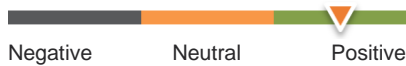


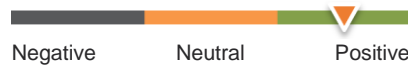
## PHU NHUAN JEWELRY JSC (PNJ) - UPDATE

<b>Market Price</b> VND96,000	<b>Target Price</b> VND120,700	<b>Dividend Yield</b> 1.9%	<b>Rating</b> ADD	<b>Sector</b> RETAIL
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### Outlook – Short term



### Outlook – Long term



### Valuation



10 August 2018

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**PNJ announced strong 2Q2018 business results in line with our expectations. Our positive view on PNJ is strengthened by the company's growing store coverage, robust Same-Store Sales Growth (SSSG) and successful expansion into fashion accessories such as watches. We upgrade PNJ to an ADD rating based on a new target price of VND120,700/share.**

**PNJ's 2Q net profit surged 39.9% yoy to VND180.4bn on the back of a 37.2% yoy increase in net revenue to VND3,217.4bn.** Cumulative 6M2018 results were also strong with increases of 34.3% yoy in the top line and 36.8% yoy in the bottom line. With these half year results, the company has also achieved 53.6% of its revenue target and 58.6% of its net profit goal for FY2018.

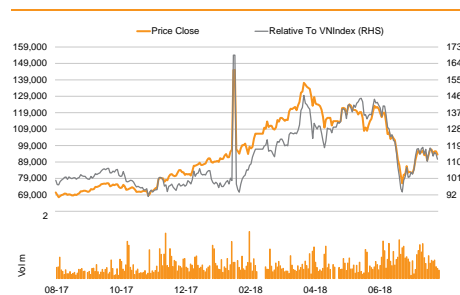
**1H18 gross margin improved 100 bp to 18.4% due to the continued improvement in the product mix and the slight expansion in GPM of gold retail segment.** Comparing to the same period last year, jewelry retailing increased its contribution to total revenue from 50.1% to 53.5% while the contributions from jewelry wholesaling and gold bar trading reduced to 25.2% and 20.0% from 26.7% and 21.5%, respectively.

**Extensive store network continued to serve as a major driver for PNJ's growth.** Retail revenue in 1H2018 surged 44.0% yoy contributed by (1) SSSG of 23.0%, (2) full 6-month revenue contribution in 1H2018 of 22 stores opened in 1H2017 and (3) revenue contribution from 56 stores opened from 3Q17 to 2Q18. In 6M2018, PNJ opened 30 new PNJ stores (vs. 40 stores in 2018 management's guidance), bringing the total store count to 298 stores.

**We expect PNJ to continue to see high growth in 2H2018.** FY2018 revenue is estimated to reach VND14,271bn (+30.0% yoy) and net profit to soar 39.3% yoy to VND1,010bn. PNJ Watch, which offers mid-range branded watches and the on-going improvement in its omni-channel platform system could become new growth engines for the company.

**Recent share price weakness has created an attractive entry point.** The on-going news flow about PNJ's former BoD member's involvement in the DongA Bank case might continue to stir up bearish sentiment but we believe this incident will not have a material impact on PNJ's fundamentals and longer-term share price outlook. PNJ is currently trading at a TTM P/E of 18.0x, a 9.1% discount to the average TTM P/E of global peers (19.8x). Given PNJ's leading position and sizeable room for growth, we reiterate our ADD rating and target price of VND120,700/share which translates into a FY18 P/E of 19.4x.

