Equity | Saudi Arabia | Chemicals

31 October 2011

SABIC

How about the super cycle?

We initiate coverage of SABIC with a Buy recommendation and target price of SAR115/share. We believe the stock should be a core holding for investors who want exposure to MENA markets.

Initiation of coverage

Buy

Target price
SR115.00

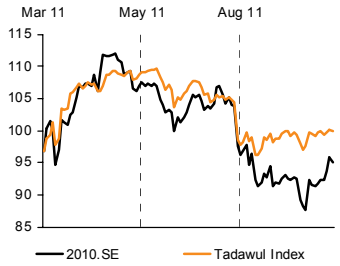
Price
SR95.00

Short term (0-60 days)
n/a

Market view
No Weighting

Price performance

	(1M)	(3M)	(12M)
Price (SR)	92.25	105.5	n/a
Absolute (%)	3.0	-10.0	n/a
Rel market (%)	2.2	-5.1	n/a
Rel sector (%)	n/a	n/a	n/a



Market capitalisation
SR285.00bn (€53.61bn)

Average (12M) daily turnover
SR646.77m (€121.93m)

Sector: European-DS Tot Mrkt
RIC: 2010.SE , SABIC AB
Priced SR95.00 at close 26 Oct 2011.
Source: Bloomberg

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue (SRm)	103,105	151,970	189,546	189,006	186,958
EBITDA (SRm)	30,757	48,502	62,382	63,404	68,186
Reported net profit (SRm)	9,074	21,529	30,357	29,802	31,727
Normalised net profit (SRm)	10,255	21,529	30,357	29,802	31,727
Normalised EPS (SR)	3.42	7.18	10.12	9.93	10.58
Dividend per share (SR)	1.50	3.50	4.05	3.97	4.23
Dividend yield (%)	1.58	3.68	4.26	4.18	4.45
Normalised PE (x)	27.79	13.24	9.39	9.56	8.98
EV/EBITDA (x)	10.90	7.11	5.34	5.13	4.45
EV/invested capital (x)	1.65	1.53	1.38	1.24	1.14
ROIC - WACC (%)	-0.62	5.24	12.20	11.50	11.30

Accounting standard: Saudi Arabia GAAP year to Dec, fully diluted
Source: Company data, Rasmala forecasts

Strong base at home; expanding elsewhere

We initiate coverage of SABIC, one of the largest chemical companies worldwide, with a Buy recommendation and target price of SR115/share. SABIC has an attractive low-cost base in Saudi Arabia and expanding presence through acquisitions and greenfield capacity build-up elsewhere, with the most recent capacity start-up at the Saudi Kayan complex. The company is also one of the largest steel producers in the Middle East.

Limited supply growth could make all the difference

Our positive view on SABIC is based on supply fundamentals of the petrochemicals industry and the lack of planned capacity additions for 2012-15. Our supply-side analysis suggests limited supply growth during this period (about 2% on average pa), and large-scale plants under consideration may even be delayed for fear of another recession. As a result, provided that global economic growth remains above 2-3%, we expect the supply-demand balance to tighten over 2011-15. We believe this, combined with an oil price outlook of US$95/bbl for 2012, will limit downside potential in petrochemical prices and spreads for the same period.

A bear-case scenario could lead to significant cuts in out forecasts

However, if the global economy stalls, petrochemicals demand and prices are likely to fall significantly. In our base case for ethylene, we assume demand growth in line with our forecast of 3.5-4% global GDP growth, and a 10% drop in chemicals prices. In our bear-case scenario, we assume lower oil and consequently even lower chemicals prices, as well as lower utilisation rates. Using this scenario, we would likely have to cut our 2012 forecasts for SABIC by about 40%. However, if we prove too negative in our base-case scenario of a 10% drop in prices, we see significant upside potential to our forecasts.

Valuation looks attractive

We believe SABIC should be a core holding in the Saudi Arabian stock market and we initiate coverage with a Buy and TP of SR115/share, suggesting 21% upside potential. We use a DCF analysis to value the stock and cross-check with peer multiples. Our target multiples suggests a 2012F EV/EBITDA of 6.1x and P/E of 11.6x.

Important disclosures can be found in the Disclosures Appendix.
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The basics

Versus consensus

EPS (SR)	Ours	Cons	% diff
2011F	10.1	10.0	+1%
2012F	9.9	9.7	+2%
2013F	10.6	10.2	+4%

Source: Bloomberg, Rasmala forecasts

Forced ranking*

Company	Rec	Upside / Downside
Industries Qatar	Buy	+29%
BASF	Hold	+25%
Orascom Construction	Buy	+23%

* by difference to target price as at time of publication. Recommendations may lie outside the structure outlined in the disclosure page.
Source: RBS and Rasmala forecasts

Key events

Date	Event
Jan 2012	2011 results

Source: Company

Catalysts 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 uptick 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.

Earnings momentum

SABIC's earnings are highly sensitive to capacity-utilisation rates of the production facilities and selling prices of its main products. We forecast a drop in utilisation rates and a drop in selling prices of about 10% in 2012, offsetting increasing volumes as a result of new capacity additions. The result is flat earnings in 2012F, compared to 2010, followed by 5-6% growth in 2013F and 2014F. We see significant upside to our forecasts, if global economic growth improves and oil and petrochemical prices are stable or move higher.

Valuation and target price

We use a DCF analysis to value SABIC, which yields a target price of SR115/share. Our valuation implies a 2012F EV/EBITDA of 6.1x and a P/E of 11.6x.

How we differ from consensus

Our recommendation is in line with Bloomberg consensus, which states 10 Buys and 3 Holds. Our forecasts are 2-4% above consensus for 2012-13.

Risks to central scenario

The risks to our investment view include lower oil prices; worse-than-expected global GDP growth resulting in weak demand for its products; increases in feedstock (gas) costs in Saudi Arabia; and political risk in the Middle East.

Key assumptions and sensitivities

Table 1 : Oil & gas price forecasts

	2011F	2012F	2013F	2014F	2015F
Crude – Brent US$/bbl	107	95	90	86	84
Naphtha	927	784	745	714	699
Natural gas (US$/MMBtu)	0.75	0.75	0.75	0.75	0.75

Source: RBS Oil Team and Rasmala forecasts

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

	2011F	2012F	2013F	2014F	2015F
Ethylene	922	859	870	864	849
Propylene	1,122	1,059	1,070	1,064	1,049
Styrene	1,384	1,200	1,236	1,273	1,311
Methanol	274	295	300	300	300
MTBE	1,044	885	900	900	900
Ethylene glycols	1,047	984	995	989	974
LDPE	1,704	1,509	1,520	1,514	1,499
LLDPE	1,272	1,209	1,220	1,214	1,199
HDPE	1,022	959	970	964	949
Polypropylenes	1,272	1,209	1,220	1,214	1,199
Polycarbonate	2,500	2,200	2,266	2,334	2,404
ABS	2,000	1,800	1,854	1,910	1,967
Ammonia	444	400	425	431	438
Urea	413	375	381	386	392
Steel bar	752	775	798	822	847

Source: Rasmala forecasts

In our bear-case scenario, we assume:

- an oil price of US$80/bbl, which drives our forecast chemicals prices;
- capacity utilisation 20% lower than our base case for all products; and
- fertiliser and steel prices at 2009 trough levels.

This analysis indicates our 2012 EPS forecast would be 42% lower than our base case.

Table 3 : Bear-case scenario sensitivities – impact of assumptions on EPS

	Oil price 2012	Cap util vs base case	Chemicals prices	Fertiliser prices	Steel prices	EPS impact 2012E
Bear case	80	-20%	Linked to oil price	2009 level	2009 level	-42%

Source: Rasmala estimates

Contents

Executive summary

We initiate coverage on SABIC with a Buy recommendation and a target price of SR115/share. Our positive view is largely based on supply fundamentals of the petrochemicals industry and SABIC's leading position in the industry.

Well-positioned globally

SABIC, the largest listed company in the MENA region by market capitalisation, is one of the largest chemical companies worldwide, with an attractive low-cost base in Saudi Arabia and is expanding through acquisitions and building greenfield capacities elsewhere. It has ambitious plans to increase its production from 67mtpa in 2010 to 120mtpa in 2020, and has the cash flow and balance sheet (we forecast net debt/EBITDA of 0.8x for 2011) to do so. EBITDA margins are high (we forecast 33% for 2011), but have been falling from the mid-40s with the addition of higher-cost production outside Saudi Arabia. SABIC is also one of the largest steel producers in the Middle East.

Supply fundamentals could make all the difference

New supply limited for an extended period,...

With fears of a global recession, chemicals may not be the obvious area for investors to consider; however, 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 the business advisory firm Chemical Market Associates, Inc (CMAI) expects supply to grow less than 2% in 2011-15. We believe this, combined with an oil price outlook of US$95/bbl, will limit any downside potential in petrochemical prices and spreads.

Demand will determine if the super cycle will occur

... but demand could spoil the party

Hence, provided global economic growth remains above 2-3%, we expect the supply-demand balance to tighten over 2011-15. However, as petrochemical demand is closely correlated to GDP growth, the relevance of the fear of a double-dip recession is material for SABIC. Whether a global recession will materialise is yet to be seen, but RBS economists in Asia, the main end market of Middle East petrochemicals, are still relatively optimistic and expect continued growth in Asia, even if lower than in previous years, to be able to offset weakness in Europe and the US. In our base-case scenario, we assume global growth of about 3.5-4.0% in 2012. Importantly, our China strategist Wendy Liu remains optimistic on China and expects Chinese GDP to grow 8-9% over the next five years.

We expect ethylene operating rates to move higher over 2011-15

Economic growth combined with a lack of new supply coming to 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 mainly determine if 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 and 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.

Under a bear-case scenario, we would have to cut our forecasts by just over 40%

Against this backdrop of a potential slowdown, we look at a scenario, where we assume:

- an oil price of US$80/bbl, which drives our forecast chemicals prices;
- capacity utilisation 20% lower than in our base case for all products; and
- fertiliser and steel prices at 2009 trough levels.

This analysis would result in a 2012 EPS forecast for SABIC that is 42% lower than our base case. However, if global GDP growth remains positive, our analysis suggests petrochemical demand could remain relatively tight during 2012. We believe we have been reasonably cautious in our forecasts, assuming a drop in both utilisation rates and prices for 2012. If we prove to be too negative, we see significant upside potential to our forecasts.

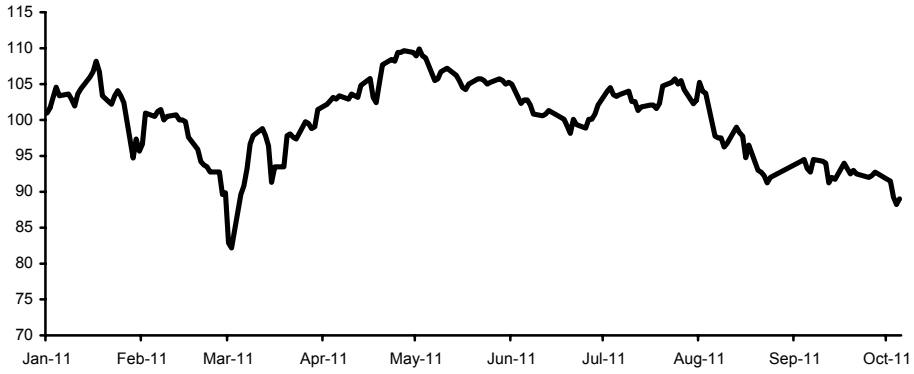
Performance and valuation

We value SABIC using a DCF analysis, which yields our target price of SR115/share, suggesting 21% upside potential. Our target price implies a 2012F EV/EBITDA of 6.1x and P/E of 11.6x.

Share price performance

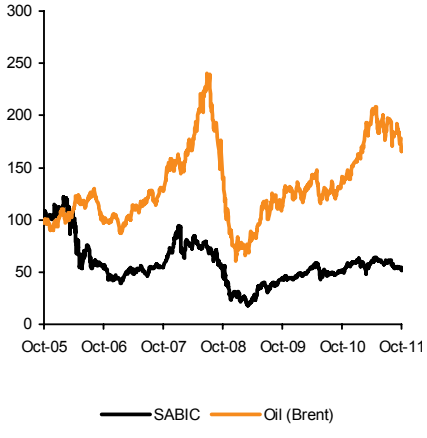
SABIC's stock price has fallen 12% since the beginning of the year, we believe driven by the political unrest in the Middle East, a somewhat lower oil price and, in the past few months, the cloudy outlook for global economic growth. At the same time, SABIC has reported (Bloomberg) consensus-beating quarterly results so far this year, and the company has a relatively positive outlook. Even compared with its peers and the oil price, SABIC's share price has been lagging.

Chart 1 : SABIC – share price performance (SR)



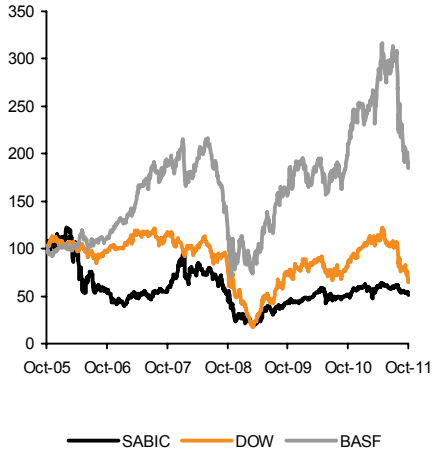
Source: Bloomberg

Chart 2 : Relative performance versus oil price



Source: Bloomberg

Chart 3 : Relative performance versus peers



Source: Bloomberg

Valuation

We value SABIC on a DCF basis, which yields a fair value of SR115/share. In our analysis, we assume a cost of equity of 11.3% (a risk-free rate of 2.5%, country- and stock-specific risk of 8.0%), beta of 1.1x and debt weight of 20%, yielding a WACC of 10.0%. We have explicit forecasts for 2011-20, after which we apply a terminal growth rate of 2%.

Table 4 : WACC computation

Risk-free rate	2.5%
Risk premium	8.0%
Beta	1.1
Cost of equity	11.3%
Cost of debt	5.0%
Tax rate	5.0%
Equity	80%
Debt	20%
WACC	10.0%

Source: Rasmala estimates

Table 5 : DCF valuation

SRm	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
EBITDA	**62,382**	**63,404**	**68,186**	**71,581**	**71,181**	**65,181**	**65,038**	**64,845**	**64,603**	**64,312**
D&A	-11,269	-11,991	-12,728	-13,139	-13,527	-13,893	-14,238	-14,564	-14,871	-15,161
EBIT	51,113	51,413	55,458	58,441	57,654	51,288	50,800	50,281	49,733	49,152
Taxes	-2,756	-2,968	-3,725	-4,535	-4,501	-5,027	-5,016	-5,003	-4,987	-4,969
NOPAT	48,357	48,446	51,733	53,906	53,153	46,261	45,784	45,279	44,746	44,183
% growth in NOPAT	36.6%	0.2%	6.8%	4.2%	-1.4%	-13.0%	-1.0%	-1.1%	-1.2%	-1.3%
Working capital change	-7,911	-3,845	3,388	-3,779	-531	782	-2,127	-132	294	-1,214
Capital expenditure	-15,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000
FCF	36,715	36,591	47,849	43,266	46,148	40,935	37,895	39,710	39,911	38,129

Source: Rasmala forecasts

Peer multiples

We compare our valuations with peers outside the region, but note that MENA multiples tend to be higher, reflecting higher EBITDA margins and lower tax rates than elsewhere. The peers include large chemical companies in Europe, the US and Asia, and petrochemical companies in Saudi Arabia.

SABIC is currently trading at 5.3x 2011F and 5.1x 2012F EV/EBITDA and 2012F P/BV of about 1.8x, in our view, discounting a deteriorating outlook for global economic growth. These multiples are in line with peers such as BASF, but below Dow Chemicals' current multiples. Our target multiples imply 2012F EV/EBITDA of 6.1x and P/E of 11.6x.

Table 6 : Chemicals – comparable multiples

	Price	Mkt cap	P/E			EV/EBITDA		
	(lc fx)	(US$m)	2011F	2012F	2013F	2011F	2012F	2013F
BASF	53.85	65,291	8.1	7.3	7.1	5.2	4.8	4.4
Dow Chemical	26.89	31,763	10.0	9.1	7.8	9.1	6.4	5.8
LyondellBasell	31.74	18,029	7.0	7.6	6.0	4.0	4.0	3.4
Formosa Plastics	88.10	16,770	9.8	8.6	8.3	6.8	5.7	5.2
PTT Chemical Pcl	106.00	5,263	6.2	4.5	4.1	4.5	2.9	2.6
Methanex	24.39	2,273	14.4	7.3	8.6	11.7	4.6	5.3

Priced as at close of 26 October 2011.
Source: RBS forecasts for BASF, Formosa Plastics and PTT Chemical Pcl, others Bloomberg consensus forecasts

Table 7 : Saudi petrochemicals – valuation multiples

	Mkt cap	P/E		EV/EBITDA		EBITDA margin	
	SRm	2011F	2012F	2011F	2012F	2011F	2012F
Saudi Kayan Petrochemical Company	26,625	63.4	10.9	35.48	11.01	59.0%	44.6%
Yanbu National Petrochemical Company	24,806	8.1	8.2	8.20	8.09	48.8%	47.2%
National Industrialization Co	22,074	9.0	9.1	6.74	6.87	31.7%	30.1%
Rabigh Refining and Petrochemical Co	19,798	12.4	7.7	12.00	9.16	7.7%	8.8%
Saudi National Petrochemical Co	10,344	-	12.5	-	9.17	-	37.8%
Saudi Industrial Investment Group	8,663	15.0	8.6	25.90	8.35	18.5%	27.9%
Saudi International Petrochemical Co	7,205	12.1	11.2	7.70	7.32	48.7%	48.3%
Sahara Petrochemical Co.	5,602	9.1	8.3	18.27	12.73	24.8%	26.9%
Advanced Petrochemical Company	3,916	8.3	9.3	6.53	6.84	26.0%	25.9%
Methanol Chemicals Company	1,405	17.8	11.3	9.75	8.15	35.3%	39.1%

Priced as at close of 26 October 2011.
Source: Bloomberg consensus

Key product price forecasts

We forecast a decline of about 10% in petrochemical prices in 2012, assuming a lower average oil price. However, under this scenario, prices will remain well above the level seen in the last trough in 2009.

Oil price will be the key driver

Oil prices are a key driver

As high-cost producers are using naphtha, rather than ethane, as their main feedstock, petrochemical prices show a high correlation with oil prices. The higher the oil price, the more favourable it is for chemicals prices.

We use the RBS oil price forecast as a base, which assumes an average Brent price of US$107/bbl for 2011 and a downward trend in prices from 2012, to reach US$84/bbl in 2015, which serves as the long-term real oil price forecast (inflated at 2.5% pa). Despite recent weakness in response to global economic growth concerns, Brent oil prices are still up on the year.

