QUANG NGAI SUGAR JSC (UPCOM: QNS)

Obstacles in the short term, stable outlook for the long term

Particular (VND bn)	Q1-FY20	Q4-FY19	+/- qoq	Q1-FY19	+/- yoy
Net revenue	1,424	1,633	-12.7%	2,000	-28.8%
PAT	117	473	-75.3%	155	-24.6%
EBIT	127	506	-74.9%	180	-29.6%
EBIT margin	8.9%	31.0%	-2,210 bps	9.0%	-10 bps

Source: QNS, Rong Viet Securities

Q1/20 – Revenue and PAT decreased strongly due to the Covid-19's impact

- Net revenue reached VND 1,424 bn, decreasing 29% YoY. Revenue from the two core businesses: soy milk's decreased 8.4% and sugar's declined 58% YoY.
- Unfavorable weather in the Central and Highland regions dragged down sugarcane productivity. In the 2019 – 2020 season, QNS only crushed 850,000 tonnes of sugarcane, -45% YoY. Decreasing supply helped sugar price to recover from the 2019's low before slightly decreasing in March due to slower demand from Covid-19.
- In Q1, QNS fulfilled 17% and 13% of its annual targets for revenue and PAT respectively. Q1 is usually the bottom for profits. Q1/2019's PAT only accounted for 11% of 2019's whole year PAT.

2020 outlook: Results are expected to recover after Covid-19 but 2020 will still be a difficult year for the sugar segment

- Soy milk is expected to recover from late Q2, when the Covid outbreak is controlled in our base case (in Q2/2020). Sugar-light soy milk will be an important revenue driver in 2H 2020. QNS also started to export soy milk to China since May, with an estimated volume of 1.7 mn liters in 2020.
- QNS will be importing raw sugar from Thailand (~30,000 tonnes) to produce RE sugar, thereby partly offsetting the loss in revenue of RS sugar (-33% YoY) due to the decline in sugarcane volume. Sugar's average selling price in 2020 is expected to increase 10% vs 2019's.

Valuation and recommendation

We believe 2020 will be the bottom for QNS's profit due to the Covid-19's impact and unfavorable weather for sugarcane. Despite that, QNS is already dominant in the branded soy milk segment. Hence potential still remains in the huge unbranded soy milk segment, premiumization trends (organic and sugar-light milk) as well as exports. For the sugar segment, while ATIGA allows QNS to freely import raw sugar to make RE sugar, it also increases pressure from imported RS sugar. Along with volatile sugarcane volume, we have a neutral view for the sugar business.

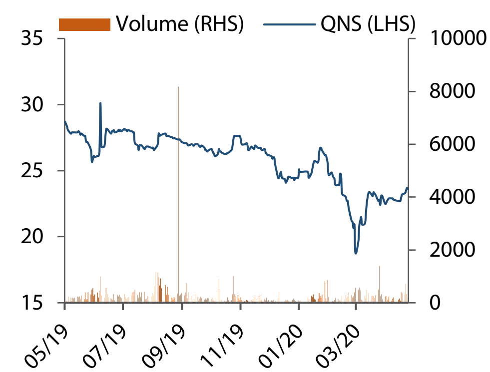
*Giving the healthy operating cash flow in the context of no significant CAPEX, we expect QNS to maintain a cash dividend rate of at least 25%, equivalent to a 70% payout ratio in the coming years. At the current market price, QNS's cash dividend yield is 11%. We use two valuation methods: FCFF and sum-of-the-parts to separately valuate each segment of the company. Our target price for the next 12 months is **VND 33,000/share** with a cash dividend of VND 2,500/share. Expected upside from May 18th's closing price is **51%**. We have a **BUY** recommendation on QNS.*

BUY	+51%
Target price (VND)	33,000
Current market price (VND)	23,500
Cash dividend (VND)*	2,500
**expected in 12 months*	

Stock Info	
Sector	Food & Beverage
Market Cap (VND billion)	8,174
Current Shares O/S	301,440,000
Avg. Daily Volume (in 20 sessions)	296,301
Free float (%)	75
52 weeks High	30,894
52 weeks Low	18,765
Beta	0.57

	FY2019	Current
EPS	4,313	4,120
EPS Growth (%)	5	-4,5
Diluted EPS	4,313	4,120
P/E	6.3	6.6
P/B	1.3	1.3
EV/EBITDA	5.0	5.1
Cash dividend yield (%)	11.1%	10.9%
ROE (%)	21.9	20.2

Price performance



Major Shareholders (%)	
Thanh Phat Limited	15.6
Vo Thanh Dang (chairman)	8.4
Remaining foreign room (%)	31.9

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ATIGA (ASEAN Trade in Goods Agreement) took effect from 01/01/2020, removing import quota for sugar from ASEAN countries, with import tax of 5%. Before ATIGA, import tax was 5% for under quota and 80-85% for over quota.

