

### Initiation Coverage

May 12, 2020

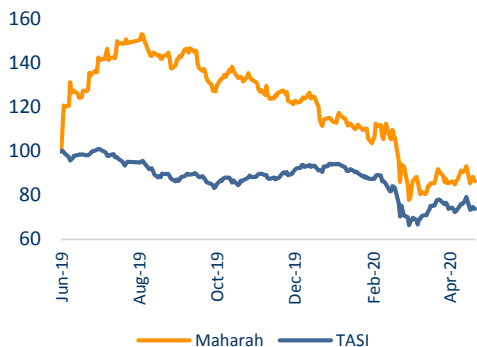
Recommendation	Overweight
Current Price (SAR)	59.6
Target Price (SAR)	66.0
Upside/Downside (%)	10.7%

As of May 07, 2020

#### Key Data (Source: Bloomberg)

Market Cap (SAR bn)	2.2
52 Wk High (SAR)	109.0
52 Wk Low (SAR)	53.0
Total Outstanding shares (in mn)	38
Free Float (%)	73.9%

#### Maharah Vs TASI (Rebased)

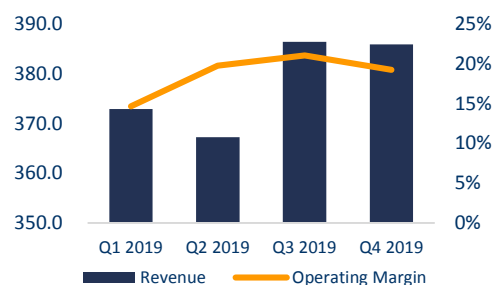


Price Performance (%)	Absolute	Relative
1m	(4.2%)	0.9%
6m	(34.4%)	(19.4%)
12m	NA	NA

#### Major Shareholders (%)

Al-Ahlia International Real Estate Investment Company	19.4%
Al KhibrahAl- MemariyaCo.	16.0%
Abdullah Suleiman Mazyad Al-Amr	12.2%

#### Quarterly Sales (SAR mn) and Operating Margin



Source: Bloomberg, Company Financials, Falcom Research; Data as of 7<sup>th</sup> May 2020

Maharah Human Resources Co. (Maharah)'s revenues grew 11.9% YoY to SAR 1.5bn as its corporate and individual segments reported top-line growth of 14% and 7%, respectively. The company recorded an improvement in the gross margin, aided by the increase in utilization of the deployed resources. Despite an increase in administrative expense and higher taxes, net income grew 21.0% YoY to SAR 267mn in FY19 owing to the factors mentioned above.

We initiate Maharah with an "Overweight" rating, as despite a projected revenue decline in 2020, the company's fundamentals remain strong, that gives confidence in long-term potential.

#### Maharah's market leading position to help capture untapped potential

KSA employed 13.4 million people by the end of 2019, of which non-Saudi labor force accounted for 76.3%. Less than 1% of KSA's manpower solutions are provided by large human resources companies. Maharah can benefit from its market leading position with a share of 17–20% (among large companies) and sizeable presence in multiple regions of the country to exploit this opportunity. In addition, with a rich experience of servicing over 800 corporate clients across industries and more than 65,000 household clients through hourly services and contractual obligations, the company boasts of its ability to service a variety of labor requirements.

#### COVID-19 may derail Maharah's growth trajectory

During 2016–19, the company's revenues rose at a CAGR of 8.6%, coinciding with KSA's current GDP growth rate of 2.7% CAGR. Rising population, higher disposable income, social changes to encourage women workers, and the government's push to promote non-oil sectors as part of Vision 2030 have led to increased labor demand. However, KSA stares at an economic contraction in 2020 amid the COVID-19 pandemic, which may increase unemployment rates. Maharah may find it difficult to add or renew employment contracts. The company has been forced to temporarily suspend 'Khidmah' hourly services that may impact annual revenues.

#### Strong balance sheet bodes well, yet falling margins remain a concern

Maharah operated from a position of total cash of SAR 299mn in FY19, with cash and time deposits at the end of FY19 making up 12.6% of the current market cap. The company possesses a sizeable asset of "available visas" (unused visas obtained from MOL) that can help expedite the manpower hiring process from foreign countries. However, the company's return on assets and equity has witnessed a steady decline in the past four years. Barring the upturn in margins in 2019 due to higher utilization of resources, the margins have come under pressure, hinting at growing price competition in the industry.

#### Aims to provide integrated human resources solutions

Maharah aims to become an integrated human resources solutions company. To this effect, it uses its comprehensive client database to design marketing initiatives to sell integrated services between its corporate segment and household segment clients. In 2018, Maharah acquired Bloovo, an algorithm-based online recruitment platform, to better map client requirements.

