Advanced Petrochemical Company

1Q24 Earnings Call Transcript

Thank you very much Iyad and SNB Capital team for hosting this Earnings Call. Ladies and gentlemen, my name is Mohammed, and I would like to welcome you to Advanced Petrochemical Company earnings call for the first quarter of Please note this call is recorded and will be published into APC's website at advancedpetrochem.com. Before we proceed, I need to read the following statement: “Statements or comments made on this conference call may be forward-looking statements. Forward – looking statements may include but are not necessarily limited to financial projections or other statements of the company’s plans, objectives, expectations, or intentions. These matters involve certain risks and uncertainties. The Company’s actual results may differ significantly from those projected or suggested and any forward-looking statements due to variety of factors which are announced and uploaded in the Saudi Exchange website.” Today’s call will be led by APC President & CEO, Mr. Fahad Al-Matrafi, and joined by the CFO, Mr. Abdulaziz Al-Ardhi. At Advanced, we are dedicated to enhancing relationships with all stakeholders by upholding our vision, mission, and values. As you know, Advanced has been in the business of manufacturing and selling of polypropylene since and its facility is in Jubail Industrial City, Saudi Arabia. For today’s call, we will start with ESG & Responsible Care update. Followed by company performance highlights. Then we will share updates about our projects and growth plans. Lastly, we will have an open Q&A session to address all of your questions. For the first item of today’s agenda, we handover the mic to our CEO, Mr. Fahad. Fahad: Thank you Muhammad and I would like to again welcome all the audience and thank you for hosting this earning call. Just to give a brief introduction, this might be the first time we are presenting or sharing a presentation. I believe my colleagues here they are trying to really adapt the best practice by bringing a new approach which is very much supporting and just to divide you know the presentation into different segmentation, one part is by the IR, and one part by me, and one part by the CFO, but eventually once we are done you will be most welcome to ask any question and we'll have our usual Q&A and interactions together. Just to touch base on the ESG and Responsible Care - Alhamdulillah - we have completed million safe man hour without any lost time injury. As you know in first quarter we had our major turnaround - Alhamdulillah - it was completed safely without any issue, despite of the peak of really workers we have has reached to almost workers during a peak time during you know maintenance activity, but eventually I think it was - Alhamdulillah - managed very well from safety and environmental point of view. In fact, we have we have recycled almost % of our waste which is something always we are aiming to do more by exploring ways and means along with the Royal Commission and other you know companies to recycle the waste. Also, we have a zero noncompliance to any regulatory requirements, which is something that we are proud, and we value as we go. I think Muhammad you will take us for next slide. Mohammed: For the company’s financial performance, we handover the mic to our CFO, Mr. Abdulaziz. Abdulaziz: Thank you Mohammed, and we welcome everyone joined us today. I'm glad to meet with you and discuss our latest financial results that we have announced for quarter one as you know that we have recorded Net Losses of around million compared to million for quarter four and around million compared to similar quarter of last year. Mainly due to reduction the sales volume around % % resulted from conducting the turnaround for in quarter one, as well as the increase in SK Advanced losses of around million that resulted from the reduction in the spread in SK Advanced as well as having the turnaround for SK Advanced plant and Ulsan Polypropylene, and this result impacted and link with the performance of - we can say - most of the petrochemicals impacting by the results starting - we can say - quarter four then this continue with us in as well as in quarter one Of course, after completing the turnaround, we expect the results will be improved in : quarter two, quarter three, and quarter four, but we are working together internally with the management to implement so many programs to optimize the cost for the company. Moving to the next slide, Mohammad. This reduction in the sales volume and sales price impacted our Revenue, Gross Profit and Net Profit, as I mentioned in the previous slide, and we can see compared to all the quarters in And here as we can see that our balance sheet in Qand the Qour asset - we can say - increased due to the assets under construction for APOC, and InshAllah we will have strong balance sheet we can see after APOC start commercial operation which will improve the profitability for Advance overall. And this is the results for SK Advanced and also Ulsan Polypropylene as I mentioned in the previous slide. Their results have been impacted