May, 2020

CENTURY SYNTHETIC FIBER CORP. (HSX: STK)

Recycled yarn to alleviate the adverse impact of COVID-19

(VND bn)	Q1-FY20	Q4-FY19	+/- qoq	Q1-FY19	+/- yoy
Net revenue	617	576	7.2%	605	1.9%
PAT	52	53	-2.5%	52	0.3%
EBIT	70	73	-3.9%	66	6.4%
EBIT margin	11.3%	12.6%	-1.3pps	10.8%	0.5pps

Source: STK, Rong Viet Securities

1Q2020: Sales grew but were lower than planned due to pandemic prevention measures in the US and EU

- Net sales only increased slightly by 2% YoY to VND 617 bn.
- Virgin yarn is down both in volume and price but recycled yarn still grew well with sales volume increasing 48% YoY. The share of recycled yarn in revenue reached 34% (1Q2019: 23%).
- GPM improved to 15.4% (1Q2019: 13.8%). However, SG&A and financial expenses increased sharply, causing PAT growth to be flat, reaching VND 52 bn.

2019 outlook: Recycled yarn to alleviate the adverse impact of COVID-19

We project the proportion of recycled yarn to sales to be 41%. The gross profit margin is estimated at 16.6%, up from 15.9% in 2019. Virgin yarn selling prices plummeted following oil price movements and fierce competition with China's virgin yarn as China's manufacturing activities have returned to normal. The price of recycled yarn increased slightly by 3% YoY due to the eco-friendly fashion trend.

Market development, pandemic prevention, the preparation for the anti-dumping lawsuit on Chinese yarn imported into Vietnam and senior personnel recruitment from 2020 will increase selling and administrative expenses.

In total, revenue was about VND 1,966 bn, down by 12% YoY. PAT is estimated at VND 182 bn, down 15% YoY, equivalent to an EPS of VND 2,570/share.

Valuation and recommendation

While the entire textile industry's value chain is badly affected by the pandemic, STK is not an exception and the worst time, in our opinion, will be 2Q when many large markets enter the drastic phase of fighting the pandemic. Consumers' uncertainty about the economic prospects after the pandemic could lead to lower spending on some types of goods, including apparels. Low demand for apparels would indirectly affect yarn demand. However, we believe that STK can somewhat limit the impact of this trend thanks to (1) their production shift toward highly profitable recycled yarn (2) the relocation of textile production from China to Vietnam and other Asian countries and (3) the increasing trend of using domestically made yarn by Vietnamese garment companies to take advantage of EVFTA tariffs incentives.

*Using methods of FCFF cash flow discount and P/E, we estimate STK's fair value at VND **20,000 /share**. With a cash dividend of VND 1,500/share in the next 12 months, the expected return is 25% compared to the closing price of May 18th, 2020. We maintain our **BUY** recommendation. The target price has been adjusted by 13% compared to what it was in the 2020 Strategic Report to reflect the impact of the COVID-19 pandemic.*

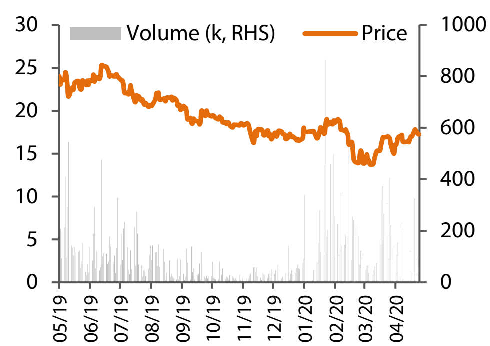
BUY	+25%
Target price (VND)	20,000
Current market price (VND)	17,250
Cash dividend (VND)[*]	*1,500*

[*]Expected in the next 12 months

Stock Info	
Sector	Textile
Market Cap (VND billion)	1,160
Current Shares O/S	68.2
Avg. Daily Volume (in 20 sessions)	186,984
Free float (%)	58.3
52 weeks High	24,000
52 weeks Low	13,750
Beta	1.1

