Borouge Q1 2023 Results

Samar Khan:
A warm welcome to everyone and thank you for joining us today. My name is Samar Khan, and I am the Vice President of Investor Relations at Borouge. With me today, I have Hazeem Al Suwaidi, our CEO, Rainer Hoefling, Chief Marketing Officer, Jan-Martin Nufer, Chief Financial Officer, and Louis Desal, Chief Operating Officer. We will begin with a short presentation by the management team in respect to performance for the period, as well as our outlook for 2023. We will then open the call to your questions. I will now hand over to our CEO, Hazeem, to discuss highlights from Q1.

Hazeem Al Suwaidi:
Thank you, Samar, and thank you all for joining us today. While Q1 was a challenging quarter, it was also marked by several important strategic and operational initiatives. I'm pleased to report that the planned Borouge 2 turnaround was executed on time and on budget, and on 17th March the facility came back online. This returns 200kt of capacity to our platform, supporting full production volumes going forward. Revenue declined by 13 percent versus the prior quarter, primarily impacted by lower sales volumes resulting from the planned turnaround and partially offset by higher polyolefin selling prices over the period.

EBITDA and net profit consequently declined, but margins remained stable versus the previous quarter supported by cost savings. We would note the early success of our Value Enhancement Program, which has already delivered over $100 million in cost savings and revenue optimization at quarter-end. We will touch on this in more detail later, and we are looking forward to further positive impacts from the program later in the year. Strong cash conversion remains an important differentiator for our business, supporting our commitment to pay at least $1.3 billion in dividends for 2023 . I'll now hand over to Rainer to talk about our market, the opportunities it presents, and to provide an update on improving pricing and premia.

Rainer Hoefling:
Thank you, Hazeem, and good afternoon, everyone. As you will already be aware, Q4 2022 was characterized by challenging operating conditions, driven by a global inflationary environment, industry-wide softening of prices and volatility in oil and gas markets. Much of this has carried into 2023. As a business, we are in a strong position, proactively addressing market needs and with the ability to place volumes and be tactical about the markets we serve in response to changes in demand. We offer a highly diversified portfolio of premium products that is purpose-built to address global trends such as growing demand for energy transition infrastructure, the rising popularity of electric vehicles, and the critical need for water access and sanitation . Borouge is serving high growth markets, with 68 percent of global polyolefin demand coming from our core geographies. These markets are expected to drive global demand, representing 86 percent of forecasted growth from 2022 to 2026. It is also important to note that the long-term industry environment for polyethylene continues to be robust, with new demand expected to significantly outpace new supply during the coming years. Moving onto polyolefins pricing and premia.

Polyolefin average selling prices improved in Q1 driven by improved market demand and constrained supply due to planned and unplanned production shutdowns, resulting in improved product benchmark prices and premia expansion. Average selling prices for PE and PP improved by 8 percent and 6 percent, respectively vs. Q4 2022. In Q1, we recorded Polyethylene premia of $264 per ton and Polypropylene premia of $137 per ton. Market outlook remains cautious and market analysts anticipate a narrow band price volatility in 2023. Market analysts also expecting stable demand growth in Borouge target markets -- statistics for in-country consumption in China are positive as indicated by PMI indices, though exports remain lower reflecting macro dynamics in developed markets. We are therefore able to reaffirm our over-the-cycle guidance for premia of $200/ton for Polyethylene and $140/ton for Polypropylene, which is made possible by our differentiated product mix and our ability to capture tactical and regional pricing opportunities. I'll now hand over to Louis to take us through some operational highlights from the first quarter.

Louis Desal:
Thank you, Rainer. We'll now look at production volumes and operational upgrades before I ask Rainer to discuss sales. The major operational event of the quarter was the planned Borouge 2 turnaround, impacting production volumes which declined by almost 19 percent vs. the prior quarter. As this slide shows, there was a significant capacity utilization impact during the quarter, for both Polyethylene and Polypropylene, which had previously averaged more than 100 percent utilization. With the turnaround successfully executed on time and on budget, we have since returned 200kt of capacity to total production volume.

