الجزيرة كابيتال
ALJAZIRA CAPITAL الجزيرة للأسواق المالية

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SAL

SAL Saudi Logistics Services Company

Initiation Report

A dominating player in a market with high growth potential

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SAL Saudi Logistics Services Company (SAL): Initiate with "Overweight" rating and a TP of SAR 146/share

SAL is a leading player in cargo handling and logistic solutions services in Saudi Arabia with 95% market share in cargo handling, across the airports at which the company operates, with a total 722,000 tons cargo volume handled in FY22. Saudi government's National Transportation and Logistics Strategy, and National Industrial Development and Logistics Program of Vision 2030 are focused on investments in and development of logistical infrastructure to make the country a regional logistics hub. Given SAL's strong market position, long standing experience and expertise in the sector, it is likely to capitalize on expected growth cargo handling volume and overall growth in logistics solutions market in the Kingdom. The company's expansion plan and financial strength to implement the capacity expansion reinforce its ability to make the most out of upcoming opportunities. Moreover, SAL also has room for expanding its operations into passenger handling, warehousing, and fulfillment services. We initiate our coverage on SAL with an "Overweight" rating and a TP of SAR 146/share.

A key beneficiary of expected demand growth in cargo handling volume and overall: Saudi Arabia's cargo handling market is expected to grow at a 14.1% CAGR from 0.8mn tons in FY22 to 2.3mn ton in FY30. In FY22, SAL held 95% of the market share across the airports it operates with total cargo handling volume of 722,000 tons. Thus, the anticipated growth in cargo volume is likely to be directly reflected in SAL revenue. Moreover, the total logistics solutions market (11.0%), passenger ground services market (11.3%) and fulfilment market (13.1%) are also estimated to expand at double digit rates during the same period. Thus, overall conditions in the sector seem conducive and are expected to provide ample growth opportunities for the key market players such as SAL.

SAL's well defined expansion strategy aligns well with sector dynamics: Considering the upcoming growth in demand, SAL has a plan to invest around SAR 1.5bn in state-of-the-art cargo terminal facilities, such as additional fully automated cold storage facilities and other fully automated systems and cargo handling equipment. Additionally, the company plans to expand its warehousing capacity significantly by FY27 at Jeddah (770,000 tons, expected cost SAR 396mn), Riyadh (827,000 tons, SAR 410mn) and Dammam (252,000 tons, SAR 100mn). We expect SAL's topline growth will be driven by capacity expansion that will cater to rising demand. Thus, we forecast revenue CAGR of 14.8% during FY23-27E, growing from SAR 1.2bn in FY22 to SAR 2.4bn in FY27E. Subsequently, the company's net profit is also estimated to increase at CAGR of 18.9% to reach SAR 860.0mn in FY27E.

Healthy operating cash flows, comfortable balance sheet leverage and manageable working capital requirements support execution of expansion plan: SAL's cash flow from operations stood at SAR 556mn in FY22. The company's net debt to equity was 1.0x as of June 2023 and working capital requirements (9% of revenue in FY22) are easily met. Thus, we believe that the company has the financial strength to expand its capacity to match expected surge in demand.

Strong ROAE and dividend yield reflect good returns to shareholders: SAL posted ROAE of 35.6% during FY22. We expect ROAE to improve further due to the expected expansion of margins associated with healthy revenue growth. Moreover, we see a possibility of a high dividend payout in future in the range of 75-80%, despite expected capex requirements, due to robust FCF generation (FY22: SAR 475mn or SAR 5.9 per share). Based on our estimates for FY24E, the stock is expected to deliver a dividend yield of 4.9% at the IPO offer price of SAR 106 per share.

AJC view and valuation: Attractive prospects of Saudi cargo and logistics sector coupled with planned capacity expansion are expected to be the key factors for SAL's growth in the medium to long term. The company's healthy profitability level, sound financials and cash flow generating ability further strengthen the possibility of the company delivering robust performance. We value SAL with 50% weightage to DCF (risk free rate = 3.5%, terminal growth rate = 2.5%, WACC = 8.9%) and 25% each to P/E (19.0x) and EV/EBITDA (15.5x) valuation based on our FY24E estimates. The blended valuation indicates a fair value of **SAR 146.0 per share**, an upside of **37.7%** from IPO offer price. Thus, we initiate our coverage on the stock with an **"Overweight"** rating. However, lack of expected demand growth, inability to implement expansion plan, loss of market share to new players in the market are key downside risks for the company's valuation.

Recommendation	Overweight
Target Price (SAR)	146.0
Upside / (Downside)*	37.7%

*Upside from IPO offer price

Key Financials

SARmn (unless specified)	FY21	FY22	FY23E	FY24E
Revenue	962	1,223	1,434	1,705
Growth %	13.6%	27.1%	17.3%	18.9%
Gross Profit	486	591	761	908
Net Income	276	362	451	556
Growth %	15.9%	31.5%	24.5%	23.3%
EPS	3.44	4.53	5.64	6.95
DPS	2.97	3.81	4.51	5.21

Source: Company reports, Aljazira Capital

Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	50.5%	48.3%	53.0%	53.2%
Net Margin	28.6%	29.6%	31.5%	32.6%
ROE	31.2%	35.6%	40.4%	45.1%
ROA	9.0%	11.2%	13.6%	16.5%
P/E (x)	NM	NM	18.8	15.2
P/B (x)	NM	NM	7.3	6.5
EV/EBITDA (x)	NM	NM	14.4	12.2
Dividend Yield	NM	NM	4.3%	4.9%

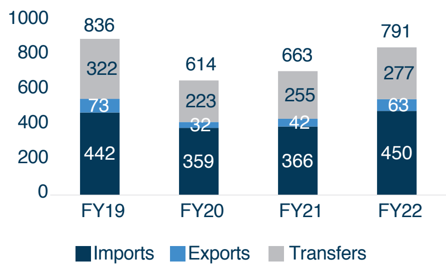
Source: Company reports, Aljazira Capital

Key Market Data

IPO price (SAR/share)	106.0
Share Outstanding (mn)	80.0
Market Cap at IPO price (SAR mn)	8.5

Source: Company reports, Aljazira Capital

KSA Cargo volumes ('000 tons)



Source: Company reports, Aljazira Capital

Company Overview

SAL Saudi Logistics Services Company (SAL) is a closed joint-stock company. The legal name of the Company was SAL Cargo Company Limited, prior to conversion to a closed joint stock company. The operations of the company were initially provided by Saudi Arabian Airlines Public Corporation ("Saudi Airlines Corporation") since its formation date and have existed for more than 70 years. By privatizing several of its strategic business units, notably the air cargo and ground handling division, Saudi Airlines Corporation created several subsidiaries. The privatization process was completed in 2008 with the commencement of the Saudi Airlines Cargo Company ("Saudia Cargo" or "SACC"). General warehousing of various goods, ground transportation of goods, ground management and supervision services in airports, ground service providers, loading and unloading of air cargo aircraft, authorized air cargo agencies, handling of goods and mail in air cargo, and logistics services are some of the company's primary business activities. GACA is largely responsible for regulating and supervising the company's operations. The company provides airside and landside cargo handling services as well as other airline support services, such as ramp handling, cargo handling, terminal handling, managing customs inspections, facility storage services, cold chain, escorting, road feeders, and screening services. The company also offers logistics solutions services, such as end-to-end solutions, unique projects, customs clearance, and warehousing. The company plans to offer passenger handling services in the future, which will include loading and unloading of passenger bags.

Source: IPO Prospectus

Valuation Summary

We value SAL with 50% weightage to DCF (risk free rate = 3.5%, terminal growth rate = 2.5%, WACC = 8.9%) and 25% each to P/E (19.0x) and EV/EBITDA (15.5x) valuation based on our FY24E estimates. The blended valuation indicates a fair value of **SAR 146.0 per share**, an upside of **37.7%** from IPO offer price. The DCF valuation implies an enterprise value of SAR 13.3bn and market value of SAR 12.4bn, translating into fair price of SAR 155.3 per share. Whereas relative valuation based on P/E (19.0x) and EV/EBITDA (15.5x) multiples yielded fair values of SAR 132.1 per share and SAR 141.0 per share, respectively. We applied multiples slightly at premium to our valuation for SGS due to better profitability and high growth potential.

IPO Offering Summary

SAL Logistics is floating 24.0mn shares, representing 30% of the company's share capital post offering, with a fully paid nominal value of SAR 10 per share. The IPO is divided into two tranches: one for institutional investors and the other for retail investors. A total of 24.0mn shares (100%) were offered to institutional investors. The book building process for institutional investors started from September 25 and ended on October 01. The institutional offering was 72.0x oversubscribed. In case of strong retail demand, the allocation to the institutional category would decrease to a minimum of 21.6mn, representing 90.0% of the offering's total shares. The retail offering, which was open from October 11-13, accounted for up to 10.0% (2.4mn shares) of the offer size. The retail offering was also oversubscribed at 16.1x. The company has set the IPO price at SAR 106 per share.

Structure of the company's shareholders pre- and post-offering

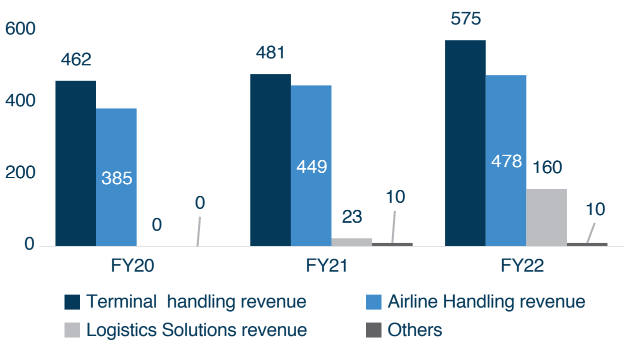
	Pre-Offering			Post-Offering		
	No. of Shares	Par Value (SAR)	Direct ownership	No. of Shares	Par Value (SAR)	Direct ownership
Saudi Airlines Corporation	56,000,000	560,000,000	70%	39,200,000	392,000,000	49%
Tarabot	24,000,000	240,000,000	30%	16,800,000	168,000,000	21%
The Public	-	-	-	24,000,000	240,000,000	30%
Total	**80,000,000**	**800,000,000**	**100%**	**80,000,000**	**800,000,000**	**100%**

Source: IPO Prospectus

Segmental Analysis – Terminal handling services the leading contributor to the topline, while Riyadh is the largest terminal in terms of revenue

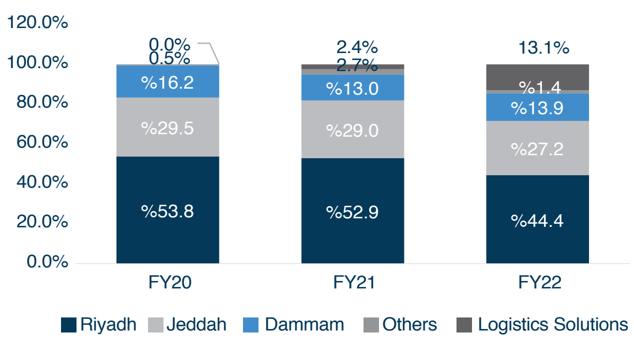
SAL's revenue included terminal handling revenue (47.0% of total revenue in FY22), airline handling revenue (39.1%), Logistic solutions revenue (13.1%) and other revenue (0.8%). Riyadh was the largest terminal in terms of revenue contribution (44.4% in FY22), followed by Jeddah (27.2%) and Dammam (13.9%).

Figure 1: Revenue by type (SAR mn)



Source: Company Prospectus, Aljazira Capital Research

Figure 2: Revenue by station (as % of total revenue)

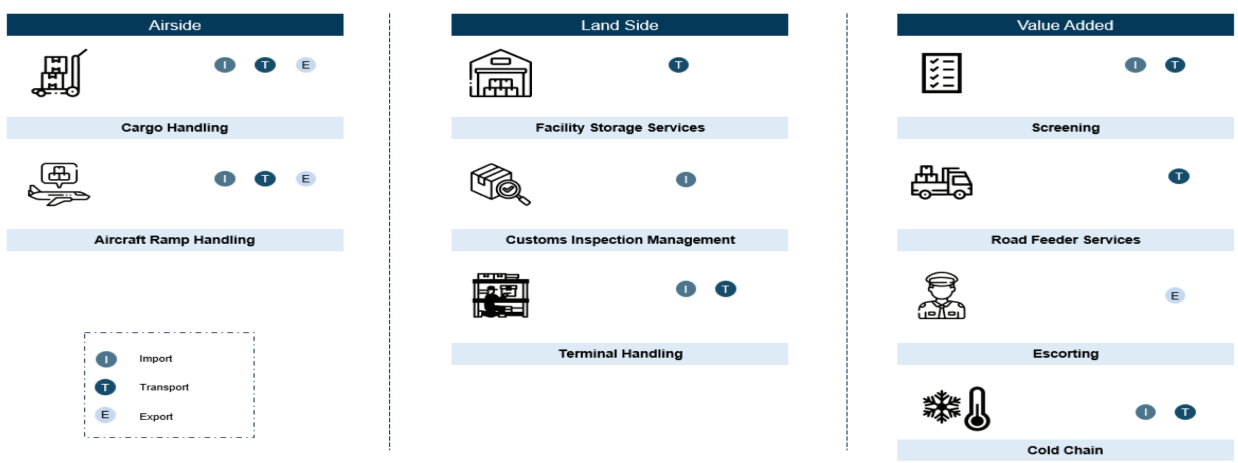


Source: Company Prospectus, Aljazira Capital Research

Terminal handling services revenue: Revenue from services rendered on the terminal side, mostly those connected to the handling and storage of cargo according to its kind, was created through terminal handling services. The increase in volumes (+13.1 thousand tonnes of imports and exports) was the main factor for the 2.9% Y/Y increase in terminal handling services income in FY21. As a result of higher volumes handled (+ 24.7 thousand tonnes) because of a resurgence in flight activity in KSA, the segment revenues increased by 23.7% Y/Y in FY22. The product mix and higher average revenue per KG recorded for General Cargo (which accounted for about 56% of total sales in FY22) also contributed to the Y/Y revenue rise in FY22.

