

Abdullah Al Othaim Markets

Target Price: SAR 14.00
Upside/ (Downside): 10.0%

Recommendation

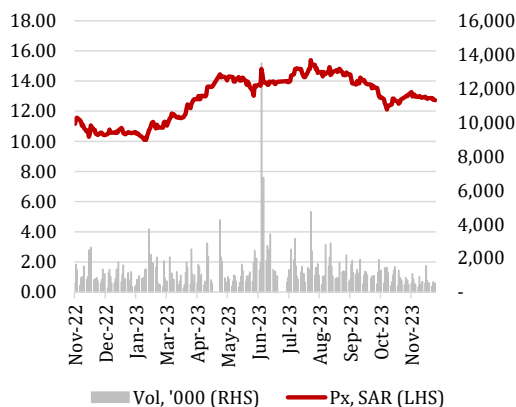
	Hold
Bloomberg Ticker	AOTHAIM AB
Current Market Price (SAR)	12.72
52wk High / Low (SAR)	15.60/10.08
12m Average Vol. (000)	1,200.9
Mkt. Cap. (USD/SAR Mn)	29,765/11,448
Shares Outstanding (mn)	900.0
Free Float (%)	66%
3m Avg Daily Turnover (SAR '000)	12,392.1
6m Avg Daily Turnover (SAR '000)	19,097.7
P/E'23e (x)	23.5
EV/EBITDA'23e (x)	14.8
Dividend Yield '23e (%)	11.8%

Price Performance:

1 month (%)	(1.5)
3 month (%)	(11.7)
12 month (%)	14.0

Source: Bloomberg, valued as of 29 Nov 2023

Price-Volume Performance



Source: Bloomberg

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- Abdullah Al Othaim continues to add new stores at a brisk pace across the length and breadth of the country. Accordingly, we revised our FY23 store count to 394 from 380 previously and expect it to cross 440 stores by FY27 (vs. 428 earlier).
- We raise our FY23 revenue growth estimate to 8.5% from 7.6% earlier while maintaining FY22-27 revenue CAGR estimate at 7% as we opine to open new stores the company will move to smaller towns which generally have lower average per capita spending than larger cities.
- We maintain Hold rating as we believe current valuation levels seem to price in most of the positives leaving limited upside.

We review our coverage of Abdullah Al Othaim Markets and raise the target price to SAR 14.00 (previously, SAR 13.00), as we revise our FY23-27 store count estimates higher, increase FY23 earnings forecast, and lower cost of equity on a decrease in market return expectations. At the current market price, our target price gives an upside of 10.0% and accordingly, we maintain our **Hold** rating on the stock. The stock trades at FY'23e P/E of 23.5x and EV/EBITDA of 14.8x, compared to 12m blended forward 3y daily average P/E of 24.5x, and its 12m blended forward 3y daily average EV/EBITDA of 14.4x.

Investment Thesis

Fundamentals and business prospects remain strong but the current valuation levels seem to price in most of the positives

i) Al Othaim has consistently grown its shopping centers, including during the pandemic period. During 9M 2023, it already has added more stores than in FY22 and hence we lift our FY23 store count forecast by 14 to 394. However, we expect the pace of new store additions to reduce going forward assuming Al Othaim will be reaching optimum store levels at some locations.

ii) We raised our FY23 revenue growth estimate to 8.5% from 7.6% earlier. However, we maintain our FY22-27 revenue CAGR estimate at 7% as we opine to open new stores the company will move to smaller towns which generally have lower average per capita spending than larger cities.

iii) Margins improved in 9M23 and are likely to rise further, with Al Othaim taking various steps like process automation, cost controls, and improved logistical processes to enhance overall cost efficiency.

iv). Improved profitability will support healthy cash flow generation, helping Al Othaim to fulfill its capex and dividend payment needs internally.

Year	FY20	FY21	FY22	FY23e	FY24e	FY25e
Revenues (SAR mn)	8,811.5	8,415.9	9,565.7	10,382.5	11,749.0	12,378.1
Net income (SAR mn)	451.0	300.1	1,079.1	487.8	424.6	490.9
Gross margin	21.7%	21.2%	21.7%	22.1%	21.8%	22.4%
Net profit margin	5.1%	3.6%	11.3%	4.7%	3.6%	4.0%
RoE	29.9%	20.8%	77.8%	35.1%	32.0%	38.8%
FCF (SAR/share)	0.8	0.7	0.9	0.6	0.1	0.3
DPS (SAR/share)*	0.6	0.4	1.2	0.6	0.6	0.6
Dividend Yield**	4.9%	3.7%	11.8%	4.5%	4.5%	4.5%
P/E (x)**	24.5x	32.4x	8.7x	23.5x	27.0x	23.3x
EV/EBITDA (x)**	14.2x	16.0x	11.7x	14.8x	13.7x	12.4x

