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Larger audience outdoors, and more sites to advertise at- all signs for AlArabia's coming chapter

AlArabia Contracting Service | Initiation Coverage Report

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Arabian Contracting Services Co. (AlArabia): Initiation coverage with an "Overweight" rating and a TP of SAR 137.0/share

The firm's strong hold on the outdoor advertisement segment's market share, coupled with the Kingdom's entertainment and tourism initiatives to attract a wider population and offer more reasons to be out-of-home, and AlArabia's campaign towards digitalizing their services, places AlArabia favorably as the advertisement needs will follow the increase influx in population and activities. Moreover, at AlArabia's current valuation, with strong return profile (ROE and ROA) is recognized as an attractive stock with its current specifications. Thus, we initiate our coverage on the stock with "Overweight" rating and a TP of SAR 137.0/share.

- **A proven track record:** AlArabia, despite facing the friction of COVID-19 restrictions, displayed strong revenue growth, recording an expected 5-year CAGR of 14.22% from FY18 to FY22E along with a net profit CAGR of 16.8% for the same period. The growth was led by increase in demand for their roadside advertisement services, the segment which the firm currently concentrates its operations towards, as well as an increase in demand and activity on their indoors services segment. AlArabia has more than tripled its indoor segment contracts from 2020 to date (25 contracts from 8).
- **Robust growth in topline to continue:** With the sector drivers in place and supported by AlArabia's leading market share of the segment, we see the inertia behind the company's revenue to drive it towards a CAGR of 9.89% from FY22's end to FY26. Government initiatives, more people tending to be outdoors (18.5% increase time spent at retail and leisurely areas from February 2022), and more digitalized billboards offering expanded services to clients (66% of faces currently digital, to reach 80% in FY25) are all supportive factors for AlArabia's growth in coming periods.
- **Ability to generate high returns, and digitalization-supported margins will auger well for AlArabia's profitability:** The company recorded high return on equity utilizing relatively lesser gearing than its peers. This earmarks its profitable efficiency of AlArabia. We expect the company to maintain its healthy return profile in coming years driven by healthy margins and efficient use of capital (ROIIC of 8.12% from FY17 to FY21). We forecast ROAE to average at 36.3% and ROAA at 11.0% during FY22E-24E. With 66% of faces digital, the amount of billboards will come down, with more faces (panels) to be displayed with less human intervention and more services offered. We anticipate gross margins to expand by 288bps by 2027 from 39.1% in 9M-22.
- **The acquisition of 100% of Faden Media, if completed, will be quick to reap the benefits, as we expect Faden to contribute an annualized net SAR 1.76 per share (SAR 88mn) to AlArabia's investors.** Faden Media could become a vessel for AlArabia to expand into building advertisement (large ad faces covering a building) and in Transit advertisement (in travel hubs) through Faden's subsidiary Wave Media, in which Faden owns 42.5%. Faden and Wave media together claimed 12.1% of the outdoor advertising market share in 2020. At historical rates, they both offer an implied 6.18% of market share which is likely to grow as a result of synergies among them.

AJC view and valuation: AlArabia is positioned to reap the benefits of increased out-of-home activity in the Kingdom as it sits at a dominant share of the outdoor advertising market. Its digitalization campaigns have offered more to its clients, attracting a larger demand at better margins. We value AlArabia with 50% weightage to DCF (Rfr = 4.0%, terminal growth = 2.5%, average WACC = 7.1%) and 50% weightage to FY23E P/E (18x). This yields a TP of **SAR 137.0/share**. Thus, we initiate our coverage on the stock with "**Overweight**" rating.

Upside risks: 1) Increase in population's time outdoors in the Kingdom driving demand for advertisement 2) Digitalization of billboards 3) Faden Acquisition to grant more market share and synergies. **Downside risks: 1)** Concentration towards government lease contracts 2) inability to ay leases on time 3) less demand for outdoor activities resulting from a slowdown in population influx.

Recommendation	**Overweight**
Target Price (SAR)	**137.0**
Upside / (Downside)*	**26.9%**

Source: Tadawul *prices as of 23th of January 2023

Key Financials

SARmn (unless specified)	FY20	FY21	FY22E	FY23E
Revenue	498	720	1,091	1,242
Growth %	-36.8%	44.8%	51.5%	13.9%
Gross Profit	99	330	435	492
Net Income	25	206	283	344
Growth %	-88.8%	718.4%	37.3%	21.4%
EPS	0.5	4.1	5.7	6.9

Source: Company reports, Aljazira Capital

Key Ratios

	FY20	FY21	FY22E	FY23E
Gross Margin	19.9%	45.9%	39.9%	39.6%
Net Margin	5.1%	28.6%	26.0%	27.7%
ROE	4.8%	32.8%	35.9%	38.4%
ROA	2%	6%	9%	11%
P/E (x)	NM	NM	18.9	15.7
P/B (x)	NM	NM	6.3	5.7
EV/EBITDA (x)	NM	NM	8.5	7.4
Dividend Yield	NM	NM	3.2%	4.5%

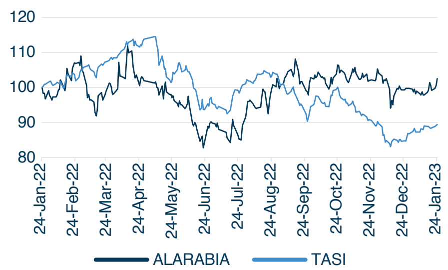
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (SAR mn)	5,400
YTD	1.1%
52-week (High)/(Low)	127.0 / 89.5
Share Outstanding (mn)	50.0

Source: Company reports, Aljazira Capital

Fig 1: AlArabia's Price Performance (Rebased)



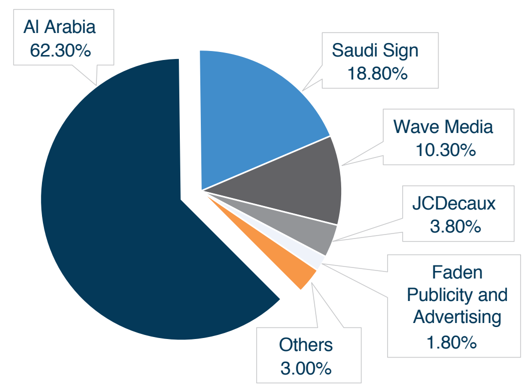
Source: Bloomberg, AlJazira Capital

Company Overview

Arabian Contracting Service (AlArabia) was established in 1983 and has been trading on Tadawul's main market since 2021 within the Media & Entertainment sector, along with its peers. The firm leads in the Saudi advertising market and is highly positioned on global advertisement leaderboards as well. AlArabia's advertisement activities are concentrated towards outdoors advertising (referring to out-of-home or public advertisings) to service their diverse clientele through roadside advertisements, indoor advertisements (displayed in shopping centers and indoors public areas), airport and transit advertising, as well as well as printing services.

Fig 1: Share of KSA outdoors advertising (2020):

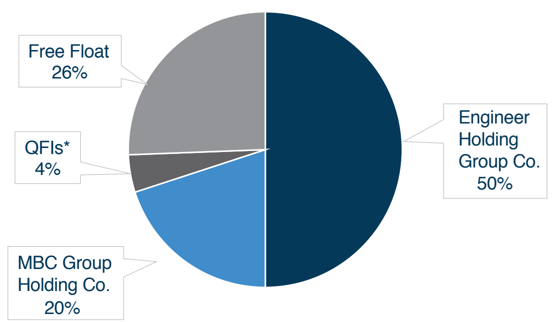
Rank	Company	Market Share
1.	Al Arabia	62.30%
2.	Saudi Sign	18.80%
3.	Wave Media	10.30%
4.	JCDecaux	3.80%
5.	Faden Publicity and Advertising *	1.80%
6.	Others	3.00%



Sources: Company Data. AlJazira Capital. | * AlArabia signed an agreement to fully acquire Faden Media. The SAR 1.05bn acquisition is currently pending regulatory approvals.

Engineer Holding Group are AlArabia's largest shareholder, followed by television production group MBC Group Holding Company- AlArabia's ownership from a media company grants the firm strategic and operational synergies as the firm is able to offer services beyond its direct operations to its clients through its affiliated entities. Through MBC's reach and its subsidiaries such as SMC, AlArabia is able to bundle packages to its clients that expand past AlArabia, and onto radio and television among other mediums.

Fig 2: AlArabia's Ownership Structure:

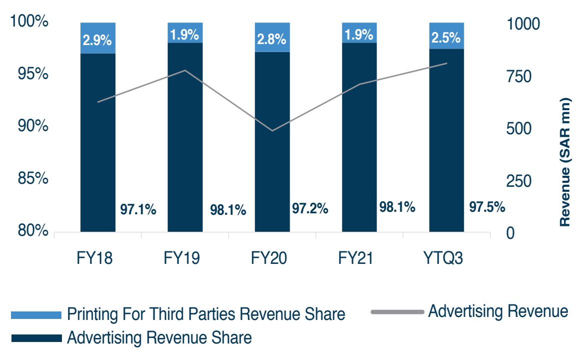


Sources: Company reports, AlJazira Capital *Qualified Foreign Investors

AlArabia's Operations and Business Segments:

The firm's operational activities are concentrated around the outdoor advertisement business; which as of FY21 constituted 98.1% of AlArabia's total sales, the majority of which is from roadside advertising services. The rest of the firm's revenues stem from the firm's printing activities. (Printing revenues associated with AlArabia's Advertisement campaign services are recorded under revenues from the Advertisement segment). On average (from FY18 to FY20), approximately 27.0% of printing services were for third party advertisement campaigns.

Fig 3: AlArabia's Revenue Streams:



Sources: Company reports, AlJazira Capital

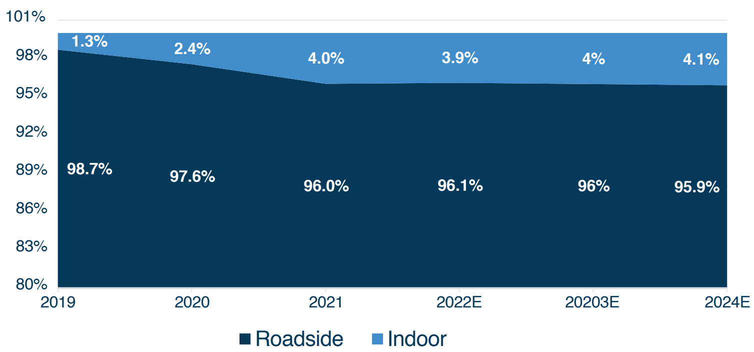
AlArabia's segments are described below:

1. **Roadside Advertisement:** The firm bids for contracts (mainly from government municipalities and secretariats) to lease out the sites offered, and install the required billboard type for that tender. The terms of the tender include a one-month grace period (after being awarded the bid) to grant the firm time to pay the first year's rent for the site, and before finalizing the contract. During that time, the firm is granted a leeway to exit the agreement, as AlArabia has done in a recent Jeddah deal in order to allocate their resources to a more favorable tender. The maximum term for a lease is 10 years. The firm operates almost a dozen different types of billboards; some having static dual faces with posters that need to be changed (such as the 'Mupi billboards), while other billboards able to digitally display 10 different faces that are controlled remotely (such as the 'Meza' billboards). The majority of the firm's revenues are from this segment (at an estimated 96.1% for FY22).

    a. **Indoor Advertisement:** In 2019, AlArabia began extending the range of its operations by entering indoor advertising market. As of Q3-FY22, AlArabia was engaged in 25 contracts under this sector (almost tripling its indoors contracts count in 2020), where the firm displays advertisements on billboards installed inside commercial centers.

2. **Printing services:** AlArabia's print shops serve printing for the advertisement campaigns displayed by the firm (for the most part, as 73% of prints were for AlArabia campaigns from FY18 to FY20 on average). Otherwise, the firm also runs printing services for third party advertisement campaigns run by other firms, as well as printing business cards and other confectionary items for third parties. AlArabia runs two print shops, one in Jeddah focused on digital printing, and another in Riyadh for digital, silk-screen, and offset printing.

Fig 4: AlArabia's outdoor advertisement breakdown:



Sources: Company reports, AlJazira Capital

Fig 5: Contracts per segment:

	Outdoor	Indoor
2022*	97	25
2021	100	17
2020	20	8
2019	78	-
2018	90	-

Sources: Company reports, AlJazira Capital. *To date

AlArabia's main customer base are concentrated towards 'Media Buyers', groups that purchase advertisement space to display their own advertisement services. Revenues from this category of buyers made up 66% of AlArabia's total revenues (on average from FY18 to FY20). As for the firm's suppliers, the sites AlArabia operates in are mainly spaces from government and quasi-government entities, as they make up the large majority of the firm's advertisement sites with 96.6% of the firm's revenues come from government and quasi-government spaces. The firm's hardware suppliers for billboard purchases are made through purchase orders from various suppliers. Billboard purchases made up 66% of the firm's total purchases, on average (from FY18 to FY20).

