

**Advanced Petrochemicals Co. (2330.SE)**
**OVERWEIGHT**

<b>CMP Target Upside</b>	<b>SAR 22.85 SAR 30.06 31.6%</b>
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MSCI GCC Index	425.62
Tadawul All Share Index	6,465.69

**Key Stock Data**

Sector	Petrochemical
Reuters Code	2330.SE
Bloomberg Code	APPC AB Equity
Net Out. Shares (bn)	0.141
Market Cap (SAR bn)	3.230
Market Cap (USD bn)	0.863
Avg. 12m Vol. (mn)	1.525
Volatility (30 day)	16.163
Volatility (180 day)	29.338

**Stock Performance (%)**

52 week high / low (SAR)	28.60/ 13.90		
	1M	3M	12M
Absolute (%)	-5.2	-7.7	48.4
Relative (%)	-7.4	-10.0	4.2

**Shareholding Pattern (%)**

IDB Infrastructure Fund	8.90
National Polypropylene Co.	7.90
Public	83.20

**APC and Tadawul All Share Index**

**Quarterly Result Update**

- APC's top-line remained almost flat at SAR 1,467 million during FY09, which was 5.2% higher than our estimate.
- Net profit declined 39.5% to SAR 127 million during the year, which was 20.6% lower than our estimate on higher than expected operating costs.
- We have increased our 2010E sales by 10.0% on account of improving demand and price scenario for polypropylene. However, net profit estimate has been revised upward by only 3.2%, considering higher operating costs.
- We are reiterating our earlier OVERWEIGHT recommendation with a revised DCF target price of SAR 30.06, implying an upside of 31.6%.

**Overview**

SAR Million	2008A	2009A	2010E	2011E	2012E
Sales	1,459	1,467	2,107	2,547	2,671
EBITDA	366	357	497	594	617
EBITDA Margin	25.1%	24.3%	23.6%	23.3%	23.1%
Net Profit	210	127	288	386	407
Net Profit Margin	14.4%	8.7%	13.7%	15.1%	15.2%
Adjusted EPS (SAR)	1.49	0.90	2.04	2.73	2.88
Total Assets	3,507	3,414	3,489	3,551	3,549
RoAE	13.9%	7.7%	16.7%	20.6%	20.0%

**Operating Revenues**

Advanced Petrochemicals Co.'s (APC) revenues increased to SAR 1,467 million in 2009 from 1,459 million in 2008, mainly on account of higher volumes.

**Costs and operating expenses**

Cost of sales (CoS), including depreciation and amortisation, increased 5.9% to SAR 1,249 million from SAR 1,180 million which, as a percentage of revenues, was up 430 bps to 85.1%. Sales and distribution expenses jumped 83.1% to SAR 30.28 million and, as a percentage of revenues, almost doubled to 2.1%. General and administration expenses increased 65.4% to SAR 14.70 million. Overall, total expenses increased 7.4% to SAR 1,294 million from SAR 1,205 million in 2008. Furthermore, the company incurred finance charges of SAR 47.83 million compared to SAR 48.34 million a year earlier, due to a decline in the average cost of funds and lower outstanding debt.

**Profitability**

APC reported a 31.9% decline in operating profit to SAR 172.94 million from SAR 254.09 million, as a result of higher operating expenses. The company's operating margin fell 562 basis points to 11.8% during the year. Other income more than halved to SAR 2.01 million from SAR 4.40 million in 2008. Consequently, the company's net income plunged 39.5% to SAR 127.12 million from SAR 210.15 million in 2008. Net margin stood at 8.7% as against 14.4% in the previous year. Adjusted EPS declined to SAR 0.90 from SAR 1.49 during 2008.

## Peer Comparison

We have considered Saudi International Petrochemical Co. (SIPCHEM) and Saudi Industrial Investment Group (SIIG) for a peer comparison of companies in the GCC.

Financial Performance of Comparable Companies						
	SIPCHEM		SIIG		APC	
	2008	2009	2008	2009	2008	2009
<b>(SAR Million)</b>						
Sales	1,709	830	2,139	3,760	1,459	1,467
YoY change	11.8%	-51.4%	46.6%	75.8%	NA	0.5%
EBITDA	954	168	168	560	366	357
YoY change	5.3%	-82.4%	-64.6%	233.4%	NA	-2.4%
Net Profit	537	141	49	285	210	127
YoY change	-9.6%	-73.8%	-88.9%	484.5%	NA	-39.5%
Total Assets	10,833	11,831	8,649	19,675	3,507	3,414
YoY change	39.8%	9.2%	74.2%	127.5%	37.8%	-2.7%
Shareholders' Equity	4,965	4,922	5,197	5,482	1,617	1,670
YoY change	65.7%	-0.9%	66.3%	5.5%	14.2%	3.3%
<b>Ratios:</b>						
Total Assets Turnover Ratio (x)	0.18	0.07	0.31	0.27	0.48	0.42
EBITDA Margin	55.9%	20.3%	7.9%	14.9%	25.1%	24.3%
Net Profit Margin	31.4%	17.0%	2.3%	7.6%	14.4%	8.7%
RoAE	13.5%	2.8%	1.2%	5.3%	13.9%	7.7%
RoAA	5.8%	1.2%	0.7%	2.0%	6.9%	3.7%
<b>Market Indicators:</b>						
Adj. EPS (SAR)	1.61	0.42	0.11	0.63	1.49	0.90
P/E (x)	14.16	53.95	203.07	34.74	15.37	25.41
Adj. BVPS (SAR)	14.89	14.77	11.55	12.18	11.44	11.82
P/BV (x)	1.53	1.54	1.90	1.81	2.00	1.93
Current Market Capitalisation (SAR Million)	7,600	7,600	9,900	9,900	3,230	3,230

Source: Zawya and APC's financial statements

## Risks and Concerns to Valuation:

- ❖ Any deviation in the estimated demand and price realisations for polypropylene could affect our forecasts and ratings.

## Valuation Methodology:

We have used the DCF valuation method to arrive at the fair value of APC, as explained below:

### Assumptions:

- (i) Risk free Rate (Rf) of 3.40%, equivalent to 12-months average yield on a 10-year US T-bill;
- (ii) Levered Beta of 1.44;
- (iii) Terminal growth rate of 2.0%

Based on the above and using the Capital Asset Pricing Model (CAPM), we have arrived at a Cost of Equity of 13.62% and a WACC of 10.29%.

## DCF Calculation

DCF Valuation (FCFF Model)					
(in SAR Million)	2010E	2011E	2012E	2013E	2014E
<b>NOPAT</b>	324	417	433	446	462
Add: Depreciation and Amortisation	172	178	184	190	197
Less: Capex	28	91	107	112	118
Less: Change in Net Working Capital	63	59	20	19	22
<b>Operating Free Cash Flows to Firm (OFCFF)</b>	<b>406</b>	<b>444</b>	<b>489</b>	<b>505</b>	<b>518</b>
Add: Non-Operating Cash Flows (After Tax Non-Operating Income)	4	5	5	5	5
<b>Free Cash Flow to Firm (FCFF)</b>	<b>409</b>	<b>449</b>	<b>495</b>	<b>510</b>	<b>524</b>
<b>WACC (Ko)</b>	<b>10.29%</b>	<b>10.29%</b>	<b>10.29%</b>	<b>10.29%</b>	<b>10.29%</b>
Present Value / Discount Factor	0.9067	0.8221	0.7454	0.6758	0.6128
<b>Long-Term Growth Rate (g)</b>					<b>2.00%</b>
Terminal Multiple $[(1 + g) / (WACC - g)]$					12.30
<b>Nominal Terminal Value <math>[(FCFF * (1 + g)) / (WACC - g)]</math></b>					<b>6,444</b>
<b>Present Value of Free Cash Flows</b>	<b>371</b>	<b>369</b>	<b>369</b>	<b>345</b>	<b>321</b>

Calculation of Equity Value and Fair Value Per Share	
<b>NPV of Free Cash Flows (during Explicit Forecast Period)</b>	<b>1,775</b>
<b>Terminal Value:</b>	
Residual Cash Flow (FCFF of 2014E)	524
WACC	10.29%
Long-Term/Terminal Growth Rate (g)	2.00%
Divided by Capitalisation Rate (WACC - g)	8.29%
Equals Nominal Terminal Value	6,444
<i>Implied Multiple of 2014E EBITDA</i>	9.78
Times PV/Discount Factor	0.61
<b>Present Value of Terminal/Residual Value</b>	<b>3,949</b>
<b>Enterprise Value</b>	<b>5,724</b>
<i>Implied Multiple of 2014E EBITDA</i>	8.69
Less: Market Value of Long-term Debts	1,474
Less: Market Value of Preferred Shares	0
Add: Surplus Cash and Investments	0
<b>Equity Value</b>	<b>4,250</b>
Net shares outstanding (Million)	141
<b>Fair Value Per Share (SAR)</b>	<b>30.06</b>

Source: Figures in SAR Million unless specified

## Sensitivity Analysis

The following tables present a sensitivity analysis and indicate the probable nominal terminal value, discounted terminal value and enterprise value, given different growth rate and WACC assumptions. The shaded areas represent the most probable outcomes.

Sensitivity Analysis of Nominal Terminal Value (SAR Million)					
Discount Factor	Long-Term Growth Rate				
	1.00%	1.50%	2.00%	2.50%	3.00%
8.29%	7,256	7,829	8,493	9,271	10,197
9.29%	6,381	6,824	7,328	7,906	8,576
<b>10.29%</b>	5,694	6,048	<b>6,444</b>	6,891	7,400
11.29%	5,141	5,430	5,751	6,108	6,507
12.29%	4,686	4,927	4,927	5,484	5,807

Sensitivity Analysis of Discounted Terminal Value (SAR Million)					
Discount Factor	Long-Term Growth Rate				
	1.00%	1.50%	2.00%	2.50%	3.00%
8.29%	4,872	5,257	5,703	6,225	6,847
9.29%	4,092	4,376	4,700	5,070	5,500
<b>10.29%</b>	3,489	3,706	<b>3,949</b>	4,223	4,534
11.29%	3,011	3,181	3,368	3,577	3,812
12.29%	2,624	2,760	2,908	3,071	3,253

Sensitivity Analysis of Enterprise Value (SAR Million)	
Discount Factor	Long-Term Growth Rate

	1.00%	1.50%	2.00%	2.50%	3.00%
8.29%	6,745	7,130	7,576	8,099	8,720
9.29%	5,915	6,199	6,522	6,893	7,323
<b>10.29%</b>	5,264	5,481	<b>5,724</b>	5,998	6,309
11.29%	4,740	4,909	5,097	5,306	5,540
12.29%	4,309	4,444	4,592	4,756	4,937

## Investment Opinion

The petrochemical sector has been witnessing a gradual improvement in demand as economies around the world have started seeing signs of recovery. The sector's performance is strongly correlated to the overall economic conditions. The sector witnessed healthy growth till mid-2008 on sound economic growth in most countries, which translated into strong demand for petrochemicals. At the same time, price realisations followed an upward trajectory leading to record top-line and bottom-line growth for companies operating in the sector. However, towards the later part of 2008, the sector witnessed a slowdown as demand suffered due to the worldwide economic weakness. The slowdown, driven by multiple factors like the subprime crisis, declining commodity prices and weak economic conditions, was the key factor behind the dip in demand. Prices of basic petrochemicals such as ethylene, butadiene, propylene, styrene, and benzene slumped to three-year lows. Even China, which continues to be one of the largest consumers of petrochemicals, was no exception and witnessed a slump in demand for the first time in 10 years. As the crisis deepened, the petrochemicals sector saw production facilities shutting down and capacity addition plans getting either shelved or delayed.

