

Equity Update | February 18, 2019

We reiterate our BUY rating for PNJ with a 12M TP of VND 123,000 (26% upside). Below are key investment highlights:

▪ **2018 snapshots: Diamond & Gemstone jewelry is key to SSSG & margin upswing**

PNJ ends 2018 with VND 14,680bn in sales (+33% YoY) and VND 960bn in NPAT (+32.5% YoY). The continuously breakneck growth is attributable to: 1) 20% SSSG of gold jewelry retail, 2) overall margin improved by 160 bps to 18.9%, and 3) 61 new stores, grossing 324 stores nationwide. Our research indicates the primary factors to SSSG & margin upswing are accelerated demand for jewelry products and the increasing proportion of diamond & gemstone jewelry in gold retail.

In 2018, PNJ established 2 subsidiaries as replacements for PNJ Labs, 1st is PNJP Ltd. (PNJ Production Ltd.) focusing on wholesales and 2nd is CECL (Customer Era Company Ltd.) focusing on applying high tech (big data, omni channel etc.) in optimizing marketing & logistics activities. It is noticeable that PNJ booked from services a record sale of VND 106.4bn in 2018 (+250% YoY) and enjoyed VND 85bn gross profit (+983% YoY).

The only unit that underperformed in 2018 is silver retail, which recorded 0% SSSG and suffered plummeting margin (-380bps yoy to 61.9%).

▪ **2019F outlook: Key themes are Diamond & Gemstone jewelry, New collections & Data-driven customer approach**

We estimate PNJ to achieve VND 18,145bn in sales (+23.6% YoY) and VND 1,249bn in NPAT (+30.1% YoY) in 2019F. Followings are our key assumptions:

- Diamond & Gemstone jewelry to continue rising its proportion in gold retail as company guidance, which consequentially allows PNJ to increase both ticket size and margin in long run.
- Silver retail to recover as PNJ plans to redesign its silver collections towards more bold and larger pieces. We estimate 5% SSSG and 65% GPM for this unit in 2019.
- Wholesales & gold bar to see 20% YoY growth in sales (same as 2018) while export sales to see 10% YoY growth (2018: +25.6% YoY).
- 50 new stores, including 44 PNJ Gold, 3 CAO Fine and 3 watches stores.
- SG&A expenses to sales ratio to remain stable at 10.5% (2018: 10.4%).

▪ **Valuation:** We reiterate our BUY rating for PNJ with a 12M TP of VND 123,000 – a 26% upside, derived from both DCF – VND 118,000 (see Figure 7) and P/E – VND 128,000 @ PER 17.1x and 2019F EPS of VND 7,500 (see Figure 8). We expect 2019F dividend to be VND 2,000, implying ROI of 28.1%.

▪ **Investment risks:** (1) Lower-than-estimate demand for jewelry retail; (2) Slower store expansion due to lack of retail locations; (3) SG&A expands at faster pace than estimate.

BUY – Potential Upside 28.1%

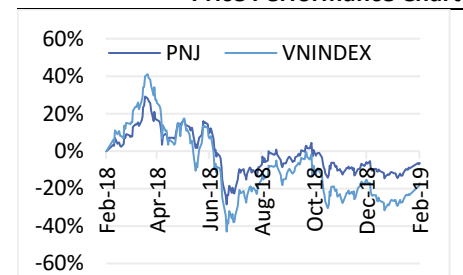
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Target Price
 12-month price target: **VND 123,000**
 Expected 12-month dividend: **VND 2,000**

Trading Data and Key Metrics

Ticker	PNJ
Sector	Jewelry & Luxury Goods
Listed since	Mar-2009
Price as of Feb 13, 2019 (VND)	97,600
52-week range (VND'000)	74.5/134.5
Market cap (VND bn)	16,309
Shares outstanding (mn)	167.1
Free Float (mn)	141.9
15-day average volume	214,911
2018 P / B (x)	4.2x
2018 P / E (x)	16.2x
Dividend yield (%)	1.7%
Net Debt to Equity (x)	0.36

Source: TVS Research, Bloomberg Data

Price Performance Chart

Price performance	3M	12M	YTD
Absolute	+5.3%	-6.3%	+6.1%

Source: Bloomberg

Company Description

Phu Nhuan Jewelry Joint Stock Company is the No.1 jewelry and watch specialist retailer in Vietnam with 30% market share by end-2018. The Company manufactures and markets jewelry pieces, stamped gold bars, and jewelry products made of gold and silver. It also trades luxury watches, gemstones and precious metals as materials for jewelry manufacturing. The Company operates jewelry stores under various brand names, such as PNJ Gold, PNJ Silver and CAO Fine Jewelry. In addition, the Company provides jewelry evaluation and testing services. The Company's competitive advantages lie in its fully integrated value chain from manufacturing to retail, and 324 retail stores nationwide. Major shareholders are Chairwoman and Related parties (15.5%).

