JAPAN VIETNAM MEDICAL INSTRUMENT JSC (JVC) – VISIT NOTE

Market Price	Target Price	Dividend Yield	Rating	Sector
VND4,810	N/A	0.00%	NOT RATED	HEALTH CARE

Outlook – Short term

Negative Neutral Positive

Outlook – Long term

Not rated

Valuation

Not rated

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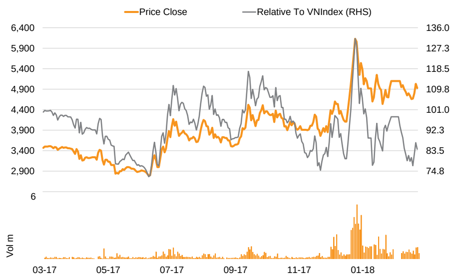
Financial health still shaky but the new board of management has now proven their ability to sustain the core operation while setting a new strategic direction. However, a potential sell-out by key shareholders such as DI could threaten management continuity and lead to fresh uncertainty for the core operation.

Core operations have been resurrected. Device and consumable supply sales surged 27.1% in 9M FY17 from the previous year's low base but still only equivalent to 61% of FY2014 revenue level prior to the Chairman's arrest in 2015. Critical supplier, Hitachi (contributed 40% of FY16 revenue) granted exclusive distribution rights back to JVC in April 2017 following JVC's restructuring efforts and timely repayment of payables owed to Hitachi.

Ghost receivables of the past to have no impact on future earnings. JVC now fully provisioned for the bad-debt worth up to ~1,100bn related to receivables generated from inflated sales figures in the past. The recovery ratio for this amount is admittedly low and expected to be 1% in the best case. Hence, the management has not really focused on collection of these receivables and, instead, has concentrated on restoring the core operation and rebuilding the company's balance sheet.

Hospital affiliate service contracting provide recurring revenue to buffer against volatility inherent in device sales and has potential to scale. JVC is operating nearly 140 medical equipment systems in 80 hospitals (out of a total of 1,322 hospitals nationwide as of 2016 of which 1,091 were public facilities) in Vietnam under a profit-sharing agreement. The contracts last for 7-10 years with payback periods of 1-3 years and gross margins of 20-30%, post profit share with the hospitals. Revenue from these contracts is expected to contribute 20% of FY17 revenue. The company will set up 20 new such hospital medical equipment systems in FY18 with several more contracts currently under negotiation. We believe that increased revenue contribution from this business line will improve overall quality of earnings, over time.

Price performance



Source: VNDIRECT

Key statistics

52w high (VND)	6,130
52w low (VND)	2,790
3m Avg daily volume (shares)	1,166,937
3m Avg daily value (VNDmn)	5,954
Market cap (VNDbn)	554.6
Outstanding shares (m)	112.5
Free float (%)	45.0
TTM P/E	27.7
Current P/B	4.6

Ownership

DI Asian Industrial Fund	19.4%
PYN Elite Fund	11.0%
Vietnam Equity Holding	6.3%
Others	63.3%

Source: VNDIRECT

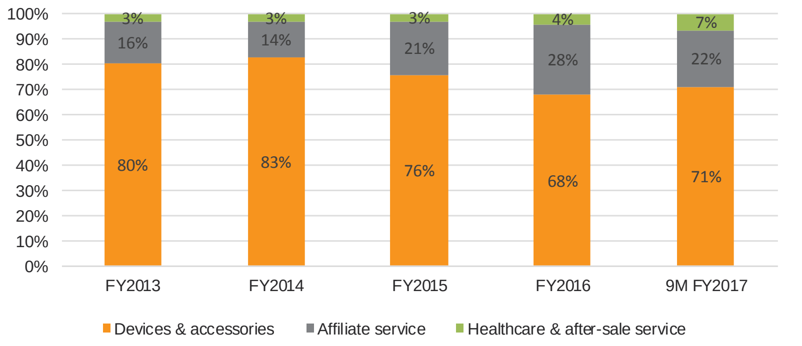
Financial summary (VND)	03-13A	03-14A	03-15A	03-16A
Net revenue (bn)	594	923	507	499
Revenue growth		55.4%	(45.0%)	(1.6%)
Gross margin	29.3%	33.1%	0.7%	18.8%
EBITDA margin	31.0%	37.6%	(245.3%)	9.2%
Net profit (bn)	42	178	(1,336)	(32)
Net profit growth		326.5%		
Recurring profit growth		323.5%		
Basic EPS	118	313	(11,874)	(282)
Adjusted EPS	118	313	(11,874)	(282)
BVPS	2,686	2,516	11,306	4,543
ROAE		14.9%	(98.9%)	(3.6%)

Source: VNDIRECT

Business summary: outsourced diagnostic services will bring recurring revenue and help JVC ride the sustained rise in healthcare spending

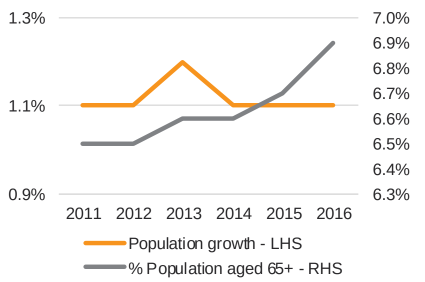
Most of JVC's operation is centered on distributing diagnostic imaging medical devices and equipment to local hospitals and other healthcare facilities. The key OEM on the supply side is Hitachi of Japan with sales of their equipment contributing nearly 20% of JVC's FY16 revenue. The other product types are consumables, imaging parts and accessories used for the medical devices sold by JVC. The company is also running an affiliate service program with local hospitals to provide outsourced medical diagnostic services to them; JVC will essentially set-up and run these services for the hospitals. Under this model, the equipment is held and operated by JVC, but serve the hospital's patients. The 60-70% of gross profit from the affiliate service will be returned to the company after haircuts to the hospitals, resulting in post-sharing gross margins of 20-30%.

Figure 1: Revenue structure by activity



Source: VNDIRECT, JVC

Figure 2: Elderly population is growing



Source: GSO, VNDIRECT

BMI research also believes that the medical device market will grow at a CAGR of 10% in the next 5 years in value terms thanks to the expanding elderly population and increasing number of healthcare facilities across both the public and private sector. The government has a limited budget to expand healthcare capacity to help relieve the current overload in the public healthcare system. Through its affiliate program providing outsourced diagnostic services, JVC is pioneering efforts to help public hospitals improve their diagnostic facilities without having to incur huge capital outlays on device purchases; this will help expand domestic healthcare service capacity in an asset-light manner. Even though this service model will cannibalize the traditional device sales business, it will generate recurring, predictable revenues which will improve JVC's quality of earnings over time. We therefore view this as a positive development.

Visible turnaround in earnings for FY17 due to strong recovery in device sales; this should also fuel growth in consumables and spare parts sales into next year.

In 9M FY2017, JVC started making profits again for first time in the last two years as provisions for bad-debt tapered off and the company manage to regain its distribution right for Hitachi devices. This supplier has also allowed JVC to exclusively sell Hitachi medical devices in both the North and South of Vietnam. The hospitals have also resumed equipment purchases from JVC as evidenced by the 70% surge in 9M FY17 device sales. However, consumables and accessories (X-ray & CT films, spare-parts, medical tools, etc.) sale stayed flat versus the last fiscal year same period due to the disruptions in device sales in previous years. This explains why total revenue grew at a slower pace than device sales revenue (16.7% YoY) as the device sales contribution was only ~20% of total revenue. Consumables and spare parts sales typically lag device sales and, hence, we expect that the strong tick-up in device sales this year will fuel strong growth in consumables and accessories sales in the next fiscal year.

JVC also doubled its gross profit in 9M FY2017, attributed mostly to the aforementioned growth in medical device sales. By pushing sales, JCV also received more marketing subsidies from its suppliers to report VND15.5bn in other income. Overall, the bottom line was positive at VND5.4bn instead of the loss seen in FY16. With this result, we expect JVC could easily deliver its target for 630bn revenue and bn19bn EAT for FY17. The management is also aiming for a 20% growth in FY18 EAT based on the increase in the number of medical devices installed under the affiliate service program.

Figure 3: Key financial results

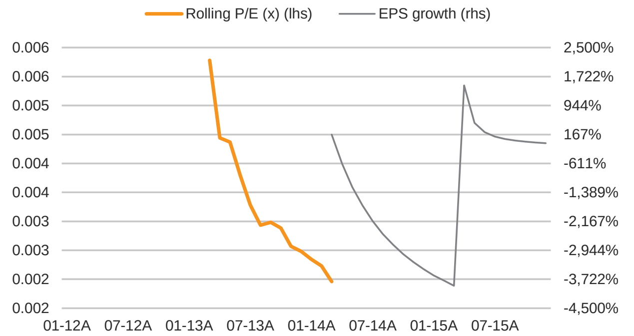
VNDbn	9M FY17	9M FY16	%Change
Net sale revenue	436.5	373.2	17.0%
Cost of sales	-333.8	-322.6	3.5%
Gross profit	102.7	50.6	103.0%
Selling expenses	-77.1	-26.9	186.6%
G&A expenses	-34.0	-63.5	-46.5%
Operating profit/(loss)	-10.3	-43.8	-76.5%
Net other income	15.5	0.7	2114.3%
EBT	5.2	-43.2	
EAT	5.4	-45.7	

