Abdullah Al Othaim Markets

Retail – Industrial
AOTHAIM AB: Saudi Arabia
10 May 2017

الراجحي المالية
Al Rajhi Capital

US$1.248bn	66%	US$1.326mn
Market cap	Free float	Avg. daily volume

Target price	111.0	6.7% over current
Current price	104.0	as at 9/5/2017

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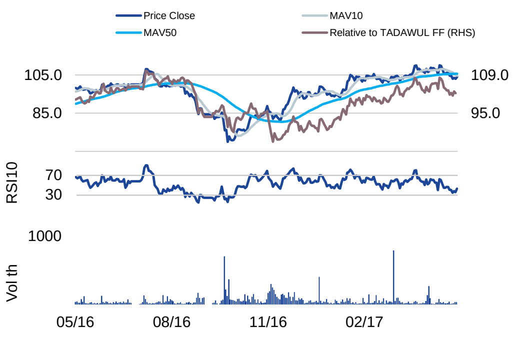
Existing rating

Underweight | **Neutral** | Overweight

Performance



Source: Bloomberg

Earnings

Period End (SAR)	12/13A	12/14A	12/15A	12/16A
Revenue (mn)	4,580	5,284	6,036	7,172
Revenue Growth	11.6%	15.4%	14.2%	18.8%
EBITDA (mn)	262	304	339	381
EBITDA Growth	9.6%	16.2%	11.4%	12.5%
EPS	4.3	4.8	5.1	5.1
EPS Growth	12.1%	11.6%	7.5%	-1.1%

Source: Company data, Al Rajhi Capital

Al Othaim
Q1 2017: Strong performance

Al Othaim's Q1 2017 results were ahead of our estimates. Specifically, SG&A expenses being lower than our estimates was a key positive. For the previous few quarters, Al Othaim's gross margin increase y-o-y offset the increase in SG&A expenses (% of revenue), hence operating margin remained stable/ marginally declined on y-o-y basis. However, in the last two quarters, Al Othaim demonstrated meaningful SG&A control with the result that operating margins were coming in higher than our estimates. While management's opex control is the key driver, one other factor mentioned by the company is improvement in subsidiaries performance as a result of stopping some non-profitable activities. The market is fairly confident of Al Othaim's ability to clock 14-15% revenue CAGR in the next two years while maintaining gross margin (or even gradually improving it; the company has many drivers for the same). However, SG&A expenses, which were consistently increasing for a few quarters was a concern area since the grocery retailing business operates on thin margins (3.3% EBIT margin in 2016). Overall, we believe that the company demonstrating ability to manage margins will lead to higher earnings visibility which could re-rate the valuation multiples. We remain Neutral on Al Othaim with unchanged target price of SAR111.0 per share. Our target price implies 6.7% upside from the current market price.

- **Revenue:** Revenue at SAR1,876mn (+16.8% y-o-y) was lower than our estimate of SAR1,939mn (+18.2% y-o-y, on non-IFRS base of Q1 2016). Aggressive store expansions in the previous few quarters was the primary driver of revenue growth. LFL growth for old stores (excluding Egypt) is ~3% y-o-y by our calculations, which is still a healthy level in the current environment. We build in 3-3.5% y-o-y LFL growth for the next couple of years.

- **Net profit:** Net profit at SAR60.2mn (+29% y-o-y) was higher than our estimate of SAR56.9mn. However, there was a provision of SAR3.5mn in Q1 2017 due to a fire incident at one of the branches. Adjusting for this provision, the net profit would have been higher at SAR63.7mn. Higher operating margin was the key reason for beat at net profit level.

- **Valuation:** We continue to use average of DCF and P/E based valuation to arrive at our target price for Al Othaim. Our unchanged target price of SAR111.0 per share represents 6.7% upside from current market price. Maintain Neutral rating.

Figure 1 Al Othaim: Summary of Q1 2017 results

(SAR mn)	Q1 2016	Q4 2016	Q1 2017	% Chg YoY	% Chg QoQ	ARC Est
Revenue	1,606	1,928	1,876	16.8%	-3%	1,939
Gross Profit	265	363	320	21%	-12%	328
Gross Profit margin	16.5%	18.8%	17.1%	na	na	16.9%
Operating Profit	50.1	105.8	64.4	29%	-39%	53.2
Net Profit	46.6	95.5	60.2	29%	-37%	56.9

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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