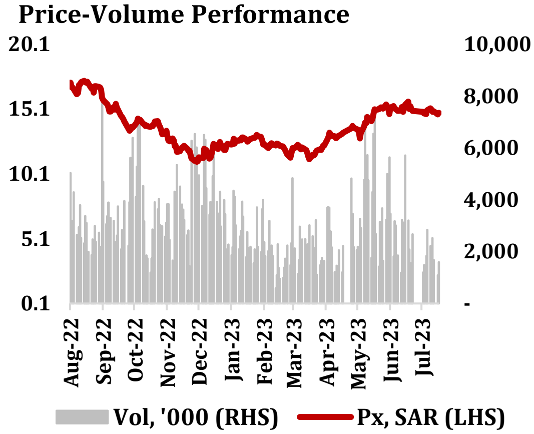
National Industrialization Company SJSC (NIC AB)

Target Price: SAR 16.0/share
Upside: 8.30%

Recommendation	**Hold**
Bloomberg Ticker	NIC AB
Current Market Price (SAR)	14.78
52wk High / Low (SAR)	17.420/10.840
12m Average Vol. (000)	3,043.2
Mkt. Cap. (USD/SAR mn)	2,692/9,887
Shares Outstanding (mn)	668.91
Free Float (%)	83%
3m Avg Daily Turnover (SAR'000)	42,959.4
6m Avg Daily Turnover (SAR'000)	34,023.7
P/E'23e (x)	10.7 x
EV/EBITDA'23e (x)	12.4 x
Dividend Yield '23e (%)	0.0%
Price Performance:	
1 month (%)	-3.9%
3 month (%)	11.6%
12 month (%)	4.1%

Source: Bloomberg, values as of 17 July 2023

Price-Volume Performance



Source: Bloomberg

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- **Likely increase in demand for portfolio products along with improvement in petrochemical prices to drive topline post-2023.**
- **Expected improvement in spreads and margins to support earnings growth from 2024 onwards.**
- **Financial stability and resilience demonstrated by robust cash flows and prudent leverage.**

We review our coverage of National Industrialization Company (NIC AB Equity: Saudi Arabia) and raise our **target price to SAR 16.0** while maintain a **Hold** rating on the stock, considering an upside potential of 8.30% from the current levels. The stock is currently trading at a P/E of 10.07x based on our 2023 estimates, compared to its historical average 1-year forward P/E of 14.91x. The stock is likely to benefit from favorable demand visibility from key end-market applications such as packaging, paints, and cosmetics etc. and expected stabilization of petrochemical products prices after 2023.

Investment Thesis

Tasnee's diversified portfolio, along with the surge in demand for its products contribute to improving profitability and return ratios, making it an attractive investment opportunity. The company's improving financial metrics and anticipated demand growth in both domestic and international markets further strengthen the case for its future success.

- With the anticipated improvement of petrochemical prices and surge in demand for paints and cosmetics in the KSA region, the company is well positioned to register a CAGR of ~4.3% for revenue from FY23-27e.
- Despite the ongoing volatility in the petrochemical market in 2023, Tasnee's diversified portfolio helps to mitigate risk.
- The company consistently generates a significant amount of cash from its operations signifying strong operational efficiency and effective liquidity management.
- Tasnee's minimal reliance on external debt for financing demonstrates sound financial management and a low-risk profile .

Valuation and risks: Our valuation is based on a mix of DCF (80% weight), and multiples approach (10% weight each to P/E and EV/EBITDA based multiples). Key downside risks: Low product prices, market instability and operational risk due to unplanned shutdown.

Key indicators

Year	FY21	FY22	FY23e	FY24e	FY25e
Sales	3,673	3,883	3,920	4,100	4,274
Gross profit	987	864	689	920	1,026
EBITDA	3,449	1,494	1,272	1,520	1,645
Operating profit	3,177	1,262	1,039	1,280	1,394
Net income	2,054	1,086	915	1,107	1,453
EPS	3.76	1.62	1.37	1.65	2.17
P/E	5.31	7.62	10.70	8.85	6.74
EV/EBITDA	5.73	8.95	10.51	8.79	8.13
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%

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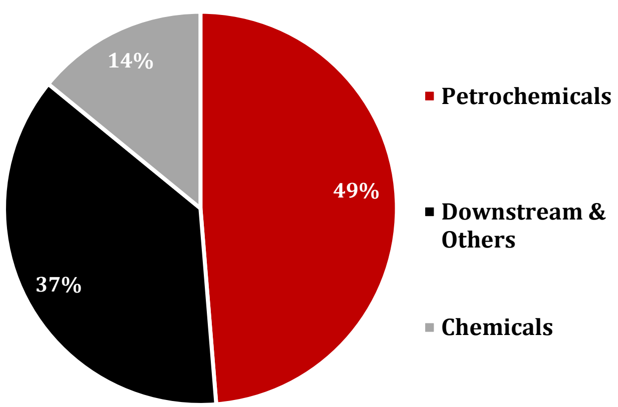
Investment Rationale

Tasnee's Titanium bet: A new frontier for product diversification

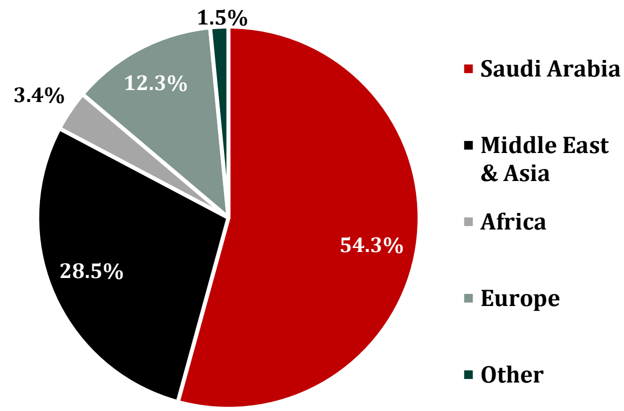
Tasnee is a fully owned joint stock company in Saudi Arabia that aims to advance economic diversification in the country. As one of the largest industrial and petrochemical companies in the KSA, Tasnee is also a major investor in titanium, which has helped to diversify its product portfolio. In addition, Tasnee generates revenue through its downstream business, which primarily focuses on liquid batteries for automobiles. In terms of geographic mix, Saudi Arabia remain the dominant revenue contributor in FY22 followed by the other MENA and Asia region.

