Quarter Ended 31 March 2012 PETRONAS Chemicals Group Bhd Earnings Presentation

Event Date: 29 May 2012, 5.00pm

Wan Asmah Che Din:

Good evening, everyone. My name is Wan Asmah from Investor Relations. I would like to welcome everyone joining us for the PETRONAS Chemicals Group financial highlights briefing for the quarter ended March 31, for the financial year 2012. With us today is Dr. Abd Hapiz, the President and CEO; and Miss Wan Shamilah Saidi, the CFO.

If you have yet to download today's presentation, please visit www.petronaschemicals.com. If you are joining us on the webcast, please look for the download link to the presentation on the webcast window. Before we start, please read through the disclaimer statements in the briefing pack.

Over to you, Dr. Hapiz.

Abd Hapiz:

Thank you, Wan Asmah. And thank you to all of you for joining us today. It is with great pleasure for us to share with you all today our results for the quarter 1, ended March 31, 2012.

We had a good start to the financial year 2012 and certainly a good quarter. We achieved revenue of MYR4.4 billion and with EBITDA of MYR1.6 billion.

There are four key highlights that I'd like to share with all of you. One is the improved plant performance. Both of the Group's business segments attained higher plant utilisation in the first quarter.

Secondly is on the supply of methanol to plants improved. We saw a recovery in the supply of feedstock to our methanol plant in Labuan.

Thirdly we, however, had challenging market environment with demand softening and global economic events further pressuring our regional markets.

And the fourth highlight is on Project SAMUR. It is progressing very well.

These are the four key highlights that I'd like to highlight to all of you.

With that, let me now hand it over to our CFO, Wan Shamilah, to provide details on our financial performance.

Wan Shamilah Saidi:
Good afternoon, everybody. Thank you, Dr. Hapiz. Allow me to present the financial highlights for the current quarter.

Before I start, can I also highlight that we have now adopted the Malaysian Financial Reporting Standards, which is in line with International Financial Reporting Standards. The date of implementation was January 1, 2012, with the transition date on the beginning of the preceding financial year, which is April 1, 2011. So please bear that in mind.

So let me go through the results against corresponding quarter. Our revenue grew slightly by 1%. The marginal increase with comparable sales volume and prices compared to corresponding quarter.

We did see improved operational performance which can be seen in higher plant utilisation rates. But in the corresponding quarter, due to lower production, we also undertook trading activities to mitigate system shortfall to meet our commitment to customers. So when we look and compare sales volume, it's only marginally different, although we saw improved level of plant performance in the current quarter.

Our operating profit stands at MYR1.4 billion, an increase of 15%. Contribution from our associates and jointly-controlled entities saw a drop of 56% or MYR92 million. This is following lower production level, as well as with one of our associate companies, is now facing higher effective tax rate following full utilisation of the tax benefits in the quarter ending December 2010.

EBITDA is strong at MYR1.6 billion with EBITDA margin at 37%.

Compared to preceding quarter, with the improved plant performance, despite slight weakening in prices, we saw our revenue increasing by 12% at MYR4.4 billion, compared to MYR3.9 billion.

Our contribution from associates and jointly-controlled entities saw an improvement by 33%. So overall, our profit grew by 22% and our EBITDA grew by 18%, with EBITDA margin being slightly higher by 2%.

Moving on, let me give you a bit more detail on Group performance. Our plant utilisation rate, as you can see, is just shy by 0.2% compared to our target of 90%. The plant performed well this quarter. We achieved 89.8%, which is higher compared to both corresponding and preceding period.

In the corresponding quarter, we did see high-level plant maintenance but a lot less in the current quarter; similar pattern against preceding quarter.

So as a result, I already explained about revenue, why it's at par, although with improved plant performance. Against preceding quarter, revenue grew by nearly MYR0.5 billion or 12% and our EBITDA grew by MYR250 million or 18%.

Segmental performance, you can see a nice trend for our Olefins & Derivatives segment. Continuous improvement in our plant utilisation rates, with very strong performance at 95.2% in the current quarter for our Olefins & Derivatives segment.

This is mainly the reason why trading activities in the corresponding period to mitigate system shortfall was undertaken. That's why you again see plateau in terms of revenue, but against corresponding, it grew by MYR300 million or 11%.

EBITDA margin was steadily strong at 36%.

For the Fertilisers & Methanol segment, we had challenges in our gas supply to our Labuan facility, and this quarter we saw improving levels of plant performance at 85.2%. And with that, stronger level of revenue at MYR1.2 billion and a very strong EBITDA margin at 42%, the strongest we have seen so far.

Moving on to our cash position; cash position stood at MYR9.7 billion as at March 31, 2012. One key highlight, you do see a reduction in cash flows generated from operating activities. That's due to the timing of sales only. We did see lower levels of sales in the month of December and January, therefore, less settlement of those sales during the current quarter. So no issue there, it's just simply driven by the timing of the sales conducted.

We're also pleased to share, on the next page, our cost optimisation target. If you recall, when we went for listing, we also shared a target with the market that we have a KPI or a target of achieving MYR130 million cost optimisation by March 31, 2012. So, we are presenting to you our results up to March 31, 2012.

Our cost optimisation activities or efforts are mainly in three broad categories. Let me start from the bottom first. Basically, under the unified management of PCG, we have undertaken a lot of centralisation.

The purpose of the centralisation is to have more efficient use of resources, as well as raising the level of performance in specific areas. So, the areas where we saw a lot of value being generated is in the areas of centralised procurement and services, as well as centralised logistics. We now have a dedicated unit that manages all the procurement activities and all the logistic activities for the Group.

We have achieved cost optimisation through undertaking simple efforts such as in the areas of logistics, for example, we can optimise our costs by optimising the routes. So where possible, if we can co-load to multiple locations or co-load products where it's feasible, then we can achieve reduction in our transportation costs.

Negotiation of contracts, we have many facilities within our stable. Prior to unified management, they undertook the negotiation of each contract separately, but under the unified management, we conduct the negotiations as one Group. Therefore, through economies of scale, as well as centralised negotiation, we do see reducing rates in our contracts.

A simple example would be something that I've also shared before previously, in scaffolding rates, where some of our operating units see even up to 50% reduction in the scaffolding rates in the master agreement for scaffolding for the Group.

So they're not difficult to do, it just needs some focus and centralisation of resources and management.

In terms of process and value chain optimisation, this is simply looking at the various practices across the Group, and sharing of best practices and enhancing the focus in certain areas to reduce wastages and improve the usage of energy that brings about a lower cost of production. So this is simply enhancing/optimising the level of spending through sharing of best practices across the Group.

So, as a result, we have recorded a modest achievement of MYR159.5 million as at March 31, 2012. But this is actually just the beginning. There's a lot more that we can do and the area where we feel we can achieve higher levels of optimisation would be in the way we manage the value chain as one value chain.

We now, for example, have a unified management of the ethylene grid, so that enables us to optimise the flow of ethylene to our various customers. When we have excess, we will be able to optimise and maximize our ability to export given the limitations of our infrastructure.

We also have another example, unified management of the ethane buffer tank. Currently, we only have an ethane buffer tank at our OPTIMAL facility. So in periods where you see some reduction in daily flow of ethane, we are able to optimise our older cracker of PETRONAS Chemicals Ethylene, where direct flow of ethane is received first, so that we optimise the usage of the ethane buffer tank as well.

So those are just two simple examples of what we are doing now under unified management to optimise our ability to produce and generate revenue.

This is over and above the number that we shared or that you see on the slide of MYR159 million; over and above, improving our ability to generate revenue.

Other areas where we are focusing on to improve, is our ability to execute or operate the plant in the areas of turnaround management. For the first time this year, we have completed a catalyst change-out during the current quarter and that was completed on time; first time conducted by the centralised turnaround team.

Next year, when we undertake the turnaround of one of our crackers, it will be the first time that they'll be doing a major shutdown or turnaround. So we hope to see a lot of value in more effective execution of turnaround, whereby we can reduce, hopefully, the number of days and again, that will increase our ability to generate or produce revenue.

With that, I end my presentation and I hand over back to Dr. Hapiz.

Abd Hapiz:
Thank you, Wan Shamilah. Ladies and gentlemen, as I highlighted earlier from the beginning, we have certainly shown a lot of improvement in our plant performance; addressed the supply of methanol to our plants in Labuan; meeting of challenges in the markets; and also, making good progress with our projects like SAMUR.

Moving forward, we remain cautiously optimistic on our markets which are mainly those in Asia Pacific.

There are challenges, no doubt, in the near term and uncertainties remain. Our belief is the usual seasonal demand in the second half of the year may lend support to the demand and prices going forward.

Amidst all these external challenges within the market, we in PCG, will strive to achieve operational excellence, maintain our plant utilisation rates and by doing this safely.

To that, ladies and gentlemen, I say thank you and we are open for questions.

<u>Question and Answer Session</u>

Alex Goh, AmResearch:
I just want to ask on the supply of gas for Olefins as well as for Fertilisers & Methanol. Wan Shamilah, you mentioned that there were trading activities to replace some shortfall. But if you don't include these trading activities, how much would the system shortfall be? That's my first question.

And on the Fertilizers & Methanol division, is the supply of methane to the Labuan plant sustainable?

Wan Shamilah Saidi:
For the supply of methane gas to our Labuan facility, we certainly see an improvement in the flow rate which has assisted our level of or our ability to produce and operate the plant.

We are actually quite encouraged by the progress of the efforts undertaken by upstream partners. They are certainly dedicating a lot of resources to ensure that we get sufficient supply of gas.

So we are encouraged by what we see so far and we are seeing continuous improvements.

The first question, let me clarify, the trading activities was actually undertaken in corresponding quarter; quarter ending March 2011. And, if you recall, during that period, our utilisation rate was lower compared to current quarter.

So it was not related to gas supply issues, it was driven by our plant utilisation rate. In the corresponding quarter, it was only 83.6%.

Mayank Maheshwari, Morgan Stanley:
The first question is, now that you are seeing a good strong EBITDA margin on the Fertiliser division consistently for more than two to three quarters, is there any discussions with the parent, PETRONAS, on anything regarding gas-price change formula like we saw it in 2008? So that's my first question.

And the second one is, can you give us some guidance of what you are hearing from the upstream side in terms of gas supplies for 2012?

Wan Shamilah Saidi:
Answering your first question, currently there are no discussions. On your second question, can you please clarify, if you don't mind?

Mayank Maheshwari, Morgan Stanley:
The second question is regarding what you're hearing from the upstream side, in terms of gas supplies. Are you seeing any major turnarounds that they're taking throughout this year, or that's now kind of behind us?

Wan Shamilah Saidi:
We saw heavy maintenance upstream in year 2011. So far as you can see, even in this quarter, we do not see challenges in that area, Mayank.

Mayank Maheshwari, Morgan Stanley:
So you are not hearing anything more for the entire 2012 currently from the upstream side?

Wan Shamilah Saidi:

Currently that is not a constraint to our performance.

John Chung, UBS:

First of all, from your financial report, Q1 financial statements, you mentioned that the revenue increased by about 12% quarter on quarter and that was mainly driven by the sales volume growth of 23%, and the average product price actually declined by 6%.

I was just wondering, back in Q1, obviously, oil price was rising, a lot of chemical prices were moving up. Why was the average selling price down on a quarter-on-quarter basis? Was it because of the increasing utilisation rate of the fertilizer plants, hence the overall ASP was slightly down?

Second question is regarding the utilisation rate. Obviously, Q1 was terrific; we see very good utilisation rates for both Olefins and Fertilizers. Just a question on the scheduled maintenance, how much was it down in Q1 and do you have any that's currently undergoing or do you plan to do any more in the second quarter?

Wan Shamilah Saidi:

John, before I take your questions, I just want to clarify Mayank's question earlier about the gas supply situation for 2012.

I clarified just now that we are not constrained by level of supply, but for methanol, the trend for our facility in Labuan is still improving, but subject to sufficient availability of gas with our facility, there might still be some challenges there. But we are seeing improving trends.

Coming to John Chung's question now, revenue combined QoQ, i.e., the current quarter against quarter ending December; we did see some declining trends during the current quarter for prices of our Fertiliser & Methanol business segment. So I hope that answers your question.

We did see Olefins & Derivatives improving, which is in line with the market.

On the maintenance, previously we have shared that for the current year; our maintenance plan is for all our facilities in Fertiliser & Methanol, as well as a catalysts change-out activity at our OPTIMAL facility.

The catalyst change-out activity has been completed. That was undertaken actually in the current month, the month of May, and we have also undertaken maintenance work at our ethylene facility of PETRONAS Chemicals Ethylene.

If you recall in our previous analyst briefing, we shared that it suffered power interruptions during October 2011 and we did share that we are doing assessments. If we need to do some rectification work arising from that power interruption, which led to abrupt shutdown, we will do so.

And we are pleased to share that we have already undertaken that activity and was completed only recently; so that is already work completed as well. And our ethylene cracker was, therefore, out of operation in the month of May for about three weeks or so.

Going forward, the remaining maintenance work that we are scheduling for, is our fertilizer facility in both Bintulu and Kedah and also a small maintenance work that we have to undertake for our vinyl chloride facility.

So that's the remaining maintenance work left for us to undertake for the rest of the year.

John Chung, UBS:

May I just clarify on the first one? You said the fertiliser price was weaker in Q1, but Olefins and Derivatives were actually stronger?

Wan Shamilah Saidi:

Yes, correct. Both Fertiliser and Methanol prices on average were lower.

John Chung, UBS:

Regarding the second question, so basically, it sounds like second quarter, we're going to have more maintenance activities versus Q1, is that correct?

Wan Shamilah Saidi:

Correct, but we are sharing with you that we have already completed the work. The facilities affected were down for about three weeks. The significant ones were about three weeks of maintenance work undertaken at our ethylene cracker, PETRONAS Chemicals Ethylene, and also catalyst change-out that we undertook at our OPTIMAL facilities.

So that will certainly have an impact on our quarter 2 results. But the work is done and completed, and we were on track.

John Chung, UBS:

We saw a lot of the crackers where petrochem producers in Northeast Asia cutting down the run rates because the margins have been bad and demand has been weak.

I just wondered if you are seeing the same situation. Are you seeing weakening demand? Do you plan to lower utilisation rates, to avoid rising inventories?

Wan Shamilah Saidi:

We expect challenging market conditions. We still maintain our plant utilisation rate of 90%, but what we'll do is actually manage the value chain.

We have that flexibility under the unified management of PCG; that we are able to really manage the molecule and direct it where we see the higher margin, given the kind of market situation. So that's what we'll do differently. Our target utilisation rate remains.

John Chung, UBS:

Can you be more specific on how you try to do it? What's the value chain management, how do you do that?

Wan Shamilah Saidi:

We have various products that we produce from the downstream facilities, and we can direct more molecules into certain facilities versus another, depending on the level of margins.

Mayank Maheshwari, Morgan Stanley:

On BASF PETRONAS, any updates in terms of improved utilisations or any updates in terms of how the operations there are doing? That will be useful. Thank you.

Wan Shamilah Saidi:

BASF PETRONAS Chemicals, I think the main concern rather than utilisation rates is really about market conditions.

In terms of plant-performance, it is improving trends compared to preceding quarter. But I think the market conditions, similar to other players, will be the challenge, rather than production levels of the plants.

Mayank Maheshwari, Morgan Stanley:

Just to clarify, you have seen some improvement on utilisation there?

Wan Shamilah Saidi:

Well, certainly, in the current quarter, we do see a higher level of production compared to the preceding quarter.

Mayank Maheshwari, Morgan Stanley:

And how is the situation there currently?

Wan Shamilah Saidi:

It's certainly better than preceding quarter. As I shared earlier, Mayank, it's more about the market conditions.

I shared earlier about maintenance work that we are planning, I'd like to also share that in the current quarter, our methanol facility is also undergoing maintenance work. But it should be up in early June.

Mayank Maheshwari, Morgan Stanley:
One question that I had in my mind was on Project RAPID and Project SAMUR. Can you give us any updates of what's the progress, and what can we expect in 2012 on both fronts?

Abd Hapiz:
For Project SAMUR, it is progressing well, as I mentioned earlier. We had our groundbreaking ceremony back in February this year, and it looks like things are on track for us to have the plant ready by early 2015; making good progress there.

With regards to RAPID, as you are aware, it's a project undertaken by PETRONAS, not PCG. Obviously, we will be looking at the viability of that, once the work has been done, and that's been planned sometime next year.

There are a couple of things to highlight on RAPID. One is that we had the groundbreaking ceremony, just 2 weeks ago on 13th May, and that went well with all the necessary participations.

They have also signed two sets of heads of agreement. One is with BASF, on the specialty chemical side. And also signed two other heads of agreement; one is with ITOCHU, and the third one is with PTT Global Chemicals.

So RAPID is also moving quite well, rather smoothly and on track, as for what we have committed to do. And all are ready for, as per committed, to start up in the 2016/17 timeframe.

Wan Shamilah Saidi:
But it's still at early days of the project.

Abd Hapiz:

Yes, early days, right.

Gerald Ambrose, Aberdeen Asset Management:

Most of my question was answered in the previous questions, but I just wondered, on the timing, you're getting pleasantly close to MYR10 billion worth of cash. And I think between now and 2015, your total investment in SAMUR will be about MYR4.7 billion. It leaves quite a bit, and your cash flow is still very positive, operationally.

I'm just asking if you know really how much you intend to spend in RAPID, but I think from the earlier question, you're not sure yet?

Abd Hapiz:

The answer is yes, we're not sure yet.

Wan Shamilah Saidi:

I think the indications that we have shared previously, and we're giving that guidance for now, is that for RAPID, ballpark potentially half of the $20 billion that PETRONAS has indicated for RAPID. Half of it will be related to the petrochemical portion of RAPID. So if PCG is to undertake the petrochemical portion, that's what we will be facing.

Por Yong Liang, BNP Paribas:

I just have a question on selling and distribution expenses. It seems to have gone up quite a bit again in this quarter. Can you guide us on whether this level going to carry through for the rest of the year? And also, what is the reason for the increase?

Wan Shamilah Saidi:

Our selling and distribution expense for the quarter increased generally, that's in line with our volumes that we have produced. There's no extraordinary trend here, so these are normal.

Por Yong Liang, BNP Paribas:

What I mean is that, let's say, revenue in quarter 1 was MYR4.4 billion and the expense was MYR183 million. And if you look at the equivalent quarter, which was January to March 2011, it was the same revenue, but expenses was only MYR108 million. So it's gone up quite a fair bit.

So I was wondering, obviously, your cost optimisation has brought down costs quite a bit, but I'm just wondering why it's not showing up here, or maybe it's showing up elsewhere?

Wan Shamilah Saidi:

The cost optimization that I shared earlier, when we compute, we are comparing to prevailing rates. So when we, for example, enter into term contracts, what we have managed to contract for, are compared to prevailing rates. So the example I gave you about co-loading, it's the savings that we can achieve if we do two separate trips using two separate vessels, compared to if we co-load into one and only incur one.

So freight rate also has its own market movements, you need to bear in mind that where we shared the cost optimization numbers earlier, it's compared to the prevailing rate and how we do our transportation contracts, to make sure we are incurring it at the most optimum level to meet business requirements, compared to prevailing rates.

So, again, as I shared earlier, there are no abnormal trend in our selling and distribution expenses and all in line with the volume and the type of products that we undertake.

THE END