

VGC (HOSE)

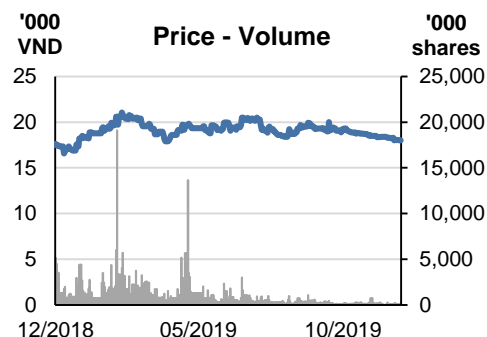
On rock solid footing for sustainable development

Rating

BUY

Properties-related

Market price (VND)	18,000
Target price (VND)	21,700
Annualized price return (%)	20.6%
Expected dividend yield (%)	5.6%
Expected total return (%)	26.2%



Stock performance (%)

	YTD	1M	3M	12M
Absolute	-2%	-2%	-7%	7%
Relative	-3%	-3%	-5%	-5%

Source: Bloomberg, compared to VNIndex

Stock Statistics

03-Jan-20

52-week range (VND)	16.9k-21.1k
Shares o/s (m)	448
Mkt cap (VND bn.)	8,070
Mkt cap (\$m)	348
% Foreign owned	13.4%
Est. free float (mn. shares)	55.2
3m avg. daily vol. (shares)	168,348
VND/USD	23,173
Index: VN-Index/HNX	965/102

Source: Bloomberg, KIS

Ownership

03-Jan-20

Ministry of Construction	53.4%
Gelex	25.0%

Source: KIS

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Investment points:

- **Building materials see solid earnings.** We expect to see the solid earnings of building materials segment in 2020 because of the stable performance of the terracotta and tile sub-segments, the profitability improvement of the glass sub-segment based on more favorable input price and the sales expansion of the sanitary ware sub-segment thanks to new factories
- **Long-term potentials of industrial park.** Regarding the current positive signals of the U.S-China trade deal and the fact that most of attractive land areas of Bac Ninh and Ha Nam province was sold in 2019, we estimate IP performance has peaked in 2019. Therefore, in the short term, we forecast a slight slowdown compared to the FY2019 apex result. However, we believe IP sector has a strong growth potential in the long-term based on a large land bank and the accelerating industrialization of Vietnam.
- **State divestment to be a long-term catalyst.** According to the Decision 1232/QD-TTg, the State will divest all VGC stake before 2020. The State divestment is a long-term catalyst for Viglacera in cost cutting, sales expansion and performance improvement.

Risks:

- **Restropective valuation at IPO.** One big problem that delays the State divestment progress is retrospective revaluation of Viglacera when it officially changed its structure to joint-stock company from a State one in 2014. The revaluation may result in an additional cost that the existing or potential shareholders have to pay to the State.

Recommendation:

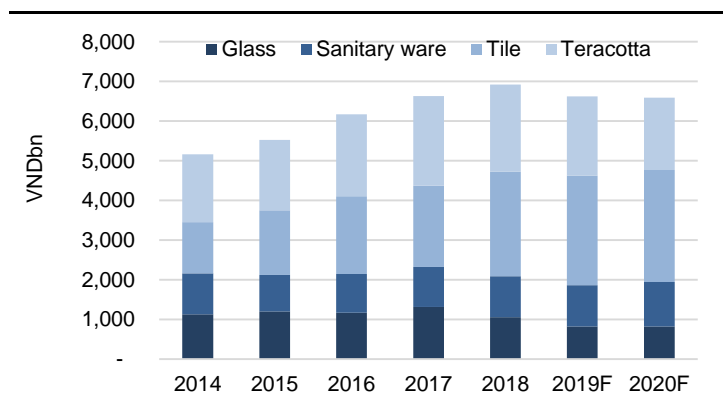
- In 2020, we estimate that the revenue and profit of Viglacera will reach VND10,026bn and VND782bn, up 1.3% YoY and -2.1% YoY. EPS will be VND1,400.
- We believe that Viglacera has a strong growth potential thanks to the inevitable industrialization and urbanization of Vietnam in the long term. Using Sum of the Parts method, we evaluate VGC share at **VND21,700** by the end of 2020. Including the VND1,000 cash dividend per share, total expected return is 26.2% at the current market price of VND18,000. Recommend **BUY**

VND bn.	2016	2017	2018	2019E	2020E
Net revenue	8,139	9,197	8,812	9,899	10,026
Growth (%)	4.1%	13.0%	-4.2%	12.3%	1.3%
Net profit	621	722	673	798	782
Growth (%)	52.7%	16.3%	-6.8%	18.6%	-2.1%
EPS (bonus-adjusted, VND)	710	1,295	1,196	1,458	1,424
Growth (%)	49.9%	82.5%	-7.7%	22.0%	-2.4%
ROE (%) (excl. minority)	10.1%	8.1%	6.6%	8.0%	7.6%
Net debt/Equity (%)	16%	-3%	4%	2%	-5%
PER (x)	26.1	14.3	15.5	12.7	13.0
PBR (x)	0.6	1.0	1.0	0.9	0.9
EV/EBITDA (x)	7.6	5.9	6.7	6.1	5.8
Dividend yield (%)	1.0%	5.1%	5.1%	5.4%	5.4%

