SMC TRADING INVESTMENT JSC (HSX: SMC)

Increasing steel price boosts the net income to a new peak in 1Q

(VND bn)	4Q-FY20	3Q-FY20	+/- qoq	4Q-FY19	+/- yoy
Net revenue	4,478	4,132	8%	3,943	14%
PAT	148	98	52%	-6	N/A
EBIT	171	117	46%	14	1146%
EBIT margin	3.8%	2.8%	10bps	0.3%	35bps

Source: SMC, Rong Viet Securities

2020: Favorable HRC price and recovering demand boosted net income

- Despite COVID-19's negative impact, sale volume increased by 2.4% YoY due to the recovery in the manufacturing and construction industry in 2H.
- GPM improved from 2.9% in 2019 to 5.1% in 2020 as HRC price surged by 19% QoQ and 18% QoQ in 3Q and 4Q respectively, highest increases over the last three years.
- High profitability and sales volume in 2H supported the annual NPAT which reached VND 300 billion, up 211% YoY.

2021: Steel prices still support the performance in 1H

We think, at the price of USD 720/ton, the HRC price is unsustainable and can decrease to USD 510/ton in 4Q2021. However, SMC can still be profitable owing to its ability to manage working capital, proved in the pandemic, and a higher the manufacturing segment's portion in NPAT. We expect HRC's average price will be USD 580/ton in 2021.

We expect that SMC's selling volume will grow by 5% YoY, reaching 1.4 million tons. In which, its steel pipe volume will increase by 16% YoY to 220.000 tons and its processed coil volume can reach 440.000 tons, up 8% YoY. Trading volume will grow by 1% YoY to 680.000 tons.

In addition, we forecast its average selling price will up by 12%, resulting in a revenue increase of 17% YoY. SMC's gross margin and NPAT are forecasted to be 4.8% and VND 340 billion (+13% YoY) respectively.

SMC's 2021 growth driver will mostly come from the steel pipe factory and the Da Nang Coil Center. It has planned to run two new processing factories by the end of this year, which will be company's growth engines in 2022 if SMC meets its target.

Valuation and recommendation

SMC's business is becoming more sustainable as its coil service and production segments are playing a more important role and its trading risk is managed better. Besides, SMC has strong competitiveness owing to its high-quality services, diversified products, and presence in key areas. In the coil processing segment, SMC's new contract of supplying coil service for Samsung shows it can meet high standards of product quality, material sources and on-time delivery. Investments in new coil processing factories will help the company to seize opportunities as FDI inflows are expected to surge, leading to stronger demand.

*Taking into account the better outlook for the steel industry, we rise up SMC's P/B to 1.0 (previously 0.6x) and P/E to 5.0 (previously 4.3x). Besides, we adjust the forecast for NPAT in 2021 from VND 176 billion to VND 340 billion due to the surging HRC price, which increased 40% over last three months. Hence, we revise up our target price to **VND 30,200 from 14.100 per share**. Together with a cash dividend in the next 12 months of VND 1,000/share, the total return is **13%**, based on the closing price of VND 27,600/share as of March 10th, 2021. Hence, we recommend to **ACCUMULATE** this stock.*

ACCUMULATE 13%

Target price (VND)	30,200
Current market price (VND)	27,600
Cash Dividend (VND)*	1,000

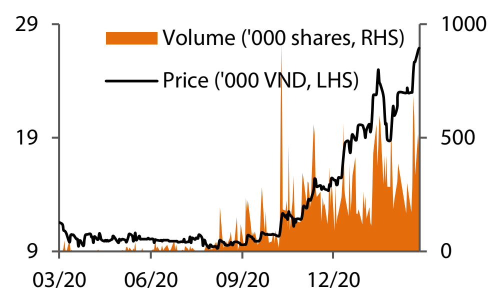
** Expected in the next 12 months*

Stock Info

Sector	Basic Materials
Market Cap (VND billion)	1,584.0
Current Shares O/S	60,923,000
Avg. Daily Volume (in 20 sessions)	354,240
Free float (%)	64
52 week High	26,900
52 week Low	9,275
Beta	0.5

