Oil & Gas

3QCY24 Report Card: Turning More Selective

OVERWEIGHT

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We maintain our OVERWEIGHT stance on the sector. 3QFY24 earnings were mixed, with equal numbers of companies under our coverage exceeding and missing expectations, particularly within the upstream services segment, while downstream and midstream companies underperformed. Notably, VELESTO reported stronger-than-expected results but anticipates weaker rig utilisation in FY25 due to changes in client's plans and the potential influx of Middle Eastern rigs. Consequently, greenfield-related companies face increased uncertainty. However, we remain optimistic about maintenance-focused players, such as those in upstream maintenance and accommodation work barges (AWBs), given the resilient demand in these areas. Additionally, regional demand is expected to bolster activity for upstream services providers amid tight supply conditions. Top picks of the sector, which all turned in an in-line quarterly reports, are DIALOG (OP; TP: RM3.37), DAYANG (OP; TP: RM3.80 and KEYFIELD (OP; TP: RM3.18).

3QFY24 report card mixed. 3QFY24 results were mixed, with 30% of companies under our coverage exceeding expectations and an equal proportion underperforming, compared to 2QFY24 when 50% exceeded expectations and only 11% fell short. Weak macro developments weighed on mid-downstream players such as MISC, PCHEM, and PETRONM, while upstream services counters like ARMADA, VELESTO, and WASCO outperformed on stronger-than-expected profit margins. This underscores the resilience of the upstream services segment amid global macro uncertainties.

To be more selective in 2025. As 2025 approaches, we recommend a more selective approach within the upstream services space, focusing on maintenance-driven sectors. VELESTO's guidance for weaker rig utilisation following HESS contract cancellations suggests a softening in drilling rig demand, though daily charter rates (DCR) remain healthy at USD90,000-110,000/day. Additionally, greenfield capex by Petronas and other producers is unlikely to see material growth given ongoing Petronas-PETROS uncertainties, though we believe the downside has been priced into valuations.

OSV supply tightness persists. The Malaysian OSV sector, particularly the AWB segment, remains bullish due to persistent vessel supply tightness from years of underinvestment. Unlike the drilling market, the local OSV market benefits from a captive structure as the cabotage policy restricts foreign vessels, while Malaysia's requirements for younger fleets (currently allowing vessels age cap of 20 years for tenders (from the cap of 15 years earlier) add to the supply constraints. With an average fleet age of 14 years, the sector is nearing a critical point for fleet renewal to sustain long-term operational efficiency. These dynamics, coupled with strong demand, position the OSV sector for continued growth and robust charter rates. If the demand sustains in the coming years, we might see a pick-up in demand for OSV newbuilds, which could potentially benefit SYGROUP (NOT RATED).

We maintain our sector call at **OVERWEIGHT** with the same emphasis placed on upstream service providers and midstream player due to a favourable macro-outlook. However, we have decided to turn more selective on our picks within the upstream service provider space as certain higher beta sub-segments appear to have shown signs of earnings peaking (for instance jack-up drilling) Post recent sell down, we believe that the risk-reward is superior in the upstream maintenance space, particularly after recent major awards for the umbrella contracts (5+5). That aside, in a space with slightly more capex uncertainty than before (possibly due to PETROS and Petronas issue), upstream maintenance still gains priority over greenfield capex-driven jobs (exploration drilling).

Our sector top picks are: -

i. **DIALOG**, given the recovery in the spot tank terminal markets, gradually improving prospects of further expansion in capacities under Pengerang Phase 3 and turn-around in margins for its EPCC, plant maintenance and specialist product businesses. We believe there is ample room for positive surprises for the stock in the medium to long term given that it is trading close to -2SD (15.3x) with FY25F PER below its historical mean of 25x.

ii. **DAYANG** is well-positioned due to its exposure to brownfield maintenance activities in the upstream sector, specifically in hook-up & commissioning and topside maintenance after the recent win in Pan Malaysia contract with a larger contract value despite less works. Its earnings growth will also be boosted by its marine division, which benefits from the booming offshore support vessel (OSV) subsegment.

iii. **KEYFIELD's** strategic focus on the maintenance-driven Offshore Support Vessel (OSV) sub-segment positions it to capitalize on sustained demand and limited vessel supply. The company's prudent fleet expansion, including the acquisition of the vessel Aulia in August 2024, aligns with its growth strategy. This approach is further supported by a robust cash flow, enabling a dividend yield of approximately 3.65% in FY24, a notable figure in the typically cyclical OSV industry.

Quarterly Results Performance

	3QCY24						2QCY24					
	KENANGA			CONSENSUS			KENANGA			CONSENSUS		
	Above	Within	Below	Above	Within	Below	Above	Within	Below	Above	Within	Below
ARMADA	1				1		1				1	
DAYANG		1			1		1			1		
DIALOG		1			1		1				1	
KEYFIELD		1			1		1					
MISC			1			1		1			1	
PCHEM			1			1			1		1	
PETDAG		1				1		1			1	
PETRONM			1						1			
VELESTO	1				1			1				1
WASCO	1				1		1				1	
Total	**3**	**4**	**3**	**0**	**6**	**3**	**5**	**3**	**2**	**1**	**6**	**1**
Total (%)	**30**	**40**	**30**	**0**	**67**	**33**	**50**	**30**	**20**	**11**	**67**	**11**

Source: Kenanga Research, Bloomberg

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net. Div. (sen)	Net Div Yld
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
BUMI ARMADA BHD	OP	0.620	0.600	-3.2%	3,675.3	Y	12/2024	15.1	11.9	167.5%	-21.6%	4.1	5.2	0.6	14.5%	0.0	0.0%
DAYANG ENTERPRISE HLDGS BHD	OP	2.03	3.80	87.2%	2,350.3	Y	12/2024	25.9	29.1	37.1%	12.7%	7.8	7.0	1.3	17.0%	6.0	3.0%
DIALOG GROUP BHD	OP	1.83	3.37	84.2%	10,326.1	Y	06/2025	11.1	11.8	3.6%	5.6%	16.4	15.6	1.6	10.3%	5.0	2.7%
KEYFIELD INTERNATIONAL	OP	2.09	3.18	52.2%	1,678.6	Y	12/2024	23.1	28.9	81.2%	25.0%	9.1	7.2	2.4	38.3%	5.0	2.4%
MISC BHD	MP	7.41	7.78	5.0%	33,076.4	Y	12/2024	50.7	50.1	5.1%	-1.1%	14.6	14.8	0.8	5.7%	30.0	4.0%
PETRONAS CHEMICALS GROUP	MP	4.83	5.00	3.5%	38,640.0	Y	12/2024	25.1	33.0	23.4%	31.7%	19.2	14.6	0.9	4.9%	12.6	2.6%
PETRONAS DAGANGAN BHD	OP	20.80	21.20	1.9%	20,663.8	Y	12/2024	99.7	109.8	1.4%	10.1%	20.9	18.9	3.5	16.9%	80.0	3.8%
PETRON MALAYSIA REFINING	MP	4.11	4.15	1.0%	1,109.7	Y	12/2024	65.6	87.4	-34.9%	33.3%	6.3	4.7	0.4	7.0%	20.0	4.9%
VELESTO ENERGY BHD	OP	0.155	0.210	35.5%	1,273.4	Y	12/2024	100.0	(72.4)	83.0%	-155.8%	0.2	N.A.	0.0	5.7%	0.0	0.0%
WASCO BHD	OP	1.10	1.83	66.4%	851.7	Y	12/2024	16.1	17.6	61.5%	9.5%	6.8	6.3	1.0	16.2%	2.0	1.8%
YINSON HOLDINGS BHD	OP	2.68	3.60	34.3%	7,869.0	N	01/2025	14.7	14.8	22.1%	1.1%	18.3	18.1	1.6	8.6%	4.0	1.5%
SECTOR AGGREGATE					**122,484.3**					**20.4%**	**5.5%**	**14.8**	**14.0**	**1.2**	**12.2%**		**2.1%**

Source: 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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