PhilRatings PHILIPPINE RATING SERVICES CORPORATION	RATING REPORT
	Petron Corporation

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REGULAR MONITORING

Amount of Bond Issue	Issue Date	Maturity Date	Tenor	Interest Rate	Assigned Rating and Outlook
Series C - P13.2 billion	Oct. 19, 2018	April 19, 2024	5.5 years	7.82%	**PRS Aaa Stable Outlook**
Series D - P6.8 billion	Oct. 19, 2018	Oct. 19, 2025	7 years	8.06%	
Series E - P9.0 billion	Oct. 12, 2021	Oct. 12, 2025	4 years	3.44%	
Series F - P9.0 billion	Oct. 12, 2021	Oct. 12, 2027	6 years	4.34%	
Total – P38.0 billion					

Obligations rated **PRS Aaa** are of the highest quality with minimal credit risk. The obligor's capacity to meet its financial commitment on the obligation is extremely strong. **PRS Aaa** is the highest rating assigned by PhilRatings.

A **Stable Outlook**, on the other hand, means that the assigned issue credit rating is likely to remain unchanged in the next 12 months.

OUTSTANDING PRS-RATED ISSUANCES OF RELATED COMPANIES

Bank of Commerce – 44.62% owned by SMC

Type of Rating	Outstanding Rating and Outlook
Issuer	**PRS Aa plus (corp.) with a Stable Outlook**

San Miguel Corporation (SMC) – Parent Company of Petron Corporation (Petron) and owns 68.26% of Petron's shares.

Amount of Bond Issue	Issue Date	Maturity Date	Tenor	Interest Rate	Outstanding Rating and Outlook
Series C - P6.02266 billion	Mar. 1, 2017	Mar. 1, 2027	10 years	5.76%	**PRS Aaa Stable Outlook**
Series F - P2.4385 billion	Mar. 19, 2018	Mar. 19, 2025	7 years	6.63%	
Series G - P4.4159 billion	Mar. 19, 2018	Mar. 19, 2028	10 years	7.13%	
Series H - P10.0 billion	Oct. 4, 2019	Oct. 4, 2024	5 years	5.55%	
Series I - P30.0 billion	Jul. 8, 2021	Jul. 8, 2027	6 years	3.38%	
Series J - P17.44 billion	Mar. 4, 2022	Mar. 4, 2027	5 years	5.27%	
Series K - P12.56 billion	Mar. 4, 2022	Mar. 4, 2029	7 years	5.84%	
Series L - P27.10055 billion	Dec. 14, 2022	Mar. 14, 2028	5.25 years	7.45%	
Series M - P9.71226 billion	Dec. 14, 2022	Dec. 14, 2029	7 years	7.85%	
Series N - P23.18719 billion	Dec. 14, 2022	Dec. 14, 2032	10 years	8.49%	
Total – P142.87706 billion					

San Miguel Food and Beverages, Inc. (SMFB) – SMC beneficially owns 88.76% of SMFB's shares

Amount of Bond Issue	Issue Date	Maturity Date	Tenor	Interest Rate	Outstanding Rating and Outlook
Series A - P8.0 billion	Mar. 10, 2020	Mar. 10, 2025	5 years	5.05%	**PRS Aaa Stable Outlook**
Series B - P7.0 billion	Mar. 10, 2020	Mar. 10, 2027	7 years	5.25%	
Total – P15.0 billion					

SMC SLEX Inc. (SLEX) (formerly South Luzon Tollway Corporation) – 76% owned by SMC

Amount of Bond Issue	Issue Date	Maturity Date	Tenor	Interest Rate	Outstanding Rating and Outlook
Series C - P2.5 billion	May 22, 2015	May 22, 2025	10 years	6.49%	**PRS Aaa Stable Outlook**

San Miguel Global Power Holdings Corp. (SMGP) (formerly SMC Global Power Holdings Corp.) – 100% owned by SMC

Amount of Bond Issue	Issue Date	Maturity Date	Tenor	Interest Rate	Outstanding Rating and Outlook
Series C - P4.75631 billion	Jul. 11, 2016	Jul 11, 2026	10 years	5.18%	**PRS Aaa Stable Outlook**
Series E - P6.47802 billion	Dec. 22, 2017	Dec. 22, 2024	7 years	6.25%	
Series F - P3.60902 billion	Dec. 22, 2017	Dec. 22, 2027	10 years	6.63%	
Series I - P9.23204 billion	Apr. 24, 2019	Apr 24, 2024	5 years	7.18%	
Series J - P6.92310 billion	Apr. 24, 2019	Apr 24, 2026	7 years	7.60%	
Series K - P5.0 billion	Jul. 26, 2022	Jul. 26, 2025	3 years	5.91%	
Series L - P25.0 billion	Jul. 26, 2022	Jul. 26, 2028	6 years	7.11%	
Series M - P10.0 billion	Jul. 26, 2022	Jul. 26, 2032	10 years	8.03%	
Total – P70.99849 billion					

RATIONALE

Sustained retail presence and market leadership, both in the Philippines and Malaysia

Based on the data from the Department of Energy (DOE), Petron continued to lead the local oil industry in the first half of 2022 (1H2022), accounting for a market share of 20.97%. This was a slight increase compared to the full-year 2021 level, but still lower than the company's market share from 2017 to 2020. During those years, the market share for Petron were as follows: 27.6% in 2017, 26.4% in 2018, 24.6% in 2019, and 20.1% in 2020.

In terms of the Liquefied Petroleum Gas (LPG) industry, Petron experienced a dip in market share in 2020, dropping from the top spot to third place. The company, however, made a strong comeback in 1H2022, regaining its position as the market leader. In 1H2022, Petron held 21.5% of the total LPG demand.

According to management, they are currently the third top player in the Malaysian market. This is attributed to the sustained runs of the Port Dickson refinery, complemented by the additional services provided to customers in the retail service stations for a one-stop service experience. Such services include: the availability of food and beverages via Treats convenience stores, and the option to have car wheels and windshields washed and cleaned by the gasoline station staff. The Petron service stations in Malaysia are also Go-to Safety Points (GTSPs) for customers to report local crimes.

Improving sales due to economic recovery and a significant upturn in the industrial and aviation sectors

For the year ended December 2022, Petron's total revenue went up by 95.8% to P857.6 billion, compared to the previous year's P438.1 billion. The jump in revenue was driven by the significant increase of 37.2% in sales volume, from 82.2 million barrels in 2021 to 112.8 million barrels in 2022.

Cost of goods sold, however, also increased by 102.1%, from P407.6 billion in 2021 to P823.8 billion in 2022. This was largely attributed to the spike in benchmark Dubai crude oil prices, which averaged USD96 per barrel (bbl) in 2022 compared to USD69/bbl in 2021.

Petron's consolidated net income for 2022 was at P6.7 billion, a 9.1% increase from the previous year's P6.1 billion, on account of higher sales volume for the period. The rise in sales volume was attributed to the significant upturn in commercial sales, especially in the industrial and aviation sectors. This was supported by the improvements in domestic travel and overall business activities. In addition, retail sales of Petron in the Philippines and Malaysia combined have shown a positive increase of 26%. Meanwhile, the trading volume of Petron Singapore Trading Pte. Ltd. (PSTPL) has more than doubled and the sales of polypropylene have substantially increased due to the resumption of its plant's operation in 2022.

Considering the significant growth recorded in costs and expenses, gross profit margin decreased from 7.0% in 2021 to 3.9% in 2022. Net profit margin was also lower, from 1.4% in 2021 to 0.8% in 2022, mainly due to higher interest expense incurred by the company. Return on average assets (ROAA) was slightly lower at 1.5% in 2022, from 1.6% in 2021.

Petron sold 126.9 million barrels in 2023, higher by 12.5% than the 112.8 million barrels sold in 2022. The growth was attributable to the significant growth in the Company’s Jet Fuel and LPG sales, coupled with higher production at its Bataan and Port Dickson refineries. Despite higher sales volume, Petron posted lower revenues during the period at P801.0 billion, down by 6.6% from the P857.6 billion recorded in the previous year. Such was due to price correction as full year average price of benchmark Dubai crude was USD82/bbl in 2023, a 14.6% decline from USD96/bbl in 2022. Nevertheless, Petron was able to record 51.3% growth in its net income, from P6.7 billion in 2022 to P10.1 billion in 2023, driven by the Company’s efforts to capture the continued recovery in demand and respond to market volatility.

Experienced management and synergies with companies belonging to the San Miguel Group

Petron will continue to focus on volume growth, efficient operations, and the optimal use of assets amid a challenging business environment. To ensure business sustainability, the company will continue to implement the following strategies: (1) maximize production of high-margin refined petroleum products and petrochemicals; (2) ensure reliability and efficiency of refinery operations; (3) maximize volume growth and further increase market share in the downstream oil markets in the Philippines and Malaysia; (4) innovation as a tool for customer retention and growth; and (5) continue to evaluate possible selective synergistic acquisition.

As of June 30, 2023, Petron had two principal common shareholders namely: SEA Refinery Corporation (SEA Refinery)–with 50.1% of Petron’s common shares—and SMC–with 18.16%.

SEA Refinery is 100%-owned by SMC, allowing the latter to hold an aggregate 68.26% ownership of Petron. SMC is one of the largest and most diversified conglomerates in the Philippines, with business interests in beverage, food, packaging, fuel and oil, power, and infrastructure.

Mr. Ramon S. Ang (69 years old) is the President and Chief Executive Officer (CEO) of Petron. He is also the Vice-Chairman, President, and Chief Operating Officer of SMC. In addition, Mr. Ang is currently the Vice Chairman of Ginebra San Miguel Inc. (GSMI) and SMFB. Concurrently, he is the Chairman of SMB and SLEX; and the Chairman and CEO of SMGP. Aside from these positions, Mr. Ang is also the Chairman of the Petron Malaysia companies.

Petron is seen to strongly benefit from Parent Company support given its shared directors and executive officers with SMC and other affiliates. In addition, the company has a highly capable and experienced management team with the technical expertise needed to run the business.

Increasing economic uncertainty due to the adverse impact of inflation and higher interest rates

Gross Domestic Product (GDP) growth in the last quarter of 2023 was logged at 5.6%, bringing full-year GDP growth to 5.6% in 2023. This was behind the government’s target GDP growth of 6% to 7% for the year. The industries that contributed most to the annual growth were: Wholesale and Retail Trade, Repair of Motor Vehicles and Motorcycles (5.5%); Financial and Insurance Activities (8.9%); and Construction (8.8%).

All major economic sectors posted full-year increases, as follows: Agriculture, Forestry, and Fishing (1.2% YoY and 1.4% in 4Q 2023); Industry (3.6% YoY and 3.2% in 4Q 2023); and Services (7.2% YoY and 7.4% in 4Q 2023).

On the demand side, annual growth of Household spending was at 5.6% (5.3% in 4Q 2023) while Government spending minimally rose by 0.4% (-1.8% in 4Q 2023) for the year. According to National Economic and Development Authority (NEDA) Secretary Arsenio Balisacan, the slower expansion in government spending was intentional, as the government aims to achieve fiscal consolidation. This meant prioritizing the reduction of fiscal deficit and government debt. Data from the Bureau of the Treasury showed an improved debt-to-GDP ratio of 60.2% in 2023, from 60.9% at the end of 2022.

Inflation in February 2024 broke its four-month downtrend, going up to 3.4% (from 2.8% in January 2024) on the back of higher prices for key food items, particularly rice. The figure, however, still fell within the BSP projection of 2.8-3.6%. It also marked the third straight month that inflation was kept within the government's 2-4% target range. The target inflation rate for full-year 2024 was pegged within the range of 2% to 4%.

BUSINESS RISK

Company Profile

Petron is the largest oil refining and marketing company in the Philippines. In March 2012, Petron acquired an integrated refining, distribution, and marketing business in Malaysia, increasing its regional presence in Southeast Asia. The company's primary business involves the refining of crude oil and the marketing and distribution of refined petroleum products. Its principal products are mainly categorized into fuels, oil, lubricants and greases, and petrochemicals.

The table below is a list of Petron's product lines and brands as of April 12, 2023:

Table 1 Petron's product lines and brands in Philippines and Malaysia

Product Lines and Brands	Philippines	Malaysia
Fuels	Fiesta Gas Petron Gaas Petron Blaze 100 Euro 6 Petron XCS Petron Gasul Petron Xtra Advance Petron Turbo Diesel Petron Diesel Max Petron Aviation Gasoline Petron Jet A-1	Petron Blaze 100 EURO 4M Petron Blaze 97 EURO 4M Petron Blaze 95 EURO 4M Petron Turbo Diesel Euro 5 Petron Diesel Max Petron Diesel B0 Petron Gasul Petron Kerosene Petron Jet A-1
Oils, Lubricants and Greases	Automotive oil and lubricant products Industrial oil and lubricant products Marine oil and lubricant products Greases Aftermarket Specialties	Automotive oil and lubricant products Industrial oil and lubricant products Marine oil and lubricant products Greases Aftermarket Specialties
Petrochemicals	Xylene Benzene Polypropylene Toluene Propylene	None
Other Refinery Products	Naphtha Molten sulfur Petcoke	Naphtha Low Sulfur Waxy Residue
Other Products (from the Palm Methyl Ester (PME) plant)	None	Refined Glycerin Crude Glycerin

Petron continues to invest in Research and Development (R&D), both locally and abroad, to provide its customers with new products. The company's product development is mostly driven by the requirements of automotive original equipment manufacturers and the latest technological trends in the industry. The company's R&D also ensures that its products are compliant with environmental laws and government regulations. PhilRatings notes, however, that there have been no new product lines and brands launched since July 2021.

In 2022, Petron renewed its licenses and approvals for industry standards such as the International Lubricant Specification Advisory Committee (ILSAC), Association des Constructeurs Européens d'Automobiles/Association European Automobile Manufacturers Association (ACEA), and National

Marine Manufacturers Association (NMMA). Additionally, Petron obtained original equipment manufacturers (OEM) approvals from Porsche, Volvo, Mack, Renault, Cummins, MTU, and Scania. These certifications and approvals are recognized worldwide and are also applicable to the markets of Malaysia, China, Brunei, Vietnam, and Cambodia.

The major markets in the petroleum industry are the resellers (i.e. service stations), industrial, LPG, and lube trades. Petron caters to both the retail and commercial markets, selling its products to bulk off-takers and industrial end-users. Petron's non-fuel business, on the other hand, involves Treats store operations, as well as the leasing of space at some of its service stations to third-party entities for services that provide customers with a one-stop full-service experience.

Please refer to Annex A for the list of Petron's subsidiaries and the corresponding function of each in support of the company's core business.

Operations

Petron operates the sole petroleum refinery complex in the Philippines located in Limay, Bataan, with a rated crude oil distillation capacity of 180,000 bbl per day. The refinery underwent an upgrade to a full conversion refining complex starting 2010, and began its full commercial operations in January 2016. The Refinery Master Plan Phase-2 (RMP-2) upgrade enabled Petron to convert all fuel oil into a full range of higher-valued petroleum products including LPG, gasoline, diesel, jet fuel, kerosene, and petrochemicals. These products are being sold to motorists and public transport operators throughout the country.

In January 2021, Petron's application as a registered enterprise in the Freeport Area of Bataan (FAB) was approved. The registration will allow the company's refining business to improve its financial viability as the accreditation entails tax perks. From February 10, 2021 to May 22, 2021, the Bataan Refinery underwent a planned total plant shutdown in relation to maintenance activities. Petron imported products within the period to continuously serve demand, while maintenance works were done. The Refinery continued its operations on May 23, 2021, and achieved stable and optimized performance. Refined products from the refinery are used as compound to produce petrochemical products. In 2H2022, the construction of the Bataan power plant's phase 3 expansion was completed, resulting in an additional 44MW of capacity for the co-gen facility. Petron Bataan Refinery expects to benefit from this project in two ways: by freeing up fuel oil previously used for refinery purposes for conversion into high-value products, and by generating incremental power for sale to the grid.

Aside from the power plant expansion, Petron Bataan Refinery has made other investments such as constructing a coco-methyl ester (CME)[1] plant and implementing the Propylene Transfer Line project to enhance propylene feed to the Polypropylene Plant (PPP).

Petron is currently expanding its polypropylene plant to increase annual production capacity from 160,000 Metric Tons (MT) to 225,000 MT. The completion of this expansion is expected in 2023. Petron, however, has not yet started the commissioning of the second reactor. PhilRatings notes that JG Summit Olefins Corporation (JGSOC) presently operates a polypropylene plant with a production capacity of 300,000 MT.

[1] fatty acid methyl esters (FAME) derived from coconut oil whose alkyl groups range in varying percentages from C8 to C18 suitable for compression ignition engines and other similar types of engines. For more information, see https://www.doe.gov.ph/sites/default/files/pdf/announcements/draft_pns-biofuels-cme-b100-specification.pdf?withshield=1

In Malaysia, Petron operates a petroleum refinery located in Port Dickson, Negeri Sembilan. It has a crude oil distillation capacity of 88,000 bbl per day. The Port Dickson refinery produces a range of petroleum products, including but not limited to LPG, gasoline, jet fuel, and diesel. These products are intended to meet domestic demand in Malaysia. Furthermore, it also operates a Palm Methyl Ester (PME) plant in Lumut, Perak, with a rated capacity of 78,000 MT per year of PME used for biodiesel blend. Other products such as Low Sulfur Waxy Residue and Naphtha are being exported by Petron Malaysia to various customers in the Asia-Pacific region under term and spot contracts.

