

Singapore Company Update

Dairy Farm

Bloomberg: DFI SP | Reuters: DAIR.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

7 Mar 2022

HOLD

Last Traded Price (4 Mar 2022): US\$2.64 (STI : 3,226.78)
Price Target 12-mth: US\$3.01 (14% upside) (Prev US\$3.96)

Analyst

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What's New

- FY21 core PATMI down 62.7% y-o-y to US\$102.9m
- Grocery retail strategy showing green shoots as market share decline is slowing
- Rumours on China potentially 'co-existing' with COVID-19 is positive
- Maintain HOLD with lower TP of US\$3.01

Price Relative



Forecasts and Valuation

FY Dec (US\$m)	2020A	2021A	2022F	2023F
Revenue	10,269	9,015	9,605	9,949
EBITDA	682	409	465	538
Pre-tax Profit	340	153	215	266
Net Profit	271	103	154	204
Net Pft (Pre Ex.)	276	105	154	204
Net Pft Gth (Pre-ex) (%)	(14.1)	(62.1)	47.3	32.3
EPS (US cts.)	20.0	7.61	11.4	15.1
EPS Pre Ex. (US cts.)	20.4	7.73	11.4	15.1
EPS Gth Pre Ex (%)	(14)	(62)	47	32
Diluted EPS (US cts.)	20.0	7.60	11.4	15.1
Net DPS (US cts.)	16.5	9.50	9.50	12.0
BV Per Share (US cts.)	97.8	93.7	95.6	101
PE (X)	13.2	34.7	23.2	17.5
PE Pre Ex. (X)	13.0	34.1	23.2	17.5
P/Cash Flow (X)	3.3	3.8	4.0	3.2
EV/EBITDA (X)	6.5	10.8	9.7	8.1
Net Div Yield (%)	6.3	3.6	3.6	4.5
P/Book Value (X)	2.7	2.8	2.8	2.6
Net Debt/Equity (X)	0.6	0.7	0.7	0.6
ROAE (%)	21.4	7.9	12.0	15.3
Earnings Rev (%)			(20)	(25)
Consensus EPS (US)			22.2	28.2
Other Broker Recs:		B: 3	S: 1	H: 5

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Visible green shoots

Investment Thesis

Grocery retail faces demand normalisation and intense competition. We think the grocery retail business may face challenges ahead in the form of normalizing demand in the regions where the pandemic situation has stabilised. Competition is also fierce in both the online channel (impacting Yonghui) and offline channel (Indonesia).

Transformation of DFI will not happen overnight. We think the pandemic may have changed consumption patterns in favour of value. In our view, DFI's price investment strategy may lead to a period of lower margins and will need time to bear fruit as cost structure changes are implemented.

Key catalyst – Watch for return of Hong Kong-China travel.

Health & Beauty segment revenue dropped c.US\$1bn in FY20 as the flow of visitors from Mainland China dried up. However, recent rumours that China may be looking to 'co-exist' with COVID-19 may catalyse the stock especially if it leads to a resumption of two-way travel.

Valuation:

TP of US\$3.01 based on SOTP valuation. Our target price of US\$3.01 is derived from a sum-of-parts valuation methodology. We value DFI's core business at US\$2.01 based on DCF and its 20% and 18% stakes in Yonghui and RRHI at US\$0.78 and US\$0.22 respectively based on market prices.

Where we differ:

We are more conservative on margins as we believe DFI's multi-year transformation programme will need time to take shape.

Key Risks to Our View:

A better-than-expected improvement in operating margins or earnings performance could provide upside to our TP.

