Saudi All Industries Sector
All Industries –All Sectors
Saudi Arabia
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Key themes

Our quick take on Q1 2017 financial results.

*Note: *See detailed tables for companies / sectors that are included/excluded from analysis*

Saudi Arabian Equities

Q1 2017 results: Mixed bag

The Q1 results of Saudi Arabian listed companies presented a mixed picture with most of the domestic consumption-driven sectors reporting weaker results, whereas insurance and export-driven Petrochemical sectors delivered a strong performance. An initial analysis of the overall results suggests pricing pressure at multiple levels due to subdued demand. Expectations-wise, the Q1 results also witnessed some notable deviations from estimates in a few sectors. Some of the key takeaways from the results are summarized below.

- *Aggregate annual net profit* of Saudi listed companies rose ~39% y-o-y in Q1 2017, while revenue increased 4% y-o-y. However excluding 4 sectors (Banks, Petchem, Energy and Insurance), the aggregate net profit was down ~11% y-o-y, while the top-line was down 5% y-o-y, implying margin pressure. Operating profit of these companies also declined 11% y-o-y, while gross profit was down 5%.*
- *Banking sector net interest income grew 9% y-o-y, supported by higher asset yields due to the increase in SAIBOR in the second half of 2016, while non-interest income fell 8% as commission and fees income is likely to have declined owing to a slowdown in loan growth and lower trading volumes on the Tadawul. The sector's profit slipped 1% y-o-y in Q1 2017 despite the increase in total operating income, due to the increase in provisions compared to the year-ago period. Notably, Al Rajhi bank reported healthy growth while NCB also posted a higher bottom-line.*
- *The Petchem sector's net profit almost doubled y-o-y in Q1 2017, driven by rising product prices. Most of the growth was accounted for by SABIC (66%), followed by Saudi Kayan (13%). In addition to rising product prices, higher utilization rates also boosted the sector's top-line growth of 15%. We remain positive about the sector's performance, but current valuations provide limited further upside for companies under our coverage.*
- *Revenue of consumer sectors (retail, food, telecom, hotel & tourism) declined 2.9% y-o-y in Q1 2017, as consumer spending was hit by the cut in salaries and allowances of public sector employees. However, the fall in revenue was partially offset by the increasing market share of organized players. Nevertheless, the profitability of these sectors rose 8% y-o-y, as the improved profitability of the telecom sector outweighed the other sectors.*
- *The Insurance sector posted a profit (before zakat) growth of 11% y-o-y. Excluding Medgulf, the sector's profitability jumped 42% y-o-y. Gross written premiums for the sector slipped 2%, while net written premiums were up 4% y-o-y. The cement sector's profitability almost halved on a y-o-y basis in Q1 2017, as demand remained sluggish and price competition intensified. We believe that sales volume and selling prices will remain under pressure through the year.*

Overall, we believe that consumption-driven domestic sectors are likely to recover in Q2 owing to the restoration of public sector employee salaries and allowances as well as the seasonal impact of the holy month of Ramadan. Meanwhile, construction-related sectors such as Cement and Building & Construction will remain under pressure as the government continues to rationalize spending. For the banking sector, asset quality will remain a concern while asset yields will begin to move lower on a sequential basis. The petrochemical sector is expected to continue its strong performance as rising oil prices drive petchem product prices higher, positively impacting its bottom-line.

Figure 1 Summary of results (Q1 2017 performance)

