

BUY (maintain)

Binh Duong Water & Environment JSC

(HOSE: BWE)

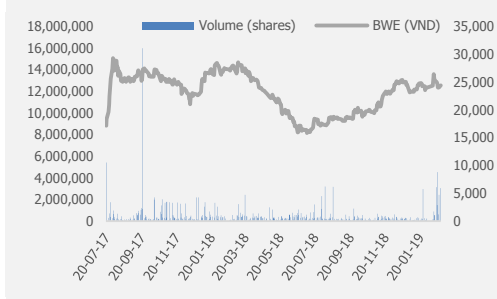
Report date	Mar. 05, 2019
Current price	VND 25,700
Target price	VND 32,500
Upside	26.5%
Bloomberg	BWE VN
Market cap	VND 3,850bn
	USD 165mn
52 weeks movement	VND 27,500
	VND 15,400
Average daily value	VND 6.5bn
	USD 0.2mn
FOL	49%
Current FO	0.07%

Dynamics strengthened from privatization

Our takeaway

- Consistent 17% increase in earnings forecast in FY19 and FY20, thanks to (i) water supply and demand in Binh Duong to yield above 20% growth in revenue with margin supported, (ii) despite a fall in margin of waste treatment segment, advanced technology of BWE could support the rise in price negotiated and volume of industrial waste treated. This segment should continue with 22% revenue growth next year.
- ROE of this utilities company should be safe at 19% in 2019 and 2020 with management strong wish to exclude the ownership of sewage plants.

Price movement



Stock performance	1M	3M	12M
BWE (%)	5%	26%	-3%
VN-Index (%)	12%	3%	-13%

Source: Bloomberg

Major Shareholders

Investment corporations and industrial development - JSC	41.00%
Thu Dau Mot Water co.	38.50%

What's new

Positive momentum in water supply segment, supply matching demand. We forecast demand growth at 10-15% pa with higher living standard of Binh Duong population and increasing industrialization. The construction of two new plants, totaling 100,000 m³ per day, would match the demand with the rise in supply by 22% by 2020. In 2019, we keep the margin unchanged with no more significant catalyst in pricing scheme and input cost reduction after the uplift in margin from 47% in 2017 to 49% in 2018.

Margin slightly squeezed in waste treatment segment due to price increase scheme first stage passed out. We keep our robust view on the amount of waste treatment in 2019 by 17%, to 2,986 tons per day, in which industrial waste treatment would maintain its high growth rate at 32% yoy (+35% in 2018). The firm re-confirmed that their capacity would meet demand with commencement of a new plant with capacity of additional 800 tons per day on 20th Feb 2019 and new incinerator to be used in late 2019. However, we expect a slightly lower margin in this segment of 32% in 2019 due to: (i) margin squeezed in 2018 after the huge impact in 2017 on price increasing scheme, (ii) price increase in waste treatment is less rigid than water treatment and subjecting to approve every two years, and (ii) challenge in waste categorization at sources, competition in this segment.

Key risks

Potential buyers of the Becamex divestment deal of 24 million shares, if related to current major holders (e.g. TDM), may not improve liquidity of the stock and corporate governance. We also note that extraordinary provision expenses on investment in two SOEs worth totaling VND 232 billion may yield higher provision expenses given illiquidity of the investment.

Valuation

We maintain BWE 12-month target price of VND 32,500 with maintained earnings forecasts. BWE is currently trading at 2019F P/E of 9.7x and 2020F P/E of 8.3x, lower than water supply and environment peers' P/E of 12.9x.

Unit: VND billion	FY18	FY19F	FY20F	FY21F
Revenue	2,198	2,783	3,202	3,698
EBIT	493	598	699	810
Net profit	325	378	442	532
Net profit (basic)	325	378	442	532
EPS (VND)	2,163	2,521	2,944	3,547
EPS growth rate (%)	57%	17%	17%	20%
P/E (x)	11.3	9.7	8.3	6.9
EV/EBITDA (x)	6.39	5.76	5.14	4.31
DPS (VND)	700	1,000	700	700
Dividend yield (%)	7.0%	10.0%	7.0%	7.0%
P/B (x)	0.9	0.8	0.8	0.7
ROE (%)	17.9%	18.6%	19.4%	20.4%
Net debt/equity (%)	208%	196%	192%	187%

Source: MBS Research



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Investment highlights

Positive momentum in water supply segment, supply well matching demand

We forecast demand growth at 10-15% pa, in line with the forecast growth rate of the management board with higher living standard of Binh Duong population and increasing industrialization.

The firm also confirmed the increase in supply to match higher water demand with the construction of two new plants totaling 100,000 m³ per day. The first plant with total investment of VND230 billion is forecast to be completed in late 2019 will supply water to the New City of Binh Duong, Ben Cat Ward, Tan Uyen District, Thuan An, Di An and part of HCMC. The other plant, which costs VND 1,000 billion, is expected to be completed in late 2020 and will cover demand in Northern area with its wider coverage of pipeline. The two plants' capacity will raise total supply by 22% by 2020.

Gross margin strengthened from 47% in 2017 to 49% in 2018 with the launch of new pricing scheme in 2018. In 2019, we keep the margin unchanged with no more significant catalyst in pricing scheme and input cost reduction.

Hence, together with 5% rise in water price and compounded effect of rising water consumption by 11% yoy in 2019, we forecast water supply revenue would be up by 19% to VND 1,514 billion, contributing 54% in total revenue (58% of total revenue in 2018).

Margin slightly squeezed in waste treatment segment due to price increase scheme first stage passed out.

Higher volume of waste treated in 2018, which led to 29% yoy rise in revenue. Aligned with our expectation, industrial waste rose impressively by 35% to 800 tons per day. Hence, we keep our robust view on the amount of waste treatment in 2019 by 17% to 2,986 tons per day, of which industrial waste treatment would maintain its high growth rate at 32% yoy.

The firm re-confirmed that capacity will rise to meet the rise in demand with commencement of a new plant with an additional 800 tons per day on 20th Feb 2019 and new incinerator to be completed in late 2019.

However, our forecast rise in revenue of this segment would be insignificant as margin squeezed in 2018 after the huge impact in 2017 on price increasing scheme. The possibility for price increase in waste treatment is easier than water treatment and the proposal for another price increase should occur every two years. This segment is subjected to challenges in waste categorization at sources and competition from other players. Thus, we expect a slightly lower margin in this segment of 32% in 2019 (32.4% in 2018). Waste treatment revenue will rise at a slower pace of 22% yoy this year (+29% in 2018), contributing 23% to total revenue.

Management board revealed wish to separate sewage treatment out of the balance sheet.

We noticed that capital investment in sewage treatment in 2018 of more than VND 1,000 billion in project Tan Uyen was reflected under "other capital" in the 4Q18 results. Management board revealed a strong wish to manage this segment, yet exclude the VND 6,000 billion ownership in four sewage treatment plants out of the balance sheet. The impact of this exclusion would rise ROE in 2019 and 2020 to 19%.

Key risks

Becamex divestment of 24 million shares is based on management's wish to improve liquidity of the stock. Yet if potential buyers are related to current major holders (e.g. TDM), it may not improve the situation. Corporate governance is still of high concern until the company enhances free float.

Special note on extraordinary provision expenses on investment in two SOEs worth totaling VND 232 billion may yield higher provision expenses given illiquidity of the investment

2019 net profit is forecast to increase by 17% yoy to VND 378 billion.

Table 1: FY18 - FY22 Earnings Forecast

VND bn	Actual			Our forecast				yoy			
	FY17	FY18	yoy	FY19F	FY20F	FY21F	FY22F	FY19F	FY20F	FY21F	FY22F
Revenue	1,796	2,198	22%	2,783	3,202	3,698	4,174	27%	15%	15%	13%
Water supply	1,019	1,277	25%	1,514	1,766	2,058	2,352	19%	17%	17%	14%
Waste treatment	406	524	29%	640	755	894	1,007	22%	18%	18%	13%
Sewage treatment	27	32	17%	37	42	49	56	15%	15%	15%	15%
Others	344	538	57%	592	639	697	759	10%	8%	9%	9%
Gross profit	650	871	34%	1,028	1,193	1,387	1,577	18%	16%	16%	14%
Water supply	477	627	31%	750	867	1,010	1,154	20%	16%	17%	14%
Waste treatment	147	170	16%	205	242	286	322	20%	18%	18%	13%
Sewage treatment	13	9	-29%	14	14	17	19	52%	1%	23%	11%
Others	13	65	399%	59	71	73	82	-9%	19%	4%	12%
PBT	238	362	52%	432	507	611	717	19%	17%	21%	17%
PAT	207	325	57%	378	442	532	625	17%	17%	20%	17%
Net profit	207	325	57%	378	442	532	625	17%	17%	20%	17%

