الراجحي المالية
Al Rajhi Capital

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Key themes

This is our monthly update on Cement production, volumes and inventory in Saudi Arabia.

What do we think?

Stock	Rating	Price Target
Yamama	Neutral	SAR 21.5
Arabian	Neutral	SAR 46.5
Southern	Neutral	SAR 73.0
Saudi	Neutral	SAR 63.0
Qassim	Neutral	SAR 60.0
Yanbu	Neutral	SAR 37.0

Saudi Cement sector:
Expect limited benefit from exports

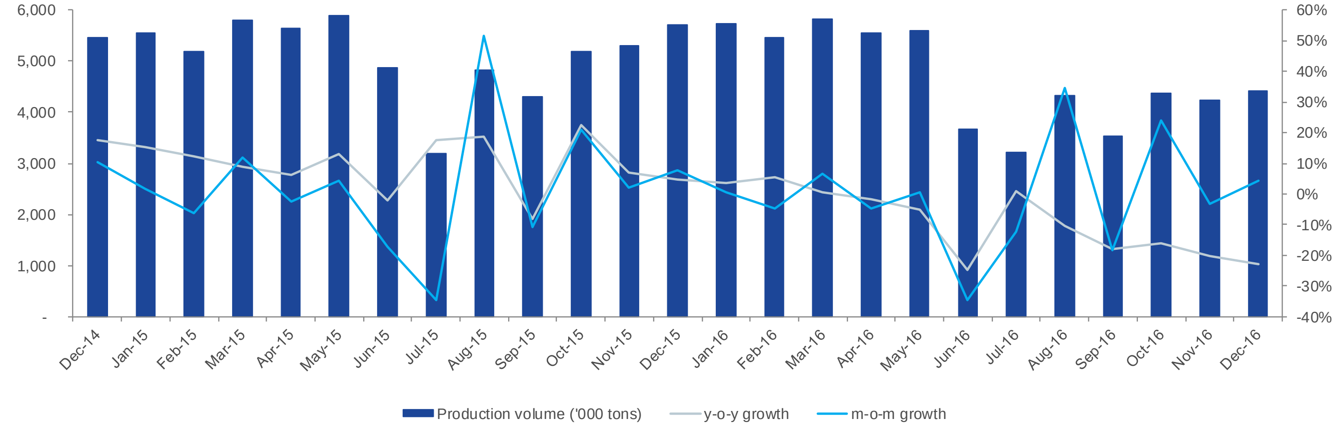
Ministry of Commerce decided to allow Cement & Steel companies to export their products on the condition of paying the difference between fuel costs in local and international markets. The ministry estimated the export fees to be between SAR85-SAR133 per ton of cement. As we mentioned earlier, we see limited financial benefit for cement producers from lifting the ban on exports as we estimate the average operating profit of producers at about SAR 90 per ton during 9M 2016. Moreover, exports will incur higher transportation costs as well, which on average is estimated by industry experts at about SAR 7/ton for 100km within the Kingdom.

According to the latest monthly data released by Yamama Cement, total cement dispatches in the Kingdom fell 25% y-o-y, but grew 3.6% m-o-m to 4.3mn tons in December. Total inventory rose 23.6% y-o-y and 1.6% m-o-m to a new record of 29.2mn tons, representing 53% of the last 12 months' sales. Clinker production in the Kingdom came in at 4.7mn tons during December, down 7% y-o-y (+8% m-o-m) and we expect it to slowdown further. Surprisingly, Yanbu cement continued to report double-digit growth in sales volume for the second month in a row by 13% and 11.3% respectively in November and December. We believe that this growth was driven by offering deep discounts on dispatches. On the other hand, Hail and Northern cement witnessed the sharpest decline in sales of -60% and -57% y-o-y, respectively. In 2017, we expect cement demand to remain modest given that construction activities are bound to remain weak for the foreseeable future as the government spending adjusts to low oil prices through spending cuts and prioritization of projects.

