Searefico JSC (SRF – HSX)

Making full use of industry growth

Particular (VND bn)	Q2-FY16	Q1-FY16	*+/- qoq*	Q2-FY15	*+/- yoy*
Revenue	305.3	156.8	95%	297.4	3%
NPAT	18.3	7.0	162%	16.0	14%
EBIT	26.6	12.3	115%	22.9	16%
EBIT margin	8.7%	7.9%	84bps	7.7%	103bps

Source: RongViet Research

- **Being among the leader firms in the M&E industry**
- **Industrial refrigeration: Unrivaled**
- **Sound financials, prominent efficiency and sufficient cash holding**

Outlook and Valuation:

Searefico JSC (SRF-HSX) is recognised among the top firms at both of its operating businesses being Mechanical & Engineering (M&E) and Industrial Refrigeration. The company's growth, therefore can benefit from both the Construction and Food & Beverage Process market growth. Sustainable backlog and new contract amounts project 2016 to be a remarkable year for SRF's M&E business. Regarding the IR business, performing overseas orders for its traditional IQF systems and exploiting new segments in the domestic IR market have demonstrated SRF's market leading position. Beside a concentrating and stable core operating activities, SRF has a solid financial situation with sound working capital and minimum long-term debt for a construction firm.

Under FCFF and P/E valuation methods, the fair price for SRF is around VND **32,100**, **20.2%** upside to the closing price on August 3rd 2016. Thus, we recommend **ACCUMULATING** SRF in **LONG-TERM**. The consistent cash dividend policy can also be a reason to consider SRF.

SRF's major risks involve the construction demand's seasonality. At the moment, the current construction activities in the domestic market has been growing considerably owing to the real estate market, yet might not sustain strong growth in the coming years.

Key financials

Y/E Dec (VND bn)	FY2014	FY2015	3M2016	FY2016E	FY2017F
Net Revenues	837.3	1,044.3	462.2	1,503.8	1,684.2
% chg	48.0%	24.7%	20.1%	44.0%	12.0%
PAT	65.4	64.6	25.3	83.7	93.6
% chg	81.5%	-1.2%	45.0%	29.4%	11.9%
EBIT margin (%)	7.8%	6.2%	5.5%	5.6%	5.6%
ROA (%)	7.9%	6.4%		7.1%	7.3%
ROE (%)	17.4%	16.1%		19.4%	20.0%
EPS (VND)	2,659	2,423		3,433	3,841
Adjusted EPS (VND)	2,659	2,423		3,433	3,841
Book value (VND)	15,859	16,989		18,172	19,780
Cash dividend (VND)	1,800	1,200		2,000	2,000
P/E (x)	9.7	10.6		8.1	7.3
P/BV (x)	1.6	1.5		1.5	1.4

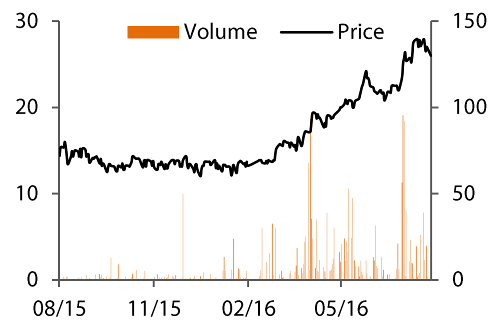
*Sources: SRF, RongViet Research estimated. * Accounted for welfare provision expense and computed based on total share number on 3rd August 2016.*

ACCUMULATE

CMP (VND)	26,700
Target Price (VND)	32,100
Investment Period	**Long-term**

Stock Info

Sector	Construction & Materials
Market Cap (VND bn)	633.4
Current Shares O/S	24,361,876
Beta	0.08
Free float (%)	39.6
52 weeks High	27,900
52 weeks Low	12,035
Avg. Daily Volume (in 20 sessions)	16,360



Performance (%)

	3M	1Y	3Y
SRF	40	85	294
Construction & Materials	14	36	N/A
VN30 Index	3	-3	13
VN Index	5	5	27

Major Shareholders (%)

Taisei Oncho JSC	24.93
Sao Phuong Nam Corp	24.20
Seaprodex	12.79
Foreigner Investor Room (%)	20.57

