

Borouge Plc

Lower selling price impacted profit despite high sales volume and decline in cost

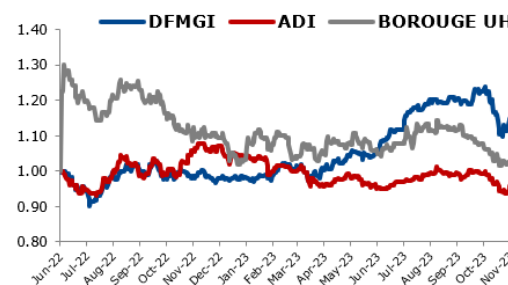
Current Price
AED 2.58

Target Price
AED 2.95

Upside/Downside (%)
+14.2%

Rating
ACCUMULATE

- The value enhancement program benefited the EBITDA with USD 420 Mn impact in 9M23. This will be split between 70/30 between cost efficiency and revenue enhancement. The Company surpassed the target of USD 400 Mn and further raised it to USD 500 Mn for the year 2023
- Utilization of PE and PP stood at 104% and 109% in 3Q23 while the OCU plant was utilized at 109%
- Borouge plans regular turnaround of Borouge 3 plant and feedstock-related operations in 2024 which will impact production volume by 500 thousand tonnes
- Borouge reiterated its commitment to pay USD 1.3 Bn in dividends in 2023 while the Company trades at attractive 2023 dividend yield of 6.2%



Stock Information

Market Cap (AED, mm)	77,548.84
Paid Up Capital (mm)	4,809.23
52 Week High	2.92
52 Week Low	2.45
3M Avg. daily value(AED)	14,350,330

3Q23 Result Review (USD, mm)

Total Assets	8,850
Total Liabilities	4,589
Total Equity	4,261
EBITDA	592
Net Profit	279

Financial Ratios

Dividend Yield (12m)	6.12
Dividend Pay-out (%)	0.00
Price-Earnings Ratio(x)	17.88
Price-to-Book Ratio (x)	4.97
Book Value (AED)	0.14
Return-on Equity (%)	21.51

Stock Performance

5 Days	2.38%
1 Months	0.39%
3 Months	-7.86%
6 Months	-3.01%
1 Year	-4.44%
Month to Date (MTD%)	2.79%
Quarter to Date (QTD%)	-2.27%
Year to Date (YTD%)	1.98%

3Q23 Net Profit higher than our estimate

Borouge Plc (Borouge/the company) net profit declined 8.3% YOY to USD 279 Mn in 3Q23, higher than our estimate of USD 227 Mn. The decline in net profit is mainly attributable to a decline in revenue owing to lower average selling prices of Polyethylene (PE) and Polypropylene (PP) as compared to the peak in prices during 3Q22, increase in G&A expenses, and higher finance cost partially offset by an increase in sales volume, decline in selling and distribution expenses, and decline in cost base. Borouge's total cost per tonne fell 26% YOY in 3Q23.

P&L Highlights

Borouge's revenue declined 10.6% YOY to USD 1,496 Mn in 3Q23 mainly driven by decline in average selling prices. PE average selling price fell 14.0% YOY to USD 1,093 per tonne in 3Q23 whereas PP average selling prices decreased 14.7% YOY to USD 967 per tonne in 3Q23. Decline in revenue was partially offset by increase in sales volume. Borouge's PE sales volume rose 7.6% YOY to 733 thousand tonnes in 3Q23 while PP volume grew 18.0% YOY to 642 thousand tonnes. The Company's production operated at high utilization rates where utilization rate of PE stood at 104% and PP at 109% in 3Q23. Moreover, Olefin Conversion Unit (OCU) which internally produces propylene operated at a high utilization rate of 109% in 3Q23. The Company's direct cost declined 7.9% YOY to USD 915 Mn in 3Q23 driven by decline in other variable and fixed production cost. Furthermore, Borouge's G&A expenses rose 21.0% YOY to USD 41 Mn in 3Q23 due to non-recurring one-off items. Whereas, selling and distribution expenses declined 50.6% YOY to USD 95 Mn in 3Q23 owing to a significant fall in freight costs. Thus, the Company's EBITDA declined 0.1% YOY to AED 592 Mn in 3Q23 with an improved EBITDA margin of 39.6% in 3Q23 as compared to 35.4% in 3Q22. As a result, operating profit declined 1.8% YOY

to USD 449 Mn in 3Q23. Moreover, the Company's finance cost rose 57.3% YOY to USD 59 Mn in 3Q23 while finance income declined 33.9% YOY to USD 7 Mn. In addition, income tax expense fell 5.6% YOY to USD 116 Mn in 3Q23 in line with decline in profitability.

Balance Sheet Highlights

The company's cash conversion increased to 97% in 3Q23 as compared to 96% in 2Q23. Whereas the operating free cash flow stood at USD 573 Mn in 3Q23 as compared to USD 496 Mn in 2Q23. The Company incurred a capex of USD 20 Mn in 3Q23, down from USD 22 Mn in 2Q23. The Company's borrowings marginally rose 0.1% QOQ to USD 3.3 Bn in 3Q23 while net debt stood at 3.02 Bn in 3Q23 as compared to USD 3.00 Bn in 2Q23.

Target Price and Rating

We maintain our ACCUMULATE rating on Borouge with a revised target price of AED 2.95. The target price is revised mainly due to PE and PB price revision amid challenging business conditions. The Company's profitability declined due to lower average selling prices of PE and PP in 3Q23 partially offset by increased sales volume. Borouge's production increased due to high utilization rates of PE at 104% and PP at 109% which led to 4% increase in sales volume during 3Q23. Moreover, OCU unit which produces propylene from ethylene operated at higher utilization of 109% in 3Q23 and the company further aims to operate it at a higher utilization rate in the upcoming period to produce propylene at a lower cost. Improved operating efficiency resulted in 417 bps YOY increase in EBITDA margin to 39.6% during 3Q23. The polyolefin market is expected to remain challenging in the near-term due to capacity addition resulting in higher competition. The Company expects its sales volumes to stay in line with 2Q23 levels while pricing is expected to remain around 3Q23 levels with slight volatility. A long-term pricing agreement with ADNOC ensures long-term feedstock security keeping the cost base lower. The value enhancement program delivered a USD 420 Mn positive impact in 9M23, surpassing the target of USD 400 Mn for 2023. It further raised the target to USD 500 Mn to mitigate the decline in polyolefin prices. In addition, the Company plans regular turnaround of Borouge 3 plant and feedstock-related operations in 2024. The feedstock-related operation shutdown will be performed in 1Q24 which will impact production by 170 thousand tonnes while Borouge 3 turnaround will take place in 4Q24 resulting in a production loss of 330 thousand tonnes. In addition, the board paid USD 650 Mn dividend in September 2023 and reiterated its commitment to pay USD 1.3 Bn in dividends for the year 2023. The Company trades at an attractive 2023 dividend yield of 6.2%. Thus, considering the above-mentioned factors, we assign a BUY rating on the stock.

Borouge - Relative valuation

(at CMP)	2021	2022	2023F
PE	NA	15.00	22.02
PB	NA	4.34	4.67
EV/EBITDA	NA	8.28	10.85
Dividend yield	NA	4.6%	6.2%

FABS Estimates & Co Data

Note – Borouge listed on ADX in June 2022. Thus, financial multiple for the prior period is unavailable

Borouge – P&L

USD mm	3Q22	2Q23	3Q23	3Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenues	1,674	1,416	1,496	1,414	5.8%	-10.6%	5.7%	6,727	5,734	-14.8%
Direct Cost	-994	-899	-915	-891	2.7%	-7.9%	1.8%	-3,792	-3,620	-4.5%
Gross Profit	680	517	581	523	11.1%	-14.5%	12.5%	2,935	2,114	-28.0%
Other income	5	5	4	4	6.0%	-22.2%	-25.8%	35	21	-39.0%
G&A expense	-34	-49	-41	-51	-19.2%	21.0%	-15.2%	-176	-180	2.3%
Selling and dist. expenses	-192	-105	-95	-111	-14.4%	-50.6%	-9.3%	-703	-400	-43.1%
EBITDA	593	518	592	499	18.7%	-0.1%	14.4%	2,646	2,024	-23.5%
Operating Profit	457	369	449	365	23.1%	-1.8%	21.8%	2,075	1,555	-25.0%
Finance costs	-37	-52	-59	-57	3.2%	57.3%	12.3%	-119	-227	90.9%
Finance income	11	4	7	6	13.5%	-33.9%	79.8%	21	25	19.0%
FX (loss)/Gain	0	-1	0	0	NM	NM	NM	-4	-2	NM
Profit before tax	431	320	398	314	26.6%	-7.7%	24.4%	1,973	1,352	-31.5%
Income tax expenses	-123	-88	-116	-85	36.6%	-5.6%	31.2%	-564	-392	-30.5%
Net Profit	304	229	279	227	22.7%	-8.3%	21.9%	1,393	951	-31.7%

FABS estimate & Co Data

Borouge - Margins

	3Q22	2Q23	3Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Gross margin	40.6%	36.5%	38.9%	-179	235	43.6%	36.9%	-677
EBITDA margin	35.4%	36.6%	39.6%	417	301	39.3%	35.3%	-404
Operating margin	27.3%	26.0%	30.0%	268	397	30.8%	27.1%	-372
Net profit margin	18.2%	16.2%	18.7%	48	248	20.7%	16.6%	-412

FABS estimate & Co Data

Valuation:

We use Discounted Free Cash Flow (DCF), Discount Dividend Method (DDM), and Relative Valuation (RV) to value Borouge. We have assigned 50% weight to DCF and 25% each to DDM and RV.

Valuation Method	Target	Weight	Weighted Value
DCF Method	3.04	50.0%	1.52
DDM Method	3.44	25.0%	0.86
Relative Valuation (RV)	2.29	25.0%	0.57
Weighted Average Valuation (AED)			2.95
Current market price (AED)			2.58
Upside/Downside (%)			+14.2%

1) DCF Method:

Borouge is valued using free cash flow to firm. We have discounted the cash flow using the weighted average cost of capital of 7.9%. It is arrived after using cost of equity of 8.4% and after tax cost of debt of 4.9% with an equity weight of 86.5% and debt of 13.7%. Cost of equity is calculated by using 10-year government bond yield of 4.5%, beta of 0.96 and equity risk premium of 4.0%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk free rate. Cost of debt of 6.5% is adjusted for a tax rate of 24.8% to arrive at after tax cost of debt of 4.9%. Also, assumed a terminal growth rate of 2.5%.

Sum of PV (USD, Mn)	3,954
Terminal value (USD, Mn)	23,904
FV to Common shareholders (USD, Mn)	24,843
No. of share (Mn)	30,058
Current Market Price (AED)	2.58
Fair Value per share (AED)	3.04

DCF Method

(All Figures in USD Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E	FY 2029E
Cash flow from operating activities	1,375	1,251	1,968	2,861	3,005	2,414	2,265
(-) Capex	-240	-240	-6,680	-180	-250	-250	-250
Free Cash Flow to Firm (FCFF)	189	1,011	-4,712	2,681	2,755	2,164	2,015
Discounting Factor	0.99	0.92	0.85	0.79	0.73	0.68	0.63
Discounted FCFF	187	926	-4,000	2,109	2,009	1,462	1,261

Source: FAB Securities

2) DDM Method:

Borouge distributed a healthy dividend in 2022 and further aims to pay a dividend of USD 1.3 Bn in 2023. It further expects this dividend payment will be sustained even in the forecasted period due to strong cash flow generation. The dividend is discounted at the cost of equity of 8.4%.

Sum of PV (USD, Mn)	8,866
Terminal value (USD, Mn)	19,272
FV to Common shareholders (USD, Mn)	28,138
No. of share (Mn)	30,058
Current Market Price (AED)	2.58
Fair Value per share (AED)	3.44

(All Figures in USD Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E	FY 2029E
Dividend Paid							
H1		455	804	1,207	1,240	974	907
H2	650	455	804	1,207	1,240	974	907
Total Dividend	650	910	1,609	2,413	2,480	1,947	1,813
Discounting Factor	0.99	0.91	0.84	0.78	0.72	0.66	0.61
Present Value of Dividend	642	830	1,353	1,873	1,776	1,287	1,106

Source: FAB Securities

2) Relative Valuation:

We have used local peers to value Borouge and it is valued using the EV/EBITDA multiple. It is valued at EV/EBITDA multiple of 10.8x. We have applied a discount to the peer valuation multiple as the Company's earnings are lower due to volatility in selling prices.

Company	Market	EV/EBITDA (x)		P/E (x)		P/B (x)	
	(USD Mn)	2023F	2024F	2023F	2024F	2023F	2024F
Yanbu National Petrochemical	5,678	21.5	10.2	NM	32.2	1.7	1.8
National Industrialization Co.	2,073	11.6	6.2	23.1	9.8	0.8	0.7
Sahara International Petrochemical	6,255	9.5	7.1	15.2	10.9	1.5	1.5
Advanced Petrochemicals Co	2,572	27.3	18.3	37.0	16.4	2.5	2.2
Saudi Ind Investment Group	61,610	9.1	6.3	44.2	17.5	1.2	1.2
Saudi Kayan Petrochemical Co	4,233	21.8	7.8	NM	46.2	1.2	1.2
Average		16.8x	9.3x	29.9x	22.2x	1.5x	1.4x
Median		16.6x	7.4x	30.1x	17.0x	1.4x	1.4x
Max		21.7x	9.6x	38.8x	28.5x	1.7x	1.7x
Min		10.0x	6.5x	21.1x	12.3x	1.2x	1.2x

Source: FAB Securities

Research Rating Methodology:

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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