October, 2017

Hang Xanh Motors Service JSC (HSX:HAX)

Rapid Growth Thanks To Expanding Market Shares

- Shareholder structure is a positive factor for the company's operation.
- Performance has been improved through out the years.
- Mercedes-Benz Vietnam (MBV) holds high gowth rate and continuously lead Vietnam's luxury car market.
- Policies of MBV affect HAX profit.

Valuation and Recommendation

Hang Xanh Motors Service JSC (HSX:HAX) is the only first authorized distributor of Mercedes-Benz (MBV) that is listed on HSX. Despite of having the smallest market share among all MBV's dealers, HAX has continuously reached many turning points in its business since 2013.

Along with the leading position in luxury car segment and prospective outlook of Mercedes-Benz in Vietnam, we find that the potential growth of HAX would remain great. Based on the new contributions from HAXACO Kim Giang (Ha Noi) and the upgrade of HAXACO Lang Ha, the company's revenue is expected to grow in 2017 and 2018 by 46.9% to VND4,229 billion and 22.2% to VND5,166 billion, respectively.

As a distributor, profit of HAX depends closely on MBV's policy. For instance, the changes in MBV's sales policy, cost escalation ascribed to interest expense, would challenge the revenue growth possibility for HAX despite having impressive sales results. As a result, we project that net profit of HAX would grow more slowly compared to the previous year and reach only VND79.9 billion (+2,5% YoY) in 2017 and VND89.5 billion (+11,9% YoY) in 2018. In other words, the average EPS in the next 2 years would be VND3,671 per share.

*According to the valuation methods P/E and P/S with the estimated two-year (2017–2018) average revenue and EPS, we rate **NEUTRAL** on HAX stock with the target price of **VND42,300 per share**. However, we also recommend investors to **MONITOR** this stock in the short term; based on the expectation that a large bonus from MBV would be recorded in the second half of this year. In the long term, investors should pay close attention to MBV's sales policy, which is less favorable, and HAX's unpredictable method in bonus recognition.*

Key financial ratios

Y/E Dec(VND Bn)	FY2015	FY2016	Q2 2017	FY2017F	FY2018F
Net revenue	1,821	2,880	1,035	4,229	5,166
%change	49.3	58.1	21	46.9	22.2
PAT	29	78	-9	80	89
% change	73	170.7	-182.0	2.5	11.9
Net margin (%)	1.6	2.7	-0.9	1.9	1.7
ROA (%)	10.2	13.3		9.8	8.8
ROE (%)	34.8	38.0		30.8	27.7
EPS (VND)	2,591	6,480		3,424	3,832
Adjusted EPS (VND)	1,234	3,340		3,424	3,833
Book value (VND)	11,630	21,184		16,488	20,320
Cash dividend (VND)	0	0		0	0
P/E (x)	6.8	6.3		11.5*	10.3*
P/BV (x)	1.5	1.9		2.4*	1.9*

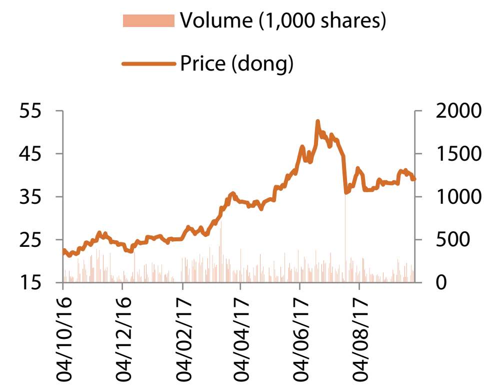
*Source: HAX, RongViet Research estimation, * Based on the price on 2 October 2017.*

NEUTRAL

CMP (VND)	39,300
Target Price (VND)	42,300

Stock Info

Sector	Automobile & Parts
Market Cap (VND billion)	40.30
Share O/S	23,342,433
Beta	1.03
Free Float (%)	74.87
52 weeks high	52,600
52 weeks low	21,250
Average trading volume (20 sessions)	128,870



Performance (%)

	3M	1Y	3Y
HAX	-19.80	74.18	852.73
VN30 Index	3.30	19.09	21.45
VN Index	3.32	16.77	30.61

Major sharholders (%)

Do Tien Dung	18.36
Vu Thi Hanh	12.72
Foreigner Investor Room (%)	16.87

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Current shareholder structure is a positive driving factor for the company's performance

Hang Xanh Automobile Service JSC used to be a showroom and automobile garage, which belonged to Sai Gon Mechanics And Automobile Corporate, namely SAMCO3. In 1999, SAMCO 3 was equitized to become Hang Xanh Automobile Service JSC (HAXACO).

With the advantage of its parent company as a partner founding Mercedes-Benz Vietnam (MBV), HAXACO became the first authorized distributor of MBV in 2004. The company is officially listed on HOSE with initial charter capital of only VND16 billion in 2006. Through the business growth improvement and continuous expansion, capital size of HAX as of Q3 2017 reached more than VND233 billion.

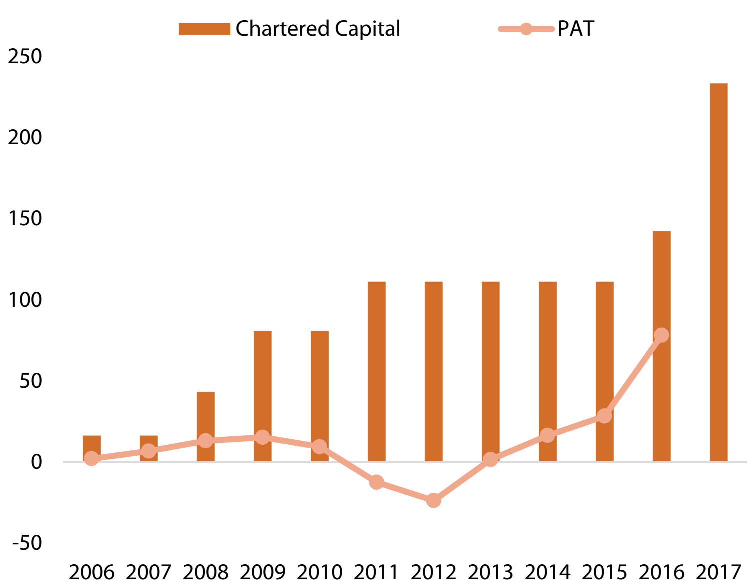
The main activity of HAX is distribution, warranty and repairs of Mercedes-Benz cars. Of the total revenue in 2016, 90.6% comes from selling activity, 6.5% from repairs and maintenance, and 2.8% from MBV bonus.

It is noteworthy that after SAMCO withdrew all of its 32.63% stake in HAX, HAX's shareholder structure became more concentrated, with the majority of shares in the hands of BOD members. In particuar, the number of shares held by Mr. Do Tien Dung (chairman) and his family members (Ms. Vu Thi Hanh - wife, Mrs. Do Ngoc Thuy Trang - son, Mrs. Do Ngoc Oanh - sister) were up to 37.2%.

Before coming to HAX, Do Tien Dung was the Vice Chairman of PTM - Automobile Production and Trading Service Joint Stock Company (a company acquired by HAX in 2016) and the Chairman of the Board of Directors of Vietnam Investment and Automobile Service Joint Stock Company (a company used to hold PTM shares). In 2013, Mr. Dung, as well as his wife and children, bought a large number of HAX shares and soon became large shareholders while SAMCO also held approximately 32%. Mr. Dung also directly participated in the management of HAXACO as CEO. Since then, HAX performance has been improving from loss-making to profitable business results. When SAMCO divested from HAX, Mr. Do Tien Dung and his relatives bought most of the shares and he became the chairperson.

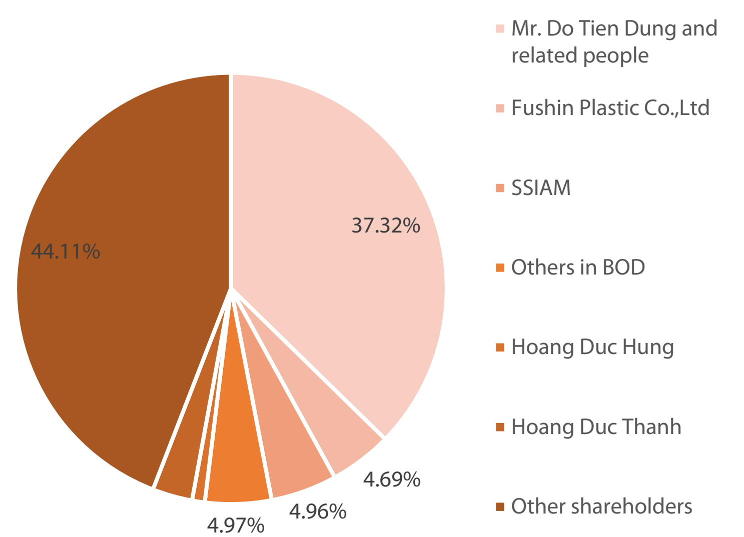
We hold the view that this shareholder structure is positive for HAX, as it shows a strong interest and motivation on the part of the BOD in general, and for Mr. Do Tien Dung to particularly look after the long-term development of the company.

Figure 1: Changes in PAT and Chartered Capital of HAX since 2006 (unit: VND B)



Source: HAX, RongViet Research

Figure 2: Curent shareholder structure of HAX



Source: HAX, RongViet Research

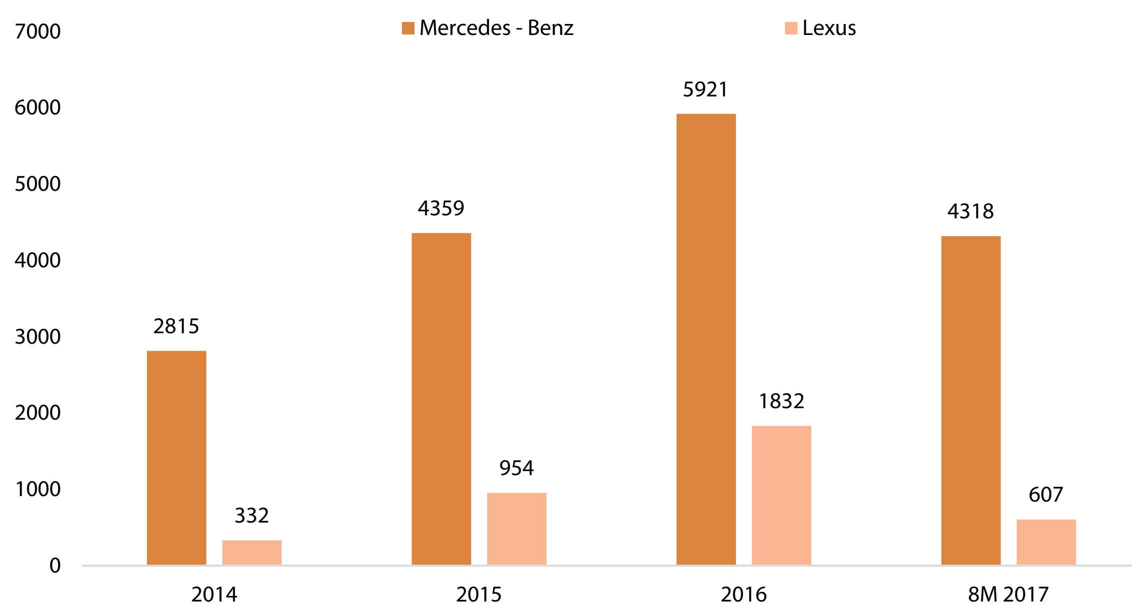
Mercedes – Benz: Impressive Growth despite Difficult Market Environment

Established in 1995, MBV is a joint venture between the Saigon Transportation Mechanical Corpooration (SAMCO) and Germany's Daimler Group. After more than 20 years of operation in Vietnam, Mercedes – Benz is the only brand that is continuously leading the country's luxury car market, with a CAGR of sales valued at 45% throughout the period of 2014–2016.

The year 2017 is a difficult year for most of automobile dealers in Vietnam as there will be many big changes leading to opposite effects next year; in particular, the current demand has been slowing down owing to most potential buyers intending to wait for the ASEAN's car import tax rates to fall to 0% in January 2018. Even though many car dealers have offered some discount programs, promotions and incentive packages to stimulate demand, sales volume in the first 8 months still experienced a downward trend (-6% YoY).

Contrary to the overall picture of the Vietnamese automobile market in 2017, we realize that the sales of MBV are growing strongly. Since the beginning of the year, MBV has handed over to customers 3,781 passenger cars, which have been up 42% compared to the results in the same period last year.

Figure 3: The number of vehicle sold of MBV and Lexus over the period of 2014 – 2017



Source: VAMA, RongViet Research

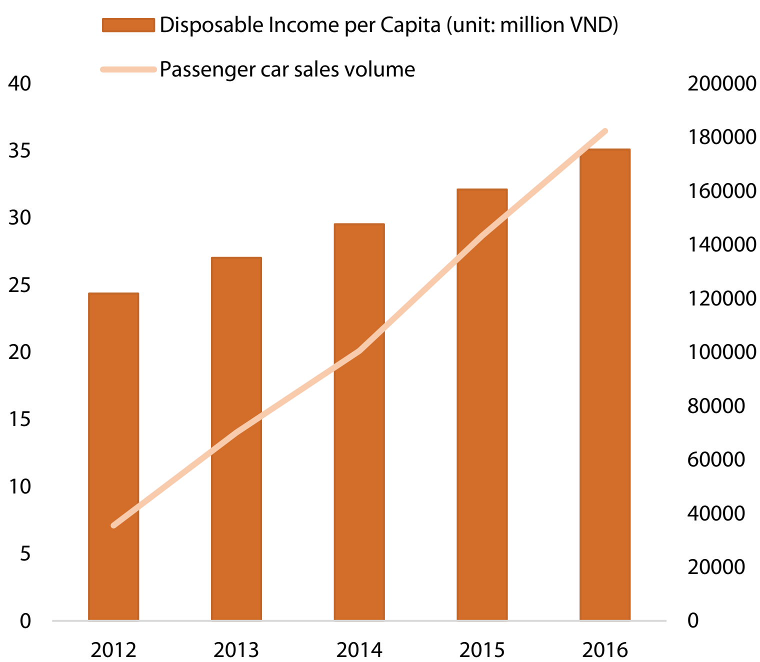
Thus, MBV continues to lead the market segment, outstripping all its rivals. Specifically, Lexus – one of MBV's peer – sold only 607 units in the first eight months; its sales plummeted 57% over the same period and could continue to decline futher.

Another competitor BMW is now facing an issue with its former dealer, Euro Auto, which was accused of violating multiple import regulations. To date, BMW cars have not been distributed through its new representative, but temporarily distributed via Performance Motors with only two showrooms in Hanoi and Ho Chi Minh City. In addition, Audi, another competitor of MBV, has just entered Vietnam in 2008 (13 years later than MBV), owns only three showrooms across the country.

Mercedes Benz currently has the highest number of sales agents in Vietnam with 13 centers throughout the country. We suppose that the role of MBV as a market would become ever more firm as it has been planning to double its sales agent network from 2016 to 2020.

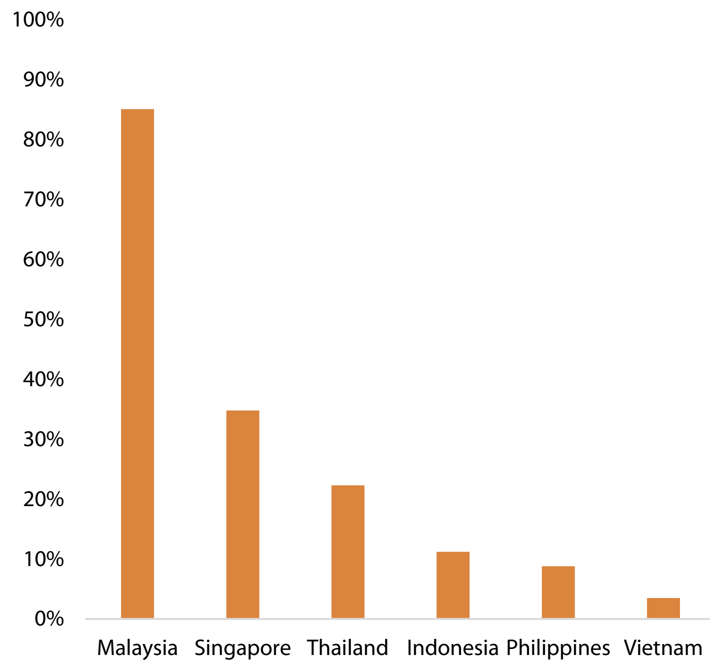
It is worth noting that one of the challenges all luxury car dealers would face next year is the change in special sales tax rate. A vehicle with the cylinder capacity of 2,500–3,000 ccs will be applied a 5% higher or 60% special sales tax rate. This change could negatively affect MBV. However, after doing research, we found out that only 10 out of 46 models could be covered by the tax rate increase. Furthermore, we hold the view that tax would not strongly affect the upper-class customers' demand on luxury cars.
On the other hand, we believe that income is one of the main factors that affect the market demand for new cars. According to the Euromonitorss report, Vietnam's disposable income per capita has improved significantly over the past years, increased by 61.63% since 2012. Solidity's research indicates that the market for premium car brands such as Mercedes in Vietnam is one of the fastest growing markets in the world due to the rapid increase in people's incomes.

Fugure 4: The correlation between the average annual disposable income and total vehicle sales volume in Vietnam



Source: Euromonitors, RongViet Research

Figure 5: The car ownership rate for households in Vietnam and some other ASEAN countries



Source: Euromonitors, RongViet Research

Moreover, Vietnam is one of the country with the lowest car ownership rate according to BMI statistics. Car owners account for only 4% of Vietnam's households while the figures in other countries in the ASEAN region such as Thailand and Indonesia are 22% and 11%, respectively. We consider that Vietnam's automobile industry has not only began its early stages of growth but also has a lot of potential for speedy growth in the long term.

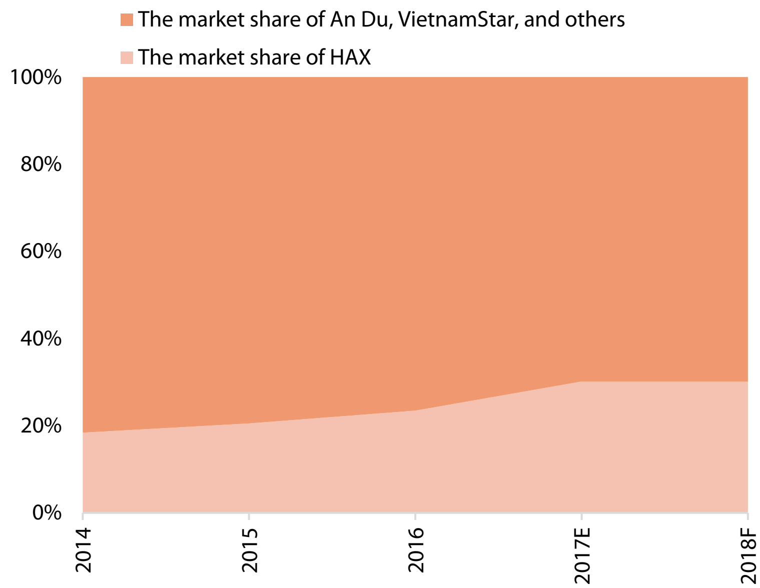
For the reasons mentioned above, we believe Mercedes-Benz's sales will continue growing as a leading brand in the Vietnamese high-end car market, but there could be some hurdles. In particular, we consider that the competition between luxury car brands would become more intense, because MBV's credible rival, BMW, expressed its intention to choose THACO as a new dealer from 1 January 2018 while other luxury car brands are also establishing their own position in the market. Consequently, we came up with our conservative forecast for MBV's sales growth at 20% per year in the period of 2018–2020, below the growth level of 45% seen in the 2014–2016 period.

HAXACO is constantly expanding its market share of Mercedes-Benz distribution

Despite being the first official distributor of MBV, Haxaco currently hold the smallest market share while VietnamStar and An Du claimed 50% and 30% in 2016, respectively.

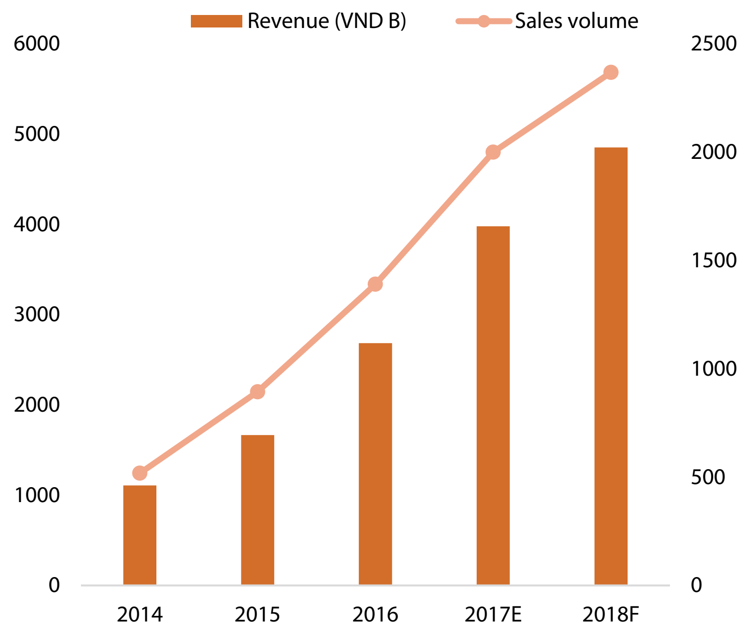
However, thanks to the continuous sales growth, specifically 58.1% YoY in 2016 and 39.7% YoY in H1 2017, HAX has been significantly expanding its market share over the years, from 18.4% in 2014 to 23.5% in 2016.

Figure 6: HAX market share expansion in 2014 - 2018F



Source: HAX, RongViet Research estimated

Figure 7: Revenue and Sales volume of HAX in 2014 – 2018F



Source: HAX, RongViet Research estimated

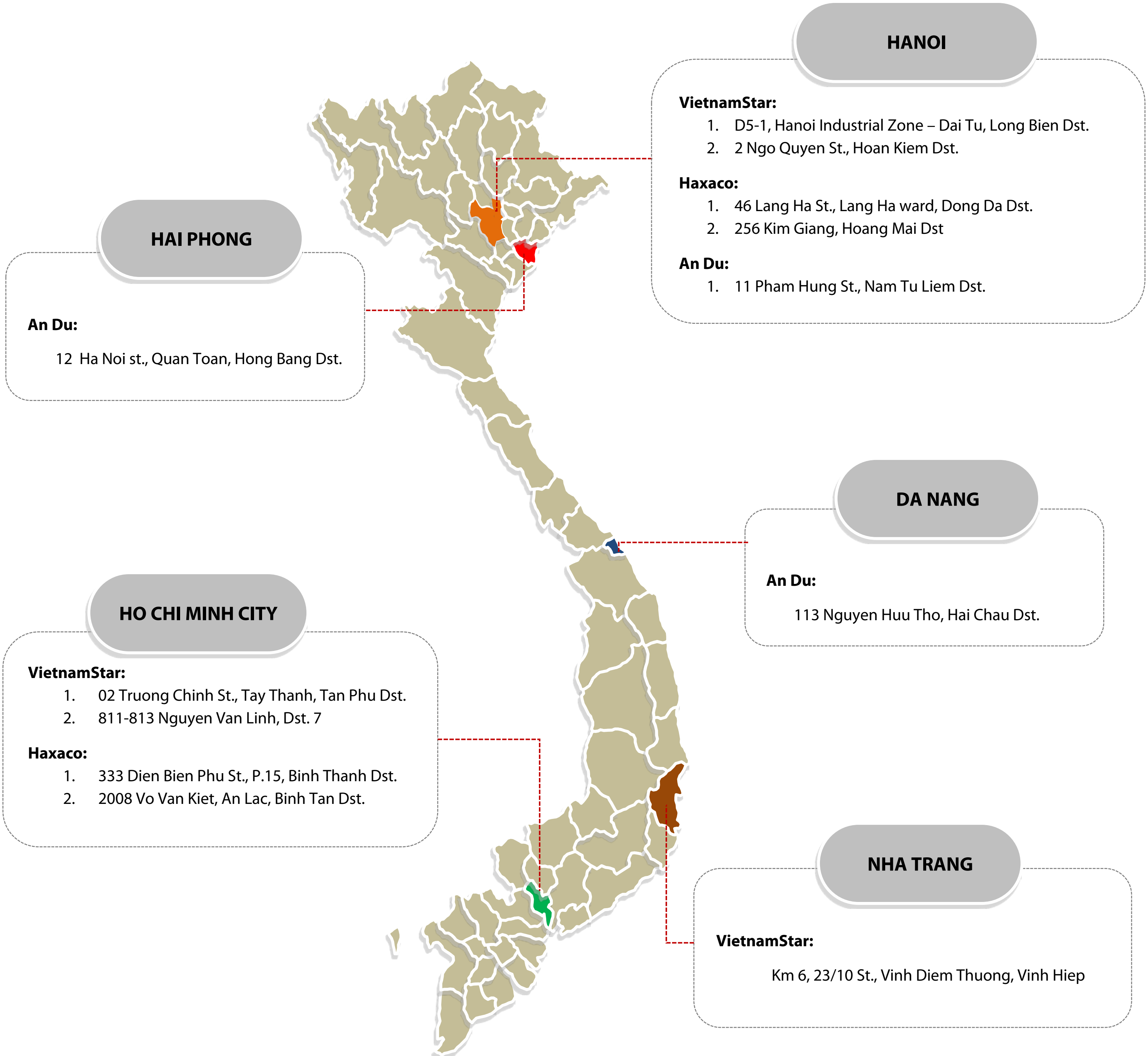
In 2016, HAX acquired 92.7% of PTM's equity. After this acquisition, HAX has opened its fourth *autohaus* named Haxaco Kim Giang at the old headquarter of PTM (256 Kim Giang street, Hanoi). This location is highly appreciated by MBV, as it is located in the planning area of the new urban area of southwest Kim Giang as well as adjacent to Linh Dam urban area with crowded population. Besides, the land leasing rate is quite low here, only about VND100 million per year. This position makes Haxaco Lang Ha easily approachable to customers in the south of Hanoi. In addition, PTM already had qualified staff and equipment, which helped HAX save more time and money than building a completely new showroom.

Besides, HAX officially upgraded Haxaco Lang Ha from Autohaus 300 to Autohaus 600 (Sales Module 600 / After-Sales Module 14) because of its rapid growth in sales and service. This means Haxaco Lang Ha has become the largest and most modern outlet of MBV across the country even though it is the first showroom of HAX in the northern market and has just been operating since 2015.

According to Mercedes-Benz terms, the distributor will allocate a certain amount of sales for each model in a year, based on the number and qualification of an *autohaus*, as well as the market share, of each dealers. Consequently, opening or upgrading an *autohaus* is very important to MBV's dealers, especially HAX, to increase the number of vehicles allowed to distribute, thereby boosting its sales and creating competitive advantage with two other distributors. Moreover, expansion also offers a higher bonus received from MBV based on the criteria set by MBV on each *autohaus*.

As a result, we highly expect that HAX's market share would jump up to 30% in 2017.

Figure 8: Location *Autohaus* of Haxaco, VietnamStar and An Du



Source: HAX, RongViet Research

As we have known, HAX has always had an ambition to open more showrooms coupled with MBV's plan that will double the number of outlets. HAXACO Kim Giang is the first step. However, it would take long and strenuous negotiations in about 1–2 years to be approved and to launch a new *autohaus* because there are many strict standards required by Daimler Group. HAX also has to compete with An Du and VietnamStar to convince MBV to open new showrooms. Therefore, we predict that HAX's expansion plan will have to wait until the end of 2018 or 2019. The next location is likely to be in central Vietnam, which HAX does not have any showrooms in as well as a potential market with low competition.

Table 1: HAX's *Autohaus* list

	Autohaus Name	Location	Utilities
1	HAXACO Lang Ha	Hanoi	Autohaus 600 Total area: 5000 m2 (with 2 main areas including a 2,500 m2 showroom and a 1,000 m2 workshop). 16 work-bays Supplying maintenance and technical service for up to 50 cars per day
2	HAXACO Kim Giang	Hanoi	Autohaus 150 Total area: 3,500 m2 17 work-bays Supplying maintenance and technical service for up to 60 cars per day
3	HAXACO Dien Bien Phu	Ho Chi Minh City	Autohaus 600 18 work-bays Supplying maintenance and technical service for up to 50 cars per day
4	HAXACO Vo Van Kiet	Ho Chi Minh City	Autohaus 300 33 work-bays Supplying maintenance and technical service for up to 100 cars per day

Source: HAX, RongViet Research

MBV's sales policy and bonus schemes are decisive factors in HAX's profit

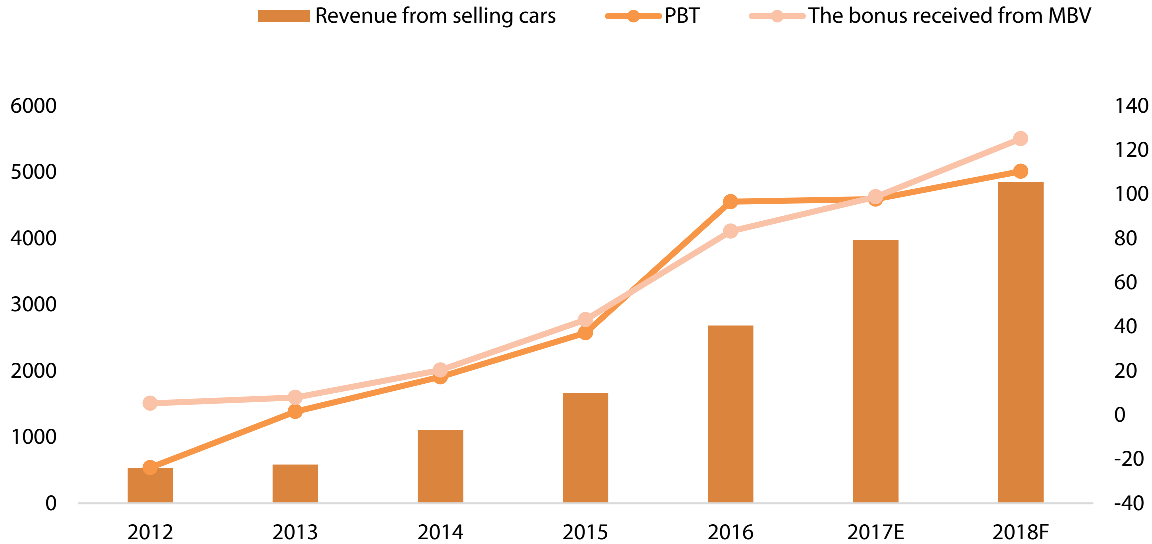
With the nature of car dealers, HAX's business depends closely on Mercedes-Benz's policies.

In terms of bonus schemes, HAX will receive support from the branch in two ways: a fixed margin on input prices and an incentive at the end of each period. Mercedes has a list price for its vehicles, which is used as a starting point to calculate prices to dealers. This then will provide 'declared support' (a discount) which varies by models but is standardized for all dealers (about 5–6%). Besides, MBV does not set the retail prices but each agent will decide for itself depending on its own sales policy. Under intense competitive pressure within Mercedes-Benz distribution system, HAX normally uses a direct discount to reduce the selling price to attract customers. Therefore, the gross profit margin from the car segment is quite low at around 3%, which will be used to cover the operation costs such as selling and administrative expenses.

For the reasons mentioned above, we suppose that HAX's profitability will be determined by the bonus rewards based on volume of sales and the achievement of certain qualitative targets. This bonus will be paid at the end of the quarter, half-year and year-end if the distributor achieves sales of more than 80% of committed output as well as some criteria (such as customer satisfaction, facilities, training, and customer information and data management).

In line with our revenue projection and based on our bonus analysis, we estimate that HAX could receive a bonus of VND99 billion in 2017 and VND125 billion in 2018.

Figure 10: HAX's revenue from selling cars, PBT and the bonus received from MBV in 2013 – 2018F (unit: VND B)

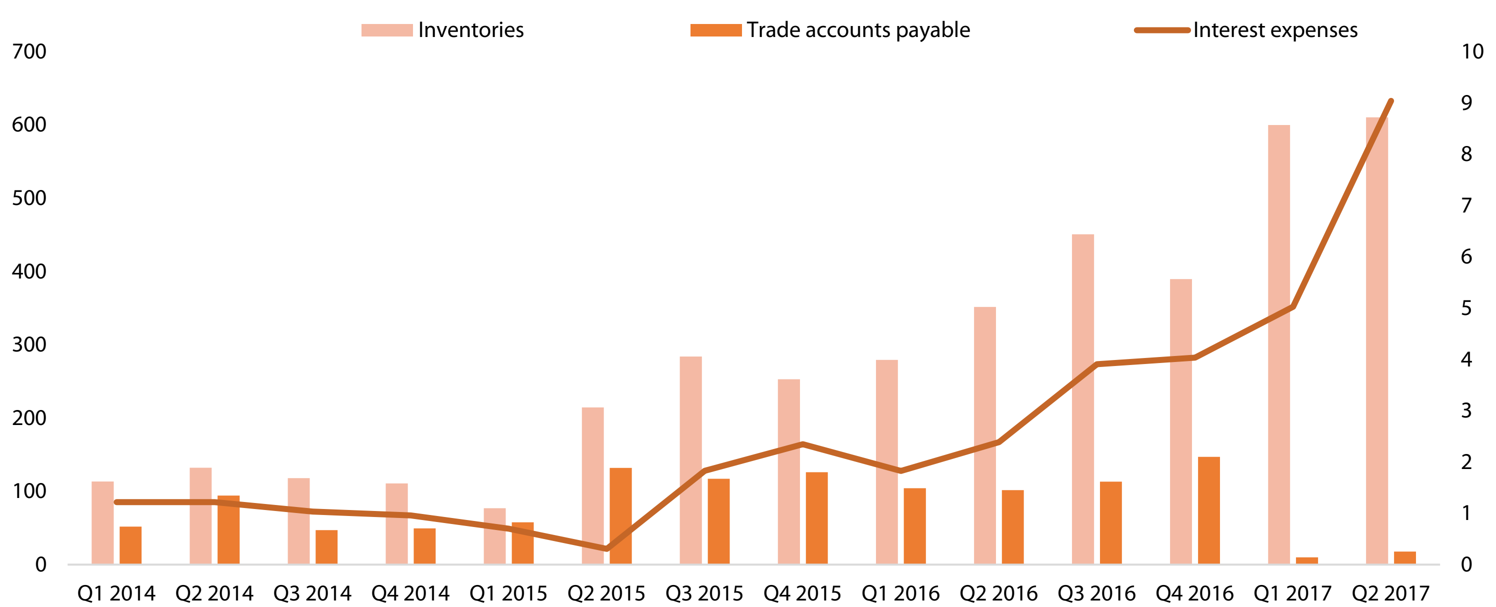


Source: HAX, RongViet Research estimated

Another notable point about HAX is that Mercedes-Benz has recently reviewed and upgraded Vietnam's market based on outstanding growth over the past years. This means that its distributors would no longer be supported by many preferential policies as before. In detail, MBV has required a "due upon receipt" payment terms instead of 90-day late payment terms since 2017. Along with an inventory requirement of at least 1.5 months of sales, it is worth noting that this change in policy may cause HAX a great debt pressure due to the sales growth. In first six months, the amount of HAX's new borrowings was 2.5 times higher than last year, and interest expense increased 3.3 times from VND4.2 billion to VND14.1 billion. Consequently, we estimate that interest expenses in 2017 and 2018 will be around VND27.5 billion and VND34.3 billion, respectively.

However, all of HAX's liabilities now is short-term, used to finance short-term assets (inventory), and the financial leverage is remains stable. We suppose that HAX have not yet faced major financial health risks even though this risk will increase if market conditions change causing sales of HAX to decline.

Figure 11: Interest expense surged after MBV changed its sales (Unit: VND B)

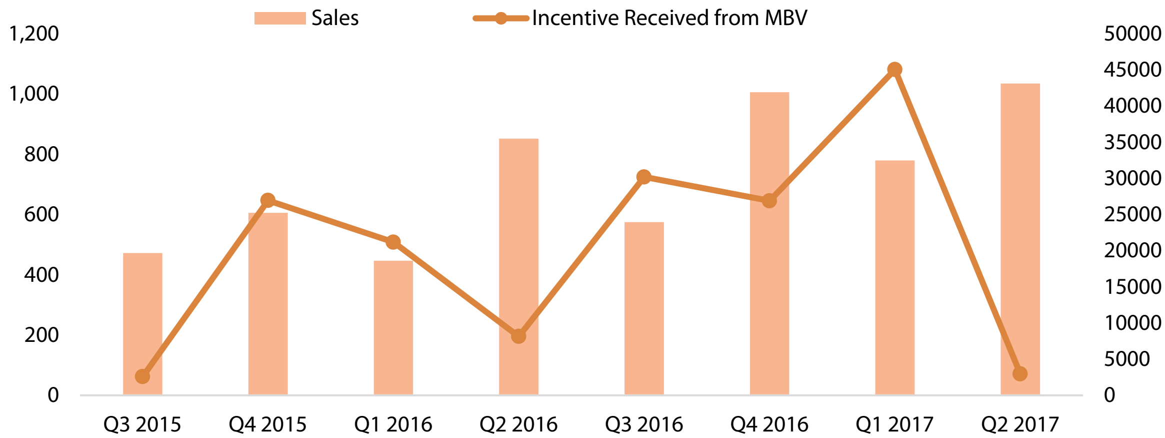


Source: HAX, RongViet Research

Expecting huge profit in short-term

In H1 2017, there was a noticeable growth in total sales MBV, which increased 59% YoY to 2,898 units. As one of the three authorized dealers of MBV, HAX posted an impressive 40% YoY growth in sales for the first half of 2017. Notwithstanding a bright picture of the total MBV consumption, HAX reported a loss after tax of nearly VND9 billion in the second quarter. In the first half of 2017, PAT also dropped 43% compared to the first half of 2016. According to the company's explanation of the loss, in the second quarter, HAX had to discount sales to its customers and even accepted losses to clear out all old C-class cars due to the upgrading period of Mercedes-Benz models. Besides, the intense competition from the two other large dealers (Vietnamstar and An Du) is forcing HAX to increase expenditure. In particular, selling and administrative expenses surged 66% YoY and 130% YoY, respectively.

Figure 12: Quarterly Sales and Incentive Received from MBV of HAX (unit: VND B)



Source: HAX, RongViet Research

As we have known, the incentive from MBV, which plays a key role in the company's profit is only recognized once MBV confirms the sales results and confirm payments. This process leads to a quarter lag between the time HAX reflects sales and records bonuses. Consequently, the amount received from MBV in Q2 which was suddenly very low (less than VND3 billion) could be explained by Q1 sales which did not meet its target in spite of the impressive 74% growth compared to Q1 2016. This contradiction is also explainable when HAX set a revenue target growth of 80.3% this year. At the end of the second quarter, MBV would determine the commission rate for HAX based on the sales results in the second quarter as well as the first half of the year.

