

Malaysia

HOLD (no change)

Consensus ratings*: Buy 4 Hold 3 Sell 1

Current price:	RM0.12
Target price:	RM0.115
Previous target:	RM0.135
Up/downside:	-4.2%
CGS-CIMB / Consensus:	-30.6%
Reuters:	VELE.KL
Bloomberg:	VEB MK
Market cap:	US\$224.3m
	RM985.9m
Average daily turnover:	US\$0.49m
	RM2.07m
Current shares o/s:	8,216m
Free float:	38.0%

*Source: Bloomberg

Key changes in this note

- FY22F core net profit forecast of RM35m slashed to a core net loss of RM38m, as we cut our JU utilisation assumption from 70% to 57%.
- FY23F core EPS forecast reduced by 5% and FY24F core EPS forecast raised by 6% on various housekeeping adjustments.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	9.1	-4	-11.1
Relative (%)	12.5	-0.5	-8.4

Major shareholders	% held
Permodalan Nasional Bhd	54.4
Urusharta Jamaah	5.0

Analyst(s)



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Velesto Energy Berhad

FY22F likely in the red; FY23F may improve

- 1Q22 core net loss of RM46m was below expectations against our full-year profit forecast of RM35m and consensus loss forecast of RM12m.
- Reiterate Hold with lower DCF-based TP of 11.5 sen as we cut our FY22F utilisation assumption and raise the cost of equity discount rate.
- We expect Velesto to report a quarterly loss in 2Q22F that is fairly similar to 1Q22, and for FY22F to be in the red, though we expect profits in FY23F.

Poor 1Q22 and low 2Q22F expectations; more 2H22F work needed

Velesto's 1Q22 core net loss of RM46m was a significant deterioration from 4Q21's RM12m core net profit, due mainly to the qoq drop in jack-up (JU) drilling rig utilisation to 39% in 1Q22 from 74% in 4Q21. Nevertheless, Velesto narrowed its loss yoy, as the JU utilisation in 1Q22 was better than 1Q21's 28%, depreciation fell due to the write-off of the Naga 7 JU rig which sank on 3 May 2021, and interest expense also dropped as Velesto used the insurance compensation to reduce its outstanding debt. We do not expect much improvement for Velesto in 2Q22F. Drilling contracts secured to-date suggest utilisation of just 41%, a marginal improvement from 1Q22's 39%; hence we expect Velesto's 2Q22F core net loss to be almost as large as for the 1Q22. Assuming no additional work, Velesto may deliver 55% utilisation in 3Q22F and 62% in 4Q22F, which is insufficient to report profits for 2H22F. This implies 49.5% utilisation for FY22F, just slightly better than FY21's disappointing 48% utilisation. Having said that, we expect new work to emerge for Naga 5 and Naga 6 in 2H22F, both of which have barely drilled this year and have not yet secured any forward jobs. In the most optimistic scenario where all available Naga 5 and Naga 6 capacity in 2H22F is fully utilised, we calculate that Velesto can at most achieve 65% utilisation for FY22F, or 57% if half of available Naga 5 and Naga 6 capacity in 2H22F is utilised. We have adopted 57% as the basis for our new FY22F utilisation assumption, revised lower from 70% previously.

FY23F outlook should be better; cost inflation remains a risk

The outlook for FY23F may improve because higher oil prices tend to spill over into higher drilling capex by oil companies with a lag. Hence, we retain our FY23F utilisation assumption of 70%, which is a step-up from FY22F's 57% utilisation. Velesto's average charter rates may also benefit after this year's upgrade of the Naga 5 and Naga 6 to possess offline capabilities, which typically lifts rates from the low-US\$70,000s to the high-US\$70,000s. Conversely, it may be difficult for Velesto to achieve utilisation higher than 70% unless it secures long-term contracts, which at the moment, remain rare. Apart from the Naga 5 and Naga 6, rate upside may be capped by Velesto having assigned all of its rigs to Petronas Carigali's call-out umbrella contract for the next two years, effective 1Q22. Cost inflation remains a concern, due to the rush to secure manpower and other resources as drilling work throughout SE Asia picks up pace. The main upside risk relates to the potential for utilisation rates to exceed our 70% assumption, but the key downside risk is for cost inflation to undo Velesto's 3-year cost optimisation efforts.

