

Industry: Materials

Recommendations BUY NAM KIM STEEL JSC (HSX: NKG)

Current price:	51.200	Report writing date:	10/03/2022	Shareholder structure	
The target price:	60,400	Outstanding Shares (Million)	219.4	Ho Minh Quang	12.83%
Dividend yield	N/A	Market capitalization (billion VND)	11,233	Unicoh Specialty Chemicals	5.88%
Potential for price increase	18%	30 session average volume	13,394,980	SMC	4.98%
		Foreign ownership	8.24%	Vietnam Enterprise Investment	4.92%

Analyst:

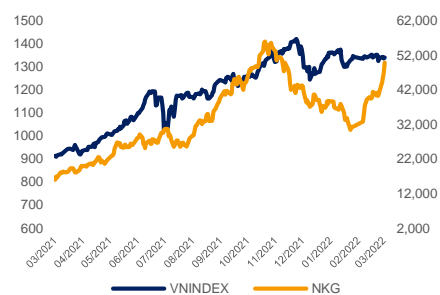
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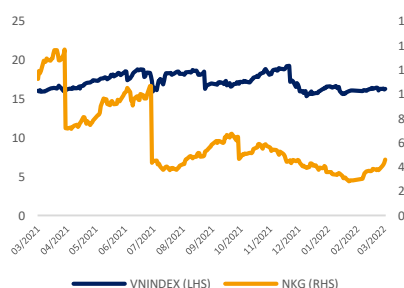
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Recommended price: 63,000 VND
Stop loss price: 46,500 VND

CP price comparison table and VN-Index



P/E and VN index comparison table



Valuation

- **NKG is being traded at PE FW = 4.7x** – relatively cheap compared to stocks in the same industry.
- BSC recommends **BUY NKG** with **1-year target price of 60,400 VND/share** equivalent to upside 18% compared to the price on 10/03/2022 based on P/E valuation method with target PE = 5.5x .

Forecasting business results

- In 2022, BSC forecasts NKG's net profit and **net profit of VND33,788 billion (+20 % YoY)** and **VND2,399 billion (+7.8% YoY)** respectively, **EPS FW = 10,985 VND/share** based on the following assumptions: (i) Consumption of all kinds of steel + 25.7 % yoy, (ii) Gross profit margin -1% yoy due to HRC price -5% yoy.

Investment perspective

- Consumption volume increased thanks to the increase in capacity of galvanized steel sheet (+30%). The export market still plays an important role in the revenue structure (80%) due to (1) the high import demand of developed countries; (2) production cost advantage in Vietnam.
- Profit margin decreased due to: (1) high competitive pressure in the export market and (2) fluctuations in input material prices.

Risk

- Steel selling price dropped more than forecast -5% yoy;
- Raw material prices fluctuated stronger than forecast.

Business Update

- Total consumption of steel products in 2021 is estimated at 1.15 million tons (+64% YoY), of which galvanized steel production will reach 978 thousand tons (+74%yoy), pipe steel output will reach 173 thousand tons (+22% yoy).
- Galvanized steel sheet exports accounted for 74% of total consumption, reaching 719 thousand tons.

	2021	2022F	Peer	VN-Index
PE (x)	7.20	4.70	6.66	16.89
PB (x)	1.50	1.39	2.19	2.61
PS (x)	0.36	0.33	1.24	3.80
ROE (%)	38.9%	29.7%	42.0%	10.3%
ROA (%)	14.5%	13.6%	19.7%	6.4%

	2019	20 20	202 1	202 2 F
Turnover	12,177	11,560	28,173	33.788
Gross profit	342	869	4,270	4.783
NPAT	47	295	2,225	2,399
EPS	260	1.622	10,189	10,985
EPS growth	N/A	524%	528%	8%

BUSINESS UPDATE

NKG's business results in 2021 showed impressive growth (Net sales reached VND28,173 billion, +144% yoy and NPAT at VND2,225 billion, +654%) with the main contribution from the export of galvanized steel sheet .

