

PetroVietnam Southern Gas (PGS - HNX)

Difficulty in CNG volume growth

Particulars (VND bn)	4QFY13	3QFY13	% (qoq)	4QFY12	% (yoy)
Net Revenues	2,101.5	1,815.1	16%	1,646.3	28%
EBIT	27.9	53.5	-48%	58.5	-52%
PAT	57.3	87.6	-35%	103.0	-44%
EBIT margin (%)	2.7%	4.8%	-210bps	6.3%	-353bps

Sources: PGS

- **2013 revenue came in close proximity to RongViet's forecast but profit was considerably lower due to Q4's dramatic drop.**
- **Q1/2014 started with difficulties.**
- **2014 consolidated earnings is seen to exceed the annual plan by 6.6%.**
- **Biomass, alternative fuel may prove problematic for expanding CNG segment business in the following years.**

Outlook: We still highly value the prospect of PGS' CNG business in the long-term although the company started off the year with some difficulties, such as the increase in CNG input price and the parting with one of its biggest clients due to biomass. As a silver lining, the subsidiary CNG Vietnam should maintain satisfying output while the accelerated depreciation policy would help CNG it finish depreciating as early as Q2. Nonetheless, we are concerned about the fact that the LPG business has not showed much efficiency and that surprises in cost accounting could make earnings results increasingly difficult to forecast.

In this update, we revise out forecast for PGS net profits in 2014 down from VND252.3 bn to VND172.4 bn due to: (i) lower profits expected for VT-Gas, (ii) a decrease in the CNG volume of the parent company, (iii) a assumed 2-percent increase in CNG selling price this year. As the underlying 2014 EPS is VND4,536, we rate this stock as **NEUTRAL** for the **INTERMEDIATE TERM**.

Key financials

Y/E Dec (VND bn)	FY2011	FY2012	FY2013	FY2014F
Net Revenues	5,764.2	6,374.9	6,902.0	7,264.0
% chg	55.6%	10.6%	8.3%	5.2%
PAT	238.5	151.3	179.0	172.4
% chg	5.7%	-36.6%	18.3%	-3.7%
EBIT margin (%)	4.1%	2.4%	2.6%	2.4%
ROA (%)	8.3%	4.9%	6.0%	5.7%
ROE (%)	43.8%	19.5%	20.8%	17.8%
EPS (VND)	6,518	3,981	4,711	4,536
Adjusted EPS (VND)	1,731	1,403	4,711	4,536
Book value (VND)	19,398	21,325	24,040	26,987
Cash dividend (VND)	2,300	1,200	1,500	1,500
P/E (x)	2.9	4.3	6.0	8.2 *
P/BV (x)	1.0	0.8	1.2	1.1*

Sources: PGS, RongViet Securities, * Price as of 25/03/2014

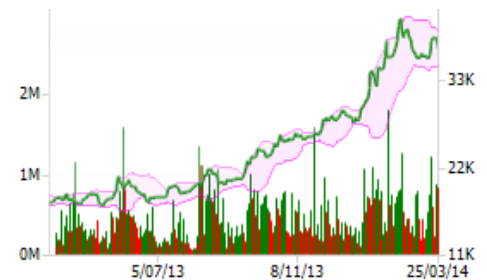
NEUTRAL

CMP (VND)	37,100
Target Price (VND)	40,000

Investment Period	Intermediate
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Stock Info

Sector	Utilities
Market Cap (VND bn)	1,459
Current Shares O/S	38,000,000
Beta	1.63
Free float (%)	52.2
52 weeks High	41,300
52 weeks Low	15,800
Avg. Daily Volume (in 20 sessions)	580,893



Performance (%)

	3M	1Y	3Y
PGS	32.4	127.2	137.0
Utilities	26.7	82.5	N/A
HNX30 Index	43.5	57.1	N/A
HNIndex	33.9	47.0	-4.7

Major Shareholders (%)

PV-Gas	35.26
Halley Sicav-Halley Asian Property	8.00
Dai A Bank	4.56
Foreign Investors Room (%)	26.2

