

Nhon Trach 2 (NT2)

Stay strong in the face of adversity

November 2, 2022

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In 3Q22, revenue rose by 74% YoY while NPAT contracted by 27% YoY

In 3Q22, PV Power Nhon Trach 2 (NT2) posted high revenue of VND2,168 billion (+74% YoY) while NPAT recorded only VND199 billion (-27% YoY) since NT2 had to set aside for bad debt from Vietnam Electricity (EVN). Commercial power output rose sharply by 95% YoY to 897.3 million kWh thanks to growing demand in 3Q22 and weakness in electricity consumption in the Southern region in the same period last year following the implementation of COVID-19 protection protocols.

NT2 booked unexpectedly high compensation for exchange rate losses for 2022, contributing to positive results

NT2 booked about VND340 billion out of VND420 billion in compensation for exchange rate losses from EVN Electric Power Trading Company (EPTC) during 2016-2021. It exceeded our expectation of VND100 billion each year of the 2022-2024 period.

The outlook remains bright in 2023 thanks to rising electricity demand and hydropower no longer supported by favorable weather

We forecast NT2's power output in 2022 to reach 4,217 million kWh (+32% YoY) on the back of continued recovery in electricity demand from the low base of 2021. In addition, hydropower is forecasted to no longer enjoy favorable weather while coal prices may continue to stay high, which will boost mobilization from gas-fired power plants. Despite a major overhaul in 2023 where NT2 might have to suspend operation for 45-50 working days or 100,000 hours, we believe NT2's output in 2023 will still touch 4,309 million kWh (+2.2% YoY) on rising demand.

We recommend BUY for NT2 with a target price of VND33,900/share

Based on FCFF and EV/EBITDA valuation methods, business outlook and possible risks, we recommend BUY for NT2 stocks. The target price is VND33,900/share, 33.5% higher than the closing price on October 31, 2022.

Buy maintain

Target price VND33,900

Upside/Downside	33.5%
Current price (Oct 31, 2022)	VND25,400
Consensus target price	VND29,900
Market cap (VNDbn)	7.313

Trading data

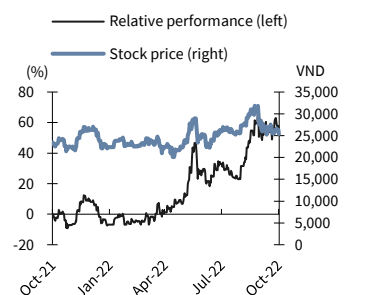
Free float	32.3%
3M avg trading value (VNDbn)	46.27
Foreign ownership	34.6%
Major shareholder	PV Power (59.4%)

Share price performance

(%)	1M	3M	6M	12M
Absolute	-7.6	1.2	17.1	12.2
Relative	1.9	18.8	55.9	57.7

Forecast earnings & valuation

FY-end	2020A	2021A	2022F	2023F
Revenue (VNDbn)	6,082	6,150	9,439	9,045
EBIT (VNDbn)	810	593	1,094	931
NPATMI (VNDbn)	625	534	1,034	889
EPS (VND)	2,095	1,778	3,592	3,088
EPS growth (%)	-17.5	-15.1	102.0	-14.0
P/E (x)	10.3	14.2	9.4	11.0
EV/EBITDA (x)	4.6	5.8	5.2	5.2
P/B (x)	1.5	1.7	2.6	2.6
ROE (%)	14.6	12.6	22.3	18.8
Dividend yield (%)	11.6	7.9	7.4	8.9



Source: Bloomberg, KB Securities Vietnam

Business performance

In 3Q22, revenue rose by 74% YoY while NPAT contracted by 27% YoY

In 3Q22, NT2 posted high revenue of VND2,168 billion (+74% YoY) while NPAT recorded only VND199 billion (-27% YoY). Commercial power output rose sharply by 95% YoY to 897.3 million kWh thanks to growing demand in 3Q22 and weakness in electricity consumption in the Southern region in 3Q21 due to the implementation of COVID-19 protection protocols.

Plummeting NPAT in 3Q22 came from: (1) huge compensation for NT2 in 3Q21 as the National Load Dispatch Center (A0) did not mobilize enough committed output resulting from reduced demand during COVID lockdowns and (2) rising general and administrative (G&A) expenses after recording VND187 billion in write-offs for EVN's bad debt.

