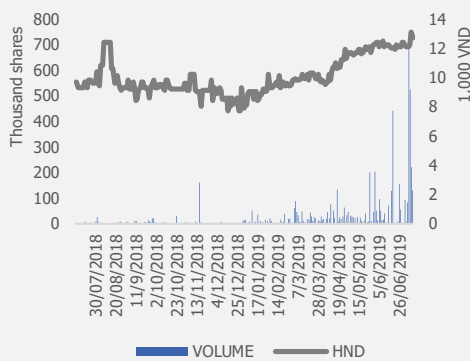


HOLD (Initiation)**Hai Phong Thermal Power JSC (UPCoM: HND)**

Report date	18/07/2019
Current price	VND 15,000
Target price	VND 14,700
Upside	-2%
Bloomberg	HND VN
Market cap	VND 6,550bn USD 281mn
52 weeks movement	VND 7,700 – VND 13,200
Average daily value	VND 0.3bn USD 0.01mn
FOL	49%
Current FO	0.16%

Volatile earnings offset by high dividend yield**Sources of opportunities**

- We recommend a HOLD for HND with a target price of 14,700 VND/share. Upside potential of our target price comes from (i) information on divestment of The State Capital Investment Corporation (SCIC) and (ii) higher profit for FY19. However, the possibility that Vietnam Electricity (EVN) may adjust the market mechanism to fix electricity purchase price implies a downside risk.
- Dividend yield could be 6-9% in the period of 2019-2022 and then improved to 18% in FY23 and 21% from FY24 onwards. The dividend payout ratio would be about 78% of net profit. We expect net profit growth will fluctuate widely in the period of 2019-2024.

Price movement

Stock performance	1M	3M	12M
HND (%)	+2%	+30%	+31%
VN-Index (%)	+1%	-2%	+6%

Source: Bloomberg

Major Shareholders

EVN GENCO2	51%
PPC	26%
SCIC	9%
Vinacomin - Power Holding Corporation	7%

Investment thesis

FY19 net profit forecast of VND 754bn (+77% yoy and 2.2x higher than plan). For 2H19, due to a drop in interest expenses and smaller loss from foreign exchange rates, we expect HND will record a bottom line of VND 239bn (+146% yoy).

Net profit growth is expected to fluctuate widely in 2020-2024. From FY20 onwards, we do not expect any one-off profit from reimbursement from EVN for foreign exchange losses. In FY20, net profit will slightly increase by 6% yoy thanks to lower major repair costs. It would lend a helping hand to maintain gross profit margin of 14% and improve core-business earnings. FY21 net profit is estimated to decrease by 20% yoy. Electricity selling price under Power Purchase Agreement (Pc) could reduce by 2% in FY21 due to downward adjustment of average fixed price after the end of "running in profile" period of the Hai Phong 2 coal-fired thermal power plant (600 MW/ total capacity of 1,200 MW). It could decrease gross profit margin to 11% in FY21 and FY22. In FY23 and FY24, net profit could rebound by 106% yoy and 21% yoy, respectively, because of strong decrease in depreciation cost.

Attractive dividend yield from FY23 onwards. We assume that HND will distribute profit mainly by cash dividend in the upcoming years.

Valuation

We apply the dividend discount model (DDM) and P/E approach to reach the target price of 14,700 VND/share. The stock is currently trading at FY19F P/E of 11x and FY20F P/E of 10x, which is equivalent to 11x of peers.

Upside potential of our target price comes from (i) information on FY19 divestment plan of 9% holding of SCIC and (ii) higher profit for FY19. In the best-case scenario in which HND receives reimbursement annually from EVN for foreign exchange losses from FY20 onwards, the target price would be 16,900 VND/share (13% upside).

Key risk

Major shareholders currently hold 93% stake in HND, creating liquidity concerns.

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Unit: VND billion	FY18	FY19F	FY20F	FY21F
Revenue	9,527	9,987	9,963	9,866
EBIT	953	1,177	1,111	833
Net profit	425	754	801	639
Net profit (basic)	892	723	900	700
EPS (VND)	850	1,357	1,443	1,150
EPS growth rate (%)	7%	60%	6%	-20%
P/E (x)	18	11	10	13
EV/EBITDA (x)	6	4	4	4
DPS (VND)	750	750	1,200	900
Dividend yield (%)	6%	6%	9%	7%
P/B (x)	1.3	1.3	1.2	1.2
ROE (%)	8%	13%	13%	10%
Net debt/equity (%)	130%	93%	61%	29%

Source: MBS Research

Recommendation and valuation

We apply the dividend discount model (DDM) and P/E approach to reach the target price of 14,700 VND/share (-2% upside). The stock is currently trading at FY19F P/E of 11x and FY20F P/E of 10x, which is equivalent to 11x of peers.

