

03 June 2019

Oil & Gas

Petronas Group's 1Q19 Results

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NEUTRAL



Petronas group posted a stronger set of 1Q19 results with core PATAMI of RM12b (+37% QoQ, +16% YoY), driven by higher sales volumes, a weakened Ringgit and lowered costs, but partially offset by lower average realised prices. While no dividends were announced during the quarter, the group had paid RM12b dividends in relation to the RM30b special dividend announced end-FY18, with the remaining RM18b to be paid throughout the rest of the year. Despite so, the group's cash-pile remains strong at RM172b – almost unchanged from end-FY2018. The group had also incurred capex of RM8.3b during the quarter, mainly attributed to upstream projects. That said, we expect capex to increase in the coming quarters given Petronas' capex commitment of >RM50b for 2019 (versus 2018 capex of RM46.8b). Nonetheless, we feel the group should be able to deliver on its committed higher capex and dividends, underpinned by improved earnings trajectory. We see key beneficiaries of an increased Petronas capex to include fabrication players (e.g. MHB, SAPNRG), drilling players (e.g. VELESTO, SAPNRG), production enhancement players (e.g. UZMA) as well as floating production providers (e.g. MISC, YINSON). Overall, we maintain NEUTRAL on the sector, given limited upside on big-cap Petronas-related counters. Although the recently concluded results season is deemed as largely within expectations, it was mostly due to lowered expectations, rather than fundamental improvement in earnings (average earnings actually declined 27% YoY). Earnings delivery and balance-sheet resilience still remain as our key stock selection criteria, and hence, we continue to favour names such as DIALOG, SERBADK, and YINSON, although we have also highlighted PANTECH and SAPNRG as potential turnaround plays.



Petronas posts stronger 1Q19 results. Petronas group posted 1Q19 core PATAMI of RM12b (after stripping-off net impairment write-backs), growing 16% YoY, helped by higher sales volume for petroleum products and LNG, on top of benefiting from the weakening Ringgit, but offset by lower average realised prices. Sequentially, the quarter's core PATAMI grew 37% QoQ, mainly due to lower production costs (gross margin +4.3 ppt), on top of lower finance costs (-39%) and fixed overhead savings (-8%). This is despite poorer revenue (-11%), dragged by lower sales volumes and average realised prices, on top of a stronger Ringgit, QoQ.

Cash-pile remains strong. During the quarter, the group paid RM12b of dividends, in relation to the RM30b special dividend declared in end-FY18, with the remaining RM18b to be paid throughout the year, although seemingly no dividends were declared this quarter. Despite so, Petronas' cash-pile remains strong at RM172b – almost unchanged from end-FY18. The group had also incurred capex of RM8.3b during the quarter (-31% YoY, -59% QoQ), mainly attributed to upstream projects. With the group having already committed to higher capex of >RM50b for 2019 (versus 2018 capex of RM46.8b), we believe higher spending would come in the coming quarters, with focus on the upstream. Nonetheless, with Petronas' improved earnings trajectory, we believe the group should be able to deliver on its committed higher capex even despite higher dividend payments for the year.

Value-chains to benefit from higher Petronas capex. We believe the higher capex, especially in the upstream space, could be sanctioned for fields under development (e.g. Kelidang, Limbayong), as well as production enhancement for existing brownfields. As such, we see potential beneficiaries of a higher Petronas capex spend to include fabrication players (e.g. SAPNRG, MHB), drilling players (e.g. VELESTO, SAPNRG), production enhancement players (e.g. UZMA), as well as floating production providers (e.g. MISC, YINSON). Nonetheless, cost optimisation would still remain as a key factor, and hence, we should continue to expect competitively lower margins for upcoming job awards.

Maintain NEUTRAL, given limited upsides to big-cap Petronas-linked counters. While we deem the recently-concluded results season to be largely in line of expectations, with only 4 out of 13 coverage stocks posting below-expectation earnings (implying a "disappointment" ratio of 31%), this was mostly due to lowered expectations, rather than an actual improvement in fundamental earnings. In fact, the sector saw an average earnings decline of 27% YoY, signalling the continued challenging business environment. Nonetheless, oil prices have managed to stabilise in recent months, on the back of continued OPEC+ cut compliance on top of involuntary output drops in countries such as Venezuela, Libya and Iran, although recent U.S-China trade tensions have seemingly spurred some demand-side uncertainties. That said, we firmly view that continued production cuts from OPEC+ beyond the current June 2019 cut-off date is paramount to sustaining current oil price levels. Overall, with earnings delivery and balance-sheet resilience still remaining as our key selection criteria, we continue to favour stable names such as DIALOG, SERBADK and YINSON, although we have also highlighted PANTECH and SAPNRG as potential turnaround plays.



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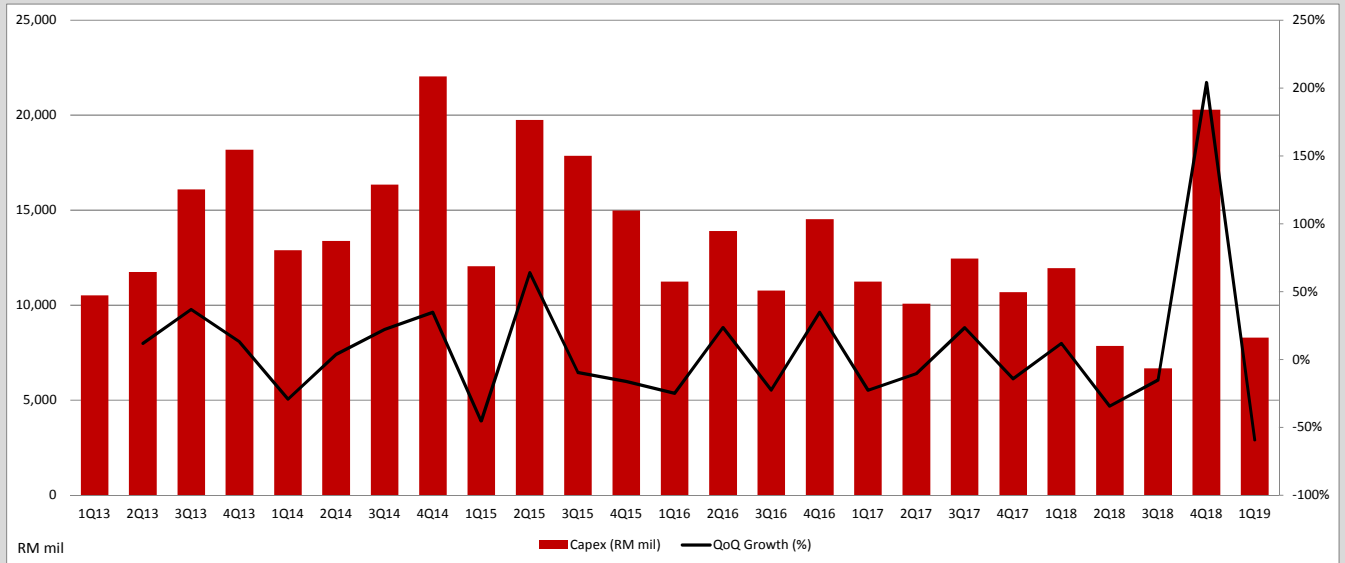
Income Statement								
	1Q	4Q	Q-o-Q	1Q	Y-o-Y	3M	3M	Y-o-Y
Y/E: Dec (RM'mil)	FY19	FY18	Chg	FY18	Chg	FY19	FY18	Chg
Revenue	61,994	69,904	-11.3%	57,922	7.0%	61,994	57,922	7.0%
Cost of revenue	(37,519)	(45,341)	-17.3%	(35,421)	5.9%	(37,519)	(35,421)	5.9%
Gross profit	24,475	24,563	-0.4%	22,501	8.8%	24,475	22,501	8.8%
Selling and distribution expenses	(1,756)	(2,368)	-25.8%	(1,541)	14.0%	(1,756)	(1,541)	14.0%
Administration expenses	(3,420)	(3,472)	-1.5%	(3,027)	13.0%	(3,420)	(3,027)	13.0%
Net impairment write-back	84	3,655	-97.7%	1,077	-92.2%	84	1,077	-92.2%
Other expenses	(509)	(311)	63.7%	(1,811)	-71.9%	(509)	(1,811)	-71.9%
Other income	1,096	194	464.9%	1,786	-38.6%	1,096	1,786	-38.6%
Operating profit	19,970	22,261	-10.3%	18,985	5.2%	19,970	18,985	5.2%
Finance costs	(1,233)	(2,035)	-39.4%	(839)	47.0%	(1,233)	(839)	47.0%
Associates and JVs	200	199	0.5%	110	81.8%	200	110	81.8%
Profit before taxation	18,937	20,425	-7.3%	18,256	3.7%	18,937	18,256	3.7%
Tax expense	(4,689)	(6,101)	-23.1%	(5,223)	-10.2%	(4,689)	(5,223)	-10.2%
Non-controlling interests	(2,158)	(1,914)	12.7%	(1,621)	33.1%	(2,158)	(1,621)	33.1%
PATAMI	12,090	12,410	-2.6%	11,402	6.0%	12,090	11,402	6.0%
Core PATAMI	12,006	8,755	37.1%	10,325	16.3%	12,006	10,325	16.3%
Gross margin	39.5%	35.1%		38.8%		39.5%	38.8%	
Operating margin	32.2%	31.8%		32.8%		32.2%	32.8%	
PBT margin	30.5%	29.2%		31.5%		30.5%	31.5%	
PATAMI margin	19.5%	17.8%		19.7%		19.5%	19.7%	
Core PATAMI margin	19.4%	12.5%		17.8%		19.4%	17.8%	
Effective tax rate	24.8%	29.9%		28.6%		24.8%	28.6%	

