

AL HOKAIR



EVENT FLASH

Profits decline on weak gross margins

Al Hokair reported a better than expected set of CY4Q16 results. Net income declined 55.6% YoY to SR40mn. This compares to the NCBC estimates of SR37mn. We believe the variance is mainly attributable to higher than expected revenues due to discounts offered. This led to margin contractions and significant decline in profitability. However, Opex declined from 4Q15 levels due to the controlled store expansions, which we believe is a key positive.

- NCBC view on the results:** Al Hokair reported a better than expected set of results, with a net income of SR40mn in CY4Q16, down 55.6% YoY. This is higher than NCBC estimates of SR37mn. The variance is mainly attributable to the higher than expected revenues due to the significant discounts offered to support sales, as domestic spending weakened post-allowance cuts. This led to a contraction in the margins and significant decline in bottom-line.
- Revenues declined 1.7% YoY to SR1,430mn, 16.0% higher than NCBC estimates of SR1,233mn. We believe the better than expected sales were due to the inventory clearance discounts, which the company offered to support sales as domestic consumer spending continues to weaken following the allowance cuts announced during 4Q16.
- Gross profit declined 20.7% YoY to SR313mn, with margins contracting 525bps YoY to 21.9%. The discounts along with inventory provisions led to pressures on margins. Inventory risk accounts for 45% of the total portfolio, which we believe is expected to decline as the management is negotiating better terms to decrease upfront purchases of inventory. Opex declined 5.9% YoY to SR228mn restricting the contraction in EBIT margins to 454bps YoY to 5.9%. EBIT declined 44.2% YoY to SR85mn. This is higher than our EBIT profit and margins estimates of SR68mn and 5.5%, respectively. We believe the lower Opex is due to the sale of the high-costing stores of Blanco.
- Financing charges increased 39.0% YoY to SR43mn vs. our expectations of SR40mn. We believe this is due to the increase in SAIBOR, resulting in the 55.6% YoY decline in earnings to SR40mn.
- We downgraded Al Hokair to Neutral in our latest update, with a PT of SR37.7. This is due to the lower discretionary spending in Saudi following the allowance cuts. We believe the full impact of this will be experienced in 1Q17 for companies selling discretionary products. The stock is currently trading at a CY2017P/E of 16.5x vs. the covered retail stocks 2017 P/E of 15.6x.

CY4Q16 Results Summary

SR mn	CY4Q16A	CY4Q15A	% YoY	CY4Q16E	% Var [^]
Sales	1,430	1,454	(1.7)	1,233	16.0
Gross income	313	394.6	(20.7)	290	8.0
Gross margin (%)	21.9%	27.1%	(5.25)	23.5%	(1.61)
Operating income	85	152.5	(44.2)	68	25.4
Operating margin (%)	5.9%	10.5%	(4.54)	5.5%	0.45
Net income	40	91.2	(55.6)	37	8.6
Net margin (%)	2.8%	6.3%	(3.44)	3.0%	(0.19)
EPS	0.19	0.43	(55.6)	0.18	8.6

Source: Company, NCBC Research [^]% Var indicates variance from NCBC estimates
Please refer to the last page for important disclaimer

NEUTRAL

Target price (SR)	37.7
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Current price (SR)	30.0
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STOCK DETAILS

M52-week range H/L (SR)	53/22
Market cap (\$mn)	1,683
Shares outstanding (mn)	210
Listed on exchanges	TADAWUL

Price perform (%)	1M	3M	12M
Absolute	(17.1)	36.8	(43.5)
Rel. to market	(14.3)	12.3	(63.2)

Avg daily turnover (mn)	SR	US\$
3M	40.7	10.9
12M	36.9	9.9

Reuters code	4240.SE
Bloomberg code	ALHOKAIR AB
	www.fawazalhokair.com

VALUATION MULTIPLES

	FY16A	FY17E	FY18E
P/E (x)	10.2	16.5	17.2
P/B (x)	2.4	2.1	1.9
EV/EBITDA (x)	7.5	8.4	8.8
Div Yield (%)	0.0	0.0	0.0

Source: NCBC Research estimates

SHARE PRICE PERFORMANCE



Source: Tadawul

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NCBC Investment Ratings

OVERWEIGHT:	Target price represents an increase in the share price in excess of 15% in the next 12 months
NEUTRAL:	Target price represents a change in the share price between -10% and +15% in the next 12 months
UNDERWEIGHT:	Target price represents a fall in share price exceeding 10% in the next 12 months
PRICE TARGET:	Analysts set share price targets for individual companies based on a 12 month horizon. These share price targets are subject to a range of company specific and market risks. Target prices are based on a methodology chosen by the analyst as the best predictor of the share price over the 12 month horizon

Other Definitions

NR: Not Rated. The investment rating has been suspended temporarily. Such suspension is in compliance with applicable regulations and/or in circumstances when NCB Capital is acting in an advisory capacity in a merger or strategic transaction involving the company and in certain other situations

CS: Coverage Suspended. NCBC has suspended coverage of this company

NC: Not covered. NCBC does not cover this company

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