In 2021, Petron successfully completed the construction of a diesel hydrotreater process unit at the Port Dickson Refinery. Such enabled the company to comply with the Malaysian government's mandate for Euro 5 specification for diesel with 10 parts per million (ppm) sulfur, which became effective in April 2021. The company also finished constructing a new marine import facility in 2021, which helped to reduce freight and demurrage costs by alleviating congestion at the existing jetty. Additionally, in January 2022, Petron completed the expansion of the Lumut Plant, which increased its capacity from 60,000 MT to 78,000 MT.

Table 2 Sales Revenues per Market

(in millions PHP)	2021	2022	9M2022	9M2023
Philippines	223,222	412,743	296,932	302,344
Exports/International*	214,835	444,895	334,206	284,939
Total	438,057	857,638	631,138	587,283
Share to Total Sales Revenues (%)	**2021**	**2022**	**9M2022**	**9M2023**
Philippines	51.0	48.1	47.0	51.5
International*	49.0	51.9	53.0	48.5
Total	100.0	100.0	100.0	100.0

**Includes China, Taiwan, Malaysia, South Korea, Singapore, Vietnam, Indonesia, and India*

Petron's total sales revenues in 2021 was at P438.1 billion. Sales from the Philippine market contributed P223.2 billion or 51% of total revenues, while the international market contributed P214.8 billion or 49% of total. Petron's overall sales revenues rose by 95.8% to P857.6 billion in 2022. The Philippine market generated P412.7 billion or 48.1% of total revenues, while the international market contributed P444.9 billion or 51.9% of total. It is worth noting that Petron's sales revenues from the international market surpassed the sales generated from Petron's domestic market in 2022. This was likely due to the growing demand for fuel in the Asia-Pacific region, as well as Petron's expansion into new markets.

In the first nine months of 2023 (9M2023), Petron's domestic operations contributed P302.3 billion, or 51.5% of total revenues. This was slightly higher compared to the P296.9 billion recorded in 9M2022. In contrast, revenues from international operations declined to P284.9 billion, or 48.5% of total revenues, against the P334.2 billion in the same period last year.

Petron has a well-diversified revenue stream from both domestic and international markets. This can be beneficial for the company's financial stability, as it can mitigate risks associated with fluctuations in local demand and global market conditions. Over the past years, there have been various global events that have had a significant impact on the world economy and the oil industry. These events have highlighted the importance of geographical diversification of revenue streams in order to manage risk. By tapping into multiple markets, Petron is less vulnerable to shifts in oil prices or political instability in a specific region.

Supply and Production

Crude oil is the main raw material which Petron uses in the production of a wide range of refined petroleum products. Petron purchases all its term and spot crude requirements for domestic operations through its wholly-owned subsidiary, Petron Singapore Trading Pte. Ltd. (PSTPL). Please refer to Annex A for the description of PSTPL's function.

Petron, through PSTPL, imports the majority of its domestic crude oil requirements from Saudi Arabian Oil Company (Saudi Aramco) under a term contract. The standard duration for the term contracts is one year, with automatic annual extension thereafter unless either the company or the crude oil supplier decides to terminate the contract, upon at least 60 days' written notice prior to its expiration date. Moreover, Petron has adopted a strategy to leave a portion of its requirements open to possible alternative crude.

Petron Malaysia, on the other hand, has a contractual agreement with ExxonMobil Exploration and Production Malaysia Inc. (EMEPMI) for a long-term supply of Tapis crude oil and Terengganu condensate for its Port Dickson Refinery. Additionally, the company has a Sale/Purchase Agreement with Exxon Trading Asia Pacific, a division of ExxonMobil Asia Pacific Pte. Ltd., for Low Sulphur Waxy Residue. In 2022, around 52% of the volume of crude and condensate processed came from EMEPMI, while the remaining 48% were obtained through spot purchases.

PhilRatings notes that for Petron Malaysia in 2022, around 52% of the volume of crude and condensate processed came from contracts while the remaining 48% were obtained through spot purchases. On the other hand, bulk of the supply requirements of Petron's Philippine operations were from term contracts. According to management, refining operations in Malaysia and the Philippines have been tailored to accommodate different types of crude oil, each with its own specific characteristics.

Aside from crude oil, various finished products are also being imported/purchased from several oil companies. Petron purchased most of its finished product import requirements in 2022 also through PSTPL. For 2023, aviation gasoline, asphalt, LPG, high Research Octane Number (RON) gasoline and base oil contracts were renewed for the period January to December 2023 through PSTPL.

Supply contracts for crude oil and finished products stipulate the estimated monthly volume requirement, pricing formula, payment terms, and contract duration. The pricing of crude oil and finished product imports/purchases are both based on Mean of Platts Singapore (MOPS) plus/minus a certain premium/discount. This pricing mechanism applies for both Philippines and Malaysia operations, with the exception of LPG pricing, which is based on Saudi Aramco contract prices plus a certain premium.

Crude oil is delivered to both the Limay and Port Dickson refineries by Very Large Crude Carriers (VLCCs) and marine vessels respectively, which are accommodated in the Single Buoy Mooring (SBM) located about 1.6 kilometers from the shore. Crude oil is then pumped off in storage tanks. The total capacity of crude oil storage tanks in Limay (Philippines) and Port Dickson (Malaysia) refineries are approximately 5 million barrels (MMB) and 1.1 MMB, respectively. From the storage tanks, crude oil is pumped to process units for distillation, treatment, and conversion to form different petroleum products. The Limay refinery has 19 process units while Port Dickson has four. The different petroleum products are then sent to designated product tanks, except for gasoline and LPG which undergo product blending. From the product tanks, the finished products are then pumped to pier facilities where vessels are docked for loading. The refined petroleum products are then delivered to the company's network of terminals and storage depots for distribution.

Distribution

From the Limay refinery, the company moves its products, mainly by sea, to different terminals and airport installations situated throughout the Philippines. As of March 31, 2023, Petron had a total of 28 depot terminals and 12 airport installations across the country. Petroleum products are transported from the Refinery to various terminals and sales offices across the country using barges and marine vessels in collaboration with marine transport companies. From the storage terminals, the products are then hauled by tank trucks to a network of service stations, LPG retail dealerships, and lube outlets, as well as to direct consumer accounts.

In Malaysia, the company transports its products from the Port Dickson refinery, by land and sea, to different terminals and depots throughout Malaysia. As of March 31, 2023, Petron Malaysia had 10 product terminals all over Malaysia. There are about 250 tank trucks that primarily move the company's products by land to the adjacent Port Dickson terminal. The remainder of the products is delivered via coastal tankers by sea to the rest of the distribution terminals in Peninsular Malaysia and Sabah. In addition, Petron Malaysia transports gasoline, diesel, and jet fuel via a Multi-Product Pipeline (MPP) to one of its terminals and depot in Peninsular Malaysia. The MPP is a fungible products pipeline, which is partly owned by the company.

The company's network of storage terminals and depots is installed with product loading facilities and automatic tank gauging equipment. These management systems enable Petron to measure the amount of product withdrawn from the terminals, ensuring that the product volume in storage tanks is being quantified in real-time. Tank trucks also regularly undergo periodic checks and calibrations based on the latest standards to ensure that reported volumes are accurate. Volumes are reconciled daily based on total withdrawals, meter readings, tank inventories, SAP system, and security logbook.

In terms of inventory, the company holds approximately three weeks' worth of crude oil and finished petroleum products in Malaysia. Locally, Petron stores about eight weeks or 57 days' supply equivalent.

The company's service stations mostly make up its extensive distribution network. As of April 12, 2023, the total number of service stations in the Philippines stood at more than 1,900. PhilRatings notes, however, that this was lower compared to the 2,435 total service stations as of December 31, 2020. According to management, the decline was due to the closure of its "bulilit" stations as demand for such gradually diminished caused by proliferation of properly sized stations. The closures, however, did not significantly impact the overall volume of Petron's operations.

In Malaysia, there were approximately 750 service stations located throughout Peninsular Malaysia and Sabah as of April 12, 2023. This was slightly higher compared to the 722 service stations recorded in the last credit rating review. According to management, Petron has been steadily expanding its network of service stations in Malaysia. These stations are designed to be of appropriate size or even larger compared to those in the Philippines. It is important to note that establishing a service station in Malaysia is subject to stricter regulations and guidelines compared in the Philippines.

