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Borouge

BOROUGE PLC – H1 and Q2 FY2022

Management Discussion & Analysis

28 July 2022

INSPIRING TOMORROW

1. Summary of Operational and Financial Performance

Borouge Plc reported significant revenue growth in Q2 and H1 2022. In Q2, revenue growth over the prior quarter of 17.6% was primarily driven by volume growth of 11.5%, and average price per tonne growth of 6.8%. Pricing was driven by higher underlying IHS Markit benchmark pricing, and higher premiums over benchmark vs the prior periods.

Plant utilisation grew quarter on quarter as we completed the ramp up of the new PP5 plant, and the turnaround of Borouge 1 ("B1"). Revenues were also supported by drawing down inventories in the month of June, a month of record sales for the business, to levels in line with mid-term guidance.

During the second quarter, operating profit and net income margins grew as we leveraged our cost base lowering our overall production costs per tonne vs the prior quarter. This was achieved despite continuing higher selling and distribution expenses, reflecting globally elevated shipping costs. In Q2 we generated Adjusted EBITDA of US$869.8MM and Net Income of US$484.8MM.

We generated significant cashflow in the period, reflecting our underlying higher profitability. Cashflow conversion was high, reflecting low capital expenditure in the period as PP5 capex finishes. Net debt remained stable in the period at approximately 1.2x Net Debt/EBITDA.

	Unaudited pro forma combined total for the year ended 31 December 2021	Unaudited pro forma six months to 30 June 2021	Unaudited pro forma six months to 30 June 2022	Unaudited pro forma Three months to 31 March 2022	Unaudited pro forma Three months to 30 June 2022	*Q2 22 vs Q1 22 (%)*
Total sales volumes (k/T)	4,422	2,143	2,328	1,100	1,227	*12%*
…Polyethylene	2,509	1,197	1,262	610	652	*7%*
…Polypropylene	1,772	828	954	458	496	*8%*
…Ethylene and others	141	118	111	32	79	*147%*
Average selling price ($/t)						
…Polyethylene	1,421	1,344	1,460	1,399	1,518	*9%*
…Polypropylene	1,313	1,436	1,409	1,381	1,435	*4%*
Product Premia ($/t)						
…Polyethylene	334	264	368	296	436	*47%*
…Polypropylene	147	262	283	244	318	*30%*
	US$MM	**US$MM**	**US$MM**	**US$MM**	**US$MM**	
Revenue	6,216	2,972	3,460	1,590	1,870	*18%*
Feedstock costs	(1,170)	(562)	(593)	(274)	(320)	*17%*
Variable & fixed production costs	(2,063)	(953)	(1,207)	(594)	(613)	*3%*
Gross profit	2,983	1,458	1,659	722	937	*30%*
General and administrative expenses (excluding D&A)	(147)	(59)	(71)	(42)	(29)	*-31%*
Selling & distribution expense	(483)	(215)	(362)	(174)	(188)	*8%*
Others	27	8	3	4	-	*-127%*
Operating profit	**2,208**	**1,192**	**1,229**	**510**	**719**	*41%*
Total comprehensive income for the period	**1,529**	832	848	363	485	*34%*
Profit Margin (%)	*25%*	*28%*	*25%*	*23%*	*26%*	*13%*
Adjusted EBITDA(1)	**2,723**	**1,486**	**1,512**	**642**	**870**	*36%*
Adjusted EBITDA Margin (%)	*44%*	*50%*	*44%*	*40%*	*47%*	*16%*
Basic earnings per share (US$)			0.03			
Diluted earnings per share (US$)			0.03			
Net Debt (US$MM)			3,543	3,306	3,543	*7%*

(1) Adjusted EBITDA includes impairment loss of property, plant and equipment

1. Operational Review

During Q2 2022 we grew overall production capacity by 5.4% through the ramp up of our new PP5 unit, adding new polypropylene capacity vs the prior quarter. This new unit initially started production with base grades, but during Q2 we have been successfully introducing more differentiated grades into its production mix, further supporting our premium product set.

We also completed the turnaround of the Borouge 1 ("B1") plant in Q1, which further contributed to production volume growth vs the prior quarter.