	FY2019	TTM
EPS	1,595	2,422
EPS Growth (%)	-48.9	51.9
Diluted EPS	1,596	2,422
P/E	6.9	6.1
P/B	0.5	0.6
EV/EBITDA	6.6	8.4
Cash dividend yield (%)	9.1	6.8
ROE (%)	7.1	8.9

Price performance



Major Shareholders (%)

Hanwa Co Ltd	19.7
Nguyen Thi Ngoc Loan	14.4
Remaining ownership room (%)	15.5

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Exhibit 1: 4Q/2020 Results

(VND Bn)	4Q-FY20	3Q-FY20	+/- (qoq)	4Q-FY19	+/- (yoy)
Net revenue	4,478	4,132	8.4%	3,943	13.6%
Gross profit	325	218	48.7%	81	299.1%
SG&A	154	102	51.3%	68	127.4%
Operating income	171	117	46.4%	14	1146.1%
EBITDA	238	142	67.7%	36	555.4%
EBIT	171	117	46.4%	14	1146.1%
Financial expenses	7	18	-60.1%	25	-70.9%
- Interest Expenses	*35*	*26*	*35.6%*	*33*	*6.3%*
Dep. and amortization	68	26	164.7%	23	198.4%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	170	119	42.2%	4	3934.5%
PAT	148	98	51.6%	-6	-2426.2%
(*) Adjusted PAT	148	98	51.6%	-6	-2426.2%

Source: SMC, Rong Viet Securities

Exhibit 2: 4Q/2020 Performance Analysis

Particulars	4Q-FY20	3Q-FY20	+/- (qoq)	4Q-FY19	+/- (yoy)
Profitability Ratios (%)					
Gross Margin	7.2%	5.3%	20bps	2.1%	52bps
EBITDA Margin	5.3%	3.4%	19bps	0.9%	44bps
EBIT Margin	3.8%	2.8%	10bps	0.3%	35bps
Net Margin	3.3%	2.4%	9bps	-0.2%	35bps
Adjusted Net Margin	3.3%	2.4%	9bps	-0.2%	35bps
Turnover *(x)					
-Inventories	10.9	12.3	-1.4	12.1	-1.1
-Receivables	10.3	9.3	1.0	10.1	0.2
-Payables	8.4	8.9	-0.6	9.7	-1.4
Leverage (%)					
Total Debt/ Equity	321.3%	281.6%	397bps	277.2%	441bps

Source: SMC, Rong Viet Securities. (*) annualized

Exhibit 3: 1Q/2021 Performance Forecast

Particulars (VND Bn)	1Q-FY21	+/-qoq	+/-yoy
Revenue	4,572	2%	33%
Gross profit	352	8%	107%
EBIT	270	58%	160%
NPAT	218	47%	2,034%

Source: Rong Viet Securities

- Revenue is going to increase by 33% YoY owing to an increase of roughly 27% YoY in average selling prices and an increase of 5% YoY in total selling volume.

- Gross margin is forecasted to expand from 4.9% in 1Q2020 to 7.7% in 1Q2021 because the average HRC price is expected to increase by 17% QoQ in 1Q2021, while it increased by only 7% QoQ in 1Q2020.

- Higher gross margin and stable USD/VND rate will support net income.

Update

SMC's profit increased sharply in 2020 owing to surging steel prices and recovering demand in 2H.

The company's NPAT grew by 211% YoY to VND 300 billion, of which roughly VND 254 billion came in 2H. This is because after controlling the pandemic better in 2Q, steel demand recovered rapidly and led HRC price to surge. 2H 2020 witnessed the strongest growth in the HRC price in the last three years. The average HRC price has increased by 19% QoQ in 3Q and 18% in 4Q, after hitting the bottom in 2Q. Due to the inventory of HRC bought at a low price, SMC earned a higher gross margin of 5.3% and 7.2% in 3Q and 4Q 2020, respectively. Besides, the contribution from the trading segment was larger to total net income temporarily owing to increased construction steel prices.

