SABIC Agri-Nutrients Co.

Petrochemicals – Industrial
SAFCO AB: Saudi Arabia
15 September 2021

US$17.010bn	40%	US$9.611mn
Market cap	Free float	Avg. daily volume

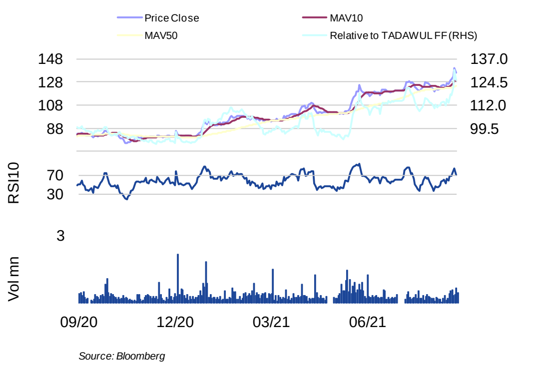
Target price	160.00	+19.4% over current
Current price	134.00	**as at 14/9/2021**

Existing rating

Underweight	Neutral	Overweight

Research Department
Pritish K. Devassy, CFA
Tel +966 11 836 5464, devassyp@alrajhi-capital.com

Performance



Source: Bloomberg

Earnings

(SARmn)	2020	2021e	2022e
Revenue	3,328	8,107	8,828
y-o-y	*1.2%*	*143.6%*	*8.9%*
Gross Profit	1,665	4,679	5,310
Gross margin	*50.0%*	*57.7%*	*60.2%*
Net income	1,294	3,341	3,834
y-o-y	*-12.1%*	*158.1%*	*14.8%*
Net margin	*38.9%*	*41.2%*	*43.4%*
EPS (SAR)	3.1	7.0	8.1
DPS (SAR)	2.0	3.0	5.0
Payout ratio	*64%*	*43%*	*62%*
P/E (Curr)	43.1x	19.1x	16.6x
P/E (Target)	51.5x	22.8x	19.9x

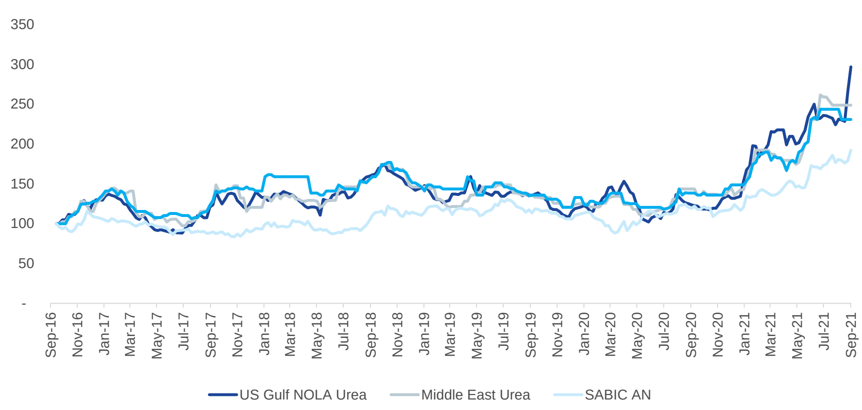
Source: Company data, Al Rajhi Capital

SABIC Agri-Nutrients Co.

Urea momentum likely to continue; Raise TP to SAR160/sh.

