

Sahara International Petrochemical Co. (Sipchem)

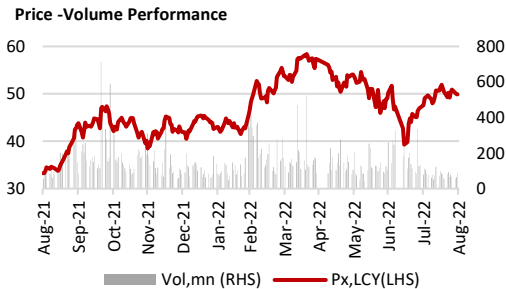
Target Price: SAR 53.4

Upside: 7.1%

Recommendation	Hold
Bloomberg Ticker	SIPCHEM AB
Current Market Price (SAR)	49.9
52wk High / Low (SAR)	58.4 / 33.3
12m Average Vol. (mn)	3.4
Mkt.Cap. (SAR bn)	36.2
Shares Outstanding (mn)	726
Free Float (%)	89%
3m Avg Daily Turnover (SAR mn)	123.3
6m Average Daily Turnover (SAR mn)	153.9
PE 2023e (x)	14.4
EV/EBITDA 2023e (x)	8.8
Dividend Yield '23e (%)	3.2%

Price Performance:	
1 month (%)	6.0%
3 months (%)	-7.9%
12 months (%)	49.9%

Source: Refinitiv, as of 30th Aug. 2022



Source: Refinitiv

Valuation method	SAR	Percentage from CMP	Weights
DCF	55.2	10.7%	80%
EV/EBITDA	48.1	-3.4%	10%
PE multiple	44.2	-11.3%	10%
Target price	53.4	7.1%	

Source: U Capital Research

31st August 2022

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- Diversified operations provide resilience to business
- Global demand likely to moderate due to looming slowdown
- Declining price environment in 3Q22 likely to persist
- We retain our previous Hold rating on the stock

Sipchem's bottom-line in 2Q22 increased by 46.0% YoY to SAR 1,383 mn, above our estimate of SAR 1,105 mn. The growth in bottom-line was mainly due to higher-than-expected selling prices and robust volume sales of most products. Vinyl Acetate and Polypropylene are the major products sold by the company. The price of Polypropylene increased 63.4% YoY, while the price of Vinyl Acetate increased 5.1% YoY. We believe the company also benefited from higher-than-expected sales volumes in spite of such higher prices. In addition to increase in prices and volumes, the revenues from the company's marketing segment grew 94.2% YoY.

The net income for 2Q22 was also boosted by increase in share of profit from joint ventures and associates, that grew by 81.3% YoY, and low base effect due to an impairment expense in 2Q21.

Corporate actions:

Dividend: Sipchem's board of directors approved a cash dividend of SAR 1.75 per share (17.5% of par value per share) for 1H22. This is higher by 133.3% compared to 1H21.

Valuation and risk: Post 2Q22 earnings, we revise upward our bottom-line estimate on Sipchem for FY22 by 11.5%, due to higher-than-expected increase in the product selling prices, increase in marketing revenues and higher share of profits from joint ventures and associates, triggered by Russia's invasion of Ukraine. However, post adjusting the bottom line, and accounting for changes in valuation, we arrive at our revised target price of SAR 53.4 per share as compared to SAR 54 per share, previously. We retain our previous **Hold** rating on the stock. The performance in 2H22 is expected to mellow down compared to 1H22 in the backdrop of looming slowdown in the global markets and due to a declining price environment in 3Q22 so far (between 10-25% fall in prices from start of 3Q22). The FY22 EPS estimate is at SAR 4.70 vs SAR 4.22 earlier. Currently, the stock trades at 14.4x P/E and 8.8x EV/EBITDA, based on our FY23 estimates. The downside risks to our valuation include weaker than expected economic activity levels and consumer demand owing to high inflation and rising interest rates, leading to a faster-than-expected correction in product selling prices, lower-than-expected sales, and unexpected plant shutdowns. Key upside risks to our valuation include rise in the prices of polypropylene, vinyl acetate and other major contributors to revenues, lower feedstock cost, sustained improvement in demand, and higher utilization levels.

