SMC TRADING INVESTMENT JSC (HSX: SMC)

Short-term support from steel prices vs. Medium-term receivables risk

(VND bn)	Q4-FY22	Q3-FY22	+/- (qoq)	Q4-FY21	+/- (yoy)
Net revenue	4,203	5,672	-26%	6,149	-32%
NPAT-MI	-515	-188	N/A	47	N/A
EBIT	-459	-172	N/A	60	N/A
EBIT margin	-10.9%	-3.0%	-79bps	1.0%	-119bps

Source: SMC, RongViet Securities

Q4/2022 – Gone past the most difficult phase historically

- The local market's sudden drop in demand and the global market's slow period were the main cause to SMC's most negative performance since listing. 4Q overall volume went down by 30% yoy, down 25% qoq.
- Steel prices' consistent slide throughout the quarter put pressure on SMC's gross margin, which was -8,8$ in 4Q2022, the lowest since listing.
- SMC's conservative actions adhered to the industry trend, as year-end inventory was cut by half compared to 2Q2022, -40% yoy. Provision for inventory write-off was VND 108 billion, equivalent to 6.4% inventory value.

Q1/2023 and whole year outlook – Steel price trend is supportive, but obstacles arise from the construction market slowdown

- Both long and flat steel prices have been recovering since the beginning of the year, which is promising news to 1Q performance among steelmakers.
- Profit recovery depends on speed of inventory circulation. Being a downstream company, SMC has been highly flexible in terms of inventory policy, hence highly feasible recovery in 1Q. Revenue and NPAT in 1Q2023 are estimated at VND 4,415 and -2 billion respectively.
- 2023 business performance is unlikely to be supported by volume growth due to unfavourable market conditions. SMC, nevertheless, is capable of slightly positive profit margin if steel prices are stabilised throughout the year. Revenue and NPAT in 2023 are forecasted at VND 23,845 and 148 billion, equivalent to VND 1,653 EPS.
- VND ~1,000 billion in receivables from Novaland is currently overdue, posting risks of provisions and further damage to financial health.

Valuation and recommendation

Having gone through the most difficult time since its listing, SMC as a trading and manufacturing steel company can now recover quickly because steel prices have been going up since the beginning of the year. The speed of recover depends on its overall sales volume across all of its business segments, which is its ability to achieve desirable scales to offset the increasing interest expense incurred by the capacity expansion during the last couple years. We appreciate SMC's ability to recover faster than its peers in the upstream parts of the steel industry. However, we recommend to ***WATCH*** *the stock because of an unresolved receivables at Novaland, one of its major trading customer, while we seek assessments of such event on SMC's future earnings, liquidity and financial solvency.*

WATCH

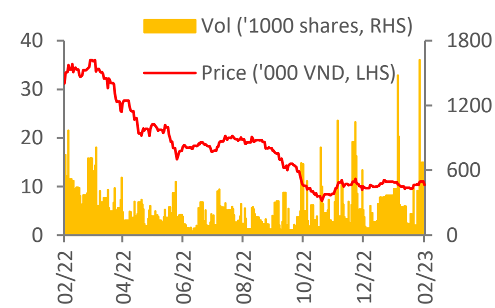
Current market price (VND)	10,450
Target price (VND)	n/a
Cash dividend (VND)	0

Stock Info

Sector	Basic materials
Market Cap (VND billion)	802
Current Shares O/S	73,606,837
Avg. Daily Volume (in 20 sessions)	347,800
Free float (%)	64
52 weeks High	37,080
52 weeks Low	6,580
Beta	0.2

	FY2021	FY2022
EPS	14,346	-8,759
EPS Growth (%)	185.8%	n/a
Diluted EPS	11,876	-8,759
P/E	2.9	n/a
P/B	1.1	n/a
EV/EBITDA	3.9	n/a
Cash dividend yield (%)	2.4%	5.2%
ROE (%)	37.5%	-33.7%

Price performance



Major Shareholders (%)	
Hanwa Co Ltd	19,7
Nguyen Thi Ngoc Loan	14,4
Foreign ownership room (%)	26.6