Since the later part of 2009, when many economies saw some signs of recovery, demand for petrochemical products has been improving and prices have been gradually moving up. OPEC crude oil price increased from USD 35.58 per barrel (bbl) at the start of 2009 to USD 75.14 per bbl as of February 3, 2010. Natural gas price moved up as well, rising 37.8% sequentially during 4Q09 to USD 4.37 million British Thermal Unit (BTU), reversing the five-quarter decline. Furthermore, prices of ethylene, LDPE, and propylene witnessed sequential improvements during 4Q09. During 3Q09 and 4Q09, ethylene prices increased 33.1% and 6.0%, LDPE prices increased 9.1% and 3.9%, and propylene prices moved up by 20.9% and 1.1%, respectively on a sequential basis. Polypropylene prices increased sequentially by 27.9% during 2Q09 and by another 6.9% during 3Q09, reversing the declines in 4Q08 and 1Q09. Despite a marginal 1.1% decline in polypropylene prices during 4Q09, the demand scenario looks upbeat as prices rebounded by 13.5% in January 2010. Going forward, the positive scenario for petrochemical prices is expected to help the financial performance of companies operating in the sector.

APC is amongst the leading producers of polypropylene in Saudi Arabia with a designed capacity of 450,000 tonnes per year. The company has access to cheaper raw materials due to its 20-year agreement with Saudi Aramco. Furthermore, the company's focus on strategic alliances for marketing its products globally is definitely a positive factor in the longer run. Moreover, the company's focus on employing proven technologies to achieve cost synergies is likely to result in higher margins. At the same time, the improving demand scenario for polypropylene and rising prices are expected to help the top-line and bottom-line performance over the upcoming quarters. Based on these fundamental positives, we continue to hold an optimistic view on APC.

We had initiated APC on May 26, 2009 with an OVERWEIGHT recommendation (target price of SAR 28.79 and an upside of 19.9%). Currently, APC is trading at a P/E multiple of 11.20x and 8.38x on 2010E and 2011E earnings, and at a P/BV multiple of 1.80x and 1.66x on 2010E and 2011E BVPS, respectively. The company has declined 8.2% since the beginning of this year, as against a 5.6% increase registered by the Tadawul All Share Index. Considering the above factors, we arrive at a price target of SAR 30.06, which exhibits a potential upside of 31.6% from its closing price of SAR 22.85 (as on February 24, 2009). **Therefore, we reiterate our earlier OVERWEIGHT recommendation on APC.**

## Financial Statements

Consolidated Income Statement					
(SAR Million)	2008A	2009A	2010E	2011E	2012E
<b>Sales</b>	<b>1,459</b>	<b>1,467</b>	<b>2,107</b>	<b>2,547</b>	<b>2,671</b>
Cost of sales	-1,068	-1,065	-1,545	-1,874	-1,973
<b>Gross profit/ (loss)</b>	<b>391</b>	<b>402</b>	<b>562</b>	<b>672</b>	<b>699</b>
Depreciation and amortisation	-112	-184	-172	-178	-184
Selling and distribution expenses	-17	-30	-43	-53	-55
General and administrative expenses	-9	-15	-21	-26	-27
<b>Operating income/ (loss)</b>	<b>254</b>	<b>173</b>	<b>324</b>	<b>417</b>	<b>433</b>
<b>EBITDA</b>	<b>366</b>	<b>357</b>	<b>497</b>	<b>594</b>	<b>617</b>
Net finance charges	-48	-48	-40	-36	-31
Other income	4	2	4	5	5
<b>Net (loss)/ income</b>	<b>210</b>	<b>127</b>	<b>288</b>	<b>386</b>	<b>407</b>

