

### 2Q 2018 Results Update

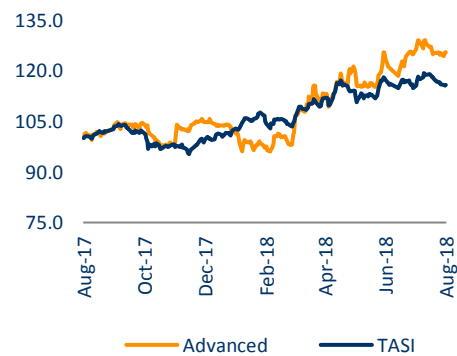
August 09, 2018

Recommendation	Overweight
Previous Recommendation	Overweight
Current Price (SAR)	55.3
Target Price (SAR)	61.4
Upside/Downside (%)	11.0%
<i>As of August 07<sup>th</sup> 2018</i>	

#### Key Data (Source: Bloomberg)

Market Cap (SAR bn)	10.9
52 Wk High (SAR)	57.2
52 Wk Low (SAR)	41.9
Total Outstanding shares (in mn)	197
Free Float (%)	93.2%

#### Advanced vs. TASI (Rebased)



Price Performance (%)	Absolute	Relative
1m	0.4%	(0.4%)
6m	28.7%	17.6%
12m	25.5%	9.6%

#### Major Shareholders (%)

Polypropylene National Company	7.95%
General Organization for Social Insurance	6.37%

#### Quarterly Sales (SAR bn) and Operating Margin



Source: Bloomberg, Company Financials, FALCOM Research; Data as of August 07<sup>th</sup> 2018

#### Stellar performance in 2Q18, driven by higher PP prices and improved production

Advanced Petrochemical (Advanced) posted remarkable second quarter results, with net profit rising +30.2% YoY, driven by higher sales volumes and an 18.2% surge in polypropylene prices. The positive performance was in spite of higher feedstock prices (propane: +39.7% YoY; propylene: +28.5% YoY) during the current quarter. Sequentially, Advanced's net profit rose +160% QoQ primarily due to 42.9% QoQ increase in sales volumes, resulting from the scheduled maintenance shutdowns in 1Q18. Following the maintenance activity, propylene plant's output increased to 490K tons from 450K tons, and polypropylene output rose to over 585K tons from 450K tons annually.

Saudi Aramco Total Refining and Petrochemical Co. (SATORP) and Advanced are in talks to increase propylene supply to Advanced from 80,000 tons in 2018 to 100,000 tons in 2019. Meanwhile, Advanced revealed that the firm is yet to reach a decision regarding Rufayah Chemicals Company (RCC)'s project for Pygas and Pyoil products in the country. SK Advanced Co. (30% owned by Advanced) recently inked a deal with PolyMirae Co. to setup a new 400 Kt per year PP plant in South Korea at a total cost of USD 420mn. The plant is likely to commence construction in January 2019, with an expected completion date in 2021. We expect this strategic investment and the SATORP deal to prove positive for the company. As per the Chemical Economics Handbook (HIS), demand for PP would increase 25% by 2022 from current levels, driven by economic growth in China and India.

- Advanced's top line increased (+24% YoY; +49% QoQ) to SAR 750mn in 2Q18, driven by higher sales prices, and the company benefiting from scheduled turnaround in 1Q18. This resulted in improved production levels in 2Q18, leading to growth in sales volumes.
- Gross profit rose 26% YoY and 133% QoQ to SAR 277mn, driven by higher sales volumes and an increase in product spread. Consequently, gross margin expanded 55bps YoY and 1,332bps QoQ to 37.0% in 2Q18. Besides expansion in the PP-Propane spread, the positive impact of plant maintenance and high operating efficiency acted as a catalysts in driving margins higher.
- Operating profit rose 28% YoY and 160% QoQ to SAR 247mn, largely driven by higher sales volumes and improved efficiency, despite 9% YoY and 25% QoQ surge in SG&A expenses. Operating margin thus expanded 112bps YoY and 1,410bps QoQ to 32.9% in 2Q18.
- Net profit for the quarter came in at SAR 253mn (+30% YoY; +160% QoQ), as operating profit growth was further enhanced by increase in share of profit from associates (SK Advanced Co.), which stood at SAR 23.6mn in 2Q18 as compared with SAR 10.5mn in 2Q17.
- In spite of strong earnings, Advanced's cash flow from operating activities declined 66% YoY and 78% QoQ to SAR 55mn, primarily attributed to an increase in accounts receivables.
- Given the supply-side pressure on the oil market, ascribed to the US sanction on Iran, we expect Advanced to benefit from elevated oil prices. Consequently, we expect petrochemical prices to follow suit, and polypropylene and propylene spreads to stabilize from current levels and gradually improve over the long term.

**Valuation:** We have revised our target price upward, with a fair value of SAR 61.4 per share, in the light of improved operational efficiencies and strong 2Q18 results. The stock has rallied 8% since our last earnings report. We maintain our 'Overweight' rating on the stock.

	2Q'18	2Q'17	% YoY	FY18E	FY17	% YoY
Revenues (SAR mn)	750	604	24.0%	2,629	2,385	10.2%
Gross Profit (SAR mn)	277	220	25.9%	881	738	19.3%
EBITDA (SAR mn)	195	144	35.2%	954	812	17.6%
Net Profit (SAR mn)	253	195	30.2%	769	631	17.6%
EPS basic (SAR)	1.3	1.0	30.2%	3.8	3.2	17.6%
Gross Margin (%)	37.0%	36.4%	0.5%	33.5%	31.0%	2.5%
EBITDA Margin (%)	26.0%	23.9%	2.2%	36.3%	34.0%	2.3%
Net Profit Margin (%)	33.8%	32.2%	1.6%	28.2%	26.5%	1.8%

Source: Company Financials, FALCOM Research

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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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