SECTOR UPDATE

Consumer – Malaysia

Clouded Outlook

Mixed signals prevail as the steep minimum wage hike is offset by stronger spending; despite an uptick in commodities prices, margins appear intact for now. The sector offers a 2024/25 earnings growth at 4.6%/8.9% respectively, and valuations that are near -1.0SD to its five-year mean. However, the sector's defensiveness may translate to underperformance against the broader market. These confluences of factors underline our MARKET WEIGHT stance on the sector. Top picks: F&N and Mr DIY.

WHAT'S NEW

- **Bracing for increased wage-related costs.** We have factored in the minimum wage increase to RM1,700 and mandatory EPF contribution for foreigners, along with its potential ripple effect into our assumptions for the companies under our coverage. For key retailers such as MyNews, 99Speedmart, and Mr DIY, the potential impact on 2025 earnings could reach -11%, -7.4%, and -4.2% respectively, assuming no cost pass-through. However, a minimal ASP adjustment of 0.3%, 0.4%, and 0.6% respectively for these companies could offset the increased wage costs.

- **Other side of the coin to the minimum wage hike.** The increase in the minimum wage to RM1,700 and civil servant salary adjustments are expected to spread RM20.4b across 6.05m individuals. With the additional RM5b from the Employees Provident Fund (EPF) Account 3 withdrawal scheme, this significant boost to disposable income could drive household spending, especially among lower-income groups. Retailers like 99Speedmart and Mr DIY, which are popular among these consumers, stand to benefit. For perspective, Mr DIY reported a RM97m sales uplift during the RM44.6b EPF withdrawal scheme in 2022, underscoring the potential impact of this increased liquidity. Other retailers such as Aeon Co, Senheng New Retail, Padini Malaysia and MyNews could benefit as well.

ACTION

- **Maintain MARKET WEIGHT as sector faces mixed signals.** The minimum wage hike is a relatively steep quantum but the cost pass-through appears digestible. Increased wages should buffer consumer spending, more than offsetting the cost of subsidy rationalisation. Meanwhile, immediate downside risk to margins appears eased for the near term, with the recent ringgit strength and average commodities prices softer vis-à-vis 2023's average earlier in the year. While there is an absence of major headwinds, the sector lacks key catalysts. This is balanced by sector earnings growth of 4.6% and 8.9% in 2024 and 2025 respectively and sector valuations that are trading at one-year forward PE of 23.2x, close to -1.0SD to its five-year mean. Furthermore, given the overall defensiveness of the sector, it should underperform relative to the risk-on outlook of the broad market. This underlines our MARKET WEIGHT rating on the sector.

- **Top picks: F&N and Mr DIY; top SELL: Farm Fresh.** We have a preference for consumer staples with an element of discretionary that appeal to the lower middle-income segment of consumers given the enhanced resiliency in that segment for 2025. Our top picks for the sector are F&N and Mr DIY. In addition, Farm Fresh is a top SELL for the sector given its lofty valuation and expected steep competition.

MARKET WEIGHT

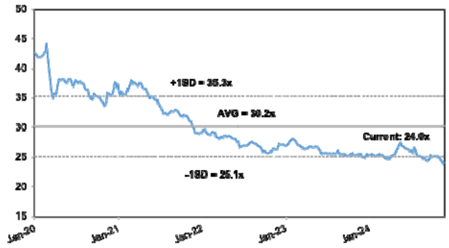
(Maintained)

3Q24 RESULTS SNAPSHOT

Company	3Q24 (RMm)	yoy % chg	qoq % chg	Results
99SM	126.1	13.5	0.5	Within
BAT	68.0	14.5	87.4	Above
Carlsberg	91.0	19.8	13.2	Within
Farm Fresh	26.2	114.8	-1.2	Within
F&N	89.2	-35.2	-27.9	Below
Heineken	97.8	12.0	7.3	Within
Mr. DIY	121.6	-1.6	-21.7	Below
MyNews	2.6	-220.4	150.0	Within
Nestle	85.4	-49.2	-8.8	Within
QL Resources	128.3	4.6	13.0	Within

Source: Bloomberg, UOB Kay Hian

SECTOR VALUATIONS



Source: Bloomberg, UOB Kay Hian

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PEER COMPARISON

Company	Tickers	Price 5 Dec (RM)	Rec	Target Price (RM)	Market Cap (RMm)	P/E FY24F	P/E FY25F	P/BV FY25F	Yield (%) FY24F	Yield (%) FY25F
MyNews	MNHB MK	0.68	HOLD	0.52	484.0	51.5	24.2	1.8	0.8	1.7
British American Tobacco	ROTH MK	7.68	HOLD	6.93	2,192.9	11.5	13.9	5.5	8.7	7.2
Farm Fresh	FFB MK	1.86	SELL	1.25	3,468.0	47.8	23.3	4.0	0.5	1.1
Carlsberg	CAB MK	20.86	BUY	25.10	6,451.3	17.8	16.6	19.3	5.2	5.5
Heineken (M)	HEIM MK	23.78	BUY	29.20	7,250.4	17.1	15.8	15.3	6.0	6.5
F&N Holdings	FNH MK	28.16	BUY	36.30	10,269.8	20.2	19.1	2.7	2.3	2.7
Mr DIY	MRDIY MK	1.84	BUY	2.35	17,691.1	34.6	28.8	9.9	2.2	2.7
QL Resources	QLG MK	4.84	HOLD	4.80	17,850.0	33.3	31.8	4.9	0.5	0.9
99 Speedmart	99SMART MK	2.51	BUY	2.60	20,244.0	36.6	33.2	13.3	1.9	1.4
Nestle	NESZ MK	97.62	HOLD	114.00	22,770.0	48.4	42.6	33.2	1.9	2.2
Average					10,867.1	31.9	24.9	11.0	3.0	3.2

