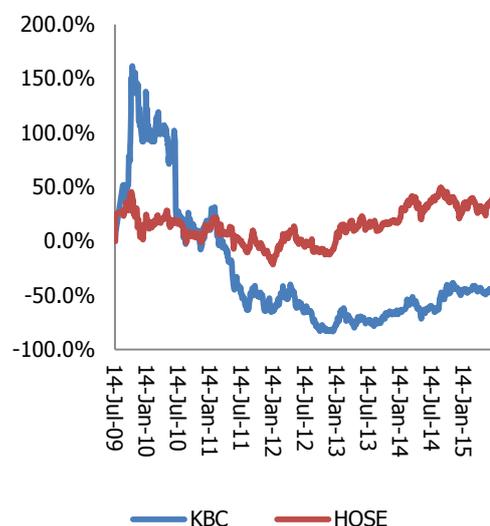


Kinh Bac City Development Share Holding Corporation - KBC

Company report

Performance since 2009



Trading information 21/07/2015

Current price (VND)	15,900
Listed shares	475,711,167
Outstanding shares	469,760,189
Market capital (VND bn)	7,422.2
Price range 52 weeks	9,900 – 18,200
Average trading volume	2,812,570
Average trading value (VND bn)	44.4
% foreign ownership	30.8%
% foreign ownership limit	49.0%
Shares available to own	230,182,493
Remaining shares available to own	85,496,354

Source: MBS research

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FORWARD UNTO DAWN

	2013	2014	2015E	2016E	2017E
Net sales	1,072.8	1,069.0	1,964.9	2,901.0	3,126.8
EBIT	396.5	592.9	896.5	1,320.7	1,515.0
Net income	78.8	312.0	536.1	866.9	1,044.6
Gross profit margin	46%	55%	51%	53%	56%
Net income margin	7%	29%	27%	30%	33%
EPS	245	823	1,176	1,902	2,292

We are initiating coverage of Kinh Bac City Development Share Holding Corporation (KBC) with a BUY rating and a 12-month price target of VND 19,400 equivalent to 20% upside. From 2015 onward, as the real estate market and Vietnamese economy in general recover, KBC will be able to exploit its low-cost land bank and grow. Further more, as demand for industrial parks rises, KBC will have a chance to expand both sales volumes and prices. Thus, KBC appears to be a sound investment at least in the medium-term.

CATALYSTS

- Economics of Vietnamese economy remain favorable, which is a good environment for real estate investment.
- The low-cost land bank is likely to help KBC outperform the real estate sector in terms of gross margins.
- Free trade agreements such as FTAs and TPP will remove barriers and encourage FDI flows to Vietnam and KBC appears to be one of the industrial park developers to benefit the most.

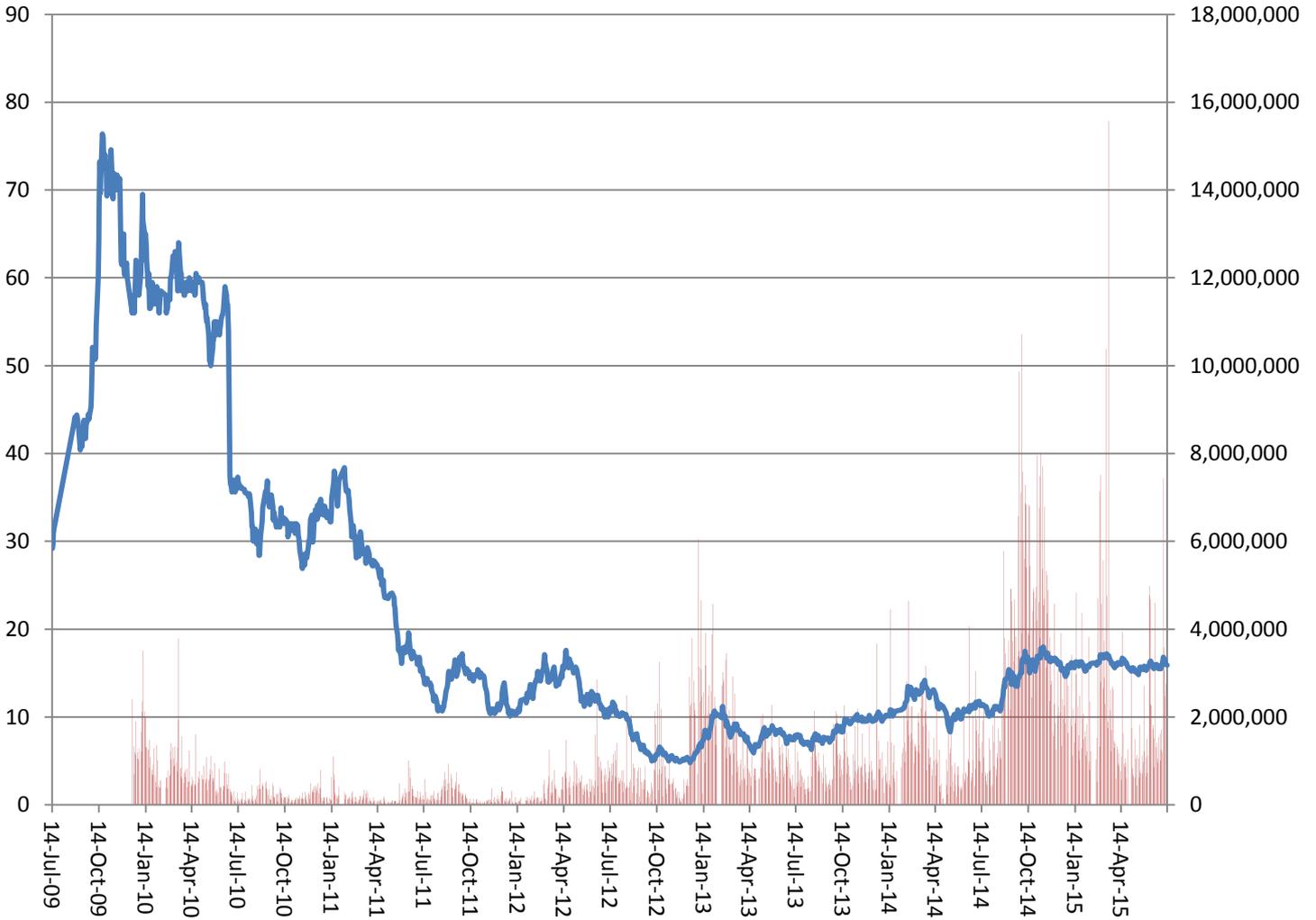
RISKS

- The negotiation stages of TPP may be extended.
- Foreign capital flows to Vietnam may not be as significant as expected. This will probably affect our projection on KBC's financial performance.
- We have not included the project to expand Trang Due IP to further 800 ha and Trang Cat due to insufficient information. This may decrease the valuation of the firm.

VALUATION

Our DCF models suggests the value of KBC stock to be approximately VND 19,400, representing a 22% upside. Our price target implies a 21.6x and 1.5x multiple of our FY 2015 EPS and BPS estimate of VND 897 and VND 13,377 respectively.

Given net sales CAGR of 42.8% and net income of 36.8%, we feel the current valuation does not reflect the growth prospect of the company. Being the domestic market leader we also believe it should trade at a premium to ITA, the only suitable comparable to KBC.

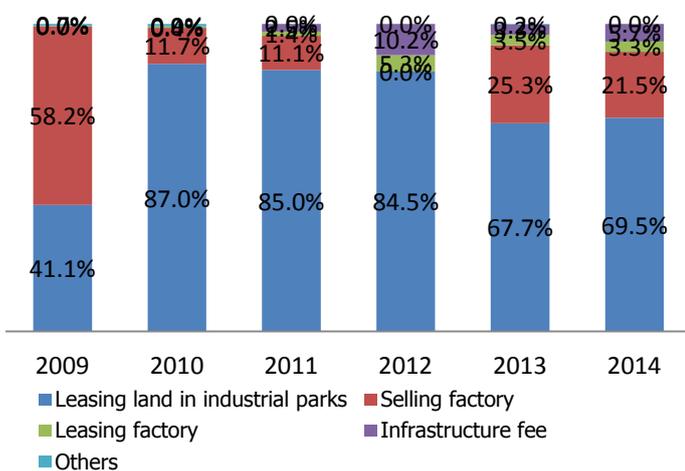


BUSINESS MODEL

KBC is a listed real estate company the business of which focuses on developing industrial parks. Although the firm does have several residential projects, most of them are to exploit the arising needs of the people working in industrial parks. Therefore, the firm’s revenue is generated mostly from services in industrial parks such as leasing land and factories.

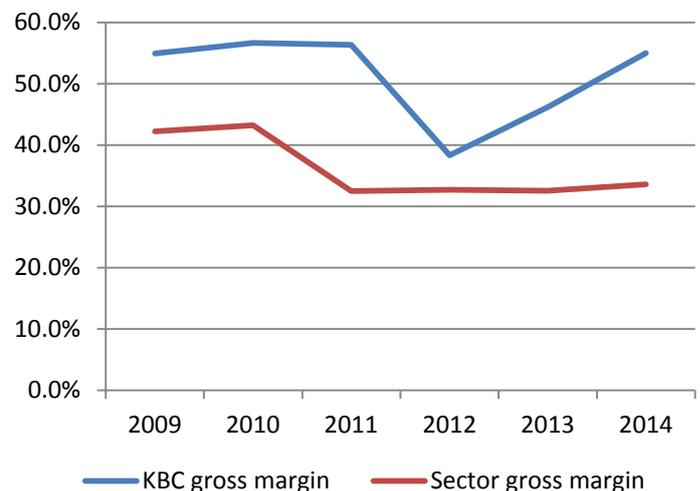
In 2014, leasing land in industrial parks accounted for about 69.5%, while sales of built-in factory contributed around 21.5% of the revenue structure. This revenue structure is likely to change with more contribution from land leasing as this business expands accordingly to the improvement in demand. In addition, built-in factories are more suitable for small companies with minimal land utilization (less than 1ha). Therefore, as the outlook of Vietnamese economy improves and global enterprises comes to Vietnam to establish their assembling factory, land leasing tends to grow faster than built-in factory sales.

Revenue breakdown



Source: KBC, MBS research

KBC vs Real Estate sector gross margin



Source: KBC, MBS research

Regarding to the firm’s profitability, KBC is earning higher gross margins than its peers. In fact, while the average gross margin of real estate sector in 2014 is about 33%, the company’s level remains at 55%. It is noteworthy that this trend to outperform has been maintained during recession periods. Its low-cost land bank is likely the key factor which helps KBC sustain this competitive advantage. In fact, the company and its affiliates is managing about 4,500 ha, of which 75% area has been compensated.

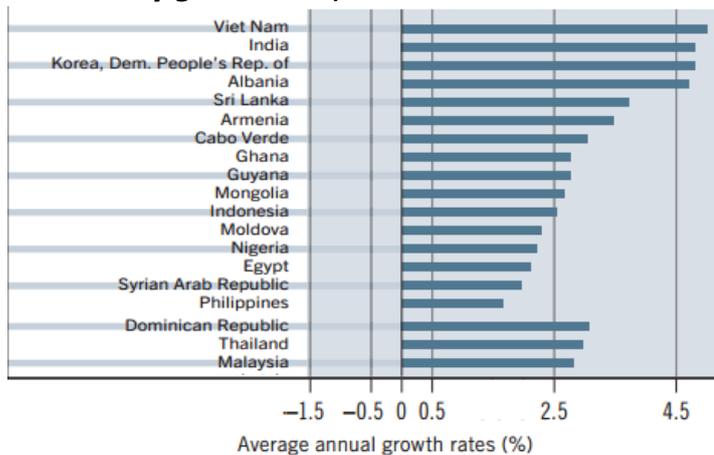
Since the time of acquisition, the cost of land in these areas has increased substantially. According to land prices listed in Decree 104/2014/NĐ-CP and Decree 188/2004/NĐ-CP, the minimum price of industrial land in Grade 2 urban areas has increased with 2004-2014 CAGR of 7.9%.

OUTLOOK

As pointed out in our industry report (June 2015), favorable performance in the Vietnamese economy is supporting growth in the real estate sector, which may help increase the value of KBC’s land bank. In fact, GDP in the first half of the year has grown 6.28%, which is higher than the target of 6.05%. This growth is likely to be sustained as the PMI is still above the 50 level over many consecutive months. In conjunction with other positive factors such as credit growth, the real estate market appears to be set to enjoy a period of significant growth in the coming years. This obviously benefits those companies which have a significant landbank similar to KBC. According to the company’s representative, the price currently applied for land compensation has increased from 2 to 4 times compared to the level that KBC used to pay in the past.

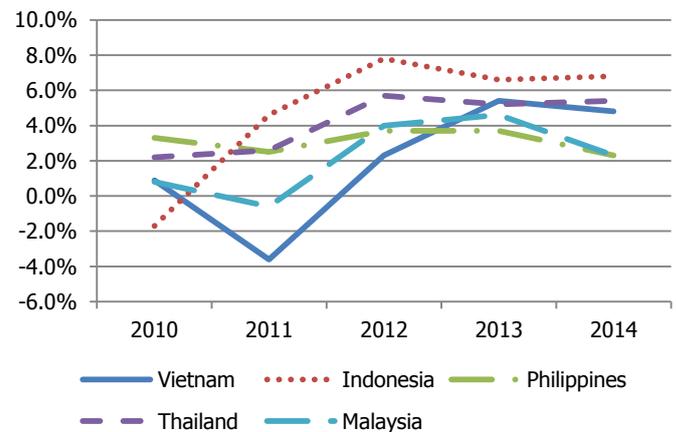
On the other hand, the favorable outlook of Vietnamese economy implies that it will remain attractive for foreign investors. This is especially important to industrial park developers (such as KBC), as the demand in this niche is influenced significantly by cash flows from foreign investment, within which FDI takes an important role. In fact, apart from the solid GDP growth mentioned above, variables such as labour productivity and interest rates remain at favorable levels. Compared to other neighboring countries, Vietnam has competitive real interest rates, while productivity growth is the highest.

Productivity growth rate, 1991 - 2013



Source: ILO, MBS research

Real interest rate by country



Source: World Bank, MBS research

In addition, free trade agreements such as FTAs to be effective from 2015 and TPP will be a significant motivation for FDI capital to flow to Vietnam. Apparently, when trade barriers are removed, the expense to establish an assembly line in Vietnam will reduce significantly. It is noteworthy that the nationality of most of KBC’s customers is Japanese or Korean. Due to political and other concerns, companies from these two countries are moving their factories out of China to a more friendly countries, including Vietnam. Therefore, KBC is likely to benefit the most from these free trade agreements. By Q1 2015, the firm had acquired several important contracts with investors from Korea such as LG and Haesung. According to the firm’s representative, in 2015 and 2016, KBC plans to transferred about 38ha to LG and 80ha to member companies of Incheon Vision Business Association. Therefore, it is likely that KBC’s financial result will have a breakthrough in the near future.

Also, as demand increases, leasing prices are likely to grow. In 2014, the industrial parks of KBC and its subsidiaries increased their leasing prices from \$60 to \$70 per sq. m. This trend is likely to continue in coming years as the company plans to increase the price to further 8-10%. This is an opportunity for the firm to increase its margin as most of its land bank has finished compensation and so COGS are unlikely to increase significantly.

Earning Model (VNDbn)	2014	2015E	2016E	2017E
Net sales	1,069.0	1,964.9	2,901.0	3,126.8
Cost of sales	(481.4)	(954.5)	(1,377.8)	(1,387.9)
Gross profit	588	1,010	1,523	1,739
<i>Gross profit margin</i>	<i>55%</i>	<i>51%</i>	<i>53%</i>	<i>56%</i>
Selling expenses	(18)	(38)	(56)	(60)
General administration expenses	(81)	(148)	(219)	(236)
Operating income/ loss	489	824	1,248	1,443
Total other income/ expenses net	104	104	104	104
Income from subsidiaries & affiliates	(1)	(32)	(32)	(32)
EBIT	592.9	896.5	1,320.7	1,515.0
Interest expense	(252)	(209)	(209)	(209)
Income before tax	341	687	1,111	1,306
Income tax expense	(49)	(151)	(245)	(261)
Deferred tax payment	20	0	0	0
Net income	312.0	536.1	866.9	1,044.6
Minority interest	14	23	38	46
Income to parent company	326	560	905	1,090
EPS (VND)	823	1,176	1,902	2,292

VALUATION

Based on our DCF model, the value of KBC stock is approximately VND 19,400, representing a 22.0% upside.

Some of our key DCF assumptions are as followed:

- Revenue to increase and peak in 2017 accordingly to the assumption that FTAs have the highest impact in 2017.
- COGS is determined by examining the the input cost of land and other related cost in the last 6 years.
- Gross margin to fluctuate accordingly to the contribution of each project to total revenue.
- D/(D+E) ratio is expected to increase gradually to the level of 50% by FY 2021

DCF Valuation

Unit: VND mn	2015E	2016E	2017E	2018E	2019E	2020E	2021E
EBIAT	717,224	1,056,548	1,211,988	1,188,788	843,181	708,949	572,914
(+) Depreciation	21,538	21,538	21,538	21,538	21,538	21,538	21,538
(-) Capital expenditures	(50,014)	(73,842)	(79,589)	(73,557)	(46,132)	(38,349)	(27,968)
(-) Increase in working capital	(1,411,508)	1,727,324	2,450,447	217,734	1,747,137	588,425	674,677
Free cash flow to the Firm	(718,759)	2,741,476	3,620,660	1,376,664	2,591,575	1,309,481	1,272,317
(+)PV Terminal value	5,330,188						
(+) Cash	149,105						
(-) Debts	(3,287,601)						
Sum PV of Free cash flow to Equity	9,252,994						
Share outstanding	475,711,167						
Implied share price (VND)	19,400						
Discounted rate	14.9%						
Beta	1.12						
Risk free rate	6.19%						
Market risk premium	11.8%						
Growth of FCFE after 2021	5%						

Source: MBS research

Relatively, the target price remains a discount to other peers (ITA is the only relevant local comparable), which are trading with PE and PB within the range of 6.9-101.6x and 0.6-9.2x respectively.

However, given that KBC is a market leader in Vietnam and has the potential to grow both from the real estate recovery as well as being a beneficiary of broader economic benefit from FTAs, KBC deserves a higher valuation. Perhaps the stock is not necessarily traded at regional peer average, at least it should be traded at 21.6x and 1.5x for PE and PB respectively to reflect its high growth potential.

Comparables

Company	Market Cap (VND)	P/E (x)	P/B (x)	Dividend yeild	EPS growth
KINH BAC CITY DEVELOPMENT SHARE HOLDING CORPORATION	7.38T	12.8	1.1	-	261.6%
TAN TAO INVESTMENT INDUSTRY CORPORATION	8.83T	29.3	0.6	15.4%	42.6%
PRAJ INDUSTRIES LTD	6.88T	26.3	3.23	1.43%	39.6%
TTCL PCL	10.99T	50.0	3.25	-	-49.7%
SHENZHEN GRANDLAND	52.45T	27.5	3.37	-	2.0%
SINO THAI ENGR & CO	22.88T	25.2	4.16	-	-12.3%
CHINA ZHONGHUA GEO	53.69T	101.6	9.15	0.17%	65.7%
AHLUWALIA CONTRACTS	5.60T	24.4	4.84	-	188.7%
ITALIAN – THAI DEVELOP	26.90T	-	3.12	-	-48.0%
EAST LAKE HIGH TECH	18.87T	20.0	3.52	-	-
SINOPEC ENGINEERING	84.97T	6.9	1.06	5.71%	-15.1%
Average	27.22T	32.5	3.40	5.73%	47.5%

Source: Bloomberg, 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	>=20%
OUTPERFORM	From 10% to 20%
HOLD	From -10% to +10%
UNDERPERFORM	From -10% to - 20%
SELL	<= -20%

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