



Rating NEUTRAL
Target price SAR116.0 (4.5% upside)
Current SAR111.3

Key themes & implications

Saudi Ceramic Company is one of the leading ceramic manufacturing companies in the region. We believe the company will offer good growth in the near future. We believe the current expansions of Saudi Ceramics coupled with improvements in margins will support its share price.

Share information

Market cap (SAR/US\$)	4.172bn / 1.112bn
52-week range	72.75 - 111.3
Daily avg volume (US\$)	14.8mn
Shares outstanding	37.50mn
Free float (est)	77%

Performance	1M	3M	12M
Absolute	6%	32.8%	20.9%
Relative to index	3.5%	28.2%	8.8%

Major Shareholder:

General Social Insurance	16.1%
Saleh Abdulaziz Al Rajhi	6.8%

Valuation

	12/12A	12/13E	12/14E	12/15E
P/E (x)	16.8	12.8	11.3	10.7
P/B (x)	3.2	2.7	2.3	2.0
EV/EBITDA (x)	13.0	10.3	9.3	8.4
Dividend Yield	2.2%	2.2%	2.2%	2.8%

Source: Company data, Al Rajhi Capital

Performance



Source: Bloomberg, Company data, Al Rajhi Capital

Company summary

Saudi Ceramic Company is one of the oldest and leading ceramics producers in the Middle East with a market value of around SAR4.1bn. The company manufactures and markets ceramic products such as ceramic tiles, sanitary ware (bathroom products) and road markers. In addition, the company manufactures water heaters as well. The company intends to launch the production of red bricks by 2014.

Saudi Ceramic Expansion plan key growth driver

Saudi Ceramic reported robust results in Q1 2013, meeting our revenue expectations. Nevertheless, the company beat our profit estimate owing to higher than expected gross margins on both its major product lines. We believe Saudi Ceramic will continue to benefit from the boom in the construction sector and higher government spending, as well as its investment in advanced technologies. Moreover, the company's planned expansions will further boost growth over the next few years. Therefore, we have raised our target price to SAR116 per share, indicating a 4.5% upside from the current levels. We thus have a Neutral rating on the stock.

Double digit growth in revenues: Saudi Ceramic reported a 13% revenue growth in Q1 2013 to reach SAR406mn, which was almost in line with our 14% growth expectation. This growth was due to higher sales volume of ceramics and sanitary ware, and water heaters. We believe the company's top-line will grow at 13% this year, supported by a steady increase in production capacity.

Margin improvement: The company's gross margin grew by a significant 600bps, driven by rising margins of major divisions, ceramics and sanitary ware (400bps), and water heaters (1,100bps). We believe that the stability in raw material supplies and improvement in operational efficiencies will enable the company to maintain gross margin above 35% for the entire 2013.

Expansion plan to boost growth: Saudi Ceramic has lined up several expansion plans to ensure double digit growth over the next few years. The most prominent one among them is a new sanitary ware factory with a capacity of 18,000 tons, which is due to commence production in H1 2014. In line with the company's estimates, we expect a top-line contribution of SAR75mn from the new line when it reaches its full capacity. Another expansion plan is the new red bricks factory with a capacity of 330,000 tons, scheduled to launch in the second half of 2014. We estimate a top-line contribution of about SAR63mn from the new bricks factory. Furthermore, the ongoing installation of the tile factory, which is expected to start production in Q3 2013, will increase the company's tiles production to 60mn square meter.

Valuation method changed: We have changed our valuation method from EVA to a blended approach based on DCF and relative valuation. As per DCF, our fair value stands at SAR125, while, we assign a fair value to SAR93 under relative valuation. Our target price carries a 70-30% weight on the above methods and thus, we arrive at a new target price of SAR116.

Period End (SAR)	12/11A	12/12A	12/13E	12/14E	12/15E
Revenue (mn)	1,221	1,447	1,636	1,909	2,088
Revenue Growth	13.1%	18.5%	13.0%	16.7%	9.3%
Gross profit margin	36.5%	33.1%	35.4%	34.1%	33.2%
EBITDA margin	29.8%	26.7%	29.4%	27.9%	27.6%
Net profit margin	19.0%	17.1%	19.9%	19.4%	18.6%
EPS	6.19	6.60	8.68	9.86	10.35
EPS Growth	5.8%	6.7%	31.5%	13.5%	5.1%
ROE	21.6%	20.2%	22.9%	22.1%	19.8%
ROCE	15.2%	13.7%	15.9%	16.0%	14.9%
Capex/Sales	22.6%	19.7%	16.8%	15.0%	12.0%

