

## Borouge PLC

Turnaround of Borouge 2 impacted the profitability

### 1Q23 Net profit slightly higher than our estimate

Borouge plc (Borouge/the company) net profit fell 45.1% YOY to USD 199 Mn in 1Q23, slightly higher than our estimate of USD 213 Mn. The decline in the net profit was mainly attributable to a decrease in revenue driven by a decline in sales volumes due to maintenance at the Borouge 2 partially offset by a significant decline in selling and administrative expenses.

### P&L highlights

Borouge recorded 13.1% YOY decline in revenue during 1Q23 primarily driven by lower sales volumes owing to the maintenance of Borouge 2 plant. Borouge's Polyethylene (PE) volumes declined 6.1% YOY to 573 thousand tonnes (kt) whereas Polypropylene (PP) volumes rose 6.6% YOY to 488 kt in 1Q23. Ethylene and other volumes rose to 96 kt in 1Q23 as compared to 32 kt in 1Q22. PE average selling price fell 14.1% YOY to USD 1,202 per tonne in 1Q23 whereas PP average prices declined 21.7% YOY to USD 1,082 per tonne. On the other hand, the Olefin Conversion Unit (OCU) which internally produced propylene was utilized at 44% in 1Q23 as compared to 100% utilization rate in 4Q22. The Company's direct cost rose 5.3% YOY to USD 914 Mn in 1Q23 mainly due to the lower utilization of OCU unit as a result of the maintenance of Borouge 2. As a result, the Company consumed a higher proportion of externally sourced propylene leading to an increase in feedstock price. Thus, gross profit declined 35.3% YOY to USD 467 Mn in 1Q23. Furthermore, G&A expense rose 16.2% YOY to USD 46 Mn in 1Q23 whereas selling and distribution expenses declined significantly 42.8% YOY to USD 100 Mn owing to lower sea freight costs. Operating expenses mainly declined due to the Company's value enhancement programme. EBITDA declined 28.3% YOY to USD 460 Mn in 1Q23 with an EBITDA margin of 33.3%. Thus, total operating profit declined 35.9% YOY to USD 327 Mn in 1Q23. Moreover, finance cost more than doubled from USD 14 Mn in 1Q22 to USD 53 Mn in 1Q23 mainly driven increase in debt and higher benchmark rates. However, finance cost is expected to decline in the remaining quarter of 2023 due to the repayment of USD 500 Mn debt in 1Q23. Similarly, finance cost rose from 2 Mn in 1Q22 to USD 10 Mn in 1Q23. In addition, income tax expense declined 38.1% YOY to 84 Mn in 1Q23 in line with decline in profitability.

### Balance Sheet highlights

The company's cash conversion stood at 82% in 1Q23 as compared to 86% in 4Q22 with an operating free cash flow of USD 378 Mn in 1Q23 as compared to USD 465 Mn in 4Q22. The Company's operating cash flow conversion rate declined in 1Q23 mainly due to additional operations expenses over the maintenance of Borouge 2. Borouge incurred a capex of USD 82 Mn in 1Q23 as compared to USD 128 Mn in 1Q22 and USD 73 Mn in 4Q22. In addition, Borouge repaid USD 500 Mn of commercial term facility in 1Q23 with a net debt of USD 3.3 Bn in 1Q23.

### Target price and recommendation

We maintain our BUY rating on Borouge with a target price of AED 3.10. The Company successfully completed the turnaround of the Borouge 2 on 17 March 2023. Due to this maintenance, Borouge 2 recorded a production loss of 200 kt in 1Q23. The turnaround of the

**Rating : BUY**

## First Look Note – 1Q23

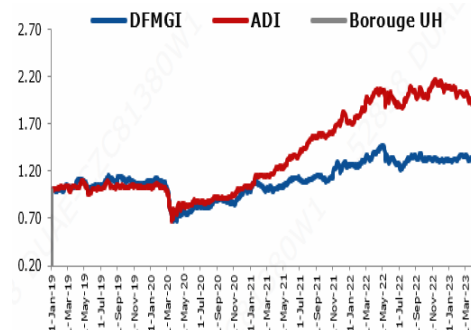
**Sector: Basic Material**

### Recommendation

Current Price (2-May-23)	2.63
Target Price (AED)	3.10
Upside/Downside (%)	+18%

### Stock Information

Market Cap (mm)	79,051.73
Paid Up Capital (mm)	4,809.23
52 Week High	3.27
52 Week Low	2.45
3M Avg. daily value (AED)	21,706,060



### Financial Ratios

Dividend Yield (12m)	4.51
Dividend Pay-out (%)	0.00
Price-Earnings Ratio (x)	15.28
Price-to-Book Ratio (x)	4.90
Book Value (AED)	0.15
Return-on Equity (%)	27.41
Earning Per Share (AED)	0.05
Beta	N/A

### Stock Performance

5 Days	0.77%
1 Months	2.73%
3 Months	-1.87%
6 Months	-1.87%
1 Year	N/A
Month to Date (MTD)	-0.38%
Quarter to Date (QTD)	2.33%
Year to Date (YTD)	3.95%

Borouge 2 plant also led to lower utilization of cost-advantaged OCU unit at 44% in 1Q23 as compared 100% in 4Q22. The Company's production rose 0.4% YOY and declined 22.6% QOQ in 1Q23. Borouge's net profit in 1Q23 mainly declined due to lower sales volume partially offset by a rise in price. The profit should improve in the upcoming quarters as the utilization of the OCU unit increases post turnaround of Borouge 2. Although, Borouge maintained a strong polyolefin premia pricing in 1Q23. The Company successfully completed the test run of PP5 unit for the production of differentiated grades for the expansion of the product portfolio and focuses on selling the same in 2023. Borouge's value enhancement programme already benefited the company with USD 100 Mn of synergy across variable and fixed costs as of 1Q23. In addition, the value enhancement programme is further expected to deliver USD 400 Mn worth of impact on EBITDA in 2023. Borouge paid a final dividend amounting to USD 650 Mn in April 2023 resulting in a total post-IPO dividend of USD 975 Mn. Consequently, the company maintained its decision to pay USD 1.3 Bn in dividend for the year 2023. Additionally, the Company repaid USD 500 Mn of its USD 3.65 Bn Commercial Term Facility which will further reduce leverage and finance cost. Thus, considering the abovementioned factors, we maintain our BUY rating on the stock.

#### Borouge - Relative Valuation

(at CMP)	2022	2023F
P/E	15.35	18.13
P/B	4.44	4.55
EV/EBITDA	8.47	8.86
Dividend Yield	4.5%	6.0%

FABS estimate & Co Data

#### Borouge - P&L

(USD Mn)	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenues	1,590	1,593	1,382	1,396	-1.0%	-13.1%	-13.3%	3,997	6,366	59.3%
Direct Cost	-868	-998	-914	-894	2.2%	5.3%	-8.4%	-2,386	-3,833	60.6%
<b>Gross Profit</b>	<b>722</b>	<b>595</b>	<b>467</b>	<b>502</b>	<b>-6.8%</b>	<b>-35.3%</b>	<b>-21.4%</b>	<b>1,611</b>	<b>2,534</b>	<b>57.3%</b>
Other income	4	17	5	6	-11.4%	22.2%	-69.0%	27	27	1.1%
G&A Expenses	-40	-71	-46	-28	62.8%	16.2%	-34.9%	-113	-136	21.0%
Selling & dist. exp	-174	-148	-100	-111	-10.6%	-42.8%	-33.0%	-414	-462	11.6%
Impairment Provision	-2	-4	0	0	NM	NM	NM	-13	0	NM
<b>EBITDA</b>	<b>642</b>	<b>541</b>	<b>327</b>	<b>508</b>	<b>-35.7%</b>	<b>-49.0%</b>	<b>-39.6%</b>	<b>2,646</b>	<b>2,524</b>	<b>-4.6%</b>
<b>Operating Profit</b>	<b>510</b>	<b>388</b>	<b>327</b>	<b>368</b>	<b>-11.1%</b>	<b>-35.9%</b>	<b>-15.8%</b>	<b>1,097</b>	<b>1,962</b>	<b>78.8%</b>
Finance costs	-14	-52	-53	-60	-11.2%	287.4%	1.5%	-96	-239	149.5%
Finance income	2	9	10	1	NM	NM	17.4%	20	5	-74.7%
FX (loss)/Gain	0	-3	-1	0	NM	NM	NM	-3	0	NM
<b>Profit before tax</b>	<b>498</b>	<b>342</b>	<b>283</b>	<b>309</b>	<b>-8.5%</b>	<b>-43.2%</b>	<b>-17.2%</b>	<b>1,019</b>	<b>1,728</b>	<b>69.6%</b>
Income tax expenses	-135	-94	-84	-96	-12.7%	-38.1%	-11.4%	-285	-536	88.1%
<b>Profit for the year</b>	<b>363</b>	<b>247</b>	<b>199</b>	<b>213</b>	<b>-6.6%</b>	<b>-45.1%</b>	<b>-19.5%</b>	<b>734</b>	<b>1,192</b>	<b>62.5%</b>

FABS Estimates & Co Data

#### Borouge - Margins

	1Q22	4Q22	1Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Gross Profit	45.4%	37.3%	33.8%	-1158	-351	40.3%	39.8%	-50
EBITDA	40.4%	34.0%	23.7%	-1670	-1030	66.2%	39.6%	NM
Operating Profit	32.1%	24.4%	23.7%	-843	-71	27.5%	30.8%	337
Net Profit	22.8%	15.5%	14.4%	-840	-111	18.4%	18.7%	37

FABS estimate & Co Data

## Valuation:

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

Valuation Method	Target	Weight	Weighted Value
Discounted Free Cash flow (DCF)	24,942	50.0%	12,471
Dividend Discount Model (DDM)	27,375	25.0%	6,844
Relative Valuation (RV)	24,322	25.0%	6,080
<b>Weighted Average Valuation (AED)</b>			<b>93,263</b>
<b>Fair Value per price (AED)</b>			<b>3.10</b>
<b>Current market price (AED)</b>			<b>2.63</b>
<b>Upside/Downside (%)</b>			<b>17.87%</b>

### 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 7.2%. It is arrived after using cost of equity of 7.8% and cost of debt of 5.9% with a equity weight of 84.4% and debt of 15.6%. Cost of equity is calculated by using 10-year government bond yield of 4.3%, beta of 0.90 and equity risk premium of 3.9%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk free rate. Cost of debt is calculated using cost of 5.9% after adjusting a tax rate of 30.6%. Also, assumed a terminal growth rate of 2.5%.

Sum of PV (AED, Mn)	4,465
Terminal value (AED, Mn)	23,602
<b>FV to Common shareholders (AED, Mn)</b>	<b>24,954</b>
No. of share (Mn)	30,058
Current Market Price (AED)	2.63
<b>Fair Value per share (AED)</b>	<b>3.05</b>

#### DCF method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E	FY 2029E
Cash Flow from Operation (CFO)	1,652	2,080	2,038	2,266	2,494	1,750	1,978
(-) Capex	-240	-240	-6,680	-180	-250	-250	-250
<b>Free Cash Flow to Equity (FCFE)</b>	<b>1,412</b>	<b>1,840</b>	<b>-4,642</b>	<b>2,086</b>	<b>2,244</b>	<b>1,500</b>	<b>1,728</b>
Discounting Factor	0.95	0.89	0.83	0.77	0.72	0.67	0.63
<b>Discounted FCFE</b>	<b>1,348</b>	<b>1,638</b>	<b>-3,854</b>	<b>1,615</b>	<b>1,621</b>	<b>1,011</b>	<b>1,086</b>

## 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 of multiple of 9.3x in line with peers.

Company	Market	EV/EBITDA (x)		PE (x)		PB (x)	
	(USD Mn)	2023	2024	2023	2024	2023	2024
Yanbu National Petrochemical	6,625	15.7	10.2	76.4	25.9	1.9	2.0
National Industrialization Co.	2,409	12.9	5.8	17.5	12.6	0.9	0.9
Sahara International Petrochemical	7,507	8.6	8.4	13.8	13.8	1.7	1.7
Advanced Petrochemicals Co	3,291	25.8	19.9	33.1	21.6	3.3	3.0
Saudi Ind Investment Group	5,104	15.8	12.5	18.0	14.5	2.0	1.8
Saudi Kayan Petrochemical Co	5,050	15.3	7.6	-38.7	23.3	1.4	1.2
<b>Average</b>		15.7	10.7	20.0	18.6	1.9	1.8
<b>Median</b>		15.5	9.3	17.8	18.1	1.8	1.7
<b>Max (Quartile 3)</b>		15.8	11.9	29.3	22.9	2.0	2.0
<b>Min (Quartile 1)</b>		13.5	7.8	14.7	14.0	1.4	1.4

## 3) DDM Method:

Borouge distributed a healthy dividend in 2022 and further aims to pay a dividend of USD 1.3 Bn in 2023 and further expects this dividend payment will sustain even in the forecasted period due to strong cash flow generation. Dividend is discounted at the cost of equity of 7.8%.

Sum of PV (AED, Mn)	8,945
Terminal value (AED, Mn)	18,430

<b>FV to Common shareholders (AED, Mn)</b>	<b>27,375</b>
No. of shares (Mn)	30,058
Current Market Price (AED)	2.63
<b>Fair Value per share (AED)</b>	<b>3.34</b>

### DDM method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E	FY 2029E
<b>Dividend paid</b>							
H1	650	994	1,004	1,126	1,212	900	1,037
H2	650	663	669	751	808	600	691
<b>Total Dividend</b>	<b>1,300</b>	<b>1,656</b>	<b>1,673</b>	<b>1,877</b>	<b>2,020</b>	<b>1,500</b>	<b>1,728</b>
Discounting Factor	0.95	0.88	0.82	0.76	0.70	0.65	0.61
<b>Present Value of Dividend</b>	<b>1,237</b>	<b>1,462</b>	<b>1,369</b>	<b>1,426</b>	<b>1,423</b>	<b>980</b>	<b>1,048</b>

**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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