	FY2019	Current
EPS	3,034	2,904
EPS Growth (%)	1.9	-9.0
Diluted EPS	3,034	2,904
P/E	5.4	5.4
P/B	1.1	1.0
EV/EBITDA	4.2	3.8
Cash dividend yield (%)	1,500	-
ROE (%)	21.5	20.3

Price performance



Major Shareholders (%)	
Huong Viet Investment Consulting Corp.	20.0
Dang My Linh	14.3
Dang Trieu Hoa	11.8
Foreign ownership room left (%)	*39.7*

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Exhibit 1: Q1/2020 Results

(VND Bn)	Q1-FY20	Q4-FY19	+/-(qoq)	Q1-FY19	+/-(yoy)
Net revenue	617	576	7.2%	605	1.9%
Gross profit	95	96	-0.9%	84	13.6%
SG&A	25	23	8.3%	18	39.9%
Operating income	70	73	-3.9%	66	6.4%
EBITDA	103	106	-3.0%	102	1.0%
EBIT	70	73	-3.9%	66	6.4%
Financial expenses	16	8	100.5%	8	88.0%
- Interest Expenses	*5*	*8*	*-33.9%*	*8*	*-33.0%*
Dep. and amortization	33	33	-1.3%	36	-8,8%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	58	72	-20.4%	59	-2.7%
PAT	52	53	-2.5%	52	0.3%
(*) Adjusted PAT	52	53	-2.5%	52	0.3%

Source: VHC, Rong Viet Securities

Exhibit 2: Q1/2020 Performance Analysis

Particulars	Q1-FY20	Q4-FY19	+/-(qoq)	Q1-FY19	+/-(yoy)
Profitability Ratios (%)					
Gross Margin	15.4%	16.7%	-1.3pps	13.8%	1.6pps
EBITDA Margin	16.7%	18.4%	-1.8pps	16.8%	-0.1pps
EBIT Margin	11.3%	12.6%	-1.3pps	10.8%	0.5pps
Net Margin	8.4%	9.3%	-0.8pps	8.6%	-0.1pps
Adjusted Net Margin	8.4%	9.3%	-0.8pps	8.6%	-0.1pps
Turnover *(x)					
-Inventories	4.4	3.6	0.8	4.1	0.2
-Receivables	22.4	18.4	3.9	26.6	-4.3
-Payables	7.0	6.0	1.1	5.0	2.1
Leverage (%)					
Total Debt/ Equity	65.5%	75.8%	-10.3pps	90.1%	-24.5pps

Source: Rong Viet Securities

Exhibit 3: Q2/2020 Forecast

Particulars (VND Bn)	Q2-FY20	+/- qoq	+/- yoy
Revenue	356	-42%	-28%
Gross profit	52	-45%	-10%
EBIT	35	-50%	-53%
NPAT	33	-37%	-43%

Source: Rong Viet Securities

Main assumptions:

- Sales decreased by 28% YoY as many fashion retail stores in major markets (US, EU) closed for epidemic prevention in April. Some countries allowed the economic reopening since mid-May but demand for garments is weak because consumers are still afraid of the contagion of the pandemic and declining consumer confidence.

- Recycled yarn accounts for 39% of total revenue

- Gross profit margin reaches 14.6%

Update

1Q2020: Sales increased but lower than planned due to the pandemic prevention measures in the US and Europe, but soaring costs made profit flat

Table 1. Business results in 1Q2020

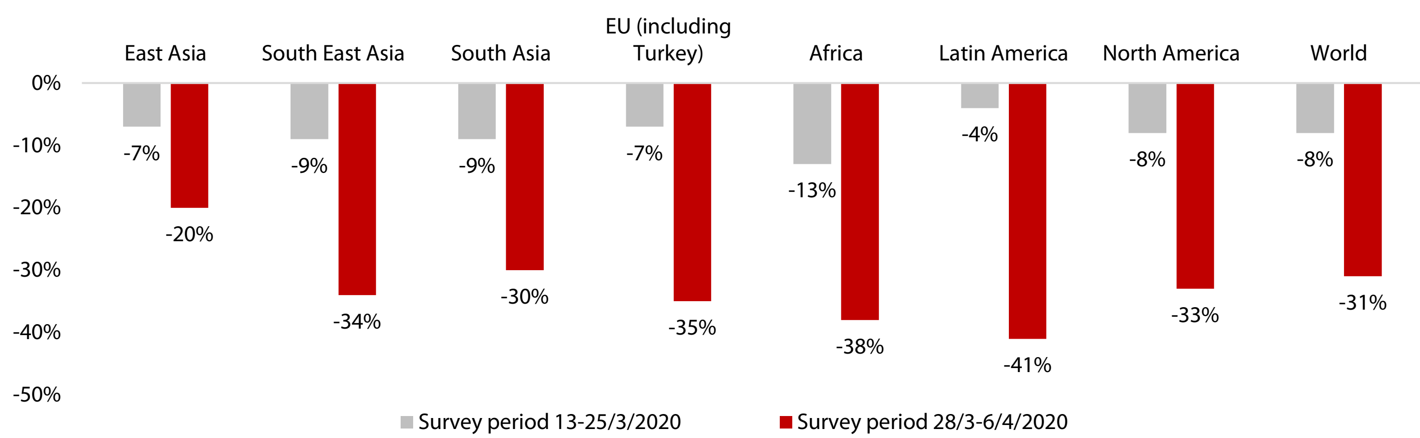
Unit: VND (bn)	1Q 2020	1Q 2019	% growth
Net revenue	617	605	1.9%
Gross profit	95	84	13.6%
Gross profit margin	**15.4%**	**13.8%**	
Selling expenses	-10	-6	73.0%
G&A expenses	-16	-12	25.1%
Financial income	4	2	100.2%
Financial expenses	-16	-8	88.0%
Interest expenses	-5	-8	-33.0%
Other profits	0	0	-54.9%
PBT	58	59	-1.7%
PBT margin	**9.4%**	**9.8%**	
PAT	52	52	0.3%
PAT margin	**8.4%**	**8.6%**	

Source: STK, Rong Viet Securities

1Q revenue increased slightly by 2% YoY, reaching VND 617 bn. Selling volume grew by 11% YoY and the average selling price decreased by 8.3% YoY. In particular, the revenue of recycled yarn increased sharply by 53% YoY, accounting for 34% of total revenue (1Q2019: 23%), with volume up 48% and average selling price up 3.3%. Meanwhile, the price of virgin yarn decreased by 10% over the same period and output, according to our calculations, decreased slightly by 3%. In the context that the supply of yarn and fabrics from China to Vietnam plummeted due to pandemic prevention measures in China, STK has actively reduced its selling prices to stimulate demand and expand market share. According to the company, domestic and international customers, including old and new customers have increased placing orders in STK to make up for the shortage supply from China.

Sales in the first 2 months grew well by 15% YoY. In the second half of March, customers have cancelled or postponed orders as many countries have deployed pandemic-fighting measures. Social distancing has severely reduced fashion revenues globally, indirectly dragging down yarn demand. According to the company, if there was no COVID-19, 1Q revenue would have increased by 10% YoY.

Figure 1: Value of textile orders reduced largely YoY due to COVID-19

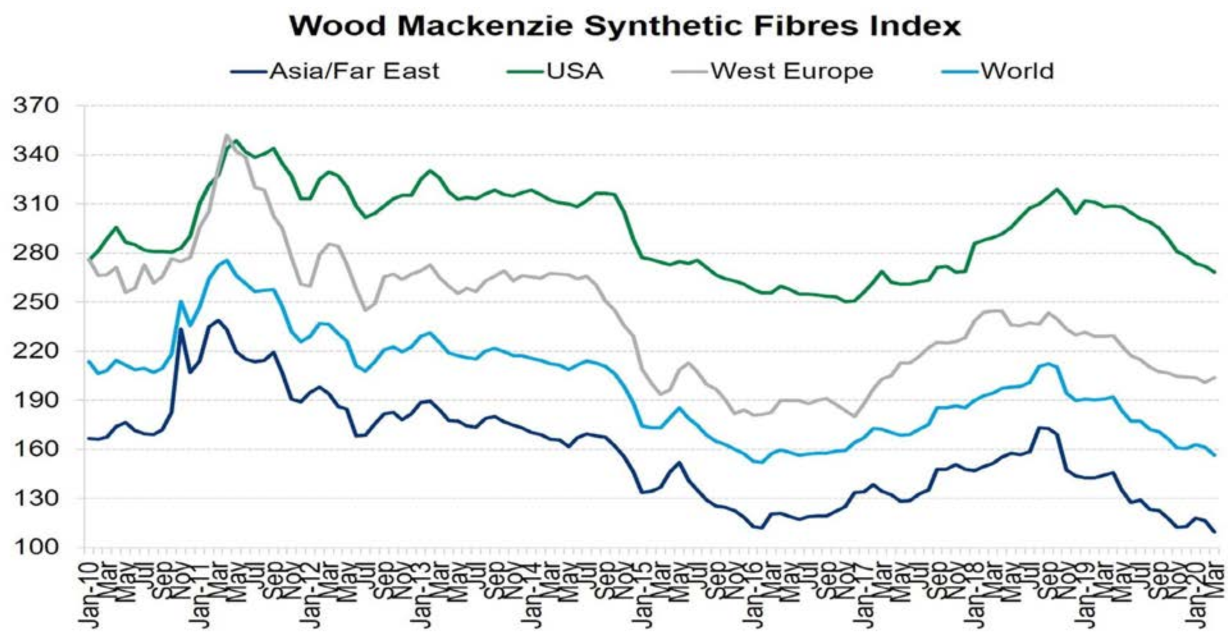


Source: International Textile Manufacturers Federation (ITMF)

STK uses polyester chips imported from many sources including Japan, ASEAN, Taiwan, the US, China, etc. with only 20-30% depending on China. The company has quickly increased imports from other countries to make up for the shortage from China when Chinese suppliers reduced production due to the pandemic. In 1Q2020, polyester chip prices dropped more sharply than yarn selling prices, averaging -16.7% YoY, in which chip prices for recycled yarn dropped by 4.7%. As a result, the gross profit margin reached 15.4%, in comparison with 13.8% in 1Q2019.

Working capital is managed effectively with the number of days receivable, although it has increased to 16 days compared to 14 days in the same period last year but has decreased compared to that at the end of 2019. The number of inventory days decreased slightly to 84 days from 88 days in 1Q2019 but has improved significantly since 3Q2019.

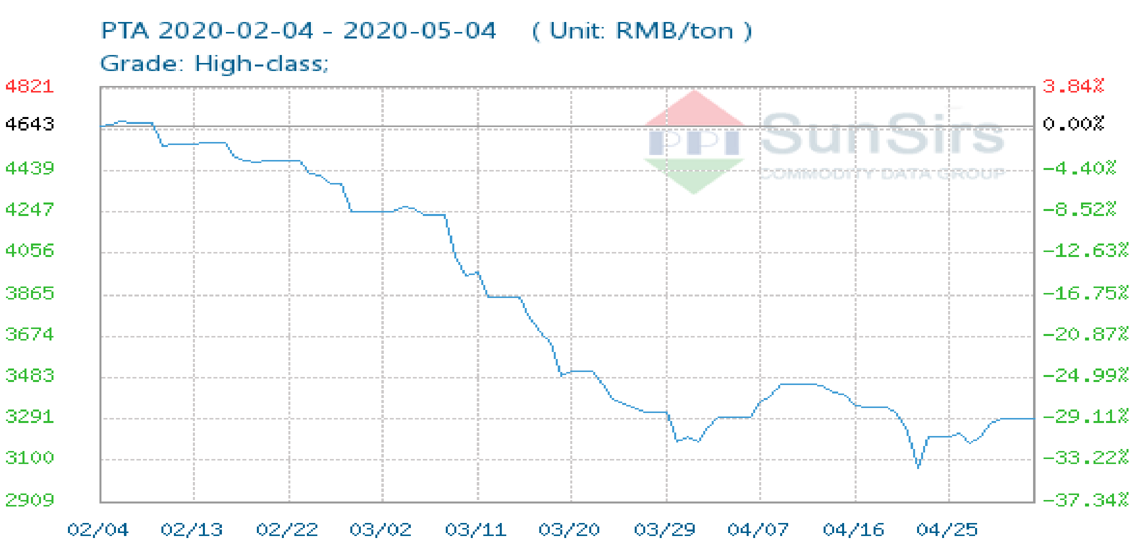
Figure 2: Global synthetic fiber price index



*including acrylic, nylon, polyester and polypropylene filament yarn and staple fibers

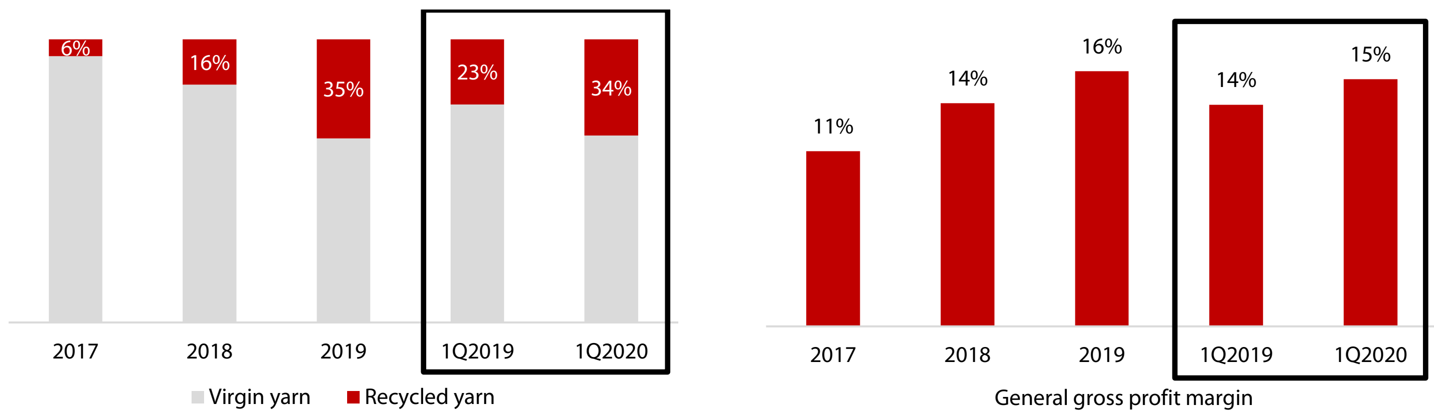
Source: Wood Mackenzie

Figure 3: PTA chip price (virgin yarn material)



Source: Sunsir.com

Figure 4: The increase of recycle yarn proportion in total revenue (left) enhanced the general gross profit margin (right)



Source: STK, Rong Viet Securities

Selling expenses climbed by 73% YoY mainly due to freight and insurance costs as the company exported more in CIF contracts than in 1Q2019. General and administration expenses also increased significantly by 25% as the company spent on pandemic prevention measures and legal advice on the lawsuit of the dumping of cheap yarn into Vietnam. As we have mentioned many times in previous reports, the dumping of Chinese and Indian yarns in many markets around the world, including Vietnam, has created unfair competition in recent years, causing great losses to many Vietnamese yarn manufacturers. Accordingly, at the end of March 2020, the Ministry of Industry and Trade initiated an anti-dumping investigation on filament imported into Vietnam from China, India, Indonesia and Malaysia. STK is working with lawyers in providing information to show how its sales have been damaged by the unfair competition of imported yarn. Financial expenses increased by 88% YoY mainly due to unrealized losses on exchange rate difference, while interest expense declined slightly.

