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Ratings

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Saudi Basic Industries Corp.

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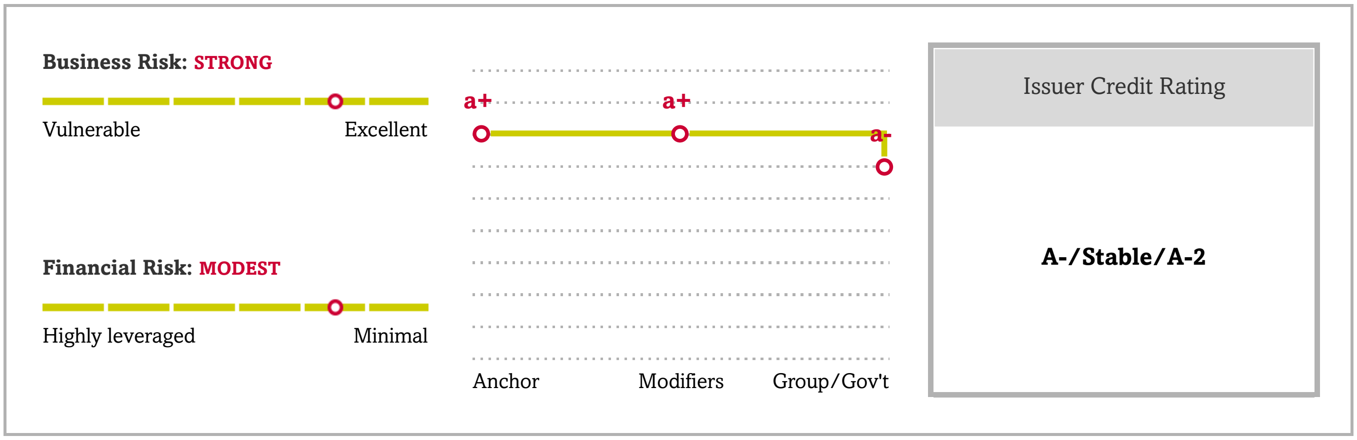


Rationale

Business Risk: Strong	Financial Risk: Modest
• Access to competitively priced gas from Saudi Aramco. • Large scale and cost-efficient plants following completion of a major investment phase. • Very high and resilient profitability. • Sovereign ownership, which helps with, for example, funding and infrastructure. • Limited geographic diversity with most of the profits stemming from Saudi Arabian production. • Exposure to cyclical petrochemicals and steel industries and volatile commodity prices.	• Moderate debt and strong free operating cash flow (FOCF), despite accelerating capital expenditures (capex). • A high dividend payout ratio (around 70% of net income for 2017).

Outlook: Stable

The stable outlook on Saudi Basic Industries Corp. (SABIC) reflects S&P Global Ratings' view on the sovereign as well as its expectations that SABIC will maintain high profitability under current benign industry conditions. We expect EBITDA margins exceeding 30% in 2018 and 2019, and continued substantial headroom in SABIC's credit metrics, including funds from operations (FFO) to debt of more than 60% (128.5% in 2017) and debt to EBITDA of less than 1.5x (0.7x in 2017). Although we see a risk of further increases in ethane and methane prices in Saudi Arabia over the medium term, SABIC should be able to maintain strong profitability even with a much higher feedstock cost.

Downside scenario

We would downgrade SABIC if we downgraded Saudi Arabia, since we don't believe that SABIC's credit quality can exceed that of the sovereign, given its close ties to the government. However, since SABIC's stand-alone credit profile is at 'a+', which is currently two notches above the ratings on the company, some deterioration of its credit profile under weaker market conditions is unlikely to trigger a downgrade. Nevertheless, adoption of an aggressive financial policy (not currently envisaged) or very large mergers and acquisitions (M&A) could lead us to consider a negative rating action.

Upside scenario

We do not foresee rating upside at this stage, since the ratings on SABIC are capped by our rating on Saudi Arabia (A-/Stable/A-2).