Financial Summary

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue (RMm)	546.9	377.5	420.1	519.0	509.8
Operating EBITDA (RMm)	273.4	14.5	135.8	235.5	237.0
Net Profit (RMm)	(491.7)	(90.8)	(38.4)	59.7	64.5
Core EPS (RM)	(0.001)	(0.023)	(0.005)	0.007	0.008
Core EPS Growth	(125%)	2092%	(79%)	8%	
FD Core P/E (x)	NA	NA	NA	16.51	15.29
DPS (RM)	-	-	-	-	-
Dividend Yield	0%	0%	0%	0%	0%
EV/EBITDA (x)	6.14	87.94	8.90	4.79	4.43
P/FCFE (x)	12.56	74.85	NA	26.59	77.60
Net Gearing	30.6%	12.8%	10.1%	6.3%	2.8%
P/BV (x)	0.43	0.44	0.44	0.43	0.42
ROE	(0.33%)	(8.20%)	(1.71%)	2.64%	2.78%
% Change In Core EPS Estimates			(209%)	(5%)	6%
CGS-CIMB/Consensus EPS (x)				1.82	0.98

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

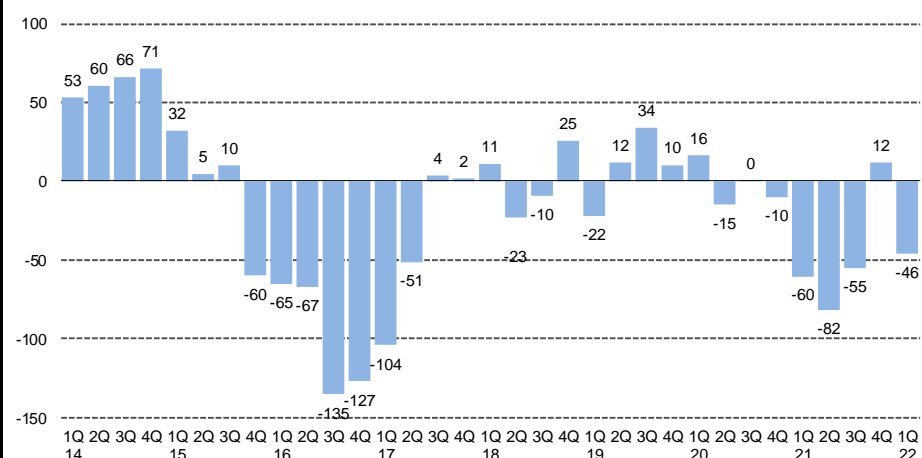
Results comparison table ►

Figure 1: Results comparison

FYE Dec (RM m)	1QFY22	1QFY21	yoy %	4QFY21	qoq %	Prev.	
			chg		chg		FY22F Comments
Revenue	77.4	43.9	76.2	158.5	(51.2)	489.9	1Q22 rev fell 51% qoq on lower utilisation rate of 39% vs.
Operating costs	(83.1)	(53.5)	55.4	(108.2)	(23.2)	(273.4)	78% in 4Q21, which caused 1Q21 EBITDA to fall into a
EBITDA	(5.7)	(9.5)	(40.3)	50.2	(111.3)	216.5	loss, vs. profit in 4Q21.
EBITDA margin (%)	(7.4)	(21.7)	-	31.7	-	44.2	
Depn & amort.	(35.6)	(41.2)	(13.5)	(39.3)	(9.2)	(147.4)	Depreciation fell yoy due to write-off of the Naga 7, which sank
EBIT	(41.3)	(50.7)	nm	11.0	(476.7)	69.1	on 3 May 2021; Velesto received insurance compensation.
Interest expense	(5.1)	(10.8)	(52.8)	(8.1)	(37.1)	(31.6)	Lower interest expense due to lower level of borrowings, as
Interest & invt inc	0.6	1.2	(49.0)	8.8	(93.1)	4.5	Velesto utilised part of the insurance receipts to repay debt.
Associates' contrib	0.0	0.0	(11.4)	0.0	14.7	0.5	
Exceptionals	-	-	nm	(6.5)	(100.0)	-	
Pretax profit	(45.8)	(60.3)	(24.1)	5.2	(978.2)	42.5	
Tax	(0.4)	(0.2)	125.1	0.2	(298.6)	(7.2)	
Tax rate (%)	(0.9)	(0.3)	-	(4.1)	-	17.0	
Minority interests	-	-	nm	-	nm	-	
Net profit	(46.2)	(60.5)	(23.6)	5.4	(951.6)	35.3	Core net loss in 1Q22 due to the low utilisation, vs. core net
Core net profit	(46.2)	(60.5)	(23.6)	12.0	(486.1)	35.3	profit in 4Q21. Core net loss narrowed yoy from 1Q21, as the
EPS (sen)	(0.6)	(0.7)	(23.6)	0.1	(951.6)	0.4	1Q21 utilisation was even lower at only 28%.
Core EPS (sen)	(0.6)	(0.7)	(23.6)	0.1	(486.1)	0.4	

