SIPCHEM

Petrochemicals – Industrial

SIPCHEM AB: Saudi Arabia

21 October 2021

US$9.181bn	90%	US$35.80mn
Market cap	Free float	Avg. daily volume

Target price	48.00	+2.2% over current
Current price	46.95	as at 20/10/2021

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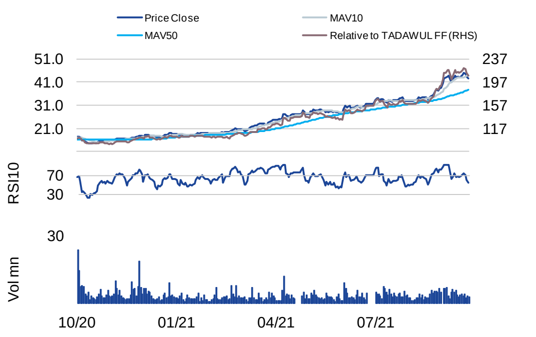
Existing rating

Underweight	Neutral	Overweight

Performance



Source: Bloomberg

Earnings

(SARmn)	2020	2021e	2022e
Revenue	5,323	9,567	8,959
Y-o-Y	-2.1%	79.7%	-6.4%
Gross profit	1,173	5,270	4,928
Gross margin	22.0%	55.1%	55.0%
EBITDA	1,291	5,019	4,660
EBITDA margin	24.3%	52.5%	52.0%
Net profit	176	3,112	3,043
Net margin	3.3%	32.5%	34.0%
EPS (SAR)	0.24	4.24	4.15
DPS (SAR)	0.50	1.50	2.00
Payout ratio	208.5%	35.3%	48.2%
ROE	0.7%	11.8%	10.7%
EV/EBITDA	28.4x	7.3x	7.9x
P/E	NM	11.1x	11.3x

Source: Company data, Al Rajhi Capital

SIPCHEM

Q3: Robust earnings; TP maintained at SAR48/sh.

Sipchem reported exceptional Q3 numbers, with quarterly net income reaching a new high, beating our and consensus estimates on the back of increased product prices, and better-operating efficiencies. In Q4 so far, average Methanol prices (Generic 1st 'ZME' Future) are up ~40% q-o-q, mainly aided by rising oil prices, healthy Methanol demand (likely to surpass the pre-COVID levels by the end of the year), and tighter supply. While one may note that Methanol prices have cooled slightly of late (from US$624/tonne to US$563 in the past 7 trading sessions), we are not yet concerned as we have baked in a margin of safety in our estimates with only US$420/t for Methanol for 2021E and US$400/t for 2022E. Also, Polypropylene prices (currently at ~US$1,420/tonne) are trading above our estimate (2021E: US$1,280/t, 2022E: US$1,310/t). Overall, we remain positive on the company, on the back of i) relatively higher product prices, ii) improving demand post economic recovery, iii) better efficiencies on cost optimization and synergy realization, and iv) a possibility of better dividend outlook. The company is also likely to continue benefiting from high operating leverage. Accordingly, we expect the company to distribute a DPS of SAR1.5 for 2021 (vs. SAR0.5/sh in 2020) with a possibility of further upside next year. Based on our DCF valuation, we maintain our TP at SAR48/sh but revise rating to Neutral (earlier Overweight) post ~24% rise in share price over the past 1 month.

Figure 1 SIPCHEM Q3 2021 results

(SAR mn)	Q3 2021	Q3 2020	Y-o-Y	Q2 2021	Q-o-Q	ARC est	vs ARC
Revenue	**2,506**	**1,362**	**84.0%**	**2,363**	**6.0%**	**2,417**	**3.7%**
Gross profit	1,369	220	521.6%	1,478	-7.3%	1,450	-5.6%
Gross margin	54.6%	16.2%		62.5%		60.0%	
Operating profit	1,140	18	6337.9%	1,140	0.0%	1,123	1.5%
Operating margin	45.5%	1.3%		48.2%		46.4%	
Net profit	**1,030**	**10**	10195.0%	**830**	24.1%	**935**	10.1%
Net margin	41.1%	0.7%		35.1%		38.7%	

Source: Company data, Al Rajhi Capital.

Q3 results: Top-line rose ~6% q-o-q to SAR2,506, largely in line with our estimate of SAR2,417mn (consensus: SAR2,251mn), primarily due to increased prices for some of the products. However, higher-than-expected costs resulted in the gross profit below our estimate. Nonetheless, the company was able to reduce the administrative costs, aided by its ongoing cost optimization initiates. This, along with lower zakat and higher equity income, pushed the net profit above estimate. Overall, the company reported a net profit of SAR1,030mn, above our (SAR935mn) and consensus (SAR756mn) estimates.

Will Methanol price sustain at this level? While there is no certainty, as long as gas, oil, and coal prices stay around these levels, the Methanol price may remain firm – but the key risk to note is that these prices may come down abruptly once we get closer to the end of Winter. In the last spike for gas, high prices persisted for a little more than a month but this time has more additional variables – mainly lower coal supply in China.

Valuation and Risks: We value Sipchem using DCF (based on FCF, cost of equity 11.3%) at SAR48/share, implying a Neutral rating (earlier: Overweight) for the stock. The stock currently trades at ~11x on our 2021/22E EPS, lower than the historical three years' average of 16.8x.

Key upside drivers are better-than-expected prices, announcement of new projects, suspending unprofitable ventures, and above-expected dividends. Major downside risks to earnings involve unexpected disruption at the company's upstream operations, which can further impact its downstream plants as well and persistent weakness in product prices, particularly oil and Methanol prices. The change in prices could be abrupt.

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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

"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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