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Continuous improvement in rubber production results

Rubber stocks had a strong bullish period in the beginning of 2017, before a sharp increase in the global rubber price. Rubber sector is currently trading at average P/E trailing of approximately 15x (excluding bonus and welfare fund).

The global rubber price fluctuated in 2M2017. Rubber price climbed by 70% yoy and then decreased by 20% in the last 2 week. Based on 2010-2015 statistics, the rubber price could maintain downward trend toward year-end and closed the year at the price of approximately 60 - 80% of the price at the beginning of the year.

BSC noted that short-term rubber price development can hardly affect business results of rubber companies due to uptapping season; and sale output, from now until May, only accounts for about 10% of annual output.

Vietnam Rubber Group sets 2017 plan of VND 35 million/ton ASP and VND 30 million/ton of average cost. BSC believes the planned ASP was conservative, expects ASP will range between VND 42-44 million/ton, based on the rubber price development statistic during the 2011-2015 period.

Updates on listed companies

TRC – BUY – 38,000 VND/share (upside 20.2%)

With the assumed ASP of VND 40 million/ton, BSC expect profits from rubber production to surge by 104% to VND 64.6 billion, and the PAT to be VND 102.3 billion (+46.7% yoy), corresponding to 2017 EPS of 2,823 VND (excluding welfare and bonus fund). P/E forward is currently at 11.2x

DPR – BUY – 48,800 VND/share (+upside 11%):

With ASP assumed at VND 40 million/ton, BSC expects profit from rubber operations to reach VND 120 billion (+150% yoy), and PAT of the parent company in 2017 to be VND 201.5 billion (+26.7%), with a respective EPS of 3,523 VND/share in 2017 and a P/E forward of 13x.

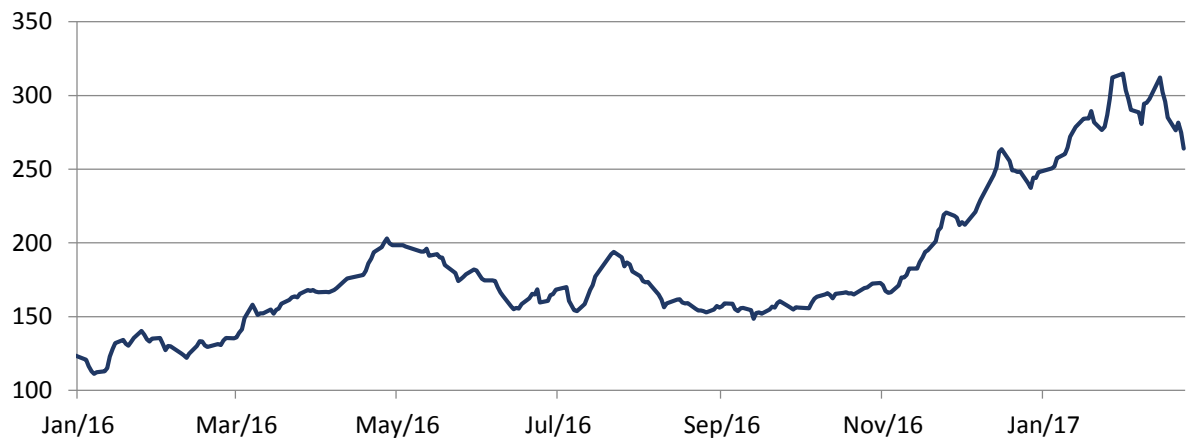
PHR – HOLD - 31,000 VND /share (upside 4.4%)

With ASP assumed at VND 40 million/ton, BSC forecasts PAT of PHR can be VND 228 billion (+5% yoy), leading to 2017 EPS of 2,249 VND and a P/E forward of 13.8x. PHR should not yield a strong growth in profits due to (1) Cultivation output is reduced by 15% due to reduction in cultivation area; (2) Profit from Industrial Zone transfer decreased from VND 106 billion (2016) to VND 20 billion.

World Rubber Price Update

Strong movement in the beginning of 2017: Thailand RSS3 rubber price changed sharply in the first two months of 2017 increased rapidly up to 314.9 JPY/ton at the end of January 2017 amid the news of floods in Thailand, and after a strong movement with a margin of 20 to 30 JPY in the first half of February. Since February 14th, the rubber price decreased sharply by 20% and it is trading at 254 JPY/ton, due to (1) Thailand declared to use its national reserve fund to meet the export demands (2) In India, rubber-tire producers cut down production because of a strong surge in rubber price.

Thailand rubber price development- RSS3 2011-2017

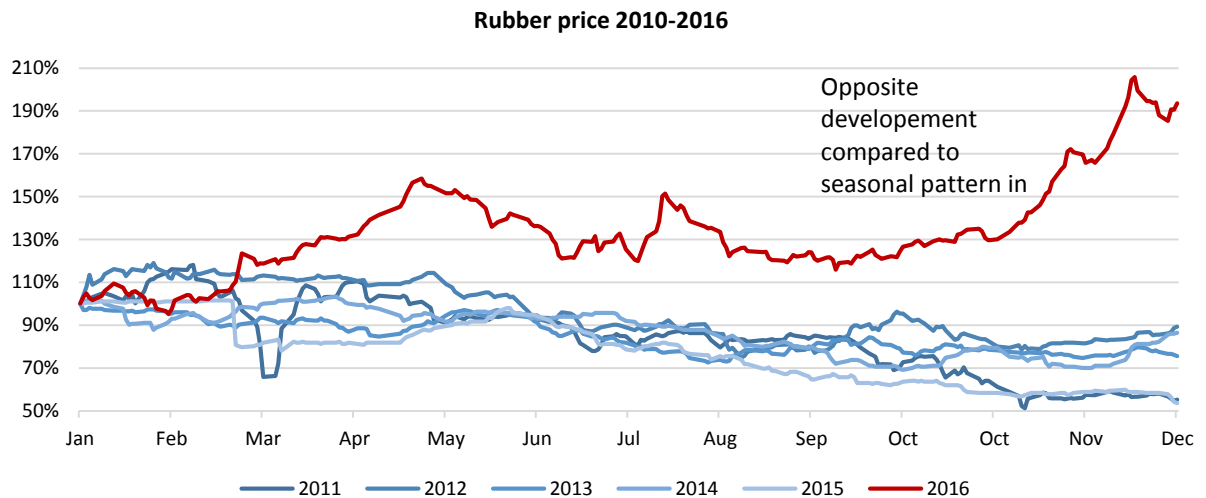


Thailand rubber price development - RSS3 2011-2017

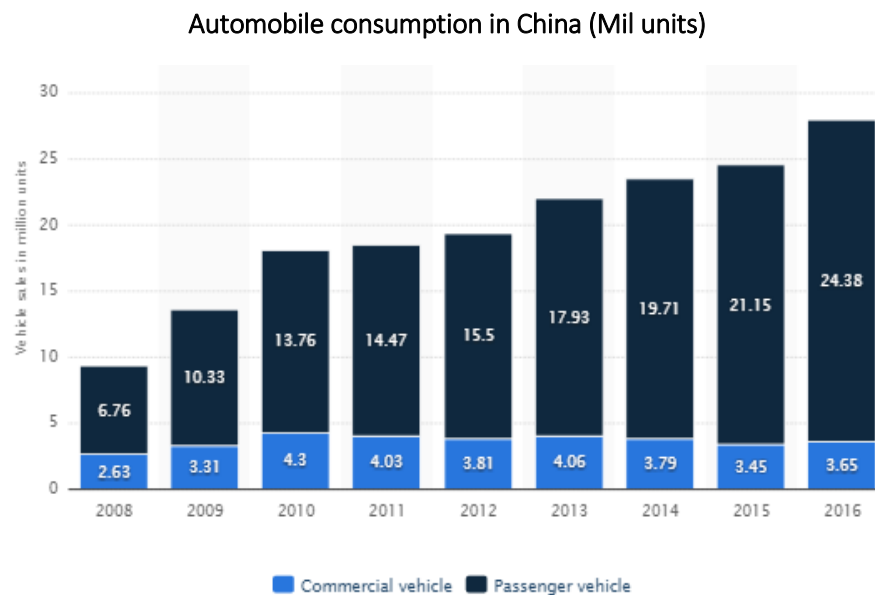


Rubber price rally has a cyclical effect. On rubber prices movements over the 2010-2015 period, which was the time of a rubber supply surplus, rubber followed uptrend over the first quarter, with growth rate of about 20% compared to the year beginning price, before gradually adjusting downward over the crop season (May – Dec). During 2010-2015, rubber prices often ended the year at the level equal to 60-80% of the beginning price. In 2017, rubber prices reached a peak of JPY 314.9, a 25% increase compared to the beginning of the year, which is unusually higher than its historical pattern, leading to an expectation

that rubber prices could be maintained at a high level over this year. Using the trend from 2011 to 2015 for 2017 forecast, we believe rubber prices could reach 200 – 220 JPY/ton by the end of the year.



