

18 June 2021

Consumer Cyclical | Retailing

Tomei Consolidated (TOME MK)

Not Rated

The Attraction of Gold

Fair Value (Return): MYR1.63 (+44%)
Price: MYR1.13
Market Cap: USD38.0m
Avg Daily Turnover (MYR/USD) 3.60m/0.88m

- **MYR1.63 FV based on 8x FY22F P/E.** We believe Tomei Consolidated's positioning as an integrated manufacturing, wholesaling and retailing business gives it a competitive advantage against most single store operators. Demand for gold tends to increase for protection against volatility, besides being a safe-haven investment. Its alternate sales platforms and better understanding of customers' needs should lead to sustainable growth. That said, our valuation is still below regional industry peers' forward P/E of 17x, implying potential opportunity.
- **An integrated manufacturer and retailer of gold, jewellery and diamonds.** TOME has 54 retail outlets under the Tomei, Goldheart, Le Lumiere and De Beers brand, while also wholesaling to other jewellery stores. More than 80% of sales are from the yellow gold product range, given the local preference for yellow gold ornaments' value and design. This is subjected to seasonality whereby festive seasons and special occasions tend to attract demand.
- **Consumer spending to help in economic uncertainty.** 1Q21 saw a remarkable increase in sales from the retail as well as manufacturing and wholesale segments, contributed by festive seasonal demand and revenge spending. The low interest rate environment, withdrawals under the i-Sinar programme, and potential higher disposable income from commodity-related earners should help encourage consumer spending.
- **Perceived value as protection against uncertainty.** Gold is widely perceived as the asset that gives protection against volatility and uncertainty. Demand for gold tends to rise as a means of hedging against inflation, and a need as a portfolio diversifier.
- **Potential improvement in product offering through alternate sales platforms and better market intelligence.** TOME has alternate sales platforms ie own website (eTomei), e-commerce market place (Lazada, Shopee, and Zalora), social media (Facebook Live and Instagram) and TV Shopping (Astro Go). While still <5% of total sales, online sales have almost doubled YoY as of 1Q21, implying consumers are more confident in purchasing gold and jewellery via the online channel. With the introduction of the Tomei Jewel Club membership to reach, reward, and retain customers, we believe the market intelligence collected will capture changes in consumer product and spending references swiftly, therefore refining product offerings and inventory management.
- **Competitive advantage.** As one of the largest domestic jewellery chain stores with its own integrated manufacturing and wholesaling business, besides own retail customers, TOME is able to reach other jewellery stores – thus having access to both urban and rural areas without operating under its own arms. This could help to secure a larger indirect customer base, especially in times of an upswing demand for gold.
- **Risks** include fluctuation in gold prices, changes in consumer preferences, and seasonality in market demand.

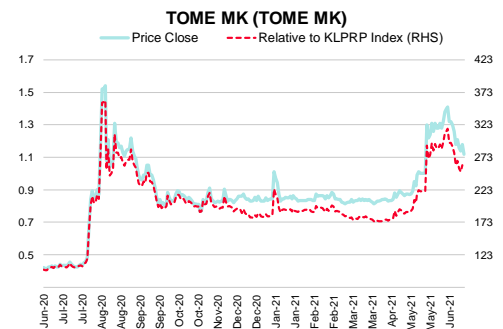
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	32.2	(13.8)	33.7	30.6	162.8
Relative	31.3	(15.6)	36.1	32.2	147.3
52-wk Price low/high (MYR)	0.43 – 1.55				



Source: Bloomberg

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	534	552	576	621	634
Recurring net profit (MYRm)	9	31	25	28	31
Recurring net profit growth (%)	-	256.7	(20.1)	13.6	8.6
Recurring P/E (x)	17.92	5.02	6.29	5.53	5.10
P/B (x)	0.7	0.6	0.5	0.5	0.4
P/CF (x)	5.78	7.49	5.28	7.21	3.22
Dividend Yield (%)	0.9	1.8	1.8	2.2	2.7
EV/EBITDA (x)	6.63	4.16	5.01	4.46	3.75
Return on average equity (%)	4.2	13.8	9.4	9.0	8.5
Net debt to equity (%)	71.6	61.8	51.6	42.3	28.3

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.06	0.22	0.18	0.20	0.22
Consumer Cyclical	DPS	0.01	0.02	0.02	0.03	0.03
Tomei Consolidated	BVPS	1.51	1.74	2.10	2.43	2.77
TOME MK	Return on average equity (%)	4.2	13.8	9.4	9.0	8.5
Not Rated						
	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Valuation basis	Recurring P/E (x)	17.92	5.02	6.29	5.53	5.10
8x FY22F P/E	P/B (x)	0.7	0.6	0.5	0.5	0.4
	FCF Yield (%)	13.4	11.4	17.0	12.0	29.2
Key drivers	Dividend Yield (%)	0.9	1.8	1.8	2.2	2.7
i. Increase in consumer spending from revenge spending, festive season and government assistance	EV/EBITDA (x)	6.63	4.16	5.01	4.46	3.75
ii. Perceived value as protection against uncertainty	EV/EBIT (x)	12.22	6.08	7.98	6.86	5.70
iii. Potential improvement in product mix being offered given increased market intelligence on customer preference and expanded online sales channel						
	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Key risks	Total turnover	534	552	576	621	634
i. Fluctuation in gold prices;	Gross profit	135	139	134	146	153
ii. Changes in consumer preferences;	EBITDA	47	75	63	69	73
iii. Seasonality in market demand.	Depreciation and amortisation	(22)	(24)	(23)	(24)	(25)
	Operating profit	26	51	39	45	48
	Net interest	(12)	(10)	(6)	(7)	(7)
	Pre-tax profit	14	41	33	38	41
	Taxation	(5)	(11)	(8)	(9)	(10)
	Reported net profit	9	31	25	28	31
	Recurring net profit	9	31	25	28	31
Company Profile						
Tomei Consolidated is an integrated manufacturer and retailer of gold, jewellery and diamonds. It has 54 retail outlets under Tomei, Goldheart, Le Lumiere and De Beers while also wholesaling to other jewellery stores.						
	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Change in working capital	11.8	(37.3)	(46.0)	(35.3)	(11.4)
	Cash flow from operations	27.1	20.9	29.7	21.7	48.7
	Capex	(6.0)	(3.0)	(3.0)	(3.0)	(3.0)
	Cash flow from investing activities	(5.9)	(3.0)	(4.8)	(3.0)	(3.0)
	Dividends paid	(1.4)	0.0	(2.8)	(3.5)	(4.2)
	Cash flow from financing activities	(14.0)	(2.6)	(11.1)	(12.6)	(12.9)
	Cash at beginning of period	11.6	19.1	23.2	20.2	25.9
	Net change in cash	7.2	15.3	13.7	6.1	32.7
	Ending balance cash	18.8	34.5	36.9	26.3	58.6
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	19	23	20	26	58
	Tangible fixed assets	46	33	36	38	41
	Total assets	446	472	518	570	624
	Short-term debt	172	174	172	170	168
	Total long-term debt	1	1	0	0	0
	Total liabilities	231	226	222	229	235
	Total equity	214	245	296	341	389
	Total liabilities & equity	446	472	518	570	624
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	(5.3)	3.4	4.2	7.9	2.0
	Recurrent EPS growth (%)	0.0	256.7	(20.1)	13.6	8.6
	Gross margin (%)	25.2	25.1	23.2	23.5	24.1
	Operating EBITDA margin (%)	8.9	13.6	10.9	11.1	11.4
	Net profit margin (%)	1.6	5.6	4.3	4.6	4.8
	Dividend payout ratio (%)	15.9	8.9	11.2	12.3	13.6
	Capex/sales (%)	1.1	0.5	0.5	0.5	0.5
	Interest cover (x)	2.19	5.12	6.46	6.50	7.05

Source: Company data, RHB

The Attraction of Gold

Integrated manufacturer and retailer of gold, jewellery and diamonds

TOME has 54 retail outlets under four brands, which are Tomei (48 outlets), Goldheart (4), Le Lumiere (1) and De Beers (1). It has manufacturing facilities in Malaysia and Vietnam. As at FY20, retail accounted for c.65% of total sales, while the remaining came from wholesaling to other jewellery stores – which also cover overseas markets such as Singapore, Vietnam, Thailand and Germany.

In terms of product offerings, over 80% of the sales are from its yellow gold product range given the local preference for the yellow gold ornaments' value and design. The balance is made up of other jewellery such as white gold, diamonds, precious and semi-precious stones.

