PT Matahari Department Store

FY16 Results – Challenging Path

NEUTRAL – IDR 13.300

02 March 2017

Adrian Lorenzo
Equity Analyst
+62 21 392 5550 ext. 618
adrian.lorenzo@sinarmassekuritas.co.id

Matahari Department Store (LPPF) books 13.4% yoy NPAT growth (5% below consensus) on the back of lower than expected 4Q16 results. On a yoy basis 4Q16 margins declined, with gross margin -10bps and EBITDA margin -180bps declining significantly as a result of the aggresive pricing strategy taken up by management in order to fix inventory issues relating to the post lebaran period. Additionally, the increasing presence of foreign specialty retailers along with growing e-commerce spending seemed to have LPPF sales as the 2.7% SSSG in 4Q16 would indicate. FY16 operating margins also declined by ~30bps in spite of the 20% fall in utiliity expenses as cost savings from the LED lighting program were outweighed by the 30% rise in marketing expenses with marketing expenses now equalling 2.9% from net sales FY16 compared to 2.5% FY15.

Slow Start to the Year Expected

Weak spending by the middle class, with no sign of an uptick has led management to guide low single digit SSSG figures for 1Q17 taking into account the strong SSSG figures posted in 1Q15 of 6%. While discouraging in the near term, revenue contributions from the ex-Java region continue to grow as LPPF's presence across Indonesia remains unrivalled. For 4Q16, the Ex-Java region contributed to ~41% from net revenues, while East and West Java outperformed significantly with 4.6% SSSG for the quarter compared to 1.3% SSSG for the Greater Jakarta area and 2.2% SSSG for Ex-Java area.

Looking Ahead

LPPF currently trades at 14.5x PE, below its 3 year mean (25.32x) and cheaper compared to its peers both locally and regionally. While we aniticipate SSSG figures are likely to rebound in 2Q16 given the shift in pre-lebaran dates from 3Q to 2Q, we forecast SSSG figures to remain at ~5.6% FY17 as the threat of E-commerce and foreign retailers looms large. FY17, we forecast gross sales to grow 9.5% yoy while anticipating slight margin contractions as LPPF may continue to opt for aggresive pricing strategies given the intense competition amongst retailers. **Taking this into account coupled with the factors mentioned above, we have therefore downgrade our recommendation to NEUTRAL with TP IDR 13,320 indicating 15.8x PE17.**

Financial Highlights	2015	2016	2017E	2018F	2019F
Net Revenue (IDR Bn)	9,007	9,897	10,836	11,909	13,108
Growth		*9.9%*	*9.5%*	*9.9%*	*10.1%*
Gross Profit (IDR Bn)	5,671	(3,684)	(4,059)	(4,507)	(4,993)
Net Income (IDR Bn)	1,781	2,020	2,166	2,445	2,668
Growth		*13.4%*	*7.2%*	*12.9%*	*9.1%*
Gross Margin (%)	35.26%	35.84%	35.79%	36.40%	36.41%
Net Margin (%)	11.07%	11.65%	11.41%	11.72%	11.62%
Return on Equity (%)	90.2%	62.2%	47.1%	39.3%	33.8%
Return on Assets (%)	45.8%	41.6%	37.5%	36.1%	33.8%
EPS (IDR)	610.3	692.2	742.3	838.0	914.3

Stock Information

Sector	Retail
Bloomberg Ticker	LPPF IJ
Market Cap (IDR Tn)	34.2
Share Out/ Float (M)	2,917.9/2,407.9
Current Price (IDR)	11,725
52 W Target Price (IDR)	13,300
Upside (%)	13.4

Share Price Performance

52 W High (07/14/16)	22,575
52 W Low (03/01/17)	11,175
52 W Beta	1.19
YTD Change (%)	-22.48%

Relative Valuations

Trailing P/E	14.5x
Forward P/E	15.8x
P/BV	18.4x
EV/EBITDA	11.5x

Potential Catalysts

Strong Java (ex Greater Jakarta) Sales Encouraging

Completion of 9 new stores in FY16 to go along with 16 store refurbishments were beyond managements expectations and stand to contribute to new stores earnings for FY17. LPPF also plans to open between 6-8 new stores and refurbish 20-25 MDS stores with new store openings targeted towards serving the outperforming regions with 5 of 6 stores set to be opened in the Java (ex Greater Jakarta) region. The Greater Jakarta area accounted for the lowest SSSG returns for both 4Q16 and FY16 earnings (1.3% and 3% respectively) as entrance of foreign specialy retailers and new mall openings continues to take market share away from LPPF in the area. Moving forward, management aims to continue to cater to the under served markets especially in the outer regions by taking advantage of LPPF's presence across Indonesia.

