

20 December 2023

Consumer Non-cyclical | Retail - Staples

SDS Group (SDS MK)

Not Rated

Baking In Sustainable Growth

- **FV of MYR1.01 is based on 13x FY25F (Mar) P/E, which is on par with the sector average.** SDS Group's solid 13% 3-year earnings CAGR should be underpinned by the robust expansion in both its operating divisions to capture the rising demand for bakery products. It is trading at an undemanding valuation, despite a solid track record in delivering earnings growth and solid fundamentals (sturdy balance sheet, experienced management team), as well as it benefiting from the resilient consumption of bakery products as a staple food.
- **Twin engines to capture demand for bakery products.** SDS began as a bakery back in 1987, and has grown into a household name in Johor after decades of expansion. Essentially, we believe there is steady consumption growth in the bakery industry – driven by the rising demand for quality and conveniently-packaged bakery products on the back of increasingly busy lifestyles, urbanisation, and growing affluence. Strategically, SDS runs two business units – wholesale and retail – to capture this growing demand. We also believe the synergistic benefits will strengthen the competitiveness of the group.
- **Wholesale: Ramping up capacity to deepen market penetration.** SDS has been expanding its delivery fleet and distribution centre network to increase drop points and extend its reach to more consumers. Playing a second-liner role to the larger industry players is a blessing in disguise, as it allows SDS to venture deeper into more rural locations where the latter are not prioritising. In addition, SDS has seen positive results in launching new products to entice consumers and raise its brand equity. Meanwhile, price increases to maintain the price gaps vs major competitors should help preserve margins, while being further aided by stabilising input costs.
- **Retail: Continues to offer a value-for-money proposition.** We believe management is taking a prudent and selective approach on expansion by targeting 3-5 new stores being opened each year. The company continues to see opportunities in Johor (33 outlets) to leverage on its entrenched brand equity, whilst the strong spending power of visitors from Singapore is also a key driver. That said, its proven business model in offering quality bakery and café food at reasonable prices is mature enough to be replicated in the major Kuala Lumpur and Selangor markets (4 outlets) to extend its retail footprint. We also like the hybrid format in placing the bakery and café under one roof (17 outlets) for cross-selling opportunities and offering more convenience to consumers.
- **Downside risks to our outlook for the company** include intensifying competition and a sharp rise in production costs.

Fair Value (Return): MYR1.01 (+40%)
Price: MYR0.72
Market Cap: USD62.4m
Avg Daily Turnover (MYR/USD) 0.53m/0.11m

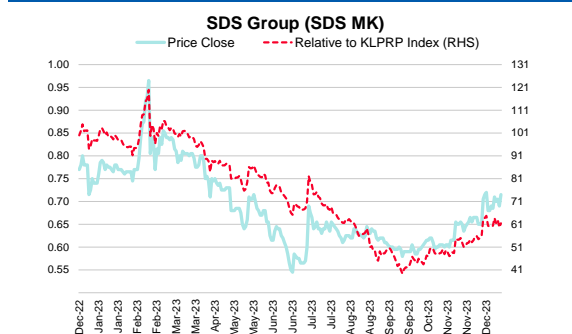
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(3.4)	10.9	20.2	26.5	(7.2)
Relative	(37.0)	11.5	21.0	1.5	(38.7)
52-wk Price low/high (MYR)				0.55 – 0.97	



Source: Bloomberg

Forecasts and Valuation	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
Total turnover (MYRm)	198	284	315	340	365
Recurring net profit (MYRm)	11	25	29	32	35
Recurring net profit growth (%)	46.0	131.0	18.4	10.7	9.6
Recurring P/E (x)	27.58	11.94	10.09	9.11	8.31
P/B (x)	3.6	2.8	2.4	2.0	1.7
P/CF (x)	9.38	6.35	6.27	5.96	5.62
Dividend Yield (%)	0.3	0.7	3.0	3.3	3.6
EV/EBITDA (x)	9.71	5.59	4.56	3.80	3.13
Return on average equity (%)	13.8	26.5	25.6	23.8	22.2
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Financial Exhibits