It is worth noting that during the Borouge 2 turnaround we were not able to utilize our Olefin Conversion Unit to produce cost-advantaged internal propylene; however, with the re-start-up of the facility, this is now back online. Overall utilization for the Olefin Conversion Unit in the quarter averaged 44 percent . During the period, we also completed the successful and safe reinstatement of our LDPE unit, allowing the XLPE to restart using own-produced LDPE base resin. Meanwhile, at PP5 we delivered a successful test run of further differentiated grades, as part of our initiative to extend the product portfolio. We look forward to providing further updates on this in due course.

Coming back to the successful execution of the Borouge 2 turnaround, I would like to take a moment to highlight the importance of regular maintenance works at our facilities. The quality and operational excellence of our plants is a key comparative advantage for us. Therefore, we make regular investments to keep our assets highly reliable and our plant turnarounds are scheduled with a five-yearly cycle. Our plants are young, well-maintained and highly reliable. 90 percent of our capacity is less than 12 years old and run year-round with limited to no downtime. In 2022, we reached an overall asset reliability run rate of 92 percent and achieved a record quality performance measured as first-time right production rate of 97 percent. As a result, we are both dynamic with our assets and flexible in our operations, thus fulfilling highest levels of customer expectations. Back to you, Rainer

Rainer Hoefling:
Thanks Louis. Let's briefly touch on sales volumes. As mentioned earlier, volumes were materially lower vs. the previous quarter, mainly linked to reduced production capacity due to the planned turnaround, although they were up more than 5 percent on a year on year basis.

Polyolefin prices improved in Q1, hence these lower volumes were partially offset by higher average selling prices. Our sales volumes for energy and infrastructure solutions were particularly strong, at 46 percent of the total polyolefin sales. Asia Pacific remains a key region with 61 percent of total sales volumes followed by Middle East and Africa with 31 percent of total polyolefin sales volumes. I'll now hand over to Jan-Martin, to discuss our financials.

Jan-Martin Nufer:
Thank you, Louis and Rainer. I'll be fairly brief on this slide because we have already covered the main reasons for the negative impacts across our income statement metrics. The quarterly revenue decline was the direct result of the planned Borouge 2 turnaround, and this also impacted EBITDA and net profit. It is important to note that our EBITDA margin of over 33 percent remained strong and stable, thanks to the cost savings and revenue optimization achieved by our value enhancement program on which we will speak more later, as well as revenues from superior product mix and differentiation. While net profit was down 19 percent from the previous quarter, the impact of lower production volumes was partially offset by improved pricing in addition to the mentioned impact of the value enhancement program. Onto the next slide.

We will now look at costs -- an area were we made already important and material progress in the first quarter. Our overall cost base declined by 12 percent as compared to Q4, a significant achievement in an operating environment that has been characterized by elevated costs, particularly for feedstock and logistics. We have been successful in reducing our selling and distribution expenses by almost 43 percent year on year respectively by 33 percent quarter on quarter, and have reduced our cost of sales by more than 9 percent as compared to Q4.

Meanwhile, other variable and fixed production costs declined 23 percent, and G&A costs by 22 percent, as compared to the previous quarter. Feedstock costs increased due to the higher market price of externally sourced propylene, and also due to the Borouge 2 turnaround, which meant we were temporarily not able to internally source propylene from cost-advantaged production by our Olefin Conversion Unit. Borouge's strong position on the cost curve is an important component that, when combined with improved premia against benchmarks, supports a strong margin profile. Going forward, our objective is to continue managing down our costs and maintaining them sustainably at lower levels, thereby taking advantage of the opportunity that will be provided by a return to full production capacity.

Sticking with efficiencies, we'll now look at our ambitious value enhancement program in more detail. As we had announced during our last earnings cycle, we have introduced a very significant Value Enhancement Program to support future growth opportunities and enhance our competitive positioning. In light of challenging market conditions, our focus is on managing conversion, logistics and fixed costs as well as revenue optimization. We expect the program to result in a net positive $400 million impact to be realized at EBITDA level for 2023, targeted to offset the impact of macroeconomic challenges and pricing pressures.

