

## BRIEF REPORT

09 Feb 2010

Current price (09 Feb 2010)

VND 22,000

## DOMINANT PLAYER IN ITS NICHE

## Highlight

- ✓ NHW leads the niche market of magnet wire and is well-known for its high quality products, especially the high-temperature round enameled wire.
- ✓ Strong core competence and strategic investment in product development promise consistent revenue growth in the long run.
- ✓ The sector is substantially subject to fluctuation risk in copper price and exchange rate as most of input materials come from imports. NHW has been implementing hedging measures to mitigate these risks. Therefore, future earnings are expected to be more stable.

## Valuation

Items	Unit	NHW	TYA	CSG	VHG
Sales	VNDbn	910.7	752.0	370.6	189.9
Gross profit	VNDbn	104.4	89.4	46.1	23.4
NPAT	VNDbn	44.2	3.6	29.6	2.1
ROA	%	9.7%	0.6%	4.9%	0.4%
ROE	%	18.0%	1.9%	5.8%	0.5%
Price as at 09/02/2010	VND	22,000	8,300	11,700	11,700
2009E P/E	x	11.4	64.3	11.0	139.3
2009E P/B	x	2.0	1.2	0.6	0.7

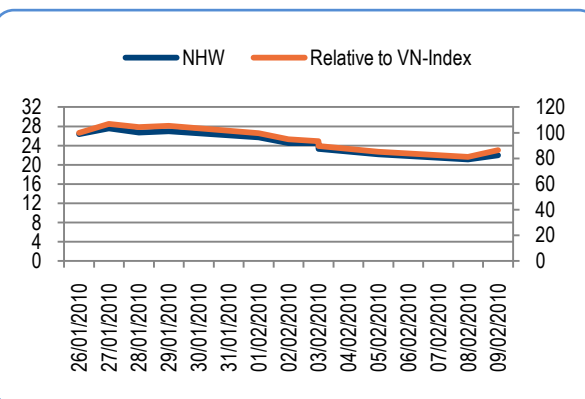
Source: NHW, TYA, CSG, VHG

- ✓ Using the market multiplier method we suppose NHW is currently traded at its fair value based on 2009 P/E and 2009 P/B. The estimated 2010 P/E level of 8.6x indicates that NHW might be worth investment consideration. However, given the moderate growth level of the sector and the specific risks the stock seems less attractive compared to several other stocks in the market.

## Forecast Earnings &amp; Valuation

Fiscal year	2008A	2009E	2010F	2011F
Sales (VNDbn)	910.7	1,147.5	1,422.9	1,735.9
Growth	0.9%	26.0%	24.0%	22.0%
Gross profit	104.4	143.4	185.0	225.7
Gross margin	11.5%	12.5%	13.0%	13.0%
Operating profit	44.6	68.8	92.4	112.7
Net profit before tax	54.0	78.2	101.8	122.2
Net profit after tax	44.2	58.7	76.4	91.6
Growth	1961.2%	32.7%	30.2%	20.0%
Net margin	4.9%	5.1%	5.4%	5.3%
Assets	456.8	484.9	571.9	670.2
Liabilities	211.0	210.9	260.4	319.4
Equities	245.8	274.0	311.6	350.8
Debt ratio	85.8%	77.0%	83.6%	91.1%
ROE	18.0%	21.4%	24.5%	26.1%
PBR	2.2	2.0	1.7	1.5
Forward PER	12.1	9.1	7.0	5.8
Trailing PER	12.1	9.1		

## Relative performance to VN-Index



## Trading Data

Market cap (VNDbn/USDmn)	504.9/27.3		
Shares outstanding	22,950,627		
52-week price high/low	VND26,400/21,100		
Daily avg turnover(VNDmn/USDk)	233.3/12.6		
<b>Performance</b>	<b>1M</b>	<b>3M</b>	<b>YTD</b>
Absolute	-16.7%	N/A	N/A
Relative to VNI	-13.7%	N/A	N/A

## SECTOR OVERVIEW

### ***Stable growth for the future***

*Demand for magnet wire had been increasing at 20%-22% rate during the period 2002-2007.*

