FALCOM

# Saudi Cement Co.

Materials | SACCO AB | 3030.SE

INTELLIGENT INVESTMENT IDEAS

## 1Q 2018 Results Update

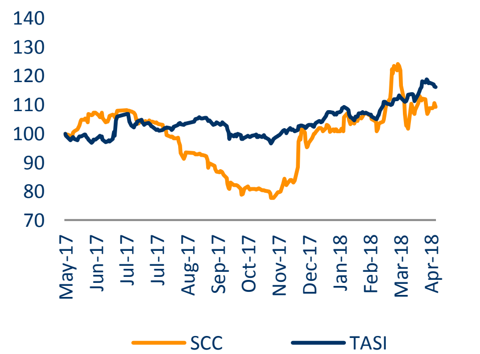
May 07, 2018

| Recommendation | Neutral |
|---|---|
| Previous Recommendation | Neutral |
| Current Price (SAR) | 51.0 |
| Target Price (SAR) | 54.1 |
| Upside/Downside (%) | 6.1% |

*As of May 07th 2018*

| Key Data (Source: Bloomberg) | |
|---|---|
| Market Cap (SAR bn) | 7.8 |
| 52 Wk High (SAR) | 60.40 |
| 52 Wk Low (SAR) | 37.20 |
| Total Outstanding shares (in mn) | 153.0 |
| Free Float (%) | 89.1% |

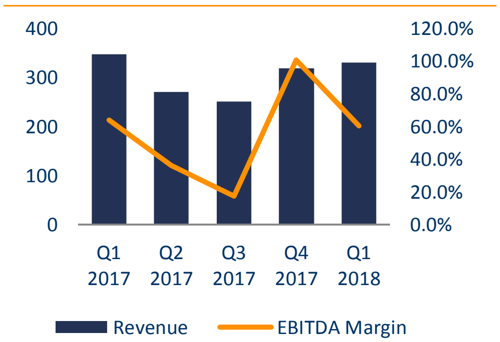
**SCC vs. TASI (Rebased)**




| Price Performance (%) | Absolute | Relative |
|---|---|---|
| 1m | 2.2% | (2.3%) |
| 6m | 35.2% | 18.2% |
| 12m | 9.2% | (6.8%) |

| Major Shareholders (%) | |
|---|---|
| Khaled Abdulrahman Saleh Al Rajhi | 8.02 |
| Public Pension Agency | 5.62 |
| General Organization for Social Insurance | 5.22 |

**Quarterly Sales (SAR mn) and EBITDA Margin**




*Source: Bloomberg, Company Financials, FALCOM Research; Data as of 07th May 2018*

**Weak demand and higher costs impacted 1Q18 profitability**

Saudi Cement's (SCC) 1Q18 revenue declined 4% Y/Y to SAR 330mn, driven by weak demand, despite improved selling prices. Increase in cost of sales per ton, driven by production cuts by SCC resulted in 11% Y/Y decline in gross profits. Further, the increase in finance charges, decline in other income and share of associate's profits weighed on net profits (-14% Y/Y to SAR142mn). During the quarter, KSA resumed cement exports to Bahrain (60,000 tons exported from mid-March to mid-April). We expect the development to support the export demand for SCC, given its geographical proximity.

Sequentially SCC's net profits rose 32% Q/Q driven by higher sales (improved demand and better price realization), lower production costs per ton, drop in selling and general expenses and increase in the share of associate's income. We believe the company's earnings will be driven by improved capacity utilization, given the moderate recovery in regional demand and resumption of exports. However, higher costs per ton would remain a challenge given current oversupply in the market. Overall, we project a high single-digit top-line expansion, while margins will continue to remain under pressure in 2018.

- SCC's top line declined -4.6% Y/Y to SAR 330mn in Q1 2018, driven by decline in the dispatches (-1.4% Y/Y excluding exports in the previous year to 1.45m tons), despite 3% Y/Y improvement in sales price. For the Eastern Region, the demand seems to be stabilizing with lesser decline than the sector average (3.3% Q/Q, -2.7% Y/Y), while Saudi being the largest regional player has seen positive impact from this trend.
- Gross profit declined 11.4% Y/Y to SAR 169mn, driven by a 3.8% Y/Y increase in the cost of sales. The costs per ton grew 13% Y/Y as SCC curtailed its production to lower its high inventory-to-LTM sales ratio (97% vs. peer average of 79%). Subsequently, the gross margins dipped 400bps to 51.2% in Q1 2018.
- SCC's operating income dropped in-line with gross profits by 11.8% Y/Y to SAR 148mn (Q1 2017: SAR 168mn). The operating margin dipped 370bps to 44.9% in Q1 2018. During the quarter, the company witnessed margin erosion due to lower capacity utilization.
- SCC's EBITDA for the quarter stood at SAR 199mn vis-à-vis SAR 221mn in Q1 2017, a 9.9% Y/Y decline, driven by lower operational efficiencies and higher costs. The EBITDA margin declined 350bps to 60.2% in Q1 2018.
- Net profit for the period stood at SAR 142mn (-4% Y/Y, +32% Q/Q), led by lower sales volumes and higher operating expenses and finance costs. Net profit margin, as of Q1 2018, stood at 43.0% compared to 47.6% in Q1 2017.
- SCC's cash flow from operating activities declined 59.5% Y/Y to SAR 95mn in Q1 2018 (Q1 2017: SAR 234mn) due to an increase in trade receivables.
- Saudi Arabia's cement sector is expected witness moderate demand revival from the complete lifting of exports tariffs in 2018, while excess inventory and high competition will keep the prices under check. We expect the exports to Bahrain and demand from Jubail project to relieve some of SCC's high inventory levels, while elevated costs per ton will keep the margins under pressure. We maintain a "Neutral" stance on SCC until we witness concrete signs of demand upturn and price stabilization over the coming quarters.

**Valuation:** We have revised our target price slightly upwards with a fair value of SAR 54.1 per share, post incorporating 1Q18 performance in our forecasts. We maintain our "Neutral" rating on the stock.

| | 1Q'18 | 1Q'17 | % YoY | FY18E | FY17 | % YoY |
|---|---|---|---|---|---|---|
| Revenues (SAR mn) | 330.5 | 346.4 | (4.6%) | 1,279.0 | 1,184.5 | 8.0% |
| Gross Profit (SAR mn) | 169.3 | 191.2 | (11.4%) | 580.6 | 568.8 | 2.1% |
| EBITDA (SAR mn) | 199.0 | 220.8 | (9.9%) | 666.0 | 681.8 | (2.3%) |
| Net Profit (SAR mn) | 142.2 | 164.7 | (13.6%) | 455.1 | 453.4 | 0.4% |
| EPS basic (SAR) | 0.93 | 1.08 | (13.6%) | 2.97 | 2.96 | 0.4% |
| Gross Margin (%) | 51.2% | 55.2% | (4.0%) | 45.4% | 48.0% | (2.6%) |
| EBITDA Margin (%) | 60.2% | 63.8% | (3.5%) | 52.1% | 57.6% | (5.5%) |
| Net Profit Margin (%) | 43.0% | 47.6% | (4.5%) | 35.6% | 38.3% | (2.7%) |

*Source: Company Financials, FALCOM Research*

## 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 ≥ 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 ≥ 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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