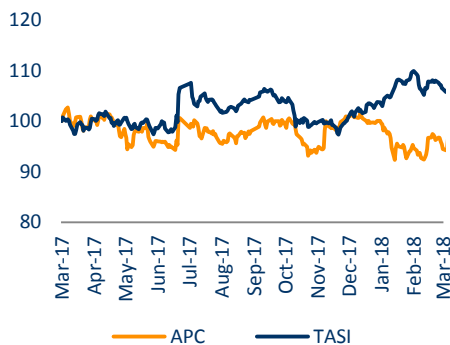



Initiation Coverage
March 22, 2018

Recommendation	Overweight
Current Price (SAR)	48.0
Target Price (SAR)	53.9
Upside/Downside (%)	12.2%

As of March 19, 2018
Key Data (Source: Bloomberg)

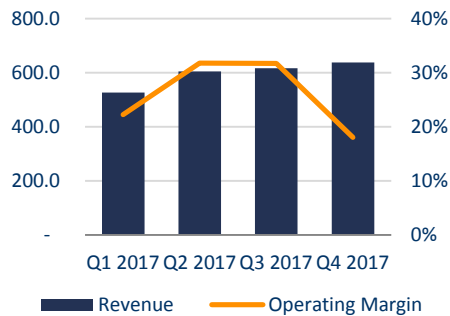
Market Cap (SAR bn)	9.4
52 Wk High (SAR)	48.75
52 Wk Low (SAR)	41.90
Total Outstanding shares (in mn)	197
Free Float (%)	93.2%

APC Vs TASI (Rebased)


Price Performance (%)	Absolute	Relative
1m	7.8%	4.7%
6m	4.3%	(0.7%)
12m	3.5%	(9.8%)

Major Shareholders (%)

Poly Propylene Holdings Co.	7.95%
General Organization for Social Insurance	6.37%

Quarterly Sales (SAR mn) and Operating Margin


Source: Bloomberg, Company Financials, FALCOM Research; Data as of 19th March 2018

In FY 2017, Advanced Petrochemicals Company (APC) reported revenues worth SAR 2.4bn, an 11.5% YoY increase, marginally short of consensus estimates of SAR 2.5bn. The rise in the revenues was mainly attributed to the higher average selling prices of Polypropylene (PP) although the sales volumes dropped 2.1% YoY to 498,277 metric tonnes for the year. During Q4 FY17, revenues grew 3.4% QoQ to SAR 637.5mn beating street expectations of SAR 598.0mn. However, gross profit slumped 31% QoQ to SAR 152.8mn impacted by the pressure on feedstock prices. Net income for Q4 FY17 stood at SAR 104mn; down 50.2% QoQ.

Strong free cash flows with over 100% utilization rates augur well for the future health of the company. In addition, the decision of the Saudi government to delay the implementation of subsidy removal program and the expected growth in demand for PP bode well for the company. APC currently trades at a 10.9% discount to its peers in terms of forward P/E multiple which gives a valuation comfort to the investors given its high dividend yield and operational efficiency. The stock has run up by 7.8% over the last one-month. Overall, we give an overweight rating to APC with a target price of SAR 53.9 per share.

Steady operational performance with an attractive dividend yield

Given the superior operational performance of APC historically, we are quietly confident that the company will continue to maintain its operating rates of over 100%. The business overall remains highly cash accretive with the FCF yield averaging 10.8% over the last five years. The balance sheet looks strong with ND/ EBITDA under 1.0x despite proposed capex of SAR 2.17bn in pygas/pyoil downstream project. The company distributed dividends of SAR 2.80 for FY 2017, with a pay-out ratio of 87%. We expect the company to maintain a pay-out ratio of ~80% in the coming years with an average dividend yield of 5.3%.

Rising PP prices, growing demand to drive top line

The increase in PP prices by 9.8% YoY during 2017 resulted in a positive revenue growth for the company. The growing global demand for PP which has a wide range of applications from auto motives to photography, drives the PP prices. As per the Chemical Economics Handbook (HIS), the demand for PP will increase 25% by 2022 from the current levels, driven by the economic growth in China and India. APC, which produces PP as its single end product will benefit from this trend and we expect revenues to grow at 2.7% CAGR from 2017-2021E.

Margins to improve as feedstock prices begin to ease

During Q4 2017, a 28% QoQ rise in the propane prices to an average of USD572/ton pulled down the net earnings for APC, however, we view the rise in the feedstock prices was partially due to short term supply disruptions from US due to hurricanes and seasonal winter heating demand. The prices have already started declining and stood at USD525/ton during February (down from USD590/ton in January). Consequently, APC's EBITDA margins are expected to improve by 1.3ppt to 35.3% in 2018E.

Delay in subsidy removal to push up industrial activity

KSA government has pushed back its target date for eliminating the budget deficit to 2023 from 2020 in anticipation to boost economic growth by driving the industrial activity. Consequently, the country has decelerated plans to eliminate subsidies on a wide range of energy products including propane which will now be gradually linked to international prices by 2020. The delay in phasing out of subsidies will ease the pressure on feedstock prices, which currently constitutes ~80% of the total cost of sales, thereby having a positive impact on APC's margins.

Valuation: We valued APC using the DCF Approach to arrive at a fair value of SAR 53.9 per share. We considered WACC at 8.2%, with a terminal growth rate of 2.0%.

	2017	2018E	2019E	2020E
Revenues (SAR bn)	2.4	2.5	2.6	2.6
Operating Profit (SAR bn)	0.6	0.7	0.7	0.7
EPS (SAR)	3.2	3.4	3.5	3.6
Operating Margin (%)	26.0%	27.4%	27.4%	27.4%
D/E (x)	0.32	0.31	0.29	0.27
RoE (%)	20.3%	20.4%	19.9%	19.0%
P/E (x)	14.3	14.0	13.6	13.5
Price/BV (x)	2.9	2.9	2.7	2.6
EV/EBITDA (x)	12.1	11.3	10.7	10.3

Source: Company Financials, FALCOM Research



Initiation Coverage

March 22, 2018

Valuation Summary

Explanation of valuation methodology and assumptions

We valued APC using the DCF Approach to arrive at a fair value of SAR 53.90 per share. We considered WACC at 8.2% with a terminal growth rate of 2.0%. In relative terms, APC is trading at 1yr forward P/E of 14.0x, at a discount of 10.9% to its sector peers and premium of 1.3% to the Tadawul All Share Index.

SAR Mn	FY 2017	FY 2018E	FY 2019E	FY 2020E	FY 2021E
EBIT	620	687	710	715	726
Taxes	(21)	(24)	(24)	(25)	(25)
Depreciation, amortization and impairment	192	198	209	220	231
Changes in working capital	43	(3)	11	19	17
Net capital expenditure	(180)	(201)	(207)	(209)	(212)
Free Cash Flow to firm	653	657	697	721	738
<i>Discount Factor</i>		0.9	0.9	0.8	0.7
PV of free cash flow to firm		618	606	579	547
Net Present Value (A)					2,350
Terminal Value					12,133
PV Terminal Value (B)					9,005
Assumed Terminal Growth Rate					2.0%
Discount Rate					8.2%
Enterprise Value (A+B)	11,355	WACC Assumptions			
Total Cash	260	Risk free rate	2.9%		
Total Debt	1,009	Equity Risk Premium	8.6%		
Minority Interest	-	Beta	0.8x		
Equity Value in SAR mn	10,607	Cost of equity	9.7%		
Number of shares in mn	197	Post tax cost of debt	3.5%		
Target Price in SAR per share	53.90	Weight of equity in capital structure	76.0%		
CMP in SAR as on March 19th, 2018	48.04	Weight of debt in capital structure	24.0%		
Upside/(Downside) to current market price	12.2%	WACC	8.2%		

Source: Company Financials, FALCOM Research Estimates

Risks

Upside Risks:

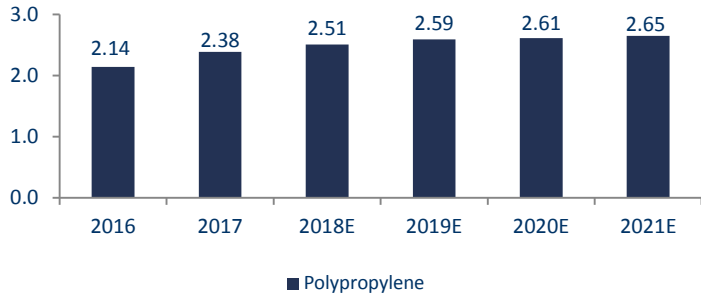
- Higher-than-expected product selling prices and lower feedstock costs can significantly increase top line and bottom line.
- A stronger KSA economy may boost government spending and provide company with additional subsidies.

Downside Risks

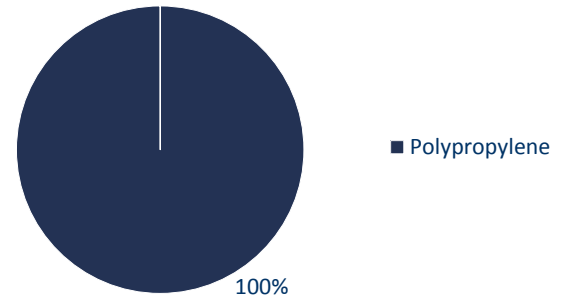
- As APC earnings are mostly dependent on a single PDH plant, its earnings are highly sensitive to the plant's operational performance.
- APC is heavily reliant on propane feedstock thus any decrease or elimination of feedstock discount is a key downside risk.
- Lower earnings from the Korean PDH JV.

Key Charts

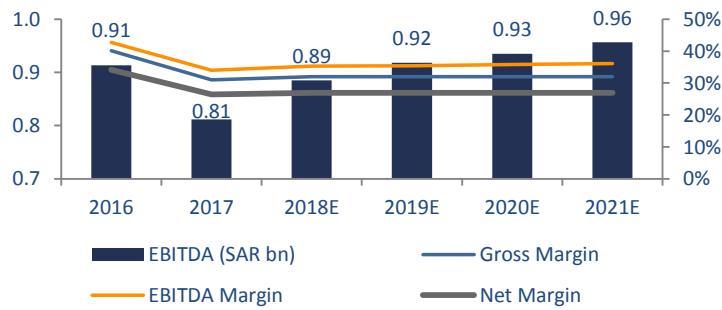
Revenue (SAR bn)



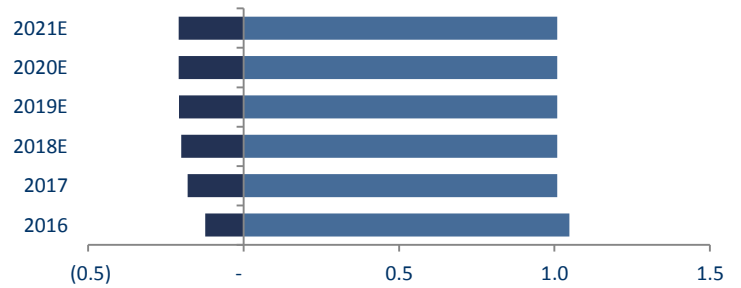
Revenue Split (2017)



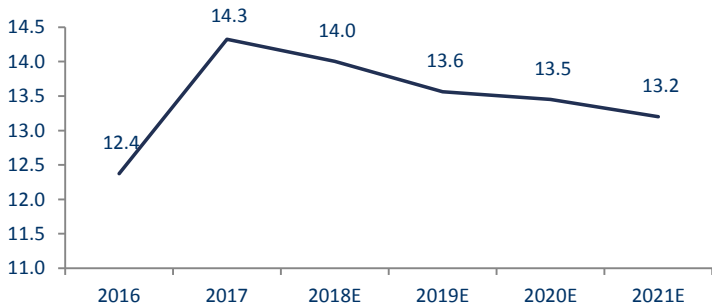
EBITDA & Margins



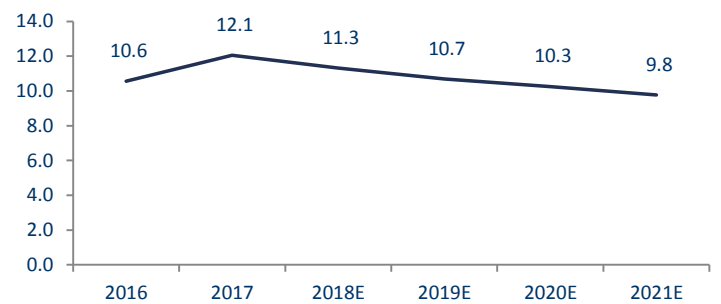
CAPEX and Debt



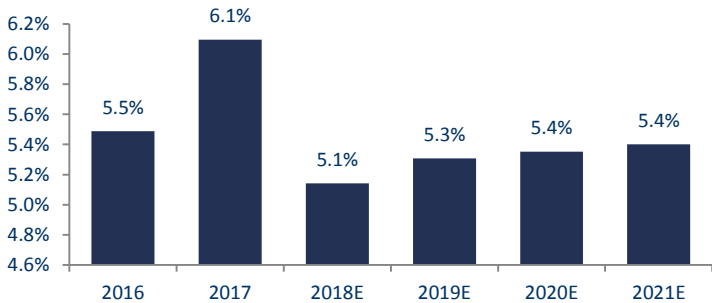
Price to Earnings



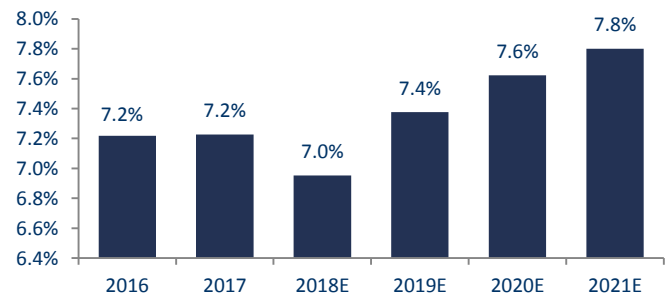
EV/EBITDA



Dividend Yield



Free Cash Flow Yield



Source: FALCOM Research Estimates



Initiation Coverage

March 22, 2018

Summary Financials

P&L (SAR mn)	2017	2018E	2019E	2020E
Revenue	2,385	2,509	2,590	2,610
Gross Profit	738	803	829	835
EBITDA	812	885	918	935
EBIT	620	687	710	715
Earnings from Associates	48	48	49	49
Finance Expense	(37)	(37)	(37)	(37)
Other	21	-	-	-
PBT	652	699	721	727
Minorities	-	-	-	-
Zakat	(21)	(24)	(24)	(25)
Net Income	631	675	697	703
EPS	3.21	3.43	3.54	3.57
DPS	3.21	3.43	3.54	3.57
BS (SAR mn)	2017	2018E	2019E	2020E
Cash and cash equivalents	260	443	650	877
Current Assets (excluding cash)	981	968	956	933
Fixed assets	1,957	1,960	1,959	1,948
Intangibles	3	3	3	3
Investments in associates and JVs	1,196	1,196	1,196	1,196
Other assets	155	155	155	155
Total Assets	4,552	4,725	4,919	5,112
Current Liabilities	327	311	310	306
Short Term Debt	10	10	10	10
Long Term Debt	999	999	999	999
Other liabilities	103	103	103	103
Shareholders Equities	3,113	3,302	3,498	3,694
Total Liabilities	4,552	4,725	4,919	5,112
CF (SAR mn)	2017	2018E	2019E	2020E
Operating Cash Flow	804	873	906	923
Working Capital Changes	43	(3)	11	19
Cash Flow from Operating Activities	846	869	916	942
Capex	(180)	(201)	(207)	(209)
Cash Flow from Investing Activities	(448)	(201)	(207)	(209)
Changes in Debt	(40)	-	-	-
Dividends	(551)	(486)	(502)	(506)
Cash Flow from Financing Activities	(591)	(486)	(502)	(506)

Source: Bloomberg, Company Financials, FALCOM Research

Growth	2017	2018E	2019E	2020E
Revenue	11.5%	5.2%	3.2%	0.8%
EBITDA	(11.2%)	9.0%	3.8%	1.8%
Operating profit	(14.9%)	10.9%	3.2%	0.8%
PBT	(13.6%)	7.2%	3.3%	0.8%
Net Income	(13.8%)	7.0%	3.3%	0.8%

Ratios (%)	2017	2018E	2019E	2020E
Gross Margin	31.0%	32.0%	32.0%	32.0%
EBITDA Margin	34.0%	35.3%	35.5%	35.8%
EBIT Margin	26.0%	27.4%	27.4%	27.4%
Net Margin	26.5%	26.9%	26.9%	26.9%
ROE	20.3%	20.4%	19.9%	19.0%
ROCE	15.0%	15.3%	15.2%	14.7%
ROA	13.9%	14.3%	14.2%	13.7%
Debt/Equity	0.32x	0.31x	0.29x	0.27x
Net Debt/EBITDA	0.9x	0.6x	0.4x	0.1x
FCF Yield	7.2%	7.0%	7.4%	7.6%
Dividend Yield	6.1%	5.1%	5.3%	5.4%

Valuation	2017	2018E	2019E	2020E
PE	14.3x	14.0x	13.6x	13.5x
PB	2.9x	2.9x	2.7x	2.6x
EV/EBITDA	12.1x	11.3x	10.7x	10.2x
EV/EBIT	15.8x	14.6x	13.8x	13.4x
EV/Sales	4.1x	4.0x	3.8x	3.7x

Peer Valuations	12M Fwd PE	12m Fwd EV/EBITDA
Saudi Kayan Petrochemical	16.0x	8.6x
Yanbu National Petrochemicals	15.7x	10.6x
Saudi Arabia Fertilizers	22.3x	16.7x
Saudi Basic Industries	15.3x	7.9x
National Industrialization Company	19.6x	14.9x
Saudi Industrial Investment Group	10.2x	8.5x
National Petrochemical Company	15.3x	9.4x
Advanced Petrochemical Company	14.0x	11.3x
Sector Median	15.7x	9.4x
TASI	13.8x	11.6x



FALCOM Rating Methodology

FALCOM Financial Services uses its own evaluation structure, and its recommendations are based on quantitative and qualitative data collected by the analysts. Moreover, the evaluation system places covered shares under one of the next recommendation areas based on the closing price of the market, the fair value that we set and the possibility of ascent/descent.

Overweight: The Target share price exceeds the current share price by $\geq 10\%$.

Neutral: The Target share price is either more or less than the current share price by 10%.

Underweight: The Target share price is less than the current share price by $\geq 10\%$.

To be Revised: No target price had been set for one or more of the following reasons: (1) waiting for more analysis, (2) waiting for detailed financials, (3) waiting for more data to be updated, (4) major change in company's performance, (5) change in market conditions or (6) any other reason from FALCOM Financial Services.

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