Saudi Cement Sector - Monthly

Cement –Industrial
Saudi Arabia
13 Nov 2017

الراجحي المالية
Al Rajhi Capital

Research Department
Mohammed AlThunayyan
Tel +966 1 211 9395, althunayyanm@alrajhi-capital.com

Key themes

This is our monthly update on Cement production, volumes and inventory in Saudi Arabia.

What do we think?

Stock	Rating	Price Target
Yamama	N	SAR 17.0
Southern	N	SAR 43.0
Saudi	N	SAR 42.0
Yanbu	N	SAR 28.0
Qassim	N	SAR 42.0
Arabian	N	SAR 36.0

Saudi Cement sector:
No signs of improvement

What to expect in 2018?

- Demand is unlikely to pick up steeply given that construction activities are bound to remain weak, thus we expect sales volume to remain modest in 2018 at a level of 43-45mn tons (down 6-8% compared to 2017) due to limited expansion plans in the private sector as well as priority of projects to the government.
- For supply, we believe that under the current weak market conditions, cutting production would be one of the realistic options through closing old production lines which could have higher cost (lower efficiency).
- Due to current weak market conditions, we expect the government to cancel the export fees in the coming few months. Iraq and Yemen are considered as key markets for exports, however, transportation costs, sluggish demand and political instability in the neighboring regions, excess supply and competitive pricing in the region are the main challenges to export.
- We expect more mergers in the sector as it will reduce competition which could result in stable selling prices. Also, this will increase the bargaining power over distributers as well as some cost savings especially if they operate in the same region.
- Dividend payments will be impacted as the industry hasn't shown any signs of recovery, however, we expect a slight drop compared to 2017 dividends. Limited expansion plans and low leverage will lead companies to raise payout ratios.
- However, on the valuation front, we believe that most of the negative factors are priced in. Hence we are Neutral on the sector and believe the, downside risks from current prices are limited.
- Taking into consideration production capacities and number of producers, we believe that Western, Southern and Northern regions are facing the most challenging conditions.
- PIF's initiatives in the Western region (NEOM, Red sea, Jeddah downtown, Rou'a Al Haram and Rou'a Al Madinah) could create a key driver for Tabuk cement and Western region producers.
- Total inventories in the sector of 36.2mn tons represent 76% of last 12 month sales volume and around 50% of total production capacity in the sector.

Q3 results

- In Q3 2017, total cement sector revenues declined 31% y-o-y on the back of lower sales volume (-6% y-o-y) and sharp drop in the average realized price/ton for most of the companies. Similarly, aggregate net income came in at SAR 300mn (-65% y-o-y), mainly due to an escalation in cost of goods sold as the sales volume declined. In Q4, we expect selling prices to remain stable at Q3 prices, while sales volume are likely to witness a 6% y-o-y drop and increase 19% q-o-q due to seasonality factors.

- On the pricing side, most of cement producers continue to offer deep discounts especially in the Central and Western regions as smaller players focus on main demand regions. In Western region, selling prices fell to ~SAR130/ton (vs. SAR205 in Q3 2016), while prices in Central region were higher compared to Western region (SAR155 on average) despite the y-o-y drop. Helped by limited competition, Eastern region's prices were the highest in the sector , however, we believe that this advantage is unlikely to sustain due to increasing competition amid current weak market conditions. Going forward, we expect selling prices to remain modest at current levels.

Monthly sales for October at 4.1mn tons:

According to the latest monthly data released by Yamama Cement, total cement dispatches in the Kingdom declined 5% y-o-y and improved 30% m-o-m to 4.1mn tons in October. Total inventory rose 36% y-o-y to a new record of 33.6mn tons, representing 76% of the last 12 months' sales. Clinker production in the Kingdom fell 9% y-o-y to 4.0 mn tons during October. Najran and Yamama cement were the most affected in October dispatches by -37% and -32% y-o-y, respectively. Despite a 50% reduction in export fees (from an earlier range of SAR85-SAR133), Saudi producers did not export cement in August, owing to unfavourable economics. Total inventories rose 28% y-o-y and 1.5% m-o-m, reaching to a record new high at 36.2mn tons, representing 76% of the last 12 months' sales. The record high inventory could be attributable to the lower demand amid slowdown in construction activities in the Kingdom and limited supply cut by Saudi producers.

Figure 1 Sector information in the first 10 months of 2017

Cement Sector	Sales volume (mn tons)			Current Inventories (mn tons)			9M 2017 Results		
	Jan-Oct 2016	Jan-Oct 2017	Y-o-Y Change	Oct-16	Oct-17	Y-o-Y Change	YTD Net profit (SARmn)	Y-o-Y Change	Q3 Sale price (SAR/ton)
Central & Eastern									
Yamama	4.6	3.7	-20.0%	4.3	4.8	11.7%	92.1	-71.5%	176.4
Qassim	3.4	3.2	-7.9%	1.0	1.6	56.4%	184.6	-41.8%	149.6
City cement	2.6	2.8	9.5%	1.3	1.3	1.8%	69.5	-59.2%	152.3
Saudi	5.8	4.1	-29.3%	4.6	5.3	13.5%	346.0	-51.5%	233.3
Eastern	2.0	1.7	-15.4%	2.0	2.6	34.5%	99.4	0.0%	188.2
Riyadh cement	2.9	2.4	-19.1%	1.7	1.3	-20.7%	-	-	-
Western & Southern									
Yanbu	5.0	4.6	-9.0%	3.7	4.0	6.6%	223.0	-47.2%	136.7
Arabian	3.8	3.0	-21.1%	0.7	0.9	21.6%	165.7	-62.1%	126.6
Umm alQura	0.0	1.0	NM	0.0	0.8	NM	30.6	N.A	143.9
United	0.0	1.4	NM	0.0	0.5	NM	-	-	-
Al Safwa	1.5	1.5	-3.3%	0.4	0.9	137.5%	-	-	-
Southern	6.5	4.6	-29.2%	1.4	2.8	101.4%	256.7	-64.6%	170.2
Najran	2.5	1.4	-44.7%	2.9	3.3	12.8%	(10.1)	N.A	196.3
Northern Region									
Northern	1.7	0.9	-42.9%	0.8	1.3	65.5%	37.3	-69.2%	-
Hail	1.2	0.8	-31.4%	1.3	2.4	75.3%	11.6	-85.2%	143.0
Jouf	1.6	1.2	-25.8%	1.2	1.2	-0.5%	32.7	-47.7%	149.3
Tabuk	1.1	0.9	-23.7%	1.0	1.4	41.0%	(2.3)	N.A	141.8
Total	**46.3**	**39.2**	**-15.4%**	**28.2**	**36.2**	**28.3%**	**1,536.8**	**-57.5%**	**162.1**

Source: Yamama cement, Company data, Al Rajhi Capital

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Contact us

Mazen Al-Sudairi
Head of Research
Tel : +966 1 211 9449
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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