

August 12, 2021

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2Q performance hit a record high

Hoa Phat Group (HPG) posted VND9,745 billion (+253% YoY) in earnings on revenue of VND35,118 billion (+72% YoY) in 2Q. Sold construction steel volume reached 982,000 tons (+25.8% YoY) and hot rolled coil (HRC) was 667,000 tons.

Limited steel supply due to Chinese production cut may benefit HPG

China Government required its steel makers not to exceed the steel output in 2020 as a measure to limit carbon emission. This may indirectly benefit steel companies in other countries, including HPG.

Public construction projects will boost steel consumption in the second half of the year

The impacts of the Coronavirus pandemic and the 'low season' in the early months of the rainy season affected the sales of HPG's products. However, public investment which is an important driver to the economy after the pandemic should be an incentive for HPG's construction materials in the 'high season' for construction in the last months of the year.

HRC is the driving force for 2H2021

We expect HPG's HRC consumption to reach 35% of crude steel output in 2H21 given two blast furnaces operating at maximum capacity, which is the driving force for the company's business performance.

2021 profit should grow 144%, hence BUY recommendation

We estimate HPG's 2021 earnings at VND32,927 billion (+144% YoY) on revenue of VND147,039 billion (+63.2% YoY). The target price is revised up to VND64,700 a piece with a BUY recommendation, upside 32.5%.

Buy maintain

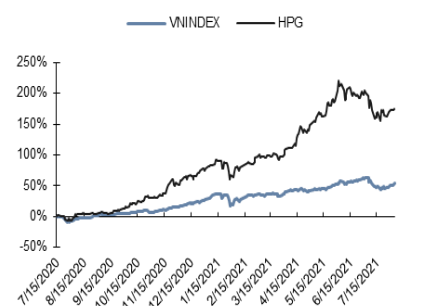
Target price	VND64,700
Upside/downside	32,5%
Current price (Aug 5, 2021)	VND48,800
Consensus target price	N/A
Market cap (VNDbn)	211/9,17

Trading data	
Free float (%)	55%
Avg trading value (3M) (VND bn/ USD mn)	1.639/71
Foreign ownership (%)	26.67%

Share price performance				
(%)	1M	3M	6M	12M
HPG	-7%	7%	53%	179%
VN-Index	-5%	7%	20%	61%

Forecast earnings & valuation

FY-end	2019A	2020A	2021F	2022F
Revenue (VNDbn)	63,658	90,119	147,039	160,071
EBIT (VNDbn)	9,031	15,289	36,519	40,896
Post-tax earnings (VNDbn)	7,578	13,506	32,926	36,865
EPS (VND thousand)	2,74	4,07	7,36	8,24
EPS growth (%)	-32%	49%	81%	12%
P/E (x)	17.31	11.65	6.45	5.76
P/B (x)	27.45	26.58	23.48	16.98
ROE (%)	16%	23%	36%	29%
Dividend yield (%)	1.6%	5%	5%	5%



Business operations

2Q profit and revenue went up 253.7% YoY and 72% YoY

2Q earnings were VND9,745 billion (+253.7% YoY), and gross profit margin was reached 32.7% (+6.5% QoQ, +18.1% YoY). The record high gross profit margin was attributable to a surge in steel prices in the quarter (+15% QoQ).

HRC is a key incentive in 2H21

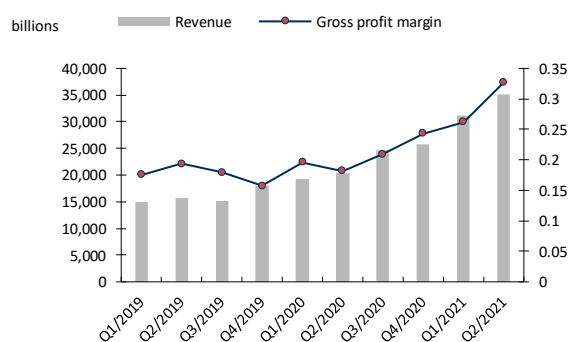
Domestic HRC consumption is estimated at 12 million tons this year and may grow 10% annually. In 2H20, HRC steel consumption only accounted for 20% of HPG's crude steel output, but in 2H2021, we expect it to hit 35% given two blast furnaces running at their maximum capacity and high demand for construction materials in the last months of the year.

Table 1. HPG – 2Q performance YoY

	2Q20	2Q21	Change	Market share
Steel consumption				
Construction steel	780.500	982.000	25,8%	35,3%
Steel pipe	202.200	191.000	-5,5%	30,1%
Revenue from steel	18.055	32,492	80%	
Revenue from agriculture	2.263	2.368	4,6%	
Net profit	2.755	9.745	253,7%	

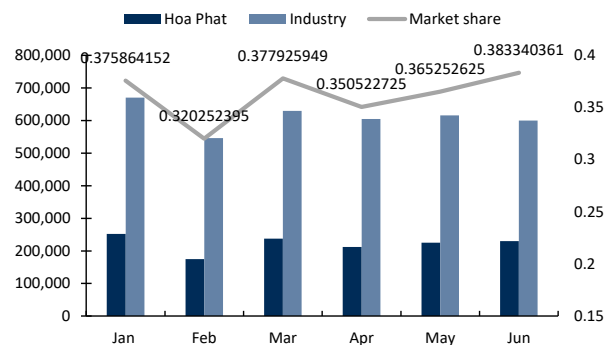
Source: Hoa Phat Group, KB Securities Vietnam

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



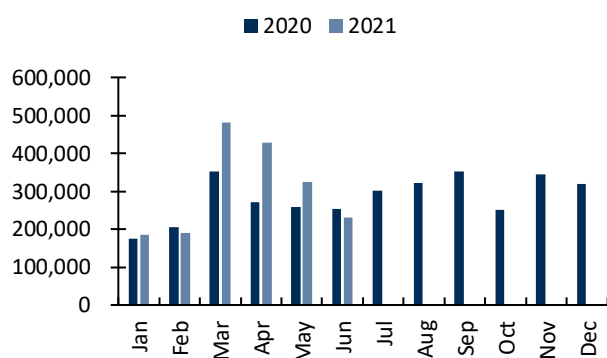
Source: Hoa Phat Group, KB Securities Vietnam

Fig 2. HPG – Consumed HRC volume (ton)



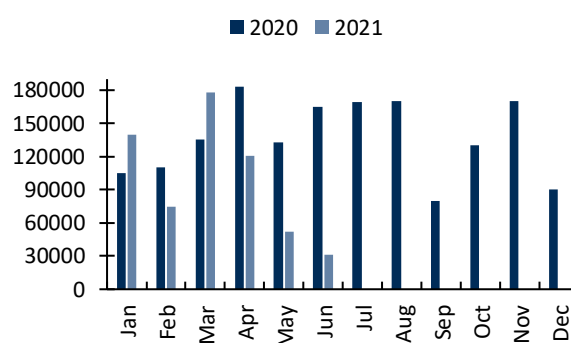
Source: Hoa Phat Group, KB Securities Vietnam

Fig 3. HPG – Consumed construction steel volume (ton)



Source: Hoa Phat Group, KB Securities Vietnam

Fig 4. HPG – Consumed still billets (ton)



Source: Hoa Phat Group, KB Securities Vietnam

Steel supply is limited due to China's efforts to cut carbon emissions to the environment

Chinese Government is exerting its utmost efforts to control its construction materials manufacturing to meet the carbon-cutting target. Chinese lawmakers require steel mills to ensure that their steel output is not higher than that of the full year 2020 (1,054 million tons). China made 560 million tons of steel (+11.5% YoY) in 1H21, so 2H21 crude steel output should decrease 10.4% YoY to meet the carbon-limit requirement.

The demand for iron ore decreases due to production restrictions, leading to a downtrend in ore prices

The above movement of China will lead to a decrease in the demand for iron ore, so the prices of ore may tend to go down. Besides, iron ore inventories at China's ports should gradually increase to serve the production in 2H21. The world's largest iron ore exporters like Australia and Brazil would also raise ore output significantly, partly making ore prices lower.

China officially removed export tax refunds

On July 29, 2021, China announced to remove export tax refunds (from 13%) August 1, 2021 for 23 steel products including cold rolled coil (CRC), galvanized steel, and steel pipes. The country also raised export taxes for cast iron from 15% to 20%, and Ferro alloy from 20% to 40% from August 1. This shows the determination of the Chinese Government in increasing the quality of the steel industry instead of quantity, as well as ensuring domestic supply amid output cut to protect the environment.

Domestic consumption slows down due to the fourth wave of the pandemic, so HPG promotes steel billet exports

The consumption of HPG's key markets – Hanoi and Southern provinces slowed down due to social distancing in the fourth wave of COVID-19. Therefore, the company has increased the export of steel billets to the main market China where the steel billet prices are much higher than those in Vietnam (Figure 3).

Public investment will boost steel consumption in 2H21

The impacts of the Coronavirus pandemic and the ‘low season’ in the early months of the rainy season affected the sales of HPG’s products. However, public investment which is an important driver to the economy after the pandemic should be an incentive for HPG’s construction materials in the ‘high season’ for construction in the last months of the year. HPG is one of the suppliers for many key public investment projects such as Vinh Tuy Bridge phase 2, North-South Expressway, My Thuan 2 Bridge and Tan Son Nhat International Airport. With a market share of over 35% in construction steel, HPG will be a big beneficiary from the government's accelerated public investment projects, especially in the second half of the year.

HPG should reap benefits from low iron ore prices and increasing steel prices in 2H21

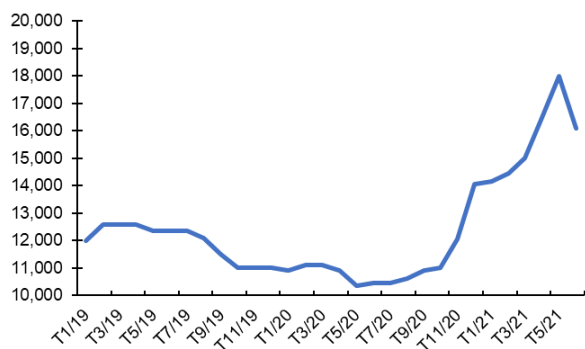
The average iron ore price increased 36% in the first half of the year, outpacing the 15% increase in steel prices. When China cuts production output in 2h21, it will put pressure on iron ore prices, thereby lowering ore prices and raising steel prices. We believe that HPG will benefit from low input ore prices, not to mention the increasing domestic demand in 2H21 and the more limited steel supply in China.

Fig 5. Vietnam & China – Construction steel billet prices (VND/kg)



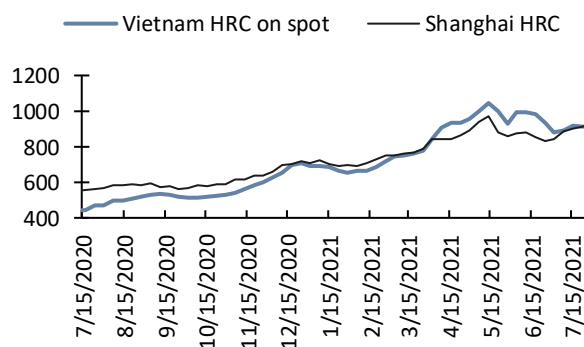
Source: Hoa Phat Group, KB Securities Vietnam

Fig 6. Vietnam – Construction steel prices (VND/kg)



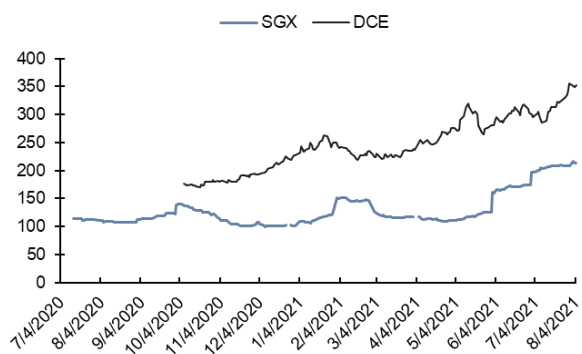
Source: VOSA Corp, KB Securities Vietnam

Fig 7. Vietnam & China – HRC prices (USD)



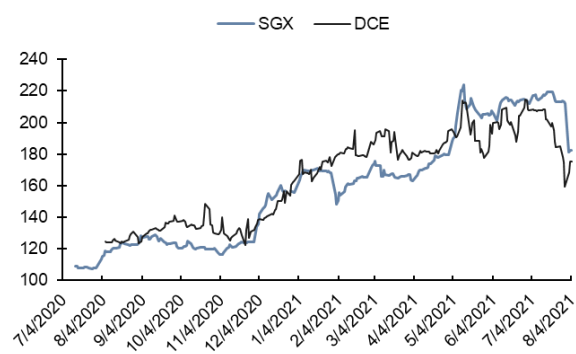
Source: Bloomberg, KB Securities Vietnam

Fig 8. Singapore & Dalian – Contract coke prices (USD)



Source: Bloomberg, KB Securities Vietnam

Fig 9. Singapore & Dalian – Contract iron ore prices (USD)



Source: Bloomberg, KB Securities Vietnam

Valuation & forecast

HPG has a positive outlook in 2021

Given the acceleration of Vietnam public construction projects and China's steel output cut, we believe HPG is the company that can gain big benefits in 2H21. We expect the company would post VND32,927 billion (+144% YoY) in earnings on revenue of VND147,039 billion (+63.2% YoY) in 2021 which are 16.6% higher and 3% lower than their respective forecasts in our previous report.

Table 2. HPG – Forecast performance

VND billion	2019A	2020A	2021F	2022F
Construction steel output (tons)	2,773,108	3,400,000	3,388,667	4,000,000
HRC output (tons)	0	681,000	2,652,000	2,400,000
Billet output (tons)	0	1,640,000	1,487,000	1,200,000
Net revenue	63.658	90.119	147.039	160.071
Growth (%)	14%	41.6%	63.2%	8.9%
COGS	52.473	71.214	105.604	114.619
Gross profit	11,185	18,905	41.435	45.452
Gross profit margin (%)	17.6%	21%	28.2%	28.4%
Financial expense	1.182	2.824	3.432	3.222
Selling expense	873	1.094	1.764	1.921
General & Administrative expense	569	690	1.314	1.431
Net profit	7,578	13,506	32.927	36.865
Growth (%)	-11.9%	78.2%	144%	12%
Net profit margin (%)	11.9%	15%	22.4%	23%

Source: KB Securities Vietnam

BUY recommendation with a target price of VND64,700 per share

Based on the average of two valuation methods, we recommend to BUY HPG shares with a target price of VND64,700 apiece, 32.5% higher than the closing price on August 4, 2021:

- According to the P/E method, HPG's reasonable P/E is 10 times, equivalent to a stock price of VND73,600.
- According to the DCF method, we value HPG share at VND55,800.

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Investment ratings & definitions

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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