

Leejam Sports Co.

Target Price: SAR 230.50
Upside/ (Downside): 23.9%

Recommendation

Buy

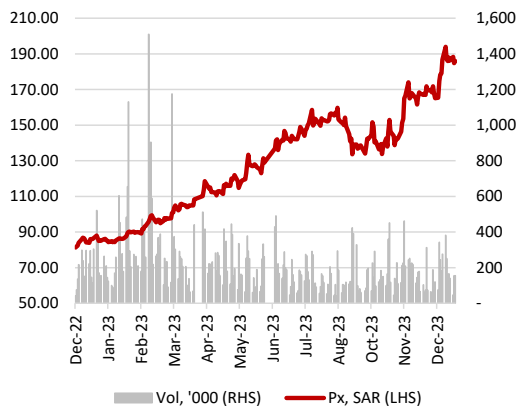
Bloomberg Ticker	LEEJAM AB
Current Market Price (SAR)	186.00
52wk High / Low (SAR)	197.80/80.00
12m Average Vol. (000)	218.0
Mkt. Cap. (USD/SAR Mn)	25,333/9,743
Shares Outstanding (mn)	52.4
Free Float (%)	48%
3m Avg Daily Turnover (SAR '000)	26,624.5
6m Avg Daily Turnover (SAR '000)	25,790.2
P/E'24e (x)	27.4
EV/EBITDA'24e (x)	14.4
Dividend Yield '24e (%)	2.0%

Price Performance:

1 month (%)	11.4
3 month (%)	35.6
12 month (%)	128.2

Source: Bloomberg, values as of 19 Dec 2023

Price-Volume Performance



Source: Bloomberg

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- **Favorable demographics, low penetration, and rising health awareness, among others, will keep the KSA gym and fitness market on a strong growth path.**
- **Leejam sustained solid growth achieved in FY22 so far in FY23 and the trend is set to continue, driven by an aggressive expansion plan.**
- **Margins in FY23 would hit their highest level since FY17, benefiting from increased utilization of existing centers and cost optimization, but could taper going forward as new centers undergo ramp-up.**
- **Accordingly, we raise our target price and rating on Leejam Sports**

We review our coverage of Leejam and raise our target price (TP) to SAR 230.50 (previously, SAR 136.00). Our TP indicates an upside of ~24% from the current market price, and hence we assign a **Buy** (previously, **Accumulate**) rating on Leejam. Currently, the stock trades at FY'24e P/E of 27.4x and EV/EBITDA of 14.4x, above its blended forward 3-year average daily P/E of 20.9x and EV/EBITDA of 11.7x. Our TP revision mainly stems from an upward revision in our earnings forecast, driven by a faster than previously estimated increase in the number of gyms and members count, based on the company's 2025 targets for the expansion of gyms and members.

Investment Summary

Focus on expansion and efficiency improvement is expected to keep the Saudi gym operator on a strong growth path:

- Leejam is expected to move to a higher growth trajectory, driven both by a likely acceleration in the overall market growth as well as rapid expansion in Fitness Time's gyms across different categories.
- Accordingly, we lift our FY24e gyms and members count to 218 and ~450k, respectively, from 187 and around 370k, previously.
- This boosts our FY22-27e top and bottom line CAGR estimates for Leejam to 11% and 12% (previously: 9% for both), respectively.
- Leejam's fixed cost model and optimization efforts will drive margins to new highs in FY'23, though they are likely to ease next year as existing gyms attain optimum utilization levels and new gyms take time to ramp up.
- Balance sheet strength is expected to improve driven by strong earnings growth, fulfilling most of Leejam's day-to-day business and expansion needs, while maintaining its dividend payout at around the current levels.

Key Indicators

	FY20	FY21	FY22	FY23e	FY24e	FY25e
Revenues (SAR mn)	662.6	885.3	1,065.8	1,297.4	1,466.6	1,636.4
Net income (SAR mn)	(58.7)	206.0	257.3	337.7	355.1	396.1
Gross margin	21.1%	42.1%	40.9%	43.6%	41.3%	40.8%
Net profit margin	-8.9%	23.3%	24.1%	26.0%	24.2%	24.2%
RoE	-8.5%	28.0%	29.5%	33.3%	30.4%	29.6%
FCF (SAR/share)	3.4	2.7	7.3	10.0	1.9	4.4
DPS (SAR/share)	-	2.1	2.7	3.5	3.7	4.2
P/E (x)	-69.0x	27.7x	NM	28.9x	27.4x	24.6x
EV/EBITDA (x)	25.8x	14.7x	9.5x	15.6x	14.4x	13.1x

