

Almarai

Target Price: SAR 66.00
Upside/ (Downside): 15.6%

Recommendation

Accumulate

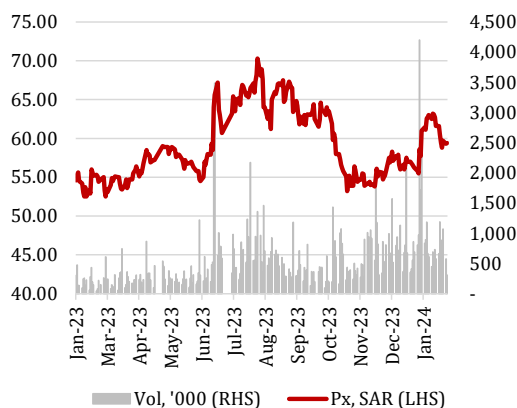
Bloomberg Ticker	ALMARAI AB
Current Market Price (SAR)	57.10
52wk High / Low (SAR)	71.000/52.400
12m Average Vol. ('000)	545.2
Mkt. Cap. (USD/SAR Mn)	15,189/57,100
Shares Outstanding (mn)	1,000.0
Free Float (%)	25%
3m Avg Daily Turnover (SAR '000)	46,910.9
6m Avg Daily Turnover (SAR '000)	39,329.8
P/E'24e (x)	24.4
EV/EBITDA'24e (x)	11.9
Dividend Yield '24e (%)	1.8%

Price Performance:

1 month (%)	1.6
3 month (%)	1.2
12 month (%)	4.6

Source: Bloomberg, valued as of 30 January 2024

Price-Volume Performance



Source: Bloomberg

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- Almarai is the market leader in each of its product categories and has held on to its position over the years, weathering competitive pressures, pandemic, commodity cost inflation, and some production issues, which indicates strong brand recognition.
- Rapid economic development in KSA, a significant increase in the poultry capacity, plans to expand the product portfolio in Qatar, launch of new products in the red meat and seafood category, are some of the catalysts for Almarai's revenue growth going forward.
- Margins are estimated to head further north, aided by continued softening in commodity costs, product/geography mix optimization, growing revenue share of higher margin segments, and cost control.

We reviewed our coverage of Almarai and raised our target price to SAR 66.00 (previously, SAR 61.00). Almarai's net income is projected to outpace its mid-single-digit revenue growth over the next five years, driven by the optimization of costs and product mix, as well as easing commodity inflation. Our target price gives 15.6% upside from the current market price and accordingly, we assign an **Accumulate** (vs. Hold, previously) rating on the stock. Currently, the stock trades at FY'24e P/E of 24.4x and EV/EBITDA of 11.9x, below its 12 months blended forward 3-year daily average P/E of 26.6x, and 3-year daily average EV/EBITDA of 14.5x.

Investment Thesis

Solid expansion plans with improved efficiency to boost earnings

i) Almarai aims to further solidify its already leading market share in select categories. Additionally, it intends to boost poultry capacity by c. 70% by FY26e, explore inorganic growth prospects, diversify in seafood and meat categories, and increase sales in Qatar.

ii) Margins are estimated to expand further in FY24 as the prices of key raw materials remain in a downtrend and the company is yet to reap the full benefit of lower-cost inventory. Net income is forecasted to outpace revenue growth on the back of operating and financial leverage.

iii) Investing heavily in expansion, Almarai has likely entered a new growth phase which could weigh on its free cash flows over the coming few years. Yet, showcasing financial prudence, the company intends to meet most of its business funding needs internally while also rewarding its shareholders with regular dividend payouts as per historical trends.

	FY21	FY22	FY23	FY24e	FY25e	FY26e
Revenues (SAR bn)	15.8	18.7	19.6	21.2	23.0	24.5
Net income (SAR bn)	1.6	1.8	2.0	2.3	2.7	3.0
Gross margin	31.9%	30.0%	30.9%	31.8%	32.0%	32.5%
Net profit margin	9.9%	9.4%	10.5%	11.0%	11.7%	12.2%
RoE	9.8%	10.7%	11.9%	12.7%	13.4%	13.8%
FCF (SAR/share)	3.5	2.7	1.6	1.0	1.0	1.5
DPS (SAR/share)	1.0	1.0	1.0	1.0	1.0	1.2
Dividend Yield	2.1%	1.9%	1.8%	1.8%	1.8%	2.0%
P/E (x)	31.2x	30.4x	27.2x	24.4x	21.3x	19.0x
EV/EBITDA (x)	14.3x	13.8x	13.1x	11.9x	10.8x	9.7x

Source: Company Reports, U Capital Research

*P/E and P/B from 2024 onwards calculated on current market price

Investment thesis

The dairy & Juice segment to remain the dominant revenue provider for the company but poultry's share is estimated to rise amid significant capacity addition

Almarai, with its leading market share, diversified products, and large sales network, stands well placed to gain from the favorable market conditions in the GCC region, which is witnessing a rapid economic and social transformation. As Saudi Arabia and several of its neighboring nations take steps to meet their respective 2030 goals, it is poised to attract hordes of temporary and permanent visitors to the region, significantly expanding the market size for the retail and consumer players.

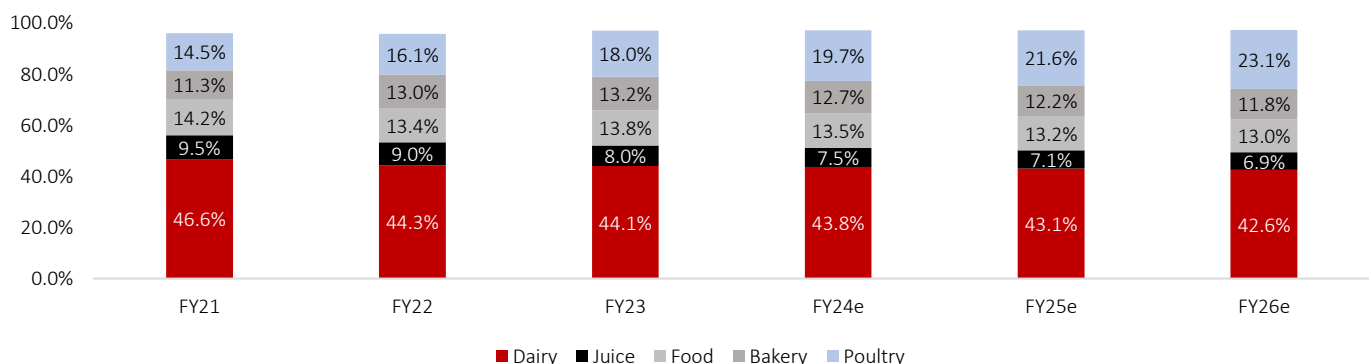
Fig. 1: Almarai has retained its market share across the product categories, indicating strong brand value (FY2023 results)

Category	Almarai Value Share %			Almarai Rank Nov-23
	Dec-21	Dec-22	Nov-23	
Dairy	51	50	48	1
Food	35	32	35	1
Juice	47	46	42	1
Bakery	55	56	54	1
Poultry (Fresh Chicken)	34	35	39	1

Source: Company FY 2023 results presentation, U Capital Research

Among Almarai's various product categories, the dairy (fresh + long-life) segment is expected to remain the major revenue provider over our forecast period, accounting for around 43%-44% of the company's total revenue, supported by its long-term vision to become the top player in the long-life dairy in the GCC region. Meanwhile, the share of the poultry segment is estimated to rise the most in the next few years, reaching ~23% in 2026 as compared to 18% in 2023, with the company working on taking the poultry segment's total capacity to 450mn birds by FY 2026 vs. about 260mn birds in FY 2023 by investing SAR 6.6bn.

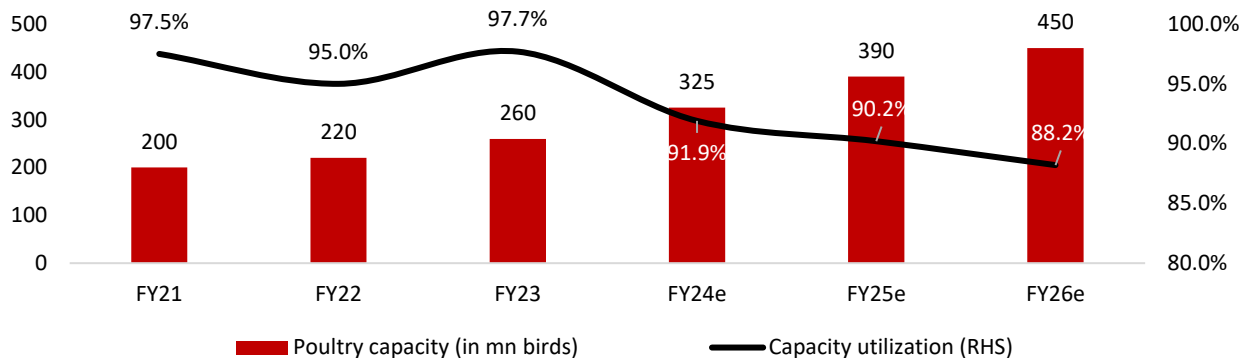
Fig. 2: Dairy (fresh + long-life) to maintain its dominant share in the revenue mix, but poultry to post a significant increase



Source: Company Reports, U Capital Research

In addition, Almarai plans to introduce more products in the seafood and red meat category this year, after they were first introduced during 2H 2023, which will provide more diversification benefits to the company. The company is also exploring inorganic growth opportunities, which currently are not included in our forecasts.

