

03 October 2024

## Consumer

### Retail Falters 1H, Eyes on Year-End Recovery

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## NEUTRAL



We maintain a NEUTRAL stance on the sector. Retail Group Malaysia (RGM) remains cautiously optimistic, projecting a 3.6% YoY growth for CY24, driven by increased tourism and civil servant salary hikes. However, consumer spending is likely to remain subdued due to the persistently high cost of living and the upcoming fuel subsidy rationalisation. That said, consumer sentiment could improve if Budget 2025 effectively addresses concerns over the subsidy plan. Additionally, the stronger MYR may ease these pressures by reducing fuel price increases and stabilising retail prices. Our sector top picks are F&N (OP; TP: RM38.25), MRDIY (OP; RM2.27) and KAREX (OP; RM1.12). Amid the strong MYR, those that may see more near-term uplift include MRDIY.

**Retail sales faltered in 2QCY24, cautious optimism for year-end boost.** RGM reported weaker-than-expected retail sales growth of 0.6% YoY in 2QCY24, missing the 1.7% target and a significant drop from the 7.8% growth seen in 1QCY24. The lower 2Q growth was largely due to softer festive sales, bringing the overall 1HCY24 retail growth to 4.6% YoY. Looking ahead, RGM expects retail sales to grow by 3.6% YoY in 3Q and 3.2% YoY in 4Q, while maintaining its full-year growth forecast of 3.6%. This outlook is supported by an expected rise in tourist arrivals from China and India, driven by the new visa-free entry policy. Additionally, the increase in civil servant salaries starting December 1 is likely to boost retail spending during the year-end holiday season. However, RGM remains cautious, as the rising cost of living and the prolonged conflict in the Middle-East may lead consumers to continue being cautious with their spending.

**Cautious sentiment persists but...** We share RGM's view and anticipate that consumer spending will remain muted throughout the rest of CY24 and potentially into early CY25, as many consumers are bracing for higher costs due to the upcoming fuel subsidy rationalisation. The expected reduction or elimination of fuel subsidies will likely lead to higher fuel prices, which will directly increase daily living costs, particularly for transportation. Additionally, we believe that the EPF Account 3 withdrawal scheme amounting to RM7.8b (as of June 2024) will have a limited effect on retail spending. The remaining funds available for withdrawal from this account are unlikely to significantly boost discretionary spending, especially for larger purchases or high-ticket items.

**...could ease following Budget 2025.** Despite the current subdued consumer sentiment, there is a possibility that the impact of fuel subsidy may not be as severe as expected. The recent strengthening of the MYR could help mitigate the impact of subsidy cuts, potentially lowering the expected increase in fuel costs and easing consumer concerns. With Budget 2025 to be tabled on 18 October, further details on fuel subsidy rationalisation could be revealed, addressing uncertainties around the timeline and magnitude of the changes. This could allow the financial impact to be eased gradually, and as financial pressures reduce and a perceived rise in purchasing power, consumers may be more inclined to spend on discretionary items, providing a lift to retail spending. We reckon consumer discretionary players like **MRDIY**, **PADINI (MP; RM3.24)** and **AEON (UP; RM1.21)** could stand to benefit from this potential boost in consumer confidence.

Additionally, a stronger MYR could lower the costs of imported raw materials, helping to ease the pressure from recent price increases in key commodities such as coffee and cocoa beans. This would reduce business costs, limiting the need for significant price hikes, contributing to stable retail prices. As a result, the financial burden on consumers would lessen, allowing them to maintain their purchasing power and support continued retail spending. We believe **MRDIY** is likely to be one of the key beneficiaries of the strengthening MYR, as it sources raw materials primarily from China at lower costs, while its sales (predominantly in MYR) remain unchanged.

