

November 09, 2017

Rating  
12- Month Target Price

Neutral  
SAR 20.00

## SAUDI CERAMICS COMPANY (SCC)

3Q2017 First Look

### Negative Surprise

Saudi Ceramics Company (SCC) announced 3Q2017 results with a loss of SAR (39) million, repeating its similar trend a year ago, with its loss of SAR (47) million in 3Q2016. A continued jolt was unexpected; results came below expectations and street's, though management cites this weakness due to seasonality and competitive pricing from cheap tile imports from China, India and Spain. We reiterate such subdued trends coincide with the tough trends in the sector, a close comparable is the weakness in cement industry, reported below par earnings. We further revise our 2017-19 estimates and our target price to SAR 20.00 (earlier SAR 24.00) but maintain Neutral. The stock trades at 2018E P/B of 0.6x, offering some respite for value investors but do not recommend exposure unless more clarity comes-in. The stock is seen under pressure, down -29% versus TASI's -4% on a YTD basis. 2018E P/E of 52.1x is expensive than TASI's 13.9x and to peers in GCC; Anwar Ceramics at 14.7x. Maintain Neutral.

### Revenue below estimate

Revenue of SAR 224 million in 3Q2017 came lower to our expectations of SAR 254 million, declined -3% Y/Y and -19% Q/Q. The continued competition from China, India and European based producers has affected selling prices largely for SCC. Tile importers control around 50-60% of the tiles market in KSA, while SCC has share of 18-20%. The low demand for tiles in other GCC-ex KSA markets has also resulted in higher exports from neighboring markets; RAK Ceramics in UAE, Anwar Ceramics in Oman are some of the beneficiaries due to its higher exports to KSA.

### Heavy fixed costs haunt margins

SCC reported a gross profit decline of -54% Y/Y and -62% Q/Q to SAR 25 million in 3Q, lower versus our estimate of SAR 64 million. The dual impact of higher fixed costs and falling selling prices continues to haunt SCC's margins. Gross margins fell to 11% from 24% in the last quarter and 24% in 3Q2016, signifies the added pressure of fixed costs, also suggest large fall in utilization. COGS fell by -5% Q/Q versus a -19% fall in revenue, with COGS to Sales of 89% in 3Q is the highest ever, led to sharp drop in gross margins.

### Fourth net loss since 3Q2016

SCC reported an operational loss of SAR (27) million reported a negative surprise to our profit estimate of SAR 6 million. The continued rise in selling costs (SG&A as % of sales at 23%) and lower volumes sales amid low margins on a gross level, overall resulted in a loss on a operating level. Without any one-off impact unlike its SAR 25 million impairment charges in 3Q2016, SCC reported its fourth loss in a span of five quarters. SCC's loss of SAR (39) million in 3Q2017 was a negative surprise to our SAR (4) million loss estimate and street's SAR 1 million.

### Cutting Target price to SAR 20; but maintain Neutral

We cut target price to SAR 20.00 from earlier SAR 24.00 as we expect trough earnings trends amid sharp topline decline. The announcements in the housing markets are expected to face slight execution delays; amid tough competition playing out in a crowded tiles market. We maintain Neutral for now.

### Key Financial Figures

FY Dec31 (SAR mln)	2016A	2017E	2018E
Revenue	1,304	1,061	1,064
EBITDA*	265	108	112
Net Profit	25	(52)	22
EPS (SAR)	0.50	(1.04)	0.44
DPS (SAR)	0.50	0.00	0.00
BVPS (SAR)	36.45	35.41	35.85

### Key Financial Ratios

FY Dec31	2016A	2017E	2018E
ROAA	1%	-1%	1%
ROAE	1%	-3%	1%
P/E	45.9x	NM	52.1x
P/B	0.6x	0.6x	0.6x
EV/EBITDA	7.1x	17.5x	16.9x
EV/Sales	1.5x	1.8x	1.8x

### Expected Total Return

Price as on Nov-08, 2017	SAR 22.94
Upside to Target Price	(12.8%)
Expected Dividend Yield	0.0%
Expected Total Return	(12.8%)

### Market Data

52 Week H/L	SAR 35.7/20.7
Market Capitalization	SAR 1,147 mln
Enterprise Value	SAR 1,894 mln
Shares Outstanding	50.0 mln
Free Float	83.8%
12-Month ADTV (000's)	169.7
Bloomberg Code	SCERCO AB

### 1-Year Price Performance



Fig in SAR mln	RC. Est	Actuals
Revenue	254	224
Gross Profit	64	25
EBIT	6	(27)
Net Income	(4)	(39)
EPS (SAR)	(0.08)	(0.78)

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## Stock Rating

Buy	Neutral	Sell	Not Rated
Expected Total Return Greater than 15%	Expected Total Return between -15% and +15%	Expected Total Return less than -15%	Under Review/ Restricted

\* The expected percentage returns are indicative, stock recommendations also incorporate relevant qualitative factors

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