

29 November 2023

Petronas Chemicals Group

Recovery Disrupted by Downtime

By *Lim Sin Kiat, CFA* / limsk@kenanga.com.my

PCHEM's 9MFY23 results disappointed due to production disruption. Its 9MFY23 core profit plunged 74% YoY due to weaker product spreads. We believe its earnings have bottomed in FY23 and it is poised for a recovery in FY24. We cut our FY23-24F net profit forecasts by 11% and 8%, respectively, reduce our TP by 8% to RM6.74 (from RM7.30) but maintain our MARKET PERFORM call.

Slightly below expectations. Its 9MFY23 core profit of RM1.4b (after excluding EI of RM185m forex gain and RM29m inventory write down) disappointed at only 74% and 55% of our full-year forecast and the full-year consensus estimate, respectively. The variance against our forecast came largely from weaker-than-expected plant utilisation, particularly at olefin & derivatives (O&D) division due to an unplanned shutdown due to power disruption. No dividends were declared in the quarter.

YoY, its 9MFY23 revenue increased 6% YoY mainly due to uptick in the O&D division's top line due to a higher sales volume and the inclusion of Perstop's revenue into the specialties division upon the completion of its acquisition. This was partially offset by weaker revenue from the fertilisers & methanol (F&M) division due to lower product prices. Its plant utilisation was flat YoY at 85%.

However, its core net profit plunged by 74% due to: (i) weaker product spreads at the O&D division, (ii) weaker urea and methanol prices at the F&M division, and (iii) losses at the specialties division on margin squeeze amidst intense competition.

QoQ, its 3QFY23 revenue contracted 5% as plant utilization fell to 77% from 82% three months ago due to higher plant maintenance activities while the specialties division continued to be hurt by weak product prices. However, its core net profit contracted by a steeper 31% due to high plant turnaround activities, partially cushioned by a better showing from the F&M division on lower feedstock costs.

The key takeaways from PCHEM's analysts briefing are as follows:

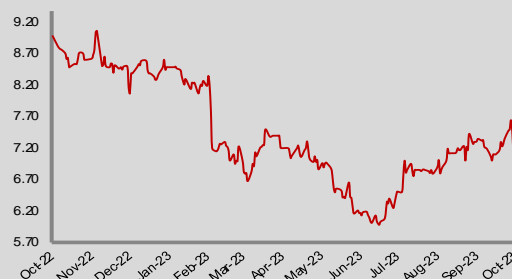
1. Its Kertih cracker plant was shut down (unplanned) in Oct 2023 due to power disruptions but had since returned to full operation. It guided for plant utilization of 85% and above in FY23 (vs. 90% a year ago).
2. It has secured ethane and propane (feedstock for O&D) supply contract extension from Petronas for another year throughout FY24.
3. Its Pengerang Integrated Complex (PIC) is targeted to be fully operational by 1QCY24. Currently, the facility is still at the pilot production stage. The good news is its loss before interest, depreciation and amortization halved QoQ on an increased volume.

Outlook. While it appears that polyolefin prices (the O&D division) have stabilised at slightly under the USD1,000/MT level, its near-term demand outlook remains tepid on soft global demand. On the supply side, the new petrochemical chemical production capacity coming onstream in China in 2024 will cap the recovery in polyolefin prices.

MARKET PERFORM ↔

Price: RM7.05
Target Price: RM6.74 ↓

Share Price Performance



KLCI 1,440.60
YTD KLCI chg -3.7%
YTD stock price chg -16.0%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PCHEM MK Equity
Market Cap (RM m)	57,760.0
Shares Outstanding	8,000.0
52-week range (H)	9.18
52-week range (L)	5.84
3-mth avg daily vol:	3,762,573
Free Float	16%
Beta	1.2

Major Shareholders

Petroliam Nasional Bhd	64.4%
Employees Provident Fund	11.6%
Amanah Saham Nasional	3.6%

