HOA PHAT GROUP JSC (HSX: HPG)

Moving to the throne

(VND bn)	4Q-FY19	3Q-FY19	+/-(qoq)	4Q-FY18	+/-(yoy)
Net revenue	17,975	15,087	19.1%	14,386	24.9%
PAT	1,917	1,755	9.2%	1,764	8.7%
EBIT	2,460	2,325	5.8%	2,159	13.9%
EBIT margin	13.7%	15.4%	-173bps	15.0%	-133bps

Source: HPG, Rong Viet Securities

4Q/2019 performance – Keep gaining market share

- Owing to new capacity from the Dung Quat Complex, HPG's revenue grew strongly, but PAT grew at a lower pace due to low steel prices (-9% yoy) and high iron ore price (+28% yoy).
- Finished construction steel sales volume came at 807,906 tons (+18% YoY), of which 187,886 tons were sold in the Southern market. HPG's now has a 21% market share in the South at the end of 4Q/2019.

2019 – Both construction steel and agriculture have made progress

- Finished construction steel and steel pipe volumes came at 2.8 million tons (+17% yoy) and 750,800 tons (+15% yoy) respectively. HPG's market share in both construction steel and steel pipe increased significantly to 26% and 32% respectively.
- Agriculture's contribution to 2019 consolidated profit increased significantly from 1.8% in 2018 to 7.4% because of the African swine cholera's positive impact on prices.

FY2020 outlook

We cut our forecast on HPG's construction steel volume by 7% from 4.2 to 3.9 million tons in 2020. The main reason is the impact of the Coronavirus epidemic on HPG's medium-term business results.

We maintain our 2020 ASP forecast at VND 11.3 million per ton of rebar, -6% YoY. Our gross margin forecast remains the same as we predict that iron ore and coking coal prices will also go down.

As a result, our 2020 revenue forecast has been adjusted to VND 79,893 billion (USD 3,444 mn, +26% yoy), slightly lower than our previous forecast. HPG's 2020 NPAT is estimated at VND 11,044 billion (USD 476 mn, +47% yoy).

Valuation and recommendation

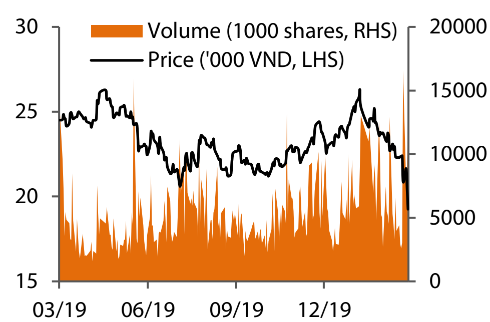
*In general, HPG's 2019 performance was similar to our expectations. Its business results were impacted by the unfavorable steel market. However, we maintain our optimistic view on HPG's growth potential for the next two years owing to the new Dung Quat Steel Complex. As mentioned in our recent company update, HPG is going to become the largest Vietnamese steel maker with high penetration in most steel segments including construction steel, steel pipe and hot-rolled coil (HRC). HPG is also going to take advantage of its modernly integrated mills to improve profitability, cash flows and long-term solvency. Using FCFF, PE and PB methods, we come up with a fair value of VND **27,300** per share (change -13% from our TP in the 2020 strategy report), equivalent to a total return of **42%** based on the closing price on March 13th, 2020. Hence, we reiterate **BUY** recommendation on this stock.*

BUY	+42%
Target price (VND)	27,300
Current market price (VND)	19,250

Stock Info	
Sector	Basic Materials
Market Cap (VND bn)	53,150.7
Current Shares O/S (mn)	2,761.1
3M Avg. Volume (K)	7,270.2
3M Avg. Trading Value (VND bn)	171.2
Remaining Foreign Room (%)	10.9
52-week range ('000 VND)	18.0 – 26.7

	FY2018	FY2019
EPS	3,794	2,556
EPS Growth (%)	-24%	-32.6%
Diluted EPS	2,942	2,556
P/E	7.7	6.6
P/B	1.6	1.4
EV/EBITDA	6.5	7.7
Cash dividend yield (%)	0	0
ROE (%)	21.2%	15.8%