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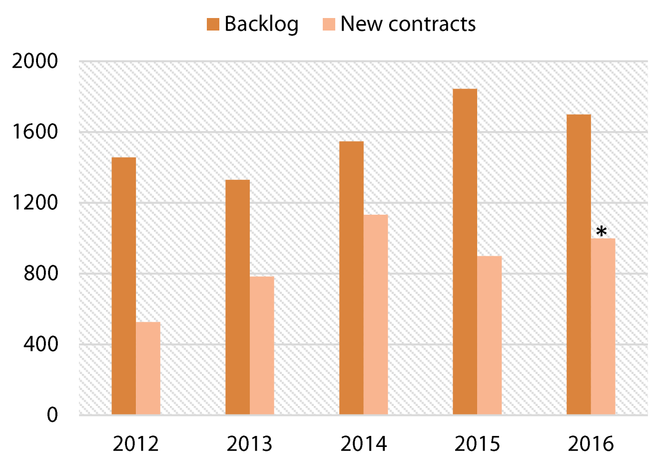
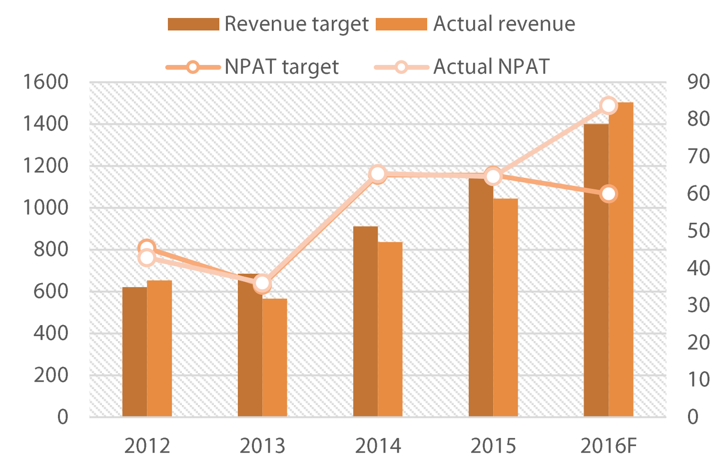
Figure 1: Backlog and New contracts



Sources: SRF, RongViet Research.
**New contracts in 6M2016*

Figure 2: Revenue and NPAT targets and actuals



Sources: SRF, RongViet Research

Being among the leader firms in the M&E industry

Moving closer to the leading position

Along with REE, SRF is a familiar name in the short-list for massive project owners including VinGroup and Sun Group. SRF's capacity is also illustrated by the variety in the project segments in its portfolio consisting of Industrial, Commercial centres, Office, Apartment blocks and Resorts.

Having a well-built network, REE has been the top M&E contractor in the domestic market. However, SRF has been moving in a greater pace. While REE's M&E revenue CAGR was around 13% in the 2011-2015 period, that of SRF was 17%. SRF's M&E revenue was equal to 47% that of REE in 2012, while the estimated figure for 2016 is nearly 86%. Therefore, it can be said that SRF has narrowed the gap between itself and the market leader by a considerable amount.

Whereas REE's M&E business is displaying a slower growth rate due to a stricter project selection process, SRF has been increasing both revenue and new contract amounts for its M&E business. With the second largest backlog after REE's among domestic M&E contractors, SRF is regarded as one of those who benefit the most from the current construction demand growth.

Table 1: Major projects

Project	Owners	Completion time
L2 Vinhomes Central Park	VinGroup	2016
Pearl Plaza	SSG Group	2015
Gateway Thao Dien	Hamon, Sơn Kim Land	2015
Garden Gate	Novaland	2015
Habitat Binh Duong	VSIP-Sembcorp Gateway MC Development Asia	2015
Hilton Hotel Da Nang	Bach Dang Hotel Trade & Service JSC	2015
Vincom Mega Mall Thao Dien	VinGroup	2015
Vista Verde	Capital Land	2015
French Village Ba Na	Ba Na Cable Service JSC	2015

Sources: SRF, RongViet Research

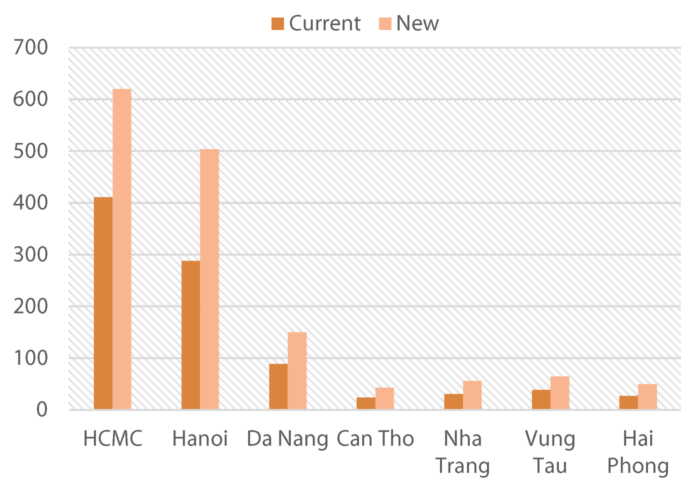
Continuing favour from the real estate market and construction activities

SRF has built a capable technical team which is expanding as it is supported by a strategic partner* of the same industry who has experience, thus M&E business's efficiency can be improved. Noticeably, SRF is capable of producing most parts of the central air conditioning system, therefore gains control in input costs, which few M&E contractors are capable of.

*Taisei Oncho is a Japanese contractor in the business of civil construction whose 2015 revenue exceeded USD 15 bn. Subsequent to taking 25% ownership in SRF via the private placement in 2013, Taisei Oncho supported the company in terms of technical training (air conditioner setup and plumbing) as well as access to prominent projects' procurements. As a result, SRF has been seen to undertake large civil projects including Viettel Trade Centre, Pearl Plaza and Liberty Riverside.

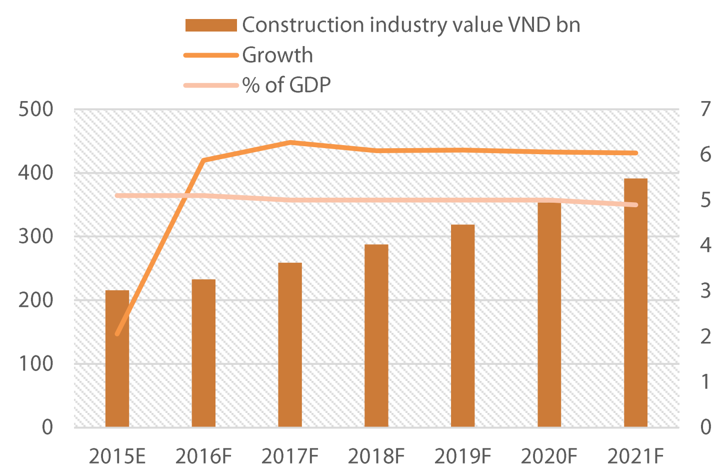
M&E's considerable growth has partly benefited from the industry factor. That the real estate market has just started its expansion phase and office renting demand's strong growth are in favour of construction contractors' backlog.

Figure 3: Current and new projects in major cities



Source: CBRE, RongViet Research compiled

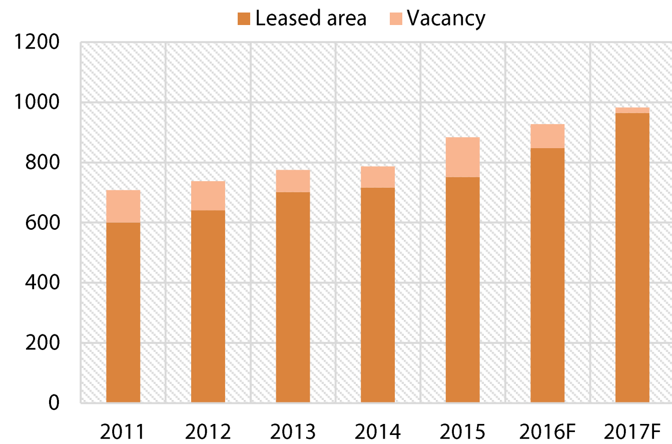
Figure 4: Construction industry value forecast



Source: BMI, RongViet Research compiled

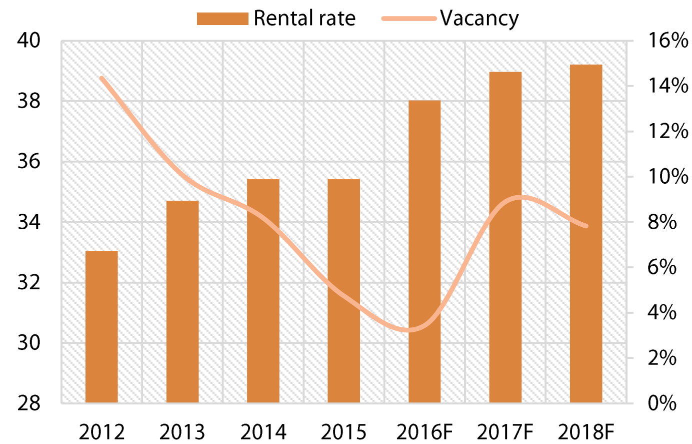
The real estate market's recovery during the economy's expansionary phase is in favour of construction companies, especially M&E contractors owing to the construction demand potential in the next 3-4 years. While the cash flows for an apartment block project greatly depends on the owner's sales ability, an M&E contractor when carrying out a commercial and office project is likely to have higher cash flow stability. As mentioned above, a majority of SRF's projects belong in the commercial, office towers or complex, which is considered less risky than the residential segment. Thus, SRF is able to improve its gross margin as well as minimise an existing segment risk.

Figure 5: Office supply in HCMC



Source: CBRE, RongViet Research compiled

Figure 6: Office renting market in HCMC

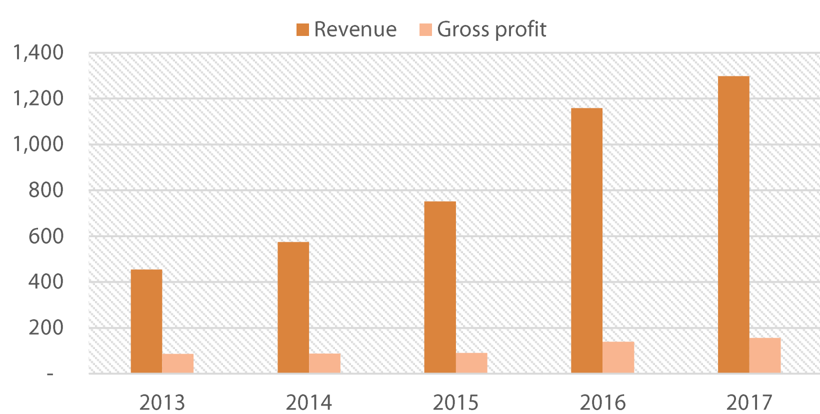


Source: CBRE, RongViet Research compiled

Observing the office renting market's supply and vacancy rates in major cities, RongViet Research predicts that the demand for office and commercial lease is increasing considerably, creating sustainable new jobs for construction companies, particularly M&E contractors.

Forecasts regarding the real estate market, construction demand and M&E activities have been expecting a strong growth for the upcoming 3-year period. 2016-2018 Construction value is projected to exceed 6% per annum in real growth while maintaining 5% proportion in GDP and might reach VND 288 trillion in value in 2018. That the industry growth is equivalent to the GDP growth can provide opportunities for M&E's market leaders to take advantage of via large-scaled and complicated projects.

Figure 7: M&E Revenue and Gross profit forecasts (VND bn)



Source: SRF, RongViet Research compiled

SRF has recently established its office in Phu Quoc, where SRF has been monitoring several projects amount up to VND 300bn in value. Moreover, numerous clients of SRF's have been carrying out various massive real estate projects on the island. Therefore, the new office establishment is not only for the sake of monitoring activities on the sites that are located further from the head quarter but also a strategic move, as the island's tourism and commercial potential has been attracting massive capital flows.

RongViet Research expects Searefico to exceed the industry average growth based on the mentioned points. The company's gross margin is also forecasted to incline in the long term, as SRF's reforming progress in project monitor in order to suits its decentralised working site locations as SRF has current projects in the central and southern region of Vietnam, including Phu Quoc. In short and intermediate term, looking at the VND 1,000 bn backlog and another VND 1,000 bn new contract value (at the end of Q2/2016), it can be predicted that SRF is going to realise a substantial revenue growth in 2016 and 2017.

Industrial refrigeration: Unrivaled

SRF is in the business of industrial freezing equipment design, assembly and setup. SRF mainly works with F&B and medicine producers and distributors, especially aquatic and seafood factories. SRF's products include:

- ✓ Freezing systems, processing belts, freezing storage in food and beverage (F&B) factories
- ✓ IQF systems
- ✓ Air blast freezers, Contact freezers
- ✓ Flake ice machines
- ✓ Insulated PU panels
- ✓ Steam cooking & cooling systems
- ✓ Food processing belts
- ✓ Stainless steel evaporative condensers
- ✓ Pressure vessels
- ✓ Factory management systems.

Figure 8: IQF

Source: SRF, RongViet Research compiled

Figure 9: Steam cooking & cooling systems

Source: SRF, RongViet Research compiled

Figure 10: Contact freezers

Source: SRF, RongViet Research compiled

Figure 11: Freezing systems

Source: SRF, RongViet Research compiled

Having over 30-year experience, SRF is considered as the most prominent domestic firm in the potential industry who has powers over both clients and suppliers

Firstly, SRF can attain a profitable bid price thanks to its consultation, design and customisation capability which can meet clients' demand. Secondly, the company's capability of producing numerous parts of the freezer system (including freezer belts, covers and panels) is another factor that inclines its gross margin as well as positions SRF above other IR contractors who mostly assembly and set up the systems. Its industrial refrigeration business's gross margin shows the unmatched power in the market.

SRF used to provide mainly aquatic and seafood processing systems, but recently has expanded to other potential segments including processing belts and freezer storage for food, beverage and medicine. Large clients include Coca-Cola, Vinamilk and CP Vietnam.

Figure 12: Vinamilk's milk plant

Source: Bloomberg, RongViet Research compiled

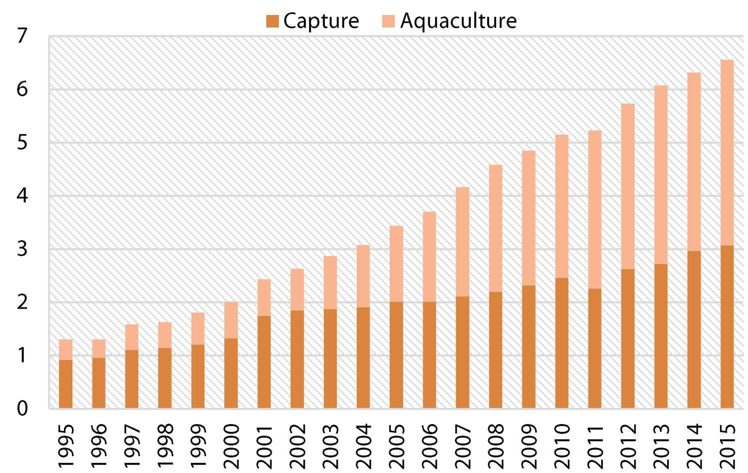
Figure 13: Coca-Cola factory (Cambodia)

Source:, SRF, RongViet Research compiled

SRF has started boosting exports and expanding to new segments

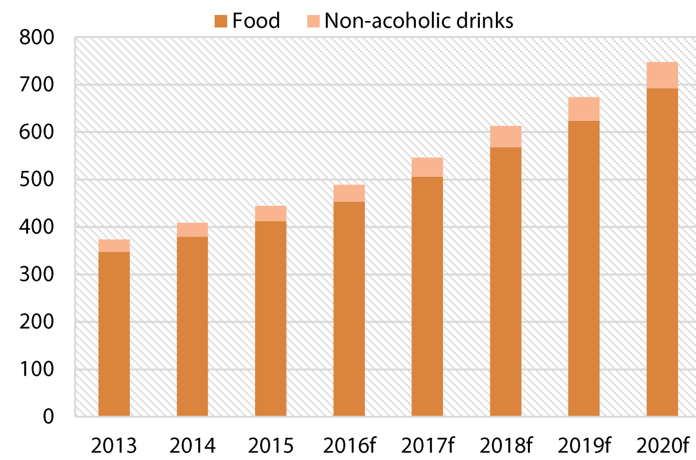
2009-2012 was the peak of investment demand in the seafood and aquatic food export industry in the domestic market, as the demand has recently stagnated, thus making SRF expanding its operating industry to sustain growth. India has just newly started the seafood exporting trend, as observed in the 6.3% CAGR in seafood and aquatic food export in the 2009-2015 period. Therefore, the refrigeration system demand appears to be potential, as SRF has just approached the market in 2014 and had exported 2 systems to India in 2015, recognising around USD 2 million revenue (VND 44 bn). In Q1/2016 only, SRF has received 2 new orders, totaling VND 40 bn, which equals to 2015 revenue from the Indian market, showing that exporting can be potential for SRF's IR business.

Figure 14: Vietnam aquatic food and seafood production



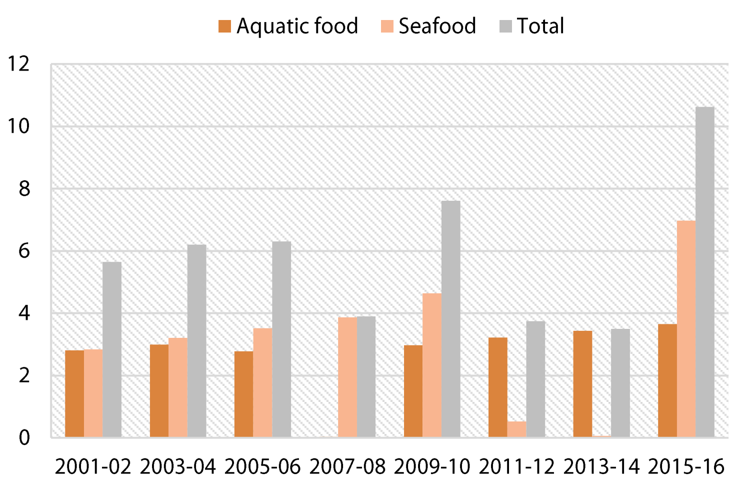
Source: VASEP, RongViet Research compiled

