NAM KIM STEEL JSC (HSX: NKG)

Recovering domestic consumption, but weakening steel prices

(VND bn)	3Q-FY21	2Q-FY21	+/- qoq	3Q-FY20	+/- yoy
Net revenue	7,531	7,010	7%	3,376	123%
PAT	607	848	-28%	83	634%
EBIT	792	1,026	-23%	143	454%
EBIT margin	10.5%	14.6%	-411bps	4.2%	628bps

Source: NKG, Rong Viet Securities

3Q2021: Revenue reached a record level owing to strong overseas demand

- Revenue increased by 123% YoY to reach VND 7,531 bn (or USD 330.3 mn) as both selling prices and volume grew strongly YoY. Despite the stricter social distancing measures, the company increased exports volume by 128% QoQ, and boosted total volume to grow by 32% YoY.
- Average selling price rose by roughly 70% YoY as steel prices in North America and Europe kept increasing while price was stable in Vietnam, thus, supporting GPM to be at a high level of 17.2%, versus 7.2% in the same period last year. Hence, NPAT grew by 670% YoY to reach VND 607 bn (USD 26.6 mn). However, GPM decreased slightly to 17.2% from 18.6% in 2Q.

4Q2021 and 2022 outlook: Domestic consumption could recover, but the selling prices can decrease.

- North American markets are attractive as hot-dipped galvanized steel FOB prices in this area are significantly higher than the NKG prices in Vietnam.
- Domestic consumption can grow strongly in 4Q2021 and 2022 owing to re-opening of the economy and public investments. However, as HRC prices have been decreasing, profitability in this market can be under pressure due to inventory accumulated at a relatively high price.
- The company plans to expand the steel pipe production capacity by 67% to 300,000 tons per year and coated steel production capacity by 30% to 1.3 million tons in 2Q/2022.
- For 2022, we expect selling volumes in the coated steel and steel pipe segments to grow by 4.0% and 8.8% YoY to reach 1.0 million tons and 0.16 million tons respectively.
- 2021 revenue and NPAT can reach VND 27,990 bn (USD 1,227 mn, +142% YoY) and VND 2,420 bn (USD 108 mn, +720% YoY), respectively. For 2022, we expect that NPAT can decline by 21% YoY to VND 1,900 bn (USD 83 mn), but still significantly higher than historical levels.

Valuation and recommendation

NKG can seize opportunities in foreign markets to maximize profit. The company showed its flexible sales strategy in 9M2021 by reallocating production volume to the most profitable markets, such as Europe and North America. In 4Q, the gross margin is going to decrease in Europe, but will still be attractive in North America. With its flexible strategy, we expect NKG to increase its selling volume in North America and offset partially decreasing profitability in Europe. In the long-term, decarbonization in the EU and China is changing the steel industry significantly and boosting steel production costs. We expect exports will continue to support NKG's NPAT in 4Q2021 and 2022 owing to its competitive production costs and favorable trade policies in Europe and North America. Besides, additional production capacity will allow the company to seize opportunities as sales in the domestic market can grow strongly in 2022.

*Using FCFF, and PER methods, we come up with a fair value of VND **48,000** per share. Together with a cash dividend in the next 12 months of VND 1,000/share, **the total return is 29%**, based on the closing price as of December 13th, 2021. Hence, we recommend investors **BUY** this stock.*

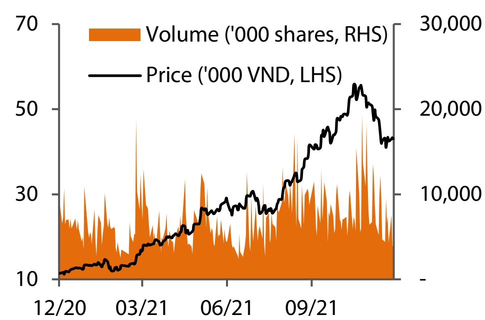
BUY	+29%
Target price (VND)	48,000
Current market price (VND)	37,900
Cash Dividend (VND)*	1,000

** Expected in the next 12 months*

Stock Info	
Sector	Basic Materials
Market Cap (VND billion)	9,238.3
Current Shares O/S (million)	218.4
Avg. Daily Volume (in 20 sessions)	7,280.6
Free float (%)	50
52-week High	55,900
52-week Low	11,191
Beta	1.3

	FY2020	TTM
EPS	1,672	9,530
EPS Growth (%)	543.1	1128.9
Diluted EPS	1,101	9,530
P/E	9.2	4.6
P/B	0.9	1.6
EV/EBITDA	7.1	4.8
Cash dividend yield (%)	0.0	2.3
ROE (%)	9.3	46.6

Price performance



Major Shareholders (%)	
Ho Minh Quang	12.9
Unicoh Specialty Chem	6.9
SMC	5.0
Remaining ownership room (%)	*42.0*

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Exhibit 1: 3Q/2021 Results

(VND Bn)	3Q-FY21	2Q-FY21	+/- (qoq)	3Q-FY20	+/- (yoy)
Net revenue	7,531	7,010	7.4%	3,376	123.1%
Gross profit	1,296	1,306	-0.8%	242	434.6%
SG&A	504	280	79.6%	99	407.0%
Operating income	792	1,026	-22.7%	143	453.8%
EBITDA	888	1,121	-20.8%	238	273.5%
EBIT	792	1,026	-22.7%	143	453.8%
Financial expenses	108	86	25.2%	73	48.8%
- Interest expenses	71	45	59.8%	56	27.2%
Dep. and amortization	95	95	0.2%	95	0.6%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	706	977	-27.7%	92	670.2%
PAT	607	848	-28.4%	83	634.3%
(*) Adjusted PAT	607	848	-28.4%	83	634.3%

