



US\$5.30bn Market cap **35.8%** Free float **US\$3.302mn** Avg. daily volume

Target price **107.1** 23.77% over current
 Consensus price **118.0** 36.4% over current
 Current price **86.50** as at 17/10/2011

Underweight **Neutral** **Overweight**

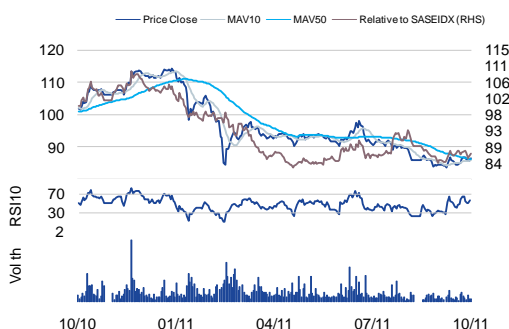
Key themes

We believe that the food industry will continue to grow strongly. Almarai has a very strong position in the GCC dairy market. We believe that Almarai will continue to enter new segments through start-ups or acquisitions to maintain its outstanding growth.

Implications

Almarai is our preferred stock in the agriculture & food sector. Almarai is performing well operationally and offers growth in the near term at a reasonable valuation. We expect high transparency to continue to support Almarai's share price, and think it will find favour with international investors if the Saudi stock market is fully opened up.

Performance

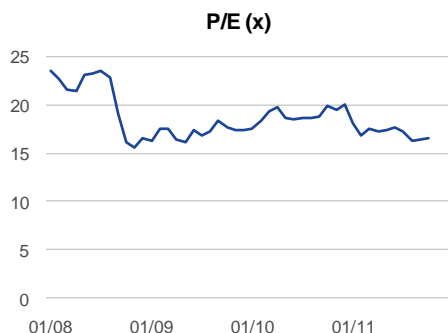


Earnings

Period End (SAR)	12/10A	12/11E	12/12E	12/13E
Revenue (mn)	6,931	7,916	9,048	10,262
Revenue Growth	18.1%	14.2%	14.3%	13.4%
EBITDA (mn)	2,095	2,228	2,585	2,976
EBITDA Growth	17.4%	6.4%	16.0%	15.1%
EPS	5.59	5.15	6.88	8.17
EPS Growth	17.2%	-7.9%	33.7%	18.7%

Source: Company data, Al Rajhi Capital

Valuation



Source: Company data, Al Rajhi Capital

Almarai

Good results despite challenges

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Almarai released a mixed bag of results for Q3 with a robust top-line y-o-y growth of 14.8%, but a weak net profit y-o-y growth of only 1.2%. All segments grew, but Poultry and juice continued to show the highest sales growth. Pressure on margins continued but it's likely to cool down as commodity prices saw a decline during Q3. Looking forward, we expect a similar operating performance in Q4 but depressed net profit due to impairment loss on its investment in Zain. Although Almarai share price might see further downside on the very short term, we remain positive on the company and hence maintain our Overweight rating. On the back of Q3 results, we have marginally revised our forecasts and lowered our target price to SAR107.1.

Solid top line growth despite boycotts: Almarai reported y-o-y sales growth of 14.8%, above our estimate of 13.9%. As we had expected, the recent boycott impact on sales was petty. According to our discussions with retailers, we believe that last Ramadan month has been the worst for all dairy companies in the last couple of years as it coincided with summer holidays. However, September's sales were the strongest during Q3, offsetting the weak sales during Ramadan. As for revenue breakdown, all segments grew strongly but poultry and juice showed the highest y-o-y sales growth of 50% and 23%. Bakery sales growth of 13% was below expectations, which the company attributed to the seasonality of business. However, we think that intensifying competition from new large entrants such as Pain D'Or has also dented the performance of this segment.