Source: Bloomberg, UOB Kay Hian

- **Putting the brakes on subsidies: Another straw on the consumers' back.** The government plans to roll back petrol subsidies in mid-25. Implementation is through a two-tier system so that the wealthiest 15% of 36.6m registered motor vehicles nationwide pay the market rate. The rationalisation should save the government RM8b a year. This may cast an overhang on the upper middle-income segment of consumers as purse strings will inevitably be constricted, affecting disposable income and potential spillover effects to inflation.

- **99SM was included in the KLCI Index** in the most recent review in Nov 24. It now ranks the 26th largest company by market capitalisation at RM20.6b. It has gained 49% since its IPO on 9 Sep, with a market capitalisation of RM13.8b then. In the past, both Nestle Malaysia (Nestle) and QL Resources (QL) rerated following their respective inclusions. We highlight that Nestle's inclusion during the Nov 17 review also sparked a rerating in QL Resources. On average, Nestle and QL rerated from a PE average of 29.9x to 46.5x.

- **Potential rerating as seen by its consumer peers.** We believe that 99SM could experience a similar rerating to its current forward PE of 36.5x. It could be further compounded by its tight free float of 17%. However, its valuations appear to also have partially priced in its index inclusion. Should 99SM trade at a forward PE of 46.5x, it would imply a share price or RM3.12. This represents ample upside to our current 99SM target price of RM2.60 and BUY recommendation (based on a PE peg of 38.9x or Mr. DIY's +1SD of its historical PE mean). We opt to observe 99SM's stable state of valuations post index inclusion prior to amending our valuations, if any.

INDEX INCLUSION RERATING

	Inclusion	Three-year forward PE historical average prior to inclusion	One-year forward PE average after inclusion	Comments
Nestle Malaysia	2017 Nov review	31.2x	50.0x	
Rerated QL Resources in 2018		28.6x	42.9x	QL Resources rerated alongside Nestle Malaysia after the latter's inclusion into the KLCI Index.
QL Resources	2022 Nov review	45.4x	31.2x	QL Resources appears to have derated but this was largely simply a function of calendarised 2023 earnings growing 24% yoy that compressed its average PE.
Mr. DIY	2021 May review	48.7x*	49.5	Mr. DIY was listed in Oct 20; similar to QL Resources, there were in-built expectations of Mr. DIY being included in the KLCI Index. Therefore, its valuations prior to inclusion were already trading at a lofty >40x PE.
Average (Nestle & rerated QL in 2018)		29.9x	46.5x	
Average (Nestle & post inclusion QL in 2023)		38.3x	40.6x	
Average (Nestle, & post inclusion QL in 2023 and Mr. DIY)		41.8x	43.6x	Rerating is not apparent as Mr. DIY had already rerated prior to inclusion.

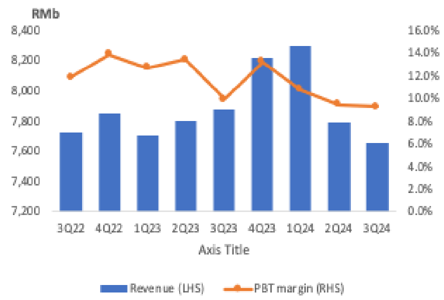
Source: Bloomberg, UOB Kay Hian **Had only been trading for 8 months*

ESSENTIALS

- **Muted sales in 3Q24.** 3Q24 sector sales were flattish at -0.2% yoy (-0.1% qoq). Had it not been for Nestle's contraction of -18.4% yoy, sector sales would have grown 3.6% yoy (+0.8% qoq). Growth was generally lifted by heavyweights such as QL Resources (+10.8%), 99SM (+8.8%) and Mr. DIY (+6.4%). The former was lifted by higher poultry-related sales while the latter two were primarily lifted by higher store count as collective SSSG was negative. Farm Fresh was a particular standout (+26% yoy) with its acquisitions and new product launches.

- **Margins remained largely intact as 3Q24 results were broadly within expectations.** Sector PAT margins softened by 0.6ppt yoy to 8.2% (-0.1ppt qoq) but adjusting for Nestle, margins were unchanged at 0.0ppt yoy (-0.1ppt qoq). Overall margins were weighed by relative heavyweight F&N which saw its margin decline 4.0ppt due to frontloaded A&P spending, which will reverse in the subsequent quarters. This implies that sector margins will continue to trend positively. Overall, 3Q24 sector earnings were broadly within expectations, expanding by 3.2% yoy (-0.3% qoq) (adjusting for Nestle's effect) off improved sales and margins.

SECTOR REVENUE AND PBT MARGIN TREND



Source: Malaysia Institute of Economic Research (MIER)

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