

Monthly Newsletter

December 2017

In this issue:

TEDPIX strength: another all-time high

Q3 corporate earnings and State Budget up next

Seasonal currency weakness persists

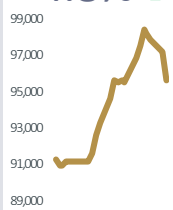
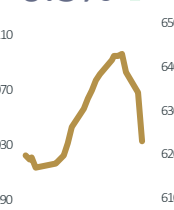
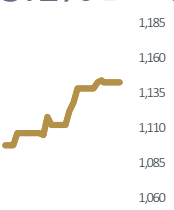
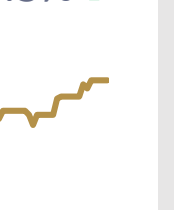
An overview of Khorasan Petrochemical Company

Please see the important Sanctions Disclaimer on pages 7 and 8 of this document.



IRAN EQUITY MARKETS

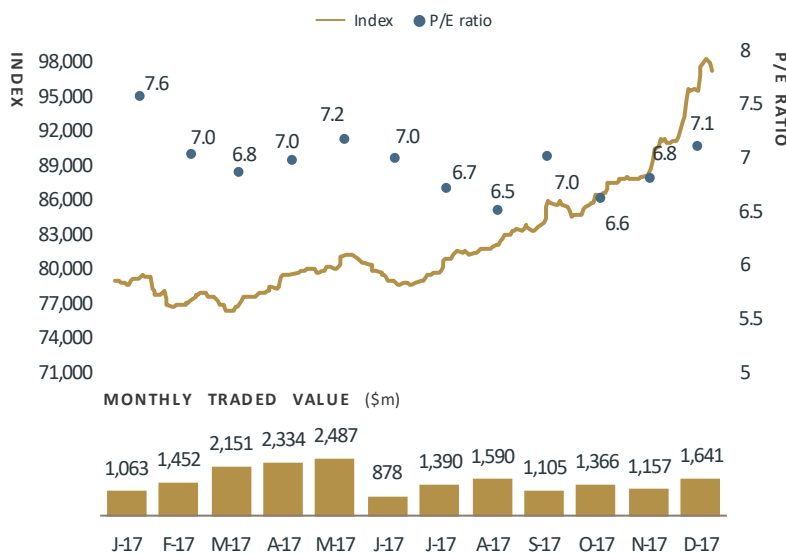
INDICES

Past month	TSE (TEDPIX)	Farabourse (IFX)	Frontier Market (MSCI FM)	Emerging Market (MSCI EM)
	4.8% ↑	0.3% ↑	3.1% ↑	0.3% ↑
Monthly Performance				
Last close	95,562	1,033	636	1,144
Past 12M	20.2%	19.0%	27.4%	32.7%
YTD	21.1%	21.2%	27.4%	32.7%
P/E (fwd.)	7.1x	8.3x	14.8x(hist.)	12.4
Div. yield	8.8%	9.8%	3.1%	2.3%

MARKETS AT A GLANCE

The TEDPIX continued its strong rally in December, having already reached an all-time high in November. The index advanced 4.8% to close the month at 95,562 – which was actually 2.8% lower than its highest intra-month level, due to notable profit-taking on the last two days – triggered by countrywide protests. By comparison, the IFX’s 0.3% December gain was much more muted. On the corporate earnings front, Q3 reports for the current fiscal year are due from the majority of listed companies in January. Separately, the Securities & Exchange Organization (SEO), Iran’s capital markets regulator, announced further transparency and trading directives for the TSE – aiming to improve the quality and consistency of corporate reporting and to provide more clarity around significant share-price moves over short time periods. December’s ADTV was \$78.2m – the highest average for the previous seven months – signifying domestic money inflows into equities. Institutional activity (52.7%) surpassed retail activity (43.7%). The most actively traded sectors were base metals (20.5%), chemicals (9.3%), mining (8.3%), auto (8.1%) and refineries (7.8%), which together comprised 54.0% of total trades. In the FX market, consistent with the seasonal pattern seen over the past three years (i.e., currency weakness in Q4 and strength in Q1), the rial weakened.

TEDPIX INDEX & P/E (fwd.) RATIO



MARKET CAPITALISATION

Market Cap (\$m)

TSE	Farabourse
91,349	14,698

Value traded (\$m)

TSE	Farabourse
1,274	367

\$1 : 41,844 IRR is the monthly average free-market exchange rate used for this report.

All market data represents the period December 1-31, 2017.

Sources: Tehran Stock Exchange, Bloomberg, MSCI, Royal Exchange, Griffon Asset Management, Bourseview.

