

Abdullah Al Othaim Markets Co.

Strong Performance FY2020, Despite Challenging Market Conditions.

Abdallah Al-Othaim Markets (Al-Othaim) achieved 7.9% top-line growth FY2020A thanks to the strong performance in H1 2020 due to COVID-related stock-piling. Improved margins throughout the year due to governmental support, while strong net income FY2020A because of unprecedented profits. Despite the VAT and expat exodus, which are expected to weaken demand, we believe that Al-Othaim's strong marketing standing provides the company with a competitive advantage.

We update our 52 weeks target price **SAR130.0**/share while maintaining our **Neutral** recommendation.

Al-Othaim seems to be impacted by the current economic challenges as revenues during the last quarter of the year dropped by 2.5% Y-o-Y, from SAR2,099mn in Q4 2019 to SAR2,045mn in Q4 2020. The weak demand is a continuation of Q3 2020's drop in demand as a result of the 15% VAT enforcement back in July 2020, in addition to the remote learning measures that impacted the typical school season. However, the company witnessed some recovery on quarterly basis as revenues increased by 12.8% Q-o-Q. COGS dropped by 4.4% during Q4 2020, in line with the drop in sales, resulting in a slight increase in gross profit by 3.1% Y-o-Y. Gross margin stood at 25.8% by Q4 2020, which is an improvement compared to 24.4% in Q4 2019 (22.7% in Q3 2020).

During the quarter, the real estate activity witnessed some pick up, which resulted in rental income for Al-Othaim that surpassed pre-COVID levels. For Q4 2020, the company reported rental income of SAR23mn in Q4 2020, compared to SAR20mn in Q4 2019 representing a 16.9% increase Y-o-Y. Moreover, SG&A remained flat Y-o-Y, which coupled with the rental income growth, resulted in Operating margin improvement. Operating margin stood at 8.9% for Q4 2020, compared to 7.8% in Q4 2019. Another factor to the improvement of the company's operating margin during the quarter is the discounts given to Al-Othaim by the suppliers that are usually accounted for in the last quarter of each fiscal year.

The company's share in associates increased by SAR1.28mn, from SAR4.7mn in Q4 2019 to SAR5.9mn in Q4 2020. Moreover, during the quarter, the company's profit from discontinued operations included a non-recurring amount of SAR6.6mn that resulted from the revaluation of the assets available for sale related to the discontinued agricultural activity at fair value. That being said, net income reached SAR165mn in Q4 2020, representing an increase of 16.5% Y-o-Y, compared to the SAR142mn posted in Q4 2019. Furthermore, net income margin increased from 6.8% in Q4 2019 to 8.1% in Q4 2020.

While the company's bottom-line numbers showed significant improvement, it is important to note that this is not a reflection of the company's operating efficiency, around 35% of the company's net income growth is due to the non-recurring profits obtained from the revaluation of the company's assets, therefore, we believe that Q4 2020 bottom-line numbers are a slightly high base for Q4 2021e.

It is worth noting that the company recently opened a new branch in Egypt, to bring the total number of branches to 45 branches

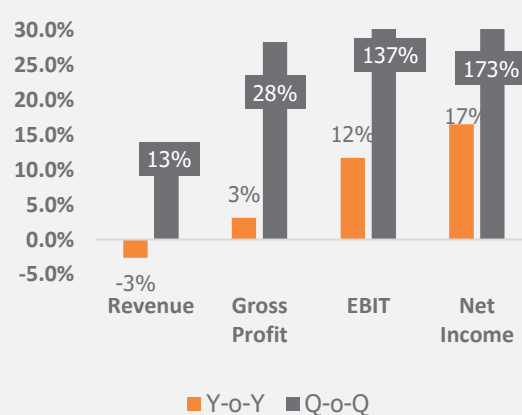
02 March 2021

Recommendation	Neutral
Previous Recommendation	Neutral
Current Price (02-03-2021)	SAR122.2
Target Price (52 Weeks)	SAR130.0
Upside/ (Downside)	6.4%
Shariah Compliance	Pass

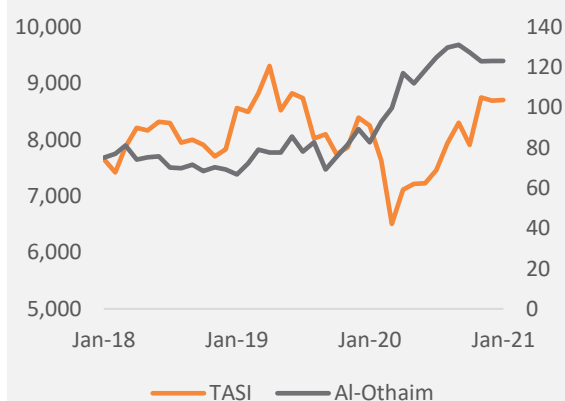
Key Financial Ratios

Ratio	Q4 2020	Q3 2020	Q4 2019
Revenue Growth	12.8%	-29.6%	8.3%
Gross Margin	25.8%	22.7%	24.4%
EBIT Margin	8.9%	4.3%	7.8%
Net Margin	8.1%	3.3%	6.8%