Valuation:

Discounted Cash Flow Method

	FY22	FY23	FY24	FY25	FY26	Terminal Value
Pegged on Aug 30, 2022						
Time period index	0.34	1.34	2.34	3.34	4.34	4.34
Free cash flow						
PAT	4,018	2,952	2,894	2,885	2,911	
Interest (1-tax rate)	309	226	209	196	178	
D&A	984	1,009	1,034	1,059	1,084	
Changes in Working Capital	218	(36)	14	(23)	(14)	
Capex	(654)	(635)	(631)	(635)	(638)	
Free cash flow to firm (FCFF)	4,876	3,516	3,520	3,481	3,522	40,595
Discounted FCFF	4,718	3,084	2,798	2,509	2,301	26,523
Enterprise Value	41,933					
Less: Total debt	4,556					
Add: Cash & equivalent	3,836					
Less: Minority interest	1,135					
Equity Value	40,068					
Shares O/S	726					
Equity Value per share	55.2					
Current share price (SAR)	49.85					
% upside/downside	10.7%					

We use a DCF methodology with a WACC of 10.3% and a long term growth rate of 1.5% which gives us a TP of SAR 55.2 per share. We have given a weightage of 80% to DCF valuation.

Petrochemical comps

Company	Region	MCap (USD bn)	PE FY23E	EV/EBITDA FY23E
Sipchem	KSA	9.7	14.4	8.8
SABIC	KSA	81.8	14.4	7.5
Yansab	KSA	7.8	22.4	10.2
Saudi Kayan	KSA	6.1	21.0	8.7
SIIG	KSA	5.4	15.2	12.9
Tasnee	KSA	3.0	10.4	8.3
Advanced	KSA	3.7	23.7	17.7
Industries Qatar	UAE	30.9	11.2	11.9
ICL Group Ltd	Israel	13.9	8.4	5.6
Sasol Ltd	USA	13.7	4.8	3.6
BASF SE	China	38.6	8.5	6.1
Median			12.8	8.5

We have given a weightage of 10% each to the EV/EBITDA and P/E multiples. At median peer P/E multiple of 12.8x and EV/EBITDA multiple of 8.5x, we arrive at target price of SAR 44.2 and SAR 48.1 per share respectively.

Sensitivity table

		Cost of Equity					Vinyl Acetate (USD/t, 2H22e)						
		11%	12%	13%	14%	15%							
Terminal Growth rate	1.00%	59.3	55.2	51.7	48.7	46.1	Polypropylene price (USD/t, 2H22e)	730	53.1	53.2	53.2	53.3	53.4
	1.25%	60.6	56.2	52.5	49.4	46.7		880	53.2	53.3	53.3	53.4	53.4
	1.50%	61.9	57.2	53.4	50.1	47.3		1030	53.3	53.3	53.4	53.4	53.5
	1.75%	63.3	58.4	54.3	50.9	47.9		1180	53.3	53.4	53.4	53.5	53.6
	2.00%	64.8	59.6	55.3	51.7	48.6		1330	53.4	53.4	53.5	53.6	53.6

