April, 2019

PETROVIETNAM FERTILIZER AND CHEMICALS (HSX: DPM)

Likely no contribution from NPK in 2019

Particulars (VND B)	Q4-FY18	Q3-FY18	+/-qoq	Q4-FY17	+/-yoy
Net revenue	2,321	2,193	5.9%	1,532	51.5%
PAT	149	156	-4.3%	103	44.8%
EBIT	188	189	-0.6%	43	339.8%
EBIT margin	8.1%	8.6%	-52bps	2.8%	531bps

Source: DPM, Rong Viet Securities

Q4/2018 result: Increasing sales compensate for the drop in gross margin

Thanks to the contribution of NPK products and the recovery of Urea prices, DPM's revenue recorded VND 2,370 bn, up 52.3% YoY. However, the higher gas input price caused gross profit margins to decrease from 28% to 20.2%. The gross profit in Q4/2018 still increased by 10.6% to VND480 bn and EBT reached VND215bn, up +75% YoY as the company managed SG&A well.

Totally, DPM posted VND 9,297 bn in revenue, up 16.2% thanks to (1) 12% growth in Urea's ASP (2) contribution from NPK in Q4/2019 (3) a rise in NH3's sales. However, the net profit was flat at VND700 bn.

2019 outlook: Profit will hit the bottom

2019 production will be negatively impacted due to plant maintenance starting at the end of February and lasting 80 days. We believe that the Urea consumption for 2019 to reach 680 thousand tons, down 15.4% YoY. Besides, the selling price of Urea has started to decline slightly since the end of 2018 while the oil price is recovering, which will negatively affect the result of the Urea business, especially in Q1/2019 and Q2/2019.

Regarding the NPK segment, we think that the NPK can not generate profit in 2019 as gross margins are expected to remain thin to cover other expenses. Therefore, NPK is unlikely to become DPM's growth engine in 2019 even though sales are forecasted to be "smooth" thanks to its good product quality and well-known brand in the region.

For 2019, we project that revenue and net profit will be VND 9,395 bn (+1.1% YoY) and VND 667 bn (-4.7% YoY), respectively.

Valuation and recommendation

DPM is a market leader in fertilizers but in the short-term we see two factors affecting its business: (1) rising gas prices and (2) declining output due to the plant maintenance. Meanwhile, the efficiency of the new NPK project is low and cannot contribute much to the overall result of the company. Now, the current support of the stock comes from PVN's divestment plan as well as the stable cash dividend that the company is pursuing. Besides, VAT policy is another factor to be expected even though this issue has been mentioned so many times before.

*We maintain **ACCUMULATE** for DPM with the target price of **VND19,800** per share, basing on the FCFF and P/E method. Plus cash dividend of VND1,000, generating a total return of **15%**, compared to the closing price on **April 16th, 2019**. The business result is likely to hit the bottom in this year before recovering in 2020. So we think that the investor should take advantage of the opportunity as the bad result is released in the coming times.*

ACCUMULATE +15%

CMP (VND)	18,100
Target price (VND)	19,800
Cash dividend (VND)*	1,000

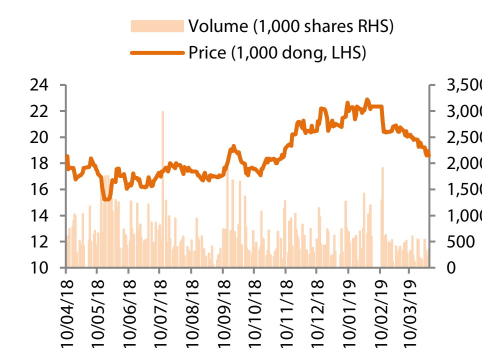
** Expected in the next 12 months*

Stock info

Sector	Chemicals
Market Cap (VND billion)	7,278
Current Shares O/S	391,334,260
Avg. Daily Volume (in 20 sessions)	331,973
Free float (%)	17.6
52 weeks High	22,887
52 weeks Low	15,231
Beta	0.23

