

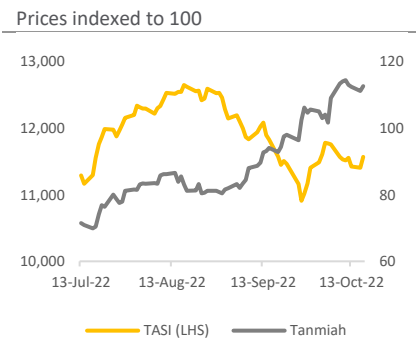
Target Price: SAR110/share
Current Price: SAR113.2/share
Upside: -2.8% (+Div. Yield: 0.7%)
Rating: Neutral

Tanmiah Food Company (Tanmiah)

Target achieved. Revise to Neutral rating

| Stock data | |
|----------------------------|---------|
| TASI ticker | 2281.SE |
| Mcap (SARmn) | 2,264 |
| Avg. Trd. Val (3m) (SARmn) | 28.0 |
| Free float | 30% |
| QFI holding | 2.3% |
| TASI FF weight | .033% |

Source: Bloomberg



Source: Bloomberg

- The stock moved up ~40%, in line with our recommendation, reaching our TP of SAR110/sh.
- Further move hinges on Q3 profits in our view. The poultry segment of Almarai reported strong Q3 numbers led by pricing – which is likely positive for Tanmiah as well.
- However, we wait for Q3 results and formal completion of Tyson's acquisition to revise our valuation and keep our TP unchanged for now at SAR110/share with a Neutral rating (from OW previously).

Post-initiation rally: We initiated on Tanmiah when the stock was at SAR80.4/share on 24 August 2022, and since then, the stock has rallied ~40% and is now at SAR113.2 (vs our Target price of SAR110/share). The strong performance has been driven by the increase in poultry prices, more than offsetting input costs (corn and soybean) and continued increase in capacity. We believe there is more interest gaining in the stock as reflected by the increase in volumes in the past 2 months.

Peer results are positive: The poultry numbers for Almarai in 3Q22 were strong, with the segment's revenue jumping 43% y/y and net income growing by over 1.7x. In the earnings call, the management attributed the robust poultry performance to an increase in prices that helped mitigate the rise in the costs of corn and soybean. While the retail poultry prices were broadly unchanged, the increase is primarily in the food service and HORECA channels. These numbers could imply record profits for Tanmiah in Q3. We expect the company to report Q3 numbers in the 1st or 2nd week of November.

Estimates/risks/valuation: We expect the company to report a 40% y/y growth in revenue (**SAR545mn**) mainly led by an increase in poultry pricing on a y/y basis. For net profit, we expect **SAR41mn**, which implies a 7.5% net profit margin (as compared to an average 3% quarterly margin since 2Q20). If the company could report SAR41mn in Q3, it would imply only ~13.7x annualized P/E for Tanmiah at the current share price. However, **post the acquisition of Tyson Foods, the EPS could be lower by 20-25% as per our estimate** thus increasing the multiples. This is because Tyson Foods will acquire a 15% equity stake in Agriculture Development Company (the main poultry arm) and a 60% equity stake in Supreme Foods Processing Company. This is one of the reasons we recommend investors to book profits at current levels. Another point to note is that cost of raw materials for the quarter is difficult to forecast given its dependence on the period of purchase and utilization of the existing inventory. We wait for Q3 numbers to revise our valuation though we believe Q3 could be slightly lower than our earlier estimate because of higher-than-expected input (spot) prices. For now, our target price at SAR110/share implies a Neutral rating (from a previously Overweight rating). An additional downside risk to our estimate is that as the poultry capacity ramps up, poultry prices could even decline as up as indicated by the MEWA minister recently. The minister expected a 10% decline in poultry prices, which was our thesis as well, as elaborated in our initiation report. Currently, the Kingdom has achieved a poultry meat self-sufficiency rate of nearly 68%.

Investment case

The company is a major domestic poultry producer in Saudi Arabia with a fresh chicken production capacity of 420,500 birds per day (as of 2Q22). The company's pricing for Poultry is considered at the lower end of the spectrum of fresh chicken prices in KSA even as Tanmiah's products enjoy consumer perception of high quality. Tanmiah has an asset-light business model (giving it a high sales/asset ratio of 100%+) wherein the company leases most of its farms, hatcheries, and other production facilities that allow better speed and scalability against competitors. Tanmiah has an integrated business model wherein a part of fresh chicken produce (whole and parts) is sent for Further Poultry Processing (FPP) for manufacturing value-added products - ~20% of revenue. A large part of the chicken for FPP is frozen/imported in our view. The company sells its products through its network of distributors and retailers as well as via online channels. It also caters to HORECA customers such as Burger King, Subway, and McDonald's. The company has the master franchise agreement for Popeye stores in KSA which is fast growing.

The sector witnessed its largest poultry price hike in a decade to offset the increase in input costs. The poultry market is highly competitive in the Kingdom but the targeted self-sufficiency of 80% by 2025 is expected to benefit domestic poultry producers. The government support for domestic poultry producers includes subsidies, import tariffs, and strict Halal compliance, providing them an edge over foreign players. If there are no regulatory bans on imports, market share gains would likely come mainly from a price war.

To capitalize on this opportunity, the company plans to expand its production capacity by around 3.2x in 4 years from 2021 levels though we believe a 2.2x capacity is more likely, for now. In any case, this should result in a proportional jump in earnings in the longer term. The high per capita chicken consumption in Saudi Arabia and other GCC markets, owing to the regional food habits, is likely to continue to support demand for poultry products. Additionally, favorable demographics including steady population growth and an influx of foreign tourist arrivals of 30mn by 2030 (compared to ~4mn in 2021) and a shift in consumer preferences to greater eating-out culture, are expected to strengthen demand in the long term.

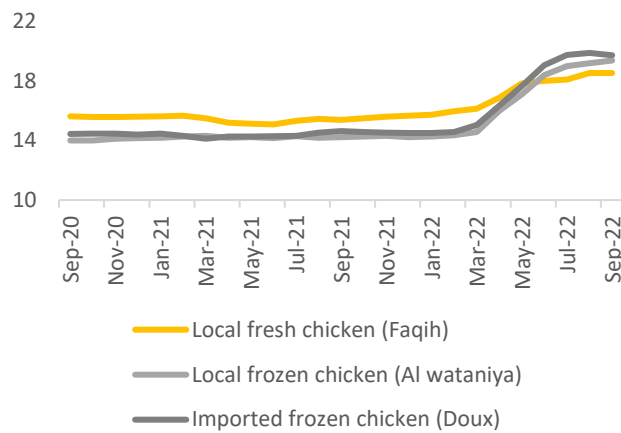
Figure 1: Income statement (SARmn) pre-adjustment to acquisition of Tyson

| Income statement | 2020a | 2021a | 2022e | 2023e |
|----------------------------------|--------------|--------------|--------------|--------------|
| Revenue | 1,212 | 1,539 | 2,067 | 2,307 |
| revenue y/y | 6% | 27% | 34% | 12% |
| COGS | 902 | 1,213 | 1,536 | 1,683 |
| Gross Profit | 310 | 327 | 531 | 625 |
| Gross Profit margin | 26% | 21% | 26% | 27% |
| Sales & Marketing | 133 | 189 | 256 | 278 |
| G&A | 66 | 89 | 115 | 126 |
| Operating profit | 107 | 47 | 158 | 219 |
| Operating margin | 9% | 3% | 8% | 10% |
| Finance costs | (26) | (26) | (33) | (39) |
| Other income | 1 | 1 | 1 | 1 |
| PBT | 82 | 20 | 125 | 180 |
| Zakat/tax | (7) | (7) | (10) | (17) |
| Net income | 74 | 14 | 115 | 163 |
| Net margin | 6% | 1% | 6% | 7% |
| y/y | 5% | -82% | 745% | 43% |
| EPS | 3.7 | 0.7 | 5.7 | 8.2 |
| DPS | 0.0 | 0.5 | 0.8 | 1.0 |
| Payout | 0% | 75% | 13% | 12% |
| EBITDA | 183 | 141 | 234 | 317 |
| Net debt (w/o lease liabilities) | 253 | 137 | 95 | 107 |
| Net debt (w/ lease liabilities) | 432 | 352 | 357 | 423 |

Source: Company, GIB Capital

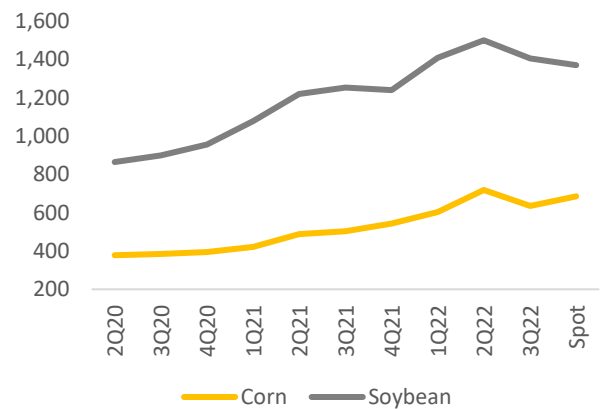
Charts

Figure 2: Chicken prices



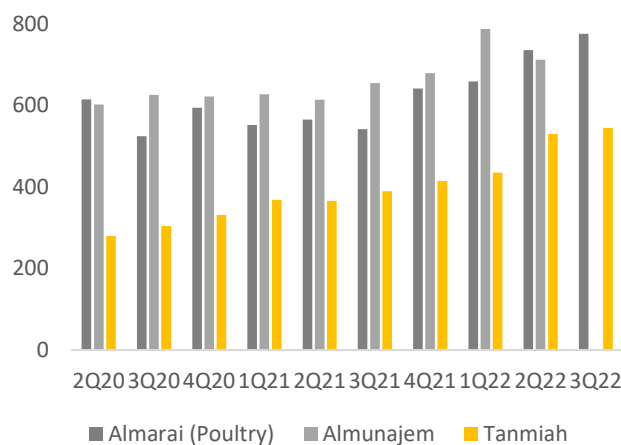
Source: GASTAT, GIB Capital

Figure 3: Corn and soybean prices



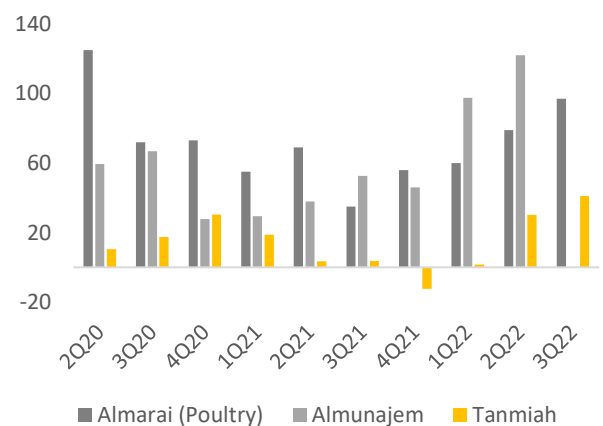
Source: Bloomberg, GIB Capital

Figure 4: Revenue comparison (SARmn)



Source: Company, GIB Capital; Tanmiah 3Q22 is estimated

Figure 5: Net income comparison (SARmn)



Source: Company, GIB Capital; Tanmiah 3Q22 is estimated

Figure 6: Financials comparison between Almarai poultry, Almunajem and Tanmiah (SARmn)

| Financials comparison | 2Q20 | 3Q20 | 4Q20 | 1Q21 | 2Q21 | 3Q21 | 4Q21 | 1Q22 | 2Q22 | 3Q22 |
|--------------------------------|------|------|------|------|------|------|-------|------|------|------|
| Almarai (poultry) - revenue | 615 | 525 | 595 | 552 | 566 | 542 | 642 | 659 | 736 | 776 |
| growth y/y | 17% | 7% | -2% | -1% | -8% | 3% | 8% | 19% | 30% | 43% |
| Almunajem - revenue | 602 | 626 | 622 | 628 | 614 | 655 | 679 | 788 | 712 | |
| growth y/y | | | | -9% | 2% | 5% | 9% | 25% | 16% | |
| Tanmiah - revenue | 280 | 304 | 332 | 368 | 367 | 390 | 415 | 435 | 531 | 546 |
| growth y/y | | | | 31% | 28% | 25% | 18% | 45% | 40% | |
| Almarai (poultry) - net income | 125 | 72 | 73 | 55 | 69 | 35 | 56 | 60 | 79 | 97 |
| growth y/y | 51% | 22% | -8% | -25% | -45% | -51% | -23% | 9% | 14% | 177% |
| Almunajem - net income | 59 | 67 | 28 | 29 | 38 | 53 | 46 | 98 | 122 | |
| growth y/y | | | | -61% | -36% | -21% | 65% | 231% | 221% | |
| Tanmiah - net income | 10 | 18 | 30 | 19 | 3 | 4 | -12 | 2 | 30 | 41 |
| growth y/y | | | | | -67% | -79% | -141% | -92% | NA | NA |
| Almarai (poultry) - net margin | 20% | 14% | 12% | 10% | 12% | 6% | 9% | 9% | 11% | 13% |
| Almunajem - net margin | 10% | 11% | 4% | 5% | 6% | 8% | 7% | 12% | 17% | |
| Tanmiah - net margin | 4% | 6% | 9% | 5% | 1% | 1% | -3% | 0% | 6% | |

Source: Company, GIB Capital

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Contact us for queries:

Pritish Devassy, CFA, CPA
Sell Side Research Department,
GIB Capital,
B1, Granada Business & Residential Park,
Eastern Ring Road, PO Box 89589, Riyadh 11692
Pritish.devassy@gibcapital.com | www.gibcapital.com