Modern Mills for Food Products Co.

Investment Update

Risk of subsidy changes to keep stock price performance in check; in base case we see notable decline in profits; update with "Neutral" rating

Modern Mills posted double-digit earnings growth of 16.0% Y/Y in Q3-25, due to 43.4% reduction in finance costs, despite stagnant revenues and lower operating profit/margins. We believe that capacity additions could drive the revenues at 8.5% CAGR over FY24–29e to reach SAR 1,507mn, however, in our base case scenario on subsidy restructuring, we expect earnings to move down significantly. Amongst the various post deregulation operating scenarios, partial removal of subsidy with no increase in retail price of flour is the most probable scenario due to almost no inflationary impact. In this backdrop, we expect operating margins to decline from 25.3% in 2025E to 21.1/15.8/14.4% and net margin to decline from 22.3% in 2025E to 18.4/13.7/12.7% in 2026/2027/2028, respectively. We forecast net profit to decline from SAR 228mn in 2025E to SAR 204/172mn in 2026/2027, respectively. The aforementioned earnings imply 2028e PE of 15.8x against local food & beverage sector's median TTM PE of 19.5x. That said, if government continued with the current structure for another few years earnings would beat our base estimates by 28/79/100% to reach SAR 261/307/350mn in 2026/27/28 and stock prices might move up sizably. We update coverage on Modern Mills with "Neutral" rating with a TP of SAR 37.9/share, implying an upside of 12.2%.

Company posted a double-digit growth in earnings in Q3-25 despite stagnant revenues and lower gross margins, due to decline in finance costs: Modern Mills reported 0.8% Y/Y growth in revenues to reach SAR 254mn by Q3-25. This growth was led by 10%+ expansion in the flour small packs segment, even as Feed business segment was impacted (10% decline) due to passing of commodity price decrease to customers. This shift in mix and pricing pressure weighed on profitability, with gross/operating margins compressing by 50/200bps to 36.8/25.3%, respectively. Despite margin pressure, robust performance of the flour small-packs segment underscores resilience in the core retail franchise, while the feed segment remains challenged by commodity pass-through dynamics. Nevertheless, absence of amortization of loan transaction cost helped lower finance costs, enabling net income to rise 16% Y/Y to SAR 56mn, highlighting the company's ability to defend bottom-line growth amid mixed operating conditions.

Amongst the various post deregulation operating scenarios, partial removal of subsidy with no increase in retail price of flour is the most probable scenario due to almost no inflationary impact: Milling companies currently enjoy a subsidized operating framework with fixed wheat cost set at SAR 180 per ton (from General Food Security Authority) and flour price set at SAR 500 per ton (for bulk packaging); this arrangement was supposed to end in July-2025. However, the company has not yet received any official notice from GFSA regarding changes to the current subsidized pricing policy. The likely scenarios under which these companies might operate thereafter are as follows, (1) complete abolishment of current subsidy mechanism, which might push net margins into single digits, however earnings might see limited contraction due to doubling of revenues owing to 3.5x flour price increase, (2) full continuation of current subsidy structure, (3) partial subsidy removal with small increase in retail price of flour and (4) partial subsidy removal over few years with no increase in retail price of flour. We believe scenario number 4 (our base case) to be most probable given that it has almost no impact on CPI inflation, and scenario three to be second most probable given minimal inflationary impact. In the following paragraphs we highlight arguments against scenario one and two.

Arguments against full removal of subsidy (scenario 1): We highlight two reasons for the government to not fully remove subsidy on wheat, (1) Food has a substantial weight of 21.4% in CPI basket – while wheat, wheat flour and related bakery products have a weight of more than 2.5% within the Food sub head, hence complete removal of subsidy might more than triple the retail prices of flour which would have a substantial impact on CPI inflation (+100-150bps annualized impact), and (2) fiscal savings from subsidy removal are quite minimal given that the total subsidy amount is ~SAR 3.5bn or roughly 0.27% of total government expenditure of SAR 1,285bn (2025).

