J.P.Morgan

Asia Pacific Equity Research
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Company Visit Note

Kinh Do Corporation

KDC is the leading confectionery company in Vietnam with major market share in all categories except candy. 9M08 sales grew 21% Y/Y supported by ASP increase but profit margins in the period were squeezed due to a lag in price increases to cover a rising cost burden.

Key takeaways from the meeting:

- **Leading market share and strong distribution networks:** KDC has one of the largest confectionary distribution networks in Vietnam, with potential for the distribution of new products. Its market share has increased to 40% in 9M08 from 35% in FY07, according to management.
- **Plans to become a diversified F&B group:** The company aims to become a diversified F&B company, building both horizontal and vertical integration through acquisitions. Management said it is considering doing OEM for global brand names in its new factory to improve capacity utilization. The company has high exposure to property (44% of shareholders' equity as of end-September 2008), and this could crowd out its core business expansion.
- **Valuation and stock performance:** The stock trades at a 12-month trailing P/E of 8.3x. KDC has underperformed the index by 16.4% in the past month, or fell 40.5% in absolute terms.

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Reuters: KDC.HM; Bloomberg: KDC VM
VND in millions, year-end December

	FY05	FY06	FY07
Sales	798,618	998,150	1,230,802
Net income	94,757	170,666	224,138
EPS (VND)	2,437	3,591	4,096
DPS (VND)	1,600	1,800	1,800
Net debt (cash)/equity (%)	23.0	28.7	Net cash
Sales growth (%)	11.1	25.0	23.3
Net profit growth (%)	16.9	80.1	31.3
EPS growth (%)	4.0	47.4	14.1
ROE (%)	24.7	31.6	14.8
P/E (x)	14.0	9.5	8.3
P/B (x)	2.7	2.8	0.8
Dividend yield (%)	5.2	5.8	5.8

Source: Company reprots, Bloomberg. Per share data is adjusted for 20% share dividend payment in July 2008.

Vietnam

Linh Truc Nguyen[AC]

linh.t.nguyen@jpmorgan.com

J.P. Morgan Securities (Asia Pacific) Limited

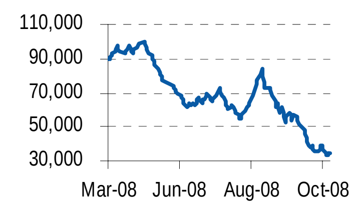
Sriyan Pietersz[AC]
(662) 684 2670
sriyan.pietersz@jpmorgan.com

JPMorgan Securities (Thailand) Limited

KDC VM, Not Covered
Confectionery

VND34,000, October 31, 2008

Share price performance
VND



Source: Bloomberg.

One-year price performance

	1M	3M	12M
Absolute (%)	(40.5)	(46.7)	(81.7)
Relative (%)	(16.4)	(25.7)	(37.3)

Source: Bloomberg.

Company data

52–week range (VND)	182,787-33,000
Mkt cap. (VND B)	1,907
Mkt cap. (US$MM)	113.3
Shares O/S (MM)	56.1
Free float (%)	100
Daily volume (MM)	0.1
Daily liquidity (US$MM)	0.3
Exchange rate (VND/US$)	16,830.0
Index: VNI	347.1
Year-end	December

Source: Bloomberg.

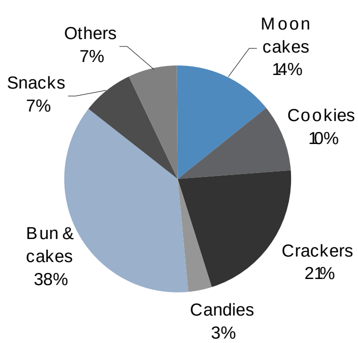
See page 7 for analyst certification and important disclosures, including non-US analyst disclosures.

Key takeaways from the meeting

Company description:

Established in 1993, Kinh Do Corporation (KDC VM) is now the leading confectionery company in Vietnam with 40% market share as of end-September 2008. The company was listed on HOSE in 2005. The founding Thanh family still holds 62% of KDC through Kinh Do Holdings and in their name. Kinh Do Holdings has four subsidiaries including confectionery (KDC), retailing, property, and financial services.

