Yanbu National Petrochemicals

Petrochemicals – Industrial

YANSAB AB: Saudi Arabia

23 April 2018

Al Rajhi Capital الراجحي المالية

US$11.07bn	37%	US$6.41mn
Market cap	Free float	Avg. daily volume

Target price	68.00	-7.9% over current
Current price	73.82	as at 19/4/2018

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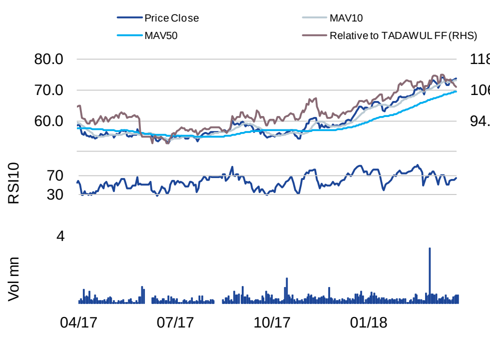
Existing rating

Underweight	Neutral	Overweight

Performance



Source: Bloomberg

Earnings

(SARmn)	2017	2018e	2019e
Revenue	7,221	8,013	7,931
Y-o-Y	15.9%	11.0%	-1.0%
Gross profit	2,870	3,193	3,485
Gross margin	39.7%	39.8%	43.9%
Net profit	2,376	2,665	2,961
Y-o-Y	1.4%	12.2%	11.1%
Net margin	32.9%	33.3%	37.3%
EPS (SAR)	4.2	4.7	5.3
DPS (SAR)	3.3	4.0	5.0
Payout ratio	76.9%	84.4%	95.0%
P/E (Curr)	17.2x	15.3x	13.8x
P/E (Target)	16.1x	14.4x	12.9x

Source: Company data, Al Rajhi Capital

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Q1: Earnings in-line

Yansab reported lower than expected Q1 revenue, probably due to higher than expected impact of shutdowns (not reported by company, source: polymer update) of HDPE and LLDPE plants. We estimated Q1 utilization rate at ~82%, however, results indicated that operating rates could have come even lower at ~75%. Despite lower top-line (-17.5% q-o-q) amid shutdowns, we observed an improvement in production efficiencies, and probably higher by-product sale from excess ethylene resulting in overall net profit (SAR631mn) coming in broadly in-line with our estimate (SAR652mn). This comes in after last two quarters of earnings beat reemphasising the law of averages at work for cyclical petchem companies. Consequently, our forward looking annual estimates which are dependent on average cycle prices and utilization rates remain broadly unchanged as we expect Yansab's performance to improve post shutdown. Hence, we reiterate our TP of SAR68/share with a Neutral rating. We do expect an increase in dividend to SAR4.0/share for 2018E, given its healthy financial position and robust FCF generation.

Additional details: Q1 revenue of SAR1,787mn was below our estimate of SAR1,966mn (consensus: SAR2,113mn), primarily due to weak sales volume amid likely plant shutdowns in February/March (HDPE/LLDPE plants: 6-7 weeks; source: PolymerUpdate), completely offsetting higher prices across its products portfolio. The ~SAR179mn miss in top-line was largely offset by better than expected production efficiencies (most likely at MEG plant) and lower SG&A expenses, leading to SAR46mn and just SAR29mn miss at the gross and operating profit levels. Consequently, net profit came in at SAR631mn, mostly in line with our estimate of SAR652mn (consensus: SAR726mn).

What to expect in the near term? Post shutdown of HDPE/LLDPE plants in Q1, we expect production rates to improve in the coming quarters and hence we reaffirm our positive outlook on the company and maintain our earlier estimates. While product prices are likely to improve gradually in the coming quarters, the company might see a pressure in feedstock prices in the near term, due to rising oil prices, which could keep the margins under-check. Additionally, we believe that dividends are likely to increase from SAR3.25/share in 2017 to SAR4.00/share in 2018E, given its healthy financial position and robust free cash flow generation. Further, the Ethylene Glycol DBN project will increase the company's MEG capacity to 850kta at the end of 2018, which would be the medium term trigger for the stock.

Figure 1 YANSAB Q1 results

(SAR mn)	Q1 2017	Q4 2017	Q1 2018	Y-o-Y	Q-o-Q	ARC est	Comments
Revenue	1,759	2,167	1,787	1.6%	-17.5%	1,966	**Missed our and consensus estimates, largely due to lower than expected utilization rate amid likely multi-weeks shutdown at its HDPE and LLDPE plants.**
Gross profit	728	897	740	1.6%	-17.5%	786	Top-line miss was partially offset by improvement in production efficiencies (most likely at MEG plant), capping the miss at the gross profit level..
Gross margin	41.4%	41.4%	41.4%			39.9%	
Operating profit	623	780	635	1.9%	-18.6%	664	SG&A expenses could have declined more than our expectation.
Operating margin	35.4%	36.0%	35.5%			33.7%	
Net profit	608	778	631	3.7%	-18.9%	652	**Largely in line with our estimate of SAR652mn (consensus: SAR726mn), aided by improved production and operating efficiencies.**
Net margin	34.6%	35.9%	35.3%			33.2%	

Source: Company data, Al Rajhi Capital

Valuation: Despite top-line miss in Q1, which was due to shutdowns, we continue to remain positive on Yansab, given its strong operational capabilities coupled with healthy balance sheet (net cash position) and robust FCF generation amid limited capex requirements (even after incorporating SAR373mn Ethylene Glycol DBN project). Post Q1 results, we do not revise our future estimates materially. At 2018 forward EPS of SAR4.7/share, the 2018 PE multiple comes at 15.3x, higher than its historical average of 14.2x. We maintain our TP of SAR68/share based on an equal mix of DCF and relative valuation (target multiple 13.5x, to adjust for higher payout as per our estimates). FY18E DPS of SAR4.0/share implies a dividend yield of ~5.5%, which is superior to most of its peers.

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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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