Key takeaways:

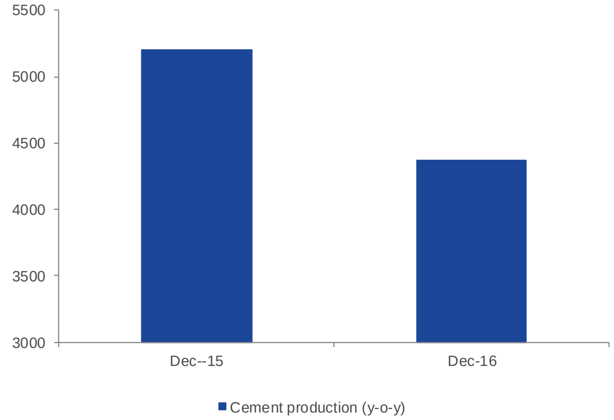
- In 2016, cement sales volume fell 10% y-o-y to 54.8mn tons (vs. 60.7mn tons in 2015), while clinker production slightly declined 2.5% y-o-y. Moving forward, we believe that balancing the market through production cuts is the best option especially with the continuous increase in inventories (29.2mn tons). However, some companies may tend to maintain current production levels prior to the potential impact from another round of energy price hikes in late 2017.
- Ministry of Commerce and Investment announced that five Cement companies applied for the new export license (Al Eqtisadiah newspaper). We anticipate limited benefit from exports due to the high export fees (SAR85-133 per ton) and given that the average operating profit per ton in the sector is only about SAR90 per ton during the first nine months of 2016. Further, transportation costs, sluggish demand and political instability in the neighboring regions, excess supply and competitive pricing in the region are other challenges to export.
- In 2017, we expect cement producers in the Western region to be under pressure as two new players (Umm AlQura & United cement) commenced commercial production in 2016 which will lead producers in the region to compete on pricing.
- Transportation costs for smaller players to far away main demand regions coupled with higher discounts in these regions are likely to lead these small players to witness further contraction in profit margins.

- **Figure 1 Cement production volume (absolute, y-o-y, m-o-m)**



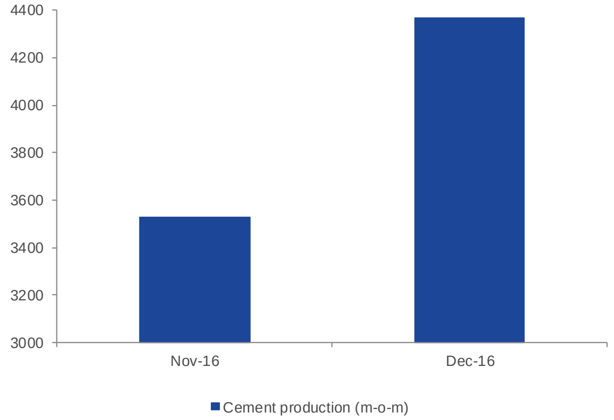
Source: Company data, Al Rajhi Capital

Figure 2   Cement production ('000 tons, y-o-y)



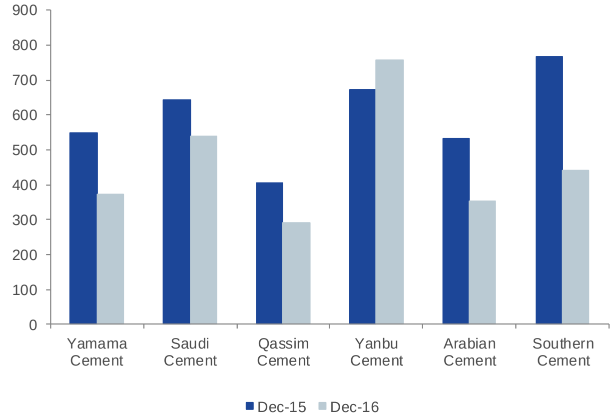
Source: Yamama data, Al Rajhi Capital

Figure 3   Cement production ('000 tons, m-o-m)