Figure 1: FY07 sales breakdown



Source: Company reports.

20.7% sales growth in 9M08 on strong moon cake sales

Kinh Do Corporation (KDC VM) had a sales growth of 20.7% in 9M08; however, its net profit prior to an adjustment of minority interest dropped by 15.1% Y/Y.

- Sales growth in 9M08 of 20.7% Y/Y, was an improvement from sales growth of 12% Y/Y in 6M08, and was mainly due to strong moon cake sales in the third quarter. This year, KDC manufactured around 1,500 tons of moon cakes, nearly triple that of other competitors; sales of moon cakes grew 25% this year due to an ASP increase. Moon cake sales were 105.8% Q/Q and contributed to 355.3% of the net profit growth in 3Q08.
- According to management, there was strong growth across the key product lines, although KDC's sales breakdown for 9M08 is not available; however, the company reports that the sales growth trend of 8M08 was strong across key products except for candies. Total sales in 8M08 grew by 27%, driven by cookies with the strongest sales growth of 80%. The growth of cookies in the 8M08 period was due to the growth of moon cakes as well as successful launches of some new cookies during the period, most notable among them is First Pie. Buns followed with 39% sales growth, while cakes sales rose 19%. Snacks and crackers of KDC remained one of the favorite choices of kids and teenage customers in Vietnam, according to the company, growing mainly on volume growth by 9% and 5% Y/Y, respectively, in 8M08. As Vietnamese customers tend to consume less sweet and sugar products, KDC candy sales dropped by 18% Y/Y in 8M08.
- The company has finished the relocation to the new factory in Binh Duong, which is now running at around 40% of its designed capacity. The company expects to raise the utilization to 60% by this year end and fully utilize it in 2.5 years by doing some OEM business with global brand names. The old factory site in Thu Duc will be used as an office building, which KDC expects to build in 1Q09.
- KDC's market share increased to 40% by the end of September from 35% in FY07. KDC said that given that almost all foreign brand names and small local brand names delayed their market penetration plans, KDC can enhance its market share further.

Table 1: KDC—9M08 financials

VND in millions, YE Dec	Jun-Sep 08	Jun-Sep 07	Y/Y change	Q/Q change	Sep-08	Sep-07	Y/Y change
Net sales	532,232	407,718	30.5%	105.8%	1,046,095	866,992	20.7%
COGS	376,233	264,532	42.2%	80.4%	769,354	623,093	23.5%
Gross profit (loss)	155,998	143,186	8.9%	211.9%	276,741	243,899	13.5%
Selling expenses	40,532	31,626	28.2%	32.8%	79,725	64,201	24.2%
G&A expenses	32,548	18,569	75.3%	43.5%	69,739	47,641	46.4%
Operating profit (loss)	82,919	92,991	-10.8%	-2709.4%	127,277	132,056	-3.6%
Non operating profit (loss)	(20,970)	(4,563)	359.5%	-198.0%	6,157	11,973	-48.6%
Interest expenses	20,015	7,238	176.5%	114.7%	36,979	19,093	93.7%
Extraordinary profit (loss)	7,870	3,411	130.7%	4130.7%	7,807	20,883	-62.6%
EBIT	60,993	91,102	-33.1%	24.7%	176,569	175,094	0.8%
EBT	69,818	91,839	-24.0%	279.4%	141,240	164,912	-14.4%
Corporate income tax	(1,912)	-		-172.3%	1,173	-	
Net profit (loss)	71,730	91,839	-21.9%	355.3%	140,067	164,912	-15.1%
Margin			% pct change				% pct change
Gross margin	29.3%	35.1%	-5.8%	10.0%	26.5%	28.1%	-1.7%
EBIT margin	11.5%	22.3%	-10.9%	-7.5%	16.9%	20.2%	-3.3%
Net margin	13.5%	22.5%	-9.0%	7.4%	13.4%	19.0%	-5.6%
Major expenses as % of sales							
Selling expenses	7.6%	7.8%	-0.1%	-4.2%	7.6%	7.4%	0.2%
G&A expenses	6.1%	4.6%	1.6%	-2.7%	6.7%	5.5%	1.2%

Source: Company reports.

