

Sector Note

Infrastructure construction

Powered up by strong backlog

- Most of listed infra construction companies recorded positive revenue growth in 1Q23 and but their net margin dropped yoy mainly due to a lack of one-off gained profit and higher interest expenses.
- Expectations of strong public investment disbursement and high backlog value will help infra construction companies break through in terms of revenue and operating profit in the 2023-25F period.
- We believe that the North-South Expressway Phase 1 & 2 projects will be the main growth drivers for construction companies in 2023-25F.

Government accelerates disbursement of infra development in order to support economy expansion

Since early 2023, Vietnam's government has stepped up public investment to support economic growth amid weak private investment and FDI inflows. Thus, we maintain our forecast that the implemented state capital to increase by 25% compared to the actual 2022 figure. We believe that infra construction companies will benefit from this trend. In fact, the backlog value of the leading companies increased significantly in 1Q23, equivalent 3.7x-6.0x compared to annual revenue in 2021-22 period.

2023 outlook: Negative bottom line growth despite promising top line

In FY23F, most of listed infra construction companies aimed for revenue growth recovery but were still concerned about the bottom-line growth due to a lack of one-off gained profit. Regarding 1Q23 business results, infra construction companies' revenue increased by 35% yoy but net profit decreased by 83% yoy mainly due to a lack of one-off gains and higher interest expense.

Financial health will determine the profitability of infra construction companies

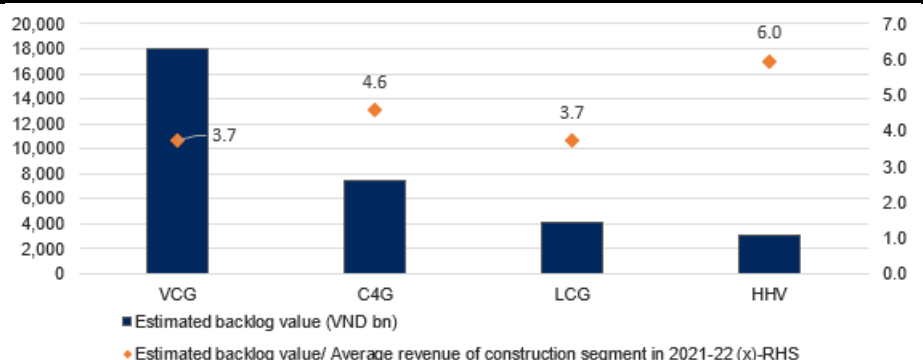
We believe that only construction companies with good construction capacity, reasonable machinery mobilisation and abundant working capital can ensure profitability at the North-South Expressway project due to (1) requiring a short construction period; and (2) a fixed profit margin to the project based on the bid price assigned by the Government. At the end of 1Q23, average net debt/equity ratio of infra construction companies was 1.1x. Notably, LCG's net debt/equity ratio was only 0.01x. Meanwhile, excluding the debt in Nam Ben Thuy 2 BOT project, the net debt/equity ratio of C4G was 0.5x at the end of 1Q23.

We believe C4G and LCG are top beneficiaries of the infra investment booming

Downside risks include: (1) disbursement of public investment is slower-than-expected, (2) shortage of raw materials due to slower-than-expected mining license.

Potential catalyst is raw material prices are lower-than-expected, supporting infra construction companies' gross margin.

Figure 1: High backlog value of infra construction companies at the end of 1Q23



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Source: VNDIRECTS RESEARCH, COMPANY REPORTS

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FY23F guidance and 1Q23 business results

Figure 2: Business guidance in FY23F and actual business results in 1Q23 of listed infra construction companies

Company	FY22 results (VND bn)		FY23F guidance (VND bn)		% change (yoy)		1Q23 results (VND bn)		% change (yoy)	
	Revenue	NPAT	Revenue	NPAT	Revenue	NPAT	Revenue	NPAT	Revenue	NPAT
VCG	8,452	931	16,340	860	93.3%	-7.6%	1,965	19	47.4%	-97.6%
C4G	2,726	154	4,500	330	65.1%	114.3%	460	41	7.7%	26.7%
HHV	2,095	297	2,478	339	18.3%	14.0%	539	83	25.2%	4.4%
LCG	1,006	194	2,850	150	183.3%	-22.7%	242	10	33.6%	-80.0%

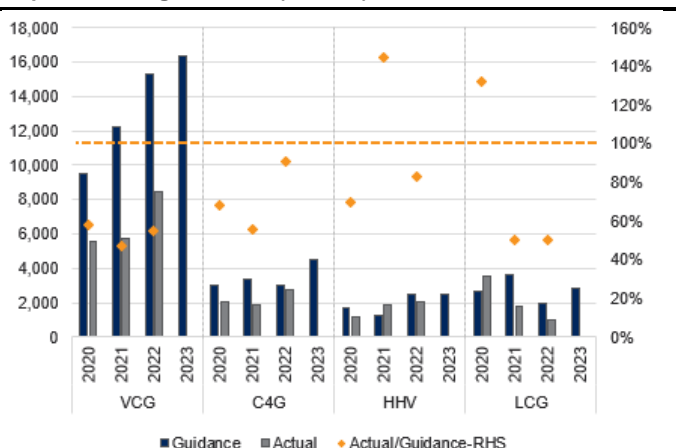
Source: VNDIRECT RESEARCH, COMPANY REPORTS

All the leading listed infra construction companies have set strong revenue growths in FY23F thanks to (1) high backlog value after winning many bidding packages at the North-South expressway project and (2) the Government's push to disburse public investment this year will help ensure construction progress and revenue recognition in transport infrastructure projects.

However, in terms of bottom-line growth, there is a division within the companies. Notably, C4G plans to increase NPAT by 114% yoy while VCG and LCG decrease 8% and 23% yoy in FY23F, respectively, mainly due to one-off gained profits including: (1) VCG recorded a profit of VND663bn from revaluation of investment in Vinaconex Investment and Tourism Development JSC (Upcom, VCR), accounting for 67% of the company's pretax profit in FY22 and (2) LCG recorded a profit of VND268bn from the divestment of two solar power projects, accounting for 109% of the company's pretax profit in FY22. Excluding these one-off gain profits, the FY23F NPAT guidance of VCG will increase 115% yoy while LCG's NPAT will improve from a loss of VND20bn in FY22 to a profit of VND150bn in FY23.

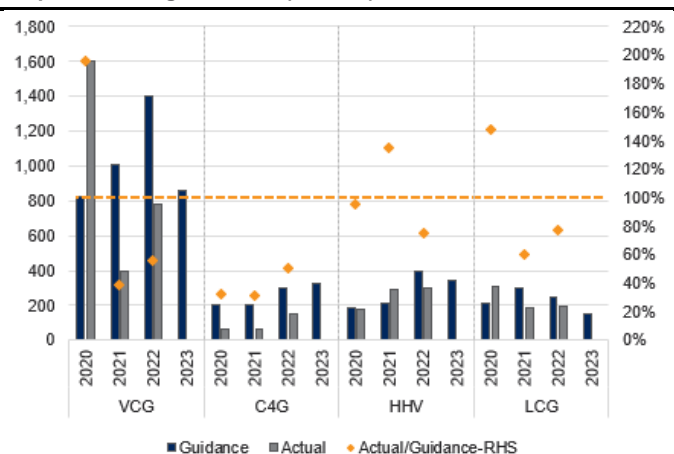
We also note that infra construction companies often miss their business guidances during FY20-22.

Figure 3: Revenue guidance and actual revenue of infra construction companies during FY20-23F (VND bn)



Source: VNDIRECTS RESEARCH, COMPANY REPORTS

Figure 4: NPAT guidance and actual NPAT of infra construction companies during FY20-23F (VND bn)



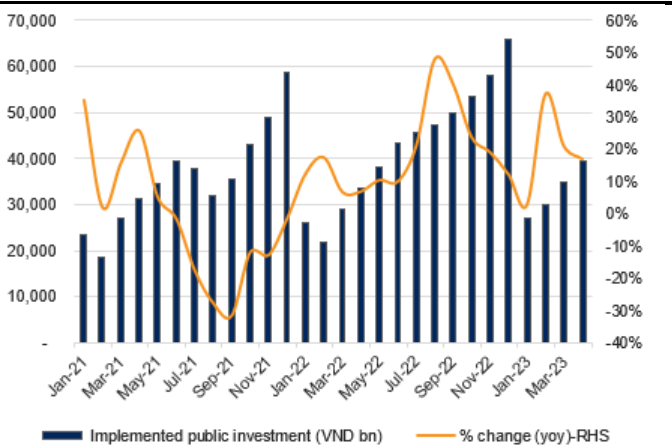
Source: VNDIRECTS RESEARCH, COMPANY REPORTS

1Q23 earning results of infra construction companies partly reflected the business guidance for the whole year. All companies recorded 1Q23 revenue growth compared to the same period last year, in line with their full-year guidance.

Infrastructure construction industry outlook in 2023F

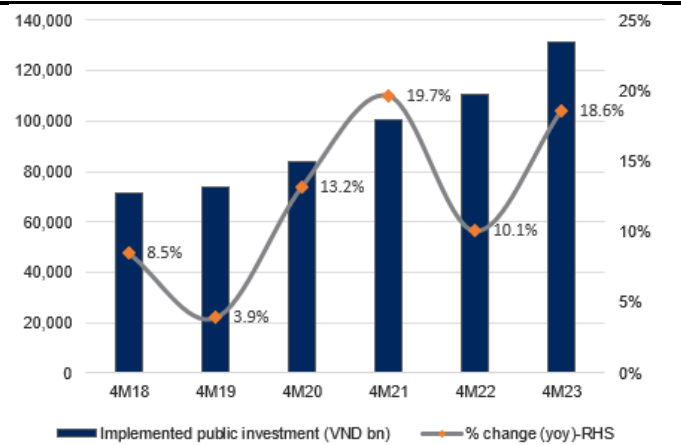
Government accelerates disbursement of infra development in order to support the economy

Figure 5: Public investment grew steadily



Source: VNDIRECTS RESEARCH, GSO

Figure 6: Implemented public investment rose 18.6% yoy in 4M23



Source: VNDIRECTS RESEARCH, GSO

Since the beginning of 2023, Vietnam's government has stepped up public investment to support economic growth amid weak private investment and FDI inflows. According to GSO, the implemented state capital (public investment) in Apr 2023 rose 16.4% yoy to VND39.3tr (vs. +18.6% yoy in Mar 2023). For 4M23, the implemented state capital rose 17.9% yoy to VND131.2tr, which is higher than the growth rate of 10.8% yoy in 4M22.

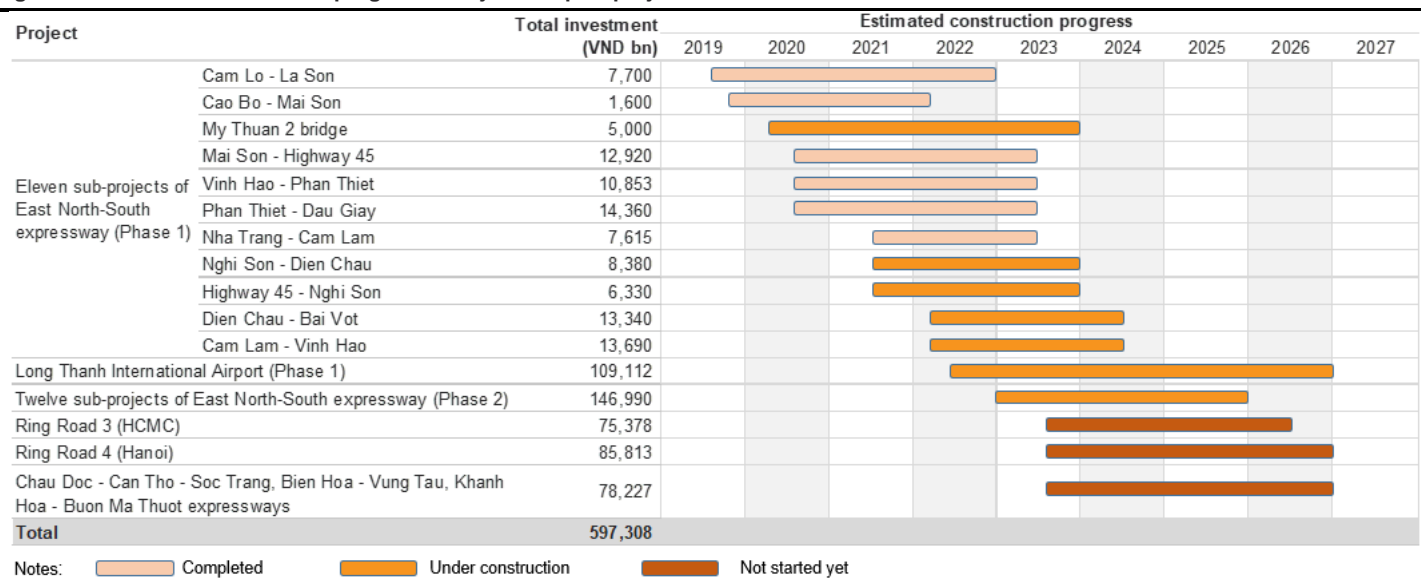
However, implementation public investment capital in 4M23 only reached about 19% of the whole year 2023 plan (vs. 18.5% of the whole year 2022 plan in 4M22). Therefore, the government needs to further promote public investment in the coming months to fulfill the goal of disbursing more than VND700tr of public investment capital in 2023. We now see several supporting factors to further accelerate public investment projects this year, including:

- Vietnam successfully lowered the public debt ratio in the past few years: Thanks to solid GDP growth in 2016-2022 period and tight spending controls, Vietnam's public debt has fallen rapidly over the years from 51% at the end of 2016 to 40% by the end of 2022 (IMF's estimation), which is much lower than Vietnam's public debt ceiling of 60% of GDP. Low public debt give room for loose fiscal policy to support the economic recovery.
- Yields of Vietnam's government bonds dropped sharply since the beginning of 2023: As of 10 May, in primary market, 10-year and 15-year G-bond yields dropped 167 and 170 bps ytd, to 3.0% and 3.1%, respectively. On secondary market, Vietnam's 5-year and 10-year G-bonds yields decreased 242 and 189 bps ytd, to 2.6% and 3.2%, respectively.
- Domestic inflation cooled down in the past few months: Vietnam's headline inflation dropped down to 2.8% yoy in Apr 23 from 4.2% yoy in 1Q23. As inflationary pressures ease, the government may consider loosening fiscal policy more to support economic recovery.

- Commencement of major transport infrastructure projects before June 30: Prime Minister Pham Minh Chinh has urged the Ministry of Transportation to complete preparations to start the construction of three expressways Chau Doc-Can Tho-Soc Trang, Bien Hoa-Vung Tau, Khanh Hoa-Buon Ma Thuot, and two ring roads including the 4th belt of Hanoi and the 3rd belt of Ho Chi Minh City. These projects need to start before June 30 this year.

Consequently, we maintain our forecast that the implemented state capital to increase by 25% compared to the actual implementation in 2022.

Figure 7: Estimated construction progress of major transport projects



Source: VNDIRECT RESEARCH, MINISTRY OF TRANSPORT

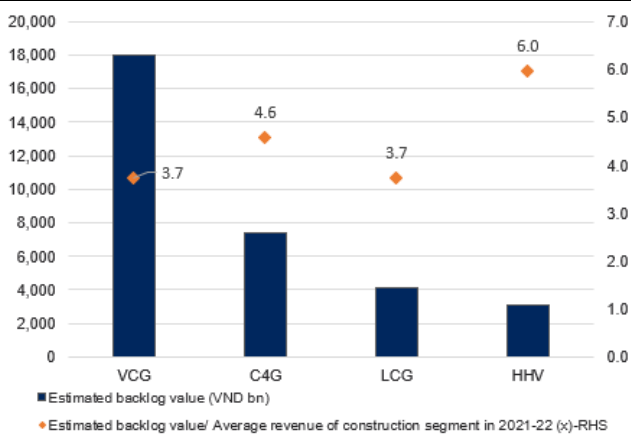
High backlog value ensures revenue growth of construction segment in FY23-25F

After being appointed contractors at many component projects at the North-South Expressway phase 2 (early 2023), leading infra construction companies have significantly increased their backlog values. Notably, HHV's backlog value was VND3,135bn at the end of 1Q23, equivalent to 6 times the average revenue of the company's construction segment in FY21-22 period.

With transport infrastructure projects usually being constructed in 2-2.5 years, in FY23-25 period, infra construction companies are facing the opportunity to double their revenue compared to the FY21-22 period.

We also note that these companies are continuously winning other construction contracts and directly benefiting from the Government's push to disburse public investment. Thus, we believe that the revenue scale of these leading infra construction companies will grow stronger in the coming years.

Figure 8: High backlog value of leading infra construction companies at the end of March 2023



Source: VNDIRECTS RESEARCH, COMPANY REPORTS

Figure 9: Bidding packages at the North-South Expressway phase 2 account for a large proportion of the backlog value of infra construction companies

Company	Expressway projects	Contract value (VND bn)
Total		5,509
VCG	Bai Vot - Ham Nghi	3,035
	Van Phong - Nha Trang	1,036
	Vung Ang - Bung	1,438
Total		3,583
C4G	Bung - Van Ninh	1,805
	Hau Giang - Ca Mau	1,778
Total		4,019
LCG	Vung Ang - Bung	1,274
	Nha Trang - Van Phong	2,745
HHV	Quang Ngai - Hoai Nhon	1,789

Source: VNDIRECTS RESEARCH, COMPANY REPORTS

Mega project of Long Thanh International Airport (LTIA) will also attract many contractors with a large construction value of VND56,000bn (phase 1). However, the contractor selection progress in package 5.10 - the largest package - for the construction of the passenger terminal at LTIA has continuously been delayed due to the unattractive bidding price and urgent construction time. We expect that after being approved to adjust these 2 bottlenecks in the coming months, LTIA will be a growth engine for domestic contractors. Management of construction companies also shared that investor's initial reciprocal capital for contractors in airport projects is usually 30-50% of the package value, higher than road projects (10-20%).

Figure 10: C4G and VCG have experience in executing many items at airports projects

Airport project	Location	Contract value (VND bn)	Construction time
C4G			
Phu Quoc	Kien Giang	437	2016-17
Cam Ranh	Khanh Hoa	642	2017-19
Tan Son Nhat	HCMC	537	2020-22
Cat Bi	Hai Phong	122	2020-22
Phu Bai	Hue	198	2020-22
Cam Ranh	Khanh Hoa	260	2022-23
VCG			
Cam Ranh	Khanh Hoa	299	2022-23
Long Thanh	Dong Nai	1,195	2022-23
Noi Bai	Ha Noi	204	2022-24

Source: VNDIRECTS RESEARCH, COMPANY REPORTS

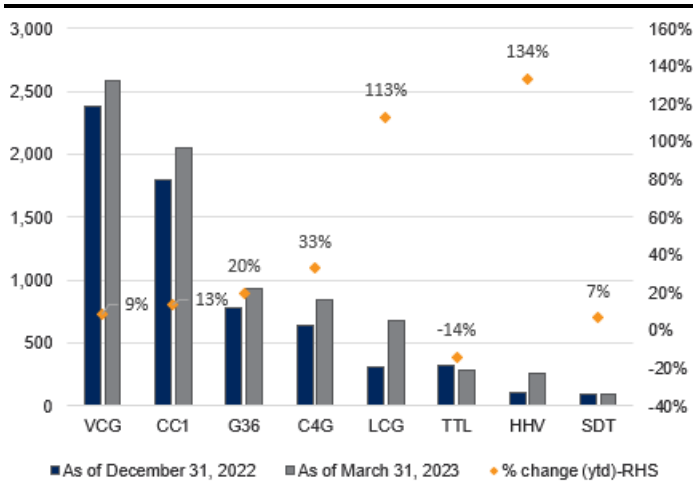
With specific technical and machinery requirements, we believe that only a few domestic contractors can participate in construction at LTIA. We like C4G and VCG for this theme because they have been participating in the construction of many Vietnam airport projects. However, with the large scale of the bidding package at LTIA, these companies must enter into a joint venture with other companies to ensure the project progress.

Financial health will determine the profitability of infra construction companies

In 8 listed companies that have been appointed contractors (early 2023) at the North-South expressway phase 2 project, 7 companies recorded an increase in 1Q23 prepayment by customers compared to the beginning of the year (details in figure 11). As a result, 1Q23 revenue/average prepayment by customers ratio of infra construction companies decreased to 2.4x from 2.7x in 2022. This trend is mainly due to efforts to accelerate disbursement of public investment, investors have proactively advanced counterpart capital for project implementation to contractors.

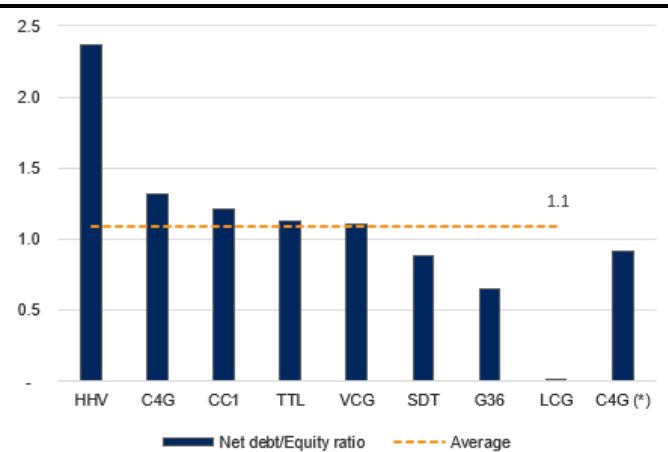
As a result, infra construction companies have reduced working capital pressure, thereby improving their net debt/equity ratio at the end of 1Q23.

Figure 11: As of March 31, 2023, prepayment by customers of infra construction companies increased ytd (VND bn)



Source: VNDIRECTS RESEARCH, COMPANY REPORTS

Figure 12: Net debt/Equity ratio of of infra construction companies as of March 31, 2023



(*) Estimated Net debt/Equity ratio of C4G after successful issuance to existing shareholders in April 2023

Source: VNDIRECTS RESEARCH, COMPANY REPORTS

At the end of 1Q23, average net debt/equity ratio of infra construction companies was 1.1x, especially, LCG had almost no net debt. Due to the consolidation of BOT projects (large debt and payments over the life of the project - lasting 10-20 years), the net debt/equity ratio of HHV and C4G was higher than the industry average, reaching 2.4x and 1.3x respectively at the end of 1Q23. However, we still think that C4G is in strong financial health thanks to the Nam Ben Thuy 2 BOT project which is bringing in annual net cash flow. Therefore, if excluding the debt in this BOT project, the net debt/equity ratio of C4G was only 0.5x at the end of 1Q23. We also note that C4G has also successfully raised VND1,123bn from existing shareholders in April 2023, thereby increasing the company's owner equity by 44% compared to the end of 1Q23.

We believe that only construction companies with good construction capacity, reasonable machinery mobilisation and abundant working capital can ensure profitability at the North-South Expressway project due to (1) require a short construction period; (2) the Government assigns a fixed profit margin to the project based on the bid price.

Ministry of Transport proposes financial support and buy back of 8 BOT projects

Recently, the Ministry of Transport has submitted a proposal to the Government for the second time to solve difficulties in 8 BOT projects. These are projects that have been completed and put into operation, but BOT fee revenue was very low compared to the financial plan.

Figure 13: The Ministry of Transport proposed the Government solutions to support 8 BOT transport infrastructure projects

Project	Related listed companies	Proposal May 2023 (VND bn)	Proposal Oct 2022 (VND bn)	% change	Total investment (VND bn)
Binh Loi railway bridge		571	612	-7%	1,302
Western belt of Thanh Hoa city		892	920	-3%	1,836
Highway 91, Can Tho city	CTI, SNZ	1,754	1,879	-7%	1,720
Thai Nguyen - Cho Moi	C4G	2,850	3,250	-12%	2,744
Ho Chi Minh road, Dak Lak province	S4A	745	703	6%	1,509
Thai Ha bridge	BOT	717	2,049	-65%	1,671
Viet Tri - Ba Vi bridge		533	1,422	-63%	1,460
Deo Ca road tunnel	HHV	2,280	2,280	0%	11,377
Total		10,342	13,115	-21%	23,619

Notes: ■ The project is proposed to terminate the contract and to be acquired by the State Budget
■ The project is proposed to continue the contract and extend the payback period

Source: VNDIRECTS RESEARCH, MINISTRY OF TRANSPORT

The total amount proposed by MoT to support or buy back these 8 projects is VND10,342bn, 21% lower than the previous proposal in October 2022.

If approved, some investor projects will suffer a loss because (1) the project was unable to collect high fees as in the original financial plan and (2) the proposed amount of the Ministry of Transport is quite close to the total investment of projects. However, the recovery of the initial large investment capital has also been a success for investors at the present time, in our view.

In addition, Vietnam's infrastructure construction demand is very huge, the Government needs to mobilize more non-budget capital sources to be able to develop. Thus, in order to increase the attractiveness of private capital, the Government needs to provide financial support for projects that have changed compared to the original financial plan.

If approved, infra construction companies including C4G, HHV will significantly improve their financial capacity and potentially win more next large-scale bidding packages.

Investment idea

We believe that infra construction companies will benefit from the Government's trend of accelerating public investment disbursement in FY23-25F. However, we prefer companies with the following criteria: (1) good construction capacity, (2) high backlog value/revenue ratio; and (3) solid financial health. Thus, we believe C4G and LCG are top beneficiaries of this trend.

Figure 14: Peer comparison

Company	Ticker	Price		Mkt cap		P/E (x)		3-year EPS		P/B (x)		ROE (%)		Total debt/Equity (%)
		VND	VND bn	TTM	FY23F	CAGR (%)	Current	FY23F	TTM	FY23F	Current			
Vietnam Construction and Import-Export JSC	VCG VN	20,200	9,815	22.8	43.8	56.9	1.4	0.9	0.6	5.7	136.1			
Deo Ca Traffic Infrastructure Investment JSC	HHV VN	14,000	4,309	14.5	na	(7.7)	0.6	na	3.9	na	246.6			
Construction Corp No 1 JSC	CC1 VN	10,700	3,516	14.2	na	158.7	0.9	na	8.1	na	162.6			
CIENCO4 Group JSC	C4G VN	13,100	4,764	16.6	15.5	22.6	1.2	1.1	8.2	7.3	142.2			
Lizen JSC	LCG VN	13,450	2,551	17.2	na	3.5	1.0	na	5.9	na	16.7			
36 Corp	G36 VN	8,600	875	39.4	na	4.9	0.8	na	2.1	na	117.9			
Thang Long JSC	TTL VN	8,900	372	69.3	na	(34.1)	0.7	na	1.0	na	111.1			
Song Da No10 JSC	SDT VN	3,000	128	na	na	na	0.2	na	(2.8)	na	93.7			
<i>Average</i>				27.7	29.6	29.3	0.9	1.0	3.4	6.5	128.4			
<i>Median</i>				17.2	29.6	4.9	0.9	1.0	3.0	6.5	127.0			

Source: VNDIRECT RESEARCH, BLOOMBERG, DATA AS OF 25 MAY 2023

Downside risks include: (1) disbursement of public investment is slower-than-expected, (2) shortage of raw materials due to slower-than-expected mining license.

Potential catalyst is raw material prices are lower-than-expected, supporting infra construction companies' gross profit margin.

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RECOMMENDATION FRAMEWORK

Stock Ratings

Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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