COTECCONS CONSTRUCTION JSC (CTD – HSX)

Diversifying for Future Growth

Particulars (VND bn)	Q2-FY17	Q1-FY17	+/- qoq	Q2-FY16	+/- yoy
Net revenue	6,183	4,361	42%	5,003	24%
PAT	412	301	37%	355	16%
EBIT	407	375	9%	443	-8%
EBIT margin	6.6%	8.6%	-202bps	8.8%	-226bps

Source: CTD, RongViet Research

H1 2017 Performance: Tracking Closely to the Guidance

- Most figures are in line with the company's annual target as well as our expectation.
- Profit margins declined in Q2 due to increasing COGS and salary expenses.
- Coteccons signed over VND14,300 billion value of new contracts in H1 2017. Backlog at Q2/2017 was over VND26,000, +17% YoY.

Q3/2017 Potential: The Domestic Construction Demand is Still Abundant

Our forecast includes a 34% revenue growth and 28% NPAT growth. We remain our 2017 forecast for CTD, as Coteccons' revised targets are akin to those in our 2017 Strategy Report. Many of the new contracts are large projects such as Ho Tram Strip and Diamond Island- Phase 2, which are expected to contribute remarkably to CTD's performance.

Regarding financials, we forecast that CTD will manage to maintain their net working capital on a neutral level, as their market power and internal resources are sufficient for the company to be debt-free while disbursing on Capex for machinery. CTD's cash surplus is going to produce a considerable amount of interest income for CTD in 2017. On the other hand, we anticipate a surge in G&A expenses due to a higher level of compensation for employees as well as a decrease in reversals of provisions for doubtful debts.

Valuation and Recommendation*: CTD is an outstanding construction contractor in the domestic market and the company has proven the power to win the largest bids as well as the internal resources to satisfy clients' demand in terms of design capacity and progress. Despite the market concerns over the peaking housing sector, we anticipate a sustainable growth in other segments of the real estate market including industrial, commercial and infrastructure, which will manage to keep the construction demand growth. Subsequently, as the leading firm, CTD is able to develop new growth drivers as well as to skim the most profitable jobs in the market. The company is going to adapt to a new revenue structure, which allows them to diversify their portfolio and maintain a decent growth rates over the next three-year period.*

We evaluate CTD price at ***VND251,200/share****, which is* ***20.6%*** *higher than the closing price on 31st July 2017 and we recommend* ***ACCUMULATING*** *the stock in the* ***Long-term****. This target price is revised from that in our 2017 Strategy report published in March because we raise the forecast for the upcoming years based on CTD's potential. It should also be noticed that we use the forecasted 2018 EPS in the P/E valuation to address the new time horizon.*

**current room (at 49% FOL). FOL has been approved to raise to 60%.*

ACCUMULATE

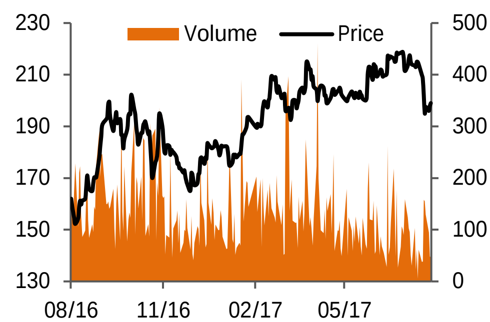
CMP (VND)	208,300
Target Price (VND)	251,200
Investment Period	**Long-term**

Stock Info

Sector	Construction & Materials
Market Cap (VND B)	16,036
Current Shares O/S	76,983,344
Beta	0.79
Free float (%)	89.07
52 week High	218,800
52 week Low	152,250
Avg. Daily Volume (20 sessions)	76,221

	FY2016	Current
EPS	20,894	20,254
EPS Growth (%)	88.62	-10.54
Adjusted EPS	15,093	17,986
P/E	8.73	9.87
P/B	2.25	2.36
EV/EBITDA	6.03	6.37
Cash dividend	5,500	5,000
ROE (%)	28.51	28.11

Price performance



Major Shareholders (%)

KUSTOSHEM	18.0
Thanh Cong Com&Inv Ltd.	14.5
Nguyen Ba Duong	4.7
Foreign ownership room (%)	3.2*

