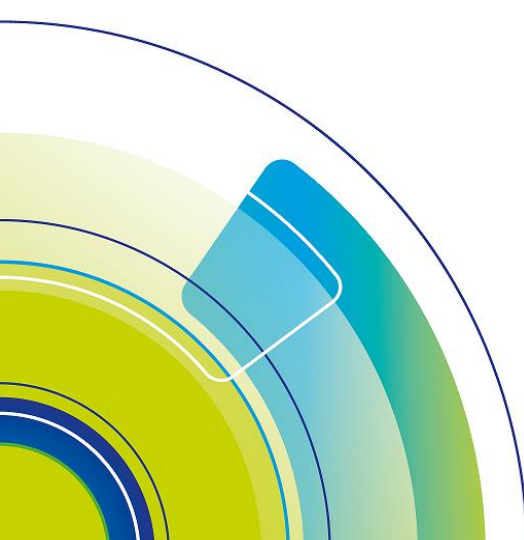




HPG Update - BUY

Thursday, June 16, 2022



Mr. Huy Huynh

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Company Update

Recommendation

BUY

HOSE: HPG

Steel manufacture

Current price (VND) 33,800

Target price (VND) 54,870

Expected share price return 62.3%

Expected dividend yield 1.4%

Expected total return 63.7%

Stock performance (%)

	YTD	1M	3M	12M
Absolute	-26.8	-15.4	-32.2	-32.8
Relative	-13.9	-18.7	-21.2	-32.2

Source: Bloomberg



Ownership

Mr. Tran Dinh Long (Chair)	25.35%
Ms. Vu Thi Hien (Chair's wife)	7.34%
Dragon Capital	4.95%
VOF Investment Limited	3.76%

Stock Statistics

10-Jun-22

Bloomberg code HPG VN

52-week range (VND) 32,650 - 58,400

Shares O/S (m) 4,473

Mkt cap (VND bn) 151,856

Mkt cap (USD m) 6,575

Foreign room left (%) 28.1

Est. free float (%) 54.3

3m avg daily vol (shrs) 20,039,070

VND/USD 23,095

Index: VNIndex / HNX 1299.08/310.69

HOA PHAT GROUP JSC (HPG VN)

HPG's longer term outlook remains positive as capacity expansion has begun, however the company is unlikely to repeat last year's stellar results as short term margin pressures mount and capacity limitations restrict growth. We maintain our **BUY** recommendation with a pre-issuance target price of 54,870 VND/share at the end of 2022, equivalent to a forward P/E of 6.4x.

In May 2022, total crude steel production of Hoa Phat reached 780,000 tons, increasing 16% yoy. While total steel sales of all kind reached 660,000 tons, increasing 10% yoy. Construction steel sales in May reached 393,000 tons, increasing 21% yoy as May 2021 was a low base when Ho Chi Minh city went into lockdown period due to COVID-19. Exporting activities also contributed to the positive operation results of Hoa Phat as the company exported 167,000 tons of steel in May (+100% yoy).

In 5 months of 2022, Hoa Phat produced 3.6 million tons of crude steel (+10% yoy), while total steel sales reached 3.4 million tons (+5% yoy). Construction steel is still the main product of the company, contributing 2 million tons to the total sale volume (+26% yoy), in which 631,000 tons of construction steel sales comes from exports (+100% yoy). Sales volumes of HRC steel reached 1.2 million tons, slightly higher than 2021.

Hoa Phat 5 months production	5M.2021	5M.2022	Growth
Total crude steel (mil. tons)	3.27	3.60	10%
Total sale volume (mil. tons)	3.23	3.40	5%
Construction steel sale volume	1.59	2.00	25.7%
HRC steel sale volume	1.10	1.20	9.1%

Source: Hoa Phat

The outlook for the remainder of 2022 is not as attractive as years past as Hoa Phat's growth is expected to be constrained by capacity limitations. The high price of coal also puts pressure on the company's gross margin as global demand for coal has been increasing. The recent COVID wave that put China into a long lockdown period has resulted in reduced global steel demand, which has prevented steel prices from

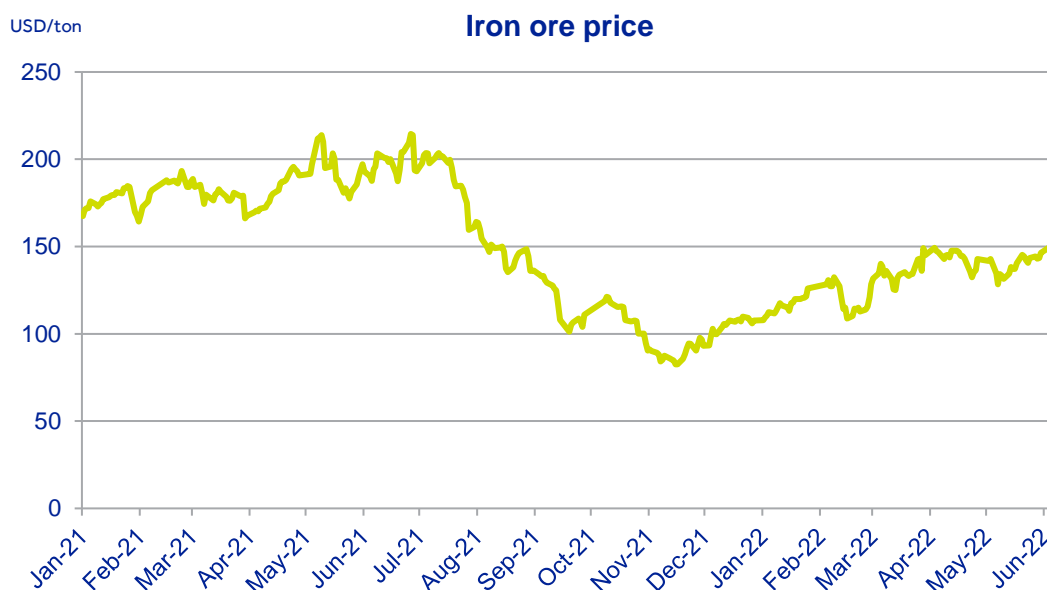
HPG SUMMARY	2018	2019	2020	2021	2022E
Net Sales (VNDbn)	55,836	63,658	90,119	149,679	154,027
Growth (%)	21.0%	14.0%	41.5%	65.5%	3.4%
EBITDA (VNDbn)	12,834	12,381	22,359	46,475	36,497
Growth (%)	10.4%	-3.5%	80.6%	109.1%	-21.7%
Net Profit (VNDbn)	8,601	7,508	13,506	34,520	24,829
Growth (%)	7.1%	-12.7%	79.9%	155.6%	-26.4%
EPS (bonus-adjusted, VND)	1,858	1,691	3,020	7,170	4,056
Growth (%)	16.9%	-9.7%	78.5%	155.6%	-26.4%
ROE (%)	24.3%	18.6%	25.2%	37.9%	27.8%
ROIC (%)	13.1%	15.2%	17.6%	29.3%	25.4%
Net debt/EBITDA (x)	1.1	1.3	1.4	0.1	0.0
EV/EBITDA (x)	5.7	11.1	7.6	8.8	5.8
PER (x)	6.1	8.6	12.9	8.9	6.4
PBR (x)	1.5	2.0	2.3	2.1	1.4
DPS (VND)	0.0	0.0	500	500	500
Dividend Yield (%)	0%	0%	1.1%	1.1%	1.4%

keeping pace with increasing coal prices and have been putting a squeeze on steel producers' margins.

Although the company is facing many short-term challenges, we still maintain a positive outlook for Hoa Phat in the long term. The company has started construction of Dung Quat Phase 2 project, which is expected to be completed in early 2024 and will bring an additional 5 million tons production of HRC to the market (HPG's current capacity is 8.6 million of crude steel per year, in which HRC capacity accounts for 3 million). Hoa Phat is also in the construction phase of a factory for the production of shipping containers, which is current in the machine set up phase and is expecting the first products to come to the market in November and diversify Hoa Phat's production.

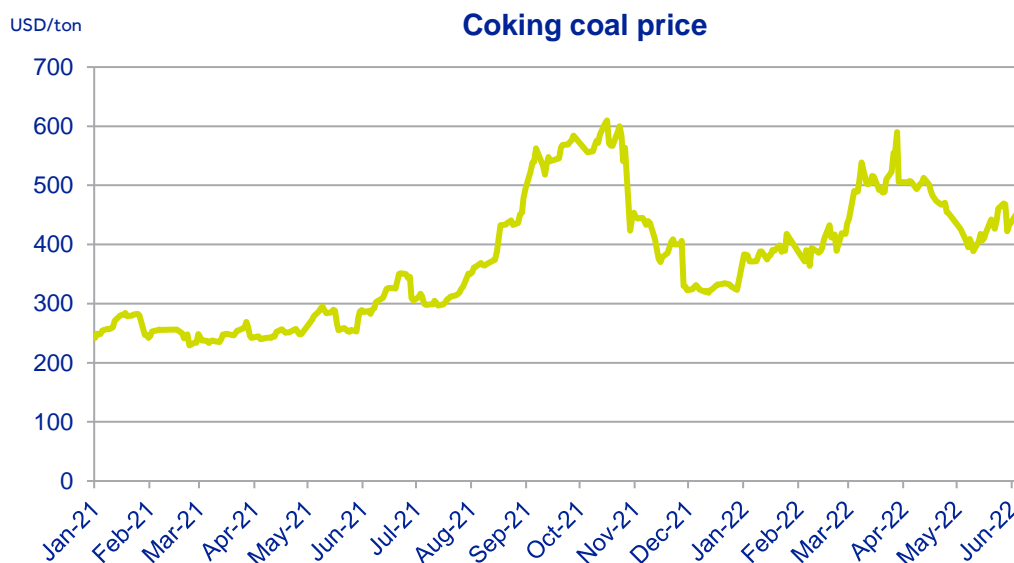
Short-term unfavorable market conditions

Although facing flat demand from large Chinese steel makers due to strict lockdowns since COVID broke out in many big cities of China from April 2022, iron ore prices are still in an uptrend since the end of 2021.



Source: Bloomberg

Iron ore prices have increased 50% since the beginning of 2022. In our opinion, the main factors pushing iron ore price are rising fuel prices and tight production from large miners. The easing of lockdowns in some large economic hubs in China indicate positive signs for steel making activities, where steel production accounts for nearly half of total global production. Therefore, the outlook for iron ore prices could be not lower than current levels, as the return from lockdowns in China and higher costs of mining activities will support higher prices.



Source: Bloomberg

The rise of oil prices have put a pressure on the energy industry, making countries shift to alternative sources of energy beside oil and gas. Coking coal experienced an uptrend since the beginning of 2022, aided by the Russian invasion of Ukraine, which strongly affected the global coal supply as many countries refused to buy coal from Russia.



Source: Bloomberg

Steel price started to fall from their peak since the beginning of April as major economic hubs in China went into strict lockdowns due to the outbreak of COVID-19. The stagnation during strict lockdowns of the world's biggest steel consumer has reduced the global steel consumption outlook and led to the reduction in steel prices.

In our opinion, current situation of steel market is putting high pressure on steel makers' gross margin from both sides as selling prices have receded but input costs are rising. As per our estimations, the average gross margin from BOF steel makers has fallen from over 23% to less than 17% in April and May, making the expectation for Q2 2022 operation result of steel makers to be much lower than Q1 2022.

Company outlook and valuation update

Domestic construction steel prices have reduced to 17,800 VND/kg due to low demand from builders. Although this price level is 14% higher than average of 2021 (15,900 VND/kg), it is still 2.1% lower than 5M average in 2022 of 18,210 VND/kg. Construction steel prices reached the peak in the middle of March at 19,500 VND/kg before reversing trend when China applied mass lockdowns in early April. Domestic real estate development activities have slowed as access to credit by real estate developers has become more difficult following some recent events that have lead to more scrutiny on capital raising through the credit markets. Although the limitations in real estate credit could help to stabilize the market, it makes it more difficult for developers to raise funds for new project through the banking system or debt markets. Moreover, global steel prices remain subdued by low construction and industrial activities in China as lockdowns have been preventing many development activities.

For the long-term, as lockdowns in China are lifted, steel demand for industrial and construction activities will return and global demand is expected to revert to pre-China lockdown levels. We also expect global steel prices can recover to the level of 800 USD/ton by the end of 2022 as economic activities in China recover.

We expect HPG can reach 154,026 bil.VND revenue (+3.4% yoy) and 24,828 bil.VND (-26.4% yoy) net profit in FY2022. Our projections are 3.7% and 0.6% lower to the company guidance in revenue and net profit, respectively, as we put a cautious view on the recovery of both domestic and global steel price till the end of 2022. Combining both DCF and P/E method, we derive a target pre-issuance price of HPG to the end of 2022 at 54,870 VND per share, equivalent to a 6.4x F. P/E multiple.

HPG FINANCIALS MODEL	Price (VND):		33,800	Target (VND):		54,870	Mkt cap (VND bn):		151,856
(VND bn except where stated)	2018	2019	2020	2021	2022E	2023E	2024E		
Total Net Sales	55,836	63,658	90,119	149,679	154,026	160,266	233,046		
<i>Sales growth (%)</i>	<i>21.0%</i>	<i>14.0%</i>	<i>41.5%</i>	<i>65.5%</i>	<i>3.4%</i>	<i>4.1%</i>	<i>45.4%</i>		
CoGS ex-dep'n	41,882	47,510	66,415	95,952	114,408	118,594	178,978		
SG&A	1,121	1,232	1,784	2,925	3,121	3,247	4,722		
<i>SG&A as % of net sales</i>	<i>2.0%</i>	<i>2.0%</i>	<i>2.0%</i>	<i>2.0%</i>	<i>2.0%</i>	<i>2.0%</i>	<i>2.0%</i>		
EBITDA	12,834	12,381	22,359	46,475	36,497	38,424	49,346		
<i>EBITDA margin (%)</i>	<i>23.0%</i>	<i>19.8%</i>	<i>22.5%</i>	<i>31.1%</i>	<i>23.7%</i>	<i>24.0%</i>	<i>21.2%</i>		
Depreciation	2,284	2,109	4,798	5,531	5,566	5,601	8,987		
Operating profit	10,550	9,943	15,289	37,008	30,931	32,822	40,359		
<i>Operating profit margin (%)</i>	<i>18.9%</i>	<i>16.4%</i>	<i>16.7%</i>	<i>24.7%</i>	<i>20.1%</i>	<i>20.5%</i>	<i>17.3%</i>		
Net interest expense	377	1,450	2,207	1,933	2,068	2,748	2,421		
<i>as % of avg, net debt</i>	<i>5.7%</i>	<i>8.9%</i>	<i>6.8%</i>	<i>19.0%</i>	<i>149.7%</i>	<i>385.6%</i>	<i>37.5%</i>		
Tax	1,506	1,163	1,782	2,857	3,954	4,120	5,197		
<i>Effective tax rate (%)</i>	<i>14.6%</i>	<i>13.7%</i>	<i>11.7%</i>	<i>13.7%</i>	<i>13.7%</i>	<i>13.7%</i>	<i>13.7%</i>		
Minorities	27.5	23.5	67.5	42.8	47.4	48.1	54.8		
Net profit	8,601	7,508	13,438	34,520	24,828	25,870	32,635		
<i>Net profit margin (%)</i>	<i>15.0%</i>	<i>11.7%</i>	<i>14.9%</i>	<i>23.1%</i>	<i>16.1%</i>	<i>16.1%</i>	<i>14.0%</i>		
Number of shares (m)	2123.9	2,761.1	3,313.3	4,472.9	5,814.7	5,814.7	5,814.7		
Adjusted EPS (VND)	1,858	1,691	3,020	7,170	4,056	4,226	5,332		
<i>EPS growth (%)</i>	<i>16.9%</i>	<i>-9.7%</i>	<i>78.5%</i>	<i>155.6%</i>	<i>-26.4%</i>	<i>4.2%</i>	<i>26.1%</i>		

KEY CASHFLOW AND BS ITEMS	2018	2019	2020	2021	2022E	2023E	2024E
Increase in working capital	(2,766)	(9,602)	(12,914)	(16,011)	(2,687)	(1,888)	(2,008)
Capex	27,594	13,203	9,370	3,407	40,515	30,535	5,501
<i>Change in investment in affiliates</i>	-	-	-	-	-	-	-
Dividends paid	-	-	1,406	1,677	1,677	-	-
Increase in net debt	15,627	4,217	1,522	(15,350)	(2,206)	868.0	(5,217)
<i>Net debt, end of year</i>	<i>14,406</i>	<i>18,623</i>	<i>18,623</i>	<i>2,484</i>	<i>278</i>	<i>1,146</i>	<i>(4,070)</i>
Enterprise value	78,016	103,295	170,814	281,660	291,968	311,786	342,935
<i>Shareholders' equity</i>	<i>41,359</i>	<i>47,573</i>	<i>59,219</i>	<i>84,765</i>	<i>108,432</i>	<i>133,092</i>	<i>164,201</i>
BVPS (VND)	19,473	17,229	17,874	18,950	24,242	29,755	36,710
Net debt / equity (%)	35%	39%	54.6%	3%	1%	1%	-2%
<i>Net debt / EBITDA (x)</i>	<i>1.1</i>	<i>1.5</i>	<i>1.4</i>	<i>0.1</i>	<i>0.01</i>	<i>0.0</i>	<i>(0.3)</i>
Total assets	78,225	91,119	131,511	134,834	174,464	202,581	237,910

KEY RETURN AND VALUATION RATIOS	2018	2019	2020	2021	2022E	2023E	2024E
ROE (%)	24.3%	17.5%	25.2%	37.9%	27.8%	22.7%	23.3%
ROA (%)	16.2%	9.3%	11.5%	19.5%	16.1%	14.8%	16.1%
<i>ROIC (%)</i>	<i>19.1%</i>	<i>13.8%</i>	<i>17.6%</i>	<i>28.3%</i>	<i>24.4%</i>	<i>22.2%</i>	<i>22.9%</i>
WACC (%)	12.7%	12.7%	12.0%	12.7%	12.7%	12.7%	12.7%
EVA (%)	6.4%	1.1%	5.6%	15.7%	13.7%	9.6%	10.2%
<i>PER (x)</i>	<i>6.1</i>	<i>8.6</i>	<i>12.9</i>	<i>10.2</i>	<i>6.4</i>	<i>6.1</i>	<i>5.5</i>
EV/EBITDA (x)	5.7	8.6	7.6	8.8	8.5	7.6	5.9
<i>EV/FCF (x)</i>	<i>(3.6)</i>	<i>(8.7)</i>	<i>8.5</i>	<i>25.5</i>	<i>(29.2)</i>	<i>155.8</i>	<i>16.6</i>
PBR (x)	1.5	1.5	2.3	2.1	1.4	1.3	1.0
PSR (x)	1.1	1.4	1.5	1.6	1.5	1.4	0.9
<i>EV/sales (x)</i>	<i>1.4</i>	<i>1.7</i>	<i>1.9</i>	<i>2.2</i>	<i>2.0</i>	<i>1.9</i>	<i>1.6</i>
Dividend yield (%)	0.0%	0.0%	1.1%	1.1%	1.4%	0.0%	0.0%

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DISCLAIMER

Our Recommendation System

BUY: where we believe prospective 12 month VND total return (including dividends) will be 15% or more.

HOLD: where we believe it will be -15% to 15%.

SELL: where we believe it will be lower than -15%.

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