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 2: Velesto Energy quarterly core net profit/(loss) (RM m)



SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 3: Earnings revision

RM m	2021A	2022F			2023F			2024F		
		Old	New	chg	Old	New	chg	Old	New	chg
Revenue	378	490	420	-14%	497	519	4%	487	510	5%
EBITDA	14	216	136	-37%	238	235	-1%	232	237	2%
Reported PBT	(82)	43	(38)	-190%	72	69	-4%	71	75	5%
Core pretax profit	(177)	43	(38)	-190%	72	69	-4%	71	75	5%
Reported net profit	(91)	35	(38)	-209%	63	60	-5%	61	64	6%
Reported EPS	(0.01)	0.00	(0.00)	-209%	0.01	0.01	-5%	0.01	0.01	6%
Core net profit	(186)	35	(38)	-209%	63	60	-5%	61	64	6%
Core EPS	(0.02)	0.00	(0.00)	-209%	0.01	0.01	-5%	0.01	0.01	6%

SOURCES: CGS-CIMB RESEARCH ESTIMATES, COMPANY REPORTS

DCF assumptions and target price ►

Figure 4: Assumptions and DCF valuation

Assumptions				
	2017-20	2021-23F	2024-33F	2033-45F
JU: Utilisation (%)	72%	64%	70%	70%
JU: Daily earnings (US\$/day)	71,108	71,207	72,357	72,000
JU: Daily working cash costs (US\$/day)	36,367	22,167	27,700	28,000
JU: Daily stacked cash costs (US\$/day)	10,000	10,000	10,000	10,000
DCF valuation		Cost of equity		
	FY22F	Rf		4.25%
DCF value to equity (RM m)	432.6	ERP		6.00%
Add: Cash (end of FY)	255.1	Beta		2.0
Add: Residual net assets (end of FY)	252.6	Ke (nominal)		16.25%
Total equity valuation (RM m)	940.4			
No of shares (m)	8,215.6			
Per share equity valuation (RM)	0.114			
Rounded target price (RM)	0.115			

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

We cut our DCF-based target price from 13.5 sen to 11.5 sen, on account of:

- A reduction of our FY22F JU utilisation rate assumption from 70% to 57%;
- An increase in the risk-free rate assumption from 3.7% to 4.25% (to reflect the increase in 10-year Malaysian government bond yields), which increases our cost of equity discount rate from 15.7% to 16.25%; partially offset by
- An increase in the US\$ exchange rate assumption from RM4.20 to RM4.30.

Upside risks: Petronas may raise its domestic drilling capex in light of the higher oil prices, particularly for FY23F. We have assumed JU utilisation of 70% from FY23F onwards, up from FY21's 48% and FY22F's 57%.

Downside risks: Operating cost inflation could accelerate in the quarters ahead as rig utilisation in Malaysia and SE Asia increases.

