

Sapura Energy Berhad

2Q20 Narrowed Losses; Contract Wins

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Despite improved 1H20 (narrowed losses by 17%), results are deemed below expectations due to weaker-than-expected earnings from E&C and E&P segments. Meanwhile, SAPNRG announced contract wins amounting to ~RM774m, bringing YTD-wins to RM3.1b and order-book to RM16.3b. Moving forward, coming quarters could still show weak numbers, but a turnaround in FY21 is possible. Maintain **OUTPERFORM**, with lowered TP of RM0.33.

Improved 1H20 but below expectations. 1H20 registered core loss of RM257.8m (arrived after stripping-off non-recurring items e.g. gains on disposals and forex). While we had expected better performances (1H20 losses narrowed 17% YoY), we deem the improved 1H20 numbers to be inadequate to meet expectations against our forecasted full-year earnings forecasts of RM49.9m and consensus full-year losses forecasts of RM6.6m, although we acknowledge that its performance is expected to further gradually improve going into the 2H of the year. The below-expectation results were due to the slower-than-expected recovery in its E&C division, coupled with extended losses in its E&P division. No dividends were announced, as expected.

Overall improving numbers. 1H20 core loss narrowed 17% YoY, helped by: (i) massively improved performance from its E&C segment, on the back of higher activities on-hand, (ii) narrowed losses in its drilling segment, helped by depreciation savings following massive impairments in 4Q19, coupled with slightly improved rig utilisation, offset by (iii) poorer E&P performances, despite higher production volumes, given its reduced stake, on top of a purchase price adjustment following its 50%-stake disposal of the segment to OMV AG (i.e. post-disposal, book value of the asset was readjusted higher to be closer to fair value), hence leading to increased depreciation expenses. Noticeably, the period also saw lower finance costs – this being the fruition of its earlier concluded rights issue.

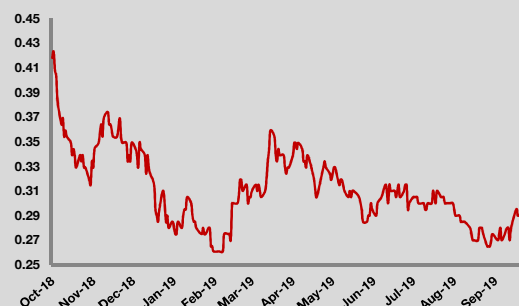
YoY, 2Q20 core loss of RM112.6m narrowed 31% YoY, similarly due to: (i) turnaround in its E&C segment, and (ii) narrowed drilling losses, masking poorer E&P – all on the aforementioned reasons. Sequentially, core loss narrowed 22% QoQ, on the back of: (i) narrowed drilling losses following improved rigs utilisation, and (ii) marginally narrowed E&P losses, following last quarter's transaction-related costs. However, this was offset by: (i) poorer E&C, given lower margin mix with newer jobs coming in at earlier project lifecycles, hence leading to frontloading of costs recognition.

More new contract wins of ~RM774m. SAPNRG had also announced a series of contract wins with a combined value of RM774m. These include (i) EPCI works for the Salman Project in Brunei, (ii) procurement, construction, hook up and commissioning works for Petronas Carigali, and (iii) three new drilling contracts in Thailand, Malaysia, and Brunei (refer to table below for detailed breakdown of new contract wins). Overall, we are positive on the new wins, as they display SAPNRG's continued job winning and delivering capabilities. This brings YTD-wins to RM3.1b (still within FY20E replenishment assumption of RM5b), and order-book of RM16.3b. Post-contract win, this would bring all 9 of its operational rigs to have a contract on hand and be utilised by end of the year, as compared to currently only 6 being utilised. Meanwhile, 7 other rigs remain stacked.

OUTPERFORM ↔

Price : **RM0.285**
Target Price : **RM0.330** ↓

Share Price Performance



KLCI	1,584.14
YTD KLCI chg	-6.3%
YTD stock price chg	0.0%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	SAPE MK Equity
Market Cap (RM m)	4,542.7
Shares Outstanding	15,939.2
52-week range (H)	0.43
52-week range (L)	0.25
3-mth avg daily vol:	53,517,080
Free Float	55%
Beta	1.5

Major Shareholders

Skim Amanah Saham Bumiputera	27.0%
Sapura Holdings Sdn Bhd	12.6%
Tan Sri Sharhil Shamsuddin	5.0%

Summary Earnings Table

FY Jan (RM'm)	2019A	2020E	2021E
Turnover	4,568.4	4,836.4	5,836.4
EBIT	(398.6)	(56.2)	226.6
PBT	(1,054.6)	(264.8)	112.2
Net Profit (NP)	207.5	(198.6)	84.1
Core Net Profit	(884.8)	(198.6)	84.1
Consensus (NP)		(6.6)	195.2
Earnings Revision (%)	-	-497.9	-53.0
Core EPS (sen)	-5.4	-1.2	0.5
CNP growth (%)	155.8	-77.6	-142.3
DPS (sen)	0.5	0.0	0.0
BV/Share (RM)	0.8	0.8	0.8
Core PER (x)	-5.3	-23.6	55.8
Price/BV (x)	0.3	0.3	0.3
Net-Gearing (x)	0.6	0.8	0.8
Dividend Yield (%)	1.8	0.0	0.0

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Improved outlook? Post-results, we revised FY20E earnings to a loss of RM198.6m and FY21E to CNP of RM84.1m (from CNP of RM49.9m and RM178.9m, respectively) after lowering our contribution assumptions from its E&C and E&P segments. Although we acknowledge its outlook is gradually improving, underpinned by (i) finance cost savings following the successful rights issue, (ii) depreciation savings following massive impairment of RM1.5b in 4Q19, (iii) healthy E&C order-book, (iv) improving utilisation for drilling rigs, and (v) jump in E&P production in 4Q20 from first gas in SK408, we reckon upcoming quarters could still potentially show weak numbers (i.e. continued losses). While its drilling and its E&P segments are expected to turn around by year-end, we believe the E&C segment could still display some sluggish performance as many of its newer jobs at hand are still in earlier phases of contract lifecycle, which would lead to back-loading of profits given upfront cost recognitions.

Maintain OUTPERFORM. We lowered our TP to RM0.33 (from RM0.43 previously), after lowering our ascribed valuation down a notch to 0.4x FY20E PBV (from 0.5x earlier) – which is somewhere between -1SD to -1.5SD from its 5-year mean, given the later-than-expected turnaround (previous expectations of a full-year turnaround in FY20). Nonetheless, we still keep our OUTPERFORM call unchanged, given improving outlook from all its segments, with the share currently trading at floor valuations of merely 0.3x and below its rights issue price of RM0.30.

Risks to our call include: (i) lower-than-expected contract replenishment, (ii) costs overrun, (iii) lower-than-expected drilling rigs utilisation, (iv) lower-than-expected E&P production volumes, and (v) poorer-than-expected operating margins.

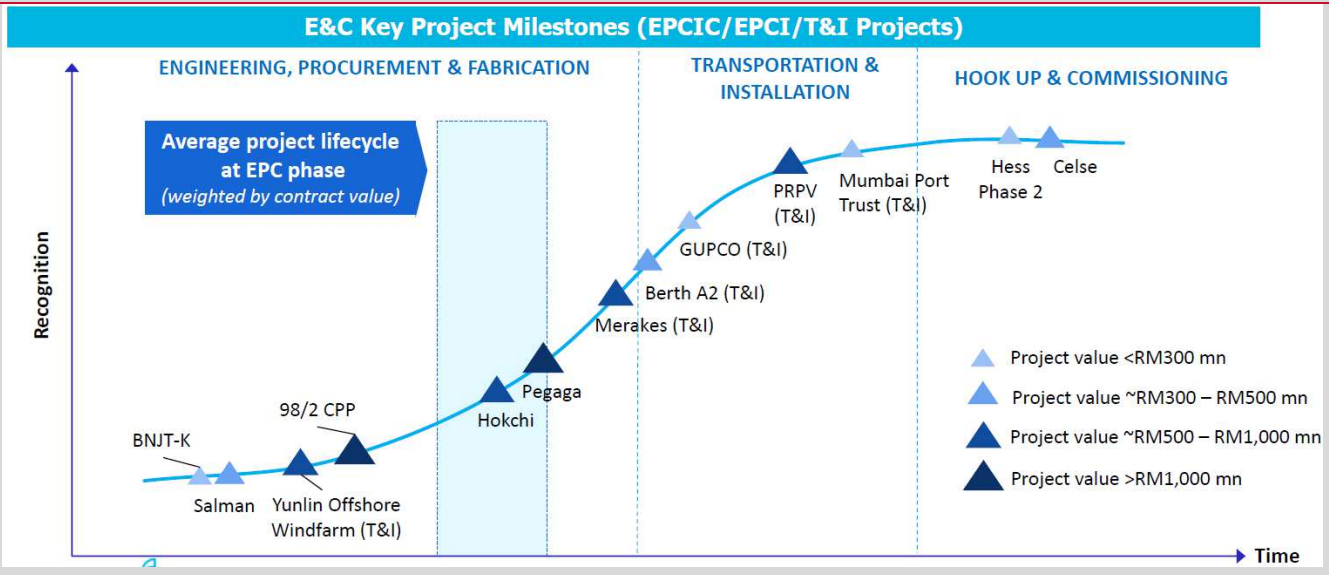
Results Highlights								
	2Q	1Q	Q-o-Q	2Q	Y-o-Y	1H	1H	Y-o-Y
FY Jan (RM' mil)	FY20	FY20	Chg	FY19	Chg	FY20	FY19	Chg
Revenue	1,927.4	1,632.5	18.1%	1,032.1	86.7%	3,559.9	1,877.3	89.6%
Other operating income	1.8	93.1	-98.0%	3.0	-39.6%	95.0	6.6	1331.1%
Operating expenses	(1,812.7)	(1,585.7)	14.3%	(906.4)	100.0%	(3,398.3)	(1,655.5)	105.3%
Profit from operations	116.6	139.9	-16.7%	128.7	-9.4%	256.5	228.4	12.3%
Deprec. and amortis.	(129.2)	(124.3)	4.0%	(167.5)	-22.8%	(253.5)	(331.3)	-23.5%
Finance income	3.2	5.0	-36.2%	8.0	-60.1%	8.2	12.5	-34.2%
Finance costs	(152.4)	(214.4)	-28.9%	(241.4)	-36.9%	(366.8)	(463.8)	-20.9%
Gains on disposal	2.1	11.1	-80.8%	0.0	N.M.	13.2	0.0	N.M.
Net forex	(5.8)	24.9	-123.4%	18.2	-132.1%	19.1	27.3	-30.0%
Associates and JV	72.4	79.3	-8.8%	93.8	-22.8%	151.7	202.0	-24.9%
Profit before tax	(93.2)	(78.4)	-19.0%	(160.2)	41.8%	(171.6)	(325.0)	-47.2%
Taxation	(23.3)	(31.0)	-24.7%	(38.9)	-40.1%	(54.3)	(58.8)	-7.6%
Non-controlling interests	0.2	0.2	6.1%	(0.1)	-337.9%	0.5	0.7	-32.5%
Net profit	(116.3)	(109.1)	6.6%	(126.1)	-7.7%	(225.4)	(261.8)	-13.9%
Core net profit	(112.6)	(145.2)	-22.4%	(163.1)	-31.0%	(257.8)	(309.5)	-16.7%
Operating margin	6.0%	8.6%		12.5%		7.2%	12.2%	
PBT margin	-4.8%	-4.8%		-15.5%		-4.8%	-17.3%	
Net margin	-6.0%	-6.7%		-12.2%		-6.3%	-13.9%	
Core net margin	-5.8%	-8.9%		-15.8%		-7.2%	-16.5%	
Effective tax rate	-25.0%	-39.5%		-24.3%		-31.6%	-18.1%	

Source: Company

Segment Breakdown								
	2Q	1Q	Q-o-Q	2Q	Y-o-Y	1H	1H	Y-o-Y
FY Jan (RM' mil)	FY20	FY20	Chg	FY19	Chg	FY20	FY19	Chg
Revenue								
E&C	1,656.5	1,402.8	18.1%	779.5	112.5%	3,059.3	1,445.1	111.7%
Drilling	272.0	230.4	18.0%	253.5	7.3%	502.4	436.9	15.0%
Operating Profit								
E&C	27.2	48.0	-43.4%	(20.5)	-232.6%	75.2	16.0	371.1%
Drilling	(35.7)	(50.9)	-29.8%	(58.3)	-38.7%	(86.6)	(127.0)	-31.8%
E&P	(5.8)	(7.5)	-22.7%	(1.1)	431.6%	(13.3)	(3.1)	322.1%
Operating Margins								
E&C	1.6%	3.4%		-2.6%		2.5%	1.1%	
Drilling	-13.1%	-22.1%		-23.0%		-17.2%	-29.1%	

Source: Kenanga Research

E&C Project Lifecycles



Source: Bursa Malaysia

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Breakdown of New Contract Wins (Part 1 of 2)

Contract Details	Segment																					
<p>Brunei</p> <p>AWARD OF CONTRACT FOR THE PROVISION OF ENGINEERING, PROCUREMENT, CONSTRUCTION AND INSTALLATION (EPCI) FOR THE SALMAN PROJECT</p> <p>Sapura Fabrication Sdn. Bhd. has been awarded a contract from Brunei Shell Petroleum Company Sdn. Bhd. for the provision of Engineering, Procurement, Construction and Installation (EPCI) works for the Salman Project in Brunei.</p> <p>The scope of work for the Contract is divided into two (2) parts as follows: -</p> <p>(a) Part 1- Salman Greenfield scope</p> <p>The scope consists of detailed design engineering, procurement, construction or fabrication, transportation and installation (EPCI) and support for hook-up, pre-commissioning and commissioning for the following five (5) packages: -</p> <table border="0"> <tr> <td>(i) Well-head platform and substructures (SLWJ-01)</td> <td>-</td> <td>Package 1</td> </tr> <tr> <td>(ii) Water injection pipeline and umbilical from CPWA-07</td> <td>-</td> <td>Package 2</td> </tr> <tr> <td>(iii) HP oil pipeline to Selangkir (SKWJ-01)</td> <td>-</td> <td>Package 3</td> </tr> <tr> <td>(iv) Water and chemical injection module in CPWA-07</td> <td>-</td> <td>Package 4</td> </tr> <tr> <td>(v) Kuala Belait Marine construction yard (MCY) upgrade</td> <td>-</td> <td>Package 5</td> </tr> </table> <p>(b) Part 2 – Egret East Greenfield scope</p> <p>Front End Engineering Design (FEED) followed by an optional engineering, construction, procurement and optional installation (EPC(I)) scope up to the completion of the work covering Egret East scope.</p> <p>The Egret East scope covers the following packages: -</p> <table border="0"> <tr> <td>(i) Well head platform and substructures</td> <td>-</td> <td>Package 1</td> </tr> <tr> <td>(ii) Oil and gas export pipelines to Egret Main (EGDP-01)</td> <td>-</td> <td>Package 2</td> </tr> </table> <p>The duration of the firm scopes for part 1 and FEED for part 2 will be for a period of three (3) years commencing from FY2020 and ending approximately in FY2023.</p>	(i) Well-head platform and substructures (SLWJ-01)	-	Package 1	(ii) Water injection pipeline and umbilical from CPWA-07	-	Package 2	(iii) HP oil pipeline to Selangkir (SKWJ-01)	-	Package 3	(iv) Water and chemical injection module in CPWA-07	-	Package 4	(v) Kuala Belait Marine construction yard (MCY) upgrade	-	Package 5	(i) Well head platform and substructures	-	Package 1	(ii) Oil and gas export pipelines to Egret Main (EGDP-01)	-	Package 2	Engineering and Construction
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Source: Bursa Malaysia

Breakdown of New Contract Wins (Part 2 of 2)

Contract Details	Segment
<p>Malaysia</p> <p>PROVISION OF PROCUREMENT, CONSTRUCTION, HOOK UP AND COMMISSIONING (PCC) WORKS OF BNJT-K BN-84 WELL TIE-IN FOR BARDEGG-2 AND BARONIA ENHANCED OIL RECOVERY (EOR) DEVELOPMENT PROJECT FOR PETRONAS CARIGALI SDN BHD</p> <p>Sapura Fabrication Sdn. Bhd. has been awarded a contract for the provision of Procurement, Construction, Hook-up and Commissioning (PCC) works of BNJT-K BN-84 Well Tie-In for Bardegg-2 and Baronia EOR Development Project from PETRONAS Carigali Sdn. Bhd.</p> <p>The Contract scope of work consists of procurement, construction, commissioning and start-up of the BNJT-K BN-84 well tie-in. The scope of work also includes project management, administration, fabrication engineering and pre-engineering of the materials, as well as hook-up and commissioning of the well start-up.</p> <p>Works are expected to be completed by Q3 FY2020.</p>	Engineering and Construction
<p>Thailand</p> <p>AWARD OF CONTRACT FOR TENDER ASSIST DRILLING RIG “SAPURA T-17” BY PTT EXPLORATION AND PRODUCTION PUBLIC COMPANY LIMITED</p> <p>Sapura Drilling Asia Limited has been awarded a contract by PTT Exploration and Production Public Company Limited for the provision of its tender assist drilling rig “Sapura T-17” services.</p> <p>The scope of work comprises the provision of barge tender-assist drilling rig services for one (1) year commencing Q1 FY2021 plus options for extension, at the Bongkot field, offshore Gulf of Thailand.</p>	Drilling
<p>Malaysia</p> <p>LETTER OF CONTRACT AMENDMENT AND EXTENSION BY PETRONAS CARIGALI SDN. BHD FOR THE PROVISION OF SEMI-SUBMERSIBLE TENDER-ASSIST DRILLING RIG “SAPURA BERANI”</p> <p>Sapura Drilling Asia Sdn. Bhd. has been awarded a Letter of Contract Amendment and Extension by PETRONAS Carigali Sdn. Bhd. for the provision of semi-submersible tender-assist drilling rig, “Sapura Berani”.</p> <p>The Contract entails the drilling of five (5) additional wells at Erb West, offshore Sabah and Dulang facilities, offshore Peninsular Malaysia. The work related to the five wells is expected to be completed by Q2 FY2021.</p>	Drilling
<p>Brunei</p> <p>EXTENSION OF CONTRACT FOR SEMI-SUBMERSIBLE TENDER-ASSIST DRILLING RIG “SAPURA PELAUT” FROM BRUNEI SHELL PETROLEUM COMPANY SDN. BHD.</p> <p>Sapura Drilling Sdn. Bhd. has been awarded a contract extension from Brunei Shell Petroleum Company Sdn. Bhd. for the provision of a semi-submersible tender-assist drilling rig, “Sapura Pelaut”, and drilling services.</p> <p>The scope of the Contract Extension comprises the provision of a semi-submersible tender-assist drilling rig for a firm period of one (1) year from Q1 FY2021.</p>	Drilling

Source: Bursa Malaysia

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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	0.335	1,968.6	N	12/2019	-15.9%	0.0%	34.4%	2.3%	8.7	6.5	6.3	0.6	0.6	9.0%	0.0%	0.200	UP
DAYANG ENTERPRISE HLDGS BHD	1.65	1,591.9	Y	12/2019	22.2%	4.4%	-33.9%	9.1%	9.7	14.7	13.4	1.4	1.4	9.5%	0.0%	1.45	MP
DIALOG GROUP BHD	3.39	19,113.9	Y	06/2020	17.7%	6.1%	4.5%	9.7%	35.7	34.1	31.1	5.0	4.8	14.4%	1.2%	4.15	OP
MALAYSIA MARINE AND HEAVY EN	0.830	1,328.0	Y	12/2019	-10.1%	43.0%	845.5%	139.3%	N.A.	91.6	38.3	0.6	0.5	0.6%	0.0%	1.05	OP
MISC BHD	7.73	34,504.8	Y	12/2019	3.1%	-2.9%	30.2%	5.3%	26.1	20.0	19.0	1.0	1.0	4.9%	3.9%	8.80	OP
PANTECH GROUP HOLDINGS BHD	0.495	371.2	Y	02/2020	1.3%	5.9%	1.3%	6.4%	8.5	8.4	7.9	0.7	0.6	7.6%	3.2%	0.690	OP
PETRONAS CHEMICALS GROUP BHD	7.53	60,240.0	Y	12/2019	-13.9%	4.8%	-30.3%	14.5%	12.1	17.4	15.2	2.0	1.9	11.1%	2.9%	7.70	MP
PETRONAS DAGANGAN BHD	23.48	23,326.3	Y	12/2019	-5.6%	2.0%	12.9%	7.7%	27.9	24.7	22.9	4.0	3.8	15.6%	2.8%	22.45	MP
SAPURA ENERGY BHD	0.285	4,542.7	Y	01/2020	5.9%	20.7%	-445.5%	236.1%	N.A.	N.A.	55.8	0.3	0.3	-1.4%	0.0%	0.330	OP
SERBA DINAMIK HOLDINGS	4.20	6,167.7	Y	12/2019	23.2%	14.3%	17.2%	13.3%	16.1	13.7	12.1	3.0	2.6	20.2%	2.2%	5.25	OP
UZMA BHD	0.870	278.4	Y	06/2020	-7.6%	-0.1%	117.5%	44.1%	28.7	13.2	9.2	0.6	0.5	4.2%	0.0%	0.610	MP
VELESTO ENERGY BHD	0.325	2,670.1	Y	12/2019	5.3%	6.2%	119.7%	152.0%	N.A.	175.7	69.7	1.0	0.9	0.5%	0.0%	0.350	OP
WAH SEONG CORP BHD	0.625	481.5	Y	12/2019	-47.7%	-7.7%	-18.8%	-18.1%	7.7	9.4	11.5	0.5	0.5	5.4%	0.0%	0.620	MP
YINSON HOLDINGS BHD	6.70	7,240.3	Y	01/2020	0.1%	70.1%	-17.9%	66.8%	27.5	33.5	20.1	4.2	3.8	11.9%	0.9%	7.75	OP
Simple Average					-1.6%	11.9%	45.5%	49.2%	19.0	35.6	23.8	1.8	1.7	8.1%	1.2%		

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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