Table 8 : Oil & gas price forecasts

	2010	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
Crude – Brent US$/bbl	80	107	95	90	86	84	86	88	90	93	95
Naphtha (US$/tonne)	692	927	784	745	714	699	715	732	749	766	784
Natural gas (US$/MMBtu)	0.75	0.75	0.75	0.75	0.75	0.75	2.00	2.00	2.00	2.00	2.00

Source: Bloomberg, RBS Oil Team and Rasmala forecasts

Petrochemical prices have already declined by almost 15% since the beginning of August, but are still above 2010 levels. The oil price assumption is the main driver for the decline we forecast for petrochemicals prices in 2012 from current levels, as we maintain petrochemical spreads relatively stable compared with 2011. Our resulting petrochemical price forecasts are down on average 10% in 2012, but the petrochemical prices remain at a relatively high level and thus we expect cash margins to remain high for SABIC. However, we note that any expectation of lower chemical prices could result in a wait-and-see approach by customers and could lead to destocking and a short-term impact on volumes.

Table 9 : Key price assumptions (US$/tonne)

	2011E	2012E	2013E	2014E	2015E
Ethylene	922	859	870	864	849
Propylene	1,122	1,059	1,070	1,064	1,049
Styrene	1,384	1,200	1,236	1,273	1,311
Methanol	274	295	300	300	300
MTBE	1,044	885	900	900	900
Ethylene glycols	1,047	984	995	989	974
LDPE	1,704	1,509	1,520	1,514	1,499
LLDPE	1,272	1,209	1,220	1,214	1,199
HDPE	1,022	959	970	964	949
Polypropylenes	1,272	1,209	1,220	1,214	1,199
Polycarbonate	2,500	2,200	2,266	2,334	2,404
ABS	2,000	1,800	1,854	1,910	1,967
Ammonia	444	400	425	431	438
Urea	413	375	381	386	392
Steel bar	752	775	798	822	847

Source: Rasmala estimates

Cheap gas is key competitive advantage

Cheap gas is the main driver to invest in petrochemicals and fertilisers, which have become the region's key strategic industries. For Saudi Arabia, we are not pencilling in an increase in gas prices yet, but if it were to happen we expect the impact to be minimal.

SABIC has an advantageous cost position in Saudi Arabia

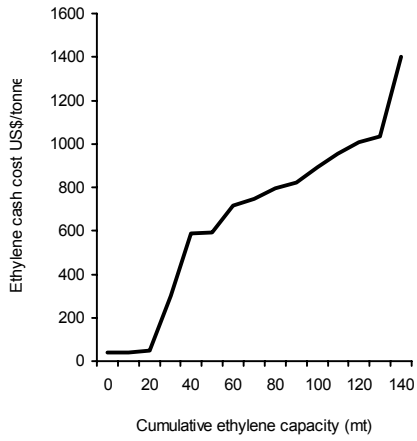
Saudi Arabian petrochemical producers are at the very low end of the global cash cost curve, and the widening differential between global gas prices has strengthened their position in recent years. Gas prices are fixed in most GCC countries, except in Qatar, where they are variable but still well below global levels.

The mix has been changing for petrochemicals

But even within petrochemicals, cost advantages differ from product to product. Ethylene can be produced by a wide variety of hydrocarbon feedstocks, but the end products vary as a result. Naphtha, gasoil and condensates, commonly used in Europe and Asia, yield more propylene, C4 olefins and aromatics as co-products. Ethane and propane, the dominant feedstocks in North America and the Middle East, produce only ethylene and propylene. Because naphtha costs are more similar across regions than ethane, the polypropylene cost curve is flatter than for ethylene. In addition, plants that produce just ethylene and propylene are cheaper to construct and less complicated to operate. According to CMAI, in 2010, 50% of global ethylene production was based on naphtha and 32% on ethane. In North America and the Middle East, the average use of ethane is 60-70% in ethylene production; in Europe, around 10%.

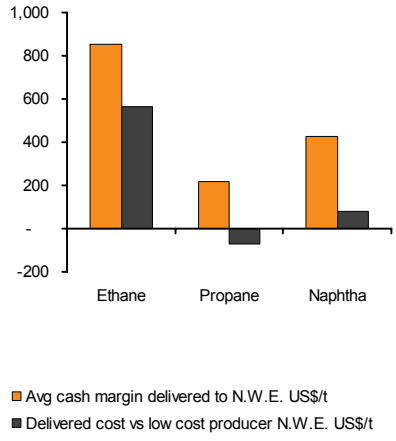
With a fixed gas price, the cost advantage is the highest during times that selling prices are high, and vice versa. The ethylene cost curve moves up and down with changes in crude oil and natural gas price swings, but also to the right, with additions of new low-cost additions in the Middle East.

Chart 4 : Current ethylene cash cost curve for global capacity



Source: CMAI, Rasmala

Chart 5 : Ethane-based production in Mideast the most competitive (2010)



Source: CMAI, Bloomberg

Average cash costs remain below US$100/tonne

For its production in Saudi Arabia, SABIC has a clear cost advantage, paying US$0.75/MMBtu for natural gas and a 30% discount to global prices for liquids. Outside the region, it pays market prices, which means group EBITDA margins are lower than for some other petrochemical producers that have all production based in the region.

Gas prices in Saudi Arabia could rise, but for now we assume it will remain at US$0.75/MMBtu

We discussed our view on natural gas prices in the region and the cost implications, particularly in Saudi Arabia, in our sector note of 13 October 2011 (*'MENA Fertilisers: Fertile growth opportunities'*) and in our MENA strategy note of 14 October 2011 ('*Mena Strategy: Natural gas in the Mena region*'). In summary, we believe it is inevitable that in the long term gas prices will rise, but we do not assume an increase in the short term for now.

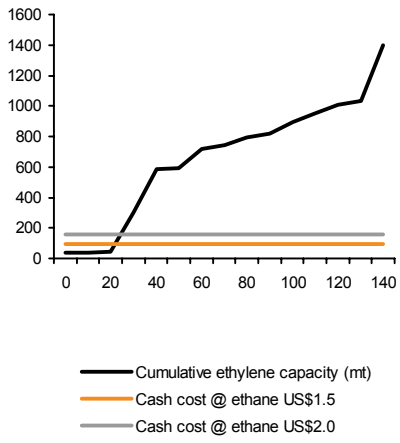
Ethane feedstock costs could double

Nevertheless, the market has been widely expecting a price increase in Saudi Arabia, from US$0.75/MMBtu currently to US$1.25/MMBtu. We estimate that for every US$1/MMBtu increase in the natural gas price, the average ethylene cash cost will rise by about US$60/tonne, assuming no change in co-product credits, or other costs (utilities, catalysts and chemicals). Therefore, if the gas price in Saudi Arabia were to increase from US$0.75 to US$1.25, we estimate that the average ethane feedstock cost for ethylene increases from US$40-50 to US$70-80/tonne, still well below costs in other regions, even taking into account freight costs of up to US$200/tonne currently.

But fluctuations in the oil price have a more profound impact on profitability

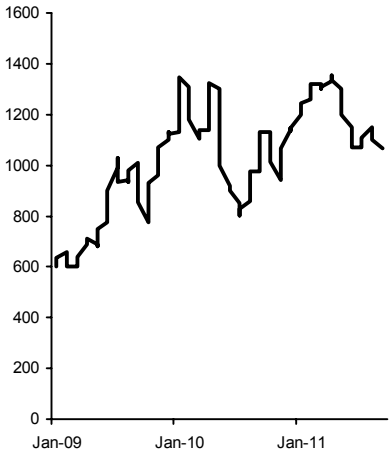
About half the new crackers in the kingdom have ethane as a feedstock, the rest heavier feedstocks. Some recent capacity additions (Kayan, etc) have already been based on a mixed-feedstock cracker, and the latest projects under consideration are destined to be oil-based or mixed feed, including the largest petrochemical project, the Aramco–Dow US$15bn petrochemicals complex in Jubail, which was recently given the go-ahead. The shift away from gas to heavier feedstocks has a more profound impact on margins than an increase in natural gas prices, even if these are doubled or tripled. Liquid prices in Saudi Arabia are at a 30% discount to market prices, rather than being fixed like ethane. It takes about 3.3t of naphtha to produce 1t ethylene; hence the sensitivity to a change in oil prices is high and has a potentially large impact on cash costs. For SABIC, we have assumed a gas-to-liquids ratio for its Saudi Arabian production base of 70:30.

Chart 6 : Cost advantage for ethane seems here to stay



Source: CMAI, Rasmala estimates

Chart 7 : Ethylene prices support strong cash margins (US$/t)



Source: Bloomberg

Supply looking good, demand main variable

The petrochemical supply/demand balance has been tight so far this year, and, with limited new supply, we expect it to remain so. We see downside price risk from continued talk of the strength of the economy and lower oil prices.

Petrochemicals – will the super cycle materialise?

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 CMAI expects supply to grow less than 2% in 2011-15. In our view, this will limit any downside potential in petrochemical spreads.

Demand side could be volatile

In the past year, the chemicals sector has enjoyed strong upward momentum, benefiting from tight markets and strongly increased selling prices. The economic recovery and a lack of new supply coming to the market in the near future have resulted in much talk in the market about the super cycle for petrochemicals, in which economic growth combined with limited new capacity drives strong petrochemical earnings for an extended period, at least until 2015.

However, there are still uncertainties about this occurring, especially on the demand side, especially if the fear of a double-dip recession materialises. Petrochemical demand is closely correlated with GDP growth, and we expect demand for ethylene, the largest petrochemical product and as such a proxy for the wider petrochemicals industry, to grow at a similar rate or above – hence the relevance of the fear of another recession, which would have a direct negative impact on industrial production and consequently demand for chemicals.

But we do not expect much growth in supply in 2011-15

Much of the excitement for a super cycle stems from the outlook for new chemical plants, or the lack thereof. After substantial capacity increases over the past two years (almost a 7% increase in 2010 alone), we expect the next few years to be relatively quiet and estimate that capacity will grow well below global economic growth of 3.5-4.0% according to our economists and even lower (less than 2%) in 2011 and 2012. With supply limited, the demand side will be the main determinant for the super cycle to materialise.

RBS economists expect 4% GDP growth in 2011-12

Whether a global recession will materialise is yet to be seen, but RBS economists in Asia (the main end market of Middle East petrochemicals) are still relatively optimistic and expect continued growth in Asia to offset weakness in Europe and the US. For global growth, RBS economists still forecast about 4% GDP growth in 2011 and 2012, and, importantly, our China strategist Wendy Liu remains optimistic on China and expects its GDP to grow 9% in 2012 and 8-9% on average per annum over the next five years. This bodes well for operating rates for petrochemicals and thus, for now, petrochemical earnings growth seems sustainable, especially if global uncertainty results in the cancellation or delay of new capacities.

Table 10 : Global GDP forecasts

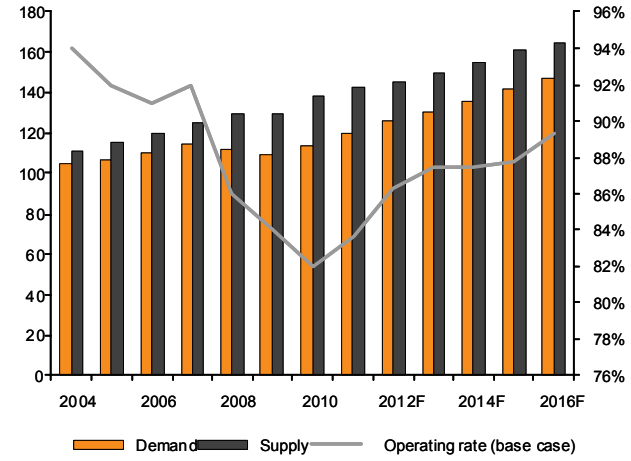
	GDP growth (%)			
	2009	2010	2011F	2012F
US	-3.5	3.0	1.7	2.1
Euro area	-4.3	1.7	1.6	1.1
UK	-4.9	1.4	1.6	1.2
Japan	-6.3	4.0	-0.5	2.3
G-4	-4.2	2.6	1.3	1.8
Asia (ex-Japan)	6.4	9.6	8.1	7.7
- China	9.1	10.3	9.6	9.0
- India	6.8	10.1	7.6	7.6
Emerging Europe and SA	0.5	4.7	4.4	3.7
Latin America				
- Brazil	-0.6	7.5	4.0	4.0
- Argentina	-0.9	9.1	6.6	3.1
RBS- World	-1.0	5.0	3.9	4.0

Source: IMF, RBS forecasts

Historically, ethylene demand has grown on average 1.0-1.5x GDP, but could be higher when the economy slows rapidly or comes out of a recession. In our base case, we use a multiplier of around 1.3x, in line with the RBS view on petrochemicals in Asia (see *Petrochemicals Journal: Fear overtaking fundamentals*', by Avin Sony, published on 16 September 2011).

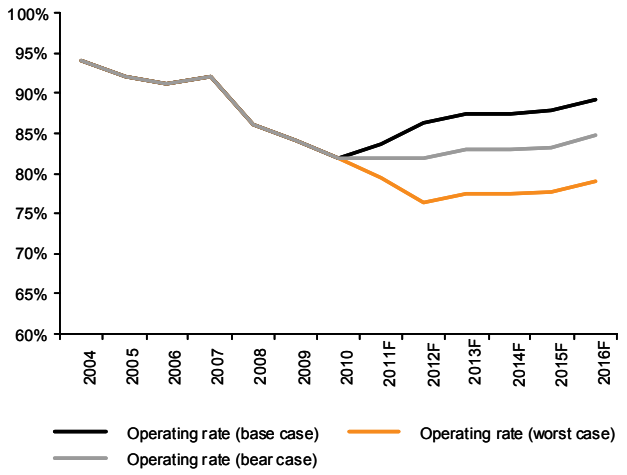
In this scenario of petrochemical demand growth of about 5% during 2011-12, operating rates should rise steadily from the low to mid-80% level achieved in 2008-10 to about 88% by 2013, sufficient to ensure strongly improved margins for the global chemical industry. However, in a bear-case scenario of 2-3% growth, in line with supply growth, operating rates are more likely to remain at current levels during 2011-13, whereas we expect operating rates to fall under a worst-case scenario of no global growth in 2012, resulting in a drop in petrochemicals demand of about 2% that year.

Chart 8 : Ethylene global supply/demand balance and operating rates



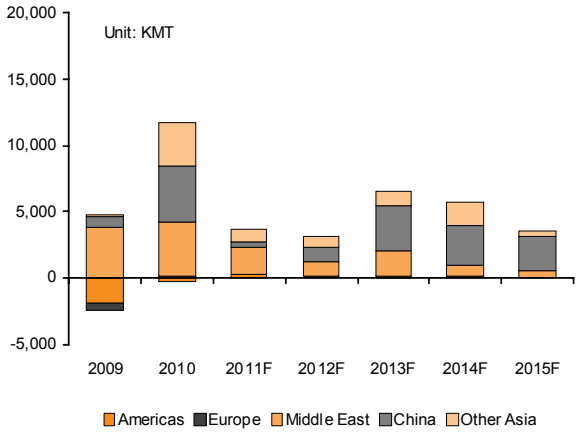
Source: CMAI, ICIS, Rasmala forecasts

Chart 9 : Global ethylene operating rates under different scenarios (%)



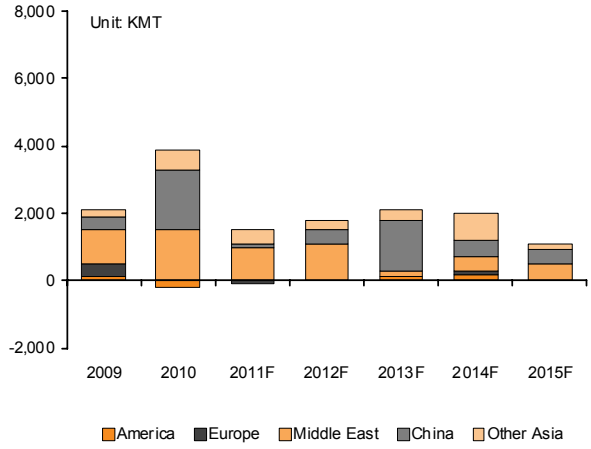
Source: CMAI, ICIS, Rasmala forecasts

Chart 10 : Ethylene capacity additions



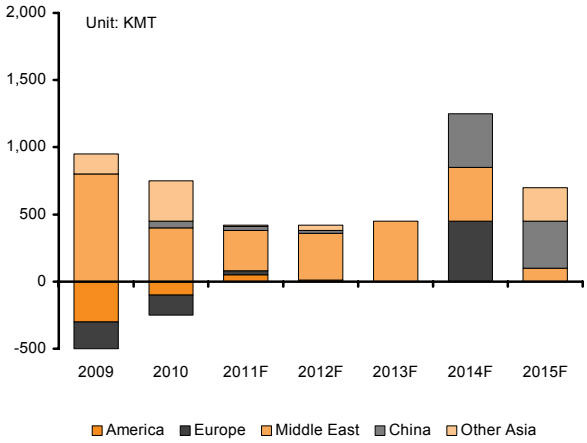
Source: CMAI, RBS forecasts and Rasmala forecasts

Chart 11 : HDPE capacity additions



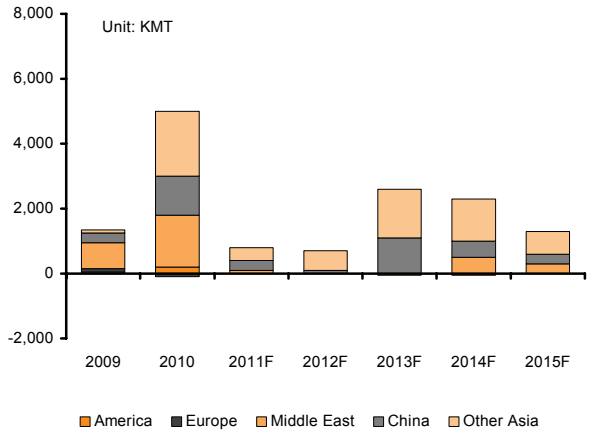
Source: CMAI, RBS forecasts and Rasmala forecasts

Chart 12 : LDPE capacity additions



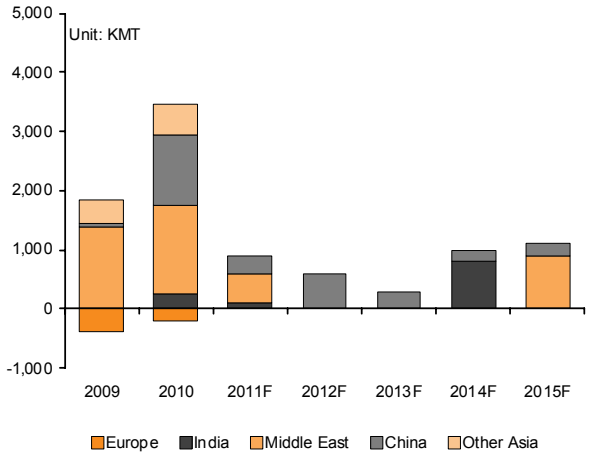
Source: CMAI, RBS forecasts and Rasmala forecasts

Chart 13 : LLDPE capacity additions



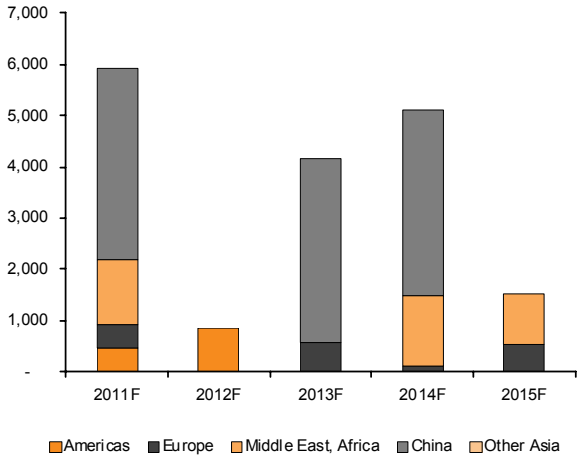
Source: CMAI, RBS forecasts and Rasmala forecasts

Chart 14 : MEG capacity additions



Source: CMAI, RBS forecasts and Rasmala forecasts

Chart 15 : Methanol capacity additions



Source: CMAI, RBS forecasts and Rasmala forecasts

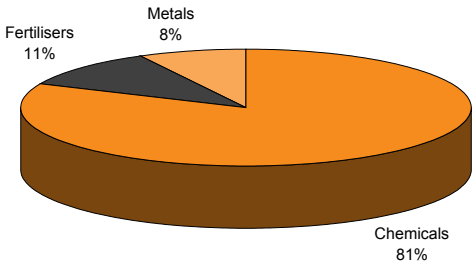
SABIC's ramping up of new capacity

SABIC's growth has been impressive over the past 10 years, largely the result of new capacity additions and acquisitions. The company is ramping up several large projects in Saudi Arabia and China.

Organic growth and likely acquisitions drive future growth

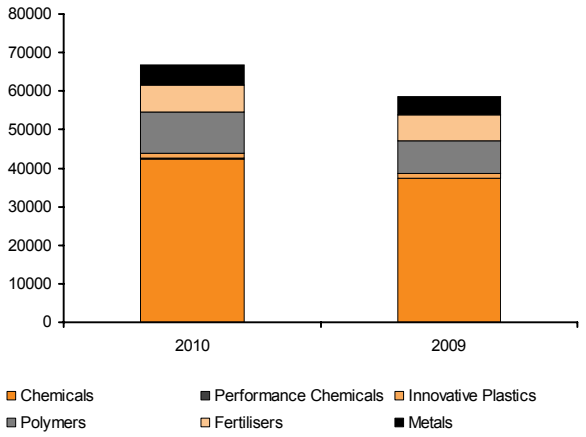
SABIC is predominantly a chemicals producer, but also has large capacities in fertilisers and metals. In 2010, chemicals accounted for 81% of its production, fertilisers 11% and metals 8%. In 2010, its total production amounted to about 67mt, an increase of 8mt, and the company is targeting to increase this to 120mt by 2020. This seems ambitious, but SABIC has several projects in the start-up phase and with annual capital expenditures of US$5bn-10bn and a healthy balance sheet, we expect SABIC to continue its growth path.

Chart 16 : Breakdown of production by segment, 2010



Source: Company data

Chart 17 : Production of main product categories (ktpa)

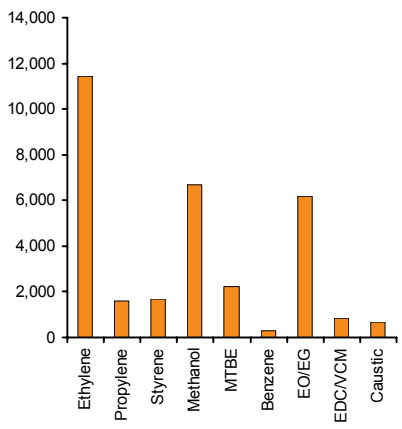


Source: Company data

One of the largest ethylene producers globally

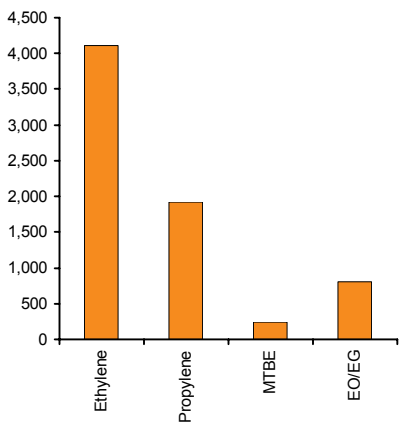
The company is among the top petrochemicals companies and market leaders globally in the production of polyethylene, polypropylene and advanced thermoplastics, glycols, methanol and fertilisers – and it is one of the largest steel producers in the Middle East. The company does not provide detailed overviews of capacities and production by product, but we estimate it has about 15mtpa of ethylene capacity (including minority shares), in Saudi Arabia, Europe and China, making it one of the largest producers globally. It is also a major player in the methanol market, with a capacity of almost 7mtpa.

Chart 18 : Basic and intermediate chemical capacities by end-2012 – Saudi Arabia (ktpa)



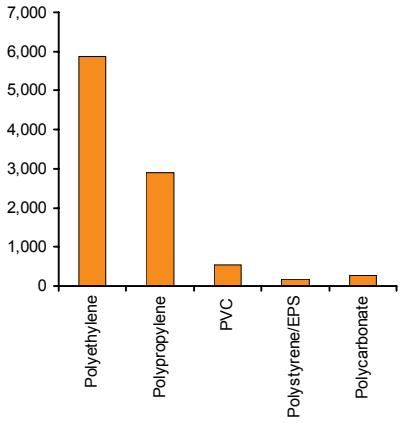
Source: Company data, Rasmala estimates

Chart 19 : Basic and intermediate chemical capacities by end-2012 – other regions (ktpa)



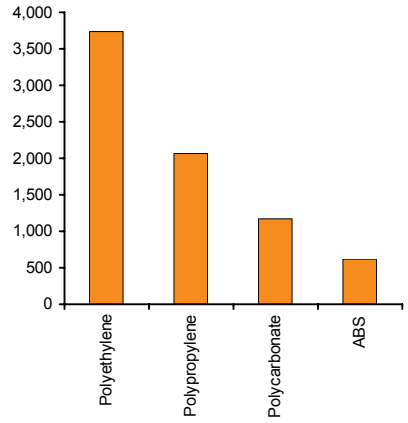
Source: Company data, Rasmala estimates

Chart 20 : SABIC: polymer capacities by end-2012 – Saudi Arabia (ktpa)



Source: Company data, Rasmala estimates

Chart 21 : SABIC: polymer capacities by end-2012 – other regions (ktpa)



Source: Company data, Rasmala estimates

Several projects in start-up phase

For SABIC, the main new capacities being ramped up are at Yansab, Saudi Kayan and Sharq in Saudi Arabia, and Tianjin in China, a 50:50 joint venture with Sinopec.

Tianjin

3.2mtpa capacity

Last May, SABIC began commercial production in Tianjin, China, in a 50:50 joint venture with Sinopec. The project has total capacity of about 3.2mtpa of ethylene and derivatives products and caters to the domestic market. It was built at a cost of US$2.7bn. Besides a 1mtpa ethylene cracker, the complex also has a 400ktpa ethylene oxide/ethylene glycol, a 300ktpa LLDPE, a 300ktpa HDPE and a 450ktpa PP facilities.

Yansab

SABIC has a 52% stake in Yansab

Established in 2006, Yanbu National Petrochemical Company (Yansab) is a Saudi Arabia-based petrochemical company that produces basic chemicals (ethylene, propylene), polymers (polypropylene, high and low density polyethylene) and intermediates (ethylene glycol), and other petrochemicals mostly for export to Asia and Europe. Yansab launched its commercial operations in March 2010. SABIC is majority shareholder with a 52% stake. The strong tie-up with SABIC gives the company an advantage to access SABIC's global marketing network and distribution channels.

Total production capacity of about 4mtpa

The Yanbu-based facilities are designed to produce 4.0m tonnes of different grades of petrochemical products ranging from basic chemicals to intermediaries to polymers. Most of the plant's capacity is dedicated to produce ethylene and its related intermediaries and polymer products.

Saudi Kayan

Established in 2007 as a partnership between SABIC (which has a 35% stake and management control) and Al Kayan Petrochemical Co, Kayan produces propylene, polypropylene, ethylene, high- and low-density polyethylene, polycarbonate, ethylene glycol, ethylene oxide, acetone, and other chemical and petrochemical products. It has a portfolio of products, which is more downstream than most of SABIC's other production facilities in Saudi Arabia. In particular, the company has a large polycarbonate production facility with capacity of 260kt at its Jubail Industrial city complex.

Production capacity of more than 5mtpa

Commercial production has started

Kayan operates a petrochemical complex at Jubail Industrial City. Kayan began trial production at its key units in 2H10 and began commercial operations in October 2011. The company expects the complex to be fully operational in 2013 with annual capacity of 5.5mtpa. In January 2011, the

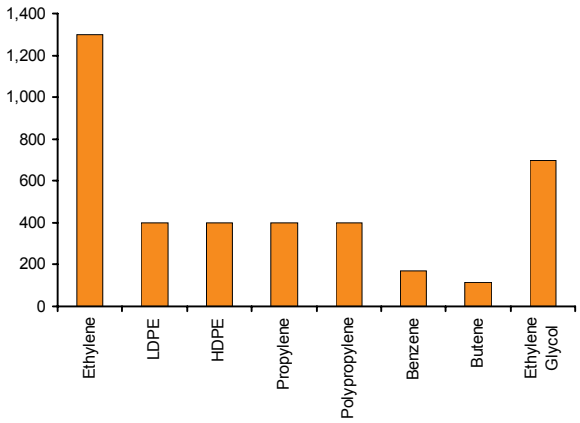
plant became the first Middle East exporter of acetone, an organic compound used to make polycarbonate.

