



Lowest GP margin since Q3-18, impacted by lower sales prices and unexpected rise in COGS.

Southern Cement posted a net income of SAR 49.0mn (down 43.7%Y/Y), below our and consensus estimates of SAR 66.0mn and SAR 77.0mn, respectively. The deviation from our estimate is mainly due to higher than expected COGS. Volumetric sales were reported at 1.7MT (down 1.7%Y/Y and 12.2%Q/Q), in-line with our estimate. Realization per ton is expected to stand at SAR 173.3/tonne vs. SAR 187.4/tonne in Q1-22 (down 7.5% Y/Y), but in-line with our estimate of SAR 172.7/tonne. Cost per ton was reported at SAR 132.3/ton (increased by 6.0% Q/Q) leading to a weak GP margin of 23.7% compared to 32.2% in Q1-22. We maintain our “Neutral” recommendation at a TP of SAR 58.0/Share.

- Southern Cement posted a net income of SAR 49.0mn in Q1-23 (EPS: SAR 0.35/share); compared to SAR 87.0mn in Q1-22 and SAR 65.0mn in the previous quarter. Net income came below our and market consensus of SAR 66.0mn SAR 77.0mn, respectively. The Q/Q decline of 21% in net income, and the deviation from our estimate is due to higher-than-expected cost per tonne. Net profit margin came at 16.3%, compared to 26.4% in Q1-22 and 18.5% in Q4-22, the lowest since Q3-18.
- Revenue stood at SAR 300.0mn in Q1-23 (down 10.5%Q/Q, and 9.1%Y/Y), in-line with our estimated SAR 301.0mn. The company's average price realization saw a slight increase Q/Q to stand at SAR 173.3/tonne, compared to SAR 170.0/tonne in Q4-22, and in-line with our estimate of SAR 172.7/tonne. Sales volume stood at 1.7MT, in-line with our estimates and with the 1.8MT recorded in Q1-22; impacted by the seasonality effect of Ramadan as it occupied a third of the month of March.
- Gross profit stood at SAR 71.0mn, below our estimate of SAR 83.5mn. The deviation from our estimate is mainly due to higher-than-expected cost per tonne, which stood at SAR 132.3/tonne compared to our forecasted SAR 124.8/tonne. GP margin reached 23.7%, lower by 850bps from the GP margin in Q1-22, and the lowest since Q3-18. We believe that the margin contraction was led by an abnormal rise in the COGS, while an increase in discounted export sales also likely aided the contractionary pressure on margins.
- Operating profit amounted to SAR 53.0mn, below our estimate of SAR 68.1mn, resulting mainly from the contracted GP margin. OPEX declined by 15.6%Q/Q, but increased by 14.9%Y/Y, totaling SAR 18.0mn. As a result, the OPEX-to-sales ratio for Q1-23 reached 6.0%, slightly lower than the 6.4% in Q4-22, but above the 4.8% recorded in Q1-22. Operating profit margin came to 17.7% compared to 27.5% in Q1-22 and 20.2% in Q4-22, due to a weak gross profit.

AJC view and valuation: The highlight of Southern Cement's Q1-23 results was the higher-than-expected cost per ton, which could possibly revert to normality in the coming quarters. The cost per ton stood at SAR 132.3/tonne, compared to SAR 124.0 per tonne in Q4-22. Furthermore, the company had a net profit margin of 16.3%, the weakest since Q3-18, due to lower selling prices and higher production costs. Slow construction activities led to an 11.1% drop in local demand for cement in 4M-23 compared to 4M-22. The company's inventory level stands at 3.56MT by the end of April, sufficient to cover seven months of sales. Meanwhile, its TTM local market share declined by 100 bps Y/Y to 11.4% by the end of April. Despite announcing a USD 330.0mn CAPEX plan to replace old production lines, which will be financed via debt, we expect the company's dividend payment to increase to SAR 1.75/share in FY23, resulting in a DY of 3.4%. The stock is currently trading at 30.9x compared to a forward P/E of 27.2x based on FY23 earnings. Our recommendation for Southern Cement remains “Neutral,” with a TP of **SAR 58.0/Share**.

Results Summary

| SARmn | Q1-22 | Q4-22 | Q1-23 | Change Y/Y | Change Q/Q | Deviation from AJC Estimates |
|--------------|-------|-------|-------|------------|------------|------------------------------|
| Revenue | 330.0 | 335.0 | 300.0 | (9.1%) | (10.5%) | (0.3%) |
| Gross Profit | 106.0 | 89.0 | 71.0 | (33.0%) | (20.2%) | (15.0%) |
| Gross Margin | 32.2% | 26.6% | 23.7% | - | - | - |
| EBIT | 91.0 | 68.0 | 53 | (41.8%) | (22.1%) | (22.2%) |
| Net Profit | 87.0 | 62.0 | 49.0 | (43.7%) | (21.0%) | (25.8%) |
| EPS | 0.62 | 0.46 | 0.35 | - | - | - |

Source: Company Reports, Aljazira Capital

| Recommendation | Neutral |
|----------------------|---------|
| Target Price (SAR) | 58.0 |
| Upside / (Downside)* | 11.7% |

Source: Tadawul *prices as of 21th of May 2023

Key Financials

| | FY20 | FY21 | FY22 | FY23E |
|------------|-------|--------|--------|--------|
| Revenue | 1,653 | 1,339 | 1,222 | 1,148 |
| Growth % | 27.1% | -19.0% | -8.7% | -6.1% |
| Net Income | 609.4 | 429.1 | 301.0 | 267.0 |
| Growth % | 31.7% | -29.6% | -30.0% | -11.3% |
| EPS | 4.35 | 3.07 | 2.15 | 1.91 |

Source: Company reports, Aljazira Capital

Key Ratios

| | FY20 | FY21 | FY22 | FY23E |
|----------------|-------|-------|-------|-------|
| Gross Margin | 41.1% | 37.7% | 29.2% | 29.8% |
| Net Margin | 36.9% | 32.0% | 24.6% | 23.2% |
| P/E (x) | 19.4 | 22.9 | 23.7 | 27.2 |
| P/B (x) | 3.6 | 3.1 | 2.2 | 2.3 |
| EV/EBITDA (x) | 14.0 | 14.8 | 14.0 | 14.8 |
| Dividend Yield | 5.6% | 3.6% | 2.5% | 3.4% |

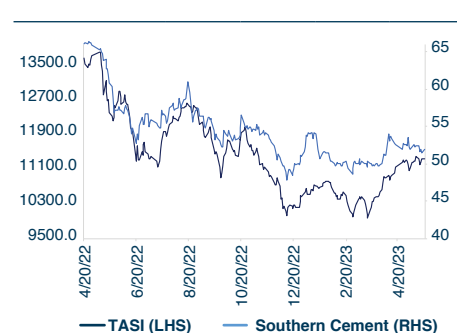
Source: Company reports, Aljazira Capital

Key Market Data

| | |
|-------------------------|-----------|
| Market Cap (bn) | 7.27 |
| YTD % | 0.98% |
| 52 Week (High)/(Low) | 47.6/62.4 |
| Shares Outstanding (mn) | 140.0 |

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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RESEARCH DIVISION

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1. **Overweight:** This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. **Underweight:** This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. **Neutral:** The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. **Suspension of rating or rating on hold (SR/RH):** This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

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