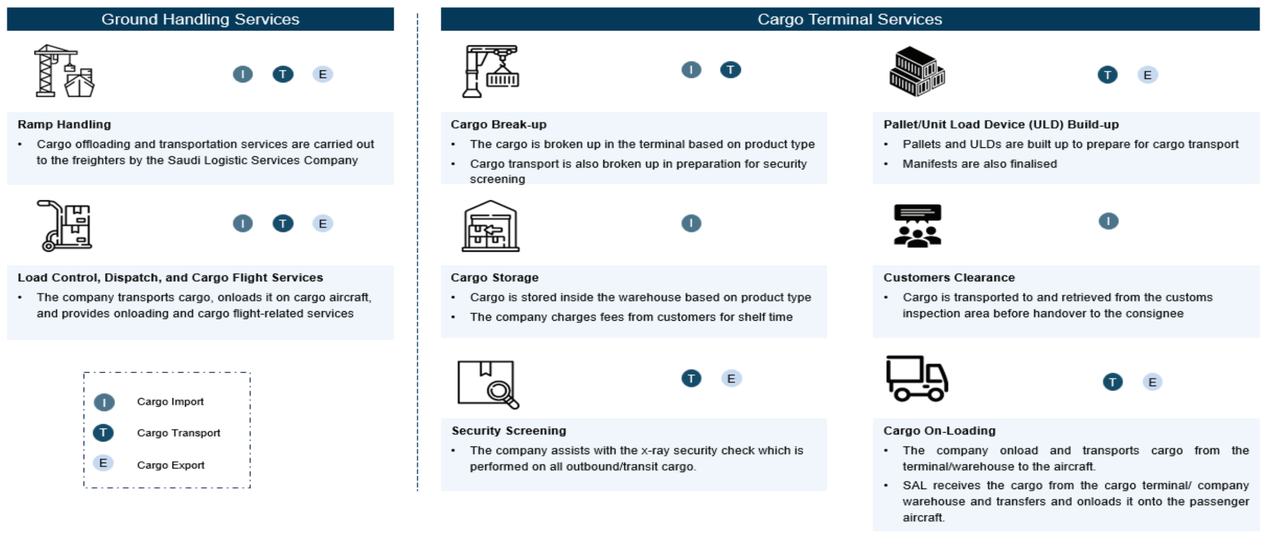
Airline handling services revenue: Revenue from airside and delivery services, which are mostly associated with ramp handling operations, was generated from airline handling services, also known as "Airside service". Normally, the airlines handle all types of cargo (export, transit in, transit out, and import). i) Higher overall volumes handled because of the historically negative impact of COVID-19 on flight activity; and ii) charging an amount of SAR 23.5mn to SACC in connection with domestic revenue recovery which was billed at once in FY21. These factors combined to lead to an increase in airline handling services revenue by 36.8% in FY21. The revenue for airline handling services increased by 10.5% Y/Y in FY22 in line with the higher volumes handled, primarily from transfer volumes, and the change in the domestic station recovery arrangement, which was previously based on a cost + 15% ratio and was changed in FY22 to a 60:40 combined loss/profit ratio, whereby SACC bears 60% of the combined losses/profits and SAL bears the remaining 40%.

Figure 3: Cargo Handling Services



Source: IPO Prospectus, Aljazira Capital Research

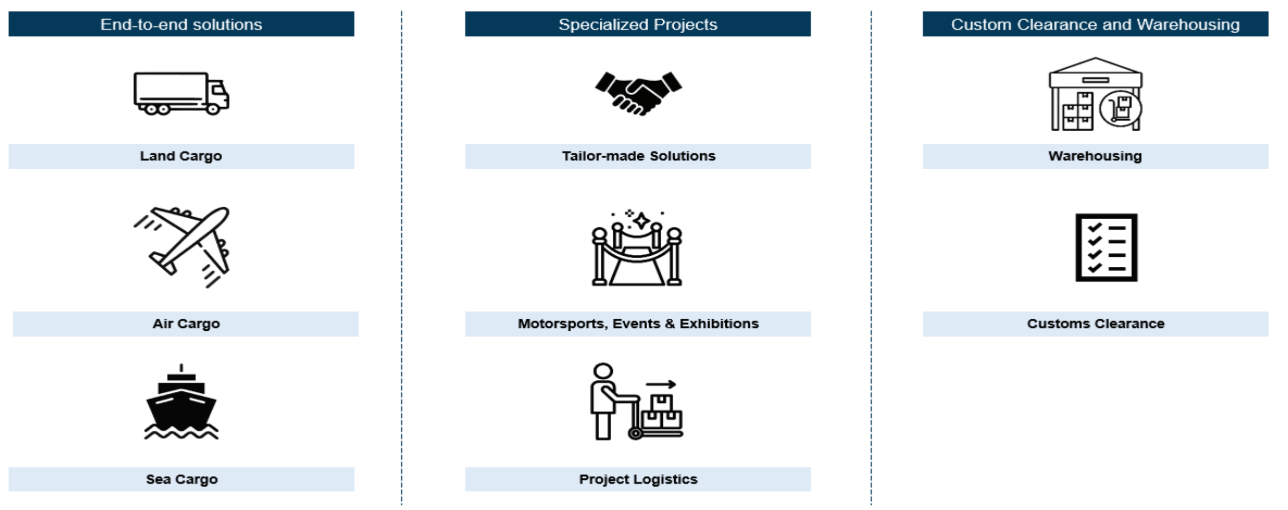
Figure 4. Ground Handling Services and Cargo Terminal Services for Inbound, Outbound and Transit/Transfer cargo.



Source: IPO Prospectus, Aljazira Capital Research.

Logistic solutions revenue: By focusing on their specific projects and demands, the Logistic Solutions segment, which was started in FY21 with sales reaching SAR 22.8mn, provided end-to-end third-party logistics solutions services to KSA governmental and semi-public entities. The offerings included warehousing, freight forwarding, customized solutions, and clearance of customs. Prior to the beginning of the Logistic Solutions segment, the company recorded SAR 9.5mn in ad hoc activities during the same year. Due to the ramp-up of this service line and the completion of projects with important customers, Logistic Solutions' revenue climbed to SAR 160.4mn in FY22.

Figure 5. Logistics solutions services



Source: IPO Prospectus, Aljazira Capital Research

Others revenue: Others revenue for FY21 totaled SAR 9.5mn and was primarily attributable to ad hoc operations before the introduction of Logistic Solutions. In FY22, other income totaled SAR 9.7mn and was primarily derived from two sources: i) office and space rental fees to various governmental agencies using the terminals, and ii) regulatory staff training of the company's vendors.

Riyadh and Jeddah are the major terminals of the company

The company has cargo terminals at key locations in the Kingdom, which includes the company's offices at these locations.

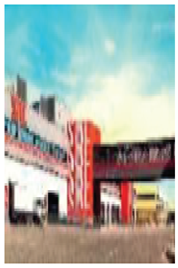
The company also leases facilities at 4 key locations and 14 Other International and Domestic Airports in the Kingdom. Revenue was mainly generated from operations in 3 stations Riyadh (44.4% of total revenue in FY22), Jeddah (27.2%) and Dammam (13.9%).

Figure 6: Details of the Key Facilities and Locations as of 31 December 2022

Medina

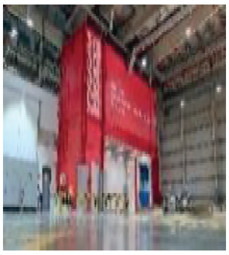
Fights handled (per day) +11	Capacity 5.5k tons
Annual Volume handled FY22 2k tons	Cargo terminal area (sqm) 1,900

Riyadh



Fights handled (per day) +159	Capacity 332k tons
Annual Volume handled FY22 358k tons	Cargo terminal area (sqm) 70,000

Jaddah



Fights handled (per day) +157	Capacity 352K tons
Annual Volume handled FY22 289k tons	Cargo terminal area (sqm) 33,500

Dammam

Fights handled (per day) +53	Capacity 160K tons
Annual Volume handled FY22 71k tons	Cargo terminal area (sqm) 34,000

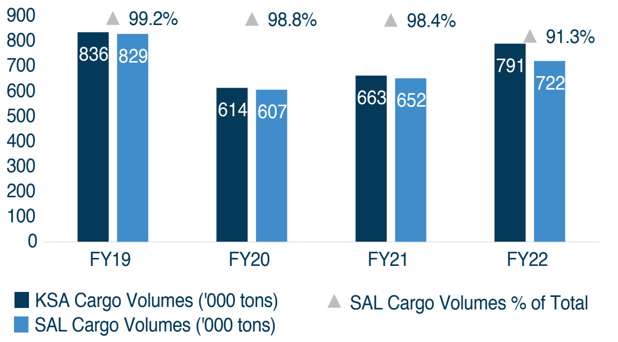
Source: IPO Prospectus, Aljazira Capital Research

Entrenched market position gives SAL an edge over new entrants/competitors

Anticipated rapid growth in the sector in line with Vision 2030 advantageous for the company

SAL is well-established in Saudi Arabia's cargo and logistics with operations at the four key locations and offerings at 18 regional and domestic airports in KSA. SAL consistently accounted for more than 90% of total cargo volumes handled in Saudi Arabia. By taking advantage of its unrivaled position in air cargo handling, the company will be able to use its industry knowledge, extensive market knowledge, and relationships to capitalize on the expected growth in domestic consumption and capture increased air cargo volumes, rapid e-commerce growth, and demand for third-party logistics services, including warehousing and fulfilment centers.

Figure 7: Cargo volumes ('000 tons)

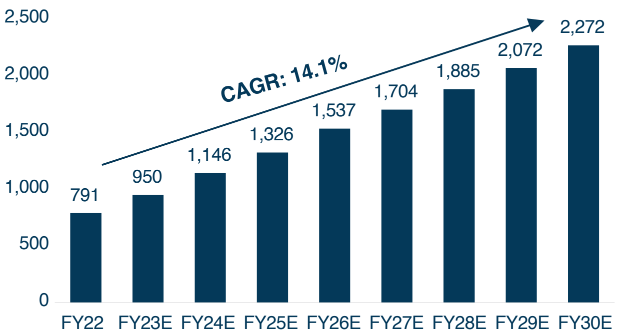


Source: Company Prospectus, Aljazira Capital Research

SAL expansion strategy in line with upcoming demand surge

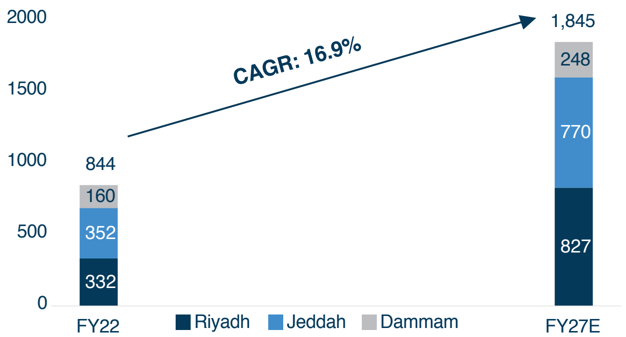
SAL's has laid out an extensive capacity expansion plan at its key terminals. The expansion plan aligns with the forecasted growth in the sector. Thus, the company is expected to maintain its leadership position in the growing market.

Figure 8: KSA cargo volumes forecast ('000 tons)



Source: Company Prospectus, Aljazira Capital Research

Figure 9: SAL's cargo handling capacity expansion ('000 tons)



Source: Company Prospectus, Aljazira Capital Research

Presence across the ground handling value chain

From unloading, handling, and supporting the supply cycle through transportation and loading, SAL is present along the entire ground handling value chain at all domestic airports in the Kingdom of Saudi Arabia. Additionally, it now manages 78,285 tons of e-commerce entering KSA via air. This indicates that the company is ready to capture opportunities across the subsegments of the business.

A broad clientele of government entities and international airlines under long-term contracts

The company has enduring partnerships with customers around the world. The company had agreements with 58 airline customers as of December 31, 2022. These agreements are generally signed for longer terms. The top 10 medium-long term contracts with clients of the company represent, directly and indirectly, approximately 33.3% of the company's business in total.

High barriers to new entrants favorable for the established players

SAL's operating market has an extremely high barrier to new entrants. Fulfilling regulatory requirements such as developing a large terminal as part of GACA's concession agreements will be a key challenge for a new player. Further, developing relationships with government entities (which SAL has developed over the period of 50 years) such as GACA, ZATCA, GDI and SFDA will be another challenging task for the new entrants.

Ready to tap opportunities with a strategically focused CAPEX and plans to increase presence across logistics value chain

Considering the Kingdom's Vision 2030 goal to establish KSA as a hub for global logistics, SAL has created a solid strategy that concentrates on expanding the capacity and developing infrastructure to cater anticipated high demand and increase presence across the various segments of the business.

A well-defined strategic plan with SAR 1.5bn investments for cargo handling capacity expansion and other infrastructure

SAL's current development plans include strategic investments worth SAR 1.5bn to increase total handling capacity to ~1.9mn tons per year, including inbound, outbound and transfer cargo; total warehouse space to ~169,000 sq. m.; and material handling system (MHS) capacity to 1,240 positions (aircraft storage containers used for cargo) by the end of Q1-27. This included increasing cargo handling capacity at the key terminals of Riyadh, Jeddah and Dammam.

Figure 10: Expansion plan

Terminal	Current Capacity (FY22)		Planned Capacity Volume (tons)	Expected cost SAR mn	Expected date of completion
	Area (sq. m)	Volume (tons)			
Riyadh	70,000	332,000	827,000	410.0	FY27
Jeddah	33,500	352,000	770,000	396.0	FY27
Dammam	34,000	160,000	248,000	100.0	FY25
Total	**137,500**	**844,000**	**1,845,000**	**906.0**	

Source: Company Prospectus, Aljazira Capital Research

Greater penetration in emerging and promising market for logistics solutions

According to Vision 2030, KSA's requirement for end-to-end logistical services is increasing, with a big emphasis on specialized government-related events and activities. For the extension of its value proposition for logistical solutions, the company has given priority to four sectors: (i) the public sector; (ii) the auto and aircraft parts sector; (iii) events and entertainment; and (iv) healthcare. SAL intends to introduce more efforts that focus on customer retention and market share, as well as broaden its product and service offerings, in order to obtain greater penetration in the logistics solutions industry.

Increasing passenger ground services to support ground handling of air cargo

SAL is in a position to increase its presence in passenger ground services. The company plans to collaborate with a top international ground handling company in order to facilitate the development of passenger ground services in KSA and to gain a sizable market share with the largest local and international low-cost carriers ("LCCs") in the Kingdom, in order to leverage the market growth.

Incorporating warehousing and fulfillment as an addition to the logistics value chain

The company's goal is to become the go-to partner for e-commerce warehousing and fulfillment services in KSA by offering state-of-the-art, functional facilities that are supported by technology solutions, integrated with partners (technology, first mile and last mile delivery, shipping and warehouse operators), and have a wide network and coverage throughout KSA.

KSA's cargo and logistics industry to witness a spike in demand

The COVID-19 pandemic's effects have caused two significant shifts in KSA's cargo and logistics business. Before COVID-19, belly cargo and freighters made up an equal portion of the cargo trade. However, because the passenger fleet's capacity was limited, existing airlines that run specific freighters began to handle more of the demand for cargo. Despite a steady recovery over the past two years, aviation freight traffic is still 13.6% below FY19 levels. Additionally, COVID-19's benefits sparked expansion in sectors including e-commerce and healthcare. E-commerce in the KSA is anticipated to continue growing at its current rate given the rapid pace of digitization and the forced shift in consumer behavior brought on by the epidemic. The healthcare market is expected to see strong recovery due to vaccination which lessens the risk of further lockdowns and social distancing measures. Healthcare and e-commerce have a high value proposition in the current logistics market.

KSA Cargo market

Prior to COVID-19 and the resulting disruptions, the KSA freight market had a volume of more than 836,205 tons (FY19). Over the past ten years, volumes have experienced fluctuations ranging from significant reversals to recoveries, including during the 2008 financial crisis, the 2012 trade recession, the 2017–2019 increase in oil prices that increased the cost of air freight, and the 2019 manufacturing slowdown. The COVID-19 pandemic caused additional disruption to the cargo business, which despite demonstrating notable resilience in comparison to the air passenger transport market saw cargo volume decline to 613,952 tons in FY20. Compared to a 50% decline in air passenger capacity, the global cargo capacity decreased by about 20%.

Between FY22-FY30, the cargo market in the KSA is predicted to expand at a CAGR of 14.1%, propelled by the country's expanding GDP and population, its increased production capacity, its increased reliance on e-commerce, and its strategic focus on attracting logistics leakage to its neighboring countries.

With a presence in all of the KSA's main airports, SAL is the largest provider of cargo handling services. In FY22, the company held roughly 95% of the market, according to SAL's records.

Figure 11: KSA Cargo Market Forecast (in Tons)

	2019	2020	2021	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	CAGR 2022-2030
Total	**836,205**	**613,952**	**663,090**	**790,534**	**950,491**	**1,145,551**	**1,325,825**	**1,536,578**	**1,704,359**	**1,885,129**	**2,072,197**	**2,272,454**	**14.1%**
Import	441,708	359,407	366,373	450,234	541,632	640,566	734,405	831,097	932,331	1,038,152	1,148,492	1,263,572	**13.8%**
Export	72,986	32,012	42,044	63,348	88,983	118,947	143,161	168,398	194,912	223,190	253,197	285,001	**20.7%**
Transit/ Transfer cargo*	321,511	222,533	254,673	276,952	319,876	386,038	448,259	537,083	577,116	623,787	670,508	723,881	**12.8%**

Source: Company Prospectus, Aljazira Capital Research, *- Includes transfer and transit cargo.

Very limited competition in KSA cargo handling market

SAL, which is present in all the main airports in Saudi Arabia, is the largest provider of cargo handling services in KSA as of FY21. SATS, the first foreign cargo handler to operate in Saudi Arabia, was the only rival at the time.

SATS is a global company specializing in providing specialized cargo handling and logistics services, as well as catering solutions in the aviation sector. In recent years, SATS has pursued a geographic expansion strategy through a combination of acquisitions and new partnerships to enhance its presence in Southeast Asia, the United Arab Emirates, and the Kingdom of Saudi Arabia.

Nevertheless, it is anticipated that SAL would maintain its market dominance in Saudi Arabia during the coming decade. The company anticipates keeping several foreign airlines as well as the major domestic carriers (Saudia, Saudia Cargo, etc.) as clients.

GACA, the country's single aviation regulatory body, issues license necessary for operation in Saudi Arabia. Currently, SAL possesses all licenses and certifications necessary to guarantee the efficient operation of cargo to and from Saudi Arabia.

Logistics Solutions market

In the KSA logistics market, maritime freight is the largest mode of transportation. It accounted for almost 90% of national trade in terms of volume and around 65% of national trade in terms of value in FY21. In terms of volume, air cargo accounts for around 1% of the nation's trade and about 21% of its value.

SAL has created integrated logistics services by utilizing its leadership in the industry of cargo handling services and the durability of its presence throughout the KSA. SAL wants to increase the value it offers, meet the logistical requirements of its clients, and aid in the expansion of the KSA as a hub for international logistics.

SAL identified four key segments as high priority in order to expand its value proposition within the current logistics market solutions: healthcare, arts, events and entertainment, automotive and aerospace, and the public sector.

Figure 12. Target market segments

Market segment	Market size	Expected CAGR until FY30
Healthcare	162,400 tons (FY21)	5.0%
Events and Entertainment	23,370 tons (FY21)	21.0%
High-value Aircraft Parts	4,900 tons (FY22)	9.0%
High-value Automotive Parts	1,100 tons (FY22)	3.3%

Source: Company Prospectus, Aljazira Capital Research

Passenger Ground Handling Market

The company is considering getting into the passenger handling business, concentrating on domestic low-cost carriers. The services offered by an airport include passenger-related activities (such as check-in, baggage services, boarding, and disembarkation) and aircraft-related activities (such as marshalling, pushback, towing, potable water provision, waste removal, refueling, baggage and catering loading).The performance of low-cost airlines in terms of total supply in the KSA has increased from 14% in FY13 to 22% in FY22, resulting in an average CAGR of 9.2%. This growth is related to the expansion of low-cost airlines in the KSA over the previous several years. A favorable macroeconomic outlook and prospects of recovery in the wake of the COVID-19 pandemic are likely to fuel organic passenger traffic growth in the KSA, which is anticipated to increase from 100mn passengers in FY19 to 158mn passengers by FY30, at a CAGR of 4%. Additionally, aspirations to position KSA as a worldwide hub for transit/transfer goods match with goals for the development of KSA as a global tourist destination for both leisure and business travelers, which might further support the organic market growth. By FY30, the GACA projects that 330mn people would travel by air.

Warehousing and Fulfilment Services Market

To meet the needs of KSA e-retailer customers, the company aims to develop warehousing, fulfillment, and last-mile delivery services. Short-term outsourcing capabilities will come from foreign partners with a local presence, and long-term insourcing will occur once sufficient scale of volumes have been reached.

Due to COVID-19 lockdown measures, e-commerce sales considerably rose, reaching SAR 32bn in FY21.Considering that 60% of the population is under the age of 30, and that mobile internet usage rates are above 75%, KSA Vision 2030 aspires to enhance the contribution of contemporary commerce and e-commerce to 80% of the retail sector by FY30. However, a lackluster logistics infrastructure, inadequate Arabic-language e-commerce content, and rigorous cross-border enforcement restrictions impede the growth of e-commerce.

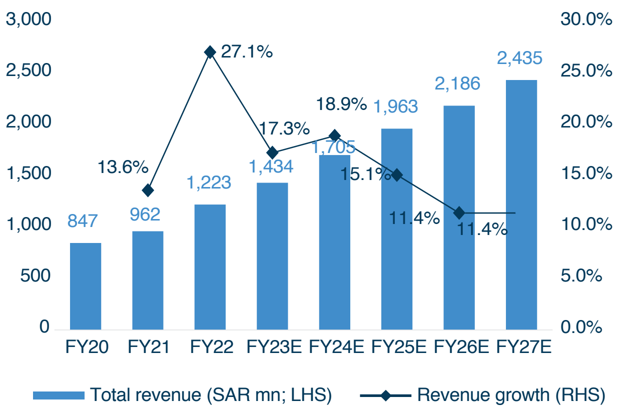
The population increase, the influx of new clients, the high per capita disposable income, and the high penetration of e-commerce are expected to drive the KSA e-commerce retail market's growth between FY22-30 at a CAGR of 13%. This will bridge the adoption gap that currently exists between the KSA and other developed economies, where the prevalence rate of e-commerce typically ranges between 15% and 35%.

A bet on expansion-led growth, sound financials, healthy profitability and dividend yield prospects

Surge in cargo handling volumes and capacity expansion to drive growth for SAL

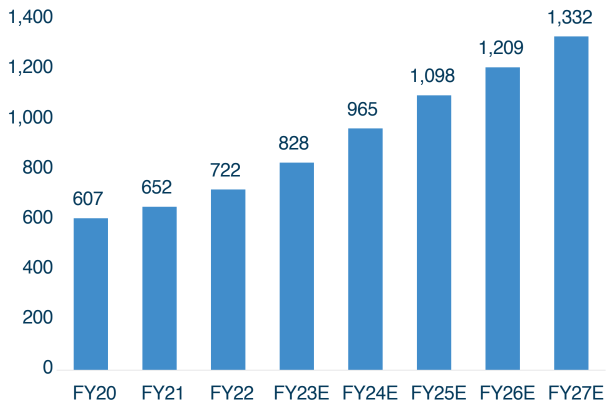
The expected growth in Saudi Arabia's cargo handling volumes bolstered by government initiatives to develop a regional cargo hub will reflect in higher cargo volumes for SAL. The volumes for SAL were up 10.6% in FY22. Going forward, cargo volumes are likely to see accelerated growth. Thus, we forecast the cargo volumes for SAL to rise at CAGR of 13.0% during FY23-27E. As a result, revenue is estimated to increase at CAGR of 14.8% during the same period. The topline growth will be well supported by the company's planned expansion of capacity at Jeddah, Riyadh and Dammam.

Figure 13: Total revenue (SAR mn)



Source: Company Prospectus, Aljazira Capital Research

Figure 14: SAL's cargo volume handled ('000 tons)

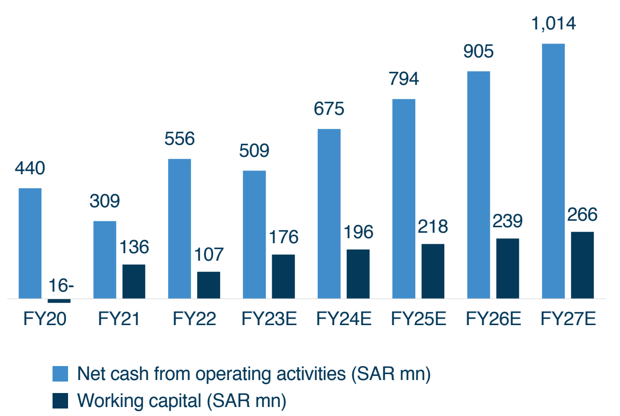


Source: Company Prospectus, Aljazira Capital Research

Financial strength underline's ability to tap upcoming growth opportunities

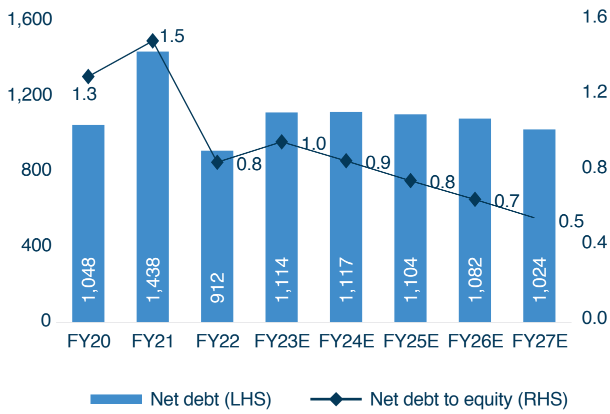
SAL's cash flow from operations is very robust and stood at SAR 556mn in FY22. Moreover, with the anticipated strong growth in revenue and improvement in profitability, we expect the company to continue to generate healthy cash flows in future. Additionally, the company's debt is also at moderate level with net debt to equity of 1.0x as of June 2023. Working capital requirements are also well within manageable limits (9% of revenue in FY22) for the company. Hence, we believe SAL is in a comfortable position to invest in upcoming growth opportunities.

Figure 15: Cash from operations and working capital (SAR mn)



Source: Company Prospectus, Aljazira Capital Research

Figure 16: Net debt (SAR mn) and net debt to equity

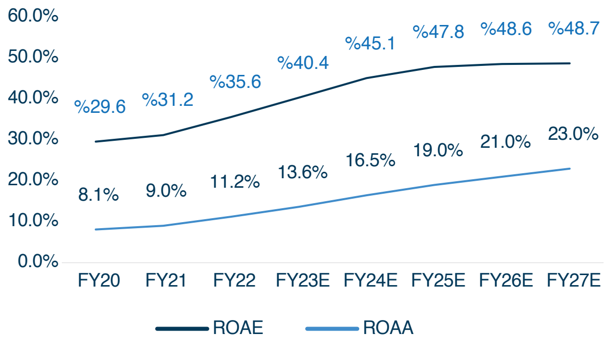


Source: Company Prospectus, Aljazira Capital Research

Robust return profile expected to improve further

SAL's ROAE and ROAA stood at 35.6% and 11.2%, respectively, in FY22. We expect ROAE and ROAA to improve further due to the expected expansion of margins associated with healthy revenue growth. Dupont analysis indicates ROAE expansion would be driven by continuous improvement in net margin coupled with growing asset turnover. This will more than compensate for the impact of the decrease in financial leverage due to the increase in equity.

Figure 17: ROAE and ROAA



Source: Company Prospectus, Aljazira Capital Research

Figure 18: Dupont analysis

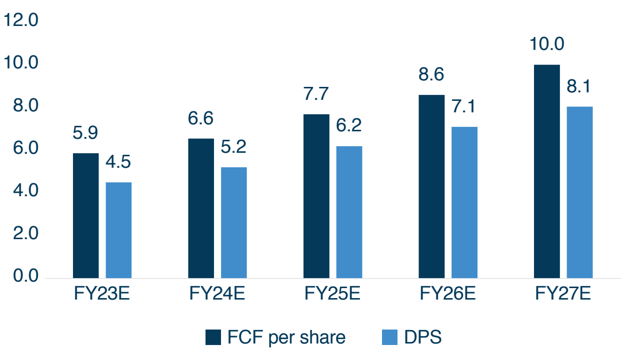
	FY20	FY21	FY22	FY23F	FY24F	FY25F	FY26F	FY27F
ROE	**29.6%**	**31.2%**	**35.6%**	**40.4%**	**45.1%**	**47.8%**	**48.6%**	**48.7%**
Net Margin	28.1%	28.6%	29.6%	31.5%	32.6%	33.8%	34.7%	35.3%
Asset Turnover	0.29	0.32	0.38	0.43	0.50	0.56	0.61	0.65
Financial Leverage	3.64	3.45	3.17	2.96	2.74	2.52	2.31	2.12

Source: Company Prospectus, Aljazira Capital Research

Healthy dividend yield driven by FCF generation bodes well for shareholders

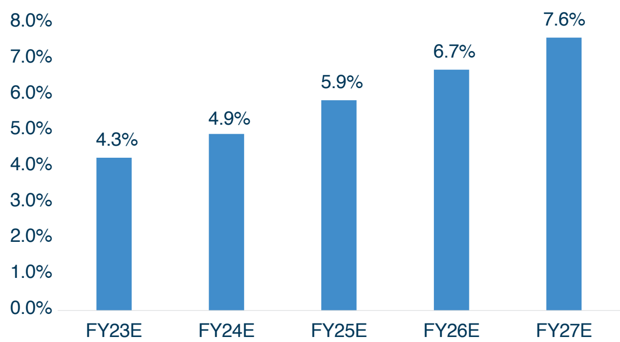
We see a possibility of a high dividend payout in future in the range of 75-80%, despite expected capex requirements, due to robust FCF generation (FY22: SAR 475mn or SAR 5.9 per share). Based on our estimates for FY24E, the stock is expected to deliver a dividend yield of 4.9% at the IPO offer price.

Figure 19: FCF per share and DPS (SAR)



Source: Company Prospectus, Aljazira Capital Research

Figure 20: Dividend yield



Source: Company Prospectus, Aljazira Capital Research

Key Risks

- SAL's inability to properly execute its expansion strategy, capitalize on the industries that are expected to grow, and contribute to the Kingdom's air cargo volume in the way and timescale that it intends. This can have a negative and significant impact on the company's performance in future.
- The company is highly dependent on SACC, any decrease in the volume of services provided to SACC at any given time, as well as any non-renewal or early termination of the agreement, will have a materially negative impact on the company.
- Inability of the company to match its services to the requirements of technologically advanced new airports, like the new KAIA airport or some of the current being obsolete due to modern technologies is another risk to the company.

Valuation Methodologies

DCF Valuation

We performed DCF valuation based on our forecasts for the next five years. We assumed risk free rate of 3.5%, a market risk premium of 6.5% and a beta of 1.0 to arrive at WACC of 8.9%. Terminal growth rate is assumed at 2.5%. Our valuation of SAL is based on DCF yielded an enterprise value of SAR 13.3bn and fair value to equity shareholders of SAR 12.4bn, which translated into a TP of **SAR 155.3 per share.**

SAR mn	FY23E	FY24E	FY25E	FY26E	FY27E
EBIT	540	648	750	838	940
Depreciation & Amortization	123	136	150	164	176
Change in working capital	-68	-21	-21	-22	-26
CFO	594	763	878	979	1,090
Capex	-124	-238	-262	-291	-288
FCFF	470	525	616	689	803
Discounting factor	1.0	0.9	0.8	0.8	0.7
Present value of FCFF	**463**	**476**	**517**	**536**	**581**
Sum of the PV					**2,573**
Terminal Value					14,876
PV of terminal value					10,771
Enterprise Value					**13,344**
Cash and cash equivalents					1,048
Debt					1,888
FV to common shareholders					**12,423**
No outstanding shares (mn)					80
Fair value per share					**SAR 155.3**

Terminal growth rate	Risk premium				
	5.5%	**6.0%**	**6.5%**	**7.0%**	**7.5%**
1.9%	160.7	150.5	141.4	133.3	126.0
2.2%	169.3	158.0	148.0	139.1	131.2
2.5%	178.9	166.3	155.3	145.5	136.9
2.8%	189.8	175.7	163.4	152.7	143.1
3.1%	202.3	186.3	172.6	160.6	150.1

Above is an illustration of sensitivity of our DCF valuation to the change assumptions of terminal growth rate (range: 1.9%-3.1%) and risk premium (5.5%-7.5%). The sensitivity analysis indicates valuation in the range between a minimum of SAR 126.0 per share (at terminal growth rate of 1.9% and risk premium of 7.5%) and a maximum of SAR 202.3 per share (at terminal growth rate of 3.1% and risk premium of 5.5%).

Relative valuation

We valued SAL using the relative valuation methodologies based on P/E and EV/EBITDA multiples applied to our FY24E estimates.

P/E Valuation:

All figures in SAR mn, unless specified	
P/E multiple	19.0x
Premium/discount	0%
Market value	10,569
Shares (mn)	80
Relative value (SAR/share)	**132.1**

EV/EBITDA Valuation:

All figures in SAR mn, unless specified	
EV/EBITDA multiple	15.5x
Premium/discount	0%
Enterprise value	**12,199**
Net debt	840
Employee end of service benefits	81
Market value	11,279
Shares (mn)	80
Relative value (SAR/share)	**141.0**

Blended Valuation

Valuation Summary	Fair Value	Weight	Weighted Average
DCF	155.3	50%	77.6
P/E	132.1	25%	33.0
EV/EBITDA	141.0	25%	35.2
Weighted average 12-month TP			**146.0**
IPO Offering Price (SAR /share)			106.0
Expected Capital Gain			**37.7%**

We assigned 50% weightage to DCF, and 25% each P/E and EV/EBITDA multiples. Based on the combined valuation, we arrived at a weighted average TP of **SAR 146/share.** This reflects an upside of 37.7% over the IPO offer price of SAR 106 per share. Thus, we initiate the stock with an **"Overweight"** rating.

Key upside and downside risks to valuation: Lack of expected demand growth, inability to implement expansion plan, loss of market share to new players in the market are key downside risks for the company's valuation. Whereas higher than expected demand generated due to government initiatives and faster completion of capacity expansion by the company are some upside risks to the valuation.

Key Financial Data

Amount in SAR mn, unless otherwise specified	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E	FY27E
Income statement								
Revenues	847	962	1,223	1,434	1,705	1,963	2,186	2,435
Y/Y		**13.6%**	**27.1%**	**17.3%**	**18.9%**	**15.1%**	**11.4%**	**11.4%**
Cost	(449)	(476)	(632)	(673)	(797)	(916)	(1,021)	(1,134)
Gross profit	**398**	**486**	**591**	**761**	**908**	**1,047**	**1,165**	**1,301**
Sales and distribution expenses	15	28	30	36	42	47	51	56
General and administrative expenses	135	137	147	201	237	271	300	331
Operating profit	**312**	**345**	**427**	**540**	**648**	**750**	**838**	**940**
Y/Y		**10.9%**	**23.5%**	**26.5%**	**20.0%**	**15.9%**	**11.6%**	**12.2%**
Finance expense	71	70	75	91	79	59	39	30
Income before zakat	**240**	**279**	**370**	**490**	**605**	**720**	**825**	**935**
Zakat	2	3	8	39	48	58	66	75
Net income	**238**	**276**	**362**	**451**	**556**	**662**	**759**	**860**
Y/Y		**15.9%**	**31.5%**	**24.5%**	**23.3%**	**19.1%**	**14.6%**	**13.3%**
Balance sheet								
Assets								
Cash & equivalent	715	492	940	696	619	560	496	471
Other current assets	291	723	411	681	736	783	821	862
Total current assets	1,005	1,215	1,351	1,377	1,355	1,343	1,317	1,333
Property plant & equipment	555	659	705	771	939	1,118	1,313	1,493
Other non-current assets	1,365	1,299	1,227	1,181	1,133	1,086	1,037	988
Total assets	**2,926**	**3,173**	**3,284**	**3,329**	**3,428**	**3,547**	**3,667**	**3,814**
Liabilities & owners' equity								
Total current liabilities	708	317	344	374	406	446	460	483
Total non-current liabilities	1,415	1,894	1,866	1,791	1,719	1,634	1,550	1,458
Paid -up capital	1	800	800	800	800	800	800	800
Additional capital contribution	468	-	-	-	-	-	-	-
Statutory reserves	0	28	64	109	165	231	231	231
Retained earnings	339	155	227	272	355	454	644	859
Total owners' equity	803	962	1,073	1,163	1,302	1,468	1,658	1,873
Total equity & liabilities	**2,926**	**3,173**	**3,284**	**3,329**	**3,428**	**3,547**	**3,667**	**3,814**
Cashflow statement								
Operating activities	440	309	556	509	675	794	905	1,014
Investing activities	(227)	(528)	282	(331)	(240)	(264)	(293)	(290)
Financing activities	502	(4)	(389)	(422)	(512)	(590)	(675)	(749)
Change in cash	715	(223)	448	(244)	(77)	(59)	(63)	(25)
Ending cash balance	**715**	**492**	**940**	**696**	**619**	**560**	**496**	**471**
Key fundamental ratios								
Liquidity ratios								
Current ratio (x)	1.4	3.8	3.9	3.7	3.3	3.0	2.9	2.8
Profitability ratios								
Gross profit margin	47.0%	50.5%	48.3%	53.0%	53.2%	53.3%	53.3%	53.4%
Operating margin	36.8%	35.9%	34.9%	37.6%	38.0%	38.2%	38.3%	38.6%
EBITDA margin	48.4%	47.3%	44.6%	46.4%	46.2%	46.0%	46.0%	46.0%
Net profit margin	28.1%	28.6%	29.6%	31.5%	32.6%	33.8%	34.7%	35.3%
Return on assets	8.1%	9.0%	11.2%	13.6%	16.5%	19.0%	21.0%	23.0%
Return on equity	29.6%	31.2%	35.6%	40.4%	45.1%	47.8%	48.6%	48.7%
Market/valuation ratios								
EV/sales (x)	NM	NM	NM	6.7	5.6	4.9	4.4	3.9
EV/EBITDA (x)	NM	NM	NM	14.4	12.2	10.6	9.5	8.5
EPS (SAR)	3.0	3.4	4.5	5.6	7.0	8.3	9.5	10.8
BVPS (SAR)	10.0	12.0	13.4	14.5	16.3	18.4	20.7	23.4
DPS (SAR)	-	2.97	3.81	4.51	5.21	6.21	7.11	8.06
Market price (SAR)*	NM	NM	NM	106	106	106	106	106
Market-Cap (SAR mn)	NM	NM	NM	8,480	8,480	8,480	8,480	8,480
P/E ratio (x)	NM	NM	NM	18.8	15.2	12.8	11.2	9.9
P/BV ratio (x)	NM	NM	NM	7.3	6.5	5.8	5.1	4.5
Dividend yield	NM	NM	NM	4.3%	4.9%	5.9%	6.7%	7.6%

Source: Company Prospectus, Aljazira Capital Research; *IPO offering price is taken as market price

الجزيرة كابيتال
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RESEARCH DIVISION

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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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