1. Building materials see solid earnings

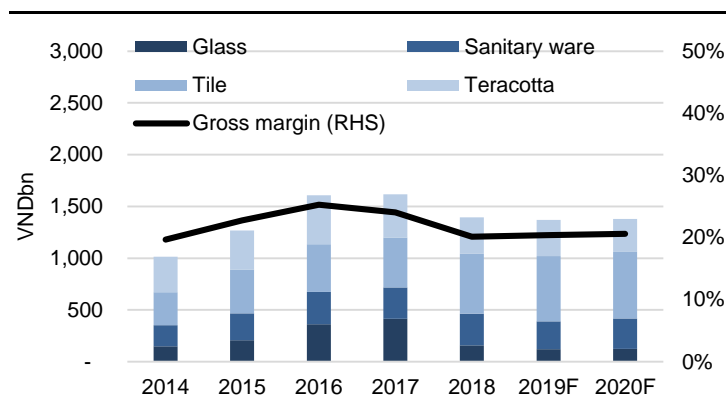
This segment includes 4 main sub-segments: terracotta, tile, glass and sanitary ware. We expect to see the solid earnings of building materials segment in 2020 because of the stable performance of the terracotta and tile sub-segments, the profitability improvement of the glass sub-segment based on more favorable input price and the sales expansion of the sanitary ware sub-segment thanks to new factories.

Fig 01. Building materials revenue breakdown



Source: VGC, KIS

Fig 02. Building materials gross profit breakdown

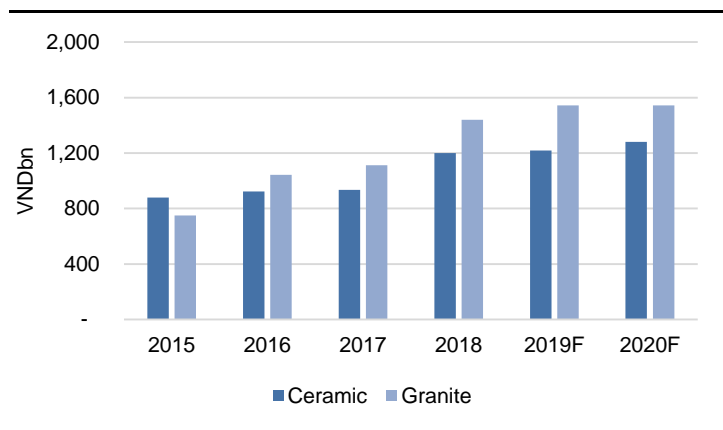


Source: VGC, KIS

1.1. Stable ceramic and granite tile

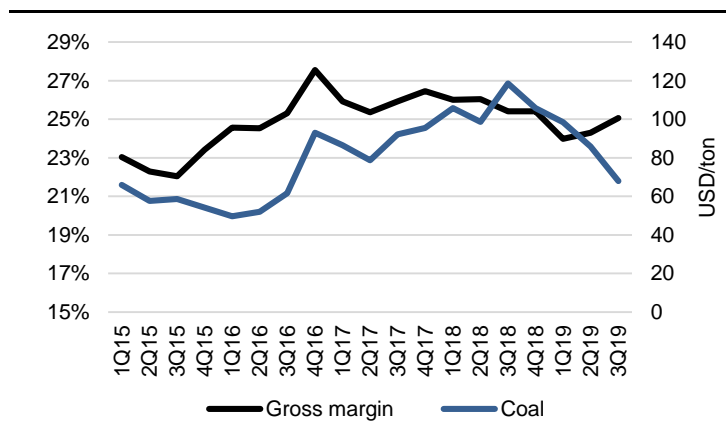
We estimate a stable performance for this segment in the following years because the company is operating at more than 100% of the designed capacity while no new factory is under construction. Therefore, higher operating efficiency and lower input prices (CNG and coal) are likely the main drivers for earnings growth in 2020. We estimate ceramic and granite tile revenue in FY2020 at VND1,280bn and 1,544bn, up +5.2% YoY and 0% YoY respectively.

Fig 03. Tile revenue breakdown by product



Source: VGC, KIS

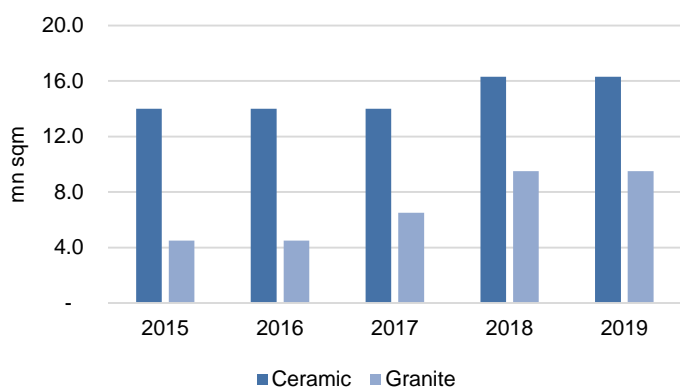
Fig 04. Coal price vs Gross margin of tile segment



Source: Bloomberg, VGC, KIS

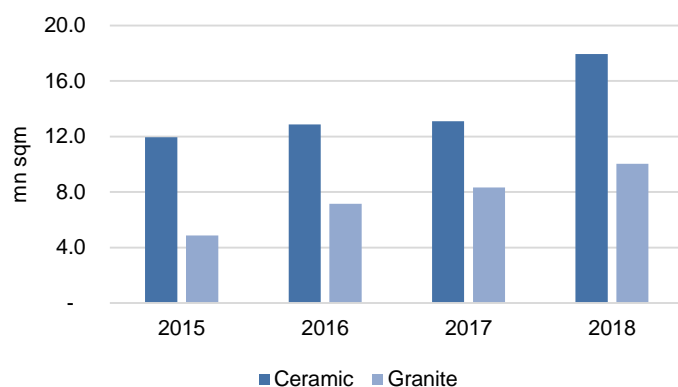
In the long-term, Viglacera has plenty of room to expand this segment by gaining market share from its rivals and expanding geographically. We estimate that Viglacera accounts for less than 4% and 8% in Vietnam ceramic and granite markets, respectively. Currently, all tile factories of Viglacera is located in the North, except My Duc 3mn sqm factory in Vung Tau. In the future, Viglacera plans to double the capacity of My Duc granite factory to 6mn sqm and invest into a 3mn sqm ceramic tile factory in Cuba.

Fig 05. Tile capacity breakdown by product



Source: VGC, KIS

Fig 06. Tile actual output breakdown by product



Source: VGC, KIS

1.2. And terracotta segment as well

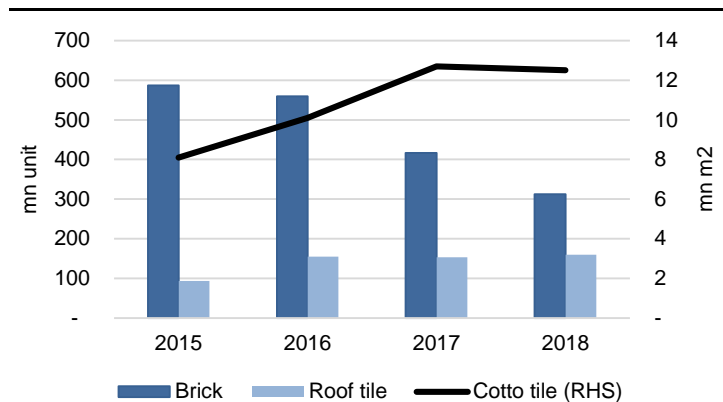
We expect a less negative impact of brick and a plateau of cotto tile in 2020.

Cotto tile, which accounts for more than 40% of terracotta revenue, has little room for growth due to capacity constraint. Currently, Viglacera is supplying around 12mn sqm per year, equivalent to more than 40% of market size.

Regarding brick, since 2015, because brick had been less profitable than the other products, the company has planned to transform all brick production lines into roof tile ones. Therefore, brick output witnessed a significant decline of around 50% from 2015 to 2019. In addition, the parent company also plans to divest inefficient brick member companies. However, the current proportion of brick in terracotta revenue is less than 10%, so that the negative impact of brick business contraction will not be significant and can be covered by the expansion of roof tile product of which current output is around 7.2mn sqm, equivalent to more than 30% of market size of tile market.

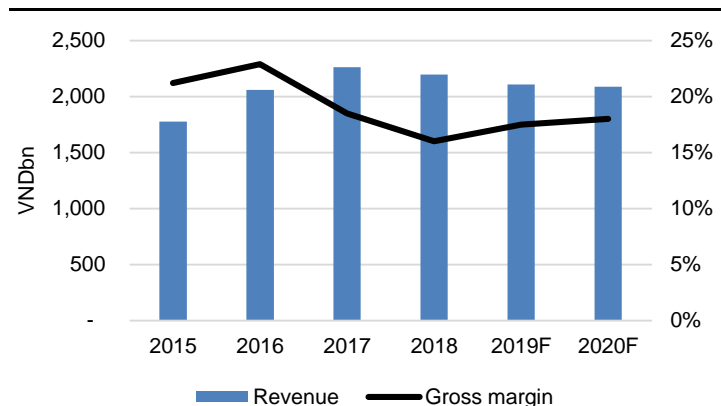
As a result, in 2020, we expect terracotta revenue will be stable at VND2,088bn while gross margin will be improved to 18% thanks to the decrease of CNG and coal price.

Fig 07. Terracotta output breakdown



Source: VGC, KIS

Fig 8. Terracotta performance



Source: VGC, KIS

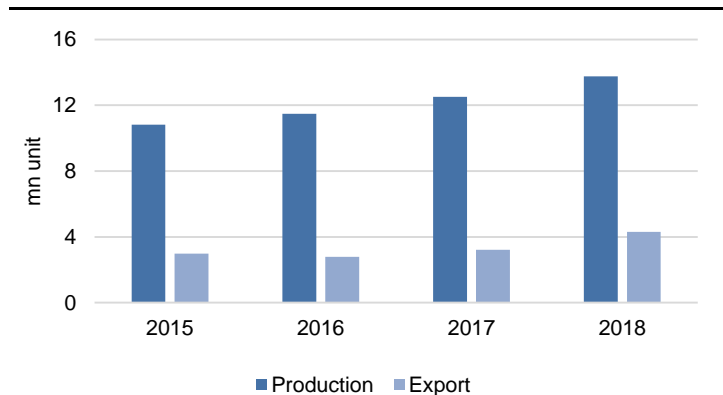
1.3. Sanitary ware poises to rise

Thanks to a new factory, we expect a higher contribution from sanitary ware segment with revenue being projected at VND1,121bn, up +8.2% YoY while gross margin likely being flat.

Viglacera is now one of the 4 biggest players in local sanitary ware market with around 10% market share. Before 2019, Viglacera had to face with capacity constraint and market expansion problems when all sanitary ware factories of Viglacera are in the North. Thanks to My Xuan factory which is located in the South, sanitary ware capacity of Viglacera increased by 60% YoY to 2mn units in 2019, solving the two above problems. We expect the utilization rate of My Xuan factory can reach above 70% in 2020.

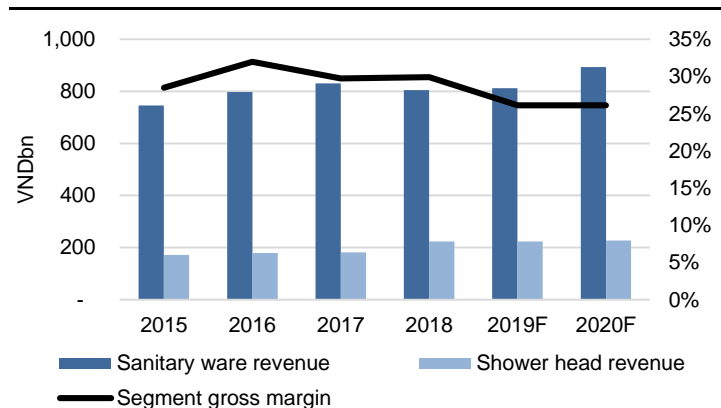
Moreover, the company has a plan to invest into a high-class 750k-unit-per-year sanitary ware factory in Phu Tho and a 154k-unit-per-year sanitary ware factory in Cuba in the following years.

Fig 09. Vietnam sanitary ware production



Source: Ministry of Construction, KIS

Fig 10. Sanitary ware segment performance of Viglacera



Source: VGC, KIS

1.4. Glass segment far from 2017 acme

In our point of view, increasing Fuel Oil (FO) price and tough competition from imported products rather than local producers are the main drivers to the poor performance of Viglacera in 2018 and 2019. We see no significant fundamental change of local producers to compete with foreign players in 2020. However, as HSFO price is projected to fall down due to IMO 2020, we expect gross margin of this segment to improve by 1% in 2020.

1.4.1. Higher cost structure compared with foreign players

According to Viglacera, Vietnam glass producers cannot compete with foreign players due to obsolete technology and higher fuel input (accounts for 31%-40% of Viglacera selling price but this figure of global competitors is around 25-30%). Currently, Binh Son Refinery (HSX: BSR) and Nghi Son Refinery can provide less than 25% of Vietnam FO consumption while imported FO has a higher price due to imported tariff of 3.04%. Moreover, while local producers using FO for heating process, many global players prefer natural gas thanks to higher efficiency.

1.4.2. Lower import tax lures foreign players

Competition with foreign players has been more severe since Vietnam signed FTAs with ASEAN, China, and Korea which have reduced tax tariffs on glass products. As a result, the lower tax barrier has made Vietnam suffer a large import volume. We estimate that around 90mn sqm of glass was imported to Vietnam in 2018.

	2012	2013	2014	2015	2016	2017	2018	2019	2020
Raw glass									
Preferential import tax	40%	40%	40%	40%	40%	40%	40%	40%	40%
ASEAN (ATIGA)	5%	5%	5%	5%	5%	5%	0%	0%	0%
ASEAN - China (ACFTA)	*	*	*	*	*	*	50%	50%	50%
ASEAN – Korea (AKFTA)	*	*	*	*	*	20%	20%	20%	20%
Processed glass									
Preferential import tax	30%	30%	30%	30%	30%	30%	30%	30%	30%
ASEAN (ATIGA)	5%	5%	5%	0%	0%	0%	0%	0%	0%
ASEAN - China (ACFTA)	10%	5%	5%	0%	0%	0%	0%	0%	0%
ASEAN – Korea (AKFTA)	*	*	*	*	*	20%	20%	20%	20%

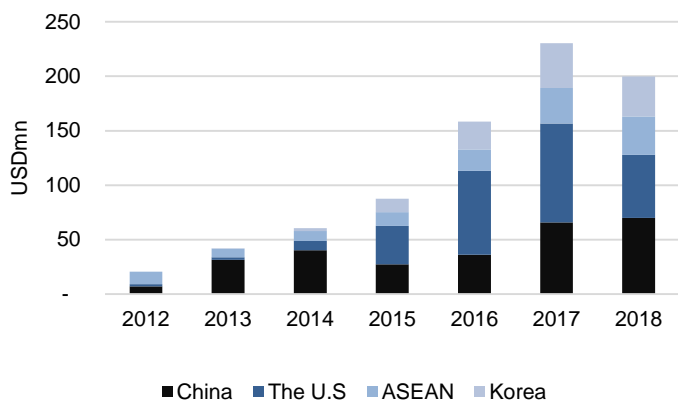
*: applies preferential import tax
Source: MoF, VN Customs, KIS

1.4.3. Selling price to remain stable

In 2020, Viglacera will put its new ultra-white factory of 37mn sqm into operation. Although the old factory of Chu Lai Indevco (capacity of 50mn sqm) will be halted for maintenance, giving Viglacera some advantages, we expect imported volume at around 90mn sqm will fill the shortage easily. Therefore, we estimate domestic glass

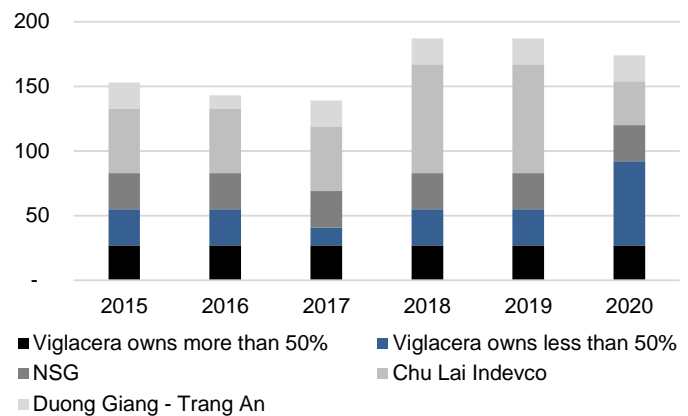
selling price will likely be stable. From the input side, more favorable FO price thanks to IMO 2020 regulation will improve the profitability of domestic glass players.

Fig 11. Main float glass exporters to Vietnam



Source: VN Customs, KIS

Fig 12. Capacity of Vietnam players



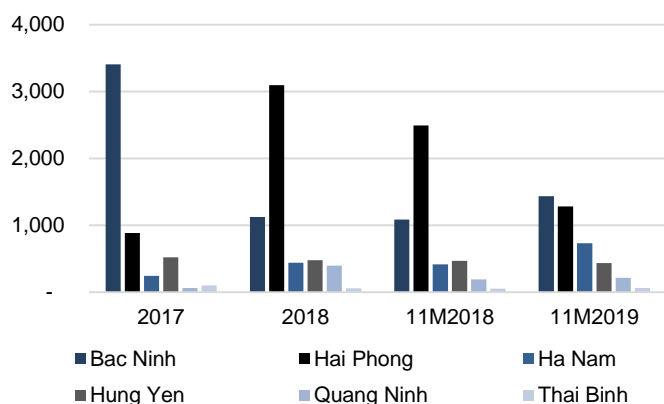
Source: KIS

2. Long-term potentials of Industrial park

2.1. Top player in the North

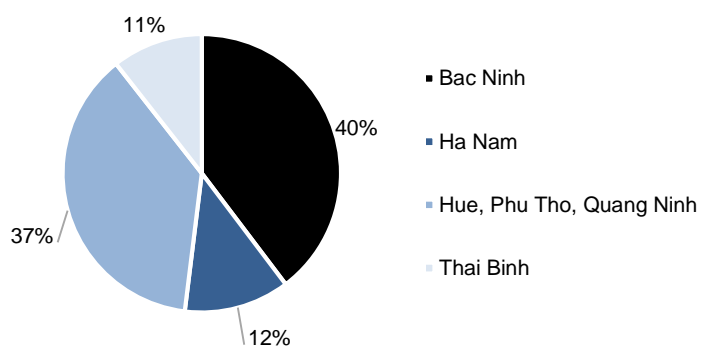
Beside VSIP and Kinh Bac Corporation (HSX: KBC), Viglacera is one of the largest players in the North. Compared with the South, Northern Industrial Parks (IPs) are near China so that if Chinese labor cost increases too fast and the trade tension of the U.S. and China escalates, global manufacturers may shift their factories from China to the North of Vietnam.

Fig 15. Registered FDI, 11M2019



Source: MPI, KIS

Fig 16. Total leasable land of Viglacera, 2019



Source: KIS

We estimate the total remaining land bank of Viglacera at around 992ha. Given the historical land sales of 100-150ha in the 2017-2019 period, the current land bank can ensure the stable IP revenue in the next 5-10 years.

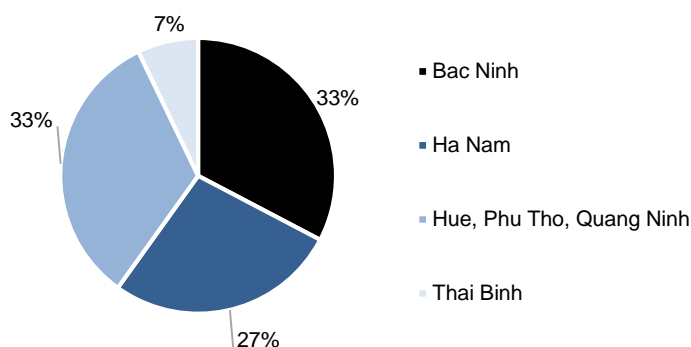
2.2. Long-term potentials

Based on a large land bank and the accelerating industrialization of Vietnam, we believe IP sector has a strong growth potential in the long-term. However, in the short term, we forecast a slight slowdown in 2020 compared to the FY2019 apex result.

We estimate that Viglacera sold an extraordinarily high volume of around 150ha in 2019, up 150% YoY thanks to the trade tension between the U.S. and China that has made many global manufacturers plan to shift their factories to Vietnam. Regarding the current positive signals of the U.S-China trade deal and the fact that most of attractive land areas of Bac Ninh and Ha Nam province was sold in 2019, we estimate IP performance has peaked in 2019.

