

Sector: Tire sector - ICB 3357
May 27, 2014

COMPANY ANALYSIS REPORT THE SOUTHERN RUBBER INDUSTRY JSC (CSM)



TRADING CHART



Based on adjusted price volume unit 10,000 share

INVESTMENT VIEW

Investment view	BUY
Target price	43,500
Current price	38,400
Prospect in 6 month	Increase
Prospect in 12 month	Increase

TRADING INFORMATION

Outstanding (mil. shares)	67.3
Market capital (bil. dong)	2,584
Book value (bil. dong)	19,272
Foreign ownership (%)	12.83%
Current price (dong/share)	38,400
Average trading volume in 10 days (shares)	908,595
Lowest price in 52 weeks (dong)	25,600
Highest price in 52 weeks (dong)	44,600
+/- in 7 days	4%
+/- in 1 month	-4.5%

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INVESTMENT HIGHLIGHTS

- ❖ **CSM is the leading manufacturer in Vietnam tire sector.** CSM accounts for 33% of the total domestic marketshare và 12% of the export marketshare, which are the highest among Vietnam tire companies. In particular, CSM is superior in tire segments for auto (25% market share) and motorcycles (35% market share). In tire segment for truck, CSM accounts for 8% market, which is lower than DRC.
- **Continuos decline in natural rubber prices** brings cost advantages for tire businesses: raw rubber materials accounted for 85% of the CSM's material structure. Quarter 1/2014, natural rubber prices continued to decline by 10.83% compared to the end of 2013.
- **Motivation for medium- and long-term growth from new radial tire factory and export markets:** the radial tire factory (with a total capacity of 1 million tires, expects to export 60% of the production) is expected to be the main growth driver of the company in the context of domestic demand stability. However, we believe that the radial factory will not contribute much to the revenue and profit of the company in 2014.
- **Divestment in non-core business:** in 2013, the company divested in Phuoc Hoa Rubber Company. In 2014, the company will probably divest in Carbon Philip Company (8%), transfer two projects, namely No. 9 Nguyen Khoai and 504 Nguyen Tat Thanh; and stop a number of projects in Ho Chi Minh City.
- ❖ The company's performance in Q1/2014 showed a positive result with the profit after tax of VND 79 billion, which increased by 14.42% q-o-q, mainly due to the sharp fall in raw rubber prices and in administration costs (VND 10 billion).
- ❖ We expect the revenue and profit after tax of CSM in 2014 will respectively be VND 3,252 billion, up 3.77% and VND 336 billion, down 6.63% (EPS of 4,996 dong) compared with 2013. The company will continue to benefit from the low rubber price. However, net profit margins may decrease (from 11.49% in 2013 to 10.34% in 2014) due to increases in depreciation and interest expenses.

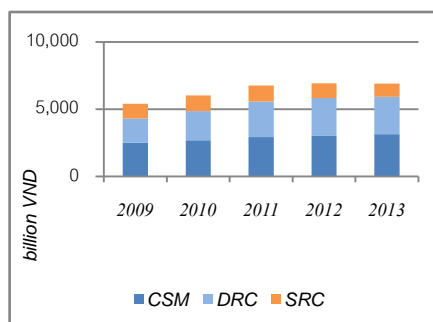
Investment recommendation: CSM has pretty good basic indicators, high dividend (expected 23% in 2013); If the consumption of radial tire products goes well, the company will grow well in the long term. We recommend buying CSM share with the 12 months target price of 43,500 dong, up 13.28% over the current price.

Financial information	2011	2012	2013	Q1/2014 (TTM)
Net revenue (Bil. VND)	2,924	3,044	3,134	3,117
% y-o-y		4.10%	2.96%	-0.55%
Total asset (Bil. VND)	1523	1847	2921	3069
Shareholder equity (Bil.VND)	619	967	1218	1297
Charter Capital (Bil. VND)	422	585	673	673
No.outstanding shares (Mil. Shares)	58.52	42.25	67.30	67.30
Profit after tax (Bil. VND)	39.26	253.88	360.07	370.54
% y-o-y		546.61%	41.82%	2.91%
EPS end of period (VND/share)	671	5266	5856	5506
Book value (VND/share)	10.577	22.882	18.105	19.272
Gross margin (%)	8.98%	23.23%	26.72%	27.06%
ROS	1.34%	8.34%	11.49%	11.89%
ROE	6.07%	32.02%	32.95%	29.46%
ROA	2.90%	15.07%	15.10%	12.37%

(Sources: CSM)

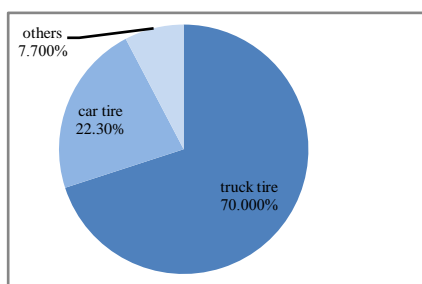
SECTOR OUTLOOK

Revenue of CSM, DRC, SRC



(Sources: CSM, DRC, SRC)

Imports breakdown



(Sources: ITC, Vietnam Rubber Association, Vietnam rubber market news- April 2013 edition)

Vietnam's tire exports 2006-2012 (bil USD)



(Sources: ITC, Vietnam Rubber Association, Vietnam rubber market news- April 2013 edition)

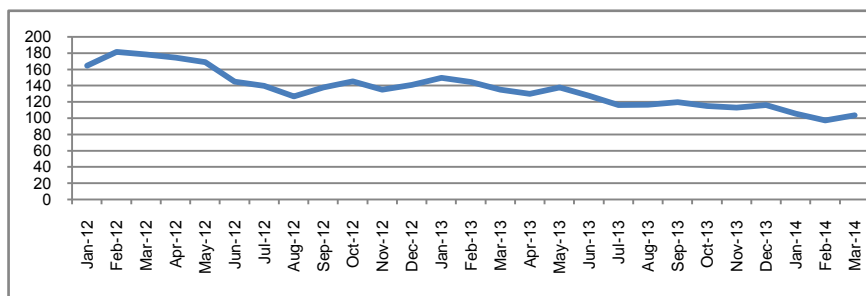
Stable domestic market thanks to the demand for replacement: Vietnam tire market has a considerably small scale of about VND 16,800 billion. In particular, 94% of annual sales come from the needs of replacing products. The potential growth of the market is not high due to the tire demand for bikes and motorcycles saturated; the growth auto tire segment is good but the sales are low, auto tire production can only meet 30-40% of the domestic demand.

The potential domestic market for radial tires: Compared with Bias tires, Radial tires have superior properties such as 2-fold increase in durability, reducing fuel consumption from 12% to 16%, low heat, fast heat dissipation,... and especially suitable for cars running at high speed. In developed countries, Radial tires account for over 90% of total tire market; in the developing countries, this figure is 60%. However, in Viet Nam this ratio is pretty low, only about 10%, in which 90% of radial tires are imported.

Potential growth thanks to boosting exports: According to a report by Freedonia Group and Pirelli, the tire demand worldwide will grow by an average rate of 4.7% / year to reach 3.3 billion units by 2015. Vietnam has advantages in natural rubber, cheap labor, tire export tax of 0% which is lower than the rate of 8% in the world's largest tire-exporting country - China. However, the export market is currently dominated by FDI enterprises; three companies SRC, CSM and DRC accounted for only 12.8% export market. It is estimated that output and export revenues of the DRC and CSM will increase after radial tire factory going into operation.

Natural rubber prices which continue to decline brings cost advantages for tire businesses: raw rubber materials accounted for 85% of the CSM's material structure. In 2013, natural rubber prices decreased 16.7% compared to 2012; in quarter 1/2014 it continued to fall 10.83% from the level at the end of 2013. In quarter 1/2014, gross margins of CSM and DRC achieved 27.06% and 25.94% respectively, which are higher than the rates at the end of 2013 (26.72%, 25.57%).

Spot price movement of rubber RSS3



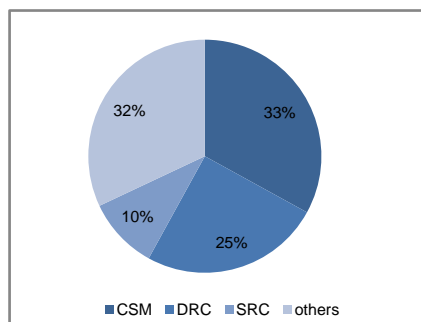
(Sources: Index Mudi, WB)

Heavy dependence on imported raw materials: In addition to natural rubber, Vietnam has to import most of the remaining materials (about 65%). Therefore, the domestic companies are strongly influenced by the price volatility of raw materials over the world and exchange rate risks.

The TPP agreement if achieved will not only support export activities but also increase competition in the domestic market: In terms of value, Vietnam mainly exports tires to the U.S. (23%), Malaysia (8%) while most imported from Thailand (44%), Japan (17%) and China (12%). If the TPP agreement is signed, import and export tax rates will gradually approach 0%; hence improve exports, especially to the U.S. and Malaysia. Meanwhile, the import duty in Vietnam will also reduce from 10-25% to 0%, thus the supply of imported tires will also increase.

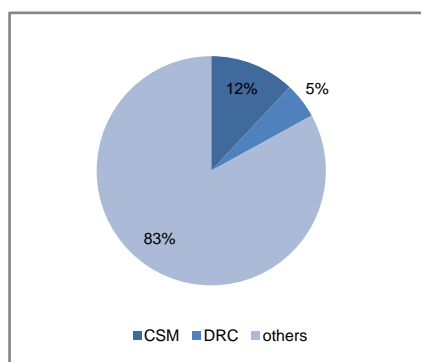
CORE BUSINESS OPERATION

Domestic market share



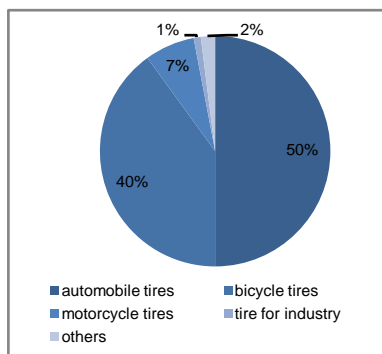
(Source: CSM)

Market share for exports



(Source: CSM)

CSM Revenue Breakdown in 2013



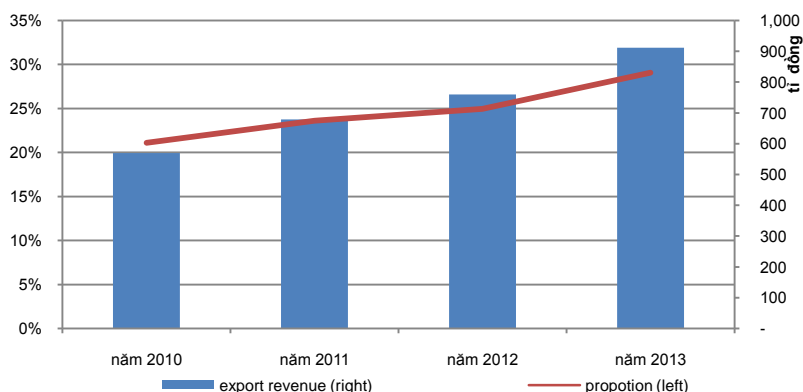
(Sources: CSM, BSC)

Material breakdown 2012

CSM is now the leading producer in Vietnam tire market. CSM accounts for 33% of domestic market and 12% of export market, being the biggest tire company in Vietnam. In particular, CSM is superior in auto tires segment (25% market share) and motorcycles tires segment (35% market share). In the segment of truck tires, CSM comes in the second place, after DRC, with 8% market share.

Revenue breakdown: Sales of auto tires occupies the largest proportion in the revenue structure of the CSM (about 50%), followed by motorcycles tires with 40% and bicycle tires 7%. In 2013, sales of auto and motorcycle tires increased by 16% and 13% respectively.

Revenue and Exports proportion 2010-2013

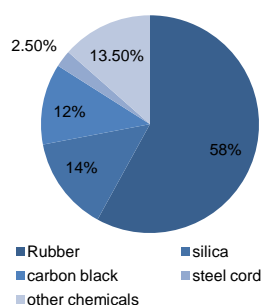


(Sources: Index Mudi, WB)

The growth momentum in the medium and long term comes from steel radial tires factory: Demand for bicycle tires, motorcycle slightly decreased; and that for auto tires has a relatively high growth rate but not sustainable due to the trend of switching to radial tires. Radial tire factory with a total capacity of 1 million tires per year is expected to help CSM to regain its growth momentum with the sales of 5,000 billion per year. However, because new factory is under construction and testing time as well as needs to obtain quality certifications which are required for exporting, we believe that the Radial project will not contribute much in the company's total revenue and profits in the coming year.

Boosting exports: in 2013, while the CSM's domestic sales fell 1%, the export revenues increased by 20% compared to that of 2012. The proportion of exports in revenue increased from 24.98% in 2012 to 29.09% in 2013. CSM products are currently exported to 36 countries and territories in which, Asian markets account for 75%. CSM anticipated that in 2018 exporting will contribute 35% of its revenue, and 60% of the radial tire will be exported.

Distribution Network: CSM has the largest number of primary distributions among the listed companies (over 200 agents). The distribution network extends from the North to the South. The revenue is mainly attributed to the southern market. The company also has numerous supplying agreements with institutional clients such as: Continental (Germany), Continental Simetire (Thailand) and Truong Hai Auto...



(Source: CSM)

Divestment in non-core business: in 2013, the company divested in Phuoc Hoa Rubber. The company will probably divest in Carbon Philip (8%) by 2014, transfer the project number 9 Nguyen Khoai and 504 Tan Thuan Nguyen Tat Thanh Vietnam, and discontinue the existing project in Hiep Binh Chanh, Thu Duc District, Ho Chi Minh City; lot number 5 Kha Van Can Street, Hiep Binh Chanh Ward, Thu Duc District, Ho Chi Minh City; land at 146 Nguyen Schedule, Ward 2, District 5, Ho Chi Minh City. Divesting projects No. 9 Nguyen Khoai and No. 504 Nguyen Tat Thanh is anticipated to generate the profit of around VND 70-80 billion to the company.

Investment risk:

- **Competitive Risk:** We assessed this risk might be not high. CSM products do not compete directly with domestic enterprises and foreign companies that already have factories in Vietnam due to differences in product segments and target markets. In term of competition with imports, CSM products have price advantages (due to the exporters to Vietnam within and without AFTA have the import duties of 10% and 25% respectively) and a good warranty. However, the level of competition may increase if the TPP agreement is signed and increasing competition with imported products from China.
- **Risk of rising raw material prices:** Input materials make up the majority of the cost of goods sold. In 2014, the price of raw rubber (58% of raw material costs) is projected to continue to bring low cost advantages for CSM.
- **Exchange rate risk:** Except for natural rubber, CSM has to import most of raw materials and equipments for Radial factory. The company has debts of more than US\$ 24 million. Besides, exports accounted for approximately 30% of the company's revenue. Therefore, exchange rate fluctuations have a direct impact on revenue and profit of CSM.
- **Interest rate risk:** CSM has a large percentage of debt (accounting for 43.71% of total capital). In 2014, State Bank plans to reduce interest rates by 1-2% in order to lessen companies' interest burden.

