



**US\$1012.5bn** **31%** **US\$0.933mn**  
 Market cap Free float Avg. daily volume

**Target price** **67.00** **+14.52% over current**  
**Current price** **58.50** as at 30/04/2019

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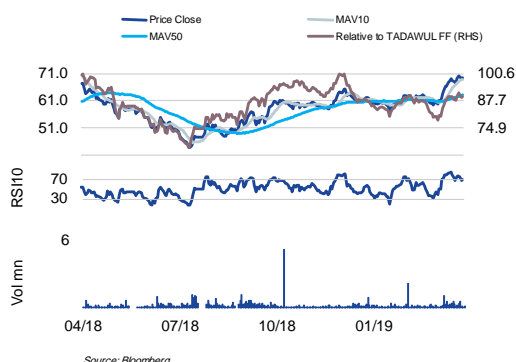
**Existing rating**

**Underweight**

**Neutral**

**Overweight**

**Performance**



**Earnings**

Period End (SAR)	12/17A	12/18A	12/19E	12/20E
Revenue (mn)	1158	1227	1321	1413
Revenue growth	0%	6%	8%	7%
EBITDA (mn)	274	288	307	333
EBITDA growth	-10%	5%	7%	8%
EPS	3.1	3.2	3.6	3.9
EPS growth	-8%	2%	13%	11%

Source: Company data, Al Rajhi Capital

## Herfy Foods

### OW: Raise TP to SAR67

Herfy reported net income of SAR48.1mn (+0.7% y-o-y) for Q1 FY19, missing our and consensus estimates of SAR51mn. The miss in bottom-line was mainly due to higher administrative and marketing expenditure and increase in finance costs due to implementation of IFRS16. The top line came in at SAR313mn (+9.5% y-o-y) beating our estimate of SAR302mn. We believe the top line was driven primarily by LFL growth (vs our expectation of negative LFL sales), increase in the number of restaurants and better than expected performance of meat and bakery segment. Going forward we expect the company's top line to be driven by continued improvement in LFL growth as the consumer sentiments gradually pick up, improving efficiency of the current stores as well as store expansion in new geographies. We expect a revival of consumer spending in food and beverages sector which should improve the LFL growth for the old as well as new stores over the next few years. Our revised forecasts result in an upward revision of the target price to SAR67 per share (earlier SAR56 per share) with an "Overweight" rating. The company's FY19 anticipated dividend yield of ~4% is also attractive.

**Q1 Results:** Revenue increased 9.5% y-o-y to SAR313mn (beating our estimate of SAR302mn), the main reason for the growth in topline is yet to be revealed as detailed presentation is not yet published but as per our assumptions the growth was mainly driven by better than expected performance from restaurants segment (+8.5% y-o-y as per our estimates), well supported by growth in Meat and Bakery segments. Growth in Restaurants sales would have been primarily driven on the back of increase in sales from new restaurants opened in 2018 (25 in 2018), complemented by LFL sales growth (our estimate of +1.2% y-o-y vs -3.2% y-o-y in Q1 FY 2018). Gross profit grew 18.4% y-o-y mainly due to reduction in the cost of goods sold (+6% y-o-y). We believe this decline in COGS is mainly because of the company sourcing most of its raw material needs from its own bakeries and meat factory. As such, gross margin expanded ~150bps y-o-y to 29.1%. The operating profit rose 14% y-o-y to SAR59.2mn, due to higher gross margin and an increase in other income. Despite the higher gross margin and better operating income the net profit was subdued for the higher interest cost due to implementation of IFRS 16.

**Outlook:** Herfy's topline growth of 9.5% y-o-y looks sustainable given the improvement in LFL growth we are expecting on the back of increasing consumer spending on food and beverages. We expect the bottom line growth to pick up due to higher sales and better margins once the impact of finance cost due to IFRS implementation is fully settled. Store expansion (increasing market share) along with LFL growth will remain the key growth driver for the topline. We also expect the bakery business (currently contributes ~10% of the total revenue) to pick some pace and add to the topline as well as bottom-line because bakery is generally a high margin business. Broad based economic recovery and economies of scale should further benefit the company going forward.



**Valuation:** Herfy has a solid payout history, a dividend payout of ~70% over the previous four years (except 2018), thereby implying a dividend yield of ~4% for FY19E. We continue to value Herfy based on equal weights for DCF and P/E based relative valuation. Our DCF based target price is SAR 62.4 per share, assuming 9% WACC (20% debt in capital structure) and 2.6% terminal growth. The P/E based relative valuation at 20x FY19 EPS yields a target price of SAR71.3 per share. The equal weighted target price stands at SAR67 per share, implying a 13.6% upside from current price. We remain “Overweight” on Herfy.

**Figure 1 Herfy: Summary of Q1 2019 results**

(SAR mn)	Q1 2018	Q4 2018	Q1 2019	y-o-y	q-o-q	ARC est
Revenue	286	325	313	9.4%	-3.7%	302
Gross Profit	79	91	94	19%	3.3%	87
Gross margin	28%	28%	30%	8.7%	7.3%	29%
Operating Profit	52	57	59	13.5%	3.5%	53
Net profit	48	52	48	0.6%	-7.6%	51

Source: Company data, Al Rajhi Capital



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