Source: Company Reports, U Capital Research

*P/E, P/B, and dividend yield from 2023 onwards are based on current price

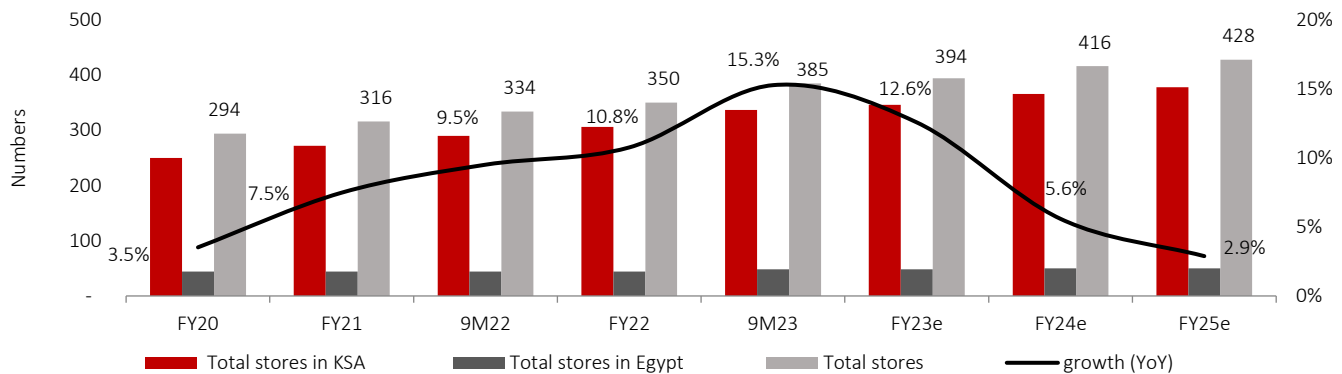
Investment thesis

Al Othaim remains on an expansion spree as it adds more centers in 9M 2023 than in the whole of FY 2022, beating our expectations

Abdullah Al Othaim Markets exceeded our shopping centers' additions estimate of 5 in 3Q 2023 by a noticeable margin as its overall store count increased by 16 during the last quarter. With this, the company established 35 shopping outlets during 9M 2023, one more than in FY 2022, reaching 385 stores. These rapid additions of centers are aligned with the company's ambition to further solidify its already leading position in the Kingdom's retail industry by expanding its geographical footprint. In addition, Al Othaim also eyes to expand its wholesale customer services like restaurants, catering centers, hotels, etc. by setting up more wholesale markets. Accordingly, we lift our FY 2023-end total store count number, including retail stores in Egypt, by 4% to 394 from 380 previously.

We also raise our FY 2022-2027 shopping centers' CAGR for Al Othaim to 5% from the 4% forecasted earlier, considering the recent trend as well as the company's medium-term strategic business plans. However, we expect the pace of new stores' addition to reduce gradually over the next few years as we believe the company might experience some level of saturation in terms of its geographical presence in the Kingdom.

Fig. 1: Al Othaim's ambition to boost its stronghold in the Kingdom's organized retail sector will drive the expansion of its shopping centers' network



Source: Company Reports, U Capital Research

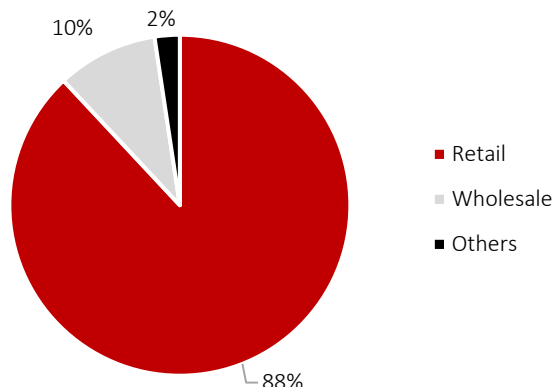
Despite an upward revision in our store addition forecast, top line CAGR estimate for FY 2022-27e is retained owing to a relatively conservative growth expectation of average revenue per store

The sustained rapid addition of new shopping centers by Al Othaim is expected to keep the top line on a healthy growth path over the coming years, underpinned by an overall expansion in the country's retail market led by the government's efforts to boost the Kingdom's attractiveness as a major regional business and tourist hub which should culminate into increased footfalls at the company's stores, given its leading market position. In addition, campaigns and activities run by the company to enhance members of its IKTISSAB loyalty program are equally important in lifting overall store utilization and repeat sales. Accordingly, we forecast Al Othaim's top line to clock 7% CAGR during FY 2022-27e, slightly higher than the 6% CAGR registered during FY 2017-22.

We would like to highlight that although we have revised our store counts higher, we retain our FY 2022-27e revenue CAGR at 7% owing to our conservative estimate of average revenue per store than earlier, as the blended average revenue of retail stores, which accounted for around 88% of the company's top line in 3Q 2023, decreased more-than-expected. In our opinion, to add more retail shopping centers, the company would move to tier-II or tier-III cities where the average household income and spending will lag those in major cities and urban areas.

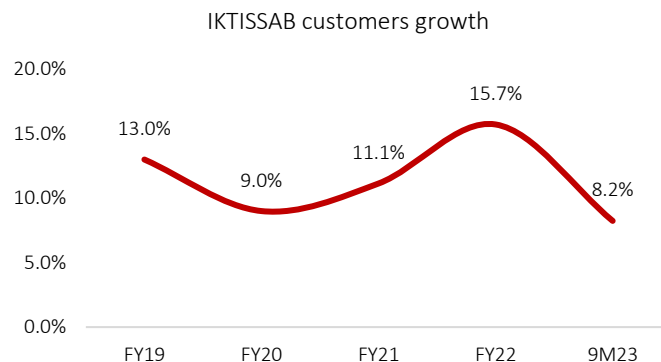
Thus, an increase in the count of such centers with a relatively lower average revenue generation could weigh on the overall blended average revenue per store for the company.

Fig. 2: Retail stores account for the bulk of the company's top-line



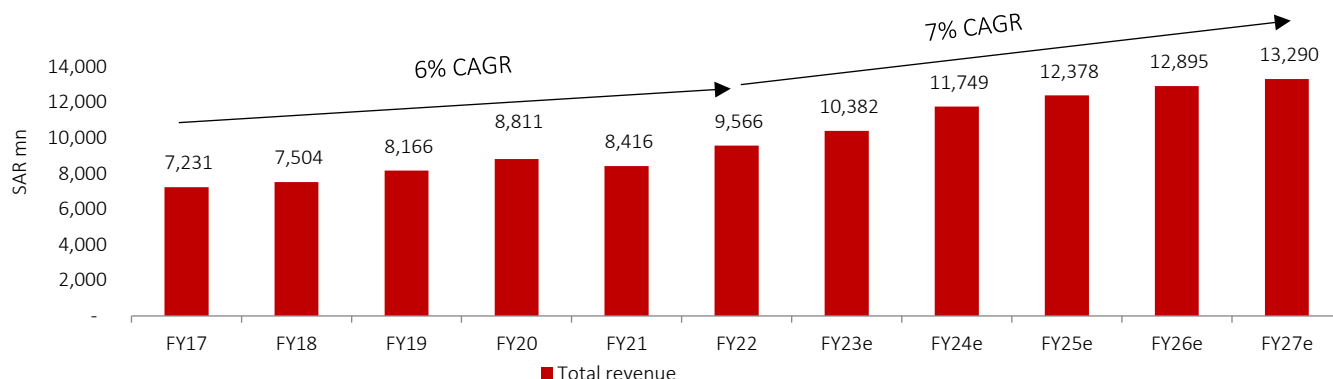
Source: Company Reports, U Capital Research; *for 9M 2023 period

Fig. 3: Members of Al Othaim's loyalty program IKTISSAB continue to expand, boding well for its recurring sales



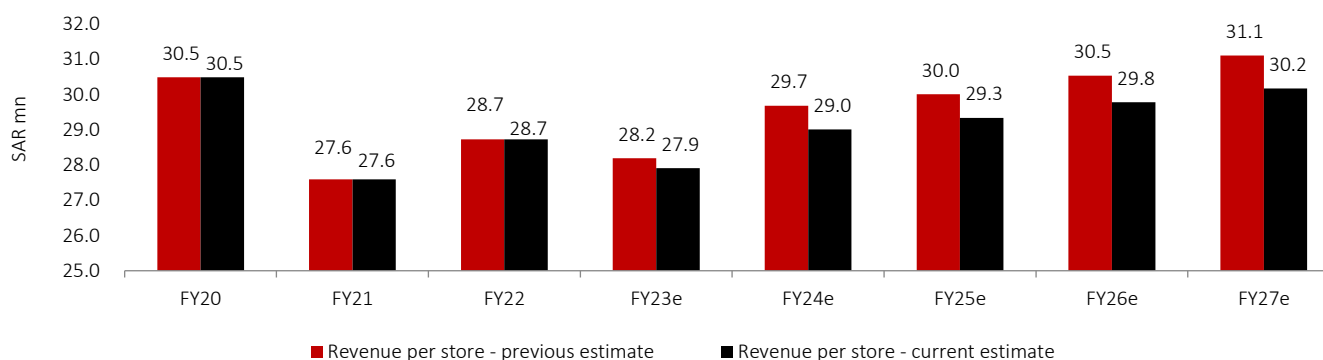
Source: Company Reports, U Capital Research

Fig. 4: Total revenue is estimated to rise at a slightly higher rate than historical average



Source: Company Reports, U Capital Research

Fig. 5: Average revenue per store is revised lower on the premise that will move to smaller towns to further grow its shopping outlets network which are likely to have a lower revenue generation capability than stores in bigger cities



Source: Company Reports, U Capital Research

Efficient cost management supports consistent expansion in gross margin; operating margin is likely to expand in FY 2023 after remaining stagnant over the last two years

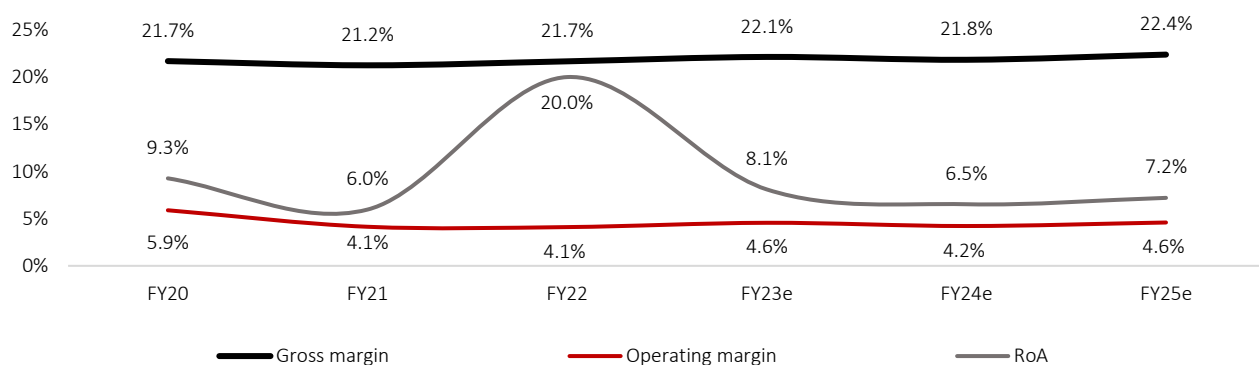
Al Othaim did a commendable job in balancing growth and profitability, in our view, under the difficult operating conditions of the past 2-3 years resulting from the spread of the COVID-19 pandemic. Its gross profit margin (GPM) has consistently improved since FY 2016, except in FY 2021 when it fell slightly, and the trend is expected to continue as the GPM in 9M 2023 rose by nearly 60 basis points (bps) to 21.2%. This showcases the company not only managed the operations of its vast network efficiently but was also able to ramp up its new branches quickly.

Operating profit margin (OPM), after contracting in FY 2021 in the aftermath of the pandemic, remained stable in FY 2022 and appears to expand this year with the 9M 2023 OPM improving to 3.6% from 3.3% in 9M 2022. We believe this was supported by the company's 2026 strategy as a part of which it intends to intensify its cost rationalization efforts, implement diversification plans for its branches, and introduce more automation processes.

Al Othaim is also working to enhance the efficiency of its logistical operations and supply chain management by adopting a multi-pronged strategy, like, strengthening the communication with suppliers and customers by holding regular meetings, joint coordination, etc., improving warehouse management, enhancing the transportation & distribution fleet, among others.

We contend these are good moves to ensure sustained profitability improvement given that after direct costs, selling & marketing expenses account for a major portion of the company's total costs (averaging 16%-17%).

Fig. 6: Cost rationalization effort to keep margins trading higher largely

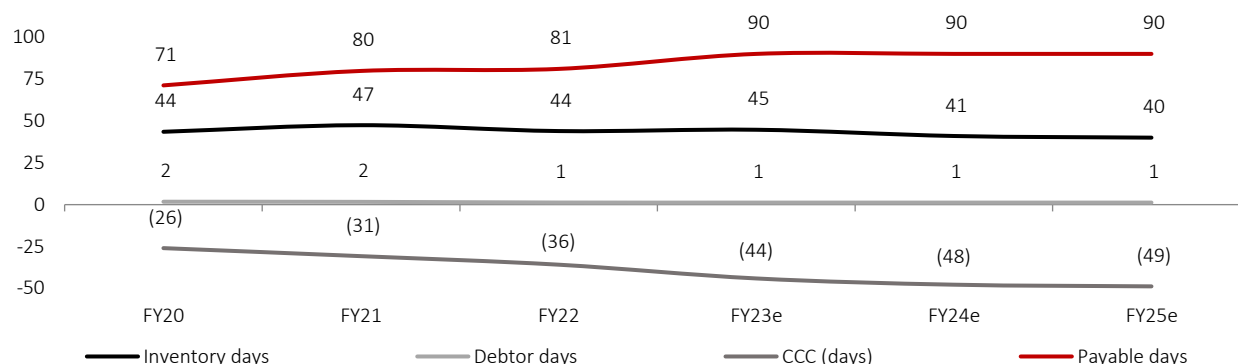


Source: Company Reports, U Capital Research; *The spike in RoA in FY22 is due to a one-off gain

Prudent financial management backed by healthy cash flows to aid the company in meeting its expansion capex requirements internally

Al Othaim has remained debt-free historically despite consistently investing in the rapid expansion of its shopping outlets across the Kingdom, indicating strong financial and working capital management. Given our expectations that the company will remain on a healthy growth path in terms of top-line accompanied by an improvement in profitability, we believe Al Othaim will be able to comfortably fund its future capital expenditure (capex) requirements through internally generated cash flows, without needing to resort to raising loans or borrowings.

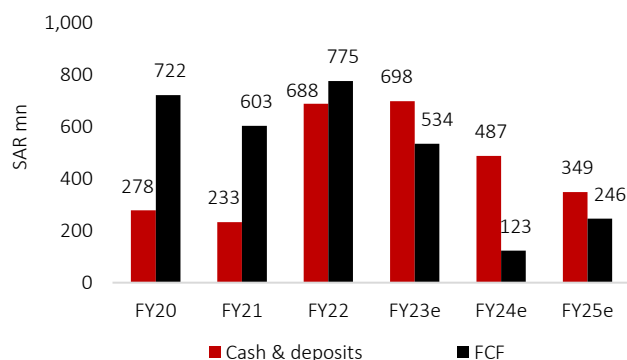
Fig. 7: Efficient working capital management aided the company in maintaining healthy liquidity



Source: Company Reports, U Capital Research

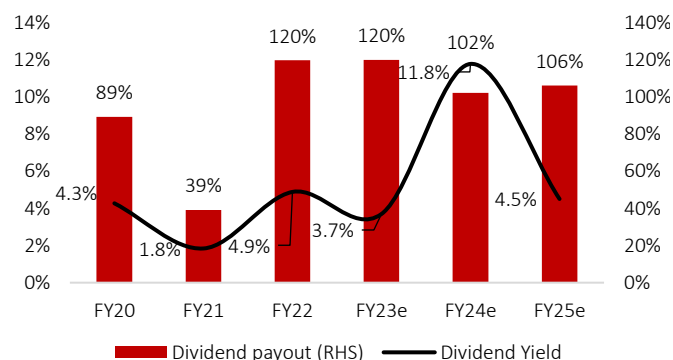
Not only Al Othaim has fulfilled its capex as well as day-to-day business funding requirements through internal resources, but it has also rewarded its shareholders generously. Over the last three years, the company's dividend payout ratio has exceeded 100%, though the FY 2022 dividend payout (DP) ratio of ~102% included the special dividend of SAR 0.75 per share, excluding which the DP ratio reduces to about 40%. Nevertheless, based on our ~SAR 488mn net profit estimate for FY 2023, we expect the DP ratio to surpass 100%. This is considering SAR 0.3 dividend per share (DPS) interim dividend for 1H 2023 (1H 2022: SAR 0.2 DPS), and SAR 0.28 estimated final DPS for 2H 2023, the same as that of 2H 2022. At the current market price, the FY 2023 estimated dividend gives a yield of around 4.5%.

Fig. 8: Strong cash flows strengthened cash balances...



Source: Company Reports, Bloomberg, U Capital Research

Fig. 9: ...aiding the company to dole out generous dividends



Source: Company Reports, U Capital Research

Risks

Key downside risks:

- The ongoing volatile geopolitical situation in the region, if escalates, might adversely impact consumer sentiments and spending, leading to lower-than-estimated average store sales and total revenue.
- Lesser-than-estimated expansion in margins owing to any unexpected cost pressure or newly added branches taking a longer time than usual to reach their optimum utilization level.

Key upside risks:

- We expect the pace of new store additions to gradually decelerate as the company moves to other smaller towns or cities. However, if the company continues to execute store additions at a more than forecasted rate, it could lead to a higher than estimated revenue and/or earnings.

- ii) Al Othaim is taking several steps towards cost optimization which could lead to a more-than-expected expansion in margins.

Valuation

Our target price is based on blended valuation methodologies – (i) DCF and (ii) Relative Valuation (using P/E and EV/EBITDA).

Post the 3Q 2023 earnings outturn, we increase our store count estimates for FY 2023-27, and raise FY 2023 earnings forecast. Also, we estimate a reduced cost of equity on a relatively lower Saudi market return expectation. Accordingly, we revised our target price for Abdullah Al Othaim to SAR 14.00 (previously, SAR 13.00). At the current market price, our target price gives an upside of 10.0% and accordingly, we maintain our **Hold** rating on the stock. Currently, the stock trades at FY'23e P/E of 23.5x and EV/EBITDA of 14.8x, near its 12 months (12m) blended forward 3-year daily average P/E of 24.5x, and its 12m blended forward 3-year daily average EV/EBITDA of 14.4x.

Valuation

	Al Othaim
(Currency)	SAR
DCF (60% weight)	
PV of Free Cash Flow (mn)	
Year 1	532
Year 2	117
Year 3	222
Year 4	315
Year 5	443
Terminal	17,280
PV of Terminal Value	14,037
Assumptions	
Risk Free Rate (%)	5.1%
Adjusted Beta	0.77
Risk Premium (%)	2.9%
Cost of Equity (COE) (%)	7.3%
WACC (%)	5.2%
Equity value (mn)	14,487
Outstanding Shares (mn)	900.0
Target Price	16.10
P/E based Relative Valuation (20% weight)	
Target P/E multiple (x)	21.3
EPS 2023e	0.54
Target Price	11.52
EV/EBITDA based Relative Valuation (20% weight)	
Target EV/EBITDA Multiple (x)	11.9
EBITDA FY23e (mn)	870
Target Price	10.17
Weighted Average Target Price	14.00
Current Market Price	12.72
Upside/(Downside), %	10.0%
Recommendation	Hold

Source: Company Financials, Bloomberg, U Capital Research

Peer Group Valuation

Name	Mkt Cap (SAR mn)	Last Px (LC)	Px Change 1M, %	Px Change 3M, %	Px Change YTD, %	EV/EBITDA'23e, (x)	P/E'23e, (x)	ROE'23e, (%)	Div Yield' 23e, (%)	FCF Yield TTM (%)
Organized Retail										
Bindawood Holding Co.	6,846.6	5.99	-1	-4	24	11.7	25.7	12.5%	2.4%	7.2%
Abdullah Al Othaim Markets	11,448.0	12.72	-2	-12	22	14.8	23.5	35.1%	4.5%	9.6%
Savola	19,703.9	36.90	7	0	34	11.2	19.1	10.1%	2.0%	7.1%
Al Meera Consumer Goods Co.	2,743.0	12.94	1	-8	-16	9.1	13.6	12.3%	34.8%	6.6%
Average						11.7	20.5	17.5%	10.9%	7.6%
Median						11.5	21.3	12.4%	3.5%	7.1%

Source: Bloomberg, U Capital Research, na - not available, nm - not meaningful; *valued as of 29 November 2023