Urea prices have moved up significantly this month, reaching multi-year highs. In our view, there are multiple drivers at play which are likely to sustain in the medium term, pertaining to supply, demand and cost push factors. Supply constraints are due to tight supply amid disruptions to US Gulf Coast due to Hurricane Ida while China is focussing lesser on exports for boosting domestic supply. In terms of demand, India is likely to announce a new tender in the coming weeks, pushing Urea prices higher while the pandemic has resulted in structurally higher food demand, as reflected in rising global food prices (+40% over the past 15 months; source: Food and Agriculture Organization). As for the cost push factor, gas prices and coal prices are rising sharply, driving cost and in turn Urea pricing. We have witnessed a ~30% rise in Urea prices (US Gulf NOLA Urea) in Sept so far, but the company's share price is up only by 10%. Given the bullish market outlook, we revise our Urea price assumptions and thereby revise our forward-looking estimates. Overall, we expect the company to post strong earnings in 2021 (mainly in H2 2021), despite a couple of planned shutdowns. This would result in higher cash flow generation, implying a possibility of higher dividend pay-out. Post revision in our Urea price assumptions and better-than-expected efficiencies improvement in Q2, we raise our TP to SAR160/sh. (SAR115/sh. earlier) and rating to Overweight (earlier Neutral) on the stock.

Figure 1 Urea prices vs SABIC AN share price



Source: Bloomberg, Al Rajhi Capital

Planned shutdowns in H2 2021: SABIC Agri-Nutrients Co., in its 2020 Annual Board report, announced a couple of planned maintenance shutdowns in H2 2021, which are as follows.

- 36 days shutdown at the Ammonia and Urea plants (SAFCO 4) in H2 2021
- 32 days shutdown at the Urea plant (SAFCO 5) in H2 2021
- 23 days shutdown at the 2-Ethylhexanol plant (Al Bayroni) in H2 2021 (we have assumed in Q3 2021)

Nonetheless, the impact from these shutdowns would be more than offset by higher Urea prices, increased cost efficiencies, and better inventory management.

Q2 results round-up. Q2 top-line reported at SAR1,839mn, below our estimate of SAR2,054mn (consensus: SAR1,920mn), mainly due to lower-than-expected sales volume. However, better-than-expected improvement in cost efficiencies offset the top-line miss, resulting in largely in-line gross and operating profits. This, along with lower-than-expected zakat and income tax provisions, pushed the net profit above our estimate (SAR836mn vs. SAR760mn expected vs. SAR769mn consensus estimates).

Figure 2 SAFCO Q2 2021 results

(SAR mn)	Q2 2021	Q2 2020	Y-o-Y	Q1 2021	Q-o-Q	ARC est	vs ARC
Revenue	**1,839**	**929**	**98.0%**	**1,506**	**22.1%**	**2,054**	**-10.5%**
Gross profit	1,123	454	147.2%	645	74.2%	1,088	3.2%
Gross margin	61.1%	48.9%		42.8%		52.9%	
Operating profit	951	360	164.3%	502	89.6%	923	3.0%
Operating margin	51.7%	38.8%		33.3%		44.9%	
Net profit	**836**	**360**	132.4%	**423**	97.9%	**760**	10.0%
Net margin	45.5%	38.7%		28.1%		37.0%	

Source: Company data, Al Rajhi Capital

Valuation and risks: We expect top-line and bottom-line to improve in 2021/22, backed by healthy Urea prices, increased sales volume (post SANIC acquisition), and cost control initiatives. Margins are likely to improve in 2021, aided by increased Urea prices and benefits of high operating leverage, offsetting higher costs associated with the SANIC plants. Post sharp increase in Urea prices so far this year, we revise our Urea price forecast to US$435/t for 2021E (earlier: US$400/t), leading to revision to our forward-looking estimates. Consequently, our revised TP stands at SAR160/share (SAR115/sh. earlier) based on equal mix of relative and DCF valuation.

Key upside risks to our estimates include major shutdowns of Urea plants globally, delay suspension of construction of newer Urea plants worldwide, sharp pick-up in demand, higher than expected rise in Urea prices, and increase in dividends above our expectations. Downside risks to our estimates may arise from a steep decline in Urea price and acquisition of associates/subsidiaries at expensive valuations.

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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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Contact us

Mazen AlSudairi
Head of Research
Tel : +966 11 836 5468
Email: alsudairim@alrajhi-capital.com

Al Rajhi Capital
Research Department
Head Office, King Fahad Road
P.O. Box 5561, Riyadh 11432
Kingdom of Saudi Arabia
Email: research@alrajhi-capital.com

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