

19 November 2020

Petronas Chemicals Group

Earnings Recovery in 3QFY20

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3QFY20 saw a recovery in earnings, as expected, amidst a rebound in product prices from the bottom in the previous quarter. Its Pengerang plant is scheduled for a start-up in 1QFY21, with commercialisation 1-2 quarters thereafter. However, we are not entirely positive on the commercialisation given negative EBITDA contribution during its gestation phase. Commencement of the plant will also further increase fluctuations of the group's product margins given its exposure to naphtha-based products. **Maintain MP with TP of RM6.45.**

9MFY20 broadly within expectations. 9MFY20 core net profit of RM1,112m (adjusted for net forex gains and net inventories write-backs), is deemed to be broadly within expectations at 73% of our, and 69% of consensus, full-year earnings forecast. This is considering the weak 1HFY20, especially the slump in earnings in 2QFY20, due to weak product prices amidst peak lockdowns globally. No dividends were announced, also as expected.

Recovery in 3QFY20. 3QFY20 quarter core net profit came in at RM560m, representing a 3.5x jump QoQ, mainly due to the recovery in product prices from the bottom witnessed in the previous quarter. The higher product prices managed to offset the lower production volume (-9%), as a landslide incident at supplier's facilities in Sabah resulted in lower plant utilisation during the quarter (90% vs 100%). The plants have already resumed full operations during the quarter. YoY, 3QFY20 also managed a jump of 19% in core earnings. This was mainly due to the higher plant utilisation (90% vs. 81%) from lesser turnaround activities, offsetting poorer product prices.

Cumulatively, 9MFY20 saw a decline in core earnings by 53% YoY. This was largely attributable to poorer product prices, in tandem with the declining crude oil prices amidst the global Covid-19 pandemic.

Pengerang geared for start-up in 1QFY21. PCHEM is aiming for an integrated start-up of its Pengerang Integrated Complex (PIC) in 1QFY21, with commercialisation to start 1-2 quarters thereafter. However, we are not all positive on the commencement of the plant, as the plant would be loss-making immediately upon commercialisation. Upon commercialisation, the group will have to start recognising fixed costs of depreciation and finance expenses amounting to possibly up to ~RM600m/year. We believe the plant may take >12 months to see positive EBITDA contributions. Additionally, the Pengerang plant would also expose the group to naphtha-based products, potentially increasing fluctuations in product margins, and also heightening the group's earnings correlation to crude oil prices.

Meanwhile, in the more immediate-term, petrochemical prices have been steadier of late, and thus, we may expect to see another stable quarter going into 4QFY20. Note that 4QFY20 may see a one-off charge of USD56m (~RM232m) following the disposal of an associate (40% stake in Butanediol Complex) as part of a portfolio realignment exercise.

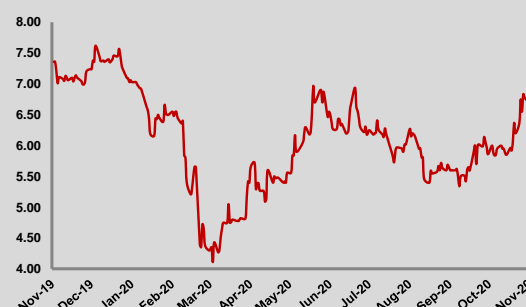
Maintain MARKET PERFORM, and TP of RM6.45, pegged to 21x PER on FY21E EPS, at +0.5SD above its 5-year. No changes were made to our FY20-21E earnings post-results.

Risks to our call include: (i) fluctuations in petrochemical product prices, and (ii) unexpected lower plant utilisation/maintenance.

MARKET PERFORM ↔

Price: RM6.75
Target Price: RM6.45 ↔

Share Price Performance



KLCI	1,604.75
YTD KLCI chg	1.0%
YTD stock price chg	-8.2%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PCHEM MK Equity
Market Cap (RM m)	54,000.0
Shares Outstanding	8,000.0
52-week range (H)	7.62
52-week range (L)	4.00
3-mth avg daily vol:	2,735,602
Free Float	20%
Beta	1.6

Major Shareholders

Petroleum Nasional Bhd	64.4%
Employees Provident Fund	8.8%
Skim Amanah Saham Bumiputera	7.1%

Summary Earnings Table

FYE Dec (RM m)	2019A	2020E	2021E
Revenue	16,370	13,692	15,110
EBIT	2,789	1,679	2,769
PBT	3,155	1,745	2,841
Net Profit (NP)	2,811	1,516	2,450
Core NP (CNP)	2,897	1,516	2,450
Consensus (CNP)		1,605	2,516
Earning Revision (%)		-	-
EPS (sen)	36.2	19.0	30.6
EPS growth (%)	-43.5	-47.7	61.6
DPS (sen)	18.0	9.5	15.3
BV/share (RM)	3.74	3.8	4.0
PER (x)	18.6	35.6	22.0
PBV (x)	1.80	1.76	1.69
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Div. Yield (%)	2.7	1.4	2.3

