

30 May 2023

# Petronas Chemicals Group

## Earnings Routed Yet Again

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**PCHEM's 1QFY23 results underwhelmed expectations, mainly due to weak volumes and product spreads which we believe will prevail in the near term given a weak demand outlook. Hence, we cut our FY23-24F net profit forecasts by 62% and 17%, respectively, lower our TP by 21% to RM6.20 (from RM7.80) and downgrade our call to UNDERPERFORM (from MARKET PERFORM).**

**Grossly below expectations.** 1QFY23 core net profit of RM459m disappointed, merely making up 9% of our full-year forecast and 12% of the full-year consensus estimate. The variance versus our forecast was mainly due to lower-than-expected sales volumes and product spreads at the fertilizers & methanol (F&M) segment.

**Fertilizers faltered.** Its weaker core net profit (-52% QoQ) were mainly due to: (i) contraction in sales volume, and (ii) weak product spreads on the back of lower average selling prices (ASP). Additionally, this was exacerbated by: (i) a weaker USD versus MYR, and (ii) chunky net pre-operating costs at Pengerang Integrated Complex (PIC) (circa RM100m). In particular, bottomline contraction was mainly driven by the F&M segment due to tepid sales for urea and ammonia products. Meanwhile, 1QFY23 production volumes (-5% QoQ) were impacted by lower plant utilization (PU) of 96% (4QFY22: 100%). This was due to increased plant maintenance activities at PC Aromatics and PC LDPE. The above more than offset narrowed losses at the specialties segment as sales volumes improved (+16%).

**Specialties turned loss making after Perstop acquisition.** The dismal YoY performance (-77%) was mainly attributed to: (i) high earnings base given that record 1QFY22 profit was propped by strong product spreads, (ii) increased energy and utilities costs, and (iii) USD strength versus MYR. Therefore, bottomline contracted in spite of a surge in topline. The latter was underpinned by a higher sales volumes as well as consolidation of PCHEM's newly acquired specialty chemicals company, Perstop. Meanwhile, volumes were propped by higher PU of 96% (1Q22: 87%) given less turnaround activities at the olefins & derivatives plants.

**Demand still languishing.** We believe that the recovery in global demand for petrochemicals will likely be muted in the near term due to tepid consumer spending, particularly in China. This is mainly underpinned by an inflationary environment that has hit consumer spending. Moreover, Chinese consumption has recently shifted from consumer goods during the pandemic to services currently. This change in behaviour is likely driven by the upliftment of Covid-19 lockdowns. Hence, Chinese consumers are now prioritizing travel and social activities. As such, this has dented demand for consumer goods that require petrochemical feedstock as raw material input.

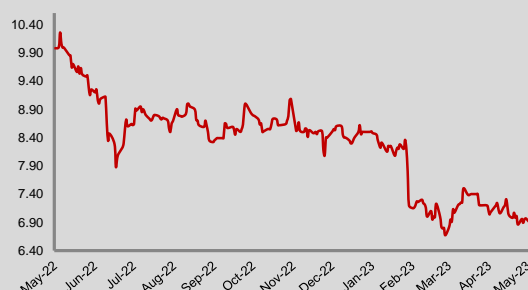
**Forecasts.** We cut our FY23-24F net profit forecasts by 62% and 17%, respectively, to account for weaker ASPs and volumes at the F&M segment.

We also lower our valuation on PCHEM to 14.3x CY24 PER (from 15x). This is in-line and to correspond with its large Asian peers (e.g. PTT Chem, LG Chem, Formosa, LCTITAN) which have recently been de-rated. As a result of this, and coupled with the cut in our forecasts, our TP is lowered to RM6.20 (from RM7.80). There is no change to our TP based on ESG given a 3-star rating as appraised by us (see Page 5).

