

Buy

TP SR113.00 (from SR115.00)

RBS Refiner

Price (close 23 Jan)	SR92.25
3M high/low	SR97.25/89.50
Market cap	SR276.75bn
Av (12M) turnover	SR609.88m
Freefloat	30%
Reuters	2010.SE
Bloomberg	SABIC AB
Net debt (cash) FY10	SR59953.77m
3yr EPS CAGR 11-13F	13.9%
Income (2012F div yield)	5.1%

Source: RBS forecasts, Bloomberg

RBS vs consensus

EPS (SR)	Rasmala	Cons	% diff
2012F	9.46	9.97	-5%
2013F	10.61	10.53	1%
2014F	11.18	10.81	3%

Source: RBS forecasts, Bloomberg

Price performance

	(1M)	(3M)	(12M)
Price (SR)	95.75	92.25	n/a
Absolute (%)	-3.7	0.0	n/a
Rel to mkt*(%)	-5.6	-5.5	n/a

*Tadawul Index
Source: Bloomberg

Key events

Date	Event
Apr-12	1Q12 results

Source: Bloomberg

SABIC

Look beyond 1H12

We expect a relatively weak start to 2012, but expect a recovery in petrochemical demand and margins in the second half of the year. SABIC has strong leverage to improving economic growth. We believe the stock is cheap at 5.3x 2012F EV/EBITDA, and we maintain our Buy recommendation.

Event: 4Q11 results below expectations, but we reiterate our Buy recommendation

Following SABIC's 4Q11 results, we adjust our forecasts and maintain our Buy recommendation. 4Q11 revenues of SAR47bn were in line with our forecast, but 4Q11 net income was 18% below our forecast and full-year net income 4% below, although we were at the lower end of the consensus range. SABIC cited a lower pricing environment as the main reason behind the 36% qoq decline in net income and 20% drop in gross profit, despite an increase in sales volumes. We believe margins have suffered as oil prices remained high in the 4Q, but petrochemical prices dropped in 4Q11. The average ethylene and LDPE prices were down as much as 10% in 4Q11 versus 3Q11, as customers have been careful about restocking inventories and producers were unable to pass on high raw material costs. We believe SABIC's operations in Europe in particular are likely to have been affected.

Forecasts: We assume a weaker start to the year than in our previous forecasts

We are reducing our 2012 EBITDA forecast by 4% and our net income forecast by 5%, but maintain our forecasts for 2013 and beyond. We now assume a somewhat weaker start to 2012 than in our previous forecasts, mainly assuming a lower utilisation rate for SABIC's European operations, but we have not made any changes to our base-case forecast of a 10% drop in petrochemicals prices for 2012. We expect a recovery in demand in 2H12, which, combined with relatively limited new supply coming into the market, should lead to higher operating rates and petrochemical spreads. We expect further improvement in 2013 and 2014.

Valuation: SABIC should be a core holding in the Saudi Arabian stock market

As a result of our downgrade for 2012, we reduce our target price slightly, from SR115 to SR113/share. We use a DCF analysis (WACC 10%, g=2%, beta 1.1x) to value the stock and cross-check with peer multiples. Current valuation multiples of 5.3x 2012F EV/EBITDA and 9.8x PE and 2012F target EV/EBITDA of 6.3x and PE of 11.9x look cheap compared with peers and historical values, further supported by a dividend yield exceeding 5%. Key risks to our investment case are a substantial drop in oil prices, worse-than-expected global GDP growth resulting in weak demand for SABIC's products, increases in feedstock costs in Saudi Arabia and political risk in the Middle East.

