

Hoa Phat Group (HPG)

Waiting for recovery signs from real estate

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4Q22 net revenue fell 42% while NPAT recorded the second consecutive quarter of loss

Hoa Phat Group (HPG) announced a 4Q22 loss of VND1,992 billion (-127% YoY) on revenue of VND25,826 billion (-42% YoY). Consumed steel volume declined 31% YoY to 1,756,000 tons amid real estate businesses' liquidity difficulties. Full year NPAT is VND8,444 billion (-76% YoY) and revenue reached VND141,409 billion (-6% YoY). In 4Q22, HPG recorded VND970 billion in financial revenue thanks to the recovery of VND/USD exchange rate in the last months of the year.

HPG proactively restructures working capital, optimizes cash flow to prepare for immediate difficulties

HPG's 4Q operating cash flow reached VND5,440 billion thanks to reducing inventory and recovering short-term receivables, thereby improving working capital to VND7,506 billion (+107% QoQ). Reduced short-term and long-term debt (-12% QoQ) helped reduce interest expenses in 2023. Given the shutdown of four out of seven blast furnaces in Hai Duong and Dung Quat 1, HPG aims to optimize production costs and improve profit margins.

Input material prices continue to rise in 2M23

Iron ore and coke prices have gained 23% and 15% respectively since the beginning of 4Q22 while the prices of steel have climbed by a mere of 8% due to the decline in domestic demand, causing HPG's profit margin to decline sharply (4Q GPM was -3%, compared to 21% in the same period of 2021).

HOLD recommendation with the target price of VND23,700/share

We estimate HPG's 2023 revenue and NPAT at VND126,770 billion (-10% YoY) and VND3,799 billion (-55% YoY). Combining two valuation methods P/E and EV/EBITDA, we determine the target price of HPG at VND23,700/share.

Hold update

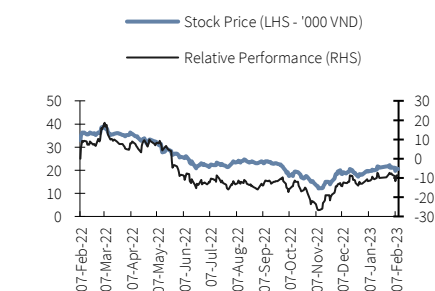
Target price	23,700
Upside	15%
Current price (Feb 16, 2023)	20,800
Market cap (VNDtn/USDbn)	120,948/5.15

Trading data	
Free float	55%
3M avg trading value (VNDbn/USDmn)	613/26
Foreign ownership	22%

Share price performance				
(%)	1M	3M	6M	12M
Absolute	4	69	-14	-38
Relative	3	58	2	-9

Forecast earnings & valuation

FY-end	2021A	2022A	2023F	2024F
Net sales (VNDbn)	149,680	141,409	126,770	133,430
Earnings (VNDbn)	37,008	9,794	4,470	14,735
NPAT (VNDbn)	34,521	8,444	3,799	12,515
EPS (VND)	7,166	1,459	653	2,154
EPS growth (%)	163%	-80%	-55%	230%
P/E (x)	2.03	13.8	7	7
P/B (x)	2.5	1.2	1.2	1.1
ROE (%)	46%	9%	4%	12%
Dividend yield (%)	5%	0%	0%	0%



Source: Bloomberg, KB Securities Vietnam

Business operation

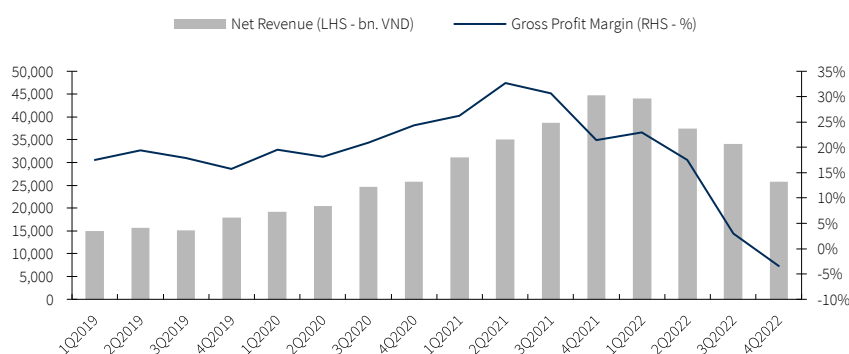
HPG recorded a loss of VND1,992 billion (-127% YoY) in 4Q and NPAT of VND 8,444 billion (-76% YoY) in 2022

HPG recorded revenue of VND25,826 billion (-42% YoY) with a GPM of -3% in 4Q22 (compared to 21% in 4Q21). The relevant figures for the whole year of 2022 are VND141.409 billion (-6% YoY) and 12% (vs 27% in 2021).

The sharp drop in business performance in the late 2022 period reflected the challenges of the steel industry in general: (1) The consumption demand from real estate and construction businesses was strongly affected by interest rates and the corporate bond market. (2) The prices of input materials such as iron ore and coke rose again when China expected to reopen its economy and normalize economic activities, causing profit margins to decline.

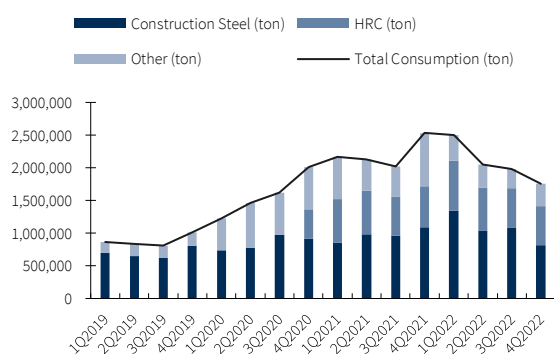
As a result, HPG continued to record an additional loss of VND1,992 billion in 4Q, making the group's 2022 accumulated NPAT only reach VND8,444 billion (-76% YoY), equivalent to a 6% NPAT margin.

Fig 1. HPG – Revenue & profit margin (VNDbn, %)



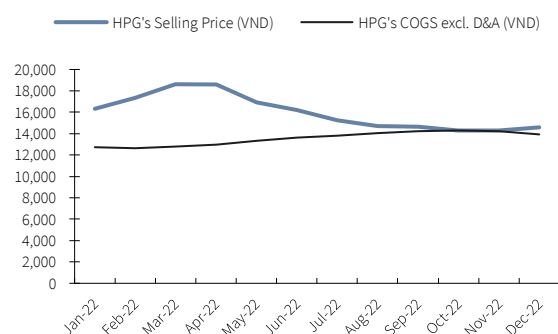
Source: Hoa Phat Group, KB Securities Vietnam

Fig 2. HPG – Sold steel volume by quarter (ton)



Source: Hoa Phat Group, KB Securities Vietnam

Fig 3. HPG – Construction steel prices and costs (VND)

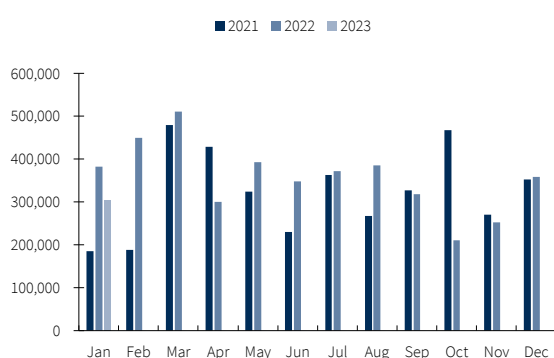


Source: Hoa Phat Group, KB Securities Vietnam

Consumption volume dropped sharply in 1H23

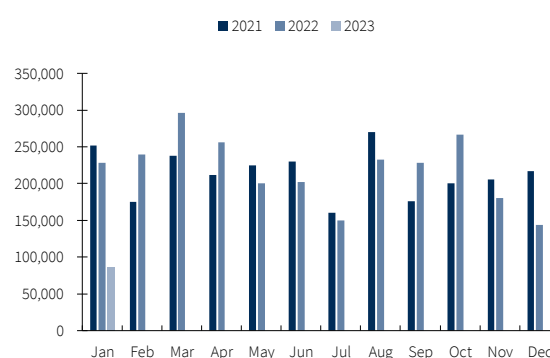
HPG's sold steel volume reached 1,756,000 tons in 4Q22 (-31% YoY). For the main products such as steel bars and coils, HRC consumed 820,000 tons (-14% YoY) and 591,000 tons (-2% YoY) respectively. The decline showed no sign of slowing down in January 2023 when the total sales volume reached 477,000 tons (-34% YoY), of which steel bars, coils and HRC decreased by 35% and 57% respectively over the same period. Although the subdued performance was also attributable to the Tet holiday shutdown, we are afraid that this downward trend may last until the end of 2Q23 when the main consumers from real estate market start to recover.

