

SABIC reported a weak set of result with a net loss of SAR 2.22bn, above our estimated loss of SAR 187mn due to an impairment provision of SAR 1.18bn for its petrochemical assets in the European region. Normalized earnings stood at a net loss of SAR 1.04bn, above market consensus estimated loss of SAR 209mn. Stabilized volumetric sales were offset by weak product prices and lower contribution from the company's associates and joint ventures. Sales declined by 18.4%Q/Q impacted by lower product prices and challenging supply / demand conditions. Although we expect the Q2-20 is the bottom for SABIC and other petrochemical players, oversupplied market still look challenging during FY21/24. We remain **"Neutral"** on the stock with a revised TP of **SAR 80.8/share**.

- **Weak selling prices and a SAR 1.18bn provision are the key pressures:** Saudi Basic Industries Corporation (SABIC) posted net losses of SAR 2.22bn; below our estimate of loss of SAR 187.4mn and the market consensus estimates of loss of SAR 209mn. The weak performance is mainly attributed to i) an impairment provision of SAR 1.18bn for its certain petrochemical assets in the European region ii) lower average sales prices and products spreads iii) weak performance of listed subsidiaries, SAFCO's earnings came above market estimates, while Kayan and Yansab reported below expectations performance. Although top line came in-line with our estimate, the deviation of Q2-20 earnings from our estimates is mainly attributed to the recorded provision of SAR 1.18bn; and weaker than expected product spreads.
- **Despite COVID-19; SABIC showed solid plant utilization rates and sales volume:** SABIC's reported 29.5%Y/Y decline in revenue for Q2-20 to SAR 24.62bn, in-line with our estimate of SAR 25.9bn and below SAR 30.2bn in Q1-20 due to challenging supply/ demand conditions coupled with lower oil prices, which were negatively impacted by COVID-19. However, operational performance was resilient as evident in the flat sales volumes maintained in the second quarter with only a decline of 1%Q/Q despite a difficult demand environment. During the quarter, the average selling prices of Polyethylene plunged by 9.8%Q/Q and 24.8%Y/Y. Methanol prices dropped the most by 28.3%Q/Q and 42.2%Y/Y. while MEG-SABIC declined by 19.2%Q/Q and 24.9%Y/Y. PP and PC average prices declined by 8.9%Q/Q and 9.4%Q/Q, respectively.
- **Lower average feedstock prices partially offset by a decrease in product prices:** Gross profit stood at SAR 3.47bn, below our estimate of SAR 5.18bn primarily due to weak product spreads and the impairment of assets. Gross margin declined to 14.09% vs. 15.60% in the previous quarter and our estimate of 19.0%, despite relatively lower average cost of some feedstock. On Q/Q basis, SABIC's total gross margin was marginally supported by a 40% Q/Q decline in propane/butane cost (Almost 35% of the total feedstock), resulting in Propane-HDPE and Propane-PP spreads expansion by 16.2%Q/Q and 14.6%Q/Q, respectively.
- **Continuous focus on cost controls:** SABIC's witnessed 19.5%Q/Q EBITDA decline in Q2-20 to SAR 3.5bn, resulting in EBITDA margins of 14.2% in Q2-20 vs. 14.4% in the first quarter of 2020. Operating loss stood at SAR 1.26bn, missing our estimates of SAR 700mn and SAR 60mn recorded in Q1-20. The Company's OPEX stood at SAR 4.8bn, as compared our estimate of SAR 4.41bn and SAR 5.24bn in the previous quarter due to lower expenses associated with weak sales and continuous focus on cost controls

AJC view and valuation: Despite the challenging environment due to COVID-19, the company showed resilient operating performance and sales. During Q2-20, pressure on the company's top line and margins was mainly due to the significant decline in most main products prices such as MEG, MTBE and Methanol. Going forward, products prices started to improve gradually and we expect further recovery beyond Q3-20 with the pick-up in the global economic activities. SABIC deconsolidate numbers of businesses "YANPET", "KEMYA", "SHARQ" and SAMAC in the quarter after the Aramco deal, while retrospectively reassessed the control over other investments related to SADAF and ARRAZI. Thus, SABIC's net profit for 2019 has been restated and reduced by SAR 365mn and increases the net losses of Q1-20 by SAR 97mn. Although restrictions are beginning to ease around the world, the International Monetary Fund (IMF) further downgraded its global GDP forecast by 1.9% to -4.9% for 2020, with a very slow recovery seen in 2021. The near-term outlook is pointing to a continued recovery, while downside risks clearly dominating on Petchem industry by the coming capacity expansions and rising tension between the US and China. We believe the continued high operating rate, cost reduction initiatives and the current products prices recovery are likely to improve overall earnings for H2-20. The company is trading at a forward PE of 36.2x based on our FY21 earnings forecasts. We expected the company to be able to pay dividend at SAR 3.0/share during FY20, given the company's strong balance sheet and healthy cash flow generation. We remain **"Neutral"** on SABIC with a revised TP of **SAR 80.8/share**.

Neutral

Target Price (SAR) 80.8

Upside / (Downside)* -8.8%

Source: Tadawul *prices as of 17th of August 2020

Key Financials

SARmn (unless specified)	FY18	FY19	FY20E	FY21E
Revenues	169,128	139,737	113,386	130,497
Growth %	12.9%	-17.4%	-18.9%	15.1%
Net Income	21,521	5,563	(1,066)	7,345
Growth %	16.8%	-74.1%	NM	NM
EPS	7.17	1.85	(0.36)	2.45

Source: Company reports, Aljazira Capital

Key Ratios

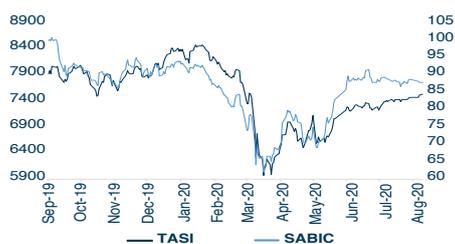
	FY18	FY19	FY20E	FY21E
Gross Margin	33.86%	25.42%	19.8%	26.1%
Net Margin	12.76%	3.98%	-0.9%	5.6%
P/E	16.76x	50.64x	NM	36.2x
P/B	2.12x	1.67	1.67	1.72
EV/EBITDA (x)	6.58x	7.82x	12.59x	9.25x
Dividend Yield	3.7%	4.7%	3.4%	4.5%

Key Market Data

Market Cap(SAR bn)	265.5
YTD%	-5.1%
52 week (High)/(Low)	104.80 /61.90
Share Outstanding (mn)	3000.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Company reports, Aljazira Capital, Bloomberg

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Investment Update

Key Financial Data

Amount in SAR mn, unless otherwise specified	FY18	FY19	FY20F	FY21F	FY22F	FY23F
Income statement						
Revenues	169,128	139,737	113,386	130,497	140,341	145,995
YoY growth	12.9%	-17.4%	-18.9%	15.1%	7.5%	4.0%
Cost of sales	(111,520)	(104,217)	(90,891)	(96,413)	(102,188)	(105,764)
Gross profit	57,608	35,520	22,496	34,085	38,153	40,232
General & administrative expense	(21,345)	(20,687)	(19,563)	(21,851)	(23,509)	(24,455)
Other income/expenses (net)	(406)	(128)	(157)	(159)	(160)	(162)
share of result of integral joint ventures			1,021	1,393	1,441	1,492
Operating profit	35,857	14,705	3,796	13,467	15,925	17,107
YoY growth	22.4%	-59.0%	-74.2%	254.8%	18.2%	7.4%
Share in earnings of equity-accounted investees	1,050	(1,595)	(877)	147	874	892
Financial / bank charges	(1,223)	(1,427)	(1,385)	(1,152)	(939)	(764)
Profit before zakat & minority interest	35,683	11,682	1,534	12,462	15,861	17,234
Minority interest	(10,365)	(2,900)	(1,251)	(3,514)	(4,473)	(4,860)
Zakat	(3,798)	(3,219)	(1,349)	(1,603)	(1,992)	(2,221)
Net profit	21,521	5,563	(1,066)	7,345	9,396	10,153
YoY growth	16.8%	-74.1%	NM	NM	27.9%	8.1%
Balance sheet						
Assets						
Cash and bank balance	42,591	38,313	27,479	19,415	17,196	15,861
Other current assets	55,182	51,090	49,378	53,465	56,703	59,503
Property plant & equipment	163,820	162,990	160,205	157,375	154,877	152,709
Other non-current assets	48,303	45,348	47,304	49,295	51,314	53,365
Total assets	319,711	310,366	297,083	292,357	292,990	294,431
Liabilities & owners' equity						
Total current liabilities	37,881	37,447	34,598	34,451	34,328	33,911
Long-term loans	41,692	34,460	32,737	31,428	34,571	38,028
Total non-current liabilities	18,702	27,207	27,479	27,754	28,031	28,312
Minority interests	48,352	42,489	43,573	44,684	45,823	46,992
Paid -up capital	30,000	30,000	30,000	30,000	30,000	30,000
Statutory reserves	15,000	15,000	15,000	15,000	15,000	15,000
General reserves	109,530	107,624	107,624	107,624	107,624	107,624
Retained earnings	18,555	16,138	6,072	1,416	(2,388)	(5,435)
Total owners' equity	173,084	168,762	158,696	154,040	150,236	147,189
Total equity & liabilities	319,711	310,366	297,083	292,357	292,990	294,431
Key fundamental ratios						
Liquidity ratios						
Current ratio (x)	2.8	2.5	2.4	2.3	2.3	2.4
Cash ratio (x)	1.1	1.0	0.8	0.6	0.5	0.5
Profitability ratios						
Gross profit margin	34.06%	25.42%	19.8%	26.1%	27.2%	27.6%
Operating margin	21.20%	10.52%	3.3%	10.3%	11.3%	11.7%
EBITDA margin	30.00%	25.41%	18.9%	23.0%	23.9%	23.0%
Net profit margin	12.72%	3.98%	-0.9%	5.6%	6.7%	7.0%
Return on assets	6.71%	1.77%	-0.4%	2.5%	3.2%	3.5%
Return on equity	12.77%	3.25%	-0.7%	4.7%	6.2%	6.8%
Leverage ratio						
Interest coverage (x)	29.31	10.30	2.74	11.69	16.97	22.38
Debt / equity (x)	0.25	0.21	0.21	0.21	0.24	0.27
Market/valuation ratios						
EV/sales (x)	2.13	1.99	2.39	2.13	2.02	1.97
EV/EBITDA (x)	7.10	7.82	12.66	9.25	8.78	8.58
EPS (SAR)	7.17	1.85	(0.36)	2.45	3.13	3.38
BVPS (SAR)	57.69	56.25	52.90	51.35	50.08	49.06
Market price (SAR)*	120.40	93.90	88.60	88.60	88.60	88.60
Market-Cap (SAR mn)	361,200	281,700	265,800	265,800	265,800	265,800
Dividend yield	3.7%	4.7%	3.4%	4.5%	5.0%	5.0%
P/E ratio (x)	16.78	50.64	(249.26)	36.19	28.29	26.18
P/BV ratio (x)	2.09	1.67	1.67	1.73	1.77	1.81

Source: Company financials, AlJazira research



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- Underweight:** This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
- Neutral:** The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
- Suspension of rating or rating on hold (SR/RH):** This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

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