Quarter Ended 30 September 2013 PETRONAS Chemicals Group Bhd Earnings Presentation
Event Date: 8 November 2013, 5.00pm

Nor Shahda Zakaria (Head of IR):

Hi, good afternoon everyone. I'm Shahda. Welcome to PETRONAS Chemicals Group Berhad's quarterly briefing for the financial result ended September 2013.

With us today are Dr. Abd Hapiz, President and CEO; Wan Shamilah, CFO; Shah, Head of the Fertiliser and Methanol segment; and Herman Schrijver, Head of Operational Excellence and Health, Safety and Environment.

We will begin the session with a presentation and followed by a Q&A session. This analyst briefing is accessible via conference call or webcast which is available on our corporate website, www.petronaschemicals.com. Likewise, the presentation slides are also available for download from the webcast window or directly from the PCG website.

Before we start, please read through the disclaimer statement in the briefing pack.

Thank you. I will now hand over to Dr. Hapiz.

Dr. Abdul Hapiz Abdullah (President/CEO):

Thank you, Shahda. Ladies and gentlemen, good afternoon and thank you for joining us today.

The global economy registered positive improvement in Quarter 3. Based on recent economic data, markets in US, Europe and China are improving. Overall for us, O&D prices are firm in line with the market, driven by healthier demand amidst supply limitations within the region.

The fertiliser and methanol market however was mixed, with urea prices pressured due to ample supply in a soft market.

During the quarter we undertook maintenance activities at our main cracker and related downstream facilities. For your information, this is our first cracker turnaround since our listing 3 years ago. With lower volume, the Group's financial results for the quarter therefore declined.

At this juncture, I will hand over the session to Wan Shamilah, our Chief Financial Officer, to provide details on PCG's financial performance for the quarter.

Over to you, Shamilah.

Wan Shamilah Saidi (CFO):

Thank you, Dr. Hapiz. Good afternoon, everyone. I have the pleasure of presenting to you the results for our Quarter 3. Can I please take you to slide number 5. Generally, as mentioned by Dr. Hapiz, during the quarter, we undertook maintenance work which was heavier than usual. It involved our main cracker that has 60% of our total cracker capacity as well as its related downstream facilities.

Accordingly, therefore, our production and sales volume were lower, and hence, similarly, financial performance. Overall, for the 9 months period comparatively, it was slightly better.

If I can take you to the next page and take you through more details; revenue for the quarter compared to the quarter last year, was lower by 10% as a result of the lower sales volume. Correspondingly, operating profit was lower by 15%. On the front of our associates, the contribution was higher with improved market conditions for their products.

Overall at the Group level, profit before tax was lower by 10% and our EBITDA was lower by MYR1 billion with 29% EBITDA margin. This is mainly as a result of the maintenance work at our cracker and its related facility. Basically, it took away the benefit of the volume from our ethane-based products.

When you compare against preceding quarter, revenue was lower by 9% for the similar reason of lower sales volume, and you can observe the same trend for operating profit, profit before tax and EBITDA.

Over to the next slide, on our operational performance. The trend is lower compared to preceding and corresponding. We recorded at the Group level, 69% plant utilisation rate due to the heavy maintenance work that we undertook during the quarter, and that correspondingly, led to the lower revenue as well as lower EBITDA margin that you see at the Group level.

By segment, you see the same pattern for Olefins and Derivatives (O&D). It achieved plant utilisation rates of 77.6%, affected by the activities undertaken at the main cracker as well as the four related downstream facilities. Product prices for O&D was better compared to corresponding quarter, and ~~it~~ was comparable against preceding. The revenue overall was lower by 9% against corresponding and by 4% compared to preceding mainly due to the lower sales volume. EBITDA margin for O&D hence, is at the lowest you've seen because of the effect of less volume from our ethane-based value chain.

For Fertiliser and Methanol (F & M); it also recorded lower plant utilisation rate level compared to preceding quarter at 63.2%. Mainly during the quarter, there were maintenance activities undertaken at our methanol facility due to technical issues. On the supply side, we do not face issue with gas supply situations.

