Saudi Aramco

Oil & Gas
Aramco AB: Saudi Arabia
23 March 2023

US$1.886trn	5.81%	US$140.80mn
Market Cap	Free Float	Avg. Daily Volume

Target price	38.00	+18% above current
Current price	32.15	as at 23/03/2023

Existing rating

Underweight | Neutral | **Overweight**

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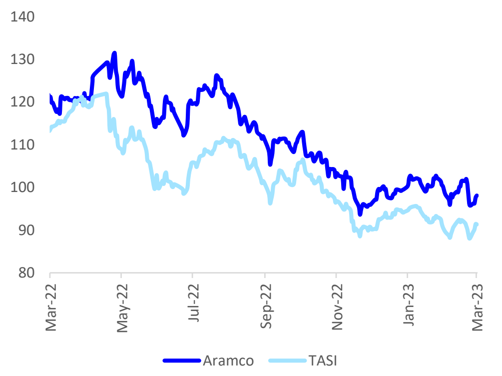
Performance



Earnings

(SARbn)	2022	2023E	2024E
Revenue	2,007	1,713	1,779
Y-o-Y	49.0%	-14.6%	3.8%
Operating profit	1,144	1,009	1,059
Operating margin	57.0%	58.9%	59.5%
Net profit	597	523	546
Y-o-Y	51.1%	-12.5%	4.5%
Net margin	29.8%	30.5%	30.7%
EPS (SAR)	2.71	2.38	2.48
DPS (SAR)	1.29	1.33	1.33
Payout ratio	47.5%	56.0%	53.6%
Dividend yield	4.0%	4.1%	4.1%
P/E (Curr)	11.8x	13.5x	13.0x
P/E (Target)	14.0x	16.0x	15.3x

Source: Company data, Al Rajhi Capital.

Saudi Aramco

TP revise to SAR38/sh. on near-term headwinds

Aramco's Q4 earnings came in below our expectation, primarily due to lower hydrocarbon production (-6.0% q-o-q). Despite the Q4 earnings miss, the company has declared a dividend of SAR0.3326/sh. for Q4 2022, ~4% higher than the dividend declared for Q3 2022, and above our estimate of SAR0.3198/sh., which could be attributable to strong FCF of US$38.3bn. Further, the company's financial position has improved significantly in 2022 with the gearing ratio improving to -7.9% as of Dec 222 from 12% in 2021.

After rising ~42% y-o-y in 2022, crude oil prices may come under pressure in 2023, mainly due to tight liquidity (declining open interest) in the paper market, mainly due to higher inflation levels and the recent banking crisis. However, we expect the oil market fundamentals to remain healthy, driven by higher demand growth (OPEC: +2.3mmb/d in 2023e; EIA: +1.5mmbd) and limited supply amid active OPEC's role in balancing the oil market. This, along with the lack of substantial investments amid depleting production run rates, may keep oil prices mostly firm over the medium term. While we expect Aramco to witness earnings pressure in 2023, mainly due to lower oil prices, we remain positive on the company, mainly due to i) its plan to increase its MSC to 13mmb/d by 2027, with the first increments expected to come on stream in 2024, ii) 50% anticipated rise in gas production by 2030, iii) a strong FCF generation abilities with robust financial positions. Further, the recent increase in quarterly dividend is commendable as the company also plans to increase its capex by ~33% (at mid-point) to US$45-50bn (including external investments) in 2023e, confirming our positive oil market outlook going forward. Furthermore, the company's recent announcement of 1 bonus share for every 10 shares demonstrates its confidence in its future growth prospects. Post updating our recent commodity price deck, we revise our estimates downwards, resulting in a revision in our TP to SAR38.0/sh. (SAR42/sh. earlier). The stock currently offers a healthy dividend yield of 4.1%, which will continue to provide support to the share price.

Figure 1 Aramco's Q4 2022 results

(SAR bn)	Q4 2022	Q3 2022	Q4 2021	Q4 2020	ARC Est.	Cons Est.	q-o-q	y-o-y	% ch vs 2020	vs ARC	vs Cons
Revenue	**434.2**	**543.7**	**403.4**	**219.3**	**479.6**	**504.8**	***-20.1%***	***7.6%***	***98.0%***	***-9.5%***	***-14.0%***
Op. costs	(192.5)	(243.5)	(175.3)	(114.8)	(197.3)	NA	*-20.9%*	*9.8%*	*67.8%*	*-2.4%*	*NM*
Op. profit	**241.7**	**300.2**	**228.1**	**104.5**	**282.3**	**NA**	***-19.5%***	***5.9%***	***131.3%***	***-14.4%***	***NM***
Op. margin	*55.7%*	*55.2%*	*56.5%*	*47.7%*	*58.9%*	*NA*					
Net profit*	**115.2**	**159.1**	**121.4**	**52.5**	**149.0**	**139.1**	***-27.6%***	***-5.1%***	***119.7%***	***-22.7%***	***-17.2%***
Net margin	*26.5%*	*29.3%*	*30.1%*	*23.9%*	*31.1%*	*27.6%*					

Source: Company data, Al Rajhi Capital. * Before minority

Q4 results. Top-line decreased ~20% q-o-q to ~SAR434bn, lower than our (SAR480bn) and consensus (SAR505bn) estimates, mainly due to weaker-than-expected hydrocarbon production. Based on our calculation, the total hydrocarbon production might have declined by 7% q-o-q to ~13.5mmboe/d in Q4 2022, below our estimate of 14.2mmboe/d (14.4mmboe/d in Q3 2022), leading to a top-line miss. Further, operating profit missed our estimate, primarily weighted down by lower-than-expected revenues. Accordingly, net income (before minority) was reported at ~SAR115bn, below our estimate of SAR149bn (consensus: SAR139bn).

Valuation. For 2023, we expect the company to increase DPS marginally to SAR1.33 from SAR1.29/sh. in 2022, although it can potentially increase it even further, given its strong FCF and financial positions. This is because we believe the company is driven by longer-term goals and is likely to exhibit resilience and stability. To capture this potential growth, we use the DCF valuation method (9.1% cost of equity; 8% WACC), implying a TP of SAR38.0/sh. (SAR42/sh. earlier), and an Overweight rating on the stock.

Risks. The key downside risk to our valuation is a surge in interest rates which looks unlikely at this point. Other downside risk factors to our estimates are lower-than-expected dividends, geo-political tensions, delay in recovery in oil prices, and further slowdown in the global economy.

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