

05 June 2015 | Sector update

Oil and Gas sector

Maintain POSITIVE

A peek into the mindsets of investors and stakeholders

INVESTMENT HIGHLIGHTS

- Market expectations on crude oil price provide insights into investor and stakeholders' mindsets on how O&G industry will pan out in the coming months
- A survey was taken by MIDF Research amongst institutional funds, O&G industry professionals and quasi-government agencies
- The survey was to gauge future expectations on crude oil price, merger and acquisition (M&A) potentials and stock price valuation
- **Maintain POSITIVE** on local oil and gas sector riding on stabilising global crude oil price, sustained national crude oil production rate and stock price upside potential

The survey*. We conducted a survey amongst institutional funds, O&G industry professionals and quasi-government agencies** to gauge their perception on what will transpire in the 2H15. Three questions were asked in the survey: (i) *Expectation of Brent crude oil price at end-2015*; (ii) *Potential O&G sub-segments for mergers and acquisitions* and; (iii) *perception of current valuation for Bursa-listed O&G stocks*. Through this non-scientific survey, we believe that we can gain valuable insights into investor and stakeholders' mindsets on how the O&G industry could pan out in the coming months.

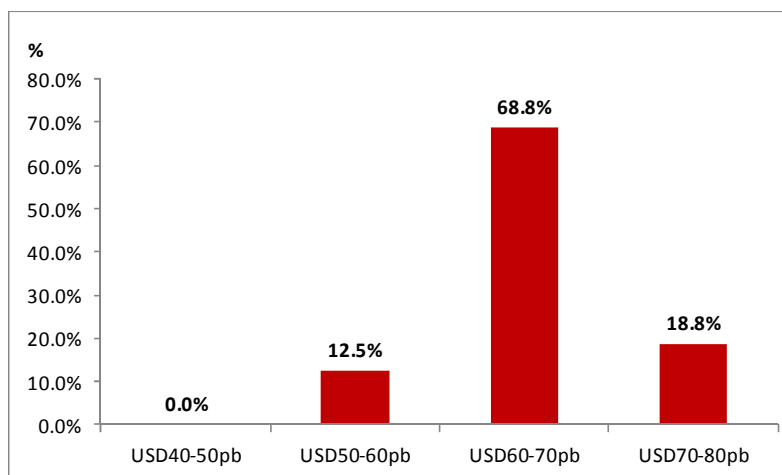
The results:

A. Expectation of Brent crude oil price by end-2015

Close to 70% of the respondents expect that the Brent crude oil price will end the year between **USD60-70pb**. However, approximately 20% of the respondents were more optimistic expecting Brent crude oil price to end 2015 above USD70pb. Only a fraction believes that Brent crude oil price could revert to levels below <USD60pb. This could indicate that both investors and industry participants are of the opinion that current crude oil price levels of USD60-68pb could be sustainable. In addition, this could also indicate that the local market expects the Organization of Petroleum Exporting Countries (OPEC) to maintain its current output target of 30mbpd. Viewed from a positive angle, investors could have come to terms that the current oil price level is the new norm and that stock prices should have priced-in and have normalised to the respective stock price levels.

QUESTION 1: What is your Brent Crude oil price expectation by year end 2015?

- USD40-50 per barrel
- USD50-60 per barrel
- USD60-70 per barrel
- USD70-80 per barrel



B. Potential O&G sub-segments for mergers and acquisitions

In addition to that, respondents were also asked which sub-segments of the O&G value chain could potentially see more active M&A activities. Approximately 31% of the respondents reckon that the Offshore Support Vessel (OSV) industry could see more M&A activities pursuant to the latest general offer launched by Dayang Enterprise Holdings Berhad (BUY; TP: RM3.82) on Perdana Petroleum Berhad (NEUTRAL; TP: RM1.55). We also believe that the reason why investors and stakeholders are expecting more M&As in the OSV sub-segment is due to the overall dismal first quarter financial results for OSV companies. The second sub-segment which investors and stakeholders (~21% of respondents) believe M&As could take place in due course is Offshore Fabrication works. Again, we believe that due to the comparatively low global oil price compared with yesteryears, large offshore fabrication projects are a rarity. As such, the market could expect large fabricators such as Malaysia Marine & Heavy Engineering Berhad (NEUTRAL; TP: RM1.27) and TH Heavy Engineering Berhad (not-rated) to experience business consolidations and costs rationalisations.

QUESTION 2: Which sub-segment of the O&G industry do you think will experience more/most merger & acquisition exercise? Multiple choices allowed.