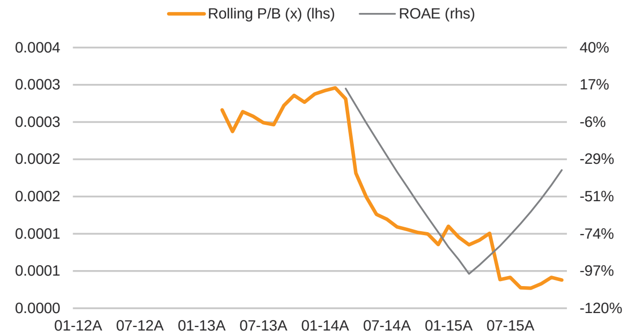
Source: VNDIRECT, JVC

Exit of key shareholder remains a risk

We applaud the company’s resurgence and see a promising outlook for the company based on its revamped business plan. However, we remain concerned about the continued commitment of strategic investor Dream Incubator (DI). The fund is currently open to divesting its 19.4% stake in JVC and, if this were to happen, it could again lead to a management reshuffle as most of the current members of the management board have been appointed by DI. Any future change of key management will disrupt management continuity at a time when the recovery of the business remains somewhat fragile. This also raises questions on how serious management is about their new business strategy – is the new strategic plan just “window-dressing” or a genuine attempt at restoring JVC to its former glory?

Valuation





Income statement

(VNDbn)	03-14A	03-15A	03-16A
Net revenue	923	507	499
Cost of sales	(617)	(504)	(405)
Gen & admin expenses	(38)	(1,159)	(71)
Selling expenses	(5)	(36)	(49)
Operating profit	**262**	**(1,192)**	**(27)**
Operating EBITDA	332	(1,117)	44
Depreciation and amortisation	**(70)**	**(75)**	**(71)**
Operating EBIT	**262**	**(1,192)**	**(27)**
Interest income	1	1	0
Financial expense	(48)	(134)	(7)
Net other income	16	(11)	4
Income from associates & JVs	0	0	0
Pre-tax profit	**230**	**(1,336)**	**(30)**
Taxation	(53)	0	(2)
Minority interests	0	0	0
Net profit	**178**	**(1,336)**	**(32)**
Adj. net profit to ordinary	178	(1,336)	(32)
Ordinary dividends			
Retained earnings	**178**	**(1,336)**	**(32)**

Balance sheet

(VNDbn)	03-14A	03-15A	03-16A
Cash and equivalents	503	48	26
Short term investments	15	0	0
Accounts receivables	945	668	169
Inventories	308	265	80
Other current assets	24	15	3
Total current assets	**1,794**	**996**	**278**
Fixed assets	463	523	461
Total investments	13	112	(0)
Other long-term assets	14	42	26
Total assets	**2,285**	**1,673**	**764**
Short-term debt	470	22	14
Accounts payable	29	113	75
Other current liabilities	178	119	76
Total current liabilities	**677**	**254**	**164**
Total long-term debt	92	58	27
Other liabilities	85	89	62
Share capital	844	1,125	1,125
Retained earnings reserve	304	(275)	(1,035)
Shareholders' equity	**1,430**	**1,272**	**511**
Minority interests	0	0	0
Total liabilities & equity	**2,285**	**1,673**	**764**

Cash flow statement

(VNDbn)	03-14A	03-15A	03-16A
Pretax profit	**230**	**(1,336)**	**(30)**
Depreciation & amortisation	70	75	70
Tax paid	(34)	30	(34)
Other adjustments	(26)	1,281	34
Change in working capital	**(238)**	**(369)**	**36**
Cash flow from operations	**3**	**(319)**	**76**
Capex	(53)	(9)	(43)
Proceeds from assets sales	75	2	3
Others	(14)	184	1
Other non-current assets changes			
Cash flow from investing activities	**8**	**178**	**(39)**
New share issuance	329	0	0
Shares buyback	0	0	0
Net borrowings	137	(346)	(16)
Other financing cash flow	(2)	32	(43)
Dividends paid	(28)	0	0
Cash flow from financing activities	**436**	**(314)**	**(59)**
Cash and equivalents at beginning of period	57	503	48
Total cash generated	**447**	**(456)**	**(21)**
Cash and equivalents at the end of period	503	48	26

Key ratios

	03-14A	03-15A	03-16A
Dupont			
Net profit margin	19.3%	(263.3%)	(6.3%)
Asset turnover	0.47	0.26	0.41
ROAA	9.1%	(67.5%)	(2.6%)
Avg assets/avg equity	1.64	1.46	1.37
ROAE	14.9%	(98.9%)	(3.6%)
Efficiency			
Days account receivable	271	367	357
Days inventory	182	192	72
Days creditor	17.4	82.0	67.8
Fixed asset turnover	2.03	1.03	1.02
ROIC	8.9%	(98.8%)	(5.7%)
Liquidity			
Current ratio	2.65	3.93	1.69
Quick ratio	2.19	2.88	1.20
Cash ratio	0.76	0.19	0.16
Cash cycle	436	477	362
Growth rate (yoy)			
Revenue growth	55.4%	(45.0%)	(1.6%)
Operating profit growth	92.9%		
Net profit growth	326.5%		
EPS growth	165.9%		
Share value			
Basic EPS (VND)	313	(11,874)	(282)
BVPS (VND)	2,516	11,306	4,543

Source: VNDIRECT

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Description:	Excellent	Very Good	Good	N/A	

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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.

Country Ratings	Definition:
Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

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