Aldrees Petroleum

Oil and Gas – Industrial

ALDREES AB: Saudi Arabia

15 June 2021

Al Rajhi Capital

الراجحي المالية

US$1.360bn	100%	US$7.29mn
Market cap	Free float	Avg. daily volume

Target price	82.00	26% over current
Current price	65.00	as at 14/6/2021

Research Department

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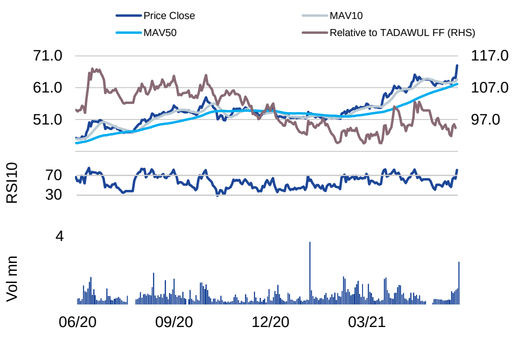
Existing rating

Underweight | Neutral | **Overweight**

Performance



Source: Bloomberg

Earnings

	2020	2021E	2022E
Revenue	4,974	8,195	9,594
Y-o-Y	-12%	65%	17%
Gross Profit	326	403	492
Gross Margin	7%	5%	5%
Operating Profit	188	255	340
Operating Margin	4%	3%	4%
Net Profit	121	140	224
Y-o-Y	-59%	15%	60%
Net Margin	2.4%	1.7%	2.3%
EPS (SAR)	1.62	1.86	2.98
P/E (Curr.)	41.7x	36.1x	22.6x
P/E (Target)	96.6x	83.7x	52.3x

Source: Company data, Al Rajhi Capital

Aldrees Petroleum

Expansion plans to drive profitability; Raise to 82/sh.

Aldrees Q1 2021 net income of SAR39mn came below our estimate of SAR54mn, mainly due to lower revenue compared to our expectations. The revenue increased 21% y-o-y to SAR1.76bn, driven by 22% y-o-y growth in fuel volume. The reported gross margin of 5.81% was similar to Q1 2020 levels but diluted 131bps q-o-q, mainly due to higher depreciation expense related to IFRS 16 and higher labour cost as the number of operated stations increased by 24 during Q1 2021. The operating margins improved slightly y-o-y but declined q-o-q mainly due to the reasons explained above. The gas station industry is undergoing consolidation as the smaller players are either exiting (due to high capex requirement) or leasing their stations to the organized players. Aldrees being a market leader (5.68% market share in terms of the number of stations operated) is leading this consolidation by aiming to operate 1,000 stations by FY2025e. The stock is currently trading at a FY 2022e P/E of 22.6x, which we believe is cheap given the double-digit top-line, and bottom-line growth we expect for the company.

Figure 1 Summary of 1Q 2021 earnings

(SAR mn)	1Q 2021	1Q 2020	Y-o-Y	4Q 2020	Q-o-Q	ARC est	vs ARC
Revenue	1,760	1,458	*21%*	1,497	*18%*	1,909	*-8%*
Gross profit	101	85	*19%*	107	*-5%*	114	*-11%*
Gross margin	6%	6%		7%		6%	
Operating profit	63	52	*23%*	67	*-5%*	77	*-18%*
Operating margin	4%	4%		4%		4%	
Net profit	39	30	*30%*	40	*0%*	54	*-27%*
Net margin	2%	2%		3%		3%	

Source: Company data, Al Rajhi Capital

Increase in the number of fuel stations to drive the profitability and profitability ratios: The number of stations operated by Aldrees has increased by 62 in FY 2020 and it has added another 24 stations in Q1 2021, taking the total number of stations to 568. The company aims to operate 1,000 stations by FY 2025e. This should increase the company's profitability significantly. We expect Aldrees ROCE and ROIC to reach 21% and 20%, respectively (in FY 2020 ROCE and ROIC were 14% and 16% respectively) in FY 2022e because of higher profitability.

Aldrees a pure-play on rising tourism and reopening of school: In FY 2020 due to lockdown the demand for fuel took a nosedive; this delayed the ramp-up of the new stations. However, with the gradual roll-out of vaccines, the local tourism could be higher than the last year, which could lead to a rise in fuel demand. The re-issuance of tourist visas, reopening of flights and resumption of schools are the other near-term catalysts for Aldrees. We expect the fuel volume to grow 18% in FY 2021e.

Overall economic recovery to drive the transportation segment: In the transportation segment, the company handles sugar, chemicals, and oil, and also operates warehouses. In Q1 2021, the transport segment revenue declined ~3% y-o-y to SAR71mn, mainly due to a drop in revenue contribution from Ma'aden (SAR8.1mn in Q1 2021 V/S SAR16.8mn in Q1 2020). However, there was an increase in revenue contribution from the grains segment by 1656% y-o-y

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(SAR10.4mn in Q1 2021 v/s 0.6mn in Q1 2020). We expect the transport segment revenue to improve in the upcoming quarters, in line with the overall economy.

Outlook and Valuation: We like Aldrees as the company is expanding aggressively by opening new stations as well as by entering into profit-sharing agreements with smaller players to operate their stations. This should help the company in increasing its market share further and strengthen its leadership position. We see high barriers to entry for the new players in this industry due to licensing and high capex requirements. With almost 87.5% of the industry is fragmented, the opportunity for Aldrees is huge which may even extend from the current guidance of 1,000 stations by 2025e in our view.

Figure 2 Fuel volume breakup and throughput per station

Ltrs	1Q 2020	4Q 2020	1Q 2021	Y-o-Y %	Q-o-Q %
Diesel					
Volume	401,283	460,477	500,090	25%	9%
Throughput/Station	828	870	899	9%	3%
Petrol 91					
Volume	716,769	815,626	824,038	15%	1%
Throughput/Station	1,479	1,542	1,482	0%	-4%
Petrol 95					
Volume	41,117	71,529	85,613	108%	20%
Throughput/Station	85	135	154	81%	14%

Source: Company data, Al Rajhi Capital

Valuation: The stock is currently trading at a FY 2022e PE of 22.6x, which we believe is cheap given the strong top-line, and bottom-line growth we expect for the company. We value Aldrees using an equal mix given to DCF, PE-based relative valuation, and EV/EBITDA-based valuation methods. Our DCF TP based on 8.28% WACC and 2% terminal growth is SAR93/sh, EV EBITDA based TP based on 13.3x multiple and FY 2022e EBITDA is SAR77/sh and PE-based TP based on 25x FY 2022e EPS is SAR75/sh thus equal-weighted TP stands at SAR82/sh, which implies 26% upside from CMP of SAR65/sh. We remain "Overweight" on Aldrees.

Key downside risks to our valuation:

1) If the new station ramps up slower than our expectations then it will have a negative impact on our revenue forecast and valuations.

2) Traveling ban from certain countries where Aldrees hires the labours to operate gas stations might affect the operation of new stations, which might have downside risk to our valuations.

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