Our Base-Case Scenario

Net income for the first half of 2018 was Saudi Arabian riyal (SAR) 17.65 billion (about $4.7 billion), up 42% year on year due to higher production and prices. SABIC's earnings are sensitive to output prices, given that the prices of a large share of its feedstock costs (ethane and methane) are fixed.

We believe margins for the global chemicals industry will largely stabilize in 2018 following several years of improvement, attributable to the increase in commodity chemical capacity. Demand for chemicals will be driven by expected global GDP growth of 3.9% in 2018 and 2019, with support from key end markets like industrial, automotive, and housing markets. The key risk to credit quality is the sector's ongoing M&A trend, and the potential negative impact on credit metrics from funding them with debt. Weakness in subsectors such as fertilizers also remains a risk. Large new North American capacity in olefins such as ethylene and propylene, and in downstream products such as polyethylene, are an important development in the industry. The growth in capacity is a response to the emergence of low-cost shale gas as an input material in this region. The potential shutdown of less cost-competitive capacity is an important unknown variable that will influence the impact on total supply from the increase in U.S.-based capacity.

Assumptions

- Improving output prices and revenues in 2018, as increasing oil prices boost petrochemical prices. We anticipate an at least stable pricing environment for petrochemicals in 2019 based on our forecast of robust chemicals demand amid healthy global GDP growth, despite capacity additions in the U.S. and the Middle East.
- An oil price of $70 per barrel (/bbl) in 2018, $65/bbl in 2019, $60/bbl in 2020, and $55/bbl thereafter. Oil remains a key input for the global chemicals industry, and product prices are typically based on the marginal producer, which primarily uses more expensive oil-derived feedstocks.
- Stable production with capacity utilization in line with previous years.
- Margins expected to remain broadly stable at 30%-32% in 2018 and 2019.
- Capex of $11 billion in 2018 and $24 billion in 2019 and minor opportunistic acquisitions.
- A stable dividend payout and no share buybacks.

Key Metrics

	2017A	2018F	2019F
EBITDA (bil. $)	45.4	52-53	51-52
EBITDA margin (%)	31.4	31-32	31-32
Adjusted debt/EBITDA (x)	0.7	<1.0	<1.0
FFO/adjusted debt (%)	128.5	>100	>100

A--Actual. F--S&P Global Ratings' forecast.

Company Description

SABIC is the fourth-largest diversified chemical company in the world. The company is listed on Saudi Arabia's stock exchange, but remains majority owned by the Kingdom of Saudi Arabia, which holds a 70% stake. We estimate SABIC's total production at about 75 million metric tons (mmt) in 2018, which ranks it among the top five global producers of ethylene, polyethylene (PE), polypropylene (PP), ethylene glycol, methanol, and methyl tertiary butyl ether (MTBE). Following a major investment program over recent years, SABIC now operates 14 crackers, 11 of which are located in Saudi Arabia and three in Europe. SABIC also uses its access to low-priced domestic gas by diversifying into nitrogen-based fertilizer production--such as ammonia and urea--as well as steel operations. Most activities involve joint ventures. However, SABIC exercises control and consequently fully consolidates these entities.

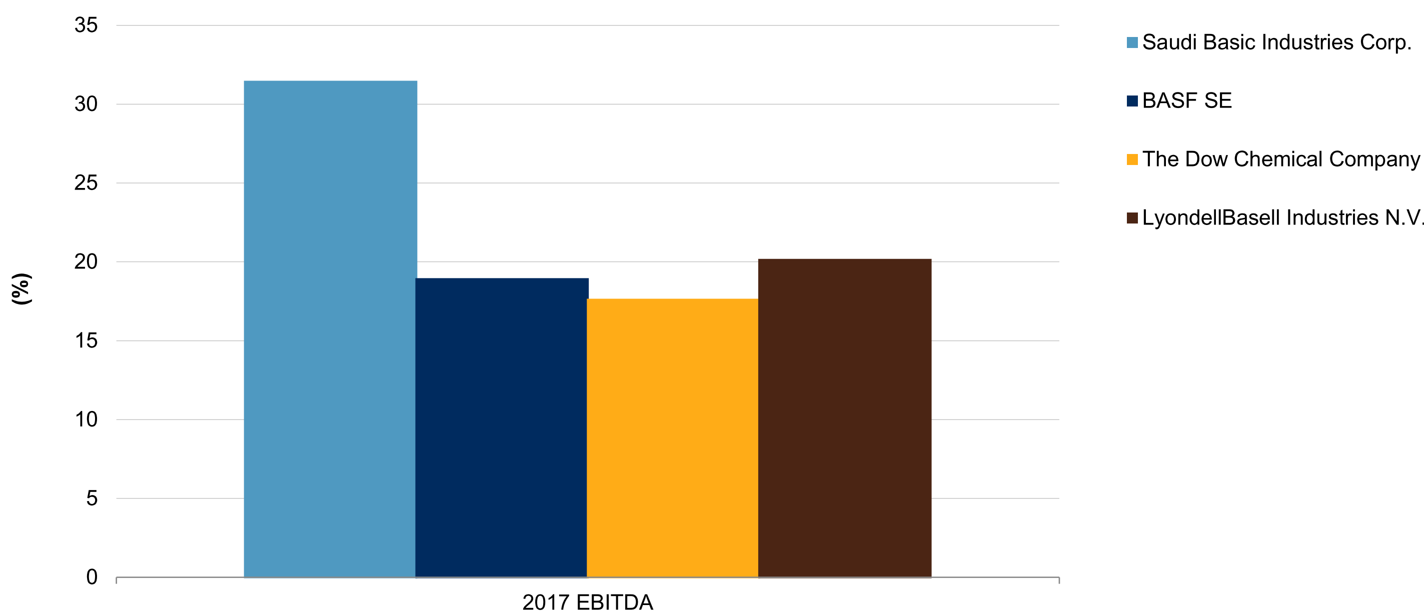
Despite SABIC's large international diversification in recent years, most of its EBITDA (but not sales) stems from its Saudi Arabian activities, which are distinctly more profitable. Bearing in mind that the majority of its Saudi production is also exported, SABIC's sales profile is geographically well balanced (see chart).

Business Risk: Strong

SABIC's key strength is the strong profitability of its Saudi operations, which enjoy access to gas-based feedstock at prices well below the global market average, positioning the company in the first quartile of the global cost curve. North American and Middle East producers that use natural gas rather than naphtha remain at the top in terms of cost-competitive locations for commodity chemical production. We expect gas prices in Saudi Arabia to rise closer to global market prices in the coming year, but believe SABIC will remain a low cost producer due to its large scale and modern production facilities. SABIC enjoys EBITDA margins of over 30%, compared with a global average of around 20%.

Chart 1

SABIC's EBITDA 2017 Margin Is Superior To Peers'



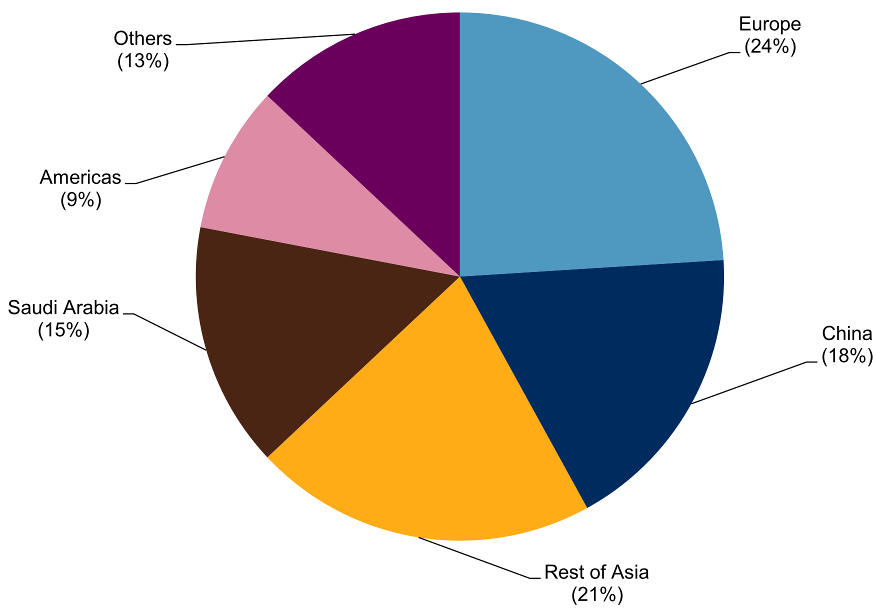
SABIC's scale and ability to expand organically in Saudi Arabia due to good access to infrastructure and additional gas supply is another key strength. The company is the world's No. 3 producer of polyolefins and is a market leader in ethylene, ethylene glycol, methanol, MTBE, and polyethylene. Its all-in production--which comprises mainly petrochemicals, intermediates, polymers, and, secondarily, fertilizers and steel--reached 71.2 mmt in 2017, up from 58.5 mmt in 2009. SABIC's 12 domestic gas crackers and chemical complexes are located at the Jubail and Yanbu industrial sites. SABIC's international activities, SABIC Europe and SABIC IP, are important revenue contributors, but less so for profits, since they don't benefit from the same feedstock supply.

SABIC aims to continue expanding both organically and via acquisitions, as it seeks to diversify into higher value-added and more stable specialty chemicals, as demonstrated by its recent purchase of a 24.9% stake (SAR11.25 billion) in Clariant AG and the formation of a long-term strategic partnership with Clariant. We expect SABIC will continue to make opportunistic acquisitions of a similar magnitude, and believe this can be accommodated within the current rating. We expect capex will increase significantly over the coming two years, since a number of large-scale investments are reaching a final investment decision, including the $7.3 billion U.S. cracker joint venture with ExxonMobil. We expect investments to target feedstock-advantaged production, like U.S. shale gas, and access to growth markets, such as China.

SABIC's limited geographic diversity by location of production is a key rating constraint. Its Saudi Arabian production assets continue to account for the majority of profits, even though it exports most of its domestic production. Sales by end market are well diversified, however (see chart 2). Other relative weaknesses are the cyclicality of SABIC's petrochemicals and steel-production business units.

Chart 2

SABIC Generates Most Of Its Sales In Europe And Asia



*Based on the six months to June 30, 2018.

Peer comparison

Large scale, strong, and stable margins, a strong liquidity position and low leverage are key strengths of SABIC versus rated peers. Key weaknesses are the concentration of its asset base in Saudi Arabia and focus on higher volatility commodity chemicals.

Table 1

Saudi Basic Industries Corp.--Peer Comparison				
Industry Sector: Chemical Cos				
	Industries Qatar QSC	**Saudi Basic Industries Corp.**	**LyondellBasell Industries N.V.**	**Sasol Ltd.**
Rating as of Sept. 24, 2018	A+/Negative/--	A-/Stable/A-2	BBB+/Stable/A-2	BBB-/Stable/A-3
(Mil. $)	**--Fiscal year ended Dec. 31, 2017--**			**Fiscal year ended June 30, 2017**
Revenues	3,919.9	39,933.4	34,484.0	13,288.0
EBITDA	1,271.3	12,546.3	6,945.0	4,108.8
Funds from operations (FFO)	1,336.1	11,027.6	5,160.5	3,084.1
Net income from cont. oper.	910.4	4,914.2	4,897.0	1,555.1
Cash flow from operations	1,183.6	10,083.4	5,429.5	2,827.1
Capital expenditures	125.8	2,936.0	1,527.0	4,605.7
Free operating cash flow	1,057.9	7,147.4	3,902.5	(1,778.7)
Discretionary cash flow	388.6	2,619.2	2,487.5	(2,512.7)
Cash and short-term investments	2,834.8	16,902.2	2,850.0	2,109.9
Debt	0.0	8,584.8	8,781.6	6,604.2
Equity	9,401.6	56,031.1	9,726.1	16,681.3
Adjusted ratios				
EBITDA margin (%)	32.4	31.4	20.1	30.9
Return on capital (%)	10.3	13.6	28.9	12.3
EBITDA interest coverage (x)	23.2	15.0	11.1	7.5
FFO cash int. cov. (X)	47.3	20.2	16.4	56.1
Debt/EBITDA (x)	N.M.	0.7	1.3	1.6
FFO/debt (%)	N.M.	128.5	58.8	46.7
Cash flow from operations/debt (%)	N.M.	117.5	61.8	42.8
Free operating cash flow/debt (%)	N.M.	83.3	44.4	(26.9)
Discretionary cash flow/debt (%)	N.M.	30.5	28.3	(38.0)

N.M.--Not meaningful.

Financial Risk: Modest

SABIC has low debt in relation to its impressive FOCF before dividends, and sizable cash balances that will help fund its increasing capex program. Although the company does not have a formal leverage target, we understand it is targeting a rating in the 'A' category.

SABIC's EBITDA margins and key leverage metrics--debt to EBITDA and FFO to debt--have remained relatively stable over the past five years, even under weaker market conditions.

SABIC's gross financial debt declined to SAR38.2 billion ($10.2 billion) as of June 30, 2018, with reported cash and short-term deposits at a high SAR65.8 billion ($17.5 billion). Of this amount, we view around SAR16.5 billion as unavailable for immediate debt repayment at the parent company level. Our adjusted net debt figure was SAR38.4 billion at the end of June 2018. Apart from the abovementioned cash adjustment, we add pension obligations of SAR14.2 billion and operating leases of SAR4.5 billion to debt.

Financial summary

Table 2

Saudi Basic Industries Corp.--Financial Summary					
Industry Sector: Chemical Cos					
	--Fiscal year ended Dec. 31--				
(Mil. SAR)	**2017**	**2016**	**2015**	**2014**	**2013**
Revenues	149,766	132,827	148,086	188,123	189,032
EBITDA	47,054	44,449	45,585	54,211	58,280
Funds from operations (FFO)	41,358	40,636	42,112	50,315	54,472
Net income from continuing operations	18,430	17,839	18,769	23,347	25,278
Cash flow from operations	37,817	30,547	45,535	62,981	63,291
Capital expenditures	11,011	13,390	18,520	15,190	12,137
Free operating cash flow	26,806	17,157	27,014	47,791	51,154
Discretionary cash flow	9,823	2,244	10,510	14,591	23,480
Cash and short-term investments	63,390	60,872	68,559	72,949	66,828
Debt	33,380	38,757	43,279	50,842	35,487
Equity	210,138	210,327	209,857	211,419	206,656
Adjusted ratios					
EBITDA margin (%)	31.4	33.5	30.8	28.8	30.8
Return on capital (%)	13.6	11.8	11.9	15.8	17.9
EBITDA interest coverage (x)	15.0	18.7	22.5	23.4	25.9
FFO cash int. cov. (x)	20.2	21.6	27.4	27.5	29.9
Debt/EBITDA (x)	0.7	0.9	0.9	0.9	0.6
FFO/debt (%)	123.9	104.8	97.3	99.0	153.5
Cash flow from operations/debt (%)	113.3	78.8	105.2	123.9	178.3
Free operating cash flow/debt (%)	80.3	44.3	62.4	94.0	144.1
Discretionary cash flow/debt (%)	29.4	5.8	24.3	28.7	66.2

SAR--Saudi Arabian riyal.

Liquidity: Strong

We view SABIC's liquidity as strong and calculate that liquidity sources should exceed liquidity needs by more than 1.5x over the 12 months started June 30, 2018, and by more than 1x over the next 24 months. We also take into account the company's solid bank relationships and high standing in credit markets. Debt at the parent company level has no financial covenants, which we view as a supportive liquidity factor.

Principal Liquidity Sources	Principal Liquidity Uses
• For the 12 months as of June 30, 2018, SAR65.8 billion of cash and cash equivalents available at the end of the second quarter of 2018. • Our expectation of about SAR47 billion of cash FFO. • $2 billion (SAR7.5 billion) of undrawn bank lines maturing in 2020 and $133 million maturing in 2023.	• Short-term debt of SAR27.6 billion. • Our expectation of working capital outflow of SAR4 billion. • Capex of about SAR18 billion. • Annual dividend payment of around SAR13 billion.

Government Influence

We view SABIC as a government-related entity (GRE) and see a high likelihood of SABIC receiving extraordinary support in the event of stress. We view the company's link with the Saudi Arabian government as very strong and, in our opinion, SABIC plays an important role in Saudi Arabia's strategy to diversify its economy toward the non-oil industry. In addition, the company is a significant employer in Saudi Arabia. About 90% of the local workforce are Saudi nationals.

SABIC is 70% owned by the Public Investment Fund (PIF), itself owned by the Saudi Arabian government. The board of directors comprises nine members, five of whom represent the Saudi government, including the chairman and vice chairman.

SABIC benefits from very high ongoing support in that the government sets the price of the gases SABIC uses as feedstock in the production of petrochemicals, fertilizers, and steel in Saudi Arabia. This has a strong positive influence on SABIC's profitability, and is intended to further diversify Saudi Arabia's industrial operations and add value to its natural hydrocarbon resources. The state's current ethane price of $1.75 and methane price of $1.25 per million British thermal units position SABIC favorably on the worldwide cost curve. In addition, the government supports and participates in the funding of new projects for SABIC, through government-related agencies such as PIF or the Saudi Industrial Development Fund.

Our sovereign rating on Saudi Arabia currently caps the rating on SABIC, since we do not rate companies with a very strong link to the government higher than the government itself. This is because the government controls SABIC's operating strategy and financial policy.

Reconciliation

Table 3

Reconciliation Of Saudi Basic Industries Corp. Reported Amounts With S&P Global Ratings Adjusted Amounts (Mil. SAR)

	--Fiscal year ended Dec. 31, 2017--							
Saudi Basic Industries Corp. reported amounts								
	Debt	**Shareholders' equity**	**EBITDA**	**Operating income**	**Interest expense**	**EBITDA**	**Cash flow from operations**	**Capital expenditures**
Reported	58,063	163,922	45,408	28,998	1,749	45,408	38,677	11,471
S&P Global Ratings adjustments								
Interest expense (reported)	--	--	--	--	--	(1,749)	--	--
Interest income (reported)	--	--	--	--	--	1,291	--	--
Current tax expense (reported)	--	--	--	--	--	(4,066)	--	--
Operating leases	4,561	--	1,282	348	348	934	934	--
Postretirement benefit obligations/deferred compensation	14,254	(0)	--	--	581	(364)	(1,334)	--
Surplus cash	(47,542)	--	--	--	--	--	--	--
Capitalized interest	--	--	--	--	460	(460)	(460)	(460)
Dividends received from equity investments	--	--	364	--	--	364	--	--
Non-operating income (expense)	--	--	--	2,711	--	--	--	--
Non-controlling Interest/Minority interest	--	46,217	--	--	--	--	--	--
Debt - Guarantees	2,860	--	--	--	--	--	--	--
Debt - Other	1,184	--	--	--	--	--	--	--
D&A - Impairment charges/(reversals)	--	--	--	1,564	--	--	--	--
Total adjustments	(24,683)	46,217	1,646	4,623	1,389	(4,050)	(860)	(460)
S&P Global Ratings adjusted amounts								
	Debt	**Equity**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Capital expenditures**
Adjusted	33,380	210,138	47,054	33,621	3,138	41,358	37,817	11,011

SAR--Saudi Arabian riyal.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014

- Criteria - Corporates - Industrials: Key Credit Factors For The Commodity Chemicals Industry, Dec. 31, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	**Modest**	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	**a+/a**	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of September 24, 2018)

Saudi Basic Industries Corp.		
Issuer Credit Rating		A-/Stable/A-2
Issuer Credit Ratings History		
22-Feb-2016	*Foreign Currency*	A-/Stable/A-2
11-Feb-2015		A+/Negative/A-1
29-Sep-2006		A+/Stable/A-1
22-Feb-2016	*Local Currency*	A-/Stable/A-2
11-Feb-2015		A+/Negative/A-1
22-Apr-2008		A+/Stable/A-1

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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