Source: Company Reports, U Capital Research *P/E, P/B, and dividend yield from 2023 onwards are based on current price

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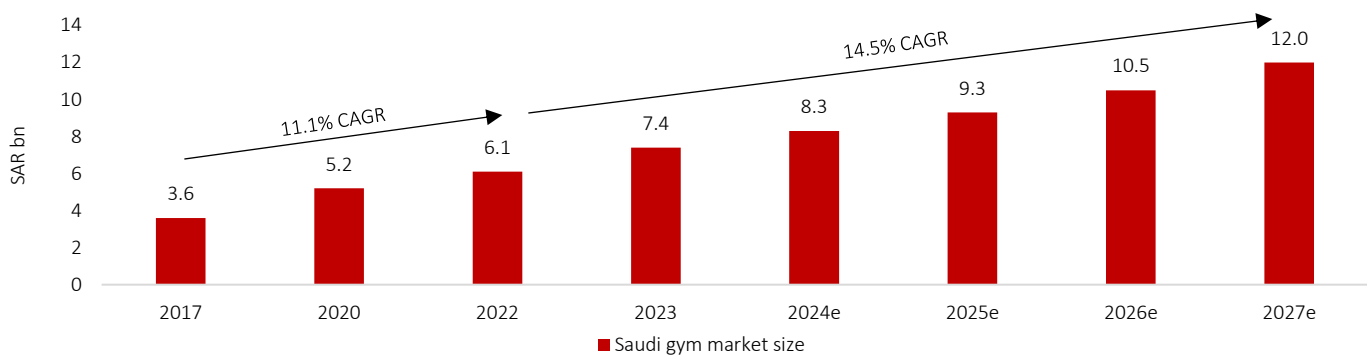
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Investment rationale

Top-line growth is expected to remain in high gear as the company continues to expand its fitness centers at a brisk pace

Saudi Arabia's health & fitness sector as part of the overall sports market is forecasted to clock a relatively higher rate of expansion over the next half a decade as compared to the past 4-5 years. The major catalysts providing the thrust for the acceleration of this growth are: i) initiatives being taken by the government to raise the physical activity level of its residents as part of its National Sport Strategy to achieve overall health & sports target of Vision 2030, ii) an underpenetrated market, iii) favorable demographics with a young and growing population, iv) rising income levels with a growing women participation in the job market, v) increasing health consciousness, particularly after the COVID, and vi) rising instances of lifestyle diseases, with the WHO ranking the Kingdom 2nd in the Middle East and 7th globally in diabetes cases, among others.

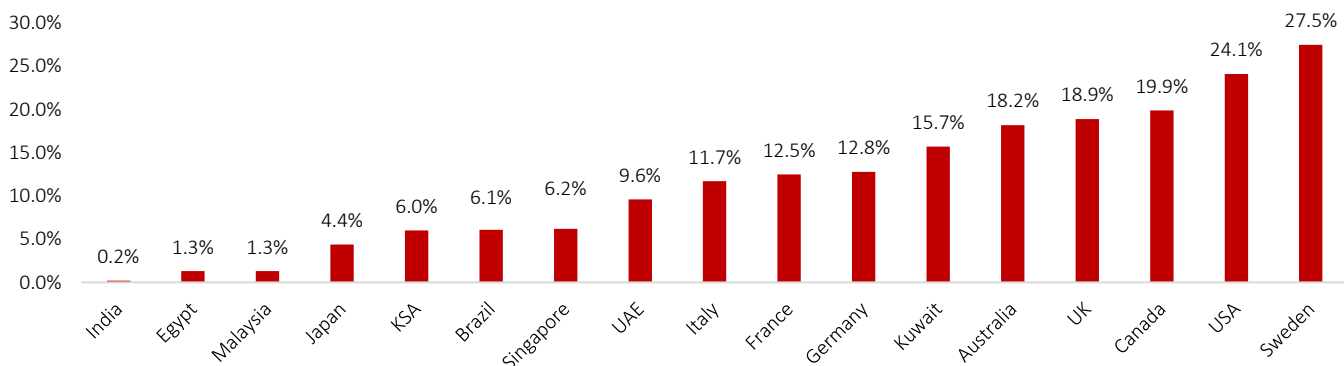
Fig. 1: Saudi Arabia's gym market is forecasted to expand at an accelerated pace over the next five years



