REFRIGERATION ELECTRICAL ENGINEERING JSC (HSX:REE)

Effective Investments Continue to Drive Earnings Growth

(VND bn)	Q4-FY17	Q3-FY17	*+/- qoq*	Q4-FY16	*+/- yoy*
Net revenue	1,668	1,083	53.97%	1,302	28.1%
PAT	424	398	6.47%	654	-35.2%
EBIT	685	374	83.34%	567	20.8%
EBIT Margin	41%	35%	6.6 bps	434%	-2.4 bps

Sources: REE, RongViet Securities

2017 Performance: Growth Seen in All Business Segments

- Utilities contributed the largest share of total NPAT (45%).
- This segment, including power and water, was also the main driver for the growth in the bottom line with key catalysts including: (1) PPC, (2) hydropower, and (3) Thu Duc III water plant, operating at full capacity.
- Revenues and profits from the office-leasing segment increased by 0.8% YoY and 0.7% YoY, respectively. Total leasable area fell by 4% due to the re-construction of the e.town 5 building.

2018 Outlook: Power and Water Utilities and Real Estate Continue to Drive Growth

Our forecast is for 13% revenue growth and 23% NPAT growth. This potential rise in 2018 earnings would come from key business segments including power and water utilities (+37% YoY), and real estate development (+47% YoY).

REE's e.town Central building came into operation in late 2017. The expected average occupancy rate in 2018 will only be 50%. We estimate that the building will start to generate profits from 2019.

Valuation and Recommendation:

With strong experience in management in that sector and the company's constructive attitude toward shareholders, we consider REE as an efficient way to get exposure to the power and water utilities sector. In 2018, the catalyst in this business segment will be the contribution from new associate companies including CHP and VCW, which account for 11% of its earnings. Meanwhile, VIID and SGR with expected earnings growth of 60% and 43%, respectively, would contribute 11% to the total NPAT of VND 1,683 billion, corresponding to EPS of VND 5,374.

*In addition, since REE's prospect shows that its current business model could ensure stable growth rate of 10 – 15% YoY, the stock could be re-rated to a P/E ratio of about 10x. However, we also notice that the long-term prospect of VIID, a subsidiary that accounts for 10% of REE's earnings, is still unclear. Therefore, we decide to discount the forward P/E ratio by 10%. Our target price is VND 48,400 per share. This, coupled with a VND1,600 cash dividend, yields a total return of 33% (calculated based on the closing price on 20 April). Therefore, we have a **BUY** on REE.*

BUY

CMP (VND)	37,600
Target Price (VND)	48,400
Cash Dividend (VND)*	**1,600**

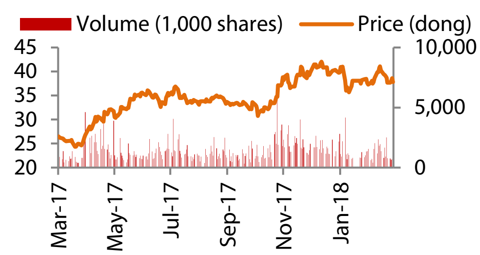
** Expected in the next 12 months*

Stock Info

Sector	General Industrials
Market Cap (VND Bn)	11,689
Current Shares O/S	310,058,841
Beta	0.8
Free float (%)	2.7
52 week High	43,800
52 week Low	24,650
Avg. Daily Volume (20 sessions)	1,200,176

	FY2017	Current
EPS	4,441	4,441
EPS Growth (%)	26.22	26.22
Adjusted EPS	4,441	4,441
P/E	9.34	9.34
P/B	1.48	1.48
EV/EBITDA	10.2	10.2
Cash dividend	1,600	1,600
ROE (%)	17.1	17.1

Price performance



Major Shareholders (%)

Platinum Victory Pte Ltd	23.9
Nguyen Thi Mai Thanh	7.3
Nguyen Ngọc Hai	5.5
State (HFIC)	5.3
Apollo Asia Fund Ltd.	5.9
Foreign ownership room (%)	0