**Valuation:** We valued Maharah using the DCF approach to arrive at a fair value of SAR 66.0 per share. We considered WACC at 8.3% with a terminal growth rate of 2.0%.

	2019	2020e	2021e	2022e
Revenues (SAR mn)	1,512	1,441	1,512	1,575
Gross Profit (SAR mn)	380	359	378	394
EPS (SAR)	7.3	6.7	6.9	7.1
Operating Margin (%)	18.7%	18.5%	18.4%	18.2%
RoE (%)	46.1%	34.2%	29.3%	25.8%
P/E (x)	11.9x	8.8x	8.6x	8.4x
P/BV (x)	5.5x	3.0x	2.5x	2.2x
EV/EBITDA (x)	10.0x	6.6x	6.1x	5.6x

Source: Company Financials, Falcom Research

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## Valuation Summary

### Explanation of the valuation methodology and assumptions

We valued Maharah using the DCF approach to arrive at a fair value of SAR 66.0 per share. We considered WACC at 8.3% with a terminal growth rate of 2.0%.

In relative terms, Maharah is trading at a PE of 14.8x, showing a discount of 12.6% to its sector peers and an EV/EBITDA multiple of 6.9x at a discount of 18.8% to its peers.

SAR Mn	FY 2019A	FY 2020E	FY 2021E	FY 2022E	FY 2023E
EBIT	283	266	278	287	297
Taxes	(26)	(27)	(31)	(35)	(39)
Depreciation, amortization and impairment	13	14	18	21	24
Changes in working capital	(196)	(37)	(57)	(52)	(99)
Net capital expenditure	(24)	(29)	(33)	(39)	(48)
<b>Free Cash Flow to firm</b>	<b>49</b>	<b>188</b>	<b>175</b>	<b>182</b>	<b>135</b>
<i>Discount Factor</i>		0.9	0.9	0.8	0.7
<b>PV of free cash flow to firm</b>		<b>178</b>	<b>153</b>	<b>147</b>	<b>101</b>
<b>Net Present Value (A)</b>					<b>579</b>
<b>PV Terminal Value (B)</b>					<b>1,632</b>
<b>Assumed Terminal Growth Rate</b>					<b>2.0%</b>
<b>Discount Rate</b>					<b>8.3%</b>
<b>Enterprise Value (A+B)</b>	<b>2,211</b>	<b>WACC Assumptions</b>			
					Risk free rate 2.6%
<b>Total Cash</b>	299				Market returns 7.2%
<b>Total Debt</b>	35				Beta 0.8x
<b>Minority Interest</b>	(5)				<b>Cost of equity 8.4%</b>
<b>Equity Value in SAR mn</b>	<b>2,480</b>				
<b>Number of shares in mn</b>	38				<b>Post tax cost of debt 0.7%</b>
<b>Target Price in SAR per share</b>	<b>66.0</b>				Weight of equity in capital structure 98.9%
<b>CMP in SAR as on May 7<sup>th</sup> 2020</b>	<b>59.6</b>				Weight of debt in capital structure 1.1%
<b>Upside/(Downside) to current market price</b>	<b>10.7%</b>				<b>WACC 8.3%</b>

Source: Company Financials, Falcom Research Estimates

### Risks

#### Upside Risks:

- A V-shape economic recovery following the COVID-19 pandemic containment can significantly boost labor demand and thereby help the company grow
- A regulation by the Saudi government to allow only licensed intermediaries to supply foreign manpower resources to avoid human trafficking and labor exploitation and help the company capture more market share

#### Downside Risks

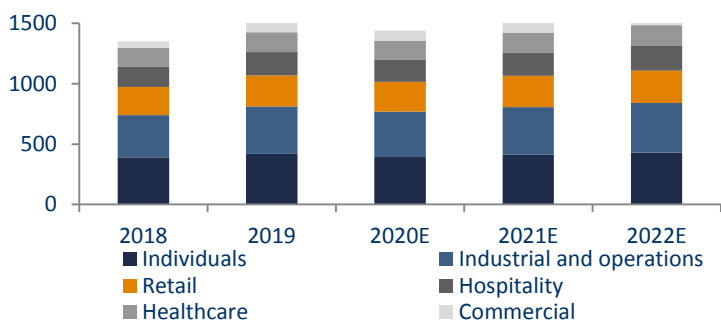
- Regulatory changes with increased focus on Saudization policies can have a significant adverse impact on the company's growth prospects though at present the company primarily supplies manpower for industries such as retail, construction, wholesale etc where employment of Saudi nationals is low
- Technological advancement and automation may diminish demand for unskilled labor

