RONGVIET SECURITIES

04 July 2016

DRY CELL AND STORAGE BATTERY JSC (PAC– HSX)

PROFIT DRIVER FROM REPLACEMENT SEGMENT

Dry Cell & Storage Battery Joint Stock Company Pinaco (PAC-HSX) is the leading battery manufacturing company in Vietnam. With the advantages in market share, distribution channel, and customer relationship with Thaco Trường Hải, Ford, demand for PAC is ensured and growth is stable. Due to optimistic factors in the market, revenue and net profit in first quarter 2016 recorded the growth rates of 19.7% and 12% compared to previous period. We estimated revenue and net profit for 2016 as VND 2,428 billion (+17%) and VND 121 billion (+33.8%) respectively which match with an EPS forward 2016 of VND 2,344. Besides, stable dividends over the years and healthy financial status with safe leverage ratio are the attractive points to investors.

Information about the dividend of 25-50% of par value in cash is the main reason for PAC's share price to raise by 60% in the past 03 months. The dividend comes from the development fund and share premium.

Referring to average P/E of automobile parts manufacturing companies in Asia at 24,7 times and PAC's growth prospects in the next 5 years, we determine that the reasonable P/E for PAC shares is between 12-13 times. Using the valuation method FCFF, we forecast the price of PAC at **36.600** VND per share. With the closing price at this day higher than the reasonable price by 14.7%, we recommend to **REDUCE** for PAC in **INTERMEDIATE**.

Investors should keep in mind that sale projection is the main focus in our evaluation of PAC share price. We excluded the possible effect of changing major shareholders (Vinachem withdraw) and speculating cash flow as "buying stock with a strong domestic brand, then sell to foreign investors in the same sector."

Key financials

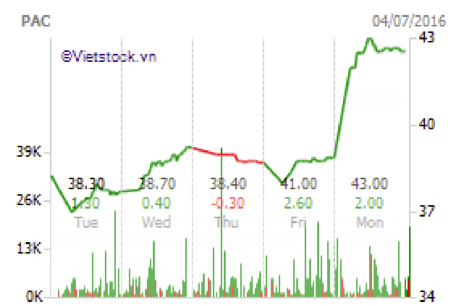
Y/E Dec (VND bn)	FY2014	FY2015	FY2016F	FY2017F
Net Revenues	2,026.3	2,116.8	2,428,6	2,888.6
% chg	7.8%	4.5%	14.7%	18.9%
PAT	74.6	90.5	121.0	138.8
% chg	21.4%	21.3%	33.8%	14.7%
EBIT margin (%)	3.7%	4.3%	5.0%	4.8%
ROA (%)	5.6%	7.2%	9.7%	10.5%
ROE (%)	15.6%	18.2%	23.5%	24.8%
EPS (VND)	1.920	2.334	2.344	2.987
Adjusted EPS (VND)	2,763	2,920	2,344	2,987
Book value (VND)	17,951	16,336	11,189	12,908
Cash dividend (VND)	2,000	1,500	2,500	1,200
P/E (x)	11.8	14.3	18.1	14.2
P/BV (x)	1.3	2.0	3.8	3.3

*Sources: PAC, RongViet Research estimated. * As of closing price in 4 July 2016*

REDUCE

Market price (VND)	43,000
Target price (VND)	36,600
Investment term	**INTERMEDIATE**

Stock Info	
Sector	Automobile & Parts
Market Cap (VND bn)	1,998
Current Shares O/S	46,471,707
Beta	0,18
Free Float (%)	39,31
52 weeks High	43,000
52 weeks Low	15,300
Avg. Daily Volume (in 20 sessions)	287.890



Source: Vietstock

Performance (%)	3T	1N	3N
PAC	25%	49%	161%
Retail	32%	28%	84%
VN30 Index	17%	15%	33%
HSX Index	12%	7%	17%

Major shareholders (%)

