

**Healthy topline growth on recovery in aviation sector and a robust non-airline business, margins under pressure**

Saudi Airlines Catering Co. (Catering) posted a net profit of SAR 57.1mn in Q1-23, a growth of 61.8% Y/Y. The net profit was below AJC's and market estimates of SAR 73.4mn and SAR 84.5mn, respectively. The deviation from our estimate was primarily attributed to a lower-than-expected gross margin and higher OPEX to sales ratio. Revenue grew to SAR 521.6mn (+32.2% Y/Y) in line with our estimate of SAR 500.8mn. The gross margin stood at 27.3%, below our estimate of 30.7%. We downgrade our recommendation on catering to "Neutral", while keeping the TP unchanged at SAR 91.0/share.

- Catering's net profit surged 61.8% Y/Y to SAR 57.1mn in Q1-23 but missed AJC's and consensus estimates of SAR 73.4mn and SAR 84.5mn, respectively. The lower-than-expected GP margin resulted in lower net income than our expectation. OPEX to sales was also on the higher side vs. our estimates as well as compared to Q1-22. On a Q/Q basis, net income fell 46.7% due to contraction in gross margin in Q1-23 and a positive impact in Q4-22 from reversal of impairment over investment in associate and termination of lease.
- Revenue jumped 32.2% Y/Y to SAR 521.6mn, in line with our estimate of SAR 500.8mn. The revenue growth was driven by the increase in the number of flights coupled with higher sales from remote sites and railways catering. Sequential growth in the topline was mainly led by non-aviation business.
- Catering's gross profit rose 38.3% Y/Y to SAR 142.6mn supported by healthy revenue growth. The gross margin expanded 122bps Y/Y to 27.3% but was lower than our estimate of 30.7% and 30.1% recorded in the previous quarter.
- Operating profit increased 41.4% to SAR 65.2mn, below our estimate of SAR 84.2mn. OPEX increased 35.8% Y/Y, while OPEX to sales increased to 14.8% from 14.4% in Q1-22, coming higher than our estimate.

**AJC view:** Catering continued to record strong revenue growth Q1-23, as the aviation business recovers, while non-aviation keeps the growth. The company's topline now stands close to the pre-covid level. However, the recovery in margins was not in line with the recovery in revenue. We believe that the company's costs will continue to feel pressure from inflation in coming quarters as well, thus keeping margins below the pre-COVID level. However, the recovery in number of flights operating and expected non-airline business growth amid higher number of visitors for Hajj and Umrah this year would support the growth. Additionally, the launch of the new airline Riyadh Air is another potential growth factor for the company. We expect the company to pay a higher dividend this year with an improvement in profits. FY23E dividend yield is estimated to be at 2.8% (SAR 2.50/share) at the current price. The stock is currently trading at a P/E of 23.0x and EV/EBITDA of 14.6x based on our FY23 estimates. We downgrade our recommendation to "Neutral" on Catering with an unchanged TP of SAR 91.0/share.

### Results Summary

SARmn	Q1-22	Q4-22	Q1-23	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
Revenue	394.6	508.0	521.6	32.2%	2.7%	4.1%
Gross Profit	103.1	152.7	142.6	38.3%	-6.6%	-7.1%
<i>Gross Margin</i>	<i>26.1%</i>	<i>30.1%</i>	<i>27.3%</i>	-	-	-
EBIT	46.1	98.2	65.2	41.4%	-33.6%	-22.6%
Net Profit	35.3	107.1	57.1	61.8%	-46.7%	-22.3%
EPS	0.43	1.31	0.70	-	-	-

Source: Company Reports, Aljazira Capital

<b>Recommendation</b>	<b>Neutral</b>
<b>Target Price (SAR)</b>	<b>91.0</b>
<b>Upside / (Downside)*</b>	<b>1.4%</b>

Source: Tadawul \*prices as of 22<sup>nd</sup> of May 2023

### Key Financials

SARmn (unless specified)	FY21	FY22	FY23E	FY23E
Revenue	1212	1818	2246	2370
Growth %	30.9%	49.9%	23.6%	5.5%
Net Income	14.1	257	320	342
Growth %	NM	NM	24.5%	6.9%
EPS	0.17	3.14	3.90	4.17

Source: Company reports, Aljazira Capital

### Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	27.4%	28.4%	28.9%	29.0%
Net Margin	1.2%	14.1%	14.2%	14.4%
ROE	1.6%	28.2%	31.6%	30.8%
P/E (x)	HIGH	23.9	23.0	21.5
P/B (x)	7.3	6.5	6.8	6.4
EV/EBITDA (x)	29.2	15.2	14.6	14.2
Dividend Yield	0.0%	0.7%	2.8%	3.7%

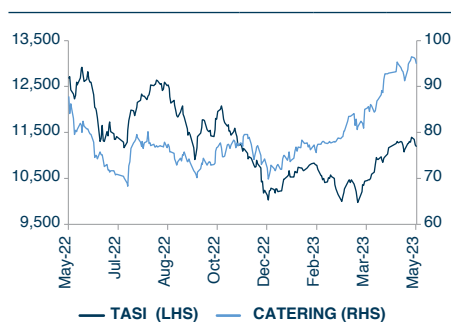
Source: Company reports, Aljazira Capital

### Key Market Data

Market Cap(bn)	7.3
YTD%	17.3%
52-week (High)/(Low)	96.9/67.7
Share Outstanding (mn)	82.0

Source: Company reports, Aljazira Capital

### Price Performance



Source: Argaam, Aljazira Capital

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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.

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