

## PHU NHUAN JEWELRY JSC (PNJ) – UPDATE

<b>Market Price</b>	<b>Target Price</b>	<b>Dividend Yield</b>	<b>Rating</b>	<b>Sector</b>
VND52,100	VND78,800	3.5%	ADD	CONSUMER GOODS

27 July 2020

**Outlook – Short term:** **Neutral**
**Outlook – Long term:** **Neutral**
**Valuation:** **Positive**

Consensus\*: Add:8 Hold:2 Reduce:0

Target price / Consensus: +9.6%

**Key changes in the report**

➤ N/a

**Price performance**


Source: VND RESEARCH

**Key statistics**

52w high (VND)	92,000
52w low (VND)	48,300
3m Avg daily value (VNDmn)	36,621
Market cap (VND bn)	11,729
Outstanding shares (m)	225.1
Free float (%)	80
TTM P/E (x)	11.3
Current P/B (x)	2.5

**Ownership**

Cao Thi Ngoc Dung	9.0%
LGM Investments Ltd	4.4%
Route One Investment Company	3.9%

Source: VND RESEARCH

**Analyst(s):**

**Bach Phan Nhu**

bach.phannhu@vndirect.com.vn

### 2Q20 results hit hard by COVID-19

- PNJ's 2Q20 revenue dropped 7.2% yoy to VND2.270bn while net profit plunged 81.3% yoy to VND32bn.
- PNJ's 1H20 revenue edged up 0.2% yoy to VND7,817bn while net profit fell 26.4% yoy to VND440bn, making up 45% of our full-year forecast.
- Reiterate ADD with unchanged TP of VND78,800

### 2Q20 results hit hard by social distancing

2Q20 revenue dropped 7.2% yoy to VND2.270bn while net profit plunged 81.3% yoy to VND32bn following a 22-day store closure during the social distancing period in Apr 2020. However, we saw a recovery in both revenue and net profit in Jun (+4% yoy/+6% yoy; +20% qoq/+74% qoq) due to the pent-up effect post social distancing, which boosted revenue from jewelry retail segment by 26% yoy (+21% qoq).

### 1H20 results still on track with our forecasts

1H20 revenue edged up 0.2% yoy to VND7,817bn while net profit fell 26.4% to VND440bn. Gross profit margin shrank 2.1 pts yoy to 19.5% in 1H20 due to a change in product mix, in which contribution of gold bar sales in total revenue increased to 23.1% from 20.3% in 1H19, while the proportion of jewelry wholesale fell from 20.6% to 16.6% in 1H20.

### Store restructuring to optimize the retail network

In 2Q20, PNJ opened eight gold stores and upgraded two gold stores, while closing 20 stores, bringing PNJ's total number of stores down to 339. We believe PNJ will focus on the strategy of expanding retail network in 2H20F, with faster store opening than store closing, which would bring the total number of stores to 360 by end-20.

### The increase in gold price may give an advantage to PNJ in 3Q20F

The gold price rally of more than 22% since the beginning of 2020 and 5% QTD could signal a short-term improvement in jewelry GPM in the next quarter thanks to low-cost inventory stocked in 2019. However, the demand of jewelry products will decrease as consumer income gets hurt by Covid-19; and the increase in gold price can exert pressure on PNJ's COGS when inventory is restocked at higher costs.

### Reiterate ADD with unchanged TP of VND78,800

Potential re-rating catalysts include 1) a faster-than-expected store opening speed, 2) better-than-expected demand recovery after the pandemic, and 3) the launch of new products/brands which are expected to boost sales. Downside risk to our call is the next wave of COVID-19 outbreak in Vietnam.