Cooling commodities is a catalyst: Almarai's gross margin has contracted by 200bps during the last couple of quarters due to rising feedstuffs and packaging costs. This pressure is likely to ease as most commodities prices have fallen in Q3 including corn, juice concentrates and crude oil (packaging costs) on concerns that global economy is on the verge of another recession. That said, the benefit of this fall is unlikely to be seen during Q4. We believe that cooling commodity prices coupled with increased government subsidies on feedstuffs will improve Almarai's gross margin by at least 90bps starting from Q1 2012.

Net profit likely to take a hit in Q4: As Zain stock continued to trade at levels far below par value, Almarai announced that it would reflect this impairment in its income statement. In our view, this is the best time to record such loss as the share price has been already depressed and any further deterioration should be limited. There is no clarity on how much this amount would be as it depends on Zain's share price, but we assume that it will be in the range of SAR120mn to SAR150mn. It's worth noting that any positive news on Zain's financial restructuring could support its stock price and hence reduce this impairment.

Conclusion and valuation: Despite the challenges including rising feedstuff costs and difficulties to pass them on to consumers followed by a boycott in Q3, Almarai continued to deliver good results. The impairment loss on Zain investment is disappointing; however, we think that this is the best time to record such loss and we credit the company for high transparency. We maintain our long term positive view but have slightly trimmed our forecasts. Therefore, we remain Overweight with a revised target price of SAR107.1 (old target price: SAR110.7). Our new target offers around 23% upside potential.



Corporate summary	Share information	Valuation																																																							
Almarai is the largest integrated dairy foods company in the world, with a reputation for quality in the Gulf states in which it operates. Almarai began in 1976 under the leadership of HH Prince Sultan bin Mohammed bin Saud Al Kabeer, as it remains to this day. The company is based in Riyadh, the capital of Saudi Arabia. Almarai's network extends throughout the Arabian Peninsula, leading and influencing the agricultural, dairy processing and food distribution industries. Almarai started as a pure dairy company but it has greatly expanded to include cheese, bakery, juice, and poultry.	Market cap (SAR/US\$) 19.90bn / 5.30bn 52-week range 83.75 - 114.3 Daily avg volume (US\$) 3.302mn Shares outstanding 230.0mn Free float (est) 35.8% Performance: 1M 3M 12M Absolute 2.4% -5.2% -14.3% Relative to index 3.1% -0.1% -12.2% Major Shareholder: Savola Al-Azizia United Co 29.9% Al-Saud Sultan Mohamed 28.6% Source: Bloomberg, Al Rajhi Capital	<table border="1"> <thead> <tr> <th>Period End</th> <th>12/10A</th> <th>12/11E</th> <th>12/12E</th> <th>12/13E</th> </tr> </thead> <tbody> <tr> <td>Revenue (SARmn)</td> <td>6,931</td> <td>7,916</td> <td>9,048</td> <td>10,262</td> </tr> <tr> <td>EBITDA (SARmn)</td> <td>2,095</td> <td>2,228</td> <td>2,585</td> <td>2,976</td> </tr> <tr> <td>Net Profit (SARmn)</td> <td>1,285</td> <td>1,183</td> <td>1,583</td> <td>1,879</td> </tr> <tr> <td>EPS (SAR)</td> <td>5.59</td> <td>5.15</td> <td>6.88</td> <td>8.17</td> </tr> <tr> <td>DPS (SAR)</td> <td>2.00</td> <td>2.00</td> <td>2.00</td> <td>2.45</td> </tr> <tr> <td>EPS Growth</td> <td>17.2%</td> <td>-7.9%</td> <td>33.7%</td> <td>18.7%</td> </tr> <tr> <td>EV/EBITDA (x)</td> <td>11.8</td> <td>11.9</td> <td>10.5</td> <td>9.4</td> </tr> <tr> <td>P/E (x)</td> <td>15.5</td> <td>16.8</td> <td>12.6</td> <td>10.6</td> </tr> <tr> <td>P/B (x)</td> <td>3.2</td> <td>3.0</td> <td>2.6</td> <td>2.2</td> </tr> <tr> <td>Dividend Yield</td> <td>2.3%</td> <td>2.3%</td> <td>2.3%</td> <td>2.8%</td> </tr> </tbody> </table> Source: Company data, Al Rajhi Capital	Period End	12/10A	12/11E	12/12E	12/13E	Revenue (SARmn)	6,931	7,916	9,048	10,262	EBITDA (SARmn)	2,095	2,228	2,585	2,976	Net Profit (SARmn)	1,285	1,183	1,583	1,879	EPS (SAR)	5.59	5.15	6.88	8.17	DPS (SAR)	2.00	2.00	2.00	2.45	EPS Growth	17.2%	-7.9%	33.7%	18.7%	EV/EBITDA (x)	11.8	11.9	10.5	9.4	P/E (x)	15.5	16.8	12.6	10.6	P/B (x)	3.2	3.0	2.6	2.2	Dividend Yield	2.3%	2.3%	2.3%	2.8%
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Q3 results: in line with our estimates