SUMMARY FINANCIALS

Earning Model (VNDbn)	2017A	2018A	2019F	2020F
Net sales	10,977	14,573	18,012	20,956
Cost of sales	9,065	11,794	14,482	16,718
Gross profit	1,912	2,779	3,530	4,238
Selling expenses	775	1,171	1,441	1,781
General administration expenses	188	346	450	629
Other operating income/(expenses)	6	3	3	4
EBITDA	994	1,307	1,691	1,893
Depreciation & Amortization	39	42	49	61
EBIT	955	1,265	1,642	1,832
Net interest income/(expenses)	-48	-59	-74	-86
Net investment income	0	0	0	0
Others (recurring)	0	0	0	0
Pretax Profit	907	1,206	1,569	1,746
Income tax	183	246	320	356
Tax rate (%)	20%	20%	20%	20%
Minorities	0	0	0	0
Net Income	725	960	1,249	1,391
EPS (basic, reported)	6,434	5,749	7,479	8,327
Weighted shares outstanding (mn)	108	167	167	167
Common dividends declared	0	0	0	0
DPS (VND)	1,713	1,585	2,062	2,296
Dividend Payout ratio (%)	27%	28%	28%	28%
Dividend cover (X)	3.8x	3.6x	3.6x	3.6x

Growth and Margin	2017A	2018A	2019F	2020F
Sales Growth (%)	28.2%	32.8%	23.6%	16.3%
EBITDA Growth (%)	24.0%	31.5%	29.3%	12.0%
EBIT Growth (%)	24.4%	32.5%	29.8%	11.6%
Net Income Growth (%)	60.6%	32.5%	30.1%	11.3%
EPS Growth (%)	46.8%	-10.6%	30.1%	11.3%
Gross Margin (%)	17.3%	18.9%	19.5%	20.1%
EBITDA Margin (%)	9.1%	9.0%	9.4%	9.0%
EBIT Margin (%)	8.7%	8.7%	9.1%	8.7%
Net Income Margin (%)	6.6%	6.6%	6.9%	6.6%

Cash flow Statements (VNDbn)	2017A	2018A	2019F	2020F
Pretax profit	907	1,206	1,569	1,746
<i>Adjustments for:</i>				
Depreciation and amortization	39	42	49	61
Change in inventories	-563	-1,414	-426	-1,126
Change in trade receivables	-42	-123	-21	-16
Change in trade payables	17	289	112	62
Other operating cash flow	-249	-305	-426	-414
Cash flow from operations	109	-305	856	313
Net Capital expenditure	-115	-336	-300	-92
Acquisition	0	0	0	0
Divestures	0	0	0	0
Other investments, net	-149	168	0	0
Cash flow from investing	-264	-169	-300	-92
Equity issued	975	97	0	0
Net borrowings	-615	672	564	-11
Dividends to shareholders	-185	-265	-344	-383
Cash flow from financing	174	505	220	-395
Net cash flow	20	31	775	-173
Opening cash	155	175	207	982
Closing cash	175	207	982	809

Balance Sheet (VNDbn)	2017A	2018A	2019F	2020F
Cash and equivalents	175	207	982	809
Financial investment	160	0	0	0
Accounts receivable	40	79	100	116
Inventory	3,402	4,816	5,242	6,368
Prepaid expenses, other CA	119	179	221	257
Total current assets	3,896	5,280	6,545	7,551
Property and equipment				
At cost	397	454	612	730
<i>Less accumulated depreciation</i>	<i>-191</i>	<i>-228</i>	<i>-275</i>	<i>-334</i>
Net property and equipment	206	226	337	396
Net intangibles	281	493	591	639
Total investment	0	0	0	0
Other long - term assets	109	304	486	471
Total Assets	4,492	6,303	7,959	9,057
Account Payables	279	291	402	464
Short-term debt	846	1,558	2,121	2,108
Other current liabilities, CL	364	693	857	997
Total Current Liabilities	1,489	2,542	3,380	3,569
Long-term debt	46	8	10	11
Other long-term liabilities	8	8	10	11
Total long-term liabilities	54	16	19	22
Stockholders' equity	2,950	3,745	4,560	5,465
Common Equity	1,081	1,670	1,670	1,670
Treasury shares	877	925	925	925
Capital surplus	0	0	0	0
Retained earnings	772	885	1,641	2,481
Budget sources and other funds	220	265	324	389
Minority interest	0	0	0	0
Total liabilities and equity	4,492	6,303	7,959	9,057
Capitalized leases	0	0	0	0
Capital employed	3,003	3,761	4,579	5,488

