



US\$1.135bn Market cap
51% Free float
US\$3.934mn Avg. daily volume

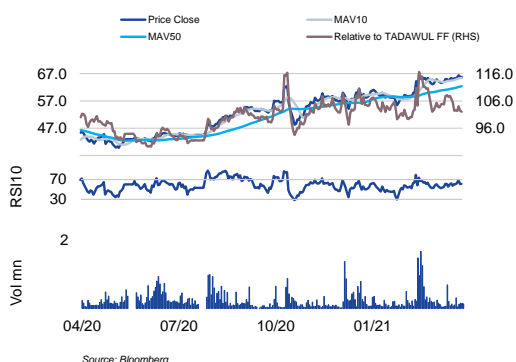
Target price **54.00** -18.0% over current
 Current price **66.00** as at 7/4/2021

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Existing rating
Underweight Neutral Overweight

Performance



Earnings

Period End (SAR)	12/19A	12/20A	12/21E
Revenue (mn)	1,288	1,076	1,239
Revenue growth	5.0%	-16.5%	15.2%
EBITDA (mn)	388	251	343
EBITDA growth	35%	-35%	37%
Net Profit	196	53	162
Net Profit Margin	15%	5%	13%
EPS	3.03	0.82	2.50
EPS growth	-4%	-73%	206%
DPS	2.10	1.00	1.75
Payout Ratio	69%	122%	70%
ROE	20%	6%	16%

Source: Company data, Al Rajhi Capital

Herfy Foods

Expect muted top-line growth due to rising competition; Downgrade to underweight

Herfy's Q1 FY2021 earnings of SAR25mn missed our expectations of SAR44mn, the main reason for the miss was lower revenue compared to our expectations and lower gross margins. The company in our view is facing competition from other international QSR's and expat exodus. We expect the top-line to remain flattish to marginally positive compared to FY 2019 level but a double-digit growth on a low base in FY 2020. The company opened 7 large-scale restaurants in FY 2020 and intends to open 12 new restaurants in FY 2021. Apart from local expansion it also aims to open 5 new stores in Nigeria each year till 2030 through franchise model (currently they operate through franchise model in Bangladesh and Kuwait). Herfy's revenue per store has been in a declining trend for the last couple of years and with population de-growth and competition from international QSR's we expect the ramp-up of new stores to further delay which will erode profit margins and the company's ROCE. Post Q1 2021 earnings we cut our FY 2021e forecast and expect a revenue/EBITDA/net-income growth of 15%/37%/206% y-o-y. We revise our tp lower to SAR54/sh from SAR58/sh as we see no near term catalyst, which can improve the revenue and margins for Herfy. Accordingly, we reduce the tp to SAR54/sh which implies "underweight" rating.

Q1 FY2021 earnings summary: Revenue increased 4% y-o-y to SAR310mn, the gross margins increased slightly by 65bps y-o-y. The operating profit declined 2% y-o-y mainly due to higher SG&A, which increased likely due to rising contribution of online sales thereby leading to a higher commission paid to food aggregators. The company disclosed in its earnings release that the interest expense and other income also declined y-o-y. The net income increased marginally 1.5% y-o-y to SAR25.5mn in Q1 2021.

Figure 1 Herfy 1Q 2021 earnings summary

(SAR mn)	1Q 2021	1Q 2020	Y-o-Y	4Q 2020	Q-o-Q	ARC est	vs ARC
Revenue	310	297	4%	298	4%	332	-7%
Gross profit	82	77	7%	78	5%	93	-12%
Gross margin	26%	26%		26%		28%	
Operating profit	34	35	-2%	30	14%	50	-31%
Operating margin	11%	12%		10%		15%	
Net profit	25	25	1%	21	24%	44	-42%
Net margin	8%	8%		7%		13%	

Source: Company data, Al Rajhi Capital

Valuations and Key Risks: We downgrade Herfy to sell as we expect the top-line growth to remain muted (compared to 2019) due to competition from other QSR's and population de-growth. We value the company using equal mix given to DCF and PE based relative valuation. Our PE based relative valuation based on 20x FY2021e EPS is SAR50/sh while DCF based tp based on 8.7% WACC and 2% terminal growth is SAR58/Sh. Thus equal weighted tp stands at SAR54/sh which implies 18% downside from CMP of SAR66/sh. We downgrade Herfy to "underweight".

Key Upside risks to our valuation: 1) Any new product launches or change in strategy will have a positive impact on revenue and poses an upside risk to our valuations.

2) Increase in tourism both religious and leisure will have an overall positive impact on company's earnings and valuations.



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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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