

Singapore Consumer

Loosening purse string

SINGAPORE | CONSUMER | UPDATE

- Retail outlook brighten, expect to turnaround in near term on the back of higher demand and favourable employment condition
- Renewed optimism on a better prospect of Singapore economy will lift consumer sentiment; while growing household net worth encourage consumers to spend
- Indicators showed that: (i) Consumers are spending more on Food & Beverages and dining out more often; (ii) consumer preference shift back to Supermarkets; and (iii) potential recovery in luxury goods
- Earnings to drive share price; waiting for more evidence of economy growth trends and improved profits to catch up with the valuation
- We have an “Overweight” view on Singapore Consumer Sector

Singapore consumers were pessimistic on dim economy prospects in the past year amid global economic uncertainties. Consumers’ main concern was that slower growth would translate into rising unemployment and future income. Both FTSE Straits Times Consumer Goods Index and FTSE Straits Times Consumer Services Index underperformed the Straits Times Index over the past 1-year.

How do we view this?

Although there are still lingering uncertainties in view of the future US economic policies under new administration, as well as political uncertainties in the euro area, we think that retail sales will rebound in near term.

- We see green shoots of recovery in Singapore economy. Improving Goods Producing Industries will lift GDP growth.
- Brighter prospects on Singapore economy would lift consumer sentiment; while wealth effect from increasing household net worth would spur spending.
- With higher wages and stable unemployment rate, consumers have higher purchasing power.
- Positive signals:** Consumers are spending more on Food and Beverages, dining out more often, supermarket and luxury spendings showed signs of recovery.

Investment actions

We have an overweight view on Singapore Consumer Sector, on the brighter Singapore economy outlook and in anticipation of improved consumer sentiment.

Consumer Staples

Resilient earnings supported by domestic demand.

We have an ‘Accumulate’ rating on **Sheng Siong (TP: S\$1.06)** and a ‘Buy’ rating on **Old Chang Kee (TP: S\$0.98)**. Both companies are expanding their store counts, reaping benefits from economies scale and improved operating efficiencies via automation and utilization of their central warehouse/kitchen.

Consumer Cyclical

The upticks in luxury goods sales could imply a broader recovery in cyclical sector.

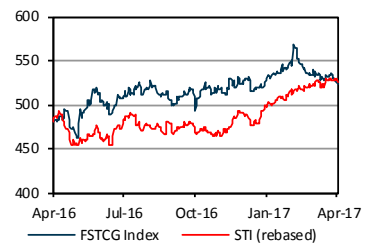
13 April 2017

Overweight

INDEX PERFORMANCE (%)

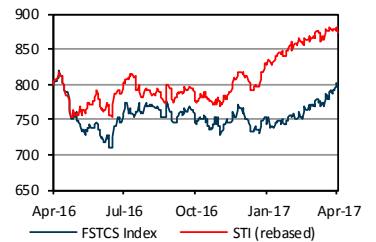
	1M TH	3M TH	1YR
FSTACG RETURN	(14)	0.1	14.3
FSTACS RETURN	4.1	7.8	6.3
STI RETURN	188	6.92	17.81

FSTCG VS. STI



Source: Bloomberg, PSR

FSTCS VS. STI



Source: Bloomberg, PSR

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Growing optimism over economic outlook to fuel spending

Singapore's small, open economy made it vulnerable to external factors, particularly demand shock due to the slowdown in global growth or any decline in global trade, and financial shock. It was the first country in East Asia to slip into recession following the 2007-08 global financial crisis.

