August, 2018

NAM KIM STEEL JSC (HSX: NKG)

Difficulties are temporary

Particulars (VND B)	Q2-FY18	Q1-FY18	+/-qoq	Q2-FY17	+/-yoy
Net revenue	4,291	3,586	20%	3,095	39%
PAT	109	121	-10%	195	-44%
EBIT	207	200	3%	246	-16%
EBIT margin	4.8%	5.6%	-75bps	7.9%	-312bps

Source: NKG, RongViet Securities

1H 2018 performance: affected by input price hike

- Total volume reached 381,000 tons in 1H2018, up 30% YoY, a bit lower than expectations. Coated steel volume increased by 25% YoY, while steel pipe volume went up by nearly 50% YoY due to the new mill Nam Kim 4.
- 1H2018 revenue went up by 44% while NPAT decreased by 37% because surging input prices put pressure on gross margin.
- Increases in inventory and receivables caused rising short-term debts and interest expenses.

2018: facing short-term difficulties but attractive valuation

There is rising competition in the domestic coated steel market because most large firms expanded their capacity, including NKG. In addition to lower margins in order to boost sales, NKG has to offer more attractive credit policies to its customers. NKG also needs to boost exports to achieve volume growth. Based on the fact that NKG only completed under 40% of its annual volume target, we slightly lower our forecast for sales for 2018.

We expect that it will be difficult for the company to achieve its NPAT guidance of VND 750 billion in 2018, given that 1H2018 NPAT was equivalent to only 31% of the target.

Nevertheless, NKG has certain advantages being the country's second highest firm in terms of capacity of cold-rolling. We believe that NKG can achieve higher earnings results in the long-term when input price pressure diminishes.

Valuation and recommendation*: NKG is facing several barriers in order to achieve earning growth in 2018. The rapid hike of HRC price in 1H2018 has put huge pressure on NKG's profitability. Moreover, harsh competition in the domestic coated steel market also affected its gross margin and caused rising interest expense, further lowering its net margin. These short-term pessimistic catalysts have been depressing the share price, while the long-term advantages regarding output capacity and selling ability remain the positive elements for the business.*

Based on the intermediate term potential of the company, we made several adjustments in our forecast including volume growth and gross margin to evaluate NKG's profitability in 2018. NKG price is adjusted with a target of VND ***18,000/share****, total return is estimated at* ***42%*** *from the closing price on August 30th, 2018 and we recommend to* ***BUY*** *the stock.*

BUY +42%

CMP (VND)	13,350
Target price (VND)	18,000
Cash dividend (VND)*	1,000

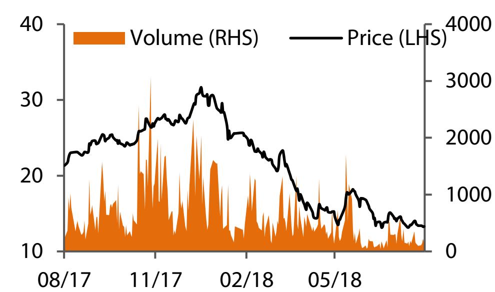
** Expected in the next 12 months*

Stock info

Sector	Materials
Market Cap (VND billion)	1,413
Current Shares O/S	105,072,000
Avg. Daily Volume (in 20 sessions)	203,491
Free float (%)	33.4
52 weeks High	31,643
52 weeks Low	13,150
Beta	1.00

	FY2017	Current
EPS	4,779	3,603
EPS growth (%)	-2.32	-57.51
Adjusted EPS	4,779	3,603
P/E	5.80	3.73
P/B	1.72	0.80
EV/EBITDA	6.90	5.18
Cash dividend	714.29	
ROE (%)	31.32	28.06

Price performance



Major Shareholders (%)