**Price swings in commodities.** Prices of wheat, corn, soybean, cotton have dropped more than 10% YTD and are likely to remain soft due to strong global supply driven by abundant harvests in their major production regions. In contrast, prices of coffee and cocoa have surged 39% and 85%, respectively, on poor crop yields amidst severe weather events in their production areas such as Brazil, Southeast Asia and West Africa. Notably, sugar prices surged 27% in the past month due to concerns that ongoing drought in Brazil may reduce sugar production. Nevertheless, above-average monsoon rains in India and a weaker Brazilian real are expected to normalise prices. Additionally, the doubling of shipping costs as indicated by 100% YTD increase in the Shanghai Shipping index could put pressure on **PADINI** and **MRDIY**, both of which depend largely on importing goods from China.

**Valuation update:** Our earnings forecasts, valuation methodology, target prices, and ratings remain unchanged for the consumer sector portfolio, except for **NESTLE (OP; RM114.90)**, **PWROOT (MP; RM1.28)** and **QL (UP; RM4.20)**. While we maintain the earnings forecasts and TP for **NESTLE** and **PWROOT**, we upgrade **NESTLE** to OP (from UP) and **PWROOT** to MP (from UP) following the recent share price correction. Additionally, we adjust our TP for **QL** to RM4.20 (from RM6.25 previously) following its one-for-two bonus share issuance, while keeping our valuation basis unchanged. With that, we downgrade **QL** to UP (from MP) due to the recent surge in its share price.

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Our TP and recommendation for consumer stocks are summarised in Exhibit 2.

Our top picks for the sector are:

- **F&N** for: (i) its earnings defensiveness given the stable demand for essential food items despite high inflation and an uncertain global economic outlook, (ii) the rising popularity of ready-to-drink products where F&N has a strong presence, (iii) proxy to the recovery of domestic consumption and the return of tourists in Thailand, and (iv) its long-term growth prospects driven by its investment in a sizeable dairy farm in Gemas, Negeri Sembilan.
- **MRDIY** for: (i) its dominant position in Malaysia's home improvement market, (ii) its size that translates to strong bargaining position vs. its suppliers, and economies of scale, (iii) its ample headroom for growth in terms of store count, and (iv) its continued efforts to improve operational efficiency such as the introduction of an automated inventory system.
- **KAREX** for: (i) its leading market position and global reach in the rapidly growing condom industry, projected by industry experts (such as Global Market insights and Extrapolate) at a CAGR of 8% to 9% over the immediate term, (ii) its strong R&D and product innovation, (iii) its adherence to international standards and certifications, (iv) its strategic shift in moving up higher the value chain, and (v) growing preference for high quality innovative condom products.

### Exhibit 1: Raw Material / Commodities Price Trend

	Last Price @	Price Change					vs. 2023 average price	vs. 2022 average price	vs. 2021 average price	Future Price Trend*
	9/20/2024	1M	QTD	2QCY24	YTD					
Sugar (USD/lb)	22.4	27.2	10.0	-9.8	8.6	-7.2	18.7	25.1	↓	
Coffee (USD/lb)	261.7	6.4	14.3	10.8	39.0	52.5	22.2	54.7	↑	
Cocoa (USD/MT)	7,750.0	-15.5	0.3	-20.9	84.7	135.0	214.6	211.3	↑	
Milk (USD/MT)	3,448.0	5.8	1.6	8.0	7.5	11.9	-11.3	-10.3	↓	
Wheat (USD/MT)	383.7	1.6	-1.4	2.4	-10.0	-13.4	-37.6	-19.8	↓	
Corn (USD/Bushel)	335.0	1.9	-0.4	-7.8	-13.9	-27.1	-40.7	-28.7	↓	
Soybean (USD/Bushel)	1,017.8	6.3	-11.5	-3.4	-21.3	-27.8	-33.7	-25.7	↓	
CPO (RM/MT)	4,004.0	3.6	0.7	-8.1	9.3	5.0	-21.1	-9.0	↓	
Cotton (USD/lb)	71.6	5.3	2.5	-23.6	-11.6	-13.8	-36.3	-23.4	↓	
Aluminium (USD/MT)	2,544.6	4.7	2.2	8.0	8.2	12.3	-6.0	2.6	↑	
Baltic Dry Index	1,976.0	13.9	-3.6	12.6	-5.6	43.4	2.2	-32.9	↓	
WTI Crude Oil (USD/Barrel)	71.8	-3.0	-11.9	-2.0	0.2	-7.5	-23.9	5.5	↑	
Volatility Index	16.4	3.0	31.4	-4.4	31.3	-3.0	-36.2	-16.8		
Dollar Index	1,223.3	-0.5	-3.6	1.9	0.9	-1.3	-2.3	6.8	↑	
USDMYR	4.19	4.6	12.6	-0.2	-8.8	-8.3	-4.9	1.0	↑	
Shanghai Shipping Index	1,818.31	-15.0	-5.4	59.1	100.0	94.0	-34.2	-31.0		