<b>Consolidated Balance Sheet</b>					
(SAR Million)	2008A	2009A	2010E	2011E	2012E
<b>ASSETS</b>					
<b>Current Assets</b>					
Cash and cash equivalents	216	296	350	376	425
Trade receivables	345	272	373	444	459
Other receivables and prepayments	20	32	32	32	32
Inventories	195	221	285	336	348
Short term investments	0	12	12	13	13
<b>Total Current Assets</b>	<b>776</b>	<b>833</b>	<b>1,053</b>	<b>1,201</b>	<b>1,276</b>
<b>Non-Current Assets</b>					
Intangible assets	88	83	68	53	38
Property, plant and equipment	2,643	2,498	2,369	2,297	2,236
<b>Total Non-Current Assets</b>	<b>2,731</b>	<b>2,581</b>	<b>2,436</b>	<b>2,350</b>	<b>2,273</b>
<b>Total Assets</b>	<b>3,507</b>	<b>3,414</b>	<b>3,489</b>	<b>3,551</b>	<b>3,549</b>
<b>LIABILITIES AND EQUITY</b>					
<b>Liabilities</b>					
<b>Current Liabilities</b>					
Accounts payable and other liabilities	172	261	364	426	432
Current portion of long term loan	125	140	155	171	171
Short term loan	188	94	84	75	64
Accrued dividend	0	1	0	0	0
<b>Total Current Liabilities</b>	<b>484</b>	<b>496</b>	<b>604</b>	<b>672</b>	<b>667</b>
<b>Non-Current Liabilities</b>					
Long term loans	1,400	1,240	1,085	914	743
End-of-service indemnities	5	7	10	14	19
<b>Total Non-Current Liabilities</b>	<b>1,405</b>	<b>1,247</b>	<b>1,095</b>	<b>928</b>	<b>762</b>
<b>Total Liabilities</b>	<b>1,890</b>	<b>1,743</b>	<b>1,699</b>	<b>1,599</b>	<b>1,429</b>
<b>Equity</b>					
Share capital	1,414	1,414	1,414	1,414	1,414
Statutory reserve	21	34	63	102	142
Retained earnings	182	223	314	436	565
<b>Equity attributable to equity holders of the company</b>	<b>1,617</b>	<b>1,670</b>	<b>1,791</b>	<b>1,951</b>	<b>2,121</b>
<b>Total Liabilities and Equity</b>	<b>3,507</b>	<b>3,414</b>	<b>3,489</b>	<b>3,551</b>	<b>3,549</b>

## Consolidated Cash Flow Statement

(SAR Million)	2008A	2009A	2010E	2011E	2012E
<b>OPERATING/ PRE-OPERATING ACTIVITIES</b>					
Net income	210	127	288	386	407
<b>Adjustments for:</b>					
Depreciation and amortisation	112	184	172	178	184
End-of-service indemnities	3	3	4	5	7
<b>Cash from operations/ pre-operations before working capital changes</b>	<b>324</b>	<b>314</b>	<b>465</b>	<b>569</b>	<b>598</b>
<b>Working capital changes:</b>					
Trade, other receivables and prepayments	-355	61	-110	-81	-24
Inventories	-191	-27	-64	-50	-12
Accounts payable and other liabilities	110	87	102	62	6
<b>Cash used in operating/ pre-operating activities</b>	<b>-112</b>	<b>436</b>	<b>394</b>	<b>499</b>	<b>568</b>
End-of-service indemnities paid	0	-1	-1	-2	-2
Income tax paid	-1	-1	-3	-4	-4
<b>Net cash used in operating/ pre-operating activities</b>	<b>-113</b>	<b>434</b>	<b>390</b>	<b>494</b>	<b>562</b>
<b>INVESTING ACTIVITIES</b>					
Short term investments	0	-12	0	0	0
Additions to property, plant and equipment	-361	-11	-28	-91	-107
Increase in intangible assets	-41	-23	0	0	0
<b>Net cash used in investing activities</b>	<b>-401</b>	<b>-46</b>	<b>-28</b>	<b>-91</b>	<b>-108</b>
<b>FINANCING ACTIVITIES</b>					
Due to bank	0	-94	-9	-9	-11
Repayment of short term loan and long term loan	0	-145	-140	-155	-171
Drawdown of short term loan	188	0	0	0	0
Drawdown of long term loan	455	0	0	0	0
Cash dividend paid	0	-70	-158	-212	-223
<b>Net cash from (used in) financing activities</b>	<b>643</b>	<b>-309</b>	<b>-308</b>	<b>-377</b>	<b>-405</b>
<b>Net change in cash and cash equivalents</b>	<b>128</b>	<b>80</b>	<b>53</b>	<b>26</b>	<b>49</b>
Cash and cash equivalents at the beginning of the period	89	216	296	350	376
<b>Cash and cash equivalents at the end of the period</b>	<b>216</b>	<b>296</b>	<b>350</b>	<b>376</b>	<b>425</b>