Looking further ahead, we expect to sustain a 15 percent net, positive EBITDA impact from 2024, versus our 2022 baseline. I'm pleased to report that as at the end of Q1, we have already realized a total program impact over cost and revenue elements in excess $100 million USD. We consider this is a major achievement this early our Value Enhancement Program as implementation of improvement programs usually is ramping up gradually.

In terms of where this has been realized, well over half has been realized as expected through the reduction of logistics variable costs, almost a third from revenue optimization, and the remaining from reductions to fixed costs and conversion variable costs. Particularly in the fixed cost area, the immediate measures taken early in the preparation have shown the positive effects. This has been an excellent start to our highly ambitious program, and we look forward to providing you with further updates on progress during the coming quarters.

I'll finish by discussing Capex and cash flow, before handing over to Hazeem to conclude the presentation. Cash conversion in the quarter was 82 percent versus 86 percent in the previous quarter, this due to operations expenses related to the Borouge 2 Turnaround. Our net debt stood at $3,277 million USD. In January we took the opportunity to repay $500 million USD of our commercial term facility from the excess cash at hand. This resulted in interest cost savings and we intend to further actively manage our debt portfolio and very strong balance sheet going forward. I'll now hand back to Hazeem to summarize and wrap up the presentation.

Hazeem Al Suwaidi:
Thank you, Jan-Martin. Activity in our core markets remains stronger than in developed economies. In-country demand in China, an important geography for us, is looking healthier. We continue to focus on differentiated products and markets, in particular on our energy and infrastructure solutions segment, which is demonstrating relatively more resilient pricing. We reiterate our over-the-cycle guidance of $200 per ton for PE and $140 per ton for PP, and we expect strong results from our value enhancement program to continue for the remainder of the year. From Q2 onwards, as we will return to full production capacity and maximum asset utilization, we expect to return to full production.

Before closing, I would like to take the opportunity to re-iterate our business highlights which position Borouge favorably through-the-cycle. We own and operate a young, well-maintained, and highly reliable asset base, one of the largest single-site fully integrated polyolefin production platforms in the world with a nameplate production capacity of 5 million tons per year. Our core markets are the largest and fastest growing markets globally, with robust long term demand growth. We have a strong foothold in these markets, thanks to the strength of our commercial platform and distribution network. We continue to provide high value differentiated products leveraging our direct sales network. Our technology and commercial excellence have allowed us to produce superior products which yield premium prices, and we are also focused on R&D, as seen in our dedicated, state-of-the-art Abu Dhabi Innovation Centre. Our feedstock contracts are priced competitively in the first quartile of the cost curve and run for a long-term, thereby ensuring security of supply.

We have demonstrated an ability to realize premiums over benchmark prices consistently, a key differentiator of our business . We maintain a strong cash conversion which is supported by resilient through-the-cycle margins. Before we move to the Q-and-A, I would like to say a few words about today, COO, our Chief Operation Officer announcement. I would like to thank Louis for his many contributions to Borouge and for his strong leadership and commitment toward always driving operational excellence and transformations with a 100 percent safety mindset. We will assist Hasan in a transitional capacity to ensure business continuity and a seamless transition before returning to take the role at Borealis.

And with this, I would like to also, with a pleasure, to welcome Dr. Hasan Karam, who has been confirmed as Borouge COO, effective from the 1st of May 2023. Hasan comes with 29 years of experience in senior operations roles with Adnoc and most recently managing the operations at Adnoc Refining. And with that, we will move to the Q-and-A session, please.

Operator:
Thank you. If you would like to ask a question, please press star followed by one on your telephone keypad now. If you change your mind, please press star followed by two. When preparing to ask your question, please ensure your line is unmuted locally. Again, that's star followed by one on your telephone keypad now. Our first question comes from Ricardo Rezende from Morgan Stanley. Your line is now open. Please go ahead.

Ricardo Rezende:
Hi, good morning and thanks for taking my questions. Two questions on my side, the first one, if we look at the improvement on the benchmark prices for PE and for PP during the quarter, it was a lot lower than the improvement in your premia for the product. So if you could just give us a little bit, some more color on what are the major drivers for such a relevant improvement on the premium for the first quarter? And then, on the second question, you mentioned the impact from the lower utilization of the OCU during the quarter and how that impacted costs. Would you be able to provide any color on the financial impact from the lower utilization? Thank you.