Sale volume increased slightly due to the higher demand for flat and construction steel in 2H 2020. Steel output reached 1.35 million tons, up 2.4% YoY, while construction steel, coated steel, and processed coil volume were stable, steel pipe production volume increased sharply by 20% YoY from 142,000 tons to about 189,000 tons. Per management, SMC's factories were all running at full capacity in 2H2020, showing large demand for the company's products. This can be explained by the recovery in manufacturing and construction activities after the pandemic's peak. According to VSA, steel pipe and construction steel consumption increased by 27% YoY and 5% YoY respectively in 2H2020. Besides, a new contract with Samsung supported SMC's coil service volume growth in 4Q. The coil service volume that is supplied to Samsung contributed to roughly 6% of its processed coil volume in 4Q2020.

We expect the company's production output to grow roughly 5% in 2021, mainly from steel pipe and processed coil.

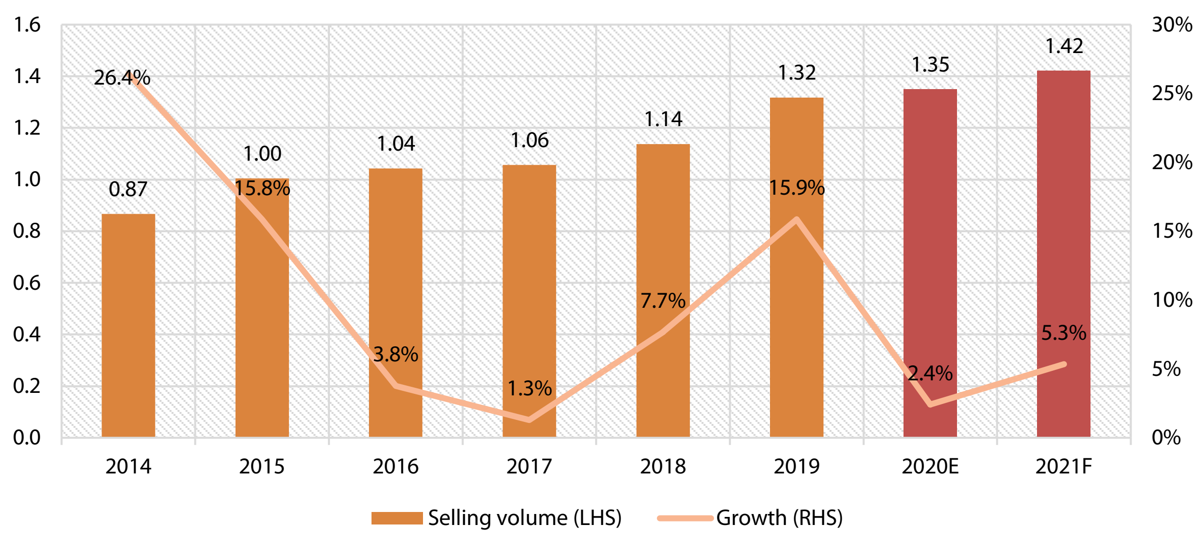
Steel pipe volume will increase by 16% to 220,000 tons and coil service volume will increase by 8% to 440,000 tons. Meanwhile, trading volume, which accounts for 55% SMC's total selling volume, will grow merely by 1% YoY.

Per management, SMC will install some more steel pipe production lines in the Sendo factory in 2021, making its capacity up by 10% to roughly 220,000 tons per year.

The Coil Center in Da Nang, which has come into operation in March 2020, reached its full-capacity status by the end of 2020, and supplied about 35,000 tons of processed steel (a utilization rate of roughly 90%). We believe that the Coil Centers will continue to run at maximum capacity in 2021 due to the great demand from downstream machinery manufacturers, which will be fueled by the expansion of many large foreign producers in Vietnam. Hence, SMC can meet its target to increase consumption volume at Coil Center Da Nang to 50,000 tons in 2021.

Because production activities slowed down in two-three months due to the pandemic in 2020, we believe that processed steel output will register a positive growth this year.

Figure 1: Selling volume (million tons) and growth rate (%)

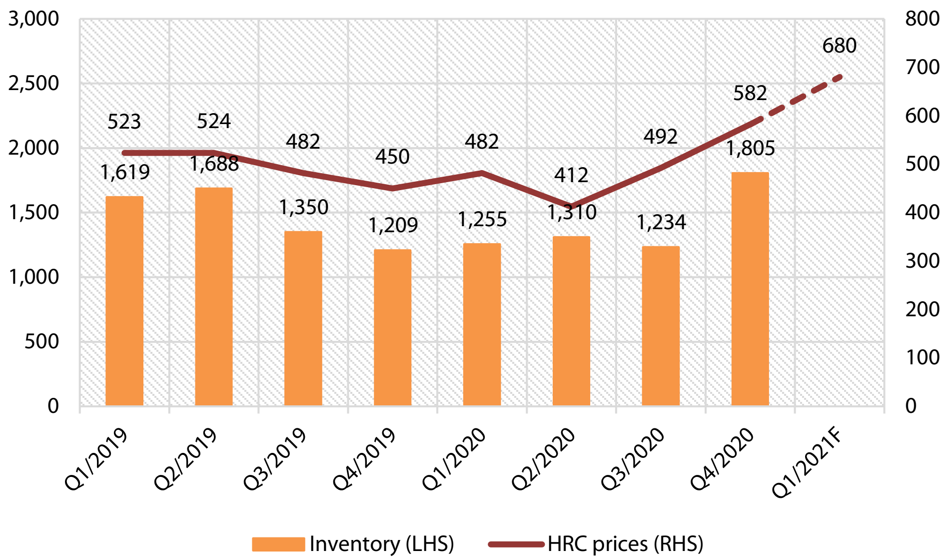


Source: SMC, RongViet Securities

The increase in the HRC price and high inventories are going to boost SMC's net income in 1Q 2021

We project SMC's profit in 1Q to reach VND 218 billion, mostly twenty-times higher than VND 14 billion in the same period last year. The company's inventories increased from VND 1,234 billion in 3Q 2020 to VND 1,805 billion in 4Q, of which 67% was raw materials and 30% was finished goods. A sharp increase of 46% QoQ in the company's inventories in Q4 showed that it has accumulated a considerable amount of steel. We estimate that SMC stored roughly 100,000 tons of flat steel and 30,000 tons of construction steel. The accumulated flat steel is enough for production and selling for roughly two months. We expect hot-rolled steel price in Q1 2021 to average roughly USD 680/ton, up 17% QoQ. An increase in the HRC price will have a positive impact on SMC's profitability. Hence, the company can earn a gross margin of 7.7% in 1Q, which is relatively high compared to the average quarterly gross margin of 4.0% in the last three years.

Figure 2: Inventory (VND billion) and HRC prices (USD/ton)



Source: SMC, RongViet Securities

We believe that SMC's NPAT can exceed its target of VND 160 billion in only one quarter and continue to grow YoY The company is likely to benefit from the high HRC price and inventory in 1Q. However, HRC price can go down in late-Q2 2021, leading SMC's gross margin to decrease in 2H. In our base case, we expect that the quarterly average HRC price will decrease from USD 680/ton in 1Q to USD 510/ton in 4Q 2021. Hence, SMC's gross margin in the second half of the year will fluctuate in the 2.7% - 3.1% range, significantly lower than the gross margin of 5.6% in the 1H. We forecast that its 2021 NPAT will be VND 340 billion, increasing by 13% YoY.

New steel processing factories will be key growth drivers in 2022 and allow the company to expand its value chain in the coil service segment.

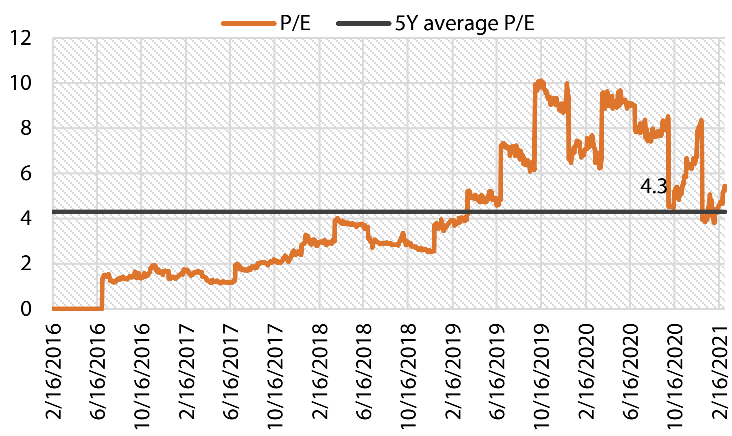
SMC plans to invest about VND 560 billion in two new factories in Ba Ria - Vung Tau province, including Phu My precision mechanical factory and Phu My steel service factory. Capital expenditure for each factory is roughly 280 billion VND, of which 60% will be financed by external sources, including borrowings, and financial leases. We think SMC will not face difficulties to finance these projects. The company has plenty of cash and it is likely to reduce inventory and receivables in late-2021. The construction of these two factories' construction is expected to start in mid-March and be completed in late-3Q 2021. Regarding their capacity, Phu My Precision Mechanical Factory can produce 50,000 tons/year and Phu My Steel Service Plant will have a capacity of 150,000 tons/year.

We believe that these new factories are the right investments to seize opportunities as demand for steel processing services is increasing owing to the shift of moving production plants to Vietnam. The partnership with Samsung will guarantee the consumption of precision mechanical factory output. Besides, due to the higher added value, the company can increase profitability and limit the impact of steel price movements on its results. We expect the precision engineering factory's gross margin to be 8.5%, higher than other SMC's processing factories' gross margin of roughly 5%. These two factories are expected to contribute NPAT of VND 100 billion in 2022, equivalent to 26% of SMC's total NPAT.

Valuation

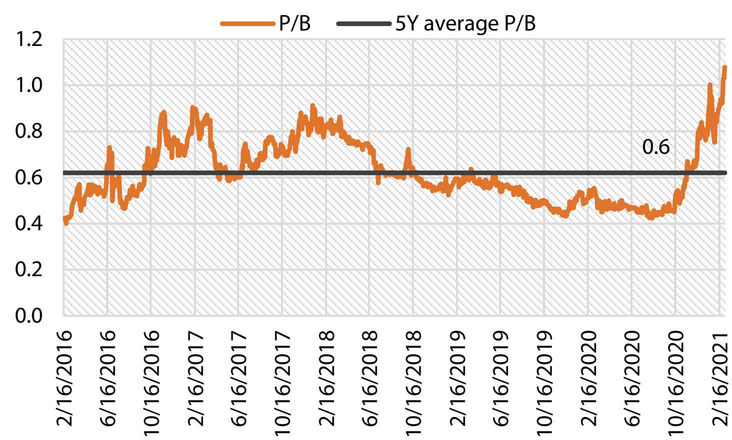
Based on DCF and sum-of-the-parts (SoTP) methods, we estimate SMC's fair value is roughly VND 30,200 per share. In the DCF method, we apply a WACC of 9.3% and exit EV/EBITDA of 6.0x. Regarding the SoTP valuation, we think SMC should be trading at a higher P/B ratios than the 5-year average P/B because the company's business is becoming more sustainable given that its net income mainly comes from steel production and coil services, accounting for roughly 85% of total net income. Hence, we use a P/B ratio of 1.0 for the manufacturing segment, which is equivalent to the industry's mean. We use a P/E ratio of 5.0 to evaluate the trading segment.

Figure 3: Historical P/E ratio



Source: SMC, RongViet Securities

Figure 4: Historical P/B ratio



Source: SMC, RongViet Securities

Table 1: Valuation (VND)

	Segment	Method	Weight	Price	Contribution
DCF	The whole company	FCFF (WACC of 9.3%, exit EV/EBITDA of 6.0x)	50%	30,288	15,144
Sum-of-the-parts	Trading	P/E (5.0x)		1,755	
	Manufacturing	P/B (1.0x)		28,436	
		Sum of the parts	50%	30,191	15,096
Target price					**30,200**
Cash dividend					**1,000**
Current price					**27,600**
Upside					**13%**

Source: RongViet Securities

VND Billion

INCOME STATEMENT	2019	2020	2021E	2022F
Revenue	**16,836**	**15,736**	**18,373**	**19,609**
COGS	16,346	14,931	17,492	18,678
Gross profit	**490**	**805**	**881**	**931**
Selling expenses	160	197	205	223
G&A expenses	125	194	161	176
Financial income	103	68	65	66
Financial expenses	167	117	140	126
Other income/loss	5	-11	0	0
Gain/(loss) from JVs	0	8	5	5
PBT	**146**	**361**	**445**	**478**
Tax expense	46	51	89	73
Minority interests	8	10	16	15
PAT	**92**	**300**	**340**	**389**
EBIT	204	413	515	533

%

FINANCIAL RATIO	2019	2020	2021E	2022F
Growth (%)				
Revenue	2.2	-6.5	16.8	6.7
Operating Income	-29.3	87.7	10.5	8.3
EBITDA	-39.1	102.5	24.7	3.5
PAT	-46.6	227.6	13.1	14.5
Total Assets	0.6	31.4	-7.3	-0.4
Equity	2.7	18.4	18.1	18.1
Profitability (%)				
Gross margin	2.9	5.1	4.8	4.8
EBITDA margin	1.8	3.5	3.3	3.4
EBIT margin	1.2	2.6	2.8	2.7
Net margin	0.5	1.9	1.8	2.0
ROA	1.8	4.5	5.5	6.3
ROE	14.5	25.3	24.0	21.6
Efficiency				(times)
Receivable Turnover	11.5	9.2	10.9	10.1
Inventory Turnover	13.5	8.3	11.5	10.5
Payable Turnover	10.1	6.0	8.2	8.2
Liquidity				(times)
Current	1.0	1.1	1.1	1.2
Quick	0.7	0.7	0.7	0.8
Finance Structure (%)				
Total Debt/Equity	167.6	174.9	124.7	82.6
Current Debt/Equity	162.1	171.7	109.0	69.3
Long-term Debt/Equity	5.5	3.2	15.7	13.3

VND Billion

BALANCE SHEET	2019	2020	2021E	2022F
Cash and cash equivalents	596	1,183	550	360
Short-term investments	274	557	502	251
Accounts receivable	1,464	1,717	1,683	1,942
Inventories	1,209	1,805	1,527	1,776
Other current assets	318	254	267	280
Property, plant & equipment	776	665	1,161	1,053
Acquired intangible assets	138	139	138	137
Long-term investments	239	277	277	277
Other non-current assets	97	118	124	130
Total assets	**5,112**	**6,715**	**6,227**	**6,205**
Accounts payable	1,619	2,471	2,127	2,269
Short-term borrowings	2,081	2,609	1,957	1,468
Long-term borrowings	70	49	282	282
Other non-current liabilities	2	1	1	1
Bonus and Welfare fund	4	4	4	4
Technology-science, dev. fund	0	0	0	0
Total liabilities	**3,776**	**5,133**	**4,369**	**4,023**
Common stock and APIC	864	863	863	863
Treasury stock (enter as -)	0	-1	-1	-1
Retained earnings	109	272	540	857
Other comprehensive income	1	1	1	1
Inv. and Dev. Fund	310	385	391	399
Total equity	**1,283**	**1,519**	**1,795**	**2,119**
Minority Interest	**53**	**63**	**63**	**63**

VALUATION RATIO	2019	2020	2021E	2022F
EPS (dong)	1,595	4,932	5,516	6,315
P/E (x)	21.8	2.2	4.9	4.3
BV (dong)	21,026	24,907	29,423	34,739
P/B (x)	1.6	0.4	0.9	0.8
DPS (dong/cp)	1,000	1,000	1,000	1,000
Dividend yield (%)	2.9%	9.3%	3.7%	3.7%

VALUATION MODEL	Price	Weight	Average
FCFF	30,288	50%	15,144
SoTP	30,191	50%	15,096
Target price			**30,200**

VALUATION HISTORY	Price	Recommendation	Period
10/07/2020	11,100	ACCUMULATE	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%

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