



Beats consensus despite weak volume growth

Northern Cement has reported a net profit of SAR49mn (-24% Y/Y, +13% Q/Q) for 2Q16 above our estimates (9%) and beat consensus by 30%. The company posted SAR 252mn revenue which was in line with our estimates. The earnings beat stems from stronger than expected gross margins, as management appears to have sacrificed market share in order to maintain net retention prices. The Y/Y decline in net income was ascribed to weaker volume, as the construction activity continues to fare poorly in the face of lower government spending and cash flow constraints as payment delays continue and increase in fuel costs. Weak volume was also driven by seasonal reasons (holy month of Ramadan). Northern gross margins have declined to 38% in 2Q16 from 41% in 2Q15 mainly due to rising cost and weaker volume. However the company has been able to keep its net margins steady at 19% 2Q16. (2Q15: 20%). At the operating level, the company reported a profit of SAR56mn (down 30% Y/Y and up 3% Q/Q). Northern's volume growth underperformed the sector, it's total volume for 2Q16 decreased 15% YoY vis-à-vis -9% for the sector. Dispatches stood at 0.52mtn tons in 2Q versus 0.72 mtn tons in the previous quarter. In 2Q 2016, market share averaged 3.5% versus 4.2% in 1Q 2016.

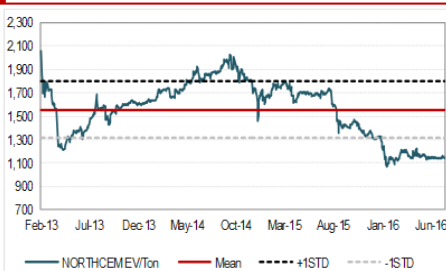
Some silver linings, but sector to struggle near term

There are some silver linings for the sector in the shape of declining clinker inventory and more importantly the National Transformation Program's (NTP) heavy focus on improving household ownerships by citizens. In the NTP, significant steps have already taken place with the implementation of the white land tax underway and the government inking agreements with foreign contractors / developers for housing development. However in the near to medium term, we continue to expect the sector to struggle with overcapacity, poor pricing power and weak volumes, and cannot rule out further upwards adjustments in electricity and fuel costs.

Maintain SELL rating with TP of SAR11.7

The stock has decreased 17% YTD 2016 (versus -7.7% for the sector) mainly due to the concerns related to the weaker volume growth and energy price hikes. At 12.5x 2016E PER (versus sector 2016 PER 8.7x) valuation is relatively expensive and it trades at a premium to our target price. We maintain our SELL rating on Northern Cement, with a target price of SAR 11.70.

EV / Ton of Northern Cement



Source: Bloomberg, SFC

	2Q16A	2Q16SFC	% diff	Cons.	% diff	1Q16	% Ch. QoQ	2Q15	% Ch. YoY
Revenues	252	249	1%	Na	Na	231	9%	324	-22%
Gross Profit	95	90	6%	Na	Na	76	25%	133	-29%
EBIT	56	55	2%	Na	Na	54	3%	79	-30%
Net Income	49	45	9%	38	30%	43	13%	64	-24%

Source: Company, SFC, Bloomberg

Rating Summary

Recommendation	SELL
12-Month Target price (SAR)	11.7
Upside/(Downside)	-6%

Stock Details

Last Close Price*	SAR	12.4
Market Capitalization	SAR mln	2,330
Shares Outstanding	mln	180
52-Week High	SAR	22.3
52-Week Low	SAR	10.7
Price Change (TYD)	%	-17.3
EPS 2016E	SAR	1.04
Reuters / Bloomberg	3004.SE	NORTHCEN AB

Source: Tadawul, Bloomberg *as of 27 July 2016,

SFC Estimates

SAR	2016E	2017E
Revenues (mln)	1,028	1,102
Gross Margin	36.7%	37.2%
EBITDA (mln)	228	225
Net Income (mln)	186	187

Source: SFC

Price Multiples

	2016E	2017E
P / E	12.0x	11.9x
EV / EBITDA	9.7x	9.7x
Dividend Yield	6.5%	5.6%

Source: SFC

1-Year Share Performance



Source: Bloomberg

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Rating Framework

BUY

Shares of the companies under coverage in this report are expected to outperform relative to the sector or the broader market.

HOLD

Shares of the companies under coverage in this report are expected to perform in line with the sector or the broader market.

SELL

Shares of the companies under coverage in this report are expected to underperform relative to the sector or the broader market.

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