Rainer Hoefling:
I'll take up the question on pricing and then premium. So what we have seen already in the quarter four in December was that due to the fact that China was opening up the overall fundamentals the sentiment in the market that got better, so demand went up. Also, we have seen this in China with PMI index went up from 47 to 52. So which means we were facing a good demand growth in the first quarter in China, in Southeast Asia and in the GCC region it was always a good, stable growth. Then in combination right where we had a number of shutdowns seen in the Middle East regions and some unplanned shutdowns. The supply got constrained and there we could use – and the momentum, of course, then a combination to move the prices up significantly.

Due to the fact that we always said we are not a commodity player, we are a differentiated player, right. And we are able to be also tactical when it comes to our volume allocation. We took also this momentum either to increasing the prices specifically on the infrastructure segment, stronger than the commodity prices went up. And then were also able due to the fact that we were -- ourselves to the turnaround a bit constrained on the volumes. With tactically move the volumes also more into regions with higher netbacks, so Asia South and the Middle East regions. And this is how we brought the premiums higher up than the market went up. So premium went up in polyethylene and 8 percent and in polypropylene 6 percent.

So overall, I think a good achievement in quarter one in terms of prices and premium.

Louis Roland R. Desal:
Thank you, Rainer. I will take the question on the Olefin Conversion Unit. So as mentioned earlier in the call here, our Borouge 2 turnaround was one of the key activities in the first quarter. And our Olefin Conversion Unit is part of the turnaround scope. So it is belonging to the Borouge 2 complex and therefore it was not in operation during the turnaround. That brought the total utilization in the quarter to 44 percent. The unit is, of course, restarted together with the other units after the turnaround. And looking forward, we are looking at a utilization rate which will be 100 percent because we are maximizing the flexibility we have to 100 percent and running propylene production based on advantage feedstock. So that is the outlook for the rest of the year. So we are back on track with maximizing propylene from olefins. Thank you.

Operator:
And our next question comes from the line of Prateek Bhatnagar from HSBC. Prateek, your line is now open. Please go ahead.

Prateek Bhatnagar:
Yeah, thanks a lot for taking my question. I have two. So the first one is basically a follow up of the previous one. You said that the LDPE plant has started back and you've also guided to OCU unit operating at a higher elevated operating rate. So how do you get additional ethylene from it? Have you got additional ethane allocation to which, again, to which you can operate your ethylene cracker at a higher operating rate and supply more LDPE unit and OCU? So that's my first question. How do you operate both at elevated operating rates? The second question is on the China demand. You've guided to higher PMI and better margins in Q1, but at present, what kind of demand improvement are you seeing from China's opening in terms of order book and the uptick from infrastructure or real estate segment? Thanks. These are my two questions.

Rainer Hoefling:
So I'm not one hundred percent sure if I all captured that. I think that the first part was a bit about the supply demand and operating rates in the market. And the second question about how China is developing as such on the demand side and also in relation to PMI, is that what I captured?

Prateek Bhatnagar:
The first one was also on LDPE, OCU.

Rainer Hoefling:
Okay. I think Louis can take on --

Hazeem Al Suwaidi:
Just if the person can repeat the questions again, please. Just in short and in a slow manner, please.

Prateek Bhatnagar:
Sure I'll repeat. You've guided that OCU, your Olefin Conversion Unit will run at an elevated operating rate and your LDPE unit has also started back. So how do you get additional ethylene

unit – ethylene to supply both of them? Because earlier your guidance for OCU was that it will run at around 50 to 60 percent. So how do you get additional ethylene to supply both the –

Louis Roland R. Desal:
Okay, that's good.

[talking simultaneously]

Prateek Bhatnagar:
The second one is on China. Any demand uptick, do you see after China reopening at present?

Louis Roland R. Desal:
Okay, I can take the first part. So, as you know, if I start with the Olefin Conversion Unit, the Olefin Conversion Unit is one of our key assets, which gives us a lot of flexibility, anticipating – okay, is this better?

Okay, so on the Olefin Conversion Unit, our Olefin Conversion Unit is one of the key strategic assets that we have that gives us the flexibility to look at optimized utilization depending on what the pricing is of feedstock and how the market looks like. So the current view is that maximizing utilization of OCU gives us the best net profit. That's also why currently we are looking at maximizing utilization. And of course this is driven by the fact that we have excellent production of our olefin units. So we have maximized production of ethylene, which gives us the opportunity to also maximize utilization of the Olefin Conversion Unit.

Given that our PP5 plant is also performing excellent after the start of last year and ramping up to maximum capacity is also demanding this extra propylene. So that's one of the areas also why we are using our Olefin Conversion Unit maximum. When they go back to LDPE, LDPE was restarted in the first quarter, indeed. So it was restarted in the month of March and is operating at excellent rates, giving us the required base resin for XLPE [spelled phonetically] production unit, which is our most profitable wire and cable product that we have. So we are back fully on track with our LDPE/XLPE combination, which gives us, of course, a very good outlook for the rest of the year.

Rainer Hoefling:
And let me quickly elaborate a bit on China. So after China opening up and also welcoming international companies, they have seen that the PMI index or manufacturing index went up to around the 52 coming from a very low number. But you also see that the private consumer index went up to 50, 56, 57, also from a lower number. So there's following going on. I think in China, they stimulate the consumer behavior, consumer spending. What you see, I was myself in China for one and a half week now. I talked to a number of people. And what you see in China is that they start consuming again. They don't spend yet the money for luxury goods and big goods, don't buy big cars, but this will come when they gain the confidence.

But the government is doing -- they stimulate the infrastructure projects and also project towards energy transition. We, ourself, had the finalize some projects in in China recently where we were supplying material for pipes in a nuclear power plant or we were supplying material, where more than 100 kilometers of phone cable was produced for an offshore park in China, either for submarine cable. So there's a number of things going on there.

So there will be a stable growth. What is still a bit cautious on China, of course, is the export side. So in country growth will come. The export side, though, they are depending a bit also on growth opportunities in Europe and in the U.S. This will take a little bit more time. But there is a positive momentum in. We had the Chinaplast for one week and when it were three years ago, right before the pandemic, Chinaplast has seen 130,000 visitors. This time it was 250,000. So the industry -- so they invited international companies. So there is a momentum in it. We need to be a bit patient that it takes off. But the 55 percent ambition on GDP growth and polyolefin goes hand in hand with GDP, factor 1.2, 1.4 in infrastructure. We will see a good growth and this will help also have impact on Southeast Asia and in the rest of our territories.

Prateek Bhatnagar:
Thanks a lot. Very helpful.

Operator:
Our next question comes from Faisal Al Azmeh from Goldman Sachs. Faisal, your line is now open. Please go ahead.

Male Speaker:
Hi, good afternoon, everyone, and thank you for the presentation. This is Waleed from Goldman Sachs,asking on behalf of Faisal Al Azmeh. We just have a couple of questions from our end. First of all, on the Companies Value Enhancement Program, you've already mentioned that the company realized around 100 million USD in the first quarter. I was wondering if you could just give us some guidance on how you -- how should we think about the phasing of the remaining target over the second through fourth quarter of the year? That's my first question. And on the second question is on the international expansion/M&A front. Could you provide us with some updates on the areas/product that you're considering growing? That's it from my end.

Siegfried Wengler:
Yeah, hello, this is Siegfried Wengler, the vice president for Finance. Thank you for the question. I will take the first one on the value enhancement program. So as you have stated, we have communicated the delivery of the first 100 million in the first quarter. And we also reconfirm the delivery of the full 400 million over the course of the year, 2023. So that means up to date we are on track with the execution and the delivery of the benefits committed and we expect the delivery now specifically on quarter two, quarter three, and quarter four. As you can see, we are around 25 percent. So from that angle, the expectation is that similar benefits are contributed over the upcoming quarters to achieve the 400 million over the year. It's now I hand over to Hazeem for the second question.

