

Advanced Petrochemicals Co

Petrochemicals – Industrial

APPC AB: Saudi Arabia

11 April 2022

الراجحي المالية
Al Rajhi Capital



US\$5.02bn

Market cap

9%

Free float

US\$9.03mn

Avg. daily volume

Target price

75.00

+3.6% over current

Current price

72.40

as at 10/4/2022

Research Department

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Existing rating

Underweight

Neutral

Overweight

Performance



Earnings

(SARmn)	2021	2022E	2023E
Revenue	3,111	3,909	3,459
Y-o-Y	39.4%	25.6%	-11.5%
Gross profit	1,059	1,116	1,143
Gross margin	34.0%	28.5%	33.0%
Net profit	815	879	968
Y-o-Y	36.9%	7.9%	10.1%
Net margin	26.2%	22.5%	28.0%
EPS (SAR)	3.1	3.4	3.7
DPS (SAR)	2.2	2.2	2.6
Payout ratio	69.0%	65.0%	69.9%

P/E (Curr)	23.1x	21.4x	19.4x
P/E (Target)	23.9x	22.2x	20.1x

Source: Company data, Al Rajhi Capital

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Q1: Maintain TP at SAR75/sh

APPC announced lower-than-expected Q1 earnings at SAR164mn. The miss was primarily due to increased other fixed costs (which we had expected to improve on the seasonality factors in Q1), and likely further impacted by lower product spreads, offsetting increased sales volume and controlled operating costs. Going forward, we expect product spreads to improve, on the back of likely improvement in average PP prices (already up by ~10% so far in Q2) on limited product availability and healthy regional demand. Further, higher freight rates amid tight container availability, and relatively slower increase expected in feedstock prices on easing oil prices, may further drive the product spreads higher. Overall, the long-term outlook remains positive, aided by i) healthy sales volume, ii) better-operating efficiencies, iii) the absence of any planned shutdowns, iv) healthy project pipeline and v) consistent dividend track-record. Considering the current market dynamics, we maintain our TP at SAR75/sh (post adjusting for bonus shares) based on SAR55/share for the existing plants (4% dividend yield on DPS2.2/share), SAR12/share for the PDH-PP Jubail plant (NPV basis), and SAR8/share for the Petrochemical Complex - Jubail 2 project. Post +23% YTD return, we revise our rating to Neutral (Overweight earlier) on the stock.

Figure 1 APPC Q1 2022 results

(SAR mn)	Q1 2022	Q1 2021	Y-o-Y	Q4 2021	Q-o-Q	ARC est	vs ARC
Revenue	866	632	37.0%	905	-4.3%	886	-2.2%
Gross profit	211	200	5.5%	245	-13.9%	283	-25.4%
Gross margin	24.4%	31.6%		27.1%		31.9%	
Operating profit	182	164	11.0%	186	-2.2%	225	-19.3%
Operating margin	21.0%	25.9%		20.6%		25.5%	
Net profit	164	171	-4.1%	158	3.8%	187	-12.1%
Net margin	17.8%	28.4%		27.1%		21.3%	
EPS	0.63	0.66	-4.3%	0.62	1.9%	0.72	-12.2%

Source: Company data, Al Rajhi Capital.

Q1 results: APPC reported Q1 revenues at SAR866mn (largely in line with our estimate of SAR886mn), down 4.3% q-o-q, primarily driven by lower PP prices (-10% q-o-q), offsetting increased sales volume (+7% q-o-q). However, higher-than-expected other COGS pushed gross and operating profits below our estimates, offsetting better-than-expected improvement in SG&A costs. The company continued to incur losses from its equity investment (SK Advanced), although it managed to reduce the losses to ~SAR12mn (vs. our expected losses of SAR24mn), capping the miss at the net profit level. Overall, net profit came in at SAR164mn, missing our estimate of SAR187mn.

APPC' shareholders approve 20.1% capital increase via bonus share, and buyback plans: Advanced petrochemical company (APPC) recently announced two material developments (capital increase via bonus shares and share repurchase plan). We believe that both these announcements are positive for the stock, as this implies the company's confidence in its existing operations and future expansion projects and also its commitment to shareholders.

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APPC's shareholders approve 20.1% capital by way of issuing bonus shares. To support the current asset base and future expansions, APPC's shareholders recently approved the board of directors recommended of a 20.1% capital increase by issuing one bonus share for every five shares held. Post bonus share issuance, the share capital has increased from SAR2.2bn (216.5mn shares) to SAR2.6bn (260mn shares). The company might have capitalized SAR174mn from retained earnings and SAR261mn from statutory reserve to increase the capital increase.

APPC announces repurchase plan for employee shares incentive program. Similar to bonus shares, APPC's shareholders approved the company's buyback plan at a maximum of 1.5mn shares (worth ~SAR110mn at the current price) and retain them for the Employee Shares Incentive Program, probably as the current stock price might not be reflecting its actual fair value. This share repurchase program will be funded through internal resources (cash and cash equivalents as of Q3 2021: SAR312.5mn), which we believe is sufficient and manageable. The announced buyback plan would also act as a support to its stock price going forward. However, this might cap its dividend-paying abilities (2022E DPS: SAR2.2).

Valuation and risks: We continue to remain positive on the company's medium to long-term growth prospects, due to i) strong utilization rates, ii) consistent operating performance, iii) FCF generation ability, iv) healthy balance sheet, and v) excellent management quality. The stock is currently trading at a P/E of 19.4x on our 2022E EPS despite the massive expansion (3Y historical avg. of 18.2x).

We value the existing plants using a 4% historical dividend yield on DPS of SAR2.2 for 2022. 2021 results assure management commitment that dividends will remain untouched despite the projects. To this, we add our estimated value of the new PDH-PP KSA plant ([SAR12/sh based on our NPV analysis](#); after adjusting for bonus) and the Petrochemical Complex - Jubail 2 project (SAR8/sh) to arrive with a TP of SAR75/sh (after adjusting for bonus shares). We believe that the stock deserves to trade at a premium to its peers, given the superior performance. However, in the medium term, the stock may continue tracking the PP-propane spreads or pricing the stock at ~4% dividend yield. We believe that the dividend yield-based valuation approach is ideal to value the fundamentally strong dividend-paying companies like APPC amid the current market dynamics.

The key upside trigger might be attributed to sustained improvement in spreads while further weakness in product spreads, a dividend cut, and/or any unplanned shutdown may act as the downside triggers.



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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.

"Target price": We estimate target value per share for every stock we cover. This is normally based on widely accepted methods appropriate to the stock or sector under consideration, e.g. DCF (discounted cash flow) or SoTP (sum of the parts) analysis.

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