

SECTOR UPDATE

Oil & Gas – Thailand

Concerned On China's Petrochemical Demand In 2H23; Downgrade To MARKET WEIGHT

We downgraded the O&G sector to MARKET WEIGHT. Despite a balance in demand and supply in the crude and refinery segments, we see potential risks for the petrochemical sector due to weak China demand in 2H23 and a substantial increase in new supply. These factors are expected to restrict the improvement in spreads margin. Our top picks include PTT Exploration & Production (PTTEP TB/Target: Bt174.00) and PTT Oil and Retail (OR TB/Target: Bt29.00).

WHAT'S NEW

- **Less surplus from higher oil demand and limited supply.** In Apr 23, OPEC and its alliances (OPEC Plus) announced a further oil output cut by about 1.16m barrels per day (m bpd) from May onwards in a surprise move when market expected the cartel to maintain its 2m bpd cut agreed in Oct 22. The limited increase in oil supply aims to support the potentially softer oil demand. Some OPEC members recently foresee world demand in 2023 growing only 2m bpd in 2023 (vs 2.3m bpd in its latest Oil Market report in early-June). This means world oil demand grew only 2% compared with a growth of 3.36m bpd in 2022. The surging crude and fuel prices help drive up inflation and act as a drag on the global economy. OPEC is watching for signs that high fuel prices will lead to oil demand destruction.

- **Short-term GRM continues to be weak, but there is a possibility of recovery in 2H23.** The risk factors that contribute to the downward pressure on gross refining margins (GRM) in the short term include: a) reduced demand for diesel fuel, particularly in the power generation sector, as electricity producers opt for cheaper gas to generate electricity, b) an increase in China's refined oil export quota, leading to a rise in oil supply in the region, and c) increased supply from new refinery in the Middle East, especially during 2Q23, with an additional production of over 1m bpd. These factors collectively contribute to the challenging environment for refining margins in the short term. Average Singapore GRM qtd has declined substantially to US\$4.20/bbl from US\$8.22/bbl in 1Q23.

The demand for middle distillate oil has decreased following the conclusion of the recent winter season and the tourist season. Additionally, there are high levels of reserves for oil in the middle distillate group, particularly jet fuel. These factors are expected to exert pressure on middle distillate margins until the high season returns in late 4Q23.

PEER COMPARISON

Company	Ticker	Rec.	Last Price (Bt)	Target Price (Bt)	Upside/ (Downside) (%)	Market Cap (US\$m)	PE 2022 (x)	PE 2023F (x)	PE 2024F (x)	EPS CAGR 2022-24F (%)	PEG 2023F (x)	P/B 2023F (x)	Yield 2023F (%)	ROE 2023F (%)
Bangchak Petroleum	BCP TB	BUY	34.50	40.00	15.9	1,357	3.7	9.9	9.6	(37.7)	(0.2)	0.7	3.5	5.6
Esso (Thailand)	ESSO TB	BUY	8.80	12.50	42.0	870	3.2	7.0	7.6	(35.0)	(0.1)	1.0	2.3	15.3
IRPC	IRPC TB	HOLD	2.22	2.20	(0.9)	1,296	n.a.	14.0	7.0	na	(0.1)	0.6	4.5	4.0
Indorama Ventures	IVL TB	BUY	32.50	37.00	13.8	5,214	5.9	13.0	6.4	(3.8)	(0.2)	0.9	3.4	7.1
PTT Oil&Retail Business	OR TB	BUY	20.50	29.00	41.5	7,029	23.7	16.7	15.9	22.2	0.4	1.1	1.8	6.5
PTG Energy*	PTG TB	BUY	11.60	18.80	62.1	553	20.7	14.6	11.1	36.9	0.3	2.6	3.4	18.3
PTT	PTT TB	BUY	31.25	39.00	24.8	25,503	9.8	9.8	9.1	3.9	(604.6)	0.8	6.4	8.2
PTTEP	PTTEP TB	BUY	145.50	174.00	19.6	16,504	8.1	9.2	7.7	3.2	(0.8)	1.2	5.5	13.7
PTTGC	PTTGC TB	HOLD	36.25	41.00	13.1	4,670	n.a.	16.8	12.8	na	(0.1)	0.5	2.8	2.9
Siam Cement	SCC TB	HOLD	321.00	360.00	12.1	11,006	18.0	13.4	12.4	20.3	0.4	1.0	3.7	7.9
Star Petroleum Refining	SPRC TB	HOLD	8.15	9.00	10.4	1,010	4.6	12.8	8.6	(26.7)	(0.2)	1.1	4.9	7.8
Thai Oil	TOP TB	HOLD	43.25	53.00	22.5	2,521	3.0	7.4	7.1	(35.3)	(0.1)	0.6	5.8	8.0
Sector						77,532	10.5	11.5	9.8			0.9	4.8	8.8

Source: Bloomberg, UOB Kay Hian

MARKET WEIGHT

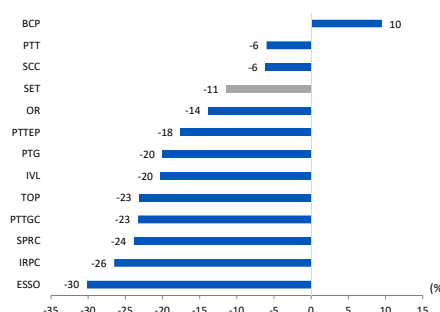
(Downgraded)

SECTOR PICKS

Company	Rec	Share Price (Bt)	Target Price (Bt)
OR	BUY	20.50	29.00
PTTEP	BUY	145.50	174.00