Source: Company Reports, U Capital Research

Recognizing the healthy growth potential of the market, Leejam, which operates gyms under the "Fitness Time" brand across the country, has devised a strategy to sustain the strong growth momentum its business is currently witnessing. To achieve this, the company intends to further bolster its already dominant market position by leveraging its scale and reach, brand resonance with the public, and long-standing customer association, among others. Not only the company has formulated a strategy, but recent results indicate it is vigorously working to achieve its goals. For instance, Leejam revised its target for new center additions in FY 2023 twice, first raising it from 167-171 range to 171-176 and again to 181-191. We believe the company will achieve its current guidance comfortably, as its total fitness centers reached 180 by the end of November 2023 vs. 156 at the end of December 2022. Accordingly, we estimate Leejam's fitness centers to reach 185 by the end of this year, around the mid-point of its current guidance range, eight centers more than our earlier estimate and indicating a net addition of 29 gyms during FY 2023e (vs. 11 in 2022).

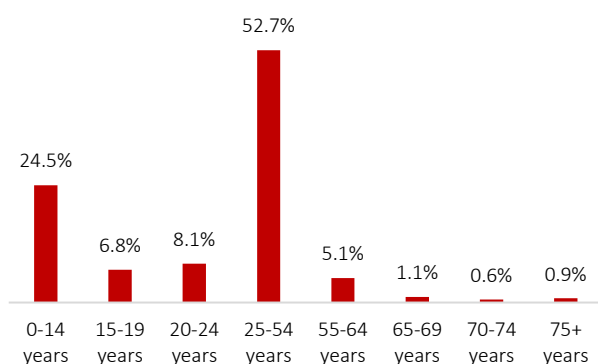
Fig. 2: Saudi Arabia lags behind some of its GCC neighbors in 'Gym Membership Penetration' rate



Source: Company Reports, U Capital Research; *based on 2022 data

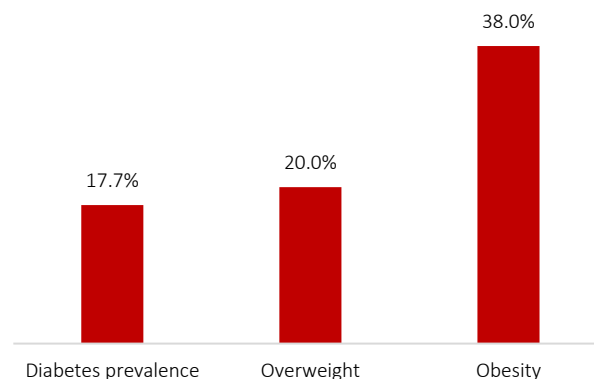
The rapid growth in Leejam's portfolio of fitness centers is being accompanied by a similar increase in active members. During 9M 2023, the company registered a 53% YoY jump in footfalls at its premises while the total number of members climbed 21.9% YoY to c. 448k by the end of September 2023. We believe this remarkable growth is spearheaded by several factors such as locational advantage and brand awareness; availability of gyms and/or packages for different categories of customers like male/female, adult/kids, and value seekers/premium clients; upgrade of existing assets by including smart gym equipment to appeal newer generations, etc. Driven by these traits, efforts to further diversify the client base by targeting government employees, students, top industry brands, and the continued addition of new gyms, we now expect the total gym members of Leejam to reach close to 400k by FY 2023-end, nearly 40k higher than our previous forecast and reflecting around 21% YoY increase, although it will be lower from 448k members registered by the company at the end of 3Q 2023. This is because the number of members in the first and fourth quarters of a year is generally lower than in the second and third quarters of a year owing to seasonality.

Fig. 3: KSA has a predominately young population, a positive for the fitness & sports sector



Source: GASTAT, U Capital Research

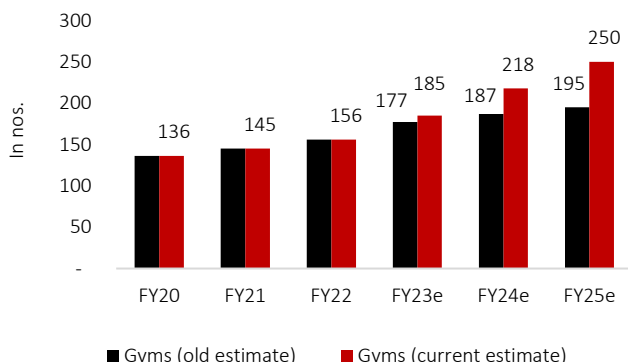
Fig. 4: The prevalence of lifestyle diseases is one of the highest in KSA, which should increase awareness about health & fitness



Source: Company Reports, U Capital Research

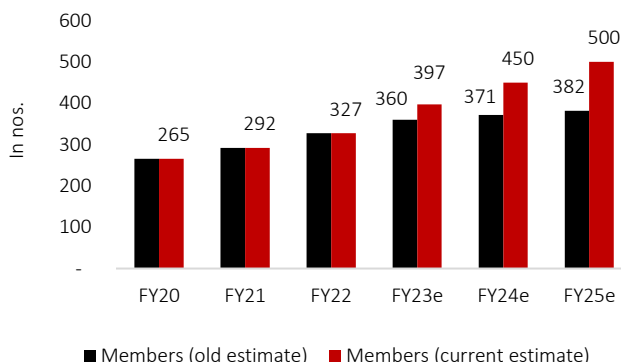
Leejam has set an ambitious growth target for the next two years, aiming to reach 250 fitness centers and 500k members by FY 2025. More than 50 locations for new Fitness Time gyms out of a pipeline of 100 gyms have already been confirmed, which gives us confidence that the company will reach the intended 250 fitness centers by 2025, indicating an estimated addition of 65 gyms over the next two years. By then, we expect Leejam to have covered the bulk of the major Saudi towns and urban centers and hence we forecast a considerable deceleration in the addition of the new fitness centers thereafter as the company moves to smaller cities. Considering the large number of gyms to be added during FY 2023e-2025e and the 6-18 months required to ramp up a gym, depending on its location, competition, etc., we expect average members per center to decline. Yet, even with a relatively lower average number of members per gym, we estimate total members to reach the targeted 500k members in FY 2025e.

Fig. 5: Leejam intends to increase its gyms significantly...



Source: Company Reports, U Capital Research

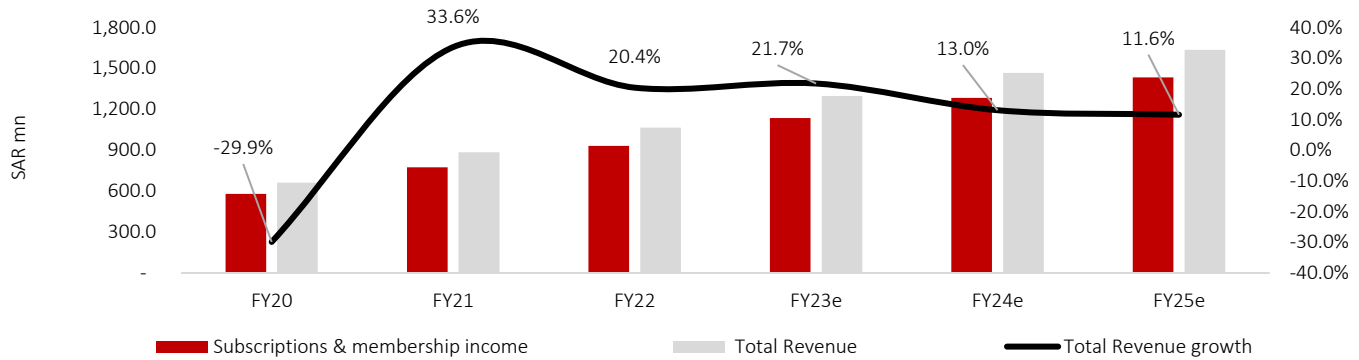
Fig. 6: ...aiming to reach 500k membership by FY 2025e



Source: Company Reports, U Capital Research

We also estimate average realization per member to remain largely flat during FY 2023-FY 2025, until the newly added fitness centers reach the normal levels. Post that we expect average realization to grow nominally, given our premise that the company would slow down expansions and could focus more on value-added activities. Incorporating these changes, we raise our FY 2024 top-line estimate by 10% and forecast FY 2022-2027e revenue CAGR at 12% (vs. 9%, previously).

Fig. 7: Subscription & membership will continue to drive the bulk of the revenue for the company

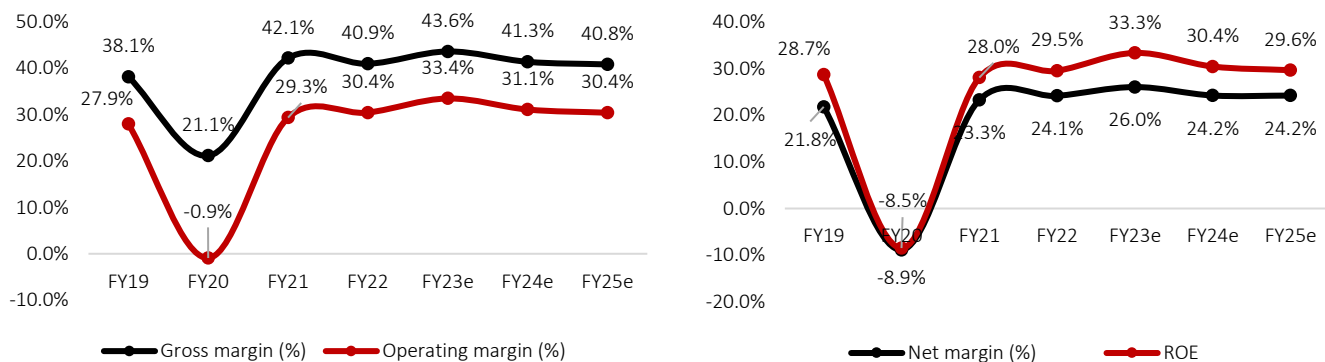


Source: Company Reports, U Capital Research

Benefitting from increased utilization, high operating leverage, and cost optimization efforts, gross and operating margins are likely to scale new heights in FY 2023e, but are estimated to taper next year onwards on ramp-up efforts of new gyms

Leejam’s business model is characterized by high operating leverage as around 70%-80% of its costs are fixed in nature. This bodes well for an expansion in profit margins with an increase in utilization. The company’s margin trends during 9M 2023 corroborate this as the gross, operating, and net margin during the first three quarters of FY 2023 improved YoY as the solid increase in members driven by the revamped strategy put in place likely enhanced utilization. However, as the existing centers reach their optimum utilization levels, we expect profitability to taper down FY 2024 onwards as the new centers will take time to get fully ramped up and reap the benefits of operating leverage, though continued digitization and optimization efforts and an expected reduction in the depreciation expenses post the refurbishment of fitness centers should support the margins.

Fig. 8: Margins are estimated to ease in FY 2024 relative to FY 2023 till new gyms reach optimum utilization rate



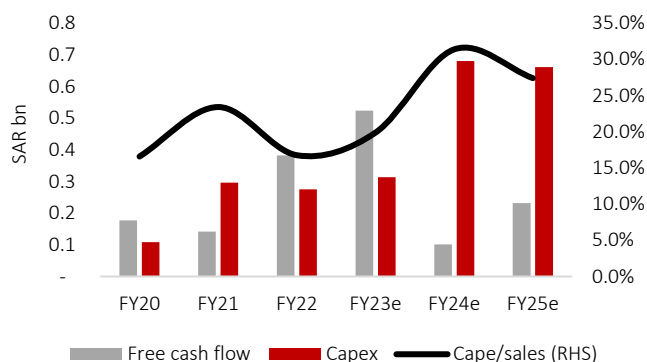
Source: Company Reports, U Capital Research

Aggressive expansion with efficient financial management boosts balance sheet strength

Leejam’s management exercised prudent financial management, as over the past five years till FY 2022, its top-line growth translated into a similar bottom-line growth. Accordingly, the company generated healthy cash flows during this period.

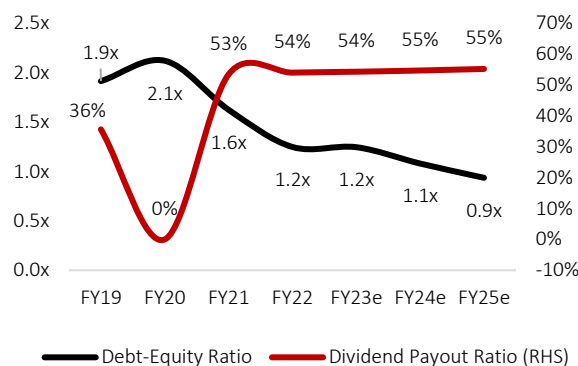
Going forward, as we estimate operating and net income (FY 2022-2027e CAGR: +12%) to outpace top-line growth (FY 2022-2027e CAGR: +11%) driven by efficiency gains and operating leverage benefits, liquidity position is expected to strengthen further supported by efficient working capital management. Thus, we believe future cash flows should largely fulfill Leejam's organic as well as inorganic growth requirements, aiding it in gradually bringing down its leverage while also aiding in maintaining its dividend payout ratio. In 3Q 2023, Leejam paid SAR 0.95 per share cash dividend, exceeding our estimate of SAR 0.70 per share, resulting in a 54.0% payout ratio, in line with its historical average. Consequently, we revise our FY 2023 dividend per share (DPS) estimate to SAR 3.50 vs. around SAR 3.10 previously, indicating 55.2% on our FY 2023 estimated profit.