	FY2018	Current
EPS	1,551	1,551
EPS growth (%)	1.2	1.2
Adjusted EPS	1,551	1,551
P/E	14.4	14.4
P/B	1.1	1.1
EV/EBITDA	5.5	5.5
Cash dividend	1,000	1,000
ROE (%)	8.7	8.7

Price performance



Major Shareholders (%)

PVN	59,5
Nghe An Ltd	3,7
Edgbaston	4,9
Foreign ownership room (%)	26.07

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Exhibit 1: Q4 2018 results

Particulars (VND B)	Q4-FY18	Q3-FY18	+/-(QoQ)	Q4-FY17	+/-(YoY)	4Q-FY18	+/-(YoY)
Net revenue	2,321	2,193	5.9%	1,532	51.5%	9,297	16.3%
Gross profit	480	490	-2.2%	434	10.5%	1,899	-10.0%
SG&A	68	17	290.2%	21	220.6%	1,098	-23.8%
Operating income	412	473	-13.0%	413	-0.3%	801	19.6%
EBITDA	341	362	-5.7%	91	275.5%	1,321	53.3%
EBIT	188	189	-0.6%	43	339.8%	801	19.6%
Financial expenses	33	23	43.3%	1	4248.0%	74	5247.8%
- Interest Expenses	28	21	32.6%	0	28330.0%	63	32842.1%
Dep. and amortization	153	173	-11.3%	48	218.4%	519	171.3%
Non-recurring items (*)							
Extraordinary items (*)							
PBT	215	190	12.9%	120	79.5%	871	2.1%
PAT	149	156	-4.3%	103	44.8%	700	0.7%
(*) Adjusted PAT	149	156	-4.3%	103	44.8%	700	0.7%

Source: DPM, Rong Viet Securities

Exhibit 2: Q4 2018 performance analysis

Particulars	Q4-FY18	Q3-FY18	+/-(QoQ)	Q4-FY17	+/-(YoY)
Profitability ratios (%)					
Gross margin	20.7	22.4	-170bps	28.3	-767bps
EBITDA margin	14.7	16.5	-180bps	5.9	876bps
EBIT margin	8.1	8.6	-52bps	2.8	531bps
Net margin	6.4	7.1	-68bps	6.7	-30bps
Adjusted net margin	6.4	7.1	-68bps	6.7	-30bps
Turnover *(x)					
-Inventories	4.4	4.0	0.4	3.7	0,7
-Receivables	18.7	19.6	(1.0)	14.8	3,8
-Payables	4.6	3.7	0.9	4.1	0,5
Leverage (%)					
Total debt/ equity	18.3	24.9	-658bps	17.6	71bps

Source: DPM, (*) Annualized turnover

Exhibit 3: Q4 2018 performance forecast

Particulars (VND B)	Q4-FY18	+/-(QoQ)	+/-(YoY)
Revenue	2,450	5.6%	17.6%
Gross profit	497	3.7%	7.0%
EBIT	211	12.1%	6.1%
NPAT	176	18.2%	-2.3%

Source: DPM, Rong Viet Securities.

Update:

Factory maintenance hit the Urea and NH3

DPM's Urea plant is always operating at 100% capacity thanks to high domestic demand while the domestic supply is unstable due operational problems in Ha Bac Urea plant and Ninh Binh one in Northern Vietnam. However, due to the maintenance process totalling 80 days starting from the end of Feb 2019, Urea output in 2019 will be affected. With production output expected to be only 671 thousand tons, equivalent to 84% of capacity, we believe that urea consumption in 2019 will stay at 680 thousand tons, down 15.4%. However, we believe the average selling price will still be 2% higher than 2018 while the cost of input gas decreases by 10.5%, helping the gross profit of Urea to be stable at VND1,558 bn in 2019.