Product prices for F&M were lower by 12% against corresponding and 8% against preceding, mainly driven by lower urea prices, which Shah will elaborate further later. But with the export tax window from China, the additional capacity in the market as well as softer demand, we see significant reduction in urea prices, which in our view had bottomed, so going forward it should stabilise.

Hence, overall, for the F&M segment, sales volume was lower, but during the quarter we also undertook less product purchases. So, as a result we, in terms of profit, we did not face as much reduction compared to revenue. EBITDA was at 31%.

Moving on to cash flow, I'll go very quickly here because there's not much to highlight since the situation is similar. Our cash flow remained strong. We do not have any gearing. So as at end of the quarter our cash stands at MYR10.6 billion.

With that overview, I will handover to Dr. Hapiz to cover Olefins and Derivatives segment.

Dr. Abdul Hapiz Abdullah (President/CEO):

Thank you, Shamilah. As mentioned, I will cover the Olefins and Derivatives segment of our business. In general, our key O&D products prices strengthened throughout Quarter 3, gaining from strong naphtha prices and improved market sentiments. Specifically for ethylene, prices started to improve from mid-August due to supply constraint resulting from heavy turnaround season for regional crackers including our own cracker.

Moving forward, ethylene prices are expected to remain stable overall. It will soften slightly towards the end of the year with new capacities from China and Taiwan coming up.

For the polymer business, prices were on an uptrend for most of Quarter 3 due to severe supply constraint following plant outages in the region. LDPE prices specifically, reached high levels of $1,600 by end of September. This limited supply situation is expected to continue for most of Quarter 4. Hence, price is expected to continue to be firm. However, bear in mind that demand usually taper off end of the year as buyers opt to draw from their own inventories.

MEG prices improved in Quarter 3, supported by higher ethylene prices and firmer demand from downstream polyester markets. In addition, demand was also supported by restocking activities ahead of the two major Chinese holidays in September and October. Prices are anticipated to soften in Quarter 4, in line with seasonal lower demand at year-end from polyester markets.

Aromatics prices remained firm in Quarter 3, supported by naphtha prices. Aromatic prices are expected to stabilise in the next quarter as the supply and demand fundamentals are expected to be balanced.

That's the short brief on O&D. Let me pass you to Shah, Head of Fertiliser and Methanol.

Muhammad Shah Bin Ali (Head of Fertilisers & Methanol Business):

Thank you, Dr. Hapiz. Good evening everyone. Let's start with an update for urea. Firstly, we saw a huge downward impact on Quarter 3 urea prices created by the opening of the China export window. That was also mentioned by Shamilah just now.

We saw an additional 6.6 million tonnes flooding the market. In addition, we also saw the additional supply out of Fertil and Sorfert new capacities amidst lackluster demand from unfavorable weather conditions. At the start of Quarter 4, we've seen some potential price recovery mainly from the upcoming Indian tenders. Total of 4.5 million tonnes have been purchased to date, and these buyers are foreseen to step in again for another 1.5 million tonnes to 2.5 million tonnes.

With one of the Iranian urea plant being down, as well as the closing of the China low export tax window, India will be left with no choice but to source the remaining tonnage from the market possibly at a much higher price. The Yuzhny urea producers have been shutting down their plants following the current sluggish market sentiment. We expect these plants to remain idle going into winter.

Meanwhile in the US, buyers have played the wait-and-see game for too long and now we expect them to rush to secure their fall and winter planting season requirements. This potentially will be pushing the October and potentially November, Middle East prices. Urea prices will experience a spike towards mid-November before the market goes quiet again due to the holidays and low planting season towards the end of Quarter 4.

Moving on to ammonia, the market has been pretty quiet with slow demand that was seen from both fertilisers and industrial buyers. Quarter 3 prices in Southeast Asia have been stable, supported by supply shortages with the planned shutdowns that we are seeing at our plant~~s~~ as well as in KPI in Indonesia respectively. KPI is expected to resume operations only when prices hit mid $500 levels.

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Again, all eyes are on India as demand is slowly recovering in region going into Quarter 4. However, this ammonia supply shortages is expected to be offset by poor urea and DAP market conditions, and also coupled with weakening caprolactam and acrylonitrile prices, hence we expect the ammonia market moving sideways towards year-end.

Lastly, methanol; in Quarter 3, methanol prices soared as a result of tight supply from plant outages, mainly from PC Methanol and Brunei Methanol. The supply continues to be tight going into Quarter 4, with additional 45 days shutdown expected in Kaltim Methanol Indonesia starting November.

At the same time, the Middle East producers are diverting their cargos into Europe to capture the high netbacks in that region. Looks like for the time being, only the biodiesel producers can afford the high methanol prices.

Situation in China - buyers are currently surviving on limited domestic supply amidst the escalating prices as low coal prices are favourable for them to increase production. Coal prices were around $90 in August and falling further in September and October. Therefore, we expect prices for remaining Quarter 4 to sustain at above $450 levels, CFR, going into November and December.

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That's all from F&M. Thanks for your kind attention. Back to you, Hapiz.

Dr. Abdul Hapiz Abdullah (President/CEO):

Okay, ladies and gentlemen, that's the end of our presentation. Overall, we achieved good results for the 9 months of the year supported by the strong first quarter. Enhancing operational excellence will remain our key imperative going forward. We are confident that our efforts towards operational excellence would position the Group to leverage on opportunities within the growing petrochemical market. We now open the floor for question and answers. Thank you very much.

Question and Answer Session

Horace Chan – Citi – Analyst

I have two questions. The first one is on methanol number two plant. What is the exact problem with the plant, and is it a mechanical issue or is it utility related (water issue like a few years ago)?

And the second question is on the gas supply contract on Project SAMUR. Has it been finalised? And how long would the contract be? Could you talk a little bit on the contract detail; is it going to be profit sharing or is it going to be linked to oil price?

Thanks very much.

Wan Shamilah Saidi (CFO):

Okay, there are two questions. The first is on the methanol technical issues that we had to attend to during the quarter. Its usual operational issues that we face. Because of our operating philosophy, we take the approach that we will rectify it, because our priority is for long-term sustainability.

The issue is partly also related to gas quality issues that we had faced that led to certain equipment concerns. But that has now been identified and addressed. But for methanol, we would also like to share that; synchronized with the upstream facility, there will be further shutdowns undertaken. In fact, it's already being undertaken now. It will be shut down until the end of the year. But next year, it looks encouraging because the gas supply is now stable and we have done a lot of maintenance activity this year. So, it will be better performance in 2014.

On the second question about gas supply contract, we have concluded a 20-year gas supply contract with PETRONAS. It has similar structure to our other fertiliser and methanol supply contract because this is a segment that buys methane as the feedstock. So it is of similar structure. It is usual when we build a new plant, the contract is for 20 years; to ensure that we are able to achieve the threshold target return from such a project, and that requires certainty in gas supply. So that is in place.

Mayank Maheswari – Morgan Stanley – Analyst

I have three questions. Firstly, a broader question regarding how PETRONAS Chemicals think about the impact coming in from the government's overall plan of rationalising subsidies on gas in Malaysia, and what do you think would be the longer term impact on PETRONAS Chemicals, positive or negative?

My second question is regarding the olefins plant. Can you give us a status update on the plant utilisation rates now, in which you had shut in the third quarter and what's the outlook on utilisation for next year?

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And the third and the final question is regarding SAMUR and on aroma complex with BASF. Can you give us some updates on what's happening in terms of project progress? Thank you.

Wan Shamilah Saidi (CFO):

Okay. On the first question about gas subsidy, we purchase our feedstock based on long-term contracts. So, the gas that we purchase, that is at regulated gas pricing, is actually not a big amount. It's roughly approximately about 1 million mmBtu in volume per month. So, if there are any increase in regulated gas pricing, we will also see cost increase~~s~~ for methane that we purchase.

Our other purchases of ethane, propane, butane and methane, these are via long-term contracts, which has its own pricing formula that is generally, apart from ethane, linked to market references.

On olefins plants, this is the cracker that underwent maintenance, we like to highlight that the maintenance activity that commenced early September, it's still ongoing. We expect it to be back on stream by middle of November. It is extended, compared to our plan, due to execution challenges that we are now managing and we expect it to be up by middle of the month.

On aroma complex or the project to venture into aroma project downstream at our site in Kuantan; that is progressing well. And we are targeting BASF PETRONAS Chemicals to reach final investment decision by end of the year in December.

For SAMUR, it is also progressing. To date, we have incurred just under 45% CAPEX year-to-date. So it is on track for commissioning in 2015.

Mayank Maheswari – Morgan Stanley – Analyst

On Project SAMUR, you did mention that it's a similar structure like it was for your current plants. But have you seen any increase or reduction in discounts that you used to get methane on back of this, or is the range similar for Project SAMUR as well?

Wan Shamilah Saidi (CFO):

The gas supply contracts that we have for Fertiliser and Methanol segments are consistent between the companies as well as SAMUR. It's similar structure.

Yong Liang Por – BNP Paribas – Analyst

If I may just ask, thanks for the explanation on the methanol, the Mega Methanol plant issues, could you please give us a little bit more detail on exactly what happened? I mean, you mentioned that the gas quality was poor. Was it high sulfur? Did it corrode some equipment? And just generally I just seem to remember this plant constantly experiencing issues. What assurances can we have that next year's utilisation rates will be much smoother? Thank you.

Wan Shamilah Saidi (CFO):

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Well, certainly for PC Methanol, we have undertaken a lot of work in 2013. As we have said earlier, we are at the moment, not producing from the new Mega Methanol plant. It will be undergoing maintenance until the end of the year. So, it is ~~a~~ significant ~~asset and~~ investment that we are taking in 2013, to address all the technical issues that we're facing. please check.

We are not able to go into detail about what the nature of the issues are, but again, the outlook for 2014 is, given the amount of work that we have opted to do in 2013, we will be in a better shape next year.

Trevor Buchinski - Macquarie – Analyst

I'm just wondering, given the operational challenges that you are guiding for in the fourth quarter, are you able to offer any firm number in terms of expected utilisation? Both on the olefins and the methanol and fertiliser side and on the Group level as well? That's my question, thanks.

Wan Shamilah Saidi (CFO):

For the full year, we don't give forecast numbers. But I think we will be below our target of 90%, certainly. We see similar levels of shutdown in the last two quarters of the year. But, once our cracker is back on stream, we should be able to recover our performance. But, for the full year, we do not give forecast numbers, but we can guide that, certainly, it will be lower than our stated target. I'm sure that's not a surprise, but Quarter 4 will be at a higher level than Quarter 3.

Samuel Lee - JP Morgan – Analyst

Can I just get a clarification on the operations of the number two Mega Methanol plant? So, this plant will be out of production until the end of the year, is that correct? Thank you very much.

Wan Shamilah Saidi (CFO):

Yes, that's correct.

Mayank Maheswari – Morgan Stanley – Analyst

Ma'am, have you seen any improvement on the gas supply side of things on East Malaysia and West Malaysia as such? And the other thing is, obviously you are seeing some delays on RAPID. So are you looking at alternative use of cash as well (which is about a good $3.5 million odd on your balance sheet)? Thank you.

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Wan Shamilah Saidi (CFO):

The gas supply situation for East Malaysia, specifically, for our methanol plant, is better. It has been steadily better. So what's important to us now is to make sure that plant running rate would be optimised next year, but supply side is good.

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Delays in RAPID, yes, PETRONAS has shared some rephasing of when they're going to reach FID. ~~It's~~ now scheduled to be by the end of Quarter 1, 2014.

As you are aware, Project RAPID is one of our key strategies that we are pursuing, and we remain focused on Project RAPID.

Trevor Buchinski - Macquarie – Analyst

Yes, just a follow-up. Any updates on divestments that you are pursuing? And if so, any indication as to what sort of gains you might realise that is associated with that? Thanks very much.

Wan Shamilah Saidi (CFO):

We shared on the 6th of November, that we have signed SPA to divest PMPC to Asahi Glass and Mitsubishi. Of course it is customary there are conditions precedent that need to be met by both parties, including regulatory approval. So we expect, and we hope that we will close or meet all the condition precedent by quarter 2, 2014. Unfortunately, we are not able to give you any guidance on any gains or otherwise, because we are not disclosing the purchase consideration at this stage.

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Chong Mun Wei - Employees Provident Fund – Analyst

I'm sorry, I joined in late. So I'm not sure if you have given any guidance for plant maintenance in 2014.

Wan Shamilah Saidi (CFO):

No, we have not. If we could just share with you the main activity. The main activity next year involves our smaller cracker, and that is scheduled to take place in Quarter 2 of 2014. And this would be the smaller cracker that has 40% of capacity and is related downstream plants as well. So, that is the main activity next year.

Chong Mun Wei - Employees Provident Fund – Analyst

This is the 400,000 ethane cracker, right? And what are the related plants on the downstream side?

Wan Shamilah Saidi (CFO):

Yes, correct. It will be the polyethylene plant. This is the smaller chain compared to the olefins cracker that we undertook this year.

Chong Mun Wei - Employees Provident Fund – Analyst

What is the capacity of the polyethylene plant that will be shut down together?

Dr. Abdul Hapiz Abdullah (President/CEO):

250,000 tonnes.

Julia Nelson - RHB Research – Analyst

Actually I would like to refer to a newspaper article by Wall Street Journal highlighting the possibility of refining capacity expansion in Vietnam. So, I was wondering whether the management has any opinion on that. Thank you.

Dr. Abdul Hapiz Abdullah (President/CEO):

PETRONAS does not have any plans on any refining operations in Vietnam. Our only refining operation that we are targeting right now is RAPID Project, and that will take place with an FID, hopefully in first quarter of next year.

Julia Nelson - RHB Research – Analyst

Yes, but just revisiting the article, because Vietnam is expected to come out with huge capacity expansion by 2017 and is expected to be at about well over 1 million barrels per day. So, do you have any thoughts there? Whether it will affect RAPID Project, or is it not?

Dr. Abdul Hapiz Abdullah (President/CEO):

We are of the opinion that it will not affect our RAPID Project. We are still on a go-mode on RAPID. Again, RAPID decision will come in on the first quarter of next year, whether or not we go ahead with the RAPID project.

Wan Shamilah Saidi (CFO):

And we can't comment on other projects.

Chong Mun Wei - Employees Provident Fund – Analyst

Sorry, I forgot to ask just now. How long would the shutdown of the ethylene cracker in second quarter be?

Wan Shamilah Saidi (CFO):

It will be about 2 months.

Chong Mun Wei - Employees Provident Fund – Analyst

Okay, how about on the fertiliser and methanol side, will there be any shutdown? For how many days?

Wan Shamilah Saidi (CFO):

It will not be involving the plant number two. There are no shutdowns at our major facility, only plant number one, and that will also happen in quarter 2.

Usually, we don't provide detailed days, it ranges from 30 to 60 days. But, this is a smaller facility. So next year, no planned activity for our Mega Methanol plant.

Chong Mun Wei - Employees Provident Fund – Analyst

Just one more question. The discontinuation of your vinyl chain in Kertih, what is the progress on the usage of the land there?

Dr. Abdul Hapiz Abdullah (President/CEO):

I think right now we are in the process of decommissioning and that is going as per plan. And the decommissioning process will take a while. And we will only address the issues later, once we finish the decommissioning element.

Nor Shahda Zakaria (Head of IR):

All right. Since there are no more question, we have come to the end of our briefing. We thank you for your participation. The recording of this webcast will be made available on our website at the end of the day. Thank you very much and good evening.

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