Velesto's secured drilling contracts ►

Figure 5: Velesto's drilling contracts from FY19 onwards

BASED ON RIGLOGIX DATA (MODIFIED BY INFORMATION FROM VELESTO)

Firm contracts	Days													
	FY19	FY20	1Q21	2Q21	3Q21	4Q21	FY21	1Q22	2Q22F	3Q22F	4Q22F	FY22F	FY23F	FY24F
Naga 2	220	298	0	0	46	92	138	59	61	92	6	218	0	0
Naga 3	231	0	0	0	0	0	0	0	0	30	50	80	0	0
Naga 4	365	315	90	75	46	87	298	46	73	92	92	303	59	0
Naga 5	289	182	0	61	92	92	245	5	0	0	0	5	0	0
Naga 6	282	321	0	0	0	78	78	10	0	0	0	10	0	0
Naga 7	286	337	90				90							
Naga 8	365	154	0	91	92	92	275	90	91	92	92	365	365	91
Total firm contract days	2,038	1,607	180	227	276	441	1,124	210	225	306	240	981	424	91

Option periods

Naga 2	0	0	0	0	0	0	0	0	0	0	64	64	0	0
Naga 3	0	0	0	0	0	0	0	0	0	0	40	40	0	0
Naga 4	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Naga 5	0	0	0	0	0	0	199	0	0	0	0	5	0	0
Naga 6	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Naga 7	0	0	0				0	0						
Naga 8	0	0	0	0	0	0	0	0	0	0	0	0	0	275
Total option contract days	0	0	0	0	0	0	199	0	0	0	104	109	0	275

BASED ON RIGLOGIX DATA (MODIFIED BY INFORMATION FROM VELESTO)

CURRENT CONTRACTS

Total contract days	2,038	1,636	180	227	276	441	1,124	210	225	306	344	1,085	424	366
- Firm contract days	2,038	1,636	180	227	276	441	1,124	210	225	306	240	981	424	91
- Option contract days	0	0	0	0	0	0	0	0	0	0	104	104	0	275
Total calendar days	2,555	2,555	637	576	552	552	2,317	540	546	552	552	2,190	2,190	2,190
Total utilisation rate (%)	79.8%	64.0%	28.3%	39.4%	50.0%	79.9%	48.5%	38.9%	41.2%	55.4%	62.3%	49.5%	19.4%	16.7%
- Firm contract days	79.8%	64.0%	28.3%	39.4%	50.0%	79.9%	48.5%	38.9%	41.2%	55.4%	43.5%	44.8%	19.4%	4.2%
- Option contract days	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	18.8%	4.7%	0.0%	12.6%

BASED ON VELESTO'S QUARTERLY DISCLOSURES

Total contract days	2,034	1,664	176	219	282	431	986	211
Total utilisation rate (%)	79.6%	66.0%	28.0%	38.0%	51.0%	78.0%	48.0%	39.0%

SOURCES: CGS-CIMB RESEARCH, RIGLOGIX, COMPANY REPORTS

Naga 2

Naga 2's 5-well firm drilling contract with Petronas Carigali was supposed to begin in early-April 2022, but the start date was delayed to late-April instead. Drilling is scheduled to continue until early-October 2022, after which Petronas Carigali has the option to exercise two 1-well drilling contracts, lasting about 30 days each.

Naga 3

The Naga 3 has been idle since late-May 2020, and recently secured a 2-well firm and 1-well option drilling contract with Vietnam's Hoang Long Joint Operating Company (JOC). Drilling is scheduled to start in early-October and last until end-December 2022. In the meantime, the Naga 3 has been sent to a shipyard for technical modification works from mid-May and will remain in the yard until late-August. This means that it will not be able to accept any additional jobs while waiting for the Hoang Long JOC work to begin.

Naga 4

Naga 4's contract with Sarawak Shell was supposed to start in February or March 2022, but the start date was delayed to mid-April 2022. The 7-well drilling contract will last until end-February 2023.

Naga 5

Naga 5's drilling contract for Petronas Carigali ended in early-January 2022, and was sent to Keppel Shipyard for offline capability upgrades from early-March. It will exit the yard in late-May 2022. Velesto has not announced any work for the Naga 5 following its shipyard exit, but Riglogix reported it may drill for PTTEP Malaysia or Hess Malaysia, from October 2022 onwards.

Naga 6

Naga 5's drilling contract for Petronas Carigali ended in early-January 2022, and was sent to Keppel Shipyard for offline capability upgrades from early-May to early-August 2022. Velesto is working to secure new work for Naga 6 after that.