Regional Revenue Contributions	4Q15	4Q16	*yoy growth*	FY15	FY16	*yoy growth*
Sumatera	336.48	368.26	*9.4%*	1,412.76	1,551.08	*9.8%*
Java	1,269.73	1,382.80	*8.9%*	5,456.53	6,067.22	*11.2%*
Kalimantan, Sulawesi & Maluku	406.55	418.36	*2.9%*	1,495.98	1,589.27	*6.2%*
Others	169.99	187.16	*10.1%*	591.42	626.44	*5.9%*

Source: Sinarmas Investment Research

Strong Cash Position Opening Possibility for Other Ventures

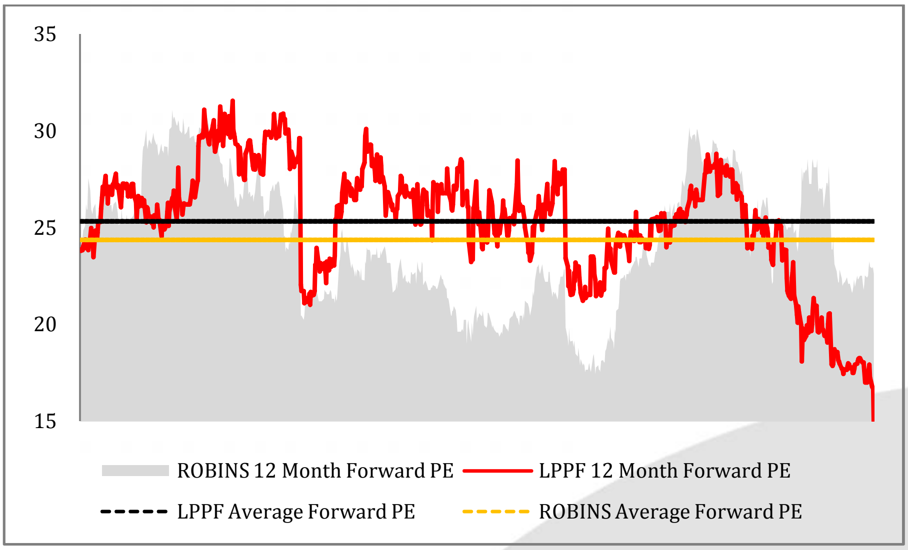
LPP's strong cash position IDR 1.713tn means the company will have no problems funding for new store openings and refurbishments. For the year LPPF has set CAPEX between IDR 400-450bn with 30-35% set for new store openings and 20-25% for MDS store refurbishments after spending IDR356.8bn in CAPEX FY16. Management also announced that the CAPEX figures are excluding the IDR 590bn set to be invested into MM with the IDR165bn investment early this year also not included in this years CAPEX spending. On another note, LPPF has also plans to collaborate with local designers for exclusive collections in order to increase the number of private brands served in MDS stores and in their Mataharistore.com website.

Nevada Specialty Stores an Option

Adding to the 9 new department stores opened, the company also opened a specialty store for its top DP brand Nevada as a test to survey Nevada's impact compared to other specialty brands in a high traffic center. Moving forward, the company aims to test the Nevada brand in multiple locations with different demographics and in higher traffic areas.

Valuations Support

Currently trading at 14.5x PE, LPPF trades at a discount compared to its local peers and to its regional peers. Comparing LPPF's case to Robinson Department Store in Thailand (ROBINS TB), ROBINS bottomed at 17x PE17 early in 2016 following FY15 results. ROBINS currently trades at 22.7x PE18 following strong performances in 2Q16 and 3Q16. With the pre-lebaran period set to shift earlier this year, strong SSSG results in 2Q-3Q this year could catalyze a potential re-rating for LPPF.



Source: Sinarmas Investment Research

Downside Risks

E-Commerce Venture a Factor

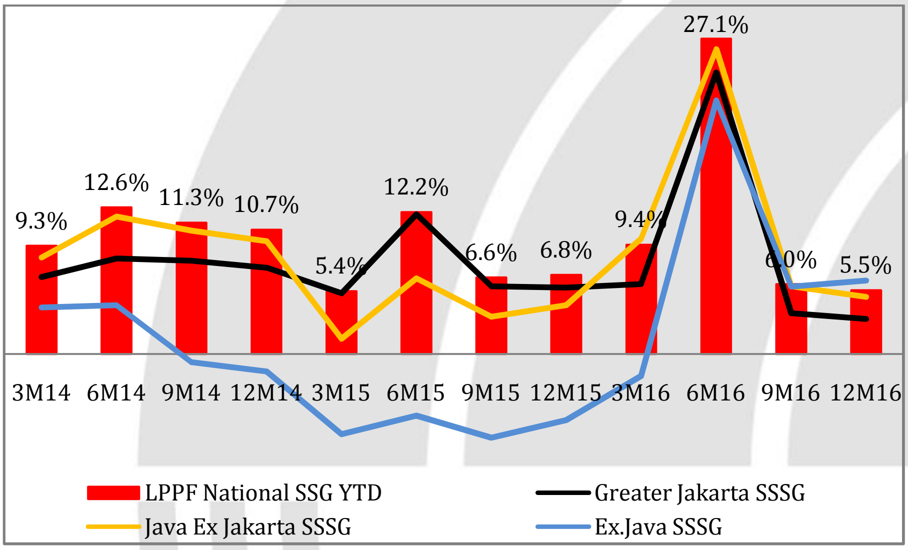
Since the launch of Mataharistore.com acting as a dedicated page within Mataharimall.com's (MM) site, LPPF has been able to complete over 100,000 (as per FY16 results) transactions taking advantage of the high traffic typically associated with launch of new e-commerce sites. Comparing to MDS stores, LPPF was able to leverage its Top 5 DP brands (namely Nevada, Connexion, Cole, Little M and Super T) to account for 67% of DP online sales as compared to 55% offline DP sales with Nevada in particular accounting for 32.1% of DP online sales. Additionally the company announced that they will not be involved in any further investments into the E-Commerce platform. Despite these very early results, the negative sentiments from LPPF's additional IDR 590bn into MM outweight the positives given the intense competition expected going forward amongst online retailers.

Margins at Risk

Stemming from inventory issues in 3Q16, LPPF resorted to aggresive pricing schemes resulting in average inventory days to fall from 112 days to 109 as of end 4Q16. Solving the inventory issue however, resulted in compressed margins especially for DP products. Looking deeper into 4Q16 SSSG results, 0.8% SSSG was down to increase in unit volume with the rest attributed to increase in AUR with FY16 SSSG driven bvy 3.8% in AUR amd 1.6% increase in unit volume. Looking ahead, the increased presence of global brands in Indonesia looms large with the company possibility resorting to either offering more discounts on its products or needing to conduct further marketing campaigns to increase sales. Aggresive marketing campaigns however, will likely lead to higher OPEX which witnessed a 10.2% yoy in spite of the cost efficiency actions taken by management as utility expenses declined by 20% on the heels of the LED lighting initiative. Moving forward, we expect marketing expenses to continue to increase given the need to leverage LPPF's new private label brands. We forecast margin contractions for LPPF with operating, EBITDA and Net Profit margins declining by -20bps, -20bps and -30bps respectively.

Greater Jakarta Sales a Concern

Accounting for the lowest SSSG returns the Greater Jakarta area underperformed compared to the other regions. The increased number of malls in Jakarta resulting in easier access to other specialty or department stores has impacted LPPF's sales in the region with pressure coming to both LPPF's lower end products given RALS' aggresive marketing campaign, as well as the higher end products with the promotional discounts on offer at various high end specialty stores. We also view continued e-commerce spending by the middle segment as a risk to MDS' sales especially in the Greater Jakarta area as the area accounted for 77% from total online sales by Matahari.com.



Source: Sinarmas Investment Research

Appendix – Financial Statements, Ratios & Margins

Income Statement (IDR Bn)	2015	2016	2017E	2018F	2019F
Gross Revenues	16,083.01	17,332.99	18,977.01	20,856.69	22,955.79
Net Revenues	**9,007**	**9,897**	**10,836**	**11,909**	**13,108**
Cost of Goods Sold	(3,336)	(3,685)	(4,044)	(4,317)	(4,749)
Gross Profit	**5,671**	**6,212**	**6,792**	**7,592**	**8,359**
Operating Expenses	(3,342)	(3,684)	(4,059)	(4,507)	(4,993)
Depreciation	241	261	290	333	377
Operating Income	**2,330**	**2,534**	**2,733**	**3,085**	**3,366**
EBITDA	2,582	2,806	3,035	3,433	3,761
Tax Expenses	(464)	(513)	(550)	(621)	(678)
Net Income	**1,781**	**2,020**	**2,166**	**2,445**	**2,668**
EPS (Rp.)	610.31	692.17	742.26	837.96	914.34