- A. Exploration and drilling
- B. Fabrication
- C. Offshore Support Vessels
- D. Product supply ie. tubing, fluid, manpower
- E. Maintenance
- F. Others: *[please specify]*

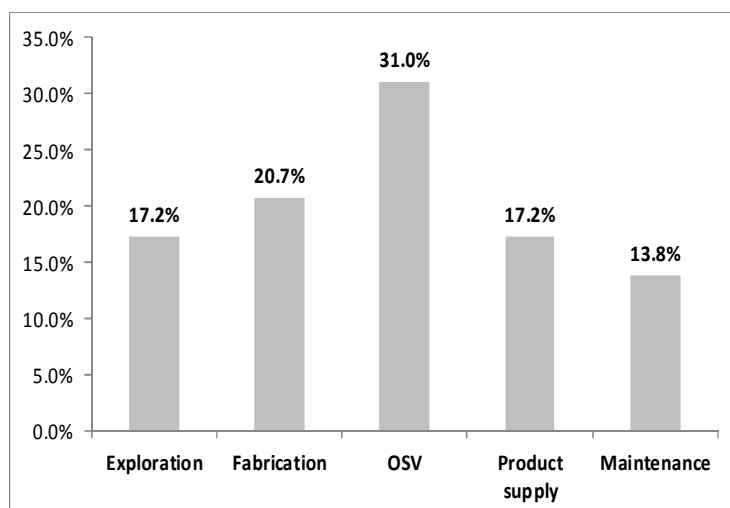


Table 1: OSV companies and fabricators with dismal 1Q15 results

Company	Revenue (RMm)		PBT (RMm)		PATAMI (RMm)		% change		
	1Q14	1Q15	1Q14	1Q15	1Q14	1Q15	Revenue	PBT	PATAMI
Icon Offshore	80.07	63.59	19.70	2.74	19.50	2.71	-20.6	-86.1	-86.1
Perdana Petroleum	87.27	69.51	22.36	9.58	22.02	8.64	-20.4	-57.2	-60.8
Alam Maritim	79.15	73.71	15.17	9.77	15.59	8.59	-6.9	-35.6	-44.9
Tas Offshore	114.29	74.37	12.28	0.58	10.46	0.68	-34.9	-95.3	-93.5
TH Heavy Engineering	142.11	47.80	0.52	-25.32	1.73	-18.85	-66.4	loss	loss

Source: Bursa Malaysia, MIDFR

C. Perception of current valuation for Bursa-listed O&G stocks

When respondents were posed with this question, a fraction of the respondents chose not to give their views on the current Bursa-listed O&G valuations. However, 50% of the respondents believe that current stock prices are undervalued, whereas 32% of respondents believe that O&G stocks are fairly-priced currently. This is interesting as no respondents were of the opinion that the general valuation for O&G stocks is overpriced. This could mean that: (i) investor interests in local O&G stocks could have return, looking for undervalued bargains or; (ii) there are no near term catalyst to re-rate local O&G stocks.

Compared to 1 January 2015 and 1 June 2014, stock prices under our coverage have generally undergone a de-rating in stock price valuations. During the fall in crude oil prices that happened over a span of six months in the latter part of 2014, overall PER for the stocks under our coverage has fallen by approximately -32% from an average of 28x (1 June 2014) to 19x (1 January 2015). The valuation subsequently consolidated and gained some footing to 20x (3 June 2015) after crude oil prices were seen holding steady above USD60pb. As such, there is currently a split view with one camp believing that stock prices will continue to trade sideways and the other camp believing that prices could experience an uptrend in due course.

QUESTION 3: In general, do you think that the overall Bursa-listed oil and gas companies stocks are *overvalued, fairly-valued or undervalued* given the current crude oil price and investor sentiments?