Source: \*Trading Economics, Bloomberg, Kenanga Research

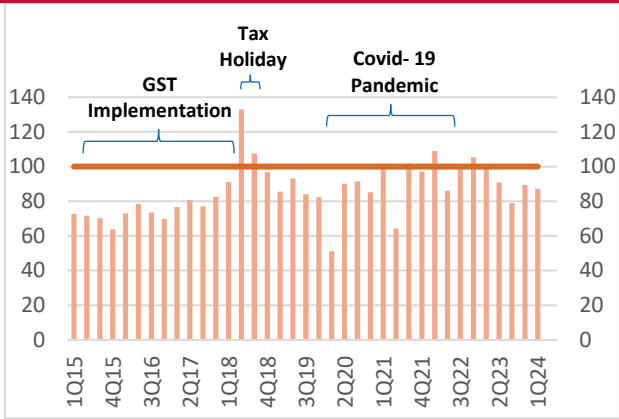
### Exhibit 2: Changes to TPs and Recommendations

Company	Target Price (RM)			Recommendation		
	After	Before	Chg	After	Before	Chg
AEON	1.21	1.21	↔	UP	UP	↔
F&N	38.25	38.25	↔	OP	OP	↔
MRDIY	2.27	2.27	↔	OP	OP	↔
NESTLE	114.90	114.90	↔	OP	UP	↑
PADINI	3.24	3.24	↔	MP	MP	↔
PWROOT	1.28	1.28	↔	MP	UP	↑
QL	4.20	6.25	↓	UP	MP	↓
KAREX	1.12	1.12	↔	OP	OP	↔

Source: Kenanga Research

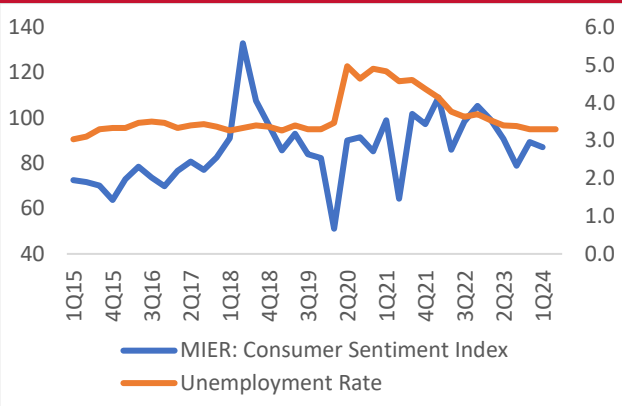
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Exhibit 3: MIER Consumer Sentiment Index



