for further growth in the private corporate and consumer sectors. On the consumer side, household credit penetration stood at around 44.7% of GDP as at Dec 2017 (source: CEIC, World Bank), still low relative to countries such as Thailand (78%) or Malaysia (84%) which have similar levels of headline credit penetration to Vietnam (165% and 124%, respectively versus close to 130% for Vietnam). On the private corporate side, we note that new business registrations continued to grow by 16% yoy in FY18 while business closures decreased by 5% yoy in the same period; while we do not have data on private corporate credit penetration in Vietnam, we believe it is far lower than the regional average.

However, the key to winning in the retail banking game is service and customer-focused sales. Distribution and sales capabilities are therefore critical for banks to win in this fast growing segment. **As such, banks with bigger branch networks and a larger customer base are positioned to outperform. We believe VCB and MBB meet this criteria.**

Figure 80: Banks with large exposure to individual and private corporate lending are able to enjoy higher asset yields (2017)



Source: Stoxplus, VNDIRECT

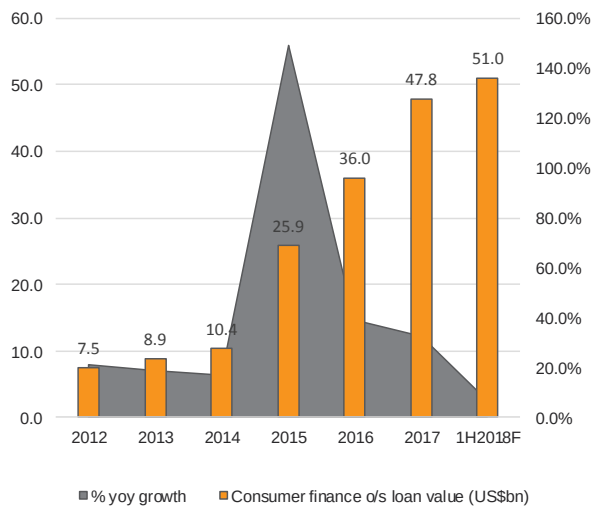
Is consumer finance still attractive? We see long-term potential

The consumer lending industry enjoyed a robust CAGR of 44.8% in terms of outstanding loans over the period 2012 - 2017. This has largely been driven by favourable demographics, rising urbanisation and incomes and increased levels of home, car, and durable goods ownership and demand.

However, consumer lending started to cool down in 1H2018 amid greater regulatory scrutiny of consumer finance operations. In April 2018, SBV requested consumer finance institutions to review their internal regulations, ensure that the staff follow due process and improve the quality of recruitment and staff evaluation. Regulations on stringent process review and staff quality control requirements have

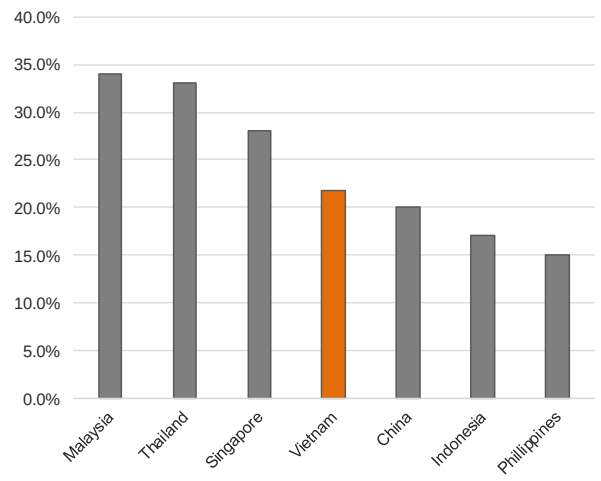
raised operating expenses of consumer finance companies and curtailed loan growth. By end-Jun 2018, consumer lending growth hovered at 6.7% ytd, even lower than total loan growth of commercial banks. Sluggish lending growth has dampened consumer finance companies' profitability. In 1H18, FE Credit, a subsidiary popularly dubbed as 'the golden egg-laying goose' of parent company VPB, only contributed 36% to the bank's consolidated net profit, down from 50% in the previous year.

Figure 81: Consumer finance: a marked deceleration



Source: Stoxplus, VNDIRECT

Figure 82: Regional consumer credit penetration (2017)



Source: Stoxplus, VNDIRECT

We believe Vietnam's consumer finance market is still in its infancy with an undiversified product portfolio and low credit card penetration implying that lots of "low-hanging fruit" remain to be picked. Thus, consumer finance still has ample room for NIM expansion even if lending rates come under some scrutiny, going forward.

Firstly, consumer finance is helping support the rise in expenditure on house, car and durable goods, thereby boosting consumption and having a huge multiplier effect across the economy. Given that this sector is improving access to credit and supporting consumption for the low-to-middle income segment of the population, policymakers would have an interest in continuing to use it as a tool to support the government's development agenda.

Secondly, consumer loans in Vietnam accounted for 17% of total outstanding loans by end-FY17, of which outstanding loans by finance companies (non-bank) amounted to 8% (the figure is 34% in ASEAN-5 and 20% in China). Total consumer credit penetration (including regular bank lending and non-bank lending) in Vietnam was estimated at 22% of GDP, still lower than regional peers. We believe consumer finance still has room to grow from its current low base penetration.

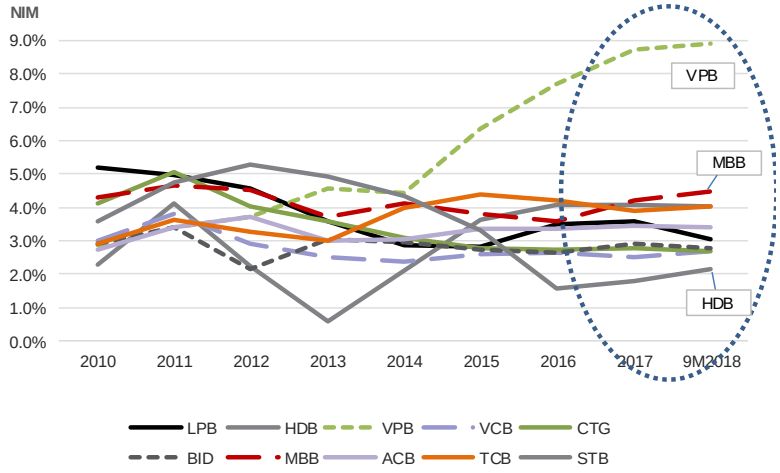
Modest NIM expansion at best as a continued rise in blended asset yields is countered by rising cost of funds

NIM improvements are critical for Vietnamese banks' profitability, especially when loan growth is moderating, because net interest income (NII) accounts for around 80% of Total operating income (TOI), across the system. We therefore acknowledge the shift in asset mix towards higher yielding consumer and SME loans as a positive

development for banks as reflected in rising asset yields across the board over the past few years. However, higher asset yields might be partially offset by a few factors including more stringent regulations on funding structures and rising deposit rates on the back of higher competition for longer-term retail deposits.

Among listed banks, VPB, HDB and MBB have enjoyed the fastest NIM expansion over the past few years because of their recent aggressive push into retail lending and consumer finance.

Figure 83: NIM expansion on the back of changing loan mix

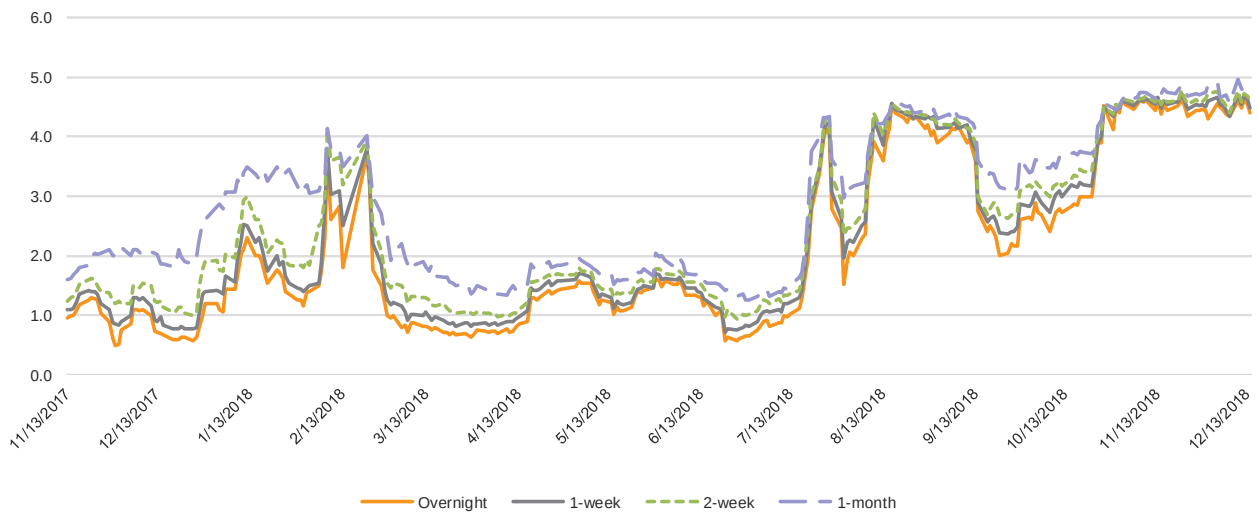


Source: VNDIRECT, Banks

On the regulatory front, under the new rules which will take effect on 1 Jan 2019, the risk weighting for interbank loans, deposits in other financial institutions and debt securities will increase to 50% from the current 25%. Thus we expect interbank borrowings to fall slightly in 2019-20. In addition, banks will not be allowed to use more than 40% of their short-term funds for loans with maturities longer than 12 months, a tighter cap than the current 45%. As of May 2018, according to the SBV, the ratios of short-term funds used for medium and long-term loans of SOE banks and private banks were 30.2% and 31.6%, respectively. This is still broadly in compliance with the new threshold but limits these banks' ability to lend to real estate developers, going forward (this is typically long-term lending and carries higher asset yields).

On the cost of funds side, since Jul 2018, deposit rates across the board have inched up by 100 – 150bp from the cyclical lows seen in May 2018. **We believe the deposit rate is likely to increase over 4QFY18 - FY19, creating headwinds for NIM expansion. We see two factors that could continue to put upward pressure on deposit rates: rising competition for deposits and rising policy rates.**

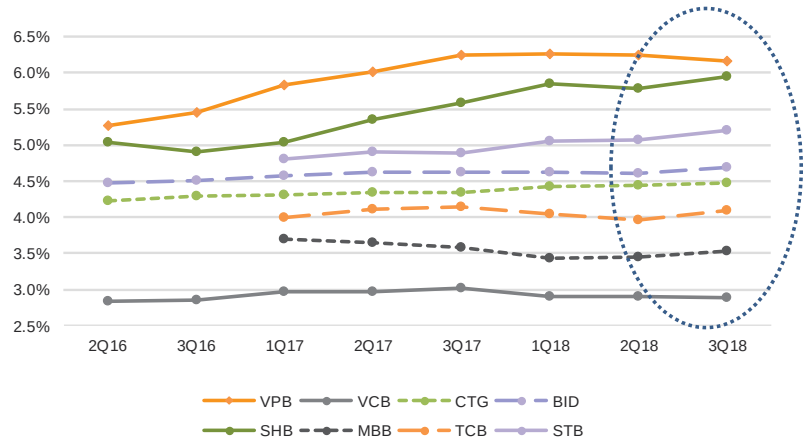
Figure 84: Interbank interest rates increased sharply across tenures (%)



Source: Bloomberg, VNDIRECT

However, we believe the government and SBV would like to keep lending rates stable on a yoy basis, in order to support the SME sector and economic growth, particularly in an environment of slowing global economic growth which could ultimately create headwinds for Vietnam's export growth. Thus, the pass-through of the rise in deposit rates to lending rates is unlikely to be dramatic.

Figure 85: Quarterly cost of funds likely to pick up on the back of rising deposit rates

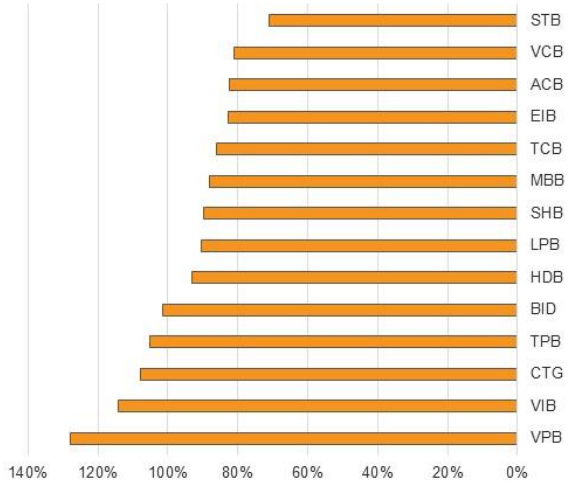


Source: VNDIRECT, Banks

We expect industry-wide FY19 NIM to improve modestly or even stay flat despite improving asset mix, but the NIM trend will be rather uneven across individual banks as banks' sensitivity to competition for deposits and need for funding mobilisation varies widely. We expect:

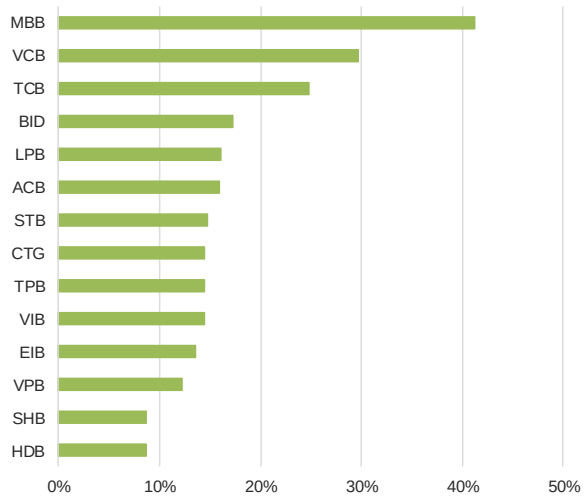
- banks with a lower LDR (below 90%) to have better funding flexibility (e.g. VCB and ACB);
- banks with better deposit franchises to be less sensitive to competition (SOCBs with a wider branch network do look better in this regard); and
- banks with high CASA ratio (e.g. VCB, MBB and TCB) to better manage rising funding costs.

Figure 86: LDR among banks as of end-Sep FY18



Source: VNDIRECT, Banks

Figure 87: CASA among banks as of end-Sep FY18

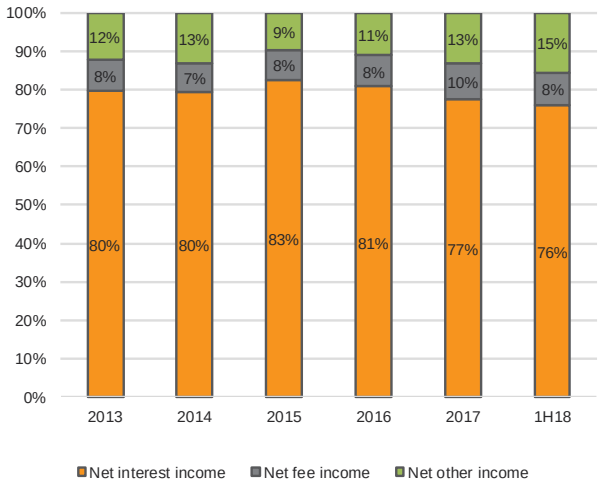


Source: VNDIRECT, Banks

Non-interest income growth to slow but stay robust

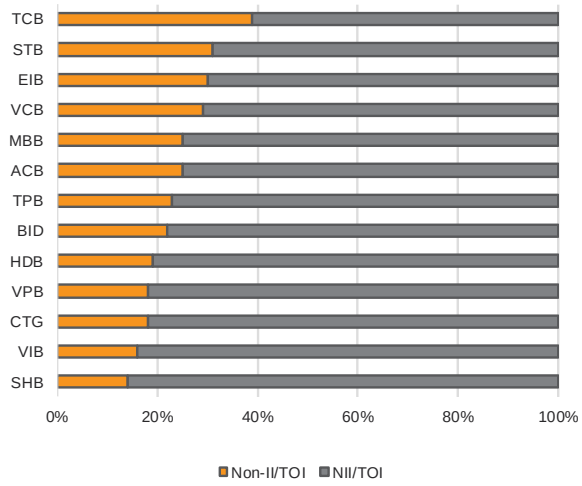
We forecast non-interest income (Non-II) of banks under our coverage to grow by 28.5% yoy in 2018 and 11.1% yoy in 2019, driven by strong growth in fee income from bancassurance and bad-debt recovery, beyond traditional banking fee-based services such as payment, guarantees, credit cards, etc.

Figure 88: System-wide Non-II/TOI ratio



Source: Stoxplus, VNDIRECT

Figure 89: Non-II/TOI in 9MFY18



Source: VNDIRECT, Banks

Bancassurance will become the new growth engine

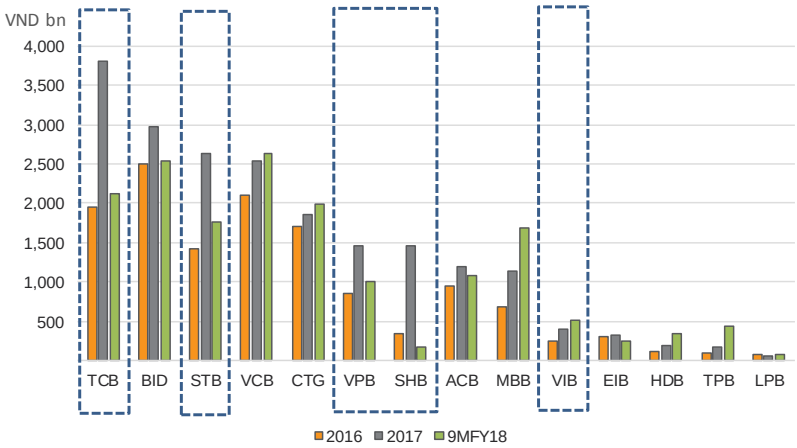
Over 2017-2018, the market witnessed a wave of banks signing contracts to be exclusive agents for insurance partners, like TCB with Manulife, STB with Dai-ichi Life, CTG with Aviva, VPB with AIA, NCB with Prevoir, and so on, while others are actively selling life insurance products of multiple insurers concurrently on a non-exclusive basis. Banks are also packaging their credit products with non-life insurance products, e.g. compulsory property and casualty insurance, goods on

transportation insurance and so on, to offer their customer network to potential and existing partners, and target a higher proportion of bancassurance fees in total fee income.

Up to now, 18 out of 29 life insurance companies and 9 out of 14 non-life insurance companies are implementing bancassurance into their banking practices. By the end of 2017, the value of new insurance gross premiums written and distributed via the banca channel rose to around 10% of total gross premiums written, up from just 1% in 2013. This is still low compared to the level of 30-50% witnessed in neighbouring markets such as Thailand, Indonesia, Hong Kong, Singapore, etc. We believe that bancassurance premiums will grow at 30-40% yoy in the coming years, and the proportion of premium written value distributed via banca will grow to 12% in 2018 and 14% in 2019. Bancassurance fees will therefore become one of the key drivers of non-NII growth of banks.

Landmark exclusive bancassurance partnerships in 2017-2018

Figure 90: A few banks recorded strong fee income growth during 2017-2018 with extraordinary gains from exclusive bancassurance partnerships



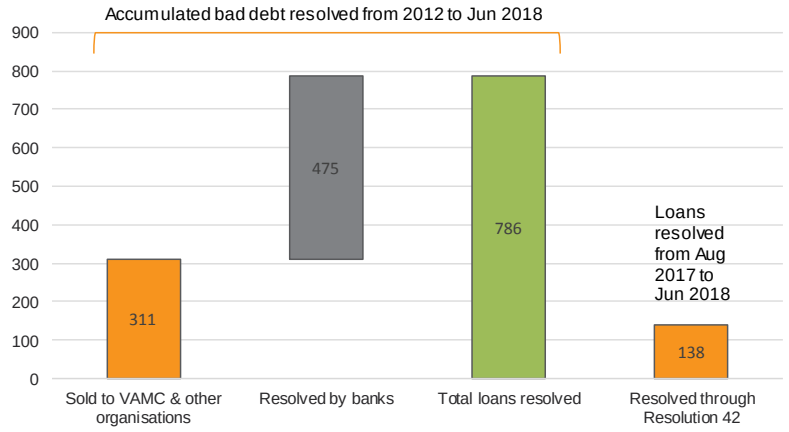
Source: VNDIRECT, Banks

Improving bad debt recovery could spring earnings surprise

Since Aug 2017, the Government issued Resolution 42/2017/QH14 on piloting bad debt settlement of credit institutions to provide thorough guidance on the procedures for recovery and repossession of collateral. The new legal framework confers lenders with more power in collecting collateral which could be considered as the first critical step to resolve legacy distressed assets. The new legal framework also provides incentives to encourage NPL trading, as it provides liquidity and helps price the assets through market mechanisms. It also sets a framework for a secondary debt trading market, which is high on the wish list of both foreign and domestic investors.

We believe the new resolution has removed previously existing legal impediments and that it will hasten the bad debt clean-up process. In addition, various banks, including VCB, MBB, CTG and VIB, have started to repurchase bad debt from Vietnam Asset Management Company (VAMC) to handle them in-house, signalling an improvement in their financial capacities and confidence in the new policy measures to streamline bad debt recovery.

Figure 91: Accumulated bad debt resolved from 2012 to Jun 2018 (VND tr)

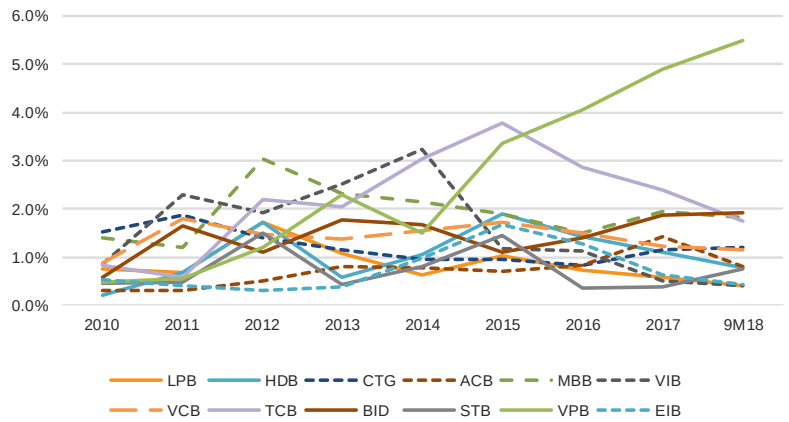


Source: VAMC, VNDIRECT

Credit costs are declining but NPLs will probably inch up

Credit costs will decline as more banks resolve their legacy problem assets thereby leading to a tapering off of VAMC bond provisioning. Credit costs associated with legacy problem loans have become manageable for most rated banks, with pre-provision income generated in 2018 exceeding the amount of VAMC bonds not covered by existing provisions. Heading into 2019, six banks (VCB, MBB, VIB, TCB, ACB, CTG) that have fully written off their VAMC bonds will post substantial improvements in their returns on tangible assets, with more banks to follow suit. We also see that some banks, including TPB and OCB, are likely to finish the VAMC bonds provisioning cycle in 2019.

Figure 92: Credit cost across the board have been declining since 2015



Source: VNDIRECT, Banks

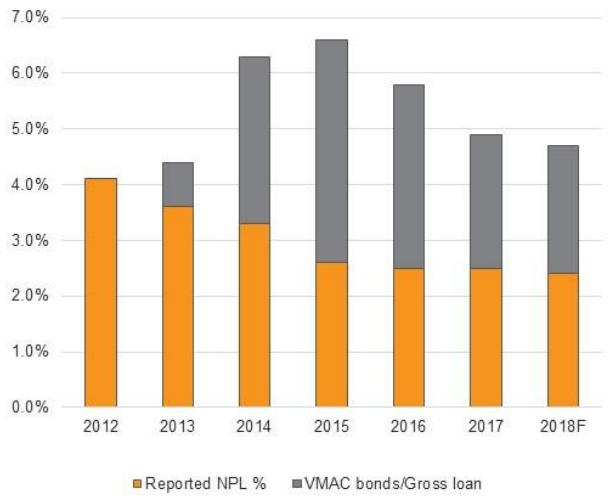
While the bad debt legacy of the past is being cleaned up in some banks, the formation of new NPLs will nevertheless continue. However, in contrast to the legacy loans of the past, which arose mainly from loans related to speculative activities, non-core businesses (i.e. banks, brokerage and property), and inefficient SOE investment, the formation of new NPLs today is more related to private investment and household consumption, which is especially true at retail-focused commercial banks. Therefore, we believe NPLs will be

the highest at banks with aggressive expansion especially in consumer finance lending, which is typically high-risk in nature, and lower at banks with more stringent lending criteria to both corporate and retail clients and less aggressive expansion in lending to individuals.

In addition, the SBV has tightened banks' corporate bond purchases to swap debt through issuing Circular No.15/2018/TT-NHNN which became effective since Aug 2018. Under this Circular, credit organisations and foreign bank branches are not allowed to purchase bonds issued by businesses with the purpose of restructuring their debt. We believe the issuance of bonds to swap debt is like a double-edged sword. However, the tightening of regulations on bond issuance to swap debt may cause a spike in the reported NPL ratio as the banks have to reassess and reclassify their corporate bad debt exposure.

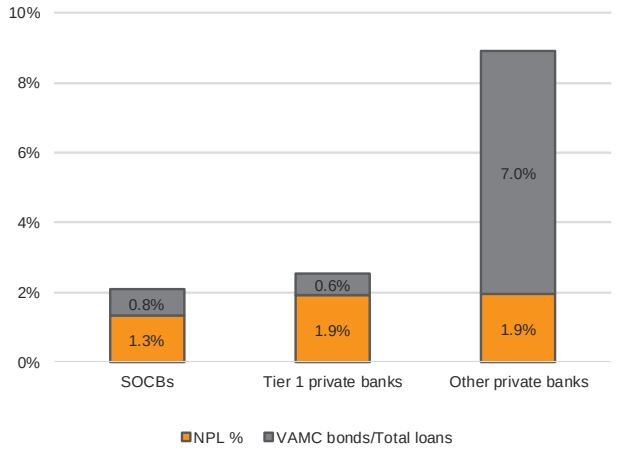
In our view, the reported NPL ratio of the whole sector will edge up slightly, but remain manageable at below 3%. By the end of 2018, the reported NPL ratio of the sector had declined to 2.4% (vs. 2.5% in 2017). Thus, the system-wide distressed asset ratio (including VAMC bonds) decreased to 4.7% at end-2018 from 4.9% at end-2017.

Figure 93: System-wide legacy distressed asset ratio



Source: SBV, VAMC, VNDIRECT

Figure 94: NPLs concentrated in small, privately-owned commercial banks



Source: SBV,VNDIRECT

BANKING SECTOR STOCK PICKS: VCB & MBB

Figure 95: Forecasted ratio of banks under our coverage (1)

	Loan Growth			Deposit Growth			Net Interest Income Growth			Non Interest Income Growth			Fee Income Growth		
	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F
ACB	15.0%	15.0%	15.0%	13.0%	14.0%	15.0%	19.3%	16.0%	17.5%	3.5%	34.5%	6.7%	25.0%	25.0%	25.0%
MBB	15.0%	15.0%	15.0%	9.0%	12.0%	14.0%	26.3%	15.7%	16.9%	62.7%	15.7%	17.3%	85.0%	25.0%	25.0%
VCB	15.0%	15.0%	15.0%	14.0%	14.5%	14.5%	22.7%	17.6%	18.0%	40.2%	8.8%	11.3%	35.0%	30.0%	25.0%
VPB	16.5%	15.5%	15.5%	20.0%	19.7%	18.8%	21.0%	16.0%	16.5%	21.5%	19.9%	13.8%	2.0%	20.0%	20.0%
LPB	14.0%	15.0%	15.0%	16.0%	16.0%	16.0%	-0.1%	14.6%	18.1%	n/m	n/m	n/m	45.0%	20.0%	15.0%
Average	*15.1%*	*15.1%*	*15.1%*	*14.4%*	*15.2%*	*15.7%*	*17.9%*	*16.0%*	*17.4%*	*32.0%*	*19.7%*	*12.3%*	*38.4%*	*24.0%*	*22.0%*
Median	*15.0%*	*15.0%*	*15.0%*	*14.0%*	*14.5%*	*15.0%*	*21.0%*	*16.0%*	*17.5%*	*30.8%*	*17.8%*	*12.5%*	*35.0%*	*25.0%*	*25.0%*

Source: VNDIRECT

Figure 96: Forecasted ratio of banks under our coverage (2)

	Asset yields			Cost Of Funds			NIM			CIR			Provision Charge/Avg Cust Loans		
	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F
ACB	8.4%	8.5%	8.6%	5.0%	5.1%	5.2%	3.5%	3.6%	3.7%	46.0%	47.0%	47.0%	0.4%	0.4%	0.4%
MBB	7.8%	8.0%	8.3%	3.6%	3.6%	3.7%	4.5%	4.7%	4.9%	41.5%	43.0%	43.0%	1.5%	1.4%	1.4%
VCB	5.1%	5.2%	5.4%	2.7%	2.8%	2.8%	2.5%	2.6%	2.7%	42.0%	42.0%	42.0%	1.2%	1.2%	1.2%
VPB	14.5%	14.6%	14.7%	6.2%	6.3%	6.3%	8.9%	9.0%	9.1%	35.0%	35.0%	35.0%	5.5%	5.4%	5.3%
LPB	8.2%	8.4%	8.6%	5.2%	5.3%	5.5%	3.2%	3.3%	3.4%	63.0%	64.0%	63.0%	0.4%	0.4%	0.4%
Average	*8.8%*	*8.9%*	*9.1%*	*4.5%*	*4.6%*	*4.7%*	*4.5%*	*4.6%*	*4.8%*	*45.5%*	*46.2%*	*46.0%*	*1.8%*	*1.8%*	*1.7%*
Median	*8.2%*	*8.4%*	*8.6%*	*5.0%*	*5.1%*	*5.2%*	*3.5%*	*3.6%*	*3.7%*	*42.0%*	*43.0%*	*43.0%*	*1.2%*	*1.2%*	*1.2%*

Source: VNDIRECT

Figure 97: Forecasted ratio of banks under our coverage (3)

	ROAA			ROAE			Total CAR (%)			LLR			Gross NPL Ratio (%)		
	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F
ACB	1.7%	1.7%	1.7%	27.0%	24.7%	22.4%	12.2%	12.6%	12.8%	130.5%	131.4%	131.9%	0.8%	0.9%	1.0%
MBB	1.8%	1.9%	2.0%	19.6%	19.2%	19.3%	10.9%	11.1%	11.4%	103.5%	103.4%	102.0%	1.6%	1.8%	2.0%
VCB	1.1%	1.1%	1.2%	20.5%	20.2%	20.0%	10.8%	11.2%	11.4%	153.3%	164.3%	172.6%	1.2%	1.3%	1.4%
VPB	2.4%	2.5%	2.6%	22.2%	22.3%	22.0%	13.8%	13.4%	13.9%	50.8%	53.0%	54.0%	3.7%	3.8%	3.9%
LPB	0.6%	0.6%	0.7%	10.4%	11.0%	13.0%	10.5%	9.9%	9.6%	121.6%	122.3%	120.6%	0.9%	0.9%	0.9%
Average	*1.5%*	*1.6%*	*1.6%*	*19.9%*	*19.5%*	*19.3%*	*11.6%*	*11.7%*	*11.8%*	*111.9%*	*114.9%*	*116.2%*	*1.6%*	*1.8%*	*1.9%*
Median	*1.7%*	*1.7%*	*1.7%*	*20.5%*	*20.2%*	*20.0%*	*10.9%*	*11.2%*	*11.4%*	*121.6%*	*122.3%*	*120.6%*	*1.2%*	*1.3%*	*1.4%*

Source: VNDIRECT

Figure 98: Banking peer comparison (price as of 11 Jan 2019)

Banks	Ticker	Market cap (VND bn)	TTM ROA %	TTM ROE %	FY18F P/B (x)	FY18F P/E (x)	FY19F P/B (x)	FY19F P/E (x)
Vietcombank	VCB	204,730	1.2%	21.0%	3.1	20.9	2.7	18.2
BIDV	BID	109,057	0.7%	16.1%	2.0	18.2	1.7	15.3
Techcombank	TCB	90,911	3.0%	21.7%	1.8	10.9	1.5	9.2
Vietinbank	CTG	70,000	0.7%	11.5%	1.0	10.1	0.9	7.7
VPBank	VPB	46,924	2.4%	22.2%	1.4	6.5	1.2	5.6
Military Bank	MBB	41,589	1.6%	16.2%	1.3	7.5	1.1	6.5
Asia Commercial Bank	ACB	36,043	1.5%	24.6%	1.7	7.4	1.3	6.2
HDBank	HDB	28,645	1.3%	15.6%	1.8	11.3	1.6	9.5
Tien Phong Bank	TPB	17,777	1.2%	18.2%	1.7	8.6	1.4	7.5
LienViet Post Bank	LPB	6,930	0.6%	10.6%	0.7	7.5	0.6	6.5
Average			**1.4%**	**17.8%**	**1.6**	**10.9**	**1.4**	**9.2**
Median			1.2%	17.2%	1.7	9.4	1.4	7.6

Source: VNDIRECT, Bloomberg

We are generally neutral on the banking sector in 2019 amid tightening credit policy, rising interest rates and the potential spillover from global economic risks. However, we believe each bank has its own unique combination of challenges and opportunities. We prefer banks with the following characteristics: 1) good exposure to and strong ability to capture the opportunities from retail lending and non-interest income activities; 2) well-positioned to offset the challenges from rising funding costs and lower credit growth room; 3) good asset quality to buffer against the risks of rising system-wide NPL ratio. Our top picks in the banking sector are VCB and MBB.

Military Bank (MBB VN, ADD, TP:VND31,100): MBB has actively re-oriented its loan book from corporate lending to retail lending in the past few years but the individual loan book only made up 36.4% of the total loan book as of end-3Q18; still lower than the retail bank peer average of 54.0%. We believe there is room for further expansion of the retail lending business. In addition, the consumer finance subsidiary – MCredit – will help the bank penetrate into the lucrative business of unsecured lending, a sector that is expected to see explosive growth over the medium-to-long term. The expansion of retail lending at the parent bank and the growing contribution of MCredit to the consolidated loan book will improve NIM. On the non-interest income side, MBB is executing on a multi-pronged strategy to boost its fee income franchise. We project 25.0% CAGR in fee income over FY18-20F thanks to banking digitalisation, bancassurance and cross-selling of products through its partner network. At the current share price, MBB is trading at FY18F P/B of 1.3x, an 23.7% discount to the peer average P/B.

Vietcombank (VCB VN ADD, TP:VND73,800]: We believe VCB is strongly positioned to capture growth opportunities in retail lending, thanks to its position as the No.1 card issuer, its extensive network and large SOE client base. With a retail loan/total loan ratio of 45% and a pure loan/deposit ratio (LDR) of 80% as of end-3Q18, there is still room for NIM improvement as VCB aims to increase the weight of the retail loan book to 50% and increase the pure LDR to 85% and has the ability to meet Basel II capital adequacy requirements through proceeds from its recent private placement (3% stake) and future subordinated debt issuance. On the non-interest income franchise, there is potential for developing a new fee income stream as well as extraordinary income through a potential exclusive bancassurance deal. In addition, the divestment from MBB and EIB in 4Q18 brought VCB one-time gains worth approximately VND1,000bn in FY18.

Other banks under our coverage

Asia Commercial Bank (ACB HNX, ADD,TP:VND39,800): ACB is a well-established retail bank with a strong retail customer base. Being the first mover in retail banking, ACB has built its reputation as one of the leading retail banks, with the third largest market share in both individual lending and individual deposits among private commercial banks as of end-FY17. The bank's earnings during FY12-17 were dragged down by provisioning for legacy bad debt, but it resolved all legacy debt in FY17. As a result, there will be a reduction of credit costs going forward. Solid growth in core income and a drop in provision expenses helped ACB to achieve the highest ROE of the sector at 24.6% in 9M18. We like ACB for: 1) its established expertise in retail banking which is an advantage in penetrating the new target segments of affluent and lower mass market customers; 2) good asset quality with the lowest level of distressed assets in the sector at 0.9% of total loans as of end-9M18.

VPBank (VPB VN, ADD, TP:VND26,100): Making a timely bet on the consumer lending boom in Vietnam with an aggressive business expansion strategy, FE Credit – VPB's subsidiary has become the top player in this industry, with 48% market share in FY17. The high-yielding business has helped VPB achieve the second highest ROE in the sector at 22.2% in 9M18. After a few years of high growth, loan growth at both the parent bank and FE Credit decelerated in FY18 following the SBV's stricter control of credit growth. However, we believe loan growth will recover in FY19F after the bank completes the restructuring of its loan portfolio. Meanwhile, the bank has aggressively focused on technology changes to capture opportunities in digital banking, micro SME banking and Fintech. Although the bank faced strong headwinds from a loan growth slowdown, more regulatory scrutiny of its loan recovery practices and a sharp rise in its NPL ratio in FY18, we believe the lacklustre performance in FY18 has been priced in, with FY18F P/B of 1.4x, a 17.7% discount to the industry average.

Lien Viet Postbank (LPB VN, ADD, TP:VND12,900): LPB is aggressively building an extensive network with around 200-230 new transaction offices per year until FY20F. Network expansion has weighed on NIM but we expect the benefits of a larger network to materialise in the medium term as there is a time lag between deposit mobilisation and lending at the new transaction offices. We like LPB for the following reasons: 1) LPB will be the only bank with an extensive network in every district in Vietnam, even in rural areas; 2) LPB is seeking an exclusive bancassurance agreement for 15-20 years, which will bring sizeable upfront agency fees and a new income stream from insurance commissions; 3) LPB is considering migrating to HOSE which will improve liquidity and transparency; and 4) LPB's stock carries a high dividend yield of 11.4%. At the current price, LPB is trading at a FY18F P/B of 0.7x, a 60.0% discount to the industry average.

MILITARY BANK (MBB)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND19,250	VND31,100	3.1%	ADD	FINANCIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019
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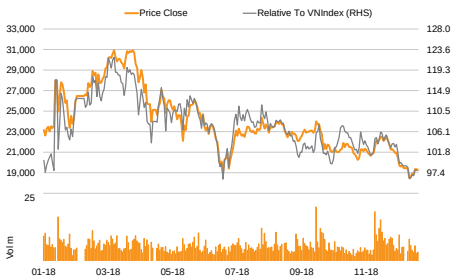
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	30,924
52w low (VND)	18,500
3m Avg daily volume (shares)	5.7m
3m Avg daily value (VNDmn)	119,588
Market cap (VNDbn)	41,589
Outstanding shares (m)	2,160
Free float (%)	20
TTM P/E (x)	8.8
Current P/B (x)	1.3

Ownership

Viettel	14.6%
SCIC	9.7%
Vietnam Helicopter Corporation	7.8%
Vietcombank	5.0%
Saigon NewPort Corporation	7.8%
Others	55.1%

Source: VNDIRECT

Solid earnings on improving NIM and strong fee income growth with huge room to continue to boost asset yields.

Continued shift towards retail lending supports NIM expansion. MBB has actively transformed itself from a wholesale to a retail bank with its individual loan book growing at a 33.0% CAGR over FY15-9M18. Individual loans made up 36.4% of the total loan book at end-9M18, still far below its retail bank peer average of 54.0%, leaving ample room for retail lending expansion at MBB. The new consumer finance subsidiary is another driver of NIM expansion, thanks to high-yield loan products and strong uptake off a low penetration base.

Dynamic strategy to boost fee income. We project 25.0% CAGR in fee income over FY18-20F with banking digitalisation, bancassurance and cross-selling of products through its partner network. The newly launched card products are initiatives to push payment fees. However, bancassurance will be the major driver for fee income growth as MBB just started distributing life insurance products of its subsidiary MB Ageas Life in FY17.

Prudent risk management evinced by a clean balance sheet. MBB applies the best-practice "three lines of defense" model in its risk management. MBB is also diligent in provisioning and loan write-offs, resulting in the fourth-lowest level of distressed assets in the sector as of end-9M18 (at 1.6% of total loans) and a high provision buffer, with end-9M18 loan loss reserves (LLR) of 106.0%.

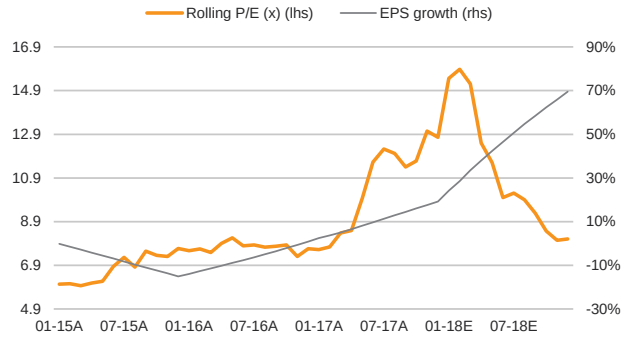
We project a net profit CAGR of 16.5% over FY18-20F, driven by 16.3% CAGR in net interest income on the back of a 15.0% loan CAGR and 39bp NIM expansion over the period. We also forecast a 25.0% FY18-20F CAGR in fee income and 7.9% FY18-20F CAGR in other non-interest income. We project a deceleration in provision expense CAGR from the 17.2% seen in FY14-17 to 9.8% in FY18-20F as the provision cycle tapers off.

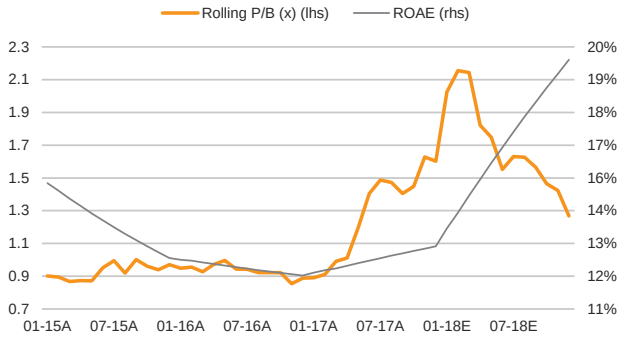
Key risks: Upside risks stem from the divestment from MBLand Holdings and Military Insurance Joint Stock Company. Downside risks are increased NPLs due to the higher risks inherent in retail lending and an imminent rise in interest rates.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	7,979	11,219	14,165	16,388
Net interest margin	3.5%	4.1%	4.5%	4.7%
Total operating income (bn)	9,855	13,867	18,475	21,375
Total provision charges (bn)	(2,030)	(3,252)	(3,004)	(3,212)
Net profit (bn)	2,912	3,520	5,995	6,882
Net profit growth	16.7%	20.9%	70.3%	14.8%
Adjusted EPS	1,293	1,517	2,572	2,952
BVPS	11,846	13,039	15,338	17,924
ROAE	12.1%	13.2%	19.6%	19.2%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**11,219**	**14,165**	**16,388**
Non interest income	**2,648**	**4,309**	**4,987**
Total operating income	**13,867**	**18,475**	**21,375**
Total operating costs	(5,999)	(7,667)	(9,191)
Pre-provision operating profit	**7,868**	**10,808**	**12,184**
Total provision charges	**(3,252)**	**(3,004)**	**(3,212)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**4,616**	**7,803**	**8,972**
Tax expense	(1,125)	(1,639)	(1,884)
Profit after tax	**3,490**	**6,165**	**7,088**
Minority interest	29	(170)	(206)
Net profit	**3,520**	**5,995**	**6,882**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	184,188	211,816	243,589
Loans to banks	53,497	54,567	57,296
Total gross loans	**237,686**	**266,384**	**300,885**
Securities - total	53,841	54,918	58,213
Other interest earning assets	6,805	6,941	7,358
Total gross IEAs	**298,332**	**328,243**	**366,456**
Total provisions	**(2,486)**	**(3,830)**	**(4,927)**
Net loans to customers	**182,062**	**208,354**	**239,051**
Total net IEAs	**295,847**	**324,414**	**361,529**
Cash and deposits	1,842	1,989	2,149
Total investments	1,077	1,164	1,257
Other assets	15,112	16,321	17,626
Total non-IEAs	**18,031**	**19,474**	**21,031**
Total assets	**313,878**	**343,887**	**382,560**
Customer deposits	220,176	239,992	268,791
Cds outstanding	6,022	6,323	6,639
Customer interest-bearing liabilities	226,198	246,315	275,430
Bank deposits	47,949	53,057	56,165
Broad deposits	274,147	299,372	331,596
Other interest-bearing liabilities	297	297	297
Total IBLs	**274,444**	**299,669**	**331,893**
Deferred tax liability			
Other non-interest bearing liabilities	9,832	9,480	10,138
Total non-IBLs	**9,832**	**9,480**	**10,138**
Total liabilities	**284,277**	**309,149**	**342,031**
Share capital	18,155	21,605	21,605
Additional paid-in capital	828	828	828
Treasury shares	0	0	0
Retained earnings reserve	5,977	7,495	13,081
Other reserves	3,209	3,209	3,209
Shareholders' equity	**28,170**	**33,137**	**38,723**
Minority interest	1,431	1,601	1,807
Total equity	**29,601**	**34,738**	**40,530**
Total liabilities & equity	**313,878**	**343,887**	**382,560**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	13.0%	9.0%	12.0%
Gross cust loan growth	22.2%	15.0%	15.0%
Net interest income growth	40.6%	26.3%	15.7%
Pre provision operating profit growth	38.5%	37.4%	12.7%
Net profit growth	20.9%	70.3%	14.8%
Growth in IEAs	23.3%	9.7%	11.4%
Share value			
Basic EPS (VND)	1,637	2,775	3,186
BVPS (VND)	13,039	15,338	17,924
DPS (VND)	600	600	600
EPS growth	19.2%	69.5%	14.8%

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	4.1%	4.5%	4.7%
Cost-income ratio	(43.3%)	(41.5%)	(43.0%)
Reported NPLs / gross cust loans	1.2%	1.6%	1.8%
Reported NPLs / net cust loans	1.2%	1.6%	1.8%
GP charge / average cust loans	1.9%	1.5%	1.4%
Total CAR	12.0%	10.9%	11.1%
Loan deposit ratio	81.4%	86.0%	88.4%
Margins and spreads			
Return on IEAs	7.3%	7.8%	8.0%
Cost of funds	3.5%	3.6%	3.6%
Interest return on average assets	3.9%	4.3%	4.5%
ROAE	13.2%	19.6%	19.2%

Source: VNDIRECT

VIETCOMBANK (VCB)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND55,200	VND73,800	1.4%	ADD	FINANCIALS

Outlook – Short term	Outlook – Long term	Valuation
Negative Neutral Positive	Negative Neutral Positive	Negative Neutral Positive

11 January 2019
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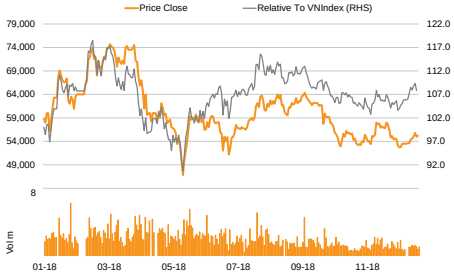
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	73,751
52w low (VND)	46,206
3m Avg daily volume (shares)	1.3m
3m Avg daily value (VNDmn)	69,881
Market cap (VNDbn)	204,730
Outstanding shares (m)	3,709
Free float (%)	7.9
TTM P/E (x)	20.8
Current P/B (x)	3.2

Ownership

State Bank of Vietnam	74.8%
Mizuho Corporate Bank	15.0%
GIC Private Limited	2.6%
Others	7.6%

Source: VNDIRECT

Solid core earnings growth with earnings from divestment and bancassurance deals creating uncaptured upside

Strongly positioned to penetrate the retail banking segment. VCB is the No.1 card issuer in Vietnam with 30% share of total credit cards in circulation and 44% share of Vietnam's credit card payment volume in 2017. This provides the bank a large retail customer base to cross sell other retail banking products, such as mortgages. In addition, VCB has an extensive network and large SOE client base (large number of employees), which facilitates the push into the retail and SME segments. The expansion into retail lending will boost NIM, in our view.

Well-regarded bank with best-in-class asset quality and strong deposit franchise. VCB is always considered the "safest bank" in the Vietnam banking system. As of end-9M18, VCB has the second lowest level of distressed assets at 1.2% of total loans and an LLR of 155.5%. VCB's funding mobilisation capability and liquidity are strong due to its leading deposit franchise with 10% system-wide deposit market share. It also benefits from depository relationships with SOE clients and plays an important role in the national payment system.

Successful private placement enhanced capital buffers. In Jan 2019, VCB announced it completed a 3% private placement to foreign investors at VND55,510/share to raise VND6,168bn of fresh capital. At this selling price, VCB was valued at 2.9x post-money 2018 book value. The new shares were bought by Mizuho and GIC, who now hold 15.0% and 2.6% stakes post issuance, respectively. We estimate the newly injected capital would increase its regular CAR by 90bp to ~ 12%. VCB was among the first three banks to apply Basel II in 2019.

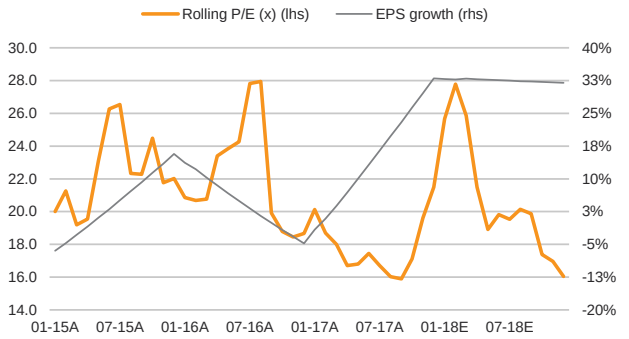
We expect VCB to sustain a net profit CAGR of 16.0% over FY18-20F, on the back of a 17.8% CAGR in net interest income driven by 15.0% loan CAGR and 22bp improvement in NIM; as well as a 10.0% CAGR in non-interest income.

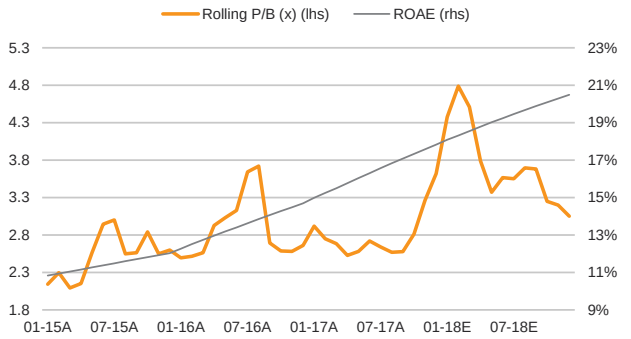
Key risks: Upside risks include the divestment from MBB and EIB, which brought VCB a gain of c.VND1,000bn in FY18. Medium-term upside risk would come from a potential exclusive bancassurance deal, worth up to US$1bn, which will benefit VCB with sizeable agency fees and a new income stream from insurance commissions.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	18,528	21,938	26,921	31,654
Net interest margin	2.6%	2.5%	2.5%	2.6%
Total operating income (bn)	24,880	29,403	37,385	43,038
Total provision charges (bn)	(6,406)	(6,198)	(6,718)	(7,726)
Net profit (bn)	6,832	9,087	11,996	13,816
Net profit growth	28.6%	33.0%	32.0%	15.2%
Adjusted EPS	1,566	1,999	2,639	3,040
BVPS	13,330	15,003	17,537	20,577
ROAE	14.7%	17.8%	20.5%	20.2%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**21,938**	**26,921**	**31,654**
Non interest income	**7,466**	**10,463**	**11,385**
Total operating income	**29,403**	**37,385**	**43,038**
Total operating costs	(11,868)	(15,702)	(18,076)
Pre-provision operating profit	**17,536**	**21,683**	**24,962**
Total provision charges	**(6,198)**	**(6,718)**	**(7,726)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**11,337**	**14,965**	**17,236**
Tax expense	(2,224)	(2,933)	(3,378)
Profit after tax	**9,113**	**12,032**	**13,858**
Minority interest	(26)	(36)	(42)
Net profit	**9,087**	**11,996**	**13,816**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	543,434	624,950	718,692
Loans to banks	232,922	267,860	308,039
Total gross loans	**776,356**	**892,809**	**1,026,731**
Securities - total	139,761	146,749	154,087
Other interest earning assets	94,448	99,170	104,129
Total gross IEAs	**1,010,565**	**1,138,729**	**1,284,947**
Total provisions	**(8,253)**	**(12,130)**	**(16,172)**
Net loans to customers	**535,321**	**613,039**	**702,751**
Total net IEAs	**1,002,312**	**1,126,599**	**1,268,774**
Cash and deposits	10,103	10,507	10,927
Total investments	3,547	3,689	3,837
Other assets	19,373	20,148	20,954
Total non-IEAs	**33,023**	**34,344**	**35,718**
Total assets	**1,035,335**	**1,160,943**	**1,304,492**
Customer deposits	708,506	807,696	924,812
Cds outstanding	18,215	21,857	26,229
Customer interest-bearing liabilities	726,720	829,554	951,041
Bank deposits	238,327	245,102	252,113
Broad deposits	965,047	1,074,656	1,203,154
Other interest-bearing liabilities	23	24	24
Total IBLs	**965,070**	**1,074,679**	**1,203,178**
Deferred tax liability			
Other non-interest bearing liabilities	16,198	23,079	27,192
Total non-IBLs	**16,198**	**23,079**	**27,192**
Total liabilities	**981,269**	**1,097,759**	**1,230,370**
Share capital	35,978	35,978	35,978
Additional paid-in capital	0	0	0
Treasury shares			
Retained earnings reserve	11,862	18,479	26,537
Other reserves	6,138	8,638	11,518
Shareholders' equity	**53,977**	**63,095**	**74,033**
Minority interest	89	89	89
Total equity	**54,067**	**63,184**	**74,122**
Total liabilities & equity	**1,035,335**	**1,160,943**	**1,304,492**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	20.0%	14.0%	14.5%
Gross cust loan growth	17.9%	15.0%	15.0%
Net interest income growth	18.4%	22.7%	17.6%
Pre provision operating profit growth	17.5%	23.7%	15.1%
Net profit growth	33.0%	32.0%	15.2%
Growth in IEAs	32.2%	12.4%	12.6%
Share value			
Basic EPS (VND)	2,526	3,334	3,840
BVPS (VND)	15,003	17,537	20,577
DPS (VND)	800	800	800
EPS growth	33.0%	32.0%	15.2%

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	2.5%	2.5%	2.6%
Cost-income ratio	(40.4%)	(42.0%)	(42.0%)
Reported NPLs / gross cust loans	1.1%	1.2%	1.3%
Reported NPLs / net cust loans	1.2%	1.3%	1.4%
GP charge / average cust loans	1.2%	1.2%	1.2%
Total CAR	11.2%	10.8%	11.2%
Loan deposit ratio	74.8%	75.3%	75.6%
Margins and spreads			
Return on IEAs	5.2%	5.1%	5.2%
Cost of funds	2.9%	2.7%	2.8%
Interest return on average assets	2.4%	2.5%	2.6%
ROAE	17.8%	20.5%	20.2%

Source: VNDIRECT

ASIA COMMERCIAL JSB (ACB) - INITIATION

Market Price	Target Price	Dividend Yield	Rating	Sector
VND28,900	VND39,800	0.0%	ADD	FINANCIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

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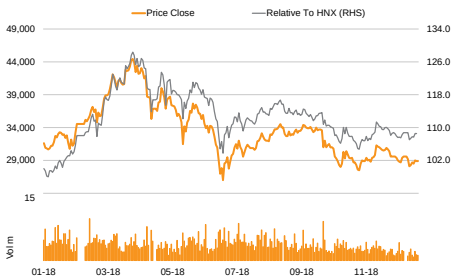
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	44,435
52w low (VND)	26,000
3m Avg daily volume (shares)	3.5m
3m Avg daily value (VNDmn)	102,374
Market cap (VNDbn)	36,043
Outstanding shares (m)	1,247
Free float (%)	35
TTM P/E (x)	8.3
Current P/B (x)	1.8

Ownership

Chairman and related parties	10.2%
Dragon Financial Holdings Limited	6.9%
First Burns Investments Limited	4.0%
Asia Reach Investments Limited	3.2%
Others	75.7%

Source: VNDIRECT

Stable growth expected now that legacy issues are resolved. We initiate coverage on ACB with an Add rating.

Well-established retail brand name and customer base. ACB pursued a retail banking business model since its inception in 1993 and was the first bank to have a two-year professional training course on retail banking standards. Being the first mover in retail banking, ACB has built its reputation as one of the leading retail banks, with the third largest market share in both individual lending and individual deposits among private commercial banks in FY17.

Large retail customer base enables a strong fee income franchise. In 9M18, ACB was among the top five listed banks ranked by contribution of fee income to total income (at 10.9%). The bank recently launched various initiatives to expand its customer base to the affluent and lower mass segments as a bigger customer base will enable growth in fee income. In addition, new customers will help increase CASA with new demand deposits, thus leading to higher NIM.

Legacy issues resolved, resulting in a healthy balance sheet. ACB has a conservative lending strategy with one of the lowest rates of exposure to both real estate and unsecured lending. Legacy assets related to the former vice chairman were, however, an issue. These assets were completely resolved in FY17. As of end-9M18, ACB has the lowest level of distressed assets in the sector at 0.9% of total loans; and high loan loss buffers with an LLR of 129.5%.

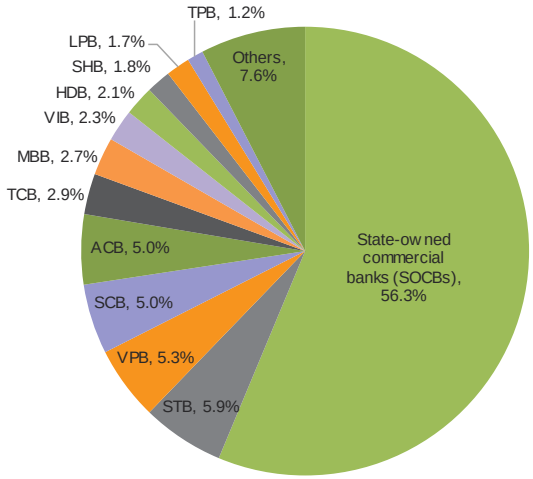
We forecast a net profit CAGR of 16.8% over FY18-20F, driven by 16.8% CAGR in net interest income, on the back of 15.0% loan CAGR and a 16bp improvement in NIM. We project a non-interest income CAGR of 19.8% driven by a healthy combination of payment fees, card fees, bancassurance, bad debt recovery related to legacy debt and VAMC debt written-off in previous years.

Key risks: Upside risks stem from lower cost-to-income ratio (CIR) compared to our forecasts. We forecast a CIR of 46.0% for FY18F and 47.0% for FY19-20F, higher than the 44.9% CIR in 9M18, due to increased investment in digital banking. Downside risks are slower-than-expected bad debt recovery, which would dent non-interest income growth prospects.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	6,892	8,458	10,092	11,710
Net interest margin	3.3%	3.4%	3.5%	3.6%
Total operating income (bn)	7,563	11,439	13,179	15,861
Total provision charges (bn)	(1,218)	(2,565)	(851)	(991)
Net profit (bn)	1,325	2,118	4,997	5,913
Net profit growth	28.9%	59.8%	135.9%	18.3%
Adjusted EPS	1,022	1,658	3,912	4,630
BVPS	11,276	12,854	16,860	21,602
ROAE	9.9%	14.1%	27.0%	24.7%

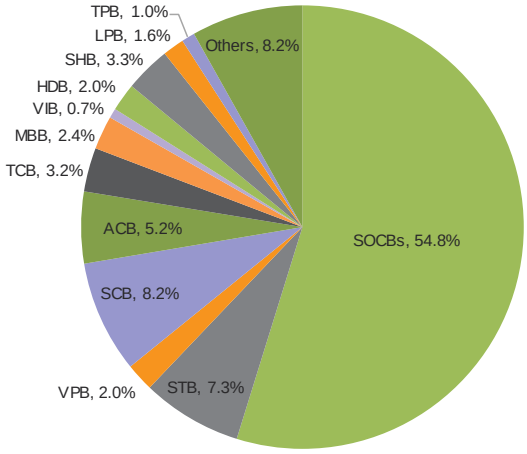
Source: VNDIRECT

Figure 99: Individual loan market share, as of end-FY17.



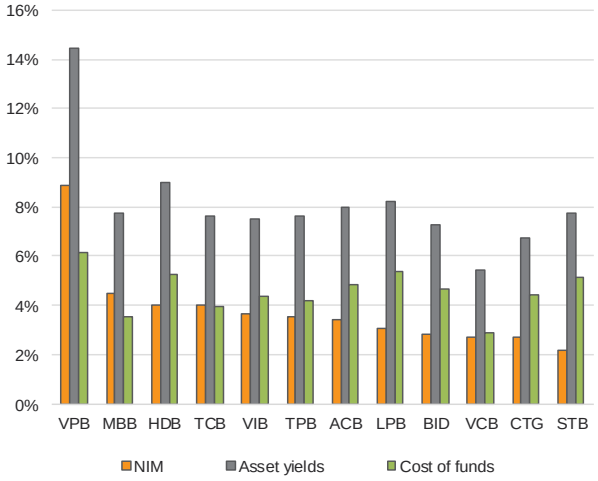
Source: VNDIRECT, BANKS

Figure 100: Individual deposit market share, as of end-FY17.



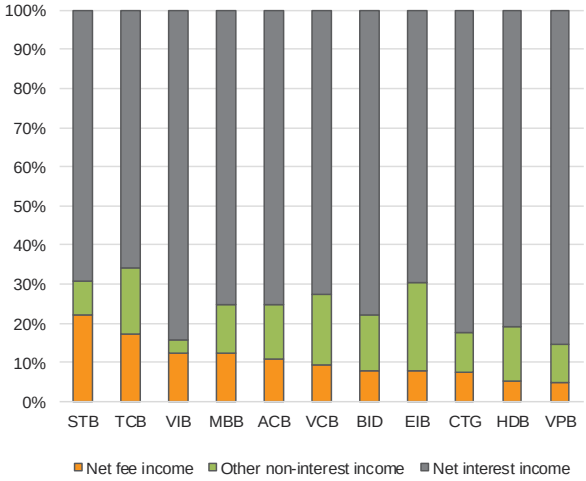
Source: VNDIRECT, BANKS

Figure 101: ACB charges relatively high lending rates but has higher funding costs, making for middling NIMs (9M18 data)



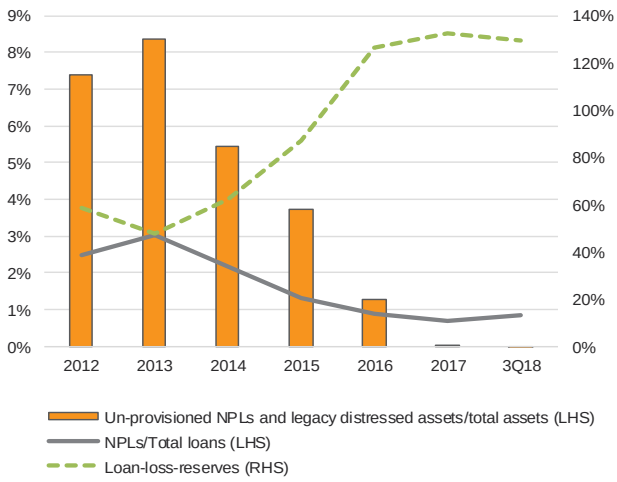
Source: VNDIRECT, BANKS

Figure 102: ACB is among the top five banks in terms of ratio of net fee income/total operating income. (9M18 data)



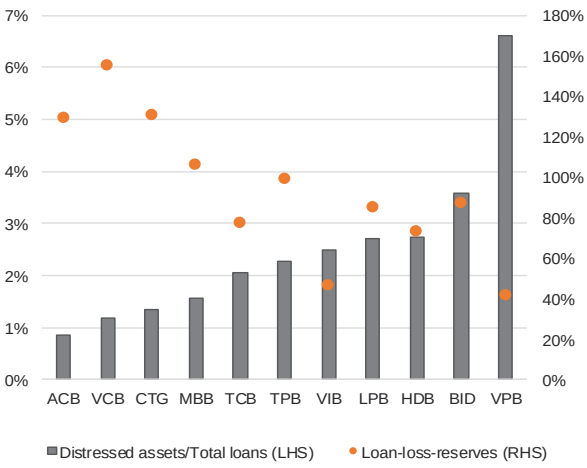
Source: VNDIRECT, COMPANY

Figure 103: ACB has low NPL, high LLR and has resolved all legacy debt issues in FY17.



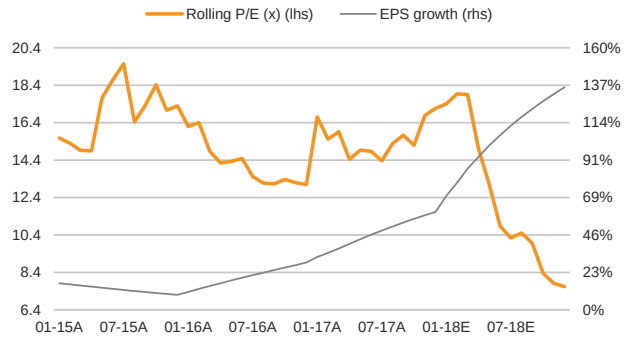
Source: VNDIRECT, BANKS

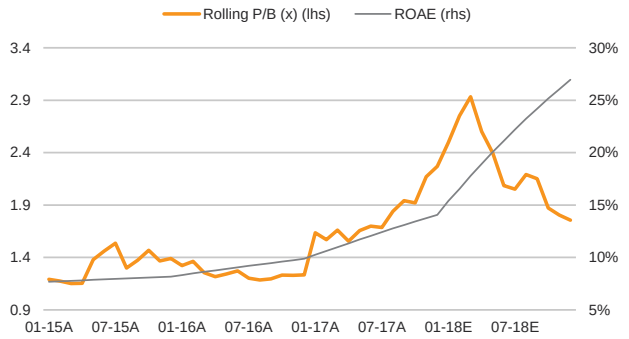
Figure 104: ACB has the lowest level of distressed assets, as of end-9M18.



Source: VNDIRECT, BANKS

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**8,458**	**10,092**	**11,710**
Non interest income	**2,981**	**3,087**	**4,151**
Total operating income	**11,439**	**13,179**	**15,861**
Total operating costs	(6,217)	(6,062)	(7,455)
Pre-provision operating profit	**5,222**	**7,117**	**8,407**
Total provision charges	**(2,565)**	**(851)**	**(991)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**2,656**	**6,266**	**7,416**
Tax expense	(538)	(1,269)	(1,502)
Profit after tax	**2,118**	**4,997**	**5,913**
Minority interest	0	0	0
Net profit	**2,118**	**4,997**	**5,913**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	198,513	228,290	262,534
Loans to banks	8,942	16,095	18,509
Total gross loans	**207,455**	**244,386**	**281,043**
Securities - total	54,396	51,363	56,922
Other interest earning assets	8,315	9,562	10,996
Total gross IEAs	**270,165**	**305,310**	**348,962**
Total provisions	**(2,285)**	**(2,850)**	**(3,610)**
Net loans to customers	**196,669**	**225,854**	**259,383**
Total net IEAs	**267,880**	**302,460**	**345,352**
Cash and deposits	4,852	5,191	5,555
Total investments	446	477	511
Other assets	11,138	11,918	12,752
Total non-IEAs	**16,436**	**17,587**	**18,818**
Total assets	**284,316**	**320,046**	**364,170**
Customer deposits	241,393	272,774	310,962
Cds outstanding	6,761	6,761	6,761
Customer interest-bearing liabilities	248,154	279,535	317,723
Bank deposits	15,454	13,908	14,604
Broad deposits	263,608	293,443	332,327
Other interest-bearing liabilities	147	154	162
Total IBLs	**263,755**	**293,598**	**332,489**
Deferred tax liability			
Other non-interest bearing liabilities	4,531	5,421	4,740
Total non-IBLs	**4,531**	**5,421**	**4,740**
Total liabilities	**268,285**	**299,019**	**337,229**
Share capital	10,273	12,886	12,886
Additional paid-in capital	0	0	0
Treasury shares	(666)	(666)	(666)
Retained earnings reserve	3,510	5,894	11,807
Other reserves	2,914	2,914	2,914
Shareholders' equity	**16,031**	**21,028**	**26,941**
Minority interest	(0)	(0)	(0)
Total equity	**16,031**	**21,028**	**26,941**
Total liabilities & equity	**284,316**	**320,046**	**364,170**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	16.6%	13.0%	14.0%
Gross cust loan growth	21.5%	15.0%	15.0%
Net interest income growth	22.7%	19.3%	16.0%
Pre provision operating profit growth	81.0%	36.3%	18.1%
Net profit growth	59.8%	135.9%	18.3%
Growth in IEAs	22.4%	12.9%	14.2%
Share value			
Basic EPS (VND)	1,698	4,006	4,741
BVPS (VND)	12,854	16,860	21,602
DPS (VND)	0	0	0
EPS growth	59.8%	135.9%	18.3%

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	3.4%	3.5%	3.6%
Cost-income ratio	(54.4%)	(46.0%)	(47.0%)
Reported NPLs / gross cust loans	0.7%	0.8%	0.9%
Reported NPLs / net cust loans	0.7%	0.8%	0.9%
GP charge / average cust loans	1.4%	0.4%	0.4%
Total CAR	11.5%	12.2%	12.6%
Loan deposit ratio	80.0%	81.7%	82.6%
Margins and spreads			
Return on IEAs	8.2%	8.4%	8.5%
Cost of funds	4.9%	5.0%	5.1%
Interest return on average assets	3.3%	3.3%	3.4%
ROAE	14.1%	27.0%	24.7%

Source: VNDIRECT

VPBANK (VPB)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND19,100	VND26,100	0.0%	ADD	FINANCIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

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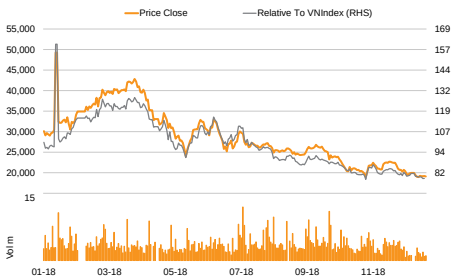
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	42,826
52w low (VND)	18,950
3m Avg daily volume (shares)	3.3m
3m Avg daily value (VNDmn)	70,496
Market cap (VNDbn)	46,924
Outstanding shares (m)	2,457
Free float (%)	73
TTM P/E (x)	6.8
Current P/B (x)	1.5

Ownership

Mr. Ngo Chi Dzung	4.5%
Mr. Bui Hai Quan	2.3%
Mr. Lo Bang Giang	0.1%
Others	93.1%

Source: VNDIRECT

Recovery expected after a lacklustre 2018

The leading market player in consumer finance with high returns on capital. Being the first mover in the consumer finance business, coupled with aggressive business expansion, FE Credit – VPB's subsidiary – has become the industry titan, with 48% market share in FY17. FE Credit's high-yield loans accounted for 23.3% of the bank's total loan book as of end-3Q18, making VPB the bank with the second highest ROE in the sector in 9M18 at 22.2%.

Stricter credit controls hampered earnings growth in FY18F. Loan growth slowed at both the parent bank and FE Credit as SBV tightened credit. Loan growth at FE Credit also decelerated substantially with the suspension of some risky products following the SBV inspection after various customer complaints. The slowdown in loan growth together with rising bad debts led to a hike in the NPL ratio. In addition, deceleration in loan growth also hurt the topline, thereby eroding the bank's capacity to write-off bad debt.

