



Not a short-term buy; downgrade to N

- **Robust revenue growth not expected to filter through to bottom line in 2012e due to sustained margin pressure and higher interest charges, but pricing flexibility is a key catalyst**
- **We are more positive on Juhayna's medium-term prospects as its profitability profile is enhanced and integration plans come to fruition**
- **Downgrade to Neutral from Overweight; cut TP 28% to EGP5.07/share**

Double-digit top-line growth to continue: We expect Juhayna's revenue to grow a healthy 22% y-o-y in 2012e, boosted by (1) strong volume growth across all segments, (2) the resumption of exports to Libya (Juhayna's main export market, c6% of top line), and (3) higher selling prices (up 5% y-o-y blended). We remain positive about Juhayna's long-term revenue prospects (2012–16e CAGR of 19%), which will remain supported by Egypt's favorable demographics, an accelerated trend of conversion to packaged from loose dairy products, and product innovation (more than 50 new SKUs in 2011).

Margin compression and towering interest charges to hinder bottom-line growth in 2012e, but high pricing flexibility is a key catalyst: We expect Juhayna's bottom line to grow a marginal 9% in 2012e as we forecast a flat gross margin, given (1) no expected reversal in commodity price trends, (2) a raw milk purchase price equivalent to 2011's fixed at cEGP3/kg as per biannually renewable contracts with milk farms (assuming a peak milk price of EGP3.25/kg would lower our valuation 10%), and (3) additional cost-side pressure due to EGP depreciation (with USD denominated purchases representing 25%–30% of total COGS). Furthermore, we expect additional debt obtained to finance a hefty CAPEX bill (expected at EGP750m in 2012e alone) and increased lending rates on floating-rate loans (which make up the majority of Juhayna's debt) to push the company's interest expense up c31% y-o-y in 2012e. Higher than expected product price increases are a key catalyst, in our view, and hinge on Juhayna's marked ability to pass raw material and/or forex-related cost increases on to consumers. Each 1% increase in blended average selling price raises our valuation 3%.

We downgrade Juhayna to N from OW and cut our TP 28% to EGP5.07/share (2% upside) on the back of lower long-term gross margin assumptions (down 192 bps on average), higher CAPEX guidance (cEGP2bn 4-year spending program), and an increased cost of capital (up 227 bps). We are more positive on Juhayna after 2012e as its profitability profile is enhanced and integration benefits are realized. The stock seems fairly priced at current levels, trading at a 2012e P/E of 13.4x, in line with global peers' P/E versus EPS growth.

Neutral

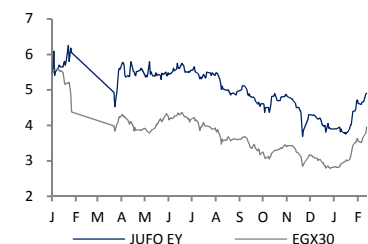
Target price (EGP)	5.07
Current price (EGP)	4.97
Potential return	2.0%

Bloomberg	JUFO EY
Reuters	JUFO.CA

Mcap (EGPm)	3,509
Mcap (USDm)	581
Number of shares (m)	706
Free float	47%
Daily volume (USDm)	0.4
Foreign own. limit	N/A
Foreign ownership	N/A

Note: All prices as of 14 February 2012

Price performance



15 February 2012

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Please refer to important disclosures and analyst certifications on pages 15–16 of this report.

Key indicators	2010	2011e	2012e	2013e
Clean EPS (EGP)	0.30	0.34	0.37	0.45
Clean P/E	16.7x	14.6x	13.4x	10.9x

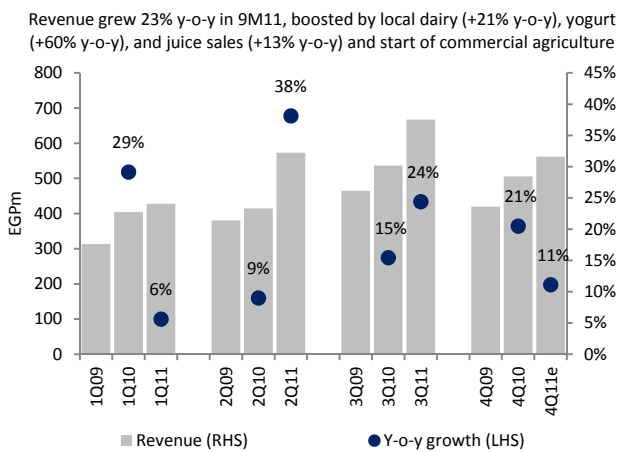
Source: Company data, HC



Double-digit top-line growth to continue

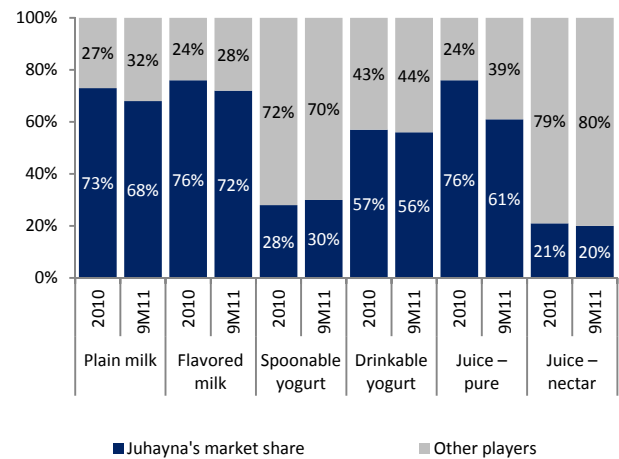
We expect Juhayna's revenue to grow a healthy 22% in 2012e (in line with management guidance of high double-digit growth, similar to the level achieved in 9M11) and to grow at a 4-year revenue CAGR of 19% thereafter, boosted by (1) strong volume growth across all segments, (2) the resumption of exports to Libya (Juhayna's main export market, c6% of top line) after exports plummeted 35% y-o-y in 9M11 on the back of turmoil in the country, and (3) higher selling prices. We remain positive about Juhayna's medium- to long-term revenue prospects, which will remain supported by Egypt's favorable demographics, an accelerated trend of conversion to packaged from loose dairy products, and product innovation (more than 50 new SKUs in 2011).

Revenue growth impressed in a tough year...



