

## Saudi Arabian Mining Co. (Maaden)

TASI Code: 1211 | Reuters Code: 1211.SE | Bloomberg Code: MAADEN ABJ  
Current Market Price: SAR 16.7 (As of 16 Feb 10)

February 2010

Stock Volatility	Expected Return (Feb 2010)		
	Low	Medium	High
Low			
Medium			
High			

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- Saudi Arabian Mining Company's (Maaden) price rose 62.4% YoY in 2009 against the TASI index, which gained 27.5% over the same period. However, on a YTD basis Maaden has lost 4%, against the TASI's gain of 3.4%.
- Maaden currently trades at a P/E (TTM) of 38.9x; substantially higher than the TASI's 19.9x. In 2009, Maaden's P/E fell 18.2% to reach 39.6x from 48.4x at the end of 2008. Being a new listing, we are cautious about placing a fair value on the stock at this juncture.
- Maaden's 2009 revenue increased 37.8% YoY to reach USD 169 mn, led by increase in the volume of gold sold. The revenue from sale of gold rose 40.2% YoY to reach USD 157 mn, backed by a 27.1% increase in the volume of gold sold. Maaden's 2009 profit before tax (PBT) surged 229% YoY to reach USD 176 mn, which included a non-operating income of USD 80 mn received as fee from Alcoa for the participation in the company's aluminum project in Saudi Arabia. A large proportion of earnings are driven by income from short-term investments. The rise in Maaden's 2009 PBT was, however, partially offset by the provision for income tax (zakat), amounting to USD 70 mn. Net profit rose 98% YoY to reach USD 106 mn in 2009.
- The company is diversifying its revenue stream into phosphate and aluminum businesses as all of its gold mines will cease by 2014. Maaden's USD 5.5 bn phosphate project is expected to start production in the second-half of 2010, while its USD 10.8 bn aluminum project is expected to start by 2013. Correspondingly, beginning 2011, phosphate will emerge as the key revenue driver for the company. Currently 93% of the revenue is contributed by the gold business.
- The company's return on equity (ROE) and return on assets (ROA) have fallen over the years. Maaden's ROE declined to 2% in 2009 from 4% in 2005. The company's ROA fell to 1% in 2009 from 4% in 2008. The company's returns have been low on account of huge cash piling in its balance sheet as funds raised from its IPO couldn't be deployed efficiently.
- In 2010, we expect Maaden's net profit to increase by 37% to reach USD 38 mn from USD 27 mn (excluding USD 80 mn non-operating income) in 2009. Gross revenue is expected to increase 31% to reach USD 221 mn in 2010, on account of higher sales from its gold business.

USD Mn	2005	2006	2007	2008	2009	2010f
Revenue	74	93	65	122	169	221
Net profit	57	84	(66)	54	107	38
P/E (LTM)	NA	NA	NA	48.4x	39.6x	38.9x
P/B (LFI)	NA	NA	NA	0.6x	1.0x	0.9x
Market Cap	NA	NA	NA	2,625	4,267	3,909
Stock Returns	NA	NA	NA	-47%	62%	-4%

Note: 2010 figures – M.Cap as on 10-Feb-10, Stock return is YTD return

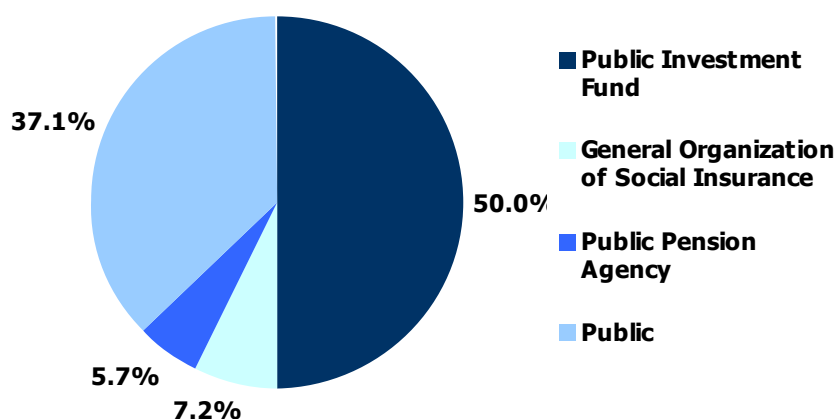
Source: Maaden financial Reports, Bloomberg, Reuters, Markaz Research