### Price performance



Source: VNDIRECT

### Key statistics

52w high (VND)	123,965
52w low (VND)	76,000
3m Avg daily volume (shares)	422,058
3m Avg daily value (VNDmn)	53,135
Market cap (VNDbn)	15,565
Outstanding shares (m)	162
Free float (%)	64
TTM P/E (x)	18.0
Current P/B (x)	3.2

### Ownership

Cao Thi Ngoc Dung	9.2%
LGM Investments Ltd	4.5%
Route One Investment Company	4.1%
Others	82.2%

Source: VNDIRECT

Financial summary (VND)	12-16A	12-17A	12-18E	12-19E
Net revenue (bn)	8,565	10,977	14,271	17,432
Revenue growth	11.1%	28.2%	30.0%	22.1%
Gross margin	16.5%	17.4%	17.9%	18.2%
EBITDA margin	7.4%	8.4%	8.7%	8.3%
Net profit (bn)	451	725	1,010	1,169
Net profit growth	517.8%	60.8%	39.3%	15.7%
Recurring profit growth	385.7%	76.2%	40.2%	15.8%
Adjusted EPS	2,483	3,848	5,513	6,426
Diluted EPS	3,068	4,471	6,229	7,209
BVPS	10,211	18,193	22,621	27,826
ROAE	32.0%	32.6%	30.5%	28.6%

## 1H2018 recap: Accelerated store network expansion and higher SSSG drove a surge in revenues

**PNJ is widening its store coverage lead over its competitors.** By opening 30 new stores and reaching a total of 298 jewelry stores, PNJ has gone far ahead of Doji, SJC and PRECITA at the end of 1H2018 (~100 competitor stores in total).

**SSSG for gold jewelry retail stores touched 23.0% in 1H18 (vs. 22.4% in 2017)**, supported by an expanded customer base (+25.0% yoy), a larger average ticket size (+13.0% yoy) and the shortened return visit period (-5.0% yoy). Accordingly, gold stores brought in VND3,800bn (+44.0% yoy), accounting for 51.6% of 1H18 total revenue. SSSG for silver stores was 1.0% and translated to VND125bn (+27.0% yoy) in silver jewelry retail sales. PNJ Silver has not been able to realize the potential of the high-end silver jewelry segment (GPM at 60-70% level) and plans to shift its strategy to focus on a slightly older customer demographic (25-30 years old) instead of teenagers and those in their early twenties.

Figure 1: Comparison of Financial Results

FYE (VNDbn)	2QFY18	yoy	1HFY18	yoy	vs. old forecast	vs. revised forecast	Comments
		chg		chg			
<b>Net revenue</b>	<b>3,217.5</b>	<b>37.2%</b>	<b>7,356.8</b>	<b>34.3%</b>	<b>56.0%</b>	<b>51.6%</b>	
<i>Jewelry revenue</i>	3,201.8	37.3%	7,324.1	34.5%	56.0%	51.6%	Higher than our expectations, supported by rapid store network expansion and higher SSSG.
<i>Accessories</i>	4.8	8.9%	12.0	9.4%	39.4%	30.0%	
<i>Services</i>	10.9	43.4%	20.7	43.0%	77.9%	76.7%	
<b>Gross profit</b>	<b>582.9</b>	<b>45.7%</b>	<b>1,352.9</b>	<b>42.3%</b>	<b>53.7%</b>	<b>53.1%</b>	
<i>Gross profit margin</i>	18.1%	+1.0% pts	18.4%	+1.0% pts	-0.8% pts	+0.5% pts	GPM improved as PNJ continued to improve its product mix
Selling expenses	268.9	44.5%	550.5	49.1%	59.4%	54.0%	Higher than our forecasts due to ramped-up marketing activities, more expenses incurred for digital transformation project and the expansion of store network
G&A expenses	73.7	73.0%	134.3	63.9%	60.0%	57.6%	
<b>Operating profit</b>	<b>226.8</b>	<b>45.3%</b>	<b>646.6</b>	<b>38.4%</b>	<b>47.2%</b>	<b>49.9%</b>	
Pre-tax profit	227.5	40.8%	648.3	37.1%	46.0%	51.4%	
<b>Net profit</b>	<b>180.4</b>	<b>39.9%</b>	<b>516.7</b>	<b>36.8%</b>	<b>45.9%</b>	<b>51.2%</b>	
<b>EPS (sem)(VND/share)</b>	<b>1,112.5</b>		<b>3,186.5</b>		<b>45.9%</b>	<b>51.2%</b>	