by the reduction in the spread, as well as having the turnaround in quarter one. Just to share with you uh the progress on the and the PDH-PP plants (APOC project), Alhamdulillah, we have reached around % as a progress. Already we are into a pre-commissioning activities, already started in fact the pre-commissioning activities in some of the systems in terms of blowing, flushing, making some system ready especially, in addition to electricity is the cooling water system and the other utility systems, boiler will be fired by hopefully in June time - in the first days two weeks - from now. We had you know a plan with Samsung on the right time because we need just to look for integration also with Technomint on the other side for a Readiness of a common utility system together that's why there was a bit a couple of weeks delay in in firing but this will not impact the overall schedule uh this will be helping to for blowing of the steam you know uh system and also other require system um also in the same time we are we are bushing uh on you know uh completing other operational and maintenance activity Readiness uh hand on hand with Technomint and Samsung uh trying also to set up a plan control room almost ready now will be ready Insha’Allah soon already the council uh AR and under erection it will be ready soon so uh in the coming months uh you know functional test and L test will be will be started uh and we will be ready InshAllah for the startup um we are we are you know getting very close I believe now working with Samsung and Technomint to make the seamless startup and pre commissioning activity without a major issues InshAllah uh most of the utilities even from the EXT external resources are ready lined up uh and we are I think moving in the right direction so basically the second half of the year will be real ready for startup to make sure and startup to make sure things are moving in the right direction there are with some you know challenges here and there but I think that team they are really putting a lot of effort to pressure trying to move InshAllah within the end of the year in the second half for both uh B and baby for IPA as you know that already cup meeting in fact already started uh contract you know it has been awarded in the month of February this year moving in in the right direction so we are expecting inshallah to be ready for commissioning as a planned by end of uh we are working in in different aspect in terms of you know preparing other you know marketing agreements and other aspect which we have a good time to work at already in fact we have um a potential of takers and part of them is in fact is our of taker or hour of takers they are they ready and they are willing because they are marketing the same product so things are moving inshallah in the right direction regarding the Methan project as you know that we have signed with SH and we are closely uh working with the with the foreign investor uh we have we had in fact our team they had several discussion on the J discussions um and they have really completed a very high percentage terms of our progress and the key terms and condition almost there hopefully third quarter should be this is our internal Target even with the foreign partner to get it done and complete it B so we are moving this aspect so no I mean issue as such um yeah next for the cracker project uh as we have discussed last time uh it is under uh configuration with a consultant and we are just waiting we have we start to receive in fact you know a short list of the products which we are reviewing in in fact next week we're supposed to have a meeting with the Consultants to review a short listed products so uh basically once we complete the configuration because this will be an input to the financial model as well so this will give us Clarity on what would be the potential project and the action itself and the financial model so we we'll have a better understanding on the also the estimated CICS and you know bath forward the cracker people compounding we are working closely also uh with the with the ministry you know to facilitate some of the you know coordination with a potential for partner on this aspect so we are also getting closer hopefully with the support of the ministry we can work out something on the B compounding uh and we are evaluating as we go uh how the discussion will move since now the ministry is supporting in that that aspect uh this in brief I believe just to touch base on and I think in more organized manner compared to what we used to it was just you know a verbal update I think I think trying to enhance our IR and trying to bring a material that would be shared. I believe also my colleagues will put this material on the website so it can be a reference if you'd like to look at it and we are always welcoming if any comments or any feedback so by this we would like to leave the floor to you if you have any questions and we are ready to answer. Thank you, Mr. Fahad. Ladies and gentlemen, we will start now the Q&A session if you wish to ask a question, please raise your hand or type in the Q&A box.

