Edge Weekly

Cover Story: O&G stocks that could ride oil price recovery

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IT has been close to four years since crude oil — once one of the world's most prized commodities — traded near the US$100 mark. However, it still has a significant role in the movement of the Bloomberg Commodity Index with a weightage of 7.23% for Brent Crude and 7.2% for West Texas Intermediate. In other words, it is still a valuable commodity. And its impact is far-reaching, with industries such as aviation, plastics and chemicals still depending on it.

Malaysia, which derived 41% of its revenue from oil in 2009, has now reduced that dependence to 14% this year.

The low oil price environment that started in mid-2014 led national oil company Petroliam Nasional Bhd (Petronas) to undertake cost-optimisation measures in 2016, which included reducing its capex and opex by RM50 billion over four years, from 2016 till 2020.

Crude oil started to trade higher from late last year, with Brent crude oil futures hitting US$69 per barrel on Jan 26, its highest level in almost three years. However, the price retreated 7% to US$65 per barrel on Feb 20.

IQI Global chief economist Shan Saeed sees oil prices trading at between US$60 and US$87 per barrel this year, with demand touching 98 million barrels per day — mostly driven by China. According to the International Energy Agency, world oil demand stood at 96.65 million barrels per day as at the first quarter of 2017.

While there were headlines hailing the return of oil at US$100, a further read of the text shows that such a case is remote. But while oil is far from a full recovery phase, it has been trading at sustainable levels of US$60 per barrel and above since last November.

At these prices, we look at five oil and gas stocks that are likely to benefit from the recovery and stability of crude oil prices.

Dayang Enterprise Holdings Bhd

Dayang is involved in offshore topside maintenance services and the chartering of marine vessels.

MIDF Research's oil and gas analyst Aaron Tan Wei Min writes in a Dec 22, 2017, note that Dayang has a strong utilisation rate for its 25 vessels, of which 17 are from its subsidiary Perdana Petroleum Bhd.

"Average fleet utilisation for its financial year ended Dec 31, 2017 (FY2017) now stands at 53%. Dayang's current order book stands at RM3.415 billion, with long-term contracts ranging from two to five years.

"The company is also in the midst of increasing its order book, currently participating in RM8 billion worth of tenders," says Tan.

MIDF has a "buy" call on Dayang with a target price of 95 sen per share, premised on a large potential share price upside, earnings upward cycle for FY2018, an improving oil and gas industry climate with higher activity levels, improving utilisation rate as well as improving conditions for Perdana Petroleum.

Yinson Holdings Bhd

Yinson is the world's sixth largest floating production storage offloading (FPSO) service provider. A recovery in the oil and gas sector, especially upstream, could see Yinson getting more contracts for its FPSOs.

UOB Kay Hian analyst Kong Ho Meng in a Jan 30 note on the counter maintained his "buy" call, with an upgraded target price of RM4.80 from RM4.40 previously. "Our sum of total parts-based target price is mostly based on discounted cash flow on the FPSO divisions and implies a forward FY2020 price earnings of 18 times."

"For FY2019, Yinson may secure [the FPSO contract for the] Layang [field] and one new mega FPSO contract. Our valuation factors in new contract catalysts, namely 39 sen per share estimate for FPSO Layang, and the option value of 77 sen per share for a mega contract win.

"Even though we have raised our target price as our earlier option value assumed a 40% chance of a mid-sized contract win, we remain conservative on the win chance because of competition from other strong FPSO contenders," he writes.

Petronas Dagangan Bhd

Petronas Dagangan (PetDag) operates petrol stations and sells downstream oil and gas products.

MIDF's Tan believes for the fourth quarter ended Dec 31, 2017 (4QFY2017), PetDag's normalised earnings — excluding its disposals — will most likely outpace the firm's expectations by 5%.

This, he says, is premised on the higher average RON95 price of RM2.26 per litre in 4QFY2017 compared with RM2.10 per litre in 3QFY2017 and the appreciation of Brent crude oil prices .

"In addition to the expected commendable earnings, we believe that there could potentially be a special dividend or higher final dividend. The three cumulative dividends declared for FY2017 amounted to 48 sen per share.

"We believe that there could be an additional 35 sen to 40 sen declared, bringing the total dividend declared to 83 sen to 88 sen per share, with a payout exceeding 80%. This is a result of a large gain on disposal — from the disposals of a 100% stake in Petronas Energy Philippines Inc and 40% equity interest in Duta Inc — recorded in 3QFY2017," he says.

MIDF has a "buy" call on PetDag with an unchanged target price of RM28 per share.

Serba Dinamik Holdings Bhd

Serba Dinamik is an engineering solutions service provider for the oil and gas industry and stands to benefit from more operation and maintenance jobs, given its international exposure. Most of its jobs are currently in the Middle East.

UOB Kay Hian's Kong maintains his "buy" call and target price of RM3.80 in a Feb 6 note on the company.

"This is pegged to 12 times 2019 forward price earnings, at a premium to local smaller peer Deleum Bhd, given Serba's superior diversification, earnings compound annual growth rate (CAGR) of 19% to 36% and return on equity (ROE) of 24%.

"We continue to like its high growth strategies and believe that an earnings rerating will drive share price upside. We retain our target price for now pending its results announcement at the end of February," he writes.

"However, we highlighted that in a blue sky scenario, in which we assume the company will close 2018 with an order book of RM7.5 billion — implying new order wins exceeding RM3 billion — our earnings forecasts could be adjusted upwards by 16%, and target price to RM4.40," he says.

Sapura Energy Bhd

Sapura Energy is an integrated oil and gas services and solutions provider. It is engaged in providing end-to-end solutions and services to the upstream petroleum industry.

In a Feb 6 note on the counter, AmInvestment Bank analyst Alex Goh says even though the pace of offshore projects remains tepid globally, the group's order book still translates into 2.2 times forward financial year ending Jan 31, 2019 (FY2019F) revenue, with management hopeful of further wins from tender prospects worth up to US$9.5 billion.

"The stock currently trades at an attractive 0.3 times FY2018F book value vs 0.9 times for Bumi Armada Bhd and 0.5 times for Malaysia Marine and Heavy Engineering Holdings Bhd," he says.

Goh notes that Sapura's last major award announcement was for multiple contracts worth RM1.5 billion on Nov 15 last year, while its FY2018 contract awards totalled RM3.7 billion compared with AmInvestment's assumption of RM6 billion.

AmInvestment has a "buy" call on Sapura Energy with a fair value of RM1.

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