

Consumer Sector

(Neutral)

“Cautiously Optimistic”

Some consumer stocks under our coverage delivered soft performance in 1H15 corporate earnings season, hammered by below expectation of 2Q15 performance. Issues such as higher cost of living and depreciation of the Ringgit continued to weigh on the consumer sector. We foresee Malaysian consumer will face a number of challenges this year due to the rising cost of living. This is due to the impact of GST implementation in April 2015 and uncertain economic outlook. We maintain a Neutral call on the sector.

F&B sector. Overall, F&B consumer stocks under our coverage (Nestle, Dutch Lady and MSM) reported earnings in line with ours and consensus estimate for 1H15 respectively. Nestle recorded a net profit that grew by 3.2% y-o-y to RM311 million in 6M15 while Dutch Lady's net profit jumped by 39% y-o-y to reach RM66 million in 6M15 (+39% y-o-y) and finally, MSM 6M15 net profit gained by 11% y-o-y to RM150 million (+11% y-o-y). The positive earnings growth was pushed by lower raw material prices (e.g. CPO, sugar, milk and coffee bean) and aggressive promotional and marketing activities taken by all.

Retail sector. Retail stocks under our coverage including Padini, Parkson and Amway reported earnings that fell below ours and consensus estimates in 2Q15 led by Padini's PAT that tumbled by 12% y-o-y to RM91 million while Parkson made a net loss of RM17 million. In the meantime, Amway recorded 6M14 of RM47 million, that dropped by 9% y-o-y compared to 6M14. The disappointing Padini, Parkson and Amway performance was derailed by the pullback in spending in retail industry as consumers became more selective in their spending due to higher cost of living and depreciating of the RM against USD.

In summary, the consumers sector has shown 2 different speed of growth as aforementioned. Outlook wise, we don't expect much difference in 2016 with consumers predicted to be cautious in their spending whilst commodity prices are expected to remain soft due to exogenous factors.

Malaysia consumer confidence index. Consumer confidence index in Malaysia has shown a deceleration in momentum to 71.7 points in 2Q15 from 72.60 points in 1Q15, a 1.2% q-o-q drop. The lower consumer confidence index in 2Q15 was mainly impacted by higher cost of living due to the implementation of GST in April 2014 and also aided by uncertain economic outlook. Therefore, consumers have changed their spending habits and this has given some negative effect to the consumers' player (F&B and retail industry). With not much change in the outlook, we expect the Malaysian consumer confidence index to continue to be soft in the next few quarters.

RM vs. USD. Ringgit has depreciated by 13% y-o-y in 6M15 against USD (6M15: RM3.77 per Dollar vs. 6M14: RM3.21 per Dollar). The depreciation of Ringgit against USD would likely affect consumer sector players particularly for the import cost of their raw material or products. Of note, Amway gross profit margin has narrowed by 50bps to 26% in 6M15 (6M14's GP margin: 31%), pressurised by higher importation cost (70% of products imported). In sum, the cost of their products importation will be higher due to weakening of Ringgit and this will like impact Amway's product price directly. If this remains, we believe consumer will shift their consumption to cheaper product and this situation will give impact to Amway's earnings performance for the next few quarters.

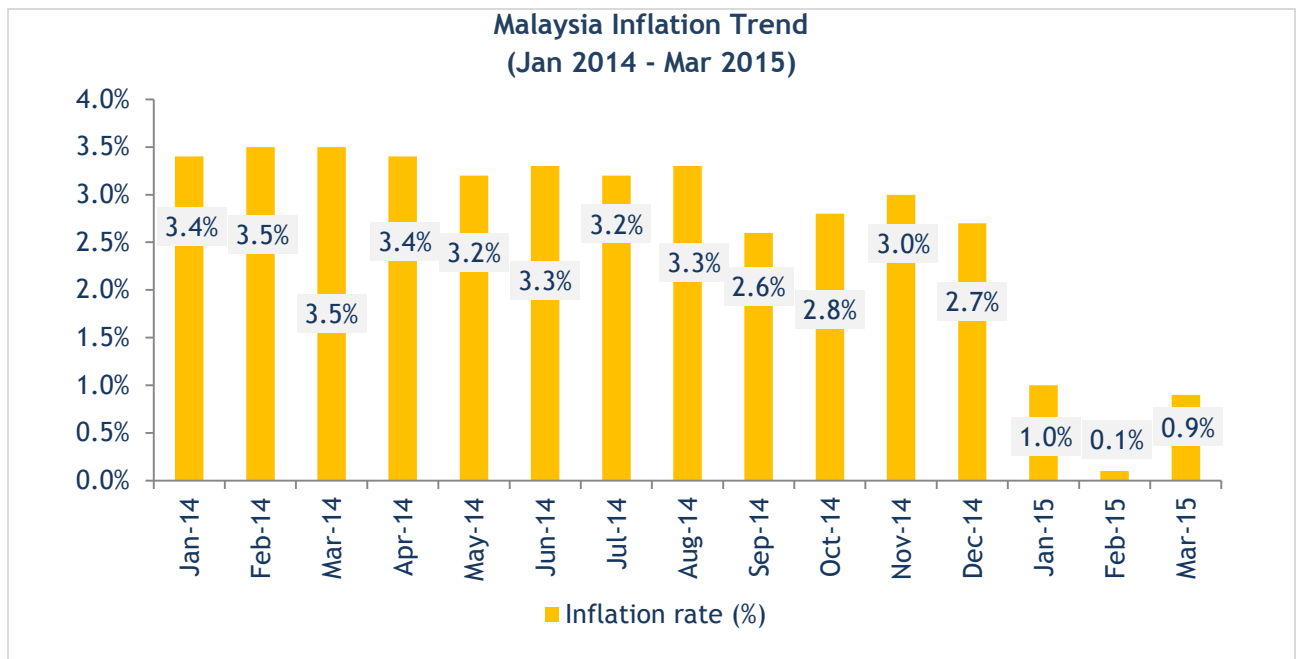
Commodity price. The lower commodity prices in 2Q15 have given positive impact to earnings of the F&B sector players under our coverage, such as Dutch Lady, Nestle and MSM. Weakening commodity price has pushed Dutch Lady's gross profit margin to reach 40% in 6M15 compared to 33% in 6M14 (+70% bps) while Nestle's and MSM's gross profit margin have been lifted to 39% and 25% in 6M15 respectively (6M14: Nestle 35%; MSM 21%) due to the same reason. Of note, commodity prices had shown declining trend in this quarter compared to 2Q14. This includes commodity prices for CPO that declined by 9% y-o-y, sugar (-26% y-o-y), and milk that fell by 39% y-o-y. In addition, Arabica and Robusta coffee prices have also shown a downtrend which declined by 24% y-o-y and 6% y-o-y respectively. We expect commodity prices will be soft for the few next quarters thanks to China's increasing downside risk to growth and also due to the US impending interest rate adjustment. Notably, this will give positive impact to the F&B players' earnings in the next few quarters.

Outlook. We foresee the outlook for F&B and retails sector remain challenging in 2H15 due to 1) higher cost of living due to GST implementation, 2) depreciation of Ringgit against USD, and 3) weakening in consumer spending as consumers become selective in their spending habit. Nonetheless, seasonality factor will continue support the sector thanks to 2H15 festivities and year-end holiday and sale (e.g. Deepavali, Christmas and school break season). Given the factors that may continue weigh on the sector, we maintain a **NEUTRAL** call on the sector with Zhulian (BUY; TP: RM1.80) emerges as our top pick.

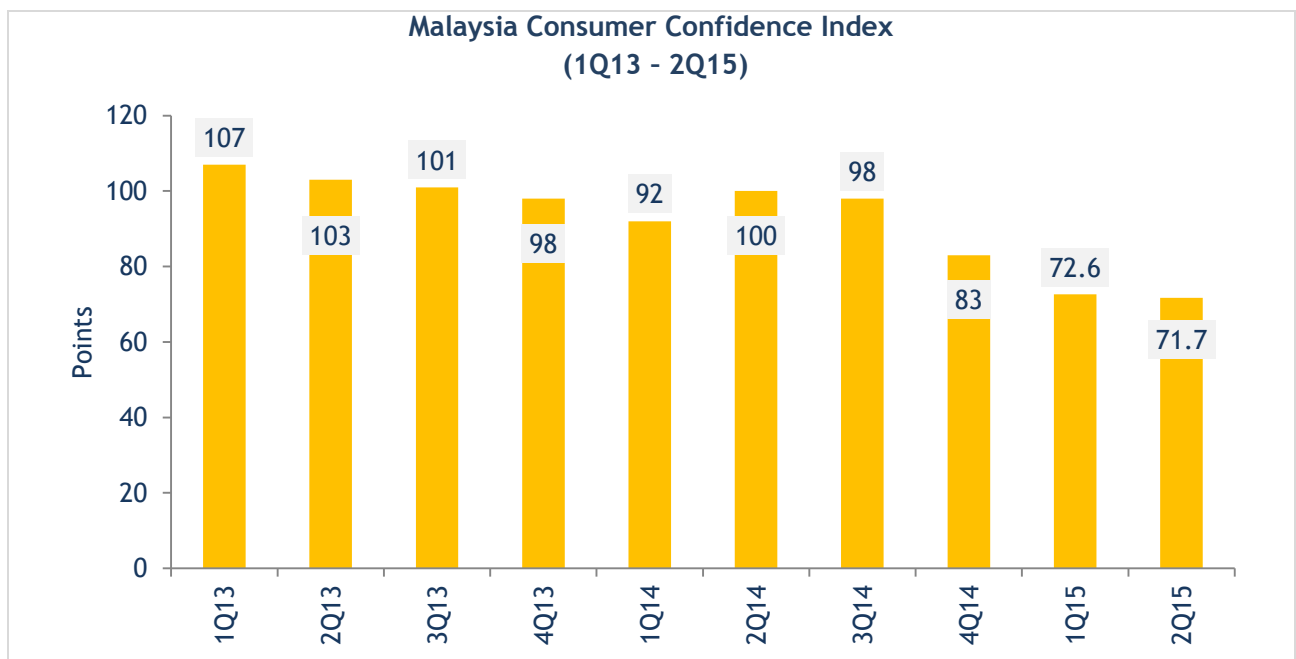
Table 2: Peers comparison (Calenderised)

Company	YE	Price (RM)	EPS (sen)		P/E (X)		P/BV (X)		ROE (%)	DY (%)	TP (RM)	Call
			FY15	FY16	FY14	FY15	FY15	FY16				
Parkson*	Jun	1.01	17	19	17	16	1	1	5	NA	1.20	Buy
Amway	Dec	9.80	69	73	17	16	9	8	55	3.4	10.50	Hold
Nestle	Dec	71.90	254	277	27	24	18	18	58	3.5	59.30	Sell
MSM	Dec	4.94	34	38	14	13	2	2	13	5.1	5.46	Hold
Dutch Lady	Dec	47.00	216	229	22	20	14	16	58	2.4	41.60	Sell
Padini*	Jun	1.38	15	18	13	11	3	3	24	5.0	1.45	Hold
Scientex	July	6.85	68	80	10	8	2	2	20	4.0	7.30	Hold
Zhulian	Nov	1.54	11	33	10	6	2	2	10	5.1	1.80	Buy
Aeon Co	Dec	2.80	18	19	23	21	3	3	14	1.4	na	na
QL Resources	Mac	4.00	16	18	19	17	3	3	15	1.0	na	na
Average					18	15	5	5				