Fig 4. HPG – Sold construction steel volume (ton)



Source: Hoa Phat Group, KB Securities Vietnam

Fig 5. HPG – Sold HRC volume (ton)



Source: Hoa Phat Group, KB Securities Vietnam

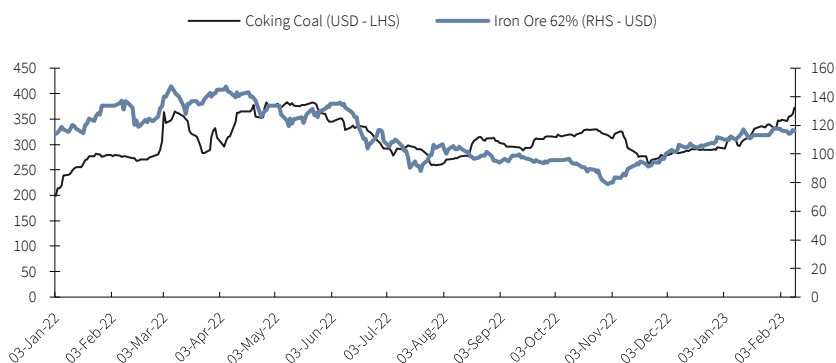
The prices of input materials continue to increase, which will narrow the GPM

China's eased COVID-19 protocols raise expectations of a recovery in the international market, which has triggered rallies in iron ore and coke prices (up by 23% and 15% respectively) since 4Q22.

KBSV believes the uptrend of input material prices will last until the end of 2Q23 because: (1) The mining of coke in Australia is affected by floods, which delays the deliveries to the US and EU. (2) Manufacturers are taking a cautious attitude in importing materials when spot prices are high. (3) Therefore, steel consumption in the market will also be limited as foreign contractors are cautious in importing, slowing down the recovery of the steel market.

In terms of output, HPG's construction steel has had two price increases since the beginning of 2023 (from VND14,900/kg to VND15,450 /kg and then VND15,750/kg. HPG has to adjust the prices to ensure the its GPM amid rising material costs. According to our estimates, the prices of steel products have gained by 6% YTD, while the prices of raw materials (ores, coke and scrap iron) have increased by 14% on average.

Fig 6. Global – Iron ore & coke prices (USD)



Source: Hoa Phat Group, KB Securities Vietnam

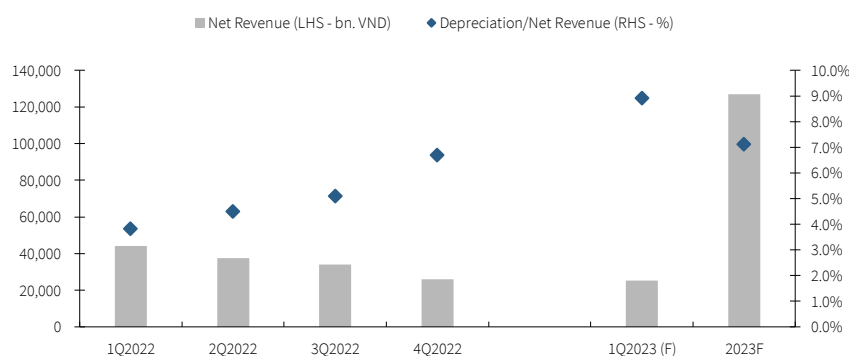
Dung Quat 2 project continues to be implemented on schedule

HPG said that the implementation of Dung Quat 2 project is still on schedule. However, for the time being, with the shutdown of four out of seven blast furnaces in Hai Duong and Dung Quat 1, HPG's business results will be affected by the depreciation of the above plants and limited sales volume and GPM.

We assume that HPG will continue to invest in Dung Quat 2 as originally planned, hence the estimated depreciation value for 2023F and 2024F at VND8,994 billion (+32% YoY) and VND11,173 billion (+24% YoY) respectively.

To reach the above goal, HPG should focus on optimizing working capital in 2023 to ensure the progress of Dung Quat 2 project and to adapt to market conditions (low sales volume, high costs and inventory, and limited cost of goods sold).

Fig 7. HPG – Revenue & depreciation to fixed assets ratio (VNDbn, %)



Source: Hoa Phat Group, KB Securities Vietnam

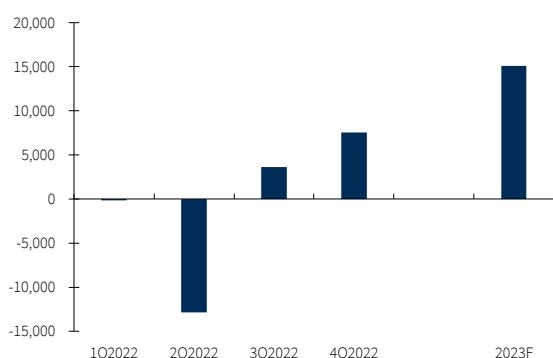
HPG actively optimized working capital and debt structure, ensuring cash flow

With the suspension of four out of seven blast furnaces in Hai Duong and Dung Quat 1 in 4Q2022, HPG has focused on structuring and optimizing working capital to ensure business cash flow. 4Q working capital reached VND7,506 billion (+107% compared to 3Q22).

As a result, HPG actively reduced 4Q22 debt to VND57,900 billion (29% in USD and 71% in VND). However, according to our assessment, in case the policy rate gains 100–200 bps in 2023, HPG may face the risk of interest expense increasing by VND659–1.355 billion (the ratio of interest expense to revenue up 1.33–1.88%).

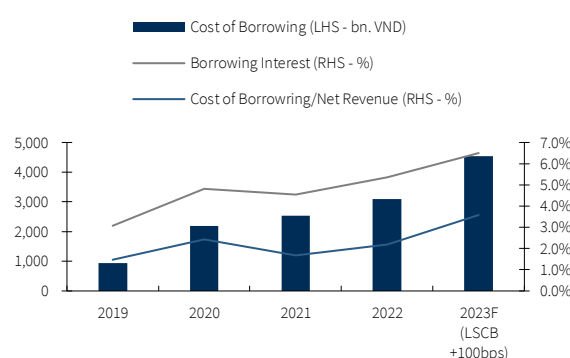
We believe that HPG's debt will increase in 2023 and 2024 due to high capital demand for investment in Dung Quat 2 project, however HPG should focus on the proportion structure between short-term and long-term loans to optimize interest expenses (estimated at 6.5%, up 1.2% compared to 2022) in the context of a high interest rate environment.

Fig 8. HPG – Changes in Working Capital



Source: Hoa Phat Group, KB Securities Vietnam

Fig 9. HPG – Impact of interest on cost of borrowing

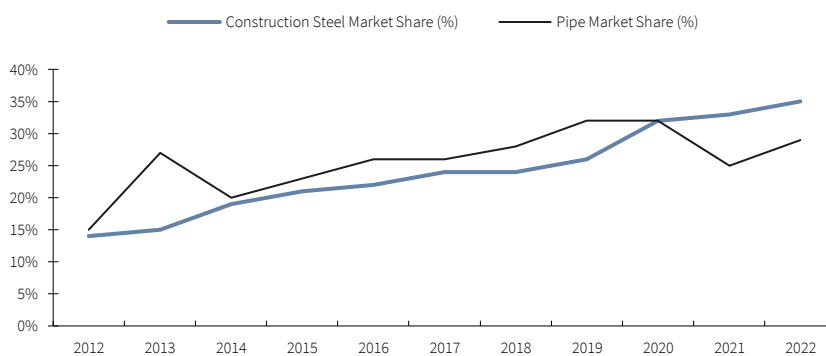


Source: Hoa Phat Group, KB Securities Vietnam

HPG expects to gain market share after short-term difficulties

By the end of 2022, HPG’s market shares of construction steel and steel pipe were 35% and 29% respectively, compared to 33% and 25% in 2021. Given the general difficulties of steel industry enterprises, along with the prospect of the project Dung Quat 2, we think HPG will be able to take advantage of its leading position to increase its market share in production and distribution in the long term.

Fig 10. HPG – Construction steel and steel pipe market share (%)



Source: Hoa Phat Group, KB Securities Vietnam

Forecast & valuation

Steel consumption expects for more recovery signs from the real estate and construction market

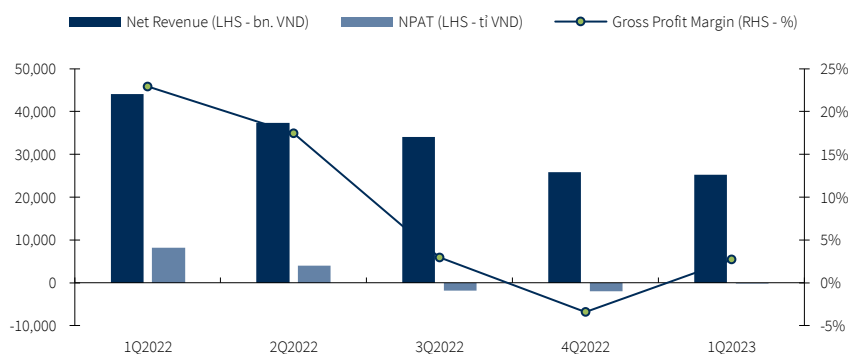
We forecast HPG's sales volume in 1Q23 will reach 1,453,750 tons (-42% YoY) and improve from 2Q, assuming real estate market support mechanisms are approved and business activities enterprises become busier. However, in the conservative case, we think HPG's blast furnaces will return to 100% capacity from 4Q23 before a blast furnace back comes in operation in 2Q.

HPG may record a loss of VND130 billion in 1Q23 (-102% YoY)

Given the current difficulties, we forecast HPG's sales volume in 1Q23 would reach 1,453,750 tons (-42% YoY), of which bar and HRC output will be 796,250 tons and 412,500 tons, respectively. 1Q revenue should be VND24,588 billion (-44% YoY) billion with low profit margin (3% compared to 23% in the same period last year). NPAT may be -VND130 billion VND (-102% YoY) thanks to the reversal of provision for devaluation of inventories as 1Q23 raw material prices rebounds to 2Q-3Q22 levels.

For the whole year of 2023, KBSV forecasts HPG's revenue would reach VND126,770 billion (-10% YoY) with total sales volume of 6,947,500 tons (-16% YoY). NPAT is estimated at VND3,799 billion (-55% YoY).

Fig 12. HPG – Forecast revenue, NPAT & GPM (VNDbn, VNDbn, %)