Asia	Financial summary (MYR)	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
Malaysia	Recurring EPS	0.03	0.06	0.07	0.08	0.09
Consumer Non-cyclical	DPS	0.00	0.00	0.02	0.02	0.03
SDS Group	BVPS	0.20	0.25	0.30	0.36	0.42
SDS MK	Return on average equity (%)	13.8	26.5	25.6	23.8	22.2
Not Rated						
	Valuation metrics	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
Valuation basis	Recurring P/E (x)	27.58	11.94	10.09	9.11	8.31
P/E	P/B (x)	3.6	2.8	2.4	2.0	1.7
	FCF Yield (%)	7.7	10.6	9.1	11.7	12.7
Key drivers	Dividend Yield (%)	0.3	0.7	3.0	3.3	3.6
i. Market penetration;	EV/EBITDA (x)	9.71	5.59	4.56	3.80	3.13
ii. Successful new product launches;	EV/EBIT (x)	19.04	8.15	6.41	5.27	4.25
iii. Favourable input costs						
	Income statement (MYRm)	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
Key risks	Total turnover	198	284	315	340	365
i. Intense competition;	Gross profit	62	89	101	110	119
ii. Sharp rise in input costs;	EBITDA	30	49	55	60	64
iii. Weak consumer sentiment.	Depreciation and amortisation	(15)	(15)	(16)	(17)	(17)
	Operating profit	15	33	39	43	47
Company Profile	Net interest	(1)	(1)	(0)	0	1
SDS Group is involved in manufacturing and retailing bakery products. Wholesales brands under its manufacturing division are Top Baker and Daily's whereas retail outlets are operated under three different concepts – bakery, cafeteria, and bakery-cum-cafeteria.	Pre-tax profit	14	33	39	43	47
	Taxation	(4)	(8)	(10)	(11)	(12)
	Reported net profit	11	25	29	32	35
	Recurring net profit	11	25	29	32	35
	Cash flow (MYRm)	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
	Change in working capital	6.2	3.4	2.3	1.5	1.5
	Cash flow from operations	31.2	46.2	46.7	49.2	52.1
	Capex	(8.8)	(15.1)	(20.0)	(15.0)	(15.0)
	Cash flow from investing activities	(9.2)	(19.2)	(20.0)	(15.0)	(15.0)
	Dividends paid	(1.0)	(4.1)	(8.7)	(9.6)	(10.6)
	Cash flow from financing activities	(19.1)	(19.6)	(9.0)	(9.5)	(10.0)
	Cash at beginning of period	17.2	20.1	27.5	45.2	69.8
	Net change in cash	2.9	7.4	17.7	24.7	27.1
	Ending balance cash	20.1	27.5	45.2	69.8	96.9
	Balance sheet (MYRm)	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
	Total cash and equivalents	30	39	57	83	111
	Tangible fixed assets	100	107	111	109	107
	Total assets	143	162	185	210	236
	Short-term debt	8	5	5	5	5
	Total long-term debt	21	11	11	11	11
	Total liabilities	61	58	60	63	65
	Total equity	82	104	124	147	172
	Total liabilities & equity	143	162	185	210	236
	Key metrics	Mar-22	Mar-23	Mar-24F	Mar-25F	Mar-26F
	Revenue growth (%)	14.1	43.1	11.0	7.9	7.4
	Recurrent EPS growth (%)	46.0	131.0	18.4	10.7	9.6
	Gross margin (%)	31.1	31.5	32.0	32.3	32.5
	Operating EBITDA margin (%)	15.2	17.1	17.6	17.6	17.4
	Net profit margin (%)	5.4	8.6	9.2	9.5	9.7
	Dividend payout ratio (%)	9.6	8.3	30.0	30.0	30.0
	Capex/sales (%)	4.4	5.3	6.3	4.4	4.1
	Interest cover (x)	10.5	37.6	53.2	58.2	71.0

Source: Company data, RHB

Valuation & Forecasts

We peg a 13x P/E to SDS' FY25F EPS to derive our FV of MYR1.01. This is after taking into account the mid-teen and low-teen average forward P/Es commanded by small-cap consumer staples and consumer discretionary counters respectively. Notwithstanding the relatively smaller market capitalisation, we believe the valuation for SDS is warranted – given its solid earnings growth over the years as well as its superior ROE. In addition, we believe SDS' earnings are less cyclical, as consumption in the bakery industry should be driven by favourable changes in consumer preferences, urbanisation and rising disposable income. SDS' strong presence in Johor also renders it a good proxy to benefit from the exciting developments in the state and capture the strong spending power of visitors from Singapore.

Figure 1: Peer comparison

Company	Country	FYE	Mkt Cap (USDm)	Price	P/E (x)			Div. Yld (%)	ROE (%)	EV/ EBITDA	NP Growth (%)	
				18-Dec-23								
				(Local Currency)	Actual	1 Yr Fwd	2 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd
Consumer Staple												
Farm Fresh	MA	Mar	530.3	1.33	47.1	37.4	23.0	0.7	10.4	22.5	25.9	62.2
Power Root	MA	Mar	179.2	1.82	13.6	16.7	14.8	4.8	17.4	10.6	-18.6	12.5
Hup Seng Industries	MA	Dec	133.8	0.79	22.5	14.9	13.7	5.1	29.8	8.9	51.4	8.7
Apollo Food	MA	Apr	92.0	5.40	13.0	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Oriental Food	MA	Mar	85.9	1.68	20.0	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Mkt. Cap Weighted Avg.			339.9		32.6	29.4	19.8	2.3	15.0	17.8	20.5	43.1
Simple Avg.			204.2		23.2	23.0	17.2	3.6	19.2	14.0	19.6	27.8
Consumer discretionary												
Mr DIY Group	MA	Dec	2896.1	1.44	26.9	24.1	20.8	2.1	39.1	13.3	11.6	15.7
Padini	MA	Jun	473.6	3.38	9.5	12.6	11.3	3.3	16.8	5.6	-24.4	11.4
Aeon Co (M)	MA	Dec	343.9	1.15	13.6	14.0	12.7	3.5	6.4	5.1	-2.7	9.8
Senheng New Retail	MA	Dec	105.4	0.33	7.7	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Focus Point	MA	Dec	72.8	0.74	8.9	10.7	9.5	4.5	31.2	4.7	-16.6	12.4
Mynews	MA	Oct	82.3	0.52	-18.2	-28.9	48.4	0.6	-6.0	8.8	-37.0	-159.7
Bonia	MA	Jun	73.8	1.73	6.0	8.3	7.7	4.0	9.1	3.8	-27.7	7.8
Mkt. Cap Weighted Avg.			2058.9		21.0	19.8	18.7	2.4	31.1	10.9	2.2	11.2
Simple Avg.			535.0		8.1	7.7	17.4	3.1	16.2	6.8	-17.2	-12.1
SDS	MA	Mar	60.2	0.70	11.5	9.7	8.8	3.1	25.6	4.5	18.4	10.7

Source: Bloomberg, RHB

We project a 3-year earnings CAGR of 13% (FY23-26F). In view of the conducive environment of consumption, we expect both operating divisions to continue churning healthy growth, underpinned by their own expansion plans. The wholesale division will penetrate more markets and increase the touch points – supported by capacity expansion, innovative product launches and rising brand equity. Meanwhile, the segmental margins should be supported by price adjustments, stabilising input costs and volume growth. Meanwhile, for the retail wing, outlet openings to replicate the proven existing model in offering value-for-money and quality products to consumers will bode well for SDS, whilst we like the hybrid model which facilitates cross-selling opportunities and offers more convenience to consumers.

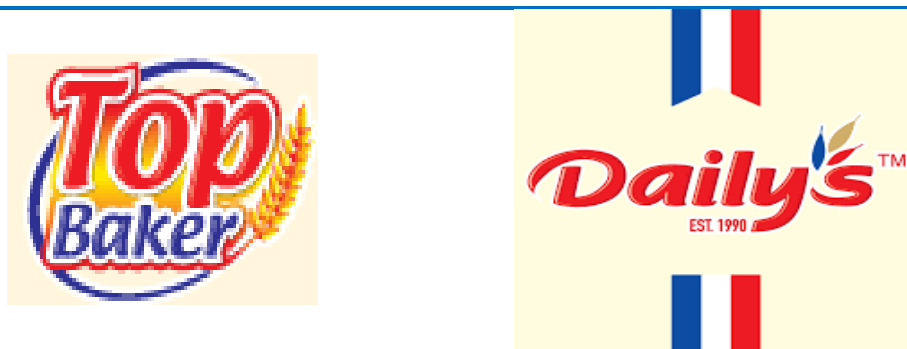
Company Overview

SDS is principally involved in manufacturing and distributing bakery products as well as operating F&B outlets. Established in Johor in 1987, SDS is led by Managing Director Tan Kim Seng and Executive Director Tan Kim Chai, who are industry veterans in the bakery industry with >30 years of experience. Its products are sold via both wholesale and retail channels.

Wholesale segment (c.two-thirds of FY21-23 revenue)

Bakery products manufactured by SDS for the wholesale channel are catered towards the mass market across West Malaysia as well as Singapore. The products are marketed under its trademarked brands, Top Baker and Daily's. Currently, SDS has two main manufacturing production plants in Kempas, Johor and Seremban, Negeri Sembilan.

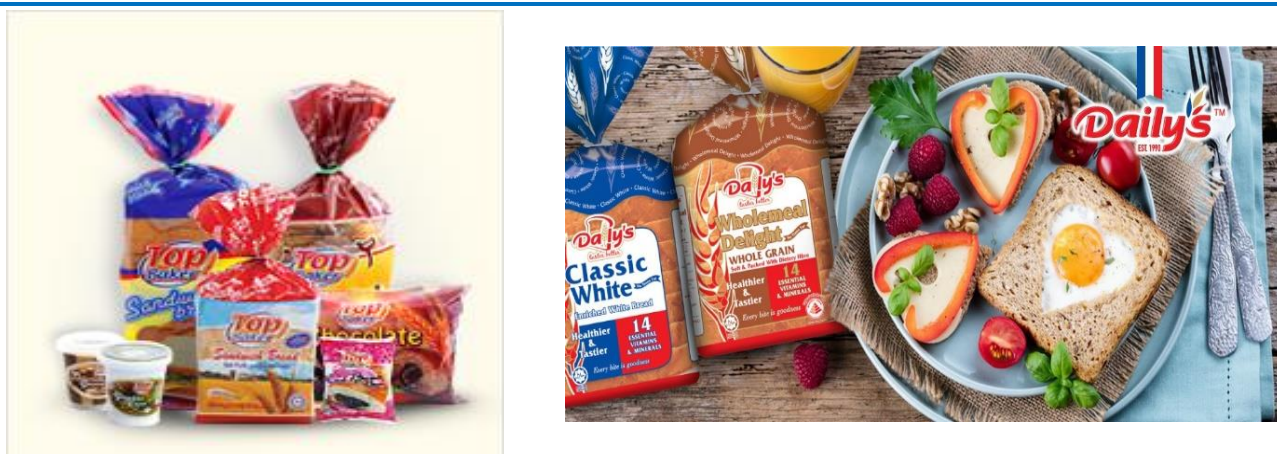
Figure 2: Wholesale brands under SDS



Source: Company

The Daily's brand products are typically sold at channels that require listing fees such as hypermarkets, supermarkets, and convenience stores. Meanwhile, Top Baker are more commonly sold at smaller grocery and sundry shops as well as factories, schools, and coffee shops – where there are no listing fees.

Figure 3: Wholesale products



Source: Company data

Retail segment (c.one-third of FY21-23 revenue)

SDS operates F&B outlets under three different formats – bakery, café and bakery-cum-café. As of 31 Sept, SDS had 38 outlets (33 in Johor, four in KL/Selangor and one in Negeri Sembilan).

Figure 4: Retail brands under SDS

Source: Company data

Figure 5: Retail outlets

Source: Company data

Figure 6: Retail outlets

Source: Company data

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-03-09	Not Rated	na	0.26

Source: RHB, Bloomberg

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Analyst	Company
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