More digitalisation initiatives to grow fee income and cut costs. VPB has launched a new digital platform in SME banking, retail banking and consumer finance. Digitalisation improves convenience, processing time and also reduces operating costs. Digital banking at VPB is a bright spot as VPB's digital initiatives have shown traction, as evinced by a 72% growth in the number of digital banking users by end of 9M18, as compared to year-end FY17.

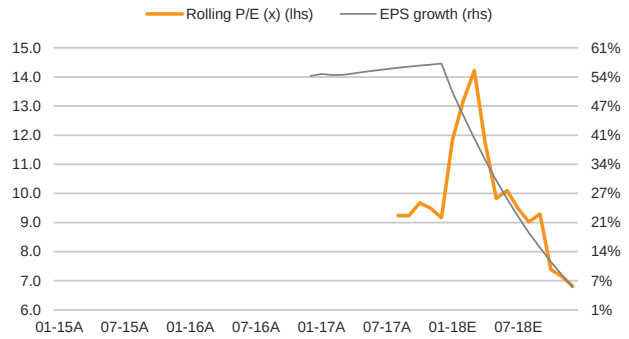
We expect profit growth to recover in the coming years. FY18F profit growth has been hampered by slowing loan growth. We expect loan growth in the coming years will recover after the bank completes restructuring of its lending portfolio in 2018. Bad debt spiked due to a shortage of collection staff in early 2018 and slowing loan growth eroding write-off capacity. VPB has actively recruited staff since 2Q18 and the recovery in loan growth will enhance bad debt handling capacity. We believe that the poor performance in 2018 has been priced into the 2018 P/B of 1.4x, a 17.7% discount to peer average.

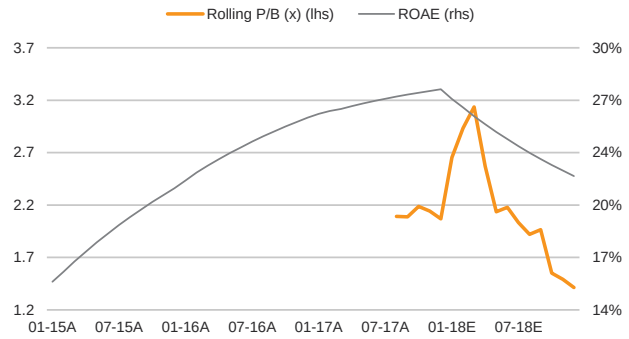
Key risks: Upside risks include a better-than-expected recovery in loan growth which could boost the top line. The main downside risk is a continued rise in bad debt that will fuel higher credit costs.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	15,168	20,625	24,961	28,961
Net interest margin	7.6%	8.6%	8.9%	9.0%
Total operating income (bn)	16,864	25,023	30,308	35,370
Total provision charges (bn)	(5,313)	(8,002)	(10,783)	(12,484)
Net profit (bn)	3,935	6,438	7,134	8,405
Net profit growth	64.2%	63.6%	10.8%	17.8%
Adjusted EPS	1,695	2,702	2,924	3,421
BVPS	7,687	12,255	14,113	16,521
ROAE	25.7%	27.5%	22.2%	22.3%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**20,625**	**24,961**	**28,961**
Non interest income	**4,399**	**5,346**	**6,409**
Total operating income	**25,023**	**30,308**	**35,370**
Total operating costs	(8,895)	(10,608)	(12,379)
Pre-provision operating profit	**16,128**	**19,700**	**22,990**
Total provision charges	**(8,002)**	**(10,783)**	**(12,484)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**8,126**	**8,917**	**10,506**
Tax expense	(1,688)	(1,783)	(2,101)
Profit after tax	**6,438**	**7,134**	**8,405**
Minority interest	0	0	0
Net profit	**6,438**	**7,134**	**8,405**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	182,666	212,858	245,912
Loans to banks	23,980	20,383	23,441
Total gross loans	**206,646**	**233,242**	**269,353**
Securities - total	55,961	65,474	76,605
Other interest earning assets	0	0	0
Total gross IEAs	**262,607**	**298,716**	**345,958**
Total provisions	**(4,127)**	**(5,161)**	**(6,332)**
Net loans to customers	**179,517**	**208,871**	**240,954**
Total net IEAs	**258,481**	**293,554**	**339,625**
Cash and deposits	2,574	2,754	2,947
Total investments	153	163	175
Other assets	16,543	17,701	18,940
Total non-IEAs	**19,270**	**20,618**	**22,062**
Total assets	**277,750**	**314,173**	**361,687**
Customer deposits	133,551	160,203	191,839
Cds outstanding	66,105	65,705	71,847
Customer interest-bearing liabilities	199,655	225,908	263,686
Bank deposits	33,226	41,502	45,179
Broad deposits	232,882	267,410	308,866
Other interest-bearing liabilities	4,060	780	780
Total IBLs	**236,942**	**268,190**	**309,645**
Deferred tax liability			
Other non-interest bearing liabilities	11,115	11,310	11,453
Total non-IBLs	**11,115**	**11,310**	**11,453**
Total liabilities	**248,057**	**279,500**	**321,099**
Share capital	15,706	25,300	25,300
Additional paid-in capital	5,866	5,866	5,866
Treasury shares	0	(2,492)	(2,492)
Retained earnings reserve	5,370	3,248	9,164
Other reserves	2,751	2,751	2,751
Shareholders' equity	**29,693**	**34,672**	**40,589**
Minority interest			
Total equity	**29,693**	**34,672**	**40,589**
Total liabilities & equity	**277,750**	**314,173**	**361,687**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	7.9%	20.0%	19.7%
Gross cust loan growth	26.3%	16.5%	15.5%
Net interest income growth	36.0%	21.0%	16.0%
Pre provision operating profit growth	57.5%	22.1%	16.7%
Net profit growth	63.6%	10.8%	17.8%
Growth in IEAs	21.2%	13.6%	15.7%
Share value			
Basic EPS (VND)	2,765	2,924	3,421
BVPS (VND)	12,255	14,113	16,521
DPS (VND)	0	0	0
EPS growth	57.0%	5.8%	17.0%

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	8.6%	8.9%	9.0%
Cost-income ratio	(35.5%)	(35.0%)	(35.0%)
Reported NPLs / gross cust loans	3.4%	3.7%	3.8%
Reported NPLs / net cust loans	3.5%	3.8%	3.9%
GP charge / average cust loans	4.9%	5.5%	5.4%
Total CAR	14.6%	13.8%	13.4%
Loan deposit ratio	91.5%	94.2%	93.3%
Margins and spreads			
Return on IEAs	14.3%	14.5%	14.6%
Cost of funds	6.1%	6.2%	6.3%
Interest return on average assets	8.1%	8.4%	8.6%
ROAE	27.5%	22.2%	22.3%

Source: VNDIRECT

LIENVIET POST BANK (LPB)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND8,800	VND12,900	11.4%	ADD	FINANCIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019
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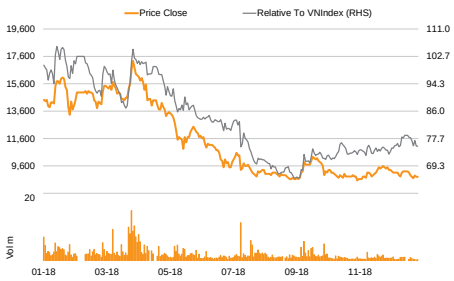
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	17,143
52w low (VND)	8,476
3m Avg daily volume (shares)	1.2m
3m Avg daily value (VNDmn)	10,497
Market cap (VNDbn)	6,930
Outstanding shares (m)	787
Free float (%)	20
TTM P/E (x)	6.9
Current P/B (x)	0.7

Ownership

Vietnam Post	11.5%
Mr. Nguyen Duc Huong	4.5%
H.T.H Co., Ltd	4.5%
Nguyen Dinh Thang	3.9%
Khai Hung Co., Ltd	2.3%
Others	73.3%

Source: VNDIRECT

Network expansion a drag on earnings but will start to pay-off in the medium term.

LPB has embarked on an extensive branch network expansion initiative that is unmatched by other banks. The acquisition of Vietnam Postal Savings Company in 2011 allowed LPB to offer banking services through a postal network. LPB is actively upgrading postal transaction offices to bank transaction offices. LPB has opened 198 new transaction offices so far this year and it plans to open 200-230 transaction offices per year in FY19-20F to complete network expansion in FY20F. Fast network expansion led to a surge in individual deposits while lending at new transaction offices has yet to catch up. As such 9M18 NIM dropped 60bp yoy. We project that network expansion benefits will materialise in the medium term. LPB will be the only bank with an extensive network in every district.

Potential for a boost in fee income from bancassurance. Currently LPB is not really active in bancassurance; it only sells insurance at around 30 transaction offices. However, LPB is seeking an exclusive bancassurance agreement for 15-20 years, which will bring sizeable upfront agency fees. If LPB ramps up bancassurance distribution across its vast network, its bancassurance revenue could achieve robust growth in the coming years.

LPB is considering migrating to HOSE. A listing on HOSE will increase liquidity for LPB and HOSE requires a higher standard of information disclosure which could improve transparency and boost the appeal of the stock to institutional investors.

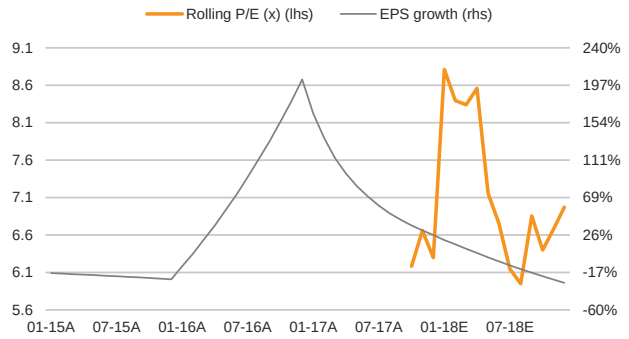
High dividend yield on a low valuation. LPB plans to pay a cash dividend of VND1,000/share for FY18F, equivalent to an 11.4% dividend yield. LPB currently trades at 0.7x P/B, a deep discount to the peer average P/B of 1.6x.

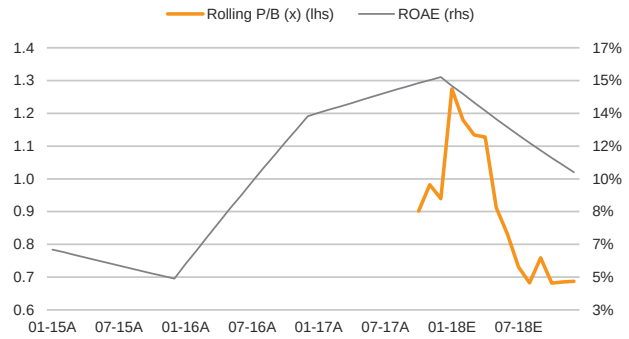
We project net profit CAGR of 22.1% over FY18-20F, with the major driver being net interest income (NII) while non-interest income is still projected to post losses. We forecast NII to grow at 16.4% CAGR in FY18-20F on 15.0% loan CAGR and a 20bp NIM expansion. Provision expense is expected to grow by 10.8% CAGR in FY18-20F. Downside risks include a further fall in the LDR which will impede a NIM recovery.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net interest income (bn)	4,024	5,227	5,224	5,988
Net interest margin	3.5%	3.6%	3.2%	3.3%
Total operating income (bn)	3,872	5,103	4,872	5,784
Total provision charges (bn)	(492)	(522)	(469)	(530)
Net profit (bn)	1,063	1,368	1,032	1,201
Net profit growth	203.8%	28.7%	(24.6%)	16.4%
Adjusted EPS	1,397	1,657	1,177	1,360
BVPS	11,588	12,451	13,389	14,314
ROAE	13.3%	15.4%	10.4%	11.0%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net interest income	**5,227**	**5,224**	**5,988**
Non interest income	**(124)**	**(352)**	**(204)**
Total operating income	**5,103**	**4,872**	**5,784**
Total operating costs	(2,813)	(3,069)	(3,702)
Pre-provision operating profit	**2,290**	**1,803**	**2,082**
Total provision charges	**(522)**	**(469)**	**(530)**
Income from associates & JVs			
Net other income			
Pre-tax profit	**1,768**	**1,333**	**1,552**
Tax expense	(400)	(302)	(351)
Profit after tax	**1,368**	**1,032**	**1,201**
Minority interest	0	0	0
Net profit	**1,368**	**1,032**	**1,201**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Gross loans to customers	100,621	114,708	131,914
Loans to banks			
Total gross loans	**100,621**	**114,708**	**131,914**
Securities - total	32,650	35,692	40,199
Other interest earning assets	23,292	19,491	21,441
Total gross IEAs	**156,563**	**169,891**	**193,554**
Total provisions	**(2,015)**	**(2,284)**	**(2,673)**
Net loans to customers	**99,392**	**113,431**	**130,448**
Total net IEAs	**154,548**	**167,608**	**190,880**
Cash and deposits	893	1,607	1,768
Total investments	325	357	393
Other assets	7,668	8,435	9,279
Total non-IEAs	**8,886**	**10,399**	**11,439**
Total assets	**163,434**	**178,007**	**202,319**
Customer deposits	128,275	148,799	172,607
Cds outstanding	6,157	10,159	10,159
Customer interest-bearing liabilities	134,433	158,959	182,767
Bank deposits	1,332	1,931	1,545
Broad deposits	135,764	160,889	184,311
Other interest-bearing liabilities	14,709	2,524	2,321
Total IBLs	**150,473**	**163,414**	**186,632**
Deferred tax liability			
Other non-interest bearing liabilities	3,577	4,050	4,415
Total non-IBLs	**3,577**	**4,050**	**4,415**
Total liabilities	**154,050**	**167,464**	**191,047**
Share capital	6,460	7,500	7,875
Additional paid-in capital	0	0	0
Treasury shares			
Retained earnings reserve	1,794	1,978	2,331
Other reserves	1,129	1,066	1,066
Shareholders' equity	**9,383**	**10,544**	**11,272**
Minority interest	0	0	0
Total equity	**9,383**	**10,544**	**11,272**
Total liabilities & equity	**163,434**	**178,007**	**202,319**

	12-17A	12-18E	12-19E
Growth rate (yoy)			
Cust deposit growth	15.6%	16.0%	16.0%
Gross cust loan growth	26.3%	14.0%	15.0%
Net interest income growth	29.9%	(0.1%)	14.6%
Pre provision operating profit growth	24.4%	(21.3%)	15.5%
Net profit growth	28.7%	(24.6%)	16.4%
Growth in IEAs	15.8%	8.5%	13.9%
Share value			
Basic EPS (VND)	1,858	1,319	1,525
BVPS (VND)	12,451	13,389	14,314
DPS (VND)	1,000	1,000	600
EPS growth	25.7%	(29.0%)	15.6%

Key ratios

	12-17A	12-18E	12-19E
Net interest margin	3.6%	3.2%	3.3%
Cost-income ratio	(55.1%)	(63.0%)	(64.0%)
Reported NPLs / gross cust loans	1.1%	0.9%	0.9%
Reported NPLs / net cust loans	1.1%	0.9%	0.9%
GP charge / average cust loans	0.6%	0.4%	0.4%
Total CAR	11.0%	10.5%	9.9%
Loan deposit ratio	74.8%	72.2%	72.2%
Margins and spreads			
Return on IEAs	7.9%	8.2%	8.4%
Cost of funds	4.5%	5.2%	5.3%
Interest return on average assets	3.4%	3.1%	3.1%
ROAE	15.4%	10.4%	11.0%

Source: VNDIRECT

REAL ESTATE: SUPPLYSIDE HEADWINDS DENTING TOPLINE GROWTH PROSPECTS

HCMC condo market: reduced supply in mid-range segment led to fall in sales volume in 2018; we expect supply to moderate further in 2019 with a renewed project focus on the mid-range segment.

According to a CBRE 4Q18 report, new condo supply remained stable in 2018 compared to 2017, but with less mid-range and more high-end condos launched in the period. Mid-range condos still comprised the biggest chunk of total transaction volume but saw a reduction of 17.0% yoy in 2018 due to lower supply, dragging total condo transaction volume down by 7.0% to 31,083 units. This, together with the slow presales of high-end condos, dragged the blended take-up rate down by 7.7% pts yoy in 2018 to touch 101%. Selling price ticked up by 5-7% yoy in most segments but skyrocketed by 19% for luxury condos in 2018. Mid-range condo prices were also unaffected by the supply shortage with prices about flat as new mid-range condo projects moved further away from the CBD.

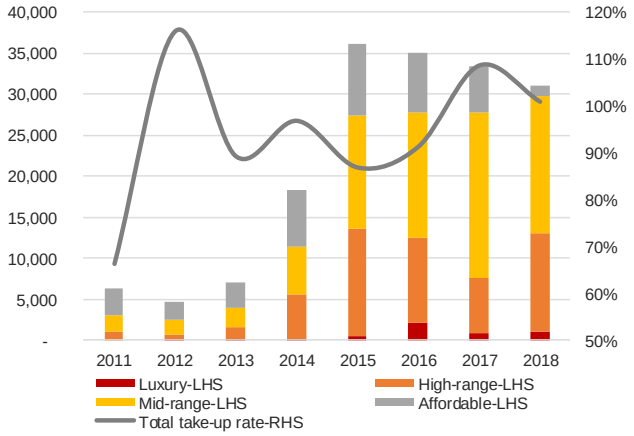
Figure 105: HCMC 2018 condominium transaction details by segment

Units	Luxury	High-range	Mid-range	Affordable	Total
New supply	1,636	12,381	16,007	768	30,792
Sold volume	981	12,082	16,755	1,265	31,083
Take-up rate	60%	98%	105%	165%	101%

Source: CBRE

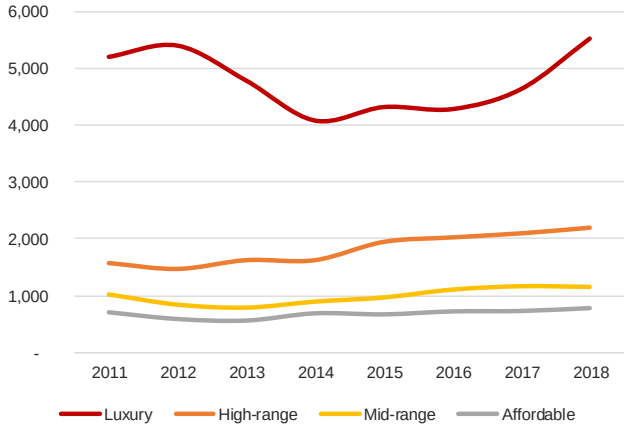
In 2019, CBRE expects a fall in new condo supply as the slow project launch trend will continue into this year and reduce transaction volume to ~29,000 apartments. Future supply will continue to be focused on the mid-range segment and will be largely located in Districts 9 & 2 with these two districts expected to contribute 61% to total transaction volume in HCMC. We expect a 5% increase in prices for the high-range, mid-range, and affordable segments in 2019 but luxury condo prices in the CBD may reach over US$10,000/sq m with the launch of a key upcoming project, the Centennial (Ba Son Phase 2) by Alpha King. A key downside risk to prices in the mid-range segment, however, is the launch of higher-than-expected supply from the Vincity project by Vinhomes (VHM VN, Not rated).

Figure 106: HCMC condominium transaction volume (units) – fewer launches in the mid and affordable range caused sales volume to fall in 2018



Source: CBRE

Figure 107: HCMC condo price (US$/sq m) – Luxury condo prices ticked up in 2018 with the introduction of new prime location projects with prices quoted at ~US$7,000-8,000/sq m.



Source: CBRE

Hanoi condo market: Improving presales with more supply

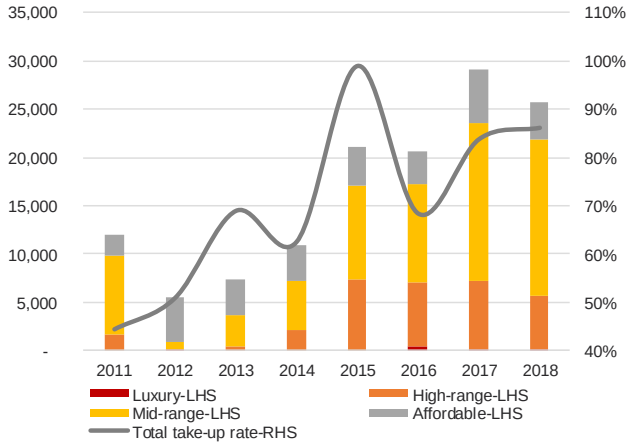
In line with the trend in HCMC, Hanoi was also reported to have less new supply in 2018 but demand stayed strong. Consequently, the take-up rate increased 25% pts to 86% (CBRE). New supply and transactions were concentrated in the mid-range segment located mostly in the south-west of the city. The north and east will see massive construction from a number of large scale projects to be launched in 2019F. CBRE also expects ~34,000 units (+14% yoy) to enter the market in 2019F driven by an increase in mid-range condo projects. Also from the agency's report, 2019F primary selling prices for most segments are expected to be stable except for a 30% hike in luxury condo prices as more premium projects are slated for launch this year.

Figure 108: Hanoi 2018 condominium transactions by segment

Units	Luxury	High-range	Mid-range	Affordable	Total
New supply	0	6,109	20,615	3,116	29,840
Sold volume	127	5,608	16,133	3,890	25,758
Take-up rate		92%	78%	125%	86%

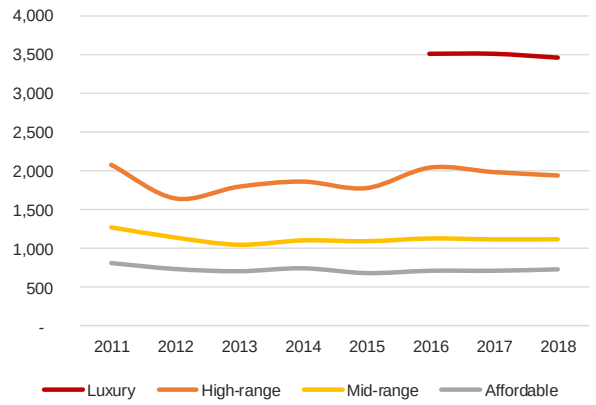
Source: CBRE

Figure 109: Hanoi condominium transaction volume (units) – Strong demand for new launches in 2018 raised take-up rates



Source: CBRE

Figure 110: Hanoi condo price (US$/sq m) – Prices stable for most segments in 2018

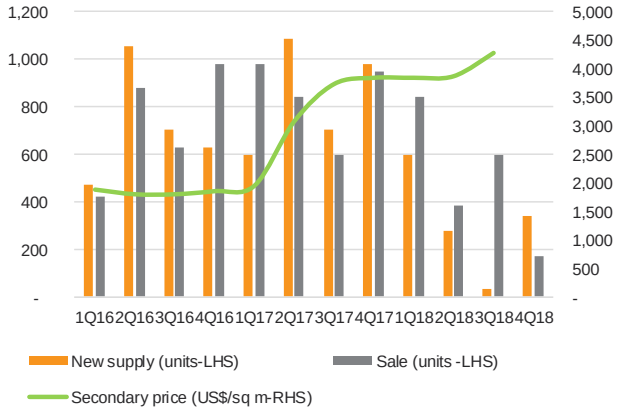


Source: CBRE

Landed property market: weak volume with lack of new supply to push up prices, rendering the segment ripe for speculation

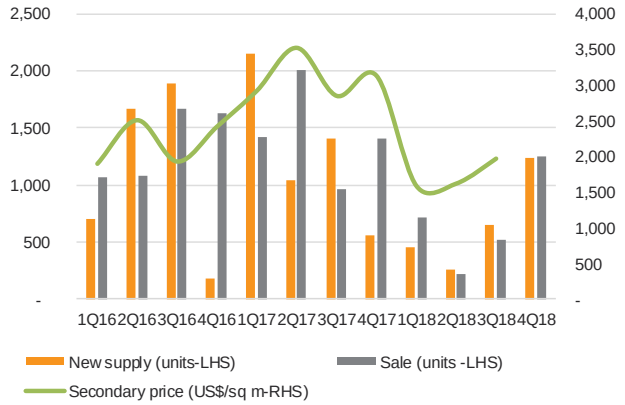
New supply has become expensive and unfeasible for new low-rise development. Hence, 2018 transaction volume (excluding land lots) also fell 40.8% yoy in HCMC and 53.4% yoy in Hanoi given the tight supply (CBRE). Secondary selling prices for landed properties (townhouses/villas), therefore, skyrocketed 47-117% yoy depending on asset type in HCMC but dived 37.3% in Hanoi due to higher secondary transactions in surburban areas which usually come with lower price tags than in the main urban area. We continue to be bearish on the segment volume as we believe 2019F new supply will still be limited and mostly appear in upcoming township projects in both HCMC and Hanoi. Landed property prices, therefore, will remain strong this year and may lead to property speculation in this asset class.

Figure 111: HCMC villa/townhouse performance – Few new projects launched in 2018 but demand was plentiful



Source: CBRE

Figure 112: Hanoi villa/townhouse performance – 2018 saw good absorption rates as supply remained very muted



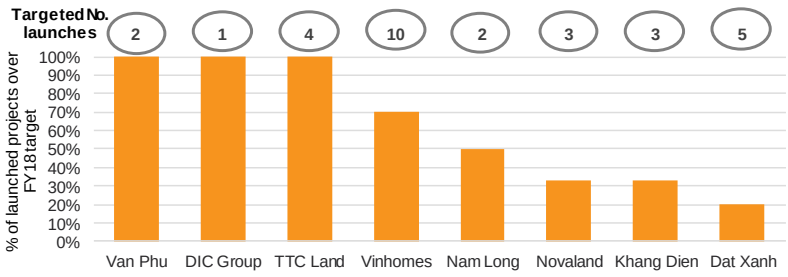
Source: CBRE

Regulatory environment still unfavourable

Developer pipeline has already been impacted

We collected some data from listed developers on planned launches in early 2018 and compared it to the number of actual launched projects in 11M18. Most top-tier developers like Vinhomes **(VHM VN, Not rated),** Novaland **(NVL VN, Not rated),** Khang Dien **(KDH VN, HOLD, TP:VND34,900**), and Nam Long **(NLG VN, ADD, TP:VND37,700)** were tracking below their annual targets for presale launches towards the end of the year. Most of the projects contributing to the gap were either postponed to 2019F or transferred to other parties, and most of these were located in HCMC. Besides NVL, who admitted having problems with Land Use Rights (LUR) issues, the others cited a range of reasons for not obtaining their construction licences and delaying their project launches. Although their delayed projects are expected to be launched this year, a number of developers have already postponed their launches multiple times, making investors sceptical about the recent "rollover" claims.

Figure 113: Actual project launches over FY18 target – Project licensing was difficult for most HCMC developers when preparing for their project launches in 2018



Source: VNDIRECT, Companies

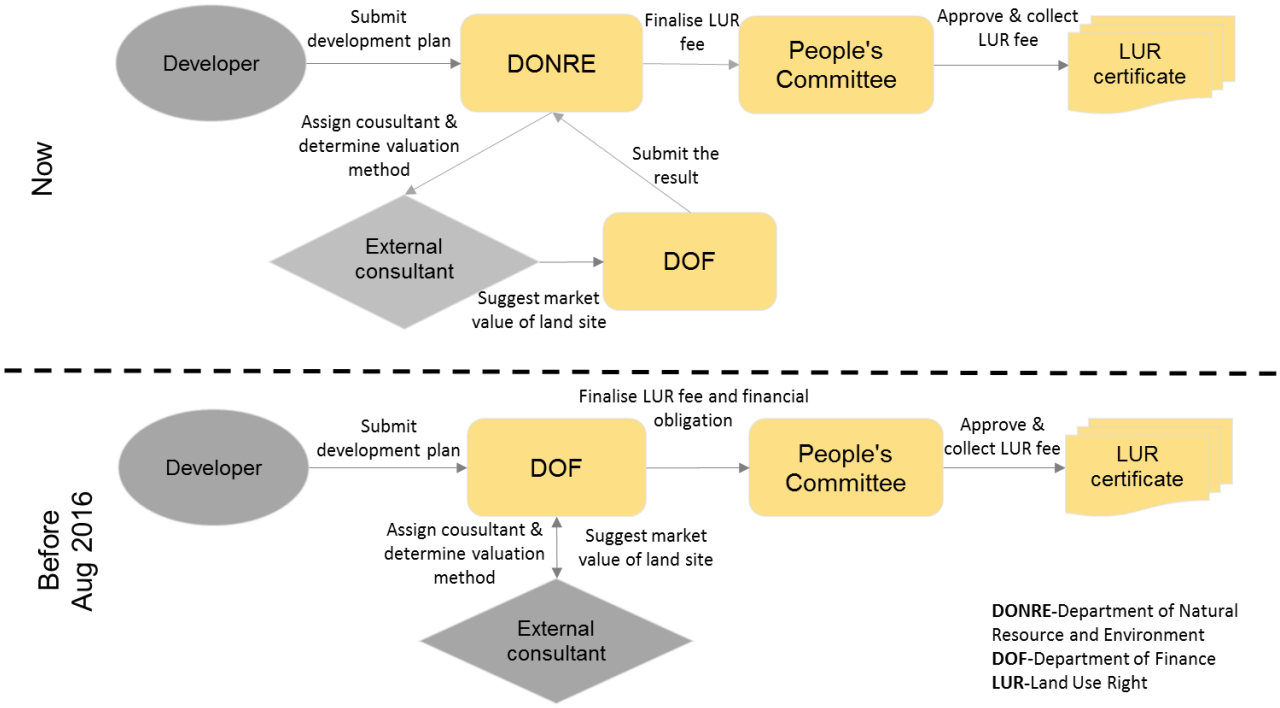
Endless loops in Land Use Right (LUR) approval process

Previously, the LUR fee was calculated solely by the Department of Finance (DOF) based on their valuation methods. However, since the circular No. 87 & 88/2016/TT-TTLT-BTC-BTNMT released in 2016 guiding the new approval procedure, DOF and Department of Natural Resource and Environment (DONRE) are required to collaborate in calculating the LUR fee for any new development. Indeed, HCM Real Estate Association (HoRea) said it now takes 1-3 years to reach a final

agreement by both departments as they usually have different views on the land value and valuation method. Once DOF rejects the land value, the procedure will go back to the very start at DONRE to revise the method or to change the valuation agency. Also, developers can no longer advance the LUR fee upon their rough calculation to start construction while waiting for the final figure from the authorities, as was the case before.

Moreover, DONRE is only responsible for assessing purely residential land and only 26% of the land sites that were filed for LUR certificates in HCMC (accumulated since 2015, [HoRea]) met this requirement. For new developments on land sites mixed with non-residential land parcels, other departments will also need to grant approval. This lengthens approval times as one project cannot simultaneously be filed at different departments. These are just two of many obstacles mentioned in the HoRea study and give just a glimpse into the multiple difficulties developers currently have to deal with. Without the LUR certificate or construction license, developers cannot start construction and this could lead to a plunge in pre-sales volume.

Figure 114: Simplified procedure to calculate LUR fee



Source: Ho Chi Minh Real Estate Association (HoRea)

Mounting scrutiny of zoning and legacy state land transfers

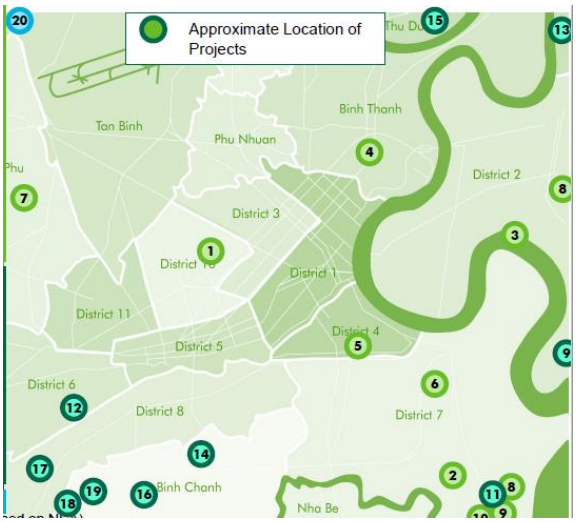
The new township Thu Thiem – HCMC highlighted the flaws in city zoning and land compensation in 2017. Since then, real estate has become one of the biggest targets of the state inspection schedule and hundreds of cases of misconduct in state land transfer deals and improper zoning have been detected mostly in HCMC and Hanoi. Since then, the city authorities have been cautious about signing-off on new sizeable projects, especially before the revision of the housing master plan for 2016-20, which was recently released in Dec 2018. According to the Ho Chi Minh Real Estate Association as of 24 Dec 18, the number of new approved projects in 2018 fell 12.7% yoy and project launches planned for 2019F may be postponed if their licenses have not already been obtained in 2018.

Overall, the new twists in the approval process for the LUR and construction licenses are obvious bottlenecks for new project supply. In fact, the government needs more time to completely remove the obstacles and trim their current heavy regulatory regime. Hence, for 2019, we do not foresee any major and effective improvement in project launches. Nonetheless, we also do not expect a sector-wide absence of new projects as the magnitude and duration of these regulatory roadblocks will vary for each project.

A tale of two cities: soaring land prices in HCMC to deter supply in central urban areas while Hanoi offers more room for growth

Before the newly approved HCMC zoning plan which will limit new residential development in the CBD, the city's land bank was already extremely limited for new development in the last three years. The new master plan seems to discourage new supply and clearly creates good reason for sellers to lift asking prices of existing projects. However, Hanoi still presents room for developers as new projects are still located close to the CBD while new projects in HCMC are located further away, at the city fringes.

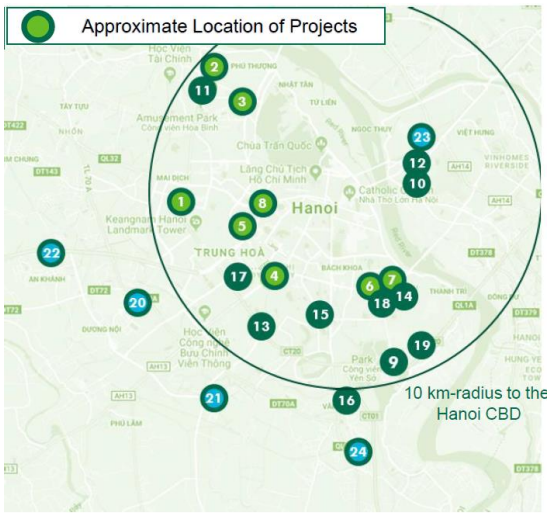
Figure 115: 3Q18 HCMC new condo project map - developments have moved even further away from the CBD



Blue: Affordable; Green: Mid-range; Dark green: high-range

Source: CBRE

Figure 116: 3Q18 Hanoi new condo project map – more developments compared to HCMC with more projects located close to the CBD



Blue: Affordable; Green: Mid-range; Dark green: high-range

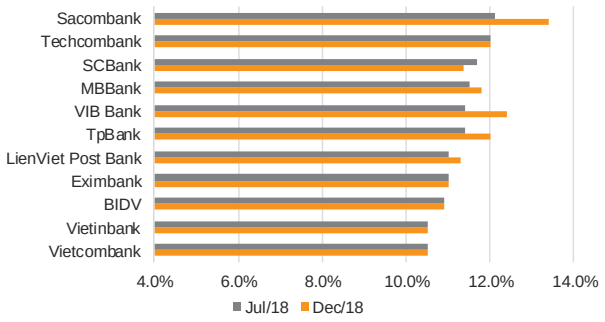
Source: CBRE

HCMC is currently revising its land price benchmark for 2019F (used for LUR fee calculation) with a suggestion of a 19-30% increase (HoRea) to take into account the actual land price increase in the market while the corresponding increase in 2018 was only 5-8%. This new rate, if approved, would certainly deliver a financial shock to developers operating in HCMC. Hanoi, however, will keep using the same benchmark until the end of 2019. The land cost usually covers 20-30% of a high-rise development's total project cost which implies that the proposed increase in the land price benchmark translates into a 4-9% increase in total project development cost. The combined impact of land bank scarcity and the state's land price benchmark revision presents a formidable threat to developer profit margins if they are unable to pass this through in the form of higher selling prices without scaring-off homebuyers and, in the process, risking their project liquidity.

Homebuyers will still enjoy cheap mortgages in 2019 despite an imminent rate rise; this should support end-user demand

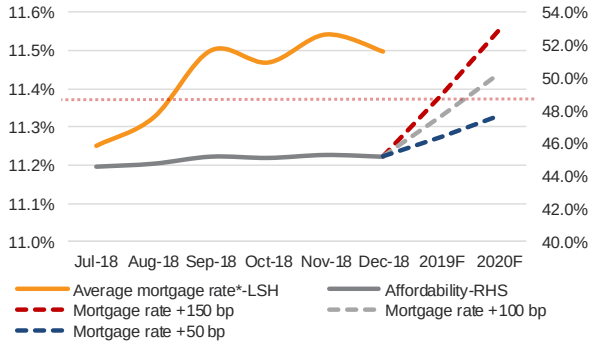
As discussed in our initiation report and banking sector reports, local banks are being forced to reduce their long-term lending to the real estate sector and track an uptrend in policy rates in 2019. We tracked mortgage rates of several popular banks and forecast how housing affordability will change based on a forecasted rise in interest rates. The average mortgage rate notched up 25bp in the last six months but the mortgage payment-to-income ratio has not yet breached the 50% level which we believe to be the upper bound of mortgage affordability in Vietnam. We maintain our assumptions laid out in our sector initiation report and still believe that mortgages will stay affordable despite a 50 bp increase in rates in 2019. We are, therefore, bullish on demand for mid and affordable range condos in 2019.

Figure 117: Mortgage rates across selected banks



Source: VNDIRECT

Figure 118: Mortgage rates vs buyer affordability – home buyers unlikely to be hurt by rate rises at least in 2019

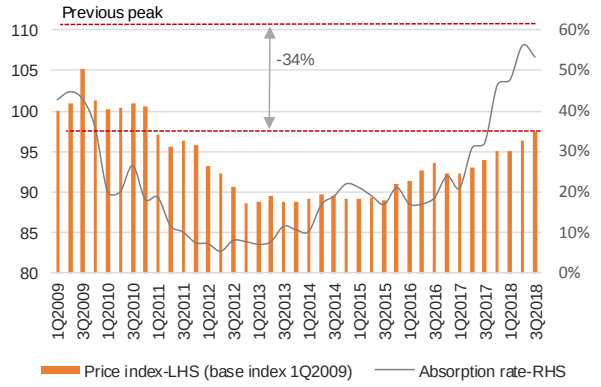


Source: VNDIRECT

We expect a pause rather than a sharp downturn

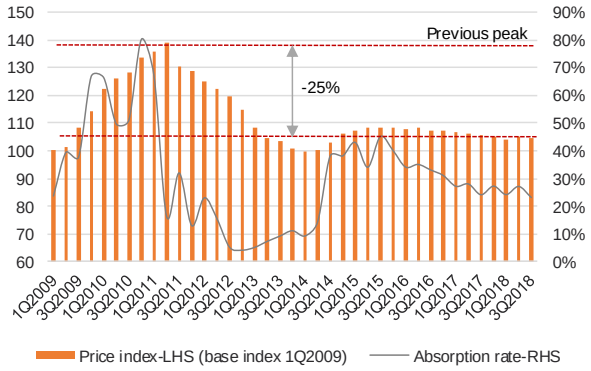
Based on the Savills index, HCMC property prices inched up only by a 2% CAGR since 2013 and are still 34% below the bubble peak levels seen in 2Q08. This is because of the change in market product mix wherein affordable and mid-range properties took the lead in transaction volume comprising 54-66% of all transactions per year in the period 2014-18. Hanoi housing prices, however, flattened in the last three years and now hover 25% below the local peak seen in 2Q11. **Overall, we do not believe that the market has overheated and prices remain at levels that are affordable for real homebuyers.** This explains the rise in presale absorption rates in both cities in 2018 compared to the last pre-bubble period when absorption rates weakened; also the current absorption rate is much higher than the 43% absorption rate seen after the last property bubble burst in 2008. **While foreign buyers have been important drivers of demand this time, especially in the high-end condo segment, we do not see this as a risk as foreign interest is unlikely to dry up given Vietnam's emergence as a major tourism destination and a regional business and manufacturing force and also given that foreign buyers comprise a small portion of total market volumes.**

Figure 119: HCMC – Prices are not really far from the 2013 trough while absorption is at historical highs.



Source: Savills

Figure 120: Hanoi – Demand no match with HCMC even though supply is plentiful in Hanoi, thereby weighing on absorption



Source: Savills

A clear indicator before the last housing bubble burst in Vietnam (2008-09) or the US market (2007-09) was the rapid build-up of a huge amount of high-priced property. In HCMC, we witnessed a good improvement in absorption rates year after year since 2013, touching a healthy level of 53% as at 3Q18. Faster presales helped reduce real estate inventory throughout the period, in line with the 82.1% fall in the city's real estate inventory value from VND128tr in 1Q13 to VND23tr as at Nov 2018, as reported by the Ministry of Construction. Most of the current outstanding stock is from suspended projects or located far from the CBD with limited transportation links. Also, the apartments sold to speculators contributed only 3.1% of total successful condo transactions in 2013-17 (Savills). Given these conditions, we are not concerned about a material softening in future property prices due either to unsold inventory or speculators who might bail out of the market and dump their assets at fire-sale prices.

Figure 121: Neither city is on the cusp of a property crisis

Real estate bubble indicators	HCMC	Hanoi
Pre-bursting of bubble signals		
Housing prices skyrocket and breach home buyer affordability	✗	✗
Real estate inventory increases	✗	✓
Mortgage rate increases	✓	✓
High level of real estate speculation	✗	✗
Bursting bubble signals		
Property prices start decreasing sharply	✗	✗
Market turns illiquid with immediate fall in transaction volume	✗	✗
Mortgage loans are too expensive and discourages leveraged home purchases ; mortgage default risk appears	✗	✗
Speculators bail out of the market and dump their inventory at a deeply discounted price	✗	✗

Source: VNDIRECT

From the above, we do not believe that Vietnam's residential property market, especially HCMC, will see a sharp downturn in 2019F as the typical indicators of a bubble market, such as a dramatic increase in property prices or a large amount of asset dumping by speculators, are currently not "flashing red". The transaction volume may fall but more due to lack of supply and could, nonetheless, still be maintained at a healthy level. Meanwhile, price increase will still track the increase in purchasing power of most homebuyers in 2019F. The tightening of regulations on new project development appears to be helping to reduce the risks of the market overheating.

Conclusion and rating

Barring a steeper-than-expected increase in interest rates for 2019F, real demand will help absorb a still sizeable volume of anticipated new supply from upcoming large scale projects about to be launched in 2019F in both HCMC and Hanoi. With a less stringent regulatory environment than HCMC, Hanoi may lead market volume in 2019F while HCMC will slow down due to project approval delays. HCMC is currently the key market for most leading, listed developers like DXG, NVL, NLG, KDH, and PDR. Therefore, slow project launches in the city will definitely impact their pipeline and presale backlog for at least the next six months.

We **Downgrade** the sector rating to **Neutral** to reflect the impact of the unfavourable regulatory changes land surging land prices in HCMC in 2019F which will pressure new launch volumes as well as developer margins. However, we still maintain our view that real housing demand remains robust and, therefore, expect sustained high absorption rates for projects in 2019F, mostly in the mid-end condominium segment. Hence, we prefer listed developers that have sizable projects that have already obtained the regulatory permits and are scheduled for launch in 2019F.

Stock picks – we are still bullish on NLG and laud VHM's strategic pivot into the mid-end segment, placing it on our watch list.

We like developers that meet the following key criteria:

1) About to launch projects which already have construction licenses or LUR certificates, or have a high likelihood of securing them in 2019F;
2) With material exposure to mid-range and affordable condos as these segments are driven by real end-user demand;
3) Buffered by a healthy financial position (low leverage, strong liquidity) to counter the risk of tight credit flow to the real estate market as discussed in our initiation report.

Based on the above criteria, Nam Long (NLG VN, ADD, TP: VND37,700) is our top pick and we place Vinhomes (VHM VN, Not rated) on our watch list for 2019.

Vinhomes: (VHM VN, Not rated) VHM has a fabulous track record in prime land site acquisition and relatively clean legal status. Its outstanding execution teams are able to stick to their project launch time frames and help to mitigate the aforementioned political and regulatory risks that are plaguing the HCMC property market. VHM announced a solid project launch schedule for 2019 back in the fourth quarter of 2018 with a total of 10.7m sq m NSA of residential products from 11 projects in Hanoi, HCMC, and other lower-tier cities slated for launch in the year. In Oct 2018, the company also successfully introduced its new brand, Vincity, to penetrate the mid-range condo market. This mid-range housing product comprised 70% of the total 7,549 units that were launched in 2018 at Vincity Ocean Park (Gia Lam-Hanoi).

At the end of 3Q18, VHM's reported 9M18 net profit surged 143% yoy compared to 9M17 pro-forma results which adjusted for the consolidation effects from its ownership of various projects as a part of VHM's restructuring prior to listing. This mostly came from delivery of Harmony, Golden River, Central Park, and the stake transfer at Vinhomes Dinh Tien Hoang and Lotus. The company is aiming to achieve VND17.6tr of net profit for FY18F, a 77.8% increase over FY17 pro-forma figures mostly due to delivery at Metropolis, Imperia, Green Bay, and Golden River in 4Q18F. The stock is trading at a FY18

P/E of 14.6x on company guidance earnings which is higher than the domestic peer average.

Nam Long (NLG VN, ADD, TP:VND37,700): To double the planned launch volume at Akari, NLG delayed the project launch from 1Q19 to 3Q19 to complete all legal requirements. The company is also currently undertaking landfilling for Phase 1 of its Waterpoint project, launched in 2Q19F with 830 villas and land lots. Given its location in Long An province, a substantial distance away from HCMC, the project uses land acquired at low cost and could help create the very first fully integrated and self-contained township adjacent to HCMC with higher living standards compared to the surrounding community. The presales of this project should also be supported by rising industrial activity and economic development in the surrounding area boosted by the upcoming completion of Trung Luong-Long Thanh highway and Ring Road 4, in our view.

We expect NLG to record VND705bn in net profit (+31.8% yoy) for 2018 of which 42% would be contributed by the 130ha land transfer at Waterpoint in 3Q18 and the remaining would come from deliveries at Fuji, Kikyo, and Ehome Phu Huu. We also project a 140% increase in presales value fuelled by launches at Akari, Waterpoint and Mizuki Phase 2 with a total expected 3,822 units sold in FY19F. The stock is currently trading at a 39.2% discount to our RNAV.

Figure 122: Real Estate peer comparison

Company name	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (%)	TTM P/E (x)	TTM P/B (x)
Vinhomes Jsc	VHM	11,059	N/A	N/A	7.9	23.5	136.0	23.6	2.8
Novaland	NVL	2,378	47.1	-2.3	3.8	14.2	81.4	25.0	3.1
Khang Dien House	KDH	544	12.2	27.3	5.8	10.5	-15.1	21.7	2.0
Dat Xanh Group	DXG	351	56.9	56.2	9.0	25.9	13.2	7.6	1.8
Phat Dat Real Es	PDR	297	46.4	54.9	6.1	18.3	-5.4	13.4	2.2
Van Phu Invest	VPI	284	2,256.5	530.0	13.1	38.8	13.0	9.6	3.6
Nam Long Group	NLG	262	42.2	24.9	8.7	22.4	-20.7	6.1	1.3
Hai Phat Invest	HPX	209	370.9	81.7	5.7	20.0	62.4	8.1	2.3
DIC Group	DIG	169	258.1	249.8	4.4	9.7	52.4	14.3	1.3
Ldg Investment	LDG	117	113.2	74.6	14.2	17.4	-16.7	7.6	1.2
Sai Gon Thuong	SCR	105	-87.5	42.7	3.8	9.6	47.6	6.0	0.6
NBB Investment	NBB	86	-12.7	49.4	1.8	4.8	26.3	23.0	1.1
QCGL	QCG	57	-48.8	797.5	0.4	1.3	9.0	25.8	0.3
Thu Duc Housing	TDH	35	N/A	16.7	2.4	5.1	26.7	9.4	0.5
First Real	FIR	21	95.9	N/A	N/A	N/A	8.8	6.2	2.1
Netland Real Est	NRC	20	117.6	2.4	N/A	N/A	-3.2	6.7	3.0
Simple average			**233.4**	**143.3**	**6.2**	**15.8**	**26.0**	**13.4**	**1.8**
Median			**52.0**	**52.1**	**5.7**	**15.8**	**13.1**	**9.5**	**1.9**

Source: VNDIRECT

NAM LONG INVESTMENT CORP (NLG)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND25,450	VND37,700	2.0%	ADD	REAL ESTATE

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

Tho Dien Hong

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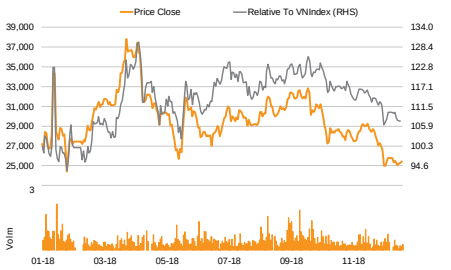
Key changes in the report

- Reduced 35.3% FY18F contracted value
- Increased 43.9% FY18F land transfer revenue

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	37,809
52w low (VND)	24,423
3m Avg daily volume (shares)	377,475
3m Avg daily value (VNDmn)	10,673
Market cap (VNDbn)	6,086
Outstanding shares (m)	239
Free float (%)	46.3
TTM P/E (x)	6.1
Current P/B (x)	1.3

Ownership

Nguyễn Xuân Quang	13.5%
Ibeworth Pte. Ltd.	10.0%
PYN Elite Fund	5.3%
Others	71.2%

Source: VNDIRECT

We remain overweight on NLG's FY19F presales prospects given the clean legal status of its new projects even as competitors are mired in regulatory red-tape. The recent price correction does not stem from a worsening of company fundamentals in our view, and has increased the potential upside to 48.1% based on our TP.

Project delay has led to haircut of our FY18F presales estimate. We estimated a 29.2% fall in FY18 presales value due to the unexpected absence of contribution from the Akari project, delayed until 3Q19 due to construction licenses not being secured in time. Therefore, Novia was the only new launch in 2018 and was sold out in Nov 2018. We haircut by 30.8% our FY18 estimated presales to VND3,415bn, which would be mostly contributed by Mizuki, Novia, and Ehome Nguyen Son with 2,378 units sold in total.

Project licenses bode well for FY19F launches. 1,862 mid-range Akari apartments will be ready for presale in 3Q19 and we expect a take-up rate of 83.3% on the project. In the same quarter, NLG will also prepare to launch Phase 2 of Mizuki Flora condo which saw 1,000 condo units sold in 2Q18. We expect total FY19 presale value to surge by 140% yoy helped by the low base effect caused by the Akari delay.

New land parcel acquired in Dec to support long term growth. NLG fully paid VND1,200bn for a 45ha land site on Dai Phuoc island (Dong Nai), a part of the new self-contained satellite township close to HCMC. The company is also currently in the process of acquiring another 22ha land site in Hai Phong for landed property development. NLG expects to release the development plan for these land sites in mid-2019. This will boost long-term presales growth

Maintain Add as Akari delay offset by enlarged launch volume. We raise our TP slightly to VND37,700 based on a 10% discount to our revised RNAV valuation. Akari's delay has not yet impacted our valuation thanks to a faster presale schedule in our view on the back of a doubling of launch volume versus the previous plan. A key risk to our call is a potential increase in mortgage rates which could curb buyer appetite for mid-range condos.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	2,534	3,161	3,448	2,734
Revenue growth	101.3%	24.8%	9.1%	(20.7%)
Gross margin	32.5%	41.0%	41.3%	34.0%
EBITDA margin	19.4%	30.5%	34.1%	42.0%
Net profit (bn)	345	535	705	833
Net profit growth	67.4%	55.0%	31.8%	18.1%
Recurring profit growth	67.0%	(59.9%)	182.0%	62.5%
Basic EPS	1,993	2,927	3,647	3,977
Adjusted EPS	1,861	2,693	3,417	3,758
BVPS	14,311	15,208	24,024	23,906
ROAE	14.7%	19.8%	18.6%	16.6%

Source: VNDIRECT

PROJECT LICENCING STATUS BODES WELL FOR FY19 LAUNCHES

Updated project pipeline

Newly acquired 42ha land site in Dai Phuoc Island – Dong Nai province is designated for Valora villas from 2020 onwards. The land is fully compensated and ready for construction once the license is approved. The project would be NLG's second satellite township project after Waterpoint and the developer is betting on the new bridge link to HCMC to cut travel time to the island and eventually boost the property's value. FY19 will see two new project launches from Waterpoint (Phase 1) and Akari with LUR licenses fully paid for and landfill and foundation works prior to presales already in progress.

Figure 123: Project development pipeline (from launch to delivery)

Project Name	Location	Sub-project	Owner-ship	Land site (ha)	GFA (sqm)	2016	2017	2018	2019	2020	2021	2022	2023	2024
Fuji	Dis. 9, HCMC	Valora	50%	5.6	70,060									
		Flora												
Kikyo	Dis. 9, HCMC	Valora	50%	17.8	34,820									
		Flora												
		Ehomes	100%		77,834									
Dalia	Can Tho	Land lot	75%	15.4	65,627									
Mizuki	Binh Chanh, HCMC	Valora	50%	26.4	446,927									
		Flora												
Nguyen Son	Binh Chanh, HCMC	Ehomes	87%	11.0	108,881									
		Villa island												
Akari	Binh Tan, HCMC	Flora	50%	8.8	397,345									
Novia	Thu Duc, HCMC	Flora	100%	1.1	43,878									
Waterpoint	Long An	Land lot	50%	165.0	283,725									
		Townhouse			116,928									
		Villa			132,300									
		Phase 2	100%	190.0	N/A									
Nam Long 2	Can Tho	Land lot	100%	43.0	N/A									
Dai Phuoc	Dong Nai	Valora/Land lot	100%	45.0	N/A									

Source: VNDIRECT, NLG

Forecast revision

We reduce our FY18 estimated presales value by 30.8% to reflect the delayed launch of Akari condos from 4Q18 to 3Q19 due to the doubling of the number of condos planned for launch and the delay in obtaining construction approval. The entire Phase 1 (Six blocks of condos) with total volume of 1,862 units will be launched in 3Q19. The delay, however, barely impacts our projected cash collections from this project as there will likely be a higher sales volume per annum as a result of the accelerated launch plan under which the presale period is being shrunk from 5 to 3 years. We cut our previous forecast for FY19F presales at Waterpoint and Mizuki by 42.8% and 33.3% respectively to account for the company's newly launch schedule for these two projects which calls for lower launch packages. This reduces by 2.3% our FY19 total presales value forecast despite the projected increase in presales at Akari this year.

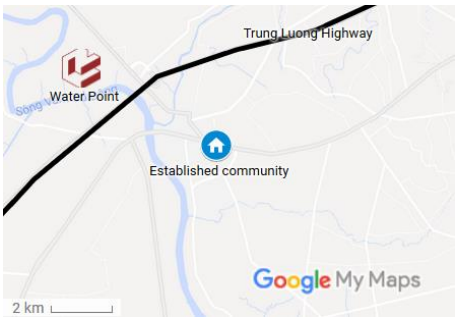
We also raise 89% our projected land transfer profit – a result of the re-casting of Waterpoint as a BCC project – to VND297bn in FY18F. We also expect NLG to book VND195bn in financial gains from transferring the remaining 30ha in Waterpoint and 88ha in Akari to BCC joint-ventures in FY19F. We revise up by 12.5% our estimated FY18F net profit to VND705bn since the Waterpoint land transfer was completed faster than we had expected. We move 50% of total deliveries at the Novia project from FY19F to FY20F in our model to account for delays in construction works but we add VND993bn from land lot deliveries at Waterpoint to this year's forecasts. FY19F delivery value will mostly be contributed by Mizuki and Nguyen Son, with 2,427 units handed over and VND3,640bn booked in the topline. FY19F net profit is projected to surge 18.1% yoy due to the larger delivery volume countering the reduction in land transfer profit.

Figure 124: Forecast revision

VNDbn	New				Old			Change		
	FY2017A	FY2018F	FY2019F	FY2020F	FY2018F	FY2019F	FY2020F	FY2018F	FY2019F	FY2020F
Presale volume (units)	2,954	2,378	3,822	3,259	3,438	3,722	3,335	-30.8%	2.7%	-2.3%
Presale value (VNDbn)	4,822	3,415	8,196	6,852	5,280	8,392	7,352	-35.3%	-2.3%	-6.8%
Handover volume (units)	1,647	1,989	2,427	2,704	1,989	2,461	2,996	0.0%	-1.4%	-9.7%
Handover value (VNDbn)	2,243	2,795	3,640	6,810	2,695	3,209	7,717	3.7%	13.4%	-11.8%
Net sales	**3,161**	**3,448**	**2,734**	**695**	**3,019**	**2,382**	**2,715**	**14.2%**	**14.8%**	**-74.4%**
Property delivery	2,243	2,496	1,800	502	2,396	2,301	2,626	4.2%	-21.8%	-80.9%
Project transfer	838	792	759	-	550	-	-	43.9%		
Other	83	160	176	194	73	80	88	119.2%	119.2%	119.2%
Gross profit	**1,295**	**1,423**	**929**	**178**	**1,152**	**826**	**1,016**	**23.5%**	**12.4%**	**-82.5%**
Gross margin	*41.0%*	*41.3%*	*34.0%*	*25.6%*	*38.2%*	*34.7%*	*37.4%*	*3.1% pts*	*-0.7% pts*	*-11.8% pts*
SG&A expenses	(414)	(385)	(340)	(230)	(395)	(412)	(451)	-2.5%	-17.5%	-48.9%
Operating profit	881	1,038	588	(52)	757	414	565	37.1%	42.2%	-109.2%
Financial income	95	153	577	1,555	385	507	229	-60.3%	13.8%	579.9%
Financial expense	(29)	(59)	(70)	(70)	(59)	(70)	(70)	0.0%	0.0%	0.0%
Profit/loss in JV/associates	(3)	-	-	-	10	120	1,148	-100.0%	-100.0%	-100.0%
PATMI	**535**	**705**	**833**	**1,147**	**627**	**778**	**1,114**	**12.5%**	**7.0%**	**3.0%**

Source: VNDIRECT

Figure 125: Waterpoint is not far from the nearest established town.



Source: Google maps, VNDIRECT

Valuation

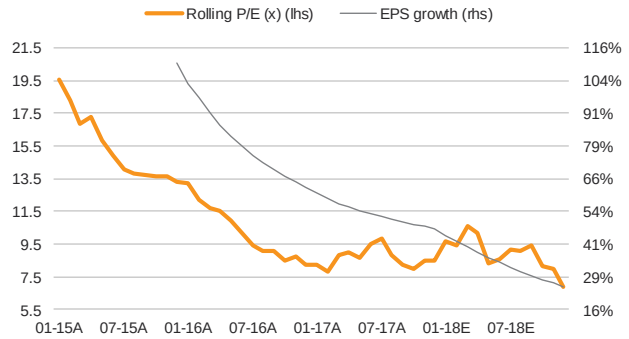
The stock price has fallen 12.3% since our last update, widening the upside to 48.1% based on our RNAV-based TP of VND37,700. Based on our financial model, Waterpoint should be the leading driver of stock performance as the project now contributes 40.3% to our total RNAV. The improved prospects of this project are related to its improved connectivity to key transport routes to HCMC. The management is now targeting buyers from both HCMC and the nearby town (Ben Luc-Long An) as its economy is expanding with increasing industrial activity in the area. We believe that strong market take-up at the anticipated launch in 3Q19F could remove investor scepticism about demand for this project and, thereby, trigger a re-rating of the stock.

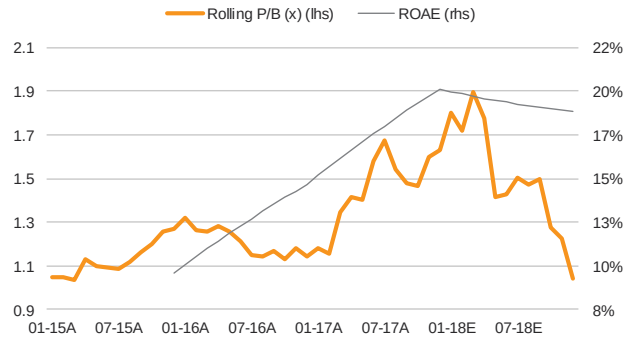
Figure 126: Equity Valuation (VNDbn)

Project Name	BV as at 30 Sep 2018 (VNDbn)	Premium (VNDbn)	Fair value (VNDbn)	Method	Note
Water Point	862	3,195	4,057	Market value	Phase 2 land value is based on the Phase 1 transfer price of VND1.2m/sq m annouced by the management
Fuji	24	3	27	DCF	
Nguyen Son & Mizuki	572	283	855	DCF	
Areco (Irish)	197	136	333	DCF	
Kikyo	353	330	682	DCF	
Dalia	10	82	92	DCF	
Akari (Hoang Nam)	804	765	1,569	DCF	A 50% stake of the 8.8ha will be transferred to the other partner, based on the announced price of VND14.7m/sq m
Other	325		325	Book value	
Total inventory	**3,147**	**4,794**	**7,941**		
Add:					
Cash and cash equivalent			2,847		
Short-term investments			0		
Short-term receivables			894		
Other short-term assets			0		
Long-term assets			2,139		
Less:					
Net debt (exclude CB)			1,067		
Other liabilities			3,027		
Minority interest			738		
RNAV			**10,037**		
Shares outstanding (m)			**239**		
Discount to RNAV			**10%**		Compensates for execution and pre-sale risks at projects Waterpoint, Mizuki and Akari
Target price (VND/share)			**37,700**		

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	3,161	3,448	2,734
Cost of sales	(1,866)	(2,024)	(1,806)
Gen & admin expenses	(195)	(194)	(232)
Selling expenses	(219)	(191)	(108)
Operating profit	**881**	**1,038**	**588**
Operating EBITDA	868	1,023	573
Depreciation and amortisation	**14**	**15**	**16**
Operating EBIT	**881**	**1,038**	**588**
Interest income	95	153	577
Financial expense	(29)	(59)	(70)
Net other income	6	0	0
Income from associates & JVs	(3)	0	0
Pre-tax profit	**950**	**1,132**	**1,096**
Tax expense	(194)	(226)	(219)
Minority interest	(221)	(200)	(44)
Net profit	**535**	**705**	**833**
Adj. net profit to ordinary	535	705	833
Ordinary dividends	(71)	(71)	(112)
Retained earnings	**464**	**634**	**721**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	2,082	2,257	819
Short term investments	61	61	61
Accounts receivables	579	609	544
Inventories	3,884	4,643	4,003
Other current assets	173	106	92
Total current assets	**6,779**	**7,676**	**5,518**
Fixed assets	56	50	43
Total investments	755	4,672	5,430
Other long-term assets	315	726	325
Total assets	**7,906**	**13,123**	**11,317**
Short-term debt	216	234	209
Accounts payable	291	316	282
Other current liabilities	2,553	5,277	2,656
Total current liabilities	**3,061**	**5,827**	**3,147**
Total long-term debt	700	834	784
Other liabilities	423	780	983
Share capital	1,572	2,240	2,240
Retained earnings reserve	864	1,226	1,902
Shareholders' equity	**2,920**	**4,680**	**5,356**
Minority interest	803	1,003	1,047
Total liabilities & equity	**7,906**	**13,123**	**11,317**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**950**	**1,132**	**1,096**
Depreciation & amortisation	14	15	16
Tax paid	(238)	(226)	(219)
Other adjustments	(145)	(196)	(621)
Change in working capital	**1,681**	**1,968**	**(1,336)**
Cash flow from operations	**2,261**	**2,693**	**(1,064)**
Capex	(6)	(4)	(4)
Proceeds from assets sales	1	0	0
Others	(781)	(3,764)	(181)
Other non-current assets changes			
Cash flow from investing activities	**(786)**	**(3,768)**	**(186)**
New share issuance	78	706	0
Shares buyback	(20)	(10)	0
Net borrowings	217	623	0
Other financing cash flow	(476)	0	(75)
Dividends paid	(123)	(71)	(112)
Cash flow from financing activities	**(324)**	**1,249**	**(187)**
Cash and equivalents at beginning of period	932	2,082	2,257
Total cash generated	**1,151**	**174**	**(1,438)**
Cash and equivalents at the end of period	2,082	2,257	819

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	16.9%	20.5%	30.5%
Asset turnover	0.45	0.33	0.22
ROAA	7.6%	6.7%	6.8%
Avg assets/avg equity	2.61	2.77	2.44
ROAE	19.8%	18.6%	16.6%
Efficiency			
Days account receivable	26.2	26.2	26.2
Days inventory	760	837	809
Days creditor	57.0	57.0	57.0
Fixed asset turnover	56.6	64.8	58.6
ROIC	11.5%	10.4%	11.3%
Liquidity			
Current ratio	2.21	1.32	1.75
Quick ratio	0.95	0.52	0.48
Cash ratio	0.70	0.40	0.28
Cash cycle	729	806	778
Growth rate (yoy)			
Revenue growth	24.8%	9.1%	(20.7%)
Operating profit growth	83.6%	17.8%	(43.3%)
Net profit growth	55.0%	31.8%	18.1%
EPS growth	46.9%	24.6%	9.1%
Share value			
Basic EPS (VND)	2,927	3,647	3,977
BVPS (VND)	15,208	24,024	23,906

Source: VNDIRECT

VINHOMES JSC (VHM)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND76,600	N/A	0.0%	NOT RATED	REAL ESTATE

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Tho Dien Hong
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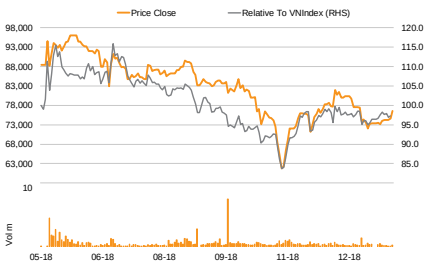
9M18 pro forma net profit surged 143% yoy on the back of robust property delivery and strong project transfer gains. The stellar launch of Vincity Ocean Park with a 70% absorption rate was proof of the continued thirst for affordable and mid-range products.

In 10M18 the company recorded a total VND52.7tr in handover value (+161% yoy) from both consolidated projects and projects under Business Cooperation Contracts (BCC) signed with Vingroup. The major deliveries were at Harmony, Golden River, Imperia, Green Bay, and Central Park. Consolidated gross margin contracted by 708 bp yoy because of the lower margin on delivery of lower-priced units at key projects like Golden River and Central Park.

10M18 presales was sizable with Vincity launch but tracking below 2017 levels. VHM launched four projects in Hanoi, Thanh Hoa and Ha Tinh with approximately 522 units contracted, equal to a 35% take-up rate in 10M18. Vincity Ocean Park in Hanoi also opened 7,549 condo units for non-cancellable deposit booking in Oct 2018 and 70% of the amount was taken up at an ASP of VND30m/sq m. This is a 10-15% premium on prices for comparable projects. In total, there were signed sales contracts or non-cancellable deposit agreements worth ~VND8.7tr for Vincity Ocean Park. Including presales from Vinhomes projects, 10M18 total contracted/deposited sale value amounted to VND33.1tr, 48% of the FY17 figure. Unbooked presales backlog amounted to VND56.8tr at the end of 10M18.

Aggressive launch schedule for FY19F. After the launch of Vincity Ocean Park in Nov 2018, Vinhomes Cau Rao (Hai Phong) was launched in Dec 2018 with ~1,187 villas, translating to VND6.4tr in GDV to be booked over 2018-20F. In 2019, the company will launch ten more Vinhomes projects and two Vincity projects. Most of them will be in Hanoi. The GDV of these new projects for FY19-23F calculated from the company's expected selling prices for these units is pegged at VND186tr, of which 47% will be from condo units and equivalent to 7.6x of FY18G revenue.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	96,000
52w low (VND)	61,800
3m Avg daily volume (shares)	578,054
3m Avg daily value (VNDmn)	42,862
Market cap (VNDbn)	259,572
Outstanding shares (mn)	3,350
Free float (%)	10.4
TTM P/E (x)	23.6
Current P/B (x)	2.8

Ownership

Vingroup JSC	69.7%
GIC	5.7%
Others	24.6%

Source: VNDIRECT

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	6,513	4,920	11,217	15,297
Revenue growth	(7.2%)	(24.5%)	128.0%	36.4%
Gross margin	25.7%	33.2%	39.7%	33.8%
EBITDA margin	18.3%	28.9%	31.5%	22.4%
Net profit (bn)	499	795	1,649	1,410
Net profit growth	(55.1%)	59.4%	107.3%	(14.5%)
Recurring profit growth	(46.7%)	(1.2%)	166.4%	4.6%
Basic EPS	665	1,060	2,198	1,880
Adjusted EPS	665	1,060	2,198	1,880
BVPS	3,531	4,540	2,936	9,206
ROAE	17.0%	26.3%	58.8%	31.0%

Source: VNDIRECT

2018F likely to have been a bonanza year

The 9M18 bottom line registered 143% growth versus the pro-forma 9M17 results with large profits booked from key projects and stake transfer of Vinhomes Lotus. VHM's management is confident it will meet its full-year net profit target of VND17.6tr (+260% versus pro-forma FY17) mostly by booking the remaining contracted value of the abovementioned projects, the first batch of Vinhomes Metropolis deliveries and project transfer gains worth VND800 bn from the sale of Vinhomes Dinh Tien Hoang to a third party.

Figure 127: VHM's 9M18 financial results

VNDbn	3Q18	yoy	9M18	yoy	vs. pro-forma 9M17*	Vs. FY18F guidance
Revenue	6,878	0%	22,405	86%	16%	91%
Property handover	*5,534*	-9%	*20,329*	106%	8%	
Other	*1,345*	62%	*2,077*	-5%	394%	
Gross profit	2,665	-3%	6,991		-5%	
Gross margin	39%	-1.2 % pt	31%	-8.5 % pt	-7.1 % pt	
Financial income	3,685	2348%	11,036	1670%		
Profit from BCC projects	*1,305*		*7,016*		966%	
Project transfer	*1,992*		*3,028*	*1197%*		
Financial expense	(718)	80%	(1,643)	96%		
Pre-tax profit	5,126	186%	15,101	393%	147%	69%
Net profit	3,848	176%	11,887	395%	143%	68%

(*) To reflect Vinhomes projects under Vingroup prior to transfer to VHM in 1H18.

