Vietnam Dairy Products JSC (HSX: VNM)

Growing Constantly

Unit: VND billion	*Q2-FY17*	*Q1-FY17*	*+/- qoq*	*Q2-FY16*	*+/- yoy*
Net revenue	13,348	12,049	10.8%	12,449	7.2%
PAT	2,922	2,935	-0.4%	2,815	3.8%
EBIT	3,248	3,282	-1.0%	3,182	2.1%
EBIT margin	24.3%	27.2%	-2.9%	25.6%	-1.2%

Source: VNM, RongViet Research

H1 2017 Performance: Fulfilling 60% of profit guidance. In the first six months, revenue posted VND25,397 billion, up 11.4% YoY thanks to the growing volume while selling price remained. The domestic market was the key top line's driver that enabled Vinamilk to gain market share in most of the main segments like liquid milk, yogurt and powdered milk. The selling expense to revenue ratio slightly decreased to 21.1% from 28.8%.

Despite 30% YoY higher in milk powder, gross margin in H1 2017 still remained at the highest level of all time: 48.7% due to purchasing the milk powder before a significant hike. Moreover, rising contributions from top gross profit products – yogurt and powdered milk – have kept gross margin stable.

H2 2017 Potential: Bottom line is forecasted to grow 16.5% YoY

Vinamilk has already concluded the milk powder price, which is 20% higher for the rest of 2017, compared to the previous period, so the gross margin in H2 2017 will likely be affected. According to VNM, the company could increase the selling price to a maximum of 3% to compensate the input cost. As a result, we estimate the gross margin in H2 2017 to adjust to 45.7% from 48.7% in H1 2017. Besides, the selling expense to revenue ratio is forecasted to slightly increase to 22%, compared to the H1 2017 ratio of 21.1%. With all these assumptions, we expect revenue and net profit to reach VND27,525 billion (+14.6% YoY) and VND5,102 billion (+16.5% YoY), respectively.

Valuation and Recommendation: *Vinamilk ended the first six months of 2017 with outstanding results when revenue and net profit resulted to growth of 11% YoY and 16% YoY, respectively. Thanks to the leading position, Vinamilk could take advantage of the favorable domestic market as well as potential foreign markets like China to sustain its growth in the future. Moreover, expanding the cow farms and upgrading the Mega Factory are key steps for Vinamilk to complete all the targets in AGM 2017.*

*Long-term prospects remain positive and Vinamilk still owns the competitive advantage. We revise the target price to **VND169,300**, which is higher than the previous one in the 2017 Strategy Report, owning to an increase in our forecast in 2017, 2018 net profit and it should also be noticed that we apply the 2018 EPS in the P/E valuation. With the total yield of **16.8%** in the next 12 months, compared to the closing price on 14/9/2017, we recommend **NEUTRAL** for VNM share.*

NEUTRAL

CMP (VND)	148,300
Target Price (VND)	169,300
Cash Dividend (VND)*	4,000

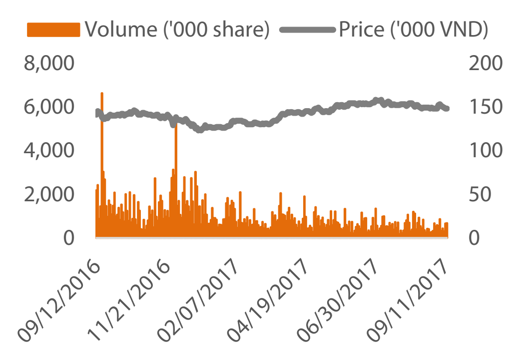
** Expected in the next 12 months*

Stock Info

Sector	F&B
Market Cap (VND B)	214,940
Current Shares O/S	1,451,453,429
Beta	0.57
Free float (%)	5.3
52 week High	157,600
52 week Low	122,500
Avg. Daily Volume (20 sessions)	483,220

	FY2016	Current
EPS	5,831	7,053
EPS Growth (%)	19.8	20.9
Adjusted EPS	5,799	7,053
P/E	21.5	21.0
P/B	8.1	8.7
EV/EBITDA	14.8	16.9
Cash dividend	6,000	6,000
ROE (%)	42	44

Price performance



Major Shareholders (%)

SCIC	39.3
F&N	18.7
Foreign ownership room (%)	44.7

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Exhibit 1: Q2/2017 Results

Particulars (VND billion)	Q2-FY17	Q1-FY17	+/- (qoq)	Q2-FY16	+/- (yoy)	H1-FY17	+/-(yoy)
Net revenue	13,348	12,049	10.8%	12,449	7.2%	25,398	11.5%
Gross profit	6,541	5,819	12.4%	6,044	8.2%	12,360	11.6%
SG&A	2,813	2,069	35.9%	2,359	19.2%	4,882	7.1%
Operating income	3,728	3,750	-0.6%	3,685	1.2%	7,478	15.9%
EBITDA	3,563	3,593	-0.8%	3,478	2.4%	18,870	15.2%
EBIT	3,248	3,282	-1.0%	3,182	2.1%	17,054	16.0%
Financial expenses	29	28	5.1%	16	78.5%	57	15.3%
- Interest Expenses	4	13	-70.0%	9	-53.8%	17	2.4%
Dep. and amortization	314	311	1.0%	296	6.1%	1,816	6.8%
Non-recurring items (*)							
Extraordinary items (*)							
PBT	3,444	3,476	-0.9%	3,362	2.4%	6,920	17.8%
PAT	2,922	2,935	-0.4%	2,815	3.8%	5,857	15.6%
(*) Adjusted PAT	2,922	2,935	-0.4%	2,815	3.8%	5,857	

Source: VNM, RongViet Research

Exhibit 2: Q2/2017 Performance Analysis

Particulars	Q2-FY17	Q1-FY17	+/- (qoq)	Q2-FY16	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	49.0%	48.3%	0.7%	48.5%	0.5%
EBITDA Margin	26.7%	29.8%	-3.1%	27.9%	-1.2%
EBIT Margin	24.3%	27.2%	-2.9%	25.6%	-1.2%
Net Margin	21.9%	24.4%	-2.5%	22.6%	-0.7%
Adjusted Net Margin	21.9%	24.4%	-2.5%	22.6%	-0.7%
Turnover *(x)					
-Inventories	6.7	5.9	0.8	6.1	0.6
-Receivables	13.5	14.9	-1.4	14.8	-1.3
-Payables	4.9	5.1	-0.2	6.0	-1.1
Leverage (%)					
Total Debt/ Equity	27.1%	22.1%	5.0%	27.5%	-0.4%

Source: VNM

Exhibit 3: Q3/2017 Performance Forecast

Particulars (VND billion)	H2 2017	+/- H1 2017	+/- H2 2016
Revenue	27,525	8.4%	14.6%
Gross profit	12,585	1.8%	19.1%
EBIT	5,883	-9.9%	20.2%
NPAT	5,102	-12.9%	16.6%

Source: VNM, RongViet Research

Updates:

Vinamilk targets to reach VND80,000 billion in revenue at the end of 2021, posting a CAGR of 11.9% The domestic market still plays the main role with a contribution of 76% of total sales. Specifically, VNM will try to maintain its domestic market growth rate by 10% per year by gaining market share from peers as well as taking advantage of the industry's overall growth rate when milk consumption per capita in Vietnam is still low – 17 liters per year, compared to 35 liters per year in Thailand and 45 liters per year in Singapore – according to a recent report from the Kantar World Panel.

Regarding the foreign market, Vinamilk plans to post a CAGR of 17.1% by penetrating new markets such as African countries or China, as the traditional markets in the Middle East are in difficult situation due to the political instability. Recently, Vinamilk has signed an MOU to export products to China, expected to begin in 2018 after adapting all product quality requirements. The initial exporting value may not contribute much to the overall result but this marks a big step for the company to bring its products to the market with the world's largest population.

