

United Electronics Co. Extra

Minimal impact from COVID-19 and a bigger market share in Q12020

07 June 2020

United Electronics Co. (Extra) was able to increase market share from 16.9% in Q1 2019 to 17.8% Q1 2020 on the back of the increase in online demand and the marginalization of smaller competitors. Extra's e-commerce platform was a big support for the company's top-line performance, amid the major COVID-19 shutdowns. While e-commerce sales increased in Q1 2020 by nearly 7 times compared to Y-o-Y, "Tasheel finance" maintained momentum leading to a 17% increase in revenue Y-o-Y.

During the second half of March, Extra was forced to shut down 10% of its stores in malls (5 stores). However, the shutdown didn't seem to have a significant impact on the company's sales during Q1 2020 as revenue increased from SAR1,058mn in Q1 2019 to SAR1,232mn in Q1 2020. According to the company's disclosure, the increase in revenue during the quarter was mainly due to the company's e-commerce, which reached a 20% contribution out of total sales, in addition to revenue from consumer finance service "Tasheel Finance". The company was able to capitalize on the lockdown in the Kingdom through its online platform and already high exposure due to Extra's partnership with Noon. It is expected that the company will continue to benefit from its e-commerce, given that it improves its delivery services that were not up to standards during the spike in demand. Moreover, we expect a significant increase in revenues generated by the consumer finance segment going forward, as the market conditions and the increasing rate of unemployment from the impact of COVID-19 call for such service. We believe that "Tasheel Finance" will support any potential decline in sales in the retail segment, leading to a faster rebound of Extra compared to its competitors.

The cost of sales increased by 16% Y-o-Y from SAR870mn in Q1 2019 to SAR1.011mn in Q1 2020, which is an expected increase parallel to the increase in revenue. Similarly, the company's gross profit increased by 17% Y-o-Y, representing a flat performance in terms of gross margin as it remained at around 18% in Q1 2019 and Q1 2020.

In Q1 2020, SG&A increased by 21% Y-o-Y, from SAR118mn in Q1 2019 to SAR142mn in 2020. The increase in SG&A could be attributed to the costs of Extra's new segment "Tasheel Finance" that wasn't functioning yet in Q1 2019. Despite the increase in SG&A, Extra managed to achieve a 7% Y-o-Y increase in EBIT from SAR47mn in Q1 2019 to SAR51mn in Q1 2020. However, the EBIT margin decreased by 40bp Y-o-Y. Similarly, net margin also declined by 40bp Y-o-Y despite an increase in net income by 4%. From SAR34mn in Q1 2019 to SAR35mn in Q1 2020.

It is worth mentioning that due to the anticipated increase in the implementation of the VAT in July this year, we expect a higher-than-average in sales in June, knowing that Extra's products are the durable kind, where people are likely to lock them with a lower price before the VAT impact on prices.

Extra is no exception in terms of the negative impact, which should be reflected in Q2 2020; however, we expect that the increase in June retail sales combined with the surge in financing services revenue is bound to offset the complete shutdowns that took place during April partially.

In consideration of the recent rise in the number of outstanding shares by 10mn shares in addition to the impact of COVID-19, **we cut our 52 weeks target price SAR52.2/share while maintaining our Neutral recommendation.**

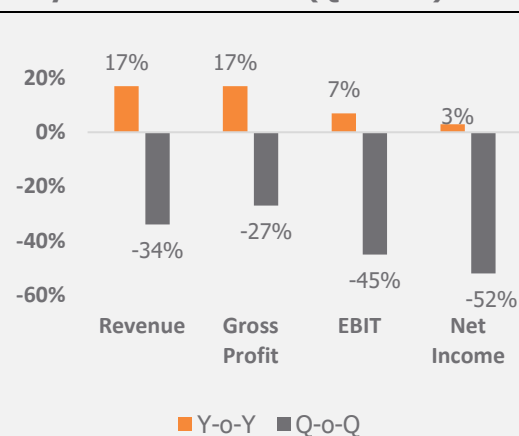
Recommendation **Neutral**

Previous Recommendation	Neutral
Current Price (04-06-2020)	SAR48.5
Target Price (52 Weeks)	SAR52.2
Upside/ (Downside)	7.6%
Shariah Compliance	Pass

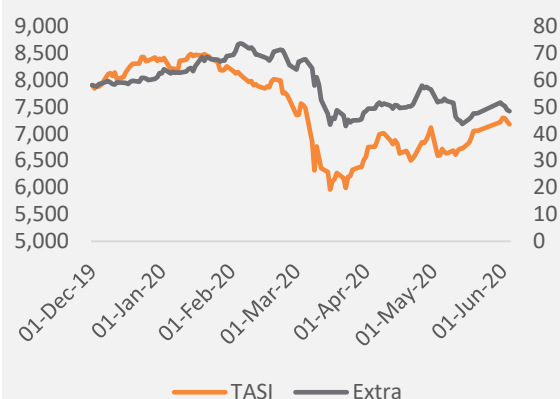
Key Financial Ratios

Ratio	Q1 2020	Q1 2019	Q4 2019
Revenue Growth	16.5%	16.1%	22.3%
Gross Margin	17.9%	16.0%	17.8%
EBIT Margin	4.1%	4.9%	4.5%
Net Margin	2.8%	3.8%	3.2%

Key Financial Results (Q1 2020)



Share Price Performance



Financial Projection

DCF Valuation

	2019 A	2020 E	2021 F	2022 F	2023 F	2024 F
EBITDA	348	310	409	499	593	694
Operating CF	27	(137)	(78)	61	213	464
Capex	(86)	(112)	(114)	(116)	(118)	(121)
FCFF	(60)	(249)	(192)	(55)	94	344
Stub Period (FCF to be discounted)	0	(188)	(192)	(55)	94	344
PV (FCFF)	0	(176)	(166)	(43)	69	226
WACC	8.9%					
Perpetuity Growth	3.0%					
PV-FCFF	0					
PV-TV	3,985					
Net Debt	(702)					
Less: End of services benefits	(62)					
Add: investments	0					
Intrinsic Values	3,129					
Shares Outstanding	60					
Equity value per share	52.2					
CMP (04-06-2020)	48.5					
Upside / (Downside%)	7.6%					

We have valued Extra using DCF approach, considering a WACC is equal to 8.9% (based on a risk-free rate of 4.4%, market risk premium 7.3%, Beta of 1.4).

Based on the DCF valuation, the fair price Extra share price is SAR52.2 which is higher than the traded value by 7.6%.

Financial Ratios

	2018A	2019A	2020E	2021F	2022F	2023F	2024F
Return on Average Assets (%)	8.9%	8.9%	4.6%	6.8%	7.9%	8.9%	9.9%
Return on Average Equity (%)	26.6%	31.5%	18.7%	28.8%	33.3%	35.4%	36.0%
Earnings Before Zakat Margin (%)	3.9%	4.3%	2.8%	4.2%	5.2%	6.0%	6.8%
Net Income Margin (%)	3.7%	4.0%	2.6%	4.0%	4.9%	5.7%	6.5%
Revenue Growth (%)	4.4%	16.9%	-2.9%	13.6%	10.0%	9.3%	8.2%
EPS	2.7	3.4	2.2	3.8	5.1	6.4	8.0

Income Statement

	2018A	2019A	2020E	2021F	2022F	2023F	2024F
Revenues	4,394	5,135	4,985	5,662	6,227	6,804	7,365
Cost of Revenues	(3,614)	(4,225)	(4,101)	(4,630)	(5,074)	(5,530)	(5,972)
Gross Profit	780	910	883	1,031	1,153	1,274	1,393
SG&A	(559)	(561)	(573)	(623)	(654)	(680)	(700)
Zakat	(8)	(12)	(10)	(14)	(17)	(21)	(24)
Net Income	161	206	130	226	304	387	478

Balance Sheet

	2018A	2019A	2020E	2021F	2022F	2023F	2024F
Current Assets	1,376	1,427	1,564	1,933	2,244	2,545	2,867
Non-Current Assets	590	1,208	1,436	1,665	1,874	2,058	2,175
Total Assets	1,966	2,635	3,000	3,598	4,118	4,603	5,042
Current Liabilities	1,178	1,325	1,491	1,808	2,119	2,371	2,555
Non-Current Liabilities	143	650	779	955	1,010	1,035	1,022
Total Equity	646	660	730	835	990	1,196	1,465
Total Liabilities and Equity	1,966	2,635	3,000	3,598	4,118	4,603	5,042

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 it 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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