الراجحي المالية
Al Rajhi Capital

US$6.62bn	40%	US$1.878mn
Market cap	Free float	Avg. daily volume

Target price	59.00	0.16% over current
Current price	58.90	as at 24/10/2017

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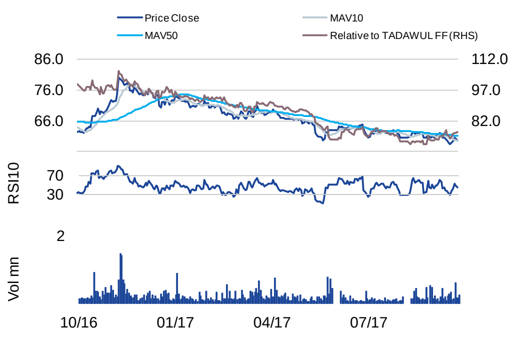
Existing rating

Underweight	Neutral	Overweight

Performance



Source: Bloomberg

Earnings

(SARmn)	2016	2017e	2018e
Revenue	2855.9	2915.1	3555.2
y-o-y	*-19.5%*	*2.1%*	*22.0%*
Gross Profit	1346.5	1401.2	1837.7
margin	*47.1%*	*48.1%*	*51.7%*
Net income	1034.4	1100.1	1459.3
y-o-y	*-51.4%*	*6.3%*	*32.7%*
net margin	*36.2%*	*37.7%*	*41.0%*
(SAR)			
EPS	2.5	2.6	3.5
DPS	2.5	1.9	3.2
Payout ratio	*101%*	*70%*	*90%*
P/E (Curr)		22.6x	17.0x
P/E (Target)		22.3x	16.8x

Source: Company data, Al Rajhi Capital

SAFCO

Q3 above expectations. We remain Neutral as Urea remains oversupplied

SAFCO reported Q3 earnings at SAR188mn, up by 1.2% y-o-y , primarily supported by higher contribution from Ibn Al-Baytar and improved Urea prices, beating our estimate of SAR157mn (consensus: SAR195mn). Despite improved production efficiencies and increase in Urea price, top-line declined, possibly due to shutdown of SAFCO IV and V plants. As the company's 2016 board report stated that the company would close down its IV (84 days) and V (25 days) plants during 2H 2017 for maintenance, we believe the company could have initiated a shutdown towards the end of Q3. Hence, we expect SAFCO IV plant to remain partially closed in Q4, resulting into lower sales volume in Q4. The impact could be completely offset by the sharp increase in average Urea prices in October (~30% higher since Q3), resulting into almost flattish earnings growth. Despite rising urea price, we remain cautious on the stock due to an oversupplied Urea market, which could pull Urea price back to its 3Y average price of ~SAR230-250/t in near to medium term. Nevertheless, we expect DPS to improve to SAR1.1/sh for 2H, resulting into SAR1.9/share DPS for 2017 and SAR3.2/share for 2018 (yield: 5.3%). Since our last report on SAFCO, the share price has declined ~6% and has already reached our target price of SAR59/share. The stock is currently trading at a P/E of 17x based on our 2018E EPS, above global fertilizer peers' multiple of 15.1x. We reaffirm our TP of SAR59/sh and maintain a Neutral rating.

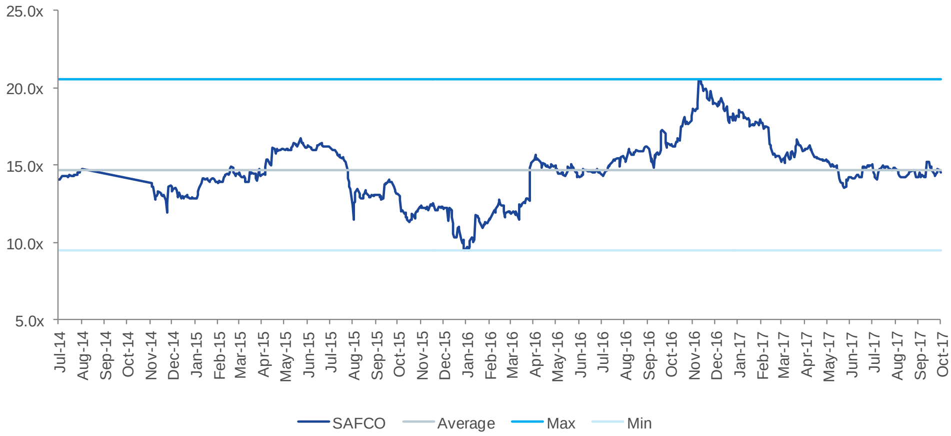
Figure 1 SAFCO Q3 results

(SAR mn)	Q3 2016	Q2 2017	Q3 2017	Y-o-Y	Q-o-Q	ARC est	Comments
Revenue	**690**	**679**	**617**	**-10.5%**	**-9.2%**	**587**	**A decline in top-line due to lower sales volume**
Gross profit	293	289	269	-8.5%	-7.0%	229	Likely Improvement in cost of production per tonne or lower depreciation expenses during the Q3
Gross margin	42.6%	42.5%	43.5%			38.9%	
Operating profit	203	187	175	-13.6%	-6.6%	141	Higher G&A expenses impacted the operating margin slightly during the Q3.
Operating margin	29%	28%	28%			24%	
Net profit	**186**	**204**	**188**	**1.2%**	**-7.8%**	**157**	**Higher contribution from Ibn Al-Baytar pushed net profit higher on a y-o-y basis in Q3.**
Net margin	27%	30%	31%			27%	