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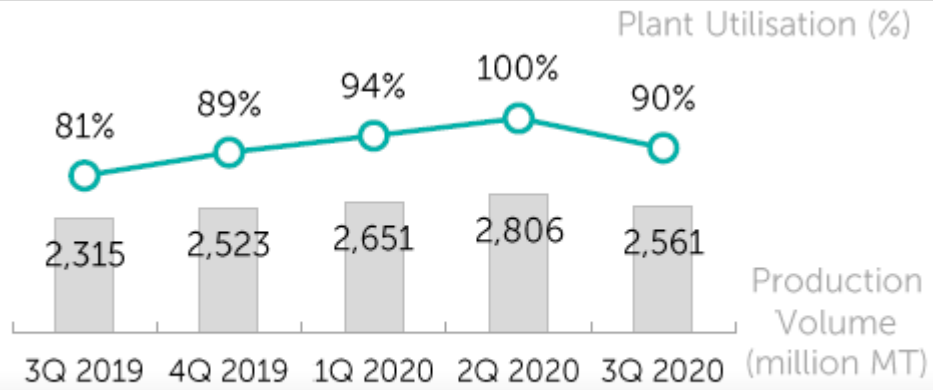
Income Statement								
Y/E : Dec (RM m)	3Q FY20	2Q FY20	Q-o-Q Chg	3Q FY19	Y-o-Y Chg	9M FY20	9M FY19	Y-o-Y Chg
Revenue	3,457	3,178	8.8%	3,669	-5.8%	10,526	12,136	-13.3%
Cost of revenue	(2,574)	(2,458)	4.7%	(2,775)	-7.2%	(8,170)	(8,450)	-3.3%
Gross profit	883	720	22.6%	894	-1.2%	2,356	3,686	-36.1%
Selling and distribution expenses	(227)	(246)	-7.7%	(195)	16.4%	(717)	(646)	11.0%
Administration expenses	(166)	(184)	-9.8%	(152)	9.2%	(537)	(530)	1.3%
Other expenses	(95)	(47)	102.1%	(34)	179.4%	(8)	(50)	-84.0%
Other income	78	82	-4.9%	140	-44.3%	310	403	-23.1%
Operating profit	473	325	45.5%	653	-27.6%	1,404	2,863	-51.0%
Financing costs	(6)	(4)	50.0%	3	-300.0%	(16)	(18)	-11.1%
Joint ventures and associates	12	(30)	-140.0%	(12)	-200.0%	(50)	(59)	-15.3%
Profit before taxation	479	291	64.6%	644	-25.6%	1,338	2,786	-52.0%
Tax expense	(27)	(106)	-74.5%	(86)	-68.6%	(208)	(303)	-31.4%
Non-controlling interests	19	1	1800.0%	(5)	-480.0%	32	(12)	-366.7%
Net profit	471	186	153.2%	553	-14.8%	1,162	2,471	-53.0%
Core Net profit	560	159	252.2%	471	18.9%	1,112	2,366	-53.0%
Gross margin	25.5%	22.7%		24.4%		22.4%	30.4%	
Operating margin	13.7%	10.2%		17.8%		13.3%	23.6%	
PBT margin	13.9%	9.2%		17.6%		12.7%	23.0%	
Net margin	13.6%	5.9%		15.1%		11.0%	20.4%	
Core net margin	16.2%	5.0%		12.8%		10.6%	19.5%	
Effective tax rate	5.6%	36.4%		13.4%		15.5%	10.9%	

Source: Company, Kenanga Research

Segmental Breakdown								
Y/E : Dec (RM m)	3Q FY20	2Q FY20	Q-o-Q Chg	3Q FY19	Y-o-Y Chg	9M FY20	9M FY19	Y-o-Y Chg
Revenue								
Olefins and Derivatives	2,006	1,664	20.6%	2,281	-12.1%	6,071	7,384	-17.8%
Fertilisers and Methanol	1,243	1,317	-5.6%	1,381	-10.0%	3,820	4,725	-19.2%
EBITDA								
Olefins and Derivatives	414	315	31.4%	416	-0.5%	918	1,803	-49.1%
Fertilisers and Methanol	519	404	28.5%	545	-4.8%	1,516	2,044	-25.8%
PAT								
Olefins and Derivatives	258	31	732.3%	232	11.2%	273	1,131	-75.9%
Fertilisers and Methanol	323	198	63.1%	315	2.5%	880	1,360	-35.3%
EBITDA Margins								
Olefins and Derivatives	20.6%	18.9%		18.2%		15.1%	24.4%	
Fertilisers and Methanol	41.8%	30.7%		39.5%		39.7%	43.3%	
PAT Margins								
Olefins and Derivatives	12.9%	1.9%		10.2%		4.5%	15.3%	
Fertilisers and Methanol	26.0%	15.0%		22.8%		23.0%	28.8%	

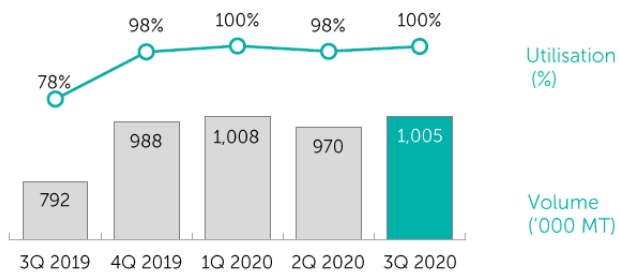
Source: Company, Kenanga Research

PCHEM's Plant Utilisation and Production Volumes

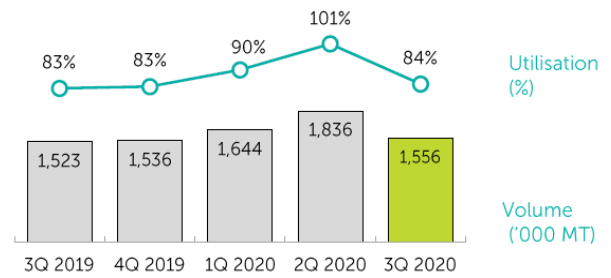


Source: Company

Olefins and Derivatives – Plant Utilisation and Volumes



Fertiliser and Methanol – Plant Utilisation and Volumes



Source: Company

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Peer Comparison

Name	Last Price	Market Cap	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price	Rating
	(RM)	(RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
BUMI ARMADA BHD	0.270	1,589.2	N	12/2020	1.4%	4.8%	17.9%	7.2%	5.6	4.8	4.4	0.5	0.4	9.8%	0.0%	0.300	OP
DAYANG ENTERPRISE HLDGS BHD	0.990	1,146.2	Y	12/2020	-35.3%	15.2%	-74.8%	34.2%	4.9	19.4	14.5	0.7	0.7	3.7%	0.0%	1.20	MP
DIALOG GROUP BHD	3.63	20,470.7	Y	06/2021	29.4%	11.7%	7.8%	8.2%	34.0	31.5	29.1	5.0	4.5	14.9%	1.0%	4.35	OP
MALAYSIA MARINE AND HEAVY EN	0.375	600.0	Y	12/2020	-1.8%	29.8%	-371.3%	-144.8%	N.A.	N.A.	N.A.	0.3	0.3	-4.0%	0.0%	0.380	OP
MISC BHD	6.90	30,799.8	Y	12/2020	-4.1%	13.5%	24.0%	0.9%	19.1	15.4	15.3	0.9	0.9	5.6%	4.3%	8.90	OP
PANTECH GROUP HOLDINGS BHD	0.395	295.1	Y	02/2021	-41.9%	57.1%	-47.6%	79.8%	9.0	17.1	9.5	0.5	0.5	2.8%	2.5%	0.310	UP
PETRONAS CHEMICALS GROUP BHD	6.75	54,000.0	Y	12/2020	-16.4%	10.4%	-47.7%	61.6%	18.6	35.6	22.0	1.8	1.8	5.0%	1.4%	6.45	MP
PETRONAS DAGANGAN BHD	19.50	19,372.4	Y	12/2020	-41.6%	32.0%	-60.1%	86.6%	23.6	59.1	31.7	3.2	3.2	5.5%	1.4%	16.00	UP
SAPURA ENERGY BHD	0.120	1,917.5	Y	01/2021	-11.4%	8.7%	-112.1%	-242.4%	N.A.	N.A.	N.A.	0.2	0.2	-1.8%	0.0%	0.050	UP
SERBA DINAMIK HOLDINGS	1.70	5,726.1	Y	12/2020	15.0%	15.0%	9.6%	12.1%	11.5	10.5	9.4	2.4	1.8	19.5%	3.2%	2.70	OP
UZMA BHD	0.480	153.6	Y	06/2021	-6.8%	2.3%	681.5%	43.1%	56.9	7.3	5.1	0.3	0.3	4.7%	0.0%	0.570	MP
VELESTO ENERGY BHD	0.130	1,068.0	Y	12/2020	-15.8%	6.9%	-222.8%	-131.0%	33.4	N.A.	N.A.	0.4	0.4	-1.4%	0.0%	0.130	UP
WAH SEONG CORP BHD	0.425	329.1	Y	12/2020	-56.3%	45.5%	-283.5%	-185.5%	4.7	N.A.	N.A.	0.3	0.4	-14.1%	0.0%	0.430	UP
YINSON HOLDINGS BHD	5.04	5,368.0	Y	01/2021	44.8%	4.9%	121.4%	4.1%	25.0	11.3	10.9	3.4	2.7	26.4%	1.2%	5.50	OP
Simple Average					-10.1%	18.4%	-25.6%	-26.1%	20.5	21.2	15.2	1.4	1.3	5.5%	1.1%		

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
 MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
 NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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Published and printed by:

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