Financial summary (VND)	12-18A	12-19A	12-20E	12-21E
Net revenue (bn)	14,573	17,001	17,215	19,208
Revenue growth	32.8%	16.7%	1.3%	11.6%
Gross margin	19.1%	20.4%	17.9%	18.1%
EBITDA margin	9.0%	9.8%	8.0%	8.9%
Net profit (bn)	960	1,191	978	1,258
Net profit growth	32.4%	24.1%	(17.9%)	28.6%
Basic EPS	4,312	5,287	4,341	5,584
Adjusted EPS	3,889	4,847	3,875	5,096
BVPS	16,819	20,303	22,842	26,632
ROAE	28.7%	28.6%	20.1%	22.6%

Source: VND RESEARCH

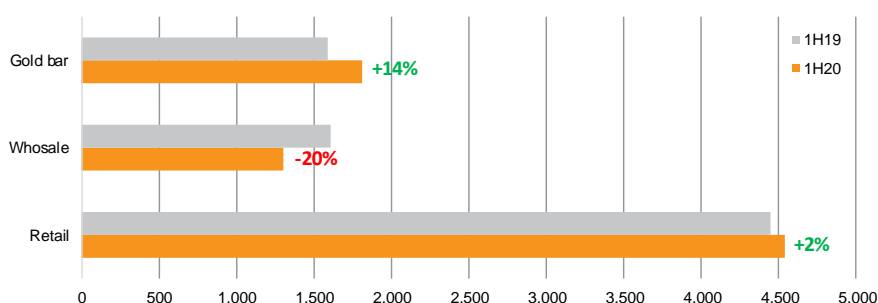
**2Q20 results hit hard by COVID-19 but still on track with our forecasts**

Figure 1: 1H20's results comparison

(VNDbn)	2Q20	2Q19	1H20	1H19	2Q20 %chg yoy	1H20 %chg yoy	vs 2020F VND's Comment forecast
<b>Revenue</b>	<b>2,770</b>	<b>2,983</b>	<b>7,817</b>	<b>7,804</b>	<b>-7.2%</b>	<b>0.2%</b>	<b>45.4% Inline with our forecast</b>
COGS	2,271	2,326	6,223	6,060	-2.4%	2.7%	
Gross profit	473	636	1,523	1,685	-25.5%	-9.6%	49.3% Inline with our forecast
Gross margin	17.1%	21.3%	19.5%	21.6%	-4.2% pts	-2.1% pts	Higher than our 2020F's gross margin at 17.9% due to the high GM in 1Q20, before being hit by Covid-19
Financial expenses	42	22	87	47	87.8%	87.5%	In order to restructure and expand retail network, PNJ increased their short-term debt which the debts as at 30 Jun 2020 jumped 82% yoy to VND2,647bn.
Selling expenses	289	287	657	654	0.8%	0.5%	
%vs Revenue	10.4%	9.6%	8.4%	8.4%	0.8% pts	0.0% pts	49.5%
General and administrative expenses	96	116	224	232	-17.1%	-3.2%	
%vs Revenue	3.5%	3.9%	2.9%	3.0%	-0.4% pts	-0.1% pts	
Operating profit	43	210	555	754	-79.7%	-26.4%	45.4% Due to the increase of Financial expenses in 1H20 followed by the increase in short-term debt, operating profit (including financial expense) only meet 45.4% of our forecast
Profit before tax	43	210	554	753	-79.7%	-26.4%	
<b>Net profit</b>	<b>32</b>	<b>169</b>	<b>440</b>	<b>598</b>	<b>-81.3%</b>	<b>-26.4%</b>	<b>45.0% Inline with our forecast</b>

Source: VND RESEARCH, COMPANY REPORTS

Figure 2: PNJ's revenue breakdown by segment in 1H20 (Unit: VNDbn)



Source: VND RESEARCH, COMPANY REPORTS

**Store restructuring to optimize the retail network**

In 2Q20, PNJ opened eight gold stores and upgraded two gold stores, while closing 20 stores, bringing PNJ's total number of stores down to 339. With the total number of opened / closed stores at 30 gold stores, PNJ's restructuring pace in 2Q20 is faster than in 1Q20 with total opened / closed stores at 10 gold stores (six gold stores opened/ two other gold stores closed). We believe PNJ will focus on the strategy of expanding retail network in 2H20F, with faster store opening than store closing, which would bring the total number of stores to 360 by end-20F in our estimates.

