# Singapore Sector Update

27 August 2019

Consumer | Consumer

# Consumer

# Neutral (from Overweight)

## Spending Drops On Possible Recession

| | |
|---|---|
| Stocks Covered | 9 |
| Ratings (Buy/Neutral/Sell): | 5 / 4 / 0 |
| Last 12m Earnings Revision | Neutral |

- **Downgrade to NEUTRAL; Top Picks are Sheng Siong and Delfi.** 2Q19 results were disappointing. Delfi, Genting Singapore (GENS) and Sheng Siong reported in-line numbers, while Food Empire and Thai Beverage (Thaibev) beat our estimates. BreadTalk, Dairy Farm, Jumbo and MindChamps underperformed our projections. We have since downgraded Thaibev to TAKE PROFIT from Buy, and it is no longer a sector top pick. Sheng Siong and Delfi remain the preferred picks for the sector.
- **Limited upside from heavyweights in the near term.** While Thaibev beat our estimate this quarter, there is limited upside ahead, as we expect to see margins contract in its spirits segment. This is underpinned by: the normalisation of brown spirits' sales volumes; increased usage of new bottles for white spirits; and a higher molasses cost. High finance costs from the beer segment would also weigh down growth from SABECO. It is trading at 21x FY20F P/E – above the 5-year historical average of 20x – we think it is difficult for its share price to see a major lift, given anticipated slower growth next year.

  We also remained NEUTRAL on Dairy Farm, as strong results from its associates are likely to be dragged down by: weakened consumer sentiment following the Hong Kong protests; pre-opening costs of new *IKEA* stores; and declining sales in its food segment.

  GENS delivered decent numbers during the quarter, but this was only due to a high VIP win rate. We remain NEUTRAL, as it faces weaker mass gaming volumes following the increase in levy for Singaporeans and permanent residents. We also expect near-term headwinds on the VIP segment, given the economic uncertainties.
- **Gravitate towards low-risk stocks** over the next 12 months, with preference for Sheng Siong and Delfi amidst an impending recession. The Government has downgraded Singapore's 2019F GDP growth to 0-1%. Cognisant of the weakening economic outlook, consumers have turned cautious on spending, resulting in YTD negative growth in retail sales. We do not expect a recovery in the next 6-12 months, given the weakening outlook. Sheng Siong remains our top sector pick, as grocery players remain more resilient vs the rest of the retail sector. We also like Delfi, as the pruning of unprofitable value-products should also help to improve earnings in the near term. In the longer term, we think there is potential upside for GENS, as expansion of the integrated resort and the Government's plan to develop the Greater Southern Waterfront area could boost foot traffic.

| Company Name | Rating | TP (SGD) | % Upside (Downside) | P/E (x) Dec-19F | P/BV (x) Dec-19F | Yield (%) Dec-19F |
|---|---|---|---|---|---|---|
| Delfi | BUY | 1.68 | 41.2 | 19.7 | 2.5 | 2.5 |
| Food Empire | BUY | 0.73 | 40.4 | 9.2 | 1.0 | 1.6 |
| Jumbo | BUY | 0.47 | 27.0 | 19.8 | 3.3 | 3.5 |
| Mindchamps | BUY | 0.83 | 56.6 | 16.7 | 2.0 | 2.7 |
| Sheng Siong | BUY | 1.32 | 14.8 | 22.3 | 5.6 | 3.2 |
| BreadTalk | NEUTRAL | 0.71 | 6.0 | 30.5 | 2.7 | 2.2 |
| Genting | NEUTRAL | 0.97 | 10.2 | 15.8 | 1.3 | 4.0 |
| Dairy Farm | NEUTRAL | 7.38* | 8.5 | 25.4 | 5.9 | 3.2 |
| Thai Beverage | TAKE PROFIT | 0.92 | 1.1 | 21.8 | 3.8 | 2.3 |

*Note: * in USD*
*Source: Company data, RHB*

| Top Picks | Target Price |
|---|---|
| Sheng Siong (SSG SP) – BUY | SGD1.32 |
| Delfi (DELFI SP) – BUY | SGD1.68 |

