

Arabian (Cenomi) Centers Co.

Target Price: SAR 27.00
Upside/ (Downside): 25.6%

Recommendation

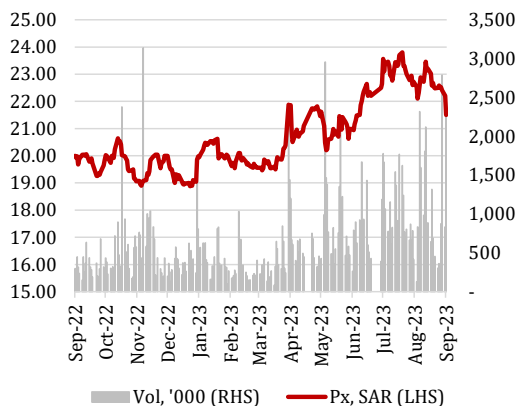
	Buy
Bloomberg Ticker	CENOMICE AB
Current Market Price (SAR)	21.50
52wk High / Low (SAR)	23.88/17.84
12m Average Vol. (000)	618.2
Mkt. Cap. (USD/OMR mn)	2,716/10,213
Shares Outstanding (mn)	475.00
Free Float (%)	33%
3m Avg Daily Turnover (SAR'000)	21,540.1
6m Avg Daily Turnover (SAR'000)	17,634.6
P/E'23e (x)	8.4
EV/EBITDA'23e (x)	10.7
Dividend Yield '23e (%)	7.5%

Price Performance:

1 month (%)	(5.4)
3 month (%)	2.5
12 month (%)	12.7

Source: Bloomberg, valued as of 04 Sep 2023

Price-Volume Performance



Source: Bloomberg

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- **Favorable industry dynamics as the Kingdom is the Gulf region's largest retail market but lags notably in per capita retail GLA.**
- **New projects are expected to push the gross leasable area (GLA) of the company by about 50% from the current levels by FY26/FY27.**
- **With a strong increase in footfalls and high tenants' occupancy at the malls, sales growth is set to accelerate vs. the historical past.**
- **Non-core asset sales will complement core cash flows, allowing ACC to meet its capex, debt servicing, and dividend payment needs.**

We review our coverage of **Arabian (Cenomi) Centres Co. (ACC)** and raise our target price slightly to SAR 27.00 (previously, SAR 25.50), indicating an upside of 25.6% from the current market price. Hence, we assign a **Buy** rating on the stock, as compared to Accumulate, previously. We remain optimistic about the company's prospects, given its robust expansion plan, and increase our margins' estimate as we contend ACC's profitability has moved to a higher trajectory, which indicates the management's strong fiscal and operational skills. Currently, the stock trades at FY'23e P/B of 0.7x and EV/EBITDA of 10.7x, below its 3-y daily average TTM P/B of c. 1.6x; TTM EV/EBITDA 14.8x.

Investment Thesis

ACC is a leading player in KSA's organized retail sector and currently operates 21 big and small malls located in 10 cities across Saudi Arabia, including the major cities Riyadh, Jeddah, Makkah, Madinah, etc. ACC is set to solidify its leading market position within KSA's retail space with new mall additions leading to healthy earnings growth.

i) Saudi Arabia is the GCC's largest retail market yet lags some of its GCC peers by a wide margin in terms of retail mall GLA per capita, which implies there remains significant market expansion potential.

ii) ACC's position in the Kingdom's retail industry will be bolstered further as the company is working to increase its retail mall GLA by c.50% from the current levels over the next 4-5 years.

iii) Led by capacity expansion, and high average occupancy amid a favorable macro environment, we estimate ACC's top-line to grow at 6% CAGR during FY22-27e (FY17-22: -1% revenue CAGR, hit by the COVID pandemic),

iv) We lift our gross margin estimates by ~9-10 pp on average over our forecast period considering the recent margin trends, as the company takes steps to optimize operations and achieve better productivity.

v) We expect ACC to maintain a healthy dividend payout, driven by improved profitability on average, offering an attractive yield in the range of 6-7%.

