

SAFCO posted lower than expected results in Q3-19 with net income of SAR 414.2mn; indicating a fall of 20.7%Y/Y. The result was mainly impacted by lower volumetric sales, weak contribution from Ibn-AlBaytar, despite a zakat reversal provision of SAR 40mn. The contribution from Ibn-AlBaytar is expected to decline to SAR 19mn from SAR 34.2mn in Q2-19, against our estimate of SAR 35.0mn. Y/Y Lower Urea prices led gross margin to contract by 682 bps to 51.13% from 57.95% in Q3-18. The company's operating rate is likely to increase in Q4-19; driven by higher ammonia capacity after reliability enhancement project during H1-19. **"Neutral"** recommendation on the stock with TP at **73.50/share**.

- SAFCO posted net income of SAR 414.2mn in Q3-19 (EPS; SAR 0.99); indicating a fall of 20.7%Y/Y and an increase of 8.9%Q/Q. Net profit came below AJC and the market consensus estimates of SAR 443mn and SAR 420mn. We believe that the weak Y/Y result is mainly attributed to i) lower volumetric sales after the scheduled maintenance of SAFCO 3 during previous quarter ii) increase in COGS iii) lower contribution from Ibn-AlBaytar, despite a zakat reversal provision of SAR 40mn. The contribution from Ibn-AlBaytar is expected to decline to SAR 19mn from SAR 34.2mn in Q2-19, against our estimate of SAR 35.0mn.
- The company reported a 9.8%Y/Y decline in revenue for Q3-19 to SAR 909.7mn, which is in-line with our estimate of 907.6mn. We believe the Y/Y sales decline is ascribed to lower operating rate and sold quantities after SAFCO-3 turnaround during 1H-19. Based on our estimates, we assume that the plant was running at lower operating rate of 90.5%, as compared to the average of 94.2% in 3Q-18. For Q3-19, Urea prices declined to an average price of USD 269/tonne from USD 288/tonne in Q3-18, indicating a fall of 6.8%Y/Y.
- Gross profit stood at SAR 465.1mn; indicating an increase of 20.4%Y/Y, below our estimates of SAR 501mn due to higher than expected COGS after the completion of plant maintenance. Gross margin declined to 51.13% in Q3-19 from 51.60% in Q2-19; against our estimate of 54.6%.
- Operating profit stood at SAR 363.7mn, after recording an increase in OPEX (SG & A) at SAR 101.4mn as compared to our estimates of SAR 94.3mn and SAR 95mn in Q2-19.

Ajc view: We believe, the stabilized operating rate and Urea prices, in Q3-19, was offset by lower contribution from Ibn-AlBaytar and weak other income. Urea prices have flattened during Q3-19 to reach USD 268/tonne from an average price of USD 270/tonne in Q2-19, as urea market finds support from Indian demand; however, Indian demand will again be scrutinized in November when fresh tender is announced. On the other hand, operating efficiency and operating rate are the key catalyst for the company beyond H1-19, where operating rate is likely to stabilize above 95% in FY20. The ammonia reliability enhancement project in Q2-19 aims to improve energy utilization, and boost annual production capacity by 100KT. Moreover, we expect that the weak contribution from Ibn Al-Baytar could be ascribed to one-off impact, and is expected to offer an opportunity for growth in FY19/20. Based on our FY19 earnings forecasts, the company is trading at forward PE of 19.9x against global peer average PE of 15.5x. We reiterated our **"Neutral"** recommendation on SAFCO with TP at **SAR 73.50/share**.

Results Summary

SARmn (unless specified)	Q3-18	Q2-19	Q3-19	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
Revenue	1,008.7	813.6	909.7	-9.8%	11.8%	0.2%
Gross Profit	584.5	419.7	465.1	-20.4%	10.8%	-7.9%
<i>Gross Margin</i>	<i>57.95%</i>	<i>51.59%</i>	<i>51.13%</i>	-	-	-
EBIT	481.2	324.9	363.7	-24.4%	11.9%	-11.5%
Net Profit	522.2	380.4	414.2	-20.7%	8.9%	-6.5%
EPS	1.25	0.91	0.99	-	-	-

Source: Company Reports, AlJazira Capital

Neutral

Target Price (SAR) **73.50**

Upside / (Downside)* **-7.7%**

Source: Tadawul *prices as of 22nd of October 2019

Key Financials

SARmn (unless specified)	FY17	FY18	FY19E	FY20E
Revenue	2,759	3,859.8	3,337	3,671
Growth %	-3.4%	39.9%	-13.5%	10.0%
Net Income	879	1,783.4	1,518	1,657
Growth %	-15.2%	97.8%	-13.6%	9.2%
EPS	2.11	4.17	3.64	3.98

Source: Company reports, AlJazira Capital

Key Ratios

SARmn (unless specified)	FY17	FY18	FY19E	FY20E
Gross Margin	43.0%	55.3%	52.3%	51.8%
Net Margin	31.8%	45.0%	45.5%	45.1%
P/E	28.26x	20.21x	21.77x	19.94x
P/B	3.62x	4.80x	3.93	3.70
EV/EBITDA (x)	19.03x	15.71x	17.02	13.86
Dividend Yield	2.9%	2.9%	3.4%	3.8%

Source: Company reports, AlJazira Capital

Key Market Data

Market Cap (bn)	33.0
YTD %	5.3%
52 Week (High)/(Low)	92.40/73.00
Shares Outstanding (mn)	416.67

Source: Company reports, AlJazira Capital

Price Performance



Source: Tadawul, AlJazira Capital

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- Overweight:** This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
- Underweight:** This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
- Neutral:** The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
- Suspension of rating or rating on hold (SR/RH):** This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

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