Recommendation	Neutral
Target Price (SAR)	37.9
Upside / (Downside)*	12.1%

Source: Tadawul *prices as of 24th of Nov 2025

Key Financials

in SAR mn, (unless specified)	FY24	FY25E	FY26E	FY27E
Revenues	1,000	1,023	1,112	1,256
Growth %	6.6%	2.3%	8.7%	12.9%
Gross Profit	373	372	351	330
Growth %	8.0%	-0.4%	-5.5%	-6.2%
Oper. profit	259	259	235	199
Growth %	2.2%	0.0%	-9.4%	-15.3%
Net Income	209	228	204	172
Growth %	3.3%	9.3%	-10.4%	-16.1%
EPS	2.5	2.8	2.5	2.1
DPS	2.0	2.0	2.0	1.5

Source: Company reports, Aljazira Capital Research

Scenario analysis

	No subsidy no price limit	Full subsidy	Partial subsidy & sale price increase	Partial subsidy & no sale price increase
EPS 2028E	2.04	4.28	3.05	2.14
PE	16.6	7.9	11.1	15.8
Blended TP	35.0	69.4	51.7	37.9
Upside	3.7%	105.4%	52.9%	12.1%

Source: Company, AlJazira Capital research

Key Ratios

	FY24	FY25E	FY26E	FY27E
Gross Margin	37.3%	36.3%	31.6%	26.2%
Oper Margin	25.9%	25.3%	21.1%	15.8%
Net Margin	20.9%	22.3%	18.4%	13.7%
ROE	79.4%	69.3%	48.5%	34.4%
ROA	16.0%	16.9%	15.0%	12.5%
P/E (x)	16.1	12.1	13.5	16.1
P/B (x)	12.8	8.4	6.6	5.5
EV/EBITDA (x)	12.0	10.3	11.3	12.7
Dividend Yield	4.9%	5.9%	5.9%	4.4%

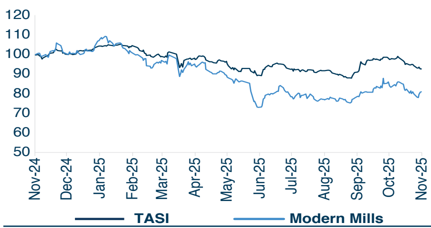
Source: Company reports, Aljazira Capital Research

Key Market Data

Market Cap (SAR bn)	2.7
YTD%	-20.1%
52 weeks (High)/(Low)	44.8/29.6
Share Outstanding (mn)	81.8

Source: Company reports, Aljazira Capital Research

Price Performance



Source: Company, AlJazira Capital research

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Arguments against continuation of current subsidy structure (scenario 2): On the other hand, our view against continuation of subsidy in full (at current levels) is supported by the following two factors, (1) under the current pricing structure modern mills enjoys much higher operating margins of 25.9% (2024), as compared 2.5% for global millers, and 11% for listed food and beverage producers, despite much less value addition; hence there is space for rationalization of margins and (2) government has significantly reduced subsidies on other basic food items such as Chicken and poultry, and raised fuel (diesel and petrol) prices to bring them close to region/global average.

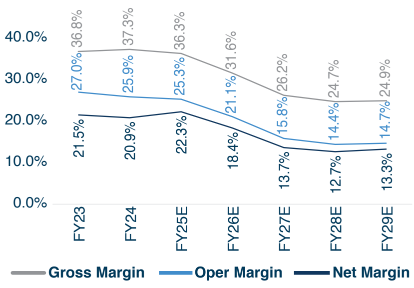
Sizable decline in earnings is expected in our base case; on our revised estimates modern mills trades at 2028e PE of 15.8x vs Saudi Food & Beverage sector TTM median PE of 19.5x: In our base case we see sizable reduction in profitability over the next three years. We expect government to keep prices of flour at current SAR 500 per ton but reduce subsidy by SAR 15 per ton in each quarter starting from Q1-26. In this backdrop, we expect operating margins to decline from 25.3% in 2025E to 21.1/15.8/14.4% and net margin to decline from 22.3% in 2025E to 18.4/13.7/12.7% in 2026/2027/2028, respectively. We forecast net profit to decline from SAR 228mn in 2025E to SAR 204/172/175mn in 2026/2027/2028, respectively. The aforementioned earnings imply 2028e PE of 15.8x against local food & beverage sectors median TTM PE of 19.5x.

A temporary extension in subsidy can rally stock price: If government continues with the current structure for another few years, 2026/27/28e operating margins will exceed our base estimates by 5.3/11.2/13.1ppts and earnings would beat our base estimations by 28/79/100% to reach SAR 261/307/350mn. This might trigger a stock rally given that implied 2028e PE would decline to 7.6x. That said we highlight that in the long run government is moving the economy towards more deregulation. Hence profits and margins are likely to decline over the long run.