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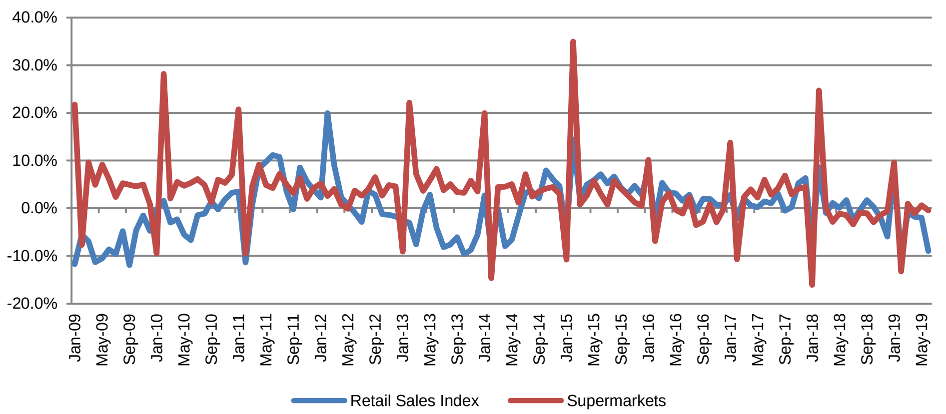
# Slowing Economic Outlook; Spend Wisely

The Government has downgraded GDP growth forecast for 2019 to 0-1%, from 1.5-2.5% previously. Against a slowing economy and potential recession, we advocate gravitating to low-risk consumer staples in the near term, while selectively positioning for longer-term growth. According to Singapore's retail sales index and food and beverage (F&B) sales index's 10-year history, supermarkets, medicine & toiletries and value-F&B formats are most resilient during an economic slowdown.

**Figure 1: Supermarket sales have been more resilient during tough times**

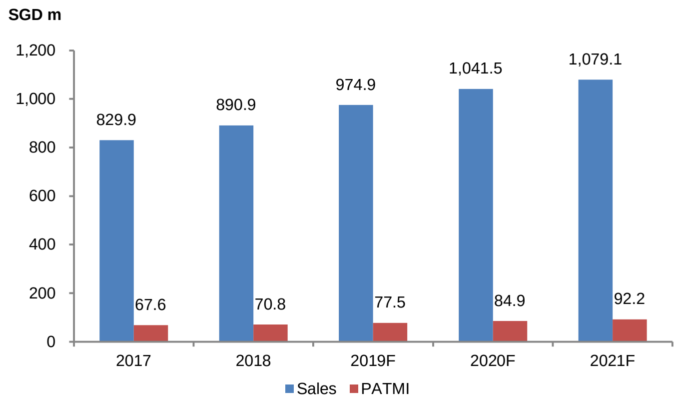



*Source: Singapore Department of Statistics (SingStats)*

## Continue to buy mass market products at Sheng Siong

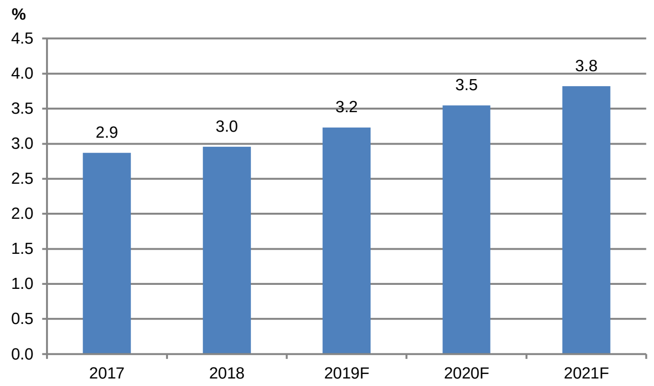
**Sheng Siong (SSG SP, BUY, TP: SGD1.32) is the *de facto* Top Pick in our consumer coverage universe.** Sheng Siong is the third largest supermarket operator in Singapore, with 57 outlets in the country and two in China. Even as Singapore retail sales declined 4.3% YoY in 2Q19, supermarket market retail sales remained resilient, dipping 0.3% YoY. Sheng Siong, on the other hand, managed to grow revenue by 12% through opening new stores. We believe the market will continue to favour Sheng Siong for its defensive nature and FCF-generative business model. We expect PATMI to grow at 9.2% CAGR over FY18-21F. Its FY20F dividend yield of 3.5% is also attractive, when compared to the Singapore 10-Year Government Bond yield of 1.8%.

**Figure 2: Expect continued sales and earnings growth on the back of a store count expansion**




*Source: Company data, RHB*

**Figure 3: Decent dividend yields of 3-4%**




*Source: Company data, RHB*

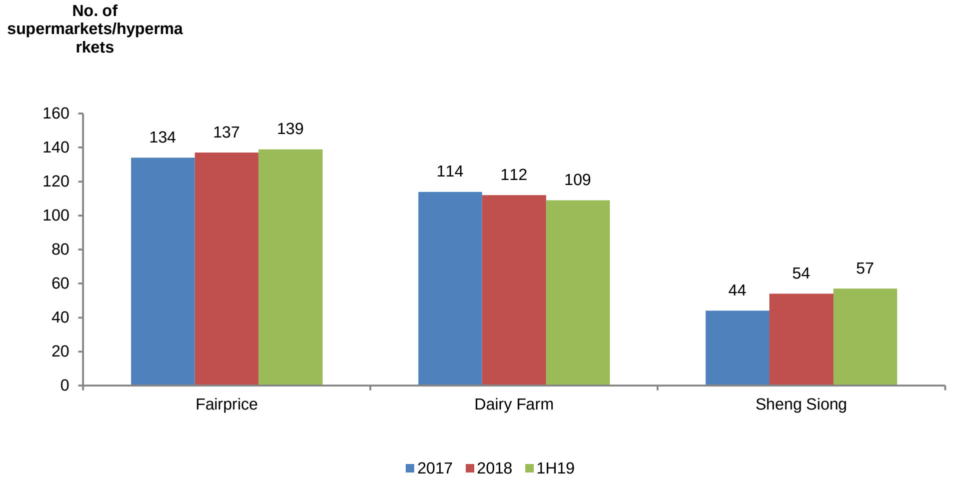
**Sales from new store to offset declining retail sales in the sector.** The group opened 10 stores in 2018 and 3 new stores in 1H19. We expect the group to open another 3-4 stores in 2H19. Historically, each Sheng Siong supermarket took 2-3 years to ramp up to recording mature, stable revenue – with the first twelve months generating only c.50% of its optimal revenue. Therefore, we believe the new stores opened in FY18-19F will continue to drive earnings growth over FY20-21F.

**Mass market branding to help.** In a softening economy, we also expect consumers to tighten their purse strings and reduce discretionary purchases. Sheng Siong, well-known for its mass-market pricing, should see more resilient sales. In addition, while F&B retail sales have done fairly well YTD, we believe it is partly attributed to the opening of new malls such as Changi Airport Jewel and Funan Mall, which brought about new F&B concepts as well as promotions given by food delivery apps. Against the backdrop of a softening economy, we believe expenditure on dining out and food delivery would be reduced in favour of cooking at home and grocery expenditures.

**In the medium term, Sheng Siong is expected to emerge stronger in the grocery retail space.** Across the grocery retail landscape, it has been vigorously bidding for new stores released by the Housing Development Board in the last two years. Despite the slowing economy, we understand that management would like to continue to expand its footprint – especially in new residential areas where it does not have a presence yet.

In contrast, its main competitors – NTUC FairPrice and Dairy Farm have been fairly subdued in new store expansion. According to *Euromonitor*, NTUC FairPrice (inclusive of *FairPrice, FairPrice Finest* and *FairPrice Xtra*) opened three new stores in 2018. YTD, we noticed that NTUC FairPrice has opened a high-end supermarket – *FairPrice Finest* – in Funan Mall and a hypermarket – *FairPrice Xtra* – in Vivocity. Dairy Farm, on the other hand, has been rationalising its store portfolio these two years. We believe Sheng Siong should emerge stronger in the medium term, when the economy recovers. This is as its expansion initiative would allow the group to gain market share and lock in lower rental rates.

**Figure 4: Sheng Siong has been expanding more aggressively than its peers**




*Source: Euromonitor, Company Data, RHB estimates*

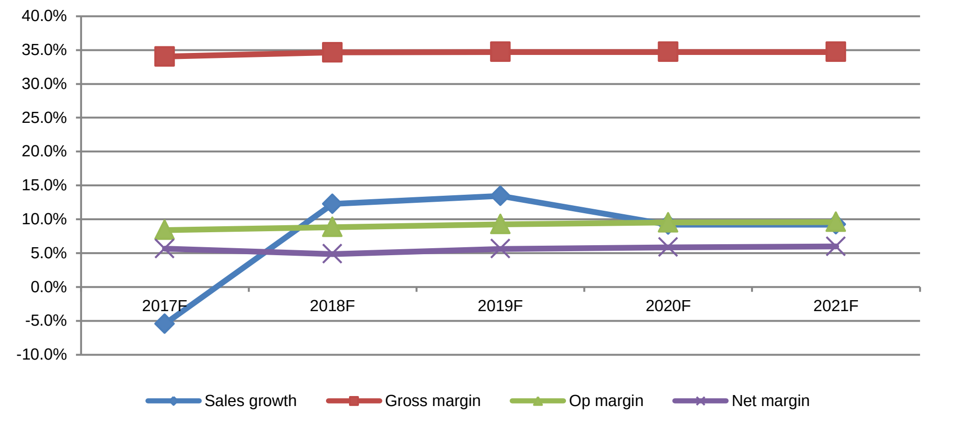
**Key risks** include squeezed margins, if all the new stores are opened in the same period – this should lead to a sudden surge in fixed costs, at a time when revenue from Sheng Siong's new stores have not ramped up yet.

## Delfi – banking on Indonesia's mid- to high-end domestic consumption

**Delfi (DELFI SP, BUY, SGD1.68) is one of the preferred picks of the sector**. Delfi is the largest chocolate confectionery player in Indonesia. It also distributes its own brand and agency brand chocolates in its regional markets including the Philippines, Malaysia and Singapore. Its core brands are *SilverQueen*, *Ceres*, *Selamat* and *Delfi*. Due to portfolio rationalisation two years ago, as well as the culling of unprofitable value-segment products, the group now has greater exposure to mid- to high-end consumers. We believe this would allow it to be more immune to the decline in consumer spending, when the Indonesian Government cuts cash subsidies in 2020F.

**Focusing on premium end.** Delfi has been seeing the positive effects of its stock-keeping units (SKUs) rationalisation initiatives which were done two years ago. By focusing on core brands, it has been able to generate stronger revenue growth and wider gross margins in the past two years (Figure 5). With further pruning of unprofitable value-segment products in 1H19, the group now generates 60% of its revenue from premium products, compared to industry average where c.40% of the sales were from premium products. By targeting the mid- to high-end consumers, we believe the group would be less impacted by slowing GDP growth and the decline in populist measures in 2020.

**Figure 5: Revenue and margins improved since portfolio rationalisation in 2017**




*Source: Company, RHB*

Moving ahead, we do not expect its gross margin to keep expanding as its proportion of sales from premium products were already higher than the industry average. However, we still expect a PATMI CAGR at 15% over FY18-21F, led by improved sales and operating leverage. The stock is currently trading at 19x FY19F P/E, at a substantial discount vs its Indonesia consumer peers, which are trading at an average of 26x FY19F P/E.

**Key risks.** Depreciation of IDR and lower-than-expected domestic consumption as GDP continues to slowdown.

**Figure 6: Comparison with other Indonesia consumer stocks**

| Company | Rating | Mkt cap (IDRtrn) | TP (IDR) | % Upside (Downside) | P/E (x) Dec-19F | Yield (%) Dec-19F |
|---|---|---|---|---|---|---|
| ICBP | Buy | 138.8 | 12,300 | 3.4 | 28.2 | 1.7 |
| MAPI | Buy | 17.3 | 1,300 | 24.4 | 19.4 | 1.0 |
| AMRT | Buy | 36.5 | 1,200 | 36.3 | 31.2 | 1.3 |
| MYOR | Buy | 53.9 | 3,300 | 36.9 | 24.9 | 1.1 |
| LPPF | Buy | 9.2 | 5,000 | 58.2 | 5.4 | 10.5 |

*Source: Bloomberg, RHB*

## Probably have to eat at food court

**Koufu (Koufu SP, NR) is the other domestic consumer staple name that we like**. Koufu is the largest food court operator in Singapore. It has 47 food courts, 16 coffee shops and one hawker centre in the country and two food courts in Macau, in which, it owns and operates 77 F&B stalls. It also operates seven quick-service restaurants (QSR), two full-service restaurants and 20 bubble tea stalls. Food court is one of the staple F&B formats that would likely be resilient in times of an economic slowdown. The group has committed to a dividend payout ratio of at least 50% for FY19F.

**New food courts to sustain growth in near term.** YTD, the group opened one new food court, one coffee shop, three F&B stalls and four new bubble tea shops. It has secured three more food court leases in Singapore and is in the midst of finalising another lease in Macau. The group is likely to expand its F&B stalls by 1-2, in tandem with the opening of each food court.

**Improving productivity to sustain margins.** Over the years, Koufu has improved productivity through the use of roaming tray-return robots and adoption payment systems that accept both cash and cashless options. As the construction of the group's integrated facility should be completed sometime next year, it may increase preparation of food done in the central kitchen and switch to centralised dishwashing, to reduce its reliance on manpower. Management also plans to rent out unutilised space in its integrated facility to stall tenants, as having a mini-central kitchen would help them improve labour productivity. The rental income from the integrated facility is expected to cover the additional depreciation expense.

**Key risks.** While management cited there has been strong interest for the tenancies of the mini-central kitchen, none of them have been committed – since the construction of the integrated facility has yet to be completed. Inability to rent out unutilised space could lead to a 4% erosion in earnings as a result of the additional depreciation costs.

We currently do not have a recommendation for Koufu.

## Looking at the longer term – beyond the recession

**NEUTRAL on GENS (GENS SP, NEUTRAL, TP: SGD0.97) for now…** We are NEUTRAL on GENS, given the current risk-off mode. Although 2Q19 delivered a strong set of results, we are cautious on the near-term outlook of the VIP segment against the slowing economy. Following the 50% increase in casino levy for Singaporeans and permanent residents, mass gaming is also likely to take a longer time to recover under the current economic circumstances.

**… but brighter spots if you look at the longer term.** We believe GENS would benefit from increased accessibility and higher footfall following its Resort World Sentosa 2.0 (RWS 2.0) mega expansion plan, coupled with the Government's plan to develop the Greater Southern Waterfront, rejuvenate Sentosa and redevelop Pulau Brani.

**RWS 2.0.** The group is expected to spend a total of SGD4.5bn in capex to expand its gross floor area by 50% and add new attractions to its site. Aside from adding 500sqm of gaming space and 800 machines for its casino, GENS would be adding new sections to its Universal Studios theme park and enlarging its S.E.A. Aquarium into Singapore Oceanarium. It would also build two new hotels with 1,100 new rooms and increase meetings, incentives, conferences and exhibition (MICE) space by 11,000sqm. The expansion would be delivered in phases with the first new attraction *Adventure Dining Playhouse* expected to be completed by end-2020. Finally by 2026, the group expects to introduce a new driverless transport system to provide improved accessibility between the Singapore's mainland and Sentosa Island.

**Figure 7: Artist's impression of the new Minion Park Ride at Universal Studios Singapore**

*Source: Resort World Sentosa*

**Figure 8: Artist's impression of a new Oceanarium Singapore**

*Source: Resort World Sentosa*

**Development of Greater Southern Waterfront.** During the 2019 National Day Rally, Prime Minister Lee Hsien Loong announced the development of Greater Southern Waterfront. The Greater Southern Waterfront comprises 30km of coastline stretching from the Gardens by the Bay East area to Pasir Panjang. It contains 2,000ha of land – six times the size of Marina Bay. The area would be transformed into a new major gateway and location for urban living along Singapore's southern coast. About 9000 housing units will be built on the site.

Development will take place in phases, starting with the former Pasir Panjang Power District, Keppel Club and Mount Faber in the next 5-10 years, with the full project expected to be completed beyond 2040.

**Figure 9: Greater Southern Waterfront**


*Source: Channel News Asia*

**Positive for GENS in the longer term.** We believe the new developments from GENS and Greater Southern Waterfront would help revitalise RWS. As the projects are delivered in phases, we think it would create a constant flow of novelties and excitements to RWS, thereby generating reasons for recurring visits.

Greater Southern Waterfront would also be an extension to the central business district area in the future – similar to what Marina Bay Sands is to the CBD area currently. The expansion of office and residential space in the Greater Southern Waterfront would bring younger and more vibrant demographics closer to RWS. Consequently, we think GENS would be able to compete more competitively in terms of its location.

Outside of Singapore, winning of the Japan integrated resort bid would be a key catalyst to its share price. Management believes the earliest Osaka could select an operator is in 2Q20.

## RHB Guide to Investment Ratings

| | |
|---|---|
| **Buy:** | Share price may exceed 10% over the next 12 months |
| **Trading Buy:** | Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain |
| **Neutral:** | Share price may fall within the range of +/- 10% over the next 12 months |
| **Take Profit:** | Target price has been attained. Look to accumulate at lower levels |
| **Sell:** | Share price may fall by more than 10% over the next 12 months |
| **Not Rated:** | Stock is not within regular research coverage |

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