Source: Company reports

Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	4,920	11,217	15,297
Cost of sales	(3,286)	(6,764)	(10,131)
Gen & admin expenses	(500)	(884)	(453)
Selling expenses	(417)	(1,298)	(1,586)
Operating profit	718	2,272	3,128
Operating EBITDA	897	2,627	3,539
Depreciation and amortisation	(179)	(355)	(410)
Operating EBIT	718	2,272	3,128
Interest income	89	822	964
Financial expense	(264)	(947)	(1,652)
Net other income	274	143	(243)
Income from associates & JVs	161	505	(88)
Pre-tax profit	978	2,795	2,109
Tax expense	(187)	(588)	(543)
Minority interest	3	(559)	(156)
Net profit	795	1,649	1,410
Adj. net profit to ordinary	795	1,649	1,410
Ordinary dividends			
Retained earnings	795	1,649	1,410

Balance sheet

(VNDbn)	**12-15A**	**12-16A**	**12-17A**
Cash and equivalents	557	2,802	1,562
Short term investments	418	0	0
Accounts receivables	3,906	4,616	24,775
Inventories	6,146	8,475	17,006
Other current assets	1,349	599	1,079
Total current assets	**12,377**	**16,492**	**44,421**
Fixed assets	3,347	8,096	3,818
Total investments	8,858	10,542	1,755
Other long-term assets	726	2,391	1,310
Total assets	**25,307**	**37,521**	**51,304**
Short-term debt	3,887	9,157	8,700
Accounts payable	828	1,666	925
Other current liabilities	12,315	16,006	24,598
Total current liabilities	**17,031**	**26,828**	**34,223**
Total long-term debt	1,085	0	6,628
Other liabilities	63	1,143	329
Share capital	2,000	2,000	2,000
Retained earnings reserve	1,446	2,971	5,003
Shareholders' equity	**3,405**	**2,202**	**6,904**
Minority interest	3,723	7,347	3,220
Total liabilities & equity	**25,307**	**37,521**	**51,304**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	978	2,795	2,109
Depreciation & amortisation	179	355	410
Tax paid	(265)	(344)	(872)
Other adjustments	(584)	(482)	812
Change in working capital	8,514	2,417	337
Cash flow from operations	8,822	4,741	2,796
Capex	(738)	(2,222)	(2,405)
Proceeds from assets sales	(9,207)	75	34
Others	1,444	(7,974)	(7,088)
Other non-current assets changes	0	0	0
Cash flow from investing activities	(8,500)	(10,121)	(9,459)
New share issuance	3,361	3,393	28
Shares buyback	0	0	0
Net borrowings	(3,092)	4,572	5,394
Other financing cash flow	0	0	0
Dividends paid	(340)	(340)	0
Cash flow from financing activities	(71)	7,625	5,422
Cash and equivalents at beginning of period	306	557	2,802
Total cash generated	251	2,246	(1,241)
Cash and equivalents at the end of period	557	2,802	1,562

Key ratios

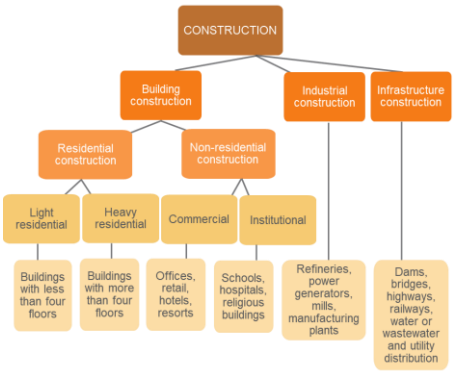
	12-15A	12-16A	12-17A
Dupont			
Net profit margin	16.2%	14.7%	9.2%
Asset turnover	0.24	0.36	0.34
ROAA	3.9%	5.2%	3.2%
Avg assets/avg equity	6.7	11.2	9.8
ROAE	26.3%	58.8%	31.0%
Efficiency			
Days account receivable	9	14	285
Days inventory	683	459	613
Days creditor	91.9	90.2	33.3
Fixed asset turnover	1.63	1.96	2.57
ROIC	6.6%	8.8%	5.5%
Liquidity			
Current ratio	0.73	0.61	1.30
Quick ratio	0.37	0.30	0.80
Cash ratio	0.06	0.10	0.05
Cash cycle	599	382	864
Growth rate (yoy)			
Revenue growth	(24.5%)	128.0%	36.4%
Operating profit growth	(34.1%)	216.4%	37.7%
Net profit growth	59.4%	107.3%	(14.5%)
EPS growth	59.4%	107.3%	(14.5%)
Share value			
Basic EPS (VND)	1,060	2,198	1,880
BVPS (VND)	4,540	2,936	9,206

Source: VNDIRECT

CONSTRUCTION: SLOWDOWN IN INFRA AND RESIDENTIAL SEGMENT BUT INDUSTRIAL AND NON-RESIDENTIAL BUILDING SHOW VIGOR

Residential building construction companies are changing their focus to affordable condos instead of high-end condos but face headwinds and possible margin compression in this segment

Figure 128: Construction industry segments



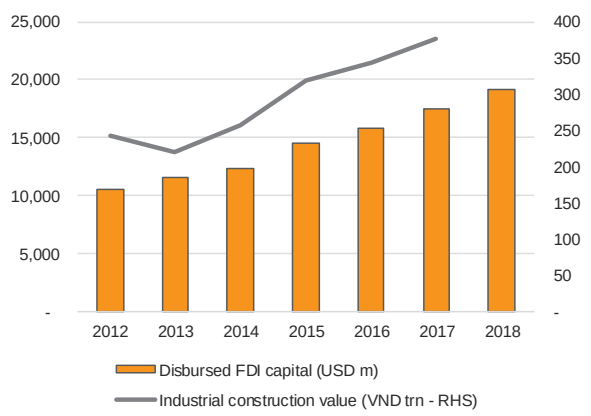
Source: VNDIRECT

According to our real estate team's analysis, in 2019, residential market demand will be focused on affordable, mid-range condos and landed property. As such, residential building contractors must win more affordable and mid-range condo projects to maintain their backlog, despite lower gross margins for such projects as compared with high-end condo projects. For example, construction of Vincity, which is a mega, affordable mid-range condo project by Vingroup (VIC VN: Non-rated), has just begun in 4Q2018 with top contractors including Coteccons (CTD VN: Non-rated) and Hoa Binh Group (HBC VN: Non-rated) both providing construction services. Both contractors have admitted that the project has a lower profit margin as compared to their other projects (Vincity GPM is around 6% vs. non-Vincity GPM of around 8.7%) but it is a sizable project that contributes greatly to the order backlog of both contractors.

Despite great medium and long-term growth potential, we are neutral on the residential building construction segment in 2019. Top contractors such as CTD and HBC have disclosed that the tightening of the legal approval process (detailed in the Real Estate section of this report) for new projects starting around the middle of 2018 has delayed many of their heavy residential building projects. We do not see any new policy measures to solve the problem and anticipate that this will continue into 2019, creating difficulties for heavy residential building contractors. According to BMI Research, residential building construction will grow 9.8% in 2019, down 1.7% pts from the estimated growth rate in 2018.

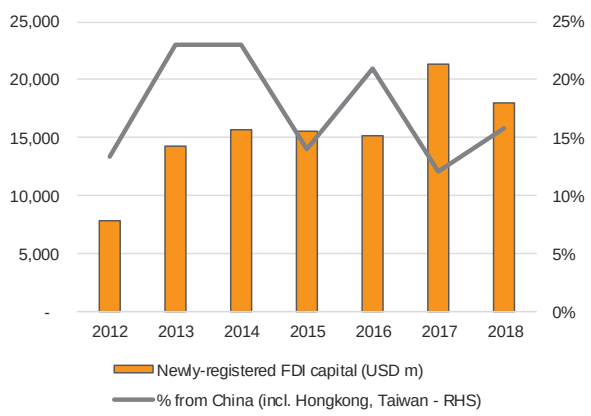
Industrial construction will be boosted significantly by rising FDI flows into Vietnam, especially after the US-China trade war

Figure 129: FDI flow and industrial construction value



Source: VNDIRECT, GSO

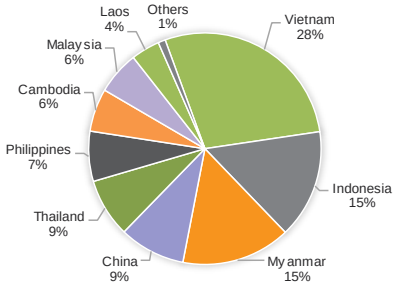
Figure 130: FDI flow and the proportion from China



Source: VNDIRECT, GSO

Vietnam is wooing foreign investors more than ever with a mixture of tax incentives and facilitated by lower wages, a large labour pool, improving infrastructure, political stability and a long coast line along one of the busiest maritime routes in the world.

Figure 131: Results of a survey on the favourite Investment destination in Southeast Asia and neighboring region (04/2018)



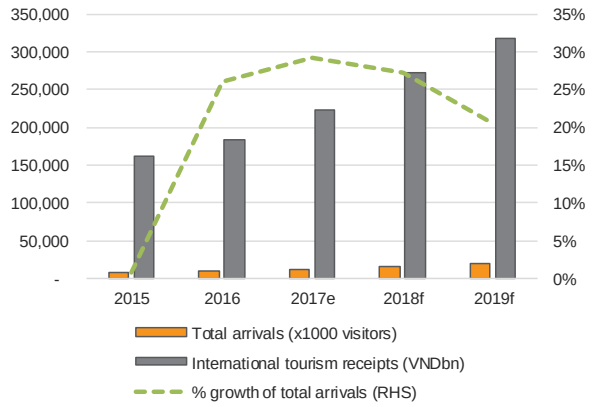
Source: VNDIRECT, GRANT THORNTON

Though the trade war is helping Vietnam attract more FDI, the shift of manufacturing jobs from China to Vietnam has been occurring for the last few years and is not a short-term trend. In addition to the South Korean companies like Samsung and LG that are both producing in Vietnam, many garment, textile and footwear companies that have operations in China have also moved a large part of their production to Vietnam over the last few years. We believe that any further escalation of the US-China trade war could accelerate FDI flow from China into Vietnam and also spur more multinationals to add future capacity in Vietnam, instead of China.

This will boost industrial construction activity and greatly benefit industrial construction contractors. In fact, in 9M2018 results, top contractors such as CTD and HBC already reported a huge upsurge in industrial construction contribution in their revenue mix. According to BMI Research, industrial construction will grow by 12% in 2019, accelerating by 1.1% pts from the estimated growth rate in 2018.

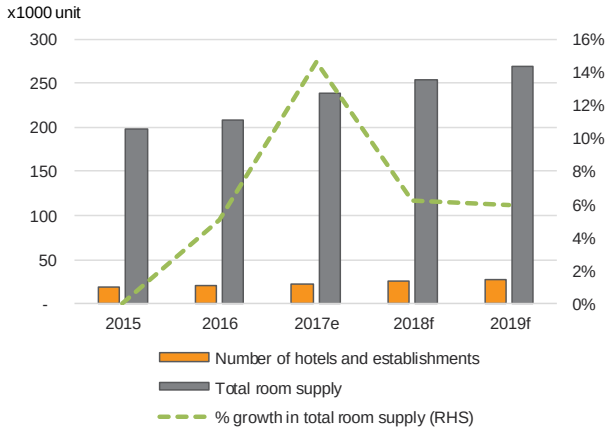
Hotel & resort segment will be boosted by robust tourism growth

Figure 132: International visitors and their spending in Vietnam



Source: VNDIRECT, FITCH SOLUTIONS REPORT

Figure 133: Number of hotel rooms in Vietnam



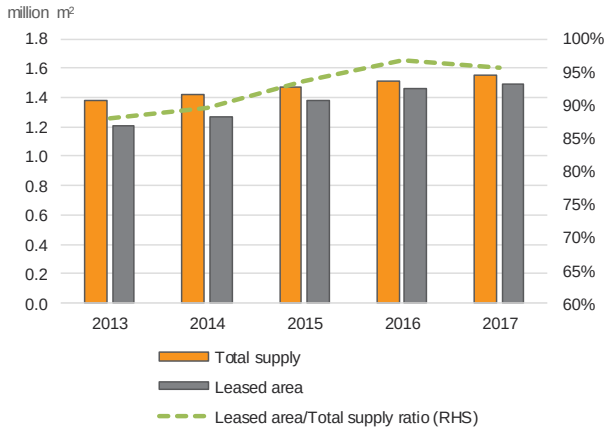
Source: VNDIRECT, FITCH SOLUTIONS REPORT

In general, the recent high growth rates of Vietnam's tourism industry are a result of the government's tourism-friendly policies and aggressive promotional activities. The country offers easy visa procedures for a host of countries while the growth of low-cost carriers in the region is making it cheaper to get to and from Vietnam. The country's generally low cost for hotels, food, transportation and sightseeing is an added advantage especially as Chinese tourists look to trade down to cheaper holiday destinations in response to a worsening economic environment in China. Furthermore, in the short-term, the weakening Vietnam Dong will help to ensure that the industry remains competitive within the Southeast Asia tourism space.

The growth in tourism is being reflected in a rising demand for and investment in tourism-related construction projects, particularly in hotels and resorts. We maintain a positive view on this segment for 2019. According to BMI Research, the hotel and resort construction segment will grow 14.3% in 2019, accelerating by 2.7% pts from the 2018 estimated growth rate.

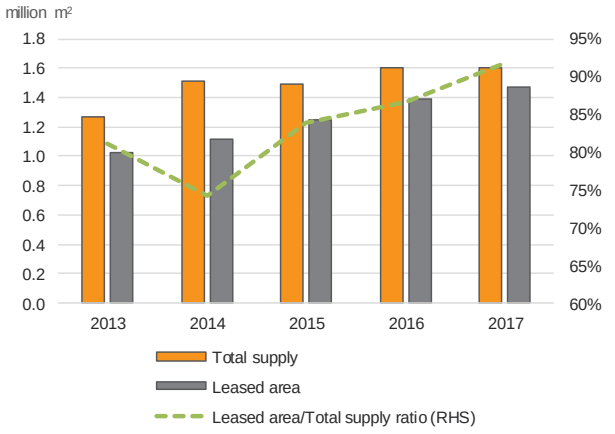
The office building market is characterised by limited supply, rising demand and low vacancy rates

Figure 134: HCMC total office supply and leased area



Source: VNDIRECT, SAVILLS

Figure 135: Hanoi total office supply and leased area



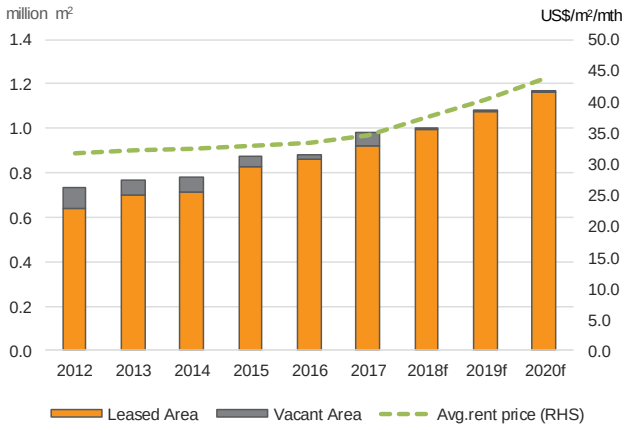
Source: VNDIRECT, SAVILLS

Figure 136: Regional office property market performance in 2017 (Size/Occupancy/Rents)

	Total supply (million m²)	Occupancy	Gross rent (US$/m²/mth)
Bangkok (Thailand)	9	92%	29
Hanoi (Vietnam)	2	92%	35
HCMC (Vietnam)	2	96%	48
Kuala Lumpur (Malaysia)	10	79%	24
Manila (Philippines)	6	97%	31
Jakarta (Indonesia)	10	80%	37

Source: VNDIRECT, SAVILLS

Figure 137: HCMC office space supply forecast (Grade A & B)



Source: VNDIRECT, SAVILLS

HCMC and Hanoi are the most developed cities in Vietnam and contributed about 45% to Vietnam's GDP in 2017. As a result, major economic activities are concentrated in these two cities and they account for the majority of the office rental market of Vietnam.

With robust economic growth over the past few years, demand for office rental space increased significantly while supply was very limited. Despite the projected shortage of office supply in 2019-20, the ongoing investigation of corruption and real estate-related offenses, as well as shortage of land bank in HCMC and Hanoi will hold back the growth of this segment in 2019. We are neutral on the office segment in 2019 although BMI Research foresees that the office construction segment will grow 14.3% in 2019, up 2.7% pts from the 2017 estimated growth rate.

The government has large-scale infrastructure development plans despite a lack of near-term funding

Due to difficulties in capital disbursement from the government and shrinking concessional loans, the government is increasingly relying on PPP contracts to attract private investment as a funding source for infrastructure development. Although the government is working to meet international standards, there are still many inadequacies in the

implementation process in PPP contracts. The representatives of top listed infrastructure companies shared with us that they do not participate in BOT projects at the moment unless there is a paucity of non-PPP projects. Therefore, we maintain a fairly negative view on the infrastructure segment in 2019 until the government can address the issue of insufficient funding for infrastructure development. According to BMI Research, the infrastructure construction segment will grow 9.6% in 2019, down 1.2% pts from last year's estimated growth rate.

Figure 138: Major mega infrastructure projects

	Investment Value (VND billion)	Length (km)	Project Duration	Status
Vietnam expressway and ring road network	**1,300,000**	**6,411**	**2017 - N/A**	**-**
Phase 1	500,000	2,703	2017 - 2021	Under construction
Phase 2	500,000	2,699	2021 - 2025	At planning stage
Phase 3	300,000	1,009	After 2030	At planning stage
North-South high speed railway	**1,300,000**	**1,545**	**2020 - 2045**	**At planning stage**
Hanoi Metro project (8 lines)	**930,000**	**318**	**2011 - N/A**	**Under construction**
HCMC Metro project (8 lines)	**500,000**	**173**	**2007 - N/A**	**Under construction**
Long Thanh International Airport	**425,000**	**N/A**	**2019 - 2050**	**-**
Phase 1	180,000	N/A	2019 - 2025	At planning stage
Phase 2	86,000	N/A	2025 - 2035	At planning stage
Phase 3	159,000	N/A	2035 - 2050	At planning stage
Total value	**4,455,000**			

Source: VND RESEARCH

Falling steel prices in 2019 can improve margins of contractors

We think that rebar steel prices may fall with decreasing raw material input prices in 2019 (more details in the Materials section) and a sizable increase in supply. We forecast that rebar steel prices will fall at least 10% yoy in 2019. This may help construction companies improve their margins, in our opinion.

Figure 139: TTM P/E of Vietnam construction sector is lower than peers' (as of 03/12/2018)

India	25.4
Singapore	17.8
Malaysia	14.6
Japan	13.5
China	11.1
Indonesia	10.7
Vietnam	**9.9**

Source: VNDIRECT, BLOOMBERG

Construction companies have been heavily net-sold this year

Increasing rebar steel prices (+19% yoy), higher social insurance costs and the slowdown in real estate have all contributed to a negative perception of the construction industry in 2018. Moreover, the market is weary of an oversupply of high-end condos and this has weighed on the valuations of high-end condo contractors. Unfortunately, the two largest listed contractors in Vietnam, CTD and HBC (collectively accounting for 42% of the construction industry's market capitalization), specialise in high-end condo construction. In 2018, their share prices have declined: 39% for HBC and 27% for CTD. That is one major reason why construction was the worst performing sector in 2018 falling by 37.9% while the VN-Index fell by 9.3%.

Figure 140: Construction industry share and rating by segment

	2017 Value share	Rating
Residential building segment	40%	Neutral
Industrial segment	32%	Positive
Non-residential building segment	17%	Neutral
Hotel & Resort		*Positive*
Office		*Neutral*
Infrastructure segment	11%	Negative
Overall		**Neutral**

Source: VNDIRECT

CONSTRUCTION STOCK PICKS: WE LIKE CTD AS IT IS THE LARGEST AND MOST FAVOURED CONTRACTOR AMONG MAJOR PROPERTY DEVELOPERS

We are overall **Neutral** on the Vietnam construction industry in 2019. However, we place Coteccon **(CTD VN, Not rated)** on our watchlist because of: 1) its strong presence in the non-infrastructure segment, 2) its existing presence in or ability to easily move into construction segments with good growth prospects -- industrial and hotels & resorts, and 3) good asset quality with a large amount of cash to fund working capital as credit tightens.

Figure 141: Construction peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
Coteccons Jsc.	CTD VN	527	-0.9%	0.6%	10.9%	21.6%	0.0	7.5	1.5
Hoa Binh Group	HBC VN	140	-13.5%	-4.2%	5.3%	28.7%	1.8	4.4	1.3
Construction Jsc. No.5	SC5 VN	18	-50.4%	-29.3%	2.0%	11.8%	1.4	10.5	1.2
Tanky Construction Corporation	TKC VN	13	-82.2%	-21.5%	2.0%	11.1%	1.1	16.2	1.7
Average		**175**	**-36.7%**	**-13.6%**	**5.0%**	**18.3%**	**1.1**	**9.6**	**1.4**
Median		**79**	**-32.0%**	**-12.8%**	**3.6%**	**16.7%**	**1.2**	**9.0**	**1.4**

Source: VNDIRECT, FiinPro

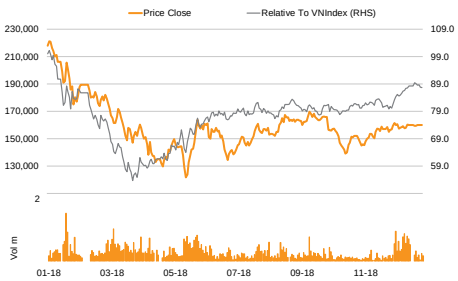
COTECCONS JSC (CTD)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND158,500	NOT RATED	3.12%	NOT RATED	INDUSTRIALS

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Nguyen Xuan Hung
hung.nguyenxuan@vndirect.com.vn

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	221,000
52w low (VND)	122,000
3m Avg daily volume (shares)	161,830
3m Avg daily value (VNDmn)	24,615
Market cap (VNDbn)	12,395
Outstanding shares (m)	78.2
Free float (%)	55
TTM P/E (x)	7.5
Current P/B (x)	1.5

Ownership

Kustocem Pte. Ltd	18.1%
Nguyen Ba Duong & Management Team	11.3%
Thanh Cong Investment	14.5%
Others	56.1%

Source: VNDIRECT

Coteccons is focusing on non-residential building and industrial construction segments to sustain growth.

Number one contractor in Vietnam's construction industry. Coteccons (CTD VN, Not rated) has been the leading contractor in Vietnam since 2011. Revenue grew 36% yoy to reach VND27,153bn in 2017, equivalent to 2.3% share of Vietnam's construction market.

Favourite contractor of top real estate investors in Vietnam. CTD is the most favoured contractor among Vietnam's top developers and investors such as Hoa Phat (HPG VN, ADD), Vingroup (VIC VN, Not rated), Novaland (NVL VN, Not rated) and Refico (Unlisted). These large companies usually make payments on time and even pre-pay 10-20% of contract value, according to CTD. As such, CTD has the lowest receivables risk relative to its peers, no debt and a huge amount of cash & cash equivalents (VND4,777bn as at 30/09/2018, equal to 32% of total assets and 38% of market cap).

Vincity will contribute significantly from 2019. CTD announced in the latest analyst meeting in October 2018 that it has just started building Vincity. Vincity is the biggest affordable condo project in Vietnam so far (comprising Vincity Gia Lam, Vincity District 9 and Vincity Tay Mo). According to CTD, there are a total of 200 towers with 22-25 floors for each tower. CTD will build 35% of those towers. This project will contribute at least VND5,500bn/year for the next nine years to group revenue. This revenue, on an annual basis, amounts to 20% of CTD's 2017 revenue. Vincity will help to secure revenue growth in the next nine years despite lowering CTD's gross margins (Vincity GPM is around 6% vs. non-Vincity GPM of around 8.7%).

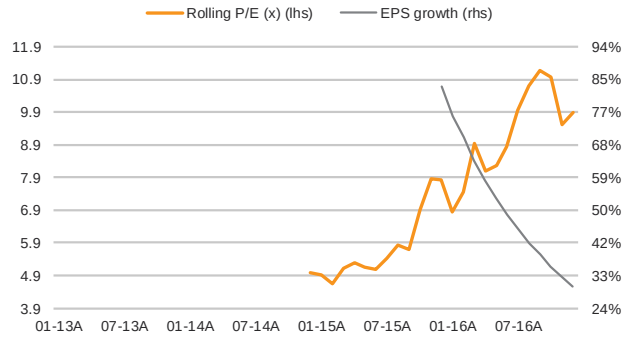
Large backlog creates a strong foundation for the next two years. As of 31/09/2018, CTD's backlog was VND22,065bn (excluding Vincity projects, according to CTD), equal to 81.2% of 2017 revenue.

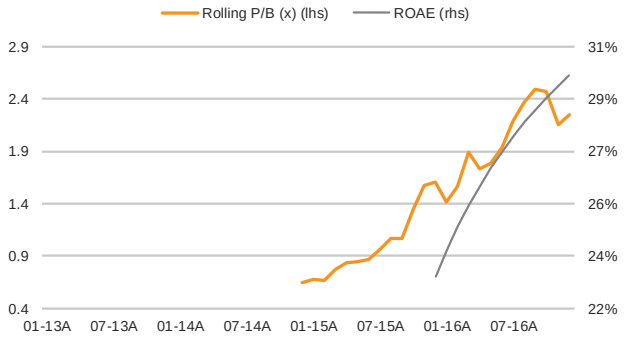
At the current price, CTD is trading at a TTM P/E of 7.5x, which is lower than the company's 5-year average P/E of 8.6x and a significant discount to the regional peer average TTM P/E of 9.1x.

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	7,634	13,669	20,783	27,153
Revenue growth	23.3%	79.1%	52.0%	30.7%
Gross margin	7.3%	8.1%	8.7%	7.4%
EBITDA margin	6.6%	7.1%	8.7%	7.9%
Net profit (bn)	327	666	1,422	1,653
Net profit growth	27.3%	103.5%	113.5%	16.2%
Recurring profit growth	27.3%	103.5%	113.5%	16.2%
Basic EPS	7,757	14,214	18,457	21,449
Adjusted EPS	7,757	14,214	18,457	21,449
BVPS	59,887	69,195	80,901	94,832
ROAE	13.6%	23.1%	30.0%	24.4%

Source: VNDIRECT

Valuation





Income statement			
(VNDbn)	12-15A	12-16A	12-17A
Net revenue	13,669	20,783	27,153
Cost of sales	(12,557)	(18,983)	(25,137)
Gen & admin expenses	(363)	(299)	(395)
Selling expenses	0	0	0
Operating profit	**749**	**1,500**	**1,622**
Operating EBITDA	796	1,555	1,703
Depreciation and amortisation	**(47)**	**(55)**	**(82)**
Operating EBIT	**749**	**1,500**	**1,622**
Interest income	126	170	325
Financial expense	(2)	(0)	(0)
Net other income	39	60	82
Income from associates & JVs	14	33	32
Pre-tax profit	**927**	**1,763**	**2,061**
Tax expense	(194)	(341)	(408)
Minority interest	(67)	0	0
Net profit	**666**	**1,422**	**1,653**
Adj. net profit to ordinary	666	1,422	1,653
Ordinary dividends	(167)	(257)	(383)
Retained earnings	**499**	**1,165**	**1,270**

Cash flow statement			
(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**913**	**1,730**	**2,029**
Depreciation & amortisation	47	55	82
Tax paid	(194)	(341)	(408)
Other adjustments	(332)	(301)	(350)
Change in working capital	**861**	**(240)**	**(197)**
Cash flow from operations	**1,295**	**904**	**1,155**
Capex	(242)	(189)	(215)
Proceeds from assets sales	41	63	86
Others	153	(1,841)	839
Other non-current assets changes			
Cash flow from investing activities	**(48)**	**(1,967)**	**710**
New share issuance	563	1,875	
Shares buyback			
Net borrowings			
Other financing cash flow	(650)	(20)	(168)
Dividends paid	(167)	(257)	(383)
Cash flow from financing activities	**(254)**	**1,599**	**(551)**
Cash and equivalents at beginning of period	469	1,462	1,996
Total cash generated	**993**	**535**	**1,315**
Cash and equivalents at the end of period	1,462	1,996	3,311

Balance sheet			
(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	1,462	1,996	3,311
Short term investments	928	2,675	2,479
Accounts receivables	2,609	3,484	6,344
Inventories	1,051	1,241	1,874
Other current assets	436	547	316
Total current assets	**6,486**	**9,943**	**14,323**
Fixed assets	488	604	768
Total investments	493	715	377
Other long-term assets	349	479	410
Total assets	**7,815**	**11,741**	**15,877**
Short-term debt			
Accounts payable	1,962	3,228	4,631
Other current liabilities	2,597	2,267	3,929
Total current liabilities	**4,559**	**5,495**	**8,560**
Total long-term debt			
Other liabilities	13	12	11
Share capital	1,854	3,729	3,729
Retained earnings reserve	639	1,435	1,741
Shareholders' equity	**3,242**	**6,233**	**7,307**
Minority interest			
Total liabilities & equity	**7,815**	**11,741**	**15,877**

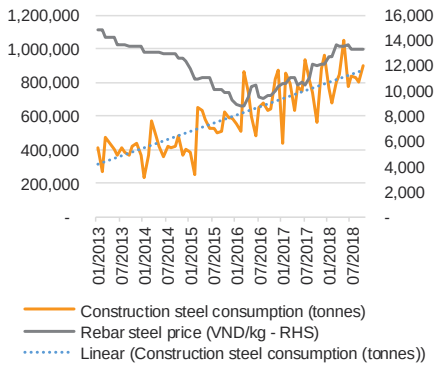
Key ratios			
	12-15A	12-16A	12-17A
Dupont			
Net profit margin	4.9%	6.8%	6.1%
Asset turnover	2.16	2.13	1.97
ROAA	10.5%	14.5%	12.0%
Avg assets/avg equity	2.20	2.06	2.04
ROAE	23.1%	30.0%	24.4%
Efficiency			
Days account receivable	69.7	61.4	85.3
Days inventory	30.6	23.9	27.2
Days creditor	57.0	62.2	67.2
Fixed asset turnover	36.8	38.1	39.6
ROIC	20.5%	22.8%	22.6%
Liquidity			
Current ratio	1.42	1.81	1.67
Quick ratio	1.19	1.58	1.45
Cash ratio	0.52	0.85	0.68
Cash cycle	43.2	23.0	45.2
Growth rate (yoy)			
Revenue growth	79.1%	52.0%	30.7%
Operating profit growth	119.5%	100.3%	8.1%
Net profit growth	103.5%	113.5%	16.2%
EPS growth	83.2%	29.9%	16.2%
Share value			
Basic EPS (VND)	14,214	18,457	21,449
BVPS (VND)	69,195	80,901	94,832

Source: VNDIRECT

CONSTRUCTION STEEL: SUPPLYSIDE CONSOLIDATION TO GATHER PACE

2018 REVIEW: Construction steel maintained a solid growth momentum due to robust domestic construction activity

Figure 142: Growth momentum maintained



Source: VNDIRECT

We estimate that domestic construction steel demand grew by 9-10% yoy (vs. 12.1% in 2017), to around 10.3 million tonnes in 2018. This was mainly attributed to robust construction growth of 9.2% yoy vs. 8.5% yoy in 2017. At the same time, rebar steel prices continued to inch higher in 2018 to an average of VND13.2m per tonne (+16.1% yoy). In 2018, Hoa Phat Group remained the largest construction steel producer with a market share of 23.8%, unchanged compared to that of 2017 despite the appearance of a new competitor in the domestic market – Formosa Ha Tinh Steel Corporation (FHS). In 2018, FHS achieved a dramatic increase in sales volume (+290.8% yoy) from a low base thanks to the ramp-up of new production lines. Exports contributed about 9.1% to its sales volume while the remaining was consumed domestically.

2019 OUTLOOK: We expect steel prices to correct on moderating demand growth and rising supply

Construction steel supply will outpace demand throughout 2019

During 2013-18, the Vietnam construction industry grew at an average rate of 10.9% per annum while local construction steel demand grew by a CAGR of 15.9%. As we expect the Vietnam construction industry to continue growing in 2019, construction steel demand, therefore, should follow suit. We project construction steel demand growth to remain at 9-10% in 2019, equivalent to an additional demand of around 1.0m tonnes. On the supply side, we forecast an incremental supply of 1.5m tonnes of construction steel coming on stream, mainly due to the ramp-up in production from the first phase of the Hoa Phat-Dung Quat Steel Complex project. As a result, supply could outpace demand and weigh on the construction steel outlook in 2019, in our view.

Steel prices and margins in 2019 to be lower than in 2018

Domestic rebar prices peaked in mid-2018 at VND13.6-13.9m/tonne, then declined to VND12.7m/tonne as of end-2018 due to weak demand during the rainy season. Sentiment has also been negatively hit by a sharp drop in Chinese steel prices. In 2019, given our expectations of a slight deterioration in the domestic supply-demand balance, the downtrend in construction steel prices is expected to continue. In addition, lower raw material prices could also be a drag for steel prices. According to experts, iron ore and coking coal prices are expected to be driven down by both supply growth and softening demand from China in 2019. Our base case assumes a 10.0% decrease in rebar steel prices in 2019. Steel mill margins should narrow as steel price declines will outpace input raw material price declines.

Figure 143: Steel prices and BOF implied spread forecast

Unit: US$/t	Iron ore	Hard coking coal	Raw material cost	Domestic rebar	Implied spread	China export rebar
2016	61	114	150	421	271	313
2017	74	210	212	501	289	476
2018E	72	208	208	567	359	533
2019F	67	199	196	510	314	498
2020F	65	189	189	485	296	485

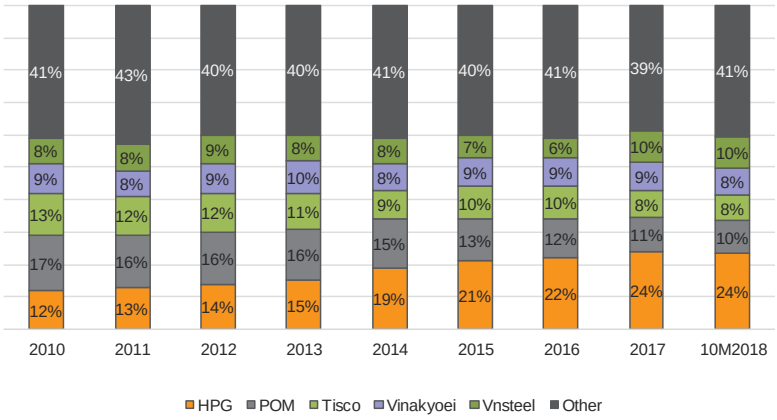
Source: VNDIRECT, DBS Research, Bloomberg

Note: Raw material cost = 1.65 * Iron ore + 0.43 * Coking Coal; Implied spread = Domestic rebar – Raw material cost

Vietnam's steel industry will see market share consolidation from 2019, led by HPG

Similar to the biggest steel producer globally, China, Vietnam is trying to consolidate its steel industry to improve competitiveness. With cost advantages (through scale and the use of BOF technology to produce steel), a wide distribution network and a strong brand name, HPG has successfully grabbed market share from other inefficient steel producers and became the market leader since 2014. In fact, HPG increased its market share from 12% in 2010 to 24% in 10M2018 while the second largest EAF steel producer Pomina saw its market share decrease from 17% to 10% in the same period. HPG reached maximum capacity in 2017 while other industry players were running at only 60-80% of their operational capacity. From mid-2019, HPG will launch new capacity and we expect it will keep grabbing market share from EAF producers and imported steel suppliers who together hold more than 50% of construction steel market share.

Figure 144: Vietnam's construction steel market share (2010-2018)



Source: VNDIRECT

Headwinds from Chinese steel industry to rise in 2019-20F

China's excess capacity was a big burden for the Vietnamese steel market in 2015-16, dampening steel prices and profitability of domestic steel producers. Following Chinese supply-side reforms and tariffs on Chinese imported steel, exports of Chinese steel products to Vietnam have decreased significantly in 2017-18. However, we expect Chinese steel exports to Vietnam to recover in 2019, as the Chinese government will encourage exports amid weakening domestic demand. For example, China has recently removed export duties on billet products since Jan 1, 2019 in order to boost steel exports amidst a backdrop of flagging domestic demand.

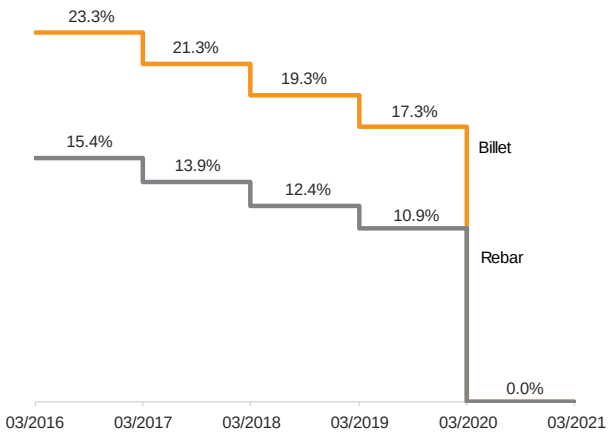
We also expect the Chinese government to boost infrastructure spending as a stimulus measure to cushion the slowdown in its economy and believe this could be a wild card for global steel price trends. According to DBS research, an infrastructure boost could directly benefit the Chinese steel sector by an additional demand of c.80m tonnes (~10.4% of total Chinese steel demand in 2018). However, we believe this is still not enough to reverse the downtrend in global steel prices assumed under our base case.

Vietnamese steel producers are still protected by current anti-dumping measures

There has been rising protectionism in the global steel industry in the last decade. For instance, key industry players and regions such as

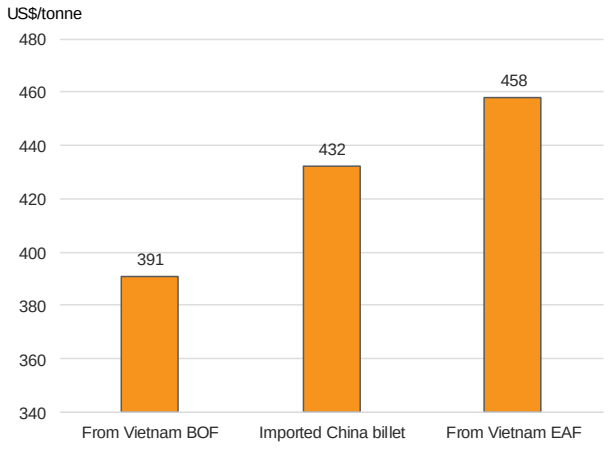
the US, EU, India and ASEAN applied tariffs and/or quotas on imported steel. Vietnam has also applied anti-dumping tariffs on Chinese imported steel products since 2016. These tariffs will last until Mar 2020.

Figure 145: The schedule of anti-dumping duties on imported Chinese steel



Source: VNDIRECT, GSO

Figure 146: Billet cost per tonne (data as of 06/12/2018)



Source: VNDIRECT

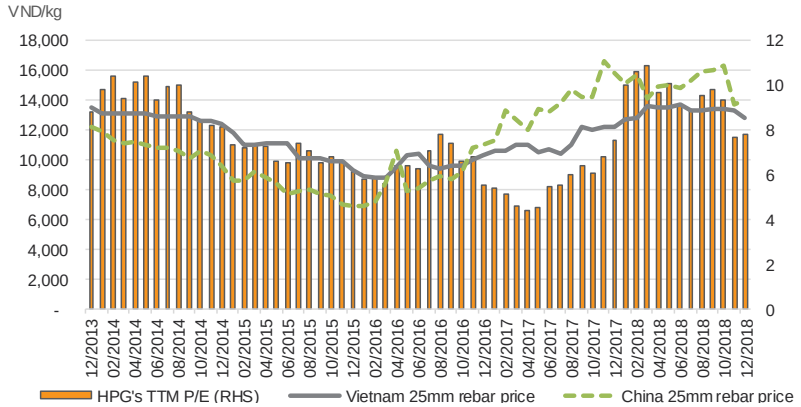
Note: 1) BOF: Blast Oxygen Furnace; EAF: Electric Arc Furnace
2) Assuming Vietnam and China use the same quality of iron ore and coking coal and imported China billet is from BOF

Assuming the same quality of iron ore and coking coal is used to produce steel in China and Vietnam, we estimated the cost per tonne of Vietnam billet versus China billet based on data as of 6/12/2018. Despite a lowering of tariffs from 19.3% to 17.3% as scheduled, imported China billet is still around 10% more expensive than domestically produced billet in terms of cost per tonne. In addition, continued supply-side reform in China's steel industry will indirectly raise production costs for Chinese steel producers by regulating iron ore and coking coal quality. In summary, we believe Vietnamese construction steel producers will still be relatively insulated by current anti-dumping measures.

STEEL STOCK PICKS: WE LIKE HPG AS RECENT NEGATIVE SENTIMENT HAS RENDERED THE VALUATION ATTRACTIVE

In our view, the recent fall in Vietnamese construction steel companies' share prices (notably Hoa Phat, **HPG VN, ADD, TP:VND39,100**) was largely due to a sharp decline in Chinese steel prices despite stable domestic fundamentals in Vietnam. A continued downtrend in Chinese steel prices could continue to weigh on sentiment but we believe that a further decline in steel prices is already priced-in for HPG. We also note that the expected fall in steep prices presents HPG with an opportunity to consolidate its leading position in the Vietnam steel industry by leveraging on its integrated production chain and strong distribution network to elbow out marginal players. Despite some headwinds for the sector in 2019, we expect the company to achieve higher sales volume of 38.3% yoy and 11.1% yoy earnings growth in the year.

Figure 147: Construction steel prices vs. HPG's TTM P/E



Source: VNDIRECT

Figure 148: Steel peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
JSW Steel	JSTL IN	9,919.5	76.4	76.4	7.1	25.1	1.4	11.2	2.5
Tata Steel	TATA IN	7,643.5	110.6	119.0	4.7	19.5	1.5	3.0	0.8
NMDC	NMDC IN	4,145.1	39.1	39.1	13.9	16.1	0.0	7.7	1.2
Maanshan Iron & Steel-A	600808 CH	3,851.2	105.0	105.0	10.0	28.0	1.0	3.9	1.0
Shanxi Taigang Stainless-A	000825 CH	3,596.6	162.9	162.9	9.9	25.8	1.3	3.7	0.8
Sansteel Minguang Co Ltd -A	002110 CH	3,226.4	110.9	107.5	32.2	50.9	0.1	3.0	1.3
Steel Authority of India	SAIL IN	3,063.8	91.5	91.5	(0.2)	(0.6)	1.1	8.6	0.6
Hunan Valin Steel Co Ltd -A	000932 CH	2,746.9	188.7	188.7	9.7	57.9	2.7	2.6	1.2
Hoa Phat Group JSC	**HPG VN**	**2,688.1**	**21.7**	**21.7**	**15.6**	**26.7**	**0.4**	**6.8**	**1.6**
Liuzhou Iron & Steel Co-A	601003 CH	2,565.6	192.3	192.3	18.6	59.9	1.5	3.7	1.9
Xinxing Ductile Iron Pipes-A	000778 CH	2,543.5	83.6	77.3	4.4	11.0	0.9	8.2	0.8
Xinyu Iron & Steel Co Ltd-A	600782 CH	2,385.9	258.9	216.8	17.4	42.6	0.6	2.8	0.9
Nanjing Iron & Steel Co-A	600282 CH	2,334.5	131.7	115.0	11.6	36.9	0.8	3.4	1.1
Jindal Steel & Power Ltd	JSP IN	2,046.6	32.4	32.5	(1.5)	(4.5)	1.4	8.5	0.5
SGIS Songshan Co Ltd-A	000717 CH	1,667.2	73.5	73.5	23.3	91.7	2.4	3.2	2.0
Average		*3,628.3*	*111.9*	*107.9*	*11.8*	*32.5*	*1.1*	*5.4*	*1.2*
Median		*2,746.9*	*105.0*	*105.0*	*10.0*	*26.7*	*1.1*	*3.7*	*1.1*

Source: VNDIRECT, BLOOMBERG, Data as of Jan 11 2019

HOA PHAT GROUP JSC (HPG)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND29,350	VND39,100	0.00%	ADD	BASIC MATERIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

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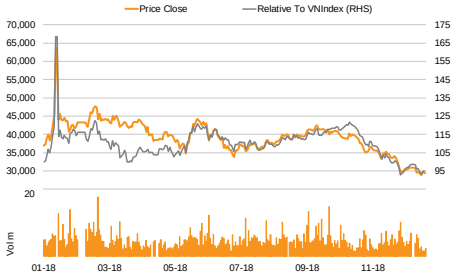
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	63,600
52w low (VND)	28,850
3m Avg daily volume (shares)	4,691,313
3m Avg daily value (VND mn)	165,521
Market cap (VND bn)	63,292
Outstanding shares (m)	2,156
Free float (%)	46.0
TTM P/E (x)	6.8
Current P/B (x)	1.6

Ownership

Tran Dinh Long	25.2%
Dragon Capital	7.7%
Vu Thi Hien	7.3%
Others	59.8%

Source: VNDIRECT

We see some headwinds in 2019F due to steel price weakness but market share consolidation on the back of new capacity will drive healthy earnings growth for HPG.

We believe HPG will further consolidate its domestic market share. Given the fact that HPG will double its construction steel capacity to 4.0m tonnes by mid-2019, we expect HPG to continue grabbing market share from local EAF producers and imported steel suppliers thanks to 1) HPG's production costs remaining competitive vs. other local steel mills; 2) tariffs on Chinese imported steel lasting until 2020, which provides enough time for HPG to consolidate its leading position. HPG will also continue to push its exports to regional countries, i.e. Cambodia, Malaysia and Japan and aims to raise its 2019 export volume to 400,000 tonnes (+66.7% yoy).

Higher sales volume but lower ASP. We expect sales volume to increase by 38.3% yoy to 4.4m tonnes in 2019F. Of this, sales volume of construction steel is estimated at 3.5m tonnes (+47.2% yoy), mainly due to the ramp-up in production of the first phase of the Dung Quat Complex project. However, as we expect supply to outweigh demand in 2019F, and combined with an expected downtrend in Chinese steel prices, we assume a 10.0% decline in domestic steel prices in 2019. HPG's GM is expected to narrow to 19.8% (from an estimated 22.0% in 2018).

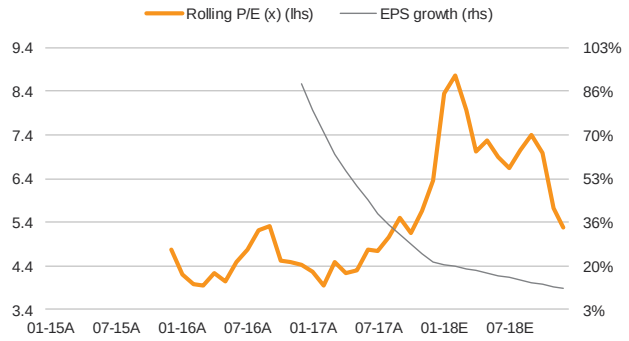
Slight delay and capex overruns on the second phase of Dung Quat Steel Complex project. Some reasons include: 1) HPG choosing to buy EU instead of Asian machinery (in order to comply with Vietnam's environmental policies on steel production); and 2) the captive port in Dung Quat, currently under construction, will now be expanded to service ships of up to 200,000 tonnes, while the initial plan was only to develop a port to accommodate ships up to 100,000 tonnes. We expect HPG to complete the second phase of the Dung Quat project in early 2020.

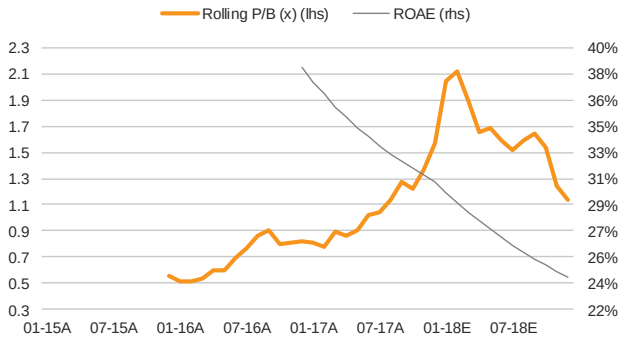
2019F earnings look solid and valuation has corrected sharply, maintain ADD. We revise down our earnings forecast for 2019-20F to reflect lower steel prices. Despite declining steel prices and lower margins, we still expect HPG to deliver net profit of VND9,865bn (+11.0%yoy) in 2019F. Given our lower DCF forecasts, and lower target P/E to reflect the recent correction in regional peer valuations, we revise down our 12-month target price to VND39,100 (from VND47,800).

Key risks: Downside risks include 1) lower-than-expected steel prices largely on a continued deterioration of China's economy; 2) cost pressure from iron ore and coal; and 3) rising interest rates. Upside risks include a re-rating in global steel stocks on a de-escalation of trade tensions.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	33,283	46,162	57,227	70,878
Revenue growth	21.2%	38.7%	24.0%	23.9%
Gross margin	26.3%	23.1%	21.8%	19.8%
EBITDA margin	28.2%	24.5%	22.3%	21.4%
Net profit (bn)	6,602	8,007	8,891	9,865
Net profit growth	89.4%	21.3%	11.0%	11.0%
Recurring profit growth	89.4%	21.3%	11.0%	11.0%
Basic EPS	4,352	5,278	5,860	6,502
Adjusted EPS	3,804	4,895	5,567	6,177
BVPS	23,425	21,282	27,144	33,646
ROAE	38.6%	30.8%	24.2%	21.4%

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	46,162	57,227	70,878
Cost of sales	(35,487)	(44,773)	(56,809)
Gen & admin expenses	(409)	(572)	(673)
Selling expenses	(643)	(858)	(1,099)
Operating profit	**9,622**	**11,023**	**12,297**
Operating EBITDA	11,626	13,400	16,377
Depreciation and amortisation	**(2,005)**	**(2,377)**	**(4,080)**
Operating EBIT	**9,622**	**11,023**	**12,297**
Interest income	186	314	259
Financial expense	(556)	(979)	(1,480)
Net other income	36	36	36
Income from associates & JVs	(0)	(0)	(0)
Pre-tax profit	**9,288**	**10,394**	**11,112**
Tax expense	(1,274)	(1,477)	(1,219)
Minority interest	(8)	(27)	(28)
Net profit	**8,007**	**8,891**	**9,865**
Adj. net profit to ordinary	8,007	8,891	9,865
Ordinary dividends			
Retained earnings	**8,007**	**8,891**	**9,865**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	4,265	4,278	4,556
Short term investments	9,937	7,937	1,937
Accounts receivables	6,555	4,578	8,505
Inventories	11,769	17,909	21,588
Other current assets	552	663	795
Total current assets	**33,077**	**35,365**	**37,381**
Fixed assets	17,924	37,718	49,336
Total investments	740	17	17
Other long-term assets	1,281	1,320	1,363
Total assets	**53,022**	**74,420**	**88,096**
Short-term debt	11,329	13,162	7,088
Accounts payable	6,487	8,059	10,226
Other current liabilities	0	0	0
Total current liabilities	**17,815**	**21,221**	**17,314**
Total long-term debt	1,651	10,560	18,085
Other liabilities	1,158	1,326	1,521
Share capital	15,171	21,239	21,239
Retained earnings reserve	13,397	15,775	25,146
Shareholders' equity	**32,287**	**41,179**	**51,044**
Minority interest	111	133	133
Total liabilities & equity	**53,022**	**74,420**	**88,096**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**9,288**	**10,394**	**11,112**
Depreciation & amortisation	2,005	2,377	4,080
Tax paid	(1,724)	(1,477)	(1,219)
Other adjustments	(363)	(288)	(315)
Change in working capital	**(3,149)**	**(2,701)**	**(5,572)**
Cash flow from operations	**6,058**	**8,306**	**8,086**
Capex	(8,875)	(22,159)	(15,686)
Proceeds from assets sales	7	0	0
Others	(9,058)	2,000	6,000
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(17,926)**	**(20,159)**	**(9,686)**
New share issuance	5,057	0	0
Shares buyback	0	2	0
Net borrowings	6,520	12,478	2,565
Other financing cash flow	1	(613)	(688)
Dividends paid	(4)	0	0
Cash flow from financing activities	**11,574**	**11,867**	**1,877**
Cash and equivalents at beginning of period	4,559	4,265	4,278
Total cash generated	**(294)**	**13**	**278**
Cash and equivalents at the end of period	4,265	4,278	4,556

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	17.3%	15.5%	13.9%
Asset turnover	1.07	0.90	0.87
ROAA	18.6%	14.0%	12.1%
Avg assets/avg equity	1.66	1.73	1.76
ROAE	30.8%	24.2%	21.4%
Efficiency			
Days account receivable	15.8	20.6	36.8
Days inventory	121	146	139
Days creditor	66.7	65.7	65.7
Fixed asset turnover	2.91	2.06	1.63
ROIC	17.6%	13.7%	12.9%
Liquidity			
Current ratio	1.86	1.67	2.16
Quick ratio	1.20	0.82	0.91
Cash ratio	0.80	0.58	0.37
Cash cycle	70	101	110
Growth rate (yoy)			
Revenue growth	38.7%	24.0%	23.9%
Operating profit growth	22.5%	14.6%	11.6%
Net profit growth	21.3%	11.0%	11.0%
EPS growth	21.3%	11.0%	11.0%
Share value			
Basic EPS (VND)	5,278	5,860	6,502
BVPS (VND)	21,282	27,144	33,646

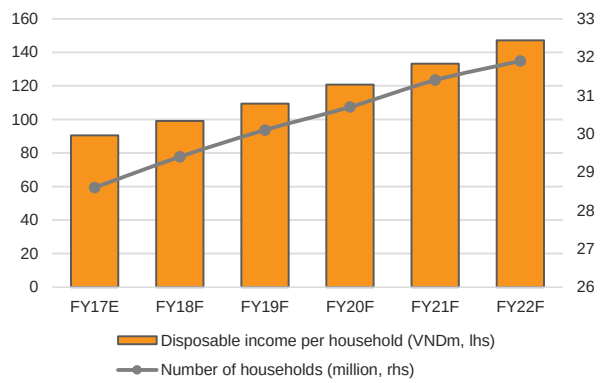
Source: VNDIRECT

CONSUMER: SLOWER BUT ROCK SOLID GROWTH

In line with the slowdown in overall economic growth, private consumption growth is expected to retreat to 6.8% in 2019 from 7.0% in 2018, according to BMI. However, private consumption in Vietnam will still grow above the average FY08-17 annual consumption growth level of 6.2% and offers opportunities for consumer goods companies that are quick to take advantage of rapidly shifting consumer behaviour.

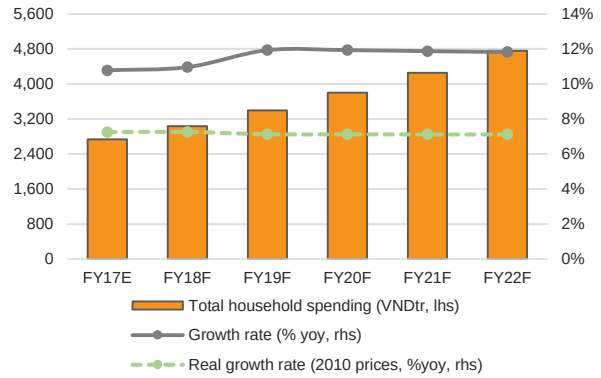
Rising disposable income per household continues to be the main driver of growth in consumer spending. Average disposable income per Vietnamese household is projected to grow at a FY18-22 CAGR of 10.4%, driven by wage growth from a low base (minimum wage expected to surge by 5.3% yoy in 2019 per Vietnam's Wage Council) and sustained low levels of unemployment (expected to remain constant at 3.4% during FY19F-FY22F per Business Monitor International). On the back of climbing disposable income, Vietnamese consumer spending will witness stable growth of ~7.1% per year over the term FY19F-FY22F in real terms (BMI, 2018).

Figure 149: Household income in Vietnam (FY17E - FY22F)



Source: VNDIRECT, BMI

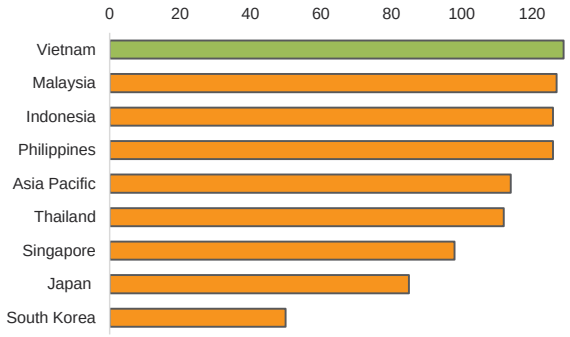
Figure 150: Vietnam's consumer expenditure (FY17E-FY22E)



Source: VNDIRECT, BMI

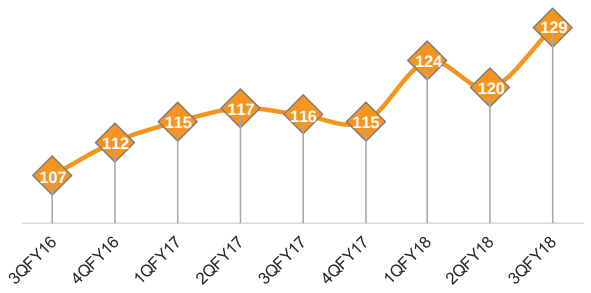
Highest level of consumer confidence in a decade. Vietnamese have become more willing to spend on big ticket items to improve quality of life on the back of a better perceived state of personal finances. According to market research firm Nielsen, consumer confidence reached a decade-long record high level of 129pts in 3QFY18 thanks to the enhanced job prospects and personal finances. Vietnam's consumer confidence was also well above regional peers' and the global average, reflecting the positive outlook of Vietnam's economy in the coming years, relative to the rest of the world.

Figure 151: Asia Pacific Consumer Confidence Index in 3QFY18



Source: VNDIRECT, NIELSEN

Figure 152: Consumer Confidence Index from 3QFY16-3QFY18

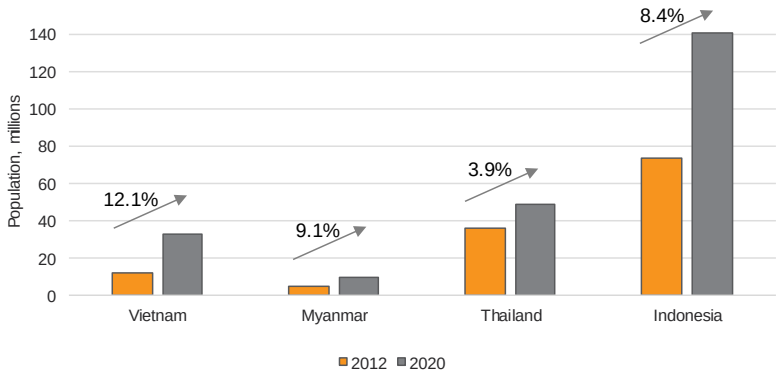


Source: VNDIRECT, NIELSEN

Spare cash is gradually flowing more into discretionary categories. In the latest survey by Nielsen, nearly half of Vietnamese consumers (48%) mentioned that they would like to go on holidays, 53% of consumers would buy new clothes, 47% would purchase new technological products and 46% stated that they would use the spare cash for home entertainment activities.

The expansion of the middle and affluent class could push up spending on non-essential products. According to Boston Consulting Group (BCG), the middle and affluent class (MAC - whose monthly income is above VND15m in Vietnam) will jump from 12m in 2012 to 33m in 2020 (CAGR of 12.1%), making Vietnam stand out among other Southeast Asian peers in terms of wealth creation. In the next two years, the MAC population is projected to make up 34.3% of the total population in Vietnam (vs. 13.6% in 2012).

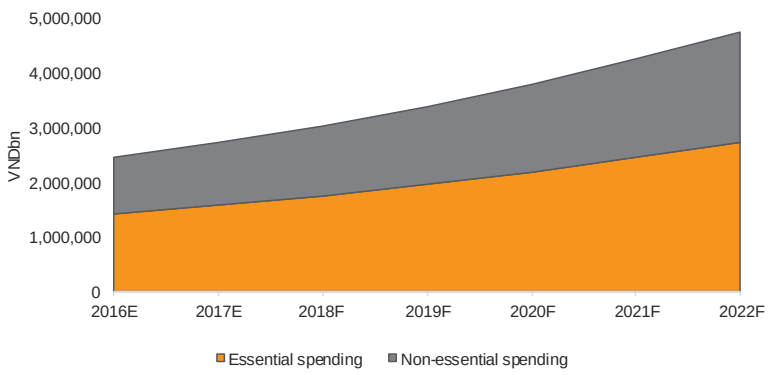
Figure 153: Vietnam has a fast-growing middle and affluent - class population



Source: VNDIRECT, BCG

It is conceivable that the new members of the MAC bracket will trade up to premium products and increase their spending on luxury goods. This group is characterised by their willingness to pay a premium for quality and customised options for a product, which would reflect their individuality and social status. Therefore, the expansion of the MAC population is expected to lead to stronger demand for premium and luxury goods including high technology products, watches, jewellery and liquor. As a result, projected growth in household expenditure on non-essential goods and services will slightly outpace that for essential spending over the forecast period of FY19F-FY22F (BMI 2018).

Figure 154: Non-essential spending growth to outpace essential spending growth in Vietnam in the period FY19F-FY22F



Source: VNDIRECT, BMI

2018 FMCG review – a slight moderation in growth

Most of the top FMCG producers in Vietnam posted lower net sales growth in 2018 with a mixed trend for gross margins (See figure 155). These results were shaped by three major factors: (1) sales volume in urban areas was weaker, while like-for-like price growth was under pressure due to intensifying competition (2) product premiumisation became the key driver for sales growth and (3) mixed input price trends led to dispersion of gross margin performance.

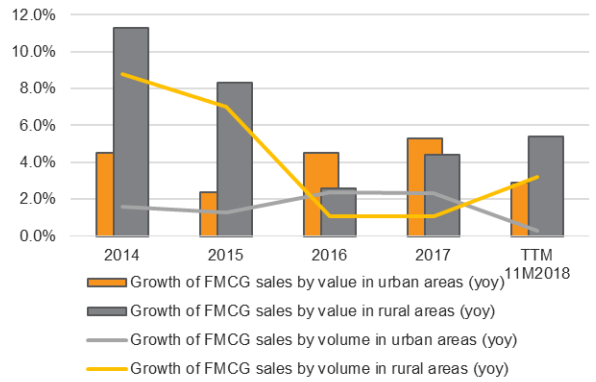
Figure 155: Most top FMCG producers posted lower yoy net sales growth in 2018

		Net sales growth			GPM			SG&A as % revenue			NPM		
		9M17	9M18	Chg	9M17	9M18	Chg	9M17	9M18	Chg	9M17	9M18	Chg
Producer	Product category	%	%	pts	%	%	pts	%	%	pts	%	%	pts
VNM	Dairy-Beverage	10.6%	2.2%	-8%	48.2%	46.6%	-2%	23.5%	24.5%	1%	22.1%	20.0%	-2%
MCH	Packaged food-Beverage	-3.4%	32.6%	36%	45.2%	45.4%	0%	30.8%	22.8%	-8%	14.4%	21.3%	7%
SAB	Beverage	8.7%	7.8%	-1%	27.0%	23.1%	-4%	10.5%	9.4%	-1%	14.9%	13.0%	-2%
QNS	Packaged food-Beverage	12.8%	3.5%	-9%	23.9%	27.3%	3%	11.0%	13.0%	2%	11.5%	12.8%	1%
KDF	Packaged food	7.5%	-14.2%	-22%	54.1%	53.3%	-1%	40.1%	47.1%	7%	11.7%	4.4%	-7%
LIX	Home care	8.9%	10.3%	1%	19.9%	19.4%	0%	10.9%	11.3%	0%	7.3%	6.5%	-1%
TAC	Packaged food	6.0%	4.5%	-2%	11.8%	12.0%	0%	8.6%	10.2%	2%	2.8%	1.7%	-1%
BHN	Beverage	-5.4%	-5.9%	-1%	26.9%	25.0%	-2%	17.0%	17.0%	0%	8.7%	7.5%	-1%

Source: FiinPro

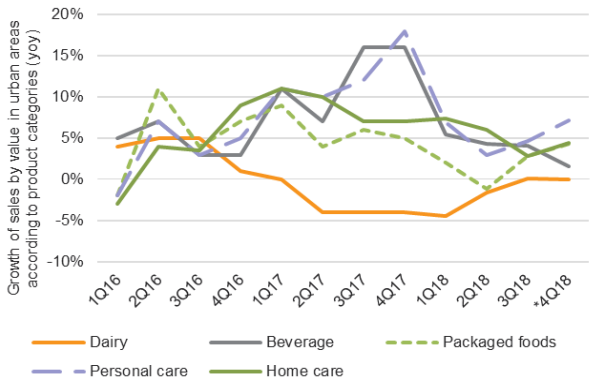
Growth rate of FMCG sales by volume in urban areas was weaker, across all five product categories. Data from Kantar World Panel indicated a slowdown across all five product categories with the dairy group suffering the most as evinced by negative volume growth in 2018.

Figure 156: FMCG consumption decelerated sharply in urban areas but accelerated in rural areas



Source: Kantar World Panel

Figure 157: Weaker sales growth in 2018 in urban areas was recorded across all five product categories

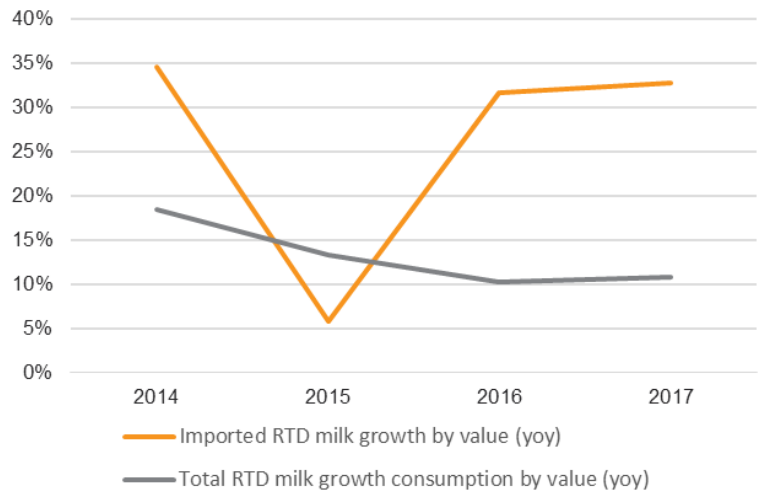


Source: Kantar World Panel

Changing consumer behaviour and lower intensity of ad spend by major companies likely contributed to the urban FMCG slowdown. Rapidly evolving patterns of FMCG product consumption by urban residents might have led to volume growth weakness. In recent years, aspirations for a healthier lifestyle have been increasing, imprinted in the mind of city dwellers with repeated marketing messages delivered by all FMCG producers. The choice is now quality over quantity and consumers are willing to pay more money for better, healthier products of a similar size, and we believe a considerable number of consumers prefer to spend the same amount of money on a smaller basket of premium products, resulting in weak 2018 volume growth. Ready-to-drink (RTD) or liquid milk consumption is a reflection of the first trend as growth of imported RTD milk (which is generally

believed to be better and is more expensive) by value was maintained at above 30%. This compares favourably against the overall market context wherein growth of total RTD milk sales by value slowed from 18% yoy in 2014 to 11% yoy in 2017. We believe the slowdown in growth in 2018 is transitory and reflects the fact that FMCG producers have been slow to tailor their product strategies to keep up with changes in customer preferences.

Figure 158: Growth of imported RTD milk consumption accelerated despite a slowdown in total RTD milk consumption



Source: Euromonitor, International Trade Center

Lower ad spend intensity may keep the brakes on sales growth. Total spending on advertising by the top five FMCG producers as a percentage of net sales fell by 0.7% pts to 4.0% yoy in 9M2018 compared to the previous year as a result of changing trends in marketing from traditional high-cost channels (e.g. TV, radio, newspaper) to online and social media (e.g. Facebook, webpage, mobile phones). The new marketing trend may help reduce marketing cost per unit of revenue generated, but will take time to manifest in sales growth improvements.

Figure 159: Advertising expense as % of net sales decreased in 9M2018

	9M15	9M16	9M17	9M18
QNS	2.8%	3.0%	2.8%	3.2%
VNM	4.2%	3.8%	3.7%	3.6%
SAB	3.4%	3.7%	3.7%	2.4%
MCH(*)	11.4%	14.0%	18.1%	12.7%
KDC (*)	5.8%	12.8%	3.5%	3.6%
Total	**3.8%**	**3.9%**	**4.7%**	**4.0%**

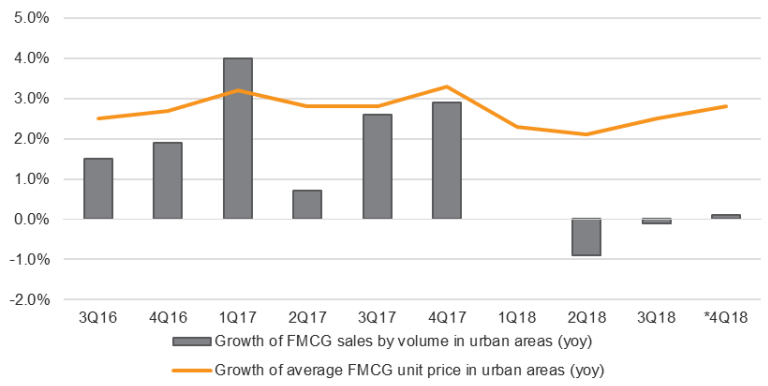
Note: MCH and KDC data are 6M

Source: VNDIRECT

Product premiumisation in the FMCG sector continued to gather pace while sales volume growth moderated. Higher average unit prices as the result of the premiumisation trend was recorded in each product category, especially with packaged food sold in urban areas and beverages sold in both rural and urban areas. Meanwhile, sales volume growth in urban areas was weak in most categories. Some successful products that represent this premiumisation trend are Greek Yogurt and Organics RTD milk launched by Vietnam Dairy Products JSC (VNM), TH Milk's walnut RTD milk, the Kokomi and Omachi noodle cup-with-meat and Tuna fish sauce products launched

by Masan Consumer Corp (MCH) and Fami Go soymilk launched by Quang Ngai Sugar (QNS).

Figure 160: Premiumisation became the main driver for revenue sales value growth as volumes were stagnant in 2018



Source: Kantar World Panel

Figure 161: Images of some premium products launched in 2018

Vietnam Dairy Product JSC's Greek Yoghurt

Vietnam Dairy Product JSC's Organic UHT fresh milk

Masan Consumer Corp's instant noodle cup with meat bar

Saigon Alcohol Beer and Beverages Corp's Saigon Gold

TH's Food Chain JSC's Nuts UHT Fresh Milk

Quang Ngai Sugar Company 's Fami GO

Source: Companies' websites, internet

Figure 162: Some notable premium products launched in 2018

Producer	Premium product		Normal product		Price premium
	Name	Retail price (*VND/unit*)	Name	Retail price (*VND/unit*)	
VNM	Organic RTD UHT milk 180ml	12,000	RTD UHT milk 180ml	7,223	66%
VNM	Greek yoghurt 100g	8,500	Plain yoghurt 100g	4,500	89%
SAB	Saigon Gold 330ml	20,000	333' Export 330ml	10,500	90%
QNS	Fami Go soymilk 200ml	6,500	Regular Fami 200ml	4,500	44%
MCH	Omachi noodle cup with meat bar	13,000	Omachi noodle cup	10,500	24%
TH(*)	TH Walnut RTD fresh milk 180ml	12,500	Regular TH's fresh milk 180ml	7,750	61%

Note: TH = TH Food Chain JSC
Source: Internet

Food material prices diverged in 2018, leading to dispersion in producer margins. Annual average prices of wheat, barley, soybean, cocoa and milk powder increased while sugar and vegetable oil prices retreated from 2017 levels. Barley and wheat saw the steepest rise in annual average price. Refined (RS) sugar and palm oil, on the other hand, saw the steepest price declines. Gross margins of Sabeco – the largest beer brewer in Vietnam – contracted by a dramatic 247bp yoy due to the increase in malt price (+36% yoy) and aluminium prices (+12% yoy) in 9M2018. Quang Ngai Sugar's soy milk segment, on the other hand, benefitted from the fall in soybean and sugar prices during the year with gross margin improving by 252bp yoy.

Figure 163: Food and beverage raw material yearly average price change

	Barley	Wheat	Soybean	Cocoa	*Milk	Palm oil	RS sugar
	US$/MT	US$/MT	US$/MT	US$/MT	US$/MT	US$/MT	US$/MT
FY2017	98	178	393	2,029	2,974	751	353
FY2018	126	204	394	2,294	3,046	639	276
% change	**28.9%**	**14.4%**	**0.3%**	**13.0%**	**2.4%**	**-14.9%**	**-21.9%**

(*)Milk = Whole milk powder
Source: Worldbank, agrimonitor, USDA

2019 FMCG outlook – Premiumisation the key driver for growth

We do not see any major risks for the FMCG sector in 2019 due to steady economic growth and high consumer confidence in Vietnam. Business results of producers will, nonetheless, be affected by three trends: (1) product premiumisation and (2) a recovery in advertising expense which will reduce producer's EBIT margin and (3) raw material price swings which will continue to drive dispersion in producer gross margins.