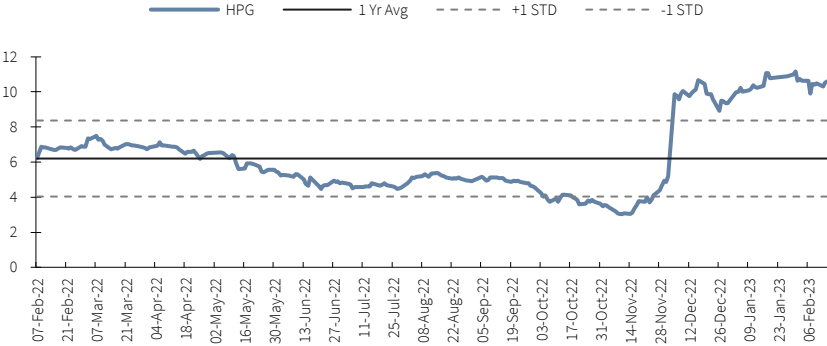


Source: Hoa Phat Group, KB Securities Vietnam

HOLD recommendation for HPG shares, target price: VND23,700 apiece

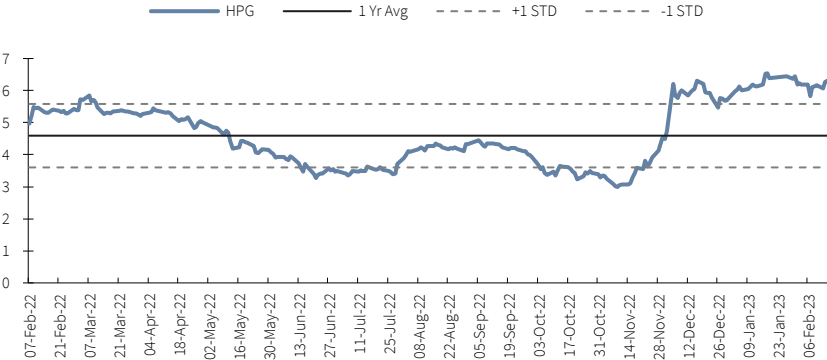
Combining two valuation methods P/E and EV/EBITDA with reasonable valuation of 7x and 4.5x respectively, we recommend HOLD for HPG stocks with the target price of VND23,700 /share (equivalent to an upside of 15%).

Fig 12. HPG - P/E (x)



Source: Hoa Phat Group, KB Securities Vietnam

Fig 13. HPG - EV/EBITDA



Source: Hoa Phat Group, KB Securities Vietnam

HPG – 2023–2024F financials

Income Statement (bn. VND)	2021	2022	2023F	2024F
(Standard Report)				
Net Revenue	149,680	141,409	126,770	133,430
Cost of Goods Sold	-108,571	-124,646	-117,131	-114,120
Gross Profit	41,108	16,763	9,640	19,310
Financial Income	3,071	3,744	3,806	5,074
Financial Expenditure	-3,732	-7,027	-4,539	-5,647
Including: Cost of Borrowing	-2,526	-3,084	-4,539	-5,647
Profit/(loss) from affiliated companies	4	-1	0	0
Selling expenditures	-2,120	-2,666	-2,958	-2,669
General and administrative expenditures	-1,324	-1,019	-1,479	-1,334
Profit/(loss) from operating	37,008	9,794	4,470	14,735
Other income	797	872	0	0
Other expenditures	-748	-743	0	0
Net Other Income	48	129	0	0
Profit/(loss) from affiliated companies	0	0	0	0
Profit/(loss) before tax	37,057	9,923	4,470	14,735
Tax	-2,536	-1,479	-670	-2,210
Profit/(loss) after tax	34,521	8,444	3,799	12,525

Operating Ratios	2021	2022	2023F	2024F
Gross Profit Margin	27.5%	11.9%	7.6%	14.5%
EBITDA Margin	30.5%	13.9%	14.2%	23.6%
EBIT Margin	26.4%	9.1%	7.1%	15.3%
PBT Margin	24.8%	7.0%	3.5%	11.0%
Operating Profit Margin	24.7%	6.9%	3.5%	11.0%
Net Profit Margin	23.1%	6.0%	3.0%	9.4%

Cash Flow Statement (Standard Report)	2021	2022	2023F	2024F
PBT	37,057	9,923	4,470	14,735
Depreciation	6,077	6,814	8,994	11,173
Profit/(loss) from investing	-1,661	-1,822	0	0
Cost of borrowing	2,526	3,084	4,539	5,647
Profit/(loss) before changes in WC	44,209	19,199	18,002	31,555
(Increase)/decrease in receivables	-3,039	4,723	2,038	-302
(Increase)/decrease in inventory	-16,949	8,022	4,801	-5,831
Increase/(decrease) in payables	9,250	-14,681	8,240	-4,458
(Increase)/decrease in pre-paid expenses	-814	-19	0	0
Sellable securities, cost of borrowing, tax	0	0	0	0
Operating Cash Flow	26,721	12,192	28,954	11,223
Purchases of fixed assets and other long term	-11,621	-17,966	-27,700	-28,333
Proceeds from disposal of fixed assets	49	14	0	0
Loans granted, purchases of debt instruments	-41,061	-55,506	0	0
Collection of loans, proceeds from sales of debt	31,076	47,413	0	0
Investments in other entities	0	-372	0	0
Proceeds from divestment in other entities	834	0	0	0
Dividends and interest received	1,054	1,706	0	0
Investing Cash Flow	-19,669	-24,712	-27,700	-28,333
Proceeds from issue of shares	11	4	0	0
Payments for share returns and repurchases	0	0	0	0
Proceeds from borrowings	125,075	135,257	159,103	169,350
Repayment of borrowings	-121,653	-134,631	-135,257	-159,103
Finance lease principal payments	0	0	0	0
Dividends paid	-1,693	-2,247	0	0
Interests, dividends, profits received	0	0	0	0
Financing Cash Flow	8,792	-14,137	25,101	-6,862
Net increase in cash and cash equivalents	13,696	22,471	8,325	33,426
Cash and cash equivalents at the beginning of period	-16	-10	0	0
Cash and cash equivalents at the end of period	22,471	8,325	33,426	26,563

Source: Hoa Phat Group, KB Securities Vietnam

Balance Sheet (bn. VND)	2021	2022	2023F	2024F
(Standard Report)				
TỔNG CỘNG TÀI SẢN	178,236	170,336	207,303	223,734
CURRENT ASSETS	94,155	80,515	98,777	98,047
Cash and cash equivalents	22,471	8,325	33,426	26,563
Short-term investments	18,236	26,268	26,268	26,268
Accounts receivable	7,663	9,893	7,855	8,157
Inventories	42,134	34,491	29,690	35,521
LONG-TERM ASSETS	84,082	89,821	108,526	125,686
Long-term trade receivables	809	894	894	894
Fixed assets	69,281	70,833	89,539	106,699
Long-term incomplete assets	9,699	13,363	13,363	13,363
Long-term investments	7	1	1	1
Good will (before 2015)	0	0	0	0
NỢ PHẢI TRẢ	87,456	74,223	107,391	111,297
Current liabilities	73,459	62,385	57,657	60,014
Trade accounts payable	23,729	11,107	19,347	14,889
Short-term borrowings	43,748	46,749	32,699	41,397
Other short-term liabilities	5,983	4,530	5,612	3,728
Long-term liabilities	13,996	11,837	49,733	51,282
Long-term trade payables	0	0	0	0
Other long-term liabilities	532	686	686	686
Long-term borrowings	13,465	11,152	49,048	50,597
OWNER'S EQUITY	90,781	96,113	99,912	112,437
Paid-in capital	44,729	58,148	58,148	58,148
Share premium	3,212	3,212	3,212	3,212
Other funds	1,076	920	920	920
Undistributed earnings	41,763	33,834	37,633	50,158

Main Ratios (x, %, VND)	2021	2022	2023F	2024F
Valuation Ratios				
P/E	6.6	13.8	31.8	9.7
P/E (diluted)	6.6	13.8	31.8	9.7
P/B	2.5	1.2	1.2	1.1
P/S	1.5	0.8	1.0	0.9
P/Tangible Book	3.1	1.7	1.7	1.7
P/Cash Flow	8.3	9.6	42.8	108.3
EV/EBITDA	6.0	8.4	7.9	5.1
EV/EBIT	6.3	13.0	18.8	9.1
Management Efficiency				
ROE%	46%	9%	4%	12%
ROA%	22%	5%	2%	6%
ROIC%	25%	8%	2%	6%
Financial Ratios				
Cash Ratio	0.3	0.1	0.6	0.4
Quick Ratio	0.7	0.7	1.2	1.0
Current Ratio	1.3	1.3	1.7	1.6
Long-term borrowing/Owner's Equity	0.1	0.1	0.5	0.5
Long-term borrowing/Total Asset	0.1	0.1	0.2	0.2
Short-term borrowing/Owner's Equity	0.5	0.5	0.3	0.4
Short-term borrowing/Total Asset	0.2	0.3	0.2	0.2
Short-term payables/Owner's Equity	0.3	0.1	0.2	0.1
Short-term payables/Total Asset	0.1	0.1	0.1	0.1
Total payables/Owner's Equity	0.3	0.1	0.2	0.1
Total payables/Total Asset	0.1	0.1	0.1	0.1
Operating Ratios				
Receivables turnover	33.6	35.7	35.7	30.4
Inventory turnover	3.2	3.3	3.7	3.5
Payables turnover	7.2	6.7	7.7	6.7

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(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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