Petron Malaysia sells LPG both for domestic and industrial use to redistribution centers, stockists, dealers, and resellers. Lubricants and specialty products are marketed through a network of appointed distributors, as well as through the company's service stations. Petron Malaysia continues to expand its retail network, building more stations nationwide, particularly in areas where the company is underrepresented, as well as in locations identified as high growth with upcoming residential and commercial developments.

Customers

The company supplies fuel to large commercial and industrial customers, particularly those involved in the power and transportation sectors. Petron's top five industrial clients in the Philippines and Malaysia accounted for a manageable share of total sales revenues in 2022.

The company's sales contracts with industrial customers and dealers include estimated monthly volume requirements, pricing formula, payment terms, and contract duration. In the Philippines, sales contracts are supplemented with an Equipment Loan Agreement, which states that Petron will provide equipment to the customer/dealer but ownership will remain with the Company.

Pricing Strategy

The main goal of Petron is to balance competitive pricing with full cost recovery. Considering that the Philippine oil industry is a free and competitive market, weekly price adjustments can be made based on international benchmark prices (e.g., MOPS, Brent, etc.) and foreign exchange movements.

In Malaysia, however, pricing is regulated by the government through the Automatic Pricing Mechanism (APM). Since December 1, 2014, the Malaysian government has implemented a managed float system, wherein, the government mandates the retail prices for gasoline and diesel on a monthly basis based on the previous month's MOPS. In case of an increase in international crude oil prices, the Malaysian government may subsidize fuel prices so consumers need not bear the full cost of the increase. If the government-mandated prices are lower than the company's built-up APM cost, then Petron Malaysia receives a subsidy from the Malaysian government. Conversely, if the government-mandated prices are higher than the total APM cost, then Petron Malaysia pays duties to the Malaysian government.

Aside from pricing, the Malaysian government also regulates the volume of diesel sales by imposing a quota on the company which sells diesel at its service stations, as well as on the customer. Diesel sales exceeding the volume permitted under the company's or customer's quotas are not eligible for government subsidies. This is to ensure that the subsidized diesel sold at service stations (meant strictly for road transport vehicles) is not illegally sold to industrial or commercial customers at unregulated prices.

The prices of 12-kg & 14-kg LPG cylinders are also regulated under the APM, while 50kg and bulk LPG prices are not covered. Despite the pandemic, the Malaysian government did not revise any regulation on fuel prices. As of report writing date, Malaysia still adopts the APM model to manage subsidy/duty on Retail R95 and Automotive Diesel Oil (ADO) volumes. Pump prices of R95, R97, and ADO are regulated and adjusted based on the movement of MOPS every week. Household LPGs in 12-kg and 14-kg cylinders likewise remained subsidized, while Industrial LPGs are fully deregulated.

Risk Management

Petron employs an enterprise-wide risk management framework for identifying, assessing, and addressing the risk factors that affect or may affect its business. Following a bottom-up approach for its risk management process, each division conducts a regular assessment of its risk profile and formulates action plans for managing identified risks. Petron has likewise established functional teams for oversight and technical assistance.

One of the major risks that could have a critical impact on the company if it occurs is the substantial disruption in operations caused by accidents, process failure, human error, or any adverse events outside of human control. Any disruption in operations may lead to facility shutdown and unplanned inventory build-up, among others. To manage this risk, Petron has a corporate-wide Health, Safety, and Environment (HSE) program that implements effective maintenance practices at its refineries, multifunctional audits, and safety inspections at the company's depots and terminals, service stations, and third-party LPG filling plants. Turnarounds are scheduled at the Bataan Refinery every four years. Since there is a cost to restarting refinery operations after a shutdown, it was then more economical for the company to restart refinery operations only after the completion of the scheduled turnaround.

Fluctuating foreign exchange rates can also have a significant effect on the company's operating results. The company is exposed to foreign exchange risk arising from its dollar-denominated purchases of crude oil and petroleum products. In addition, foreign exchange risk also arises from the sales and purchases of Petron Malaysia whose transactions are in Malaysian Ringgit, which are then converted into US dollars before being translated to its equivalent in Philippine Peso. Fluctuations in the foreign exchange rate would result in the revaluation of key assets, and liabilities and may have a negative impact on the company's bottom line. To mitigate foreign exchange risk, Petron enters into hedging transactions and substitutes its dollar-denominated liabilities with peso-based debt. The company also enters into short-term forward currency contracts to hedge its currency exposure on crude oil importations.

Any change in the relative prices of input crude oil and output refined petroleum products, particularly when mismatched, may produce significant volatility in the company's profit margin and cash flows. Such could also result in higher financing expenses. To mitigate this risk, the company implements commodity hedging for crude and petroleum products. The hedges are intended to protect crude inventories from risks of downward prices and squeezed margins. Petron's hedging policy includes the use of commodity price swaps, time-spreads, and put options, among others. In addition, Petron arranges long-term contracts for some of its fuel and petroleum products, as these provide a partial hedge on future cash flow uncertainty.

Other Key Matters

Dispute with the Philippine National Oil Company (PNOC)

In October 2017, Petron filed a complaint against the PNOC for the reconveyance of various landholdings it declared as property dividends to PNOC in 1993. These landholdings consist of the refinery lots in Limay, Bataan, 23 bulk plant sites, and 66 service station lots located in different parts of the country. As a result of the government-mandated privatization of the company in 1993, these landholdings were conveyed by Petron to PNOC. The Deeds of Conveyance, however, provided for an automatic renewal of lease agreements between Petron and PNOC for Petron's continued long-term use of the conveyed lots for its business operations.

The complaint stemmed from PNOC's refusal to honor both the automatic renewal clause in the lease agreements for the bulk plants and the service station sites, as well as the renewed lease agreement for the refinery lots. This was on the alleged ground that such lease agreements were grossly disadvantageous to PNOC. In the complaint filed by Petron, the company alleged that PNOC committed a fundamental breach of contract by unilaterally setting aside the renewal clause of the lease agreements.

Petron management said that a court-mandated mediation conference took place on February 5, 2018. It was, however, terminated without any agreement between Petron and PNOC. In 2019, the case proceeded to the trial court. Petron then filed a motion for a summary judgment where Petron claimed that there is no genuine issue of material fact. The trial court granted Petron's motion and issued a decision in favor of the company, ordering the return of the properties to Petron. The case then moved to a reconsideration with Petron asking for PNOC to return the leases the company paid since 1993. The trial court denied both motions; subsequently, both parties went up to the Court of Appeals.

In November 2020, a trial court granted Petron's motion for summary judgment and ordered the rescission of the Deeds of Conveyance related to leased premises that the company conveyed to PNOC in 1993. The court also ordered the reconveyance of the properties to Petron and the payment of P143,000 to PNOC with legal interest from 1993. Petron sought partial reconsideration of the judgment to include an order directing PNOC to return all lease payments made since 1993. Both PNOC and Petron filed notices of appeal after the trial court denied their motions for reconsideration. In December 2021, the Court of Appeals dismissed both appeals and upheld Petron's position that PNOC breached its contractual obligation under the lease agreements. The Court of Appeals ruled that Petron should pay PNOC the rentals for the use and enjoyment of the properties. Petron filed a motion for reconsideration on January 11, 2022, but the Court of Appeals denied it in October 2022. In December 2022, PNOC filed a petition for review on certiorari[2] with the Supreme Court. As of December 31, 2022, Petron is awaiting orders from the Supreme Court and has decided not to pursue a petition for review on the issue of rental payments.

Effect of COVID-19 and Impact of Russia - Ukraine Conflict

Petron, which is in the fuel business, was negatively impacted by the pandemic and lockdowns, resulting in reduced economic activities and travel restrictions. The global oil prices also plunged due to the price war and demand disruption caused by COVID-19. Recovery in oil prices, however, was seen in May 2020 due to output cuts agreed upon by the Organization of the Petroleum Exporting Countries (OPEC) and Russia. The gradual opening-up of economies and vaccination efforts led to the recovery of demand reaching pre-pandemic levels by 4Q2021. China's continued zero-tolerance policy against COVID-19, however, affected its economy, causing a drop in oil demand in 2022.[3] The invasion of Ukraine by Russia in February 2022 resulted in a sudden escalation in oil prices, with Dubai crude breaching the USD100/bbl mark by March 2022. The Company's sales volume grew substantially in 2022, and total revenues almost doubled the 2021 level to P857.6 billion. Despite market volatility and elevated costs, the robust refining margins allowed the Company to realize a net income of P6.7 billion, higher as last year's net income level.

Market and Competition

Philippines

Based on the data from DOE, as shown in the table below, Petron continued to lead the local oil industry in 1H2023, accounting for a market share of 23.2%. This was an increase compared to the full-year 2021 level, but still lower than the company's market share from 2017 to 2019. During those years, the market share percentages for Petron Corporation were as follows: 27.6% in 2017, 26.4% in 2018 and 24.6% in 2019. In 2021, the company's market share stood at 19.2%.