**UNDERPERFORM** ↓

**Price:** RM6.87  
**Target Price:** RM6.20 ↓

### Share Price Performance



KLCI 1,404.93  
YTD KLCI chg -6.1%  
YTD stock price chg -20.1%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PCHEM MK Equity
Market Cap (RM m)	54,960.0
Shares Outstanding	8,000.0
52-week range (H)	10.26
52-week range (L)	6.67
3-mth avg daily vol:	5,688,105
Free Float	15%
Beta	1.0

### Major Shareholders

Petrolia Nasional Bhd	64.4%
Employees Provident Fund	11.0%
Amanah Saham Nasional	5.2%

### Summary Earnings Table

FYE Dec (RM m)	2022A	2023F	2024F
Revenue	28,953	28,964	33,631
EBIT	6,634	2,419	4,073
PBT	6,733	2,269	3,923
<b>Net Profit (NP)</b>	<b>6,322</b>	<b>1,997</b>	<b>3,453</b>
<b>Core NP (CNP)</b>	<b>6,436</b>	<b>1,997</b>	<b>3,453</b>
Consensus (CNP)	-	5,268	5,393
Earning Revision (%)	-	-61.8	-17.3
EPS (sen)	80.5	25.0	43.2
EPS growth (%)	-11.4	-69.0	72.9
DPS (sen)	41.0	12.0	22.0
BV/share (RM)	4.9	5.0	5.2
PER (x)	9.7	27.5	15.9
PBV (x)	1.6	1.4	1.3
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Div. Yield (%)	5.3	1.7	3.2

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We downgrade PCHEM to **UNDERPERFORM** from **MARKET PERFORM** due to the gloomy outlook for ASPs. This emanates from the weak demand outlook as highlighted above. In turn, this may result in sustained weakness in product spreads, and hence earnings.

**Risks to our call include:** (i) demand rebounds due to strong economic growth, (ii) dip in crude oil prices leading to cheap feedstock costs for PIC, and (iii) market supply tightens due to plant outages and delay of upcoming capacity.

### Result Highlights

	1Q	4Q	Q-o-Q	1Q	Y-o-Y
FYE Dec (RM m)	FY23	FY22	Chg	FY22	Chg
Revenue	7,557	8,704	-13.2%	6,634	13.9%
Cost of revenue	-6,167	-6,707	-8.1%	-4,157	48.4%
<b>Gross profit</b>	<b>1,390</b>	<b>1,997</b>	<b>-30.4%</b>	<b>2,477</b>	<b>-43.9%</b>
Selling and distribution expenses	-496	-539	-8.0%	-279	77.8%
Administration expenses	-337	-493	-31.6%	-183	84.2%
Other expenses	-72	-428	-83.2%	0	#DIV/0!
Other income	107	83	28.9%	82	30.5%
<b>Operating profit</b>	<b>592</b>	<b>620</b>	<b>-4.5%</b>	<b>2,097</b>	<b>-71.8%</b>
Financing costs	-40	-32	25.0%	-7	471.4%
Joint ventures and associates	38	-27	-240.7%	123	-69.1%
<b>Profit before taxation</b>	<b>590</b>	<b>561</b>	<b>5.2%</b>	<b>2,213</b>	<b>-73.3%</b>
Tax expense	-54	-77	-29.9%	-141	-61.7%
Non-controlling interests	-4	-3	33.3%	4	-200.0%
<b>Net profit</b>	<b>532</b>	<b>481</b>	<b>10.6%</b>	<b>2,076</b>	<b>-74.4%</b>
<b>Core Net profit</b>	<b>459</b>	<b>963</b>	<b>-52.3%</b>	<b>2,025</b>	<b>-77.3%</b>
Gross margin	18.4%	22.9%		37.3%	
Operating margin	7.8%	7.1%		31.6%	
PBT margin	7.8%	6.4%		33.4%	
Net margin	7.0%	5.5%		31.3%	
Core net margin	6.1%	11.1%		30.5%	
Effective tax rate	9.2%	13.7%		6.4%	