Premiumisation will be a key sales driver for FMCG producers with volume sales projected to expand only slightly. Sales volume in urban areas is expected to be stagnant in 2019 as rapidly evolving consumer preferences continue to be, on aggregate, unsatisfactorily addressed by product portfolio changes, thus far. We do note, however, that producers are gradually adapting to changing consumer preferences as illustrated by the recovery in growth across all five major product categories after a sharp fall in 1Q18. As developing a completely new product line is more difficult and time consuming than upgrading existed product lines, we believe that most major producers will focus on product premiumisation to reignite sales growth in 2019.

Higher spending on advertising and promotions to weigh on operating margins. We believe stagnant sales volumes in urban areas will lead to increased competition among FMCG producers. This will coincide with the growing presence of international brands in the

Vietnam market which carry higher perceived quality and will be favoured by increasingly quality-conscious urban consumers, thereby increasing the pressure on domestic incumbents to maintain market share.

FMCG material prices will continue to diverge, leading to a mixed impact on producer gross margins. We believe average global soybean prices will be lower in 2019 compared with 2018 due to the ongoing trade war between the US and China. We note that China resumed purchases of US soybeans from 23 December 2018. However, global soybean prices made a weak recovery of 3% after three weeks because the purchase volume in the first order was only 1.1m tonnes compared to the market's expectation of 5m to 8m tonnes. According to the US Soybean Association, there were no further notable increases in purchases from China. As such, the 2019 soybean price is expected to recover only slow from its dramatic fall in 2018, leading to a lower average price in 2019, per our expectations. This is likely to benefit soymilk or soybean oil producers in Vietnam such as QNS, VNM or KDC. Meanwhile, the gross margins of beer producers may contract further in 2019 due to the increased cost of malt caused by bad weather in Europe during the 2018 crop season.

2018 Retail review – a "land grab" underway

Vietnam's retail market is attractive in a regional context, ranking 6th globally and 2nd within Southeast Asia in the Global Retail Development Index (GRDI) in 2017. Vietnam's retail industry prospects are underpinned by the low market saturation levels due to the low penetration of modern retailing. Illustratively, total retail sales of goods and services in Vietnam continued to post double-digit growth and reached ~VND4,400 trillion in 2018 (+11.7% yoy). It is projected to grow at 13% per annum from now until 2020 and 14% per annum from 2021 to 2025 (Domestic Trade Development Strategy - Ministry of Industry and Trade/MoIT).

Figure 164: Top Southeast Asian countries in 2017 GRDI Ranking

Country	2017 GRDI Ranking	2017 GRDI score	Market attractiveness	Market saturation	Time pressure	GDP per capita, PPP	National retail sales (US$bn)
Malaysia	4	60.9	77.1	23.3	56.2	27,234	92
Vietnam	**6**	**56.1**	**26.7**	**72.4**	**100**	**6,422**	**90**
Indonesia	8	55.9	49.3	52.1	76.7	11,699	350
Philippines	18	48.4	33.2	39.9	73.5	7,696	137
Thailand	30	47.8	47.4	5.8	47.8	16,835	119
			0 = low attractiveness	*0 = saturated*	*0 = no time pressure*		
			100 = high attractiveness	*100 = not saturated*	*100 = urgency to enter*		

Source: ATKEARNY 2017

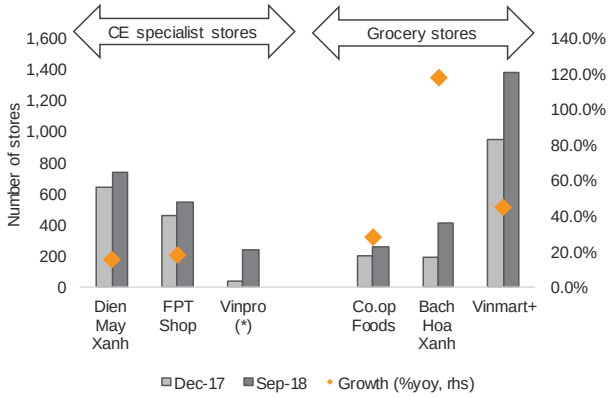
Organised retail competition is heating up in Vietnam. Many domestic and foreign players have either entered the market or expanded their network in the period 2017-2018 via both M&A activities and aggressive store openings. Many large enterprises have undertaken acquisitions mainly to utilise the distribution system and store network of the acquired companies. Incumbents are rapidly expanding their store footprints in a bid to win market share.

Figure 165: Notable M&A deals between retailers in 2017-2018

Acquiring firm	Acquired firm	Holding %	Value (US$m)	Acquisition date
Mobile Word JSC	Tran Anh JSC	>99%	~36.8	Aug-17
BRG Group	Hapro	65%	~78.5	Jun-18
VinCommerce	Fivimart	100%	N/A	Oct-18
VinPro	Vien Thong A	65%	N/A	Nov-18

Source: VNDIRECT, WEBSITES

Figure 166: Notable retail chains' expansion in 2017-2018



Source: VNDIRECT, COMPANY WEBSITES

* Vinpro increased the number of stores by nearly 6 times in 9M18. post – acquisition of Vien Thong A

Grocery retailing is currently the most hotly contested segment of the retail market. The two formats gaining interest from grocery retailers are mini food stores and convenience stores. Currently, BHX from MWG and Vinmart+ from Vingroup (VIC VN, Not rated) are the leading mini food store chain and convenience store chain, respectively. Foreign retailers are also piling into Vietnam and rapidly expanding their convenience store franchise such as Circle K, Shop & Go, Mini-stop and 7-Eleven. In non-grocery retail, consumer electronics (CE) seems to be a focus area. Key CE retailers have expanded their store footprints even as concerns about a maturing of key CE segments have taken hold, particularly mobile handsets. Mobile World JSC (MWG VN, Not rated) still maintained its leadership with 45% market share in the mobile phone segment, followed by FPT Retail (FRT VN, Not rated) with 18% market share. MWG also held an industry-leading 35% market share in the CE segment in 2018.

Segment leaders stayed on their thrones. MWG, FRT, Phu Nhuan Jewelry (PNJ VN, ADD, TP:VND126,500) and Digiworld (DGW VN, Not rated) stayed on top of their respective segments. Notably, MWG saw a deceleration in net sales growth (from 54.7% in 9M17 to 37.5% in 9M18) due to a slowdown in store expansion but managed to expand GPM by 0.6% pts thanks to a better product mix and improvement in performance of Bach Hoa Xanh (BHX), its grocery chain. FRT followed in MWG's wake with its mobile chain growth supported by signature features including F.Friends (consumer financing arm) and TPS (telco price subsidy programme). PNJ continued to lead the branded jewelry market with accelerating net sales growth and GPM expansion, contributed by an improving revenue and product mix. Another impressive performer was the CE distributor and market expansion service provider DGW which saw a dramatic turnaround in mobile phone sales in 9M18 (+294 % yoy) driven by the continued penetration of Xiaomi in Vietnam's mobile phone market thanks to its exclusive distribution rights for this brand.

Figure 167: Notable retailers' performance in FY18

Retailers	Product category	Net revenue growth			GPM			Net profit growth			Store expansion		
		9M17	9M18	Chg	9M17	9M18	Chg	9M17	9M18	Chg	9M17	9M18	Growth
		%	%	% pts	%	%	% pts	%	%	% pts	%	%	% yoy
MWG	Consumer electronics - Grocery	54.7%	37.5%	-17.2	17.0%	17.6%	0.6	33.7%	33.9%	0.2	1,920	2,184	13.8%
FRT	Consumer electronics - Pharmacy	22.1%	19.5%	-2.6	14.6%	13.4%	-1.2	39.5%	29.8%	-9.7	473	560	18.4%
PNJ	Jewellery	31.0%	35.5%	4.5	17.4%	18.6%	1.2	41.6%	37.8%	-3.7	269	306	13.8%
DWG	Consumer electronics	-3.4%	62.6%	66.0	6.9%	5.1%	-1.7	0.3%	38.0%	37.7	N/A	N/A	N/A

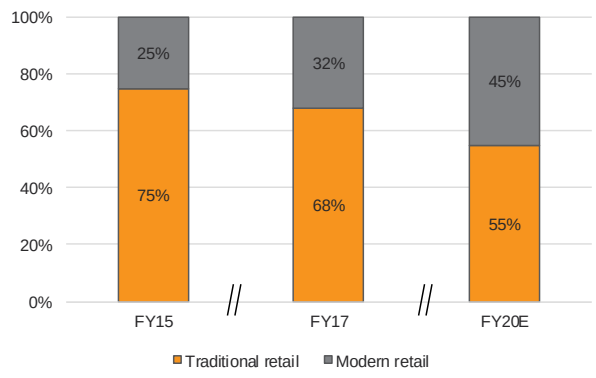
Source: VNDIRECT, BLOOMBERG

2019 Retail outlook: Rapid transformation of retail landscape to gather pace

Modern retailing to see rapid growth on the back of continued consumer preferences. The retail industry in Vietnam is still unorganised and fragmented with traditional retail (i.e. wet markets, small mom-and-pop shops) accounting for 68% of total retail value in 2017 and modern retail (i.e. convenience stores, hypermarkets, supermarkets) accounting for the rest (VCCI 2018). However, Vietnamese consumers are rapidly switching from traditional market to modern retail channels and, hence, modern retail penetration is expected to touch 45% by 2020 (MoIT).

Increasing concerns about food safety, hygiene and demands for convenience and product choice are driving the increased penetration of modern retailing (according to USDA 2018). The growing presence of convenience stores is mostly playing out in urban areas, especially in Ho Chi Minh City (HCMC) and Hanoi.

Figure 168: Retail channel by value contribution in Vietnam



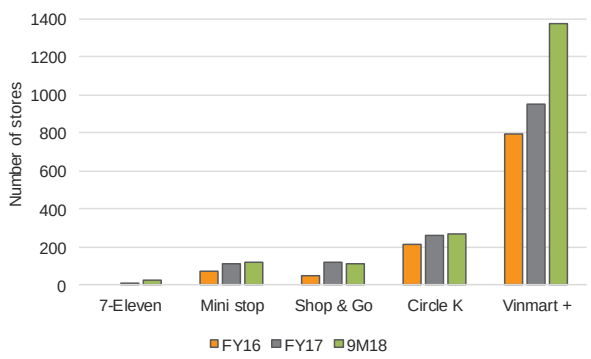
Source: VNDIRECT, VCCI 2018

Figure 169: FMCG retail landscape by value share % -- urban versus rural

Source: VNDIRECT, KANTAR WORLDPANEL

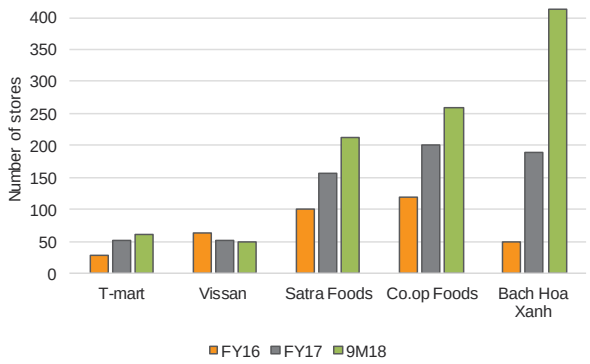
According to Nielsen, Vietnamese shoppers are making less visits to wet markets and flocking to convenience stores or minimarts more often. This trend has encouraged fierce competition between convenience store/mini mart chains in Vietnam including both domestic brands (Vinmart+, Bach Hoa Xanh, Co.op Food) and foreign players (Circle K, B's mart, 7-Eleven). We expect the growth of modern retail grocery stores to continue on the back of aggressive store expansion by both foreign and domestic retailers.

Figure 170: Convenience store footprint in Vietnam



Source: VNDIRECT. COMPANY WEBSITES

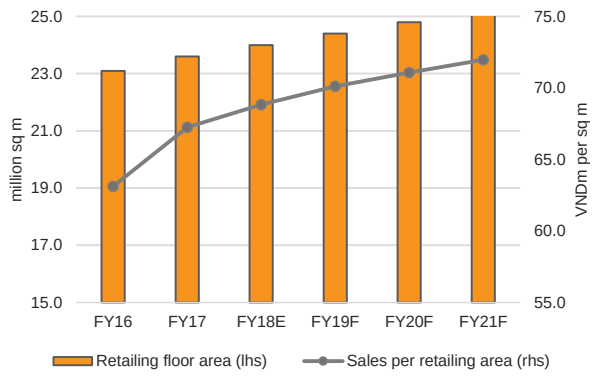
Figure 171: Minimart/food-store footprint in Vietnam



Source: VNDIRECT, COMPANY WEBSITES

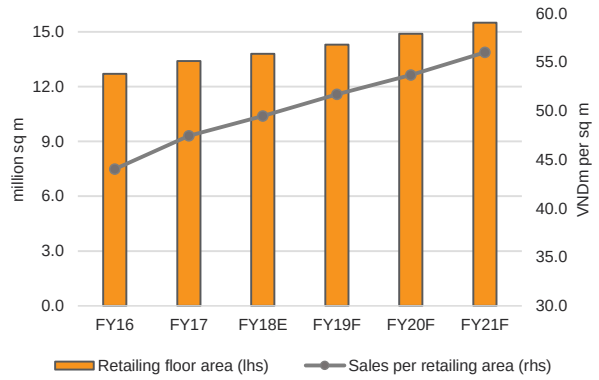
We expect both physical footprint expansion and greater e-commerce channel penetration. Retailers are expected to continue to enhance their footprints in 2019 to maintain and further capture market share. According to Kantar Worldpanel, minimart/convenience stores and specialty stores saw the highest value growth among all modern trade formats of 43% yoy and 20% yoy as of 2Q18, respectively. Thus, we expect retailers to concentrate on opening new outlets under the two formats mentioned above. Grocery retailers (including convenience stores and mini marts) and non-grocery retailers are projected to increase their retailing floor area at CAGRs of 1.5% and 3.8%, respectively, over the period FY17-FY22F according to Euromonitor.

Figure 172: Grocery retailing in Vietnam 2016-2021



Source: VNDIRECT, EUROMONITOR

Figure 173: Non-grocery retail in Vietnam 2016-2021



Source: VNDIRECT, EUROMONITOR

Retailers are also expected to catch up with the new trend of e-commerce. Vietnam has one of the least developed e-commerce markets in the region (accounting for around 1% of total retail sales as of 2017). However, e-commerce is becoming a focus area and investment is pouring in to develop reliable integrated payment platforms, better logistics and delivery services. Domestic retailers namely MWG, FRT and PNJ are developing their own e-commerce systems via the omni-channel platform.

Figure 174: B2C e-commerce landscape

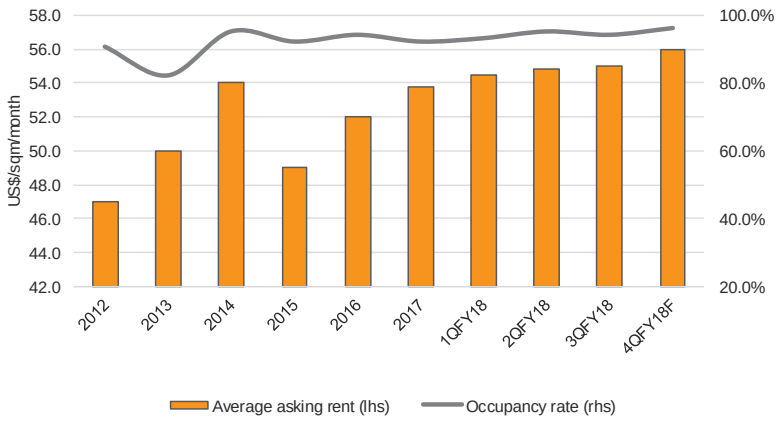
Websites	Type	Year of launch	Key investors	Monthly visits (as of 3Q18)
Shopee Vietnam	E-marketplace	2016	Sea Ltd.	34.5m
Thegioididong	E-commerce sales website	2004	MWG	30.3m
Lazada	E-marketplace/E-commerce sales websites	2012	Alibaba	30.2m
Tiki	E-marketplace/E-commerce sales websites	2010	JD.com, VNG	29.4m
Sendo	E-marketplace/E-commerce sales websites	2012	FPT Group	20.8m
FPT Shop	E-commerce sales website	2012	FPT Group	11.6m
Dienmayxanh	E-commerce sales website	2014	MWG	8.6m
Adayroi	E-commerce sales website	2015	VIC	5.4m
CellphoneS	E-commerce sales website	N/A	CellphoneS	5.3m
Vatgia.com	E-marketplace	2007	VNP Group	4.6m
Nguyen Kim	E-commerce sales website	2011	Central Group	4.0m

Source: VNDIRECT, EBVN 2018, IPRICE INSIGHTS

MWG and FRT have effectively leveraged their brick-and-mortar networks as delivery points and online-to-offline conversion points to drive their e-commerce strategies.

Higher rents could pressure retail margins. According to Euromonitor, rental costs rose in response to the higher demand for rental space driven by the rapid expansion of modern grocery retailers and specialist stores. In HCMC in 3QFY18, average rental rates for shopping centres, department stores and retail podiums surged to reach US$54.60/sq m/month (+0.4% qoq, +2.2% vs. 2017 rental rates) and occupancy rates remained high (Colliers International 2018).

Figure 175: HCMC: sustained high occupancy drove rental rate appreciation



Source: VNDIRECT, COLLIERS INTERNATIONAL

Higher rental rates might encourage retailers to reduce floor area per outlet and relocate stores to cheaper locations. Retailers that focus on boosting sales per square metre through better in-store service and merchandising should be able to weather this rise in rental costs.

2019 CONSUMER STOCK PICKS – WE LIKE QNS, PNJ, MWG AND VTP

We prefer consumer companies that meet the following three criteria: (1) companies with strong brands and sizable revenue contribution from premium products, (2) companies with a strong financial base to withstand intensifying competition and invest in innovation and (3) companies that will benefit from raw material price movements. Among Vietnam's top FMCG producers, we see Quang Ngai Sugar (**QNS VN, ADD, TP:VND51,000)** as having the best potential.

QNS will benefit from higher sugar prices and lower soybean prices in 2019. The company is the leading packaged soymilk producer (82% market share 2017) and a large sugar maker in Vietnam (11.5% market share in the 2017-2018 harvesting season). Soymilk and sugar contributed 47% and 29% respectively to total revenue in 9M2018. We forecast the company's revenue growth rate to accelerate by 68 bp to 8.1% yoy in 2019. Our forecast is based on expectations of a recovery in sugar prices in 2019 and stronger sales of soymilk as the company was successful in increasing soymilk sales in 3Q18 after six months of weak sales in 1H18, largely through better advertising and branding.

Among listed retailers, we like **PNJ (ADD, TP:VND126,500)** and place **MWG (Not rated)** on our watch list, both in recognition of their continued ability to ride the retail industry transformation story on the back of (1) rapid network expansion, (2) organic growth through both

online and physical stores (SSSG) and (3) business diversification and expansion based on a strong foundation of existing core businesses.

PNJ is expected to maintain leadership in the branded jewelry segment. We expect PNJ to continue to see high growth in FY2019. FY2019 revenue is estimated to reach VND17,432bn (+22.1% yoy based on our estimated FY18 revenue) and net profit to soar 15.7% yoy (based on FY18E net profit) to VND1,169bn. The jeweler will continue to maintain its extensive store footprint lead over its competitors and continue to scale up new business lines and channels such as PNJ Online, PNJ Silver and PNJ Watch.

MWG will ride the modern grocery retail trend in the long term while it improves grocery retailing operations in the near term. The grocery chain, Bach Hoa Xanh (BHX), is still the main focus of management. BHX has strived to effectively expand its store footprint while optimising revenue per store. BHX is on track to break-even at the expense of slower expansion. Besides BHX, MWG is expected to continue to witness stable growth across retail categories given its dominant market share. MWG is also well positioned to ride the continued penetration of online retailing in Vietnam given its dominant position in electronics e-retailing and its extensive network of physical stores which could give it an advantage in delivery logistics as well as in driving an online-to-offline strategy.

We like Viettel Post (VTP VN, ADD, TP:VND157,000) as a broad vehicle to ride Vietnam's e-commerce boom. VTP has the second largest market share in the parcel delivery market and is the fastest growing and most profitable delivery company for B2C commerce in Vietnam. With an impressive growth track record (core revenue CAGR of 62.4% and EBT CAGR of 61.3% over 2013-2017), VTP has attracted a lot of attention from investors since listing in late 2018, despite limited liquidity due to its UPCOM listing and mid-size market cap. We think VTP is a great vehicle to ride Vietnam's B2C services logistics market given its superb growth prospects, healthy financial status and modern and expansive logistics infrastructure footprint.

Figure 176: Consumer peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
FMCG									
Vinamilk	VNM VN	9,930	-7.0%	-7.0%	27.6%	37.7%	0.0	24.1	9.2
Sabeco	SAB VN	6,549	3.9%	3.9%	21.0%	28.5%	0.0	32.5	9.2
Massan Consumer	MCH VN	2,610	45.6%	45.6%	19.8%	32.8%	0.4	19.5	6.3
Habeco	BHN VN	822	5.3%	5.3%	6.9%	12.1%	0.1	30.3	4.5
Quang Ngai Sugar	QNS VN	515	-12.4%	-12.4%	14.6%	23.5%	0.4	10.8	2.4
LIX Detergent	LIX VN	66	-2.1%	-2.1%	18.7%	29.3%	0.1	10.5	2.9
Kido Frozen Food	KDF VN	41	-61.2%	-61.2%	4.6%	7.4%	0.2	17.9	1.4
Tuong An Veg Oil	TAC VN	39	7.8%	7.8%	6.9%	17.3%	1.0	9.0	1.8
Average			**-2.5%**	**-2.5%**	**15.0%**	**23.6%**	**0.3**	**19.3**	**4.7**
Median			**0.9%**	**0.9%**	**16.7%**	**26.0%**	**0.2**	**18.7**	**3.7**
Retail									
Mobile World Investment	MWG VN	1,603	38.7%	32.1%	13.1%	41.2%	1.1	13.2	4.5
Phu Nhuan Jewelry	PNJ VN	657	32.4%	28.6%	17.8%	28.7%	0.4	16.3	4.4
FPT Retail	FRT VN	203	29.7%	5.7%	8.4%	37.8%	1.9	13.9	4.6
Digiworld Corp	DGW VN	39	31.9%	10.6%	6.6%	14.3%	0.9	9.1	1.3
Average			**33.2%**	**21.2%**	**11.5%**	**30.5%**	**1.1**	**13.1**	**3.7**
Median			**32.1%**	**19.6%**	**10.7%**	**33.2%**	**1.0**	**13.5**	**4.5**
Postal-Delivery									
Singapore Post LTD	SPOST SP	1,620	-61.6%	-65.3%	4.2%	8.3%	0.2	23.1	1.7
POS Malaysia Berhad	POSM MK	369	-78.7%	-78.7%	0.8%	1.3%	0.2	61.2	0.8
Viettel Post	VTP VN	245	61.4%	61.4%	14.2%	51.3%	1.0	24.1	9.3
Average			**-70.2%**	**-72.0%**	**2.5%**	**4.8%**	**0.2**	**42.2**	**1.2**
Median			**-70.2%**	**-72.0%**	**2.5%**	**4.8%**	**0.2**	**42.2**	**1.2**

Source: Bloomberg, FiinPro, VNDIRECT

QUANG NGAI SUGAR (QNS)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND41,500	VND51,000	3.7%	ADD	CONSUMER

Outlook – Short term	Outlook – Long term	Valuation
Negative / Neutral / Positive	Negative / Neutral / Positive	Negative / Neutral / Positive

11 January 2019
Nguyen Tien Duc
duc.nguyentien2@vndirect.com.vn

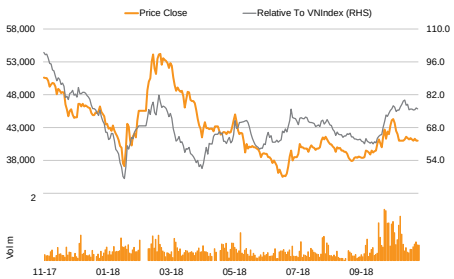
QNS is the leading branded soymilk player in Vietnam and a major sugar producer. The company commanded 82% market share of the packaged soymilk market and accounted for around 10% of total nationwide sugar supply in 2017.

We expect QNS to report good 2018 results despite multiple headwinds. Average sugar prices in 2018 fell 19% yoy and soymilk sales stagnated in 1H18 as the FMCG sector witnessed a sharp slowdown. However, we expect QNS to report annual net sales/NPAT growth of 7.4%/11.4% yoy due to (1) increased sugar sales as production capacity was expanded by 40.0% yoy, (2) successful soymilk product premiumisation strategy helped soymilk sales recover in 2H18. In 9M18, the company had achieved 75% of our full year revenue forecast and 69% of our full year net profit projection.

We forecast revenue/net profit growth of 7.4%/10.1% yoy in 2019 driven by rising sugar prices and soymilk premiumization. The sugar segment will be the main driver for 2019 growth with sales expected to grow by 15.5% yoy due to a 5.0% yoy increase in production output and 10.0% higher ASP as global sugar prices are projected to recover on the back of planned supply cuts by Brazil and Thailand. Soymilk, on the other hand, is forecast to see 5.0% sale growth thanks to a successful premiumisation strategy led by the launch of the nutrient-rich breakfast replacement product FAMI GO which is priced at a 44% premium to the regular FAMI soymilk product. The soymilk segment should also enjoy better margins thanks to lower average soybean prices stemming from the US-China trade war and despite the resumption in Chinese purchases of US soybean in recent months.

We reiterate our ADD recommendation on QNS. We use a sum-of-parts valuation method, with each part being valued using a target P/E multiple applied to our 2019 forward EPS. Our target P/E multiple for the soymilk, sugar and other segments are 10.1x, 6.9x and 14.5x respectively, in line with the peer average for each. Our TP translates into an implied 2018 P/E of 11.3x and a 2019 P/E of 10.3x. The stock carries a reasonable cash dividend yield of 3.7%.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	54,213
52w low (VND)	35,500
3m Avg daily volume (shares)	372,759
3m Avg daily value (VND mn)	15,731
Market cap (VNDbn)	12,054
Outstanding shares (m)	294
Free float (%)	80
TTM P/E (x)	10.8
Current TTM P/B (x)	2.4

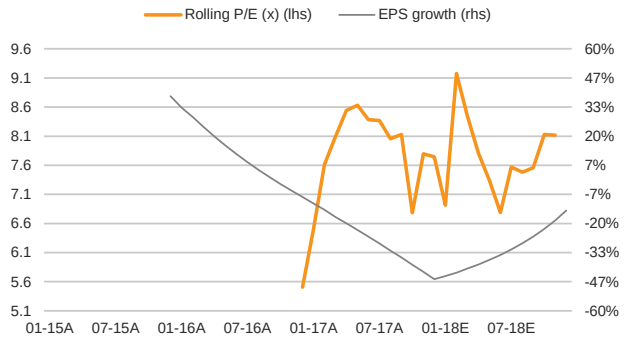
Ownership

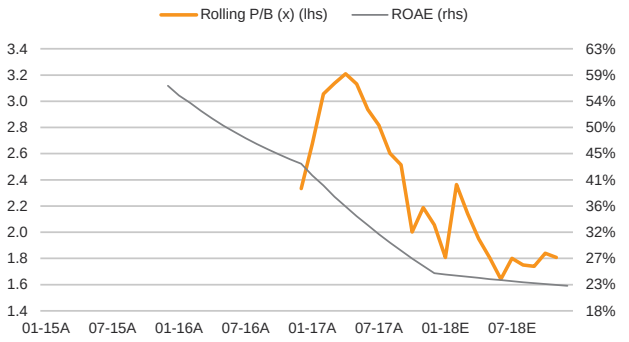
Thanh Phat Trading Ltd.	15.8%
Foremost Worldwide Limited	5.2%
Võ Thanh Đàng	5.0%
Others	74.0%

Source: VNDIRECT

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	6,972	7,633	8,195	8,797
Revenue growth	(10.4%)	9.5%	7.4%	7.4%
Gross margin	32.6%	26.2%	28.6%	29.0%
EBITDA margin	27.8%	21.3%	22.4%	23.1%
Net profit (bn)	1,410	1,027	1,143	1,258
Net profit growth	14.6%	(27.2%)	11.3%	10.1%
FD EPS	5,550	4,042	4,499	4,954
BVPS	25,120	21,836	22,770	25,789
ROAE	43.3%	24.5%	22.3%	20.4%

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	7,633	8,195	8,797
Cost of sales	(5,637)	(5,853)	(6,250)
Gen & admin expenses	(146)	(218)	(234)
Selling expenses	(697)	(849)	(911)
Operating profit	**1,153**	**1,275**	**1,402**
Operating EBITDA	1,567	1,824	2,011
Depreciation and amortisation	**(414)**	**(548)**	**(609)**
Operating EBIT	**1,153**	**1,275**	**1,402**
Interest income	38	62	51
Financial expense	(78)	(76)	(64)
Net other income	26	28	31
Income from associates & JVs	0	0	0
Pre-tax profit	**1,138**	**1,290**	**1,420**
Tax expense	(112)	(147)	(162)
Minority interest	0	0	0
Net profit	**1,027**	**1,143**	**1,258**
Adj. net profit to ordinary	1,027	1,143	1,258
Retained earnings	**661**	**704**	**1,258**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	528	789	837
Short term investments	751	951	951
Accounts receivables	289	489	725
Inventories	320	470	570
Other current assets	19	160	279
Total current assets	**1,907**	**2,860**	**3,362**
Fixed assets	4,852	4,980	5,541
Total investments	0	(0)	0
Other long-term assets	240	255	278
Total assets	**6,999**	**8,094**	**9,181**
Short-term debt	1,404	1,338	1,378
Accounts payable	540	500	440
Other current liabilities	401	364	406
Total current liabilities	**2,345**	**2,202**	**2,224**
Total long-term debt	145	79	379
Other liabilities	27	29	27
Share capital	2,438	2,926	2,926
Retained earnings reserve	2,135	2,870	3,548
Shareholders' equity	**4,482**	**5,784**	**6,551**
Minority interest	0	0	0
Total liabilities & equity	**6,999**	**8,094**	**9,181**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**1,138**	**1,290**	**1,420**
Depreciation & amortisation	414	548	609
Tax paid	(116)	(147)	(162)
Other adjustments	57	16	318
Change in working capital	**131**	**(537)**	**(318)**
Cash flow from operations	**1,625**	**1,170**	**1,868**
Capex	(874)	(676)	(1,610)
Proceeds from assets sales	0	0	0
Others	(196)	(200)	0
Other non-current assets changes	19	15	(23)
Cash flow from investing activities	**(1,051)**	**(861)**	**(1,633)**
New share issuance	(0)	0	0
Shares buyback	0	0	0
Net borrowings	222	280	340
Other financing cash flow	(64)	0	(88)
Dividends paid	(339)	(328)	(439)
Cash flow from financing activities	**(182)**	**(48)**	**(187)**
Cash and equivalents at beginning of period	137	528	789
Total cash generated	**391**	**261**	**48**
Cash and equivalents at the end of period	528	789	837

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	13.5%	13.9%	14.3%
Asset turnover	1.16	1.09	1.02
ROAA	15.6%	15.1%	14.6%
Avg assets/avg equity	1.56	1.47	1.40
ROAE	24.5%	22.3%	20.4%
Efficiency			
Days account receivable	1.04	3.19	6.92
Days inventory	20.7	29.3	33.3
Days creditor	34.9	31.2	25.7
Fixed asset turnover	1.70	1.67	1.67
ROIC	17.0%	15.9%	15.1%
Liquidity			
Current ratio	0.81	1.30	1.51
Quick ratio	0.68	1.09	1.26
Cash ratio	0.55	0.79	0.80
Cash cycle	(13.2)	1.4	14.5
Growth rate (yoy)			
Revenue growth	9.5%	7.4%	7.4%
Operating profit growth	(24.0%)	10.6%	9.9%
Net profit growth	(27.2%)	11.3%	10.1%
EPS growth	(27.2%)	11.3%	10.1%
Share value			
FD EPS (VND)	4,042	4,499	4,954
BVPS (VND)	21,836	22,770	25,789

Source: VNDIRECT

PHU NHUAN JEWELRY (PNJ)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND92,500	VND126,500	1.6%	ADD	RETAIL

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019
Natalie Nguyen
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PNJ is expected to continue to witness robust performance in 2019, resting upon its market leadership in the branded jewellery segment and its ability to capitalise on the expansion of the middle-affluent class in Vietnam. We maintain our ADD recommendation.

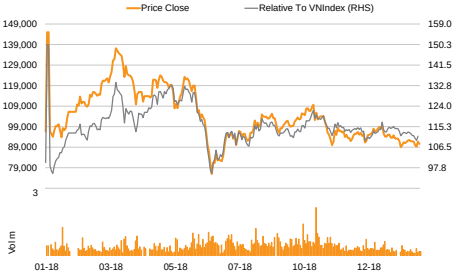
PNJ is leading the jewellery market in Vietnam with an estimated 30% market share in the branded segment in 2018, per management. The company is well ahead of its competitors in terms of store coverage, customer service, marketing prowess and product diversity. For FY18, PNJ recorded VND14,573bn in net revenue (+32.8%yoy, completing 106% of annual target) and realized VND960bn in EAT (+32.4% yoy, fulfilling 109% of annual target).

Extensive store network and still expanding. PNJ has brought the total store count to 324 stores as of end-FY18 (+20.4% yoy), far ahead of its competitors including SJC (52 stores), Doji (50 stores), and PRECITA. The store opening plan appears to be tracking our projections of ~45 new stores per year to reach over 500 jewellery stores by FY2022. PNJ's footprint could also be enhanced further by the launch of PNJ Watch stores expected in 2019.

Sustained momentum at PNJ Gold and anticipated turnaround at PNJ Silver to drive strong topline growth. Average revenue per store of PNJ Gold is expected to grow at 5% per year while PNJ Silver should see an improvement in performance through cultivation of greater brand loyalty, improved merchandising and regular introduction of new collections; we expect PNJ Silver revenue per store to growth by 4% per year. PNJ Watch and the company's new omni-channel strategy could further boost topline growth.

27.0% earnings growth expected for 2019 based on 26.4% topline growth and 0.2% points of GPM expansion, driven by continued improvements in the revenue mix. We maintain an ADD recommendation on PNJ with a target price of VND126,500/share, translating to a P/E of 17.3x based on our FY19 forecasted earnings.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	135,926
52w low (VND)	73,559
3m Avg daily volume (shares)	380,614
3m Avg daily value (VNDmn)	37,122
Market cap (VNDbn)	15,448
Outstanding shares (m)	167
Free float (%)	85
TTM P/E (x)	16.3
Current P/B (x)	4.4

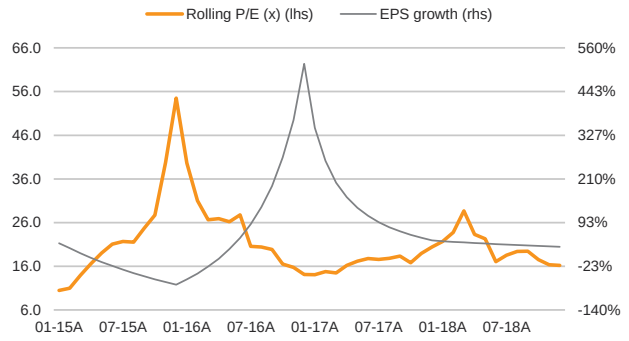
Ownership

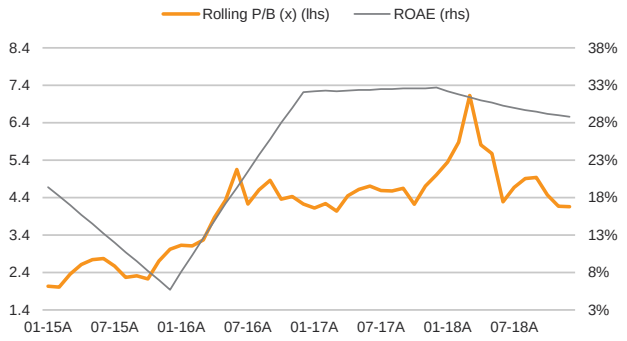
Cao Thi Ngoc Dung	9.2%
LGM Investments Ltd	4.5%
Route One Investment Company	4.1%
Others	82.2%

Source: VNDIRECT

Financial summary (VND)	12-16A	12-17A	12-18A	12-19E
Net revenue (bn)	8,565	10,977	14,573	18,422
Revenue growth	11.1%	28.2%	32.8%	26.4%
Gross margin	16.5%	17.4%	19.1%	19.3%
EBITDA margin	7.4%	8.4%	8.4%	8.5%
Net profit (bn)	451	725	960	1,218
Net profit growth	517.8%	60.8%	32.4%	26.9%
Recurring profit growth	385.7%	76.2%	33.1%	27.0%
Basic EPS	3,068	4,471	5,749	7,293
Adjusted EPS	2,565	3,928	5,138	6,587
BVPS	10,211	18,193	22,425	27,731
ROAE	32.0%	32.6%	28.7%	29.1%

Valuation





Income statement

(VNDbn)	12-17A	12-18A	12-19E
Net revenue	10,977	14,573	18,422
Cost of sales	(9,065)	(11,794)	(14,867)
Gen & admin expenses	(188)	(346)	(505)
Selling expenses	(775)	(1,171)	(1,421)
Operating profit	**949**	**1,262**	**1,629**
Operating EBITDA	988	1,304	1,695
Depreciation and amortisation	**(39)**	**(42)**	**(66)**
Operating EBIT	**949**	**1,262**	**1,629**
Interest income	9	7	9
Financial expense	(56)	(66)	(118)
Net other income	6	3	3
Income from associates & JVs	0	0	0
Pre-tax profit	**908**	**1,206**	**1,523**
Tax expense	(183)	(246)	(305)
Minority interest	0	0	0
Net profit	**725**	**960**	**1,218**
Adj. net profit to ordinary	725	960	1,218
Ordinary dividends	(185)	(265)	(334)
Retained earnings	**540**	**695**	**884**

Balance sheet

(VNDbn)	12-17A	12-18A	12-19E
Cash and equivalents	175	207	306
Short term investments	160	0	0
Accounts receivables	85	176	208
Inventories	3,402	4,816	5,767
Other current assets	74	82	110
Total current assets	**3,896**	**5,281**	**6,391**
Fixed assets	487	719	1,129
Total investments	0	0	0
Other long-term assets	109	304	320
Total assets	**4,492**	**6,304**	**7,840**
Short-term debt	846	1,558	1,969
Accounts payable	279	291	347
Other current liabilities	364	693	878
Total current liabilities	**1,489**	**2,542**	**3,194**
Total long-term debt	46	8	8
Other liabilities	7	9	7
Share capital	1,081	1,670	1,670
Retained earnings reserve	772	885	1,699
Shareholders' equity	**2,950**	**3,745**	**4,631**
Minority interest	0	0	0
Total liabilities & equity	**4,492**	**6,304**	**7,840**

Cash flow statement

(VNDbn)	12-17A	12-18A	12-19E
Pretax profit	**908**	**1,206**	**1,523**
Depreciation & amortisation	39	42	66
Tax paid	(154)	(232)	(305)
Other adjustments	(142)	(175)	(11)
Change in working capital	**(542)**	**(1,144)**	**(760)**
Cash flow from operations	**109**	**(303)**	**513**
Capex	(115)	(336)	(477)
Proceeds from assets sales	8	1	2
Others	3	6	0
Other non-current assets changes	(160)	160	(16)
Cash flow from investing activities	**(264)**	**(169)**	**(491)**
New share issuance	975	97	0
Shares buyback	0	0	0
Net borrowings	(615)	672	411
Other financing cash flow	0	0	0
Dividends paid	(185)	(265)	(334)
Cash flow from financing activities	**175**	**504**	**77**
Cash and equivalents at beginning of period	155	175	207
Total cash generated	**20**	**32**	**99**
Cash and equivalents at the end of period	175	207	306

Key ratios

	12-17A	12-18A	12-19E
Dupont			
Net profit margin	6.6%	6.6%	6.6%
Asset turnover	2.72	2.70	2.60
ROAA	17.9%	17.8%	17.2%
Avg assets/avg equity	1.82	1.61	1.69
ROAE	32.6%	28.7%	29.1%
Efficiency			
Days account receivable	1.33	1.98	1.70
Days inventory	137	149	142
Days creditor	11.2	9.0	8.5
Fixed asset turnover	24.3	24.2	19.9
ROIC	18.9%	18.1%	18.4%
Liquidity			
Current ratio	2.62	2.08	2.00
Quick ratio	0.33	0.18	0.20
Cash ratio	0.22	0.08	0.10
Cash cycle	127	142	135
Growth rate (yoy)			
Revenue growth	28.2%	32.8%	26.4%
Operating profit growth	30.9%	33.0%	29.1%
Net profit growth	60.8%	32.4%	26.9%
EPS growth	45.7%	28.6%	26.9%
Share value			
Basic EPS (VND)	4,471	5,749	7,293
BVPS (VND)	18,193	22,425	27,731

Source: VNDIRECT

MOBILE WORLD INVESTMENT CORP (MWG)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND85,000	N/A	1.7%	NOT RATED	RETAIL

Outlook – Short term	Outlook – Long term	Valuation
N/A	N/A	N/A

11 January 2019
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Slowing but steady growth in the mobile phone retail chain The Gioi Di Dong (TGDD) and consumer electronics retail chain Dien May Xanh (DMX) while grocery retail chain Bach Hoa Xanh (BHX) to be the major long-term growth engine.

TGDD and DMX continued to beat the market while BHX saw a significant improvement. For 11M18, revenue from mobile phones, tablets and laptops grew by 18% yoy (vs. ~3% yoy growth of the overall market); revenue from electronics, white goods and small appliances grew by 70% yoy (vs. 20% yoy growth of the overall market); and revenue from fresh foods & FMCG products surged by 214% yoy.

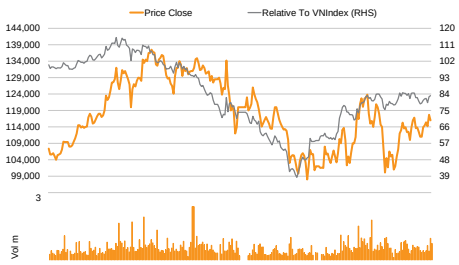
Legacy chains to remain the mainstay of MWG's business in FY2019. TGDD is expected to maintain its leadership with 45% market share in mobile retailing while DMX could increase its market share to reach 40% (from 35% in FY17). Both chains will be integrated more closely with continuing store conversions of TGDD stores to DMX/DMX mini formats while DMX mini formats will be upgraded to to standard formats. Adjustments to store layout, merchandising and display optimisation and new pricing policies are all expected to continue to drive store level performance.

BHX is the new growth engine, despite its current small revenue contribution to MWG of around 4.7% in 11M18. MWG will rapidly expand BHX's footprint across the country while executing on its plan to convert all stores to standard format, complete its planned store coverage in the south and continue to optimize supply chain and logistics. Average monthly sales per store opened before Nov 2018 reached over VND1.1bn/store (up by 38% vs. Jun 2018). Management expects the chain to reach store-level EBIT break-even by end-FY19, at the latest.

MWG aims to extend dominance in the online channel to BHX. MWG already dominates online retailing with 55% channel share in the mobile phones and tablets segment and 45% channel share in the consumer electronics segment. BHX is looking to also tap into the online channel to complement its brick-and-mortar expansion in grocery retailing.

MWG's Board has approved an aggressive FY2019 plan aiming at 25.6% topline growth and 37.2% earnings growth versus the FY2018 target. MWG is currently trading at a TTM PER of 13.2x, a 53.0% discount to the average TTM PER of global peers (20.2x).

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	99,241
52w low (VND)	72,471
3m Avg daily volume (shares)	449,858
3m Avg daily value (VNDmn)	48,521
Market cap (VNDbn)	37,666
Outstanding shares (m)	443
Free float (%)	65
TTM P/E (x)	13.2
Current P/B (x)	4.5

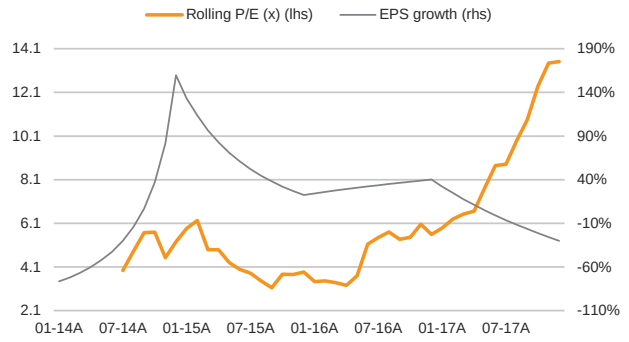
Ownership

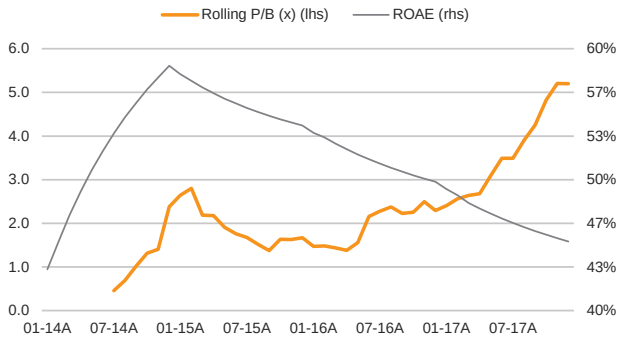
PYN Elite Fund	4.4%
NTASIAN Discovery	3.7%
Dragon Capital Group Ltd	3.6%
Others	88.3%

Source: BLOOMBERG

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	15,757	25,253	44,613	66,340
Revenue growth	65.9%	60.3%	76.7%	48.7%
Gross margin	15.2%	15.5%	16.2%	16.8%
EBITDA margin	6.4%	6.4%	5.6%	5.6%
Net profit (bn)	668	1,072	1,576	2,207
Net profit growth	162.0%	60.5%	47.0%	40.0%
Recurring profit growth	159.3%	59.9%	50.3%	39.1%
Adjusted EPS	5,930	7,272	10,205	7,150
FD EPS	2,474	3,771	5,284	7,387
BVPS	13,174	16,911	24,943	18,635
ROAE	58.7%	54.1%	49.8%	45.3%

Valuation





Income statement			
(VNDbn)	12-15A	12-16A	12-17A
Net revenue	25,253	44,613	66,340
Cost of sales	(21,330)	(37,399)	(55,198)
Gen & admin expenses	(249)	(935)	(1,346)
Selling expenses	(2,351)	(4,288)	(7,017)
Operating profit	**1,323**	**1,991**	**2,779**
Operating EBITDA	1,520	2,378	3,469
Depreciation and amortisation	**(197)**	**(387)**	**(690)**
Operating EBIT	**1,323**	**1,991**	**2,779**
Interest income	81	135	251
Financial expense	(41)	(120)	(234)
Net other income	23	(1)	14
Income from associates & JVs	0	0	0
Pre-tax profit	**1,386**	**2,005**	**2,810**
Tax expense	(310)	(428)	(602)
Minority interest	(4)	(1)	(1)
Net profit	**1,072**	**1,576**	**2,207**
Adj. net profit to ordinary	1,072	1,576	2,207
Ordinary dividends	(2)	(220)	(232)
Retained earnings	**1,070**	**1,356**	**1,975**

Balance sheet			
(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	344	997	3,411
Short term investments	0	0	0
Accounts receivables	636	1,410	2,766
Inventories	4,933	9,371	12,050
Other current assets	264	510	636
Total current assets	**6,177**	**12,288**	**18,863**
Fixed assets	849	2,096	3,464
Total investments	0	0	0
Other long-term assets	241	470	496
Total assets	**7,267**	**14,854**	**22,823**
Short-term debt	2,053	4,789	5,604
Accounts payable	1,971	4,680	7,373
Other current liabilities	757	1,543	2,736
Total current liabilities	**4,781**	**11,012**	**15,713**
Total long-term debt	0	0	1,200
Other liabilities	0	0	0
Share capital	1,469	1,540	3,170
Retained earnings reserve	978	2,262	2,699
Shareholders' equity	**2,484**	**3,840**	**5,907**
Minority interest	2	2	3
Total liabilities & equity	**7,267**	**14,854**	**22,823**

Cash flow statement			
(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**1,386**	**2,005**	**2,810**
Depreciation & amortisation	197	387	690
Tax paid	(196)	(531)	(691)
Other adjustments	33	86	102
Change in working capital	**(2,061)**	**(2,534)**	**(246)**
Cash flow from operations	**(641)**	**(587)**	**2,665**
Capex	(587)	(1,279)	(2,065)
Proceeds from assets sales	0	1	0
Others	(71)	2	29
Other non-current assets changes	0	0	(85)
Cash flow from investing activities	**(658)**	**(1,276)**	**(2,121)**
New share issuance	0	0	92
Shares buyback	(2)	0	0
Net borrowings	1,434	2,736	2,010
Other financing cash flow	0	0	0
Dividends paid	(2)	(220)	(232)
Cash flow from financing activities	**1,430**	**2,516**	**1,870**
Cash and equivalents at beginning of period	213	344	997
Total cash generated	**131**	**653**	**2,414**
Cash and equivalents at the end of period	344	997	3,411

Key ratios			
	12-15A	12-16A	12-17A
Dupont			
Net profit margin	4.2%	3.5%	3.3%
Asset turnover	4.73	4.03	3.52
ROAA	20.1%	14.2%	11.7%
Avg assets/avg equity	2.70	3.50	3.87
ROAE	54.1%	49.8%	45.3%
Efficiency			
Days account receivable	1.11	1.99	7.88
Days inventory	84.4	91.7	79.7
Days creditor	33.7	45.8	48.8
Fixed asset turnover	39.3	30.3	23.9
ROIC	23.6%	18.3%	17.4%
Liquidity			
Current ratio	1.29	1.12	1.20
Quick ratio	0.26	0.26	0.43
Cash ratio	0.07	0.09	0.22
Cash cycle	51.8	47.9	38.8
Growth rate (yoy)			
Revenue growth	60.3%	76.7%	48.7%
Operating profit growth	64.1%	50.5%	39.6%
Net profit growth	60.5%	47.0%	40.0%
EPS growth	22.3%	40.1%	(30.0%)
Share value			
Basic EPS (VND)	7,306	10,237	7,166
BVPS (VND)	16,911	24,943	18,635

Source: VNDIRECT

VIETTEL POST (VTP)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND140,500	VND157,000	1.1%	ADD	LOGISTICS

Outlook – Short term	Outlook – Long term	Valuation
Negative Neutral Positive	Negative Neutral Positive	Negative Neutral Positive

11 January 2019

Nguyen Tien Duc

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Key statistics

52w high (VND)	140,500
52w low (VND)	95,200
3m Avg daily volume (shares)	108,493
3m Avg daily value (VNDmn)	13,703
Market cap (VNDbn)	5,749
Outstanding shares (m)	41.4
Free float (%)	17.8%
TTM P/E (x)	20.5
Current P/B (x)	9.3

Ownership

Viettel Group	68%
MB Capital	5%
Others	27%

Source: VNDIRECT

Viettel Post Corporation (VTP) – a subsidiary of Viettel Group – is an interesting vehicle to ride Vietnam's e-commerce boom. VTP has the second largest market share, is the fastest growing and most profitable delivery company for B2C commerce in Vietnam. We recommend ADD with TP of VND157,000/share.

High growth company in a fast-evolving industry. With the boom in Vietnam's e-commerce industry, the courier market grew at a brisk CAGR of 10.5% over 2013-2017 in value terms (according to MoIT). Viettel Post (VTP) has reinvented itself and is rapidly penetrating the fast-emerging market for express direct-to-consumer deliveries. VTP's market share of total direct-to-consumer deliveries has skyrocketed from just 8.0% in 2010 to 25.7% in 2017, largely led by express delivery market penetration.

VTP's market share gains can be attributed to advanced technology and strong infrastructure. Unlike start-up delivery companies with technological strength but weak financial and infrastructure foundations, traditional postal and parcel delivery companies have extensive networks but outdated technology. VTP has a nation-wide postal network, healthy financial status and has invested aggressively in both technology and logistics systems, giving it a competitive edge.

VTP's core sales is expected to grow at a CAGR of 48.5% to 2020. They expect to hold 30-37% of the parcel delivery market share by 2020 facilitated by the following core strategies: (1) incorporating technological improvements in its products and services, (2) expanding logistics facilities, (3) building a digital store management platform for online SMEs and mom & pop shops including payment and delivery solutions, (4) offering military-level service quality to boost customer trust and loyalty.

Healthy financial status with strong cash reserves and high ROE. Company has a net cash position with cash and equivalents contributing 50% of total assets, supporting future capital investment needs. Unusually for a high growth company, VTP is also highly profitable with an ROE of close to 40%, much higher than the peer average of 17.8%.

Our target price for VTP share in 2019 is VND157,000. We expect stellar growth to continue in 2019 with 48.5% yoy growth in net revenue and 39% growth in net profit, translating to a 2019 forecasted EPS of VND8,183. We use the peer average trailing P/E of 19.2x as the basis for our target price, despite its higher ROE than industry average, to account for the inherent volatility and liquidity risk associated with an UPCOM listing.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	2,928	4,031	4,626	6,868
Revenue growth	47.0%	37.6%	14.8%	48.5%
Gross margin	8.5%	8.6%	11.2%	10.7%
EBITDA margin	5.9%	6.3%	8.9%	8.4%
Net profit (bn)	117	170	271	376
Net profit growth	86.5%	45.7%	59.1%	39.0%
Recurring profit growth	67.6%	40.3%	63.5%	39.0%
Basic EPS	2,821	4,110	6,540	9,092
Adjusted EPS	2,538	3,601	5,886	8,183
BVPS	15,971	16,490	19,826	27,068
ROAE	42.4%	39.8%	41.3%	38.8%

Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	4,031	4,626	6,868
Cost of sales	(3,686)	(4,107)	(6,132)
Gen & admin expenses	(137)	(176)	(251)
Selling expenses	(14)	(22)	(32)
Operating profit	**194**	**321**	**453**
Operating EBITDA	232	380	537
Depreciation and amortisation	**(38)**	**(58)**	**(83)**
Operating EBIT	**194**	**321**	**453**
Interest income	21	29	36
Financial expense	(3)	(14)	(22)
Net other income	1	2	3
Income from associates & JVs	0	0	0
Pre-tax profit	**214**	**338**	**470**
Tax expense	(43)	(68)	(94)
Minority interest	0	0	0
Net profit	**170**	**271**	**376**
Adj. net profit to ordinary	170	271	376
Ordinary dividends	(34)	(45)	(62)
Retained earnings	**136**	**226**	**314**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	477	514	762
Short term investments	401	520	595
Accounts receivables	479	553	821
Inventories	19	25	38
Other current assets	47	54	81
Total current assets	**1,423**	**1,666**	**2,296**
Fixed assets	245	287	353
Total investments	0	0	0
Other long-term assets	83	182	183
Total assets	**1,751**	**2,135**	**2,831**
Short-term debt	193	324	481
Accounts payable	77	86	129
Other current liabilities	992	904	1,091
Total current liabilities	**1,261**	**1,314**	**1,701**
Total long-term debt	0	0	0
Other liabilities	0	0	11
Share capital	297	414	414
Retained earnings reserve	175	390	689
Shareholders' equity	**489**	**820**	**1,120**
Minority interest	0	0	0
Total liabilities & equity	**1,751**	**2,135**	**2,831**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**214**	**338**	**470**
Depreciation & amortisation	38	58	83
Tax paid	(40)	(68)	(94)
Other adjustments	(12)	(14)	(12)
Change in working capital	**239**	**(177)**	**(110)**
Cash flow from operations	**439**	**139**	**338**
Capex	(110)	(101)	(149)
Proceeds from assets sales	3	2	4
Others	(247)	(90)	(39)
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(353)**	**(189)**	**(184)**
New share issuance	0	0	0
Shares buyback	0	0	0
Net borrowings	153	131	157
Other financing cash flow	0	0	0
Dividends paid	(34)	(45)	(62)
Cash flow from financing activities	**119**	**87**	**95**
Cash and equivalents at beginning of period	273	477	514
Total cash generated	**204**	**36**	**249**
Cash and equivalents at the end of period	477	514	762

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	4.2%	5.8%	5.5%
Asset turnover	2.85	2.38	2.77
ROAA	12.0%	13.9%	15.1%
Avg assets/avg equity	3.31	2.97	2.56
ROAE	39.8%	41.3%	38.8%
Efficiency			
Days account receivable	28.9	30.0	30.0
Days inventory	1.92	2.25	2.24
Days creditor	7.62	7.68	7.68
Fixed asset turnover	19.2	17.4	21.5
ROIC	24.9%	23.7%	23.5%
Liquidity			
Current ratio	1.13	1.27	1.35
Quick ratio	1.11	1.25	1.33
Cash ratio	0.70	0.79	0.80
Cash cycle	23.2	24.6	24.6
Growth rate (yoy)			
Revenue growth	37.6%	14.8%	48.5%
Operating profit growth	39.9%	65.4%	41.1%
Net profit growth	45.7%	59.1%	39.0%
EPS growth	45.7%	59.1%	39.0%
Share value			
Basic EPS (VND)	4,110	6,540	9,092
BVPS (VND)	16,490	19,826	27,068

Source: VNDIRECT

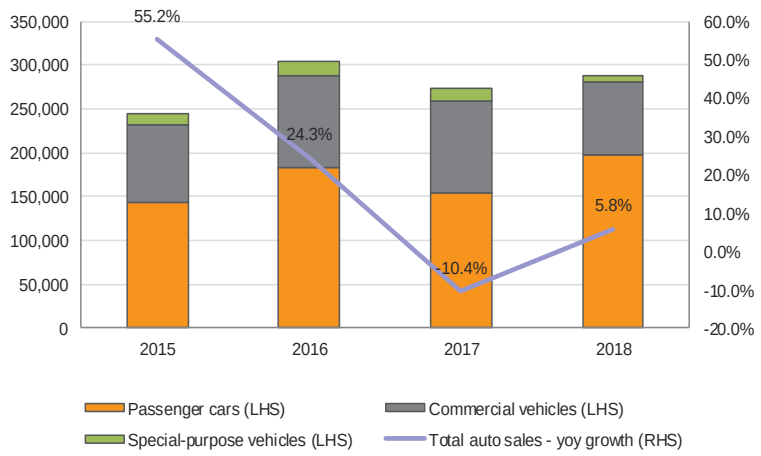
AUTOMOTIVE: RECOVERY TO GO INTO FULL GEAR

Auto sales recovered slightly in 2018

As predicted in our Navigating 2018 report, auto sales made a slight recovery in 2018 with sales growing 5.8% yoy, after falling 10.4% yoy in 2017 according to a report provided by Vietnam Automobile Manufacturers' Association (VAMA). The fall in sales volume in 2017 was due to the postponement of purchases as customers began to anticipate a lowering of car prices when the import tariff for Complete Built-Ups (CBUs) from ASEAN countries was dropped from 30% to 0% on 1 Jan, 2018. After the new tariff came into effect, the pent-up demand from 2017 was unleashed, driving the recovery in sales in 2018.

The recovery was muted due to a slew of non-tariff barriers imposed on car imports. However, the sales volume only increased slightly as auto sales was disrupted by a new regulation which imposes non-tariff barriers on imported CBUs from ASEAN countries. In October 2017, the Vietnamese government issued Decree 116 which poses two challenges to cars imports: 1) each car model must have a Vehicle Type Approval (VTA) issued by the exporting country certifying that the model satisfies the safety and emission standards of Vietnam; 2) a sample is selected from every batch of imported cars for safety and emission tests, instead of having only the first shipment tested, as was the case previously. The first rule disrupted car imports into Vietnam in the first three months of 2018, while the second rule made the customs clearance process lengthier and also more costly, as car producers now incur additional costs for warehousing.

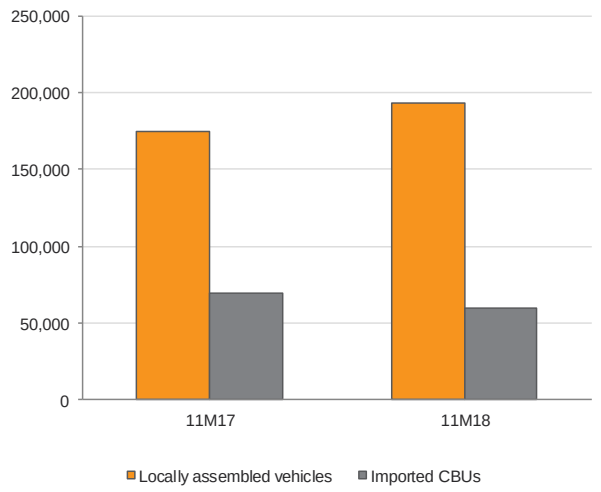
Figure 177: Auto sales recovered slightly in 2018 (units)



Source: VNDIRECT, VAMA

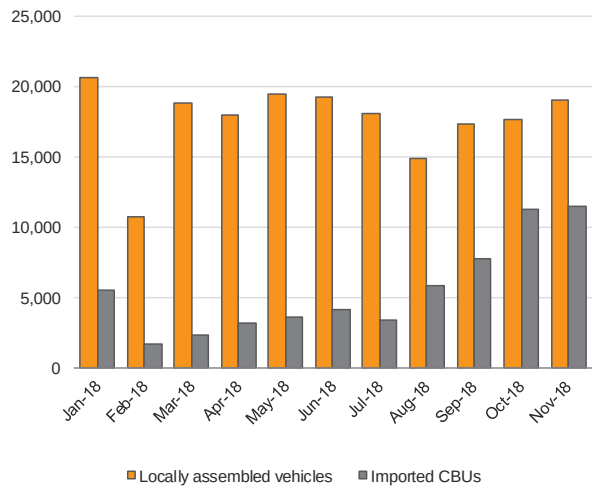
Decree 116 created a shortage in supply of imported cars. As a result, local assemblers ramped up car sales to fill the void. In 11M18, sales volume of locally assembled autos grew 10.7% yoy while the sales volume of imported autos declined 13.8% yoy. Although the new decree disrupted car imports in early 2018, car producers eventually obtained their VTAs from Thai and Indonesian authorities in March 2018. Honda imported its first batch of cars in March 2018 while Toyota and Mitsubishi imported their first batch in late June 2018. As importers have successfully obtained their VTAs, imported car sales have improved in 2H18 and should continue to do so into 2019.

Figure 178: Local assemblers ramped up sales amid the absence of imported vehicles (units)



Source: VNDIRECT, VAMA

Figure 179: Imported vehicle sales recovered in 2H18 (units)



Source: VNDIRECT, VAMA

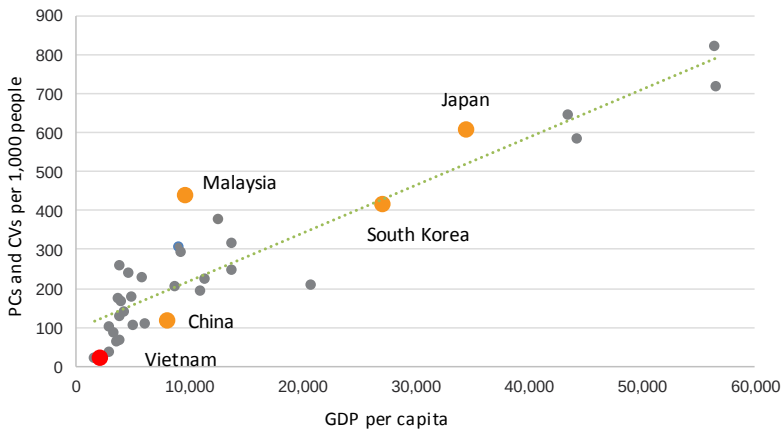
Besides getting VTAs from exporting countries, auto companies are proposing and advocating a Mutual Recognition Arrangement (MRA) between Thailand and Vietnam. According to this agreement, cars to be exported to Vietnam will be inspected at testing agencies in Thailand. Therefore, when these cars are exported to Vietnam, some inspections will be waived and clearance time will be reduced. This agreement will speed up the customs clearance process and reduce costs for auto companies, but this cost reduction will only be realised in the medium-term rather than in the short-term.

Sales growth should accelerate into 2019

We expect auto sales growth to improve in 2019, based on the following considerations: 1) more importers will successfully adjust to the new regulation (i.e. obtaining VTAs from exporting countries) resulting in an increase in the volume of imported CBUs in 2019; 2) demand remains strong with robust economic growth, rising incomes and supported by current low car ownership rates.

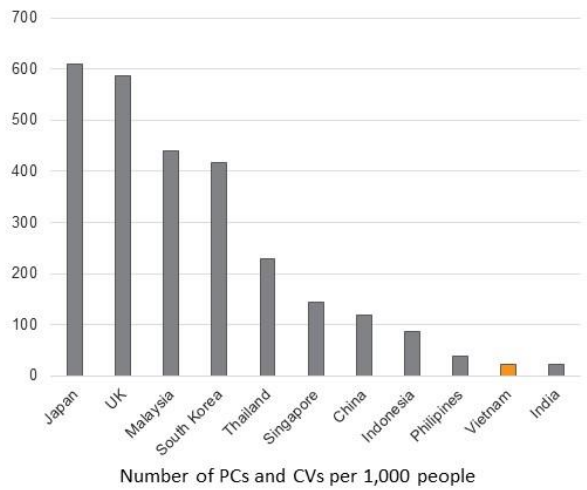
According to the International Organization of Motor Vehicle Manufacturers (OICA), Vietnam is among the countries with the lowest levels of car ownership in Asia, with only 23 passenger cars and commercial vehicles per 1,000 people in 2015, a low car ownership rate even in a regional context. Vietnam's middle class population is expected to grow rapidly over the next decade and this will fuel a rapid rise in demand for cars. Our macro team projects that Vietnam's GDP will grow by 6.6% in 2019. As such, purchasing power will continue to increase, supporting car sales growth. According to a BMI report, auto sales are expected to grow at 19.9% in 2019 as more CBUs get imported into Vietnam after importers obtain VTAs from exporting countries.

Figure 180: GDP per capita versus Passenger Cars (PCs) and Commercial Vehicles (CVs) penetration rates in 2015



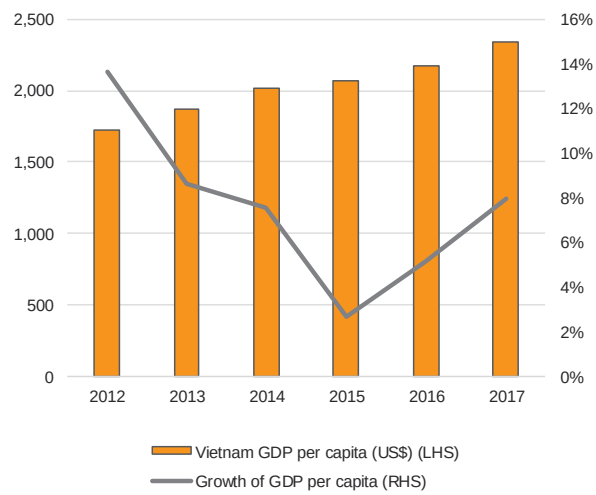
Source: World Bank, , VNDIRECT

Figure 181: Vietnam has a low car ownership rate (Data: 2015)



Source: OICA, VNDIRECT

Figure 182: Vietnam's GDP per capita has grown steadily in the past few years



Source: World Bank, VNDIRECT

The elimination of tariffs on imported Complete Knocked-Downs (CKDs) will increase competition for pure importers

In anticipation of a surge in car imports from ASEAN countries into Vietnam starting in 2018, the Vietnamese government issued Decree 125/2017 to support local car production. Decree 125, effective on 1/1/2018, cut the tariff for imported CKDs to 0% from 15-30% previously during the 5-year period from 2018-2022. The 0% tariff reduces production costs and helps locally-assembled cars to remain competitive versus imported cars in an era of 0% tariffs on CBUs. However, only CKDs of the vehicle models with 40%-and-higher localisation rates are eligible for 0% tariffs. In addition, to be eligible for this new tariff, auto producers must commit to produce a certain volume of vehicles. As the required volume is relatively large, only a handful of auto producers can meet the requirement of Decree 125, including Hyundai Thanh Cong, Toyota Vietnam and Thaco.

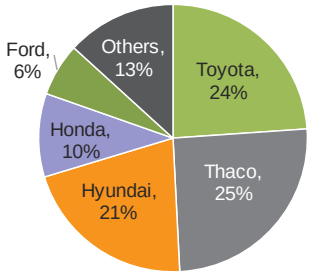
Figure 183: Required production volume under Decree 125/2017

	2018	2019	2020	2021	2022
Minimum total volume	8,000	8,500	10,000	11,500	13,500
Minimum volume of the committed model	3,000	3,500	4,000	4,500	5,000

Source: Decree 125/2017

The reduction of import tariffs on CKDs will help local vehicles stay competitive against the cheaper imported cars, but we do not expect the price of local vehicles to fall below the price of imported cars due to the low localisation rate of Vietnam's auto industry. Vietnam's auto industry is fragmented with a low localisation rate of 20-40%, compared to the 80% rate in neighbouring countries like Thailand and Indonesia which have much more developed automotive supply chains. In our view, the main purpose of the import tariff elimination on CKDs is to protect local assemblers by reducing costs but it has yet to create a competitive edge over car importers until the localisation rate improves.

Figure 184: Vietnam's passenger car market share by OEM, as of Nov 2018



Source: VAMA, VNDIRECT

We believe that the new zero tariff on CKDs will increase competition for pure importers as they will need to compete for the sales which would have accrued to them if the tariff for CKDs had not been reduced. In Vietnam's auto industry, many players are both auto dealers and assemblers. Big OEMs such as Toyota and Hyundai have factories in Vietnam and other ASEAN countries. Hence, they get double benefits from zero tariff on both CBUs and CKDs. These companies will allocate vehicle production capacity in Vietnam and in other ASEAN countries in the most cost-effective way, taking advantage of the lower tariffs on imports of both CBUs and CKDs. Hence, the zero tariff on CKDs might hurt pure importers but there are only a small number of pure importers in Vietnam.

Figure 185: Vietnam's passenger car landscape by OEM

Companies	Importer/assembler	Brand portfolio
Toyota	Importer and assembler	Camry, Corolla Altis,Vios, Innova, Fortuner, Landcruiser, Land Prado, Yaris, Avanza, Wigo, Rush, Alphard
Honda	Importer and assembler	CR-V, City, Jazz, Accord, Odyssey, Civic, HR-V
Ford	Importer and assembler	Fiesta, Focus, Ranger, Everest, EcoSport
Thaco	Assembler	Kia, Mazda, CX-5, BT-50, Peugeot
Hyundai	Assembler	Grand i10, Accent, Elantra, Kona, Tucson, SantaFe
Mitsubishi	Importer and assembler	Outlander, Pajero Sport, Mirage, Attrage, Triton, Xpander
GM Vietnam	Importer and assembler	Spark, Aveo, Cruze, Orlando, Trax. Captiva, Trailblazer, Colorado
Isuzu	Importer	D-Max, mu-X
Suzuki	Importer	Vitara, Ertiga, Ciaz, Celerio

Source: VNDIRECT

VinFast's aggressive expansion might impact the market from 2020 onwards

Vinfast is a subsidiary of Vingroup **(VIC VN, Not rated**) - the largest private sector company in Vietnam. Vinfast was established in June 2017 with the key aim of producing cars with internal combustion engines, environmentally-friendly electric cars and motorcycles. Vinfast has quite an aggressive plan with 250,000 cars per annum

planned for production in the first phase from 2017 to 2024 and 500,000 units per annum planned for the second phase from 2025. To put this into perspective, in 11M18, the collective passenger car sales of companies that are members of the Vietnam Automobile Manufacturers' Association (VAMA) was 172,515 cars. VAMA members also accounted for around 70% of total car sales. Vinfast has pulled in best-in-class talent from General Motors, Deluca and Pininfarina. In July 2018, Vinfast acquired General Motors' operations in Vietnam, including a factory which it will use to produce hatchbacks, 24 showrooms, the right to distribute Chevrolet cars in Vietnam and a patent for a brand-new hatchback model.

