

# Velesto Energy Berhad

## FY19 Stages Turnaround to Profit

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**FY19 results managed a turnaround from losses, slightly beating our expectations, thanks to healthier drilling rig utilisation (80% vs 73%). Moving forward, with all rigs expected to be utilised throughout 2020, we believe FY20 will be an even stronger year. Possible renegotiation of higher charter rates could also act as further catalyst. Maintain OUTPERFORM with TP of RM0.43.**

**Above our expectation, but below market's.** VELESTO recorded FY19 core net profit of RM32m, exceeding our forecast by 8% due to slightly better-than-expected margins. However, results came in below market's expectations, making up only 74% of consensus estimate. We suspect this could be due to market's overestimation of VELESTO's drilling rig utilisation rates during the year. Meanwhile, no dividends were announced, as expected.

**FY19 turning to black, but weaker 4QFY19.** VELESTO managed to turn around in FY19 from losses last year, thanks to healthier rig utilisation (80% vs 73%). 4QFY19 posted core net profit of RM8.1m – a steep decline both YoY and QoQ. The poorer quarterly results were due to lower rig utilisations of 86% versus 92% in 3QFY19 and 91% in 4QFY18, as two of its rigs (namely Naga 3 and 7) underwent their mandatory five-yearly Special Periodic Survey (SPS).

**An even stronger FY20 to come.** Moving forward, VELESTO is set to post an even stronger year in FY20, as all seven of its rigs already have contracts at hand and will be utilised throughout the year. Meanwhile, a possible rate renegotiation with Petronas Carigali upon extension of contracts for rigs Naga 2, 3, 5 and 6 (existing firm period contracts set to expire in at around mid-FY20) could also act as another catalyst for the stock, should the renegotiated rates be higher than existing ones. We believe should a renegotiation take place, it would most likely be announced by end-2QFY20.

**Maintain OUTPERFORM**, with unchanged TP of RM0.43 pegged to 1.2x FY20E PBV – which is still close to -1.5SD below its 5-year mean valuations.

Post-results, we made no changes to our FY20E forecasts, but introduce new FY21E numbers. Our forecasts are based on the assumptions of: (i) 90% rig utilisation, (ii) USD75k/day and USD77k/day daily charter rates for FY20 and FY21, respectively, and (iii) MYR/USD exchange rate of RM4.10/USD.

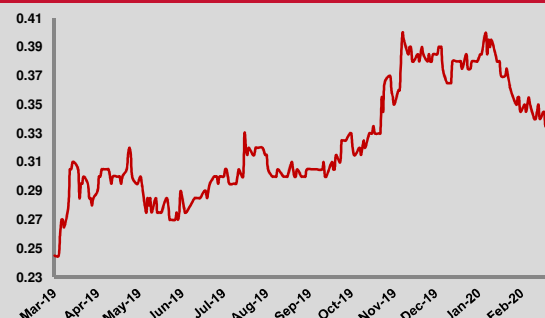
We continue to like VELESTO given its clear earnings visibility for the next 1-2 years. Key catalysts would include continued earnings delivery, and the aforementioned renegotiation of rates, on top of further contract awards. The name is also an ESG-play within the oil and gas sector, being a constituent of the FTSE4GOOD index.

**Risks to our call include:** (i) poorer-than-expected rigs utilisation, (ii) weaker-than-expected charter rates, (iii) lower-than-expected margins, and (iv) stronger-than-expected Ringgit.

**OUTPERFORM** ↔

Price : **RM0.340**  
Target Price : **RM0.430** ↔

### Share Price Performance



KLCI 1,500.88  
YTD KLCI chg -5.5%  
YTD stock price chg -10.5%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	VEB MK Equity
Market Cap (RM m)	2,793.3
Shares Outstanding	8,215.6
52-week range (H)	0.41
52-week range (L)	0.23
3-mth avg daily vol:	26,588,730
Free Float	47%
Beta	1.4

### Major Shareholders

Skim Amanah Saham Bumiputera	33.6%
Yayasan Pelaburan Bumiputera	12.4%
Employees Provident Fund	7.3%

### Summary Earnings Table

FY Dec (RM m)	2019A	2020E	2021E
Revenue	670.8	722.1	741.0
EBIT	123.9	167.5	184.3
PBT	42.5	87.5	104.3
<b>Net Profit (NP)</b>	<b>33.2</b>	<b>65.6</b>	<b>78.3</b>
<b>Core NP</b>	<b>32.0</b>	<b>65.6</b>	<b>78.3</b>
Consensus CNP		84.8	131.2
Earnings revision (%)		-	NEW
Core EPS (sen)	0.4	0.8	1.0
C. EPS growth (%)	N.M.	105.2	19.3
DPS (sen)	0.0	0.0	0.0
BVPS (RM)	0.3	0.3	0.4
Core PER (x)	87.4	42.6	35.7
Price/BV (x)	1.0	1.0	0.9
Net Gearing (x)	0.4	0.3	0.2
Div. Yield (%)	0.0	0.0	0.0

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Income Statement								
	4Q FY19	3Q FY19	Q-o-Q	4Q FY18	Y-o-Y	12M FY19	12M FY18	Y-o-Y
Y/E : Dec (RM m)								
Revenue	178.1	208.6	-14.61%	189.9	-6.20%	670.8	573.8	16.90%
Operating Expenses	(147.4)	(156.1)	-5.59%	(157.3)	-6.27%	(557.8)	(545.1)	2.31%
Other Operating Income	0.1	2.0	-95.29%	1.7	-94.49%	2.7	26.2	-89.63%
<b>Profit From Operations</b>	<b>30.8</b>	<b>54.4</b>	<b>-43.41%</b>	<b>34.3</b>	<b>-10.20%</b>	<b>115.7</b>	<b>54.9</b>	<b>110.91%</b>
Finance Costs	(18.2)	(20.7)	-12.14%	(22.4)	-18.97%	(81.5)	(85.1)	-4.31%
Associates	0.1	0.1	-9.84%	0.1	3.77%	0.2	0.2	-6.43%
Investment Income	1.9	2.1	-6.23%	3.6	-46.70%	8.0	12.4	-35.72%
<b>Profit Before Tax</b>	<b>14.6</b>	<b>35.8</b>	<b>-59.27%</b>	<b>15.5</b>	<b>-5.99%</b>	<b>42.5</b>	<b>(17.6)</b>	<b>N.M.</b>
Taxation	(4.4)	(2.5)	75.92%	(2.4)	79.89%	(9.4)	(2.9)	227.98%
Non-controlling Interests	0.0	(0.0)	N.M.	0.0	N.M.	0.1	0.9	-83.70%
<b>Net Profit</b>	<b>10.2</b>	<b>33.3</b>	<b>-69.39%</b>	<b>13.1</b>	<b>-22.17%</b>	<b>33.2</b>	<b>(19.5)</b>	<b>N.M.</b>
<b>Core Net Profit</b>	<b>8.1</b>	<b>34.7</b>	<b>-76.55%</b>	<b>23.5</b>	<b>-65.34%</b>	<b>32.0</b>	<b>(18.2)</b>	<b>N.M.</b>
<i>Rig utilisation</i>	<i>86%</i>	<i>92%</i>		<i>91%</i>		<i>80%</i>	<i>73%</i>	
Operating margin	17.28%	26.08%		18.05%		17.25%	9.56%	
PBT margin	8.19%	17.18%		8.17%		6.33%	-3.06%	
Net margin	5.73%	15.98%		6.90%		4.95%	-3.40%	
Core net margin	4.57%	16.65%		12.38%		4.77%	-3.17%	
Effective tax rate	30.09%	6.97%		15.73%		22.18%	-16.36%	

Source: Company

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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 BHD	0.380	2,233.1	N	12/2019	-15.9%	0.0%	34.4%	2.3%	9.9	7.4	7.2	0.7	0.7	9.0%	0.0%	0.530	OP
DAYANG ENTERPRISE HLDGS BHD	2.67	3,002.5	Y	12/2020	8.7%	9.0%	8.6%	9.9%	14.4	13.2	12.1	2.1	1.8	15.0%	0.0%	3.40	OP
DIALOG GROUP BHD	3.35	18,888.3	Y	06/2020	17.7%	6.1%	4.5%	9.7%	35.3	33.7	30.8	5.0	4.7	14.4%	1.2%	4.15	OP
MALAYSIA MARINE AND HEAVY EN	0.765	1,224.0	Y	12/2020	3.2%	28.4%	360.0%	23.2%	N.A.	128.8	104.6	0.5	0.5	0.4%	0.0%	0.890	OP
MISC BHD	7.50	33,478.1	Y	12/2020	3.4%	5.4%	0.6%	1.0%	20.8	20.7	20.5	1.0	0.9	4.6%	4.0%	8.70	OP
PANTECH GROUP HOLDINGS BHD	0.480	359.7	Y	02/2020	1.3%	5.9%	-19.3%	8.9%	8.2	10.2	9.4	0.7	0.6	6.1%	4.2%	0.570	OP
PETRONAS CHEMICALS GROUP BHD	6.40	51,200.0	Y	12/2019	-13.9%	4.8%	-30.3%	14.5%	10.3	14.7	12.9	1.7	1.6	11.1%	3.4%	7.70	MP
PETRONAS DAGANGAN BHD	21.40	21,259.9	Y	12/2020	1.3%	2.0%	10.7%	2.2%	25.9	23.4	22.9	3.6	3.5	15.0%	3.4%	21.35	MP
SAPURA ENERGY BHD	0.225	3,595.3	Y	01/2020	67.1%	-25.1%	-200.9%	-166.8%	N.A.	N.A.	N.A.	0.3	0.3	-3.2%	0.0%	0.330	OP
SERBA DINAMIK HOLDINGS	2.35	7,247.0	Y	12/2019	23.2%	14.3%	17.2%	13.3%	18.7	15.9	14.1	3.5	3.0	20.2%	4.0%	2.50	OP
UZMA BHD	0.815	260.8	Y	06/2020	21.4%	2.2%	215.5%	9.8%	26.9	8.5	7.8	0.5	0.5	6.2%	0.0%	0.850	MP
VELESTO ENERGY BHD	0.340	2,793.3	Y	12/2019	7.6%	2.6%	105.0%	19.4%	87.3	42.6	35.7	1.0	1.0	2.3%	0.0%	0.430	OP
WAH SEONG CORP BHD	1.27	978.5	Y	12/2020	16.5%	4.1%	-3.4%	6.6%	14.0	14.5	13.6	1.0	0.9	6.7%	0.0%	1.40	MP
YINSON HOLDINGS BHD	7.10	7,596.8	Y	01/2020	0.1%	70.1%	-17.9%	66.8%	29.1	35.5	21.3	4.4	4.0	11.9%	0.8%	8.80	OP
<b>Simple Average</b>					<b>10.1%</b>	<b>9.3%</b>	<b>34.6%</b>	<b>1.5%</b>	<b>25.1</b>	<b>28.4</b>	<b>24.0</b>	<b>1.8</b>	<b>1.7</b>	<b>8.5%</b>	<b>1.5%</b>		

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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