



US\$3.109bn Market cap
90% Free float
US\$19.50mn Avg. daily volume

Target price 12.00 -24.5% over current
Current price 15.90 as at 26/10/2020

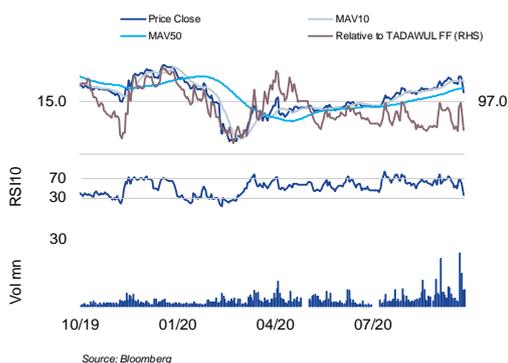
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Existing rating

Underweight **Neutral** **Overweight**

Performance



Earnings

(SARmn)	2019	2020e	2021e
Revenue	5,440	5,133	5,744
Y-o-Y	8.0%	-5.6%	11.9%
Gross profit	1,635	887	1,264
Gross margin	30.1%	17.3%	22.0%
EBITDA	1,797	988	1,406
EBITDA margin	33.0%	19.2%	24.5%
Net profit	300	(120)	212
Net margin	5.5%	-2.3%	3.7%
EPS (SAR)	0.52	(0.16)	0.29
DPS (SAR)	0.60	-	0.30
Payout ratio	116.3%	NM	103.8%
ROE	1.2%	-0.5%	0.8%
EV/EBITDA	4.7x	8.5x	6.0x
P/E	30.8x	NM	55.0x

Source: Company data, Al Rajhi Capital

SIPCHEM
Q3: Earnings miss

Sipchem posted a quarterly net profit in Q3, the first in the last four quarters, aided by improvement in product prices and a recovery in demand post easing lockdowns. However, Q3 earnings missed our as well as street expectations despite a strong beat in the topline. While details are not fully known, we suspect this could have been because of marketing revenues and mostly similar extent of costs as gross profit came broadly in-line with our estimate. Methanol prices are up on a sustainable recovery trend, up by ~11% q-o-q in Q3, on the back of tight supply due to unexpected production outages in Southeast Asia and the Middle East along with improvement in demand, mainly from the MTO and pharmaceutical sectors (source: ICIS). Methanol prices continue to maintain its upward trend in Q4 so far, rising ~14% q-o-q, indicating an improving the Methanol market fundamentals. However, the stock price has already gained ~30% since March, and consensus estimates do not factor material improvement in earnings (Figure 2). While the company's announcement of a share repurchase program may have improved sentiments, it may lead to no dividends for 2020. Accordingly, we maintain our TP at SAR12/sh. and rating for the stock.

Figure 1 SIPCHEM Q3 2020 results

(SAR mn)	Q3 2020	Q3 2019	Y-o-Y	Q2 2020	Q-o-Q	ARC est	vs ARC
Revenue	1,362	1,402	-2.9%	950	43.3%	1,147	18.7%
Gross profit	220	362	-39.1%	150	47.1%	229	-4.0%
Gross margin	16.2%	25.8%		15.8%		20.0%	
Operating profit	18	177	-90.0%	(23)	NM	69	-74.3%
Operating margin	1.3%	12.6%		-2.5%		6.0%	
Net profit	10	111	-91.0%	(99)	NM	16	-35.7%
Net margin	0.7%	7.9%		-10.4%		1.4%	

Source: Company data, Al Rajhi Capital.

Q3 Results. Q3 top-line reported at SAR1,362mn (+43.3% q-o-q), beating our estimate of SAR1,147mn, likely due to a jump in marketing revenues. Overall, Q3 net profit came in at SAR10mn, lower than ours (SAR16mn) as well as consensus (SAR18.1mn) estimates.

Share buyback plan may limit dividend paying ability: On Sep 30, 2020, Sipchem completed the first phase of its share purchase program, buying ~2.5mn shares (excluding 1.05mn shares associated with the employees' incentive program) worth SAR39.02mn at an average price of SAR15.6/share. This just accounts for 3.4% of the approved share buyback plan. The company, earlier in April 2020, announced its plan to buyback the 73.33mn shares (worth ~SAR1bn as per our calculations) by April 2021 using available cash and cash equivalents (SAR3.3bn as of Q2 2020) and credit facilities. While we don't see any funding gap, this could lower the company's dividend-paying abilities due to deteriorated earnings performance over the past few quarters. Accordingly, the company may skip distributing the dividends for 2020. For 2021, we expect the company to distribute SAR0.3/sh, with a possible downside in case Methanol prices do not recover.



Valuation and Risks: While there are near term headwinds in the elevated costs levels and global economic contractions, the medium-term outlook looks positive, given its healthy fundamentals, production & operating efficiencies, and likely cost-synergies (SAR175-225mn impact in recurrent EBITDA post its merger with Sahara), along with healthy FCF generation capabilities and comfortable debt position.

Figure 2 Bloomberg consensus earnings 2021 vs. Sipchem stock price



Source: Bloomberg, Al Rajhi Capital.

We value Sipchem using DCF (based on FCF, cost of equity 12.1%) at SAR12/share, implying an Underweight rating for the stock. Key upside drivers for the stock are better-than-expected product prices, and higher than expected dividends. Major downside risks to earnings involve unexpected disruption at the company’s upstream operations, which can further impact its downstream plants as well and persistent weakness in product prices, particularly Methanol prices.



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"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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