Vinfast has started selling its cars but will only start deliveries of its sold models in September 2019. Its products are new to the market, therefore, customers will need some time to test the products. As Vinfast will not deliver cars until late 2019, and it takes time for brand building, we expect the launch of Vinfast cars will not have a significant impact on the market in 2019. However, with an aggressive production plan, Vinfast is surely a new threat to existing players from 2020 onwards. However, the magnitude of its impact will depend on the success of its car models, which is unknown at the moment.

We look at Vinfast as a new player in the auto industry with a lack of experience compared to existing brand names like: Toyota, Honda, Ford, Mazda and Yamaha. However, the revolution of electric automobiles will reconstruct the landscape of the car industry and this disruption could be exploited by Vinfast. Moreover, Vinfast is also cooperating and developing a synchronous ecosystem for the automobile and electric motorcycle manufacturing industry. Vinfast's vision for electric vehicles, including e-scooters, electric cars, and electric buses are also aligned with the environmental protection and emission regulation standard objectives of the Vietnamese government. This should benefit Vinfast's long-term growth objectives.

AUTOMOTIVE SECTOR STOCK PICKS: WE PREFER DEALERS OF MID-MARKET PASSENGER CAR BRANDS

We do not cover any stocks in this sector, but have been monitoring some stocks in this area that demonstrate potential. We expect the volume of imported passenger cars from ASEAN to increase in 2019 as more companies adjust to the new regulations on imported cars. As such, we like companies that distribute imported passenger cars in the mid-market segment. We also like companies that can switch between imported CBUs and locally assembled cars, as they benefit from zero tariffs on both imported CBUs and imported CKDs.

Figure 186: Vietnam's major auto companies[1]

Company	Company type	Main products	Source	Brand portfolio
Thaco	Assembler & Dealer	Passenger car, truck, bus	CKD	Mazda, Kia, Peugeot, Thaco truck and bus
VEA	Assembler & Dealer	Agriculture vehicles & machinery	CBU and CKD	Ownership in Toyota, Honda, Ford
SVC	Dealer	Passenger car	CBU and CKD	Hyundai, Toyota, Ford, Suzuki, Volvo, Chevrolet, Veam, Mitsubishi, Fuso, Honda, Hino
HHS	Dealer	Truck, bus	CBU	Dong Feng
HAX	Dealer	Passenger car	CBU and CKD	Mercedes-Benz
HTL	Dealer	Truck, bus	CBU	Datano, Hino, Shinmaywa
TMT	Assembler & Dealer	Truck, bus	CBU and CKD	Tata, Sinotruk, Hyundai (truck)
CMC	Assembler & Dealer	Industrial vehicle	CBU and CKD	Komasu, Hitachi
CTF	Dealer	Passenger car	CBU and CKD	Ford

Source: VNDIRECT

[1] CTF and HAX import CKDs for car maintenance and repairing

Among passenger car dealers, **Saigon General Service Corporation (SVC VN, Not rated) and City Auto Corporation (CTF VN, Not rated)** are likely the most exposed to the recovery in car imports, as they are distributing most of the low-end and medium-range brands in the market. In addition, brands distributed by these two companies have factories in both Vietnam and ASEAN countries, therefore, SVC and CTF could quickly switch between selling imported CBUs and locally assembled cars. However, we prefer SVC to CTF due to its diversified brand portfolio, which could fuel higher sales growth when more imported cars enter Vietnam in 2019.

Vietnam Engine and Agricultural Machinery Corporation, also known as VEAM, (VEA VN, Not rated) is another company that could benefit from the recovery in car imports. Although VEA's core business is manufacturing agricultural machinery and trucks, it has stakes in Toyota Vietnam (20% stake), Honda Vietnam (30% stake) and Ford Vietnam (25% stake) and all of VEA's profit is generated from through these equity associates. Toyota, Honda and Ford sell both imported cars and locally assembled cars, and they can benefit from lower tariffs for imported CBUs and CKDs. As these companies obtained VTAs in 2018, their sales volume for imported cars will improve in 2019, thereby fuelling profit growth. VEA, therefore, will benefit from higher financial income.

Hang Xanh Motors Service JSC (HAX VN, Not rated) is a name to note as well. The company has been performing well in the luxury car segment with the premium brand Mercedes-Benz. Decree 116/2017 disrupted car imports in early 2018 and HAX was only able to import a small number of cars from September 2018 onwards. As the company adjusts to the new regulation, car imports will recover in 2019. Imported CBUs account for around 10% of HAX's product mix with the remaining cars sold largely being locally assembled by Mercedes Benz Vietnam. In addition, HAX recently secured the dealership for Nissan and is under negotiations to become a dealer for Vinfast. The company will start selling Nissan cars in 2019. We expect the new products to boost earnings in 2019.

In the short-term, some local assemblers may suffer lower sales growth due to the increased volume of imported cars. In 11M18, the sales volume of locally assembled vehicles grew 10.7% yoy while the sales volume of imported vehicles declined 13.8% yoy, as local assemblers filled up the void left by importers that struggled to cope with newly imposed non-tariff barriers. With the comeback of imported cars in 2019, there will be more competition for local assemblers.

Figure 187: Automotive peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
TMT	TMT	15	-9.1%	-9.1%	0.4%	2.0%	3.9	36.8	0.8
CMC	CMC	1	n/m	n/m	-3.4%	-6.5%	1.1	-6.4	0.4
Assembler average		-			**-1.5%**	**-2.3%**	**2.5**	**15.2**	**0.6**
VEAM Corp	VEA*	2,138	28.0%	28.0%	26.8%	31.4%	0.0	10.8	3.0
Savico	SVC	47	38.4%	38.4%	4.0%	10.7%	1.8	7.4	1.1
Hoang Huy Service	HHS	43	167.3%	174.2%	5.8%	6.2%	0.1	5.1	0.3
City Auto	CTF	40	258.4%	47.6%	5.0%	15.8%	2.3	13.0	2.1
Hang Xanh Motor	HAX	24	21.2%	21.2%	6.1%	22.6%	2.7	6.6	1.4
Truong Long	HTL	9	-6.4%	-6.4%	3.4%	8.0%	1.3	12.3	1.1
Dealer Average					**8.5%**	**15.8%**	**1.4**	**9.2**	**1.5**

Price as of 11 Jan 2019

Source: Stoxplus, VNDIRECT

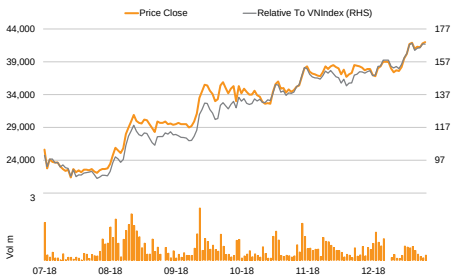
VEAM CORP (VEA)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND41,700	N/A	6.72%	NOT RATED	AUTOMOTIVE

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Lê Hồng Thanh (Andy Le)
thanh.lehong@vndirect.com.vn

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	42,000
52w low (VND)	21,381
3m Avg daily volume (shares)	500,087
3m Avg daily value (VNDmn)	18,201
Market cap (VNDbn)	55,411
Outstanding shares (m)	1,314
Free float (%)	11
TTM P/E (x)	10.8
Current P/B (x)	3.0

Ownership

Ministry of Industry and Trade	88.5%
Hoa An LLC	6.0%
Others	5.5%

Source: VNDIRECT

Steady profits from stakes in the local subsidiaries of leading auto and motorbike OEMs.

VEA has benefitted from its stakes in large auto producers in Vietnam. VEA is a State-Owned Enterprise (SOE) specialising in the manufacture of agricultural machinery and equipment, motorbikes and automobile spare parts, as well as trucks. However, 97% of its profit is contributed by its affiliates. VEA currently has stakes in Toyota Vietnam (20%), Honda Vietnam (30%), and Ford Vietnam (25%), which are well-known auto producers in Vietnam.

VEA to ride Vietnam's fast growing car market. VEA and its affiliates collectively have the largest share in the passenger car market at 40% as of Nov 2018, followed by Thaco (25% share) and Hyundai (21% share). With the leading market share and the diversified product portfolio of its affiliates, VEA is poised to benefit from the strong growth of Vietnam's passenger car market, driven by rising income and supported by current low car ownership. According to BMI, Vietnam passenger car sales is projected to grow at 23.1% CAGR over FY19-22.

Stable profit from stake in Honda thanks to the latter's dominant position in Vietnam's motorbike market. As Vietnam's motorbike market has entered a saturation stage, sales are expanding at a low single-digit rate (3.5% growth in 2018). However, Honda is a dominant brand in this market with 73% market share as of end-3Q2018. We expect Honda will sustain its leading position due to its prestigious reputation, well-developed product portfolio and extensive distribution network. In addition, the shift from manual motorbikes to higher margin automatic motorbikes is another driver for Honda's bottomline, and consequently VEA's profit. (In 2017, scooters accounted for 48% of Honda sales compared to 42% in 2015).

VEA trades at a trailing P/E of 10.8x, higher than Vietnam's auto dealer peer average trailing P/E of 8.9x. However, VEA has a far superior ROE of 31.4% versus the peer average ROE of 12.7%.

Key risks: Upside risk includes a potential listing on HOSE, which was planned in 2018 but has yet to be implemented. A medium term downside risk is the growing competition posed by Vingroup's aggressive expansion plans in both the passenger car and motorbike markets.

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	5,086	5,893	6,307	6,563
Revenue growth		15.9%	7.0%	4.1%
Gross margin	8.4%	10.6%	10.1%	9.4%
EBITDA margin	0.7%	0.4%	0.4%	0.7%
Net profit (bn)	3,330	4,373	4,515	5,046
Net profit growth		31.0%	3.0%	12.0%
Basic EPS	7,336	8,922	3,390	3,797
Adjusted EPS	7,336	8,922	3,390	3,797
BVPS	30,11	30,61	9,87	13,84
ROAE	26.8%	30.2%	31.5%	32.0%

Source: VNDIRECT

Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	5,893	6,307	6,563
Cost of sales	(5,268)	(5,669)	(5,943)
Gen & admin expenses	(614)	(530)	(595)
Selling expenses	(225)	(315)	(282)
Operating profit	**(214)**	**(207)**	**(258)**
Operating EBITDA	29	35	47
Depreciation and amortisation	**(243)**	**(242)**	**(304)**
Operating EBIT	**(214)**	**(207)**	**(258)**
Interest income	73	435	254
Financial expense	(150)	(318)	(42)
Net other income	37	26	(3)
Income from associates & JVs	4,590	4,576	5,170
Pre-tax profit	**4,337**	**4,512**	**5,122**
Tax expense	33	(20)	(36)
Minority interest	3	12	(40)
Net profit	**4,373**	**4,504**	**5,046**
Adj. net profit to ordinary	4,373	4,504	5,046
Ordinary dividends	(50)	(2,115)	(3,716)
Retained earnings	**4,323**	**2,389**	**1,330**

Balance sheet

(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	1,330	3,799	2,488
Short term investments	182	304	2,152
Accounts receivables	1,669	1,688	2,610
Inventories	2,024	2,372	3,503
Other current assets	117	111	234
Total current assets	**5,321**	**8,274**	**10,987**
Fixed assets	2,453	2,606	2,634
Total investments	8,780	9,044	9,265
Other long-term assets	519	453	475
Total assets	**17,073**	**20,376**	**23,361**
Short-term debt	505	428	285
Accounts payable	444	450	2,155
Other current liabilities	586	5,944	2,122
Total current liabilities	**1,535**	**6,822**	**4,563**
Total long-term debt	235	198	175
Other liabilities	52	46	48
Share capital	4,901	13,288	13,288
Retained earnings reserve	8,081	(250)	4,993
Shareholders' equity	**15,045**	**13,147**	**18,406**
Minority interest	206	163	169
Total liabilities & equity	**17,073**	**20,376**	**23,361**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**4,337**	**4,512**	**5,122**
Depreciation & amortisation	243	242	304
Tax paid	(19)	(33)	(50)
Other adjustments	(4,235)	(4,744)	(1,538)
Change in working capital	**(183)**	**5,006**	**(4,380)**
Cash flow from operations	**143**	**4,983**	**(541)**
Capex	(189)	(453)	(462)
Proceeds from assets sales	7	5	138
Others	38	114	(12)
Other non-current assets changes	(46)	17	3,461
Cash flow from investing activities	**(190)**	**(317)**	**3,125**
New share issuance	70	0	0
Shares buyback	0	(0)	0
Net borrowings	114	(81)	(178)
Other financing cash flow	0	0	0
Dividends paid	(50)	(2,115)	(3,716)
Cash flow from financing activities	**134**	**(2,197)**	**(3,894)**
Cash and equivalents at beginning of period	1,243	1,330	3,799
Total cash generated	**87**	**2,469**	**(1,311)**
Cash and equivalents at the end of period	1,330	3,799	2,488

Key ratios

	12-15A	12-16A	12-17A
Dupont			
Net profit margin	74.2%	71.4%	76.9%
Asset turnover	0.36	0.34	0.30
ROAA	26.8%	24.1%	23.1%
Avg assets/avg equity	1.14	1.33	1.39
ROAE	30.4%	32.0%	32.0%
Efficiency			
Days account receivable	100	92	119
Days inventory	140	153	215
Days creditor	31	29	132
Fixed asset turnover	2.60	2.49	2.51
ROIC	27.3%	32.3%	26.5%
Liquidity			
Current ratio	3.47	1.21	2.41
Quick ratio	2.15	0.87	1.64
Cash ratio	0.99	0.60	1.02
Cash cycle	209	216	202
Growth rate (yoy)			
Revenue growth	15.9%	7.0%	4.1%
Operating profit growth	8.0%	(3.1%)	24.4%
Net profit growth	31.3%	3.0%	12.0%
EPS growth	21.6%	(62.0%)	12.0%
Share value			
Basic EPS (VND)	8,922	3,390	3,797
BVPS (VND)	30,697	9,894	13,852

Source: VNDIRECT

AVIATION: A FANTASTIC LONG-TERM STORY DESPITE NEAR TERM HEADWINDS

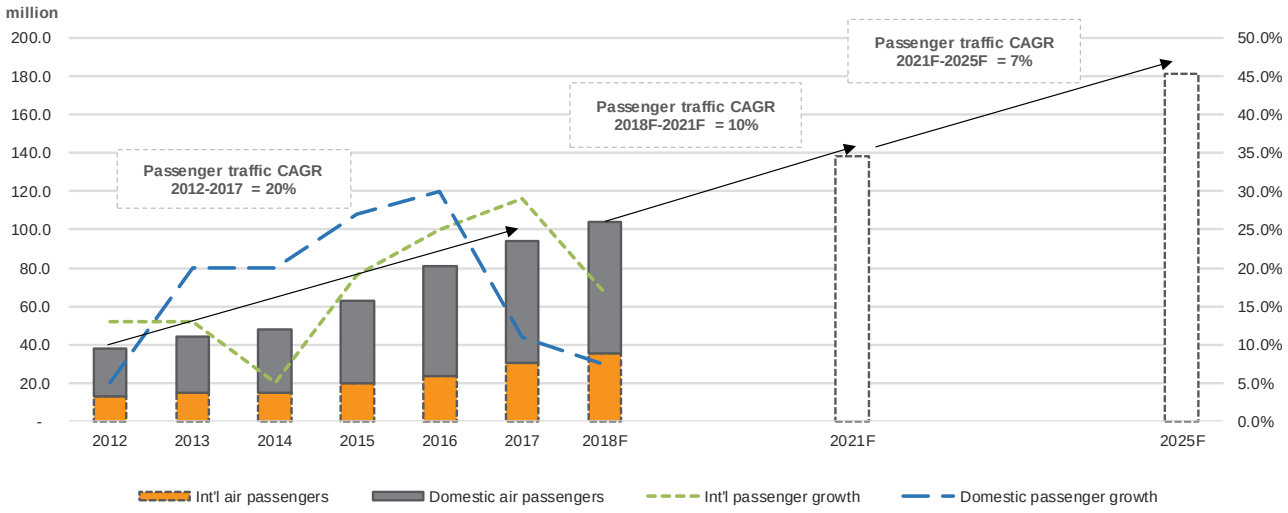
Trend 1: Passenger growth has slowed but likely to sustain a healthy growth momentum in the medium term

Double digit passenger throughput growth in 2018 despite airport capacity constraints

According to Civil Aviation Authority of Vietnam (CAAV), all 21 airports in Vietnam collectively served about 104m passengers in 2018, up 10.4% on a y-o-y basis. Domestic passengers accounted for approximately 66% share of country passenger traffic and grew by only 7.4% yoy given severe capacity constraints at key airports as domestic flights usually operate during peak hours (from 6AM to 10PM), unlike international flights. Meanwhile, international passenger throughput surged by 16.8% yoy in 2018, fuelled by continued strong growth in foreign tourist arrivals and new international flight route launches. In 2018, there were 15 new flight routes launched to connect Vietnam to the rest of the world.

After clocking phenomenal growth rates in the past five years, air passenger traffic is expected to grow by around 10% p.a in the period 2018F-2021F and moderate to around 7% in the period 2021F-2025F (source: Airports Corporation of Vietnam). We believe the two main pillars of growth for Vietnam's aviation sector are: 1) continued rise in international visitors to Vietnam and (2) higher domestic travel demand amid increasing leisure spending and lower average airfares.

Figure 188: Vietnam air passenger traffic volume: historical and forecasted



Source: CAAV, ACV, VNDIRECT

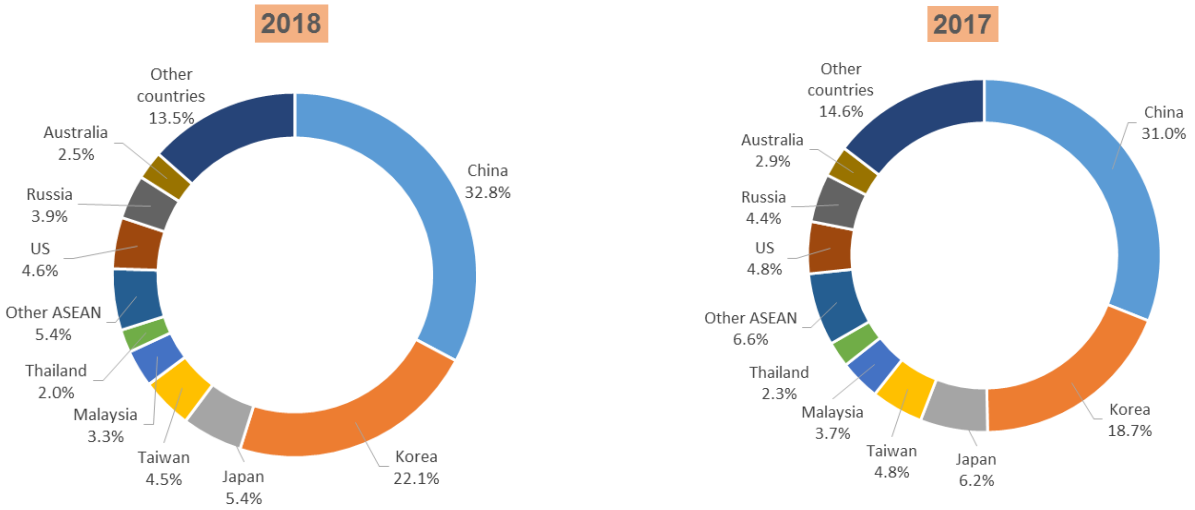
International passenger traffic boosted by surging international tourist arrivals, largely from Northeast Asia

According to the General Statistics Office of Vietnam (GSO), in 2018, international visitor arrivals to Vietnam reached 15.5m pax, up 19.9% yoy, largely driven by Chinese (+23.9% yoy) and Korean tourists (+44.3% yoy). We expect that the proportion of Korean and Japan visitors will rise in the future as Vietnam – South Korea and Vietnam – Japan diplomatic relations continue to improve and trade and investment ties between Vietnam and these countries continues to flourish. At the moment, South Korea and Japan are Vietnam's largest

FDI investors, followed by Singapore and Taiwan. Both South Korea and Japan have also started to loosen visa requirements for Vietnamese visitors this year. Lower visa requirements will further encourage the number of Vietnamese outbound travellers, which have been growing significantly in recent years and could become a new engine of passenger throughput growth in the near future.

Nonetheless, international visitor arrivals by air in 2018 grew by 14.4% yoy, lower than an increase of 32.1% yoy seen in 2017. This slowdown was due to the sluggish growth in Russian tourist arrivals of 5.7% yoy (versus 32.3% yoy in 2017) due to the World Cup which was hosted in Russia during May and June of 2018 and, perhaps, also due to weakness in the Russian ruble. Also, the delay in visa exemption extensions for five EU countries (Germany, Italy, France, UK and Spain) in 1Q18 has dampened the growth in tourist arrivals from these countries (8.1% yoy in 2018 vs. 16.6% yoy in 2017).

Figure 189: International tourist arrivals in VN by source country



Source: GSO, VNDIRECT

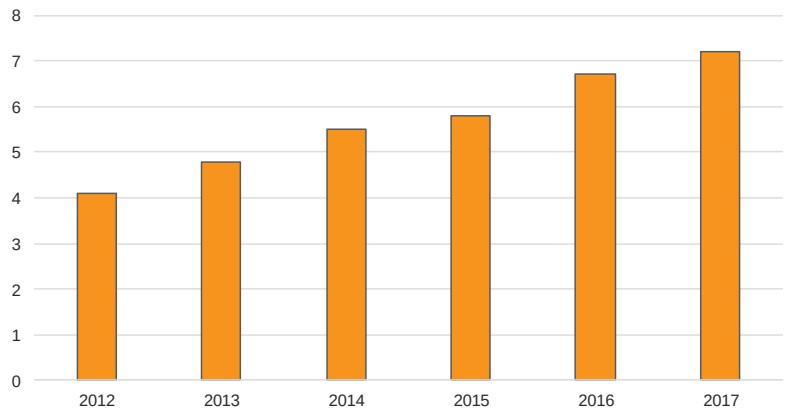
Despite the recent deceleration, we believe tourist arrivals are likely to sustain double-digit growth thanks to several efforts of the Government recently to promote Vietnam as an international tourism destination, such as extending visa waivers for EU-5 countries till 2020, implementing e-visa schemes for other country visitors, etc.

Upwardly-mobile Vietnamese now prefer to spend their holidays overseas.

An increasing number of upper-middle-class and upper-class Vietnamese prefer to take their holidays in foreign countries, even during the Tet holiday that is traditionally the time for family gatherings. These days, many upper-class Vietnamese choose to hold their Tet family gatherings overseas. This is a significant change in the preferences and spending behaviour of the Vietnamese people. According to Euromonitor, Vietnamese outbound tourism has been growing by 10-15% p.a. over the past three years and could maintain double-digit growth rates over the next decade. Top foreign travel destinations for Vietnamese travellers are China, Cambodia and Thailand due to the affordability of these destinations. A small number of wealthy travellers favour the US and Germany. Japan and South Korea are also increasingly becoming destinations of choice for many travelers as they gradually loosen visa policies for Vietnamese tourists. The main reason for this is the strengthening of bilateral economic,

political and cultural relationships between Vietnam and these countries.

Figure 190: Number of Vietnamese outbound trips (m)



Source: EUROMONITOR, VNDIRECT

Open skies policies will create ample room for international passenger growth

In July 2018, the Ministry of Transport (MoT) proposed to raise the Foreign Ownership Limit (FOL) for airlines from the current 30% to 49%. Aside from increasing FOL, the draft decree would also remove the difference in minimum charter capital requirements between international and domestic flight operators in Vietnam, thus levelling the playing field.

We believe the draft decree reflects the Government's efforts to broaden its engagement with the ASEAN Single Aviation Market (ASAM), better known as ASEAN Open Skies agreement which has been fully ratified by member countries since April 2016. ASAM is a regional aviation policy aiming to establish an integrated aviation market in Southeast Asia. The policy is devised to fully liberalise international air travel within Southeast Asia.

The neighbouring countries of Singapore and Thailand have already taken significant steps to fully liberalise their respective limits on foreign participation in locally-based airlines. Meanwhile, Indonesia, Malaysia and Cambodia have raised their FOL on local airlines up to 49%.

Figure 191: Airline foreign ownership limits of ASEAN countries

Country	Maximum percentage of FOL permitted by national statute
Singapore	100%
Thailand	100%
Indonesia	49%
Cambodia	49%
Malaysia	45%
Philippines	40%
Vietnam	30%

Source: IDEAS, May 2018

Trend 2: Private investors eyeing airport infrastructure investments in Vietnam

Recent rapid passenger traffic growth has created stresses and strains on Vietnam's aviation infrastructure. We believe capacity constraints across five major airports was the key factor behind the slowdown in

domestic passenger traffic in the past few quarters to single-digit rates after a long period of double-digit growth.

In order to alleviate the current traffic congestion, a number of airport capacity expansions are in the pipeline through 2050. Among these, Long Thanh International Airport (LTI) is a key project. Once operational, this mega project is expected to become a state-of-the-art airport and a major transit hub in Southeast Asia. The airport is expected to serve the greater HCMC metropolitan area and ease the current severe congestion at HCMC's Tan Son Nhat Airport.

Figure 192: Current capacity and expansion plan by key airport

Capacity & pax througput as of end-2017 (in million pax.)					Capacity expansion pipeline	
Airports	**IATA Code**	**Designed capacity**	**2017 pax. Throughput**	**Designed capacity utilization**	**Upgraded capacity**	**Period of completion**
Tan Son Nhat International Airport (TIA)	SGN	28.0	36.0	129%	45.0	2019-2020
Noi Bai International Airport (NIA)	HAN	25.0	23.8	95%	40.0	2020-2023
Danang International Airport (DIA)	DAD	10.0	10.8	108%		
Phu Quoc International Airport (PQIA)	PQC	4.0	2.7	68%	5.0	2019 -2021
Cam Ranh International Airport (CRIA)	CXR	2.5	6.4	256%	6.0	2018
Total 21 airports		**91.0**	**94.2**	**104%**		
Long Thanh International Airport	LTI				100.0	
Phase 1					*25.0*	*2020-2025*
Phase 2					*25.0*	*2025-2035*
Phase 3					*50.0*	*2035-2050*

Source: Ministry of Transport, CAAV, VNDIRECT

Rapid growth and the huge potential of the local aviation industry has whetted the appetite of private investors to jump into airport infrastructure, especially given limited government resources to fund infrastructure expansion. So far, three airport infrastructure projects are being carried out by private investors, including Van Don International Airport (VDO), DAD International terminal and CXR International terminal. Located in Quang Ninh province and operating since Dec 2018, VDO with designed capacity of 2.5 m pax per annum is owned and operated by Sun Group, a leading hospitality and entertainment project developer. DAD's new international terminal opened in Jun 2017 and was developed by a consortium comprising ACV (10% stake) and Taseco-Hancorp-AOV Investment (90% stake). Similarly, CXR's new international terminal, which was developed by a JV between ACV (10% stake), IPP Group (60% stake) and another four shareholders (Yen Khanh, NASCO, Vietjet, VietXuan Moi, undisclosed stake) was inaugurated in July 2018 with an initial capacity of 4m passengers per year and a possible capacity expansion of up to 8m per year.

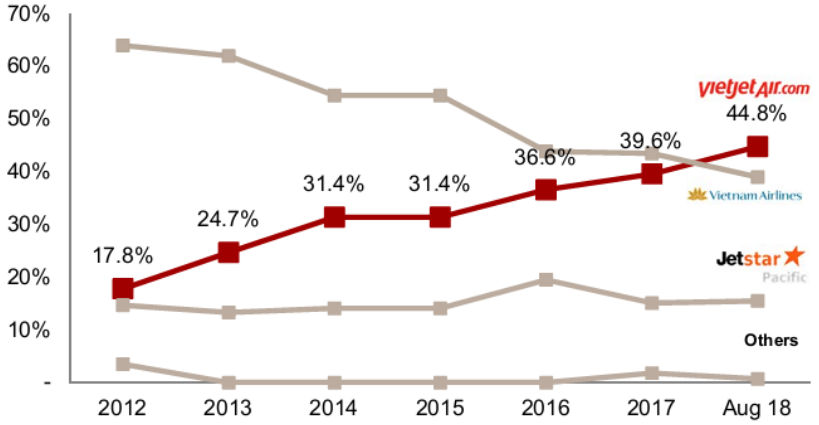
We observe that many private investors are in line waiting for approval from the government to invest in aviation infrastructure. IPP Group is also keen on developing a runway in PQC and a new international terminal in Tuy Hoa Airport. Meanwhile, FLC Group (FLC VN), owner of Bamboo Airways, received approval-in-principle to upgrade and expand Dong Hoi to an international airport with designed capacity of 10m pax per annum. Private investors also show strong interest in other local airports such as Chu Lai (in Quang Nam province) and Cat Bi (in Hai Phong province).

We expect that the growing participation of the private sector would speed up capacity expansion and ease bottlenecks on industry growth.

Trend 3: Increasing competition with fleet expansion and entry of newcomers

Vietnamese airlines are all racing to expand their fleets to capture the continued growth in the industry and competition is heating up as a result. Vietjet Air (VJC) has received 17 new aircraft in 2018 and another 13 aircraft are expected to be delivered in 2019. Vietnam Airlines (HVN) took delivery of its first A321neo in Nov 2018 while another 19 A321neo aircraft will join the fleet in 2019.

Figure 193: In 2018, Vietjet surpassed Vietnam Airlines to be the largest carrier by domestic market share



Source: Vietjet Air

While Vietnam's aviation market is currently dominated by VJC and HVN, Bamboo Airways, a startup carrier with the backing of conglomerate FLC Group is looking to enter the market although the company has not announced its first flight yet after several delays. However, the company disclosed that they were well-prepared to commence operations with a fleet of 5 leased A320 Airbus as of end-2018. Meanwhile, 44 new airplanes ordered under two contracts worth US$8.8 billion signed with Airbus and Boeing are tentatively scheduled to be delivered starting in 2020. Bamboo Airways plans to provide direct international flights to destinations where FLC Group resorts and hotels are located, such as Quy Nhon, Quang Ninh, Hai Phong, and Quang Binh, in addition to domestic flights connecting tourist spots in Vietnam.

Along with the launch of Bamboo Airways, regional behemoth Air Asia recently signed a MOU with two local partners Haiau Aviation (HAA) and Thien Minh Group (TMG) to set up a JV Low Cost Carrier (LCC). AirAsia owns 30% of the new venture, the maximum allowed foreign ownership of an airline under current law, although the government is considering lifting the limit to 49% as mentioned earlier. The launch date has not been announced yet as several licences need to be acquired. AirAsia expects the venture to focus on underserved routes connecting key cities including Hanoi and Ho Chi Minh City. Besides, AirAsia recently launched three new international flight routes connecting Vietnam in 2018 which increased their total routes into Vietnam to five.

We believe that newcomers' entry will spur intense competition and further lower fares, thereby boosting the addressable market as prices come within reach of an ever greater segment of the Vietnamese population. Furthermore, we don't expect to see a clear winner in this race as companies compete largely on price, to the ultimate benefit of passengers.

Trend 4: Jet fuel price volatility might hurt the earnings growth of airlines

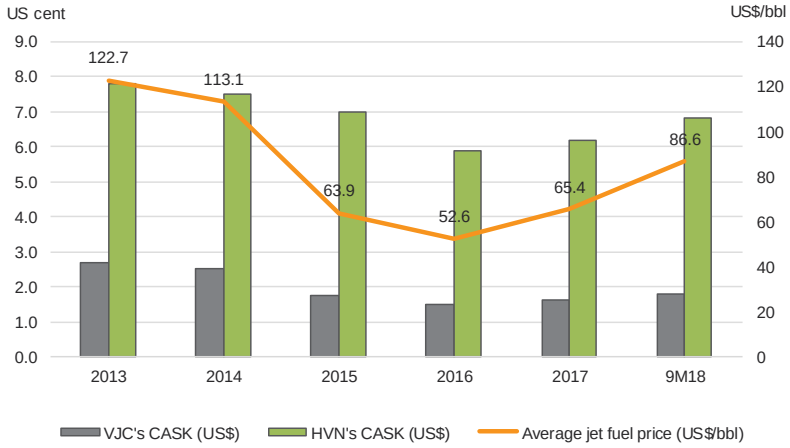
Figure 194: Jet Kerosene prices (US$/bbl) vs. Brent crude price (US$/bbl)

Source: EIA, VNDIRECT

Spot jet fuel prices have, in tandem with crude oil, climbed sharply since late 2017 which hurt the bottomline of airlines. Although oil prices have been reversing in the past few weeks, we believe jet fuel prices have troughed. In the short-term, we see the crude oil market remaining well-supported as OPEC is considering re-imposing supply cuts to counter strong output growth from the US. Brent crude oil prices will probably stay above US$60/bbl during FY19-22, per consensus estimates.

Fuel cost currently accounts for 39-42% of Cost per Available Seat Kilometer (CASK) for Vietnamese carriers. We note that both VJC and HVN do not use any fuel hedging strategies and, therefore, a recovery in jet fuel prices will push the airlines to decide between: a) absorbing the increases at the cost of gross margin contraction; 2) passing on fuel cost increases to customers, thereby risking volume weakness or market share erosion. Given the rising competition, the pass-through of any future recovery in fuel prices is unlikely to be dramatic.

Figure 195: Impact of jet fuel price on CASK by Vietnamese airlines



Source: EIA, Company reports, VNDIRECT

AVIATION SECTOR STOCK PICKS: BET ON MONOPOLY AIRPORT OPERATOR ACV TO RIDE LONG-TERM GROWTH IN VIETNAM'S AVIATION DEMAND

Figure 196: Aviation peer comparison

Company	Bloomberg Ticker	Market cap (in US$bn)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROE (%)	TTM ROA (%)	D/E (curr.)	TTM P/E (x)	TTM P/B (x)	TTM EV/EBITDA (x)
Airlines										
China Southern Airlines	1055 HK	11.7	13.8%	11.1%	10.9%	2.4%	9.4	8.8	0.9	8.6
China Eastern Airlines	670 HK	10.3	12.9%	12.9%	7.7%	1.8%	8.6	13.8	1.0	15.6
Singapore Airlines	SIA SP	8.5	-23.7%	-23.7%	4.8%	2.4%	5.5	17.2	0.8	3.0
Cathay Pacific	293 HK	6.2	N/A	N/A	0.9%	0.3%	9.7	91.6	0.7	5.9
Vietnam Airlines	HVN VN	2.0	-17.0%	-17.0%	12.1%	2.4%	2.4	22.3	2.8	9.7
Thai Airways	THAI TB	0.9	49.9%	49.9%	-8.0%	-0.8%	9.4	16.9	1.0	9.7
Bangkok Airways	BA TB	0.8	N/A	N/A	5.3%	2.7%	15.6	15.6	0.8	9.4
Average-FSCs			*7.2%*	*6.6%*	*4.8%*	*1.6%*	*8.7*	*26.6*	*1.1*	*8.8*
Spring Airlines	601021 CH	4.4	58.7%	43.2%	13.7%	6.4%	N/A	19.3	2.2	5.5
Vietjet Air	VJC VN	2.9	33.2%	9.5%	47.5%	16.3%	0.6	11.6	5.1	10.8
AIRASIA GROUP	AAGB MK	2.5	115.5%	115.6%	30.4%	13.6%	3.0	3.6	1.0	18.7
Westjet Airlines	WJA CH	1.6	-62.7%	-62.0%	4.9%	1.7%	4.7	20.7	0.9	7.1
Air Arabica	AIRARABI UH	1.3	-9.9%	-14.6%	8.3%	4.0%	5.9	9.7	0.7	4.7
Average LCCs			*27.0%*	*18.3%*	*21.0%*	*8.4%*	*3.5*	*13.0*	*2.0*	*9.4*
Average-regional airlines			**17.1%**	**12.5%**	**11.6%**	**4.4%**	**6.8**	**20.9**	**1.5**	**9.1**
Median-regional airlines			**13.3%**	**10.3%**	**8.0%**	**2.4%**	**5.9**	**16.2**	**1.0**	**9.0**
Airports										
Airport of Thailand	AOT TB	31.3	21.1%	21.1%	18.3%	17.0%	0.1	36.7	6.4	22.9
Airports Corporation of Vietnam	ACV VN	8.5	25.3%	25.3%	21.7%	12.1%	0.5	34.2	6.5	19.2
Malaysia Airports Holdings	MAHB HK	3.3	N/A	N/A	8.0%	3.3%	8.4	21.0	1.6	8.4
Average-regional airports			**23.2%**	**23.2%**	**16.0%**	**10.8%**	**3.0**	**30.6**	**4.8**	**16.8**

Source: Bloomberg, VNDIRECT

Airports Corporation of Vietnam (ACV VN, ADD, TP:VND105,000): In our view, regional airlines are a risky bet, given the deep cyclicality inherent in the airline industry, the industry's exposure to rising and volatile oil prices, and the flood of LCC capacity in the pipeline in Asia. **The potential end of a duopolistic airline market in Vietnam with the potential entry of Air Asia and Bamboo Airlines also means that competition among airlines in Vietnam is likely to intensify with risks of a possible price war in the near future.**

We therefore believe that ACV is a far safer and higher-quality long-term bet on the secular growth in Vietnam's aviation industry. We like ACV for the following four reasons:

- Airport operations carry national security and national development implications and, hence, are highly unlikely to ever be liberalised to the same extent as the airline sector. In most countries you do not see quite the same plethora of airport operators (private or public) that you come across in the airline industry.
- In the same vein, ACV is, and will likely remain, a monopoly airport operator for several years to come, in our view. While the government might privatise select airports in the future, it will still want the majority of airport assets in the country to be under the control of the state. Even though the government is relatively cash-strapped and needs to urgently upgrade the currently strained airport infrastructure in the country, it will seek to do this through project-level participation from private strategic partners, which we

think means that no private airport operator will really be able to challenge ACV on a nation-wide level.

- We prefer ACV to airlines as it is less exposed to fuel price volatility. Meanwhile, ACV is rising a phased hike in passenger handling fees and there is room for sustained appreciation as domestic handling fees still remain low in a regional context.
- Finally, we believe that ACV has only just "scratched the surface" in terms of monetising its duty free retailing potential and non-aeronautical revenue contribution remains very low relative to regional peers like Airports Authority of Thailand (AOT). As more duty free concessions are handed out and overall retailing space improves across Vietnamese airports, ACV will see a surge in its non-aeronautical revenue streams.

AIRPORTS CORPORATION OF VIETNAM (ACV)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND89,300	VND105,000	1.12%	ADD	AVIATION

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

Hien Tran Khanh

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ACV is a robust long-term bet on the aviation growth story than even a basket of domestic airline stocks. ACV will benefit from rising passenger throughput, passenger fee hikes and an expansion in non-aeronautical revenue streams.

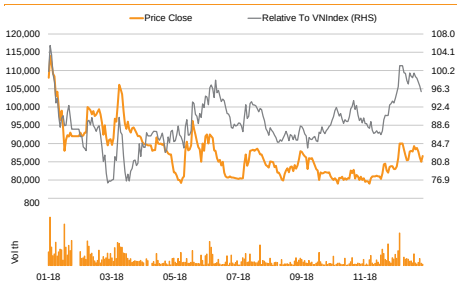
We forecast revenue growth of 12.4% in FY19F driven by 12.1% passenger traffic growth and recent passenger fee hikes which will be fully reflected in 2019 performance. Meanwhile, non-aeronautical revenue is expected to grow by 5.6% yoy. We did not take into account the possibility of a resumption of booking of landing charge revenue which is being negotiated between ACV and MOT. This revenue is related to flight operation assets (runways, taxiways).

MOT's divestment of ACV stake to be a significant catalyst. The Ministry of Transport (MOT) plans to divest 30% of its current ownership of 95% in ACV by end-2020F. We expect the divestment to bolster ACV's free float and boost the share price. ACV has also announced that it will pursue a HOSE listing, possibly in 2019F. However, firstly, ACV must reach a consensus with the MOT on the accounting treatment of flight operation assets adhered to above.

High return on capital and superior growth prospects justify valuation premium. ACV currently trades at a TTM EV/EBITDA of 19.2x, higher than the TTM regional peer average of 16.8x. However, we believe the stock deserves to trade at a significant premium to regional peers because: 1) the company's FY18-19F ROAE of 20.7-21.4% is much higher than the regional peer average of 16.0%; 2) ACV is a monopoly airport operator in Vietnam and the risk of new entrants is limited, in our opinion despite partial privatization; and 3) Vietnam's aviation market is the fastest growing in Asia.

Maintain Add rating with a TP of VND105,000. (DCF TP, ERP: 11.0%; LTG:5.0%). Our TP translates to a FY19F EV/EBITDA of 16.2x. Downside risks include a sudden change in aviation policy, particularly with regards to privatization, and further VND depreciation against the JPY which would lead to forex losses on debt revaluation.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	114,000
52w low (VND)	79,000
3m Avg daily volume (shares)	118,800
3m Avg daily value (VNDmn)	5,291
Market cap (VNDbn)	194,406
Outstanding shares (m)	2,177
Free float (%)	5
TTM P/E (x)	34.2
Current P/B (x)	6.5

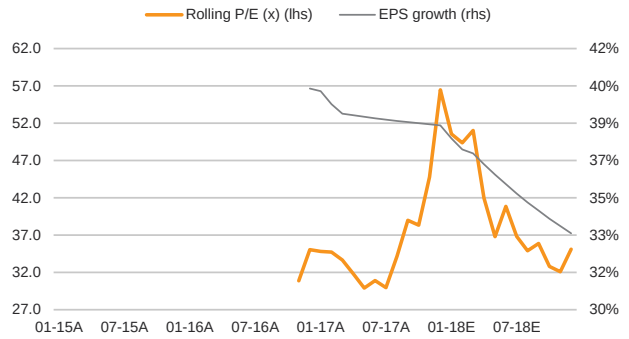
Ownership

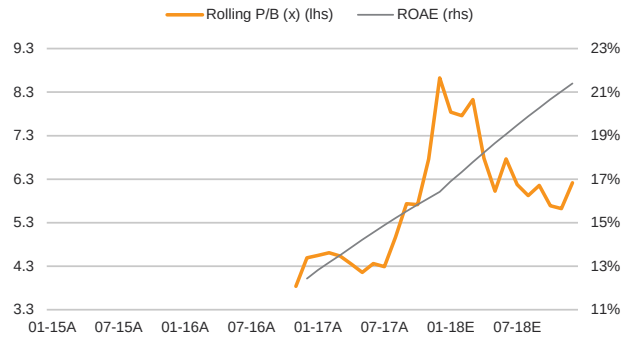
Ministry of Transport	95.0%
Others	5.0%

Source: VNDIRECT

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	10,691	13,849	16,774	18,857
Revenue growth	(18.8%)	29.5%	21.1%	12.4%
Gross margin	38.0%	41.1%	48.4%	47.8%
EBITDA margin	57.7%	69.7%	73.6%	74.7%
Net profit (bn)	2,696	4,182	6,304	7,048
Net profit growth	59.4%	55.1%	50.7%	11.8%
Recurring profit growth	66.0%	44.3%	50.2%	11.7%
Basic EPS	1,238	1,921	2,896	3,237
Adjusted EPS	1,238	1,921	2,896	3,237
BVPS	10,821	12,580	14,480	16,723
ROAE	12.4%	16.4%	21.4%	20.7%

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	13,849	16,774	18,857
Cost of sales	(8,157)	(8,649)	(9,838)
Gen & admin expenses	(824)	(986)	(1,034)
Selling expenses	(295)	(357)	(377)
Operating profit	**4,574**	**6,782**	**7,609**
Operating EBITDA	8,736	11,097	12,746
Depreciation and amortisation	**(4,162)**	**(4,315)**	**(5,138)**
Operating EBIT	**4,574**	**6,782**	**7,609**
Interest income	1,219	1,531	1,560
Financial expense	(701)	(726)	(654)
Net other income	61	0	0
Income from associates & JVs	249	343	350
Pre-tax profit	**5,402**	**7,930**	**8,864**
Tax expense	(1,198)	(1,594)	(1,781)
Minority interest	(21)	(32)	(36)
Net profit	**4,182**	**6,304**	**7,048**
Adj. net profit to ordinary	4,182	6,304	7,048
Ordinary dividends	(1,306)	(2,177)	(2,177)
Retained earnings	**2,876**	**4,127**	**4,871**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	914	3,596	4,037
Short term investments	17,963	19,963	19,963
Accounts receivables	7,300	7,261	7,888
Inventories	402	654	744
Other current assets	88	502	564
Total current assets	**26,667**	**31,976**	**33,196**
Fixed assets	19,618	17,802	20,902
Total investments	2,691	2,691	2,691
Other long-term assets	186	225	253
Total assets	**49,161**	**52,694**	**57,043**
Short-term debt	148	119	95
Accounts payable	1,136	1,321	1,474
Other current liabilities	6,031	5,664	6,397
Total current liabilities	**7,315**	**7,104**	**7,965**
Total long-term debt	14,328	13,895	12,462
Other liabilities	84	101	114
Share capital	21,772	21,772	21,772
Retained earnings reserve	5,602	9,740	14,622
Shareholders' equity	**27,388**	**31,526**	**36,408**
Minority interest	47	68	93
Total liabilities & equity	**49,161**	**52,694**	**57,043**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**5,402**	**7,930**	**8,864**
Depreciation & amortisation	4,162	4,315	5,138
Tax paid	(1,726)	(1,594)	(1,781)
Other adjustments	(836)	(1,874)	(1,910)
Change in working capital	**(1,432)**	**(808)**	**107**
Cash flow from operations	**5,570**	**7,969**	**10,418**
Capex	(2,578)	(2,500)	(8,238)
Proceeds from assets sales	17	0	0
Others	475	(39)	(28)
Other non-current assets changes	(4,315)	(126)	1,910
Cash flow from investing activities	**(6,402)**	**(2,665)**	**(6,356)**
New share issuance	249	(462)	(1,456)
Shares buyback	0	0	0
Net borrowings			
Other financing cash flow	(652)	18	13
Dividends paid	(1,306)	(2,177)	(2,177)
Cash flow from financing activities	**(1,709)**	**(2,622)**	**(3,621)**
Cash and equivalents at beginning of period	3,166	914	3,596
Total cash generated	**(2,541)**	**2,682**	**441**
Cash and equivalents at the end of period	625	3,596	4,037

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	30.2%	37.6%	37.4%
Asset turnover	0.29	0.33	0.34
ROAA	8.7%	12.4%	12.8%
Avg assets/avg equity	1.89	1.73	1.62
ROAE	16.4%	21.4%	20.7%
Efficiency			
Days account receivable	53.9	56.1	60.2
Days inventory	18.0	27.6	27.6
Days creditor	50.8	55.7	54.7
Fixed asset turnover	0.65	0.90	0.97
ROIC	10.0%	13.8%	14.4%
Liquidity			
Current ratio	3.65	4.50	4.17
Quick ratio	3.59	4.41	4.07
Cash ratio	2.58	3.32	3.01
Cash cycle	21.1	28.0	33.2
Growth rate (yoy)			
Revenue growth	29.5%	21.1%	12.4%
Operating profit growth	73.4%	48.3%	12.2%
Net profit growth	55.1%	50.7%	11.8%
EPS growth	55.1%	50.7%	11.8%
Share value			
Basic EPS (VND)	1,921	2,896	3,237
BVPS (VND)	12,580	14,480	16,723

Source: VNDIRECT

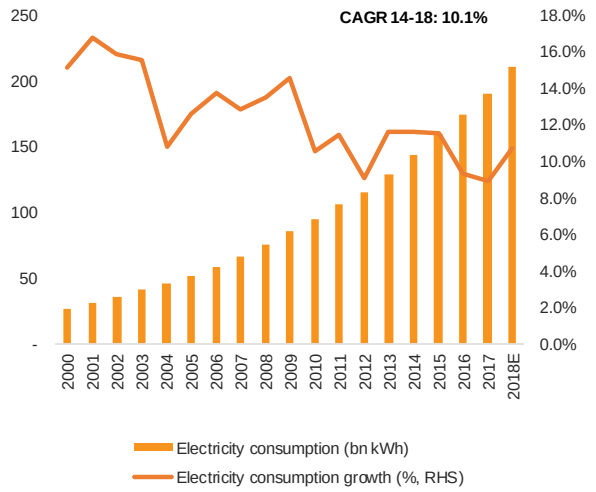
POWER: GROWTH WITH DEFENSIVE ATTRIBUTES

2018 Review: The sun rises on Vietnam's power sector

Accelerating growth in electricity demand with muted capacity growth

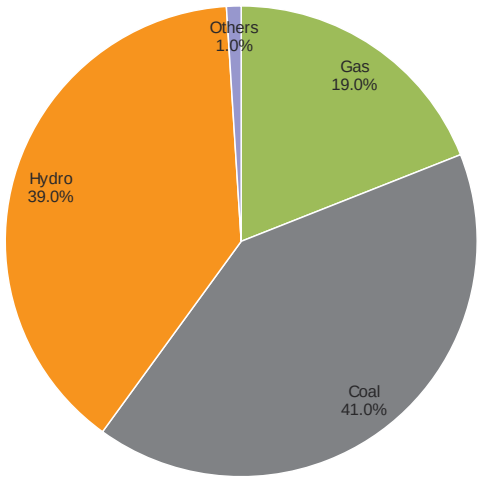
Vietnam's power sector continued to enjoy strong growth in consumption in 2018 (~10.7% vs. 9.0% in 2017). In 2018, we estimate that Vietnam's power capacity only grew by 6.0% to 48.7GW, which was much lower than demand growth. Despite a huge planned capacity expansion, many power plant projects are at risk of delay due to capital constraints and policy changes. However, we see an interesting shift towards investments in renewable power, especially solar power in 2018.

Figure 197: Electricity consumption grew at an average of 10.1% during 2014-18E



Source: VNDIRECT, GSO

Figure 198: Vietnam's electricity consumption by source (2018)



Source: VNDIRECT, EVN

An increasing focus on solar power

Technological advances have reduced the development cost for solar power significantly. In Vietnam, the investment cost per kW for solar power has fallen to US$1.0-1.2m/MW compared to US$3.0-4.0m/MW in the past (before 2013). With the introduction of Feed-in-Tariffs (FiT) for solar power plants in 2017, many investors have ramped up their development plans because at the FiT of 9.35 cents/kWh and unit capex cost of US$1.0-1.2m/MW, solar power producers can enjoy healthy returns, especially compared to wind power producers.

Many new solar power plant projects were licensed in 2018. As of Sep 2018, more than 120 projects have been added to the revised Power Development Plan VII (revised PDP VII). Installed capacity for solar power is expected to increase to 6.1GW by 2020 and 7.2GW by 2030 vs. the earlier plan of 850MW by 2020 and 4.0GW by 2030 in the initial national PDP VII. Boosted by expectations of an extension of the FiT scheme to 2020, the registered capacity of current solar power (~26GW , equivalent to 53.4% of total installed capacity) is tracking far ahead of the government's plan, according to the Ministry of Industry and Trade.

Electricity price hikes were delayed to keep the lid on inflation

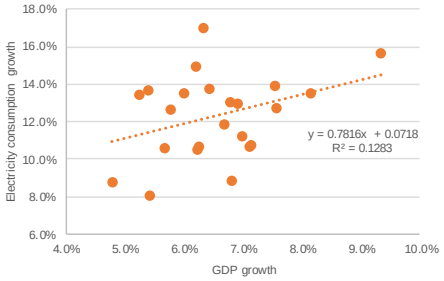
In 2018, the government delayed increasing electricity prices as rising food and fuel prices were stoking inflation concerns. Meanwhile, Vietnam Electricity's (EVN) financial position has also continued to

deteriorate due to rising production costs and controlled retail prices. As we expect inflation risks to remain muted in 2019, there is a high possibility that retail electricity prices will be hiked this year.

2019 Outlook: We see some tailwinds for existing power generators

Investment is lagging demand growth but should pick-up

Figure 199: Annual electricity demand vs. GDP growth

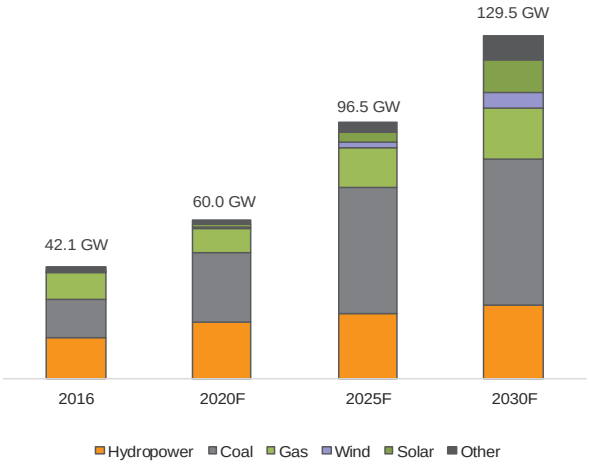


Source: VNDIRECT, GSO

Given strong growth in the manufacturing sector and improved standards of living, we expect electricity demand to grow by 10.0% in 2019. According to the revised PDP VII, to keep pace with demand, investments in new generation capacity and transmission infrastructure in the power sector will need to increase substantially for the period 2016-20F. At the end of 2018, Vietnam's national installed generation capacity was estimated at ~48.7GW, which is tracking well below the government's target of 60.0GW by 2020 (according to the revised PDP VII).

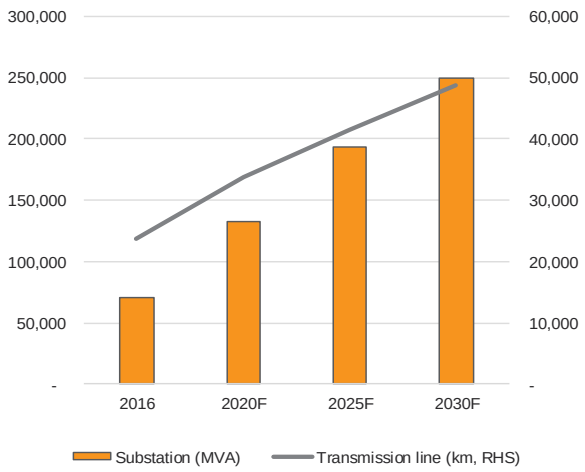
We expect a gradually strengthening project pipeline in the next two years with major power plant projects including: Upper Kon Tum (220 MW, 3Q2019); Vinh Tan 4 expansion (600 MW, end-2019) and Thai Binh 2 (1,200 MW, 2020). At the end of 2018, EVN National Power Transmission (EVN NPT) initiated construction works of the third national 500kV transmission line (over 740 km at an investment cost of nearly US$516m). The construction completion time is estimated at around 20 months and this transmission line is scheduled to be operational by mid-2020.

Figure 200: Vietnam's installed power capacity by source (2016-30F)



Source: VNDIRECT, Revised PDP VII

Figure 201: Vietnam's transmission lines and substation infrastructure (2016-30F)



Source: VNDIRECT, Revised PDP VII

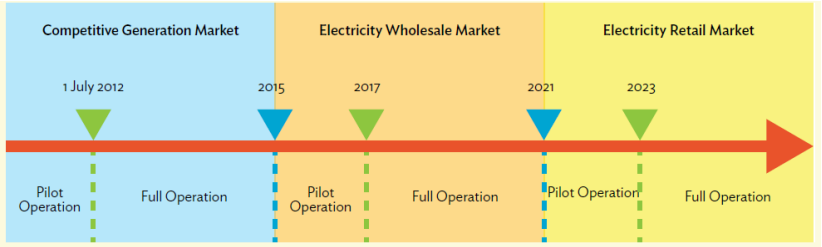
Tightening supply-demand balance should support wholesale power prices and boost volumes for select generators

Based on the current project pipeline, we think the government will likely to miss the target for power capacity and transmission infrastructure by 2020. Lagging investment amid strong demand could create power shortages, implying higher sales volume mobilized for generators with spare capacity and higher electricity selling prices in the Competitive Generation Market (CGM), in our view.

The official launch of the Wholesale Electricity Market (WEM) will be a leap forward in the power reform agenda but it will take time

Currently, generators that collectively account for around 47.2% of the national system's total installed capacity (~23.0GW) participate in the Competitive Generation Market. However, only 15-20% of each of these generator's sales volume is transacted at spot market prices and the rest is sold through standard power purchase agreements (PPA) negotiated between the generator and EVN. Although the competitive generation market is still in its infancy, we believe there has been a marked improvement in transparency and competitiveness in Vietnam's power industry.

Figure 202: Planned timeline for the Vietnam competitive power market



Source: VNDIRECT, ADB

Following on from the development of the CGM, the WEM officially commenced operations at the beginning of this year. Under the WEM, the single buyer model will be dissolved, and power generators can sell electricity directly to Electric Power Trading Company (EPTC – EVN's unit) and another five state-owned power distributors. In addition, big customers (industrial parks/large industrial plants) are allowed to buy directly from power plants. In an ideal scenario, as the power generators are free to sell electricity to different buyers that will need to compete with each other, a more competitive wholesale market could evolve and help to gradually raise the bargaining power of power generators. However, EVN will remain the main buyer in the near-term as we see other power distributors having limited ability to negotiate electricity prices with power generators.

We believe that the continued transition to a market-based pricing mechanism will benefit, not harm thermal generators

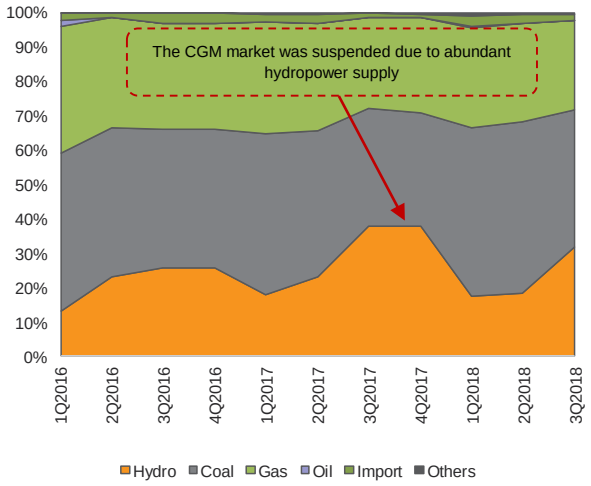
Figure 203: Unit cost of electricity production by source (cents/kWh)

Source: VNDIRECT

Under the CGM mechanism, hydropower plants can offer far more competitive prices compared to other thermal power plants owing to their production cost advantages. However, we believe that the WEM mechanism will not lead to market share losses for thermal power generators. The main reasons include the following:

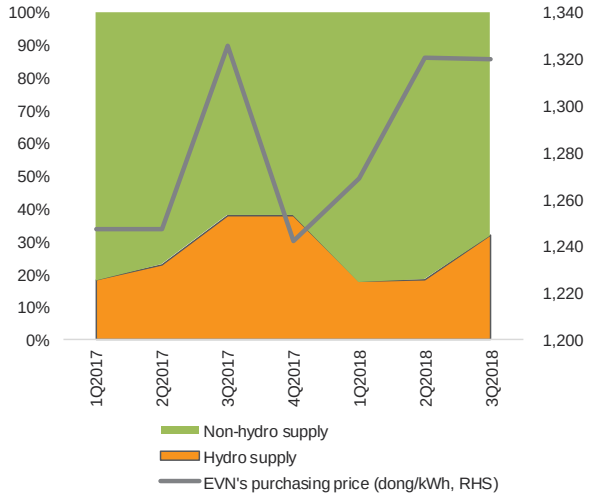
- New capacity addition in thermal power will be much higher than hydro power, which has limited ability to expand with most of Vietnam's hydropower potential having already been exploited. In 2018, only 22.6% of CGM sales by volume came from hydro power sources versus 33.0% in 2017, according to EVN;
- Despite competitive production costs vs. thermal power plants, hydro players have to deal with unpredictable weather conditions. An El Nino event, which will likely happen in 2019-20, could weigh on hydro power output;
- In 4Q2017, the CGM was suspended for one month to raise purchasing volumes from gas-fired power plants. This move impacted hydropower plants negatively and raised concerns about the true extent of liberalisation of the power market. Indeed, we believe it will take many more years for Vietnam's power industry to be fully liberalised.

Figure 204: CGM electricity procurement by source (1Q16-3Q18)



Source: VNDIRECT, MoIT

Figure 205: EVN's purchasing price and market share of hydro generators vs. other power generators in the CGM market



Source: VNDIRECT, MoIT

Note: Market price in 4Q2017 fell sharply due to the suspension of the CGM market.

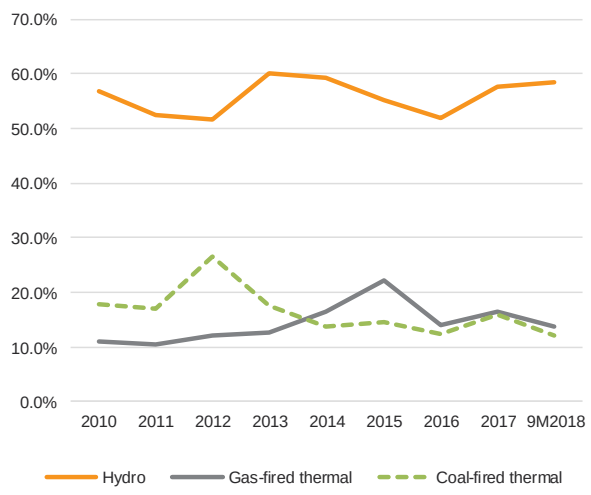
With the possibility of power shortages (especially in the South) due to the delayed commencement of many thermal power plants, existing power generators could operate at full capacity in order to meet rising demand spurred by a rapidly growing manufacturing base and rapid urbanisation in the South of Vietnam. At the same time, the competitive market will continue to open up to thermal power plants in 2019. To be specific, the percentage of volume that can be sold on the competitive market will be raised from 15% of total volume in 2018 to 20% for thermal power plants in 2019 while this cap will be maintained at 20% for hydro power plants. This could lead to a potential higher CGM prices increase for efficient thermal power plants in 2019.

We expect favourable input costs in 2019 for thermal producers

In 2018, rising input costs put considerable pressure on thermal power companies' gross margins while hydropower companies benefitted from abundant rainfall and enhanced competitiveness versus thermal producers. However, the recent slump in prices of both oil and thermal coal might lead to a gradual decrease in input costs for thermal power plants. In addition, new regulations in the shipping sector require the shipping industry to consume better quality fuel with lower sulphur levels which could weigh on FO prices, creating more favourable input costs for gas-fired power plants.

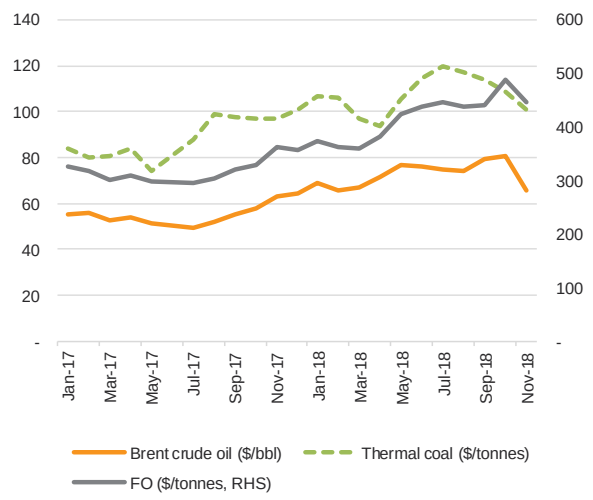
Factoring in favourable input costs and a rise in average blended wholesale power prices thanks to the CGM mechanism – and accommodated by retail electricity price hikes – we expect the gross margins of listed thermal power companies to improve slightly in 2019.

Figure 206: Gross margins of listed power plants by type



Source: VNDIRECT, FIINPRO

Figure 207: Input cost of thermal power plants



Source: VNDIRECT, BLOOMBERG

POWER SECTOR STOCK PICKS: WE LIKE PC1 AND PLACE POW ON OUR WATCH LIST AS THESE COMPANIES STAND TO BENEFIT FROM CONTINUED DEMAND AND CAPACITY GROWTH AND HAVE LIMITED COMMODITY PRICE EXPOSURE.

Companies operating in the power industry have relatively recession-proof earnings as they provide essential services for which demand is remarkably steady. We like Power Construction JSC No.1 **(PC1 VN, ADD, TP: VND28,400)** as this company stands to benefit from investment in the third 500kV national transmission line and growth private sector participation in Vietnam's power sector which is helping to alleviate public funding constraints for the massive infrastructure build-out needed to support demand growth. The development pipeline of renewable energy is also creating new opportunities for PC1 as it wins more contracts to build solar power installations.

Among generators, we place PVPower (**POW VN, Not rated)** on our watch list because its diversified portfolio of power plants across the country provides a natural hedge against changes in relative competitiveness of key input commodities like gas, coal and fuel oil. POW accounts for nearly 9.0% of total nationwide installed capacity. In addition, the GCM mechanism could benefit POW with solid volume growth and higher CGM prices due to the anticipated electricity shortage in the south where most of POW's power plants are currently located. Finally, as we mentioned above, we expect POW's gross margins to recover in 2019 thanks to expected softness in thermal power feedstock prices.

Figure 208: PC1 peer comparison

Name	Ticker	Market cap	TTM NP growth	TTM EPS growth	TTM ROA	TTM ROE	D/E (curr.)	TTM P/E	TTM P/B
		(US$m)	(% yoy)	(% yoy)	(%)	(%)	(x)	(x)	(x)
Specialty Construction									
Power Engineering Consulting 2	TV2	69.9	68.9	72.9	15.2	51.8	(1.3)	6.2	2.6
Construction No.5	SC5	17.8	(33.8)	(33.8)	2.1	11.8	0.4	10.5	1.2
Song Da No.11	SJE	16.5	102.4	92.9	5.4	21.5	1.4	3.1	0.8
Power Engineering Consulting 3	TV3	14.0	66.5	96.0	8.9	22.6	(0.7)	21.3	3.5
Vietnam Electricity Construction	VNE	13.2	4.5	12.9	6.1	10.7	0.0	3.1	0.3
Power Engineering Consulting 4	TV4	11.7	0.9	(6.8)	9.5	13.8	(0.3)	10.7	1.6
Average		*23.9*	*34.9*	*39.0*	*7.9*	*22.0*	*(0.1)*	*9.2*	*1.7*
Median		*15.3*	*35.5*	*42.9*	*7.5*	*17.7*	*(0.1)*	*8.3*	*1.4*
Small Hydropower									
Southern Hydropower	SHP	89.7	1.8	(3.8)	7.9	13.9	0.7	10.8	1.8
Vietnam Power Development	VPD	68.7	189.7	210.5	6.1	14.0	-	9.4	1.2
Can Don Hydropower	SJD	61.7	(0.7)	(0.7)	13.3	18.7	0.1	7.2	1.5
Mien Trung Power Investment & Development	SEB	43.6	(20.8)	(21.3)	15.0	33.0	0.7	7.9	2.7
Srok Phu Mieng IDICO Hydropower	ISH	32.2	274.1	321.3	8.4	13.6	0.4	8.4	1.4
Gia Lai Hydropower	GHC	27.5	66.0	66.0	29.5	34.3	(0.4)	5.9	1.7
Nam Mu Hydropower	HJS	22.3	(0.8)	(0.9)	11.7	19.0	0.0	11.3	1.8
Hydropower - Power No.3	DRL	20.0	(18.1)	(17.3)	36.0	36.7	(0.6)	9.0	4.1
PC3 - Investment	PIC	18.1	(29.2)	(29.3)	5.0	8.4	0.5	11.8	1.2
Dak Doa Hydropower	HPD	6.4	148.2	148.2	8.1	16.4	0.9	8.2	1.3
Average		*39.0*	*61.0*	*67.3*	*14.1*	*20.8*	*0.2*	*9.0*	*1.9*
Median		*29.8*	*0.6*	*(0.8)*	*10.0*	*17.6*	*0.3*	*8.7*	*1.6*
Power Construction No.1	**PC1**	**128.8**	**110.1**	**108.3**	**7.6**	**18.1**	**0.5**	**6.4**	**1.0**

Source: VNDIRECT, BLOOMBERG
Data as of Jan 11 2019

Figure 209: POW peer comparison

Name	Ticker	Market cap	TTM NP growth	TTM EPS growth	TTM ROA	TTM ROE	D/E (curr.)	TTM P/E	TTM P/B
		(US$m)	(% yoy)	(% yoy)	(%)	(%)	(x)	(x)	(x)
Global Power Synergy Pcl	GPSC TB	2,638.8	25.9	22.7	5.9	9.3	0.5	23.4	2.1
Ratchaburi Elec Gen Hodg Pub	RATCH TB	2,349.5	(36.5)	(36.5)	5.3	8.7	0.5	14.1	1.3
Guangzhou Development Grp-A	600098 CH	2,318.0	42.5	42.5	1.9	4.5	0.9	21.5	1.0
B Grimm Power Pcl	BGRIM TB	2,305.9	54.0	3.1	2.6	17.3	3.1	29.4	3.9
Banpu Power Pcl	BPP TB	2,111.2	0.4	(22.5)	9.2	10.9	0.1	16.2	1.7
Inner Mongolia Mengdian Hu-A	600863 CH	2,052.5	162.0	162.0	1.4	5.2	2.1	25.0	1.3
Huadian Fuxin Energy Corp -H	816 HK	1,909.0	4.7	4.7	2.1	11.1	3.5	6.2	0.6
United Power Generation And	UPGO BD	1,863.2	(25.5)	(26.1)	29.7	30.5	-	37.4	10.4
Torrent Power Ltd	TPW IN	1,757.9	118.2	118.2	4.3	12.9	1.2	13.1	1.6
JSW Energy Ltd	JSW IN	1,633.3	(90.9)	(91.0)	0.3	0.7	1.0	145.9	1.0
PetroVietnam Power Corp	POW VN	1,575.3	107.9	107.9	3.4	9.1	1.0	15.2	1.4
Jointo Energy Investment C-A	000600 CH	1,510.1	351.7	348.6	0.7	2.0	1.2	47.7	0.9
NLC India Ltd	NLC IN	1,457.4	(41.0)	(35.3)	5.4	15.3	0.9	5.1	0.8
First Gen Corporation	FGEN PM	1,430.4	48.9	58.7	3.4	9.1	1.4	9.0	0.8
CESC Ltd	CESC IN	1,284.7	56.9	56.9	2.6	9.6	1.7	10.9	1.1
Reliance Power Ltd	RPWR IN	1,173.9	(6.6)	(6.6)	1.6	4.7	1.2	8.0	0.4
Reliance Infrastructure Ltd	RELI IN	1,149.9	9.5	9.5	1.3	5.6	0.9	5.8	0.3
Malakoff Corp Bhd	MLK MK	966.9	(34.7)	(34.2)	0.8	3.5	2.4	17.3	0.6
Cikarang Listrindo Tbk Pt	POWR IJ	971.0	20.7	20.7	6.8	13.9	0.8	11.0	1.5
Hub Power Company	HUBC PA	740.0	(4.2)	(4.1)	6.9	36.1	1.7	10.1	4.8
North Bangkok Power Plant BI	EGATIF TB	737.9	(12.5)	(2.2)	9.4	9.4	-	11.8	1.1
First Philippine Hldgs	FPH PM	733.1	55.4	103.0	2.2	8.9	1.7	4.8	0.4
Jiangxi Ganneng Co-A	000899 CH	672.3	40.7	33.7	0.6	0.9	0.5	108.9	1.0
Top Energy Co Ltd Shanxi-A	600780 CH	579.8	813.7	675.7	1.9	4.7	0.8	16.8	0.8
Summit Power Ltd	SUMITPOW BD	567.6	16.9	17.1	8.1	14.2	0.4	9.5	1.2
Average		*1,459.6*	*67.1*	*61.1*	*4.7*	*10.3*	*1.2*	*25.0*	*1.7*
Median		*1,457.4*	*20.7*	*17.1*	*2.6*	*9.1*	*1.0*	*14.1*	*1.1*

Source: VNDIRECT, BLOOMBERG | Data as of Jan 11 2019, POW's data as of Jan 14 2019 after moving to HOSE exchange

POWER CONSTRUCTION JSC NO.1 (PC1)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND22,800	VND28,400	0.0%	ADD	INDUSTRIALS

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

My Tran Ha
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We believe PC1 is a beneficiary of current tailwinds in Vietnam's power industry. We expect the grid erection and steel pole segments to recover in 2019F. However, earnings are likely to fall before recovering in 2020F due to a significant drop in profit booking from the real estate segment.