Fig. 10: Organized retail – P/E & Dividend Yield

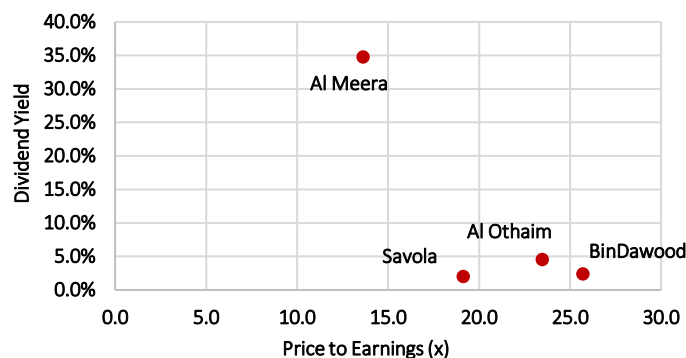
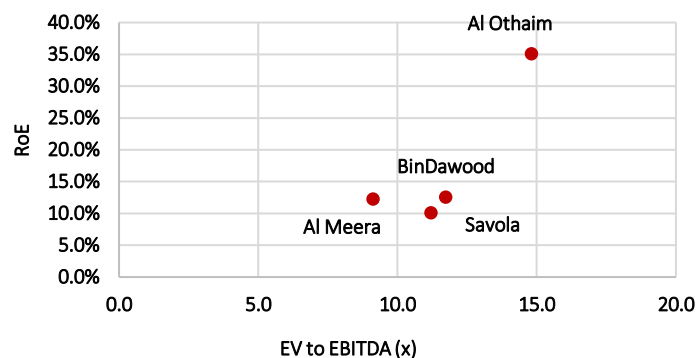


Fig. 11: Organized retail – RoE & EV to EBITDA



Source: Bloomberg, U Capital Research; As of 29 November 2023

Key financials

In SAR mn, except stated otherwise	FY20	FY21	FY22	FY23e	FY24e	FY25e
Income Statement						
Net sales	8,811	8,416	9,566	10,382	11,749	12,378
Cost of sales	(6,900)	(6,628)	(7,493)	(8,085)	(9,184)	(9,608)
Gross profit	1,911	1,788	2,072	2,298	2,565	2,770
General and administrative expenses	(109)	(128)	(150)	(163)	(186)	(197)
Selling and marketing expenses	(1,343)	(1,400)	(1,610)	(1,747)	(1,988)	(2,119)
Rental income, net	57	86	78	83	101	111
Operating profit	519	348	393	473	496	568
Other income (expenses), net	(4)	8	12	10	11	12
Financing charges, net	(1)	(1)	(1)	(32)	-	-
Income before zakat and income tax	469	318	1,113	509	440	509
Zakat	(16)	(11)	(31)	(15)	(13)	(15)
Net income for the period	451	300	1,079	488	425	491
Balance Sheet						
Cash and cash equivalents	278	183	313	643	432	294
Trade receivables, net	42	34	32	37	39	41
Inventories	859	864	940	1,042	1,032	1,053
Right of use leased assets	1,330	1,443	1,615	1,838	2,074	2,268
Property, plant and equipment, net	1,408	1,393	1,511	1,657	1,799	1,923
Total assets	4,965	5,101	5,691	6,357	6,654	6,978
Accruals and other payables	618	617	696	754	820	855
Lease contracts liabilities	1,388	1,528	1,726	1,962	2,214	2,422
Trade payables	1,364	1,536	1,793	2,196	2,266	2,370
Total liabilities	3,396	3,696	4,248	4,943	5,330	5,677
Paid-in share capital	900	900	900	900	900	900
Retained earnings	523	338	267	481	388	361
Equity Attributable to Shareholders	1,524	1,368	1,407	1,373	1,280	1,254
Cash Flow Statement						
Net cash generated from operating activities	887	835	1,023	1,094	994	1,105
Net cash generated from investing activities	(114)	(274)	360	(48)	(939)	(933)
Net cash (used in) provided by financing activities	(758)	(656)	(1,254)	(716)	(266)	(310)
Cash and cash equivalents at the end of the period	278	183	313	643	432	294
Key Ratios						
Gross margin (%)	21.7%	21.2%	21.7%	22.1%	21.8%	22.4%
EBITDA margin (%)	9.7%	8.2%	9.7%	8.4%	8.3%	8.9%
Operating margin (%)	5.9%	4.1%	4.1%	4.6%	4.2%	4.6%
Net margin (%)	5.1%	3.6%	11.3%	4.7%	3.6%	4.0%
ROA	9.3%	6.0%	20.0%	8.1%	6.5%	7.2%
ROE	29.9%	20.8%	77.8%	35.1%	32.0%	38.8%
Current Ratio (x)	0.7x	0.6x	0.7x	0.7x	0.6x	0.5x
Capex/Sales	1.6%	1.8%	3.0%	3.7%	7.1%	6.7%
Debt-Equity Ratio	0.9x	1.1x	1.2x	1.4x	1.7x	1.9x
EPS	0.5	0.3	1.2	0.5	0.5	0.5
BVPS	1.7	1.5	1.6	1.5	1.4	1.4
DPS*	0.6	0.4	1.2	0.6	0.6	0.6
Dividend Payout Ratio	119.7%	120.0%	102.2%	106.1%	121.9%	105.4%
Dividend Yield (%)	4.9%	3.7%	11.8%	4.5%	4.5%	4.5%
P/E (x)	24.5x	32.4x	8.7x	23.5x	27.0x	23.3x
P/BV (x)	7.3x	7.1x	6.7x	8.3x	8.9x	9.1x
EV/EBITDA (x)	14.2x	16.0x	11.7x	14.8x	13.7x	12.4x
Price as at period end**	12.3	10.8	10.4	12.7	12.7	12.7


Source: Company Reports; *Current market price is used for forecast periods


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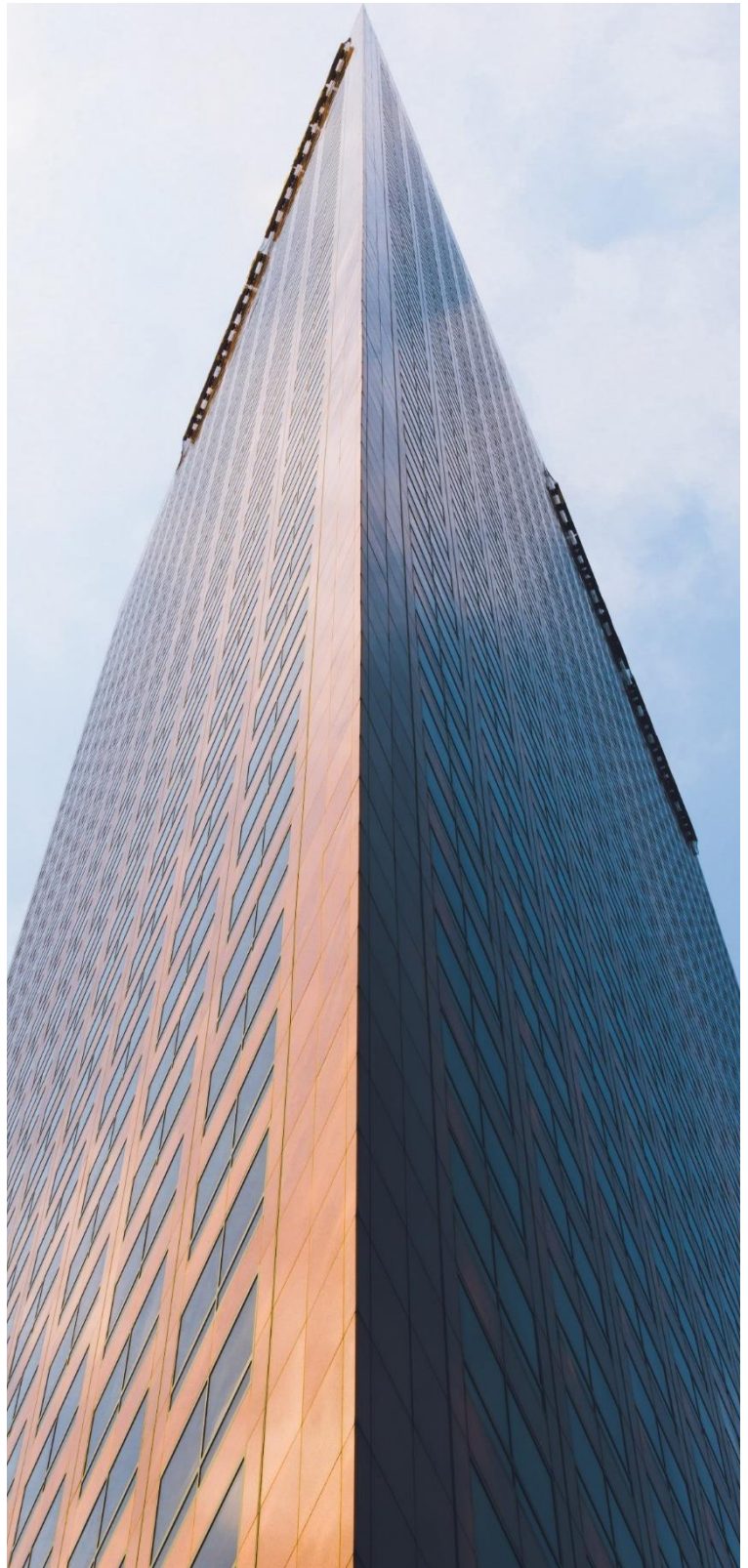
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Recommendation

BUY	Greater than 20%
ACCUMULATE	Between +10% and +20%
HOLD	Between +10% and -10%
REDUCE	Between -10% and -20%
SELL	Lower than -20%

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