My Tran

(084) 08- 6299 2006 – Ext 348

my.tth@vpsc.com.vn

Exhibit 1: 4QFY2013

Particulars (VND bn)	4QFY13	3QFY13	% chg (qoq)	4QFY12	% chg (yoy)
Net Revenues	2,101.5	1,815.1	15.8	1,646.3	27.7
Gross profits	259.9	297.0	-12.5	304.9	-14.7
SG&AC	217.7	212.3	2.5	181.7	19.8
Operating Income	42.3	84.7	-50.1	123.2	-65.7
EBITDA	95.9	164.3	-41.6	170.7	-43.8
EBIT	57.3	87.6	-34.6	103.0	-44.3
Financial expenses	10.6	13.4	-20.6	45.8	-76.8
- Interest Expenses	9.4	9.4	-0.1	12.1	-21.9
Dep. and amortization	-38.6	-76.6	-49.6	-67.7	-43.0
Non-recurring Items (*)					
Extraordinary Items (*)	6.9	0.5	1193.4	6.7	2.0
PBT	47.9	78.2	-38.7	91.0	-47.3
PAT	27.9	53.5	-47.8	58.5	-52.3
(*) Adjusted PAT	21.9	53.0	-58.6	53.3	-58.9

Sources: PGS, RongViet Securities

Exhibit 2: 4QFY2013 performance analysis

Particulars	4QFY13	3QFY13	% chg (qoq)	4QFY12	% chg (yoy)
Profitability Ratios (%)					
Gross Margin	12.4	16.4	-399bps	18.5	-615bps
EBITDA Margin	4.6	9.0	-448bps	10.4	-581bps
EBIT Margin	2.7	4.8	-210bps	6.3	-353bps
Net Margin	1.3	2.9	-162bps	3.6	-223bps
Adjusted Net Margin	1.0	2.9	-188bps	3.2	-219bps
Turnover *(x)					
-Inventories	41.6	59.0	-17.4	42.3	-0.8
-Receivables	10.7	10.5	0.2	10.6	0.1
-Payables	24.4	27.0	-2.7	23.3	1.1
Leverage (%)					
Total Debt/ Equity	2.1	2.1	0.0	2.4	-0.3

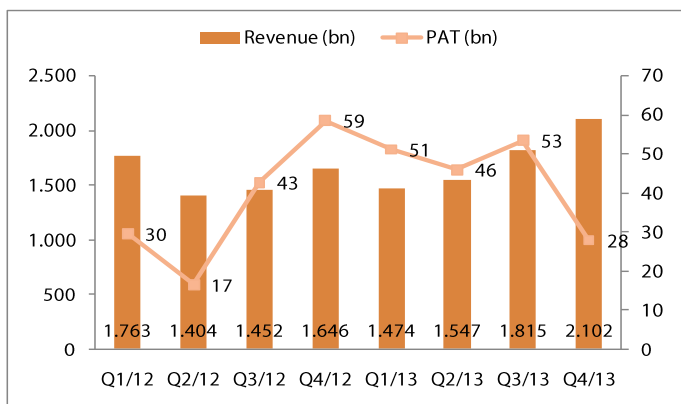
Sources: PGS, (*) Annualized turnover

2013 revenue came in close proximity to RongViet's forecast but profit was considerably lower due to Q4's dramatic drop.

Revenue from the LPG and CNG were VND4,327 bn (-4% yoy) and VND1,187 bn (+33% yoy), respectively. The LPG arm remained stable while CNG took off during the year, mainly thanks to the increase in volume. According to PGS, CNG sale volume reached 78.4 million cubic meters, up by 10.2% as compared to the previous year.