Summary Earnings Table

FYE Dec (RM m)	2022A	2023F	2024F
Revenue	28,953	24,390	27,961
EBIT	7,087	1,913	4,176
PBT	6,733	2,025	4,288
Net Profit (NP)	6,322	1,704	3,596
Core NP (CNP)	6,333	1,704	3,596
Consensus (CNP)	-	2,586	3,619
Earning Revision (%)	-	-10.7	-7.6
EPS (sen)	79.0	21.3	45.0
EPS growth (%)	-13.9	-73.0	111.1
DPS (sen)	41.0	14.9	22.5
BV/share (RM)	4.9	4.9	5.2
PER (x)	8.9	33.1	15.7
PBV (x)	1.4	1.4	1.4
Net Gearing (x)	-0.2	-0.2	-0.2
Div. Yield (%)	5.8	2.1	3.2

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Meanwhile, the urea market has eased recently with prices at USD299/MT (from USD345/MT in 1HFY23) due to easing of supply concerns globally and weak global demand. We believe similar dynamics will persist into FY24 although demand for urea is expected to recover gradually YoY. Losses in its specialities division are expected to narrow as its US and Europe markets are showing early signs of recovery.

Forecasts. We cut our FY23F earnings by 11% after adjusting for lower plant utilisation to 86% from 89% and FY24 earnings by 8% after assuming lower urea price assumption of USD350/MT (from USD400/MT).

As a result, we cut our TP by 8% to RM6.74 (from RM7.30) which is based on an unchanged 15x PER FY24F - in line with the valuations of Asian peers (e.g. PTT Chem, LG Chem, Formosa, LCTITAN). There is no change to our ESG rating (3-star rating) as appraised by us (see Page 5).

We like the company due to: (i) signs of bottoming of polyolefin prices supported by crude prices, (ii) specialty chemicals division potentially seeing trough earnings in FY23 with FY24 a year of expected gradual recovery, and (iii) its superior margins vs. its peers due to a favourable cost structure. However, the upside to its earnings and hence share price is capped by the limited upside of its product prices amidst a tepid global economic outlook. Maintain **MARKET PERFORM**.

Risks to our call include: (i) worse-than-expected economic growth globally leading to weaker petrochemical prices, (ii) PIC costs exceeding estimates due to operational issues, and (iii) worse-than-expected oversupply in specialty chemicals particularly in European region.

Result Highlights								
	3Q	2Q	Q-o-Q	3Q	Y-o-Y	9M	9M	Y-o-Y
FYE Dec (RM m)	FY23	FY23	Chg	FY22	Chg	FY23	FY22	Chg
Revenue	6,784.0	7,113.0	-4.6%	7,032.0	-3.5%	21,454.0	20,249.0	6.0%
Cost of revenue	-5,556.0	-5,923.0	-6.2%	-4,942.0	12.4%	-17,646.0	-13,570.0	30.0%
Gross profit	1,228.0	1,190.0	3.2%	2,090.0	-41.2%	3,808.0	6,679.0	-43.0%
Selling and distribution expenses	-470.0	-468.0	0.4%	-340.0	38.2%	-1,434.0	-897.0	59.9%
Administration expenses	-394.0	-279.0	41.2%	-219.0	79.9%	-1,010.0	-664.0	52.1%
Other expenses	-2.0	0.0	#DIV/0!	0.0	#DIV/0!	-74.0	-11.0	572.7%
Other income	244.0	259.0	-5.8%	509.0	-52.1%	610.0	906.0	-32.7%
Operating profit	606.0	702.0	-13.7%	2,040.0	-70.3%	1,900.0	6,013.0	-68.4%
Financing costs	-33.0	-22.0	50.0%	-19.0	73.7%	-95.0	-34.0	179.4%
Joint ventures and associates	13.0	14.0	-7.1%	-1.0	-1400.0%	65.0	192.0	-66.1%
Profit before taxation	586.0	694.0	-15.6%	2,020.0	-71.0%	65.0	192.0	-66.1%
Tax expense	-147.0	-61.0	141.0%	-122.0	20.5%	-262.0	-329.0	-20.4%
Non-controlling interests	-15.0	-5.0	200.0%	-3.0	400.0%	-24.0	-2.0	1100.0%
Net profit	424.0	628.0	-32.5%	1,895.0	-77.6%	1,584.0	5,840.0	-72.9%
Core Net profit	312.0	450.0	-30.7%	1,717.0	-81.8%	1,417.0	5,448.0	-74.0%
Core EPS	5.3	7.9	-32.5%	0.2	2137.5%	19.8	73.0	-72.9%
DPS	0.0	8.0	-100.0%	0.0	nm	8.0	25.0	-68.0%
Gross margin	18.1%	16.7%		29.7%		17.7%	33.0%	
Operating margin	8.9%	9.9%		29.0%		8.9%	29.7%	
PBT margin	8.6%	9.8%		28.7%		0.3%	0.9%	
Net margin	6.3%	8.8%		26.9%		7.4%	28.8%	
Core net margin	4.6%	6.3%		24.4%		6.6%	26.9%	
Effective tax rate	25.1%	8.8%		6.0%		403.1%	171.4%	