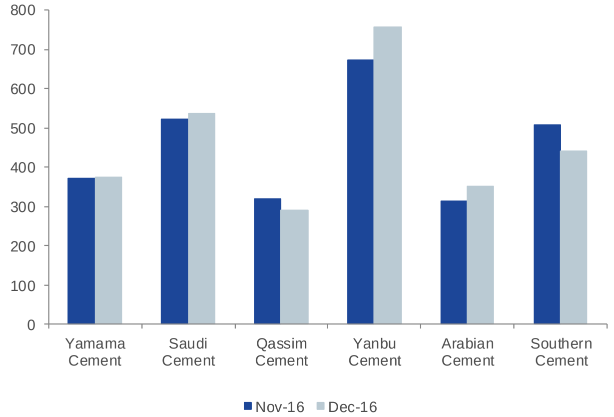
Source: Yamama data, Al Rajhi Capital

Figure 4   Cement production ('000 tons, y-o-y)



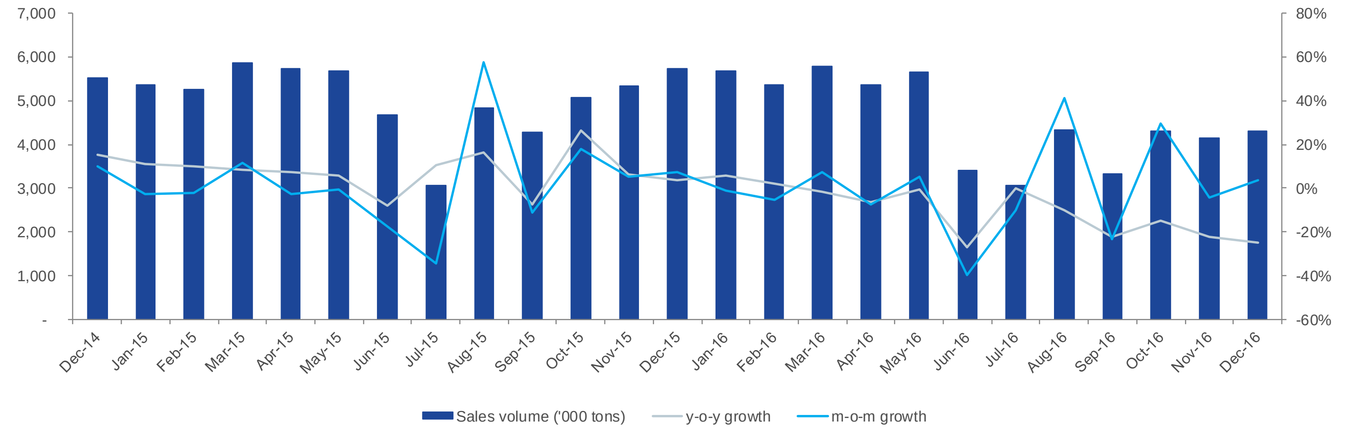
Source: Yamama data, Al Rajhi Capital

Figure 5   Cement production ('000 tons, m-o-m)



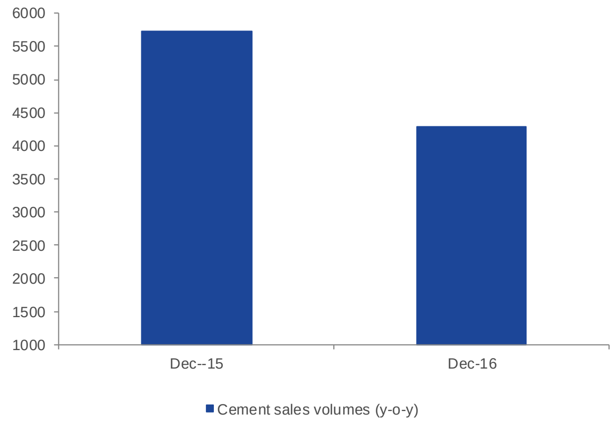
Source: Yamama data, Al Rajhi Capital

Figure 6 Cement sales volumes (absolute, y-o-y, m-o-m)



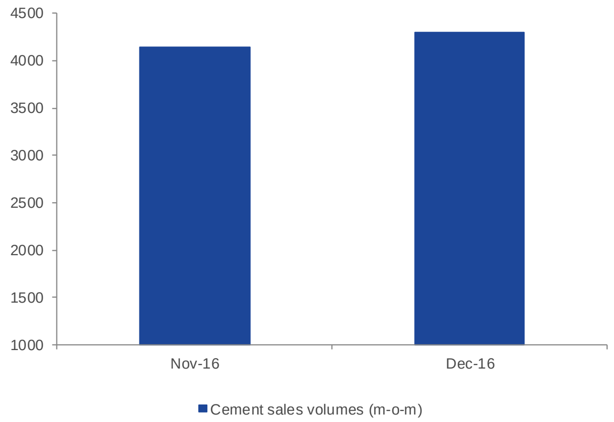
Source: Company data, Al Rajhi Capital

Figure 7 Cement sales volumes ('000 tons, y-o-y)



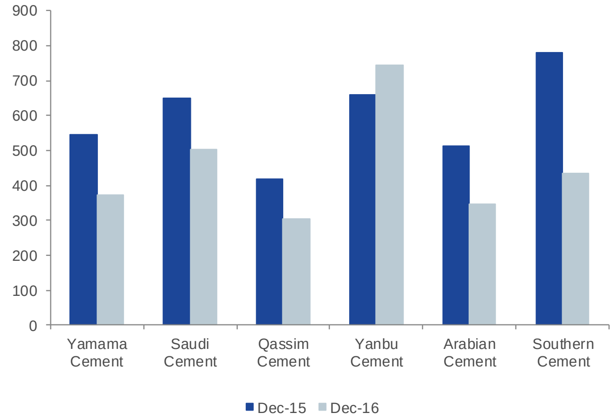
Source: Yamama data, Al Rajhi Capital

Figure 8 Cement sales volumes ('000 tons, m-o-m)



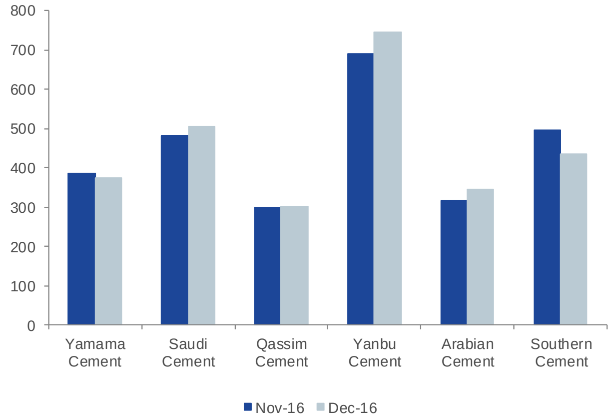
Source: Yamama data, Al Rajhi Capital

Figure 9 Cement sales volumes ('000 tons, y-o-y)



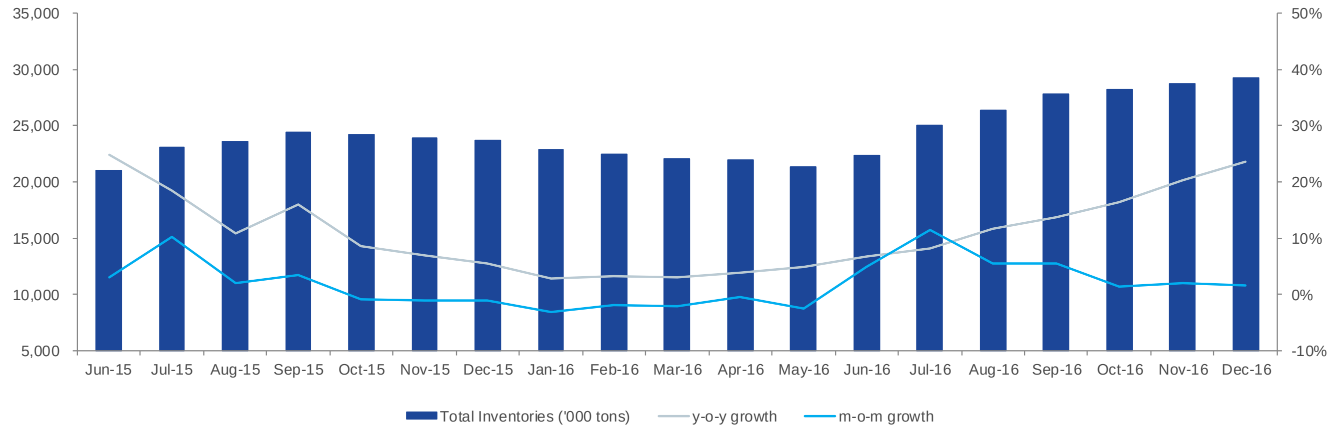
Source: Yamama data, Al Rajhi Capital

Figure 10 Cement sales volumes ('000 tons, m-o-m)



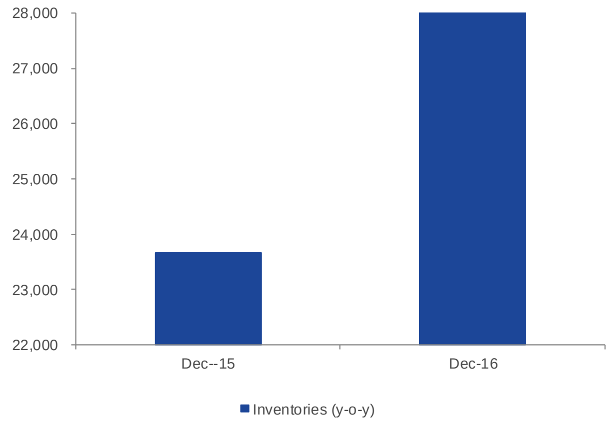
Source: Yamama data, Al Rajhi Capital

Figure 11 Inventories (absolute, y-o-y, m-o-m)



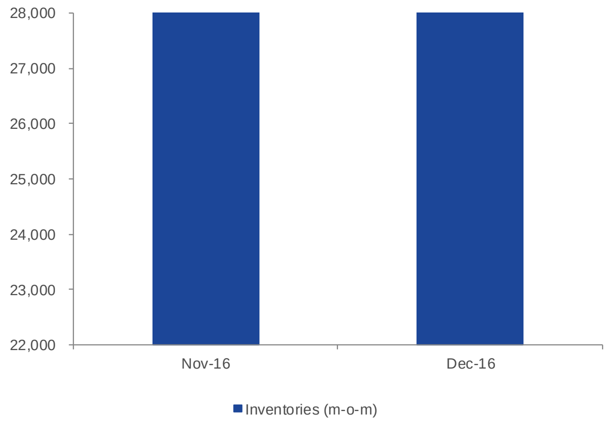
Source: Company data, Al Rajhi Capital

Figure 12 Inventories ('000 tons, y-o-y)



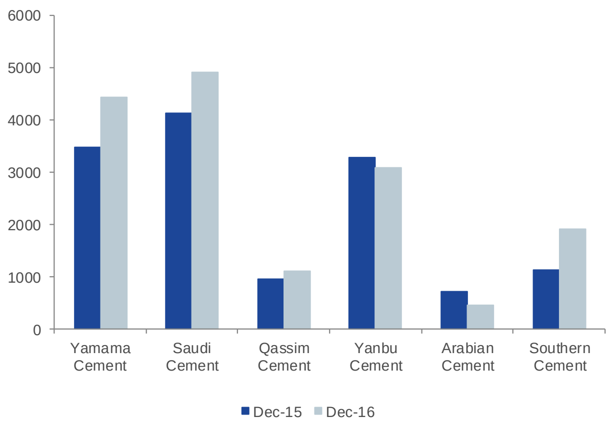
Source: Yamama data, Al Rajhi Capital

Figure 13 Inventories ('000 tons, m-o-m)



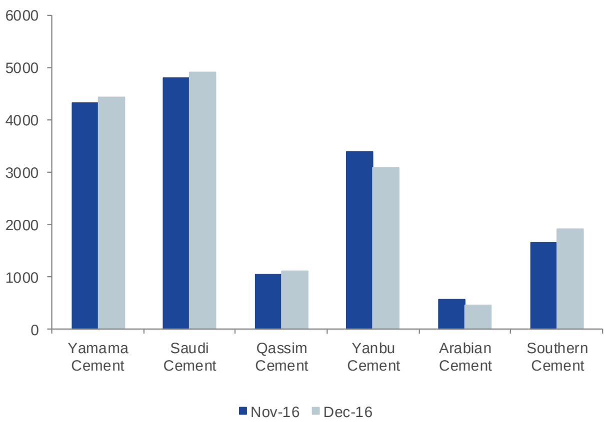
Source: Yamama data, Al Rajhi Capital

Figure 14 Inventories ('000 tons, y-o-y)



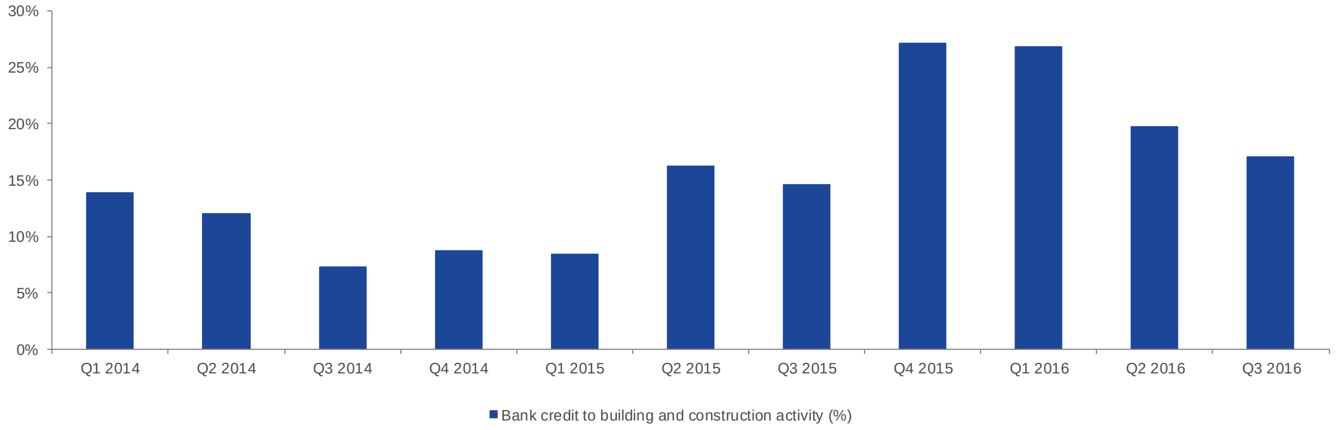
Source: Yamama data, Al Rajhi Capital

Figure 15 Inventories ('000 tons, m-o-m)



Source: Yamama data, Al Rajhi Capital

Figure 16 Y-o-Y change in Bank credit to building and construction activity (%)



Source: SAMA, Al Rajhi Capital

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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

"Target price": We estimate target value per share for every stock we cover. This is normally based on widely accepted methods appropriate to the stock or sector under consideration, e.g. DCF (discounted cash flow) or SoTP (sum of the parts) analysis.

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