midf RESEARCH

15 May 2018 | 1QFY18 Results Review

MISC Berhad

Petroleum segment remains challenging

Maintain NEUTRAL

Reduced Target Price (TP): RM7.14

(Previously: RM7.36)

INVESTMENT HIGHLIGHTS

- **1QFY18 earnings below estimates**
- **Long term contracts to sustain LNG segment**
- **Petroleum segment to remain weak**
- **Contract renewal risks linger in offshore division**
- **Challenging outlook for heavy engineering**
- **Maintain NEUTRAL with reduced TP of RM7.14 per share**

1QFY18 results below expectations. MISC reported a normalised PATAMI of approximately RM331.6m in 1QFY18 which was -62.3%yoy lower and was below our and consensus estimates by a variance of more than 5%.

Lower number of operating LNG vessels. The revenue and PBT of the LNG segment in 1QFY18 both declined by -11.3%yoy and -7.4%yoy respectively. The decline in revenue and PBT is mainly attributable to the lower number of operating vessel and lower charter rates locked in for Puteri Firus back in October 2017.

Resilient LNG time charter rates. Most LNG vessels of MISC operate on long term charter contracts which have been quite resilient and higher compared to spot charter rates for most of the time. Meanwhile on average, the LNG spot rates in 1Q18 declined by about -5.6% amid onset of warmer weather and oversupply of tonnage. This trend low spot rates is expected to persist due to the huge pile-up of new deliveries in 2018. With the delivery of Seri Camar and Seri Cemara in 1HFY18 that operate on long term contracts, this could further support the growth in earnings in addition to the extension of time charter contracts for Seri Bakti and Seri Anggun.

Petroleum segment remains in the red. The petroleum segment registered a loss before tax for the fourth consecutive quarter as charter rates secured were much lower than expected amid tonnage oversupply. Management guided that the segment to perform weaker than the year before. Nonetheless, the pickup in scrapping activities in the environment of slow crude tanker growth bodes well for freight rates in the long term. Moreover, higher term to spot ratio of 55:45 compared to 53:47 in 1QFY17 for its petroleum vessels acts as a sustainability factor for the segment.

RETURN STATS	
Price (14 May 2018)	RM7.00
Target Price	RM7.14
Expected Share Price Return	+2.0%
Expected Dividend Yield	+4.3%
Expected Total Return	**+6.3%**

STOCK INFO	
KLCI	1,850.42
Bursa / Bloomberg	3816 / MISC MK
Board / Sector	Main / Trading Services
Syariah Compliant	Yes
Issued shares (mil)	4,463.8
Market cap. (RM'm)	31,246.55
Price over NA	0.90
52-wk price Range	RM6.73 - RM7.90
Beta (against KLCI)	0.92
3-mth Avg Daily Vol	1.46m
3-mth Avg Daily Value	RM10.3m
Major Shareholders (%)	
Petronas	62.67
PNB	7.15
EPF	5.93

Renewal risk for FSO contracts. The offshore segment recorded a -246%yoy decline in PBT following the construction of FSO Benchamas 2 nearing its completion towards the end of 1QFY18. In mid-April, the FSO Benchamas 2 arrived at Chevron's field and is expected to contribute earnings of not more than USD10m per annum. Support in the offshore segment will come from the stable and higher oil prices coupled with improved prospects following the expected increase of project approval both locally and internationally. Furthermore, the cost in offshore upstream projects has declined by about 40% since 2014, giving more viability of the project targeted. Notwithstanding this, other existing offshore contracts that are expiring in FY18 and FY19 such as FSO Angsi, FPSO Ruby 2 and FPSO Bunga Kertas are in the midst of renegotiations. Hence, this represents a contract renewal risk which may outweigh the impact from the new FSO and extension of other FSO contracts as overall earnings in the segment may decline amid the recognition of the finance lease.

Challenging outlook for heavy engineering. Despite crude oil prices and the overall operating climate improving, FY18 will continue to be a challenging year for the heavy engineering segment. This is predominantly due to the timing differences in revenue and profit recognition between tail-end projects and new projects. The large portion of its orderbook consist of the RM1b Bokor CPP job which will only undergo the first steel cut in 3QFY18 – the large portion of works will happen only in FY19. Overall segment contribution is less than 10% of total group profit.

Earnings impact. We are revising our earnings downwards our earnings forecast for FY18 and FY19 by 12.2% and 11.1%, respectively after taking into account the lower revenue from petroleum that is expected to be weaker in FY18.

Maintain NEUTRAL with reduced TP of RM7.14 per share (previously RM7.36 per share) pegged to 0.89x price-to-book value representing a discount of -1.0(previously -0.75) standard deviation below its five-year average to reflect the lower charter rates amid tonnage oversupply. Our neutral stance is predicated on: (i) timing differences in revenue recognition of tail end and new projects for the heavy engineering segment, (ii) contract renewal risk for its FSO projects and (iii) low demolition in the LNG shipping space. This could be offset by MISC Berhad's strategic term-to-spot ratio for its petroleum vessels coupled with its chemical tankers being injected into a pool to optimise utilisation.