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Exhibit 1: Q4/2017 Results

(VND bn)	Q4-FY17	Q3-FY17	+/- (qoq)	Q4-FY16	+/- (yoy)	FY17	+/-(yoy)
Net revenue	1,668	1,083	53.9	1,302	28.1	4,995	36.5
Gross profit	542	312	73.8	428	26.6	1,429	21
SG&A	143	62	131.8	139	2.9	336	8.8
Operating income	494	444	11.1	723	-31.7	1,712	25.1
EBITDA	717	401	78.8	604	18.8	1,223	20.9
EBIT	685	374	83.3	567	20.8	1,093	25.3
Financial expenses	100	34	193.3	21	369.9	275	306.1
- Interest Expenses	43	22	98.2	18	134.2	105	73.9
Dep. and amortization	31	14	124.5	36	-13.7	130	-6.8
Non-recurring items (*)							
Extraordinary items (*)							
PBT	497	448	11.1	723	-31.2	1,721	25.1
PAT	424	398	6.5	654	-35.2	1,523	29.8
(*) Adjusted PAT	424	398	6.5	654	-35.2	1,523	29.8

Source: REE, RongViet Securities

Exhibit 2: Q4/2017 Performance Analysis

Particulars	Q4-FY17	Q3-FY17	+/- (qoq)	Q4-FY16	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	32.5	28.8	3.7 bps	32.9	-0.4 bps
EBITDA Margin	42.9	37.0	5.9 bps	46.4	-3.4 bps
EBIT Margin	41.1	34.5	6.6 bps	43.6	-2.5 bps
Net Margin	25.4	36.8	-11.3 bps	50.3	-24.9 bps
Adjusted Net Margin	25.4	36.8	-11.3 bps	50.3	-24.9 bps
Turnover *(x)					
-Inventories	2.8	1.9	0.9	3.3	-0.5
-Receivables	5.6	3.2	2.4	3.5	2.1
-Payables	1.9	1.3	0.6	1.8	0.1
Leverage (%)					
Total Debt/ Equity	33.7	34.7	-1 bps	33.6	0.1 bps

Source: REE, (*) Annualized turnover

Exhibit 3: FY2018 Forecast

Particulars (VND bn)	2018	+/- YoY
Revenue	5,659	13%
Gross profit	1,793	25%
EBIT	1,398	28%
NPAT	1,698	23%

Source: REE, RongViet Securities

Updates:

Cost management becomes the key theme for the mechanical & electrical engineering segment (M&E)

The total backlog transferred from 2017 is VND 5,405 billion while the expected new order book value is VND 2,400 billion – VND 3,000 billion. Among this backlog, the Van Don Airport project with contract value of over VND 1,000 billion is expected to be completed in 2018. We expect net margins of this segment to remain high at about 12% in 2018, translating to NPAT of VND 322 billion. In addition, with prospect of more fierce competition and rising material prices, the key theme of M&E segment in 2018 would be cost management, especially in purchasing process.

Exhibit 4. Target for M&E in 2018

	2017 (VND Bn)	2016 (VND Bn)	Change (%)	Plan 2018 (VND Bn)
New orders	3,728	2,058	+81.1	2,400
Revenue	2,377	1,739	+36.7	2,700
Profit after tax	322	296	+8.7	240

Source: REE

Moreover, REE tends to be very selective in choosing projects and choosing key-investors. Therefore, we believe that the company would be able to maintain the current net margin of 12% - 13% and growth of 10% - 15% in the next few years.

Office leasing segment is expected to remain flat in 2018 but grow from 2019 – 2020

In 2018, REE targets this to grow by 27% YoY in revenues while NPAT will remain flat. This is due to the e.town Central office building in district 4, which came into operation in late 2017 and will contribute to revenue growth from 2018 on. However, with low expected occupancy rate of about 50% in the first year, the building may only reach its break-even point in 2018.

Exhibit 5. Targets for office leasing segment in 2018

	2017 (VND Bn)	2016 (VND Bn)	Change (%)	Plan 2018 (VND Bn)
Revenue*	511	507	+0.8	656
Profit after tax	278	276	+0.7	280

**Revenue excludes electricity charges collected from tenants*

Source: REE

In addition to e.town Central, REE also has called e.town 5, an office building that is still under construction and will be completed in late Q2 2018. Accounting for a third of REE's total leasable area, these two buildings are expected to become the key catalyst for this segment in 2019.

Exhibit 6. REE's new office buildings compared to its current portfolio

	Location	Leasable area (m^2)	Price (USD/m^2)
REE's current leasable area	Tan Binh district; District 1, 3, 4, 5	98,829	17 - 21
e.town Central	11 Doan Van Bo st., dist. 4	35,000	25
e.town EW	364 Cong Hoa st., Tan Binh dist.	16,000	17

Source: REE

Target for real estate development is based only on visible sources

This is the only segment that REE's management targeted for strong growth in 2018 with NPAT rising by 48% YoY.

