STEEL INDUSTRY

INTO THE TROUGH

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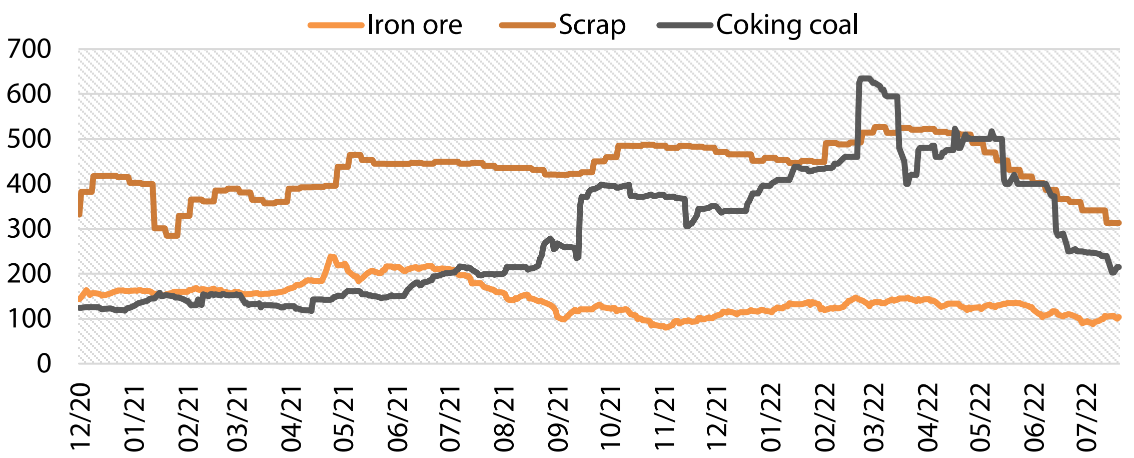
The price of steel and raw materials increased sharply in the wake of the war and then quickly cooled down

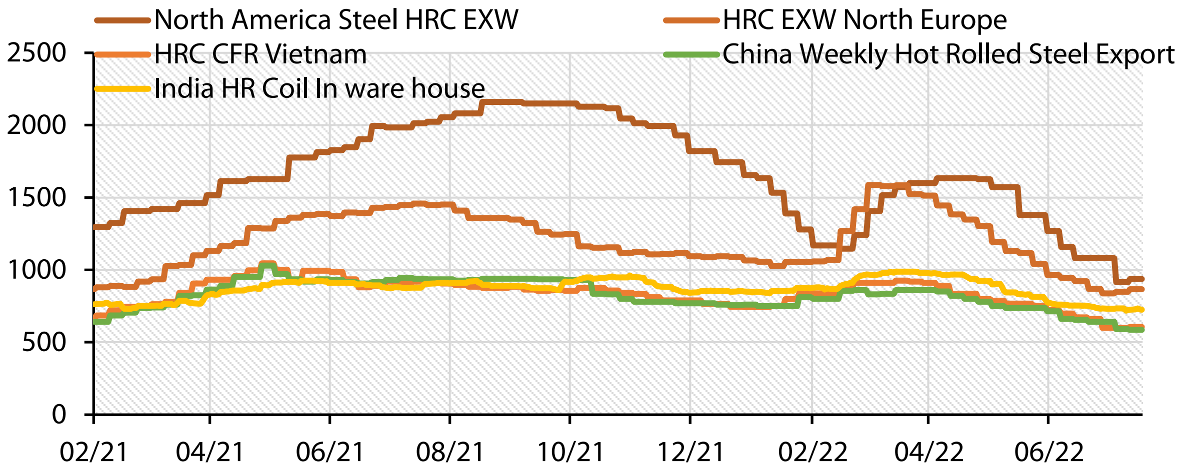
- Panic sentiment over the lack of steel supply pushed steel and raw material prices up in the early stage of the war.
- The fear of economic recession gradually prevailed, causing demand for steel and steelmaking materials to decline and the price reversed rapidly.
- The decline in steel prices is weakening and showing signs of reversing upward thanks to positive news about China's real estate market stimulus measures. However, we believe that the upside momentum in the second half of the year is not much due to high global inflation.

Figure 1: Material prices (USD/ton)



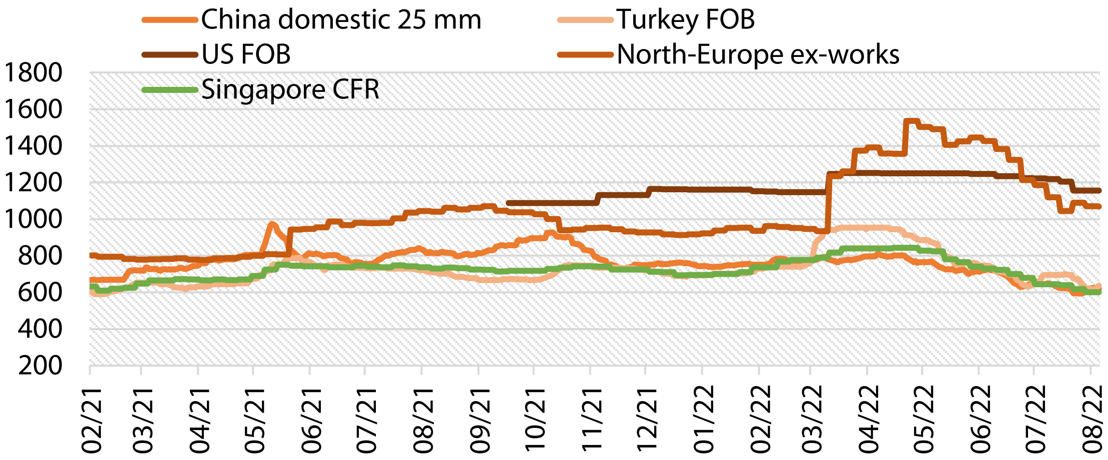
Source: Bloomberg, Rong Viet Securities

Figure 2: HRC price (USD/ton)



Source: Bloomberg, Rong Viet Securities

Figure 3: Rebar price (USD/ton)



Source: Bloomberg, Rong Viet Securities

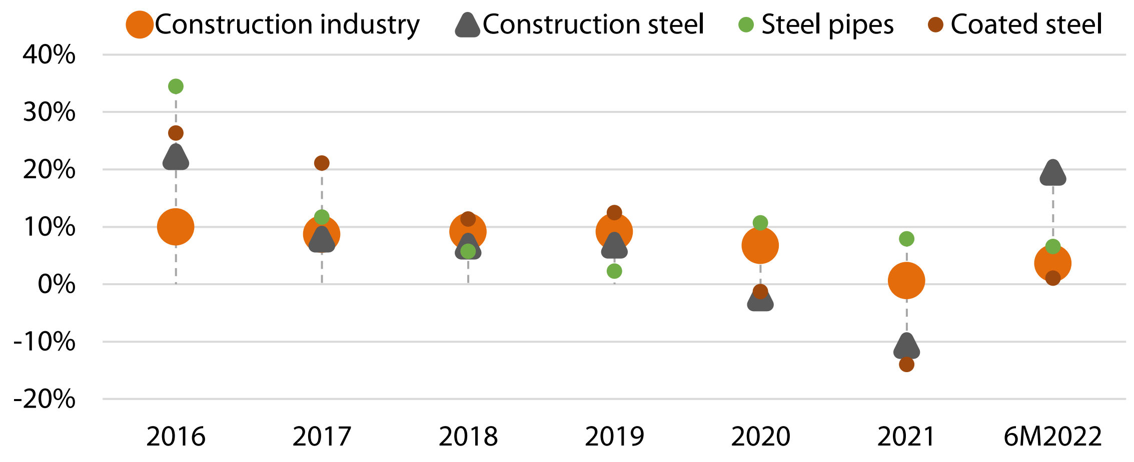
Domestic demand for steel is low due to low cash flows into the real estate market and slow disbursement of public investment.

Steel prices have fallen continuously since the end of April, prompting domestic distributors to find ways to reduce inventories, only buying from manufacturers when they have orders from customers.

The slowing demand from other markets combined with export competition with many countries, including China's low-priced steel, made the export volume of finished steel in 6M2022 only increase slightly by 3.1% to 3.64 million tons.

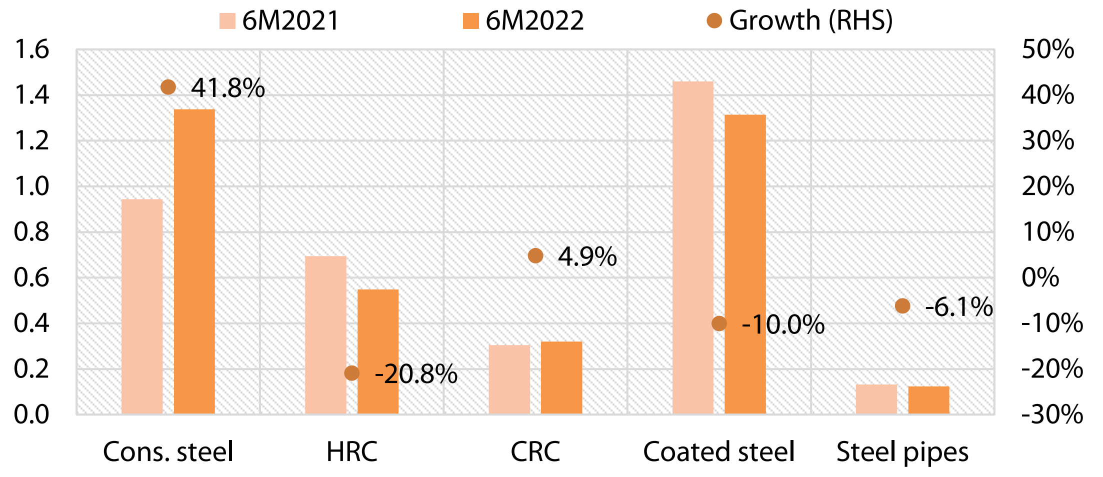
High inventory pressure forced factories to both cut capacity and compete fiercely on selling prices, pulling the price level down continuously.

Figure 4: Growth of steel consumption and construction sector



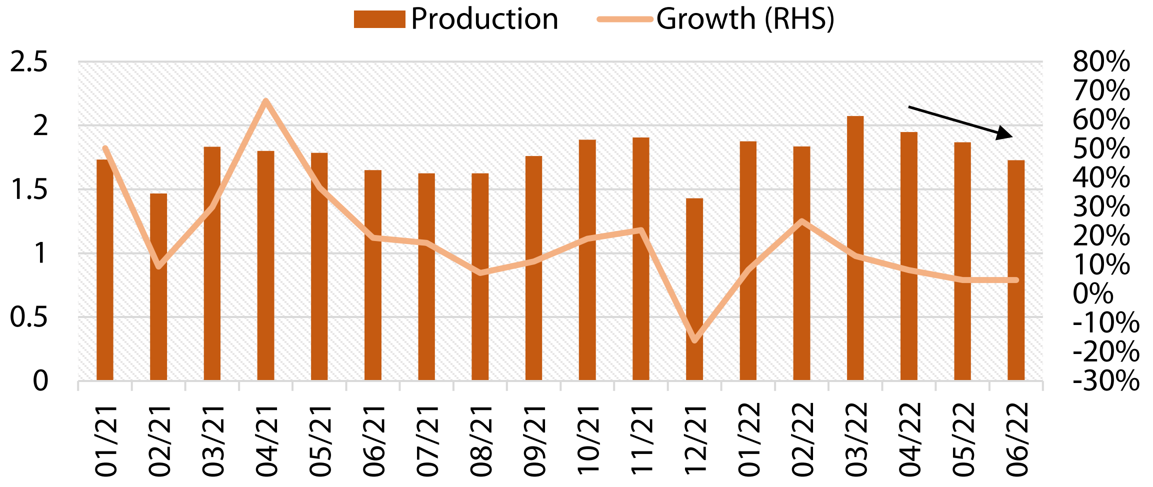
Source: GSO, VSA, Rong Viet Securities

Figure 5: 6M2022 exports by product (million tons)



Source: VSA, Rong Viet Securities

Figure 6: Crude steel output (million tons)



Source: VSA, Rong Viet Securities

RISING CHALLENGES IN COATED STEEL EXPORT

Changes in trade policies of major markets such as the US and EU to be more challenged to Vietnam.

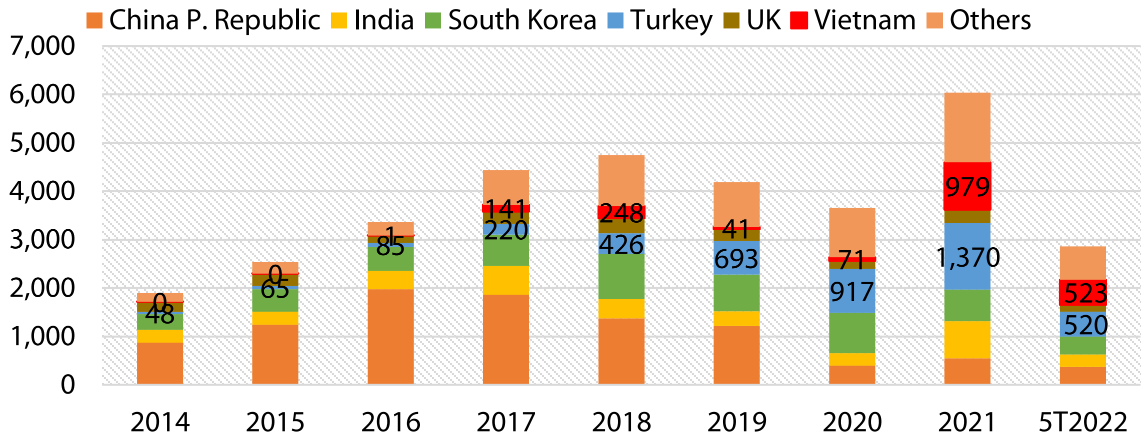
1. The US in late 2021 and early 2022 has relaxed tariff quotas on Japanese, EU and UK steel.

2. The EU reccently increased protection measures on Vietnamese coated steel. From July 1, 2022 to June 30, 2024, Vietnam's metal coated steel sheet (group 4A) is managed under to quotas. The tariff-free quota of the group of "Other countries", including Vietnam, is 1.8 million tons for the period July 1, 2022 to June 30, 2023 and increases by 4% in the following year. If the quota is exceeded, the import tax to be paid for the excess is 25%.

- In 2021, Vietnam sold 979 thousand tons of coated steel to the EU, a sharp increase compared to previous years in terms of supply shortage in the EU combined with quota exemption incentives for Vietnam from July 1, 2020. This was the reason why the EU has increased barriers to Vietnam's coated steel.
- Apart from India, Korea and the United Kingdom who are subjected to separate quotas, Turkey is Vietnam's biggest rival. Turkey has the advantage of transport distance to the EU and steel supply and demand in the EU will be stable in the coming years, it would be difficult for Vietnam to maintain high exports to the EU.

Vietnamese manufacturers will have to increase their exports to ASEAN, to offset the decline in Europe-North America demand, but profit margins will be lower.

Figure 7: EU's imports of steel from third parties ('000 tons)



Source: EUROFER, Rong Viet Securities

Table 1: Newest tariff-free import quotas of EU for galvanized steel (group 4A, thousand tons)

Country	From 7/1/2022 to 6/30/2023	From 7/1/2023 to 6/30/2024
South Korea	143.3	149.0
India	204.8	213.0
UK	135.0	140.4
Other countries	1,802.5	1,874.6

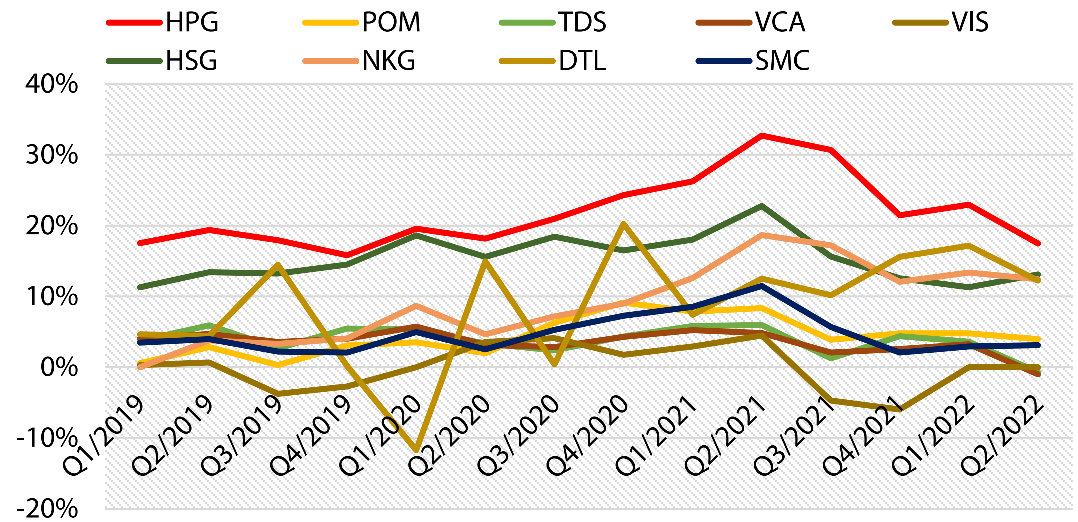
Source: EC, Rong Viet Securities

In the first half of the year, the price of raw materials for steel production fluctuated greatly, bringing difficulties to business of steel companies. Profit margins of steel companies weakened due to lower selling prices, higher provision for inventory devaluation and increased transportation costs, mainly in Q2.

Construction steel demand will soon recover. Vietnam's public investment disbursement will accelerate from the end of 2022 after the public investment plan 2021-2025 completes the approval process. Worldsteel forecasts that the infrastructure investment incentives of the ASEAN 5 countries will underpin the recovery of the region's construction steel demand, with an increase of 4.8% in 2022 and 6.1% in 2023, higher than the corresponding increases in world steel demand of 0.4% in 2022 and 2.2% in 2023.

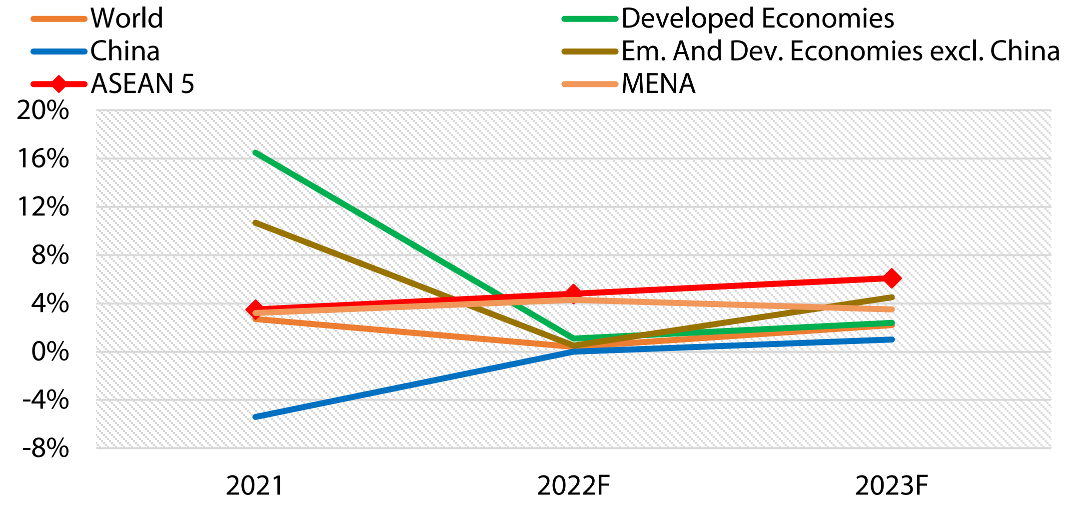
Flat steel demand is expected to remain weak for the next few quarters. Recently, HRC price has continuously decreased, but the domestic price of coated steel has not adjusted significantly thanks to the support from exports. In the coming time, when exports become low, domestic coated steel prices will be under greater pressures due to the loss of support from exports.

