FPT Digital Retail JSC (HSX: FRT)

Not yet attractive after a deep fall

Particulars (VND B)	1Q-FY19	4Q-FY18	+/- QoQ	1Q-FY18	+/-yoy
Net revenue	4,018	4,266	-6%	3,884	3%
PAT	64	120	-47%	64	1%
EBIT	100	155	-36%	89	13%
EBIT margin	2.5%	3.6%	-115 bps	2.3%	+20 bps

Source: FRT, Rong Viet Securities

1Q 2019 results: Weak due to the Iphone.

1Q 2019 Revenue and NPAT rose a modest 3.5% and 0.5% respectively. Sales from new iPhone models dissapointed, forcing the company to reduce selling prices to clear old stocks. Revenue from the Subsidy program was not good either as negotiations with Vietnamobile and Mobifone have been temporarily suspended.

Since this year, FRT started importing accessories directly from China, enabling the company to sell its products at a price 20% below the old average price yet expand gross profit margins to 50% from 40%. In the first quarter, the company had to clear old accessories (those have high COGS) at the same price as the newly imported accessories, hence, the profit margin was also affected.

2019: Modest growth in the ICT segment while the pharmacy model is being optimized

Although Apple introduced supportive policies for retailers in Q2, FRT's ICT segment is set to grow at a slower pace this year, +10% YoY. Gross margins are expected to decrease by 30 basis points to 13.1% while net margins should be maintained at 2.3% in 2019. SG&A expense growth fell as FRT spent a lot on advertising for the Subsidy program in 1Q 2018.

2019 is the pivotal year for Long Chau pharmacy chain. Priority is to optimize its product portfolio and logistics to expand outside of HCMC. Since Long Chau is still in the process of completing its business model, it is not expected to break even this year.

Valuation and recommendation:

Weak 4Q 2018 and 1Q 2019 business results reflect the less positive outlook for the ICT market. Special installment programs, accessory sales and collaboration with Nguyen Kim and Fado have not shown promising results yet or are still in the testing phase.

We adjusted the forecasted P/E of FPT Shop from 12x to 8x. Meanwhile, Long Chau pharmacity is a long-term story. Although we appreciate FRT's approach, it remains challenging to expand the chain rapidly given fierce competition. We estimate Long Chau's value at around VND 5,000 / share (down from VND 8,500 per share in the previous report). Rising costs associated with the expansion, result in a net loss for this business. Long Chau is estimated to reach break-even by 2020.

*Our target price for FRT is **50,000 VND / share**. We have a **NEUTRAL** recommendation on the stock.*

NEUTRAL +2%

CMP (VND)	50,000
Target price (VND)	50,000
Cash dividend (VND)*	1,000

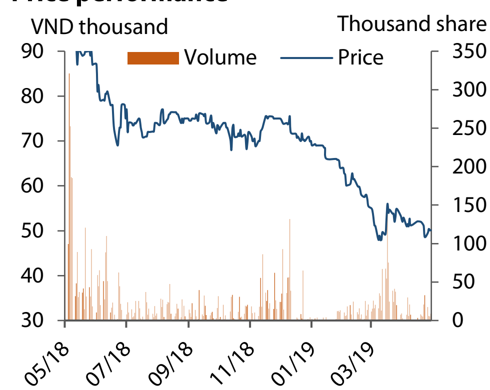
** Expected in the next 12 months*

Stock info

Sector	Retail
Market Cap (VND billion)	3,413
Current Shares O/S	68.7
Avg. Daily Volume (in 20 sessions)	0.73
Free float (%)	45.0
52 weeks High	93,600
52 weeks Low	47,900
Beta	10,112

	FY2018	Current
EPS	5,101	5,119
EPS growth (%)	+20.0	+0.4
Adjusted EPS	5,114	5,119
P/E	14.5	9.5
P/B	4.2	2.4
EV/EBITDA	11.6	10.7
Cash dividend	2.8	2.0
ROE (%)	30.7	32.0

Price performance



Major Shareholders (%)

FPT JSC	47
Dragon Capital	20
VinaCapital	15
Foreign limit room (%)	49

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Exhibit 1: 1Q 2019 results

Particulars (VND B)	1Q-FY19	4Q-FY18	+/-(qoq)	1Q-FY18	+/-(yoy)
Net revenue	4,018	4,266	-5.8%	3,884	3.4%
Gross profit	479	563	-14.8%	488	-1.9%
SG&A	247	190	30.4%	214	15.5%
Operating income	232	373	-37.8%	274	-15.4%
EBITDA	100	155	-35.4%	89	12.5%
EBIT	100	155	-35.6%	89	12.6%
Financial expenses	35	29	18.4%	26	34.9%
- Interest Expenses	32	28	14.0%	22	44.0%
Dep. and amortization					
Non-recurring items (*)					
Extraordinary items (*)					
PBT	80	151	-46.6%	80	0.6%
PAT	64	120	-46.5%	64	0.8%
(*) Adjusted PAT	64	120	-46.5%	64	0.8%

Source: FRT, Rong Viet Securities

Exhibit 2: 1Q 2019 performance analysis

Particulars	1Q-FY19	4Q-FY18	+/-(qoq)	1Q-FY18	+/-(yoy)
Profitability ratios (%)					
Gross margin	11.9	13.2	-130 bps	12.6	-60 bps
EBITDA margin	2.5	3.6	-110 bps	2.3	+20 bps
EBIT margin	2.5	3.6	-110 bps	2.3	+20 bps
Net margin	1.6	2.8	-120 bps	1.6	+0.0 bps
Adjusted net margin					
Turnover (x)					
-Inventories	5.8	6.9	-1.1	7.5	-1.7
-Receivables	12.5	15.8	-3.3	16.7	-4.1
-Payables	11.3	11.9	-0.6	10.1	1.2
Leverage (%)					
Total debt/ equity	284.8	362.1	-7,730 bps	378.8	-9,400 bps

Source: FR, Rong Viet Securities

Exhibit 3: 2Q 2019 performance forecast

Particulars (VND B)	2Q-FY19	+/- qoq	+/- yoy
Revenue	3.955	-2%	11%
Gross profit	526	10%	6%
EBIT	116	16%	1%
NPAT	75	17%	-9%

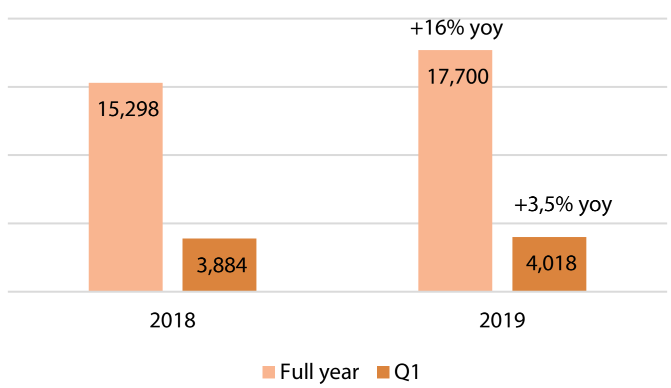
Source: Rong Viet Securities.

Update

The mobile phone market dropped 8% YoY in value in 1Q 2019, according to GFK. FRT's phone revenue in Dec 2018 and 1Q 2019 was strongly impacted by low sales of new iPhone models launched in late 2018. The company had to reduce selling prices significantly to clear iPhone inventory, reducing iPhone gross margins by 1.5%. iPhones accounted for 36% of phone sales in Q1 and FRT's gross margin decreased 70 basis points YoY to 11.9% in 1Q 2019. Because the company spent big on Subsidry program advertising in 1Q 2018, SG&A expenses dropped by 80 basis points to 1.6%/revenue.

Since April, Apple has started to support retailers by reducing prices for old models such as iPhone 7 and iPhone 8. Therefore, business results in April improved with revenue and profit before tax up 31% and 44% YoY respectively. We expect the phone segment to recover in the rest of this year thanks to improved gross margins on iPhone, Samsung and Oppo products. The latter two have significant market share in Vietnam and will both launch key products from Q2 onwards. By the end of 1Q 2019, FRT opened eight FPT Shops and achieved SSSG of 1%.

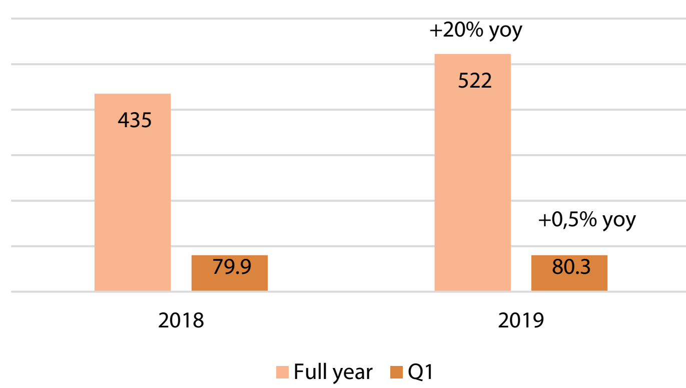
Figure 1: Revenue (VND bn)



Sources: FRT, Rong Viet Securities

**2019's full year revenue is FRT's target*

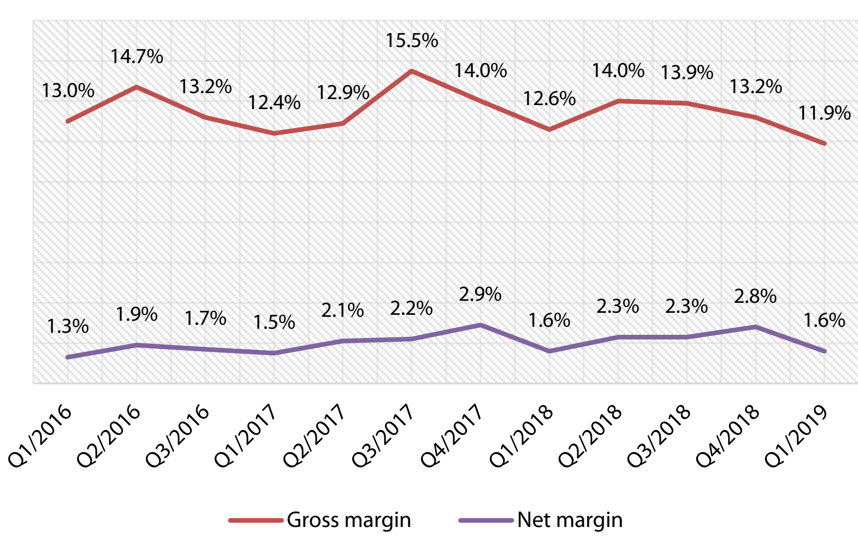
Figure 2: Profit before tax (VND bn)



Sources: FRT, Rong Viet Securities

***2019's full year PBT is FRT's target*

Figure 3: Gross margin and net margin by quarter



Sources: FRT, Rong Viet Securities

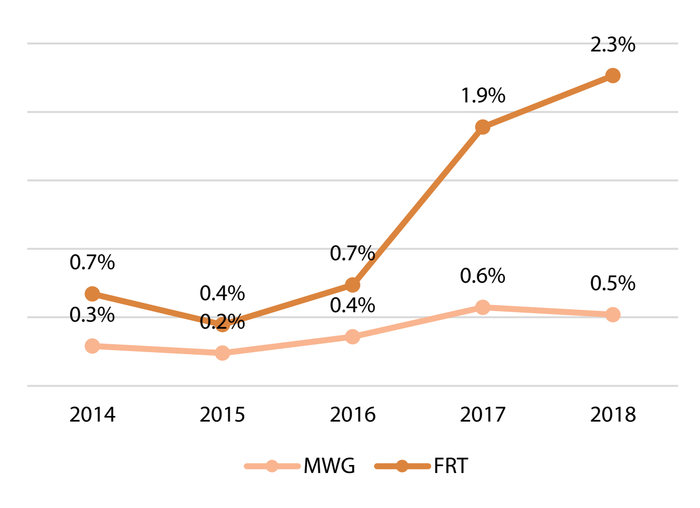
The Subsidy and F.Friends progams

The Subsidy program with Vietnamobile and Mobifone has yet to convince customers that feel uncomfortable changing their phone number. However, this should be temporary, the new policy of the Ministry of Information and Communication at the end of 2018 allows subscribers to switch networks without having to change phone number. Telecom companies however, still try to make it difficult for users to switch. FRT also that since there are still many terms that had not been able to negotiate and agree upon with Vietnamobile and Mobifone, they have not signed new packages for Subsidy. Thus, we can expect this program to slow down in this year.

