

STRATEGY – SINGAPORE

Alpha Picks: Looking For Quality

Media headlines in the later part of January regarding the 2019 novel coronavirus have added more elements of uncertainty to the market. From 20-31 January, the STI fell 3.9%, more than erasing the 1.8% gain over 1-20 January. Stocks have retraced to even more inexpensive levels and we suggest investors look to accumulate quality stocks with an eye on a market recovery in the next six months or so. For Feb 20, we remove SMM, CDREIT, Koufu and Fu Yu but add FCT, Japfa and Food Empire.

WHAT'S NEW

- **Reviewing picks in January.** The FSSTI lost 2.1% in Jan 20. Similarly, most of our alpha picks suffered declines with our portfolio retracing 2.0% mom, narrowly outperforming the FSSTI. Outperformers within our portfolio include ST Engineering which recorded decent gains of 4.3% mom, and our short call on Sembcorp Marine (SMM, -12.1% mom) while calls that worked against us were Yangzijiang (-15.2% mom) and CSE Global (-7.3% mom).

ACTION

- **For the large-cap stocks, we remove SMM and CDREIT and add Frasers Centrepoint Trust (FCT).** We take the opportunity to remove SMM as its share price performance has worked in our favour in the past two months and we believe much of the bad news is currently in the price. We also remove CDREIT as we believe in the next 6-8 months, its Singapore portfolio (c.62% of FY19 NPI) will continue to be weighed down by novel coronavirus (nCoV) related cancellations. Although China accounts for c.10% of CDREIT's Singapore hotel business, the collateral effect may be larger with affected hotels cutting prices to gain market share. In its place, we have put in FCT as the company's exposure to suburban malls is defensive in nature given that spending at its malls are necessity-based. In addition, the company potentially has growth via the acquisition of stakes in its sponsor's suburban malls in Singapore.
- **For our small-cap picks, we reshuffle our picks by removing Koufu and Fu Yu and adding in Japfa and Food Empire.** We take profit on Fu Yu which has gained a commendable 34% since being placed into our alpha picks. We also remove Koufu and while we retain our BUY rating on the stock, we believe the spread of the nCoV could weigh on its earnings in the short term due to the decline in mainland China tourist arrivals in Singapore and Macau. On the other hand, we add Japfa as we believe it has been unjustifiably sold down post news of the nCoV. We favour the stock as we see multiple positive earnings indicators on the back of the rise of ASPs for its key segments. Recently-initiated Food Empire has also been added as the stock trades at an attractive valuation of 9.4x 2020F PE, and we expect earnings to gain traction in 2019-20F.

ANALYSTS' TOP ALPHA* PICKS

| Analyst | Company | Rec | Performance# | Catalyst |
|-------------------------------|----------------|-----|--------------|--|
| Jonathan Koh | Frasers Ctr Tr | BUY | - | Acquisition from sponsor of stakes in various suburban malls in Singapore |
| John Cheong/ Joohijit Kaur | Japfa | BUY | - | Better-than-expected prices of products for key segments |
| Joohijit Kaur/ Clement Ho | Food Empire | BUY | - | Higher-than-expected volume growth, better-than-expected performance of currencies in key markets. |
| Joohijit Kaur/ John Cheong | CSE Global | BUY | -2.7 | Large greenfield project wins, accretive acquisitions. |
| Adrian Loh | Yangzijiang | BUY | 5.2 | New ship-building order announcements |
| Adrian Loh | Keppel Corp | BUY | 7.1 | Continued recovery in new-order flow in 2H19 |
| K Ajith | ST Engineering | BUY | 9.2 | New order wins. |
| Jonathan Koh | DBS | BUY | -6.9 | US-China trade deal and strong deposit franchise which ensures firmer NIM. |

* Denotes a timeframe of 1-3 months and not UOBKH's usual 12-month investment horizon for stock recommendation

Share price change since stock was selected as Alpha Pick

Source: UOB Kay Hian

KEY RECOMMENDATIONS

| Company | Rec | Share Price (S\$) | Target Price (S\$) | Upside/ (Downside) to TP (%) |
|----------------|-----|-------------------|--------------------|------------------------------|
| CSE Global | BUY | 0.545 | 0.70 | 28.4 |
| DBS | BUY | 25.70 | 28.65 | 11.5 |
| Food Empire | BUY | 0.70 | 0.89 | 27.1 |
| Frasers Cpt Tr | BUY | 2.92 | 3.05 | 4.5 |
| Japfa | BUY | 0.56 | 0.80 | 42.9 |
| Keppel Corp | BUY | 6.75 | 7.75 | 14.8 |
| ST Engrg | BUY | 4.17 | 4.32 | 3.6 |
| Yangzijiang | BUY | 1.01 | 1.46 | 44.6 |

Source: UOB Kay Hian

CHANGE IN SHARE PRICE

| Company | Rec | Jan 20 (%) | To-date* (%) |
|-----------------|------|------------|--------------|
| CDL Htrst | BUY | (3.7) | (7.3) |
| CSE Global | BUY | (7.3) | (2.7) |
| DBS | BUY | (2.0) | (6.9) |
| Fu Yu | BUY | 0.0 | 34.0 |
| Keppel Corp | BUY | (1.3) | 7.1 |
| Koufu | BUY | (4.5) | (7.5) |
| Sembcorp Marine | SELL | (12.1) | (13.7) |
| ST Engrg | BUY | 4.3 | 9.2 |
| Yangzijiang | BUY | (15.2) | 5.2 |
| FSSTI | | (2.1) | |

* Share price change since stock was selected as alpha pick

Source: UOB Kay Hian

PORTFOLIO RETURNS

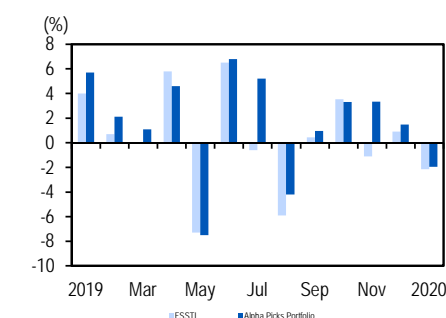
| | 2019 | 1Q19 | 2Q19 | 3Q19 | 4Q19 |
|---------------------------|------|------|------|------|------|
| FSSTI return | 5.0 | 4.7 | 3.4 | -6.1 | 3.3 |
| Alpha Picks Return | | | | | |
| - Price-weighted | 3.0 | -0.4 | 1.2 | 0.4 | 5.4 |
| - Market cap-weighted | 3.4 | -0.3 | 3.1 | -0.5 | 6.1 |
| - Equal-weighted | 8.2 | 5.3 | 2.7 | 2.0 | 7.4 |

Assumptions for the 3 methodologies:

- 1) Price-weighted: Assuming same number of shares for each stock; a higher share price will have a higher weighting.
- 2) Market cap-weighted: Weighting based on the market cap at inception date; a higher market cap will have a higher weighting.
- 3) Equal-weighted: Assuming same investment amount for each stock; every stock will have the same weighting.

Source: UOB Kay Hian

MONTHLY PORTFOLIO RETURNS SINCE JAN-19 (WE OUTPERFORMED FSSTI 9 OUT OF 12 MONTHS IN 2019)



Source: Bloomberg, UOB Kay Hian

ANALYST(S)

Singapore Research
+65 6535 6868
research@uobkayhian.com

Frasers Centrepoint Trust – BUY (Jonathan Koh)

- **Pipeline of assets from sponsor supports next phase of growth.** FCT could acquire: a) the remaining 60% stake in Waterway Point, or b) Northpoint City South Wing from sponsor Frasers Property
- **Strong 2019 results, with positive rental reversions of 5.0%.** Key contributors were Causeway Point (+7.1%), Changi City Point (+5.1%) and Anchorpoint (+5.1%). FCT signed 60 leases with total NLA of 142,103sf in 1QFY20. Shopper traffic increased 8.4% yoy, driven by Northpoint City North Wing (relocation of bus interchange).
- **We have a BUY rating on FCT and a target price of S\$3.05** based on DDM (required rate of return: 6.0%, terminal growth: 2.0%). The company has a strong balance sheet with gearing at 33.2%. During 4Q19, FCT's all-in cost of borrowings improved by 6bp qoq to 2.57% while interest coverage ratio is at a healthy 5.9x.

Share Price Catalyst

- Events: Acquisition of stakes in various suburban malls in Singapore from its sponsor.
- Timeline: 3-12 months.

Food Empire – BUY (Joo hijit Kaur & Clement Ho)

- **Coffee mix market leader in CIS countries with successful diversification efforts.** Food Empire Holdings' (Food Empire) flagship brand, MacCoffee, is the leading 3-in-1 coffee mix brand in Commonwealth Independent States (CIS) countries. With its strong brand equity and broad network of distributors, it commands the largest market share of Russia's coffee mix market. Sales contribution from Russia was about 60% prior to the ruble's collapse in 2H14 but has since fallen to 40%, mainly due to its geographic expansion into regions such as Vietnam and diversification efforts into the upstream business.
- **Successful entry into Vietnam.** Food Empire has successfully gained entry into Vietnam through its iced coffee mix product, Café Pho, which was launched in 2013. Café Pho is among the top 5 leading brands by volume share and a top 3 player based on value share in the Vietnam 3-in-1 coffee mix market. Revenue from Indochina, which includes Vietnam, grew nearly fivefold from US\$10.5m in 2014 to US\$50.4m in 2018. The Vietnam business contributes close to 18% of top-line, making it Food Empire's second-largest market and its stronghold in Asia. We believe Food Empire will be able to continue to gain market share through the introduction of new products, leveraging on its extensive network of distributors and sales representatives in Vietnam.
- **Strengthening margin from cost rationalisation.** Efforts to streamline operations and the exit of its loss-making Myanmar business improved 9M19 reported net margin by 2.6ppt to 9.8%. The group is expected to have record year in 2019 (highest level of reported net profit), underpinned by stable revenue growth coupled with margin expansion. With management's focus on key markets and less of a drag from underperforming markets, margin should continue to trend upwards.

Share Price Catalyst

- Event: Higher-than-expected volume growth, better-than-expected performance of currencies in key markets.
- Timeline: 3-6 months.

Japfa – BUY (John Cheong & Joo hijit Kaur)

- **Vietnam's swine price has exceeded its 5-year high due to the ASF.** We believe the development of African swine fever (ASF) in Vietnam is somewhat similar with China, where the number of affected cases will reach its peak in the first six months and then start to improve. This is also in line with Japfa's base-case scenario. Also, we understand that the affected swine is within Japfa's expectation of <25% of its total swine population.

We estimate that on a net basis, the profitability of Japfa's Vietnam swine segment should benefit, as the spike in swine ASP should more than offset the volume decline. We expect the core profit of this segment to reach US\$28m in 2020, up from only US\$3m in 2019.

- **China's raw milk price has exceeded its 5-year high due to undersupply.** Dairy used to be Japfa's most stable segment due to the stability of raw milk ASP in China. However, the ASP has exceeded its 5-year high since late-3Q19. We believe this is attributable to the undersupply in the market due to a prolonged low ASP environment, which has not incentivised the building of new dairy farms.

Share Price Catalyst

- Event: Better-than-expected prices for Indonesia poultry, China dairy and Vietnam swine products.
- Timeline: 3-6 months.

CSE Global – BUY (JooHijit Kaur & John Cheong)

- **Healthy orderbook and earnings-accretive acquisitions should lift earnings in 2020.** CSE has secured approximately S\$580m (+51% yoy) new orders in 2019 with year-end order backlog exceeding S\$300m – the highest level since 2012. In addition, we expect recent acquisitions to drive growth and earnings in 2020, particularly its acquisition of Volta which we conservatively forecast will make a net profit contribution of S\$3m in 2020.
- **Beneficiary of Smart Nation initiatives in Singapore.** With the government's emphasis on smart nation initiatives and the inclusion of digital defence as part of the overall Total Defence framework, CSE will be able to capitalise on future government tenders in this space. CSE managed to secure approximately S\$60m from security related government contracts in 4Q18; further wins in this area will add to CSE's growth momentum in 2020.
- **Attractive dividend yield at 5.0%.** The group has adopted an absolute DPS payout of 2.75 S cents/share since 2014 and intends to maintain dividend at 2.75 S cents/share for 2019, translating into a generous dividend yield of 5.0%.

Share Price Catalyst

- Event: Large greenfield project wins, accretive acquisitions.
- Timeline: 3-6 months.

Yangzijiang Shipbuilding (Holdings) – BUY (Adrian Loh)

- **On 22 Dec 19, Yangzijiang (YZJ) announced that its chairman Ren Yuanlin would return to the company on 23 Dec 19.** We had believed that the initial share price weakness over the course of Aug-Sep 19 regarding its chairman assisting investigations in China was unwarranted, given that it does not involve the company or its funds, and the first part of our thesis has so far worked out.
- **YZJ's current management ran the company well** while the chairman was away. In particular, Mr Ren Letian, the CEO of YZJ for the past five years and the son of Chairman Ren Yuanlin, has been with the company since 2006 in various roles. With his detailed knowledge of shipyard and shipbuilding operations, the core business did not falter and recorded solid results. Gross profit margin in 3Q19 expanded 0.8ppt yoy to 19.5%, while core shipbuilding margin remained robust at 14%.
- **Positive shipbuilding outlook in the medium term.** New shipbuilding orders for YZJ have mildly disappointed in 2019. However, we remain confident that in the near to medium term, the International Maritime Organisation (IMO) 2020 regulations will lead to new orders for the company. As at end-3Q19, the company had net cash of Rmb4.2b, part of which we believe could be used to pay a special dividend. During its 3Q19 results briefing, YZJ had stated that it would look to scale back some capex in 2020; thus, use of

funds will likely decline yoy. The company is trading at an inexpensive valuation of 0.7x 2020F P/B (-1SD below 5-year average). We have a BUY recommendation on the stock and a P/B-based price target of S\$1.46.

Share Price Catalyst

- New ship-building order announcements, specifically from Japanese shipowners due to the positive synergistic effects of the Mitsui JV.
- Timeline: 2-3 months

Keppel Corp – BUY (Adrian Loh)

- **Temasek's partial offer to acquire an additional 31% of Keppel (KEP) shares appears to have put a 'floor price' on the company** of around \$6.80/share or so. However we still believe there is room for further upside as the company has been executing its plans well. Prior to Temasek's partial offer, Keppel had been investing heavily into new areas (telecommunications and asset management) while its offshore & marine unit has made good headway with targeting new clients in the offshore renewable space.
- **Decent growth outlook.** During its 2019 results, KEP reported that, with the exception of a slight decline in its property segment, all other business units saw yoy operating profit growth. In our view, the company's growth outlook is likely to be robust this year with demand continuing at healthy levels for its China properties, its offshore marine segment looking to increase headcount due to business-activity levels, and the Keppel Marina East Desalination Plant coming close to completion and scheduled to commence operations in the current half year.

Share Price Catalyst

- Event: Continued recovery in new-order flow in 2H19.
- Timeline: 3-6 months.

DBS – BUY (Jonathan Koh)

- **Wealth management continued to outperform in 3Q19.** Fees grew 17.1% yoy, driven by wealth management (+22% yoy). AUM expanded 9% yoy to S\$241b. Contribution from cards and transaction services (cash management and trade finance) also increased 9% and 7% yoy respectively.
- **Hong Kong expected to remain resilient.** DBS Hong Kong services large corporations, including conglomerates in Hong Kong and state-owned companies in China. The bulk of loans is China-related but booked in Hong Kong. The SME book is well collateralised, mainly secured by properties with low LTV ratio. Companies in industries affected by social unrest, such as retail, hospitality and tourism, are primarily depositors and have limited appetite to borrow.

Share Price Catalysts

- Event: Improvement in cost-to-income ratio due to digitalisation and strategic cost management initiatives.
- Timeline: 3-6 months.

ST Engineering (K Ajith)

- **S\$1.3b in M&A in the aerospace and electronics division is expected to be earnings accretive and enable STE to move up the value chain.** The acquisition of nacelle manufacturer MRA system (MRAS) will provide a steady pipeline of OEM aerospace work for the next 10 years. Meanwhile, the acquisition of Satcom firm, Newtec and Glowlink will enhance STE's Satcom capabilities for applications in the aerospace, defense and maritime segments.

- **Scope for higher earnings in 2020.** STE's 4Q19 earnings should also show sequential qoq improvement due to prior quarter's write-down on impairment on intangible assets. Potential positive surprises in next few quarters could include the award of smart utility meter contracts from PUB, an increase in contracts from MRAS due to problems from a competition engine option for the A320 Neo as well as a multi-million dollar replacement contract for Singapore's M113 armour fighting vehicle.
- We have valued STE on an EV/Invested Capital with ROIC at 13.4%, WACC at 5.9% and long-term growth rate of 2.3%. At our fair value of S\$4.32, STE trades at 21.5x 2020F PE.

Share Price Catalyst

- Event: New contract wins for the marine division.
- Timeline: 3-6 months.

VALUATION

| Company | Ticker | Rec | Price 6 Feb 20 (S\$) | Target Price (S\$) | Last Year End | PE | | | Yield 2020F (%) | ROE 2020F (%) | Market Cap. (S\$m) | Price/ NTA ps (x) |
|----------------|-----------|-----|----------------------------|--------------------------|---------------------|-------------|--------------|--------------|-----------------------|---------------------|--------------------------|-------------------------|
| | | | | | | 2018 (x) | 2019F (x) | 2020F (x) | | | | |
| CSE Global | CSE SP | BUY | 0.545 | 0.70 | 12/18 | 13.8 | 12.6 | 10.5 | 5.0 | 14.3 | 276.8 | 1.6 |
| DBS | DBS SP | BUY | 25.70 | 28.65 | 12/18 | 12.0 | 10.5 | 10.9 | 5.0 | 11.5 | 65,640.9 | 1.4 |
| Food Empire | FEH SP | BUY | 0.70 | 0.89 | 12/18 | 15.3 | 10.6 | 9.4 | 1.6 | 14.4 | 375.5 | 1.4 |
| Frasers Cpt Tr | FCT SP | BUY | 2.92 | 3.05 | 9/19 | 27.1 | 25.7 | 25.3 | 4.2 | 5.2 | 3,268.8 | 1.3 |
| Japfa | JAP SP | BUY | 0.56 | 0.80 | 12/18 | 7.5 | 12.3 | 8.9 | 0.9 | 10.1 | 1,043.5 | 1.0 |
| Keppel Corp | KEP SP | BUY | 6.75 | 7.75 | 12/19 | 13.0 | 17.4 | 12.9 | 3.1 | 8.4 | 12,260.6 | 1.1 |
| ST Engineering | STE SP | BUY | 4.17 | 4.32 | 12/18 | 26.3 | 22.8 | 20.7 | 3.8 | 26.4 | 12,989.4 | 6.2 |
| Yangzijiang | YZJSGD SP | BUY | 1.01 | 1.46 | 12/18 | 5.4 | 5.8 | 7.2 | 3.0 | 8.4 | 3,958.0 | 0.7 |

Source: UOB Kay Hian

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