

7-Eleven Malaysia Holdings (SEM MK)

ESG 2.0: Work in progress

HOLD

Share Price MYR 1.98
 12m Price Target MYR 2.10 (+8%)
 Previous Price Target MYR 2.10

Below average ESG rating

SEM's overall ESG score is below average at 41 (out of 100) under our proprietary ESG scoring methodology. The key absence is the group's lack of a long-term commitment in sustainability targets even though it has identified specific areas of concern and are addressing them to minimise the group's environmental impact.

Available data points provided ...

The convenience retail industry as a whole has moderate exposure to environmental and social factors where the industry's main risks lie with the usage of single-use plastics/packaging and handling of food wastages. In this respect, SEM publishes specific carbon emission data points to enable better tracking in its sustainability progress.

... but certain areas should be improved

Although key focus areas have been identified to lower SEM's group wide environmental impact, it has yet to commit to any long-term sustainability targets, similar to its domestic convenience store peers. We believe investors' perception of SEM's ESG compliance will improve once the group begins to commit to concrete targets in relation to sustainable food packaging, renewable energy usage and waste management.

Maintain HOLD with an unchanged TP of MYR2.10

We keep our earnings estimates unchanged. As we expect consumer spending to ease in absence of festive celebrations, sequential earnings are likely to be soft. That said, SEM's efforts to grow its group margins through higher fresh food sales from the expansion in its 7-Café stores should partially mitigate potential earnings downside.

Company Description

7-Eleven Malaysia Holdings Berhad through its subsidiary 7-Eleven Malaysia Sdn. Bhd. is the owner and operator of 7-Eleven stores in Malaysia.

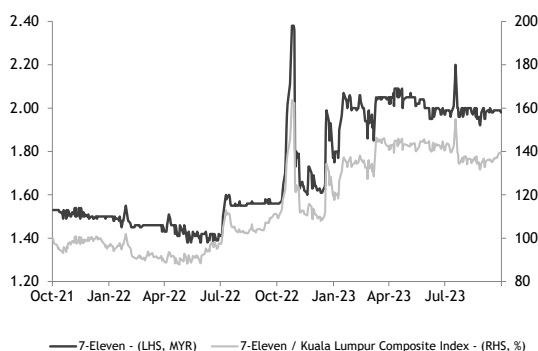
Statistics

52w high/low (MYR) 2.38/1.56
 3m avg turnover (USDm) 0.0
 Free float (%) 36.5
 Issued shares (m) 1,278
 Market capitalisation MYR2.5B
 USD536M

Major shareholders:

TSAI HONG TU 22.8%
 TAN CHEE YIOUN 19.4%
 Berjaya Land Bhd. 5.1%

Price Performance



	-1M	-3M	-12M
Absolute (%)	0	1	27
Relative to index (%)	3	(1)	25

Source: FactSet

FYE Dec (MYR m)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	2,809	3,764	4,343	4,998	5,698
EBITDA	352	416	442	385	392
Core net profit	44	69	75	84	98
Core EPS (sen)	3.9	6.2	6.8	7.5	8.8
Core EPS growth (%)	2.7	56.5	9.8	11.1	17.5
Net DPS (sen)	1.6	3.9	4.2	4.6	5.2
Core P/E (x)	38.1	31.3	29.3	26.4	22.4
P/BV (x)	18.8	15.9	13.5	11.2	9.3
Net dividend yield (%)	1.1	2.0	2.1	2.3	2.6
ROAE (%)	56.6	61.0	50.5	46.5	45.4
ROAA (%)	2.1	2.8	2.8	2.9	3.2
EV/EBITDA (x)	6.4	6.4	5.8	6.4	6.1
Net gearing (%) (incl perps)	264.9	181.6	84.4	37.3	8.1
Consensus net profit	-	-	90	104	110
MIBG vs. Consensus (%)	-	-	(16.2)	(19.5)	(10.6)

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Risk Rating & Score ¹	NA
Score Momentum ²	NA
Last Updated	NA
Controversy Score ³	NA

Business Model & Industry Issues

- ESG risks for convenience stores and pharmacies revolve around the usage of single-use plastics, food wastages and energy consumption. SEM has implemented several measures to reduce its contribution towards plastic pollution and organic waste - however its ability to do so is also subject to the initiatives of its suppliers (eg. larger food manufacturers) to adopt sustainable product packaging for a bigger positive impact to the environment.
- Consumer confidence and brand perception are important factors for the success of consumer retail companies. To that end, SEM ensures that all F&B products sold at its stores abide by product quality and safety regulations. Medicines sold at its pharmacies have also been screened by its internal listing committee.
- SEM's ESG strategy is comparable to its peers, and the industry as a whole has moderate ESG exposure, in our view. Its present ESG disclosure is brief and long-term sustainability targets are noticeably absent. Should SEM share more detailed sustainability metrics/goals, its brand perception would be enhanced, we believe.