P&Q Ltd	14.2
Ho Minh Quang	10.3
VEIL	9.9
Foreign ownership room (%)	70.5

Trinh Nguyen

(084) 028- 6299 2006 – Ext 1331

trinh.nh@vdsc.com.vn

Exhibit 1: Q2 2018 results

Particulars (VND B)	Q2-FY18	Q1-FY18	+/-(QoQ)	Q2-FY17	+/-(YoY)	2Q-FY18	+/-(YoY)
Net revenue	4,291	3,586	19.7%	3,095	38.7%	7,877	44%
Gross profit	309	296	4.5%	338	-8.6%	604	-6%
SG&A	102	96	6.6%	92	10.8%	198	28%
Operating income	207	200	3.5%	246	-15.9%	406	-34%
EBITDA	312	304	2.5%	245	27.1%	616	13%
EBIT	207	200	3.5%	246	-15.9%	406	-17%
Financial expenses	111	87	27.8%	89	25.6%	199	7%
- Interest Expenses	82	81	1.6%	67	21.7%	163	35%
Dep. and amortization	105	104	0.5%	(0)	-28478.4%	209	274%
Non-recurring items (*)							
Extraordinary items (*)							
PBT	117	131	-10.8%	202	-42.1%	248	-35%
PAT	109	121	-10.1%	195	-44.2%	230	-37%
(*) Adjusted PAT	109	121	-10.1%	195	-44.2%	230	-37%

Source: NKG, RongViet Securities

Exhibit 2: Q2 2018 performance analysis

Particulars	Q2-FY18	Q1-FY18	+/-(QoQ)	Q2-FY17	+/-(YoY)
Profitability ratios (%)					
Gross margin	7.2%	8.2%	-105bps	10.9%	-372bps
EBITDA margin	7.3%	8.5%	-122bps	7.9%	-66bps
EBIT margin	4.8%	5.6%	-75bps	7.9%	-312bps
Net margin	2.5%	3.4%	-84bps	6.3%	-377bps
Adjusted net margin	2.5%	3.4%	-84bps	6.3%	-377bps
Turnover *(x)					
-Inventories	4.5	3.6	0.9	4.3	0.3
-Receivables	17.9	14.2	3.7	16.7	1.2
-Payables	17.7	13.5	4.2	15.1	2.6
Leverage (%)					
Total debt/ equity	165.1%	145.7%	1,933bps	196.5%	-3,142bps

Source: NKG, (*) Annualized turnover

Exhibit 3: Q3 2018 performance forecast

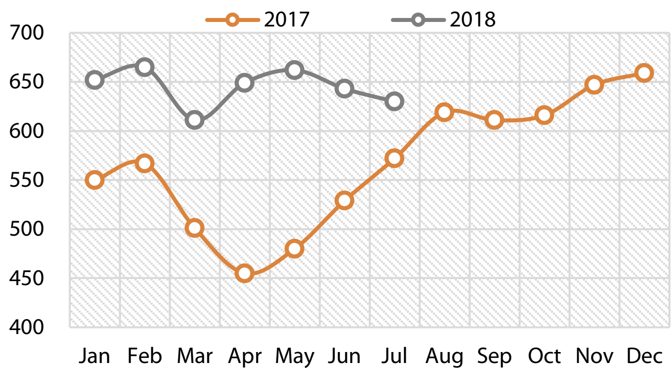
Particulars (VND B)	Q3-FY18	+/-(QoQ)	+/-(YoY)
Revenue	5,928	38%	56%
Gross profit	434	40%	10%
EBIT	310	50%	5%
NPAT	169	55%	-18%

Source: NKG, RongViet Securities.

Updates

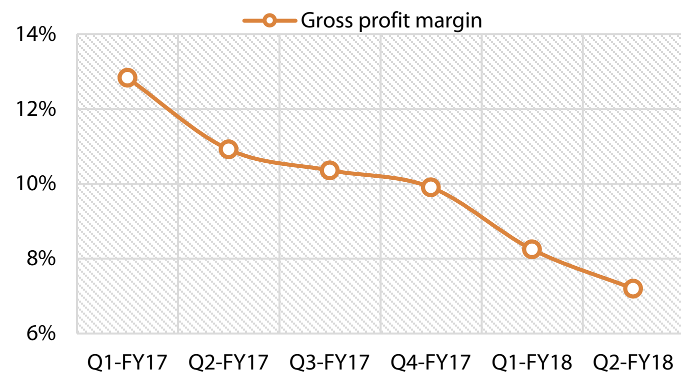
Strong input price fluctuations continue to be the major factor affecting NKG's gross margin. NKG was under overwhelming pressure from rising HRC price, which went up by over 20% YoY in 1H2018. NKG's 1H2018 gross margin was only 7.7%, compared to 11.7% in 1H2017. Our adjusted forecasts are based on the assumptions that HRC price will remain at the current level during the remaining of 2018. As the increase in the domestic coated steel supply fuels competition, we forecast that NKG will have to accept lower margin in 2H2018 to boost sales volume.

