Equity Research report
SACO AB Equity
22 August 2024

Target Price: SAR63.0/share
Current Price: SAR74.1/share
Upside: -15% (+Div. Yield: 0.8%)
Rating: Neutral

Saudi Automotive Services Company (SASCO)

2Q earnings beat; Raise TP to SAR63 on network expansion

Stock data	
TASI ticker	4050
Mcap (SARmn)	5,187
Avg. Trd. Val (3m) (SARmn)	37.5
Free float	82.2%
QFI holding	8.3%
TASI FF weight	0.20%

Source: Bloomberg

Prices indexed to 100

Source: Bloomberg

- Fuel network expansion (30 new stations likely to be added in 2H24 and 40 in 2025) and higher throughput to drive topline growth; Gross margin may improve from 2025.
- Growing optimism about the fuel margin hike drove the stock price again, although there is no official confirmation yet.
- Post revision of our estimates and rolling forward valuation, we raise our TP to SAR63/sh., based on the DCF valuation. Despite a downside of ~15%, we remain Neutral on the stock due to the possibility of a margin hike (although timing remains uncertain).

Expanding fuel stations network with growing SASCO Palm stores: Over the last twelve months, SASCO added 45 fuel stations, with 22 of these added in 2Q24 alone, bringing the total to 562 stations by 2Q24. Further, in 3Q24 so far, the company has opened an additional 8 stations, reflecting an acceleration in expansion activities. Overall, on a conservative basis, we expect the total number of stations to reach 592 (previously 587) by 2024e, slightly lower than the management guidance of ~620 stations. We note that the rate of expansion can be further accelerated through franchise agreements. Moreover, SASCO continues to open new SASCO palm stores inside its operated stations, adding ~15 stores per quarter. SASCO plans to expand its Palm stores to 172 by 2024e (150 in 2Q24; 120 in 2023) and further to 400 in the next 5 years, enabling it to attract and serve more customers and diversify source of income.

Improvement in throughput on ramp up operation of renovated station: Throughput per station was robust in 2Q24, increasing by ~3% y/y compared to 0.8% y/y (on an average) over the 3Q23-1Q24 (~9% y/y decline in 2023). The growth was mainly driven by increased Diesel volume (+32% y/y). This also indicates that the impact of renovation and the ramp-up of new stations is diminishing, and the company is beginning to benefit from the renovated fuel stations in the form of higher throughput per station. This, along with its focus on improving efficiency, is likely to further enhance throughput going forward, in our view. Given the pickup in expansion activity along with a healthy improvement in throughput, we expect the revenue to grow by ~13% in 2024 (~10% earlier) and ~11% in 2025 (~8% earlier).

Figure 1: Key financial metrics

SARmn	2022a	2023a	2024e	2025e	2026e
Revenue	7,852	9,113	10,286	11,463	12,376
Revenue growth	*93%*	*16%*	*13%*	*11%*	*8%*
Gross profit	259	293	326	384	441
Gross profit margin	*3.3%*	*3.2%*	*3.2%*	*3.4%*	*3.6%*
EBITDA	366	513	589	717	774
Operating Profit	81	169	196	242	287
Net profit attributable to equity holders	75	105	53	77	117
Net profit margin	*1.0%*	*1.2%*	*0.5%*	*0.7%*	*0.9%*
EPS (SAR)	1.1	1.5	0.8	1.1	1.7
DPS (SAR)	0.9	1.1	0.6	0.8	1.3
P/E	69.0x	49.2x	97.3x	67.3x	44.2x

Source: Company data, GIB Capital

Kunal Doshi
+966-11-834 8372
Kunal.doshi@gibcapital.com

Margin to remain under pressure in 2024 before likely improvement from next year: SASCO's gross margin has been under pressure over the past few quarters, mainly due to higher upfront costs for refurbishing, increased government licensing fees, and a slow ramp-up of new stations. Accordingly, we revise our 2024e gross margin forecasts to 3.2% (3.6% earlier). Nonetheless, we expect a gradual improvement in gross margin going forward, reaching 3.4% and 3.6% by 2025e and 2026e, respectively, driven by ramping up of new/renovated stations, increased contributions of SASCO Palm stores (turned profitable, expecting to generate 4-5% gross margin) and operating leverage.

Recap of 2Q24 result: Revenue increased by 11.2% y/y, reaching SAR2,487mn (in-line with our estimate), mainly driven by an increase in fuel stations and a hike in Diesel prices. However, gross profit rose at a slower pace, rising by 1.5% y/y, with gross margin narrowing down by 30bps y/y, missing our gross margin estimate of 3.2%. Subsequently, increased OPEX (+9.6% y/y) pushed operating profit lower by 3.3% y/y, falling short of our estimate. Nonetheless, the company reported lower-than-expected financial costs, mainly due to capitalization of some costs. This, coupled with higher other income resulted in a better-than-expected earnings growth (+14.8% y/y).

Figure 2: 2Q24 result summary

SARmn	2Q24	2Q23	y/y %	1Q24	q/q %	GIBC est.	Variance %
Revenues	**2,487**	**2,236**	**11.2%**	**2,453**	**1.4%**	**2,473**	**0.6%**
Cost of Goods	2,410	2,161	11.5%	2,377	1.4%	2,393	0.7%
Gross Profit	**77**	**75**	**1.5%**	**76**	**0.2%**	**80**	**-4.1%**
Opex	31	28	9.6%	28	8.3%	28	10.7%
Operating Profit	**46**	**47**	**-3.3%**	**48**	**-4.5%**	**52**	**-12.0%**
Net Income	**13**	**11**	**14.8%**	**10**	**28.4%**	**11**	**16.3%**
Gross Margin	3.1%	3.4%		3.1%		3.2%	
Operating Margin	1.8%	2.1%		2.0%		2.1%	
Net Profit Margin	0.5%	0.5%		0.4%		0.4%	

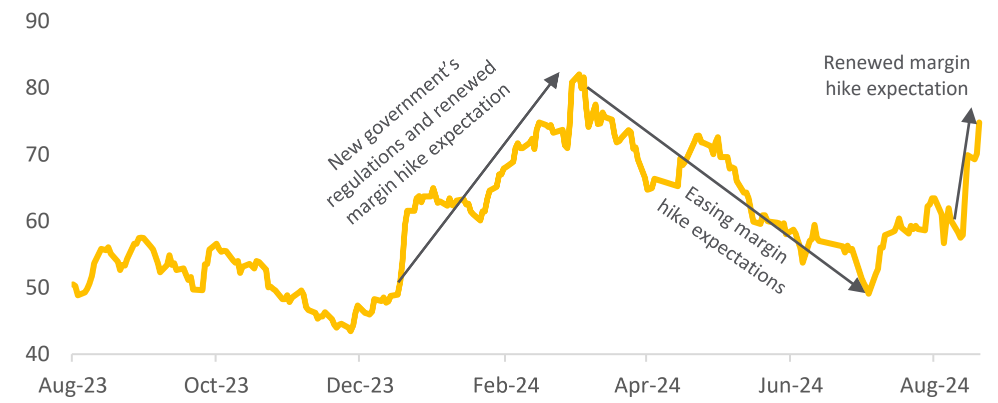
Source: Tadawul, GIB Capital

Valuation and Risks: Post revision in our estimates, and rolling forward our valuation, we revise our TP to SAR63/sh. based on the DCF valuation using the WACC of 7.8% and terminal growth of 2% (both unchanged). Despite an implied downside of ~15% (assuming unchanged fuel margin), we remain Neutral on the stock due to a possibility of fuel margin revision (although the timing remains uncertain). The key downside risks include aggressive expansion by competition/new entrants, any detrimental regulatory change (e.g. increased capex requirements), higher Saudization targets, a downward revision of fuel gross margin, one-off costs such as goodwill write-off and related profit volatility and shift to EV.

Assessing the impact of a possible fuel margin hike: The Saudi fuel retail market is highly regulated with fuel prices (Petro 91/95 and Deisel) and margins on fuel retailing are fixed by the government, resulting in largely stable but thin gross and net margins for the fuel retailers. With the new government's regulations (announced in December 2023), focusing on upgrading and maintaining the quality of fuel stations, the domestic fuel retailers including SASCO, have been incurring notable costs to improve their fuel station network as per the revised requirements.

To cover the increased refurbishing expenses, in addition to general inflation-driven costs, most of the market participants, early this year, started expecting a possible upward revision in fuel margins, which remained unchanged at SAR0.15/liter for Octane 91/95 and SAR0.05/liter for Deisel since the last revision in 2018-19. Accordingly, the share price of both listed fuel retailers, SASCO and Aldress (non-covered) increased sharply in 1Q24 but later normalized on easing expectations. However, there has been a renewed discussion of a possible margin hike, driving the share prices of these companies again.

Figure 3: SASCO share price movement over the last one year (SAR)



Source: Tadawul, GIB Capital

<u>As there has been no official announcement on this so far and the timing/possibility of the margin hike (if any) remains uncertain, we maintain our fuel margin forecasts at the current level to derive our TP.</u> However, we present below the sensitivity to fuel margin hike on our estimates (assuming everything else remains the same), showing a significant earnings upside.

Figure 4: 2025e gross margin sensitivity to fuel margin hike

Diesel margin (SAR/liter)	Octane 91/95 margin (SAR/liter)							
		0.15	0.16	0.17	0.18	0.19	0.20	0.21
	0.050	3.4%	3.7%	4.1%	4.4%	4.8%	5.1%	5.5%
	0.060	3.5%	3.8%	4.2%	4.5%	4.9%	5.3%	5.6%

Source: GIB Capital

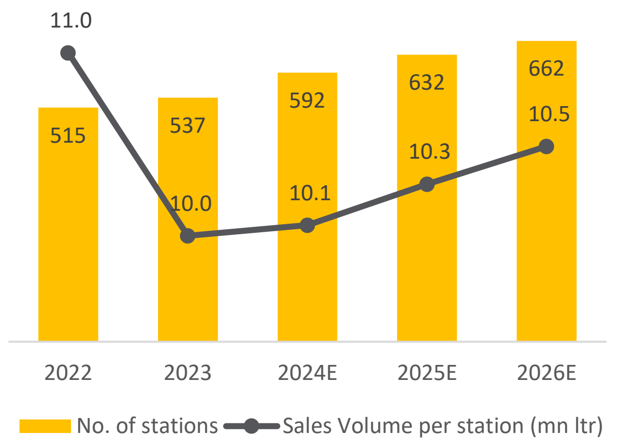
Figure 5: 2025e EPS (SAR) sensitivity to fuel margin hike

Diesel margin (SAR/liter)	Octane 91/95margin (SAR/liter)							
		0.15	0.16	0.17	0.18	0.19	0.20	0.21
	0.050	1.10	1.55	2.00	2.46	2.91	3.36	3.81
	0.060	1.28	1.73	2.18	2.63	3.08	3.53	3.99

Source: GIB Capital

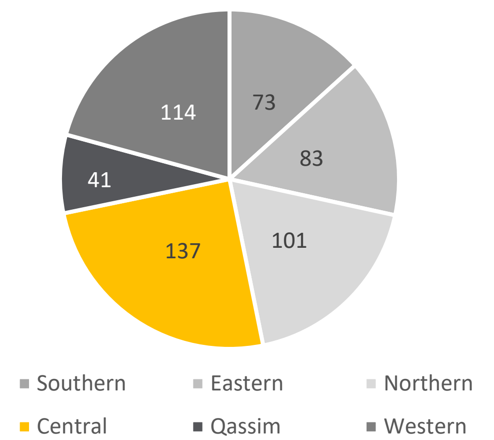
Financial analysis in charts

Figure 6: No. of fuel stations and sales volume per station



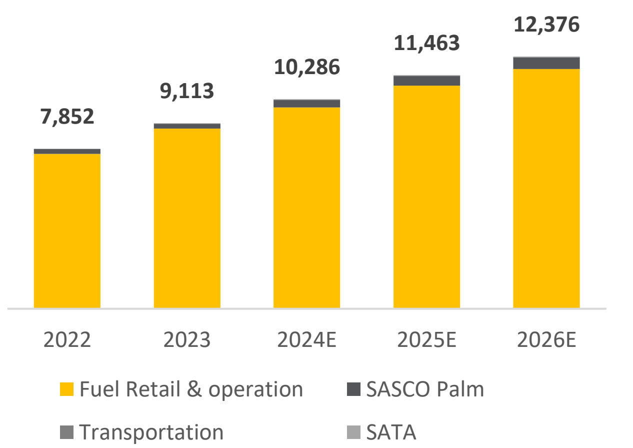
Source: Company data, GIB Capital

*Figure 7: Fuel station breakup by geography – as of 2Q24**



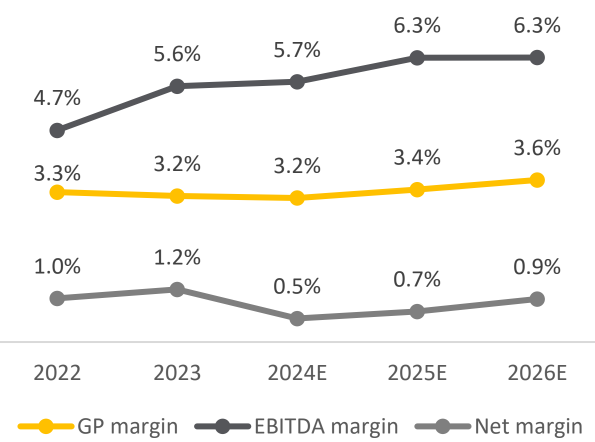
*Source: Company data, GIB Capital, *excludes 13 mobile stations*

Figure 8: Revenue breakup (SARmn)



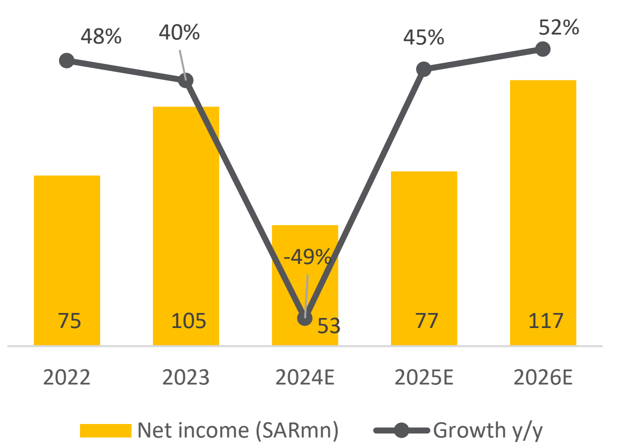
Source: Company data, GIB Capital

Figure 9: Margin trend



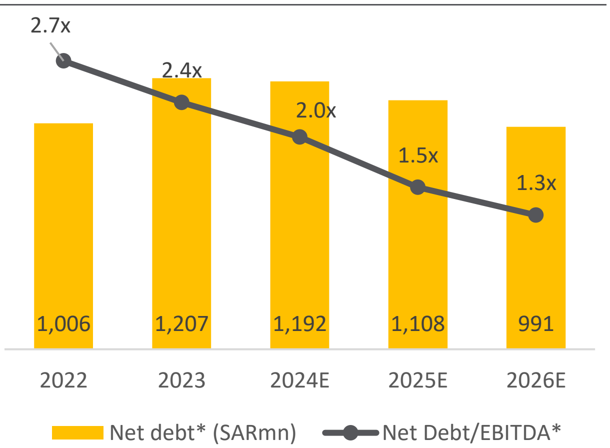
Source: Company data, GIB Capital

Figure 10: Net income (SARmn)



Source: Company data, GIB Capital

Figure 11: Leverage trend



*Source: Company data, GIB Capital, *net debt excludes lease liabilities*

Summarized Financial statements

Figure 12: Summarized basic financial statements (SARmn)

Income statement	2022a	2023a	2024e	2025e	2026e
Revenue	**7,852**	**9,113**	**10,286**	**11,463**	**12,376**
revenue y/y	*93%*	*16%*	*13%*	*11%*	*8%*
COGS	7,593	8,820	9,960	11,079	11,935
Gross Profit	**259**	**293**	**326**	**384**	**441**
Gross Profit margin	*3.3%*	*3.2%*	*3.2%*	*3.4%*	*3.6%*
Selling and distribution expenses	4	5	5	6	6
General and administrative expenses	177	110	124	138	149
Expected credit loss/(reversal)	-4	9	5	3	3
Other income	0	0	-4	-4	-4
Operating profit	**81**	**169**	**196**	**242**	**287**
Operating margin	*1.0%*	*1.9%*	*1.9%*	*2.1%*	*2.3%*
Finance costs	115	159	166	171	165
Other	127	126	38	28	28
PBT	**93**	**136**	**68**	**99**	**150**
Zakat/tax	9	6	6	9	14
Non-controlling interests	9	25	9	13	19
Net income attributable to equity holders	**75**	**105**	**53**	**77**	**117**
Net margin	*1.0%*	*1.2%*	*0.5%*	*0.7%*	*0.9%*
y/y	*66%*	*54%*	*-52%*	*45%*	*52%*
EPS	**1.1**	**1.5**	**0.8**	**1.1**	**1.7**
DPS	0.9	1.1	0.6	0.8	1.3
Payout	80%	71%	75%	75%	75%
EBITDA	**366**	**513**	**589**	**717**	**774**
Net debt (w/o lease liabilities)	1,006	1,207	1,192	1,108	991
Net debt (w/ lease liabilities)	3,373	3,648	4,179	4,348	4,321

Balance Sheet	2022a	2023a	2024e	2025e	2026e
Inventories	83	109	123	137	147
Trade receivables	133	127	143	160	172
Cash and cash equivalents	637	183	390	374	341
Prepaid and other assets	98	101	101	101	101
Derivative Financial instruments	0	2	2	2	2
Total Current Assets	**950**	**522**	**759**	**773**	**764**
Property, plant and equipment	1,741	2,009	2,065	2,071	2,045
Right of use asset	2,221	2,283	2,853	3,120	3,222
Good will	495	492	492	492	492
Investment at fair value	158	150	150	150	150
Investment in debt instruments	250	250	250	250	250
Other non-current assets	277	258	258	258	258
Total Non-Current Assets	**5,142**	**5,442**	**6,068**	**6,341**	**6,417**
Total Assets	**6,092**	**5,964**	**6,827**	**7,114**	**7,181**
Current Liabilities	1,399	1,426	1,685	1,820	1,910
Non-current Liabilities	3,716	3,537	4,118	4,239	4,167
Equity	977	1,001	1,024	1,055	1,104
Total Equity and Liabilities	**6,092**	**5,964**	**6,827**	**7,114**	**7,181**
BVPS	14.0	14.3	14.6	15.1	15.8

Cashflow	2022a	2023a	2024e	2025e	2026e
Cashflow from Operations	619	618	694	808	844
Cashflow from Investing	-1,235	-293	-181	-134	-103
Cashflow from Financing	1,078	-751	-306	-689	-773
Total Cashflows	**463**	**-426**	**207**	**-16**	**-33**

Source: Company, GIB Capital

Figure 13: Key ratios

Key ratios	2022a	2023a	2024e	2025e	2026e
Profitability ratios					
RoA	1%	2%	1%	1%	2%
RoE	8%	11%	5%	7%	11%
Net margin	1.0%	1.2%	0.5%	0.7%	0.9%
Liquidity ratios					
Currrent Assets/ Current Liabilities	0.7	0.4	0.5	0.4	0.4
Debt to Total Equity (w/ IFRS liab.)	4.1	3.8	4.5	4.5	4.2
Receivable Days	6	5	5	5	5
Inventory Days	4	5	5	5	5
Payable days	37	33	33	33	33
Cash conversion cycle	-27	-24	-24	-24	-24
Debt ratios					
Net Debt/EBITDA*	2.7	2.4	2.0	1.5	1.3
Debt/Assets	0.7	0.6	0.7	0.7	0.6
Net Debt/Equity*	1.0	1.2	1.2	1.0	0.9
Valuation ratios					
P/E	69.0	49.2	97.3	67.3	44.2
P/B	5.3	5.2	5.1	4.9	4.7
EV/EBITDA	25.5	18.2	15.8	13.0	12.0
FCF Yield	6.4%	2.4%	3.5%	5.5%	6.6%
Dividend Yield	1.2%	1.4%	0.8%	1.1%	1.7%

*Source: Company, GIB Capital, *net debt excludes lease liabilities*

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Contact us for queries:

Sell Side Research Department,
GIB Capital,
B1, Granada Business & Residential Park,
Eastern Ring Road, PO Box 89589, Riyadh 11692
www.gibcapital.com