In order to restructure and expand its retail network, PNJ increased its short-term debt; the debts as at 30 Jun 2020 jumped 82% yoy to VND2,647bn. This led the short-term debt / total assets ratio to increase from 22% at end-1H19 to 32% at end-1H20. As a result, PNJ's interest expense in 1H20 surged 86.7% yoy.

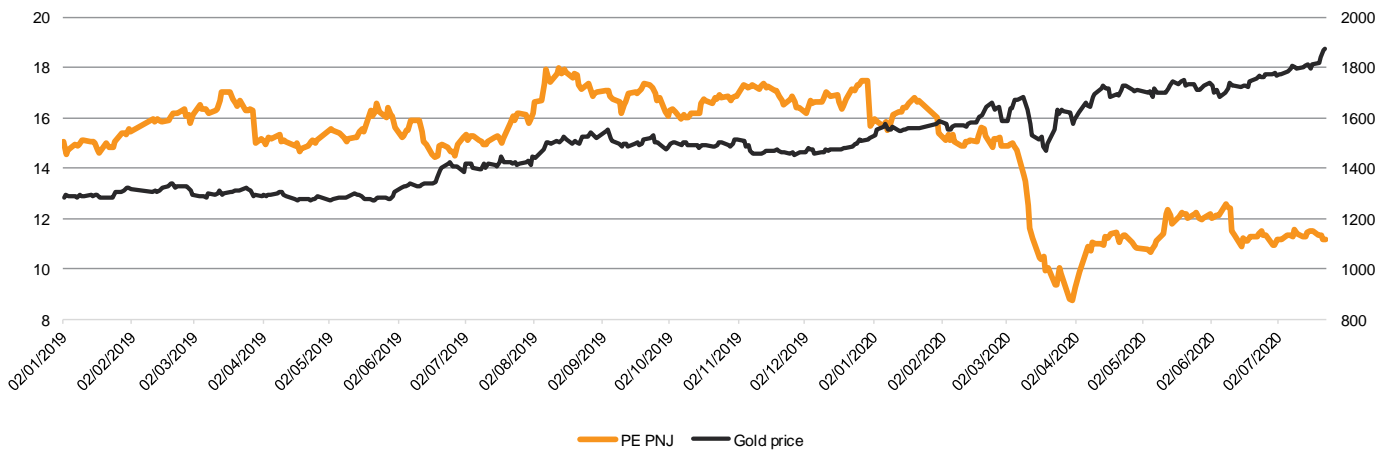
**The rise in gold price may give an advantage to PNJ in 3Q20F**

The gold price rally of more than 22% since the beginning of 2020 and 5% QTD signaled a short-term improvement in jewelry GPM in the next quarter thanks to low-cost inventory stocked in 2019. However, the demand of jewelry

products will decrease as consumer income gets hurt by Covid-19; and the increase in gold price can exert pressure on PNJ's COGS when inventory is restocked at higher costs.

Moreover, we observe that the trailing P/E of PNJ is negatively correlated with the global gold price, especially from the beginning of 2020. Therefore, the continuous increase in gold prices will put a strong pressure on PNJ's P/E in the future.

Figure 3: PNJ's P/E and gold price in period of 2019-2020



Source: BLOOMBERG, VNDIRECT RESEARCH

### We expect a slight recovery in 2H20F

**Demand for gold bar is growing strongly** due to the impact of the pandemic and the world economy's slowdown. Gold bar price followed an upward trend and increased 22% since the beginning of 2020. We believe that PNJ's gold bar sales in 2H20F will maintain a high yoy growth as in 1H20.

**The wholesale segment is the worst hit** by the pandemic after 1) exports faced disruptions since 1Q20, 2) wholesale buyers have reduced stocking amid rising gold prices, which even hit a record high, and 3) the number of jewelry stores is expected to shrink as demand is expected to weaken after the pandemic.

**Jewelry retail sales will be resilient in 2H20F** after PNJ re-opened all of their stores since 22 Apr and launched many promotional campaigns in 2Q20, which helped jewelry retail segment increased 26% yoy (+21% qoq). We expect the retail segment to continue its slight recovery in 2H20F.