- A. Overvalued
- B. Undervalued
- C. Fairly valued
- D. No opinion

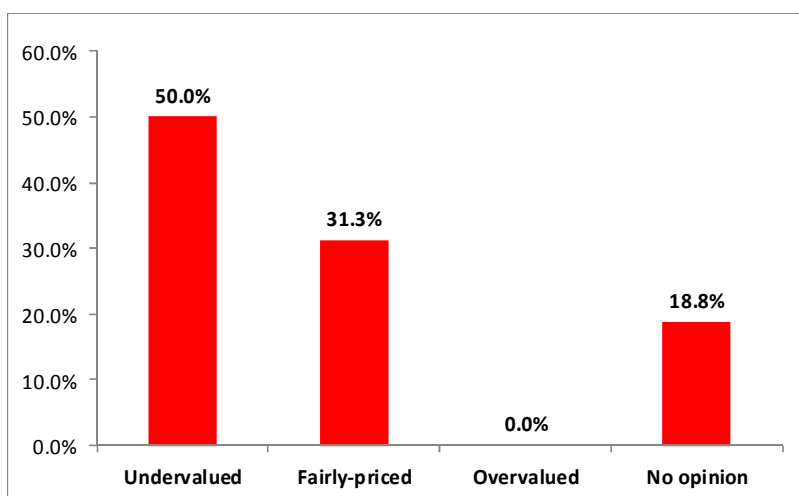


Table 2: Stock price valuation

Company	Last price (RM)	Target Price (RM)	Call	PER (x)		
				at 1 June 2014	at 1 January 2015	at last price
Bumi Armada	1.30	1.20	Neutral	51.2	26.3	30.2
Dayang Enterprise Holdings	2.48	3.82	Buy	17.4	13.7	11.6
Dialog Group	1.68	1.57	Neutral	40.0	33.0	36.5
Gas Malaysia	2.82	2.87	Neutral	27.7	24.0	21.5
Sapurakencana Petroleum	2.68	3.39	Buy	22.8	12.8	14.8
KNM Group	0.55	1.15	Buy	25.5	16.6	19.0
Malaysia Marine & Heavy Engineering	1.31	1.27	Neutral	46.9	21.6	16.2
Petronas Gas	21.98	19.27	Neutral	25.6	23.6	23.6
Petronas Chem	6.21	5.04	Neutral	21.7	17.4	20.0
Wah Seong Corp	1.45	1.91	Buy	12.1	7.5	8.9
Perdana Petroleum	1.52	1.55	Neutral	14.8	9.3	12.7
Favelle Favco	2.77	3.30	Buy	8.5	6.9	6.8
Petronas Dagangan	19.90	17.47	Neutral	48.5	33.9	39.4
Average PER (x)				27.9	19.0	20.1

Source: MIDFR

In conclusion, this survey gives us an insight into the mindsets of investors and stakeholders. The market generally believes that global crude oil prices could continue to hover at current levels and that the OSV and fabrication businesses could experience consolidations moving forward. In addition, investors also opine that current valuations for O&G stocks are either undervalued or fairly-priced. We continue to reiterate our **POSITIVE** stance on the oil and gas sector, riding on stabilising global crude oil price, sustained national crude oil production rate and stock price upside potential. Maintain 2015 average Brent Crude oil price forecast at **USD60-70pb.**



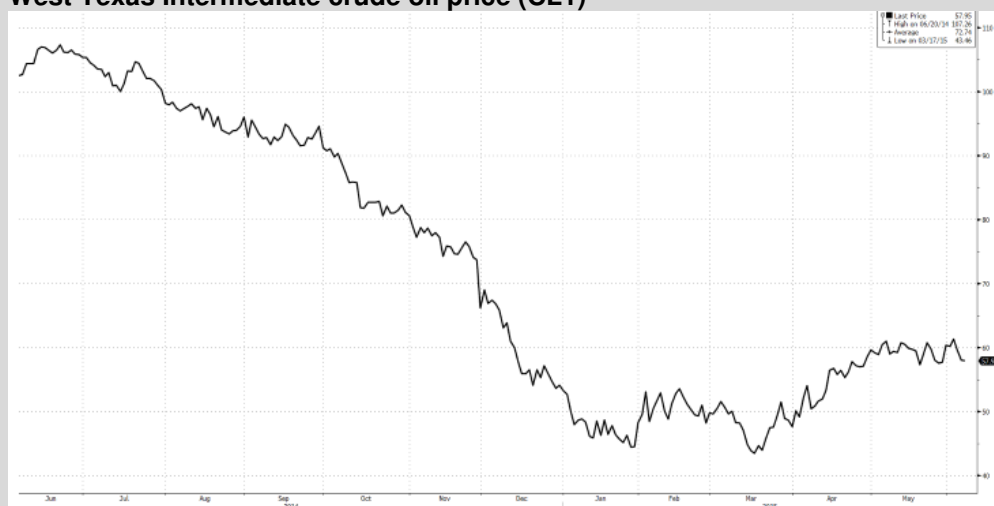
DAILY PRICE CHART

Brent crude oil price (CO1)



Source: Bloomberg, MIDFR

West Texas Intermediate crude oil price (CL1)



Source: Bloomberg, MIDFR

Aaron Tan Wei Min
aaron.tan@midf.com.my
03-2772 1650

* The survey conducted is non-scientific in nature

**50% of respondents are from Institutional funds (Fund Manager & Analysts), 44% from O&G industry (professionals) and 6% from quasi-government agencies

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.