Table 1: Summary of business results for 4Q2021 for the whole year of 2021

<i>Billion VND</i>	4Q2021	4Q2020	% yoy	2021	2020	% yoy	Note
Net sales	8,780	3.418	157%	28,173	11,560	144%	Net sales grew strongly when consumption of all kinds of steel +64% yoy and average steel price +43% yoy)
Revenue by market:							
<i>Domestic</i>				9,005	6,874	31%	
<i>Export</i>				19,201	4,740	305%	
Gross profit	1.058	307	244%	4,270	869	391%	
Gross profit margin	12.0%	9.0%		15.2%	7.5%		
SG&A	537	110	388%	1.521	360	323%	Selling expense increased sharply due to the increase in export costs
% SG&A/Net sales	6.1%	3.2%		5.4%	3.1%		
EBIT	521	197	164%	2.749	509	440%	
Interest	68	49	39%	244	222	ten%	
Financial revenue	106	25	324%	199	89	124%	Cash and short-term financial investment +102% yoy help increase financial income
NPAT	452	154	194%	2,225	295	654%	
Steel consumption (tons)							
Steel pipe	34.315	58,030	-41%	173.336	141,744	22%	
Galvanized	251.692	140,450	79%	978.543	561,989	74%	
Domestic market share							
Steel pipe	7%	8%		8%	6%		
Galvanized	9%	ten%		ten%	twelfth%		
Export market share							
Galvanized	22%	17%		21%	18%		
Export share in total consumption							
Galvanized	80%	57%		77%	53%		
Some items in the balance sheet							
Short-term debt				3.773	2,520	50%	
Long-term debt				forty six	482	-90%	
Inventory				8,281	2,371	249%	NKG promotes stockpiling of raw materials and finished products from 2Q2021 when steel prices increase sharply
Cash, cash equivalents & Short-term investments				751	219	243%	

Source: NKG, Fiiipro, BSC Research

BUSINESS OUTLOOK 2022

GALVANIZED STEEL EXPORT IS FOCUSED IN THE COMING TIME

The export market is the focus of NKG's sales strategy. The company has always maintained a high proportion of exports of galvanized steel in the past few years, and especially promoted exports when the Covid-19 epidemic broke out, disrupting the steel supply chain and flat steel prices in EU and North America increased sharply.

Figure 1: The share of exports in total consumption of galvanized steel increases sharply in 2021

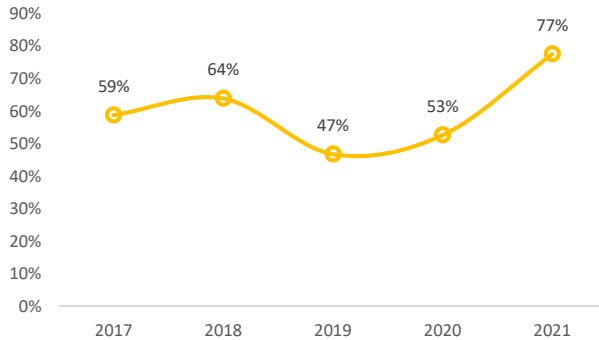
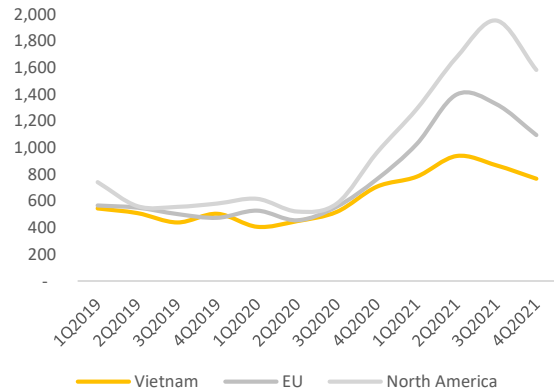


Figure 2: The sharp increase in HRC (input material for flat steel) prices in the EU and North America creates a large gap with domestic prices



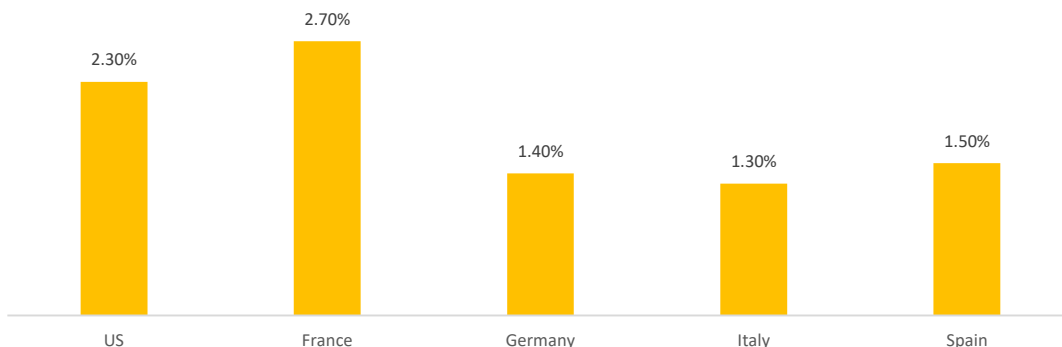
Source: NKG, Bloomberg, BSC Research

BSC believes that NKG will continue to maintain the export proportion of galvanized steel at 80% in 2022 based on the following factors: (1) demand in the EU and North American markets remains high and (2) production cost advantage remains at least until the end of 2Q2022.

(1) Steel demand in the EU and North American markets will continue to be high as (i) these countries all have plans to invest in large-scale infrastructure upgrades; (ii) the Russian-Ukrainian conflict may disrupt steel supply in the EU.

(i) Developed countries in the EU and the United States both plan to deploy large public investment packages in infrastructure to support economic recovery after the epidemic. The US is expected to invest \$2.2 trillion between now and 2030, while the size of investment packages in the EU is smaller and the implementation time is shorter, but also up to 750 billion euros. We believe that the deployment of investment in infrastructure will stimulate demand for steel in these markets.

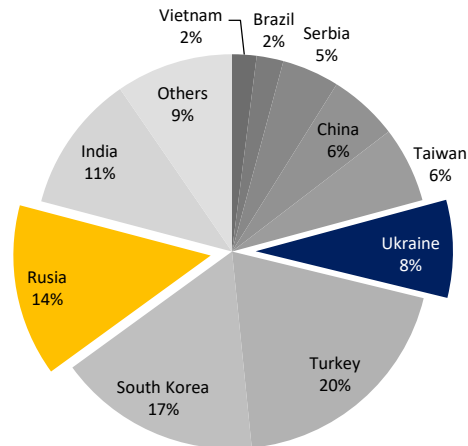
Figure 3: Size of economic stimulus packages in EU and US (% GDP)



Source: Allianz, BSC Research

(ii) Conflict Russia - Ukraine may disrupt steel supplies in the EU. Russia and Ukraine account for a large proportion of steel exports to the EU (22% of EU flat steel imports). Escalating tensions in this region have provoked EU countries against Russia with economic sanctions. We believe that the embargo on Russia's steel exports to the EU and the US, if it happens, will create a great deal of room for Vietnamese steel producers to exploit, especially the galvanized sheet manufacturers.

Figure 4: Russia and Ukraine account for a large proportion of flat steel export partners to the EU

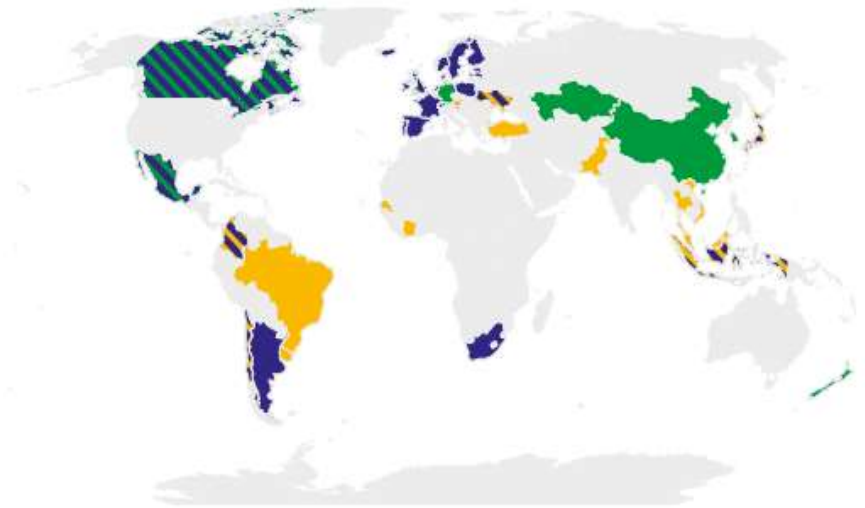


Source: Eurofer, BSC Research

(2) The advantage of low production costs is still maintained in the short term thanks to: (i) the management policy for the steel industry in Vietnam is more favorable than in the importing countries; (ii) the trend of clean steel production makes some major exporting countries more affected when scrap steel prices increase; (iii) domestic supply of HRC is expected to increase slightly.

(i) Environmental impact management policy for the steel industry in Vietnam is looser than in the importing country. Steel supply in developed countries such as the EU and North America is limited by policies to reduce carbon emissions to protect the environment. The standard carbon price in the EU emissions trading system is at 65.07 USD/ton and is expected to increase to 81.36 USD/ton in 2022 (according to Reuters), making production costs in the EU 110-150 USD/ton higher than that of the EU with Vietnam (assuming BOF blast furnace technology is used).

Figure 4: Most developed countries have adopted carbon emission control measures



Green: ETS applied (*)
Gold: Consider ETS/Carbon Tax
(*) Maximum emission limit

Purple: Consider a Carbon Tax
Blue with purple stripes: ETS and Carbon Tax applied
Purple striped yellow: Applied Carbon Tax, considering ETS

Source: World Bank, BSC Research

(ii) **The trend of clean steel production makes steel production costs in other major exporting countries more affected when scrap steel prices increase.** Large steel exporting countries such as Turkey or South Korea are increasingly using electric furnace technology (EAF) in steel production to limit carbon emissions, of which scrap steel accounts for more than 70% of the input material cost. This causes scrap steel demand to skyrocket, pushing scrap prices to rise above the average level in 2021.

Figure 6: Electric furnace (EAF) steelmaking technology accounts for a large proportion of Turkish steel production

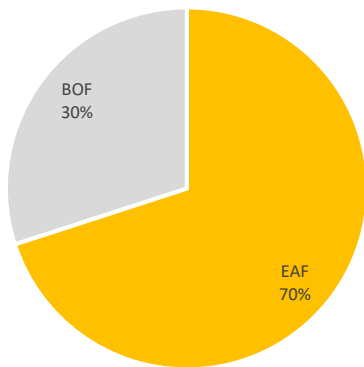
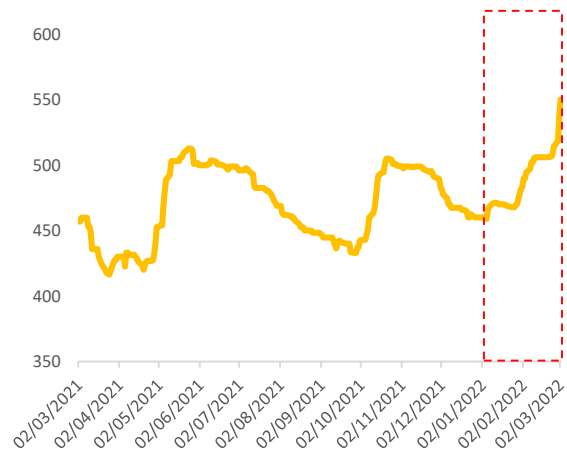


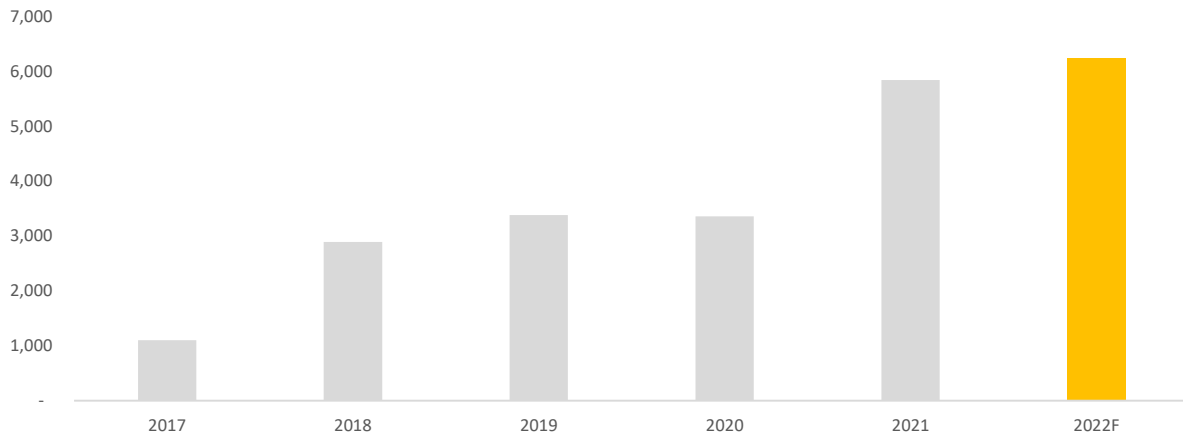
Figure 7: Scrap prices have risen sharply since the beginning of 2022, reflecting growing demand



