



Fawaz Abdulaziz Alhokair Co. (AlHokair) posted Q4-18 earnings below estimates. Revenue growth is expected to remain subdued in the near term, mainly attributable to sluggish consumer demand driven by decline in customer base. To improve profitability, AlHokair has lowered its store count by closing down non-profitable ones. We expect consumer demand to increase gradually, boosted by an increase in disposable income driven by economic growth and higher employment rate. Margins are expected to remain stable in the medium term, driven by cost-cutting initiatives. We upgrade AlHokair to “**Overweight**” view with a TP of **SAR 24.30/share**.

**Revenue growth to remain subdued in near term:** AlHokair posted a loss of SAR 141.0mn in Q4-18, below AJC’s and the market consensus estimate of SAR 35.5mn and SAR 25.2mn, respectively. Revenue declined 10.1% Y/Y due to subdued consumer demand and reduced store count (net reduction in number of stores in FY18 stood at 170). We expect revenue per store to increase marginally in FY19 as the company closes more non-profitable stores in FY19. However, revenue growth is expected to be relatively flat in FY19. We expect a rebound in demand from FY20, which should benefit AlHokair in the medium term.

**Closure of non-profitable stores and cost reduction measures to enhance margins in medium term:** AlHokair’s GP margin decreased Y/Y in Q4-18 to 3.2% from 3.8%. This was mainly due to higher provision, on inventory shrinkage and slow-moving inventory, which was SAR 145mn in Q4-18 Vs. SAR 78.1mn in Q4-17. The Operating margins improved to -4.9% in Q4-18 from -11.8% in Q4-17 due to the optimization of head-office and back-office expenses, and closure of non-profitable stores. GP margin of AlHokair increased to 20.0% in FY18 Vs. 19.9% in FY17. The provisioning expenses would be lower in FY19 as compared to FY18, as the company has already done close to 90% of its planned store closures. This is expected to result in increase in GP margin in FY19.

**Improvement in international business augurs well in the long run:** The net loss of international business improved by 52.5% in FY18 (SAR 66mn in FY18 Vs. SAR 139mn in FY17). Key initiatives such as focus on growth potential markets (Egypt, Georgia), development of trade fairs for brands generating good returns, and focusing on profitable brands should turnaround the international operations. We expect that it would take another couple of years for international operations to be profitable.

**Portfolio diversification, e-commerce, pick-up in retail demand to drive long-term growth:** AlHokair plans to launch its e-commerce platform shortly; it would form a new, modern channel for sales generation. To diversify its portfolio, the company is looking to explore other avenues such as cinemas and restaurants. It is in talks with operators of entertainment cities to increase its presence in upcoming shopping malls. We expect retail demand to pick up in FY20, driven by higher disposable income and a rising employment (due to the Saudization drive).

**AJC View and Valuation:** We believe AlHokair stands to benefit from increased retail demand, which would be the company’s key driver of growth in the long run. We have modeled an increase in store count from 1,694 in FY18 to 1,924 at the end of FY22, coupled with a low-single-digit increase in average revenue per store. AlHokair is close to completing its target of closing non-profitable stores. We expect the company to focus on expansion going forward. We value AlHokair on 50% weight for DCF (3.0% terminal growth and 7.8% WACC), 25% weight each for P/E (18.6x FY19 EPS) and EV/EBITDA (9.8x FY19 EBITDA) based relative valuation. These yield a target price of **SAR24.3 per share**, implying a 11.2% upside from the current levels. The stock is currently trading at a P/E of 17.1x, based on our FY19 EPS estimate. We upgrade AlHokair to “**Overweight**” rating from ‘**Neutral**’.

## Overweight

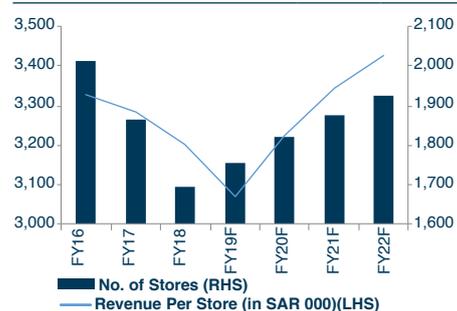
**Target Price (SAR)** 24.30  
**Upside / (Downside)\*** 11.2%

Source: Tadawul \*prices as of 5<sup>th</sup> of July 2019

### Key Financials

SARmn (unless specified)	FY17	FY18	FY19E
Revenue	6,116.5	5,425.8	5,447
Gross Profit	1,214.6	1,084.5	1,223.7
Net Profit	103.5	144.7	268.1
EPS	0.49	0.69	1.28

### No. of Stores and Revenue per Store



Source: Bloomberg, AlJazira Capital, Y/E March

### Key Ratios

SARmn (unless specified)	FY17	FY18	FY19E
Gross Margin	19.9%	20.0%	22.5%
Net Margin	1.7%	2.7%	4.9%
P/E	54.3x	35.6x	17.1x
P/B	2.6x	2.1x	1.7x
EV/EBITDA (x)	13.3x	10.5x	8.6x

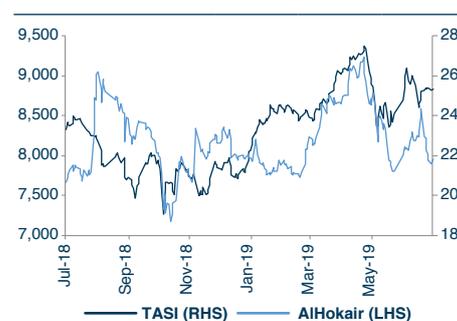
Source: Company reports, AlJazira Capital

### Key Market Data

Market Cap (bn)	4.6
YTD %	-0.70%
52 Week (High)/(Low)	27.1/17.6
Shares Outstanding (mn)	210.0

Source: Company reports, AlJazira Capital

### Price Performance



Source: Tadawul, AlJazira Capital

Senior Analyst

Jassim Al-Jubran

+966 11 2256248

i.aliabran@aljaziracapital.com.sa



## Investment Update

### Key Financial Data

Amount in SAR mn, unless otherwise specified	FY16	FY17	FY18	FY19E	FY20E	FY21E	FY22E
<b>Income statement</b>							
Revenues	6,692	6,117	5,426	5,447	5,788	6,118	6,404
Y/Y	-3.6%	-8.6%	-11.3%	0.4%	6.3%	5.7%	4.7%
Cost of Sales	(5,175)	(4,902)	(4,341)	(4,223)	(4,494)	(4,747)	(4,970)
<b>Gross profit</b>	<b>1,517</b>	<b>1,215</b>	<b>1,084</b>	<b>1,224</b>	<b>1,294</b>	<b>1,370</b>	<b>1,434</b>
Selling and marketing expenses	(254)	(248)	(180)	(192)	(199)	(207)	(214)
General and Administrative exp	(333)	(322)	(281)	(277)	(289)	(302)	(313)
Depreciation and amortization	(310)	(318)	(290)	(310)	(332)	(353)	(377)
Other income	-	(13)	79	45	41	31	32
<b>Operating profit</b>	<b>620</b>	<b>314</b>	<b>412</b>	<b>489</b>	<b>515</b>	<b>539</b>	<b>563</b>
YoY growth	-27.2%	-49.4%	31.3%	18.7%	5.3%	4.5%	4.4%
Financial charges	(167)	(181)	(201)	(194)	(175)	(128)	(94)
<b>Profit before zakat</b>	<b>502</b>	<b>133</b>	<b>193</b>	<b>295</b>	<b>381</b>	<b>441</b>	<b>501</b>
Zakat	(31)	(43)	(55)	(32)	(23)	(26)	(30)
<b>Net income</b>	<b>434</b>	<b>103</b>	<b>145</b>	<b>268</b>	<b>362</b>	<b>419</b>	<b>475</b>
Y/Y	-29.5%	-76.2%	39.9%	85.2%	35.0%	15.7%	13.5%
<b>Balance sheet</b>							
<b>Assets</b>							
Cash & bank balance	365	331	516	1,437	939	741	762
Other current assets	2,927	2,919	3,038	2,430	2,583	2,729	2,857
Property & Equipment	1,904	2,046	1,752	1,616	1,574	1,508	1,452
Other non-current assets	1,444	1,416	1,401	1,401	1,401	1,401	1,401
<b>Total assets</b>	<b>6,639</b>	<b>6,711</b>	<b>6,707</b>	<b>6,884</b>	<b>6,497</b>	<b>6,379</b>	<b>6,472</b>
<b>Liabilities &amp; owners' equity</b>							
Total current liabilities	3,191	2,501	2,112	1,845	1,703	1,611	1,554
Total non-current liabilities	1,346	2,025	2,184	2,359	1,754	1,309	983
Paid -up capital	2,100	2,100	2,100	2,100	2,100	2,100	2,100
Statutory reserves	181	191	206	233	269	311	358
Other reserve	(532.9)	(525.5)	(452.2)	(452.2)	(452.2)	(452.2)	(452.2)
Retained earnings	365	482	624	865	1,191	1,568	1,995
Minority interest	(11)	(64)	(67)	(67)	(67)	(67)	(67)
Total owners' equity	2,102	2,185	2,411	2,679	3,041	3,460	3,935
<b>Total equity &amp; liabilities</b>	<b>6,639</b>	<b>6,711</b>	<b>6,707</b>	<b>6,884</b>	<b>6,497</b>	<b>6,379</b>	<b>6,472</b>
<b>Cashflow statement</b>							
Operating activities	624	782	712	652	617	695	786
Investing activities	(236)	(491)	114	30	(289)	(288)	(320)
Financing activities	(320)	(290)	(556)	238	(825)	(606)	(444)
Change in cash	68	1	270	920	(498)	(198)	21
<b>Ending cash balance</b>	<b>365</b>	<b>331</b>	<b>516</b>	<b>1,437</b>	<b>939</b>	<b>741</b>	<b>762</b>
<b>Key fundamental ratios</b>							
<b>Liquidity ratios</b>							
Current ratio (x)	1.0	1.3	1.7	2.1	2.1	2.2	2.3
Quick ratio (x)	0.5	0.6	0.8	1.3	1.1	1.1	1.2
<b>Profitability ratios</b>							
Gross profit margin	22.7%	19.9%	20.0%	22.5%	22.4%	22.4%	22.4%
Operating margin	9.3%	5.1%	7.6%	9.0%	8.9%	8.8%	8.8%
EBITDA margin	13.9%	10.3%	12.9%	14.7%	14.6%	14.6%	14.7%
Net profit margin	6.5%	1.7%	2.7%	4.9%	6.3%	6.8%	7.4%
Return on assets	6.5%	1.6%	2.2%	3.9%	5.4%	6.5%	7.4%
Return on equity	22.3%	4.7%	6.1%	10.3%	12.4%	12.6%	12.6%
<b>Market/valuation ratios</b>							
EV/sales (x)	1.4	1.4	1.4	1.3	1.2	1.1	1.1
EV/EBITDA (x)	10.4	13.3	10.5	8.6	8.1	7.7	7.3
EPS (SAR)	2.1	0.5	0.7	1.3	1.7	2.0	2.3
BVPS (SAR)	10.0	10.4	11.5	12.8	14.5	16.5	18.7
Market price (SAR)*	32.2	26.8	24.5	21.8	21.8	21.8	21.8
Market-Cap (SAR mn)	6,751.5	5,619.0	5,153.4	4,586.4	4,586.4	4,586.4	4,586.4
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
P/E ratio (x)	15.5	54.3	35.6	17.1	12.7	11.0	9.7
P/BV ratio (x)	3.2	2.6	2.1	1.7	1.5	1.3	1.2

Source: Company financials, AlJazira research (Y/E is March)



RESEARCH DIVISION

Head of Research  
**Talha Nazar**  
+966 11 2256250  
t.nazar@aljaziracapital.com.sa

Senior Analyst  
**Jassim Al-Jubran**  
+966 11 2256248  
j.aljabran@aljaziracapital.com.sa

Analyst  
**Abdulrahman Al-Mashal**  
+966 11 2256374  
A.Almashal@Aljaziracapital.com.sa

BROKERAGE AND INVESTMENT CENTERS DIVISION

General Manager – Brokerage Services & sales  
**Alaa Al-Yousef**  
+966 11 2256060  
a.yousef@aljaziracapital.com.sa

AGM-Head of international and institutional brokerage  
**Luay Jawad Al-Motawa**  
+966 11 2256277  
lalmutawa@aljaziracapital.com.sa

AGM-Head of Qassim & Eastern Province  
**Abdullah Al-Rahit**  
+966 16 3617547  
aalrahit@aljaziracapital.com.sa

AGM-Head of Sales And Investment Centers  
Central Region, & acting head Western and Southern Region Investment Centers  
**Sultan Ibrahim AL-Mutawa**  
+966 11 2256364  
s.almutawa@aljaziracapital.com.sa

RESEARCH DIVISION

AlJazira Capital, the investment arm of Bank AlJazira, is a Shariaa Compliant Saudi Closed Joint Stock company and operating under the regulatory supervision of the Capital Market Authority. AlJazira Capital is licensed to conduct securities business in all securities business as authorized by CMA, including dealing, managing, arranging, advisory, and custody. AlJazira Capital is the continuation of a long success story in the Saudi Tadawul market, having occupied the market leadership position for several years. With an objective to maintain its market leadership position, AlJazira Capital is expanding its brokerage capabilities to offer further value-added services, brokerage across MENA and International markets, as well as offering a full suite of securities business.

RATING TERMINOLOGY

- Overweight:** This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
- Underweight:** This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
- Neutral:** The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
- Suspension of rating or rating on hold (SR/RH):** This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

## Disclaimer

The purpose of producing this report is to present a general view on the company/economic sector/economic subject under research, and not to recommend a buy/sell/hold for any security or any other assets. Based on that, this report does not take into consideration the specific financial position of every investor and/or his/her risk appetite in relation to investing in the security or any other assets, and hence, may not be suitable for all clients depending on their financial position and their ability and willingness to undertake risks. It is advised that every potential investor seek professional advice from several sources concerning investment decision and should study the impact of such decisions on his/her financial/legal/tax position and other concerns before getting into such investments or liquidate them partially or fully. The market of stocks, bonds, macroeconomic or microeconomic variables are of a volatile nature and could witness sudden changes without any prior warning, therefore, the investor in securities or other assets might face some unexpected risks and fluctuations. All the information, views and expectations and fair values or target prices contained in this report have been compiled or arrived at by Al-Jazira Capital from sources believed to be reliable, but Al-Jazira Capital has not independently verified the contents obtained from these sources and such information may be condensed or incomplete. Accordingly, no representation or warranty, express or implied, is made as to, and no reliance should be placed on the fairness, accuracy, completeness or correctness of the information and opinions contained in this report. Al-Jazira Capital shall not be liable for any loss as that may arise from the use of this report or its contents or otherwise arising in connection therewith. The past performance of any investment is not an indicator of future performance. Any financial projections, fair value estimates or price targets and statements regarding future prospects contained in this document may not be realized. The value of the security or any other assets or the return from them might increase or decrease. Any change in currency rates may have a positive or negative impact on the value/return on the stock or securities mentioned in the report. The investor might get an amount less than the amount invested in some cases. Some stocks or securities maybe, by nature, of low volume/trades or may become like that unexpectedly in special circumstances and this might increase the risk on the investor. Some fees might be levied on some investments in securities. This report has been written by professional employees in Al-Jazira Capital, and they undertake that neither them, nor their wives or children hold positions directly in any listed shares or securities contained in this report during the time of publication of this report, however, The authors and/or their wives/children of this document may own securities in funds open to the public that invest in the securities mentioned in this document as part of a diversified portfolio over which they have no discretion. This report has been produced independently and separately by the Research Division at Al-Jazira Capital and no party (in-house or outside) who might have interest whether direct or indirect have seen the contents of this report before its publishing, except for those whom corporate positions allow them to do so, and/or third-party persons/institutions who signed a non-disclosure agreement with Al-Jazira Capital. Funds managed by Al-Jazira Capital and its subsidiaries for third parties may own the securities that are the subject of this document. Al-Jazira Capital or its subsidiaries may own securities in one or more of the aforementioned companies, and/or indirectly through funds managed by third parties. The Investment Banking division of Al-Jazira Capital maybe in the process of soliciting or executing fee earning mandates for companies that is either the subject of this document or is mentioned in this document. One or more of Al-Jazira Capital board members or executive managers could be also a board member or member of the executive management at the company or companies mentioned in this report, or their associated companies. No part of this report may be reproduced whether inside or outside the Kingdom of Saudi Arabia without the written permission of Al-Jazira Capital. Persons who receive this report should make themselves aware, of and adhere to, any such restrictions. By accepting this report, the recipient agrees to be bound by the foregoing limitations.

Asset Management | Brokerage | Corporate Finance | Custody | Advisory

Head Office: King Fahad Road, P.O. Box: 20438, Riyadh 11455, Saudi Arabia. Tel: 011 2256000 - Fax: 011 2256068