24 May 2022

Consumer Cyclical | Retailing

Retailing

Overweight (Maintained)

Cautious Optimism Towards a Recovery Path; O/W

Stocks Covered	6
Rating (Buy/Neutral/Sell):	5 / 1 / 0
Last 12m Earnings Revision Trend:	Negative

- **Maintain OVERWEIGHT, with Ace Hardware (ACES) as the Top Pick.** Mall traffic was strong during the *Lebaran* festivities – substantially higher than the previous two years. This should bode well for all retailers. However, it has yet to recover to pre-pandemic levels. As such, we remain concerned on retailers' performance, given the various challenges post *Lebaran*. ACES remains our Top Pick, given its strong recovery story and resilient margin profile in 2022.
- **Traffic in shopping malls is still 80-90% lower than pre-pandemic levels,** with a full recovery more likely in 2023. Channel checks at several retailers – shopping malls and standalone stores – in Jakarta a week before and after *Lebaran* found that retailers across all types of businesses, formats, locations and customer segments gained strong traction. Before *Lebaran*, fashion and household products attracted buyers, whilst F&B and entertainment (ie cinema, kids' playground) performed well post *Lebaran*. Interestingly, despite mid-to high-end department stores managing to attract traffic, there was a substantially higher volume of buyers in stores catered to the mid- to low-income segment, such as in Ramayana Lestari (RALS) and Matahari Department Store (LPPF). Nonetheless, we think this concept remains challenging given changing customer behaviour, especially in Tier-1 cities, which may limit Matahari Putra Prima's (MAPI) performance going forward.
- **Despite online commerce flourishing, offline stores should regain relevance as economic reopening continues.** Increasing offline contribution should be more positive for F&B players as dine-in revenue commands higher margins. Our discussions with retailers indicate that online contribution has started to normalise. Some structural issues still need to be resolved by online players to bring more meaningful contribution. As such, we expect shopping malls to still remain relevant, albeit, continuously providing an interesting customer experience to stay competitive. We also learnt that new shopping malls will commence operations in 2024. Possible challenges for key retailers that prefer to open in a standalone format lie in attracting tenants. This might provide opportunity for retailers with a strong presence and sizable space occupied ie MAPI to have more bargaining power to lower rental rates.
- **Numerous challenges await retailers in 2H22** amidst seasonality and a high inflationary environment, likely yielding softer consumer purchasing power. Overall, we think, the impact will be far reaching, particularly for the mid-to-low segment, while the reopening of international borders and number of limitations on imported high-end products may also curb mid- to high-end retailers' performance. Margin might be pressured as rental rates start to normalise. As such, we remain cautiously optimistic on this sector as more supportive government regulations and assistance could help to contain the impact. Retailers also plan to conduct massive promotions to entice shopping activities. Low COVID-19 cases and tailwinds from high commodity prices may also partly alleviate the pressure, especially in ex-Java.
- **ACES is our Top Pick,** owing to its sturdy earnings recovery from the increase in mobility, higher shopping appetite for home improvement products, and solid 2021 property marketing sales. Margin should also be solid in light of its resilient premium client focus, more prudent purchasing decisions, distinctive product offering, long inventory days, and enhanced operational efficiency from the absence of lockdowns in 2022.

Company Name	Rating	Target (IDR)	% Upside (Downside)	P/E (x) Dec-22F	P/B (x) Dec-22F	ROAE (%) Dec-22F	Yield (%) Dec-22F
ACE Hardware	Buy	1,490	49.7	26.3	2.8	13.4	1.4
Erajaya Swasembada	Buy	1,100	117.8	6.1	1.1	20.9	3.4
Matahari Department Store	Buy	6,600	16.8	13.2	8.9	79.4	4.7
Matahari Putra Prima	Buy	1,200	338.0	na	3.1	(6.4)	-
Mitra Adiperkasa	Buy	1,000	12.4	17.4	3.1	13.9	0.1
Ramayana Lestari	Neutral	750	11.1	16.7	1.0	6.2	-

Source: Company data, RHB

Top Picks

Top Picks	Target Price
Ace Hardware (ACES IJ)	IDR1,490

Analyst

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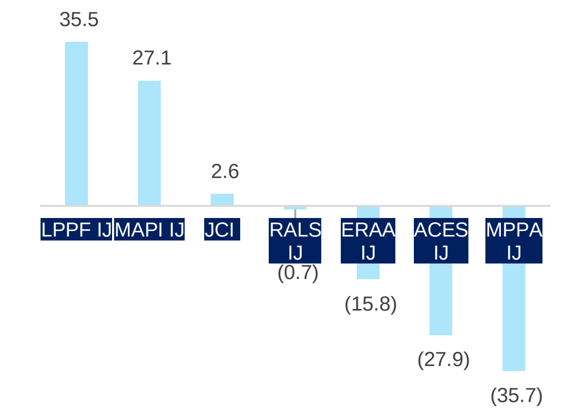
YTD share price performance (in percentage)



Source: Company data, RHB

Ground Checks

We conducted ground checks at a number of retailers (shopping malls and standalone stores) in Jakarta a week before and after the Lebaran festivities. Similar to Indonesia Shopping Centre Association's and other retailers' view, traffic has been strong. We think there were several catalysts to trigger shopping appetite. The Government had announced an additional four days of public holidays for *Lebaran*, bringing the total days off for this festive holiday to 10. This is higher than the previous years' 2-5 days, given stricter health protocols to control COVID-19 numbers then. This triggered the massive hometown exodus (*mudik*) and travel, which we believe induced greater shopping activities. Retailers ought to enjoy stronger benefit following the previous two years of interrupted *Lebaran* festivities. We think the five weekends and one long weekend during the fasting period also boosted shopping appetite.

This was supported by sturdy purchasing power given ample of cash distribution to the country's grassroots and high commodity price tailwinds. We saw three paydays during the fasting period. With no more restrictions to travel after the Government allowed the *mudik* provides better cash savings for consumers in our view. Purchasing power of the mid-to-low segment should also be partly helped by the distribution of two additional rounds of cash assistance, in our view, ie a cooking oil cash subsidy and cash aid for those earning below IDR3.5m. Using a back-of-envelope calculation, we estimate these the two rounds of assistance make up c.40% of the average national minimum wage.

From our observation, families formed the largest segment of visitors while F&B outlets were the most popular. Traffic in shopping malls reached its peak a week before *Lebaran* as people made purchases to bring back to their respective hometowns. We also learnt children's playgrounds and cinemas became a crowd puller, especially on public holidays post *Lebaran*. Grocery business gained traction across all segments whilst home improvement stores such as ACES and IKEA managed to attract visitors too. Interestingly, department stores, even the mid-to-high segment, showed strong traffic. Nonetheless, we think department stores targeting the mid-to-low segment such as RALS and LPPF had much stronger traffic.

Numerous challenges await retailers in 2H22 amidst seasonality and a high inflationary environment, likely yielding softer consumer purchasing power. Overall, we think, the impact will be far reaching, particularly for the mid-to-low segment, while the reopening of international borders and number of limitations on imported high-end products may also curb mid- to high-end retailers' performance. Margin might be pressured as rental rates start to normalise. As such, we remain cautiously optimistic on this sector as more supportive government regulations and assistance could help to contain the impact. Retailers also plan to conduct massive promotions to entice shopping activities. Low COVID-19 cases and tailwinds from high commodity prices may also partly alleviate pressure, especially in ex-Java.