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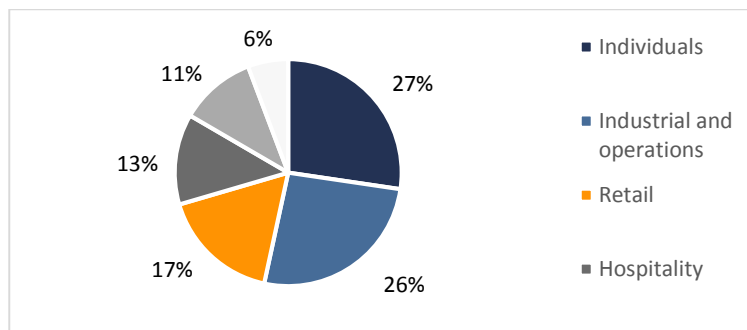
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## Key Charts

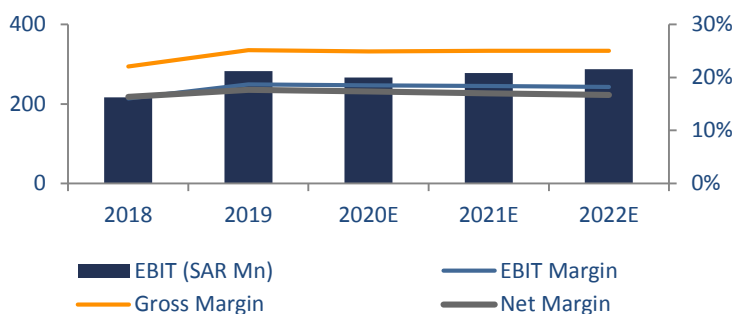
Revenue (SAR mn)



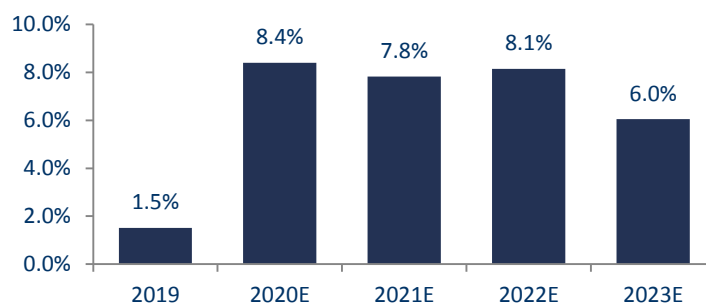
Revenue Split (2019)



