Jarir Marketing Co.

Investment Update

Rising competition & changing consumer behavior to pressure margins in the medium term; 5.5% DY is amongst the highest in sector

Rising number of brick & mortar and e-commerce establishments have resulted in increased competition and are forcing Jarir to make price cuts, which are impacting margins and profitability. Moreover, consumer demand is adversely affected by rising living expenses, high interest rates and new entertainment avenues. Demand for high margin stationary, school and office supplies is facing a slowdown due to increasing digitalization. The aforementioned headwinds were reflected in the Q1-24 results, where company posted lower than consensus earnings due to weaker sales and gross margins. That said, after retreating 21.6% over the last 12 months' the company offers one of the highest dividend yields of 5.5% for 2024 and trades at a 15.8% discount to its historical PE. We maintain our 'Overweight' rating on the stock with a revised price target of SAR 16.5/share.

Q1-24 results fell short of expectations due to lower sales and margin attrition: Jarir reported net income of SAR 219mn in Q1-24, down 11.5% and 19.3% Y/Y and Q/Q, respectively. The result was 15.9% and 14.5% below our and consensus estimates. The deviation is primarily attributable to lower than estimated sales (-6% deviation) and lower gross margins (-30bps deviation). The Y/Y drop in sales is owed to decline in e-commerce sales as consumers preferred to make in store purchases after BNPL was introduced. Overall e-commerce sales dropped by 28% Y/Y in Q1-2024. Gross margins for the company receded by 79bps Y/Y to 11.1%, as company went for price cuts to maintain market share in increasingly competitive market.

Competitive pressures mount; forcing discounts that are impacting margins: Rising number of brick & mortar and e-commerce establishments have resulted in increased competition in the Saudi retail landscape. In such backdrop, Jarir had to reduce product prices (especially for smartphones) in order to maintain market share, which resulted in further contraction in margins. Q1-24 gross and operating margin declined by 79bps and 77bps Y/Y to 11.1% and 9.0%, respectively. Where management has not confirmed if it will continue with the current policy of price reductions, we retain lower margins in our working in the medium term and expect 61bps and 21bps Y/Y reduction in gross margins in 2024 and 2025 respectively. We see margins beginning to revert to mean in 2026 (GPM +23bps Y/Y).

Consumer demand affected by rising living expenses, high interest rates and new spending avenues: Increasing cost of living, house rents, education, food, healthcare and basic utilities 'electricity & telecommunication' is constraining discretionary consumer spending. Moreover, consumer behavior and spending patterns are changing; more discretionary spending is being channeled towards new avenues like, concerts, sports events etc. Further impacting shopping budgets is the increased cost of consumer financing and mortgages, thanks to multi-decade high interest rates. High interest rates and inflation are likely to keep demand under some pressure over the next 12-18 months, until price pressures and borrowing costs ease.

Demand for high margin stationary, school and office supplies facing a slowdown due to increasing digitalization: The back to school season with more sales of high margin stationary and school supplies continues to face slowdown, due to growing digitalization. Office supplies segment is also experiencing a downtrend due to the digital transformation from paper based products to digital products like digital note pads, smart pens, interactive white boards, cloud services and Artificial intelligence. This weakness in demand is clearly visible in Q1-24 results, where the wholesale and corporate contract sales dropped by 25% Y/Y. This segment is likely to continue to face headwinds as digitalization is expected to grow further.

Revenue and earnings growth to remain muted in the medium term: After two years of muted growth, Jarir saw its revenues grow by 12.8% Y/Y in 2023, however this increase was mainly coming from the Buy Now Pay Later (BNPL) sales, and was at the expense of margins. If we exclude the impact of BNPL sales from 2023 topline, revenues were largely flat over 2020-23. Overall, we forecast revenues to grow at 2.3% CAGR over 2023-28 primarily driven by store expansions and small increase in revenue per store. We have built in two store additions in 2024, and beyond 2024 we assume three annual store additions in our estimates, which corresponds to total count reaching 84 by 2028. We estimate net income to post a five year CAGR of 3.4%, and gross and operating margins to revert to 12.1% and 10.4% respectively by 2028 (from 11.1% and 9.0% in Q1-24).

Recommendation	**Overweight**
Target Price (SAR)	**16.5**
Upside / (Downside)*	**28.3%**

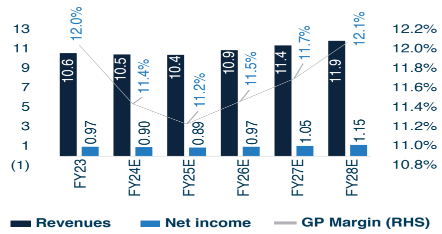
Source: Tadawul *prices as of 28th of May 2024

Key Financials

SARmn (unless specified)	FY23	FY24E	FY25E	FY26E
Revenue	10,595	10,459	10,411	10,888
Growth %	12.8%	-1.3%	-0.5%	4.6%
Net Profit	973	901	889	968
Growth %	0.3%	-7.4%	-1.3%	8.8%
EPS	0.81	0.75	0.74	0.81

Source: Company reports, Aljazira Capital

Fig 1: Profitibility trend (SAR bn)



Source: Company reports, Aljazira Capital

Key Ratios

	FY23	FY24E	FY25E	FY26E
GP Margin	12.0%	11.4%	11.2%	11.5%
Net Margin	9.2%	8.6%	8.5%	8.9%
P/E (x)	19.2	17.1	17.4	15.9
P/B (x)	10.6	8.5	8.3	8.1
EV/EBITDA (x)	15.8	13.7	13.9	12.8
Dividend Yield	5.3%	5.5%	5.5%	6.0%

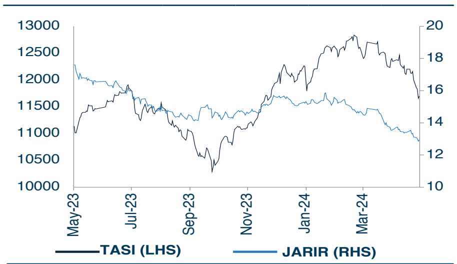
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (SAR bn)	15.5
YTD%	-17.4%
52 weeks (High)/(Low)	17.6/12.9
Share Outstanding (mn)	1200.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Bloomberg, Aljazira Capital

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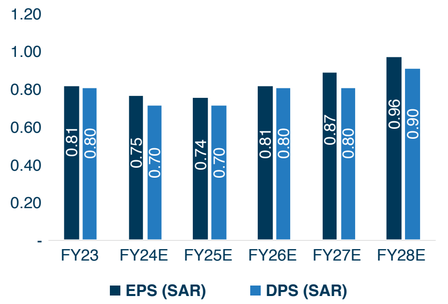
Strong dividend yield which is backed by robust debt free balance sheet and discount to past multiple supports investment case: Jarir offers one of the highest dividend yields in the sector, that limits the downside risk in the stock price in our view. Robust free cash flow generation, low capital intensive business, and almost debt free balance sheet helps the company sustain robust payouts, despite store additions. The chairman in a recent interview guided that the company will continue the high dividends. We estimate 2024/25E DY at a healthy 5.5/5.5% respectively. At 2024E PE 17.1x Jarir trades at a 15.8% discount to historical PE average of 20.5x.

Investment thesis: Our view on Jarir is supported by the company's expansion plans, healthy return profile (2024E ROE 50.4%) and strong dividend yield (2024E DY 5.5%). Moreover, we see Jarir as a good demographic play (63% of Saudi's are under age 30, and Saudi has one of the highest net incomes in the world with GDP per capita USD 59,065). However, we acknowledge that competitive pressures, especially from increasing stores & online establishments and new entertainment avenues would keep earnings growth and margins under pressure in the medium term.