For NH3 products, commercial volume will also be affected when the plant is undergoing maintenance. With the assumption of 16% reduction in volume and additional depreciation from last year's NH3 – NPK project, NH3's gross profit is expected decrease by 38.9% to VND91 bn.

Table 1: Urea and NH3 forecast

	Unit: VND bn	2018	2019F	% change
Urea	Revenue	5,665	4,863	-14.1%
	Gross profit	1,536	1,558	1.4%
NH3	Revenue	408	349	-14.4%
	Gross profit	149	91	-38.9%

Source: Rong Viet Securities forecast

NPK result is still a question

With a huge demand for the high quality NPK in the country, building a NPK plant is a right way for DPM to expand its business. High quality and good brand should ensure the consumption of NPK Phu My products in the Southern market. However, we have concerns over its profitability given the large initial investment in the NPK-NH3 factory.

Assuming sales volume of 184 thousand tons with average selling price similar to 2018s, NPK gross profit margins are projected at 5.2%, which is quite thin to cover other expense. In order to increase the gross profit, DPM can increase the selling price or cut the selling expense. But the company may find it hard to increase selling prices owing to the competition in the Southern market or to cut selling expenses when the proportion of SG&A / revenue in 2018 has decreased significantly compared to the previous years **(see figure 4)**. As such, we believe that NPK could not generate profit for DPM in 2019.

Table 2: NPK forecast

Unit: VND bn	2018	2019F	2020F	2021F
Revenue	321	1,703	1,893	1,912
Gross profit	12	89	136	155
GPM (%)	*3.6%*	*5.2%*	*7.2%*	*8.1%*

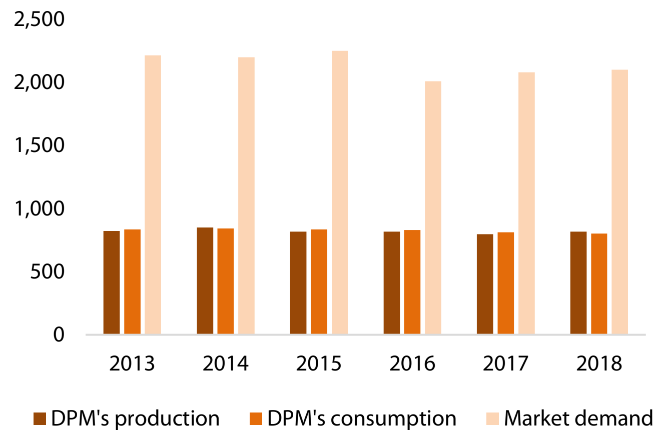
Source: Rong Viet Securities forecast

Divestment and changing the VAT policy could be a support in short term

Regarding VAT policy, putting fertilizer into the 5% VAT bracket would help DPM save money and increase its profit. However, the approval for this policy is still pending now.

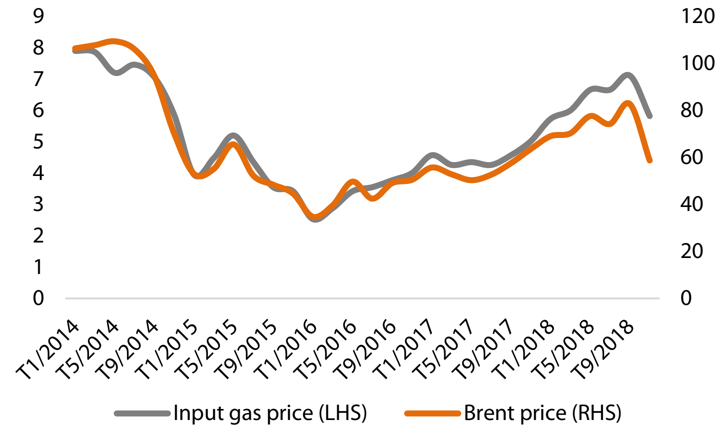
For the divestment plan, PetroVietnam considers a merger between DPM and DCM. Currently, DPM and DCM are the two largest Urea players in the Southern region. So in our opinion, the consolidation in our opinion is good in terms of business when DPM and DCM's position has been proven in recent years. This combination will create a highly competitive enterprise in the Southern region with nearly 100% market share. However, in terms of finance, DCM will no longer receive gas price support from 2019 onwards, which will significantly affect DPM's profit when conducting the M&A. In order for this option to become feasible, we believe that there must be a-new mechanism to support DCM so that the M&A with DPM does not cause financial losses for DPM as well as ensure the benefit for the current shareholders. Anyway, the M&A only stops at the proposal and we will get more comments when new related information is published.

Figure 1: Urea production and consumption of DPM and Urea market demand (thousand tons/year)



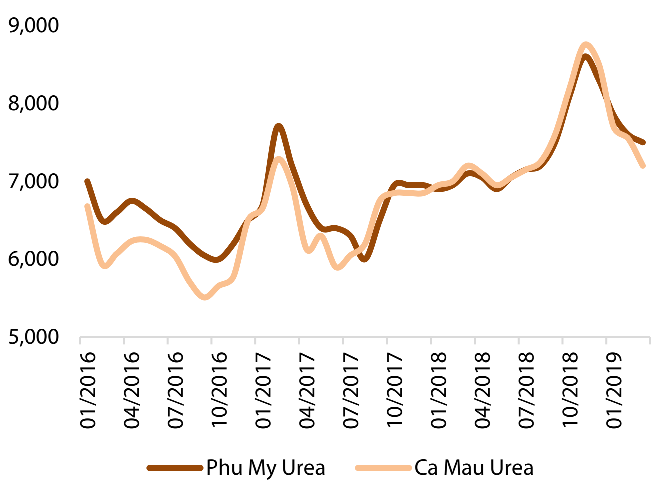
Source: DPM

Figure 2: Input gas price (USD/MMBTU) and Brent crude oil price (USD/barrel)



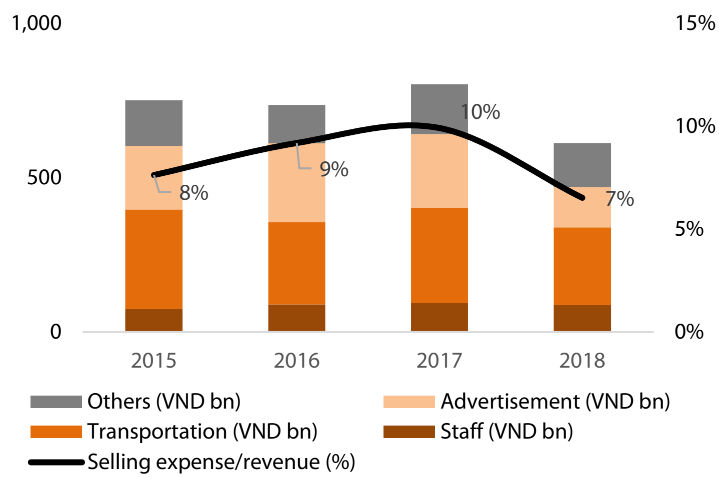
Source: DPM

Figure 3: Domestic Urea price (VND/kg)



Source: Rong Viet Securities complied

Figure 4: Selling expense breakdown (LHS) and selling expense/sales (RHS)



Source: DPM

VND in billions

Income statement	FY2017	FY2018	FY2019F	FY2020F
Revenue	7,996	9,297	9,395	10,561
COGS	5,884	7,398	7,488	7,944
Gross profit	**2,111**	**1,899**	**1,907**	**2,618**
Selling expense	803	612	611	845
G&A expense	639	486	489	613
Financial income	165	124	95	118
Financial expense	1	74	84	72
Other income/loss	16	16	16	16
Gain/(loss) from JV	4	3	3	4
PBT	**853**	**871**	**838**	**1,226**
Tax expense	145	158	159	233
Minority interests	13	13	12	18
PAT	**694**	**700**	**667**	**975**
EBIT	670	801	808	1,160
EBITDA	862	1,321	1,268	1,640