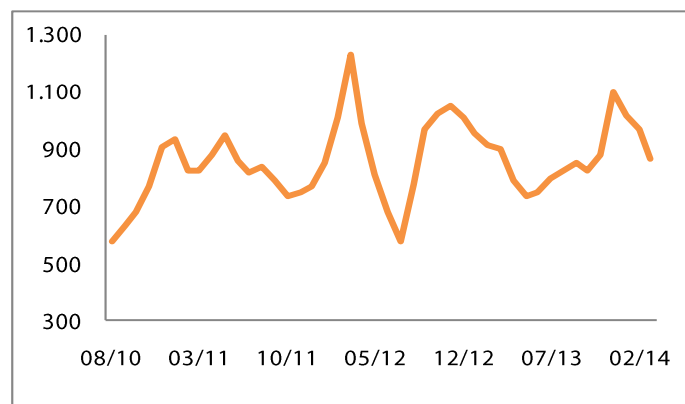
The Company's profit steadied at VND50 bn each quarter in the first nine months but dropped sharply in Q4, causing net income for the parent company's shareholders to reach only VND179 bn for the year of 2013. As explained by PGS, the LPG business was not very good and many additional costs incurred in the last quarter (corporation brand promotion, insurance, compensation and incentives, etc...). Besides, as we have observed, it is possible that the subsidiary VT-Gas did record a loss in Q4, which negatively affected to the consolidated earnings.

PGS's quarterly revenue and net profit price chart



Source: PGS

LPG price chart



Source: Aramco

Q1/2014 started with difficulties

Because of the seasonal factor, LPG price has begun to subside since Jan and is now trading at 863 USD/ton, down 22% from the end of 2013. The LPG business thus has been struggling with a lower profit margin since year-start. We estimate that the LPG volume of the parent company in Q1/2014 may decrease by 5% qoq to around 41,000 tons or about 19% of the projected volume for the year 2014 (~213,000 tons).

The CNG segment has also had a hard time as one of the largest clients of PGS, namely Ajinomoto, which makes up about 25% of the parent company's CNG volume, terminate their gas contract in February to switch to biomass, which we will mention in more details below. However, the CNG volume of PGS in Q1 is forecasted to be maintained relatively unchanged from the same period last year, about 16.7 million m³, thanks to new customers at Long Duc Industrial Park and Y My Ceramic' continued use of CNG after a period of disruption.

In the first quarter, CNG input price was imposed a 5-percent gain from 8.93 USD/MMBTU to 9.4 USD/MMBTU. Meanwhile, as shared by the company, a raise if selling price is rather difficult now. In our forecast, we assume that the selling price will be kept unchanged in Q1, which led CNG profit margin to decrease from 46% in the end of 2013 to 43.2%.

Consolidated net profit for the parent company's shareholders in Q1 is estimated with caution at around VND37.8 billion (up 36% from Q4/2013 but down 26% from a year ago).

Exhibit 3: 1QFY2014 Forecast

Particulars (VND bn)	1QFY14	%chg (qoq)	%chg (yoy)
Net Revenues	1,422.1	-32	-3
Gross profits	248.2	-5	-6
EBIT	60.0	5	-35
PAT	37.8	36	-26

Sources: PGS, RongViet Securities

2014 consolidated earnings is seen to exceed the annual plan by 6.6%

Higher CNG input price and fixed selling price were both consistent with our forecast while the switch of some customers of PGS and CNG Vietnam to the use of biomass fuel is new information that may negatively impact CNG sale volume. In addition, VT-Gas, a subsidiary acquired by PGS in Q1/2014 at

USD3.85 million (~VND81.3 billion), has just planned net profits of about VND13.5 billion for this fiscal year, far below our previous expectation. In light of such significant events, we lower our outlook for PGS' earnings in 2014 to such that net revenue for the parent company is estimated around VND5,812 bn and gross profit around VND603 bn.

For CNG Vietnam, PGS has yet to announce the specific restructuring scheme. After CNG Vietnam's additional share issuance in Oct, 2013, PGS now has 55.2% of interest in this company. The subsidiary's operation in 2013 steadied with profit-after-tax of about VND123.9 billion, up 5.1% yoy. Like the parent company, CNG Vietnam also faced difficulties after the input as price increased 5% in Q1 and another 5% in QIII. However, we maintain our optimistic outlook for CNG Vietnam' earnings due to supporting factors such as the increase in volume and the firm's being fully depreciated since QII/2014. We estimate profit-after-tax of CNG Vietnam in 2014 at about VND158.4 billion (+28% yoy).

