

3Q19 Results Update

November 10, 2019

| Recommendation | Overweight |
|-------------------------|------------|
| Previous Recommendation | Overweight |
| Current Price (SAR) | 10.5 |
| Target Price (SAR) | 12.0 |
| Upside/Downside (%) | 14.1% |

As of November 10th, 2019

Key Data (Source: Bloomberg)

| | |
|----------------------------------|-------|
| Market Cap (SAR bn) | 15.8 |
| 52 Wk High (SAR) | 14.9 |
| 52 Wk Low (SAR) | 9.6 |
| Total Outstanding Shares (in mn) | 1,500 |
| Free Float (%) | 65.0% |

SAUDI KAYAN vs. TASI (Rebased)



| Price Performance (%) | Absolute | Relative |
|-----------------------|----------|----------|
| 1m | 1.0% | 3.8% |
| 6m | (18.8%) | (4.4%) |
| 12m | (31.8%) | (30.9%) |

Major Shareholders (%)

| | |
|----------------------------|-------|
| Saudi Basic Industries Co. | 35.0% |
|----------------------------|-------|

Revenue (SAR bn) and Operating Profit Margin (%)



Source: Bloomberg, Company Financials, FALCOM Research; Data as of 10th November 2019

Kayan's return to profitability surprises street analysts

Kayan's revenues declined 31.8% YoY and 5.2% QoQ to SAR 2,303.2mn in 3Q19, largely impacted by lower average selling prices. Consequently, gross profit also contracted 59.6% YoY to SAR 375.4mn. On the other hand, gross profit improved 95.0% QoQ owing to a decline in cost of sales as a result of the reduced feedstock cost. Operating income fell 73.6% YoY to SAR 201.2mn, mainly due to increased selling, general, and administrative expenses. The company recorded a profit of SAR 1.3mn against a loss of SAR 273.1mn in 2Q19, surpassing consensus estimates of a loss of SAR 142.83mn.

A surprise drops in feedstock prices, higher sales volumes, production efficiency, and lower financing charges were responsible for the company's return to profitability in 3Q19, after reporting three straight quarters of losses. Though feedstock prices are expected to rise in the coming quarters resulting in lower the margin spreads of products, Kayan's focus on generating positive cash and minimizing its existing debts is likely to benefit the company' bottom line growth. The company saw the positive impact of debt-reducing measures implemented in the earlier quarter, which helped to substantially lower its finance cost as a result of lower Sibor rates. Kayan also aims to enhance financial competency by repaying and restructuring its remaining secondary debts. We, therefore, maintain our "Overweight" rating on the stock.

- Kayan's revenue declined 31.8% YoY to SAR 2,303.2mn in 3Q19 due to the decreased average selling price of products. Revenue slipped 5.2% QoQ despite a rise in volumetric sales.
- Gross profit fell 59.6% YoY to SAR 375.4mn even though the average cost of feedstock declined. Consequently, its gross margin narrowed to 16.3% in 3Q19 compared to 27.5% in the same quarter a year ago. Gross profit, however, jumped 95.0% QoQ.
- Operating income plunged 73.6% YoY to SAR 201.2mn in 3Q19 due to higher selling, general, and administrative expense, resulting in contraction in the operating margin to 8.7% in 3Q19 from 22.6% in 3Q18.
- EBITDA for the quarter fell 40.8% to SAR 792.7mn vis-à-vis SAR 1,339.5mn in 3Q18. Consequently, EBITDA margins stood at 34.4% in 3Q19.
- Kayan's net profit plummeted to SAR 1.3mn in 3Q19 from SAR 471.9mn in 3Q18. However, it recorded profit for the first time over the last three quarters, which can be ascribed to a decrease in financing costs, following the implementation of the company strategy to reduce financing expense, and a slump in feedstock prices. The net profit margin came in at 0.1% for 3Q19 vis-à-vis the net loss margin of 11.2% in 2Q19, while it had posted a net profit margin of 14.0% in 3Q18.

Valuation: We revise our target price downward to a fair value of SAR 12.0 per share. We maintain our "Overweight" rating on the stock.

| | 3Q'19 | 3Q'18 | % YoY | FY19E | FY18 | % YoY |
|-----------------------|-------|-------|---------|--------|--------|---------|
| Revenues (SAR mn) | 2,303 | 3,376 | (31.8%) | 9,699 | 12,263 | (20.9%) |
| Gross Profit (SAR mn) | 375 | 929 | (59.6%) | 1,164 | 3,365 | (65.4%) |
| EBITDA (SAR mn) | 793 | 1,340 | (40.8%) | 2,885 | 4,933 | (41.5%) |
| Net Profit (SAR mn) | 1 | 472 | (99.7%) | (454) | 1,702 | NM |
| EPS Basic (SAR) | 0.00 | 0.31 | (99.7%) | (0.30) | 1.13 | NM |
| Gross Margin (%) | 16.3% | 27.5% | (11.2%) | 12.0% | 27.4% | (15.4%) |
| EBITDA Margin (%) | 34.4% | 39.7% | (5.3%) | 29.7% | 40.2% | (10.5%) |
| Net Profit Margin (%) | 0.1% | 14.0% | (13.9%) | (4.7%) | 13.9% | (18.6%) |

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 $\geq 10\%$.

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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