

SADAFCO

Target Price: SAR 252.00
Upside/ (Downside): 18.1%

Recommendation

Hold

Bloomberg Ticker	SADAFCO AB
Current Market Price (SAR)	213.40
52wk High / Low (SAR)	239.80/155.00
12m Average Vol. (000)	29.1
Mkt. Cap. (USD/SAR Mn)	18,032/6,936
Shares Outstanding (mn)	32.5
Free Float (%)	60%
3m Avg Daily Turnover (SAR '000)	6,023.9
6m Avg Daily Turnover (SAR '000)	7,397.4
P/E'23e (x)	23.0
EV/EBITDA'23e (x)	12.7
Dividend Yield '23e (%)	2.8%

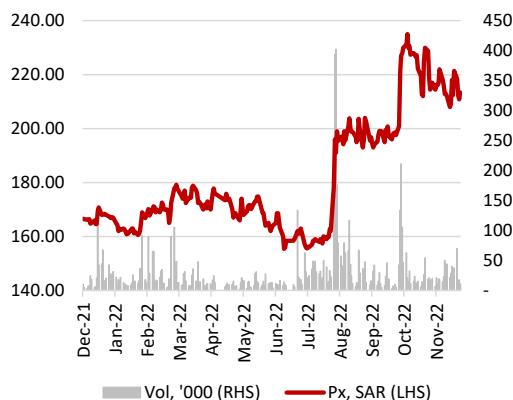
Price Performance:

1 month (%)	(0.5)
3 month (%)	5.3
12 month (%)	28.1

Source: Bloomberg

Source: Bloomberg, valued as of 21 December 2022

Price-Volume Performance



Source: Bloomberg

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- **SADAFCO has taken several initiatives recently to enhance efficiency and reach new markets which have aided the company in posting strong growth during 1H FY 2022-23**
- **Additionally, the company has also benefitted from its investment in Poland as the high commodity costs are proving to be a boon for its Polish subsidiary**
- **Sustaining its leading market share across product categories, we believe SADAFCO has become more agile and looks well set to stand strong under the current scenario which is turning gloomy. Hence, at the current market price, we assign an Accumulate rating**

SADAFCO has benefitted greatly from macro and micro factors. Launch of new and innovative products, start of the new ice cream factory during Mar'22 quarter with a capacity of 22,000 Ice Cream sandwiches per hour, the opening of new sales routes, automation of production plants, a presence in Europe (Poland), re-start of schools in physical mode, an increase in visitors, among others, has aided the company in posting solid growth during 1H FY 2022-23 (revenue: +29.7% YoY; net profit: +55.3% YoY). The company has witnessed solid growth both in different geographies and product segments, which is commendable. With the recent turnaround, improved efficiencies, and a strong balance sheet with negligible debt, we believe the company stands well placed in weathering a weakening operating environment well.

2Q FY 2022-23 earnings synopsis: SADAFCO's revenue in 2Q FY 2022-23 climbed 31% YoY, beating our estimate by 23%. All the segments posted strong top-line growth (milk and tomato paste: +28% YoY, each; ice cream: +25% YoY), driven by back-to-school initiatives, new product offerings, the opening of new sales routes, and other logistical initiatives. In terms of geographies, Saudi Arabia remained the top revenue contributor (83.8% of the total; +25% YoY), while sales of SADAFCO's Polish subsidiary Mlekoma soared 90% (9.9% revenue contribution) owing to relatively high commodity prices. Gross and operating margins expanded nearly 170 bp and over 500 bp YoY to 32.2% and 16.5%, respectively, as the sourcing of raw material from Mlekoma at competitive terms, enhancement of logistical efficiencies, and benefits accruing from Jeddah's factory automation helped. Consequently, the company's net profit expanded ~58% YoY to SAR 85.6mn (42% more than our estimate).

Valuation and risks: We continue to value SADAFCO based on blended valuation methodologies – (i) Discounted Cash Flow (DCF) and (ii) Relative Valuation (using P/E and EV/EBITDA multiples) with equal weights assigned to each of them. SADAFCO raised average milk prices by ~6% during the year ended Mar'22. Yet the company has maintained its robust market share {Milk (standalone basis): ~61% during 2Q FY 2022-23}. Market share in the other two product segments also remains firm (Tomato Paste: ~54%, and Ice Cream: ~29%). In our opinion, the current inflationary conditions in commodities will aid Mlekoma in sustaining healthy growth, and accordingly, we now expect a 31% YoY increase in revenue from Poland (earlier estimate: +7% YoY growth). Revenue from KSA is also likely to grow in the low double-digit during FY 2022-23 (previously: flattish growth). Overall, this has led to an upward revision in our FY 2022-23 EPS estimate by c. 20% and FY 2023-24 EPS estimate by c. 32%. Thus, we assign an **Accumulate** rating on the stock with a target price of SAR 252.00, implying a ~18% upside. Currently, the stock trades at 23.0x P/E and 12.7x EV/EBITDA, based on our FY 2022-23 estimates. Downside risks to our valuation include less-than-expected realization or sales quantity, a lower-than-expected contribution from Poland, and below-estimated margins. Key upside risks to our valuation include more-than-expected increase in realization or sales quantity, above-expected contribution from Poland, and above-estimated margins.

Valuation

	SADAFCO
(Currency)	SAR
DCF (33.33% weight)	
PV of Free Cash Flows (mn)	
Year 1	353
Year 2	324
Year 3	327
Year 4	324
Year 5	313
Terminal Value	9,652
PV of Terminal Value	7,434
Less: Debt	(60)
Less: Minority interest	(20)
Less: Employee retirement benefits	(132)
Add: Cash & bank balances	605
Add: Investments	-
Equity value (mn)	9,468
Outstanding Shares (mn)	32.0
Assumptions	
Risk Free Rate (%)	4.4%
Adjusted Beta	0.45
Risk Premium (%)	3.8%
Cost of Equity (Ke) (%)	6.2%
WACC (%)	6.3%
Target Price	295.86
P/E based Relative Valuation (33.33% weight)	
Target P/E multiple (x)	24.8
EPS FY 2022-23e	9.28
Target Price	230.40
EV/EBITDA based Relative Valuation (33.33% weight)	
Target EV/EBITDA multiple (x)	14.1
EBITDA FY 2022-23e	493.12
Target Price	229.74
Weighted Average Target Price	252.00
Current Market Price	213.40
Upside/(Downside), %	18.1%
Recommendation	Accumulate

