Bawan Company

Engineering - Industrial
BAWAN AB: Saudi Arabia
21 May 2023

US$0.507bn	76.06%	US$6.14mn
Market Cap	Free Float	Avg. Daily Volume

Target price	37.00	16.7% above current
Current price	31.70	as at 18/05/2023

Existing rating

Underweight | Neutral | **Overweight**

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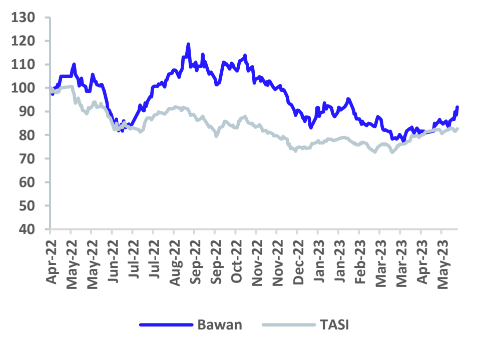
Performance (Rebased to 100)



Earnings

(SARmn)	2022A	2023E	2024E
Revenue	3,632	3,717	3,801
Revenue growth	13%	2%	2%
Gross profit	447	459	468
Gross margin	12%	12%	12%
EBITDA	303	313	320
EBITDA margin	8%	8%	8%
Net profit	163	170	180
Net margin	4%	5%	5%
EPS	2.7	2.8	3.0
DPS	1.5	1.6	1.7
Payout ratio	55%	55%	55%
EV/EBITDA	8.4x	8.0x	7.7x
P/E	11.7x	11.2x	10.6x
RoE	18.9%	18.1%	17.7%

Source: Company data, Al Rajhi Capital.

Bawan Co.

Target price increased to SAR37/sh, margins to recover in second half

Bawan reported Q1 2023 revenue at SAR944mn with a -1.0% decline y-o-y. However, the revenue was marginally higher than our estimate of SAR935mn. The revenues in the Steel and Wood segment declined by 4.4% y-o-y in Q1 2023. Nonetheless, the Electrical segment surprised with ~15% growth in revenues y-o-y. We note that revenues in the Metal segment took a hit due to the volatility in steel prices, specifically on the downside. Consequently, the contribution of Metal and wood segment to the bottom line fell sharply y-o-y. The Electricity segment constituted 52% of the net profits in Q1 2023 compared to a mere 6% in Q1 2022. Steel and wood contributed 24% to net profit (versus 66% in Q1 2022) followed by 14% from the plastic segment, and 4% from the Concrete segment. However, in our view, a part of the volatility in steel prices in Q1 2023 can be attributed to the market's exaggeration of China reopening after exiting from its zero covid policy. We believe that steel prices might be close to hitting the bottom at the back of Q2 2023 future prices being close to the spot price in the short term. Hence, H2 2023 shall see some recovery in margins in the steel segment. Although, the wood and concrete segment saw slowdown in revenues owing to lower volumes, our outlook for the wood, plastic and concrete segment remains stable in the near term. On the other hand, the performance in the electricity segment was robust and it shall stand to benefit from the strong order backlog in place. Going forward, we expect healthy margins in the electricity segment margins to sustain for 2023. Gross Margins of Bawan Company fell from 13% in Q1 2022 to 11% in Q1 2023 at the back of increased cost of sales. The net income fell by 31.0% y-o-y due to higher interest burden. However, the high financing cost scenario will reverse in the medium term. Besides, the outlook for the metal vertical looks geared up for recovery in the second half. Although revenues for 2023 are estimated to grow marginally by 2% y-o-y, margins will continue to be stable as 2022. Overall, post-Q1 2023 earnings we revise our estimates upwards and increase our target price to SAR37/sh, from the earlier target price of SAR32/sh and maintain our rating at "Overweight".

Figure 1 **Earnings Summary Q4 2022**

(SARmn)	Q1 2023	Q4 2022	Q1 2022	% chg q-o-q	% chg y-o-y	ARC Estimates
Revenue	944	951	950	-1%	-1%	935
Gross Profit	100	113	125	-12%	-20%	115
Gross Margin	*11%*	*12%*	*13%*	*NA*	*NA*	*12%*
Operating Profit	47	52	67	-11%	-30%	53
Operating Margin	*5%*	*5%*	*7%*	*NA*	*NA*	*6%*
Net Profit	35	30	50	16%	-31%	36
Net Margin	*4%*	*3%*	*5%*	*NA*	*NA*	*4%*

Source: Company data, Al Rajhi Capital

Valuations: We value the company based on an equal mix of DCF and relative valuation. The DCF-based target price has a 2% terminal growth and 11.2% WACC and comes to SAR38/sh. P/E based relative valuation has a 13x multiple and gives a target price of SAR37/sh. Thus, we revise our target price for the company to SAR37/sh, implying an upside of 16.7%, and maintain our rating at “Overweight”.

Risks: The key downside risks to our valuation assumptions are further slump in steel prices, lower mortgage demand, adverse movement of commodity prices, and an increase in the working capital requirement, resulting in an increase in leverage.

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"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

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