الراجحي المالية
alrajhi capital

US$2.13bn	65.51%	US$4.29mn
Market Cap.	Free Float	Avg. Daily Value traded

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Abdullah Al Othaim Markets Co.

Underweight on Muted Earnings Expectation

We update our investment case for Abdullah Al Othaim Markets Co. with an underweight rating and a fair value of SAR7.75/sh, having a downside of 12.7% to the last close. Our Investment case in premised on expectation of low single-digit topline growth and low probability of gross margin expansion on the back of high intensity of competition within the food retailer industry. Furthermore, we opine that changing customer shopping habits and the resultant need for more dense retail network should likely keep operating expense elevated. Hence, we expect the company's earnings to decline by 2.1% in 2025 and then remain relatively stagnant over the medium-term. We value the company using discounted cashflow method and our fair value of SAR7.75/sh implies a 2025 forward P/E of 21.5x.

Investment Thesis: Our Underweight rating on Abdullah Al Othaim Markets Co. is based on the following:

- High intensity of competition in the retail food industry on the back of both supply and demand factors. Supply is expected to increase as 1) most food retailers plan to aggressively increasing their store network, 2) discounters are gaining popularity, and 3) food delivery platforms have integrated backwards aimed at fulfilling groceries orders through their own dark stores. At the same time, growth in demand is expected to remain muted as customers become bargain hunters in the midst of increase in rents.
- The gaining popularity of discounter is a bigger threat to Al Othaim in our opinion (as compared to other food retailers) since the company positions' itself as a value player (some players such as LuLu position themselves as offering a wide assortment of SKUs aimed at targeting both local and expat population; Similarly, some players such as Danube position themselves as a premium brand and target more quality conscious customers willing to pay a higher price).
- Furthermore, changing customer shopping behavior also does not bode well for the company. Over the last few years, average basket size of customers has reduced while the number of transactions has grown. Essentially, rather than visiting the grocery store once or twice a month, customers now visit more often and make smaller purchase at each occasion. This means that commute time has now become more important than before and Al Othaim either has to increase the density of its store network (at the expense of cannibalization and higher operating expense) or risk losing out its customers to its competitors. We believe the management has chosen the lesser of the two evils, as visible by the recent aggressive store openings.
- Additionally, company can be expected to continue being impacted by the weak performance of Egypt's retail division and KSA wholesale division (both of these segments combined account for ~10% of the company's topline). The significant devaluation of Egyptian pound in the past has completely negated the impact of company increasing its selling area in the country as well as the increase in sales density (in-terms of Egyptian pound). At the same time the sales density of wholesale business has declined by 21% between 2022-24 on account of increasing intensity of competition. We believe both of these problems will persist in the medium-term and negatively impact the performance of these segments.

Underweight

Price Target (SAR): 7.75

Current : 8.88
Upside/Downside: 12.7% below current

Valuation Multiples	24A	25E	26E
P/E (x)	15.6	24.6	24.5
EV/EBITDA (x)	12.4	11.6	11.3

Major Shareholders	% Ownership
Al Othaim Holding Company	34.42%

Price Performance	1M	3M	YTD
Absolute	-9.2%	-17.0%	-15.4%
Relative to TASI	-5.2%	-10.0%	-11.3%

Earnings

(SAR Mn)	2024	2025E	2026E
Revenue	10,716	11,014	11,481
Revenue growth	4.7%	2.8%	4.2%
Gross profit	2,411	2,480	2,583
Gross margin	22.5%	22.5%	22.5%
EBITDA	860	910	949
EBITDA margin	8.0%	8.3%	8.3%
Net Income to Shareholders	511	325	327
Adj. Net Income to Shareholders	332	325	327
Adj. Net margin to Shareholders	3.1%	3.0%	2.8%
EPS	0.57	0.36	0.36
DPS	0.41	0.35	0.36
Payout ratio	72.2%	96.9%	100.0%
P/E	15.6x	24.6x	24.5x
ROE	36.0%	23.2%	23.2%

Source: Company data, Al Rajhi Capital.

2025/2026 Expectations & Assumptions: On the back of the above highlighted factors, we expect the company's adjusted earnings to decline by 2.1% YoY in 2025 and then remain relatively stagnant over the medium-term. We expect the company's topline to grow at a CAGR of 3.9% between 2025-28 driven by 4.4% CAGR of the KSA retail business (on account of 3.5% CAGR in selling area and 0.8% CAGR in sales density; the growth in selling area is expected to be lower than the 5.1% CAGR in store network on account of company's focus towards smaller format supermarkets and express stores). Egypt retail business is expected to decline by 5.6% as we expect devaluation of Egyptian pound to continue (we rely on forward exchange rates) and the management is expected to slow-down the pace of its store expansion in Egypt. Finally, we expect the company's wholesale division to remain stagnant. Other major assumptions include:

- Operating expenses are expected to remain elevated at ~19% of the topline (in-line with recent history and on account of factors mentioned above)
- Finance cost on lease liability is expected to grow by ~4% in-line with the total expansion in store selling area.
- Finally, effective tax rate is expected to be ~3% (in-line with company's history).

Recommendation and Valuation:
We value the company using a discounted cashflow method using a cost of equity of 10.5% and terminal growth rate of 2.5% to arrive at our fair value of SAR7.75/sh, having a downside of 12.7% to the last close. Hence, we have an Underweight rating on the stock.

Figure 1 **Valuation**

DCF Valuation		
DCF Valuation	SAR/sh	7.75
CMP	SAR/sh	8.88
Upside/(Downside)	**%**	**-12.7%**
Dividend yield	%	3.9%
Total returns	**%**	**-8.8%**

Source: Company Data, Al Rajhi Capital estimates

Financials

Figure 2 **Income Statement**

SAR Mn	2024	2025E	2026E
Revenue	**10,716**	**11,014**	**11,481**
y-o-y growth	*4.7%*	*2.8%*	*4.2%*
Cost of Sales	8,305	8,533	8,897
Gross Profit	**2,411**	**2,480**	**2,583**
y-o-y growth	*6.3%*	*2.9%*	*4.1%*
margins	*22.5%*	*22.5%*	*22.5%*
Operating Profit	**449**	**457**	**472**
y-o-y growth	*1.0%*	*1.7%*	*3.3%*
margins	*4.2%*	*4.1%*	*4.1%*
Net Income to Shareholders	**511**	**325**	**327**
y-o-y growth	*6.0%*	*-36.4%*	*0.5%*
margins	*4.8%*	*3.0%*	*2.8%*
EPS	0.57	0.36	0.36

Source: Company Data, Al Rajhi Capital estimates

Figure 4 **Ratios and Multiples**

	2024	2025E	2026E
ROE	36.0%	23.2%	23.2%
(Debt+Lease)/EBITDA (x)	3.2	2.9	3.0
P/E (x)	15.6	24.6	24.5
D/Y	4.6%	3.9%	4.1%
EV/EBITDA (x)	12.4	11.6	11.3

Source: Company Data, Al Rajhi Capital estimates

Figure 3 **Balance Sheet**

SAR Mn	2024	2025E	2026E
Cash & Short term investments	142	138	149
Accounts receivable, net	57	44	47
Inventories	1,226	1,096	1,219
Advance payments	191	191	191
Total current assets	**1,616**	**1,470**	**1,607**
PPE & Intangible Assets	2,097	2,176	2,289
Right of use assets	2,257	2,252	2,302
Investment in associates	303	303	303
Investment properties	644	620	594
Equity investment	8	8	8
Others	118	118	118
Total Assets	**7,043**	**6,948**	**7,221**
Accounts payable	1,982	1,973	2,072
Short-term Debt	315	150	200
Lease Liability	141	152	159
others	528	528	528
Total Current liabilities	**2,966**	**2,803**	**2,959**
Lease Liability	2,326	2,378	2,491
Others	337	337	337
Total Liabilities	**5,629**	**5,518**	**5,786**
Share Capital	900	900	900
Retained earnings	479	494	499
Reserve	36	36	36
Total shareholders' equity	**1,415**	**1,430**	**1,435**
Total Liabilities & Equity	**7,043**	**6,948**	**7,221**

Source: Company Data, Al Rajhi Capital estimates

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