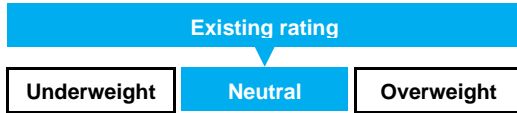




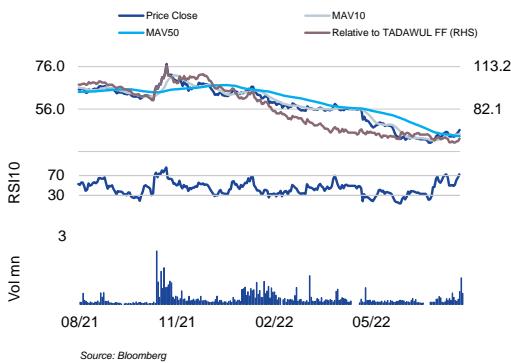
US\$0.796bn Market cap
51% Free float
US\$1.971mn Avg. daily volume

Target price **46.00** +1% over current
 Current price **45.40** as at 15/8/2022

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Performance



Earnings

Period End (SAR)	12/21A	12/22E	12/23E
Revenue (mn)	1,314	1,315	1,350
Revenue growth	22%	0%	3%
EBITDA (mn)	328	310	333
EBITDA growth	31%	-6%	7%
Net Profit	161	135	165
Net Profit Margin	12%	10%	12%
EPS	2.49	2.08	2.56
EPS growth	204%	-16%	23%
DPS	0.00	0.00	1.53
Payout Ratio	0.0%	0.0%	60.0%
ROE	15%	11%	13%

Source: Company data, Al Rajhi Capital

Herfy Foods

Earnings miss due to higher competition, maintain neutral rating

Herfy reported revenue of SAR292mn (-9.3% y-o-y), lower than our estimate of SAR348mn. The miss was mostly attributable to higher competition which resulted in lower sales across segments. The restaurant segment which is the biggest contributor to the top-line saw biggest decline in sales (-14.6% y-o-y) followed by Meat (-12.3% y-o-y) and bakery (-9.2% y-o-y). On the cost front the company experienced inflation impact which resulted in contraction in gross margin. Herfy reported a gross margin of 22.4% vs. 25.2% last year and 24% our estimate. A lower top line along with reduced margin resulted in the company reporting a gross profit of only SAR65mn (-19.1% y-o-y) considerably lower than our estimate of SAR82mn (-20% miss). However, the company was able to manage its G&A costs efficiently which came in lower and also got some relief due to higher other income which aided in posting an operating margin of 9% which was in-line with our estimates. Moreover, the lower interest expense and taxes further helped in reducing the impact on bottom-line. Consequently, the net profit margin also was in line with our estimate (7%) however, the cost saving measures could only partially offset the impact from top-line miss and as such the net profit was reported at SAR20mn, lower than our estimate of SAR26mn and 2Q'21 profit of SAR27mn.

Outlook: We see the competitive forces to continue to impact sales in the near term. Also, considering the rising trend in inflation and the supply constraints the costs of key inputs are likely to stay elevated. As such the margins at the gross level would continue to remain under pressure. However, with the higher efficiency at operating level and better cost management the company can limit the impact on bottom line to certain extent.

Figure 1 Herfy 2Q 2022 earnings summary

(SAR mn)	2Q 2022	2Q 2021	Y-o-Y	1Q 2022	Q-o-Q	ARC est	vs ARC
Revenue	292	321	-9.3%	328	-11%	348	-16%
Gross profit	65	81	-19.1%	83	-21%	82	-20%
Gross margin	22%	25%		25%		24%	
Operating profit	27	35	-22%	35	-24%	33	-17%
Operating margin	9%	11%		11%		9%	
Net profit	20	27	-24%	28	-29%	26	-22%
Net margin	7%	8%		9%		7%	

Source: Company data, Al Rajhi Capital

Valuation: We value Herfy food using equal mix given to DCF and PE based relative valuation. Our DCF target price based on 2% terminal growth and 8.6% WACC is SAR43/sh and PE based relative valuation based on 21x 12 month forward EPS of SAR2.3 is SAR49/sh. Thus, equal weighted target price stands at SAR46/sh (earlier 50/sh) which implies 1% upside from CMP of SAR45.4/sh. We maintain 'Neutral' rating on Herfy

Key Risks:

Downside risks to our valuation includes:

- 1) Steep increase in inflation of key commodities will be detrimental to margins as well as demand and can impact our valuation.
- 2) Increase in competition can impact the value proposition offered by Herfy impacting its sales and thus our valuation.



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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

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Please note that the achievement of any price target may be impeded by general market and economic trends and other external factors, or if a company's profits or operating performance exceed or fall short of our expectations.

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