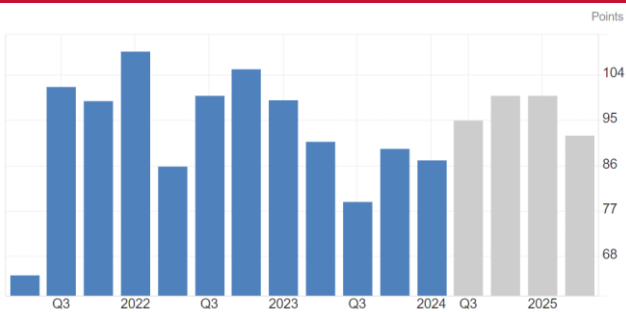
Source: MIER, Kenanga Research

Exhibit 4: Jobless Rate & Consumer Sentiment



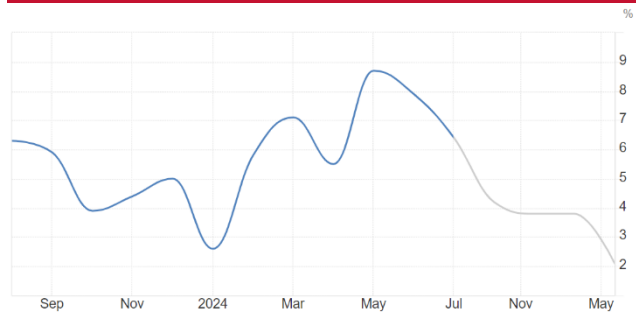
Source: DOSM, CEIC, Kenanga Research

Exhibit 5: Malaysia Consumer Confidence



Source: Trading Economics, Kenanga Research

Exhibit 6: Malaysia Retail Sales YoY Growth



Source: Trading Economics, Kenanga Research

Exhibit 7: Sugar Prices (USD/lb)



Source: Trading Economics, Kenanga Research

Exhibit 8: Coffee Prices (USD/lb)



Source: Trading Economics, Kenanga Research

Exhibit 9: Cocoa Prices (USD/MT)

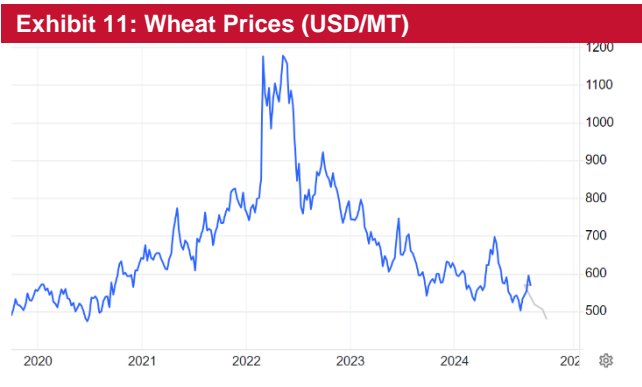


Source: Trading Economics, Kenanga Research

Exhibit 10: Milk Prices (USD/MT)



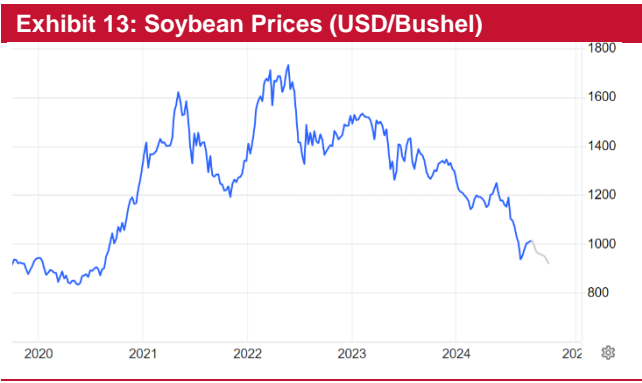
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Source: Trading Economics, Kenanga Research



Source: Trading Economics, Kenanga Research



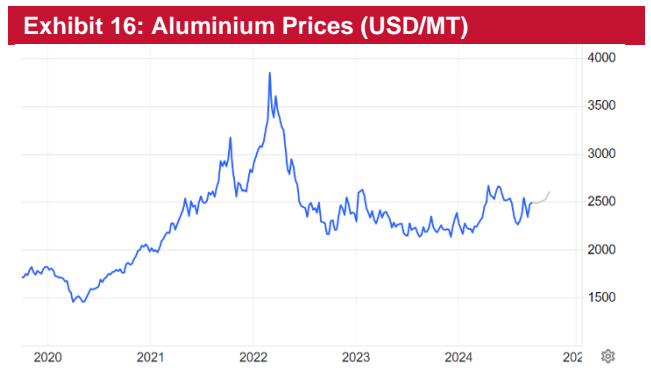
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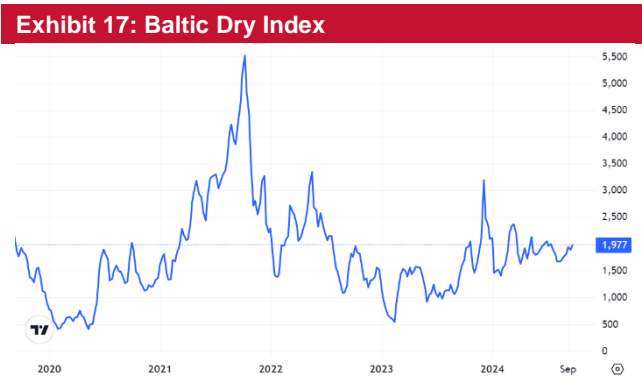
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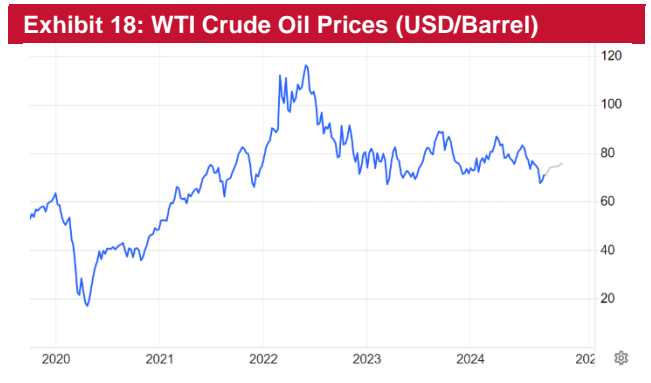
Source: Trading Economics, Kenanga Research



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## Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net Div. (sen)	Net Div. Yld. 1-Yr.
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.				
<b>CONSUMER</b>																	
AEON CO. (M) BHD	UP	1.47	1.21	-17.7%	2,063.9	Y	12/2024	8.8	9.0	8.0%	1.6%	16.6	16.4	1.1	6.6%	4.0	2.7%
FRASER & NEAVE HOLDINGS BHD	OP	31.50	38.25	21.4%	11,553.5	Y	09/2024	166.1	176.2	25.8%	6.1%	19.0	17.9	3.2	17.6%	85.0	2.7%
MR D.I.Y. GROUP (M) BHD	OP	2.05	2.27	10.7%	19,382.3	Y	12/2024	7.0	8.1	17.3%	16.8%	29.5	25.3	9.9	35.4%	5.0	2.4%
NESTLE (MALAYSIA) BHD	OP	105.50	114.90	8.9%	24,739.8	Y	12/2024	255.4	284.1	-9.2%	11.2%	41.3	37.1	36.0	87.9%	250.0	2.4%
PADINI HOLDINGS BHD	MP	3.55	3.24	-8.7%	2,335.6	Y	06/2025	24.0	30.7	7.8%	27.6%	14.8	11.6	2.0	13.7%	12.0	3.4%
POWER ROOT BHD	MP	1.40	1.28	-8.6%	621.2	Y	03/2025	8.0	9.2	-9.4%	14.1%	17.4	15.3	1.9	10.8%	7.0	5.0%
QL RESOURCES BHD	UP	4.70	4.20	-10.6%	17,150.9	Y	03/2025	13.0	13.8	8.8%	6.0%	36.0	34.0	5.2	16.1%	5.0	1.1%
KAREX BHD	OP	0.830	1.12	34.9%	874.4	Y	06/2025	4.2	4.8	87.6%	15.5%	19.9	17.2	1.7	8.9%	2.5	3.0%
<b>SECTOR AGGREGATE</b>					<b>78,721.6</b>					<b>9.6%</b>	<b>11.1%</b>	<b>29.1</b>	<b>26.2</b>	<b>5.8</b>	<b>20.0%</b>		<b>2.8%</b>

Source: Bloomberg, Kenanga Research

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**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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