[2] Certiorari is a court process to seek judicial review of a decision of a lower court or government agency.

[3] https://www.aljazeera.com/economy/2022/5/2/oil-falls-as-chinas-covid-restrictions-threaten-fuel-demand

Table 3 Market Share Per Industry Player

Company (%)	2017	2018	2019	2020	2021	1H 2023
Petron Corporation	27.6	26.4	24.6	20.1	19.2	23.2
Pilipinas Shell	20.0	18.5	18.5	18.0	15.0	15.6
Chevron Philippines	7.0	7.9	7.6	5.8	5.3	4.4
Independent Oil Players	36.8	39.1	43.0	48.8	52.7	51.6
Other Independent Oil Players						
Phoenix	6.2	6.9	7.1	7.1	7.5	1.4
Unioil	2.8	3.4	4.9	6.9	7.5	8.3
Insular	N/A	2.7	3.5	4.4	7.5	6.6
Seaoil	5.1	4.7	5.1	5.4	7.5	7.7
End Users	8.6	8.1	6.4	7.3	7.9	5.3

Pilipinas Shell, on the other hand, had a slight increase in market share to 15.6% in 1H2023 from 15.0% in 2021. Chevron Philippines' market share decreased from 5.3% in 2021 to 4.4% in 1H2023. Independent oil players continued to dominate the market, with their combined market share accounting for more than half of the industry at 51.6%. End users' market share fell to 5.3%.

In relation to the LPG industry, Petron experienced a dip in market share in 2020, dropping from the top spot to third place. The company, however, made a strong comeback in 1H2023, regaining its position as the market leader. In 1H2023, Petron held 23.7% of the total LPG demand. Liquigaz held the second largest market share at 19.1%, followed by South Pacific, Inc. (SPI) with a share of 16.0%. Pryce Gases and Isla Gas followed with shares of 15.6% and 12.9%, respectively. Phoenix LPG had a market share of 7.8%, while Peak Fuel held 4.2%.

The deregulation of the Philippine oil industry in 1998 resulted in the industry having low barriers to entry. Since then, more than 90 smaller players have entered the market, resulting in keener competition. As the smaller players tend to engage in price wars and aggressive discounting, they are attracting more and more customers. In particular, public utility vehicles, logistics, and hauling companies tend to look for gasoline stations that would offer them the lowest price. Nevertheless, Petron's advantage lies in its extensive retail and distribution network, terminals, and airport installations strategically located nationwide.

Malaysia

Based on the company's estimates, Petron Malaysia held a 20.3% share in the country's total petroleum market in 2022. Such was a slight increase compared to the 20.2% market share recorded in 2021. Petron Malaysia's major competitors include the following: Petronas Dagangan Berhad (Petronas), Shell Malaysia Trading Sdn Bhd (Shell Malaysia), and Chevron Malaysia Limited.

According to management, they are currently the third top player in the Malaysian market. This is attributed to the sustained runs of the Port Dickson refinery, complemented by the additional services provided to customers in the retail service stations for a one-stop service experience. Such services include the availability of food and beverage via Treats convenience stores, and the option to have car wheels and windshields washed and cleaned by the gasoline station staff. The Petron service stations in Malaysia are also GTSPs for customers to report local crimes.

Ownership and Management

As of September 30, 2023, Petron had two principal common shareholders namely: SEA Refinery with 50.1% of Petron's common shares and SMC with 18.16%. The remaining 31.74% shares were held by others including the public.

SEA Refinery is 100%-owned by SMC, allowing SMC to hold an aggregate 68.26% ownership of Petron. SMC is one of the largest and most diversified conglomerates in the Philippines, with business interests in beverage, food, packaging, fuel and oil, power, and infrastructure.

Mr. Ramon S. Ang (69 years old) is the President and CEO of Petron. He is also the Vice-Chairman, President, and Chief Operating Officer of SMC. In addition, Mr. Ang is currently the Vice Chairman of GSMI and SMFB. Concurrently, he is the Chairman of SMB and SLEX; and the Chairman and CEO of SMGP. Aside from these positions, Mr. Ang is also the Chairman of Petron Malaysia companies.

Petron is seen to strongly benefit from Parent Company support given its shared directors and executive officers with SMC and other affiliates. In addition, the company has a highly capable and experienced management team with the technical expertise needed to run the business.

As of December 31, 2022, Petron had a total of 2,171 employees, of which 77% were Philippine-based; while the remaining 23% were based in Malaysia and Singapore. Both employees in the Philippines and Malaysia have stayed in the company for an average tenure of nine years.

The Company maintains Collective Bargaining Agreements (CBAs) with three labor unions in the Philippines. The first union, Petron Employees Association, is made up of 190 members and is affiliated with the National Association of Trade Unions. Their CBA was in effect from January 1, 2023, until December 31, 2025. The second union, Petron Employees Labor Union, consists of 43 members, and their CBA is valid from January 1, 2022, to December 31, 2024. Lastly, Bataan Refiners Union of the Philippines has 329 members and is affiliated with the Philippine Transport and General Workers Organization. Their CBA is effective from January 1, 2022, to December 31, 2024. As of December 31, 2022, approximately 25% of the Company's workforce in the Philippines were covered by CBAs.

In Malaysia, the Company has CBAs with two labor unions. The first is National Union of Petroleum & Chemical Industries Workers and PMRMB/PFISB. The signed CBA took effect on January 1, 2023, and will remain in force for three years. This union currently represents 137 workers. The second union, Sabah Petroleum Industry Workers Union, has eight members, and their existing CBA is valid from May 1, 2020, to April 30, 2023. Negotiations between the Sabah Petroleum Industry Workers Union and POMSB for new terms are scheduled to take place in July 2023. As of December 31, 2022, around 25% of the Company's employees in Malaysia were covered by CBAs.

It is worth noting that the Company has not encountered any significant strikes or work stoppages related to employee relations for over 20 years. Such is seen as an indication of the Company maintaining a positive relationship with its employees.

Strategy

Petron will continue to focus on volume growth, efficient operations, and optimal use of assets amid a challenging business environment. To ensure business sustainability, the company will continue to implement the following strategies: (1) maximize the production of high-margin refined petroleum products and petrochemicals; (2) ensure reliability and efficiency of refinery operations; (3) maximize volume growth and further increase market share in the downstream oil markets in the Philippines and Malaysia; (4) innovation as a tool for customer retention and growth; and (5) continue to evaluate possible selective synergistic acquisition.

In recent years, Petron has made a strategic shift in its production by transitioning from lower-margin fuel oils to higher-margin products. The company continues to invest in upgrading its production capabilities, focusing on the development of higher-margin petroleum products and petrochemicals.

Petron aims to enhance operational efficiency and reduce production costs. This includes improving crude optimization and expanding the sources of crude oil supply. Investments are also being made to enhance receiving and storage facilities, as well as to improve existing infrastructure. Additionally, the company focuses on managing crude oil freight costs and ensuring the availability of terminal-compliant vessels. Distribution costs are being reduced through the optimization of the terminal network.

The company is likewise offering competitive prices to stimulate volume growth. It aims to optimize retail outlets for fuels, LPG and lubricants, while improving the productivity of its existing service station network. Petron plans to introduce new products with differentiated and superior qualities, expanding its lubricants distribution network through additional sales channels. Furthermore, the company is actively expanding its non-fuel business segment and intensifying training programs for dealers and sales personnel.

Petron is investing in digital offerings, such as the Petron App, and adopted contactless payment solutions through PayMaya at more than 1,600 service stations nationwide. Moreover, Petron is open to considering and evaluating selective opportunities for expansion both within and outside the Philippines through strategic acquisitions. The aim is to create operational synergies and add value to the existing business, while ensuring a careful assessment of each opportunity.

Petron has also taken strategic steps to enhance its operations by establishing a logistics company and successfully implementing its service integration program. Previously, the company relied on third-party providers for logistics support. However, in the middle of last year, Petron made a significant investment by purchasing 300 new trucks to augment its existing fleet and reduce dependency on external services.

FINANCIAL RISK

Analyst's Note: PhilRatings' calculation of certain financial metrics may differ from that of the Company.

Table 4 Financial Highlights

in millions PHP (except Sales Volume and ratios*)	2021	2022	9M2023
Sales Volume (in million barrels)	82.2	112.8	93.6
Sales Revenues	438,057	857,638	587,283
Cost of Goods Sold	407,558	823,788	548,913
Gross Profit	30,499	33,850	38,370
Selling & Administrative Expenses	14,557	16,175	12,617
EBITDA	26,589	32,173	34,661
Interest Expense	10,008	13,094	13,706
Net Income	6,136	6,697	9,508
Gross Profit Margin (%)	7.0	3.9	6.5
Net Profit Margin (%)	1.4	0.8	1.6
EBITDA Interest Cover Ratio (x)	2.7	2.5	2.5

Profitability

2022 vs. 2021

For the year ended December 2022, Petron's total revenue went up by 95.8% to P857.6 billion, compared to the previous year's P438.1 billion. The jump in revenue was driven by the significant increase of 37.2% in sales volume from 82.2 million barrels in 2021 to 112.8 million barrels in 2022. The rise in sales volume was attributed to the significant upturn in commercial sales, especially in the industrial and aviation sectors. This was supported by the improvements in domestic travel and overall business activities. In addition, the retail sales of Petron in the Philippines and Malaysia combined have shown a positive increase of 26%. Meanwhile, the trading volume of PSTPL has more than doubled, and the sales of polypropylene have substantially increased due to the resumption of its plant's operations in 2022.

Cost of goods sold also increased by 102.1%, from P407.6 billion in 2021 to P823.8 billion in 2022. This was largely attributed to the spike in benchmark Dubai crude oil prices, which averaged USD96/bbl in 2022 compared to USD69/bbl in 2021.

Petron's gross profit for the year increased by 11.0% to P33.9 billion. Gross profit margin decreased from 7.0% in 2021 to 3.9% in 2022, however, as cost of goods sold increased faster than revenues.

Selling and administrative expenses increased by 11.1%, from 14.6 billion in 2021 to P16.2 billion in 2022. This was mainly driven by higher maintenance and repairs related to service stations, terminals and information technology, outsourced services, advertising expenses and employee costs. Other operating income also increased by 20.8% to P1.5 billion, primarily due to higher rental income.

Interest expense and other financing charges increased by 30.8%, from 10.0 billion in 2021 to P13.1 billion in 2022. Such was on account of higher borrowing levels due to the increase in working capital requirements, as well as higher average interest rates. Interest income increased by 59.2% to P0.9 billion on account of higher average placements and interest rates versus previous year. Income tax expense also increased by 20.9% to P1.4 billion.

Backed by higher sales volume, Petron's consolidated net income for 2022 was at P6.7 billion, a 9.1% increase from the previous year's P6.1 billion. Net profit margin, however, decreased from 1.4% in 2021 to 0.8% in 2022. ROAA of 1.5% was slightly lower than the prior year's 1.6%.

9M2023 vs. 9M2022

In 9M2023, Petron's sales revenues declined by 6.9% to P587.3 billion, from P631.1 billion in the same period last year. Despite recording a higher sales volume, the company's topline was lower due to the continued correction in oil prices, from record-high levels amid the invasion of Ukraine by Russia.

In line with the decrease in sales revenues, Petron's cost of goods sold fell by 9.2%, from P604.4 billion in 9M2022 to P548.9 billion in 9M2023, on account of lower cost per liter. Benchmark Dubai crude dipped by 18.0%, from USD100/bbl in 9M2022 to USD82/bbl in 9M2023. As a result, gross profit posted a significant gain of 43.4%, from P26.8 billion in 9M2022 to P38.4 billion in 9M2023.

Selling and administrative expenses increased by 10.9%, from P11.4 billion in 9M2022 to P12.6 billion in 9M2023. The growth was due to higher maintenance and repairs at the service stations, more LPG cylinders purchased during the period, and increased spending for promotional activities. Interest expense and other financing charges likewise jumped by 55.3%, from P8.8 billion in 9M2022 to P13.7 billion in 9M2023, due to interest rate hikes, coupled with higher average borrowing levels.

Petron also recorded Other Expense amounting to P1.9 billion in 9M2023, a reversal from last year's Other Income of P1.4 billion. Such was on account of losses in mark-to-market of commodity hedges and net foreign exchange-hedging this year versus gains recorded in 9M2022.

Given the aforementioned, the company reported a net income of P9.5 billion, an increase of 16.2% compared to the P8.2 billion registered in the same period last year. Gross and net profit margins increased to 6.5% and 1.6%, respectively.

2023 Full-Year Performance[4]

Petron sold 126.9 million barrels in 2023, higher by 12.5% than the 112.8 million barrels sold in 2022. The growth was attributable to the significant growth in the Company's Jet Fuel and LPG sales, coupled with higher production at its Bataan and Port Dickson refineries. Despite higher sales volume, Petron posted lower revenues during the period at P801.0 billion, down by 6.6% from the P857.6 billion recorded in the previous year. Such was due to price correction as full year average price of benchmark Dubai crude was USD82/bbl in 2023, a 14.6% decline from USD96/bbl in 2022. Nevertheless, Petron was able to record 50.7% growth in its net income, from P6.7 billion in 2022 to P10.1 billion in 2023, driven by the Company's efforts to capture the continued recovery in demand and respond to market volatility.

Projected Period

Petron forecasts an improvement in its bottom line over the projected period. Despite an anticipated slowdown in sales, margins are seen to improve as cost of goods sold, as well as selling and administrative expenses, will be more manageable. Interest expense, however, is projected to slightly grow due to the high interest rate environment.

[4] Based on the press release of Petron dated March 5, 2024. Petron has yet to release its 2023 Audited Financial Statements, as of report writing date.

PhilRatings notes that the Philippine market will continue to account for more than half of the company's total sales.

Cashflow and Liquidity

Table 5 Cash Flow Items and Ratios

in million PHP (except ratios)	2021	2022	9M2023
Cash and Cash Equivalents	36,406	37,183	28,633
Operating Cash Inflows (Outflows)	(10,668)	(22,661)	22,412
Investing Cash Inflows (Outflows)	(9,759)	(2,382)	(4,889)
Financing Cash Inflows (Outflows)	28,098	22,794	(25,940)
Current Ratio (x)	0.99	1.07	1.02
Debt Service Coverage Ratio (x)	0.19	0.20	0.21
EBITDA Interest Coverage Ratio (x)	2.66	2.46	2.53

2022 vs. 2021

Cash and cash equivalents increased from P36.4 billion in 2021 to P37.2 billion in 2022. The company's net cash outflows from operations, however, increased significantly from P10.7 billion in 2021 to P22.7 billion in 2022. During the year, cash generated from operations was used to fund the P13.1 billion in interest and tax payments, P5.68 billion spending for various refinery, terminal, and service station capital projects, and to partly cover the increase in working capital requirement of P 38.3 billion.

Petron's investing activities showed a different trend, with the cash outflow decreasing from P9.8 billion in 2021 to P2.4 billion in 2022. Such covered for the shortfall in funding given higher working capital requirements. Net cash provided by financing activities also decreased from P28.1 billion in 2021 to P22.8 billion in 2022 due to higher loan payments compared to the previous year.

Petron's liquidity position improved in 2022, ending the year with a slightly higher current ratio of 1.1x compared to 1.0x a year ago. The company's Long-term Debt Service Coverage Ratio also improved from 0.8x in 2021 to 1.2x in 2022. EBIT interest coverage ratio had a minimal decline from 1.7x in 2021 to 1.6x in 2022, but remains at a healthy level.

9M2023 vs. 9M2022

Petron generated a positive operating cash flow of P22.4 billion in 9M2023, a significant improvement from the P25.9 billion outflow recorded in the same period last year. Cash generated from operations amounting to P36.0 billion was more than adequate to cover interest and taxes, and partially pay outstanding loans.

Net cash flows used in investing activities stood at P4.9 billion, mainly attributed to the acquisition of property, plant and equipment. Meanwhile, Petron had a financing outflow of P25.9 billion, primarily due to the repayment of loans and redemption of capital securities.

As a result, the company's cash and cash equivalents declined by 23.0% to P28.6 billion as of September 30, 2023. EBITDA interest coverage ratio remained more than sufficient at 2.5x. Debt service coverage ratio (DSCR), however, was still below 1.0x. Nevertheless, current ratio was stable at 1.0x.

Projected Period
Current ratio is expected to slightly decline over the projected period due to lower cash and cash equivalents. Despite such, PhilRatings notes that the company will still continue to have access to enough cash and existing bank lines to fund future expenses, particularly interest expense and debt payment.

According to management, Petron's rated bonds Series B (P7.0 billion) and Series C (P13.2 billion), which will mature in 2023 and 2024, respectively, will be paid using available cash and, if needed, through the availment of additional loans.

