

Business update report

DRC - Da Nang Rubber JSC

22/03/2019

BSC

Recommendation:

Vuong Chi Tam (FA)

tamvc@bsc.com.vn

Target price	27,180
Closing price	22,300
Upside	21.9%

Le Quoc Trung (TA)

trunglq@bsc.com.vn

Target price	23,000
Cut loss price	20,000

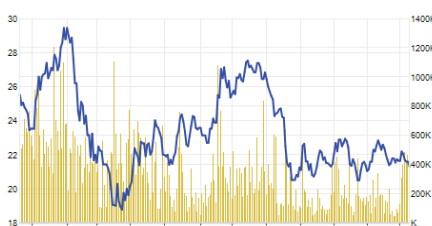
Market data

Number of shares (stock)	118,793
Capitalization (billion VND)	2,566
Highest price 52 weeks	29,450
The average trading volume	233,864
Foreign ownership	23.41%

Major shareholders

Vinachem	50.51%
KWE Beteiligungen	6.02%
PXP VN	4.06%
FTIF	2.86%

Price movement for 1 year



Company Overview

Currently DRC is focusing on developing Radial tire products for sale of steel and steel. DRC's second stage of Radial tire has come into operation and received positive feedback from partners.

LONG-TERM ROAD

Valuation

We recommend to BUY with DRC shares with a target price of 27,180 VND/share, upside 21.9% with 3 methods P/E (20%), FCFE (40%) and FCFF (40%). Currently, DRC is being traded with P/E = 18.51x, lower than the current regional tire industry average (21.0x).

Forecast of business results 2019

BSC forecasts, in 2019, DRC will record net revenue and NPAT at VND 3,933 billion (+ 10.8% yoy) and VND 157 billion (+ 13.2% yoy), equivalent to EPS 2019 = VND 1,192 / share. Assuming (1) Bias tire consumption will not change much compared to 2018, (2) Radial tire output reaches 450,000 tires, (3) natural rubber price + 0% yoy, rubber price artificial and chemical -5% yoy because oil price is forecasted to decrease, price of black coal is not much volatile, (4) interest rate is expected to decrease because businesses do not need to invest, thus improving NPM margin.

Catalyst

- Natural rubber price is forecasted to remain low (about VND 34 million/ton) in 2019, oil price is expected to be -12% yoy to support price reduction of chemicals and artificial rubber.
- Vinachem plans to divest DRC to 36% in quarter 2/2019.

Investment Risk

- Price fluctuation of materials.
- High competition for automobile tires.

Update business results

(1) 2018 business results. In 2018, DRC recorded net revenue and NPAT of VND 3,551 billion (-3.2% yoy) and VND 139 billion (-16.3% yoy) due to high competition status, Enterprise is difficult to raise selling prices to compensate for the increase in material costs.

(2) DRC's consumption of automobile tires in 2018 reached 1.084 million tires (-11% yoy) due to the decrease in bias tire production. In particular, the consumption of bias tires reached 708,911 tires (-20% yoy), of which, light truck tires volume was -25.75% yoy. In contrast, Radial tire production grew well, reaching 375,610 tires (+ 12.63% yoy), domestic consumption reached 120,203 tires (+ 13.27% yoy), exports reached 255,407 tires (+ 12.34% yoy).

(3) Raw material prices tend to decrease. On average in 2018, natural rubber prices -19.84% yoy, artificial rubber -15.7% yoy (50% of rubber material prices). However, COGS is still high due to chemical price + 24.8% yoy and black coal + 41.06% yoy, making DRC's gross profit margin decrease to 12% (2017: 12.5%).

(4) Phase 2 of Radial factory went into operation and started supplying products to the market. We expect in 2019, Radial tire production will reach 450,000 tires from this contribution.

Other reports

Link

2018 business results. In 2018, DRC recorded net revenue and NPAT of VND 3,551 billion (-3.2% yoy) and VND 139 billion (-16.3% yoy) due to high competition status, enterprises hardly increase selling prices to compensate for the increase in raw material costs (prices of chemicals and black coal increased sharply + 25% and + 40% yoy, respectively, these 2 materials contribute about 32% of the material cost of the enterprise). In addition, because enterprises do not meet Euro 4 standards as expected by big firms like Thaco, ..., the production of light truck tires decreases, affecting the overall profit of enterprises. DRC's gross profit margin in 2018 reached 12%, down slightly from 12.5% last year. It is worth noting that Radial tires have started to profit, achieving a gross margin of 2.69% this year.

DRC's consumption of automobile tires in 2018 reached 1.084 million tires (-11% yoy) due to the reduction of bias tires.

- **The consumption of bias tires is 708,911 tires (-20% yoy)**, in which, light truck tire production was - 25.75% yoy, only reaching 493 thousand tires due to the influence of Euro 4 standard.