Source: NKG, Rong Viet Securities

Exhibit 2: 3Q/2021 Performance Analysis

	3Q-FY21	2Q-FY21	+/- (qoq)	3Q-FY20	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	17.2%	18.6%	-142bps	7.2%	1,003bps
EBITDA Margin	11.8%	16.0%	-420bps	7.0%	475bps
EBIT Margin	10.5%	14.6%	-411bps	4.2%	628bps
Net Margin	8.1%	12.1%	-403bps	2.4%	561bps
Adjusted Net Margin	8.1%	12.1%	-403bps	2.4%	561bps
Turnover *(x)					
-Inventories	3.8	4.8	-1.0	4.9	-1.1
-Receivables	9.1	10.8	-1.7	10.6	-1.6
-Payables	4.4	5.4	-1.0	10.8	-6.4
Leverage (%)					
Total Debt/ Equity	195.8%	201.8%	-600bps	148.1%	4,775bps

Source: NKG, Rong Viet Securities. (*) annualized

Exhibit 3: 4Q/2021 Forecast

(VND Bn)	4Q-FY21	+/-qoq	+/-yoy
Revenue	8,598	14.2%	151.5%
Gross profit	1,282	-1.1%	316.9%
EBIT	797	0.6%	303.3%
NPAT	649	6.9%	321.2%

Source: Rong Viet Securities

- We expect revenue to increase by 151% YoY due to both higher selling volume and steel prices.

- We forecast that total selling volume can grow by 55% YoY to 306,000 tons of products owing to strong overseas demand. Meanwhile, the average selling price can also rise by 60% to roughly VND 27.5 mn/ton.

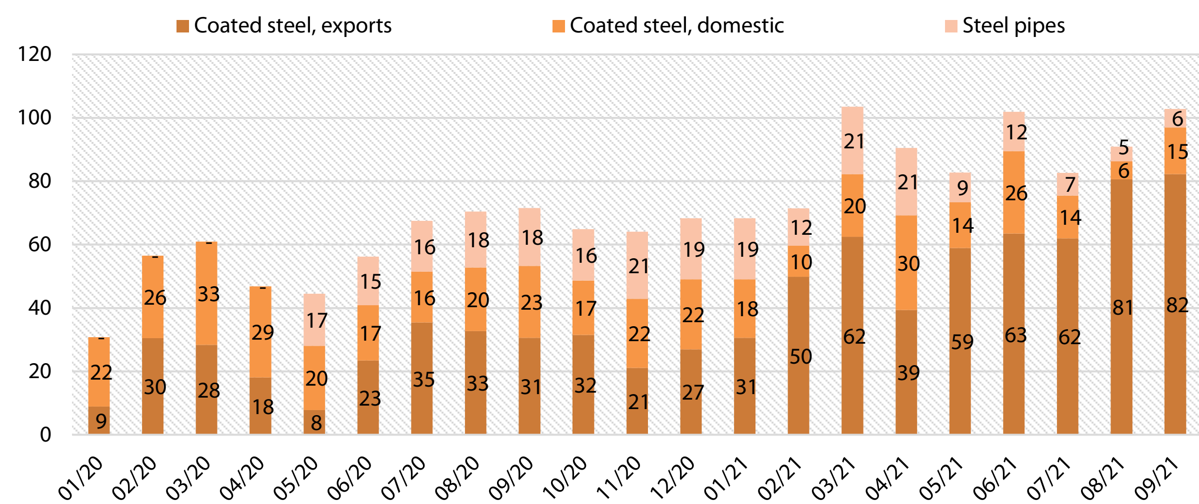
Update

3Q update – Exporting to North America and Europe boosted revenue and profitability.

NKG seized export opportunities to maintain selling volume at a record level. The company sold roughly 276,000 tons of products in 3Q, rising by 32% YoY. Export volume increased strongly by 39% QoQ and 128% YoY to reach 224,000 tons in 3Q, contributing 81.5% to total selling volume as the demand overseas was strong and NKG proactively boosted exports to offset weak demand in the domestic market. In which, Europe and North America were NKG's key markets, accounting for roughly 70% of total selling volume. On the contrary, the demand in the domestic market was weak due to the negative impact of stricter social distancing in July and August.

There were some positive signs from the domestic market in September as social distancing has been easing in many Southern provinces. Selling volume in the domestic market recovered from roughly 10,000 tons in August to roughly 20,000 tons in September. Meanwhile, export volume was stable at roughly 82,000 tons in September, similar to that of 80,600 tons in August.

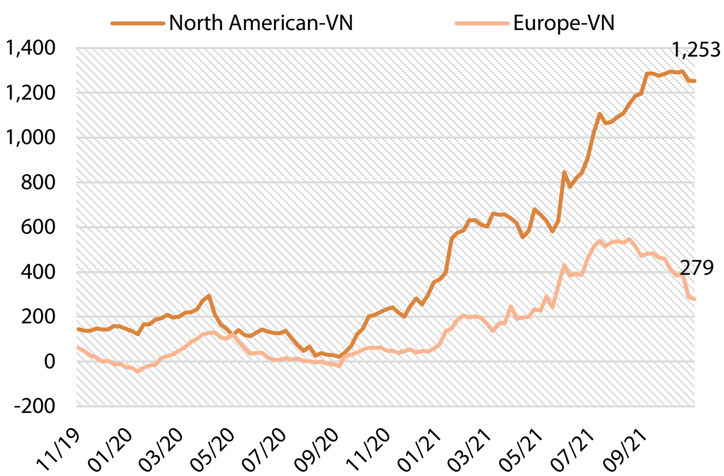
Figure 1: Selling volume (thousand tons)