At A Glance

Issued Capital (m shrs)	1,353
Mkt. Cap (US\$m/US\$m)	3,573 / 3,573
Major Shareholders (%)	
Jardine Matheson Holdings Ltd	77.6
Free Float (%)	22.4
3m Avg. Daily Val (US\$m)	2.9
GIC Industry : Consumer Staples / Food & Staples Retailing	



Watchlist the stock on Insights Direct to receive prompt updates



Live more, Bank less

Dairy Farm

WHAT'S NEW

Visible green shoots

FY21 earnings below consensus as Grocery Retail underperforms

- FY21 revenue declined 12.2% y-o-y to US\$9.0bn, forming 95.7% of consensus estimate.
- Consequently, FY21 core PATMI plunged 62.7% y-o-y to US\$102.9m, forming 84.6% of consensus estimate.
- Notably, Dairy Farm was dragged down by losses incurred by its associate, Yonghui which led to the Group recording a US\$41.8m loss from associates.
- Operating margins were also softer across most segments as government support tapered off.
- The biggest drag remained Grocery Retail which saw operating profit declining 46.4% y-o-y.

Operating profit across all segments lower y-o-y

- Decline in Grocery Retail operating profit was attributed to divestment of Wellcome Taiwan, withdrawal of Giant Indonesia, absence of panic buying relative to FY20, and lack of government reliefs.
- Lower Convenience Stores operating profit on lower customer traffic as a result of COVID restrictions in Singapore and China.
- Similarly, reduced levels of traffic at Health & Beauty stores saw FY21 segment operating profit decreasing
- Pre-opening expenses, supply chain issues and pandemic restrictions impacted operating profit of Home Furnishings segment.

Key financial metrics

US\$m	2H21	2H20	y-o-y	1H21	h-o-h
Revenue	4,478.6	5,028.6	-10.9%	4,536.8	-1.3%
Gross Profit	1,456.8	1,590.9	-8.4%	1,412.9	3.1%
Op Profit	190.8	178.3	7.0%	120.0	59.0%
Assoc/JV Result	(13.7)	69.2	-119.8%	(28.1)	-51.2%
PATMI	74.6	155.7	-52.1%	16.7	346.7%
Core PATMI	70.8	170.6	-58.5%	32.1	120.6%
DPS	6.50	11.50	-43.5%	3.00	116.7%
GP Margin	32.5%	31.6%	0.9ppt	31.1%	1.4ppt
Op Margin	4.3%	3.5%	0.7ppt	2.6%	1.6ppt
<i>Operating Profit</i>					
Grocery Retail	60.5	119.5	-49.4%	82.7	-26.8%
Conv. Stores	35.4	56.1	-36.9%	18.6	90.3%
H&B	35.8	23.3	53.6%	20.6	73.8%
Home					
Furnishings	33.5	45.4	-26.2%	11.5	191.3%
Acc adjustment	33.2	28.7	15.7%	50.2	-33.9%
<i>Op Margins</i>					
Grocery Retail	3.1%	4.7%	-1.6ppt	3.8%	-0.7ppt
Conv. Stores	3.0%	5.1%	-2.1ppt	1.7%	1.3ppt
H&B	3.9%	2.4%	1.4ppt	2.3%	1.6ppt
Home					
Furnishings	7.8%	10.3%	-2.5ppt	3.0%	4.8ppt

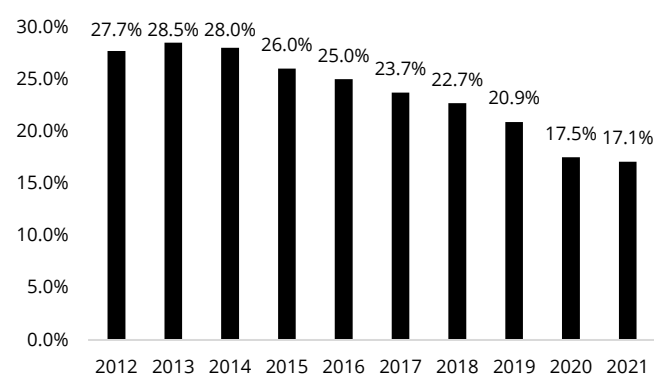
Source: Company, DBS Bank

Grocery Retail

Impact of price investment strategy to take time but Hong Kong could deliver a boost. In Singapore, there is some impact from DFI's price investment strategy. DFI's FY21 market share declined at a much slower pace of 0.4ppt (FY20: -3.4ppts) amongst modern grocery retailers according to Euromonitor. This was achieved even as operating margins were maintained at above 3%, a significant performance compared to the 2017 – 2019 period where operating margins had not crossed 2.2%. That said, the better margins come on the back of pandemic driven demand. The impact of DFI's price investment strategy will become clearer as demand normalizes.