Capital Adequacy

Table 6 Balance Sheet Items and Ratios

in million PHP (except ratios)	2021	2022	9M2023
Total Assets	407,420	460,071	456,927
Total Liabilities	296,507	346,521	355,052
Total Debt	211,841	244,947	240,987
Total Equity	110,913	113,550	101,875
Debt to Equity Ratio (x)	1.9	2.2	2.4
Total Debt to Capitalization (%)	65.6	68.3	70.3
Solvency Ratio (x)	1.4	1.3	1.3

2022 vs. 2021
Petron's total assets as of December 31, 2022, amounted to P460.1 billion, which represents an increase of 12.9% compared to the previous year. The company's higher asset base can be attributed to higher volumes and prices of crude and finished products. Property, plant and equipment was stable at P170.2 billion in 2022. Trade and other receivables increased by 58.4%, while inventories increased by 26.1%.

Total liabilities increased by 16.9% to P346.5 billion as of December 31, 2022. The increase was mainly due to higher debt levels and higher payables for crude oil and petroleum products as the company increased its inventory levels to meet higher demand. Petron's solvency ratio decreased slightly to 1.3x in 2022.

Petron's total equity increased by 2.4% to P113.6 billion as of December 31, 2022. The company's debt to equity ratio increased from 1.9x to 2.2x as of December 31, 2022 due to the increase in total debt. Petron's total debt to capitalization ratio likewise increased from 65.6% to 68.3%.

9M2023 vs. 2022
Total assets stood at P456.9 billion as of end-September 2023, a marginal decrease of 0.7% from P460.1 billion as of end-2022. In contrast, total liabilities increased by 2.5%, from P346.5 billion as of end-2022 to P355.1 billion as of end-September 2023. The growth was mainly due to higher outstanding liabilities to vendors and suppliers, as well as availment of long-term loans, net of maturities paid during the period. Petron's total debt was lower by 1.6%, from P244.9 billion as of end-2022 to P241.0 billion as of end-September 2023.

The company's total equity contracted by 10.3% to P101.9 billion as of end-September 2023, from P113.6 billion as of end-2022. This was mainly on account of the company's full redemption of its US$500 million Senior Perpetual Capital Securities.

Debt to equity ratio increased to 2.4x as of end-September 2023, primarily due to the increase in total liabilities. Furthermore, total debt to capitalization ratio moved to 70.3%.

Projected Period
Over the projected period, Petron is expected to maintain its focus on gradually lowering its debt levels, which will lead to improved financial stability and long-term growth. As such, debt to equity ratio will further improve as the company pays off its maturing debt obligations.

Financial Flexibility
As of report writing date, Petron had a significant amount of available credit facilities with various banks. Moreover, the company is listed in the Philippine Stock Exchange (PSE) and had a market capitalization of P29.4 billion as of April 4, 2024. Petron may tap the domestic equity market should the need arise.

ECONOMY
2023[5]
GDP growth in the last quarter of 2023 was logged at 5.6%, bringing full-year GDP growth to 5.6% in 2023. This was behind the government's target GDP growth of 6% to 7% for the year. The industries that contributed most to the annual growth were: Wholesale and Retail Trade, Repair of Motor Vehicles and Motorcycles (5.5%); Financial and Insurance Activities (8.9%); and Construction (8.8%).

All major economic sectors posted full-year increases, as follows: Agriculture, Forestry, and Fishing (1.2% YoY and 1.4% in 4Q 2023); Industry (3.6% YoY and 3.2% in 4Q 2023); and Services (7.2% YoY and 7.4% in 4Q 2023).

On the demand side, annual growth of Household spending was at 5.6% (5.3% in 4Q 2023) while Government spending minimally rose by 0.4% (-1.8% in 4Q 2023) for the year. According to NEDA Secretary Arsenio Balisacan, the latter's slower expansion was intentional as the government aims to achieve fiscal consolidation. This meant prioritizing reduction of fiscal deficit and government debt. Data from the Bureau of the Treasury showed an improved debt-to-GDP ratio of 60.2% in 2023, from 60.9% at the end of 2022.

Despite falling behind the target GDP growth in 2023, the Philippines was still among the top performing countries in Asia. NEDA Secretary Balisacan shared that the Philippines recorded the second highest growth among some Asian countries that released their performances in 2023 (as of January 2023). On the top spot was Vietnam which posted a growth of 6.7% in 2023. Third was China and followed by Malaysia, posting expansions of 5.2% and 3.4%, respectively.

GDP growth target for 2024 was set at 6.5% to 7.5%, nominally down from the previous goal of 6.5% to 8% growth for this year.

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[5] Sources: https://www.pna.gov.ph/articles/1217973
https://www.psa.gov.ph/content/gdp-expands-56-percent-fourth-quarter-2023-brings-full-year-2023-gdp-growth-rate-56-percent

Inflation

Inflation in February 2024 broke the its four-month downtrend, going up to 3.4% (from 2.8% in January 2024) on the back of higher prices for key food items, particularly rice. The figure, however, still fell within the BSP projection of 2.8-3.6%. It also marked the third straight month that inflation was kept within the government's 2-4% target range.

The target inflation rate for full-year 2024 was pegged within the range of 2% to 4%. First Metro Investment Corporation (FMIC) and the University of Asia and the Pacific (UA&P) forecast that inflation will settle at 3.8% in 2024. This forecast was based on the slightly lower trend in crude oil prices, while imports and better second half harvests will limit rice price gains. The price of rice notably increased further by 22.6% in January from 19.6% in December 2023. The ASEAN+3 Macroeconomic Research Office (AMRO) also forecasts Philippine inflation at 3.6% in 2024, likewise within the government's target.

INDUSTRY[6]

In the Philippines, there are a total of 151 storage facilities strategically located across different regions. Out of these, 59 are import terminals, including Petron Refinery's storage facility, while the remaining 92 are distribution depots. The combined storage capacity of these facilities is 41,634 MB. Of the total storage capacity, 9,609 MB or 23.08% is allocated to refinery storage owned by Petron Corporation's Bataan Refinery in Limay, Bataan. Such comprises crude oil, intermediate stocks, and finished petroleum products. The remaining storage capacities of 26,602 MB or 58 import terminals are dedicated to receiving imported finished petroleum products, while the 5,422 MB or 92 depots serve as distribution facilities owned by various downstream oil players. It's worth mentioning that the number of depots has decreased due to some reported depots being converted into LPG refilling plants.

Supply

As of end-December 2022, the reported stock of crude oil stood at 250 million liters (ML), while finished petroleum products, excluding biofuels, amounted to 1,901 ML. Breaking it down by product, the stocks were as follows: gasoline at 507 ML (equivalent to 25 days' supply), diesel oil at 742 ML (equivalent to 24 days' supply), kerosene at 13 ML (equivalent to 64 days' supply), jet A1/Avturbo at 141 ML (equivalent to 27 days' supply), fuel oil at 104 ML (equivalent to 30 days' supply), LPG at 159 ML (equivalent to 17 days' supply), and other products at 235 ML (57 days' supply).

In 2022, the country imported a total of 6,892 ML of crude oil, reflecting a 46.0% increase compared to the 2021 volume of 4,721 ML. This increase in crude oil imports was primarily due to the normal operation and recovery of the refinery after its shutdown in 2021. Additionally, the country's economic recovery, expansion of public transport capacity, and the removal of travel restrictions also contributed to the increase.

All the crude oil imported during the period came exclusively from the Middle East, with Saudi Arabia being the major supplier, accounting for 52.5% (3,619 ML) of the total. The United Arab Emirates (UAE) followed with a 30.8% share (2,126 ML), Iraq with an 11.0% share (757 ML), and Kuwait with a 5.7% share (310 ML).

From January to December 2022, the total imports of petroleum products amounted to 19,588 ML, representing a marginal decrease of 0.68% compared to the previous year's level of 19,721 ML. Among

[6] https://www.doe.gov.ph/taxonomy/term/74
https://www.trade.gov/energy-resource-guide-philippines-oil-and-gas

the products, avturbo imports saw the most significant increase of 114.6%, while diesel and fuel oil grew by 1.0% and 0.4% respectively. Conversely, kerosene, LPG, and gasoline imports dropped by 50.4%, 4.7%, and 3.4% respectively.

The top supplier of imported finished petroleum products in the country was South Korea, accounting for 30.7% of the total imports, followed by Singapore with a 22.3% share. China held a 15.4% share, Malaysia accounted for 9.5%, and Japan had a 6.3% share. Other countries such as Taiwan, Brunei, Qatar, Russia, Thailand, India, UAE, Algeria, Kuwait, USA, Australia, Nigeria, Saudi Arabia, and other countries contributed to the remaining percentage.

The product import mix was primarily comprised of diesel oil at 41.4%, gasoline at 25.2%, LPG at 15.3%, avturbo at 5.8%, fuel oil at 5.8%, kerosene at 0.2%, and other products at 6.5% share. Gasoline imports met 66.2% of the gasoline demand, while diesel oil imports satisfied 72.6% of the diesel demand. LPG imports accounted for 87.4% of the LPG demand. In total, the product imports fulfilled 73.08% of the total product demand.