Figure 1: LNG tanker rates (US$'000/day)

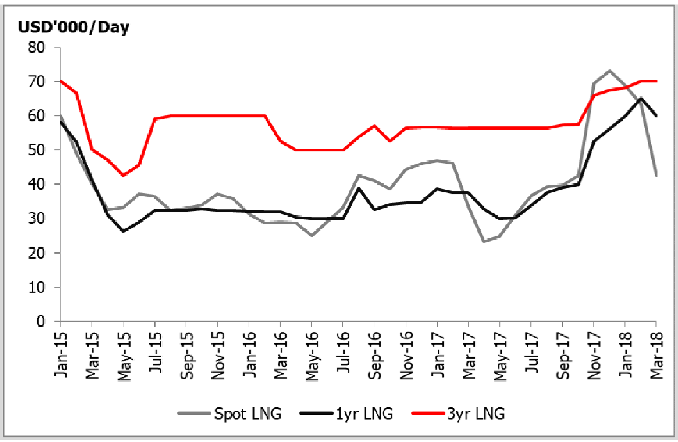
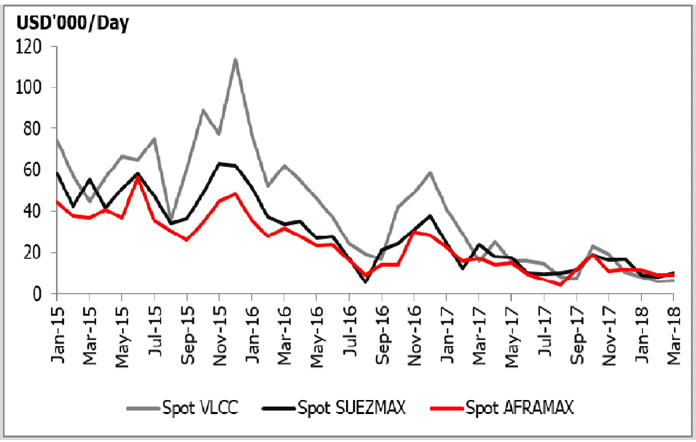


Figure 2: Spot Petroleum tanker rates (US$'000/day)



Source: Company, Ship Brokers' Reports, MIDFR

INVESTMENT STATISTICS

FYE Dec	FY15	FY16	FY17	FY18F	FY19F
Revenue (RM' m)	10,908.4	9,597.2	10,068.2	9,282.5	9,466.1
EBIT (RM' m)	2,746.9	3,011.6	2,172.1	2,092.9	2,212.9
Pretax Profit (RM' m)	2,566.9	2,814.0	2,003.6	1,873.4	2,034.9
Net Profit (RM' m)	2,513.9	2,793.3	1,990.7	1,862.1	2,022.7
Normalised Profit (RM'm)	3,085.1	1,883.0	2,788.9	1,862.1	2,022.7
EPS (sen)	69.4	42.2	62.5	41.7	45.3
EPS growth (%)	75.4	-39.2	48.1	-6.5	8.6
PER (x)	10.1	16.6	11.2	16.8	15.4
Net Dividend (sen)	30.0	30.0	30.0	30.0	30.0
Net Dividend Yield (%)	4.3	4.3	4.3	4.3	4.3

Source: MIDFR, Company

DAILY PRICE CHART

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Source: Bloomberg

MISC: 1QFY18 RESULTS SUMMARY

All in RM'm unless stated otherwise	Quarterly Results					*Comments*
FYE Dec	***1QFY18***	***4QFY17***	***1QFY17***	***%QoQ***	***%YoY***	
Revenue	2020.8	2434.5	2984.9	-17.0	-32.3	Lower operating vessels
COGS	(1456.6)	(1713.0)	(1883.8)	-15.0	-22.7	
Gross profit	564.2	721.5	1101.1	-21.8	-48.8	
Other income	65.8	151.8	62.0	-56.7	6.1	
SG&A	(246.6)	(246.3)	(481.8)	0.1	-48.8	
Operating profit	383.4	627.0	681.3	-38.9	-43.7	
Finance Cost	(75.7)	(68.6)	(65.8)	10.3	15.0	
Assoc. & JV Contribution	12.6	35.9	50.3	-64.9	-75.0	
Exceptional gain/(loss)	(1.1)	(552.3)	30.8	-99.8	-103.6	
Profit before tax	319.2	42.0	696.6	660.0	-54.2	
Taxation	(10.2)	5.1	(2.7)	-300.0	277.8	
PATAMI	309.0	68.2	676.2	353.1	-54.3	
Normalized PATAMI	331.6	565.0	879.2	-41.3	-62.3	

OPERATING SUMMARY (USD'm)

Segmental Revenue	***1QFY18***	***4QFY17***	***1QFY17***	***%QoQ***	***%YoY***	***Comments***
LNG	148.9	153.8	167.9	-3.2	-11.3	Lower operating vessel
Petroleum	248.7	281.5	289.0	-11.7	-13.9	Lower freight rate
Offshore	75.1	107.4	165.2	-30.1	-54.5	Construction of Benchamas 2 nearing the end
Heavy Engineering	45.8	60.0	53.0	-23.7	-13.6	Timing difference of revenue and profit recognition
Total	518.5	602.7	675.1	-14.0	-23.2	
Segmental PBT	***1QFY18***	***4QFY17***	***1QFY17***	***%QoQ***	***%YoY***	***Comments***
LNG	65.3	(20.2)	70.5	-423.3	-7.4	
Petroleum	(18.4)	(70.9)	12.6	-74.0	-246.0	
Offshore	32.4	83.4	73.2	-61.2	-55.7	
Heavy Engineering	(6.6)	17.2	(4.0)	-138.4	65.0	
Total	72.7	9.5	152.3	665.3	-52.3	

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% 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.