Savola Group Company

Food & Agriculture Sector
SAVOLA AB: Saudi Arabia
01 May 2011

US$3.706bn	60.1%	US$4.693mn
Market cap	Free float	Avg. daily volume

Target price	33.70	21.33% over current
Consensus price	37.00	33.1% over current
Current price	27.80	as at 30/4/2011

Underweight | Neutral | **Overweight**

Research Department
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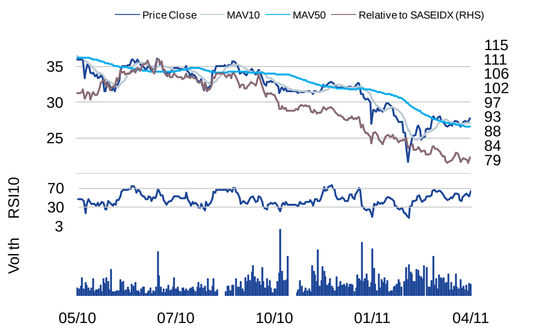
Key themes

Driven by rising population and improving education, we expect the food sector in Saudi Arabia to continue growing. Rising shopping in supermarkets and hypermarkets should support food sales and benefit Savola with its presence in retailing as well as food.

Implications

Savola is one of our top picks in the food sector. It has attractive financial ratios that reflect its improvement. It is performing well operationally and offers growth in the near term at a reasonable valuation.

Performance

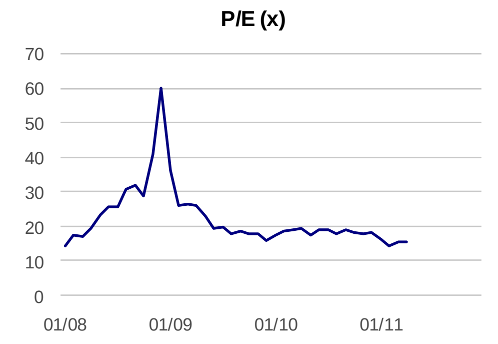


Earnings

Period End (SAR)	12/10A	12/11E	12/12E	12/13E
Revenue (mn)	21,070	23,804	25,991	28,356
Revenue Growth	17.6%	13.0%	9.2%	9.1%
EBITDA (mn)	1,359	1,575	1,728	1,898
EBITDA Growth	4.1%	15.9%	9.7%	9.8%
EPS	1.77	1.90	2.17	2.35
EPS Growth	-6.8%	7.4%	13.9%	8.3%

Source: Company data, Al Rajhi Capital

Valuation



Source: Company data, Al Rajhi Capital

Savola Group
Q1: decent recovery

Savola released Q1 results with robust year-on-year sales growth of 17% and operating profit growth of 16% (excluding operating income from associates). Net profit significantly declined by 58% from last same period to reach SAR167mn. This can be mainly attributed to the fact that Q1 2010 net profit included capital gain of SAR196mn (Herfy IPO). However, this figure is still below our net profit forecast of SAR195mn. The discrepancy can be explained by the high interest expenses and minority interests. However, we think that Q1 results are decent and showed some recovery after the unsatisfying results of the previous quarter (Q4 2010). We also believe that the damage to Savola's share price has already been done as it fell from SAR32 level to around SAR27. We maintain our Overweight rating and price target of SAR33.7, which implies 21% upside.

Food prices and overseas business supported top line growth in Q1: Savola's achieved year-on-year strong revenue growth of 17% in Q1; with all segments growing strongly but food segment continued to drive growth. We believe that growth came from both higher prices and volumes. Foodstuff prices, sugar and edible oil, had been skyrocketing until recently when sugar price fell from US$31 to US$22 (Bloomberg: Sugar #11). Despite the 5% decline in revenues from Egypt operations due to the recent unrest, overseas operations have driven Savola's top line growth in Q1. Revenues from Iran and other countries grew by 41% and 19% respectively. On the other hand, retail sales grew by 16% to reach SAR2.1bn in Q1 driven by new stores and the two salary bonus (declared by the government and other private entities). Savola hasn't disclosed the full details of its revenues breakdown but we suspect that plastics sales grew by 16% driven by lofty oil prices. We expect Q2 revenues growth to be slightly below Q1 as foodstuff prices (mainly sugar) have marginally declined.

Respectable operating profit but net income below expectations: Savola's gross margin declined from 16.8% in Q1 2010 to 16.5% in Q1 2011. We explain this drop chiefly by a decline in the gross margin in the food and plastics operations. Nevertheless, Savola's operating profit (excluding third party's operating income) grew by 16% from SAR177mn to SAR206mn due to a remarkable decline in SG&A costs. Net profit, however, declined by 15% from SAR198mn to SAR167mn (excluding the capital gain of SAR196mn recorded on the IPO of Herfy in Q1 2010). Looking forward, we believe that Savola can achieve in 2011 a gross margin similar to 2010 level of 16.9%. We also expect to see better net profits over the next three quarters.