Source: Company data, Al Rajhi Capital



Saudi Ceramic steady growth, stable margins

We estimate Saudi Ceramic to maintain its steady performance

With an estimated size of about SAR5.2bn, the Saudi ceramics market is one of the biggest in the MENA region. We expect the market to grow steadily, driven by increasing population, rising disposable income, booming construction industry and higher government spending. The ceramic tiles market in Saudi Arabia is dominated by imported products, which represent around 70% of the market. Saudi Ceramic holds a 25% share, while the remaining 5% share is held by small private companies such as Alfannar, Future Ceramic and Al-Jawdah Ceramic. Saudi Ceramic's business consists of two segments: Ceramic tiles & bathroom products (sanitary ware), and Water heaters. In Q1 2013, ceramic tiles segment contributed 77% of total revenues, whereas water heaters contributed 23%. Both the divisions have performed decently in the recent past; the ceramic tiles and bathroom products segment reported a 14% y-o-y growth in Q1, while the water heaters segment grew by 10%. We believe the ceramic tiles and bathroom products segment will drive the company's growth over the medium term and further boosted by the capacity expansions coupled with the increasing demand from government projects.

Gross margins for Saudi Ceramic remained stable over the last four years at about 36.5%, except for 2012, where gross margins dropped by 250bps to 33%. This was mainly attributed to an increase in production costs on account of higher transport costs incurred by the company. The imposition of time limits on the entry of trucks into Riyadh since 2012 has led to higher transport costs, which created inconvenience for several companies including Saudi Ceramic. Later in the year, this time limit was extended to provide some relief for the companies. Further, the installation of new machineries increased the operational efficiency at the factories and therefore, we believe the low profit margin was an exception in 2012. Going ahead, we estimate Saudi Ceramic's gross margin to remain stable at around 35% for the rest of 2013.

Valuation

Changed valuation methodology

We have changed our valuation methodology from the earlier Economic Value Added (EVA) to a blended methodology, combining the DCF and Relative Valuation (RV) methodologies.

We have used a two-stage DCF model, with an explicit period of five years till 2017, and a terminal value after 2017. For Saudi Ceramic, our DCF fair value came in at SAR125 based on our 8.1% WACC and 2.5% long term growth. As per relative valuation, we have compared Saudi Ceramic's multiples with its GCC peers, i.e., Alanwar in Oman and Rak in UAE. Saudi Ceramic is the largest ceramic company in the GCC region and thus, trades at a above average valuation as compared to its peers. As per relative valuation, we assign a fair value of SAR93 to Saudi Ceramic. Our target price carries a 70% weight for DCF and 30% for relative valuation. Thus, our new target price is SAR116, which is 29% higher than our previous target of SAR86.7. However, we are Neutral on Saudi Ceramic, considering the recent rally witnessed in the stock.

Figure 1 Relative Valuation

	Market cap.	EV	P/E		EV/EBITDA	
	(US\$)	(US\$)	2013E	2014E	2013E	2014E
Saudi ceramic	4,172	4,825	12.8	11.3	10.3	9.3
Alanwar	104	99	13.8	11.6	9.4	8.5
RAK	1,330	3,088	5.8	5.1	7.6	7.2
Average			10.8	9.3	9.1	8.3