Robust backlog in 2019F. According to the company, the total backlog of the grid erection and installation segment is estimated at VND2,829bn at the beginning of 2019, which is much higher than that of last year (VND1,300bn). The backlog in the steel pole production segment also reached a high of VND1,093bn at the beginning of 2019 (vs. VND139bn in early-2018) thanks to contract wins from the third 500kV national transmission line project. Given this order book strength, we estimate a 28.0% increase in revenue of these segments, contributing 57.5% of total revenue in 2019F vs. 44.5% in 2018E.

We expect margin contraction in 2019F. In 2018, the margins of the grid erection and steel pole production segments declined due to higher input costs and rising competition in bidding activities. Because of continued fierce competition expected in these segments and smaller contribution from the real estate segment in 2019F, we expect PC1's blended gross margin to shrink by 2.6% pts to touch 14.9%.

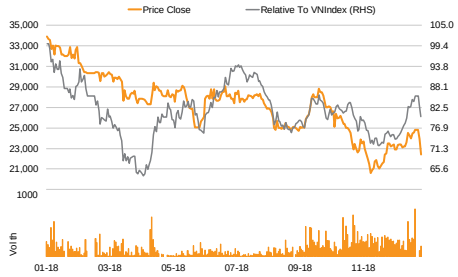
Promising outlook for hydropower segment. Investments in hydropower have gradually helped improved PC1's earnings quality thanks to high margins and recurring, stable revenues. The company is operating four hydropower plants with total installed capacity of 114MW, contributing to 11.1% of total revenue in 2018. Currently, PC1 targets to build another five plants in order to raise its capacity to 300MW by 2022. This long-term strategy, would require PC1 to raise capital to fund capital expenditures in the next 1-2 years but could help the company build a buffer against the volatility inherent in its core contracting business.

Earnings likely to bottom in 2019; maintain Add. We project a net profit of VND390bn in 2019F (-22.0% yoy), mainly due to lower net profit contribution from the real estate segment. However, we believe PC1's earnings could recover in 2020-21F thanks to 1) the launch of new real estate projects; 2) a series of new hydropower plants coming on stream; and 3) a potential rise in M&E contracting volume due to the need to upgrade the national grid erection system.

Key risks to our view: 1) Slower-than-expected launch of new real estate projects; 2) Continued delays in the Vietnam power industry's investments; 3) Higher competition in the grid erection and installation segment which could pressure contract pricing and, consequently, GMs.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	3,008	3,161	5,168	5,119
Revenue growth	(3.0%)	5.1%	63.5%	(0.9%)
Gross margin	17.5%	15.2%	17.5%	14.9%
EBITDA margin	15.2%	16.3%	17.2%	16.3%
Net profit (bn)	305	237	499	390
Net profit growth	24.1%	(22.3%)	111.0%	(22.0%)
Recurring profit growth	24.1%	(22.3%)	111.0%	(22.0%)
Basic EPS	2,294	1,782	3,759	2,933
Adjusted EPS	2,124	1,643	3,496	2,728
BVPS	26,003	23,238	23,216	25,588
ROAE	18.7%	10.2%	17.3%	12.0%

Price performance



Source: VNDIRECT

Key statistics

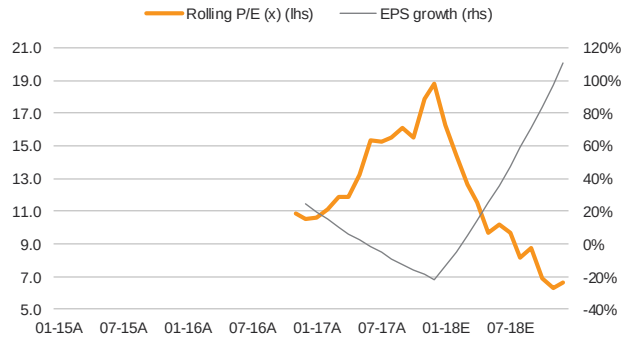
52w high (VND)	33,914
52w low (VND)	20,600
3m Avg daily volume (shares)	231,299
3m Avg daily value (VND mn)	5,284
Market cap (VNDbn)	3,027
Outstanding shares (m)	142
Free float (%)	71
TTM P/E (x)	6.4
Current P/B (x)	1.0

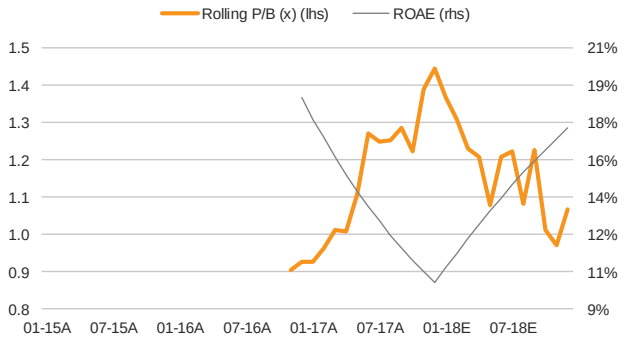
Ownership

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

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	3,161	5,168	5,119
Cost of sales	(2,679)	(4,265)	(4,357)
Gen & admin expenses	(126)	(150)	(154)
Selling expenses	0	(67)	(10)
Operating profit	**355**	**686**	**598**
Operating EBITDA	470	829	785
Depreciation and amortisation	**(115)**	**(143)**	**(186)**
Operating EBIT	**355**	**686**	**598**
Interest income	11	16	6
Financial expense	(103)	(121)	(169)
Net other income	40	40	40
Income from associates & JVs	1	1	1
Pre-tax profit	**303**	**622**	**477**
Tax expense	(47)	(99)	(62)
Minority interest	(20)	(23)	(25)
Net profit	**237**	**499**	**390**
Adj. net profit to ordinary	237	499	390
Ordinary dividends			
Retained earnings	**237**	**499**	**390**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**303**	**622**	**477**
Depreciation & amortisation	115	143	186
Tax paid	(63)	(99)	(62)
Other adjustments	(74)	(77)	(77)
Change in working capital	**(240)**	**(392)**	**(353)**
Cash flow from operations	**41**	**197**	**171**
Capex	(821)	(468)	(1,068)
Proceeds from assets sales	2	0	0
Others	(77)	(7)	0
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(896)**	**(474)**	**(1,068)**
New share issuance	519	0	0
Shares buyback	(0)	0	0
Net borrowings	705	205	799
Other financing cash flow	0	(68)	13
Dividends paid	0	0	0
Cash flow from financing activities	**1,224**	**137**	**812**
Cash and equivalents at beginning of period	419	567	644
Total cash generated	**369**	**(141)**	**(84)**
Cash and equivalents at the end of period	788	426	560

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	567	644	584
Short term investments	100	50	50
Accounts receivables	1,302	1,670	1,599
Inventories	1,085	701	1,134
Other current assets	38	40	42
Total current assets	**3,092**	**3,105**	**3,409**
Fixed assets	2,816	3,077	3,965
Total investments	91	98	98
Other long-term assets	213	307	271
Total assets	**6,212**	**6,587**	**7,742**
Short-term debt	294	691	994
Accounts payable	794	584	597
Other current liabilities	745	528	505
Total current liabilities	**1,833**	**1,803**	**2,095**
Total long-term debt	1,527	1,507	2,055
Other liabilities	40	40	40
Share capital	1,155	1,328	1,328
Retained earnings reserve	716	932	1,236
Shareholders' equity	**2,684**	**3,084**	**3,399**
Minority interest	128	153	153
Total liabilities & equity	**6,212**	**6,587**	**7,742**

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	7.5%	9.7%	7.6%
Asset turnover	0.59	0.81	0.71
ROAA	4.4%	7.8%	5.4%
Avg assets/avg equity	2.31	2.22	2.21
ROAE	10.2%	17.3%	12.0%
Efficiency			
Days account receivable	101	86	81
Days inventory	148	60	95
Days creditor	108	50	50
Fixed asset turnover	1.28	1.75	1.45
ROIC	5.1%	9.2%	5.9%
Liquidity			
Current ratio	1.69	1.72	1.63
Quick ratio	1.09	1.33	1.09
Cash ratio	0.36	0.39	0.30
Cash cycle	141	96	126
Growth rate (yoy)			
Revenue growth	5.1%	63.5%	(0.9%)
Operating profit growth	(10.6%)	93.2%	(12.8%)
Net profit growth	(22.3%)	111.0%	(22.0%)
EPS growth	(22.3%)	111.0%	(22.0%)
Share value			
Basic EPS (VND)	1,782	3,759	2,933
BVPS (VND)	23,238	23,216	25,588

Source: VNDIRECT

PVPOWER CORP (POW)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND15,600	N/A	N/A	NOT RATED	UTILITIES

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
My Tran Ha
my.tranha@vndirect.com.vn

In our view, POW stands to benefit from the development of the Vietnam power industry thanks to 1) its diversified portfolio of power plants (4.2 GW); 2) the gradual liberalisation of the Vietnam power market; 3) sizable long-term capacity addition through the new thermal power plants Nhon Trach 3 & 4.

Potential power shortage could lead to higher sales volume. PV Power is the second largest power generator in Vietnam, holding 11% of national capacity with most of its power plants operating in the south. With the high possibility of power shortages in this region in 2019, we expect POW to achieve higher sales volume compared to the previous year.

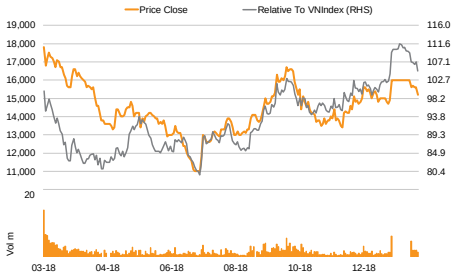
POW will benefit from the gradual liberalisation of the Vietnam electricity market. In our view, the commencement of WEM in 2019 could lead to a higher market selling price given the power shortage situation in Vietnam. The proportion of volume that can be sold on the competitive market will be raised to 20% in 2019 (from 15% in 2018). Therefore, POW could improve its margins by selling more power in the competitive market rather than through Power Purchasing Agreements (PPAs).

Lower depreciation expenses could help earnings to surge in 2019. According to the company, both Ca Mau 1 & 2 plants have fully depreciated their assets in 2018, while Nhon Trach 1 plant will be fully depreciated in 3Q2019. This could help to lower depreciation expenses by about VND700bn while the PPA prices are unchanged, leading to a surge in gross margins in 2019.

Nhon Trach 3 & 4 will be a long-term catalysts for POW. These power plants could boost the company's capacity by another 1.5 GW (c. 35%) once they come on stream (expected to happen in 2022-23). In our view, POW needs to put in a lot of work into the design and planning of these plants. The company also needs to cooperate with other PVN companies to build facilities to guarantee stable feedstock supply for new power plant operations.

The company was listed on the HOSE on Jan 14, 2019. Management expects that after six months of listing on the main bourse, POW will satisfy conditions for inclusion in the VN30 Index. The inclusion into the VN30 could be a strong re-rating catalyst.

Price performance



Key statistics

52w high (VND)	17,800
52w low (VND)	11,000
3m Avg daily volume (shares)	1,342,180
3m Avg daily value (VNDmn)	20,035
Market cap (VNDbn)	7,485
Outstanding shares (m)	2,342
Free float (%)	3.6
TTM P/E (x)	15.2
Current P/B (x)	1.4

Ownership

PVN	79.9%
Others	20.1%

Source: VNDIRECT

Financial summary (VND)	12-15A	12-16A	12-17A
Net revenue (bn)	23,230	28,212	29,710
Revenue growth	(4.6%)	21.4%	5.3%
Gross margin	22.5%	13.4%	16.6%
EBITDA margin	29.0%	26.0%	28.2%
Net profit (bn)	2,216	1,060	2,211
Net profit growth		(52.2%)	108.5%
Recurring profit growth		(52.2%)	108.5%
Basic EPS	885	423	883
Adjusted EPS	885	423	883
BVPS	10,852	11,048	11,436
ROAE		4.4%	9.0%

Source: VNDIRECT

Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	23,230	28,212	29,710
Cost of sales	(18,002)	(24,429)	(24,787)
Gen & admin expenses	(991)	(739)	(815)
Selling expenses	(17)	(17)	0
Operating profit	**4,220**	**3,027**	**4,107**
Operating EBITDA	7,045	7,343	8,423
Depreciation and amortisation	**(2,825)**	**(4,316)**	**(4,316)**
Operating EBIT	**4,220**	**3,027**	**4,107**
Interest income	523	459	414
Financial expense	(1,699)	(1,798)	(1,806)
Net other income	6	(6)	(4)
Income from associates & JVs	0	0	0
Pre-tax profit	**3,050**	**1,681**	**2,711**
Tax expense	(443)	(178)	(132)
Minority interest	(391)	(443)	(368)
Net profit	**2,216**	**1,060**	**2,211**
Adj. net profit to ordinary	2,216	1,060	2,211
Ordinary dividends			
Retained earnings	**2,216**	**1,060**	**2,211**

Balance sheet

(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	6,073	4,671	2,266
Short term investments	150	60	1,039
Accounts receivables	5,848	10,230	6,744
Inventories	3,701	3,347	3,533
Other current assets	244	211	196
Total current assets	**16,016**	**18,519**	**13,778**
Fixed assets	51,680	48,350	44,282
Total investments	781	931	957
Other long-term assets	2,806	1,933	1,567
Total assets	**71,283**	**69,732**	**60,583**
Short-term debt	6,651	5,888	6,099
Accounts payable	4,797	6,169	5,041
Other current liabilities	5,594	6,021	2,729
Total current liabilities	**17,043**	**18,078**	**13,868**
Total long-term debt	27,074	24,669	18,779
Other liabilities	840	189	213
Share capital	21,774	21,774	21,774
Retained earnings reserve	1,348	1,015	1,282
Shareholders' equity	**23,629**	**24,055**	**24,902**
Minority interest	2,697	2,741	2,822
Total liabilities & equity	**71,283**	**69,732**	**60,583**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**3,050**	**1,681**	**2,711**
Depreciation & amortisation	2,825	4,316	4,316
Tax paid	(416)	(242)	(190)
Other adjustments	(167)	384	(485)
Change in working capital	**(250)**	**(2,392)**	**(239)**
Cash flow from operations	**5,042**	**3,749**	**6,113**
Capex	(372)	(1,673)	(308)
Proceeds from assets sales	15	0	1
Others	4,762	298	(752)
Other non-current assets changes	0	(0)	0
Cash flow from investing activities	**4,405**	**(1,375)**	**(1,060)**
New share issuance	0	0	31
Shares buyback	0	0	0
Net borrowings	10,324	(3,168)	(5,680)
Other financing cash flow	(17,532)	(179)	(247)
Dividends paid	(1,683)	(430)	(1,563)
Cash flow from financing activities	**(8,892)**	**(3,776)**	**(7,458)**
Cash and equivalents at beginning of period	5,518	6,073	4,671
Total cash generated	**555**	**(1,402)**	**(2,405)**
Cash and equivalents at the end of period	6,073	4,671	2,266

Key ratios

	12-15A	12-16A	12-17A
Dupont			
Net profit margin	9.5%	3.8%	7.4%
Asset turnover		0.40	0.46
ROAA		1.5%	3.4%
Avg assets/avg equity		2.96	2.66
ROAE		4.4%	9.0%
Efficiency			
Days account receivable	71	127	80
Days inventory	75.0	50.1	52.0
Days creditor	97.3	92.4	74.2
Fixed asset turnover		0.56	0.64
ROIC	3.7%	1.8%	4.2%
Liquidity			
Current ratio	0.94	1.02	0.99
Quick ratio	0.72	0.84	0.74
Cash ratio	0.37	0.26	0.24
Cash cycle	48.3	85.2	57.7
Growth rate (yoy)			
Revenue growth	(4.6%)	21.4%	5.3%
Operating profit growth		(28.3%)	35.7%
Net profit growth		(52.2%)	108.5%
EPS growth		(52.2%)	108.5%
Share value			
Basic EPS (VND)	885	423	883
BVPS (VND)	10,852	11,048	11,436

Source: VNDIRECT

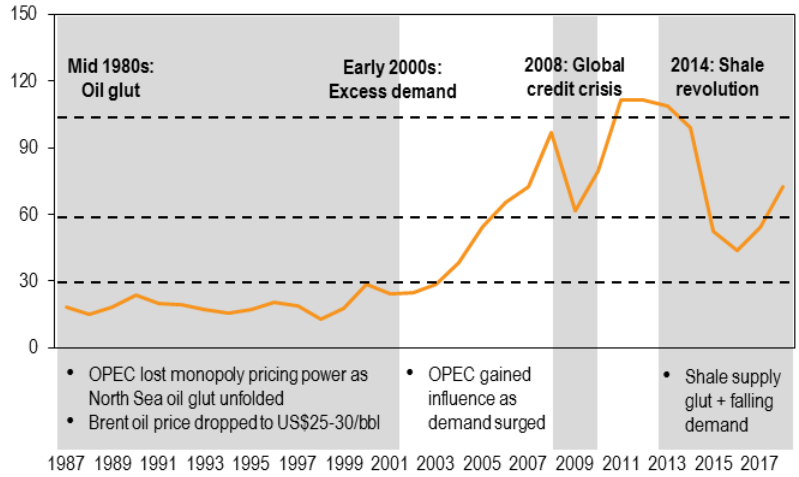
OIL AND GAS: TIME FOR SOME BOTTOM FISHING?

Crude oil could climb out of bear territory

We believe oil prices have come full circle since a historic collapse in 4Q14, driven by the supply glut from shale oil. However, the oil market has been re-balanced since 2016 thanks to stalled supply growth and stronger demand from Asia Pacific. Accordingly, the average Brent crude oil price touched US$54.1/bbl in 2017 (+24.0% yoy) and US$71.2/bbl in 208 (+31.5% yoy).

Crude oil prices crashed in late 2014 as OPEC, in a bid to kill off competition from US shale oil, decided to flood the market with cheap oil. However, this strategy failed and OPEC had to agree on a supply cut to re-balance the market by the end of 2016. Crude oil prices have gradually recovered since then.

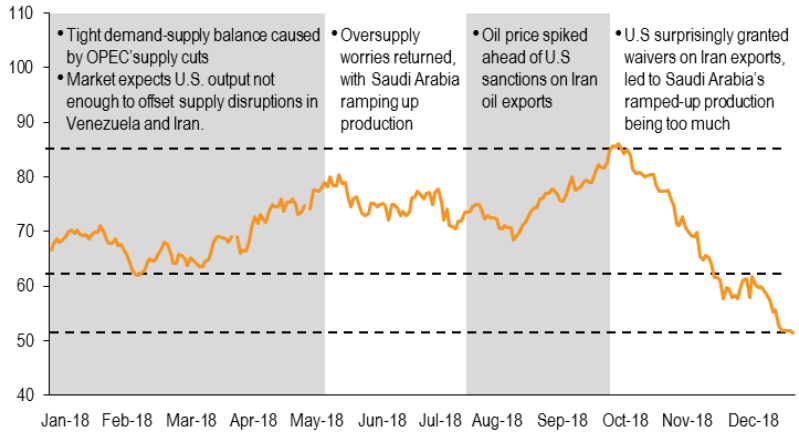
Figure 1: Brent oil price history (US$/bbl)



Source: VNDIRECT RESEARCH, IEA

While the correction in 4Q18 raised concerns about crude oil price falling back into bear territory, we believe that sentiment is running ahead of fundamentals due to a combination of broad equity market sell-off and growing fears of a global economic slowdown as well as due to Saudi Arabia's reduced geopolitical leverage to effect cuts, following the murder of Saudi journalist Jamal Khashoggi.

Figure 2: Movements of Brent crude oil price in 2018 (US$/bbl)



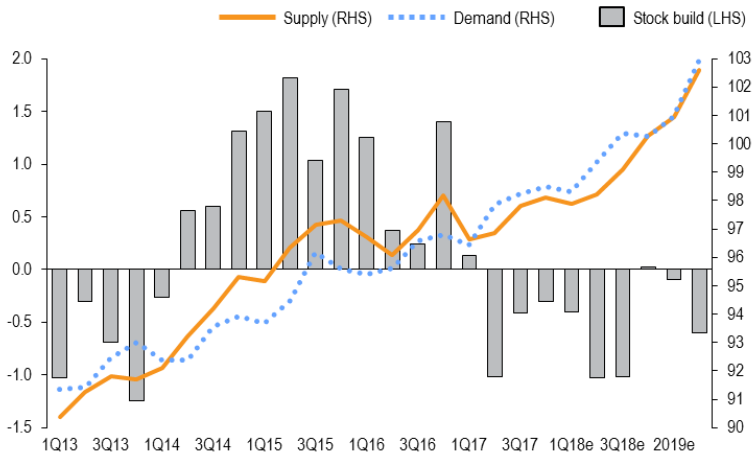
Source: VNDIRECT RESEARCH, IEA

Fundamentally, the global crude oil market is still expected to remain well balanced in 2019, once the production cuts from Organization of the Petroleum Exporting Countries (OPEC) take effect and prevent inventories from building further. Barring a severe economic slump, global oil demand will grow at roughly the pace seen in recent years,

powered by emerging economies which, aside from China, continue to be in good health.

We project the crude oil market to be well-supported in 2019, with global stock declines as demand outstrips supply. Since 2017, six consecutive quarters of stock building have helped to clear stock oversupply and re-balanced the global oil market.

Figure 3: Crude oil demand – supply balance (mbd)

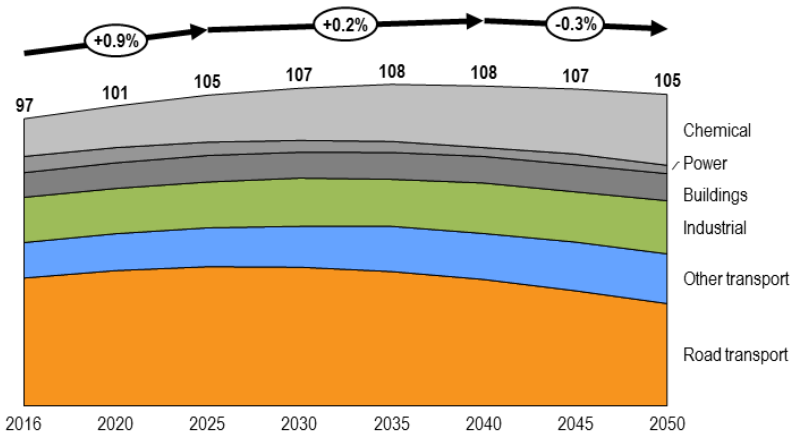


Source: VNDIRECT RESEARCH, IEA

In the long term, while future oil demand growth is expected to peak by 2030 by which point other energy sources have become more cost-competitive (renewables and electric vehicles) and socially acceptable (nuclear), we still see a certain long-term need for oil due to its competitive pricing and widespread popularity. We note that crude oil is used not just for transportation and, in fact, the fastest-growing driver for oil consumption is chemicals. A rising middle class globally means the need for petrochemicals will also increase as they are the base constituents of many basic products from paint to personal care items, growth in demand for which tends to track overall consumption growth; also there are no obvious substitutes for these petrochemicals in their application areas. As such, we see long term growth in demand for petrochemicals by manufacturers which should support oil demand.

In the long term, it is expected that petrochemical production will replace transportation as the main demand driver for crude oil. A rising middle class globally means the need for petrochemicals will also increase as they are the base constituents of many products from paint to personal care items.

Figure 4: Global oil demand (mbd)

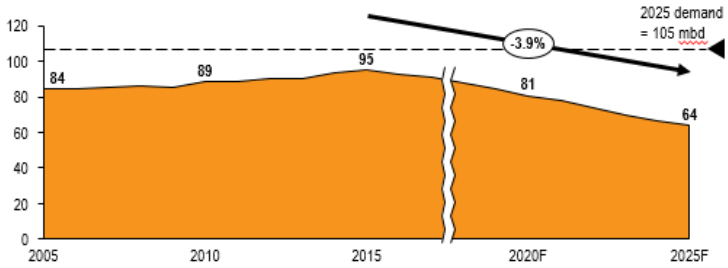


Source: VNDIRECT RESEARCH, IEA

Compounding this issue, significant cutbacks in exploration spending have reduced global oil discoveries to just c.7 btoe. in 2017, the lowest amount since 1940s and down sharply from an average of c.15 btoe per year discovered in the 2004-2014 period. Given the rapid depletion of existing oil fields, if exploration activities remain as sluggish as in 2017, the world is likely to face a supply shortage of c.35 mbd by 2040.

Natural output decline in maturing existing production fields suggests a supply gap of c.35 mbd by 2025 if exploration activities remain at 2017 levels.

Figure 4: Global oil supply if oil discoveries remain at 2017-2018 levels, in mbd.

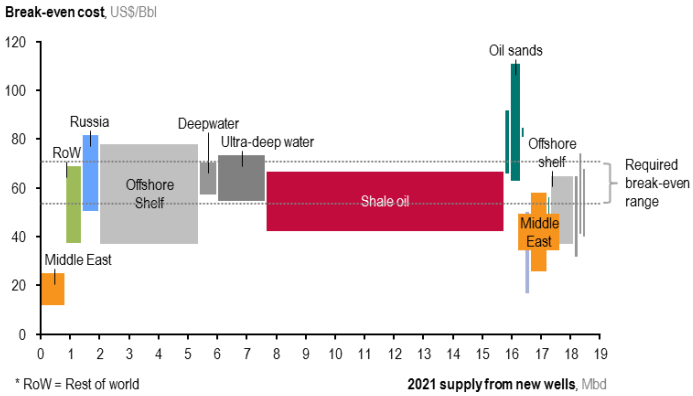


Source: VNDIRECT RESEARCH, RYSTAD ENERGY

In the near future up till 2021, we see that extraction economics will demand that crude oil trades in a range from US$60-US$70/bbl with an approximately 50% increase in extraction costs from 2015 levels as the current shallow-water oil fields get depleted and extraction moves to deeper-water oil fields with higher complexity and development cost.

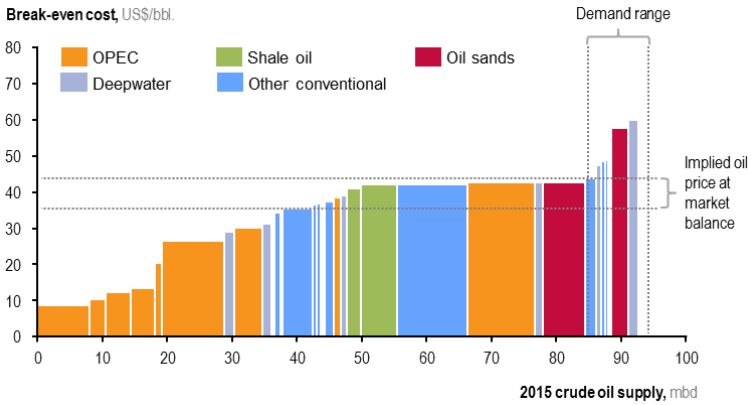
Changing extraction economics demands that crude oil prices range from US$60-US$70/bbl over the medium-term. According to Rystad Energy, only c.3 mbd out of 18.5 mbd of new production expected to come on stream by 2020 is profitable at prices below US$40/bbl.

Figure 5: Break-even cost of global new crude oil supply till 2021



Source: VNDIRECT RESEARCH, RYSTAD ENERGY

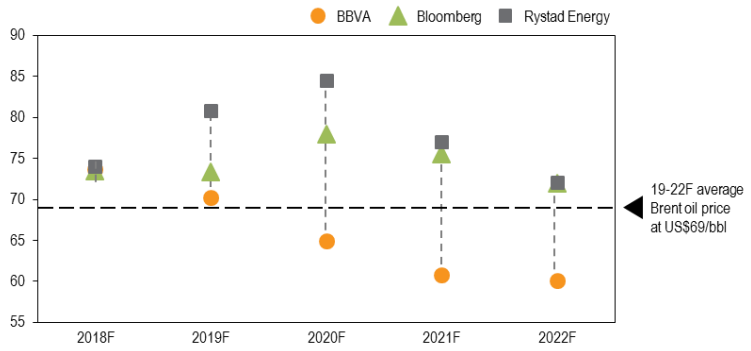
Figure 6: Break-even cost of global crude oil supply in 2015.



Source: VNDIRECT RESEARCH, RYSTAD ENERGY

In our view, and based on the above data, Brent crude oil price will stay above US$60/bbl during FY19-22F.

Figure 7: Brent crude oil price forecast, US$/bbl.

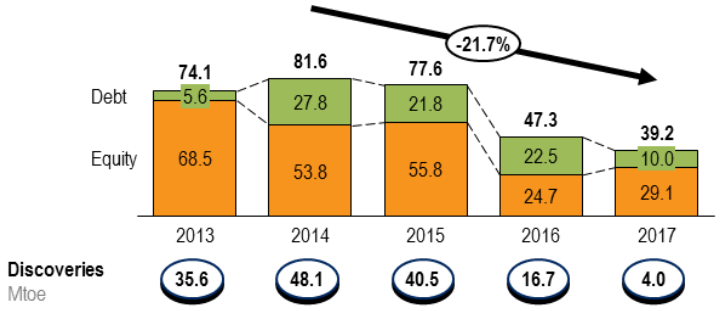


Source: VNDIRECT RESEARCH, RYSTAD ENERGY

Vietnam's energy security is under threat in the medium term

Vietnam's oil and gas production has been declining at an annual rate of c.8% during recent years. This steep drop in production was has roughly tracked the decline in PetroVietnam's capital expenditure for exploration activities since 2015, due to depressed crude oil prices. This lack of exploration has led to insufficient new discoveries, with annual reserve growth falling to 4 million tons of oil equivalent (mtoe) in 2017, the lowest level in history.

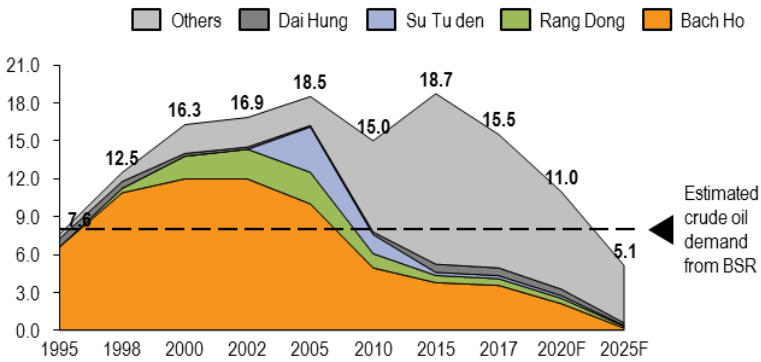
Figure 8: PetroVietnam's capital expenditure (VNDtr)



Source: VNDIRECT RESEARCH, PETROVIETNAM

Meanwhile, the majority of existing oilfields in Vietnam are already in their final stages of production, with production outputs declining by 15%-30% per year. If there are no new discoveries, the domestic supply of crude oil will not be enough to satisfy the feedstock demand from Binh Son refinery (BSR, Not rated) from 2020 onwards. Note that BSR currently relies entirely on domestic crude as feedstock.

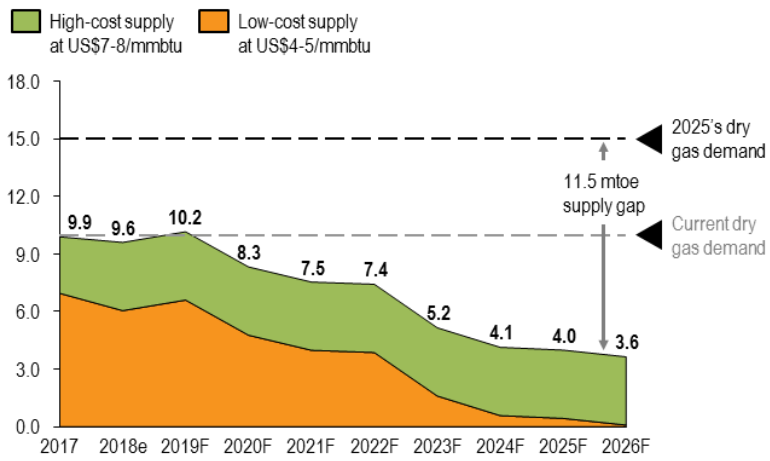
Figure 9: Vietnam's crude oil output assuming no new discoveries (tons million)



Source: VNDIRECT RESEARCH, VIETNAM PETROLEUM INSTITUTE

The depletion of natural gas output is even more worrying as domestic natural gas demand is expected to grow 50% by 2025 when three new gas-fired power plants begin operation.

Figure 10: Vietnam's natural gas output assuming no new discoveries (bcm)

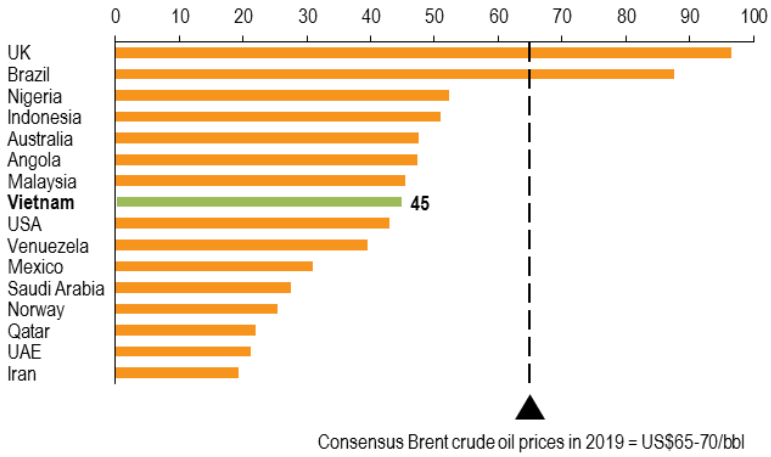


Source: VNDIRECT RESEARCH, PETROVIETNAM

We see a significant increase in exploration already underway

The oil price rally prior the latest bout of weakness had put Vietnam in a good position to step up exploration activities after years of subdued investments. The average oil extraction cost in Vietnam is ~US$45/bbl., below consensus forecasts for Brent crude oil prices of US$65-US$70/bbl in 2019. Given the looming energy security issues alluded to earlier, this might help to boost Vietnam's exploration activities in medium term.

Figure 11: Average crude oil extraction cost (US$/bbl.)



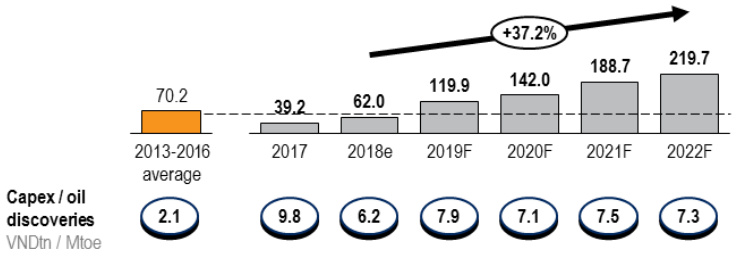
Source: VNDIRECT RESEARCH, RYSTAD ENERGY

According to PVN's business plan until 2020, the targets for annual growth of oil and gas reserves is 20-40 mtoe. This target, which is 2-4 times higher than 2018's estimated reserve growth of 10 mtoe, is highly demanding given the escalated exploration cost of new discoveries. As shelf oil fields run dry, the frontier of exploration will be pushed to more remote areas which require higher levels of equipment, technology, and expensive specialists.

Under intense pressure to increase discoveries and given the higher cost of developing new oil fields, we expect Vietnam to increase capital

expenditure for oil exploration by 50% annually until 2020 in order to replenish current reserves and boost production output.

Figure 12: PetroVietnam's capex forecast (VNDtr).

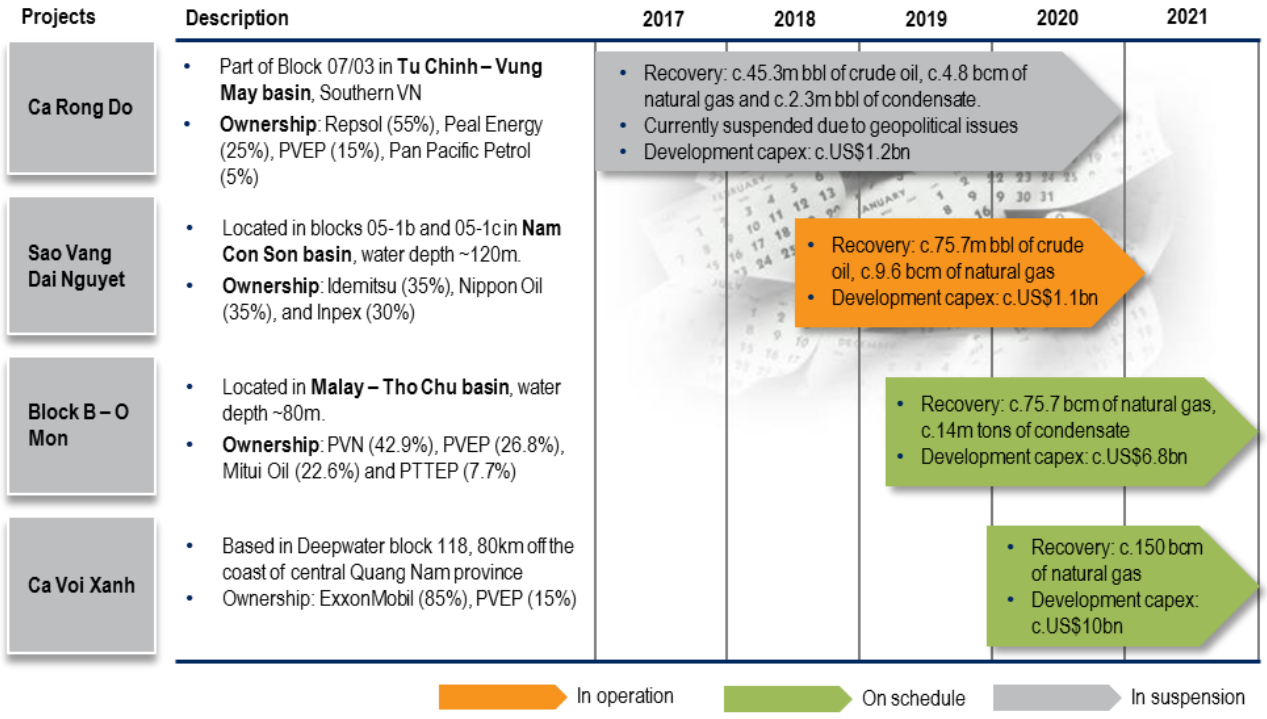


Source: VNDIRECT RESEARCH, PETROVIETNAM

In the medium term, PetroVietnam is planning large oil exploration and drilling projects like Ca Rong Do (Red Emperor), Ca Voi Xanh (Blue Whale) and Block B-O Mon. Those projects are reported to have the largest oil and gas production potential in Vietnam.

Meanwhile, Sao Vang-Dai Nguyet and other gas fields are being developed in parallel with the second phase of Su Tu Trang (White Lion) project to ensure sufficient gas supply for the southeast region once two new gas-fired power plants, namely Nhon Trach 3 and Nhon Trach 4, come into operation in 2021.

Figure 13: Key oil and gas projects in the medium term



Source: VNDIRECT RESEARCH, WOOD MACKENZIE

The key threat that can hinder Vietnam's oil and gas exploration ramp-up is the on-going territorial dispute with China in the East Sea. Some of Vietnam's major oil and gas projects such as Ca Rong Do and Blue Whale, fall within China's "nine-dash line," which serves as the basis for China's controversial claims to most of the resource-rich waterway in the east sea. Such claims by China has been rejected by Vietnam

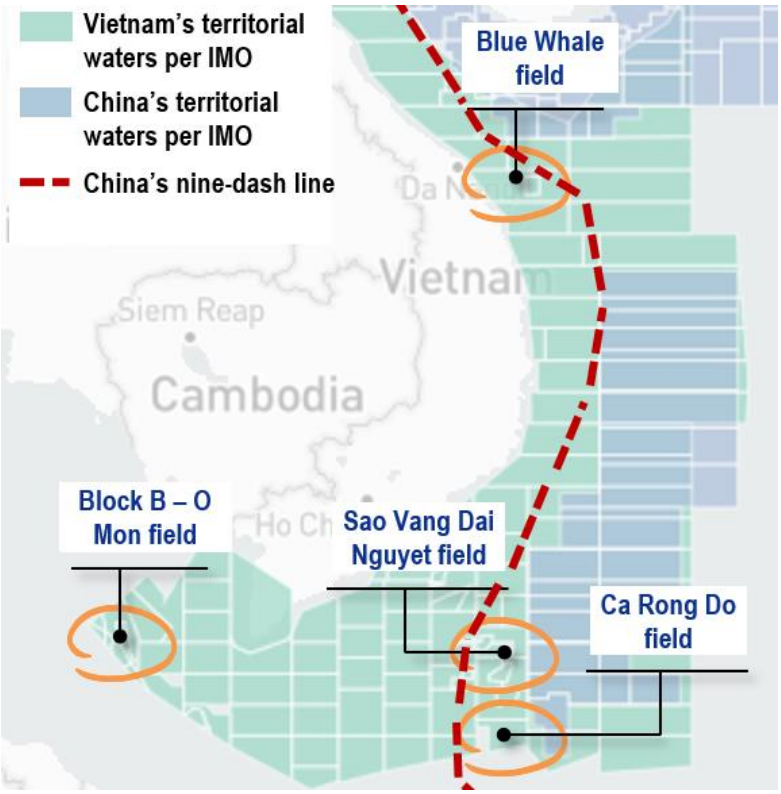
as the nine-dash line extends over large portions of Vietnam's exclusive economic zone.

While China has never used the nine-dash line as an inviolable border to its sovereignty, a certain amount of pressure was still imposed on Vietnam's oil and gas exploration activities in these areas. In March 2018, Ca Rong Do project was suspended indefinitely, supposedly due to pressure from China.

Despite geopolitical tensions with China being a considerable concern, we believe major oil and gas projects in Vietnam will proceed in time to meet rising dry gas demand through domestic sources. While Block B – O Mon project is not within the disputed area, Sao Vang Dai Nguyet project is located well within the long-time developed Nam Con Son basin, and Blue Whale project has the participation of Exxon Mobil – the giant US-based energy developer that thwarted China's protests in striking an exploration deal with Vietnam in 2008. With China clearly on the "back foot" in ongoing trade negotiations with the US, we believe it will be more careful in challenging US companies' interests in the South China Sea.

The key threat that can hinder Vietnam's oil and gas exploration ramp-up is the on-going territorial dispute with China in the east sea. However, we believe major oil and gas projects in Vietnam will proceed in time to meet rising dry gas demand domestically. Block B – O Mon project is not within the disputed area, Sao Vang Dai Nguyet project is located well within the long-time developed Nam Con Son basin, and Blue Whale project has the participation of US company Exxon Mobil.

Figure 15: Location of key oil and gas projects vs. China's nine-dash line



Source: VNDIRECT RESEARCH

OIL AND GAS STOCK PICKS: WE LIKE OILFIELD SERVICES PLAYERS.

Typically, fluctuations in crude oil prices have the most impact on up-to-midstream oil and gas companies. Indeed, we see that the profitability of PetroVietnam Gas Jsc **(GAS VN, Not Rated)** has closely tracked the movements of crude oil prices yoy. In the first 9 months of 2018, average crude oil prices rose by c.45% yoy while GAS posted 9M18 EPS growth of 54.1% yoy. However, the link between oil prices and earnings is more nuanced for oil field service companies owing to

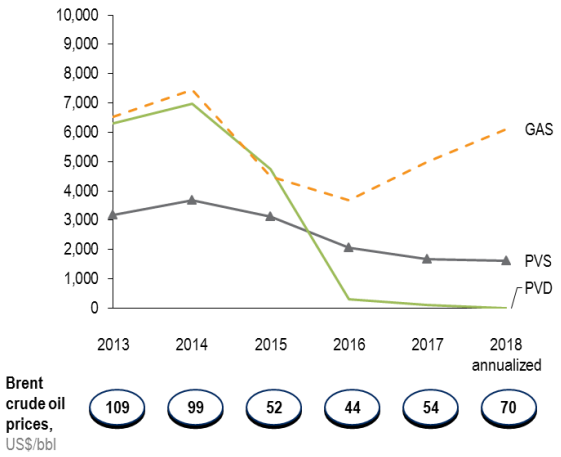
their dependence on E&P activity which tends to track oil prices but with a big time lag.

Both PetroVietnam Technical Services Corp **(PVS, Not Rated)** and PetroVietnam Drilling & Well Services Corp **(PVD, Not Rated)** have seen their EPS sharply decrease during the crude oil price plunge in 2014 which led to sharp falls in E&P activity. While PVS has managed to maintain a decent level of profitability, PVD has become loss-making since the end of 2017 due to the twin impact of falling day rates (oil-linked) as well as rig utilization. As opposed to GAS, the financial performance of PVS and PVD has not picked up in response to the recovery in crude oil prices since 2017. Generally, it often takes 1-2 years before oilfield service companies start benefitting from upward movements of crude oil prices due to the long lead times associated with a resumption of exploration activity.

We believe that the oil price recovery over the course of 2017 and the first half of 2018 has already created some momentum for a resumption of E&P work and that this will materialize soon despite the recent weakness in oil prices which we believe is transitory and driven more by sentiment than by fundamentals.

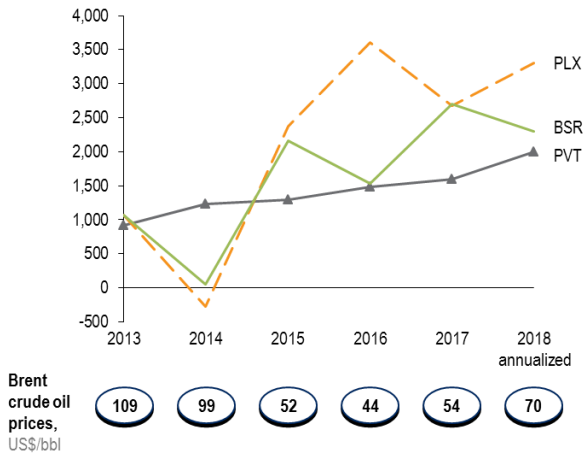
Meanwhile, we see that the profitability of downstream oil and gas companies such as PetroVietnam Transportation Corp. **(PVT VN, ADD, TP: VND21,000)**, Binh Son Refinery **(BSR VN, Not rated),** and Petrolimex **(PLX VN, Not rated),** have only a limited correlation to the movements in crude oil prices.

Figure 14: EPS of key upstream and midstream oil and gas stocks (VND)



Source: BLOOMBERG

Figure 15: EPS of key downstream oil and gas stocks (VND)



Source: BLOOMBERG

We put oilfield service stocks such as PVS (Not rated) and PVD (Not rated) on our watch list, as we believe they will be the first beneficiaries of the expected recovery in Vietnam's oil exploration activities.

We also like PVT due to its dominant market share in the domestic fuel transportation business. We expect the company's transportation volume to grow on the back of higher oil and gas consumption in Vietnam with oil demand growth being largely driven by the new Nghi Son Refinery. Note that LPG demand is expected to grow fast and PVT holds around 90% market share in LPG transportation.

Meanwhile, we see a challenging time ahead for GAS. We expect the on-going depletion of cheap domestic dry gas supply to put upward pressure on GAS's input cost. Meanwhile, GAS's output price is

unlikely to see a dramatic increase in 2019 even though it might rise somewhat on the back of a recovery in oil prices from current levels.

The scaling up of upstream exploration activities has little impact on the profitability of downstream refiners and distributors such as BSR and PLX. We thereby do not include these stocks on our watch-list for 2019.

Figure 16: Summary of our view on major oil and gas stocks

	Impact of our sector investment thesis on major oil and gas stocks	Degree of impact
PVS	• PVS, as an offshore EPC contractor, is the biggest beneficiary of PVN's increasing upstream capital expenditure. PVS will participate in almost all key oil and gas projects in the coming time such as Sao Vang Dai Nguyet, Block B, Su Tu Trang Phase 2, etc.	Very positive
PVD	• As Vietnam needs to scale up oil and gas exploration activities quickly, we see PVD securing more domestic projects in the medium term. Charter rates for offshore drillers are also likely to improve with Brent oil prices still expected to exceed US$60/bbl in the coming years.	Positive
GAS	• The quick depletion of cheap gas supplies will put upward pressure on GAS's input cost. Meanwhile, we see little room for GAS to increase their output prices, due to a flat outlook for crude oil prices in the short-to-medium term.	Negative
BSR	• BSR will need to import crude oil from overseas once there is insufficient domestic supply. However, BSR may be granted a 0% import tax rate for such imports. We hold a neutral view for BSR as the impact of our sector thesis is uncertain.	Neutral
PLX	• PLX is basically a petroleum retailer with regulated selling price and standardised profit. Our sector thesis will not have any significant impact on PLX.	Neutral
PVT	• PVT is the main domestic transporter of oil and gas products. We expect the Company's transportation volume to grow along with higher oil and gas consumption in Vietnam. Crude oil prices above US$55/bbl are also beneficial to PVT's floating storage and offloading (FSO) business.	Positive

Source: VNDIRECT RESEARCH

Figure 17: Oil & Gas peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	A/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
Gas distribution companies									
PTT PLC	PTT TB	45,088	-5.3%	-5.3%	4.7%	7.7%	2.7	5.3	0.4
Toho Gas Ltd	9533 JP	43,500	2.7%	2.7%	2.8%	4.6%	1.7	30.0	1.3
Petronas Gas Bhd	PTG MK	9,217	5.8%	5.8%	10.8%	15.2%	1.4	20.0	3.0
PV GAS	GAS VN	7,920	25.0%	25.0%	15.7%	23.6%	1.5	14.8	4.2
Indraprastha Gas	IGL IN	2,650	2.0%	2.0%	4.7%	2.2%	1.4	25.4	0.6
China Gas Holdings	384 HK	2,271	56.6%	42.0%	8.6%	24.9%	2.9	18.5	3.9
Titas Gas Trans & Distri	TITASGAS BD	432	4.3%	4.3%	3.6%	6.6%	1.9	7.6	0.6
Oil and gas services companies									
Keppel Corp	KEP SP	8,159	56.8%	56.8%	4.7%	10.1%	2.5	10.1	0.9
Hyundai Engineering	000720 KS	4,979	47.8%	47.8%	1.6%	4.6%	2.8	19.3	0.9
Dialog Group	DLG MK	4,164	32.3%	27.2%	8.4%	14.5%	1.8	33.9	4.9
Sembcorp Marine	SMM SP	2,604	N/a	N/a	-2.3%	-8.6%	3.7	N/a	1.3
Yinson Holdings	YNS MK	1,085	-3.5%	-3.5%	4.0%	9.6%	2.5	16.8	1.4
PV Technical Services	PVS VN	424	-0.3%	-10.3%	3.1%	6.7%	2.2	13.6	0.9
PV Drilling	PVD VN	275	N/a	N/a	0.1%	0.2%	1.8	N/a	0.5
Malaysia Marine Eng	MMHE MK	212	-28.0%	-28.0%	0.8%	1.0%	1.3	36.0	0.4
Mermaid Maritime	MMT SP	119	N/a	N/a	-3.1%	-4.2%	1.4	N/a	0.3
Oil and gas transportation companies									
Jinhui Shipping and Trans	JNSTF US	950	0.1%	0.1%	1.6%	2.8%	1.7	13.1	0.3
Eusu Holdings	000700	388	28.3%	28.3%	0.4%	1.0%	2.7	6.2	0.8
PV Trans	PVT VN	204	21.5%	21.5%	5.6%	14.7%	2.6	7.5	1.2
Pakistan National Shipping	PNSC PA	63	-20.6%	-20.6%	5.4%	6.7%	1.3	4.3	0.3
Average - Gas distribution peers					**7.3%**	**12.1%**		**17.4**	**2.0**
Average - Oil and gas services peers					**1.9%**	**3.8%**		**21.6**	**1.3**
Average - Oil and gas transportation peers					**3.0%**	**5.9%**		**7.5**	**0.6**

Source: VNDIRECT RESEARCH, BLOOMBERG

PETROVIETNAM TRANSPORTATION CORP (PVT)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND16,000	VND21,000	6.45%	ADD	OIL & GAS SERVICES

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019

Vu Viet Linh

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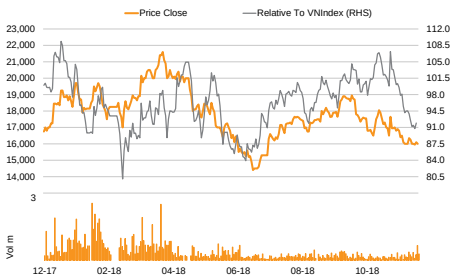
Key changes in the report

- N.A.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	21,600
52w low (VND)	14,400
3m Avg daily volume (shares)	
3m Avg daily value (VNDmn)	3,447
Market cap (VNDbn)	4,531
Outstanding shares (m)	283
Free float (%)	37
TTM P/E (x)	7.5
Current P/B (x)	1.23

Ownership

PetroVietnam Group	51.0%
VietcomBank	2.9%
Yurie Vietnam Securities	5.1%
Others	41.0%

Source: VNDIRECT

A beneficiary of secular oil and gas demand growth in Vietnam with stable cash flow and a robust business model.

PVT boasts a stable business model with assured annual transportation volumes and long-term charter rates. The company is the sole and privileged oil and gas transporter for PetroVietnam Group (PVN), with a virtual monopoly on crude oil and LPG transportation in Vietnam. Meanwhile, due to the nature of long-term charter rates in most transportation operations, PVT is basically unaffected by the fluctuation of crude oil prices. During FY13-17, PVT's sales and EPS posted CAGRs of 5.5% and 20.4% respectively.

We expect PVT to post EPS growth of 21.5% and 11.9% in FY18F and FY19F respectively. The strong projected EPS growth in FY18 will be largely contributed by: (1) higher profitability of the FSO business thanks to crude oil prices returning to above the US$55/bbl threshold level (which triggered an upward revision to charter rates), and (2) low base effect due to the 52-day maintenance of Binh Son Refinery plant (BSR, Not rated) in FY17. In FY19F, we see the full commercial operation of Nghi Son Refinery Plant (NSRP) as the main driver for PVT's revenue and EPS expansion.

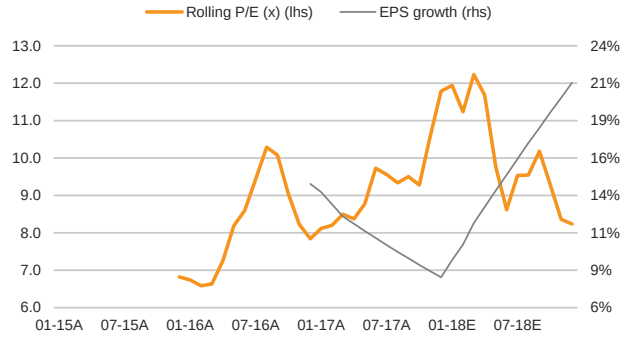
We see the ongoing fleet rejuvenation benefitting PVT's long-term prospects. As at end-FY17, the majority of PVT's transportation fleet was already old and in dire need of replacement. While the expected huge capex of VND3.2tr over FY19-21F will push up PVT's depreciation and interest expenses in the short term, we see significant benefits for PVT in the long term. We believe that a younger transportation fleet will enable PVT to incur less maintenance and fuel expenses, improving its operational efficiency.

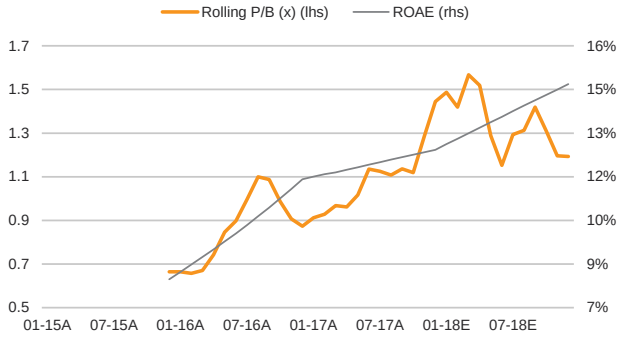
We maintain an ADD recommendation for PVT based on steady EPS growth and attractive valuation. At the current price, PVT is trading at a P/E of 7.4x on our forecasted FY19 EPS, which is much lower than the company's historical 5-year average forward P/E of 9.3x. Our target price is VND21,000, which translates into a target FY19F P/E of 9.7x and equivalent to a 30.4% upside to current price.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	6,785	6,148	7,873	8,807
Revenue growth	18.6%	(9.4%)	28.1%	11.9%
Gross margin	11.2%	13.8%	11.5%	11.6%
EBITDA margin	17.3%	23.5%	21.7%	21.6%
Net profit (bn)	398	450	547	612
Net profit growth	20.2%	13.2%	21.5%	11.9%
Recurring profit growth	20.2%	13.2%	21.5%	11.9%
Basic EPS	1,480	1,599	1,943	2,173
Adjusted EPS	1,480	1,599	1,943	2,173
BVPS	13,287	13,051	13,408	14,474
ROAE	11.4%	12.4%	14.7%	15.6%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	6,148	7,873	8,807
Cost of sales	(5,302)	(6,965)	(7,788)
Gen & admin expenses	(233)	(205)	(229)
Selling expenses	(10)	(12)	(14)
Operating profit	**603**	**692**	**777**
Operating EBITDA	1,228	1,403	1,585
Depreciation and amortisation	**(625)**	**(711)**	**(808)**
Operating EBIT	**603**	**692**	**777**
Interest income	188	173	167
Financial expense	(161)	(206)	(231)
Net other income	13	108	121
Income from associates & JVs	27	35	39
Pre-tax profit	**671**	**801**	**873**
Tax expense	(137)	(164)	(178)
Minority interest	(84)	(91)	(83)
Net profit	**450**	**547**	**612**
Adj. net profit to ordinary	450	547	612
Ordinary dividends	(302)	(446)	(347)
Retained earnings	**148**	**100**	**264**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	2,003	1,991	1,571
Short term investments	918	918	918
Accounts receivables	855	1,000	1,119
Inventories	95	119	133
Other current assets	65	39	44
Total current assets	**3,935**	**4,067**	**3,784**
Fixed assets	4,920	5,940	7,070
Total investments	254	257	261
Other long-term assets	83	83	83
Total assets	**9,192**	**10,348**	**11,199**
Short-term debt	537	688	769
Accounts payable	703	870	973
Other current liabilities	804	1,029	1,151
Total current liabilities	**2,044**	**2,587**	**2,893**
Total long-term debt	2,153	2,757	3,085
Other liabilities	349	349	349
Share capital	2,814	2,814	2,814
Retained earnings reserve	606	706	1,007
Shareholders' equity	**3,673**	**3,773**	**4,074**
Minority interest	972	881	798
Total liabilities & equity	**9,192**	**10,348**	**11,199**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**671**	**801**	**873**
Depreciation & amortisation	625	711	808
Tax paid	(115)	(164)	(178)
Other adjustments	(302)	(501)	(369)
Change in working capital	**113**	**248**	**88**
Cash flow from operations	**991**	**1,096**	**1,222**
Capex	(398)	(1,732)	(1,938)
Proceeds from assets sales	16	87	6
Others	390	128	128
Other non-current assets changes	76		
Cash flow from investing activities	**83**	**(1,517)**	**(1,803)**
New share issuance	100	100	100
Shares buyback	0	0	0
Net borrowings	(461)	(461)	(461)
Other financing cash flow	331	1,217	870
Dividends paid	(302)	(446)	(347)
Cash flow from financing activities	**(333)**	**409**	**161**
Cash and equivalents at beginning of period	1,262	2,003	1,991
Total cash generated	**741**	**(12)**	**(420)**
Cash and equivalents at the end of period	2,003	1,991	1,571

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	7.3%	6.9%	6.9%
Asset turnover	0.67	0.81	0.82
ROAA	4.9%	5.6%	5.7%
Avg assets/avg equity	2.52	2.62	2.75
ROAE	12.4%	14.7%	15.6%
Efficiency			
Days account receivable	50.8	46.4	46.4
Days inventory	6.53	6.23	6.23
Days creditor	48.4	45.6	45.6
Fixed asset turnover	1.23	1.45	1.35
ROIC	6.1%	6.7%	7.0%
Liquidity			
Current ratio	1.93	1.57	1.31
Quick ratio	1.88	1.53	1.26
Cash ratio	1.43	1.12	0.86
Cash cycle	8.86	7.01	6.99
Growth rate (yoy)			
Revenue growth	(9.4%)	28.1%	11.9%
Operating profit growth	14.3%	14.6%	12.3%
Net profit growth	13.2%	21.5%	11.9%
EPS growth	8.1%	21.5%	11.9%
Share value			
Basic EPS (VND)	1,599	1,943	2,173
BVPS (VND)	13,051	13,408	14,474

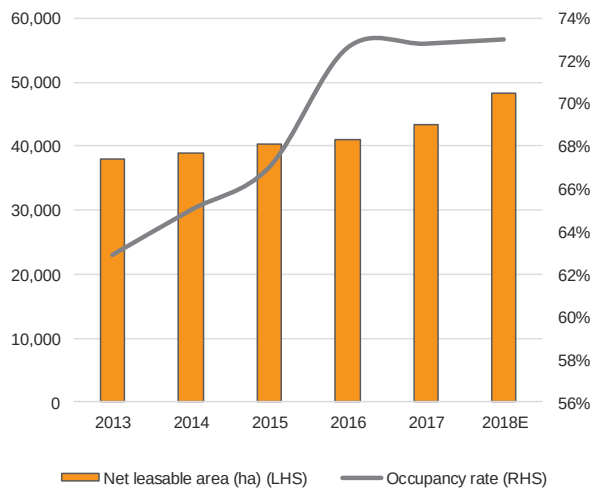
Source: VNDIRECT

INDUSTRIAL PROPERTY: SNOWBALLING MOMENTUM

2018: A year of healthy momentum

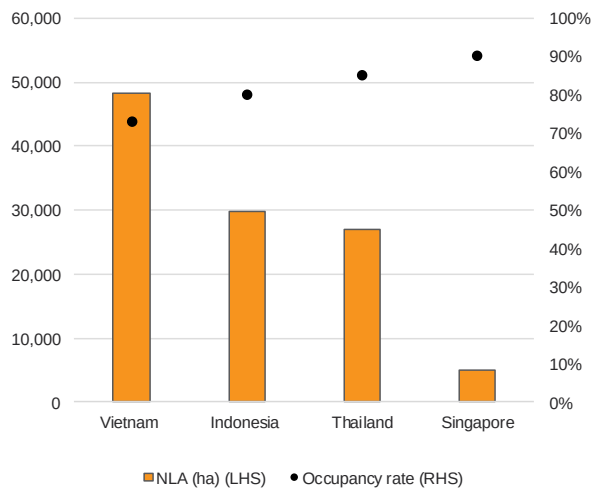
Over the past 20 years, Vietnam has established itself as one of the brightest manufacturing hotspots in Southeast Asia. According to the Ministry of Planning and Investment (MPI), around 48,200ha of Net Leasable Area (NLA) of industrial parks was under operation by end-2018F (+9% yoy), mostly on the back of new supply from northern Industrial Parks (IPs) in Hai Phong and Bac Ninh, Ba Ria Vung Tau. The Ministry of Planning and Investment estimated the average nation-wide IP occupancy rate over 2016-18F at 73% thanks to robust FDI inflows as well as strong demand from domestic enterprises on the back of rapid and accelerating economic growth.

Figure 210: Rising occupancy rates despite expanding capacity



MPI of Vietnam

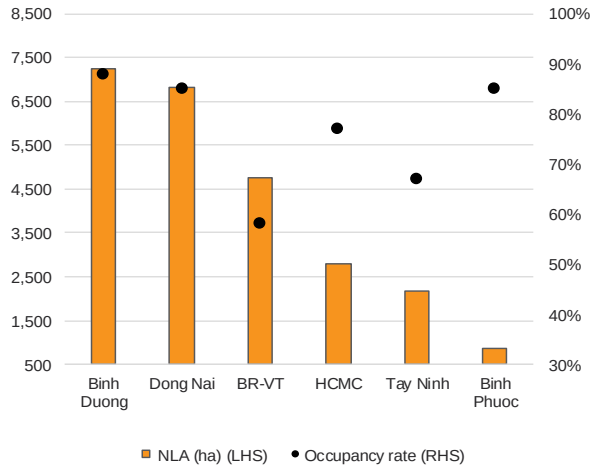
Figure 211: Vietnam was already a regional leader in terms of total industrial park area at year end 2018



Colliers International Report 4Q2018

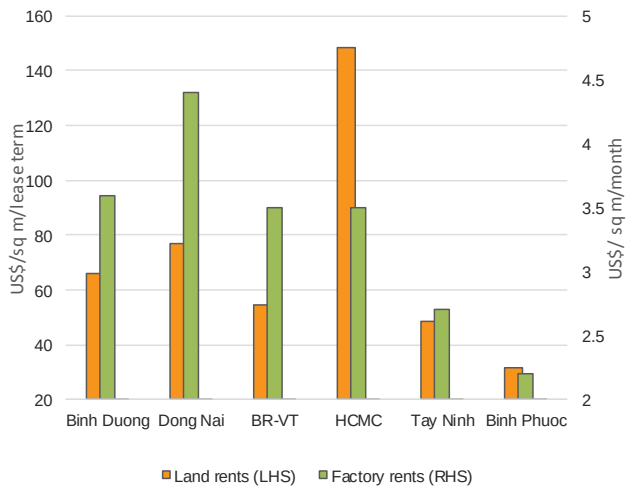
IPs are located throughout Vietnam but the southern and northern economic zones are more established when compared to the central region. The southern region, centered on HCMC, Binh Duong and Dong Nai Provinces, is considered the most active economic zone in the country. According to real estate services firm Jones Lang LaSalle's figures, as of end-Dec 2018, southern industrial park supply registered a large increase of 9% from end of 4Q17 levels, bringing the total net leasable area to about 26,119ha. Most new supply came from Ba Ria –Vung Tau and Binh Phuoc province, the less established provinces in the southern region. Binh Duong and Dong Nai are still the leading markets, accounting for nearly 56% of total supply in the south. The average southern region-wide occupancy rate was 77% in 4Q18, a 300 bp increase yoy compared to 4Q17. This increase in average occupancy was mostly contributed by Binh Duong and Dong Nai due to strong cluster effects and good transportation access. The average land rent in the southern IPs was US$80 per sq m per lease term (50 years), an increase of 11% compared to 4Q17.

Figure 212: The largest southern IPs at end-2018 were Binh Duong and Dong Nai.



Source: JLL

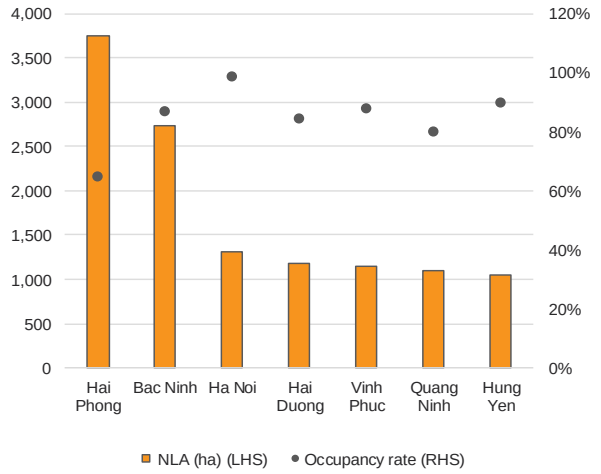
Figure 213: Rents by type of industrial property and by location in the south. HCMC is still the most expensive IP.



Source: JLL

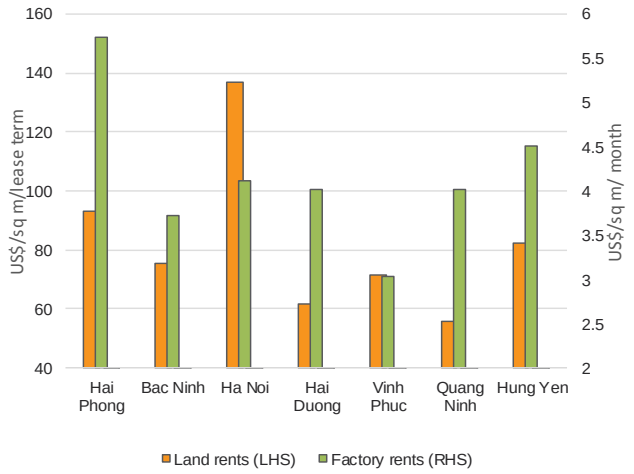
As a late starter in comparison to the south, the northern region, led by Hanoi, Hai Phong and Quang Ninh, has been able to attract more advanced, hi-tech industries. According to JLL, at end-2018, the total leasable industrial land area in the northern IPs was 12,260ha, an increase of nearly 8% compared to end of 2017. Hai Phong and Bac Ninh remain in their leading positions, contributing 53% of the total stock of leasable industrial land in the north. Having significant advantages such as accessibility to major markets, wide and developed logistical connectivity to China's Pearl River Delta, the world's preeminent electronics manufacturing hub, and strong support from the government, Bac Ninh and Hai Phong remain the most desired northern destinations for investment. With healthy demand backed by strong manufacturing growth, the 4Q18 occupancy rate, supported mostly by Hai Phong, Bac Ninh and Hai Duong, averaged 85%, an increase of 400 bp yoy. The average industrial land rent was US$82/sqm, an increase of nearly 10% yoy. Hanoi's average industrial land rent in 4Q18 increased significantly to US$137/sqm per lease term, the highest among the northern IPs.

Figure 214: The largest northern IPs at end-2018 were Hai Phong and Bac Ninh.



Source: JLL

Figure 215: Rents by type of industrial property and by location in northern Vietnam (US$/ lease term). Hanoi is the most expensive IP in term of land rents.



Source: JLL

Industrial property demand to sustain growth momentum in 2019-20F due to emerging cluster effects and the trade war

JLL estimates more than 9,793ha of industrial land supply is expected to enter the southern market over the next three years, of which extended phases of existing projects will contribute the largest proportion. Approximately 13,000ha of industrial land will enter the northern market through 2020; mainly from Hai Phong, Hai Duong and Vinh Phuc. Collectively, supply is expected to expand by 47.2% by 2020.

