

29 May 2019

Consumer Non-cyclical | Retailing

Dairy Farm (DFI SP)

Neutral (from Buy)

Wait For Bargain Sales; Reduce To NEUTRAL

Target Price (Return) USD8.25 (+3%)
 Price: USD7.98
 Market Cap: USD10,795m
 Avg Daily Turnover (SGD/USD) 6.9m/5.0m

- **Downgrade to NEUTRAL from Buy** as share price edges closer to our USD8.25 TP, implying 3% upside and 2.8% dividend yield. In view of the escalating uncertainties brought forth by the ongoing US-China trade war, and that the share price has rebounded from the low of USD7.34 in March this year, we think the stock is now fairly valued, and downgrade to Neutral.

- **Health & Beauty segment could see slower growth in 2H19.** Health & Beauty continued to deliver stellar results in 1Q19 across most markets. According to the interim statement, North Asia was still seeing strong tourist footfall. Malaysia and Indonesia also saw encouraging results.

However, we note that total medicines and cosmetics retail sales in the Hong Kong market only grew 2.3% YoY in 1Q19. Moreover, consumer confidence in Mainland China seemed to have been impacted by the US-China trade war, with retail sales growth slowing more than expected to 7.2% YoY in Apr 2019. While YTD mainland tourist arrivals to Hong Kong grew in the mid-teens, we think growth in the Health & Beauty segment would slow down in 2H19 if consumer sentiment worsens.

- **US-China trade tensions may cap growth from associates.** Dairy Farm's 20%-owned Yonghui registered tremendous growth of 38% YoY in its core PATMI. While consensus is still bullish on Yonghui's performance this year, the escalation of US-China trade tensions and the resulting depreciation of CNY could cap its contribution to Dairy Farm, when translated to the group's reporting currency (USD).

- **Share price is likely to stay rangebound,** as the one-off growth arising from the full-year contribution of Yonghui (vs 9M contribution in FY18), maiden contribution from its RRHI associate, new acquisitions from Maxim's and reduction in opex could mitigate downside risks in the Health & Beauty segment and weaker earnings in the Food segment. In terms of valuation the stock is now trading at 22x FY19F P/E, similar to the peer average (Figure 13).

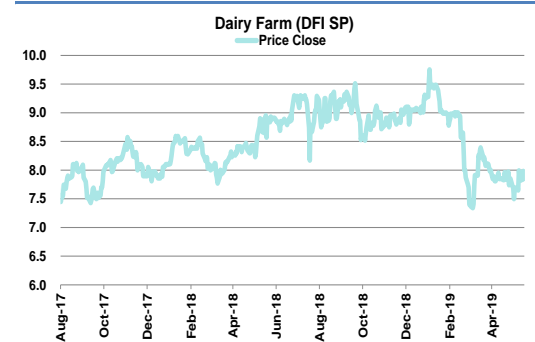
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(13.0)	0.3	(12.0)	(11.1)	(9.0)
Relative	(15.9)	7.6	(10.2)	(12.6)	1.3
52-wk Price low/high (USD)	9.94 – 7.02				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (USDm)	11,289	11,749	12,030	12,255	12,719
Recurring net profit (USDm)	466.4	424.0	498.8	534.4	591.6
Recurring net profit growth (%)	1.3	(9.1)	17.6	7.1	10.7
Recurring P/E (x)	23.1	25.4	21.6	20.2	18.2
P/B (x)	6.1	7.2	6.4	5.6	5.0
P/CF (x)	16.1	16.8	17.5	15.4	13.7
Dividend Yield (%)	2.6	2.6	2.8	3.1	3.3
EV/EBITDA (x)	19.4	37.6	18.4	17.1	15.8
Return on average equity (%)	23.8	6.4	30.1	28.5	27.9
Net debt to equity (%)	35.6	51.4	47.7	37.8	26.6
Interest coverage	14.0	2.4	12.7	12.9	18.8

Source: Company data, RHB

Figure 1: TP derivation

USD m	FY19F	FY20F	FY21F	FY22F	FY23F	FY24F
Net income	498.8	534.4	591.6	630.0	661.5	691.3
D&A costs	224.5	242.0	259.6	262.2	264.8	300.0
Net capex	(300.0)	(300.0)	(300.0)	(300.0)	(300.0)	(300.0)
Change in net working capital	109.4	43.1	68.6	68.6	30.0	0.0
Change in debt	(40.2)	0.0	(200.0)	0.0	0.0	0.0
Free cash flow to equity (FCFE)	493	520	420	661	656	691
Terminal value						12,416.3
Present value	492.5	480.1	358.6	521.6	478.8	8835.8
Total discounted FCFE	11167.5					
Value/ share (USD)	8.25					
Cost of equity	8.21%					
Risk-free rate	2.30%					
Beta	0.80					
Country risk premium	0.15%					
Market expected return	9.50%					
Terminal growth	2.50%					

Source: RHB

Food division remains a drag. Based on Dairy Farm's interim management statement, 1Q19 sales and profits from the food division continue to decline YoY. This is largely due to the store consolidation plan in the ASEAN region. Our recent ground checks in Kuala Lumpur (KL), Malaysia and Singapore further suggest that the group still has quite a number of hypermarkets and supermarkets caught in poor locations or have not undergone store improvement programmes. We believe the restructuring programme is still very much ongoing. As a result, we think the ASEAN supermarket business is likely to stay in the red in FY19F.