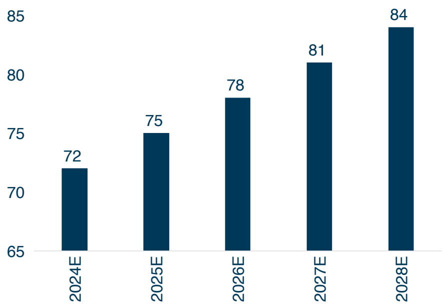
Valuation: We value Jarir assigning 50% weight to DCF (2.5% terminal growth and 8.3% WACC), while we assign 50% weight to PE (19.0x based on FY24E EPS). We expect the company to post net income of SAR 901/889mn in FY24/25 (down 7.4/1.3% Y/Y), the company trades at FY24E forward PE of 17.1x. We maintain our "**Overweight**" recommendation on Jarir, with a revised down TP of **SAR 16.5/share**.

Fig 2: EPS and DPS



Source: Company reports, AlJazira Capital

Fig 3: No.of stores



Source: Company reports, AlJazira capital

Valuation Summary	Fair value	Weights	Weighted Fair Value
DCF	18.7	50%	9.4
P/E	14.3	50%	7.1
Recommended Target Price (SAR/share)			16.5
Expected Capital Gain			**28.3%**

Key Financial Data

Amount in SAR mn, unless otherwise specified	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Income statement								
Revenues	9,088	9,392	10,595	10,459	10,411	10,888	11,369	11,855
Y/Y	**-2.3%**	**3.3%**	**12.8%**	**-1.3%**	**-0.5%**	**4.6%**	**4.4%**	**4.3%**
Cost of Sales	(7,859)	(8,104)	(9,319)	(9,262)	(9,242)	(9,640)	(10,039)	(10,424)
Gross profit	**1,229**	**1,287**	**1,276**	**1,196**	**1,169**	**1,248**	**1,330**	**1,431**
General and Administrative exp	(127)	(132)	(136)	(128)	(122)	(122)	(122)	(121)
Selling and marketing expenses	(141)	(194)	(167)	(148)	(142)	(146)	(150)	(154)
Other income	100	57	73	54	58	65	72	80
Operating profit	**1,061**	**1,019**	**1,045**	**975**	**963**	**1,045**	**1,130**	**1,236**
Y/Y	**-3.6%**	**-4.0%**	**2.6%**	**-6.7%**	**-1.2%**	**8.5%**	**8.2%**	**9.4%**
Financial charges	(42)	(41)	(43)	(45)	(46)	(46)	(47)	(49)
Profit before zakat	**1,019**	**978**	**1,002**	**930**	**917**	**998**	**1,083**	**1,187**
Zakat	(27)	(8)	(29)	(28)	(28)	(31)	(33)	(36)
Net income	**992**	**970**	**973**	**901**	**889**	**968**	**1,050**	**1,151**
Y/Y	**-1.1%**	**-2.2%**	**0.3%**	**-7.4%**	**-1.3%**	**8.8%**	**8.4%**	**9.7%**
EPS (SAR)	**8.27**	**0.81**	**0.81**	**0.75**	**0.74**	**0.81**	**0.87**	**0.96**
DPS (SAR)	**8.00**	**0.80**	**0.80**	**0.70**	**0.70**	**0.80**	**0.80**	**0.90**
Balance sheet								
Assets								
Cash & bank balance	432	526	50	452	491	508	540	572
Other current assets	1,636	1,808	2,161	1,962	1,943	2,028	2,113	2,196
Property & Equipment	1,083	1,015	995	998	1,006	1,015	1,024	1,034
Other non-current assets	961	908	905	842	868	886	898	919
Total assets	**4,112**	**4,257**	**4,110**	**4,255**	**4,307**	**4,436**	**4,575**	**4,721**
Liabilities & owners' equity								
Total current liabilities	1,633	1,696	1,572	1,660	1,662	1,732	1,804	1,875
Total non-current liabilities	711	760	767	777	783	794	808	826
Paid -up capital	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Statutory reserves	394	394	-	90	113	127	155	179
