

AlJouf Agriculture: Disappointing 3Q2017 earnings at SAR 11.47mn due to SAR 6.81mn drop in sales and higher than expected COGS that is partially ascribed to higher depreciation rate amounting to SAR 10.1mn after IFRS implementation. Gross margin contracted on YoY basis to 20.58% Vs. 39.27% due to higher contribution rate of low-margin products. Bottom line was supported by lower OPEX of SAR 3.2mn and a decline in other expenses. The company is expected to maintain recording YoY sales decline and weak margin in 4Q2017. We remain "Neutral" with lower PT at SAR 25.40/share.

- AlJouf Agriculture Company (AlJouf) result came below estimates, missing AJC profits estimates of SAR 19.60mn. AlJouf Agriculture Company posted net income of SAR 11.47mn; indicating a fall of 65.1%YoY and an increase of 48.8%QoQ. The weak profitability is mainly attributed to i) SAR 6.81mn drop in sales ii) SAR 17.2mn higher cost of goods sold, despite the YoY decline in OPEX by SAR 3.2mn. Although the company's revenues came broadly above our estimates; the higher deviation in bottom line with our estimates was strongly impacted by higher than expected production cost that is partially ascribed to an increase of SAR 10.1mn in depreciation rate after IFRS implementation, despite lower than expected other expense and SG & A expenses. We believe that the company's higher production cost in 3Q2017 compared to the same period last year was due to overall sales decline and a decline in sales of products with high margins such as wheat and green fodder. This is expected to comply with the previous decision to reduce the cultivation of mentioned products. Thus, the impact of higher COGS is likely to continue in 4Q2017 and onwards.
- The company reported a 5.6%YoY decline in revenue for 3Q2017 to SAR 114.02mn, above AJC estimate of 108.2mn, and SAR 67.2mn in 2Q2017 which was due to harvest seasonal impact. Despite the seasonal productivity and a strong demand on some products categories, the sales decline is expected to be due to a decline in green fodder and wheat cultivation. However, after the decision of completely phase out wheat production by the end of 2017, the Ministry of Environment, Water and Agriculture allowed the cultivation of wheat in an area not exceeding 50 hectares (0.5mn square meter), that would help mitigate the impact on future production. Moreover, we believe that government initiatives to stop domestic production of green fodder would noticeably impact Al-Jouf's total revenue from green fodder by end of 2018/2019 and onwards, to stand at 19.5% in FY2019 of total sales, as compared to 33.4% in FY2016.
- AlJouf reported a 50.5%YoY decline in gross profit to SAR 23.46mn, below our estimates of SAR 36.2mn and SAR 47.4mn in 3Q2016. The company's gross margin contracted 1,869 bps YoY to 20.58% due to higher COGS compared to the same period last year. We believe the deviation is mainly attributed to higher contribution of low-margin products to total sales volume and higher depreciation rate after IFRS implementation. In 3Q2017, the Company registered an increase in depreciation rate by 78.5%QoQ to stand at SAR 22.8mn from SAR 12.7mn in 3Q2016. Operating expenses came at SAR 10.23mn, as compared to our estimates of SAR SAR 11.4mn and SAR 12.9mn in 3Q2016 that could be largely driven by better than expected operational efficiencies.

AJC View: Based on the 9M-2017 performance, we expect the company to maintain recording YoY sales decline in 4Q2017 due to the impact of low wheat cultivation & green fodder production decline. However, the successful expansions in olive cultivation and other crops with high margin such as potatoes are expected to help the company to lower the future impact. We believe that the ongoing tendency to sell a large part of the crops before harvest would mitigate the future input cost. Furthermore, we believe that the company needs to set plans to increase efficiency; which could be a key factor in countering the upcoming risk of energy prices hikes. AlJouf Agriculture Co. is expected to post SAR 40.1mn in net income (1.34 EPS) for FY2017, recording a fall of 42.4%YoY due to sales decline and higher COGS. Thus, we remain our 'Neutral' recommendation for the stock with lower TP at SAR 25.40/share; indicating a potential upside of 6.3% over current market price. The company is trading at a forward PE and PB of 17.8x and 0.87x respectively based on our FY2017 earnings forecast. We expect the company to maintain its dividend payment at SAR 1.0 DPS (4.1% D/Y) in FY2017.

Results Summary

SARmn (unless specified)	Q3-2016	Q2-2017	Q3-2017	Change YoY	Change QoQ	Deviation from AJC Estimates
Revenue	120.83	67.21	114.02	-5.6%	69.7%	5.4%
Gross Profit	47.45	22.25	23.46	-50.5%	5.4%	-35.2%
Gross Margin	39.27%	33.11%	20.58%	-	-	-
EBIT	34.45	12.07	13.22	-61.6%	9.5%	-46.8%
Net Profit	32.88	7.71	11.47	-65.1%	48.8%	-41.5%
EPS	1.10	0.26	0.38	-	-	-

Source: Company reports, Aljazira Capital

Recommendation	'Neutral'
Current Price* (SAR)	23.90
Target Price (SAR)	25.40
Upside / (Downside)	6.3%

Source: Tadawul * 07th of November 2017

Key Financials

SARmn (unless specified)	FY15	FY16	FY17E
Revenue	369.0	380.2	346.3
Growth %	5.3%	3.1%	-8.9%
Net Income	72.40	69.74	40.14
Growth %	-32.3%	-3.7%	-42.4%
EPS	2.41	2.32	1.34

Source: Company reports, Aljazira Capital

Key Ratios

SARmn (unless specified)	FY15	FY16	FY17E
Gross Margin	33.1%	35.7%	25.5%
Net Margin	19.6%	18.3%	11.6%
P/E	13.82x	14.92x	17.86x
P/B	1.30	1.27	0.87
EV/EBITDA (x)	8.56x	8.27x	5.02x
Dividend Yield	3.0%	2.9%	4.1%

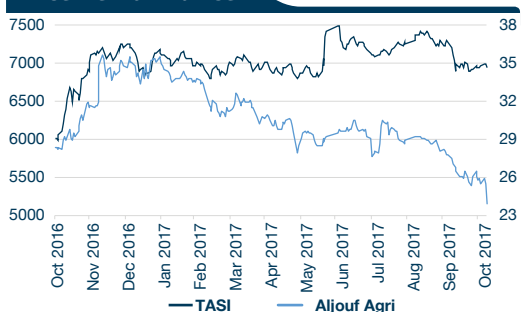
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (mn)	713.4
YTD %	-31.8%
52 Week (High)	37.00
52 Week (Low)	23.10
Shares Outstanding (mn)	30.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Bloomberg, Aljazira Capital

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2. **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.
3. **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.
4. **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.

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