

# United Electronics (Extra)

## Initiation of Coverage Report

**Extra had exceptional revenue growth in 9m2019; reporting double-digit Y-o-Y growth every quarter. We expect further growth for the rest of 2019/2020e; supported by the company's new consumer finance business, e-commerce growth, and Annual Mega Sale in Q4 2019.**

<b>Recommendation:</b>	<b>NEUTRAL</b>
<b>Current Price (06-11-2019):</b>	<b>SAR71.6</b>
<b>Target Price (52 Weeks):</b>	<b>SAR77.3</b>
<b>Upside/ (Downside):</b>	<b>7.9%</b>
<b>Sharia Compliance:</b>	<b>Pass</b>

### Key Points

We start our coverage for Extra with a **NEUTRAL** recommendation and 52 weeks target price at **SAR77.3**; this represents an upside potential of **7.9%**.

- Extra recently penetrated the financial services sector, parallel to its conventional retail business. In May 2019, Extra was the first retail company in the Kingdom to receive approval from SAMA to practice consumer finance business offering personal financing and installment services through its subsidiary United Company for Financial Services (Tas'heel Finance).
- Extra consistently reported double-digit top-line growth every quarter in 2019. Revenue growth reached 15.7% in Q3 2019 (Y-o-Y) and 17.3% for the nine months ended 30 September 2019. However, this growth did not filter into net income in Q3 2019; as a result of cost pressures from the company's new startup Tas'heel Finance, which is still recording losses. Recording of non-recurring securitization losses in Q3 2019 of SAR10.2mn also impacted the company's bottom-line significantly.
- We expect further growth for Extra in 2019/2020, supported by the company's geographic expansion and Like-For-Like sales growth. Penetration in the consumer finance business is also expected to be a key catalyst in the coming years. Moreover, Extra's peak season is yet to come in Q4, where the company will hold an annual mega sale event.

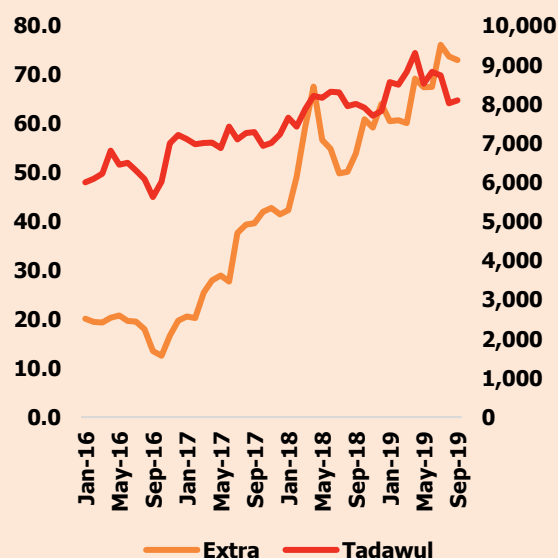
### Key Growth Catalysts

- Credit sales growth
- Penetration of the consumer finance sector
- Partnership with Noon.com

### Key Risk Factors

- A downtrend in the electronics market
- Lack of geographical dispersion of stores

<b>Reuters Code</b>	4003.SE
<b>Bloomberg Code</b>	EXTRA: AB
<b>52 Weeks High</b>	SAR79.40
<b>52 Weeks Low</b>	SAR56.80
<b>Market Cap</b>	SAR3.58bn
<b>P/E</b>	18.2
<b>EPS</b>	SAR3.9
<b>Last Dividends</b>	SAR1.0
<b>AVG Value Traded</b>	SAR317.78mn



