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Positive growth potential owing to capacity expansion

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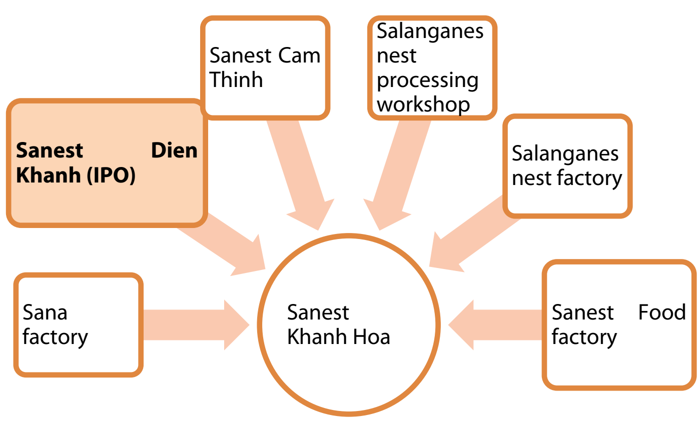
Company overview

Dien Khanh Sanest one-member company Limited (Sanest Dien Khanh) is a subsidiary under **Khanh Hoa Salanganes Nest Company**. The company was formerly known as High-end Beverage Sanest Dien Khanh factory, a 5 million products/year factory which went into operation in 2003. The capacity then has been increased and in 2013, the operating capacity was upgraded to 50 million products per year. On December 2014, the factory's name was changed to the current one.

Khanh Hoa Salanganes Nest Company (**Sanest Khanh Hoa)** is a 100% State owned enterprise which was established in 1990 and has the main business in manufacturing salanganes nest. This product of bird's nest contains rich nutrients and has contributed high economic value to South Central provinces in general and Khanh Hoa province in particular. Currently, the parent company has nationwide sales system, branches and convenience stores which include branches in three major cities: Ho Chi Minh, Ha Noi and Da Nang. Moreover, its main export markets include US, Australia, Canada, Japan, Korea and Cambodia.

After many years operating in edible bird's nest industry and having experienced Research and development teams, Sanest Khanh Hoa relatively has a wider range of products in comparison with its competitors. Its category includes dried birdnests, Sanest Collagen, canned Sanest, high-end sanest biscuit, bottled birdnests, which meet the varied demands and tastes.

Figure 1: Khanh Hoa Salanganes nest company's members



Source: RongViet Research

Figure 2: Sanest Khanh Hoa 's products

Source: Sanest Khanh Hoa

Sanest Khanh Hoa currently has two in-operation salanganes nest factories including Sanest Dien Khanh and Sanest Cam Thinh, both located in Khanh Hoa province. The latter was built in 2011 with the capacity of 30,000 units per hour. At the end of 2015, operating capacity of Sanest Dien Khanh was 70 million units/year and of Sanest Cam Thinh was 50 million units/year. Two factories have the same product lines, which are bottle birdnest (only producing in Sanest Dien Khanh), canned birdnests and high quality bottle birdnest.

Table 1: Total capacity

Capacity (mil units/year)	2004	2011	2014	2015
Dien Khanh	5	45	55	74
Cam Thinh		30	50	50
Total	5	75	105	124

Source: RongViet Research estimates

With years of experience in salanganes nest industry, Sanest Khanh Hoa has developed large areas for raw material, which have been not only within Khanh Hoa province (which has 169 nest caves and 32 nest islands) but also in other South Central provinces such as Phu Yen, Ninh Thuan, Quang Binh, Quang Ngai, Con Dao islands, etc. In 2015, the company harvested 3.4 tons of salanganes nest, which is 76% higher compared to 1990. With over 1000 distributors and distribution agents nationwide, we highly value the Sanest brand that the parent company has been building. In addition, the advantage from input materials with natural nest islands plays an important role for the company's product positioning in the nutrient food market. After Sanest Dien Khanh, other four subsidiaries of Sanest Khanh Hoa will conduct equitization plan. The parent company also has plan to equitize but the schedule has not been announced.

Regarding of Sanest Dien Khanh, being a subsidiary of Sanest Khanh Hoa helps Sanest Dien Khanh to stabilise its supply and therefore, input prices. Besides, via a large distribution network possessed by the parent company, Sanest Dien Khanh's products have a stable consumption potential.

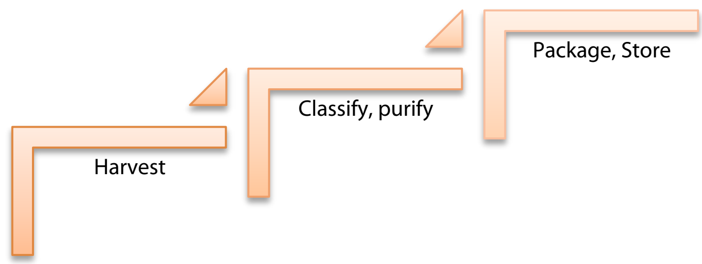
However, being a part of the value chain (producer, particularly "packager"), Sanest has little room for radical strategy changes, which mostly are growth and expense cut. Moreover, greate dependence on the holding company in terms of both input and output may lead to conflicts of interest between major and minor shareholders.

Salanganes Nest Industry Overview

Salanganes Nest Industry which provides nutrient-rich and expensive products, is valued at USD5 bn. The major consumer markets locate in East Asia, South East Asia and the US. Salanganes nest is mainly produced in ASEAN countries like Indonesia, Thailand, Vietnam, Singapore, Malaysia and Hainan island (a province of People's Republic of China). Indonesia and Malaysia are the two largest suppliers, currently account for 70% and 20% of total global supply respectively.

The salanganes nest harvesting process is highly manual from harvesting to classifying to purifying stage. As a result, the products require a large amount of time and effort. Additionally, costs of raw materials and labour account for over 90% cost of a completed bird's nest manufacturing process.

Figure 3: Salanganes nest processing from natural bird's nest



Source: RongViet Research

Vietnam has entered this market for about 10 years. The quality of Vietnamese products are highly rated but the quantity is relatively low, at 10 tons/year in comparison with 100 tons/year of the Indonesian's and 60-70 tons/year of the Malaysian's and Thailand's.

In term of domestic demand, the continuous improvement in Vietnamese well-being has boosted the growth of nutrient-rich product demand. From 2014 to 2015, the positive economic outcome alongs with the stable CPI were the strong base for the growth of the nutrient-rich industry. According to BMI, the industry recorded a 12% growth in 2015, equivalent to VND 26,7 bn. During the 2015-2020 period, it is anticipated that the nutrient industry will maintain the 10% yearly average growth and reach VND 42,2 bn in sales in 2020.

According to the Ministry of Planning and Investment, Vietnamese income per capita will grow to approximately USD 3,200–3,500 in 2020 from USD 2,109 in 2015. As a consequence, the higher the income, the more money people willing to spend on nutrient products. Thus, it is reasonable for companies in this industry to invest in reasearch and expanding their business lines in the upcoming years.

However, the market share is segmented by both domestic and foreign firms. The rising competition not only comes from the increasingly investing nest house of the former but also imported products from the latter. On this occasion, we expect that leading player like Sanest Khanh Hoa can maintain its growth rate by pushing advertisement, expanding factories and distribution system.

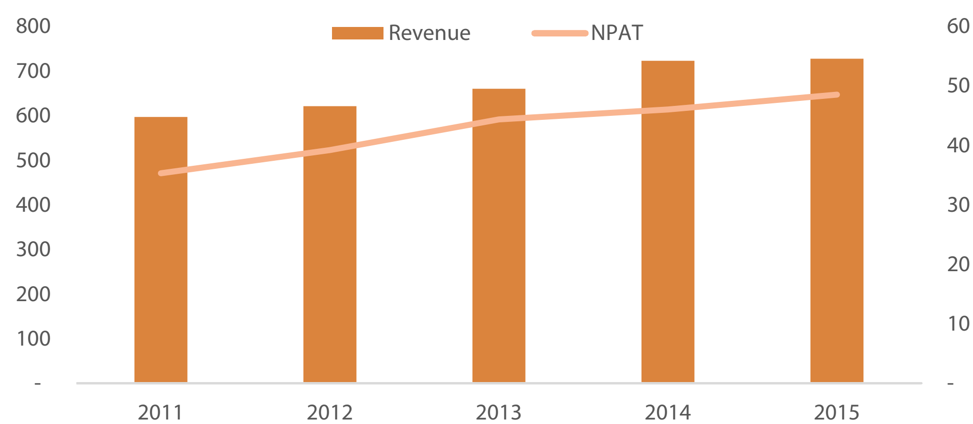
2015 earnings: Stable performance, positive production volume growth

Because Sanest Dien Khanh's input and output depend heavily on the parent company, its earning result remains relatively stable. In the 2011-2014, revenue and NPAT recorded an average growth of 7% and 9% respectively which mainly came from the ability to expand the capacity.

In 2014, the operating capacity achieved 55 million units/year. It was up to 70-75 million units/year in 2015, improved by 30% yoy. Since 2015, the company's accounting method has been independent with its parent company, thus the recording method for output prices has been changed. According to our estimates, revenue could grow at the equivalent rate with volume growth in 2015 if the accounting method remains unchanged.

