

# Velesto Energy Berhad

## 2Q19 Turns to Black

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**2Q19 managed to turn to black (broadly in-line of expectations), driven by improved jack-up rigs utilisation (74%). That said, expect a much stronger 2H19 from its on-hand contract schedules. Maintain OUTPERFORM with TP of RM0.35, given its turnaround story with clear earnings visibility for the next 1-2 years, coupled with limited downside risks. Furthermore, it is also an ESG play within the O&G sector, being a member of the FTSE4 Good Bursa Malaysia Index.**

**1H19 broadly within expectations.** VELESTO recorded 1H19 core losses of RM10.9m – deemed broadly within expectations against our full-year earnings forecasts of RM15.2m and consensus of RM25.1m, as we anticipate a much stronger 2H19 given the company's rigs contracting schedules. No dividends were announced, as expected.

**2Q19 turns to black.** 2Q19 had managed to turn to black by recording a core net profit of RM11.8m, with jack-up rigs utilisation of 74%. YoY, this was a turnaround from losses of RM20.2m, driven by the higher utilisation (74% vs 59%). QoQ, similar turnaround from losses of RM22.8m, driven by improved utilisation (74% vs 66%). Cumulative YTD, 1H19 core losses narrowed 67% given improved utilisations (70% vs 62%). Meanwhile, daily charter rates had remained somewhat flattish since 2017 (at around ~USD70k/day).

**Expected turnaround in FY19/20.** Moving forward, we are expecting a much stronger 2H19, given the company's rigs contracting schedules to drive higher utilisations and bring full-year earnings to a black. Our numbers are based on a utilisation assumption of 80%/85% for FY19/20E. Given the certainty of its turnaround story, the company had also proposed an ESOS scheme, which may result in a share base dilution of up to 7.5%, although no further details have been disclosed yet. Overall, we highlight VELESTO as a beneficiary of Petronas' increased drilling rig demand, being the largest jack-up rig player in the country by far.

**Maintain OUTPERFORM**, with an unchanged TP of RM0.35 pegged to 1x PBV on FY20E – roughly in-line with its 2-year mean valuations. Post-results, we made no changes to our FY19-20E numbers.

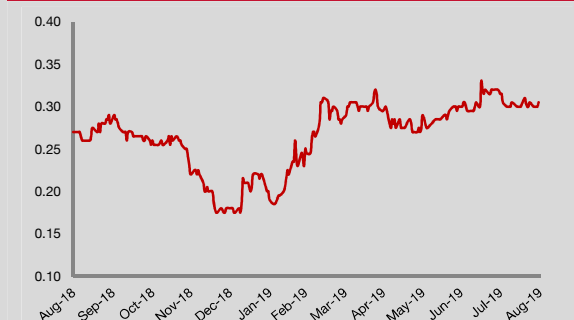
We continue to like VELESTO given the certainty of its turnaround story, clear earnings visibility for the next 1-2 years, while we also see limited downside risks from current share price levels. Additionally, the company reportedly had also demonstrated satisfactory environmental, social and governance practices, being one of the new names within the oil and gas industry to be included into the FTSE4Good Bursa Malaysia Index. That said, we believe a range-bound trading strategy of RM0.30-0.35 would suite the stock.

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

# OUTPERFORM ↔

Price : **RM0.305**  
Target Price : **RM0.350** ↔

### Share Price Performance



KLCI	1,612.14
YTD KLCI chg	-4.6%
YTD stock price chg	69.4%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	VEB MK Equity
Market Cap (RM m)	2,505.8
Shares Outstanding	8,215.6
52-week range (H)	0.34
52-week range (L)	0.17
3-mth avg daily vol:	18,101,170
Free Float	42%
Beta	1.7

### Major Shareholders

Skim Amanah Saham	37.9%
Yayasan Pelaburan	13.3%
Employees Provident Fund	6.8%

### Summary Earnings Table

FY Dec (RM'm)	2018A	2019E	2020E
Revenue	573.2	603.4	641.1
EBIT	68.4	105.2	131.0
PBT	(16.7)	20.2	51.0
<b>Net Profit (NP)</b>	<b>(17.9)</b>	<b>15.2</b>	<b>38.3</b>
<b>Core NP</b>	<b>(18.2)</b>	<b>15.2</b>	<b>38.3</b>
Consensus CNP		25.1	43.8
Earnings revision (%)		-	-
Core EPS (sen)	(0.2)	0.2	0.5
C. EPS growth (%)	N.M.	N.M.	152.3
DPS (sen)	0.0	0.0	0.0
BVPS (RM)	0.3	0.3	0.3
Core PER	N.M.	165.2	65.5
Price/BV (x)	0.9	0.9	0.9
Net Gearing (x)	0.4	0.4	0.3
Div. Yield (%)	0.0	0.0	0.0