For FY22F, we have forecast sales to grow by 3.4% vs a 22.4% decline in FY21. Correspondingly, Grocery Retail operating margins should rise to 3.8%, driven by pandemic restrictions and panic buying due to the COVID-19 situation in Hong Kong.

DFI's grocery retail strategy slowing market share decline in Singapore



Source: Euromonitor, DBS Bank

Convenience Stores

Sporadic COVID-19 outbreaks could dent performance.

Mainland China and Hong Kong have seen multiple outbreaks of COVID-19, each of which has resulted in stricter pandemic restrictions that affected convenience store sales. Even as Hong Kong battles its fifth COVID-19 wave, we are encouraged that pandemic control measures in Mainland China are becoming more localised. We are projecting revenue growth of 6.1% y-o-y for convenience stores in FY22F, largely predicated on continued

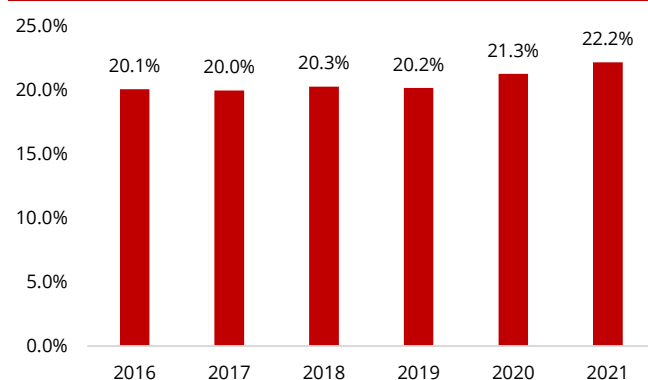
Dairy Farm

momentum in store growth at 4.0% y-o-y. Operating margin is assumed to inch up by 0.1ppt to account for the more localised restrictions in Mainland China, which are likely to boost convenience stores recovery.

Health & Beauty

Mainland China-Hong Kong border reopening remains critical. Prior to COVID-19, we estimate that about a third of segment revenue was contributed by mainlanders shopping at Hong Kong's Mannings stores. We think that a reopening of this border coupled with a convenient border crossing will be critical for the segment to regain this lost revenue. In the meantime, we project FY22F sales to grow 4.5% y-o-y on an expected boost from COVID-19 driven purchases by locals in Hong Kong.

Guardian stores gaining market share in Singapore



Source: Euromonitor, DBS Bank

Home Furnishings

Home Furnishings to record a bounce on reopening and new stores. FY21 saw IKEA stores in Taiwan and Indonesia disrupted as COVID-19 cases surged. We see both markets strongly recovering this year. A full year of sales from new stores together with a recovery in Taiwan and Indonesia leads us to project FY22F segment sales growth and operating margin of 28.3% and 7.5% respectively.

Maintain HOLD with lower TP of US\$3.01. We lower our FY22F/23F earnings by 20%/25% mostly on the delay of the China-Hong Kong border reopening due to a spike in COVID-19 cases in Hong Kong. Positively, recent rumours that China is considering a shift to 'co-exist' with COVID-19 could potentially spur the opening of the China-Hong Kong border and revive mainland Chinese traffic in Hong Kong. Such a shift will be welcomed by Dairy Farm's 3 major segments (Grocery Retail, Convenience Stores, Health & Beauty) where mainlanders either make up a significant portion of customers (Grocery Retail and Health & Beauty) or have frequented stores less due to COVID-19 outbreaks and restrictions in China (Convenience Stores). Indeed, the recent spike in COVID-19 cases in Hong Kong and the lack of reaction in Dairy Farm's share price may be indicative that the market is indifferent to COVID-19 driven supermarket demand but instead is more focused on the return of mainland Chinese traffic.