In sum, PBT was VND 58 bn, down slightly by 1.7% YoY but PAT was flat, reaching VND 52 bn thanks to lower corporate income tax expenses. With this result, STK has completed 24% and 22% of its plan for revenue and PAT.

2020 forecast

We expect that the demand of yarn for making clothing will decline in 2Q and recover gradually in the second half of the year. **Revenue in 2020 could reach VND 1,966 bn, down 12% YoY.**

At present, most of China's yarn factories have fully resumed production. Competition from China in the remaining months of the year, together with the decline in oil price, may cause the price of virgin yarn to plummet by 11%. For recycled yarn, the selling price for the whole year may increase slightly by 3% due to the eco-friendly fashion trend and the chip prices for making recycled yarn being not affected by the oil price. We forecast **recycled yarn to contribute about 41% of total revenue, higher than 35% in 2019. The gross profit margin, therefore,** will **increase to 16.6%** (2019: 15.9%), despite the average selling price falling by 3.6%.

From April 2020 to the end of 2021, STK will supply industrial yarn (used to make car headliners) to the US market with a volume of 200 tons/month, under a contract signed in late March. Because of higher quality compared to the fiber used to make clothes, this product has a selling price and gross profit margin higher than virgin yarn by 20-30% and 4-8 pps, respectively. As industrial yarn accounts for only 4% of yearly total volume, we think the contribution of this product to total revenue in the coming years is insignificant and did not include in our pricing model.

In addition, in 2020, the company will recruit a German expert to the position of Deputy General Director in charge of technology and product research and development and two other experts in market development and manufacturing. Together with the costs of pandemic prevention and legal advice related to the anti-dumping lawsuit, the cost of administration in 2020 could increase by 12% YoY.

In general, **2020 PAT is estimated at VND 182 bn, down 15% YoY**, equivalent to an EPS of VND 2,570/share.

In 2021, yarn demand will recover as garment demands rises. However, competition with cheap Chinese yarn is still servere, so the price of virgin and recycled yarn may inch up slightly by about 1%. If there is a recovery in oil price in 2021, it will increase raw material costs by 12%. **Thanks to the continued shift of production toward the highly profitable recycled yarn segment with the proportion of recycled yarn on revenue expected to reach 50%** (2020: 41%), **the average selling price could increase by 9% YoY and gross profit margin expand to 17.2%** (2020: 16.6%). Accordingly, we forecast **sales of 2021 to reach VND 2,197 bn, up 12% YoY and PAT to reach VND 223 bn, up 23% YoY.**

VND Billion

INCOME STATEMENT	FY2018	FY2019	FY2020F	FY2021F
Revenue	2,408	2,229	1,966	2,197
COGS	2,073	1,875	1,640	1,819
Gross profit	**335**	**354**	**326**	**379**
Selling Expense	34	27	31	33
G&A Expense	56	58	64	68
Finance Income	11	14	15	21
Finance Expense	53	35	36	40
Other profits	-3	5	1	1
PBT	-1	0	0	0
Prov. of Tax	**199**	**253**	**212**	**260**
Minority's Interest	21	39	30	37
PAT to Equity S/H	0	0	0	0
EBIT	**178**	**215**	**182**	**223**
EBITDA	245	269	231	278