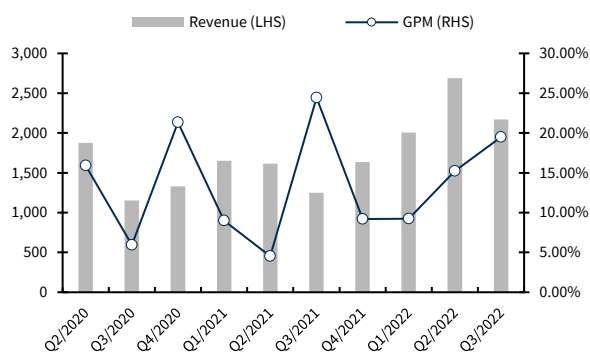
Gross profit margin in the third quarter kept improving thanks to compensation for exchange rate losses

NT2 booked about VND340 billion out of VND420 billion in compensation for exchange rate losses from EPTC in the 2016-2021 period. Moreover, contractual output (Qc) in 3Q22 was estimated at 761.8 million kWh, representing 85% of NT2's total commercial power output during the quarter. We believe the above two reasons were the key factors behind high gross profit margin of 19.5% in 3Q22, only below the 24.4% level of 3Q21 after receiving compensation for undistributed volume.

NT2 set aside VND187 billion for EVN's bad debt

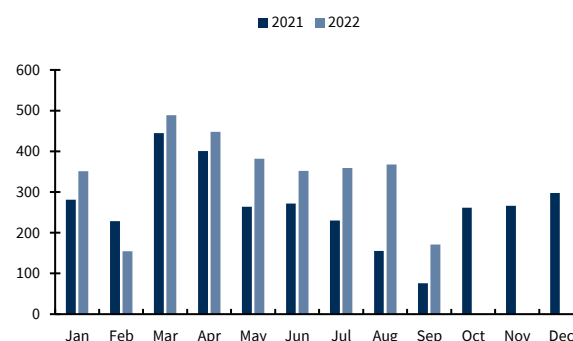
In the third quarter of 2022, NT2 recorded VND209 billion (+10x YoY) in G&A expenses due to the provision for bad debt from EVN. As far as we know, it was attributable to the incurred transportation cost arising from the new gas pipeline from Phu My to Ho Chi Minh City under a tripartite gas deal among PV GAS (GAS), NT2 and EVN. NT2 agreed to pay the incurred cost for GAS and pass it on to electricity prices through a power purchase agreement (PPA) with EVN. However, EVN disagreed on this issue, prompting NT2 to make a provision for this amount of money until further decisions from the Government to reverse it in the future.

Fig 1. NT2 – Revenue, gross profit margin (VNDbn, %)



Source: Nhon Trach 2, KB Securities Vietnam

Fig 2. NT2 – Commercial power output (million kWh)



Source: Nhon Trach 2, KB Securities Vietnam

Table 1. NT2 – 2Q22 business results

VND bn	9T2021	9T2022	YoY %	Notes
Output (mil. kWh)	2,350	3,073	30.8%	
Contractual output (Qc)	2,350	2,615	11.3%	In 2021, NT2 only operated according to the assigned contractual output, did not generate electricity on the CGM.
Output sold on the CGM (Qm)	0	458	N/A	
Average gas price (USD/MMBTU)	7.57	9.86	30.2%	Gas prices increased due to Brent oil price surge in 9M2022.
Average selling price (VND/kWh)	1,921	2,233	16.2%	Average selling price increased thanks to favorable price movements on the CGM.
Revenue (billion VND)	4,515	6,863	52.0%	The increase in revenue was mainly due to high gas prices, which led to an increase in the average selling price of both PPA and CGM contracts due to NT2's effective bidding strategy. In addition, NT2 said that it has recorded 340 billion VND in exchange rate compensation from EVN in Q3/2022.
Gross profit	526	1,017	93.3%	
GPM (%)	11.65%	14.81%		Gross profit margin improved thanks to high Qc to total volume and NT2 has an effective bidding strategy that keeps CGM prices high while NT2 has retroactively business results under the new PPA contract in the same period of Q2/2021.
SG&A	(62.0)	(247.6)	299.3%	NT2 made provision for bad debts of VND187 billion from EVN in 3Q2022.
% SG&A / Revenue	-1.37%	-3.61%		
Profit from operating activities	464	769		
Financial income	13.5	6.0		
Financial expenses	47.7	7.4	-84.4%	Financial expenses were significantly reduced thanks to NT2 repaying long-term debts in 2Q2021.
Other net income	5	0		
Profit before taxes	435	768	76.5%	
Profit after taxes	413	724	75.3%	
NPM (%)	9.15%	10.55%		

