

January 24, 2017

Rating **Neutral**
12- Month Target Price **SAR 72.00**

SOUTHERN PROVINCE CEMENT COMPANY (SOUTHERN)
4Q2016 First Look

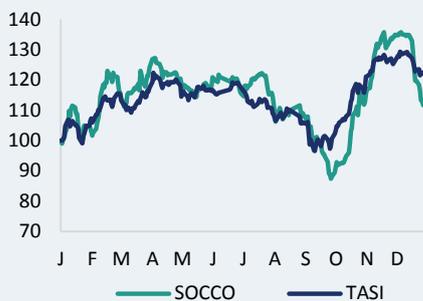
Expected Total Return

Price as on Jan-23, 2017	SAR 73.99
Upside to Target Price	(2.7%)
Expected Dividend Yield	6.1%
Expected Total Return	3.4%

Market Data

52 Week H/L	SAR 82.8/53.2
Market Capitalization	SAR 10,069 mln
Enterprise Value	SAR 10,359 mln
Shares Outstanding	140.0 mln
Free Float	46.8%
12-Month ADTV (000's)	51.7
Bloomberg Code	SOCCO AB

1-Year Price Performance



Source: Bloomberg

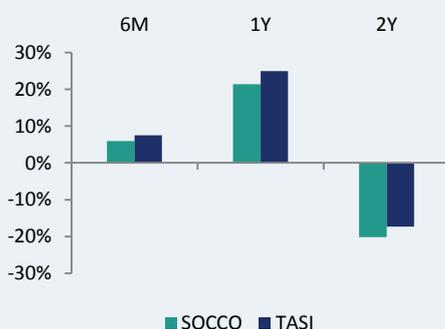


Fig in SAR mln	RC. Est	Actuals
Revenue	428	354
Gross Profit	235	180
EBIT	241	156
Net Income	193	156
EPS (SAR)	1.38	1.11

Tough Trends Ahead

Southern Cement Company (Southern) announced 4Q2016 preliminary numbers, with earnings missing RC and street expectations. EPS of SAR 1.11 came in lower to our SAR 1.38 estimate and streets SAR 1.37. A key synopsis of 4Q2016 for investors are i) the large drop in the sales volumes with -30% Y/Y decline ii) -5% Q/Q decline in realization to SAR 230/ton and lii) 34% Y/Y decline in revenue and -48% Y/Y decline in earnings, the lowest revenues and earnings reported in the recent history. We revise our outlook and trim our 2017-19 estimates due to slowing cement demand in 2017. However, Southern managed to retain some of its superior pricing capabilities despite the sector seeing swings in the range of SAR 154/ton (Yanbu) and industry average at SAR 190/ton during 4Q2016. We revise our target price to SAR 72.00 (earlier SAR 75.00) but maintain our Neutral rating.

Southern witnessed large erosion in market share

Revenue declined by -7% Q/Q and -34% Y/Y, on lowering volume sales and drop of -5% in realization to SAR 230/ton in 4Q2016. As a result, revenue of SAR 354 million in 4Q2016 came in lower to our estimate of SAR 428 million. Southern missed to upscale its volumes sales, being the only large-scale producer to report a drop of -2% Q/Q in dispatches, when industry volumes increased by +19%. However, this is a decent strategy when it has lower operational concerns on inventory, meaning less disruption on realization. Our adjusted inventory backlog versus 2016 sales volumes stands at 28% as of 4Q2016, the lowest in the sector, making Southern prone to lesser operational risk. However, it lost 2.5% volume market share to 11.9% from 14.5% in the last quarter, while Yanbu managed to increase 5% in market share, suggest cross selling in respective demand centers.

Gross Margins improve sequentially

Gross profit of SAR 180 million missed our SAR 235 million estimate. It declined by -2% Q/Q due to realization higher than industry. However, a -44% Y/Y decline is due to change in depreciation policy, an additional depreciation impact of SAR 20 million from 42 million in 4Q2015 to SAR 62 million in 4Q2016. Gross margins improved to 51% from 48% in 3Q2016 but lower than 59% in 4Q2015 on added impact of depreciation and energy prices hikes.

Earnings miss estimates

Operating profit of SAR 156 million missed our SAR 241 million estimate. Margins declined to 44% from 46% in 3Q as stable cash costs of SAR 129/ton in 4Q deemed supportive, while a -49% Y/Y fall in operating profit is a result of an impact of +23% increase in cash costs, a mix of delivery costs and price discounts. The overall impact has led to earnings decline of -10% Q/Q and -48% Y/Y, with earnings missing street and consensus by large margin. Net margins declined to 44% in 4Q from 46% in 3Q.

Yields attractive, maintain Neutral

We cut DPS to SAR 4.50 for 2017E, yielding 6.1% but recent rally had priced in most positives. We maintain a Neutral rating as current valuations looks unattractive with 2017E P/E of 13.6x at par with TASI's 14.3x.

Key Financial Figures

FY Dec31 (SAR mln)	2015A	2016A	2017E
Revenue	2,047	1,777	1,674
EBITDA*	1,222	1,080	980
Net Profit	1039	880	762
EPS (SAR)	7.42	6.29	5.44
DPS (SAR)	6.00	5.50	4.50
BVPS (SAR)	23.06	23.85	24.79

*2016 FBITDA is an estimate

Key Financial Ratios

FY Dec31	2015A	2016A	2017E
ROAA	24%	18%	16%
ROAE	32%	26%	22%
P/E	10.0x	11.8x	13.6x
P/B	3.2x	3.1x	3.0x
EV/EBITDA	8.2x	9.3x	10.3x
EV/Sales	4.9x	5.7x	6.0x

Santhosh Balakrishnan

santhosh.balakrishnan@riyadcapital.com
+966-11-203-6809

Khalid A AlMadhyan

khalid.a.almadhyan@riyadcapital.com
+966-11-203-6813

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Stock Rating

Buy	Neutral	Sell	Not Rated
Expected Total Return Greater than 15%	Expected Total Return between -15% and +15%	Expected Total Return less than -15%	Under Review/ Restricted

* The expected percentage returns are indicative, stock recommendations also incorporate relevant qualitative factors

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