Source: Kallanish, Bloomberg, BSC Research

(iii) **The domestic supply of HRC is still guaranteed** because Hoa Phat Group (one of the only two domestic HRC manufacturers) maintains its domestic sales policy. Therefore, we believe that the supply and price difference of input HRC are still attractive enough for Vietnam's galvanized steel exporters.

Figure 8: Domestic HRC supply in 2022 is expected to increase slightly when HPG's factory is operating at full capacity (thousand tons)



Source: Fiinpro, BSC Research

We believe that when consumption demand in key export markets remains high, NKG will benefit from its large export market share. NKG is in the top 2 largest exporters of coated steel sheets in Vietnam (after Hoa Sen Group) and has an increase in market share in 2021 (NKG's market share increased by 3%, while Hoa Sen's market share decreased by 7%). We believe that NKG's market share will continue to increase in 2022 as the company plans to increase its galvanized steel sheet capacity from 1 million tons/year to 1.3 million tons/year, which is expected to be completed in Q2/2022.

BSC estimates, if the enterprise completes the project to increase capacity as expected, **the consumption of galvanized steel sheet of NKG will be +30% yoy.**

Figure 9: NKG is in the top 2 exporters of galvanized steel sheet

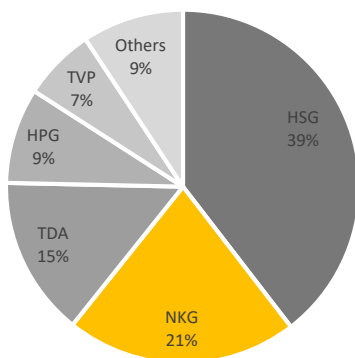
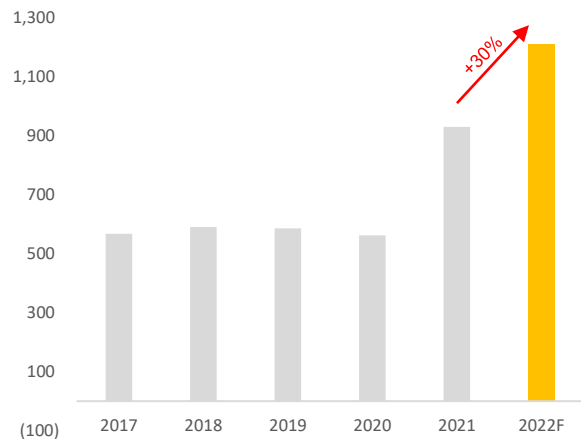


Figure 10: Galvanized steel sales volume forecast +30% yoy in 2022 (thousand tons)



Source: Fiinpro, BSC Research

COMPETITION INCREASES , BUT THE PRICE OF MATERIALS ARE MOVING IN A BENEFITS FOR NKG

We believe that competition among steel exporters will increase in 2022. The high rate of vaccine coverage in major steel-producing countries facilitates the reopening of production. Competitors' steel output gradually recovered to pre-pandemic levels, causing flat steel prices in the export market to gradually decrease.

Figure 11: Factory efficiency in China increased to the highest level in the past 2 years