Revenue by segment (FY'23E)



Source: Company Reports, U Capital Research

Revenue by geography (FY'22)



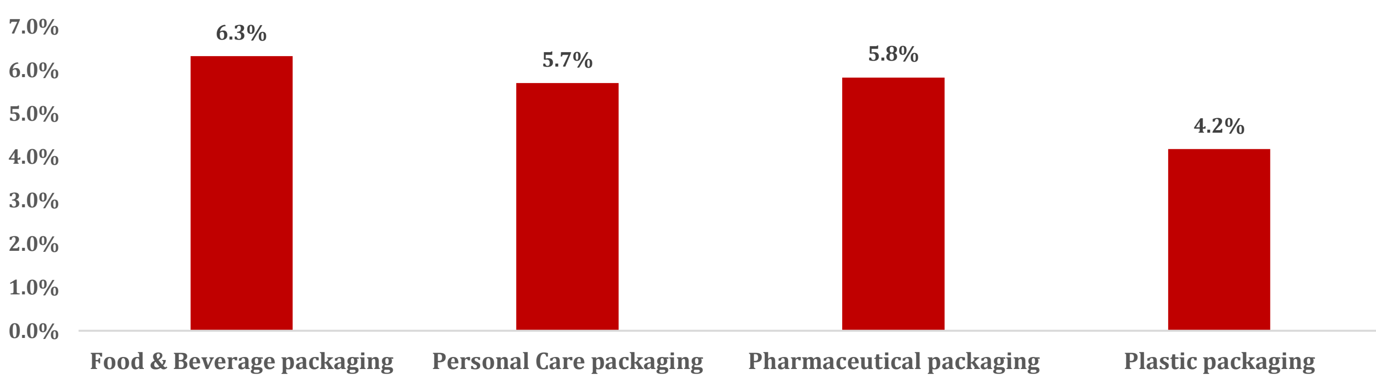
Source: Company Reports, U Capital Research

Plastic packaging boom in MENA driven by e-commerce and changing Lifestyles

The packaging product market in the MENA region is expected to grow at a CAGR of 4.1% from 2023 to 2030 with Saudi Arabia having a CAGR of 3.6% during the same period. Among packaging, plastic packaging is gaining popularity among consumers in the GCC region because of its lightweight, unbreakable, and user-friendly characteristics. Its affordability also makes it an attractive choice for businesses looking to improve profit margins.

The plastic packaging industry is experiencing significant growth in the region, primarily fueled by advancements in the food & beverage, personal care, and pharmaceutical sectors.

CAGR of packaging industry in GCC region (2023-2028E)



Source: U Capital Research

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The increasing demand for specialty and processed foods, as well as ready-to-eat and convenience foods, is driving the surge in demand for F&B packaging. According to the Saudi Arabian General Authority for Investment (SAGIA), spending on food services is expected to grow by ~6% per annum over the next five years. The rise of "dark kitchens" is also contributing to the market growth. Looking ahead, factors such as rising disposable income, the expanding e-commerce market, and increasing consumer health consciousness will drive growth in the personal care packaging sector. Additionally, government investments and the growing demand for generic drugs will support the growth of the pharmaceutical packaging industry.

Among plastic packaging, Polyethylene terephthalate (PET), Polypropylene (PP) and Polyethylene are the most popular which are derived from Ethylene, Propylene, HDPE, and LDPE and these are the key products for Tasnee. Thus, we expect the growing demand for packaging will lead to an increase in the petrochemical business for Tasnee.

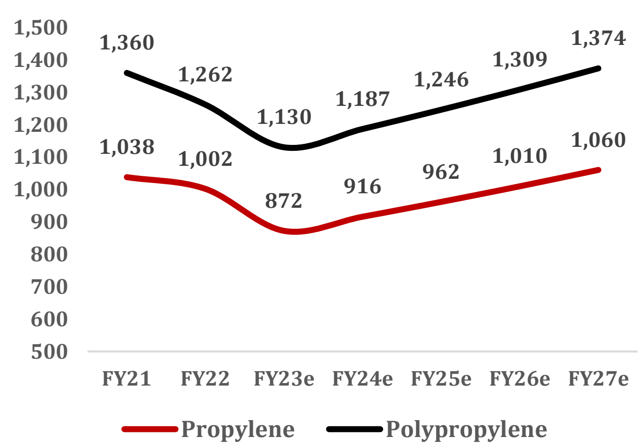
Plastic material with their properties and CAGR in the GCC region from 2023-28e

Material	Used in applications	CAGR (2023-28E for GCC region)
Polyethylene terephthalate (PET)	Bottles and flims	10.3%
Polypropylene (PP)	Packaging, Automotive, Textiles, Electrical & electronics and Medical	6.9%
Polyethylene	Packaging, Automotive, Textiles, Electrical & electronics and Medical	6.8%

Source: U Capital Research

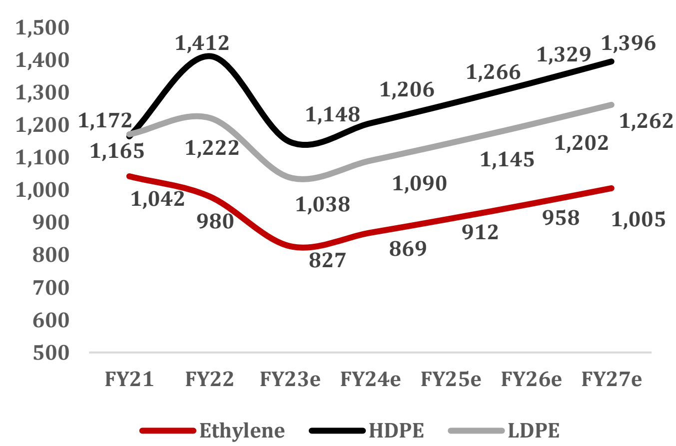
On the pricing side. petrochemical prices surged in 2021 and the first half of 2022, but they have begun to correct in the second half of 2022 and into 2023. We expect prices to stabilize after 2023, with HDPE and LDPE prices correcting by approximately 18.7% and 15%, respectively, and Ethylene and propylene prices declining by 15.6% and 12.9%, respectively. We believe that prices will recover and gradually improve beyond 2023.

Propylene and Polypropylene prices ($/MT)



Source: Company Reports, U Capital Research

Ethylene, HDPE, and LDPE prices ($/MT)



Source: Company Reports, U Capital Research

Positive outlook for KSA Paints and Cosmetic sector

The KSA paint sector is set for growth with expected CAGR of 3.38% between 2023-28, driven by expanding construction sector, increasing disposable income, rising awareness of the importance of painting, and government support through infrastructure investments. The sector is also benefiting from the government's efforts to diversify the economy along with development of new industries, such as the automotive and tourism industries, which are driving demand for paints.

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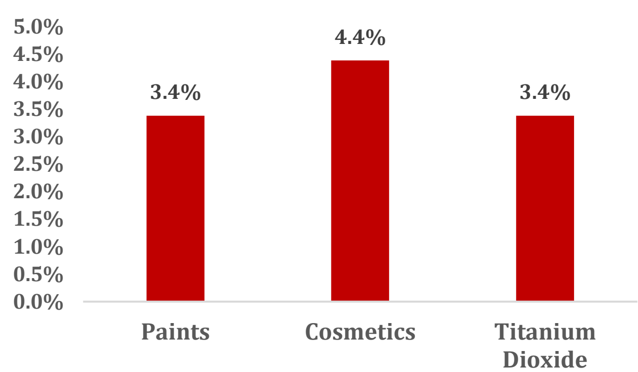
Similarly, the cosmetic sector is expected to grow at a CAGR of 4.38% during 2023-2028 amid increasing demand for personal care products, rising disposable income, and the growing e-commerce market in the region. Additionally, Saudi Arabia is witnessing a growing demand for halal beauty products which has gained enormous popularity in the region and is not limited to the Muslim community only. The growing importance of personal care and grooming, along with the influence of social media on beauty trends, further supports a positive outlook for the sector.

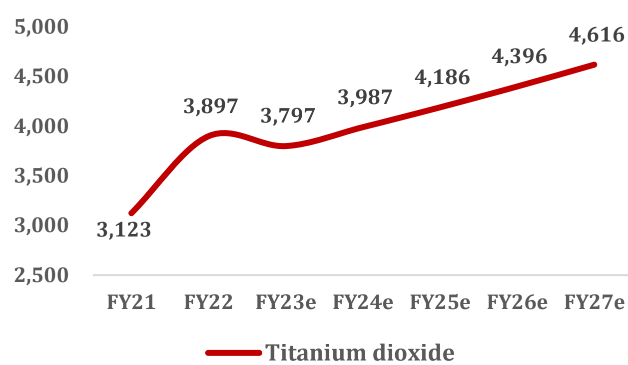
Titanium dioxide, the most widely used pigment in the world, plays a significant role in both paint and cosmetic production. Tasnee, as a major investor in the titanium value chain, stands to benefit from the surge in demand for paints and cosmetics. Thus, with a surge in demand for paints and cosmetics in the KSA region, we project an improvement in revenue as this segment is expected to contribute ~14% of the total revenue for 2023. Prices for titanium dioxide are expected to rise steadily post dip in 2023e.

CAGR (2023-2027e)



Source: Company Reports, U Capital Research

Titanium dioxide prices ($/MT)



Source: Company Reports, U Capital Research

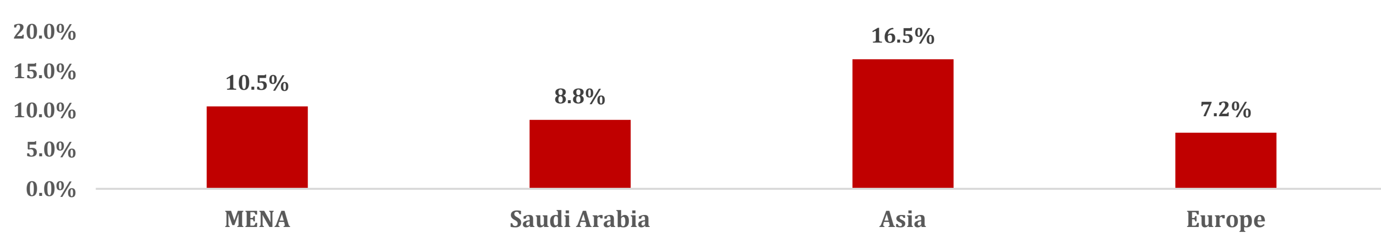
Liquid batteries poised for growth in MENA, Asia, and Europe

The market for liquid batteries for cars in the MENA region is expected to grow at a CAGR of 10.5% from 2023-28 driven by increasing demand for electric vehicles and due to the advantages of liquid batteries, including their high energy density and long lifespan. Technological advancements in the field are also expected to drive market expansion. With access to raw materials like lithium and cobalt, coupled with the rising demand for electric vehicles, the MENA liquid battery market is well-positioned to capitalize on these trends.

In Asia, particularly in China, Japan, and South Korea, the demand for liquid batteries is rapidly increasing due to the growing adoption of electric vehicles. Liquid batteries are perceived as more efficient and safer compared to traditional lithium-ion batteries, making them a popular choice for electric vehicles.

While in Europe, the liquid battery market for cars is still in its early stages, it is experiencing significant growth. Factors such as government support for electric vehicles and substantial investments in research and development are driving this growth. As the demand for electric vehicles continues to rise in Europe, the liquid battery market is expected to surge in the coming years.

CAGR for liquid batteries (2023-2028E)



Source: U Capital Research

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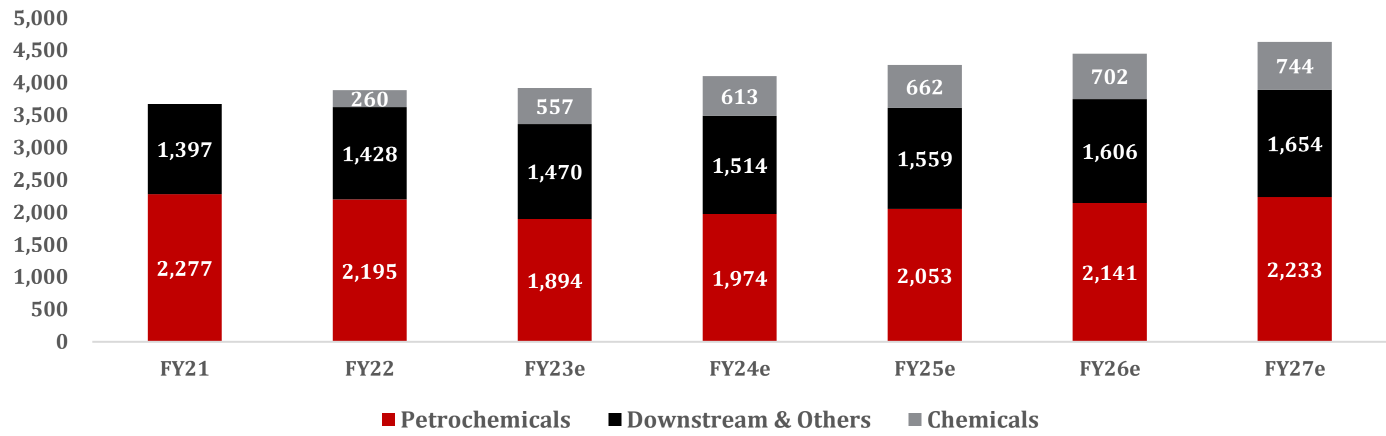
Tasnee poised for revenue growth amid surging demand across various applications

Tasnee generates ~48% of its revenue from petrochemical segment, with end markets related to plastic packaging in the KSA, MENA, Asia, and Europe regions. Most of the revenue (78%) is derived from the MENA and Asia regions, with Saudi Arabia being the highest contributor at 49.2%. With the anticipated increase in demand for these products, Tasnee is expected to see revenue growth post-2023. Revenues from petrochemical segment surged in 2021 due to rising prices but are expected to fall by 13.7% in 2023 due to decline in product prices. However, this decline will be offset by growth in the chemical (Titanium Dioxide) segment, which is expected to increase by 114% due to increased demand for paints and cosmetics in the KSA region as this segment derives revenue only from Saudi Arabia.

The downstream segment, which contributes around 37% of Tasnee's total revenue, is also expected to grow in the coming years due to the surging demand for liquid batteries from the MENA, Asia, and Europe regions. MENA and Asia regions contributes 82% of the downstream sales, thus the rapid growing demand for EV in these regions is going to drive revenue from downstream in coming years.

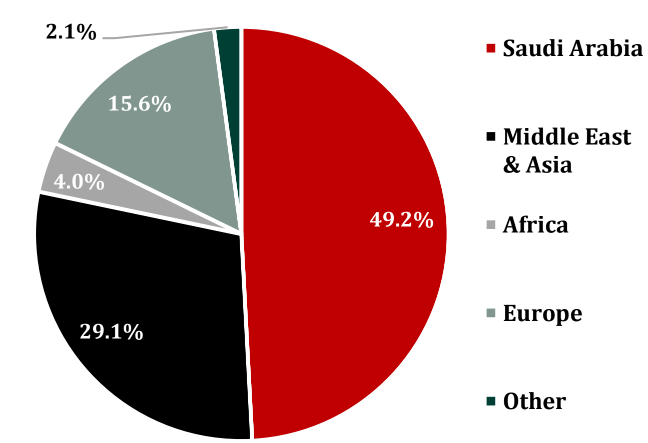
Overall, Tasnee's revenue growth stood at 5.7% in FY'22 but is projected to decline to 1% in FY'23 due to the challenges in the petrochemical sector. However, post-2023, steady revenue growth of ~4.6% is expected in 2024, with a CAGR of 4.3% between 2023-2027, indicating a positive trajectory for the group's financial performance.

Steady improvement in revenue post-2023



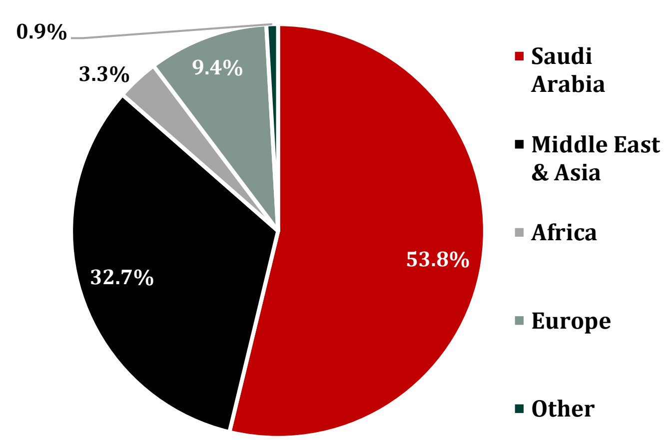
Source: Company Reports, U Capital Research

Petrochemical revenue by geography (FY'22)



Source: Company Reports, U Capital Research

Downstream revenue by geography (FY'22)



Source: Company Reports, U Capital Research

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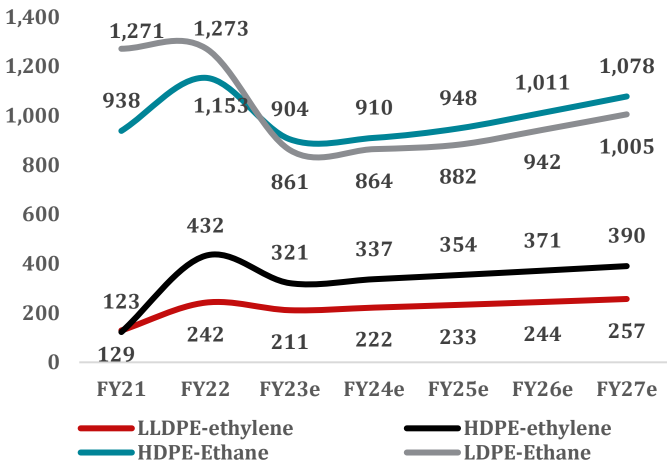
Tasnee exhibits robust performance amid improving spreads

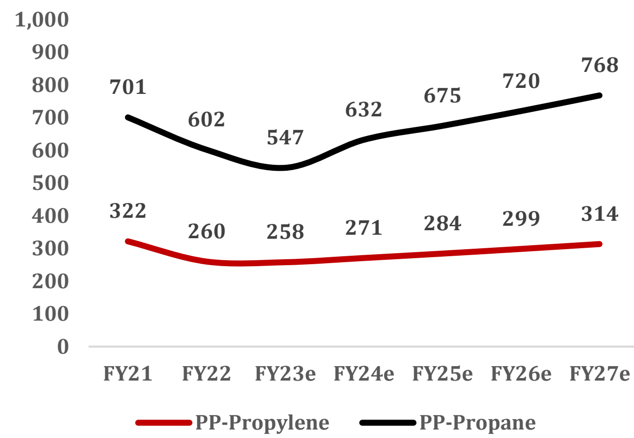
In FY’21, Tasnee saw an improvement in spreads across its entire petrochemical product portfolio. However, in FY’22 and 1H’23, spreads for PP-Propylene and PP-Propane declined due to price corrections. As a result, we expect spreads to decline for FY’23. Nevertheless, prices are projected to stabilize in FY'24 and gradually improve, leading to enhanced margins for the company.

Spreads likely to improve post 2023 ($/MT)



Source: Company Reports, U Capital Research

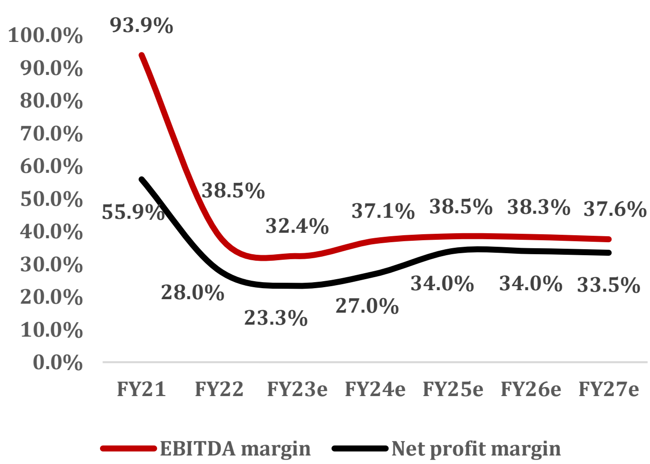
PP spreads expected to recover ($/MT)



Source: Company Reports, U Capital Research

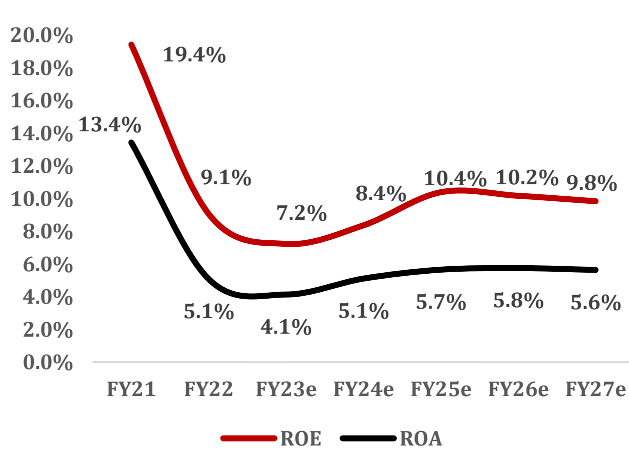
Petrochemicals account for a significant portion of Tasnee's revenue, so any change in spreads across petrochemicals directly impacts the company’s margins and profitability. In FY’21, EBITDA and net margins reached record highs of 93.9% and 55.9%, respectively. This exceptional performance was driven by increased profits from associates and joint ventures associated with the petrochemical business, attributed to higher petrochemical product prices in FY'21. However, margins declined in FY’22 and are expected to follow a similar trend in FY’23e. We anticipate EBITDA and net income margins to improve after FY23e and reach 37.8% and 34.1%, respectively, as spreads improve due to stabilizing prices and increased demand across the company's product portfolio.

Margins to recover post FY23



Source: Company Reports, U Capital Research

ROE & ROA: Recovery post FY23



Source: Company Reports, U Capital Research

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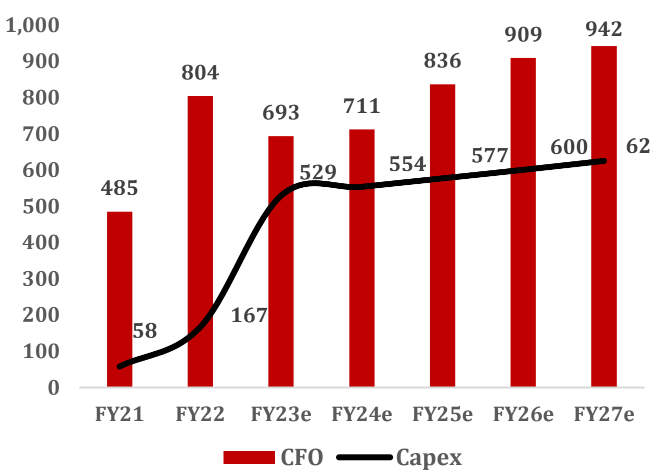
Tasnee's financial position: Resilient and growing

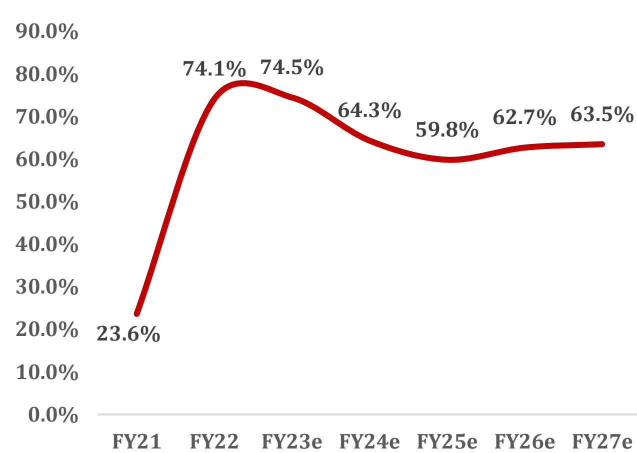
Tasnee is expected to maintain a strong financial position with consistent cash flow from operations and improving cash conversion ratio. In FY'22, cash flow from operations increased by 66% to SAR 804 million, driven by price increases that improved margins. However, cash flow from operations is expected to decline by 14% in fiscal year 2023 due to declining product prices. Nevertheless, post-FY'23e, as prices and demand recover, cash flow from operations is expected to grow at a CAGR of 7.7% from FY'23e to FY'27e. On capex side, we expect a surge in investing activity in FY'23e, with strategic investments expected in titanium dioxide (chemical segment) and liquid batteries (downstream segment). Going forward, we expect capex to steadily improve as the company prioritizes suitable prospects, instead of paying dividends

Surging CFO with Capex



Source: Company Reports, U Capital Research

Cash conversion ratio

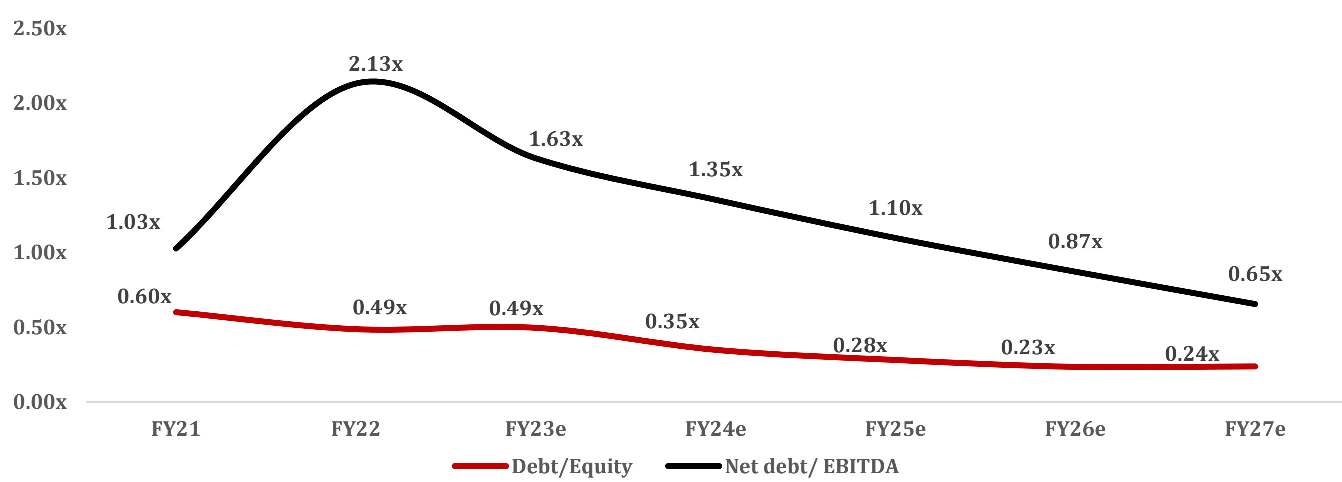


Source: Company Reports, U Capital Research

Prudent leverage demonstrates financial strength

Tasnee has demonstrated financial prudence by adopting a cautious approach to debt management, resulting in a strong financial position. The company's debt-to-equity ratio is expected to decrease, suggesting that it is relying less on debt. Similarly, the leverage ratio is expected to decline as Tasnee intends to further reduce its debt burden, indicating lower reliance on debt.

Leverage likely to decline going forward



Source: Company Reports, U Capital Research

Sensitivity Analysis

Our TP for National Industrialization Co (Tasnee AB) is sensitive to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards Cost of Equity. Our TP is also sensitive (although relatively much lower) to the Polypropylene and LDPE prices.

NIC AB

Terminal Growth rate	Cost of Equity: 8.8%	9.8%	10.8%	11.8%	12.8%
0.50%	18.5	16.7	15.2	13.9	12.8
0.75%	19.1	17.2	15.6	14.2	13.1
1.00%	19.8	17.7	16.0	14.6	13.4
1.25%	20.5	18.3	16.5	15.0	13.7
1.50%	21.3	18.9	17.0	15.4	14.0

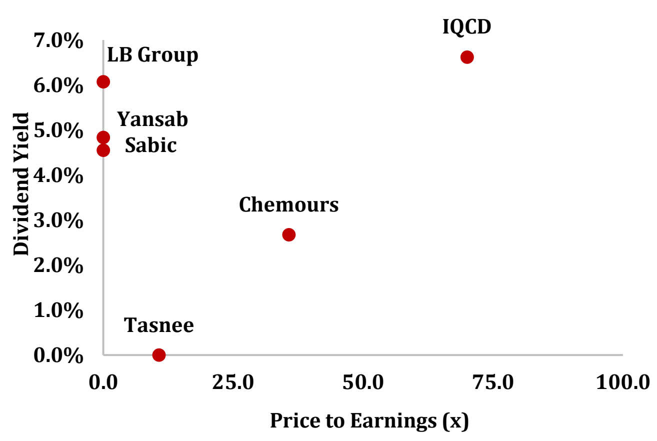
LDPE Price ($/MT, 2023e)	Polypropylene price ($/MT, 2023e): 572	722	872	1022	1172
638	15.6	15.9	16.1	16.3	16.5
838	15.5	15.8	16.1	16.3	16.5
1,038	15.4	15.7	16.0	16.2	16.4
1,238	15.3	15.6	16.1	16.2	16.4
1,438	15.2	15.5	16.1	16.1	16.3

Peer Group Valuation

Name	Mkt Cap (SAR mn)	Last Px (AED)	Px Change 1M, %	Px Change 3M, %	Px Change YTD, %	EV/EBITD A'23e, (x)	P/E'23e, (x)	ROE'23e, (%)	Div Yield' 23e, (%)	FCF Yield'23e (%)
NATIONAL INDUSTRIALIZATION Co	9,886.6	14.78	-3.9%	11.6%	19.6%	10.5	10.7	7.2%	0.0%	22.2%
LB GROUP CO LTD-A	21,074.9	16.89	1.0%	-17.2%	-10.7%	NA	NA	18.7%	6.1%	-4.6%
CHEMOURS CO/THE	21,305.8	38.07	12.3%	28.5%	24.3%	9.0	35.7	49.5%	2.7%	7.9%
SAUDI BASIC INDUSTRIES CORP	2,61,000.0	87.00	-1.5%	-5.4%	-2.7%	9.4	NA	7.8%	4.6%	10.3%
YANBU NATIONAL PETROCHEMICAL	26,634.4	47.35	1.3%	9.0%	13.8%	24.6	NA	7.9%	4.8%	5.4%
INDUSTRIES QATAR	74,120.6	11.90	1.9%	-5.2%	-7.1%	10.9	70.0	12.5%	6.6%	12.7%
Average						**12.9**	**38.8**	**17.3%**	**4.1%**	**9.0%**
Median						**10.5**	**35.7**	**10.2%**	**4.7%**	**9.1%**

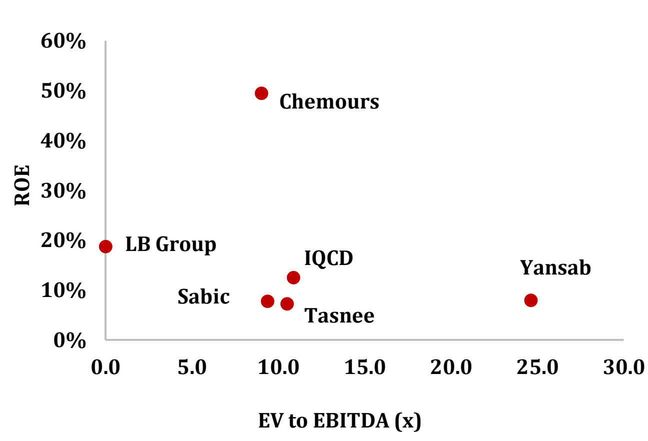
Source: Bloomberg, U Capital Research, na – not available, nm – not meaningful; *valued as of 17 July 2023 Market-cap weighted average multiples – EV/ EBITDA, and P/E

Price to Earnings & Dividend Yield



Source: Bloomberg, U Capital Research; As of 17 July 23

EV/EBITDA & ROE



Source: Bloomberg, U Capital Research; As of 17 July 23

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Valuation

To value Tasnee, we have used two valuation methods: the Discounted Cash Flow (DCF) and Relative Valuation. In our DCF analysis (80% weight), we used a WACC of 8.5%, a cost of equity of 10.8%, a risk-free rate of 3.8%, a beta of 1.17, and a risk premium of 5.9%. This method yielded a fair value of ~SAR 16.7 per share.

On the other hand, we have considered two multiples, P/E and EV/EBITDA, each with a 10% weight under the Relative Valuation method. We derived these multiples based on industry median values, resulting in a P/E multiple of 8.9x and an EV/EBITDA multiple of 10.2x. We then applied these multiples to our forecasted EPS of SAR 1.37/share and EBITDA of SAR 1,272mn, yielding fair values of SAR 12.2 and SAR 14.5 per share respectively.

Taking a weighted average of these valuations, we arrived at an overall fair value of SAR 16.0 per share.

Valuation

	Tasnee
DCF (80% weight)	
PV of Free Cash Flow (SAR mn)	
2023e	796
2024e	745
2025e	832
2026e	815
2027e	769
Terminal value	10,375
Total PV of Future Cashflows (Enterprise Value, SAR mn)	14,331
Assumptions	
Risk Free Rate (%)	3.8%
Adjusted Beta	1.17
Risk Premium (%)	5.9%
Cost of Equity (COE) (%)	10.8%
WACC (%)	8.5%
Equity value (SAR mn)	11,150
Outstanding Shares (mn)	669
Target Price (SAR)	**16.7**
P/E based Relative Valuation (10% weight)	
Target P/E multiple for 2023e	8.9x
EPS 2023e (SAR)	1.37
Target Price (SAR)	**12.2**
EV/EBITDA based Relative Valuation (10% weight)	
Target EV/EBITDA multiple for 2023e	10.2x
EBITDA 2023e (SAR mn)	1,272
Net Debt (SAR mn)	*3181*
Target Price (SAR)	**14.5**
Weighted Average Target Price (SAR)	**16.0**
Current Market Price (SAR)	*14.8*
Upside/(Downside), %	8.3%
Recommendation	**Hold**

Source: Company Financials, Bloomberg, U Capital Research

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Financial tables

(SAR mn)	FY21	FY22	Prev. FY23e	FY23e	Prev. FY24e	FY24e	FY25e
Income Statement							
Sales	3,673	3,883	3,495	3,920	2,757	4,100	4,274
COGS	-2,686	-3,019	-3,048	-3,232	-2,457	-3,181	-3,248
Gross profit	**987**	**864**	**446**	**689**	**300**	**920**	**1,026**
SG&A expenses	-593	-493	188	-554	194	-598	-642
Share of results of investments in associates and joint ventures	2,783	1,147	783	904	851	958	1,011
Operating profit	**3,177**	**1,262**	**1,417**	**1,039**	**1,346**	**1,280**	**1,394**
Other income – net	-625	390	210	389	165	407	424
Finance charges	-170	-279	-97	-271	-15	-287	-47
Income before tax	**2,383**	**1,373**	**1,529**	**1,157**	**1,497**	**1,399**	**1,771**
Zakat and Income tax	-329	-287	-229	-242	-225	-293	-319
Net income for the period	**2,054**	**1,086**	**1,300**	**915**	**1,272**	**1,107**	**1,453**
Balance Sheet							
Cash and bank balances	3,394	2,836	5,401	4,312	5,591	2,652	2,222
Prepayments and other current assets	628	554	628	554	628	554	554
Trade and other receivables	1,688	1,223	1,606	1,235	1,264	1,288	1,347
Inventories	700	760	794	813	638	798	818
Property, plant and equipment	2,825	2,639	2,606	2,636	2,485	2,606	2,576
Investments in joint ventures	12,306	11,765	12,040	11,777	12,343	12,032	12,298
Right of use assets	116	159	145	233	148	300	362
Total assets	**24,980**	**24,658**	**26,357**	**25,544**	**26,133**	**24,518**	**24,771**
Trade and other payables	1,889	1,414	1,764	1,568	1,114	1,523	1,556
Long-term borrowings	5,865	4,515	4,839	4,811	4,191	3,527	3,009
Lease liabilities	112	152	98	137	94	125	114
Share capital	6,689	6,689	6,689	6,689	6,689	6,689	6,689
Statutory reserve	1,490	1,557	1,700	1,615	1,778	1,686	1,780
Retained earnings	1,109	1,752	2,994	2,236	3,697	2,875	3,715
Total stockholders' equity	**11,563**	**12,395**	**14,206**	**12,901**	**15,355**	**13,550**	**14,403**
Total liabilities & stockholders' equity	**24,980**	**24,658**	**26,357**	**25,544**	**26,133**	**24,518**	**24,771**
Cash Flow Statement							
Cash from operating activities	485	804	1,205	693	614	711	836
Cash from investing activities	613	533	853	268	471	50	64
Cash from financing activities	-741	-1,895	-1,113	-285	-894	-2,421	-1,330
Net changes in cash	356	-558	945	676	190	-1,660	-430
Cash at the end of the period	3,011	2,836	5,401	4,312	5,591	2,652	2,222
Key Ratios							
Current ratio	1.3	1.2	1.9	1.3	2.2	1.0	1.0
Inventory turnover ratio	4.2	4.1	3.9	4.3	3.4	3.9	4.0
Debtors' turnover ratio	2.6	2.7	2.1	3.1	1.9	3.2	3.2
Creditors turnover ratio	3.4	2.7	3.6	2.4	3.4	2.6	3.4
Gross profit margin	26.9%	22.3%	12.8%	17.6%	10.9%	22.4%	24.0%
Operating margin	86.5%	32.5%	40.5%	26.5%	48.8%	31.2%	32.6%
Net profit margin	55.9%	28.0%	37.2%	23.3%	46.1%	27.0%	34.0%
EBITDA margin	93.9%	38.5%	47.4%	32.4%	57.7%	37.1%	38.5%
Average return on equity	19.42%	9.06%	9.54%	7.23%	8.61%	8.37%	10.39%
Average return on assets	13.43%	5.08%	5.56%	4.14%	5.15%	5.11%	5.66%
Debt/Equity (x)	0.60x	0.49x	0.40x	0.49x	0.32x	0.35x	0.28x
Interest coverage ratio (x)	18.71x	4.53x	14.55x	3.84x	90.86x	4.46x	29.62x
P/E	5.31x	7.62x	6.81x	10.80x	6.96x	8.93x	6.81x
EV/EBITDA	5.73x	8.95x	8.93x	10.51x	9.29x	8.79x	8.13x
EV/Sales	5.38x	3.66x	4.23x	3.41x	5.36x	3.26x	3.13x
EPS (SR)	3.76	1.62	1.94	1.37	1.90	1.65	2.17
Dividend payout ratio	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Dividend yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net debt (SR 'million)	3,537	3,181	329	2,072	-617	2,055	1,802
Net debt/ EBITDA	1.03x	2.13x	0.20x	1.63x	-0.39x	1.35x	1.10x
ROCE	15.72%	6.57%	6.48%	5.18%	6.01%	6.58%	7.03%

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