Hazeem Sultan Al Suwaidi:
Thank you, Siegfried. I can take the second question on the international expansion. As we have communicated last time we, of course, in Borouge continue focus on our organic growth. For example, the landmark Borouge 4 project which is truly going in the right direction, the project execution is progressing quite well. Just to remind everybody, this is a 1.4 million tons of

additional capacity, which is -- a 30 percent additional capacity would be added to Borouge by 2025 as we have communicated.

We also as well as -- also communicated as well that our board has mandated us, the management, that we continue to seek and explore growth opportunities through international expansion. We are, of course, we are always open to the right opportunities provided by the value accretive to the business that has to fit within our disciplines approach to capital allocation. And it has to be also -- it has to complement our organic growth program. And of course, any expansions that would come has to come through new or existing assets will be focused on geographies and markets that support companies existing strategic priorities.

So for now, we cannot disclose the level of investments we will be committing to these activities at the present time, but our very strong cash flows and robust balance sheet both contribute to our ability to invest in growth while paying highly competitive dividends to our shareholders.

Male Speaker:
Thank you.

Operator:
As a reminder, if you would like to ask a question, please press star followed by one on your telephone keypad now. Our next question comes from Rene Selouan from Jadwa Investments. Rene, your line is now open. Please go ahead.

Rene Selouan:
Hi. Thank you for the call and the presentation. Very useful. So I wanted to ask about the cost of the turnaround. How much cost was incurred at the B2 turnaround? And second, as of April, you're saying you're operating at 100 percent. So is there any enhancement in this turnaround where we can assume higher volumes post the turnaround? And what are the planned turnarounds for '23 other than this one or '24?

Male Speaker:
This can be answered by Siegfried.

Siegfried Wengler:
Yeah, thank you for the questions on the Borouge 2 turnaround. So we -- I'm happy to confirm that we have completed the Borouge 2 turnaround on time and within budget. And from that part, the production has now resumed. And on the operating rates, I hand over to Louis.

Louis Roland R. Desal:
Yeah. So on the enhancements question, have we done any enhancements? We have -- I mean, the turnaround scope is, of course, always there to ensure that the reliability of the assets between the turnaround cycles is maximized. So if -- and that means that we have done several enhancements such as lifetime extension of systems, upgrading of systems, to secure this reliability. So we have a continuous program of reliability uplift, and that is where you can see the enhancements.

In addition to that, as part of the preparation for Borouge 4, there have been also tie-ins, so connections, future connections between the assets installed in the Borouge 2 complex to make sure that when Borouge 4 is ready for starting, that those connections are available and that we don't need to have additional stops on the assets.

So if you look at the totality of the turnaround activity, you have the specific turnaround scope. And then next to that, we have some specific projects which enable us to start Borouge 4 later with connected systems between the assets. So that is where the additional enhancements have been done with the focus on our growth based on Borouge 4.

Rene Selouan:
Okay, thanks. And would you mind sharing the cost of this turn around?

Hazeem Al Suwaidi:
So we are not disclosing the Capex for the Borouge turnaround stand alone, but as alluded by Jan-Martin earlier in the presentation on the overall capital expenditure, the costs have been fully captured in those numbers disclosed.

Rene Selouan:
Okay, thanks. And what are the [inaudible]? Sorry, I was asking about the future turnarounds, if possible, in '23 and '24.

Hazeem Al Suwaidi:
So the future turnaround today is looking such that in 2024 we have the Borouge 3 turnaround. Yeah, that is the -- this was announced earlier that the Borouge 3 turnaround is in 2024 and as we had the Borouge 1 turnaround last year in 2022, that would mean that then the next turnaround is 2026 for Borouge 1 again. So it's a -- sorry, 2027. It's a five year cycle. So the – Borouge 1 was one was last year and '22. So the next Borouge 1 is in '27 and next year we have Borouge 3 to complete the turnaround of one, two, and three.

Rene Selouan:
Okay, very clear. Thank you.

Operator:
And there are no further questions, so I'll hand the call back to the management team for any closing remarks.

Hazeem Al Suwaidi:
I would like to thank everybody for participating with us today and we are always happy to take your inquiries. Looking forward to interacting with you next time round. Thank you, everyone.

[end of transcript]