


US\$1.210bn

Market cap

30%

Free float

US\$3.182mn

Avg. daily volume

Target price

20.00 -7.4% over current

Current price

21.60 as at 11/2/2019

Research Department

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Existing rating
Underweight
Neutral
Overweight
Performance

Earnings

Period End (SAR)	3/17A	3/18A	3/19E	3/20E
Revenue (mn)	6,692	6,117	6,131	6,216
Revenue Growth	-3.6%	-8.6%	0.2%	1.4%
EBITDA (mn)	979	632	627	728
EBITDA Growth	-16.8%	-35.5%	-0.8%	16.2%
EPS	2.0	0.5	0.6	1.1
EPS Growth	-30.9%	-75.7%	22.7%	79.0%

Source: Company data, Al Rajhi Capital

Fawaz Abdulaziz Al Hokair **Beat estimates; remain Neutral**

Alhokair reported a net profit decline of 45.5% y-o-y to SAR27mn, beating our estimate of SAR-18mn loss. Revenue declined 8.6% y-o-y, likely due to muted consumer spending and closure of non-profitable stores. Given the challenging market dynamics, the company continues to follow a prudent strategy of closing non-profitable stores while improving its cost efficiency in order to boost profit margins. In the near term, we expect Alhokair's top-line to remain under pressure, largely due to weak consumer demand, driven by changing consumption basket and declining customer base. Further, its gross margin to remain under pressure, mainly due to higher discounts offered to support top-line. However, a likely improvement in the international sales and higher demand of value products, coupled with recent traction in newly launched products should partially offset the decline in LFL sales in the medium term. For the longer-term, we remain optimistic on the top-line growth that is likely to be boosted by pick-up in consumer sentiments following a broader based economic recovery amid higher government spending, as announced in the Budget 2019. We remain Neutral on the stock, while we revise our target price upwards to SAR 20.0 per share (earlier: SAR 19 per share) largely due to beat in top line and better than expected gross margin.

- Q3 FY19 Results:** Revenue declined 8.6% y-o-y to SAR1,233mn (beating our estimate of SAR1,156mn), likely impacted by lower number of stores and continued pressure on LFL sales in the Kingdom. Gross profit decreased 13.2% y-o-y to SAR277mn, with corresponding margin declining 119bps y-o-y to 22.4%. However, the company managed to control sales & marketing expenses (-13.4% y-o-y), while continued cost efficiency program resulted in lower general & administrative expenses (-5.0% y-o-y). Consequently, operating profit declined 17.4% y-o-y to SAR85mn. Net profit came in at SAR27mn (-45.5% y-o-y), beating our estimate of SAR-18mn.
- Risks:** Downside risks include (a) higher-than-expected rise in employment expenses on the back of Saudization, (b) lower than expected rebates on rent, which can result in higher number of store closures and (c) significant decline in expat population. Upside risks include higher-than-expected rise in disposable income in the hands of Saudi population driven by Saudization.
- Valuation:** The stock is currently trading at a P/E of 19.6x, based on our FY20 EPS estimate, significantly higher than its 3-year average P/E of 13.4x. Our DCF based target price is SAR20 per share, assuming 8.5% WACC (35% debt in capital structure) and 3.0% terminal growth, which implies a Neutral rating on the stock.

Figure 1 Fawaz Al hokair: Summary of Q3 FY19 results

(SAR mn)	Q3 FY18	Q2 FY19	Q3 FY19	% chg y-o-y	% chg q-o-q	ARC est
Revenue	1,349	1,273	1,233	-8.6%	-3.1%	1,156
Gross profit	319	250	277	-13.2%	10.7%	227
Gross profit margin	23.6%	19.6%	22.4%			19.7%
Operating profit	103	65	85	-17.4%	30.7%	28
Net profit	49	10	27	-45.5%	165.0%	(18)

Source: Company data, Al Rajhi Capital



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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.

"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

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