

Malaysia Consumer

NEUTRAL

[Unchanged]

Ready for Ready Meals?

Still a relatively under-developed market segment

Coming from a low base and with stepped up efforts to market ready meals by both the suppliers and convenience stores, we believe there is much room for growth in this F&B segment. In the medium term, earnings enhancement for the convenience players would depend on their product offerings and consumers' shifting preference for their potential offerings. Bison remains a BUY with a TP of MYR2.05 (CY17 PER of 25.0x; regional retailer peer average). SEM remains a HOLD.

Moderate growth so far

According to *Euromonitor*, Malaysia's ready meal market grew from MYR105m in 2010 to MYR125m in 2015, posting a CAGR of 3.6%. Meanwhile, Thailand's ready meal market grew at a much faster pace, with a CAGR of 13% (from THB3,611m in 2010 to THB6,725m in 2015), driven by (i) shifting consumer habits towards greater convenience and (ii) the emergence of top convenience players that has increased the availability of ready meals. This does imply that there is still much room for the ready meal market to grow domestically, but this has to be driven by increased offerings by the incumbent and upcoming operators of convenience stores.

Stepping up efforts

As F&B generally carries better margins relative to other offerings in a convenience store, a push up the value chain towards F&B will certainly help with incremental expansion in margins. SEM is now in collaboration (since Apr 2016) with Brahim's SATS Food Services (BSFS) on fresh food/ready meals. BSFS supplies the menu and products to be marketed through SEM's outlets while SEM will provide a centralized distribution centre to handle product delivery. BSFS's products can now be found in over 200 of SEM's stores (mainly in Klang Valley). As for Bison, plans are underway to construct its food processing and distribution facility and this is targeted to be completed by FY18.

Neutral on the convenience retail sector

We maintain our HOLD call on SEM but with a higher TP of MYR1.54 (+16sen), pegged to a higher 27.5x PER CY17 (25x previously) to reflect the current valuations of its regional convenience store peers. Much of the positives are reflected in its current share price. We are positive on Bison. While it is smaller in terms of store count vs. market leader SEM in Malaysia, we believe that it offers a much stronger growth profile, coming from a lower base. Bison has also consistently delivered higher net margins in the past 3 years (3-year average of 6.8% vs. SEM's 3-year average of 2.9%) mainly on better cost controls (eg. admin and S&D expenses) and higher contribution of A&P income as a % of revenue. Bison remains a BUY with a TP of MYR2.05, pegged to CY17 PER of 25x, which is about a 10% discount to SEM and its regional convenience store peers, to reflect its smaller market capitalization.

Sector summary table

	Rec	Share Px (MYR)	Market Cap (MYR m)	Target price (MYR)	PE		Div Yield		ROE		PBV		EPS CAGR
					CY16 (x)	CY17 (x)	CY16 (%)	CY17 (%)	CY16 (%)	CY17 (%)	CY16 (x)	CY17 (x)	CY15-17 (%)
7-Eleven	HOLD	1.73	1,976	1.54	35.2	30.9	1.4	1.6	32.5	31.4	10.8	9.1	10.3
Bison	BUY	1.88	583	2.05	28.7	23.0	0.8	0.8	17.5	14.6	3.6	3.6	32.1

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Ready meal, anyone?

Modest growth over the past few years

According to *Euromonitor*, Malaysia's ready meal market grew from MYR105m in 2010 to MYR125m in 2015, posting a CAGR of 3.6% (2010-2015). While stable, growth is moderate when compared against Thailand's ready meal market which grew from THB3,611m to THB6,725m (CAGR of 13%, 2010-2015).

Strong growth witnessed in Thailand is mainly due to changing lifestyles as more time pressed consumers seek for more convenience. The rise in convenience stores in Thailand has also increased the availability of ready meals and this in turn, has benefited sales.

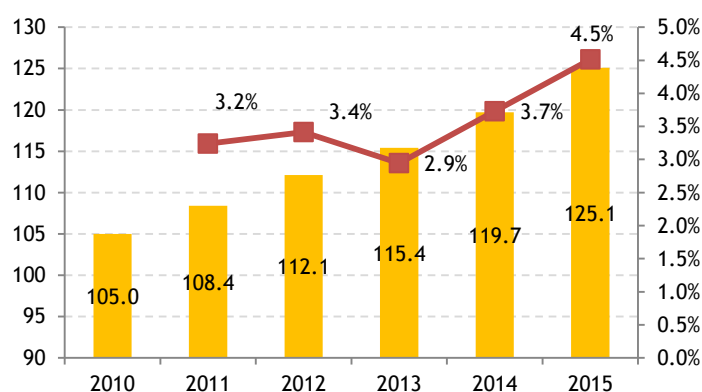
Convenience store in Thailand is the largest distribution channel for ready meals, accounting for 47% of retail value in 2015 (vs. Malaysia's 7.3% in 2015).

Definition of a Ready meal:

Products that have had recipe "skills" added to them by the manufacturer, resulting in a high degree of readiness, completion and convenience. This includes frozen, dried, chilled, canned/preserved meals, dinner mixes, frozen pizza, chilled pizza and prepared salads.

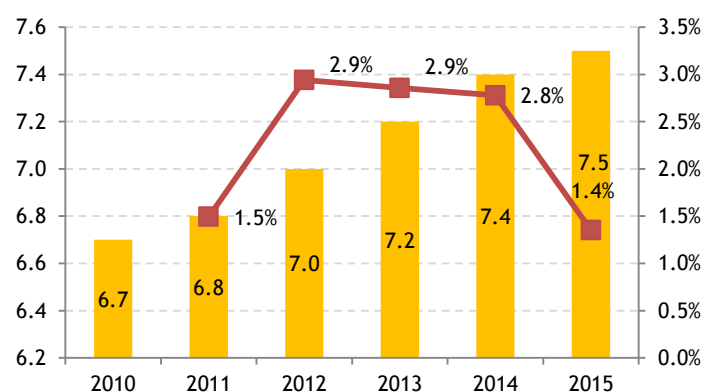
Source: Euromonitor

Ready meal - Malaysia (Retail value and YoY Growth, %)



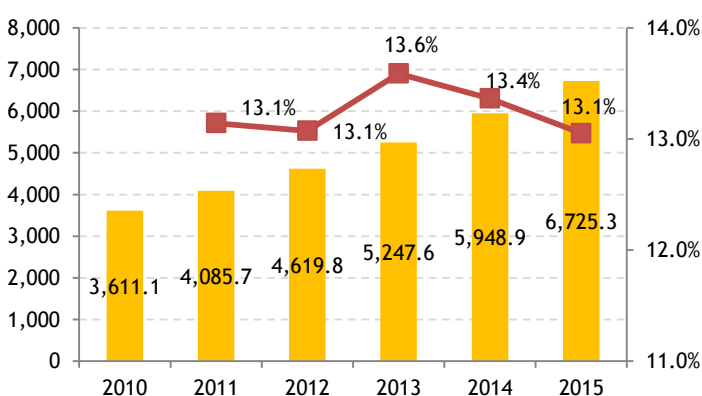
Source: Euromonitor

Ready meal - Malaysia ('000 tonnes and YoY Growth, %)



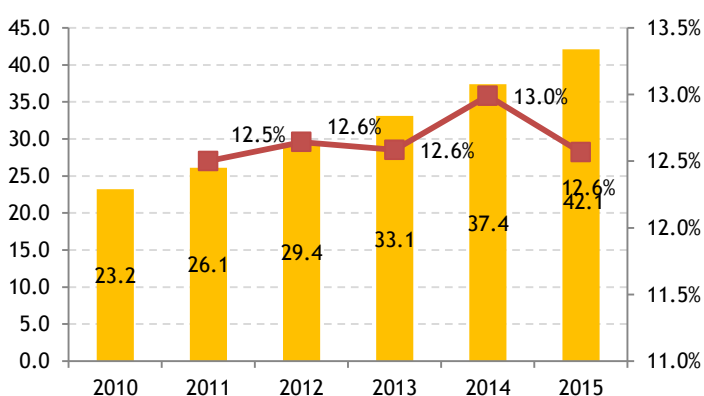
Source: Euromonitor

Ready meal - Thailand (Retail value and YoY Growth, %)



Source: Euromonitor

Ready meal - Thailand ('000 tonnes and YoY Growth, %)



Source: Euromonitor

Distribution of Ready Meals by Convenience Store Format: % Value

	2010	2011	2012	2013	2014	2015
Malaysia	7.0	7.3	7.5	7.4	7.4	7.3
Singapore	8.2	8.0	8.0	8.0	8.1	8.1
Thailand	46.5	46.7	46.8	46.9	47.0	47.1

Source: Euromonitor

Room to grow

As compared to neighboring countries such as Thailand and Singapore, Malaysians consume relatively less ready meals at 0.2kg/capita (vs. Thailand’s 0.6kg/capita and Singapore’s 1.1kg/capita in 2015). On lower consumption of ready meals in Malaysia, Euromonitor’s findings suggest that it is partly due to the consumer’s perception in that ready meals contain preservatives and unhealthy ingredients.

Moving forward, with some of the convenience retailers/food suppliers (i) increasing their food offerings (eg. upping choices and healthier options), (ii) and stepping up their marketing activities, greater variety and awareness should provide the impetus to growth.

Ready meal volumes (kg per capita)

	2010	2011	2012	2013	2014	2015
Malaysia	0.2	0.2	0.2	0.2	0.2	0.2
Singapore	1.1	1.1	1.1	1.1	1.1	1.1
Thailand	0.3	0.4	0.4	0.5	0.5	0.6

Source: Euromonitor

Enhancing its food supply chain

Convenience Stores: F&B generally carries better margins

F&B typically carries higher margins (>40% GP margin) as compared to other offerings (eg. tobacco which carries an estimated 10% GP margin; accounts for 35-40% of sales) in a domestic convenience store.

Meanwhile, while there will be a critical need to control wastage, we understand that fresh food/ready meals which account for estimated 8-10% of sales carry even higher margins of over 50% GP margin. Therefore, a push up the product value chain towards higher margin products (eg. fresh food/ready meals) will certainly help with the incremental expansion of margins in the medium term.

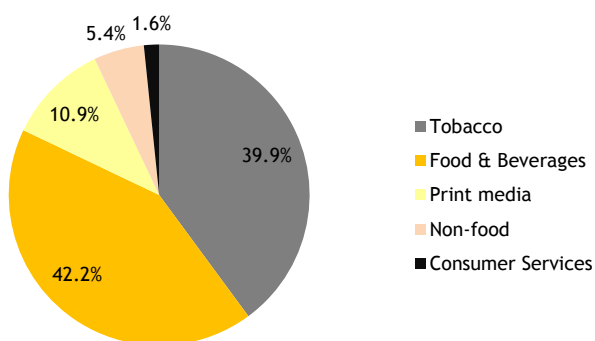
Food and beverage (F&B): *Snack foods, confectionaries, beverages, perishables, ready meals.*

Ready meals: *Subset of F&B. Frozen, dried, chilled, canned/preserved meals, dinner mixes, frozen pizza, chilled pizza and prepared salads.*

Fresh food: *Subset of F&B and ready meals. Ambient and chilled meals, bakery items.*

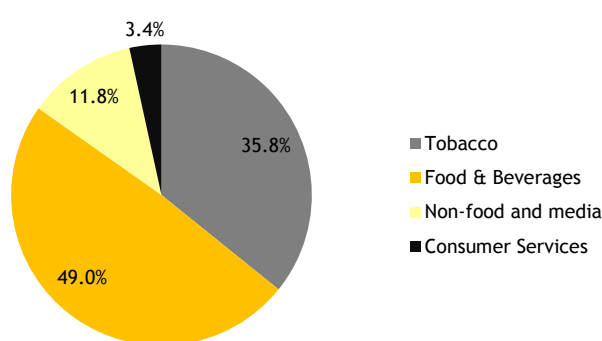
Source: Euromonitor, Maybank KE, Company

Bison’s retail sales mix (end-FY15)



Source: Company, Maybank KE

7EM’s retail sales mix (est.)



Source: Company, Maybank KE

Increasing availability of ready meals

In the recent years, convenience players such as 7EM and Bison have embarked on store expansion plans. With the emergence of these top players with store expansion plans and sharpened focus on the F&B segment, we believe ready meals will see increasing availability or point of sales through the convenience channels. In the longer term however, earnings enhancement for the convenience store players would depend on the type of offerings and the demand for their potential offerings.

7EM has planned for 600 new store openings from CY14-16E. Beyond 2016, management does not rule out the possibility of continuing with the expansion of 200 outlets p.a.. 7EM has 2,001 (end-Jun 2016) outlets in Malaysia.

Bison had in FYE10/14 and FYE10/15 opened 31 and 33 stores, respectively. Looking forward, it targets to open 70 stores p.a. for FY16-18. Bison has 277 (end-Jul 2016) outlets in Malaysia.

QL Resources (Family Mart), a potentially formidable player, has planned for its first store to be opened by Dec 2016. In the next five years, it targets to open 300 stores in Malaysia and be a food centric chain, with an ambitious target of deriving more than 50% of its sales mix from F&B in the longer term.

7-11 Malaysia - Collaboration with BSFS

On the collaboration with Brahim's SATS Food Services (BSFS) (since Apr 2016), SEM is now marketing BSFS' fresh food products in over 200 of its stores which are mainly located in Klang Valley. As a recap, BSFS will supply menu specifications and products to SEM, while SEM will provide a centralized distribution centre (CDC) to BSFS to handle products delivery.

Working with a rather sizeable party could benefit SEM in the longer term in terms of product consistency/quality/choices and cost efficiencies while not having to move away from its core competence of managing convenience stores.

As a recap, SEM has been working with multiple food suppliers. We understand one of the suppliers is PK Agro-Industrial Products (M) Sdn Bhd, a food operator which is part of the Charoen Pokphand Group. It currently supplies ready-to-eat frozen food to SEM.

7-11 Malaysia: Fresh to go (snapshot on The Sun Daily; 19 Sep 2016)



Source: The Sun Daily, Company

Bison - Food processing and distribution facility

As for Bison, plans are underway to construct its food processing and distribution facility and this is targeted to be completed by end of FY18. It has in July 2016 acquired a piece of land (MYR6.75m). The freehold land is 60,000 sq ft and is located just about 500 metres away from its CDC in Rawang, Selangor.

By having a self-managed food processing and distribution facility, Bison views that (i) it can have better control over the quality and consistency of products, (ii) achieve lower costs as it builds scale and (iii) lower logistics costs on having some third party suppliers deliver to its food distribution centre. Upon completion, Bison's targeted mix is 40:60, between third party food supply vs. in-house processing.

Valuations and recommendation

Winner in the works, still unclear for now

All in, we believe that the ready meal/fresh food market segment is relatively under-developed in Malaysia compared to countries such as Thailand and Singapore mainly due to both supply and demand issues. While in the medium term, the food supply chain may be enhanced (on increasing availability), earnings enhancement for convenience store players would depend on their product offerings and consumers' shifting preference for their potential offerings.

Convenience stores will need to be more innovative in terms of product offerings to create a differentiating factor between them. As suggested by *Euromonitor's* finding, consumers in Malaysia generally perceive that ready meals contain unhealthy ingredients and preservatives. In that, convenience store players may begin to introduce healthier product variants. Players are also expected to come up with more creative marketing efforts to both educate consumers and drive sales.

NEUTRAL on the sector

We are NEUTRAL on the convenience retail sector but positive on Bison:

- In the case of SEM, we maintain our earnings forecasts, but with a higher TP of MYR1.54 (+16sen), pegged to a higher 27.5x PER CY17 (25x previously) to reflect the current valuations of its regional convenience store peers. Much of the positives are in the price already at this stage and thus we maintain our HOLD call.
- **Bison** currently trades at a PER of 23x CY17. While SEM, its closest competitor, is larger in terms of store count (2,001 stores as of end-Jun 2016 vs. Bison's 277 stores as of end-Jul 2016), we believe that Bison offers a much stronger growth profile, coming from a lower base. We project a 3-year EPS CAGR of 25%, versus SEM's 11% 3-year CAGR. We also note that Bison has consistently delivered higher net margins in the past 3 years (3-year average of 6.8% vs. SEM's 3-year average of 2.9%). The higher margins achieved are mainly due to better cost controls (eg. S&D and admin expenses) and higher contribution of Advertising and Promotion income as a % of revenue. Bison remains a BUY with a TP of MYR2.05, pegged to CY17 PER of 25x, which is about a 10% discount to SEM and its regional convenience store peers, to reflect its smaller market capitalization.

Consumer sector - Peer valuation summary

Company	Rec	B. Ticker	Share Px	Market Cap	Target price	PE		Div Yield		ROE		PBV		EPS CAGR
						CY16	CY17	CY16	CY17	CY16	CY17	CY16	CY17	CY15-17
			(MYR)	(MYR m)	(MYR)	(x)	(x)	(%)	(%)	(%)	(%)	(x)	(x)	(%)
BAT (M)	SELL	ROTH MK	50.58	14,442	48.50	21.9	21.5	4.1	4.4	100.9	86.3	18.9	18.2	(14.3)
Nestle Msia	HOLD	NESZ MK	79.00	18,526	78.00	27.6	26.7	3.6	3.7	94.1	96.6	28.4	28.1	8.4
AEON CO	SELL	AEON MK	2.91	4,086	2.10	40.2	33.4	0.9	1.0	5.4	6.3	2.2	2.1	(4.2)
QL Resources	HOLD	QLG MK	4.44	5,541	4.15	26.9	24.2	1.0	1.1	12.7	12.7	3.2	2.9	7.3
Heineken Msia	BUY	HEIM MK	17.74	5,359	18.10	20.1	19.8	4.9	5.1	74.5	68.7	14.8	12.5	8.5
Carlsberg Msia	HOLD	CAB MK	14.54	4,473	14.70	18.7	18.1	5.3	5.5	68.9	68.6	12.6	12.2	3.7
MSM Malaysia	HOLD	MSM MK	4.90	3,445	4.22	19.4	17.8	3.1	3.4	8.6	9.0	1.6	1.6	(16.2)
7-Eleven	HOLD	SEM MK	1.73	1,976	1.54	35.2	30.9	1.4	1.6	32.5	31.4	10.8	9.1	10.3
Padini Holdings	HOLD	PAD MK	2.85	1,875	2.50	13.1	12.4	3.8	3.5	30.3	27.5	3.7	3.1	22.9
Berjaya Food	HOLD	BFOOD MK	1.87	702	2.00	28.2	22.2	1.9	2.0	6.3	7.7	1.8	1.7	7.7
Oldtown	HOLD	OTB MK	1.99	898	1.95	16.2	15.3	3.7	3.6	15.2	14.6	2.5	2.3	12.3
Bison	HOLD	BISON MK	1.88	583	2.05	28.7	23.0	0.8	0.8	17.5	14.6	3.6	3.6	32.1
Simple average						24.7	22.1	2.9	3.0	38.9	37.0	8.7	8.1	6.5

Source: Maybank KE, Bloomberg *Closing price on 29 Sep 2016

Regional consumer peer comparison

Company	Bloomberg Code	Shr px (local)	Mkt cap (USD'm)	PER (x)		EV/EBITDA (x)		Div Yield (%)		ROE (%)		3Y EPS^ CAGR (%)	PEG (x)
				FY16	FY17	FY16	FY17	FY16	FY17	FY16	FY17		
Convenience stores													
CP ALL	CPALL TB	61.3	15,887	33.4	28.1	20.1	18.1	1.6	1.9	38.5	38.1	19.5	1.7
President	2912 TT	249.5	8,261	27.3	25.3	14.2	13.1	3.0	3.2	32.8	32.7	10.7	2.6
Tw Familymart	5903 TT	222.0	1,578	33.4	28.8	12.7	11.5	2.4	2.8	29.7	32.2	15.5	2.2
7-11 Malaysia	SEM MK	1.7	480	33.3	27.9	13.6	11.8	1.8	2.0	33.4	34.2	14.9	2.2
Bison	BISON MK	1.9	142	31.9	24.4	20.7	15.9	0.8	0.9	20.5	18.9	31.0	1.0
Simple average			-	31.9	26.9	16.3	14.1	1.9	2.1	31.0	31.2	18.3	1.9
Mkt cap wtd avg			26,471	31.5	27.5	17.8	16.1	2.1	2.3	36.0	35.9	16.5	2.0
Departmental stores / hypermarkets / supermarkets													
Dairy Farm	DFI SP	7.2	9,668	21.7	19.7	15.8	14.3	3.0	3.4	30.1	28.9	8.2	2.6
Big C	BIGC TB	209.0	4,979	22.8	20.2	13.7	12.3	1.4	1.7	15.3	15.5	11.2	2.0
Siam Makro	MAKRO TB	32.8	4,539	29.1	25.1	18.3	16.1	2.6	2.9	36.1	38.0	10.6	2.7
Matahari	LPPF IJ	19,025.0	4,278	25.4	21.9	18.0	15.8	2.5	3.0	134.6	97.3	16.9	1.5
Robinson RH	RRHI PM	77.5	2,219	22.8	20.1	14.5	12.5	0.7	0.8	10.2	10.5	11.2	2.0
Robinson DS	ROBINS TB	60.3	1,932	26.3	22.5	13.7	12.2	1.9	2.2	17.4	18.1	16.8	1.6
Sumber Alfaria	AMRT IJ	525.0	1,680	34.2	26.1	9.2	8.5	0.7	1.0	13.2	14.0	27.5	1.2
Mitra Adiperkasa	MAPI IJ	4,690.0	600	43.9	23.2	9.3	7.8	0.1	0.3	5.9	9.7	128.9	0.3
Ramayana	RALS IJ	1,140.0	623	21.2	18.1	11.4	9.9	2.3	2.5	10.5	11.1	12.9	1.6
Simple average			-	27.5	21.9	13.8	12.2	1.7	2.0	30.3	27.0	27.1	1.8
Mkt cap wtd avg			30,518	25.0	21.5	15.3	13.7	2.2	2.5	19.6	19.7	14.6	2.1
Blended													
Simple average			-	29.7	24.4	15.0	13.1	1.8	2.1	30.7	29.1	22.7	1.8
Mkt cap wtd avg			57,017	28.1	24.2	16.4	14.8	2.2	2.4	37.7	34.9	15.4	2.1

Source: Bloomberg, Maybank KE ^3-year EPS CARG from CY15-18 *Closing price on 29 Sep 2016

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