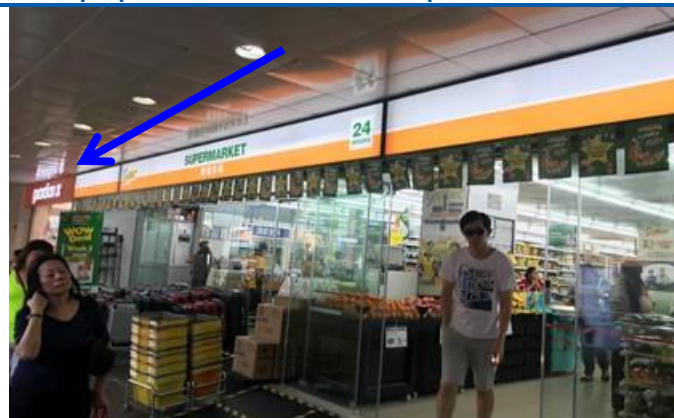
In addition, Hong Kong and Macau markets, which were holding up the food division's earnings, are seeing margin erosion due to higher rental and labour costs. The convenience store format is also suffering from higher operating costs. Consequently, we expect the food division to fare worse than last year.

Figure 2: Old Giant Supermarket at Bishan (during renovation period in Mar 2019)



Source: RHB

Figure 3: A portion of the Bishan Giant Supermarket has been repurposed as a Guardian store post-renovation



Source: RHB

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Figure 4: Post-renovation, *Giant* Supermarkets in Singapore feature new signboards, cool lighting and glass doors



Source: RHB

Figure 5: New/renovated *Guardian* stores also follow a similar concept



Source: RHB

Figure 6: New *Guardian* stores in Singapore also feature more sales promoters to provide help and advice to patrons...



Source: RHB



Figure 7: ... but there are still plenty of stores in Singapore which have not yet undergone store improvement



Source: RHB

Figure 8: Some of the *Giant* stores do not even have self-checkout machines yet



Source: RHB

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Figure 9: In KL, newly-renovated *Giants* also feature new signboards and increased space allocation for fresh produce



Source: RHB

Figure 10: Most of the *Guardian* stores we visited in KL also feature cool lighting and improved store layout



Source: RHB

Figure 11: But there are still a number of *Giant* stores with excessive retail space or caught up in poor locations...



Source: RHB

Figure 12: ... while others still have wide areas allocated to slow-moving, lower-margin general merchandise



Source: RHB

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Figure 13: Peer comparison

Company	BB Code	Share	Market	P/E			EV/ EBITDA	P/BV	ROE	Div Yield
		price	cap	FY19F	FY20F	FY21F	FY19F	FY19F	FY19F	FY19F
		(lcl ccy)	(USD m)	(x)	(x)	(x)	(x)		(%)	(%)
Dairy Farm	DFI SP	7.98	9,929	21.6	20.2	18.2	15.0	4.7	30.1	2.8
Sheng Siong	SSG SP	1.08	1,202	21.6	18.0	N/A	12.8	5.1	25.2	3.7
Yonghui Superstores	601933 CH	8.64	12,321	36.2	28.0	N/A	N/A	3.8	10.3	1.8
PT HERO	HERO IJ	945	278	N/A	N/A	N/A	N/A	N/A	N/A	N/A
CPALL	CPALL TB	74.5	21,150	28.4	25.3	21.0	17.2	8.2	21.3	1.6
President Chain	2912 TT	296.5	10,002	27.9	26.0	26.7	13.6	8.5	29.4	3.0
Puregold Price Club	PGOLD PM	48.65	2,652	19.0	16.9	15.0	N/A	2.2	12.5	0.9
Philippine Seven Corp	SEVN PM	124	1,782	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Taiwan Familymart	5903 TT	220.5	1,598	28.0	25.4	N/A	10.8	8.3	28.8	3.0
Wumart	1025 HK	2.68	178	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Lianhua	980 HK	1.4	200	N/A	N/A	N/A	N/A	0.9	-17.1	N/A
7-Eleven Malaysia	SEM MK	1.45	401	29.0	29.0	24.2	10.3	16.3	48.9	2.1
Robinsons Retail	RRHI PM	82.75	2,478	20.7	17.9	15.6	13.9	1.8	9.2	1.0
BGF Retail	282330 KS	213500	3,261	20.9	18.8	16.1	10.3	5.6	29.9	1.2
Sun Art Retail Group	6808 HK	7.14	8,677	22.1	20.4	19.6	6.6	2.3	10.7	1.9
AEON Malaysia	AEON MK	1.59	547	17.7	19.9	19.9	5.8	1.1	5.2	2.5
SIAM MAKRO	MAKRO TB	36.75	5,575	29.5	27.6	25.1	17.4	8.5	30.6	2.4
Wesfarmers Ltd	WES AU	34.62	27,941	18.5	19.2	17.9	N/A	4.0	13.8	7.7
Valor Holdings	9956 JP	2773	1,342	15.8	14.1	13.0	N/A	1.2	7.7	1.7
Seven & I Holdings	3382 JP	4555	36,197	19.9	16.7	15.6	N/A	1.6	8.1	2.1
AVERAGE				22.8	21.1	19.1	11.9	5.0	17.6	2.5

Source: RHB

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