Ratios	2017A	2018A	2019F	2020F
ROE (%)	24.6%	25.6%	27.4%	25.4%
ROA (%)	16.1%	15.2%	15.7%	15.4%
ROIC (%)	24.1%	25.5%	27.3%	25.3%
Inventory days	124	125	125	125
Receivable days	1	1	2	2
Payable days	11	8	10	10
Cash conversion cycle (days)	114	119	117	117
Asset Turnover (x)	2.4x	2.3x	2.3x	2.3x
Net debt/equity (x)	0.2x	0.4x	0.3x	0.2x
Interest cover - EBIT(x)	17.4x	20.7x	17.0x	16.3x

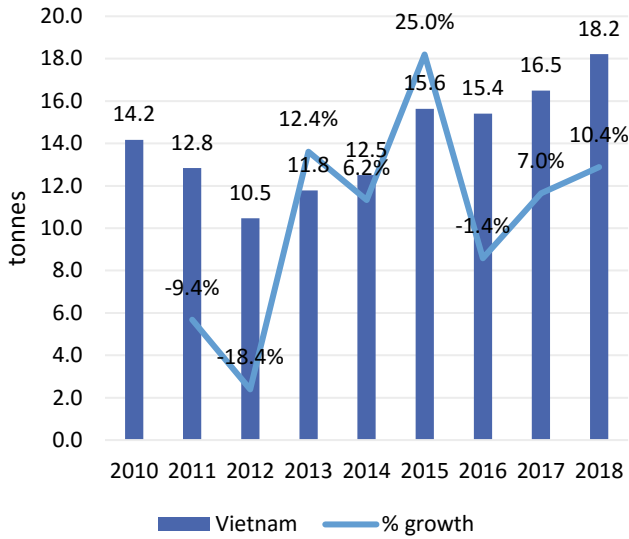
Valuation (Multiples)	2017A	2018A	2019F	2020F
EV / EBITDA (x)	9.6x	11.9x	9.6x	8.6x
P/E (x)	13.7x	16.2x	13.1x	11.7x
Dividend Yield (%)	1.9%	1.7%	2.1%	2.4%
P/B (x)	3.2x	4.2x	3.6x	3.0x