Balance Sheet (IDR Bn)					
Current Assets					
Cash & Cash Equivalents	947	1,713	1,541	2,792	3,557
Trade & Other Receivables	76	95	107	114	127
Inventories	1,008	995	1,225	1,346	1,482
Total Current Assets	**2,273**	**2,974**	**3,106**	**4,530**	**5,506**
Fixed Assets	877	980	1,062	1,122	1,137
Investments & Others	740	905	1,608	1,130	1,254
Total Assets	**3,889**	**4,859**	**5,776**	**6,782**	**7,896**
Current Liabilities					
Trade & Other Payables	1,704	1,791	1,899	1,956	2,074
Accrued Expenses	331	451	472	481	503
Current Loans	-	-	-	-	-
Total Current Liabilities	**2,439**	**2,588**	**2,721**	**2,780**	**2,918**
Long Term Liabilities	344	415	431	449	468
Total Liabilities	**2,783**	**3,004**	**3,152**	**3,229**	**3,386**
Equity					
Share Capital & APIC	(3,185)	(3,185)	(3,185)	(3,185)	(3,185)
Retained Earnings	4,291	5,040	5,809	6,738	7,695
Total Liabilities & Equity	**3,889**	**4,859**	**5,776**	**6,782**	**7,896**

Financial Ratios					
P/E	19.25	16.98	15.83	14.02	12.85
Yield (%)	2.9%	3.6%	4.1%	4.4%	5.0%
P/B	30.99	18.48	13.07	9.65	7.60
EV/EBITDA	16.73	11.61	12.30	10.51	9.39
ROE	90.2%	62.2%	47.1%	39.3%	33.8%
ROA	45.8%	41.6%	37.5%	36.1%	33.8%
Current Ratio	0.93	1.15	1.14	1.63	1.89
D/E	-	-	-	-	-
Debt/ Assets	-	-	-	-	-

Retail Specifics					
National SSSG	**6.8%**	**5.5%**	**5.6%**	**5.9%**	**6.1%**
Matahari Department Stores	142	151	159	167	175
Receivable Days	3.08	3.49	3.61	3.48	3.53
Payable Days	186.43	177.40	171.40	165.40	159.40
Inventory Days	110.28	109	110.54	113.80	113.88
Cash Conversion Cycle	(73.07)	(75.34)	(57.25)	(48.12)	(42.00)

Profitability Margins					
Gross Profit Margin	35.26%	35.84%	35.79%	36.40%	36.41%
Operating Profit Margin	14.48%	14.62%	14.40%	14.79%	14.66%
EBITDA Margin	16.05%	16.19%	15.99%	16.46%	16.38%
Net Profit Margin	11.07%	11.65%	11.41%	11.72%	11.62%

Source: Sinarmas Investment Research

DISCLAIMER

This report has been prepared by PT Sinarmas Sekuritas, an affiliate of Sinarmas Group.

This material is: (i) created based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such; (ii) for your private information, and we are not soliciting any action based upon it; (iii) not to be construed as an offer to sell or a solicitation of an offer to buy any security.

Opinions expressed are current opinions as of original publication date appearing on this material and the information, including the opinions contained herein, is subjected to change without notice. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this publication may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, integrating and interpreting market information. Research will initiate, update and cease coverage solely at the discretion of Sinarmas Research department. If and as applicable, Sinarmas Sekuritas' investment banking relationships, investment banking and non-investment banking compensation and securities ownership, if any, are specified in disclaimers and related disclosures in this report. In addition, other members of Sinarmas Group may from time to time perform investment banking or other services (including acting as advisor, manager or lender) for, or solicit investment banking or other business from companies under our research coverage. Further, the Sinarmas Group, and/or its officers, directors and employees, including persons, without limitation, involved in the preparation or issuance of this material may, to the extent permitted by law and/or regulation, have long or short positions in, and buy or sell, the securities (including ownership by Sinarmas Group), or derivatives (including options) thereof, of companies under our coverage, or related securities or derivatives. In addition, the Sinarmas Group, including Sinarmas Sekuritas, may act as market maker and principal, willing to buy and sell certain of the securities of companies under our coverage. Further, the Sinarmas Group may buy and sell certain of the securities of companies under our coverage, as agent for its clients.

Investors should consider this report as only a single factor in making their investment decision and, as such, the report should not be viewed as identifying or suggesting all risks, direct or indirect, that may be associated with any investment decision. Recipients should not regard this report as substitute for exercise of their own judgment. Past performance is not necessarily a guide to future performance. The value of any investments may go down as well as up and you may not get back the full amount invested.

Sinarmas Sekuritas specifically prohibits the redistribution of this material in whole or in part without the written permission of Sinarmas Sekuritas and Sinarmas Sekuritas accepts no liability whatsoever for the actions of third parties in this respect. If publication has been distributed by electronic transmission, such as e-mail, then such transmission cannot be guaranteed to be secure or error-free as information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete, or contain viruses. The sender therefore does not accept liability for any errors or omissions in the contents of this publication, which may arise as a result of electronic transmission. If verification is required, please request a hard-copy version.

Additional information is available upon request.

Images may depict objects or elements which are protected by third party copyright, trademarks and other intellectual properties.