IRAN EQUITY MARKETS

SECTOR PERFORMANCE^(a)

BEST PERFORMING SECTORS

Chemicals	↑	10.1%
Base metals	↑	9.0%
Metallic ore	↑	8.1%
Refineries	↑	7.6%
Conglomerates	↑	6.8%

WORST PERFORMING SECTORS

Ceramics & tiles	↓	-8.6%
Metal products	↓	-7.2%
Machinery	↓	-5.4%
Rubber & tyre	↓	-5.3%
Cements, limes & plasters	↓	-5.0%

TOP GAINERS AND LOSERS

GAINERS

Sepahan Oil	<i>Petroleum products</i>	↑	40.6%
Eastern Azarbaijan Pegah Milk	<i>Food stuff excl. Sugar</i>	↑	34.2%
Dr. Abidi Laboratories	<i>Pharmaceuticals</i>	↑	25.4%
Razi Glass Group	<i>Non-metallic ore</i>	↑	25.1%
Kharg Petrochemical	<i>Chemicals</i>	↑	25.0%

LOSERS

Iran Argham Co.	<i>IT & computers</i>	↓	-30.6%
Piazar Agriculture	<i>Food stuff excl. sugar</i>	↓	-25.8%
Pakdis Co.	<i>Food stuff excl. sugar</i>	↓	-23.2%
Azar Refractories	<i>Non-metallic ore</i>	↓	-22.8%
Sarma Afarin	<i>Machinery</i>	↓	-21.7%

SECTOR NEWS

Metals and Mining

The State has recently decreased import tariffs on steel products, creating a more competitive environment for local producers supplying the domestic market. Duties on steel products have recently averaged 20%; now, duties on the most widely used steel products – hot rolled coil (HRC) and blooms/billets – will be reduced to 10% and 5%, respectively.

Additionally, the two largest mining companies, Golgohar and Chadormalu, are becoming more vertically integrated as they expand downstream into steel production. For example, a subsidiary of Golgohar Mining & Industrial Co. plans to start producing up to two million tonnes of semi-finished steel products next year.

Autos

The Government has approved new rules, including new restrictions, on auto importers. The new rules require importers to offer after-sales services and to document verifiable representation deals with the foreign carmaker(s) or respective official distributor(s).

Import duties have also increased significantly. As per the larger directives, vehicles entering the country will be assigned to one of four categories based on engine capacity. The new import tariffs have increased 15-40% overall.

\$1 : 41,844 IRR is the monthly average free-market exchange rate used for this report.

(a) Smaller sectors (i.e., those comprising less than three companies) have been excluded.

All market data represents the period December 1-31, 2017.

Sources: SEO, Bourse Press, Financial Tribune, Techrasa.ir, Codal.ir, Griffon Asset Management.

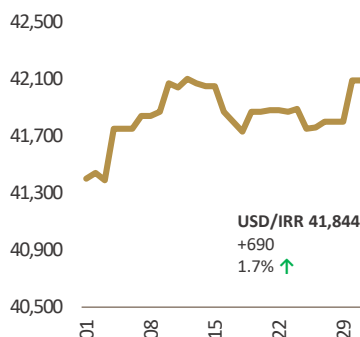
IRAN EQUITY MARKETS

TOP 10 COMPANIES BY MARKET CAPITALISATION

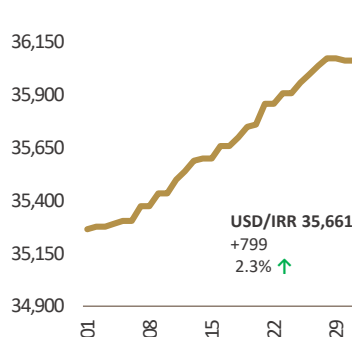
Price values in IRR	Market cap (\$m)	Close price		1M	YTD	52 w/h	52 w/l
Khalij Fars Petrochemicals Chemicals	6,784	5,670	↑	20.6%	36.4%	5,676	3,790
	5.9%						
Mobarakeh Steel Base metals	5,275	3,001	↑	10.3%	135.5%	3,119	1,232
	4.6%						
MCI Telecommunication	3,916	16,988	↓	-1.8%	44.0%	17,502	11,663
	3.4%						
NICICO Base metals	3,547	2,525	↑	23.8%	78.1%	2,525	1,367
	3.1%						
Maroon Petrochemicals Chemicals	3,523	36,600	↓	-2.7%	26.1%	40,500	26,057
	3.1%						
TCI Telecommunication	3,226	2,245	↑	0.0%	22.5%	2,299	1,796
	2.8%						
Tapico Chemicals	2,820	1,455	↑	13.1%	1.9%	1,540	1,210
	2.5%						
Golgozar Mining & Industrial Metallic ore	2,389	3,380	↑	13.8%	63.6%	3,490	1,817
	2.1%						
Parsian Oil & Gas Chemicals	2,348	2,426	↑	2.7%	28.3%	2,555	1,670
	2.1%						
Bandar Abbas Oil Refining Petroleum products	2,335	7,090	↑	2.8%	73.3%	7,500	3,944
	2.0%						