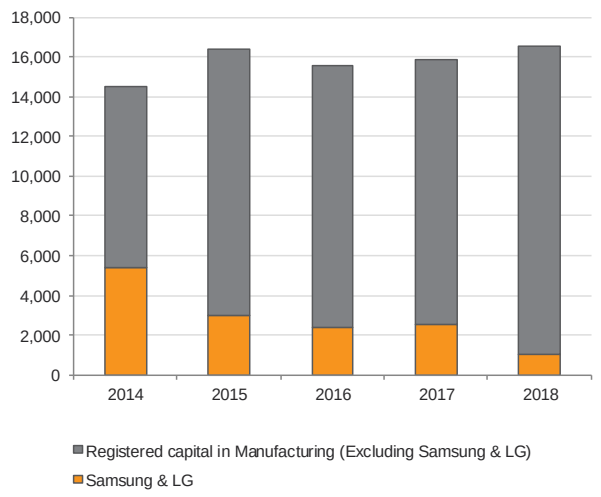
We believe strong demand for industrial properties will continue in the medium term, driving a sustained occupancy and rental rate growth to record levels. Demand for good quality, ready-built warehouse/factory space is set to grow strongly, in line with demand for industrial land. Demand will increase due to the following factors:

FDI in the manufacturing sector remains steady on the back of low-operating costs in Vietnam

Despite an increasing proportion of registered FDI going into real estate, the manufacturing sector still made up the biggest share with over 45% of FDI registered of each year in the period 2014-2018. According to the Foreign Investment Agency (FIA), the total amount of FDI going into the manufacturing sector posted a CAGR of 14.4% over this period, excluding contribution from Samsung and LG, which are huge anchor FDI investors in Vietnam and tend to distort the true manufacturing FDI picture due to the high variations in their FDI amounts from year to year. Including FDI contributions from Samsung and LG, the CAGR from 2014 to 2018 works out to 3.4% owing to large investments registered in 2014 which were not matched in 2018.

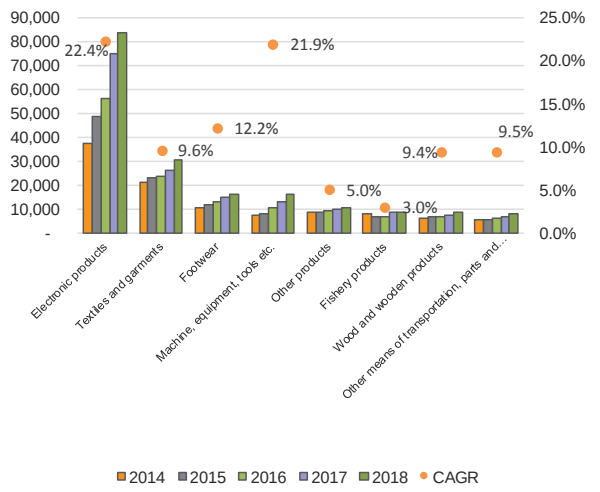
Growth in manufactured exports has been broad-based with electronic products and machinery/equipment products growing the fastest among key categories, a trend that we believe will continue as Vietnam leverages the trade tensions between China and the US to increase its share of electrical and electronic exports.

Figure 216: Growing registered capital in manufacturing (excluding Samsung & LG) (US$m, 2014-2018)



Source: FIA

Figure 217: Exports in top product categories (US $m) have grown strongly over the years; electronics and machinery are the growth leaders



Source: GSO

Figure 218: Comparative advantage of each ASEAN country by sector

Country	Sector	Reasons
Singapore	**High-tech**	- Singapore is not competitive in manufacturing due to its high operating costs and strong currency. - Manufacturing is focused on high value, low volume products or those that customers insist on doing in Singapore given its strong intellectual property protection regime.
Vietnam	**Textile, clothing & footwear**	- Vietnam has much lower labour costs than China and most ASEAN peers with sizable labour forces. - The country has been a major exporter of textile, apparel and footwear for well over a decade and therefore, has a strong skills base relative to other ASEAN countries.
	Electronics	- The country is shifting gear into electronics manufacturing, spurred by large anchor investments from Samsung and LG. - Vietnam's proximity to China's Pearl River Delta and long coastline make it easy to ship in components and parts which is a crucial advantage given the complex supply chains in this sector and China's position as a dominant supply hub.
Indonesia	**Food and beverage**	- Huge domestic market potential and well supported by productive agricultural sector and relatively predictable yields.
	Textile and clothing	- Low labour costs relative to China and a large labour force - Indonesia's textile exports contribute c.2% of the world textile demand, the second largest exporter after Vietnam in ASEAN implying a strong skills base. - Expertise in production of functional clothing (i.e. sports-wear) on top of basic clothing production ability.
	Automotive	- Indonesia has the largest automotive production capacity within ASEAN and was second only to Thailand in terms of auto exports in 2017.
	Plastics/ Rubbers	- Indonesia is the second largest natural rubber producer globally. Around 85% of Indonesia's rubber production is exported, while domestically sold rubber is mostly consumed by the automotive sector.
Thailand	**Automotive**	- Thailand has been the auto production hub in Southeast Asia over the past few decades as Thailand has a large domestic market and the government never had a national car brand development policy, thereby making way for global OEMs. - The Thai labour force is highly-skilled relative to most of ASEAN. - Strong presence of Japanese OEMs has also attracted many auto parts suppliers into the country, that have learnt to supply auto makers on a just-in-time basis. - Strong road, rail and port infrastructure helps reduce logistics costs.
	Electronics	- Strong automotive manufacturing ecosystem has created spillovers into electronics auto part manufacturing capabilities. - Thai electronic companies have ventured into making components for mobile phones and IT telecom equipment which also gives it an advantage in finished electronic goods production. Thailand is a major producer of consumer electrical appliances.
	Food and beverage	- Thailand is one of the largest food producers in the world due to a large agrarian base; the country has been a leading producer of processed food for years.
	Plastics/ Rubbers	- Thailand ranks as the largest rubber producer and exporter in the world. Complementing the natural rubber industry, Thailand is also growing its synthetic rubber segment by leveraging its robust petrochemicals production base. - Tyres are the number one rubber-based export from Thailand, with tyre producers accounting for roughly half of domestic rubber consumption given the country's large automotive manufacturing base. - Thailand has a large petrochemicals industry and is a regional leader in plastics production. Plastic packaging accounts for 48% of Thailand's raw plastic consumption, followed by 15% for its electronic sector, 14% for its construction sector and 8% for its automotive sector, according to ASEAN Briefing.
Malaysia	**Semiconductor**	- Malaysian semiconductor companies have built niche capabilities in assembly, packaging and testing of semiconductor chips. - Malaysian semiconductor companies have been the preferred partners/suppliers for foreign MNCs that are concerned over Intellectual Property (IP) infringement issues experienced with contract manufacturers in China. - The sector is supported by a strong ecosystem of local suppliers in Penang.
	Automotive	- Malaysia has a strong ecosystem of auto parts suppliers, many of which leverage its strong electronics parts and components manufacturing ecosystem.
	Plastics/ Rubbers	- Malaysia is the ASEAN region's top plastic export country. Its primary export destinations include Europe, China, Singapore, Japan and Thailand. - The Malaysian plastics market was estimated at US$3,305.4m, by revenue, in 2017 and is likely to expand at an estimated CAGR of 5.27%, during the forecast period 2018-2023, according to Mordor Intelligence.

Source: VNDIRECT

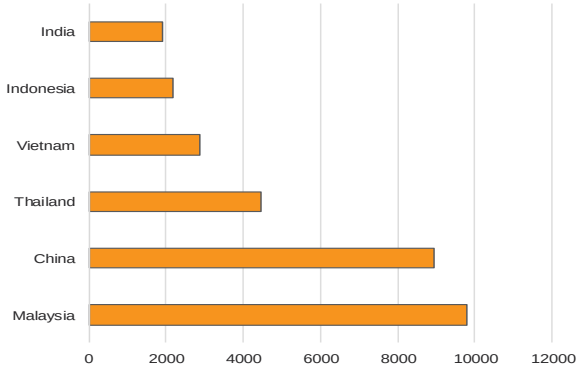
We believe low operating costs and attractive tax incentives and political stability have made Vietnam a regional sourcing hub. Compared with other ASEAN countries, Vietnam is a low-cost manufacturing base with average annual salary at end-2017 of just US$2,880, equivalent to just one-third of the average wages in China and even lower than that of Thailand.

Beside the labor cost, the growth in industrial land prices in key cities such as Shanghai in China have also risen faster than in other Southeast Asian urban areas, further eroding China's export competitiveness. According to real estate agency Colliers International, at end of 4Q2018, industrial land rental rates in HCMC ranged from US$80-160/sq m/lease term. This is compelling versus the Philippines, which is a less established manufacturing hub but a regional competitor in manufactured exports.

Despite the low cost of land and utilities, Vietnam reduced its Corporate Income Tax (CIT) from 22% to a 20% flat rate in 2016 for all domestic and foreign companies to bolster its attractiveness as a manufacturing hub.

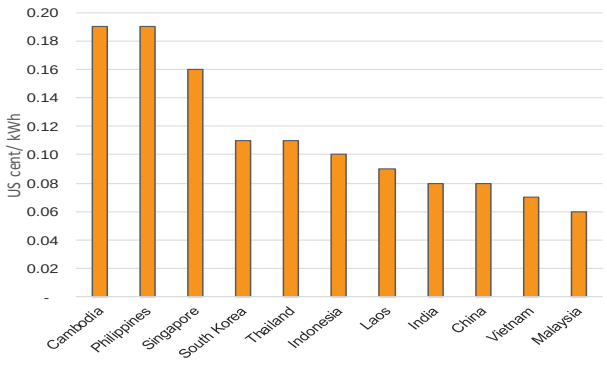
Vietnam also grants tax incentives (in two forms of preferential tax rates – reduced tax rates and tax holidays – for a certain period of time or throughout the project life) for projects in disadvantaged areas or in priority sectors targeted by the government such as high-tech electronics manufacturing. For example, Samsung Electronics Vietnam Thai Nguyen project, worth US$5b in registered capital and located in Thai Nguyen Province, enjoys tax exemptions for its first four years of operations, and a reduced tax rate of 10% in the next nine years. It is not surprising that Vietnam is a manufacturing hub for textile, garments, footwear and electronics, since projects in these sectors are eligible for tax incentives of 10% over fifteen years and all these sectors are both labor intensive and energy intensive in nature, conferring Vietnam a natural competitive advantage.

Figure 219: Vietnamese workers' annual salary (US$) among the lowest in Asia as at 2017.



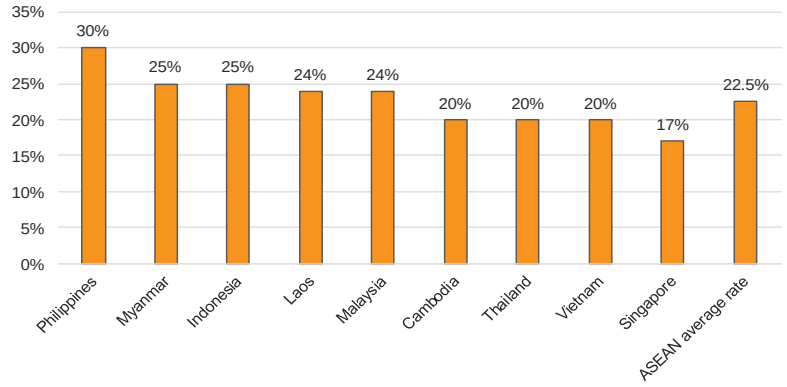
Source: Trading Economics

Figure 220: Vietnam's electricity prices are low vs. region



Source: Colliers International

Figure 221: Vietnam's standard CIT rate is lower than the average rate in other ASEAN countries (2017)



Source: VNDIRECT

Figure 222: Vietnam's range of industrial land prices 4Q2018 is compelling compared with regional peers

Country	Location	Average USD/sq m/lease term	Lease term
Thailand			Maximum 50 years
	Bangkok, Samut Prakarn, Pathumthani, Nonthaburi, Nakorn Pathom, Samut Sakorn	257.9	
China			Maximum 40 years
	Beijing, Tianjing	422	
	Shanghai, Nanjing	383.7	
	Chengdu, Chongqing	123.3	
	Guangdong, Shenzhen	68.9	
Malaysia			Maximum 30 years
	Shah Alam	301.4	
	Port Klang	161.5	
	Seremban, Negeri Sembilan	148.6	
	Johor Bahru	200.2	
Philippines			Maximum 50 years
	North of Metro Manila	152	
	South of Metro Manila	190	
	Cebu	95	
Singapore			30 years or 60 years
	Plot ratio 1	209	
	Plot ratio 2	343	
Vietnam	East of HCMC	156.8	Maximum 50 years
	West of HCMC	80	

Source: Colliers International 4Q2018

Trade war bolsters Vietnam's position as an alternative sourcing hub

As the possibility for increased tariffs by the US in the ongoing US-China trade war forces Chinese companies or foreign companies in China to look at shifting/diversifying production, assembly or sourcing to other countries, Southeast Asia has emerged as the leading choice, with Vietnam the key beneficiary. **We expect Vietnam to gain share in electrical/machinery and textile exports while Thailand gains share in electrical and auto part exports, over the longer term, as we detail in our Asean strategy report dated 19 Dec 2018.**

Figure 223: Summary of how we arrived at our shortlist of "high potential" sectors for ASEAN to benefit from the trade war

	Machinery/ Electrical	***Plastics/ Rubbers***	***Textiles/ Footwear& Headgear***	***Transportation (Automotive)***
How big Is the addressable market for ASEAN exporters (China's current exports to US)?	●	◐	◕	◔
How does ASEAN currently stack-up versus China in exporting to the US?	◐	◕	◕	◔
Is ASEAN's relative market share of exports to the US small enough to allow for market share gains from China (<0.5)?	*Yes*	*Yes*	*Yes*	*Yes*
How sizable is ASEAN's existing manufacturing base in the sector (for domestic + exports)?	◕	◕	◕	◐
How contained is the competitive threat from other regions ex-ASEAN in gaining export market share from China?	◕	◕	◔	◐
Overall attractiveness rating	●	◕	◐	◐

NOTE: ● = "Very favourable"; ○ = "Unfavourable"

Source: VNDIRECT

Figure 224: Importance of success factor by export sector and potential ASEAN trade-war beneficiaries by sector

	Machinery/ Electrical		***Plastics/ Rubbers***		***Textiles/ Footwear & Headgear***		***Transportation (Automotive)***	
Cheap labour force	◐	VN, ID	◔	VN, ID	●	VN, ID	◔	VN, ID
Proximity to major component supply base	●	VN, TH	◔	SG, TH, MY, VN	◐	VN, TH	◕	TH, MY, VN
Strong existing manufacturing/relevant skills base	◕	MY, TH, VN	◐	SG, TH, ID, MY	◔	VN, ID	●	TH, MY
Captive raw material supply base	◔	NONE	◕	TH, ID, MY	◐	TH	◔	TH, ID, VN
Strong existing US export orientation	◕	MY, TH, VN	◐	TH, ID, MY	◐	VN, ID	●	TH
Biggest potential beneficiaries in ASEAN by sector, based on comparative advantage	**MY, TH, VN**		**TH, ID, MY**		**VN, ID**		**TH, MY**	

NOTE: ● = "Critical success factor", ○ = "Unimportant success factor"

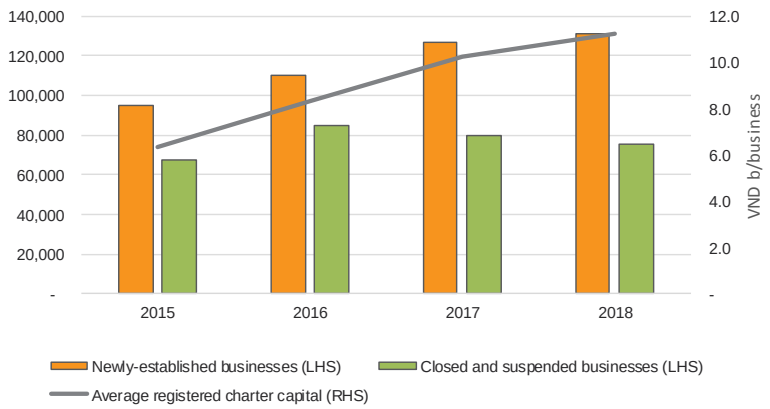
Source: VNDIRECT

Positive economic outlook boosting local business confidence

The World Bank projects Vietnam's GDP to expand sustainably at over 6.5% over the medium term with some upside potential in the short run, if the global economy remains healthy. This positive medium-term economic outlook could support production and consumption. The number of local, newly-established companies has grown since 2015, accompanied with decreasing business closures. This is anchored by heightened business confidence amid a positive economic outlook. Rising capital investment by domestic manufacturers and retailers will

drive continued demand for factory /warehouse leasing and industrial land. The average amount of registered capital per business entity in 2018 has also doubled from 2015 levels, implying more businesses are ready to capitalise on the growth prospects in Vietnam.

Figure 225: Number of newly-established local businesses in Vietnam



Source: VNDIRECT

Booming e-commerce creates demand for warehouse leasing

Mobile phone shopping has been growing rapidly in Vietnam, facilitated by strong growth in smartphone penetration in major cities. The e-commerce market has witnessed some significant events such as a successful collaboration between Alipay and National Payment Corporation of Vietnam while local e-commerce portal Tiki received funding from JD.com. For e-commerce firms, it is critical to come up with new business models to handle a soaring number of frequent and small-sized orders, driving a huge demand for ready-built warehouses/factories and a need for significant investments to improve technology and infrastructure.

Figure 226: E-commerce sales are growing fast

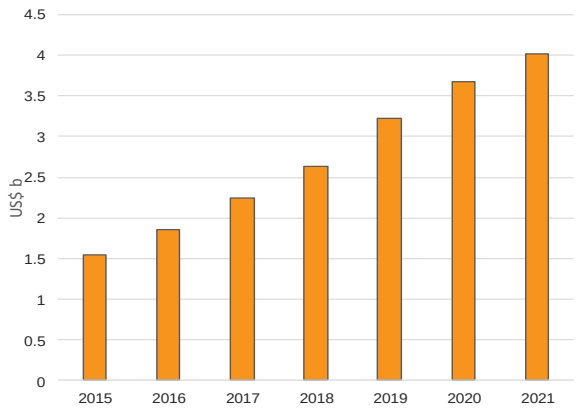
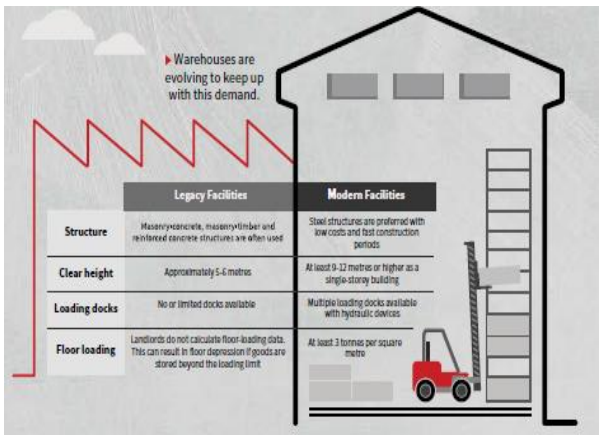


Figure 227: Warehouses evolving to keep up with e-commerce growth



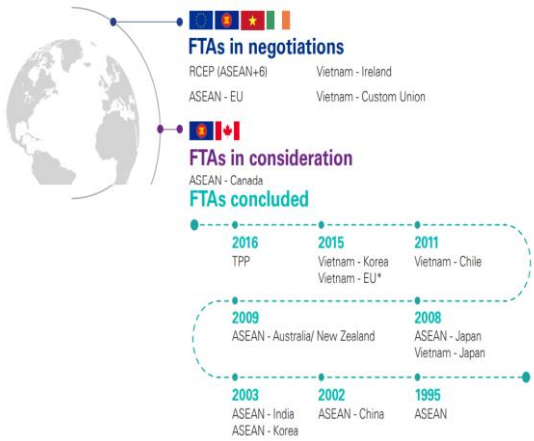
Source: "Digital in 2017: Southeast Asia" Report, Jan 2017 by Wearesocial and Hootsuite

FTAs create tailwinds for FDI inflows

Vietnam is on its way to acquire duty free access for its exports to the EU under the EU-Vietnam Free Trade Agreement. It also signed the 11-nation Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in March 2018. Once the tariff reduction schedules of these FTAs are completed, Vietnam will offer close to tariff-free access into EU countries and much of emerging Asia, including the giant markets of China and India. Other benefits available

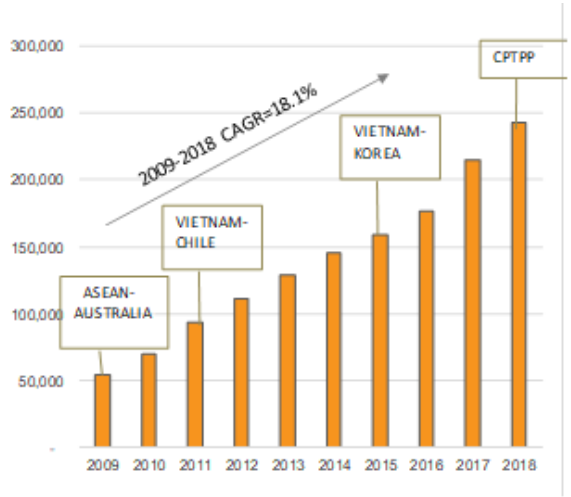
under FTAs include reduced import costs, increased access to a wide range of products eligible for preferential treatment, improved customs clearance times, and less complicated trade procedures. Through FTAs, businesses operating in Vietnam can access more raw material and intermediate inputs from other countries as well as procuring better quality capital goods at competitive prices.

Figure 228:



Source: Lang LaSalle

Figure 229: Exports (US$m) from Vietnam being boosted by a slew of free trade agreements



Source: Custom Bureau of Vietnam

INDUSTRIAL PROPERTY SECTOR STOCK PICKS: WE PUT KBC AND LHG ON OUR WATCHLIST

We favour industrial property stocks with sizable NLA available for leasing, strategically located industrial parks and healthy profitability namely Long Hau Corporation **(LHG VN, Not rated)** and Kinh Bac City Development Corporation **(KBC VN, Not rated),** as we believe they will be the first beneficiaries of strong demand for industrial property leasing. This demand will result in positive earnings growth. We advise investors to keep an eye on these names.

Kinh Bac City Development Corporation (KBC VN, Not rated). We are positive on land leasing prospects across its current IPs. Located in northern Vietnam, these parks are likely to see a strong increase in new leased area per year over the next two years due to their proximity to China and with supporting logistical infrastructure completed and already operational. Furthermore, the residential segment will become a big revenue contributor on the back of a strong pre-sales backlog driven by the recent stellar real estate market in Bac Ninh province. The Phuc Ninh townhouse project is being launched in two phases with total Net Saleable Area (NSA) of 13.9ha to be launched in phase one. Total cumulative contracted sales during 2018-2020F is forecasted to touch VND2,337bn while unbooked presales at end-2017 was reported at VND1,361bn, all of which is yet to be booked as revenue (the presales backlog figure for 2018 year end has not been disclosed yet).

However, the Trang Cat townhouse project in Hai Phong has not been launched due to insufficient funding and market timing issues. We foresee that the project will not be monetised easily in 2019F due to sizable development costs.

Long Hau Corporation (LHG VN, Not rated). In the short term, the opening of Long Hau 3 industrial park with 100ha of NLA and new

factories in 2019 will boost revenue and earnings growth in 2019. In the long term, LHG can leverage its 981ha land bank in Long An, the fourth largest lank bank among that of listed rivals, to secure its long-term revenue prospects.

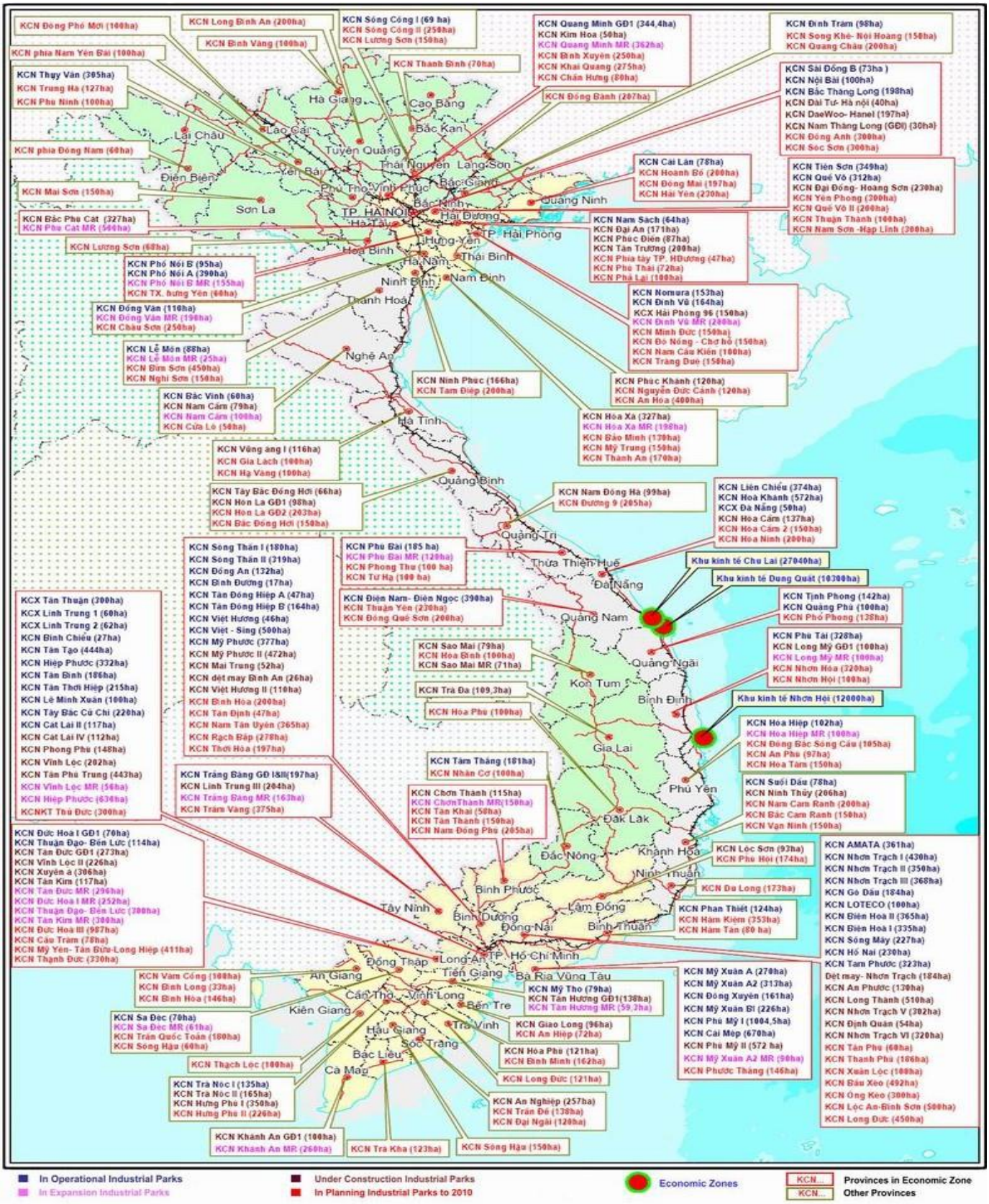
LHG's attraction also lies in a stable and juicy dividend yield of 8.3-10% in 2019-2020F, based on the company's stated dividend policy and the current share price. The company's net cash position also sharpens its competitive edge.

Figure 230: Sector comparative multiples (price as of 11 Jan 2019)

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
Kinh Bac Urban Development	KBC	275.9	70.5	22.2	3.3	5.7	0.3	12.2	0.7
IDICO	IDC	247.7	-14.4	-14.4	2.5	9.1	0.9	2.8	1.9
SONADEZI	SNZ	171.4	14.9	3.3	2.7	6.4	0.6	9.2	0.9
Tan Tao Industrial Park	ITA	120.2	5956.3	141.8	1.1	1.3	0.1	20.3	0.3
Nam Tan Uyen Industrial Park	NTC	57.0	139.1	21.1	6.1	47.6	0.3	7.1	3.2
TANIMEX	TIX	42.1	98.7	12.1	8.5	13.0	0.0	10.3	1.3
Long Hau	LHG	38.7	-52.8	-0.7	12.3	22.2	0.0	3.5	0.8
Industrial Urban Development No.2	D2D	31.1	2.3	0.2	6.7	17.7	0.0	9.2	1.6
Sonadezi Long Thanh	SZL	23.8	11.4	13.0	6.7	19.2	0.0	5.3	1.0
Vinh Phuc Infrastructure Development	IDV	20.0	28.9	-3.5	9.3	32.3	0.0	7.3	2.1
Tinnghia Industrial Park	TIP	17.8	19.2	5.1	8.4	11.0	0.0	8.2	1.0
Bao Thu Development	BII	2.0	128.7	73.6	1.1	1.4	0.1	5.2	0.1
Simple average			533.6	22.8	5.7	15.6	0.2	8.4	1.2
Simple average (excluding ITA)			**40.6**	**12.0**	**6.1**	**16.9**	**0.2**	**7.3**	**1.3**
Median			24.0	8.6	6.4	12.0	0.1	7.8	1.0

Source: VNDIRECT

Figure 231: Map of key industrial parks throughout Vietnam



Source: MPI of Vietnam

KINHBAC CITY DEVELOPMENT CORP (KBC)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND13,800	N/A	0.00%	NOT RATED	PROPERTY

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Nhan Lai Thi Thanh
nhan.laithanh@vndirect.com.vn

The company is enjoying healthy IP leasing momentum on the back of an increase in new land area leased per year and new recently-launched industrial properties. The residential segment is also starting to take-off with an estimated VND 2,337 of new contracted sales to be realised over 2018-2020F, per management.

Enjoying a surge in northern industrial property leasing demand. With the second largest NLA of 519ha in the northern industrial zones, KBC expects to benefit from not only strong demand for industrial property in the medium term but also a higher-than-market average increase in rental rates thanks to its strong brand name and blue chip tenant base. KBC's Que Vo and Trang Due IPs are home to the regional manufacturing hubs of South Korean multinational giants.

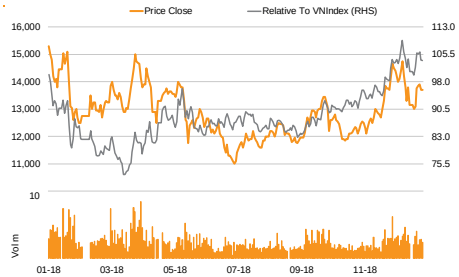
Phase 1 of the Nam Son Hap Linh industrial park will launch in 2019. KBC will launch the new Nam Son Hap Linh IP with an NLA of 66ha in Bac Ninh province this year, adding to its total available NLA of 453ha as at end-2017. KBC has guided that this new park will realise a healthy rental rate of US$80/sq m/lease term and see rising occupancy driven by its proximity to Que Vo IP, the manufacturing base of Samsung Electronics Vietnam Co.,Ltd and its satellites.

Strong pre-sales backlog for residential segment. The Phuc Ninh townhouse project is being launched in two phases with a total NLA of 13.9ha in the first phase. Management guides for total contracted sales of VND2,337bn over 2018-20F and the reported unbooked presales backlog at end-2017 was VND1,361bn. However, the People's Committee of Bac Ninh province has issued a notice in Oct 2018 of KBC's non-compliance with the master zone plan.

Illiquid inventory has not yet been monetised. The company has not launched its Trang Cat Townhouse project, the largest component of its inventory, due to market-timing issues. This illiquid inventory has weighed on KBC stock, leading it to trade at a discount to its BVPS over 2016-18F.

Positive 2018F results. With strong growth in the leasing and residential segments, KBC guides for 2018F revenue of VND2,600bn (+106.3% yoy) and net profit of VND800bn (36.7% yoy)

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	15,300
52w low (VND)	11,000
3m Avg daily volume (shares)	3,746,523
3m Avg daily value (VNDmn)	31,619
Market cap (VNDbn)	6,436
Outstanding shares (m)	470
Free float (%)	37
TTM P/E (x)	12.2
Current P/B (x)	0.7

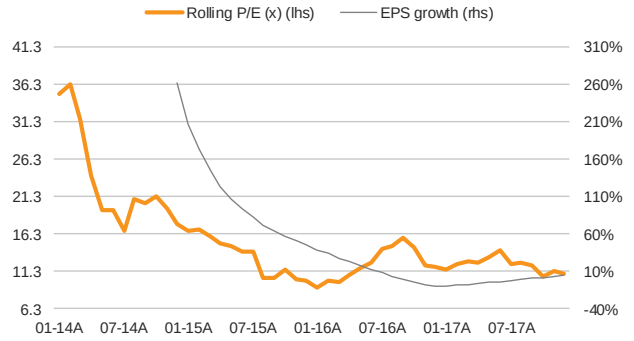
Ownership

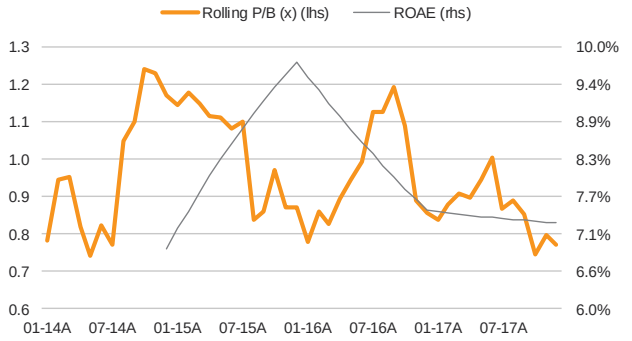
Dang Thanh Tam	16.0%
Kinh Bac Consulting and Investment	9.6%
Dragon Capital	5.6%
Others	68.8%

Source: VNDIRECT

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	1,069	1,435	1,972	1,260
Revenue growth	(0.4%)	34.2%	37.5%	(36.1%)
Gross margin	55.0%	40.0%	56.1%	51.6%
EBITDA margin	55.5%	57.1%	50.9%	72.9%
Net profit (bn)	326	612	557	585
Net profit growth	349.1%	87.9%	(8.9%)	4.9%
Recurring profit growth				
Basic EPS	904	1,316	1,172	1,229
Adjusted EPS	904	1,316	1,172	1,229
BVPS	13,585	15,062	16,192	17,423
ROAE	6.9%	9.8%	7.5%	7.3%

Valuation





Income statement			
(VNDbn)	12-15A	12-16A	12-17A
Net revenue	1,435	1,972	1,260
Cost of sales	(861)	(865)	(611)
Gen & admin expenses	(35)	(33)	(22)
Selling expenses	(93)	(121)	(155)
Operating profit	**446**	**953**	**473**
Operating EBITDA	446	953	473
Depreciation and amortisation			
Operating EBIT	**446**	**953**	**473**
Interest income	26	34	76
Financial expense	(41)	(99)	(109)
Net other income	291	12	353
Income from associates & JVs	10	22	19
Pre-tax profit	**730**	**921**	**812**
Tax expense	(128)	(210)	(193)
Minority interest	10	(154)	(34)
Net profit	**612**	**557**	**585**
Adj. net profit to ordinary	612	557	585
Ordinary dividends			
Retained earnings	**612**	**557**	**585**

Balance sheet			
(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	228	295	505
Short term investments	2	1	1
Accounts receivables	3,362	4,382	4,744
Inventories	8,364	8,244	8,323
Other current assets	47	89	158
Total current assets	**12,003**	**13,011**	**13,730**
Fixed assets	376	359	269
Total investments	893	893	912
Other long-term assets	382	395	868
Total assets	**13,653**	**14,658**	**15,780**
Short-term debt	1,205	863	1,132
Accounts payable	77	114	134
Other current liabilities	1,662	2,396	2,060
Total current liabilities	**2,945**	**3,373**	**3,326**
Total long-term debt	1,352	1,105	1,591
Other liabilities	1,322	1,559	1,825
Share capital	4,757	4,757	4,757
Retained earnings reserve	1,782	2,319	2,905
Shareholders' equity	**7,165**	**7,703**	**8,288**
Minority interest	871	918	750
Total liabilities & equity	**13,653**	**14,658**	**15,780**

Cash flow statement			
(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**730**	**921**	**812**
Depreciation & amortisation	28	27	40
Tax paid	(121)	(6)	(3)
Other adjustments	(362)	32	(30)
Change in working capital	**(353)**	**(65)**	**(758)**
Cash flow from operations	**(78)**	**909**	**61**
Capex	(40)	(58)	(94)
Proceeds from assets sales			
Others	206	3	(529)
Other non-current assets changes	7	(198)	
Cash flow from investing activities	**173**	**(253)**	**(623)**
New share issuance			
Shares buyback			
Net borrowings	(15)	(589)	772
Other financing cash flow			
Dividends paid			
Cash flow from financing activities	**(15)**	**(589)**	**772**
Cash and equivalents at beginning of period	149	228	295
Total cash generated	**79**	**67**	**209**
Cash and equivalents at the end of period	228	295	505

Key ratios			
	12-15A	12-16A	12-17A
Dupont			
Net profit margin	42.6%	28.3%	46.4%
Asset turnover	0.11	0.14	0.08
ROAA	4.6%	3.9%	3.8%
Avg assets/avg equity	2.13	1.90	1.90
ROAE	9.8%	7.5%	7.3%
Efficiency			
Days account receivable	126	203	352
Days inventory	3,544	3,488	4,976
Days creditor	32.6	48.1	80.3
Fixed asset turnover	3.82	5.37	4.01
ROIC	5.8%	5.3%	5.0%
Liquidity			
Current ratio	4.08	3.86	4.13
Quick ratio	1.24	1.41	1.63
Cash ratio	0.08	0.09	0.15
Cash cycle	3,637	3,643	5,248
Growth rate (yoy)			
Revenue growth	34.2%	37.5%	(36.1%)
Operating profit growth	(8.9%)	113.9%	(50.4%)
Net profit growth	87.9%	(8.9%)	4.9%
EPS growth	45.7%	(11.0%)	4.9%
Share value			
Basic EPS (VND)	1,316	1,172	1,229
BVPS (VND)	15,062	16,192	17,423

Source: VNDIRECT

LONG HAU CORP (LHG)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND18,200	N/A	8.3%	NOT RATED	PROPERTY

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Nhan Lai Thi Thanh
nhan.laithanh@vndirect.com.vn

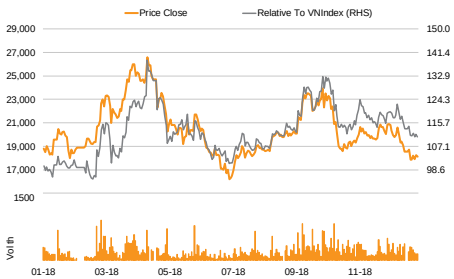
The newly-launched Long Hau 3 Industrial Park (LH3 IP) in 2019 will bring LHG a new revenue stream from land rental over FY2019-20F. Factory leasing will also start to be a big revenue contributor from 2019F. The company operates 176 ha of total IP area with another 90 ha in the development pipeline.

Benefitting from steady demand growth at the leading industrial zone. Located close to HCMC's Nha Be District, LHG's IPs have an advantage compared to other IPs not only from comprehensive supporting infrastructure such as major roads and the nearby Hiep Phuoc port but also from robust demand for industrial properties in the southern zones, the initial hub of industrial development in Vietnam.

Long Hau 3 industrial park ensures a new revenue stream over the next two years: LHG states that it will launch a new 90ha LH3 IP in 2019F in Long An to secure a new revenue stream over 2019-20F. To date, leases on 10ha has been secured through MOUs with foreign clients. Due to compensation disagreements with some local residents, land clearance has not been completed. The current compensation ratio is 60% of the total LH3 area. However, the management states it is a matter of time before the issue is settled given the high opportunity cost to all stakeholders associated with further delays in compensation negotiations.

A high dividend yielding name with positive guidance for 2019F and supported by low gearing. Together with growth in land leasing income from the LH3 IP, the factory leasing segment is expected to expand with 62.9% growth in revenue in 2019F driven by the newly-launched 20ha of industrial space in Da Nang high technology IP based on company guidance. Hence, the company is expecting to record in 2019F a total revenue of VND650bn, + 37% yoy and a net profit of VND170bn, +13.3% yoy. The company guides for a 15% dividend payout on par in 2019, equivalent to a 8.3% dividend yield. At the end of 3Q18, the company's balance sheet showed a net cash position.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	26,600
52w low (VND)	16,200
3m Avg daily volume (shares)	270,427
3m Avg daily value (VNDmn)	5,718
Market cap (VNDbn)	913
Outstanding shares (m)	50.4
Free float (%)	42
TTM P/E (x)	3.5
Current P/B (x)	0.8

Ownership

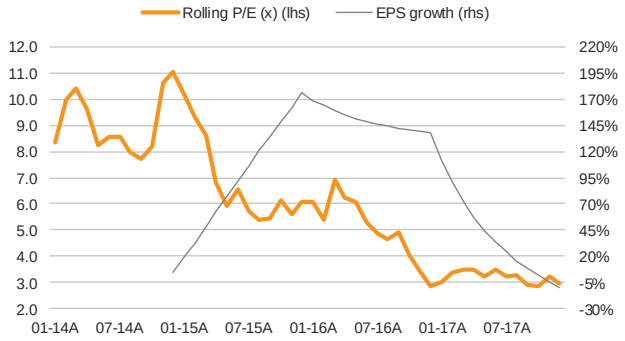
Tan Thuan Industrial Park Development	48.6%
Indochina Growth Master Fund	6.8%
Minh Phuc Trading	1.7%
Others	42.9%

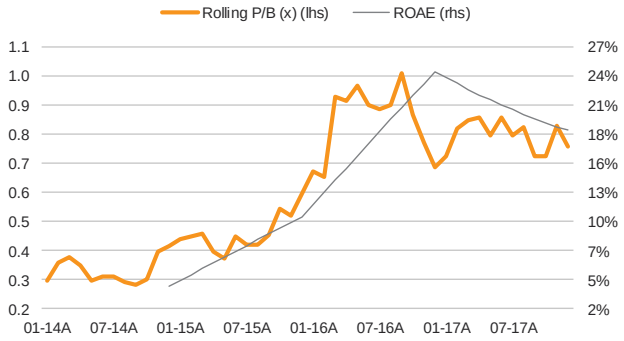
Source: VNDIRECT

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	313	232	480	488
Revenue growth	30.0%	(25.7%)	106.8%	1.6%
Gross margin	53.3%	43.2%	56.9%	55.6%
EBITDA margin	24.7%	24.0%	43.0%	43.9%
Net profit (bn)	25	70	165	166
Net profit growth	4.0%	176.5%	137.8%	0.2%
Recurring profit growth				
Basic EPS	965	2,668	6,345	5,718
Adjusted EPS	965	2,668	6,345	5,718
BVPS	24,495	26,217	25,693	21,822
ROAE	3.9%	10.5%	24.4%	18.8%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	232	480	488
Cost of sales	(132)	(207)	(217)
Gen & admin expenses			
Selling expenses	(52)	(89)	(79)
Operating profit	**48**	**184**	**192**
Operating EBITDA	48	184	192
Depreciation and amortisation			
Operating EBIT	**48**	**184**	**192**
Interest income	7	19	13
Financial expense	(22)	(9)	(6)
Net other income	1	3	9
Income from associates & JVs			
Pre-tax profit	**34**	**197**	**208**
Tax expense	35	(32)	(42)
Minority interest			
Net profit	**70**	**165**	**166**
Adj. net profit to ordinary	70	165	166
Ordinary dividends			
Retained earnings	**70**	**165**	**166**

Balance sheet

(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	128	255	456
Short term investments	2	12	362
Accounts receivables	363	419	216
Inventories	277	216	307
Other current assets	3	1	0
Total current assets	**772**	**903**	**1,340**
Fixed assets	53	49	53
Total investments	185	225	225
Other long-term assets	369	349	370
Total assets	**1,379**	**1,527**	**1,988**
Short-term debt	87	22	24
Accounts payable	11	11	12
Other current liabilities	314	509	521
Total current liabilities	**412**	**542**	**557**
Total long-term debt	48	50	39
Other liabilities	235	265	301
Share capital	261	261	500
Retained earnings reserve	345	331	440
Shareholders' equity	**684**	**670**	**1,091**
Minority interest			
Total liabilities & equity	**1,379**	**1,527**	**1,988**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**34**	**197**	**208**
Depreciation & amortisation	27	27	29
Tax paid			
Other adjustments	46	24	(83)
Change in working capital	**44**	**23**	**159**
Cash flow from operations	**151**	**272**	**313**
Capex	(3)	(11)	(43)
Proceeds from assets sales		2	
Others		(29)	(349)
Other non-current assets changes	10	(4)	16
Cash flow from investing activities	**6**	**(42)**	**(376)**
New share issuance			312
Shares buyback			
Net borrowings	(101)	(64)	(8)
Other financing cash flow			
Dividends paid	(47)	(39)	(39)
Cash flow from financing activities	**(148)**	**(103)**	**265**
Cash and equivalents at beginning of period	119	128	255
Total cash generated	**9**	**127**	**201**
Cash and equivalents at the end of period	128	254	456

Key ratios

	12-15A	12-16A	12-17A
Dupont			
Net profit margin	30.0%	34.5%	34.0%
Asset turnover	0.16	0.33	0.28
ROAA	4.9%	11.4%	9.4%
Avg assets/avg equity	2.16	2.15	2.00
ROAE	10.5%	24.4%	18.8%
Efficiency			
Days account receivable	540	221	41
Days inventory	768	383	517
Days creditor	30.0	20.0	20.6
Fixed asset turnover	2.87	9.37	9.55
ROIC	8.5%	22.3%	14.4%
Liquidity			
Current ratio	1.87	1.67	2.40
Quick ratio	1.20	1.27	1.85
Cash ratio	0.31	0.49	1.47
Cash cycle	1,278	584	537
Growth rate (yoy)			
Revenue growth	(25.7%)	106.8%	1.6%
Operating profit growth	(61.4%)	281.4%	4.1%
Net profit growth	176.5%	137.8%	0.2%
EPS growth	176.5%	137.8%	(9.9%)
Share value			
Basic EPS (VND)	2,668	6,345	5,718
BVPS (VND)	26,217	25,693	21,822

Source: VNDIRECT

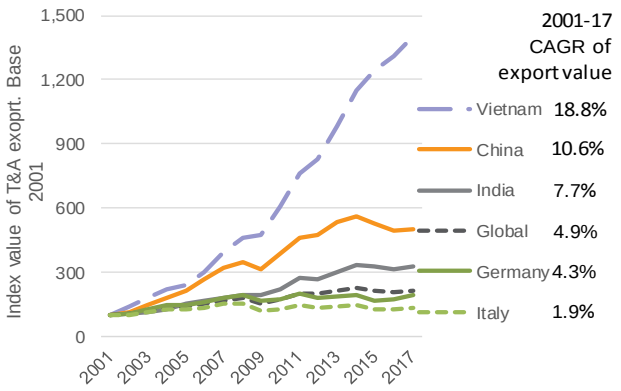
TEXTILE AND APPAREL: RIDING ON THE COAT TAILS OF VIETNAM'S GROWING TRADE INTEGRATION

Vietnam Textile and Apparel industry review

Vietnam is the world's fastest growing Textile and Apparel exporter

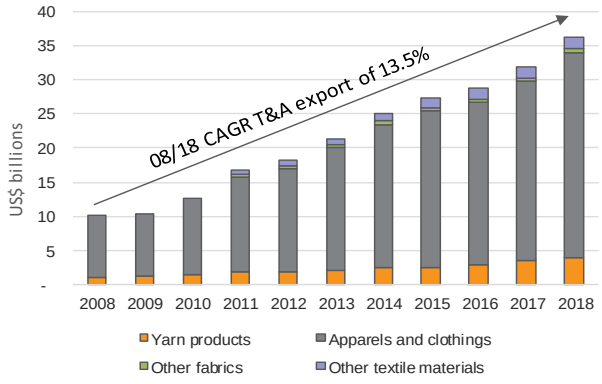
The Vietnam Textile and Apparel (T&A) sector in Vietnam has developed rapidly since Vietnam's ascension to the World Trade Organization. Total exports in this sector surged at a CAGR of 18.8% over the period 2001-2017 reaching US$31.2bn in 2017, vs the average growth rate of 4.9% over the same period in global textile and apparel exports, according to the WTO. In FY18, total textiles and apparel exports of Vietnam touched US$36.1bn (+16.0% yoy), surpassing the annual plan of US$35bn set by Vietnam Textile and Apparel Association (VITAS).

Figure 232: Vietnam is the fastest growing T&A exporter



Source: VNDIRECT, WTO

Figure 233: Vietnamese T&A exports growth has been driven by downstream garment production (2008-18)

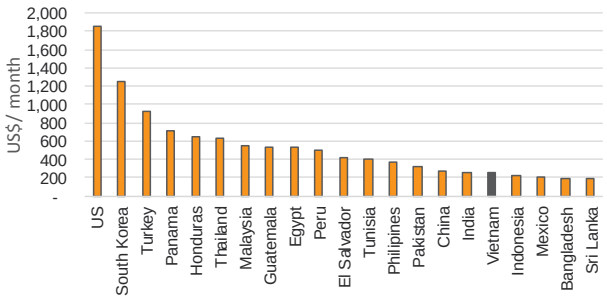


Source: VNDIRECT, VITAS

Boosted by cheap labour and Free Trade Agreements (FTAs)

Textile production is a labour-intensive industry. According to our estimation, labour costs account for around 20% of a garment product's retail price on average, therefore having a large and cheap labour force is a vital comparative advantage. Vietnam's large and relatively cheap labor force has enabled it to gain export market share from incumbent China which has seen a steep rise in labor costs.

Figure 234: Average minimum monthly wage of garment workers in 2017 (US$)



Source: VNDIRECT, PRI

Figure 235: Signed FTAs with major textile trading partners

FTAs with major T&A trading partners

Name	Partners	Effective from	Effective import tax rate for textiles (%)		2017 export value (US$ bn)	% share of Vietnam T&A exports in 2017 to FTA partner
			Before signing	After signing		
VJEPA	Vietnam - Japan	2009	10% - 40%	0%	3.3	10.7%
VKFTA	Vietnam - Korea	2015	10% - 30%	0%	3.1	10.0%
ACFTA	ASEAN - China	2006	Over 10%	0%	3.4	11.1%

Source: VNDIRECT

At the same time, Free Trade Agreements (FTAs) have played a crucial role in enhancing Vietnam's export competitiveness as these FTAs, on average, have led to a waiver or phased reduction of import taxes as high as 10%. Vietnam, participating in 16 FTAs (both bilateral

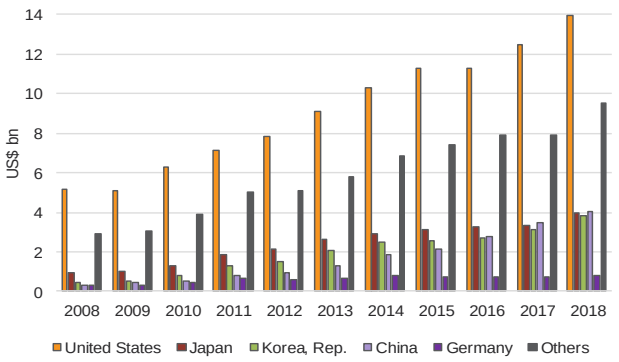
and multi-lateral) with a majority of leading textile and clothing importers, has largely benefitted from these import tax and duty exemptions in key export markets.

While the US remains Vietnam's top T&A export destination, Vietnam is diversifying its export footprint with a tilt to Asia

We are seeing a diversification in Vietnam's export destinations toward Asia, notably China and South Korea. T&A export value from Vietnam to China grew at a CAGR of 29.2% over 2008-17 while exports to South Korea grew by 24.9% over the same period. The share of T&A exports to China in Vietnam's total T&A exports rose from 3.4% to 11.1% while the corresponding figure for South Korea increased from 4.1% to 10.5% over 2008-17.

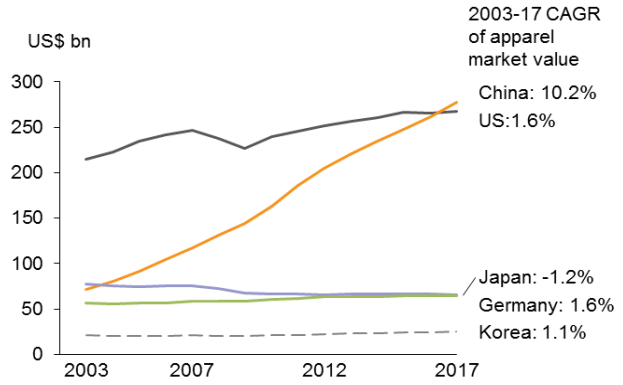
One key driver of China's growing share in Vietnam's T&A export mix is the strong growth in the Chinese apparel market which clocked a 2003-17 value CAGR of 10.2% to reach US$278bn, surpassing the US to become the largest apparel market in the world. This growth was driven by strong economic growth which led to higher purchasing power and led consumers to trade up to branded clothing and also to premium and high-end products, according to Euromonitor. In the same period, the US share of total Vietnam T&A exports decreased from 51.2% in 2008 to 40.3% in 2017 due to a slowdown in the US apparel market (with 2003-17 CAGR of value reaching 1.6%) as it appears at maturity.

Figure 236: Vietnam T&A exports by key destination country



Source: VNDIRECT, Vietnam Customs

Figure 237: Apparel market value of Vietnam's major T&A trading partners



Source: VNDIRECT, Euromonitor

Vietnamese T&A enterprises recorded a solid performance in 2018, driven by (1) a rise in large export orders that were re-allocated from China to Vietnam due to US-China trade tensions; and (2) expanding gross margins thanks to a gradual shift towards higher value-added products such as FOB products (versus CMT) and recycled yarn (versus regular yarn).

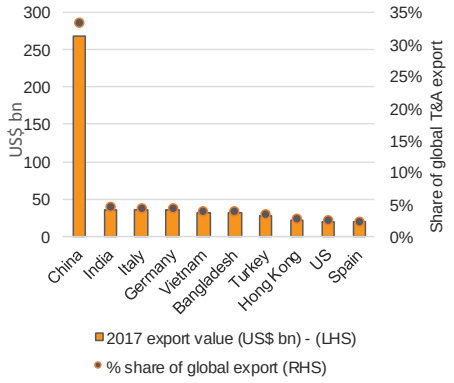
Figure 238: Summary of Vietnamese T&A enterprises' operating results

		Net sales growth (% yoy)			Gross margin (%)		
Enterprises	Segment	2017	9M2018	change (pts)	2017	9M2018	change (bp)
TCM	Textiles and apparel	4.5%	15.4%	10.9%	15.7%	17.6%	194
TNG	Apparel	31.8%	47.6%	15.7%	17.6%	17.5%	-3
EVE	Bedding	15.1%	27.1%	12.0%	33.2%	32.6%	-59
STK	Yarn (Textiles)	46.4%	24.4%	-22.0%	10.9%	14.3%	338
VGT	Textiles and apparel	12.8%	10.7%	-2.1%	9.1%	10.0%	88
VGG	Apparel	12.3%	16.8%	4.5%	11.7%	11.3%	-38
MSH	Apparel, bedding	9.7%	21.1%	11.4%	17.2%	19.4%	224

Source: VNDIRECT

A host of external factors will support the continued growth of Vietnam's Textiles and Apparel export industry.

Figure 239: China is still a dominant player in the global T&A export market



Source: VNDIRECT, WTO

Structural changes in China's economy underway to focus on innovation and technology-led sectors.

The Chinese government wants the country to move up the value chain after adopting the 13th Five-Year plan (for the period 2016 – 2020) in 2016 with the objective of developing an innovation-driven, balanced and green economy. This means that technology and other science innovation industries will become the main growth driver in the future. At the same time, industries that are polluting (including textiles, which accounts for 5.4% of total global carbon emission and 20% of water pollution, according to NRDC) will be strictly monitored and likely to be curtailed. Also, in our view, the value added by the textile industry will be much smaller than that by the technology sector, going forward, in helping maintain an annual GDP growth of 6.5% during 2016-2020, as set by the Chinese government.

In April 2016, China decided to end all subsidies for T&A exports (which run contrary to WTO rules regarding fair trade agreements) including crucial tax advantages and tax rebates, dealing yet another blow to the competitiveness of this industry.

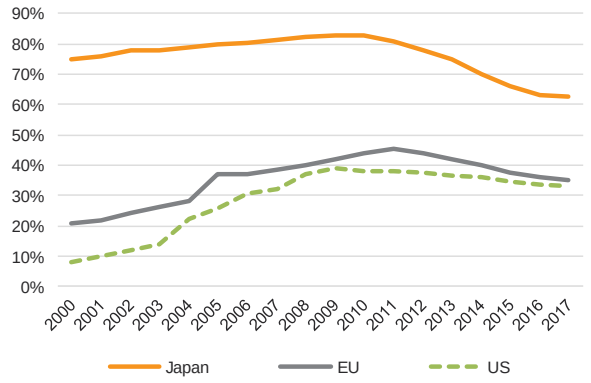
Figure 240: Summary of China's 13th Five-Year plan regarding textiles and apparel industry

Indicators	Actual 2011-2015 performance	2016-2020 goals (under the 13th Five-year plan)	Our views/comments
Textiles and apparel annual value growth rate (%)	8.5%	6.0%-7.0%	Much slower growth rate due to the focus on high-tech sectors
Output of textile fiber	Reached 53m tons in 2015, +4.5% annually	Not mentioned	China seems not to be expanding capacity in textile production (including cotton and synthetic yarn) as the global textile industry is recording slow growth
Fiber end-use production proportion by value	45.6% apparel (eg: clothing)	40.0% apparel	There will be a shift of production towards advanced products that require high-tech know how such as industrial textiles and away from apparel which is labour-intensive
	28.1% home textiles (eg: bedding, carpets)	27.0% home textiles	
	25.3% industrial textiles (eg: automotive, protective, agro textiles)	33.0% industrial textiles by 2020	
Annual labour productivity growth (%)	10.0%	8.00%	We think that Chinese T&A labour productivity is approaching diminishing growth
Exports	Increased at 2011-15 CAGR of 6.6%. Total exports reached US$291bn in 2015. Market share in global textile exports rose by 3.1% in the same period.	Maintain a stable market share in global textile exports	In our view, despite slower growth, China will still be the leader in the global textile export market (33.5% market share in 2017 vs 4.5% from India, which is in 2nd place.
Number of enterprises with annual revenue over US$1.5bn	Around 20	Arround 50 by 2020	The Chinese government intends to use a "big player" strategy to take advantage of its size and achieve economies of scale

Source: VNDIRECT, Official sources

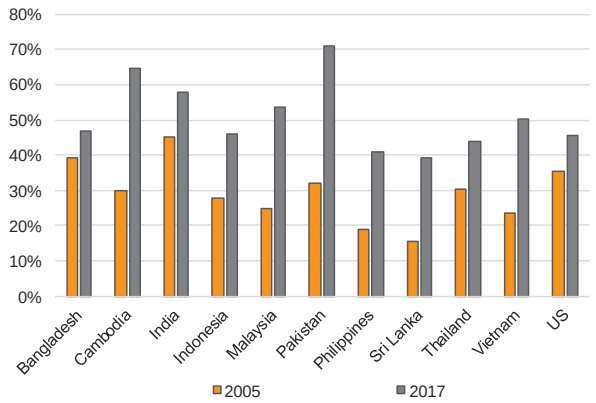
Overall, we expect the whole Chinese Textile and Apparel (T&A) industry to slow down due to the structural shift underway in the economy. Also, within the industry, we forecast a shift into upstream segments that are less labour-intensive with China continuing to be the dominant global textile material sourcing hub in the future. China's apparel export share has decreased after reaching a peak in 2010 with many other exporting nations taking away market share from China.

Figure 241: China's share of apparel exports to large markets is past its peak



Source: VNDIRECT, UNComtrade

Figure 242: China's rising share of textile imports by key garment exporting nations shows its migration upstream



Source: VNDIRECT, WTO

China's shift away from labour-intensive garment production will leave a sizable void for other exporters like Vietnam to fill

China's T&A industry is expected to keep shifting away from labour-intensive segments (eg: apparel, clothing) due to a surge in average labour wages that have risen by 64% over 2011 – 2017. Therefore, the reduction in apparel production (from 47% to 40% of total industry value in 2015-20 under the 13th Five-Year plan will leave a huge gap (worth around US$23bn, equivalent to 71% of Vietnam's 2017 T&A export value) for other countries (including Vietnam) to fill.

We think that Vietnam is potentially the largest beneficiary from the changes in the Chinese apparel industry, along with India, Bangladesh and Cambodia given relatively low labour costs, and the rapid development of an integrated production chain starting from upstream yarn production all the way to cutting and sewing operations. Vietnam's T&A industry also has a track record of relatively good compliance with international social, environmental and labour safety standards which differentiates it from other major exporters like Bangladesh which has seen a number of garment factory accidents in recent years.

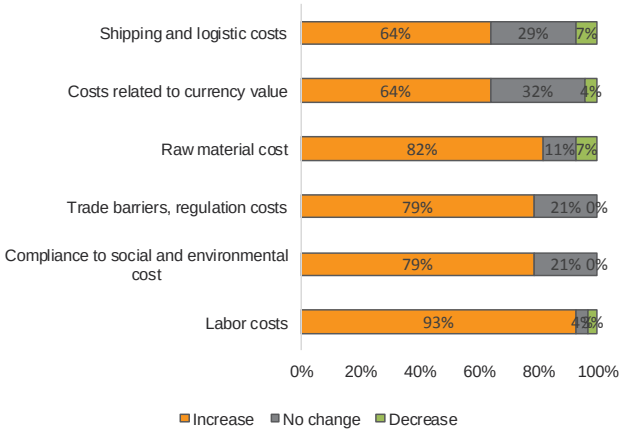
Figure 243: Strength and weakness as a sourcing base

Region	Sourcing Destination	Speed to market	Sourcing cost	Risk of Compliance	Total score
Western Hemisphere	US	5.0	1.5	4.0	**10.5**
	Mexico	4.0	3.0	3.0	**10.0**
	CAFTA-DR	3.5	3.5	3.0	**10.0**
	Colombia	3.0	2.5	3.0	**8.5**
Asia	China	3.0	3.5	3.0	**9.5**
	Vietnam	**3.0**	**4.0**	**3.0**	**10.0**
	Bangladesh	2.0	4.5	1.5	**8.0**
	Indonesia	2.5	3.5	3.0	**9.0**
	India	2.5	3.5	2.5	**8.5**
	Sri Lanka	2.5	3.5	3.0	**9.0**
	Cambodia	2.5	3.5	2.5	**8.5**
Others	AGOA	2.0	3.5	2.5	**8.0**
	Egypt	2.5	3.0	3.0	**8.5**

Notes: 1 is the worst perfomance, 5 is the best performance (compared to average) for each criteria. The scores measure strength and weakness of sourcing countries, survey from US apparel importers.

Source: VNDIRECT

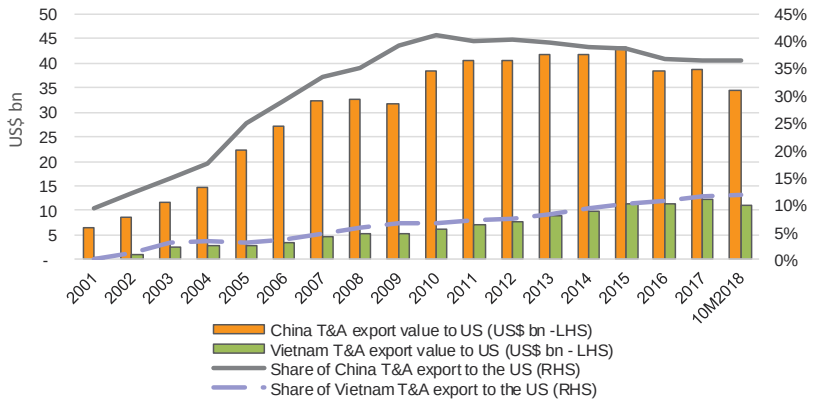
Figure 244: Expected change in sourcing cost by component (results of a survey of US textile buyers - % of respondents)



Note: Sourcing costs are measured on a global basis.

US-China trade tensions yet to affect Chinese T&A exports to US

Figure 245: T&A exports from Vietnam and China to US market

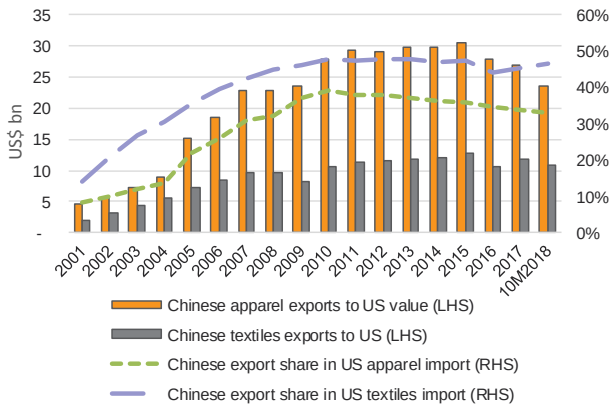


Source: VNDIRECT, OTEXA

On 24 Sep 2018, the US imposed tariffs of 10% on US$200bn worth of Chinese goods including some upstream textile products such as cotton, polyester yarn and related polyester products, with a total import value of around US$3bn. Until now, we have not seen any clear impact on Chinese textile exports to the US in value terms which grew by 12.6% yoy in 10M2018 (vs CAGR 2007-17 of 2.0%) while the Oct 2018 rate was recorded at an even higher 18.1% yoy, reported by OTEXA. The first reason in our opinion is that there is a time lag of 45 - 60 days, which is the amount of time it takes for an order to be manufactured in China and sent to the US. Secondly, we think that buyers rushed to hoard products from China before the expected tariff escalation in January – this is masking the overall weakness in Chinese exports across export categories to the US, not just textiles.

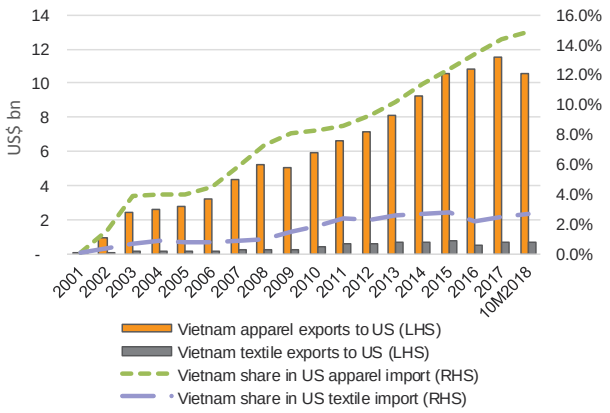
It should be noted that Chinese apparel and clothing have not yet been included in the current $200bn tariff package, while 94.4% of Vietnam's T&A exports to the US are comprised of apparel. Hence, the impact of the US-China trade spat on Vietnam's T&A exports might not be that significant in the near term even though buyers in the US have been preparing to diversify their sourcing mix away from China in anticipation of an escalation in trade tensions to include apparel exports from China.

Figure 246: China T&A exports to US (US$bn) show a migration into upstream products



Source: VNDIRECT, OTEXA

Figure 247: Vietnam T&A exports to US (US$bn) are focused on downstream apparel

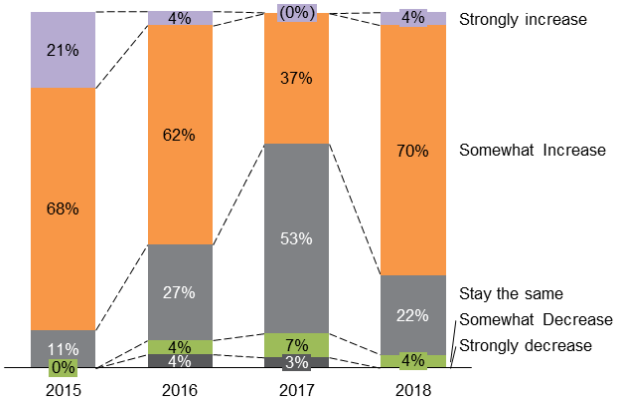


Source: VNDIRECT, OTEXA

US-China trade tensions are bound to improve Vietnam's future T&A export prospects even in the event of a trade deal

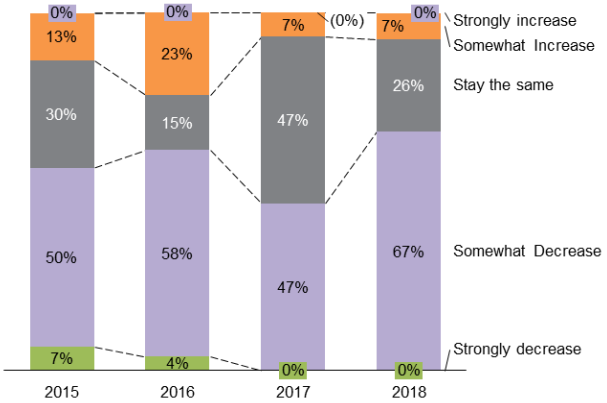
A "China plus one" sourcing strategy has become an imperative for global T&A importers following the recent trade tensions between China and the US. Even if there is a trade deal, global importers will continue to shift their sourcing to Vietnam in anticipation of a resurgence in trade tensions in the future. Below are the results of a survey conducted by the United States Fashion Industry Association (USFIA) regarding the apparel sourcing strategy of T&A importers. It is expected that Vietnam will continue to gain ground against China.

Figure 248: Results of survey of US buyers' planned changes in T&A sourcing (in value terms) from Vietnam



Source: VNDIRECT, USFIA

Figure 249: Results of survey of US buyers' planned changes in T&A sourcing (in value terms) from China



Source: VNDIRECT, USFIA

CPTPP and EVFTA may give Vietnam T&A exports an immediate lift.

Figure 250: Overlap between CPTPP and signed FTAs

Country	% of 2017 Vietnam T&A export value	Overlap with signed FTAs
Japan	11.9%	VJEPA, effective from 2008
Canada	2.1%	
Australia	0.7%	AANZFTA, drop to 0% in 2018
Malaysia	0.4%	
Chile	0.3%	
Mexico	0.3%	
Singapore	0.3%	
New Zealand	0.1%	AANZFTA, drop to 0% in 2018

Source: VNDIRECT, MOIT

After the withdrawal of the US from TPP in 2017, 11 other countries have grouped and formed a new trade deal called CPTPP (with similar rules) which has officially come into effect on 14 Jan 2019 after countries signed up on 3 Aug 2018. CPTPP will immediately eliminate 95-98% of tariff lines and the rest in the next five years. In addition, EVFTA (Vietnam – European Union FTA), which has reached agreement in Oct 2018 and is expected to be signed and made effective by the EC in 1Q2019, will remove 99% of tariff lines on Vietnam exports. Vietnam T&A exports to EU contributes around US$3.8bn or 12.1% of total Vietnam's T&A exports while the similar figure for CPTPP members is US$5.0bn (accounting for 16.1% of total T&A exports). We estimate the tax savings for importers from these tariff exemptions can reach up to US$484m (at the average tariff rate of 10%, after excluding overlaps with previous FTAs), hence potentially raising exports to these destinations.

"Rules of Origin" pose a challenge since the dyeing stage remains a bottleneck in Vietnam due to the environmental norms

It should be noted that these two trade pacts have very strict sets of rules in terms of material usage called "Rules of Origin" for exporters to quality for favourable tariff lines. The requirement of EVTFA is "fabric forward" and for CPTPP, it is called "yarn forward". These rules mean apparel exporters have to source the required materials domestically or from other trade pact member countries.

These rules might cause problems for Vietnamese apparel exporters as they meet 74% of national yarn needs per year through imports, while the dyeing stage is considered a bottleneck since Vietnamese fabric production only satisfies 32% of domestic consumption. Toxic chemical substances used in dyeing fabric require heavy investment

in effluent treatment facilities (from US$2m to US$5m of capex) per dyeing factory, a requirement which favours only foreign-owned or large domestic enterprises. Secondly, local authorities are also reluctant to provide licences for dyeing projects after many environmental scandals in Vietnam in recent years. For instance, in June 2018, Vinh Phuc province authorities proposed that the Prime Minister reject granting an operating licence for a huge dyeing factory with capex of US$350m due to environmental concerns.

Upstream manufacturers and vertically-integrated textile producers are expected to benefit significantly

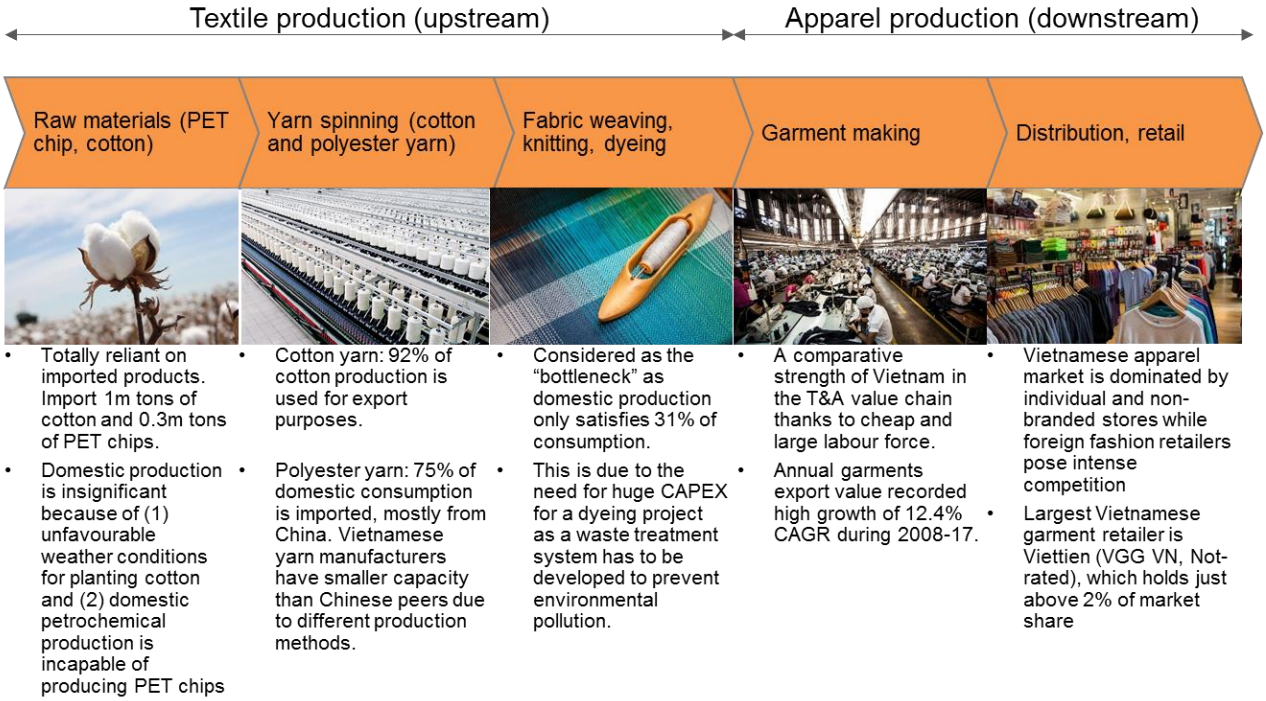
In our opinion, the largest beneficiaries from these trade deals are upstream manufacturers (including yarn and fabric enterprises, such as STK – a polyester yarn manufacturer) or firms that have a comprehensive production chain (such as TCM). This is because Vietnamese exporters will have to start sourcing intermediates closer to home to meet rules of origin requirements. Also, versus downstream exporters that will have to compete with large Chinese garment exporters that are relocating their facilities to Vietnam, upstream players will see an increase in their addressable market opportunity due to this relocation of foreign garment production.

Also, we think that foreign-owned enterprises in Vietnam will benefit the most since the majority of upstream product is manufactured by foreign-owned enterprises (over 70% of yarn exports from Vietnam).

Vietnam's T&A manufacturing capabilities are improving

Production chains are being vertically integrated

Figure 251: Apparel making methods and corresponding gross margin (based on our estimation and observation)

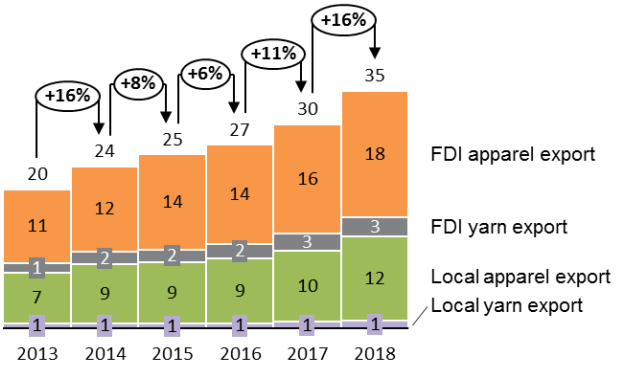


Source: VNDIRECT

Vertical integration is being driven by continuous FDI flows, focusing on upstream processes, to benefit from trade war tensions and trade pacts.

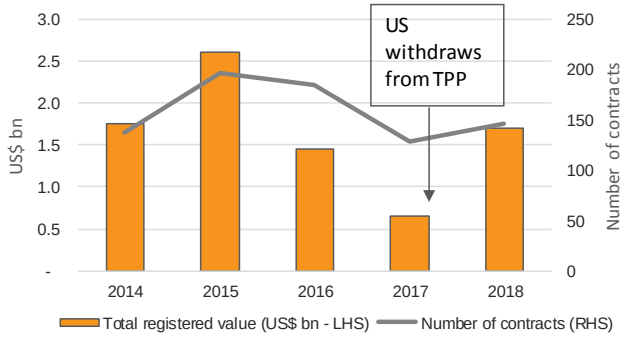
The FDI sector plays a crucial role in Vietnam's T&A industry as it accounts for 70% and 60% of national textiles and apparel exports in term of value, respectively. It recorded a strong growth during 2013-16 with an export value CAGR of 10.9% vs domestic sector export value growth of 8.0% during the period, driven to a large extent by the expected ratification of the Trans Pacific Partnership (TPP). FDI flows into Vietnam's T&A industry paused in 2017, after the withdrawal of US (the largest country) from the TPP and only recovered in 2018 as the CPTPP ratification become imminent.

Figure 252: T&A export value of FDI vs domestic sectors



Source: VNDIRECT, Vietnam Custom

Figure 253: Registered FDI into Vietnam's T&A industry

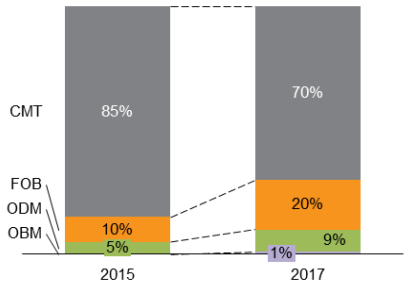


Source: VNDIRECT, VITAS

After successfully negotiating CPTPP and EVFTA, we expect FDI to resume its momentum in the following years, specifically in upstream production since demand for domestic upstream products will be increasingly large thanks to "Rules of Origin". Also, from our perspective, opportunities for investment in the upstream manufacturing segment is expected to be huge. Currently, the Vietnam textile industry has a relatively strong capacity in sewing, and garment and apparel manufacturing, but is relatively weak in manufacturing upstream products (including yarn and fabric) which is capital intensive, hence creating a "bottleneck".

Many Chinese textile manufacturers have started to relocate their factories from China to Vietnam due to concerns over the US-China trade war. In our view, this might help to strengthen the textile production chain of Vietnam without creating severe competition since (1) the potential market is large as explained above, (2) Chinese yarn manufacturers provide a wide range of products (including advanced ones) which are different from local products hence avoiding direct competition. Therefore, local apparel exporters will be able to source locally instead of importing, hence reducing logistic costs and order lead times for imported materials (10 - 20 days on average).

Figure 254: Vietnam's garment production mix is improving (% export revenue by type)



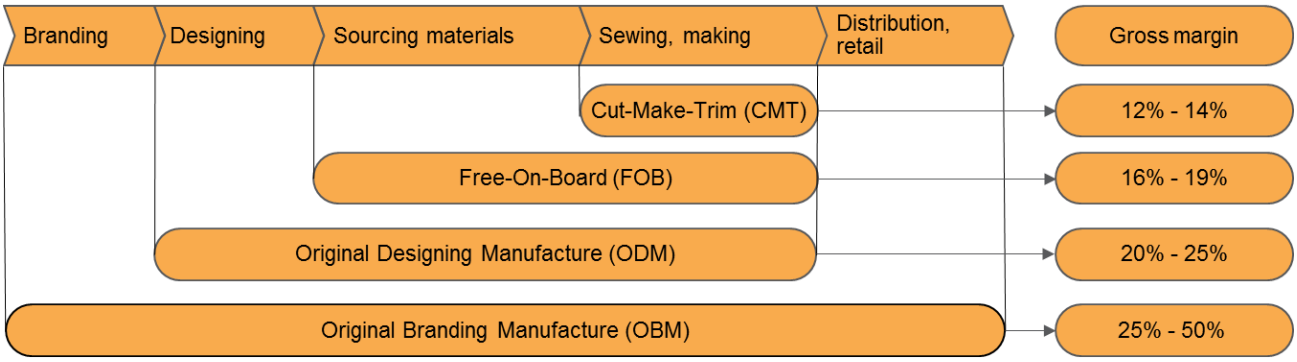
Source: VNDIRECT, VITAS

Gradual shift towards high value-added apparel production

We are seeing manufacturers upgrading their production from Cut–Make-Trim (CMT) towards Free-On-Board (FOB) due to the increasingly integrated value chain of the Vietnamese T&A industry and the rising credibility of Vietnamese apparel exporters amongst global clothing and brand owners and retailers. The first impact of this change is that orders will generate an additional 2% of gross margin (FOB vs CMT) on average as they will have come with the added responsibility of material sourcing. Secondly, this will help to improve the competitiveness of the Vietnamese apparel industry, since Bangladesh (a direct competitor as an apparel sourcing location) has

around 20% lower labour costs than Vietnam but focuses more on CMT orders.

Figure 255: Garment production methods and gross margin (based on our observations and T&A enterprises' disclosure)



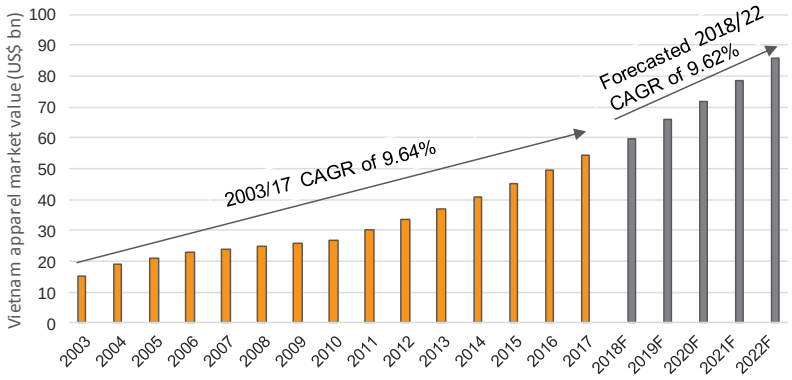
Source: VNDIRECT

Domestic apparel market not attractive currently due to the small size and fierce competition but constitutes long-term opportunity

The domestic apparel market carries huge, untapped potential

The Vietnam apparel market has grown at a 2003-17 value CAGR of 9.6% to reach VND54tr in 2017 thanks to rising disposal income which is triggering discretionary spending, especially on branded items. According to Euromonitor, this growth rate is expected to be sustained for the next five years, potentially making Vietnam's apparel market one of the fastest growing in the world, comparing against a global forecasted 2017-2022 CAGR of around 1.3%.

Figure 256: High growth of Vietnam apparel market is expected to continue



Source: VNDIRECT, Euromonitor

Fiercely competitive domestic market, dominated by individual stores and stimulated by entrance of foreign fashion giants. Vietnam's apparel market is extremely fragmented with the dominance of individual and non-branded stores that account for 89.6% of retail value in 2017 while the largest retailer is Viettien Garment (VGG VN, Not-rated) which holds just over 2.3% of market share in 2017. The competition has also heated up significantly with the entry of several international fashion brands including Zara and H&M which have proven to be popular with Vietnamese consumers. In 1H2018, Zara realised revenue of VND950bn from its Vietnam operations, in comparison with VGG's FY17 revenue of VND1,002bn.

Overall, we think that the domestic pie is still small and might not be worth fighting for in the short term. In order to compete with foreign fashion retailers, Vietnamese garment enterprises, who are

mostly currently at the CMT and FOB space, need to move up to the OBM method, which will take time and require heavy investments.

Even though we see Vietnamese consumers increasingly trading up to branded clothes to improve their status and personal image, this will work largely to the benefit of international fashion brands, rather than expanding the overall market. In sum, we think that the domestic market might not be worth fighting for in the short term. This is because (1) the domestic apparel market is very small (FY17 value of around US$2.4bn vs total apparel exports of US$26.1bn) and (2) Vietnamese firms are disadvantaged in the domestic market versus new foreign entrants owing to weaker brand equity, quality and design.

Textiles sector Stock picks: We like TCM and STK and put MSH on our watch list

We like textile players that meet the following criteria: (1) net beneficiaries of FTAs, CPTPP and trade war due to the right export market footprint and a midstream or upstream value chain presence; and (2) have plans to either invest in a new range of products or raise existing production capacity. Therefore, our stock picks are Thanh Cong Textiles Garment Investment Trading **(TCM VN, ADD, TP:VND26,000)** and Century Synthetic Fiber Corp **(STK VN, ADD, TP: VND24,600)**. We also put **Song Hong Garment (MSH, Not rated)** on our watch list.

TCM is the only T&A enterprise that has a fully vertically integrated production chain from yarn production to garment making. We expect TCM to be a net beneficiary of CPTPP and EVFTA as they already have in-house production facilities for both fabric as well as yarn, hence satisfying the Rule of Origin criteria in these two trade pacts. Secondly, TCM will invest in a dyeing factory with a capex of around US$10m in FY19F that is expected to add capacity of 3,000m of fabric/day hence reducing outsourcing expenses and potentially raising gross margins by around 1%.

STK will strongly benefit from trade war and CPTPP. Chinese polyester yarn and related products have now been subjected to a 10% import tariff, on average, in the US market which has made Vietnamese yarn relatively more competitive. Secondly, CPTPP (with yarn-forward rules) will require local exporters to source yarn domestically or from CPTPP member countries. Therefore we expect increasingly large orders coming from domestic downstream garment and fabric producers as well as from other countries which do not have a comparative advantage in yarn production, such as Mexico. Finally, Trang Bang 5 factory will raise STK's total yarn production capacity by 5.5% to 63,300 tons of DTY after expected commissioning in 1Q2019.

MSH is one of the largest apparel exporters in Vietnam with a focus on supplying large upper-mid market global fashion brands. According to MSH's management, the company will see an increase in FOB revenue contribution from existing customers such as Columbia, Calvin Klein, Tommy Hilfiger, etc which carries higher margins than CMT orders. In addition, a new factory (Song Hong 10) which will be built in April 2019 with a capex of US$16m and go into operation in the beginning of 2020, raising total capacity by 20%, per management. Also, MSH has a very attractive dividend policy with expected dividend in upcoming years of VND3,500/ share – VND4,500/share (equivalent to a dividend yield of 9.8% annually based on the current share price).

Figure 257: Textile & Apparel peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
VINATEX	VGT	228.5	17.7%	4.1%	2.3%	6.2%	1.3	10.9	0.9
Viet Tien Garment	VGG	95.8	4.9%	1.3%	9.3%	26.6%	0.1	5.2	1.3
Song Hong Gament	MSH	84.3	167.3%	32.4%	13.7%	38.0%	0.7	5.9	1.9
Phong Phu Corp.	PPH	59.2	1.1%	0.6%	3.5%	11.8%	2.0	7.0	0.9
Thanh Cong Textile Garment	TCM	51.3	85.5%	85.5%	7.7%	20.7%	1.0	5.2	1.0
Century Synthetic Fiber	STK	43.6	162.8%	162.8%	7.8%	19.8%	1.1	6.3	1.2
TNG Invm't and Trading	TNG	35.4	38.0%	-6.3%	6.2%	23.4%	2.1	5.2	1.1
Everpia	EVE	25.9	191.4%	40.3%	5.7%	8.6%	0.5	7.6	0.6
Garment 10 Corporation	M10	23.8	23.0%	-33.6%	4.1%	15.5%	1.2	5.0	1.6
Saigon Garment	GMC	22.9	183.0%	51.4%	10.8%	34.6%	1.2	5.2	0.8
Viet Thang Corp.	TVT	22.6	42.8%	9.0%	6.1%	14.2%	1.6	9.3	1.4
Hoa Tho Textile - Garment	HTG	20.8	-10.6%	-2.9%	5.5%	24.7%	2.4	4.4	1.2
Average		**60.1**	**75.6%**	**28.7%**	**6.9%**	**20.3%**	**1.3**	**6.4**	**1.2**
Median		**40.0**	**40.4%**	**6.6%**	**6.2%**	**20.3%**	**1.2**	**5.5**	**1.1**

Source: VNDIRECT, Fiinpro

THANH CONG TEXTILE GARMENT INVESTMENT TRADING JSC (TCM)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND22,250	VND26,000	2.25%	ADD	TEXTILES

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019
Vũ Minh Tú
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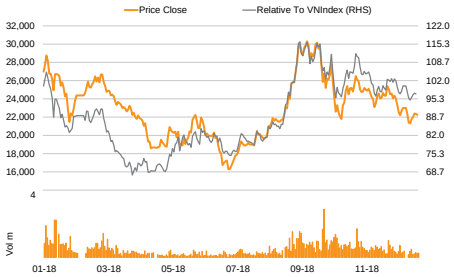
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	30,300
52w low (VND)	16,300
3m Avg daily volume (shares)	755,858
3m Avg daily value (VNDmn)	19,604
Market cap (VNDbn)	1,261
Outstanding shares (m)	56.1
Free float (%)	49
TTM P/E (x)	5.2
Current P/B (x)	1.0

Ownership

E-land Asia Holdings Pte., Ltd Singapore	43.3%
VCBF	2.6%
Lê Quốc Hưng	1.9%
Others	52.20%

Source: VNDIRECT

We expect TCM's recurring earnings to surge 19.8% yoy in FY19 on the back of 10.1% yoy sales growth, supported by the newly implemented CPTPP trade pact.

The only vertically-integrated textile manufacturer in Vietnam. TCM owns a near-complete production chain, including yarn, fabric and garments, allowing it to reduce its reliance on imported materials (yarn, fabric). The majority of intermediates used for making garments (annual capacity of 27m units), are insourced from two yarn factories (11,000 tonnes of cotton yarn) and two fabric factories (capacity of 15,000 tonnes of knitted fabric and 9.6m metres of woven fabric).

We expect FY19F revenue to rise by 10.1% yoy to reach VND3,992bn, with a slight gross margin expansion of 10bp to touch 17.6%. FY19F EAT is estimated to touch VND228bn (+2.1% yoy) since TCM will not realize financial gains this year (VND53bn from land sales in FY18F).

Sears's bankruptcy will dent FY18F and FY19F earnings. TCM's management disclosed that a provision of VND30bn will be booked in FY18F for Sears' receivables (total receivables amount to VND95bn) and the rest (of around 31bn, in our estimation) will be booked in FY19F. We haircut our FY19F forecasted revenue by a further VND250bn to account for lost revenue from Sears' orders.

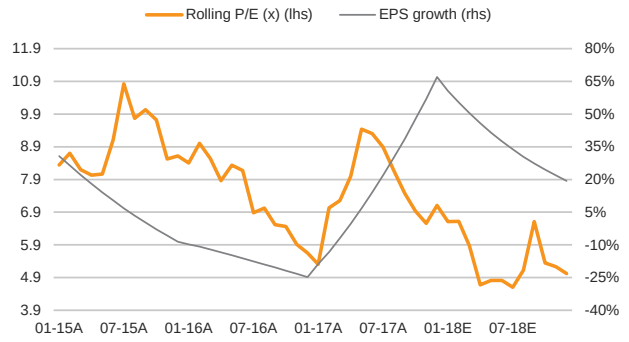
EVFTA is expected to confer a competitive advantage to TCM due to "Fabric forward Rules of Origin", which require garment exporters to use domestic fabric in making garments to qualify for the import tax waiver. TCM is likely to benefit greatly since it has in-house fabric production capabilities and 15% of garment revenue already comes from exports to the EU market.

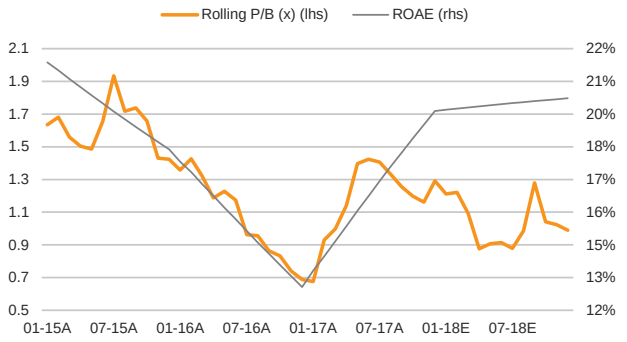
Maintain ADD rating as stronger growth prospects outweigh potential impact of Sears bankruptcy. We base our valuation on FY2019F recurring EPS of VND5,039/share and a target TTM P/E of 5.3x to our forecasted core earnings for the year, based on the peer average TTM P/E. We apply a haircut of 2.2% to our target price valuation to account for the Sears receivables risk and arrive at a target price of VND26,000/share.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	3,071	3,209	3,627	3,992
Revenue growth	10.0%	4.5%	13.0%	10.1%
Gross margin	13.6%	15.7%	17.5%	17.6%
EBITDA margin	8.4%	12.1%	12.0%	10.9%
Net profit (bn)	116	193	223	228
Net profit growth	(24.8%)	67.1%	15.4%	2.1%
Recurring profit growth	(25.6%)	42.1%	40.4%	19.8%
Basic EPS	2,246	3,753	4,202	4,204
Adjusted EPS	1,572	3,195	3,572	3,573
BVPS	18,461	20,635	22,614	25,688
ROAE	12.9%	19.6%	19.5%	17.4%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	3,209	3,627	3,992
Cost of sales	(2,706)	(2,994)	(3,288)
Gen & admin expenses	(148)	(200)	(218)
Selling expenses	(112)	(134)	(148)
Operating profit	**243**	**299**	**338**
Operating EBITDA	349	401	443
Depreciation and amortisation	**(106)**	**(102)**	**(106)**
Operating EBIT	**243**	**299**	**338**
Interest income	26	33	44
Financial expense	(71)	(101)	(92)
Net other income	42	53	0
Income from associates & JVs	(5)	(5)	(5)
Pre-tax profit	**235**	**279**	**285**
Tax expense	(43)	(56)	(57)
Minority interest	1	0	0
Net profit	**193**	**223**	**228**
Adj. net profit to ordinary	165	190	194
Ordinary dividends	(33)	(27)	(27)
Retained earnings	**161**	**196**	**201**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	130	152	250
Short term investments	151	201	201
Accounts receivables	528	449	430
Inventories	806	940	1,034
Other current assets	44	95	157
Total current assets	**1,659**	**1,837**	**2,072**
Fixed assets	1,197	1,172	1,103
Total investments	101	1	1
Other long-term assets	131	131	131
Total assets	**3,088**	**3,141**	**3,307**
Short-term debt	969	920	913
Accounts payable	292	269	295
Other current liabilities	418	366	366
Total current liabilities	**1,679**	**1,554**	**1,573**
Total long-term debt	294	308	289
Other liabilities	44	44	44
Share capital	517	542	542
Retained earnings reserve	299	429	563
Shareholders' equity	**1,064**	**1,226**	**1,393**
Minority interest	8	8	8
Total liabilities & equity	**3,088**	**3,141**	**3,307**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**235**	**279**	**285**
Depreciation & amortisation	106	102	106
Tax paid	(43)	(56)	(57)
Other adjustments	(35)	(166)	(13)
Change in working capital	**23**	**(131)**	**(109)**
Cash flow from operations	**286**	**29**	**212**
Capex	(93)	(100)	(60)
Proceeds from assets sales	82	104	0
Others	(109)	50	0
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(121)**	**54**	**(60)**
New share issuance	0	0	0
Shares buyback	0	0	0
Net borrowings	(48)	(34)	(27)
Other financing cash flow	(50)	0	0
Dividends paid	(33)	(27)	(27)
Cash flow from financing activities	**(131)**	**(61)**	**(54)**
Cash and equivalents at beginning of period	96	130	152
Total cash generated	**34**	**22**	**98**
Cash and equivalents at the end of period	130	152	250

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	6.0%	6.2%	5.7%
Asset turnover	1.09	1.16	1.24
ROAA	6.5%	7.2%	7.1%
Avg assets/avg equity	3.00	2.72	2.46
ROAE	19.6%	19.5%	17.4%
Efficiency			
Days account receivable	49.4	41.1	41.1
Days inventory	109	115	115
Days creditor	39.4	32.8	32.8
Fixed asset turnover	2.66	3.06	3.51
ROIC	8.3%	9.1%	8.8%
Liquidity			
Current ratio	0.99	1.18	1.32
Quick ratio	0.51	0.58	0.66
Cash ratio	0.17	0.23	0.29
Cash cycle	119	123	123
Growth rate (yoy)			
Revenue growth	4.5%	13.0%	10.1%
Operating profit growth	36.1%	22.9%	13.0%
Net profit growth	67.1%	15.4%	2.1%
EPS growth	67.1%	12.0%	0.0%
Share value			
Basic EPS (VND)	3,753	4,202	4,204
BVPS (VND)	20,635	22,614	25,688

Source: VNDIRECT

CENTURY SYNTHETIC FIBER CORP (STK)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND17,100	VND24,600	4.68%	ADD	TEXTILES

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Negative Neutral Positive

Valuation

Negative Neutral Positive

11 January 2019
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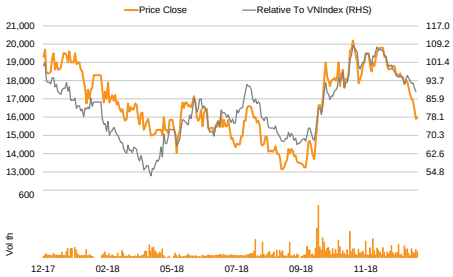
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	20,200
52w low (VND)	13,150
3m Avg daily volume (shares)	63,630
3m Avg daily value (VNDmn)	1,180
Market cap (VNDbn)	953
Outstanding shares (m)	59.6
Free float (%)	50
TTM P/E (x)	6.3
Current P/B (x)	1.2

Ownership

Huong Viet Investment Consultant Corporation	20.2%
Dang Trieu Hoa	13.9%
Dang My Linh	8.5%
Dang Huong Cuong	8.5%
Vietnam Holding Ltd	4.7%
Others	44.2%

Source: VNDIRECT

FY19F should be an outstanding year for STK with commissioning of the TB5 yarn factory in 1Q19F which will lift production capacity by 5.5% and a continued shift into recycled yarn that will raise blended gross margins. The CPTPP trade pact and the US-China trade war will also benefit the company.

Second-largest synthetic fiber manufacturer in Vietnam. STK's current total capacity of 60,000 tons of yarn, makes it the largest Vietnamese synthetic yarn manufacturer, and it is ranked second-largest in the domestic market, after Taiwanese firm, Formosa (1326 TT, Not rated). STK produces Fully-Drawn Yarn (FDY), Drawn-Textured Yarn (DTY) and recycled yarn, which are used as key input materials for the textile and apparel industry.

FY19F EAT is projected to surge 33.6% yoy on the back of 13.0% yoy revenue growth and margin expansion. Topline growth will be driven by a rise in ASP of 7.6% yoy and 5.1% yoy volume growth. We also expect gross margin to expand by 80bp to reach 14.8% due to a continuous shift into high-margin recycled yarn, which is expected to contribute 17% of FY19F revenue (up from 14% in FY18F).

STK is a direct beneficiary of CPTPP and the US-China trade war. With the tariffs imposed by the US on Chinese goods extended to US$200bn worth of imports, including synthetic fiber and related products, Vietnamese yarn is now more competitive. In addition, "yarn forward rules of origin" under CPTPP will require garment exporters to source yarn domestically which should buoy STK's order volumes.

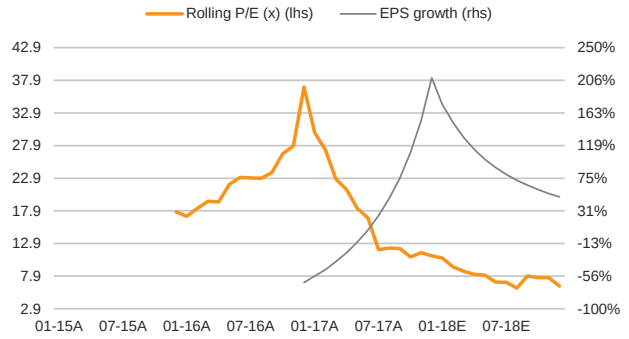
Trang Bang 5 (TB5) project's commercial operations will start in 1Q19F. TB5, which has a designed capacity of 3,300 tons of DTY and 1,500 tons of recycled chips (used to produce recycled yarn), is currently in the trial phase and will launch commercial operation in 1Q2019 with an expected utilisation rate of 90% for 2019. The commissioning of this facility could be a positive share price catalyst.

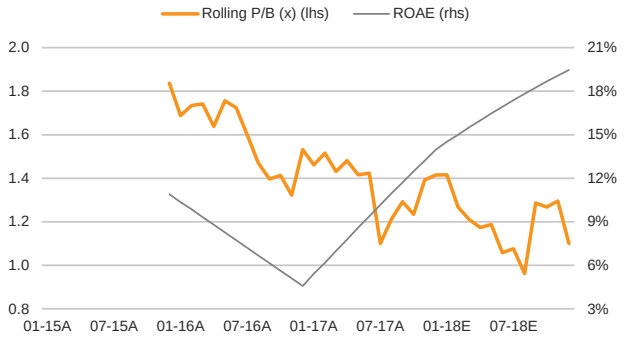
We maintain an ADD rating with target price of VND24,600 per share, based on a target P/E of 6.9x (in line with the average TTM P/E of regional yarn manufacturers) and our FY19F forecasted EPS of VND3,560.

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	1,358	1,989	2,362	2,670
Revenue growth	31.2%	46.4%	18.7%	13.0%
Gross margin	9.5%	10.9%	14.0%	14.8%
EBITDA margin	12.5%	14.1%	16.0%	16.8%
Net profit (bn)	29	100	174	233
Net profit growth	(59.6%)	246.7%	74.0%	33.6%
Recurring profit growth	(54.2%)	248.0%	74.2%	33.9%
Basic EPS	577	1,764	2,905	3,560
Adjusted EPS	577	1,764	2,905	3,560
BVPS	12,998	13,002	15,251	16,655
ROAE	4.2%	13.6%	20.6%	22.2%

Source: VNDIRECT

Valuation





Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	1,989	2,362	2,670
Cost of sales	(1,773)	(2,031)	(2,275)
Gen & admin expenses	(59)	(70)	(79)
Selling expenses	(32)	(38)	(43)
Operating profit	**126**	**224**	**274**
Operating EBITDA	274	373	433
Depreciation and amortisation	**(148)**	**(149)**	**(159)**
Operating EBIT	**126**	**224**	**274**
Interest income	8	6	16
Financial expense	(30)	(29)	(23)
Net other income	1	2	2
Income from associates & JVs	0	0	1
Pre-tax profit	**105**	**202**	**270**
Tax expense	(5)	(28)	(37)
Minority interest	0	0	0
Net profit	**100**	**174**	**233**
Adj. net profit to ordinary	100	174	233
Ordinary dividends	(16)	(48)	(35)
Retained earnings	**84**	**126**	**197**

Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	117	320	520
Short term investments	0	0	0
Accounts receivables	63	59	66
Inventories	399	400	452
Other current assets	35	57	48
Total current assets	**613**	**836**	**1,087**
Fixed assets	1,209	1,181	1,030
Total investments	156	172	192
Other long-term assets	0	0	0
Total assets	**1,979**	**2,190**	**2,309**
Short-term debt	341	336	380
Accounts payable	307	352	385
Other current liabilities	84	72	81
Total current liabilities	**732**	**759**	**846**
Total long-term debt	467	516	285
Other liabilities	0	0	0
Share capital	599	599	707
Retained earnings reserve	143	269	424
Shareholders' equity	**779**	**914**	**1,178**
Minority interest			
Total liabilities & equity	**1,979**	**2,190**	**2,309**

Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
Pretax profit	**105**	**202**	**270**
Depreciation & amortisation	148	149	159
Tax paid	(5)	(28)	(37)
Other adjustments	(6)	(6)	(20)
Change in working capital	**63**	**10**	**(9)**
Cash flow from operations	**306**	**328**	**362**
Capex	(5)	(121)	(8)
Proceeds from assets sales	0	0	0
Others	(22)	0	0
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(27)**	**(121)**	**(8)**
New share issuance	0	0	66
Shares buyback	0	0	0
Net borrowings	(233)	44	(185)
Other financing cash flow	0	0	0
Dividends paid	(16)	(48)	(35)
Cash flow from financing activities	**(249)**	**(4)**	**(155)**
Cash and equivalents at beginning of period	87	117	320
Total cash generated	**30**	**204**	**200**
Cash and equivalents at the end of period	117	320	520

Key ratios

	12-17A	12-18E	12-19E
Dupont			
Net profit margin	5.0%	7.4%	8.7%
Asset turnover	0.99	1.13	1.19
ROAA	5.0%	8.4%	10.3%
Avg assets/avg equity	2.71	2.46	2.15
ROAE	13.6%	20.6%	22.2%
Efficiency			
Days account receivable	10.4	8.1	8.1
Days inventory	82.2	71.9	72.6
Days creditor	63.3	63.2	61.8
Fixed asset turnover	1.55	1.98	2.41
ROIC	6.3%	9.9%	12.6%
Liquidity			
Current ratio	0.84	1.10	1.28
Quick ratio	0.29	0.57	0.75
Cash ratio	0.16	0.42	0.61
Cash cycle	29.4	16.8	18.9
Growth rate (yoy)			
Revenue growth	46.4%	18.7%	13.0%
Operating profit growth	117.2%	77.2%	22.4%
Net profit growth	246.7%	74.0%	33.6%
EPS growth	205.7%	64.7%	22.5%
Share value			
Basic EPS (VND)	1,764	2,905	3,560
BVPS (VND)	13,002	15,251	16,655

Source: VNDIRECT

SONG HONG GARMENT JSC (MSH)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND40,700	N/A	9.80%	NOT RATED	TEXTILES

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11January 2019
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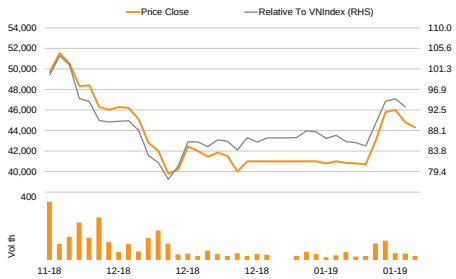
Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	51,538
52w low (VND)	39,800
3m Avg daily volume (shares)	0.08
3m Avg daily value (VNDmn)	3,659
Market cap (VNDbn)	1,938
Outstanding shares (m)	47.6
Free float (%)	46.1
TTM P/E (x)	5.9
Current P/B (x)	1.9

Ownership

Bui Duc Thinh	21.6%
FPTS	13.6%
Bui Viet Quang	10.9%
Nguyen Thi Dao	7.7%
Others	46.1%

Source: VNDIRECT

We visited MSH and its factories in Nam Dinh province recently and here are some key takeaways from the meeting.

MSH is one of the largest Vietnamese garment exporters that focuses on contract manufacturing for upper-mid market global clothing brands including Calvin Klein, Tommy Hilfiger, Karl Lagerfeld, etc. with annual capacity of 60m units, supported by 155 sewing lines and over 9000 workers. MSH also owns a domestic bedding brand called Song Hong that holds a 27% share of the Vietnamese branded bedding market.

2018 prelim results were strong with sales growth of 19% and a 68% jump in earnings; margins expanded on improved sales mix. Revenue of VND3,950bn (+19% yoy) of which FOB accounted for VND2,714bn, CMT accounted for VND828bn while bedding contributed VND400bn. EAT is estimated at between VND330bn to VND335bn (+64.7% to +67.5% yoy). Gross margin touched 19.3% (+183bps yoy) due to an increase in revenue contribution from FOB production (which has higher gross margins) from 61% in FY17 to 69% of total revenue in FY18

MSH will continue to raise FOB revenue contribution, to touch 100% of garment export revenue by 2024. Management guides for FY19 revenue of around VND4,356bn (+11% yoy), within which FOB revenue is expected to rise 22.9% yoy to reach VND3,335bn while CMT revenue is expected to fall by 25% yoy.

FOB penetration to be focused on large client accounts, including Haddad (distributor of Converse, Nike), G-III (distributing Calvin Klein, Karl Lagerfeld) and Columbia. Ralph Lauren is a potential customer, according to management. MSH has signed an FOB contract worth US$40m with Hong-Kong based Luen Thai for exporting garments that will be phased over 4 years and should help increase blended margins, per management.

Expansion plan in 2020 to lift capacity by 20%. Song Hong 10 factory (SH 10) involves a capex of US$16m (financed 70% by debt and 30% by equity). The factory will have 40 sewing lines and employ 2000 – 2500 workers, raising total production capacity by around 20%. Construction is expected to break ground in April 2019 and operate at the start of 2020.

Attractive dividend payout. The company expects to pay a dividend of VND3,500/share – VND4,500/share (equivalent to a dividend yield of 7.9% - 10.1%) per year over the next few years. There are no capital-raising plans on the anvil, per management.

Financial summary (VND)	12-15A	12-16A	12-17A
Net revenue (bn)	2,548	2,992	3,282
Revenue growth		17.4%	9.7%
Gross margin	18.1%	16.6%	17.2%
EBITDA margin	11.6%	11.9%	11.6%
Net profit (bn)	160	185	200
Net profit growth	12.6%	15.8%	8.4%
Recurring profit growth	9.4%	15.8%	8.4%
Basic EPS	10,138	8,153	8,656
Adjusted EPS	7,436	5,689	6,388
BVPS	27,422	28,793	31,713
ROAE	28.1%	29.0%	28.5%

Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	2,548	2,992	3,282
Cost of sales	(2,087)	(2,496)	(2,718)
Gen & admin expenses	(125)	(169)	(188)
Selling expenses	(108)	(132)	(151)
Operating profit	**228**	**195**	**225**
Operating EBITDA	297	298	339
Depreciation and amortisation	**(69)**	**(103)**	**(114)**
Operating EBIT	**228**	**195**	**225**
Interest income	50	55	58
Financial expense	(80)	(32)	(49)
Net other income	2	(3)	(2)
Income from associates & JVs	0	0	0
Pre-tax profit	**200**	**214**	**231**
Tax expense	(40)	(29)	(31)
Minority interest	0	0	0
Net profit	**160**	**185**	**200**
Adj. net profit to ordinary	160	185	200
Ordinary dividends	(68)	(130)	(108)
Retained earnings	**92**	**54**	**92**

Balance sheet

(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	89	47	344
Short term investments	470	469	302
Accounts receivables	300	403	487
Inventories	325	413	534
Other current assets	46	28	8
Total current assets	**1,231**	**1,360**	**1,675**
Fixed assets	630	691	648
Total investments	0	50	0
Other long-term assets	75	91	58
Total assets	**1,937**	**2,192**	**2,381**
Short-term debt	406	516	723
Accounts payable	177	187	152
Other current liabilities	438	543	558
Total current liabilities	**1,022**	**1,245**	**1,433**
Total long-term debt	293	294	192
Other liabilities	0	0	0
Share capital	227	227	238
Retained earnings reserve	370	353	391
Shareholders' equity	**622**	**653**	**755**
Minority interest	0	0	0
Total liabilities & equity	**1,937**	**2,192**	**2,381**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**200**	**214**	**231**
Depreciation & amortisation	69	103	114
Tax paid	(60)	(86)	(74)
Other adjustments	6	(27)	(9)
Change in working capital	**62**	**(53)**	**(118)**
Cash flow from operations	**277**	**153**	**145**
Capex	(256)	(159)	(119)
Proceeds from assets sales	(106)	(48)	222
Others	30	39	42
Other non-current assets changes	0	0	0
Cash flow from investing activities	**(332)**	**(168)**	**145**
New share issuance	5	0	11
Shares buyback	0	0	0
Net borrowings	109	103	105
Other financing cash flow			
Dividends paid	(68)	(130)	(108)
Cash flow from financing activities	**46**	**(28)**	**8**
Cash and equivalents at beginning of period	99	89	47
Total cash generated	**(9)**	**(43)**	**297**
Cash and equivalents at the end of period	89	47	344

Key ratios

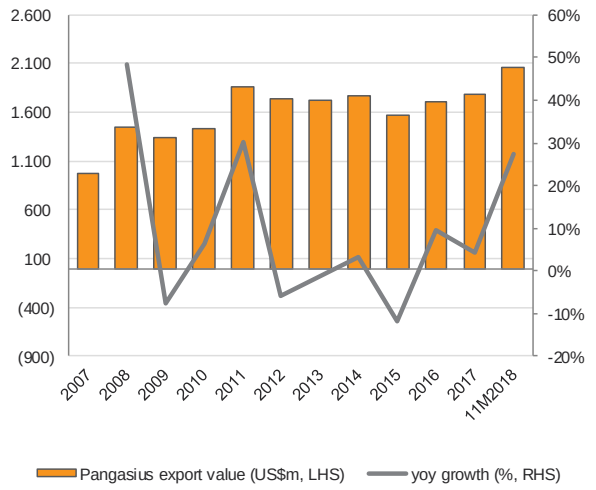
	12-15A	12-16A	12-17A
Dupont			
Net profit margin	6.3%	6.2%	6.1%
Asset turnover	1.45	1.45	1.44
ROAA	9.1%	9.0%	8.8%
Avg assets/avg equity	3.08	3.24	3.25
ROAE	28.1%	29.0%	28.5%
Efficiency			
Days account receivable	41.2	47.0	50.3
Days inventory	56.9	60.6	71.6
Days creditor	31.0	27.4	20.5
Fixed asset turnover	4.88	4.53	4.90
ROIC	12.1%	12.6%	12.0%
Liquidity			
Current ratio	1.20	1.09	1.17
Quick ratio	0.89	0.76	0.80
Cash ratio	0.55	0.41	0.45
Cash cycle	67	80	101
Growth rate (yoy)			
Revenue growth		17.4%	9.7%
Operating profit growth	9.4%	(14.8%)	15.7%
Net profit growth	12.6%	15.8%	8.4%
EPS growth		(19.6%)	6.2%
Share value			
Basic EPS (VND)	10,138	8,153	8,656
BVPS (VND)	27,422	28,793	31,713

FISHERY: ANOTHER GOOD YEAR AHEAD

2018 Review: Setting new export records

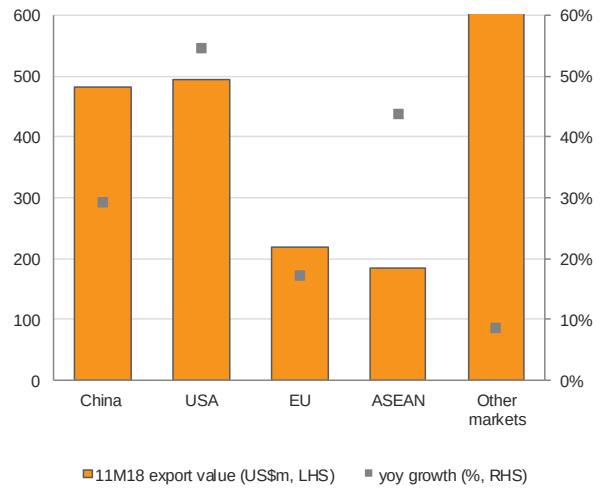
Pangasius export value to major markets witnessed impressive growth

Figure 258: Impressive growth in 2018 export value



Source: VNDIRECT, VASEP

Figure 259: Growth was supported by strong performance of major export markets

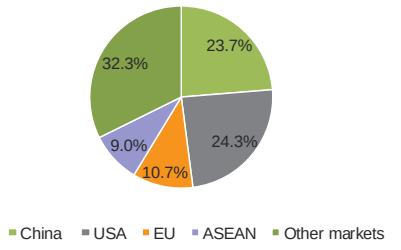


Source: VNDIRECT, VASEP

The Ministry of Agriculture and Rural Development (MARD) expects pangasius export value in 2018 to have reached an all-time high of US$2.2bn (+23% yoy), which looks very reasonable given that the year-to-date export value already reached US$2.04bn in 11M18 (+26.3% yoy). The sector experienced strong growth in major markets such as China (+29.3% yoy), the US (+54.6% yoy), ASEAN countries (+43.7% yoy) and a significant recovery in the EU market (+17.1% yoy) after many consecutive years of negative growth.

Export value spike resulted from a surge in selling price and the increasing contribution of high-value products

Figure 260: Pangasius export share in 11M18 by major market



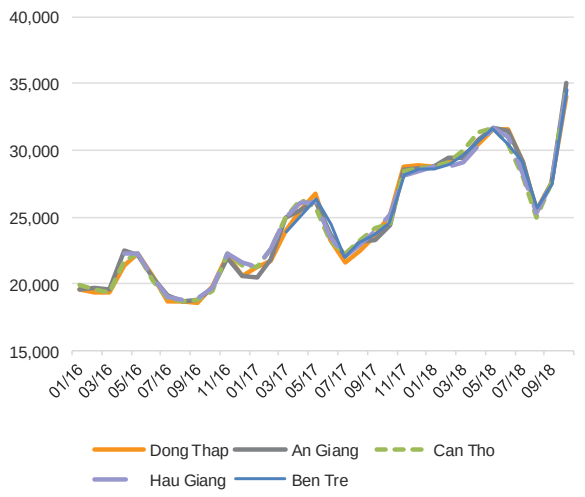
Source: VASEP

The main reason for the surge in pangasius export value was the surge in raw fish prices on top of a shortage in supply amidst robust demand. According to MARD, in 10M18, the domestic supply of pangasius (raw fish) reached 1.1m tonnes, up 7.2% yoy but was still insufficient to meet export demand, hence pushing raw fish prices up 20-30% compared to the same period last year.

High export prices also discourage farmers from retaining fish to produce fingerlings, leading to a further supply shortage of fingerlings. This, combined with the increase in fish feed prices (+15-25% yoy, as at Oct 2018, according to Agromonitor), has raised the cost of production and lifted raw fish prices and, consequently, export prices.

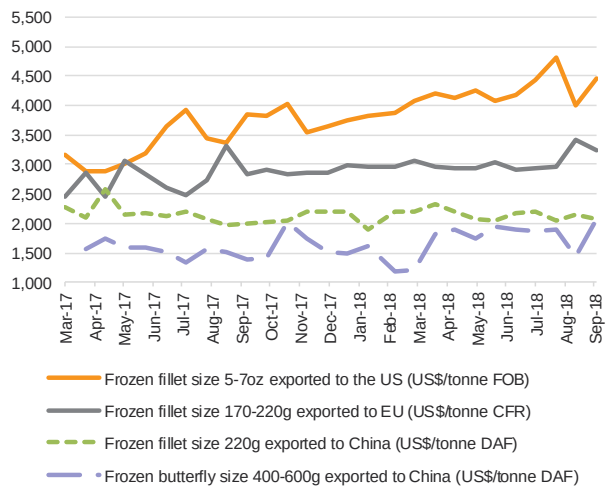
In addition, according to the Chairman of the Vietnam Association of Seafood Exporters and Producers (VASEP), rising exports of high-value products (such as ready-to-cook products) also contributed to the increase in export value of pangasius products, especially in the EU markets where Vietnamese companies previously focused on using competitive pricing strategies to boost market penetration.

Figure 261: Prices of pangasius (raw fish) size 700-900g in the Mekong Delta, by province (VND/kg)



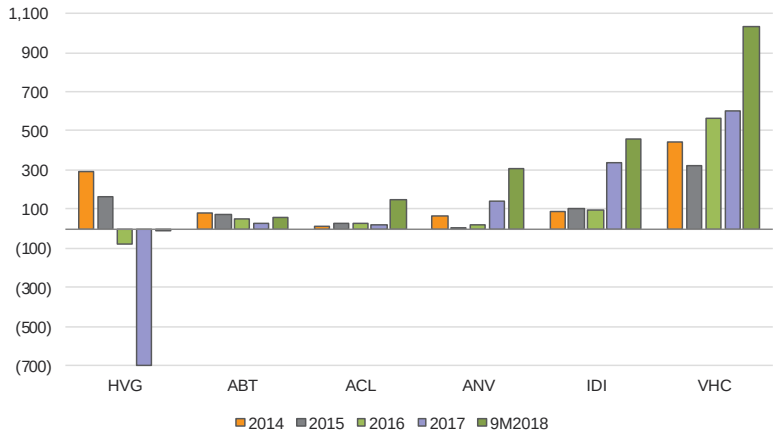
Source: VNDIRECT, AGROMONITOR

Figure 262: Export prices of Vietnamese pangasius to some markets



Source: VNDIRECT, AGROMONITOR

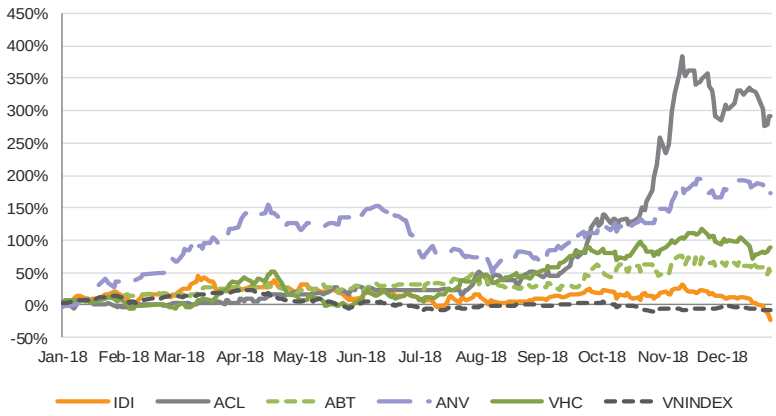
Figure 263: Net profit of major pangasius exporters saw impressive growth in 9M2018 thanks to favourable market conditions (VNDbn)



Source: VNDIRECT, Stoxplus

Pangasius exporters' stocks outperformed the VN-INDEX. Stock prices of pangasius exporters were among the top gainers in 2018. Many stocks set new all-time-highs such as VHC, ANV and ACL.

Figure 264: Pangasius exporters' stocks outperformed the VN-INDEX in 2018



Source: VNDIRECT, BLOOMBERG

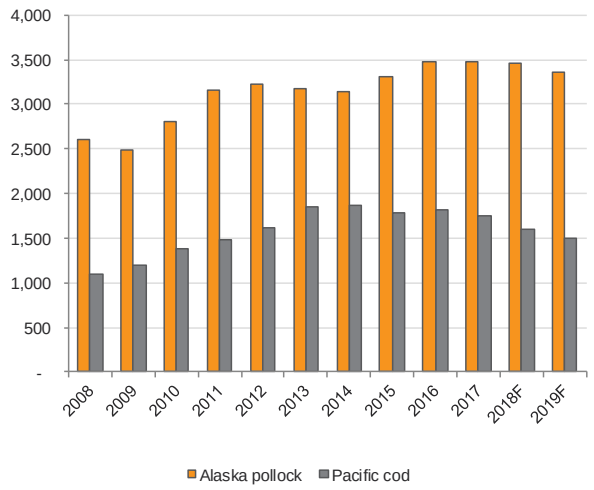
2019 should be another good year

We expect that pangasius exports will stay strong in 2019 with continued growth in major export markets such as USA, China and ASEAN countries. Vietnam could remain the leading supplier of pangasius in the world, despite growing competition from new suppliers, thanks to higher product quality and cost advantages relative to other pangasius exporting nations.

Supplies of other white-fish substitutes such as Alaska pollock and Pacific cod are expected to decline in 2019

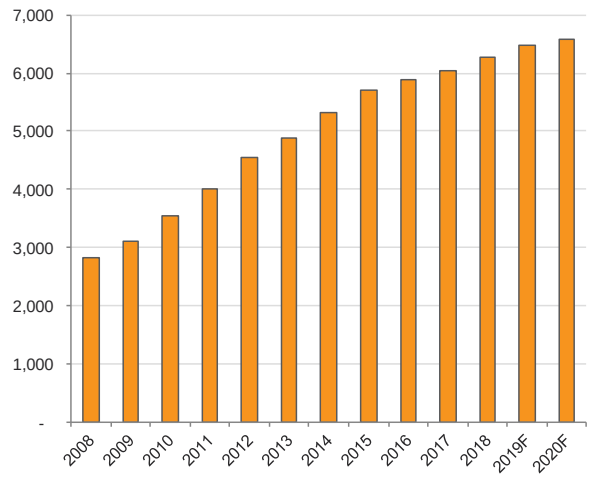
Currently, the main substitutes of pangasius included Alaska pollock, Pacific cod (wild-caught fish) and Chinese tilapia (farmed fish). The Pacific cod and Alaskan pollock supply have been continuously decreasing since 2016 (see Figure 265) and are expected to continue their downward trend in the coming years due to: (1) declining supply due to over-fishing and (2) stricter regulations on fishing in developed countries, especially in the US and EU (for example, setting lower Total Allowable Catches - TAC).

Figure 265: Global Alaska pollock and Pacific cod supply in 2008-2019F (m tonnes)



Source: Groundfish Forum

Figure 266: Global tilapia supply in 2008-2020F (m tonnes)



Source: Groundfish Forum

Vietnam pangasius suppliers are expected to gain more market share from other white-fish suppliers in major markets such as the US and China

Vietnam pangasius suppliers could grab whitefish market share in the US from Chinese tilapia as the latter has recently been subject to trade war-induced tariffs. In the context of rising trade tensions between the US and China, the US government has decided to apply a 10% import tax on seafood products imported from China, including tilapia from Oct 2018. Since then, some local news reported that sales of Chinese tilapia at US supermarkets has decreased by 20-30% compared to the period before the tax imposition, and Chinese imports were replaced by other whitefish products including Vietnamese pangasius.

Vietnam pangasius enjoyed reduced anti-dumping duties in the US market. According to the preliminary results of the 14th period of review (POR 14) released in Sep 2018, the US lowered anti-dumping tariffs on pangasius imports from Vietnam from the levels stipulated in the POR 13. The anti-dumping rates applied to the two mandatory respondents of the POR 14 were US$1.37/kg for NTSF Seafoods JSC

(Unlisted) and 0% for Hung Vuong Group (HVG VN, Not Rated). The rate applied to voluntary respondents was US$0.41/kg and that for the remaining Vietnamese pangasius exporters was US$2.39/kg. This was a significant reduction from the average tariff set in POR 13 of US$3.87/kg (highest rate was US$7.74/kg). The US government will announce the final results of POR 14 in Jan 2019.

Figure 267: Summary of imposed tariffs on Vietnamese pangasius in the US market

POR	Unit	Mandatory respondents	Voluntary respondents	Other exporters	Application period
POR 8	USD/kg	0.19	0.02	0.77	1/8/2010 - 31/7/2011
POR 9	USD/kg	0	2.15	2.11	1/8/2011 - 31/7/2012
POR 10	USD/kg	0	0.97	2.39	1/8/2012 - 1/8/2013
POR 11	USD/kg	0	0.60	0	1/8/2013 - 31/7/2014
POR 12	USD/kg	0.69	2.39	2.39	1/8/2014 - 31/7/2015
POR 13	USD/kg	3.87	7.74	2.39	1/8/2015 - 31/7/2016
POR 14 (prel.)	USD/kg	0-1.37	0.41	2.39	1/8/2016 - 31/7/2017

Source: VNDIRECT, VASEP

The decline in US tariffs could create a price advantage for Vietnamese pangasius imports into the US relative to other white-fish substitutes, especially Chinese tilapia (which accounted for 45% of total US whitefish imports in 2017 vs. pangasius' 25% share). In light of our expectations for continued trade tensions between the US and China despite the recent progress on trade talks, this could create better opportunities for Vietnamese exporters to gain market share in the US.

China also eased import duties on Vietnam pangasius products from 10% to 7% in mid-2018. Data from the International Trade Centre showed that catfish, including pangasius, currently accounts for 5.7% of China's total imports of whitefish while Pacific cod accounts for 41.5%, implying ample room for Vietnamese pangasius products to gain more market share from Alaska pollock and Pacific cod in China.

Opportunities in new export markets in Southeast Asia and the Middle East

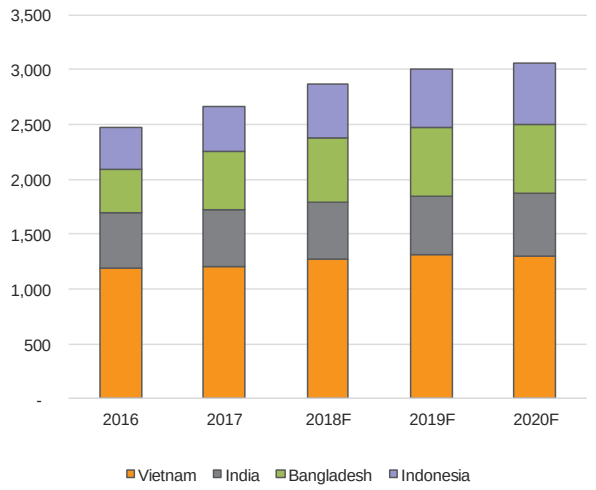
In addition to rising consumption in large markets such as the US, China and EU, demand for Vietnamese pangasius is growing in a more diverse range of markets such as ASEAN and the Middle East. Over 11M18, there was double-digit growth in export value to certain countries such as Thailand (+48.1% yoy), Singapore (+25.1% yoy), Philippines (+39.3% yoy), UAE (+117.6% yoy), and Egypt (+26.4% yoy in 10M18). We believe these are prospective markets for future export growth, with increasing income per capita, urbanisation and stagnating wild-caught volumes (which in turn would foster the development of farmed fish such as pangasius).

Vietnam will remain the leading exporter of pangasius in the world thanks to high quality and cost advantages, despite growing competition from new suppliers

Global pangasius supply is expected to grow at a CAGR of 3.3% during 2018-2020F, with supply increases mostly coming from newcomers such as India, according to the Global Aquaculture Alliance (GAA). Vietnam's pangasius supply is forecast to expand by 1.4% per year during 2018-2020 (compared to the average growth rate of 3.3% during 2016-2018), which is lower than the production growth of other competitors, including India, Bangladesh and Indonesia. Total pangasius supply of these countries is expected to increase at a CAGR of 4.9% during 2018-2020 (lower than the corresponding average growth rate of 11.8% during 2016-2018). Although

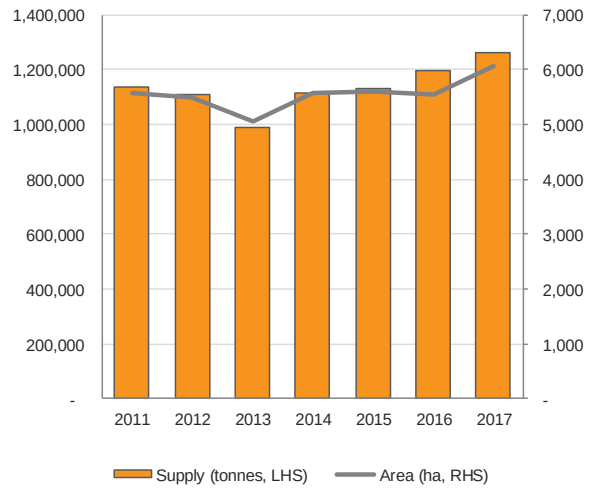
incremental supply will be added to a sizable extent by newcomers, their scale is still small relative to Vietnam's, and can only satisfy domestic demand. They would therefore not pose a significant risk to Vietnamese producers which are more export-focused and account for 45% of global pangasius production and 95% of pangasius imports into the US.

Figure 268: Pangasius supply of major producing countries (m tonnes)



Source: VHC, Undercurrent News

Figure 269: Pangasius supply and farming area in Vietnam



Source: VASEP

Vietnam pangasius has great advantages in export markets thanks to high quality and competitive price. The Mekong River leading to the sea is considered the ideal environment for pangasius farming. Thanks to that natural advantage, productivity and quality of Vietnamese pangasius is higher than those of other competitors. In terms of quality, Vietnamese pangasius meat is white and contains less tannin while pangasius meat in other countries is yellow and contains more tannin. Therefore, in large markets with high standards regarding quality products such as the US and China, pangasius products of other countries such as India, Bangladesh and Indonesia are still unable to compete with Vietnamese products. In terms of productivity, farming yield in Vietnam in the 2011-2017 period averaged 204 tonnes/ha, which was much higher than other competitors' yields such as Bangladesh (50-70 tonnes/ha), India (15 tonnes/ha) and Indonesia (15 tonnes/ha). Vietnam's higher productivity is also partly due to extensive experience in raising pangasius. Therefore, we believe these emerging suppliers will not be a strong threat to Vietnam's pangasius exporters in the near term.

In conclusion, we remain optimistic about the prospects of pangasius exporters in 2019 thanks to: (1) their ability to take market share from white-fish substitutes such as Alaska pollock and Pacific cod which are expected to see supply declines and Chinese tilapia which is subject to trade war-induced tariffs; (2) their benefitting from lower tariffs in major markets such as the US and China. We prefer companies that have built strong vertically integrated production chains (fingerlings & fish feed – raw fish – value-added products) and are already export leaders to the US or China markets. On this basis, we place Vinh Hoan Corp (VHC VN, Not rated) on our watch list.

Figure 270: Fisheries peer comparison

Company	Ticker	Market cap (US$m)	TTM NP growth (% yoy)	TTM EPS growth (% yoy)	TTM ROA (%)	TTM ROE (%)	D/E (x) (curr.)	TTM P/E (x)	TTM P/B (x)
Vinh Hoan Corp	VHC VN	366	141%	141%	23.0%	38.3%	0.4	6.9	2.2
Nam Viet Corp	ANV VN	147	293%	142%	9.8%	23.7%	1.1	9.7	2.2
IDI Corp	IDI VN	66	148%	148%	11.5%	23.9%	0.9	2.6	0.6
Cuu Long An Giang Fish JSC	ACL VN	32	436%	436%	12.7%	34.9%	1.1	4.9	1.4
Aquatex Bentre	ABT VN	21	185%	169%	11.1%	16.2%	0.1	7.4	1.2
Average		**127**	**241%**	**207%**	**13.6%**	**27.4%**	**0.7**	**6.3**	**1.5**
Median		**66**	**185%**	**148%**	**11.5%**	**23.9%**	**0.9**	**6.9**	**1.4**

Note: Data as of Jan 11, 2018
Source: VNDIRECT, FiinPro

VINH HOAN CORP (VHC)

Market Price	Target Price	Dividend Yield	Rating	Sector
VND91,000	N/A	2.2%	NOT RATED	FISHERIES

Outlook – Short term	Outlook – Long term	Valuation
Not rated	Not rated	Not rated

11 January 2019
Pham Le Mai
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Stellar performance in 2018 (11M export sales +27% yoy, 9M net profit +152% yoy) was driven by strong ASP increases which outweighed raw fish input price growth.

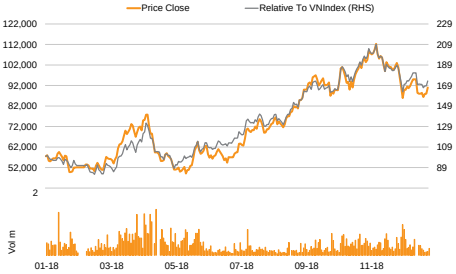
Low US anti-dumping tariff a key advantage. VHC has been enjoying 0% anti-dumping tariff when exporting to the US for the past five years (lower than most other producers), hence allowing the company to become the top Vietnamese pangasius exporter to the US with ~43% market share by total export value (2017). We believe with its strong market position and preferential tariffs, VHC could still see healthy but more moderate growth in the US in 2019 (due to high-base effect in 2018 with 9M export value +45% yoy) driven by export price and volume increases.

A possible US-China trade war beneficiary. Higher tariffs applied to Chinese seafood (including tilapia, which accounts for 63% of total tilapia exported into the US in 2017) could open new opportunities for Vietnamese exporters, especially market leaders such as VHC as pangasius is a substitute for tilapia. The US is already the largest export market of VHC to date (66% of 9M18 sales came from the US).

Production capacity expansion thanks to new farming area and upgraded factory. With the operation of the new farming area in Tan Hung (220ha), VHC expects to improve its raw material in-sourcing rate to 70% in 2019 (from the current ~50-60%), giving the company better control of input cost, especially in times of rising raw fish prices like in 2018. In addition, VHC also plans to increase the processing capacity of its Thanh Binh factory from 100 tonnes of raw fish/day to 150 tonnes/day by end-2018 and 300 tonnes/day by 2019. Given most of the company's factories already run near maximum capacity, this could help VHC increase its total capacity to meet demand growth.

The company surpassed its 2018 profit guidance (VND620bn) by 67% in 9M2018, driving its share price up 89% in 2018. It is currently trading at a TTM P/E of 6.9x, which is fairly low given its strong profit growth, leading market share and the highest ROE and ROA among peers. Pangasius exports still look promising in 2019 with catalysts from new FTAs such as CPTPP, EVFTA and the US-China trade war all potentially benefitting VHC as the leading exporter in the segment.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	112,300
52w low (VND)	49,100
3m Avg daily volume (shares)	264,347
3m Avg daily value (VNDmn)	24,785
Market cap (VNDbn)	8,409
Outstanding shares (m)	92.4
Free float (%)	26
TTM P/E (x)	6.9
Current P/B (x)	2.2

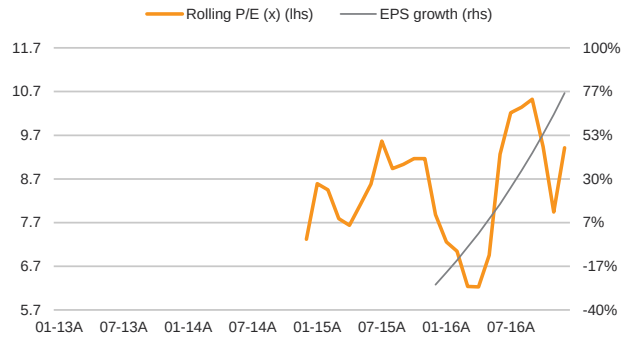
Ownership

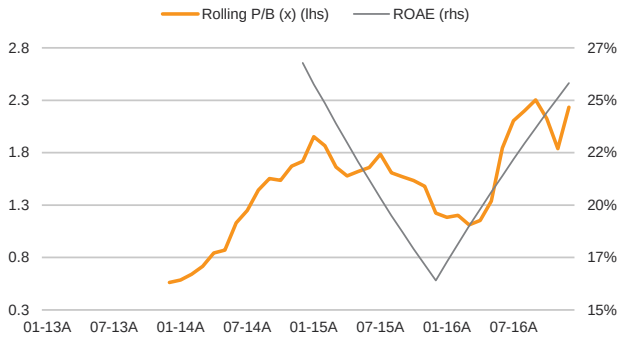
Truong Thi Le Khanh	42.8%
Mitsubishi Corp	6.5%
Red River Holding	4.9%
Others	45.8%

Source: VNDIRECT

Financial summary (VND)	12-14A	12-15A	12-16A	12-17A
Net revenue (bn)	6,292	6,493	7,304	8,151
Revenue growth		3.2%	12.5%	11.6%
Gross margin	13.1%	12.4%	14.6%	14.4%
EBITDA margin	11.9%	8.7%	12.2%	12.2%
Net profit (bn)	439	323	567	605
Net profit growth		(26.5%)	75.7%	6.7%
Recurring profit growth		(31.1%)	74.1%	14.8%
Basic EPS	4,753	3,491	6,140	6,551
Adjusted EPS	4,753	3,274	5,707	6,551
BVPS	20,236	22,477	25,861	31,879
ROAE	26.3%	16.3%	25.4%	22.7%

Valuation





Income statement

(VNDbn)	12-15A	12-16A	12-17A
Net revenue	6,493	7,304	8,151
Cost of sales	(5,691)	(6,237)	(6,980)
Gen & admin expenses	(118)	(115)	(141)
Selling expenses	(253)	(266)	(269)
Operating profit	**432**	**686**	**761**
Operating EBITDA	577	833	960
Depreciation and amortisation	**(144)**	**(147)**	**(199)**
Operating EBIT	**432**	**686**	**761**
Interest income	166	87	58
Financial expense	(210)	(93)	(89)
Net other income	(2)	(7)	(8)
Income from associates & JVs			
Pre-tax profit	**387**	**672**	**723**
Tax expense	(66)	(107)	(118)
Minority interest	2	1	0
Net profit	**323**	**567**	**605**
Adj. net profit to ordinary	323	567	605
Ordinary dividends	(92)	(231)	(0)
Retained earnings	**230**	**336**	**605**

Balance sheet

(VNDbn)	12-15A	12-16A	12-17A
Cash and equivalents	296	165	45
Short term investments	0	169	373
Accounts receivables	1,188	1,150	1,329
Inventories	1,300	1,214	1,202
Other current assets	63	50	54
Total current assets	**2,847**	**2,748**	**3,004**
Fixed assets	1,313	1,500	1,790
Total investments	13	17	1
Other long-term assets	184	185	247
Total assets	**4,357**	**4,451**	**5,043**
Short-term debt	1,334	866	1,008
Accounts payable	199	276	233
Other current liabilities	286	375	429
Total current liabilities	**1,819**	**1,517**	**1,671**
Total long-term debt	438	518	402
Other liabilities	10	23	27
Share capital	924	924	924
Retained earnings reserve	936	1,250	1,805
Shareholders' equity	**2,077**	**2,387**	**2,943**
Minority interest	12	6	0
Total liabilities & equity	**4,357**	**4,451**	**5,043**

Cash flow statement

(VNDbn)	12-15A	12-16A	12-17A
Pretax profit	**387**	**672**	**723**
Depreciation & amortisation	144	147	199
Tax paid	(39)	(33)	(115)
Other adjustments	(33)	(100)	(211)
Change in working capital	**(312)**	**268**	**(147)**
Cash flow from operations	**146**	**955**	**448**
Capex	(348)	(356)	(243)
Proceeds from assets sales	13	7	0
Others	(48)	20	(163)
Other non-current assets changes	863	(136)	(188)
Cash flow from investing activities	**480**	**(465)**	**(593)**
New share issuance	0	0	0
Shares buyback	0	(3)	0
Net borrowings	(327)	(388)	27
Other financing cash flow	0	0	0
Dividends paid	(92)	(231)	(0)
Cash flow from financing activities	**(419)**	**(622)**	**27**
Cash and equivalents at beginning of period	89	296	165
Total cash generated	**207**	**(131)**	**(119)**
Cash and equivalents at the end of period	296	165	45

Key ratios

	12-15A	12-16A	12-17A
Dupont			
Net profit margin	5.0%	7.8%	7.4%
Asset turnover	1.47	1.66	1.72
ROAA	7.3%	12.9%	12.7%
Avg assets/avg equity	2.24	1.97	1.78
ROAE	16.3%	25.4%	22.7%
Efficiency			
Days account receivable	55.0	47.3	54.3
Days inventory	83.4	71.2	62.9
Days creditor	12.8	16.2	12.2
Fixed asset turnover	5.23	5.19	4.96
ROIC	8.4%	15.0%	13.9%
Liquidity			
Current ratio	1.57	1.81	1.80
Quick ratio	0.85	1.01	1.08
Cash ratio	0.16	0.22	0.25
Cash cycle	126	102	105
Growth rate (yoy)			
Revenue growth	3.2%	12.5%	11.6%
Operating profit growth	3.8%	58.6%	11.0%
Net profit growth	(26.5%)	75.7%	6.7%
EPS growth	(26.5%)	75.9%	6.7%
Share value			
Basic EPS (VND)	3,491	6,140	6,551
BVPS (VND)	22,477	25,861	31,879

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.

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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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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