Figure 8: Gross profit margin of steel companies



Source: Companies's financial reports, Rong Viet Securities

Figure 9: Forecast of steel demand growth



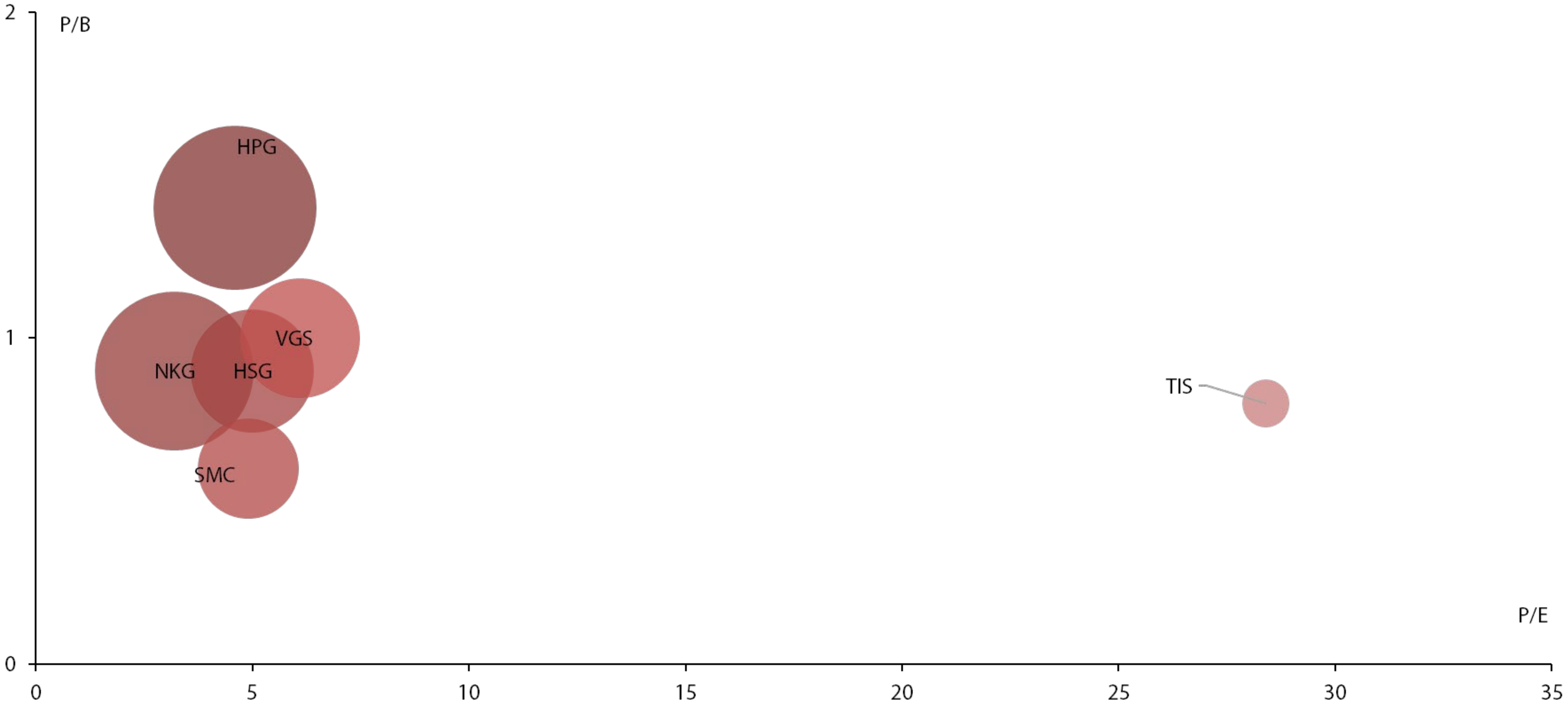
Source: Worldsteel, Rong Viet Securities. ASEAN 5: Indonesia, Malaysia, Philippines, Thailand, Vietnam. MENA: Middle East and North Africa

INDUSTRY COMPARABLE (TTM)

Ticker	Market cap (VND bn)	Target price (VND)	Sales Growth (% YoY)	EBITDA Growth (% YoY)	EBITDA Margin (%)	Operating Income Margin (%)	Net Income Growth (% YoY)	Net Profit Margin (%)	ROA (%)	ROE (%)	DY (%)	Current P/E (x)	Current P/B (x)
HPG	5,940	33,000	41.2	19.2	24.8	20.8	19.5	18.2	16.4	31.8	1.6	5.0	1.4
NKG	243	25,100	64.3	21.7	8.6	7.3	26.0	5.8	11.7	33.0	3.9	3.0	0.9
HSG	447	N/A	39.5	-35.2	0.0	0.0	-45.6	3.6	8.6	19.3	0.0	5.0	0.9
SMC	63	N/A	19.9	-53.7	2.5	2.1	-68.6	1.3	2.9	13.0	4.2	4.7	0.5
VGS	38	N/A	4.0	-2.3	2.6	2.4	2.3	2.0	6.0	17.3	0.0	6.1	1.0
TVN	265	N/A	-13.4	-46.0	10.1	5.7	-64.6	4.5	6.2	9.0	0.0	8.7	0.6

Source: Fiinpro, Rong Viet Securities. Share price as of August 10, 2022.

PE, PB & ROE (TTM)

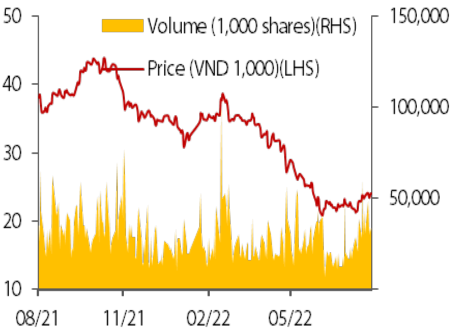


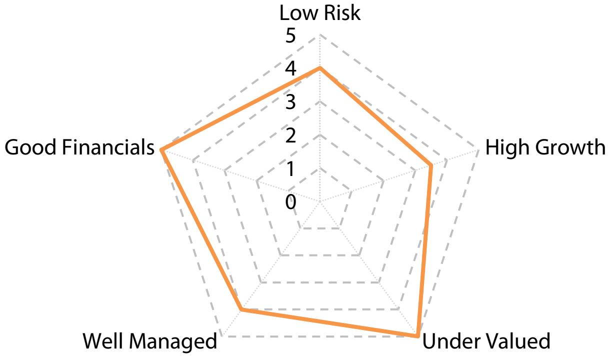
Source: FiinGroup, Rong Viet Securities. Bubble size equals respective ROE. Share price as of 10 August 2022.

GLOOMY OUTLOOK DUE TO GLOBAL INFLATION

HSX: HPG

<BUY: 39%> **<MP: 23,800>** **<TP: 33,000>**





STOCK INFO

Sector	Basic Materials
Market Cap ($ mn)	5,918
Current Shares O/S (mn shares)	5,815
3M Avg. Volume (K)	26,309
3M Avg. Trading Value ($ mn)	634
Remaining foreign room (%)	28.8
52-week range ('000 VND)	20.5 - 44.9

FINANCIALS

FINANCIALS	2021A	2022F	2023F
Revenue (VND bn)	149,680	139,687	166,275
NPATMI VND bn)	34,478	24,323	32,858
ROA (%)	19.5	12.5	14.9
ROE (%)	38.0	23.3	30.3
EPS (VND)	7,246	4,494	6,071
Book Value (VND)	20,261	20,545	21,341
Cash dividend (VND)	500	0	0
P/E (x)	6.0	5.5	4.0
P/B (x)	2.3	1.0	1.0

INVESTMENT RATIONALES

Short-term weak sales mainly in flat steel segment, before recovering from 2024

- Slow disbursement of public investment, tightening management of the residential real estate market and a decline in global demand for durable goods, making total steel consumption to decrease slightly by 6% compared to 2021, per our expectation. Construction steel will recover sooner than flat steel when public investment disbursement is accelerated from the beginning of 2023. In the next 12 months, flat steel consumption may remain quiet due to high inflation globally.
- Dung Quat 2's first blast furnace will be completed by the end of 2023, rising crude steel capacity by 33% to 11.3 million tons/year.

Profit margin stays at low level in Q3 and improves from Q4/2022

- Material prices have cooled down rapidly from May until now. Due to the time lag of 2–3-month material stocking before production, gross margin will improve from Q4.
- Weak demand in many parts of the world alongside sluggish domestic consumption from March caused construction steel prices and HRC prices to drop sharply. However, the amplitude of recent declines in selling prices has narrowed.
- Gross profit margin in 2022 is estimated at 23.6%, compared to 27.5% in 2021, due to higher input prices and falling selling prices in Q2 and Q3.

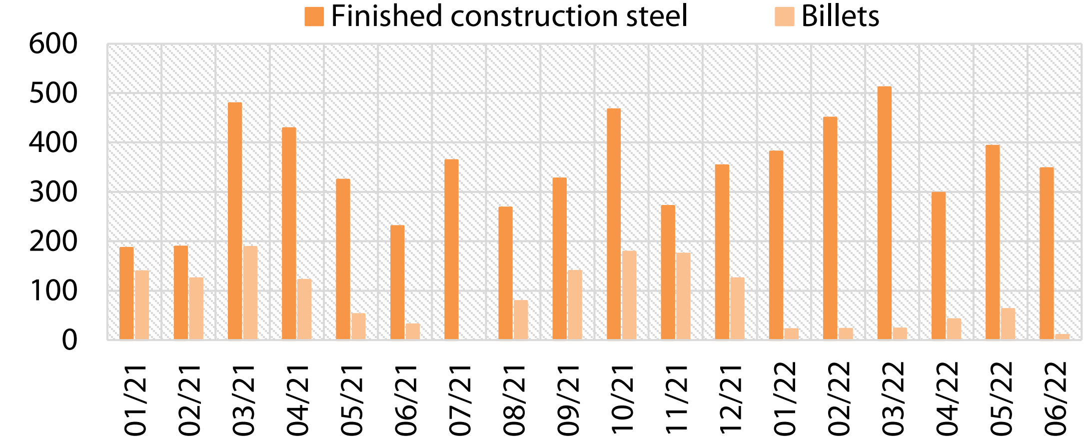
Many large investment plans increase capacity and business efficiency in the long term. In addition to the project of making containers in November 2022, HPG also plans to invest in Dung Quat 3 focusing on HRC and section steel, buying more iron ore mines in Australia and bauxite ore mines in the Central Highlands.

RISKS TO OUR CALL

- Changes in China's pandemic control policy and real estate market made steel consumption and selling price higher than expected.

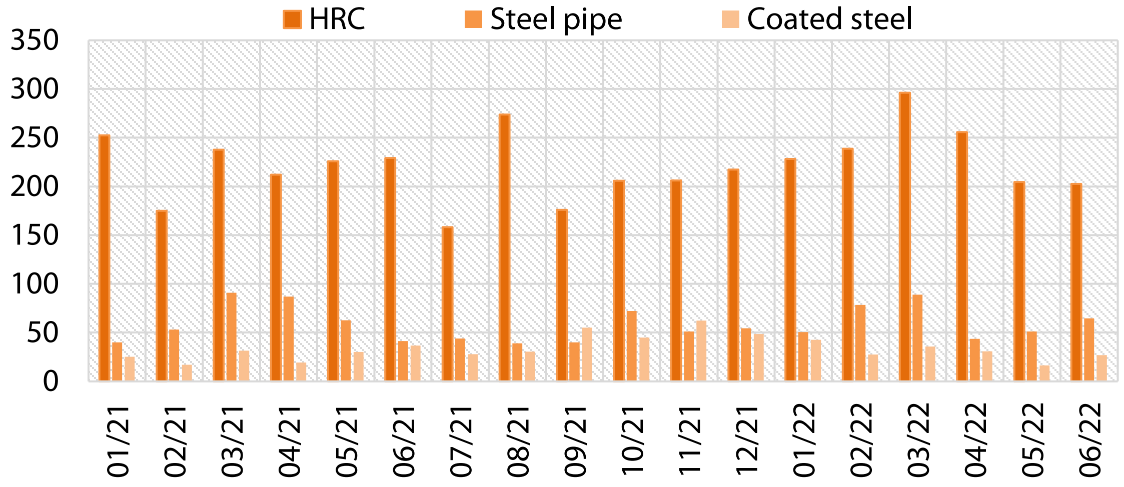
1H2022: HIGH GROWTH OF SALES

Figure 1: Construction steel consumption (thousand tons)



Source: VSA, Rong Viet Securities

Figure 2: Consumption of flat steel (thousand tons)



Source: VSA, Rong Viet Securities

Total consumption increased by 4% YoY to 3.98 million tons thanks to domestic and global demand recovering from the pandemic and the panic of steel and materials stockpiling in the wake of the Russian-Ukrainian war.

- Finished construction steel output reached 2.38 million tons, up 30%.
- HRC output increased 7% to 1.43 million tons.

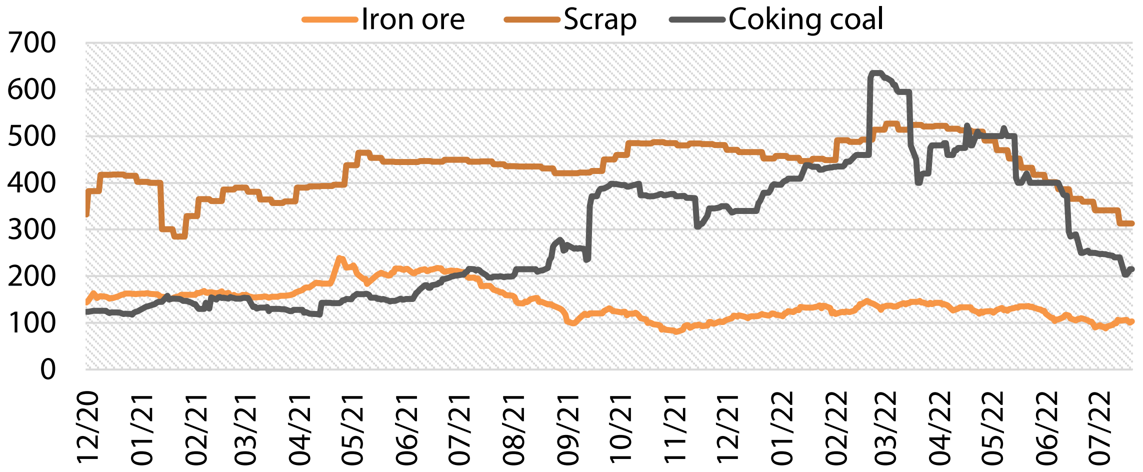
Export of coated steel reaches a high level

- High demand from Europe and North America. Consumption volume reached 98 thousand tons, up 16.5% YoY. However, consumption weakened significantly in May and June when the Russia-Ukraine war caused anxiety about inflation and economic recession.

Consumption of billet is weak due to almost no export

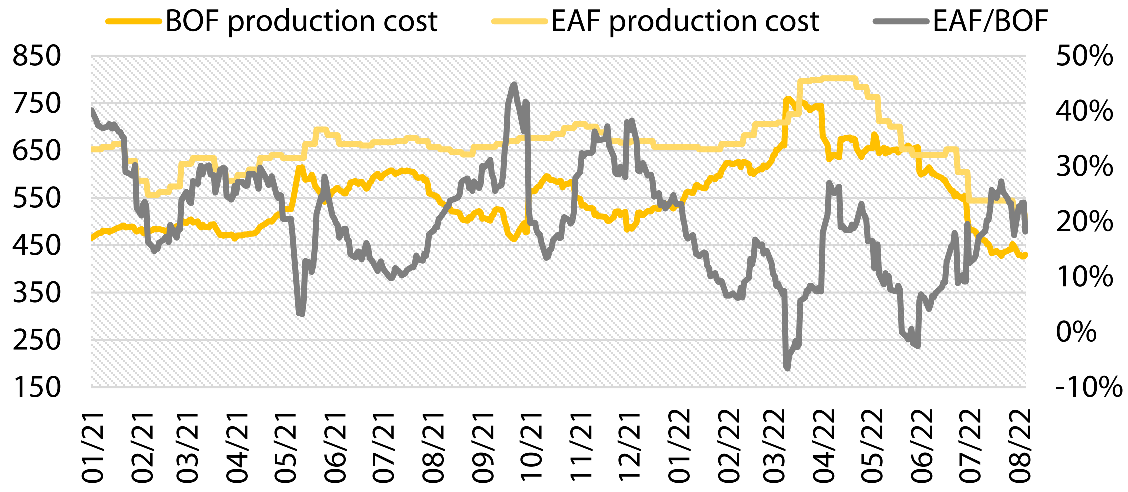
- Billet sales decreased by 72% YoY to 184,000 tons, 84% was domestic consumption, while 1H21 exports accounted for about 90%. Export of billet decreased to focus on producing commercial steel products.

Figure 3: Material price (USD/ton)



Source: Bloomberg, Rong Viet Securities

Figure 4: Steel production cost (USD/ton)



Source: Bloomberg, Rong Viet Securities

Material prices increased sharply at the beginning of Q2 (coking coal saw the strongest surge) and decreased rapidly from May until now

- Coking coal prices peaked at USD 625/ton in mid-March, fluctuated strongly at high levels due to panic sentiment when the war broke out. Prices have dropped rapidly from the end of May until now to USD 240/ton, equivalent to the price as end-September 2021, when steel demand was quiet in China.
- Iron ore prices fell more sharply than scrap steel prices. The trend is likely to maintain in the near future.
- The cost difference between blast furnace and electric furnace is estimated to be high, about 20%.

Steel production costs are expected to drop significantly from Q4

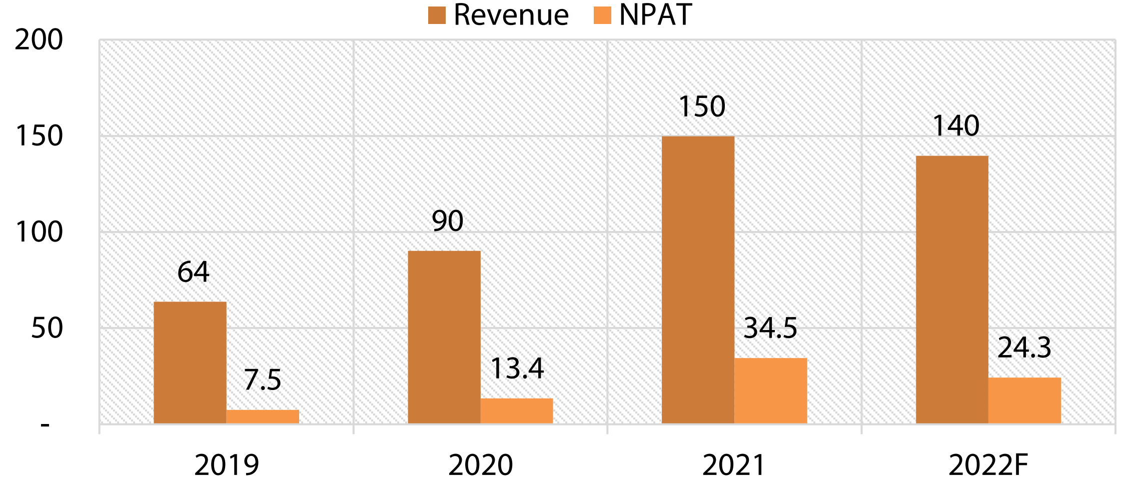
- Billet production cost is estimated to increase from around USD 570/ton in Q1 to USD 626/ton in Q2 (+10.3% QoQ) before falling to USD 565/ton in Q3 and USD 495/ton in Q4.

Gross margin of construction steel segment declined less than HRC's

- In Q2, the selling prices of construction steel and HRC was estimated to increase by 3% QoQ and 16% QoQ. Since the beginning of May, steel prices have continued to decline with construction steel prices down 15% and HRC prices down 35% due to slow downstream consumption and a sharp drop in offer prices of imported HRC.

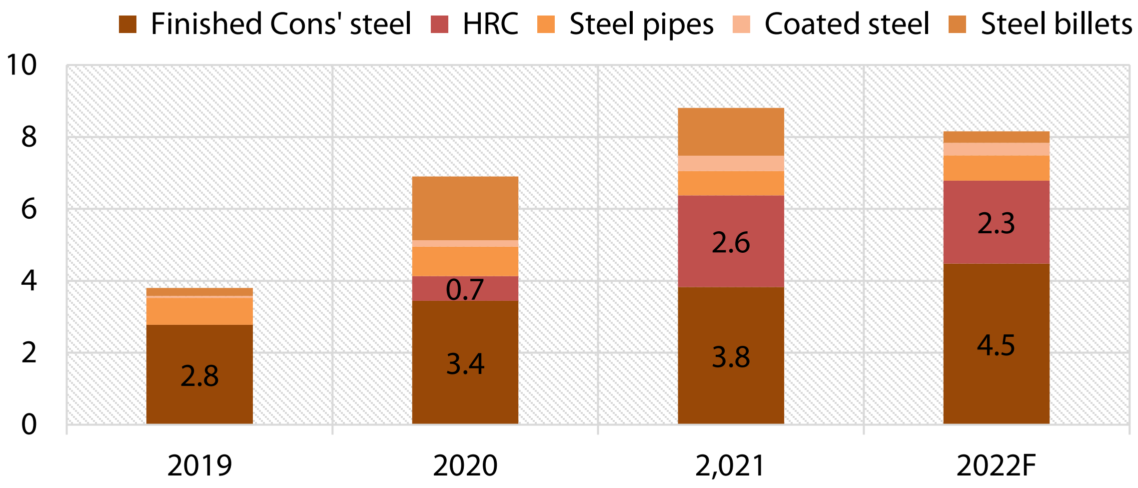
2H2022: NOT MUCH POSITIVE SIGNALS FOR CONSUMPTION

Figure 5: Forecast of revenue and profit after tax (trillion)



Source: HPG, Rong Viet Securities

Figure 6: Steel production forecast (million tons)



Source: HPG, Rong Viet Securities

Flat steel output fell more sharply than that of construction steel

- Slow disbursement of public investment, real estate market is quiet waiting for a new legal framework. The output of finished construction steel in 2H22 can be 12% lower compared to 1H, reaching 2.1 million tons.
- HRC volume may decrease by 38% versus 1H to 880 thousand tons due to high global inflation.

Gross profit margin of HRC and coated steel may decrease due to weak prices

- Weak flat steel demand keeps flat steel prices low (HRC and coated steel) in the next few quarters.
- Export competition increase as the US has loosened protection measures on steel from Vietnamese competitors and the EU has changed to manage Vietnam coated steel under quotas from July 1, 2022.

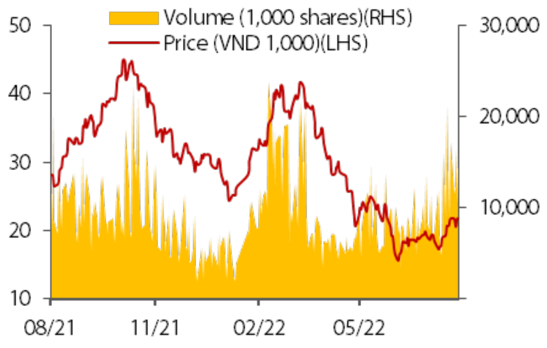
Update on Dung Quat 2 steel factory

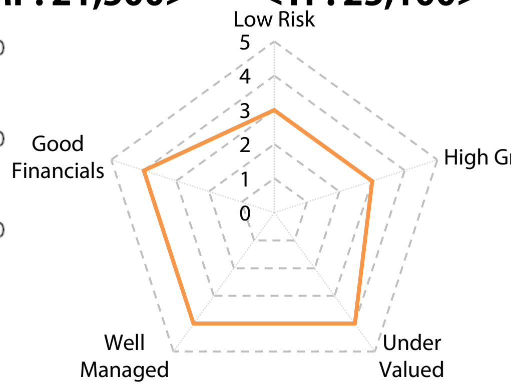
- Construction started in May 2022.
- Dự kiến hoàn thành cuối năm 2024.
- It's expected to be completed by the end of 2024.
- The two blast furnaces have a total capacity of 5.6 million tons. The first is expected to come into operation by the end of 2023 and the second by the end of 2024.

TEMPORARY DECREASE BEFORE BACK TO HIGH GROWTH

HSX: NKG

<ACCUMULATE: 11%> **<MP: 21,500>** **<TP: 25,100>**





STOCK INFO

Sector	Basic Materials
Market Cap ($ mn)	242
Current Shares O/S (mn shares)	263
3M Avg. Volume (K)	9,085
3M Avg. Trading Value ($ mn)	189
Remaining foreign room (%)	43.4
52-week range ('000 VND)	15.6 - 47.1

FINANCIALS	2021A	2022F	2023F
Revenue (VND bn)	28,173	20,060	19,002
NPATMI VND bn)	2,225	874	1,204
ROA (%)	14.5	7.4	9.7
ROE (%)	38.9	14.8	17.5
EPS (VND)	7,278	3,235	4,455
Book Value (VND)	23,467	22,573	26,195
Cash dividend (VND)	0	0	1,000
P/E (x)	2.3	5.4	4.2
P/B (x)	0.9	0.8	0.7

INVESTMENT RATIONALES

Weak consumption and falling prices in the second half in both the domestic and export markets.

- HRC price has continuously decreased since April-end while the price of coated steel has not decreased at the same pace, causing domestic buyers to reduce transactions to wait for coated steel prices to go down further. Selling prices, therefore, are under further downward pressure but domestic consumption will only rise back from September as July-August is the rainy season. Domestic consumption of coated steel in 2H2022 can reach 94 thousand tons (+14% YoY) thanks to the low base in Q3/2021, equaling to an increase of 1% for the whole year to 202 thousand tons.
- Prolonged high global inflation and rising competition in major markets could slow Vietnam export value until mid-2023. The US has eased protection measures on Japanese, EU and UK steel from the end of 2021/early 2022. EU has re-imposed tariff quotas on Vietnam's coated steel from July 2022 to mid-2024. Exports of coated steel in 2H2022 is projected to reach 50 thousand tons (-88% YoY), equaling to a drop of 48% for the whole year to 378 thousand tons.
- The price gaps with other markets narrowed to decrease export gross margin to 12.9% (FY20-21: 18.4%). Domestic selling prices lose support due to weak exports. Domestic gross margin drop to 5.9% (2021: 12.4%).

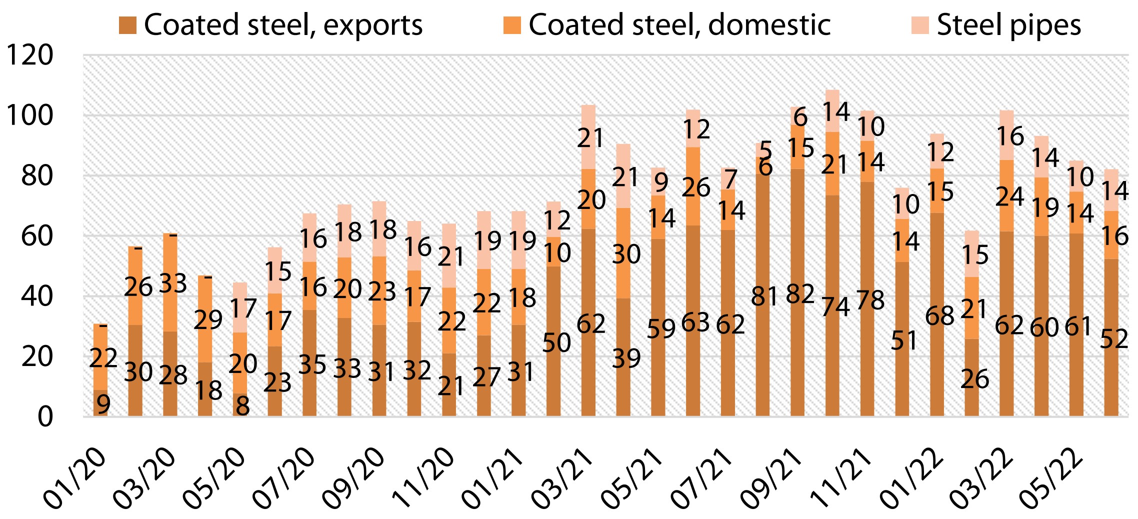
Doubling capacity by 2027 will drive growth in the medium term. The project is invested in 3 phases from Q4 2022 to 2026-end, financed mostly by equity. Revenue and NPAT in the period 2022-2027 are estimated to grow at compound rates of 6.1%/year and 18.8%/year.

RISKS TO OUR CALL

- Changes in China's pandemic control and real estate market policies makes steel consumption and selling prices higher than expected.

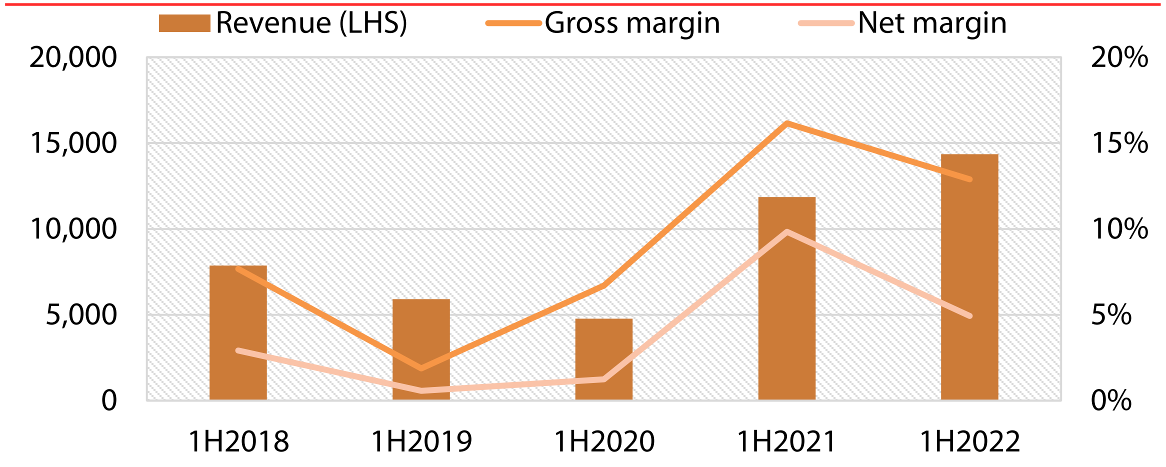
1H22: DOMESTIC CONSUMPTION DECLINED

Figure 1: Consumption volume by market ('000 tons)



Source: VSA, Rong Viet Securities

Figure 2: Revenue (VND bn) and profit margin

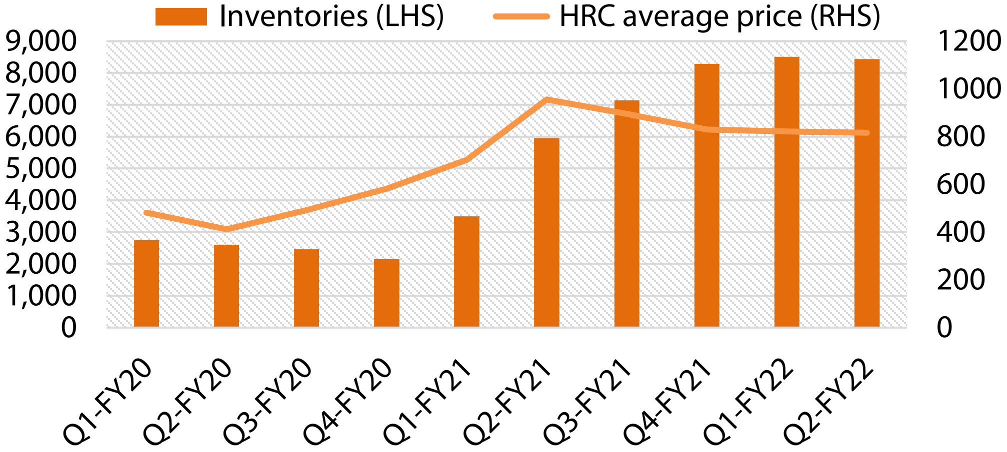


Source: NKG, Rong Viet Securities

After 1H2022, NKG's revenue posted VND 14,347 billion (+21% YoY), whereas PAT plummeted sharply by 39% YoY to VND 708 billion amidst pressure in the domestic market and rising input prices.

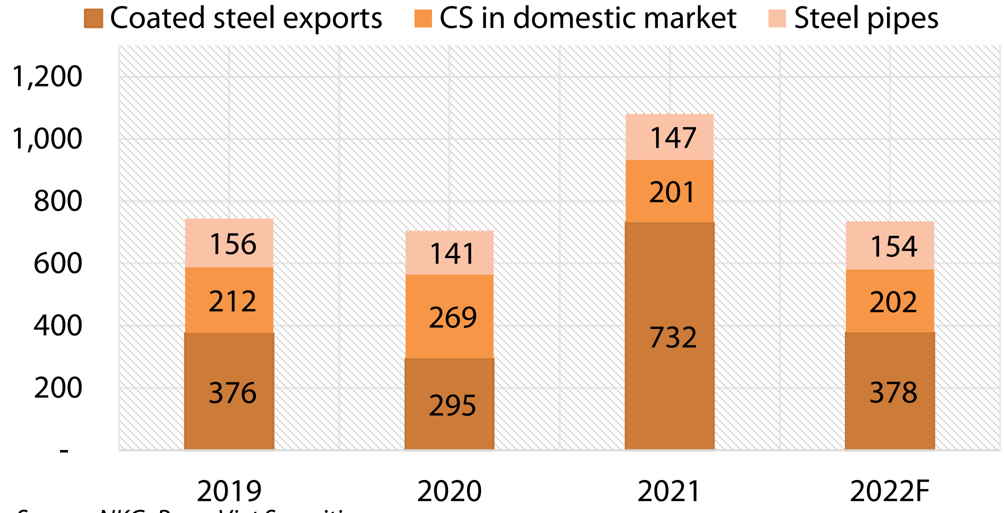
- Coated steel export volume increased by 8% YoY to 328 thousand tons, accounting for 63% of total sales volume. Europe and North America weighed on 65-70%.
- Conversely, domestic consumption has weakened since April as market waited for selling prices to decrease following HRC prices. Domestic output of coated steel in 1H decreased by 9% YoY to 108 thousand tons and of steel pipe fell by 15% YoY to 81 thousand tons.
- NKG could maintain stable domestic selling price in Q2 compared to Q1 thanks to good exports.
- HRC Vietnam CFR price increased from USD 743/ton at the end of Jan 2022 to USD 910/ton in Mar before decreasing from April 2022 to USD 698/ton at the end of June 2022. The surge in HRC prices in Europe and North America followed by a rapid decline in early Q2 did not pause the downward trend of Q2 gross margin.
- Gross margin decreased from 16.2% in 1H2021 to 12.9% in 1H2022.

Figure 3: Inventory (VND bn) and HRC price (USD/ton)



Source: NKG, Bloomberg, Rong Viet Securities

Figure 4: Forecast consumption ('000 tons)



Source: NKG, Rong Viet Securities

Weak consumption and prices in downtrend

- Coated steel exports may reach 50 thousand tons (-88% YoY) due to the decline in global demand. Domestic consumption of coated steel and steel pipes posted 94 thousand tons (+14% YoY) and 73 thousand tons (+41% YoY) on the low base of Southern lockdown in Q3/2021.
- The price gap between Vietnam and other markets decreased, causing the gross margin to decline. Coated steel's gross margin may reach 5.1%, of which export GPM will reach 4.6% and domestic GPM 5.3%, significantly lower than the respective levels of 17.5%, 18.6% and 11.5% in the same period last year.
- The 2H's revenue is projected at VND 5,536 billion (-58% YoY) and a loss of VND 50 billion.

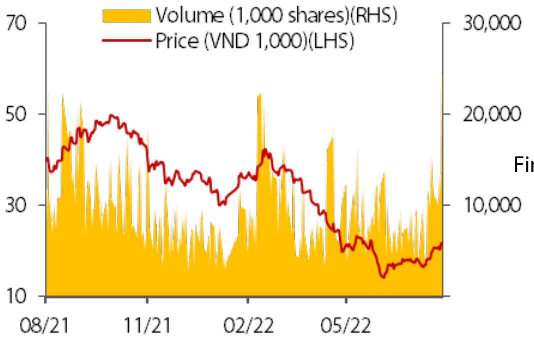
2023 – Consumption is difficult to recover strongly

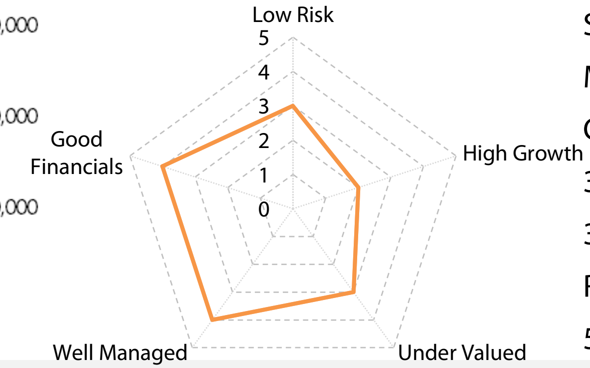
- Inflation cooling down from 2023 will encourage the demand for coated steel. The difference in HRC price between Vietnam and the EU and the US markets will not be high since there is no production disruption in these regions. Export competition with many other countries will rise .
- Steel output may increase by 10.5%, selling price will decrease following HRC prices. Gross profit margin will reach 10.1%, roughly the same as 9.8% in 2021.

GLOOMY CONSUMPTION BECAUSE OF WEAK DEMAND

HSX: HSG

<MONITOR> <MP: 20,900> <TP: N/A>





STOCK INFO

Sector	Basic Materials
Market Cap ($ mn)	445
Current Shares O/S (mn shares)	498
3M Avg. Volume (K)	8,669
3M Avg. Trading Value ($ mn)	167
Remaining foreign room (%)	42.3
52-week range ('000 VND)	13.8 - 51.3

FINANCIALS	2021A	2022F	2023F
Revenue (VND bn)	48,727	48,439	41,136
NPATMI VND bn)	4,249	921	1,292
ROA (%)	16.0	3.7	5.9
ROE (%)	39.4	7.9	10.3
EPS (VND)	8,611	1,735	2,435
Book Value (VND)	21,855	23,591	25,526
Cash dividend (VND)	0	0	500
P/E (x)	5.4	9.8	7.0
P/B (x)	2.1	0.7	0.7

INVESTMENT RATIONALES

Weak consumption and falling prices over the next few quarters.

- HRC price has continuously decreased since April-end while the prices of coated steel has not decreased at the same pace, causing domestic buyers to reduce transactions to wait for prices to fall further. Selling prices, therefore, are under further downward pressure but domestic consumption will only grow sinificantly from September as July-August is the rainy season. Domestic consumption of coated steel for this year may increase by 8% to 577 thousand tons.
- Prolonged high global inflation and rising competition in major markets could slow exports until mid-2023. The US has eased protection measures on Japanese, EU and UK steel from the end of 2021/early 2022. The EU has re-imposed tariff quotas on Vietnam's coated steel from July 2022 to mid-2024. Exports of coated steel for the whole year are projectd to reach 821 thousand tons, down 34%.
- The price gap with other markets narrowed, causing the export gross margin to decrease to 12.5% (FY20-21: 16.9%). Weak exports together with lower HRC prices will push more pressures on domestic selling prices. Domestic gross margin will fall to 11.9% (FY20-21: 22.4%).

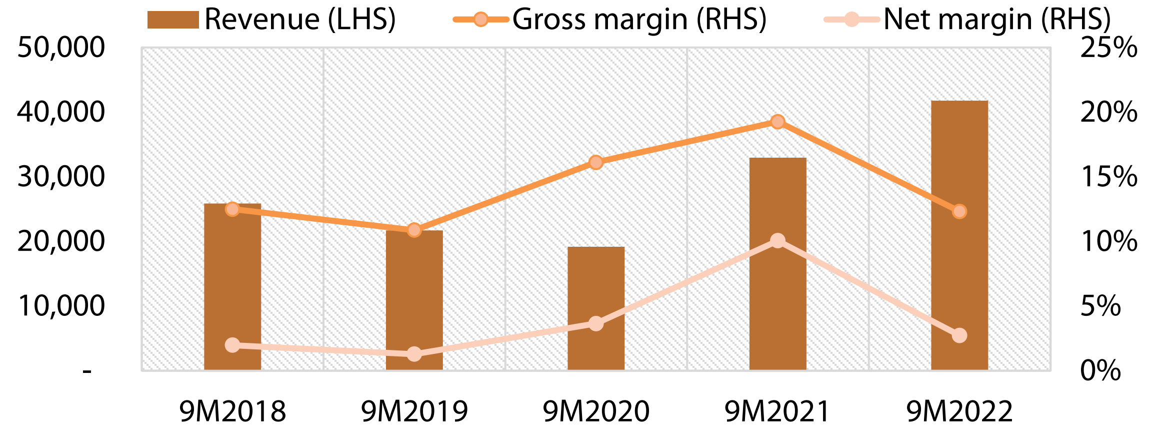
Financial health is continuously improving. At the end of Q3/FY21-22, the debt/equity ratio dropped to 94% compared to 150% of Q3/FY20-21. A safer capital structure will help HSG reduce interest expenses during the current difficult business period. The company aims to be debt-free by FY23-24.

RISKS TO OUR CALL

- Changes in China's pandemic control and real estate market policies makes steel consumption and selling prices higher than expected.

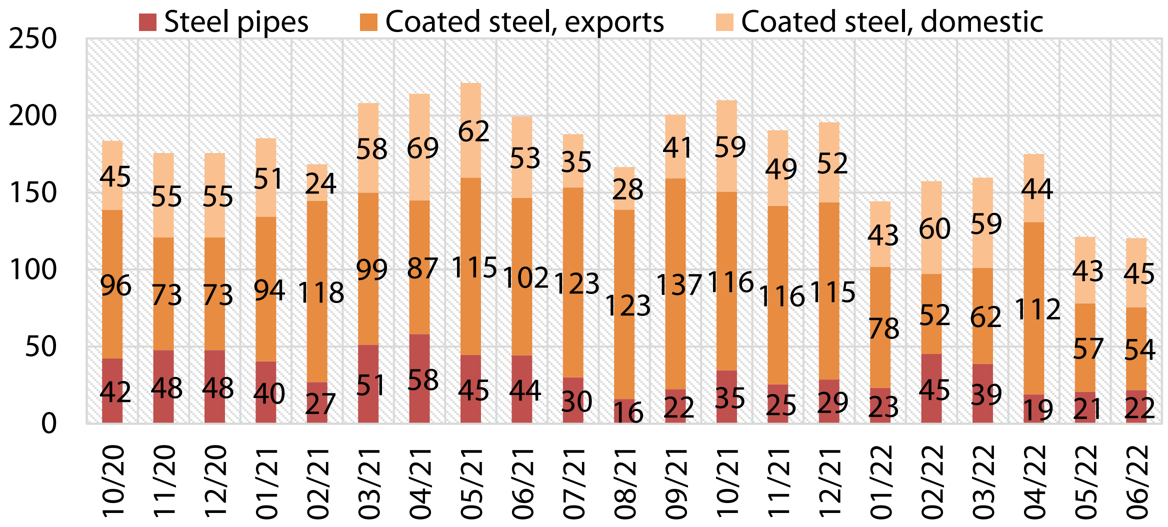
9M/FY21-22: CONSUMPTION DROP WITH PRESSURES

Figure 1: Revenue (VND bn) and profit margin



Source: HSG, Rong Viet Securities

Figure 2: Consumption volume by market ('000 tons)



Source: VSA, Rong Viet Securities

Revenue posted 41,772 billion (+27% YoY) and PAT came at 1,137 billion (-66% YoY). Steel consumption volume reached 1.47 million tons, a decrease of 15% YoY. Consumption gradually dropped due to the sentiment of buyers waiting for prices to fall and observing the movements of market demand.

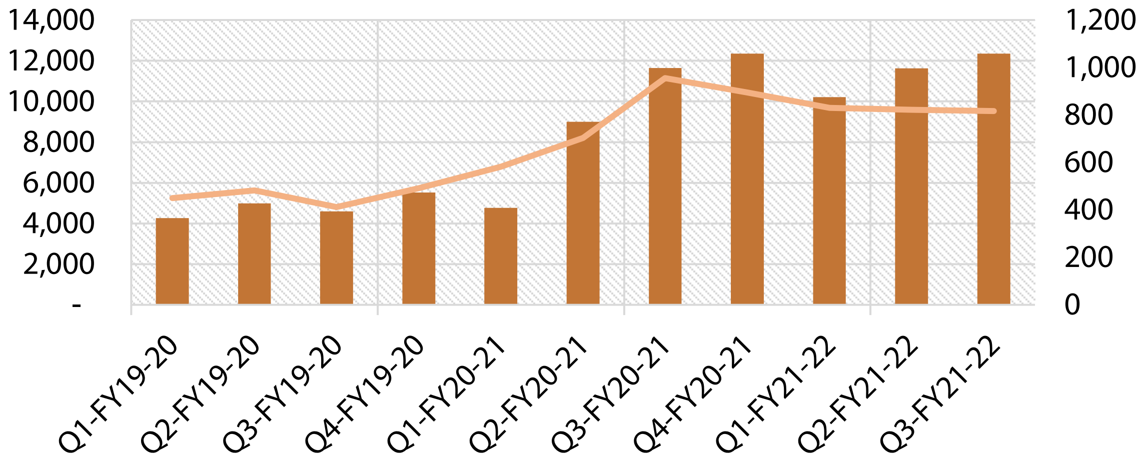
- Coated steel production reached 1.22 million tons, down 8.4% YoY, of which export value was 763 thousand tons, down 11% YoY and domestic volume was 454 thousand tons, down 3.6% YoY.
- Steel price gap between Vietnam and Europe and North America narrowed rapidly after the panic hike when the Russian-Ukrainian war broke out. Domestic market slowed down and waited for price adjustments of coated steel following HRC prices.

Profit margin plummeted due to pressures from high material costs.

- HRC Vietnam CFR price increased from USD 743/ton at the end of Jan 2022 to 910 USD/ton in March before declining from April to USD 698/ton at June-end. The high price of HRC in Europe and North America at the beginning of Q3 did not pause the shrink of Q3 GPM.
- Gross margin decreased from 19.3% in 9M/FY20-21 to 12.3% in 9M/FY21-22.

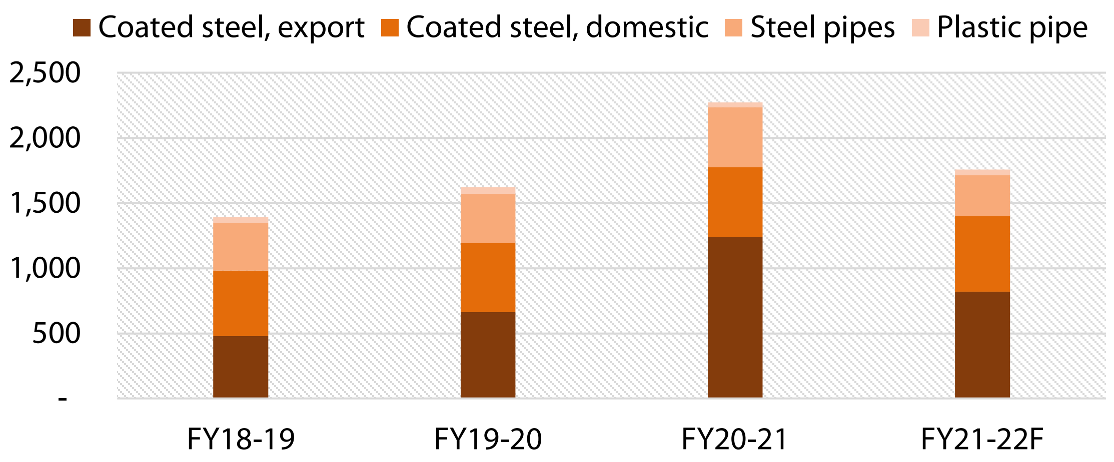
Interest expense dropped sharply by 25% YoY thanks to the reduction in debt. The debt/equity ratio at the end of Q3 was 94%, stayed unchanged from the beginning of 2022 but better than the level 140 % of Q3/FY20-21.

Figure 3: Inventory (VND bn) HRC price (USD/ton)



Source: HSG, Rong Viet Securities

Figure 4: Consumption volume project ('000 tons)



Source: HSG, Rong Viet Securities

Q4/FY21-22: Weak sales, falling selling prices and high material prices to eat up profits

- Coated steel exports may reach 58 thousand tons (-74% QoQ and -85% YoY) due to the decline in global demand. Domestic consumption of coated steel hit 123 thousand tons (-7% QoQ and +19% YoY) on the low base of lockdown in the South in Q4/FY20-21. Steel pipe consumption posted 59 thousand tons (-4% QoQ, -14% YoY).
- The price gap between Vietnam and other markets decreased, causing the gross margin to drop. Coated steel gross profit margin may reach 9.6%, of which export GPM will reach 9.7% and domestic GPM 9.5%, significantly decreasing compared to 17%, 16.5% and 19% respectively of the same period, according to our estimates.
- Q4 revenue and NPAT are project at VND 6,693 billion (-58% YoY) and VND -183 billion.

FY22-23: Consumption is difficult to recover strongly

- Coated steel exports are forecast to rebound from Q3/FY22-23 onwards, owing to cool-down inflation. HRC gap price between Vietnam and European and American markets will not be high since there is no production disruption in these regions. Export competition increased with many other countries.
- Steel output may increase by 8%, selling price will decrease following HRC price. Gross profit margin is approximately 11.6% of FY21-22.

INVESTMENT FOR NEW CAPACITY TO BE DELAYED DUE TO LOW DEMAND

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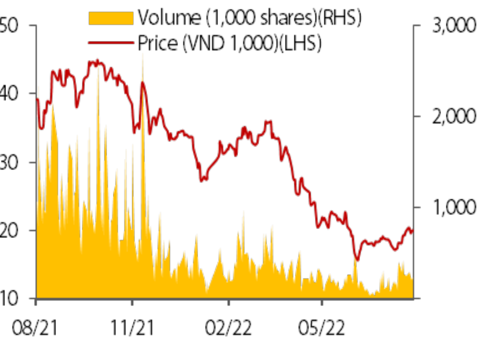
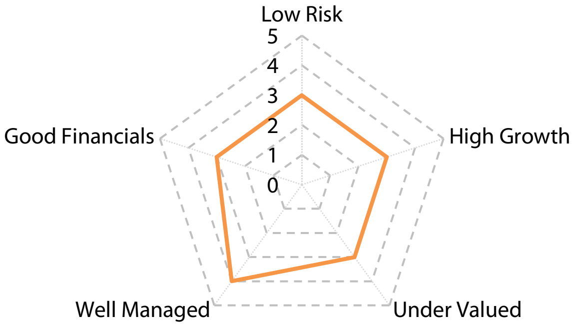




STOCK INFO

Sector	Basic Materials
Market Cap ($ mn)	63
Current Shares O/S (mn shares)	73
3M Avg. Volume (K)	184
3M Avg. Trading Value ($ mn)	4
Remaining foreign room (%)	0.0
52-week range ('000 VND)	15.6 - 47.1

FINANCIALS

FINANCIALS	2021A	2022F	2023F
Revenue (VND bn)	21,312	24,164	25,479
NPATMI VND bn)	875	106	411
ROA (%)	9.7	1.2	4.4
ROE (%)	45.0	5.7	19.6
EPS (VND)	14,369	1,439	5,552
Book Value (VND)	31,875	25,501	28,554
Cash dividend (VND)	1,000	1,000	1,000
P/E (x)	1.4	13.9	3.6
P/B (x)	0.5	0.8	0.7

INVESTMENT RATIONALES

Adverse conditions affect steel consumption and prices in the second half of the year.

- High inflation, gloomy real estate market and slow disbursement of public investment reduced the demand for construction steel and flat steel. High inflation is likely to persist for the next few quarters while public investment disbursement will gradually increase in 2023.
- Steel prices have continued to decline sharply since April. Vietnam HRC prices CFR fell from USD 925/ton in early April to USD 600/ton at the end of July and remained around USD 605/ton so far.
- SMC's steel sales volume is expected to decrease by 1% in 2022, after a decrease of about 5% YoY in 2021. Of which, output in 1H increased by 8.4% YoY and in 2H is forecast to decrease by 10.3% YoY.

Outsourcing orders are weak and plans to invest in new factories are being delayed.

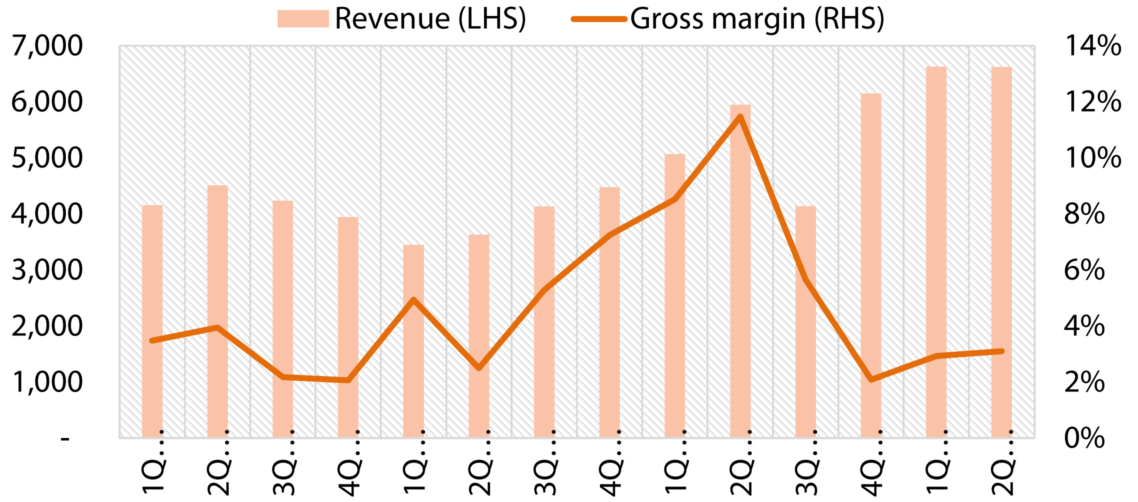
- Samsung factories in Vietnam are cutting output due to the lack of semiconductor chips and transportation difficulties, affecting SMC's outsourcing orders.
- Phu My Steel Processing factory and Phu My Precision factory, operating from the beginning of 2022, currently have low-capacity mobilization, only about 15-20% of design capacity. SMC will delay the completion time of 2022 investments from end-2022 to mid-2023 or later, depending on the recovery of demand.

RISKS TO OUR CALL

- Changes in China's pandemic control and real estate market policies makes steel consumption and selling prices higher than expected.

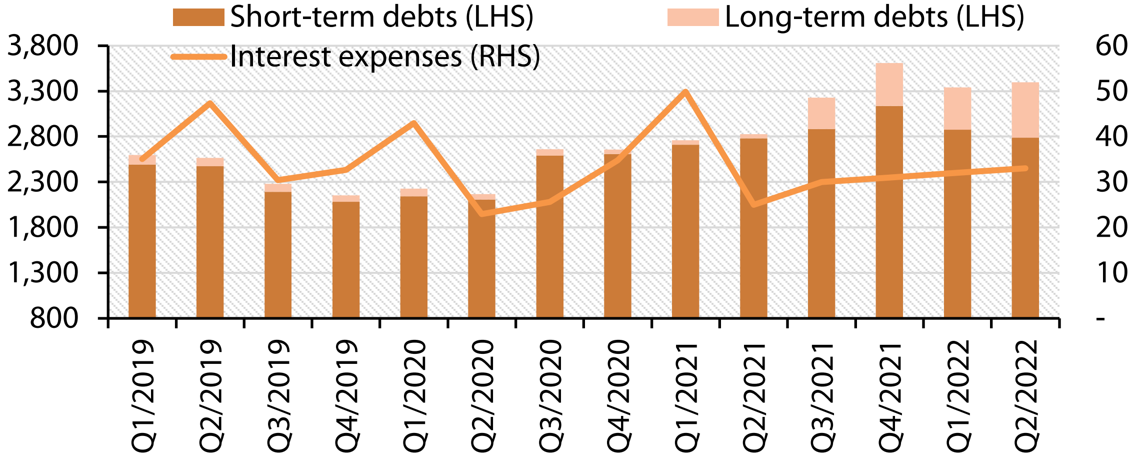
1H22: PROFIT REDUCED BECAUSE OF HIGH COST

Figure 1: Revenue (VND bn) and gross profit margin (%)



Source: SMC, Rong Viet Securities

Figure 2: Debt and interest expense (VND bn)



Source: SMC, Rong Viet Securities

Sales volume increased by 8.4% YoY combined with 11% higher steel prices made revenue grew sharply by 20% YoY, reaching VND 13,250 billion.

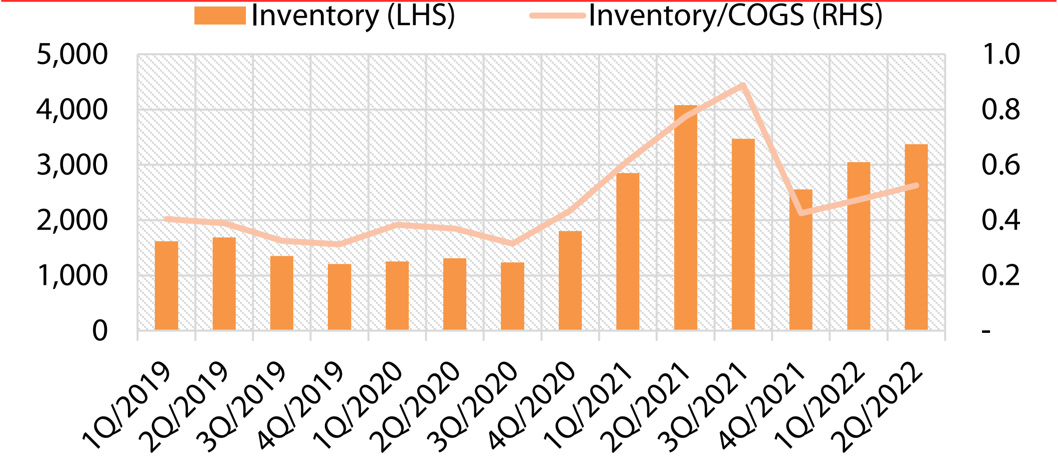
NPAT decreased by 82% to VND 127 billion due to a decrease in gross profit margin to 3% from 10.1% in 1H2021 along with a sharp increase in exchange rate loss and interest expense in Q2.

Adverse effects from geopolitical fluctuations and tightening of global monetary policy

Steel selling price continuously decreased in Q2 while inventories were stored at high prices, causing gross profit margin to decline. This is in contrast to 1H2021, where gross profit margin improved strongly, reaching 10.1% compared to 3-5% YoY, thanks to the continuous increase in steel price combined with low cost of inventory.

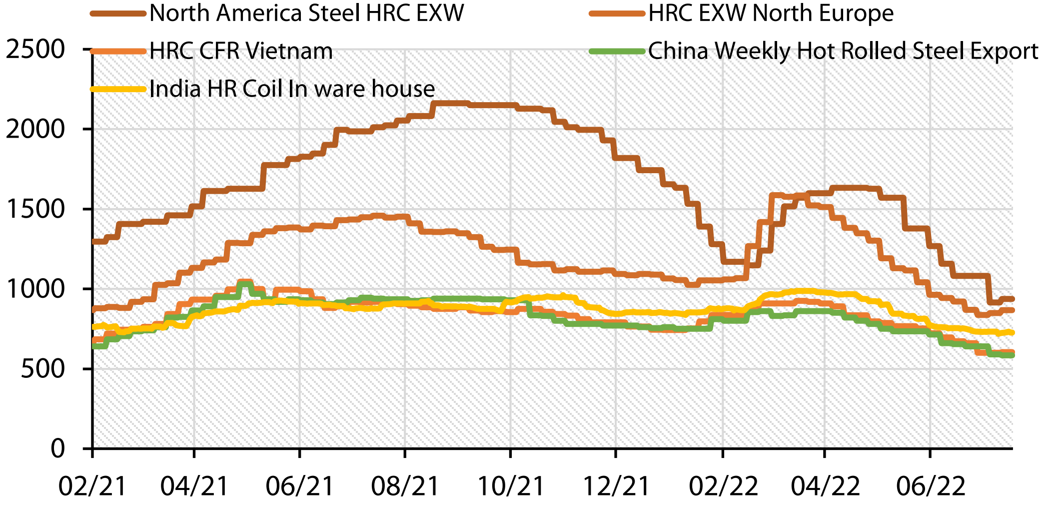
Financial expenses increased by nearly 7 times compared to Q2/2021, mainly due to (1) increase in realized exchange rate loss, affected by strong exchange rate, and (2) increase in interest expense due to increase in borrowing. long-term and finance lease from Q3/2021.

Figure 3: Inventories (VND billion)



Source: SMC, Rong Viet Securities

Figure 4: HRC price (USD/ton)



Source: Bloomberg, Rong Viet Securities

Inventories increased by 19% and 11% respectively in the last two quarters to VND 3,542 billion. Steel prices continued to fall causing the company to make provision for depreciation of inventories of VND 170 billion at the end of Q2.

Gross profit margin has little chance to improve in the second half of the year as steel prices have not recovered significantly.

HRC Vietnam CFR price has decreased from USD 925/ton in April to USD 600/ton at the end of July and is maintaining around USD 605/ton. Prices are likely to recover slowly, given the uncertainty surrounding the pandemic, geopolitics and high inflation.

Pressure on the margin of the processing segment is high with the raw material inventory period of this segment being higher than that of the commercial segment. We estimate the outsourcing segment may have a gross loss in Q3 and recover gradually from Q4.

Sales volume may recover slowly in the second half of the year due to lack of supporting factors

Consumption volume is forecasted to decrease by 19.3% compared to 1H22 and 10.3% compared to 2H21, to 565 thousand tons.

In the second half of the year, we estimate H1 revenue to grow 6% YoY to VND 10,914 billion. The loss of VND 62 billion in Q3 makes the loss in 2H2022 come at VND 21 billion.

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