

Lotte Chemical Titan Holding Bhd

TP: RM1.64 (-18.0%)

Boosted by Cheap Feedstock and Pent-Up Demand

Last Traded: RM2.00

SELL

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Review

- Lotte Chemical Titan Holding Bhd's (TTNP) reported a core net loss of RM129mn (1H19: RM82mn profit) for 1H20. The results performance was above our expectation but below consensus' forecasts. The variance versus our forecast was due to higher-than-expected volumes and reversal of write-down of inventories of RM102mn (1Q20: RM81mn).
- QoQ turnaround was mainly driven by: (1) recovery in volumes (+28%) and plant utilization (PU), (2) reversal of inventories write-down, and (3) improved product spreads due to the plunge in naphtha feedstock prices (-23%). To a lesser extent, narrowed associate losses from LC USA propped up the bottomline as well. The above more than offset the sustained drop in Average Selling Prices (ASP).
- TTNP achieved record volumes in May-June as customers restarted operations and replenished inventories. Nevertheless, moving forward, management guided that volumes will normalize in 2H20.
- PU jumped to 86% in 2Q20 (1Q20: 66%) following completion of major TA exercises in early-April and some minor TA in June. For the remainder of FY20, there will be one last additional TA at Cracker 1 (capacity: 430k tpa) in July for 30 days. Nevertheless, management retained its guidance of 85% PU in FY20.
- Despite operating at close to full capacity, LC USA slipped to operational losses in 2Q20. This was due to compressed spreads caused by the surge in ethane gas feedstock cost. On the bright side, total losses reduced QoQ as 1Q20 was dragged by loss on interest rate swaps.
- 1H20 losses was attributed to: (1) lower ASP, (2) decreased sales volumes, (3) associate losses almost doubled due to weakness at LC USA, and (4) plant start-up costs recognized in 2Q20 following completion of TA exercises.
- 1H20 volumes were lower (-11%) due to: (1) lower production as a result of plant TA activities in 1Q20, and (2) weaker demand as operations at TTNP's main customers were affected by Covid-19 (C-19) lockdowns.

Impact

- We raise FY20 sales volumes by 10% and reduce inventory costs by circa 25% to reflect actual 2Q20 results. As a result, our FY20 earnings forecast is revised to RM10mn (previous: RM47mn loss).

Outlook

- Whilst TTNP benefitted from lower naphtha feedstock price (-23% QoQ) in 2Q20, we do not expect this to recur in 2H20. This is on the back of stronger crude price (current: USD44/bbl, 2Q20: USD32/bbl) as a result of

Share Information

Bloomberg Code	TTNP MK
Stock Code	5284
Listing	Main Market
Share Cap (mn)	2,273
Market Cap (RMmn)	4,546
52-wk Hi/Lo (RM)	2.85/0.98
12-mth Avg Daily Vol ('000 shrs)	5,402.0
Estimated Free Float (%)	12.0
Beta	1.6
Major Shareholders (%)	Lotte Group - 76%
	EPF- 4.1%

Forecast Revision (%)

	FY20	FY21
Forecast Revision (%)	>-100	0
Core Net Profit (RM mn)	9.6	227.7
Consensus	151.3	283.2
TA/Consensus (%)	6.3	80.4
Previous Rating	Sell (Maintained)	

Scorecard

	% of FY	
vs TA	nm	Above
vs Consensus	nm	Below

Financial Indicators

	FY20	FY21
Net Debt/Equity (x)	Net Cash	Net Cash
ROA (%)	0.1	1.6
ROE (%)	0.1	1.9
NTA/Share (RM)	5.3	5.4
P/NTA (x)	0.4	0.4

Share Performance

Price Change (%)	TTNP	FBMKLCI
1 mth	12.4	6.8
3 mth	17.6	13.9
6 mth	(10.3)	3.8
12 mth	(29.6)	(2.4)

(12-Mth) Share Price relative to the FBMKLCI



Source: Bloomberg

expected inventory drawdowns in 2H20. Moreover, as per management's guidance, record volumes in May-June 2020 will normalize in upcoming quarters.

- According to EIA, global inventories rose at a rate of 6.7mn bpd in 1H20. This is expected to reverse to 3.3mn bpd of drawdowns in 2H20. Thus, this will likely eliminate most surplus inventories that accumulated in early 2020.
- The current oversupply of polymers in Asia is expected to exacerbate in 2020-22. This is underpinned by sizeable recent new capacity, including: (1) Zhejiang Petrochemical (1st phase): one line of 450k tpa HDPE/LLDPE swing plant, HDPE (300k tpa), and PP (900k tpa), (2) Hengli Petrochemical: PP (430k tpa), and HDPE (400k tpa), and (3) Petronas Chemicals: LLDPE (350k tpa), PP (900k tpa), and HDPE (400k tpa).
- Due to economic headwinds emanating from C-19, TTNP is undertaking a strategic review on the project timing and progress of its new Lotte Chemical Indonesia New Ethylene (LINE) Project (stake: 51%).

Valuation

- Our target price of RM1.64 is based on unchanged 2.5x CY21 EV/EBITDA. Maintain Sell.

Figure 1: Quarterly Results Analysis

YE 31 Dec (RM mn)							Cumulative	
	2Q20	1Q20	QoQ	2Q19	YoY	1H20	1H19	YoY
Revenue	1,576.3	1,461.8	7.8	2,127.2	(25.9)	3,038.1	4,297.2	(29.3)
EBITDA	262.0	(104.5)	>-100	230.5	13.6	157.5	446.9	(64.8)
Depreciation	(142.5)	(134.7)	5.8	(155.5)	(8.4)	(277.2)	(311.8)	(11.1)
Finance Costs	14.8	19.9	(25.7)	22.6	(34.8)	34.6	44.5	(22.3)
Associates	(24.8)	(35.1)	(29.3)	(18.1)	37.4	(59.9)	(31.5)	90.3
EI	(0.1)	48.6	>-100	58.6	>-100	48.5	79.2	(38.8)
Pretax Profit	109.2	(205.8)	>-100	138.2	(21.0)	(96.6)	227.3	>-100
Taxation	(13.4)	36.3	>-100	(33.2)	(59.8)	22.9	(66.5)	>-100
Minority Interest	(7.2)	0.6	>-100	(0.1)	>100	(6.6)	(0.1)	>100
Reported Net Profit	88.7	(168.9)	>-100	104.8	(15.4)	(80.2)	160.7	>-100
Core Net Profit	88.9	(217.5)	>-100	46.2	92.3	(128.7)	81.5	>-100
Core EPS (sen)	3.9	(9.6)	>-100	2.0	92.2	(5.7)	3.6	>-100
DPS (sen)	-	-	-	-	-	-	-	-
EBITDA Margin	17%	-7%		11%		5%	10%	
Core Net Margin	6%	-15%		2%		-4%	2%	

Figure 2: Quarterly Segmental Analysis

YE 31 Dec (RM mn)	2Q20	1Q20	2Q19	QoQ%	YoY%	1H20	1H19	YoY%
Revenue								
Olefins & Derivatives	269.9	1,022.2	487.3	(73.6)	(44.6)	1,292.2	922.9	40.0
Polyolefins	1,306.3	1,215.0	1,639.8	7.5	(20.3)	2,521.4	3,374.3	(25.3)
Eliminations	0.0	(775.4)	0.0	nm	nm	(775.4)	0.0	nm
Group	1,576.3	1,461.8	2,127.2	7.8	(25.9)	3,038.1	4,297.2	(29.3)
PBT								
Olefins & Derivatives	29.9	(130.8)	(7.3)	>-100	>-100	(100.9)	8.9	>-100
Polyolefins	155.8	(127.9)	117.2	>-100	33.0	28.0	214.4	(87.0)
Eliminations	(76.5)	52.9	28.3	>-100	>-100	(23.6)	4.0	>-100
Group	109.2	(205.8)	138.2	>-100	(21.0)	(96.6)	227.3	>-100
PBT margin								
Olefins & Derivatives	11%	-13%	-1%			-8%	1%	
Polyolefins	12%	-11%	7%			1%	6%	
Group	7%	-14%	6%			-3%	5%	

Figure 3: Earnings Summary

FYE Dec (RM mn)	2018	2019	2020E	2021F	2022F
Revenue	9,244.7	8,438.0	5,880.7	6,768.9	7,572.4
EBITDA	1,116.0	763.6	609.4	904.4	908.2
EBITDA margin (%)	12.1	9.1	10.4	13.4	12.0
Pretax Profit	764.0	503.3	70.6	269.6	327.8
Reported Net Profit	697.9	439.7	58.0	227.7	276.8
Core Net Profit	639.1	312.2	9.6	227.7	276.8
Core EPS (sen)	31.7	13.7	0.4	10.0	12.2
Core EPS growth (%)	(42.4)	(56.6)	(96.9)	>100	21.6
PER (x)	6.3	14.6	475.4	20.0	16.4
DPS (sen)	17.0	17.0	0.0	1.0	1.0
Dividend Yield (%)	8.5	8.5	0.0	0.5	0.5

Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.
HOLD : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.
SELL : Total return is lower than the required rate of return.
Not Rated: The company is not under coverage. The report is for information only.

Total Return is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

Required Rate of Return of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

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As of Monday, August 03, 2020, the analyst Kylie Chan Sze Zan who prepared this report, has interest in the following securities covered in this report:
 (a) nil

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