Saudi Kayan Petrochemical Co.

Result Flash Note 4Q-2016 | **January 2017**

ALJAZIRA CAPITAL الجزيرة للأسواق المالية

Please read Disclaimer on the back

Saudi KAYAN: 4Q-2016 earnings came below estimates; the result was impacted by higher feedstock cost, an increase in the financial charges and OPEX, despite the higher operating rate and selling prices. Recommendation updated to "Neutral".

Amount in SAR mn; unless specified	Forecasts 4Q-16	Actual 4Q-16	Deviation (%)
Sales revenues	2,322.6	2,449	**0.05%**
Net profit	118.0	103.65	**-12.1**
EPS (SAR)	0.08	0.07	**(0.01)**

Higher operating rate and selling prices were partly offset by higher production cost and SAR 245mn financial charges in 4Q2016: 4Q2016 net profit came below our expectation and showed a deviation of 12.1% from our estimates and 21.5% from the market Consensus of SAR 132mn. Saudi Kayan (KAYAN) reported a net profit of SAR 103.65mn; (EPS; SAR 0.07); as compared to losses of SAR 624.1mn in 4Q2015 and net profit of SAR 156.3mn in 3Q2016. The QoQ weak performance is mainly attributed to i) higher feedstock cost ii) an increase in the financial charges iii) higher OPEX, and despite the higher operating rate and selling prices.

We believe that despite the higher than expected sales volume, the impact of higher production cost after the increment in some particular feedstock prices (Propane & Butane) has strongly impacted the gross margin in 4Q2016, as compared to the previous quarter. On the other hand, the rise in financial charges has negatively impacted Saudi Kayan due to highly leveraged balance sheet with long-term obligation of SAR 24.8bn. The company is expected to report a finance charge of SAR 245mn; higher than our estimate of SAR 202mn, SAR 208.9mn in 3Q2016 and SAR 147.3mn in 4Q2015.

Gross profit stood at SAR 454.8mn, well above our forecast of SAR 410.2mn that can be attributed to higher than expected operating rate. Gross margin stood at 18.57% in 4Q2016 vs. 20.2% in 3Q2016, which due to higher feedstock prices. Operating profit stood at SAR 348.6mn; as the company recorded higher OPEX expenses (SG & A) at SAR 106.2mn, as compared to our estimate of SAR 99.5mn and SAR 97.7mn in 3Q2016.

Kayan's sales in 4Q2016 stood at SAR 2,449mn, well above our estimates of SAR 2,323mn, which ascribed to higher than expected operating rate. The plant was running with operating rate of 98.5%, higher than our estimates of 97.3% and 87.5% in 4Q2015. We believe that the maintenance on March/April-2016 had positively impacted the overall performance, and we expect a more improved performance in FY2017. Our outlook will remain optimistic in the year FY2017 due to continued improvement after plant maintenance in 2Q2016. Furthermore, gross margin is expected to slightly increase to an average of 18.4% in FY2017 compared to an average of 16.2% in FY2016 due to the impact of maintenance in H1-2016.

During the quarter, Asian average prices of Kayan key products such as, HDPE, PP and MEG products average prices increased by 1.0%QoQ, 3.3%QoQ and 16.8%QoQ in 4Q2016 respectively.

Higher feedstock cost led to a tight margin in 4Q2016: In 4Q2016, Naphtha average prices increased by 14.9%QoQ to USD 446/ton, in line with the increase in crude oil prices. Where polymer and other Petchem product prices remained flat, increasing less than the feedstock prices. Furthermore, higher increase in feedstock price than the final product prices has resulted in PP-Naphtha spreads to shrink in QoQ basis. PP-Naphtha spread contracted 4.1%QoQ to USD 585/ton. On the other hand, The company was granted a grace period for ethane, butane and methane and new feedstock prices will be gradually applied by 2Q2017.

We update our recommendation to "Neutral" on KAYAN with a PT of SAR 8.80/ share indicating a potential upside of 4.8%: Saudi Kayan Co. is expected to post SAR 610mn in net income (0.41 EPS) for 2017, as compared to SAR 134.7mn in 2016 that mainly attributed to the impact of scheduled maintenance in 1H-2016 and expected higher crude oil prices in 2017. The company is trading at a forward PE and P/B of 20.7x and 0.93x respectively based on our 2017 earnings forecast.

