Abdullah Al Othaim Markets

Retail – Industrial
AOTHAIM AB: Saudi Arabia
23 October 2016

الراجحي المالية
Al Rajhi Capital

US$0.939bn	66%	US$1.277mn
Market cap	Free float	Avg. daily volume

Target price	88.0	12.5% over current
Current price	78.3	as at 20/10/2016

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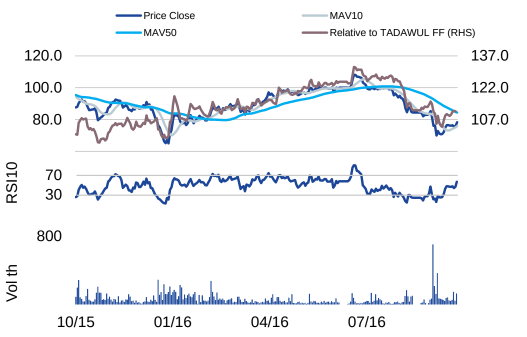
Existing rating

Underweight | Neutral | **Overweight**

Performance



Source: Bloomberg

Earnings

Period End (SAR)	12/14A	12/15A	12/16E	12/17E
Revenue (mn)	5,284	6,036	7,019	8,057
Revenue Growth	15.4%	14.2%	16.3%	14.8%
EBITDA (mn)	304	339	353	393
EBITDA Growth	16.2%	11.4%	4.2%	11.3%
EPS	4.77	5.13	4.97	5.54
EPS Growth	11.6%	7.5%	-3.0%	11.3%

Source: Company data, Al Rajhi Capital

Al Othaim
Q3: Steady performance

Al Othaim reported yet another quarter of robust performance, in-line with our view that it remains one of the safes bets in the current environment due to its higher revenue visibility vs. peers (due to near complete exposure to non-discretionary products) and steady margins. Q3 revenue growth at 17.4% y-o-y was below our estimate of 20.8% growth, however it is still a healthy rate with LFL sales holding up. While SG&A expenses are consistently higher than our estimates for the past few quarters, gross margin expansion is mostly negating the increase in operating costs. On an average, gross margin has expanded 180bps y-o-y for the past 4 quarters, which cushioned the impact of increase in operating costs. Increase in operating costs is generally sticky, except for promotions and costs associated with rolling out new stores. Hence, maintaining gross margin becomes key to sustain operating margin at current levels. We believe strong revenue growth led by aggressive store expansion, resultant scale efficiencies, LFL growth, market share gains, and supply chain optimization will aid Al Othaim to sustain higher gross margin going forward, which should offset majority impact of higher operating costs. Based on our revised estimates post Q3 results, our new target price stands at SAR88 per share (SAR84.2 earlier) and we maintain Overweight rating.

- **Operating and net profit:** Gross margin expanded ~150bps y-o-y which was negated by ~200bps increase in operating costs, resulting in ~50bps y-o-y decline in operating margin. Lower operating profit (SAR29.9mn vs. SAR37.4mn estimate) resulted in a net profit of SAR36.6mn being slightly lower than our estimate of SAR40.7mn. Also, the difference between operating profit and net profit indicates Al Othaim likely realized either higher share of investment income (holds 13.5% share in Al Othaim Real Estate Dev co) or higher other income.

- **Valuation:** Our revised target price (equal weights to P/E based relative valuation and DCF) stands at SAR88 per share (SAR84.2 earlier), implying 12.5% upside and we maintain our Overweight rating. Given persisting risks in the current environment, investors with a bias for safety can prefer staples with high revenue visibility. Almarai and Al Othaim top our pecking order of relatively safer stocks, with near complete exposure to non-discretionary products and in our view, these stocks will continue to command premium valuations vs. peer group and broader market.

Figure 1 Al Othaim: Summary of Q3 2016 results

(SAR mn)	Q3 2015	Q2 2016	Q3 2016	% Chg YoY	% Chg QoQ	ARC Est
Revenue	1,349	2,020	1,583	17%	-22%	1,629
Gross Profit	221	337	283	28%	-16%	269
Gross Profit margin	16.4%	16.7%	17.9%	na	na	16.5%
Operating Profit	32.3	51.3	29.8	-8%	-42%	37.4
Net Profit	37.1	50.3	36.6	-1%	-27%	40.7

Source: Company data, Al Rajhi Capital

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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

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