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Exhibit 1: Q4-2022 Results

(VND Bn)	Q4/2022	Q3/2022	+/- (qoq)	Q4/2021	+/- (yoy)
Net revenue	4203	5672	-25.9%	6,149	-31.6%
Gross profit	-368	-67	452.4%	128	-387.3%
SG&A	91	106	-13.9%	68	33.8%
Operating income	-459	-172	166.3%	60	-864.9%
EBITDA	-426	-136	212.3%	83	-611.2%
EBIT	-459	-172	166.3%	60	-864.9%
Financial expenses	102	86	18.3%	67	51.5%
- Interest Expenses	77	69	10.8%	54	42.5%
Dep. and amortization	33	36	-7.4%	23	43.7%
Non-recurring items (*)					
Extraordinary items (*)					
PBT	-534	-217	146.6%	41	-1388.3%
NPAT-MI	-515	-188	174.2%	47	-1194.1%
Adjusted NPAT-MI for (*)	-515	-188	174.2%	47	-1194.1%

Source: SMC, RongViet Securities

Exhibit 2: Q4-2022 Performance Analysis

Particulars	Q4/2022	Q3/2022	*+/- (qoq)*	Q4/2021	*+/- (yoy)*
Profitability Ratios (%)					
Gross Margin	-8.8%	-1.2%	-76bps	2.1%	-108bps
EBITDA Margin	-10.1%	-2.4%	-77bps	1.4%	-115bps
EBIT Margin	-10.9%	-3.0%	-79bps	1.0%	-119bps
Net Margin	-12.3%	-3.3%	-89bps	0.8%	-130bps
Adjusted Net Margin	-12.3%	-3.3%	-89bps	0.8%	-130bps
Turnover*(x)					
-Inventories	9.5	8.1	1.4	8.0	1.5
-Receivables	5.4	6.6	-1.2	9.9	-4.5
-Payables	5.8	5.4	0.4	7.8	-2.1
Leverage (%)					
Total Liabilities/Equity	346.1%	288.0%	581bps	252.9%	932bps

*Source: RongViet Securities, * Annualized*

Exhibit 3: Q1/2023 Performance Forecast

Particulars (VND Bn)	Q1-FY23	+/- qoq	+/- yoy
Revenue	4,415	5%	-33%
Gross profit	132	n/a	-32%
EBIT	88	n/a	-34%
NPAT-MI	-2	n/a	n/a

Source: RongViet Securities

Q1/2023 assumptions:

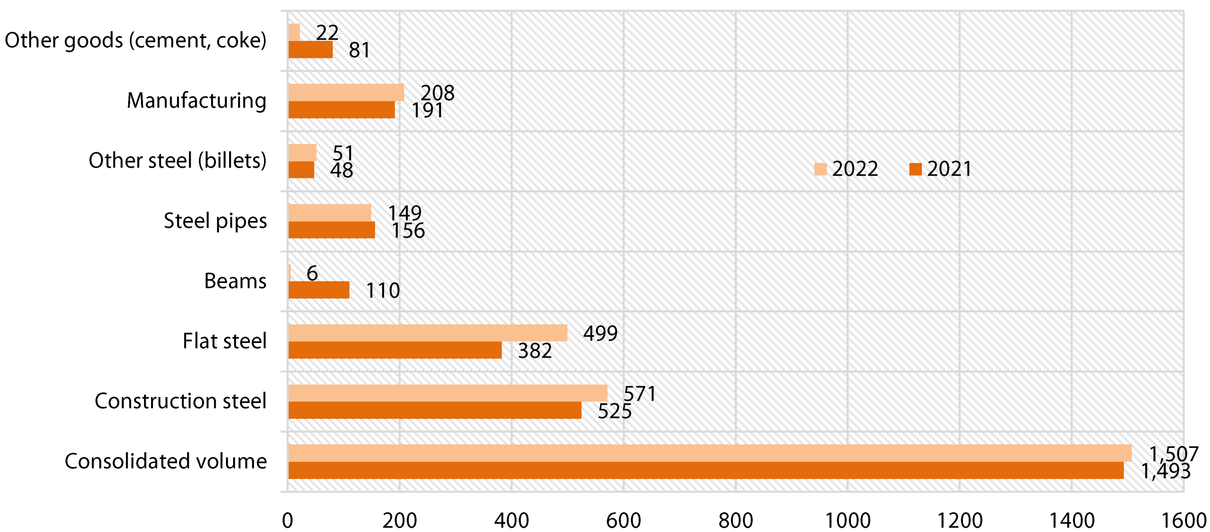
- Steel prices' uptrend throughout 1Q is the base assumption for positive gross profit.
- Volume is estimated to be lower yoy considerably because of demand slowdown, but better than 4Q22.
- Gross profit, however, might not be able to cover all expenses, especially as interest expense went up because of new debts.
- Net profit is slightly negative, which is a recovery compared to the previous six months.