Vietnam National Chemical Group	51.43
Beira Limited	5.21
FOL(%)	28.17%

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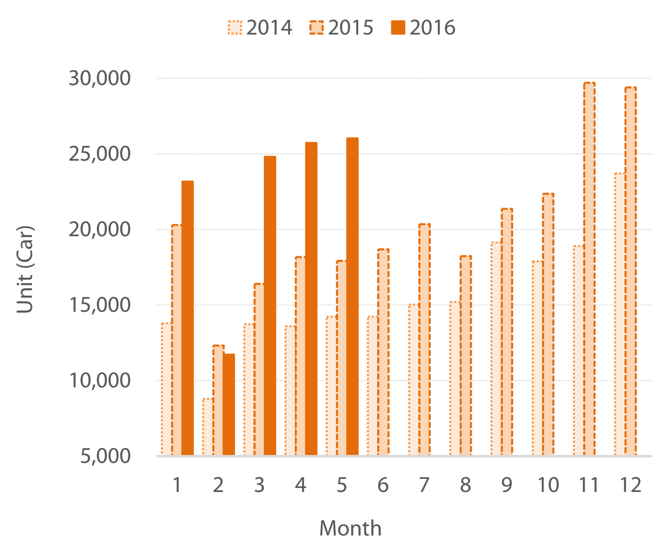
High expectation for automobile battery segment

Dry Cell and Storage Battery JSC (PAC –HSX) is a leading company in Vietnam specializing in manufacturing and producing dry cell and storage battery; in which, storage battery contributes up to 70% of total revenue. In 2016, automobile battery is expected to be the key driver for its profit growth. Fundamentally, battery replacement does not heavily depend on the volatility of the automobile industry. A battery replacement tends to last up to two years or less depending on the frequency and condition of usage. Thus, 2016 demand for battery replacement would anchor to the demand of automobile market during 2014-2015. Looking back at the last two years, automobile market recorded impressive growth rates thanks to (1) tightening truck load policy, (2) reducing import tariff according to the free trade agreement (ATIGA). Hence, 2016 is projected to be a "big" year for battery replacement. According to our calculation, in 2016, demand for storage battery could go up by 30% y-o-y.

Apart from the battery replacement, OEM segment is expected to keep a positive growth rate in this year. According to VAMA, in 5M2016, sale volume reached 111,438 cars (+22% y-o-y); in which, passenger and commercial cars up 21% and 42% y-o-y respectively. As shown in the figure, sale volume remained its uptrend but unable to achieve last year's impressive growth rate. For the remaining of the year, automobile demand is forecasted to rise thanks to (1) the adjustment of special tax rate which lower tax for low volume capacity cars and (2) reducing import tariff. In our opinion, OEM sale volume could be up about 5% y-o-y.

Exhibit: Sale volume of automobile market during 2014-2016



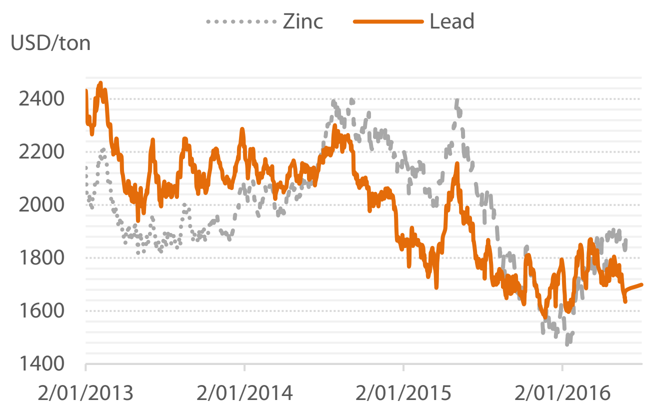
Source: VAMA

Two factors that contribute to the change in gross margin (%)

Lead materials takes up to 80% of the cost of goods sold. Excluding the exchange rate's impact, 1% up of lead prices would lead to a 2-3% variation in gross margin. Currently, the ratio between domestic and imported materials is about 25:75, thus, PAC greatly depends on the fluctuation of global prices.

Ceasing major lead mines in Australia, Mexico and Ireland (See the appendix below) did not stop lead prices to plunge at around 1.700 USD/ton (down 14.9% y-o-y) in 2015. According to International Lead and Zinc Study Group, till April 2016, current lead surplus is about 49.000 ton. In 2016, the global lead market is likely to see a bigger surplus than previously expected due to falling consumption; total 2016 surplus could be about 76.000 ton. Particularly, production and usage are forecasted to increase 2.3% and 2% respectively. According to Bloomberg, lead price is forecasted to remain downtrend and the average price would be about 1,795 USD/ton. In the long term perpestive, PAC aims to replace imported by domestic materials in order to minimize exchange rate risk. However, PAC has been struggling to find a suitable supplier that could meet its standard requirements. Thus, in the short-term, PAC will still be depending on the volatility of worldwide prices.

Movement of lead and zinc prices during 2013-2016



Source: Bloomberg

Expected lead prices in 2016

	2016	2017	2018	2019	2020
Median	1768	1875	2030	2025	2200
Average	1795	1917	2041	2053	2070
Highest	2315	2425	2535	2535	2200
Lowest	1604	1494	1772	1673	1739

Source: Bloomberg

Apart from lead prices, gross margin is also impacted by the adjustment of discount rates. In 2015, lead prices reached its lowest since 2011, expressing a drop of 45% in comparison with its highest price. However, PAC gross margin recorded a drop by 0.97% due to (1) adjustments in selling expense in compliance with Circular N200, (2) Raising discount rate. Under the scenario, we estimate that the discount rate would hover around 10% and gross margin would be about 15.77%, down 2.2% y-o-y.

Investment risks

Investors who consider investing in this stock should take notice of the following risks (1) Relocation of storage battery and dry cell factories, (2) Exchange rate risk and (3) Input price volatility. Firstly, factory relocation is likely to impact on production capacity and hence revenue itself. According to PAC, Saigon Storage Battery Factory would be moved to Nhon Trach whereas Dry Cell factory would be moved to Saigon factory in order to perform better management. In order to avoid production interruption, PAC may choose to relocate the factory in a progress rather than moving everything at the same time. Secondly, the majority of input materials are imported thus PAC is vulnerable to the widely fluctuating world prices. Investor can check out the table below which shows NPAT's sentivity to exchange rate and change in import volume. Thirdly, market players are pointing the finger at China's black market for weak lead prices. Currently, China accounts for 40% of global lead metal demand. If feasible, a new policy to tighten the control over the black market may boost global demand and thus lead to a rise in prices.

Table: Sensitivity of NPAT to exchange rate and volume of materials

Loss from exchange rate (VND bn)		**Change in exchange rate (%)**				
		1%	**2%**	**3%**	**4%**	**5%**
Change in volume (%)	5%	0.90	1.79	2.69	3.59	4.49
	10%	1.79	3.59	5.38	7.18	8.97
	15%	2.69	5.38	8.07	10.76	13.46
	20%	3.59	7.18	10.76	14.35	17.94

	25%	4.49	8.97	13.46	17.94	22.43

Source: RongViet Research

Q2 FY2016 and FY 2016 Forecast

With the above base case scenario and assumption, we forecast that 2016 revenue and NPAT could be VND 2.644 bn (+17% y-o-y) and VND 121 bn (+34% y-o-y) respecitvely. After taking out bonus and welfare (10%), EPS forward is estimated at around 2,344 dong per share. The above forecast is different from the most recent update due to (1) The potential prospect of the battery replacement and OEM segment, (2) The input prices' recovery, especially lead and zinc.

In Q2 2016, PAC business results is expected to remain its uptrend thanks to the plunge of input prices and optimistic prospect of automobile battery segment. Furthermore, based on historical data, Q2 tends to be the peak quarter for PAC. Thus, with the above assumption, we forecast that Q2 net revenue and NPAT at about VND 628.7 bn (+5% y-o-y) and VND 33.1 bn (+51% y-o-y) respectively.

Exhibit: Q2 –FY 2016 Forecast

Particulars	Q2-FY16	Q1-FY16	+/- qoq	Q2-FY15	+/- yoy
Net Revenues	628.7	542.5	15.9%	601.2	5%
NPAT	33.1	21.9	51%	27.6	20%
EBIT	44.3	33.7	31%	37.2	19%
EBIT margin	7.1%	6.2%	83bps	6.2%	87bps

Source: RongViet Research

What do PAC's shareholders expect from Vinachem's withdrawal?

Investors has expected Vinachem's withdrawal for quite sometimes. We recently noticed significant increase in PAC's share price because of the possibility of Vinachem's withdrawal in this year.

During 2011-2016, Vinachem has planned to withdraw invested capital from more than 17 firms but it has failed to complete its target due to several reasons such as legal issues, unsuccessful auctions… Vinachem has successfully withdrawn from almost 10 firms which reached 50% of its target and 2/3 of those are not public companies. Due to the small number of successfully cases, it is hard to forecast the impact of exiting on the performance of those firms.