Source: Nhon Trach 2, KB Securities Vietnam

The outlook remains bright in 2023 thanks to rising electricity demand and hydropower no longer supported by favorable weather

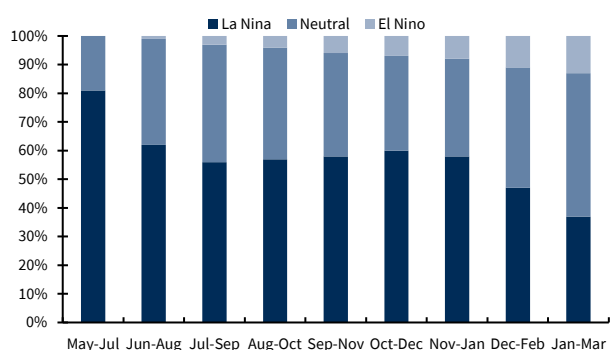
We believe the recovery of electricity demand nationwide, especially in the South, will be a growth engine for power plants in the region and NT2. We forecast NT2's electricity output this year to reach 4.217 million kWh (+32% YoY) thanks to the continued recovery of consumption demand against the low base seen in 2021 due to social distancing and low load.

The International Research Institute for Climate and Society (IRI) and the National Centre for Hydro-Meteorological Forecasting said the La Nina pattern would likely persist until the end of 2022. Besides, the forecast suggested an above 50% chance of weather entering the neutral phase from 2023, which means less water flowing into dams for hydroelectric power stations compared to the 2021-2022 period. Furthermore, the Brent price is projected to cool in 2023, averaging USD90/barrel, helping NT2 gain its competitively advantageous position and hence receive higher mobilization. Also, coal-fired power plants are facing a lot of difficulty arising from surging coal prices in the face of scarce

supply caused by Western sanctions against Russian energy. We anticipate coal prices will remain high and further increase for the rest of 2022 and in early 2023 amid limited supply and growing demand among major countries, especially Asian ones, following their post-pandemic economic reopening.

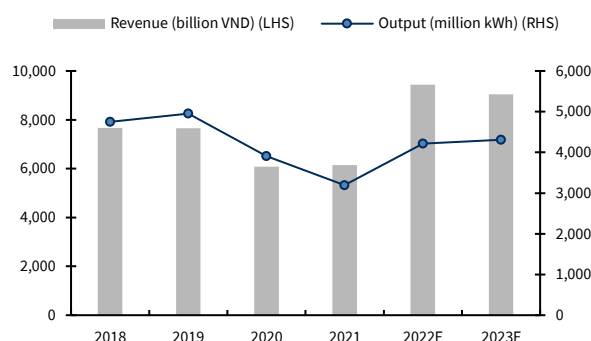
In that context, we believe that gas-fired thermal power plants will have an advantage over coal-fired power plants, especially in the South. Despite a major overhaul in 2023 where NT2 might have to suspend operation for 45-50 working days or 100,000 hours, we believe NT2's output in 2023 will still touch 4,309 million kWh (+2.2% YoY) on rising demand. Accordingly, we estimate NT2's NPAT at VND885 billion (-26% YoY) and revenue at VND9,045 billion (-4% YoY) in 2023, given the high base achieved in 2022 after receiving compensation for exchange rate losses.