Revenue and profit in PGS's segments and its subsidiaries

	2012	2013	2014P	2014F	Q1/2014F
PGS parents					
LPG					
Volume (tons)	200,219	212,312	213,000	216,558	41,040
Revenue (bn)	4,485.6	4,326.6	-	4,786.0	880.3
CNG					
Volume (million m3)*	63.7	78.4	69.0	70.2	16.7
Revenue (bn)	764.0	1,092.9	-	1,004.7	232.8
PGS parents					
Total revenue	5,254.4	5,431.9	5,629.9	5,811.6	1,112.8
EBIT (bn)	180.9	145.8	-	101.6	34.0
PAT	154.1	155.3	96.6	123.0	45.2
CNG Vietnam					
Volume (million m3)*	53.1	62.4	70.0	71.4	15.0
Revenue (bn)	801.2	949.8	999.6	1,094.1	225.3
EBIT (bn)	138.2	134.7	-	171.5	20.5
PAT	117.9	123.9	110.0	158.4	19.8
PAT VT-GAS**	23.1	12.1	13.5	16.2	4.1
Other profit	11.3	2.2	-	0.0	0.0
PAT consolidated	150.6	179.0	163.7	172.4	37.8

Source: PGS, RongViet Securities

* Due to the loss of a big client, we adjust the CNG volume forecast for the parent company down 19.5% from the previous estimate (02/01/2014) to 70 million m3. For CNG Vietnam, the projected volume is revised up to 71.4 million m3 based on the recovery in the business of construction material producers being CNG Vietnam's customers.

** Profit-after-tax of VT-Gas in 2014 is revised up 46% from the previous estimate (02/01/2014) to VND16.2 billion.

On the above notions about PGS prospects, we estimate the company's 2014 consolidated revenue at about VND7.264 bn (+5.2% yoy) and profit-after-tax at VND172.4 bn (-3.7% yoy), translating to EPS of VND4,536. Cash dividend for this fiscal year is expected to be increased from 12% to 15%.

Biomass, alternative fuel may prove problematic for expanding CNG segment business in the following years.

As an energy source created from the by-products of agriculture (straws, sugar cane dregs, rice husk...) and forestry (scrap wood, firewood...), biomass stands for mass production in of the agriculture-based economy like Vietnam. In industrial manufacturing, biomass is mainly used for heating steam compressors. From the economics view, biomass could save its users about 30-50% energy costs as compared with CNG. However, one of the constraints of biomass is that its thermal conversion rate makes it suitable only for food manufacturing (MSG, milk, beer, confectionary...). Construction material manufacturers (steel, ceramic...) need fuels with higher and more stable heat-generating efficiency. In addition, factories that use biomass need a sufficient large land area for the building of steam compressors. The construction as well as necessary procedures on environmental safety need to make such specialized facilities functional could take 5-10 months to complete, depending on the factory size. Thus, CNG suppliers would not be ill-prepared when their customers decide to stop using the gas. This supports our theory that PGS probably have accounted for Ajinomoto loss in their projected CNG volume in 2014.

Amongst current clients of CNG Vietnam, Vinamilk is a big client in confectionary industry and according to PGS, the country's largest milk producer has already considered switching to biomass. By the information we have in hands, a factory of Vinamilk at My Phuoc 2 Industrial Park has been using Biomass since Q4/2013, while another plant at VSIP1 is building steam compressor in order to prepare for the fuel switch somewhere between the late of 2014 and early of 2015. Thus, it is possible that CNG Vietnam will lose about 12.5% of its CNG volume after Vinamilk's departure in 2015.

In the midst of worries over the risk of competition with biomass, PGS announced that they have found new customers (Long Duc Industrial Park, Y My Ceramic, Tay Do Construction Material...), who could compensate for 70-80% of the lost volume. Besides, under optimistic outlook for the construction sector, the possibility that construction material manufacturers would increase capacity may lift concerns over CNG volume growth. Nevertheless, we still apply more caution against our expectation of the CNG volume of the parent company PGS as well as the risk premium in our valuation model for the stock.

