

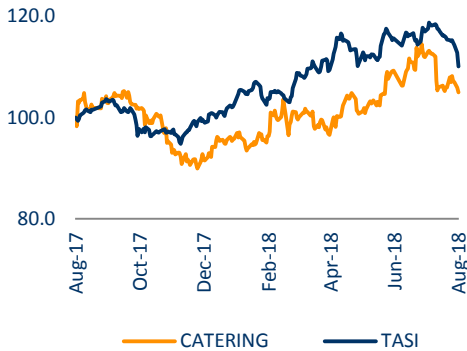
2Q 2018 Results Update

August 16, 2018

Recommendation	Neutral
Previous Recommendation	Neutral
Current Price (SAR)	90.0
Target Price (SAR)	91.0
Upside/Downside (%)	1.1%
<i>As of Aug 15th 2018</i>	

Key Data (Source: Bloomberg)	
Market Cap (SAR bn)	7.4
52 Wk High (SAR)	96.5
52 Wk Low (SAR)	75.2
Total Outstanding shares (in mn)	82.0
Free Float (%)	63.8%

CATERING vs. TASI (Rebased)



Price Performance (%)	Absolute	Relative
1m	(6.2%)	(0.3%)
6m	8.9%	2.7%
12m	5.0%	(5.1%)

Major Shareholders (%)

Public Institution for Arab Airlines	35.70%
Strategic Supply Co. Ltd.	9.31%
Abdul Mohsen Abdul Aziz Al-Hokair Holding Group	8.67%

Quarterly Sales (SAR mn) and Operating Margin



Source: Bloomberg, Company Financials, FALCOM Research; Data as of 15th Aug 2018

Weak retail sales weigh on the bottom line

Saudi Airlines Catering Co.'s (Catering) net profit for 2Q18 fell slightly short of consensus estimates, and dropped 8.2% YoY to SAR 120mn, primarily due to a plunge in retail sales revenue (-43% YoY), along with a rise in general and administrative expenses and one-time impact of reversal of trade receivables as a result of the implementation of IFRS 9.

Revenue grew 2% YoY to SAR 562mn; however, gross profit declined 3.5% YoY to SAR 189mn due to a rise in personnel expenses and other operating costs. Operating income declined 9.5% YoY to SAR 131mn, mainly due to the SAR 6mn charge for reversal of trade receivables, and higher general and administrative expenses. Debt free operations and healthy operating cash flows continue to support stock's attractiveness to investors, the emergence of low cost carriers, poses an inherent risk to Catering's business model. Given the countervailing factors, we retain our 'Neutral' rating on the stock.

- Revenue from in-flight catering grew 8% YoY to SAR 413mn, while revenue from business lounge segment was up 16.6% YoY to SAR 47mn, and non-airline segment revenue expanded 19.5% YoY to SAR 42mn. Retail segment's revenue, however, declined 43.3% YoY to SAR 45mn. Thus, total revenue expanded 2.0% YoY and 5.8% QoQ to SAR 562mn in 2Q18.
- Cost of sales rose 5% YoY and 4.7% QoQ to SAR 373mn, led by a surge in personnel cost (+21.3% YoY) and other operating cost (+31.4% YoY). As a result, gross profit declined 3.5% YoY to SAR 189mn. Gross margin for the quarter stood at 33.7%, contracting 191bps YoY.
- Operating expenses for the quarter advanced 13.6% YoY and 36.7% QoQ to SAR 58mn. General and administrative expenses increased 9.1% YoY to SAR55.1mn. Additionally, a one-time charge of SAR 6.3mn for the reversal of trade receivables was booked in 2Q18, as a result of IFRS 9 implementation. Other income grew from 0.9mn in 2Q17 to 3.3mn in 2Q18, partially offsetting the rise in operating expenses. As a result, operating margin shrank 296bps YoY to 23.3%.
- Net income declined 8.2% YoY to SAR 120mn in 2Q18, but ended flat on a QoQ basis. Consequently, net income margin contracted 237bps YoY and 124bps QoQ to 21.4%. EPS stood at SAR 1.47 per share for 2Q18.
- During 1Q18, the company had adjusted its provision for bad debts as per IFRS 9, and its positive impact had compensated for lower revenues in that quarter. As a result, net profit remained flat sequentially, despite an increase in revenues in 2Q18.
- The board has recommended 14% (SAR 1.4 per share) cash dividend for 2Q18, amounting to SAR 114.8mn, which is in line with the company's dividend pay-out policy of more than 90%.

Valuation: We have revised our target price slightly upwards, with a fair value of SAR 91.0 per share. The stock has run-up 4% since our previous earnings report, however we see limited upside potential from current levels. We maintain a "Neutral" rating on the stock.

	2Q'18	2Q'17	% YoY	FY18E	FY17	% YoY
Revenues (SAR mn)	562.0	551.1	2.0%	2326.6	2223.4	4.6%
Gross Profit (SAR mn)	189.4	196.3	-3.5%	799.2	722.8	10.6%
EBITDA (SAR mn)	146.9	156.4	-6.1%	664.3	583.0	14.0%
Net Profit (SAR mn)	120.3	131.0	-8.2%	553.4	481.7	14.9%
EPS basic (SAR)	1.5	1.6	-8.2%	6.7	5.7	18.1%
Gross Margin (%)	33.7%	35.6%	-1.9%	34.4%	32.5%	1.8%
EBITDA Margin (%)	26.1%	28.4%	-2.2%	28.6%	26.2%	2.3%
Net Profit Margin (%)	21.4%	23.8%	-2.4%	23.8%	21.7%	2.1%

Source: Company Financials, FALCOM Research

FALCOM Rating Methodology

FALCOM Financial Services uses its own evaluation structure, and its recommendations are based on quantitative and qualitative data collected by the analysts. Moreover, the evaluation system places covered shares under one of the next recommendation areas based on the closing price of the market, the fair value that we set and the possibility of ascent/descent.

Overweight: The Target share price exceeds the current share price by $\geq 10\%$.

Neutral: The Target share price is either more or less than the current share price by 10%.

Underweight: The Target share price is less than the current share price by $\geq 10\%$.

To be Revised: No target price had been set for one or more of the following reasons: (1) waiting for more analysis, (2) waiting for detailed financials, (3) waiting for more data to be updated, (4) major change in company's performance, (5) change in market conditions or (6) any other reason from FALCOM Financial Services.

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