

China Petroleum & Petrochemicals Industry – Global oil price hovering within a narrow band amid spiking tensions over the Iranian nuclear issue

- ❖ **Event:** During the Chinese New Year holiday period, the prices of global oil futures continued to hover within a narrow band. On 27 Jan 2012, the NYMEX light crude oil futures and ICE Brent futures (both for delivery in March) closed at US\$99.56/bbl (+1.3% WoW) and US\$111.46/bbl (+1.5% WoW).
- ❖ Iran's strong response to sanctions spiked geopolitical tension. On 23 Jan, the EU foreign ministers' meeting decided to ban imports of Iranian crude oil and petroleum products; stop all financing and insurance services for Iran's oil trade, and ban imports of Iranian gold and other petrochemical products. Additionally, EU froze the assets of the Iranian central bank. Existing contracts can be fulfilled until July 1. Responding to the sanctions, Iran's parliament is drafting legislation calling for the government to immediately halt oil exports to EU countries. The bill would also require Iran to embargo imports from countries participating in the EU ban.
- ❖ Iran's retaliation would lead to a lose-lose situation. With abundant oil and gas resources, Iran is the world's fourth largest oil producer and OPEC's second largest oil exporter. Its current daily export of ~2.6mn barrels account for 62% of its total crude output. Petroleum is the lifeline of Iran's economy and generates the bulk (85%-plus) of its total foreign income. EU's crude oil imports from Iran totals ~500,000 barrels per day (Italy, Spain and France lead other EU members in this respect). According to latest media reports, voting on the proposed bill submitted to the Iranian parliament to cut oil exports to EU, scheduled on 29 Jan, has been delayed. The geopolitical tension is extremely high at the moment. Once Iran implements the harsh retaliatory measures, both EU and Iran would suffer grave losses. From a supply-demand viewpoint, we do not see any base for an immediate and substantial hike in global crude price. Nevertheless, we advise closely monitoring the impact of the Iranian nuclear issue on international oil prices.
- ❖ Historically, global oil prices typically remain sensitive to geopolitical events for 1-2 years. Global oil prices are constantly subjected to geopolitical risks, especially major events in oil producing countries or countries where oil passes through. Such events have become the key factor affecting short/medium-term oil prices. The three major geopolitical events in history that greatly affected oil prices are: (i) the Arab oil embargo of 1973; (ii) the Islamic revolution of 1978-79; and (iii) the first Gulf War in 1990. Global crude surged for 1-2 years after the outbreak of each event, and the magnitudes of the price hikes were impressive. As these events came to an end, oil price would begin to pull back slowly, typically over a period of more than two years.

Peers' comparison – China Petroleum & Petrochemicals Industry (HK)

Company	Price (HK\$)	PER (x)			PEG (x)	P/B (x)	Yield (%)	RoE (%)
		10	11E	12E				
Hong Kong -average		10.7	9.6	8.5	0.9	1.3	2.8	17
Sinopec (00386.HK)	9.42	9.3	8.6	8.0	1.2	1.2	3.3	17
CNOOC (00883.HK)	15.94	10.6	8.4	8.7	1.0	1.9	4.0	23
PetroChina (00857.HK)	11.34	12.1	11.4	8.4	0.6	1.5	4.3	15
Shanghai Petrochem (00338.HK)	2.75	5.8	8.8	7.5	NA	0.8	2.7	10
COSL (02883.HK)	12.66	11.2	11.0	9.6	1.4	1.4	2.1	15
Kunlun Energy (00135.HK)	12.24	25.0	16.6	13.3	0.7	2.1	1.9	16
Yizheng Chem (01033.HK)	1.96	5.2	6.3	7.0	NA	0.6	1.9	9
MIE Holdings (01555.HK)	2.33	6.8	5.6	5.4	0.6	1.3	2.2	28

Source: Respective companies, Bloomberg, CSI

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Investment rating system

Performance of stock or sector relative to MSCI-China over next 6 months after research publications

	Rating	Remark
Stock rating	Buy	Relative performance over MSCI-China Index >20%
	Overweight	Relative performance over MSCI-China Index 5% ~ 20%
	Hold	Relative performance over MSCI-China Index -10% ~ 5%
	Sell	Relative performance over MSCI-China Index > -10%
	NR	Not rated
Sector rating	Outperform	Relative performance over MSCI-China Index >10%
	Neutral	Relative performance over MSCI-China Index -10% ~10%
	Underperform	Relative performance over MSCI-China Index > -10%

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