Source: Company data, Al Rajhi Capital

Valuation: Despite a good set of Q3 numbers and recent improvement in Urea prices, we keep our TP at SAR59/share based on equal mix of DCF and relative valuation (PE of 17x is above historical average as growth is expected to pick up from a low base amid higher urea prices). We believe the rally seen in Urea price may not sustain and expect it to be range bound averaging around SAR240/t. In-line with our recommendation in our last report on SAFCO, the share price has declined ~6%. Given that Urea oversupply concerns still remain, we advise investors to wait to take a position in SAFCO. However if the stock goes meaningfully below SAR59/share, a tactical position can be considered. The stock is currently trading at a PE of 17x based on 2018E EPS, higher than its global fertilizers peers, at 15.1x. We use only global fertilizer peers as it is not right to compare with Saudi petchem companies' valuation multiples which remain low.

Figure 2 SAFCO 1Y Forward P/E trend



Source: Bloomberg, Al Rajhi Capital

Risks: Key upside risks to our price may be related to major shutdowns of Urea plants globally, delay or suspension of construction of newer Urea plants worldwide, sharp pick-up in demand which may be because of change in regulations across Asian countries (import tax in China, fertilizer import quota in India etc.) all of which could tilt the supply-demand balance in favour of suppliers. Other upside risks relate to increase in dividends above our expectations, increase in stake of associates/subsidiaries which could help bring in some efficiencies. Downside risks may arise from further decline in Urea price and acquisition of associates/subsidiaries at expensive valuations.

Figure 3 Margins and Valuation Metrics - SAFCO vs. global peers

	Market Cap (US$ 'mn)	TTM OPM (%)	TTM NPM (%)	2017E PE	2018E PE	2017E EV/EBITDA	2018E EV/EBITDA
Saudi Arabia							
SAFCO	6,621	35.5	36.7	22.6x	17.0x	15.9x	13.8x
Middle East & Africa (ex-Saudi Arabia)							
Israel Chemicals	5,340	0.0	-3.4	14.0x	11.6x	8.1x	7.4x
Jordan Phosphate Mines	312	-8.6	-13.9	NA	NA	NA	NA
Abou Kir Fertilizers & Chemical Industries	1,324	26.9	38.1	NA	NA	NA	NA
Arab Potash/The	2,008	8.4	19.6	NA	NA	NA	NA
Europe							
K+S	4,686	5.3	3.2	23.6x	13.7x	10.2x	7.4x
Yara International	12,601	4.2	3.0	23.1x	15.7x	9.8x	7.6x
North America							
CF Industries	8,469	-1.0	-10.0	NA	NA	16.9x	12.3x
Mosaic	7,383	3.7	2.1	29.0x	19.9x	10.5x	8.2x
Potash Corp	16,215	15.0	11.1	31.2x	28.9x	14.2x	12.7x
Agrium	14,894	8.6	4.2	22.0x	18.3x	11.3x	10.0x
Latin America							
Sociedad Quimica y Minera de Chile SA	14,817	25.5	16.3	37.3x	34.4x	17.2x	15.8x
Fertilizantes Heringer SA	47	3.7	-0.4	NA	NA	4.4x	4.0x
Asia							
China XLX Fertilizer	371	7.0	1.9	8.0x	6.5x	7.3x	6.5x
Coromandel International	2,345	8.8	4.8	24.3x	20.5x	15.1x	13.4x
Engro Fertilizers	807	9.9	13.1	9.0x	8.3x	7.0x	6.3x
National Fertilizers	465	6.2	2.7	NA	NA	NA	NA
Phosagro	5,304	24.8	21.5	11.4x	10.2x	6.9x	6.3x
Taiwan Fertilizer Co Ltd	1,276	7.7	4.1	NA	NA	NA	NA
Fauji Fertilizer Bin Qasim Ltd	311	-12.7	1.7	14.2x	11.3x	NA	37.0x
Hubei Yihua Chemical Industry Co Ltd	705	-3.6	-9.0	NA	NA	NA	NA
Acron PJSC	2,526	20.6	16.0	7.7x	8.1x	7.4x	7.1x
Luxi Chemical Group Co Ltd	2,385	10.2	5.2	13.7x	9.9x	8.7x	7.5x
PhosAgro PJSC	5,123	24.8	21.5	11.1x	9.9x	6.7x	6.1x
Dorogobuzh PJSC	725	13.4	29.2	NA	NA	NA	NA
Median		**8.0**	**4.2**	**14.2x**	**11.6x**	**9.2x**	**7.5x**
Average		**8.7**	**7.6**	**18.6x**	**15.1x**	**10.1x**	**10.3x**

Source: Bloomberg, Al Rajhi Capital. Notes: All valuation ratios as of October 24, 2017

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"Overweight": Our target price is more than 10% above the current share price, and we expect the share price to reach the target on a 12 month time horizon.

"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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