Key forecasts

year to Dec	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue (SRm)	103,105	151,970	189,546	184,943	186,958
EBITDA (SRm)	30,757	48,502	60,065	60,772	68,078
Normalised PTP (SRm)	18,457	35,754	48,324	47,171	53,474
Norm fully diluted EPS (SR)	3.42	7.18	9.74	9.46	10.61
Normalised PE	27.00	12.90	9.47	9.76	8.70
Dividend per share (SR)	1.50	3.50	5.00 ▲	4.73 ▲	5.30 ▲
Dividend yield (%)	1.63	3.79	5.42	5.13	5.75

Use of ▲ ▼ indicates that the line item has changed by at least 5%.
Accounting standard: Saudi Arabia GAAP

Source: Company data, Rasmala forecasts

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Important disclosures can be found in the Disclosures Appendix.
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RBS Equities Essentials: SABIC

Company description

SABIC, headquartered in Riyadh, Saudi Arabia, ranks among the world's top petrochemicals companies and among its market leaders in the production of polyethylene, polypropylene and advanced thermoplastics, glycols, methanol and fertilisers. Also, it is one of the largest producers of steel in the Middle East. It is the largest listed company in the Middle East and North Africa region by market capitalisation.

Company drivers

- SABIC has a low-cost production base in Saudi Arabia, where it pays a fixed US\$0.75/MMBtu, making it one of the most competitive petrochemical producers globally.
- SABIC has a strong balance sheet that it could use for either further capacity expansion or acquisitions.
- SABIC is a truly global player, with production capacity in the Middle East, the US, Europe and China, which gives it access to all major end markets.
- SABIC is very focused on the commodity part of the chemicals value chain, which makes earnings more volatile, but the company has intentions to broaden its product portfolio.

Industry drivers

- Petrochemicals demand is highly correlated to GDP growth, hence clarity on a recovery would be positive for the sector.
- We expect limited major capacity additions of about 2% on average for 2011-15, compared with 4-10% new annual capacity additions between 2007 and 2010.
- Higher oil prices should lead to higher petrochemical prices given the strong correlation between the two.
- The construction, consumer non-durables and automotive sectors are the main drivers for global petrochemical volumes.

SWOT analysis

Strengths

Low-cost production, access to cheap gas in Saudi Arabia. Global reach with production in Saudi Arabia, the US, Europe and Asia. Large integrated petrochemicals sites. Strong balance sheet.

Weaknesses

Sensitivity to factors outside the company's control: oil prices, product prices and global economic growth. Cyclical businesses.

Opportunities

Continued capex to grow top and bottom lines, both inside and outside the region. Moving downstream in the value chain. Balance sheet strong enough to do this.

Threats

Expansion of petrochemicals capacity by competitors, inside and outside the region.

Ethylene demand correlation with GDP growth

	2003	2004	2005	2006	2007	2008	2009	2010
Global GDP growth	3.60%	4.90%	4.60%	5.20%	5.40%	2.90%	-0.50%	5.00%
Global demand growth	4%	5%	0%	4%	5%	-6%	2%	4%
Multiplier effect	0.99	1.10	0.02	0.72	1.00	-1.92	-4.54	0.81
Global supply growth	1%	1%	4%	4%	4%	4%	2%	8%
Demand growth over supply growth	3%	4%	-4%	0%	1%	-10%	0%	-4%

Source: RBS economics team, Rasmala

RBS Equities Assumptions: SABIC

Catalyst for share price performance

The key catalysts for share price performance include a more positive outlook for economic growth, particularly in Asia (SABIC's main end market) and stable or rising oil prices. Petrochemical pricing is the main driver of SABIC's earnings and margins. Given that we believe the market is already factoring in a decline in prices from current levels, we believe any improvement in the outlook for petrochemicals prices and spreads should provide a positive catalyst. Other catalysts include announcements of further capacity additions, which we generally see as value-accretive, and the successful ramp-up of recent capacity additions such as Saudi Kayan.

RBS sensitivity to central scenario

Our sensitivity analysis is based on assumptions for the following variables: 1) product prices (petrochemicals, fertilisers and metals) as a discount or premium to our current forecasts; 2) capacity utilisation for the different plants versus our base case, where we assume utilisation rates between 75% (for petrochemicals outside Saudi Arabia) to just over 100% for fertilisers. Both scenarios would result in relatively small changes of less than 5% to our valuation, with only greater sensitivity if we were to assume these changes for a longer period than just for 2012.