- **In contrast, Radial tire production grew well, reaching 375,610 tires (+ 12.63% yoy), domestic consumption reached 120,203 tires (+ 13.27% yoy), exports reached 255,407 tires (+ 12.34% yoy).** We realize that DRC's radial tire production has grown well, > + 30% in both domestic and export markets in the fourth quarter of 2018 when the second phase of Radial factory came into operation. In 2019, we expect that the second phase of Radial factory will continue to contribute and improve the revenue and profit of enterprises.

- **We forecast that in 2019, DRC will consume 450,000 Radial tires (+ 19.8% yoy)**, with the expectation of (1) tire consumption in Vietnam, according to BSC's forecast, up 9% yoy in 2019, (2) Radial tires have a faster consumption rate due to their small scale and quality. Good products (assessed as equivalent to tires of FDI enterprises). Regarding Bias tire, we expect there will not be much fluctuation due to (1) reduced light truck tires offset by semi-steel radial tires, (2) long-term partners will continue to consume and create a stable source for Bias tires.

Raw material prices tend to decrease. On average in 2018, natural rubber prices -19.84% yoy, artificial rubber -15.7% yoy (50% of rubber material prices). However, COGS is still high due to chemical price + 24.8% yoy and black coal + 41.06% yoy (material structure: chemicals 17%, black coal 14%), DRC's gross profit margin decreased to 12% (2017: 12.5%). We expect that in 2019, rubber prices will continue to remain low due to oversupply in the world, oil prices, according to BSC, forecast at 65 USD/barrel, -12% yoy to support price reduction of chemicals and black coal. Gross profit margin of 2019 is expected at 11.9% according to BSC's forecast.

Vinachem plans to divest from DRC in quarter 2/2019, reducing its ownership rate from 51% to 36%. This receives the attention of many domestic and foreign investors.

Forecast 2019. BSC forecasts, in 2019, DRC will record net revenue and NPAT at VND 3,933 billion (+ 10.8% yoy) and VND 157 billion (+ 13.2% yoy), equivalent to EPS 2019 = VND 1,192/share with the assumption that (1) Bias tire consumption will not fluctuate much compared to 2018, (2) Radial tire output reaches 450,000 tires, (3) natural rubber price + 0% yoy, artificial rubber price and chemical price -5% yoy because oil price is forecasted to decrease, price of black coal is not much changed. Currently, DRC shares are being traded at P/E = 18.6x, lower than the average level of the tire industry at 21x.

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Financial analysis

22/03/2019

BSC

	2015	2016	2017	2018	2019F
Net revenue	3,318	3,361	3,669	3,551	3,933
Gross profit	799	701	458	427	467
Financial revenue	11	16	8	12	11
Financial expenses	(124)	(83)	(74)	(98)	(72)
Interest	(55)	(43)	(42)	(49)	(42)
Selling expenses	(77)	(85)	(118)	(113)	(132)
General and administrative	(84)	(73)	(66)	(55)	(77)
Operating profit/loss	526	476	207	173	197
Other loss/profit	7	18	0	2	-
Profit before tax	532	494	208	175	197
Profit after tax	415	395	166	139	157
Minority interest	-	-	-	-	-
Parent company profit	415	395	166	139	157
EPS (trừ quỹ KTPL)	4,234	3,252	1,132	1,110	1,192
Current assets	1,304	1,247	1,090	1,246	1,243
Money and short-term in	240	51	67	51	214
Short-term receivables	278	419	412	315	440
Inventories	785	771	596	846	575
Other current assets	0	6	15	35	15
Long-term assets	1,839	1,568	1,704	1,587	1,470
Long-term receivables	0	0	0	0	0
Fix assets	1,760	1,488	1,518	1,517	1,412
Long-term uncompleted i	59	16	131	0	-
Other long-term assets	16	59	50	66	54
Total assets	3,143	2,815	2,794	2,833	2,714
Liabilities	1,470	1,233	1,268	1,310	1,152
Short-term liabilities	877	842	859	1,065	994
Short-term Debt	446	513	525	707	567
Long-term liabilities	593	392	409	245	157
Long-term Debt	593	392	409	245	157
Equity	1,673	1,582	1,527	1,523	1,562
Contributed capital	914	1,188	1,188	1,188	1,188
Undistributed profits	461	225	142	113	155
Total resources	3,143	2,815	2,794	2,833	2,714
% yoy sales	26%	21%	31%	9%	11%
Gross profit margin	24.1%	20.9%	12.5%	12.0%	11.9%
Interest/Net revenue	1.6%	1.3%	1.1%	1.4%	1.1%
Selling expenses/Net r	2.3%	2.5%	3.2%	3.2%	3.4%
General and administrat	2.5%	2.2%	1.8%	1.5%	2.0%
Net profit margin	15.8%	14.2%	5.6%	4.9%	5.0%

Net revenue 2018 -3.2% yoy. Bias tire consumption dropped sharply, -20% yoy, Radial tire consumption increased by 12.63% yoy. Radial tires also continued to profit, gross margin in 2018 reached 2.7%.

Compared to 2017, natural rubber price decreased by 19.84%, artificial rubber price decreased by 15.7%, chemicals + 24.8% yoy and black coal + 41.06% yoy made the LNG margin of enterprises go sideways, reaching 12% (same period 12.5%).

Financial expenses increased due to increased debt financing for Phase 2 Radial project.

Receivables from customers decreased by 23.5% yoy.

Inventories increased by 42% yoy because enterprises imported materials to produce Radial tires for phase 2.

Short-term debt increased by 24% yoy to finance tire production materials for Phase 2 of Radial factory.

Gross profit margin of the company in 2018 decreased to 12% due to rising raw material prices.

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FINANCIAL RATIO

	2015	2016	2017	2018	2019F
1. Liquidity					
Current ratio	1.49	1.48	1.27	1.17	1.25
Quick ratio	0.59	0.56	0.56	0.34	0.48
2. Capital structure					
Current assets/Total as	0.41	0.44	0.39	0.44	0.46
Long-term assets/Total	0.59	0.56	0.61	0.56	0.54
Liabilities/Total assets	0.47	0.44	0.45	0.46	0.42
Liabilities/Equity	0.88	0.78	0.83	0.86	0.74
Short-term Liabilities/Tc	0.28	0.30	0.31	0.38	0.37
Long-term liabilities/Tot	0.19	0.14	0.15	0.09	0.06
3. Operational capacity					
Inventory turnover	3.4	3.4	4.7	4.3	4.9
Receivables turnover	12.6	10.4	9.5	10.4	10.4
Accounts payable turnc	18.0	20.1	17.5	15.0	15.6
Days' sales in inventory	108.7	106.7	77.7	84.2	74.8
Days sales in receivabl	28.9	34.9	38.3	35.1	35.0
Days payable outstandi	20.3	18.2	20.8	24.3	23.4
CCC	117.3	123.5	95.1	95.1	86.4
4. Profitability					
Net profit margin	12.5%	11.8%	4.5%	3.9%	4.0%
ROE	25.9%	24.3%	10.7%	9.1%	10.0%
ROA	13.2%	13.3%	5.9%	4.9%	5.8%
Net operating profit ma	15.8%	14.2%	5.6%	4.9%	5.0%
5. Dupont analysis (5 components)					
Financial leverage	1.96	1.83	1.80	1.85	1.74
Assets turnover	1.06	1.13	1.31	1.26	1.45
EBIT margin	0.18	0.16	0.07	0.06	0.06
Interest burden	0.91	0.92	0.83	0.78	0.82
Tax burden	0.78	0.80	0.80	0.79	0.80
6. Valuation					
PE	5.7	7.3	18.3	18.1	17.8
PB	1.3	1.8	1.9	1.7	1.6
EPS	4,542	3,531	1,398	1,170	1,192
BVPS	18,307	13,523	12,853	12,820	13,151
7. Growth (%)					
Total assets	0%	-10%	-1%	1%	-4%
Debt	8.9%	-5.4%	-3.5%	-0.3%	-12.1%
Net revenue	2.0%	1.3%	9.2%	-3.2%	10.8%
Gross profit	-0.5%	-12.3%	-34.7%	-6.7%	9.4%
Net income	17.7%	-4.8%	-58.0%	-16.5%	13.2%

Short-term payment ratio decreased sharply over the same period

Property structure:

Asset structure remains at about 40% of short-term assets, 60% of long-term assets over the years.

Debts and financial leverage tend to increase mainly due to investment loans for Phase 2 of Radial factory.

Operation capacity is not much changed. Days' sales in inventory and Days payable outstanding increased, Days sales in receivables decreased.

Net profit margin decreased due to the increase in raw material prices.

Technical highlights:

- Current trend: Accumulation
- MACD trend indicator: Divergence at the central road
- RSI indicator: Neutral zone, approaching the upper Bollinger channel.
- MA lines: Three MA lines are moving sideways, MA20 and MA50 converge at 21.82.

Outlook: DRC is in the mid-term cumulative price channel 20.2-23.16. The liquidity of the sessions has not been uniform, indicating that the accumulation status can still last. The MACD indicator and the 3-MA moving line support the cumulative trend. RSI indicator shows that short-term reversal signal will happen when RSI is close to the upper Bollinger channel and does not tend to break out.

Recommendations: The position to buy at the price range of 20.2-21 and close at the price range of 22.5-23 when there is no signal to break the mid-term accumulation trend. Take a loss if the stock returns to the price zone of 20.

Technical graph



Disclosure

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BSC Headquarter

BIDV Tower, 10th & 11th Floor
35 Hang Voi, Hoan Kiem, Ha Noi
Tel: +84 4 3935 2722
Fax: +84 4 2220 0669

Ho Chi Minh City Office

146 Nguyen Cong Tru St, 9th Floor
District 1, Ho Chi Minh City
Tel: +84 8 3821 8885
Fax: +84 8 3821 8510

<http://www.bsc.com.vn>
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