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Borouge

BOROUGE PLC – Q2 / H1 2023

Management Discussion & Analysis

28 July 2023

INSPIRING TOMORROW

1. Summary of Operational & Financial Performance

Borouge PLC (Borouge) reported Q2 2023 revenue of $1,416 million, representing a quarter-on-quarter increase of 2.5 percent, primarily due to a 4.2 percent increase in sales volume after the successful completion of the planned B2 turnaround in the previous quarter. On a year-on-year basis, Q2 revenue is down 24 percent, driven by a 25 percent reduction in average selling prices. On a half yearly basis, revenue is down 19 percent to $2,798 million in H1 2023 versus $3,460 million in H1 2022, primarily due to a 22 percent decline in average polyolefin prices during this period.

Despite a challenging pricing environment, in Q2 2023, Borouge achieved healthy premia over product benchmark price of $249 per tonne for Polyethylene (PE) and $150 per tonne for Polypropylene (PP), respectively. Premia achieved was above management's through-the-cycle guidance of $200 per tonne and $140 for tonne for PE and PP, respectively, owing to Borouge's differentiated product range and strong market positioning in key product segments.

Borouge reported Q2 2023 Adjusted EBITDA of $518 million, operating profit of $369 million, and net profit of $231 million. Net profit declined 53 percent year-on-year, primarily owing to a 25 percent decrease in average selling prices over the period, offset by a 9 percent reduction in the overall cost base (equivalent to 16 percent reduction in costs per tonne) over the period.

On a half yearly basis, operating profit is down 43 percent to $696 million in H1 2023 versus $1,229 million in the same period last year. Adjusted EBITDA is down 35 percent to $978 million, and net profit is down by 50 percent to $431 million. These declines are driven primarily by lower average selling prices during the period.

The Value Enhancement Program has contributed $253 million to EBITDA in H1 2023.

Cash conversion in Q2 2023 increased to 96 percent versus 82 percent in the previous quarter due to lower maintenance capex in Q2 2023, following the successful completion of the B2 turnaround in Q1 2023. Net debt as of 30 June 2023 is $3,167 million, versus $3,277 million as of 31 March 2023.

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
Total sales volumes (kt)	**1,206**	**1,227**	**1,157**	**2,363**	**2,328**
…Polyethylene	659	652	573	1,232	1,263
…Polypropylene	547	496	488	1,035	954
…Ethylene and others	0	79	96	96	111
Average selling price ($/t)					
…Polyethylene	1,166	1,518	1,202	1,182	1,460
…Polypropylene	1,041	1,435	1,082	1,060	1,409
Product premia ($/t)					
…Polyethylene	249	436	264	256	368
…Polypropylene	150	318	137	144	283

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
	US$MM	**US$MM**	**US$MM**	**US$MM**	**US$MM**
Revenue	**1,416**	**1,870**	**1,382**	**2,798**	**3,460**
Cost of sales	(899)	(932)	(914)	(1,813)	(1,800)
Gross profit	**517**	**937**	**467**	**984**	**1,659**
General and administrative expenses (excluding D&A)	(49)	(31)	(46)	(95)	(71)
Selling & distribution expense	(105)	(188)	(100)	(204)	(362)
Other income and expenses	5	1	5	10	3
Operating profit	**369**	**719**	**327**	**696**	**1,229**
Profit for the period	**231**	**490**	**199**	**431**	**853**
Profit margin (%)	*16%*	*26%*	*14%*	*15%*	*25%*

Total comprehensive income for the period	226	485	201	427	848
Adjusted EBITDA(1)	**518**	**868**	**460**	**978**	**1,512**
Adjusted EBITDA margin (%)	*37%*	*46%*	*33%*	*35%*	*44%*
Basic earnings per share (US$)	0.01	0.02	0.01	0.01	0.03
Diluted earnings per share (US$)	0.01	0.02	0.01	0.01	0.03
Net debt	3,167	3,543	3,277	3,167	3,543

(1) Adjusted EBITDA is calculated as EBITDA plus adjustments on foreign exchange gain or loss and impairment loss on property, plant and equipment.

2. Operational Review

In Q2 2023, production resumed at very high utilisation rates of 110 percent and 99 percent for PE and PP, respectively, following the successful completion of the B2 turnaround in Q1 2023. Resultantly, sales volumes picked up by 4 percent on a quarter-on-quarter basis.