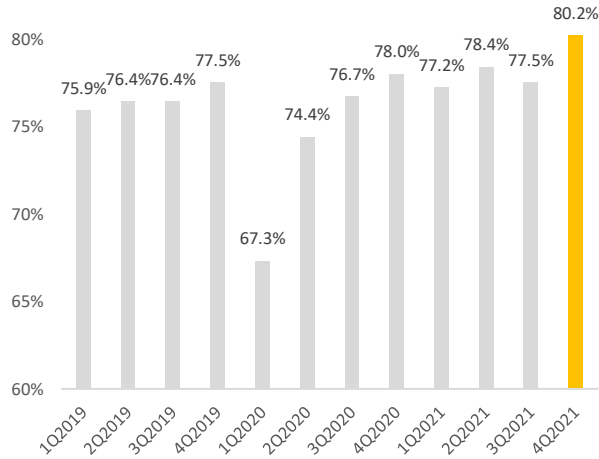
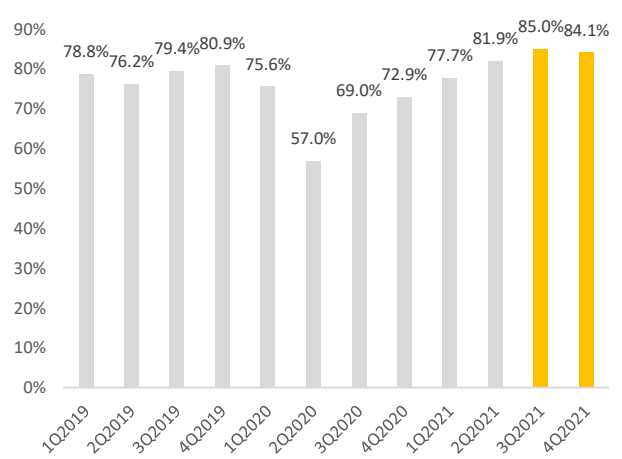


Figure 12: Performance of steel mills in the US gradually recovers when the epidemic is under control

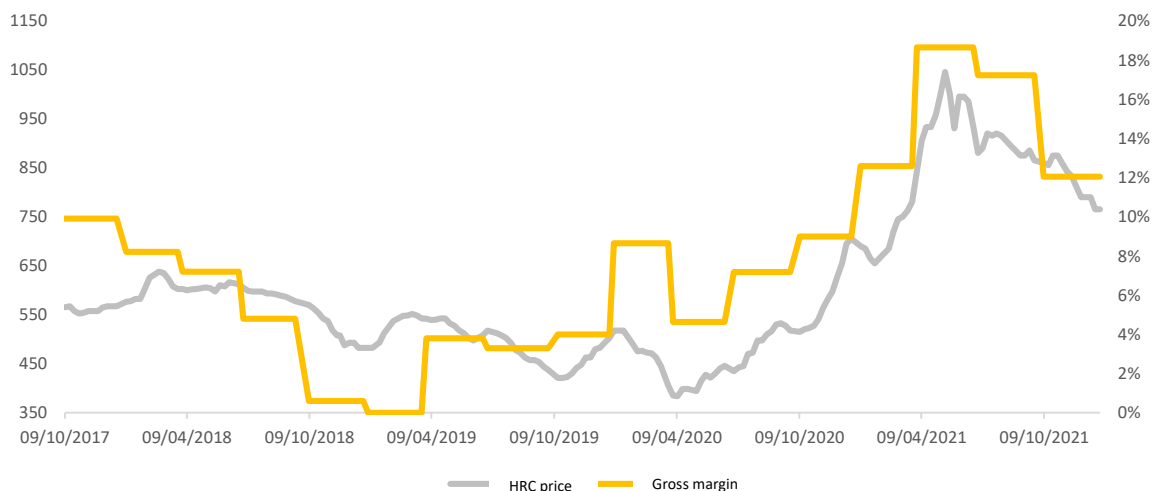


Source: CNBS, Fred, BSC Research

Raw material prices are moving in favor of NKG.

HRC price fluctuations have a great influence on NKG's gross profit margin. Although HRC is the main input to the production of galvanized sheet and steel pipes, NKG has the ability to pass on the increased raw material costs into the selling price of the finished product and, in the past, stockpiling helped increase NKG's gross profit margin when the price of HRC rose sharply.

Figure 13: NKG's gross profit margin tends to move in the same direction as HRC price (USD/ton)



Source: Fiinpro, Bloomberg, BSC Research

HRC price is a short-term support factor for NKG. HRC price reverses when input material prices such as iron ore, coke and scrap steel suddenly increased sharply since the beginning of 2022 due to the recovery of consumption demand in steel exporting countries, and the fear of thermal coal supply of Russia (the third largest coal reserves and accounts for 4.5% of the world's mined output) disrupted by embargoes. We believe that

NKG will benefit from the increase in HRC price as the company accumulates large inventories at high steel prices in the second half of 2021.

Figure 14: The price of input materials has increased sharply since the beginning of 2022



Source: Bloomberg, BSC Research

However, we also note that the price increase of raw materials is being largely influenced by the tension between Russia and the West, and governments will take measures to curb the increase in the long term . In China - a country that imports 67% of iron ore and consumes 50% of the world's coal (according to OEC and IEA) - the government has recently adjusted iron ore speculation, as well as imposed a ceiling price – floor price when trading coal at some major seaports of this country. In the medium to long term, iron ore supply will recover as major suppliers in Australia and Brazil restore production to pre-pandemic levels , but coal supply has not yet met demand, so we expect The average HRC price in 2022 -5% yoy causes NKG's profit margin to decrease by 1% compared to 2021.

FORECAST OF BUSINESS RESULTS

BSC forecasts NKG's net sales and net income in 2022 at **VND33,788 billion (+20% YoY)** and **VND2,399 billion (+7.8% YoY)**, **EPS FW = 10,985 VND/share** based on the following assumptions: (i) Steel sales volume +25.7% yoy, (ii) GPM -1% yoy due to HRC price -5% yoy.

VALUATION

NKG stock is currently trading at a PE FW of, in our estimation, only 4.7x. This valuation is relatively cheap compared to stocks in the same industry.

We use the P/E method, with a target PE of 5.5x - the same as the average PE over the previous period for this stock. With EPS 2022 FW forecast at VND10,985/share, we recommend **BUY** for NKG stock with a target price of **60,400 VND/share**, equivalent to an **upside of 18%** compared to the closing price on 10/03/2022.

Figure 15: NKG's P/E

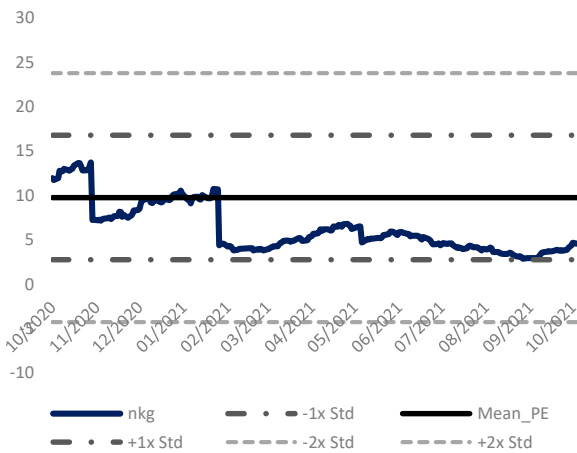
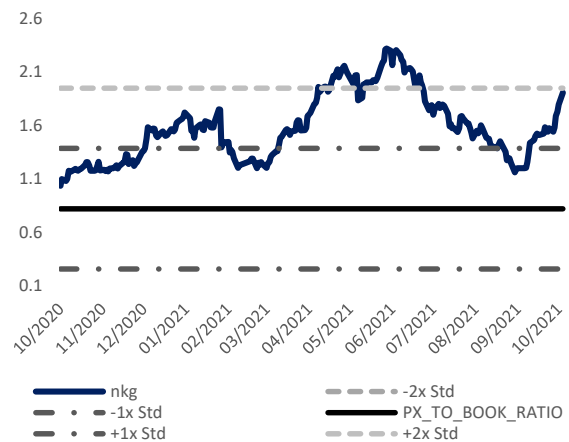