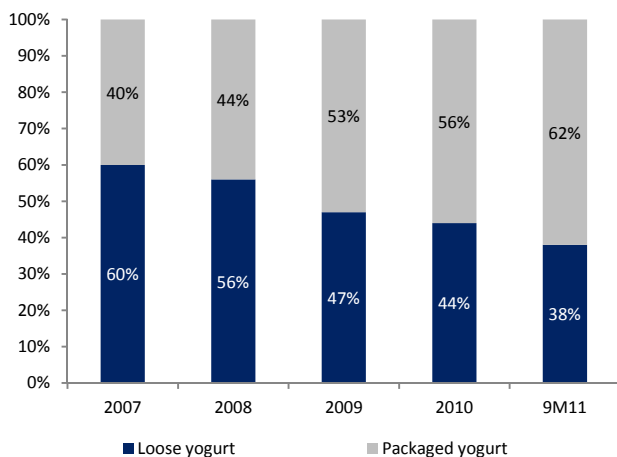
Source: Juhayna, HC

...on price increases and some market share gains



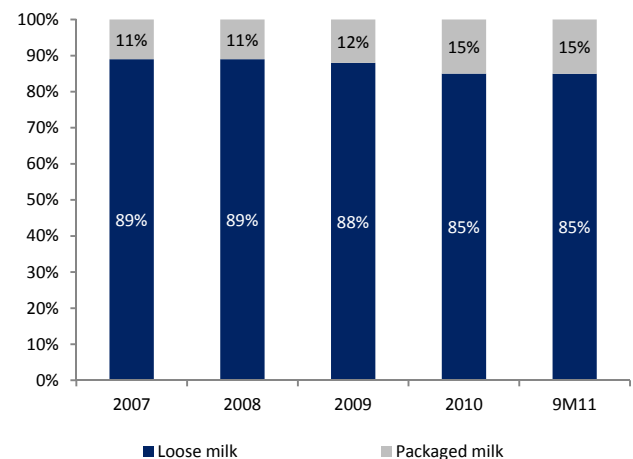
Source: Juhayna, HC

Faster pace of conversion to packaged yogurt...



Source: Juhayna, HC

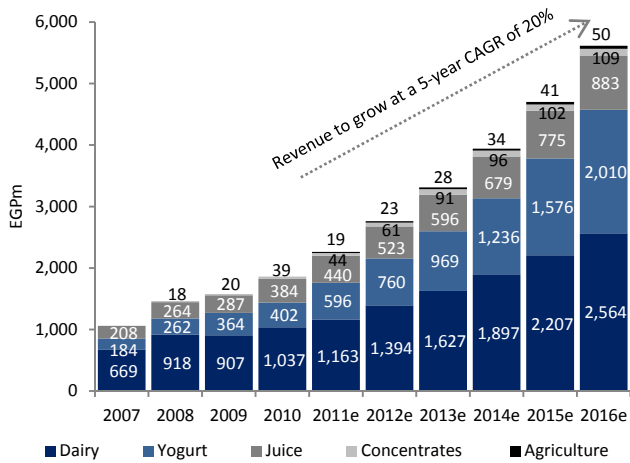
...than to packaged milk



Source: Juhayna, HC

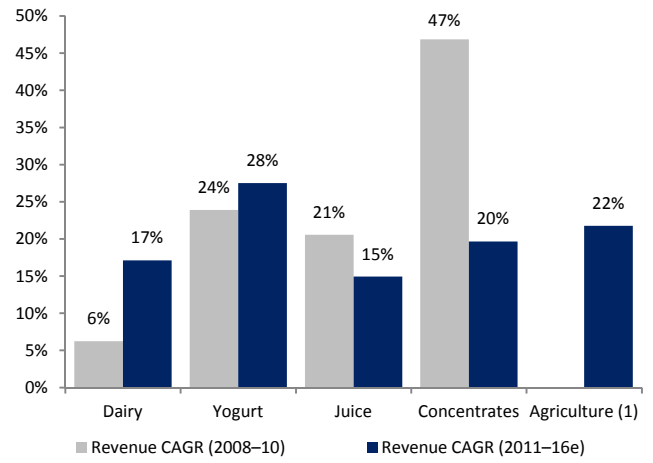


Sturdy growth to continue across all segments...



Source: Juhayna, HC

...with yogurt to deliver the highest growth



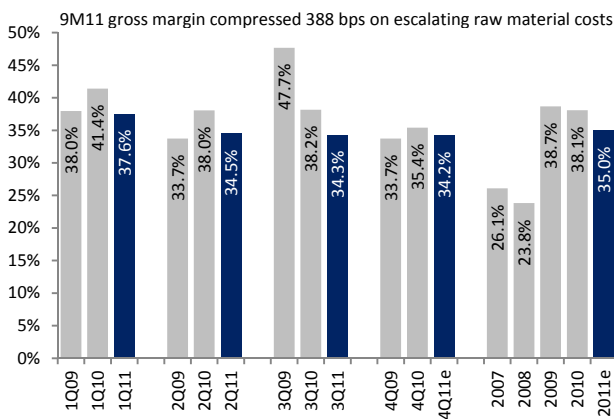
Source: Juhayna, HC

Note: (1) Commercial agricultural production began in 1Q11

Margin pressure likely to persist in 2012e as input costs remain high

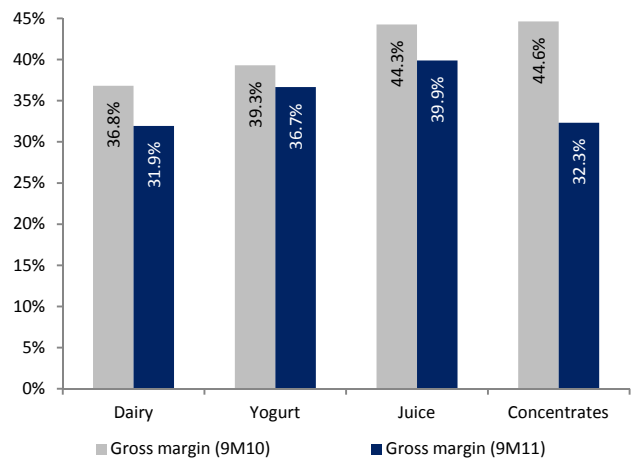
The cost of raw milk (Juhayna’s main input, c60% of COGS, 90% sourced externally) increased c18% y-o-y in 2011 on the back of significant animal feed cost inflation (see the charts on the following page) and heightened local unrest. The price of raw milk purchased from farms increased to an average of EGP3.25/kg in 3Q11 from cEGP3.0/kg in May and averaged cEGP3.1/kg in 2011 compared with cEGP2.6/kg in 2010, according to management.

Gross margins deteriorated significantly in 9M11...



Source: Juhayna, HC

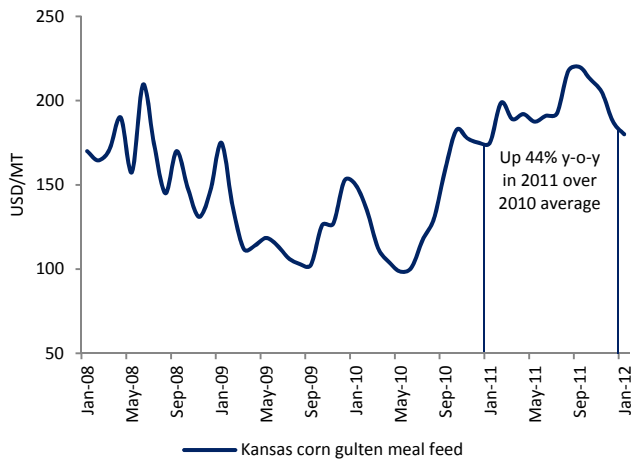
...across all segments



Source: Juhayna, HC

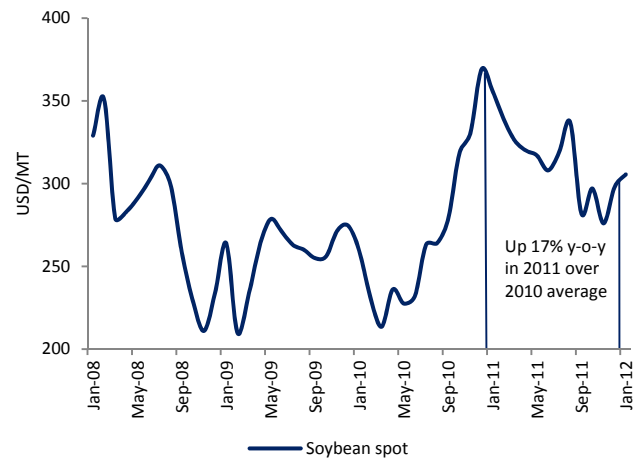


Corn prices



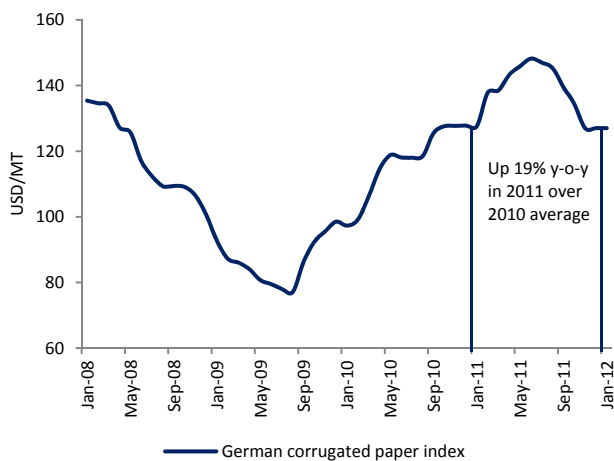
Source: Bloomberg, HC

Soybean prices



Source: Bloomberg, HC

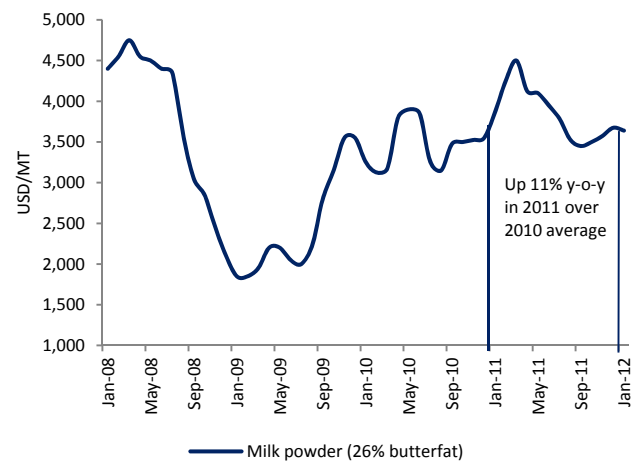
Corrugated paper prices⁽¹⁾



Source: Bloomberg, HC

Note: (1) Juhayna's corrugated paper packaging cost is based on an annually renewable agreement with Tetra Pak; packaging makes up c25% of total COGS

Powdered milk prices⁽¹⁾



Source: Bloomberg, HC

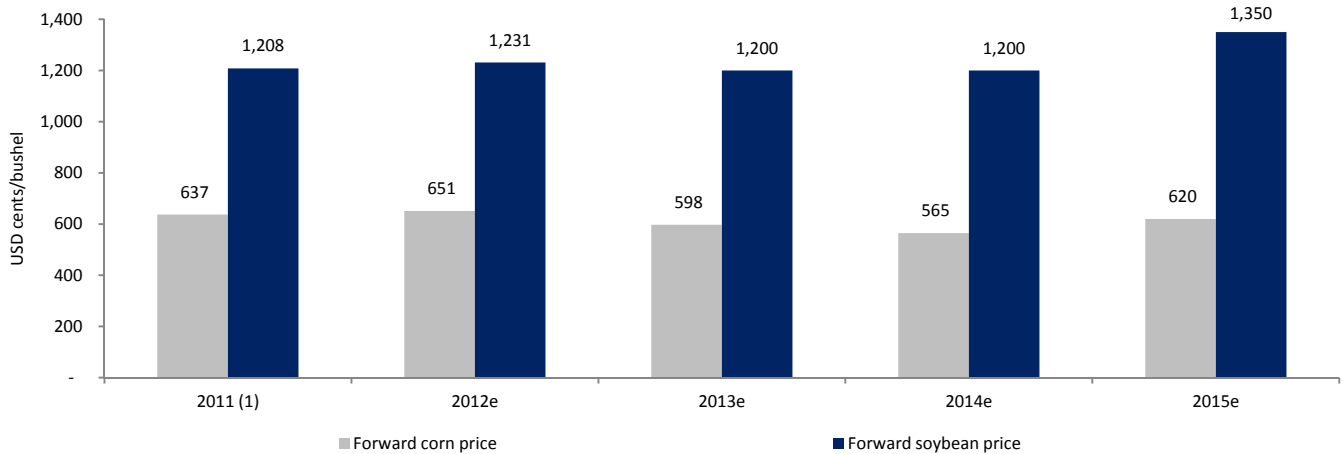
Note: (1) Powdered milk represents c20% of total milk used and makes up c60% of yogurt content

New raw milk pricing formula fixes purchase price at cEGP3.1/kg for 2012e

To reduce margins' susceptibility to volatility in raw milk purchase prices (with only c8%–10% of raw milk requirements sourced internally from 40% owned associate Milkys), management has started signing long-term contracts (with some 70 farms) to fix raw milk purchase prices biannually, based on a new raw milk pricing formula that varies with animal feed (mainly corn and soy) prices, which should help reduce – but not eliminate – margin variability, in our view. Based on the new raw milk pricing protocol, Juhayna's contracted raw milk purchase price is fixed at cEGP3.1/kg for 2012e, in line with the 2011 average, as animal feed prices are expected to remain almost unchanged. **Assuming a 2012e raw milk purchase price of EGP3.25/kg (equivalent to 3Q11's peak levels) would dilute Juhayna's aggregate gross margin 316 bps and lower our valuation 10%.**



No sign of easing in animal feed prices



Source: Bloomberg, HC
 Note: (1) Spot prices

Some risk from EGP depreciation...

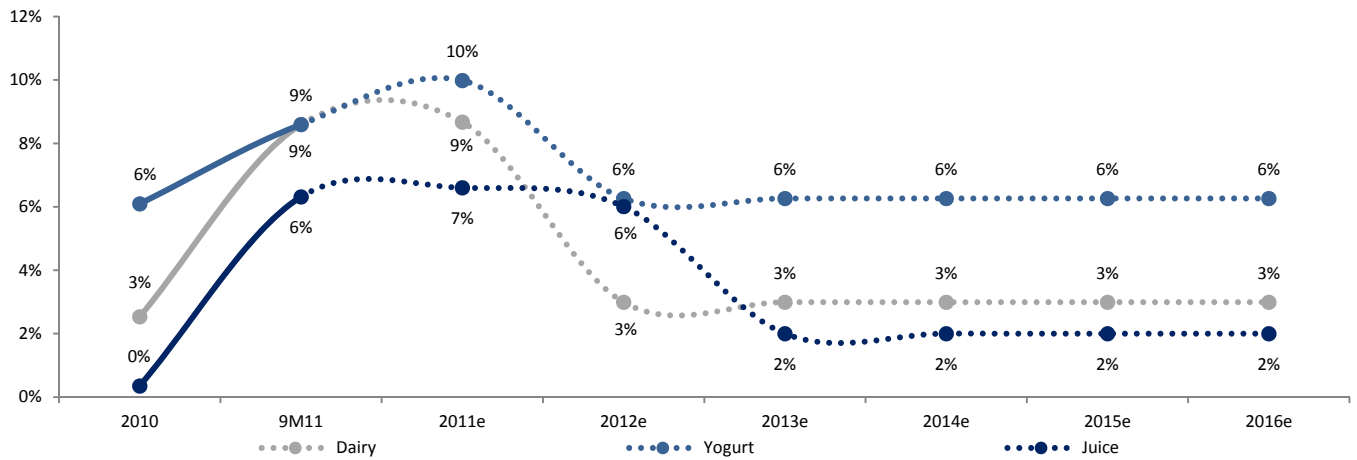
Juhayna is likely to experience additional cost-side pressure in 2012e on the back of further EGP depreciation, with USD denominated purchases comprising 25%–30% of the company’s cost base.

...but a margin surprise is likely given Juhayna’s pricing flexibility

We see limited risk to Juhayna’s margins from currency depreciation given the company’s ability to fully pass raw material and/or forex-related cost increases on to consumers through price increases, even if it bears them for the first few months. For example, the company did not recapture the 15% raw milk cost increase that occurred in May until June (when it raised the retail price of its 1 liter milk carton to EGP7.25) and later in November (when it raised the price of its low-end 0.5kg Bekhero milk package 5%). The company also managed to raise its yogurt selling prices c10% and juice prices 8% in 2011 and intends to raise selling prices further in 2012e.



Estimated y-o-y increase in average selling price by segment

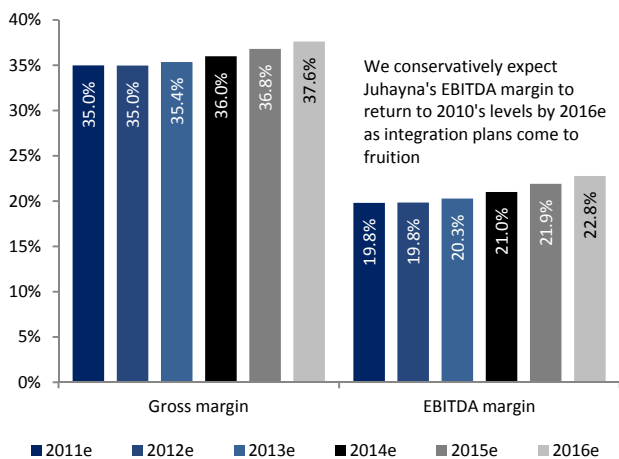


Source: Juhayna, HC

Expecting flat gross margin in 2012e

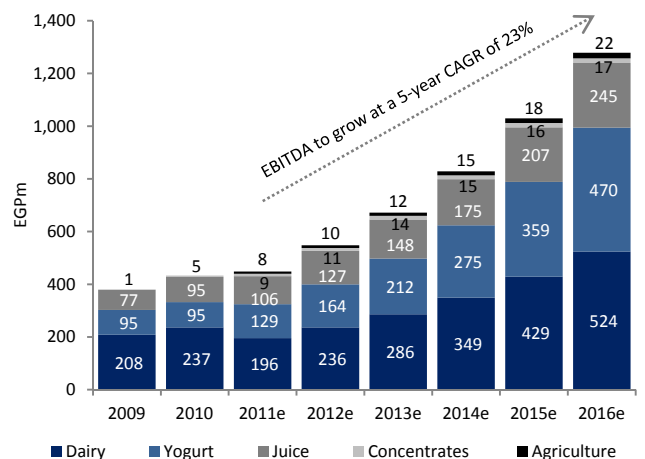
We conservatively expect Juhayna's gross margin to remain flat in 2012e given that no reversal is expected in commodity price trends and raw milk purchase prices are fixed at levels equivalent to those of 2011. However, management is guiding toward a slight improvement in gross margin from 2011, which we believe could happen if (1) global commodity prices soften (prices were down 14% y-o-y for soy and 6% y-o-y for powdered milk but were up 3% y-o-y for corn in January 2012) and/or (2) higher than expected price increases take place, especially for the company's higher-end products with more pricing flexibility, such as its 'Pure' juice and cream products.

Backward integration to enhance margins in the medium term...



Source: Juhayna, HC

...with dairy to remain the highest contributor to EBITDA



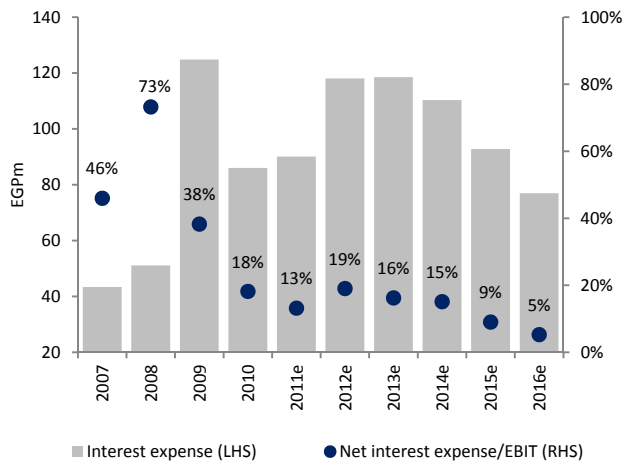
Source: Juhayna, HC



Interest cost hike to squeeze net margins in 2012–13e

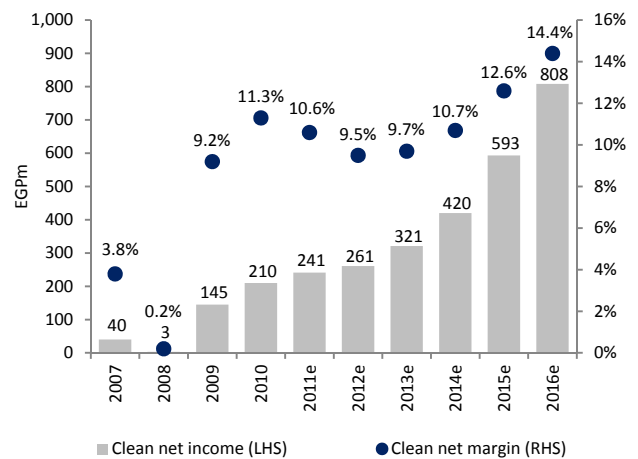
We expect Juhayna’s interest expense to rise c31% y-o-y in 2012e as (1) bank lending rates increase, in line with the central bank corridor, with the majority of the company’s debt in floating-rate loans and (2) the company’s debt balance grows to EGP907m with the addition of the EGP300m, 11.5% credit facility received in 4Q11 for the reconstruction of its yogurt factory.

Assuming a c130 bps increase in lending rates in 2012e



Source: Juhayna, HC

Juhayna’s net income and net margin⁽¹⁾



Source: Juhayna, HC

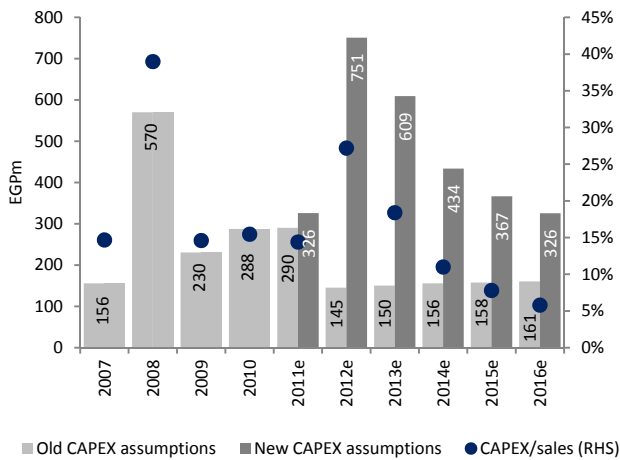
Note: (1) Both exclude nonrecurring items

Hefty CAPEX bill strains valuation

Juhayna is planning a 4-year spending program worth cEGP2bn, of which EGP750m is expected to be spent this year on (1) partial reconstruction of the company’s damaged yogurt plant at an estimated investment cost of EGP320m (construction began in 4Q11, with the factory expected to be operational by early 2013e), (2) the establishment of dairy farms and orchards at a total investment cost of EGP600m, (3) the renewal of its truck fleet (the company plans to add 100–120 new trucks in 2012e after it doubled its fleet to 813 vans in 2011), (4) 6 new distribution centers (on top of its existing 21), and (5) maintenance CAPEX.

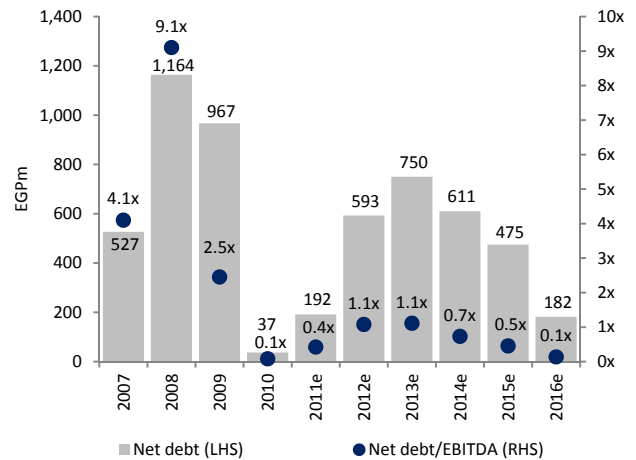


CAPEX to peak in 2012e



Source: Juhayna, HC

Company to stay in a net debt position until 2016e



Source: Juhayna, HC

Progress on backward integration project through dairy farming and orchards

Farms

- **Total area:** 18,500 feddans
- **Total CAPEX:** EGP600m
- **Rationale:** Vertical integration and margin expansion (300 bps upon completion)
- **Time frame:** 4–5 years (completion expected by 2015–16)

Dairy farm

- **Area:** 8,500 feddans
- **CAPEX:** cEGP300m
- **Rationale:** To supply 40%–50% of raw milk needs
- **Progress:** Design phase is complete; construction will begin in early 2012e; first batch of milking cows (3,600 cows) to be received by the end of 2012e; herd to reach c12,000 milking cows by the end of 2015e

Orchard and cattle feed farm

- **Area:** 10,000 feddans
- **CAPEX:** cEGP300m
- **Rationale:** To supply 40%–50% of fruit (orange, mango, and guava) needs and cattle feed
- **Progress:** 2,500 feddans already up and running; commercial agriculture began generating revenue in 1Q11 (currently selling soy, corn, and alfalfa; second plot of land to be received from the government soon)

Source: HC, Juhayna

Cut net income forecasts 26% to reflect lower margin expectations and higher interest and depreciation charges

We raise our 2011–15e revenue forecasts 3% on average to reflect (1) higher yogurt sales after factory reconstruction and a rapid trend of conversion to packaged yogurt and (2) a 4% annual increase in Juhayna's blended average selling price. We lower our EBITDA forecasts 5% on average as we adopt a more conservative outlook on margins until we see (1) a clear reversal in the margin deterioration trend and/or (2) faster than expected realization of integration benefits. We cut net income a wider 26% on average due to higher interest (up 63%) and depreciation (up 48%) costs as the company takes on more debt to finance expansion projects.



Estimate revisions (EGPm)

	New estimates					Old estimates				
	2011e	2012e	2013e	2014e	2015e	2011e	2012e	2013e	2014e	2015e
Revenue	2,263	2,761	3,311	3,943	4,701	2,259	2,701	3,209	3,814	4,533
Gross profit	792	965	1,171	1,419	1,730	842	1,006	1,201	1,437	1,726
<i>Gross margin</i>	35.0%	35.0%	35.4%	36.0%	36.8%	37.3%	37.3%	37.4%	37.7%	38.1%
EBITDA	448	548	672	828	1,030	493	586	703	850	1,034
<i>EBITDA margin</i>	19.8%	19.8%	20.3%	21.0%	21.9%	21.8%	21.7%	21.9%	22.3%	22.8%
Net income	241	261	321	420	593	299	359	465	602	776
<i>Net margin</i>	10.6%	9.5%	9.7%	10.7%	12.6%	13.2%	13.3%	14.5%	15.8%	17.1%

Source: HC

HC versus consensus estimates (EGPm)

	2011e			2012e			2013e		
	HC	Consensus	% dev.	HC	Consensus	% dev.	HC	Consensus	% dev.
Revenue	2,263	2,291	-1%	2,761	2,688	3%	3,311	3,117	6%
EBITDA	448	449	0%	548	525	4%	672	662	2%
<i>EBITDA margin</i>	19.8%	19.6%		19.8%	19.5%		20.3%	21.2%	
Net income (clean)	241	232	4%	261	269	-3%	321	364	-12%
<i>Net margin</i>	10.6%	10.1%		9.5%	10.0%		9.7%	11.7%	

Source: Bloomberg, HC



Valuation

We downgrade Juhayna to Neutral from Overweight and cut our TP 28% to EGP5.07/share (which offers 2% upside to the current market price) on the back of lower margin assumptions and higher CAPEX guidance. We raise our WACC 212 bps to 15.2% as we increase our risk-free rate to 12.6%, in line with after-tax 1-year T-bill rates, and raise our after-tax cost of debt 100 bps to reflect higher bank lending rates. We apply a market risk premium of 7.5%.

Juhayna valuation summary (EGPm)

	2012e	2013e	2014e	2015e	2016e
EBITDA	548	672	828	1,030	1,279
Taxes	(37)	(46)	(60)	(85)	(116)
Appropriations	(18)	(22)	(29)	(42)	(57)
Change in working capital	(74)	(86)	(88)	(93)	(98)
CAPEX	(751)	(609)	(434)	(367)	(326)
Free cash flows (FCFs)	(333)	(92)	217	443	684
WACC	15.2%				
Terminal growth rate	3.5%				
Present value of FCFs	(294)	(70)	144	256	343
Terminal value	6,745				
Present value of terminal value	3,381				
Enterprise value	3,760				
Excess cash ⁽¹⁾	618				
Debt ⁽¹⁾	842				
Net debt	223				
Investments ⁽¹⁾	42				
Total equity value	3,578				
Number of shares (m)	706				
Total value/share (EGP)	5.07				

Source: HC

Note: (1) As of 30 September 2011

Sensitivity of Juhayna's valuation to WACC and terminal growth rate (EGP/share)

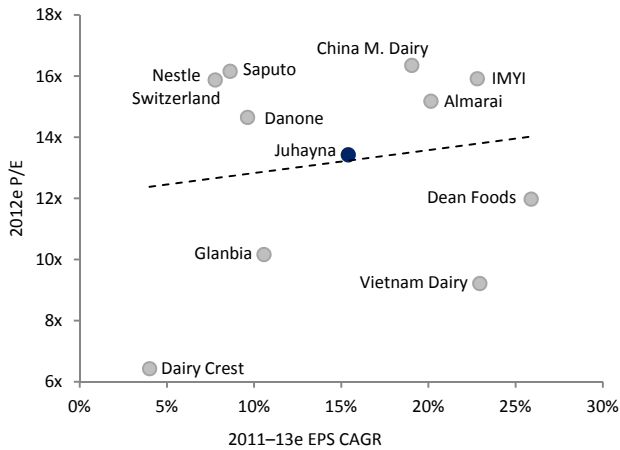
		WACC				
		13.2%	14.2%	15.2%	16.2%	17.2%
Terminal growth rate	1.5%	5.46	4.86	4.36	3.92	3.54
	2.5%	5.93	5.25	4.68	4.19	3.77
	3.5%	6.53	5.73	5.07	4.51	4.04
	4.5%	7.21	6.27	5.50	4.86	4.33
	5.5%	8.10	6.95	6.03	5.29	4.68

Source: HC



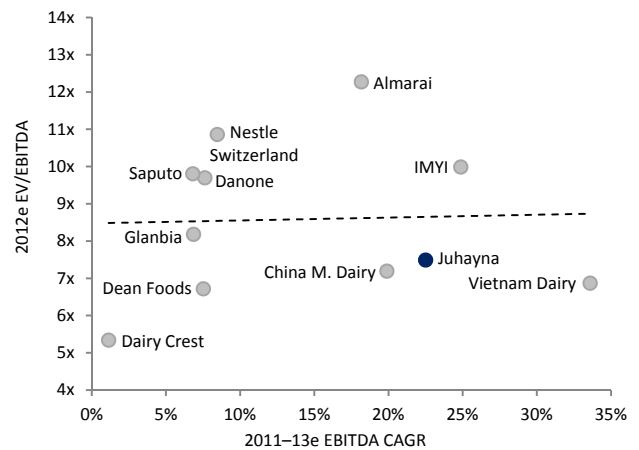
The stock is currently trading at a 2012e P/E of 13.4x, in line with peers' P/E versus EPS growth. However, the stock is trading at a 13% discount to global peers on EV/EBITDA versus EBITDA growth, which is now unwarranted given Juhayna's growing debt level (in line with the average leverage of international dairy peers). We expect the company to generate a FCF yield of -9% in 2012e and -3% in 2013e on the back of its increased CAPEX.

2011–13e EPS CAGR versus 2012e P/E



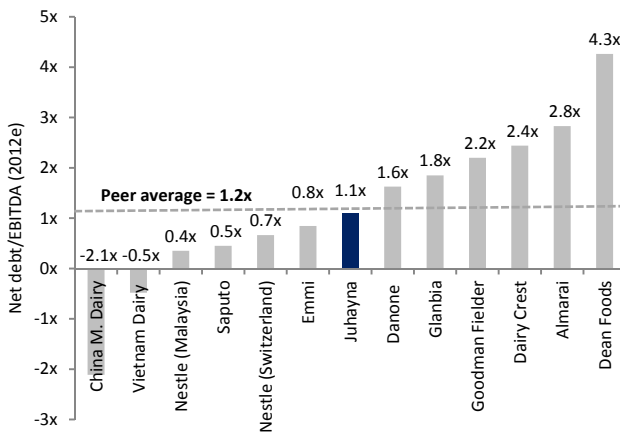
Source: Bloomberg, HC

2011–13e EBITDA CAGR versus 2012e EV/EBITDA



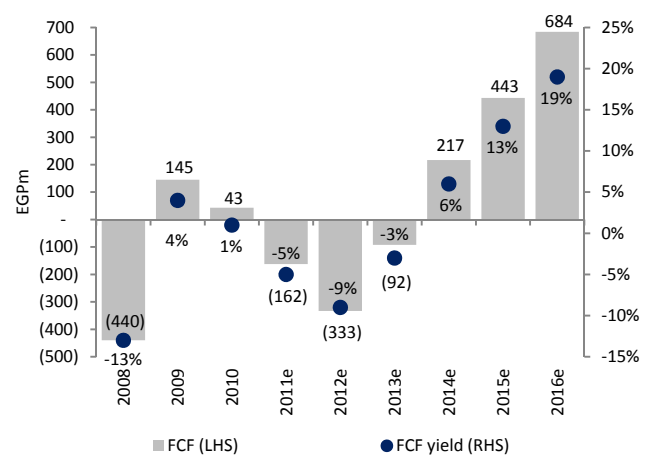
Source: Bloomberg, HC

Average leverage compared with global peers'



Source: Bloomberg, HC

FCF and FCF yield



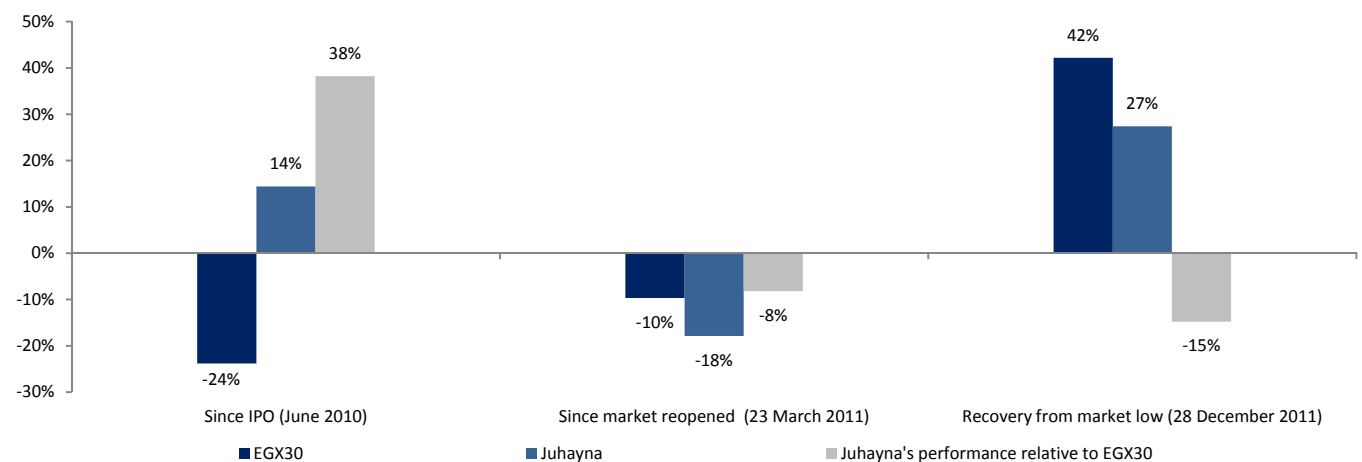
Source: HC



Outcome of monopolistic practices lawsuit is a looming concern

The stock has been heavily sold off since November – trading below its IPO price from 14 November 2011 to 30 January 2012 and hitting a historic low of EGP3.69/share on 22 November – following the referral to the general prosecutor of a monopolistic practices case in which Juhayna, Beyti, and Enjoy are accused of colluding to fix the purchase price of raw milk from farmers. Under Egypt’s antitrust law, a company can be fined EGP100,000–EGP300m (the latter representing c9% of Juhayna’s current market cap or 96% of its 2012e cash balance) if charged with monopolistic practices.

Juhayna’s share price performance versus EGX30



Source: Bloomberg, HC

Risks

Upside risks include (1) faster than expected margin recovery due to softening in global commodity prices, (2) higher than expected price increases across product categories, (3) accelerated margin benefits from vertical integration, (4) lower than expected interest charges, and (5) a favorable outcome in the dairy monopoly case.

Downside risks include (1) a sharper than expected impact on margins from currency depreciation and/or raw material cost inflation, (2) less flexibility to raise prices, (3) delayed margin benefits from vertical integration, (4) slower than expected conversion to packaged products, (5) a more adverse than expected impact of competition in the short to medium term, and (6) an unfavorable outcome in the dairy monopoly case.



Juhayna financial statements and ratios

EGPm	2010	2011e	2012e	2013e	2014e	2015e	2016e
Income statement							
Sales	1,861	2,263	2,761	3,311	3,943	4,701	5,616
<i>Growth</i>	18%	22%	22%	20%	19%	19%	19%
COGS	(1,152)	(1,471)	(1,796)	(2,141)	(2,524)	(2,971)	(3,504)
Gross profit	709	792	965	1,171	1,419	1,730	2,112
<i>Gross margin</i>	38.1%	35.0%	35.0%	35.4%	36.0%	36.8%	37.6%
SG&A expenses	(293)	(352)	(430)	(514)	(608)	(721)	(856)
Export subsidies	14	9	13	15	18	20	23
EBITDA	429	448	548	672	828	1,030	1,279
<i>EBITDA margin</i>	23.1%	19.8%	19.8%	20.3%	21.0%	21.9%	22.8%
<i>Growth</i>	9%	4%	22%	23%	23%	24%	24%
Depreciation	(126)	(139)	(183)	(242)	(273)	(299)	(322)
Other expenses	(167)	(14)	(18)	(19)	(21)	(22)	(24)
Other revenue	176	19	18	22	26	31	37
Associate income	3	4	4	4	5	5	6
EBIT	315	317	369	438	566	745	976
<i>EBIT margin</i>	16.9%	14.0%	13.4%	13.2%	14.4%	15.9%	17.4%
Interest income	29	48	48	47	25	25	25
Interest expense	(86)	(90)	(118)	(119)	(110)	(93)	(77)
Net interest expense	(57)	(42)	(70)	(71)	(86)	(68)	(52)
FX gains (losses)	(2)	(3)	-	-	-	-	-
EBT	255	272	299	366	481	678	924
Taxes	(28)	(31)	(37)	(46)	(60)	(85)	(116)
Net income before minorities	228	241	261	321	420	593	809
Minority interest	(0)	(0)	(0)	(0)	(0)	(0)	(0)
Reported net income	228	241	261	321	420	593	808
Extraordinary loss ⁽¹⁾	-	(38)	-	-	-	-	-
Net income after extraordinary loss	228	203	261	321	420	593	808
Clean net income⁽²⁾	210	241	261	321	420	593	808
<i>Net margin</i>	11.3%	10.6%	9.5%	9.7%	10.7%	12.6%	14.4%
<i>Growth</i>	45%	14%	9%	23%	31%	41%	36%
Balance sheet							
Cash and equivalents	724	587	314	164	170	170	356
Inventory	280	440	503	570	637	707	780
Receivables	63	58	66	77	89	104	121
Other current assets	236	241	240	246	253	262	272
Total current assets	1,303	1,325	1,123	1,056	1,149	1,242	1,529
Goodwill	97	97	97	97	97	97	97
Net fixed assets	1,289	1,469	2,036	2,404	2,565	2,633	2,637
Other noncurrent assets	39	43	48	52	57	62	68
Total noncurrent assets	1,425	1,609	2,181	2,553	2,719	2,792	2,802
Total assets	2,728	2,934	3,304	3,609	3,868	4,035	4,331
Short-term loans	377	486	403	441	440	409	376
Payables	108	117	125	135	148	167	192
Other current liabilities	138	107	97	86	324	412	522
Total current liabilities	623	709	625	662	913	988	1,090
Long-term debt	384	293	503	473	340	236	161
Other long-term liabilities	77	81	82	82	83	84	85
Total noncurrent liabilities	461	374	585	555	423	320	246
Total liabilities	1,084	1,083	1,210	1,217	1,336	1,308	1,336
Shareholder equity⁽³⁾	1,644	1,851	2,094	2,392	2,531	2,727	2,994

Source: Juhayna, HC

Note: (1) Extraordinary loss due to yogurt factory fire incident; represents difference between book value of damages and recovered amount net of tax

(2) Excludes nonrecurring items (3) Issued and paid-in capital reduced to EGP706m after adjustment for treasury stock cancellation



Juhayna financial statements and ratios (continued)

EGPm	2010	2011e	2012e	2013e	2014e	2015e	2016e
Cash flow statement							
Net income before minorities	228	241	261	321	420	593	809
Noncash items and others	217	216	310	357	380	389	396
Change in working capital	(71)	(236)	(74)	(86)	(88)	(93)	(98)
Operating cash flows	374	221	498	592	712	888	1,107
CAPEX	(288)	(326)	(751)	(609)	(434)	(367)	(326)
Other investments	58	6	1	1	1	1	1
Investing cash flows	(230)	(320)	(750)	(609)	(433)	(366)	(325)
Proceeds from capital increase	999	-	-	-	-	-	-
Change in debt	(273)	17	128	7	(133)	(136)	(107)
Dividends paid	(26)	-	-	-	-	(252)	(356)
Other	(187)	(56)	(148)	(141)	(140)	(134)	(134)
Financing cash flows	513	(39)	(20)	(134)	(273)	(522)	(596)
Change in cash	657	(137)	(273)	(150)	6	0	186
Key price ratios							
EV/EBITDA	8.3x	8.3x	7.5x	6.3x	5.0x	3.9x	2.9x
Clean P/E	16.7x	14.6x	13.4x	10.9x	8.3x	5.9x	4.3x
P/B ⁽¹⁾	2.3x	2.0x	1.8x	1.5x	1.4x	1.3x	1.2x
Dividend yield	0%	0%	0%	0%	7%	10%	14%
FCF yield	1%	-5%	-9%	-3%	6%	13%	19%
Key financial ratios							
Net debt/equity	0.0x	0.1x	0.3x	0.3x	0.3x	0.2x	0.1x
Net debt/EBITDA	0.1x	0.4x	1.1x	1.1x	0.7x	0.5x	0.1x
ROAA ⁽¹⁾	9%	9%	9%	10%	12%	15%	20%
ROAE ⁽¹⁾	21%	15%	14%	15%	18%	23%	29%

Source: Juhayna, HC

Note: (1) Adjusted for nonrecurring items and intangibles



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