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
Production capacity (kt)	**1,242**	**1,242**	**1,228**	**2,470**	**2,470**
…Polyethylene	686	686	678	1,364	1,364
…Polypropylene	556	556	550	1,106	1,106
Utilisation rate					
…Polyethylene	110%	92%	78%	94%	87%
…Polypropylene	99%	87%	81%	90%	85%

The Olefin Conversion Unit (OCU), which allows Borouge to internally produce large amounts of propylene from ethylene also operated at a high utilization rate in Q2. Ethylene is typically prioritized for use in maximizing PE production and the additional quantities are sent to the OCU.

3. Revenue & Pricing

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
Sales volumes by product (kt)					
…Polyethylene	659	652	573	1,232	1,263
…Polypropylene	547	496	488	1,035	954
…Ethylene and others	0	79	96	96	111
Polyethylene (US$ / t)					
…Average sales prices	1,166	1,518	1,202	1,182	1,460
…Premia	249	436	264	256	368
...Benchmark	916	1,082	938	926	1,092
Polypropylene (US$ / t)					
…Average sales prices	1,041	1,435	1,082	1,060	1,409
…Premia	150	318	137	144	283
…Benchmark	891	1,117	945	916	1,126

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
Revenue by product	**(US$MM)**	**(US$MM)**	**(US$MM)**	**(US$MM)**	**(US$MM)**
…Polyethylene	820	1,049	758	1,578	1,953
…Polypropylene	591	734	555	1,145	1,386
…Ethylene and others	5	87	69	74	121
Total revenues	**1,416**	**1,871**	**1,382**	**2,798**	**3,461**

(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 2023 sales volumes are up by 4.2 percent versus the prior quarter, mainly due to the resumption of production following the B2 the successful completion of the planned Borouge 2 Turnaround. Sales volumes from energy & infrastructure solutions represent c.40 percent of polyolefin sales volumes in the second quarter. This is part of Borouge's strategy to focus on durable products for industrial applications. Specifically, sales volumes of PE100, a key premium product used in infrastructure applications, have contributed positively to the overall sales mix outcome. The Asia Pacific market continues to be the largest destination for polyolefin sales with 66 percent of total polyolefin sales volumes followed by the Middle East and Africa with 27 percent of total polyolefin sales volumes.

On a year-on-year basis, blended average selling prices across PE and PP were down 25 percent from the exceptionally high prices achieved in Q2 2022. On a sequential quarter-on-quarter basis, prices were down 3 percent.

Despite a challenging pricing environment, Borouge was able to command high premia over benchmark prices, reflecting Borouge's strong market positioning in key market segments. Premia for PE and PP were $249 per tonne (down 6 percent Q-o-Q basis) and $150 per tonne (up 9 percent Q-o-Q basis), respectively.

Segmental revenue breakdown (includes polyolefins and olefins)

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
By product group					
…Polyethylene	58%	56%	55%	56%	56%
…Polypropylene	42%	39%	40%	41%	40%
…Ethylene and others	0%	5%	5%	3%	4%
By end market					
…Consumer solutions	52%	48%	45%	49%	48%
…Infrastructure solutions	45%	45%	48%	46%	46%
…Other	3%	6%	7%	5%	6%
By geography					
…Asia Pacific	65%	57%	59%	62%	57%
…Middle East & Africa	28%	32%	29%	29%	32%
…Rest of World	6%	7%	7%	7%	7%
…Ethylene & others	0%	5%	5%	3%	3%

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

Segmental volume breakdown (includes polyolefins and olefins)

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
By product group					
…Polyethylene	55%	53%	50%	52%	54%
…Polypropylene	45%	40%	42%	44%	41%
…Ethylene and others	0%	6%	8%	4%	5%
By end market					
…Consumer solutions	58%	50%	49%	53%	50%
…Infrastructure solutions	40%	42%	41%	40%	44%
…Other	2%	8%	10%	6%	7%
By geography					
…Asia Pacific	66%	57%	56%	61%	58%
…Middle East & Africa	27%	30%	28%	28%	30%
…Rest of World	7%	6%	7%	7%	7%
…Ethylene & others	0%	6%	8%	4%	5%

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

4. Costs

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
	US$MM	**US$MM**	**US$MM**	**US$MM**	**US$MM**
Revenue	**1,416**	**1,870**	**1,382**	**2,798**	**3,460**
Cost of sales (excluding D&A)	(750)	(792)	(781)	(1,531)	(1,528)
…Feedstock costs	(324)	(320)	(375)	(699)	(593)
…Other variable and fixed production costs	(426)	(472)	(406)	(832)	(935)
…as % of revenue	*53%*	*42%*	*57%*	*55%*	*44%*
General and administrative expenses (excluding D&A)	(49)	(31)	(46)	(95)	(71)
…as % of revenue	3%	2%	3%	3%	2%
Selling and distribution expenses	(105)	(188)	(100)	(204)	(362)
…as % of revenue	*7%*	*10%*	*7%*	*7%*	*11%*
Other income and expenses	5	1	5	10	3
Depreciation and amortization	(149)	(141)	(133)	(282)	(272)
Operating profit	**369**	**719**	**327**	**696**	**1,229**
…as % of revenue	*26%*	*38%*	*24%*	*25%*	*36%*

The Value Enhancement Program continues to perform strongly, achieving a $253 million EBITDA impact in H1 2023, comprising an approximate 70/30 split between cost efficiencies and revenue enhancement, respectively. The overall cost base in Q2 is down 9 percent year-on-year and down 1 percent quarter-on-quarter. Total cost per tonne in Q2 2023 are down 16 percent year-on-year and 18 percent quarter-on-quarter. Cost of Sales are down 5 percent year-on-year and 4 percent quarter-on-quarter, supported by a 14 percent decrease in feedstock costs.

General and admin expenses increased by 56 percent from $31 million to $49 million on a year-on-year basis due to non-recurring one-off items such as bad debt provisions. Selling and distribution expenses in Q2 2023 are down by 44 percent year-on-year primarily due to significant decreases in freight costs versus the same period last year.

5. Cash Generation

	Three Months Ended			Six Months Ended	
	30 June 2023	30 June 2022	31 March 2023	30 June 2023	30 June 2022
	US$MM	**US$MM**	**US$MM**	**US$MM**	**US$MM**
Profit for the period	231	490	199	431	853
Income tax expense	88	212	84	172	347
Net finance loss, including foreign exchange loss	49	17	44	93	29
Depreciation of property, plant, and equipment	139	135	126	265	259
Depreciation of right-of-use assets	10	0.4	6	15	2
Amortisation of intangible assets	1	5	1	2	11
Impairment loss on property, plant & equipment	-	8	-	-	10
Adjusted EBITDA (1)	**518**	**868**	**460**	**978**	**1,512**

Capital expenditure (2)	22	(44)	83	105	84
Adjusted operating free cash flow (3)	496	912	378	873	1,428
Cash conversion (%)	*96%*	*105%*	*82%*	*89%*	*94%*

(1) Adjusted EBITDA is calculated as EBITDA plus adjustments on foreign exchange gain or loss and impairment loss on property, plant and equipment.
(2) Capital expenditure is calculated as additions to property, plant and equipment for the period.
(3) Adjusted Operating Free Cash Flow is calculated as Adjusted EBITDA less capital expenditure.

Adjusted EBITDA in Q2 2023 increased by 13 percent to $518 million versus the prior quarter, reflecting the increased sales volumes and the positive impact of the Value Enhancement Program. On a half yearly basis, adjusted EBITDA is down by 35 percent to $978 million reflecting a decrease in the top line due to the challenging overall pricing environment.

Borouge generated $496 million of adjusted operating free cashflow during the second quarter at a conversion rate of 96 percent versus 82 percent in the previous quarter due to lower maintenance related capex in the period in Q2 2023 following the completion of the turnaround activities in the previous quarter.

6. Current Trading & Outlook

The outlook for polyolefins in the remainder of 2023 remains cautious and market analysts anticipate a narrow band of price volatility during this period. Market analysts expect a soft pricing environment in Asia to remain, resulting from new polyolefin production capacities coming online and until the delayed recovery in China and Asian demand materializes.

Borouge Management re-affirms the existing through-the-cycle premia guidance for PE and PP of $200 per tonne and $140 per tonne, respectively.

Management expects production volumes to remain strong and focused on more differentiated products. Borouge's core strategy of developing innovative products continues to support our premium pricing.

Within our cost base, ethane costs will remain essentially fixed under our long-term pricing agreement with ADNOC, which provides us with significant long-term feedstock security, a key competitive advantage. Propylene costs, which broadly track oil prices, remain elevated. We anticipate continuing to run our OCU at high rates in the coming quarter, generating cost effective propylene feedstock for PP production. We also anticipate strong progress to continue to be made on the Value Enhancement Program during the remainder of the year.

Management reiterates its commitment to pay $1.3 billion in dividends for the Financial Year 2023. In relation to H1 2023, the Board has endorsed an interim dividend of $650 million to be approved by shareholders during the second half of 2023.

The Company will announce its Q3 2023 results on 31 October 2023.