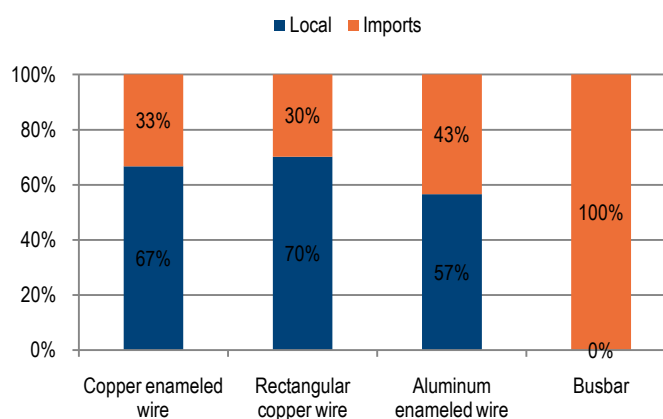
Magnet wire is normally used in electric motors, transformers and other electric equipments and appliances. The sector growth is linked directly to industrial production and partially to construction industry. During the period from 2002-2007 industrial production had been increasing steadily at 17% yoy on average. Accordingly, consumption for electric motors and transformers – two major products using magnet wire – had been growing at 33% and 27% yoy on average, respectively during the same period. As a result, demand for magnet wire also grew at 20%-22% in the past years. In 2008 and 2009, due to the economic crisis the industrial production growth had been reduced to 14.6% and 7.6%, respectively leading to a lower growth for the magnet wire sector at around 17%-9%.

*Growth rate for the sector is expected to remain in the 18%-22% range in the next 5 years.*

In 2010 industrial production is forecasted to grow by 12% and construction to grow by 20% over 2009. As there are increasing demand for electricity distribution and electrical equipment, we forecast a growth of approximately 18%-20% for magnet wire in general. Growth rate for the sector is expected to remain in the 18%-22% range in the next 5 years.

### ***Imports are required and currently hard to substitute***

**<Figure 1>** Market share of domestic consumption of magnet wire



Source: NHW

Currently domestic supply of magnet wire focuses on lower quality products in which supply already exceeds demand. However, in higher quality segment such as high-temperature (>180°C) enameled wire and bus bar there are few domestic suppliers which requires the need for imports. Moreover, FDI companies – mostly Japanese ones – are sometimes required to import from suppliers assigned by their parent companies.

In the long run, localization of materials from these FDI companies is expected to emerge due to proximity, convenience and cost-efficiency.

### ***Substantially subjective to volatility in copper price and exchange rate***

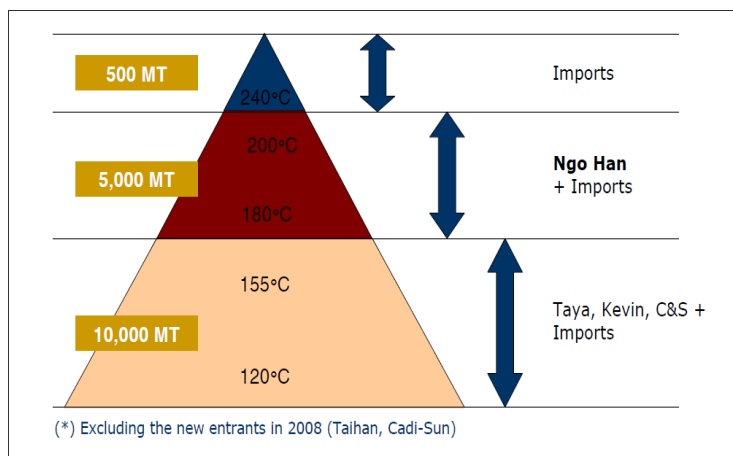
Copper is the major input material for this sector accounting for almost 80% of production cost and it mostly comes from imports. Dramatic fluctuation in copper price will lead to significant impact on the bottom line of companies in the sector. Ngo Han and other cable and wire companies experienced negative impact on their earnings when copper price on London Metal Exchange (LME) dropped 63.4% in 2H2008. This dip pulled the selling price down accordingly while inventory was purchased at much higher prices.

Similarly, the depreciation of the VND against the USD increases financial cost for the companies to pay their suppliers. In 2008 NHW incurred VND25bn financial expense due to FX rate difference. That amount for TAYA in 2008 was VND47bn.

## COMPANY ANALYSIS

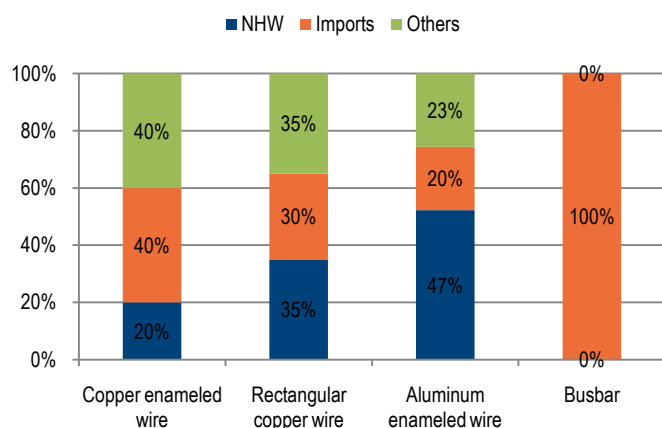
### ***Market leader targeting higher-end segment with differentiating strategy***

**<Figure 2> Enameled wire grade and supply structure**



Source: NHW

**<Figure 3> Market share by product**



Source: NHW

***NHW differentiates from others by producing consistently high quality products.***

There are more than 50 companies operating in the magnet wire sector with most of them having Taiwanese or Korean origins. NHW differentiates from others by producing consistently high quality products. Its products passed the quality audits conducted by overseas customers such as GE, Sony, Samsung, NEC-Tokin, etc. Locally, the company is the only one who can produce high-temperature enameled wire and busbar. Therefore competition in its segment mostly comes from imports but NHW has

advantages with proximity, convenience and cost-efficiency. Its major direct competitors include TAYA (Taiwanese), KEVIN (Korean) and CADIVI (Vietnamese). All of them are competing in the lower-temperature enameled wire. Among the direct competitors only TAYA is currently listed on HSX – the same bourse with NHW.

### **Consistently strategic investment in product development**

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*Strong competence and strategic investment in product development promise consistent revenue growth in the long run.*

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Being incorporated in 1987, NHW has more than 20 years of operation in the sector which enables the company to accumulate expertise and competence. Currently its production technologies and facilities as well as quality control are in par with Taiwanese and Korean counterparts. The company's products are favored by FDIs and overseas customers who usually account for more than 20% of its revenue. NHW also consistently invests in product development. Initially, NHW only had round enameled copper wire and rectangular copper wire, which still remain the company's core products today. The company extended product portfolio to include semi-finished products such as copper rod and round bare copper wire (from the same high quality copper material with enameled wire) which are cheaper, easier but also lower profitability. These products are highly demanded by the domestic market and enable NHW to clear inventory quicker when price movement is unfavorable.

Later, NHW added aluminum as another material for its product offering. Recently (12/2009), it has launched busbar as the latest addition to its range. Currently domestic consumption of busbar (>1,200 tonnes/year) comes entirely from imports. With its competitive advantages, NHW is expected to generate substantial revenue in the future by penetrating this segment. The company is also planning to launch electric motors and fans (utilizing its magnet wires) and switchboards (utilizing its busbar). However those are still in R&D phase. We believe these strategic investments in product development could promise consistent revenue growth for the company in the long run.

Company's forecast of busbar production					
Item	Unit	2010F	2011F	2012F	2013F
Production	MT	300	600	900	1,200
Revenue	USD	2,721,875	5,443,751	8,165,626	10,887,502
Market share	%	22%	40%	53%	64%

Source: NHW

### **Hedging measures to mitigate sector risks suggest stable earnings in the future**

Like other companies in the sector NHW is subject to fluctuation risk in copper price and exchange rate. In 2006 the company earned significant arbitrage profit by stocking materials (high inventory day) in the first half and sold products at much higher price.

This explains the impressive gross margin in 2006. However, in 2007 there were major fluctuations in copper prices occurring frequently which led to a drop in gross margin. In 2H2008 the dramatic drop in copper price pulled domestic selling price of all copper-based products. As the inventory was purchased at much higher price in 1H2008, NHW had to make provision which led to a further reduction in gross margin.

*Hedging measures help mitigate risks and smooth out earnings over the years.*

As NHW is not in the business of copper speculation, mitigation strategies for the risk of copper price fluctuation has been applied by the company, including:

- Swap contract (Copper Risk Management) with ANZ;
- Back-to-back processing with large orders;
- Materials procurement matching with fixed orders at monthly average price;
- Reducing inventory day; and
- Maintaining inventory level at equal or lower than current price.

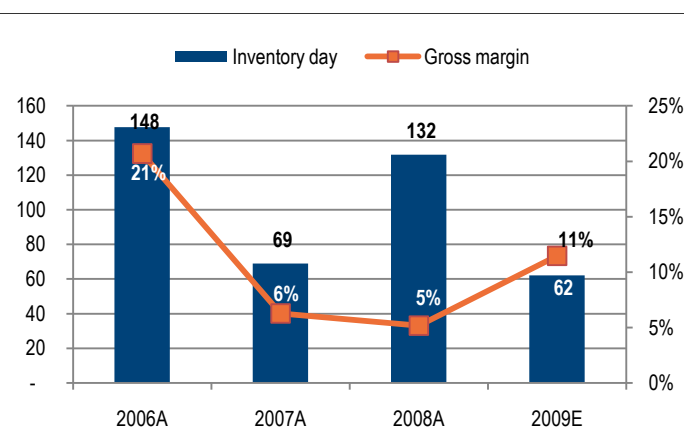
In 2009 the company partially benefited from importing materials at low price in Q4/2008 which led to an increase in gross margin to 11%. Since 2010 onwards the company is forecasted to reach to 13% gross margin level with contribution from busbar and other higher margin products such as motors, fans and switchboards. With the hedging measures, earnings are expected to stabilize at around 13% over the years.

<Figure 4> LME copper price over years



Source: Bloomberg

<Figure 5> Inventory day and gross margin over years



Source: NHW

## EARNINGS FORECAST

**Income Statement items**

With sound fundamentals together with the key highlights above we expect NHW to outperform the sector average of 18%-22% growth yoy. In 2010 NHW will have the whole year contribution from busbar. Thus we expect revenue to grow by 26% yoy and gradually go down to 16% by 2015 due to higher competition and saturation.

Gross margin is expected to gradually improve and stable thanks to the hedging measures and the launch of higher margin products. Other expenses are kept at approximately same level relative to sales. The tax rate applicable since 2010 onwards will be 25%.

Year (end Dec 31)	Unit	2008A	2009E	2010F	2011F	2012F	2013F
Net revenue	VNDbn	843.3	910.7	1,147.5	1,422.9	1,735.9	2,083.1
<i>Growth</i>	%	0.9%	8.0%	26.0%	24.0%	22.0%	20.0%
Gross profit	VNDbn	43.7	104.4	143.4	185.0	225.7	270.8
<i>Gross margin</i>	%	5.2%	11.5%	12.5%	13.0%	13.0%	13.0%
Financial revenue	VNDbn	10.9	8.7	12.6	15.7	19.1	25.0
Financial expense	VNDbn	37.1	52.9	67.7	83.9	102.4	122.9
Selling expense	VNDbn	6.9	7.5	9.4	11.7	14.3	17.1
Administration expense	VNDbn	7.0	8.0	10.1	12.6	15.3	16.7
Operating profit	VNDbn	3.6	44.6	68.8	92.4	112.7	139.1
<i>Operating margin</i>	%	0.4%	4.9%	6.0%	6.5%	6.5%	6.7%
NPBT	VNDbn	3.7	54.0	78.2	101.8	122.2	148.5
NPAT	VNDbn	2.1	44.2	58.7	76.4	91.6	111.4
<i>Growth</i>	%	-93.6%	1961.2%	32.7%	30.2%	20.0%	21.6%
<i>Net margin</i>	%	0.3%	4.9%	5.1%	5.4%	5.3%	5.3%
EPS	VND	94	1,926	2,502	3,148	3,670	4,323
<i>Growth</i>	%	-93.6%	1940.8%	29.9%	25.8%	16.6%	17.8%

**Balance Sheet items**

Trade receivable day is maintained at the 2009 level while we increase the inventory day to 70-75 as we believe this is a healthy level and necessary to meet potentially more large orders as the economy picks up. Historically, trade payable day was averaged at 7 which is a good level for working capital management so we gradually rise trade payable day to this target. Short-term debt is reduced to 50%-52% as business results bring sufficient cash for the company. Except for the USD439k invested

for the busbar production line, we assume NHW will reach full capacity in 2012 therefore the company will incur large CAPEX to increase its capacity. In other years there are only small CAPEX is required annually for maintenance and other miscellaneous installations.

Year (end Dec 31)	Unit	2008A	2009E	2010F	2011F	2012F	2013F
<b>Asset</b>	<b>VNDbn</b>	<b>548.2</b>	<b>456.8</b>	<b>484.9</b>	<b>571.9</b>	<b>670.2</b>	<b>784.1</b>
Current	VNDbn	477.9	384.9	413.1	506.1	598.1	715.9
<i>Cash &amp; cash equivalents</i>	<i>VNDbn</i>	<i>54.6</i>	<i>91.5</i>	<i>43.7</i>	<i>49.3</i>	<i>40.8</i>	<i>35.8</i>
<i>Short-term investments</i>	<i>VNDbn</i>	<i>0.3</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Receivables</i>	<i>VNDbn</i>	<i>123.0</i>	<i>152.8</i>	<i>172.9</i>	<i>214.4</i>	<i>261.6</i>	<i>325.3</i>
<i>Inventories</i>	<i>VNDbn</i>	<i>288.6</i>	<i>137.3</i>	<i>192.4</i>	<i>237.2</i>	<i>289.3</i>	<i>347.2</i>
<i>Other current assets</i>	<i>VNDbn</i>	<i>11.4</i>	<i>3.3</i>	<i>4.2</i>	<i>5.2</i>	<i>6.3</i>	<i>7.6</i>
Non-current	VNDbn	70.3	71.9	71.8	65.8	72.1	68.2
<i>Fixed assets</i>	<i>VNDbn</i>	<i>71.3</i>	<i>69.3</i>	<i>70.7</i>	<i>70.6</i>	<i>64.7</i>	<i>70.9</i>
<i>Other non-current assets</i>	<i>VNDbn</i>	<i>1.0</i>	<i>1.2</i>	<i>1.2</i>	<i>1.2</i>	<i>1.2</i>	<i>1.2</i>
<b>Liability</b>	<b>VNDbn</b>	<b>285.1</b>	<b>211.0</b>	<b>210.9</b>	<b>260.4</b>	<b>319.4</b>	<b>389.0</b>
Current	VNDbn	281.4	209.8	209.7	259.2	318.3	387.8
<i>Short-term debts &amp; borrowings</i>	<i>VNDbn</i>	<i>88.5</i>	<i>241.7</i>	<i>172.7</i>	<i>168.5</i>	<i>208.4</i>	<i>252.1</i>
<i>Trade payables</i>	<i>VNDbn</i>	<i>1.6</i>	<i>30.3</i>	<i>7.4</i>	<i>13.8</i>	<i>17.0</i>	<i>24.8</i>
<i>Other current liabilities</i>	<i>VNDbn</i>	<i>44.2</i>	<i>9.4</i>	<i>29.7</i>	<i>27.5</i>	<i>33.9</i>	<i>41.4</i>
Non-current	VNDbn	3.7	1.1	1.1	1.1	1.1	1.1
<i>Long-term debts &amp; borrowings</i>	<i>VNDbn</i>	<i>10.0</i>	<i>3.7</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Other long-term liabilities</i>	<i>VNDbn</i>	<i>-</i>	<i>-</i>	<i>1.1</i>	<i>1.1</i>	<i>1.1</i>	<i>1.1</i>
<b>Equity</b>	<b>VNDbn</b>	<b>263.0</b>	<b>245.8</b>	<b>274.0</b>	<b>311.6</b>	<b>350.8</b>	<b>395.2</b>
Share capital	VNDbn	227.2	229.5	234.4	242.6	249.7	257.7
Retained earnings	VNDbn	35.8	16.3	39.6	69.0	101.1	137.5

Source: NHW, MAS

## VALUATION

### *Market multiplier method*

Currently TAYA is the only direct competitor listed on the HCM stock exchange with ticker TYA. However in the electrical component and equipment sector there are a few companies producing electrical and telecom cables which are similar to NHW. We pick CSG, VHG as they have relatively the same asset base and market capitalization. We do not include SAM in our comparison as it is significantly larger in size.

Items	Unit	NHW	TYA	CSG	VHG
Sales	VNDbn	910.7	752.0	370.6	189.9
Gross profit	VNDbn	104.4	89.4	46.1	23.4
NPAT	VNDbn	44.2	3.6	29.6	2.1
Gross margin	%	11.5%	11.9%	12.4%	12.3%
NPAT margin	%	4.9%	0.5%	8.0%	1.1%
Assets	VNDbn	456.8	610.7	603.8	528.8
Equity	VNDbn	245.8	189.3	510.5	436.7
ROA	%	9.7%	0.6%	4.9%	0.4%
ROE	%	18.0%	1.9%	5.8%	0.5%
Price as at 09/02/2010	VND	22,000	8,300	11,700	11,700
Mkt cap	VNDbn	504.9	231.5	325.6	292.5
2009E P/E	x	11.4	64.3	11.0	139.3
2009E P/B	x	2.0	1.2	0.6	0.7

Source: NHW, TYA, CSG, VHG

NHW has the lowest gross margin compared to its peers but it controls financial and SGA expenses more effectively. As a result its net margin is higher than TYA and VHG. We think the P/E ratio does not reflect the fair value of TYA and VHG as their price level is significantly higher than their earnings but it is supported by their book value. Therefore we exclude TYA and VHG in our comparison. 2009 P/E for NHW is slightly higher than that of CSG which we think reasonable given NHW having the higher NPAT margin. The weighted average 2009 P/E for both NHW and CSG is 11.3x. Historically the average P/E for the Industrial sector fluctuated around 12x – 14x. Current average P/E for the Industrial sector is roughly 13.4x (Source: Stox). Within the Industrial sector, NHW has a relatively small-to-medium scale and the magnet wire segment itself also has moderate size, growth together with substantial risks. Accordingly we think current P/E level reflects the fair value of the company. Based on the Company's target and our



forecast, NHW could reach a 2010 EPS of VND2,502 equivalent to a P/E level of 8.6x. This is a reasonable P/E level for investment.

The P/B ratio is commonly used to value manufacturing companies, especially their low level “supporting” price. The weighted average P/B across the four companies is 1.2x. As NHW produces the highest equity returns we believe a premium is reasonable. Historically the average P/E for the Industrial sector fluctuated around 1.5x – 2.5x. Current average P/E for the Industrial sector in general stands at 2.0x (Source: Stox). Accordingly, we think the current 2009 P/B level of 2.0x also reflects the fair value of the Company. In our forecast, 2010 Book value per share is VND11,689 therefore NHW is currently traded at 2010 P/B of around 1.8x which does not deviate far from the 2009 P/B level.

## CONCLUSION

NHW was first listed on HSX on 26/01/2010 and closed at VND26,400/share. The price since then went down by 16.7% by end of today which underperforming the VN-Index by 13.65% within the same period. It is likely that investors considered the stock to be overpriced given the sector risks and the low liquidity. Major shareholders include founder, company's executives, BIDV, VietCapital and Mekong Capital who collectively hold more than 90% of the company. Institutional investors acquired the stocks more than 1 year ago. So it is possible that the price can go down once they decide to realize the investment.

Using the market multiplier method we suppose NHW is currently traded at its fair value based on 2009 P/E and 2009 P/B. The estimated 2010 P/E level of 8.6x indicates that NHW might be worth investment consideration. However, given the moderate growth level of the sector and the specific risks the stock seems less attractive compared to several other stocks in the market.

## Disclosure Appendix

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