



Petrochem reported net income of SAR 171mn, above our estimates of SAR 153.4mn due to higher than expected revenue. Revenue was supported by improved operating rate; where Polymers plant' operating rate increased to the highest record since inception. Q/Q Gross margin declined to 25.28% from 27.38% in 2Q-19; as a result of the revised feedstock prices mechanism(Ethan/Propane) during 3Q-19. Despite the weak product prices, the company's ability to increase its production efficiency and operating rates are the key support for FY20 and onwards. We upgrade our recommendation to **"Overweight"** on the stock with revised TP of **SAR 26.0/share**.

- National Petrochemical Company (Petrochem) posted net income of SAR 171mn; indicating a decline of 44.3%Y/Y and 6.6%Q/Q. Q3-19 net profit came above our and consensus estimates of SAR 153.4mn and SAR 149.1mn. The Y/Y decline was mainly associated with a decrease in product prices and product spreads. The deviation of Q3-19 earnings from our estimates is mainly ascribed to higher volumetric sales; which could be due to an increase in inventory utilization and improved operating rate.
- Petrochem Co. reported 18.6%Q/Q upsurge in revenue for Q3-19 to SAR 1,958mn, well above our estimates of SAR 1,588mn due to improved operating rate. We assume the plant was running at a utilization rate of 105%, as compared to our estimate of 87.0% and 83.5% in Q2-19. During the quarter, average selling prices of PP declined by 6.0%Q/Q and 16.3%Y/Y. Polystyrene plunged by 6.9%Q/Q and 22.7%Y/Y. Average selling price of HDPE declined by 6.7%Q/Q and 26.1%Y/Y.
- Gross profit stood at SAR 495mn; depicting a decline of 32.7%Y/Y and an increase of 9.5%Q/Q, above our estimate of SAR 430.2mn due to higher than expected revenue. Gross margin stood at 25.28% in Q3-19 vs. 27.38% in 2Q-19 and against our estimates of 27.1%. This we believe is due to implementation of the new feedstock prices (Ethan/Propane) during 3Q-19, which indicates lower spreads across products. In Q3-19, the change in feedstock price compared to the final product prices has resulted in PP-Naphtha spreads to decline by 3.8%Q/Q to USD 685/tonne from USD 712/tonne in 2Q-19.
- Operating profit stood at SAR 335mn, depicting a decline of 41.4%Y/Y and an increase of 4.4%Q/Q, where the company witnessed a remarkable increase in OPEX (SG & A) to record SAR 160mn as compared to SAR 130.8mn in 2Q-19 due to higher sales.

**AJC View:** Despite the weaker than expected gross margin and weak product prices, we believe that the production efficiency and operating rate will continue to be positively reflected on the sales volume. Polymers plant's average operating rate is expected to stabilize above 95% in FY19 and 98% in FY20, as compared to an average of 90% during FY18. We expect the sudden upsurge in production capacity could be due to either outsourcing basic materials from the local market or obtaining additional feedstock from Aramco. On the other hand, new feedstock prices was completely applied during 3Q-19, where the grace period on Ethane and Propane ended in Aug/Sep FY19 (Propane represents almost 60% of the company's feedstock). During September, propane price was set at a 20% discount on Saudi Aramco Propane prices, as compared to previous 28% discount on Naphtha prices. The company is trading at a forward TTM PE of 10.8x based on our FY20 earnings forecast, lower than the current sector average PE of 17.1x. We upgrade our recommendation to **"Overweight"** on the stock with revised TP of **SAR 26.0/share**.

## Results Summary

SARmn	Q3-18	Q2-19	Q3-19	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
<b>Revenue</b>	<b>2,297</b>	<b>1,651</b>	<b>1,958</b>	<b>-14.7%</b>	<b>18.6%</b>	<b>23.4%</b>
Gross Profit	736	452	495	-32.7%	9.5%	15.1%
<b>Gross Margin</b>	<b>32.04%</b>	<b>27.38%</b>	<b>25.28%</b>	-	-	-
EBIT	569	321	335	-41.1%	4.4%	9.1%
<b>Net Profit</b>	<b>307</b>	<b>183</b>	<b>171</b>	<b>-44.3%</b>	<b>-6.6%</b>	<b>11.5%</b>
EPS	0.64	0.38	0.36	-	-	-

Source: Company Reports, Aljazira Capital

## Overweight

Target Price (SAR) **26.0**

Upside / (Downside)\* **18.7%**

Source: Tadawul \*prices as of 28<sup>th</sup> of October 2019

## Key Financials

SARmn (unless specified)	FY17	FY18	FY19E	FY20E
Revenue	7,367	8,930	7,444	7,812
Growth %	21.4%	21.3%	-16.6%	5.0%
Net Income	888	1,165	718	978
Growth %	123.5%	31.2%	-38.4%	36.2%
EPS	1.85	2.43	1.50	2.04

Source: Company reports, Aljazira Capital

## Key Ratios

	FY17	FY18	FY19E	FY20E
Gross Margin	30.7%	30.1%	26.4%	30.2%
Net Margin	12.1%	13.1%	9.6%	12.5%
P/E	10.0x	10.6x	14.6x	10.8x
P/B	1.31x	1.65x	1.28x	1.20x
EV/EBITDA (x)	5.50x	5.14x	5.84x	4.50x
Dividend Yield	2.7%	1.9%	2.3%	4.6%

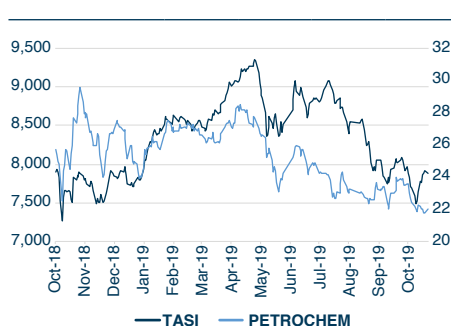
Source: Company reports, Aljazira Capital

## Key Market Data

Market Cap (bn)	10.53
YTD %	-9.5%
52 Week (High)/(Low)	29.60/21.74
Shares Outstanding (mn)	480.00

Source: Company reports, Aljazira Capital

## Price Performance



Source: Tadawul, Aljazira Capital

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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.

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