Fig 3. Global - Weather patterns



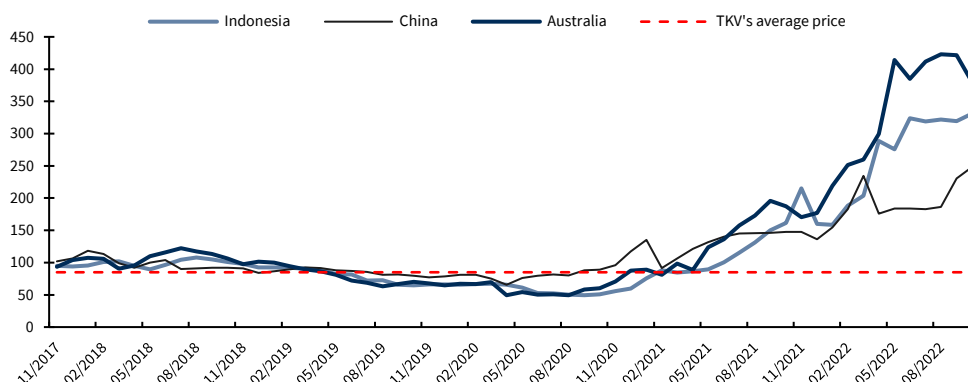
Source: Nhon Trach 2, KB Securities Vietnam

Fig 4. NT2 - Revenue & commercial power output (VNDbn, million kWh)



Source: Nhon Trach 2, KB Securities Vietnam

Fig 5. Vietnam - Imported and domestic coal prices (USD/ton)



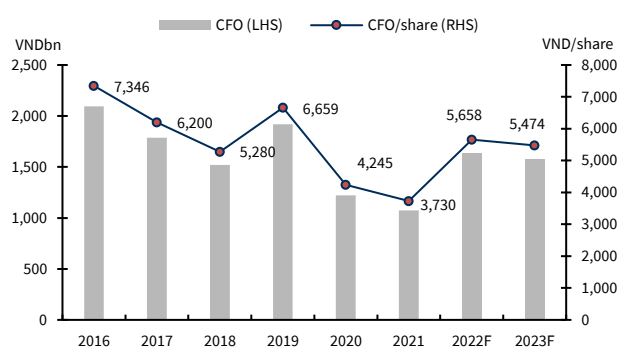
Source: Bloomberg, Vinacomin, KB Securities Vietnam

NT2 is a defensive stock with attractive dividends and is not affected by exchange rate volatility

We believe that NT2's business results will not be heavily affected by fluctuations in the exchange rate and interest rates like other peers, considering its strong operating cash flow thanks to the bounce of business performance, no long-term liabilities, and only short-term debt to ensure working capital. The firm, therefore, will potentially raise its dividends to VND2,500/share for 2022 and VND3,000/share for 2023.

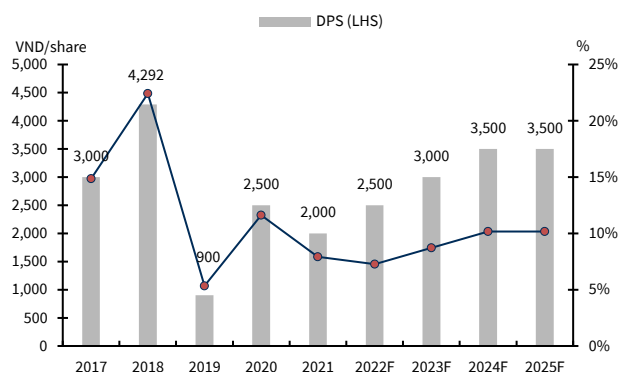
Meanwhile, PV Power (POW), NT2's parent company, is developing LNG (liquefied natural gas) power projects Nhon Trach 3 and Nhon Trach 4 with a total investment of over VND30,000 billion in the 2022-2024 period. As a result, it is very likely that NT2 will increase its dividend payout ratio to help POW finance the two projects. Given its closing price of VND25,400/share on October 28, 2022, a dividend yield of 9.8%, and robust growth throughout the year, NT2 is a good defensive stock to invest in a volatile stock market.

Fig 6. NT2 – Operating cash flow (VNDbn)



Source: Nhon Trach 2, KB Securities Vietnam

Fig 7. NT2 – Dividend payment (VND/share)



Source: Nhon Trach 2, KB Securities Vietnam

Forecast & Valuation

In 2022F, revenue and NPAT should increase sharply by 54% YoY and 94% YoY respectively

We estimate NT2's NPAT and revenue at VND1,034 billion (+94% YoY) and VND9,439 billion (+54% YoY) respectively based on the following assumptions:

- Commercial power output is 4,217 million kWh (+32% YoY) thanks to rising demand for economic growth and the low base of 2021.
- The average price of natural gas is USD9.92/MMBTU (+24.5% YoY) due to a sharp rise in world prices.
- The electricity price in the competitive generation market (CGM) averages VND1,500/kWh on higher mobilization from gas and coal-fired power with high input costs.
- NT2 records VND340 billion in compensation for exchange rate losses in 3Q22.
- NT2 sets aside VND187 billion for EVN's bad debt.

In 2023F, revenue and NPAT may decrease by 4% YoY and 14% YoY respectively

We estimate NT2's NPAT and revenue at VND889 billion (-14% YoY) and VND9,045 billion (-4% YoY) respectively based on the following assumptions:

- Commercial power output should be 4,309 million kWh (+2% YoY) thanks to growing consumption and increased mobilization of gas-fired power.
- The average price of natural gas is USD9.62/MMBTU (-3% YoY) thanks to cooling oil prices.
- The electricity price in the CGM averages VND1,575/kWh (+7% YoY) as more thermal power will be mobilized rather than hydropower.
- NT2 records about VND80 billion in compensation for exchange rate losses in 2023.

Table 2. NT2 – 2022F business results

VND bn	2021	2022	YoY %	Notes
Output (mil. kWh)	3,195	4,217	32.0%	
Contractual output (Qc)	3,195	3,669	14.8%	Qc output recovers on A0's allocation to cover the shortfall from coal-fired power and recover from the low base of 2021.
Output sold on the CGM (Qm)	0	548	N/A	The prices on CGM are more convenient for NT2's bidding on CGM market.
Average gas price (USD/MMBTU)	7.89	9.92	25.7%	Gas prices increase due to the strong increase of Brent oil price and the establishment of a new high.
Average selling price (VND/kWh)	1,925	2,130	10.7%	The average selling price increased due to the increase in gas price, which increased the average selling price of PPA and average CGM price.
Revenue (billion VND)	6,150	9,439	53.5%	
Gross profit	676	1,363	101.7%	
GPM (%)	10.99%	14.44%		GPM increased as CGM price remained high and NT2 booked exchange rate compensation in 3Q2022.
SG&A	(83.0)	(269.0)		Including VND187 billion provision for bad debt from EVN.
% SG&A / Revenue	-1.35%	-2.85%		
Profit from operating activities	593	1,094		
Financial income	18	30		
Financial expenses	-52	-19	-63.5%	Financial expenses were significantly reduced thanks to NT2 repaying long-term debts in 2Q2021.
Other net income	7	7		
Profit before taxes	566	1,097	93.9%	
Profit after taxes	534	1,034	93.7%	
NPM (%)	8.68%	10.95%		

Source: Nhon Trach 2, KB Securities Vietnam

Valuation

We recommend BUY for NT2 stocks with a target price of VND33,900/share

Based on two valuation methods, FCFF (free cash flow to firm) and EV/EBITDA (enterprise-value-to-EBITDA) with a ratio of 50:50, we reiterate our BUY recommendation for NT2 stocks. The target price is VND33,900 apiece, equivalent to a total return of 33.5% against the closing price of VND25,400/share on October 31, 2022.

Table 3. NT2 – DCF valuation

K_E	13.60%	PV of Terminal Value	8,935
Risk-free rate	5.00%	PV of Free Cash Flows	0
Equity risk premium	7.80%	Total value of FCF and TV	8,935
Beta	1.1	Plus: Cash & ST investments	746
Cost of debt	7.00%	Less: Debt	-192
Corporate tax rate %	5.0-20.0%	Less: Minority Interest	0
WACC	12.7%-13.6%	Equity Value	9,489
Terminal growth rate	0.00%	No. of shares outstanding (mn shares)	287.90
		Value per share (VND)	32,959

Source: KB Securities Vietnam

Table 4. NT2 – Target price based on FCFF and EV/EBITDA (VND/share)

Valuation method	Forecast price	Weight	Weighted price
FCFF	32,959	50%	16,480
EV/EBITDA (5.5x)	34,859	50%	17,430
Target price (rounded)			33,900
Current price (Oct 31, 2022)			25,400
Upside			33.5%

Source: KB Securities Vietnam

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Investment Ratings for Stocks

(based on expectations for absolute price gains over the next 6 months)

Buy:	Hold:	Sell:
+15% or more	+15% to -15%	-15% or more

Investment Ratings for Sectors

(based on expectations for absolute price gains over the next 6 months)

Positive:	Neutral:	Negative:
Outperform the market	Perform in line with the market	Underperform the market

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