Source: Company, Kenanga Research

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Segmental Breakdown								
FYE Dec (RM m)	3Q FY23	2Q FY23	Q-o-Q Chg	3Q FY22	Y-o-Y Chg	9M FY23	9M FY22	Y-o-Y Chg
<u>Revenue</u>								
Olefins and Derivatives	3,496.0	3,633.0	-3.8%	3,419	2.3%	10,522.0	9,438.0	11.5%
Fertilisers and Methanol	1,809.0	1,874.0	-3.5%	3,187	-43.2%	6,987.0	9,317.0	-25.0%
Specialties	1,467.0	1,591.0	-7.8%	-	-	4,803.0	-	-
<u>PAT</u>								
Olefins and Derivatives	211.0	422.0	-50.0%	843	-75.0%	803.0	2,530.0	-68.3%
Fertilisers and Methanol	360.0	241.0	49.4%	994	-63.8%	1,134.0	2,958.0	-61.7%
Specialties	44.0	-164.0	-126.8%	-	#DIV/0!	-149.0	-	-
<u>PAT Margins</u>								
Olefins and Derivatives	6.0%	11.6%		24.7%		7.6%	26.8%	
Fertilisers and Methanol	19.9%	12.9%		31.2%		16.2%	31.7%	
Specialties	3.0%	-10.3%		-		-3.1%	-	

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	0.535	0.580	8.4%	3,168.6	N	12/2023	10.3	13.6	-25.9%	31.9%	5.2	3.9	0.5	11.1%	0.0	0.0%
DIALOG GROUP BHD	OP	2.09	3.10	48.3%	11,793.0	Y	06/2024	9.9	10.3	10.7%	4.2%	21.1	20.3	2.0	9.7%	4.2	2.0%
MISC BHD	MP	7.20	7.00	-2.8%	32,139.0	Y	12/2023	46.8	49.6	-11.8%	6.0%	15.4	14.5	0.8	5.5%	30.0	4.2%
PETRONAS CHEMICALS GROUP BHD	MP	7.08	6.74	-4.8%	56,640.0	Y	12/2023	21.3	45.0	-73.0%	111.1%	31.6	15.0	1.4	8.7%	14.9	2.2%
PETRONAS DAGANGAN BHD	MP	22.16	22.40	1.1%	22,014.9	Y	12/2023	94.8	94.4	25.2%	-0.4%	23.4	23.5	3.7	16.1%	75.8	3.4%
PETRON MALAYSIA REFINING	MP	4.57	4.74	3.7%	1,233.9	Y	12/2023	109.3	99.6	-2.0%	-8.8%	4.2	4.6	0.5	12.6%	21.0	4.6%
UZMA BHD	OP	0.780	1.22	56.4%	302.0	Y	06/2024	11.8	12.2	16.9%	3.5%	6.6	6.4	0.6	8.7%	0.0	0.0%
VELESTO ENERGY BHD	UP	0.225	0.190	-15.6%	1,848.5	Y	12/2023	0.6	1.3	-45.8%	104.6%	35.7	17.4	0.8	2.2%	0.0	0.0%
WAH SEONG CORP BHD	MP	0.945	0.94	-0.5%	731.7	Y	12/2023	8.8	10.4	-46.5%	18.2%	10.7	9.0	1.2	8.8%	0.0	0.0%
YINSON HOLDINGS BHD	OP	2.47	3.79	53.4%	7,179.7	N	01/2024	29.0	29.9	13.7%	3.0%	8.5	8.3	1.4	18.4%	2.0	0.8%
Sector Aggregate					138,927.0					-38.1%	32.4%	18.6	14.1	1.3	9.7%		1.7%

Source: Kenanga Research

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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KENANGA INVESTMENT BANK BERHAD (15678-H)
 Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
 Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my