Notes: CA = current assets; CL = current liabilities

Source: Fiiipro historical data, TVS model and forecast

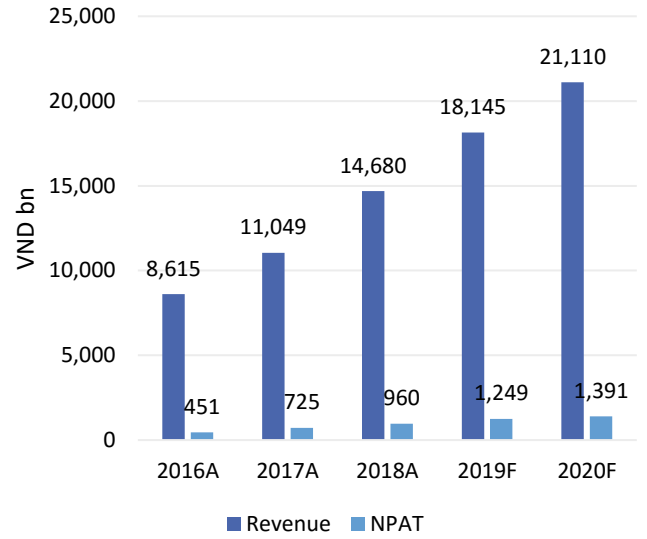
FOCUS CHARTS

Figure 1: Jewelry demand in Vietnam witnesses strong growth in recent years



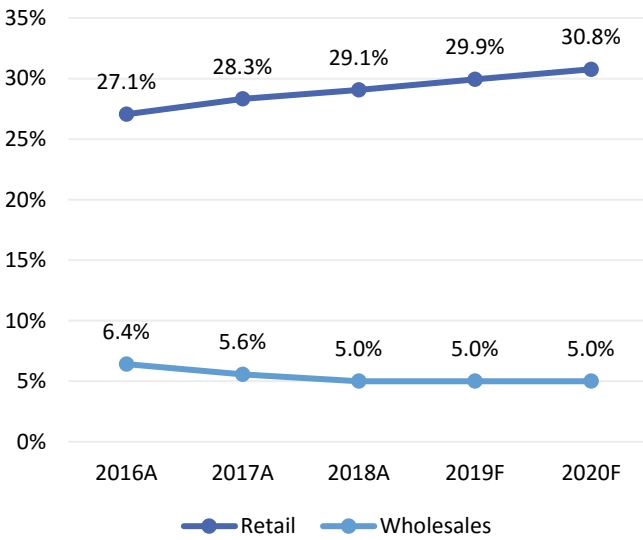
Source: World Gold Council

Figure 2: 2019-20F revenue and NPAT forecast



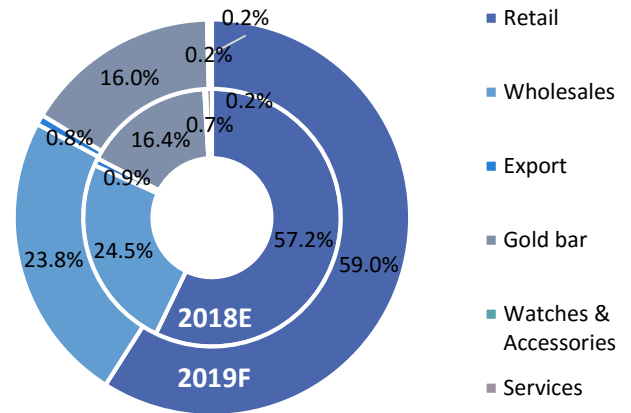
Source: Company data, TVS Research

Figure 3: Margin expansion in jewelry retail will continue boosting overall margin



Source: Company data, TVS Research

Figure 4: Retail to increase its proportion in total revenue as company guidance



Source: Company data, TVS Research

PNJ ends 2018 with VND 14,680bn in sales (+33% YoY) and VND 960bn in NPAT (+32.5% YoY) thanks to 1) 20% SSSG of gold jewelry retail, 2) overall margin improved by 160 bps to 18.9%, and 3) 61 new stores.

In 2018, PNJ established 2 subsidiaries, 1st is PNJP Ltd. focusing on wholesales and 2nd is CECL focusing on applying high tech in optimizing marketing & logistics activities

The only segment that underperformed in 2018 is silver retail.

2018 snapshots: Diamond & Gemstone jewelry is key to SSSG & margin upswing

PNJ ends 2018 with VND 14,680bn in sales (+33% YoY) and VND 960bn in NPAT (+32.5% YoY) despite the 57% expansion of SG&A expenses. The continuously breakneck growth is attributable to: 1) 20% SSSG of gold jewelry retail, 2) overall margin improved by 160 bps to 18.9%, and 3) 61 new stores, grossing 324 stores nationwide. Our research indicates the primary factors to SSSG & margin upswing are:

1. Accelerated demand for jewelry products. According to World Gold Council, Vietnam's jewelry market posted 10% YoY growth in 2018, achieving an all-time-high consumption amount of 18.2 tones. This record placed Vietnam amongst top 3 growing markets for jewelry after Hongkong & Egypt (global average +0% YoY).
2. The increasing proportion of diamond & gemstone jewelry in gold retail, which contains 2-2.5x unit price vs. ordinary jewelry and thus yields superior margin (c.50% vs. c.20%, Company comments). Particularly, diamond & gemstone jewelry sales grew 57% YoY to appx. VND 2,100bn last year, contributing c.25% to gold retail sales (2017: 23.8%) and lifting margin of this unit to 27.9% (+130bps YoY). Overall, gold retail sales grew 44.5% YoY and accounted for 55.2% of total revenue (2017: 50.8%), while wholesales, gold bar, watches & accessories also enjoyed healthy growth of ~20% YoY each.

In 2018, PNJ established 2 subsidiaries as replacements for PNJ Labs, particularly 1st is PNJP Ltd. (PNJ Production Ltd.) with VND 100bn capital focusing on wholesales and 2nd is CECL (Customer Era Company Ltd.) with VND 20bn capital focusing on applying high tech (big data, omni channel etc.) in optimizing marketing & logistics activities. It is noticeable that PNJ booked a record sale of VND 106.4bn from services last year (+250% YoY), mostly in 4Q18 when PNJP provided non-recurring processing work for 3rd parties. Accordingly, PNJ enjoyed VND 85bn gross profit from services in 2018 (+983% YoY).