USD/IRR EXCHANGE RATE, DECEMBER 2017

FREE MARKET RATE



CBI OFFICIAL RATE



SECTOR NEWS (CONT'D)

Cars with engine capacities of <1.5 litres, 1.5–2 litres, 2–2.5 litres and 2.5-3 litres will have import duties of 55%, 75%, 95% and 130% respectively. The new directive will also ban the import of ‘luxury cars’ – defined as those costing more than \$40,000 or having an engine capacity of >3 litres (previously >2.5 litres).

IPO

This month there was an IPO in the financial institutions sector: Omid investment bank (10% free float, \$209.8m market cap) became the first investment bank to IPO on the TSE. It debuted on 20 December and closed 12.0% higher as of 31 December.

State Budget

The State Budget for Iranian fiscal year 1397 (March 2018 to March 2019) was submitted to Parliament. The proposed total budget is IRR 11,949 trn (~\$285.6 bn), of which IRR 3,680 trn (~\$87.9 bn) is the general budget for public expenditure. This is 15% higher (in rials) than the 1396 budget and will be financed mainly by tax and oil & gas revenues, comprising 35% and 27%, respectively. It is estimated that the budget is pricing in \$55/barrel for oil (assuming 2.5mbd of exports) with an *effective* official USD/IRR FX rate of 38,500, once FX gains for oil exports are accounted for.

FX

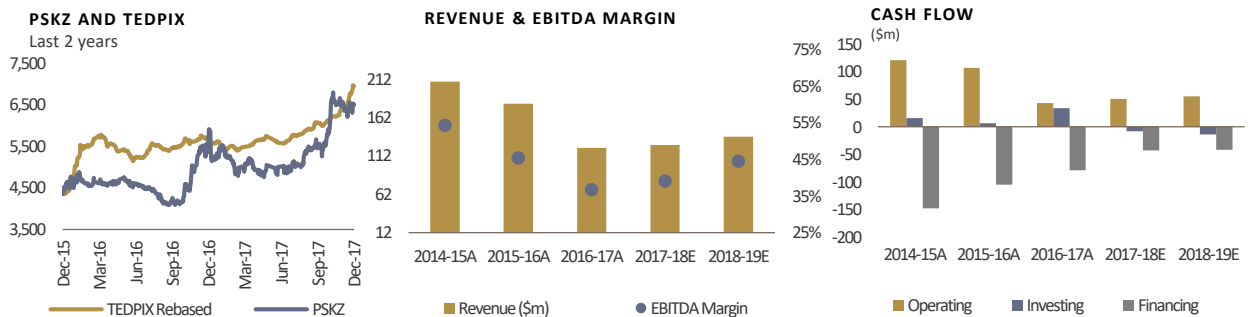
In December, the rial fell 1.7% and 5.8% versus the dollar and euro, respectively.

All market data represents the period December 1-31, 2017.

Sources: SEO, CBI, IFB, Donya-e-Eghesad, Codal.ir, Tehran Stock Exchange, Royal Exchange, Griffon Asset Management.

COMPANY OVERVIEW: KHORASAN PETROCHEMICAL COMPANY

KHORASAN PETROCHEMICAL CO.			
Symbol: PSKZ	Market cap.: \$279.2m	P/E (17-18E) ^(b) : 5.4x	12-month return: ↑12.5%
Exchange: IFB	Enterprise value ^(a) : \$234.6m	5-yr (avg.) dividend payout ratio: 100%	EV/revenue (17-18E) ^(b) : 1.9x
Listed since: 2013	% of market (TSE): 0.25%	Dividend yield (17-18E) ^(b) : 17.4%	EV/EBITDA (17-18E) ^(b) : 4.8x
Last close: IRR 6,523	Free float: 5%	Avg. daily trade value: \$77.5K	ROCE (hist.): 43.4%
90-day change: ↑17.8%	Shares outstanding: 1.79Bn.	52-wk high/low (IRR): 6,798/4,759	ROE (hist.): 40.3%



