



Petronas Chemicals Group Berhad

(5183 | PCHEM MK) Industrial Products & Services | Chemicals

Maintain NEUTRAL

Headwinds Remain amid Positive Demand Outlook

Revised Target Price: RM6.72
(previously RM7.04)

KEY INVESTMENT HIGHLIGHTS

- **Maintain NEUTRAL, revised TO TP: RM6.72**
- **2Q23 earnings contracted more-than-expected by -67%yoy due to lower product spread, lower share of profit and forex loss**
- **2Q23 revenue increased +8%yoy from inclusion of subsidiary and higher production volume**
- **Slower demand recovery and inflationary pressures remain a challenge**

Maintain NEUTRAL, revised TP: RM6.72. Petronas Chemicals Group (PCG)'s 1HFY23 earnings came in below our expectation at 31.3% of full year FY23 earnings estimates. Given the continuously challenging outlook, we maintain **NEUTRAL** on PCG with a lower **target price of RM6.72** (previously RM7.04).

Earnings down -67%yoy. PCG's 2QFY23 earnings down by -66.6%yoy to RM628m. This was due to lower product spread and lower share of profit from joint ventures and as associates compounded by unrealised forex loss on revaluation of debt at Petstorp.

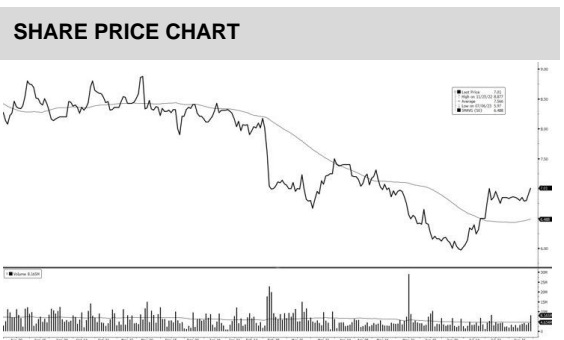
Revenue up +8.1%yoy. 2QFY23 revenue was up +8.1%yoy to RM7.1b, due to higher sales volumes and inclusion of revenue contribution from a recently acquired subsidiary, partially offset by lower product prices. Overall plant utilisation rate in 2QFY23 was higher at 82% (2QFY22: 72%) due to no statutory turnaround and lower plant maintenance activities.

Olefins & Derivatives (O&D). O&D's 2QFY23 earnings down-55.8%yoy to RM422m. 2QFY23 revenue was up +10.9%yoy to RM3.6b. Lower earnings were due to: (i) lower product spreads, (ii) higher energy and utilities costs, and (iii) pre-operation costs from a joint operating company. Meanwhile, revenue was higher due to higher sales volumes and weakening Ringgit against US Dollar. Plant utilisation rate was higher at 98% (2QFY22: 89%).

Fertilisers & Methanol (F&M). F&M's 2QFY23 earnings dropped -69.6%yoy to RM241m. 2QFY23 revenue was also down -33.7%yoy to RM1.9b. The decrease in earnings and revenue was due to lower product spreads and lower product prices, offset by weakening Ringgit against US Dollar. Plant utilisation rate was higher at 73% (2QFY22: 62%)

Specialties. Specialties slipped to a loss of RM164m in 2QFY23 from a loss of RM29m in 1QFY23. 2QFY23 revenue was lower by -8.8%qoq to RM1.6b. The lower earnings were attributable to lower sales volume and higher foreign exchange loss on revaluation of loan, as well as slower demand recovery and increased price competition from China.