Upside potential of our target price comes from (i) information on FY19 divestment plan of 9% holding of SCIC and (ii) higher profit for FY19. In the best-case scenario in which HND receives reimbursement annually from EVN for foreign exchange losses from FY20 onwards, the target price would be 16,900 VND/share (13% upside). The reimbursement from EVN for foreign exchange losses is estimated at VND 200bn annually in the forecasted period based on the assumption of 2% depreciation per annum of VND.

In contrast, the possibility that EVN may adjust the market mechanism to fix electricity purchase price implies downside risk for the stock.

HND is restructuring its human resource management, in accordance with the guideline of EVN GENCO2 parent company. Particularly, in December 2018, HND held an extraordinary general meeting to elect Mr. Ta Cong Hoan (deputy general director, representing 30% holding in HND of GENCO2) to the Board of Management (BOM) and he is currently the Chairman of the Board. In April 2019, HND held an annual general meeting to approve the amendment and supplement of the company's charter. It focused on expanding the approval authority of the BOM and correspondingly limiting the decision of CEO. In June 2019, HND announced the Resolution of BOM to approve the term extension (from 19 Jun 2019 to 30 Sep 2019) of Mr. Nguyen Thuong Quang as the CEO. Nonetheless, we deem that these changes will have no significant impact on the company's financial results.

Table 1: Target price

Method	Fair value (VND/share)	Proportion
DDM	13,430	50%
P/E	16,041	50%
Target price	14,700	

Source: MBS Research

Table 2: Valuation Summary

Unit: VND billion	FY19F	FY20F	FY21F	FY22F	FY23F	FY24F	FY25F
Net profit	754	801	639	720	1,481	1,798	1,691
Investment and development fund	38	40	32	36	74	90	85
Bonus and welfare fund	75	80	64	72	148	180	169
Retained earnings	266	81	93	62	59	78	87
Cash dividend	375	600	450	550	1,200	1,450	1,350
DDM			Re & g				
Present value for FY19 – FY25 cash dividend	3,050		rf	4.7%			
Present value for terminal value	3,665		Beta	1.0			
Total present value	6,715		rm	15.6%			
Shares outstanding (mn)	500		Re	15.6%			
Target share price (VND)	13,430		g	2.0%			

Source: MBS Research

Table 3: P/E of peers

Stock	Market Capitalization (VND bn)	Market price (VND/share)	EPS	P/E
PPC	9,971	31,100	3,501	9
QTP	4,860	10,800	612	18
NT2	7,744	26,900	2,717	10
Average				11

Source: Listed companies, MBS Research

Investment highlights

FY19 net profit forecast of VND 754bn (+77% yoy)

FY19 net profit is forecasted at VND 754bn (+77% yoy and 2.2x higher than FY19 plan). For 2H19, due to a drop in interest expenses (VND 179bn, -26% yoy) and smaller loss from foreign exchange rates (VND 90bn, -70% yoy), we expect HND will record a bottom line of VND 239bn (+146% yoy). Starting from FY19, HND will not record losses from foreign exchange rates in (i) capital construction of the Hai Phong 2 coal-fired thermal plant and (ii) revaluation of foreign currency items at the end of FY15 (booking a loss of VND 299bn in FY18).

Lower financial expenses could well cover a decrease in gross profit margin from 17% to 14% in 2H19. FY19 electricity production cost is estimated to increase by 8% yoy based on higher coal prices and major repair costs. However, the average selling price could only improve by 3% yoy due to:

- (i) A 9% reduction of average fixed price in Pc after finalization of work construction.
- (ii) Selling price in Competitive Generation Market - CGM (Pm) is anticipated to lessen 3% owing to a decline in FY19 Capacity-Add-on price from 221 to 144 VND/kWh on average (according to Electricity Regulatory Authority of Vietnam).

In 1H19, HND recorded a net profit of VND 515bn (+57% yoy) thanks to lower financial expenses and VND 153bn one-off profit in 2Q19 from reimbursement from EVN for FY16 foreign exchange losses. The results are equivalent to 68% our full year net profit forecast and 1.5 times higher than the company's FY19 target. The profit usually peaks in the 2nd quarter (as dry season reaches peak) or the 4th quarter (high power demand for industrial production for national holidays). In FY19, HND plans to conduct major inspection of unit 1 (300 MW) from August to early October and medium inspection of unit 3 (300 MW) in September.

Fluctuation in net profit growth in the period of 2020-2024

From FY20 onwards, we do not expect any one-off profit from reimbursement from EVN for foreign exchange losses. In FY20, net profit will increase slightly by 6% yoy thanks to lower major repair costs. It would lend a helping hand to maintain gross profit margin of 14% and improve core-business earnings. FY21 net profit is estimated to decrease by 20% yoy. Pc could reduce 2% in FY21 due to downward adjustment of average fixed price after the end of "running in profile" period of the Hai Phong 2 coal-fired thermal power plant (600 MW). It could decrease gross profit margin to 11% in FY21 and FY22. In FY23 and FY24, net profit could rebound by 106% yoy and 21% yoy, respectively, because of strong decrease in depreciation cost by VND 750bn and VND 310bn, respectively. We expect that HND would fully depreciate by FY27.

In addition, our forecasts are based on the following key assumptions:

- Using 5a1/6a1 coal dust at the ratio of 70%/30%.
- Average coal volume of 3.2 million tons per year, supplied by Vietnam National Coal and Mineral Industries Group (Vinacomin) and Dong Bac Corporation.
- Coal consumption rate of 459 g/kWh.
- Self-consumption of electricity of 9.2%.
- The ratio of volume sold under PPA (Qc)/volume sold in CGM (Qm) would maintain at 80%/20%.
- Pc would not be changed significantly in case of PPA renegotiation or re-signing (if any).
- Financial expenses continue to decrease following long-term loan repayment schedule. From FY25, HND would be free of foreign long-term loans, leading to no interest expenses and foreign exchange losses correspondingly.

- Corporate income tax would be 5% in the period of 2020-20Y24 and increase to 10% by FY25.
- Total capacity would maintain at 1,200 MW. HND has not announced any expansion plan for the upcoming years. The VND 1,428bn investment project of emission control technology has been suspended to wait for direction from the Prime Minister.
- Every year, HND would conduct major inspection of each unit alternately. Hence, the production output would not be strongly impacted by the inspection.

Attractive dividend yield from FY23 onwards

Forecasted dividend yield could be 6-9% (1,000 VND/share on average) in the period of 2019-2022 and then improve to 18% (2,400 VND/share) in FY23 and 21% (2,800 VND/share) from FY24 onwards. The dividend payout ratio would be about 78% of net profit. We assume that HND will distribute profit mainly by cash dividend in the upcoming years.

Table 4: FY18 – FY25 financial results of HND

	Unit	FY18	FY19F	FY20F	FY21F	FY22F	FY23F	FY24F	FY25F
Production ratio									
Utilization rate		66%	66%	66%	66%	66%	66%	66%	66%
Production volume	Million kWh	6,967	6,955	6,955	6,955	6,955	6,955	6,955	6,955
Selling volume	Million kWh	6,327	6,315	6,315	6,315	6,315	6,315	6,315	6,315
Coal prices	VND/ton	1,577,545	1,794,016	1,852,480	1,912,884	1,975,293	2,039,775	2,106,400	2,175,242
Production costs									
	VND/kWh	1,254	1,349	1,359	1,392	1,427	1,344	1,332	1,370
Material cost	VND/kWh	863	942	972	1,003	1,034	1,067	1,101	1,136
Depreciation cost	VND/kWh	292	285	284	285	285	166	117	117
Repair cost	VND/kWh	44	63	48	48	48	48	48	48
Labor cost	VND/kWh	29	30	25	26	28	29	30	32
Outsourcing cost	VND/kWh	10	10	11	11	12	12	13	14
Others	VND/kWh	17	18	19	20	21	22	23	24
Selling prices									
	VND/kWh	1,504	1,554	1,576	1,561	1,595	1,629	1,665	1,701
Financial results									
	VND bn								
Revenue									
		9,527	9,987	9,963	9,866	10,078	10,296	10,521	10,753
Electricity		9,518	9,814	9,955	9,858	10,070	10,288	10,513	10,745
Reimbursement from EVN for foreign exchange losses		-	153	-	-	-	-	-	-
Cost of goods sold									
		7,935	8,518	8,579	8,791	9,009	8,487	8,410	8,651
Gross profit									
		1,592	1,469	1,384	1,075	1,068	1,809	2,111	2,101
Financial income		24	22	22	22	22	22	22	22
Financial expenses									
		997	520	376	229	127	56	14	6
Interest expenses		504	383	268	161	85	31	6	6
Realized foreign exchange losses		26	31	41	27	18	17	8	-
Unrealized foreign exchange losses		169	106	67	41	24	8	-	-
Booking foreign exchange differences (*)		299	-	-	-	-	-	-	-
G&A expenses									
		169	177	186	196	205	216	226	238
Operating profit									
		450	794	844	672	758	1,559	1,892	1,879
EBT									
		449	794	844	672	758	1,559	1,892	1,879
Net profit									
		425	754	801	639	720	1,481	1,798	1,691
Basic earning									
		892	723	900	700	756	1,501	1,802	1,688