In order to better compare and evaluate the Vinachem's effect, we put together a list of firms on the stock market that had been effected by the government shareholder and met a couple conditions like (1) operating in the manufacturing sector, and (2) government shareholders exited before January 2015. DQC, RAL, RDP, INN, DBC are the selected firms. Reviewing the pre-exit performance period 2010-2014, most of all firms has improved their performance, shown a positive revenue growth, and value-added financial ratios. One year after the exit, except for DQC, profit margins of all other firms have shown the improvement in 2015. RDP's profit margin has been doubled compared to 2014. ROA and ROE of all others firms also showed improvement. In addition, post-exit period also illustrated a short enhancement of market price (details in reference table page 9). As a result, investors' expectation about the positive impacts on the business performance of government firm is validated based on historical events (example above).

In the case of PAC, we set out a scenario assumes that major shareholder Vinachem will divest this year. With this assumption, the profit margin is expected to improve as in the case of companies in the considered sample. Basis to make this expectation is the exclusive distribution system with sales discount is high (at approximate 10-11%) and can be adjusted after the withdraw of the state shareholder Vinachem. By adjusting the discount sales, PAC's profit margin can increase by around 3 - 5%. With the mentioned scenario of production and the average lead price, PAC can realize Net Income of about VND 196.7 billion corresponding to VND 3.811 in EPS. Notably, this is only a scenario and we do not have specific information about the route of Vinachem divestment at the present. The above analysis is set to help investors quantify the impact of the divestment (as assumed) on business results.

Additionally, the divestment of the State from a strong-domestic-brand company like Pinaco can attract the attention of many foreign investors in the same business, whose goal is to master the Vietnam potential market which plays a more important role than improving the business performance.

Exhibit: Vinachem divesment plan in 2011-2020

Status	Company
Fully divested	*Vinh Thinh ChemCo*
	Phuong Dong
	Son Chat Deo
	CECO JSC
	Additives And Petroleum Products JSC
	CK TM và CN VN
	Bao Minh
	Viet Duc Welding Electrode JSC
	JVF JSC
	CT TC CP Hóa Chất
To divest	*XNK hóa chất miền Nam*
	Inoe Rubber Vietnam
	TCP Vina Plastic& Chemical Corp., Ltd
	Ha Noi Soap JSC
	Vinh Phu Storage and Battery JSC
	Sơn TH HN
	Sovigaz
	Habac Nitrogenous Fertilizer & Chemicals Company Limite

Nguồn: Vinachem,. Rong Viet Research

Outlook and valuation

Dry Cell & Storage Battery Joint Stock Company Pinaco (PAC-HSX) is the leading battery manufacturing company in Vietnam. With the advantages in market share, distribution channel, and customer relationship with Thaco Trường Hải, Ford, demand for PAC is ensured and growth is stable. Due to optimistic factors in the market, revenue and net profit in first quarter 2016 recorded the growth rates of 19.7% and 12% compared to previous period. We estimated revenue and net profit for 2016 as VND 2,428 billion (+17%) and VND 121 billion (+33.8%) respectively which match with an EPS forward 2016 of VND 2,344. Besides, stable dividends over the years and healthy financial status with safe leverage ratio are the attractive points to investors.

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Valuation	Price	Weighted	Average
FCFF	48,390	40%	19,356
P/E	28,827	60%	17,296
Target price		**100%**	**36,652**