## Financial Ratios

	2008A	2009A	2010E	2011E	2012E
<b>Liquidity Ratios:</b>					
Current Ratio (x)	1.60	1.68	1.74	1.79	1.91
Quick Ratio (x)	1.20	1.23	1.27	1.29	1.39
Inventory Conversion Period (Days)	34	71	60	61	63
Average Collection Period (Days)	NA	77	56	59	62
Length of Operating Cycle (Days)	NA	148	116	119	125
Average Payment Period (Days)	39	74	74	77	79
Length of Cash Cycle (Days)	NA	74	42	42	46
<b>Activity Ratios:</b>					
Debtors Turnover Ratio (x)	NA	4.76	6.53	6.23	5.92
Creditors' Turnover Ratio (x)	9.36	4.92	4.94	4.75	4.60
Total Assets Turnover Ratio (x)	0.48	0.42	0.61	0.72	0.75
Equity Turnover Ratio (x)	0.96	0.89	1.22	1.36	1.31
<b>Profitability Ratios:</b>					
Gross Profit Margin (GPM)	26.8%	27.4%	26.7%	26.4%	26.2%
EBITDA Margin	25.1%	24.3%	23.6%	23.3%	23.1%
Operating Profit Margin (OPM)	17.4%	11.8%	15.4%	16.4%	16.2%
Net Profit Margin (NPM)	14.4%	8.7%	13.7%	15.1%	15.2%
Return on Average Equity (RoAE)	13.9%	7.7%	16.7%	20.6%	20.0%
Return on Average Assets (RoAA)	6.9%	3.7%	8.4%	11.0%	11.5%
<b>Leverage Ratios:</b>					
Debt to Equity (D/E) Ratio (x)	1.06	0.88	0.74	0.59	0.46
Shareholders' Equity to Total Assets Ratio (x)	0.46	0.49	0.51	0.55	0.60
Total Liabilities to Total Assets Ratio (x)	0.54	0.51	0.49	0.45	0.40
Current Liabilities to Equity Ratio (x)	0.30	0.30	0.34	0.34	0.31
<b>Growth Rates:</b>					
YoY Growth in Revenue	NA	0.5%	43.6%	20.9%	4.9%
YoY Growth in Operating Profit	NA	-31.9%	87.6%	28.4%	3.9%
YoY Growth in EBITDA	NA	-2.4%	39.2%	19.6%	3.8%
YoY Growth in Net Profit	NA	-39.5%	126.9%	33.7%	5.5%
YoY Growth in Total Assets	37.8%	-2.7%	2.2%	1.8%	0.0%
YoY Growth in Shareholders' Equity	14.2%	3.3%	7.2%	9.0%	8.7%
<b>Ratios used for Valuation:</b>					
Adj. EPS (SAR)	1.49	0.90	2.04	2.73	2.88
Adj. BVPS (SAR)	11.44	11.82	12.66	13.80	15.00
P/E Ratio (x)	15.37	25.41	11.20	8.38	7.94
P/BV Ratio (x)	2.00	1.93	1.80	1.66	1.52
Current Market Price (SAR)*	22.85	22.85	22.85	22.85	22.85

\* CMP as on Feb 24, 2009