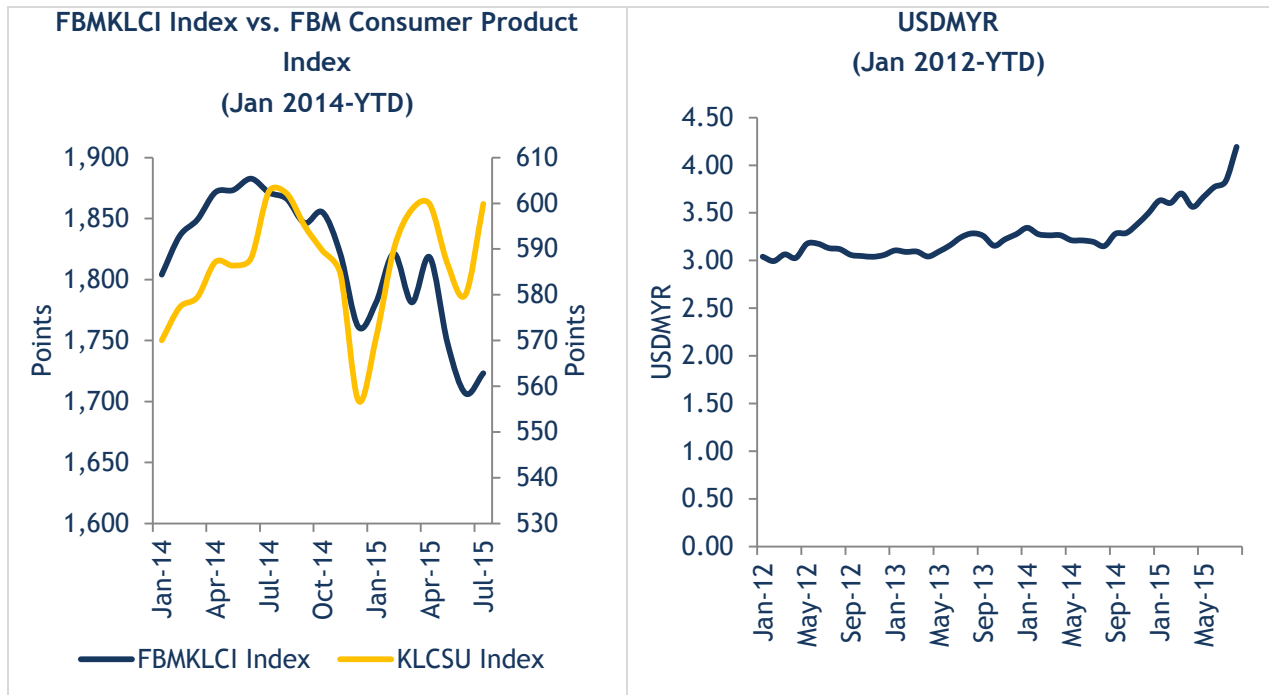
Source: Bloomberg, M&A Securities



Source: Department of Statistic Malaysia, M&A Securities

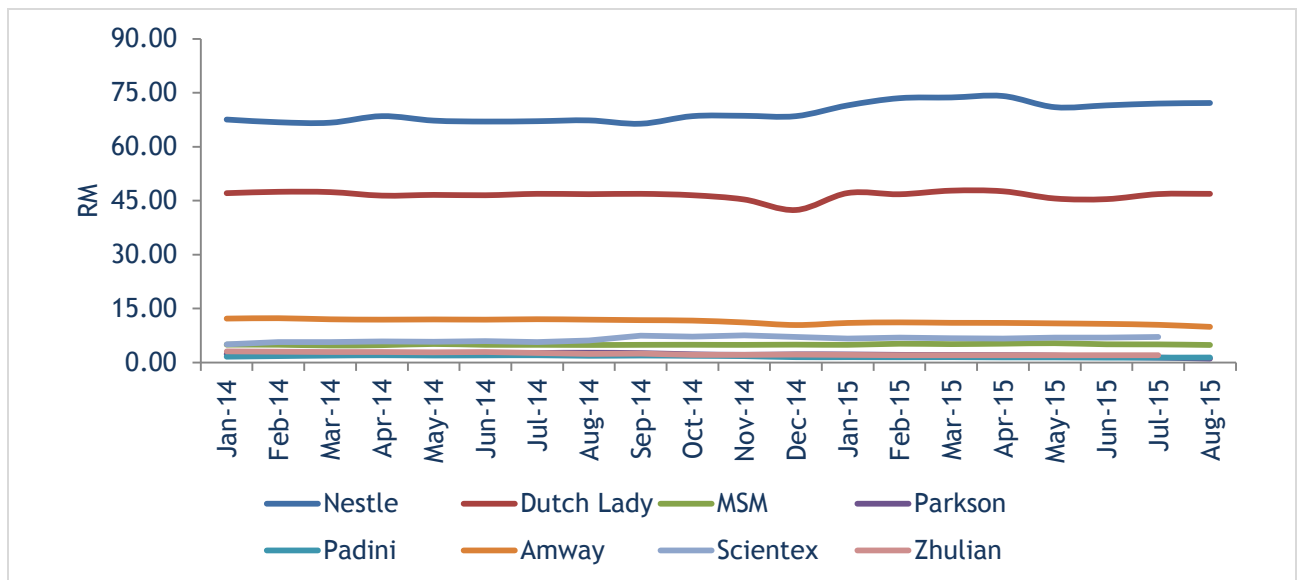


Source: Department of Statistic Malaysia, M&A Securities

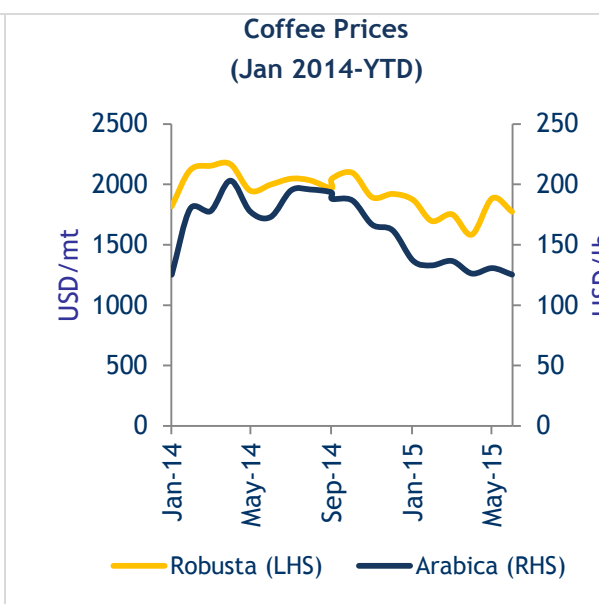
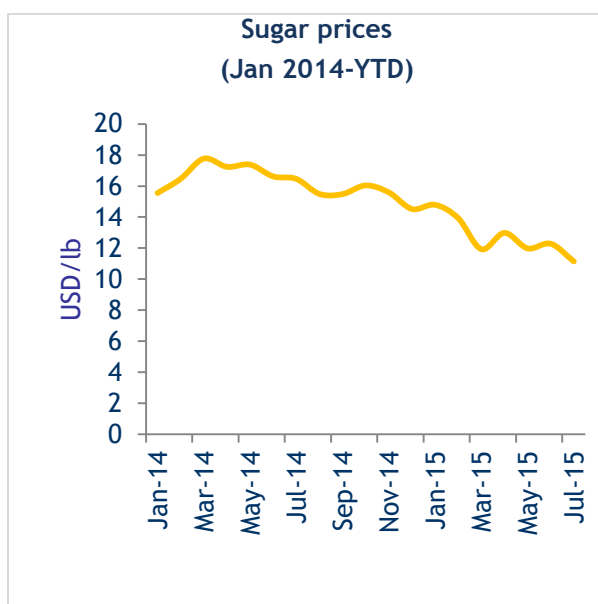
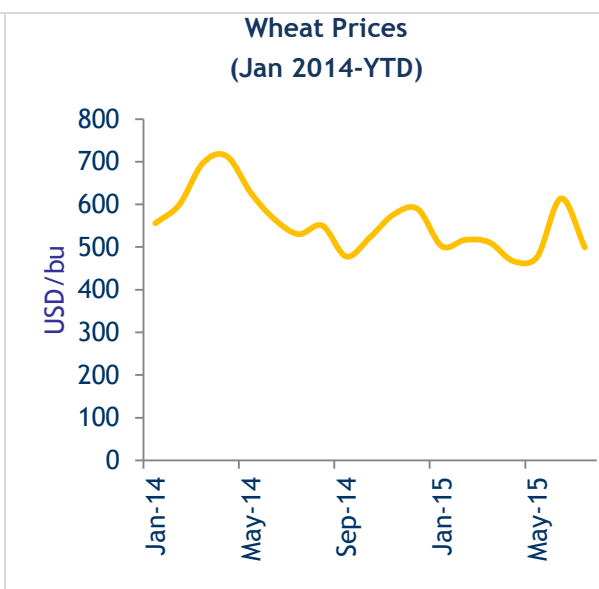
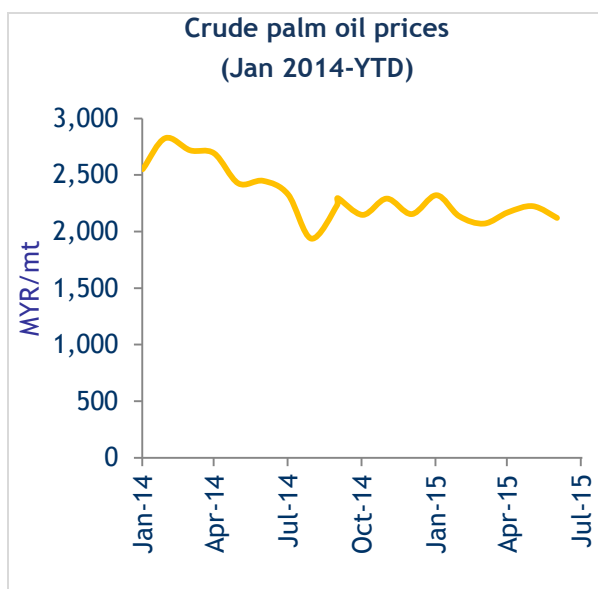
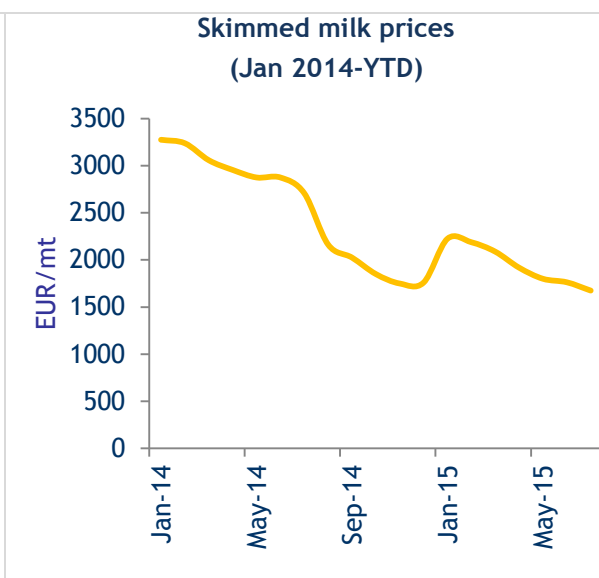
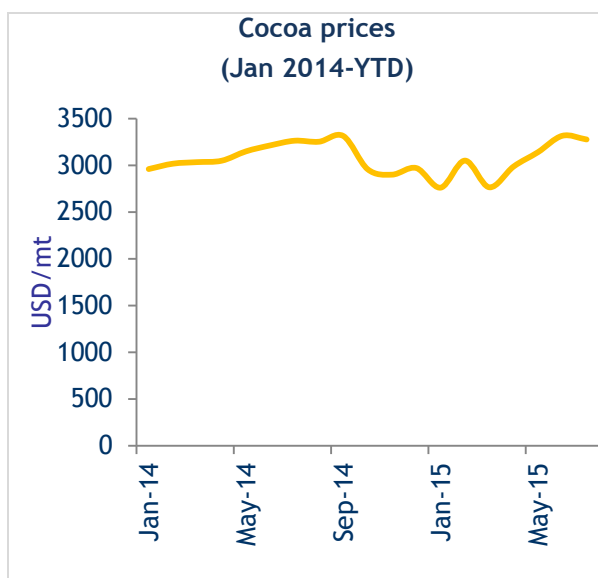


Source: Bloomberg, M&A Securities

Consumer Players Share Price Performance (Jan 2014-YTD)



Source: Bloomberg, M&A Securities



Source: Bursa Malaysia, M&A Securities

Research Team

research@mna.com.my

03-22821820 ext. 257, 229, 221, 249, 258

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

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M & A Securities Sdn Bhd (15017-H)

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A Participating Organisation of Bursa Malaysia Securities Berhad

Principal Office

Level 1,2,3 No.45-47 & 43-6

The Boulevard, Mid Valley City,

Lingkaran Syed Putra,

59200 Kuala Lumpur

Tel: +603 - 2282 1820 Fax: +603 - 2283 1893