



US\$0.917bn Market cap	63.6% Free float	US\$2.925mn Avg. daily volume
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Target price	174.2	26.71% over current
Consensus price	120.0	-12.7% over current
Current price	137.5	as at 18/4/2011

Research Department
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Existing rating

Underweight Neutral **Overweight**

Saudi Ceramic

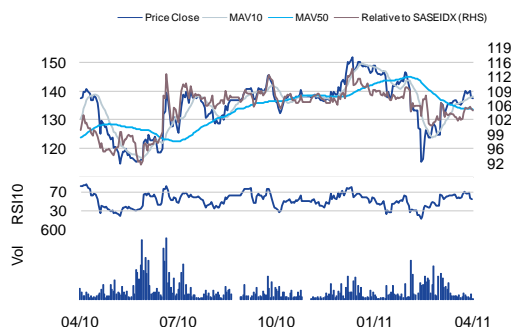
Q1: better than it looks

Flash view

Flash View is an analyst's preliminary interpretation of a results announcement or the impact of a major event. Our investment rating and earnings estimates are not being changed in this report. Any formal changes to our investment rating or earnings estimates will be made in a subsequent report, which may differ from the preliminary views expressed here.

Saudi Ceramics announced its Q1 preliminary results with robust top line growth of 14% year-year. We believe the major factor behind this growth is the utilization of the new tile plant. Contrary to our forecast, however, gross and net margins declined mainly due to prices decrease as well as the high interest costs. We view this decrease as temporary issue and expect margins to improve in the long run due to the expected change in product mix. Considering the full utilization of the fourth ceramic tile first commercial launch, strong growth in sales justifies the weak profit at this point. Therefore, we expect to marginally cut our forecasts but maintain our overweight rating.

Performance

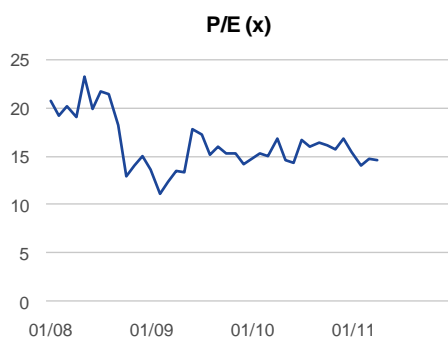


Earnings

Period End (SAR)	12/10A	12/11E	12/12E	12/13E
Revenue (mn)	1,080	1,259	1,420	1,539
Revenue Growth	12.7%	16.5%	12.8%	8.4%
EBITDA (mn)	318	373	441	481
EBITDA Growth	12.6%	17.4%	18.3%	8.9%
EPS	8.77	10.69	12.61	13.75
EPS Growth	11.2%	21.9%	18.0%	9.0%

Source: Company data, Al Rajhi Capital

Valuation



Source: Company data, Al Rajhi Capital

Earnings vs. our forecast	Above	In Line	Below
Likely impact:			
Earnings estimates	Up	No Change	Down
Dividend estimates	Up	No Change	Down
Recommendation	Upgrade	No Change	Downgrade
Long term view	Stronger	Confirmed	Weaker

- **Respectable revenue growth:** Saudi Ceramics revenue grew year-on-year by 14% to reach SAR306mn. Although it was below our forecasts of 19%, we believe that it is respectable given that some products' prices especially tiles were cut to boost sales volume. In other words, they concentrated on popular but low margin products to ensure large unit sales and low finished goods inventory levels. We further note that finished goods inventory levels reached one of its highest levels in Q4 2010 of 14% of sales.
- **Gross profit:** Gross profit increased by 11% y-o-y to reach SAR112mn. It was below our expectation of SAR123mn. As mentioned earlier, we believe that the product mix affected margins. Gross margin declined 2.6% y-o-y and was below our expectation by 4%. As much as we would've liked an improvement in margins, we find it justified by the increase in sales and the full utilization of the fourth ceramic tile first commercial launch. In our view, boosting sales and achieving full utilization of the new plant at this stage is more important than focusing on margins.
- **Net profit:** Bottom line results for Saudi Ceramics was disappointing, the 3% y-o-y growth was 18% below our expectation. We suspect that the amortization of the financing cost put pressure on net profit growth and thus we expect the net profit growth to be halted by these expenses in the coming quarters as well.
- **Conclusion:** We believe the major reason for the 14% y-y top line increase is the utilization of the first phase of the fourth ceramic tile plant. We suspect that the price decrease in some of the products mainly tiles squeezed margins. Also, high financial costs seem to have pressured bottom line. We expect to marginally cut our forecasts but maintain our overweight rating.



Corporate summary

Saudi Ceramic Company is one of the oldest and leading ceramics producers in the Middle East with a market value of around US\$1bn. The company manufactures and markets ceramic products such as ceramic tiles, sanitary ware (bathroom products) and road markers; in addition, the company manufactures water heaters. The company intends to launch production of red bricks by 2012.

Share information

Market cap (SAR/US\$) 3.438bn / 0.917bn
 52-week range 115.0 - 151.8
 Daily avg volume (US\$) 2.925mn
 Shares outstanding 25.00mn
 Free float (est.) 63.6%

Performance:	1M	3M	12M
Absolute	10%	-6.5%	0.4%
Relative to index	2.4%	-3.8%	5%

Major Shareholder:

General Social Insurance	15.9%
Saleh Abdulaziz Al Rajhi	14.3%

Source: Bloomberg, Al Rajhi Capital

Valuation

Period End	12/10A	12/11E	12/12E	12/13E
Revenue (SARmn)	1,080	1,259	1,420	1,539
EBITDA (SARmn)	318	373	441	481
Net Profit (SARmn)	219	267	315	344
EPS (SAR)	8.77	10.69	12.61	13.75
DPS (SAR)	3.50	4.60	5.98	7.77
EPS Growth	11.2%	21.9%	18.0%	9.0%
EV/EBITDA (x)	12.5	10.7	9.3	8.8
P/E (x)	15.7	12.9	10.9	10.0
P/B (x)	3.4	2.9	2.5	2.3
Dividend Yield	2.5%	3.3%	4.3%	5.7%

Source: Company data, Al Rajhi Capital



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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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