## Company Overview

Saudi Government is the major shareholder

Maaden is a Saudi Arabian company engaged in the exploration and extraction of precious metals, primarily gold, in addition to bauxite and zinc. The company has planned to begin extraction of other metals, such as phosphate and aluminum. Maaden was established in 1997 by the Saudi government with the intention to develop the kingdom's mining resources. In July 2008, Maaden was listed on the Saudi Arabia Stock Exchange (Tadawul). The company raised USD 2.5 bn through its IPO, offloading a 50% stake. However, the Saudi government, through its various entities, still remains the major shareholder (constituting 63% of shares). After its IPO and the subsequent dilution of the government stake, the company has started paying zakat<sup>1</sup> beginning 2009.

**Figure 1: Shareholding Pattern (as of Sept 2009)**



Source: Zawya

93% revenue from gold sales

Revenue from the sale of gold dominates Maaden's revenue stream (around 93% of 2009 revenue). The revenue from gold sales increased at a CAGR of 21% to reach USD 157 mn in 2009 from USD 74 mn in 2005. Revenue from sale of bauxite and zinc, which began in 2008, contributed 5% and 2%, respectively, to total revenue.

Joint Ventures to enter into new business segment

The company has formed JVs with some prominent industry players recently to diversify away from gold. The company entered into a JV with SABIC to form Maaden Phosphate Co. (MPC), wherein Maaden holds a 70% share while SABIC holds the remaining 30%. For expanding into aluminum, the company has tied up with Alcoa - Maaden has a 60% stake while the remaining 40% is held by Alcoa. Maaden has also signed a 50:50 JV with Sahara Petrochemical Company worth USD 400 mn to build production capacity of 0.25 Million tonnes per year (Mtpy) of caustic soda and 0.3 Mtpy of ethylene di-chloride with expected completion in the second half of 2012. Maaden has also entered into a contract worth USD 25.3 mn with Al Olayan Descon to produce 140,000 tons of magnesite over the next 20 years, with production starting 2011.

<sup>1</sup> Zakat is an annual charge equal to 2.5% of wealth which is given to the poor

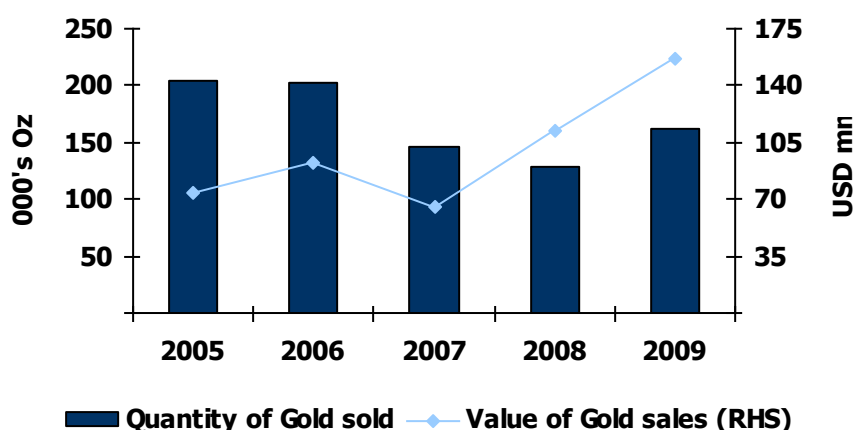
## Investment Highlights

### Gold business faces decline

Gold sales grew at a CAGR of 21% over 2005-2009 despite 5.5% decline in sales volume over the same period

The revenue from gold sales has increased at a CAGR of 21% over the last four years to reach USD 157 mn in 2009. However, the volume of gold sales declined at a CAGR of 5.5% over the same period to reach 162,409 ounces in 2009, from 203,655 ounces in 2005. The increase in gold sales was due to the rise in gold prices, which increased at a CAGR of 26% over 2005-2009 to reach USD 1,097 per ounce in 2009. Maaden's revenue increased significantly after 2007 after it cancelled forward contracting. The company incurred a loss of USD 119 mn on its forward positions before this shift. While the company is un-hedged, it will benefit from any increase in gold prices.

**Figure 2: Volume and Value of Gold Sales over the years**



Source: Company's financial report

All the five operating mines to close over the period 2010-2014

Going forward, Maaden's revenue from gold is expected to decline as the company will close all of its mines between 2010 and 2014, due to gradual decline in reserves. The company's operating margin is likely to improve with the closure of the low grade Bulgah mine in 2010. Mining companies have a higher proportion of fixed cost and low grade mines, with relatively smaller output, depress margins. On the other hand, with the closure of Bulgah mine, revenues and hence earnings will also dip, unless the company discovers new gold reserves from its other exploration projects, such as Ad Duwayhi.

**Table 2: Gold mines in operation**

Mines	Grade (Grams/Ton)	Reserves (ounces)	Expected closure
Mahd Ad'Dahab	8.7	347,000	2013
Al Hajar	1.3	87,000	2011
Sukhaybarat mine	0.4	2,000	2014
Bulghah mine	0.8	428,000	2010
Al Amar	9.9	429,000	2014

Source: Company's website, SRK report, figures of 2007

### Diversifying into phosphate business

Focusing towards other revenue sources

Maaden aims to exploit phosphate deposits at Al Jalamid in northern Saudi Arabia and produce Diammonium Phosphate (DAP), the most widely used phosphate based fertilizer. Maaden has been granted a 30 year license by the Saudi Government to utilize the site to mine phosphate ore. The company shall also produce phosphoric acid, ammonia and sulfuric acid from the mine.

In 2007, Maaden entered into a JV with SABIC to form MPC to operate the phosphate project. The total cost of the project is estimated to be around USD 5.5 bn with a production capacity of 2.92 Mtpy of DAP and production is expected to start by the end of 2010. For the first 15 years, SABIC will sell 77% of the DAP production while Maaden will sell the remaining 23%. In addition, SABIC will also be responsible for selling the excess ammonia and phosphoric acid production during the period.

Integrated cost model to enhance the operating margin

The phosphate project will give fillip to the company's top-line. Also, the phosphate project is expected to improve the company's operating margin. The project will be entirely integrated and hence the company will have more control over the supply and cost of raw materials. Maaden will mine internally to source the requirement of the raw material, phosphate ore. This appears to be a big advantage over some of the non-integrated producers in the region. In addition, the company has access to cheap natural gas supplies from Saudi Aramco. However, the overall cost of production is also dependent on various external factors, particularly the timely completion of the North-South railways and port facilities required for transportation of raw material. Both North-South railway and Ras Az Zour Port are currently under construction and are expected to be completed in the second half of 2010, very close to the company's own expected production date. Any delay in the completion of these projects will force Maaden to rely on road transport, which will increase its cost of production.

To fund this project, Maaden has planned to raise 70% of the project cost through debt and the remaining 30% through equity. Maaden and SABIC will contribute in proportion to their respective stake in the project.

### Aluminum project at an early stage

Too early to have a clear revenue visibility

Maaden's biggest diversification is its aluminum project worth USD 10.8 bn. The company aims to exploit the kingdom's bauxite resources for domestic and export market. The capacity of the project is 4.0 Mtpy of bauxite, 1.8 Mtpy of alumina and 0.74 Mtpy of aluminum.

Maaden had initially signed a 51:49 JV with Rio Tinto Alcan to build the project. However, amid the global economic crisis, Rio Tinto faced financial difficulties and pulled out of the project. In December 2009, Maaden tied up with Alcoa, in a 60:40 JV to build its aluminum project.

The key concern remains funding this project. Maaden is expected to contribute around USD 3.5 bn as its share of equity contribution while Alcoa will contribute around USD 1.8 bn. The remaining USD 5.6 bn is expected to be financed through debt. Under the current tight credit market conditions, raising funds will remain an area of concern for the company.

### Low returns

Maaden's return on equity (ROE) and return on assets (ROA) have been very low. In 2009, Maaden's ROE declined to 2% from 4% in 2005. Further, its ROA declined to 1% in 2009 from 5% in 2005.

High cash balance generating low return and subjected to zakat

Maaden's return has fallen over the years due to substantial increase in its cash balance, post IPO. Maaden raised around USD 2.5 bn from its IPO, intended for funding its phosphate and aluminum projects. However, since its aluminum project did not make much progress in 2008 owing to Rio Tinto Alcan backing off, the company piled on huge cash and short-term investments. The company's cash and short-investments increased to USD 3.1 bn in 2009 from USD 735 mn in 2007. High cash balance has resulted in a higher proportion of earnings (interest income) generating low returns. The company is also required to make higher provision for zakat on cash, putting further pressure on the company's net income. Going forward, Maaden's return measures are likely to improve as the phosphate and aluminum projects come online.

### Zakat provision has been a drag on earnings

Filing for zakat started in 2009

Prior to its IPO, Maaden was fully-owned by the government and did not pay any taxes. However with the dilution of the government stake after the IPO, Maaden is required to pay zakat beginning 2009. The company's zakat provision for 2009 amounted to USD 70 mn, equivalent to 73% of 2009 PBT (excluding extra-ordinary income). All of this zakat is not associated with the company's earnings. The government also charges zakat on cash. The earnings and cash are both subject to 2.5% zakat. In 2009, the company on average held over USD 3 bn in liquid assets – cash and short-term securities. Until the company deploys idle cash efficiently, the current zakat provisioning will continue to remain a drag.

### Adequate Government support

The government of Saudi Arabia holds a majority stake in Maaden and in effect, the company has received adequate support from the government. In addition to exclusive license rights, Maaden enjoys support such as project financing, provision of infrastructure as well as various other facilities required for the successful running of a given project. Maaden's upcoming phosphate and aluminum projects have largely benefited from government support. The land at Ras Az Zawr, on which the phosphate and aluminum production facilities are being constructed, is owned by the government. Key infrastructure facilities such as the railway and ports required for the projects are being built by the government. In addition to providing cheap access to inputs required for production, the government has also sourced fuel for the power station and natural gas for the ammonia plant through Saudi Aramco. The government has also provided a significant subsidy for the power supply at Ras Az Zawr. Apart from these operational supports, the government, through the Public Investment Fund, has granted loan facilities amounting to USD 1.1 bn.

## Earnings

### 2009 earnings review

2009 net profit came in at USD 107 mn due to a one-time gain of USD 80 mn

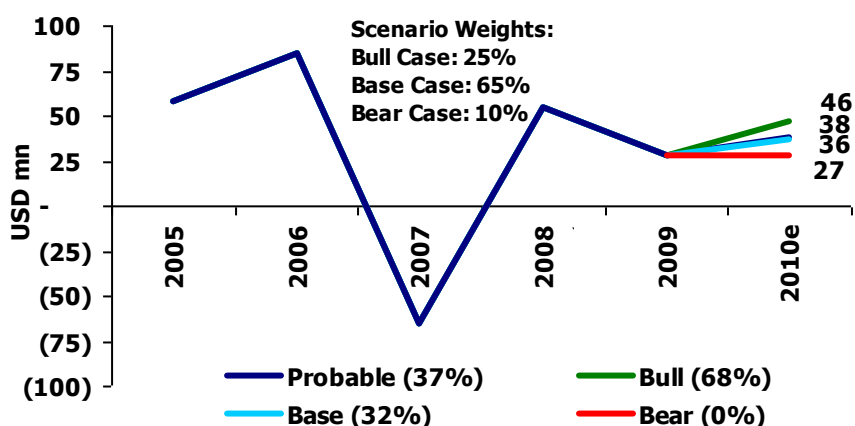
In 2009, gross revenue rose 39% YoY to reach USD 169 mn led by 40% YoY increase in the sales of gold. The operating profit was reported at USD 27 mn in 2009 compared to a loss of USD 15 mn in 2008. Income from short-term investments (term-deposits with commercial banks) contributed significantly (around 48%) to Maaden's PBT, rising 8.5% YoY to reach USD 84 mn in 2009. The net profit increased 98.8% YoY to reach USD 107 mn in 2009. In 2009 Maaden for the first time made a provision for zakat, amounting to USD 70 mn.

For the fourth quarter of 2009, Maaden reported an increase of 177% YoY in its net profit after tax to reach USD 91 mn, which includes an amount of USD 80 mn received from Alcoa as a fee for participation in the company's aluminum project. Excluding this one-time gain, Maaden's 4Q09 net profit dipped 67% YoY to reach USD 11 mn. Maaden's 4Q09 revenue rose 5% YoY to reach USD 36 mn led by a 38% YoY increase in average gold price, which offset the 15% YoY fall in the quantity of gold sold. Maaden reported an operating profit of USD 6.0 mn in 4Q09 compared to a loss of USD 5.0 mn in 4Q08. This was due to a 42% and 13% YoY decline in cost of sales and SG&A expenses, respectively.

### Earnings Growth

Our call on 2010 net profit is a weighted product of three scenarios. Our expected 2010 net profit growth is derived after excluding any one-time gain such payment of USD 80 mn participation fees by Alcoa in 2009. We expect the company to generate a USD 38 mn net profit for 2010. The Bull Case scenario calls for (a 68% rise in earnings, and a 25% probability of occurring), while the Base Case is a 32% increase in net earnings and a 65% probability of occurring, and finally, the Bear Case calls for no increase in net earnings, however, we see only a 10% chance of this occurring.

Figure 3: Net Income



Source: Company Financials, Markaz Research

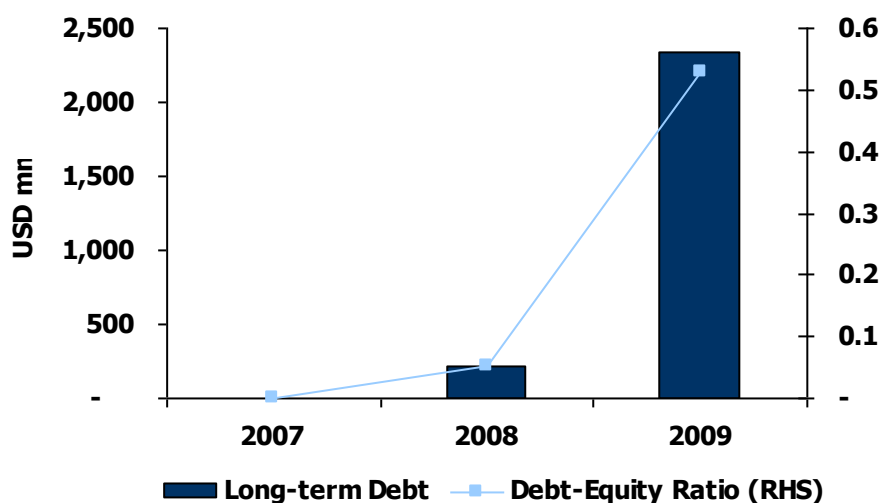
### Rising debt level

To finance its ongoing and new projects Maaden has resorted to high debt financing in 2009. The company's long-term debt increased to USD 2.3 bn in 2009 from USD 0.2 bn in 2008. Debt to equity ratio has increased to 0.5x in 2009, compared with 0.1x in 2008.

Maaden's debt profile is characterized by the presence of only long-term loans, with no short-term commitments currently. Maaden raised debt for the first time in 2008 from Public Investment Fund (PIF) amounting to USD 200 million. The loan carries an interest rate of LIBOR plus 0.5% per annum to be repaid on semi-annual basis, with equal principal repayments starting June 2012 until December 2023. PIF has granted financing facilities worth USD 1.1 bn to fund the construction and operation of Maaden's phosphate project. During 2009, Maaden raised funds worth USD 1.7 bn from various Islamic and Commercial Banks. These loans carry interest rate of LIBOR plus 0.5%-1.15% per annum to be repaid semi-annually, with equal principal repayments between December 2011 and December 2023. The company plans to launch a USD 7 bn financing deal for its aluminum smelter project in 2Q10. Thus, in 2010, Maaden's balance sheet can witness a further increase in its long-term debt.

Funds raised at an attractive terms of payment

**Figure 4: Maaden's Debt Profile**



Source: Maaden's financial report

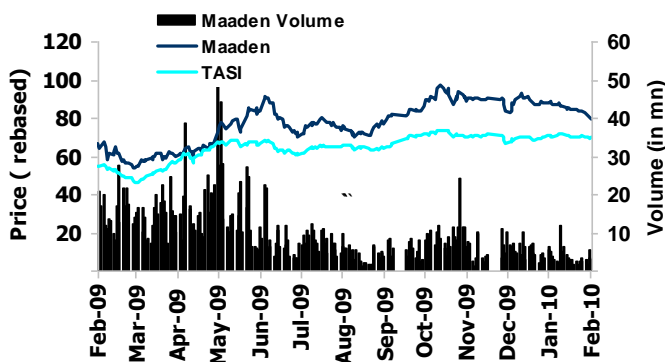
### Valuation

On a YTD basis, Maaden has lost 4%, while the Saudi Stock Market, increased 3.4% (Figure 5). The company's current PE is at 38.9x, and fell 18.2% in 2009. Maaden's PE has fallen a further 1.8% in 2010. Since Maaden is a newly listed company, (listed in July 2008 on Saudi Stock Exchange), we take a cautious approach and don't place any fair value P/E on the stock at this point.

If gold prices rise further, Maaden's gold business is expected to benefit. However, the closure of all the operational mines over 2010-2014 will impact its top-line. Maaden's phosphate business is expected to start production in 4Q10 and will be a key component from 2011. Aluminum project is at early stages of development and thus in the near term no revenue can be associated to this project. The future performance of Maaden is dependent on the success of its ongoing and new projects (especially phosphate and aluminum).

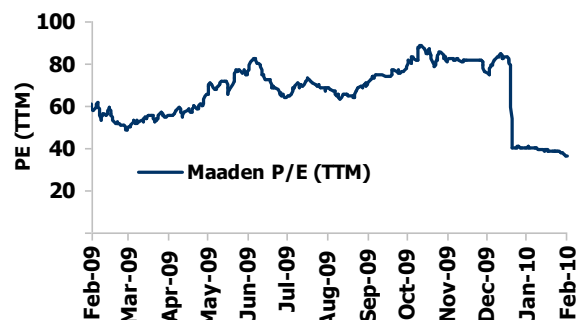
Maaden has very a high turnover velocity of 283.3% and 282.6% in 2008 and 2009, respectively, owing to being a very liquid and highly traded stock. We expect Maaden to provide low returns with low risk as per the Markaz Volatility Index (Figure 7).

Figure 5: Price & Volume Trend



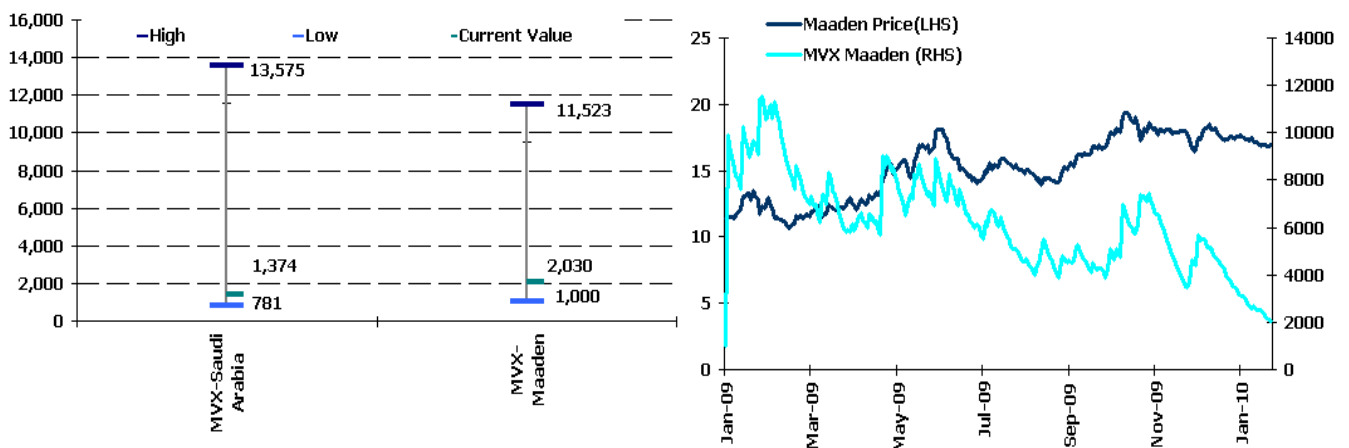
Source: Bloomberg

Figure 6: P/E Trend



Source: Bloomberg, Markaz Research

Figure 7: Markaz Volatility Index (January 2010)



Source: Markaz Research

## Appendix 1: Key Statistics

<b>Income statement (USD mn)</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010e</b>
Gold Revenue	74	93	65	112	157	205
Low Grade Bauxite Revenue	-	-	-	8	9	12
Zinc Revenue	-	-	-	2	3	4
Gross Revenue	<b>74</b>	<b>93</b>	<b>65</b>	<b>122</b>	<b>169</b>	<b>221</b>
Net profit	<b>57</b>	<b>84</b>	<b>-66</b>	<b>54</b>	<b>107</b>	<b>38</b>
<b>Balance Sheet (USD mn)</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010e</b>
Cash	1,277	1,300	735	3,047	3,078	
Total LT Assets	198	279	702	2,381	4,537	
<b>Total Assets</b>	<b>1509.2</b>	<b>1610.0</b>	<b>1559.6</b>	<b>5695.6</b>	<b>7778.1</b>	
Total Current Liabilities	40	51	67	953	496	
Short Term Debt	-	-	-	-	-	
Long Term Debt	-	-	-	219	2,342	
<b>Total Liabilities</b>	<b>65.6</b>	<b>81.7</b>	<b>97.1</b>	<b>1,378.9</b>	<b>3,353.7</b>	
<b>Total Shareholders' Equity</b>	<b>1,443.6</b>	<b>1,528.4</b>	<b>1,462.4</b>	<b>4,316.7</b>	<b>4,424.4</b>	
<b>Key Ratios</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010e</b>
Average Realized gold price per oz ( USD)	364	459	445	877	967	
Return on Assets (%)	4%	5%	-4%	1%	1%	
Return on Equity (%)	4%	6%	-5%	1%	2%	1%
Earnings Growth (%) (Exc. Extraordinary gain)	NA	47.5%	NA	NA	-49%	37%
Revenues Growth (%)	NA	25.8%	-30.2%	88.5%	37.9%	30.8%
P/E	-	-	-	48.40x	39.60x	
Price/Book	-	-	-	0.60x	1.00x	
Debt/ Equity	-	-	-	0.05x	0.53x	
Market Price (SR)	-	-	-	10.7	17.3	
EPS (SR)	0.23	0.34	-0.27	0.22	0.44	
Assets Growth	NA	7%	-3%	265%	37%	
Equity Growth	NA	6%	-4%	195%	2%	
Annual Trading Volume (mn)	-	-	-	2240	2740	
Annual Trading Value (USD mn)	-	-	-	12,454	10,306	
Turnover Velocity				283.3%	282.6%	
M Cap (USD mn)	-	-	-	2,625	4,267	

**Source: Zawya, Reuters, Company Financials**

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**Research Coverage Market  
Cap as % of total Market cap 29%**

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- Mobinil (Sep-08)
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**Research Coverage Market  
Cap as % of total Market cap 45%**

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- OIB (July-08)

**Research Coverage Market  
Cap as % of total Market cap 69%**

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**Research Coverage Market  
Cap as % of total Market cap 39%**

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Low	Where the potential return is less than 10%
Medium	Where the potential return is between 10% and 25%
High	Where the potential return is greater than 25%

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High	Where the Current MVX and band width of stock is more than the respective country benchmark
Medium	Where the current MVX is lower than benchmark and band width higher than or lower than benchmark
Low	Where the current MVX is lower than the benchmark and the band width lower than the benchmark

MVX refers to Markaz Volatility Index calculated by Markaz based on in-house proprietary model

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