Demand for jewellery products is exposed to seasonality whereby festive seasons (ie Lunar New Year, *Aidil Fitri*, Deepavali, and Christmas) and special occasions (ie Valentine's Day, Mother's Day, Father's Day, wedding engagement, and anniversaries) tend to attract demand for jewellery.

On 7 Jan, TOME announced the proposed listing of its manufacturing division through a special purpose vehicle on the Ace Market of Bursa Malaysia. While this is subjected to approval and details are scarce for now, given the capacity of the manufacturing division is almost fully taken up, we assume that if the group manages to go ahead with the proposed listing, this could mean potential opportunity ahead from this division.

Consumer spending to help in economic uncertainty

We see FY20 as a year of change and adjustment in consumer spending. Domestically, while FY20 was impacted by movement control restrictions, with shopping malls not allowed to operate during MCO 1.0, contribution from the manufacturing and wholesales segment improved 29% YoY in FY20, which we believe is due to higher selling price and volume.

According to an article published on the Singapore Bullion Market Association's website: "Malaysia's Precious Jewellery Market", there are over 3,500 retail stores in Malaysia, of which most are run by single-store operators. While TOME's stores are predominantly in major shopping malls, it has a competitive advantage as an integrated manufacturer and wholesaler as it also supplies to other jewellery stores, which we believe helps to reach out to rural customers.

Moving into FY21, 1Q21 saw a remarkable increase in sales from the retail (+32% QoQ; +151% YoY) as well as manufacturing and wholesale (+54% QoQ; +70% YoY) segments, mainly driven by higher sales volume. We believe this is contributed by festive seasonal demand and revenge spending, caused by pent up demand and travel restrictions.

As consumers were not allowed to host major social events during the CMCO, and a total prohibition of social events during the FMCO period, we anticipate the savings from hosting these events could entice more big-ticket item purchase, as a form of psychological compensation.

Our in-house view on the consumer sector expects continuous government assistance in the form of ultra-low interest rate (overnight policy rate (OPR) of 1.75%) and withdrawals from pension funds under the i-Sinar programme could help encourage consumer spending. Additionally, we expect potentially higher disposable income from commodity-related earners, particularly from the CPO industry, as we see CPO prices have increased c.75% from c.MYR2,021 per tonne in early Jan 2019 to c.MYR3,537 per tonne in mid-June 2021.

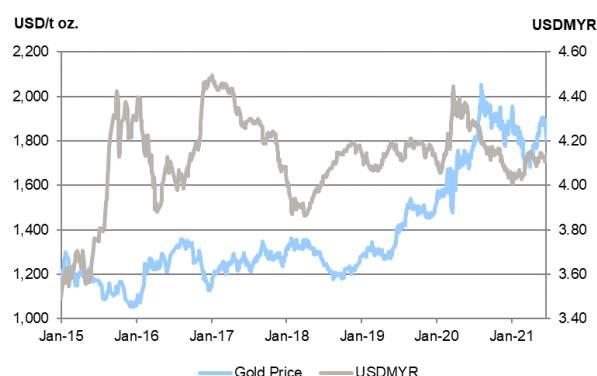
Perceived value as protection against uncertainty

Gold is widely perceived as the asset that gives protection against volatility and uncertainty. In times of depreciation of currency value, investors tend to invest in or purchase gold physical assets as a form of a safe-haven investment, which eventually drives up gold prices.

Additionally, gold is also utilised as a hedging tool against inflation, as rising inflation over a longer period tends to lower monetary value. Given the current low interest rate environment, we believe this could also drive demand for gold, which contributes as a portfolio diversifier.

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Figure 1: Assuming ceteris paribus, gold price tends to drop as the USD strengthens against MYR

Source: Bloomberg, RHB

Figure 2: Share price tends to be more negatively correlated with USD/MYR during an economic downturn

Dec 07 – Jun 09	Tomei	Gold Price	USDMYR
Tomei	1		
Gold Price	0.16	1	
USDMYR	(0.85)	(0.35)	1
End Jan 20 – Jun 21	Tomei	Gold Price	USDMYR
Tomei	1		
Gold Price	0.75	1	
USDMYR	(0.64)	(0.39)	1

Source: Bloomberg, RHB

Based on our study in Figure 2, when the USD strengthens against MYR, TOME's share price tends to move downwards in the challenging market environment. However, there is no highly skewed strong correlation in the movement in gold prices and demand. To illustrate, the drop in gold price may reduce demand from the group of consumers who opt for gold for investment purposes. However, the lower gold price could serve as an opportunity for consumers looking for cheaper jewellery. As such, we view the ability to come out with a variety of products that meets market demand helps to retain and attract sales.

In view of the expectation of an improvement in FY22F-23F earnings (with share price tending to retrace when gold price drops), we believe this could present a better entry opportunity for investors.

Potential improvement in product offering through alternate sales platform and better market intelligence

In order to help partially recoup sales that were not captured from its traditional brick and mortar outlets, the group has gone into alternate sales platforms such as own website (eTomei website), e-commerce marketplace (i.e. Lazada, Shopee, and Zalora), social media (i.e. Facebook Live and Instagram) and TV shopping (ie Astro Go).

We observe that TOME has started to go on Facebook Live since Jun 2020 to promote its products. Over time, it has increased its frequency from once per week to every alternate day, in three different languages, which we think can help to reach various target groups. Also, it serves as a platform to receive instant customer feedback, which can help better understand customer interest.

While only constituting less than 5% of total sales so far, we gather that online sales have almost doubled YoY as of 1Q21. This implies that consumers are more confident in purchasing gold and jewellery via online channels, especially with the insurance being fully covered. As e-commerce is operational during the FMCO period, we still expect c.4% overall growth in FY21 sales.

As the gold and jewellery business is not deemed as an essential service, the manufacturing factory and physical retail stores are not allowed to operate during the FMCO period. We expect this to have a negative impact during this period, as fixed costs are expected to lower profitability. All in, after taking into account of the higher number of COVID-19 infected cases in the country, and uncertainty in near-term recovery, we assume lower FY21F PAT margin of 4.3% (FY20: 5.6%).

Notably, in our opinion, the introduction of Tomei Jewel Club could potentially contribute to the next leg of growth for the group. It is a free membership that helps to reward and retain customers, while serving as a communications channel to reach and update customers. This provides an alternate route for the group to keep customers abreast on its latest product offerings.

Meanwhile, as customers' transactions are being recorded, the data collected and feedback from consumers could help TOME better plan its product offerings. We believe this is vital as it could help to capture changes in consumer preference and spending patterns. By refining its product mix, improvement in inventory management is likely, thereby lowering stock obsolescence and leaving more room for new product offerings.

Progressive improvement in financial health

The group's net gearing was 0.57x as at 1Q21, from 0.92x in FY15, as its cash pile increased over the years. Borrowings are in the form of trade lines, bank overdraft and revolving credit, which are mainly for stock purchase. As such, we do not anticipate any significant decrease in borrowings in the near-medium term. However, given the current low interest rate environment, we anticipate interest savings in FY21F-22F earnings.

Similar to FY20, we assume capex of c.MYR3m pa for FY21F-23F, for renovation and refurbishment of retail outlets purposes. We think this is essential to maintain the image of the store and shopping ambience through the visual merchandise display in order to continue to attract customer footfall.

As for dividend, we anticipate FY21F-23F dividend payout ratio to remain, similar to a historical payout of c.8-16% of PAT, or c.2-3% yield.

Scenario analysis

Base case scenario. Our valuation of 8x FY22F P/E – based on +1.5SD from its 3-year mean – is still below regional peers' forward P/E of 17x. Domestically, despite no information of the forward earnings, we gather that its closest competitor, Poh Kong (PKH MK, NR) is trading at around 6x trailing P/E, higher than TOME's c.4x trailing P/E. We think this could be due to the latter's non-*Shariah* compliant status as well as lower number of retail stores and dividend payout comparatively. However, after a series of kitchen sinking exercises in FY18, TOME moved to streamline operations in FY19, which we think has helped to improve operation efficiencies, thereby achieving significant improvement in FY19 earnings. Share price at that time was trading at c.7x FY19 P/E. Given that our FY21F-23F earnings are about 2-3x higher than FY19, we believe our valuation is deemed reasonable.

We believe its positioning as one of the largest domestic jewellery chain stores with its own integrated manufacturing and wholesaling business stream, gives it a competitive advantage to fare better than most single store operators. Also, in times of economic uncertainty, its products are sought after for various purpose, ie protection against volatility and inflation, or part of a big-ticket item purchase that can fulfil satisfaction from revenge spending while preserving investment value. Given its adaptive approach in the alternate sales platform and more emphasis on digital marketplace and market data collection, we think this could pan out to more sustainable growth in the long run.