Source: Company data, Bloomberg, Al Rajhi Capital

Our new target price is based on DCF and relative valuation



Income Statement (SARmn)	12/11A	12/12A	12/13E	12/14E	12/15E
Revenue	1,221	1,447	1,636	1,909	2,088
Cost of Goods Sold	(775)	(968)	(1,057)	(1,257)	(1,395)
Gross Profit	446	479	579	652	692
Government Charges					
S.G. & A. Costs	(203)	(221)	(225)	(251)	(273)
Operating EBIT	244	258	354	401	419
Cash Operating Costs	(857)	(1,060)	(1,155)	(1,376)	(1,512)
EBITDA	365	387	481	533	576
Depreciation and Amortisation	(121)	(129)	(127)	(132)	(157)
Operating Profit	244	258	354	401	419
Net financing income/(costs)	(4)	(2)	(19)	(20)	(21)
Forex and Related Gains					
Provisions	-	-	-	-	-
Other Income					
Other Expenses					
Net Profit Before Taxes	239	256	336	381	398
Taxes	(7)	(9)	(10)	(11)	(10)
Minority Interests					
Net profit available to shareholders	232	248	326	370	388
Dividends	(88)	(94)	(94)	(94)	(116)
Transfer to Capital Reserve					
	12/11A	12/12A	12/13E	12/14E	12/15E
Adjusted Shares Out (mn)	37.50	37.50	37.50	37.50	37.50
CFPS (SAR)	9.41	10.04	12.07	13.37	14.55
EPS (SAR)	6.19	6.60	8.68	9.86	10.35
DPS (SAR)	2.333	2.500	2.500	2.500	3.106
Growth	12/11A	12/12A	12/13E	12/14E	12/15E
Revenue Growth	13.1%	18.5%	13.0%	16.7%	9.3%
Gross Profit Growth	13.8%	7.4%	20.8%	12.6%	6.2%
EBITDA Growth	14.7%	6.1%	24.4%	10.8%	8.0%
Operating Profit Growth	10.4%	5.8%	37.5%	13.2%	4.4%
Net Profit Growth	5.8%	6.7%	31.5%	13.5%	5.1%
EPS Growth	5.8%	6.7%	31.5%	13.5%	5.1%
Margins	12/11A	12/12A	12/13E	12/14E	12/15E
Gross profit margin	36.5%	33.1%	35.4%	34.1%	33.2%
EBITDA margin	29.8%	26.7%	29.4%	27.9%	27.6%
Operating Margin	20.0%	17.8%	21.7%	21.0%	20.1%
Pretax profit margin	19.6%	17.7%	20.5%	20.0%	19.1%
Net profit margin	19.0%	17.1%	19.9%	19.4%	18.6%
Other Ratios	12/11A	12/12A	12/13E	12/14E	12/15E
ROCE	15.2%	13.7%	15.9%	16.0%	14.9%
ROIC	14.1%	13.6%	16.6%	17.5%	16.3%
ROE	21.6%	20.2%	22.9%	22.1%	19.8%
Effective Tax Rate	3.1%	3.3%	3.0%	3.0%	2.5%
Capex/Sales	22.6%	19.7%	16.8%	15.0%	12.0%
Dividend Payout Ratio	37.7%	37.9%	28.8%	25.4%	30.0%
Valuation Measures	12/11A	12/12A	12/13E	12/14E	12/15E
P/E (x)	18.0	16.8	12.8	11.3	10.7
P/CF (x)	11.8	11.1	9.2	8.3	7.6
P/B (x)	3.6	3.2	2.7	2.3	2.0
EV/Sales (x)	4.0	3.5	3.0	2.6	2.3
EV/EBITDA (x)	13.5	13.0	10.3	9.3	8.4
EV/EBIT (x)	20.2	19.5	13.9	12.3	11.5
EV/IC (x)	2.7	2.4	2.2	2.0	1.8
Dividend Yield	2.1%	2.2%	2.2%	2.2%	2.8%

Source: Company data, Al Rajhi Capital



Balance Sheet (SARmn)	12/11A	12/12A	12/13E	12/14E	12/15E
Cash and Cash Equivalents	64	57	272	263	400
Current Receivables	136	132	151	267	276
Inventories	535	598	594	614	689
Other current assets	57	106	122	122	122
Total Current Assets	793	893	1,139	1,266	1,486
Fixed Assets	1,415	1,572	1,720	1,874	1,967
Investments	61	81	80	80	80
Goodwill	-	-	-	-	-
Other Intangible Assets	-	-	-	-	-
Total Other Assets	-	-	-	-	-
Total Non-current Assets	1,476	1,653	1,800	1,954	2,047
Total Assets	2,269	2,546	2,939	3,219	3,533
Short Term Debt	355	333	341	341	341
Accounts Payable	175	201	222	227	246
Accrued Expenses	-	-	-	-	-
Dividends Payable	-	4	-	-	-
Other Current Liabilities	78	55	73	73	73
Total Current Liabilities	620	618	650	655	674
Long-Term Debt	454	570	700	700	700
Other LT Payables	-	-	-	-	-
Provisions	48	52	55	55	55
Total Non-current Liabilities	502	622	755	755	755
Minority interests	-	-	-	-	-
Paid-up share capital	250	375	375	375	375
Total Reserves	897	931	1,159	1,435	1,729
Total Shareholders' Equity	1,147	1,306	1,534	1,810	2,104
Total Equity	1,147	1,306	1,534	1,810	2,104
Total Liabilities & Shareholders' Equity	2,269	2,546	2,939	3,219	3,533
Ratios	12/11A	12/12A	12/13E	12/14E	12/15E
Net Debt (SARmn)	744	846	769	778	641
Net Debt/EBITDA (x)	2.04	2.19	1.60	1.46	1.11
Net Debt to Equity	64.9%	64.8%	50.1%	43.0%	30.4%
EBITDA Interest Cover (x)	83.4	225.2	25.6	26.3	28.1
BVPS (SAR)	30.58	34.82	40.91	48.26	56.12
Cashflow Statement (SARmn)	12/11A	12/12A	12/13E	12/14E	12/15E
Net Income before Tax & Minority Interest	239	256	336	381	398
Depreciation & Amortisation	121	129	127	132	157
Decrease in Working Capital	(19)	(101)	6	(130)	(64)
Other Operating Cashflow	9	13	(22)	(11)	(10)
Cashflow from Operations	350	297	446	371	482
Capital Expenditure	(276)	(286)	(275)	(286)	(251)
New Investments	(9)	(24)	-	-	-
Others	-	-	-	-	-
Cashflow from investing activities	(285)	(310)	(275)	(286)	(251)
Net Operating Cashflow	65	(12)	171	85	231
Dividends paid to ordinary shareholders	(88)	(89)	(94)	(94)	(94)
Proceeds from issue of shares	-	-	-	-	-
Effects of Exchange Rates on Cash	-	-	-	-	-
Other Financing Cashflow	-	-	-	-	-
Cashflow from financing activities	(40)	6	43	(94)	(94)
Total cash generated	25	(7)	214	(9)	137
Cash at beginning of period	39	64	57	272	263
Implied cash at end of year	64	57	272	263	400
Ratios	12/11A	12/12A	12/13E	12/14E	12/15E
Capex/Sales	22.6%	19.7%	16.8%	15.0%	12.0%