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Income Statement								
	2Q	1Q	Q-o-Q	2Q	Y-o-Y	1H	1H	Y-o-Y
	FY19	FY19		FY18		FY19	FY18	
<b>Y/E : Dec (RM'm)</b>								
Revenue	157.1	127.0	23.63%	111.8	40.42%	284.1	233.6	21.61%
Operating Expenses	(126.1)	(128.1)	-1.52%	(120.1)	4.99%	(254.2)	(243.3)	4.50%
Other Operating Income	0.2	0.5	-63.97%	1.6	-88.55%	0.7	24.5	-97.26%
<b>Profit From Operations</b>	<b>31.1</b>	<b>(0.6)</b>	<b>N.M.</b>	<b>(6.7)</b>	<b>N.M.</b>	<b>30.5</b>	<b>14.8</b>	<b>105.76%</b>
Finance Costs	(21.2)	(21.4)	-0.59%	(19.8)	7.48%	(42.6)	(41.5)	2.59%
Associates	0.1	0.1	12.73%	0.1	-7.46%	0.1	0.1	-12.03%
Investment Income	1.8	2.2	-21.44%	1.8	-0.79%	4.0	6.8	-41.19%
<b>Profit Before Tax</b>	<b>11.7</b>	<b>(19.6)</b>	<b>N.M.</b>	<b>(24.7)</b>	<b>N.M.</b>	<b>(7.9)</b>	<b>(19.7)</b>	<b>-59.81%</b>
Taxation	0.1	(2.6)	N.M.	(0.1)	N.M.	(2.5)	(0.2)	N.M.
Non-controlling Interests	0.1	0.0	N.M.	0.7	N.M.	0.2	0.8	N.M.
<b>Net Profit</b>	<b>11.9</b>	<b>(22.2)</b>	<b>N.M.</b>	<b>(24.1)</b>	<b>N.M.</b>	<b>(10.3)</b>	<b>(19.1)</b>	<b>-45.94%</b>
<b>Core Net Profit</b>	<b>11.8</b>	<b>(22.8)</b>	<b>N.M.</b>	<b>(20.2)</b>	<b>N.M.</b>	<b>(10.9)</b>	<b>(33.4)</b>	<b>-67.29%</b>
Rig utilisation	74%	66%		59%		70%	62%	
Operating margin	19.80%	-0.44%		-6.03%		10.75%	6.35%	
PBT margin	7.44%	-15.44%		-22.05%		-2.79%	-8.44%	
Net margin	7.59%	-17.49%		-21.53%		-3.63%	-8.16%	
Core net margin	7.54%	-17.92%		-18.06%		-3.84%	-14.28%	
Effective tax rate	-0.65%	-13.32%		-0.49%		-32.00%	-0.95%	

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 BERHAD	0.255	1,498.5	N	12/2019	-15.9%	0.0%	34.4%	2.3%	6.6	4.9	4.8	0.4	0.4	9.0%	0.0%	0.200	UP
DAYANG ENTERPRISE HLDGS BHD	1.39	1,341.1	Y	12/2019	22.2%	4.4%	-33.9%	9.1%	8.2	12.4	11.3	1.2	1.2	9.5%	0.0%	1.45	MP
DIALOG GROUP BHD	3.48	19,621.3	Y	06/2020	17.7%	6.1%	4.5%	9.7%	36.6	35.0	32.0	5.2	4.9	14.4%	1.1%	4.15	OP
MALAYSIA MARINE AND HEAVY EN	0.800	1,280.0	Y	12/2019	-10.1%	43.0%	845.5%	139.3%	N.A.	88.3	36.9	0.5	0.5	0.6%	0.0%	1.05	OP
MISC BHD	7.26	32,406.8	Y	12/2019	3.1%	-2.9%	30.2%	5.3%	24.5	18.8	17.9	0.9	0.9	4.9%	4.1%	7.60	MP
PANTECH GROUP HOLDINGS BHD	0.500	375.0	Y	02/2020	1.3%	5.9%	1.3%	6.4%	8.6	8.4	7.9	0.7	0.6	7.6%	3.2%	0.690	OP
PETRONAS CHEMICALS GROUP BHD	6.93	55,440.0	Y	12/2019	-13.9%	4.8%	-30.3%	14.5%	11.1	16.0	13.9	1.8	1.7	11.1%	3.1%	7.70	MP
PETRONAS DAGANGAN BHD	22.88	22,730.2	Y	12/2019	-5.6%	2.0%	12.9%	7.7%	27.2	24.1	22.3	3.9	3.7	15.6%	2.9%	22.45	MP
SAPURA ENERGY BHD	0.275	4,383.3	Y	01/2020	5.9%	20.7%	1875.6%	258.5%	N.A.	90.8	25.3	0.3	0.3	0.4%	0.0%	0.430	OP
SERBA DINAMIK HOLDINGS	4.40	6,461.4	Y	12/2019	23.2%	14.3%	17.2%	13.3%	16.8	14.4	12.7	3.1	2.7	20.2%	2.1%	5.25	OP
UZMA BHD	0.675	216.0	Y	06/2020	-7.6%	-0.1%	117.5%	44.1%	22.3	10.2	7.1	0.5	0.4	4.2%	0.0%	0.610	MP
VELESTO ENERGY BHD	0.305	2,505.8	Y	12/2019	5.3%	6.2%	119.7%	152.0%	N.A.	164.9	65.4	0.9	0.9	0.5%	0.0%	0.350	OP
WAH SEONG CORP BHD	0.610	470.0	Y	12/2019	-47.7%	-7.7%	-18.8%	-18.1%	7.5	9.2	11.2	0.5	0.5	5.4%	0.0%	0.620	MP
YINSON HOLDINGS BHD	6.95	7,509.5	Y	01/2020	0.1%	70.2%	-7.1%	55.9%	28.6	30.8	19.7	4.4	3.9	13.5%	0.9%	7.75	OP

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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