Also, according to an article titled "Mined gold supply still not keeping up with demand" by Mining.com, after stripping off recycled gold of 1,297.4 tonnes, total annual gold mine production of 3,400.8 tonnes in 2020 was -4% YoY. Demand, however, was higher at 3,759 tonnes, indicating that demand could only be met after taking into account recycled gold. Over the longer run, we believe gold prices may trend upwards as gold mine reserves dwindle. In view of scarcity of the precious metal and an expectation of increase in gold intrinsic value, we believe this will drive the demand for gold eventually.

Bear case scenario. In the event that the recovery progress from pandemic drags on beyond FY21 and a deep dive in gold prices happen within a short period of time, we believe this will be detrimental to consumer income, and result in lower demand for products in the longer run. As such, our bear case assumes a sharper decline in demand – we apply a lower 7x FY22F P/E (+1SD). Despite lower revenue and earnings expectations, we believe it still deserves a slight premium in valuation – as an integrated manufacturer and retailer of gold, jewellery and diamonds with chain stores across the country, along with its cost optimisation, alternate sales platform and market intelligence adaptive strategy in place, we think TOME will be able to withstand the challenging market environment.

Bull case scenario. Our bull case assumes 9x FY22F P/E (+2SD) with a more optimistic forecast on the revenue. Assuming gold prices continue to climb while the economy recovers at a quicker-than-expected pace, we believe the increase in domestic spending power, resumption of social events as well as recovery in the tourism sector will help to spur demand. That said, we still assign a lower FY21F-22F PAT margin of 5.0-5.2% (FY20: 5.6%), as we expect normalisation in gold margins as the purchase price increases in tandem with the selling price.

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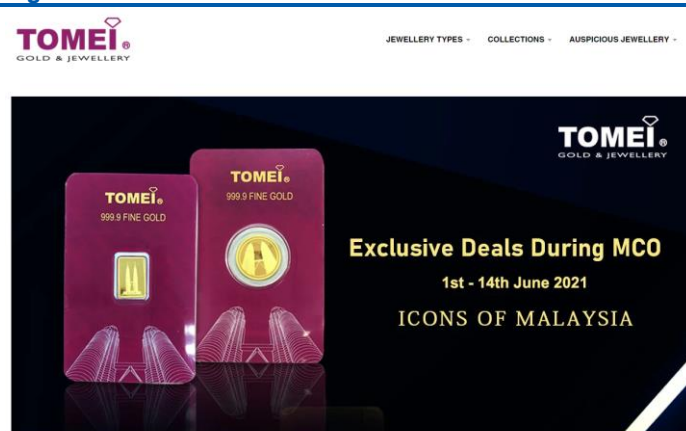
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Figure 3: A brief study on bear, base and bull case scenarios

	Bear		Base		Bull	
	FY21F	FY22F	FY21F	FY22F	FY21F	FY22F
Revenue	472.5	500.9	574.9	621.2	637.3	701.0
PAT	19.3	17.0	24.9	28.3	31.8	36.5
PAT margin (%)	4.1%	3.4%	4.3%	4.6%	5.0%	5.2%
EPS (sen)	0.14	0.12	0.18	0.20	0.23	0.26
Assigned P/E (x)		7		8		9
FV (MYR)		0.86		1.63		2.37
Potential upside/(downside) (%)		-24%		44%		110%

Source: RHB

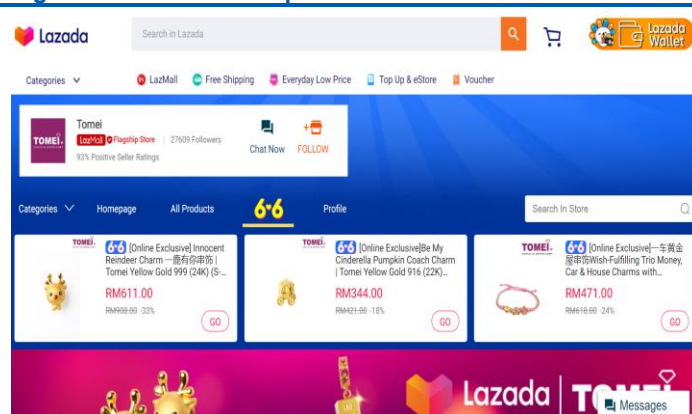
Figure 4: eTomei website



Start your gold investment with exclusive deals for our KLCC Twin Tower during MCO period. Your order will be dispatched on the next business day via SkyNet. All online parcels are fully insured by eTomei.com.

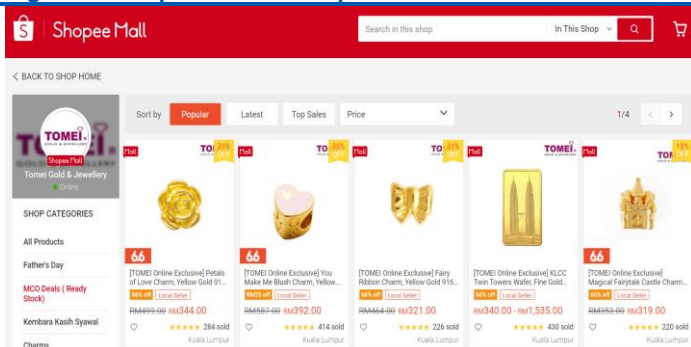
Source: Company

Figure 5: Lazada online platform



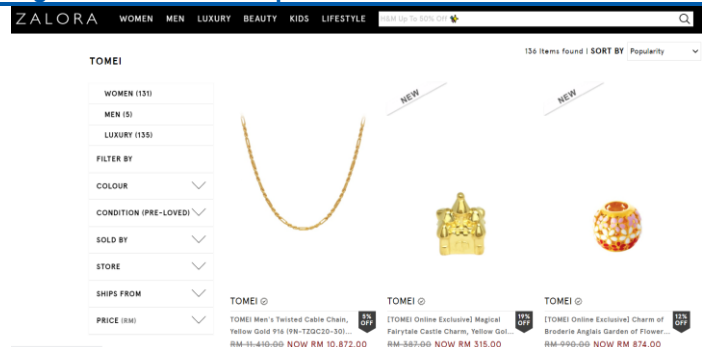
Source: Company

Figure 6: Shopee Mall online platform



Source: Company

Figure 7: Zalora online platform



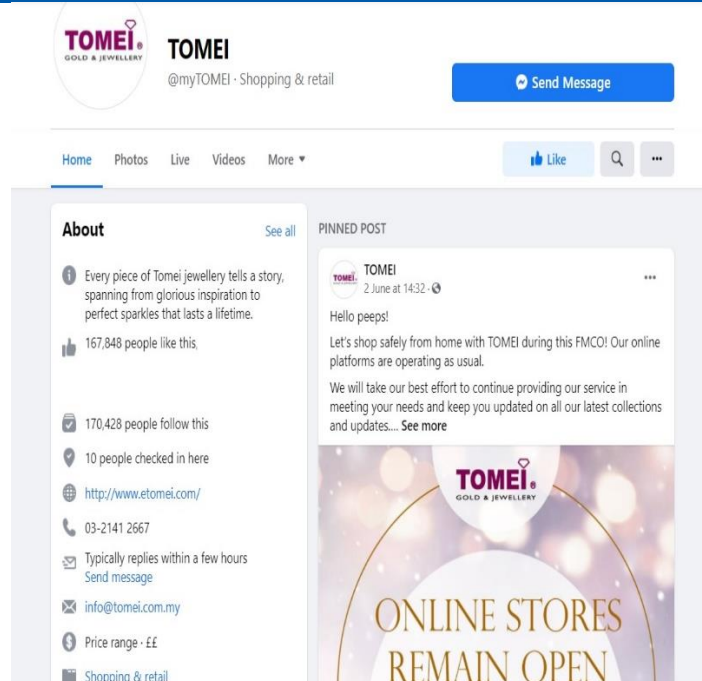
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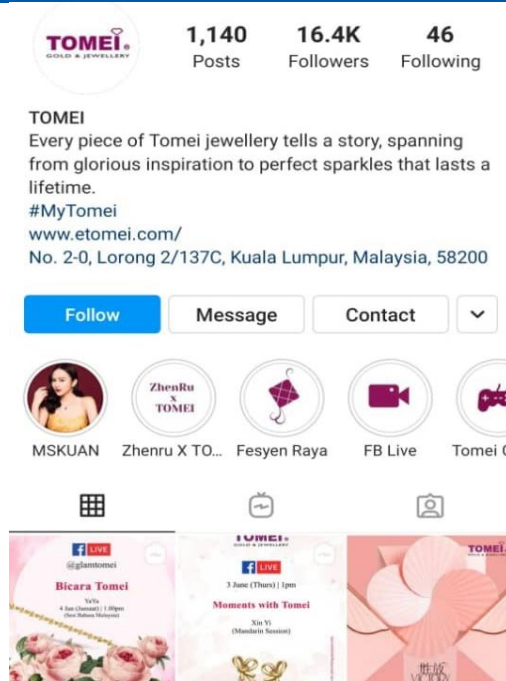
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Figure 8: Facebook page that features Facebook Live videos