FRT will focus on promoting F.Friends program more this year, which grew from 2,000 businesses with 650,000 members (mid-2018) to 2,500 businesses with 1 million members by the end of last year. FRT will expand its customer base from manufacturing enterprises to service companies, where workers have higher income and often use high-end products. At the same time, the company is also developing customer credit rating software based on the database of the credit information center (CIC) of the State Bank of Vietnam and sales history of FRT. We will update on effectiveness of these initiatives in the upcoming reports. In Q1, the two programs mentioned above only grew 3% YoY, contributing just 10% to total revenue (our previous forecast for 2019 was 13%).

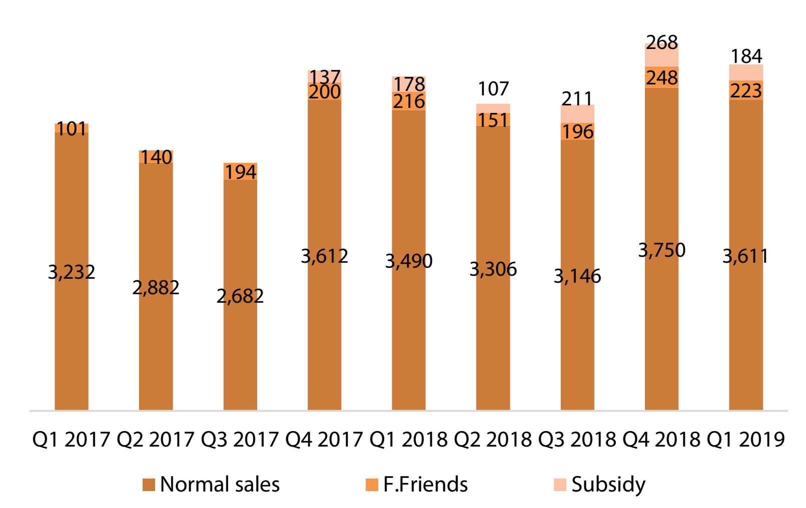
We believe both F.Friends (from 2017) and Subsidy (from 2018) have supported FRT to maintain SSSG around 1-3% in the past two years, similar to MWG and good considering FRT's ICT sector is more dependent on the saturated high-end phone segment.

Figure 4: Average trade account receivable of MWG and FRT



Sources: MWG, FRT, Rong Viet Securities

Figure 5: FRT's revenue breakdown



Sources: FRT, Rong Viet Securities

Collaboration with Nguyen Kim and Fado is a part of FRT's attempt to increase existing store sales. Nguyen Kim's electronic products will be available on FPT Shop's website. FRT's website also has a separate section for online-purchased goods from Amazon, in collaboration with Fado - a cross-border shipping/trading business. Since this is only in the testing phase, FRT only gets a tiny commission. If however the results are positive, the scope of collaboration could expand to FPT Shop stores. However, given high and increasing competition in the electronics industry and cross-border commerce, we believe that even if FRT could convert additional traffic into its ICT revenue, the contribution from this collaboration to the business result would be limited.

Long Chau pharmacy chain opened 6 new stores in 1Q 2019, bringing the total number to 28. Total revenue was VND 53 bn, and SSSG of stores open longer than 18 months reached 6%. Note however that consolidated revenue from Long Chau is only VND 37 Bn as there are still approximately 10 stores that have not been converted from family business to corporation yet.

Thanks to a new inventory management system, the cost of overdue products in Long Chau decreased from VND 100 mn / month to VND 10-20 mn / month after being acquired by FRT. Long Chau also expanded to other provinces, including 2 stores in Dong Nai and 1 store in Tien Giang. Competing in price is still the key for Long Chau, especially in the provincial markets. Long Chau does not apply a same price policy and sells at cheaper prices in provinces where people have lower average incomes. We think that this is an appropriate strategy given its main competitors are mom-and-pop pharmacies whose prices are very competitive. In the short-term, this will obviously reduce profit margins.

2019 forecast

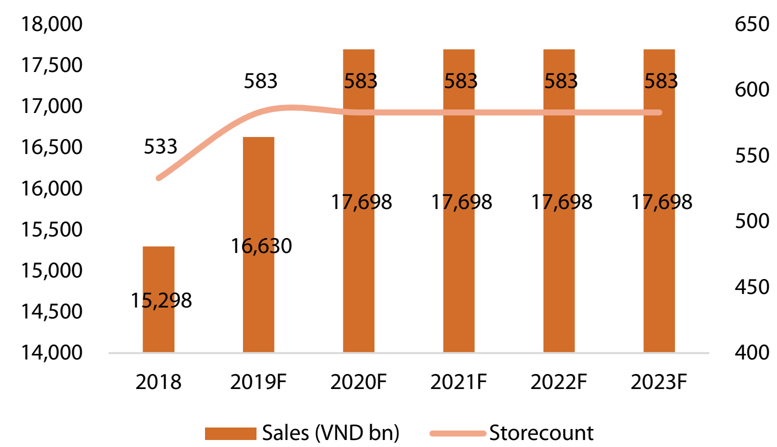
Since the overall phone market is forecasted to decline, we believe that FRT's SSSG will be around 0% -1%. The increased contribution of F.Friends and Subsidy (from 10% to 12%) and accessory sales can help total revenue increase 10% YoY. The ICT segment's profit margin is likely to contract with 30 basis points to 13.1% in 2019.

FRT is likely to accelerate its store expansion from 2Q 2019 onwards and open 50 new stores in 2019, lower than the initial target of 100.

The iPhone market in Vietnam is still struggling and currently FRT has no plans to expand its iPhone retail chain. Only one new **F.Studio** opened in 2018. Temporarily, we consider F.Studio as a part of FPT Shop and will follow up on any new developments.

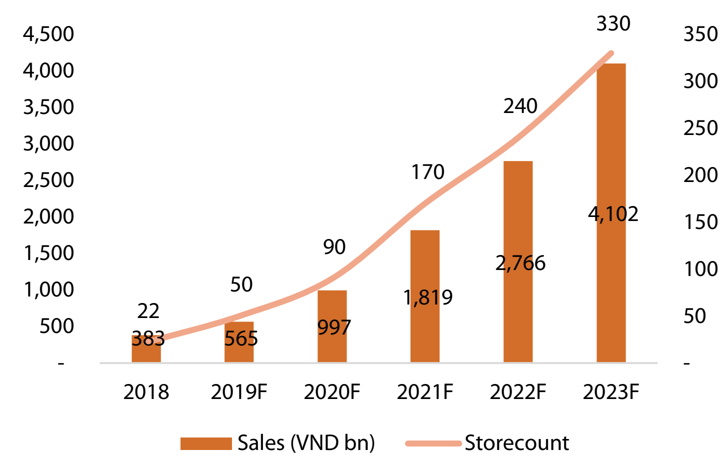
Long Chau will open 28 new stores in 2019, bringing the total number of stores to 50. FRT continues to focus on Ho Chi Minh City and the company will need time to optimize its product portfolio and price policies before expanding to other provinces. We estimate that Long Chau will not be able to reach breakeven this year, with a net profit margin of -3% for the whole year.

Figure 6: Forecast on FPT Shop's result (including F.Studio)



Sources: FRT, Rong Viet Securities

Figure 7: Forecast on Long Chau's result



Sources: FRT, Rong Viet Securities

VND in billions

Income statement	FY2017	FY2018	FY2019F	FY2020F
Revenue	13,147	15,298	17,195	18,695
COGS	11,330	13,255	14,905	16,095
Gross profit	**1,816**	**2,044**	**2,290**	**2,600**
Selling expense	1,154	1,225	1,432	1,601
G&A expense	300	358	355	429
Finance income	54	43	66	79
Finance expense	82	101	135	133
Other profits	29	32	32	32
PBT	**363**	**435**	**466**	**548**
Prov. of tax	73	87	93	110
Minority's interest	0	0	0	0
PAT to equity S/H	**290**	**348**	**373**	**439**
EBIT	362	460	503	570

%

Financial ratio	FY2017	FY2018	FY2019F	FY2020F
Growth (%)				
Revenue	21.1%	16.4%	12.4%	8.7%
Operating income	56.7%	27.0%	10.1%	13.4%
EBITDA	57.4%	27.2%	9.2%	13.4%
PAT	39.7%	20.0%	7.3%	17.6%
Total assets	-17.8%	38.3%	20.6%	8.9%
Equity	54.6%	42.4%	27.3%	25.8%
Profitability (%)				
Gross margin	13.8%	13.4%	13.3%	13.9%
EBITDA margin	2.8%	3.0%	3.0%	3.1%
EBIT margin	2.8%	3.0%	2.9%	3.1%
Net margin	2.2%	2.3%	2.2%	2.3%
ROA	7.5%	6.5%	5.8%	6.2%
ROE	36.4%	30.7%	25.9%	24.2%
Efficiency (x)				
Receivable turnover	12.9	12.0	13.0	11.8
Inventory turnover	6.6	5.3	5.7	5.7
Payable turnover	6.0	10.7	7.0	7.0
Liquidity (x)				
Current	1.1	1.2	1.2	1.3
Quick	0.6	0.6	0.7	0.7
Solvency (%)				
Total debt/equity	147.3%	260.0%	197.9%	157.6%
Current debt/equity	147.3%	260.0%	197.9%	157.6%
Long-term Debt/equity	0.0%	0.0%	0.0%	0.0%

VND in billions

Balance sheet	FY2017	FY2018	FY2019F	FY2020F
Cash and cash equivalents	638	1,069	1,913	1,940
Short-term investments	0	4	4	4
Accounts receivable	1,016	1,274	1,320	1,581
Inventories	1,723	2,506	2,594	2,841
Other current assets	131	150	157	165
Property, plant & equipment	5	5	5	4
Acquired intangible assets	41	40	36	31
Long-term investments	0	0	0	0
Other non-current assets	316	307	432	467
Total assets	**3,871**	**5,355**	**6,460**	**7,034**
Accounts payable	1,890	1,236	2,114	2,302
Short-term borrowings	1,173	2,947	2,856	2,861
Long-term borrowings	0	0	0	0
Other non-current liabilities	0	0	0	0
Bonus and welfare fund	12	12	21	30
Technology-science, dev. fund	0	0	0	0
Total liabilities	**3,075**	**4,196**	**4,992**	**5,193**
Common stock and APIC	400	680	694	707
Treasury stock (enter as -)	0	0	0	0
Retained earnings	396	454	750	1,108
Other comprehensive income	0	0	0	0
Inv. and dev. fund	0	0	0	0
Total equity	**796**	**1,134**	**1,443**	**1,815**
Minority interest	**0**	**25**	**25**	**25**

Valuation ratio	FY2017	FY2018	FY2019F	FY2020F
EPS (VND)	4,263	5,114	5,254	6,070
P/E (x)	N/A	14.5	9.5	8.2
BV (VND)	19,911	16,673	20,807	25,661
P/B (x)	N/A	4.2	2.4	1.9
DPS (VND/cp)	2,000	2,000	1,000	1,000
Dividend yield	N/A	2.8	2.0	2.0

Valuation model	*Price*	*Weight*	*Average*
FPT Shop			45,000
Long Chau			5,000
Target price (VND)			**50,000**

Valuation history	*Price*	*Recommendation*	*Period*
07/2018	84,000	Accumulate	1 year
05/2019	50,000	Neutral	1 year

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

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