

SAVOLA GROUP COMPANY

Food Diversified – Industrial
SAVOLA AB: Saudi Arabia
15 May 2023



US\$4.74bn Market Cap
77.14% Free Float
US\$4.6mn Avg. Daily Volume

Target price 40.00 **22% above current**
Current price 32.80 **as at 15/05/2023**

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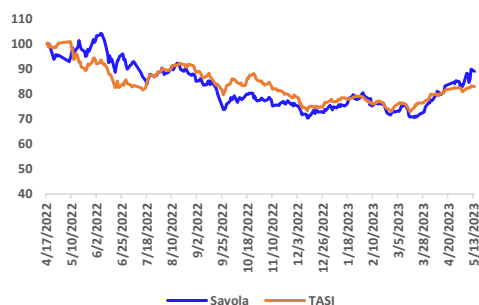
Existing rating

Underweight

Neutral

Overweight

Performance (Rebased to 100)



Earnings

Period End (SARmn)	2022	2023E	2024E
Revenue	28,055	30,061	31,189
Revenue Growth %	13.8%	7.2%	3.8%
EBITDA	2,720	3,219	3,468
EBITDA Margin %	9.7%	10.7%	11.1%
Net Profit	743	1,027	1,273
Net Profit Margin	0.9%	2.6%	3.4%
EPS	1.39	1.92	2.38
EPS Growth %	234.8%	38.3%	24.0%
DPS	0.66	1.00	1.00
Payout Ratio	47%	45%	45%
ROE	9.1%	12.1%	14.0%
P/E	23.8	17.2	13.9
P/S	0.6	0.6	0.6
EV/EBITDA	10.0	8.5	7.9

Source: Company data, Al Rajhi Capital.

Savola

Margin expansion driven by lower raw material prices, we revise our target price to SAR40/sh and maintain overweight.

Savola reported a set of strong numbers in 1Q23 as top-line grew by 4.3% mainly driven by the retail (Panda) and frozen food segments, while we were expecting lower growth of around 1.7%. Gross profit for the quarter rose sharply, as prices and volume improved, while raw material prices declined by a significant amount from the peak seen last year. Gross profit came in at SAR1,502mn with a growth of 16.9% y-o-y vs our estimate of SAR1,371mn a 6.7% growth y-o-y with an estimated gross margin of 18% vs the actual 19.2%. The deviation in gross profit came from the improvement in raw material prices. Operating expenses witnessed a growth of 2.8% y-o-y as they came in at SAR980mn vs our estimate of SAR982mn. Net income for the period came in around SAR393mn vs our estimated net income of SAR263mn. As a result of the strong recovery in earnings, we revise our target price from SAR34/sh to SAR40/sh while the current market price is SAR32.8/sh (22% upside).

Figure1: Summary of 1Q23 Results

(SAR mn)	1Q 2023	1Q 2022	Y-o-Y	4Q 2022	Q-o-Q	ARC est
Revenue	7,815	7,489	4.3%	6,605	18.3%	7,614
Gross profit	1,502	1,285	16.9%	1,192	26.0%	1,371
Gross margin	19.2%	17.2%		18.0%		18.0%
Operating profit	738	529	39.6%	249	197.1%	573
Operating margin	9.4%	7.1%		3.8%		7.5%
Net profit	393	271	45.0%	95	315.6%	265
Net margin	5.0%	3.6%		1.4%		3.5%

Source: Company data, Al Rajhi Capital

Segments analysis:

The strong bottom-line growth came mainly from the food processing segment, which has shown a growth of around 81% y-o-y to reach to SAR257mn in 1Q23 vs SAR142mn in 1Q22. Also, the frozen food segment recorded decent growth of around 13%. Losses from the retail segment (Panda) have slowed to only SAR14mn in this quarter compared to SAR35mn in 1Q22. While Herfy recorded a loss of SAR13mn in 1Q23 vs SAR28mn profits in 1Q22.

Outlook:

The improvement in the profitability of the food processing segment was driven by the recent decline in raw materials for edible oil, and we believe the improvement of the food processing segment will continue for the rest of the year. We are expecting earnings from the food processing segment to be in the range of SAR650mn to SAR700mn, up from 2022 earnings of SAR405mn. Meanwhile, Panda's losses are coming down with management guidance for net profit in 2024 and the improvement in Almrari earnings, all of which will support the performance of the company in the current year. However, what is more important is the FCF the company can generate. Although, the company FCF suffered during 2021 and 2022 mainly due to high working capital, which is driven by inflationary pressure. The change in working capital was negative for both years, by an amount of SAR701mn and SAR534mn respectively. Given the recent decline in commodity prices, especially the edible oil prices, the burden on working capital will ease, translating to a higher FCF for the period.

PANDA CXR Update:

During 2022, the company revamped around 48 stores of the CXR program which targets revamping 75 stores. The remaining is expected to be executed during the first half of 2023. In the first quarter and after three quarters of y-o-y revenue decline, the retail segment posted growth of 11%. This will help the company in reaching profitability in 2024 as targeted.

Valuations:

We arrived at our 12m forward-looking target price for the company using only DCF approach. The DCF target price is based on a 2.5% terminal growth and a WACC of 10.4% reaching to SAR40/share. Overall, we change our target price to SAR40/sh and maintain an overweight rating. Due to the great subjectivity in the SoTP method we preferred not to use it as many inputs are volatile and thus affect the valuation. Upside risks to our valuation are, better than expected improvement in earnings, lower than expected capex spending, faster than expected recovery of Panda stores. Downside risks, higher than expected depreciation of currency in the countries the company operates in.

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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.

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