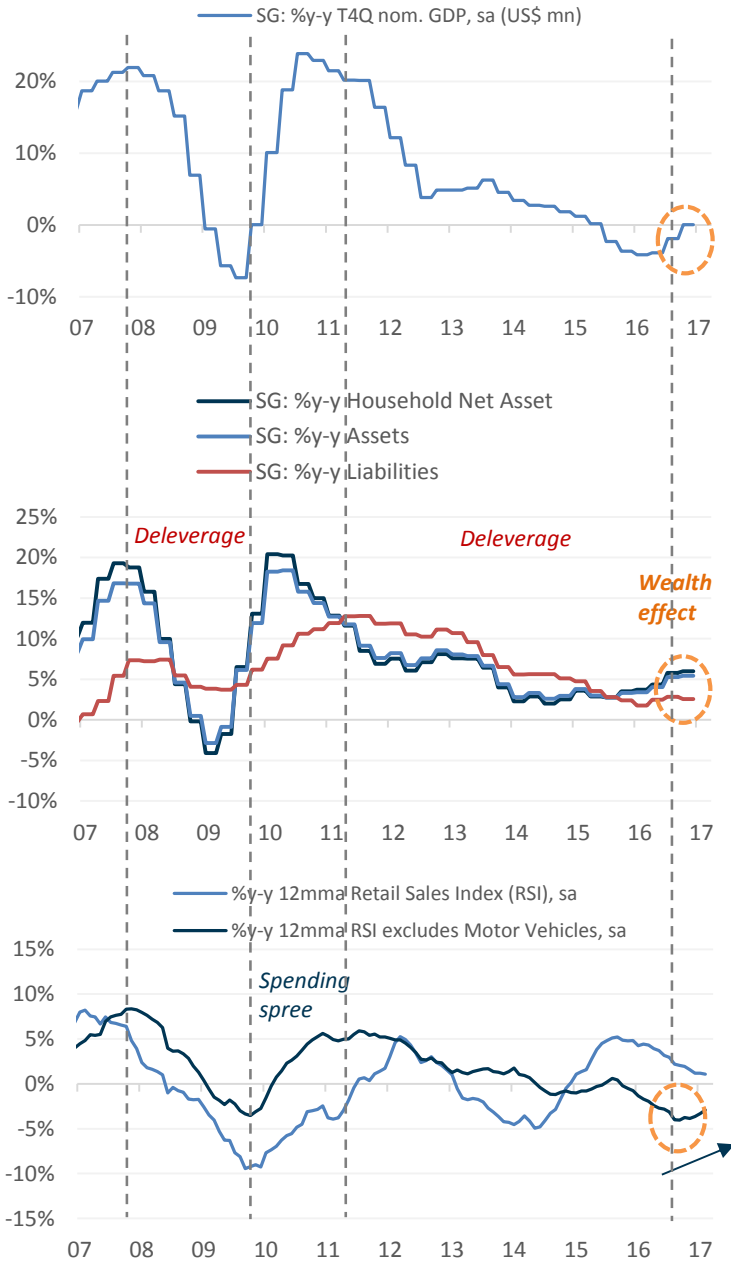
As Singapore economy slowed down from its peak in end-2007, retail sales started to decline. Refer to **Figure 1**, during the period of end-2007 to end-2009, Singapore had also gone through deleveraging as households borrowed less.

Singapore had maintained a stable near-zero interest rate in the period between 2009 and 2014, following the US Federal Reserve's policy. Such low interest rate environment spur spending and borrowing. Singapore economy reacted positively to the monetary easing. Retail sales rebounded by end-2009 after Singapore economy showed clearer sign of bottoming out.

However, the upward momentum was staggered by European debt crisis in 2011, where retail sales started to slowdown following the sluggish economy growth.

Singapore economy showed sign of bottoming up in late 2016. We think that retail sales should turnaround in near term. In addition, the growth of household assets outpaced the growth of loans in mid-2015 provides a second supporting signal for improving retail sales. *(We will further discuss on wealth effect later)*

Figure 1: GDP growth a leading indicator for retail sales



Source: CEIC, PSR

Note:

In 2007-08: Global financial crisis

End-2008: The US Federal Reserve cut interest rate to near zero

In 2011: European debt crisis

GDP growth gain momentum from robust growth in Manufacturing sector

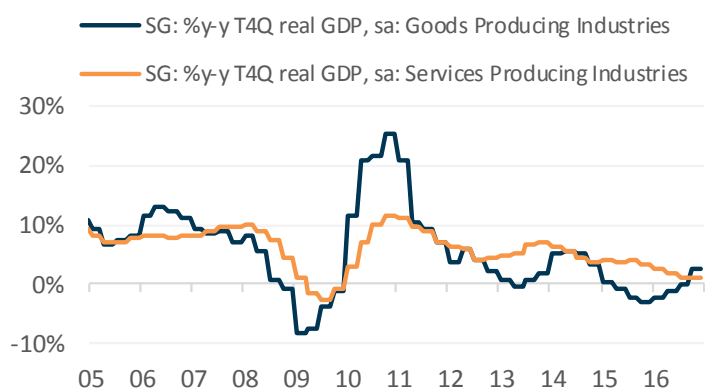
Services Producing Industries contributed c.67% to Singapore's 2016 GDP while Goods Producing Industries accounted for c.24% of it.