Additionally, ethanol imports increased by 22.9% from 225 ML in YTD December 2021 to 277 ML in 2022. This rise can be attributed to the requirement set by Republic Act No. 9367 of 2006, which mandates that all gasoline sold in the country should contain 10% bioethanol content (E-10).

The refinery production output from January to December 2022 saw a significant increase of 52.2% compared to the same period in 2021, rising from 4,577 ML to 6,968 ML. This surge in production output can be attributed to the normal operation and recovery of the refinery after its scheduled maintenance shutdown in 2021. On a per-product basis, gasoline production output increased by 56.6%, diesel by 39.3%, LPG by 37.6%, kerosene by 13.4%, and avturbo by a significant 152.7% to meet the growing demand. Other products such as naphtha, propylene, mixed xylene, toluene, benzene, petroleum coke, and sulfur also showed an increase of 47.4% compared to the volume in YTD December 2021. Fuel oil production output, however, experienced a significant decrease of 75.5%.

The production mix was dominated by diesel oil with a share of 39.4%, followed by gasoline and avturbo with 25.6% and 12.1% respectively. LPG, kerosene, and fuel oil held shares of 5.5%, 0.4%, and 0.10% respectively, while other products accounted for 16.8% of the production mix, including naphtha, mixed xylene, propylene, benzene, toluene, petroleum coke, and sulfur.

Demand

The total demand for petroleum products in the Philippines in 2022 reached 26,803 ML, showing a 9.2% increase compared to the previous year's figure of 24,553 ML. This translates to an average daily requirement of 73.4 ML, up from 67.3 ML in the previous year. The growth in demand can be attributed to increased economic activity and the relaxation of travel restrictions nationwide.

Compared to the same period in 2021, the demand for diesel oil increased by 5.4%. Similarly, fuel oil, gasoline, and LPG experienced growth rates of 12.3%, 10.1%, and 5.4% respectively. With the easing of travel restrictions, avturbo demand surged by 112.8%. kerosene demand, however, declined by 20.5%.
In terms of the product demand mix, diesel oil continued to dominate with a share of 41.7%, followed by gasoline at 27.8%, LPG at 12.8%, avturbo at 7.2%, fuel oil at 4.7%, kerosene at 0.3%, and other products (such as asphalts, avgas, condensate, solvents, naphtha, petroleum coke, and mixed xylene) accounting for a 5.7% share in the total product demand mix.

Regionally, the National Capital Region (NCR) had the highest share of petroleum product demand, accounting for 28.55% of the total market. South Luzon and North Luzon followed with shares of 21.99% and 20.4% respectively, while Mindanao captured 15.35% of the market. The remaining 13.71% was in the Visayas region.

In terms of trade classification, 33.25% of the total trade demand was distributed to the Reseller Trade, which involves volume sold to retail outlets. Industrial/Commercial Trade accounted for 55.2% of the demand, representing volume sold directly to commercial, industrial, transport, power generation, and agriculture sectors. The remaining volumes were distributed to International Trades (6.1%), Independent Refillers (5.05%), Philippine Government (0.40%), and Foreign Embassies (0.0012%).

The total export of petroleum products from the Philippines in the year-to-date period ending in December 2022 decreased by 29.9%, amounting to 500 ML compared to 713 ML in the same period of 2021. The product export mix included mixed xylene (21.5%), naphtha (20.2%), propylene (16.2%), toluene (13.5%), molten sulfur (10.6%), gasoline (6.7%), fuel oil (6.6%), and benzene (4.7%).

The majority of the country's product exports were destined for China, accounting for 40.9% of the export share. Malaysia followed with an export share of 22.7%, while Singapore, Taiwan, and Korea had export shares of 8.1%, 7.96%, and 7.8% respectively. Other export destinations included India (5.8%), Vietnam (3.6%), Indonesia (2.9%), and Japan (0.4%).

The total crude oil exported by the Philippines as of the year-to-date period ending in December 2022 was 76 ML, representing a decline of 24.1% compared to 100 ML in the same period of 2021. The exported crude oil was primarily destined for Korea and Thailand.

The Department of Energy in the Philippines has set an ambitious goal to achieve energy security and implement power market reforms. By 2040, the country plans to increase production and reserves of local oil, gas, and coal, improve policies for downstream oil industries, and establish a natural gas industry with investment opportunities. The goal is to compensate for the impending depletion of the Malampaya natural gas fields by finding alternative energy sources to maintain economic growth and infrastructure development. Offshore investment and liquefied natural gas (LNG) infrastructure development are being encouraged, but there are concerns about low foreign investment due to issues of contract sanctity and lack of incentives. The Philippines risks facing an energy crisis if it cannot address the challenges in offshore exploration and LNG development.

Malaysia[7]

The oil and gas sector in Malaysia experienced a strong performance in 2022, largely driven by higher oil prices, particularly in the early months. Malaysia's national oil company, Petronas, is on track to meet its RM100 billion earnings target for the financial year 2022, benefiting from geopolitical factors such as the war between Russia and Ukraine, which caused a surge in oil prices to over USD120/bbl in March. This was a significant increase from the starting price of around USD80/bbl. However, oil prices softened towards the end of the year.

The war between Russia and Ukraine resulted in Western nations imposing bans on imports of Russian oil and gas, leading to a global spike in oil prices. The United States and the United Kingdom, in particular, restricted imports following Russia's invasion of Ukraine. The tight supply situation was further

[7] https://www.nst.com.my/business/2023/01/866628/malaysias-og-posts-one-best-performances-2022

compounded when OPEC decided to reduce production by 100,000 barrels per day, contrary to its earlier plan to increase production by 275,000 barrels per day.

The geopolitical factors had an impact on Malaysia's oil and gas listed firms, as reflected in the Bursa Energy Index. The index reached its highest level in May at 864.15 points due to higher crude prices but dropped to its lowest level at 604.64 in mid-July amid concerns of a global recession and interest rate hikes to control inflation.

Despite the challenges, it has been a favorable year for the oil and gas companies, with profits being generated from the rebound in economic activity in key markets and supply disruptions caused by the Russia-Ukraine war. Experts, however, anticipate a more challenging year ahead for the sector in 2023, with expectations of a slowdown in economic activity due to ongoing interest rate increases aimed at curbing inflation.

The International Energy Agency's latest report indicates signs of a contraction in crude oil demand in the fourth quarter of last year, which contributed to the decline in Brent and WTI crude prices. Demand for LNG, however, remains high as Europe seeks alternative energy sources, creating opportunities in the LNG market for the coming year. Additionally, local oil and gas players are expected to benefit from the increase in domestic capital expenditure by Petronas. Companies such as Yinson Holdings Bhd, Dialog Group Bhd, and Hibiscus Petroleum Bhd are likely to benefit from the 34% year-on-year increase in Petronas' domestic capex.

Annex A: Subsidiaries, as of December 31, 2023

Company Name	Business Description	Equity
Overseas Ventures Insurance Corporation Ltd. (Ovincor)	Reinsurance	100%
Petron Freeport Corporation (PFC)	Wholesale or retail sale of fuels, operation of retail outlets, restaurants and convenience stores, and the manufacture of fuel additives	100%
Petron Marketing Corporation (PMC)	Wholesale or retail sale of fuels, operation of retail outlets, restaurants and convenience stores with pharmaceutical items, and bakeries	100%
Petrofuel Logistics, Inc. (PLI)	Hauling and logistics.	100% indirect interest
Petrochemical Asia (HK) Limited (PAHL)	Investment holding	100%
Petron Finance (Labuan) Limited (PFL)	Investment holding	100%
Petron Global Limited (PGL)	Investment holding	100%
Petron Singapore Trading Pte. Ltd. (PSTPL)	Trading	100%
Petron Oil & Gas Mauritius Ltd. (POGM)	Investment holding	100%
Petron Oil and Gas International Sdn Bhd (POGI)*	Investment holding	100% indirect interest
Petron Malaysia Refining and Marketing Bhd (PMRPMB) *	Manufacturing and marketing of petroleum products in Peninsular Malaysia	73.4% indirect interest
Petron Fuel International Sdn Bhd (PFISB) *	Marketing of petroleum products in Peninsular Malaysia	100% indirect interest
Petron Oil (M) Sdn Bhd (POMSB)*	Marketing of petroleum products in East Malaysia	100% indirect interest
New Ventures Realty Corporation (NVRC)	Purchase and sale of properties suitable for use as service station sites, bulk plants or sales offices	86%
Mema Holdings, Inc.	Investment Holding	100%

Collectively referred to as **"Petron Malaysia"*