We expect PNJ to post a 1.3% yoy growth in net revenue, yet a 17.9% yoy decline in net profit in FY20F. Net revenue and net profit are forecasted to increase 11.6% and 28.6%, respectively, in FY21F. These are on the basis of: 1) revenue per gold store is expected to decrease 11% yoy in 2020F, increase 7.0% in 2021F then grow 3%/year afterwards, while that of a silver store will decrease 20% in 2020F before making an annual rise of 2.0%/year, 2) 10/10 net new stores will be opened in FY20F/21F, and 3) gross margin is expected to stay at 17.9% in FY20F and expand 0.2% pts to 18.1% in FY21F on an expected lower demand for gold bars.

### Valuation

**We maintain our ADD rating with TP at VND78,800**, due to the sharp fall in PNJ price in 2Q20 that gives a potential upside of 51.2% from current price (VND52,100, at 27<sup>th</sup> July 20). We forecast FY20-29F EBIT growth at CAGR of 7.8%. Our DCF-based target price is VND78,800 on the assumptions of risk-free rate at 4% and WACC at 10.7%.

Potential re-rating catalysts include 1) a faster-than-expected store opening speed, 2) better-than-expected demand recovery after the pandemic, and 3) the launch of new products/brands which are expected to boost sales. Downside risk to our call is the next wave of COVID-19 outbreak in Vietnam.

**Figure 4: Discounted Cash Flow (DCF Valuation)**

DCF Valuation	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
EBIT	1,309	1,650	1,841	2,025	2,285	2,441	2,607	2,876	3,028	3,187	3,555
Tax	-244	-315	-352	-388	-439	-469	-502	1,263	1,619	1,309	1,650
Depreciation	56	61	74	90	103	118	136	150	164	181	199
Capex	-121	-267	-352	-293	-336	-386	-296	-325	-357	-393	-432
Change in working cap	714	-445	-532	-648	-198	-181	-184	1	5	-11	101
Free Cash Flows	1,714	684	679	786	1,415	1,523	1,761	2,147	2,255	2,346	2,708
Present Value of FCF	1,628	588	530	550	891	868	916	1,009	947	891	948

Source: VNDIRECT RESEARCH

**Figure 5: Assumptions**

Cost of Capital	Current
Beta	0.9
Market Risk Premium	10.1%
Risk Free Rate	4.0%
Cost of Equity	13.5%
Cost of Debt	5.0%
Corporate Tax Rate	20.0%
WACC	10.7%

Source: VNDIRECT RESEARCH

**Figure 6: Target price**

DCF Method	Amount	Unit
PV of Free Cash Flows	7,190	VNDbn
PV of Terminal Value (2.0% growth)	11,312	VNDbn
<b>Enterprise value</b>	<b>18,502</b>	<b>VNDbn</b>
Cash and cash equivalents	974	VNDbn
Total debts	(1,725)	VNDbn
Equity Value	17,751	VNDbn
Shares	225	million
<b>Price per share</b>	<b>78,800</b>	<b>VND/share</b>

Source: VNDIRECT RESEARCH

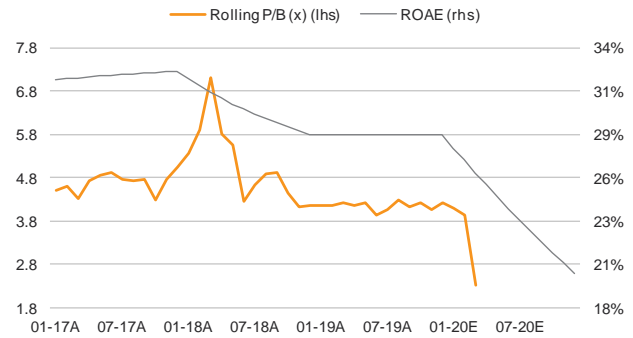
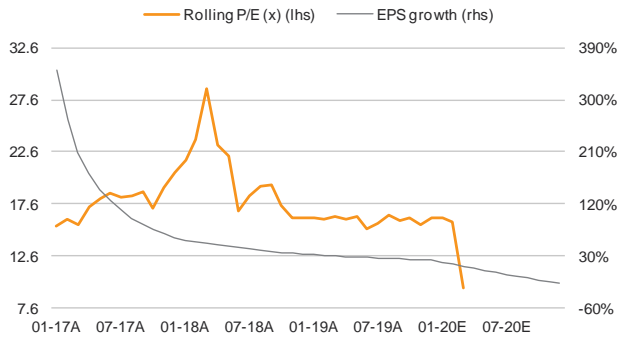
**Figure 7: Peer Comparison**

