Almarai Co.

Result Flash Note 4Q-2018

ALJAZIRA CAPITAL الجزيرة للأسواق المالية

Almarai's net profit came below expectation due to non-recurring write off and higher than expected COGS. The company continues to witness sales decline, impacted by market condition, demographics changes with an increase in product promotions. Higher alfalfa cost, material cost and labor costs led to gross margin contraction by 263 bps Y/Y to 36.43% from 39.06%. The company's overall revenue will continue to be under pressure in FY19, along with weaker margins due to complete dependence on imported alfalfa and higher expat fees. We revised our recommendation to "**Neutral**" on Almarai with TP of SAR 51.00/share.

- Q4-18 net profit came below AJC and the market consensus estimates of SAR 530.8mn and SAR 523.1mn, impacted by one-time write off. Almarai posted net income of SAR 369.6mn; indicating a fall of 27.9%Y/Y and 41.7%Q/Q. The Y/Y weak performance is mainly attributed to (i) an increase in other expenses by SAR 88.7mn due to one-off provision for discontinuation of local alfalfa operation; and impairment losses of SAR 50mn. (ii) Lower contribution from dairy & juice and baker. (ii) higher GOGS, driven by higher alfalfa cost and an increase in labor costs. The deviation of Q4-18 earnings from our estimates is mainly attributed to higher than expected COGS and one time write off.
- The company reported a 0.9%Y/Y decline in revenue for Q4-18 to SAR 3,388.7mn, which came in-line with our estimate of 3,393.1mn. We believe the noticeable Y/Y sales growth in poultry business (up by 20% expected) and improved infant Nutrition sales were offset by 4.0% sales decline in its largest segment (dairy & juice, represents almost 73.0% of the total sales in 2018) due to market conditions coupled with increased promotions and discounting. Its other key segments registered mixed performance, where Bakery registered a 2.5%Y/Y decline in revenue as a result of heavy competition and an increase of sales discounting and promotions in some discretionary part of the bakery portfolio. Poultry segment is expected to post a net profit of SAR 39.0mn, as compared to SAR 13.0mn in Q4-17.
- Almarai reported a 7.5%Y/Y decline in gross profit to SAR 1,234.7mn, below AJC expectation of SAR 1,338.2mn due to higher than expected alfalfa import cost, labor and depreciation costs. Accordingly, gross margin in Q4-18 contracted by 263 bps Y/Y to 36.43% from 39.06%. However, the higher COGS have been partially mitigated by enhanced production efficiencies according to the company.
- Operating profit stood at SAR 465.7mn, depicting a fall of 22.2%Y/Y and 38.3%Q/Q due to weak top line; however, the company witnessed a decline in OPEX to record SAR 642.2mn as compared to SAR 648.7mn in Q4-17; driven by strong operational efficiencies.

AJC view: We believe that the current operational improvement in poultry segment and strong recovery in infant nutrition sales has mitigated the impact on the company's overall performance during FY18. However, the company's overall revenue is likely to continue to be under pressure in FY19, given the weak consumer purchasing power, market share dynamics and the changes in demographics with continued decline in expat population. The company's largest two segments dairy & juice and bakery have been impacted the most due to the change in macroeconomic sentiments and market size. However, switching to profitability in the poultry segment, while gaining a market share in infant Nutrition are the key support for higher operating efficiency. Although the company was able to gain market shares in most categories, along with continued focus on business efficiency; margins in FY19 may be under pressure due to fully imported alfalfa and higher expat fees. We revised our recommendation to "**Neutral**" on Almarai, while maintaining our TP at SAR **51.00/share**. The company's EPS was revised down to 2.00 for FY19 from previous 2.14 EPS. Based on our estimates, Almarai trades at a forward PE of 26.30x, higher than the average PE of 25x in the last three years.

Results Summary

SARmn (unless specified)	Q4-17	Q3-18	Q4-18	Change YoY	Change QoQ	Deviation from AJC Estimates
Revenue	**3,418.7**	**3,370.8**	**3,388.7**	-0.9%	0.5%	-0.1%
Gross Profit	1,335.3	1,452.2	1,234.7	-7.5%	-15.0%	-7.7%
Gross Margin	*39.06%*	*43.08%*	*36.43%*	-	-	-
EBIT	598.51	755.1	465.9	-22.2%	-38.3%	-28.3%
Net Profit	**512.9**	**634.5**	**369.6**	-27.9%	-41.7%	-30.8%
EPS	0.51	0.63	0.37	-	-	-

Source: Company reports, Aljazira Capital

Neutral

Current Price* (SAR)	**52.60**
Target Price (SAR)	**51.00**
Upside / (Downside)*	**-3.0%**

Source: Tadawul *prices as of 20th of January 2019

Key Financials

SARmn (unless specified)	FY17	FY18	FY19E
Revenue	13,936	13,723	13,587
Growth %	-2.8%	-1.5%	-1.0%
Net Income	2,182	2,013	2,003
Growth %	1.6%	-7.7%	-0.5%
EPS	2.18	2.01	2.00

Source: Company reports, Aljazira Capital

Key Ratios

SARmn (unless specified)	FY17	FY18	FY19E
Gross Margin	40.1%	39.7%	39.8%
Net Margin	15.7%	14.7%	14.7%
P/E	24.63x	23.84x	26.30x
P/B	4.20x	3.42x	3.49x
EV/EBITDA (x)	15.49x	13.56x	14.77x
Dividend Yield	1.3%	1.5%	1.3%

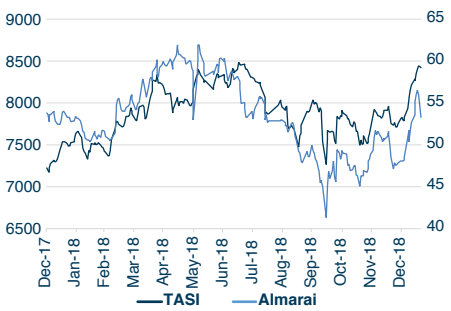
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (bn)	53.3
YTD %	16.7%
52 week (High)/(Low)	62.80/40.80
Shares Outstanding (mn)	1000.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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RATING TERMINOLOGY

1. 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.
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.

Disclaimer