RETURN STATISTICS	
Price @ 22 nd August 2023 (RM)	7.01
Expected share price return (%)	-4.1
Expected dividend yield (%)	+6.0
Expected total return (%)	+1.9



Price performance (%)	Absolute	Relative
1 month	7.8	5.0
3 months	16.8	-1.5
12 months	-19.4	-17.4

INVESTMENT STATISTICS			
FYE Mar	2023E	2024F	2025F
Revenue	25,261	26,219	27,527
Operating Profit	2,875	3,155	3,471
Profit Before Tax	2,874	3,170	3,513
Core PATAMI	2,672	2,988	3,350
Core EPS	33.4	37.4	41.9
DPS	40.0	41.0	42.0
Dividend Yield	6.0%	6.1%	6.3%

KEY STATISTICS	
FBM KLCI	1,451.53
Issue shares (m)	8,000.0
Estimated free float (%)	16.5
Market Capitalisation (RM'm)	54,080.0
52-wk price range	RM5.84-RM9.18
3-mth average daily volume (m)	4.56
3-mth average daily value (RM'm)	29.76
Top Shareholders (%)	
Petroleum Nasional Bhd	64.35
Employees Provident Fund	11.51
Amanah Saham Nasional Bhd	3.62

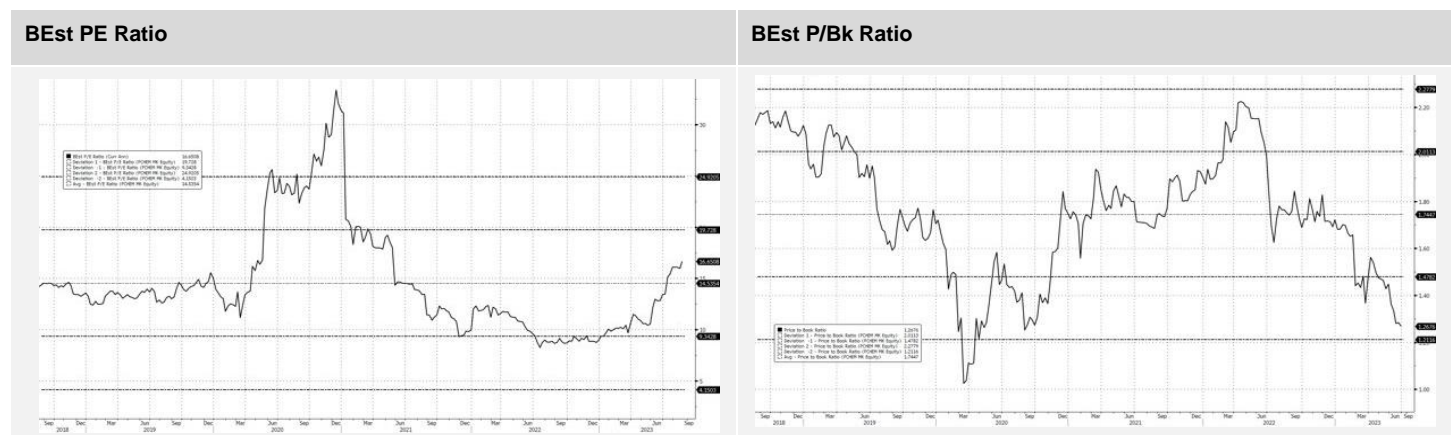
Improvement from increased Brent price and upcoming festivities. We believe that a full utilization of PCG’s production plants relies on maintenance activities, raw material availability and utilities supply. For O&D, ethylene pricing is expected to be supported by firm naphtha price to an average of USD695/MT in the coming quarters (average YTD price: USD640/MT), despite ample supply. Ethylene and Paraxylene are also expected to remain stable on sufficient supply amid China’s plant shutdowns on top of a balanced demand. Polyethylene is believed to improve in pricing ahead of festivities. For F&M, we are expecting a near term demand improvement for Urea in consideration of the planting season. Meanwhile, Ammonia and Methanol are expected to have a weaker demand on top of a stable supply due to maintenance shutdowns. For specialties chemicals, with the weak demand from certain end markets and softening of raw material prices in Europe, we expect that this segment will be sluggish in the near future, and will be critically supported by China’s recovery in 2HCY23.

Key challenges. PCG’s performance is tied to: (i) the global economic climate in terms of rate hikes and inflationary pressures, (ii) petrochemical product prices in correlation with Brent crude oil prices, (iii) utilization rate of production facilities, and (iv) fluctuations in foreign exchange rates. However, we opine that the improvement from China’s economic recovery in CY23 to be the main catalyst to mitigate these challenges, in addition to higher demand amid sufficient supply and feedstock.

Revised earnings estimates. In consideration of the 1HFY23 earnings coming below our expectations, we revised our FY23 and FY24 earnings estimates downwards by -28% and -37% respectively. We input additional cost of sales in tandem with its extensive maintenance activities until end year and higher energy and utilities cost.

Revised target price. Accordingly, we **revised our target price to RM6.72** (previously RM7.04). The petrochemicals market’s ambiguity in global demand may remain affected by consumer expenditures and competition from other producers. The potential for an excess of products in the market might lead to downward price pressure, impacting profits and lowering plant usage. Nonetheless, we maintain a conservative stance on our perspective for PCG, on the back of a higher Brent crude price and supply-demand balance, as well as PCG’s commitment to operational and commercial excellence, in the near term. Our target price is based on pegging a PER of 18x to an EPS24 of 37.4sen. The PER is a discount from the chemical and material industry’s 5-year average of 20x, due to the current slowdown in demand for petrochemicals in CY23.

FORWARD BAND



Source: Bloomberg, MIDFR

Table 1: Petronas Chemicals's quarterly earnings review

Financial year ending 31st Dec (in RM'm unless stated otherwise)	Quarterly results					Cumulative results		
	2QFY22	1QFY23	2QFY23	QoQ (%)	YoY (%)	1HFY22	1HFY23	YoY (%)
Revenue	6,583.0	7,557.0	7,113.0	-5.9	8.1	13,217.0	14,670.0	11.0
Cost of revenue	(4,471.0)	(6,167.0)	(5,923.0)	-4.0	32.5	(8,628.0)	(12,090.0)	40.1
Gross Profit	2,112.0	1,390.0	1,190.0	-14.4	-43.7	4,589.0	2,580.0	-43.8
Selling & Dist Expenses	(278.0)	(496.0)	(468.0)	-5.6	68.3	(557.0)	(964.0)	73.1
Admin Expenses	(262.0)	(337.0)	(279.0)	-17.2	6.5	(445.0)	(616.0)	38.4
Other Expenses	-	(72.0)	-	-100.0	nm	8.0	(72.0)	-1000.0
Other Income	315.0	107.0	259.0	142.1	-17.8	397.0	366.0	-7.8
Operating Profit	1,887.0	592.0	702.0	18.6	-62.8	3,992.0	1,294.0	-67.6
Net Financing Costs	(8.0)	(40.0)	(22.0)	-45.0	175.0	(15.0)	(62.0)	-
Associates	70.0	38.0	14.0	-63.2	-80.0	193.0	52.0	-73.1
Profit Before Tax	1,949.0	590.0	694.0	17.6	-64.4	4,170.0	1,284.0	-69.2
Tax expense	(66.0)	(54.0)	(61.0)	13.0	-7.6	(207.0)	(115.0)	-44.4
Profit After Tax	1,883.0	536.0	633.0	18.1	-66.4	3,963.0	1,169.0	-70.5
Minority Interests	(3.0)	(4.0)	(5.0)	25.0	66.7	(7.0)	(9.0)	28.6
PATAMI	1,880.0	532.0	628.0	18.0	-66.6	3,956.0	1,160.0	-70.7
				<i>+ / (-) ppts</i>				<i>+ / (-) ppts</i>
Gross margin (%)	32.1	18.4	16.7	-1.7	-15.4	34.7	17.6	-17.1
Operating profit margin (%)	28.7	7.8	9.9	2.0	-18.8	30.2	8.8	-21.4
PBT margin (%)	29.6	7.8	9.8	1.9	-19.8	31.6	8.8	-22.8
PATAMI margin (%)	28.6	7.0	8.8	1.8	-19.7	29.9	7.9	-22.0
Tax rate (%)	3.4	9.2	8.8	-0.4	5.4	5.0	9.0	4.0
Segmental:								
<i>Revenue</i>								
- Olefins & Derivatives	3,276.0	3,393.0	3,633.0	7.1	10.9	6,019.0	3,633.0	-39.6
- Fertilisers & Methanol	2,826.0	2,407.0	1,874.0	-22.1	-33.7	6,130.0	1,874.0	-69.4
- Specialties	-	1,745.0	1,591.0	-8.8	nm	-	1,591.0	nm
<i>Profit After Tax</i>								
- Olefins & Derivatives	954.0	170.0	422.0	148.2	-55.8	1,687.0	592.0	-64.9
- Fertilisers & Methanol	792.0	533.0	241.0	-54.8	-69.6	1,964.0	774.0	-60.6
- Specialties	-	(29.0)	(164.0)	465.5	nm	-	(193.0)	nm

Source: Company, MIDFR

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023E	2024F	2025F
Revenue	23,025	28,953	25,261	26,219	27,527
EBITDA	7,010	6,643	2,875	3,155	3,471
D&A	1,650	1,589	1,637	1,641	1,647
Profit before tax	7,710	6,742	2,874	3,170	3,513
Tax	-391	-406	-184	-164	-145
Core PATAMI	7,319	6,323	2,672	2,988	3,350
Balance Sheet (RM'm)	2021A	2022A	2023E	2024F	2025F
Fixed assets	22,041	27,213	21,961	22,537	22,948
Intangible assets	684	9,364	2,275	2,730	3,159
Others	2,303	2,835	10,000	9,469	9,129
Non-current assets	25,028	39,412	34,236	34,736	35,236
Cash	16,390	8,888	9,075	8,167	7,926
Trade debtors	2,737	3,619	2,591	2,576	2,692
Others	2,299	3,511	5,575	7,327	8,246
Current assets	21,426	16,018	17,241	18,070	18,864
Trade creditors	4,378	5,914	3,829	4,265	4,156
Short-term debt	232	229	546	491	339
Current liabilities	4,953	6,502	4,375	4,756	4,495
Long-term debt	2,156	2,489	1,703	2,043	2,077
Others	3,959	6,706	7,771	7,531	7,417
Non-current liabilities	6,115	9,195	9,474	9,574	9,494
Share capital	8,871	8,871	8,871	8,871	8,871
Retained earnings	25,980	30,207	24,086	24,582	25,286
Others	535	655	4,670	5,023	5,953
Equity	35,386	39,733	37,627	38,476	40,110
Cash Flow (RM'm)	2021A	2022A	2023E	2024F	2025F
PBT	7,710	6,742	2,874	3,170	3,513
Depreciation & amortisation	1,650	1,589	1,637	1,641	1,647
Changes in working capital	-188	910	192	275	328
Operating cash flow	8,186	8,049	6,292	6,217	6,252
Capital expenditure	-1,539	-1,881	-2,041	-1,858	-1,759
Investing cash flow	-1,557	-12,951	-4,172	-4,630	-4,751
Debt raised/(repaid)	321	352	1,350	843	633
Dividends paid	-3,206	-3,844	-2,544	-2,589	-2,630
Financing cash flow	-3,184	-3,806	-1,933	-2,495	-2,442
Net cash flow	3,456	-8,238	187	-908	-1,241
Beginning cash flow	12,707	16,390	8,888	9,075	8,167
Ending cash flow	16,390	8,888	9,075	8,167	7,926
--Profitability Margins	2021A	2022A	2023E	2024F	2025F
EBITDA margin	30.4%	22.9%	11.4%	12.0%	12.6%
PBT margin	33.5%	23.3%	11.4%	12.1%	12.7%
Core PAT margin	31.8%	21.8%	10.6%	11.4%	12.1%

Source: Bloomberg, MIDFR

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MIDF AMANAH INVESTMENT BANK: GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.

ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell

☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology