

Summary of our ratings

Stock	Current Rating	TP	CMP	Upside/downside
First Milling	N	57.00	57.00	0.0%
Modern Mills	N	37.00	36.95	0.1%

Source: Al Rajhi Capital Estimates. N = Neutral. CMP: close of 13 May 2025

Financial Summary - First Milling

(SAR Mn)	2024	2025E	2026E
Revenue	1,049	1,094	1,150
Revenue growth	8.8%	4.3%	5.1%
Gross profit	457	433	398
Gross margin	43.6%	39.6%	34.6%
EBITDA	374	356	309
EBITDA margin	35.7%	32.5%	26.9%
Net Income	251	244	186
Net margin	23.9%	22.3%	16.2%
EPS	4.52	4.40	3.35
DPS	2.84	2.86	2.18
Payout ratio	62.8%	65.0%	65.0%
P/E	12.6x	13.0x	17.0x
ROE	27.3%	25.7%	18.8%

Source: Company Data, Al Rajhi Capital Estimates.

Financial Summary - Modern Mills

(SAR Mn)	2024	2025E	2026E
Revenue	1,000	1,039	1,112
Revenue growth	6.6%	3.9%	7.0%
Gross profit	373	366	336
Gross margin	37.3%	35.2%	30.2%
EBITDA	319	311	268
EBITDA margin	31.9%	30.0%	24.1%
Net Income	209	220	173
Net margin	20.9%	21.1%	15.6%
EPS	2.55	2.69	2.12
DPS	2.00	2.00	1.50
Payout ratio	78.4%	74.5%	70.8%
P/E	14.5x	13.8x	17.4x
ROE	81.8%	75.6%	50.4%

Source: Company Data, Al Rajhi Capital Estimates.

First Milling & Modern Mills

Turn Neutral on expectation of gradual decline in primary margins

- We update our investment case for First Milling and Modern Mills with a Neutral rating and fair value of SAR57/sh and SAR37/sh respectively
- Our base case investment thesis, is premised on expectation of regulator gradually increasing the cost of wheat for milling companies (from current cost of SAR180/ton) while maintaining the current regulated flour price at SAR500/ton. We are of the opinion that that the current net margins of the milling companies (north of 20%) does not seem economically rational given the fact the milling companies sell a commodity and operate in a highly regulated environment with low risk of demand (flour is an essential staple item) and a fixed primary margin (both end product price and cost of raw material is fixed).

Base Case Investment Thesis: Details of our Base case investment thesis are:

- In our base case, we assume that the regulator shall gradually increase the cost of wheat for milling companies (from current cost of SAR180/ton) while maintaining the current regulated flour price at SAR500/ton. This we believe should not only reduce the cost of subsidy for the government but also will not have any negative socio-economic impact as highlighted in the Bear case
- We are of the opinion that the current net margins of the milling companies (north of 20%) does not seem economically rational given the fact the milling companies sell a commodity and operate in a regulated environment with low risk of demand (flour is an essential staple item) and a fixed primary margin (both end product price and cost of raw material is fixed)
- Furthermore, the fact that the original investors who acquired the milling companies as part of the privatization process have already recovered (and in some cases significantly exceeded) their cost of acquisition points to the fact that the reduction in subsidy would not in any way negatively impact the Kingdom's goals of increasing private sector contribution to the economy and investments by the private sector
- We believe both the milling companies would try to mitigate the impact of margin compression through growth in sales volumes for both flour (in the export market) and animal feed
- Additionally, there is a possibility that the milling companies might try to pass-on the impact of increase in wheat prices to the non-regulated segment (less than 45Kg bags). However, given that around 80% of the sale volumes occur in 45kg bags and in bulk volume, any increase in prices of non-regulated segment (even-though it would be difficult to implement) would likely not completely pass-on the impact of increase in wheat cost.

Medium-term Expectations - First Milling & Modern Mills: Summary of medium-term expectation of First Milling and Modern Mills is as follows:

- First Milling:** Earnings are expected to contract by 39% between 2025-28 on the back of 960bps reduction in gross margin as the subsidy on wheat flour is expected to gradually reduce. As a result, company's net margins are expected to decline to ~12%-13% range from 2028 onwards (from 2024 net margins of 24%)

- **Modern Mills:** Similarly, earnings are expected to contract by 38% between 2025-28 on the back of 1024bps reduction in gross margin as the subsidy on wheat flour is expected to gradually reduce. As a result, company's net margins are expected to decline to ~12% from 2028 onwards (from 2024 net margins of 21%).

Recommendation and Valuation:

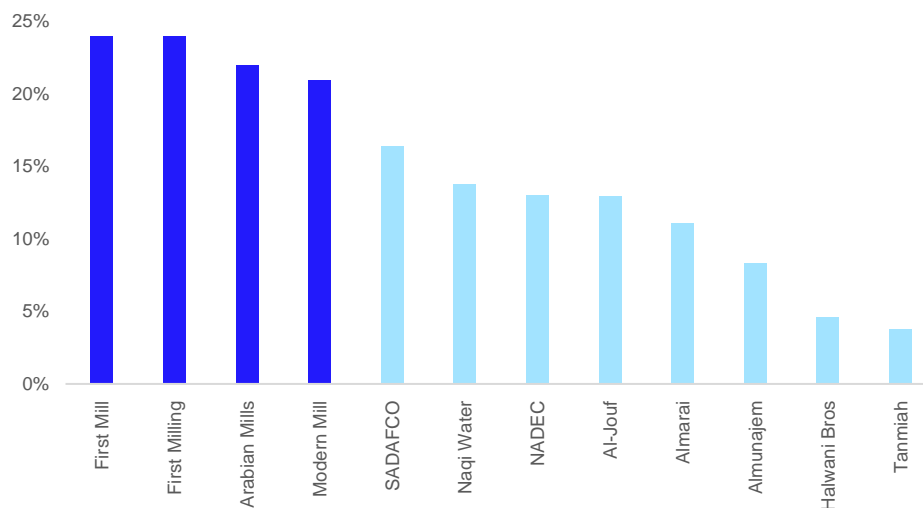
We value both the milling companies in our coverage using discounted cashflow method, using a cost of equity of 10.5% and terminal growth rate of 2.5%. Our fair value of First Milling and Modern Mill stands at SAR57/sh and SAR37/sh respectively. Hence, we turn Neutral on both the milling companies in our coverage universe.

Figure 1 **Valuation**

DCF Valuation		First Milling	Modern Mills
DCF Valuation	SAR/sh	57.00	37.00
CMP	SAR/sh	57.00	36.95
Upside/(Downside)	%	0.0%	0.1%
Dividend yield	%	5.0%	5.4%
Total returns	%	5.0%	5.5%

Source: Company Data, Al Rajhi Capital estimates

Figure 2 **2024 Recurring Net Margins in Food & Beverage Sector**



Source: Company Data, Al Rajhi Capital.

Figure 3 **Return of Original investors**

		First Milling	Modern Mills
Privatization Cost	USD Mn	(540)	(238)
Dividend Received (from Privatization till IPO)	"	212	192
Net IPO Proceeds	"	255	314
Proportionate dividends received since IPO till Jun-25	"	58	46
Dividends & IPO Proceed	"	525	552

Source: Company data, Al Rajhi Capital.

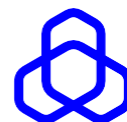


Figure 4 Investment Case

Investment Case		Bear Case	Base Case	Bull Case
Change in Subsidy Mechanism		Subsidy removed	Subsidy is reduced gradually	Current Subsidy extended for 6 month/1 Year
Probability		Low	Medium to High	Low to Medium
Rational for Probability		Wheat is an essential staple and a vital component of Kingdom's food security strategy. Complete removal of the subsidy mechanism can lead to food security risks.	In our base case, we assume that the regulator shall gradually increase the cost of wheat for milling companies (from current cost of SAR180/ton) while maintaining the current regulated flour price at SAR500/ton. This we believe should not only reduce the cost of subsidy for the government but also will not have any negative socio-economic impact as highlighted in the Bear case.	The current subsidy mechanism shall end on 12th June, 2025. The regulator might require more time in finalizing the changes in subsidy mechanism since it has significant consequences.
		In our opinion, the current cost of subsidy on wheat (~SAR3.5bn or 0.3% of the total fiscal expenditure for 2024) is immaterial given the socio-economic impact of the increase in flour/bread prices (being a staple item having a weight of ~1% in the CPI basket in KSA). As per our calculations, if the subsidy on wheat is removed the regulated price of flour would grow by around 2.5x from its current level of SAR500/ton to SAR1,260/ton (even if we assume that the margin on wheat milling goes down from SAR320/ton to SAR60/ton). This in-turn would contribute an addition of ~270bps to the country's inflation (or increase it from 2.3% level in Mar-25 to 5.0%).	We are of the opinion that the current net margins of the milling companies (north of 20%) does not seem economically rational given the fact the milling companies sell a commodity and operate in a highly regulated environment with low risk of demand (flour is an essential staple item) and a fixed primary margin (both end product price and cost of raw material is fixed). Furthermore, the fact that the original investors who acquired the milling companies as part of the privatization process have already recovered (and in some cases significantly exceeded) their cost of acquisition points to the fact that the reduction in subsidy would not in any way negatively impact the Kingdom's goals of increasing private sector contribution to the economy and investments by the private sector.	
Impact		As per First Milling company's mangement the gross margins on export markets (competative market without subsidy) ranges from low single-digit to low double digit. The operating expense (as a percentage of sales) for First Milling and Modern Mills is around 13% and 11% respectively.	We expect the cost of wheat to increase by SAR35/ton annually starting from 2Q25 untill the net margins of the milling companies come in-line with the rest of the food and beverage industry (this as per our calculation would require cost of wheat to be increased gradually till 2027).	The current margins of the companies would largely remain stable (largely, not same, because both the milling companies in our coverage aim at increasing export of flour).
		Additionally, a complete reduction in subsidy would signifiactly increase the working capital requirement for the milling companies leading to a higher debt. (This is the reason First Milling signed a SAR630mn bank facility with SAB despite only having Capex requirement of SAR280mn - this capex requirement includes contingent capex for acquisition of a feed mill)	As a result, net margins of First Milling would reduce to ~12%-13% (24% in 2024) and the sustainable net margins of Modern Mill would reduce to ~12% (from 21% in 2024).	Even if the subsidy is extended for a limited/short period, we opion that the share prices of listed milling companies would remain subdued due to the overhang of removal of subsidy in the future.

Source: Company data, Al Rajhi Capital.



Financials – First Milling

Figure 5 Income Statement

SAR Mn	2024	2025E	2026E
Revenue	1,049	1,094	1,150
<i>y-o-y growth</i>	8.8%	4.3%	5.1%
Cost of Sales	592	661	752
Gross Profit	457	433	398
<i>y-o-y growth</i>	10.6%	-5.2%	-8.2%
<i>margins</i>	43.6%	39.6%	34.6%
Operating Profit	318	295	248
<i>y-o-y growth</i>	11.0%	-7.3%	-15.9%
<i>margins</i>	30.4%	27.0%	21.6%
Net Income	251	244	186
<i>y-o-y growth</i>	13.9%	-2.7%	-23.9%
<i>margins</i>	23.9%	22.3%	16.2%
EPS	4.52	4.40	3.35

Source: Company Data, Al Rajhi Capital estimates

Figure 7 Ratios and Multiples

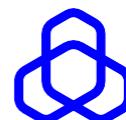
	2024	2025E	2026E
ROE	27.3%	25.7%	18.8%
(Debt+Lease)/EBITDA (x)	3.6	3.8	4.1
P/E (x)	12.6	13.0	17.0
D/Y	5.0%	5.0%	3.8%
EV/EBITDA (x)	11.5	12.2	14.0

Source: Company Data, Al Rajhi Capital estimates

Figure 6 Balance Sheet

SAR Mn	2024	2025E	2026E
Cash and cash equivalents	193	181	113
Inventories	162	174	185
Trade receivables	19	20	20
Others	31	30	30
Current Assets	404	406	349
Property, plant and equipment	682	750	818
Right-of-use assets	300	285	270
Intangible assets	9	11	11
Goodwill	1,091	1,091	1,091
Others	10	10	10
Total Assets	2,496	2,553	2,548
Trade and other payables	60	68	72
Long-term loans	162	165	100
Lease liabilities	31	33	32
Others	107	150	150
Current Liability	361	416	354
Long term loans	848	850	850
Lease liabilities	309	299	291
Others	32	30	30
Total Liability	1,550	1,595	1,526
Share capital	555	555	555
Retained earnings	333	347	412
Reserves & Others	57	55	55
Total Equity	945	957	1,022
Total Liabilities & Equity	2,496	2,553	2,548

Source: Company Data, Al Rajhi Capital estimates



Financials – Modern Mills

Figure 8 Income Statement

SAR Mn	2024	2025E	2026E
Revenue	1,000	1,039	1,112
<i>y-o-y growth</i>	6.6%	3.9%	7.0%
Cost of Sales	627	673	776
Gross Profit	373	366	336
<i>y-o-y growth</i>	8.0%	-1.9%	-8.2%
<i>margins</i>	37.3%	35.2%	30.2%
Operating Profit	259	253	208
<i>y-o-y growth</i>	2.2%	-2.5%	-17.5%
<i>margins</i>	25.9%	24.3%	18.7%
Net Income	209	220	173
<i>y-o-y growth</i>	3.4%	5.3%	-21.1%
<i>margins</i>	20.9%	21.1%	15.6%
EPS	2.55	2.69	2.12

Source: Company Data, Al Rajhi Capital estimates

Figure 10 Ratios and Multiples

	2024	2025E	2026E
ROE	81.8%	75.6%	50.4%
(Debt+Lease)/EBITDA (x)	2.8	2.4	3.0
P/E (x)	14.5	13.8	17.4
D/Y	5.4%	5.4%	4.1%
EV/EBITDA (x)	11.7	12.0	14.0

Source: Company Data, Al Rajhi Capital estimates

Figure 9 Balance Sheet

SAR Mn	2024	2025E	2026E
Cash and cash equivalents	183	41	79
Inventories	87	101	106
Trade receivables	10	12	12
Others	36	20	20
Current Assets	316	174	217
Property, plant and equipment	778	860	923
Right-of-use assets	207	196	187
Intangible assets	4	5	5
Total Assets	1,304	1,234	1,332
Trade and other payables	53	51	53
Current portion of long-term loans	30	30	30
Current portion lease liabilities	14	14	13
Others	99	100	100
Current Liability	195	194	196
Long term loans	617	500	550
Lease liabilities	221	214	209
Others	7	7	7
Total Liability	1,041	916	963
Share capital	82	82	82
Retained earnings	206	262	313
Reserves & Others	(25)	(25)	(25)
Total Equity	263	319	369
Total Liabilities & Equity	1,304	1,234	1,332

Source: Company Data, Al Rajhi Capital estimates

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