

Saudi Company for Hardware (SACO)

Weak demand impacts SACO's Revenues for Q1 2022, while Road to Recovery Remains Promising

Notable net recovery by SACO after 2 consecutive quarters of net losses. Meanwhile, revenue dropped by 5.0% Y-o-Y due to slower weak demand during Q1 2022. SACO is expected to finalize migration to the new distribution center in Riyadh, which is expected to boost efficiency and support SACO's long-term recovery.

SACO saw a 5.0% Y-o-Y (0.3% Q-o-Q) decline in revenues from SAR336.4mn in Q1 2021 to SAR319.5mn, due to a general decline in demand during the quarter combined with an increase in freight and shipping cost leading to a drop on COGS by only -2.2% Y-o-Y. Gross profit dropped by 16.4% Y-o-Y, leaving gross profit margin at 17.5% for Q1 2022, compared to 19.9% in Q1 2021. (13.1 Q4 2021),

The company's focus on finalizing the migration into two centralized distribution centers (in Riyadh & Dammam) by Q2 2022, led to notable increase in SG&A by 17.7% Y-o-Y (-22.4% Q-o-Q). During the quarter, SACO reported an impairment reversal of SAR3.1mn vs. impairment loss of SAR0.1 in Q1 2021. EBIT for the quarter was SAR12.5mn, a Y-o-Y drop of 54.4% compared to SAR27.4mn in Q1 2021. EBIT margin stood at only 2.9% compared 8.1% in Q1 2021 (-5.8% Q4 2021).

Finance income and other income remained almost flat Y-o-Y, suggesting the drop of income by 92.9% Y-o-Y is mainly due to the significantly high SG&A during Q1 2022, coupled with the higher freight and shipping cost.

Net income margin was only 0.3% compared to 4.6% in Q1 2021.

While having signed a SAR194mn land investment contract in Jeddah in March 2022, SACO announced in May of this year that the contract has been canceled and is expected to have no financial impact on the company.

Moreover, SACO announced a dividend freeze for 2021 to finance the company's working capital and ongoing development projects. The last dividend distribution by SACO was a total of SAR1.25/ share FY2020 (SAR0.5/ share and SAR0.75/ share for H1 2021 & H2 2021, respectively)

Despite the relatively low margins in Q1 2022, we believe that SACO was able to recover significantly from the past consecutive quarters (Q1 2021, Q2 2021), where net losses reached SAR13.9mn and SAR44.7mn, respectively.

The company plans on fully completing the migration to the two centralized distribution centers (DC) by Q2 2022, which is expected to boost productivity and efficiency in terms of accuracy and prompt delivery to customers

within showrooms. It's important to note that SACO's new centralized DC in Dammam is now operational & Riyadh DC is expected to be fully operational end of Q2 2022.

We believe that the company's main focus in FY 2022 is to improve efficiency and recover margins. We expect improvement in the company's top and bottom-line numbers towards Q3 2022, especially with the potential to benefit from growth opportunities through store expansion, introduction of new product categories, new distribution centers, and increased online sales. The only risks are related to pressure on revenues due to the current pressure on purchasing power.

We update our 52 weeks target price for SACO to SAR45.1 /share while maintaining a Neutral recommendation.

08 June 2022

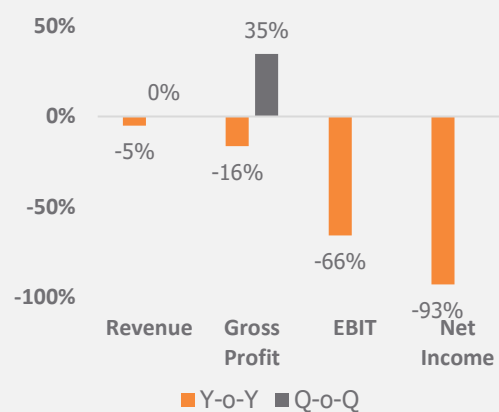
Recommendation Neutral

Previous Recommendation	Neutral
Current Price (07-06-2021)	SAR42.9
Target Price (52 Weeks)	SAR45.1
Upside/ (Downside)	-1.1%
Shariah Compliance	Pass

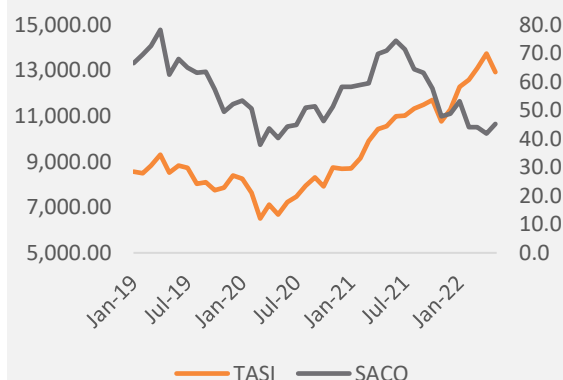
Key Financial Ratios

Ratio	Q1 2022	Q4 2021	Q1 2021
Revenue Growth	0.2%	8.2%	-16.3%
Gross Margin	17.5%	13.1%	19.9%
EBIT Margin	2.9%	-5.8%	8.1%
Net Margin	0.3%	-14.0%	4.6%

Key Financial Results (Q1 2022)



Share Price Performance



Financial Projection

DCF Valuation

	2022E	2023F	2024F	2025F	2026F
EBITDA	275	310	340	370	400
Operating CF	263	273	303	334	365
Capex	(166)	(219)	(220)	(221)	(221)
FCFF	97	54	83	114	143
Stub Period (FCF to be discounted)	73	54	83	114	143
PV (FCFF)	69	48	68	86	99
WACC	7.3%				
Perpetuity Growth	3.0%				
PV-FCFF	369				
PV-TV	2,057				
Net Debt	(769)				
Less: End of services benefits	(42)				
Add: Investments	10				
Intrinsic Value	1,625				
Shares Outstanding (million shares)	36				
Equity value per share	45.1				
CMP (07-06-2022)	42.90				
Upside / (Downside %)	5.2%				

We have valued SACO using DCF approach, considering a WACC is equal to 7.3 % based on a risk-free rate of 2.7%, market risk premium 7.0%, Beta of 1.2).

Based on the DCF valuation, the fair price of SACO share price is SAR45.1, which is higher than the traded value by 5.2%.

Financial Ratios

	2020 A	2021 A	2022 E	2023 F	2024 F	2025 F	2026 F
Return on Average Assets (%)	5.1%	-1.6%	2.5%	4.8%	6.3%	7.5%	8.6%
Return on Average Equity (%)	15.2%	-4.9%	8.6%	15.7%	19.3%	22.0%	24.2%
Earnings Before Zakat Margin (%)	7.0%	-1.3%	3.8%	5.9%	6.9%	7.7%	8.4%
Net Income Margin (%)	5.9%	-2.2%	2.9%	5.0%	6.0%	6.8%	7.5%
Revenue Growth (%)	1.6%	-14.1%	29.8%	9.7%	7.6%	7.0%	6.6%
EPS	2.43	-0.79	1.33	2.49	3.23	3.92	4.63

Income Statement

	2020 A	2021 A	2022 E	2023 F	2024 F	2025 F	2026 F
Revenues	1,482	1,273	1,651	1,811	1,948	2,084	2,221
Cost of Revenues	(1,185)	(1,065)	(1,346)	(1,459)	(1,560)	(1,659)	(1,758)
Gross Profit	296	208	305	352	388	425	463
SG&A	(150)	(180)	(191)	(193)	(202)	(213)	(226)
Zakat	104	(17)	63	106	134	160	186
Net Income	87	(28)	48	90	116	141	167

Balance Sheet

	2020 A	2021 A	2022 E	2023 F	2024 F	2025 F	2026 F
Current Assets	728	777	757	624	596	576	567
Non-Current Assets	910	1,129	1,133	1,202	1,268	1,330	1,389
Total Assets	1,639	1,906	1,891	1,826	1,863	1,906	1,955
Current Liabilities	402	546	558	479	495	508	521
Non-Current Liabilities	627	803	774	761	748	735	721
Total Equity	610	556	559	586	621	663	713
Total Liabilities and Equity	1,639	1,905	1,891	1,826	1,863	1,906	1,955

Guide to Ratings and Disclaimer

Guide to Ratings

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

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