**SIPCHEM**
**Petrochemicals – Industrial**
SIPCHEM AB: Saudi Arabia
03 March 2022

الراجحي المالية
Al Rajhi Capital

| US$9.445bn | 90% | US$34.39mn |
|---|---|---|
| Market cap | Free float | Avg. daily volume |

| | | |
|---|---|---|
| **Target price** | 55.00 | +13.9% over current |
| **Current price** | **48.30** | **as at 1/3/2022** |


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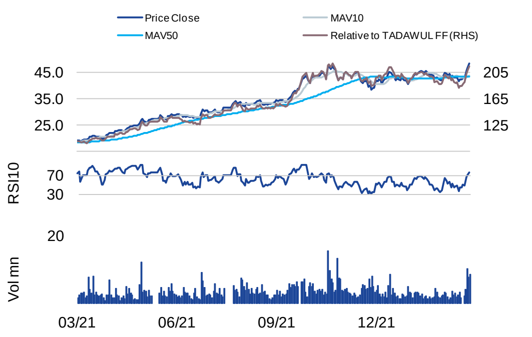
**Existing rating**

| Underweight | Neutral | Overweight |
|---|---|---|

**Performance**



Source: Bloomberg

**Earnings**

| (SARmn) | 2020 | 2021 | 2022e |
|---|---|---|---|
| Revenue | 5,323 | 9,982 | 9,508 |
| Y-o-Y | -2.1% | 87.5% | -4.7% |
| Gross profit | 1,173 | 5,580 | 5,039 |
| Gross margin | 22.0% | 55.9% | 53.0% |
| EBITDA | 1,291 | 5,377 | 4,816 |
| EBITDA margin | 24.3% | 53.9% | 50.6% |
| Net profit | 176 | 3,592 | 3,321 |
| Net margin | 3.3% | 36.0% | 34.9% |
| EPS (SAR) | 0.24 | 4.94 | 4.53 |
| DPS (SAR) | 0.50 | 2.25 | 2.50 |
| Payout ratio | 208.5% | 45.5% | 55.2% |
| ROE | 0.7% | 13.7% | 11.8% |
| EV/EBITDA | 28.9x | 7.0x | 7.8x |
| P/E | NM | 9.9x | 10.8x |

**Source:** Company data, Al Rajhi Capital

# SIPCHEM

## Raise Target Price to SAR55/sh.

*Sipchem reported strong Q4 results with bottom-line reaching record highs, beating our and consensus estimates by more than 30%, aided by higher-than-expected sales volume, coupled with better-than-expected operating efficiencies and equity income. While benchmark Methanol prices were around cUS$400/tonne in mid-Jan 2022 vs our US$420/tonne for 2022E, today they are around US$460/tonne. Given the Russian-Ukraine situation, with Brent at US$110+/barrel, we believe that Methanol and likewise other key products are likely to play catch up. Polymer prices generally follow oil prices with a lag. However, even without factoring for an increase in prices, just from the improved operating efficiencies that we witnessed in 2021, EPS could reach SAR4.5/share (vs EPS 4.9/share) even after adjusting for the planned shutdowns at Al Waha and SAMAPCO in Q1 2022. In addition, we see the possibility of a further increase in pay-out with DPS reaching SAR2.5 for 2022 (vs. SAR2.25/sh. in 2021), implying a dividend yield of 5%, at only 55% earnings pay-out. We raise our estimates higher, resulting in an increase in our TP to SAR55/sh. (SAR48 per share earlier) based on our DCF valuation model. Accordingly we upgrade our rating to Overweight (from Neutral).*

**Figure 1 SIPCHEM Q4 2021 results**

| (SAR mn) | Q4 2021 | Q4 2020 | Y-o-Y | Q3 2021 | Q-o-Q | ARC est | vs ARC |
|---|---|---|---|---|---|---|---|
| **Revenue** | **3,083** | **1,607** | **91.9%** | **2,506** | **23.0%** | **2,704** | **14.0%** |
| Gross profit | 1,777 | 519 | 242.6% | 1,369 | 29.8% | 1,503 | 18.2% |
| Gross margin | 57.6% | 32.3% | | 54.6% | | 55.6% | |
| Operating profit | 1,452 | 299 | 385.5% | 1,140 | 27.4% | 1,283 | 13.1% |
| Operating margin | 47.1% | 18.6% | | 45.5% | | 47.5% | |
| **Net profit** | **1,321** | **318** | 315.8% | **1,030** | 28.3% | **1,023** | 29.1% |
| Net margin | 42.9% | 19.8% | | 41.1% | | 37.8% | |
| **EPS** | **1.80** | **0.43** | **315.6%** | **1.40** | **28.2%** | **1.38** | **30.7%** |

Source: Company data, Al Rajhi Capital.

**Q4 results:** Top-line jumped ~23% q-o-q to SAR3,083, beating our estimate of 2,704mn (consensus: SAR2,773mn), primarily due to higher-than-expected sales volume and increased intermediate product prices (mostly VAM and AA). Further, better-than-expected improvement in cost efficiencies led to a further beat at the gross profit level with gross margin coming 2.1pps above our estimate. However, it seems operating costs (mainly SG&A costs) could have increased by ~42% q-o-q (10.5% of revenues; above its guidance of 9%) in Q4, likely due to year-end seasonality, resulting in lower-than-expected operating margin (47.1% vs. 47.5% estimated). Nonetheless, the company has reported a strong equity income of ~SAR266mn in Q4, significantly higher than our estimate. Accordingly, net profit jumped 28% to SAR1,321mn, above our (SAR1,023mn) and consensus (SAR1,134mn) estimates.

**Sipchem announces a couple of shutdowns at Al Waha and SAMAPCO.** Sipchem recently announced periodic maintenance shutdowns at Al Waha Petrochemical Company (75% holding) and Sahara & Ma'aden Petrochemical Company (SAMAPCO; an affiliate of Sipchem with 50% stake) for about 4 weeks, starting 14 Feb 2022. These shutdowns are in line with the company's 2022 business plan and the relevant financial impact would be reflected in Q1 2022 results. Based on our initial calculations, we expect a total financial impact of around SAR140mn in 2022, which is around 4% of our 2022E earnings estimates.

**Strong synergy realizations ahead of schedule.** Sipchem has achieved total synergies of SAR298mn in 2021 (well ahead of targeted June 2022) through its merger with Sahara Petrochemical. The company had earlier indicated possible synergies of SAR175-225mn at the EBITDA level after three years of its merger. Quicker synergy realizations, coupled with healthy product prices and better efficiencies ensure sustainable and healthy earnings performance for the company in 2022 as well.

**Sipchem unit inks SAR1bn refinance deal with BSF.** Sipchem recently announced that its affiliate, Al Waha Petrochemicals Co. has signed SAR 1bn Shariah-compliant facility agreement with Banque Saudi Fransi (BSF) to refinance an existing SAR1.96bn syndicated bank facility. This could lower the interest burden going forward as the new facility offers favorable terms and prices.

**Sipchem distributes above expected dividends for H2 2021.** Sipchem distributed a cash dividend per share of SAR1.5/sh. (SAR0.75/sh. for H1 2021; SAR2.25/share for 2021) for H2 2021, above our forecasted DPS of SAR0.75/sh, which could be attributed to increased cash flows driven by higher product prices. For 2022E, we see a possibility of further increase in pay out to SAR2.5/sh. (~5% yield; ~55% payout vs. ~110% average over 2018-21), supported by healthy product prices amid improving demand post-economic recovery, and better efficiencies on cost optimization and synergy realization.

**Valuation and risks.** We continue to remain positive on Sipchem, given its strong fundamentals, production & operating efficiencies, and cost-saving measures along with strong FCF generation capabilities and comfortable debt position. We value Sipchem using DCF (based on FCF, cost of equity 11.3%) at SAR55/share (SAR48/sh. earlier), implying an Overweight rating for the stock. The stock currently trades at ~11x on our 2022E EPS, lower than the historical three years average of ~17x.

Key upside risks include better-than-expected product prices, faster-than-expected ramping up production at IMC, and higher dividends in 2020. Major downside risks involve unexpected disruption at the company's upstream operations, which can further impact its downstream plants as well and persistent weakness in product prices, particularly Methanol prices.

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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.

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