

# Petronas Chemicals Group Berhad

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

**Maintain BUY**

## Earnings marred by unplanned plant shutdown

**Revised Target Price: RM6.75**

(Previously RM8.77)

### KEY INVESTMENT HIGHLIGHTS

- **Petronas Chemicals Group Bhd's 4QFY19 core profit of RM340.0m came in below expectations**
- **Revenue and earnings impacted by unplanned plant shutdown and subdued product prices due to weak crude oil price**
- **Differentiated and specialized products to cushion the impact from subdued product prices**
- **FY20F earnings revised down by -17.9%**
- **Maintain BUY with a lower TP of RM6.75 per share**

**4QFY19 earnings below expectations.** Petronas Chemicals Group Bhd's (PChem) 4QFY19 core earnings came in at RM340.0m. This brings its FY19 cumulative earnings to RM2,815.0m which was below our and consensus' expectations at 77.5% and 84.2% respectively. Comparing against 4QFY18, revenue and earnings during the quarter contracted by -16.4%yoy and -73.5%qoq mainly due to the unplanned shutdown of its PC Methanol Plant 2 during the quarter coupled with soft product prices. Meanwhile on a quarterly sequential basis, revenue grew by +15.4%qoq due to higher sales volume vs 3QFY19 however, earnings dipped by -38.5%qoq due to the weak product prices. Average product prices were down by -19%yoy and -21%qoq during the quarter.

**Overall PUR of 89% recorded in 4QFY19.** The dip in PChem's revenue and earnings during the quarter were due to several reasons. Firstly, there was an unplanned plant shutdown that took place during the quarter at its PC Methanol Plant 2 which resulted in lower production volume. Secondly, the subdued product prices during the quarter mainly due to the weak movement of crude oil price and last but not least, the strengthening of Ringgit during the quarter.

**Olefins and Derivatives.** The segment reported a lower PUR rate of 98% (vs 100% in 4QFY18) during the quarter due to higher maintenance activities. As a result, sales volume was lower in-line with the lower production which resulted in revenue and earnings declining by -27.9%yoy and -69.9%yoy respectively. Furthermore, the segment's average product prices were lower due to the market being amply supplied and the soft movement of the crude oil price during the quarter.

**Fertilisers and Methanol.** The segment recorded a lower PUR of 83% during the quarter vs 89% in the same period last year mainly due to unplanned shutdown at its PC Methanol Plant 2 which lasted for 21days. This has resulted in lower production during the quarter. However; sales volume was higher due to product drawdown from inventory. Furthermore, the higher sales volume was negated also by the subdued product prices with revenue and earnings registering a decline of -22.1%yoy and -37.2%yoy respectively.

### RETURN STATISTICS

|   |              |
|---|--------------|
| Price @ 26 <sup>th</sup> February 2020 (RM) | 5.85         |
| Expected share price return (%)             | +15.3        |
| Expected dividend yield (%)                 | +6.3         |
| <b>Expected total return (%)</b>            | <b>+21.6</b> |

### SHARE PRICE CHART



| Share price performance (%) | Absolute | Relative |
|-----------------------------|----------|----------|
| 1 month                     | -15.46   | -11.07   |
| 3 months                    | -20.41   | -12.10   |
| 12 months                   | -36.76   | -27.29   |

### KEY STATISTICS

|                                  |            |
|----------------------------------|------------|
| FBM KLCI                         | 1,495.19   |
| Syariah compliant                | Yes        |
| Issue shares (m)                 | 8,000      |
| Estimated free float (%)         | 16.92      |
| Market Capitalisation (RM'm)     | 46,800     |
| 52-wk price range                | 5.7 – 9.49 |
| Beta vs FBM KLCI (x)             | 0.93       |
| Monthly velocity (%)             | 11.02      |
| Monthly volatility (%)           | 14.33      |
| 3-mth average daily volume (m)   | 4.08       |
| 3-mth average daily value (RM'm) | 28.3       |
| Top Shareholders (%)             |            |
| Petroleum Nasional Bhd           | 64.35      |
| Employees Provident Fund         | 7.71       |
| Skim Amanah Saham Bumiputera     | 5.68       |

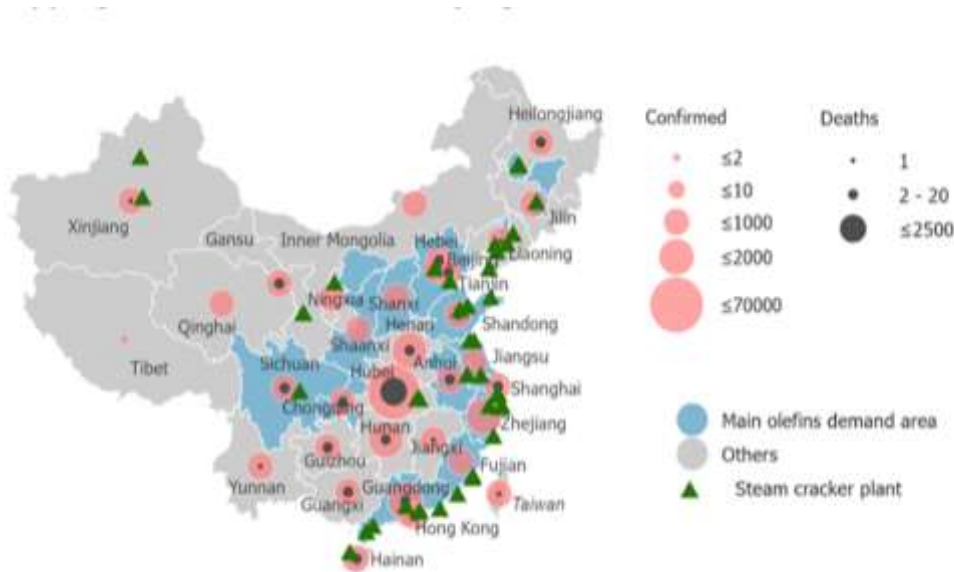
### Analyst(s)

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**Coronavirus to cause disruptions to petrochemicals supply and demand from China.** The recent outbreak of Coronavirus (Covid-19) in China has since spread to various countries across the world. This has caused major delays and shutdowns of business operations in several provinces in China including at the epicenter of the virus which is the Hubei Province. The prolonged Lunar New Year holiday that took place since late-January had further exacerbated the situation with disruptions at various petrochemical plants in China. This includes Sinopec-SK Wuhan Petrochemical which had lowered the operating rate of its 800kta cracker by 10% recently. Its 300kts cracker expansion which is scheduled for completion in July has also been delayed.

While some of the businesses have gradually re-opened, many of the cities are still in lockdown which reduces not only traveling and working activities but also the consumer spending activities significantly. Correspondingly, the consumption of commodities as well as disposable packaging has declined with the weak consumer spending activities which resulted in lower demand for petrochemicals. Refer to Figure 1 below. As the outbreak currently showing no immediate signs of abating, we are of the opinion that the outbreak might last the entire 1QFY20. Hence, we opine that the supply-demand dynamics of the petrochemicals market will result in continued pressure on the average selling prices across the petrochemicals value chain especially on the olefins and derivatives.


**Figure 1: Map of China’s olefins industry vs coronavirus cases**



Source: WHO, Wood Mackenzie

**FY20F earnings revised down by -17.9%.** After assessing the impact from the coronavirus outbreak as well as the potential continued weak movement of the crude oil price, we are reducing our FY20F earnings by -17.9% to RM3,597 (from RM4,381m previously). We have also introduced our FY21-22F numbers in this report.

**Maintain BUY with a lower TP of RM6.75.** Post earnings revision, we are maintaining our **BUY** recommendation on PChem with a lower target price of **RM6.75** (from RM8.77 previously). Our valuation is derived from pegging a lower PER20 of 15x to a lower EPS20 of 45.0sen. We remain sanguine on company given that its fundamentals remain intact and we foresee some form of recovery in product prices given the recent performance of the crude oil price.

Additionally, with the full-commissioning of RAPID Pengerang this year, we are expecting PChem to start moving towards producing more differentiated and specialized products starting with the commissioning of PC Isononanol in Pengerang. Furthermore, with the completion of its statutory TA activities, production volumes will be restored to pre-TA period and further ramp-up from Pengerang – which will be able to produce a wider product range (C2-C6) compared to Kerteh and Gebeng combined, will assist in arresting the impact from the subdued product prices if it lingers into next year. Dividend yield remains attractive at 5.0% FY20F as of yesterday’s closing price. 

**INVESTMENT STATISTICS**

| <b>Financial year ending 31st Dec (in RM'm unless stated otherwise)</b> | <b>2018A</b> | <b>2019A</b> | <b>2020E</b> | <b>2021F</b> | <b>2022F</b> |
|---|--------------|--------------|--------------|--------------|--------------|
| Revenue   | 19,576       | 16,370       | 17,527       | 18,184       | 19,388       |
| EBIT  | 5,559        | 3,214        | 4,319        | 4,761        | 5,076        |
| Pretax Profit   | 5,650        | 3,155        | 4,594        | 5,044        | 5,364        |
| Net Profit  | 4,979        | 2,815        | 3,597        | 3,950        | 4,200        |
| EPS (sen)   | 62.0         | 35.2         | 45.0         | 49.4         | 52.5         |
| EPS growth (%)  | 19.2%        | -43.2%       | 27.8%        | 9.8%         | 6.3%         |
| PER (x)   | 9.4          | 16.6         | 13.0         | 11.8         | 11.1         |
| Dividend per share (sen)  | 32.0         | 18.0         | 37.0         | 38.0         | 39.0         |
| Dividend yield (%)  | 5.5%         | 3.1%         | 6.3%         | 6.5%         | 6.7%         |

Source: Company, MIDFR

**PETRONAS CHEMICALS GROUP BERHAD: 4QFY19 RESULTS SUMMARY**

| Financial year ending 31st Dec<br>(in RM'm unless stated<br>otherwise) | Quarterly results |                |                |                     |              | Cumulative results |                 |                     |
|--|-------------------|----------------|----------------|---------------------|--------------|--------------------|-----------------|---------------------|
|  | 4QFY18            | 3QFY19         | 4QFY19         | QoQ (%)             | YoY (%)      | FY18               | FY19            | YoY (%)             |
| <b>Revenue</b>   | <b>5,062.0</b>    | <b>3,669.0</b> | <b>4,234.0</b> | <b>15.4</b>         | <b>-16.4</b> | <b>19,576.0</b>    | <b>16,370.0</b> | <b>-16.4</b>        |
| Cost of revenue  | (3,355.0)         | (2,775.0)      | (3,464.0)      | 24.8                | 3.2          | (12,702.0)         | (11,914.0)      | -6.2                |
| <b>Gross Profit</b>  | <b>1,707.0</b>    | <b>894.0</b>   | <b>770.0</b>   | <b>-13.9</b>        | <b>-54.9</b> | <b>6,874.0</b>     | <b>4,456.0</b>  | <b>-35.2</b>        |
| Selling & Dist Expenses  | (220.0)           | (195.0)        | (232.0)        | 19.0                | 5.5          | (818.0)            | (878.0)         | 7.3                 |
| Admin Expenses   | (181.0)           | (152.0)        | (224.0)        | 47.4                | 23.8         | (694.0)            | (754.0)         | 8.6                 |
| Other Expenses   | (19.0)            | (34.0)         | (90.0)         | 164.7               | 373.7        | (200.0)            | (163.0)         | -18.5               |
| Other Income   | 152.0             | 140.0          | 153.0          | 9.3                 | 0.7          | 397.0              | 553.0           | 39.3                |
| <b>Operating Profit</b>  | <b>1,439.0</b>    | <b>653.0</b>   | <b>377.0</b>   | <b>-42.3</b>        | <b>-73.8</b> | <b>5,559.0</b>     | <b>3,214.0</b>  | <b>-42.2</b>        |
| Net Financing Costs  | (4.0)             | 3.0            | (13.0)         | -533.3              | 225.0        | (17.0)             | (31.0)          | -                   |
| Associates   | 42.0              | (12.0)         | 5.0            | -141.7              | -88.1        | 108.0              | (54.0)          | -150.0              |
| <b>Profit Before Tax</b>   | <b>1,477.0</b>    | <b>644.0</b>   | <b>369.0</b>   | <b>-42.7</b>        | <b>-75.0</b> | <b>5,650.0</b>     | <b>3,129.0</b>  | <b>-44.6</b>        |
| Tax expense  | (178.0)           | (86.0)         | (57.0)         | -33.7               | -68.0        | (592.0)            | (334.0)         | -43.6               |
| <b>Profit After Tax</b>  | <b>1,299.0</b>    | <b>558.0</b>   | <b>312.0</b>   | <b>-44.1</b>        | <b>-76.0</b> | <b>5,058.0</b>     | <b>2,795.0</b>  | <b>-44.7</b>        |
| Minority Interests   | 14.0              | 5.0            | (28.0)         | -660.0              | -300.0       | 79.0               | (20.0)          | -125.3              |
| <b>PATAMI</b>  | <b>1,285.0</b>    | <b>553.0</b>   | <b>340.0</b>   | <b>-38.5</b>        | <b>-73.5</b> | <b>4,979.0</b>     | <b>2,815.0</b>  | <b>-43.5</b>        |
|  |                   |                |                | <i>+ / (-) ppts</i> |              |                    |                 | <i>+ / (-) ppts</i> |
| Gross margin (%)   | 33.7              | 24.4           | 18.2           | -6.2                | -15.5        | 35.1               | 27.2            | -7.9                |
| Operating profit margin (%)  | 28.4              | 17.8           | 8.9            | -8.9                | -19.5        | 28.4               | 19.6            | -8.8                |
| PBT margin (%)   | 29.2              | 17.6           | 8.7            | -8.8                | -20.5        | 28.9               | 19.1            | -9.7                |
| PATAMI margin (%)  | 25.4              | 15.1           | 8.0            | -7.0                | -17.4        | 25.4               | 17.2            | -8.2                |
| Tax rate (%)   | 12.1              | 13.4           | 15.4           | 2.1                 | 3.4          | 10.5               | 10.7            | 0.2                 |
| <b>Segmental:</b>  |                   |                |                |                     |              |                    |                 |                     |
| <i>Revenue</i>   |                   |                |                |                     |              |                    |                 |                     |
| - Olefins & Derivatives  | 3,224.0           | 2,281.0        | 2,576.0        | 12.9                | -20.1        | 12,297.0           | 9,955.0         | -19.0               |
| - Fertilisers & Methanol   | 1,850.0           | 1,381.0        | 1,441.0        | 4.3                 | -22.1        | 7,369.0            | 6,165.0         | -16.3               |
|  |                   |                |                |                     |              |                    |                 |                     |
| <i>Profit After Tax</i>  |                   |                |                |                     |              |                    |                 |                     |
| - Olefins & Derivatives  | 693.0             | 232.0          | 45.0           | -80.6               | -93.5        | 2,829.0            | 1,151.0         | -59.3               |
| - Fertilisers & Methanol   | 524.0             | 315.0          | 329.0          | 4.4                 | -37.2        | 2,261.0            | 1,708.0         | -24.5               |

Source: Company, MIDFR

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### MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

#### STOCK RECOMMENDATIONS

|                     |  |
|---------------------|--|
| <b>BUY</b>          | Total return is expected to be >10% over the next 12 months.   |
| <b>TRADING BUY</b>  | 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.  |
| <b>NEUTRAL</b>      | Total return is expected to be between -10% and +10% over the next 12 months.  |
| <b>SELL</b>         | Total return is expected to be <10% over the next 12 months.   |
| <b>TRADING SELL</b> | 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

|                 |  |
|-----------------|--|
| <b>POSITIVE</b> | The sector is expected to outperform the overall market over the next 12 months.   |
| <b>NEUTRAL</b>  | The sector is to perform in line with the overall market over the next 12 months.  |
| <b>NEGATIVE</b> | The sector is expected to underperform the overall market over the next 12 months. |