Source: NKG, VSA, Rong Viet Securities

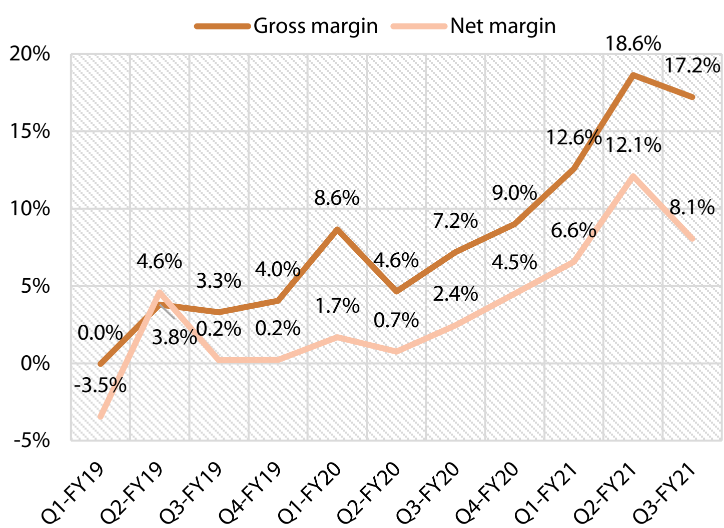
Increasing selling prices in foreign markets supported profitability. Steel prices in North America and Europe increased strongly in 3Q owing to recovering demand and tight supply caused by limited import volume. As a proxy for flat steel prices, quarterly average hot-rolled coil (HRC) price rose by 24.0% QoQ in the US, and 10.9% QoQ in Europe. Therefore, although the company bought HRC at a higher price, it maintained a high gross margin, which was 17.2%. Because of higher export volume to North America and Europe as well as increasing ocean freight costs, selling expenses rose by 90% QoQ to VND 465 bn (USD 20.4 mn), leading the net margin to decrease at a higher pace compared to gross margin (Figure 3).

Figure 2: HRC price difference (USD/ton)



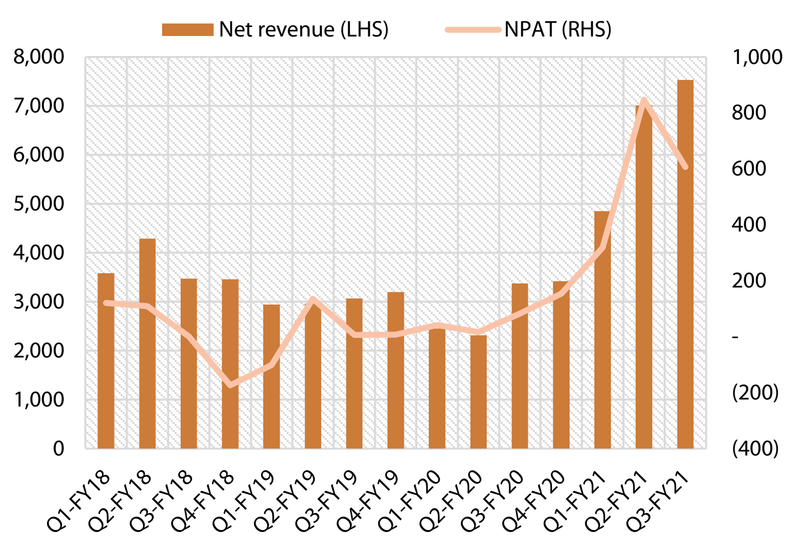
Source: Bloomberg, Rong Viet Securities

Figure 3: Gross margin and net margin



Source: NKG, Rong Viet Securities

Figure 4: Net revenue and NPAT (VND bn)



Source: NKG, Rong Viet Securities

Owing to high selling volume and increasing selling prices, the company posted revenue of VND 7,531 bn (USD 330 mn), the highest level in history. Meanwhile, NPAT decreased from VND 848 bn (USD 37 mn) in 2Q to VND 607 bn (USD 27 mn) in 3Q but still increased by 634% YoY.

Outlook

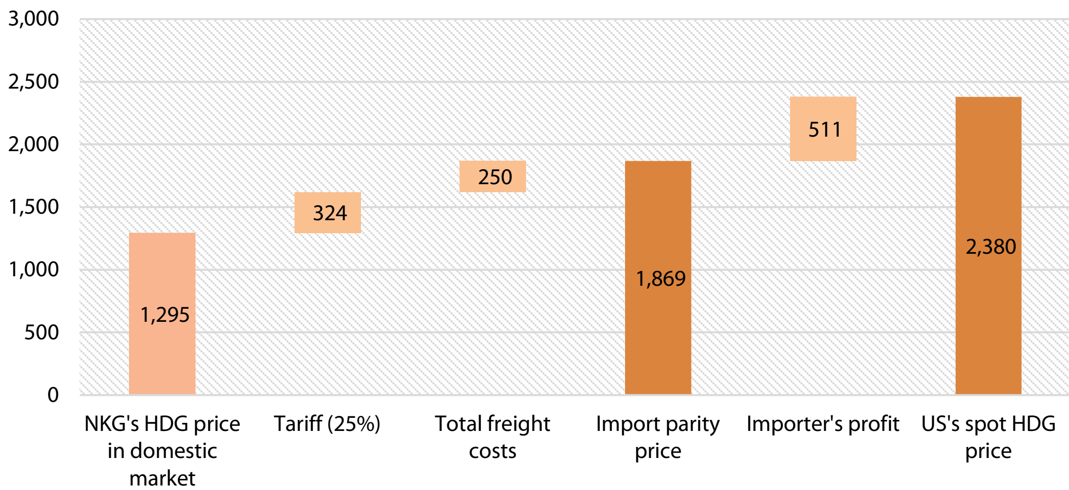
We expect exports to continue supporting NKG's selling volume in 4Q2021 and 2022 owing to its competitive production costs and favorable trade policies in Europe and North America. In the short term, NKG's profitability in North American could increase in 4Q due to favorable steel price movements.