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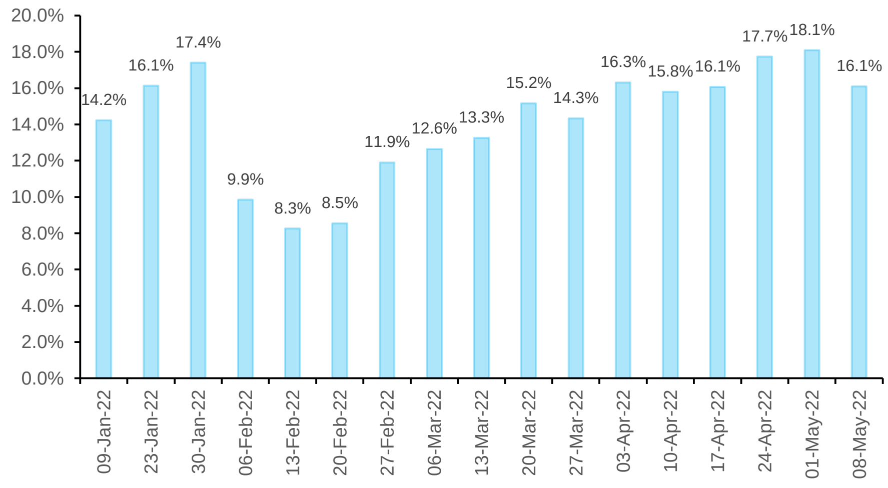
Figure 1: Jakarta's key shopping malls have seen traffic, as a percentage of capacity, get stronger



Source: Peduli Lindungi Apps, RHB

- Traffic in key shopping malls in Jakarta continued to increase – traffic one week/day before *Lebaran* saw a rising trend since Jan 2022, save for Feb 2022 due to the increased number of COVID-19 cases from the Omicron variant.

Figure 2: Regional peer comparison

Company	Bloomberg code	Market cap (IDRbn)	2022F EPS growth (%)	2022F P/E (x)	2022F EV/EBITDA (x)	2022F P/BV (x)	2022F ROE (%)	2022F Div yield (%)
Mitra Adiperkasa	MAPI IJ	14,774	196.0	23.7	7.6	3.1	13.9	0.1
Erajaya Swasembada	ERAA IJ	8,055	34.0	5.5	3.9	1.1	20.9	3.4
Ace Hardware Indonesia	ACES IJ	17,064	10.0	22.1	13.2	2.8	13.4	1.4
Ramayana Lestari Sentosa	RALS IJ	4,790	122.0	17.8	4.5	1.0	6.2	-
Matahari Department Store	LPPF IJ	14,838	175.4	8.3	1.5	8.9	79.4	4.7
Matahari Putra Prima	MPPA IJ	2,323	85.3	-	7.1	3.1	(6.4)	-
Simple Average			**103.8**	**12.9**	**6.3**	**3.3**	**21.2**	**1.6**
Weighted Average			**108.7**	**15.8**	**7.0**	**4.0**	**29.0**	**2.0**

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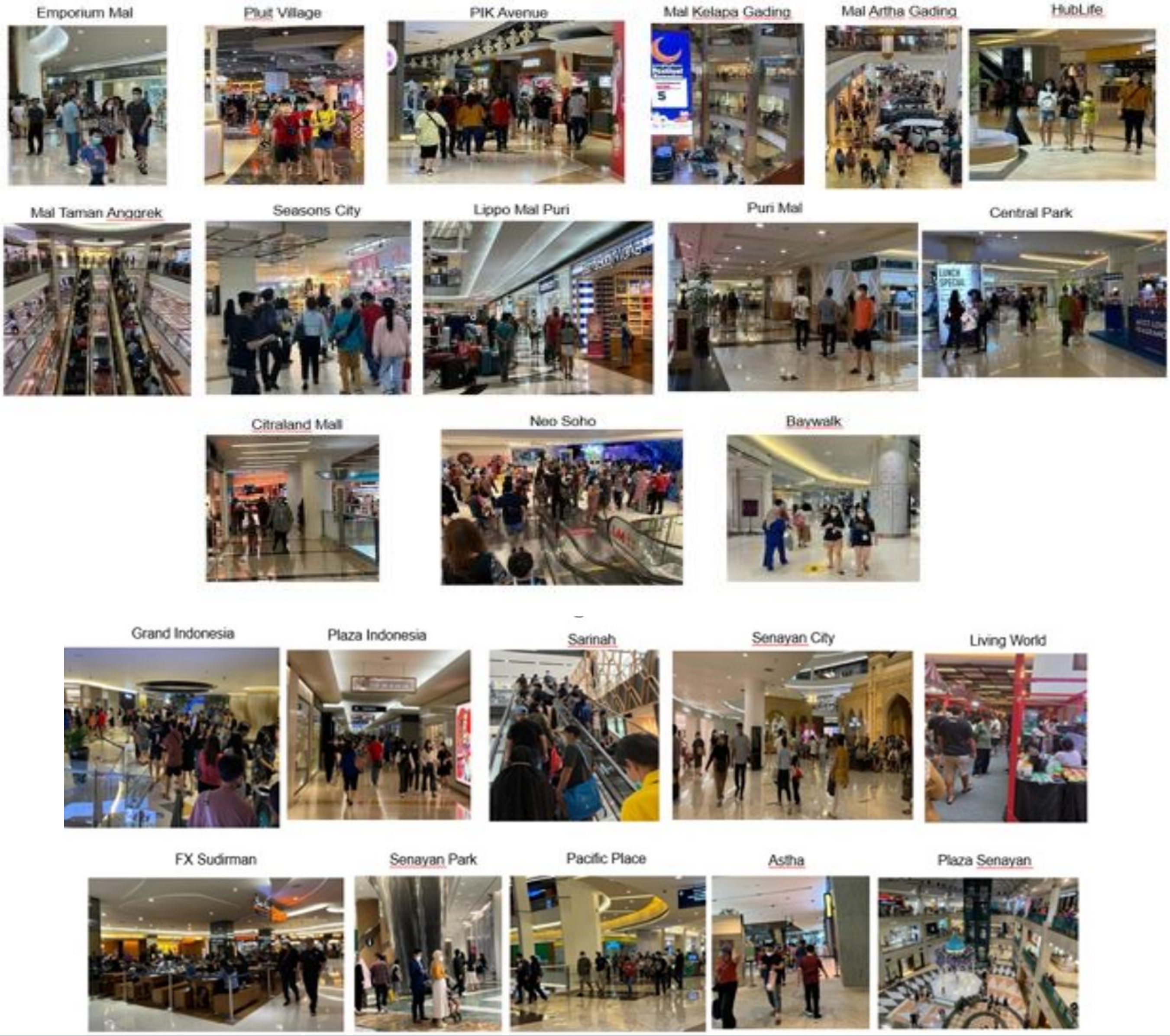
Golden Eagle Retail Group	3308 HK	1,165.5	(16.7)	5.8	2.9	0.9	6.1	8.3
AEON Co (M)	AEON MK	473.9	28.1	19.0	5.7	1.2	21.2	2.6
Falabella	FALAB CI	6,776.4	(17.1)	10.3	6.3	1.1	9.7	2.3
SM Investments	SM PM	19,550.0	19.7	34.6	16.6	2.9	8.8	0.7
Rainbow Digital Commercial	002419 CH	1,604.0	44.2	21.3	14.8	2.2	10.4	1.3
Ripley Corp	RIPLEY CI	309.4	(60.6)	9.3	13.2	0.3	3.7	0.0
Hyundai Department Store	069960 KS	1,435.2	26.2	7.5	5.8	0.4	5.3	1.4
Simple Average			**3.4**	**15.4**	**9.3**	**1.3**	**9.3**	**2.4**
Weighted Average			**11.3**	**25.9**	**13.1**	**2.2**	**9.0**	**1.4**

Source: Company data, Bloomberg, RHB

Figure 3: Heavy mall traffic before and after *Lebaran*. We noticed that it mainly comprised families and focused on F&B



Source: RHB

Figure 4: F&B continued to attract substantial traffic, especially during the *Lebaran* holiday

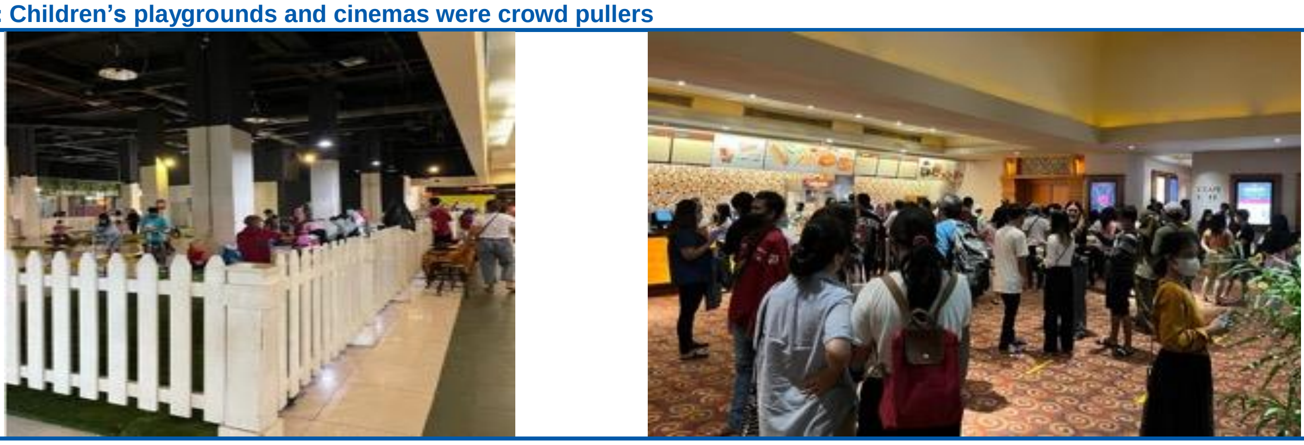
Source: RHB

Figure 5: Groceries business gained traction across all segments

Figure 6: Home improvement stores such as ACES and IKEA also attracted visitors

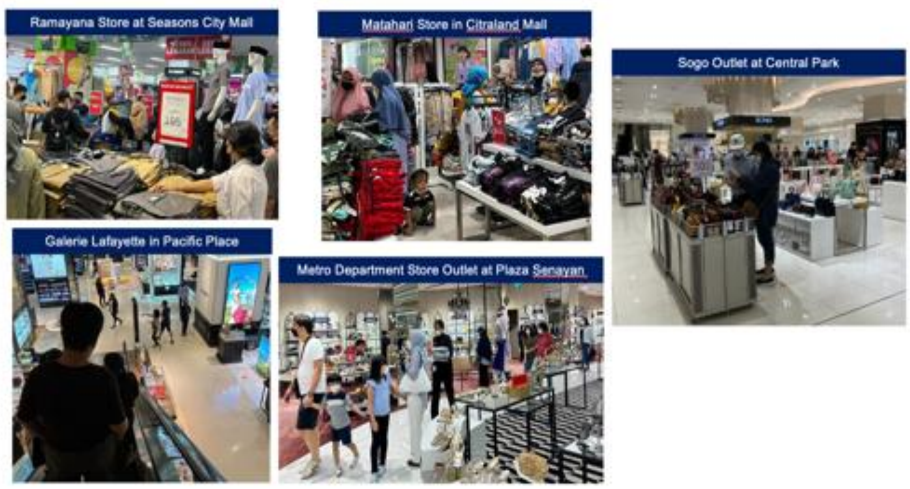
Source: RHB

Figure 7: Children's playgrounds and cinemas were crowd pullers



Source: RHB

Figure 8: Department stores showed strong recovery, particularly mid-to-low segment



Source: RHB

- Interestingly, department stores – even for mid to high segment – showed strong traffic
- Nonetheless, we deem department stores targeting the mid-to-low segment such as RALS and LPPF having much stronger traffic

Retail Associations' Key Takeaways

Indonesian Shopping Centre Association (ISCA)

Retail traffic was heavy during the uninterrupted fasting period and *Lebaran* celebrations. Low COVID-19 cases translated to eased social restrictions, triggering hometown exodus and shopping appetite. Alphonsus Widjaja, ISCA chairman expects 2022 traffic to hit 80% of pre-pandemic levels (2019), higher than 2020's 50% and 2021's 60%. Occupancy is also estimated to improve to 80% (2020: 70%; 2021: 70%; 2019: 90%). Rental rate discounts are trending down. The association expects no discounts to be provided in 2H22 (1H22: c.25%, 2021: 50%). There is a likelihood of an increase in COVID-19 cases but the impact should be substantially less severe due to the high vaccination rate and better health awareness.

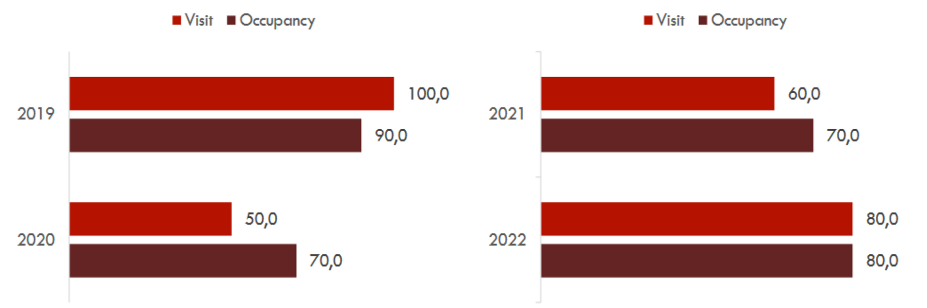
Shopping malls expansion resumed given stronger economic recovery. Shopping malls under construction include Bintaro XC Phase 2, Pakuwon Mall Bekasi, Living World Kota Wisata, Living World Grand Wisata, and AEON Mall Deltamas. These malls are expected to open by 2024. Despite the threat from online commerce, ISCA remains optimistic on shopping mall development – it sees consumer interest as still high since malls also function as a social connection hub. According to the association, business prospects of malls continue to be promising as shopping malls are also public facilities needed to meet basic needs and wants. Another factor is that retailers, too, form one of the public consumption sectors that dominates Indonesia's economy. However, ISCA acknowledges the challenges are higher for shopping malls and offline retailers to remain relevant in the current environment. We believe shopping malls need to not only become a place to make purchases but also provide a shopping experience for customers. Digitalisation, to an extent, can be applied to mall operations to improve the service.

Providing suitable tenant mix that in line with targeted customers is also pertinent. We note that F&B and entertainment sectors performed well during the *Lebaran* period, while the clothing and household segments gained traction during *Ramadan*. Despite the strong performance during both periods, department stores, especially in Tier-1 cities, and hypermarkets, are expected to remain under pressure going forward. Home improvement stores such as ACES are still in the black. However, players like IKEA acknowledge the importance of having a presence in shopping malls – it recently opened a store in Mal Taman Anggrek, Jakarta. Meanwhile, the electronic products sector witnessed a consolidated industry landscape with a number of players having to close down their operations such as Best Denki and Electronic Solution. This prompted Electronic City Indonesia (ECII IJ, NR) to conduct an aggressive expansion drive in order to fend off new competitors such as JD ID.