Source: PNJ, VNDIRECT

**We have revised up our forecasted FY18 revenue by 8.7% and reduced our projected net profit by 10.3%.** Top line growth was driven by the assumption of average revenue growth per gold store of 5.0%, average revenue per silver store of 2.0% and 45 gold stores launched within 2018. However, we lower our bottom line projection as we increase the projected full-year contribution of low-margin segments (gold bar and wholesale) and reduce the forecasted GPM on retail gold sales. The decline in revenue contribution of low margin segments has underwhelmed our expectations largely due to sustained demand for gold bar trading on the back of high gold price volatility in 1H2018 and a renewed push into the jewelry wholesale business.

Figure 2: Earnings revision

FYE (VNDbn)	2017A	2018F		Comments
		Old	New	
Net revenue	10,977	13,127	14,271	8.7% Higher revenue forecast of gold bar sales and wholesales
Net revenue growth	28.2%	19.6%	30.0%	
Gross profit	1,912	2,521	2,549	1.1%
Gross profit margin	17.4%	19.2%	17.9%	-1.3% pts Higher contribution of low-margin segments, lower GPM assumption for retail gold sales than previous forecast
EBIT	949	1,369	1,296	-5.3%
EBT	909	1,408	1,262	-10.4%
Net profit	726	1,126	1,010	-10.3% Driven by the lower GPM
EPS (VND)	7,032	6,946	6,229	-10.3%

Source: VNDIRECT

**Long-term outlook: PNJ Watch and the on-going improvement in the omni-channel system could further bolster profit growth**

PNJ is diversifying its jewelry-focused product mix by introducing fashion accessories such as mid-range branded watches since 2012. The revenue from this experimental segment stayed at a modest level of VND10bn-20bn per year before rising to VND24bn in sales in 2017. Although its contribution to total revenue is not yet significant, GPM of the segment is high at 60-70% level (vs. jewelry segment GPM of ~19.3%). Thus, PNJ aims for a breakthrough with plans to launch signature PNJ Watch stores in 2018, while also selling the products online and cross selling them through its existing jewelry stores. PNJ holds high hopes for this new business as 1) the domestic watch retail market is fragmented without any big player; 2) PNJ Watch products come with a warranty, giving the buyers more quality assurance than branded watches bought overseas and resold in Vietnam by informal middlemen; the latter do not come with a warranty; and 3) it can cross-sell its products to its existing jewelry customer base as high-end watches are increasingly seen as fashion accessories and lasting stores of value, much like jewelry.

Figure 3: PNJ Watch available on PNJ's online website



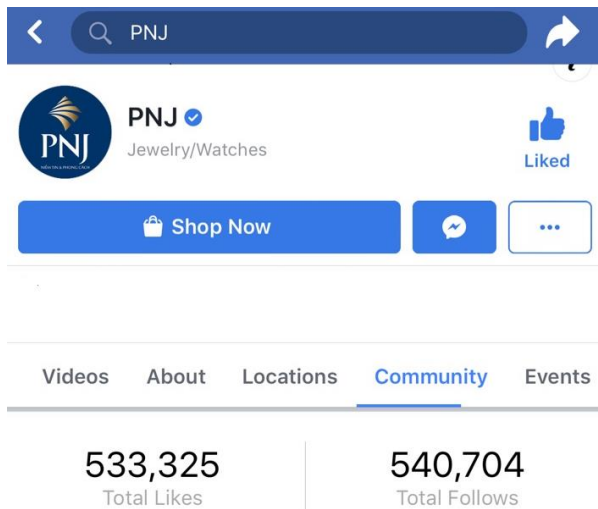
Source: PNJ

*\*Translation: PNJ Watch – Authentic watches now available with 0% interest installment plan. (Applicable to online customers)*