According to the prospective business outlook of MBV in general as well as HAX in particular, we estimate the second half's revenue of HAX would reach VND4,228 billion (+46.9%). Thus, we estimate that HAX will receive a large estimated bonus of VND50.8 billion based on the sales results in the Q2, Q3, and the second half of the year.

Table 2: H2 2017 and 2017's Performance Forecast

	H2 2017	+/-YoY	2017E	+/-YoY
Sales	2,415.6	+ 52.7%	4,228.7	+ 46.9%
GPM	94.3	+ 69.1%	143.9	+ 44.4%
EBIT	85.3	+ 33.6%	127.6	+ 17.1%
PAT	60.8	+ 34.6%	79.9	+ 2.5%

Source: RongViet Research

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Table 3: Valuation model

Valuation method		Price	Weight (%)	Average
P/E	P/E = 11.5 Average P/E = VND3,671 per share	41.722	50	20.861
P/S	P/S = 0.2 Average P/S = VND9,394 per share	42.930	50	21.465
Target Price			**100**	**42,300**

Source: RongViet Research

Unit: VND billion

INCOME STATEMENT	2015A	2016A	2017F	2018F
Revenue	1,821	2,880	4,229	5,166
COGS	1,768	2,780	4,085	4,991
Gross profit	52	100	144	175
Selling expense	36	59	85	121
G&A expense	19	23	41	49
Financial income	0	1	2	3
Financial expense	5	12	28	34
Other income/loss	44	91	108	137
Gain/(loss) from JV	0	0	0	0
PBT	37	97	100	112
Tax expense	9	18	20	22
Minority interests	1	0	0	0
PAT	29	78	80	89
EBIT	42	109	128	146
EBITDA	6	33	153	175

FINANCIAL RATIO	2015A	2016A	2017F	2018F
Growth (%)				
Revenue	49.3	58.1	46.9	22.2
EBITDA	-19.5	416.8	367.6	14.4
EBIT	438.0	156.9	17.1	14.7
PAT	72.9	170.7	2.5	11.9
Total Asset	93.7	94.9	41.1	22.4
Total Equity	28.1	133.2	27.7	23.2
Profitability (%)				
Gross profit margin	2.9	3.5	3.4	3.4
EBITDA margin	0.3	1.1	3.6	3.4
EBIT margin	2.3	3.8	3.0	2.8
Net profit margin	1.6	2.7	1.9	1.7
ROA	6.5	9.1	6.6	6.0
ROIC or RONA	32.3	35.5	32.7	30.5
ROE	22.3	25.9	20.8	18.9
Efficiency (x)				
Receivables turnover	24.6	13.4	22.2	22.2
Inventories turnover	7.0	7.1	6.4	6.4
Payables turnover	10.8	12.8	64.5	64.5
Liquidity (x)				
Current	1.2	1.2	1.1	1.2
Quick	0.4	0.5	0.4	0.4
Financial Structure (x)				
Total debt/ Equity	113.9	112.1	197.8	196.0
ST debt / Equity	113.9	112.1	197.8	196.0
LT debt/ Equity	0.0	0.0	0.0	0.0

Unit: VND billion

BALANCE SHEET	2015A	2016A	2017F	2018F
Cash and cash equivalents	23	41	76	151
Short term investment	0	0	0	0
Accounts receivable	74	215	191	233
Inventories	253	390	639	781
Other current assets	13	18	27	35
Tangible Fixed Assets	61	116	200	204
Intangible Fixed Assets	13	78	78	78
Long term investment	0	0	0	0
Other non current assets	5	5	5	5
Total Asset	**442**	**861**	**1,215**	**1,487**
Account Paybale	163	217	63	77
Short term borrowings	147	338	761	930
Long term borrowings	0	0	0	0
Other non-current liabilities	1	1	2	2
Bounus and Welfare fund	0	0	0	0
Technology – Science dev fund	0	0	0	0
Total Liabilities	**311**	**556**	**826**	**1,009**
Common stock and APIC	112	206	297	297
Treasury stock	0	0	0	0
Retained Earnings	13	88	77	162
Other comprehensive income / (loss)	0	0	0	0
Investment and Development Fund	4	8	11	15
Total Equity	**129**	**301**	**385**	**474**
Minority Interest	**1**	**4**	**4**	**4**

CASH FLOW STATEMENT	2015A	2016A	2017F	2018F
Profit before tax	**37**	**97**	**100**	**112**
Depreciation	4	10	26	29
Adjustment	11	13	-	-
Working capital	(96)	(236)	(408)	(201)
Net Operating CFs	**(44)**	**(117)**	**(282)**	**(60)**
Fixed Asset	(29)	(65)	(101)	(33)
Deposit, equity investment	(3)	9	-	-
Interest, dividend, cash profit received	0	-	-	-
Net Investing CFs	**(32)**	**(56)**	**(101)**	**(33)**
Capital	-	31	-	-
Debt	87,981	191	423	169
Dividend paid & other	(87,893)	(31)	(5)	(0)
Net Financing CFs	**88**	**190**	**419**	**168**
Net Cash flow				
Beginning cash & equivalents	**13**	**23**	**41**	**76**
Effect of exchange rate	12	18	35	75
Ending cash & equivalents	**23**	**41**	**76**	**151**

COMPANY REPORT

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	NEUTRAL	SELL
Total Return including Dividends in 12-month horizon	>20%	-20% to 20%	<-20%

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