Petronas Chemicals Group Berhad

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

Lower Product Spread Drags 1Q23 Earnings Down

***Downgrade to* NEUTRAL**

(previously BUY)

***Revised* Target Price: RM7.04**

(previously RM10.82)

KEY INVESTMENT HIGHLIGHTS

- **Downgrade to NEUTRAL, revised TP: RM7.04**
- **1QFY23 earnings came below expectations, -74%yoy due to lower product spread, higher internal energy cost**
- **This was despite higher revenue (+14%yoy) from inclusion of subsidiary and higher production volume**
- **Uncertain demand, inflation and oversupply remain as challenges**

Downgrade NEUTRAL, revised TP: RM7.04. Petronas Chemicals Group (PCG)'s 1QFY23 earnings came in below our full year estimates. Given the challenging outlook for PCG, we downgrade our recommendation for PCG to **NEUTRAL** with a lower **target price** of **RM7.04** (previously RM10.82).

Earnings down -74%yoy. PCG's 1QFY23 earnings shrunk by -74.4%yoy but gained +10.6%qoq to RM532m. This was due to lower product spread, as well as higher energy and utilities costs. Nonetheless, 1QFY23 revenue was up +13.9%yoy but down -13.2%qoq to RM7.6b.

Olefins & Derivatives (O&D). O&D's 1QFY23 earnings down-76.8%yoy but surged nearly 4-fold from 4QFY22, to RM170m. Revenue was up +23.7%yoy but down -2.9%qoq to RM3.4b.

Plant utilisation rate was higher at 94% (1QFY22: 75%) due to lower plant statutory turnaround and maintenance activities, subsequently resulting in higher production and sales volume.

Fertilisers & Methanol (F&M). F&M's 1QFY23 earnings dropped -54.5%yoy and -52.1%qoq to RM533m. Revenue was also down -27.1%yoy and -31.9%qoq to RM2.4b.

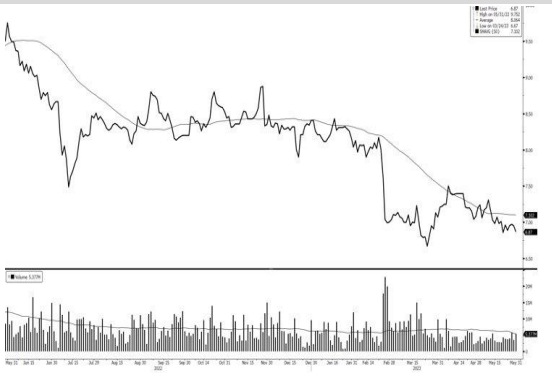
Plant utilisation rate was higher of 97% (1QFY22: 93%) due to lower plant maintenance activities resulting in higher production and sales volumes. The decrease in earnings and revenue was mainly due to lower product prices; offset by weakening of MYR against USD.

Specialties. Specialties segment to a loss of RM29m in 1QFY23. Revenue was up by over 2-fold to RM1.7b from RM578m in 4QFY22. The higher revenue was due to the recent inclusion of a subsidiary, Perstorp. However, the segment is loss-making, as a result of lower demand and less cyclicality attributable to the higher customised requirements of the products and more barriers for substitution.

Inflation fears and stabilised prices expected. We opine that plant maintenance, feedstock availability, and utilities play a vital role in ensuring the full utilization of PCG's production plants. We remain cautious of the group's prospects as product prices are expected to soften from the uncertain demand for O&D due to global inflationary pressure. Prices for F&M products, however, are expected to stabilize, supported by improving demand.

RETURN STATISTICS	
Price @ 29th May 2023 (RM)	6.87
Expected share price return (%)	+2.5
Expected dividend yield (%)	+5.7
Expected total return (%)	**+8.2**

SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	-3.0	-2.2
3 months	-2.8	-0.7
12 months	-31.3	-24.5

INVESTMENT STATISTICS

FYE Mar	2023E	2024F	2025F
Revenue	25,014	23,376	23,041
Operating Profit	4,252	4,348	4,378
Profit Before Tax	4,961	5,005	5,017
Core PATAMI	4,759	4,834	4,862
Core EPS	59.5	60.4	60.8
DPS	40.0	41.0	42.0
Dividend Yield	4.1%	4.2%	4.3%

KEY STATISTICS	
FBM KLCI	1,404.9
Issue shares (m)	8000.0
Estimated free float (%)	15.1
Market Capitalisation (RM'm)	54,960.0
52-wk price range	RM6.67-RM10.20
3-mth average daily volume (m)	5.45
3-mth average daily value (RM'm)	38.68
Top Shareholders (%)	
Petroliam Nasional Bhd	64.35
Employees Provident Fund	11.01
Amanah Saham Nasional Bhd	5.21

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For specialty chemicals, the demand recovery is expected to persist as restocking is underway and also to support ESG practice which the usage of green chemicals. in light with the growing demand for green chemicals for ESG practices.

Key risks. PCG is expected to face key challenges in the near term, including: (i) turbulent global economic conditions, (ii) volatile prices of petrochemical products, which closely correlate with crude oil prices, and (iii) fluctuations in foreign exchange rates.

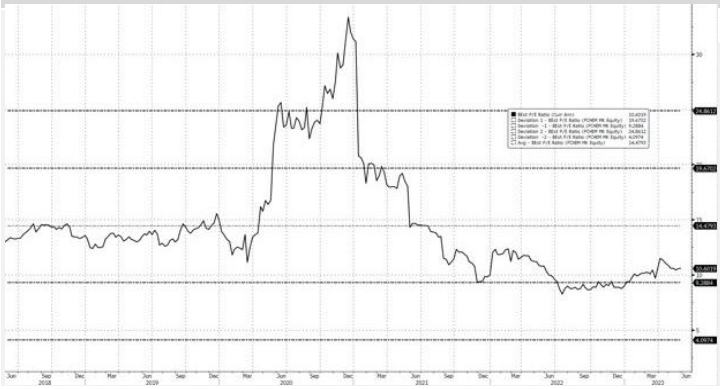
Revised earnings estimates. In consideration of the 1QFY23 earnings and the uncertainty of the F&M demand in tandem with the growing pressure of inflation influencing the feedstock and product prices, we revised our FY23 and FY24 earnings estimates downwards by -47% and -40% respectively.

Revised target price. Accordingly, we **revised our target price to RM7.04** (previously RM10.82). The uncertainty of the petrochemicals market in terms of global demand, influenced by weak consumer spending due to inflationary pressures remain. The possibility of oversupply of products in the market could also pressure prices to go downward and affect profitability and reduced plant utilization. Nevertheless, we remain cautious on our outlook for PCG despite the support of crude oil prices, stabilizing in a USD75pb to USD85pb range and is likely to maintain as such in the near foreseeable future.

Our target price is based on pegging a PER of 15.5x to an EPS23 of 45.3sen. The PER is based on the chemical and material industry's 5-year average.

FORWARD BAND

BEst PE Ratio



BEst P/Bk Ratio



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		
	1QFY22	4QFY22	1QFY23	QoQ (%)	YoY (%)	3MFY22	3MFY23	YoY (%)
Revenue	**6,634.0**	**8,704.0**	**7,557.0**	**-13.2**	**13.9**	**6,634.0**	**7,557.0**	**13.9**
Cost of revenue	(4,157.0)	(6,707.0)	(6,167.0)	-8.1	48.4	(4,157.0)	(6,167.0)	48.4
Gross Profit	**2,477.0**	**1,997.0**	**1,390.0**	**-30.4**	**-43.9**	**2,477.0**	**1,390.0**	**-43.9**
Selling & Dist Expenses	(279.0)	(539.0)	(496.0)	-8.0	77.8	(279.0)	(496.0)	77.8
Admin Expenses	(183.0)	(493.0)	(337.0)	-31.6	84.2	(183.0)	(337.0)	84.2
Other Expenses	8.0	(428.0)	(72.0)	-83.2	-1000.0	8.0	(72.0)	-1000.0
Other Income	82.0	83.0	107.0	28.9	30.5	82.0	107.0	30.5
Operating Profit	**2,105.0**	**620.0**	**592.0**	**-4.5**	**-71.9**	**2,105.0**	**592.0**	**-71.9**
Net Financing Costs	(7.0)	(32.0)	(40.0)	25.0	471.4	(7.0)	(40.0)	-
Associates	123.0	(27.0)	38.0	-240.7	-69.1	123.0	38.0	-69.1
Profit Before Tax	**2,221.0**	**561.0**	**590.0**	**5.2**	**-73.4**	**2,221.0**	**590.0**	**-73.4**
Tax expense	(141.0)	(77.0)	(54.0)	-29.9	-61.7	(141.0)	(54.0)	-61.7
Profit After Tax	**2,080.0**	**484.0**	**536.0**	**10.7**	**-74.2**	**2,080.0**	**536.0**	**-74.2**
Minority Interests	(4.0)	(3.0)	(4.0)	33.3	0.0	(4.0)	(4.0)	0.0
PATAMI	**2,076.0**	**481.0**	**532.0**	**10.6**	**-74.4**	**2,076.0**	**532.0**	**-74.4**
				+/(-) ppts				*+/(-) ppts*
Gross margin (%)	37.3	22.9	18.4	-4.5	-18.9	37.3	18.4	-18.9
Operating profit margin (%)	31.7	7.1	7.8	0.7	-23.9	31.7	7.8	-23.9
PBT margin (%)	33.5	6.4	7.8	1.4	-25.7	33.5	7.8	-25.7
PATAMI margin (%)	31.3	5.5	7.0	1.5	-24.3	31.3	7.0	-24.3
Tax rate (%)	6.3	13.7	9.2	-4.6	2.8	6.3	9.2	2.8
Segmental:								
Revenue								
- Olefins & Derivatives	2,743.0	3,494.0	3,393.0	-2.9	23.7	2,743.0	3,393.0	23.7
- Fertilisers & Methanol	3,304.0	3,533.0	2,407.0	-31.9	-27.1	3,304.0	2,407.0	-27.1
- Specialties	-	578.0	1,745.0	201.9	-	-	1,745.0	#DIV/0!
Profit After Tax								
- Olefins & Derivatives	733.0	47.0	170.0	261.7	-76.8	733.0	170.0	-76.8
- Fertilisers & Methanol	1,172.0	1,112.0	533.0	-52.1	-54.5	1,172.0	533.0	-54.5
- Specialties	-	113.0	(29.0)	-125.7	-	-	(29.0)	-

Source: Company, MIDFR

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023E	2024F	2025F
Revenue	23,025	28,953	25,014	23,376	23,041
EBITDA	7,010	6,643	4,252	4,348	4,378
D&A	1,650	1,589	1,637	1,641	1,637
Profit before tax	7,710	6,742	4,961	5,005	5,017
Tax	-391	-406	-273	-265	-251
Core PATAMI	7,319	6,323	4,759	4,834	4,862

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	2,750	3,150
Non-current assets	**25,028**	**39,412**	**26,295**	**27,432**	**28,300**
Cash	16,390	8,888	12,472	12,500	12,591
Trade debtors	2,737	3,619	2,591	2,576	2,692
Current assets	**21,426**	**16,018**	**17,294**	**17,401**	**17,727**
Trade creditors	4,378	5,914	4,829	5,015	5,206
Short-term debt	232	229	240	245	280
Current liabilities	**4,953**	**6,502**	**5,605**	**5,504**	**5,762**
Long-term debt	2,156	2,489	1,703	2,043	2,077
Non-current liabilities	**6,115**	**9,195**	**6,415**	**7,282**	**7,517**
Share capital	8,871	8,871	8,871	8,871	8,871
Retained earnings	25,980	30,207	24,086	24,582	25,286
Equity	**35,386**	**39,733**	**33,568**	**34,047**	**34,749**

Cash Flow (RM'm)	2021A	2022A	2023E	2024F	2025F
PBT					
Depreciation & amortisation	1,650	1,589	1,637	1,641	1,637
Changes in working capital	-188	910	192	275	128
Operating cash flow	**8,186**	**8,049**	**6,292**	**6,217**	**6,352**
Capital expenditure	-1,539	-1,881	-2,041	-1,858	-1,759
Investing cash flow	**-1,557**	**-12,951**	**-4,172**	**-4,630**	**-4,951**
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**	1,274	1,800	1,911
Beginning cash flow	**12,707**	**16,390**	**8,888**	**10,612**	**12,412**
Ending cash flow	**16,390**	**8,888**	**10,162**	**12,412**	**14,323**

--Profitability Margins	2021A	2022A	2023E	2024F	2025F
EBITDA margin	30.4%	22.9%	17.0%	18.6%	19.0%
PBT margin	33.5%	23.3%	19.8%	21.4%	21.8%
Core PAT margin	31.8%	21.8%	19.0%	20.7%	21.1%

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 *rise* 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 *fall* 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