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Exhibit 1: Q2/2017 Results

Particulars (VND bn)	Q2-FY17	Q1-FY17	+/- (qoq)	Q2-FY16	+/- (yoy)	H1-FY17	+/-(yoy)
Net revenue	6,183	4,361	41.8%	5,003	23.6%	10,544	29%
Gross profit	497	382	30.2%	411	20.8%	879	20%
SG&A	90	95	-5.3%	25	253.5%	184	75%
Operating income	407	287	41.9%	386	5.5%	694	20%
EBITDA	424	389	8.9%	455	-6.8%	813	7%
EBIT	407	375	8.5%	443	-8.0%	783	7%
Financial expenses	0	-	-	-	-	0	-50%
- Interest Expenses	-	-	-	-	-	-	-
Dep. and amortization	17	14	19.1%	12	35.5%	31	19%
Non-recurring items (*)							
Extraordinary items (*)							
PBT	517	375	37.8%	443	16.8%	892	20%
PAT	412	301	37.2%	355	16.2%	713	22%
(*) Adjusted PAT	412	301	37.2%	355	16.2%	713	22%

Source: CTD, RongViet Research

Exhibit 2: Q2/2017 Performance Analysis

Particulars	Q2-FY17	Q1-FY17	+/- (qoq)	Q2-FY16	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	8.0%	8.8%	-72bps	8.2%	-18bps
EBITDA Margin	6.9%	8.9%	-207bps	9.1%	-224bps
EBIT Margin	6.6%	8.6%	-202bps	8.8%	-226bps
Net Margin	6.7%	6.9%	-22bps	7.1%	-42bps
Adjusted Net Margin	6.7%	6.9%	-22bps	7.1%	-42bps
Turnover *(x)					
-Inventories	16.3	12.7	3.6	14.1	2.1
-Receivables	6.7	5.0	1.6	7.7	-1.0
-Payables	4.2	3.1	1.0	4.3	(0.2)
Leverage (%)					
Total Debt/ Equity	101.3%	76.0%	2,526bps	132.6%	-3,134bps

Source: CTD, (*) Annualized turnover

Exhibit 3: Q3/2017 Performance Forecast

Particulars (VND bn)	Q3/2017	+/- QoQ	+/- YoY
Revenue	7,107	15%	34%
Gross profit	601	21%	31%
EBIT	490	20%	8%
NPAT	469	14%	28%

Source: CTD, RongViet Research

Updates:

CTD is going to raise their FOL in the near future, which was approved at the 2017 AGM. The current cap of 49% will be lifted to 60%, which can be attractive as the remaining room is only few percent.

As mentioned above, we anticipate a change in CTD's revenue structure in the future. Even though the contribution from the residential segment still accounted for over 70% of CTD's revenue in 1H2017, we expect some stagnation in the number of new housing projects in the long term. Moreover, we also expect the leading firm in the industry to be a pioneer in diversifying the backlogs toward other market segments including commercial and office buildings, industrials and even infrastructure. We notice several signals of CTD reforming their revenue structures.

Regarding commercial and office buildings, it is estimated that among VND14,000 billion new contracts signed in 2017 until now, over 50% is the value of commercial and housing complex, hotels and office buildings. The figure was only 15% in 2016, which we attribute to the number of new housing projects levering off and a stronger growth of new commercial-housing complex projects. In fact, it was reported by CBRE that the office rental's vacancy rate kept stable in both HCMC and Hanoi even though the supply increased, which implies an ample potential for this segment in the future. According to the same source, decentralisation is the trend in both cities, which means the upcoming office tower projects are going to produce a strong demand for construction in the suburban districts.

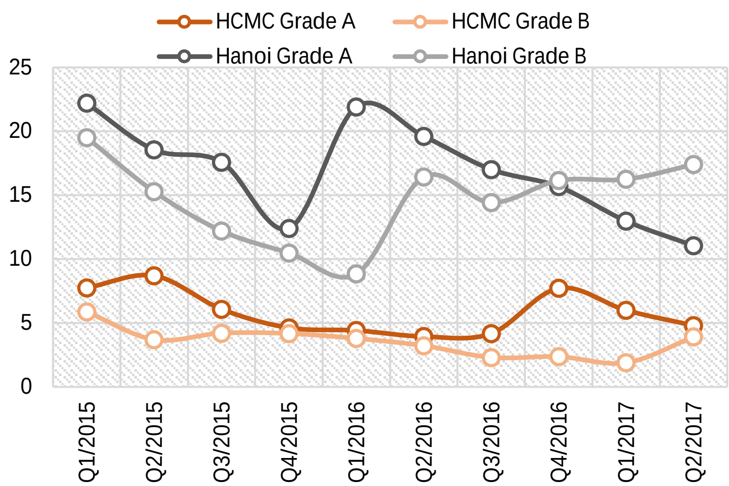
In terms of industrial projects, we expect this segment to contribute more into CTD's revenue in the future. Industrial construction used to account for a large part of CTD's revenue but shrinking, which were 38%, 17% and 9% in 2015, 2016 and H1 2017 respectively. During difficult times of the construction industry, factory-building activity was one of the factors that prevent further deterioration for the company, which suffered from moderate decrease in revenue in 2012 compared to 2011. We consider the construction demand from manufacturers to be more stable over the years and less risky than that of real estate developers, thus the segment can help CTD reduce the risk of depending on the housing market.