(SARmn)	Revenue					Gross Profit					Operating Profit					Net income				
Summary	**Q1 16**	**Q4 16**	**Q1 17**	***y-o-y***	***q-o-q***	**Q1 16**	**Q4 16**	**Q1 17**	***y-o-y***	***q-o-q***	***Q1 16***	**Q4 16**	**Q1 17**	***y-o-y***	***q-o-q***	**Q1 16**	**Q4 16**	**Q1 17**	***y-o-y***	***q-o-q***
Petrochemical	49,541	54,912	57,212	*15%*	*4%*	12,991	14,967	17,824	*37%*	*19%*	*6,326*	7,650	11,462	*81%*	*50%*	3,571	4,046	7,108	*99.0%*	*76%*
Cement	3,649	2,567	2,483	*-32%*	*-3%*	1,802	1,055	976	*-46%*	*-8%*	*1,630*	872	816	*-50%*	*-6%*	1,565	770	792	*-49.4%*	*3%*
Retail	9,021	10,293	9,593	*6%*	*-7%*	1,828	2,044	2,032	*11%*	*-1%*	*665*	705	851	*28%*	*21%*	578	621	806	*39.5%*	*30%*
Food	12,066	12,103	11,274	*-7%*	*-7%*	3,198	2,921	2,930	*-8%*	*0%*	*1,078*	225	874	*-19%*	*288%*	718	-96	604	*-15.9%*	*NA*
Energy & Utilities	9,406	11,161	9,440	*0%*	*-15%*	-279	-1,899	-590	*NA*	*NA*	*-370*	-1,420	5,317	*NA*	*NA*	-748	-2,041	5,001	*NA*	*NA*
Telecom	18,517	16,818	17,704	*-4%*	*5%*	10,095	9,797	10,021	*-1%*	*2%*	*2,905*	1,963	2,865	*-1%*	*46%*	2,104	1,819	2,387	*13.5%*	*31%*
Multi-investment	1,417	1,209	1,349	*-5%*	*12%*	492	229	616	*25%*	*169%*	*244*	-6	352	*44%*	*NA*	84	-137	177	*110.8%*	*NA*
Industrial investment	5,456	5,149	5,822	*7%*	*13%*	1,428	1,129	1,762	*23%*	*56%*	*655*	-474	920	*40%*	*NA*	445	-468	463	*4.0%*	*NA*
Building & Construction	5,325	4,542	4,132	*-22%*	*-9%*	1,039	846	783	*-25%*	*-7%*	*478*	142	280	*-41%*	*97%*	307	-131	147	*-52.0%*	*NA*
Real estate	1,114	1,541	1,244	*12%*	*-19%*	500	1,164	578	*16%*	*-50%*	*262*	853	336	*28%*	*-61%*	151	723	251	*66.4%*	*-65%*
Transport	3,314	3,142	3,226	*-3%*	*3%*	1,145	613	806	*-30%*	*32%*	*962*	455	643	*-33%*	*41%*	902	429	589	*-34.7%*	*37%*
Media & Publishing	606	747	655	*8%*	*-12%*	119	239	150	*26%*	*-37%*	*-33*	23	16	*-148%*	*-29%*	16	18	-5	*NA*	*NA*
Hotels & Tourism	973	986	847	*-13%*	*-14%*	554	469	444	*-20%*	*-5%*	*283*	202	196	*-31%*	*-3%*	272	182	169	*-38.1%*	*-7%*
Total	**120,405**	125,170	**124,979**	*4%*	*0%*	**34,914**	**33,575**	**38,333**	*10%*	*14%*	***15,085***	**11,190**	**24,929**	*65%*	*123%*	**9,966**	**5,735**	**18,490**	*85.5%*	*222%*
	NII					**Non-interest income**										**Net income**				
Banks	13,995	14,760	15,211	*9%*	*3%*	6,881	5,592	6,350	*-8%*	*14%*						11,719	8,080	11,646	*-1%*	*44%*
	GWP					**NWP**										**Net income before zakat**				
Insurance	11,752	7,781	11,493	*-2%*	*48%*	9,526	6,642	9,877	*4%*	*49%*						349	768	496	*42%*	*-35%*
All inclusive																**22,035**	**14,583**	**30,633**	***39.0%***	***110.1%***
All ex Petchem & Energy																**19,211**	**12,578**	**18,524**	***-3.6%***	***47.3%***

Source: Company data, Al Rajhi Capital (Please note that Q4 2016 revenue figures are not comparable as the implementation of IFRS has led to restatement of earlier results, and Q4 2016 restated revenue numbers are not available yet)

Note:
We have excluded the following companies from our calculations (as comparable results were not available) - Makkah Construction, Sahara Petrochemical, Sanad corporative, Weqaya Takaful, Mohammad Al Mojil, and Saudi Cable.

Petrochemicals: Higher prices of most products, especially intermediate products, helped the Saudi petchem sector improve its top-line (as per IFRS) by ~15% y-o-y, with SABIC accounting for ~45% of the growth, followed by Petro Rabigh (23%). While key polymer products such as HDPE, LDPE, PP increased in the range of 5-20% y-o-y in Q1 due to higher upstream costs and improved demand, intermediate products such as MEG, Acrylic Acid and Butanediol surged in the range of 45-60% y-o-y in Q1. Key feedstock prices also rose significantly with average Naphtha price rising ~44% y-o-y, while average Propane and Butane price increasing 53% and 63%, respectively in Q1. Despite higher feedstock prices, most Saudi petchem companies (except APCC and Petro Rabigh) witnessed a healthy operating performance, supported by higher revenue and improved cost efficiencies. Market heavyweight SABIC, which represented ~72% of the consolidated sector's operating profit, witnessed a sharp operating profit improvement (+79% y-o-y) in Q1, while APCC, which mainly uses NGLs as a feedstock, came under pressure with its operating profit declining more than 20% y-o-y on higher production costs and lower sales volume due to the 8-day plant shutdown in January. SAFCO, which primarily uses Methane at a fixed price, also witnessed an improvement in its operating profit (53% y-o-y) due to higher urea prices (22% y-o-y) and improved operating leverage. Consequently, the sector's earnings almost doubled on an annual basis in Q1, primarily on account of higher product prices and healthy operating performance. While we remain positive about the sector's overall operating performance in 2017, the current valuation of the companies under coverage offers limited further upside potential unless product prices and spread improve further.

Telecom: The Saudi telecom sector had a mixed quarter. At the net profit level, STC and Zain posted stronger than expected numbers, while Mobily's Q1 earning was below estimates. STC's revenues declined in Q1 on account of the cut in public sector employee salaries and allowances, while the bottom-line was supported by higher non-operating income. We believe that the restoration of public sector employee salaries and incentives augurs well for the sector and STC may be the biggest beneficiary of the same. As a result, we believe that the company may reverse its declining top-line trend in the coming quarter. Mobily also posted a decline in revenues during the quarter, which resulted in it posting a bigger net loss on a y-o-y basis (compared to a small profit in Q4 2016). In our view, Mobily is likely to focus on customer acquisition in the short-term to maintain market share, while continuing to work on containing operating costs. On the other hand, Zain KSA continued to post healthy revenue growth and improved margins, resulting in its first quarterly profit. Zain appears to be better positioned than its peers in the Saudi telecom sector, in terms of gaining market share and witnessing profit growth. However, we believe that the stock incorporates these positives at current levels and we maintain our Neutral rating on the Zain stock with a target price of SAR9.5.

Retail: Revenue of retail companies under our coverage has been a mixed bag in Q1 2017. As in Q4 2016, revenue for electronic retailers (Jarir & Extra) outperformed our and consensus estimates, driven by better than estimated sales from smartphone segment on the back of regulatory tailwinds. However, LFL growth of Fawaz Al Hokair was lower than our estimate due to full quarter impact of allowances cut, while that for Al Othaim was in-line our estimates. Net profit of retailers came ahead of our estimates due to better than estimated gross margin and lower than estimated SG&A expenses. As outlined in our March 2017 consumer note “Saudi consumer sector: Adjusting to a new normal”, most of the one-off impacts from inventory write-downs etc are now behind us (which aids gross margins) and SG&A rationalization efforts are starting to bear fruit. The EBIT margin of all retailers under our coverage has been better than estimates. Going forward, we expect an uptick in revenue and margin for retailers, especially for discretionary retailers such as Fawaz Al Hokair, Jarir and Extra, from the restoration of allowances, which will take effect in May 2017. We have adjusted our target prices during the earnings updates to reflect the same. Among our retail sector coverage, we are Overweight on Fawaz Al Hokair and Neutral on Jarir, Extra and Al Othaim.

Food: For the second consecutive quarter, revenue for food sector companies was below our estimates, despite the non-discretionary nature of their product profile. Almarai reported tepid revenue growth led by continuing weakness in its flagship Dairy and Juice segment, while Savola’s revenue was weighed down by retail segment, which is not yet out of the woods (even in terms of stabilization, if not turnaround). Herfy’s revenue was impacted by sustained weakness in LFL growth due to consumer spending slowdown, exacerbated by allowances cut for public sector employees. Going forward, as allowances are restored in May 2017, we expect an uptick in revenue for Herfy and Savola due to their non-discretionary products lineup, with little to no upside for Almarai. The margins of Almarai and Herfy have been better than estimates, spurred by continuing gains from lower commodity prices. However, Savola’s margins were lower than estimates due to the significant revenue impact. We believe that the declining raw material prices over the last two and a half years may bottom out in mid-2017 and may resume their uptrend toward the end of 2017. Hence, we maintain our cautious stance on the sector. We have assigned an Underweight rating to Almarai and Neutral rating on both Herfy and Savola.

Healthcare: For companies under our coverage, Q1 revenue grew 8% y-o-y. Excluding Care, which reported 20% y-o-y decline in revenue, the revenue growth remained at a healthy rate of ~17% y-o-y. Hammadi led the sector’s top-line growth, +25% y-o-y, on the back of the low base of Q1 2016, which saw Olaya hospital operate for only 5 weeks in the quarter due to the fire incident. Mouwasat continued its healthy performance as revenues grew 20% on a yearly basis, supported by improving performance of the Riyadh hospital (opened in 2014-end) and the subspecialty clinics. Dallah also posted a revenue growth of 6% y-o-y; however, it was considerably lower than the 14-22% growth levels witnessed over the last four quarters. On the other side, the decline in Care Q1 revenue by -20% y-o-y was attributed to pricing revision with one of the major governmental clients. On the profitability front, the sector was supported by the growth in revenues on a yearly basis as well as reversal and lower provisions compared to the previous quarter. Aggregate operating profit of four companies grew ~8% y-o-y, though excluding Care, operating profit was +29% on an annual basis. The sector’s net profit expanded ~9% y-o-y.

Cement: Cement sector reported another quarter of weak results due to sluggish demand, lower selling prices, and inventory pile up. During Q1, sales volume declined 20% y-o-y, while clinker production declined 7% y-o-y, resulting in inventory levels of 29.5mn tons (~ 54% of sales volume in 2016). Total revenue of the sector declined 32% y-o-y and net profit fell 50% y-o-y. Due to low demand and oversupply in the market, cement producers' operating performance in Q1 was impacted by sharp decline in average realized price/ton especially in Central and Western regions which witnessed a drop of ~20% and ~15% y-o-y, respectively. However, the unexpected improvement in selling prices in quarterly basis for Western region companies was impressive given the stiff competition in the region. For Eastern province producers, sales volume impacted by implementing export fees to Bahrain since mid-March 2017. For Southern cement, pricing pressures in the Western region weighed on the company's average realized price which declined 18% y-o-y and -14% q-o-q to ~SAR198/ton. In Q1 2017, all listed cement companies (excluding Umm AlQura) witnessed y-o-y decline in the top line and bottom line. Najran and Hail cement reported the most declines in net profit by -82% and 74% y-o-y, respectively. Our near and medium-term view of the sector is largely weighed down by weak demand, further energy price reforms, high export fees and high inventory levels. Current total cement production capacity is about 70mn tons, while total dispatches in 2016 were 54.8mn tons and total inventories are at 29.2mn tons. Moving forward, we do not see signs of any remarkable turnaround for the construction sector in the short term and we expect further cut in dividend payments in the sector for 2017. For now, we are Neutral on all cement companies under our coverage.

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