Q4 2022: Both volume and price went down

Output fell due to weak demand in both domestic and foreign markets

In general, output in 2022 is lower than in 2021 due to the decline in steel demand. This can be seen clearly from Q1/2022, due to weak domestic demand for civil construction. The increase in interest rates, the devaluation of the VND, especially the credit tightening policies in the second half of the year have caused capital flows into the real estate - construction industry to stagnate. SMC said that this is common among not only for retailers but especially for developers and large general contractors, whose group represent the majority of sales volume in SMC's construction steel trading segment.

Figure 1: SMC sales volume (thousand tons)



Source: SMC, RongViet Securities

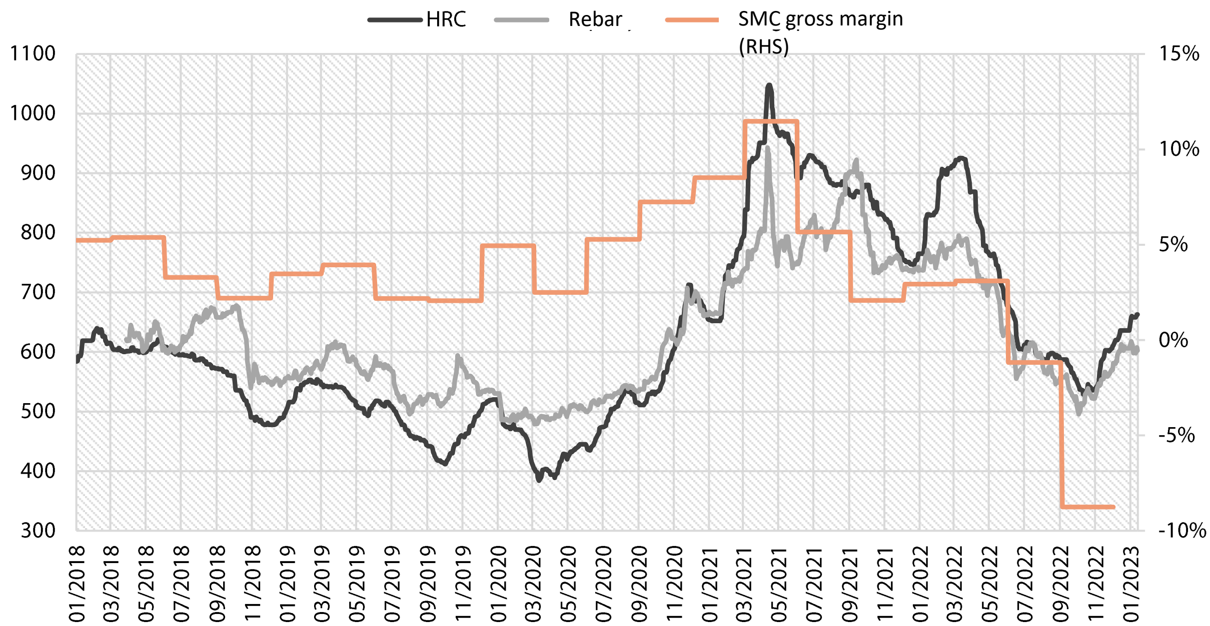
Regarding the OEM segment, the disruption of global supply activities in general and the shortage of chips in particular have affected Samsung's production plans in Vietnam. This causes the actual output of tier 1 vendors like SMC to decline. The output of this segment depends entirely on Samsung's decision, and we expect that SMC will not be able to recover the utilisation rate at SMC Phu My Precision Mechanical Factory soon.