Fig. 9: Continued healthy free cash flow generation likely to fulfill most of the company's capex needs



Source: Company Reports, U Capital Research

Fig. 10: Dividend payout is expected to remain steady in the 50%-55% range



Source: Company Reports, U Capital Research

Risks

Key downside risks:

- i) The company lagging behind our estimated expansion for fitness centers either due to location issues or competition.
- ii) An unexpected firming of inflation adversely impacts the cost of consumables as well as estimated capital expenditure.
- iii) Less-than-estimated profitability improvement in case of members at new or existing centers fall below the optimum level.

Key upside risks:

- i) The company adding new centers as per its plan, as our estimate is on a bit conservative side.
- ii) Sooner-than-expected ramp-up of new centers.
- iii) Higher than estimated utilization of existing portfolio of centers.
- iv) Higher than expected reduction in debt balance, a positive under the current elevated interest rate environment.

Valuation

Our target price is based on blended valuation methodologies – (i) DCF and (ii) Relative Valuation (using P/E & EV/EBITDA multiples).

We raise our TP of the company to SAR 230.50 (previously, SAR 136.00), as we believe the company is on the verge of witnessing accelerated earnings growth, propelled by a rapid expansion of its gym network as well as members. At the current stock price, our TP indicates an upside of 23.9% from the current stock price. Accordingly, we maintain our **Accumulate** rating on the stock. Currently, the stock trades at a P/E of 27.4x and EV/EBITDA of 14.4x, based on our FY 2024 estimates.

Valuation

	Leejam Sports
(Currency)	SAR
DCF (Equal weight)	
PV of Free Cash Flow (mn)	
Year 1	578
Year 2	299
Year 3	385
Year 4	572
Year 5	619
Terminal	15,842
PV of Terminal Value	11,931
Assumptions	
Risk Free Rate (%)	4.9%
Adjusted Beta	0.96
Risk Premium (%)	3.1%
Cost of Equity (COE) (%)	7.9%
WACC (%)	7.3%
Equity value (mn)	13,383
Outstanding Shares (mn)	52.4
Target Price	255.48
P/E based Relative Valuation (Equal weight)	
Target P/E multiple (x)	29.1
EPS 2024e	6.78
Target Price	197.47
EV/EBITDA based Relative Valuation (Equal weight)	
Target EV/EBITDA Multiple (x)	17.9
EBITDA FY2024e (mn)	752
Target Price	238.54
Weighted Average Target Price	230.50
<i>Current Market Price</i>	186.00
Upside/(Downside), %	23.9%
Recommendation	Buy

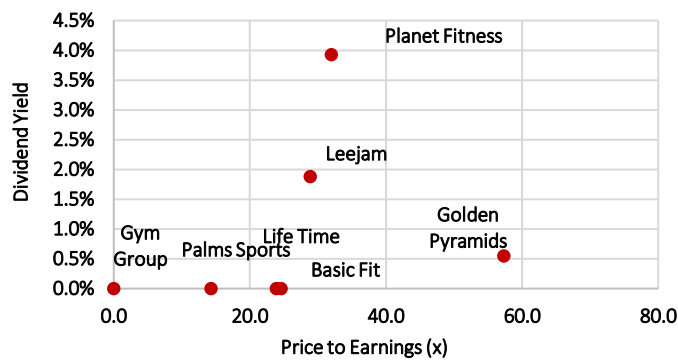
Source: Company Financials, Bloomberg, U Capital Research

Peer Group Valuation

Name	Mkt Cap (SAR mn)	Last Px (LC)	Px Change 1M, %	Px Change 3M, %	Px Change YTD, %	EV/EBITDA' 23e, (x)	P/E'23e, (x)	ROE'23e, (%)	Div Yield' 23e, (%)	FCF Yield TTM (%)
Fitness & sports										
Leejam Sports Co.	9,743.3	186.00	11	36	121	15.6	28.9	33.3%	1.9%	3.9%
Golden Pyramids Plaza	3,345.4	1.44	0	0	0	24.2	57.3	1.8%	0.5%	-29.1%
Palms Sports P.J.S.C	1,884.5	12.30	-3	0	26	17.0	14.3	27.1%	na	6.0%
Basic-Fit Nv	7,510.5	27.64	3	1	13	12.8	24.6	10.8%	0.0%	7.0%
Planet Fitness Inc - Cl A	23,399.5	70.77	9	52	-10	19.0	32.0	-85.6%	3.9%	3.2%
Life Time Group Holdings Inc.	10,995.8	14.92	1	-3	25	13.3	23.9	3.9%	na	-10.2%
Gym Group Plc/The	896.4	105.00	6	-9	-4	8.2	nm	-5.5%	0.0%	15.4%
Average						15.7	30.2	-2.0%	1.3%	-0.6%
Median						15.6	26.7	3.9%	0.5%	3.9%