Table 2: Revision In Financial Model of BWE

VND bn	New		Previous		New/previous (%)	
	FY19F	FY20F	FY19F	FY20F	FY19F	FY20F
Revenue	2,783	3,202	2,570	3,045	108%	105%
Water supply	1,514	1,766	1,556	1,827	97%	97%
Waste treatment	640	755	571	742	112%	102%
Sewage treatment	37	42	27	27	134%	155%
Others	592	639	416	449	142%	142%
Gross profit	1,028	1,193	1,016	1,215	101%	98%
Water supply	750	867	777	905	97%	96%
Waste treatment	205	242	177	226	116%	107%
Sewage treatment	14	14	13	13	104%	103%
Others	59	71	49	71	121%	100%
PBT	432	507	444	539	97%	94%
PAT	378	442	386	468	98%	94%
Net profit	378	442	386	468	98%	94%

Source: BWE, MBS Research

Financials and Valuation Summary

Income statement (VND bn)	2018	2019F	2020F	2021F
Net revenue	2,198	2,783	3,202	3,698
Cost of goods sold	1,326	1,756	2,010	2,311
Gross profit	871	1,028	1,193	1,387
Financial income	20	46	42	41
Financial expenses	-186	-172	-199	-206
SG&A expenses	-385	-486	-544	-629
Operating profit	256	231	346	415
Other profit	16	18	16	18
EBT	362	432	507	611
EAT	325	378	442	532
Net profit	325	378	442	532
Minority interests	0	0	0	0

Balance sheet	2018	2019F	2020F	2021F
Current assets	1,486	2,734	3,746	4,332
I. Cash & cash equivalents	167	969	1,680	1,993
II. Short-term investments	176	194	213	235
III. Current accounts receivable	761	1,015	1,196	1,325
IV. Inventories	375	549	648	770
V. Other current assets	6	7	8	9
Non-current assets	12,211	12,278	12,018	11,702
I. Long-term receivables	14	22	25	21
II. Fixed assets	4,298	3,069	4,422	4,998
1. Tangible fixed assets	4,214	2,986	4,329	4,896
2. Intangible fixed assets	84	84	93	102
III. Investment properties	0	0	0	0
IV. Long-term assets in progress	7,196	8,470	6,853	5,967
V. Long-term investments	653	669	669	669
VI. Other long-term assets	50	49	49	49
Total assets	13,697	15,011	15,764	16,035
Liabilities	9,475	10,250	10,710	10,837
I. Current liabilities	1,476	1,810	2,085	2,392
1. Short-term payables	713	923	1,001	1,124
2. Short-term loans	763	887	1,084	1,268
II. Non-current liabilities	7,999	8,440	8,625	8,444
1. Long-term payables	6,352	6,560	6,755	6,732
2. Long-term loans	1,647	1,879	1,870	1,712
Equity	4,149	4,689	4,982	5,126
1. Charter capital	1,500	1,500	1,500	1,500
2. Surplus	0	0	0	0
3. Retained earnings	369	559	851	1,225
4. Foreign exchange differences	3	3	3	4
5. Minorities interests	2,348	2,699	2,699	2,469
Total liabilities & equity	13,696	15,011	15,764	16,034

Key ratios	2018	2019F	2020F	2021F
Profitability				
Gross profit margin	40%	37%	37%	38%
EBITDA margin	41%	36%	35%	36%
Net profit margin	15%	14%	14%	14%
ROE	18%	19%	19%	20%
ROA	3%	3%	3%	3%
Growth				
Revenue growth	22%	27%	15%	15%
Gross profit growth	34%	18%	16%	16%
EBT growth	52%	19%	17%	21%
Net profit growth	57%	17%	17%	20%
EPS	57%	17%	17%	20%

Liquidity				
Current ratio	1.01	1.51	1.80	1.81
Quick ratio	0.75	1.21	1.49	1.49
Liabilities/Total assets	64%	62%	62%	61%
Liabilities/Equity	208%	196%	192%	187%
Interest coverage ratio	3.75	3.62	3.64	4.06

Valuation				
Dividend yield	7.0%	10.0%	7.0%	7.0%
EPS (VND)	2,163.4	2,521.4	2,944.1	3,547.1
BVPS (VND)	28,121.0	31,723.0	33,672.5	34,628.4

Source: MBS Research

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STOCK RATING: The recommendation is based on the difference between the 12-month target price and the current price:

Rating	When (target price – current price)/ current price
BUY	>=15%
HOLD	From -15% to +15%
SELL	<= -15%

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