

3 October 2022

Energy & Petrochemicals | Oil & Gas Services

Petronas Dagangan (PETD MK)

Neutral (Maintained)

Site Visit To Kota Kinabalu

Target Price (Return): MYR20.15 (+1%)
 Price (Market Cap): MYR20.00 (USD4,289m)
 ESG score: 3.10 (out of 4)
 Avg Daily Turnover (MYR/USD) 5.03m/1.12m

- **Keep NEUTRAL and MYR20.15 TP, 1% upside.** We saw a high level of compliance to Petronas' healthy and safety policies in place, coupled with an increasing emphasis on sustainability efforts from our site visit to terminals at Kota Kinabalu. Despite sales volume recovery, Petronas Dagangan's operating cash flow may remain volatile in the near term.

- **Sabah's site visit.** Last week, PETD hosted an investor relations visit to its business operations in Kota Kinabalu, Sabah – Sepangar Bay Fuel & LPG Terminal (SBFLT) and Kota Kinabalu Aviation Fuel Terminal (KKAFL). Sabah contributed about 10-15% of total sales volume in the past. For the retail division, there are currently 76 petrol stations in Sabah, with a 2-3 new station expansion pa. For SBLFT, the bulk of the products are sourced from refineries in Malacca. Cost-to-serve for fuel and LPG (which includes logistic and storage costs) have lowered YoY to MYR0.1389/litre and MYR30.67/tonne, thanks to volume recovery following the re-opening of economies and borders. SBLFT is looking to obtain the supply from refineries in Pengerang once the plants achieve stable output and this could further reduce logistic costs. SBLFT is also one of the 14 selected terminals under Project Drive Optimisation Value (DOVE), embarked since 2020, whereby PETD will no longer own inventory at the terminal. The management and ownership of these inventories have been transferred to PETCO Trading Labuan Company Ltd (PTLCL). This will allow PETD to eliminate exposure of the unfavourable Means of Platts Singapore (MOPS) movement. Meanwhile, we saw a high level of compliance to Petronas' healthy and safety policies being demonstrated, coupled with an increasing emphasis on sustainability efforts.

- **Targeted fuel subsidy timeline uncertain.** PETD is still in close discussion with the Government on the potential targeted subsidy, and the implementation timeline remains uncertain. At the same time, PETD is also negotiating with the Government to recoup the delayed fuel subsidy payment. Recall that its operating cash flow has declined by MYR551m in 2Q22 as the increase in trade receivables (+1.5x QoQ) was offset by the spike in trade payables (+1.1x QoQ). Hence, we may continue to see a rather volatile operating cash flow, mainly from the escalated fuel subsidy from the Government amidst higher product prices.

- **We maintain our earnings estimates.** DCF-derived TP is kept at MYR20.15 with the incorporation of a 2% ESG premium, based on its score of 3.1. We have assumed a lower dividend payout of 65% in FY22 (1H22 implied payout at 55%) before normalising to 80% in 2023F, vs the pre-pandemic average historical payout ratio of 78% (ex-special dividends).

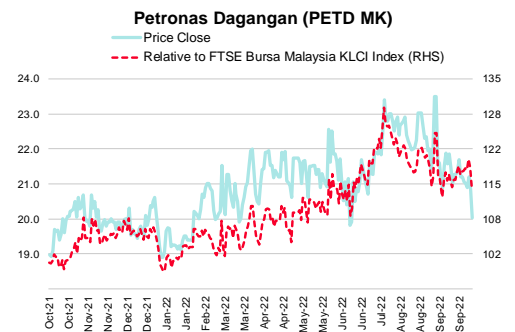
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(2.8)	(14.8)	(5.2)	(2.4)	4.7
Relative	8.2	(7.0)	(1.8)	9.5	14.0
52-wk Price low/high (MYR)	18.9 – 23.5				



Source: Bloomberg

Overall ESG Score: 3.10 (out of 4)

E: MODERATE

PETD continues to put in meaningful efforts in implementing initiatives that address climate change and natural resource preservation. The group enhanced the role of solar energy in its operations, with an additional 3.6 MWh of photovoltaic capacity installed. Through this effort, total GHG emissions decreased by 12% in 2021. Furthermore, PETD had installed rainwater harvesting tanks at its retail stations to reduce environmental footprint. There is good disclosure on its environmental impact, efforts, and implementation. However, PETD recorded three hydrocarbon spills in the year (an increase from previous year's two spills).

S: EXCELLENT

Good disclosures on efforts in employee relations, health & safety, and community engagement. There are policies in place that protect employee welfare. Additional benefits are also provided: Childcare facilities, maternity leave, etc. It has good track record on health & safety; with fatality remaining at zero and Lost Time Injury Frequency reduced from 0.33 to 0.3 in 2021. The firm is actively involved in community engagement efforts, eg its Food Bank programme at over 300 PETRONAS stations nationwide to provide food to communities affected by the pandemic.