Key Financials

(SAR mn)	FY19	FY20	FY21	Prev. FY22e	FY22e	Prev. FY23e	FY23e	Prev. FY24e	FY24e
Income Statement									
Sales	5,440	5,323	9,982	9,883	9,935	9,655	9,655	9,597	9,597
COGS	(3,804)	(4,150)	(4,402)	(4,752)	(4,753)	(5,151)	(5,172)	(5,133)	(5,166)
Gross profit	1,635	1,173	5,580	5,130	5,182	4,503	4,483	4,464	4,431
SG&A expenses	(729)	(813)	(1,115)	(1,129)	(1,111)	(1,124)	(1,142)	(1,131)	(1,150)
Operating profit	906	360	4,464	4,001	4,070	3,379	3,341	3,333	3,281
Share of results of investments in associates and joint ventures	(27)	(34)	531	548	455	409	356	380	327
Other income – net	(119)	153	(269)	(20)	30	0	87	0	86
Finance charges	(370)	(294)	(319)	(239)	(326)	(234)	(270)	(212)	(249)
Income before tax	390	185	4,408	4,291	4,230	3,554	3,514	3,501	3,446
Zakat and Income tax	(145)	(128)	(450)	(687)	(211)	(569)	(562)	(560)	(551)
Net income for the period	245	57	3,958	3,604	4,018	2,985	2,952	2,941	2,894
Balance Sheet									
Cash and bank balances	1,791	2,497	2,690	5,061	4,496	6,729	5,904	9,208	7,420
Prepayments and other current assets	188	190	227	227	227	227	227	227	227
Trade and other receivables	842	1,061	1,862	1,354	1,361	1,323	1,323	1,311	1,311
Inventories	957	908	1,145	1,107	1,107	1,200	1,204	1,192	1,200
Property, plant and equipment	13,971	13,016	12,218	11,578	11,994	10,931	11,729	10,277	11,438
Investments in joint ventures	3,560	3,493	3,963	4,247	4,153	4,381	4,282	4,557	4,431
Right of use assets	68	61	120	133	121	144	121	153	122
Total assets	23,991	23,765	24,504	25,783	25,550	26,849	26,731	28,679	27,938
Trade and other payables	188	227	312	269	267	290	291	288	289
Long-term borrowings	6,699	5,340	4,721	4,145	3,773	3,747	3,481	4,037	3,255
Lease liabilities	69	63	154	147	147	138	138	130	130
Share capital	7,333	7,333	7,333	7,333	7,333	7,333	7,333	7,333	7,333
Statutory reserve	1,235	1,253	1,612	1,918	1,954	2,172	2,205	2,422	2,205
Retained earnings	603	398	2,014	3,376	3,532	4,504	4,647	5,615	5,987
Total stockholders' equity	14,338	13,836	15,696	17,499	17,700	18,992	19,177	20,464	20,625
Total liabilities & stockholders' equity	23,991	23,765	24,504	25,783	25,550	26,849	26,731	28,679	27,938
Cash Flow Statement									
Cash from operating activities	1,797	1,610	4,898	4,801	5,440	3,726	3,817	3,756	3,843
Cash from investing activities	(269)	51	(260)	117	(349)	144	(311)	74	(358)
Cash from financing activities	(1,665)	(956)	(4,445)	(2,548)	(3,286)	(2,202)	(2,097)	(1,350)	(1,970)
Net changes in cash	(137)	705	193	2,370	1,805	1,668	1,409	2,480	1,516
Cash at the end of the period	1,791	2,497	2,690	5,061	4,496	6,729	5,904	9,208	7,420
Key Ratios									
Current ratio	2.1	1.4	2.0	2.6	2.5	3.3	3.0	4.0	3.6
Inventory turnover ratio	4.3	4.5	4.3	4.0	3.8	4.5	4.5	4.3	4.3
Debtors' turnover ratio	7.2	5.6	6.8	6.4	6.1	7.2	7.2	7.3	7.3
Creditors turnover ratio	3.8	2.9	3.3	8.1	9.5	7.4	8.1	7.5	8.7
Gross profit margin	30.1%	22.0%	55.9%	51.9%	52.2%	46.6%	46.4%	46.5%	46.2%
Operating margin	16.7%	6.8%	44.7%	40.5%	41.0%	35.0%	34.6%	34.7%	34.2%
Net profit margin	4.5%	1.1%	39.7%	36.5%	40.4%	30.9%	30.6%	30.6%	30.2%
EBITDA margin	33.2%	24.5%	54.8%	50.4%	50.9%	45.2%	45.1%	45.1%	45.0%
Average return on equity	2.28%	0.41%	26.81%	21.72%	24.06%	16.36%	16.01%	14.91%	14.54%
Average return on assets	4.60%	1.51%	18.79%	16.33%	16.61%	13.41%	13.19%	12.66%	12.55%
Debt/Equity (x)	0.59x	0.59x	0.40x	0.29x	0.28x	0.24x	0.24x	0.24x	0.21x
Interest coverage ratio (x)	2.45x	1.23x	14.00x	16.75x	12.50x	14.43x	12.39x	15.72x	13.18x
P/E	34.54x	72.17x	8.50x	9.18x	10.60x	11.08x	14.43x	11.25x	14.72x
EV/EBITDA	867.79x	28.15x	6.77x	7.44x	7.53x	8.49x	8.75x	8.56x	8.82x
EV/Sales	9.44x	10.72x	3.71x	3.75x	3.83x	3.83x	3.94x	3.86x	3.97x
EPS (SR)	0.52	0.24	4.94	4.22	4.70	3.49	3.45	3.44	3.39
Dividend payout ratio	177.9%	206.9%	45.2%	38.72%	45.55%	38.72%	45.55%	38.72%	45.55%
Dividend yield (%)	5.15%	2.87%	5.31%	4.22%	4.30%	3.49%	3.16%	3.44%	3.10%
Net debt (SR 'million)	5,742	4,875	3,064	(30)	142	(2,174)	(1,619)	(4,323)	(3,410)

Source: Company Reports, U Capital Research

Disclaimer

Recommendation

BUY	Greater than 20%
ACCUMULATE	Between +10% and +20%
HOLD	Between +10% and -10%
REDUCE	Between -10% and -20%
SELL	Lower than -20%



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