

22 June 2018

Consumer Cyclical

## Consumer

**Overweight** (Maintained)

### Set For The Year

Stocks Covered: 8  
 Ratings (Buy/Neutral/Sell): 7 / 1 / 0  
 Last 12m Earnings Revision Trend: Positive

**Maintain OVERWEIGHT. Top Picks are Sheng Siong and Food Empire. We remain optimistic about Singapore's consumer sector, as economic growth continues to bolster domestic spending, while tourism activities remain strong. Our channel checks show that retailers are revamping themselves to attract consumers to spend. Beyond Singapore, sentiment in the region is also improving. This is positive for the sector since most stocks under our coverage have exposure in regional markets.**

#### Top Picks

Sheng Siong (SSG SP) – BUY  
 Food Empire (FEH SP) – BUY

#### Target Price

SGD1.18  
 SGD1.07

**Retail sales to stay buoyant.** Excluding motor vehicles, retail sales were up by 0.7% in April and +2% YTD. Retail sales are largely a function of consumers' ability and willingness to spend. We believe robust growth in consumer durables category shows that consumers are more confident about the future. Over the next two quarters, we believe the sector's outlook remains bright with positive drivers from demand and supply.

Consumer sentiment should remain on solid footing, from strong economic growth (1Q18 GDP growth: 4.4% YoY) and an improved job market outlook. This month, key events like International Federation of Association Football (FIFA) World Cup and Great Singapore Sale (GSS) would also help drive consumer spending.

**Retailers are revamping themselves to attract consumers.** On the supply side, the past three challenging years of intensifying competition from e-commerce and muted consumer spending have forced retailers to redefine themselves. Many retailers have embraced omni-channels to improve overall brand experience. Online players are setting up physical stores, thereby offering more variety in the offline space.

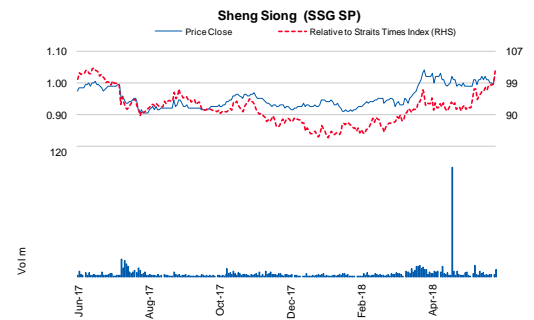
On the other hand, offline players are refreshing their store image, building flagship stores, creating new concepts to offer better in-store experience. We believe such efforts would help rejuvenate the retail scene and motivate consumers to get out of the house and spend.

**Regional markets doing well.** Most stocks under our coverage have exposure beyond Singapore. We note that North Asia is still seeing strong demand. China is chalking up close to 10% YoY growth in retail sales, while Hong Kong's retail sales are also backed by upbeat consumer sentiment and increased tourism. We are positive on Dairy Farm, which derives c.60% of sales from North Asia.

Consumer companies with exposure in Malaysia could expect a rosier outlook with the recent zero-rated GST. In Thailand, recent GDP data show the fastest growth in five years. A recovery in agricultural prices would be positive in raising overall purchasing power and benefit Thailand-concentrated companies like Thai Beverage. In Indonesia, strong consumer confidence and expectation of tapered inflation should keep domestic spending intact.

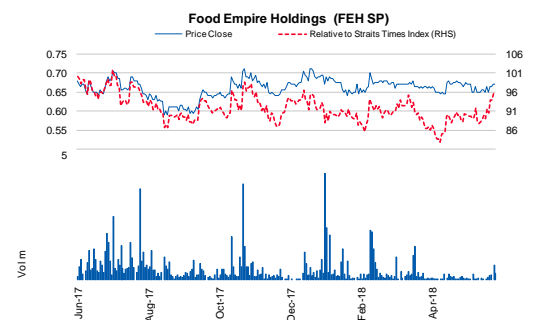
**Maintain OVERWEIGHT,** with preference for Sheng Siong and Food Empire. Sheng Siong is largely a Singapore play and expected to benefit from the uplift in domestic spending, new store openings and potential margin expansion. We like Food Empire as new snack line could bring higher sales and profitability to food ingredients business.

#### Sheng Siong's price chart



Source: Bloomberg

#### Food Empire's price chart



Source: Bloomberg

Company Name	Rating	Price	Target	% Upside (Downside)	P/E (x) Dec-18F	P/B (x) Dec-18F	Yield (%) Dec-18F
Dairy Farm	BUY	USD8.83	USD9.66	9.4	22.5	6.2	2.8
Delfi	BUY	SGD1.28	SGD1.47	15.0	26.0	2.6	2.3
Food Empire	BUY	SGD0.65	SGD1.07	63.9	11.0	1.3	1.6
Japan Foods Holding	BUY	SGD0.50	SGD0.63	25.0	13.9	2.4	4.2
Kimly	BUY	SGD0.35	SGD0.43	24.6	18.0	4.6	2.8
Sheng Siong	BUY	SGD1.00	SGD1.18	17.6	20.0	5.2	3.7
Thai Beverage	BUY	SGD0.77	SGD1.06	37.7	16.7	3.3	3.0
BreadTalk	NEUTRAL	SGD1.00	SGD0.93	(7.2)	29.2	4.1	2.1

Source: Company data, RHB

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# Singapore

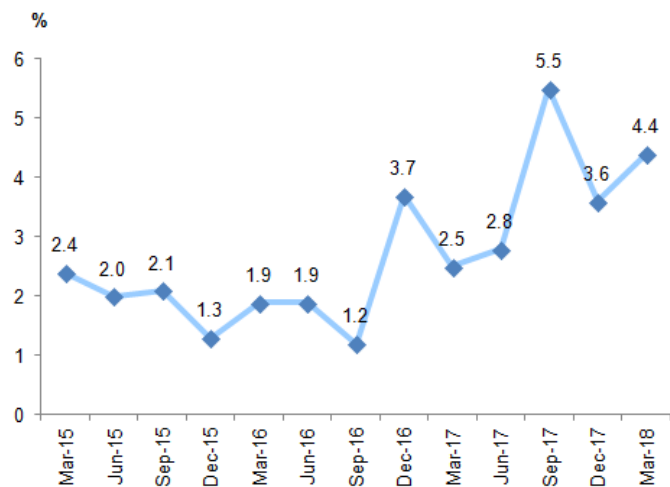
## Stronger consumer confidence, stronger domestic spending

**Healthy economic indicators prop up domestic spending.** Consumer spending is largely influenced by economic situation and purchasing power. Last year, the economy expanded at 3.6%, leading to retail sales picking up. This year, consensus is forecasting healthy growth in GDP, averaging about 3.2%, while Singapore's Ministry of Trade and Industry is expecting GDP growth of 2.5-3.5%.

Job prospects are also looking brighter with the number of job vacancies exceeding the number of unemployed people. Unemployment rate moderated to 2% in 1Q18 (1Q17: 2.2%). As a result, we expect domestic spending to remain strong over the next two quarters in tandem with the stronger economy and improved job market outlook.

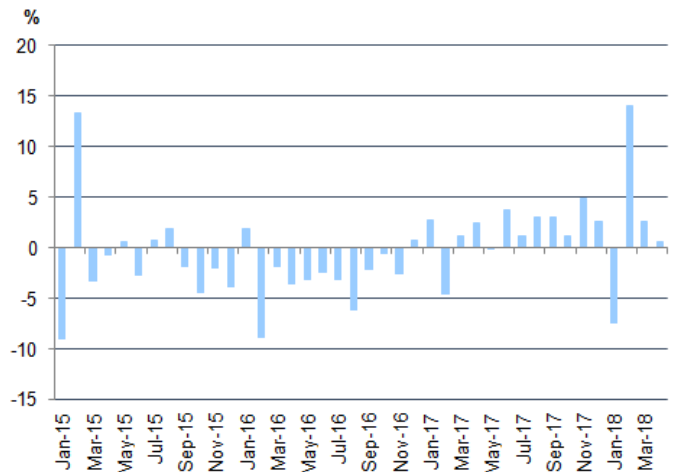
◆ Domestic spending to grow in tandem with economic growth