Other reserve	(64.9)	(93.8)	(105.9)	(105.9)	(105.9)	(105.9)	(105.9)	(105.9)
Retained earnings	240	301	677	633	655	689	714	747
Total owners' equity	1,769	1,802	1,772	1,818	1,862	1,910	1,963	2,020
Total equity & liabilities	4,112	4,257	4,110	4,255	4,307	4,436	4,575	4,721
Cashflow statement								
Operating activities	1,428	999	689	1,361	1,075	1,130	1,227	1,329
Investing activities	24	122	(65)	(199)	(198)	(207)	(216)	(225)
Financing activities	(1,116)	(1,027)	(1,098)	(760)	(838)	(906)	(979)	(1,072)
Change in cash	336	94	(474)	402	39	17	32	32
Ending cash balance	**432**	**526**	**50**	**452**	**491**	**508**	**540**	**572**
Key fundamental ratios								
Liquidity ratios								
Current ratio (x)	1.3	1.4	1.4	1.5	1.5	1.5	1.5	1.5
Quick ratio (x)	0.5	0.6	0.4	0.6	0.6	0.6	0.6	0.6
Profitability ratios								
GP Margin	13.5%	13.7%	12.0%	11.4%	11.2%	11.5%	11.7%	12.1%
Operating Margins	11.7%	10.8%	9.9%	9.3%	9.3%	9.6%	9.9%	10.4%
EBITDA margin	13.4%	12.6%	11.6%	10.9%	10.8%	11.2%	11.7%	12.1%
Net Margins	10.9%	10.3%	9.2%	8.6%	8.5%	8.9%	9.2%	9.7%
Return on assets	24.5%	23.2%	23.3%	21.5%	20.8%	22.1%	23.3%	24.8%
Return on equity	56.9%	54.8%	54.0%	50.4%	48.1%	51.4%	54.3%	57.9%
Market/valuation ratios								
EV/sales (x)	2.6	1.9	1.8	1.5	1.5	1.4	1.4	1.3
EV/EBITDA (x)	19.6	15.3	15.8	13.7	13.9	12.8	11.8	10.9
EPS (SAR)	8.3	0.8	0.8	0.8	0.7	0.8	0.9	1.0
BVPS (SAR)	14.7	1.5	1.5	1.5	1.6	1.6	1.6	1.7
Market price (SAR)*	196.8	15.0	15.6	12.9	12.9	12.9	12.9	12.9
Market-Cap (SAR mn)	23,616.0	18,000.0	18,696.0	15,432.0	15,432.0	15,432.0	15,432.0	15,432.0
Dividend yield	4.0%	5.1%	5.3%	5.5%	5.5%	6.0%	6.5%	7.1%
P/E ratio (x)	23.8	18.6	19.2	17.1	17.4	15.9	14.7	13.4
P/BV ratio (x)	13.3	10.0	10.6	8.5	8.3	8.1	7.9	7.6

Source: Company Reports, AJC Research

الجزيرة كابيتال
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RESEARCH DIVISION

AlJazira Capital, the investment arm of Bank AlJazira, is a Shariaa Compliant Saudi Closed Joint Stock company and operating under the regulatory supervision of the Capital Market Authority. AlJazira Capital is licensed to conduct securities business in all securities business as authorized by CMA, including dealing, managing, arranging, advisory, and custody. AlJazira Capital is the continuation of a long success story in the Saudi Tadawul market, having occupied the market leadership position for several years. With an objective to maintain its market leadership position, AlJazira Capital is expanding its brokerage capabilities to offer further value-added services, brokerage across MENA and International markets, as well as offering a full suite of securities business.

RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer