

Quarterly Earnings Preview

Petrochemicals –Industrial

Saudi Arabia

9 April 2011

الراجحي المالية
Al Rajhi Capital



US\$102.2bn Market cap
27.7% Free float
US\$317.1mn Avg. daily volume

Target mkt cap **SAR445bn** 16.2% over current
Consensus mkt cap. **SAR434bn** 13.4% over current
Current mkt cap. **SAR389bn** as at 09/04/2011

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Underweight

Neutral

Overweight

Key themes

We expect Saudi petrochemicals suppliers to outperform global rivals with margins driven by cheap feedstock costs and strong demand coming from Asia. We believe a shift towards heavier, more expensive feedstock in plants from now on will not constrain profits growth as improving prices and higher volumes should offset the higher costs.

Implications

We like SABIC's broad business mix, its low-cost production and its strategy of high investment. Sipchem should see a strong recovery as new investment diversifies revenue streams and moves it further up the petrochemicals value chain. Conversely, Saudi Kayan has suffered severe delays in plant construction and we do not expect any sales or profits for the next few quarters. We do not have ratings on Yansab or PetroRabigh.

What do we think?

Stock	Rating	Price Target
SABIC	Overweight	SAR127.5
Sipchem	Overweight	SAR27.2 [#]
Saudi Kayan	Underweight	SAR15.5
Yansab	No rating	
Petro Rabigh	No rating	

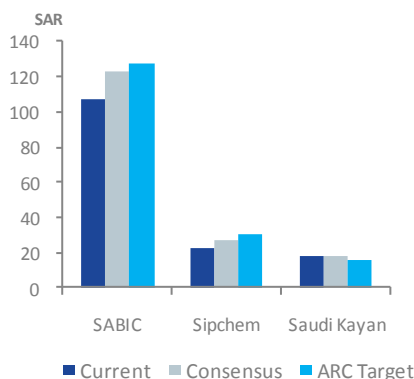
[#] Adjusted for the bonus issue dated 16 March 2011.

Why do we think it?

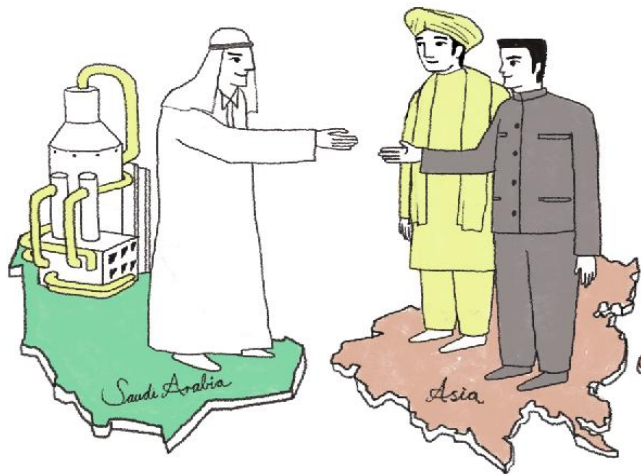
Stock	3 year EBITDA CAGR*	2010 EV/EBITDA
SABIC	10.6%	9.4x
Sipchem	24.3%	12.5x
Saudi Kayan	NA	NA
Yansab	18.3%	13.7x
Petro Rabigh	33.1%	19.2x

* 2010-2013, ie after strong cyclical recovery in 2009-10

Where are we versus consensus?



Source Bloomberg, Al Rajhi Capital



Saudi Petrochemicals Sector: Buoyed by uptrend in prices

We expect Saudi petrochemicals companies under our coverage to report robust results for Q1 2011, due to improved price realisations coupled with strong volume growth driven by demand from major markets like China and India. We have maintained our target prices for Sipchem (adjusted for bonus issue) and Kayan while marginally raising the target price for SABIC.

Petrochemicals prices continue to trend upwards. After dipping in Q3 2010, petrochemicals prices recovered in Q4 2010 primarily due to higher crude oil and natural gas prices. The prices further maintained the upward trend in Q1 2011 and were higher both on a sequential and on year-on-year basis. The combined average of Petrochemicals prices in Q1 2011 was up 20% on a year-on-year basis as against increase of 37% year-on-year for Brent crude in the same period. The oil prices rose mainly due to political crises in MENA region.

Increased oil production improves gas availability. According to industry sources, Saudi Arabia has increased its oil production (by 3.3% in Feb over Jan) in the wake of turmoil in Libya. Further, it plans to expand its oil rig count by about 28% in order to ensure adequate spare production capacity as the supply uncertainty persists. The higher oil production results in an increased associated gas production, which should partly alleviate fear of ethane shortage.

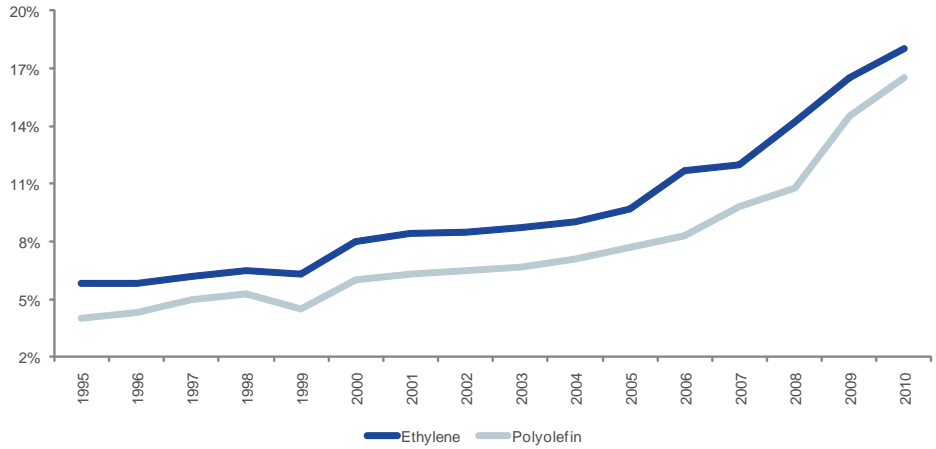
We expect robust earnings for Q1 2011. We expect the Saudi petrochemicals sector to record an aggregate 26.6% year-on-year increase in revenues in Q1 2011 primarily due to a year-on-year rebound in petrochemicals prices and the increased utilisation at the new units which were commissioned in 2010. We expect the EBITDA to grow by 21% to SAR15.6 bn. We forecast the net profit to increase by about 17.3% year-on-year to SAR7.0bn.

Conclusion: The crude oil prices continue to stay at elevated levels due to political unrest in the MENA region and improved economic scenario in the United States. We remain Overweight on SABIC and Sipchem and maintain our Underweight rating for Saudi Kayan. We have marginally raised our target price for SABIC to SAR127.5, implying 19% upside potential from the current levels.



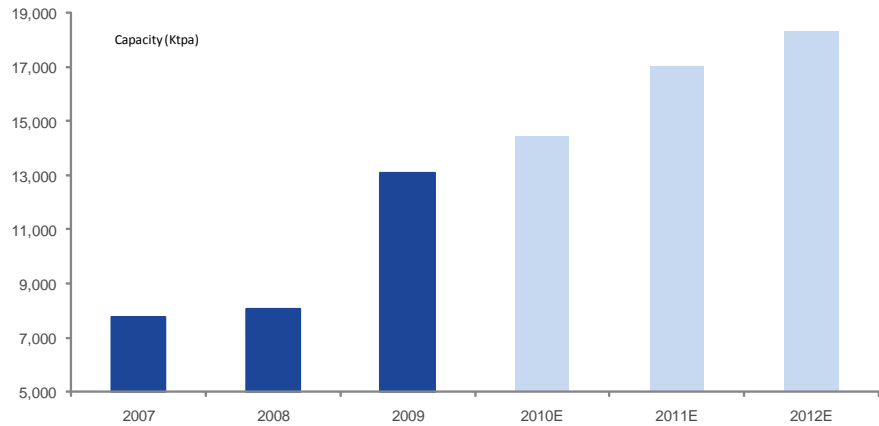
Middle East has seen rapid petrochemicals capacity growth since 2007

Figure 1. Share of Middle Eastern capacity in global petrochemicals production



Source: Industry data, Al Rajhi Capital

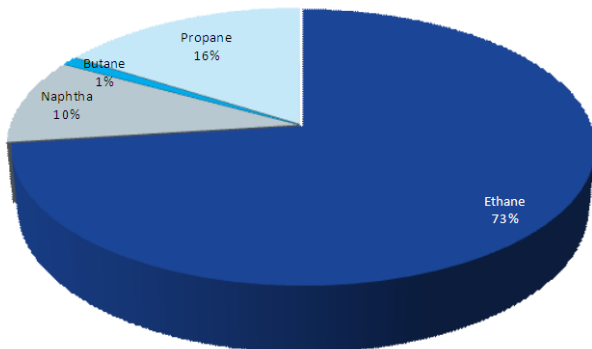
Figure 2. Saudi Arabia ethylene capacity



Source: Industry data, Al Rajhi Capital

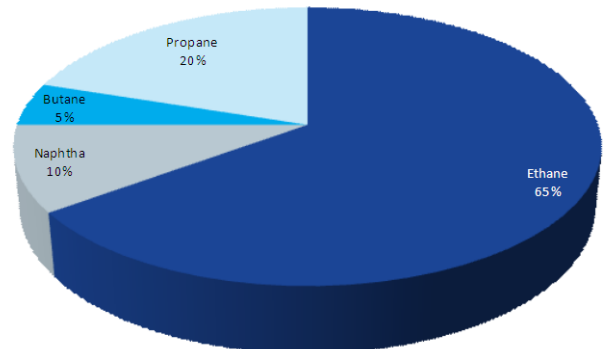
Saudi Arabia is leading capacity additions

Figure 3.1 Saudi Arabia: feedstock composition (2007)



Source: Industry data, Al Rajhi Capital

Figure 3.2 Saudi Arabia: feedstock composition (2014e)



Source: Industry data, Al Rajhi Capital



Saudi petrochemicals: Expansion continues

Capacity additions and
expansions in India

Petrochemicals prices
continued their upward
momentum in the quarter

We expect the Saudi petrochemicals sector to maintain its strong growth momentum in Q1 2011. We expect aggregate sector revenues to increase by 26.6% year-on-year in Q1 2011 due to a year-on-year rebound in petrochemicals prices and a moderate increase in volumes through the commissioning of new units. SABIC reportedly is in talks with Indian petrochemical players for a joint venture for cracker projects and downstream refineries. In January this year, Kayan sent its first shipment of acetone (1,600 tons) to India's markets. During the quarter, Saudi Kayan started the trial operations at its HDPE (0.4 mtpa) and Jubail polycarbonate (0.26 mtpa) plants (Source: Company's website). We estimate aggregate EBITDA of SAR15.63bn in Q1 2011, an increase of 21.1% on a year-on-year basis. We expect net profit to rise by 17.3% year-on-year to SAR7.08 bn.

The petrochemicals prices which recovered in Q4 2010 continued their upward momentum in Q1 2011, reflecting higher crude oil and natural gas prices. Average prices for basic petrochemicals products rose by about 25% year-on-year, by March end suggesting an improving market environment. Moreover, the prices of Ethylene, Propylene and Benzene have reached the levels last seen in 2008. The combined average of Ethylene, Propylene and Benzene in Q1 2011 was up 24.7% on a year-on-year basis.

Figure 4. Saudi PPC sector (Q1 performance analysis)

(SAR mn)	Q1 2010	Q1 2011E	% Chg
SABIC			
Revenues	34,126	42,152	23.5%
EBITDA	11,906	13,278	11.5%
EBITDA margin (%)	34.9%	31.5%	
Operating Profit	9,712	10,439	7.5%
Net Profit	5,432	5,905	8.7%
Yansab			
Revenues	689	2,120	207.8%
EBITDA	391	1,017	159.9%
EBITDA margin (%)	56.8%	48.0%	
Operating Profit	310	758	144.2%
Net Profit	259	638	145.8%
Saudi Kayan			
Revenues			
EBITDA			
EBITDA margin (%)			
Operating Profit	(3.7)	(4.1)	12.1%
Net Profit	(3.8)	(4.1)	9.3%
PetroRabigh			
Revenues	10,676	12,922	21.0%
EBITDA	447	926	107.2%
EBITDA margin (%)	4.2%	7.2%	
Operating Profit	(50)	410	n.a.
Net Profit	272	359	32.3%
Sipchem			
Revenues	306	800	161.9%
EBITDA	171	416	143.1%
EBITDA margin (%)	56.0%	52.0%	
Operating Profit	135	352	161.2%
Net Profit	81	189	132.6%
Aggregate			
Revenues	45,797	57,994	26.6%
EBITDA	12,916	15,638	21.1%
EBITDA margin (%)	28.2%	27.0%	
Operating Profit	10,104	11,954	18.3%
Net Profit	6,041	7,086	17.3%

Source: Company data, Al Rajhi Capital

We expect petrochemical
companies to post strong
results; on the back of
impressive growth in revenues



Further appreciation in the petrochemicals prices to drive growth in Q1

SABIC (Overweight)

We expect SABIC to report revenues of SAR42.15bn in Q1 2011 compared to SAR34.12bn in Q1 2010 driven by higher petrochemicals prices and a moderate increase in production volume. Our estimate for EBITDA is SAR13.27bn for Q1 2011 versus SAR11.90bn in the prior year quarter. We assume higher EBITDA due to growth in sales and additional profit from increasing petrochemicals prices. We expect the company to fully utilize its capacities for Q1 2011 consistent with the earlier quarter. We expect net profit to increase by about 8.7% on a year-on-year basis to SAR5.90bn, but by only 1.6% compared to the net profit of SAR5.81bn in Q4 2010. The substantial increase in revenues is not translating in to profit growth because of our higher assumptions of operating costs for 1Q 2011 in line with the last three quarters.

We have marginally raised our estimate of long-run fair value per share on a discounted economic profit (DEP) basis for SABIC by 1.2 %, from SAR126.0 to SAR127.5 reflecting an increase in overall Petrochemical prices and continued stronger demand from Asia. Based on our new target price, SABIC offers 19% upside from the closing price of SAR106.75 on 5th April.

Sipchem (Overweight)

We expect Sipchem to report revenues of about SAR800mn in Q1 2011 compared to SAR306mn in Q1 2010 primarily due to the additional revenue from the Phase 2 expansion. We expect EBITDA to surge from SAR171mn to SAR416mn due to increased revenue coupled with a higher gross margin. We forecast operating profit of SAR352mn compared to SAR135mn in the same period of 2010. On a year-on-year basis, we expect net profit to increase 133% to SAR189mn in Q1 2011 reflecting increasing revenues and gross margin.

As a part of the strategy to grow in downstream products, in full integration with current products portfolio, Sipchem plans to start production at ethyl acetate/butyl acetate plant (capacity of 0.1 mtpa) at its complex in Jubail during Q2 2013. In mid-December 2010, Sipchem announced that it intends to raise US\$400mn in Q1 2011 to finance its expansion project, of which around US\$100mn is due to be spent on the ethyl acetate plant.

On March 16 2011, Sipchem raised its share capital by 10% to SAR3.7bn from SAR3.3bn by issuing a bonus share for every 10 shares. We have maintained our target price at SAR27.2 (after adjusting for the bonus issue), which implies 21.2% upside from the current market price.

Saudi Kayan (Underweight)

We expect Saudi Kayan to report a net loss of SAR4.1mn for Q1 2011 as its plants are in pre-operational stage. Saudi Kayan started trial operations at its olefins plant at the end of July 2010, ethylene glycol and polypropylene plants in August 2010 and Jubail polycarbonate plant in March 2011. During the quarter, the Company also signed a SAR2bn murabaha facility agreement with Banque Saudi Fransi to cover the escalated construction costs. Currently we assume that the commercial production will not start until Q1 2012. We retain our Underweight rating on Saudi Kayan with a target price of SAR15.5.

Yansab (No rating)

Yansab launched commercial production in Q1 2010. We estimate Yansab's Q1 2011 revenues at SAR2.12bn and EBITDA at SAR1.01bn. We estimate operating profit at SAR758mn and net profit at SAR638mn (implying a net margin of 30.1%). On a quarter-on-quarter basis, we estimate revenue growth of 12% driven mainly by an increase in the capacity utilisation. Yansab has not specified the production unit's operating rates; however, we are estimating a cracker utilisation rate of about 95% for 2011 higher than our estimates for 2010.

PetroRabigh (No rating)

We expect PetroRabigh to report revenues of SAR12.92bn in Q1 2011, representing year-on-year growth of 21.0%. This reflects a year-on-year recovery in petrochemicals prices and growth in volumes. We estimate EBITDA of SAR926mn in Q1 2011 compared to EBITDA of SAR447mn in Q1 2010. We predict net profit of SAR359mn for Q1 compared to a net profit of SAR272mn in Q1 2010. We attribute the increase in the net result to the commissioning of units after Q4 2009.

Sipchem to start ethyl acetate production by Q2 2013

We expect commercial production to start from Q1 2012

Higher plant operating rates to propel Yansab's earnings

To invite tenders for second phase of construction in Q2

Disclaimer and additional disclosures for Equity Research

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Additional disclosures

1. Explanation of Al Rajhi Capital's rating system

Al Rajhi Capital uses a three-tier rating system based on absolute upside or downside potential for all stocks under its coverage except financial stocks and those few other companies not compliant with Islamic Shariah law:

"Overweight": Our target price is more than 15% above the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

"Neutral": We expect the share price to settle at a level between 5% below the current share price and 15% above the current share price on a 6-9 month time horizon.

"Underweight": Our target price is more than 5% below the current share price, and we expect the share price to reach the target on a 6-9 month time horizon.

2. Definitions

"Time horizon": Our analysts make recommendations on a 6-9 month time horizon. In other words, they expect a given stock to reach their target price within that time.

"Fair value": We estimate fair 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.

"Target price": This may be identical to estimated fair value per share, but is not necessarily the same. There may be very good reasons why a share price is unlikely to reach fair value within our time horizon. In such a case we set a target price which differs from estimated fair value per share, and explain our reasons for doing so.

Please note that the achievement of any price target may be impeded by general market and economic trends and other external factors, or if a company's profits or operating performance exceed or fall short of our expectations.

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