Figure 1: GDP started picking up in 2017



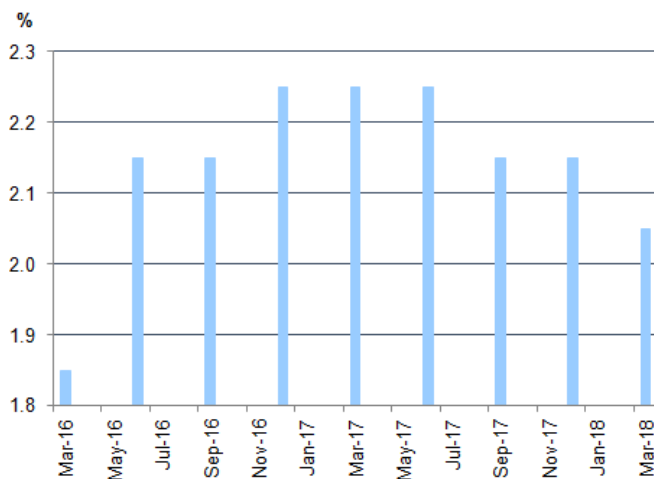
Source: Ministry of Trade and Industry Singapore, CEIC

Figure 2: Retail sales picked up in tandem with GDP growth



Source: Department of Statistics Singapore, CEIC

Figure 3: Lower unemployment rate also positive for consumer sentiment



Source: Ministry of Manpower Singapore, RHB

**Pent-up demand to give extra boost.** We note that economic growth was lacklustre in 2015-2016, leading to muted consumer spending and a challenging retail environment, before picking up strongly in 2H17. We believe the pent-up demand will be unleashed this year, giving extra boost to retail sales.

◆ Willingness to spend remains high due to pent-up demand in 2015-2016

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**Positive signs on consumer confidence.** YTD, Singapore's retail sales index has been fairly positive. In particular, consumer durables have shown robust growth. Higher expenditures in this category suggest consumers are more confident in their outlook and more willing to spend for the future. We believe this would translate to overall positive growth in domestic spending over the near term.

**Figure 4: Robust growth in consumer durables and consumer discretionary**

	Mon-Apr YoY growth
Retail Sales Index excluding Motor Vehicles	+2%
<b>Significant categories</b>	
Food & Beverage	+10%
Furniture & Household	+6%
Wearing Apparels & Footwear	+4%
Department Stores	+3%

Source: Department of Statistics Singapore

Department stores and consumer discretionary items like footwear and apparel have had higher-than-average growth YTD. This suggests higher spending power and willingness to spend. This could also be partially attributed to higher tourist arrivals in Singapore, which tie in with our observation of more tourists in retail malls including Bugis Junction, Wisma Atria and Marina Bay Sands. We believe increased tourism certainly helped boost foot traffic in department stores and lend support to sales growth.

**Figure 5: Strong foot traffic at BHG department store on a weekend, backed by both locals and tourists**



Source: RHB

**Figure 6: High crowd traffic even on a weekday at Wisma Atria**



Source: RHB

**Figure 7: Marina Bay Sands crowded with tourists on a weekend**



Source: RHB

**Figure 8: Tourists were not just window-shopping as we noticed purchases were made for luxury brands**



Source: RHB



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### Key events to prompt consumers to spend

**World Cup.** June marks the start of the FIFA World Cup, with games being played around the evenings and late nights in Singapore. Viewers are likely to watch in the games in the comfort of their homes, or in restaurants or pubs.

We expect sales of snacks, takeaway foods, as well as alcoholic and non-alcoholic beverages to rise, thereby giving a slight sales kick to supermarkets and convenience store operators like Sheng Siong and Dairy Farm. Do note however, that these are not high margin items for the grocery retailers.

Restaurants and fast food outlets that air football matches at their premises are likely to see a one-off surge in volumes. Takeaway foods and food delivery services could benefit as well. foodpanda Singapore for instance, advertises during the 15-minute half-time break. On the other hand, full-service restaurants that do not air matches could lose out during these two months.

In Thailand, we are optimistic on Thaibev, which could potentially see some recovery in alcohol consumption with the aid of World Cup.

**GSS.** Apparel, footwear and department stores are the main categories that will benefit from the GSS. We expect retail sales to pick up amid the improved consumer sentiment. Coupled with increased tourism activities and pent-up demand domestically, we expect sales at both specialty stores and department stores to do well during these two months.

- ◆ Expect June-July to show stronger sales growth for food & beverage products/retailers with the help of World Cup

Figure 9: GSS has started



Source: RHB

Figure 10: Victoria's Secret sales drew crowds



Source: RHB

### Resurrection of retailers

**On the supply side, retailers are putting in more effort.** The past three years of intensifying competition from e-commerce and muted consumer spending have compelled retailers to be less complacent, and they are now revamping themselves to reel in consumers to spend.

Many retailers have not only embraced online platforms but also reinvested in physical stores to improve the overall brand experience. From our observation, the following are some of the new retail trends put in place to woo consumers:

- Refreshing store image to attract millennial consumers.** Millennials are image-conscious and do not like to be seen stepping into an "uncool" shop. As such, brands must constantly refresh their image to attract the younger crowd. Sheng Siong's outlets in new housing estates for instance, feature cleaner and more organised displays as opposed to older stores, which used to cater to lower-income consumers.

- ◆ New retail trends in place to woo consumers

- ◆ Revamping of store images to keep brands fresh

Dairy Farm now incorporates a wine and dine section within some of its *Cold Storage* supermarkets, giving consumers more time to spend within the store and hopefully, purchase more.

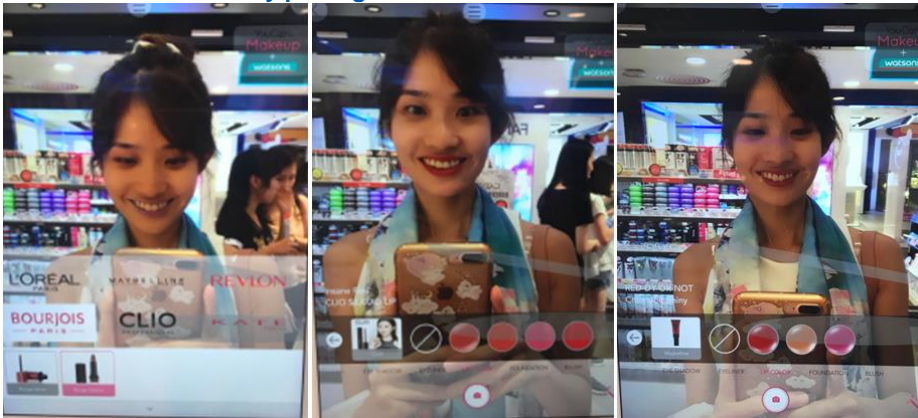
See [Sheng Siong: Still Thriving](#) (11 Apr 2018) and [Retail - Staples: Shopaholic Hits The Grocery Stores](#) (21 May 2018).

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In the health & beauty industry, Watsons Singapore and Sephora Singapore are leading the game by incorporating interactive digital screens that allow consumers to try on make-up virtually. Such features are fuss-free, more hygienic and attract digital-savvy millennials to enter the stores to try on new products and have fun. This encourages customers to try more products, have fun, and hopefully buy more.

- ◆ Integrating digital apps to enhance in-store experience

**Figure 11: Watsons' digital app available in-store allows customers to try on cosmetics without really putting them on**



Source: RHB

ii. **Flagships store on the rise.** Following the steps of major retail players like Uniqlo (Singapore), Victoria's Secret, and Apple (AAPL US, NR) to reinvest in physical stores to improve overall brand experience, more companies are opening flagship stores. Last year, we saw lifestyle brand, *Muji* opening its flagship store in Plaza Singapura, while technology and electronics retailer, *Challenger* opened a flagship store in Bugis Junction.

- ◆ More flagship stores to feature more products and concepts

**Figure 12: Apple conducts free hands-on sessions at its flagship store to enhance in-store brand experience**



Source: RHB

**Figure 13: Muji's flagship store houses new merchandise lines and even has a cafe**



Source: RHB

iii. **Concatenation of concepts.** Like *Muji's* flagship store, we are increasingly seeing mixed retail concepts in Singapore where food, play and shopping are combined. Bars like *Hopheads* and *Level Up* for instance, combine a "playing element" into the food and beverage (F&B) bar concept. These bars not only offer a great place to lounge in, with food and alcoholic options, they also have arcade machines, card games, foosball tables, and beer pong tables for patrons to enjoy.

- ◆ Combining more concepts into one store to give more reasons for consumers to visit

In this digitalised era where food delivery apps are sprouting, we think that the "playing element" at these bars gives consumers a more compelling reason to visit the physical outlets. It also encourages spending on F&B items, as customers receive tokens to play the arcade machines upon ordering alcoholic beverages.



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On the other hand, new arcades in Singapore like *Cow Play Cow Moo* and *Fat Cat* are combining retail and bringing it to a whole new level. These arcades feature over 200 machines and bring back the fun of winning tickets. They have a large redemption station with a wide selection of prizes. The prize selections include over 1,000 toys, collectibles and board games. The winning tickets can be regarded as “currency” to purchase prizes.

**Figure 14: Level Up Bar offers entertainment on top of food and drinks**



Source: Level Up

**Figure 15: Cow Play Cow Moo Arcade features over 200 machines and 1,000 different prizes to choose from**



Source: RHB

## Beyond Singapore

**Strong demand from North Asia.** China’s retail sales remain robust, chalking up 9.7% YoY growth during the first four months. Growth from retail sales of meals, cosmetics and commodities were higher than the overall average.

Retail sales in Hong Kong were even stronger (January-April: +13.9% YoY), backed by upbeat consumer sentiment and increased tourism. Sales of jewellery & watches, electronics and medicines & cosmetics skewed the high growth. We think this could be partly attributed to higher mainland Chinese tourist arrivals.

On this front, we are positive on Dairy Farm, which derives c.60% of its sales from North Asia. Its health & beauty segment is likely a key beneficiary of improved medicine & cosmetics sales in Hong Kong and China.

**Malaysia.** Consumer companies with exposure in Malaysia could expect a rosier outlook. The recent zero-rated GST is likely to improve sentiment and boost consumer spending over the next 12 months.

**In Thailand,** recent GDP data shows that growth is at its fastest in five years. Although private consumption has yet to see broad-based expansion, we note that the contraction in farm income has begun to slow. A recovery in agricultural prices would be positive in raising overall purchasing power and would benefit Thailand-concentrated company like Thaibev.

**In Indonesia,** consumer confidence has shown monthly consecutive improvement in May. This should benefit Delfi and Japfa, which have large exposure to the Indonesian market. Currently, we are expecting inflation to subside post-*Lebaran*, which should help boost demand. However, continuous IDR depreciation is a key risk, as consumers’ purchasing power would be negatively affected by cost pressures.

- ◆ Retail sales in China and Hong Kong still going strong on upbeat consumer sentiment

- ◆ Rosier outlook in Malaysia with zero-rated of GST

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## Conclusion

**Positive on near term outlook.** We are optimistic about the consumer sector in Singapore this year, as we expect to see higher consumer spending. Strong economic growth and an improved job outlook would continue to back consumer sentiment.

In addition, efforts put in by retailers would help rejuvenate the retail scene and motivate consumers to head outside of the house to spend. This would also have a positive spillover effect on other brick-and-mortar players when shopping malls and districts see stronger foot traffic.

Amongst our coverage, our Top Pick is grocery retailer, Sheng Siong. As a largely pure Singapore play, it is likely to benefit from the uplift in domestic spending and new store openings. The refreshed image at its outlets in new housing estates would also help attract new target consumers – the millennials. It would also enjoy margin expansion, as consumers purchase higher quality and higher value products such as fresh produce, which generate higher gross margins.

We also like Food Empire, an instant coffee mix player. We see Food Empire's efforts in diversifying outside of core Commonwealth of Independent States' (CIS) markets blossoming over the years. Growth should be driven by improved sales and profitability at the food ingredients business, as it ramps up utilisation at the second snack line. In Russia, declining income has led to increased opportunities in the mass-market product segment. With an approximately 50% market share in Russia's instant coffee mix industry, we believe Food Empire will remain resilient in spite of the depreciating RUB. Restructuring of its distribution in Ukraine will likely see positive impact on this year's earnings.

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