Target Price: SAR11.50/share
Market price: SAR9.54/share
Upside: +21%
Rating: Overweight

Saudi Kayan Petrochemical Co. - Kayan

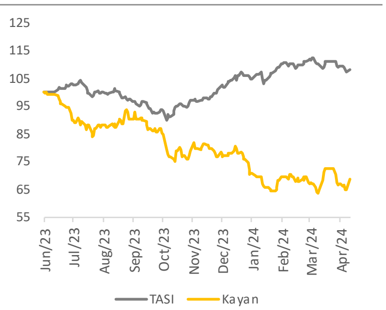
1Q24 earnings in line; TP set at SAR11.5 on revised outlook

- In line 1Q24 operating performance, aided by price recovery and lower OPEX, offsetting a 9% q/q decline in sales volume.
- PC and MEG near-term market fundamentals remain weak, due to lower demand and excess supply, although the downside to prices seems limited.
- Despite in-line earnings, we revise our TP to SAR11.5/sh. (SAR14.0/sh earlier) based on DCF valuation to reflect the revised market outlook but remain Overweight on the stock.

Stock data	
TASI ticker	2350
Mcap (SARmn)	14,310
Avg. Trd. Val (SARmn)	34.9
Free Float	65.0%
QFI Holding	9.8%
TASI FF weight	0.40%

Source: Bloomberg

Prices indexed to 100



Source: Bloomberg

1Q24 results: Top-line declined by 7.7% q/q to SAR1,976mn (GIBCe: SAR2,212mn), mainly due to lower sales volume (-9% q/q), offsetting an improvement in average product prices (+2% q/q). We note that lower sales volume during the quarter could be due to slower ramping up of production at the Bisphenol plant (key feedstock for PC), coupled with ongoing Red Sea conflict. Nonetheless, as expected, relatively higher feedstock prices (mainly Butane) amid a high fixed-cost structure continued to impact the performance with the company incurring gross and operating losses (in-line aided by lower OPEX) for the seventh consecutive quarter. In addition, higher financial charges further deepened losses. Overall, Kayan reported a net loss of SAR572mn, largely in line our estimate (consensus: SAR512mn loss).

Market outlook: MEG (40% of revenues) and PC (10%) prices remained flat q/q, while Polymer prices (PP, HDPE, LDPE) rose 2-8% q/q in 1Q24. Going forward, despite rising crude oil prices and a positive economic data in China, we expect MEG and PC market fundamental to remain mostly weak in the near term, mainly due to i) lower demand in the end markets, particularly in China's housing sector, ii) ample supply. We note that China's PC import (-26% y/y; Figure 4) reached its lowest level in a decade in 2023, while MEG inventory in China, after witnessing a decline over Nov 2023 – Mar 2024, have started rising again (+23% from early March 2024; Figure 5), keeping product prices under check in the near-term. Nonetheless, we expect Polymer prices to continue improve gradually this year. Further, Butane prices are down by ~5% q/q in 2Q24 but still remain relatively high level at US$585/t, keeping spreads lower than the historical level. Nonetheless, we believe product prices and spreads are mostly bottomed out (Figure 3) and may recover later this year, aided by easing economic concerns, better demand from the end industries, high input costs, and rationalization of capacity expansion.

Figure 1: Key financial metrics

SARmn	2022a	2023a	2024e	2025e
Revenue	11,157	8,171	9,015	9,957
Revenue growth	*-12%*	*-27%*	*10%*	*10%*
Gross Profit	(97)	(846)	(407)	348
Gross Profit margin	*-1%*	*-10%*	*-5%*	*3%*
EBITDA	1,543	1,014	1,391	1,913
Op. income	(857)	(1,446)	(976)	(240)
Net profit	(1,244)	(2,136)	(1,702)	(874)
Net profit margin	*-11%*	*-26%*	*-19%*	*-9%*
EPS (SAR)	(0.8)	(1.4)	(1.1)	(0.6)
P/E	NM	NM	NM	NM

Source: Company data, GIB Capital.

Kunal Doshi
+966-11-834 8372
Kunal.doshi@gibcapital.com

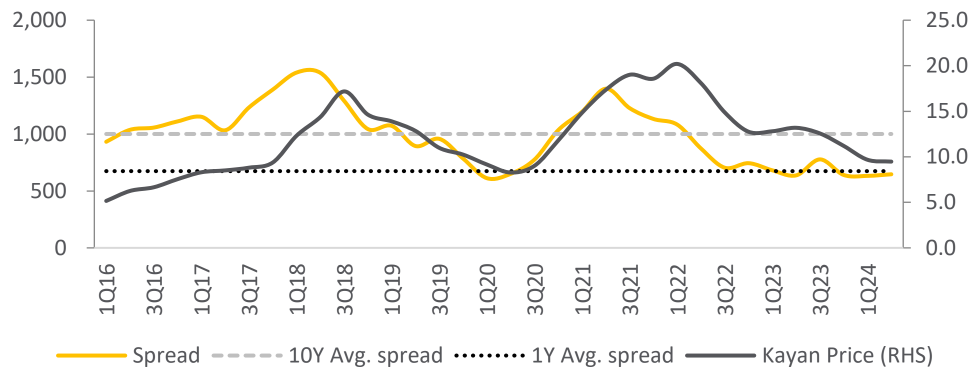
Abdulaziz Alawwad
+966-11-834 8486
Abdulaziz.alawwad@gibcapital.com

Figure 2: 1Q24 results summary

SARmn	1Q24	1Q23	y/y %	4Q23	q/q %	GIBC est.	Variance %
Revenues	**1,976**	**1,683**	**17.4%**	**2,142**	**-7.7%**	**2,212**	**-10.7%**
Cost of sales	2,251	2,022	11.3%	2,413	-6.7%	2,449	-8.1%
Gross profit	**(275)**	**(339)**	**19.0%**	**(271)**	**-1.4%**	**(237)**	**-15.8%**
Opex	119	155	-23.6%	174	-31.9%	153	-22.3%
Operating profit	**(393)**	**(495)**	**20.5%**	**(445)**	**11.6%**	**(390)**	**-0.9%**
Net income	**(572)**	**(673)**	**15.1%**	**(622)**	**8.1%**	**(574)**	**0.4%**
Gross margin	-13.9%	-20.2%		-12.7%		-10.7%	
Operating margin	-19.9%	-29.4%		-20.8%		-17.6%	
Net margin	-28.9%	-40.0%		-29.0%		-26.0%	

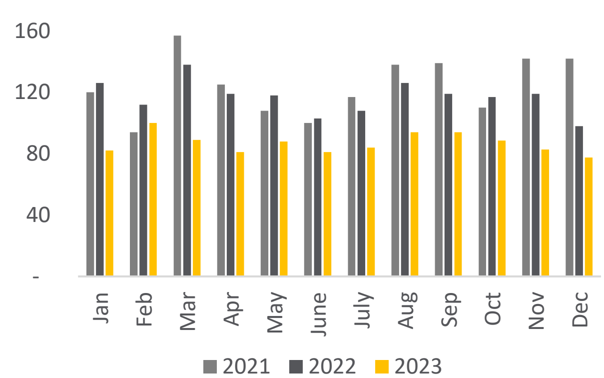
Source: Company data, GIB Capital

Figure 3: Weighted average Kayan's spreads (US$/t) vs. average stock price (SAR)



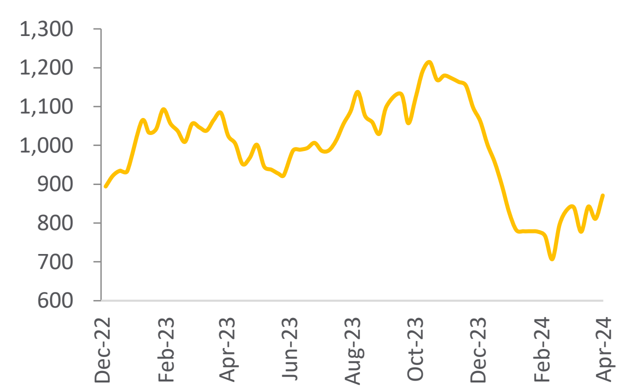
Source: Company data, Bloomberg, GIB Capital.

Figure 4: China's PC imports trend ('000 tonnes)



Source: ICIS, GIB Capital

Figure 5: East China MEG inventories ('000 tonnes)



Source: ICIS, GIB Capital

Valuation and risks: Given the weak market dynamics for PC and MEG products, we cut our total sales volume and avg. products price forecasts by ~3% and ~2%, respectively for 2024-25e, resulting in a 5% downward revision in our top-line estimate. Nonetheless, we continue to expect an improvement in Kayan's operating performance over the medium term, aided by a gradual recovery in demand, improvement in spreads, better efficiencies, and its efforts in deleveraging the balance sheet. Accordingly, we revise our TP to SAR11.5/sh. (SAR14.0/sh. earlier) based on DCF valuation (9.6% WACC; unchanged). The stock price has corrected over 30% from its 52-week high, implying all negative fundamentals are priced in. Hence, we remain Overweight on the stock. Economic slowdown, lower-than-expected product spreads, the unexpected change in subsidized feedstock prices, unplanned shutdown, and persistently high interest rates act as downside risks to our valuation.

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Contact us for queries:

Sell Side Research Department,
GIB Capital,
B1, Granada Business & Residential Park,
Eastern Ring Road, PO Box 89589, Riyadh 11692
www.gibcapital.com