Below we present Almarai's Q3 results versus our estimates.

Figure 1. Almarai: 2010Q3 vs. 2011Q3A vs. 2011Q3E

(SAR) mn	2010Q3A	2011Q3A	YOY % chg.	2011Q3E
Fresh Dairy	890.6	986.1	10.7%	977.9
Long Life Dairy	153.7	176.0	14.5%	172.1
Fruit Juice	209.3	256.7	22.6%	251.2
Cheese & Butter	319.9	353.5	10.5%	364.7
Bakery	202.1	228.4	13.0%	230.4
Poultry	49.9	75.0	50.4%	80.8
Arable & Horticulure	3.7	24.3	556.2%	7.4
Other	4.6	5.2	13.9%	4.8
Total Revenues	1,833.8	2,105.3	14.8%	2,089.3
Gross Profit	796.5	871.3	9.4%	860.8
Gross Profit Margin	43.4%	41.4%		41.2%
Operating Profit	474.5	477.0	0.5%	491.0
Net Income	424.5	429.7	1.2%	433.7

Source: Company data, Al Rajhi Capital

Q4 estimates: depressed bottom line

Below we present our estimates for Q4 and 2011 full year.

Figure 2. Almarai: 2010Q4A vs. 2011Q4E & FY2010A vs. FY2011E

(SAR) mn	2010Q4A	2011Q4E	YOY % chg.	FY2010A	FY2011E	YOY % chg.
Fresh Dairy	810.4	898.0	10.8%	3,168.7	3,499.5	10.4%
Long Life Dairy	173.2	199.1	15.0%	658.9	747.1	13.4%
Fruit Juice	187.8	229.1	22.0%	745.1	892.3	19.8%
Cheese & Butter	327.0	366.2	12.0%	1,282.4	1,441.0	12.4%
Bakery	224.3	263.5	17.5%	821.2	952.4	16.0%
Poultry	48.0	79.2	64.9%	176.1	299.4	70.0%
Arable & Horticulure	16.0	11.2	-30.0%	47.7	59.5	24.8%
Other	12.0	8.4	-30.0%	30.7	25.5	-17.0%
Total Revenues	1,798.6	2,054.7	14.2%	6,930.8	7,916.6	14.2%
Gross Profit	668.3	739.7	10.7%	2,735.9	3,012.4	10.1%
Gross Profit Margin	37.2%	36.0%		39.5%	38.1%	-3.6%
Operating Profit	319.2	345.2	8.1%	1,459.5	1,519.4	4.1%
Net Income	283.8	169.3*	-40.3%	1,285.4	1,183.5	-7.9%

*Net profit is adjusted to the expected impairment loss of SAR129mn on Zain investment

Source: Company data, Al Rajhi Capital



Income Statement (SARmn)	12/09A	12/10A	12/11E	12/12E	12/13E
Revenue	5,869	6,931	7,916	9,048	10,262
Cost of Goods Sold	(3,503)	(4,195)	(4,904)	(5,524)	(6,209)
Gross Profit	2,366	2,736	3,012	3,524	4,054
Government Charges					
S.G. & A. Costs	(1,087)	(1,276)	(1,493)	(1,696)	(1,909)
Operating EBIT	1,279	1,460	1,519	1,829	2,145
Cash Operating Costs	(4,085)	(4,836)	(5,688)	(6,463)	(7,287)
EBITDA	1,784	2,095	2,228	2,585	2,976
Depreciation and Amortisation	(505)	(635)	(709)	(756)	(831)
Operating Profit	1,279	1,460	1,519	1,829	2,145
Net financing income/(costs)	(150)	(127)	(167)	(198)	(209)
Forex and Related Gains	-	-	-	-	-
Provisions	-	-	-	-	-
Other Income	-	-	(130)	-	-
Other Expenses	-	-	-	-	-
Net Profit Before Taxes	1,129	1,333	1,223	1,631	1,936
Taxes	(29)	(26)	(31)	(41)	(48)
Minority Interests	(3)	(22)	(8)	(8)	(9)
Net profit available to shareholders	1,097	1,285	1,183	1,583	1,879
Dividends	(460)	(460)	(460)	(460)	(564)
Transfer to Capital Reserve	-	-	-	-	-
	12/09A	12/10A	12/11E	12/12E	12/13E
Adjusted Shares Out (mn)	230.0	230.0	230.0	230.0	230.0
CFPS (SAR)	6.98	8.44	8.26	10.20	11.82
EPS (SAR)	4.77	5.59	5.15	6.88	8.17
DPS (SAR)	2.000	2.000	2.000	2.000	2.450
	12/09A	12/10A	12/11E	12/12E	12/13E
Growth					
Revenue Growth	16.7%	18.1%	14.2%	14.3%	13.4%
Gross Profit Growth	14.5%	15.6%	10.1%	17.0%	15.0%
EBITDA Growth	18.3%	17.4%	6.4%	16.0%	15.1%
Operating Profit Growth	13.3%	14.1%	4.1%	20.4%	17.3%
Net Profit Growth	12.2%	17.2%	-7.9%	33.7%	18.7%
EPS Growth	12.2%	17.2%	-7.9%	33.7%	18.7%
	12/09A	12/10A	12/11E	12/12E	12/13E
Margins					
Gross profit margin	40.3%	39.5%	38.1%	39.0%	39.5%
EBITDA margin	30.4%	30.2%	28.1%	28.6%	29.0%
Operating Margin	21.8%	21.1%	19.2%	20.2%	20.9%
Pretax profit margin	19.2%	19.2%	15.4%	18.0%	18.9%
Net profit margin	18.7%	18.5%	14.9%	17.5%	18.3%
	12/09A	12/10A	12/11E	12/12E	12/13E
Other Ratios					
ROCE	13.6%	13.9%	12.2%	12.7%	12.5%
ROIC	19.1%	17.2%	15.1%	14.6%	14.8%
ROE	24.4%	22.3%	18.6%	22.0%	22.2%
Effective Tax Rate	2.6%	2.0%	2.6%	2.5%	2.5%
Capex/Sales	20.9%	30.4%	35.7%	27.1%	25.0%
Dividend Payout Ratio	41.9%	35.8%	38.9%	29.1%	30.0%
	12/09A	12/10A	12/11E	12/12E	12/13E
Valuation Measures					
P/E (x)	18.1	15.5	16.8	12.6	10.6
P/CF (x)	12.4	10.2	10.5	8.5	7.3
P/B (x)	3.7	3.2	3.0	2.6	2.2
EV/Sales (x)	4.1	3.6	3.3	3.0	2.7
EV/EBITDA (x)	13.4	11.8	11.9	10.5	9.4
EV/EBIT (x)	18.6	16.9	17.4	14.9	13.1
EV/IC (x)	2.9	2.5	2.2	1.9	1.7
Dividend Yield	2.3%	2.3%	2.3%	2.3%	2.8%