Year	FY20	FY21	FY22	FY23e	FY24e	FY25e
Revenues (SAR mn)	2,197.3	1,856.4	2,037.5	2,271.3	2,413.0	2,639.6
Net income (SAR mn)	633.9	486.7	775.4	1,213.5	1,121.8	1,225.0
Gross margin	65.5%	55.1%	82.4%	81.9%	82.0%	82.0%
Net profit margin	28.9%	26.2%	38.1%	53.4%	46.5%	46.4%
RoE	11.5%	8.1%	13.1%	8.0%	7.6%	8.1%
FCF (SAR/share)	2.0	1.8	3.1	0.9	2.1	2.0
DPS (SAR/share)	1.4	1.3	1.5	1.6	1.4	1.6
Dividend Yield	6.6%	5.6%	6.8%	7.5%	6.5%	7.4%
P/E (x)	15.7x	21.8x	13.5x	8.4x	9.1x	8.3x
P/BV (x)	1.7x	1.8x	1.8x	0.7x	0.7x	0.7x

Source: Company Reports, U Capital Research *Dividend Yield, P/E, and P/Book from FY23 onwards are calculated on current price

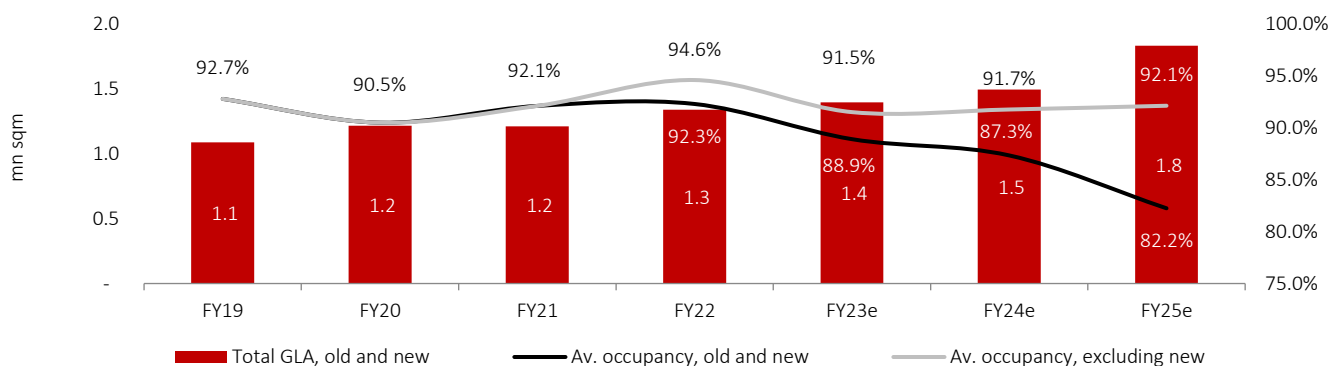
Investment thesis

ACC to boost its mall GLA by around 50% from the current levels over the next 4-5 years

ACC is a leading player in the Kingdom's organized retail sector and currently operates 21 big and small malls located in 10 cities across Saudi Arabia, including the major cities Riyadh, Jeddah, Makkah, Madinah, etc. ACC's current vast portfolio of malls is the result of several years of investment, starting from 2002. The company remains on an expansion spree and is currently developing seven new projects that are expected to start operation during FY 2023-2026. This will boost its total mall GLA by circa 50% to around 1.9mn square meters (sqm) as compared to slightly over 1.3mn sqm at present.

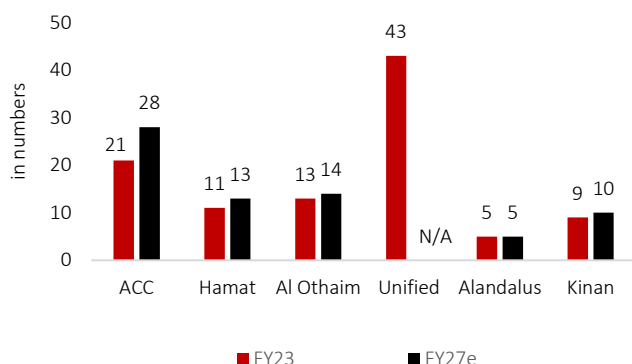
Of the new malls, two are expected to open during FY 2023. According to ACC, the construction of U Walk Jeddah is 100% complete and the mall has achieved 80% pre-lease levels. Hence, we expect it to start operations by its scheduled time in December 2023. However, we have deferred Jubail Marina Mall's opening to FY 2024 since there is little clarity on the current status of the project.

Fig. 1: Total mall GLA is estimated to climb by between 35% and 40% by FY 2025e



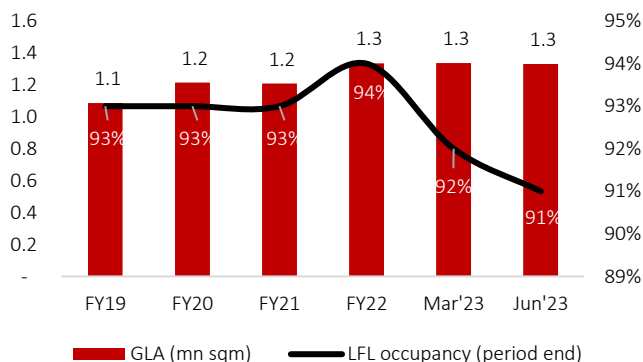
Source: Company Reports, U Capital Research

Fig. 2: ACC is seen to add most assets vs. peers in the future



Source: Company Reports, U Capital Research

Fig. 3: Period-end occupancy eases slightly but stays over 90%



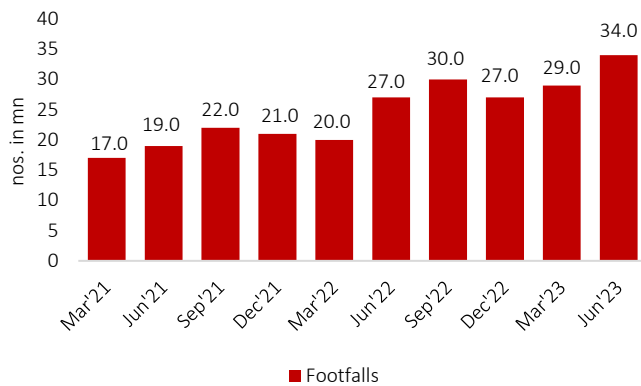
Source: Company Reports, U Capital Research

Revenue growth is estimated to accelerate driven by capacity expansion amid a favorable business environment

Despite rolling out new properties at regular intervals (four malls and one mall extension added during FY17-22 ended March), ACC registered a negative 1% CAGR in its top line during FY17-22 (March ending), as the spread of COVID-19 dragged down occupancies and the company granted significant discounts to its tenants to ease the hardships caused by the pandemic. However, post-COVID, with an improvement in occupancy, strong traction in footfalls, and the disappearance of COVID-related discounts, ACC has posted healthy revenue growth on average. During 1H 2023 ended Jun'23, the company recorded a 33.5% YoY surge in the footfalls at its malls and expects the annual footfalls to exceed

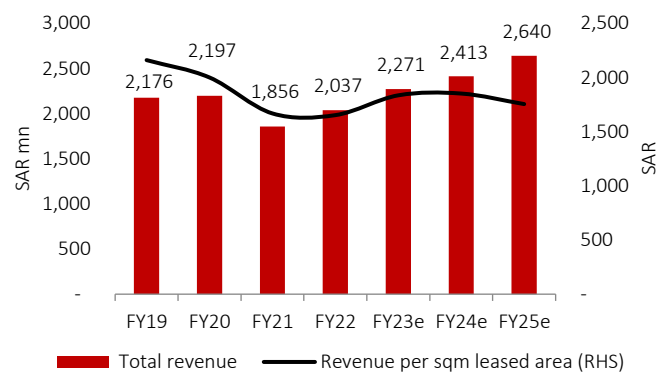
pre-pandemic levels, which suggests a conducive operating environment. Thus, supported by new capacity additions, we estimate overall revenue to clock a decent 6% CAGR during FY22-27 (ending December).

Fig. 4: Footfalls are growing strongly



Source: Company Reports, U Capital Research

Fig. 5: Revenue likely to grow at ~6% CAGR during FY22-25e



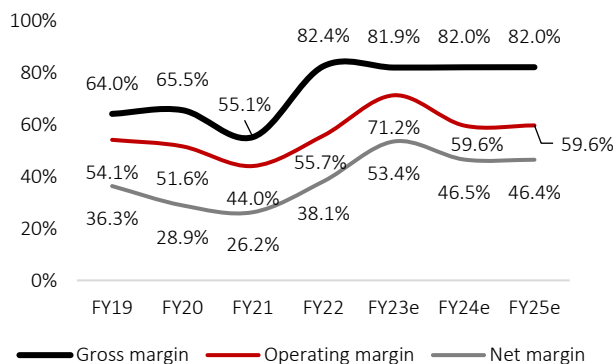
Source: Company Reports, U Capital Research

New projects might weigh on profitability, but the margins are still expected to stay above the pre-pandemic level

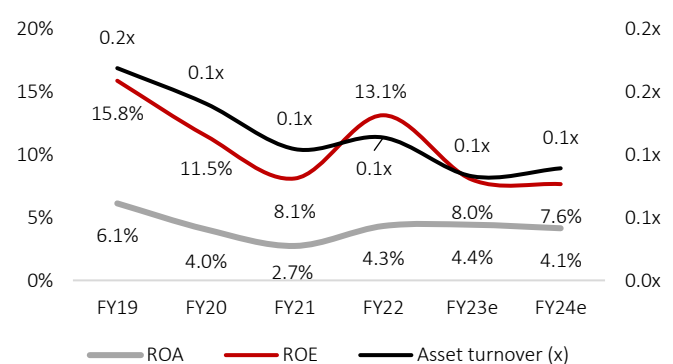
ACC's margins shifted to a higher trajectory, surpassing the pre-pandemic levels, which we believe partly resulted from the company changing the accounting of its investment properties from book value-based to fair value-based since the quarter ended Dec'22, which led to the removal of related depreciation from the income statement. Going forward, we expect margins to remain at these elevated levels, driven by healthy top-line growth, and supported by various steps taken or planned by the company like restructuring organizational structure, achieving a more optimum category mix by not renewing leases of underperforming tenants, automation of mall operations to gain higher efficiency, etc.

However, margins might ease occasionally upon the launch of new projects since some time would be required for the mall to reach its optimum operating level.

Fig. 6: Margins have transcended into a higher trajectory post a change in the valuation methodology of investment properties



Source: Company Reports, U Capital Research



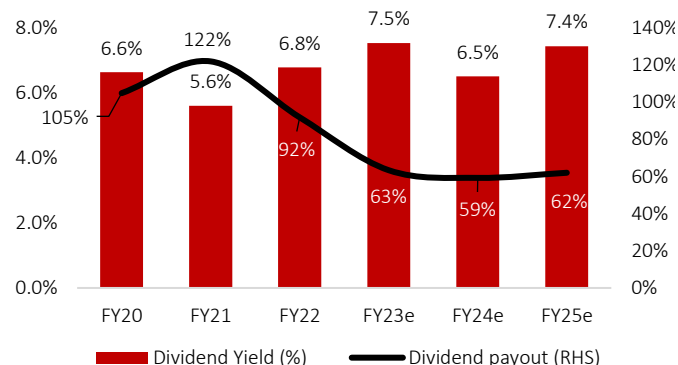
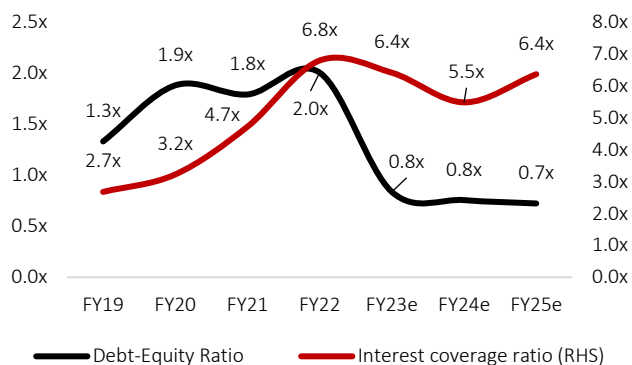
Source: Company Reports, U Capital Research

Non-core asset sale to aid in keeping the leverage ratio stable, while allowing the company to fulfill its minimum 60% dividend payout promise

ACC has been generating consistent positive cash flows over the past several years. However, the sustained addition of new commercial properties has also led to a sharp rise in their debt/equity (D/E) ratio, though a significant increase in retained earnings emanating from the adoption of fair value valuation methodology brought D/E down notably to 0.7x at the end of Dec'22 from 1.9x at the end of Sep'22. We expect the D/E ratio to keep hovering at 0.7x-0.8x during our forecast period, assuming the company will refinance its two large Sukuk repayments amounting to ~SAR 1.9bn and ~SAR 3.3bn

due in FY 2024 and FY 2026, respectively. This is because the company needs to keep spending on expansion as well as maintenance capex, while also fulfilling its commitment to keep its dividend payout at a minimum of 60%. The non-core asset sale will also complement the business cash flow generation. As per the latest filings, ACC expects to generate about SAR 1.15bn in cash flows from the sale of these assets, which we have assumed to generate a margin between 10% and 15%, based on our back-of-the-envelope calculations.

Fig. 7: The D/E ratio is estimated to remain in the 0.7x-0.8x range over our forecast period; dividend payout to largely meet 60% criteria



Source: Company Reports, U Capital Research

Source: Company Reports, U Capital Research

Risks

Key downside risks:

- i) More-than-expected delay in the addition of new projects.
- ii) Less-than-expected utilization or a decline in the same resulting from any adverse shock like a sharp economic decline, sustained rise in interest rates, etc.
- iii) Profitability weakened by more than estimated partially resulting from the new projects taking above-average time to get fully ramped up.

Key upside risks:

- i) More-than-estimated addition of new projects and at a higher-than-expected utilization rate or average revenue per GLA.
- ii) Better-than-expected profitability resulting from the new projects ramping up quickly than estimated, and or the company making any new efficiency gains.

Valuation

Our target price is based on blended valuation methodologies – (i) DDM and (ii) Relative Valuation (using P/B).

We increase our target price for the company to SAR 27.00 (previously, SAR 25.50), which indicates an upside of 25.6% at the current market price. Accordingly, we rate the company **Buy** (previously, Accumulate). We are optimistic about the company's strong growth plans, with the industry dynamics in the Kingdom appearing attractive given the rising employment levels, an expanding economy, and the government's plan to make the Kingdom a major tourist hub. Currently, the stock trades at FY'23e P/B of 0.7x and EV/EBITDA of 10.7x, below its 3-year daily average TTM P/B of c. 1.6x and TTM EV/EBITDA of ~14.8x.

Valuation

	Arabian Centers
(Currency)	SAR
DCF (70% weight)	
PV of Free Cash Flows/Dividends (mn)	
Year 1	459
Year 2	962
Year 3	861
Year 4	855
Year 5	832
Terminal Value	24,994
PV of Terminal Value	20,158
Assumptions	
Risk Free Rate (%)	4.9%
Adjusted Beta	0.88
Risk Premium (%)	4.1%
Cost of Equity (Ke) (%)	8.5%
WACC (%)	6.2%
Equity value (mn)	13,678
Outstanding Shares (mn)	475.0
Target Price	28.80
P/B based Relative Valuation (30% weight)	
Target P/B multiple (x)	0.75
BVPS 2023e	30.43
Target Price	22.81
Weighted Average Target Price	27.00
<i>Current Market Price</i>	21.50
Upside/(Downside), %	25.6%
Recommendation	Buy

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'23e, (x)	P/E'23e, (x)	ROE'23e, (%)	Div Yield' 23e, (%)	FCF Yield TTM (%)
Organized Retail										
Arabian Centres Co Ltd	10,212.5	21.50	-5	2	18	10.7	8.4	8.0%	7.5%	6.4%
Alandalus Property Co	2,314.7	24.80	4	29	60	23.4	40.7	5.3%	1.0%	3.9%
Abdullah Al Othaim Markets	12,978.0	14.42	-1	5	39	16.9	26.0	32.2%	2.1%	5.6%
Emaar Development	26,552.8	6.50	1	22	47	3.1	6.6	20.6%	8.0%	41.4%
Aldar Properties	42,317.1	5.270	0	3	19	11.0	12.7	11.0%	3.0%	-7.6%
Seef Properties	704.8	0.154	-1	1	-8	7.6	10.8	4.2%	5.2%	9.7%
Mabane Co.	13,383.9	836.000	-3	12	5	16.8	17.7	11.1%	1.6%	-4.5%
Average						12.8	17.6	13.2%	4.1%	7.8%
Median						11.0	12.7	11.0%	3.0%	5.6%

Source: Bloomberg, U Capital Research, na - not available, nm - not meaningful; *valued as of 04 Sep 2023; Note - EV/EBITDA, P/E, & RoE of Alandalus, Seef, & Mabane are current, whereas for Seef and Mabane, dividend yield is also current

Fig. 8: Organized retail - Price to Earnings & Dividend Yield

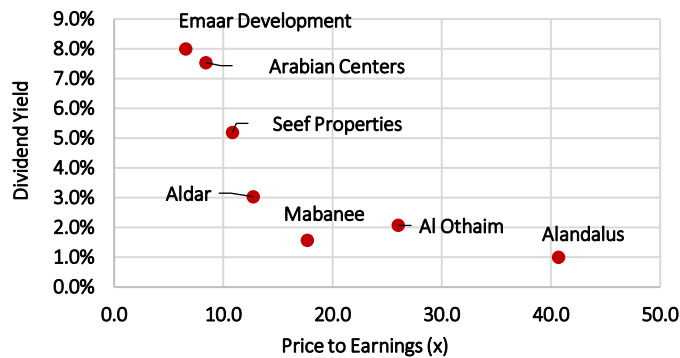
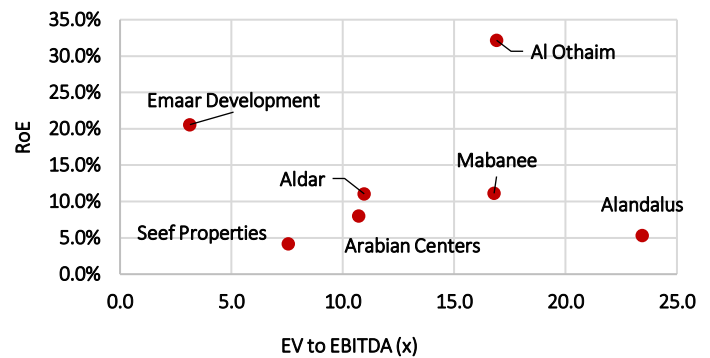


Fig. 9: Organized retail - RoE & EV to EBITDA



Source: Bloomberg, U Capital Research; As of 04 Sep 2023

Key financials

In SAR mn, except stated otherwise	FY20	FY21	FY22	FY23e	FY24e	FY25e
Income Statement						
Revenue	2,197	1,856	2,037	2,271	2,413	2,640
Cost of revenue	(759)	(833)	(359)	(412)	(435)	(475)
Gross profit	1,438	1,023	1,678	1,859	1,978	2,165
General and administrative expenses	(183)	(191)	(248)	(325)	(344)	(376)
Advertisement and promotion expenses	(13)	(20)	(25)	(33)	(35)	(38)
Other operating income	13	146	27	281	48	53
Operating profit	1,133	817	1,134	1,617	1,437	1,574
Finance costs on loans and borrowings	(351)	(173)	(167)	(252)	(262)	(247)
Finance cost on lease liabilities	(135)	(172)	(162)	(110)	(102)	(106)
Profit before zakat	663	473	790	1,260	1,165	1,272
Zakat charge	(20)	14	(40)	(43)	(40)	(43)
Profit attributable to shareholders of the company	634	487	775	1,214	1,122	1,225
Balance Sheet						
Cash and cash equivalents	1,046	636	556	837	782	872
Accounts receivable	234	248	239	348	394	431
Investment properties	11,357	11,967	12,671	24,738	24,553	24,781
Right of use assets	3,562	3,122	2,901	-	-	-
Property and equipment	91	76	73	58	59	65
Total assets	17,961	17,655	18,281	27,217	27,031	27,414
Loans and borrowings	7,016	6,981	7,791	8,972	8,157	8,002
Lease liabilities	4,237	3,861	3,804	3,121	3,121	3,121
Accounts payable and other liabilities	382	405	516	160	322	352
Total liabilities	11,977	11,602	12,501	12,711	12,065	11,979
Share capital	4,750	4,750	4,750	4,750	4,750	4,750
Retained earnings	326	320	1	8,562	9,019	9,484
Equity Attributable to Shareholders	5,983	6,051	5,782	14,453	14,910	15,375
Cash Flow Statement						
Net cash generated from operating activities	1,169	1,034	1,791	1,225	1,789	1,826
Net cash generated from investing activities	(463)	(343)	(1,077)	(479)	(103)	(574)
Net cash (used in) provided by financing activities	(118)	(1,101)	(477)	(518)	(1,742)	(1,162)
Cash and cash equivalents at the end of the period	1,046	636	872	837	782	872
Key Ratios						
Gross margin (%)	65.5%	55.1%	82.4%	81.9%	82.0%	82.0%
EBITDA margin (%)	75.9%	75.0%	84.3%	87.5%	75.0%	74.1%
Operating margin (%)	51.6%	44.0%	55.7%	71.2%	59.6%	59.6%
Net margin (%)	28.9%	26.2%	38.1%	53.4%	46.5%	46.4%
ROA	4.0%	2.7%	4.3%	4.4%	4.1%	4.5%
ROE	11.5%	8.1%	13.1%	8.0%	7.6%	8.1%
Current Ratio (x)	2.0x	1.4x	1.1x	1.1x	1.0x	1.1x
Capex/Sales	5.7%	12.7%	12.5%	49.7%	35.6%	35.8%
Debt-Equity Ratio	1.9x	1.8x	2.0x	0.8x	0.8x	0.7x
EPS	1.3	1.0	1.6	2.6	2.4	2.6
BVPS	12.6	12.7	12.2	30.4	31.4	32.4
DPS	1.4	1.3	1.5	1.6	1.4	1.6
Dividend Payout Ratio	104.9%	122.0%	91.9%	63.4%	59.3%	62.0%
Dividend Yield (%)	6.6%	5.6%	6.8%	7.5%	6.5%	7.4%
P/E (x)	15.7x	21.8x	13.5x	8.4x	9.1x	8.3x
P/BV (x)	1.7x	1.8x	1.8x	0.7x	0.7x	0.7x
EV/EBITDA (x)	12.1x	14.7x	12.4x	10.7x	11.4x	10.4x
Price as at period end*	21.1	22.3	22.1	21.5	21.5	21.5

Source: Company Reports, U Capital Research

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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