SOUTHERN HYDROPOWER JSC (SHP – HSX)

A Long-term Growth Story

Particulars (VND bn)	Q1-FY17	Q4-FY16	+/- qoq	Q1-FY16	+/- yoy
Net revenue	76.5	171.7	-55%	36.1	112%
PAT	-12.1	53.3	n/a	-54.3	n/a
EBIT	10.8	83.8	-87%	-23.1	n/a
EBIT margin	14%	49%	-3469bps	n/a	n/a

Sources: SHP, RongViet Research

The Strong Recovery in Q1 2017. La Nina effect with unseasonal rain in the first quarter was the key for SHP's performance recovery. The total output increased by 130% YoY while the average selling price was almost the same as Q1 2016, resulted in net revenue of VND76.5 billion (+122% YoY). Although this revenue is still not enough to cover production costs and interest expense, SHP has eliminated its loss in Q1 2017 to VND12 billion (reduced from 54 billion loss in Q1 2016).

For hydropower companies in the Central Highland like SHP, Q1 is in the middle of the dry season so the production output is often lowest in the year. Therefore, we still regard the lower loss in Q1 2017 as a positive recovery of SHP.

This Year May Have the Best First-Half Since Da M'Bri Plant Came Online, Making 2017 Outlook More Interesting

We estimate that production output in 1H2017 is 237 million kWh, corresponding to the expected revenue and PNAT of VND226 billion and VND23 billion respectively. This is also the highest revenue that SHP ever achieved in the first 6 months. Compared to the loss of VND53 billion in 1H2016, this NPAT is a significant improvement in business result of SHP.

Moreover, with our optimistic view on hydrological and market conditions in 2H2017, we forecast total production output this year at over 675 million kWh (+251% YoY) and revenue of VND643 billion (+25% YoY). Therefore, the NPAT in 2017 could reach VND196 billion (+100% YoY), corresponding to EPS of VND2,081.

Valuation and Recommendation: *At the closing price on 10/07/2017, SHP is trading at trailing 12M P/E of 15.6x, which is not attractive for a hydropower company being in a year of favorable weather. However, due to its potential capacity expansion in the intermediate-term and extraordinary growth of profit in 2017, we expect P/E of SHP to stay at 12x in 2017.*

Compared to our most recent recommendation on SHP in the ***Strategic Report*** *published on* ***March 15, 2017****, the business result of the company in the first half was better than our expectation and the outlook of hydrological condition in the second half is better as well. Moreover, the long-term prospect of the company is much brighter thanks to the new solar project. Therefore, we revise up our target price for SHP to* ***VND25,400/share****, which is 6****%*** *higher than the closing price on July 10, 2017 and recommend* ***NEUTRAL*** *on the stock in the* ***INTERMEDIATE-TERM****.*

In the long term, we still maintain our positive view on the company and believe that SHP stock would have considerable profitability at low risk. Therefore, investor can consider holding SHP in the long term.

NEUTRAL

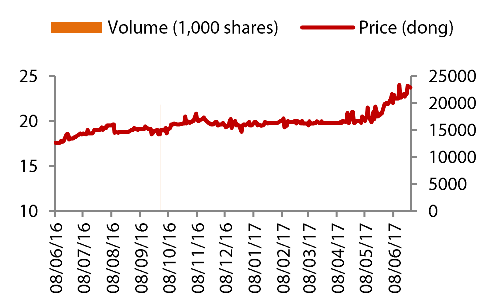
CMP (VND)	24,100
Target Price (VND)	25,400
Investment Period	**Intermediate-term**

Stock Info

Sector	Electricity
Market Cap (VND B)	1,865
Current Shares O/S	94
Beta	0.44
Free float (%)	40
52 week High	24,000
52 week Low	18,224
Avg. Daily Volume (20 sessions)	8,714

	FY2016	Current
EPS	1,043	1,444
EPS Growth	-40%	38%
Diluted EPS	1,043	1,444
P/E	19.1	16.5
P/B	1.6	2.3
EV/EBITDA	8.0	4.7
Cash dividend	8%	6%
ROE	8%	12%

Price performance



Major Shareholders (%)

EVN SPC	23.0
EVN CPC	23.0
REE Corporation	19.0

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Exhibit 1: Q1FY2017 Results

Particulars (VND bn)	Q1-FY17	Q4-FY16	+/- (qoq)	Q1-FY16	+/- (yoy)
Net Revenues	76	172	-55%	36	112%
Gross profits	16	91	-83%	-18	n/a
SG&AC	5	8	-37%	5	0%
Operating Income	-12	55	n/a	-54	n/a
EBITDA	57	130	-57%	22	163%
EBIT	11	84	-87%	-23	n/a
Financial expenses	23	29	-21%	31	-27%
- Interest Expenses	23	29	-21%	31	-27%
Dep. and amortization	46	47	-2%	45	3%
PBT	-12	55	n/a	-54	n/a
PAT	-12	53	n/a	-54	n/a

Sources: SHP, RongViet Research

Exhibit 2: 1QFY2017 Performance Analysis

Particulars	Q1-FY17	Q4-FY16	+/- (qoq)	Q1-FY16	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	20.4%	53.2%	-3283bps	-50.6%	7106bps
EBITDA Margin	74.0%	76.0%	-194bps	59.6%	1439bps
EBIT Margin	14.1%	48.8%	-3469bps	-64.0%	7815bps
Net Margin	-15.9%	31.1%	-4695bps	-150.3%	13447bps
Turnover *(x)					
-Inventories	31.8	30.3	1.5	100.3	-68.5
-Receivables	3.2	4.5	-1.3	1.9	1.3
-Payables	5.6	6.6	-1.0	2.9	2.7
Leverage (%)					
Total Debt/ Equity	120%	125%	-4bps	135%	-15bps

Sources: SHP, RongViet Research

Exhibit 3: Q2FY2017 Performance Forecast

Particulars (VND bn)	Q2-FY17	+/- qoq	+/- yoy
Revenue	142.4	91%	305%
Gross profit	67.3	328%	n/a
EBIT	61.4	462%	n/a
NPAT	35.8	n/a	n/a

Sources: SHP, RongViet Research

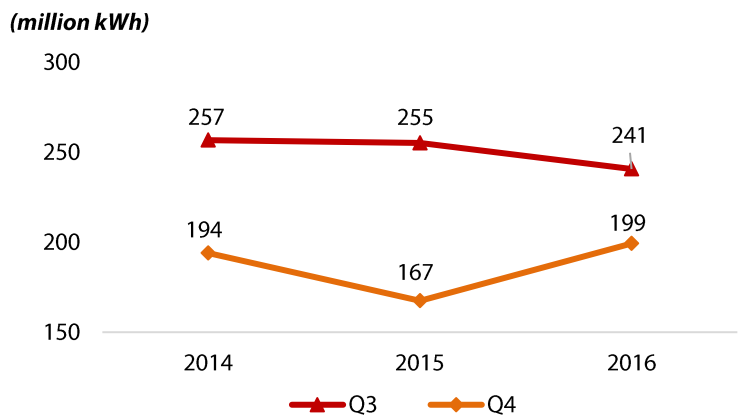
Brief Updates:

The rainy season in the Central Highland this year started early but may end early as well

The most recent weather forecast article of Vietnam National Centre for Hydrometeorological Forecasting (NCHMF) shows that the rainy season in Central Highland has already started in early May. However, NCHMF also predicted that rainy season there would end early in this October. Therefore, they forecast the rainfall level in the Central Highland to be 30% above multi-year average in Q3 2017 and 30% below multi-year average Q4 2017.

Regarding SHP, as Q3 usually contributes the highest share in total production output of the year, we believe that the overall the electricity output of the company in 2H 2017 would be no less than the average level (about 238 million kWh). This is also an important reason for us to expect the total output of SHP in 2017 at 640 million kWh (+15% YoY).

Figure 1: The electricity output of SHP in Q3 and Q4



Sources: SHP, RongViet Research

Dividend for FY2016 decreases slightly due to poor business result in 2016

Although its NPAT declined by 40% in 2016 and only reached 61% of 2016 plan, the AGM 2017 of SHP still approved dividend payment for FY2016 at VND1,500/share, which is slightly lower than in AGM 2016 plan (VND1,600/share). This is a clear evidence showing the stability in dividend policy of SHP even in the year with unfavorable weather condition. Therefore, we can expect higher dividend level in the next years when the interest expense decline, enhancing profit of SHP.

Major repair work: Get ready for the rainy season

In the first quarter of this year, SHP has completed all the major repair work for the entire 2017, including three turbines of Da Siat and Da Dang 2 plants. Thanks to their skilled engineering team and determination of the management team to ensure the continuous operation, the company finished its major repair work in each turbine within only 20 – 25 days to, much earlier than the standardized time required by EVN (40 – 45 days). This fast progress was the reason why the electricity output of Da Siat and Da Dang 2 plants remained high even in the months that had major repair.

Besides, during this major repair, the company has replaced the turbine blades in two turbines of Da Dang 2 plant with the new ones using technology that enhanced total capacity of this plant by 1.5 MW to 35.5 MW. Therefore, the total capacity of SHP now increases to 124 MW. The expense for this replacement was VND13 billion, which would be capitalized and amortized in three years.

Solar power project in Da Dang 2 plant area

The recent 2017 AGM of SHP has approved the BOD's plan to invest in a new solar project in the area of Da Dang 2 plant. According to the company, Da Dang 2 plant already has clean available land bank to install solar panel and available connection to the national power transmission grid, which would help them save some related expenses. Moreover, according to data from National Aeronautics and Space Administration (NASA), the potential solar radiation in Vietnam's territory ranges from 3.0 – 5.6 kWh/m2.day while in Da Dang 2 plant area is around 5.09 kWh/m2.day. Therefore, Da Dang 2 plant area has strong potential to develop solar power. The company is also making a detailed project plan to ask for approval to add this project to Lam Dong's Power Development Plan and set the license. SHP expects to start implementation of this project in mid-2018.

From data provided by SHP, we estimate that the investment cost per MW of this project is around VND14 billion to VND20 billion. Comparing to Cu Jut solar project that Central Hydropower JSC (HSX - CHP) is about to implement with average investment cost of VND25 billion/MW, Da Dang 2 project has relatively cheaper investment cost. Since the purchase price of solar electricity is almost fixed at 9.35 US Cent/kWh, the saving in investment expense would result in positive impact on profitability of the project. Besides, as solar power is still new to investors in Vietnam, SHP also shows conservative attitude toward selecting technology for the project to ensure long-term efficiency.

Regarding short-term prospect of Da Dang 2 project, since SHP expects to finance it largely by debt (with 70 – 80% of its total investment capital), they only expect low profitability in the first years due to high interest expense. The improvement in profitability would mainly come from the decline in amount of debt after each year, leading to lower interest expense. Therefore, we expect that Da Dang 2 solar project would drive the prospect of SHP in the long-term.

Figure 2: Summary information about Da Dang 2 solar project

Location: Duc Trong district, Lam Dong province			
Capacity (MW)	20 – 30	Investment capital (VND bn)	400
Expected debt financing ratio	70 - 80%	Average investment capital (VND bn/MW)	14 - 20

