Advanced Petrochemical Company

Materials| Advanced| 2330

INTELLIGENT INVESTMENT IDEAS

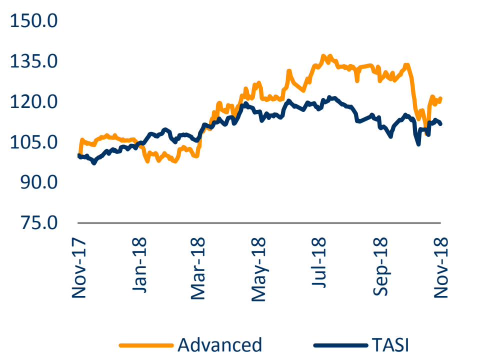
3Q 2018 Results Update **Nov 06, 2018**

Recommendation	**Overweight**
Previous Recommendation	Overweight
Current Price (SAR)	49.6
Target Price (SAR)	56.5
Upside/Downside (%)	14.0%

As of November 06th 2018

Key Data (Source: Bloomberg)	
Market Cap (SAR bn)	9.8
52 Wk High (SAR)	57.2
52 Wk Low (SAR)	41.9
Total Outstanding shares (in mn)	197
Free Float (%)	93.6%

Advanced vs. TASI (Rebased)



Price Performance (%)	**Absolute**	**Relative**
1m	(8.5%)	(6.0%)
6m	(3.0%)	0.8%
12m	21.2%	9.4%

Major Shareholders (%)	
Polypropylene National Company	7.95%
General Organization for Social Insurance	6.37%

Quarterly Sales (SAR bn) and Operating Margin

Source: Bloomberg, Company Financials, FALCOM Research; Data as of November 06th 2018

Higher feedstock costs affected 3Q18 earnings

Advanced Petrochemical (Advanced)'s net profit declined 3.0% YoY, dragged by higher feedstock costs, operating expenses, and financial expenses. Although revenues increased 20.9% YoY boosted by higher polypropylene (PP) prices and selling volumes, a 33.6% YoY rise in feedstock costs led to decline in gross margins. Furthermore, a 3.5% increase in operating expenses squeezed operating profit margins, which declined to 25.6% in 3Q18 from 31.7% in 3Q17. Higher financial expenses and zakat further narrowed the bottom line. Sequentially, Advanced's net profit fell 20.2%, hurt by lower sales (-0.6% QoQ) and higher feedstock costs (+11.5% QoQ), led by an increase in propane and outsourced propylene prices. Profits narrowed despite a higher share of profits from its Korean associate SK Advanced Co. both annually and quarterly (+7.0% YoY and +7.8% QoQ). Net profit missed consensus estimates by 7.2%.

We are, however, positive on the stock's outlook, given healthy demand for PP, which is set to increase 25% from current levels, by 2022, driven by economic growth in China and India. We also expect PP prices to recover from their downtrend, affected by Turkey's economic condition, trade war between the US and China, and the subsequent depreciation of Chinese yuan. Moreover, SK Advanced Co. (owned 30% by Advanced) is well positioned to capture increasing demand for Propylene, via its collaboration with PolyMirae. A healthy balance sheet, strong cash flows, low debt/equity, and high dividend yield make the company a good investment bet. As such, we maintain our "Oveweight" rating on the stock.

- Advanced's top line increased 20.9% YoY to SAR 745mn in 3Q18, driven by increase in product prices and volumes sold. PP-Asia prices surged 12.5% annually to USD 1,260 per tonne in 3Q18. However, sales slightly declined 0.6% QoQ due to muted growth in PP-Asia prices (-0.4% QoQ), hurt by geopolitical issues.
- Gross profit fell 1.7% YoY and 21.3% QoQ to SAR 218mn, amid surge in propane and outsourced propylene prices, which contracted PP-propane spreads. Propane and propylene prices rose on the back of higher oil prices. Consequently, gross margin contracted 673bps YoY and 769bps QoQ to 29.3% in 3Q18.
- Operating profit fell 2.5% YoY and 22.7% QoQ to SAR 191mn, primarily due to a decline in sales and higher feedstock costs. As a result, the operating margin fell 611bps YoY and 732bps QoQ to 25.6% during the quarter.
- Net profit for the quarter came in at SAR 202mn (-3.0% YoY; -20.2% QoQ), as a result of decline in sales revenue and rise in feedstock costs. An 11.2% YoY and 11.8% QoQ increase in finance expenses more than offset a rise in share of profit from associates (SK Advanced Co.), which stood at SAR 25.4mn in 3Q18 as compared with SAR 23.8mn in 3Q17 and SAR 23.6mn in 2Q18.
- During the quarter, the company announced a cash dividend of SAR 0.7 per share, amounting to SAR 137.8 mn.
- Given the recent decline in PP prices, the company plans to explore opportunities in African and South American markets, as the company believes they are likely to offer better prices vis-à-vis Advanced's current consumer markets Turkey and China. This is likely to improve margins for the company going forward.

