

FITNESS TIME

OVERWEIGHT
CURRENT PRICE SAR55.8
INITIATING COVERAGE

UPSIDE +23.5%
TARGET PRICE SAR68.9

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This is an extract of our published report, the full version of which can be found on the Alahlicapital.com website

Female gyms to drive healthy earnings growth

We initiate coverage on Fitness Time (Leejam) with an Overweight rating and a PT of SAR68.9. We believe Fitness Time will benefit from certain structural changes under Vision 2030, namely those that aim at increasing physical activity among citizens. The company is aggressively expanding its female fitness centre base. We believe the increased disposable income of women, as a result of their higher participation in the workforce, will be a key catalyst for the success of this segment. The company trades at an attractive 2019f PE of 15.1x vs the global peers average of 19.6x.

- Female fitness centres to fuel top-line growth:** Following the licensing of female fitness centres in July 2017, Fitness Time opened 23 female fitness centres in Saudi to date. The company plans to continue its expansion plan to benefit from 1) the fast ramp-up period of 1-3 months vs 12 months for male centres and 2) higher disposable income of ladies, with the ability to capture market despite offering minimal price discounts. We forecast female branches to reach 25 by year end and 75 by 2023f. We expect 9.4% CAGR in number of centres and 11.8% revenue CAGR between 2017 and 2023f.
- Diverse service portfolio supports outlook:** Fitness Time is the most dominant player in the Saudi fitness sector, with a 27% membership share and 12% share of fitness centre count. We believe the company is well positioned to benefit from the government's Vision 2030 emphasis on a healthier lifestyle. Fitness Time has six gym formats to service all demographics, which is a key positive.
- Low barrier to entry risk offset by consolidation trends:** The current level of competition in the Saudi fitness market is expected to increase further due to the growth prospects of female centres and low barriers to entry for local players. However, like other consumer subsectors, we believe the fitness industry in Saudi will consolidate. The top five players currently have a 38% share in member count and 20% share in centre count.
- Initiate with an Overweight rating and PT of SAR68.9:** We initiate on Fitness Time with an Overweight rating and a target price of SAR68.9. The stock is trading at an attractive 2019f PE of 15.1x vs global peers at 19.6x. Fitness Time is one of the few consumer names that are aligned well with Vision 2030. Moreover, we believe it is the best positioned player in the fitness industry to benefit from growth in the female fitness centres segment.

Summary Financials

SAR mn	2017a	2018f	2019f	2020f	2021f	2022f	2023f	CAGR (%)
Revenues	733	796	895	1,020	1,160	1,296	1,432	11.8%
Gross Income	279	300	331	385	449	507	569	12.6%
Gross margin (%)	38.0%	37.8%	37.0%	37.8%	38.7%	39.1%	39.7%	
Operating Income	189	202	220	258	305	346	390	12.9%
Operating margin (%)	25.7%	25.4%	24.6%	25.3%	26.3%	26.7%	27.2%	
Net Income	174	187	193	229	282	332	383	14.0%
Net margin (%)	23.8%	23.5%	21.6%	22.5%	24.3%	25.6%	26.7%	
EPS (SAR)	3.33	3.57	3.69	4.38	5.38	6.33	7.31	14.0%

Source: Company, NCBC Research estimates

STOCK DETAILS

52-week range H/L (SAR)	55.8/42.5
Market cap (\$mn)	2,923
Shares outstanding (mn)	52.4
Listed on exchanges	TADAWUL

Price perform (%)	1M	3M	12M
Absolute	9.8	11.4	NA
Rel. to market	8.8	9.9	NA

Avg daily turnover (mn)	SAR	US\$
1M	17.4	4.6
3M	16.3	4.3

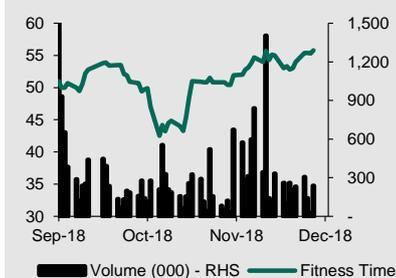
Reuters code	1830.SE
Bloomberg code	LEEJAM AB
	www.leejam.com.sa

VALUATION MULTIPLES

	17a	18f	19f
Reported PE (x)	16.8	15.6	15.1
PBV (x)	4.6	4.1	3.6
EV/EBITDA (x)	11.6	10.7	9.6
Div Yield (%)	3.2	3.4	3.5

Source: NCBC Research estimates

SHARE PRICE PERFORMANCE



Source: Tadawul

RELATIVE PERFORMANCE

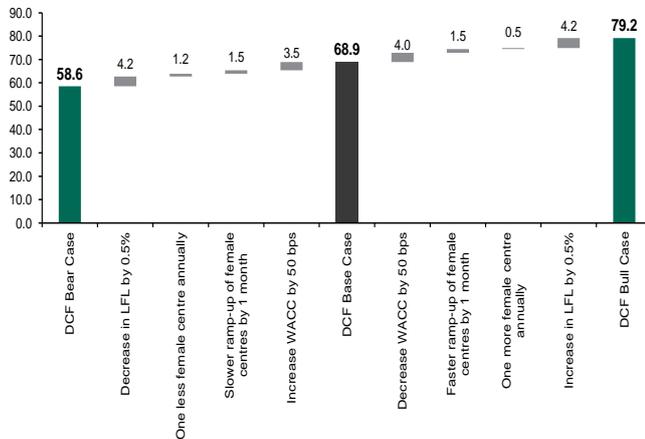


Source: Tadawul

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Investment View and Scenario Analysis