Company	Bloomberg Ticker	Recom.	Share Price (local curr)	Target Price (local curr)	Market Cap (US\$ m)	P/E (x)			3-year EPS CAGR (%)	P/BV (x)			ROE (%)			ROA (%)		
						TTM	FY20F	FY21F		TTM	FY20F	FY21F	TTM	FY20F	FY21F	TTM	FY20F	FY21F
<b>Jewelry retail companies</b>																		
Phu Nhuan Jewelry JSC	PNJ.VN	ADD	52,100	78,800	506	11.3	13.1	10.7	32.0%	2.5	2.3	2.1	23.6%	21.5%	24.2%	14.1%	12.1%	13.9%
Tiffany & Co	TIF.US	na	121.4	na	14,733	37.4	66.5	31.8	12.5%	4.6	4.2	4.0	11.1%	7.2%	12.7%	5.4%	4.3%	7.0%
Chow Tai Fook Jewellery Group Ltd	1929.HK	REDUCE	8.19	6.00	10,566	28.3	20.4	16.0	3.0%	3.1	3.0	2.9	10.2%	15.0%	18.5%	4.6%	6.9%	8.6%
Chow Sang Sang Holdings Internationa	116.HK	na	8.14	na	711	8.6	9.1	5.9	-1.0%	0.5	0.5	0.5	6.1%	5.0%	8.2%	4.3%	4.0%	5.8%
<b>Average - Jewelry retail peers</b>					<b>8,670</b>	<b>24.7</b>	<b>32.0</b>	<b>17.9</b>	<b>4.8%</b>	<b>2.8</b>	<b>2.6</b>	<b>2.5</b>	<b>9.1%</b>	<b>9.1%</b>	<b>13.1%</b>	<b>4.7%</b>	<b>5.1%</b>	<b>7.1%</b>

All prices are based on the closing prices on 27th July 2020. All estimates for Non-rated (NR) stocks are based on Bloomberg consensus estimates

Source: BLOOMBERG, VNDIRECT RESEARCH

**Valuation**



**Income statement**

(VNDbn)	12-19A	12-20E	12-21E
Net revenue	17,001	17,215	19,208
Cost of sales	(13,540)	(14,126)	(15,728)
Gen & admin expenses	(479)	(392)	(403)
Selling expenses	(1,363)	(1,388)	(1,427)
<b>Operating profit</b>	<b>1,619</b>	<b>1,309</b>	<b>1,650</b>
Operating EBITDA	1,675	1,365	1,711
<b>Depreciation and amortisation</b>	<b>(56)</b>	<b>(56)</b>	<b>(61)</b>
<b>Operating EBIT</b>	<b>1,619</b>	<b>1,309</b>	<b>1,650</b>
Interest income	2	8	9
Financial expense	(119)	(95)	(85)
Net other income	1	0	(1)
Income from associates & JVs	0	0	0
<b>Pre-tax profit</b>	<b>1,503</b>	<b>1,222</b>	<b>1,573</b>
Tax expense	(312)	(244)	(315)
Minority interest	0	0	0
<b>Net profit</b>	<b>1,191</b>	<b>978</b>	<b>1,258</b>
Adj. net profit to ordinary	1,191	978	1,258
Ordinary dividends	(344)	(406)	(406)
<b>Retained earnings</b>	<b>847</b>	<b>572</b>	<b>852</b>