Exhibit 1: Q1/2020 Results

(VND Bn)	Q1-FY20	Q4-FY19	+/- (qoq)	Q1-FY19	+/- (yoy)
Net revenue	1,424	1,633	-12.7%	2.000	-28.8%
Gross profit	358	714	-49.9%	472	-24.1%
SG&A	231	208	10.8%	291	-20.7%
Operating income	127	506	-74.9%	180	-29.6%
EBITDA	431	546	-21.0%	461	-6.5%
EBIT	127	506	-74.9%	180	-29.6%
Financial expenses	22	19	19.5%	21	5.0%
- Interest Expenses	*22*	*18*	*19.4%*	*21*	*4.8%*
Dep. and amortization	304	40	660.9%	281	8.4%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	141	557	-74.6%	189	-25.3%
PAT	117	473	-75.3%	155	-24.6%
(*) Adjusted PAT	117	473	-75.3%	155	-24.6%

Source: QNS, Rong Viet Securities

Exhibit 2: Q1/2020 Performance Analysis

Particulars	Q1-FY20	Q4-FY19	+/- (qoq)	Q1-FY19	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	25.1%	43.8%	-1,860 bps	23.6%	+150 bps
EBITDA Margin	30.3%	33.4%	-320 bps	23.1%	+720 bps
EBIT Margin	8.9%	31.0%	-2,210 bps	9.0%	-10 bps
Net Margin	8.2%	29.0%	-2,080 bps	7.7%	+50 bps
Adjusted Net Margin	8.2%	29.0%	-2,080 bps	7.7%	+50 bps
Turnover *(x)					
-Inventories	4.5	5.1	-0.6	7.6	-3,1
-Receivables	22.7	25.6	-2.9	18.9	3,9
-Payables	5.7	4.0	1.7	7.4	-1,8
Leverage (%)					
Total Debt/ Equity	39.8%	39.7%	+10 bps	49.9%	-1,010 bps

Source: Rong Viet Securities

Exhibit 3: Q2/2020 Performance Forecast

Particulars (VND Bn)	Q2-FY20	+/- qoq	+/- yoy
Revenue	1,854	+29%	-11%
Gross profit	584	+63%	-10%
EBIT	370	+191%	-15%
NPAT	311	+167%	-15%

Source: Rong Viet Securities

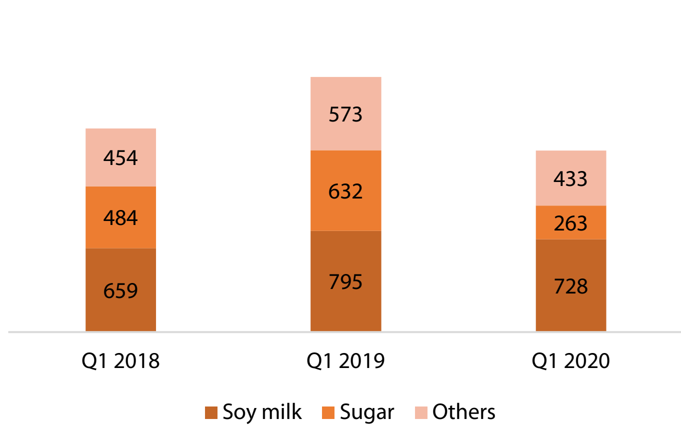
Q2/2020 comment

Covid-19 will still heavily impact domestic consumption in Q2, especially in April when the social distancing took place. We project selling volume of soy milk and sugar to decline 10% and 30% YoY respectively. Increases in average selling price of 4% for soy milk and 10% for sugar will limit revenue drop of just 6.4% and 23% for each segment respectively.

