



US\$1.261bn Market cap
58% Free float
US\$1.138mn Avg. daily volume

Target price **145.0** 13% over current
 Current price **164.0** as at 4/2/2020

Research Department
Pratik Khandelwal

Tel +966 828 4642, pratikK@alrajhi-capital.com

Existing rating

Underweight **Neutral** **Overweight**

Performance



Earnings

(SAR)	12/18A	12/19A	12/20E	12/21E
Revenue (mn)	1693	1813	1973	2099
Revenue growth	-5%	7%	9%	6%
Gross Profit	634	580	648	700
Gross Profit Margin	37%	32%	33%	33%
EBIT (mn)	274	222	277	317
EBIT growth	-14%	-19%	25%	15%
EBIT Margin	16%	12%	14%	15%
Net Profit	260	216	268	305
Net Profit Margin	15%	12%	14%	15%
EPS	8.01	6.66	8.37	9.55

Source: Company data, Al Rajhi Capital

Saudi Dairy & Foodstuff Co

Beat Estimates; Increasing TP to SAR164/sh

SADFACO's reported a net profit of SAR68mn (+27% y-o-y) beating our estimate of SAR55mn by 24%. Top-line came in at SAR488mn (+5.5% y-o-y) which was mostly in-line with our estimates of SAR490mn. The main reason for increase in net profit was gross margin improvement by 570bps (excluding Mlekoma it was 370bps) despite increase in cost of raw materials due to production efficiencies and lower discounting as a result of improving consumer sentiment. The capacity addition in ice-cream segment earlier this year along with favourable weather helped the company in increasing its ice-cream revenue by 103% which has also helped in gross margin expansion. Though there are concerns with the global increase in SMP (skimmed milk prices) prices the company by far has been able to manage the gross margins by procuring SMP from Mlekoma (its subsidiary) which has helped it in partially offsetting the impact of higher raw material prices. We have observed an improvement in consumer demand in Saudi Arabia and believe that the company will be able to maintain its leadership position in the UHT milk segment and improve the market share in ice-cream segment leading to similar level of margins in near term. Accordingly we revise our forward looking estimates and change the target price to SAR164/sh from SAR156/sh.

Q3 2020 Results summary: Revenue grew 5.5% y-o-y to SAR488mn mainly due to stable RTD milk segment growth and 103% y-o-y growth in ice-cream segment. The main reason for ice cream segment growth was capacity addition in previous quarters across GCC markets. The gross margins increased by 580bps to reach 36.1% in Q4 2019 (including sales from Mlekoma, increasing commodity prices enhances Mlekoma margins). The net profit increased 27% y-o-y to SAR68mn due to higher gross margins. RTD milk growth was almost flat at -0.5% y-o-y to SAR313mn due to stable consumer demand, ice-cream segment sales increased 103% y-o-y to SAR98mn driven by increasing sales capacity added in previous quarters. Tomato paste revenue fell 23% y-o-y to SAR42mn likely due to increasing competition from local and international brands. Powdered milk, snacks and cheese revenue declined 31% y-o-y, 13% y-o-y, 21% y-o-y respectively.

Fig1: Summary of Q3 2020 Results

(SAR mn)	Q3 2019	Q2 2020	Q3 2020	% chg y-o-y	% chg q-o-q	ARC est
Revenue	463	521	488	6%	-6%	490
Gross Profit	140	177	176	26%	0%	157
Gross Profit Margin (%)	30%	34%	36%	19%	6%	32%
Operating Profit	54	67	70	29%	5%	56
Operating Profit Margin (%)	12%	13%	14%	22%	12%	11%
Net Profit	54	65	68	27%	5%	55

Source: Company data, Al Rajhi Capital



Valuation: We value SADAFCO using equal weight of DCF and PE based relative valuation. Our DCF based target price based on 2% terminal growth and 8.17% WACC comes to SAR162 and P/E based relative valuation based on 20x FY20e EPS gives us a target price of SAR165 thus equal weighted target price stands at SAR164 which implies an upside of 13% from current market price of SAR145 thus maintaining our “overweight rating”.

Key Risks: Key downside risk to our valuation includes 1) significant increase in SMP prices will impact the gross margins and valuation negatively and accordingly poses a downside risk to our target price, 2) any slowdown in consumer spending due to any regulatory issues might impact the revenue growth of the company and ultimately our target price, 3) company’s major revenue is exposed to UHT dairy, if there is any further price led competition in the market then margins will come under pressure and will have downside risk to our target price, 4) slowdown in population growth will have a negative impact on dairy demand which in turn will impact the top-line, and 5) any changes in expat levy will increase SG&A and will reduce the operating margins going forward.



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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

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Contact us

Mazen AlSudairi
Head of Research
Tel : +966 836 5468
Email: alsudairim@alrajhi-capital.com

Al Rajhi Capital
Research Department
Head Office, King Fahad Road
P.O. Box 5561, Riyadh 11432
Kingdom of Saudi Arabia
Email: research@alrajhi-capital.com

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