RBS valuation sensitivity

Variable	Year	Bear case		RBS base case	Bull case	
		Assumption	Valuation impact		Assumption	Valuation impact
Product prices versus base case	2012	-10%	-3.5	100%	+10%	+3.6
Capacity utilisation versus base case	2012	-10 ppt	-3.8	Between 65-95%	+10 ppt	+3.8

Source: Rasmala forecast

Standard ratios

Performance (%)	FY09A	FY10A	FY11F	FY12F	Valuation (x)	FY09A	FY10A	FY11F	FY12F
Sales growth	-31.6	47.4	24.7	-2.43	EV/sales	3.17	2.22	1.72	1.74
EBITDA growth	-34.1	57.7	23.8	1.18	EV/EBITDA	10.6	6.94	5.43	5.29
EBIT growth	-45.4	89.6	28.8	-0.03	EV/EBITDA @ tgt price	12.6	8.23	6.46	6.31
Normalised EPS growth	-53.4	109.9	35.7	-2.90	EV/EBIT	16.3	8.89	6.68	6.59
EBITDA margin	29.8	31.9	31.7	32.9	EV/invested capital	1.61	1.49	1.35	1.23
EBIT margin	19.4	24.9	25.7	26.4	Price/book value	2.56	2.29	1.98	1.81
Net profit margin	9.95	14.2	15.4	15.3	Equity FCF yield (%)	1.03	4.89	12.4	11.2
Return on avg assets	7.24	11.9	14.6	13.8	Normalised PE	27.0	12.9	9.47	9.76
Return on avg equity	9.71	18.8	22.4	19.4	Norm PE @ tgt price	33.1	15.7	11.6	11.9
ROIC	10.6	18.7	21.6	20.3	Dividend yield (%)	1.63	3.79	5.42	5.13
ROIC - WACC	-0.62	5.24	11.1	10.4					
Solvency	FY09A	FY10A	FY11F	FY12F		FY09A	FY10A	FY11F	FY12F
Net debt to equity (%)	32.6	36.1	25.7	20.6	Current ratio (x)	3.31	2.64	2.97	3.06
Net debt to tot ass (%)	16.8	18.9	14.3	12.5	Operating CF int cov (x)	-8.17	-8.46	-16.9	-12.3
Net debt to EBITDA(%)	1.62	1.24	0.82	0.73	Dividend cover (x)	2.73	2.40	2.78	1.89

year to Dec

Source: Company data, Rasmala forecasts

RBS Equities Forecasts: SABIC

Income statement

SRm, year to December	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	103105	151970	189546	184943	186958
Cost of sales	-63714	-92813	-116171	-109376	-103923
Operating costs	-8634	-10654	-13310	-14795	-14957
EBITDA	30757	48502	60065	60772	68078
DDA & Impairment (ex gw)	-10773	-10610	-11269	-11991	-12728
EBITA	19985	37893	48796	48781	55350
Goodwill (amort/impaird)	-1181	0.00	0.00	0.00	0.00
EBIT	18804	37893	48796	48781	55350
Net interest	-3026	-3394	-2800	-4054	-4442
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	1497	1256	2328	2444	2567
Reported PTP	17275	35754	48324	47171	53474
Taxation	-900.0	-2500	-2658	-2830	-3743
Minority interests	-7302	-11726	-16450	-15973	-17914
Other post-tax items	-0.00	0.00	0.00	0.00	0.00
Reported net profit	9074	21529	29216	28369	31817
Tot normalised items	-1181	0.00	0.00	0.00	0.00
Normalised EBITDA	30757	48502	60065	60772	68078
Normalised PTP	18457	35754	48324	47171	53474
Normalised net profit	10255	21529	29216	28369	31817

Balance sheet

SRm, year ended December	FY09A	FY10A	FY11F	FY12F	FY13F
Cash & market secs (1)	57197	50648	59604	49276	57867
Other current assets	49267	66451	78158	82642	78744
Tangible fixed assets	157539	164889	172977	192263	200734
Intang assets (incl gw)	21901	22624	21267	19991	18791
Oth non-curr assets	10957	12967	12967	12967	12967
Total assets	296861	317580	344973	357139	369104
Short term debt (2)	6477	16754	15000	10000	5000
Trade & oth current liab	25696	27551	31346	33143	31475
Long term debt (3)	100538	93848	93848	83848	78848
Oth non-current liab	11521	13281	13281	13281	13281
Total liabilities	144231	151433	153475	140272	128604
Total equity (incl min)	152630	166147	191499	216867	240500
Total liab & sh equity	296861	317580	344973	357139	369104
Net debt	49818	59954	49244	44572	25981

Cash flow statement

SRm, year to December	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA	30757	48502	60065	60772	68078
Change in working capital	-991.4	-15443	-7911	-2687	2230
Net interest (pd) / rec	3026	3394	2800	4054	4442
Taxes paid	-900.0	-2500	-2658	-2830	-3743
Other oper cash items	-5059	-4329	-4864	-8414	-7010
Cash flow from ops (1)	26832	29625	47432	50894	63997
Capex (2)	-23988	-16100	-13000	-20000	-20000
Disposals/(acquisitions)	0.00	0.00	-2000	0.00	0.00
Other investing cash flow	-647.6	-3962	0.00	0.00	0.00
Cash flow from invest (3)	-24636	-20063	-15000	-20000	-20000
Incr / (decr) in equity	0.00	0.00	0.00	0.00	0.00
Incr / (decr) in debt	14358	3587	-1754	-15000	-10000
Ordinary dividend paid	-3750	-8962	-10500	-15000	-14184
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-6635	-10737	-11222	-11222	-11222
Cash flow from fin (5)	3973	-16111	-23476	-41222	-35406
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Incr/(decr) cash (1+3+5+6)	6170	-6549	8956	-10328	8591
Equity FCF (1+2+4)	2844	13525	34432	30894	43997

Source: Company data, Rasmala forecasts

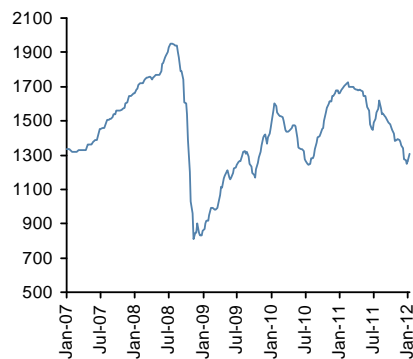
Petrochemicals

In line with SABIC's comments about the current market situation, we expect a muted demand and pricing environment for 1H12, but a recovery in demand in 2H12, which we believe should lead to a re-rating of MENA petrochemical shares.

Customers are keeping inventories at low levels

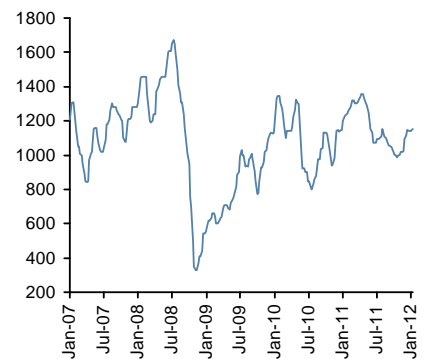
In the past six months, customers have been careful about buying product, keeping inventories to a minimum and ordering lower quantities, but at more frequent intervals than before. Oil/naphtha prices have remained high, but petrochemical prices dropped on average about 10% in 4Q11 versus 3Q11, biting into margins in the latter part of 2011. Given the massive increases in capacity over the past few years, including Saudi Kayan's massive complex in October 2011, petrochemical supply has been plentiful and hence producers have found it difficult to pass on higher costs to end customers.

Chart 1 : Ethylene (US\$/tonne)



Source: Bloomberg

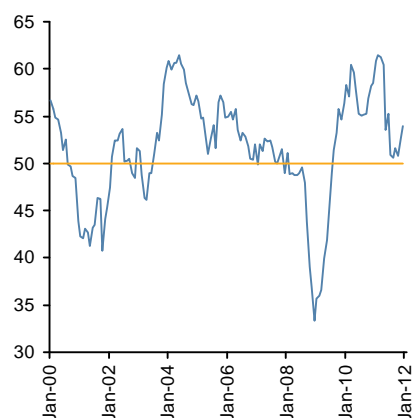
Chart 2 : LDPE (US\$/tonne)



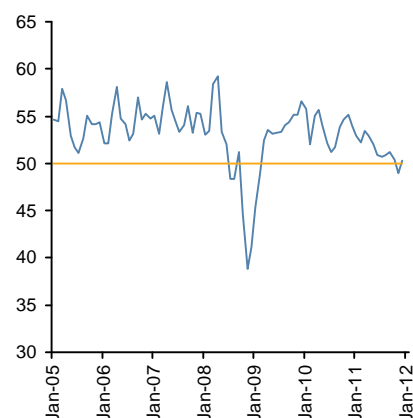
Source: Bloomberg

Petrochemical prices have stabilised within the past few weeks, but risks remain from global economic activity and some capacity additions that still must be absorbed by the market.

Furthermore, economic, and in particular manufacturing, data has been mixed, with a slowdown in Chinese manufacturing PMI in 4Q11, but still just above 50 – a level above 50 generally indicates that the industry is expanding. This is particularly relevant for the MENA petrochemical producers, since a major part of their exports goes to Asia. Elsewhere, a recession in Europe will also have a negative impact on volumes, but given that European cash costs are some of the highest in the world, this could actually lead to some plant closures. On a more positive note, the US has surprised on the upside and December PMI data recovered to 53.9 from a low of 50.8 in October.

Chart 3 : US manufacturing PMI

Source: Bloomberg

Chart 4 : China manufacturing PMI

Source: Bloomberg

1H12 probably subdued, but we see recovery as the year progresses

Petrochemical demand is closely correlated with GDP growth, hence the relevance of the fear of another recession. RBS economists forecast global growth of 3.4% for 2012, which would be positive for petrochemicals; and for the US, the most recent revision was upward, from 2.4% to 2.6%.

We believe the slowdown in Chinese PMI could pose one of the most significant threats to petrochemicals demand this year. However, China reported 8.9% GDP growth in 4Q11, stronger than our economists expected, with production growth picking up in December and domestic demand holding up better than the economists expected. RBS economists are more bullish on China than consensus, and we expect growth of 8.5% there and in Asia (ex-Japan) 7.0%, enough to support continued demand growth for petrochemicals.

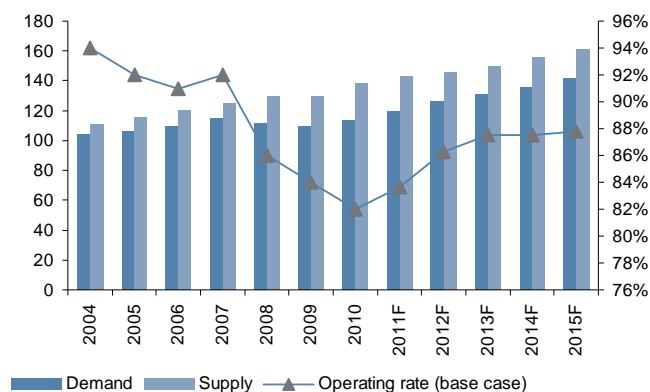
Table 1 : GDP growth outlook (% change yoy)