AJC View and Valuation: Modern mills has delivered double-digit earnings growth in Q3-25 due to lower finance expenses. We see the company delivering 8.5% sales CAGR over 2024-29, however we see substantial decline in earnings in our base case (no increase in flour price amidst staggered increase in wheat price by GFSA). Current high operating margins (compared to other food & beverage companies) support discontinuation of existing subsidy structure, while adverse inflationary affects of full subsidy removal warrant that subsidy and price controls cannot be fully abolished. In our base, we forecast net profit to decline from SAR 228mn in 2025E to SAR 204/172/175mn in 2026/2027/2028, respectively. The aforementioned earnings imply 2028e PE of 15.8x against local food & beverage sectors median TTM PE of 19.5x. Note that due to the underlying risk facing the current subsidy structure, milling companies trade at a median TTM PE of 10.4x, which implies 50% discount to F&B sector average.

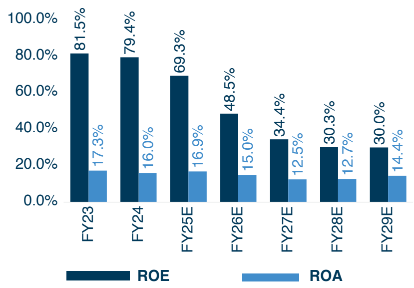
We value the company using 50% weightage to DCF (WACC = 8.1% and terminal growth = 2.5%) and 50% weightage to P/E multiple of 19.0x for FY30e EPS (discounted to Dec-26), to arrive at a blended TP of **SAR 37.9 per share**, implying an upside of 12.1%. Thus, we update our coverage with "**Neutral**" recommendation on the company.

Fig 1: Margins to move sizably down



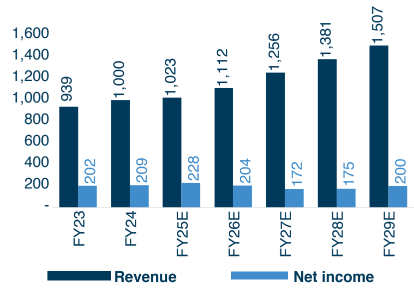
Source: Company, AlJazira Capital Research

Fig 2: ROE and ROA trend



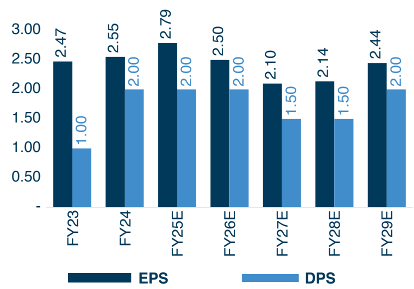
Source: Company, AlJazira Capital Research

Fig 3: Revenues and net income



Source: Company, AlJazira Capital Research

Fig 4: EPS and DPS



Source: Company, AlJazira Capital Research

Valuation Methodology	TP (SAR)	Weight	Weighted TP
DCF	SAR 38.2	50%	19.1
P/E	SAR 37.6	50%	18.8
Blended TP			**37.9**
Upside/(Downside) potential			**12.1%**

Source: AlJazira Capital Research

Key Financial Data

Amount in SARmn, unless otherwise specified	FY23	FY24	FY25E	FY26E	FY27E	FY28E	FY29E	FY30E
Income statement								
Revenues	939	1,000	1,023	1,112	1,256	1,381	1,507	1,626
Y/Y	**-4.03%**	**6.57%**	**2.29%**	**8.69%**	**12.93%**	**9.94%**	**9.18%**	**7.84%**
Cost	(593)	(627)	(651)	(761)	(926)	(1,039)	(1,132)	(1,217)
Gross profit	**346**	**373**	**372**	**351**	**330**	**341**	**376**	**408**
Gross margin (%)	**36.8%**	**37.3%**	**36.3%**	**31.6%**	**26.2%**	**24.7%**	**24.9%**	**25.1%**
Selling & distribution expense	(29)	(49)	(55)	(57)	(63)	(69)	(75)	(80)
General & administration expense	(63)	(65)	(58)	(60)	(67)	(73)	(79)	(85)
Operating profit	**254**	**259**	**259**	**235**	**199**	**199**	**222**	**244**
Y/Y	**-5.9%**	**2.2%**	**0.0%**	**-9.4%**	**-15.3%**	**0.0%**	**11.4%**	**10.1%**
Operating margin (%)	**27.0%**	**25.9%**	**25.3%**	**21.1%**	**15.8%**	**14.4%**	**14.7%**	**15.0%**
EBITDA	**312**	**319**	**315**	**285**	**247**	**246**	**268**	**289**
Financial charges	(44)	(48)	(29)	(27)	(24)	(21)	(18)	(15)
Income before zakat	**209**	**212**	**234**	**210**	**176**	**180**	**205**	**231**
Zakat	(7)	(3)	(6)	(6)	(5)	(5)	(6)	(6)
Net income	**202**	**209**	**228**	**204**	**172**	**175**	**200**	**225**
Y/Y	**-13.39%**	**3.34%**	**9.32%**	**-10.37%**	**-16.05%**	**1.85%**	**14.44%**	**12.44%**
Net margin (%)	**21.5%**	**20.9%**	**22.3%**	**18.4%**	**13.7%**	**12.7%**	**13.3%**	**13.8%**
EPS (SAR)	**2.5**	**2.5**	**2.79**	**2.50**	**2.10**	**2.14**	**2.44**	**2.75**
DPS (SAR)	**1.0**	**2.0**	**2.00**	**2.00**	**1.50**	**1.50**	**2.00**	**2.00**
Balance sheet								
Assets								
Cash & equivalent	112	183	159	106	109	118	138	169
Other current assets	130	133	122	135	161	175	187	199
Total current assets	**242**	**316**	**281**	**242**	**270**	**293**	**325**	**369**
Property plant & equipment	704	778	869	926	907	889	872	855
Right of use assets	221	207	198	194	190	187	183	179
Total assets	**1,169**	**1,304**	**1,352**	**1,367**	**1,373**	**1,374**	**1,385**	**1,407**
Liabilities & owners' equity								
Short term loans	54	30	82	77	73	68	64	60
Trade payables	41	53	53	61	76	84	90	97
Other current liabilities	99	113	106	108	111	114	117	120
Total current liabilities	**195**	**195**	**240**	**247**	**260**	**266**	**271**	**277**
Lease liabilities – non-current	232	221	210	206	202	198	194	190
Long term loans	490	617	564	484	404	324	244	164
Total non-current liabilities	**727**	**846**	**783**	**699**	**614**	**530**	**446**	**363**
Share capital	82	82	82	82	82	82	82	81
Reserves	166	181	247	339	417	495	585	686
Total owners' equity	**248**	**263**	**329**	**421**	**498**	**577**	**667**	**767**
Total equity & liabilities	**1,169**	**1,304**	**1,352**	**1,367**	**1,373**	**1,374**	**1,385**	**1,407**
Cashflow statement								
Operating activities	236	276	294	279	235	239	261	282
Investing activities	(56)	(107)	(136)	(103)	(26)	(25)	(25)	(24)
Financing activities	(186)	(98)	(182)	(228)	(207)	(206)	(216)	(227)
Change in cash	(6)	71	(24)	(53)	3	9	21	32
Ending cash balance	**112**	**183**	**159**	**106**	**109**	**118**	**138**	**170**
Liquidity ratios								
Current ratio (x)	1.2	1.6	1.2	1.0	1.0	1.1	1.2	1.3
Quick ratio (x)	0.7	0.7	0.5	0.5	0.6	0.7	0.7	0.7
Profitability ratios								
Gross profit margin	36.8%	37.3%	36.3%	31.6%	26.2%	24.7%	24.9%	25.1%
Operating margin	27.0%	25.9%	25.3%	21.1%	15.8%	14.4%	14.7%	15.0%
Net profit margin	21.5%	20.9%	22.3%	18.4%	13.7%	12.7%	13.3%	13.8%
Return on assets	17.3%	16.0%	16.9%	15.0%	12.5%	12.7%	14.4%	16.0%
Return on equity	81.5%	79.4%	69.3%	48.5%	34.4%	30.3%	30.0%	29.3%
Leverage ratio								
Debt / equity (x)	2.2	2.5	2.0	1.3	1.0	0.7	0.5	0.3
Market/valuation ratios								
EV/sales (x)	NA	3.8	3.18	2.90	2.50	2.20	1.95	1.73
EV/EBITDA (x)	NA	12.0	10.32	11.31	12.70	12.37	10.97	9.75
Market-Cap	NA	3,367	2,766	2,766	2,766	2,766	2,766	2,766
P/E ratio (x)	NA	16.1	12.13	13.53	16.12	15.83	13.83	12.3
P/BV ratio (x)	NA	12.8	8.40	6.57	5.55	4.79	4.15	3.61
DY (%)	NA	4.9%	5.9%	5.9%	4.4%	5.0%	5.7%	6.4%

Source: Company, AlJazira Capital Research

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RESEARCH DIVISION

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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