Hang Xanh Motors Service JSC (HSX – HAX)

Benefiting from the favorable luxury car market

Particulars (VND B)	Q3-FY18	Q2-FY18	*+/- QoQ*	Q3-FY17	*+/- YoY*
Net revenue	1,142	1,155	-1.2%	945	20.8%
PAT	30	32	-4.8%	39	-22.8%
EBIT	52	49	6.8%	60	-12.8%
EBIT margin	4.6%	4.2%	34bps	6.3%	-177bps

Source: HAX, Rong Viet Securities

3Q 2018 Performance: Revenue was up, but profits went down

In 3Q 2018, total revenue increased by 21% YoY to VND 1,142 billion. Revenues from car sales reached VND 1,056 billion (+18% YoY), mostly from sales of CKD cars. Due to the challenges of Decree 116, no Mercedes Benz (MBV) cars were imported in the first eight months of the year. This situation made CBU cars sales decline considerably. Surprisingly, total sales of HAX in 3Q 2018 still improved sharply. This can be explained by the considerable rise in CKD cars sales, which compensated for the loss of CBU cars sales. Despite the increase in sales, 3Q 2018 NPAT still fell by 23% YoY due to the slump of incentives. In the quarter, this amount of incentives was only VND 19 billion (-50% YoY). As a result, in 9M 2018, revenue and NPAT reached VND 3,280 billion (+18% YoY) and VND 64 billion (+9% YoY), respectively.

2018 earnings may see a strong growth amid difficulties in cars import

As the supply of MBV showed signs of recovery in late 2018, the market share of HAX moved up significantly to 37% from 27% in 2017. We forecast that 2018 sales will reach 2,260 cars (+16.8% YoY), resulting in a 17% YoY increase in 2018 revenue.

In 2018, MBV faced challenges in importing CBU cars and change in the Vehicle Identification Number (VIN) convention of the key car line (GLC). Therefore, we forecast that the amount of incentives, which MBV offers to HAX, may decrease by 20% YoY to VND 87 billion. However, because of improved profit margin of the automotive distribution segment, a core business of HAX, we still expect 2018 NPAT to reach VND 112 billion (+34% YoY), corresponding to an EPS of 3,226 VND/share.

Valuation and Recommendation:

At current market price, HAX is trading at a P/E ratio of 5.4x, which we consider quite attractive given the positive prospects for 2019. We expect a growth in earnings of 9.2% YoY in 2019 thanks to anticipated improvement in the high-range automobile segment. In the long-term, we forecast that profits of the dealer will see a CAGR of 11% for the next five years. That is based on the strong position of MBV in the luxury auto industry and HAX's ambitions to expand market share of Mercedes car sales.

*Our target price is **VND 19,600 per share**. This target price, coupled with a VND 1,500 cash dividend in the next 12 months, would yield a total return of **30%** (calculated based on the closing price on 21 December). Therefore, we have a **BUY** recommendation on HAX.*

BUY 30%

CMP (VND)	16,200
Target Price (VND)	19,600
Cash Dividend (VND	1,500

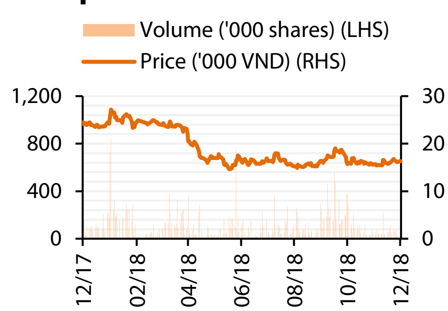
** Expected in the next 12 months*

Stock Info

Sector	Automobile & Parts
Market Cap (VND B)	553.2
Current Shares O/S	35,013,399
Beta	0.53
Free Float (%)	36.9
52-week High	27,200
52-week Low	14,600
Avg. Daily Volume (20 sessions)	60,131

	FY2017	Current
EPS	3,611	2,571
EPS Growth (% YoY)	8.1	22
Adjusted EPS	2,407	2,571
P/E	9.7	5.4
P/B	1.4	1.2
EV/EBITDA	7.8	6.8
Cash Dividend	1,500	1,500
ROE (%)	21.8	21.5

Price performance



Major Shareholders (%)

Mr. Do Tien Dung	23.9
Foreign Ownership room (%)	36.9

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Exhibit 1: Q3 2018 Results

Particulars (VND B)	Q3-FY18	Q2-FY18	+/- (QoQ)	Q3-FY17	+/- (YoY)	3Q-FY18	+/-(YoY)
Net revenue	1,142	1,155	-1.2%	945	20.8%	3,281	18.9%
Gross profit	70	64	8.0%	55	26.1%	166	58.6%
SG&A	37	35	4.7%	33	10.4%	114	19.3%
Operating income	33	29	12.0%	22	50.4%	53	-247.3%
EBITDA	62	58	6.5%	60	2.4%	142	22.0%
EBIT	52	49	6.8%	60	-12.8%	113	10.4%
Financial expenses	14	9	58.5%	10	37.7%	32	30.9%
- Interest Expenses	14	9	59.5%	10	37.7%	32	30.8%
Dep. and amortization	10	9	4.9%	1	1,637.5%	29	105.9%
Non-recurring items (*)							
Extraordinary items (*)							
PBT	38	40	-4.7%	50	-23.2%	81	9.8%
PAT	30	32	-4.8%	39	-22.8%	64	4.1%
(*) Adjusted PAT	30	32	-4.8%	39	-22.8%	64	

Source: HAX, Rong Viet Securities

Exhibit 2: Q3 2018 Performance Analysis

Particulars	Q3-FY18	Q2-FY18	+/- (QoQ)	Q3-FY17	+/- (YoY)
Profitability Ratios (%)					
Gross Margin	6.1	5.6	51.7bps	5.8	25.9bps
EBITDA Margin	5.4	5.0	39.2 bps	6.4	-97.4bps
EBIT Margin	4.6	4.2	34.2 bps	6.3	-176.5bps
Net Margin	2.7	2.8	-10.2 bps	4.2	-150.0bps
Adjusted Net Margin	2.7	2.8	-10.2 bps	4.2	-150.0bps
Turnover *(x)					
-Inventories	7	7	-0.9	5	1.3
-Receivables	11.3	11.8	-0.4	15.1	-3.8
-Payables	18	28	-10.5	40	-22.5
Leverage (%)					
Total Debt/ Equity	271.0	296.2	-2,522.6 bps	317.1	-4,611.4 bps

Source: HAX, (*) Annualized turnover

Exhibit 3: Q4 2018 Performance Forecast

Particulars (VND Billion)	Q4-2018	+/- (QoQ)	+/- (YoY)
Revenue	1,208	5.9%	12.5%
Gross profit	63	-9.2%	54.2%
EBIT	64	21.7%	43.7%
NPAT	48	58.8%	86.7%

Source: HAX, Rong Viet Securities

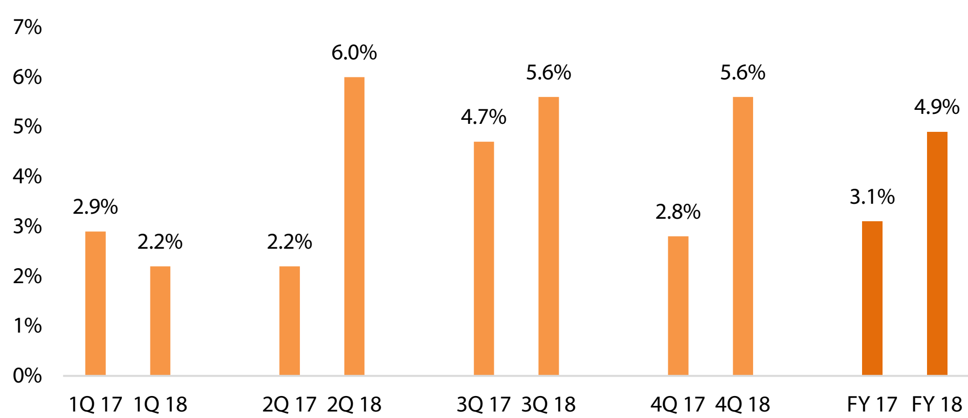
Update

Gross Profit Margin of the Automobile Business May Peak in 2018

GPM of HAX's core business has benefited from difficulties in the automobile market since 2Q 2018. Although CBU cars could not enter the Vietnamese market from January 2018 due to Decree 116, the lack of automobile supply has just started to become evident since the second quarter. In 1Q 2018, HAX had a large inventories, which were cars from 2017. Hence, HAX offered discounts to clear its old inventories. However, since 2Q 2018, as other automobile brands, supply of Mercedes - Benz brand could not meet pent-up demand. In 2Q and 3Q 2018, the firm therefore did not have to give customers a discount to boost sales as they did in 1Q 2018, leading to an uptick in GPM. Given this, GPM of HAX increased from 2.6% and 5.8 % in 2Q and 3Q 2017 to 5.6% and 6.1% in 2Q and 3Q 2018, respectively.

