HA TIEN 1 & HA TIEN 2 CEMENT JSC

SECTOR: BUILING MATERIAL

QUICK UPDATE

07/11/2009

Minh Nguyen

Analyst

minhnd@ssi.com.vn

M&A STORY

Used to be a state-owned business entity, Ha Tien Cement manufacturer was established in 1964 with a clinker production line in Kien Giang and a grinding plant in Thu Duc. In 1981, two lines split up to form Kien Luong Cement Manufacturer and Thu Duc Cement Manufacturer. In 1983, the two had merged before splitting up again in 1993, forming Ha Tien 1 Cement in Thu Duc and Ha Tien 2 Cement in Kien Giang. Among these two, Ha Tien 2 is capable of producing clinker while Ha Tien 1 is totally dependent on external supplies of clinker. For the time being, VICEM is aiming to unify its brand name by merging all its affiliates including Ha Tien 1 and Ha Tien 2. According to the proposal of advisor, Ha Tien 2's shares will be converted to Ha Tien 1 shares with conversion ratio of 1:1.

Who benefits from the acquisition?

Currently, Ha Tien 1 benefits more from the acquisition as the merger will deliver healthy financial statements and better cash flow to Ha TIen 1.

Ha Tien 1 will face lots of difficulties next year associated with the completion of Binh Phuoc grinding plant. It is unlikely for the plant to operate at full capacity right in the first year of operation since it would take time for the market to absorb all additional supply (2.2 Mta), not to mention technical problems. If Binh Phuoc plant (total investment is 4,800 billion VND) fails to maximize its capacity, Ha Tien 1's net profit will be adversely affected by heavy financial and depreciation expenses burden. Balance sheet also looks risky with dangerously high debt to equity ratio (about 5x). Moreover, cash generated from operating activities could be insufficient to finance principle payments, interest payments as well as working capital need.

Meanwhile, Ha Tien 2 is a company with high profitability (net profit margin is 12% while that of Ha Tien 1 is about 7%), healthy balance sheet (D/E is 1.1x) as well as abundant cash (cash and cash equivalent averages 200 billion VND). Moreover, Ha Tien 2 also has potential long term outlook as the company has been expanding its capacity to meet excessive demand in its consuming market.

Hence, on Ha Tien 1's perspective, the acquisition will be the cushion for the company in difficult situation next year as market risks will hamper the company's net profit and cash flow managementWhy.

Ha Tien 2 shareholders declined

In the short run, the acquisition is not bringing any significant benefits to Ha Tien 2. The company's shareholders may not recognize synergies created after the acquisition. Also, the more complicated management system and the change in brand name after the acquisition raise concerns on the company's competitiveness. The most vivid synergy that shareholder might expect is that Ha Tien 2 will feed clinker for Ha Tien 1, thus stabilizing input materials and reducing production cost. However, with currently designed capacity of 900,000 tons of clinker annual and 1,000,000 tons of cement annual, clinker provided by Ha Tien 2 will just be modest. The synergy will be more significant in 2011, when Ha Tien 2's Kien giang 2.2 production line is completed, with installed capacity of 1,260,000 tons of clinker annual and 600,000 tons of cement per year.

Acquisition: success and failure

All things considered, the 1:1 conversion ratio does not seem attractive to Ha Tien 2's shareholders, especially when market prices of these two are fairly similar. With VICEM's long term strategy to unify its brand name, the acquisition will be likely to succeed. However, in the worst scenario when the acquisition fails, the orientation of Ha Tien 1 and Ha Tien 2 being market leaders in Eastern South and Western South regions is acceptable for Vietnam Cement industry given the two markets are quite separated.

This report was be publish on VIR – 07.11.09

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CONTACT

Hang Le	Managing Director	hangltl@ssi.com.vn
Minh Nguyen	Analyst	minhnd@ssi.com.vn