Update

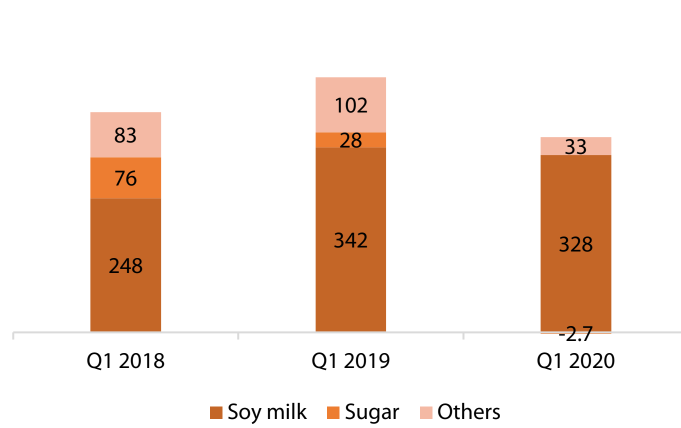
Q1/2020 result – Revenue declined across all segments due to the negative impact of Covid-19

Figure 1: Revenue breakdown (VND bn)



Sources: QNS, Rong Viet Securities

Figure 2: Gross profit breakdown (VND bn)



Sources: QNS, Rong Viet Securities

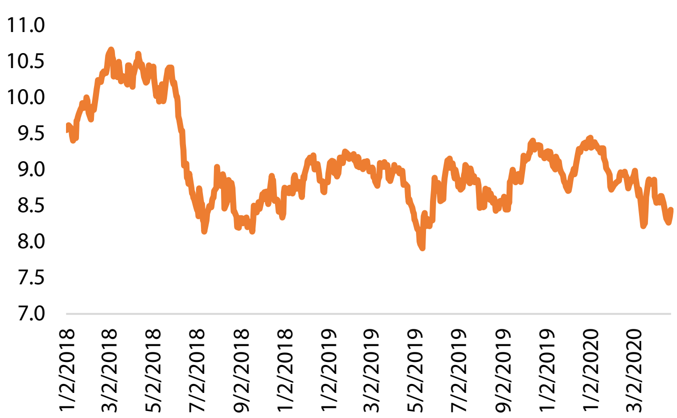
For Q1/2020, QNS recorded revenue of VND 1,424 bn, -29% YoY. Gross margin improved 150 bps to 25.1%. PAT reached VND 116.7 bn, -25% YoY. Details on each segment below:

Soy milk: Accounted for 51% of sales and 92% of gross profit.

Due to Covid-19, QNS's soy milk revenue declined 8.5% in Q1/2020. Average selling price increased nearly 4% and selling volume went down 12% YoY which was in line with the overall soy milk market. Overall, after the recovery in 2019, the milk market in general and the soy milk segment in particular are suffering from Covid-19 since consumers are limiting going for shopping

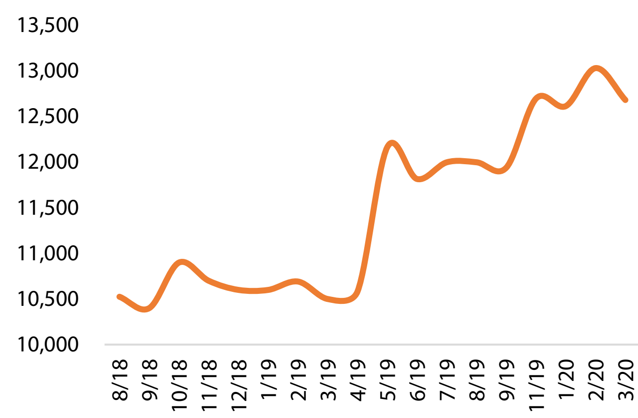
Gross margin was 45%, +200 bps YoY as a result of a slight decrease in soybean prices and an increase in soy milk selling prices, despite an increased in sugar prices.