**Balance sheet**

(VNDbn)	12-19A	12-20E	12-21E
Cash and equivalents	95	974	751
Short term investments	0	0	0
Accounts receivables	138	163	184
Inventories	7,019	6,052	6,588
Other current assets	78	139	118
<b>Total current assets</b>	<b>7,330</b>	<b>7,328</b>	<b>7,641</b>
Fixed assets	923	989	1,192
Total investments	0	0	0
Other long-term assets	346	344	352
<b>Total assets</b>	<b>8,599</b>	<b>8,661</b>	<b>9,185</b>
Short-term debt	2,611	1,722	1,537
Accounts payable	688	467	579
Other current liabilities	719	1,316	1,063
<b>Total current liabilities</b>	<b>4,018</b>	<b>3,505</b>	<b>3,179</b>
Total long-term debt	4	4	4
Other liabilities	3	6	3
Share capital	2,253	2,253	2,253
Retained earnings reserve	1,042	1,670	2,450
<b>Shareholders' equity</b>	<b>4,574</b>	<b>5,146</b>	<b>6,000</b>
Minority interest	0	0	0
<b>Total liabilities &amp; equity</b>	<b>8,599</b>	<b>8,661</b>	<b>9,185</b>

**Cash flow statement**

(VNDbn)	12-19A	12-20E	12-21E
<b>Pretax profit</b>	<b>1,503</b>	<b>1,222</b>	<b>1,573</b>
Depreciation & amortisation	56	56	61
Tax paid	(291)	(244)	(315)
Other adjustments	(186)	(94)	46
<b>Change in working capital</b>	<b>(1,757)</b>	<b>1,265</b>	<b>(671)</b>
<b>Cash flow from operations</b>	<b>(675)</b>	<b>2,205</b>	<b>694</b>
Capex	(208)	(121)	(267)
Proceeds from assets sales	1	1	1
Others	1	0	0
Other non-current assets changes	0	89	(60)
<b>Cash flow from investing activities</b>	<b>(206)</b>	<b>(31)</b>	<b>(326)</b>
New share issuance	69	0	0
Shares buyback	(2)	0	0
Net borrowings	1,048	(889)	(185)
Other financing cash flow	(2)	0	0
Dividends paid	(344)	(406)	(406)
<b>Cash flow from financing activities</b>	<b>769</b>	<b>(1,295)</b>	<b>(591)</b>
Cash and equivalents at beginning of period	207	95	974
<b>Total cash generated</b>	<b>(112)</b>	<b>879</b>	<b>(223)</b>
Cash and equivalents at the end of period	95	974	751

**Key ratios**

	12-19A	12-20E	12-21E
<b>Dupont</b>			
Net profit margin	7.0%	5.7%	6.5%
Asset turnover	2.28	1.99	2.15
ROAA	16.0%	11.3%	14.1%
Avg assets/avg equity	1.79	1.78	1.60
ROAE	28.6%	20.1%	22.6%
<b>Efficiency</b>			
Days account receivable	1.0	1.4	1.3
Days inventory	189.2	156.8	152.9
Days creditor	18.5	12.1	13.4
Fixed asset turnover	20.71	18.01	17.61
ROIC	16.6%	14.2%	16.7%
<b>Liquidity</b>			
Current ratio	1.8	2.1	2.4
Quick ratio	0.1	0.4	0.3
Cash ratio	-	0.3	0.2
Cash cycle	171.7	146.1	140.8
<b>Growth rate (yoy)</b>			
Revenue growth	16.7%	1.3%	11.6%
Operating profit growth	28.3%	(19.1%)	26.1%
Net profit growth	24.1%	(17.9%)	28.6%
EPS growth	22.6%	(17.9%)	28.6%

Source: VND RESEARCH

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## RECOMMENDATION FRAMEWORK

### 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.

## Hien Tran Khanh – Deputy Head of Research

Email: [hien.trankhanh@vndirect.com.vn](mailto:hien.trankhanh@vndirect.com.vn)

## Phan Nhu Bach – Analyst

Email: [bach.phannhu@vndirect.com.vn](mailto:bach.phannhu@vndirect.com.vn)

## VNDIRECT Securities Corporation

1 Nguyen Thuong Hien Str – Hai Ba Trung Dist – Ha Noi

Tel: +84 2439724568

Email: [research@vndirect.com.vn](mailto:research@vndirect.com.vn)

Website: <https://vndirect.com.vn>