Exhibit 7. Targets for real estate development in 2018

	2017 (VND Bn)	2016 (VND Bn)	Change (%)	Plan 2018 (VND Bn)
Revenue	407	226	+80.1	790
Profit after tax	128	121	+5.8	189

Source: REE

However, earnings from this segment are quite certain since many projects have been completed. Therefore, we believe that this strong growth is achievable.

Exhibit 8. Earning sources from real estate

Project	Sub/JV	Type	Profit contribution to REE(VND B)	Note
Ngoc Bao Vien (Quang Ngai)	VIID (subsidiary)	villas, town house	100	• Sales completed
Duc Giang (Hanoi)	VIID (subsidiary)	Land, villas, town house	39	• Scale: 14 ha land bank • Infrastructure construction completed • Sales proceed from 2018
An Phu Dong & Saigon Riverside	Saigonres (joint-venture)	Apartment,	50 - 60	

Source: REE, SGR

VIID is acquiring more land bank to develop more projects. Investors may have to wait for few years to see a sustainable project pipeline of this company. However, their joint venture, Saigonres (SGR) has been listed on HOSE to prepare for raising additional capital. SGR, with 10 projects in its portfolio, is expected to grow quickly in the next few years, which would contribute to the earnings of REE as well.

Exhibit 9. Target for 2018 of power and water utilities segment

	2017 (VND Bn)	2016 (VND Bn)	Change (%)	Plan 2018 (VND Bn)
Total investment cost in power, water	6,475	5,603	+15.6	-
Profit after tax	633	352	+79.8	617

Source: REE

Regarding this segment, the 2018 target was built on a scenario that (1) earnings of hydropower would fall relative to that of 2017 and (2) PPC, the biggest investment in thermal power, would no longer have extraordinary income in 2018. However, the movement in the electricity market in the first months of 2018 was very favorable for REE:

- Demand grew at 12% YoY, up 5 percentage points versus Q1 2017
- Hydropower supply declined
- Some large power projects were delayed/had trouble such as Duyen Hai 3 and expansion of TPP, Vinh Tan 2 TPP. As a result, CGM prices were much higher than expectations, which helped hydropower companies maintain their core earnings

In addition, REE also has Central Hydropower JSC (CHP) and Song Da Water Investment JSC (VCW), which were eligible to become its joint ventures from late December 2017. Therefore, they will start contributing to REE's earnings from 2018 and become a catalyst for the growth of this business segment.

Exhibit 10. REE's subsidiaries and joint ventures in power and water utilities

Power segment

Company	2017 NPAT (VND Bn)	(%) Ownership @ 1/1/2017	(%) Ownership @ 31/12/2017	Key business segment	Ownership type
Tra Vinh Rural Electric Development JSC (DTV)	20	66.5	66.3	Electricity infrastructure	Subsidiary
Thac Ba Hydropower JSC (TBC)	166	60.4	60.4	Electricity production	Subsidiary
Vinh Son - Song Hinh Hydropower (VSH)	286	21.0	21.0	Electricity production	Associates
Thac Mo Hydropower JSC (TMP)	311	42.6	42.6	Electricity production	Associates
Song Ba Ha Hydropower JSC (SBH)	665	25.8	25.8	Electricity production	Associates
Srok Phu Mieng Hydropower JSC (ISH)	74	34.3	34.3	Electricity production	Associates
Binh Dien Hydropower JSC	81	25.5	25.5	Electricity production	Associates
Central Hydropower JSC (CHP)	410	0.0	20.1	Electricity production	Associates
Pha Lai Thermal Power JSC (PPC)	836	23.5	23.4	Electricity production	Associates
Ninh Binh Thermal Power JSC (NBP)	44	29.4	29.4	Electricity production	Associates
Thuan Binh Wind Power JSC (TBWP)	-65	0.0	25.0	Electricity production	Associates

Water segment

Company	2017 NPAT (VND Bn)	(%) Ownership @ 1/1/2017	(%) Ownership @ 31/12/2017	Key business segment	Ownership type
Nha Be Water Supply JSC (NBW)	12	20.0	20.0	Water	Associates
Thu Duc B.O.O Water Treatment Plant (Thu Duc B.O.O)	104	42.1	42.1	Water	Associates
Tan Hiep II Water Treatment Plant (Tan Hiep II)	9	32.0	32.0	Water	Associates
Thu Duc Water Supply JSC (TDW)	15	44.2	44.2	Water	Associates
Thu Duc III Water Treatment Plant (Thu Duc III)	110	40.0	40.0	Water	Associates
Gia Dinh Water Supply JSC (GDW)	16	20.1	20.1	Water	Associates
Trung An Water Supply JSC (TAW)	2	29.0	0.0	Water	Associates
Song Da Water Investment JSC (VCW)	168	0.0	34.7	Water	Associates

Source: REE, RongViet Securities

The Ministry of Industry and Trade (MoIT) decided that Vietnam Electricity Group (EVN) would repay forex losses that incurred in 2015. The Decision is based on Circular 56, which allows power plants to transfer their forex losses to EVN. The repayment is estimated at about VND 125 billion for PPC and VND 300 billion for QTP. Therefore, we estimate that total earnings in 2018 for PPC could be above VND 1,000 billion, a record level for this power plant.

Actual 2018 earnings could surpass REE's target by over 20%

Because of the above reasons, we estimate that the power & water segment could contribute to REE's NPAT by VND 869 billion (+37% YoY), while real estate development contributes VND 189 billion (+47% YoY). This would also become an important catalyst for total earnings to reach VND 1,698 billion (+23% YoY) in 2018, corresponding to an EPS of 5,423 VND/share.

Exhibit 11. Outlook for 2018 NPAT (VND Bn)

Business segment	2017 result	2018 official plan	Change (%)	2018 expected (see footnote)	%expectation/ plan	Note
M&E	322	240	-25%	322	134%	• The conservative plan was due to higher expected material prices. However, REE is confident that they could manage a similar NPAT as that of 2017
Reetech	37	43	16%	43	100%	
Power & Water	633	617	-3%	869	141%	• Significant contribution from new joint venture companies including CHP, VCW. • PPC would book another VND 125 billion in its NPAT as the MoIT decided to repay FX losses in 2016 for power plants
Office Leasing	278	280	1%	276	99%	• The new office building will break-even in 2018, resulting in a rise in revenue and a flat bottom line
Real Estate	128	189	48%	189	100%	• NPAT by projects & companies: o SaigonRes (SGR): VND 50 - 60 billion o Ngoc Bao Vien (VIID): VND 100 billion o Duc Giang (VIID): VND 39 billion
Others	-21	-	-	-	-	
Total	**1,377**	**1,369**	**-1%**	**1,698**	**124%**	• REE also expects that NPAT could increase by at least 10 – 15% YoY in 2018

(*) 2018 expected are our projection for 2018

Source: REE, RongViet Securities

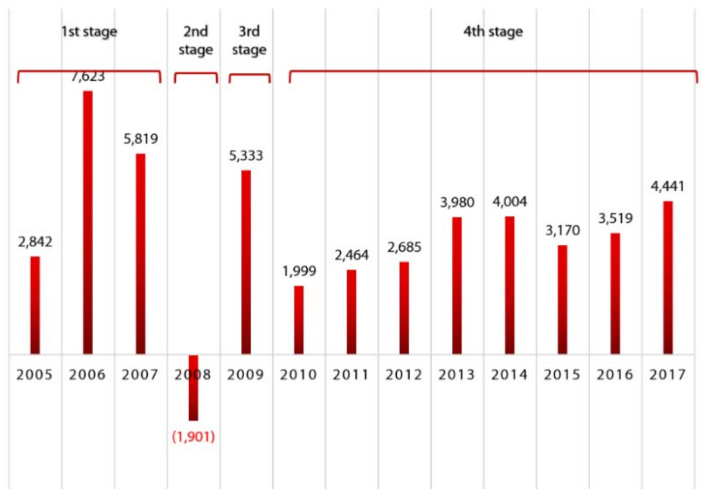
Valuation and Recommendation:

With strong experience in management in that sector and the company's constructive attitude toward shareholders, we consider REE as an efficient way to get exposure to the power and water utilities sector. In 2018, the catalyst in this business segment would be the contribution from new affiliates including CHP (VND 35 billion) and VCW (VND 57 billion). Meanwhile, VIID and SGR, with expected earnings growth of 60% and 43%, respectively, would become the key driver for total NPAT to reach VND 1,698 billion, corresponding to an EPS of VND 5,423.