Growth in Services Producing Industries has slowed down since its peak of 11.7% in 2010 to 1.0% in 2016. However, we do not think that it will fall into contraction as Service Producing Industries are backed by resilient domestic demand. The sector went into slight contraction of -0.8% for a year only in 2009. And our current situation is nowhere near 2007-08 global financial crisis as global economy outlook brightens. The International Monetary Fund is looking to revise its forecasts for 2017 and 2018 global economy growth as it is now more upbeat for the global economy outlook this year and next than in 2016. On the same note, Singapore economic growth is expected benefit from the ripple effects of higher external demand, rebounding global commodity prices and domestic reforms within the region.

On the other hand, Goods Producing Industries had made a strong recovery in the 4Q2016. It expanded 8% yoy in 4Q2016 after five consecutive contractionary quarters from 4Q14 to 4Q15, and moderate growth at less than 2% between 1Q16 to 3Q16.

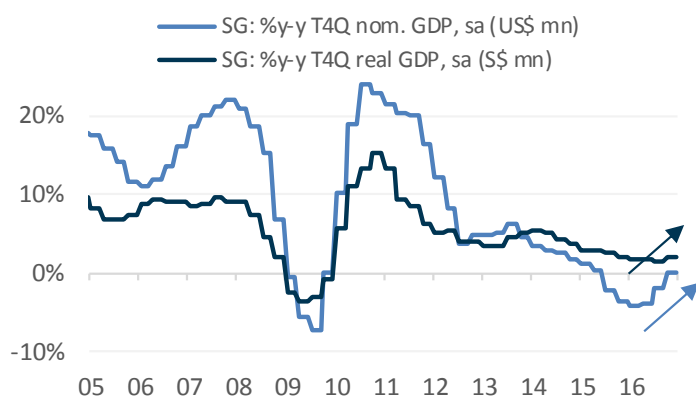
The improving Goods Producing Industries alongside a resilient Services Producing Industries signal a pick-up in economic growth in near term.

Figure 2: Goods Producing Industries rebounded to 2.8% yoy growth in 2016 vs -3.1% in 2015



Source: CEIC, PSR

Figure 3: Singapore GDP growth to gain momentum



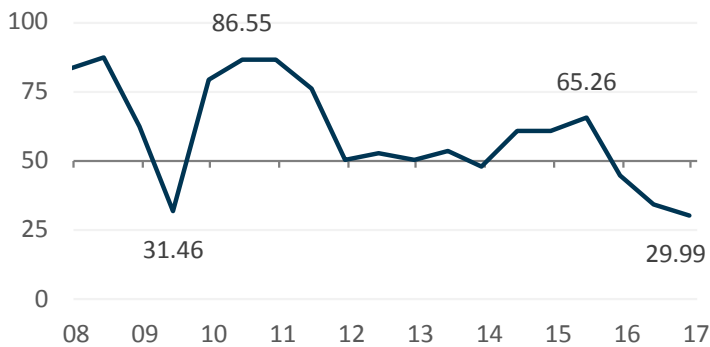
Source: CEIC, PSR

Renewed optimism to lift consumer confidence

The semi-annual MasterCard Asia Pacific Consumer Confidence survey was based on a scale of 0 to 100, with zero being the most pessimistic and 100 being the most optimistic. Index numbers between 40 and 60 were viewed as neutral.

The latest survey was based on 2H 2016. Singapore economy pick up pace in 4Q16, which we do not think that consumers have price in during the survey. We believe that the stronger economic indicators (as mentioned above) signal a brighter prospect of Singapore economy. And this will translate to an improved consumer sentiment, which will fuel private expenditures.

Figure 4: Singapore MasterCard Asia Pacific Consumer Confidence at pessimistic level 2H 2016; but likely to bottom out soon



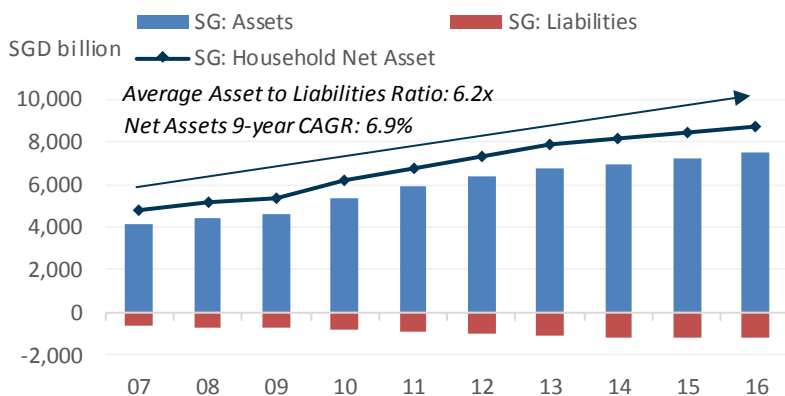
Source: Bloomberg

Feeling wealthy

Singapore’s nominal GDP grew at a compounded annual growth rate (CAGR) of 5.7% between 2007 to 2016, while the net assets of Singapore households grew at 6.9%.

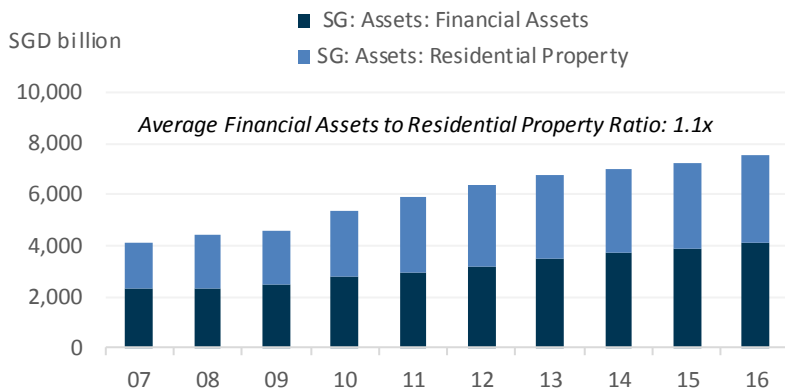
Household liabilities grew at a slightly faster pace than household assets’. Household liabilities grew at a CAGR of 6.7% as compared to household assets’ 6.5% in the same period.

Figure 5: Growing household net worth induces household spending



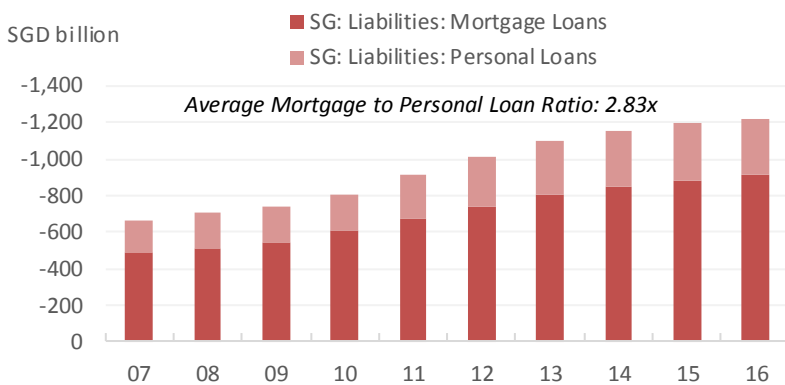
Source: CEIC, PSR

Figure 6: Household Assets comprises two components, i.e. Financial Assets and Residential Property



Source: CEIC, PSR

Figure 7: Household Liabilities comprises two components, i.e. Mortgage Loans and Personal Loans

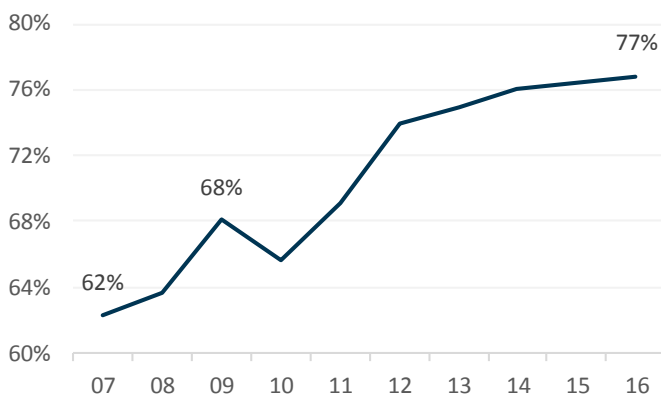


Source: CEIC, PSR

Household debt has increased from 62% of Singapore GDP in 2007 to 77% in 2016. While the figure is alarming when compared to Euro’s 58% and China’s 43%, but it is close to US’ 79% (source: tradingeconomics.com).

In addition, the debts are backed by assets which are unlikely to experience a sharp decrease in their value. Household debt to assets ratio stabled at 16% while currency and deposits, Central Provident Fund and Residential Property account for 83% of 2016 household assets.

Figure 8: Singapore household debt to GDP growing dramatically since 2011 due to low interest rate environment

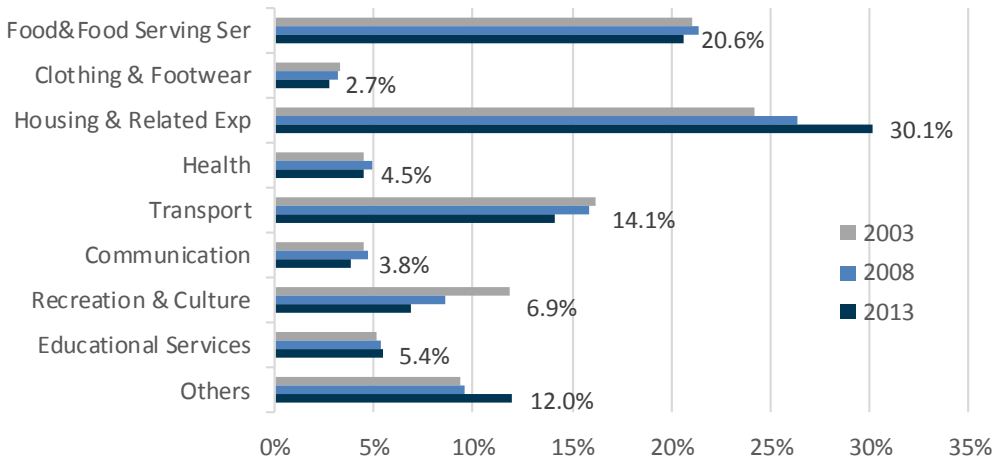


Source: CEIC, PSR

What are Singaporeans spending on?

A typical Singaporean household spends the most on Housing, Food and Transport (c.65% of 2013 total household expenditure).

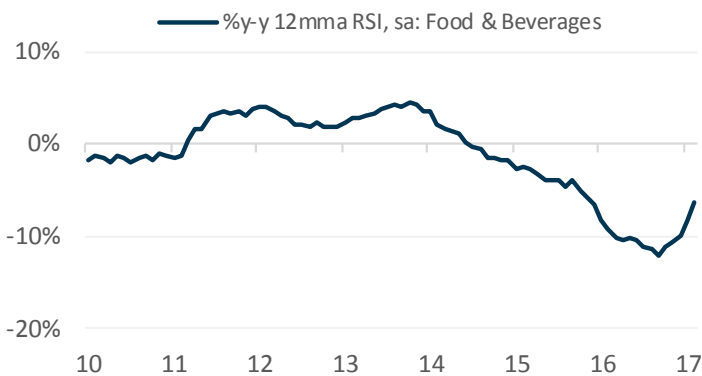
Figure 9: Distribution of Monthly Household Expenditure



Source: CEIC, PSR

Spending more on Food & Beverages and dining out more often

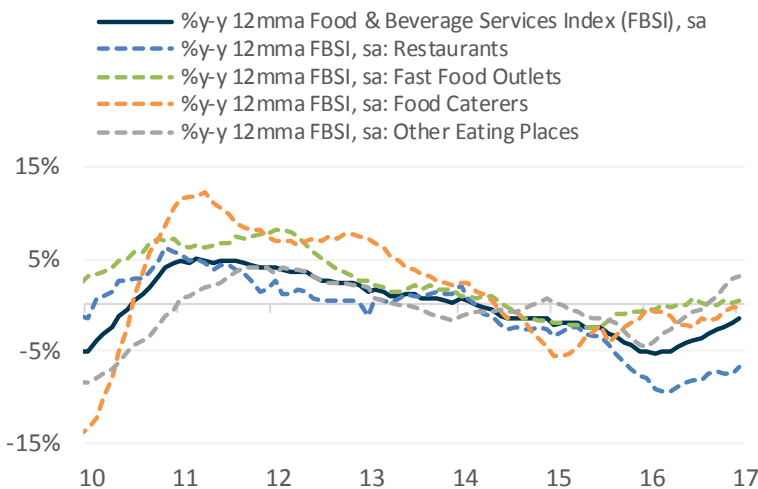
Figure 10: Retail Sales Index: Food & Beverages turned around



Retails Sales sub-index for Food & Beverages points to a broader recovery in Singapore economy.

Singaporeans are more willing to spend more on Food & Beverages – which could be in terms of volume and/or value (price point)

Figure 11: Food and Beverages Services Index and all Sub-indices bottoming out

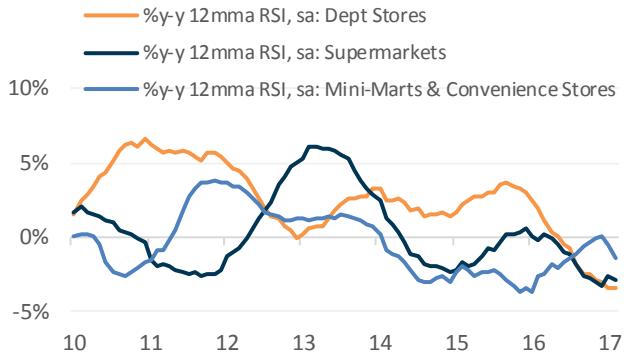


F&B Services sub-index for Restaurants, which is most sensitive to economic climate, is gaining traction, underscoring that consumers are more upbeat of their future income.

Source: CEIC, PSR

Re-visiting supermarkets

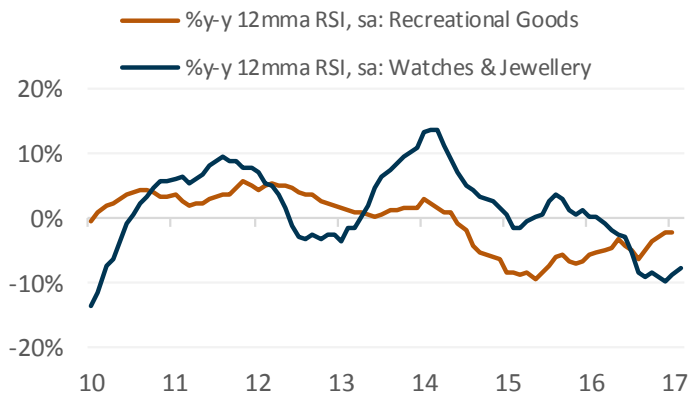
Figure 12: Sign of consumers preferring Supermarkets over Mini-Marts & Convenience Stores



Consumers tend to reduce their number of trips to the supermarkets during lacklustre economic climate, as it requires more money and travel time compared to mini-marts. Mini-marts are located within housing estates and near to home.

An uptick in cyclical expenditures

Figure 13: Sign of luxury goods recovery



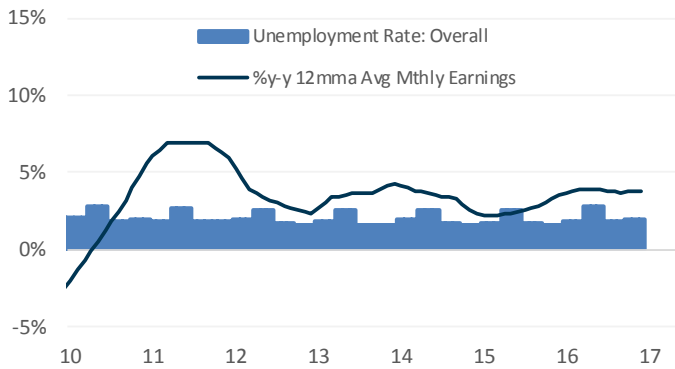
Both Cyclical Goods sub-indices are gaining traction, implying a renewed interest in international travel and frivolous purchases on the back of better economy prospect.

Purchasing power of Consumers and Costs

Employment and wages

Unemployment rate to remain stable and low at c. 2%. The tight labour market should underpin wage growth and thus supports our view on higher household spending in 2017.

Figure 14: Unemployment rate and wage growth



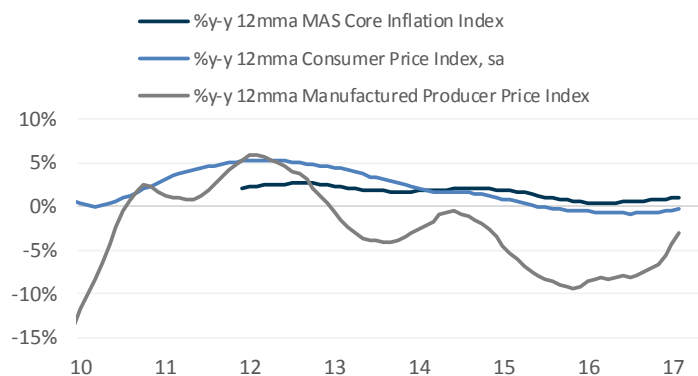
Source, CEIC, PSR

Inflation

Inflation remains muted in near term, however wholesale prices are at an upward trend. If the growth in wholesale prices accelerates, we may see higher retailing prices by end of the year. However, fiercer competition could limit the magnitude of costs businesses pass to consumers. This would imply that retailers may need to absorb the additional costs and embrace margin compression.

On the other hand, there are signs that pressure from labour costs to ease, while lower rental expenses could help to reduce operating expenses.

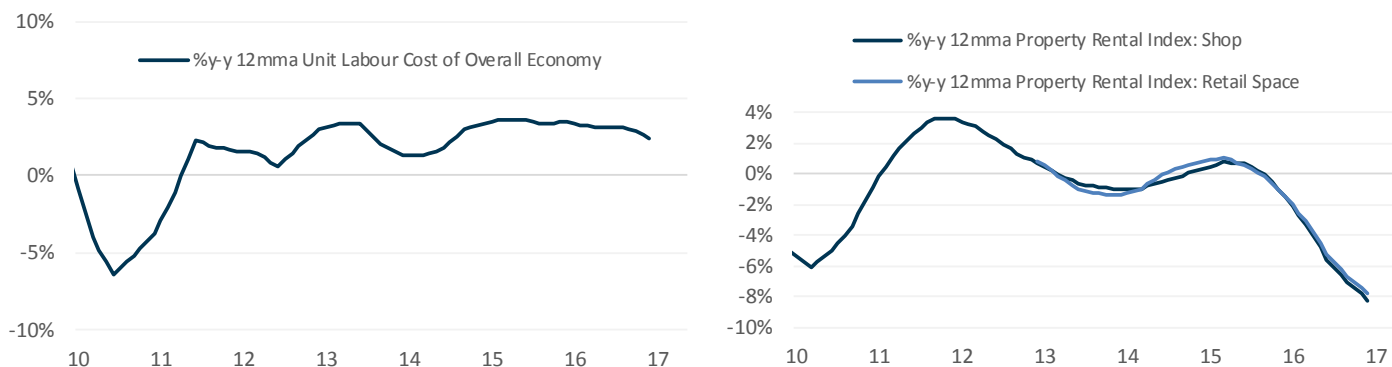
Figure 15: Rising costs at factory gate may translate to higher retailing price



Source: CEIC, PSR

Manufactured Producer Price Index is a leading indicator for Consumer Price Index.

The uptick may be driven by higher global oil prices.

Figure 16 & 17: Operating expenses to counterbalance higher input costs


Source: CEIC, PSR

Sharp interest rate hikes could dampen retail sentiment

Recall our house view that [the US Fed is behind the curve of raising interest rate](#), and interest rate hike to be steep instead the expected gradual rise. This is supported by the recent increase in US inflation rates and pickup in US economy growth, which could accelerate the tightening cycle for interest rates.

(a) FX risk

Higher US interest rates may cause capital outflows, which could in turn weaken local currency. But central bank and government had prepared to contain pressures on exchange rates and consumer prices. The Monetary Authority of Singapore (MAS) maintained its neutral policy stance of zero per cent appreciation of the S\$NEER (Singapore dollar nominal effective exchange rate) for an “extended period”.

(b) Credit implications, burden to service debts

As mentioned earlier, household leverage has increased in recent years, but we think the risk should be contained by favourable growth and employment conditions.

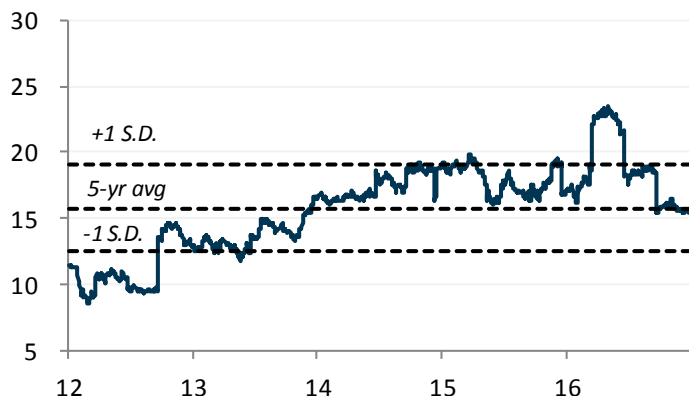
Emerging trends

- **E-commerce:** Sales via online/mobile app grow, but more e-commerce businesses are setting up physical locations. infrastructure for warehousing, for supply and logistics
- **Cashless payment system:** Digital eco-system created by ez-link, NETS, Apple Pay, Samsung Pay, etc, enables consumers to make payment through NFC (Near-field Communication)
- **Raising health awareness:** Bottled water has becoming more popular than soda; Food source tracing (integrity, safety and quality of food supply chains) has also becoming more important
- **Need for innovation amid competition and rising costs:** More automation or adoption of manpower-lean strategy to boost productivity while reducing labour costs, and thus increase operating efficiency. E.g. central kitchen, food vending machines, self-payment kiosk
- **Ageing population:** Silver economy with technologies to support elderly people in their daily living

Earnings to drive share price

We believe that we are now at a phase where investors are waiting for more clarity about economic growth trends and corporate earnings – if the economy and profits can catch up with the valuation.