Sources: CHP, RongViet Research

VND billion

INCOME STATEMENT	FY2015	FY2016	FY2017E	FY2018F
Revenue	594.7	513.0	643.2	605.2
COGS	257.5	274.3	294.5	285.4
Gross profit	**337.2**	**238.7**	**348.7**	**319.8**
Selling Expense	0.0	0.0	0.0	0.0
G&A Expense	32.4	22.3	47.3	45.8
Finance Income	0.9	0.9	0.5	0.9
Finance Expense	131.8	115.7	98.1	93.7
Other profits	-4.4	0.5	0.0	0.0
PBT	**169.5**	**102.2**	**203.8**	**181.1**
Prov. of Tax	4.9	4.1	8.2	9.1
Minority's Interest	0.0	0.0	0.0	0.0
PAT to Equity Shareholder	**164.6**	**98.1**	**195.7**	**172.1**
EBIT	304.8	216.4	301.4	273.9
EBITDA	483.1	396.9	485.6	458.2

%

FINANCIAL RATIO	FY2015	FY2016	FY2017E	FY2018F
Growth (%)				
Revenue	0	-14	25	-6
Operating Income	-12	-29	39	-9
EBITDA	-3	-18	22	-6
PAT	-25	-40	100	-12
Total Assets	-9	-9	-3	-6
Equity	1	-5	5	2
Profitability (%)				
Gross profit/Revenue	57	47	54	53
Operating profit/ Revenue	51	42	47	45
EBITDA/ Revenue	81	77	75	76
Net margin	28	19	30	28
ROAA	6	4	8	7
ROAE	13	8	16	14
Efficiency (x)				
Receivable Turnover	0.3	0.2	0.2	0.3
Inventory Turnover	0.0	0.0	0.0	0.0
Payable Turnover	1.2	0.4	0.4	0.4
Liquidity (x)				
Current	1.0	0.7	1.0	1.1
Quick	0.9	0.7	1.0	1.1
Solvency (%)				
Total Debt/Equity	1.2	1.2	1.0	0.8
Current Debt/Equity	0.1	0.1	0.1	0.1
Long-term Debt/ Equity	1.1	1.0	0.8	0.7

VND billion

BALANCE SHEET	FY2015	FY2016	FY2017E	FY2018F
Cash and short-term investment	162	52	115	166
Receivables	119	127	160	150
Inventories	3	14	2	2
Other current assets	20	6	6	6
Total Current Asset	**304**	**199**	**283**	**325**
Fixed Assets	2604	2443	2273	2090
Construction in Progress	3	3	3	3
Long-term Investment	0	0	0	0
Other long-term assets	2	1	1	1
Long-term Asset	**2,609**	**2,447**	**2,278**	**2,095**
Total Asset	**2,913**	**2,646**	**2,561**	**2,419**
Payables	131	107	128	124
Current Debt	184	160	160	167
Long-term Debt	1,360	1,200	1,040	872
Other long-term liabilities	1	1	2	3
Total Liability	**1,676**	**1,468**	**1,330**	**1,166**
Owner's Equity	**1,237**	**1,177**	**1,232**	**1,253**
Capital	937	937	937	937
Retained Earnings	300	240	295	316
Funds & Reverses	0	0	0	0
Others	**0**	**0**	**0**	**0**
Total Equity	**1,237**	**1,177**	**1,232**	**1,253**
Minority's Interest	0	0	0	0
TOTAL RESOURCES	**2,913**	**2,646**	**2,561**	**2,419**

VALUATION RATIO	FY2015	FY2016	FY2017E	FY2018F
EPS (dong)	1,752	1,043	2,081	1,830
P/E (x)	10.0	19.1	11.4	12.9
BV (dong)	13,200	12,563	13,144	13,374
P/B (x)	1.3	1.6	1.9	1.8
DPS (dong/cp)	1,600	1,500	1,600	1,800
Dividend yield (%)	8.6	7.5	6.6	7.4

VALUATION MODEL	*Price*	*Weight*	*Average*
EV/EBITDA	24,531	70%	17,172
FCFE	27,715	30%	8,314
Target price (dong/share)			**25,400**

VALUATION HISTORY	*Price*	*Recommendation*	*Period*
15/03/2017	22,800	Accumulate	Intermediate -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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