Both global and domestic steel prices fell sharply and suddenly in the second half of 2022, the whole industry suffered

Steel prices in general have experienced a year of strong and unpredictable fluctuations, causing many steel companies to suffer losses, especially in the second half of the year. With the characteristics of a processing and trading house, SMC was under great pressure in terms of gross profit margin in Q3 and Q4/2022. In addition, steel consumption slowed down suddenly in the last months of the year, causing business results to be affected more strongly when the company had to cut selling prices aggressively to turn around inventory.

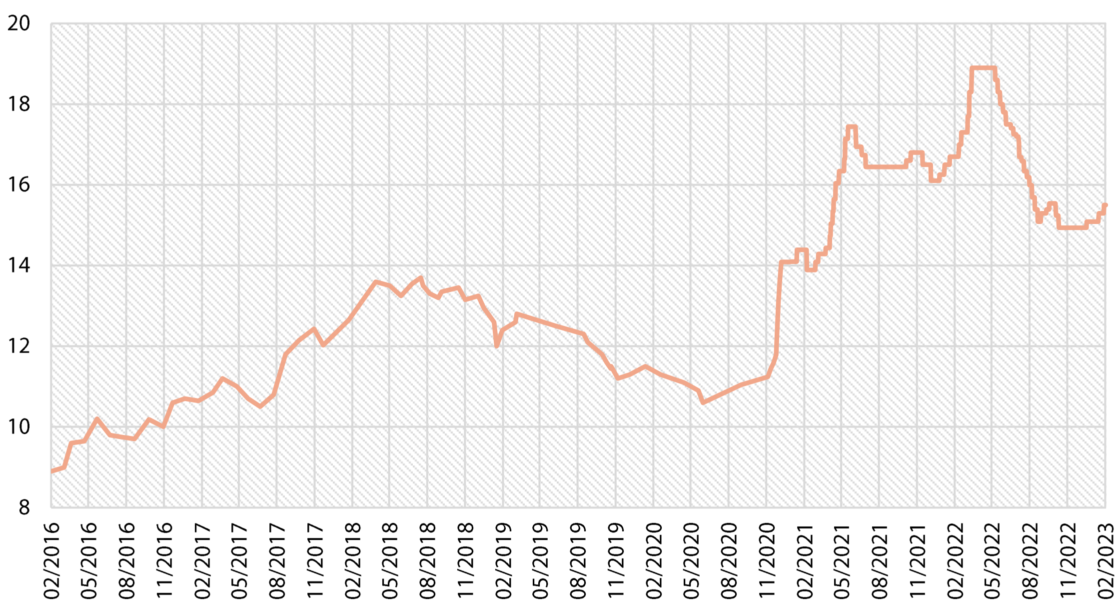
According to our calculations, SMC's processing and manufacturing activities suffered a loss in Q3 due to the continuous decline in raw material prices, and its trading activities suffered a loss in Q4 due to weak sales volume.

Figure 2: Global rebar, HRC price indices (USD per ton, LHS) and SMC's gross margin (RHS)



Source: Bloomberg, RongViet Securities

Figure 3: Domestic rebar price (VND million per ton)



Source: RongViet Securities

1Q 2023 and whole year outlook: Prices increase in the first months of the year, but the overall demand cannot fully recover immediately

1Q2023 business results will benefit from a steady increase in steel prices throughout the quarter, assisting SMC returning to positive gross profit. However, low output due to both seasonal factors (Tet month) and weak market demand will remain an obstacle for sales, preventing profit after tax from recovering to positive levels.

Steel prices are supportive in the first days of the year

The most fortunate movement for the industry's prospect is probably that steel prices in general have started to recover in the first days of the year, after bottoming in Q4/2022. Specifically, on February 24th, 2023 year-to-date, global HRC and rebar prices have improved by 10% and 4% respectively. Domestically, rebar price was adjusted twice during the first tow months, increasing by 2% in total (Figure 2,3). We consider this to be a necessary condition for downstream steelmakers to be profitable due to their quick inventory turnover cycle, and profit margin is highly dependent on the steel price trend during the period. If steel prices do not drop sharply from now until the end of Q1, SMC is likely to improve profit margin considerably.

This observation can also be true to galvanized/galvalume steel manufacturers such as HSG and NKG. Once HRC price has bottomed out and recovered, mills can resume their raw material purchases.

Consumption will take time to recover

We maintain our view on the supply-demand conditions of the steel industry as presented in our 2023 Strategy Report, which emphasizes that domestic steel demand in 2023 will depend heavily on the ability to accelerate disbursements in key public infrastructure projects, and the building material market will not be as active this year, due to the slowdown from the residential segment.

Regarding SMC, overall volume will remain under pressure in most segments. SMC is one of the leading steel distributors in the southern market for civil construction, so the potential growth in the group of retailers or developers and general contractors is still limited in the next few quarters. Commenting on the ability to penetrate public investment projects, such as the North-South Highway, SMC is quite conservative because of the typical business nature of public projects. We believe that the proportion of revenue from these projects will not be able to make up for the shortfall in sales to general contractors and private property developers.

Capacity expansion plan is flexible according to market conditions, corporate bonds at favourable rates help control financial expenses

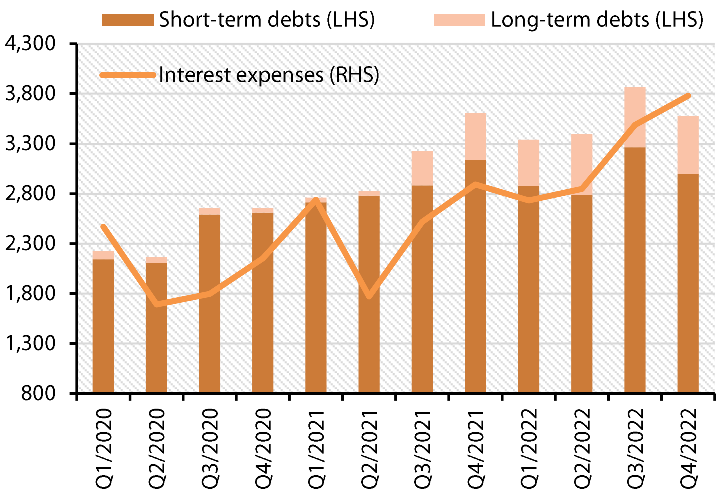
During 2021-2022, SMC made large capital expenditures and put into operation new factories, including a cluster of new factories in Phu My 2 Industrial Park. However, further expansion has been slowed down to match industry demand growth. In particular, phase 2 of SMC Da Nang Steel Processing Factory will install machinery and equipment when the market demand warms up, slower than the original plan to operate from the beginning of 2023. SMC Precision Mechanical Factory Phu My will also postpone expansion until Samsung recover their orders to improve the utilisation rate of phase one, which is currently below 50%.

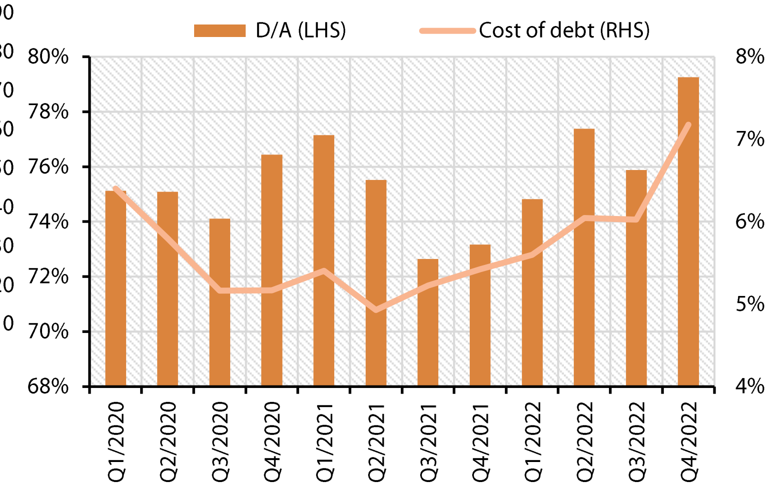
Total disbursements for fixed asset in the period of 2021-2022 reached VND 577 billion, of which the value of fixed assets increased by VND 432 billion during the period. At the end of 2022, SMC had a long-term debt of VND 579 billion, an increase of VND 530 billion compared to the end of 2020 (before capacity expansion).

Of the long-term debt incurred during this period, more than VND 313 billion are bonds maturing in 2026 and 2024, with interest rates of 5.04% and 8.2%/year, respectively , the rest is bank loans and finance lease. The fact that SMC has fixed interest rates for most long-term loans is an advantage for its financial health in the context of rising interest rates like in 2022. SMC's average cost of borrowing in 2022 was around 7.2%, a favorable cost of capital.

On the other hand, operating a series of new capacity in the difficult period is also a burden as the company has to find ways to increase utilisation to reach breakeven point. SMC's financial expense was about VND90 billion per quarter during the last year, double that of 2021, and are forecasted to remain at this level in 2023.

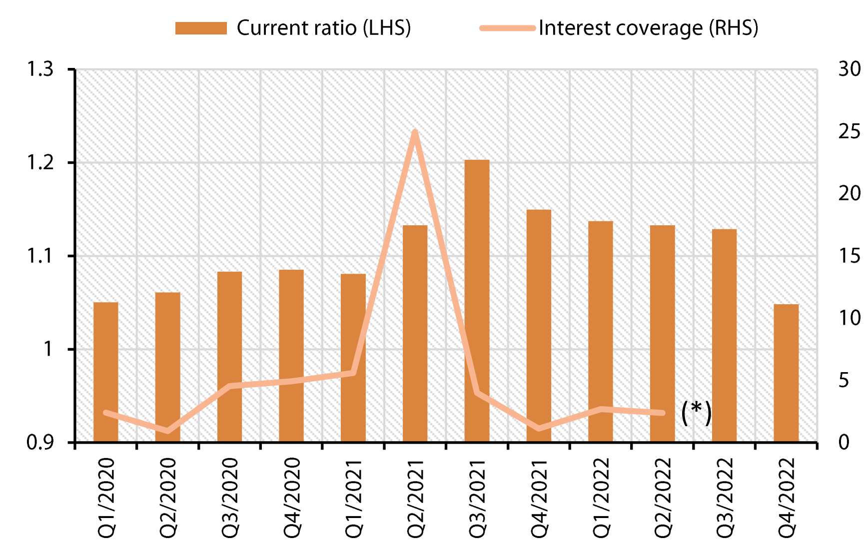
Figure 4, 5: Debts, interest expenses (VND billion) and cost of debt





Source: SMC, RongViet Securities. Cost of debt is annualised.

Figure 6: SMC's current ratio and interest coverage



Source: RongViet Securities. (*) 3Q and 4Q 2022 EBITDA were negative

Receivables at Novaland and the risks of provision for bad debts

Novaland is one of SMC's major customers in the construction steel distribution business. Currently, bout 1,000 billion VND is overdue receivables, as this property developer is having liquidity problems.

In the short term, SMC said it can arrange with banks and suppliers to extend payment time while waiting debt collections. In the long term, we believe that the possible impact on future profit will be very large if SMC has to make full provision for the amount. Since this amount has become doubtful debt and is quite large compared to SMC's average quarterly profit, its medium-term profit will depend entirely on the speed and volume of debt collection from Novaland.

As the impact of this overdue debt on SMC's future earnings has not been clearly assessed, we do not set a target price and we recommend investors watch this stock until the majority of the impact has been reflected on business performance. In this report, SMC's quarterly and annual business results is forecasted assuming all debts to Nova are recovered.

