13TH MAY 2008

Refrigeration Electrical Engineering Corporation

REE Corp • REE

Target Price: VND47,700 • US$2.96 (+9.2%)

REE Corporation

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Ownership

State	6.07%	3,476,140
Foreign	49.00%	28,057,588
Domestic	44.93%	25,726,660
Outstanding shares		57,260,388

REE • 52-week trading history (adj.)

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1QFY08:Value Emerges Despite Poor Financial Results HOLD

Company's Statistics

Exchange	Ho Chi Minh City Stock Exchange	Last price	VND 43,700 • US$ 2.71
Sector	Multi-industry	BPS	VND 33,077 • US$ 2.05
Index weight	1.1%	EPS	VND 5,083 • US$ 0.32
Market cap.	VND 2,513bn • US$ 0.16bn	EPS trailing	VND 1,935 • US$ 0.12
52-week range	VND 43,700 – VND 176,000	Hist DPS	n.a..
30-day average daily turnover	US$0.3mn	Dividend yield	n.a..
Beta	1.1	Trailing PER	23.0x
ROCE	17.0%	P/BV	1.3x

Quarterly Results Highlights

- *Losses in 1QFY2008!!!* Refrigeration Electrical Engineering Corporation's (REE) quarterly results came in below our expectations. The Group reported a loss before tax (LBT) of US$6.6mn for the 1QFY08, mainly due to the impairment of short term financial investment amounting to US$9.9mn.
- *Double digit growth in revenues.....* On a y-o-y basis, the Group's major operations, mechanical and engineering (M&E), air-conditioning systems and real estate recorded double digit revenue growth for the 1QFY08. M&E had the strongest top line growth of 58.3%, followed by real estate (51.0%) and air-conditioning system (26.1%).
- *......but disappointing profit before tax (PBT) growth!!!* Nonetheless, real estate is the only operations which registered double digit growth in PBT on a y-o-y comparison. PBT growth of air conditioning systems moderated to 4.8% while PBT of M&E contracted by 25.3% adversely impacted by the rising costs of production.

Breakdown of Revenue and PBT for 1QFY08 (US$mn)

	Revenue			PBT		
	1Q 2007	1Q 2008	Change YoY %	1Q 2007	1Q 2008	Change YoY%
M&E	6.6	10.4	58.3%	0.7	0.6	-25.3%
Air-conditioner	2.8	3.6	26.1%	0.5	0.5	4.8%
Real Estate	2.1	3.1	51.0%	1.3	1.7	35.6%
Financial Investment	-	-	-	5.4	(9.4)	-274.1%
Others	-	-	-	0.1	0.1	4.0%
TOTAL	11.5	17.1	49.1%	8.0	(6.6)	-182.4%

Quarterly Results (US$mn)	1Q 2007	4Q 2007	1Q 2008	Change QoQ %	Change YoY %
Revenue	11.5	25.4	17.1	-32.7%	49.1%
Gross Profit	3.8	6.5	4.6	-30.3%	18.9%
Operating Profit (ex. net financial income)	2.6	4.0	2.8	-30.3%	6.6%
Operating Profit	10.4	5.9	(6.7)	-212.6%	-164.3%
Pre-Tax Profit	8.0	6.2	(6.6)	-207.0%	-182.4%
Gross Profit Margin (%)	33.5%	25.8%	26.7%	3.6%	-20.3%
Operating Margin (%)	90.3%	23.3%	-39.0%	-267.4%	-143.2%
Pre-tax Margin (%)	69.8%	24.3%	-38.6%	-259.0%	-155.3%

- *Real estate to be the main driver….* With the full year earnings contribution from E-town 2 coupled with the expected completion of E-town 3 and 4 by the second half of 2008, we expect the revenue contribution from real estate operations to enjoy double digit growth in 2008. Besides that, we foresee that there could be an upside potential for its office rental rate in the medium term in view of the current supply shortage of office buildings in Ho Chi Minh City.
- *Financial holding gain is still positive, but market value has dropped drastically.* We gather from management that the market value of REE's short and long term investment holdings was about US$107mn at the end of March, translating to an unrealized investment surplus of US$21mn (net of the impairment loss of US$9.9mn) compared with its book value of US$86mn. The unrealized investment surplus arises from the Group's long term investment holdings.
- *Aggressive management forecasts.* Management has set an aggressive PBT target of US$24.2mn for 2008 in its recent annual general meeting (AGM). We believe that the target is aggressive given the expected slower earnings growth in its M&E operations. Furthermore, we believe that the continued weakness in the equity market may hinder the Group's ability to recoup its US$9.9mn impairment in short term investment provided in the 1QFY08.
- *Slashing our earnings forecast to US$4.9mn for FY2008 to reflect estimated financial loss!!* We have slashed our FY08 net earnings forecast for the Group by 81% to US$4.9mn. Our earnings downgrade mainly stems from our revised estimate for financial income since we have inputted a financial loss of US$9.9mn as per registered by the Group in this quarter compared with the financial gains of US$10mn initially assumed for 2008. We are skeptical about the ability of the Group to reverse from a financial loss position as per this quarter to a financial gain by the end of 2008. This is because REE has aggressively accumulated stocks from 1QFY07 to 3QFY07 when the VN Index was trading around 1,000 points. Furthermore, we understand that the Group's investment in Sacombank (STB) contributes to most of its present unrealized investment surplus. Therefore, we believe that REE, as a strategic shareholder of STB, is unlikely to realize any large amount of investment holdings in STB in the near term. Nonetheless, we wish to forewarn that the Group's financial income is largely dependant on the performance of equity markets, therefore any significant improvement in the equity market going forward would have a major impact on the Group's earnings.
- *Foreign interests remain high!!!* REE's stock price has declined by 68% year-to-date underperforming the VN Index which has fallen 45%. Even with the prolonged market correction, foreign interest on the Group remains high with foreign ownership sustained at the maximum 49% level.

Valuation

Switching to SOP valuation. We have decided to adopt a sum of parts (SOP) methodology to better reflect the Group's increasingly diversified business operations:

- *M&E:* We have selected Alphanam (ALP.VN) and Searefico (an OTC stock) as the sector comparables to estimate the average sector PER for REE's M&E operations. We have applied a 10% premium to derive a FY08 PER of 8x for the M&E operations taking into account the Group's dominant position in the sector.

REE M&E's Comparables

	Price per share (US$)	Market cap (US$mn)	Expected net profit FY08 (US$mn)	Expected PER
Alphanam	1.1	43.4	7.0	6.2
Searefico	3.1	14.4	1.7	8.5
Average				7.3

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- *Air-conditioning system:* We have derived expected PER of 10.6x, which represents a 30% discount of an average PER of the global air-conditioning system manufacturers (Reuters, SIC 3632). We believe that the 30% discount is justifiable given its small business scale and low competitive strength.
- *Real estate:* We have valued REE's real estate operations using discounting cash flows (DCF) model applying a perpetuity growth rate of 5% upon 2011 and a cost of equity of 17%.

REE's real estate FCFE valuation

(in US$mn)	2008	2009	2010	2011
EBT	8.7	13.2	15.8	16.6
Taxes	(2.2)	(3.3)	(4.0)	(4.2)
Net Income	6.5	9.9	11.9	12.5
Add: Depreciation	1.5	2.2	2.9	4.5
Less: Capex	(17.9)	(6.9)	(6.2)	(0.5)
FCFE	(9.8)	5.2	8.6	16.5
Terminal value				144.5
Sum of Cash Flows	(9.8)	5.2	8.6	161.0
Equity Value	86.6			

- *Investment Portfolio:* We have estimated the market value of REE's investment portfolio to be US$97.1mn as of 8th of May 2008, down from US$106.8mn announced in 31 March 2008, to reflect the continued downtrend in equity market and the decline in STB's share price. REE owns around 25mn STB shares, which represents the largest component of the Group's investment portfolio. Conservatively we have further applied a 20% discount rate on our estimated value of the investment portfolio.

Target price at US$2.97. We have derived a target price for REE at VND47,700 (US$2.97). Our target price is based on a 20% discount to our SOP valuation of VND59,700 (US$3.71). This implies an expected FY08 PER of 11.6x based on an expected core EPS of US$0.23 (excluding financial loss of US$9.9mn estimated for FY08), which we deem to be reasonable. HOLD.

SOP Valuation	Expected FY08 Net Profit (US$ mn)	PER multiple	Value (US$ mn)
REE M&E	2.7	8.0x	21.6
Air-conditioning system	2.0	10.6	21.5
Real estate	FCFE @ 17% cost of equity		86.6
Investment portfolio	Market value @ 20% discount		83.7
Total Value			213.4
No. of shares outstanding (mn)			57.51
Value per share			$3.71

Income statement (US$mn)	2004A	2005A	2006A	2007A	2008F
Revenue	22.6	24.1	51.2	60.7	73.1
Gross profit	7.5	8.6	13.5	18.5	22.9
Operating profit (ex. net financial income)	4.2	4.8	9.6	12.1	15.2
Operating profit	4.0	5.4	18.4	23.9	6.1
Profit before tax	4.0	5.0	18.6	24.4	6.5
Net profit	3.5	4.2	13.8	18.1	4.9
Gross margin (%)	33.0%	35.7%	26.3%	30.5%	31.4%
Operating margin (%)	17.6%	22.4%	36.0%	39.4%	8.4%
Pre-tax margin (%)	17.8%	20.9%	36.3%	40.1%	8.9%
Net margin (%)	15.5%	17.6%	27.0%	29.8%	6.6%
Revenue growth (%)	-2.3%	6.5%	112.8%	18.6%	20.5%
Gross profit growth (%)	11.5%	15.1%	56.7%	37.5%	24.0%
Operating growth (%)	32.6%	33.8%	266.6%	28.8%	-74.9%
Pre-tax profit growth (%)	33.8%	25.1%	269.3%	31.1%	-73.2%
Net profit growth (%)	46.9%	20.8%	227.2%	31.0%	-73.2%

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Equity Rating Definitions	
BUY	Positive recommendation of stock under coverage. Expected absolute return of +15% over 12-months, with low risk of sustained downside
HOLD	Neutral recommendation of stock under coverage. Expected absolute return between –15% and +15% over 12-months, with low risk of sustained downside.
SELL	Negative recommendation of stock under coverage. High risk of negative absolute return over 12-months.
NOT RATED	No research coverage and report is intended purely for informational purposes

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