**Based on my rough calculation, I think you might have capital work in progress, 8 billion+ right now. So, we just wanted to understand how much it could be transferred when the PP commercial production starts. So, we just want to understand how much or will it be like a significant amount of this will be transferred to PP and E and then potential depreciation amount and also the borrowing cost. What could be the expected borrowing cost and depreciation amount will be charged to the P&L during the second-half.**

I think first question was about how much cost will be transferred from capital work in progress to PP and E once we start to capitalize the plant. We have basically three units, we have PDH, we have PP, and we have the IPA. So, IPA at the end of the year will still be under construction. So, we will capitalize PDH, PP plus utility portion plus build portion basically. So, we can serve almost between $2.5 billion to $2.6 billion will be capitalized. It will be part of PP and E when we start commercial operations. Now depreciation, how much would be depreciation, we can see say based on equipment which will be different. It is between 300 million rial to 350 million rial will be additional depreciation when we start commercial operations. For interest costs again it depends on the interest rates because the expected interest rates to come down. But if you assume today's interest rate, it will between 350 million rial to 400 million rial annual interest cost, but we expect this to be coming down because of two reasons. One is interest rate are expected to come down in the next few months and plus once we start making the repayments, the costs will come down.

Yesterday I believe it was announced by the central bank, a reduction of 25 basis points and also Europe, they might follow and I think the decision would be made today or tomorrow. And the expectation also from local banks that by the end of the quarter, there will be a potential reduction of interest rates. At the same time, you know the impact will be after the commercial operations, which will be sometimes towards the end of the year. We can say 100 basis points will impact 50 million rial interest costs, so we expect that there will be some good interest rate reductions next few months, when we start commercial operations, which will reduce interest costs for us. I think commercial operations can definitely save the financial statements in terms of revenue, cost, profitability as well as balance sheets.

**My second question, I just want to understand the strategic holding of Tasnee. First quarter, you had a nice boost from the market, of course, you recorded in the comprehensive income around 50 million gain. But now it seems like you wiped off that gain right now, it came down sharply again. So, what is your strategy on the Tasnee holding? Will it be utilized to funding the future project?**

Basically, for Tasnee, as you know, as we mentioned, definitely it is an option that is available also to finance our projects in the pipeline. But we need to see, and we need to evaluate from time to time once we have at least an appreciation in the share price and to a certain level, where we can really make the right decision in the right time. We're reviewing with our board a regular base and definitely the decisions will be made timely in the right time. So definitely, it is part of our radar.

screen that we evaluate when to offload and at what the price it will sell. So, it is an option that is available, but we need to select and to make the right decision in the right time.

You mentioned that we have around a comprehensive income or profits more than 53, there's no indication for that we can say real profits, while this represents only the movement in the share price of Tasnee.

**Considering the current prices and margin levels, maybe your projections previously estimate a higher level of prices could be maybe break-even point within maybe a couple of quarters, but what is your expectation right now to break even this additional unit given the current prices and the higher expenditure on especially depreciation and borrowing costs?**

We know its on the lower side and we expect the prices to be improved in next few quarters. But if you even take today's numbers, I'm sure it will more than break even. We have good contribution margins here and we expect that the prices will be further improved on the 2025 payments. I think the most important thing from our side, is to make sure that we capitalize as much as we can produce with our number of units. The market is the market, you know, we can't impact the market. Our job is to make sure we produce as much as we can produce. We should convert as much propane available to polypropylene and flow to the market. Basically, this is our job.

This is one of the key objectives and tasks that Advanced is now working close with off takers and with other potential direct converters to be ready for the new volume family in the pipeline.

**In terms of new plant, I just wanted to get an idea if I'm thinking about this in the right way. So, you've already spent roughly in the total CapEx since 2021, you've already spent close to 8 billion rials, 7.8 billion. And in your CapEx commitments, you've already have close to 2.78 billion. So, if you even remove your maintenance CapEx, if we even think I think about 600 million rials, your new plan comes close to 10 million rial, which is like way higher than announced cost Of 6.67. So, am I right in this or is there something that I’m missing?**

**If you can comment on how the plant operations in the Asian territory considering current spreads? Are you seeing any closures or and what is the strategy for SK advanced? Or how long are they planning to continue running the plant at, you know, this negative impact?**

If you recall whatever we have announced at that time was not as we are doing right now, and we did answer it several times. Just to refresh on the same point, what we have announced, the capacity was 750 and what we're working right now is 843. This one, when I spoke second aspect, the infrastructure was not included at that time, the infrastructure even for the cracker project. So, we had a site in Jubail 2. It was decided to go and build the infrastructure or to make it ready. That would be to cater for the cracker project. So, it would be cheaper for us to do this time rather than to wait for the next time.