More importantly, we notice that CTD's recent backlog at the end of Q2 2017 has not yet included the value of Dung Quat Steel Complex, a project of Hoa Phat Group (HPG-HSX). Even though Coteccons has announced its participation as a construction contractor, the particular signed value has not been publicized. A co-contractor for this project is Hoa Binh Corporation (HBC-HSX), who has just announced being chosen by HPG to execute the construction and similarly did not provide the specific contract value. However, the whole project's construction value is calculated at VND10,000 billion which, if equally divided between CTD and HBC, would lead to VND5,000 billion share of revenue each, which would likely represent the largest project in both companies' backlogs. Nevertheless, we expect CTD to be assigned a larger part of the sum since they are more experienced in the industrial construction, thus the actual backlog of CTD at the end of Q2 could be at least 20% higher than the announced figure.

Subsequent to the news at Dung Quat Steel Complex, Coteccons also won the VND2000-billion bid as the D&B contractor at Shenzhou's textile factory. It is essential that CTD's reputation and capacity can win them mass industrial projects, whose average size can be superior to that of the average housing project. While most real estate bids stay below VND2,000 billion, there are an increasing number of mass manufacturing projects being initiated. Compared to the housing projects' risky cash flows that are highly dependent on the developers' sales activities, factory owners such as HPG and Shenzhou are more likely to fulfill their financial obligations to the contractors. Therefore, we consider the two industrial projects that CTD has just won to be firm signals for a change in CTD's revenue structure toward a less risky backlog and a higher diversification, taking advantage of the rising industrialisation trend in Vietnam.

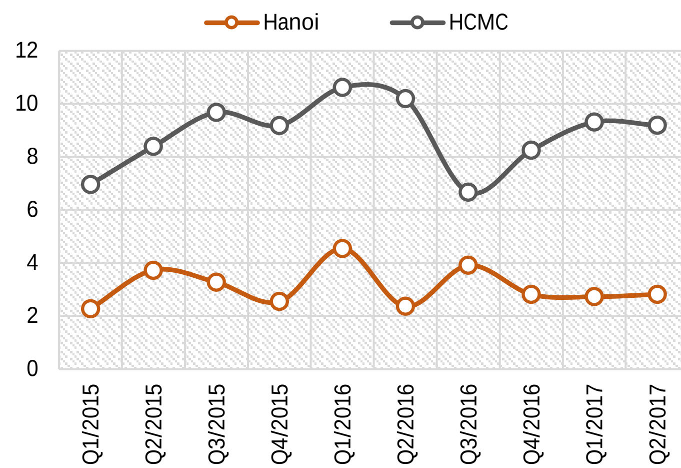
Appendix:

Figure 1: Office Vacancy Rate (%)



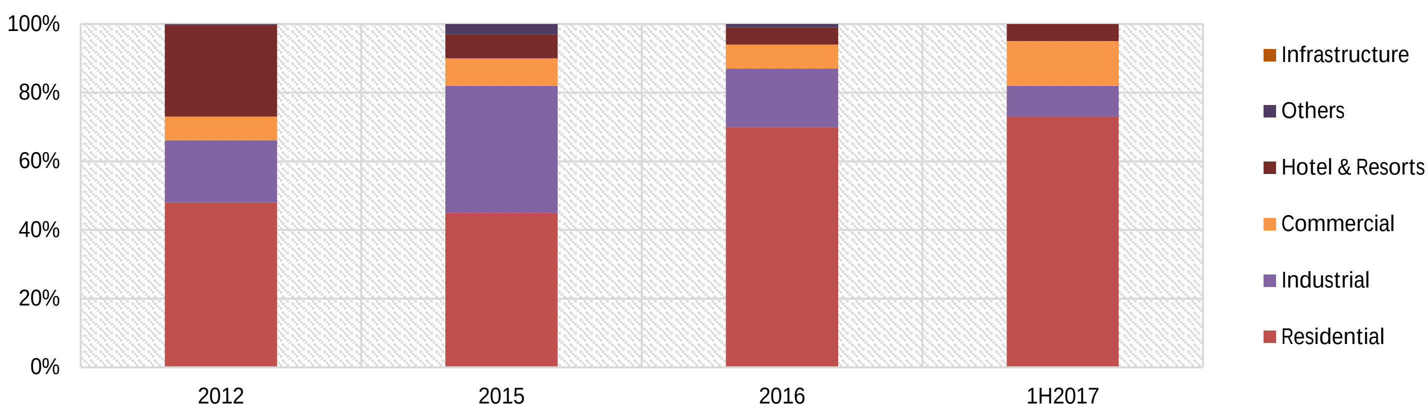
Source: CBRE

Figure 2: CBD Retail Vacancy Rate (%)