Major player in polycarbonates

SABIC has had a large presence in polycarbonates since 2007, when the company acquired the GE Plastics business, now called SABIC Innovative Plastics (SIP). Recently, SABIC announced it would build a 260kt polycarbonate plant in China, in a joint venture with Sinopec, bringing SABIC's total capacity to about 1.7mtpa, including Saudi Kayan's and SIP's capacities.

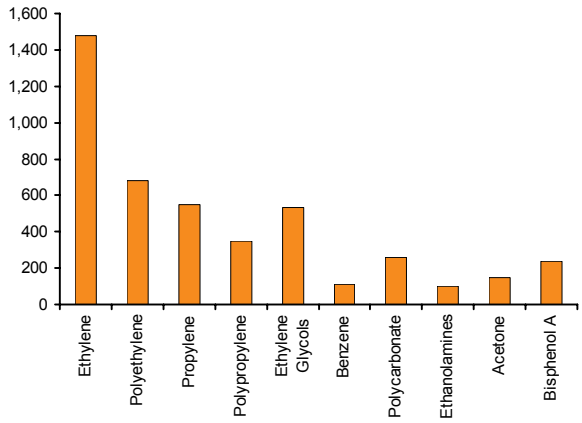
In January 2011, Kayan signed an agreement with Saudi Acrylic Acid Co. (SAAC) and a joint venture between the US-based Dow Chemical Corporation and Saudi Aramco to build an SR1.8bn n-Butanol plant in Jubail. The three parties hold equal stakes in the project, and production is scheduled to begin by the end of 2014.

Chart 22 : Current Yansab plant capacities (ktpa)



Source: Company data, Rasmala estimates

Chart 23 : Current Saudi Kayan plant capacities (ktpa)



Source: Company data, Rasmala estimates

Acquisitions: part of SABIC's growth

We expect more acquisitions

The company has completed several large acquisitions in the past decade (DSM's polymers business, GE Plastics), which have helped the company diversify its portfolio geographically and downstream in the value chain.

SABIC made its first large foray abroad with the acquisition of DSM's polyolefins business in the Netherlands and has made several acquisitions since the beginning of 2007. The acquisition of GE Plastics in 2007 was SABIC's largest, and one of the largest in the Gulf region, with a total deal value of US$11.6bn. Geographical expansion, a move further down the value chain and gaining access to technology were SABIC's main targets.

In September 2011, SABIC entered into an agreement to purchase an equity stake in INPRO, a joint venture to collaborate in automotive production innovation. SABIC will join Daimler, Siemens, ThyssenKrupp and Volkswagen as equity owners in the group. The deal is expected to be closed by the end of 2011.

Company overview

SABIC is one of the world's leading petrochemical manufacturers, with operations across the Middle East, Africa, Asia Pacific region, the Americas and Europe. It has an ambitious target to increase its global production to 120mtpa by 2020, from about 67mtpa currently.

Company description

A global leader

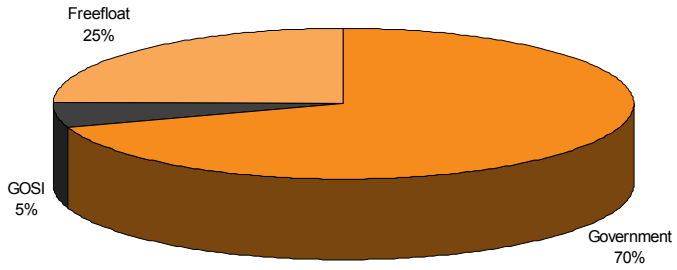
SABIC, headquartered in Riyadh, Saudi Arabia, is the largest publicly listed company by market capitalisation in the MENA region, manufacturing and marketing chemicals, fertilisers, plastics and metals. SABIC is one of the world's leading petrochemical manufacturers with operations across the Middle East, Africa, the Asia Pacific region, the Americas and Europe. The company employs around 33,000 people and has19 manufacturing complexes operated by 18 affiliates. It has major operations in the industrial cities of Al-Jubail, Dammam near the Arabian Gulf and Yanbu near the Red Sea.

SABIC's stated strategy focuses on its marketing efforts, creating high value-added products to complement its core commodity materials, improving productivity while maintaining high technical and quality standards and acquiring operating units judiciously to build its capabilities and geographical presence.

Shareholding structure

The Saudi government owns 70% of the company and 30% by private entities.

Chart 24 : SABIC shareholder structure



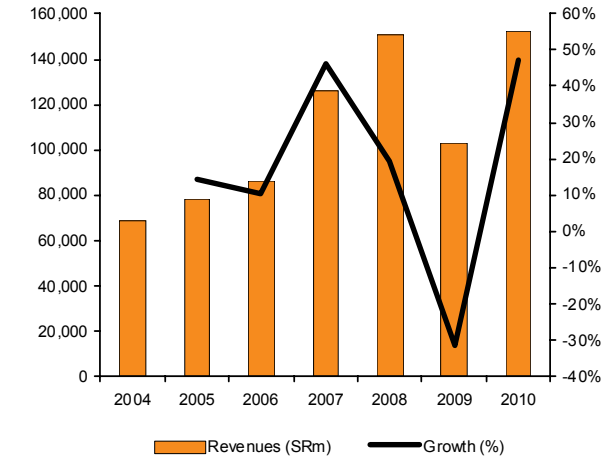
Source: Zawya

Strong historical performance

The company reports three main operating segments: chemicals, fertilisers and metals. The chemicals segment accounted for more than 80% of the company's total 2010 revenues and operates through four business units: Olefins and Gases, Aromatics and Chlor-Alkali, Oxygenates, and Glycols. The chemicals business unit achieved production of 42.3m tonnes in FY10.

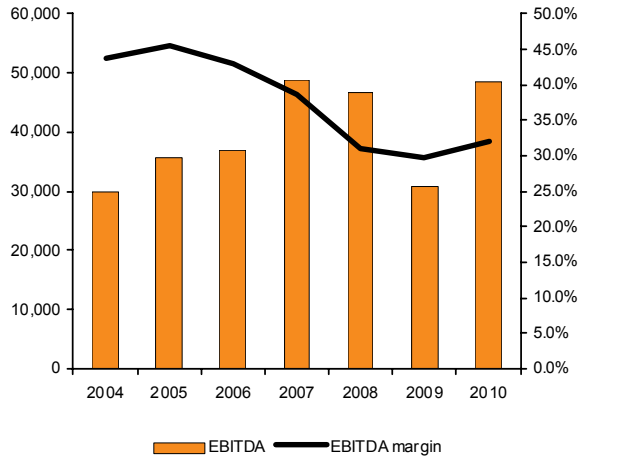
Revenues grew at an average rate of 14.2% per annum and EBITDA at 8.4% during 2004-10, with only the 2008/09 downturn denting its growth path. The performances in 2010 and 9M2011 were boosted by the start of commercial operations of Sharq (Eastern Petrochemical Company), Yansab (Yanbu National Petrochemical Company), SABIC's joint venture SSTPC (Sinopec SABIC Tianjin Petrochemical Company) in Tianjin, China, and Saudi Kayan in Al-Jubail.

Chart 25 : Revenue trend (2004-10)



Source: Company data, Rasmala

Chart 26 : EBITDA and EBITDA margin (2004-10)



Source: Company data, Rasmala

Company history

SABIC was established in Saudi Arabia in 1976 by royal decree to exploit the country's natural gas supply to produce value-added commodities such as chemicals, polymers and fertilisers. The first SABIC joint venture plant came on stream in 1983, followed by a quick succession of several affiliates. Following its acquisition of the petrochemicals division of Netherlands' DSM, which also represented the company's first expansion beyond its Saudi Arabia base, SABIC became the 11th-largest petrochemicals company worldwide. The company's total production was 6.3m tonnes in 1985, reaching 67m tonnes in 2010.

Figure 1 : SABIC – a brief history

Launch onto the worldwide market (1976 - 1985)

- **1976:** Established in Saudi Arabia to exploit the country's natural gas supply
- **1979**: Created its first manufacturing affiliates, AR-RAZI, also known as the Saudi Methanol Company, in partnership with Mitsubishi Gas Chemical Company
- **1982**: Most of SABIC's group of companies had been formed and were under construction
- **1983:** First SABIC joint venture plant came on stream in 1983, followed by a quick succession of several affiliates
- **1984**: Went public with Saudi government maintaining a 70 percent stake in the company
- **1985:** Total production capacity reached 6.2 million metric tons per year
- **1986:** Total production had topped nine million metric tons. The company became one of the country's major employers, with more than 8,000 people on payroll

Expanded its operations with addition of new affiliates (1986 - 2002)

- **1988**: Began asserting itself on the worldwide market by opening offices in London, New York, Tokyo and Hong Kong
- **1991**: Began construction on its Industrial Research and Technology complex
- **1993**: Opened a marketing subsidiary in India
- **1994**: Production jumped to more than 20 million metric tons. The company's sales had topped SR 10 billion
- **1997**: Houston, Texas, became the site of SABIC's first international technology center
- **1999**: Total capacity reached to 25 million metric tons
- **2000:** Entered into a joint venture with Japan's New Energy and Industrial Technology Development Organization, to conduct joint research on plastic processing and inspection
- **2002:** SABIC Europe was created after the acquisition of the petrochemicals business of Dutch group DSM

Continues its expansion with strategic alliances and joint ventures (2003 - present)

- **2003:** SABIC and Sud-Chemie formed a 50:50 partnership to acquire Scientific Design of New Jersey, a process and catalyst related chemical technology company
- **2004:** Started the construction of a new metals facility in 2004 that increased the existing metal production capacity of the firm by 500,000 metric tons
- **2006:** Formed a 70:30 polystyrene joint venture with Turkey-based Baser Petrokemya
- **2007:** Completed the acquisition of Huntsman's UK base chemicals and polymers business for $685 million
- **2008**: Signed a heads of agreement (HOA) towards forming a joint venture company with China Petroleum and Chemical Corporation (Sinopec)
- **2009**: Signed a memorandum of understanding (MOU) with Saudi International Petrochemical (SPICHEM) for setting up new projects in Jubail
- **2011**: Accelerated growth in Asia with key investments in polycarbonate and new technology and innovation centers in China and India

Source: Company data, Rasmala

Table 11 : SABIC's consolidated affiliates (2010)

Company	Direct or indirect ownership, 2010 (%)
SABIC Industrial Investments Company (SIIC) and its subsidiaries	100
SABIC Luxembourg S.a.r.l.(SLUX) and its subsidiaries	100
SABIC Asia Pacific Pte. Ltd. (SAPPL) and its subsidiaries	100
Arabian Petrochemical Company and its subsidiary (Petrokemya)	100
Saudi Iron and Steel Company (Hadeed)	100
SABIC Sukuk Company (SUKUK)	100
SABIC Industrial Catalyst Company (SABCAT)	100
Saudi European Petrochemical Company (Ibn Zahr)	80
Jubail United Petrochemical Company (United)	75
National Chemical Fertilizer Company (Ibn Al-Baytar)	71.5
National Industrial Gases Company (Gas)	70
Yanbu National Petrochemical Company (Yansab)	52
Saudi Methanol Company (Ar-Razi)	50
Al-Jubail Fertilizer Company (Al-Bayroni)	50
Saudi Yanbu Petrochemical Company (Yanpet)	50
National Methanol Company (Ibn Sina)	50
Saudi Petrochemical Company (Sadaf)	50
Eastern Petrochemical Company (Sharq)	50
Al-Jubail Petrochemical Company (Kemya)	50
Arabian Industrial Fiber Company (Ibn Rushd)	47.3
Saudi Arabian Fertilizer Company (Safco)	43
Saudi Kayan Petrochemical Company (Saudi Kayan)	35

Source: Company data

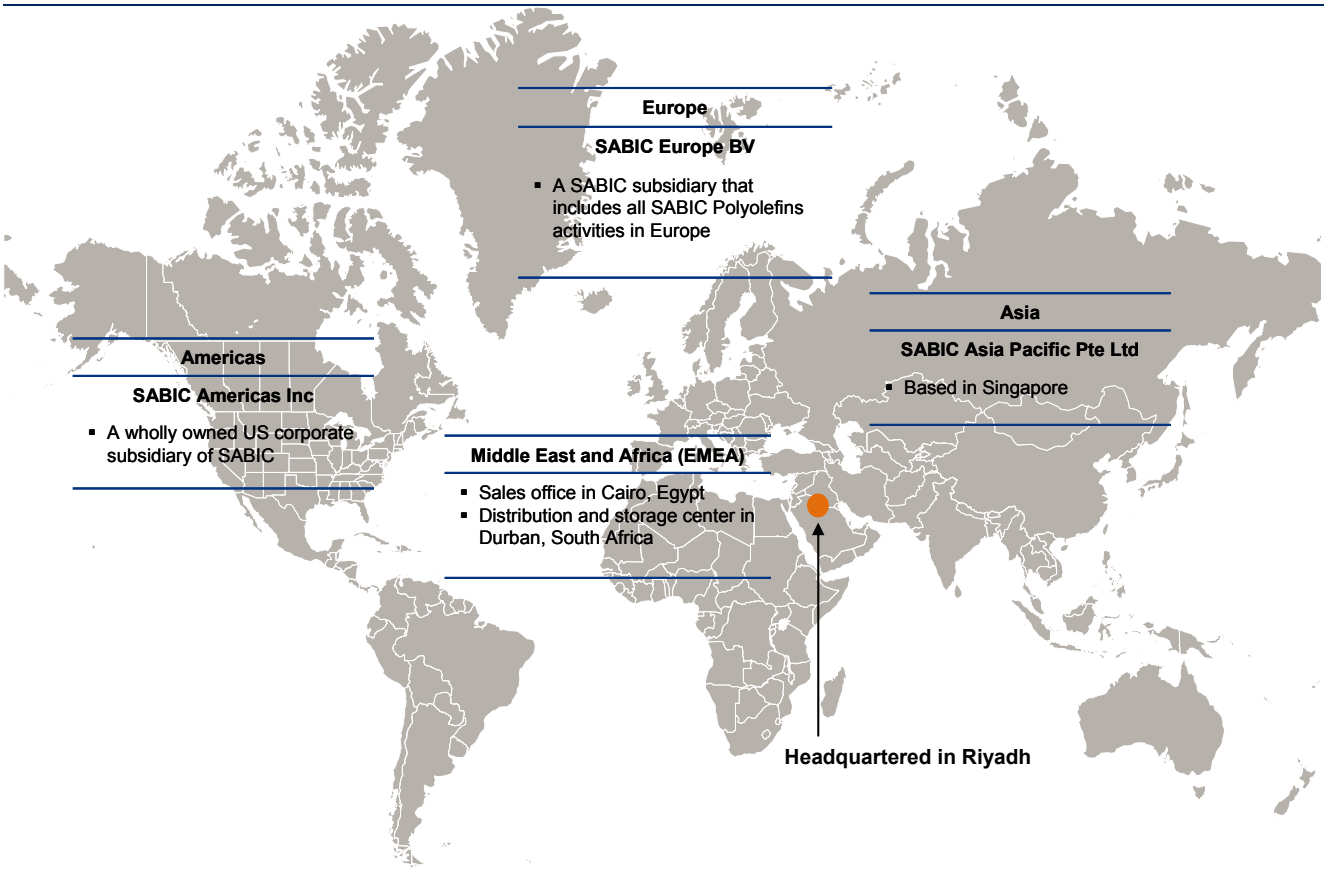
Global reach

Operations spread across more than 40 countries

SABIC has operations in more than 40 countries across the world and has 60 world-class manufacturing plants across the Middle East, Asia, Europe and the Americas. The company has major operations in Al-Jubail, Dammam and Yanbu. SABIC's global presence has increased rapidly with the development of infrastructure of manufacturing plants, distribution centres, offices and storage facilities, enabling the company to cater to its clients worldwide.

A number of the company's major manufacturing facilities are in the Middle East and Africa and are rapidly expanding within the region. SABIC currently has a sales office in Cairo, Egypt, and a distribution and storage centre in Durban, South Africa. The company has a presence in North America, with SABIC Americas Inc, an independent wholly owned US corporate subsidiary of SABIC, based in Houston, Texas. In Asia, SABIC Asia Pacific Pte Ltd is in Singapore and has operations in Europe with its subsidiary, SABIC Europe BV, which includes all polyolefins activities in the European region.

Figure 2 : SABIC's geographical presence



Source : Company reports, company filings, Rasmala

Income statement

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	103105	151970	189546	189006	186958
Cost of sales	-63714	-92813	-113876	-110481	-103815
Operating costs	-8634	-10654	-13288	-15120	-14957
EBITDA	**30757**	**48502**	**62382**	**63404**	**68186**
DDA & Impairment (ex gw)	-10773	-10610	-11269	-11991	-12728
EBITA	**19985**	**37893**	**51113**	**51413**	**55458**
Goodwill (amort/impaired)	-1181	0.00	0.00	0.00	0.00
EBIT	**18804**	**37893**	**51113**	**51413**	**55458**
Net interest	-3026	-3394	-3000	-4054	-4442
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	1497	1256	2000	2100	2205
Reported PTP	**17275**	**35754**	**50113**	**49459**	**53221**
Taxation	-900.0	-2500	-2756	-2968	-3725
Minority interests	-7302	-11726	-17000	-16690	-17768
Other post-tax items	-0.00	0.00	0.00	0.00	0.00
Reported net profit	**9074**	**21529**	**30357**	**29802**	**31727**
Tot normalised items	-1181	0.00	0.00	0.00	0.00
Normalised EBITDA	30757	48502	62382	63404	68186
Normalised PTP	18457	35754	50113	49459	53221
Normalised net profit	**10255**	**21529**	**30357**	**29802**	**31727**

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
Cash & market secs (1)	57197	50648	60744	53549	65472
Other current assets	49267	66451	78158	84207	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**	**346113**	**362977**	**376709**
Short term debt (2)	6477	16754	15000	10000	5000
Trade & oth current liab	25696	27551	31346	33550	31475
Long term debt (3)	100538	93848	93848	83848	78848
Oth non-current liab	11521	13281	13281	13281	13281
Total liabilities	**144231**	**151433**	**153475**	**140678**	**128604**
Total equity (incl min)	152630	166147	192639	222298	248105
Total liab & sh equity	**296861**	**317580**	**346113**	**362977**	**376709**
Net debt	49818	59954	48104	40299	18376

Source: Company data, Rasmala forecasts

year ended Dec

Cash flow statement

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA	30757	48502	62382	63404	68186
Change in working capital	-991.4	-15443	-7911	-3845	3388
Net interest (pd) / rec	3026	3394	3000	4054	4442
Taxes paid	-900.0	-2500	-2756	-2968	-3725
Other oper cash items	-5059	-4329	-6142	-9475	-7225
Cash flow from ops (1)	**26832**	**29625**	**48572**	**51170**	**65066**
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	-12143	-11921
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**	**-38365**	**-33143**
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	**6170**	**-6549**	**10096**	**-7195**	**11923**
Equity FCF (1+2+4)	2844	13525	35572	31170	45066

Source: Company data, Rasmala forecasts

year to Dec

Standard ratios	SABIC					Industries Qatar			BASF		
Performance	**FY09A**	**FY10A**	**FY11F**	**FY12F**	**FY13F**	**FY11F**	**FY12F**	**FY13F**	**FY11F**	**FY12F**	**FY13F**
Sales growth (%)	-31.6	47.4	24.7	-0.29	-1.08	34.4	10.4	18.0	14.6	1.58	4.78
EBITDA growth (%)	-34.1	57.7	28.6	1.64	7.54	50.0	12.1	14.8	10.9	4.56	5.31
EBIT growth (%)	-45.4	89.6	34.9	0.59	7.87	54.0	5.08	15.9	16.4	4.88	5.36
Normalised EPS growth (%)	-53.4	109.9	41.0	-1.83	6.46	46.2	7.19	16.9	25.7	10.9	3.68
EBITDA margin (%)	29.8	31.9	32.9	33.5	36.5	52.4	53.2	51.8	16.9	17.4	17.4
EBIT margin (%)	19.4	24.9	27.0	27.2	29.7	47.9	45.6	44.8	12.3	12.7	12.8
Net profit margin (%)	9.95	14.2	16.0	15.8	17.0	49.2	47.7	47.3	7.82	8.54	8.45
Return on avg assets (%)	7.24	11.9	15.2	14.3	14.6	23.8	21.8	22.0	10.9	11.4	10.8
Return on avg equity (%)	9.71	18.8	23.2	19.9	18.9	33.5	29.9	29.6	25.0	24.1	21.6
ROIC (%)	10.6	18.7	22.6	21.4	21.1	33.1	29.5	31.1	16.2	17.4	17.7
ROIC - WACC (%)	-0.62	5.24	12.2	11.5	11.3	22.0	18.4	20.0	8.32	9.46	9.79
				year to Dec			year to Dec				year to Dec
Valuation											
EV/sales (x)	3.25	2.27	1.76	1.72	1.62	4.40	3.88	3.14	0.92	0.88	0.81
EV/EBITDA (x)	10.9	7.11	5.34	5.13	4.45	8.39	7.28	6.05	5.47	5.05	4.66
EV/EBITDA @ tgt price (x)	12.8	8.35	6.30	6.08	5.33	10.5	9.21	7.73	6.11	5.66	5.25
EV/EBIT (x)	16.8	9.10	6.52	6.33	5.47	9.18	8.50	7.00	7.48	6.88	6.35
EV/invested capital (x)	1.65	1.53	1.38	1.24	1.14	2.57	2.29	2.01	1.66	1.55	1.43
Price/book value (x)	2.63	2.36	2.03	1.80	1.60	2.66	2.27	1.91	2.05	1.76	1.53
Equity FCF yield (%)	1.00	4.75	12.5	10.9	15.8	5.49	8.56	10.8	8.41	10.3	9.51
Normalised PE (x)	27.79	13.24	9.39	9.56	8.98	8.77	8.18	7.00	8.72	7.86	7.58
Norm PE @ tgt price (x)	33.6	16.0	11.4	11.6	10.9	11.1	10.3	8.84	10.1	9.11	8.79
Dividend yield (%)	1.58	3.68	4.26	4.18	4.45	5.70	6.11	7.14	4.60	4.78	5.15
				year to Dec			year to Dec				year to Dec

Per share data	**FY09A**	**FY10A**	**FY11F**	**FY12F**	**FY13F**
Tot adj dil sh, ave (m)	3000	3000	3000	3000	3000
Reported EPS (SAR)	3.02	7.18	10.12	9.93	10.58
Normalised EPS (SAR)	3.42	7.18	10.12	9.93	10.58
Dividend per share (SAR)	1.50	3.50	4.05	3.97	4.23
Equity FCF per share (SAR)	0.95	4.51	11.9	10.4	15.0
Book value per sh (SAR)	36.1	40.3	46.9	52.8	59.4
				year to Dec	

Solvency	**FY09A**	**FY10A**	**FY11F**	**FY12F**	**FY13F**
Net debt to equity (%)	32.6	36.1	25.0	18.1	7.41
Net debt to tot ass (%)	16.8	18.9	13.9	11.1	4.88
Net debt to EBITDA	1.62	1.24	0.77	0.64	0.27
Current ratio (x)	3.31	2.64	3.00	3.16	3.95
Operating CF int cov (x)	-8.17	-8.46	-16.1	-12.4	-14.5
Dividend cover (x)	2.73	2.40	2.89	2.45	2.66
					year to Dec

Priced as follows: 2010.SE - SR95.00; IQCD.QA - QR129.90; BASF.DE - €54.99
Source: Company data, Rasmala forecasts

Valuation methodology

Valuation methodology – SABIC DCF analysis

SRm	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
EBITDA	62,382	63,404	68,186	71,581	71,181	65,181	65,038	64,845	64,603	64,312
D&A	-11,269	-11,991	-12,728	-13,139	-13,527	-13,893	-14,238	-14,564	-14,871	-15,161
EBIT	51,113	51,413	55,458	58,441	57,654	51,288	50,800	50,281	49,733	49,152
Taxes	-2,756	-2,968	-3,725	-4,535	-4,501	-5,027	-5,016	-5,003	-4,987	-4,969
NOPAT	48,357	48,446	51,733	53,906	53,153	46,261	45,784	45,279	44,746	44,183
% Growth in NOPAT	36.6%	0.2%	6.8%	4.2%	-1.4%	-13.0%	-1.0%	-1.1%	-1.2%	-1.3%
Working capital change	-7,911	-3,845	3,388	-3,779	-531	782	-2,127	-132	294	-1,214
Capital expenditure	-15,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000	-20,000
FCF	36,715	36,591	47,849	43,266	46,148	40,935	37,895	39,710	39,911	38,129
Present value of free cash flow										438,422
Equity investments										8,904
Adjusted minorities										-75,944
Net debt										-52,549
Pension obligations										-7,529
Equity value										311,305
Number of shares (m)										3,000
Equity value/share (SAR)										104
Target price (SAR)										115

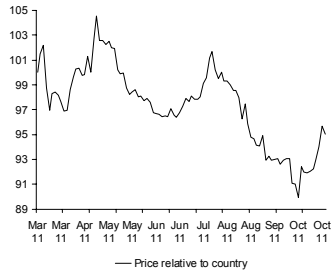
Source: Rasmala forecasts

Company description

Buy

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.

Price relative to country



Strategic analysis

Average SWOT company score: 4

Strengths 4

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 3

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

Opportunities 5

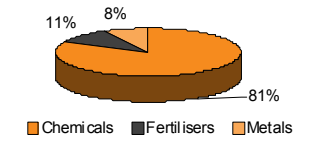
Continued capex to grow top and bottom lines, both inside and outside the region. Moving downstream in the value chain. Balance sheet strong enough to do this.

Threats 3

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

Scoring range is 1-5 (high score is good)

Production by segment, 2011



Source: Company data

Market data

Headquarters
P.O. Box 5101, Riyadh 11422 Saudi Arabia

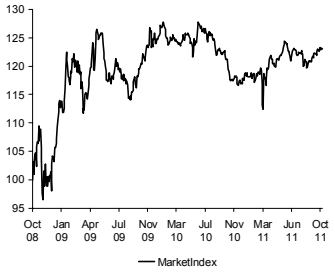
Website
http://www.sabic.com

Shares in issue
3000.0m

Freefloat
30%

Majority shareholders
Saudi Arabian government (70%), GOSI (5%)

Country rel to M East & Africa



Competitive position

Average competitive score: 3+

Supplier power 3+

Natural gas and naphtha are SABIC's main raw materials, which are low-cost, but the government controls supply and allocation. Outside the region, SABIC pays market prices.

Barriers to entry 4+

Considerable investment is needed to enter petrochemicals segment. Most capacities are built in low-cost regions of the Middle East and Asia, where demand growth is higher than in the US and Europe.

Customer power 3+

Customers can choose suppliers from any location in the petrochemical industry, so pricing is the key variable. Given its low-cost production, SABIC can be more competitive than other producers.

Substitute products 4+

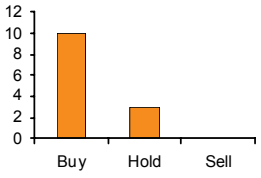
Other materials than petrochemicals and plastics (steel, aluminium) or other chemicals/plastics that SABIC does not produce.

Rivalry 3+

Competition in most markets is significant, but SABIC has the advantage of being one of the lowest-cost producers globally. Moving down the value chain should make SABIC more competitive.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse

Broker recommendations



Source: Bloomberg

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.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

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.

Valuation and risks to target price

SABIC (RIC: 2010.SE, Rec: Buy, CP: SR95.00, TP: SR115.00): We derive our target price using a DCF analysis. The risks to our investment view include lower oil prices, worse-than-expected global GDP growth resulting in weak demand for its products, increases in feedstock (gas) costs in Saudi Arabia and political risk in the Middle East.

Disclaimer