Source: Company data, Al Rajhi Capital

EPS to decline in 2011 as a result of impairment loss

Strong revenue growth above 14% in 2011

Operating margin to improve by at least 100bps in 2012

High multiples are justified by the company's strong growth



Expanding balance sheet
reflecting aggressive expansion

Balance Sheet (SARmn)	12/09A	12/10A	12/11E	12/12E	12/13E
Cash and Cash Equivalents	508	247	300	309	800
Current Receivables	455	614	740	891	1,026
Inventories	1,219	1,299	1,479	1,642	1,847
Other current assets	-	-	-	-	-
Total Current Assets	2,182	2,160	2,519	2,842	3,673
Fixed Assets	7,049	8,636	10,874	12,567	14,302
Investments	963	958	891	891	891
Goodwill	793	793	793	793	793
Other Intangible Assets	-	-	-	-	-
Total Other Assets	-	24	38	38	38
Total Non-current Assets	8,805	10,411	12,596	14,290	16,025
Total Assets	10,987	12,571	15,116	17,132	19,698
Short Term Debt	396	546	934	934	934
Accounts Payable	963	1,253	1,397	1,501	1,334
Accrued Expenses	-	-	-	-	-
Dividends Payable	-	-	-	-	-
Other Current Liabilities	82	79	104	104	104
Total Current Liabilities	1,440	1,878	2,435	2,539	2,372
Long-Term Debt	3,981	4,301	5,763	6,546	7,851
Other LT Payables	-	-	-	-	-
Provisions	166	206	232	232	232
Total Non-current Liabilities	4,147	4,507	5,995	6,778	8,083
Minority interests	17	52	60	68	77
Paid-up share capital	1,150	2,300	2,300	2,300	2,300
Total Reserves	4,233	3,834	4,325	5,448	6,867
Total Shareholders' Equity	5,383	6,134	6,625	7,748	9,167
Total Equity	5,400	6,185	6,686	7,816	9,244
Total Liabilities & Shareholders' Equity	10,987	12,571	15,116	17,132	19,698

Debt increased but remains
within reasonable level

Ratios	12/09A	12/10A	12/11E	12/12E	12/13E
Net Debt (SARmn)	3,869	4,600	6,397	7,171	7,985
Net Debt/EBITDA (x)	2.17	2.20	2.87	2.77	2.68
Net Debt to Equity	71.7%	74.4%	95.7%	91.7%	86.4%
EBITDA Interest Cover (x)	11.9	16.6	13.4	13.1	14.2
BVPS (SAR)	23.40	26.67	28.81	33.69	39.86

Cashflow Statement (SARmn)	12/09A	12/10A	12/11E	12/12E	12/13E
Net Income before Tax & Minority Interest	1,129	1,333	1,223	1,631	1,936
Depreciation & Amortisation	505	635	709	756	831
Decrease in Working Capital	163	49	(164)	(210)	(507)
Other Operating Cashflow	37	38	33	(41)	(48)
Cashflow from Operations	1,835	2,055	1,800	2,136	2,211
Capital Expenditure	(1,227)	(2,104)	(2,825)	(2,449)	(2,566)
New Investments	(484)	-	-	-	-
Others	-	(84)	1	-	-
Cashflow from investing activities	(1,711)	(2,189)	(2,823)	(2,449)	(2,566)
Net Operating Cashflow	124	(134)	(1,023)	(314)	(354)
Dividends paid to ordinary shareholders	(381)	(456)	(516)	(460)	(460)
Proceeds from issue of shares	-	-	-	-	-
Effects of Exchange Rates on Cash	-	-	-	-	-
Other Financing Cashflow	9	(98)	(219)	-	-
Cashflow from financing activities	170	(84)	1,115	322	845
Total cash generated	294	(217)	93	9	491
Cash at beginning of period	253	508	247	300	309
Implied cash at end of year	547	290	340	309	800

High capex due to recent
expansions mainly in poultry

Ratios	12/09A	12/10A	12/11E	12/12E	12/13E
Capex/Sales	20.9%	30.4%	35.7%	27.1%	25.0%

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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