VND Billion

INCOME STATEMENT	**FY2021**	**FY2022**	**FY2023E**	**FY2024F**
Revenue	**21,315**	**23,147**	**23,845**	**26,550**
COGS	19,835	23,182	23,046	25,726
Gross profit	**1,480**	**-35**	**799**	**824**
Selling Expense	219	216	202	225
G&A Expense	127	128	132	147
Finance Income	109	110	53	39
Finance Expense	183	360	341	308
Other profits	3	29	0	0
PBT	**1,100**	**-591**	**197**	**201**
Prov. of Tax	199	59	27	29
Minority's Interest	27	-72	22	23
PAT to Equity S/H	**874**	**-578**	**148**	**149**
EBIT	1,134	-379	464	452
EBITDA	1,230	-247	621	647

%

FINANCIAL RATIO	**FY2021**	**FY2022**	**FY2023E**	**FY2024F**
Growth (%)				
Revenue	35.5%	8.6%	3.0%	35.5%
Operating Income	123.6%	-120.1%	-351.8%	123.6%
EBITDA	176.4%	-133.4%	-222.5%	176.4%
PAT	185.6%	-166.1%	-125.6%	185.6%
Total Assets	34.1%	-7.4%	9.5%	34.1%
Equity	53.3%	-26.5%	-4.4%	53.3%
Profitability (%)				
Gross margin	6.9%	-0.2%	3.3%	3.1%
EBITDA margin	5.8%	-1.1%	2.6%	2.4%
EBIT margin	5.3%	-1.6%	1.9%	1.7%
Net margin	4.1%	-2.5%	0.6%	0.6%
ROA	9.7%	-6.9%	1.6%	1.6%
ROE	37.5%	-33.7%	9.0%	9.5%
Efficiency				
Receivable Turnover	7.5	7.8	8.8	8.9
Inventory Turnover	7.8	14.7	8.7	9.6
Payable Turnover	6.7	7.8	6.7	7.6
Liquidity				
Current	1.1	1.0	1.1	1.0
Quick	0.7	0.8	0.7	0.7
Finance Structure (%)				
Total Debt/Equity	154.8%	208.9%	242.6%	274.7%
Current Debt/Equity	135.0%	175.1%	197.1%	237.3%
Long-term Debt/Equity	19.8%	33.8%	37.5%	25.9%

VND Billion

BALANCE SHEET	**FY2021**	**FY2022**	**FY2023E**	**FY2024F**
Cash and cash equivalents	625	814	895	526
Short-term investments	704	687	687	687
Accounts receivable	2,858	2,955	2,694	2,967
Inventories	2,544	1,573	2,650	2,675
Other current assets	290	249	398	404
Property, plant & equipment	1,188	1,182	1,206	1,182
Acquired intangible assets	138	139	138	137
Long-term investments	328	304	304	304
Other non-current assets	330	436	251	309
Total assets	**9,006**	**8,339**	**9,225**	**9,190**
Accounts payable	2,970	2,985	3,457	3,370
Short-term borrowings	3,144	2,997	3,097	3,197
Long-term borrowings	461	579	744	584
Other non-current liabilities	5	41	43	46
Bonus and Welfare fund	7	7	7	7
Technology-science, dev. fund	0	0	0	0
Total liabilities	**6,587**	**6,609**	**7,348**	**7,204**
Common stock and APIC	863	990	990	990
Treasury stock (enter as -)	-1	-1	-1	-1
Retained earnings	1,081	338	481	588
Other comprehensive income	1	1	1	1
Inv. and Dev. Fund	385	385	387	390
Total equity	**2,329**	**1,712**	**1,858**	**1,968**
Minority Interest	**90**	**18**	**18**	**18**

VALUATION RATIO (*)	**FY2020**	**FY2021**	**FY2022E**	**FY2023F**
EPS (VND)	14,346	-8,759	1,653	1,663
P/E (x)	2.9	-1.1	12.0	11.9
BV (dong)	38,177	23,235	21,015	22,262
P/B (x)	1.1	0.4	0.9	0.9
DPS (dong/cp)	1.000	500	-	500
Dividend yield (%)	2.4%	5.2%	0.0%	2.5%

VALUATION MODEL	***Price***	***Weight***	***Average***
Sum of the parts	n/a		n/a
Target price (VND)			**n/a**

VALUATION HISTORY	***Price***	***Recommendation***	***Period***
03/2021	30,300	ACCUMULATE	Intermediate
08/2022	n/a	n/a	n/a
12/2022	n/a	n/a	n/a

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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