



SECTOR RETAILERS

Goods times are over

A slump in building activity will hit the sales of items such as couches and carpets

With national aggregate residential building approvals plunging in recent months, it is an odds-on bet that building activity will soon do likewise. Building always comes after approvals, so if approvals have slumped, it follows that construction activity will too.

Of course, there are serious second-order consequences for retailers of furniture, electronics and other household goods, not least because fewer new apartments being built and sold means fewer couches, tables and carpets.

The construction industry employs 9.6% of Australia's workforce and 37% of that number is employed directly in residential construction. That means 3.5% of the entire workforce may soon face less income or an increase in unemployment.

UBS has reported that residential building approvals have fallen from about 280,000 dwellings to 170,000 most recently – a 40% decline in forthcoming activity, taking into account that construction cannot commence without an approval.

Over the past 12 months we have noted

Adairs share price



Beacon Lighting share price



Temple & Webster share price



in this column the deteriorating outlook for car and furniture retailers. This month we examine the outlook for the retailers exposed directly to the deterioration in sales of household goods, noting that furniture and homewares is a \$13.6 billion market (excluding appliances and DIY).

As you consider these companies, ask not only whether the outlook is deteriorating or improving but what might already be

factored in. It is frequently the case that a deteriorating backdrop is already built into the price and the share price recovers long before business conditions do. And as Godfreys proved last year, even the least loved retailers can receive takeover bids.

Roger Montgomery is the founder and CIO at the Montgomery Fund. For his book, Value.able, see rogermontgomery.com.

Adairs

Adairs is a bedlinen and homewares retailer with a market cap of \$280 million after its share price fell almost 40% from its 2018 highs. In the half year to December 31, 2018, Adairs reported strong like-for-like sales growth but declining margins and cash flows, and consequently analysts downgraded their earnings per share forecasts. Further deterioration in domestic conditions could offset the company's online penetration and online sales gains as well as its overseas sales aspirations.

ASX code ADH

Price \$1.66
52wk \$2.71
52wk \$1.53
Mkt cap \$280m
Dividend 14.5¢
Dividend yield 8.8%
PE ratio 8.7

n SELL

Beacon Lighting

Beacon Lighting's first-half 2019 result was in line with market concerns, but following deteriorating January like-for-like sales the company noted that trading conditions were "unpredictable". Expect those conditions to persist. Indeed, they are unpredictable and not in a positive direction for the reasons explained. Adairs' guidance was for flat profits in 2018-19, which implies a softer second half and the requirement that analysts downgrade. If the predicted slump in construction occurs, further downgrades are likely, possibly delivering an even lower share price than the current PE of nine times.

ASX code BLX

Price \$1.10
52wk \$1.69
52wk \$1.08
Mkt cap \$239mm
Dividend 5.05¢
Dividend yield 4.6%
PE ratio 12

n HOLD

Temple & Webster

Temple & Webster describes itself as the leading online retailer for the home. In the half to December 31, 2018 it reported a 40% year-on-year jump in revenue to \$49.3 million, EBITDA of \$900,000 and a debt-free balance sheet. With only 4% of the furniture and homewares category having migrated online, the long-term thematic appears positive. The share price, however, is up from 15¢ two years ago to around \$1.60 today. Operating leverage will ensure profits grow quickly if sales growth can be maintained, but the reverse will be true if the slump in household goods sales deepens.

ASX code TPW

Price \$1.68
52wk \$1.62
52wk 52¢
Mkt cap \$181m
Dividend -
Dividend yield -
PE ratio 45

n HOLD