# Company Overview

07 November 2019 **Extra**

- Extra was established in Saudi Arabia in 2002 as a retailer of consumer electronics and home appliances. The company was listed on the Saudi Stock Exchange (Tadawul) in December 2011. Extra provides a wide range of electronics products, including mobile devices, laptops, tablets, large and small home appliances, TVs, and gaming consoles. The company also offers furniture and fashion products.
- Today Extra serves more than 12,000 different products to 12+ million shoppers in the Kingdom, Oman, and Bahrain. As of October 2019, the company operates 47 stores; 43 in Saudi Arabia, 3 in Oman, and 1 in Bahrain.
- In addition to the offered products, Extra provides sales support services including installment sales services through its finance program "Tasheel", installation of electronics, warranty services, maintenance services, AC cleaning services, and cybersecurity services for smart devices.
- Extra recently tapped into the financial services sector in Q2 2019, besides its conventional retail business, providing personal consumer finance and installment services. The new business operated through Extra's recently established subsidiary, United Company for Financial Services (Tash'eel Finance).

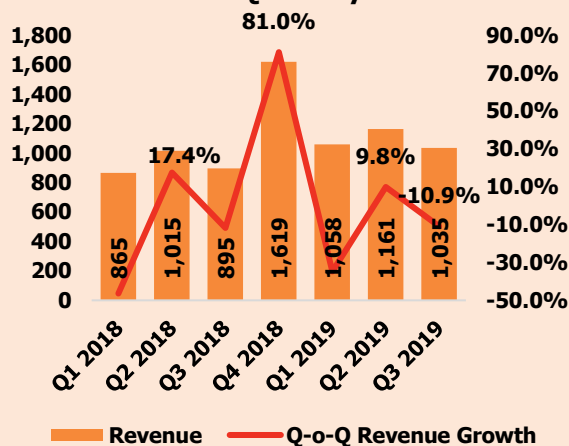
## Revenue at a Glimpse

- Extra's revenue is generated from its electronics and electrical appliances retail business as well as from its financial services business. However, the company only reports revenue segmentation on a geographical basis. The latest revenue segmentation in Q3 2019 shows that 93.6% of Extra's revenue is generated from its stores in the Kingdom, while around 6.4% generated from Oman and Bahrain operations.
- Extra's revenue increased Y-o-Y in Q3 2019 by 15.7%, reaching SAR1,035mn compared to SAR895mn in Q3 2018. For the nine months ended 30 September 2019, revenue grew by 17.3%, supported by geographic expansion, e-commerce sales, LFL sales growth, and credit sales. Extra boosted its market share in the electronics and home appliances market in 2019 by 20%, reaching a 16.9% market share compared to 14.1% a year earlier<sup>1</sup>.
- Extra's revenue experience high seasonality is a result of the company's Annual Mega Sale held at the end of the year, where it offers discounts reaching up to 50%. As a result, Extra's revenues always reach a high peak in Q4 averaging around 90% Q-o-Q growth, and accordingly, Q-o-Q revenue growth is always negative in Q1.

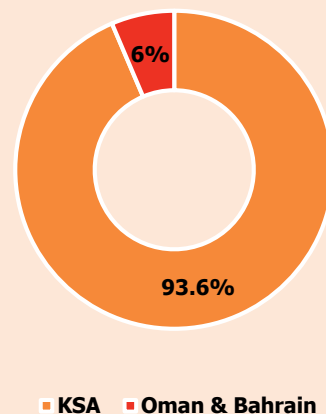
## Key Shareholders

Name	Ownership (%)
Al Fozan Holding Company	29.7%
Public	70.3%

### Extra's Quarterly Revenue



### Geographic Revenue Segmentation (Q3 2019)



Consolidated Subsidiaries	Ownership (%)	Country	Business Activity	Establishment / Acquisition Date
United Electronics Company Extra S.P.C	100%	Bahrain	Electronics trading	2011
United Electronics Company Extra L.L.C	100%	Oman	Electronics trading	2012
United Company for Maintenance Services	100%	KSA	Maintenance, repair & warranty services	2010
United Company for Financial Services	100%	KSA	Consumer finance	2018
Procco Financial Services	100%	Bahrain	Provision of technical financial services	2019

<sup>1</sup> Source: company data

## Key Growth Catalysts

### Credit Sales Growth

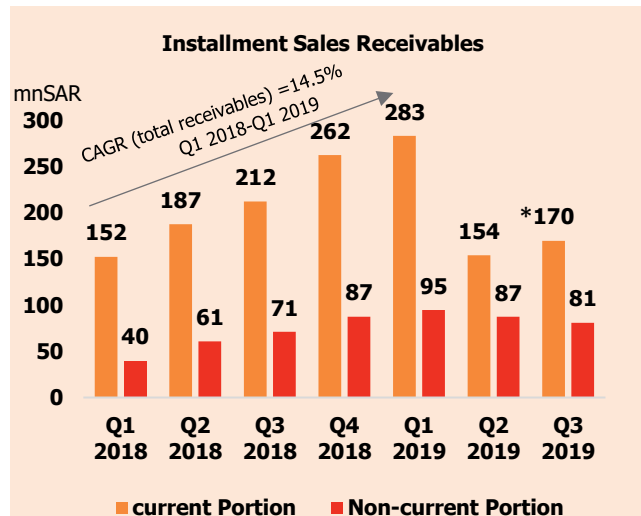
- Extra operates an installment sales program since 2014, providing its own retail customers with product installments up to 24 months and financing up to SAR30,000. Extra's installment program showed persistent and significant growth over the past years and quarters. The company announced its plans to further increase its investments in installments solutions.
- In order to continue its growth momentum in installment sales, Extra signed a securitization agreement with AlRajhi bank in June 2019 to sell a portion of its installment sales receivables worth SAR166mn (representing around 44.0% of the portfolio value). This transaction provides Extra with the opportunity to further grow its installment sales receivables portfolio as a result of increased lending capacity following the sale. According to Extra's announcements, credit sales were one of the key drivers of growth in 2019.

### Penetration of Consumer Finance Sector

- Extra started operating its new consumer finance business, Tas'heel Finance, in Q2 2019. Tas'heel Finance provides its customers with shariah-compliant personal finance loans and installments financing of products/services through a partnership with other corporates and retail outlets. Moreover, the company received preliminary approval from SAMA in October 2019 to launch new credit card financing services. Tas'heel Finance is distinguished with the provision of a convenient online application process where customers can receive instant financing and track their application progress.
- The business is already showing significant growth; according to company data, receivables from the financial services business grew by 122%, reaching SAR73mn in Q3 2019 compared to SAR33mn in Q2 2019.
- According to Research and Markets<sup>2</sup>, unsecured consumer finance market in Saudi Arabia, such as personal loans, is expected to be the highest demand generator in the consumer finance sector in the coming years. Demand for online consumer finance approval is also a developing market trend in the sector. This initiative is expected to be a key growth driver for Extra in the long term as it penetrates a new sector with high growth prospects, along with offering a strategy in line with the market's current trends.

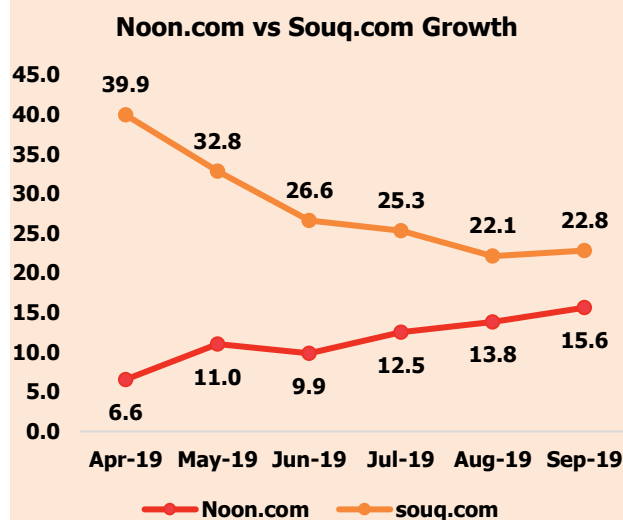
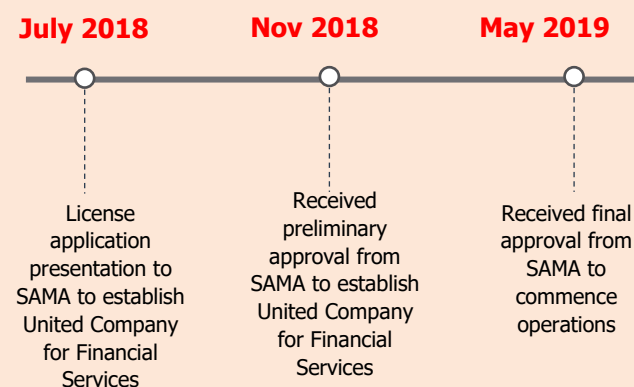
### Partnership with Noon.com

- In November 2017, Extra announced a partnership with noon.com, a leading online shopping website in UAE and Saudi Arabia, to become the exclusive supplier of electronics and home appliances on the company's platform in the Kingdom.
- Noon has already ranked the 35<sup>th</sup> most visited website in Saudi Arabia closely following Amazon and Jarir ranking 33<sup>rd</sup> and 28<sup>th</sup> respectively, even though the company was launched only two years ago. In only 6 months, noon.com total visits increased by 136% to 15.6mn visitors (24% of them are from Saudi Arabia) in September 2019 compared to 6.6mn in April 2019.
- Partnership with such a fast-growing e-commerce company is expected to be a strategic move for Extra to strengthen its position in a highly competitive e-commerce market.



Source: Company Data

\*decline in installment sales in Q2 2019 is only a result of the sale of 166mn worth of receivables



Source: SimilarWeb

<sup>2</sup> Markets & Research is a leading provider of market research reports and industry analysis

## Key Risk Factors

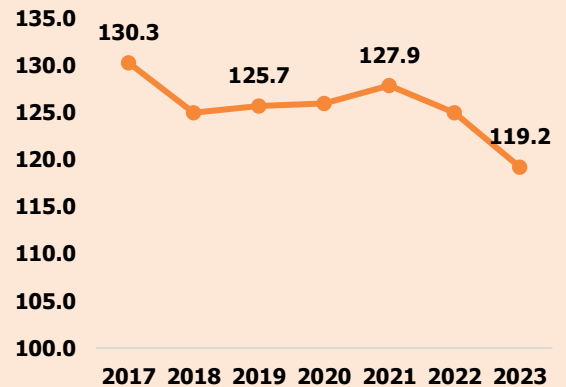
### A Downtrend in Saudi Electronics Market

- Despite the generally positive outlook for the Saudi retail sector, the consumer electronics market is still witnessing negative growth in 2019, according to recent research published by Euromonitor. Being one of the subsectors in the retail sector with the highest elasticities of demand, reduced purchasing power over the past years still has a negative impact on the electronics market in the Kingdom. On the other hand, the research emphasized that market players offering less expensive products are the key winners in 2019.
- The report expects consumer spending power to continue posing a risk on the Saudi electronics sector in the coming years as consumers are reluctant to spend on non-essential products. On the other hand, Extra has the opportunity to exploit such slowdown and turn it into increased market share through its installment sales program "Tasheel".

### Lack of Geographical Dispersion of Stores

- Extra opened a total of 5 new stores during the last three years. The latest stores are in Al Taif, Jeddah, and Al Riyadh. Looking back at Extra's stores per city, Extra has already 8 stores located in Jeddah and 9 stores in Al Riyadh. Some of the stores in these two cities are only 7km away (15 minutes ride). Distance between the stores reaches up to around 50 minutes, and the average distance between the stores is only around 20-30 minutes in both cities.
- Such proximity in stores in one city cannibalizes on the revenues of the old stores already located in these cities, as customers are distributed over the various stores. Meanwhile, such cannibalization may not have an impact on total revenues, it may even yield a low return on investment and dilute the impact of the company's investments.

**Average Revenue Per Customer (Electronics)**



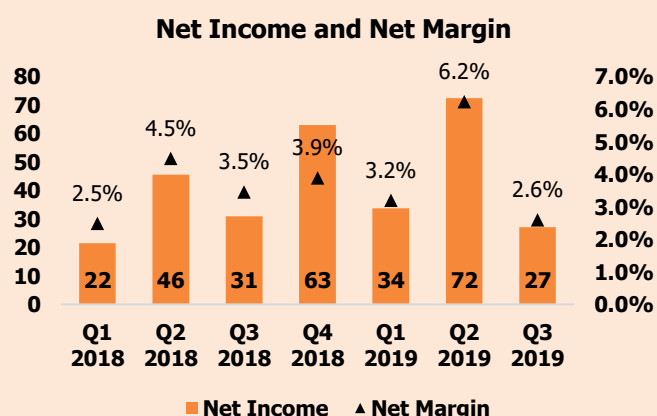
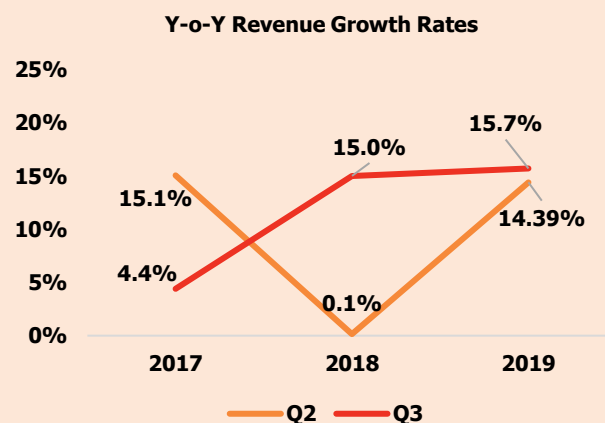
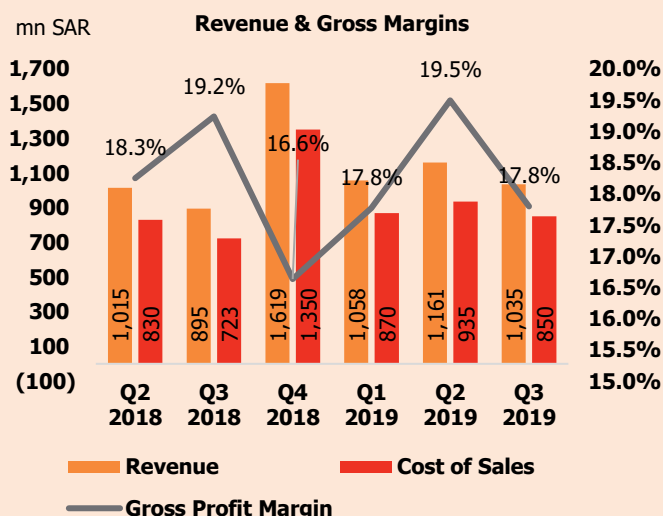
Source: Statista

**Extra's stores in Jeddah**



## Financial Results

- 2019 is an interesting year for Extra so far, where the company outperformed its competitors in terms of Y-o-Y revenue growth, consistently recording double-digit top-line growth each quarter. However, cost pressures are mounting up due to the new consumer finance business Tas'heel.
- Extra witnessed Y-o-Y revenue growth of 15.7%, where revenues stood at SAR1,035mn compared to SAR895mn in Q3 2018. On a quarterly basis, revenues declined by 10.1% due to seasonality factors. Revenue growth is a result of store additions, like-for-like sales growth, rise in credit sales, and an increase in online sales.
- On the other hand, the cost of sales increased by a higher rate of 17.5% Y-o-Y representing 82.1% of revenues compared to 80.8% in Q3 2018. As a result, gross margins dropped 130bps to 17.9% in Q3 2019 compared to 19.2% in Q3 2018. A rise in costs is mainly driven by Extra's new subsidiary Tas'heel Finance, which is still recording losses. Extra's gross profit would have jumped 13.3% in Q3 2019, adjusting for the impact of losses from Tas'heel Finance.
- On the other hand, SG&A decreased by 3.2% Y-o-Y, reaching SAR124mn in Q3 2019 compared to SAR128mn in Q3 2018, as a result of cost cuts in selling & marketing expenses.
- Despite a decline in gross margin by 130bps, Extra reported a steady EBIT margin in Q3 2019, supported by the decline in SG&A. EBIT margin only slightly decreased by 0.2% Y-o-Y recording 3.6% in Q3 2019 compared to 3.8% in Q3 2018. EBIT value increased by 10.1%, recording SAR37mn compared to SAR34mn.
- Securitization deal loss and insurance claims<sup>3</sup> income were booked in Q3 2019 other income, adding up to a loss of SAR5.6mn. It is worth mentioning that the gain of SAR17mn, as a result of the securitization deal, was recorded in Q2 2019. As a result of early booking of gains in Q2 2019, losses of SAR10.1mn were recorded in Q3 2019. On the other hand, net gains of SAR4.5mn from insurance claim proceeds diluted the decline in net income.
- As a result of securitization impact and Tas'heel losses, Extra's net income dropped by 12.0% Y-o-Y to SAR27mn compared to SAR31mn in Q3 2018.
- It is worth mentioning that meanwhile, Extra's net income shows a decline on the surface. It still reported robust financial results in Q3 when adjusted for securitization impact and Tas'heel losses, which collectively added losses of SAR19.3mn to the bottom-line. Adjusting for non-recurring gains/losses including securitization impact and insurance gains, Extra's Q3 2019 net income would stand at SAR33mn (6.1% Y-o-Y growth). When adjusting for Tas'heel losses as well, net income will be SAR42mn, representing 35.7% Y-o-Y growth.



<sup>3</sup> The company received insurance claims of SAR24.2mn (pertaining to a fire incident which took place in 2018) in return for total book loss of damaged assets amounting to SAR19.8mn



## DCF Valuation

	2019 E	2020 F	2021 F	2022 F	2023 F	2024 F
EBITDA	323	369	412	454	500	550
Operating CF	<b>206</b>	<b>238</b>	<b>222</b>	<b>265</b>	<b>308</b>	<b>369</b>
Capex	(82)	(68)	(70)	(72)	(74)	(76)
FCFF	<b>124</b>	<b>170</b>	<b>152</b>	<b>193</b>	<b>234</b>	<b>293</b>
Stub Period (FCF to be discounted)	31	170	152	193	234	293
PV (FCFF)	<b>31</b>	<b>154</b>	<b>127</b>	<b>148</b>	<b>164</b>	<b>187</b>
WACC	8.1%					
Perpetuity Growth	3.0%					
PV-FCFF	31	We have valued Extra using DCF and multiples approaches, considering a WACC is equal to 8.1% (based on a risk-free rate of 4.4%, market risk premium 6.0%, Beta of 1.1).				
PV-TV	3,584					
Net Debt	(72)	Based on the DCF valuation, the fair price of Extra share price is SAR85.2, which is higher than the traded value by 19.0%.				
Less: End of services benefits	(64)					
Add: investments	0					
Intrinsic Value	4,259					
Shares Outstanding	50					
Equity value per share	85.2					
CMP (06-11-2019)	71.6					
Upside / Downside (%)	19.0%					

## Comparable Valuation – Local Peers

Name	Country	P/E
Extra	KSA	18.2
SACO	KSA	17.9
Jarir	KSA	19.3
<b>Median</b>		<b>18.2</b>
<b>Value Per Share</b>		<b>65.4</b>

## Weighted Valuation

Based on a weighted valuation approach, where the DCF is weighed 60%, and multiple valuation is weighed 40%; we value Extra share price at SAR77.3

Valuation Approach	Weight	Value
DCF	60%	85.2
P/E	40%	65.4
<b>Valuation</b>	<b>100%</b>	<b>77.3</b>

# Financial Projection

07 November 2019 **Extra**

## Local Peers

	Country	Code	Market Price (SR)	Market Cap (SRMN)	P/E	Sales (SRMN)	Net Income (SRMN)
<b>Extra</b>	<b>KSA</b>	<b>4003</b>	<b>71.6</b>	<b>3,580</b>	<b>18.2</b>	<b>4,873</b>	<b>197</b>
SACO	KSA	4008	51.7	1,861	17.9	1,440	104
Jarir	KSA	4190	160.4	19,248	19.3	8,167	998

## Financial Ratios

	2018 A	2019 E	2020 F	2021 F	2022 F	2023 F	2024 F
Return on Average Assets (%)	7.9%	7.5%	7.3%	8.5%	9.1%	9.7%	10.3%
Return on Average Equity (%)	28.6%	30.3%	27.9%	31.4%	31.5%	30.9%	30.0%
Income Before Tax Margin (%)	3.9%	3.7%	3.4%	4.0%	4.3%	4.6%	4.9%
Net Income Margin (%)	3.7%	3.5%	3.3%	3.8%	4.1%	4.4%	4.7%
Revenue Growth (%)	4.4%	16.5%	9.2%	8.3%	7.2%	7.1%	7.0%
DPS	1.68	2.25	2.50	2.75	2.75	3.0	3.0
Payout Ratio	52.1%	62.6%	67.9%	59.5%	51.4%	48.8%	42.5%

## Income Statement

	2018 A	2019 E	2020 F	2021 F	2022 F	2023 F	2024 F
Revenues	4,394	5,121	5,591	6,055	6,488	6,947	7,433
Cost of revenues	(3,614)	(4,229)	(4,589)	(4,957)	(5,300)	(5,661)	(6,041)
Gross Profit	780	892	1,002	1,097	1,189	1,287	1,391
SG&A	(600)	(663)	(736)	(794)	(849)	(907)	(968)
Zakat	(8)	(8)	(9)	(10)	(11)	(11)	(12)
<b>Net Income</b>	<b>161</b>	<b>180</b>	<b>184</b>	<b>231</b>	<b>267</b>	<b>308</b>	<b>353</b>

## Balance Sheet

	2018 A	2019 E	2020 F	2021 F	2022 F	2023 F	2024 F
Current Assets	1,376	1,293	1,471	1,632	1,815	2,022	2,271
Non-Current Assets	1,028	1,117	1,126	1,166	1,201	1,231	1,254
<b>Total Assets</b>	<b>2,404</b>	<b>2,410</b>	<b>2,597</b>	<b>2,797</b>	<b>3,016</b>	<b>3,254</b>	<b>3,525</b>
Current Liabilities	1,210	1,158	1,303	1,432	1,551	1,672	1,788
Non-Current Liabilities	635	625	609	586	555	515	468
Total Equity	559	626	686	779	909	1,067	1,270
<b>Total Liabilities and Equity</b>	<b>2,404</b>	<b>2,410</b>	<b>2,597</b>	<b>2,797</b>	<b>3,016</b>	<b>3,254</b>	<b>3,525</b>

# Guide to Ratings and Disclaimer

## Guide to Ratings

<b>Buy</b>	An upside potential of more than 20% in 52-week period
<b>Overweight</b>	An upside Potential of more than 10% in 52-week period
<b>Neutral</b>	Will stay in the range of its value (up/down 10%) in a 52-week period
<b>Underweight</b>	A downside potential of more than 10% in 52-week period
<b>Sell</b>	A downside potential of more than 20% in 52-week period

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