Regarding the financial performance, the company is currently not ultilizing debt, which subsequently minimize any risk of interest rate volatility.

Figure 4: 2011-2015 earnings results



Source: Sanest Dien Khanh's financial reports, RongViet Research

Positive growth potential owing to capacity expansion

During 2016-2018, the Company targets to achieve 1% in average annual growth rate regarding revenue and 2% for profit after tax. We believe that the plan for 2016-2018 is relatively conservative as it has many favorable hints for expansion capacity. Firstly, investing in new production line or expanding the production are simple with low investment cost. Meanwhile, input materials will be ample in the upcoming years as Sanest Khanh Hoa is continuously developing raw material areas. Thus, in case Sanest Dien Khanh increases capacity, the raw material will be sufficient.

In terms of output, as mentioned in **Salanganes Nest Industry Overview,** we believe the demand for Salangenes nest remain high as high consumption increases in quality products.

In the equitisation plan, Dien Khanh Sanest plans to sublease the land of Khanh Hoa JSC with an area of 5,200 m2, located next to the current plant. However, the Company has not mentioned any information related to capacity increasing in the equitisation plan. However, we believe that the Sanest Dien Khanh would likely to expand its capacity without any restriction in business area.

Table 2: 2015-2018 target plan

	2015P	2015A	2016	2017	2018
Revenue	715	727	720	725	730
NPAT	46	49	47	48	49
Dividend/Charter capity	13%	13%	14%	16%	16%

Source: Sanest Dien Khanh's prospectus

With strong relationship with the parent company, Sanest Dien Khanh is ensured about the raw material for production expansion. However, depending on the holding company in terms of both input and output may lead to little room for radical strategic changes. In the 2015-2017, it is estimated that Sanest Dien Khanh will record a VND 15bn for trademark fee, equivalent to 2% of annual revenue. This rate is relatively the same as other competitors. In the long run, there will be higher risk regarding of rising trademark expense between the company and holding company.

Furthermore, after equitisation, we expect the transpency improvement in terms of expenses between Sanest Dien Khanh and Sanest Khanh Hoa. Raw material expenses currently account for 80% of total cost. Meanwhile, due to lack of information relating to the calculation method for the cost of raw materials, we cannot provide any further momments about the ability to save cost of Sanest Dien Khanh. However, in the past, many companies can efficiently and effectively cut costs under the supervision of new shareholders after equitization.

Risk

For business activities of Sanest Dien Khanh, we provide three most notable risks. First issue is the risk that market demand would record a slower growth. Vietnam's economy is forecasted to experience a positive outlook, however, the majority of people's income level have not really improved. Therefore, demand for nutritional products may witness a slower growth.

In addition, Vietnam's participation in several free trade agreements will facilitate imported products, especially from Indonesia and Malaysia - two bird nests producers, thereby causing competitive pressure on domestic producers such as Sanest Dien Khanh.

Regarding internal risks, we believe that strong dependence on both input and output may lead to little room for radical strategy change as well as conflicts of interest between major and minor shareholders.

Valuation

Salanganes nest production has been an attractive industry which is heavily localised where the products as a specialty are nutritious, which means a great growth potential. Thus, equitisation of such companies can be a catalyst for the Vietnamese stock market in 2016.

During 2016-2018, the Company targeted to achieve 1% in average annual growth regarding revenue and 2% for profit after tax. We believe that the plan for 2016-2018 is relatively reckless. After evaluating and analyzing the future prospects of Sanest Dien Khanh, RongViet Research supposes that Company's growth potential is positive in the coming years thanks to the factory expansion. In addition, the transparency in cost structure between parent company and Sanest Dien Khanh is expected to improve after the equitisation.

Under the most optimistic scenario, revenue and profit after tax for 2016 could reach VND **844** bn and VND **59** bn respectively, improved by 15% yoy and 22% yoy. 2016 EPS will be equivalent to VND **2,563**/share. Growth in revenue mostly comes from the increase in factory capacity by an addition of 11 million products/year. Furthermore, if Sanest Dien Khanh could efficiently cut costs as we assume, profit growth rate could improve and surpass the revenue growth rate, approximated at 12 – 15%/year.

Using P/E of the businesses in the food and beverage industry along with the potential growth of the firm as well as discounted room, we believe the reasonable price of Sanest Dien Khanh is in the range of **26,000-30,000** VND per share. This price matches with P/E of 10 – 11.7 times.

Based on the initial price of **23,000 VND per share**, we recommend **BUY** for Sanest Dien Khanh.

Table 3: Average Vietnamese Food and beverage P/E

Ticker	Market capital (mil VND)	P/E
HNG VN Equity	6,520,723	8.3
SBT VN Equity	6,000,089	17.4
DBC VN Equity	2,770,670	10.7
BHS VN Equity	2,294,198	9.4
BBC VN Equity	1,118,007	14.5
NAF VN Equity	834,000	15.9
SLS VN Equity	758,880	6.6
FMC VN Equity	723,000	6.2
VDL VN Equity	460,835	19.0
SAF VN Equity	371,361	10.0
SPM VN Equity	271,269	11.4
KTS VN Equity	273,273	5.9
LAF VN Equity	203,247	7.8
HNM VN Equity	166,000	38.8
SJ1 VN Equity	141,718	8.6
Average		**12.0**

Source: Bloomberg, @June 20th, 2016, RongViet Research

Equitization process

In this equitization, the firm offers 11 million shares including 5 million for common investors, 4.71 million for strategic investors and the remaining for employees. On May 25th 2016, Nha Trang commercial tourism joint stock company was appointed by Khanh Hoa Provincial People's Committee to be a strategic investor of Sanest Dien Khanh. The firm is also a subsidiary under Sanest Khanh Hoa. Besides, after the equitization process take place, the current name which is "Salanganes Nest high-end beverage Dien Khanh one member limited company" will be changed to "Khanh Hoa Salanganes Nest beverage joint stock company".

The equitization of Sanest Dien Khanh and other subsidiaries of Sanest Khanh Hoa is a part of Khanh Hoa Provincial People's Committee's SOE-equitization-scheduke. In the second quarter of 2016, Khanh Hoa Department of Planning and Investment will conduct equitization plan that the State will reduce its stake to 51% in the following SOEs: East Cam Thinh Salanganes Nest high-end beverage factory, Sanna beverage factory, Sanest Tourist and Design and Building Nest house factory Sanatech. According to Circular No.180/2015 of Ministry of Finance, 30 days after the public company register letter approved by State Securities Commission in the term of decree No. 58/2012/ND-CP, Sanest Dien Khanh can be listed on Upcom. We anticipate that the Sanest Dien Khanh will be listed on Upcom **in the beginning of 2017.**

Unit: bil VND

INCOME STATEMENT	FY2014	FY2015	FY2016F	FY2017F
Revenue	713	727	844	902
COGS	(459)	(632)	(733)	(784)
Gross profit	254	96	111	118
Selling Expense	(159)	(28)	(31)	(33)
G&A Expense	(19)	(6)	(6)	(6)
Finance Income	(17)	0	0	0
Finance Expense	(16)	0	0	0
Other profits	0	0	0	0
PBT	59	62	74	79
Prov. of Tax	358	337	(15)	(16)
Minority's Interest	0	0	0	0
NPAT	46	49	59	63
EBIT	76	62	74	79
EBITDA	76	62	74	79

Unit: bil VND

BALANCE SHEET	FY2014	FY2015	FY2016F	FY2017F
Total Current Asset	74	158	187	192
Receivables	0	111	115	120
Inventories	74	45	50	50
Other current assets	0	2	2	2
Long-term Asset	63	152	154	160
Tangible Fixed Assets	16	26	30	40
Intangible Fixed Assets	47	127	124	124
Total Asset	137	310*	341	352
Current Debt	17	51	33	13
Long-term Debt	0	0	0	0
Total Liability	137	51	33	13
Owner's Equity	119	259	308	339
TOTAL RESOURCES	137	310	341	352

Unit: %

GROWTH	FY2014	FY2015	FY2016F	FY2017F
Growth	10%	2%	16%	7%
Revenue	14%	-62%	16%	7%
Operating Income	3%	-18%	18%	7%
EBITDA	3%	-18%	18%	7%
EBIT	4%	5%	22%	7%
PAT	21%	127%	10%	3%
PROFITABILITY				
Gross profit/Revenue	36%	13%	13%	13%
Operating profit/ Revenue	11%	9%	9%	9%
EBITDA/ Revenue	11%	9%	9%	9%
Net margin	6%	7%	7%	7%
ROAA	37%	22%	18%	18%
ROIC or RONA	70%	47%	40%	35%
ROAE	39%	19%	19%	19%

**Total asset increased because of revaluation*

EFFICIENCY (x)	FY2014	FY2015	FY2016F	FY2017F
Receivable Turnover	111.8	13.0	7.5	7.7
Inventory Turnover	8.2	10.7	15.5	15.7
Payable Turnover	28.8	19.2	18.0	34.1
LIQUIDITY (x)				
Current	4.2	3.1	5.7	14.8
Quick	0.0	2.2	4.2	10.9

COMPANY REPORT

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.

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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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