According to Euromonitor, milk consumption in China will have experienced a 3% decline per year during the period 2017-2022, largely due to flavored milk drinks and shelf stable milk being related to some health problems. Instead, consumers have been shifting to premium milk products such as fresh milk, owing to its outstanding quality. As a result, Euromonitor predicts that fresh milk in China will maintain a stable CAGR of 4.9% in the next 5 years. With the strength of the "100% fresh milk" product (the leader in Vietnam among the fresh milk brands according to Nielsen), we believe that Vinamilk can fully utilize this trend to gradually penetrate this world's largest population country.

Upgrading Mega Factory to meet the future growth. To fulfill the growing demand in the future, Vinamilk is going to double the current capacity of Mega Factory from 400 million litres/year to 800 million litres/year when it is running at the full capacity. In addition, Vinamilk is also looking for a landbank to build a new factory in order to replace Truong Tho and Thong Nhat Factory in the future. The new factory will focus on producing yogurt and powdered milk.

Expanding more cow farms. At the end of 2016, Vinamilk was owning 17,500 cows in 8 farms, supplying 17% of the total raw materials for production. At the end of 2021, the herds will be increased to 44,400 cows to satisfy 40% of total demand for manufacturing. In the long term, Vinamilk plans to develop more cow farms across Vietnam as well as co-operate with farmers to ensure the input materials for all the factories.

Table 1: New cow farms

Cow farm	Quantity of cows
Ba Vi	8,000
Ha Nam	4,000
Thanh Hoa	24,000
Da Nang	4,000
Can Tho	20,000
Vinh Long	4,000
Total	***64,000***

Source: Vinamilk

Divestment from SCIC. In Oct, SCIC continues to auction 3.33% its ownership in Vinamilk (equivalent to 48.3 million shares) at the price of VND154,000/share, 3.8% higher than the closing price on 14/9/2017. In the previous divestment, SCIC sold 78.38 million shares at the price of VND144,000 and F&N was the only buyer.

Applying new standards to distinguish dairy products. The Ministry of Health announces the new QCVN 5-1:2017/BYT standard to provide clear concepts to differentiate each type of liquid milk product, thereby changing the name of dairy products on the package from March 2018. In the new standard, we find that there are differences in the way we call dairy product obtained from adding water to milk powder or condensed milk. Specifically, these products, following the new standard, will be called reconstituted milk instead of UHT milk as the old standard.

Table 2: Classify liquid milk products by two new and old standard

QCVN 5-1:2010/BYT	QCVN 5-1:2017/BYT
- Raw milk (pasteurized/sterilized)	- Raw milk (pasteurized/sterilized). - Non fat raw milk (pasteurized/sterilized)
- Fresh milk (pasteurized/sterilized)	- Fresh milk (pasteurized/sterilized) - Non fat fresh milk (pasteurized/sterilized)
- UHT milk*	**- Reconstituted milk (pasteurized/sterilized)***
- Condensed milk	- Condensed milk

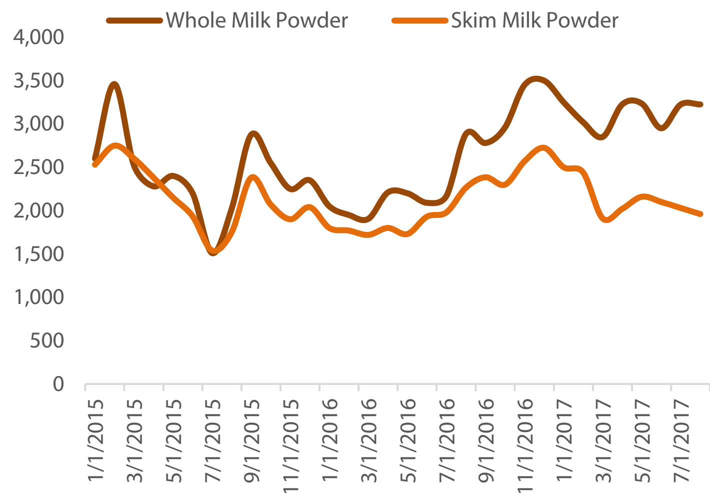
Source: Ministry of Health

The new standard may change the trend in dairy consumption. Previously, Vietnamese consumers misunderstood between fresh milk and reconstituted milk (or UHT milk) but this perception may change with the new standard. And this may lead to a new trend in dairy consumption from reconstituted milk (or UHT milk) to fresh milk which adapts the "fresh" taste of Vietnamese consumers. It should be noted that the selling price of fresh milk is 30–40% higher than reconstituted milk so we anticipate the movement will come from the urban area with a higher income than the rural one.

Regarding to Vinamilk, we believe that their business result will be less exposed to that movement thanks to the low contribution in revenue from reconstituted milk (10% as our estimation) and Vinamilk can compensate by boosting sales from the fresh milk segment with the "100% Fresh Milk" brand that has created a position in Vietnamese consumer perception.

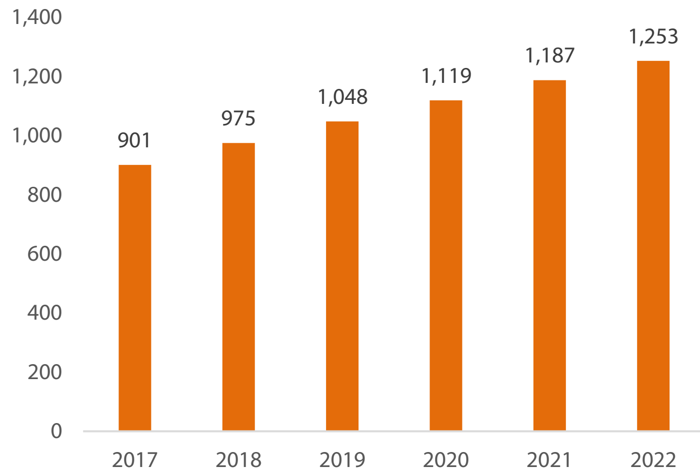
Appendix:

Figure 1: Milk powder price (USD/tonne)



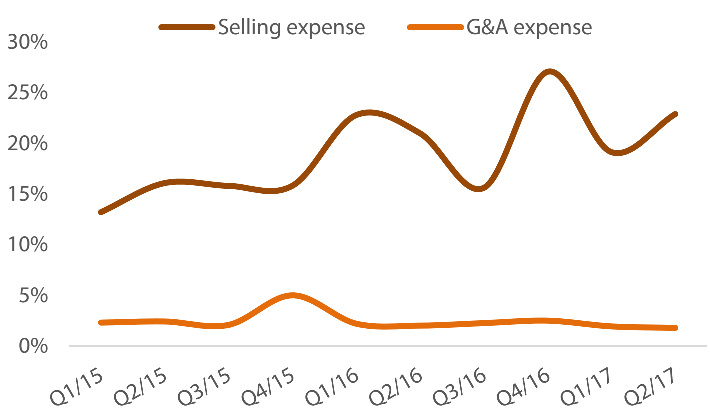
Source: Bloomberg

Figure 2: Milk consumption in Vietnam 2017-2022 (thousand tonne)



Source: Euromonitor

Figure 3: Selling expense and G&A expense over revenue (%)



Source: RongViet Research

Table 3: Market share of some segments

Product	2016	Current
Liquid milk	54.5%	56%
Powdered milk	40.6%	42%
Eating yogurt	84.7%	85%
Drinking yogurt	33.9%	37%

Source: Vinamilk

Unit: VND billion

INCOME STATEMENT	FY2015	FY2016	FY2017E	FY2018F
Revenue	40,080	46,794	52,922	59,470
COGS	23,818	24,459	27,977	31,874
Gross profit	16,262	22,336	24,945	27,596
Selling expense	6,258	10,759	11,484	12,489
G&A expense	1,233	1,053	1,048	1,308
Financial income	649	723	799	860
Financial expense	163	102	87	83
Other income/loss	96	77	77	77
Gain/(loss) from JV	13	16	18	20
PBT	9,367	11,238	13,220	14,673
Tax expense	1,598	1,874	2,247	2,494
Minority interests	-4	14	14	14
PAT	7,773	9,350	10,959	12,165
EBIT	8,772	10,524	12,413	13,799
EBITDA	9,869	11,715	13,674	15,166

Unit: %

FINANCIAL RATIO	FY2015	FY2016	FY2017E	FY2018F
Growth				
Revenue	14.3	16.8	13.1	12.4
EBITDA	24.2	18.7	16.7	10.9
EBIT	26.9	20.0	18.0	11.2
PAT	28.1	20.3	17.2	11.0
Total Asset	6.6	6.8	4.5	9.7
Total Equity	5.1	7.1	5.2	9.6
Profitability				
Gross margin	40.6	47.7	47.1	46.4
EBITDA margin	24.6	25.0	25.8	25.5
EBIT margin	21.9	22.5	23.5	23.2
Net margin	19.4	20.0	20.7	20.5
ROA	28.4	32.0	35.9	36.3
ROE	40.2	45.3	50.8	51.9
Efficiency (x)				
Receivable Turnover	14.9	16.3	20.0	20.0
Inventory Turnover	6.3	5.4	5.9	6.3
Payable Turnover	5.8	5.2	5.5	5.5
Liquidity (x)				
Current	3.0	3.1	3.2	3.2
Quick	2.3	2.4	2.4	2.4
Solvency				
Total Debt/Equity	8.9	7.5	5.4	5.0
ST debt / Equity	7.1	6.0	4.4	4.5
LT debt/ Equity	1.8	1.5	1.0	0.6

Unit: VND billion

BALANCE SHEET	FY2015	FY2016	FY2017E	FY2018F
Cash and cash equivalents	1,359	655	1,443	3,346
Short term investment	8,668	10,454	10,454	10,454
Accounts receivable	2,685	2,867	2,646	2,974
Inventories	3,810	4,522	4,756	5,100
Other current assets	209	176	185	194
Tangible Fixed Assets	8,699	8,919	9,409	9,787
Intangible Fixed Assets	561	529	497	465
Long term investment	940	614	632	652
Other non current assets	463	516	542	569
Total Asset	**27,396**	**29,251**	**30,563**	**33,540**
Account Paybale	4,124	4,668	5,082	5,790
Short term borrowings	1,475	1,333	1,030	1,140
Long term borrowings	368	327	236	146
Other non-current liabilities	182	188	198	208
Bounus and Welfare fund	405	457	457	457
Technology – Science dev fund	0	0	0	0
Total Liabilities	**6,554**	**6,973**	**7,002**	**7,739**
Common stock and APIC	12,007	14,775	14,775	14,775
Treasury stock	-5	-1	-1	-1
Retained Earnings	5,392	5,592	5,651	6,674
Other comprehensive income / (loss)	8	6	6	6
Investment and Development Fund	3,291	1,797	2,893	4,110
Total Equity	**20,693**	**22,169**	**23,323**	**25,563**
Minority Interest	231	237	237	237
Total Resources	**27,396**	**29,251**	**30,563**	**33,540**

VALUATION RATIO	FY2015	FY2016	FY2017E	FY2018F
EPS (dong)	4,864	5,831	6,796	7,543
P/E (x)	21.0	21.5	21.8	19.6
BV (dong)	17,427	15,437	16,073	17,617
P/B (x)	5.8	8.1	9.2	8.4
DPS (dong/cp)	6,000	6,000	6,000	6,000
Dividend yield (%)	5.9	4.8	4.1	4.1

VALUATION MODEL	Price	Weight	Average
FCFF	161,519	50%	80,759
PE	177,260	50%	88,630
Target price (dong)			**169,389**

VALUATION HISTORY	Price	Recommendation	Period
15/03/2017	151,800	Neutral	Long term

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	NEUTRAL	SELL
Total Return including Dividends in 12-month horizon	>20%	-20% to 20%	<-20%

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