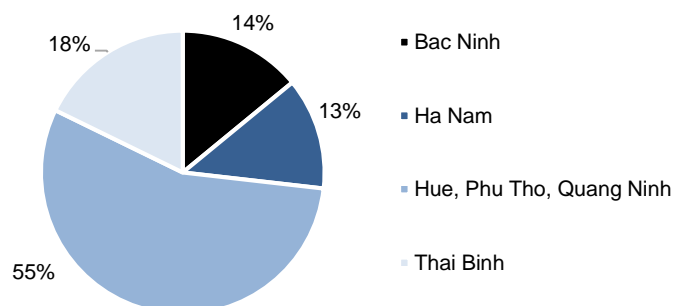
In the long term, new projects Yen My in Hung Yen and Yen Phong 2C in Bac Ninh (of which total land areas are 300ha and 170ha, respectively) will provide Viglacera attractive land areas. Currently, these projects are in land clearance process.

Fig 17. Leased land sales of Viglacera, 2019



Source: VGC, KIS

Fig 18. Remaining leasable land of Viglacera, 2019



Source: VGC, KIS

3. State divestment to be the long-term catalyst

According to the Decision 1232/QD-TTg about a plan and detail timeline to divest away from State owned enterprises from 2017 to 2020, the State will divest all VGC stake in 2019. Gelex Corp (HSX: GEX) has shown its interest in acquiring that stake. On 29 Mar 2019, Ministry of Construction sold 18% stake of VGC to Gelex at VND23k per share and the remaining 53.4% will be divested in the foreseeable future. The State divestment is a long-term catalyst for Viglacera in cost cutting, sales expansion and business performance improvement.

4. Earnings projection & Valuation

4.1. Earnings projection

VNDbn.	2018	2019E	2020E	Assumption
Net revenue	8,812	9,899	10,026	Significant growth in FY2019 thanks to contribution of IP segment
<i>Growth (%)</i>	-4.2%	12.3%	1.3%	
Materials	7,262	7,106	7,234	Solid revenue based on stable performance of the terracotta and tile sub-segments, the profitability improvement of the glass sub-segment based on more favorable input price and the sales expansion of the sanitary ware sub-segment thanks to new factories
Industrial Parks	1,072	2,689	2,638	No growth in FY2020 because of extraordinary FY2019 results
Residential projects	478	104	154	
Gross profit	6,768	7,606	7,732	
<i>Margin (%)</i>	23.2%	23.2%	22.9%	
Materials	1,460	1,413	1,459	
Industrial Parks	405	844	800	Gross profit contraction due to less attractive location of the remaining IPs
Residential projects	166	36	34	
EBIT	910	1,100	1,088	
Net interest expenses	93	108	104	
Net income	673	798	782	
EPS (VND, bonus-adjusted)	1,196	1,458	1,424	

Source: VGC, KIS forecast

4.2. Valuation

Based on Sum of the Parts method, we evaluate VGC share at **VND21,700** per share at the end of 2020. Hence, with today (03/01/2020) price is VND18,000, the total 1-year expected return is **26%**. Therefore, our recommendation on VGC is **BUY** for 1-year investment period.

Sum Of The Parts, VNDbn	2019F	2020F	Remark
1) Material part			EV/EBITDA method
Gross profit		1,459	
D&A		319	
EBITDA	937	969	
Material part value (A)	4,589	4,359	Although 3Y-average EV/EBITDA multiple of leading material companies including Hoa Phat Group (HSX: HPG), Hoa Sen Group (HSX: HSG) Ha Tien 1 (HSX: HT1) Binh Minh Plastic (HSX: BMP) is around 5.5-6.5, we only apply EV/EBITDA multiple of 4.5x for VGC's material segment, implying a discount rate of 20% because it is not the leading firm in any material field.
2) Industrial Park part			RNAV for leased IP and DCF for service activities
WACC		15%	15% over the entire life of projects

Terminal growth rate	4%	
Industrial Park part value (B)	4,319	Including 8 projects in Yen Phong, Hai Yen, Dong Van IV, Tien Hai, Phu Ha, Phong Dien and Dong Mai
3) Residential project part		RNAV method
Residential project value (C)	1,073	Book value at the end of FY2018
4) Long-term investment		
Long-term investment value (D)	382	382
Total Enterprise Value (E) = (A) + (B) + (C) + (D)	10,133	Sum of the Parts
Net debt (F)	-50	
Minority (G)	909	
Equity value (H) = (E) – (F) – (G)	9,735	
Common outstanding shares (mn shares)	448	
Target Price (VND)	21,700	2020
<i>Annualized price return</i>	20.6%	
<i>Expected dividend yield</i>	5.6%	Cash dividend per share = VND1,000
Total expected return	26.2%	2020

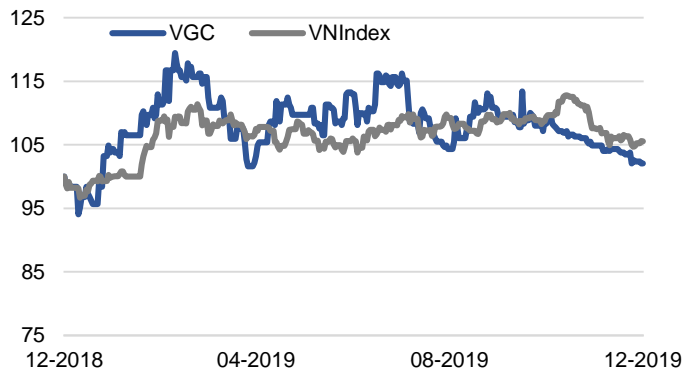
5. Risks

Retrospective valuation at IPO

We see that the divestment of the State is the main catalyst for Viglacera in FY2020. However, one big problem that delays the State divestment progress is retrospective revaluation of Viglacera when it officially changed its structure to a joint-stock company from a State one in 2014. The revaluation may result in an additional cost that the existing and potential shareholders have to pay to the State.

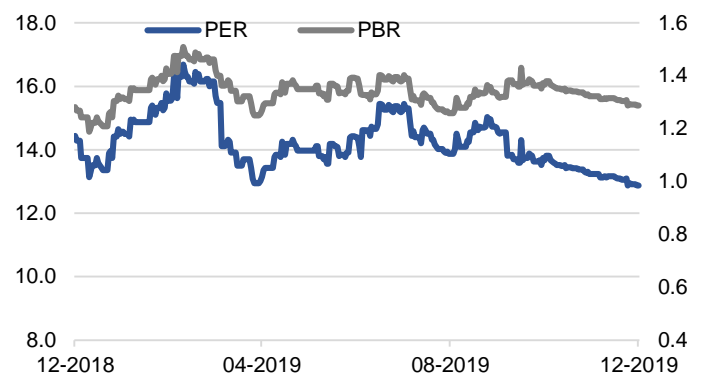
Appendix

Fig 21. 1Y Performance compared to VNIndex



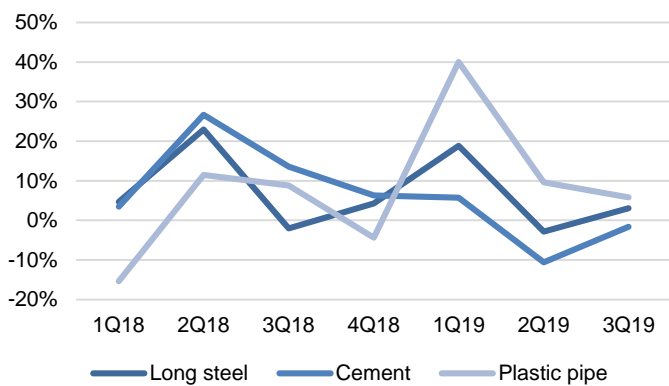
Source: Bloomberg, KIS

Fig 22. 1Y Historical PER & PBR



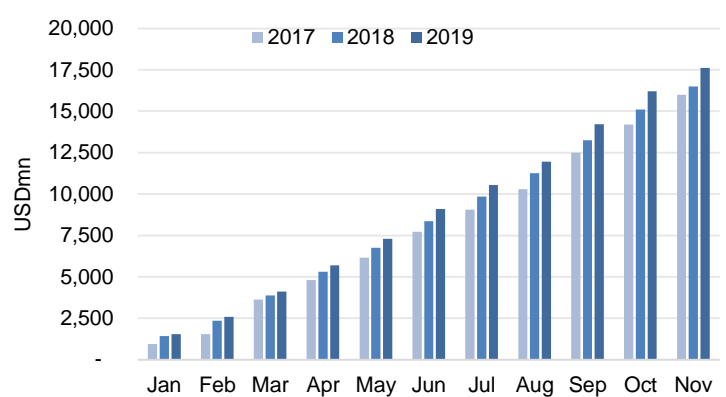
Source: Bloomberg, KIS

Fig 23. Domestic consumption growth, YoY



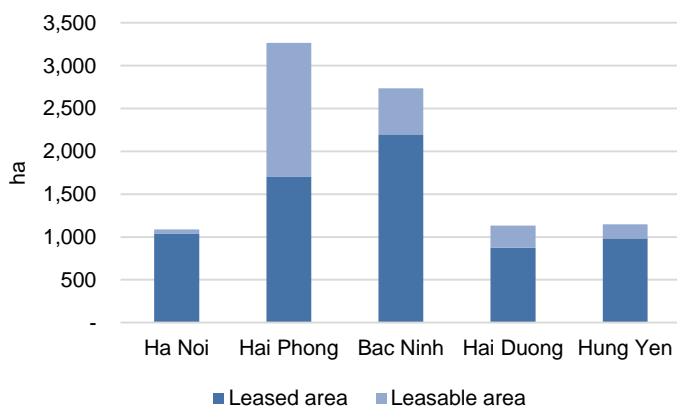
Source: VSA, VNCA, KIS

Fig 24. Aggregate FDI disbursement



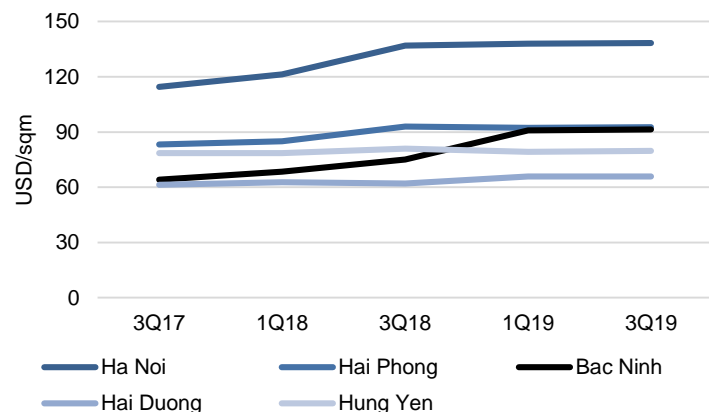
Source: MPI, KIS

Fig 25. Industrial park area and occupancy rate, 3Q2019



Source: JLL, KIS

Fig 26. Average land leased price



Source: JLL, KIS

FINANCIALS MODEL					
Unit: VNDbn.	2016	2017	2018	2019E	2020E
Net Revenue	8,139	9,197	8,812	9,899	10,026
Sales growth (%)	4%	13%	-4%	12%	1%
Tile	1,966	2,047	2,640	2,760	2,824
Terracotta	2,059	2,261	2,197	2,109	2,088
Glass	1,167	1,311	1,057	826	826
Sanitary ware	977	1,012	1,029	1,036	1,121
Industrial Park	593	1,345	1,072	2,689	2,638
Other properties	1,025	864	478	104	154
Others	341	355	340	375	375
COGS	6,160	7,056	6,768	7,606	7,732
Gross margin (%)	26.0%	23.0%	21.0%	16.8%	18.2%
SG&A	1,111	1,136	1,135	1,193	1,205
EBITDA	1,302	1,459	1,403	1,517	1,505
EBITDA margin (%)	16.0%	15.9%	15.9%	15.3%	15.0%
Depr'n & Amort'n	434	454	493	416	416
Operating profit	868	1,005	910	1,100	1,088
Operating margin (%)	10.7%	10.9%	10.3%	11.1%	10.9%
Net interest expense	143	96	93	108	104
As % of avg. net debt	11%	24%	278%	41%	-64%
Interest cover (x)	6.1	10.4	9.8	10.2	10.5
Other profit/loss	44	5	30	12	-
Tax	148	192	174	206	202
Effective tax rate (%)	19%	21%	21%	21%	21%
Net profit	621	722	673	798	782
Net margin (%)	7.6%	7.9%	7.6%	8.1%	7.8%
Minorities	107	122	102	102	102
Net attributable profit	514	600	571	697	680
Number of shares (m)	307	448	448	448	448
EPS (VND, bonus-adjusted)	710	1,295	1,196	1,458	1,424
EPS growth (%)	50%	82%	-8%	22%	-2%
DPS (VND)	400	950	950	1,000	1,000
Pay out ratio(%)	26%	73%	79%	69%	70%

EBITDA = Net revenue – (COGs - Depr'n&Amort'n)– SG&A expenses

EBIT = EBITDA – Depr'n&Amort'n

Net interest expenses = interest expenses – interest income

Other profit/loss consists of other financial income/expenses, profit share from JVs/associates and other income/loss

Payout ratio = Dividend paid / Net attributable profit

BS & CF ITEMS (VNDbn)	2016	2017	2018	2019E	2020E
Increase in WC	662	495	265	583	19
Capex	83	381	543	543	543
Other cash flow items	298	707	481	-	-
Free cash flow	10	-407	-123	598	1,145
Share issues	563	2,274	-	-	-
Dividends paid	134	516	481	448	448
Increase in net debt	-440	-1,351	604	-149	-697
Net debt, end of year	1,082	-269	336	186	-510
Enterprise value	9,859	8,630	9,336	9,288	8,693
Total equity	6,720	9,180	9,336	9,643	9,935
Minority interests	482	604	706	807	909
Shareholder's equity	6,238	8,576	8,630	8,836	9,026
BVPS (VND, bonus-adjusted)	9,245	19,128	19,249	19,708	20,131
Net debt / equity (%)	16%	-3%	4%	2%	-5%
Net debt / EBITDA (x)	0.8	-0.2	0.2	0.1	-0.3
Total assets	16,034	18,511	18,669	18,870	18,507

Net debt = debts – cash & equivalent

Working capital (WC): include long-term incomplete assets of industrial park segment

Capex: material segment only

Key ratios & Valuation	2016	2017	2018	2019E	2020E
ROE (%) (excl minority interest)	10.1%	8.1%	6.6%	8.0%	7.6%
ROA (%)	3.9%	3.9%	3.6%	4.2%	4.2%
ROIC (%)	10.7%	9.6%	8.0%	9.1%	9.0%
WACC (%)	14.1%	15.0%	15.0%	15.0%	15.0%
PER (x)	26.1	14.3	15.5	12.7	13.0
PBR (x)	0.6	1.0	1.0	0.9	0.9
PSR (x)	1.0	0.9	0.9	0.8	0.8
EV/EBITDA (x)	7.6	5.9	6.7	6.1	5.8
EV/Sales (x)	1.2	0.9	1.1	0.9	0.9
Dividend yield (%) (bonus-adjusted)	1.0%	5.1%	5.1%	5.4%	5.4%

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Recommendation System

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

HOLD: where we believe it will be -5% to 15%.

SELL: where we believe it will be -5% or less.

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