Price performance



Major Shareholders (%)	
Tran Dinh Long	25.15
Vu Thi Hien	7.32
Nguyen Manh Tuan	2.76
Remaining ownership room (%)	10.9

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Exhibit 1: 4Q/2019 Results

(VND Bn)	4Q-FY19	3Q-FY19	+/-(qoq)	4Q-FY18	+/-(yoy)
Net revenue	17,975	15,087	19.1%	14,386	24.9%
Gross profit	2,836	2,702	4.9%	2,561	10.7%
SG&A	376	377	-0.3%	401	-6.4%
Operating income	2,460	2,325	5.8%	2,159	13.9%
EBITDA	3,263	2,977	9.6%	2,737	19.2%
EBIT	2,460	2,325	5.8%	2,159	13.9%
Financial expenses	312	329	-5.0%	207	50.8%
- Interest Expenses	270	266	1.6%	145	86.4%
Dep. and amortization	803	652	23.2%	578	39.0%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	2,285	2,161	5.7%	2,037	12.2%
PAT	1,917	1,755	9.2%	1,764	8.7%
(*) Adjusted PAT	1,917	1,755	9.2%	1,764	8.7%

Source: HPG, Rong Viet Securities

Exhibit 2: 4Q/2019 Performance Analysis

Particulars	4Q-FY19	3Q-FY19	+/-(qoq)	4Q-FY18	*+/-(yoy)*
Profitability Ratios (%)					
Gross Margin	15.8%	17.9%	-213bps	17.8%	-203bps
EBITDA Margin	18.2%	19.7%	-158bps	19.0%	-87bps
EBIT Margin	13.7%	15.4%	-173bps	15.0%	-133bps
Net Margin	10.7%	11.6%	-97bps	12.3%	-160bps
Adjusted Net Margin	10.7%	11.6%	-97bps	12.3%	-160bps
Turnover *(x)					
-Inventories	3.2	2.9	0.3	3.3	-0.1
-Receivables	19.4	15.1	4.2	12.0	7.3
-Payables	7.7	7.1	0.6	4.8	2.9
Leverage (%)					
Total Debt/ Equity	113.0%	111.6%	139bps	92.6%	2,038bps

Source: Rong Viet Securities

Exhibit 3: 1Q/2020 Performance Forecast

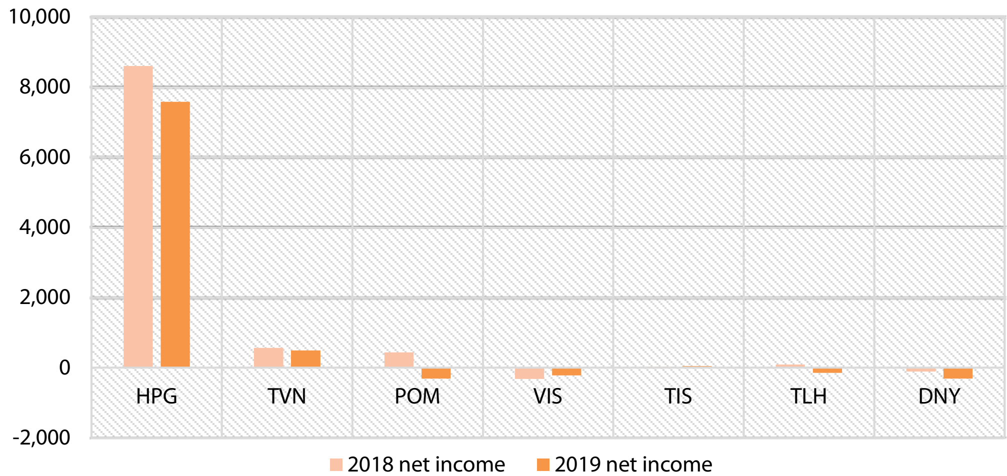
Particulars (VND Bn)	1Q-FY20	+/- qoq	+/- yoy
Revenue	17,600	-2%	+18%
Gross profit	3,548	+25%	+35%
EBIT	3,039	+24%	+32%
NPAT	2,433	+27%	+35%