Second point, IPA was not part of it at that time which we have also added. Fourth point, also OSPL, you know it was not part. OSPL was not part of an EPC, it was out. So, the announced EPC if you recall on April 2021, it was excluded in OSPL and after two months from the announcement, there

was an escalation under construction cost. And we have heard about, you know, some projects, almost 30% there was an escalation in the projects, so we came in the right time to the market. So, there was an exposure in the OSPL and in terms of an escalation on the prices, but this is compared to the main bulk, which is the PDH and PPC and also, we talk about almost 1.6 billion U.S. dollar. I think this is less compared to the major. Just to have a good reference and benchmark, if you could see the recently announced project, you will see how much is the difference and exactly cost per ton as of today and with the capacity, you will see a major difference. So, these are these factors creating the difference between what we have announced at that time versus what we undertook. The commitment number announced in 2024 is 2.7 billion rials including IPA of 7 billion rials. So, remove IPA out of it and we're talking about 2 billion. So basically currently spending plus 2 billion, this is number I gave you 2.52/2.56 billion. This is line with what we have said just now.

**So you mentioned that this also includes the CapEx for the cracker project. Can you comment how much that would be like if you can give us an idea?**

It's an infrastructure, you know, for instance, you know, for the cool water system. You know, systems that you just need to plug and play, you would need to expand and start. You don't need to really go for excavations and putting in new systems under the ground. So, we thought let's just cover it and just to give you an example for the boilers. We have in a plant now for boilers and we have left a space and with whatever facilities, but even foundation already just to put the boiler and to hook up and to connect. So, no need to put cables or lines. Everything is good. And this will be charged at a later stage for the whole site. So, at that time, we did sort of an evaluation, if we needed to do it at that time when we made the decisions versus to do it at a later stage. I think it would be much cheaper to do it one time rather than to take it to two phases and the site is one. So, if you need to do a building, do it one time, it doesn't matter sense to do it twice.

**If you could just comment on the SK advanced question also, please.**

This is one of the hot topics that eventually we're discussing with our board. I believe, we have explored all options that will really minimize the impact and also to triangulate and minimize any losses. Definitely if there's any material development in that aspect, it will be disclosed. As we speak, we have a detailed deep dive evaluation with all shareholders, not only SK Advanced shareholders, but SK Gas and also UBB as well. One of the actions that we have assigned, we have requested them to assign a consultant to really help in turn around the performance of SK Advanced and UBB. I believe we could do a lot. Honestly speaking, we are working with them closely, to optimize even the propane cost by exploring you know, MB and CB in an optimal manner. I think we have progressed very well, and this is despite of the losses. There are a lot of efforts being done, which could be even more just to minimize the market impact, by also optimizing cheaper source for propane, besides also exploring a new PP, different markets. Already there was an agreement and already started to perform what they call an operational advisory committee, which will review details of the sales of production plans and the sales by region trying to push for high net pack. So collectively, I believe there was a good result to minimize the losses. Otherwise, it could have been even higher.

The second part, it's not a secret. I think you might have heard about, there was an announcement, I think the 17th May that the South Korean government were trying to restructure, to come up with a restructured approach to help the pet-chem industry in South Korea. Some of them they start to close and some of them they start to sell assets. I think the government have announced they will step in to bring sort of a program which we are waiting for. They have formed a taskforce committee just to look after what could be the potential approach to really help with the pet-chem industry in South Korea. A representation from the pet-chem industry in South Korea, as well as supported by a technical adviser KPMG, to help them with this activity and this has been the announcement that they are expecting to complete this exercise by end of June this month, and by early July sometime in July they will announce their plan. So, this is also another point that we are counting on. We had a meeting on 26th May with the shareholders. We have discussed in addition to whatever optimization plan and other issues regarding the losses of SK Advanced is this program. So, it is in our radar screen, and we are looking after, and hopefully we can hear something positive in a way to support SK Advanced and UBB. So, we're waiting to hear end of June, early July, to hear the outcome. As explained by our CEO and communicated by our chairman by end of Q4 2023, that the shareholders currently working together to minimize the losses and we agreed a certain action to be executed in 2024. But as you mentioned, 2024 SK Advanced and UBB will be at their turn around which you can say, requires for more time to see the result of this action plan. We expect Q3, Q4 to see the further impact of these actions capitalized and the consultant efforts as well as the Korean government support since they are going to have to communicate short term support and long term as mentioned by the CEO, but we are working closely with the shareholder to minimize the losses.

**How many tons of polypropylene did you sell in Q1 and what is the plan in terms of the new project? How many tons do you expect to sell from the new project this year?**

Okay, see in Q1, I'm not sure whether I will be able to disclose exactly how many tons to be honest but, at least half of what we used to sell, at least half in Q1. For the new plant as you know Alex, we had the target in our business plan, ok, for the new plant, yet subject to, we will pass through a certain test to be done through a license or a lender test. This would also be timing the startup when it will be exactly, so we cannot confirm a number as such. This is the issue. But as we speak, we have a solid number in our business, anticipating that startup in a certain date. But we cannot disclose it because it might really mislead, this is the point.

**In China, do you have any plans or insights about Chinese growth and capacity and commentary on this impact on polypropylene prices?**

I mean, you know the announced capacities in China especially in polypropylene in the last two years the volumes that we have seen it vary from five to seven million tons in annual base. Yet, you know, the Chinese they are moving, but what we can see and what we heard from the market, I believe 2024, they might expect also about a five million tons in this year. Next year I think it will be way less next year, but one thing that at least based on the available data and information, Chinese, nobody knows how they will act and how they will move especially the expansion. Yet, also one thing more, a lot of plants are really struggling in China, and they are they are really burning cash.

They are making a negative contribution margin, and some of them running with 60% capacity utilization, 50% capacity utilization.

And we have seen, you know, this is I'm talking about the PDH producers. Imagine for the cracker propylene production, they will suffer even more. So, this might really create a sort of a hold in a way because especially the new plants, the new plants that are coming in the pipeline, they are in a very difficult financial situation, I'm wondering how they will fulfill the lenders requirements if they are really not making good results. So, it is a threat, I think it is a threat especially the Chinese they will act when the logistic costs would make sense to them and they will start to export outside of southeast Asia, region, they will move. Recently we have seen them at a certain point of time, they have reached even Latin America, they have reached Europe, they have reached Turkey, but they will reach these regions on an on and off basis it’s not in a continuous and sustainable sort of supply, which converters might not really like it especially the converters whom are really preferring to maintain a consistent quality and the supply, it’s not only just a price. It’s more into also a sustainable and reliable supply. We have no presence as we speak in China, in fact, but if things are improving, if the prices might improve definitely China, they will push a product to rest of the regions.

**Based on something you just said, BASF has made some investments in China. You just stated that you don't have anything there now. Would you ever consider something down the road to partner, JV or anything of that nature?**

At this point of time, I think with the current market situation with the project that Advanced has in hand, I think we need to focus more on this project. It's very important to really stabilize and complete our projects efficiently to stabilize our operation and really to have a focus. We have a cracker in the pipeline, and we have also other projects as well, in addition to the IPA that is under detailed engineering right now. We need to also to create sort of a balance. Now with our JV with SK Advanced, with the exposure that we have, I don't think at this stage it is an option to look for a Chinese asset or so.

**Would you continue start up agreement beyond 2025 together with the new PDH plan?**

This is one of the subjects that we are evaluating all the time. It depends, I think it has a lot of associated points to be considered for instance, the commercial discussion. I think this is one point, also even beyond 2025 for how long just, to have a criteria, usually we are maintaining two, three years, two, three years I mean. A short term, you know, supply, also by that time I think we will be much better position to know the maximum sustainable capacity of our PDH plant. That would fulfill the previous plant also at the maximum capacity because this is the cheapest form of propylene, and then we need to look at, the contract, so it is under evaluation, but definitely if it makes sense for us and our negotiation with them, it is absolutely an option yes to extend. We are not closing this door, always if there's a value addition, we need to consider part of our discussion.

**Could you please throw some lights on the upcoming expansion plan by the company?**

We have touched base as we speak, we have our project. That's supposed to be towards the end of the year, and we have the cracker project which we have talked about in our introduction is under project configuration development, financial model, completing also the market study with the consultants, trying to get it done by sometimes in the third quarter ready. And also, we have another project which is supported by the Shareek program. We are under discussion also with our foreign partner trying to move and to make the FID, if possible, by end of the year, early first quarter next year. So, these are the key projects that we are handling right now.

**I'm sure you followed Lyondell’s announcement with regard to looking at restructuring its European business. Our analysts suggests that potentially quite a lot of polypropylene plants that Lyondell currently owns may close. Is that a market you've looked at, is this potentially an opportunity for you to place some more product in Europe? Just your thoughts on that, please?**

Definitely, Europe is part of one of the key regions that we are always looking at. And yes, we are selling our product to Europe, and we have also key customers over there. We are watching closely what's going on there in terms of, offloading some of the plants or closing some of the assets. And also, the shortage of supply especially in some of the grades that we are making so we can fulfill the demand. But also, the same time, to share with you, I mean what they call a consortium, I think now there is a talk in Europe as well about, seeking support from European governments also regarding the petrochemical industry. You know, the border carbon tax mechanism, I think this is one of the different lines, I think which would be implemented in Europe just to protect and to restrict, other producers whether from Middle East or other countries. But you are right. I think the shortage of supply in Europe, definitely Europe is a key market for us and we are all always, our guys are putting a good focus and they are selling a product over there. Just would like to add that we all heard that LyondellBasell is closing their plants in Europe, but again, they are also investing heavily in Saudi petrochemical plants, which is already announced. So that will tell us the strategic position of Saudi petrochemical industry and the cost effectiveness.

**Have you done any sort of analysis to what kind of closures have been announced as percent of industry capacity and what percent do we need to sort of go back to mid cycle margins.**

Recently I think in total 1.8 million ton of PP if I’m not mistaken, which would represent about 1.6- 1.7%. So, a total market of almost close to 90 now, so about 1.8 million ton as a closure. Part of it in Europe, definitely. So, if not, most or the max in Europe. The lower capacity as well, I mean in China which and for me to be honest with you, sometimes it doesn’t make sense even lowering and running at lower capacity because still they are in negative margin. Most of their plants, most of their plants are running at 50-60% capacity. I’m talking about the PDH plant. But in Europe and other countries, what we have seen, we have seen about 1.8 million ton of polypropylene. They shut down which means that once the margin gets improved maybe they will operate again. It's not fully closed; we can say shutdown. They might close the plant, whenever it makes sense for them, they will bring it back on online.

Okay, thank you so much that was the last question. Back to you Advanced management. For our final remarks, thank you very much and really appreciate you and also the audience for this interactive session, and I wish you liked the new presentation that been developed by our team, and definitely we are welcoming any enhancement as well and looking InshAllah for a good quarter and quarter two, and hopefully things will get improved as we go down the road.

Thank you very much Mr. Fahad, and I would like to thank Advanced petrochemical management for taking the time to conduct this call. We would like also to thank all the participants for attending. We Wish You a pleasant day, thank you.