	For the Year Ended 31 December 2021	Six months to 30 June 2021	Six months to 30 June 2022	Three months to 30 March 2022	Three months to 30 June 2022
Production capacity (Mt/k)					
…Polyethylene	2,750	1,364	1,364	678	686
…Polypropylene	1,750	868	1,023	484	539
		2,232	**2,387**	**1,162**	**1,225**
Utilisation rate					
…Polyethylene	81%	91%	87%	81%	93%
…Polypropylene	98%	98%	88%	87%	90%

Olefin production volumes in the quarter were strong, with record steam cracker performance in the period.

We reported in our Q1 2022 results that propylene feedstock availability was challenged in the period following constraints at ADNOC Refining. These constraints continued into Q2, resulting in polypropylene capacity utilisation running at 90% in the period.

Notwithstanding this feedstock availability disruption, we were able to internally produce significant volumes of propylene, converting ethylene via our Olefin Conversion Unit ("OCU"), which ran at a near 100% utilisation rate in the period. Availability propylene from ADNOC Refining has resumed during the course of July, and is not anticipated to impact production volumes in Q3 FY22.

We also experienced an unplanned shutdown of our Low-Density Polyethylene ("LDPE") unit in the course of Q2, which we anticipate will continue for at least the balance of the financial year. The LDPE unit is one of 16 units at our Ruwais production complex.

We consider our flexibility to internally optimise feedstock production in circumstances such as these to be a key competitive advantage of Borouge. As a result of the LDPE shutdown, we have been able to redirect more of our cost advantaged ethylene to the OCU for conversion into propylene. Internally produced propylene is cheaper, even after conversion expenses, than purchased propylene at current market prices. This internal polypropylene production supported overall feedstock costs in Q2, helping to mitigate the LDPE shutdown impact. We are working closely with Borealis to provide supply continuity for those customers taking XLPE from us.

2. Revenues & Pricing

	For the Year Ended 31 December 2021 Combined	Six months to 30 June 2021	Six months to 30 June 2022	Three months to 30 March 2022	Three months to 30 June 2022	Q2 vs Q1 FY22 (%)
Sales volumes by product **('000 tons)**						
…Polyethylene	2,509	1,197	1,262	610	652	7%
…Polypropylene	1,772	828	954	458	496	8%
…Ethylene and others	141	118	111	32	79	147%
Polyethylene (US$)						
…Average sales prices / tonne	1,421	1,344	1,460	1,399	1,518	9%
…Premia	334	264	368	296	436	47%
...Benchmark	1,087	1,081	1,092	1,102	1,082	-2%
Polypropylene (US$)						
…Average sales prices	1,313	1,436	1,409	1,381	1,435	4%
…Premia	147	262	283	244	318	30%
…Benchmark	1,166	1,174	1,126	1,137	1,117	-2%
Revenue by product						
(US$MM)						
…Polyethylene	3,547	1,664	1,953	904	1,049	16%
…Polypropylene	2,538	1,207	1,386	652	734	13%
…Ethylene and others	131	101	121	34	86	135%
Total Revenues	6,216	2,972	3,460	1,590	1,870	18%

(1) Benchmark prices represent HDPE Blow Molding NEA CFR and polypropylene Raffia NEA CFR prices as per IHS Markit data.
(2) Average sales prices are equal to revenue over sales volumes (including commissions).
(3) Premia is equal to the difference between average sales prices and the benchmark prices.

Q2 2022 sales volumes grew by 11.5% vs Q1, reflecting both higher underlying production following the PP5 ramp up and B1 turnaround in Q1. Year over year our total sales volumes grew by 8.6%. It should be noted that the lower sales volumes achieved in the prior Q1 2022 period were also impacted by Chinese New Year which fell in that period.

We sold an increasing proportion of our products into the infrastructure solutions market in Q2 and H1 2022. The Asia Pacific market continues to be our largest destination for sales.

Our sales volumes in June 2022 were our strongest ever achieved in a single month. In particular, we note significant sales volumes of PE100 during Q2 2022, a key product used in infrastructure applications. PE100 is a premium product. Higher sales volumes of PE100 have contributed positively to our overall sales mix outcome.

We continue to achieve premia above benchmark pricing, reflecting our differentiated product mix, and our ability to capture regional price opportunities. During the quarter, our premia for PE and PP grew to US$436 and US$318 per tonne respectively.

Segmental revenue breakdown

	For the Year Ended 31 December 2021 Combined	Six months to 30 June 2021	Six months to 30 June 2022	Three months to 30 March 2022	Three months to 30 June 2022
By product group					
…Polyethylene	57%	56%	57%	57%	57%
…Polypropylene	40%	41%	40%	41%	39%
…Ethylene and others	3%	3%	3%	2%	4%
By end market					
…Consumer solutions	56%	56%	49%	49%	49%
…Infrastructure solutions	38%	38%	46%	47%	45%
…Other	6%	6%	5%	4%	6%
By geography					
…Asia Pacific	59%	59%	59%	59%	60%
…Middle East & Africa	33%	29%	32%	33%	32%
…Rest of World	9%	12%	8%	8%	8%

(1) Consumer Solutions includes sales to the agriculture sector.
(2) Other in "By End Markets" includes approximately 0.1Mt to the mobility and healthcare sectors and approximately 0.1Mt of ethylene and other products.

3. Costs

	For the Year Ended 31 December 2021 Combined	Six months to 30 June 2021	Six months to 30 June 2022	Three months to 30 March 2022	Three months to 30 June 2022	Q2 vs Q1 FY22
	US$MM	**US$MM**	**US$MM**	**US$MM**	**US$MM**	**(%)**
Revenue	6,216	2,972	3,460	1,590	1,870	*18%*
Cost of sales (excluding D&A)	2,719	1,220	1,528	736	792	8%
…Feedstock costs	*1,170*	562	593	274	320	17%
…Other variable and fixed production costs	*1,549*	658	935	463	472	2%
…as % of revenue	*44%*	*41%*	*44%*	*46%*	*42%*	-9%
Selling and distribution expenses	483	215	362	174	188	8%
…as % of revenue	8%	7%	10%	11%	10%	-8%
General and administrative expenses (excluding D&A)	146	59	71	42	29	-31%
…as % of revenue	2%	2%	2%	3%	2%	-41%
Depreciation and amortization	514	293	272	130	142	9%
Operating Profit	**2,208**	**1,192**	**1,229**	**510**	**719**	***41%***
…as % of revenue	*36%*	*40%*	*36%*	*32%*	*38%*	*20%*
Total operating costs / tonne of production	*906*	*830*	*952*	*981*	*926*	*(6)%*

During the quarter, revenues grew by 17.6% vs total cost growth of 6.4%. As a result, operating profit expanded by 41.0% to US$ 719.0MM in Q2 2022. Operating profit margin expanded to 38.5% for Q2 vs 32.1% in the prior quarter.

Within costs, feedstock expenses grew by 6% in H1 2022 vs H1 2021, reflecting our relatively fixed ethane cost base, but exposure to variable propylene prices. Q2 2022 feedstock costs grew by 17% vs Q1 FY22, reflecting higher propylene prices in the period, but primarily reflecting the impact of the ramp up of B1. As previously discussed, we were able to internally produce propylene from ethylene in Q2

2022 from our olefin conversion unit at a lower cost than the equivalent volumes procured from ADNOC in Q2 2022. We anticipate continuing to internally produce propylene in the course of Q3 2022.

Two cost lines grew more slowly than revenues, supporting margin expansion in Q2 vs Q1 2022. Firstly, other variable and fixed production costs, which includes the costs of utilities, catalysts and additives only marginally increased over the quarter vs revenue growth, contributing to lower overall costs of production as a percentage of revenues. While certain costs in this item, such as utilities inflated, we also capture the impact of changes in inventory in this line item. Q2 2022 benefitted from positive movements in this item vs Q1.

Secondly, selling and distribution costs also grew by less than our total sales volumes, also contributing to margins. While costs grew only in line with volumes in Q2, year over year we are experiencing higher selling and distribution costs. In particular, sea freight rates have climbed significantly year over year, with costs tripling on many routes, due to disruptions in the global shipping market.

G&A expenses significantly decreased over the period primarily due to the B4 carve-out, but increased year on year reflecting expenses incurred as Borouge was preparing for the listing process.

4. Cash generation

	Unaudited pro forma combined total for the year ended 31 December 2021	Unaudited pro forma Six months to 30 June 2021	Unaudited pro forma Six months to 30 June 2022	Unaudited pro forma Three months to 31 March 2022	Three months to 30 June 2022
	US$MM	**US$MM**	**US$MM**	**US$MM**	
Profit for the period/year	1,529	832	853	363	490
Income tax expense	674	361	347	135	212
Net finance loss, including foreign exchange loss	6	(1)	29	12	17
Depreciation of property, plant and equipment	485	280	259	125	135
Depreciation of right-of-use assets	5	3	2	1	0
Amortisation of intangible assets	23	11	11	6	5
Impairment loss on PPE			10		10
Adjusted EBITDA	**2,723**	**1,486**	**1,512**	**642**	**870**
Capital expenditure(1)	254	134	84	128	(44)
Operating Free Cash Flow(2)	2,469	1,352	1,428	514	914
Cash conversion (%)	*91%*	*91%*	*94%*	*80%*	*105%*

(1) Capital expenditure is calculated as additions to property, plant and equipment for the year/period.
(2) Operating Free Cash Flow is calculated as Adjusted EBITDA less capital expenditure.
(3) Changes in Net Working Capital is calculated as the difference between Net Working Capital at the end of the year/period and beginning of the year/period
(4) Adjusted EBITDA includes add back of impairment losses on PP&E

Adjusted EBITDA in Q2 grew by 35.5% vs Q1 to US$869.8MM, reflecting underlying higher revenues achieved against lower costs per unit of production, and resulting margin expansion. Working capital was a source of cash in the period, as we reduced inventories back to levels in line with our mid-term guidance. Capital expenditure in the period mostly related to maintenance expenditures at existing plants, and was lower vs the prior quarter following the completion of the PP5 unit.

In aggregate, we generated US$914.2 MM of free cashflow in the course of Q2, a conversion rate of 105.1% (Q122: 80.1%) due to Borouge 4 carve-out. From this cashflow generation, during the course of Q2 we paid US$680.0MM of dividends to pre-IPO shareholders, comprising a US$430.0MM ordinary dividend relating to Q1FY22, and a further US$250.0MM pre-IPO dividend.

5. Current trading & outlook

We note that economic activity in our core Asia Pacific and Middle East markets remains strong, with economic growth rates in-excess of developed economies.

Data from market analysts indicate that underlying benchmark prices for PE and PP have softened slightly at the start of Q3, but overall, remain at heightened levels compared to prior years.

High PE and PP prices reflect underlying market prices for propylene and ethylene, which remain elevated vs levels seen in prior years. Analysts' pricing expectations for PE and PP currently anticipate benchmark pricing will subsequently strengthen into the year end, reflecting a presumed resumption of economic activity in China in particular.

We have achieved significant price premia over these benchmarks in the course of Q2. Premia achieved have been at levels significantly above our mid-term guidance of over $200/tonne for PE and over $140/tonne for PP. Premiums in Q3 will likely remain above our mid-term guidance levels. Premiums achieved continue to reflect our highly differentiated product mix, and our ability to capture regional price opportunities. Our core strategy of developing innovative products and continuous innovation which supports our premium pricing has not changed.

Within our cost base, ethane costs will remain essentially fixed in under our long-term pricing agreement with ADNOC, which provides us with significant long-term visibility, a key competitive advantage. Propylene costs broadly track oil prices, which have fallen at the start of Q3, but remain elevated. We anticipate continuing to run our OCU at high levels of utilisation in the coming quarter, generating cost effective propylene feedstock for our PP production. We anticipate logistics costs will continue to be elevated in Q3.

Based on the current performance of its operations and current market conditions, Borouge reiterates its commitment to pay $975 million in dividends to shareholders for Financial Year 2022, and at least $1.3 billion for Financial Year 2023.

The Company will announce its Q3 results on 28 October 2022.