Recommendation	**'Neutral'**
Current Price* (SAR)	**8.40**
Target Price (SAR)	**8.80**
Upside / (Downside)	**4.8%**

*prices as of 16th of January 2017

Key Financials

SARmn (unless specified)	FY14	FY15	FY16	FY17E
Revenues	11,636	8,155	8,609	10,500
Growth %	12.4%	-29.9%	7.9%	22.0%
Net Income	(44.7)	(1,243.4)	134.7	609.9
Growth %	NM	NM	NM	352.9%
EPS	(0.03)	(0.83)	0.09	0.41

Source: Company reports, Aljazira Capital *NM: Not Meaningful

Key Ratios

SARmn (unless specified)	FY14	FY15	FY16	FY17E
Gross Margin	8.4%	-2.6%	16.2%	18.4%
EBITDA Margin	25.6%	23.3%	39.0%	38.3%
Net Margin	- 0.4%	-15.2%	1.6%	5.8%
P/E	-	-	93.51x	20.7x
P/B	1.17x	0.79x	0.97x	0.93x
EV/EBITDA (x)	14.0	17.4x	10.3x	8.1x
ROE	- 0.3%	-9.3%	1.0%	4.6%
ROA	- 0.1%	-2.8%	0.3%	1.5%

Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (bn)	12.75
YTD %	-1.02%
52 Week (High)	9.45
52 Week (Low)	4.40
Shares Outstanding (mn)	1500.0

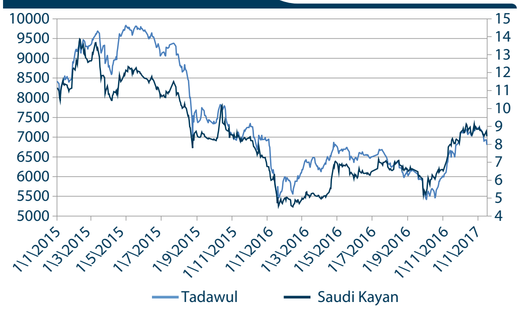
Source: Company reports, Aljazira Capital

Shareholders Pattern

Shareholders Pattern	Holding
Saudi Basic Industries Corp.	35.0%
Public	65.0%

Source: Company reports, Aljazira Capital

Price Performance



Source: Bloomberg, Aljazira Capital

Analyst
Jassim Al-Jubran
+966 11 2256248
j.aljabran@aljaziracapital.com.sa

الجزيرة كابيتال
الجزيرة للأسواق المالية ALJAZIRA CAPITAL

RESEARCH DIVISION

Acting Head of Research
Talha Nazar
+966 11 2256250
t.nazar@aljaziracapital.com.sa

Analyst
Sultan Al Kadi
+966 11 2256374
s.alkadi@aljaziracapital.com.sa

Analyst
Jassim Al-Jubran
+966 11 2256248
j.aljabran@aljaziracapital.com.sa

Analyst
Waleed Al-jubayr
+966 11 2256146
W.aljubayr@aljaziracapital.com.sa

Analyst
Muhanad Al-Odan
+966 11 2256115
M.alodan@aljaziracapital.com.sa

BROKERAGE AND INVESTMENT CENTERS DIVISION

General Manager – Brokerage Services & sales
Alaa Al-Yousef
+966 11 2256060
a.yousef@aljaziracapital.com.sa

AGM-Head of international and institutional brokerage
Luay Jawad Al-Motawa
+966 11 2256277
lalmutawa@aljaziracapital.com.sa

AGM- Head of Western and Southern Region Investment Centers & ADC Brokerage
Mansour Hamad Al-shuaibi
+966 12 6618443
m.alshuaibi@aljaziracapital.com.sa

AGM-Head of Sales And Investment Centers Central Region
Sultan Ibrahim AL-Mutawa
+966 11 2256364
s.almutawa@aljaziracapital.com.sa

AGM-Head of Qassim & Eastern Province
Abdullah Al-Rahit
+966 16 3617547
aalrahit@aljaziracapital.com.sa

RESEARCH DIVISION

AlJazira Capital, the investment arm of Bank AlJazira, is a Shariaa Compliant Saudi Closed Joint Stock company and operating under the regulatory supervision of the Capital Market Authority. AlJazira Capital is licensed to conduct securities business in all securities business as authorized by CMA, including dealing, managing, arranging, advisory, and custody. AlJazira Capital is the continuation of a long success story in the Saudi Tadawul market, having occupied the market leadership position for several years. With an objective to maintain its market leadership position, AlJazira Capital is expanding its brokerage capabilities to offer further value-added services, brokerage across MENA and International markets, as well as offering a full suite of securities business.

RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer