May, 2018

QUANG NGAI SUGAR JSC (UPCOM: QNS)

Closed its value chain to sustainable growth

(VND bn)	1Q-FY19	4Q-FY18	+/- QoQ	1Q-FY18	+/- YoY
Net revenue	2,000	1,884	+6.2%	1,597	+25.2%
NPAT-MI	155	450	-65.6%	188	-17.9%
EBIT	180	471	-61.7%	191	-5.6%
EBIT margin	9.0%	25.0%	-1,600bps	12.0%	-294bps

Source: QNS, Rong Viet Securities

1Q 2019 results – High revenue growth and rising costs

- Net revenue reached VND 2,000 bn (+25% YoY) thanks to positive growth in both soymilk and sugar as domestic demand for dairy recovers.
- However, QNS is facing pressure from (i) lower profitability in the sugar segment due to crop failure, (ii) the increase in selling & administration expenses and (iii) the lack of extraordinary income (~VND 25.8 bn), leading to a 18% YoY decline in NPAT to VND 155 bn.
- QNS achieved 24% and 78% of its revenue and net profit guidance, respectively. It should be noted that QNS has the habit of setting rather low profit targets; so completing 3/4 of the NPAT target is not considered a positive business result.

2Q 2019 outlook – Peak season, price correction offers buying opportunity

- The soymilk segment is expected to maintain its positive performance. The recovery in domestic demand and the promotion of new product lines from Q2 onwards are the company's main growth drivers.
- Sugar prices have shown signs of recovering, while QNS allocated most of its sugar segment depreciation costs in Q1. Therefore, we expect profit margins to improve from Q2 onwards.
- In addition, Q2 is considered peak season for both revenue and profit.
- We believe that the recent decline in QNS share price has created a buying opportunity for investors.

Valuation and recommendation

In the short run, the downward movement in sugar prices will negatively affect QNS' business results. However, we remain long-term positive on its core business activities, especially soymilk, where it is the undisputed market leader. QNS targets the soymilk segment to reach USD 1 Bn in revenues by 2027. For 2019, Rong Viet Securities forecasts net revenue and NPAT-MI of VND 8,155 bn (+2% YoY) and VND 1,153 bn (-7% YoY), respectively, corresponding to an EPS of VND 3,719 per share.

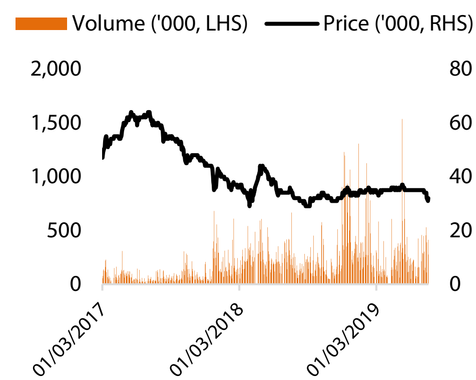
*Using a Sum-of-the-parts valuation method, we estimate the fair value of QNS at **VND 44,000** per share, resulting in an expected return of **45%** based on the May 31, 2019 closing price and including a VND 1,500 per share cash dividend. We have a **BUY** rating on the stock.*

BUY	+45%
Target price (VND)	44,000
Current market price (VND)	31,300

Stock Info	
Sector	F&B
Market Cap (VND billion)	10,958
Current Shares O/S	351,088,463
Avg. Daily Volume (in 20 sessions)	300,990
Free float (%)	29.5
52 weeks High	36,790
52 weeks Low	28,580
Beta	0.7

	FY2018	Current
EPS	4,183	4,183
EPS Growth (%)	21	21
Diluted EPS	4,183	4,183
P/E	8.3	7.5
P/B	1.9	1.7
EV/EBITDA	5.4	5.7
Cash dividend yield (%)	1,500	1,500
ROE (%)	25.1	25.1

Price performance



Major Shareholders (%)	
Thanh Phat Limited	15.8
Vo Thanh Dang & related parties	8.0
Foremost Worldwide Limited	5.2
Foreign ownership room (%)	30.8

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Exhibit 1: 1Q 2019 Results

(VND Bn)	1Q-FY19	4Q-FY18	+/-(QoQ)	1Q-FY18	+/-(YoY)
Net revenue	2,000	1,884	6.2%	1,597	25.2%
Gross profit	472	706	-33.2%	407	15.9%
SG&A	291	235	24.1%	216	34.9%
Operating income	180	471	-61.7%	191	-5.6%
EBITDA	461	529	-12.9%	333	38.5%
EBIT	180	471	-61.7%	191	-5.6%
Financial expenses	21	21	0.5%	20	6.8%
- Interest Expenses	21	19	9.3%	20	7.2%
Dep. and amortization	281	58	384.8%	142	97.8%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	189	510	-62.9%	209	-9.7%
PAT	155	450	-65.6%	188	-17.9%
(*) Adjusted PAT	155	450	-65.6%	188	-17.9%

Source: QNS, Rong Viet Securities

Exhibit 2: 1Q 2019 Performance Analysis

Particulars	1Q-FY19	4Q-FY18	+/-(QoQ)	1Q-FY18	+/-(YoY)
Profitability Ratios (%)					
Gross Margin	23.6	37.5	-1,390 bps	25.5	-190 bps
EBITDA Margin	23.1	28.1	-505 bps	20.8	221 bps
EBIT Margin	9.0	25.0	-1,601 bps	12.0	-294 bps
Net Margin	7.7	23.9	-1,614 bps	11.8	-406 bps
Adjusted Net Margin	7.7	23.9	-1,614 bps	11.8	-406 bps
Turnover *(x)					
-Inventories	7.6	7.0	0.6	7.4	0.2
-Receivables	18.9	17.5	1.4	24.7	-5.8
-Payables	7.4	5.8	1.6	5.7	1.7
Leverage (%)					
Total Debt/ Equity	49.9	49.1	75 bps	57.0	-711 bps

Source: Rong Viet Securities

Exhibit 3: 2Q 2019 Performance Forecast

Particulars (VND Bn)	2Q-FY19	+/- QoQ	+/- YoY
Revenue	2,389	19%	11%
Gross profit	693	47%	11%
EBIT	370	105%	12%
NPAT-MI	351	127%	4%

Source: Rong Viet Securities

Update

1Q business result – Revenue growth is positive, but rising costs and lack of extraordinary income results in NPAT decline.

Figure 1. Revenue by segment (VND bn)

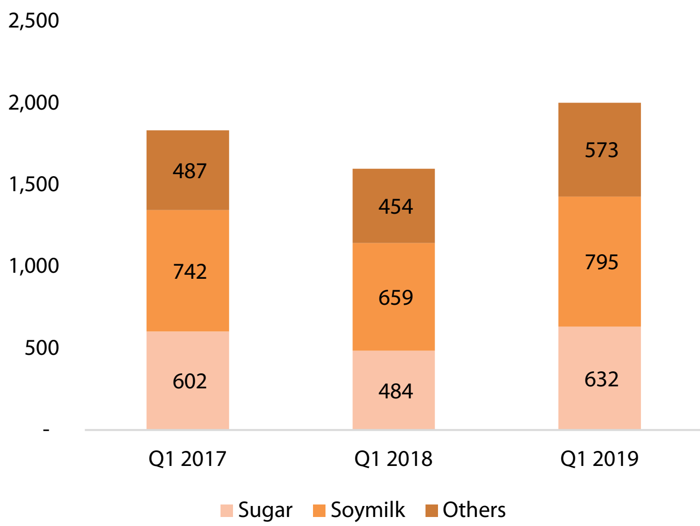
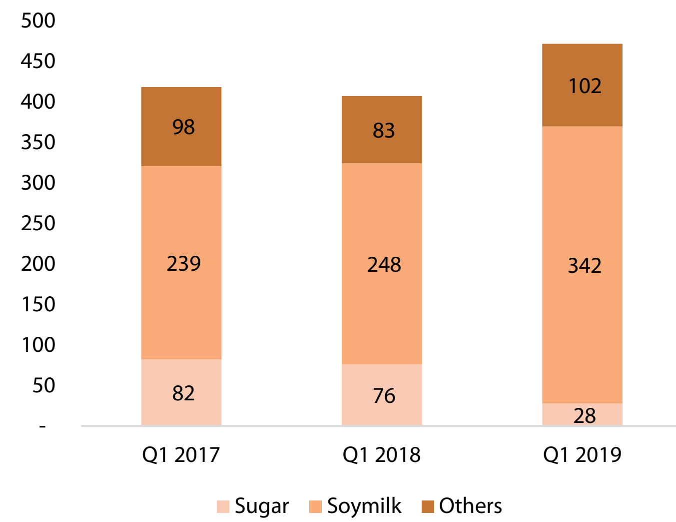


Figure 2. Gross profit by segment (VND bn)



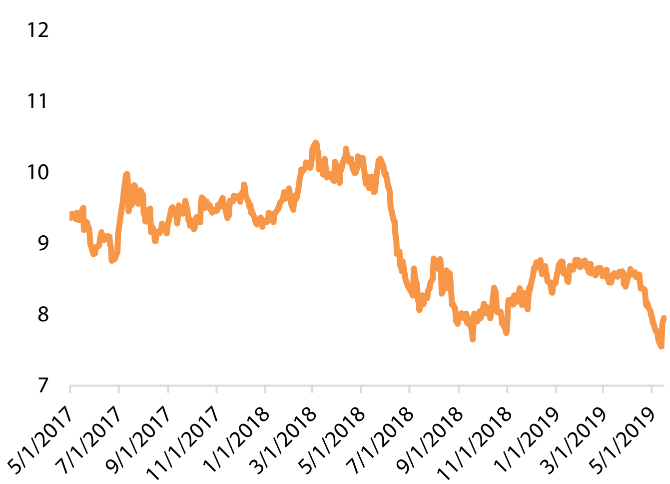
Source: QNS, Rong Viet Securities

At the end of Q1 2019, QNS achieved high growth in revenue (+25% YoY), reaching VND 2,000 bn. However, gross margins declined by 190bps to 23.6% compared to 25.5% in the same period last year. NPAT fell 18% YoY to VND 155 billion. In details:

(1) Soymilk segment: contributes around 40% of revenue and 73% of gross profit.

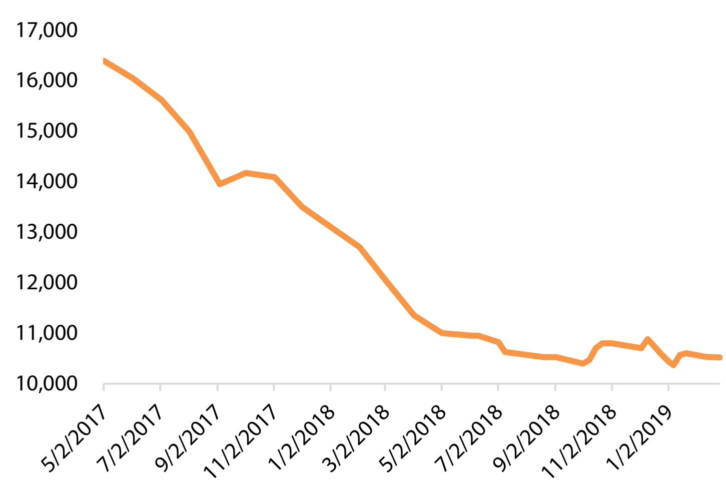
Net revenue reached VND 795 bn, up 21% YoY thanks to: (i) selling volume growth of 18% YoY, from Calcium Fami and traditional Fami products; (ii) an average selling price increase of 2% YoY thanks to the contribution of its new product line, "Fami Go" with a selling price 50% higher than the old product line. The average sugar and soybean material price dropped 17% YoY and 14% YoY, respectively (Figure 3 & 4), leading to a gross profit margin increase of 541 bps to 43% from 37.6% in the same period last year.

Figure 3. World's soybean price (USD/bushel)



Source: Bloomberg, Rong Viet Securities

Figure 4. RS's sugar price in domestic market (VND/kg)



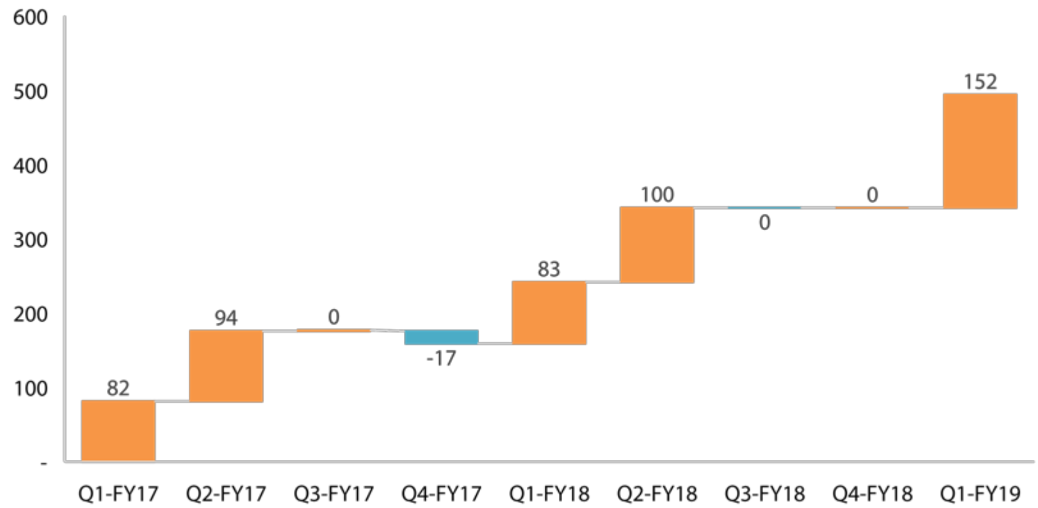
Source: VSSA, AgroMonitor, Rong Viet Securities

After a recent slowdown in domestic dairy demand, the market has shown signs of recovery. VNM, the biggest player in the dairy industry announced positive revenue growth of 9% YoY in 1Q, compared to 0.6% YoY in 1Q 2018.

(2) Sugar segment: contributes 32% of revenue and 6% of gross profit.

Net revenue grew 30% YoY, reaching VND 632 Bn thanks to a 48% YoY increase in selling volume. Meanwhile, the selling price decreased 12% YoY affected by the downward trend in domestic and world's sugar prices. In addition, depreciation expenses increased strongly (+84% YoY) because the number of production days or depreciation period (*) only lasted from January to April, while they lasted until June previous season. As a result, gross profit margins decreased sharply to 4.4% compared to 15.7% in the same period last year.

Figure 5. Sugar segment's depreciation is mainly allocated in the first 2 quarters (VND bn)



Source: QNS, Rong Viet Securities

(*) QNS often records the depreciation cost of its sugar segment through the production time (usually from January to June).

In the period 2018/19 due to the short running time, most depreciation expenses were allocated in the 1st quarter.

(3) Other businesses (beer, mineral water, biscuits, etc) recorded positive growth, with revenue reaching VND 573 bn (+26% YoY) and gross profit VND 102 bn (+ 3% YoY). The mineral water segment showed encouraging results due to the contribution of large bottles of 18.9 liters that enjoy high demand from households instead of water mainstreams with small volume (480 - 500ml).

(4) Selling & administrative expenses increased 35% YoY, totaling VND 291 bn as the company spent more on advertising (+ 66% YoY) and transportation costs (+ 48% YoY). SG&A expenses to revenue rose 104 bps, to 14.6% in 1Q 2019 from 13.5% in 1Q 2018.

(5) No extraordinary income vs. ~ VND 25.8 bn in the same period last year.

(6) Corporate income tax (CIT) increased 810 bps to 18.1% in 1Q 2019 from 10% in 1Q 2018 because the time of CIT incentives/exemption from a number of investment projects ended.

FY2019 outlook

Soymilk segment - expanding the pie, developing more soy-based products

2019 is considered a pivotal year to reach the USD 1 Bn revenue target in 2027. The BoD said boosting its market share (around 85% already) is not a key focus point. Instead QNS will aim to expand the pie and will:

(1) Increase the proportion of branded soymilk products on the market. According to Nielsen, branded soymilk currently accounts for 45% of total domestic soymilk supply vs. 70% in Thailand.

(2) Develop new nutritional products from soybeans such as soybean oil, margarine, ethanol biofuel, etc.

QNS plans to launch three new products this year, including two lines of low sugar products (end of Q2) and one high-protein offering (in Q3) to meet the health conscience needs from consumers. We expect this will be a catalyst for growth and forecast 2019 revenue growth to reach 15% YoY.

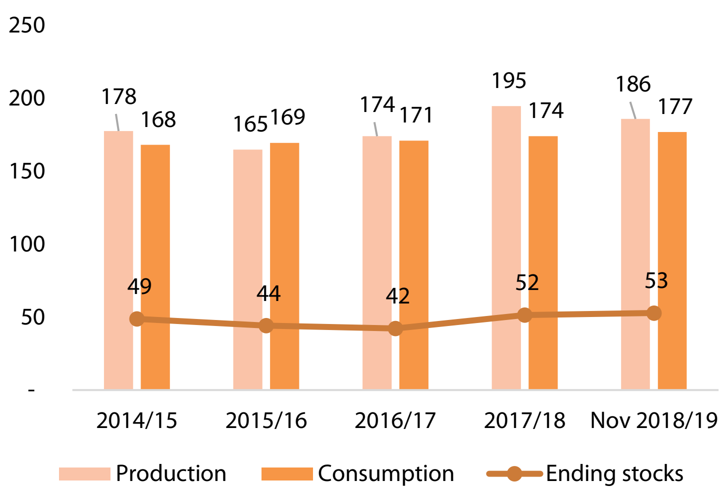
QNS has a competitive advantage as it owns more than 1,580 precious soy gene sources and is gradually expanding its soybean area. We believe that there is still room for growth through the application of this soy gene source to create high-end dairy and soy nutrition products. In 2019, QNS plans to expand the soybean material area in Cu Jut, Dac Nong province (region 1, harvest in July) to 400 ha from 200 ha in 2018. At the same time, it is investing in developing material areas in the mudflats of the central river (region 2, April harvest) to expand the time for harvesting soybeans. Its goal is to obtain "fresh" material supply for production.

On the other hand, in order to maintain its leading position and sales growth, QNS will promote the development of new product lines and invest in brand building as demonstrated in the last 2 years.

Sugar prices show signs of recovery

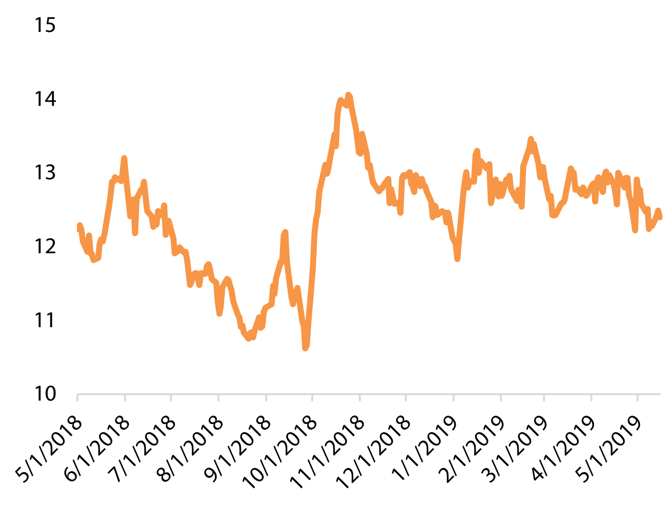
According to ISO Sugar, the 2018/19 global sugar market remains in oversupply (surplus ~ 641,000 tons) and inventories remain high (Figure 5). However, Brazil, the largest producer in the world saw a 17.2% YoY decrease in sugar production by March 31, 2019 as it increasingly turns to ethanol production. This helps reduce global supply and sugar prices in May recorded a slight increase of 3% YTD (Figure 6).

Figure 6. World's sugar production, consumption and ending stocks (mn tons)



Source: USDA, Rong Viet Securities

Figure 7. World's sugar price (US cent/lb)



Source: Bloomberg, Rong Viet Securities

In the domestic market, VSSA estimates that sugarcane production in 2018/19 crop is about 14 Mn tons. Sugar production is estimated to reach 1.3 Mn tons (-7% YoY) due to reduced sugarcane yields. Meanwhile domestic demand is estimated at around 1.6 mn tons. However, high inventories from the previous crop as well as sugar smuggled from Thailand (about 500,000 - 700,000 tons/year) continue to flood the market. Given oversupply, sugar prices still trade a low levels, VND 10,300 - VND 10,500/kg in the first 4 months of 2019. In May, sugar prices slightly recovered. The selling price of RS sugar increased by VND 500-700/kg to VND 11,000/kg. Most depreciation expenses have been allocated in 1Q so we expect the profit margin in the next quarters to improve.

Moreover, QNS expects to complete the construction of the RE refining sugar plant and conduct a trial run this July, before officially starting operations in 1Q 2020. It will import raw sugar from Thailand to refine with the goal of building its own retail brand. A part of RE sugar produced can be used for internal consumption including soy milk, soft drinks, etc and help reduce fluctuations in production costs.

QNS is implementing ESOP release for 2018

QNS qualified to issue 2018 ESOP at 2% of outstanding shares, equivalent to 5,851,492 shares. These shares will be locked for 3 years.

Table 1. Business result in 2018 (VND bn)

Items	2018	Growth	Issuance rate
NPAT	1,240	21%	
Depreciation	487	19%	
NPAT + Depreciation	**1,727**	**20.3%**	**2%**

Source: QNS, Rong Viet Securities

Valuation

In our previous reports, we used the FCFF method to estimate the fair value of the company. However, this approach has the disadvantage of not extracting the value of each separate business. There is a compelling argument branded soymilk and sugar companies should trade at different multiples. Therefore, we proceed to replace FCFF valuation by Sum-of-the-parts method. Specifically:

Table 2. Sum-of-the-parts valuation

Sector	Method	Valuation
Soymilk	P/E 13.5	33,691
Sugar	P/E 6.6	1,128
Biomass	FCFF	3,296
Others	P/E 8.3	6,348
Fair value (VND/share)		**44,000**

Source: Rong Viet Securities

Table 3. Comparison with the enterprises in the industry

Company	Stock	Market Cap (VND mn)	P/E	P/B	EV/EBITDA	P/S
Sugar sector						
Son La Sugar JSC	SLS VN Equity	376,990	6.6	0.8	8.6	0.5
Kon Tum Sugar JSC	KTS VN Equity	100,893	10.0	0.6	17.0	0.2
Dalmia Bharat Sugar & Indust	DCB IN Equity	3,198,860	5.5	0.6	7.3	0.5
Dhampur Sugar Mills Ltd	DSM IN Equity	5,055,962	6.0	1.2	6.9	0.5
Dwarikesh Sugar Indus Ltd	DSIL IN Equity	1,760,336	5.5	1.1	9.4	0.5
Avadh Sugar & Energy Ltd	AVADHSUG IN Equity	2,271,363	5.7	1.3	6.5	0.3
Average			**6.6**	**0.8**	**8.9**	**0.4**
Dairy sector						
Hebei Yangyuan Zhihui Beve-A	603156 CH Equity	116,929,530	12.8	2.9	6.2	4.2
Indofood Sukses Makmur TBK P	INDF IJ Equity	90,632,535	12.9	1.6	7.5	0.7
China Zhongdi Dairy Holdings	1492 HK Equity	3,568,047	16.8	0.5	9.8	0.7
Lanzhou Zhuangyuan Pasture-H	1533 HK Equity	7,387,931	15.1	0.8	N/A	1.4
Maeil Dairies Co Ltd	267980 KS Equity	14,218,387	12.2	2.1	6.3	0.5
Ultrajaya Milk Ind & Trading	ULTJ IJ Equity	25,353,807	18.8	3.1	10.0	2.8
Average			**13.5**	**1.9**	**7.1**	**1.8**
Others (beers, mineral waters, biscuits, etc)						
Bibica Corp	BBC VN Equity	1,000,809	10.3	1.1	4.3	0.7
Sai Gon – Mien Trung Beer JSC	SMB VN Equity	984,939	7.0	2.2	4.2	0.6
Ha Noi – Hai Duong Beer JSC	HAD VN Equity	118,800	13.3	1.6	4.0	0.8
Vinacafe Bien Hoa JSC	VCF VN Equity	4,757,665	7.9	3.1	5.2	1.5
Average			**8.3**	**1.9**	**4.6**	**0.9**
QNS	QNS VN Equity	10,989,069	7.5	1.7	5.4	1,2

Source: Bloomberg, data as at May 30th 2019, Rong Viet Securities

VND Billion

INCOME STATEMENT	FY2017	FY2018	FY2019F	FY2020F
Revenue	7,633	8,031	8,155	9,446
COGS	5,637	5,737	5,760	6,808
Gross profit	**1,996**	**2,294**	**2,395**	**2,638**
Selling Expense	697	762	846	907
G&A Expense	146	176	181	209
Finance Income	38	87	74	49
Finance Expense	78	96	65	40
Other profits	26	57	32	32
PBT	**1,138**	**1,405**	**1,409**	**1,563**
Prov. of Tax	112	165	255	289
Minority's Interest	0	0	0	0
PAT to Equity S/H	**1,027**	**1,240**	**1,153**	**1,274**
EBIT	1,153	1,357	1,368	1,522
EBITDA	1,567	1,850	1,842	2,136

%

FINANCIAL RATIO	FY2017	FY2018	FY2019F	FY2020F
Growth (%)				
Revenue	9.5	5.2	1.5	15.6
Operating Income	-14.9	18.0	-0.4	18.5
EBITDA	-24.0	17.7	0.9	14.7
PAT	-27.2	20.8	-7.0	14.2
Total Assets	14.3	14.3	1.8	11.6
Equity	14.6	19.4	19.0	14.0
Profitability (%)				**(%)**
Gross margin	26.2	28.6	29.4	27.9
EBITDA margin	20.5	23.0	22.6	22.6
EBIT margin	15.1	16.9	16.8	16.1
Net margin	13.5	15.4	14.1	13.5
ROA	14.7	15.5	14.2	14.0
ROE	22.9	23.2	18.1	17.6
Efficiency				(times)
Receivable Turnover	26.4	17.2	21.2	21.2
Inventory Turnover	17.6	9.8	12.7	11.1
Payable Turnover	6.3	6.8	6.6	6.6
Liquidity				(times)
Current	0.8	1.2	1.1	1.1
Quick	0.7	1.0	0.8	0.7
Finance Structure (%)				
Total Debt/Equity	34.6	32.3	12.9	10.3
Current Debt/Equity	31.3	32.3	12.9	10.3
Long-term Debt/Equity	3.2	0.0	0.0	0.0

VND Billion

BALANCE SHEET	FY2017	FY2018	FY2019F	FY2020F
Cash and cash equivalents	528	418	221	209
Short-term investments	751	1,699	800	600
Accounts receivable	289	468	384	445
Inventories	320	585	455	613
Other current assets	19	8	8	9
Property, plant & equipment	4,845	4,568	6,015	6,954
Acquired intangible assets	7	34	28	20
Long-term investments	0	0	0	0
Other non-current assets	240	222	233	244
Total assets	**6,999**	**8,002**	**8,144**	**9,094**
Accounts payable	899	842	874	1,033
Short-term borrowings	1,404	1,727	820	745
Long-term borrowings	145	0	0	0
Other non-current liabilities	18	19	20	21
Bonus and Welfare fund	42	52	52	52
Technology-science, dev. fund	9	8	8	8
Total liabilities	**2,517**	**2,649**	**1,775**	**1,859**
Common stock and APIC	2,726	3,214	3,273	3,273
Treasury stock (enter as -)	-834	-834	-834	-834
Retained earnings	2,135	2,467	3,367	4,169
Other comprehensive income	0	0	0	0
Inv. and Dev. Fund	454	506	563	627
Total equity	**4,482**	**5,353**	**6,369**	**7,235**
Minority Interest	**0**	**0**	**0**	**0**

VALUATION RATIO (*)	FY2017	FY2018	FY2019F	FY2020F
EPS (dong)	4,937	5,087	1,407	1,404
P/E (x)	9.1	8.3	10.9	10.9
BV (dong)	21,829	26,071	20,463	22,047
P/B (x)	2.4	1.9	0.7	0.7
DPS (dong/cp)	1,500	1,500	1,500	1,500
Dividend yield (%)	3.3	3.6	4.6	4.6

VALUATION MODEL	Price	Weight	Average
Sum-of-the-parts	44,000	100%	44,000
Target price (VND)			**44,000**

VALUATION HISTORY	Price	Recommendation	Period
2017/08/21	61,800	Buy	Long term
2017/05/12	72,800	Buy	Long term
2018/11/23	60,200	Buy	Long term

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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