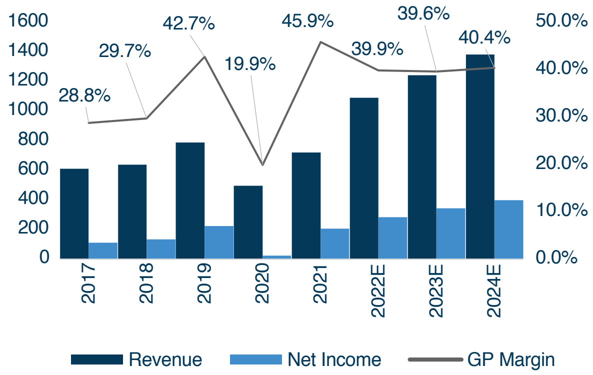
AlArabia's cost of revenue majorly consists of costs related to right-of-use assets in the form of the sites the firm displays its advertisements on. The costs of the rights-to-use leases are recorded as amortization, which for the industry constitute around 85% of COGS. AlArabia's cost drivers are no different, as amortization expenses accounted for 80.2% of the firm's COGS (on average from FY19 to FY21).

Financial Analysis:

Robust revenue growth faced the friction of pandemic lockdowns but topline is set to continue its growth trajectory afterwards. AlArabia's five years CAGR is expected to reach 14.30% by FY22's financial releases (from FY18 to FY22). The firm has never recorded losses to date, even during the 2016 and 2017 slow-downs, and more recently during the pandemic lockdown periods. As of 9M-22, AlArabia's growth in revenue reached 63.5% higher than that of the same period Y/Y. The growth in revenue (and further expected increase) is driven by multiple factors; namely a) a surge in demand for advertisement in KSA, as the Kingdom's entertainment initiatives and outdoor activities are attracting a wider audience into the Kingdom, b) an increase domestic tourism which has eroded some of the seasonality around advertisement activities throughout the year, and c) digitalized billboards offering wider services and advertisement capabilities to advertisers.

Digitalized billboards remain a strategic catalyst for the firm's growth trajectory as they offer a multi-dynamic range of services to advertisers. Digitalized billboards allow changing the ad face throughout the day (to stay or become more relevant; at times with just with a nautical change in the advertised face, from the same advertiser, to switch between a day product and a night product throughout the day). Moreover, they enable timed campaigns such as a 'road-block' campaigns which aim to populate an area with one advertiser at a specific time. Ability to adjust ads to meet the demographic structure of the area and providing data to clients are all among the reasons for the increased demand for digitalized billboards. AlArabia continues to digitalize its billboards to aim towards having 80% of faces digitalized by FY25.

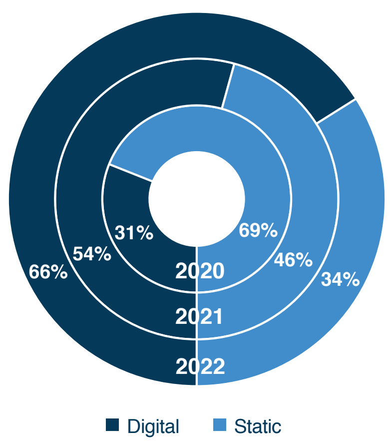
Fig 6: AlArabia's profitability



Source: Company management, AlJazira Capital

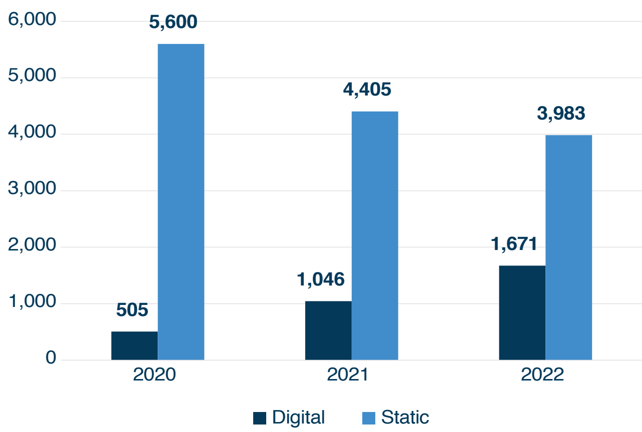
Gross margins to be supported by digitalization as AlArabia is more than half way through its target to digitalize 80% of its faces by 2025. Less upkeep cost, lower human intervention, and ability to display more panels per billboard installation earmarks the impact digitalization will have on gross margins. Static billboards (two sided, analog billboards) carry a cost of maintenance and upkeep when replacing panels that a digitalized billboard with control chips and processors do not incur. Furthermore, less machinery is needed during an expansion. This should reflect favorably on depreciated assets going forward. We anticipate gross margins to remain at a 40%+ range.

Fig 7: AlArabia's digitalization campaign underway



Sources: Company reports, AlJazira Capital

Fig 8: Digital and static billboard breakdown (by installations)



Source: IPO Prospectus, Aljazira Capital Research

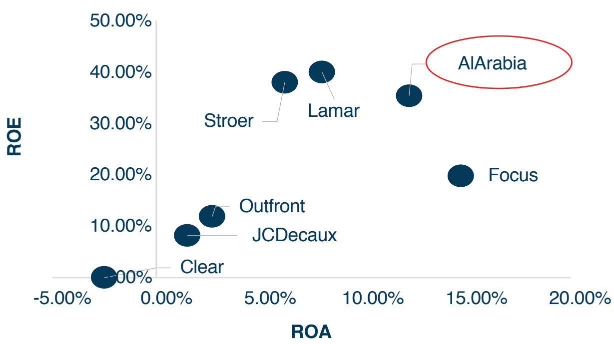
Peer Analysis:

Fig 9: Global peers comparables (TTM)*

	ROA	ROE	GP Margin	NI Margin	Borrowing/Equity	Receivables days
AlArabia	**12.2%**	**35.4%**	**40.9%**	**25.5%**	**0.43**	**196**
Clear Channel (USA)	-2.5%	(accumulated losses)	46.9%	-5.2%	N/A**	84
Outfront Media (USA)	2.7%	11.9%	49%	9.2%	1.97	61
Stroer (Germany)	6.2%	38.0%	42.0%	9.5%	1.66	38
Focus (China)	14.7%	19.8	65%	34.1	0	77
Lamar (USA)	8.0%	40%	67%	24%	2.36	52
JCDecaux**	1.5%	8.2%	60.8%	4.4%	1.1	67

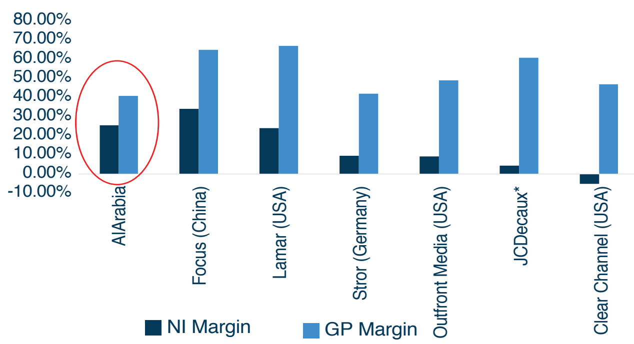
Sources: Company reports, AlJazira Capital.
*Peers in order of highest 16 outdoor advertisement revenue generators (2020). Private companies, firms with inconsistent data, and acquired companies have been excluded.
Borrowings / Equity as of MRQ.
** Firm reports bi-annually

Fig 10: Global peers profitability (TTM)



Sources: Company reports, AlJazira Capital

Fig 11: Margins Comparable (TTM)



Sources: Company reports, AlJazira Capital.

Working Capital Specifications, Client Mix, and Debt:

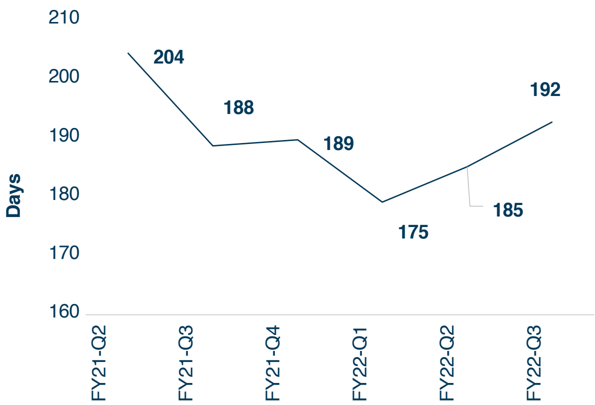
AlArabia's financial performance stand favorably among its global peers. The firm uses short term borrowings to leverage its profitability (43.6% borrowings/equity) to reach a TTM ROE of 35.4%; also the second highest TTM ROA (12.2%) observed among its global peers. Market consensus for the observed companies' Y/Y revenue growth for FY23 stands at a median of 5.6%. Comparatively, we anticipate AlArabia to grow 13.8% in revenue for the same period; owing mainly (among other drivers) to the increase in outdoor activity and demand for outdoor advertisement in the Kingdom.

Efficient profitability, and a display of efficient capital deployment earmarks the firm. AlArabia invested capital through FY17 to FY21 increased by SAR 478.4mn- yielding, however, a ROIIC of 8.12% in NOPAT for that same period, above its current WACC of 7.1%. As costs of debt are expected to peak by the end of H1-FY23, the efficiency on capital deployed will display a wider headroom in the coming periods.

The firm's most recent reduction in its working capital (9M-22) comes as a result of AlArabia's increase in short term loans and bank facilities to facilitate its expansions. During that period, reduction in working capital by almost 22% Y/Y (to facilitate AlArabia's increase in advertising sites and activities) saw a 64% Y/Y increase in revenues across the same period. The firm's total borrowings to equity reached 43.6% (TTM), with all borrowings obligations short dated. Its TTM cost of debt (over average debt obligations and interest bearing lease liabilities) comes at 3.18%. With an interest cover of 6.3x for the same period, EBIT margin is expected to expand by 140bps in FY23, and a current ratio currently standing at 1.2x (TTM); AlArabia's ability to manage its short term obligations poses no material threat to investors.

The firm's 196 days in outstanding receivables is a result of the firm offering leeway for advertisers in order to win their clientship and facilitate easier terms for their clients to part with their budgets. While the collection days are elevated among its global peers, the nature of business in KSA has many service firms contracted with the government, which is a possible chief differentiator among its peers as AlArabia's management indicated that it takes over 100 days to collect from their government client base- whom tend to have longer payment times (almost 15% of their government exposure is from direct sales to government entities). The firm indicates that their collections management is not a concern- yet management indicates that they will attempt to be more selective on their payment terms, at the challenge of balancing a trade-off between earlier collections, and favorable terms to attract more of their clients' budgets. As receivables stand over SAR 4.07bn in total revenues that the firm recorded from FY17 to Q3-22, the firm has historically only once recorded an impairment provision on its receivables at a comparatively modest SAR 8mn in 2020. Thus, despite being elevated, AlArabia's receivable days display consistent management as they are favorably stable

Fig 12: Receivable days remain in a range (TTM)



Sources: Company reports, AlJazira Capital.

Faden Media Acquisition:

A successful acquisition of 100% of Faden stands as a key turning point for the firm. Faden, as of 2020, claimed about 1.8% of market share in the outdoors advertisement market. Atop their market share, Faden owns 42.5% of another firm, Wave Media, which claimed 10.3% of market share on that same leaderboard. Together implying an additional 6.18% market share for AlArabia; should the acquisition go through. Wave Media offers more than 12,000 advertisement panels throughout 25 cities, and specializes in indoors advertisement. Along with their focus on indoor advertisement (which can add to AlArabia's scope of operations), Wave Media has an exclusive partnership with Haramain Highspeed Railway, a segment ('Transit' advertising) AlArabia is currently absent from. Faden Media in itself also offers AlArabia more than market share, as they specialize in 'Building' advertising- also an area that AlArabia is absent from. Building advertisement is an increasingly more popular form advertising that takes up the face of a building. Usually the entire face, or a large portion of a face of the building facing an audience. For inhabitants and residents of the Kingdom, the sight of a high story building covered in a digital screen is not a foreign sight to see as of lately. AlArabia aims to leverage Faden's focus in that space, along with Wave Media's focuses, to expand on AlArabia's scope of offerings.

Faden is expected to add a net SAR 0.88 per share to AlArabia's investors by this year's end as things stand, according to our estimates. At a cost of SAR 1.05bn, AlArabia will seek to finance the majority of the acquisition bill after depleting their cash holdings of almost SAR 186mn in cash. With management indicating that major developments in the deal will materialize by H1-23, we anticipate their cash holdings to rise to 200mn- leaving 850mn left from the acquisition cost to be financed to gear up their total borrowings to debt to almost 1.46x. While the firm is under negotiations with banks on the transaction, the terms of the borrowings, or possibilities of hedging the cost of debt are not set as of yet. However, we modelled the contribution that Faden's acquisition will have on AlArabia bottom line based on the following assumptions: Faden's bottom line to grow over the global sectors' expected growth. As well as- considering the position in the economic cycle that the global economy is in, we anticipate that current high cost of debt environment will begin to wind down by H2-FY23. That is consistent with the implied probabilities by the Fed Rate Futures market, which maintains a median spread over the 6M-SAIBOR of about 73bps over the data we have observed. Excluding the premium that the current market priced on the SAIBOR-Fed Rate spread due to the LDR recorded in the Kingdom, we anticipate the baseline of which banks lend at (the 6M-SAIBOR) to range around 5.25% by the year's end. We assumed a 1.5% fixed cost of funding over the SAIBOR rate, to imply a cost of debt of around 6.75% by year's end. Assuming the transaction finalizes by beginning of H2-23, and that the financing term is over the length of 10 years (while terms, grace periods, and other financing specifications are still under negotiation) the return Faden will have on AlArabia's H2-23 bottom line implies a net contribution of SAR 0.88 per share- after half a year of financing is paid off.

Global advertising market disrupted by digital media

Outdoor advertising most resilient among traditional advertising media

Digital media has captivated the global advertising market in past few years. Advisers are clearly spending more on digital advertising rather the traditional media. However, among major traditional advertising media outdoor advertising was least impacted. Expenditure on outdoor advertising increased consistently for five years before the pandemic (FY14-19). Whereas expenditure on advertising through television, newspapers and magazines declined significantly during this period. The outdoor advertising maintained ~6% share in total expenditure during the pre-COVID years despite onset of digital media. The outdoor advertising has remained relevant in changing time due to its inherent unique nature and adoption of technology to digitize the screens and use of advanced tools to analyze viewer data providing insights to the advertiser.

Fig 13: Global Advertising Expenditure by Media (SAR bn)

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Television	739	759	760	786	781	780	775	675
Newspapers	271	257	236	214	195	180	159	121
Magazines	147	142	134	132	122	113	101	79
Radio	126	129	129	134	135	139	139	118
Cinema	9	11	12	13	14	15	16	6
Outdoor Advertising	116	113	124	127	129	136	140	104
Digital Media	386	465	555	650	756	869	1,032	1,088
Total Expenditure	**1,793**	**1,876**	**1,949**	**2,057**	**2,132**	**2,231**	**2,362**	**2,192**

Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

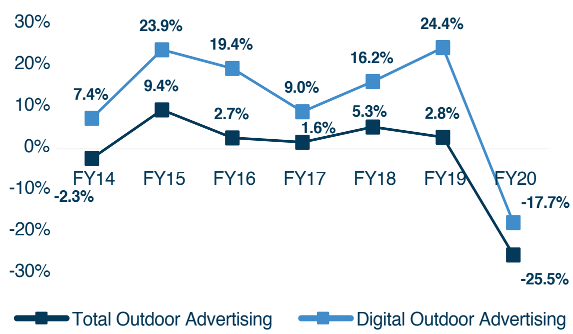
COVID restrictions severely impacted outdoor advertising

Globally, advertising expenditure reduced during the pandemic. The total expenditure was down 7.2% Y/Y in FY20. The outdoor advertising was among the most impacted media with advertising expenditure decreasing 25.5%, as lockdowns, restrictions on mobility and lack of outdoor activity affected the expenditure. However, now, with easing of precautionary measures and activities returning to normal in most of the countries outdoor advertising is expected to recover and grow thereafter.

Digital outdoor advertising to drive growth in future

Advertisers across the world are shifting from static outdoor screens (billboards) to digital screens. The global expenditure on digital outdoor advertising has outpaced substantially the total expenditure on outdoor advertising. Digital advertising is becoming preferred choice due to growing penetration of internet, 5G adoption, decreased cost of digitization and availability of data analytics tools to run a well-managed advertising campaign that increases probability of higher returns.

Fig 14: Expenditure Growth



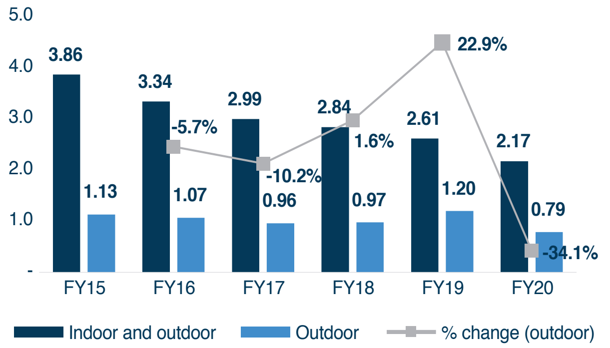
Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

Government expenditure, digitalization and increased outdoor activities to be key growth drivers for KSA outdoor advertising market

Inconsistent historical trend for outdoor advertising expenditure in Saudi Arabia

There has been a declining trend in total advertising expenditure (indoor and outdoor) in Saudi Arabia. During FY15-20, advertising expenditure declined from SAR 3.9bn to SAR 2.2bn. This decline was driven by different factors such as impact of economic slowdown on advertising spending during FY16-18 and effect of COVID-19 in FY20. However, outdoor advertising spending increased in FY18 and FY19, despite decline in overall advertising expenditure. This indicates that outdoor advertising in is mainly affected by macro factors and expenditure trends; not by competition from other available advertising channels.

Fig 15: Advertising Expenditure in KSA (SAR bn)

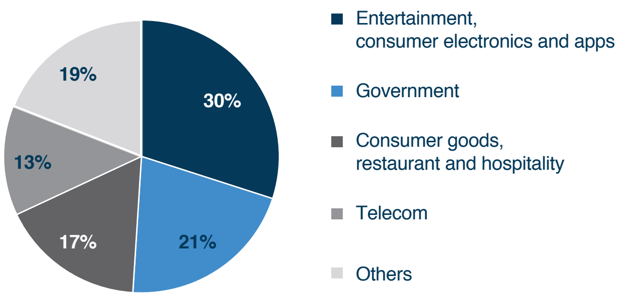


Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

Growth in outdoor advertising expected to continue post-COVID; mid-to-long term prospects positive

The expenditure on outdoor advertising saw a sharp growth of 22.9% in FY19 before the pandemic hit. This growth was led by increase in government expenditure on outdoor advertising, digitization of advertising sites (particularly sites in malls and retail stores) and government's efforts to boost non-oil sector. In FY19, around 30% of outdoor advertising expenditure came from entertainment sector, consumer electronics and apps, while government contributed 21%. Consumer goods, restaurant and hospitality accounted 17% of expenditure and telecom constituted 13%. Some firms switched back to outdoor and indoor advertising spaces in malls from digital and social media.

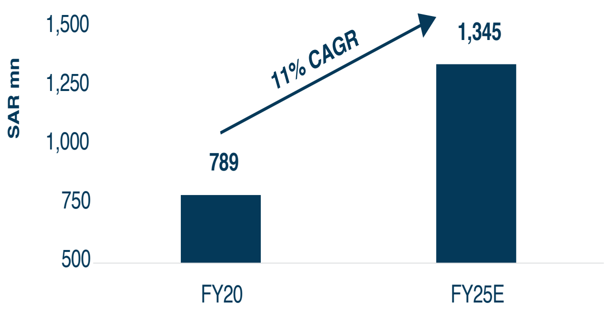
Fig 16: Non-oil Sectors Dominates Outdoor Advertising Expenditure in KSA (FY19)



Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

As the economy recovers from the COVID-19 and economic activities are gaining the pace, the outdoor advertising market is expected to grow. Additionally, acceleration in Vision 2030 activities and development of smart cities would also boost the expenditure on outdoor advertising. The expenditure is estimated to reach about SAR 1.35bn in FY25, indicating CAGR of ~11% during FY20-25.

Fig 17: Estimated Growth Total Expenditure

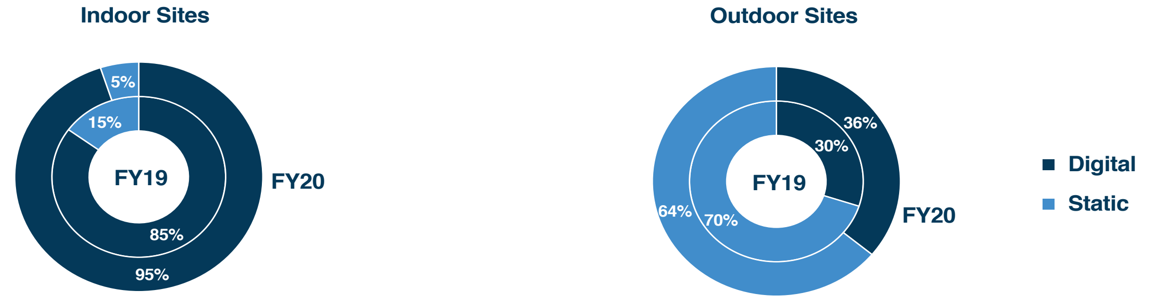


Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

KSA market shifting to digital billboards, most of the indoor sites digitalized; outdoor following the same trend

As of FY20, outdoor advertising sites across Saudi Arabia were estimated at 12,002 with total 38,053 advertising faces. Out of these 61% (FY19: 70%) were outdoor spaces such as streets, highways, parks and outdoor airport facades; while 39% (30%) were indoor spaces such as shopping centers, gyms, cafes, hotels, buildings and indoor areas at airports. Among indoor sites digitization percentage is high with 95% sites being digital and only 5% static. Whereas among outdoor sites digitization has reached 36% and expected increase further given the advertisers preference to digital billboards.

Fig 18: Increasing digitization in indoor and outdoor advertising sites



Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

Market inventory skewed towards Mupi billboards

Fig 19: Inventory distribution

Advertising Type	Percentage of FY19 inventory	Percentage of FY20 inventory
Mupi Billboards	56%	62%
Megacom Billboards	16%	17%
Super Structures and LED Billboards	6%	9%
Other Billboards	22%	12%

Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

Five major players dominate Saudi outdoor advertising market; Al Arabia the largest by far

As of FY20, top five players in Saudi outdoor advertising accounted for 97% of the market share. Al Arabia with a market share of 62.3% leads the market by a wide margin, as second largest player Saudi Sign holds 18.8% market share followed by Wave Media (10.3%), JCDecaux (3.8%) and Faden Publicity and Advertising (1.8%).

Fig 20: Market share by company

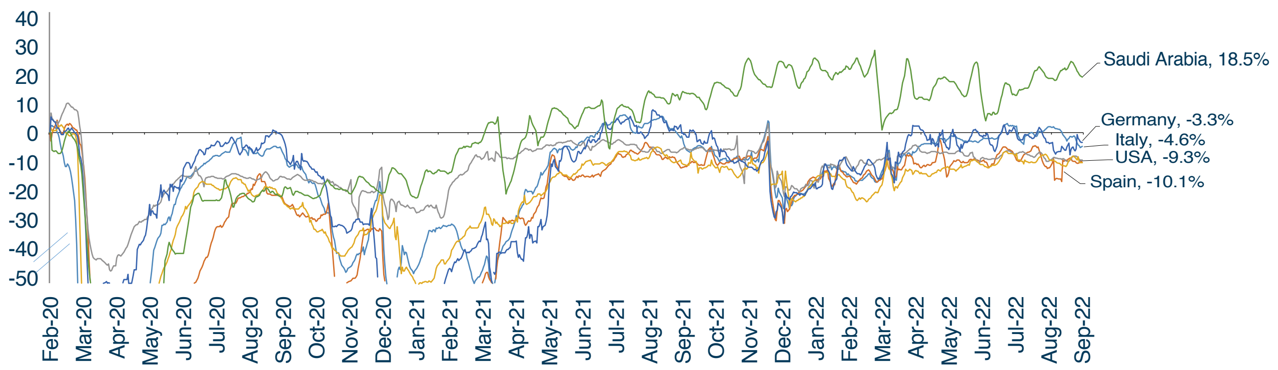
Company	Market Share
Al Arabia	62.3%
Saudi Sign	18.8%
Wave Media	10.3%
JCDecaux	3.8%
Faden Publicity and Advertising	1.8%
Others	3.0%

Source: Frost & Sullivan, IPO prospectus, Aljazira Capital

Increase in visits to outdoor venues makes a larger audience available for outdoor advertisers

Saudi Arabia has seen more visits and time spent, in all venue categories, including transit stations, since early 2020. As the Kingdom has been increasingly hosting various events, residents have more of a reason to be out-of-home. Such events include the Kingdom hosting world class sporting and entertainment events such as a Formula 1 race attracting a six figure attendance. Additionally, there are more leisurely venues have opened up and there is increase in recreational venues as well as entertainment events. These event and activities provide a large target audience to outdoor advertisers. Thus, increasing demand for outdoor advertisements.

Fig 21: Increasing number of visitors to retail and leisure venues in the Kingdom



Sources: Google Mobility Trends, AlJazira Capital. *(7 day rolling averages)

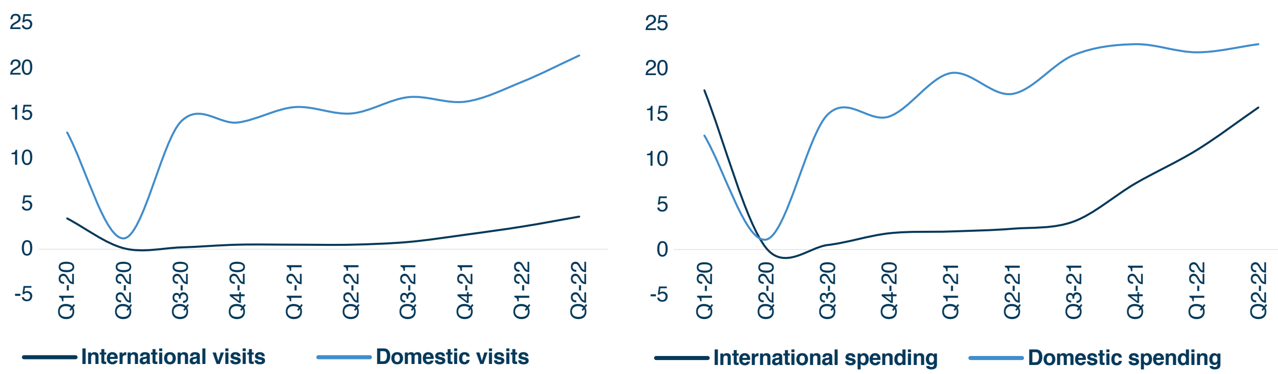
The initiatives towards more recreational venues are still underway, supporting outdoors advertisement

Among some of the large scale projects is the under-construction King Salman Park at the heart of the capital covering over 16 square kilometers of space (seven times larger than London's Hyde Park). The Mall of Saudi (also under construction) is also among some of the retail and leisurely venues to open up almost 400,000 square meters of shopping and recreation spaces. Atop the new venues there are the events to be held. Some of the events attracting tourists and domestic attendances are exclusive football cup rights to be held in Saudi attracting large attendances, the Dakar Rally (now called Saudi Dakar Rally), a music festival events which attracted 732,000 people historically, are all only some of the events to bring people outdoors and attract tourists from abroad into the Kingdom.

Tourism sector recovery and government initiatives to support the sector another factor favorable to outdoor advertising

The Saudi tourism sector is recovering from the impact of COVID-19 with easing of travel restrictions. The number of tourists in Saudi Arabia increased 45.0% Y/Y in H1-22 to 46.0mn from 31.7mn in the year earlier. Tourism spending also witnessed a jump of 73.7% Y/Y to SAR 71.2bn during the same period. From the long term perspective, the Saudi government has rolled out new tourism policies such as easing of Visa application process. Vision 2030 aims to make the Kingdom world class tourist destination. Hence, the number of visitors to Saudi Arabia are likely to increase in future and development of tourism will also boost outdoor activities.

Figs 22 & 23: International and Domestic Visits (mn) and Spending (SAR bn)



Source: GASTAT, Aljazira Capital

New cities to open new opportunities for outdoor advertising

Mega projects such as NEOM smart city and other smart city project planned across top 10 Saudi cities will provide additional spaces for outdoor advertising. The smart city initiative is expected to first target five Saudi cities, Makkah, Riyadh, Jeddah, Al-Madinah, and Al-Ahsa. This will open opportunities for expansion to new sites and growth for outdoor advertising.

Investment Thesis and Valuation

With a dominating position in the outdoor advertisement market, our bet on AlArabia is based with the Kingdom's initiatives to attract a larger no. of visitors and increased outdoor activities, which will generate a larger demand for outdoor advertisement. More people outdoors, (over COVID levels) at a time when other economies have returned back to pre-Covid baselines came as a result of the Kingdom's initiatives. Ranging from increased world class sports in the Kingdom, entertainment, tourism, and leisure areas- a resident of the KSA will find AlArabia's signages on the way to any of those outdoor activities, and possibly there as well.

Faden Media acquisition to increase AlArabia's "Advertisement empire" and complement their operations with further synergies. At a cost of SAR 1.05bn, AlArabia is eying to purchase an annualized contribution of SAR 1.78 per share to its bottom line- as well as synergies that that can indirectly contribute to the bottom line as well. Additionally, the acquisition will provide more product offerings (building and transit advertisement) to AlArabia's clients, who often buy AlArabia's services as a package of services and faces. We recognize the acquisition favorably towards AlArabia's market share, offerings, and profitability. With borrowings to equity expected to reach 1.46x, the cost of financing and the decrease in cost of capital, will potentially weigh each other off from a valuation standpoint.

AlArabia's venture into the Egyptian market is another operational development to observe in the coming periods. Still without a full year of financials on the geographic segment, AlArabia began its venture with 174 installations to contribute almost 2% of the TTM revenues. While still in its early operational developments, the expansion into the Egyptian market through its subsidiary arm United Company for Advertising Services offers shareholders a geographic exposure to a larger market through 49.9% owned subsidiary. With a presence in the UAE through another subsidiary, the stock is expanding its MENA presence to top their KSA focus. Current economic conditions in Egypt however, which drove the Egyptian pound to depreciate to the dollar by 17.3% YTD is a risk point arising from financial translation and exchange rate risks, as well as purchasing power on demand.

Upside risks:

- Favorable financial position, debt coverage, margins and profitability place the firm well to expand through a geared acquisition.
- Expanding through the Faden Media acquisition has the potential to expand AlArabia's market share by over 5%, and expand the demand towards AlArabia's services.
- With the established leadership in the outdoor advertisement sector, AlArabia's stock can be seen as a vehicle to exposure towards KSA's entertainment and population initiatives and developments.

Downside risks:

- With a focus on Outdoor advertisement, we estimate that 97% of AlArabia's revenue is generated from leases form government and semi-government entities. Changes in bidding processes, as well as the lessor entities exercising their right to advertise on the billboards free of charge can contradict with the management's momentary direction.
- Failure to pay leases on time, as the firm previously has before, can result in the firm being ineligible to bid and win tenders.
- A reversal, or reduction, of the population's outing behaviors poses a risk towards the demand for AlArabia's services.

Valuations:

DCF Valuation

Our valuation of AlArabia is based on a DCF (Rfr = 4.0%, terminal growth = 2.5%, and a WACC = 7.1%), yielding a value of SAR 7.5bn (TP of SAR 150.2 per share).

Relative Valuation

We valued AlArabia using the relative valuation methodology based on the FY23E P/E. We rounded down to normalize the sector median post JCDecaux's inflated P/E.

Peer Comparison Table (FY23E):

Company Name	P/E (FY23E)
Focus Media	18.7x
JCDecaux SE	26.4x
Lamar Advertising Co	18.1x
APG SGA SA	18.5x
Outfront Media	16.8x
Surya Citra Media Tbk	10.8x
Sector Median	**18.2x**

All figures in SAR mn, unless specified	
Sector P/E	**18.0x**
Premium over Peers	**0%**
Implicit Market Cap	**6,188.2**
Shares (Mn)	50
Relative value (SAR/share)	**123.8**

Blended Valuation

Blended Valuation

All figures in SAR, unless specified	Fair value	Weights	Weighted average
DCF based value	150.2	50%	75.1
Relative Valuation - P/E	123.8	50%	61.9
Weighted average 12-month price target			**137.0**
CMP			108.0
Upside/ Downside			**26.9%**

Source: Bloomberg, Tadawul, Company Prospectus, Aljazira Capital Research

We assigned a 50.0% weightage to DCF, and 50.0% to the FY23E P/E (18x) multiple. Based on the combined valuation, we arrived at a TP of **SAR 137.0/share**. As per our derived TP, the implied P/E multiple based on FY23E earnings is 15.7x vis-à-vis a current P/E of 20.8x based on TTM EPS.

Key financial data

Amount in SAR mn, unless otherwise specified	FY19	FY20	FY21	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E
Income statement									
Revenues	787	498	720	1,091	1,242	1,384	1,493	1,591	1,655
Y/Y		**-36.8%**	**44.8%**	**51.5%**	**13.9%**	**11.4%**	**7.9%**	**6.6%**	**4.0%**
Cost of revenue	(451)	(399)	(390)	(656)	(751)	(824)	(874)	(925)	(960)
Gross profit	**336**	**99**	**330**	**435**	**492**	**559**	**619**	**666**	**696**
Selling and distribution expenses	(42)	(11)	(31)	(41)	(47)	(54)	(58)	(62)	(62)
General and administrative expenses	(30)	(29)	(40)	(56)	(51)	(57)	(61)	(65)	(65)
Operating profit	**264**	**51**	**261**	**336**	**392**	**447**	**498**	**537**	**566**
Y/Y		**-80.6%**	**408.3%**	**28.6%**	**16.6%**	**14.0%**	**11.3%**	**7.9%**	**5.5%**
Finance cost	(32)	(21)	(33)	(51)	(46)	(44)	(40)	(38)	(38)
Other income, net	1	0	(11)	5	6	7	7	8	8
Income before zakat	**234**	**31**	**218**	**290**	**353**	**410**	**465**	**507**	**537**
Zakat	(9)	(5)	(11)	(7)	(9)	(10)	(12)	(13)	(13)
Net income	**225**	**25**	**206**	**283**	**344**	**400**	**454**	**495**	**523**
Y/Y		**-88.8%**	**718.4%**	**37.3%**	**21.4%**	**16.4%**	**13.4%**	**9.0%**	**5.7%**
Balance sheet									
Assets									
Cash & equivalent	36	27	190	328	334	321	342	377	401
Trade receivables	358	336	419	650	707	758	798	842	884
Other current assets	96	103	411	303	348	387	422	449	470
Total current assets	**490**	**466**	**1,020**	**1,280**	**1,389**	**1,466**	**1,561**	**1,667**	**1,755**
Property plant & equipment	124	155	193	215	243	264	284	302	319
Rights of use assets	775	694	2,027	1,492	1,582	1,686	1,804	1,936	2,084
Total assets	**1,389**	**1,315**	**3,240**	**2,988**	**3,215**	**3,415**	**3,649**	**3,906**	**4,158**
Liabilities & owners' equity									
Lease liabilities - current	177	215	314	305	377	393	426	455	483
Short-terms loans	239	132	448	368	343	368	353	338	323
Total current liabilities	**535**	**460**	**907**	**909**	**988**	**1,032**	**1,041**	**1,071**	**1,096**
Lease liabilities - non-current	316	316	1,587	1,219	1,262	1,316	1,425	1,525	1,618
Total non-current liabilities	**330**	**329**	**1,602**	**1,235**	**1,279**	**1,336**	**1,447**	**1,550**	**1,647**
Share capital	500	500	500	500	500	500	500	500	500
Statutory reserves	22	25	46	64	92	128	170	219	275
Retained earnings	2	1	186	280	356	420	491	566	640
Total owners' equity	**524**	**526**	**731**	**845**	**948**	**1,048**	**1,161**	**1,285**	**1,416**
Total equity & liabilities	**1,389**	**1,315**	**3,240**	**2,988**	**3,215**	**3,415**	**3,649**	**3,906**	**4,158**
Cashflow statement									
Operating activities	527	349	208	421	836	927	1,019	1,114	1,165
Investing activities	(44)	(57)	(78)	395	(632)	(693)	(743)	(786)	(817)
Financing activities	(465)	(301)	33	(678)	(197)	(248)	(254)	(294)	(324)
Change in cash	18	(10)	163	138	7	(14)	21	35	24
Ending cash balance	**36**	**27**	**190**	**328**	**334**	**321**	**342**	**377**	**401**
Key fundamental ratios									
Liquidity ratios									
Current ratio (x)	0.9	1.0	1.1	1.4	1.4	1.4	1.5	1.6	1.6
Quick ratio (x)	0.9	1.0	1.1	1.4	1.4	1.4	1.5	1.5	1.6
Profitability ratios									
Gross profit margin	42.7%	19.9%	45.9%	39.9%	39.6%	40.4%	41.4%	41.9%	42.0%
Operating margin	33.6%	10.3%	36.3%	30.8%	31.6%	32.3%	33.3%	33.8%	34.2%
EBITDA margin	84.2%	84.0%	80.1%	71.0%	73.0%	73.4%	73.9%	73.7%	73.6%
Net profit margin	28.6%	5.1%	28.6%	26.0%	27.7%	28.9%	30.4%	31.1%	31.6%
Return on assets	16.2%	1.9%	9.1%	9.1%	11.1%	12.1%	12.8%	13.1%	13.0%
Return on equity	43.0%	4.8%	32.8%	35.9%	38.4%	40.1%	41.1%	40.5%	38.7%
Leverage ratio									
Debt / equity (x)	1.4	1.3	3.2	2.2	2.1	2.0	1.9	1.8	1.7
Market/valuation ratios									
EV/sales (x)	NM	NM	10.0	6.3	5.7	5.2	4.9	4.6	4.5
EV/EBITDA (x)	NM	NM	12.5	8.9	7.8	7.0	6.6	6.3	6.1
EPS (SAR)	4.5	0.5	4.1	5.7	6.9	8.0	9.1	9.9	10.5
BVPS (SAR)	10.5	10.5	14.6	16.9	19.0	21.0	23.2	25.7	28.3
Market price (SAR)*	NM	NM	101.2	107.0	108.0	108.0	108.0	108.0	108.0
Market-Cap (SAR mn)	NM	NM	5,060	5,350	5,400	5,400	5,400	5,400	5,400
P/E ratio (x)	NM	NM	24.5	18.9	15.7	13.5	11.9	10.9	10.3
P/BV ratio (x)	NM	NM	6.9	6.3	5.7	5.2	4.7	4.2	3.8

Source: Company Reports, AJC Research

الجزيرة كابيتال
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RESEARCH DIVISION

AlJazira Capital, the investment arm of Bank AlJazira, is a Shariaa Compliant Saudi Closed Joint Stock company and operating under the regulatory supervision of the Capital Market Authority. AlJazira Capital is licensed to conduct securities business in all securities business as authorized by CMA, including dealing, managing, arranging, advisory, and custody. AlJazira Capital is the continuation of a long success story in the Saudi Tadawul market, having occupied the market leadership position for several years. With an objective to maintain its market leadership position, AlJazira Capital is expanding its brokerage capabilities to offer further value-added services, brokerage across MENA and International markets, as well as offering a full suite of securities business.

RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer