

المركز الوطني للتخصيص
NATIONAL CENTER FOR PRIVATIZATION & PPP



Flour Mills Phase1

A case study issued by the Department of Knowledge Management
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برنامج التخصيص



المؤسسة العامة للحبوب
Saudi Grains Organization (SAGO)
الهيئة العامة للغذية والتغذية
المؤسسة العامة للغذية والتغذية



رؤية
2030
الملكة العربية السعودية
KINGDOM OF SAUDI ARABIA

المركز الوطني للتخصيص
NATIONAL CENTER FOR PRIVATIZATION & PPP

وزارة المالية
Ministry of Finance

وزارة البيئة والمياه والزراعة
Ministry of Environment, Water & Agriculture
الجمهورية العربية السورية
Syrian Arab Republic



Project



Flour Mills Phase1

Description

Flour Mills Phase 1: 1st Milling Company and Milling Company 3 both companies carry out flour milling, animal feed and grain storage. Together they comprise 7,650 tonnes/day (TPD) flour milling capacity, 1,800 TPD of animal feed capacity and 195,000 tonnes of storage capacity. This amounts to 51% of the country's milling capacity and 66% of its animal feed capacity.



- Sites: Jeddah, Qassim, Tabuk, Ahsa
- **4,200 TPD** milling capacity
- **600 TPD** animal feed

شركة المطاحن الثالثة
Milling Company 3
المملكة العربية السعودية



- Sites: Khamis, Jouf, Jumoum
- **3,450 TPD** milling capacity
- **1,200 TPD** animal feed

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Method:

Strategic Sale

Timing:

Tender Launched: November 2018

Closing: July 2020

► % of Sale :

100% Sold

100% Sold

► Proceeds:

SAR2.0b (USD540.1m)

SAR750.0m (USD199.9m)

► Implied Value:

SAR2.0b (USD540.1m)

SAR750.0m (USD199.9m)

► Buyer:

Raha al Safi Consortium

Al Rajhi/Ghurair/Masafi consortium

V2030 and sector policy

The privatization of the flour milling sector was announced in 2018 as part of the publication of the Privatization Program. The Program forms a key part of Vision 2030, which aims to diversify and transform the Saudi economy, partly by increasing the contribution of the private sector. Specifically, "The Privatization Program's overarching objective is to strengthen the role of the private sector by unlocking state-owned assets for investment. Privatizing selected government services will improve quality of services and reduce government's spending while taking into account citizens' interest; it will also help the government to refocus its efforts on its legislative and organizational roles. Moreover, the program will attract foreign direct investments and improve the balance of payments."

The privatizations of these and the Government's two remaining flour mills are part of a wider reform and liberalization of the sector that sees the Government exit direct operations to focus on policy and regulatory roles, as well as maintaining responsibility for food security via the strategic reserve. Bringing in private ownership of the four Government flour mills will increase competition within the sector, improving efficiency and maintaining downward pressure on prices to consumers.

The Sector

Prior to these privatizations the flour milling and animal feed sector was a Government monopoly. Demand was served by four State-Owned Enterprises (SOEs) with regional footprints:

- ▶ First Flour Mill: based in and around Jeddah. It has 4,200 TPD milling capacity, 28% of the total in Saudi Arabia, and 600 TPD animal feed capacity, 22% of the total.
- ▶ Milling Company 2: headquartered in Riyadh, with sites in Hail and Jazan. It has 4,350 TPD milling capacity, 29% of the total in Saudi Arabia, and 600 TPD animal feed capacity, 22% of the total.
- ▶ Milling Company 3: based in and around Khamis Mushaif. It has 3,450 TPD milling capacity, 23% of the total in Saudi Arabia, and 1,200 TPD animal feed capacity, 44% of the total.
- ▶ Milling Company 4: based in Dammam, Medina and Kharj. It has 3,150 TPD milling capacity, 21% of the total in Saudi Arabia, and 300 TPD animal feed capacity, 11% of the total.

CASE STUDY



Together these four companies comprised a government-owned monopoly of the market. Government also controlled grain imports, through the Saudi Grain Organization (SAGO). Milling companies 2 and 4 are also being privatized through a separate tender process.

The market for flour has been estimated at 2.7 million tonnes in 2019 and for animal feed, 17.1 million tonnes. Both markets have been growing steadily (see Figures 1 and 2 below). The amount of flour consumed has grown by an average of 0.6% a year from 2013 to 2019. Consumption of animal feed has grown by 3.3% a year on average over the same period. In 2019 the combined total market value amounted to almost SAR2 billion (USD533m).

Privatization Program (Delivery Plan 2020), April 2018

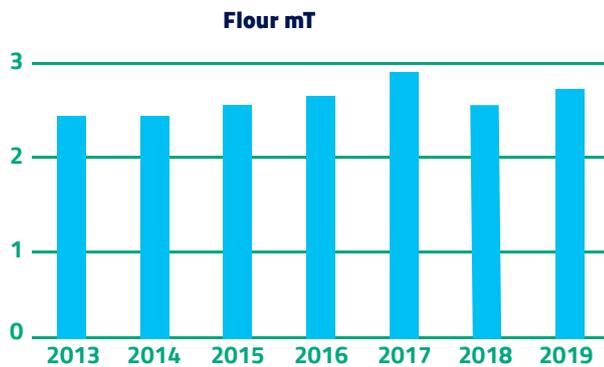


Figure 1: KSA Flour Market by volume, 2013-2019

Source: various

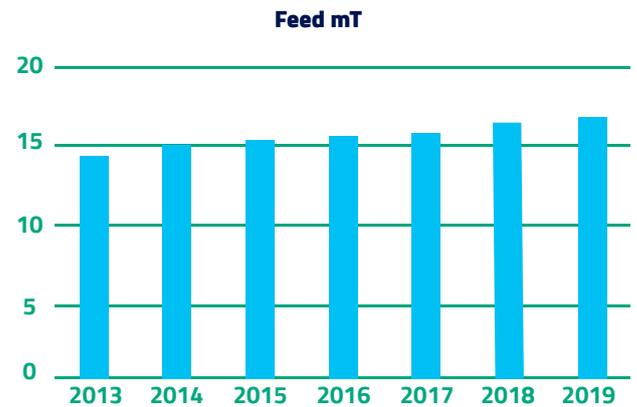


Figure 2: KSA Feed Market by volume, 2013-2019

Source: various



The flour mill privatizations form part of a fundamental reform of the sector by MEWA, the responsible Ministry, which aims to improve efficiency and competitiveness and increase private sector involvement, in line with Vision 2030 objectives. Key milestones of this reform include:

- ▶ 1972 Saudi Grains Organization (SAGO) established with a mandate to ensure food security by managing government's strategic wheat reserves and to produce flour and animal feed for the local market. Its responsibilities included being the sole importer of wheat to supply the milling operations.
- ▶ 2016 government's flour milling and animal feed operations were corporatized, establishing the milling entities as four separate companies.
- ▶ 2018 Flour Milling Law and implementing regulations, which provided for licensing of private flour mills, set quality standards and provided for regulation of tariffs. This established SAGO as the sector regulator, responsible for licensing mills and regulating standards and prices.
- ▶ 2020 shares in the four milling companies were transferred to NCP as an interim measure pending their privatization. This allowed SAGO to focus on its regulatory role, keeping it at arms' length from operations.
- ▶ 2020 wheat imports liberalized, allowing licensed mills to purchase wheat on world markets as well as from SAGO.

SAGO's new "arms' length" role as the sector regulator will focus on the following responsibilities:

- ▶ Issue milling licenses to the 4 milling companies.
- ▶ Manage the strategic reserve for wheat.
- ▶ Regulate tariffs for flour products, until the market is fully liberalized.
- ▶ Monitor the performance of the privatized flour mills to ensure they comply with licensing requirements.

In a parallel development, two major SOEs have established a joint venture (JV) called the National Grain Company (NGC) that will invest in logistics infrastructure for grain imports. Bahri, the national shipping company, and SALIC, an agriculture investment fund, are equal partners in the JV. NGC's first investment will be a new grain terminal at Yanbu commercial port with an initial capacity of 3 million tonnes per year when it begins operations in 2022, increasing to 5 million subsequently. The initial investment cost is estimated at SAR412.5 million (USD110 million).

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The Companies

First Flour Mill

Table 1: First Flour Mill Facilities

Location	Established	Capacity (tonnes/day)	
		Wheat	Animal Feed
Jeddah	1979	2,100	--
Qassim	1983	900	600
Tabuk	1998	600	--
Ahsa	2016	600	--
Total capacity	--	4,200	600

Figure 3: First Flour Mill Sales 2017-2019



The First Flour Mill saw a significant increase in sales in 2019, increasing capacity utilization and improving its financial performance. Its proximity to Jeddah port provides a strategic advantage in reducing transport costs for grain once it has been imported. At the same time, the Jeddah facility is over 40 years old and in need of investment. Qassim (37 years) and Tabuk (22 years) are also quite old.

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Milling Company 3

Table 2: Milling Company 3 Facilities:

Location	Established	Capacity (tonnes/day)	
		Wheat	Animal Feed
Khamis	1979	1,650	1,200
Jouf	1983	600	--
Jumoum	1998	1,200	--
Total capacity	--	3,450	1,200

Figure 4: Milling Company 3 Sales 2017-2019



The Third Milling Company has some relatively new assets, at Jumoum (5 years old) and Jouf (12 years), although its largest unit at Khamis is older, at 39 years. It does have the largest animal feed capacity of the four mills, with 44% of the national total. Sales and profitability have been falling in recent years.

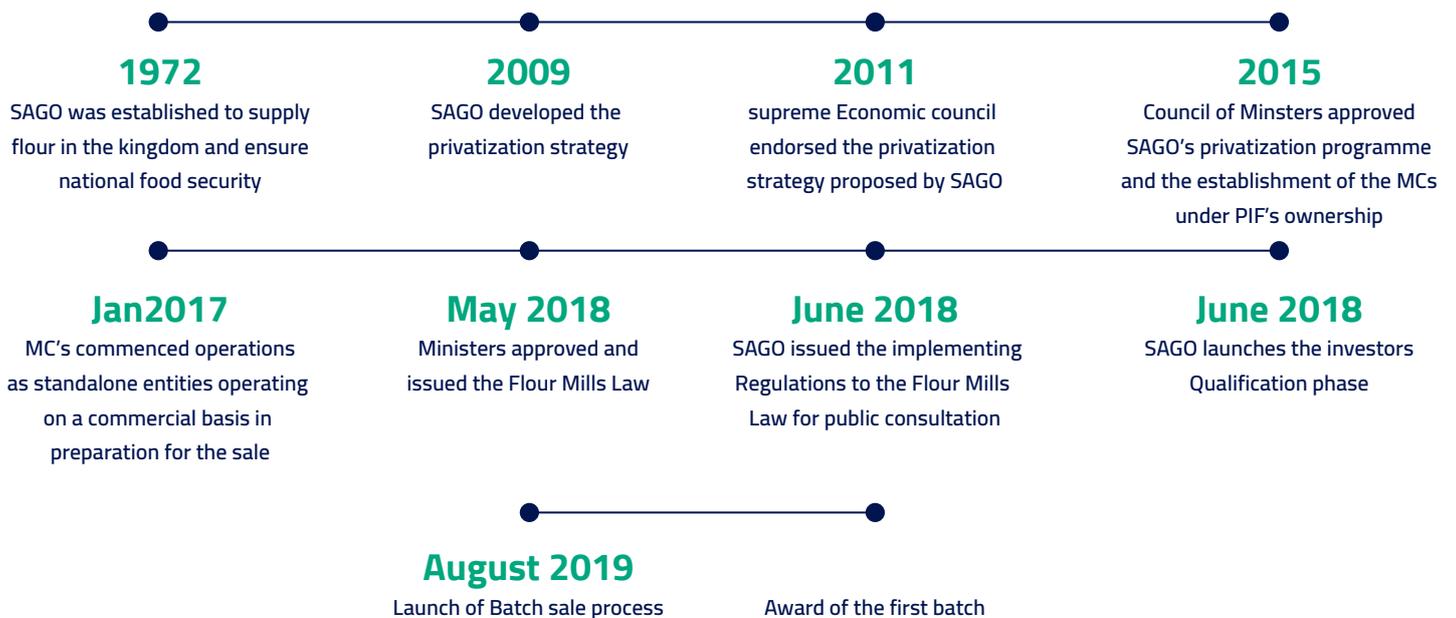
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The Privatization

The two companies were tendered in parallel and sold to different investors. The tender for the two remaining mills was launched in July 2020. Both privatizations involved the sale of 100% of the government's equity. The key milestones are illustrated in Figure 5 below.

Although the transactions were completed as part of the Vision 2030 Privatization Program, planning and preparation started as far back as 2009, when SAGO first developed the strategic sale strategy.

Flour Mill Privatization Milestones



When SAGO was established in 1972 it was a single company. The four milling companies were carved out and corporatized in November 2016 as part of a restructuring that began once the Council of Ministers agreed the privatization plan. They started operating as separate companies in January 2017. Their shares were transferred to NCP on 6th June 2020 as a temporary arrangement to facilitate privatization and allow SAGO to complete its transformation into a regulatory body.

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The approach to privatization that was adopted was for a sale of shares to strategic investors. This will facilitate the investment needed to modernize and improve the operations of the older sites. The tender was launched in June 2018 with a pre-qualification stage, where interested parties were invited to demonstrate their capabilities. There was strong interest from both international and local investors, including major global players in the sector such as Archer-Daniels-Midland (ADM), Bunge and Louis Dreyfus Company (LDC).

The proposal stage was launched in August 2019. After initial technical and financial bids and negotiations, final financial bids were submitted on 5th July 2020 and the transactions were completed shortly after.

The successful bidder for First Flour Mill was the Raha AlSafi consortium, led by the Almutlaq Group and also including Al Safi, Abunayyan Holding and Essa Al Ghurair Investment, which offered SAR2.0 billion (USD540.1m) for the shares. Almutlaq is a large, diverse Saudi conglomerate that has investments in manufacturing, utilities, finance and retail. Al Safi Danone is a joint venture between the Al Faisaliah Holding Group and the International Danone Group that is a major player in the Saudi dairy sector. Abunayyan Holding is a major investor in the Saudi power and water sectors, and also has significant operations in manufacturing, chemicals and construction. Essa Al Ghurair Investment is a Dubai-based group with ventures in maize mills, food and coffee, among others.

The successful bidder for Milling Company 3 was a consortium of Al Rajhi/Ghurair/Masafi, which offered SAR750.0 million (USD199.9m) for the shares. Al Rajhi Group is a Saudi-based holding company with diverse investments in manufacturing (food, packaging), transport and services. Al Ghurair operates flour mills and animal feed businesses in the UAE and also has investments in grain trading, property development and construction. Masafi is a Dubai-based producer of beverages and hygiene products.

CASE STUDY

Future Plans

The tender for the remaining two milling companies was launched in September 2020 and the coming months should see them also transferred to private sector ownership.

It is anticipated that the new owners will invest in upgrading and improving operations and efficiency. This will improve profitability and prepare the companies for competition. From a government-owned monopoly, flour milling and animal feeds will become a competitive industry. Initially this will be between the four existing milling companies under their new ownership. However, government may subsequently license other players to enter the market.

It is expected that the new owners will float shares on the stock exchange over the medium-term. This will allow financial and retail investors to buy shares and receive dividends.

Benefits

Strategic: The privatization is firmly in line with Vision 2030 and was included in the Privatization Program.

Key Vision 2030 objectives that it contributes to include:

Table 3: Contribution to V2030 Objectives

Objective	Contribution			
Transfer government assets to private sector	100% of the equity sold to private investors.	☑	☑	☑
Privatize certain government services	Two flour mills fully privatized.	☑	☑	☑
Reduce government spending	New owners responsible for any losses.	☑		
Create new jobs	Will depend on performance of the sector.			
Improve quality of service	Previously govt. monopoly, now private.	☑	☑	☑
Develop KSA as a thriving logistics centre	Investment, competitive pressure from liberalizing sector.	☑		
Attract foreign investment	Investment in new grain terminal by National Grain Company at Yanbu.			
Improve government entities' performance	Transfer from fully public to fully private, new owners should improve performance.	☑	☑	☑
Diversify government revenues	Proceeds from the transaction, license fees.	☑		

The privatization is also part of a major reform of the milling sector. Government has stepped back from directly operating in the sector to focus on regulation and food security roles, allowing the industry to become fully private and competitive.

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Economic: Some of the key economic benefits are expected to include:

- ▶ Investment to modernize the older facilities, and in new systems and equipment.
- ▶ Improvements in operating efficiency, driven by investment, private sector management and competitive pressure.
- ▶ Downward pressure on prices of milled products and animal feed, driven by competition and SAGO's new regulatory focus.
- ▶ Subsequent stock market listing, spreading ownership among individuals and institutions and helping to deepen the Tadawul stock exchange.

Social & Environmental: Flour milling is not a sector with a significant environmental footprint. However, investment in more efficient new equipment and facilities will help to reduce greenhouse gas emissions.

Fiscal: the key fiscal impacts of the privatization will comprise:

- ▶ Direct cash injection of SAR2.75 billion (USD740 million) as the proceeds from the sale.
- ▶ Annual license fees imposed by SAGO.
- ▶ Removal of a contingent liability - government no longer has an implicit obligation to step in if the companies were to make large losses, since this responsibility has been fully passed to the new private owners.