%

Financial ratio	FY2017	FY2018	FY2019F	FY2020F
Growth (%)				
Revenue	0.9	16.3	1.1	12.6
Operating income	-42.3	19.6	0.8	29.5
EBITDA	-38.8	53.3	-4.0	43.9
PAT	-38.4	0.7	-4.7	46.6
Total assets	7.3	8.5	-1.4	3.4
Equity	-2.1	2.7	-2.7	5.3
Profitability (%)				
Gross margin	26.4	20.4	20.3	24.8
EBITDA margin	10.8	14.2	13.5	15.5
EBIT margin	8.4	8.6	8.6	11.0
Net margin	8.7	7.5	7.1	9.2
ROA	6.8	6.3	6.1	8.3
ROE	8.8	8.7	8.5	11.2
Efficiency (x)				
Receivable turnover	31.2	17.9	16.7	16.7
Inventory turnover	4.8	4.4	4.5	4.8
Payable turnover	4.3	5.9	5.0	5.6
Liquidity (x)				
Current	3.6	3.5	3.5	4.4
Solvency (%)				
Total debt/equity	8.0	15.3	12.0	9.1
Current debt/equity	0.0	2.5	0.0	0.0
Long-term Debt/equity	8.0	12.8	12.0	9.1

VND in billions

Balance sheet	FY2017	FY2018	FY2019F	FY2020F
Cash and cash equivalents	2,362	1,717	1,974	2,080
Short term investment	895	955	745	1,612
Accounts receivable	257	521	564	634
Inventories	1,223	1,663	1,647	1,668
Other current assets	281	317	333	349
Tangible fixed assets	4,061	4,840	4,590	4,321
Intangible fixed assets	896	860	849	839
Long term investment	47	47	50	53
Other non-current assets	243	215	226	237
Total asset	**10,264**	**11,134**	**10,979**	**11,794**
Account payable	1,381	1,256	1,498	1,430
Short term borrowings	0	202	0	0
Long term borrowings	629	1,032	942	795
Other non-current liabilities	134	301	316	332
Bonus and welfare fund	36	56	156	308
Technology -science dev fund	40	33	33	33
Total liabilities	**2,221**	**2,879**	**2,944**	**2,897**
Common stock and APIC	3,935	3,935	3,935	3,935
Treasury stock	-2	-2	-2	-2
Retained earnings	442	657	437	1,300
Other comprehensive income / (loss)	0	0	0	0
Investment and development fund	3,497	3,497	3,497	3,497
Total equity	**7,872**	**8,087**	**7,867**	**8,730**
Minority interest	171	168	168	168
Total resources	**10,264**	**11,134**	**10,979**	**11,794**

Valuation ratio	FY2017	FY2018	FY2019F	FY2020F
EPS (VND)	1,532	1,551	1,448	2,118
P/E (x)	14.0	14.4	12.6	8.6
BV (VND)	20,113	20,662	21,102	22,214
P/B (x)	1.0	1.1	0.9	0.9
DPS (VND/cp)	2,000	1,000	1,000	1,000
Dividend yield	9.3%	4.5%	5.5%	5.5%

Valuation model	Price	Weight	Average
FCFF	26,310	50%	13,155
P/E	13,332	50%	6,666
Target price (VND)			**19,821**

Valuation history	Price	Recommendation *
15/03/2017	21,500*	ACCUMULATE
30/09/2017	19,900*	ACCUMULATE

** Adjusted price*

RESULTS UPDATE

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RATING GUIDANCE

Ratings	BUY	ACCUMULATE	REDUCE	SELL
Total Return including Dividends in 12-month horizon	>20%	5% to 20%	-20% to -5%	<-20%

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