Figure 1: HRC price



Source: Bloomberg

Figure 2: NKG's gross margin



Source: NKG

NKG will continue to be the second highest firm in terms of market share. However, it will still depend on exports as it sold nearly two thirds of its coated steel sheets overseas. Accordingly, NKG might face risks regarding trade protections in its major markets including ASEAN countries. However, we consider exports to be an efficient tool to hedge the foreign exchange risks as well as it is a potential sales channel since the company does not operate its own local retailers.

Figure 3: Market share based on total sales volume

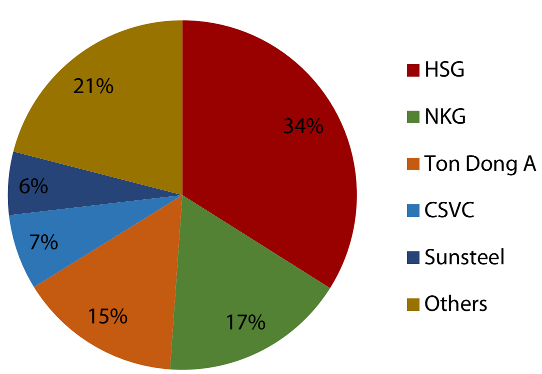
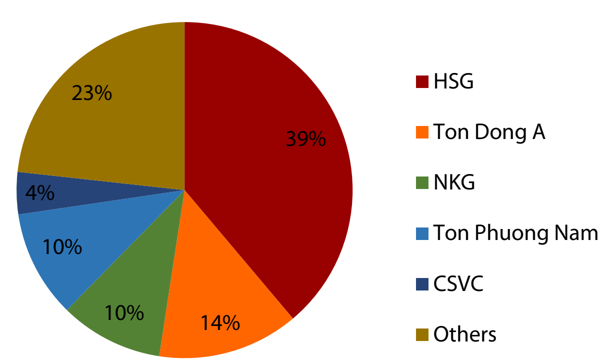


Figure 4: Market share based on domestic sales volume



Source: VSA

NKG's interest expense will continue to increase due to higher short-term debt. Firstly, NKG's receivables have been increasing strongly possibly due to credit policies offered to customers. Secondly, capacity expansion requires storing higher amounts of materials. Lastly, it can be seen that a higher amount of finished goods in NKG's inventory also puts pressure on its working capital. As a result, NKG's short-term borrowings increased strongly, causing higher interest expenses. We expect NKG's interest expenses to continue going up in the future.

Figure 5: NKG's receivables and inventories

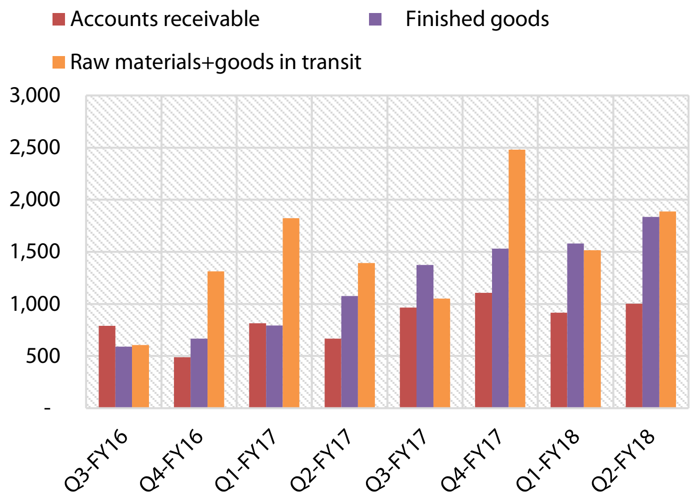
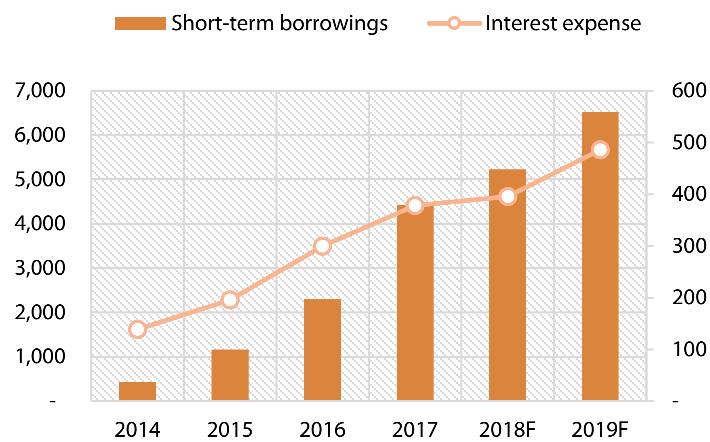


Figure 6: NKG's short-term borrowings and interest expense forecast



Source: NKG, RongViet Securities forecasted

VND in billions

Income statement	FY2016	FY2017	FY2018E	FY2019F
Revenue	8,936	12,619	19,733	28,396
COGS	7,924	11,251	18,261	26,578
Gross profit	1,012	1,368	1,472	1,818
Selling expense	162	274	355	548
G&A expense	54	69	83	96
Finance income	110	115	4	5
Finance expense	299	378	395	485
Other profits	0	20	20	20
Gain/(loss) from JVs	0	0	0	0
PBT	608	781	662	715
Prov. of tax	90	74	99	94
Minority's interest	0	0	0	0
PAT to equity S/H	518	708	562	621
EBIT	796	1,024	1,033	1,175

%

Financial ratio	FY2016	FY2017	FY2018E	FY2019F
Growth (%)				
Revenue	55.4	41.2	56.4	43.9
Operating income	122.7	39.6	12.7	24.7
EBITDA	157.1	28.6	0.9	13.7
PAT	310.8	36.6	-20.5	10.4
Total assets	78.9	59.2	24.2	22.4
Equity	146.6	86.4	13.7	12.2
Profitability (%)				
Gross margin	11.3	10.8	7.5	6.4
EBITDA margin	10.8	10.7	7.7	6.7
EBIT margin	8.9	8.1	5.2	4.1
Net margin	5.8	5.6	2.8	2.2
ROA	8.1	7.0	4.4	4.0
ROE	32.8	24.1	16.8	16.5
Efficiency (x)				
Receivable turnover	18.0	11.4	12.5	12.5
Inventory turnover	3.9	2.8	4.2	4.5
Payable turnover	12.2	11.0	11.1	11.1
Liquidity (x)				
Current	1.0	1.1	1.0	1.0
Solvency (%)				
Total debt/equity	263.5	210.1	228.0	247.8
Current debt/equity	145.5	150.5	156.2	173.9
Long-term Debt/equity	117.9	59.7	71.8	73.9

VND in billions

Balance sheet	FY2016	FY2017	FY2018E	FY2019F
Cash and cash equivalents	174	93	197	228
Short-term investments	26	415	249	261
Accounts receivable	496	1,107	1,579	2,272
Inventories	2,033	4,090	4,383	5,847
Other current assets	346	423	508	610
Property, plant & equipment	3,233	3,726	5,405	5,938
Acquired intangible assets	59	267	263	257
Long-term investments	0	24	24	24
Other non-current assets	24	29	31	32
Total assets	**6,390**	**10,174**	**12,638**	**15,469**
Accounts payable	649	1,026	1,643	2,392
Short-term borrowings	2,296	4,425	5,225	6,525
Long-term borrowings	1,860	1,755	2,402	2,774
Other non-current liabilities	1	1	1	2
Bonus and welfare fund	4	28	22	24
Technology-science, dev. fund	0	0	0	0
Total liabilities	**4,810**	**7,234**	**9,294**	**11,717**
Common stock and APIC	925	2,066	2,586	2,586
Treasury stock (enter as -)	0	0	0	0
Retained earnings	635	831	687	1,063
Other comprehensive income	5	20	20	20
Inv. and dev. fund	13	23	51	82
Total equity	**1,577**	**2,940**	**3,345**	**3,753**
Minority interest	**3**	**0**	**0**	**0**

Valuation ratio	FY2016	FY2017	FY2018E	FY2019E
EPS (VND)	1,802	3,693	2,520	2,783
P/E (x)	3.0	2.1	4.5	4.1
BV (VND)	23,888	22,619	18,377	20,618
P/B (x)	1.0	1.0	0.7	0.6
DPS (VND/cp)	0	0	1,000	1,000
Dividend yield (%)	0.00	4.29	7.49	7.49

Valuation model	*Price*	*Weight*	*Average*
PE	17,611	50%	8,805
PB	18,377	50%	9,189
Target price (VND)			**18,000**

Valuation history	*Price*	*Recommendation*	*Period*
05/02/2018	34,571	Neutral	Intermediate
19/07/2017	27,714	Buy	Intermediate
01/11/2016	21,047	Buy	Intermediate
06/11/2015	5,676	Neutral	Intermediate

RESULTS 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

ANALYSIS & INVESTMENT ADVISORY DEPARTMENT

Bernard Lapointe
Head of Research
bernard.lapointe@vdsc.com.vn
+ 84 28 62992006 (1525)

Lam Nguyen
Senior Strategist
lam.ntp@vdsc.com.vn
+ 84 28 6299 2006 (1313)
- Banking
- Market Strategy

Hieu Nguyen
Senior Analyst
hieu.nd@vdsc.com.vn
+ 84 28 6299 2006 (1514)
- Market Strategy
- Pharmaceuticals
- Aviation

Duong Lai
Senior Analyst
duong.ld@vdsc.com.vn
+ 84 28 6299 2006 (1522)
- Real Estate
- Building Materials

Vu Tran
Senior Analyst
vu.thx@vdsc.com.vn
+ 84 28 6299 2006 (1518)
- Oil & Gas
- Fertilizer

Trinh Nguyen
Senior Analyst
trinh.nh@vdsc.com.vn
+ 84 28 6299 2006 (1331)
- Steel
- Construction
- Technology

Son Phan
Analyst
son.pnt@vdsc.com.vn
+ 84 28 6299 2006 (1519)
- Utilities
- Natural Rubber

Tu Vu
Analyst
tu.va@vdsc.com.vn
+ 84 28 6299 2006 (1511)
- Macroeconomics

Son Tran
Analyst
son.tt@vdsc.com.vn
+ 84 28 6299 2006 (1527)
- Market Strategy
- Retails
- Consumer chemicals

Tung Do
Analyst
tung.dt@vdsc.com.vn
+ 84 28 6299 2006 (1521)
- Logistics
- Aviation

Thu Pham
Analyst
thu.pa@vdsc.com.vn
+ 84 28 6299 2006 (1520)
- Industrial Real Estate

Thao Dang
Analyst
thao.dtp@vdsc.com.vn
+ 84 28 6299 2006 (1529)
- Food & Beverage
- Textiles

Tam Pham
Analyst
tam.ptt@vdsc.com.vn
+ 84 28 6299 2006 (1530)
- Insurance

Anh Nguyen
Analyst
anh2.ntt@vdsc.com.vn
+ 84 28 6299 2006 (1531)
- Banking

Vy Nguyen
Analyst
vy.ntk@vdsc.com.vn
+ 84 28 6299 2006 (1528)
- Automobile & Parts

Trinh Le
Analyst
trinh.lx@vdsc.com.vn
+ 84 28 6299 2006 (1536)
- Industrials

Ha Tran
Assistant
ha.ttn@vdsc.com.vn
+ 84 28 6299 2006 (1526)

Vi Truong
Assistant
vi.ttt@vdsc.com.vn
+ 84 28 6299 2006 (1517)

DISCLAIMERS

IMPORTANT DISCLOSURES FOR U.S. PERSONS

This research report was prepared by Viet Dragon Securities Corp. (“VDSC”), a company authorized to engage in securities activities in Vietnam. VDSC is not a registered broker-dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution to “major U.S. institutional investors” in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the “Exchange Act”).

Additional Disclosures

This research report is for distribution only under such circumstances as may be permitted by applicable law. This research report has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient, even if sent only to a single recipient. This research report is not guaranteed to be a complete statement or summary of any securities, markets, reports or developments referred to in this research report. Neither VDSC nor any of its directors, officers, employees or agents shall have any liability, however arising, for any error, inaccuracy or incompleteness of fact or opinion in this research report or lack of care in this research report’s preparation or publication, or any losses or damages which may arise from the use of this research report.

VDSC may rely on information barriers, such as “Chinese Walls” to control the flow of information within the areas, units, divisions, groups, or affiliates of VDSC.

Investing in any non-U.S. securities or related financial instruments (including ADRs) discussed in this research report may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the U.S. Securities and Exchange Commission. Information on such non-U.S. securities or related financial instruments may be limited. Foreign companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect within the United States.

The value of any investment or income from any securities or related financial instruments discussed in this research report denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related financial instruments.

Past performance is not necessarily a guide to future performance and no representation or warranty, express or implied, is made by VDSC with respect to future performance. Income from investments may fluctuate. The price or value of the investments to which this research report relates, either directly or indirectly, may fall or rise against the interest of investors. Any recommendation or opinion contained in this research report may become outdated as a consequence of changes in the environment in which the issuer of the securities under analysis operates, in addition to changes in the estimates and forecasts, assumptions and valuation methodology used herein.