However, a number of challenges seen post *Lebaran* may slow down sales. The mid-to-low income segment may start to feel the pinch due to the rising cost environment (ie energy cost) and VAT implementation. Meanwhile, retailers in the mid- to high-end segment will likely see challenges from premium products' taxes and quotas, as well the reopening of international borders. That said, government support may play a more critical role at this juncture which should include the continuation of social assistance, better tax regulation (ie fair tax treatment between online vs offline), among others. We think this could help to boost purchasing power – which has yet to normalise. Aside from that, a better regulated COVID-19 law may help to improve the situation.

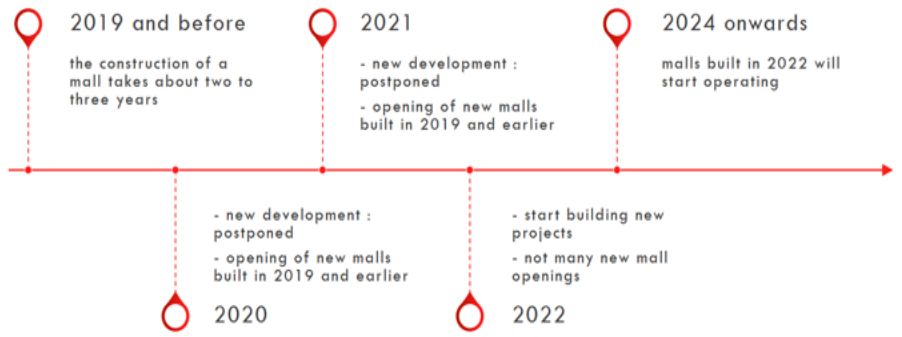
The statement is largely in line with our view that there are risks relating to rising fuel prices, higher inflation rate, and lower subsidy ahead – all of which could have a greater impact on mid-to-low segment retailers post *Lebaran*. We keep our preference for mid-to-high-end retailers, given the more resilient target market and distinctive products to pass on price increases, to cushion margin. We believe the worst is over for ACES, our Top Pick, and its recovery should be robust, partly on strong property sales and a solid margin profile.

Figure 9: Traffic and occupancy will be better than in 2021 and 2020 but still not comparable to 2019



Source: ISCA

Figure 10: Shopping malls' development timeline



Source: ISCA

Indonesia Retail and Tenant Association (IRTA)

Optimism has been high, although traffic has yet to recover to 2019 levels. Following two years of interrupted *Lebaran* festivities, IRTA sees healthy shopping appetite this year. Traffic during the Easter long weekend reached 70-75% from 2019's traffic. However, restaurants were unable to enjoy full benefits as traffic only started picking up in the second week of *Ramadan* (ie mid to end April at +20% YoY) especially during dinner time.

IRTA sees continued behavioural changes during *Lebaran* festivities… There has been a continued switching from hefty purchase of confectionary items (ie biscuit and syrup) mostly bought in hypermarkets or supermarkets to buying lifestyle merchandise (ie smartphone and clothing), with a preference for minimarkets. However, during this *Lebaran*, IRTA witnessed robust growth across all segments, although groceries performed better compared to lifestyle products. Lifestyle retail in 2022 reached 80-90% of 2019's sales, of which women's fashion displayed strong traction. In terms of categories, soft cake and cough syrup grew the most. Department stores may reap some benefits during the *Lebaran* festivities, although long term prospects remain challenging. The customers currently prefer to pay attention to an in-depth offering of products.

… also bolstered by solid purchasing power. We learn that purchasing power has been strong across the board, which should translate to stellar sales performance during *Lebaran*. There are a number of catalysts such as high commodity prices, three paydays during the fasting period, social assistance for the mid-to-low segment and full payment of festive allowance. Based on Bank Indonesia's and Kompas' research & development team, cash outflow during *Ramadan* and *Lebaran* reached IDR175trn, slightly lower than IDR192trn recorded in 2019. IRTA sees mid-to-low retailers and retailers located in Tier-2 and -3 cities enjoying more benefits as people returned to their hometowns, bringing money to be spent there. The number of indicators have also demonstrated strong recovery post a more controlled pandemic such as through GDP growth, the Consumer Confidence Index, retail sales, loan growth and consumer spending. We believe this was mainly driven by revenge spending. We believe consumer behaviour has returned to normal since the change of consumer behaviour (ie using food delivery, online grocery shopping, online education and telemedicine, as well as working from home) is not sticky.

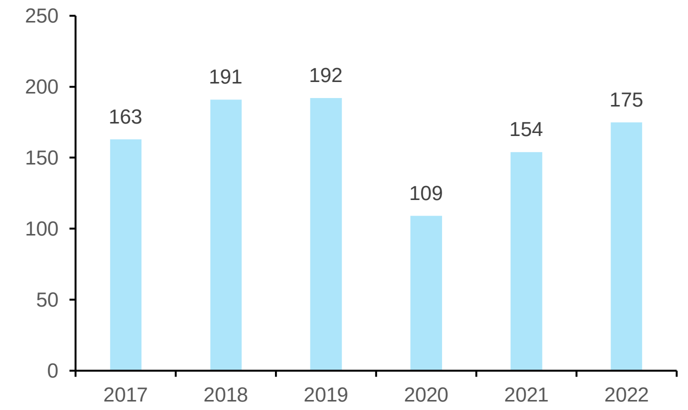
Retailers are resuming their expansion plans. IRTA shared that a number of mall openings are in the offing, particularly in 2024, mainly in ex-Jakarta areas. We think the International Trade Centre (ITC) design concept will continue to be challenging and only Sinar Mas Group's ITC may still survive as it has the upper hand given its expertise in operating this concept. Opening in a standalone format and in Tier-2 and -3 cities have also gained more interest during the pandemic. For instance, Mr DIY (MRDIY MK, BUY, TP: MYR4.50) conducted massive openings over the last few years. It has 275 outlets currently, of which 35% are located outside shopping malls. Nonetheless, opening stores in shopping malls have started to gain interest again as COVID-19 subsides. Worth mentioning, most malls are still giving rental discounts although the discount rate is lower.

Offline players should be able to regain their competitive edge post pandemic. IRTA sees offline players performing better post pandemic, while online players should not continue to pose a threat. The association notes that online sales performance in countries such as the US and China has returned to normal levels, post pandemic. Online players are faced with a number of structural issues that need to be addressed, such as improving operations to increase customer stickiness – customers are heavily reliant on discounts, and this has allowed the B2B commerce to gain stronger traction.

The share of online sales is estimated to have reached only 3-5% for grocery products and 5-10% for lifestyle products, at this juncture Online retailers, in IRTA's view, provide little customer experience, fewer services to attract customers, and see less impulsive behaviour, as well as involve higher last mile and packaging costs, albeit, faster delivery. Also, offline retailers have more experience with consumers, operational excellence, supply chain, and relationships. The threat from the Metaverse is still insignificant, especially with high hardware prices. IRTA believes the metaverse is more focused on branding activities at the moment. It says retailers should focus on providing omni-channel instead of multichannel strategies – which is currently being implemented. However, it expects a major threat from live commerce activities, which may transform shopping trends. We believe offline retailers are aware of this, leading them to start building their presence on TikTok. E-commerce players are also moving in this direction.