Outlook

We still highly value the prospect of PGS' CNG business in the long-term although the company started off the year with some difficulties, such as the increase in CNG input price and the parting with one of its biggest clients due to biomass. As a silver lining, the subsidiary CNG Vietnam should maintain satisfying output while the accelerated depreciation policy would help CNG it finish depreciating as early as Q2. Nonetheless, we are concerned about the fact that the LPG business has not showed much efficiency and that surprises in cost accounting could make earnings results increasingly difficult to forecast.

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Exhibit 4: Key Assumptions

Particular	Earlier Estimates		Revised Estimates	
	FY2013E	FY2014E	FY2013E	FY2014E
Revenue growth (%)	7.6	3.9		5.2
LPG volume growth (%)*	0.9	2		2
CNG volume growth (%)	38	7.1		0.5
Gross margin (%)	17.8	19.1		15.3
EBIT margin (%)	5.5	5.1		4.3

Sources: RongViet Securities, * the parent company

Exhibit 5: Changes in Estimates

Particular (VND bn)	FY2013E			FY2014E		
	Earlier Estimates	Revised Estimates	Var (%)	Earlier Estimates	Revised Estimates	Var (%)
Net Revenues	6,857.7	6,902.0	1	7,125.7	7,264.0	2
Gross profits	17.8%	15.9%	-11	19.1%	15.3%	-19
SG&AC	849.9	792.3	-7	977.1	850.3	-13
Operating Income	373.8	303.7	-19	381.3	264.6	-31
Financial expenses	79.9	81.0	1	47.0	50.0	6
PBT	333.2	278.1	-17	364.3	264.6	-27
PAT	215.2	179.0	-17	252.3	172.4	-32
EBITDA	690.3	655.5	-5	658.2	595.8	-9
EBIT	378.6	339.0	-10	411.3	311.6	-24
EPS (VND)	5,663	4,711	-17	6,640	4,536	-32

Sources: RongViet Securities

	VND Billion			
INCOME STATEMENT	2011A	2012A	2013E	2014F
Revenue	5,764.2	6,374.9	6,902.0	7,264.0
COGS	4,803.2	5,390.9	5,806.0	6,149.1
Gross profit	961.0	984.1	1,096.0	1,114.9
Selling Expense	374.1	509.0	623.2	665.3
G&A Expense	120.9	133.5	169.1	185.0
Finance Income	48.9	40.3	34.8	30.0
Finance Expense	134.3	145.4	81.0	50.0
Other profits	12.7	18.4	20.5	20.0
PBT	393.2	255.1	278.1	264.6
Prov. of Tax	50.4	43.3	40.4	39.7
Minority's Interest	104.4	60.5	58.6	52.6
PAT to Equity Shareholder	238.5	151.3	179.0	172.4
EBIT	515.3	372.6	339.0	311.6
EBITDA	706.1	635.7	655.5	595.8

	%			
FINANCIAL RATIO	2011A	2012A	2013E	2014F
Growth				
Revenue	55.6%	10.6%	8.3%	5.2%
Operating Income	190.1%	-26.7%	-11.1%	-12.9%
EBITDA	72.1%	-10.0%	3.1%	-9.1%
EBIT	49.6%	-27.7%	-9.0%	-8.1%
PAT	5.7%	-36.6%	18.3%	-3.7%
Total Assets	31.8%	-10.8%	5.1%	-2.1%
Equity	110.3%	9.9%	12.7%	13.7%
Internal growth rate	36.8%	9.7%	15.5%	13.0%
Profitability				
Gross profit/Revenue	16.7%	15.4%	15.9%	15.3%
Operating profit/ Revenue	8.1%	5.4%	4.4%	3.6%
EBITDA/ Revenue	12.3%	10.0%	9.5%	8.2%
EBITDA/ Revenue	8.9%	5.8%	4.9%	4.3%
Net margin	4.1%	2.4%	2.6%	2.4%
ROAA	8.3%	4.9%	6.0%	5.7%
ROIC or RONA	35.9%	22.9%	22.8%	21.3%
ROAE	43.8%	19.5%	20.8%	17.7%
Efficiency				
Receivable Turnover	9.6	11.0	10.2	9.4
Inventory Turnover	45.6	54.2	35.4	27.3
Payable Turnover	4.3	5.1	5.3	5.2
Liquidity				
Current	0.9	0.9	1.1	1.1
Quick	0.9	0.8	0.9	1.0
Solvency				
Total Debt/Equity	313.1%	233.0%	208.9%	176.4%
Current Debt/Equity	50.6%	55.7%	42.6%	39.2%
Long-term Debt/ Equity	82.2%	40.1%	16.2%	14.4%