Company Background

Dairy Farm (DFI) is a Pan Asian retailer, operating over 6,400 supermarkets, hypermarkets, health and beauty stores, convenience stores, home furnishing stores and restaurants under well-known brand names in Hong Kong, Taiwan, China, Macau, Singapore, the Philippines, Cambodia, Brunei, Malaysia, Indonesia, and Vietnam.

Dairy Farm

Interim Income Statement (US\$m)

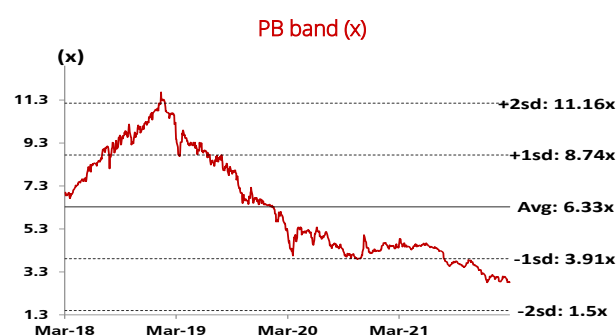
FY Dec	2H2020	1H2021	2H2021	% chg yoy	% chg hoh
Revenue	5,029	4,537	4,479	(10.9)	(1.3)
Cost of Goods Sold	(3,437)	(3,124)	(3,022)	(12.1)	(3.3)
Gross Profit	1,592	1,413	1,457	(8.5)	3.1
Other Oper. (Exp)/Inc	(1,390)	(1,258)	(1,298)	(6.6)	3.1
Operating Profit	202	155	159	(21.1)	3.0
Other Non Opg (Exp)/Inc	0	0	0	-	-
Associates & JV Inc	60	(44)	3	(94.7)	nm
Net Interest (Exp)/Inc	(68)	(60)	(59)	13.9	2.0
Exceptional Gain/(Loss)	(15)	(15)	14	nm	nm
Pre-tax Profit	179	36	117	(34.5)	229.5
Tax	(37)	(19)	(41)	11.4	115.8
Minority Interest	3	0	10	191.2	nm
Net Profit	146	17	86	(40.8)	416.2
Net profit bef Except.	160	32	72	(54.8)	125.9
EBITDA	262	111	162	(38.0)	46.3
Margins (%)					
Gross Margins	31.7	31.1	32.5		
Opg Profit Margins	4.0	3.4	3.6		
Net Profit Margins	2.9	0.4	1.9		

Source of all data: Company, DBS Bank

Historical PE and PB band



Source: Bloomberg Finance L.P., DBS Bank estimates



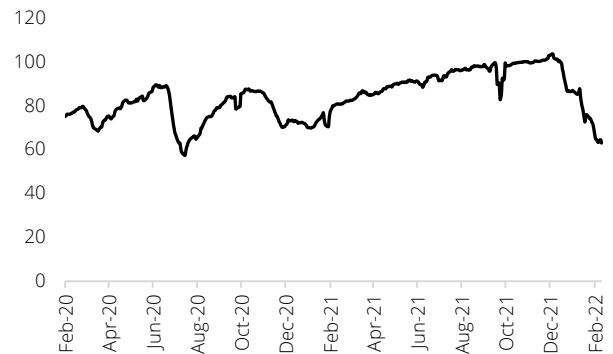
Source: Bloomberg Finance L.P., DBS Bank estimates

Dairy Farm

Residential Mobility - Hong Kong



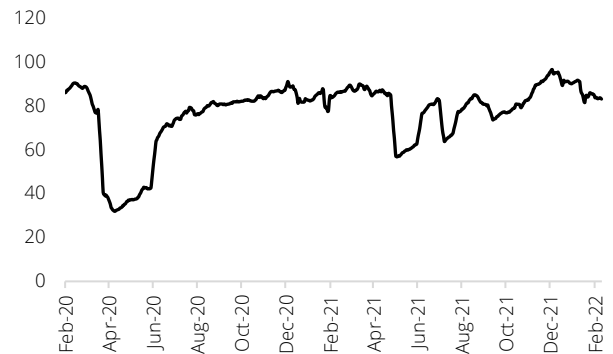
Retail & Recreation Mobility - Hong Kong



Residential Mobility - Singapore



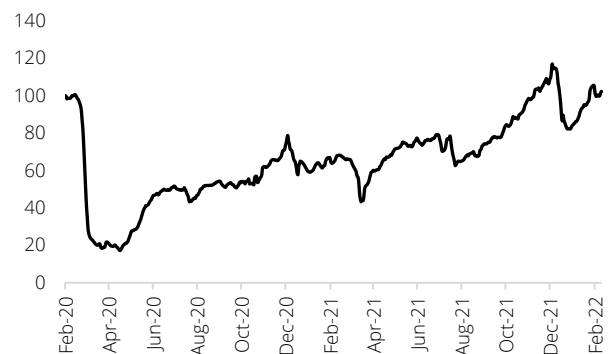
Retail & Recreation Mobility - Singapore



Residential Mobility - Philippines



Retail & Recreation Mobility - Philippines



Source: Google, DBS Bank

Dairy Farm

Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
Number of outlets	6,028	5,553	5,218	5,366	5,467
Sales per store blended	1,857	1,849	1,728	1,790	1,820

Segmental Breakdown

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenues (US\$m)					
Food	7,376	7,447	6,394	6,672	6,832
Health & beauty stores	3,051	1,990	1,805	1,887	2,011
Home furnishing stores	766	832	816	1,046	1,106
Total	11,192	10,269	9,015	9,605	9,949
Operating profit (US\$m)					
Food	145	324	197	223	224
Health & beauty stores	296	65.7	56.4	66.0	101
Home furnishing stores	42.7	70.5	45.0	78.5	88.5
Support office/others	(46.8)	(48.8)	15.2	0.36	(2.4)
Total	437	412	314	367	411
Operating profit Margins					
Food	2.0	4.4	3.1	3.3	3.3
Health & beauty stores	9.7	3.3	3.1	3.5	5.0
Home furnishing stores	5.6	8.5	5.5	7.5	8.0
Support office/others	N/A	N/A	N/A	N/A	N/A
Others	N/A	N/A	N/A	N/A	N/A
Total	3.9	4.0	3.5	3.8	4.1

Income Statement (US\$m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	11,192	10,269	9,015	9,605	9,949
Cost of Goods Sold	(7,659)	(7,078)	(6,146)	(6,547)	(6,782)
Gross Profit	3,534	3,191	2,870	3,057	3,167
Other Opng (Exp)/Inc	(3,097)	(2,779)	(2,556)	(2,690)	(2,756)
Operating Profit	437	412	314	367	411
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	115	76.0	(40.4)	(36.7)	(12.8)
Net Interest (Exp)/Inc	(158)	(143)	(119)	(115)	(132)
Exceptional Gain/(Loss)	2.90	(4.7)	(1.7)	0.0	0.0
Pre-tax Profit	396	340	153	215	266
Tax	(69.5)	(74.2)	(60.0)	(75.4)	(79.9)
Minority Interest	(2.8)	5.00	10.0	14.1	17.4
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	324	271	103	154	204
Net Profit before Except.	321	276	105	154	204
EBITDA	739	682	409	465	538
Growth					
Revenue Gth (%)	(4.7)	(8.3)	(12.2)	6.5	3.6
EBITDA Gth (%)	(12.4)	(7.7)	(40.1)	13.8	15.6
Opg Profit Gth (%)	(13.7)	(5.7)	(23.8)	17.1	11.9
Net Profit Gth (Pre-ex) (%)	(10.4)	(14.1)	(62.1)	47.3	32.3
Margins & Ratio					
Gross Margins (%)	31.6	31.1	31.8	31.8	31.8
Opg Profit Margin (%)	3.9	4.0	3.5	3.8	4.1
Net Profit Margin (%)	2.9	2.6	1.1	1.6	2.0
ROAE (%)	27.7	21.4	7.9	12.0	15.3
ROA (%)	3.8	3.3	1.3	2.0	2.7
ROCE (%)	6.9	6.3	3.9	4.9	5.9
Div Payout Ratio (%)	87.7	82.4	124.9	83.4	79.7
Net Interest Cover (x)	2.8	2.9	2.6	3.2	3.1

Source: Company, DBS Bank

Dairy Farm

Interim Income Statement (US\$m)

FY Dec	2H2019	1H2020	2H2020	1H2021	2H2021
Revenue	5,432	5,240	5,029	4,537	4,479
Cost of Goods Sold	(3,670)	(3,641)	(3,437)	(3,124)	(3,022)
Gross Profit	1,762	1,599	1,592	1,413	1,457
Other Oper. (Exp)/Inc	(1,560)	(1,389)	(1,390)	(1,258)	(1,298)
Operating Profit	202	210	202	155	159
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	41.1	15.7	60.3	(43.6)	3.20
Net Interest (Exp)/Inc	(73.9)	(74.4)	(68.3)	(60.0)	(58.8)
Exceptional Gain/(Loss)	0.0	10.1	(14.8)	(15.4)	13.7
Pre-tax Profit	169	161	179	35.6	117
Tax	(25.8)	(37.4)	(36.8)	(19.0)	(41.0)
Minority Interest	(1.1)	1.60	3.40	0.10	9.90
Net Profit	142	125	146	16.7	86.2
Net profit bef Except.	142	115	160	32.1	72.5
EBITDA	243	226	262	111	162

Growth

Revenue Gth (%)	(5.7)	(3.5)	(4.0)	(9.8)	(1.3)
EBITDA Gth (%)	(21.1)	(7.3)	16.2	(57.6)	46.3
Opg Profit Gth (%)	(13.8)	3.8	(3.8)	(23.4)	3.0
Net Profit Gth (%)	(20.0)	(11.9)	16.1	(88.5)	416.2

Margins

Gross Margins (%)	32.4	30.5	31.7	31.1	32.5
Opg Profit Margins (%)	3.7	4.0	4.0	3.4	3.6
Net Profit Margins (%)	2.6	2.4	2.9	0.4	1.9

Balance Sheet (US\$m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	820	772	803	829	872
Invt in Associates & JVs	2,102	2,257	2,164	2,128	2,115
Other LT Assets	3,943	3,484	3,312	3,234	3,124
Cash & ST Invt	301	278	210	164	315
Inventory	896	779	782	861	892
Debtors	281	304	232	250	273
Other Current Assets	26.1	28.0	101	101	101
Total Assets	8,370	7,901	7,605	7,566	7,691
ST Debt	938	852	744	794	794
Creditor	2,315	2,061	2,081	1,973	2,044
Other Current Liab	911	813	716	724	720
LT Debt	184	242	311	311	311
Other LT Liabilities	2,782	2,597	2,486	2,486	2,486
Shareholder's Equity	1,209	1,322	1,267	1,293	1,368
Minority Interests	30.3	13.6	0.0	(14.1)	(31.5)
Total Cap. & Liab.	8,370	7,901	7,605	7,566	7,691
Non-Cash Wkg. Capital	(2,023)	(1,763)	(1,683)	(1,486)	(1,499)
Net Cash/(Debt)	(821)	(817)	(844)	(940)	(789)
Debtors Turn (avg days)	9.9	10.4	10.8	9.2	9.6
Creditors Turn (avg days)	114.3	116.0	125.8	115.4	110.4
Inventory Turn (avg days)	44.2	44.4	47.4	46.8	48.2
Asset Turnover (x)	1.3	1.3	1.2	1.3	1.3
Current Ratio (x)	0.4	0.4	0.4	0.4	0.4
Quick Ratio (x)	0.1	0.2	0.1	0.1	0.2
Net Debt/Equity (X)	0.7	0.6	0.7	0.7	0.6
Net Debt/Equity ex MI (X)	0.7	0.6	0.7	0.7	0.6
Capex to Debt (%)	20.8	20.8	17.6	17.1	19.1
Z-Score (X)	1.9	1.8	1.8	1.9	1.9

