# Al Yamamah Steel Industries Co

**Metals – Industrial**
YAMAMAH AB: Saudi Arabia
1 September 2021

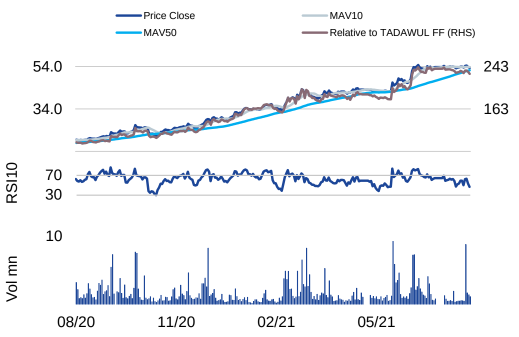
| US$0.684bn | 39% | US$22.57mn |
|---|---|---|
| Market cap | Free float | Avg. daily volume |

| | | |
|---|---|---|
| Target price | 55.00 | 8.9% over current |
| Current price | 50.50 | as at 1/9/2021 |

**Existing rating**

| Underweight | Neutral | Overweight |
|---|---|---|

### Performance



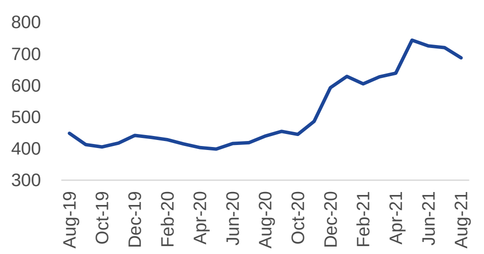
Source: Bloomberg

### Earnings

| (SARmn) | 2020A | 2021E | 2022E |
|---|---|---|---|
| Revenue | 1,867 | 1,730 | 1,885 |
| Revenue growth | 95% | -7% | 9% |
| Gross profit | 202 | 380 | 301 |
| Gross margin | 11% | 22% | 16% |
| EBITDA | 154 | 344 | 269 |
| EBITDA margin | 8% | 20% | 14% |
| Net profit | 51 | 226 | 145 |
| Net margin | 3% | 13% | 8% |
| EPS | 1.00 | 4.45 | 2.85 |
| DPS | 1.00 | 1.00 | 1.25 |
| Payout ratio | 100% | 22% | 44% |
| P/E | 50.6x | 11.4x | 17.7x |
| EV/EBITDA | 20.4x | 8.3x | 11.0x |
| RoE | 7.9% | 27.6% | 16.1% |

**Source:** Company data, Al Rajhi Capital

### LME Steel Rebar (USD/MT)



**Source:** Company data, Al Rajhi Capital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# Al Yamamah Steel Industries Co

## Beat Estimate but reduce TP to SAR55/sh as margins to remain volatile

*Al Yamamah Steel Industries Co (Yamamah) Q3 2021 revenue came in at SAR406mn (+2.7% y-o-y) higher than our estimate of SAR374mn. Higher commodity prices led to a better realization of the construction product price, which grew 54.8% y-o-y. On the flip side, the construction product volume declined 33% y-o-y, mainly due to inventory management exercise to avoid exposure to higher cost inventory (as the steel prices remained elevated during Q3 2021) in case of any slump in demand. Gross profit increased more than 3x y-o-y to SAR104mn, as the margins expanded to 25.6% (8.2% in Q3 2020 and 22.3% in Q2 2021) due to favourable pricing environment for the final product. Improvement in gross income and lower finance cost, on the back of debt reduction, resulted in ~70x y-o-y growth in net income to SAR65mn; this was better than our estimate of SAR36mn.*

**Outlook:** Overall, while the results have been better than our expectation, we feel that the current margins might not be sustainable, as the fresh lockdowns in China and concerns over delta variants across the world has led to some softening of the steel prices globally. Though this will help the company in procuring the raw materials at a lower cost, the overall spread will go down compared to recent quarters. That said, we continue to be optimistic on the overall construction spending in the Kingdom. This in turn should drive the volume growth over the coming period, with an improvement in capacity utilization for both construction and electricity segment in coming years and stable pricing scenario. Given this, we expect margins to stabilize at around 16% in FY 2022e. Therefore, post-Q3 2021 earnings, we reduce our target price from SAR65/sh to SAR55/sh, and reduce our rating to "Neutral".

- **Revenue:** Top line grew by 2.7% y-o-y, driven mainly by 3.5% y-o-y growth in the revenue from the construction segment. Construction segment revenue was aided by an 54.8% y-o-y improvement in product prices, though product volume fell by 33% y-o-y. Revenue from the electricity segment on the other hand fell by 1.4% y-o-y.
- **Operating income:** Operating income grew by more than 6x to SAR83 mn for Q3 2021, as operating margins improved to 20.5% in Q3 2021 (17.5% in Q2 2021 and 3.2% Q3 2020).
- **Net income:** In line with an improvement in revenue and margins, net income grew to SAR65 mn in Q3 2021, corresponding to a net income of SAR1 mn in Q3 2020.

**Figure 1 Earnings Summary**

| SAR(mn) | Q3 2021 | Q2 2021 | Q3 2020 | % chg y-o-y | % chg q-o-q | ARC est |
|---|---|---|---|---|---|---|
| Revenue | 406 | 453 | 395 | 3% | -10% | 374 |
| Gross Profit | 104 | 101 | 32 | 220% | 3% | 76 |
| Gross Margin | 26% | 22% | 8% | NM | NM | 20% |
| Operating Income | 83 | 79 | 13 | 555% | 4% | 53 |
| Net income | 65 | 60 | 1 | NM | 8% | 36 |

**Source:** Company data, Al Rajhi Capital

## Key growth drivers:

1. Strong construction activity driven by offtake of GIGA projects to aid volume growth in construction as well as electricity segment
2. Infrastructure spending to aid in improvement in electricity segment
3. Capacity expansion in construction sector and completion of solar power plant project a long-term catalyst

**Valuation:** We value Yamamah using the relative valuation methodology (P/E). The P/E-based relative valuation, based on a 21.0x multiple, gives us a target price of SAR55/sh, which implies an upside of 8.9% from the current market price of SAR50.5/sh.

## Key Risks:

1. Fall in oil prices, resulting in lower government spending and a fall in construction activity
2. Fall in average realization, resulting in lower revenue and lower profitability
3. Adverse movement in raw material prices and an inability of the company to pass on the same could have an adverse impact on the profitability
4. Mortgage industry is labour intensive and any shortage in labour, due to Covid related traveling restrictions, could result in delay in projects, impacting company's revenue

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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.

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