Figure 9: Instagram page that features photos & live videos



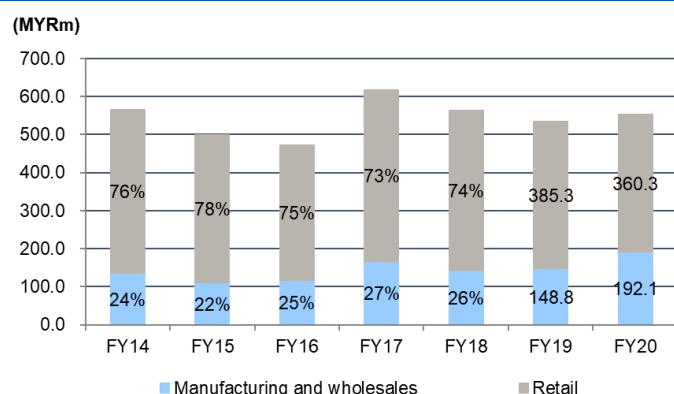
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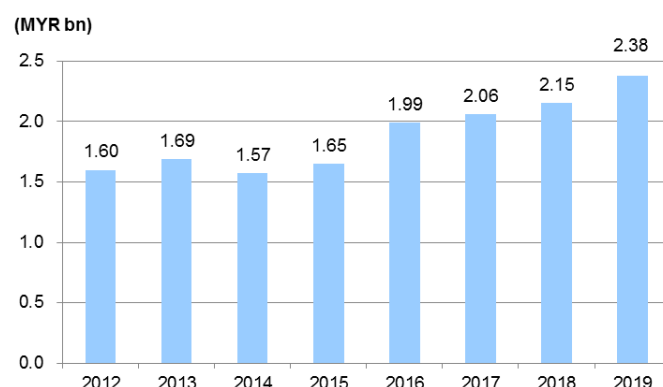
Source: Company data

Figure 10: Revenue by business segment

Figure 11: Sales value of manufactured jewellery and related items in Malaysia



Source: Company data, RHB



Source: Statista

Figure 12: Peer comparison

Company	FYE	Ctry	Price	Mkt Cap (USDm)	P/E (x)		Div. Yld (%)	ROE (%)	P/BV (x)	NP Growth (%)	
			17 Jun 2021								
						1 Yr Fwd	2 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd
Regional											
Lao Feng Xiang	Dec	CH	USD3.16	3,314	11.6	10.5	7.1	20.0	1.1	24.4	10.7
Shanghai Yuyuan Tourist	Dec	CH	CNY12.87	7,770	12.0	10.2	2.9	11.7	1.4	23.9	16.9
Fiyta Precision Technology-B	Dec	CH	HKD7.34	873	13.5	10.8	0.0	13.3	0.9	51.1	25.0
Chow Tai Fook Jewellery	Mar	HK	HKD16.18	20,840	23.9	20.9	3.1	20.9	4.9	12.0	14.3
Luk Fook Holdings Intl Ltd	Mar	HK	HKD23.30	1,762	16.4	12.4	4.3	8.0	1.3	(3.1)	32.4
Chow Sang Sang Hldg	Dec	HK	HKD14.18	1,237	9.5	8.0	4.5	8.2	0.8	84.6	19.0
Weighted Average					19.1	16.5	3.4	17.6	3.4		
(MYRm)											
Tomei Consolidated	Dec	MY	1.13	157	6.3	5.5	1.8	9.4	0.5	(20.1)	13.6

Source: Bloomberg, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-06-17			

Source: RHB, Bloomberg

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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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