**Growing benefits from expanding store network and developing omni-channel platform.** PNJ has been able to create multiple engagement points with its customers via physical stores and e-commerce, supported by the growing store network and a strengthened social networking presence. Notably, the company has made good use of its social network presence to stay in touch with younger and trendy customers, illustrated by its 500,000-strong

following on Facebook and more than 1 million views on Youtube. The e-commerce channel posted around VND56bn in revenue for the first five months of 2018 (doubling the full-year result in 2017). PNJ's management also believes that growth will accelerate in 2019 when their Online-to-Offline (O2O) system comes into operation. This system is expected to integrate online shopping with the physical shopping experience and support the development of the omni-channel platform. PNJ is also investing in an ERP system and digital transformation projects to build a firm infrastructure foundation for its multi-channel retailing.

Figure 3: PNJ's Facebook homepage



Source: PNJ Facebook

Figure 4: PNJ's video clip "Seeing the quality in you"



Source: PNJ Youtube

**Valuation attractive, reinforced by strong cash flow**

**Good prospects reflected in the strong cash flow.** We have run a 10-year forecast of PNJ's free cash flows with a FY18-28 CAGR of 8.8% in net revenue and 17.1% in EBIT.

Figure 5: Discounted Cash Flow (DCF Valuation)

DCF Valuation	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
EBIT	1,296	1,497	1,979	2,472	2,892	4,148	4,348	4,523	4,936	5,112	5,304
Tax	(252)	(292)	(387)	(484)	(567)	(817)	(857)	(892)	(974)	(1,008)	(1,047)
Depreciation	66	66	79	94	113	136	161	189	224	253	285
Capex	(150)	(180)	(216)	(260)	(312)	(340)	(401)	(474)	(419)	(474)	(482)
Change in work cap	(665)	(741)	(753)	(440)	(396)	(194)	(134)	(122)	(121)	(118)	(118)
Free Cash Flows	295	350	702	1,382	1,730	2,933	3,117	3,224	3,646	3,765	3,942
Present Value of FCF	263	277	491	871	969	1,467	1,371	1,257	1,276	1,167	1,104

Source: VNDIRECT



Figure 6: Adjusted Assumptions

Cost of Capital	
Beta	0.93
Market Risk Premium	10.1%
Risk Free Rate	5.0%
Cost of Equity	14.4%
Cost of Debt	5.5%
Debt/Capital	28.7%
Corporate Tax Rate	20.0%
WACC	12.4%

Source: VNDIRECT

Figure 7: Discounted Cash Flow (DCF Valuation)

DCF Method	Amount	Unit
PV of Free Cash Flows	9,409	VNDbn
PV of Terminal Value (2.0% growth)	10,634	VNDbn
Enterprise value	20,043	VNDbn
Cash and cash equivalents	175	VNDbn
Total debts	(1,076)	VNDbn
Equity Value	19,142	VNDbn
Shares	162	million
Price per share	118,000	VND/share

Source: VNDIRECT

**Share price retreat has made valuation attractive.** PNJ's recent share price plunge can be seen as a knee-jerk reaction to the news about the involvement of former PNJ personnel in the DongA Bank case. However, we believe the case will have no material impact on the core business of the company. PNJ still deserves to at least trade in line with its peers due to 1) its leading position and the ability to further consolidate market share via fast-growing store coverage and 2) PNJ's FY2017 ROE of 32.6% being well above its global peers (average ROE of 14.2%).

Figure 8: Peer Comparison

Company	Country	Market cap (USDmn)	TTM NPAT Growth (%)	TTM EPS growth (% YoY)	ROE(%)	ROA(%)	D/E (x)	TTM P/E (x)	P/B (x)
Tiffany & Co	U.S	17,033	19.6	(16.8)	18.0	10.8	0.3	30.1	5.2
Chow Tai Fook Jewellery Group	Hong Kong	9,325	42.4	33.7	12.3	7.5	0.4	17.9	2.2
LEYSEN Jewelry Inc	China	776	39.9	8.5	14.4	11.6	0.0	17.0	2.3
Asian Star Co Ltd	India	225	70.6	65.0	12.3	4.9	0.9	14.2	1.6
<b>Average</b>			<b>43.1</b>	<b>22.6</b>	<b>14.2</b>	<b>8.7</b>	<b>0.4</b>	<b>19.8</b>	<b>2.8</b>
<b>Median</b>			<b>41.2</b>	<b>21.1</b>	<b>13.4</b>	<b>9.1</b>	<b>0.4</b>	<b>17.5</b>	<b>2.3</b>
<b>PNJ</b>	<b>Vietnam</b>	<b>672</b>	<b>39.9</b>	<b>28.2</b>	<b>32.6</b>	<b>17.9</b>	<b>0.3</b>	<b>18.0</b>	<b>3.2</b>

Source: BLOOMBERG, VNDIRECT

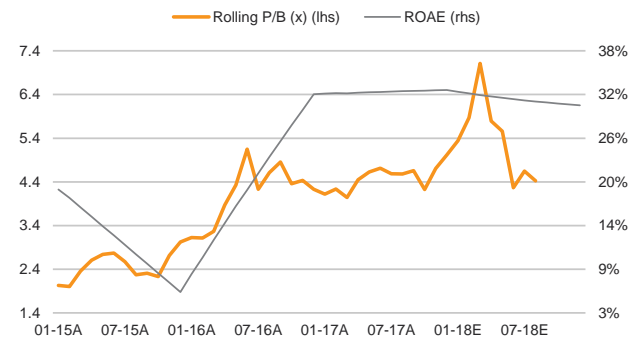
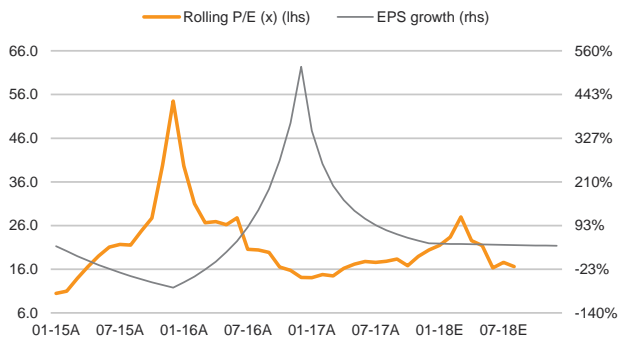
**We reiterate our ADD rating and target price of VND120,700/share.** We derive our new target price for PNJ by applying both DCF and a target PE multiple methods with equal weighting. For our target multiple, we use the peer average trailing P/E of 19.8x. Our target price translates into an upside of 25.7% and FY2018 forward PE of 19.4x.

Figure 9: Valuation summary

Method	Weight (%)	Fair value (VND/share)
DCF (ten years)	50%	118,000
2018 PER (peer's average of 19.8x)	50%	123,334
Target price		120,700

Source: VNDIRECT

## Valuation



### Income statement

(VNDbn)	12-17A	12-18E	12-19E
Net revenue	10,977	14,271	17,432
Cost of sales	(9,065)	(11,722)	(14,252)
Gen & admin expenses	(188)	(233)	(337)
Selling expenses	(775)	(1,020)	(1,346)
<b>Operating profit</b>	<b>949</b>	<b>1,296</b>	<b>1,497</b>
Operating EBITDA	910	1,230	1,431
Depreciation and amortisation	39	66	66
<b>Operating EBIT</b>	<b>949</b>	<b>1,296</b>	<b>1,497</b>
Interest income	9	7	9
Financial expense	(56)	(43)	(47)
Net other income	6	2	2
Income from associates & JVs	0	0	0
<b>Pre-tax profit</b>	<b>908</b>	<b>1,262</b>	<b>1,461</b>
Tax expense	(183)	(252)	(292)
Minority interest	0	0	0
<b>Net profit</b>	<b>725</b>	<b>1,010</b>	<b>1,169</b>
Adj. net profit to ordinary	725	1,010	1,169
Ordinary dividends	(185)	(292)	(324)
<b>Retained earnings</b>	<b>540</b>	<b>718</b>	<b>845</b>

### Balance sheet

(VNDbn)	12-17A	12-18E	12-19E
Cash and equivalents	175	319	571
Short term investments	160	214	261
Accounts receivables	85	92	118
Inventories	3,402	4,142	4,935
Other current assets	74	85	105
<b>Total current assets</b>	<b>3,896</b>	<b>4,852</b>	<b>5,990</b>
Fixed assets	487	558	657
Total investments	0	0	0
Other long-term assets	109	109	118
<b>Total assets</b>	<b>4,492</b>	<b>5,519</b>	<b>6,765</b>
Short-term debt	846	970	1,185
Accounts payable	279	361	436
Other current liabilities	364	409	520
<b>Total current liabilities</b>	<b>1,489</b>	<b>1,740</b>	<b>2,141</b>
Total long-term debt	46	105	105
Other liabilities	7	6	7
Share capital	1,081	1,622	1,622
Retained earnings reserve	772	866	1,663
<b>Shareholders' equity</b>	<b>2,950</b>	<b>3,668</b>	<b>4,512</b>
Minority interest	0	0	0
<b>Total liabilities &amp; equity</b>	<b>4,492</b>	<b>5,519</b>	<b>6,765</b>

### Cash flow statement

(VNDbn)	12-17A	12-18E	12-19E
<b>Pretax profit</b>	<b>908</b>	<b>1,262</b>	<b>1,461</b>
Depreciation & amortisation	39	66	66
Tax paid	(154)	(252)	(292)
Other adjustments	(142)	(5)	(4)
<b>Change in working capital</b>	<b>(542)</b>	<b>(628)</b>	<b>(650)</b>
<b>Cash flow from operations</b>	<b>109</b>	<b>443</b>	<b>581</b>
Capex	(115)	(150)	(180)
Proceeds from assets sales	8	14	16
Others	3	(54)	(47)
Other non-current assets changes	(160)	0	(9)
<b>Cash flow from investing activities</b>	<b>(264)</b>	<b>(190)</b>	<b>(220)</b>
New share issuance	975	0	0
Shares buyback	0	0	0
Net borrowings	(615)	183	215
Other financing cash flow	0	0	0
Dividends paid	(185)	(292)	(324)
<b>Cash flow from financing activities</b>	<b>175</b>	<b>(109)</b>	<b>(109)</b>
Cash and equivalents at beginning of period	155	175	319
<b>Total cash generated</b>	<b>20</b>	<b>144</b>	<b>252</b>
Cash and equivalents at the end of period	175	319	571

### Key ratios

	12-17A	12-18E	12-19E
<b>Dupont</b>			
Net profit margin	6.6%	7.1%	6.7%
Asset turnover	2.72	2.85	2.84
ROAA	17.9%	20.2%	19.0%
Avg assets/avg equity	1.82	1.51	1.50
ROAE	32.6%	30.5%	28.6%
<b>Efficiency</b>			
Days account receivable	1.30	1.20	1.20
Days inventory	137	129	126
Days creditor	11.2	11.2	11.2
Fixed asset turnover	24.3	27.3	28.7
ROIC	18.9%	21.3%	20.1%
<b>Liquidity</b>			
Current ratio	2.60	2.80	2.80
Quick ratio	0.30	0.40	0.50
Cash ratio	0.20	0.30	0.40
Cash cycle	127	119	116
<b>Growth rate (yoy)</b>			
Revenue growth	28.2%	30.0%	22.1%
Operating profit growth	30.9%	36.6%	15.5%
Net profit growth	60.8%	39.3%	15.7%
EPS growth	45.7%	39.3%	15.7%
<b>Share value</b>			
Basic EPS (VND)	4,471	6,229	7,209
BVPS (VND)	18,193	22,621	27,826

Source: VNDIRECT

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