	VND Billion			
BALANCE SHEET	2011A	2012A	2013E	2014F
Cash and equivalents	586	443	594	559
Short-term investment	109	69	68	110
Receivables	628	529	819	726
Inventories	75	124	204	246
Other current assets	59	25	55	55
Total Current Asset	1,457	1,190	1,739	1,696
Tangible Fixed Assets	900	840	658	683
Intangible Fixed Assets	34	34	33	33
Construction in Progress	41	29	40	40
Investment Property	0	1	0	0
Long-term Investment	101	94	0	0
Other long-term assets	719	716	587	552
Long-term Asset	1,819	1,732	1,330	1,308
Total Asset	3,276	2,921	3,070	3,004
Payables	1,020	841	1,135	984
Other current liabilities	149	105	103	131
Current Debt	373	451	389	407
Long-term Debt	606	325	148	150
Other long-term liabilities	161	167	134	160
Total Liability	2,309	1,888	1,908	1,831
Owner's Equity	737	810	914	1,038
Capital	380	380	380	380
Retained Earnings	157	166	166	193
Funds & Reverses	154	219	321	419
Others	0	0	0	0
Total Equity	738	810	914	1,038
Minority's Interest	230	223	248	135
TOTAL RESOURCES	3,276	2,921	3,070	3,004
CASH FLOW STATEMENT	2011A	2012A	2013E	2014F
Profit before tax	393.2	255.1	278.1	264.6
-Depreciation	190.9	263.1	316.6	284.1
<i>-Adjustments</i>	<i>164.0</i>	<i>107.1</i>	<i>-61.5</i>	<i>37.0</i>
+/- Working capital	-331.2	-347.1	-6.8	-133.2
Net Operating CFs	416.8	278.1	526.3	452.6
+/- Fixed Asset	-481.3	-106.6	-105.7	-247.2
+/- Deposit, equity investment	-164.2	20.2	16.1	-40.0
Interest, dividend, cash profit received	33.2	45.8	28.1	27.0
Net Investing CFs	-612.2	-40.6	-61.5	-260.2
+/- Capital	265.0	0.0	10.7	0.0
+/- Debt	249.8	-205.0	-238.8	19.5
Dividend paid	-83.1	-175.8	-86.0	-246.9
Net Financing CFs	431.7	-380.7	-314.1	-227.3
+/- cash & equivalents	236.3	-143.2	150.8	-34.9
Beginning cash & equivalents	350.0	586.3	443.0	593.8
Impact of exchange rate	0.0	0.0	0.0	0.0
Ending cash & equivalents	586.3	443.0	593.8	558.8

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 which 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 / Return Potential	BUY	ACCUMULATE	NEUTRAL	REDUCE	SELL
Intermediate- term (up to 6 months)	>20%	10% to 20%	-5% to 10%	-15% to - 5%	<-15%
Long-term (over 6 months)	>30%	15% to 30%	-10% to 15%	-15% to -10%	<-15%

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Network

Headquarter

Address: Floor 1-2-3-4, Viet Dragon Tower, 141 Nguyen Du, Ben Thanh Ward, Dist.1, Tp.HCM

Phone: 84.8 6299 2006 Fax: 84.8 6291 7986

Website: www.vdsc.com.vn

Ha Noi Branch

2C Thai Phien – Hai Ba Trung District
– Ha Noi

Nha Trang Branch

50Bis Yersin - Nha Trang

Can Tho Branch

08 Phan Dinh Phung –Cần Thơ

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