DELEUM

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Deleum's earnings upcycle seen to materialise in 2H

Deleum Bhd
(Feb 27, RM1.07)

Maintain neutral with an unchanged target price (TP) of RM1.03: Deleum Bhd's earnings for the fourth quarter of financial year 2017 (4QFY17) grew by +36.2% year-on-year (y-o-y) to RM13.5 million — highest since 2QFY15. Cumulative FY17 earnings of RM32.3 million (+21.7% y-o-y) outpaced our expectations by a variance of more than >10%.

Although segmental revenue contracted by -15.1% y-o-y, segmental profit managed to stage growth of +9% y-o-y to RM39.1 million. The contraction in revenue was largely due to lower work orders for exchange engines and retrofit projects. The higher profit on the other hand was due to a one-off restructuring charge in 4QFY16 of RM4.4 million. Excluding this one-off charge, the segmental normalised profit would have contracted by approximately -3% y-o-y.

Segmental revenue also contracted by -11.9% y-o-y largely due to a lower utilisation of slickline assets. Despite this, profit grew by +16% y-o-y to RM14.5 million attributable to higher margin from oilfield chemicals, lower write-offs and lower financing costs.

Although segmental revenue grew by +14% y-o-y, segmental profit remained flât y-o-y for the quarter largely attributable to lower-margin works and mobilisation costs related to the maintenance, construction and modification (MCM) win.

Based on its recent MCM win, we believe that the earnings upcycle is likely to happen in the second half of FY18 (2HFY18). Our view is largely due to the fact that earnings accretion from the MCM jobs will most likely be recognised towards the latter part of FY18 only. The bulk of the activity and earnings will most likely take place in FY19.

Although FY17 earnings posted better-than-expected earnings, we are maintaining our earnings forecast at this juncture as the power and machinery (P&M) segment is still expected to remain challenging while a large portion of the oilfield service projects are due to expire in 2018 and 2019. Based on the anticipated earnings upcycle in 2HFY18 from the MCM contracts and the challenging P&M division, we are maintaining our TP at RM1.03. Our TP is premised on price-earnings ratio (PER) of 12 times pegged to earnings per share (EPS) of 8.6 sen. We are maintaining our "neutral" recommendation but reiterate that Deleum's company fundamentals and prospects remain intact.

— *MIDF Research, Feb 27*