Valuation: We revised our target price downwards, with a fair value of SAR56.5 per share, in the light of dismal 3Q18 results. However, we have maintained our 'Overweight' rating on the stock, considering expectations of improved earnings going forward.

	3Q'18	3Q'17	% YoY	FY18E	FY17	% YoY
Revenues (SAR mn)	745	616	20.9%	2,718	2,385	14.0%
Gross Profit (SAR mn)	218	222	-1.7%	829	738	12.3%
EBITDA (SAR mn)	137	147	-7.0%	902	812	11.2%
Net Profit (SAR mn)	202	208	-3.0%	730	631	15.7%
EPS basic (SAR)	1.0	1.1	-3.0%	3.7	3.2	15.7%
Gross Margin (%)	29.3%	36.0%	-6.7%	30.5%	31.0%	-0.5%
EBITDA Margin (%)	18.4%	23.9%	-5.5%	33.2%	34.0%	-0.8%
Net Profit Margin (%)	27.1%	33.8%	-6.7%	26.9%	26.5%	0.4%

Source: Company Financials, FALCOM Research

FALCOM Rating Methodology

FALCOM Financial Services uses its own evaluation structure, and its recommendations are based on quantitative and qualitative data collected by the analysts. Moreover, the evaluation system places covered shares under one of the next recommendation areas based on the closing price of the market, the fair value that we set and the possibility of ascent/descent.

Overweight: The Target share price exceeds the current share price by ≥ 10%.

Neutral: The Target share price is either more or less than the current share price by 10%.

Underweight: The Target share price is less than the current share price by ≥ 10%.

To be Revised: No target price had been set for one or more of the following reasons: (1) waiting for more analysis, (2) waiting for detailed financials, (3) waiting for more data to be updated, (4) major change in company`s performance, (5) change in market conditions or (6) any other reason from FALCOM Financial Services.

FALCOM Financial Services

Contact us on the below phone numbers:
Customer Services: 8004298888
Brokerage Services: 920004711

Fax or Email us at the below number:
Fax: +966 11 2032546
Email: addingvalue@falcom.com.sa

Mail us at the following address:
P.O. Box 884
Riyadh 11421
Kingdom of Saudi Arabia

Disclaimer and Risks Warning:

The information in this report was compiled from various public sources believed to be reliable and whilst all reasonable care has been taken to ensure that the facts stated in this report are accurate and that the forecasts, opinions, future prices and expectations contained herein are fair and reasonable, FALCOM makes no representations or warranties whatsoever as to the accuracy of the data and information provided and, in particular, FALCOM does not represent that the information or expected future prices in this report is complete or free from any error. This report is not, and is not to be construed as, an offer to sell or solicitation of an offer to buy any financial securities. Accordingly, no reliance should be placed on the accuracy, fairness or completeness of the information or the expected prices contained in this report. FALCOM accepts no liability whatsoever for any loss arising from any use of this report or its contents, and FALCOM shall not be in any way responsible for the contents hereof. Opinions, forecasts or price projections contained in this report represent FALCOM's current opinions or judgment as at the date of this report only and are therefore subject to change without notice. There can be no assurance that future results, prices or events will match any such opinions, forecasts or prices projections which represent only one possible outcome and these price estimates may not occur in the future whatsoever. Further, such opinions, forecasts or price projections are subject to certain risks, uncertainties and assumptions that have not been verified and future actual results or events could differ materially. Any value or price, or income from, any investments referred to in this report may fluctuate and/or be affected by changes. Past performance is not necessarily an indicative of future performance. Accordingly, investors may receive back less than originally invested amount. This report provides information of a general nature and does not address the circumstances, objectives, and risk tolerance of any particular investor. Therefore, the person who obtain a copy of this report should understand that this report is not intended to provide personal investment advice and does not take into account his/her financial situation or any specific investment objectives or particular needs which he/she may have. Before making an investment decision the investors should seek advice from an independent financial, investment and/or other required advisers due to the investment in such kind of securities may not be suitable for all recipients. This research report might not be reproduced, nor distributed in whole or in part, and all information, opinions, forecasts and price estimates contained; are protected by the intellectual property laws, copyright and publishing rules and regulations applied in the Kingdom of Saudi Arabia.

FALCOM acquired the Saudi Capital Market Authority license number (37-06020) on 27/05/2006, and commenced providing its services to the investors in the Saudi Stock Exchange on 19/02/2007 with CR Number 1010226584 Issued on 04/12/1427H.