The only segment that underperformed in 2018 is silver retail, which recorded 0% SSSG and suffered plummeting margin (-380bps YoY to 61.9%). However, silver retail only accounted for a minor portion (1.7% of total sales) and thus doesn't have significant impact on PNJ's overall performance.

Regarding balance sheet, PNJ was still able to maintain strong cash position of VND 207bn by end-19 (+VND 32bn YoY). Cash conversion cycle has extended to 119 days (+5 days YoY), which is reasonable to support top line growth. PNJ has also increased its debt level to 29% of total capital (+6% YoY) at an exceptionally good cost of debt of 4% p.a. Free cash flow has turned negative at -VND 458bn after +VND 143bn in 2017 due to expanded working capital and heavy capex.

2019F outlook: Key themes are Diamond & Gemstone jewelry, New collections & Data-driven customer approach

We estimate PNJ to achieve VND 18,145bn in sales (+23.6% YoY) and VND 1,249bn in NPAT (+30.1% YoY) in 2019F. Followings are our key assumptions:

1. Diamond & Gemstone jewelry to continue rising its proportion in gold retail as company guidance, which consequentially allows PNJ to increase both ticket size and margin in long run. This assumption is built on: 1) 6-8 new collections to be released 2019, which could capitalize on demands for more sophisticated jewelry and of new customer segment such as LGBT community, and 2) a specialized IT unit (CECL) that would deliver more effective data-driven customer approach & logistics arrangement. See below for gold retail sales forecast.

Figure 5: Revenue projection for 2019-20F

(VND bn)	2017E	2018E	2019F	2020F	2021F	2022F	2023F
Gold retail	5,610	8,109	10,391	12,220	13,850	14,750	15,703
- Diamond & Gemstone	1,336	2,098	2,891	3,645	4,411	5,003	5,652
% yoy growth	n/a	57%	38%	26%	21%	13%	13%
% in Gold retail	23.8%	25.0%	27.0%	29.0%	31.0%	33.0%	35.0%
- Non-Diamond & Gemstone	4,274	6,011	7,500	8,576	9,439	9,747	10,051
% yoy growth	n/a	41%	25%	14%	10%	3%	3%
Gross margin	26.6%	27.9%	28.8%	29.8%	30.7%	31.6%	32.5%
- Diamond & Gemstone	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%
- Non-Diamond & Gemstone	19.3%	20.1%	20.6%	21.1%	21.6%	22.1%	22.6%

Source: TVS Research

2. Silver retail to recover as PNJ plans to redesign its silver collections towards more bold and larger pieces. We estimate 5% SSSG and 65% GPM (+310 bps) for this unit in 2019 with 10 new stores.
3. Wholesales & gold bar to see 20% YoY growth in sales (same as 2018) while export sales to see 10% YoY growth (2018: +25.6% YoY).
4. 50 new stores, including 44 PNJ Gold, 3 CAO Fine and 3 watches stores (a flagship store – PNJ Next – specializing in watches will open soon at the privileged retail corner of Hai Ba Trung-Dien Bien Phu streets, HCMC).
5. SG&A expenses to sales ratio to remain stable at 10.5% (2018: 10.4%).

Valuation: We reiterate our **BUY** rating for PNJ with a 12M TP of **VND 123,000 – a 26% upside**, derived from both **DCF – VND 118,000** (see Figure 7) and **P/E – VND 128,000 @ PER 17.1x and 2019F EPS of VND 7,500** (see Figure 8). We expect 2019F dividend to be VND 2,000, implying ROI of 28.1%.

Investment risks: (1) Lower-than-estimate demand in jewelry retail would drag down SSSG and new store sales, which undermines future earnings; (2) Slower store expansion due to lack of retail locations; (3) SG&A expands at faster pace than estimate would hinder net profit.

Figure 6: Revenue projection for 2019-20F

Revenue projection (VNDbn)	2016A	2017A	2018A	2019F	2020F
Jewelry retail	4,322	5,865	8,393	10,709	12,568
PNJ Gold	4,087	5,610	8,109	10,391	12,220
SSSG	8.0%	21.0%	20.0%	18.0%	12.0%
PNJ Silver	170	231	257	276	297
SSSG	12.0%	14.0%	0.0%	5.0%	5.0%
CAO Fine	65	24	26	42	51
SSSG	8.0%	14.0%	0.0%	5.0%	5.0%
Jewelry wholesale	2,565	3,011	3,600	4,320	4,968
% growth	-0.9%	17.4%	19.6%	20.0%	15.0%
Jewelry export	103	108	135	149	164
% growth	10.0%	4.4%	25.6%	10.0%	10.0%
Gold bar	1,596	2,011	2,412	2,895	3,329
% growth	3.5%	26.0%	19.9%	20.0%	15.0%
Watches & Accessories	10	24	34	41	48
SSSG	8.0%	14.0%	0.0%	10.0%	10.0%
Rendering services	19	31	106	32	34
% growth	-20%	62%	249%	5.0%	5.0%
Total gross revenue	8,615	11,049	14,680	18,145	21,110
New unique store	25	50	55	50	35
Total unique store	219	269	324	374	409

Source: Company data, TVS Research

Figure 7: DCF-based target price calculation for PNJ

VNDbn		2018F	2019F	2020F	2021F	2022F
EBIT		1,642	1,832	2,099	2,140	2,307
EBIT (1-tax)		1,308	1,459	1,671	1,704	1,837
D&A expenses		49	61	70	75	79
Change in working capital		-214	-977	-16	-448	-101
Capex		-300	-92	-66	-39	-39
FCFF		842	451	1,659	1,292	1,775
PV of FCFF		765	373	1,245	881	1,100
Beta	0.99					
WACC	10.0%					
Terminal growth rate	3.0%					
PV of Terminal value	16,082					
Enterprise value	20,446					
Less: Net debt	717					
Equity value	19,729					
Number of shares (mn)	167.0					
Equity value per share (VND)	118,000					

Source: TVS Research

Figure 8: Regional jewelry retail comparable valuations*

Identifier	Company Name	EV/Sales forward	Adj. P/E forward	EV/EBITDA forward	Country of HQ
PNJ.HM	Phu Nuan Jewelry JSC	1.1x	13.4x	8.3x	VIETNAM
	Comparable mean	1.1x	17.1x	8.1x	
116 HK Equity	CHOW SANG SANG HLDG	0.4x	13.4x	5.4x	HONG KONG
590 HK Equity	LUK FOOK HOLDINGS INTL LTD	0.8x	16.1x	7.0x	HONG KONG
900905 CH Equity	LAO FENG XIANG CO LTD-B	0.4x	13.9x	8.5x	CHINA
TIF US Equity	TIFFANY & CO	2.4x	17.6x	10.8x	UNITED STATES
MC FP Equity	LVMH MOET HENNESSY LOUIS VUI	2.8x	22.7x	11.3x	FRANCE
FOSL US Equity	FOSSIL GROUP INC	0.4x	18.9x	4.6x	UNITED STATES
SIG US Equity	SIGNET JEWELERS LTD	0.4x	6.4x	5.9x	UNITED STATES
1929 HK Equity	CHOW TAI FOOK JEWELLERY GROU	1.2x	28.1x	11.3x	HONG KONG

Source: TVS Research for PNJ, Bloomberg for other companies

ANALYST CERTIFICATION

I, **Trung Dong**, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies or its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

RATING and VIEWS

Buy (B), Neutral (N), Sell (S) – Analysts recommend stocks as Buys or Sell based on his own views. Being assigned a Buy or Sell is determined by as total stock's return (TSR) potential that represents the price differentials between the current share price and the price target expected during the time horizon plus expected dividend yield. Any stock not assigned as Buy or Sell is deemed Neutral.

TVS Investment Research: Equity Rating Definitions

12-month rating	Definition
Buy	Total Stock's Return Potential > 15%
Neutral	Total Stock's Return Potential between (-15%) and 15%
Sell	Total Stock's Return Potential < (-15%)
Short-term rating	Definition
Buy	Stock price expected to rise within three-month because of a specific catalyst or event
Sell	Stock price expected to fall within three-month because of a specific catalyst or event
Not-rated	The investment rating and target price, if any, suspended as there is not a sufficient fundamental basis for determining an investment rating or target.

RATING HISTORY and TARGET PRICE

Issued Date	Research	Recommendation	Market Price (VND)	01-year target price (VND)
January 31 st , 2019	Update	BUY	97,600	123,000
November 29 th , 2017	Update	BUY	76,000	92,000
July 26 th 2017	Update	BUY	66,000	76,000
May 3 rd 2017	Update	BUY	57,000	64,000
March 30 th 2017	Update	BUY	49,000	59,000

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