North America is offering attractive opportunities in the short-term.

The price gap has been boosting Vietnamese producers' sales to the US market in 2021, and this trend is likely to continue in 1H2022. Vietnam's coated steel export volume has increased from only 114,000 tons in 2020 to 305,000 tons in 10M2021. However, there is still room for growth as Vietnam accounted for only 10.9%.

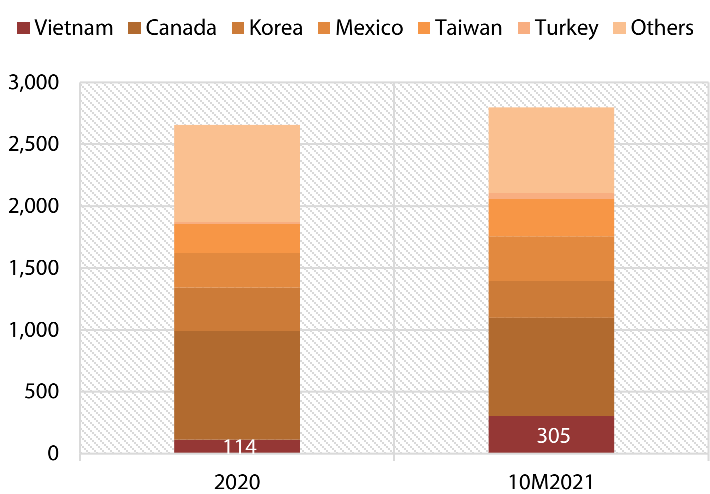
HRC prices in North America have been decreasing at a slower pace compared to Vietnam. This led the HRC price difference to rise from USD 1,020 in early July to USD 1,253/ton in early October. As of November 11, the hot-dipped galvanized price in the US was roughly USD 2,380/ton, significantly higher than NKG's price of 1,295/ton in Vietnam. After taking into account the tariff of USD 320/ton and transportation cost of roughly USD 250/ton, there are still arbitrage opportunities with a profit of USD 511/ton (Figure 5), which can be shared by NKG and the importers. With competitive production costs owing to low HRC prices, NKG's gross margin can be high in the next two to three quarters. For the long-term, we think the difference in HRC prices can fade away as the supply in the US is likely to increase driven by high profitability and we estimate that steel production costs in Vietnam are not significantly lower than in the US, averaging roughly USD 50/ton in 10M2021. Therefore, NKG's gross margin in this market can revert to a normal level of 10%-12%, lower than the current 18%-20%.

Figure 5: NKG's import parity price vs. US's spot HDG price (USD/ton) as of November 11



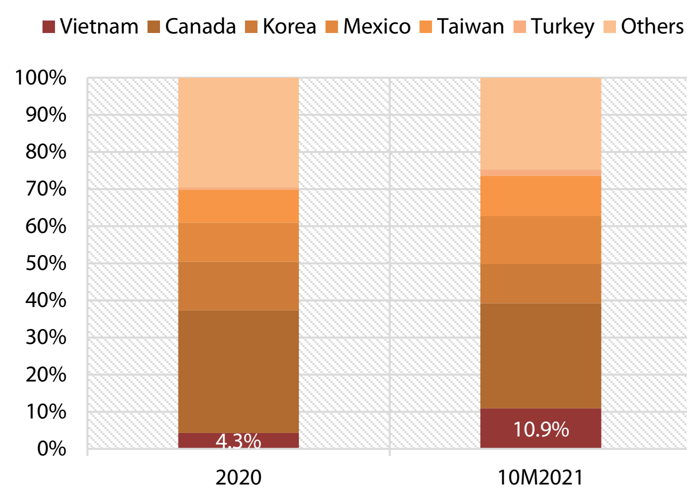
Source: Rong Viet Securities

Figure 6: US's coated steel import volume, by country (thousand tons)



Source: US's International Trade Administration, Rong Viet Securities

Figure 7: US's coated steel import structure



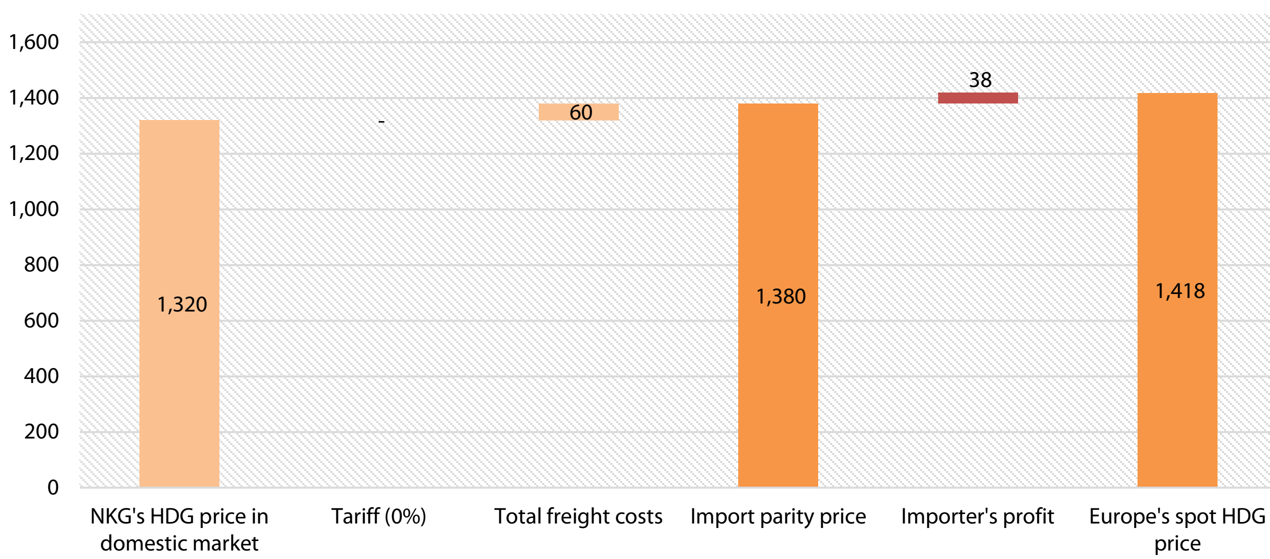
Source: US's International Trade Administration, Rong Viet Securities

Profitability in European markets has been thinner in 4Q, but Vietnamese producers have cost advantages in the next three-four years.

Hot-rolled coil and hot-dipped galvanized steel prices have decreased in October by roughly 9.3% and 8.0% MoM respectively. Hence, NKG's profitability in Europe may decrease in 4Q2021 and 1Q2022, but it can recover from 2Q2022. Firstly, steel prices can be supported by increasing steel production costs in Europe because energy prices have been rising caused by the shortage of gas. As energy prices in Europe have rallied to all-time highs, ArcelorMittal and British Steel announced a temporary energy surcharge of USD 58/ton and USD 34/ton respectively. Finally, consumption in Europe could be stronger in March due to favorable weather, thus, supporting steel demand.

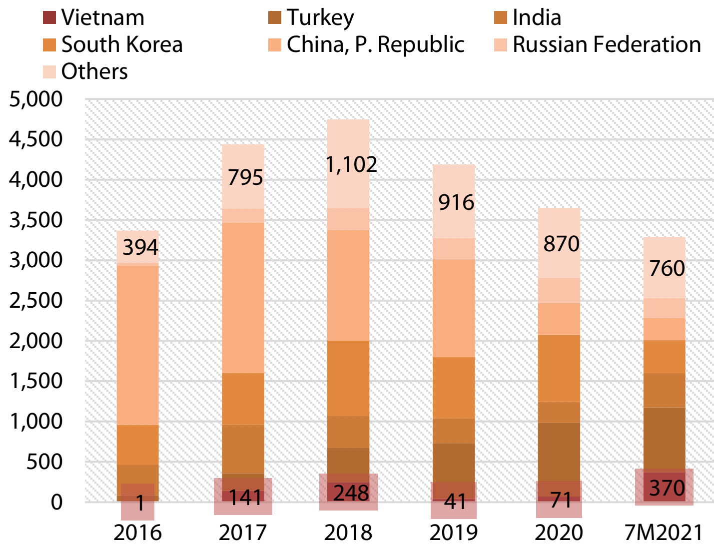
For 2022, we think Vietnam's producers will have a chance to expand their market share in Europe as main competitors face challenges related to production costs and trade policies. We estimate production costs in Europe can be USD 150-170/ton higher than Vietnam driven by carbon and electricity prices. Currently, the carbon price in Europe is roughly USD 75/ton, boosting BOF steel production cost to be USD 140/ton higher than that in Vietnam (given that producing a ton of steel by BOF emits 1.9 tons of carbon, according to WSA). Meanwhile, South Korea and India face difficulties related to trade policy as they are imposed specific quotas of only 170,000 tons/year and 210,000 tons/year respectively. Meanwhile, Turkey's HRC was imposed an anti-dumping tax of 4.7%-7.3% by the EU since April, thus, weakening its competitiveness. As can be seen in Figures 9 and 10, China's export volume decreased sharply and will continue to drop because this country wants to reduce carbon emissions. This makes room for other countries. Vietnam increased its market share to 11.2% in 7M2021 and still has the potential to grow in 2H2021 and 2022.

Figure 8: NKG's import parity price vs. Europe's spot HDG price (USD/ton) as of October 13



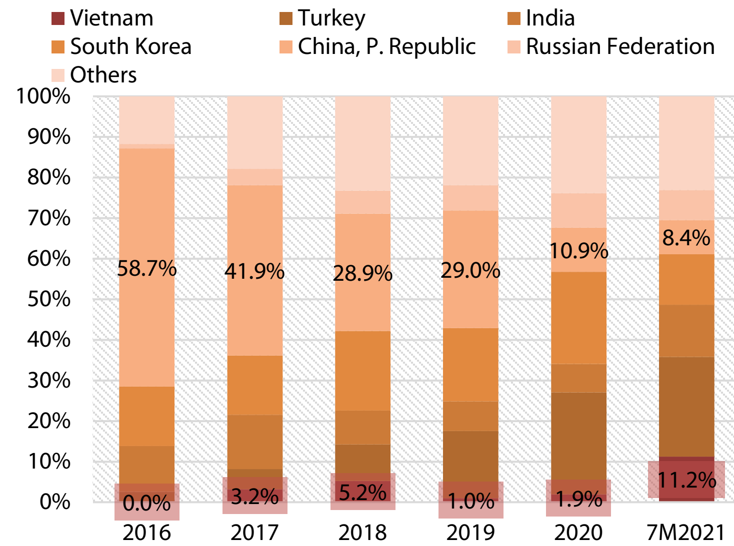
Source: Rong Viet Securities

Figure 9: EU's hot-dipped galvanized steel import volume, by country (thousand tons)



Source: EUROFER, Rong Viet Securities

Figure 10: EU's hot-dipped galvanized steel import structure



Source: EUROFER, Rong Viet Securities

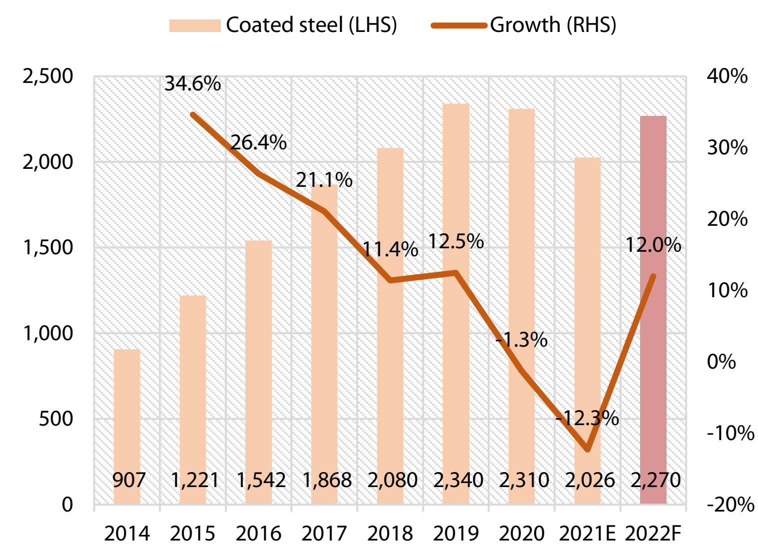
Domestic consumption can grow strongly in 4Q2021 and 2022 owing to re-opening of the economy and public investments…

The domestic demand for coated steel and steel pipes can recover in 4Q as construction activities have been allowed to continue in October in the South. We expect the recovery in domestic sales, which started in September, to continue and domestic selling volume can reach 77,000 tons in 4Q, increasing by 50.0% from a low base in 3Q. Total selling volume in 4Q is expected to reach 313,000 tons, increasing by 13.4% QoQ.

For 2022, public investments in infrastructure projects and re-opening the economy can support coated steel and steel pipe consumption. According to the medium-term public investment plan for the 2021-2025 period approved by the National Assembly, spending on transport projects accounts for a large portion. Total spending for transport projects reached VND 570.4 trillion (USD 24.8 bn), accounting for 42.3% of the central budget. The central budget expenditure plan for highway projects and key projects (such as the North-South expressway) will reach VND 183.25 trillion (USD 7.9 bn). We expect public investments to accelerate to support the economy's growth after the pandemic. Meanwhile, civil construction activities are likely to recover in 2022, boosting the demand for flat steel.

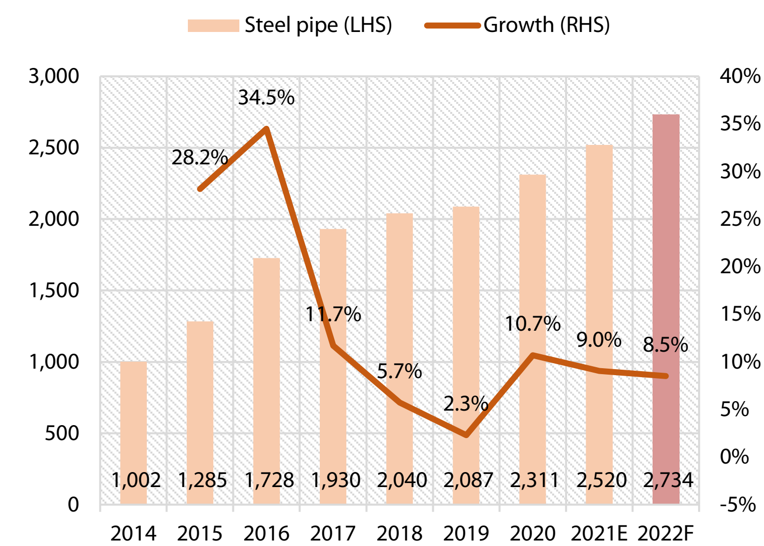
We expect domestic demand for coated steel and steel pipe to grow at a higher pace than GDP as the construction industry will be the key driver for growth. Based on the Government's 2022 GDP growth target of 6.0-6.5%, we forecast coated steel consumption in the domestic market to grow by roughly 12.0% YoY in 2022 after decreasing by an estimated 12.3% in 2021. Meanwhile, we expect steel pipe consumption to grow by 8.5% YoY in 2022.

Figure 11: Domestic coated steel consumption forecast (thousand tons)



Source: NKG, Rong Viet Securities

Figure 12: Domestic steel pipe consumption forecast (thousand tons)



Source: NKG, Rong Viet Securities

… yet decreasing flat steel prices can harm the gross margin in 1H2022.

The weak steel demand-supply in China has caused a drop in iron ore and steel prices, which also led flat steel prices in Vietnam to fall in early 4Q. The average iron ore price in October decreased by 31% compared to the average level in 3Q. Hoa Phat's HRC prices for delivery in January/2022 also decreased by 16% compared to goods delivered in July/2021. As coated steel often follow HRC prices, NKG's profitability can decrease compared to previous quarters due to inventory accumulated at a relatively high price. Hence, we forecast that GPM domestically can decrease from 9.5% in 4Q2021 to 5.6% in 1H2022, before recovering to 6.3% in 2H2022.

NKG plans to expand its production capacity in 2022.

The company will relocate its warehouse and steel pipe production line to a new factory, build in a 5-ha land bought from Dea Myung Paper company, and expand the steel pipe production capacity from 180,000 tons per year to 300,000 tons per year. After rearranging production lines, the company expects coated steel production capacity to increase by 18% from 1.1 million tons to 1.3 million tons in 2Q/2022. Total capital expenditure is estimated at roughly VND 150 bn (USD 6.6 mn). We think it is reasonable to expand capacity to seize opportunities from foreign markets as the investment is relatively small compared to potential additional NPAT. Vietnam's steel exporters will still have strong competitiveness in the next years in the European and North American markets due to less strict environmental policies, lower labor costs and electricity prices.

Forecast

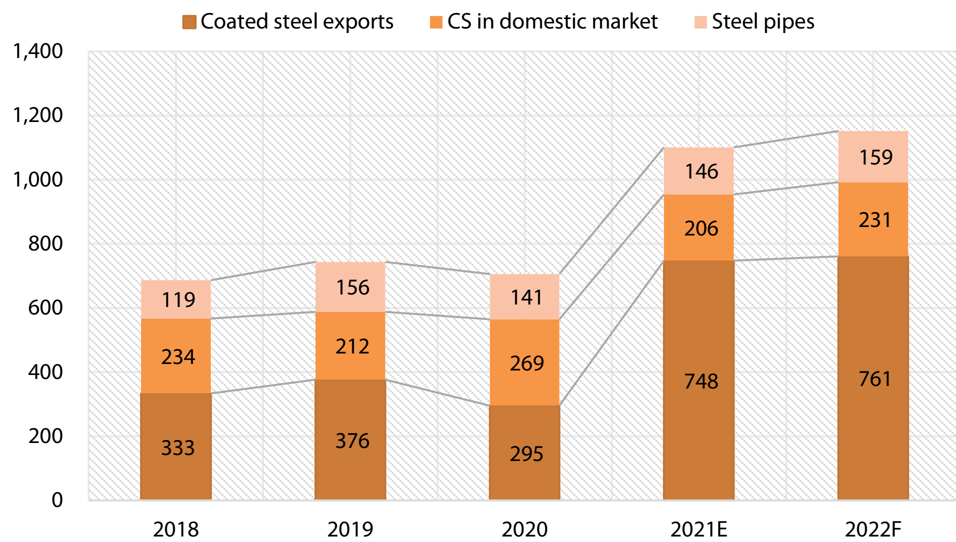
We forecast the company to sell roughly 306,000 tons of products in 4Q, increasing by 10.7% QoQ, of which domestic selling volume and export volume grow by 70% QoQ and -2.9% QoQ respectively. The company will still focus on foreign markets in 4Q as exports bring a higher gross margin compared to the domestic market and allow the company to reduce bad debt risks and receivables. NKG plans to maintain the exports' portion in total selling volume at 75%-80% in 4Q. In the exports' structure, we expect it may increase North America's portion in 4Q2021 and 1Q2022 due to higher gross margin. This trend can offset partially lower profitability in Europe. Exports' GPM can be high at 16.5% in 4Q2021 and 16.0% in 1Q2022, but a bit lower than that of 19.0%-21% in 2Q and 3Q2021.

For 2022, we expect that NKG's selling volumes in coated steel and steel pipe segments will grow by 4.0% and 8.8% to 1.0 million tons and 159,000 tons respectively. Exports would account for 66% of total selling volume, decreasing from an estimated 68% in 2021.

NKG's profitability can decline as steel prices in Europe are decreasing and selling price can take a correction caused by falling iron ore prices, but lower transportation costs can support NPAT. We forecast that NKG's gross margin can decrease from an estimated 16.4% in 2021 to

11.9% in 2022, of which exports margin can decline from an estimated 17.8% in 2021 to 14.6% in 2022. Besides, logistic disruption can be solved, leading to lower transportation costs, which accounted for 92% of selling expenses in 1H2021. Hence, we forecast selling expenses/sales ratio can decrease from an estimated 4.8% in 2021 to 4.0% in 2022.

Figure 13: Selling volume forecast (thousand tons)



Source: NKG, Rong Viet Securities

Valuation

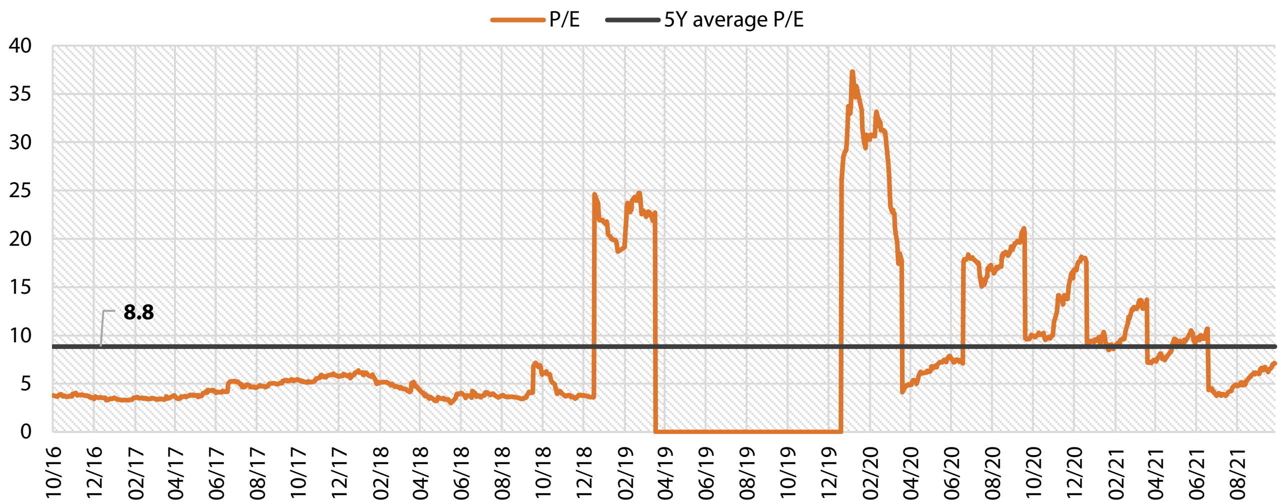
We use two methods to evaluate the stock: FCFF and PE. In the FCFF method, we apply a WACC of 12.4% and exit EV/EBITDA of 6.5x and come up with a target price of VND 48,300/share. We apply a P/E ratio of 5.7, which is roughly 35% lower than the 5-year average level of 8.8, for the 2022 EPS. The target price based on the P/E method is VND 47,500/share. Hence, our fair value comes at **VND 48,000 value per share**, implying **a total return of 29%** as of the closing price on **December 13th, 2021.**

Table 1: NKG valuation

Method	Weight	Price	Contribution
FCFF	50%	48,300	24,150
P/E (5.7x)	50%	47,500	23,750
Target price			**48,000**
Current market price			37,900
Cash Dividend			1,000
Total stock return			**29%**

Source: Rong Viet Securities

Figure 14: Historical P/E ratio



Source: Bloomberg, Rong Viet Securities

VND Billion

INCOME STATEMENT	2019	2020	2021E	2022F
Revenue	12,177	11,560	27,991	29,685
COGS	11,835	10,690	23,497	26,158
Gross profit	**342**	**869**	**4,494**	**3,526**
Selling expenses	210	268	1,333	1,176
G&A expenses	69	92	136	145
Financial income	107	89	129	200
Financial expenses	275	281	354	258
Other income/loss	195	4	0	0
Gain/(loss) from JVs	0	0	0	0
PBT	**90**	**321**	**2,799**	**2,148**
Tax expense	43	25	378	246
Minority interests	0	0	0	0
PAT	**47**	**295**	**2,421**	**1,902**
EBIT	63	509	3,025	2,205

FINANCIAL RATIO	2019	2020	2021E	2022F
Growth (%)				
Revenue	-17.8	-5.1	142.1	6.1
Operating Income	-37.8	75.5	283.8	-23.7
EBITDA	-83.9	710.8	493.9	-27.1
PAT	-17.4	524.1	719.7	-21.4
Total Assets	-0.7	-6.5	91.8	1.4
Equity	1.5	5.4	83.3	27.2
Profitability (%)				
Gross margin	2.8	7.5	16.1	11.9
EBITDA margin	4.1	7.7	12.1	8.7
EBIT margin	0.5	4.4	10.8	7.4
Net margin	0.4	2.6	8.7	6.4
ROA	0.6	3.9	16.7	13.0
ROE	1.7	13.7	49.0	28.2
Efficiency				(times)
Receivable Turnover	13.9	8.0	8.0	10.3
Inventory Turnover	4.6	5.0	3.8	4.3
Payable Turnover	6.2	8.1	5.0	6.5
Liquidity				(times)
Current	1.0	1.1	1.4	1.7
Quick	0.4	0.6	0.6	0.8
Finance Structure (%)				
Total Debt/Equity	102.5	94.4	64.4	40.0
Current Debt/Equity	79.2	79.2	61.3	38.1
Long-term Debt/Equity	23.3	15.2	3.1	2.0

VND Billion

BALANCE SHEET	2019	2020	2021E	2022F
Cash and cash equivalents	76	219	964	1,475
Short-term investments	702	370	665	1,330
Accounts receivable	877	1,439	3,503	2,888
Inventories	2,589	2,150	6,157	6,063
Other current assets	191	95	76	84
Property, plant & equipment	3,260	2,936	2,774	2,497
Acquired intangible assets	247	249	242	236
Long-term investments	48	23	23	23
Other non-current assets	74	63	66	69
Total assets	**8,064**	**7,544**	**14,470**	**14,666**
Accounts payable	1,904	1,317	4,715	4,014
Short-term borrowings	2,389	2,520	3,578	2,827
Long-term borrowings	703	482	181	145
Other non-current liabilities	2	2	2	2
Bonus and Welfare fund	49	41	162	257
Technology-science, dev. fund	0	0	0	0
Total liabilities	**5,048**	**4,362**	**8,638**	**7,244**
Common stock and APIC	2,586	2,586	2,950	2,950
Treasury stock (enter as -)	0	-78	0	0
Retained earnings	356	576	2,665	4,158
Other comprehensive income	36	37	37	37
Inv. and Dev. Fund	39	60	181	276
Total equity	**3,017**	**3,181**	**5,833**	**7,421**
Minority Interest	**0**	**0**	**0**	**0**

VALUATION RATIO	2019	2020	2021E	2022F
EPS (dong)	118	1,101	10,533	8,137
P/E (x)	26.5	9.2	4.0	5.2
BV (dong)	13,813	14,566	26,706	33,843
P/B (x)	0.4	0.9	1.6	1.3
DPS (dong/cp)	0	300	1,000	1,000
Dividend yield (%)	0.0	0.0	2.4	2.4

VALUATION MODEL	*Price*	*Weight*	*Average*
FCFF	48,300	48,300	24,150
PE	47,500	47,500	23,750
Target price			**48,000**

VALUATION HISTORY	*Price*	*Recommendation*	*Period*
08/31/2018	18,000	BUY	Intermediate
03/25/2021	24,700	ACCUMULATE	Intermediate
10/13/2021	62,000	BUY	Intermediate

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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