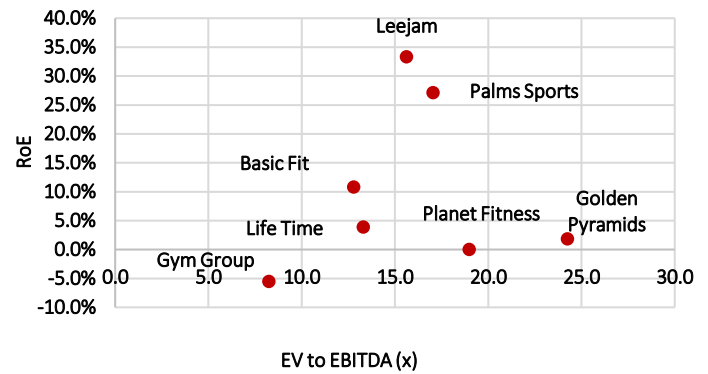
Source: Bloomberg, U Capital Research, na – not available, nm – not meaningful; *valued as of 19 December 2023

Fig. 10: Fitness & sports – P/E & Dividend Yield



Source: Bloomberg, U Capital Research; As of 19 December 2023

Fig. 11: Fitness & sports – RoE & EV to EBITDA



Summary financials

Key financials

In SAR mn, except stated otherwise	FY20	FY21	FY22	FY23e	FY24e	FY25e
Income Statement						
Revenues	663	885	1,066	1,297	1,467	1,636
Cost of revenue	(523)	(512)	(630)	(732)	(860)	(969)
Gross profit	140	373	436	565	606	667
General and Administrative Expenses	(77)	(88)	(93)	(116)	(133)	(149)
Advertising and Marketing Expenses	(16)	(14)	(14)	(14)	(18)	(22)
Other operating income, net	-	-	7	-	-	-
Operating profit	(6)	260	324	434	456	497
Finance Cost, net	(53)	(48)	(59)	(83)	(90)	(90)
Income before zakat and income tax	(59)	212	265	347	365	407
Zakat	-	(6)	(7)	(10)	(10)	(11)
Net income for the period	(59)	206	257	338	355	396
Balance Sheet						
Cash and cash equivalents	258	180	301	424	244	163
Trade Receivables	21	24	23	39	35	39
Advances to contractors, suppliers and other receivables	13	34	35	40	43	48
Right-of-Use Assets	771	787	754	977	1,093	1,187
Property, plant and equipment	1,446	1,510	1,535	1,621	1,876	2,091
Total assets	2,567	2,594	2,698	3,192	3,396	3,654
Borrowings	488	365	260	242	217	193
Lease Liabilities	921	941	911	1,111	1,130	1,140
Accounts Payable	53	81	62	98	94	106
Total liabilities	1,903	1,789	1,760	2,105	2,148	2,229
Share Capital	524	524	524	524	524	524
Retained Earnings	85	204	312	427	556	733
Equity Attributable to Shareholders	664	805	939	1,087	1,248	1,425
Cash Flow Statement						
Net cash generated from operating activities	330	439	669	846	791	903
Net cash generated from investing activities	(110)	(228)	(180)	(317)	(460)	(448)
Net cash (used in) provided by financing activities	(30)	(289)	(369)	(407)	(510)	(535)
Cash and cash equivalents at the end of the period	258	180	301	424	244	163
Key Ratios						
Gross margin (%)	21.1%	42.1%	40.9%	43.6%	41.3%	40.8%
EBITDA margin (%)	30.5%	52.8%	52.0%	52.7%	51.3%	51.1%
Operating margin (%)	-0.9%	29.3%	30.4%	33.4%	31.1%	30.4%
Net margin (%)	-8.9%	23.3%	24.1%	26.0%	24.2%	24.2%
ROA	-2.3%	8.0%	9.7%	11.5%	10.8%	11.2%
ROE	-8.5%	28.0%	29.5%	33.3%	30.4%	29.6%
Current Ratio (x)	0.5x	0.4x	0.5x	0.6x	0.4x	0.3x
Capex/Sales	16.6%	23.4%	16.8%	19.9%	31.4%	27.4%
Debt-Equity Ratio	2.1x	1.6x	1.2x	1.2x	1.1x	0.9x
EPS	(1.1)	3.9	4.9	6.4	6.8	7.6
BVPS	12.7	15.4	17.9	20.7	23.8	27.2
DPS	-	2.1	2.7	3.5	3.7	4.2
Dividend Payout Ratio	0.0%	53.4%	54.0%	54.3%	54.7%	55.2%
Dividend Yield (%)	0.0%	1.9%	3.2%	1.9%	2.0%	2.2%
P/E (x)	-69.0	27.7	17.1	28.9	27.4	24.6
P/BV (x)	6.1	7.1	4.7	9.0	7.8	6.8
EV/EBITDA (x)	25.8	14.7	9.5	15.6	14.4	13.1
Price as at period end*	81.1	77.3	109.0	126.0	126.0	126.0