Key Financial Results (Q4 2020)



Share Price Performance



Financial Overview

2020A Overview & Outlook

The Stock-piling phenomena in H1 2020 was Al-Othaim's lifeline during the pandemic. Since the first quarter of the year, Al-Othaim witnessed a significant demand on its products as people panic-purchased groceries during the enforced lockdowns. The pattern remained throughout the first half of the year, especially after the announcement of the tripling of the VAT in July, which motivated more bulk purchases in Q2 2020. However, by Q3 2020 demand decreased in light of the application of the VAT and the expat exodus, reaching its lowest revenue level of the year at SAR1,813mn. However, by Q4 2020 revenues recovered slightly as the economic conditions started to gradually improve yet didn't reach pre-COVID levels compared to Q4 2019. That being said, revenue FY2020 increased by 7.9% Y-o-Y, from SAR8,166mn FY2019A to SAR8,811mn in FY2020A. The revenue growth is mainly due to the contribution of H1 2020.

Improved margins throughout the year 2020, in light of the governmental support during the COVID-19 crisis. During FY2020, there was a significant drop in rental income, due to slow down real estate activity, coupled with discounts, exemptions and grace periods that were granted by Al-Othaim to its tenant. Rental income dropped by 28.3%, from SAR80mn FY2019 to SAR57mn FY2020. The governmental initiatives to mitigate the impact on COVID-19 significantly supported the company's margins during the year. Gross margin reached 21.7% FY2020 compared to 20.7%, while operating margin reached 5.9% FY2020 compared to 4.9% FY2019.

Non-recurring profits provided Al-Othaim with an unsustainably high net income given the market conditions. Despite the drop in rental income and share in associates during the year 2020, the company managed to end the year with a strong net income growth of 30.8% Y-o-Y. The spike in net is partially due to the strong top-line performance, however the company reported income from discontinued operations that amounted to SAR5.4mn FY2020A, compared to losses of SAR7.5mn FY2019A. During the year the company revaluated some of the assets available for sale, which were related to the discontinued agriculture activity, resulting in the non-recurring profits of SAR6.7mn. We believe that the strong bottom-line performance makes FY2020A a higher base year than normal and this level of net income growth is not expected to be sustained in the future.

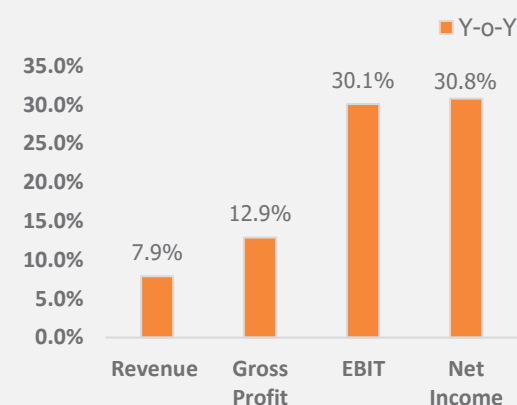
Challenging environment ahead, on the back of the expat exodus, however the company's market position and sustainable expansion will support the company's survival. It is undoubtedly that the expat exodus is bound to significantly impact demand on groceries, especially in addition of the 15% VAT. However, Al-Othaim was well prepared to such challenges, thanks to its (1) broad-based spread across the Kingdom. (2) Given the company's product offering being categorized as essentials, (3) in addition to the market consolidation, we believe that Al-Othaim's market share is secured. The company now has a total of 250 branches across the Kingdom, in addition to 45 branches in Egypt.

Going forward, we expect that during FY2021e margins will normalize to pre-COVID levels. Real estate activity is expected to continue to regain momentum during the year, especially as the movement restrictions ease. Expat exodus remain a challenge, especially in light of the anticipated consumer down-trade. However, market consolidation will provide the company with expansion opportunities that could lead to strong revenues in the near future.

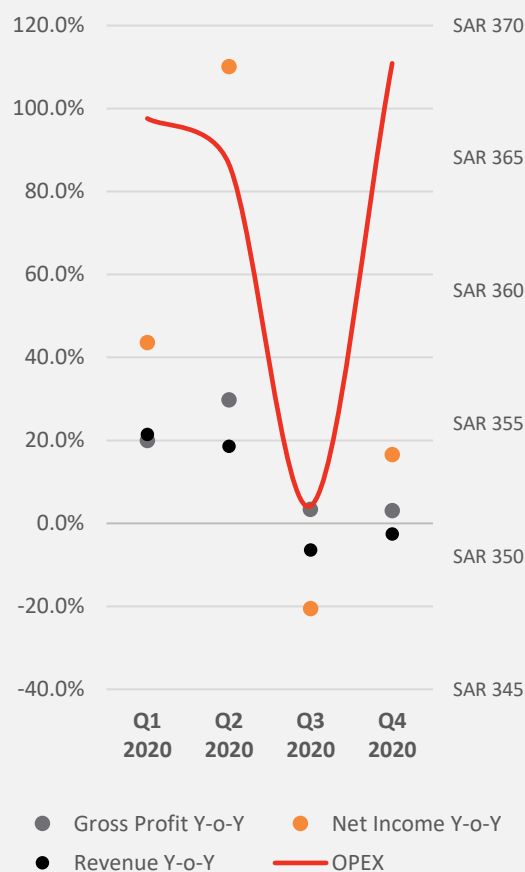
Key Financial Ratios

Ratio	FY2020	FY2019
Revenue Growth	7.9%	8.8%
Gross Margin	21.7%	20.7%
EBIT Margin	5.9%	4.9%
Net Margin	5.1%	4.1%

Key Financial Results (2020A)



Quarterly Performance



Financial Projection

DCF Valuation

	2020 A	2021 F	2022 F	2023 F	2024 F	2025 F	2026 F
EBITDA	849	875	929	988	1,043	1,098	1,152
Operating CF	837	875	954	1,018	1,069	1,123	1,176
Capex	(476)	(477)	(479)	(481)	(480)	(476)	(471)
FCFF	361	397	475	537	590	647	705
Stub Period (FCF to be discounted)	0	397	475	537	590	647	705
PV (FCFF)	0	370	411	434	444	454	461
WACC	7.58%						
Perpetuity Growth	2.50%						
PV-FCFF	2,573						
PV-TV	9,547						
Net Debt	(1,110)						
Less: End of services benefits	(171)						
Add: Investments	861						
Intrinsic Values	11,700						
Shares Outstanding	90						
Equity value per share	130.0						
CMP (02-03-2021)	122.2						
Upside / (Downside%)	6.4%						

We have valued Al-Othaim using DCF approach, considering a WACC is equal to 7.58% (based on a risk-free rate of 2.70%, market risk premium 7.0%, Beta of 0.54).

Based on the DCF valuation, the fair price Al-Othaim share price is SAR130.0, which is higher than the traded value by 6.4%.

Financial Ratios

	2019 A	2020 A	2021 F	2022 F	2023 F	2024 F	2025 F	2026 F
Return on Average Assets (%)	8.2%	9.3%	8.9%	8.9%	9.1%	9.4%	9.6%	9.8%
Return on Average Equity (%)	29.2%	28.5%	29.6%	31.7%	34.0%	35.5%	36.3%	0.0%
Earnings Before Zakat Margin	4.5%	5.3%	5.1%	5.1%	5.2%	5.3%	5.4%	5.5%
Net Income Margin (%)	4.2%	5.1%	4.9%	5.0%	5.0%	5.1%	5.2%	5.3%
Revenue Growth (%)	8.8%	7.9%	4.9%	5.5%	6.0%	5.3%	5.0%	4.8%
DPS	4.50	4.50	4.50	5.00	6.00	6.00	6.00	6.00

Income Statement

	2019 A	2020 A	2021 F	2022 F	2023 F	2024 F	2025 F	2026 F
Revenues	8,166	8,811	9,242	9,751	10,340	10,883	11,426	11,969
Cost of Revenues	(6,473)	(6,900)	(7,255)	(7,655)	(8,117)	(8,543)	(8,969)	(9,396)
Gross Profit	1,693	1,911	1,987	2,097	2,223	2,340	2,457	2,573
SG&A	(1,376)	(1,452)	(1,523)	(1,597)	(1,683)	(1,760)	(1,837)	(1,912)
Zakat	(11)	(16)	(15)	(16)	(17)	(17)	(18)	(20)
Net Income	345	451	454	484	521	557	596	636

Balance Sheet

	2019 A	2020 A	2021 F	2022 F	2023 F	2024 F	2025 F	2026 F
Current Assets	1,288	1,364	1,544	1,733	1,879	2,047	2,246	2,479
Non-Current Assets	3,478	3,602	3,730	3,843	3,944	4,031	4,104	4,162
Total Assets	4,766	4,966	5,274	5,576	5,823	6,078	6,350	6,641
Current Liabilities	1,968	1,946	2,037	2,154	2,286	2,406	2,526	2,643
Non-Current Liabilities	1,273	1,451	1,619	1,770	1,904	2,021	2,118	2,196
Total Equity	1,525	1,569	1,618	1,652	1,633	1,650	1,706	1,802
Total Liabilities and Equity	4,766	4,966	5,274	5,575	5,823	6,078	6,350	6,641

Guide to Ratings and Disclaimer

Guide to Ratings

Buy	An upside potential of more than 20% in 52-week period
Overweight	An upside Potential of more than 10% in 52-week period
Neutral	Will stay in the range of its value (up/down 10%) in a 52-week period
Underweight	A downside potential of more than 10% in 52-week period
Sell	A downside potential of more than 20% in 52-week period

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