Source: Company data, Al Rajhi Capital



Disclaimer and additional disclosures for Equity Research

Disclaimer

This research document has been prepared by Al Rajhi Capital Company ("Al Rajhi Capital") of Riyadh, Saudi Arabia. It has been prepared for the general use of Al Rajhi Capital's clients and may not be redistributed, retransmitted or disclosed, in whole or in part, or in any form or manner, without the express written consent of Al Rajhi Capital. Receipt and review of this research document constitute your agreement not to redistribute, retransmit, or disclose to others the contents, opinions, conclusion, or information contained in this document prior to public disclosure of such information by Al Rajhi Capital. The information contained was obtained from various public sources believed to be reliable but we do not guarantee its accuracy. Al Rajhi Capital makes no representations or warranties (express or implied) regarding the data and information provided and Al Rajhi Capital does not represent that the information content of this document is complete, or free from any error, not misleading, or fit for any particular purpose. This research document provides general information only. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other investment products related to such securities or investments. It is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of any specific person who may receive this document.

Investors should seek financial, legal or tax advice regarding the appropriateness of investing in any securities, other investment or investment strategies discussed or recommended in this document and should understand that statements regarding future prospects may not be realized. Investors should note that income from such securities or other investments, if any, may fluctuate and that the price or value of such securities and investments may rise or fall. Fluctuations in exchange rates could have adverse effects on the value or price of, or income derived from, certain investments. Accordingly, investors may receive back less than originally invested. Al Rajhi Capital or its officers or one or more of its affiliates (including research analysts) may have a financial interest in securities of the issuer(s) or related investments, including long or short positions in securities, warrants, futures, options, derivatives, or other financial instruments. Al Rajhi Capital or its affiliates may from time to time perform investment banking or other services for, solicit investment banking or other business from, any company mentioned in this research document. Al Rajhi Capital, together with its affiliates and employees, shall not be liable for any direct, indirect or consequential loss or damages that may arise, directly or indirectly, from any use of the information contained in this research document.

This research document and any recommendations contained are subject to change without prior notice. Al Rajhi Capital assumes no responsibility to update the information in this research document. Neither the whole nor any part of this research document may be altered, duplicated, transmitted or distributed in any form or by any means. This research document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or which would subject Al Rajhi Capital or any of its affiliates to any registration or licensing requirement within such jurisdiction.

Additional disclosures

1. Explanation of Al Rajhi Capital's rating system

Al Rajhi Capital uses a three-tier rating system based on absolute upside or downside potential for all stocks under its coverage except financial stocks and those few other companies not compliant with Islamic Shariah law:

"Overweight": Our target price is more than 15% above the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

"Neutral": We expect the share price to settle at a level between 5% below the current share price and 15% above the current share price on a 6-9 month time horizon.

"Underweight": Our target price is more than 5% below the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

2. Definitions

"Time horizon": Our analysts make recommendations on a 6-9 month time horizon. In other words, they expect a given stock to reach their target price within that time.

"Fair value": We estimate fair 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.

"Target price": This may be identical to estimated fair value per share, but is not necessarily the same. There may be very good reasons why a share price is unlikely to reach fair value within our time horizon. In such a case we set a target price which differs from estimated fair value per share, and explain our reasons for doing so.

Please note that the achievement of any price target may be impeded by general market and economic trends and other external factors, or if a company's profits or operating performance exceed or fall short of our expectations.

Contact us

Jithesh Gopi, CFA
Head of Research
Tel : +966 11 2119332
gopij@alrajhi-capital.com

Al Rajhi Capital
Research Department
Head Office, King Fahad Road
P.O. Box 5561
Riyadh 11432
Kingdom of Saudi Arabia
Email: research@alrajhi-capital.com

Al Rajhi Capital is licensed by the Saudi Arabian Capital Market Authority, License No. 07068/37.