Abdullah Al Othaim Markets
Retail – Industrial
AOTHAIM AB: Saudi Arabia
1 December 2022

الراجحي المالية
Al Rajhi Capital

US$2.757bn	66.28%	US$3.244mn
Market cap	Free float	Avg. daily volume

Target price	104.0	-9.5% over current
Current price	115.0	as at 30/11/2022

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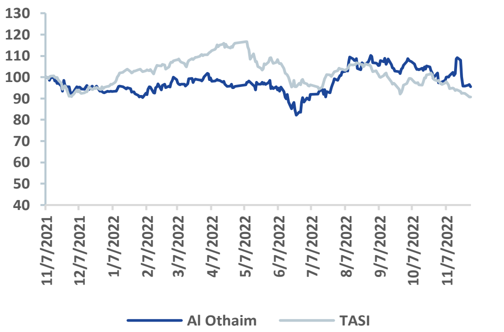
Existing rating

Underweight	Neutral	Overweight

Performance



Earnings

Period End (SAR)	2021	2022E	2023E
Revenue (mn)	8,404	9,502	10,344
Revenue Growth	-4.6%	13.1%	8.9%
Gross Profit	1,764	1,985	2,161
Gross Profit Margin	21%	21%	21%
EBITDA	685	719	815
EBITDA Margin	8.2%	7.6%	7.9%
Net Income	303	321	351
Net Income Margin	4%	3%	3%
ROE	22%	23%	26%
P/E	33.0	30.8	28.2
EV/EBITDA	13.8	13.1	11.6

Source: Company data, Al Rajhi Capital

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High OPEX to pressure earnings, we maintain our rating of Neutral with a TP of SAR104/sh

Al Othaim has seen some pressure recently from higher operating expense that raises concern over the company's earnings growth potential. Operating expense rose by a significant number (an increase of SAR169mn year to date). Moreover, another pressure faced is in the form of inflation of food prices which is impacting the food retail sector and restaurants in general. Going ahead, we expect the volumes and margins to be under pressure as consumers are becoming more sensitive to prices due to tight wallet which is mostly caused by higher inflation and the change in consumer spending habits. That being said, the lower volumes are expected to slightly hit the back margin of the Othaim in Q4. Despite the company having a strong expansion plan, we believe that it is mostly reflected in the share price of the company. We revise our value of Alothaim with a downside of around 9.5% (our TP of SAR104/sh) from the current market price of SAR115/sh.

Q3 2022 Earnings Summary:

In 3Q22 the company recorded a sales growth of 17.6% compared to 10.1% last year. The increase in revenue was largely driven by 'Back to school season' in 3Q22 vs 3Q21 when teaching was primarily remote due to the pandemic. Gross margin fell to 19.7% as compared to 20% last year mainly due to the inflation of food prices while there was an increase in absolute gross profit. We note that the company saw a change in consumer behaviour with higher focus on discounted goods. Moreover, OPEX saw a sharp increase of around SAR66.7mn which offset the increase in gross profit leading to a decline in EBIT of around SAR6mn in the 3Q22 reaching SAR50.2mn. In the same quarter, the company benefited from the sale of assets it owned in the value of SAR719.8mn (Sale of land and stake in Abdullah Alothaim Investment company) resulting in SAR744.5mn earnings for the period while the adjusted earnings came around SAR43mn (adjusting one-time income and the related tax). The company managed to maintain the level of earnings despite facing pressure from many angles.

Figure 1 Summary of Q3 2022 result

(SAR mn)	3Q 2022	3Q 2021	Y-o-Y	2Q 2022	Q-o-Q	ARC est	vs ARC
Revenue	2,348	2,001	17%	2,259	4%	2157	9%
Gross profit	463	401	15%	460	1%	453	2%
Gross margin	20%	20%		20%		21%	
Operating profit	51	57	-11%	57	-11%	54	-6%
Operating margin	2%	3%		3%		2%	
Net profit	745	45	1559%	47	1497%	44	1612%
Net margin	32%	2%		2%		2%	

Source: Company data, Al Rajhi Capital

Outlook and Valuation: We change our near-term forecast as we expect the reduction in purchasing power to impact retail sector in general. We value the company using equal mix given to DCF and PE based relative valuation. Our DCF (2.5% terminal growth, 8.8% WACC) target price is SAR115/sh and PE based relative valuation (26X FY2023 EPS) is SAR93/sh therefore equal weighted TP stands at SAR104/sh which implies ~9.5% downside from CMP of SAR115/sh. We maintain our neutral recommendation for Al Othaim.

Key downside risk to our valuation includes:

1) Delay in new store opening will have a downside risk to our valuations.

2) If the Saudization level increases then it will impact the margins adversely and poses a downside risk to our valuations.

3) If operating expenses keep increasing then it will have a negative impact on our estimate.

Key upside risks to our valuations:

1) Maintaining higher margins than our expectations.

2) Favourable and strong positioning in e-commerce.

3) Lower Capex needs than our estimate resulting in a higher FCF.

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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.

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