Source: Company, Kenanga Research

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FYE Dec (RM m)	1Q FY23	4Q FY22	Q-o-Q Chg	1Q FY22	Y-o-Y Chg
<b><u>Revenue</u></b>					
Olefins and Derivatives	3,393	3,494	-2.9%	2,743	23.7%
Fertilisers and Methanol	2,407	3,533	-31.9%	3,304	-27.1%
Specialties	1,745	1,664	4.9%	578	201.9%
<b><u>EBITDA</u></b>					
Olefins and Derivatives	299	372	-19.6%	832	-64.1%
Fertilisers and Methanol	782	1,428	-45.2%	1,396	-44.0%
Specialties	88	7	1157.1%	216	-59.3%
<b><u>PAT</u></b>					
Olefins and Derivatives	170	47	261.7%	733	-76.8%
Fertilisers and Methanol	533	1,112	-52.1%	1,172	-54.5%
Specialties	-29	-163	-82.2%	163	-117.8%
<b><u>EBITDA Margins</u></b>					
Olefins and Derivatives	8.8%	10.6%		30.3%	
Fertilisers and Methanol	32.5%	40.4%		42.3%	
Specialties	5.0%	0.4%		37.4%	
<b><u>PAT Margins</u></b>					
Olefins and Derivatives	5.0%	1.3%		26.7%	
Fertilisers and Methanol	22.1%	31.5%		35.5%	
Specialties	-1.7%	-9.8%		28.2%	

Source: Company, Kenanga Research

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### Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
BUMI ARMADA BHD	OP	0.645	0.750	16.28%	3,817.2	N	12/2023	13.1	13.6	1.0%	3.5%	4.9	4.7	0.6	13.9%	0.0	0.0%
DAYANG ENTERPRISE HLDGS BHD	OP	1.15	1.90	65.22%	1,331.4	Y	12/2023	11.2	12.6	12.0%	11.8%	10.2	9.2	0.8	8.6%	3.0	2.6%
DIALOG GROUP BHD	OP	2.11	3.10	46.92%	11,905.8	Y	06/2023	9.5	9.9	5.1%	4.8%	22.3	21.3	2.2	10.2%	2.8	1.3%
MISC BHD	MP	7.22	7.60	5.26%	32,228.2	Y	12/2023	57.5	55.0	8.1%	-4.3%	12.6	13.1	0.8	6.8%	33.0	4.6%
PETRONAS CHEMICALS GROUP BHD	UP	6.87	6.20	-9.75%	54,960.0	Y	12/2023	25.0	43.2	-69.0%	72.9%	27.5	15.9	1.4	5.0%	12.0	1.7%
PETRONAS DAGANGAN BHD	MP	22.34	24.90	11.46%	22,193.8	Y	12/2023	106.0	92.6	41.3%	-12.6%	21.1	24.1	3.9	18.3%	106.0	4.7%
PETRON MALAYSIA REFINING	MP	4.60	4.65	1.09%	1,242.0	Y	12/2023	103.0	97.8	-7.6%	-5.0%	4.5	4.7	0.5	11.9%	21.0	4.6%
UZMA BHD	OP	0.645	0.900	39.53%	227.1	Y	06/2023	7.7	9.9	85.0%	28.5%	8.4	6.5	0.4	5.1%	0.0	0.0%
VELESTO ENERGY BHD	UP	0.225	0.190	-15.56%	1,848.5	Y	12/2023	0.7	1.3	-36.1%	73.3%	30.3	17.5	0.8	2.6%	0.0	0.0%
WAH SEONG CORP BHD	OP	0.865	0.970	12.14%	669.8	Y	12/2023	10.7	12.8	6.1%	19.1%	8.0	6.8	1.0	13.4%	0.0	0.0%
YINSON HOLDINGS BHD	OP	2.60	3.65	40.38%	7,557.2	N	01/2024	20.8	25.2	-18.4%	21.2%	12.5	10.3	1.6	13.7%	2.0	0.8%
Sector Aggregate					137,981.1					-32.4%	18.1%	17.0	14.4	1.3	10.0%		1.8%

Source: Kenanga Research

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### Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★		
	Community Investment	★	★	★	★	
	Workers Safety & Wellbeing	★	★	★		
	Corporate Governance	★	★	★		
	Anti-Corruption Policy	★	★	★	★	
	Emissions Management	★	★	★	★	
SPECIFIC	Transition to Low-Carbon Future	★	★	★		
	Conservation & Biodiversity	★	★	★	★	
	Effluent/Waste Management	★	★	★	★	
	Water Management	★	★	★		
	Supply Chain Management	★	★	★		
	Energy Efficiency	★	★	★		
OVERALL		★	★	★		

☆ denotes half-star  
 ★ -10% discount to TP  
 ★★ -5% discount to TP  
 ★★★ TP unchanged  
 ★★★★ +5% premium to TP  
 ★★★★★ +10% premium to TP

### 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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