Source: Company, DBS Bank

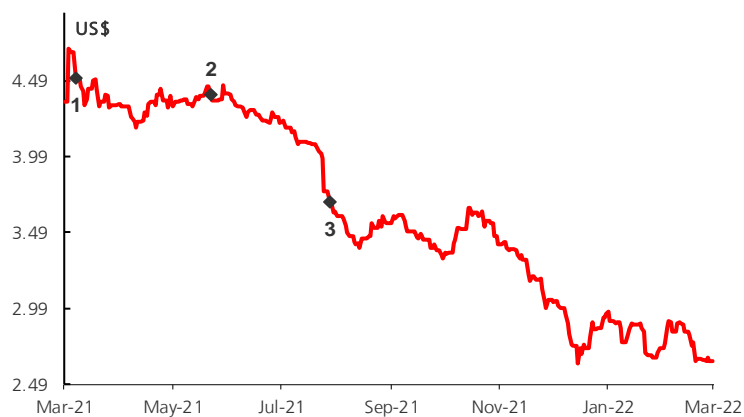
Dairy Farm

Cash Flow Statement (US\$m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	396	340	153	215	266
Dep. & Amort.	1,002	983	886	914	920
Tax Paid	(25.1)	(110)	(110)	(75.4)	(79.9)
Assoc. & JV Inc/(loss)	(115)	(76.0)	40.4	36.7	12.8
Chg in Wkg.Cap.	(76.7)	(102)	(10.4)	(205)	17.3
Other Operating CF	107	32.1	(16.2)	7.95	(4.1)
Net Operating CF	1,288	1,067	942	893	1,132
Capital Exp.(net)	(233)	(227)	(185)	(189)	(211)
Other Invt.(net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	(3.8)	(18.3)	(1.6)	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	(45.9)	159	62.0	(25.0)	(25.0)
Net Investing CF	(283)	(86.4)	(125)	(214)	(236)
Div Paid	(284)	(264)	(196)	(129)	(129)
Chg in Gross Debt	73.4	(70.7)	(59.9)	50.0	0.0
Capital Issues	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(797)	(709)	(585)	(647)	(616)
Net Financing CF	(1,008)	(1,043)	(841)	(725)	(745)
Currency Adjustments	6.30	8.00	(0.5)	0.0	0.0
Chg in Cash	3.80	(54.1)	(24.2)	(46.6)	151
Opg CFPS (US cts.)	101	86.4	70.4	81.2	82.4
Free CFPS (US cts.)	78.0	62.1	56.0	52.0	68.0

Source: Company, DBS Bank

Target Price & Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	12 Mar 21	4.51	5.02	BUY
2:	27 May 21	4.40	4.78	BUY
3:	02 Aug 21	3.69	3.96	HOLD

Note: Share price and Target price are adjusted for corporate actions.

Source: DBS Bank

Analyst: Woon Bing Yong

Dairy Farm

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Dissemination Date: 7 Mar 2022 13:04:58 (SGT)

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