FINANCIAL STATEMENTS (\$M)					
	14-15A	15-16A	16-17A	17-18E ^(b)	18-19E ^(b)
Urea production (tonnes)	594,943	563,989	530,660	573,705	573,705
Average urea sale price (USD/tonne)	300	263	237	225	260
Revenue	208.4	179.9	122.3	126.0	136.8
Growth %	-15.1%	-13.7%	-32.0%	3.1%	8.6%
EBITDA	113.2	81.7	44.9	49.2	60.9
Growth %	-35.8%	-27.8%	-45.0%	9.6%	23.7%
EBITDA margin	54.3%	45.4%	36.7%	39.0%	44.5%
Net Income	127.8	89.5	49.4	51.6	63.0
Growth %	-40.0%	-29.9%	-44.8%	4.5%	22.1%
Net Profit Margin	61.3%	49.8%	40.4%	41.0%	46.1%
Net Cash	97.2	72.2	24.0	31.0	41.7
Capex	9.5	3.7	4.0	3.8	4.1
Dividend	125.1	88.8	50.5	48.7	59.4

COMPANY OVERVIEW

Khorasan Petrochemical Co. was established in 1992 and listed on the Iran Farabourse in 2013. Khorasan’s production plant is located in Bojnord, the capital of North Khorasan province in northeastern Iran. The company produces mainly urea (of which it is one of the largest urea producers in the country) as well as ammonia and melamine. Production capacity stands at 495,000 tonnes per year, and there are no plans for expansion.

The feedstock used in production is natural gas; this is priced in USD with the CBI official FX rate. Hence two key risks for Khorasan (and the broader petrochemical industry) are the long-term future price of this feedstock and the expected unification of the dual FX rate structure. Despite the recent introduction of a formulaic pricing mechanism by the Ministry of Petroleum to address this uncertainty, the method still lacks full transparency. Feedstock prices have been volatile, rising from 3 USD cents per cubic metre in 2011 to as high as 13 USD cents in 2014. Sales of the main product, urea, are evenly split between exports and the domestic market. Domestic sales are predominantly to the agricultural sector at regulated prices and, to a lesser extent, on the Iran Mercantile Exchange (IME) at market prices. Sales to the local farming industry are subsidised in local currency, equating to significant discounts to global market prices; State regulation stipulates that urea producers have to sell up to 50% (subject to demand) of their output to local farmers. Exports, on the other hand, are based on the free-market exchange rate and sold at global market prices. Should FX unification occur (between the official exchange rate and the free-market rate) and/or the State eliminate or reduce subsidies for natural gas, Khorasan would likely be able to sell much more or even all its urea at or closer to global market prices, be it via domestic sales or increasing exports. Because of the high volume of urea Khorasan supplies to the domestic market compared to most of its domestic peers, it would be one of the main beneficiaries of this combination of events.

The most important factor governing Khorasan’s revenue is the global price of urea, given that more than 80% of the company’s sales derive solely from this product. On the cost side, alongside the feedstock already mentioned, energy and labour are notable elements, all together comprising about 65% of COGS.

This is not a stock recommendation. The above is an introductory information overview. The reference currency rates are based on the yearly average of the free market exchange rates.
 a) The enterprise value calculation is based on net debt from 2017-18 audited semi-annual reports.
 b) 2018 and 2019 numbers are based on Griffon Asset Management’s expectations.
 Sources: Annual company accounts (Codal), company website, Griffon Asset Management.

ABOUT GRIFFON CAPITAL

Griffon Capital is an Iran-focused asset management and private equity group established to unlock value from the country's public and private equity markets. Among Griffon's primary objectives is to allow local and international institutional investors the ability to seamlessly access and maximise opportunities in Iran through purpose-built vehicles and investment products spanning traditional and alternative assets.

The Group's strength is rooted in a robust operating platform developed by leading international advisors and are supported by internationally recognised administrators and auditors. Our platform consists of a high-calibre team with deep local market expertise and an international financial pedigree blended at the board, management and execution levels. This includes a management team steeped in investment banking, wealth and asset management and corporate finance experience. Griffon is also distinguished by on-the-ground local research and primary thinking and a governance culture defined by global best practices in risk management, compliance and reporting.

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On July 14, 2015, the P5+1, the European Union, and Iran reached a Joint Comprehensive Plan of Action ("JCPOA"). Subsequently, following confirmation that relevant JCPOA commitments had been

delivered, certain of the international sanctions and restrictive measures relating to Iran were eased or lifted on 'Implementation Day', 16 January 2016, including the majority of previous EU and UN sanctions on Iran. While this represented a significant relaxation of the sanctions in place against Iran, a number of important restrictions remain in force (including certain sanctions which may affect financial and investment activity).

In particular, notwithstanding the relaxation of sanctions on 'Implementation Day', certain categories of persons may be prohibited from investing in the Fund. The Fund and Investment Manager's policy is to comply with all applicable sanctions, and not to engage in activity that would be sanctionable under the sanctions applicable to non-US persons. Before making or managing any investments in Iranian securities, the Fund and the Investment Manager will put in place a robust compliance framework based on professional advice with a view to ensuring that its activities and investments are compliant with EU and applicable US sanctions and restrictive measures in force from time to time regarding Iran.

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