Source: HND, MBS Research

(*) Losses from foreign exchange rates in (i) capital construction of the Hai Phong 2 coal-fired thermal plant and (ii) revaluation of foreign currency items at the end of FY15

Financials Summary

Income statement (VND bn)	FY18	FY19F	FY20F	FY21F
Net revenue	9,527	9,987	9,963	9,866
Cost of goods sold	7,935	8,518	8,579	8,791
Gross profit	1,592	1,469	1,384	1,075
Financial income	24	22	22	22
Financial expenses	997	520	376	229
Profit of associates	0	0	0	0
Selling expenses	0	0	0	0
G&A expenses	169	177	186	196
Operating profit	450	794	844	672
Other profit	-1	0	0	0
EBT	449	794	844	672
EAT	425	754	801	639
Net profit	425	754	801	639
Minority interests	0	0	0	0

Balance sheet (VND bn)	FY18	FY19F	FY20F	FY21F
Current assets	3,021	3,462	3,636	4,055
I. Cash & cash equivalents	692	853	980	1,402
II. Short-term investments	0	0	0	0
III. Current accounts receivable	1,967	1,997	1,993	1,973
IV. Inventories	356	608	660	676
V. Other current assets	5	4	4	4
Non-current assets	10,748	8,963	7,171	5,378
I. Long-term receivables	0	0	0	0
II. Fixed assets	10,328	8,638	6,853	5,067
1. Tangible fixed assets	10,327	8,637	6,852	5,066
2. Intangible fixed assets	1	1	1	1
III. Investment properties	0	0	0	0
IV. Long-term assets in progress	168	180	180	180
V. Long-term investments	1	1	1	1
VI. Other long-term assets	252	144	137	130
Total assets	13,769	12,425	10,807	9,433
Liabilities	8,077	6,429	4,690	3,191
I. Current liabilities	2,687	3,027	2,929	2,328
1. Short-term payables	825	1,004	1,188	1,331
2. Short-term loans	1,861	2,022	1,741	997
II. Non-current liabilities	5,391	3,403	1,761	863
1. Long-term payables	0	0	0	0
2. Long-term loans	5,391	3,403	1,761	863
Equity	5,692	5,996	6,117	6,242
1. Charter capital	5,000	5,000	5,000	5,000
2. Surplus	197	197	197	197
3. Retained earnings	496	799	921	1,045
4. Foreign exchange differences	0	0	0	0
5. Minorities interests	0	0	0	0
Total liabilities & equity	13,769	12,425	10,807	9,433

Key ratios	FY18	FY19F	FY20F	FY21F
Valuation				
EPS (VND)	850	1,357	1,443	1,150
BVPS (VND)	11,385	11,992	12,234	12,484
P/E	18	11	10	13
P/B	1.3	1.3	1.2	1.2
Profitability				
Gross profit margin	17%	15%	14%	11%
EBITDA margin	25%	30%	29%	27%
Net profit margin	4%	8%	8%	6%
ROE	8%	13%	13%	10%
ROA	2.9%	5.8%	6.9%	6.3%
Growth				
Revenue growth	5%	5%	0%	-1%
EBT growth	7%	77%	6%	-20%
Net profit growth	7%	77%	6%	-20%
EPS	7%	60%	6%	-20%
Total assets	-9%	-10%	-13%	-13%
Equity	10%	5%	2%	2%
Liquidity				
Current ratio	1.12	1.14	1.24	1.74
Quick ratio	0.99	0.94	1.02	1.45
Liabilities/Total assets	59%	52%	43%	34%
Liabilities/Equity	1.42	1.07	0.77	0.51
Interest coverage ratio	7.80	3.07	4.15	5.18
Operating efficiency				
Receivables turnover	5.0	5.0	5.0	5.0
Days sales outstanding	73	73	73	73
Inventory turnover	15	14	13	13
Days sales of Inventory	25	26	28	28
Payables turnover	9.4	9.4	9.4	9.4
Days payables outstanding	39	39	39	39

Cashflow Statement (VND bn)	FY18	FY19F	FY20F	FY21F
CFO	1,151	2,465	2,643	2,508
CFI	9	(103)	7	7
CFF	(491)	(2,202)	(2,523)	(2,093)
Net cash flows during the period	669	161	127	422

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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