Source: CBRE

Figure 3: Revenue Breakdown



Source: CTD, RongViet Research

VND billion

INCOME STATEMENT	FY2015	FY2016	FY2017E	FY2018F
Revenue	13,669	20,783	27,107	33,800
COGS	12,557	18,983	24,814	30,882
Gross profit	1,112	1,799	2,293	2,918
Selling Expense	0	2	0	0
G&A Expense	363	297	425	529
Finance Income	126	170	307	338
Finance Expense	2	0	0	0
Other profits	39	60	45	34
PBT	927	1,763	2,237	2,777
Prov. of Tax	194	341	447	559
Minority's Interest	67	0	0	0
PAT to Equity S/H	666	1,422	1,789	2,218
EBIT	749	1,500	1,868	2,389
EBITDA	794	1,554	1,916	2,459

%

FINANCIAL RATIO	FY2015	FY2016	FY2017E	FY2018F
Growth				
Revenue	79.1%	52.0%	30.4%	24.7%
Operating Income	111.2%	95.7%	23.3%	28.4%
EBITDA	119.5%	100.3%	24.5%	27.9%
PAT	103.5%	113.5%	25.8%	24.0%
Total Assets	60.7%	50.2%	19.6%	23.3%
Equity	28.3%	92.2%	20.2%	22.3%
Profitability				
Gross margin	8.1%	8.7%	8.5%	8.6%
EBITDA margin	5.8%	7.5%	7.1%	7.3%
EBIT margin	5.5%	7.2%	6.9%	7.1%
Net margin	4.9%	6.8%	6.6%	6.6%
ROA	8.5%	12.1%	12.7%	12.8%
ROE	20.5%	22.8%	23.9%	24.2%
Efficiency				
Receivable Turnover	5.2	6.0	5.9	5.9
Inventory Turnover	11.9	15.3	14.3	12.0
Payable Turnover	2.8	3.5	3.8	3.8
Liquidity				
Current	1.4	1.8	1.8	1.8
Solvency				
Total Debt/Equity	0.0%	0.0%	0.0%	0.0%
Current Debt/Equity	0.0%	0.0%	0.0%	0.0%
Long-term Debt/Equity	0.0%	0.0%	0.0%	0.0%

VND billion

BALANCE SHEET	FY2015	FY2016	FY2017E	FY2018F
Cash and cash equivalents	1,462	1,997	2,273	2,712
Short-term investments	928	2,675	2,943	3,384
Accounts receivable	2,609	3,484	4,597	5,732
Inventories	1,051	1,241	1,737	2,573
Other current assets	436	547	300	330
Property, plant & equipment	480	589	953	1,303
Acquired intangible assets	100	92	91	91
Long-term investments	493	715	731	747
Other non-current assets	257	401	421	442
Total assets	**7,815**	**11,741**	**14,045**	**17,314**
Accounts payable	4,502	5,393	6,467	8,049
Short-term borrowings	0	0	0	0
Long-term borrowings	0	0	0	0
Other non-current liabilities	13	12	13	15
Bonus and Welfare fund	57	102	72	89
Technology-science, dev. fund	0	0	0	0
Total liabilities	**4,573**	**5,507**	**6,552**	**8,152**
Common stock and APIC	1,854	3,729	3,781	3,781
Treasury stock (enter as -)	-2	-2	-2	-2
Retained earnings	639	1,435	1,927	2,708
Other comprehensive income	0	0	0	0
Inv. and Dev. Fund	751	1,071	1,787	2,674
Total equity	**3,243**	**6,234**	**7,493**	**9,162**
Minority Interest	**0**	**0**	**0**	**0**

VALUATION RATIO	FY2015	FY2016	FY2017E	FY2018F
EPS (dong)	7,027	15,093	20,564	25,196
P/E (x)	12.9	9.9	9.7	7.9
BV (dong)	69,199	80,904	95,630	116,926
P/B (x)	1.6	2.3	2.1	1.7
DPS (dong/cp)	5,000	5,500	5,000	3,900
Dividend yield (%)	4.50%	3.01%	2.76%	2.51%

VALUATION MODEL	Price	Weight	Average
FCFF	250,408	50%	125,204
PE	251,960	50%	125,980
Target price (dong)			**251,200**

VALUATION HISTORY	Price	Recommendation	Period
15/03/2017	237,700	Accumulate	Long term

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Intermediate- term (up to 6 months)	>20%	10% to 20%	-5% to10%	-15% to- 5%	<-15%
Long-term (over 6 months)	>30%	15% to 30%	-10% to 15%	-15% to -10%	<-15%

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