Profitability

Returns

ROE dropped to 14.8% in FY07 and 8% in 9M08 on an annualized basis from 31.6% in FY06 due to the impact of dilution. KDC granted 20% bonus shares to its existing shareholders in July 2008 to increase its charter capital to VND561 billion.

Squeeze on margin with the new factory operation and a lag in price increases

KDC has made an effort to hedge against raw material price increases and improve the product mix portfolio. However, the company has just moved its production to its new factory and costs have risen due to higher depreciation. Moreover, given that inflationary pressure was strong in 9M08, KDC said it can partly pass the rise in costs to its customers with a lag in time. Except for the third quarter when sales from the high-margin moon cakes helped it achieve a 10% improvement in gross margin, 9M08 financials showed that gross margin fell by 1.7% Y/Y in the overall nine months of 2008.

Net profit margin in 9M08 declined by 5.6% Y/Y given the 93.7% Y/Y rise in interest costs and higher MTM write-downs for its financial investments, around VND29.4 billion in 9M08, up from VND4.9 billion at the end of FY07.

Table 2: KDC—8M08 performance

	% Y/Y growth	Gross margin (%)	Net margin (%)
Cookies	80%	47%	34%
Crackers	5%	30%	12%
Cakes	19%	19%	6%
Snacks	9%	18%	1%
Buns	39%	16%	1%
Candies	-18%	6%	-20%
TOTAL SALES	27%	27%	15%

Source: Company reports.

Outlook

KDC plans to increase sales by 30% Y/Y in FY08 to VND1,600 billion and pre-tax profit by 21% Y/Y to VND270 billion. The company hopes to achieve this through increased product coverage to 120 supermarkets, an expanded network to 180 main distributors, utilizing the full capacity of its new factory in Binh Duong, and helping affiliated companies expand their capex, facilitating increased product coverage to more cities and more shops, and effectively enhance market share at 40% in FY08. The company will focus on premium products for the high-end market segment locally and in export markets.

As for investments in 2008, KDC intends to reserve VND437 billion to invest in its affiliated companies' expansion projects:

- VND160 billion for Kinh Do Binh Duong.
- VND69 billion for Vinabico.
- VND8 billion for Tribeco Binh Duong.
- VND200 billion for M&A in other food producers.

KDC also plans to invest another VND1,051 billion in three property projects. The company expects all three projects to be completed in 1-4 years and will be implemented by Kinh Do Real Estate. The total investments by KDC would be around VND1,051 billion or US$64.6 million. There is a large supply of residential and office projects in the pipeline amid a cooling property market, and the company has high exposure to property (44% of shareholders' equity as of end-September 2008).

Expansion through M&A towards a diversified F&B group

Kinh Do Holdings, the parent company of KDC has expanded through M&A deals into smaller-size food and beverages companies and is one of the market leaders in its relevant businesses. It has an ambition to become a leading food and beverages company in Vietnam. So far, the group has successfully bought stakes in Wall Ice Cream from Unilever Bestfoods to develop it into Kido Ice Cream; 55% of Tribeco (TRI VM), the number three beverage company in Vietnam after Coca-Cola and Pepsi Cola; a 30% stake in Nutifood, one of the top five local dairy companies in Vietnam; and 51% of Vinabico, a smaller confectionary player to jointly develop processed food products in Vietnam. KDC also partnered with Tribeco to build Tribeco Binh Duong and Northern Tribeco, which it hopes will help increase its production capacity and product coverage in the Eastern, Southern and Northern markets.

The next step, according to management, will be the long-awaited merger between KDC and North Kinh Do (NKD VN) and then mergers with Kido Ice Cream, Tribeco, Nutifood and Vinabico to form a complete F&B group. In our recent meeting with KDC, management indicated that it wants to merge NKD and KDC to fulfill its commitments to shareholders and strengthen the synergy between the two companies. However, despite the completion of all the paperwork, the company thinks this is unlikely to happen this year as the merger will be the first M&A on the HOSE and market conditions continue to remain unfavorable.

Capital raising/balance sheet

Given the share premium of VND1,700 billion from its private placements of 11 million shares in FY07, which KDC has not yet disbursed into new capex expansion or property projects, the company had a strong net cash position as of end of 2007. Net debt-to-equity increased to 6.7% by the end of September 2008, compared to 28.7% in FY06. The company just paid a 20% share dividend to its shareholders in July 2008 to raise its charter capital to VND561 billion. Total debt-to-equity was only 10% by the end of September 2008, down from 15% in FY07 and 38% in FY06, and most of its debt is short term for working capital.

KDC: Summary of historical financials

Profit and loss statement

VND in millions, YE December	FY05	FY06	FY07
Revenues	798,618	998,150	1,230,802
% change Y/Y	11.1	25.0	23.3
Gross margin (%)	28.8	28.2	26.2
EBITDA	142,822	245,471	344,627
% change Y/Y	20.5	71.9	40.4
EBITDA margin (%)	17.9	24.6	28.0
EBIT	112,101	211,138	306,881
% change Y/Y	47.1	88.3	45.3
EBIT margin (%)	13.9	13.2	12.5
Net interest	-18,263	-17,490	-31,710
Earnings before tax	107,612	170,031	222,480
% change Y/Y	21.2	58.0	30.8
Tax	12,856	(635)	(1,659)
as % of EBT	11.9	-0.4	-0.7
Net income (reported)	94,757	170,666	224,138
% change Y/Y	16.9	80.1	31.3
Shares outstanding (MM)	25	30	46
EPS (reported) (VND)	2,437	3,591	4,096
% change Y/Y	4.0	47.4	14.1

Cash flow statement

VND in millions, YE December	FY05	FY06	FY07
EBIT	112,101	211,138	306,881
Depreciation & amortization	na	34,334	37,746
Change in working capital	87,170	-32,482	-312,077
Taxes	12,856	-635	-1,659
Cash flow from operations	212,647	172,517	-50,193
Capex	-79,197	-24,351	-260,386
Disposal/ (purchase)	0	0	0
Net interest	18,263	17,490	31,710
Free cash flow	4,214	-10,753	449,561
Equity raised/ (repaid)	187,949	6,668	1,742,546
Debt raised/ (repaid)	-65,051	60,557	170,160
Other	-7,855	0	20,468
Dividends paid	-62,208	-85,536	-98,493
Beginning cash	9,391	44,724	50,826
Ending cash	44,724	50,826	530,438
DPS (VND)	1,600	1,800	1,800

Balance sheet

VND in millions, YE December	FY05	FY06	FY07
Cash and cash equivalents	74,532	142,935	1,052,956
Accounts receivable	215,980	195,881	560,318
Inventories	65,953	120,403	136,272
Others	3,562	1,028	5,082
Current assets	360,027	460,247	1,754,629
Long-term investments	131,350	178,777	797,350
Net fixed assets	268,202	258,219	480,860
Total assets	784,682	936,372	3,067,474
Liabilities			
Short-term loans	100,816	171,257	263,003
Payables	122,282	118,950	173,671
Others	10,896	13,564	31,126
Total current liabilities	233,995	303,771	467,800
Long-term debt	57,182	47,299	125,713
Other liabilities	0	0	0
Total liabilities	291,177	351,070	593,513
Shareholders' equity	493,505	585,303	2,453,494
BVPS (VND)	12,693	12,317	44,838

Ratio analysis

%	FY05	FY06	FY07
EBITDA margin	17.9	24.6	28.0
Operating margin	13.9	13.2	12.5
Net profit margin	11.9	17.1	18.2
SG&A/sales	14.8	15.0	13.7
Sales per share growth	-1.2	2.3	7.1
Sales growth	11.1	25.0	23.3
Net profit growth	16.9	80.1	31.3
EPS growth	4.0	47.4	14.1
Interest coverage (x)	6.1	12.1	9.7
Net debt to total capital	17.4	20.9	Net cash
Net debt to equity	23.0	28.7	Net cash
Sales/assets	114.7	116.0	61.5
Assets/equity	1.8	1.6	1.3
ROE	24.7	31.6	14.8
ROCE	19.5	29.0	16.8

Source: Company reports, Bloomberg.

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