We note that in 2016 the rubber price had opposite movement compared to cyclical pattern in 2016, but expects 2016 was an outlier. Rubber prices surged by more than 100% in 2H2016. This sharp rise was partly caused by the strong growth in automobile sales volume of China of 13.7% in 2016, under the impact of the tax cuts. Specifically, the automobile consumption tax in China felt from 10% to 5%, effective from the end of 2015. Automobile consumption has direct impact to the tires sector, and thereby to demand for rubber. From 01/01/2017, automobile consumption tax rose to 7.5% in China, and will return to the old level of 10% from 2018. As a result, BSC believes rubber prices will not be able to repeat the trend of year-end 2016 .



Domestic rubber price doubled compared to same period last year. The floor price stated by VRG was at VND 52-59 million per ton, which is twice as much as in Feb 2016 (about VND 28-30 million per ton). The floor price has adjusted since mid February 2017, under the effect of global rubber price.

We suggest that investors should pay attention to rubber price over a longer time frame (the second half of the year) instead of 1 -2 months ahead. Because domestic rubber price usually lags by 2-3 months compared to the global rubber price, which explains the current domestic price has not decreased significantly. In addition, rubber companies is to enter uptapping season as of the end of Feb. Therefore, the short-term fluctuation in rubber price will not directly affect the rubber companies' business performance. Rubber companies will return to tapping in April - May and the rubber quantity will increases gradually toward year-end.

The Vietnam Rubber Group applied a 2017's projection price of VND 35 million/ton for its subsidies. This level is equivalent to 60% of the current rubber prices, and BSC believes that this price level is conservative. Speaking with the group representatives, the expected average prices could be around VND 38 – 40 million. According to the historical trend of the global rubber prices, we believe rubber price at year-end could reach VND 40 – 44 million, corresponding to an average rubber prices in this year of VND 41 – 42 million.

Update for listed rubber companies.

Rubber stocks experienced a strong gain at the beginning of 2017 thanks to the rally of global rubber price. The domestic rubber price followed the fluctuation of the global rubber price, bringing the expectation of strong growth in business result. However, we note that rubber price should be carefully followed when as the tapping season upfold (from the 3rd quarter). The shares are currently traded at average trailing P/E of 15x (the effect of bonus and welfare fund is excluded)

TRC_ Tay Ninh Rubber JSC_ BUY

With the assumed ASP of VND 40 million/ton, BSC expect profits from rubber production to surge by 104% to VND 64.6 billion, and the PAT to be VND 102.3 billion (+46.7% yoy), corresponding to 2017 EPS of 2,823 VND (excluding welfare and bonus fund). On February 24th 2017, TRC share was traded at the price of VND 31,600 per share, P/E forward is currently at 11.2x and P/B of 0.62x

2016 business result update_ Strong rally coming from core operation.

In 2016, Tay Ninh Rubber JSC recorded VND 350.3 billion in net sales (-3.5%) and VND 82.1 billion in PBT (+25.5% YoY). The profit growth is considerably contributed from the rubber utilization, implying VND 31.6 billion (+20.4% YoY) and a 37.3% decrease in general & administration expense since 2016 recorded abnormal retirement subsidy as the year 2015. In 2016, the firm harvested 9,050 tons (-10% YoY) due to the decline of utilization area (-1.5%) and the El-nino reducing productivity to 1.92 tons per ha. Liquidating rubber trees contributed more than half of income, equal to VND 35 billion.

Bonus and welfare fund for 2016 was 20% of PAT for parent company. 2016 EPS of the firm got VND 1,930 per share, current trailing P/E of 16.3x that is higher than the sector's average one.

2017 prospect– Strong increase in rubber production.

The firm planned that 2017 rubber output of 8,800 tons (-2.8% YoY) due to rubber area liquidation is expected to go down by 2.2% whereas productivity planned is kept constant at 1.91 tons per ha. Net profit per ton is expected to reach VND 6 million (VND 35 million in price and VND 29 million in cost), which is double from 2016 average level of VND 3.5 million. Besides, the firm could continue to liquidate about 538 ha of rubber in 2017, implying the profit of VND 53 billion (+39% YoY).

TRC investment in Tay Ninh – Siem Reap project in Cambodia will be approximately VND 175 billion in 2017. Currently, rubber trees plantation is basically completed and factory construction is to be built in 2018 before tapping in 2019. The plant will manufacture RSS3 with the capacity of 10,000 tons, approximate investment cost is VND 50 billion.

In 1Q2017, TRC's EBT of rubber utilization activity is estimated to reach VND 18 billion (1Q2016 recorded loss). Total profit from liquidating rubber trees is planned to be recorded in 1H2017. TRC set plan for PBT of parent company of VND 107.4 billion (+38.7% YoY).

BSC's recommendation – BUY – VND 38.000 (upside 20.2%)

In [the TRC initiation Report](#) and [Rubber Sector Update](#), BSC stated that TRC will be have the most benefit from recovery of rubber price due to fundamental elements and the specialized in rubber-related area. Thus, BSC expects TRC to reach the strongest growth in 2017 with expectation of rubber price recovery.

We expected that the more favorable weather in 2017 could help to bring productivity of TRC back to 2 tons per ha, equivalent to 9,230 tons output(+1.9% YoY). With the assumed ASP of VND 40 million/ton, BSC expect profits from rubber production to surge by 104% to VND 64.6 billion, and the PAT to be VND 102.3 billion (+46.7% yoy), corresponding to 2017 EPS of 2,823 VND (excluding welfare and bonus fund of 20% NPAT). Therefore, we grant a BUY recommendation for TRC with the target price of VND 38.000 per share (upside 20.2%).

DPR _ Dong Phu Rubber Joint Stock Company_BUY – upside 11%

With ASP assumed at VND 40 million/ton, BSC expects profit from rubber operations to reach VND 120 billion (+150% yoy), and PAT of the parent company in 2017 to be VND 201.5 billion (+ 26.7%), with a respective EPS of 3,523 VND/share in 2017. On February 24, 2017, DPR shares were traded at VND 44,000 per share, equivalent to P/E forward of 13x, and P/B of 0.88x (Bonus & welfare funds over 50 billion VND was excluded from 2016 EPS calculation).

2016 Business result update – Successfully bottomed out at year-end.

Revenue of Dong Phu Rubber was VND 852 billion (-1%) and its PBT was VND 196.6 billion (+1% yoy), with rubber sales output of 17,232 tons (-7.5%). The drop in output was caused by a 40% drop in quantity of latex bought from small rubber tree farms. Average rubber price in 2016 was VND 32.5 million (+4.6%) and net operating profit from rubber production was 2.5 times higher and reached VND 46.4 billion thanks to cost cutting solutions. However financial profit felt sharply by 20% resulted in the same net profit before tax compared to that period of the previous year.

The level of bonus and welfare funds in 2016 was planned at the amount of 3-month salary, correspondingly over VND 50 billion. Accordingly, 2016 EPS of DPR is expected to be VND 2,550 per share (excluding 50 Bil of bonus and welfare funds).

Q1/2017 update – Rubber price doubled.

Company's tapping activity has stopped since rubber trees enters leaf changing period for two months and will return to tapping in April-May. Instead of keeping a large stock of inventory, the company only holds sufficient stocks for long-term contracts from now till April.

In January 2017, the company produced 900 tons rubber with an ASP of VND 45 million (+70% yoy). As a result of higher selling price, net profit from rubber production will significantly improve in 1Q2017 (VND 13.5 billion in January compared to the level of VND 2 billion of 1Q2016). However, liquidation income may be lower than that in 1Q2016, leading to the lower net profit in 1Q2017. However, this year total liquidation income is similar to that of 2016.

2017 prospect – Rubber profit margin will improve.

In 2017, rubber output is expected to stay flat, because (1) The company continues to maintain D4 tapping policy in 2017, (2) The rubber liquidation area is greater than newly planted area, where productivity is still low, leading to lower average productivity. Therefore the company set productivity target at 1.9 tons/ha.

In 2017, 1000 ha will begin tapped at Kratie – Cambodia. However, due to low productivity, DPR expects this project could only break-even in 2017. At the same time, RSS3 factory will be built and operate since August 2017 with a capacity of 3,000 per month. The project is expected to operate in 4Q2017.

The 2017 profit plan will increase slightly compared to 2016 because the profitability decrease from financial activities and liquidation income, which offset the growth in rubber production profit.

- The company is expected to sell 460 ha in 2017 compared to 500 ha in 2016. Rubber wood price will increase since higher rubber price will lower the number of rubber tree cut down. Rubber liquidation price is expected to be VND 150 million per hecta, bringing a VND 70 billion net profit, which is slightly lower than that of 2016 (VND 79 billion).
- Financial profit is forecasted to be lower since dividend was highly-paid out in cash in 2016, lowering the amount of deposited cash.

BSC recommendation – BUY – target price of 48,800 VND (upside 11%)

With the average rubber price of VND 40 million per ton, our projection for rubber production is about VND 120 billion (+150% yoy). 2017 parent company's profit after tax will be VND 201.5 billion (+26.7% yoy). The 2017 EPS is sure to be VND 3,523 per share (after the exclusion of Bonus and welfare funds in 2016). P/E forward for DPR is 12.6x. Our suggestion is BUY at the price of 48,800 per share (upside 11%) according to the assumed average sale price of VND 40 billion per ton.

PHR _ Phuoc Hoa Rubber Joint Stock Company _ HOLD

With ASP assumed at VND 40 million/ton, BSC forecasts PAT of PHR can be VND 228 billion (+5% yoy), leading to 2017 EPS of 2,249 VND. On February 24, 2017, PHR was traded at VND 29,400 per share, equivalent to P/E forward of 13.8x. PHR should not yield a strong growth in profits due to (1) Cultivation output is reduced by 15% due to reduction in cultivation area; (2) Profit from Industrial Zone transfer decreased from VND 106 billion (2016) to VND 20 billion.

Updates on 2016's business result – Extraordinary gains from industrial zone compensation

Phuoc Hoa Rubber Jsc. recorded revenues of VND 1179 billion (-4%) and EBT of VND 253 billion (-4.1% yoy). In which, profit was composed of VND 106 billion of abnormal gains thanks to land compensation for the industrial zone, and around VND 100 billion of profit from liquidation. During this year, the total production was 16,406 thousand ton (-10.6% yoy), due to lower tapping area, while productivity remained stable at 2 ha/ton. Average selling prices reached 30.7 million ton (+0.6 yoy), as the product structure moved from CV50,60 to SVR 3L, with lower selling prices.

The 2016's allocation to bonus fund was planned to be at 20% of EAT, which is equivalent to VND 43 billion. Accordingly, EPS 2016 of PHR is estimated to be VND 2,125 per share, adjusted for bonus fund allocation.

2017 outlook – Strong growth from rubber production

PHR expects to record 4,500 ton as production output over Q1/2017, with an average selling price of VND 42 million (+57% yoy). Accordingly, profit from rubber production in Q1 is estimated to be VND 45 billion, considerably higher than approximately VND 5 billion in 2016.

PHR expect to have 14 thousand ton of rubber output in 2017 (-15% yoy). The high liquidation of aged rubber reduced output area, despite an improvement in productivity compared to same period of last year. A significant drop in harvested output forces the company to become dependent on trading rubber, of around 16 thousand ton. Additionally, as the purchase prices from farmers will follow closely the rubber market price, leading to profit margins from purchased rubber will be only at VND 1-3 million/ton, as compared to profit range of 5-7 million/ton for harvested rubber.

PHR will continue to liquidate approximately 1,000 ha of rubber farm in 2017, corresponding to a gain of VND 100 billion, which is lower than 2016 of VND of 140 billion. At the same time, PHR expects to record VND 20 Bil of Industrial Zone land transfer in 2017 (as compared to VND 106 billion in 2016).

In 2017, Phuoc Hoa will also invest in the construction of a RSS3 rubber sheets plant with a capacity of 3,000 ton. However, this plant will not generate any profit in 2017.

BSC's view – HOLD – fair price VND 31,000 per share (4.4% upside)

The Company estimated the EBT of the parent company to reach approximately VND 200 billion in 2017, a significant drop compared to VND 256 billion in 2016, under the assumptions that the average prices will be VND 35 million and the cost prices will be VND 30 million. However, with an expectation that the rubber prices will be at VND 40 million/ton, BSC believes that PHR's EBT could reach VND 269 billion (+5% yoy). With 20% of the profit allocated to bonus fund, 2017 EPS is estimated at VND 2,249, corresponding

to a P/E forward of 13.0x. BSC issues a HOLD recommendation for PHR with a fair price of VND 31,000 per share (4.4% upside).

Index – Comparison of financial ratios in 2016

	PHR	DPR	TRC
Operating ratio			
Cultivation area (ha)	8,324	7,020	4,615
2016 Output (ton/ha)	2.0	1.92	1.91
Production Capacity (ton/year)	27,000	17,000	9,000
Financial ratio			
% ST asset	32.3%	34.3%	22.4%
% LT asset	67.7%	65.7%	77.6%
% debt	23.6%	9.3%	5.9%
% equity	66.5%	90.7%	85.6%
Profit margin before tax	20.9%	23%	23.4%
ROA	6.1%	4.9%	4.3%
ROE	9.8%	6.0%	5.0%
Current ratio	1.24	1.48	2.53
Quick ratio	1.01	1.34	2.51
Financial leverage (debt / equity)	0.67	0.11	0.2
Valuation			
2016 EPS (excluding bonus & welfare)	2,125	2,550	1,930
2017 EPS– forecast	2,249	3,523	2,823
P/E forward	13.8	13.01	11.2
P/B	1.04	0.88	0.63

Disclosure

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