EFG HERMES المجموعة المالية هيرميس

NATIONAL SHIPPING CO. OF SAUDI ARABIA (NSCSA)

4Q2009 Results Miss, Dividend Cut Disappoints

20 JANUARY 2010

SAUDI ARABIA | SHIPPING

Current Price* : SAR 19.1 Rating: Sell
Fair Value (FV): SAR 15.0

• **4Q2009 Income below Forecasts:** While NSCSA's 4Q2009 revenue of SAR444.9 million (up 11% Q-o-Q, down 32% Y-o-Y) came in 7% ahead of forecasts, income disappointed. 4Q2009 net income came in at SAR48.1 million, down 14% Q-o-Q, 50% Y-o-Y and 27% below our forecast of SAR66.0 million. Results were similarly below at the operating level, with income coming in at SAR72.2 million, down 1% Q-o-Q, 60% Y-o-Y and 23% below our forecasts. This meant that FY2009 net income came in at SAR362.8 million, down 52% Y-o-Y and 5% below our forecasts.

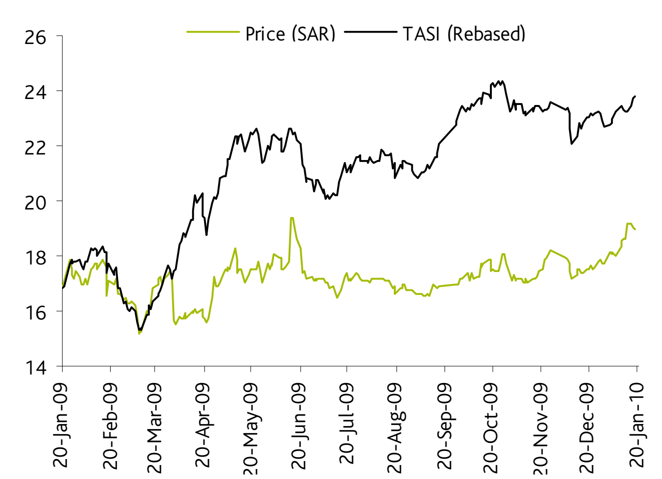
• ..**Due to a Weak VLCC Market:** The group highlighted a weak VLCC market for the drop in yearly profits, which is fair as VLCC day rates averaged cUSD32,000/day in 2009 compared to USD92,000 in 2008. However, this does not explain why gross operating income was flat Q-o-Q, as average VLCC rates rose by 70% to cUSD40,000 in the quarter (4Q2008 VLCC average rate was USD68,000/day). Instead, we suspect that this was due to the vessels being hired before the rates spiked. In addition, our forecasts assumed an improvement in the general cargo division, which may not have materialised.

• **Dividend Cut Will Disappoint:** The 33% cut in the dividend, from SAR1.50 to SAR1.0, appears sensible in our view given that earnings have fallen by 50% Y-o-Y. Furthermore, this may signal that the group does not expect to generate the high returns of 2008 in the immediate future. Although some income investors may be left disappointed it is worth highlighting that, despite the cut, the payout ratio stands at 87% and the yield remains relatively healthy at 5%.

• **Outlook Appears More Positive:** Despite the disappointing 4Q2009 numbers, the outlook appears to be more positive. VLCC rates rallied last week by a staggering 125%, to hit USD87,108/day. This bodes well for NSCSA, as it has 11 VLCCs trading on the spot market, and it puts positive pressure on our short-term forecasts. For instance, our 2010e EPS estimate would rise by 47% should the average rate move up to USD 85,000/day. That said, average rates can be misleading. For example, day rates for the Gulf to Japan route stand at cUSD100,000, while the Gulf to US route is 50% lower at USD50,000/day. Consequently a vessel's earnings can vary depending on timing and deployment.

• **Shipping Rates are Volatile and We Remain Cautious:** While the pickup in day rates is a positive boost for the industry, we would remind investors that rates can be extremely volatile. Furthermore, the International Energy Agency (IEA) has cut its global oil consumption forecast, despite the recent cold snap in the US, which suggests that the demand for oil continues to weaken. On the supply side, demolition rates have not risen substantially, suggesting that few VLCC's have been removed from the market. As a result, the fillip in day rates could be down to a short-term mismatch between supply and demand, and not therefore sustainable. We will be adjusting our forecasts once NSCSA publishes its full financials, but do not expect to materially change our numbers unless VLCC spot rates settle above USD50,000/day.

FLASH NOTE



	2009a	*2010e*	*2011e*
EPS	*1.15*	*1.56*	*2.03*
PER (x)	*16.5*	*12.2*	*9.4*
DPS	*1.00*	*1.50*	*1.50*
Div. Yield	*5.2%*	*7.9%*	*7.9%*
CFPS	*1.81*	*2.93*	*3.65*
P/CF (x)	*10.5*	*6.5*	*5.2*
BVPS	*15.9*	*15.9*	*16.5*
P/BV(x)	*1.2*	*1.2*	*1.2*

Figures in SAR, unless otherwise stated

Stock Data	
Last Dividend Date	*SAR1.5 on 31 Mar 09*
Mkt. Cap / Shares (mn)	*SAR6,001 / 315*
Av. Mthly Liqd. (mn)	*1,020*
52-Week High / Low	*SAR19.35 / 15.20*
Bloomberg / Reuters	*NSCSA AB / 4030.SE*
Est. Free Float	*71.90%*

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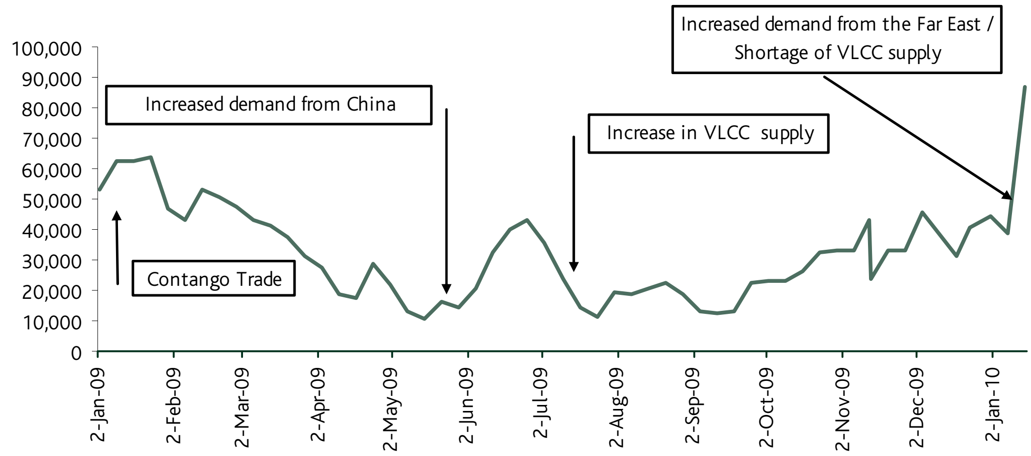
** Price as at 20 January 2010*

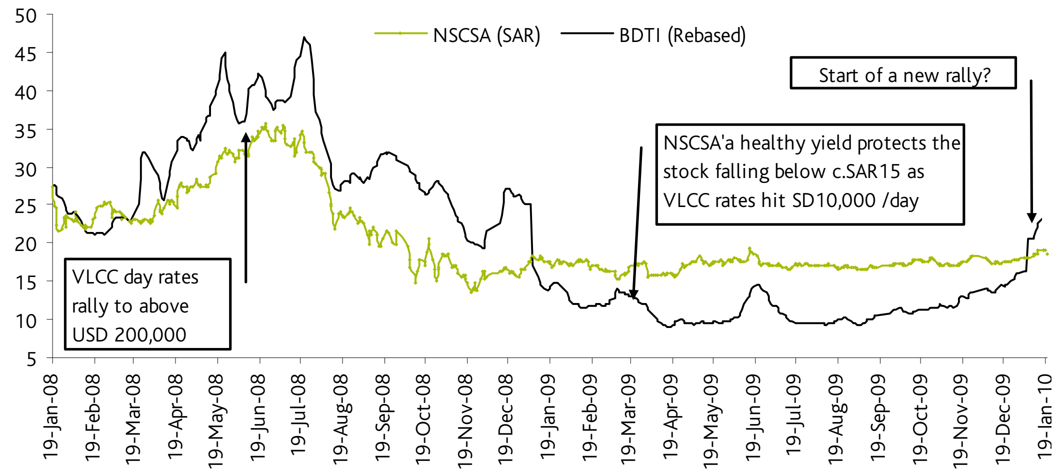
Figure 1: VLCC Day Rates
In USD thousands, unless otherwise stated



Source: EFG Hermes

The recent spike in the day rates is down to a combination of increased demand, particularly from the Far East, and a supply shortage. For example, at the end of October 2009 there were 11 idle VLCCs in the Gulf, but that number had fallen to five by the end of December 2009. This suggests that either i) some vessels have moved away from the spot to the charter market, or ii) a number of VLCCs are on longer journeys, which has caused a temporary supply shortage.

Figure 2: NSCSA Share price vs. Baltic Dry Tanker Index (BDTI)
In SAR, unless otherwise stated



Source: Zawya

While we think it unlikely the current rate of cUSD87,000/day will be sustained, and doubt that NSCSA will be able to fully take advantage of this spike in rates, it is worth emphasising that even if NSCSA earned an average rate of USD85,000/day, our DCF fair value would rise to only SAR20.1 per share. With the current price standing at SAR19.05, it would therefore seem that there is limited upside potential. However, as figure 2 illustrates, NSCSA's share price is closely correlated to average tanker earnings index, and the share price has often risen above its fundamental 'fair value' on the back of improved sentiment. Consequently, should the VLCC rate settle at the current level or continue with its upward momentum, there is a possibility that the share price could rally as it has done in the past.

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Neutral	(10%) and 15%
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