Figure 15: F&B industry value (VND bn)



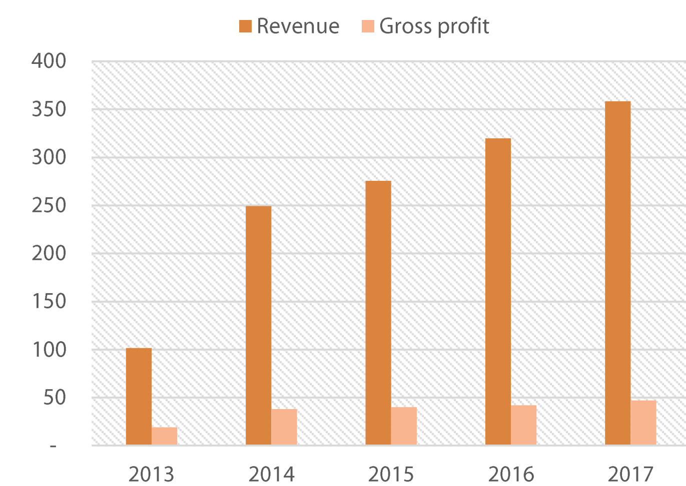
Source: BMI, RongViet Research compiled

Figure 16: India seafood and aquatic food production (million tons)



Source: MoEFCC, RongViet Research compiled

Figure 17: IR Revenue and Gross profit forecasts (VND bn)



Source: RongViet Research compiled

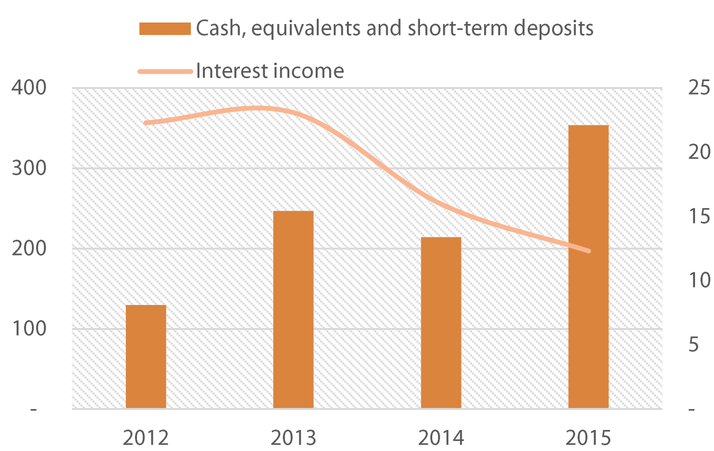
IR is a supporting industry that possesses great potential that the company can take advantage of. Used to be a company that assembles and set up shrimp freezing systems, SRF has now been able to provide freezing storage and processing belts for other F&B products, including milk, beer and soft drink factories and medicine preservation storage. The domestic demand for F&B products in a market of increasing population and growing average income is encouraging the demand for F&B storage, which SRF is focusing on.

Sound financials, prominent efficiency and sufficient cash holding

SRF's growth can be seen in its Revenue and NPAT CAGRs, which are 15% and 7.8% p.a. respectively during 2010-2015. In particular, during the trough phase of the real estate market (2012-2014), doubtful and bad debts were inconsiderable. In fact, provision for doubtful debts was also modest, around VND 28 bn during 2012-2014 which was reversed in 2015.

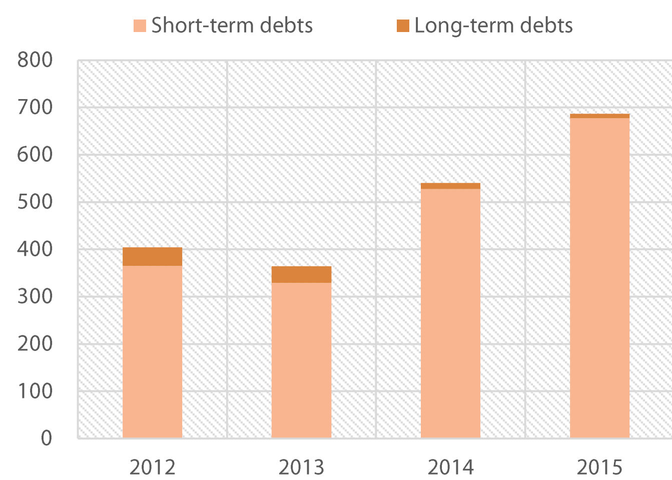
SRF has insignificant amount of long-term debts, as most borrowings are short-term loans for working capital. In the IR business, Tan Tao plant has enough capacity for the company to increase the production scale without further mass investment. Thus, most short-term debts are utilised in the M&E business with advantageous interest rate at around 4.65% p.a.

Figure 18: Cash and interest income



Source: SRF, RongViet Research compiled

Figure 19: Capital structure



Source: SRF, RongViet Research compiled

Prepayments from clients (around 10-20% of contract value) and low-cost short-term funding enable SRF to maintain safe liquidity ratios. SRF also has the pattern of holding a large amount of cash, cash equivalent and short-term bank deposits, which amounts up to VND 310 bn at the end of Q2/2016.

Table 2: Financial ratios

Particular (VND bn)	FY2014	FY2015	FY2016E	FY2017F
Capital structure (%)				
Total liabilities / Total assets	58,3	62,4	64,1	63,4
Total liabilities / Total equity	139,8	165,8	178,2	173,3
Short-term liabilities / Equity	64,5	85,5	67,3	62,3
Long-term liabilities / Equity	1,7	0,6	0,6	0,7
Working capital turnover				
Inventory turnover	3,9	5,1	6,3	5,4
Receivables turnover	3,5	3,1	3,8	3,8
Payables turnover	2,8	3,0	3,2	2,9
Cash conversion cycle (net operating cycle)	67,0	69,3	41,5	37,5
Solvency				
Interest coverage	5,1	6,1	8,1	6,6
Current ratio	1,6	1,9	1,4	1,3
EBITDA/Interest expense	4,2	5,3	7,4	6,1
DuPont analysis				
Earning before tax / Revenue	9,9	9,0	7,7	7,6
Revenue/Total assets	1,0	1,0	1,3	1,3
(A/E) x (1-t)	2,0	2,1	2,2	2,2
ROE = {(1) x (2) - (3)} x (4)	17,4	16,1	19,4	20,0

Source: SRF, RongViet Research

Table 3: Peer comparison

2015	SRF	REE
Total liabilities / Total equity (%)	165,8	46,2
Short-term liabilities / Equity (%)	85,5	6,8
Long-term liabilities / Equity (%)	0,6	8,9
Receivables turnover	3,5	2,2
Payables turnover	2,8	1,5
Cash conversion cycle (net operating cycle) (days)	67,0	42,8

Source: SRF, REE, RongViet Research

SRF, compared to the construction industry average, is presenting a prevailing efficiency. The company is capable of tying up creditors and debtors' capital and thus improving its cash conversion cycle, which illustrates its ability to control and make use of the cash flows.

Consistent cash dividend is a plus as SRF maintained a cash dividend payment of at least VND 1,000 per share since listed. That the company has committed a minimum cash dividend policy of VND 1,500 per share (equivalent to 5.6% dividend yield) can be considered as adequate for long-term holding.

Valuation

In order to compute SRF's fair price, we use a discounted cash flow and a relative evaluation method at equal weights. Regarding FCFF, 2016-2020 discount rate is 10.72% and that of 2020-on is 11.19%. FCFF's long-term growth rate is estimated at 4.55%.

P/E method takes P/E trailing from listed Materials & Construction, which is 13.14x. After adjusting for the M&E and IR industries, we use P/E 10x to project the company's value.

Accordingly, the fair price for SRF is VND **32.100 per share**, upside **20.2%** comparing to the closing price on August 3rd 2016. Thus, we recommend **ACCUMULATING** SRF in **LONG-TERM**.

Table 4: Valuation matrix

Method	Price	Weight	Weighted average
FCFF	29,979	50%	14,990
P/E	34,328	50%	17,164
Fair price		**100%**	**32,100**

Source: RongViet Research

VND Billion

INCOME STATEMENT	**2014**	**2015**	**2016F**	**2017F**
Revenue	837.3	1,044.3	1,503.8	1,684.2
COGS	709.7	907.2	1,306.4	1,465.3
Gross profit	**127.6**	**137.1**	**197.4**	**218.9**
Selling Expense	1.8	0.0	0.1	0.1
G&A Expense	86.1	93.4	121.1	134.3
Finance Income	18.0	14.7	19.6	21.9
Finance Expense	12.9	16.0	15.6	14.0
Other profits	0.2	19.4	-0.4	-0.4
PBT	**72.9**	**79.3**	**102.6**	**114.8**
Prov. of Tax	7.5	14.7	19.0	21.2
Minority's Interest	0.0	0.0	0.0	0.0
PAT to Equity Shareholder	**65.4**	**64.6**	**83.7**	**93.6**
EBIT	**83.1**	**93.6**	**115.8**	**128.1**
EBITDA	76.0	86.4	130.9	144.9

FINANCIAL RATIO	**2014**	**2015**	**2016F**	**2017F**
Growth				
Revenue	48.0	24.7	44.0	12.0
Operating Income	9.4	9.9	74.8	11.0
EBITDA	47.4	13.7	51.5	10.6
EBIT	40.2	12.5	23.8	10.6
PAT	81.5	-1.2	29.4	11.9
Total Assets	27.1	18.8	13.0	7.0
Equity	6.1	7.1	8.0	8.9
Internal growth rate	14.2	10.1	8.1	9.6
Profitability				
Gross profit/Revenue	15.2	13.1	13.1	13.0
Operating profit/ Revenue	4.7	4.2	5.1	5.0
EBITDA/ Revenue	9.1	8.3	8.7	8.6
EBITDA/ Revenue	9.9	9.0	7.7	7.6
Net margin	7.8	6.2	5.6	5.6
ROAA	7.9	6.4	7.1	7.3
ROIC or RONA	20.8	22.8	26.3	26.9
ROAE	17.4	16.1	19.4	20.0
Efficiency				
Receivable Turnover	3.5	3.1	3.8	3.8
Inventory Turnover	3.9	5.1	6.3	5.4
Payable Turnover	2.8	3.0	3.2	2.9
Liquidity				
Current	1.4	1.3	1.3	1.3
Quick	1.1	1.1	1.0	1.0
Solvency				
Total Debt/Equity	139.8	165.8	178.2	173.3
Current Debt/Equity	64.5	85.5	67.3	62.3
Long-term Debt/ Equity	1.7	0.6	0.6	0.7

VND Billion

BALANCE SHEET	**2014**	**2015**	**2016F**	**2017F**
Cash and equivalents	214	168	324	318
Short-term investment	15	187	0	0
Receivables	304	377	421	472
Inventories	189	165	248	293
Other current assets	23	6	12	14
Total Current Asset	**746**	**903**	**1,005**	**1,097**
Tangible Fixed Assets	63	58	54	53
Intangible Fixed Assets	5	1	50	49
Construction in Progress	0	5	2	0
Investment Property	0	0	0	0
Long-term Investment	72	94	94	94
Other long-term assets	40	39	38	38
Long-term Asset	**181**	**197**	**238**	**234**
Total Asset	**927**	**1,101**	**1,244**	**1,330**
Payables	166	209	314	337
Other current liabilities	112	114	173	194
Current Debt	249	354	301	303
Long-term Debt	6	3	3	3
Other long-term liabilities	6	7	7	7
Total Liability	**540**	**687**	**797**	**844**
Owner's Equity	**387**	**414**	**443**	**482**
Capital	244	244	244	244
Retained Earnings	57	82	105	135
Funds & Reverses	43	46	53	61
Others	**0**	**0**	**4**	**5**
Total Equity	**387**	**414**	**447**	**487**
Minority's Interest	0	0	0	0
TOTAL RESOURCES	**927**	**1,101**	**1,244**	**1,330**

CASH FLOW STATEMENT	**2014**	**2015**	**2016F**	**2017F**
Profit before tax	72.9	79.3	102.6	114.8
-Depreciation	7.2	7.2	15.1	16.8
-Adjustments	*83.0*	*-43.1*	*24.1*	*9.3*
+/- Working capital	-164.5	-1.8	-15.7	-105.1
Net Operating CFs	**-1.4**	**41.6**	**126.2**	**35.8**
+/- Fixed Asset	-1.0	11.1	-57.7	-12.0
+/- Deposit, equity investment	-62.4	-181.3	6.0	3.9
Interest, dividend, cash profit	24.5	10.4	10.4	10.4
Net Investing CFs	**-39.4**	**-159.8**	**-41.3**	**2.3**
+/- Capital	0.0	0.0	0.0	0.0
+/- Debt	146.8	100.8	-70.1	2.7
Dividend paid & other	-71.6	-29.2	141.6	-46.8
Net Financing CFs	**75.2**	**71.6**	**71.5**	**-44.1**
+/- cash & equivalents	34.3	-46.6	156.3	-6.0
Beginning cash & equivalents	**246.7**	**214.2**	**167.7**	**324.1**
Impact of exchange rate	0.0	0.1	0.0	0.0
Ending cash & equivalents	**214.2**	**167.7**	**324.1**	**318.1**

DISCLAIMERS

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RATING GUIDANCE

Ratings / Return Potential	BUY	ACCUMULATE	NEUTRAL	REDUCE	SELL
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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