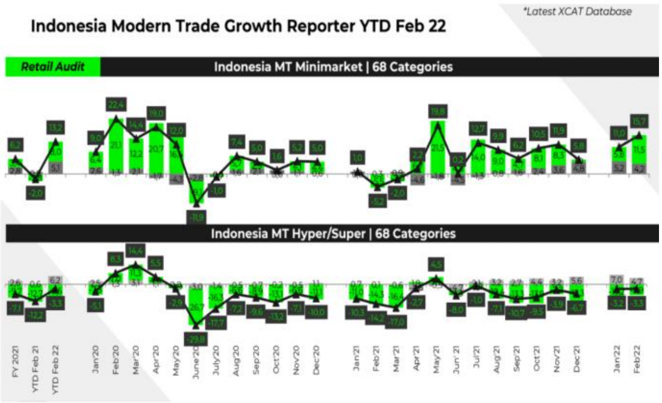
There may be a slight pinch in purchasing power post *Lebaran*, owing to seasonality, and an increasing number of cost components – leading to a high inflationary environment. This is in line with our view that mid-to-low segment retailers may feel a bigger impact. Nonetheless, we are concerned that this will create challenges for mid-to-high segment retailers, given the reopening of international borders. Higher imported product prices – due to safeguard tariffs, and the fewer products due to the import quota on high-end products – may result in more purchases abroad. We think strong government support is still needed to manage the situation. We learn from IRTA the Government is planning to continue the social assistance programme to cushion the impact on purchasing power among the mid-to-low income group. IRTA may also hold discount programmes in August to encourage shopping activities.

Figure 11: Cash outflow during *Ramadan* and *Lebaran*



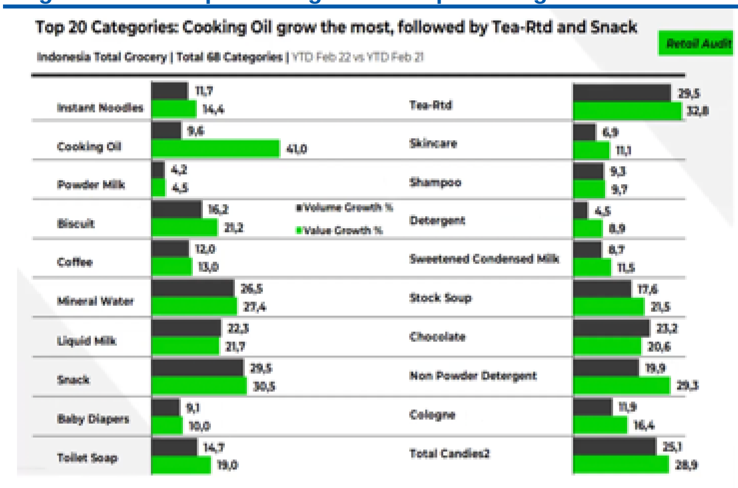
Source: IRTA, Indonesia Central Bank, Kompas R&D Team

Figure 12: Minimarket shopping is still the key driver



Source: IRTA

Figure 13: All Top 20 categories had positive growth

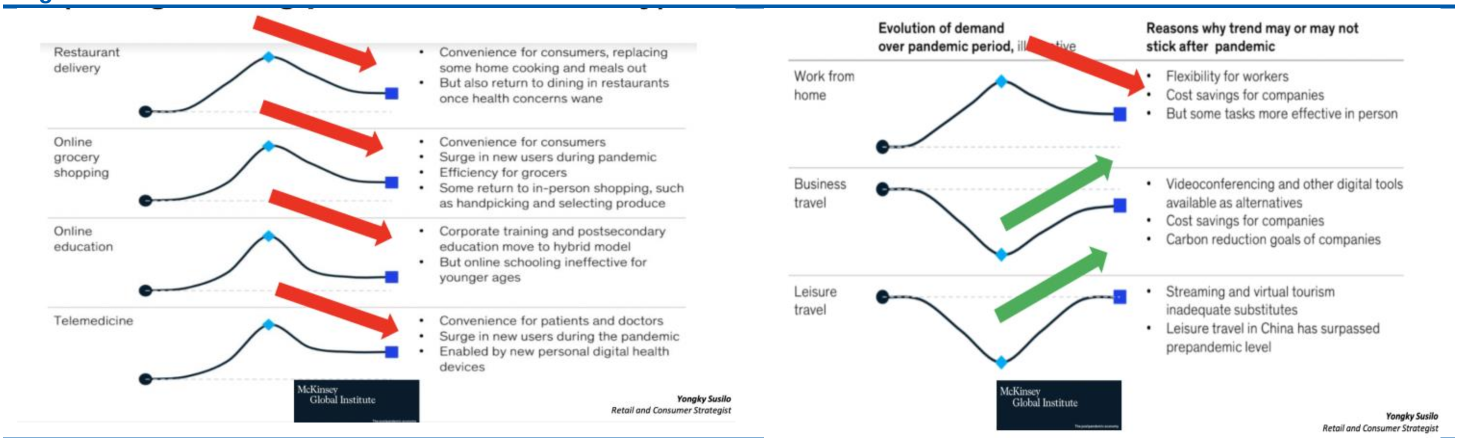


Source: IRTA

Figure 14: Soft cake, cough syrup saw the biggest growth

Source: IRTA

Figure 15: Customer behaviour has normalised



Source: IRTA, Mckinsey

Groceries

Matahari Putra Prima (MPPA IJ, BUY, TP: IDR1,200)

1Q22 revenue was in line, at IDR1.69trn (+9.2% YoY, -1.7% QoQ) due to the Omicron variant. Online sales surged by 56.3%, contributing 7.3% of its total revenue. However, sales were strong in April, with MTD sales growing 26.5% YoY at offline stores and 81% YoY at its online stores. This is mainly attributable to the improving COVID-19 situation – resulting in eased social restrictions and the end of the cooking oil shortage. Basket size fell 10-11% YoY as customers opted for products with lower prices, although the higher number of customers helped negate this, fuelling sales growth. It is worth noting that electronic product sales have been strong during the fasting period and *Lebaran*. This is in line with MPPA's goal to push the sales of electronic items amidst a less intense competition landscape.

On the online front, MPPA has started working with Bukalapak (BUKA IJ, BUY, TP: IDR900) and aims to strengthen the collaboration by onboarding more stores. It has already onboarded six stores on the Bukalapak platform. Cooperation with Lazada is in the offing. Margin for this segment has improved after the company cut back on promotions. MPPA's complete product offering helped strengthen its position as the most preferred by customers in the online space, despite intense competition. The wide range and end-to-end product offerings helped consumers purchase all of their needs in one place, which is MPPA's online store.

It aims to launch dark stores by Jun 2022 in the Greater Jakarta areas that are not served by the company's outlets. Margin for such stores – where customers collect items ordered online – are similar to offline businesses, and may help strengthen MPPA's position in the digital space. The company should be in a stronger position to compete with other pure online dark stores such as Astro and Happy Fresh. The digital store concept should be launched by 4Q22. MPPA is working with a number of vendors regarding its IT development. This new store will have advanced features, which will be gradually applied such as barcode scanning, facial recognition, self-checkout, among others.

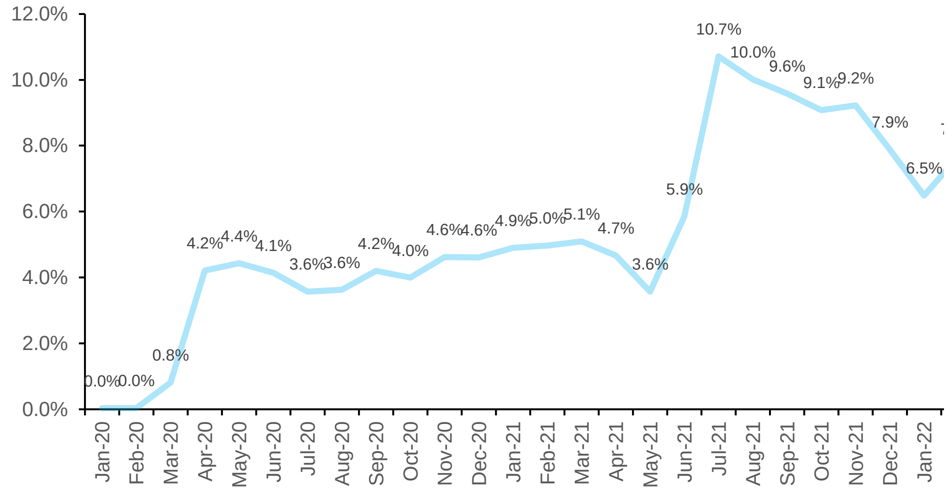
Gojek and Tokopedia combined became the top contributor of MPPA's third party online sales. Collaboration with GoTo on Go Screen initiatives has been solid, providing better insights to MPPA and its suppliers. It may provide targeted promotions, such as customised vouchers, in the future. We think more strategies are on the cards, such as collaborative data exchanges to get a better understanding of customer behaviour.

It will proceed to open more stores across all formats, but closure of non-profitable stores (mostly located inside shopping malls) will continue. The company may only acquire one more ex-Giant store, bringing the total of ex-Giant stores purchased to 10 by end-2022. Management guided that performance of those stores have been encouraging, especially by selling better quality fresh products. Revenue growth target is c.20% YoY with expected net profit to be booked by 2023. MPPA has been cautiously optimistic on its purchasing power, amidst the hyperinflationary situation and potential COVID-19 situation post *Lebaran*. It may work with e-wallet players and banks to create promotions to attract more customers.

Also, MPPA has conducted massive purchases in light of heightened geopolitical uncertainties and a rising cost environment. That said, we are likely to see an increase in inventory in the upcoming months – the company is creating buffer stock of about six months. This, in turn, may partly alleviate margin pressure. MPPA aims to cooperate with Walmart to monetise its global procurement, which should partly help to enlarge its private brands contribution (and fetch much higher margin) from 2.5% to 8-10% going forward.

1Q22 revenue should come in line with our forecasts, along with its goal to be profitable by 2023. We like its strategy to expand its presence in the online space, as well as establish its own dark stores to stay competitive. However, we will continue to monitor the situation post *Lebaran*, in terms of the COVID-19 situation and purchasing power. We think short-term sentiment will be weak for the technology sector, given the overall global situation, and this may pressure the stock as well.

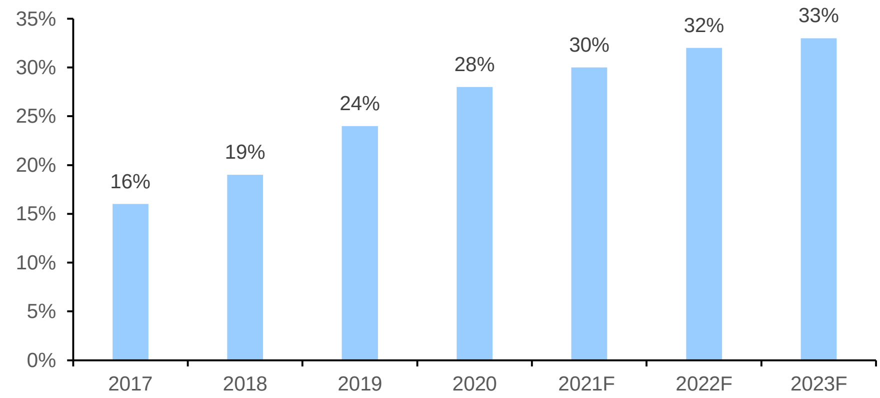
Figure 16: MPPA's online sales contribution



Source: Company data, RHB

- Online sales contribution soared to c.10-11% during the Enforcement of Restrictions on Public Activities or PPKM period. We see the trend has started to normalise, as offline sales have gained more traction
- Online sales remained strong vs 2020
- 2M22 online sales may slow down given the absence of cooking oil products. MPPA aims to resolve this issue by end-March

Figure 17: MPPA's fresh products sales contribution



Source: Company data

- The company managed to improve its competitive edge, particularly in improving the contribution of fresh products to enhance traffic and traffic frequency

Food and Beverage

Fast Food Indonesia (FAST IJ, NR)

Traffic for Fast Food Indonesia was strong during Lebaran. Daily sales during *Lebaran* almost doubled from 1Q22, albeit, still slightly lower than pre-pandemic levels. SSSG stood at about 18%, whilst transactions also rose by 16%. Nevertheless, basket size was still lower, at around 10-20% of 2019's levels. The company aims to increase transactions in the near term, especially dine-in activities. As such, management has been more prudent in increasing the price of goods to pass on cost increases. Note that the number of cost components is climbing, and this may pressure margin, as the company does not fully pass on the cost increases. It still enjoys rental discount rates from several landlords. FAST is still allowed to pay royalty fees through an instalment scheme to YUM!. The company is also more mindful in managing its labour cost. It has continuously monitored the transaction per labour matrices to manage efficiency.

Its expansion pace is still slower than 2019 levels. The company only aims to open 10-15 KFC stores this year compared to 40 store openings in 2019. While traction at Taco Bell has been positive, the company aims to open only five stores in 2022 as it needs to be prudent in terms of location. This Taco Bell concept is aimed at a different target market (ie higher income level since Taco Bell's price points are at around 10-30% higher than KFC) and customer preference. Despite the mild competition landscape in Mexican food, Indonesians are less familiar with Mexican food. As such, it mostly open stores in places with a high income level located entirely in Jakarta. Other key cities such as Bali may provide opportunities for Taco Bell's stores expansion ahead.

KFC's Naughty by Nature performance starting to normalise. We saw a massive hype during its opening, with ticket size higher than KFC or even Taco Bell. Aside from KFC's signature friend chicken, there is now also a grilled chicken option together with an array of dishes and combinations – this translates to a higher basket size. That said, it has been very selective in locating this concept store given the high price point.

A number of challenges await post *Lebaran*. The mid-to-low income segment may feel the pinch due to the rising cost environment and more intense competition. FAST aims to boost promotions post *Lebaran*. New product launches are still in the offing. Sales are expected to return to 2019 levels, while bottomline will likely be positive. The company conducted a number of activities to manage its margin such as switching between open market and contract supplier for chicken purchase. Imported components have been minimal, which should help margin.

The company has been cautiously optimistic, especially post *Lebaran*. We have concerns on its margins amidst the rising cost environment. We like FAST for its solid fundamentals and strong entrenched brand equity. We also have concerns on its thin trading liquidity. The company is mulling a number of initiatives to manage the issue. However, these were put on hold due to the pandemic.

Sarimelati Kencana (PZZA IJ, NR)

***Lebaran* sales have been strong, albeit, not at pre-pandemic levels yet.** Overall basket size in 2021 was still lower than pre-pandemic levels, as dine-in activities have not fully recovered. The increasing dine-in portion should be positive to enhance margin as dine-in revenue fetches higher margin. Ensuring product availability remains Sarimelati Kencana's key focus during the *Lebaran* season. Its Dim Sum Pizza has gained strong traction, but not as much as the 1-metre long Limo Pizza. The impact of cost increases has been manageable since cheese and meat prices are relatively stable. The company is likely to increase prices by c.2% in Jun 2022. It still enjoys rental rate relaxation, although the discount rate is much lower than the previous two years. PZZA also obtained royalty relaxation from Yum! following the agreement to open a certain number of stores for two years.

PZZA is conducting aggressive store openings at around 100 new outlets in 2022, with net opening (after deducting possible closures) at around 70 stores. It will continue to launch more stores with smaller concepts of Pizza Hut Restaurants (PHR) and Pizza Hut Delivery (PHD) – mainly free-standing concepts. Penetration to into ex-Java areas will also be stronger. For instance, the company currently has three stores in Papua and may add another one. We believe the stand-alone concept should allow PZZA more flexibility in terms of operating hours, as well as providing features such as drive-through and breakfast programmes. Its expansion to outside Java should also be positive given less intense competition and lower cost structure**.** Infrastructure developments should increase connectivity and stimulate economic activities in several cities.

Also, the smaller concept outlets should help margin given more efficient operations. This should lead to lower opex, in addition to better working capital. The smaller outlets should also help PZZA become more agile in terms of future store expansion, especially in improving its reach into smaller cities. The company has discontinued the sale of pizza via motorcycle to maintain product and service quality. It was one of its many strategies to survive during the numerous social restrictions over the last two years. However, the food truck concept will be kept to help the company gauge market perception and potential before opening a permanent store in a particular area.

PZZA launched its mobile digital app in 2020 to broaden its channel and attract more sales, particularly from the younger generation. This strategy should help it remain at the forefront of accelerating digitalisation trends, as well as support sales during the pandemic. The company previously worked with a number of aggregators to fortify its digital footprint. We learnt that sales from this channel has started to slow down post relaxation of social restrictions. Risk is likely in the form of higher commission rate charged are aggregators start to eye to be profitable. However, we think the risk is manageable as PZZA should enjoy preferred treatment since it has become one of the Top 3 merchants in the online space.

Similar to other retailers, PZZA acknowledges concerns on the uncertainties relating to geopolitical tensions and hyperinflationary situation. This may impact purchasing power. However, impact on raw materials should be more manageable considering two of its main raw materials – cheese and meat – have relatively stable prices. Also, its mid- to high-end income market segment should have relatively better purchasing power. Nevertheless, we will monitor the situation to see the impact to its margin. The company may boost promotional activities such as bundling products to cope with the situation.

The company sees sales returning to 2019 level. Additionally, we expect margins to improve in 2022, underpinned by the return of dine-in activities and as more concepts are established. We like the company as it trades at 11-12x 2022F P/E based on Street estimates. However, its main risk lies in terms of its thin trading liquidity profile.

Figure 18: New outlet with the Fast-Casual Delco (FCD) concept

Source: Company

Figure 19: Food truck concept

Source: Company

Fashion And Clothing

Matahari Department Store (LPPF IJ, BUY, TP: IDR6,600)

Sales during Lebaran appeared to be encouraging, albeit, still not at pre-pandemic levels. Note that LPPF's average basket size grew by 12% YoY in 1Q22. Categories such as children's wear, footwear, men's wear, as well as women's wear posted positive traction. The company observed that adults, especially parents, have started to buy clothes for themselves following two years of tough economic conditions, which forced them to prioritise their children. Overall, 1Q22 results were in line with our and Street estimates. Our channel checks show that traffic during Lebaran was strong, and should translate to a solid 2Q22.

New signature stores – targeting slightly higher income customer segment – performed well during Lebaran. These include Plaza Ambarukmo, Yogyakarta, and Mal Taman Anggrek, Jakarta – both with a more premium concept, to widen its customer base and grow basket size. However, stores in Mal Taman Anggrek saw softer traction – Matahari Department Store believes sales will be stronger during the Christmas season, given the customer profile. The company aims to open more new stores with a similar concept in other areas. Despite positive initial results for its premium stores, we will continue to monitor the performance post Lebaran, amidst tight competition of Tier-1 products, and mid-to high-income consumer segments.

The possibility of further mass store closures is low, as the company aims to expand its presence. The company aims to open 11 new stores in 2022. Locations of nine new stores have been identified, while two stores are already opened. It has minimal aged inventory as the company aims to maintain the freshness of its products to attract buyers and stay competitive. More new brands have been added, and mostly launched within its new-concept stores. The company has been more prudent in its merchandising strategy to manage its aged stock levels. Note that the company has conducted deep research and will continuously monitor its trial activities to see the development of its new brands. LPPF currently prefers to collaborate with prominent and more well-known branded in South-East Asia, especially Indonesia, which is easier for it to build brand awareness and sell the products inside the store.

The availability of Buy Now, Pay Later (BNPL) features like from Atome and Kredivo partly helped to boost basket size. The use of BNPL has helped to increase the basket size, along with strong traction. Results have been positive, with basket size increasing by 40-50% vs average, while sales via BNPL over three months have been similar to that clocked by digital wallet payment in one year.

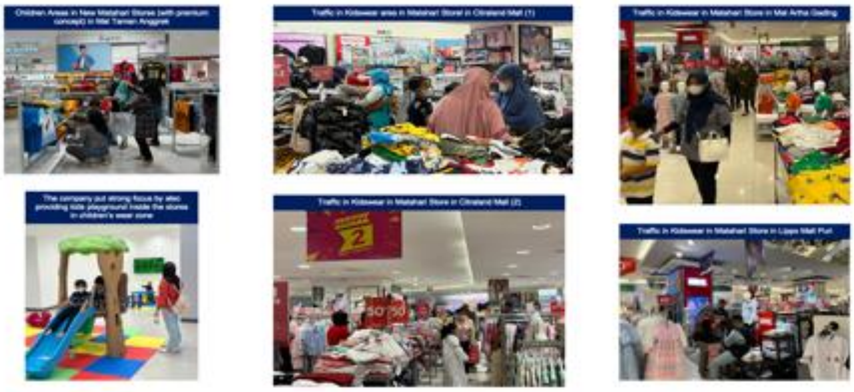
Similar to other retailers, LPPF sees the possibility of weaker purchasing power post *Lebaran*. It has several initiatives to buffer this possibility – amidst the hyperinflation environment – including intelligent pricing, selective promotions with partners (digital wallets, banks), product cross-selling among principals, and collaborations with BNPL companies. To deal with the weaker purchasing power, the company conducted a number of promotional activities to manage the impact. It expects the possibility of downtrading to provide opportunities for the company.

Figure 20: LPPF's *Lebaran* campaign

Source: Company, RHB

- The *Lebaran* campaign – under the umbrella initiative titled *Lebaran ala Indonesia* – began at end March, with a lucky draw campaign that was supported by business partners
- Results have been robust, surpassing that of 2021. However, the numbers have not recovered to 2019 levels
- Stronger digital media marketing initiatives are in place, eg ramping up collaborations with influencers

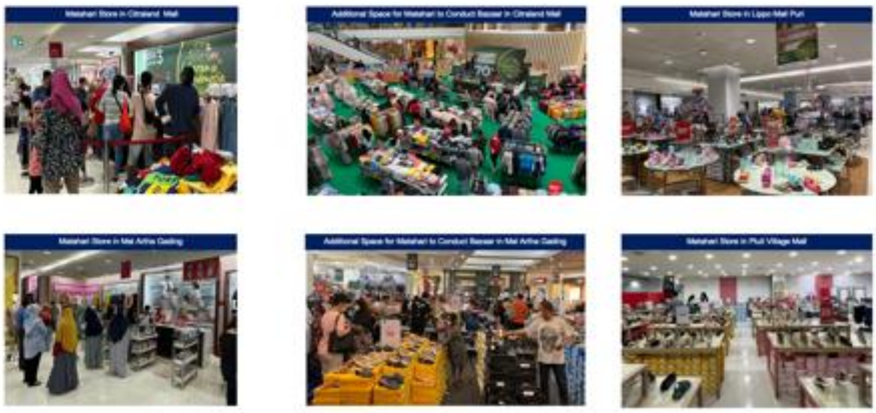
Figure 21: We like LPPF's strategy of putting greater focus on selling apparel for children



Source: Company, RHB

- The company still has a market leader in retail apparel for children, as seen by the robust shopper traffic in its sections dedicated to selling children's clothes
- LPPF has also installed playgrounds inside its premium stores to enhance the customer experience for parents and children

Figure 22: LPPF should enjoy strong sales in 2Q22



Source: Company, RHB

- Sales of children's apparel and footwear were especially strong
- LPPF has been aggressively capitalising the *Lebaran* momentum, by holding temporary bazaars outside stores

Figure 23: New stores are designed with a more premium concept in mine, vs its general department stores

Source: Company, RHB

- We note the number of differences between LPPF's premium concept store and that of its general department store. These include front entrance layout, signage of product category, spaciousness and store lighting
- The newer stores have a bigger floor area for their beauty halls. However, these stores have fewer brands – albeit – those that fetch bigger margins. Traffic at the new concept stores is slower than that of its general stores

Other Lifestyle Retailers

Erajaya Swasembada (ERAA IJ, BUY, TP: IDR1,100)

Sales were likely affected earlier this year due to the Omicron variant but recovery rate has been strong, especially in April. Although mall traffic has yet to return to pre-pandemic levels, the same cannot be said about ERAA's sales, which exceeded pre-pandemic levels. The IMEI impact and shorter payment period brought about industry consolidation, which presents a better playing field thereby benefitting ERAA, which has secured a c.30-40% of Indonesia's smartphone market share – market share of high-end products is likely more than 50%. Its strong and established relationship with suppliers has help ERAA to maintain its product supply amidst the lingering issue of chipset scarcity. It has been able to become the single distributor for DJI and Garmin products, a testament to its ability to the solid relationship with its suppliers.

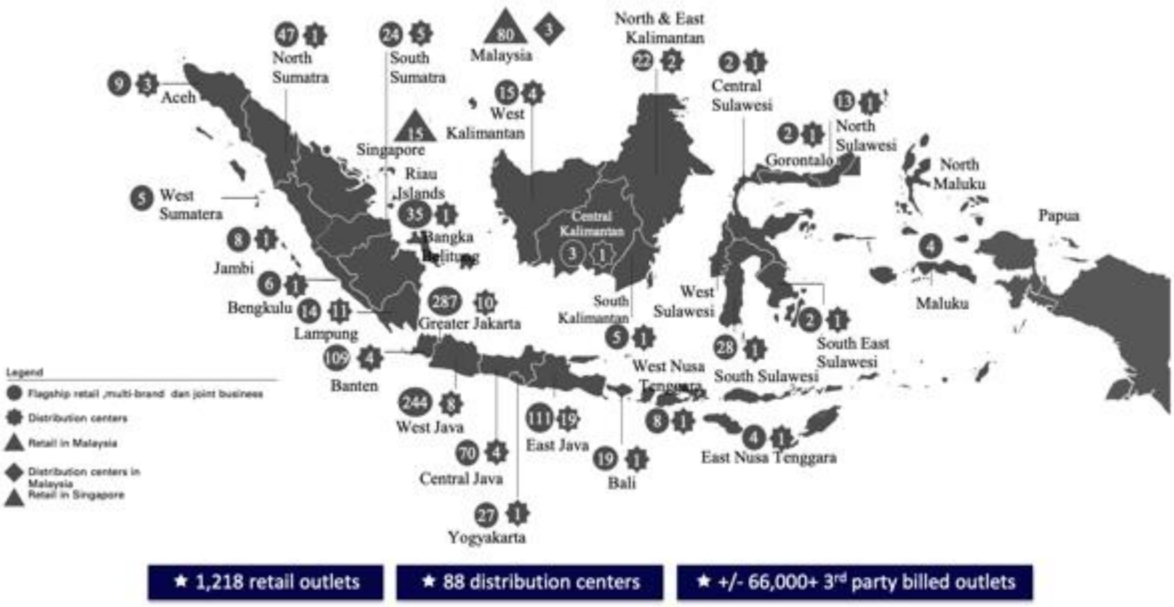
To seize the momentum, the company will continuously conduct its massive expansion plan of opening around 500 smartphone outlets in 2022. We think there may be some store closures, mainly from the termination of its collaboration with supermarkets or hypermarkets given the waning concept of these two modern trade formats. Erafone Cloud Retail Partner outlets performed well, which have reached 20 stores by 2021. More stores under this scheme are expected, albeit, ERAA prudently selecting its partners. Even though there may be concerns regarding quality control, we believe this strategy will help ERAA to rapidly expanding its footprint, particularly outside of malls, and to Tier-2 and 3 cities, with less capex required.

Ample long-term potential from diversification strategy. The company has ventured into a number of businesses, outside smartphones. ERAA has collaborated with several notable partners, in their respective fields to gain better competitive advantage. For instance, the company cooperated with JD Sports, the world's fourth largest sportswear player, which has helped them to better negotiate with big brand owners, such as Nike, Adidas, among others. The progress has been encouraging, although it needs more effort to improve Face Shop stores' performance given some pressure from rising COVID-19 cases. Grand Lucky productivity might be 3-4x higher compared to its competitors. ERAA currently has two stores, each located in Jakarta and Bali, and it plans to open more outlets. Grand Lucky's new stores will offer different and better customer experience. The company aims to open the first Wellings drugstore in May 2022, which will be located outside the shopping mall centre. ERAA aims to capture the benefits of the electronic products' industry consolidation by working with Mobile World, one of Vietnam's notable electronic products players, to open an outlet in Indonesia.

Although it may take time for meaningful contribution, we see ample potential from this diversification strategy. This should provide benefits such as i) improving customer stickiness and purchase frequency, ii) enhancing its ecosystem by creating better synergies among its business units, and iii) better profitability profile as these new businesses naturally have a larger margin and cost reduction possibilities from greater business scale and lower rental rate. Also, better margin profile in the future might translate to better valuation. The company is currently trading at less than 15x P/E as it is valued as a distributor company. With the diversification, we think consensus may value ERAA as a retailer, potentially resulting in a stock rerating.

ERAA also shares post-Lebaran purchasing power concerns. Impact on transport cost should be minimal and yearly salary increase have been factored in. The increasing contribution of the retail business should help to boost margin in 2022. Retail business – which has a higher margin – accounts for 55% of group revenue vs 45% during the strict social restriction period. The company continues to enjoy rental relaxation from several malls operators although the discount rate has been lower than the previous two years. Nevertheless, we remain concerned on its leverage amidst rising interest rates. Management guided that it is currently in discussion with banks regarding this issue.

Figure 24: ERAA's massive footprint



Source: Company

Figure 25: ERAA's business pillars

Source: Company

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