*In addition, since REE's prospect shows that its current business model could ensure stable growth rate of 10 – 15% YoY, the stock could be re-rated to get to a P/E ratio of about 10x. However, we also notice that the long-term prospect of VIID, a subsidiary that accounts for 10% of REE's earnings, is still unclear without having details about its pipeline of projects. Therefore, we come up with a target price of VND 48,400 per share. This target price, coupled with a VND1,600 cash dividend, yields a total return of 33% (calculated based on the closing price on 20 April 2018). We have a **BUY** on the stock.*

Appendix 1: REE's EPS adjusted for dilution

Figure 1: EPS adjusted for dilution during 2012 - 2017

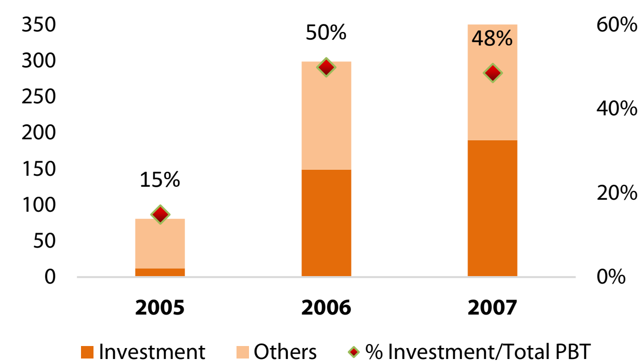


Source: REE, RongViet Securities

There are 4 important stages that REE had experienced from 2005 till now:

- 2005 - 2007: Strong growth with VNIndex
- 2008: Exposure to 2008 financial crisis
- 2009: Restructuring investment portfolio
- 2010 - now: Sustainable development

Figure 2: PBT breakdown in 2005 – 2007 (VND billion)

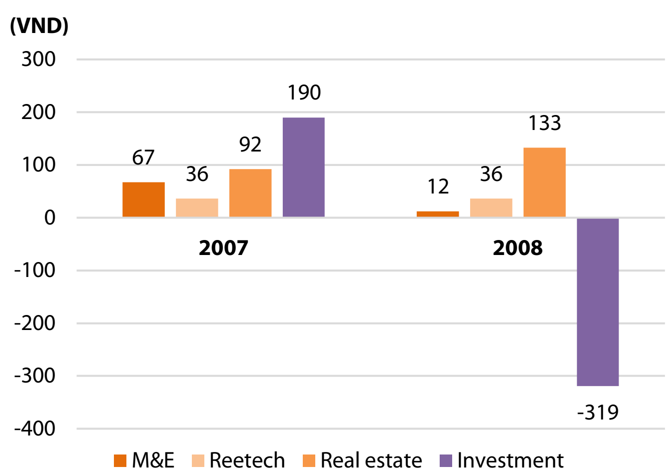


Source: REE, RongViet Securities

Strong growth with VNIndex

- This was when VNIndex grew strongly, and reached its peak (1,170 points).
- In this period, REE's portfolio with equal weight in short-term investment and long-term investment exposed strongly to stock market. As a result, besides core businesses (M&E, Reetech, office leasing), which accounted for around 50% NPAT, REE's investment activities saw a soaring profits, accounting for the other 50%. This boosted EPS to the highest level until now in 2006.

Figure 3: PBT breakdown in 2007-2008



Source: REE, RongViet Securities

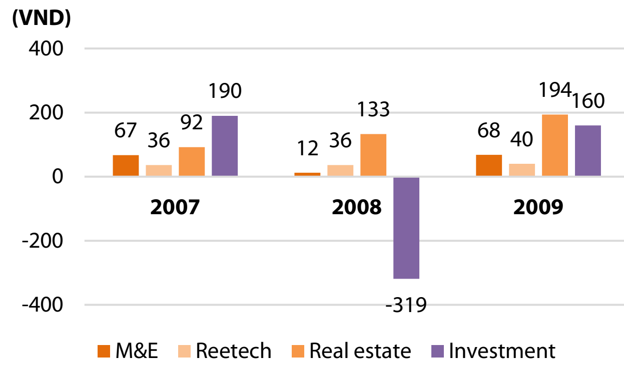
Exposure to 2008 financial crisis

- This was when VNindex went downhill. From 1170 points, it fell to 235 points in February 2009.
- REE's investment portfolio, which exposed largely to the market, experienced the same fate. From VND 190 billion PAT in 2007, it reported a negative PAT of 320 billion in 2008.
- The whole market's crisis also affected other business segments, decreasing their profits considerably.
- In 2008, REE reported a loss of 150 billion, which effectively made EPS 2008 negative.

Restructuring investment portfolio

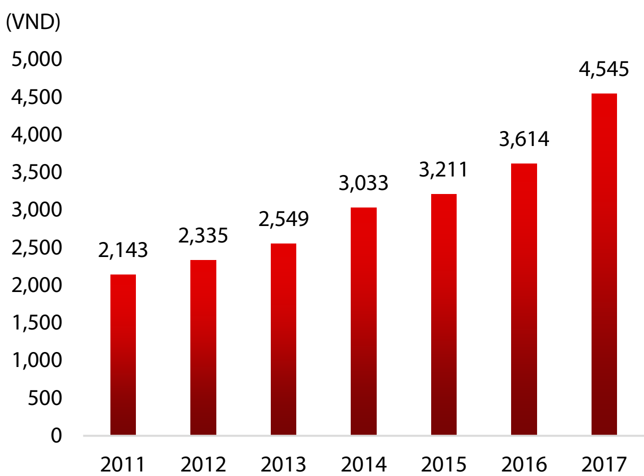
- Impact from the Financial Crisis continued.
- "Learn from yesterday", REE restructured its investment portfolio, selling all of its short-term investment since 2008. This started to take effect in 2009, when REE reported a gain of VND 160 billion from investment activities.
- Other core businesses started to regain their former glory as well, which boosted REE's EPS back to normal level.

Figure 4: PBT breakdown in 2007-2009



Source: REE, RongViet Securities

Figure 5: EPS adjusted for dilution and non-recurring factors

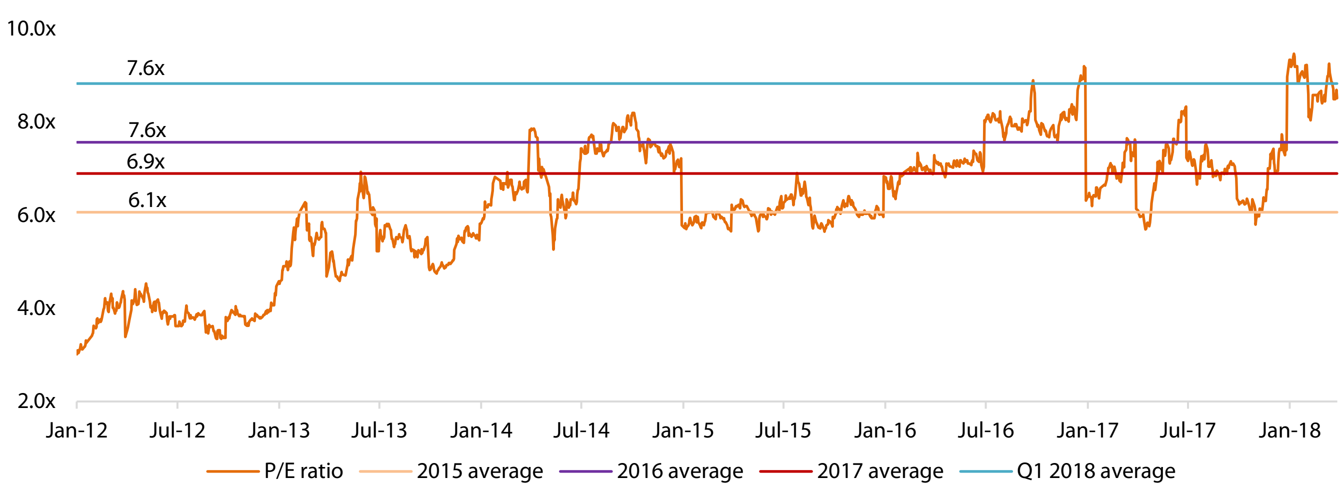


Source: REE, RongViet Securities

Sustainable development

- REE started their long-term vision of sustainable development focusing on 3 main areas:
  - M&E
  - Real estate
  - Power & water utilities
- The first step required huge additional equity, which effectively diluted EPS to a low level in 2010. Since then, the EPS has steadily improved, which prove that REE is going the right way to achieve their sustainable development.
- CAGR of adjusted EPS from 2011 to 2017 was around 13%;
- REE's investment portfolio focuses mainly on long-term investment with companies in defensive sectors including power and water utilities to reduce market risk;
- High rate of occupancy in all of its office buildings.

Appendix 2: REE's historical P/E ratio shows continuous improvement



Source: REE, RongViet Securities

VND billion

INCOME STATEMENT	FY2016	FY2017	FY2018F	FY2019F
Revenue	3,659	4,995	5,659	5,919
COGS	2,478	3,566	3,866	4,111
Gross profit	**1,182**	**1,429**	**1,793**	**1,808**
Selling Expense	89	95	120	126
G&A Expense	220	242	274	287
Finance Income	685	175	136	134
Finance Expense	64	275	296	279
Other profits	7	9	0	0
PBT	-121	719	842	840
Prov. of Tax	**1,380**	**1,721**	**2,081**	**2,090**
Minority's Interest	202	198	202	204
PAT to Equity S/H	80	146	180	153
EBIT	**1,097**	**1,377**	**1,698**	**1,734**
EBITDA	872	1,093	1,399	1,395

%

FINANCIALS	FY2016	FY2017	FY2018F	FY2019F
Growth				
Revenue	38.4	36.5	13.3	4.6
Operating Income	28.5	20.9	41.8	0.0
EBITDA	33.2	25.3	28.0	-0.3
PAT	28.6	25.5	23.3	2.1
Total Assets	26.1	25.4	7.6	6.2
Equity	13.0	12.3	14.8	13.2
Profitability				
Gross margin	32.3	28.6	31.7	30.5
EBITDA margin	27.7	24.5	30.7	29.3
EBIT margin	23.8	21.9	24.7	23.6
Net margin	30.0	27.6	30.0	29.3
ROA	9.6	9.6	11.0	10.6
ROE	15.3	17.1	18.4	16.6
Efficiency				
Receivable Turnover	3.2	4.4	3.7	3.6
Inventory Turnover	2.0	2.3	2.8	2.8
Payable Turnover	1.2	1.6	1.5	1.5
Liquidity				
Current	1.6	1.9	1.7	1.8
Solvency				
Total Debt/Equity	16.4	19.7	31.5	20.8
Current Debt/Equity	8.6	8.5	6.5	4.4
Long-term Debt/Equity	7.8	11.2	25.0	16.4

VND billion

BALANCE SHEET	FY2016	FY2017	FY2018F	FY2019F
Cash and cash equivalents	960	2,255	1,928	2,118
Short-term investments	749	517	595	749
Accounts receivable	1,148	1,131	1,528	1,657
Inventories	1,230	1,556	1,387	1,475
Other current assets	17	51	36	38
Property, plant & equipment	1,740	2,212	2,313	2,311
Acquired intangible assets	54	34	31	30
Long-term investments	5,377	6,274	7,395	7,815
Other non-current assets	113	123	121	135
Total assets	**11,397**	**14,295**	**15,380**	**16,328**
Accounts payable	2,001	2,242	2,647	2,814
Short-term borrowings	615	684	598	464
Long-term borrowings	561	899	2,309	1,710
Other non-current liabilities	159	366	384	403
Bonus and Welfare fund	2	1	18	35
Technology-science, dev. fund	0	0	0	0
Total liabilities	**3,675**	**5,601**	**5,357**	**4,963**
Common stock and APIC	4,151	4,151	4,151	4,151
Treasury stock (enter as -)	0	0	0	0
Retained earnings	2,766	3,642	4,835	6,062
Other comprehensive income	1	1	1	1
Inv. and Dev. Fund	238	240	233	226
Total equity	**7,156**	**8,034**	**9,220**	**10,440**
Minority Interest	**565**	**659**	**803**	**925**

VALUATION RATIO	FY2016	FY2017	FY2018F	FY2019F
EPS (VND/share)	3,519	4,441	5,423	5,535
P/E (x)	10.7	8.5	7.0	6.8
BV per share (VND)	23,080	25,912	29,735	33,670
P/B (x)	1.51	1.34	1.27	1.12
DPS (VND/share)	1,000	1,600	1,600	1,600
Dividend yield (%)	4.0	3.8	4.2	4.2
Stock valuation (using P/E)			48,400	
Target price (VND)			**48,400**	

VALUATION HISTORY	Price	Recommendation	Period
20/04/2017	32,800	Accumulate	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%

ABOUT US

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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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