Material E issues

- SEM has initiated several energy efficiencies programmes over the years to lower its overall carbon footprint. A cross-docking system was implemented in 2017 which has lowered trip frequency to its convenience stores by 80%.
- The group has converted 100% of its store lighting systems to LED lights.
- SEM implements stringent product management to minimise food wastages at its stores. Hence, the group minimises overstocking, particularly for F&B items with a short shelf life, and uses temperature control settings to avoid food spoilage.
- To reduce plastic waste, SEM has introduced eco-friendly packaging and biodegradable plastic bags at its stores. Styrofoam packaging is also prohibited at all its stores.

Material S issues

- In FY22, SEM employed a total of 12,181 employees with 9,845 employees under their convenience store (CVS) and 2,336 employees under their pharmacy segments. The CVS male:female ratio was 51:49 while its pharmacy segment workforce has 78% female workers.
- SEM implements annual audit targets on its convenience stores to ensure that quality and food standards are upheld. A total of 964 stores were audited in 2022.
- An array of empowerment and donation programmes is conducted through *7-Eleven community care* (i.e. *Semurni Kasih*, *Women of Will* etc.). The group also makes contributions directly to various non-profit foundations.

Key G metrics and issues

- SEM's board of directors (BOD) comprises of 10 members - 4 independent non-executive directors, 4 non-independent executive directors, and 2 executive directors.
- Independent directors make up only 40% of its BOD which is below recommended practise for at least 50% share of independent members. SEM has no plans to revise its board composition for now.
- The BOD male:female ratio was 70:30 in 2022, meeting the recommended industry practise of at least 30% women directors for large companies.
- The chairman and CEO positions are held by separate individuals.
- Annual shareholder's approval is required for independent directors serving beyond 9 years. At present, there are no independent directors who have served beyond 9 years.
- Collectively, the co-CEO's remuneration packages amounted to MYR2.8m (c.2% of SEM's FY22 pre-tax profit) while the BOD's total remuneration package equalled MYR3.4m (c.2.3% of SEM's FY22 pre-tax profit).
- The group does not disclose detailed remuneration of each member of senior management due to confidentiality purposes.
- SEM has been audited by Ernst & Young PLT since its public listing in 2015.
- The group enters recurring related party transactions mostly involving purchases of goods, digital sales of goods (through *Razer Pay*) and rental of properties. Royalty payments typically account for c.1% of total revenue.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Quantitative Parameters (Score: 41)						
	Particulars	Unit	2020	2021	2022	MNHB MK (2022)
E	Scope 1 GHG emissions	tCO2e	1,131	934	945	NA
	Scope 2 GHG emissions	tCO2e	128,715	126,360	136,800	NA
	Total	tCO2e	129,846	127,294	137,745	NA
	Scope 3 GHG emissions	tCO2e	NA	NA	24	NA
	Total	tCO2e	129,846	127,294	137,769	NA
	GHG intensity (Scope 1 and 2)	kgCO2e/tonne	378	394	409	NA
	Electricity consumption	MWh	220,026	215,999	233,846	5,622
	Water consumption	m3	12,791	12,968	14,413	NA
	Recycled waste	Kg	830	780	894	NA
	Cases of environmental non-compliance	No.	0	0	0	0
S	% of women in workforce	%	55%	56%	55%	46%
	% of women in management roles	%	NA	54.2%	56.8%	NA
	Lost time incident rate	No.	0	0	0	0
	Average hours of training/employee	p.a.	20	8	10	NA
	Total invested in the community	MYRm	2.9	4.7	5.3	9
G	MD/CEO salary as % of reported net profit	%	9.3%	5.6%	4.1%	NA
	Board salary as % of reported net profit	%	15.5%	6.8%	5.0%	NA
	Independent directors on the Board	%	44%	33%	40%	57%
	Female directors on the Board	%	33%	22%	30%	29%

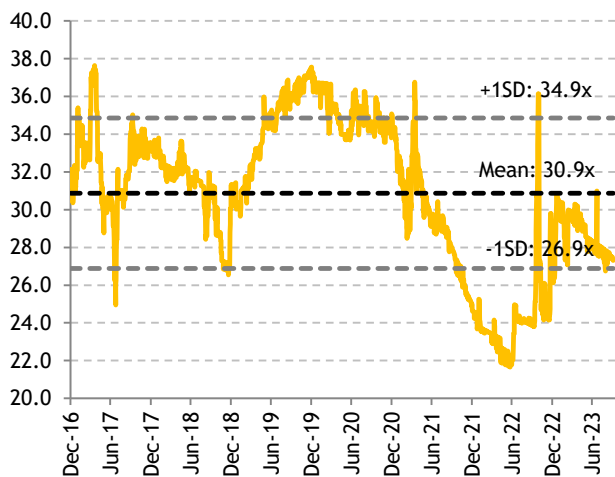
Qualitative Parameters (Score: 83)	
a) Is there an ESG policy in place and whether there is a standalone ESG committee or is it part of a risk committee?	<i>Yes - SEM has developed its own sustainability framework and strategy. Its risk management and sustainability committee was established on 20 April 2022 to better address group ESG risks and it is led by the Board of Directors.</i>
b) Is the senior management salary linked to fulfilling ESG targets?	<i>Yes.</i>
c) Does the company follow TCFD framework for ESG reporting?	<i>Yes.</i>
d) Does the company have a mechanism to capture Scope 3 emissions - which parameters are captured?	<i>Yes - It currently measures the emissions from air travel.</i>
e) What are the 2-3 key carbon mitigation/water/waste management strategies adopted by the company?	<i>SEM has installed energy-saving LED lights and induction lights to 100% of its stores. Air conditioners used in stores are also at least 3 or 4 star ratings in terms of energy efficiencies. The group also implemented its 7E Cross Dock System which minimises the number of delivery trips by individual suppliers to respective stores nationwide, thereby reducing diesel consumption and CO2 emissions.</i>
f) Does carbon offset form part of the net zero/carbon neutrality target of the company?	<i>N/A</i>

Target (Score: 0)		
Particulars	Target	Achieved
SEM currently does not have any formal ESG targets	NA	NA
Impact		
NA		
Overall Score: 41		
As per our ESG matrix, 7-Eleven Malaysia Holdings has an overall score of 41		

ESG score	Weights	Scores	Final Score
Quantitative	50%	41	21
Qualitative	25%	83	21
Target	25%	0	0
Total			41

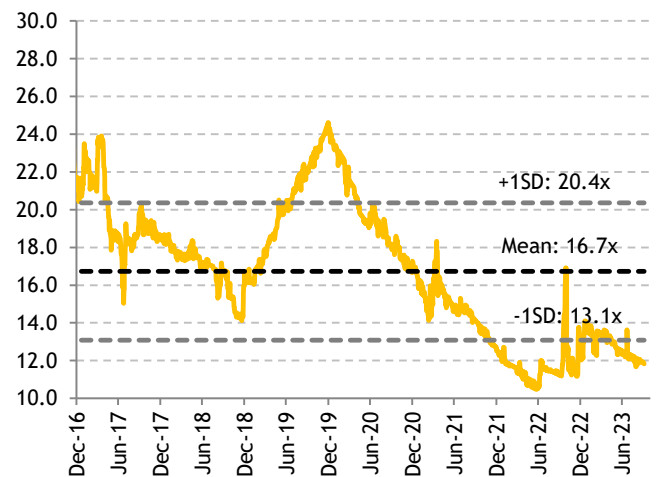
As per our ESG assessment, SEM has implemented a sustainability framework but lacks long-term ESG commitments. For these reasons, SEM's overall ESG score is 41, which makes its ESG rating below average, in our view (average ESG rating = 50; refer to Appendix I for our ESG Assessment Scoring).

Fig 1: One-year forward PER (x)



Source: Company

Fig 2: One-year forward PBV (x)



Source: Company

Risk statement

There are several risk factors for our earnings estimates, target price and rating for SEM. As tobacco sales make up an estimated 30-35% of SEM's total sales, any unfavourable regulatory changes (eg. excise tax shocks) may impact SEM's earnings. Additionally, higher operating expenses through minimum wage hikes could also impact earnings growth.

Appendix I

Methodology of our proprietary ESG scoring methodology.

We evaluate the ESG ratings based on quantitative, qualitative and ESG targets. We assign a score for each of these three parameters. The overall rating is based on the weighted average of the scores: quantitative (50%), qualitative (25%) and ESG target (25%).

For the quantitative, qualitative and ESG target, the sub-parameters are assigned a score - '0' for data not available, '+1' for improving trajectory, positive change, 'Yes', better than peers or a positive number if historical is not available and '-1' for declining trajectory, negative change, 'No', lower than peers or a negative number. The total of the scores of all the sub-parameters is divided by the total number of sub-parameters, to derive the score of each of the three parameters.

The sub-parameters may be different for different industries depending on the key areas to monitor for each industry. A company should achieve a minimum score of 50 for an average ESG rating

FYE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Key Metrics					
P/E (reported) (x)	36.9	25.2	29.3	26.4	22.4
Core P/E (x)	38.1	31.3	29.3	26.4	22.4
P/BV (x)	18.8	15.9	13.5	11.2	9.3
P/NTA (x)	(4.4)	(6.4)	(7.1)	(8.0)	(9.3)
Net dividend yield (%)	1.1	2.0	2.1	2.3	2.6
FCF yield (%)	10.7	14.7	10.9	7.8	7.2
EV/EBITDA (x)	6.4	6.4	5.8	6.4	6.1
EV/EBIT (x)	14.7	12.5	11.9	11.0	9.8
INCOME STATEMENT (MYR m)					
Revenue	2,809.1	3,764.3	4,343.4	4,998.0	5,698.1
EBITDA	351.9	415.6	442.4	385.2	392.4
Depreciation	(197.8)	(202.1)	(226.8)	(161.5)	(148.6)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	154.1	213.6	215.5	223.8	243.8
Net interest income / (exp)	(61.2)	(65.7)	(66.2)	(61.4)	(58.5)
Associates & JV	0.0	(3.3)	(3.3)	(3.3)	(3.3)
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	92.9	144.5	146.0	159.0	181.9
Income tax	(34.1)	(57.8)	(52.6)	(57.2)	(65.5)
Minorities	(14.5)	(18.0)	(18.0)	(18.0)	(18.0)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	44.3	68.6	75.4	83.7	98.4
Core net profit	44.3	68.6	75.4	83.7	98.4
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	158.0	301.0	486.1	598.1	689.4
Accounts receivable	85.8	101.6	117.3	134.9	153.8
Inventory	383.2	453.1	518.4	593.2	674.4
Property, Plant & Equip (net)	322.5	362.0	257.7	237.2	249.3
Intangible assets	473.3	473.4	473.4	473.4	473.4
Investment in Associates & JVs	0.0	9.7	19.1	28.6	38.0
Other assets	828.2	949.7	949.7	949.7	949.7
Total assets	2,250.9	2,650.4	2,821.8	3,015.2	3,228.1
ST interest bearing debt	84.9	77.4	77.4	77.4	77.4
Accounts payable	640.1	863.5	988.1	1,130.6	1,285.4
LT interest bearing debt	555.4	643.3	643.3	643.3	643.3
Other liabilities	789.0	835.0	835.0	835.0	835.0
Total Liabilities	2,068.9	2,419.3	2,543.9	2,686.4	2,841.2
Shareholders Equity	90.0	135.0	163.6	196.5	236.6
Minority Interest	92.1	96.2	114.2	132.3	150.3
Total shareholder equity	182.0	231.2	277.9	328.8	387.0
Total liabilities and equity	2,250.9	2,650.4	2,821.8	3,015.2	3,228.1
CASH FLOW (MYR m)					
Pretax profit	92.9	144.5	146.0	159.0	181.9
Depreciation & amortisation	197.8	202.1	226.8	161.5	148.6
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	(33.1)	133.9	43.6	50.1	54.6
Cash taxes paid	(45.4)	(56.9)	(52.6)	(57.2)	(65.5)
Other operating cash flow	15.0	(1.1)	0.0	0.0	0.0
Cash flow from operations	227.3	422.5	363.8	313.3	319.7
Capex	(46.4)	(106.2)	(122.5)	(141.0)	(160.7)
Free cash flow	180.9	316.3	241.3	172.3	159.0
Dividends paid	(18.0)	(29.3)	(46.7)	(50.9)	(58.2)
Equity raised / (purchased)	(4.2)	(32.9)	0.0	0.0	0.0
Change in Debt	79.9	80.6	0.0	0.0	0.0
Other invest/financing cash flow	(236.7)	(216.7)	(12.6)	(12.6)	(12.6)
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	1.9	118.0	182.0	108.9	88.2

FYE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Key Ratios					
Growth ratios (%)					
Revenue growth	10.6	34.0	15.4	15.1	14.0
EBITDA growth	16.9	18.1	6.4	(12.9)	1.9
EBIT growth	30.7	38.6	0.9	3.8	8.9
Pretax growth	48.3	55.6	1.0	8.9	14.4
Reported net profit growth	49.0	54.8	9.8	11.1	17.5
Core net profit growth	1.2	54.8	9.8	11.1	17.5
Profitability ratios (%)					
EBITDA margin	12.5	11.0	10.2	7.7	6.9
EBIT margin	5.5	5.7	5.0	4.5	4.3
Pretax profit margin	3.3	3.8	3.4	3.2	3.2
Payout ratio	40.7	63.1	62.0	60.8	59.2
DuPont analysis					
Net profit margin (%)	1.6	1.8	1.7	1.7	1.7
Revenue/Assets (x)	1.2	1.4	1.5	1.7	1.8
Assets/Equity (x)	25.0	19.6	17.2	15.3	13.6
ROAE (%)	56.6	61.0	50.5	46.5	45.4
ROAA (%)	2.1	2.8	2.8	2.9	3.2
Liquidity & Efficiency					
Cash conversion cycle	(36.9)	(35.4)	(42.0)	(42.0)	(42.1)
Days receivable outstanding	11.7	9.0	9.1	9.1	9.1
Days inventory outstanding	59.0	55.5	56.4	56.4	56.6
Days payables outstanding	107.6	99.9	107.5	107.5	107.8
Dividend cover (x)	2.5	1.6	1.6	1.6	1.7
Current ratio (x)	0.8	0.9	1.0	1.0	1.1
Leverage & Expense Analysis					
Asset/Liability (x)	1.1	1.1	1.1	1.1	1.1
Net gearing (%) (incl perps)	264.9	181.6	84.4	37.3	8.1
Net gearing (%) (excl. perps)	264.9	181.6	84.4	37.3	8.1
Net interest cover (x)	2.5	3.3	3.3	3.6	4.2
Debt/EBITDA (x)	1.8	1.7	1.6	1.9	1.8
Capex/revenue (%)	1.7	2.8	2.8	2.8	2.8
Net debt/ (net cash)	482.2	419.8	234.6	122.6	31.3

Source: Company; Maybank IBG Research

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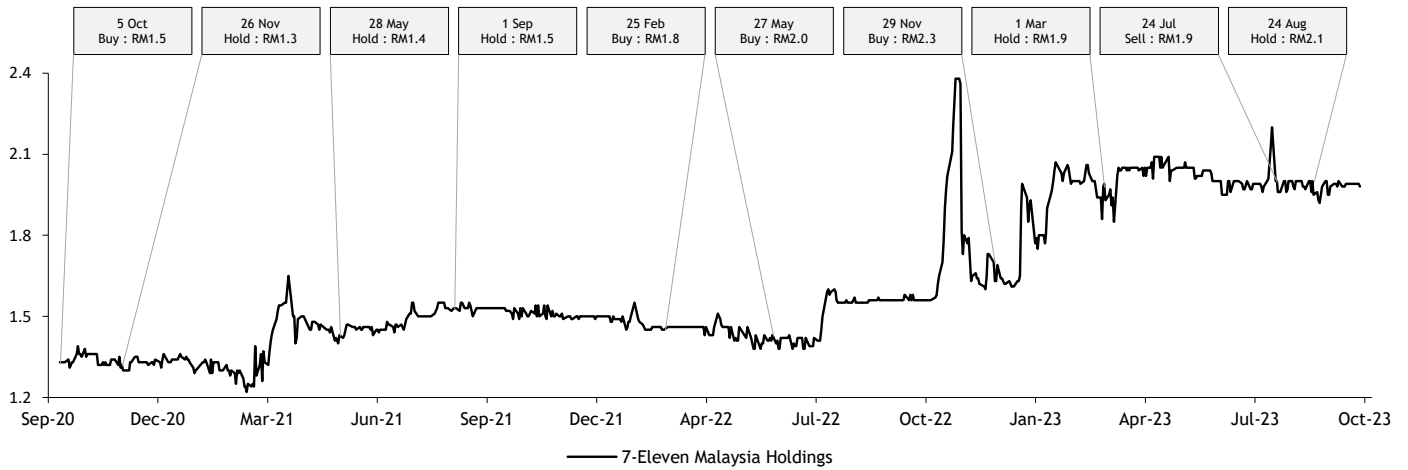
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