Figure 3: Global soybean prices (USD/bushel)



Source: Bloomberg

Figure 4: RS sugar price in Vietnam (VND/kg)

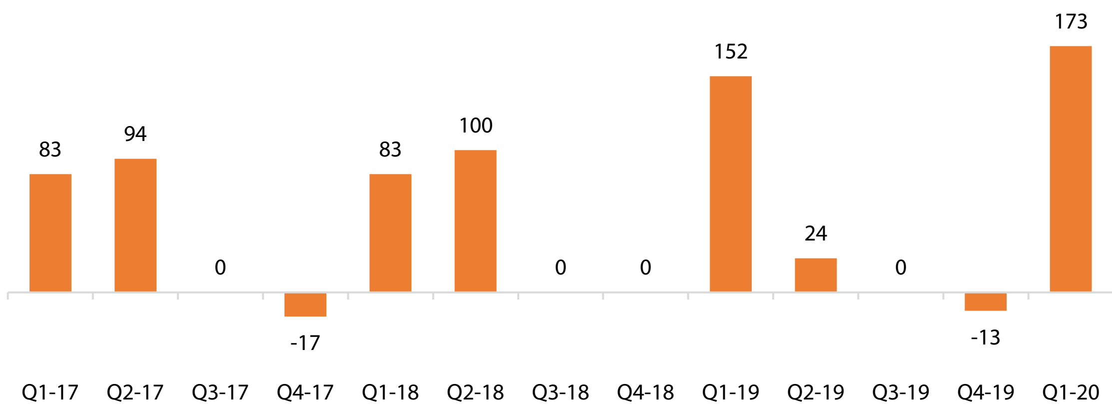


Sources: VSSA, Rong Viet Securities

Sugar: Accounted for 18% of sales while gross profit recorded a VND 2.7 bn loss, mainly from depreciation.

Net revenue dropped by 58% as a result of stumbling selling volume (-70%) YoY, mostly caused by weak demand from food & beverage producers, even though sugar prices increased by 17% in Q1 YoY. Additionally, depreciation costs increased 15% YoY due to the fact that QNS booked all of its depreciations for the RS factories in the first three months instead of four months as in last year, given less sugarcane crushing days in 2020. Previously, 2017 and 2018 had the sugarcane crushing season extended to June, therefore depreciation was evenly distributed to the first two quarters.

Figure 5: QNS's depreciation in the sugar segment (VND bn)



Sources: QNS, Rong Viet Securities

Other segments (beer, mineral water, candy, biomass) recorded revenue of VND 433 bn (-24% YoY) and gross profit of VND 33 bn (-68% YoY). For biomass, as bagasse volume decreased in Q1/2020 it only generated VND 65 bn in revenue which was a lot lower than Q1/2019's number of VND 163 bn. As of electricity's selling price, the Government decided to increase the buying price from biomass projects, taking effect from April 25th 2020. Accordingly QNS can now sell its electricity output at VND 1,634/kWh compared to VND 1,220/kWh.

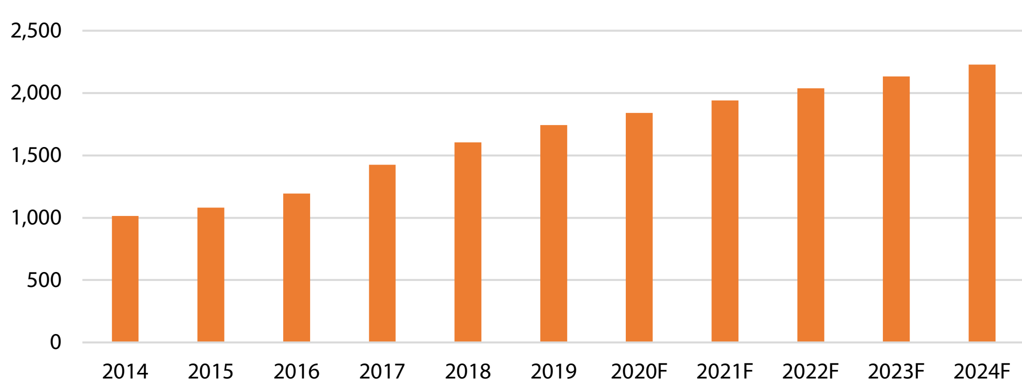
2020 Outlook

Soy milk – launching new products domestically as well as exporting to China

Expecting the pandemic outbreak to soon come to an end, the soy milk market will recover from late May. QNS plans to launch two new product lines in the coming Q3 which will be sugar-light ones. Sugar-light soy milk was initially introduced in late 2019 by two new products, by now these products' contribution to total soy milk sales has reached nearly 10%. We expect the coming products to be important drivers, helping soy milk revenue to recover from Q3 onwards.

Exporting to China: QNS plans to introduce many new products in China from May 2020, targeting to quickly gain relatively wide coverage over the South and East Coast regions of China, where make up over 80% of China's soy milk consumption. As the China-based business is only in the initial development phase as well as not having enough information, our forecast temporarily has not factored contribution from China yet. Regardless, in the long term, we believe China is a potential market for QNS, coming from (1) This is a huge market and is estimated to consistently grow in coming years (figure 6), (2) extremely fragmented market since unbranded soy milk is still dominating and (3) rising of middle and affluent classes to push consumption for healthy products.

Figure 6: Chinese soy milk consumption (USD mn)



Source: Euromonitor

For 2020, we estimate that QNS's soy milk revenue will reach VND 4,134 bn (-3% YoY) with selling volume of 264 mn liters (-5% YoY) and average the selling price will increase 2%, equivalent to VND 15,650/liter. Gross margin will go down 130 bps to 43.6% due to rising sugar prices.

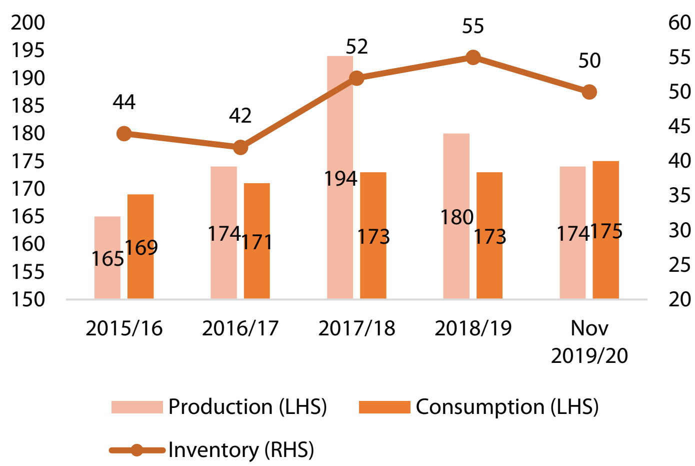
Sugar – expect sugar prices go back up after Covid-19 ends but 2020 will still be a difficult year since volume stumbles

World's sugar price crashed due to Covid-19: In the 2019/2020 season, global volume decreased by six million tonnes (-3%) and inventory decreased by five million tonnes as a result of bad weather in Brazil and India as well as the fact that sugarcane factories in Brazil were shifting from making sugar to ethanol due to low sugar prices. Consequently, sugar price bounced back sharply from Q4/2019 till before the Covid-19 breakout globally (figure 8). Weakening sugar demand caused a sudden drop in price.

Vietnam's sugar price is heavily dependent on Thailand, the origin of most of smuggled sugar in Vietnam. In the 2019/2020 season, Thailand's sugar volume is expected at only 10.5 million tonnes, which is 28% lower than the previous season and also the nine-year lowest. In Vietnam, sugarcane area falling due to low sugar price in 2019 and drought have dampened sugarcane volume. QNS's sugar consumption volume in 2020 is estimated of only 87,000 tonnes, decreasing nearly 40% YoY.

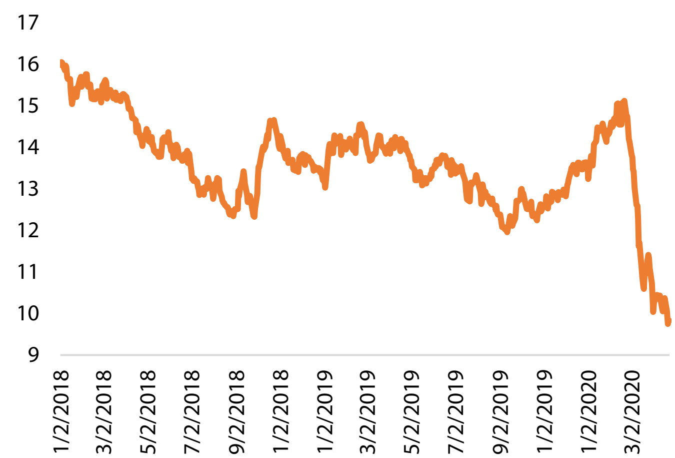
Therefore, we believe despite that official imported value to Vietnam will increase sharply post ATIGA, shortage in production from both domestic and global manufacturers (especially in Thailand) will help sugar price to recover after Covid-19 is put under control and demand from food & beverage manufacturers picks up. Average selling price in 2020 is forecasted to increase 10% compared to 2019.

Figure 7: World sugar production, consumption and inventories (million tonnes)



Source: United States Department of Agriculture

Figure 8: World sugar price (US cent/lb)



Source: Bloomberg

Starting RE sugar production: QNS has plan to import about 30,000 tonnes of raw sugar from Thailand to make RE sugar on the new plant. In Vietnam, RE sugar is not yet popular in the retail channel and retail consumers have not paid attention to brand name nor sugar quality. RE sugar is now mostly consumed by food & beverage manufacturers who will be the major target client for QNS. Due to RE sugar's short storage time (under three months), most of the competition will not be coming from imported sugar but other domestic sugar producers who can also import cheap raw sugar to make RE, after import quotas are removed under ATIGA.

We project total revenue of the sugar segment to reach VND 1,357 bn in 2020 (RE accounts for VND 361 bn), declining 9% YoY. Consumption volume will be 117,000 tonne of which 87,000 is RS and 30,000 is RE. Gross margin is expected at 4.6%, versus 10.4% in 2019 due to increase in depreciation/revenue since the factories operating at low capacities.

For the biomass segment, selling price this year will increase 28% compared to 2019, reaching VND 1,634/kWh. On the other hand, the bagasse volume will decrease 45% YoY. We forecast the biomass revenue (excluding internal revenue) for 2020 of only VND 57 bn and PAT loss of VND 61 bn.

Attractive cash dividend yield with stable operating cash flow and healthy balance sheet

In 2019, QNS paid a cash dividend of 30% (AGM's guidance of at least 15%). We expect a stable operating cash flow and no significant foreseen CAPEX demand, QNS will be able to maintain a cash dividend of at least 25%, equivalent to a 70% payout ratio. At the current market price, QNS's cash dividend yield is around 11%.

VND bn	2017	2018	2019	2020F	2021F
Cash & cash equivalents	1,279	2,117	2,875	3,296	3,635
Debt / Owner equity	0.35	0.32	0.26	0.24	0.19
Net profit	1,027	1,240	1,292	1,041	1,244
Operating cash flow	1,625	1,540	1,645	1,492	1,686
Cash dividend (VND)	1,500	1,500	3,000	2,500	3,000
Payout ratio	30%	30%	70%	74%	74%

Valuation

We combine two valuation methods: FCFF and sum-of-the-parts to separately valuate each segment. Our target price for the next 12 months is VND **33,000/share** with a cash dividend of VND 2,500/share. Expected upside from May 18th's closing price is **51%**.

FCFF		SOTP		
Risk-free rate	2.7%	**Business segment**	**Method**	**Valuation**
Market premium	15.3	Soy milk	P/E 9x	23,063
Beta	0.93	Sugar	P/E 5,5x	563
Risk premium (due to only listing on UPCOM)	1%	Biomass	FCFF	1,697
Cost of equity	17.9%	Others (beer, mineral water, candy)	P/E 7x	4,731
Cost of debt	5%			
Debt/Owner equity	0.38			
WACC	**14.1%**			
Valuation (FCFF)	**36,000**	**Valuation (SOTP)**		**30,000**
Target price, VND (50% FCFF, 50% SOTP)				**33,000**

VND Billion

INCOME STATEMENT	FY2018	FY2019	FY2020F	FY2021F
Revenue	8,031	7,681	7,177	8,175
COGS	5,737	5,224	5,044	5,759
Gross profit	**2,294**	**2,456**	**2,133**	**2,416**
Selling Expense	762	785	758	798
G&A Expense	176	214	214	229
Finance Income	87	138	169	186
Finance Expense	96	77	93	84
Other profits	57	26	26	26
PBT	**1,405**	**1,543**	**1,262**	**1,517**
Prov. of Tax	165	251	221	273
Minority's Interest	0	0	0	0
PAT to Equity S/H	**1,240**	**1,292**	**1,041**	**1,244**
EBIT	1,357	1,457	1,160	1,389
EBITDA	1,850	1,936	1,740	1,982

%

FINANCIAL RATIO	FY2018	FY2019	FY2020F	FY2021F
Growth (%)				
Revenue	5.2%	-4.4%	-6.6%	13.9%
Operating Income	18.0%	4.6%	-10.1%	13.9%
EBITDA	17.7%	7.4%	-20.4%	19.7%
PAT	20.8%	4.1%	-19.4%	19.5%
Total Assets	14.3%	13.1%	3.1%	1.1%
Equity	19.4%	20.9%	5.0%	4.6%
Profitability (%)				
Gross margin	28.6%	32.0%	29.7%	29.6%
EBITDA margin	23.0%	25.2%	24.2%	24.2%
EBIT margin	16.9%	19.0%	16.2%	17.0%
Net margin	15.4%	16.8%	14.5%	15.2%
ROA	15.5%	14.3%	11.2%	13.2%
ROE	23.2%	20.0%	16.8%	19.3%
Efficiency				(lần)
Receivable Turnover	17.2	27.4	20.5	20.5
Inventory Turnover	9.8	7.9	8.4	8.3
Payable Turnover	6.8	6.4	6.3	6.3
Liquidity				(lần)
Current	1.2	1.5	1.8	2.1
Quick	1.0	1.3	1.5	1.8
Finance Structure (%)				
Total Debt/Equity	32.3%	25.7%	24.1%	18.5%
Current Debt/Equity	32.3%	25.7%	24.1%	18.5%
Long-term Debt/Equity	0.0%	0.0%	0.0%	0.0%

VND Billion

BALANCE SHEET	FY2018	FY2019	FY2020F	FY2021F
Cash and cash equivalents	418	215	297	635
Short-term investments	1,699	2,660	3,000	3,000
Accounts receivable	468	281	350	398
Inventories	585	661	601	691
Other current assets	8	24	25	26
Property, plant & equipment	4,568	4,960	4,804	4,427
Acquired intangible assets	34	23	14	8
Long-term investments	0	0	0	0
Other non-current assets	222	225	236	248
Total assets	**8,002**	**9,048**	**9,327**	**9,433**
Accounts payable	842	822	804	917
Short-term borrowings	1,727	1,665	1,637	1,314
Long-term borrowings	0	0	0	0
Other non-current liabilities	19	19	20	21
Bonus and Welfare fund	52	66	66	66
Technology-science, dev. fund	8	5	5	5
Total liabilities	**2,649**	**2,578**	**2,532**	**2,324**
Common stock and APIC	3,214	3,923	3,981	3,981
Treasury stock (enter as -)	-834	-834	-834	-834
Retained earnings	2,467	2,813	3,028	3,280
Other comprehensive income	0	0	0	0
Inv. and Dev. Fund	506	568	620	682
Total equity	**5,353**	**6,470**	**6,795**	**7,109**
Minority Interest				

VALUATION RATIO (*)	FY2018	FY2019	FY2020F	FY2021F
EPS (dong)	4,115	4,313	3,385	4,043
P/E (x)	8.3	6.3	6.8	5.7
BV (dong)	21,733	21,465	22,543	23,587
P/B (x)	1.9	1.3	1.0	1.0
DPS (dong/cp)	1,500	3,000	2,500	3,000
Dividend yield (%)	3.6%	11.1%	10.9%	13.0%

VALUATION MODEL	*Price*	*Weight*	*Average*
FCFF	36,000	50%	18,000
SOTP	30,000	50%	15,000
Target price (VND)			**33,000**

VALUATION HISTORY	*Price**	*Recommendation*	*Period*
12/05/2017	44,000	Buy	Long term
11/12/2018	44,500	Buy	Long term
05/31/2019	40,000	Buy	Long term
05/19/2020	33,000	Buy	Long term

Previous target prices were adjusted:
*QNS paid stock dividend in May 2018 and May 2019 at 10:2 ratio
*In June 2019, QNS issued 5,851,491 shares to employees

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%

ABOUT US

RongViet Securities Corporation (RongViet) was established in 2007. licensed to perform the complete range of securities services including brokerage. financial investment. underwriting. financial and investment advisory and securities depository. RongViet now has an operating network that spreads across the country. Our major shareholders. also our strategic partners. are reputable institutions. i.e Eximbank. Viet Dragon Fund Management. etc... Along with a team of the professional and dynamic staffs. RongViet has the man power as well as the financial capacity to bring our clients the most suitable and efficient products and services. Especially. RongViet was one of the very first securities firms to pay the adequate attention to the development of a team of analysts and the provision of useful research report to investors.

The **Analysis and Investment Advisory Department** of RongViet Securities provides research reports on the macro-economy. securities market and investment strategy along with industry and company reports and daily and weekly market reviews.

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