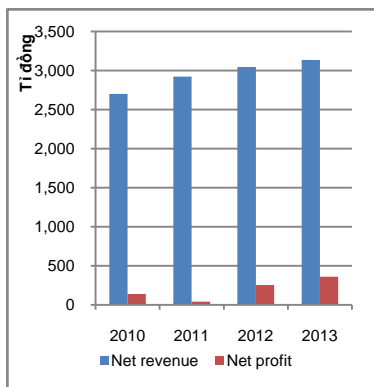
Performance in Q1/2014. Continuously decline in rubber price along with the cost savings of financial and business management expenses (10 billion) have supported business outcomes in Q1/2014. Profit after tax was VND 78.52 billion which increases 14.42% q-o-q while net sales fell slightly by 2.45% (to 684.30 billion). In 2014, we expect the company's revenue will increase by 3.77%, reaching VND 3,252 billion, of which, radial tire factory contributes about \$ 100 billion (approximately 3.67%).

Evaluating business results in 2014. According to our assessment, in 2014, the company continues to benefit from the low price of rubber. However, net profit margins may decrease (from 11.49% to 10.34% in 2014) due to increases in depreciation expense and interest expense. In 2014, the company sets targets for revenue and profit before tax of VND 3.350 billion (up 6.7%) and VND 300 billion (down 37.63%) respectively. We expect the company will obtain the revenue and profit after tax of VND 3,252 billion respectively, up 3.77% and 336 billion, down 6.63% (equivalent to EPS of VND 4,996).

FINANCIAL ANALYSIS

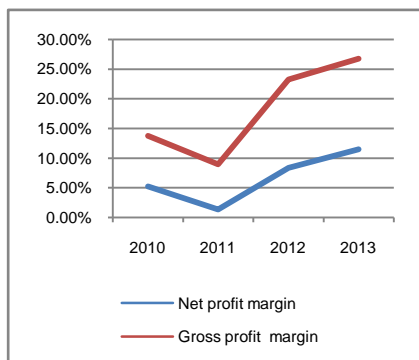
Revenue and net income

2010-2013



(Sources: CSM)

Net and Gross Profit margin 2010-2013



(Source: CSM)

Evaluating the company's growth. CSM's revenue growth has slowed. In 2013, revenue increased by only 2.96% compared to 2012, reaching VND 3,134 billion. Operating profit and profit after tax increased significantly by 41.91% and 41.82% respectively since rubber prices fell sharply (approximately 16.7%) and financial revenue increase strongly (nearly 7 -fold to VND 45 billion) while interest expense decreased rapidly (by nearly 2 times to VND 40 billion). Q1/2014, the company continues to benefit from strong fall in rubber price. Long-term assets and debts increased considerably since the company invested in new radial factory.

Capital and asset structure:

- **The proportion of long-term assets is high and increases significantly.**

Long term assets in 2013 went up by 195.53% compared to that of 2012 due to the investment in the new factory.

- **Increase in debts:** debts increased by 130.34% from the end of 2012 to the end of Q1/2014. The proportion of debt in total capital rose from 0.6 times in 2012 to 1.03 times in 2013. In Q1/2014 due to the new plant is about 70% funded by debt capital.

Indicators of insolvency: increase slightly and are higher than its peers.

Indicators of operational capacity: Days of inventory on hand went up since the company increased the storage of low-cost raw materials.

Indicator of profitability: Indicators of profitability have been improved.

- **Gross profit margin increased:** from 23.23% in 2012 to 26.72% in 2013 and 27.06% in Q1/2014 due to the plummet in raw rubber prices.
- **Net profit margin, operating profit margin increased significantly** from 10.96% and 8.34% in 2012 to 15.55% and 11.89% in Q1/2014.

Basic Indicators	CSM				DRC	SRC
	2011	2012	2013	Q1/2014 TTM		
Equity Structure						
Debt/Equity	1.21	0.60	1.03	1.03	0.99	0.42
Total Asset/Equity	2.46	1.91	2.40	2.37	2.21	1.69
Asset Structure						
Long-term Asset/Total Asset	30.42%	28.86%	49.81%	51.32%	58.34%	22.76%
Short-term Asset/Total Asset	69.58%	71.14%	50.19%	48.68%	41.66%	77.24%
Solvency						
Quick ratio	0.47	0.71	0.68	0.78	0.50	0.65
Current ratio	1.41	1.95	1.74	1.75	1.56	2.03
Activity (days)						
Days Sales Outstanding	31.08	35.33	37.72	39.66	39.82	181.07
Days Inventory Outstanding	78.64	119.05	135.73	125.71	142.06	599.70
Days Payable Outstanding	14.12	22.58	44.26	41.65	31.32	74.24
Profitability (%)						
Gross Profit Margin	8.98%	23.23%	26.72%	27.06%	25.94%	19.29%
ROS	1.34%	8.34%	11.49%	11.89%	13.35%	8.68%
ROE	6.07%	32.02%	32.95%	29.46%	30.62%	21.42%
ROA	2.90%	15.07%	15.10%	12.37%	14.35%	12.37%

Nguồn: BSC tổng hợp

INVESTMENT RECOMMENDATION

I. VALUATION

The report used P/E method to evaluate CSM's share.

Method P/E. To conduct the valuation of CSM shares, we selected companies in the tire industry that have some similar basic elements with CSM such as:

- Revenue for the latest quarter fluctuates around VND 1500-4500 billion
- The core business activity is production of tires for auto, truck and agricultural machines.
- There are radial tire factories currently in operation or planned to be in operation in the near future.

Then:

- The P/E ratio is 8.7
- Expected EPS is VND 4,996

Under this method, the fair price of CSM is VND 43,465

Investment view: CSM has pretty good basic indicators, high dividend (expected to be 23% in 2013); if the consumption of radial tire products is good, it will offer a good growth prospect in the long term for the company. In addition, divestment in 2014 is projected to offer financial income for the company. We recommend buying CSM shares with expected price in the next 12 months is VND 43,500, up 13.28% over the current price.

Company	Market	Revenue (TTM) (bil VND)	Total assets	P/E	P/B	ROE (%)	ROA (%)
Southern Rubber Industry JSC	Việt Nam	3,177	3195	7.37	2.18	29.46%	12.37%
Xiamen Sunrise Wheel Group-A	Trung Quốc	4,183	8,940	8,940	47.94	2.99%	1.48%
Falcon Tires Ltd	Ấn Độ	3,889	4,469	4,469	-	-22.64%	-5.25%
Good year Indonesia PT	Trung Quốc	3,875	2,361	2,361	23.92	9.92%	4.56%
Shandong Himile Mechanical- A	Trung Quốc	3,838	8,599	8,599	27.80	14.72%	13.68%
Cia Goodyear Del Peru-invest	Peru	3,529	4,129	4,129	4.17	11.43%	8.78%
Danang Rubber	Việt Nam	2,869	3188	3188	9.62	29.363	13.211
Goodyear Thailand	Thái Lan	2,470	2,886	2,886	10.89	9.41%	7.38%
General Tire & Rubber Co	Pakistan	1,873	1,214	1,214	10.88	24.34%	6.01%

(Source: Bloomberg, BSC)

BSC RATING SYSTEM AND VALUATION METHODOLOGY

Rating System: Our recommendations are relative to the market development and are based on the difference between the current price and our 12-month price target includes dividends over the period (Unless otherwise specified). This structure applies from 1st Jan 2014.

Valuation Methodology: The selection of methods depends on the industry, the company, the stock. Our valuations are based on a single or a combination of one of the following valuation methods: 1) Relative models (P/E, P/B, EV/EBIT, EV/EBITDA); 2) Discount models (DCF, DVMA, DDM); 3) Asset-based evaluation methods (NAV, RNAV).

Rating System	Note
STRONG BUY	If the target price is 20% higher than the market price
BUY	If the target price is 5% to 20% higher than the market price
HOLD	If the target price is 5% higher or lower than the market price
SELL	If the target price is more than 5% lower than the market price
NOT RATED	The investment rating and target price have been removed pursuant to BSC policy when BSC is acting in an advisory capacity, in a merger or strategic transaction involving this company, and in case BSC do not have enough material to perform valuation.

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