G: EXCELLENT

PETD fares well in the governance pillar as the group meets the requirement of Bursa Malaysia and the Malaysian Code on Corporate Governance with 50% independent directors. Women directors made up 38% of the board, and members are experienced, skilled professionals. Disclosure and transparency levels are within requirements of Malaysia's regulatory framework, and shareholder rights are well-protected.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (MYRm)	18,711	22,505	28,267	28,282	28,298
Recurring net profit (MYRm)	320	549	640	787	805
Recurring net profit growth (%)	(61.3)	71.7	16.7	23.0	2.2
Recurring P/E (x)	62.21	36.24	31.06	25.26	24.71
P/B (x)	3.5	3.6	3.4	3.3	3.2
P/CF (x)	54.82	100.91	46.59	8.61	54.08
Dividend Yield (%)	1.9	3.5	2.1	3.2	2.6
EV/EBITDA (x)	19.31	15.56	13.01	11.35	11.64
Return on average equity (%)	4.7	9.5	11.2	13.4	13.2
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Malaysia	Recurring EPS	0.32	0.55	0.64	0.79	0.81
Energy & Petrochemicals	DPS	0.38	0.70	0.42	0.63	0.53
Petronas Dagangan	BVPS	5.68	5.62	5.84	6.00	6.29
PETD MK	Return on average equity (%)	4.7	9.5	11.2	13.4	13.2
Neutral						
	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Recurring P/E (x)	62.21	36.24	31.06	25.26	24.71
	P/B (x)	3.5	3.6	3.4	3.3	3.2
	FCF Yield (%)	(0.4)	(0.9)	0.6	10.1	0.3
	Dividend Yield (%)	1.9	3.5	2.1	3.2	2.6
	EV/EBITDA (x)	19.31	15.56	13.01	11.35	11.64
	EV/EBIT (x)	43.19	24.10	19.08	16.07	16.14
	Income statement (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total turnover	18,711	22,505	28,267	28,282	28,298
	Gross profit	18,711	22,505	28,267	28,282	28,298
	EBITDA	900	1,163	1,413	1,499	1,500
	Depreciation and amortisation	(498)	(412)	(449)	(441)	(418)
	Operating profit	403	751	964	1,058	1,082
	Net interest	(16)	(12)	(12)	(12)	(12)
	Pre-tax profit	386	741	953	1,048	1,071
	Taxation	(114)	(210)	(315)	(262)	(268)
	Reported net profit	276	533	640	787	805
	Recurring net profit	320	549	640	787	805
	Cash flow (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Change in working capital	(316)	(766)	(660)	1,084	(853)
	Cash flow from operations	363	197	427	2,310	368
	Capex	(443)	(374)	(300)	(300)	(300)
	Cash flow from investing activities	(319)	(297)	(300)	(300)	(300)
	Dividends paid	(606)	(606)	(416)	(630)	(523)
	Cash flow from financing activities	(778)	(683)	(416)	(630)	(523)
	Cash at beginning of period	3,426	2,692	1,911	1,622	3,002
	Net change in cash	(734)	(783)	(289)	1,380	(455)
	Ending balance cash	2,691	1,909	1,622	3,002	2,546
	Balance sheet (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total cash and equivalents	2,692	1,911	1,622	3,002	2,546
	Tangible fixed assets	4,067	4,018	3,868	3,728	3,609
	Total investments	21	23	24	26	27
	Total assets	8,360	9,601	10,438	10,209	9,716
	Short-term debt	81	24	24	24	24
	Total long-term debt	97	92	92	92	92
	Total liabilities	2,684	3,985	4,600	4,215	3,441
	Total equity	5,676	5,615	5,838	5,994	6,274
	Total liabilities & equity	8,360	9,601	10,438	10,209	9,716
	Key metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Revenue growth (%)	(38.2)	20.3	25.6	0.1	0.1
	Gross margin (%)	100.0	100.0	100.0	100.0	100.0
	Operating EBITDA margin (%)	4.8	5.2	5.0	5.3	5.3
	Net profit margin (%)	1.5	2.4	2.3	2.8	2.8
	Dividend payout ratio (%)	136.8	130.5	65.0	80.0	65.0
	Capex/sales (%)	2.4	1.7	1.1	1.1	1.1
	Interest cover (x)	25.1	64.5	82.8	90.9	92.9

Source: Company data, RHB

Site Visit To Kota Kinabalu

Last week, PETD hosted an investor relations visit to its business operations in Kota Kinabalu, Sabah ie SBFLT and KKAFL. We were hosted by Chief Operating Officer Khalil Jaffri Muhammad Muri, Chief Financial Officer Farzlina Ahmad Murad, as well as Mohammad Ali Mustapha, Head of Business & Financial Solutions and other key personnel in Sabah.

Overall, the Borneo operations (Sabah, Sarawak and Labuan) consists of nine fuel terminals, six aviation terminals, four LPG bottling plants and five bunkering facilities. Sabah contributed about 10-15% of total sales volume in the past. For the retail division, there are currently 76 petrol stations in Sabah, with a 2-3 new station expansion pa.

Sepangar Bay Fuel & LPG Terminal (SBFLT)

Commissioned in 1985, SBLFT is one of the oldest terminals in Malaysia with 15 acres total buildup area comprising six hydrocarbon products and 22 storage tanks. The terminal receives different products from the port, offers storage and LPG bottling services before being distributed. We understand that SBLFT serves 60% of the population within the proximity, handling c.1.2m litres per day of oil products. The bulk of the products are predominantly sourced from refineries in Malacca. Cost-to-serve for fuel and LPG (which includes logistics and storage costs) have lowered YoY to MYR0.1389 per litre and MYR30.67 per tonne thanks to volume recovery following the re-opening of economies and borders. SBLFT is looking to obtain the supply from refineries in Pengerang once the plants achieve stable output and this could further reduce the logistics costs.

SBLFT is also one of the 14 selected terminals under DOVE, embarked since 2020, whereby PETD will no longer own inventory at the terminal. The management and ownership of these inventories have been transferred to PTLCL. This will allow PETD to eliminate exposure of the unfavourable MOPS movement.

SBLFT demonstrated a high level of compliance to Petronas' healthy and safety policies with strict safety measures implementations. Apart from that, more sustainability efforts were observed and key notables are its recycling programme and rainwater harvesting initiative. The latter was implemented since 2018 whereby the harvested rainwater is used for operational and janitorial activities (ie cylinder washing). In 2021, SBLFT saved up to 22,000 litres of water.

Figure 1: LPG bottling process



Source: RHB

Figure 2: Loading bay



Source: RHB

Figure 3: Storage tanks



Source: RHB

Figure 4: Products in barrels for military use



Source: RHB

Kota Kinabalu Aviation Fuel Terminal (KKAFL)

We also visited KKAFL to understand the operations of the aviation fuel terminal. Situated next to the airport, KKAFL services only the Kota Kinabalu airport, and is responsible for c.70% of the airport's total aviation fuel demand. There are six units of filters in use to ensure clean and dry products are delivered to clients while six bowsers and four dispensers are filled up at the loading bay before being transported to airport for refuelling process.

Figure 5: Dispenser



Source: RHB

Figure 6: Bowser



Source: RHB

Recommendation Chart

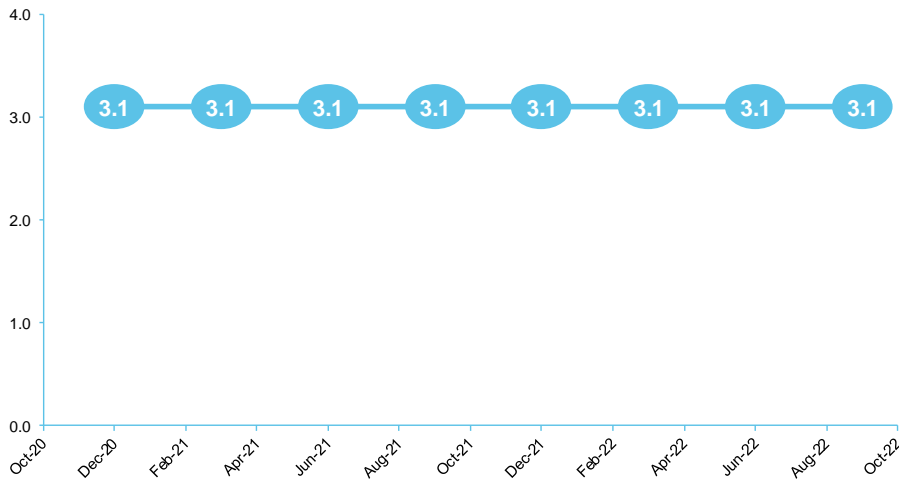


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-08-24	Neutral	20.1	21.9
2022-05-27	Neutral	20.0	21.0
2022-02-23	Neutral	19.9	20.0
2021-11-29	Neutral	20.0	19.7
2021-08-23	Neutral	19.7	18.8
2021-05-27	Neutral	20.3	19.5
2021-02-21	Neutral	20.7	19.2
2020-12-17	Neutral	21.1	19.9
2020-05-19	Sell	17.1	20.2
2020-03-27	Neutral	21.4	20.2
2019-11-25	Neutral	25.1	23.9
2019-10-04	Neutral	24.0	23.5
2019-05-29	Neutral	26.8	24.8
2019-02-27	Sell	24.0	26.6
2018-11-28	Buy	31.0	26.5

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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