	2010	2011F	2012F
US	3.0	1.8	2.6
Euro area	1.8	1.5	-0.4
Germany	3.6	3.0	-0.1
UK	1.8	0.9	0.8
Japan	4.5	-0.8	1.8
G-4	2.7	1.3	1.4
Asia (ex-Japan)	9.3	7.4	7.0
- China	10.4	9.1	8.5
- India	8.6	6.8	6.7
Emerging Europe and SA	4.7	4.8	2.6
Latin America			
- Brazil	7.5	2.8	3.1
- Argentina	9.0	8.5	4.7
World	4.9	3.5	3.4

Source: RBS Strategy

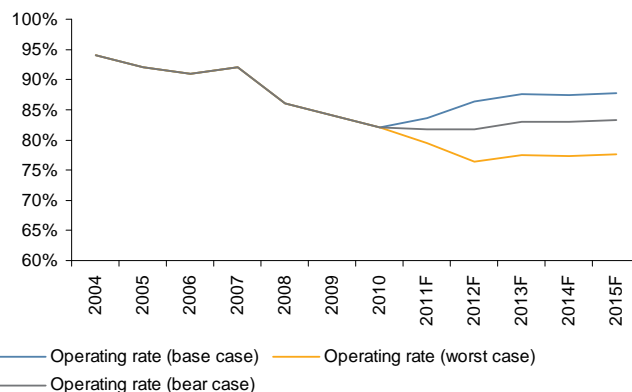
Furthermore, we do not expect major capacity additions, as we have discussed in previous notes. Our view on SABIC is largely based on the supply fundamentals of the petrochemicals industry and the lack of planned capacity additions for 2012-15. The last trough in 2008/09 was bad, when a sharp drop in demand coincided with a flood of capacity additions, especially in the Middle East and China. Supply grew on average 4-10% between 2007 and 2010, but we expect below-average capacity growth of on average 2-3% annually during 2011-15, below our economists' global GDP growth forecast.

Chart 5 : Ethylene global supply/demand balance and operating rates



Source: CMAI, ICIS, Rasmala forecasts

Chart 6 : Global ethylene operating rates under different scenarios (%)



Source: CMAI, ICIS, Rasmala forecasts

Economic growth combined with the lack of new supply coming to the market for an extended period has resulted in much talk in the market about the super cycle for petrochemicals – in our view, the demand side will be the main determiner of whether this will occur, but, for now, petrochemical earnings growth seems sustainable, especially if global uncertainty results in new capacities being cancelled or delayed. Based on current GDP forecasts of our economists and given the supply outlook, we expect global ethylene operating rates to rise from about 82% in 2010 to 88% in 2015. Only in the worst-case scenario of 0% global growth in 2012 would we expect operating rates to drop materially.

In any case, we believe operating rates for the MENA producers will remain high, as has been the case in the past during downturns, which then makes petrochemicals pricing the key variable. We are not changing our forecasts for petrochemicals prices.

Table 2 : Key price assumptions (US\$/tonne)

	2012F	2013F	2014F	2015F
Ethylene	859	870	864	849
Propylene	1,059	1,070	1,064	1,049
Styrene	1,200	1,236	1,273	1,311
Methanol	295	300	300	300
MTBE	885	900	900	900
Ethylene glycols	984	995	989	974
LDPE	1,509	1,520	1,514	1,499
LLDPE	1,209	1,220	1,214	1,199
HDPE	959	970	964	949
Polypropylenes	1,209	1,220	1,214	1,199
Polycarbonate	2,200	2,266	2,334	2,404
ABS	1,800	1,854	1,910	1,967
Ammonia	400	425	431	438
Urea	375	381	386	392
Steel bar	775	798	822	847

Source: Rasmala forecasts

Disclosure Appendix

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Relative views: Our strategy teams and analysts may provide strategy views on sectors and/or markets. An Overweight, Underweight or Neutral view implies outperformance, underperformance or a neutral performance in an indicated relative context

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