

## Hoa Phat Group (HPG – HSX)

### A new chapter

Particulars (VND bn)	3QFY13	2QFY13	% (qoq)	3QFY12	% (yoY)
Net Revenues	4,194.8	4,344.9	-3.5%	4,022.0	4.3%
EBIT	496.1	511.6	-3.0%	288.8	71.8%
PAT	677.4	677.0	0.1%	461.3	46.8%
EBIT margin (%)	16.1%	15.6%	57bps	11.5%	468bps

Sources: HPG

- Q3 profit surged from the previous year thanks to the reversal of doubtful debt provision and gross profit margin gained well.
- With the Integrated Steel Complex - Phase going into operation in early October 2013, Q4 will see new chapter opened for HPG production expansion.
- HPG's earning in 2014 should be strong growth thanks to profits from Mandarin and the efficiency at the Integrated Steel Complex - Phase II.

**Outlook and Valuation:** FY2014's upbeat earnings should be a great support for HPG price. However, now that the Integrated Steel Complex has just started operating, it is difficult to evaluate accurately how well its products can sell. Also, it should be noted that the prices of some materials (i.e. coke, iron ore) has been on retreat since the year's beginning while the future contracts prices suggest a coming rebound. Finally, HPG may have to settle for a trimmed gross profit margin in order to nurture volume expansion in 2014. Given all those factors, we are relatively conservative on our estimate of next year's gross profit margin for the steel manufacturer.

In this report, we revise the target price for HPG up 16% from the price included in our latest strategy report of VND46.600/share due to some changes in our opinion about Company's business operations. First, concerns over the output of the Integrated Steel Complex - Phase 2 are lifted in part by recent positive sales data. Second, we notice some movements in the markets for basic materials which suggest recovery in the manufacturing sector in 2014, for which HPG has soon prepared their capacity. Therefore, we also revise our recommendation for HPG from NEUTRAL to ACCUMULATE in the medium term.

### Key financials

Y/E Dec (VND bn)	FY2011	FY2012	9M/FY2013	FY2013E	FY2014F
Net Revenues	17,851.9	16,826.9	12,474.0	18,145.5	27,009.3
% chg	25.1	-5.7	-1.2	7.8	48.8
PAT	1,236.4	994.0	1,464.6	1,955.2	2,412.4
% chg	-8.4	-19.6	78.8	96.7	23.4
EBIT margin (%)	6.9	5.9	11.7	10.8	8.9
ROA (%)	7.6	5.4		9.5	11.2
ROE (%)	17.9	12.8		22.7	24.8
EPS (VND)	3,573	2,386		4,666	5,757
Adjusted EPS (VND)	2,973	2,386		4,666	5,757
Book value (VND)	21,426	19,294		21,763	24,326
Cash dividend (VND)	1,000	2,000		2,000	3,000
P/E (x)	4.5	7.2		8.4	6.8
P/BV (x)	0.7	1.1		1.8	1.6

Sources: HPG, Stock price as of 21/11/2013

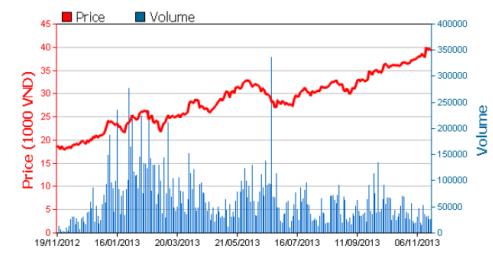
### ACCUMULATE

HPG (VND)	39,500
Target Price (VND)	46,600

Investment Period	Intermediate
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### Stock Info

Sector	General industry
Market Cap (VND bn)	16,553
Current Shares O/S	419,053,329
Beta	1.2
Free float (%)	62.0
52 weeks High	39,700
52 weeks Low	18,000
Avg. Daily Volume (in 20 sessions)	373,348



### Performance (%)

	3M	1Y	3Y
HPG	27.8	119.4	45.2
General Industry	0.5	10.4	N/A
VN30 Index	4.1	27.5	N/A
HSX Index	3.3	34.1	5.8

### Major Shareholders (%)

Tran Dinh Long	24.1
Deutsche Bank Aktiengesellschaft	5.3
BI private equity new markets II ks	4.8
VOF investment, ltd	4.7
Foreigner Investor Room (%)	9.2

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**Exhibit 1: 3QFY2013 and YTD Results**

Particulars (VND bn)	3QFY13	2QFY13	% chg (qoq)	3QFY12	% chg (yoy)	9M/FY13	% chg (yoy)
Net Revenues	4,194.8	4,344.9	-3.5	4,022.0	4.3	12,474.0	-1.2
Gross profits	657.0	835.8	-21.4	540.4	21.6	2,184.4	23.4
SG&AC	(14.7)	129.4		151.4		271.5	-35.3
Operating Income	671.7	706.4	-4.9	389.1	72.6	1,912.9	90.1
EBITDA	841.9	830.6	1.4	606.8	38.8	2,477.8	32.1
EBIT	677.4	677.0	0.1	461.3	46.8	2,008.0	40.8
Financial expenses	105.4	170.1	-38.0	124.8	-15.6	373.3	-25.6
- Interest Expenses	79.4	77.7	2.3	108.6	-26.8	238.5	-45.6
Dep. and amortization	-164.5	-153.6	-7.1	-145.5	13.1	-469.7	-4.8
Non-recurring Items (*)							
Extraordinary Items (*)	164.0					269.9	
PBT	598.0	599.3	-0.2	352.7	69.5	1,769.5	79.1
PAT	496.1	511.6	-3.0	288.8	71.8	1,464.6	78.8
(*) Adjusted PAT	373.1		-27.1		29.2	1,262.2	54.1

Sources: HPG, RongViet Securities

(\*) provision reverse of VND 164 billion (3QFY13) and transfer subsidiary share of VND 105.9 billion (1QFY13)

**Exhibit 2: 3QFY2013 performance analysis**

Particulars	3QFY13	2QFY13	% Chg. (qoq)	3QFY12	% Chg.(yoy)
<b>Profitability Ratios (%)</b>	15.7	19.2	-357bps	13.4	222bps
Gross Margin	27.3	22.6	474bps	22.6	473bps
EBITDA Margin	16.1	15.6	57bps	11.5	468bps
EBIT Margin	11.8	11.8	5bps	7.2	465bps
Net Margin	11.9	11.8	6bps	7.3	457bps
Adjusted Net Margin					
<b>Turnover *(x)</b>	1.8	2.0	-0.2	2.1	-0.3
-Inventories	11.4	10.5	0.8	8.4	3.0
-Receivables	15.8	26.5	-10.7	29.2	-13.5
-Payables					
<b>Leverage (%)</b>	1.4	1.3	0.1	1.1	0.4
Total Debt/ Equity	15.7	19.2	-357bps	13.4	222bps

Sources: (\*) Annualized turnover

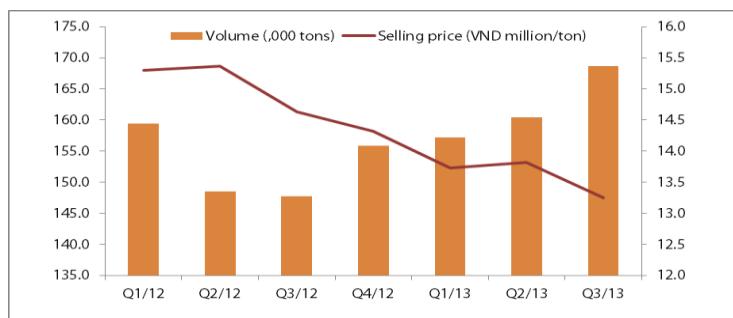
**Q3 profit surged from the previous year thanks to the reversal of doubtful debt provision**

Q3 is normally known as a trough in HPG business cycle. However, in order to prepare for the operation of the Integrated Steel Complex - Phase II, HPG maintained its offensive stance towards sales volume. As the result, Q3 output was up 5.1% from the previous quarter to 169,000 tons. Nonetheless, the average selling price was down 4%, keeping steel revenue relatively unchanged and decreasing total revenue by 3.5%. Also due to the eased selling price, Q3 gross profit margin (15.7%) shrank significantly from that of Q2 (19.2%).

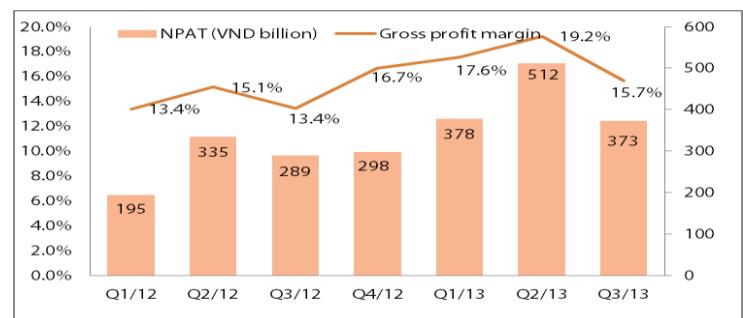
An unforeseen turning in Q3 was HPG's successful collection of VND 264 billion of "bad debt" regarding transactions with Nguyen Duc Kien. The Company, therefore, fully reversed VND 164 billion of doubtful

debt provision allocated earlier, which helped bring Q3 profit up 71.8% year-on-year. Even leaving the reversal aside, net profit was still optimistic at VND 373.1 billion, up 29.2% from a year earlier.

We highly appreciate the Company's effort and responsiveness in the strained industry. Low demand and selling price trending downward have suppressed growth in the steel industry since the beginning of the year. To make up for what the market fails to offer, HPG has taken advantages of its closed-end production line and constant declines in input prices to lower selling prices and bolster sales volume. With a well-tinkered strategy, the Company has seen its gross profit margin adding up from a year ago for each of the past 3 quarters of 2013. Even after the deductions of profits from subsidiary share liquidation and the above-mentioned provision reversal, HPG's quarterly profit still exhibited good growth over the past 9 months (see chart). Year-to-date NPAT of the holding company's shareholders was reported at VND 1.465 billion, which leads the annual targets by 22%.

**HPG's quarterly volume and selling price chart**


Sources: VSA, RongViet Securities

**HPG's quarterly GPM and NPAT chart**


Sources: HPG, RongViet Securities, NPAT were excluded the extraordinarily items

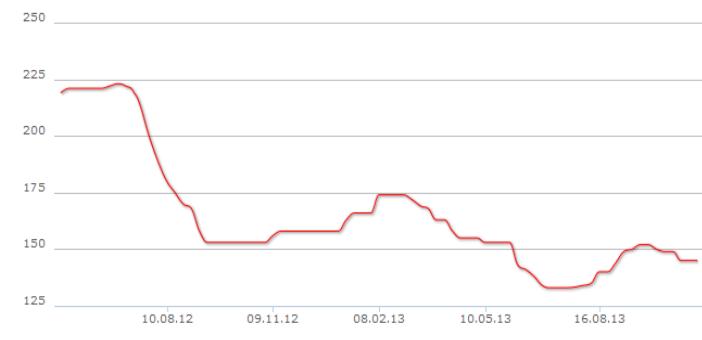
#### **Q4 is the turning point for production expansion**

The Integrated Steel Complex - Phase II, which started synchronous operation officially in 08 October, should help raise HPG's capacity from 650,000 tons to 1.15 billion tons in the last quarter of 2014. The firm expects to add around 100,000 tons to sales volume in Q4 from this expansion. In our opinion, however, putting 35,000 tons of finished steel products each month on top of the standard output of 55,000 tons each month may place a substantial pressure on the Company's sales team. As the matter of prudence, we assume that the Integrated Steel Complex-Phase II will supply an additional 35,000 tons of finished steel products and about 70,000 tons of steel billets in Q4.

As prices of input materials such as scrap steel, iron ore, coking coal... have been on a rebound since early September, HPG's Q4 gross profit margin should not be as high as in Q3. To add to the margin shrinkage, it would be hard for the Company to lift its selling price without denting its volume-boosting strategy. For that reason, non- real-estate gross profit margin for Q4 is forecasted around 14.9%.

**The scrap steel price chart**


Sources Metal expert

**The hard-coking coal price chart**


Sources: Metal expert

**About the Mandarin project**, the transfer schedule for finished apartments has been set back so that no sooner than October can house buyers receive the keys to their new homes. However, we still assume that HPG will be able to recognize about VND 100 billion from these real estates in last quarter of 2013. Q4 revenue and NPAT are estimated VND490 billion, meaning a whole-year profits figure of VND1,955 billion or VND4,700 per share.

#### Exhibit 4: 4QFY2013 Forecast

Particulars (VND bn)	4QFY13	%chg (qoq)	%chg (yoY)
Net Revenues	5,671.5	35.2	33.9
Gross profits	908.9	38.4	28.7
EBIT	711.9	5.1	132.7
PAT	490.6	-1.1	180.1

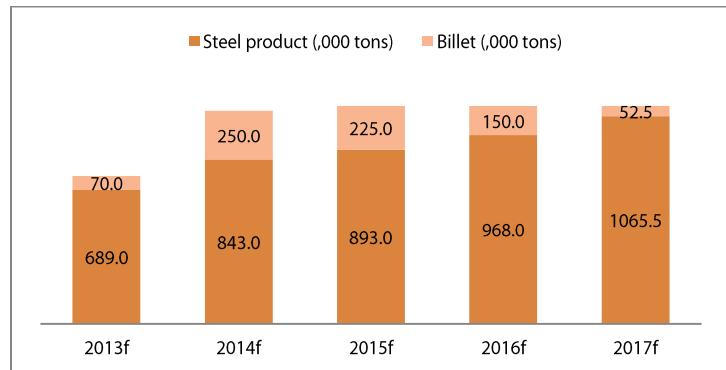
Sources: RongViet Securities

#### HPG's earning in 2014 should be strong growth thanks to profits from Mandarin and the efficiency at the Integrated Steel Complex - Phase II

As finished steel supply overwhelms demand and stiff competition become more problematic, we believe that HPG will continue to include steel billets in sales strategy for the coming years. However, the portion of billet sales in total sales may decrease gradually. Although the profit margin of this semi-finished product is lower than that of finished steel, we see that this is a proper step for the Company given the current market conditions. Advantaged by its closed-end production line, HPG's billet selling price is currently 5-7% lower than what offered in the overall market, which leaves the door open for the steel manufacturer to gain domination of this specific segment. Also, since steel billets are the main inputs of rolling mills it should not be hard to find a market for the product. Up to October, HPG has been selling billets to a Japan-based company in Viet Nam while targeting the other markets South East Asian region. In 2014, billet and finished steel volumes are expected at 250,000 tons and 850,000 tons (include of 200,000 tons from the Integrated Steel Complex - Phase II), respectively. As we will maintain constant update on HPG selling activity, such forecast assumption is open for revision in case finished steel consumption turns out to be more positive.

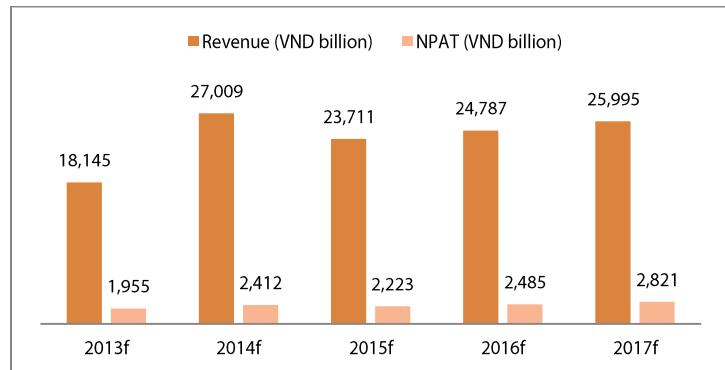
At the end of October, the Mandarin project still had about 200 apartments yet to find buyers (of the total 1,000). However, from the firm's information, we know that recent selling have been fairly positive so that 1 unit is sold in every 1-to-3 day. Thus it is safe to assume that Mandarin will finish selling and the remaining VND 400 billion of profit will be recognize in 2014. Next year's revenue and NPAT is accordingly estimated at VND27,009 billion (+49% yoY) and VND2,412 billion (+23% yoY).

#### HPG's forecasted volume in 2013-2017



Sources: RongViet Securities

#### HPG's forecasted revenue and NPAT in 2013-2017



Sources: RongViet Securities

### Outlook and valuation

FY2014's upbeat earnings should be a great support for HPG price. However, now that the Integrated Steel Complex has just started operating, it is difficult to evaluate accurately how well its products can sell. Also, it should be noted that the prices of some materials (i.e. coke, iron ore) has been on retreat since the year's beginning while the future contracts prices suggest a coming rebound. Finally, HPG may have to settle for a trimmed gross profit margin in order to nurture volume expansion in 2014. Given all those factors, we are relatively conservative on our estimate of next year's gross profit margin for the steel manufacturer.

In this report, we revise the target price for HPG up 16% from the price included in our latest strategy report of VND46.600/share due to some changes in our opinion about Company's business operations. First, concerns over the output of the Integrated Steel Complex – Phase 2 are lifted in part by recent positive sales data. Second, we notice some movements in the markets for basic materials which suggest recovery in the manufacturing sector in 2014, for which HPG has soon prepared their capacity. Therefore, we also revise our recommendation for HPG from NEUTRAL to ACCUMULATE in the medium term. Nonetheless, we have had no more than one month to evaluate the feasibility in HPG's latest sales strategy. Thus, we suggest that prudent investors to maintain their cautious stance in wait for Q4 sales results.

*We alter some of the assumptions for FY2013 forecast after gross profit surpassed our previous estimate in Q2 (material price dropped at quicker rate than selling price) and HPG was able to recover the doubtful amount regarding the transactions with Nguyen Duc Kien in Q3. In this report, we also account for the fact that HPG will sell billets in Q4 instead of selling only finished steel products as per our previous forecast.*

### Exhibit 5: Key Assumption

Particular	Earlier Estimates		Revised Estimates	
	FY2013E	FY2014E	FY2013E	FY2014E
Revenue growth (%)	6.6	-	7.8	48.8
Steel volume growth (%)	8.9	-	12.7	22.4
Billet volume growth (5)	-		-	257.1
Gross margin (%)	16.0	-	17.0	16.7
EBIT margin (%)	12.7	-	15.0	12.6

Sources: RongViet Securities

### Exhibit 6: Changes in Estimates

Particular (VND bn)	FY2013E			FY2014E		
	Earlier Estimates	Revised Estimates	Var (%)	Earlier Estimates	Revised Estimates	Var (%)
Net Revenues	17,944.0	18,145.5	1.1	-	27,009.3	-
Gross profits	16.0	17.0	100bps	-	16.4	-
SG&AC	765.0	478.5	-37.5	-	1,075.0	-
Operating Income	2,106.0	2,614.8	24.2	-	3,355.1	-
Financial expenses	392.0	493.3	25.8	-	530.0	-
PBT	1,931.0	2,391.5	23.8	-	2,995.1	-
PAT	1,530.0	1,955.2	27.8	-	2,412.4	-
EBITDA	2,988.0	3,426.3	14.7	-	4,393.4	-
EBIT	2,282.0	2,720.0	19.2	-	3,412.2	-
EPS (VND)	17,944.0	18,145.5	1.1	-	27,009.3	-

Sources: RongViet Securities

					VND Billion						
INCOME STATEMENT		2011A	2012A	2013E	2014F	BALANCE SHEET		2011A	2012A	2013E	2014F
Revenue		17,851.9	16,826.9	18,145.5	27,009.3	Cash and equivalents		1,064	1,294	2,917	2,640
COGS		14,979.1	14,341.6	15,052.1	22,579.2	Short-term investment		0	220	0	1,000
<b>Gross profit</b>		<b>2,872.8</b>	<b>2,485.2</b>	<b>3,093.3</b>	<b>4,430.1</b>	Receivables		1,897	1,646	1,800	2,718
Selling Expense		217.4	274.0	233.7	534.8	Inventories		6,347	6,822	7,830	6,100
G&A Expense		401.8	587.0	244.8	540.2	Other current assets		177	238	120	120
Finance Income		329.3	164.6	277.0	170.0	<b>Total Current Asset</b>		<b>9,486</b>	<b>10,221</b>	<b>12,667</b>	<b>12,579</b>
Finance Expense		1,069.8	585.0	493.3	530.0	Tangible Fixed Assets		4,392	4,296	7,990	7,000
Other profits		-13.2	14.9	-7.0	0.0	Intangible Fixed Assets		164	166	189	184
<b>PBT</b>		<b>1,489.1</b>	<b>1,218.2</b>	<b>2,391.5</b>	<b>2,995.1</b>	Construction in Progress		1,354	2,545	394	394
Prov. of Tax		192.3	187.7	355.4	499.0	Investment Property		11	67	63	58
Minority's Interest		60.4	36.5	80.8	83.6	Long-term Investment		273	26	29	32
<b>PAT to Equity Shareholder</b>		<b>1,236.4</b>	<b>994.0</b>	<b>1,955.2</b>	<b>2,412.4</b>	Other long-term assets		892	843	808	775
EBIT		2,254.7	1,745.2	2,720.0	3,412.2	<b>Long-term Asset</b>		953	852	752	652
EBITDA						<b>Total Asset</b>		<b>8,039</b>	<b>8,795</b>	<b>9,472</b>	<b>8,443</b>
						Payables		<b>17,525</b>	<b>19,016</b>	<b>22,139</b>	<b>21,022</b>
						Other current liabilities		982	1,708	1,656	2,032
						Current Debt		1,110	804	3,139	1,253
						Long-term Debt		4,555	4,850	5,100	4,500
						Other long-term liabilities		1,869	1,456	2,056	1,947
						<b>Total Liability</b>		1,045	1,620	474	474
						<b>Owner's Equity</b>		<b>9,561</b>	<b>10,438</b>	<b>12,425</b>	<b>10,206</b>
						Capital		<b>7,414</b>	<b>8,085</b>	<b>9,120</b>	<b>10,194</b>
						Retained Earnings		3,178	4,191	4,191	4,191
						Funds & Reverses		1,540	1,393	2,412	3,447
						<b>Others</b>		583	290	310	349
						<b>Total Equity</b>		<b>0</b>	<b>0</b>	<b>59</b>	<b>72</b>
						Minority's Interest		<b>7,414</b>	<b>8,085</b>	<b>9,179</b>	<b>10,266</b>
						<b>TOTAL RESOURCES</b>		550	492	535	550
						<b>CASH FLOW STATEMENT</b>		<b>2011A</b>	<b>2012A</b>	<b>2013E</b>	<b>2014F</b>
						<b>Profit before tax</b>		1,489.1	1,218.2	2,391.5	2,995.1
						-Depreciation		541.9	596.2	706.2	981.2
						-Adjustments		875.2	616.2	-130.0	51.6
						+/- Working capital		-2,602.1	-161.2	-262.3	-1,197.4
						<b>Net Operating CFs</b>		<b>304.2</b>	<b>2,269.4</b>	<b>2,705.4</b>	<b>2,830.5</b>
						+/- Fixed Asset		-1,709.3	-1,776.7	-2,158.3	18.1
						+/- Deposit, equity investment		647.5	134.1	196.8	19.3
						Interest, dividend, cash profit received		124.8	-17.2	0.0	0.0
						<b>Net Investing CFs</b>		<b>-937.0</b>	<b>-1,659.7</b>	<b>-1,961.5</b>	<b>37.4</b>
						+/- Capital		-62.9	100.5	0.0	0.0
						+/- Debt		714.5	-118.3	806.5	-651.1
						Dividend and others paid		-2.9	-361.8	76.9	-2,494.0
						<b>Net Financing CFs</b>		<b>648.8</b>	<b>-379.6</b>	<b>883.4</b>	<b>-3,145.1</b>
						+/- cash & equivalents		16.0	230.1	1,627.4	-277.1
						<b>Beginning cash &amp; equivalents</b>		<b>1,047.2</b>	<b>1,064.4</b>	<b>1,294.5</b>	<b>2,917.4</b>
						Impact of exchange rate		1.2	0.0	-4.4	0.0
						<b>Ending cash &amp; equivalents</b>		<b>1,064.4</b>	<b>1,294.5</b>	<b>2,917.4</b>	<b>2,640.3</b>

Please refer to important disclosures at the end of this report

### 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 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% to 10%	-15% to -5%	<-15%
Long-term (over 6 months)	>30%	15% to 30%	-10% to 15%	-15% to -10%	<-15%

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