Source: Company Financials, Bloomberg, U Capital Research

Key financials

In SAR mn, except stated otherwise	FY20	FY21	FY22	FY23e Prev.	FY23e	FY24e Prev.	FY24e	FY25e Prev.	FY25e
Income Statement									
Revenue – net	2,056	2,105	2,170	2,271	2,496	2,255	2,691	2,323	2,874
Cost of revenue	(1,367)	(1,412)	(1,514)	(1,544)	(1,692)	(1,518)	(1,807)	(1,536)	(1,914)
Gross profit	689	694	657	726	804	738	884	787	959
Selling and distribution expenses	(301)	(307)	(311)	(318)	(318)	(327)	(352)	(334)	(377)
General and administrative expenses	(101)	(109)	(113)	(116)	(118)	(115)	(136)	(119)	(149)
Operating profit	276	285	237	297	370	306	399	346	437
Finance income	11	6	4	7	13	8	8	9	9
Finance costs	(4)	(8)	(7)	(31)	(61)	(4)	(4)	(3)	(3)
Income before zakat and income tax	284	284	234	273	322	310	403	352	444
Zakat expense	(19)	(23)	(25)	(22)	(22)	(26)	(28)	(29)	(31)
Net income for the period	265	261	209	250	300	284	375	323	413
Non-controlling interests	1	(0)	(2)	(2)	(3)	(3)	(4)	(3)	(4)
Net income for equity shareholders	266	261	207	248	297	282	372	320	409
Balance Sheet									
Inventories	358	302	359	345	438	353	426	358	456
Trade and other receivables	216	227	242	198	213	216	258	223	276
Cash and cash equivalents	646	713	626	884	778	935	914	1,064	1,080
Property, plant and equipment	798	861	935	932	926	916	920	891	918
Right-of-use assets	72	63	65	53	54	41	46	30	38
Total assets	2,174	2,229	2,286	2,462	2,468	2,511	2,618	2,611	2,820
Trade and other payables	221	169	192	203	219	194	219	198	231
Employee benefit obligations	113	120	128	136	136	144	143	152	152
Total liabilities	698	675	725	844	805	832	804	833	816
Issued share and paid up capital	325	325	325	325	325	325	325	325	325
Statutory reserve	163	163	163	163	163	163	163	163	163
Treasury shares	(52)	(52)	(52)	(52)	(52)	(52)	(52)	(52)	(52)
Retained earnings	767	822	813	863	904	921	1,051	1,017	1,236
Non-controlling interests	20	21	21	22	21	25	24	28	28
Total liabilities and equity	2,174	2,229	2,286	2,462	2,468	2,511	2,618	2,611	2,820
Cash Flow Statement									
Net cash generated from operating activities	318	415	293	476	470	386	481	458	521
Net cash generated from investing activities	(91)	(151)	(165)	(106)	(107)	(96)	(109)	(91)	(120)
Net cash (used in) provided by financing activities	(163)	(194)	(209)	(113)	(205)	(239)	(237)	(238)	(235)
Cash and cash equivalents at the end of the period	646	713	626	884	778	935	914	1,064	1,080
Key Ratios									
Gross margin (%)	33.5%	33.0%	30.3%	32.0%	32.2%	32.7%	32.9%	33.9%	33.4%
EBITDA margin (%)	18.3%	18.5%	15.7%	18.5%	19.8%	19.1%	19.5%	20.5%	19.8%
Operating margin (%)	13.4%	13.6%	10.9%	13.1%	14.8%	13.5%	14.8%	14.9%	15.2%
Net margin (%)	12.9%	12.4%	9.6%	10.9%	11.9%	12.5%	13.8%	13.8%	14.2%
ROA	13.0%	11.8%	9.2%	10.4%	12.5%	11.3%	14.6%	12.5%	15.0%
ROE	19.1%	17.4%	13.5%	15.8%	18.7%	17.3%	21.7%	18.8%	21.7%
Current Ratio (x)	2.6x	2.7x	2.4x	2.2x	2.4x	2.3x	2.6x	2.6x	2.9x
Capex/Sales	3.8%	6.5%	7.1%	4.7%	4.3%	4.4%	4.3%	4.0%	4.4%
EPS	8.3	8.1	6.5	7.7	9.3	8.8	11.6	10.0	12.8
DPS	5.0	6.0	6.0	6.0	6.0	7.0	7.0	7.0	7.0
Dividend Payout Ratio	60.1%	73.7%	92.6%	77.4%	64.6%	79.5%	60.3%	69.9%	54.7%
Dividend Yield (%)	3.6%	3.6%	3.5%	3.0%	2.8%	3.5%	3.3%	3.5%	3.3%
P/E (x)	16.5x	20.3x	26.6x	25.9x	23.0x	22.8x	18.4x	20.1x	16.7x
EV/EBITDA (x)	10.4x	12.2x	14.9x	13.6x	12.7x	13.2x	11.6x	11.7x	10.4x
Price as at period end*	137.0	165.6	172.4	201.0	213.4	201.0	213.4	201.0	213.4

Source: Company Reports, U Capital Research

*Current market price is used for forecast periods

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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