Valuation: Savola is a respected group with a strong position in both food and retail industries. It also owns invaluable stakes in strong companies such as Almarai and Herfy. Although the group showed strong revenue growth in Q1, it failed to achieve consistent growth in net profits. But Q1 results overall were decent and showed signs of recovery after very weak results in Q4 last year. We expect Q2 results to be slightly weaker in terms of top line growth but stronger in terms of bottom line. We retain our Overweight rating on the company and our price target of SAR33.7, implying 21% upside potential. Savola's share price currently trades on a 2011 PE ratio of 14.6x and an EV/EBITDA multiple of 7.6x. The stock offers 3.5% dividend yield at current price.

Corporate summary

Savola, one of the leading companies in food and retail industries, is a group that holds several companies that operate in different industries. According to Savola's website, the Group operates its businesses through four Core Sectors, these are "Savola Foods Sector", including Edible Oils, Foods, and Sugar, "Savola Retail Sector", including Retail (Panda - and Hyper Panda), Real Estate Sector (Kinan International) and Savola Plastics Sector. Furthermore, Savola has a major investment in the leading dairy company in the GCC (Almarai) and in Herfy Foods Company with stakes of 29.9% and 49% respectively.

Share information

Market cap (SAR/US$)	13.90bn / 3.706bn
52-week range	21.65 - 36.10
Daily avg volume (US$)	4.693mn
Shares outstanding	500.0mn
Free float (est)	60.1%

Performance:	1M	3M	12M
Absolute	-0.4%	-4.1%	-22.8%
Relative to index	-2.7%	-8.6%	-20.5%

Major Shareholder:	
Mohammed Ibramim Alisa	11.9%
General Oraganistion for Social Insurance	10.9%

Source: Bloomberg, Al Rajhi Capital

Valuation

Period End	12/10A	12/11E	12/12E	12/13E
Revenue (SARmn)	21,070	23,804	25,991	28,356
EBITDA (SARmn)	1,359	1,575	1,728	1,898
Net Profit (SARmn)	887	952	1,085	1,175
EPS (SAR)	1.77	1.90	2.17	2.35
DPS (SAR)	1.25	1.00	1.00	0.99
EPS Growth	-6.8%	7.4%	13.9%	8.3%
EV/EBITDA (x)	8.6	7.6	7.1	6.4
P/E (x)	15.7	14.6	12.8	11.8
P/B (x)	2.0	1.9	1.8	1.6
Dividend Yield	4.5%	3.6%	3.6%	3.6%

Source: Company data, Al Rajhi Capital

Figure 1. Savola: 2010Q1A vs. 2011Q1E vs. 2011Q1A & 2010Q2A vs. 2011Q2E

(SAR) mn	2010Q1A	2011Q1E	2011Q1A	YOY % chg.	2010Q2A	2011Q2E	YOY % chg.
Revenues	**4,778.8**	**5,289.5**	**5,641.7**	**18.1%**	**4,868.1**	**5,516.4**	**13.3%**
Gross Profit	**804.5**	**835.7**	**863.0**	**7.3%**	**709.8**	**871.6**	**22.8%**
Gross margin	16.8%	15.8%	15.3%		14.6%	15.8%	
Operating profit	**177.3**	**158.3**	**206.0**	**16.2%**	**135.8**	**209.6**	**54.3%**
Net Income	**394.0**	**195.1**	**165.2**	**-58.1%**	**207.7**	**222.2**	**7.0%**