Source: Company Reports, U Capital Research; *Current market price is used for forecast periods


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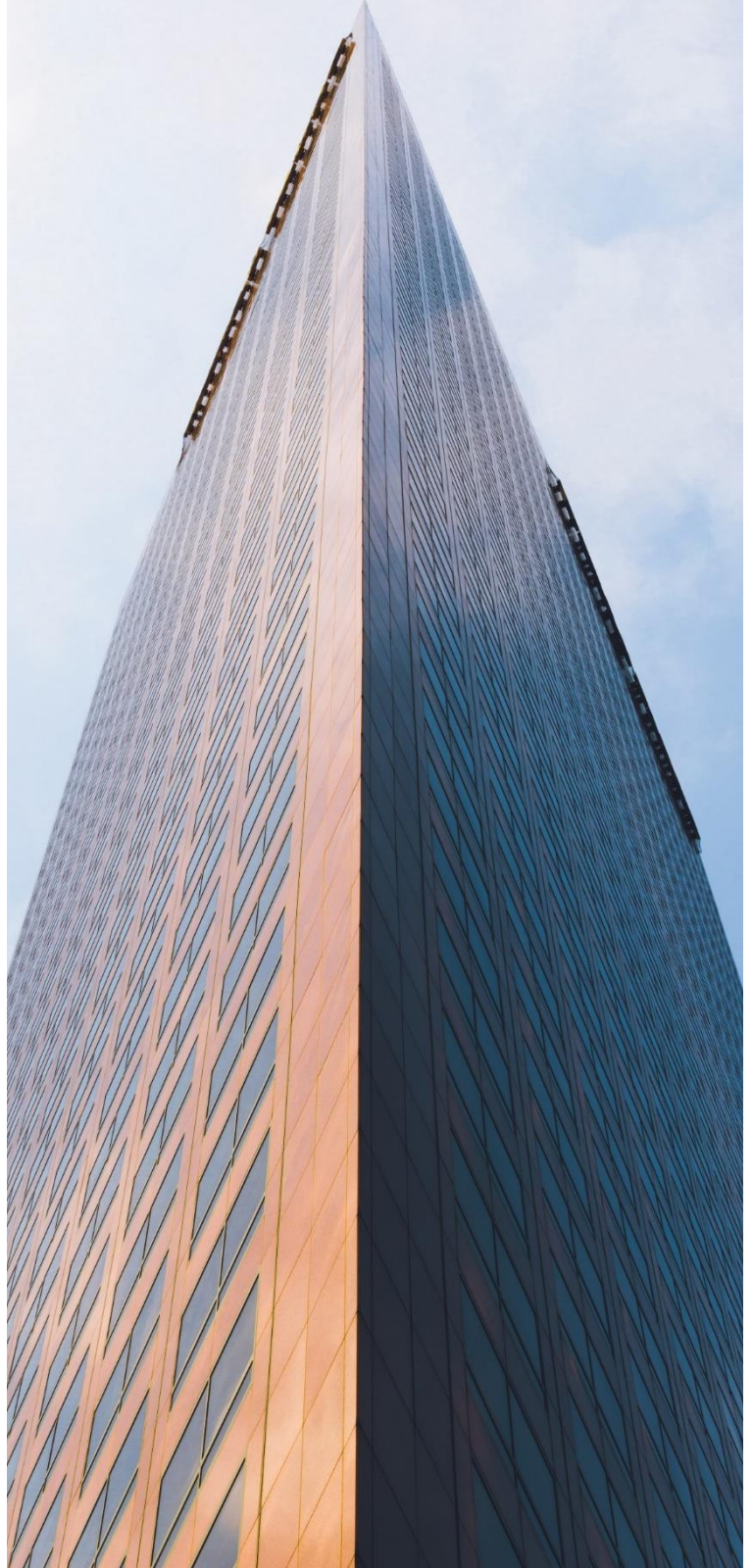
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Disclaimer

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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