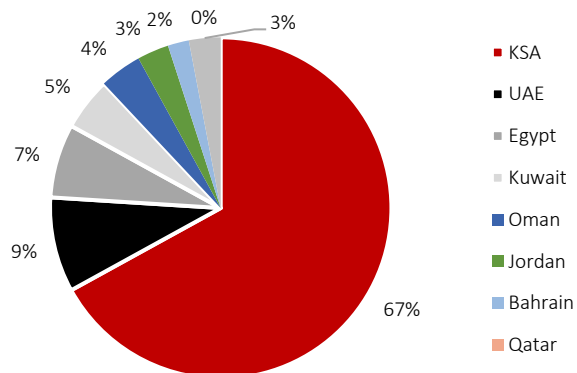
Fig. 3: Significant increase in the poultry capacity to play an important role in the company's overall revenue growth



Source: Company Reports, U Capital Research

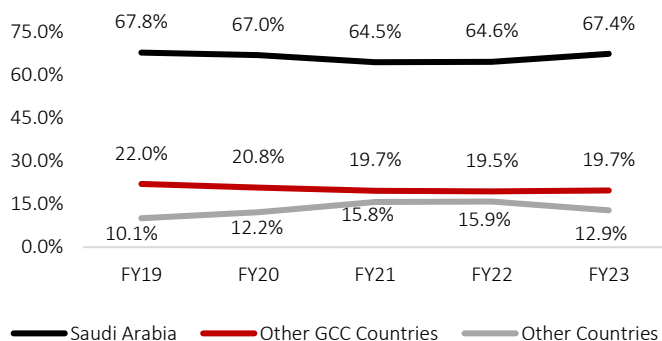
With a normalization in the production processes of the long-life dairy and fruit juice, Almarai should register a pick-up in the sales of these categories in FY 2024. We also expect other categories to sustain their rising sales trend going forward with Almarai focusing on further boosting the market share of some select products and geographies.

Fig. 4: Revenue contribution from Qatar is negligible



Source: Company Reports, U Capital Research

Fig. 5: Egypt's woes drag down other countries' revenue share



Source: Company Reports, U Capital Research

The company aims to launch more products and increase market penetration in Qatar, which currently has the least contribution to its revenue in the GCC region. Separately, Almarai's management said in their recent earnings call that the company has undertaken sufficient price increases over the past couple of years and intends to focus more on volume growth over the coming periods, which, in our opinion, could aid it in enhancing its product market share.

Overall, we estimate Almarai revenue to clock 6% CAGR during the next 5-year period (FY 2023-2028e), with weak conditions in Egypt owing to its devalued currency, and threats arising to shipping trade in the Red Sea resulting from the ongoing confrontation between Israel and Palestine casting a risk to our estimates.

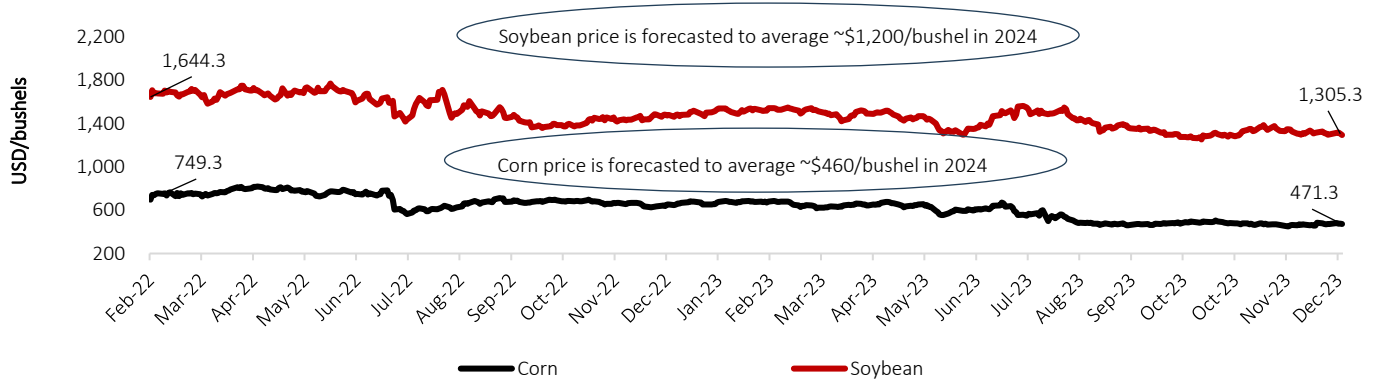
FY 2023 results overview: Almarai's top-line growth in 2023 tapered as the decent growth registered in the domestic market and other GCC countries was partly offset by a 15.4% YoY decrease in the revenue from other countries, primarily due to the devaluation of the Egyptian pound and lower Alfalfa exports from the USA. In terms of product categories, a decline in revenue of the long-life dairy and fruit juice segment constrained overall revenue growth. The decrease in the sales of the company's long-life dairy and fruit juice products was due to internal reasons as a fault in one of the machineries led to the stoppage of their production during 3Q 2023 and early 4Q 2023. This, in our opinion, partially led to a decrease in the market share of the dairy and juice segment from the end of December 2022, although the company retained its number one rank in the market in each of its product categories, which indicates Almarai

continues to enjoy strong customer associations. While Almarai's top line growth in FY 2023 slowed, operating and net profit growth accelerated backed by cost rationalization initiatives, and sales mix tilting in favor of more profitable segments.

Further expansion in margins is expected on continued softening in commodity prices, and an increase in the share of higher margin products

Almarai curbed the rise in its direct and indirect costs in FY 2023 well below the top line growth, taking advantage of the softening in the prices of its key raw materials – corn and soybean, and by implementing strict cost controls. The company also optimized its product/geography mix and benefitted from operating leverage to post a healthy improvement in its profitability. Consequently, its operating profit margin (OPM) expanded by 160 basis points (bp) to 13.8% while the net profit margin (NPM) reached 10.5%, clocking an increase of slightly over 100 bp.

Fig. 6: Prices of corn and soybean, key raw materials for the company, have been in a downtrend in FY23 and are likely to ease further slightly in FY24

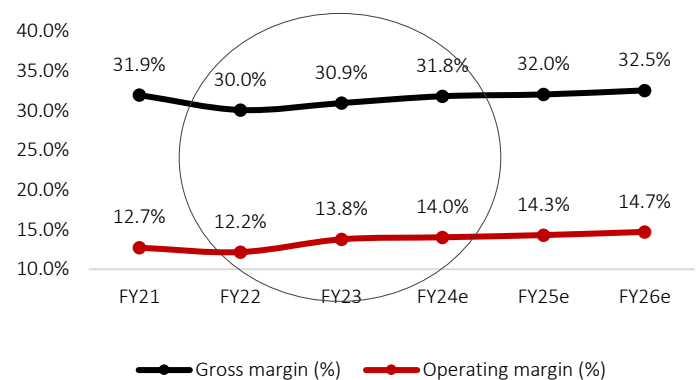


Source: Bloomberg, U Capital Research

We contend further improvements in Almarai's profitability are on the cards in FY 2024, given the forecasts of more easing in commodity prices. After declining 31% YoY and 15% YoY in 2023, the latest data from Bloomberg shows corn and soybean prices are estimated to edge lower further by about 2% YoY and 7% YoY, respectively in 2024. Another point worth noting is that Almarai said in its latest report that the full benefit of lower-cost inventory is yet to be realized, which is understandable, given the sheer size of its operations.

Fig. 7: Given the large scale of operations and inventory size, Almarai says that the full effect of lower-cost inventory will take some time to be reflected in financials, which we believe would lead to further improvements in its margins over the coming quarters

- ❖ The dairy and farming essential commodities prices have indicates stabilization; however, the benefits of the higher inventory coverage will be realized at a later stage
- ❖ The consistent implementation of strong cost control measures has significantly bolstered the operating profit.



Source: Company FY2023 results presentation, other company reports, U Capital Research

Apart from this, other factors that we believe will facilitate sustained improvement in margins are the company's focus on cost optimization, a projected rise in the share of higher-margin categories in the revenue mix like poultry, which according to Almarai is the second most profitable product segment after bakery, as well as benefits emanating from economies of scale. Thus, we estimate Almarai's OPM to average c. 14% in FY 2024 and hover in the 14%-15% range

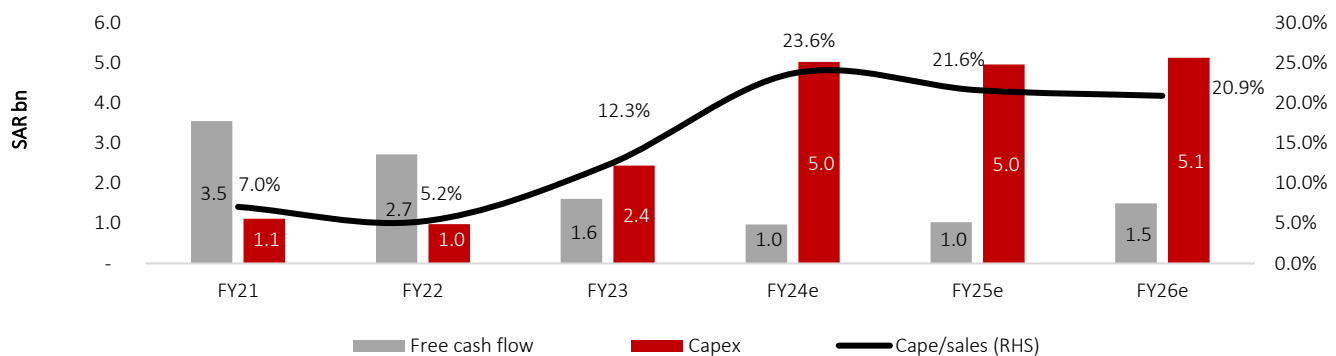
over the remaining period of our forecasts, which according to the company is its long-term range for the EBIT margin. With the rising probability of the US Fed reducing interest rates starting this year, we expect this will eventually reduce the company's interest expenses given the SAIBOR moves in tandem with the US rates owing to its currency peg.

Poultry capacity addition led increase in capex to weigh on free cash flow generation, yet internal funds will mostly suffice expansion and day-to-day business needs

Almarai's financial management has been prudent despite the company facing pressure on earnings pre-COVID (FY 2018-2019) and during the pandemic. During FY 2018-23, the company registered a 1% CAGR in its EBIT while its free cash flows (FCF) recorded a 3% CAGR during this period. Almarai has started working on increasing its poultry capacity and spent SAR 1.1bn in FY 2023, adding 40mn birds of additional capacity. Our back calculation shows that at this rate, Almarai will comfortably add another 190mn birds' worth of capacity with an intended remaining capex of SAR 5.5bn to take the total poultry capacity to 450mn by FY 2026.

We estimate this will lead to Almarai's capex more than doubling during FY 2024-26e as compared to the SAR 1.3-1.4bn capex it has been incurring over the last 3-4 years, excluding the poultry capex. With the company intending to fund most of its expansion needs through internal funds, free cash flows (FCF) are estimated to decrease significantly as compared to the trend of the past 3-4 years. We estimate to return to historical levels once the poultry capex is included.

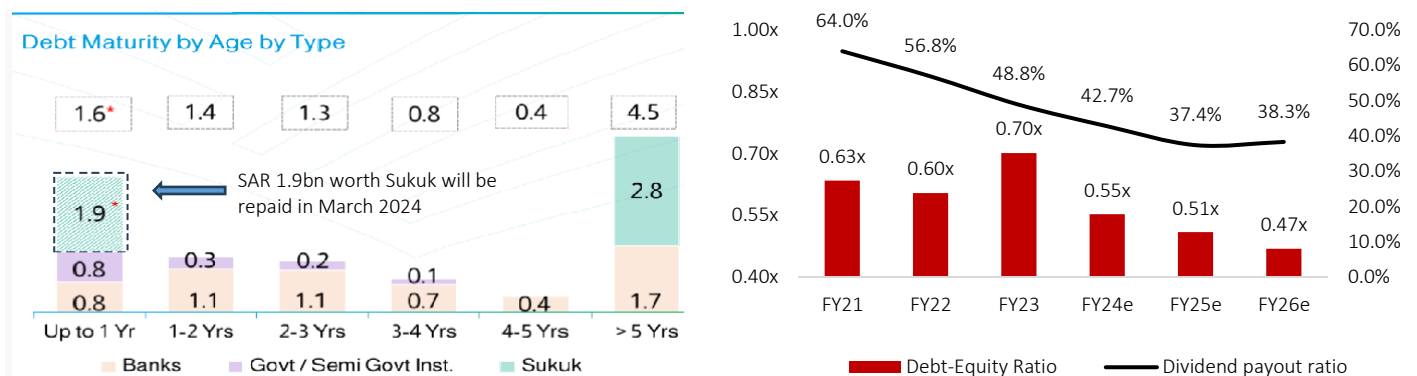
Fig. 8: Free cash flows are estimated to decrease notably amid a jump in capex for capacity expansion



Source: Company Reports, U Capital Research

Another point worth highlighting here is that while the company needs to repay Sukuk worth ~SAR 1.9bn on 05 March 2024, it has already maintained provisions for that with approximately SAR 1.9bn worth of term deposit standing on its balance sheet as at the end of December 2023. With no other major repayment scheduled during our forecast period, we contend that Almarai can also maintain its dividend per share (DPS) going forward.

Fig. 9: Debt/equity is estimated to come down with the repayment of Sukuk in 1Q24; Almarai's management is confident to fulfill their expansion and daily business needs mostly with internal cash flows, while also largely maintaining a dividend payout



Source: Company FY2023 results presentation, other company reports, U Capital Research

Valuation

Our target price is based on blended valuation methodologies – (i) DCF and (ii) Relative Valuation (using P/E and EV/EBITDA). Under DCF, we have computed free cash flow for the firm (FCFF) for our exclusive forecast period till FY 2028 and considered a 2% terminal growth rate for FCFF. These cash flows have then been discounted at the company's weighted average cost of capital (WACC) to arrive at the target price. For the relative valuation, we have taken the weighted average 12 month blended forward multiples of the regional food & beverage players as the target multiples and FY 2024e EPS and EBITDA of Almarai to compute the target price.

Almarai is likely to witness accelerated earnings growth over the next few years with the company focusing both on organic and organic expansion, supported by favorable macro factors, and improved efficiencies. Accordingly, we revised our target price for Almarai to SAR 66.00 (previously, SAR 61.00). At the current market price, our target price gives an upside of 15.6% and accordingly, we assign an **Accumulate** rating (vs. Hold, previously) on the stock. Currently, the stock trades at FY'24e P/E of 24.4x and EV/EBITDA of 11.9x, below its 12 months (12m) blended forward 3-year daily average P/E of 26.6x, and its 12m blended forward 3-year daily average EV/EBITDA of 14.5x. As compared to regional peers, Almarai is trading at a premium in terms of 12-month blended forward P/E, both considering the average of regional peers (~19x) and the average of some renowned global names in the dairy sector like Danone and Nestle (~16x). This we believe is justifiable, given the projected acceleration in the company's earnings growth, and its strong brand positioning, which is corroborated by it holding the top market share in the domestic market year over year, despite facing stiff competition from several regional and global players. Yet, in terms of 12-month blended forward EV/EBITDA, Almarai is trading almost at par with the regional average (11.8x) and slightly below the average of global peers (12.7x).

Risks

Key downside risks:

- i) The ongoing volatile geopolitical situation in the region is driving the shipping rates higher due to safety issues in the Red Sea shipping route. If the situation escalates, it can lead to an increase in the prices of final products and/or feedstock, thereby adversely affecting the company's sales and margins.
- ii) A significant increase in poultry capacity is one of the major factors behind our premise of a pickup in the company's earnings growth. However, in case the capacity addition takes longer than the estimated period, the earnings growth rate could come lower than expected.

Key upside risks:

- i) The company said in its earnings release that it is also exploring inorganic growth avenues. However, in the absence of any specific information, we have not modeled any growth coming from M&As, which exposes our estimate to upside risk in case the company fruitfully executes any such transaction.
- ii) Prices of Almarai's key commodities are forecasted to ease only slightly this year vs. last year. However, in case the prices of these commodities maintain their weakening pace, given the risks to demand from continued slowing of global growth, margins can expand at a more than expected pace.

Valuation

	Almarai
(Currency)	SAR
DCF (50% weight)	
PV of Free Cash Flows (mn)	
Year 1	915
Year 2	911
Year 3	1,247
Year 4	3,046
Year 5	2,999
Terminal Value	94,701
PV of Terminal Value	69,857
Less: Debt	(12,479)
Less: Minority interest	(11)
Less: Employee retirement benefits	(1,226)
Add: Cash & bank balances	2,592
Add: Investments	5
Equity value (mn)	67,856
Outstanding Shares (mn)	1,000.0
Assumptions	
Risk Free Rate (%)	5.0%
Adjusted Beta	0.87
Risk Premium (%)	2.8%
Cost of Equity (Ke) (%)	7.4%
WACC (%)	6.4%
Target Price	67.86
P/E based Relative Valuation (25% weight)	
Target P/E multiple (x)	24.2
EPS FY 2024e	2.34
Target Price	56.64
EV/EBITDA based Relative Valuation (25% weight)	
Target EV/EBITDA multiple (x)	14.4
EBITDA FY 2024e	5,744.2
Target Price	71.65
Weighted Average Target Price	66.00
Current Market Price	57.10
Upside/(Downside), %	15.6%
Recommendation	Accumulate

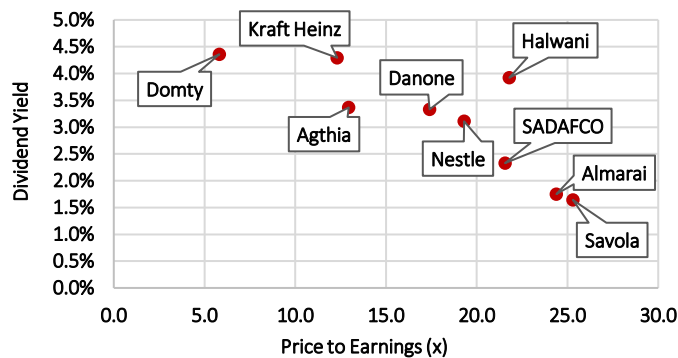
Source: Company Financials, Bloomberg, U Capital Research

Peer Group Valuation

Name	Mkt Cap (SAR mn)	Last Px (LC)	Px Change 1M, %	Px Change 3M, %	Px Change YTD, %	EV/EBITDA' 24e, (x)	P/E' 24e, (x)	ROE' 24e, (%)	Div Yield' 24e, (%)	FCF Yield TTM (%)
Food & Beverages (Regional players)										
Almarai Co.	57,100.0	57.10	2	1	2	11.9	24.4	12.7%	1.8%	2.8%
Savola	23,868.9	44.70	20	25	19	12.8	25.3	9.4%	1.6%	5.8%
Halwani Bros Co.	1,803.2	51.00	1	15	0	77.9	21.8	16.6%	3.9%	6.7%
Agthia Group	4,081.4	5.05	3	15	3	8.1	12.9	9.1%	3.4%	12.9%
Arabian Food Industries Co.	401.3	11.70	6	38	6	4.8	5.8	32.3%	4.4%	11.2%
Saudia Dairy & Foodstuff (SADAFCO)	11,297.0	347.60	4	19	4	17.2	21.6	27.4%	2.3%	4.4%
The National Agriculture Dev.	8,868.2	29.40	5	31	6	16.0	na	21.1%	na	-0.9%
Average						11.8	18.6	18.4%	2.9%	6.1%
Food & Beverages (Global players)										
Kraft Heinz Co.	171,612.7	37.31	1	18	1	10.3	12.3	7.4%	4.3%	5.5%
Danone	170,398.6	61.84	5	11	5	11.7	17.4	11.6%	3.3%	4.3%
Nestle SA	1,149,171.4	99.07	2	1	2	16.2	19.3	30.8%	3.1%	3.1%
Average						12.7	16.3	16.6%	3.6%	4.3%
Average (Regional + global)						12.1	17.9	17.8%	3.1%	5.6%
Median (Regional + global)						11.9	19.3	14.6%	3.3%	4.9%

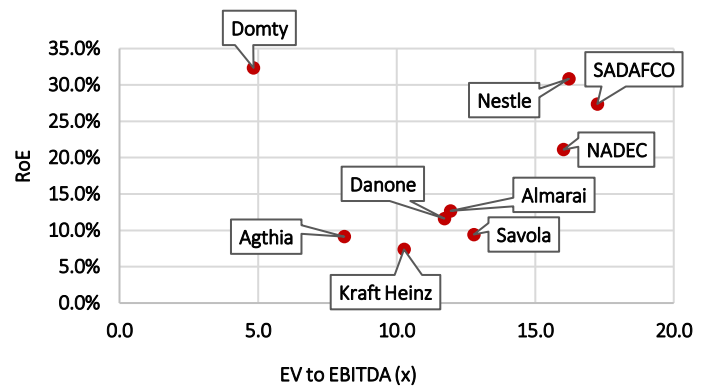
Source: Bloomberg, U Capital Research, na - not available, nm - not meaningful; *valued as of 30 January 2024, **Figures highlighted in light red are for FY 2023

Fig. 10: Food & Beverages - P/E & Dividend Yield



Source: Bloomberg, U Capital Research; As of 30 January 2024

Fig. 11: Food & Beverages - RoE & EV to EBITDA



Key financials

In SAR mn, except stated otherwise	FY21	FY22	FY23e	FY24e	FY25e	FY26e
Income Statement						
Revenues	15,850	18,722	19,576	21,217	22,974	24,538
Cost of sales	(10,790)	(13,098)	(13,524)	(14,477)	(15,623)	(16,563)
Gross profit	5,059	5,624	6,051	6,741	7,350	7,975
Selling and Distribution Expenses	(2,519)	(2,710)	(2,790)	(3,149)	(3,401)	(3,657)
General and Administration Expenses	(428)	(459)	(469)	(547)	(594)	(638)
Operating profit	2,015	2,276	2,694	2,974	3,284	3,606
Finance Cost, net	(346)	(428)	(527)	(485)	(438)	(413)
Income before zakat and income tax	1,668	1,849	2,166	2,489	2,846	3,193
Zakat	(77)	(63)	(85)	(98)	(112)	(125)
Income Tax	(11)	(8)	(29)	(34)	(38)	(43)
Net income for the period	1,579	1,778	2,052	2,358	2,696	3,024
Net income for equity shareholders	1,564	1,760	2,049	2,341	2,677	3,005
Balance Sheet						
Inventories	4,354	5,237	6,148	5,857	6,221	6,595
Trade Receivables, Prepayments and Other Receivables	1,991	2,156	2,565	2,557	2,647	2,827
Cash and Bank Balances	581	547	666	315	75	176
Property, plant and equipment	20,873	20,115	20,808	22,131	23,320	24,388
Biological Assets	1,469	1,565	1,742	2,622	3,233	3,718
Total assets	31,754	32,074	36,194	35,886	37,947	40,211
Loans and Borrowings	9,704	9,514	12,028	10,100	10,087	10,087
Trade and Other Payables	3,339	3,656	4,246	4,399	4,665	4,945
Total liabilities	15,136	15,091	18,385	16,719	17,085	17,474
Share Capital	10,000	10,000	10,000	10,000	10,000	10,000
Equity Attributable to Shareholders	16,119	16,671	17,798	19,139	20,816	22,671
Total liabilities and equity	31,754	32,074	36,194	35,886	37,947	40,211
Cash Flow Statement						
Net cash generated from operating activities	4,915	3,830	4,483	6,100	6,094	6,719
Net cash generated from investing activities	(1,814)	(1,988)	(5,180)	(3,064)	(4,911)	(5,086)
Net cash (used in) provided by financing activities	(3,024)	(1,861)	821	(3,388)	(1,424)	(1,532)
Cash and cash equivalents at the end of the period	581	547	666	315	75	176
Key Ratios						
Gross margin (%)	31.9%	30.0%	30.9%	31.8%	32.0%	32.5%
Operating margin (%)	12.7%	12.2%	13.8%	14.0%	14.3%	14.7%
Net margin (%)	9.9%	9.4%	10.5%	11.0%	11.7%	12.2%
ROA	4.9%	5.5%	6.0%	6.5%	7.3%	7.7%
ROE	9.8%	10.7%	11.9%	12.7%	13.4%	13.8%
Capex/Sales	7.0%	5.2%	12.3%	23.6%	21.6%	20.9%
Debt-Equity Ratio	0.6x	0.6x	0.7x	0.6x	0.5x	0.5x
EPS	1.6	1.8	2.0	2.3	2.7	3.0
DPS	1.0	1.0	1.0	1.0	1.0	1.2
Dividend Payout Ratio	64.0%	56.8%	48.8%	42.7%	37.4%	38.3%
Dividend Yield (%)	2.1%	1.9%	1.8%	1.8%	1.8%	2.0%
P/E (x)	31.2x	30.4x	27.2x	24.4x	21.3x	19.0x
EV/EBITDA (x)	14.3x	13.8x	13.1x	11.9x	10.8x	9.7x
Price as at period end*	48.8	53.5	55.8	57.1	57.1	57.1


Source: Company Reports; *Current market price is used for forecast periods


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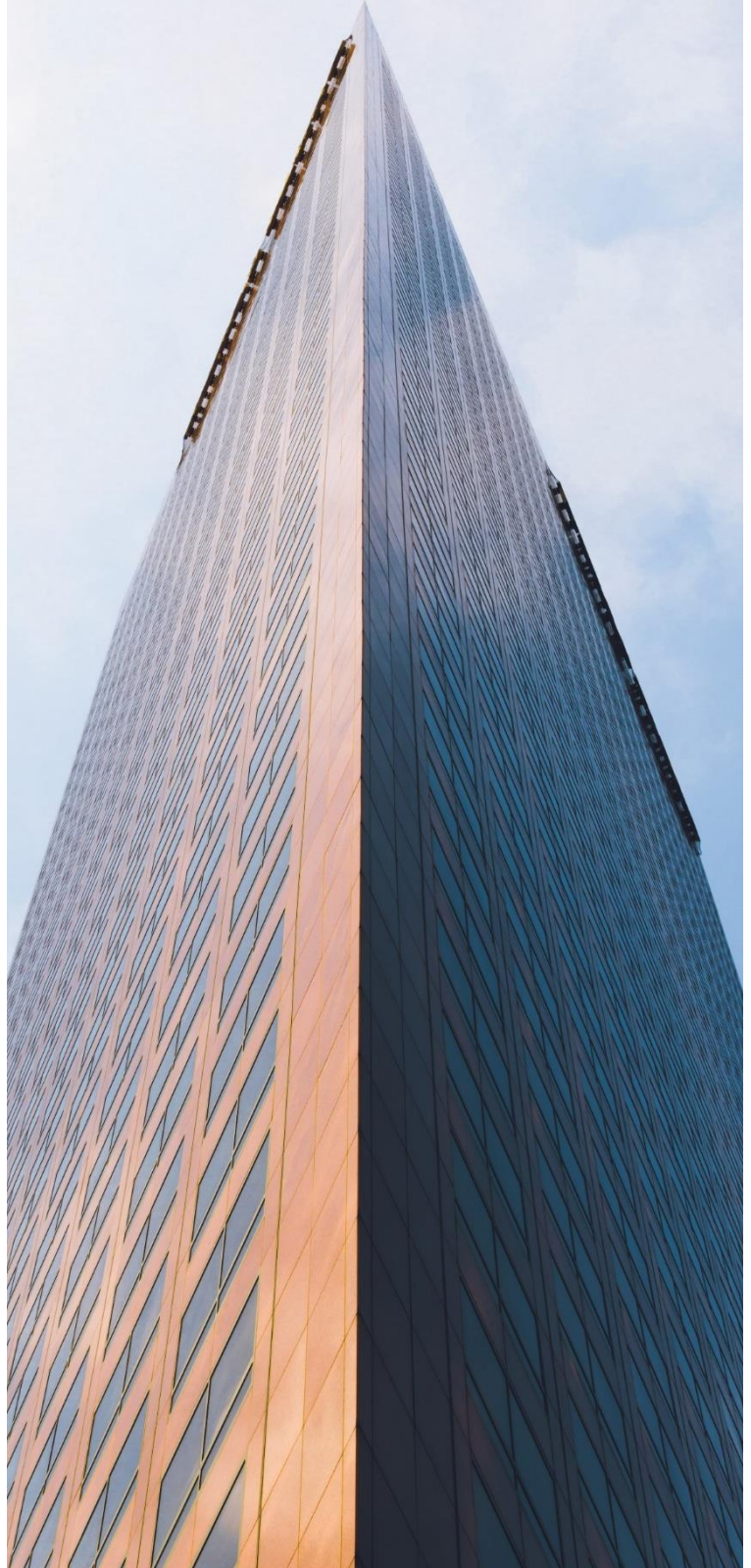
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Disclaimer

Recommendation

BUY	Greater than 20%
ACCUMULATE	Between +10% and +20%
HOLD	Between +10% and -10%
REDUCE	Between -10% and -20%
SELL	Lower than -20%

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