Source: Company data, Al Rajhi Capital

We expect revenues to reach SAR23.8bn this year

Revenue growth set to remain above 8% over the next three years

We expect gross margin to remain close to last year's level

EV/EBITDA of 7.6x is attractive

Income Statement (SARmn)	**12/09A**	**12/10A**	**12/11E**	**12/12E**	**12/13E**
Revenue	**17,917**	**21,070**	**23,804**	**25,991**	**28,356**
Cost of Goods Sold	(14,810)	(17,723)	(20,027)	(21,850)	(23,819)
Gross Profit	**3,107**	**3,346**	**3,777**	**4,140**	**4,537**
Government Charges					
S.G. & A. Costs	(2,162)	(2,494)	(2,786)	(3,034)	(3,318)
Operating EBIT	**945**	**852**	**991**	**1,106**	**1,219**
Cash Operating Costs	(16,611)	(19,711)	(22,229)	(24,262)	(26,458)
EBITDA	1,306	1,359	1,575	1,728	1,898
Depreciation and Amortisation	(361)	(507)	(584)	(622)	(678)
Operating Profit	**945**	**852**	**991**	**1,106**	**1,219**
Net financing income/(costs)	(227)	(210)	(216)	(225)	(225)
Forex and Related Gains	-	-	-	-	-
Provisions	-	-	-	-	-
Other Income	751	728	453	485	485
Other Expenses	(222)	(217)	-	-	-
Net Profit Before Taxes	**1,247**	**1,152**	**1,228**	**1,366**	**1,479**
Taxes	(63)	(128)	(48)	(28)	(30)
Minority Interests	(232)	(137)	(228)	(253)	(274)
Net profit available to shareholders	**952**	**887**	**952**	**1,085**	**1,175**
Dividends	(500)	(625)	(500)	(500)	(494)
Transfer to Capital Reserve	-	-	-	-	-

	12/09A	**12/10A**	**12/11E**	**12/12E**	**12/13E**
Adjusted Shares Out (mn)	500.0	500.0	500.0	500.0	500.0
CFPS (SAR)	3.089	3.063	3.528	3.920	4.254
EPS (SAR)	1.903	1.773	1.905	2.170	2.349
DPS (SAR)	1.000	1.250	1.000	1.000	0.989

Growth	**12/09A**	**12/10A**	**12/11E**	**12/12E**	**12/13E**
Revenue Growth	29.9%	17.6%	13.0%	9.2%	9.1%
Gross Profit Growth	73.7%	7.7%	12.9%	9.6%	9.6%
EBITDA Growth	61.5%	4.1%	15.9%	9.7%	9.8%
Operating Profit Growth	369.4%	-9.8%	16.3%	11.7%	10.2%
Net Profit Growth	370.2%	-6.8%	7.4%	13.9%	8.3%
EPS Growth	370.2%	-6.8%	7.4%	13.9%	8.3%

Margins	**12/09A**	**12/10A**	**12/11E**	**12/12E**	**12/13E**
Gross profit margin	17.3%	15.9%	15.9%	15.9%	16.0%
EBITDA margin	7.3%	6.5%	6.6%	6.6%	6.7%
Operating Margin	5.3%	4.0%	4.2%	4.3%	4.3%
Pretax profit margin	7.0%	5.5%	5.2%	5.3%	5.2%
Net profit margin	5.3%	4.2%	4.0%	4.2%	4.1%

Other Ratios	**12/09A**	**12/10A**	**12/11E**	**12/12E**	**12/13E**
ROCE	8.9%	7.9%	8.9%	9.2%	9.4%
ROIC	14.6%	10.2%	14.4%	15.2%	15.1%
ROE	14.3%	12.7%	13.3%	14.3%	14.3%
Effective Tax Rate	5.1%	11.1%	3.9%	2.0%	2.0%
Capex/Sales	5.3%	3.0%	4.0%	4.6%	4.7%
Dividend Payout Ratio	52.5%	70.5%	52.5%	46.1%	42.1%

Valuation Measures	**12/09A**	**12/10A**	**12/11E**	**12/12E**	**12/13E**
P/E (x)	14.6	15.7	14.6	12.8	11.8
P/CF (x)	9.0	9.1	7.9	7.1	6.5
P/B (x)	2.0	2.0	1.9	1.8	1.6
EV/Sales (x)	0.6	0.6	0.5	0.5	0.4
EV/EBITDA (x)	8.9	8.6	7.6	7.1	6.4
EV/EBIT (x)	12.3	13.7	12.1	11.0	10.0
EV/IC (x)	1.6	1.8	1.7	1.5	1.4
Dividend Yield	3.6%	4.5%	3.6%	3.6%	3.6%

Source: Company data, Al Rajhi Capital

Balance sheet is expanding due to the company's international expansion

Balance Sheet (SARmn)	12/09A	12/10A	12/11E	12/12E	12/13E
Cash and Cash Equivalents	1,001	660	1,074	1,132	1,371
Current Receivables	1,507	1,518	2,316	2,303	2,552
Inventories	2,297	2,513	2,573	2,556	2,836
Other current assets	836	1,166	1,281	1,281	1,281
Total Current Assets	**5,634**	**5,858**	**7,244**	**7,274**	**8,040**
Fixed Assets	5,537	4,719	5,121	5,688	6,343
Investments	5,056	6,123	6,166	6,166	6,166
Goodwill	918	1,020	1,008	1,008	1,008
Other Intangible Assets	112	-	-	-	-
Total Other Assets	-	-	-	-	-
Total Non-current Assets	**11,623**	**11,862**	**12,294**	**12,862**	**13,516**
Total Assets	**17,257**	**17,720**	**19,538**	**20,136**	**21,556**
Short Term Debt	3,022	2,783	3,369	3,369	3,369
Accounts Payable	1,830	2,003	2,702	2,697	2,977
Accrued Expenses	503	1,689	1,801	1,798	1,985
Dividends Payable	-	-	-	-	-
Other Current Liabilities	564	186	233	-	-
Total Current Liabilities	**6,313**	**6,662**	**8,105**	**7,864**	**8,332**
Long-Term Debt	1,996	2,393	2,268	2,268	2,268
Other LT Payables	61	171	169	169	169
Provisions	358	276	281	281	281
Total Non-current Liabilities	**2,415**	**2,840**	**2,717**	**2,717**	**2,717**
Minority interests	1,567	1,188	1,417	1,670	1,944
Paid-up share capital	5,000	5,000	5,000	5,000	5,000
Total Reserves	1,961	2,031	2,299	2,884	3,563
Total Shareholders' Equity	**6,961**	**7,031**	**7,299**	**7,884**	**8,563**
Total Equity	**8,528**	**8,218**	**8,716**	**9,554**	**10,507**
Total Liabilities & Shareholders' Equity	**17,257**	**17,720**	**19,538**	**20,136**	**21,556**

Net debt/EBITDA of 2.9x is slightly high

Ratios	12/09A	12/10A	12/11E	12/12E	12/13E
Net Debt (SARmn)	3,927	4,516	4,564	4,505	4,267
Net Debt/EBITDA (x)	3.01	3.32	2.90	2.61	2.25
Net Debt to Equity	46.1%	54.9%	52.4%	47.2%	40.6%
EBITDA Interest Cover (x)	5.7	6.5	7.3	7.7	8.4
BVPS (SAR)	13.92	14.06	14.60	15.77	17.13

Cashflow Statement (SARmn)	12/09A	12/10A	12/11E	12/12E	12/13E
Net Income before Tax & Minority Interest	**1,247**	**1,152**	**1,228**	**1,366**	**1,479**
Depreciation & Amortisation	361	507	584	622	678
Decrease in Working Capital	534	(86)	(116)	(212)	(60)
Other Operating Cashflow	201	222	(29)	(28)	(30)
Cashflow from Operations	**2,343**	**1,795**	**1,667**	**1,748**	**2,067**
Capital Expenditure	(945)	(634)	(963)	(1,190)	(1,333)
New Investments	(129)	(601)	(102)	-	-
Others	(427)	(20)	-	-	-
Cashflow from investing activities	**(1,500)**	**(1,255)**	**(1,065)**	**(1,190)**	**(1,333)**
Net Operating Cashflow	**842**	**539**	**602**	**558**	**734**
Dividends paid to ordinary shareholders	(513)	(627)	(626)	(500)	(496)
Proceeds from issue of shares	-	-	-	-	-
Effects of Exchange Rates on Cash	-	-	-	-	-
Other Financing Cashflow	(316)	(669)	42	-	-
Cashflow from financing activities	**(444)**	**(979)**	**(91)**	**(500)**	**(496)**
Total cash generated	398	(440)	511	58	239
Cash at beginning of period	604	1,001	660	1,074	1,132
Implied cash at end of year	**1,002**	**561**	**1,172**	**1,132**	**1,371**

We expect capex to increase due to expansion in the retail segment

Ratios	12/09A	12/10A	12/11E	12/12E	12/13E
Capex/Sales	5.3%	3.0%	4.0%	4.6%	4.7%

Source: Company data, Al Rajhi Capital

Disclaimer and additional disclosures for Equity Research

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Additional disclosures

1. Explanation of Al Rajhi Capital's rating system

Al Rajhi Capital uses a three-tier rating system based on absolute upside or downside potential for all stocks under its coverage except financial stocks and those few other companies not compliant with Islamic Shariah law:

"Overweight": Our target price is more than 15% above the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

"Neutral": We expect the share price to settle at a level between 5% below the current share price and 15% above the current share price on a 6-9 month time horizon.

"Underweight": Our target price is more than 5% below the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

2. Definitions

"Time horizon": Our analysts make recommendations on a 6-9 month time horizon. In other words, they expect a given stock to reach their target price within that time.

"Fair value": We estimate fair value per share for every stock we cover. This is normally based on widely accepted methods appropriate to the stock or sector under consideration, e.g. DCF (discounted cash flow) or SoTP (sum of the parts) analysis.

"Target price": This may be identical to estimated fair value per share, but is not necessarily the same. There may be very good reasons why a share price is unlikely to reach fair value within our time horizon. In such a case we set a target price which differs from estimated fair value per share, and explain our reasons for doing so.

Please note that the achievement of any price target may be impeded by general market and economic trends and other external factors, or if a company's profits or operating performance exceed or fall short of our expectations.

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