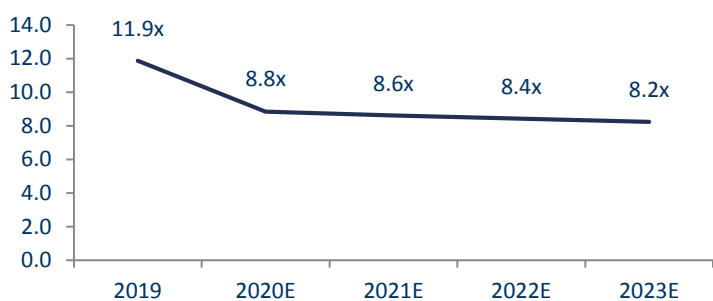
EBIT & Margins



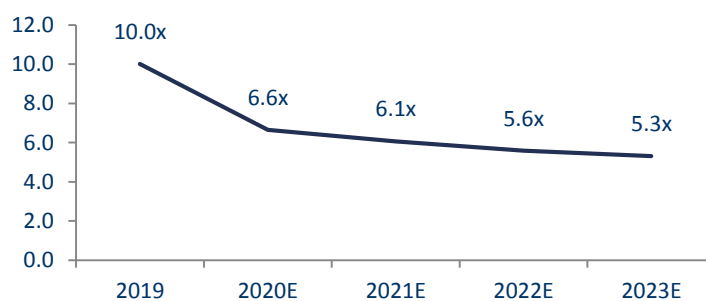
Free cash flow yield



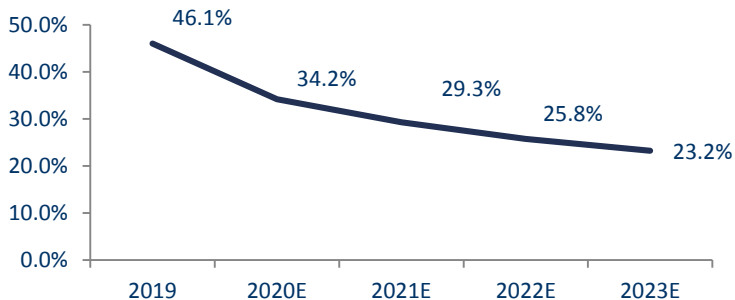
Price to Earnings



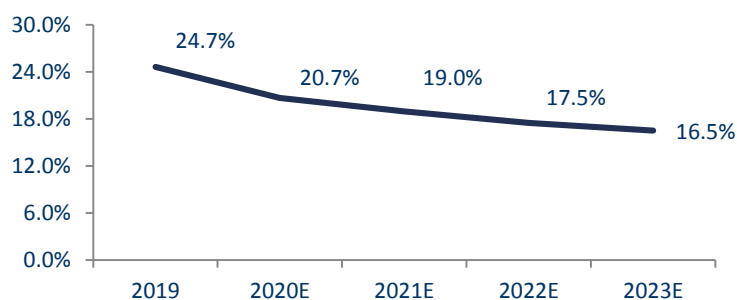
EV/EBITDA



Return on Equity



Return on Assets



Source: Falcom Research Estimates

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## Summary Financials

P&L (SAR mn)	2019	2020e	2021e	2022e
Sales	1,512	1,441	1,512	1,575
Gross Profit	380	359	378	394
EBITDA	295	280	296	308
EBIT	283	266	278	287
G&A Expenses	(67)	(67)	(73)	(79)
Other Income	11	12	12	12
Net gain on equity	1	1	1	1
PBT	293	277	288	298
Zakat	(26)	(27)	(31)	(35)
Minorities	(5)	(3)	(3)	(3)
Net Income	272	253	260	265
EPS	7.3	6.7	6.9	7.1
DPS	2.7	2.8	3.0	3.3

BS (SAR mn)	2019	2020e	2021e	2022e
Cash	189	282	352	420
Current Assets	810	912	1,042	1,170
Fixed Assets	179	194	210	228
Intangibles	4	4	4	4
Total Assets	1,103	1,222	1,368	1,516
Current Liabilities	439	412	414	421
Retained deposits	119	119	119	119
Lease liabilities	28	28	28	28
Shareholders Equities	591	738	885	1,029
Total Liabilities	518	491	493	500

CF (SAR mn)	2019	2020e	2021e	2022e
Operating Cash Flow	341	291	306	319
Working Capital Changes	196	37	57	52
Cash Flow from Operating Activities	63	229	217	231
Capex	(24)	(29)	(33)	(39)
Cash Flow from Investing Activities	153	(30)	(35)	(41)
Changes in Debt	-	-	-	-
Dividends	(100)	(105)	(113)	(122)
Cash Flow from Financing Activities	(109)	(105)	(113)	(122)

Source: Bloomberg, Company Financials, Falcom Research

Growth	2019	2020e	2021e	2022e
Revenue	11.9%	(4.7%)	4.9%	4.2%
EBITDA	29.2%	(4.9%)	5.5%	4.2%
Operating profit	30.5%	(5.7%)	4.4%	3.2%
PBT	26.3%	(5.3%)	4.0%	3.3%
Net Income	21.0%	(6.3%)	2.9%	2.1%

Ratios (%)	2019	2020e	2021e	2022e
Gross Margin	25.1%	24.9%	25.0%	25.0%
EBITDA Margin	19.5%	19.5%	19.6%	19.6%
EBIT Margin	18.7%	18.5%	18.4%	18.2%
Net Margin	17.7%	17.4%	17.0%	16.7%
ROE	46.1%	34.2%	29.3%	25.8%
ROA	24.7%	21.3%	20.4%	18.6%
ROCE	40.9%	32.6%	30.2%	26.5%
Debt/Equity	0.0x	0.0x	0.0x	0.0x
Net Debt/EBITDA	(0.9x)	(1.2x)	(1.2x)	(1.3x)
FCF Yield	1.5%	8.4%	7.8%	8.1%
Dividend Yield	3.1%	4.7%	5.0%	5.5%

Valuation	2019	2020e	2021e	2022e
P/E	11.9x	8.8x	8.6x	8.4x
P/B	5.5x	3.0x	2.5x	2.2x
EV/EBITDA	10.0x	6.6x	6.1x	5.6x
EV/EBIT	10.5x	7.1x	6.8x	6.3x
EV/Sales	2.0x	1.3x	1.2x	1.1x

Peer Valuations	P/E	EV/EBITDA
S- Pool Inc	18.7	13.6
Kforce Inc	41.6	23.7
Kelly Services Inc	17.5	8.8
Groupe CRIT	7.6	4.6
Synergie SA	33.9	9.8
Outsourcing Inc	7.6	3.6
Trueblue Inc	5.6	4.4
Heitdrick & Struggles Intl	12.4	8.2
<b>Maharah</b>	<b>14.8x</b>	<b>6.9x</b>
<b>Sector Median</b>	<b>14.1x</b>	<b>6.9x</b>
<b>Premium/ (Discount)</b>	<b>4.9%</b>	<b>0.0%</b>

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## 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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