April 30, 2017

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Rating	**Neutral**
12- Month Target Price	**SAR 8.50**

Saudi Kayan Petrochemical Company (Kayan)

1Q2017 First Look

Expected Total Return	
Price as on April-27, 2017	SAR 8.88
Upside to Target Price	(4.3%)
Expected Dividend Yield	0.0%
Expected Total Return	(4.3%)

Market Data	
52 Week H/L	SAR 9.45/5.05
Market Capitalization	SAR 13,320 mln
Enterprise Value	SAR 38,890 mln
Shares Outstanding	1,500 mln
Free Float	65.0%
12-Month ADTV (mln)	12.6
Bloomberg Code	KAYAN AB

1-Year Price Performance

Source: Bloomberg

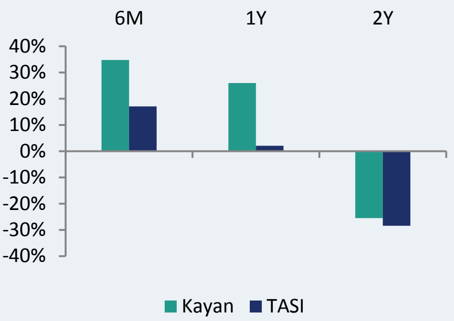

Fig in SAR mln	RC. Est	Actuals
Revenue	2,428	2,667
Gross Profit	461	727
EBIT	372	555
Net Income	157	265
EPS (SAR)	0.10	0.18

Heavy Boost in Margins

Saudi Kayan Petrochemical Company (Kayan) reported its preliminary 1Q2017 results, with an earnings surprise on improving cost efficiency. EPS of SAR 0.18 was above our estimate of SAR 0.10 and consensus of SAR 0.08. Key possibilities that have driven the positive surprise are i) a successful combination of stable prices and probable increase in utilization rates, could have driven costs heavily down ii) record jump in operating margins to its best at 21%, despite elevated feedstock prices iii) revenues improved by +9% Q/Q and +58% Y/Y on strong MEG and PC prices (SABIC MEG prices (average) up on a Q/Q basis by +31% and PC by +9% in 1Q2017). Kayan continues its record triumph of earnings surprises over the last four quarters with a strong net margin growth; surged from 4% in 2Q2016 to 10% in this quarter. With such improvement, we further revise our estimates and raise our target price to SAR 8.50 (earlier SAR 7.50), as 1Q2017 provides a head start to long-term benefits of cost optimization. Stock prices rallied by +35% versus TASI's +16% over last 6 months pointing to investor's optimism on earnings growth. However, we maintain Neutral as grace period for fuel subsidy ends in the next quarter and could start burdening margins from 3Q2017. Valuations looks overridden with 2017E P/E of 16.0x is expensive to TASI's 14.4x, suggest premium is unwarranted. Maintain Neutral.

Revenue slightly above estimates

Revenue of SAR 2.67 billion came above our estimate of SAR 2.42 billion, a +58% Y/Y and +10% Q/Q growth on stable PE and PP prices, while strong growth in MEG prices have led to a decent growth. We expect higher volume sales to have driven such impressive performance, including a +2% growth in PP and +1% growth in PE.

Successful cost optimization

Kayan has shown a large improvement with its focus on cost optimization which led to record growth in margins, as gross margins at 27% in 1Q2017 remain the best since listing. Gross profit witnessed a growth of +60% Q/Q and almost a ten-fold increase Y/Y from SAR 78 million in 1Q2016. This is despite a +36% Q/Q growth in butane prices in 1Q2017 as its feedstock mixture is 85% butane and the only producer in KSA with this structure. It is prone to a margin drop from 2H2017 as new pricing comes in to effect.

Net margins double over the quarter

Kayan reported a surprising set of operating numbers, with operating profit of SAR 555 million, growth of +59% Q/Q, returning from a loss of SAR (24) million recorded in 1Q2016. Operating margins improved 660 bps to 21% in 1Q2017 from 14% in 4Q2016. Earnings of SAR 265 million spiked by +156% Q/Q and is a large improvement from a loss of SAR (216) million recorded in 1Q2016. Earnings topped our estimate of SAR 157 million and consensus of SAR 128 million. Net margins in 1Q2017 almost doubled to 10% from 4% in 4Q2016, a positive.

Raising target price to SAR 8.50, but maintain Neutral

Kayan's stock price has rallied by +31% in 2016 and +73% in 4Q2016. We believe, this rally has priced-in most positives, investors should wait to re-enter. We raise target price to SAR 8.50, but maintain Neutral as valuation looks overridden.

Key Financial Figures

FY Dec31 (SAR mln)	2016A	2017E	2018E
Revenue	8,609	10,721	10,937
EBITDA*	3,346	4,173	4,276
Net Profit	134	835	925
EPS (SAR)	0.09	0.56	0.62
DPS (SAR)	-	-	-
BVPS (SAR)	9.39	9.93	10.51

Key Financial Ratios

FY Dec31	2016A	2017E	2018E
ROAA	2%	5%	6%
ROAE	6%	6%	6%
P/E	99.4x	16.0x	14.4x
P/B	0.9x	0.9x	0.8x
EV/EBITDA	10.2x	8.2x	8.0x
EV/Sales	4.0x	3.2x	3.1x

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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*

For any feedback on our reports, please contact research@riyadcapital.com

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