Source: Petronas, Kenanga Research

Segmental Breakdown								
	1Q	4Q	Q-o-Q	1Q	Y-o-Y	3M	3M	Y-o-Y
Y/E: Dec (RMmn)	FY19	FY18	Chg	FY18	Chg	FY19	FY18	Chg
Upstream								
Revenue	30,851	33,239	-7.2%	28,162	9.5%	30,851	28,162	9.5%
PAT	9,163	14,265	-35.8%	10,233	-10.5%	9,163	10,233	-10.5%
PAT margin	29.7%	42.9%		36.3%		29.7%	36.3%	
Downstream								
Revenue	27,358	32,840	-16.7%	26,183	4.5%	27,358	26,183	4.5%
PAT	1,913	419	356.6%	1,965	-2.6%	1,913	1,965	-2.6%
PAT margin	7.0%	1.3%		7.5%		7.0%	7.5%	
Corporate and Others								
Revenue	3,785	3,825	-1.0%	3,577	5.8%	3,785	3,577	5.8%
PAT	1,631	1,999	-18.4%	29	5524.1%	1,631	29	5524.1%
PAT margin	43.1%	52.3%		0.8%		43.1%	0.8%	

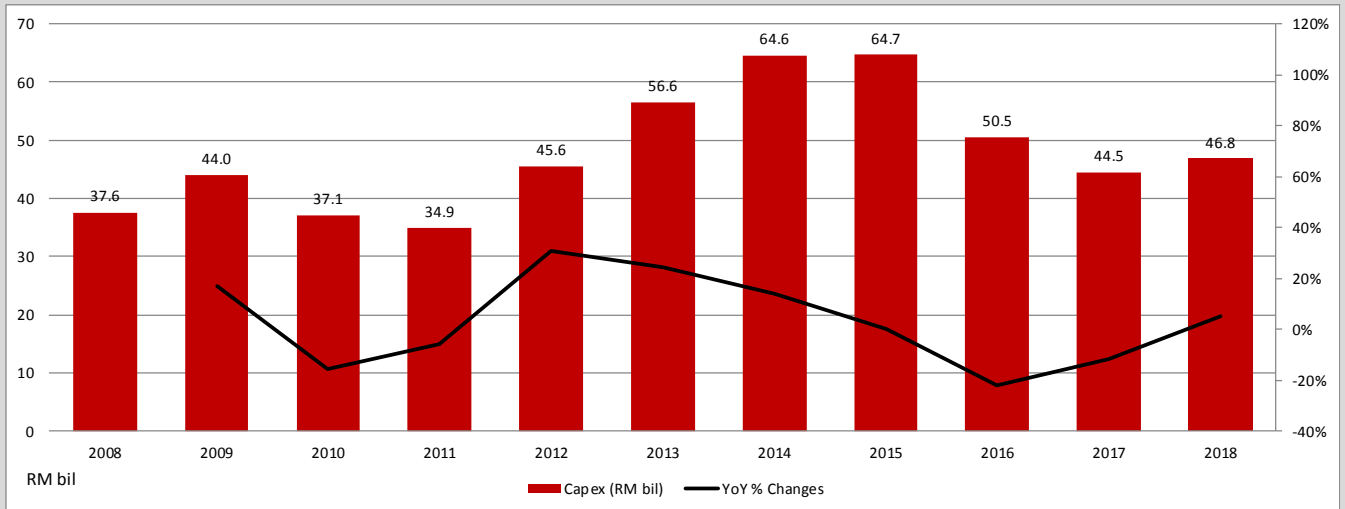
Source: Petronas, Kenanga Research

Petronas Quarterly Capex



Source: Petronas, Kenanga Research

Petronas Yearly Capex



Source: Petronas, Kenanga Research

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Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
BUMI ARMADA BERHAD	0.200	1,175.3	N	12/2019	14.3%	-19.8%	38.4%	2.2%	5.2	3.8	3.7	0.3	0.3	9.3%	0.0%	0.180	UP
DAYANG ENTERPRISE HLDGS BHD	0.975	940.7	Y	12/2019	22.2%	4.4%	-43.1%	4.0%	5.7	10.1	9.7	0.8	0.8	8.3%	0.0%	0.800	UP
DIALOG GROUP BHD	3.32	18,719.2	Y	06/2019	-22.9%	14.8%	10.1%	13.5%	43.7	39.6	34.9	5.3	5.1	13.2%	1.0%	3.80	OP
MALAYSIA MARINE AND HEAVY EN	0.715	1,144.0	Y	12/2019	-10.1%	-25.6%	845.5%	123.4%	N.A.	78.9	35.3	0.4	0.5	0.6%	0.0%	0.770	MP
MISC BHD	6.95	31,023.0	Y	12/2019	0.8%	-2.9%	21.2%	10.1%	23.5	19.4	17.6	0.9	0.9	4.6%	4.3%	6.65	MP
PANTECH GROUP HOLDINGS BHD	0.520	389.7	Y	02/2020	1.3%	5.9%	1.3%	6.4%	8.9	8.8	8.3	0.7	0.6	7.6%	3.1%	0.690	OP
PETRONAS CHEMICALS GROUP BHD	8.32	66,560.0	Y	12/2019	-9.8%	7.7%	-15.9%	17.0%	13.4	15.9	13.6	2.2	2.0	13.2%	3.1%	8.75	MP
PETRONAS DAGANGAN BHD	25.76	25,591.4	Y	12/2019	-5.6%	2.0%	33.0%	2.2%	30.6	23.0	22.5	4.3	4.1	18.4%	3.0%	24.95	MP
SAPURA ENERGY BHD	0.295	4,702.1	Y	01/2020	5.9%	20.7%	1875.6%	258.5%	N.A.	97.4	27.2	0.4	0.3	0.4%	0.0%	0.430	OP
SERBA DINAMIK HOLDINGS	4.10	6,020.9	Y	12/2019	18.6%	9.7%	12.2%	8.0%	15.7	14.0	13.0	2.9	2.5	19.4%	2.2%	4.80	OP
UZMA BHD	0.755	241.6	Y	06/2019	-24.3%	-0.1%	-86.0%	193.1%	4.7	33.6	11.5	0.5	0.5	1.5%	0.0%	0.690	UP
WAH SEONG CORP BHD	0.670	516.2	Y	12/2019	-47.7%	-7.7%	-18.8%	-18.1%	8.2	10.1	12.3	0.5	0.5	5.4%	0.0%	0.620	UP
YINSON HOLDINGS BHD	4.93	5,325.3	Y	01/2020	0.1%	70.2%	-7.1%	55.9%	20.3	21.8	14.0	3.1	2.8	13.5%	1.2%	5.50	OP
Simple Average					-4.4%	6.1%	205.1%	52.0%	16.3	28.9	17.2	1.7	1.6	8.9%	1.4%		

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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