Scenario analysis on DCF valuation

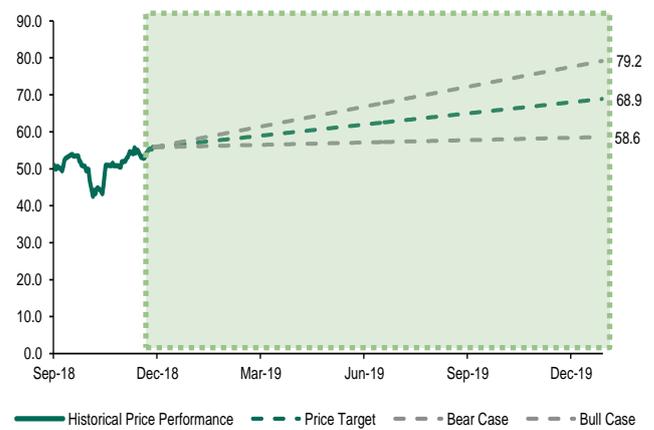


Source: NCBC Research

Investment view

- Unique investment proposition:** Fitness Time is the first listed company in the fitness segment. In addition to the positives listed above, Fitness Time has a unique proposition as it is one of the few companies that may be considered a proxy for the structural social changes under Vision 2030 and also capitalizes on the increasing disposable income of women due to their higher participation in the workforce.
- Attractive valuations:** Fitness Time trades at a 2019f PE of 15.1x, which is a steep discount to the local and international peer average of 19.6x. Moreover, the company trades at a discounted EV/EBITDA of 9.6x vs peers at 11.3x and a PB of 3.6x vs peers at 5.0x.
- Leveraging on its dominant market share:** Fitness Time is the market leader both in terms of member and fitness centre count in Saudi, with a wide gap over its competitors. With favourable regulations and demographics, the industry is expected to continue growing and we believe Fitness Time will be a key beneficiary of this growth.
- Female fitness centres to drive growth:** The licensing of female fitness centres and the rapid growth that followed in the member count reflects the growth potential in this segment. Fitness Time is capitalizing on this through aggressive expansion plans across Saudi, with minimal discounts offered on membership prices for women.
- Broad range of membership tiers mitigates concentration risk:** Fitness Time's offering across a range of affordable to premium segments reduces concentration risk.
- Strategically located branches provide convenience:** Fitness Time's presence in 23 cities in Saudi is the highest among its competitors. The majority of branches are in the major cities of Riyadh and Jeddah, due to the population concentration. The broad geographic reach provides members flexibility to visit its fitness centres across Saudi.

Historical and expected price performance



Source: NCBC Research

Investment scenarios

Price target: Weighting of DCF base case is 70%, PE is 15% and EV/EBITDA is 15%. PE is calculated using 2019f EPS of SAR3.7.
SAR68.9

DCF bull case: SAR79.2 Strong LFL growth, along with a faster than expected growth in the female fitness centre count and quick ramp-up of new centres are key growth catalysts leading to a 12.8% CAGR in sales and 16.4% CAGR in net profit.

DCF base case: SAR68.9 Aggressive expansions in the women fitness centre segment is expected to support a top-line growth of 11.8% CAGR between 2017-2023f. Despite the higher opex cost base due to the expat levy and higher cost employees in the ladies' Fitness Centres. This led to a contraction in gross margin, from 38.0% in 2017 to 37.8% in 2018f. We expect efficiencies to lead to an expansion in gross margins to 39.7% by 2023f.

DCF bear case: SAR58.6 Slower expansion and slower ramp up in operations of the female centres will translate into a revenue growth of 10.8% CAGR between 2017-2023f, with net income growing at a CAGR of 11.5% during the period.

Potential catalysts

- **Economic recovery revives male membership growth:** An economic recovery, led by higher oil prices and government spending, could lead to a revival in male membership growth. This would be specifically visible at Fitness Time's male Pro segment, due to the price sensitive nature of members in this segment. This will help the recovery of the decline seen in the male Pro segment between 2017-2019f.
- **Consolidation in a highly fragmented fitness industry:** The highly fragmented nature of the fitness industry in Saudi (Top 5 companies have 38% of member count, 20% of centre count) results in high potential for consolidation. This will support leading players such as Fitness Time, which would leverage on its leading market share and wide geographic presence.

Investment risks

- **Intense competition impacting margins:** The current intense competition in the fitness market may increase further driven by the potential growth prospects of the female fitness market. This is particularly true given the low barriers to entry of the industry for local players, despite barriers deemed to be higher for foreign entrants due to various reasons related to localisation aspects and know-how in operating such businesses in Saudi. Moreover, more aggressive expansion from local competitors or a higher presence of international fitness brands may lead to pressure on the top-line and margins of Fitness Time.
 - **Membership prices of female fitness centres:** Female members are currently being charged full price for their membership in comparison to discounts offered to their male counterparts. This is due to limited supply. Fitness Time currently offers minimal or no discounts for female membership packages. However, if higher than expected growth happens in the number of female fitness centres, this may impact the pricing and ramp-up period of newly opened female fitness centres by Fitness Time.
 - **Opex costs due to expats and hiring of ladies:** A faster than expected growth in number of centres will lead to further short-term pressure on margins, as a result of the increase in staff costs from hiring female staff and paying higher expat levies on expats hired.
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