Source: UOB Kay Hian

SHARE PRICE PERFORMANCE (% YTD)



Source: Bloomberg, UOB Kay Hian

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• **China demand in petrochemical segment seems to be slower than expected.** Based on our latest channel check, demand from China may not recover much in 2H23. For example, global polypropylene (PP) demand is about 100m tonnes per annum. Of which, 45% is from China, comprising of 47% for domestic consumption and 53% for the export market. China's exports of PP to markets in the US and Europe represent 40-50% of its total exports, where there is a risk stemming from economic factors that has led to a more cautious approach towards shopping. Consequently, there has been a decrease in overall purchasing power, particularly in the automobile and packaging industries. This decline in purchasing power has negatively impacted the petrochemical business as a whole. Additionally, the expansion of new production capacities will serve as a limiting factor for price increases and product spreads, thereby affecting potential upside for the industry.

ACTION

• **Downgrade to MARKET WEIGHT.** Despite a balance in demand and supply in the crude and refinery segments, we foresee potentially softer demand in petrochemical products due to the huge new supply. In the O&G space, our top picks include PTT Exploration and Production (PTTEP TB/Target: Bt174.00) and PTT Oil and Retail (OR TB/Target: Bt29.00).

ASSUMPTION CHANGES

• **None.**

ESSENTIALS

• **PTTEP (BUY/Target: Bt174.00).** We anticipate that crude oil prices in 2Q23 will reach their lowest point for the year. However, we expect a recovery in crude oil prices during 2H23. This recovery is likely to be influenced by several factors, including Saudi Arabia's decision to reduce production by 1.0m bpd, effective from 1 July. This production cut is expected to create a tight supply situation in the crude oil market. Additionally, we anticipate economic stimulus measures from the Chinese government, which will contribute to the ongoing recovery of demand. Moreover, the recent resolution by OPEC to extend its cooperation on production cuts from 2023 to 2024 is expected to have a positive impact on crude oil prices. However, there is optimism regarding the future outlook for crude oil prices in 2H23, which is anticipated to keep the stock price of PTTEP attractive. It is worth noting that there is a high correlation of 86% between PTTEP's stock price and crude oil prices, moving in the same direction.

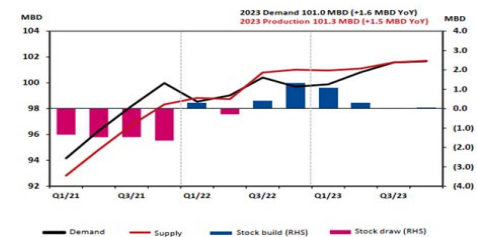
• **OR (BUY/Target: Bt29.00).** We project a core profit of Bt14.7b for 2023, which reflects a significant 42% yoy increase. This growth is primarily attributed to the recovery in marketing margins. Since the removal of measures to control retail oil prices starting on 14 February, we have observed a 17% qoq increase in gasoline marketing margins and a 5% qoq increase in diesel marketing margins during 2Q23. Looking ahead, we maintain a positive outlook for earnings in 2H23, despite the anticipated low season for domestic oil demand in 3Q23. However, we expect a recovery in oil sales volume in 4Q23 during the high season.

Despite these factors, market margin is expected to remain high, which will help limit the downside impact on 3Q23 core profit. Furthermore, there is a decreasing pressure factor as the oil fund is responsible for supporting the retail prices of petrol at service stations. The oil fund has recorded a loss of Bt69b, which is a decrease compared with the end of 2022 when the loss amounted to Bt123b. This reduction in losses indicates some improvement in the financial performance of the oil fund, potentially alleviating the burden on the fund and its impact on the retail prices.

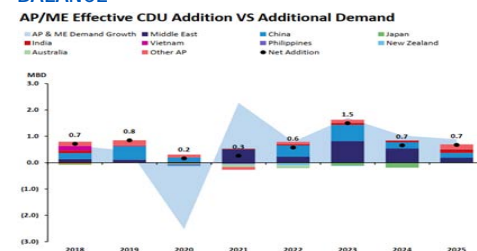
RISKS

- Rise in oil prices.
- China's demand in the petrochemical segment recovering in 2H23 as expected.

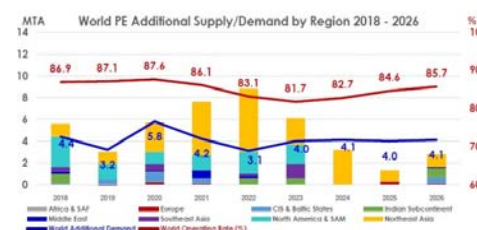
GLOBAL OIL DEMAND AND SUPPLY



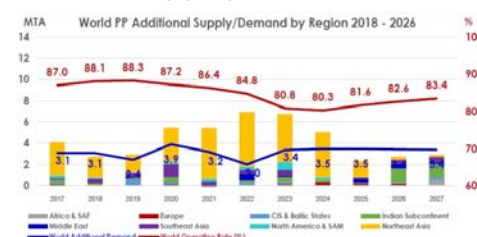
REFINERY - NEW DEMAND & NEW SUPPLY BALANCE



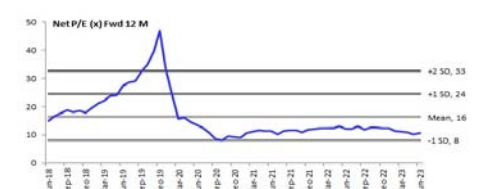
WORLD POLYETHYLENE ADDITIONAL SUPPLY / DEMAND BY REGION 2017-27



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O&G NET PE BAND



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