Figure 16: NKG's P/B



Source: Bloomberg, BSC Research

APPENDIX

Income statement (Billion VND)	2019	2020	2021	2022F	Cashflow (Billion VND)	2019	2020	2021	2022F
Net sales	12,177	11,560	28,173	33,677	(Loss)/EBT	90	321	2,547	2,754
Cost of goods sold	11,835	10,690	23,904	28,910	Depreciation & amortization	427	585	1,057	1,130
Gross profit	342	869	4,270	4,767	Change in working capital	664	(891)	(3,922)	(475)
Selling expenses	210	268	1,398	1,838	CFO	1,181	16	(318)	3,408
G&A expenses	69	92	123	147	Purchase of fixed assets	(96)	(54)	(140)	217
Gross profit	63	509	2,749	2,782	Other investments	(134)	400	(164)	(763)
Financial revenue	107	89	199	303	CFI	(230)	346	(304)	(546)
Financial expenses	275	281	397	362	Dividend payment	-	-	-	-
Interest expenses	237	222	244	290	Net borrowing	(1,315)	(sixty seven)	861	1,295
Profit from joint ventures	-	-	-	-	Other revenues	(22)	(151)	294	(20)
Other profit/loss	195	4	11	30	CFF	(1,336)	(218)	1,155	1,275
Profit before tax	90	321	2,562	2,754	C&CE at the beginning of FY	461	76	219	751
Corporate income tax	43	26	337	362	Net increase/decrease in cash	(385)	143	533	4,137
Profit after tax	47	295	2,225	2,392	C&CE at the end of FY	76	219	752	4,889
Non-controlling interest	-	-	-	-					
NPAT - Owners	47	295	2,225	2,392					
EBITDA	299	867	3,139	3,189					
EPS	260	1,622	10,189	10,951					
Balance sheet (Billion VND)	2019	2020	2021	2022F	Ratio (%)	2019	2020	2021	2022F
Cash & Short-term investments	778	589	1,199	5,723	Liquidity				
Trade account receivables	877	1,438	1,905	2,612	Current ratio	1.02	1.10	1.27	1.57
Inventories	2,589	2,371	8,281	6,281	Quick ratio	0.43	0.52	0.41	0.90
Other current assets	191	95	833	180					
Total current assets	4,435	4,492	12,219	14,796	Capital structure				
Tangible fixed assets	3,049	2,727	2,530	2,277	Debt/Assets	63%	59%	63%	54%
Intangible fixed assets	247	249	241	246	Debt/Equity	167%	144%	169%	118%
Financial lease	162	151	-	-					
Construction in progress	49	59	176	207	Working capital				
Long-term investment	48	23	8	8	Inventory days	77	85	85	85
Other noncurrent assets	74	63	209	23	Receivable days	20	30	18	24
Total noncurrent assets	3,629	3,271	3,164	2,831	Payable days	36	49	45	47
Total Assets	8,064	7,763	15,383	17,626	CCC	60	66	63	64
Account payables	1,819	1,070	4,879	3,752					
Short-term loans	2,389	2,520	3,773	4,563	Margin				
Other current liabilities	135	507	949	1,121	Gross margin	3%	8%	15%	14%
Current Liabilities	4,342	4,098	9,602	9,436	NPAT margin	0%	3%	8%	7%
Long-term loans	703	482	46	106	ROE	2%	9%	39%	30%
Other noncurrent liabilities	2	2	11	11	ROA	1%	4%	14%	14%
Noncurrent liabilities	705	484	58	118					
Total Liabilities	5,048	4,582	9,659	9,554	Valuation				
Capital	1,820	1,820	2,184	2,184	PE	N/A	16.3	7.2	4.7
Capital surplus	766	766	786	786	PB	0.4	0.5	1.5	1.4
Retained earnings	356	576	2,636	5,028					
Other equity	74	18	117	75	Growth				
Non-controlling interests	-	-	-	-	Revenue growth	-18%	-5%	144%	20%
Total Equity	3,017	3,181	5,723	8,072	EBIT Growth	-84%	711%	440%	1.2%
Total Liabilities & Equity	8,064	7,763	15,383	17,626	EBT growth	-17%	256%	699%	7%
No. of shares (million)	182	182	218	218	EPS growth	-17%	524%	528%	7%

Source: NKG , BSC Research

Disclosure

The information, statements, forecasts and projections contained herein, including any expression of opinion, are based upon sources believed to be reliable but their accuracy completeness or correctness are not guaranteed. Expressions of opinion herein were arrived at after due and careful consideration and they were based upon the best information then known to us, and in our opinion are fair and reasonable in the circumstances prevailing at the time. Expressions of opinion contained herein are subject to change without notice. This document is not, and should not be construed as, an offer or the solicitation of an offer to buy or sell any securities. BSC and other companies in the BSC and/or their officers, directors and employees may have positions and may affect transactions in securities of companies mentioned herein and may also perform or seek to perform investment banking services for these companies. This document is for private circulation only and is not for publication in the press or elsewhere. BSC accepts no liability whatsoever for any direct or consequential loss arising from any use of this or its content. The use of any information, statements forecasts and projections contained herein shall be at the sole discretion and risk of the user. No part of this material may be (i) copied, photocopied or duplicated in any form by any mean or (ii) redistributed without the prior written consent of BIDV Securities Company (BSC).

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