FINANCIAL RATIO	FY2018	FY2019	FY2020F	FY2021F
Growth (%)				
Revenue	21.0	-7.4	-11.8	11.8
Operating Income	41.7	4.5	-9.0	13.1
EBITDA	94.3	9.8	-14.1	20.3
PAT	79.1	20.3	-15.3	22.6
Total Assets	7.1	-2.4	-0.7	2.9
Equity	16.7	19.2	6.5	9.7
Profitability (%)				
Gross margin	13.9	15.9	16.6	17.2
EBITDA margin	16.1	18.2	18.8	19.0
EBIT margin	10.2	12.1	11.8	12.7
Net margin	7.4	9.6	9.2	10.1
ROA	8.4	10.4	8.8	10.5
ROE	19.6	19.8	15.8	17.6
Efficiency (times)				
Receivable Turnover	36.8	22.7	16.7	16.7
Inventory Turnover	4.1	3.6	3.3	3.4
Payable Turnover	4.8	6.1	6.7	6.7
Liquidity (times)				
Current	0.9	1.1	1.3	1.6
Quick	0.3	0.4	0.7	0.9
Finance Structure (%)				
Total Debt/Equity	85.2	62.3	56.5	45.2
Current Debt/Equity	46.9	47.1	44.8	36.3
Long-term Debt/Equity	38.3	15.1	11.7	8.9

VND Billion

BALANCE SHEET	FY2018	FY2019	FY2020F	FY2021F
Cash and cash equivalents	153	150	124	139
Short-term investments	45	80	245	355
Accounts receivable	65	98	118	132
Inventories	510	523	492	527
Other current assets	31	27	28	28
Property, plant & equipment	1,180	1,049	925	799
Acquired intangible assets	0	0	0	0
Long-term investments	2	2	2	2
Other non-current assets	133	140	120	131
Total assets	**2,119**	**2,069**	**2,054**	**2,113**
Accounts payable	433	308	246	273
Short-term borrowings	427	510	516	460
Long-term borrowings	348	164	135	112
Other non-current liabilities	0	0	0	0
Bonus and Welfare fund	2	3	3	3
Technology-science, dev. fund	0	0	0	0
Total liabilities	**1,210**	**986**	**901**	**848**
Common stock and APIC	635	742	742	742
Treasury stock (enter as -)	0	0	0	0
Retained earnings	273	340	410	522
Other comprehensive income	0	0	0	0
Inv. and Dev. Fund	1	1	1	1
Total equity	**909**	**1,083**	**1,154**	**1,265**
Minority Interest	**0**	**0**	**0**	**0**

VALUATION RATIO (*)	FY2018	FY2019	FY2020F	FY2021F
EPS (dong)	2,976	3,034	2,570	3,151
P/E (x)	5.9	4.2	6.4	5.2
BV (dong)	15,167	15,316	16,311	17,888
P/B (x)	1.2	1.1	1.0	0.9
DPS (dong/cp)	1,500	1,500	1,500	2,000
Dividend yield (%)	8.6	8.5	9.1	12.2

VALUATION MODEL	Price	Weight	Average
FCFF	29,193	40%	11,677
P/E	14,864	20%	2,973
EV/EBITDA	16,904	40%	6,762
Target price (VND)			**21,412**

VALUATION HISTORY	Price	Recommendation	Period
06/2017	24,200	BUY	Long term
11/2018	24,300	BUY	Long term
11/2019	23,000	BUY	Long term

RESULT UPDATE

This report is created for the purpose of providing investors with an insight into the discussed company that may assist them in the decision-making process. The report comprises analyses and projections that are based on the most up-to-date information with the objective that is to determine the reasonable value of the stock at the time such analyses are performed. Through this report. we strive to convey the complete assessment and opinions of the analyst relevant to the discussed company. To send us feedbacks and/or receive more information. investors may contact the assigned analyst or our client support department.

RATING GUIDANCE

Ratings	BUY	ACCUMULATE	REDUCE	SELL
Total Return including Dividends in 12-month horizon	>20%	5% to 20%	-20% to -5%	<-20%

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