Figure 18: 5-year historical PE of FTSE ST Consumer Goods Index



Source, Bloomberg, PSR

Figure 19: 5-year historical PE of FTSE ST Consumer Services Index

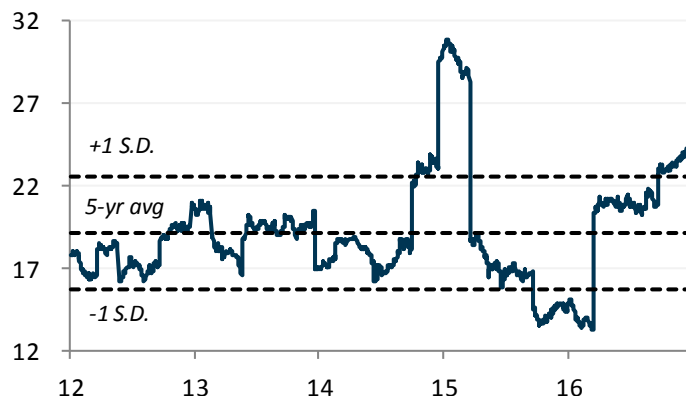


Figure 20: Consumers Sectors Top 10 Market Cap and PSR Ratings

Company	CIGS Industry	Mkt Cap (SGD mn)	Price (\$S)	PSR Rating	PSR Target		1-Yr Total Return (%)	1-Yr EPS Growth (%)	Div. Yield (%)	EV/EBITDA TTM	EBITDA Margin	P/E	P/B	Net D/E (%)	ROA (%)	ROE (%)
					Price (\$S)	1-Yr Total Return (%)										
Consumer Staples (Top 10 Highest Market Cap)																
Wilmar International Ltd	Food Products	22,124.2	3.50				5.7	-4.3	1.9	14.2	5.6%	16.3	1.1	83.2	2.6	6.7
Olam International Ltd	Food & Staples Retailing	5,214.5	1.91				17.7	539.4	3.1	15.4	6.5%	16.6	1.2	204.6	1.6	7.5
Golden Agri-Resources Ltd	Food Products	4,584.5	0.36				-8.8	3,825.0	1.7	11.2	7.9%	8.2	0.8	62.5	4.9	10.3
Fraser and Neave Ltd	Beverages	3,385.9	2.34	Reduce	1.80		19.9	-83.0	1.9	17.8	9.3%	32.2	1.3	Net Cash	3.0	4.0
First Resources Ltd	Food Products	2,898.9	1.83				-4.3	16.2	1.6	9.3	46.0%	16.6	2.4	36.7	6.9	13.4
Sheng Siong Group Ltd	Food & Staples Retailing	1,488.5	0.99	Accumulate	1.06		20.2	10.3	3.8	15.1	11.3%	23.8	5.9	Net Cash	16.6	25.2
Super Group Ltd/Singapore	Food Products	1,443.0	1.30				33.6	-6.1	1.7	15.2	15.9%	32.5	2.7	Net Cash	6.2	8.3
Japfa Ltd	Food Products	1,423.8	0.81				37.4	83.4	1.2	5.4	12.7%	8.8	1.6	46.7	5.0	21.4
Delfi Ltd	Food Products	1,375.1	2.25				-13.7	71.2	1.4	18.1	12.7%	37.7	4.9	Net Cash	7.2	11.8
Yeo Hiap Seng Ltd	Food Products	794.3	1.38				8.2	-21.6	1.5	15.2	11.0%	27.4	1.2	Net Cash	3.9	4.5
Consumer Staples (Small Cap)																
Old Chang Kee Ltd	Food Products	103.2	0.85	Buy	0.98		36.2	-5.7	3.5	6.6	15.8%	21.5	3.3	Net Cash	9.1	14.6
Simple Average							13.8	402.2	2.1	13.0	14.1%	22.0	2.4	86.7	6.1	11.6

Source: Bloomberg, Phillip Securities Research (Singapore) Estimates

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