Ticker	Company names	Market cap	P/E
600742 CH	CHANGCHUN FAWAY AUTOMBILE-A	18,360,079	6.4
200581 CH	WEIFU HIGH TECHNOLOGY GROU-B	62,927,840	9.5
STANLY TB	THAI STANLEY ELECTRIC PUB CO	8,631,995	10.9
200030 CH	FAWER AUTOMOTIVE PARTS LTD-B	31,464,032	12.9
002126 CH	ZHEJIANG YINLUN MACHINERY -A	20,569,917	14.8
SMSM IJ	SELAMAT SEMPURNA PT	11,484,971	16.0
002085 CH	ZHEJIANG WANFENG AUTO -A	96,626,217	16.8
425 HK	MINTH GROUP LTD	77,239,343	17.7
MNDA IN	MINDA INDUSTRIES LTD	6,118,100	19.2
002510 CH	TIANJIN MOTOR DIES CO LTD-A	22,140,042	19.9
002454 CH	SONGZ AUTOMOBILE AIR CON-A	24,206,269	22.2
600676 CH	SHANGHAI JIAO YUN CO LTD-A	26,324,335	22.5
603006 CH	SHANGHAI LIANMING MACHINER-A	15,895,088	23.7
002662 CH	BEIJING WKW AUTOMOTIVE PAR-A	39,334,100	25.8
603023 CH	HARBIN VITI ELECTRONICS CO-A	23,136,988	26.3
002536 CH	HENAN PROVINCE XIXIA AUTO-A	16,873,392	27.6
600523 CH	GUIZHOU GUIHANG AUTOMOTIVE-A	17,112,548	30.7
600480 CH	LINGYUN INDUSTRIAL CORP-A	20,273,142	35.9
3663 HK	XIEZHONG INTERNATIONAL HOLDI	5,079,818	36.0
300473 CH	FUXIN DARE AUTOMOTIVE PART-A	22,953,361	42.9
002448 CH	ZYNP CORP-A	29.886.918	45.7
002472 CH	ZHEJIANG SHUANGHUAN DRIVEL-A	25,885,428	46.1
601689 CH	NINGBO TUOPU GROUP CO LTD-A	67,754,836	46.7
	PE		24.70
	Adjusted PE		**12.30**

Source: Bloomberg

Appendix 1:

Exhibit: List of closed lead mines in 2015

No	Mines	Countries	Capacity per year
01	Century	Australia	50,000
02	Paroo Station	Australia	85,000
03	Lisheen	Ireland	30,000
04	Naica	Mexico	20,000

Source: International Lead and Zinc Study Group

Table: April 2016 ILZSG Global Forecasts

Thousand tonnes	Estimated 2016	2015	% Change
Production	10,904	10,653	2.3%
Usage	10,828	10,611	2.0%
Surplus/(Deficit)	76	42	81,9%

Source: International Lead and Zinc Study Group

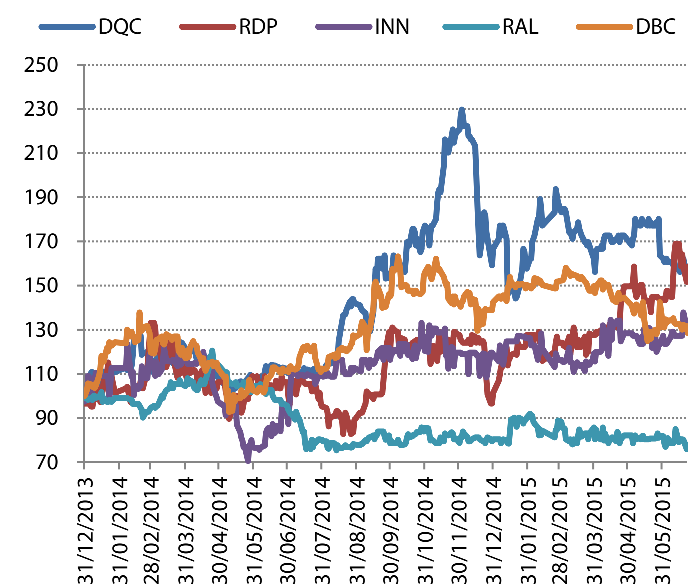
Appendix 2:

Table: SOE divestment plan of SCIC in 2014

Tickers	Exchange	% Divested
C47	HSX	25.96
DNC	HNX	57.38
DQC	HSX	15.93
HAI	HSX	49.96
INN	HNX	18.75
LAF	HSX	23.03
NSC	HSX	11.02
RDP	HSX	54.21
TBC	HSX	24.00
TET	HNX	28.65
TSC	HSX	42.21
TTR	UPCOM	53.78
YBC	UPCOM	39.85

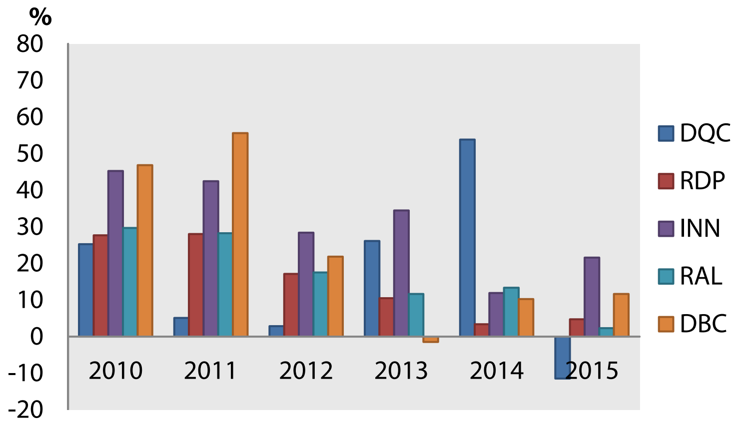
Source: RongViet Research

Exhibit: Movement of price



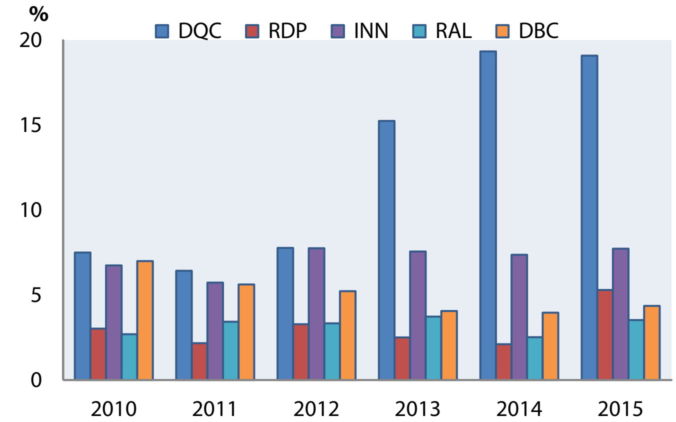
Source: RongViet Research

Exhibit: Sale growth (%) during 2010-2015



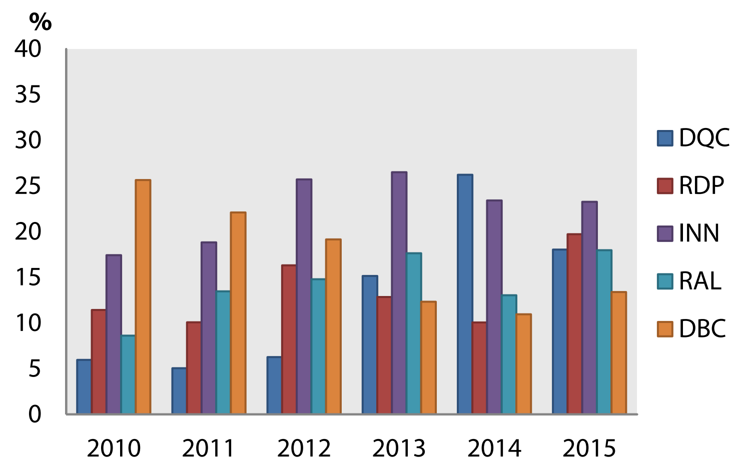
Source: RongViet Research

Exhibit: Net profit margin (%) during 2010-2015



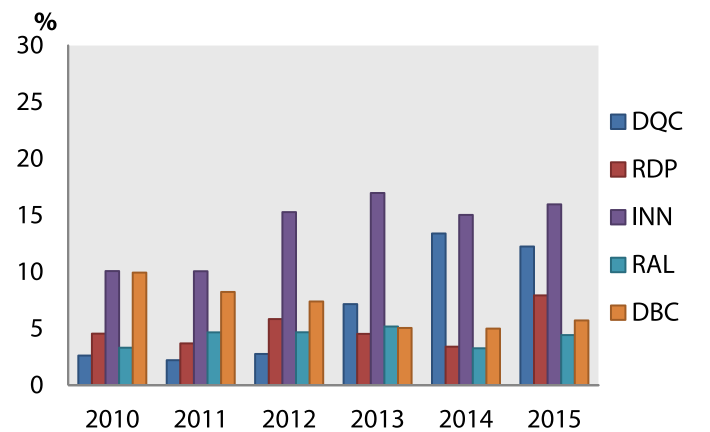
Source: RongViet Research

ROE (%) during 2010-2015



Source: RongViet Research

ROA (%) during 2010-2015



Source: RongViet Research

BRIEF 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% 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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