United Electronics Company

Retail – Industrial
EXTRA AB: Saudi Arabia
19 July 2023

US$1.7bn	76.6%	US$16.5mn
Market Cap	Free Float	Avg. Daily Volume

Target price	95.00	16.0% above current
Current price	81.90	as at 19/07/2023

Existing rating

Underweight | Neutral | **Overweight**

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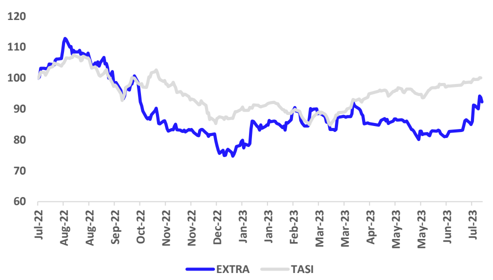
Performance (Rebased to 100)



Earnings

SARmn	FY22	FY23E	FY24E
Revenue	6,031	6,312	6,904
Revenue Growth	3.4%	4.7%	9.4%
Gross profit	1,265	1,376	1,536
Gross margin	21.0%	21.8%	22.2%
EBITDA	634	656	768
EBITDA margin	10.5%	10.4%	11.1%
Net Income	440	367	494
ROA	11.1%	8.1%	9.9%
ROE	38.6%	30.1%	34.8%
P/E	14.9x	17.9x	13.3x
EV/EBITDA	12.8x	12.4x	10.6x

Source: Company data, Al Rajhi Capital

Extra

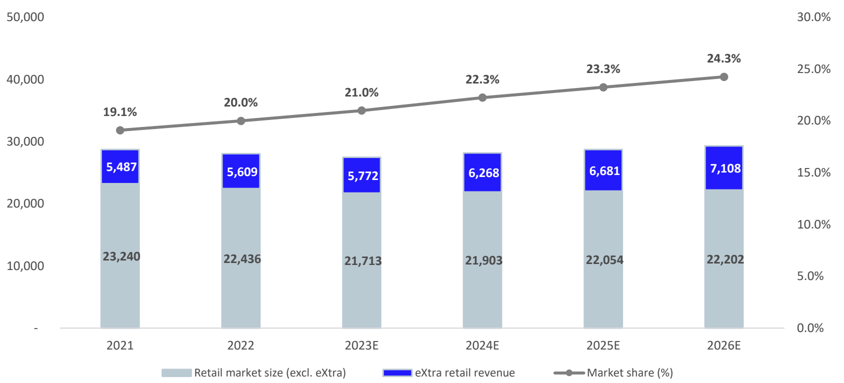
Panda to aid in market share gains, support growth. We revise TP to SAR95/sh and upgrade to overweight.

eXtra reported weak 2Q23 results due to unfavourable market conditions as inflation and the change in consumer behaviour put pressure on retailers. Sales grew by 2.3% in 2Q23 with no store additions. Despite the subdued growth in sales, gross profit grew by 6.6% to SAR342mn led by growth in the Consumer Finance segment. This reflects a gross margin of 19.7% vs 18.9% in 2Q22. However, the gains at the gross profit level were offset by higher operating expenses and higher financing costs which collectively impacted the profits of the company, in addition to provisions of the Egypt investment. We believe the higher opex relates to the expanding operations in Panda stores. Net income for the period came in at SAR62mn vs SAR127mn in 2Q22. However, adjusted net income stood at SAR100mn in 2Q23 vs SAR112mn in 2Q22. Overall, we believe the company's growth in the financing business and the expansion of the retail segment will result in higher potential growth. Thus, we revise our target price for eXtra from SAR82/sh to SAR95/sh while the current market price is SAR81.9/sh (16.0% higher).

eXtra to increase presence through Panda's stores:

In its efforts to increase its market share to 25%, eXtra entered into a strategic agreement with Panda Retail Co. (Panda) allowing the company to offer its products in Panda stores. With eXtra planning to make its products available in 66 panda hypermarkets by 1Q24, we believe the company would benefit from improved customer reach and higher visibility which could translate to market share gains. As of 2022, eXtra has a market share of 20.0% in the consumer electronics sector, while the total market size is roughly around SAR28bn. We estimate the expansion to aid market share gains of 1.0% to 1.5% for the company. Also, eXtra is focusing on increasing its share in white goods, which will contribute to achieving the targeted market share of 25%. Consequently, we expect the retail business to grow at 6.1% CAGR by 2026e. Also, we expect the retail margins to remain around the same level (GPM of 15.5% 2022-26e). Similarly, the net income margin will likely be around 4.1% during the period.

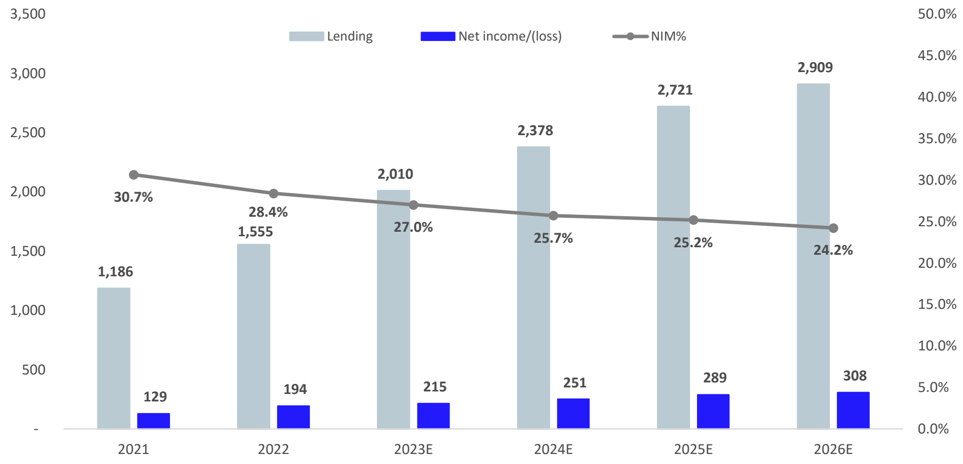
Figure:1 eXtra's Market share projections (SAR mn)



Source: Company data, Al Rajhi Capital

Consumer Finance segment: United Company for Financial Services (Tasheel), a subsidiary, witnessed a healthy growth in lending of 15.8% year to date. However, earnings growth was limited to 5.4% (SAR104mn in 1H23 vs SAR99mn 1H22) owing to cost pressure from higher SAIBOR and higher operating expenses as the business continues to expand. We expect the lending portfolio to continue growing while maintaining the required funding remains a challenge. We project the lending portfolio to grow by a CAGR of 17.0% from 2022 to 2026e supported by increasing consumer adoption of digital financing solutions. Meanwhile, earnings will witness slightly lower growth as competition is rising in the consumer finance segment, putting pressure on Tasheel's Net Interest Margins (NIMs). However, that would be somewhat offset by the possibility of an interest rate decline in the foreseeable future.

Figure 2: Tasheel lending portfolio, net profit and NIMs projections (SAR mn)



Source: Company data, Al Rajhi Capital

Also, in case Tasheel gets listed in the market, we believe that will generate around SAR900mn of cash for the company based on our valuation. Given the company's limited funding requirement, we expect to see a special dividend between SAR8/sh to SAR10/sh in such a scenario.

Dividend Policy: eXtra has been making consistent dividend payments (including the covid era) since 2017, while maintaining a gradual increase in dividends. The company paid a dividend of SAR3.9/sh in 2022. The weaker-than-expected retail segment performance in 1H23 has raised concerns about the company's capacity to pay dividends in-line with the historical trend in 2023. We expect a dividend payment of SAR3.0/sh to SAR3.5/sh. Although Tasheel has been delivering a healthy financial performance, the company will most likely reinvest the earnings to maintain the company's growth. This may further limit the company's ability to maintain dividend payments at the historical level.

Valuations: We reviewed our coverage on eXtra and upgraded our rating to Overweight with a TP of SAR95/sh. We arrived at our 12m forward-looking target price for the company using the SoTP method. The retail business was valued using a blended approach of DCF and P/E relative valuation (equal mix). The DCF target price is based on a 2.5% terminal growth and a WACC of 9.0% reaching a target price of SAR61/sh. The P/E is based on a 20x multiple and FY 2024e earnings give a TP of SAR53/sh. The blended value for eXtra's retail business came to SAR57/sh. For Tasheel, we have used the justified P/B method and came to a TP of SAR38/sh (SAR3bn value). Our justified P/B multiple is 3x reflecting the high expected growth in the lending portfolio, assuming a 26.0% sustainable ROE, 3.0% terminal growth rate, and 10.6% cost of equity based on 2024e equity value (SAR1bn).

Key upside risks to our valuations are higher sales growth than anticipated, better-than-expected improvement in gross margin, and lower-than-expected capex spending, Downside risks are lower lending growth than anticipated, lower market share gains than expected, and higher competition in the consumer electronics sector.

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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.

"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

"Target price": We estimate target value per share for every stock we cover. This is normally based on widely accepted methods appropriate to the stock or sector under consideration, e.g. DCF (discounted cash flow) or SoTP (sum of the parts) analysis.

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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