Source: Rong Viet Securities

Update

Countervailing duties on construction steel and steel billet are likely to be extended. Currently, the duties for steel billets and construction steel is 17.3% and 10.9% respectively. From March 2020, these taxes will be 0% if not extended. According to our survey, most construction steel companies are in favor of an extension. In 2019, steel companies faced difficulties and even suffered losses, such as POM, VIS, TLH, DNY. In the context that other countries are also applying high safeguard duties to protect their domestic steel market, it is essential that Vietnam does that as well. In the case that the safeguard tax is not extended, we believe that only HPG can compete against firms from China, as it has similar technology and geographical advantage.

Figure 1: Leading listed construction steel companies' net income (VND billion)

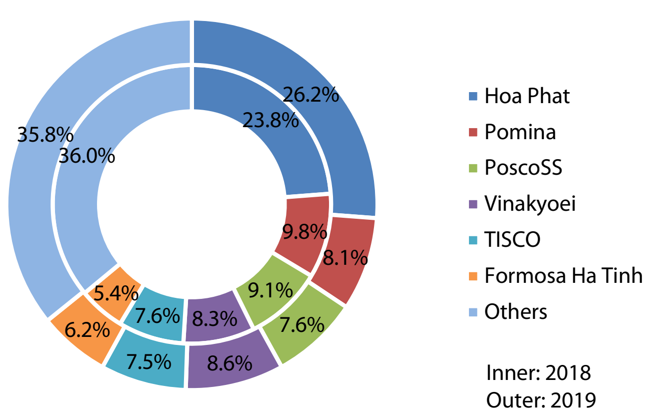


Source: Vietnam Steel Association, RongViet Securities

HPG continued to demonstrate its excellent ability to compete in the steel segment

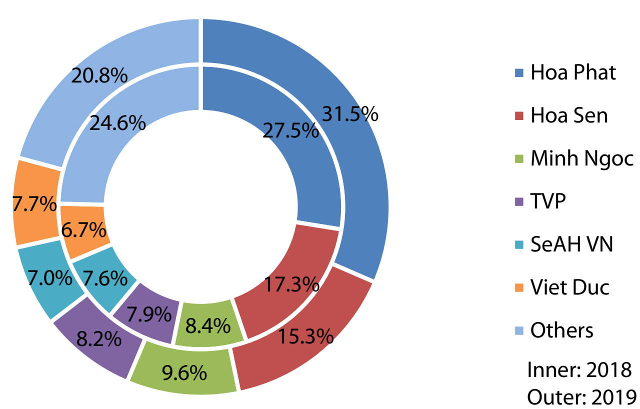
HPG still outperformed its competitors in terms of selling volume. In 2019, both finished construction steel and steel pipe's selling volume increased by 16.7% YoY and 14.8% YoY respectively, while Vietnam's construction steel and steel pipe consumption increased just 6% YoY and 0% YoY respectively. Hence, HPG's market share increased 2.4 and 4.0 percentage points respectively in these segments. Besides, HPG's export volume grew by 11.3% YoY to 265,000 tons, of which 151,000 tons was sold in Cambodia.

Figure 2: Construction steel market share



Source: Vietnam Steel Association, RongViet Securities

Figure 3: Steel pipes market share

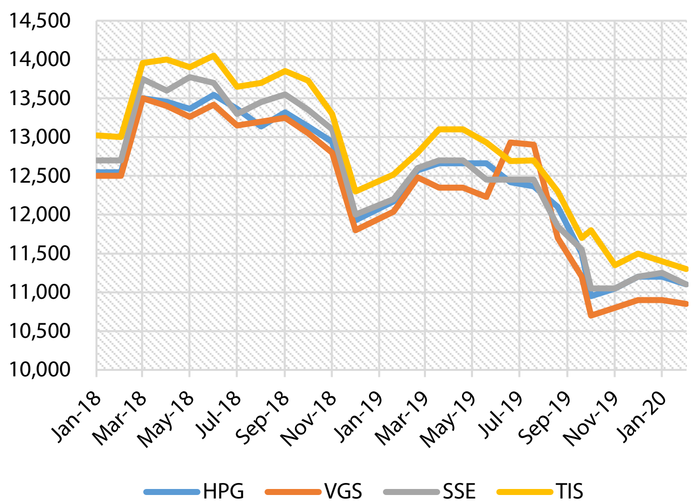


Source: Vietnam Steel Association, RongViet Securities

In the first two months of 2020, HPG's construction steel selling volume still grew strongly as per our expectations, despite the negative impact from Covid-19, owing to a surge in steel billet export volume. For the first two months of the year, while the finished product sales decreased by 15% YoY, steel billet export rose significantly by 370%, leading to a 22% increase in its construction steel selling volume, which was 592 thousand tons. We expect that HPG's selling volume will increase strongly from March on as construction activities will be more dynamic after the Tet holiday and the Covid-2019's peak period in Vietnam and China.

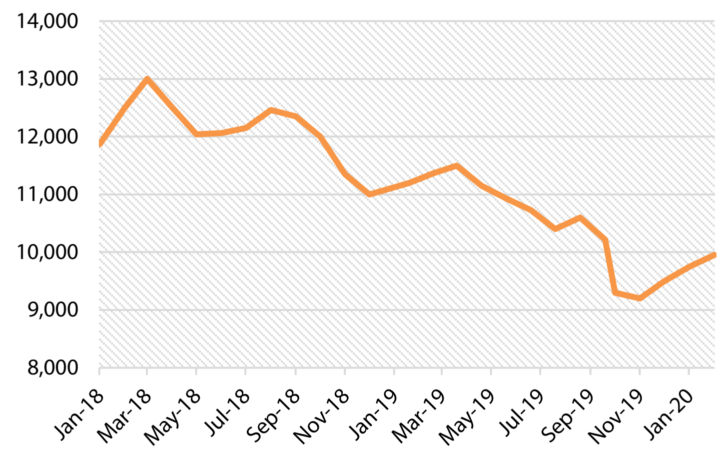
Besides, rebar and wire-rod's export sales also have potential to increase strongly in 2020. After increasing construction steel capacity to 4.2 million ton/year, HPG can export to Cambodia, which is located near from Southern Vietnam, by using its deep-sea international port. Owing to its competitive price and position, HPG is able to be successful in that country against China's manufacturers.

Figure 4: Rebar prices in Northern Vietnam (VND/kg)



Source: Vietnam Steel Association, RongViet Securities

Figure 5: Vietnam's steel billet prices (VND/kg)



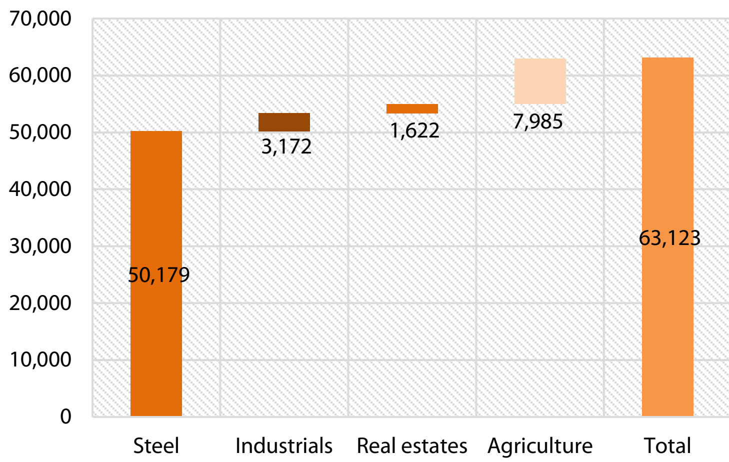
Source: Vietnam Steel Association, RongViet Securities

The agriculture segment has benefited from higher hog prices

In 2019, the agriculture segment has been strongly supported by increasing meat prices, especially hog prices. The segment's net income soared by roughly 270% compared with 2018. However, around 65% of annual net income was recorded in 4Q/2019 because hog prices increased by nearly 80% compared with 3Q/2019 (from VND 40,000/kg to VND 70,000/kg). Since the African swine fever was first detected in February 2019 it has spread to all 63 provinces in Vietnam, forcing the cull of more than 5 million pigs, equivalent to 18% of the total herd, and driving up prices noticeably. Beef prices, an important protein source, also rose.

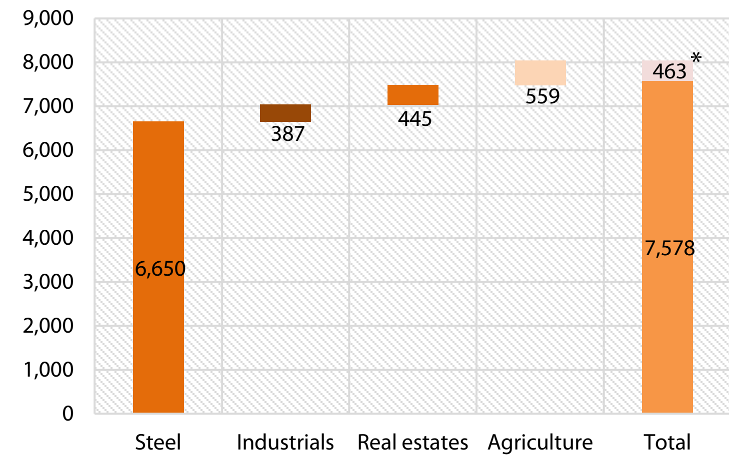
HPG plans to increase hog production by 66.7% from 300,000 heads to 500,000 heads in 2020. We expect hog prices to remain around VND 60,000/kg, 25% higher than the 2019 average.

Figure 6: HPG's revenue, by segment (VND billion)



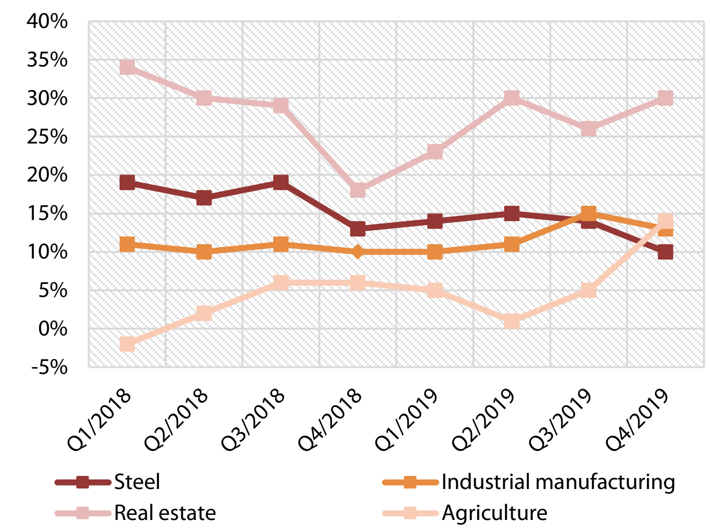
Source: HPG

Figure 7: HPG's net income, by segment (VND billion)



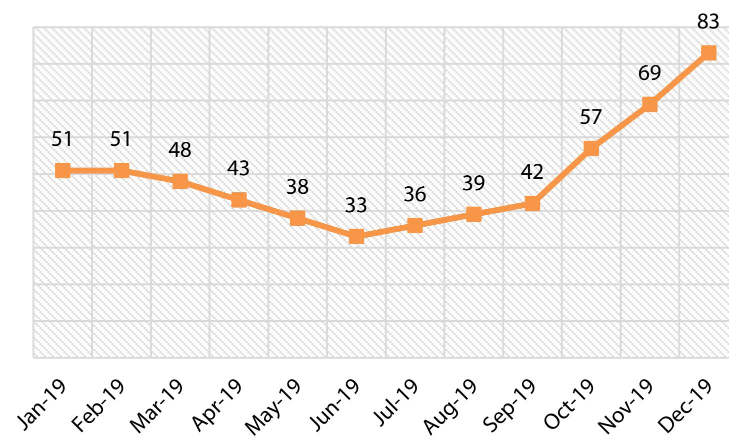
Source: HPG *(*) Intercompany elimination*

Figure 8: HPG's net margin, by segment



Source: HPG

Figure 9: Live hog price movement in 2019



Source: Hooc Mon wholesale market, Ministry of Agriculture & Rural Development (MARD)

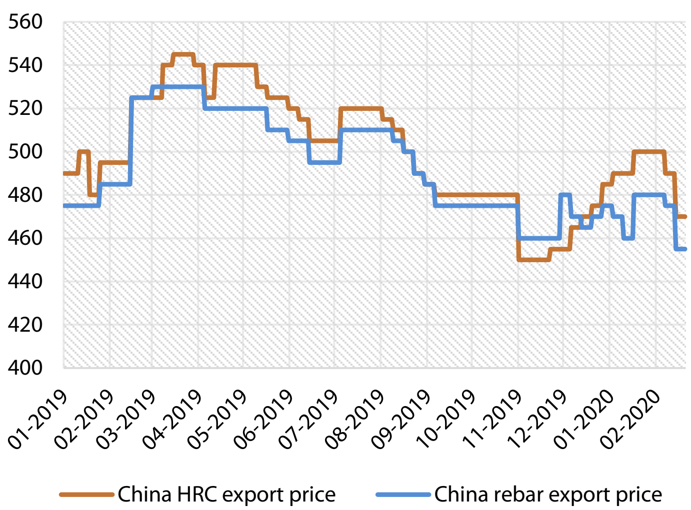
Covid-19's impact on the steel segment

In Vietnam, steel price just decreased slightly, but in China, steel and iron ore prices fell significantly due to lower demand. HRC and rebar prices in China have fallen 6.4% and 5.5% to USD 470/ton and USD 455/ton respectively since the third week of January, before the start of holidays. Iron ore prices (Fe content 62%, CFR China) decreased by 6.4% to USD 83.6/ton on February 20th from USD 89.3/ton on January 24th.

In January, HPG could not increase its ASP due to the impact of Covid-19. The demand for construction steel in 1Q/2020 could decrease as retailers expect that steel prices will drop sharply. This creates a dilemma for other domestic steel companies as they do not want to lower prices due to their high inventories, but they also have to sell products fast to improve cash flow and reduce interest expenses. However, we assume that the growth of the construction industry is not likely to decrease significantly this year.

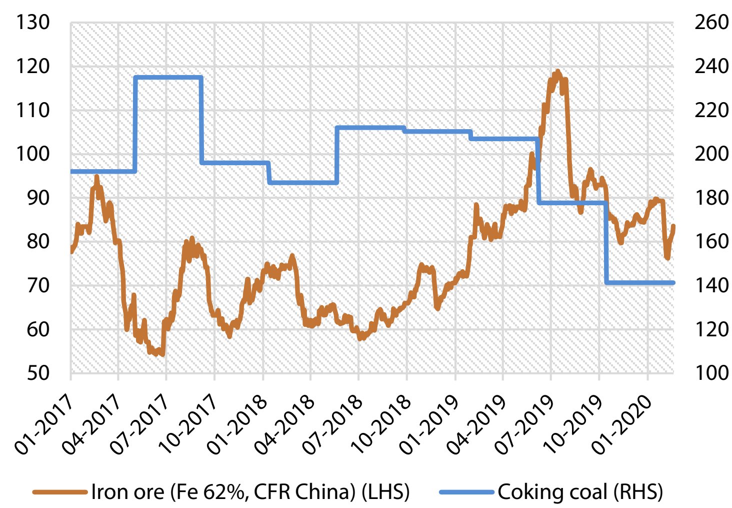
We forecast that the domestic rebar price is likely to decrease by 6% in 2020 because of high inventories and the fact that China's manufacturers will export more. On top of that domestic companies are under high pressure from interest expenses. However, iron ore and coking coal prices will also decrease, hence, HPG's margin will not be affected significantly.

Figure 10: HRC and rebar price in China (USD/ton)



Source: Bloomberg

Figure 11: Iron ore and coaking coal price (USD/ton)



Source: Bloomberg

Dung Quat steel complex

HPG's management expects the Dung Quat Complex could provide HRC as of April 2020. However, production could be low at the beginning as Chinese experts and workers cannot return to Vietnam after the Tet holiday. Hence, we revised our forecast on HRC's production volume in 2020 by 10% lower, to 720,000 tons.

HPG announced its plan for the Dung Quat Expansion phase, which requires total investment of VND 60,000 billion, of which VND 50,000 billion will be CAPEX and the remaining working capital. The company will borrow VND 20,000 billion from banks. If this plan is accepted by the Government and HPG's shareholders, the expansion will start in 2023 and take roughly three years to be completed. Out of the new HRC capacity, 1.5 million tons will be used to produce medium-sized steel sections and mechanic steel.

We have not yet included this project in HPG's valuation, partly due to the fact that this a long-term project. Our preliminary assessment is that this project has several positives: (1) HRC is still imported, which effectively means ample room for new local producers; (2) steel beams and mechanic steel allow HPG to enter potential and low-competitive niche markets. More importantly, HPG' downstream factories can consume roughly 40-50% of its HRC capacity, hence, allowing the company to reduce selling pressure and expand the flat steel segment's gross margin. In our next HPG update report, we will analyze the project thoroughly to determine the incremental value for the company.

Table 1: Dung Quat – Expansion phase's capacity

Product	Capacity (ton)
Hot-rolled coil	3,000,000
Medium-sized steel beam	1,000,000
High-quality wire rod	500,000
Mechanic steel	500,000

Source: HPG

1Q/2020 performance forecast

We forecast that HPG's revenue and net profit will increase 18% YoY and 35% YoY respectively. In terms of revenue, the steel segment and agriculture will account for 77.0% and 17.6% respectively. Regarding net income, steel and agriculture will contribute 75.2% and 17.8%

respectively. We expect that construction steel's selling volume will reach 957 thousand tons (+31% YoY), of which 365 thousand tons will be sold in March. Meanwhile, rebar and billet prices are expected to be 11,000 and 10,050 VND/kg respectively in March.

Valuation

We use three methods to evaluate the stock. We apply a PE ratio of 6.1x and PB ratio of 1.4x. Our fair value comes at **VND 27,300 value per share**, implying **a total stock return of 42%** as of the closing price on March 13th, 2020 (-13% change from our latest TP in 2020 strategy report).

Table 2: HPG valuation

Method	Weight	Price	Contribution
FCFF	40%	29,694	11,878
P/E (6.1 x)	30%	23,012	6,903
P/B (1.4x)	30%	28,557	8,567
Target price			**27,300**
Current market price			19,250
Total stock return			**42%**

Source: Rong Viet Securities

VND Billion

INCOME STATEMENT	FY2018	FY2019	FY2020F	FY2021F
Revenue	55,836	63,658	79,893	96,217
COGS	44,166	52,473	63,789	76,157
Gross profit	11,671	11,185	16,104	20,059
Selling Expenses	679	873	1,262	1,636
G&A Expenses	442	569	1,048	981
Finance Income	294	471	101	150
Finance Expenses	772	1,182	1,428	1,757
Other profits	-1	66	66	66
PBT	10,071	9,097	12,531	15,900
Prov. of Tax	1,471	1,518	1,487	1,613
Minority Interest	28	71	0	0
PAT to Equity S/H	8,573	7,508	11,044	14,287
EBIT	10,550	9,743	13,794	17,442
EBITDA	12,834	12,381	19,550	23,972

FINANCIAL RATIO	FY2018	FY2019	FY2020F	FY2021F
Growth (%)				
Revenue	21.0	14.0	25.5	20.4
Operating Income	10.3	-3.5	57.9	22.6
EBITDA	9.6	-7.6	41.6	26.4
PAT	7.1	-12.4	47.1	29.4
Total Assets	49.2	29.5	7.6	10.7
Equity	25.4	17.6	21.8	23.2
Profitability (%)				
Gross margin	20.9	17.6	20.2	20.8
EBITDA margin	23.0	19.4	24.5	24.9
EBIT margin	18.9	15.3	17.3	18.1
Net margin	15.4	11.8	13.8	14.8
ROA	11.0	7.4	10.2	11.9
ROE	21.2	15.8	19.0	20.0
Efficiency				(times)
Receivable Turnover	14.3	17.8	9.5	7.7
Inventory Turnover	3.1	2.7	2.6	2.3
Payable Turnover	3.7	5.6	5.6	6.7
Liquidity				(times)
Current	1.1	1.2	1.6	2.0
Quick	0.5	0.4	0.6	0.9
Finance Structure (%)				
Total Debt/Equity	60.0	77.1	51.8	38.0
Current Debt/Equity	28.4	35.4	26.1	24.5
Long-term Debt/Equity	31.6	41.7	25.7	13.5

VND Billion

BALANCE SHEET	FY2018	FY2019	FY2020F	FY2021F
Cash and cash equivalent	2,516	4,565	5,572	9,408
Short-term investments	3,725	1,374	1,443	1,732
Account receivable	3,915	3,575	8,389	12,508
Inventories	14,115	19,412	24,878	32,748
Other current assets	1,743	1,546	1,855	2,226
Property, plant & equipment	49,944	68,242	64,218	59,270
Acquired intangible assets	305	331	315	299
Long-term investments	67	26	24	23
Other non-current assets	1,690	1,971	2,069	2,173
Total assets	78,019	101,041	108,764	120,385
Account payable	12,029	9,340	11,482	11,424
Short-term borrowings	11,495	16,838	15,154	17,470
Long-term borrowings	12,811	19,842	14,882	9,673
Other non-current liabilities	506	7,163	7,879	8,667
Bonus and welfare fund	775	820	1,206	1,561
Technology-science, dev. fund	0	0	0	0
Total liabilities	37,616	54,003	50,603	48,795
Common stock and APIC	24,451	30,822	30,813	30,813
Treasury stock (enter as -)	0	0	0	0
Retained earnings	15,111	15,858	26,240	39,670
Other comprehensive income	0	1	1	1
Inv. and Dev. Fund	919	924	924	924
Total equity	40,481	47,605	57,977	71,407
Minority Interest	128	183	183	183

VALUATION RATIO (*)	FY2018	FY2019	FY2020F	FY2021F
EPS (VND)	3,794	2,556	3,760	4,864
P/E (x)	7.7	6.6	6.0	4.6
BV (VND)	14,661	17,241	20,998	25,862
P/B (x)	1.6	1.4	1.1	0.9
DPS (VND/cp)	0	0	0	0
Dividend yield (%)	0%	0%	0%	0%

VALUATION MODEL	Price	Weight	Average
FCFF	29,694	40%	11,878
P/E (6.1x)	23,012	30%	6,903
P/B (1.4x)	28,557	30%	8,567
Target price (VND)			**27,300**

VALUATION HISTORY	Price	Recommendation	Period
21/11/2016	31,250	ACCUMULATE	Long-term
15/03/2017	35,556	BUY	Long-term
28/12/2018	38,900	ACCUMULATE	Long-term
16/01/2020	33,400	BUY	Intermediate

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%

ABOUT US

RongViet Securities Corporation (RongViet) was established in 2007. licensed to perform the complete range of securities services including brokerage. financial investment. underwriting. financial and investment advisory and securities depository. RongViet now has an operating network that spreads across the country. Our major shareholders. also our strategic partners. are reputable institutions. i.e Eximbank. Viet Dragon Fund Management. etc... Along with a team of the professional and dynamic staffs. RongViet has the man power as well as the financial capacity to bring our clients the most suitable and efficient products and services. Especially. RongViet was one of the very first securities firms to pay the adequate attention to the development of a team of analysts and the provision of useful research report to investors.

The **Analysis and Investment Advisory Department** of RongViet Securities provides research reports on the macro-economy. securities market and investment strategy along with industry and company reports and daily and weekly market reviews.

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