In the last quarter of 2018, the shortage of automobiles may support GPM. Currently, Mercedes – Benz Vietnam has not had enough CBU and CKD vehicles to meet the high domestic demand. In terms of CBU cars, long inspection time has forced the firm to delay deliveries to customers. According to Decree 116, once vehicles arrive in Vietnam, a sample is selected from every batch of imports to run tests for emission, quality and technical safety. The inspection is repeated shipment after shipment even if it is the same car model. Therefore, after arrival at the port, it takes around two to three months for delivering vehicles to customers. Regarding CKD automobiles, change in VIN convention of GLC car line, which is the key car line of Mercedes – Benz Vietnam, has made MBV postpone registry for those cars in recent months. Hence, delivery of these cars has been delayed. To sum up, as Mercedes – Benz cars demand exceeds supply, we expect that selling prices will remain favorable for HAX in 4Q 2018. We forecast that GPM will be high in the fourth quarter, at around 5.6%. As a result, the figure for 2018 is expected to reach 4.9%.

Figure 1: Gross Profit margin of the automobile business per quarter



Source: HAX, Rong Viet Securities

Distribution of other brands supports long-term growth

In 2019, HAX plans to distribute Nissan and Vinfast vehicles. In the short-term, the benefits from this could be negligible. Can Tho Automobile Engineering JSC will open a Nissan showroom in December 2018. Currently, Nissan just accounts for a minority of the market in the Vietnam auto market, 1%, with more than 20 dealerships nationwide. Therefore, we forecast that the average sale per showroom will be 200 units next year. Revenue and earnings from the distribution of Nissan cars in 2019 is expected to reach VND 105 billion and VND 2 billion, respectively, contributing to 2% of HAX's revenue and profits. Regarding Vinfast, PTM, a subsidiary of HAX, registered to be a dealer of this new brand. In 2019, we estimate that the Vinfast retail activity will bring marginal profits to HAX, considering that Vinfast needs time to solidify its position in a highly competitive auto industry. However, we believe that the distribution of Nissan and Vinfast will pave the way for long-term earnings growth.

The outlook of HAX in 2019 will benefit from the favorable luxury car market

Sales of HAX in 2019 are forecasted to grow significantly thanks to a positive outlook for the luxury market. Supply of luxury cars may recover strongly in 2019 as most imported cars can enter the Vietnamese market as of late 2018. In addition, demand for high-end cars in 2019 may remain strong for three main reasons: (1) limited supply in 2018 has not met the high demand for luxury cars. (2) Vietnam-EU FTA may be a catalyst to stimulate demand for the sector and (3) the so-called 'affluent' population is growing, at a CAGR of 29% (2012- 2020), according to a report by the Boston Consulting Group (BCG). Therefore, sales of HAX in 2019 are expected to grow by 20% YoY.

Incentives may compensate for the decrease in GPM, resulting in a slight improvement in NPAT. As above mention, GPM of the company may have peaked in 2018. We forecast that the figure will decrease in 2019. The automotive market in 2019 will be more competitive, as it is not anticipated to suffer from the shortages of auto supply as in 2018. Hence, to maintain their market share, car dealers may have to decrease selling prices, resulting in a slight fall in gross profit margin (GPM). The figure is forecasted to go down to 4% in 2019, from 4.8% in 2018.

In addition, we predict that MBV will have to ease incentive policies to stimulate dealers to push sales. Hence, we estimate that the amount of incentive, which MBV will offer to HAX in 2019, may increase 36% YoY to VND 118 billion. As a result, 2019 NPAT is forecasted to witness a growth of 9.2% to VND 123 billion, corresponding to an EPS of VND 3,523.

Valuation and Recommendation:

At current market price, HAX is trading at a P/E ratio of 5.4x, which we consider quite attractive given the positive prospects for 2019. We expect a growth in earnings of 9.2% YoY in 2019 thanks to anticipated improvement in the high-range automobile segment. In the long-term, we forecast that profits of the dealer will see a CAGR of 11% for the next five years. That is based on the strong position of MBV in the luxury auto industry and HAX's ambitions to expand market share of Mercedes car sales.

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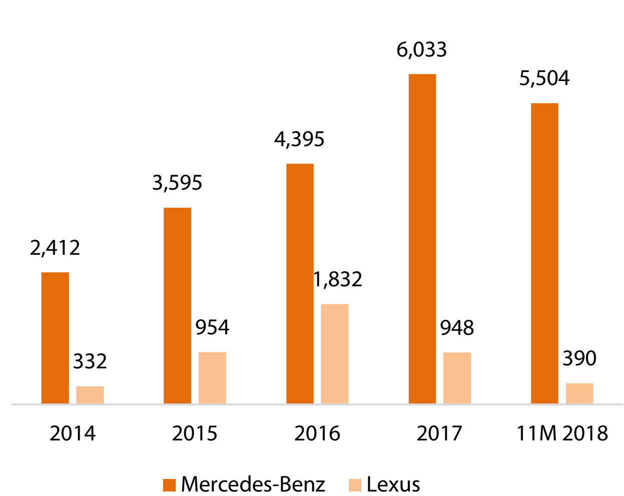
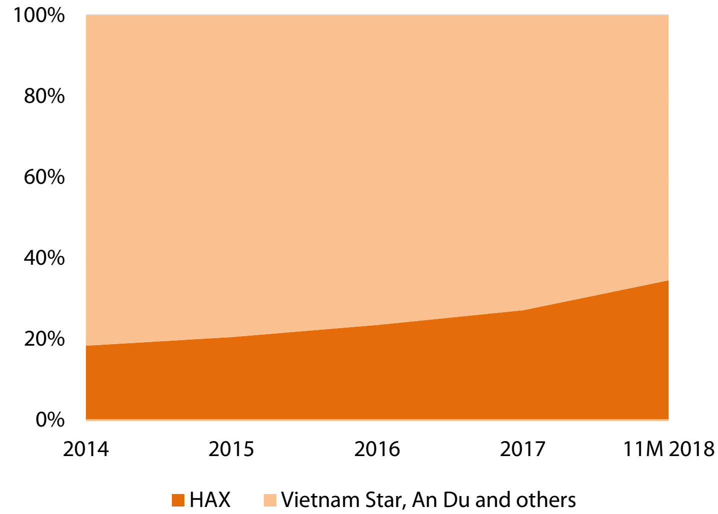
Figure 2: Mercedes and Lexus sales in Vietnam



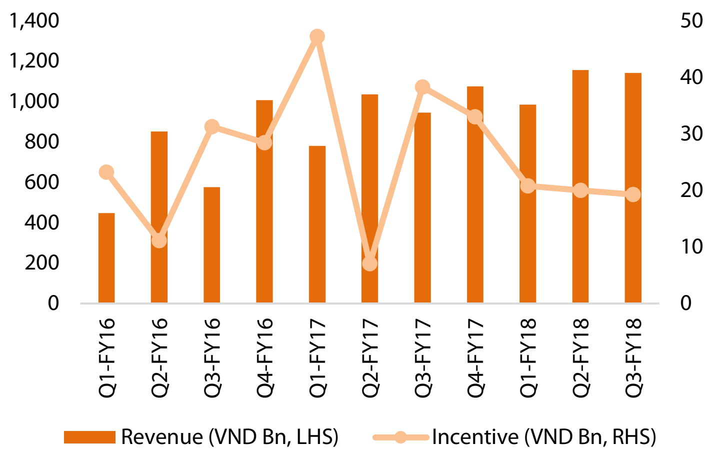
Source: VAMA, Rong Viet Securities

Figure 3: HAX's market share



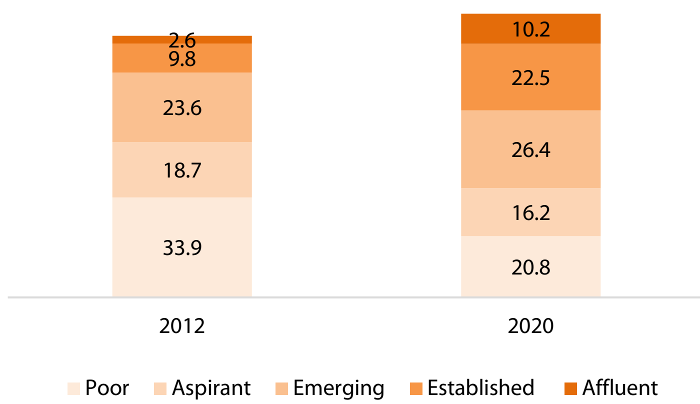
Source: HAX, Rong Viet Securities

Figure 4: HAX's revenues from selling cars and incentive from MBV



Source: HAX, Rong Viet Securities

Figure 5: Vietnam has a fast-growing middle and affluent class population (millions)



Source: BCG, Rong Viet Securities
** The MAC cutoff is monthly per capita income of USD 190*

VND Billion

INCOME STATEMENT	FY2016	FY2017	FY2018E	FY2019F
Revenue	2,880	3,833	4,489	5,382
COGS	2,780	3,688	4,260	5,146
Gross profit	**100**	**146**	**229**	**236**
Selling Expense	59	84	103	120
G&A Expense	23	41	46	54
Finance Income	1	0	1	1
Finance Expense	12	36	36	40
Other profits	91	125	96	130
PBT	**97**	**110**	**141**	**154**
Prov. of Tax	18	26	28	31
Minority's Interest	0	0	0	0
PAT to Equity S/H	**78**	**84**	**113**	**123**
EBIT	109	146	177	194
EBITDA	124	175	204	222

%

FINANCIAL	FY2016	FY2017	FY2018E	FY2019F
Growth				
Revenue	58.1	33.1	17.1	19.9
Operating Income	113.5	34.1	21.5	9.3
EBITDA	142.9	41.1	16.8	8.8
PAT	170.7	8.1	34.0	9.2
Total Assets	107.2	71.5	4.8	14.3
Equity	133.2	28.0	21.2	15.1
Profitability				
Gross margin	3.5	3.8	5.1	4.4
EBITDA margin	4.3	4.6	4.5	4.1
EBIT margin	3.8	3.8	4.0	3.6
Net margin	2.7	2.2	2.5	2.3
ROA	9.1	5.7	7.3	7.0
ROE	25.9	21.8	24.2	22.9
Efficiency				
Receivables Turnover	13.4	10.7	10.4	10.4
Inventories Turnover	7.1	5.9	6.6	6.6
Payables Turnover	12.8	18.7	17.4	17.4
Liquidity				
Current	1.2	1.0	1.1	1.1
Solvency				
Total Debt/Equity	112.1	229.5	176.9	172.1
Current Debt/Equity	112.1	229.5	176.9	172.1
Long-term Debt/Equity	0.0	0.0	0.0	0.0

VND Billion

BALANCE SHEET	FY2016	FY2017	FY2018E	FY2019F
Cash and cash equivalents	41	69	57	53
Short-term investments	0	0	0	0
Accounts receivable	215	359	430	516
Inventories	390	629	642	775
Other current assets	18	48	43	56
Property, plant & equipment	116	293	298	291
Acquired intangible assets	78	71	69	68
Long-term investments	0	0	0	0
Other non-current assets	5	8	8	9
Total assets	**861**	**1,476**	**1,547**	**1,768**
Accounts payable	217	198	245	296
Short-term borrowings	338	885	827	927
Long-term borrowings	0	0	0	0
Other non-current liabilities	1	4	3	3
Bonus and Welfare fund	0	0	0	0
Technology-science, dev. fund	0	0	0	0
Total liabilities	**556**	**1,087**	**1,076**	**1,226**
Common stock and APIC	206	297	350	350
Treasury stock (enter as -)	0	0	0	0
Retained earnings	88	84	113	184
Other comprehensive income	0	0	0	0
Inv. and Dev. Fund	8	4	4	4
Total equity	**301**	**386**	**468**	**539**
Minority Interest	**4**	**4**	**4**	**4**

VALUATION RATIO	FY2016	FY2017	FY2018E	FY2019F
EPS (dong)	2,227	2,407	3,226	3,523
P/E (x)	7.4	9.7	5.0	4.6
BV (dong)	21,184	16,525	13,357	15,380
P/B (x)	1.9	2.2	1.2	1.0
DPS (dong/cp)	0	1,500	1,500	1,500
Dividend yield (%)	0.0	6.4	9.3	9.3

VALUATION MODEL	*Price*	*Weight*	*Average*
PE	23,016	50%	11,508
EV/EBITDA	16,241	50%	8,120
Target price (dong)			**19,629**

VALUATION HISTORY	*Price*	*Recommendation*	*Period*
02/5/2018	29,000	Neutral	1-year
04/16/2018	29,500	Buy	1-year

RESULT UPDATE

This report is created for the purpose of providing investors with an insight into the discussed company that may assist them in the decision-making process. The report comprises analyses and projections that are based on the most up-to-date information with the objective that is to determine the reasonable value of the stock at the time such analyses are performed. Through this report, we strive to convey the complete assessment and opinions of the analyst relevant to the discussed company. To send us feedbacks and/or receive more information, investors may contact the assigned analyst or our client support department.

RATING GUIDANCE

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

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