Naga 8

The Naga 8 has been working for Carigali Hess Operating Company since early-April 2021 under a 3-year firm contract until early-April 2024, to be followed by three 6-month options.

Further information on the results ►

Figure 6: Revenue metrics

	1QFY22	1QFY21	yoy %	4QFY21	qoq %	
			chg			chg Comments
Revenue (RM m)	77.4	43.9	76.2	158.5	(51.2)	Drilling revenue fell qoq in 1Q22 due to lower JU utilisation rates.
- Drilling services	74.2	40.8	82.0	151.0	(50.9)	Drilling revenue rose yoy in 1Q22 due to higher utilisation rates
- Oilfield services	2.3	3.0	(21.1)	7.1	(67.1)	and higher average charter rates.
Number of rigs	6	7	(14.3)	6	-	The number of JU rigs dropped by one, due to the sinking of the
Number of HWUs	4	4	-	4	-	Naga 7 on 3 May 2021.
Drilling calendar days	540	630	(14.3)	552	(2.2)	
Days employed	211	176	19.4	431	(51.1)	
Utilisation rate	39.0%	28.0%	11.0%	78.0%	-39.0%	Utilisation rates rose yoy but fell qoq.
Charter rates (US\$/day)	75,319	53,000	42.1	74,222	1.5	Average charter rates were depressed in 1Q21, as the Naga 7 was used as a floating hotel at a low daily charter rate.

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 7: Cost metrics & operating profit

	1QFY22	1QFY21	yoy %	4QFY21	qoq %	
			chg			chg Comments
Drilling costs (RM m)	105.3	79.5	32.6	128.7	(18.1)	Cash opex rose yoy in 1Q22 due to higher utilisation rate of
- Cash operating costs	69.8	38.4	81.9	89.5	(22.0)	JU rigs.
- Depreciation	35.5	41.1	(13.5)	39.1	(9.3)	
Drilling EBIT (RM m)	(31.1)	(38.7)	nm	22.4	nm	Drilling EBIT fell into a loss in 1Q22 vs. profit in 4Q21 due to
EBIT margin (%)	-42.0%	-94.9%		14.8%		the lower utilisation of JU rigs.

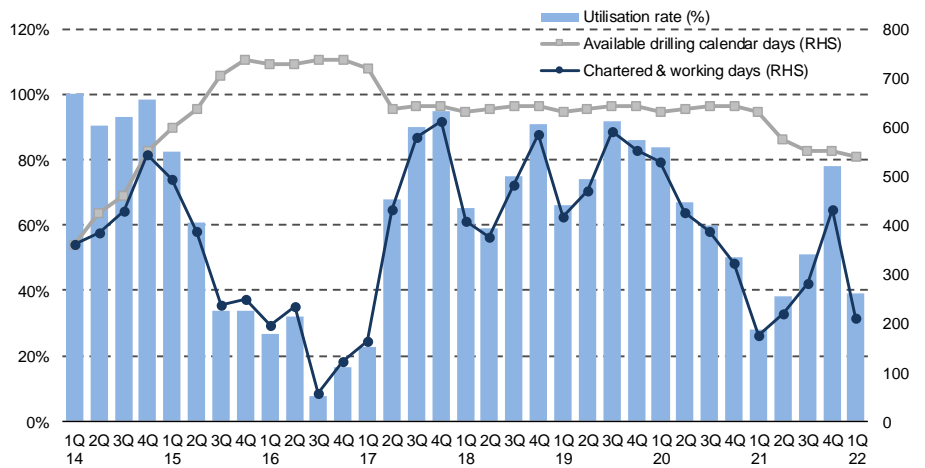
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 8: Segmental profit after tax

	1QFY22	1QFY21	yoy %	4QFY21	qoq %	
			chg			chg Comments
Profit after tax (RM m)	(44.1)	(58.6)	nm	5.4	(912.4)	Drilling segment turned into a loss in 1Q22 vs. profit in 4Q21, as
- Drilling services	(36.3)	(49.0)	(26.1)	15.0	(341.5)	utilisation rates fell qoq.
- Oilfield services	0.3	0.5	(37.0)	(1.5)	(119.0)	
- Others	(8.1)	(10.1)	(19.4)	(8.0)	0.7	

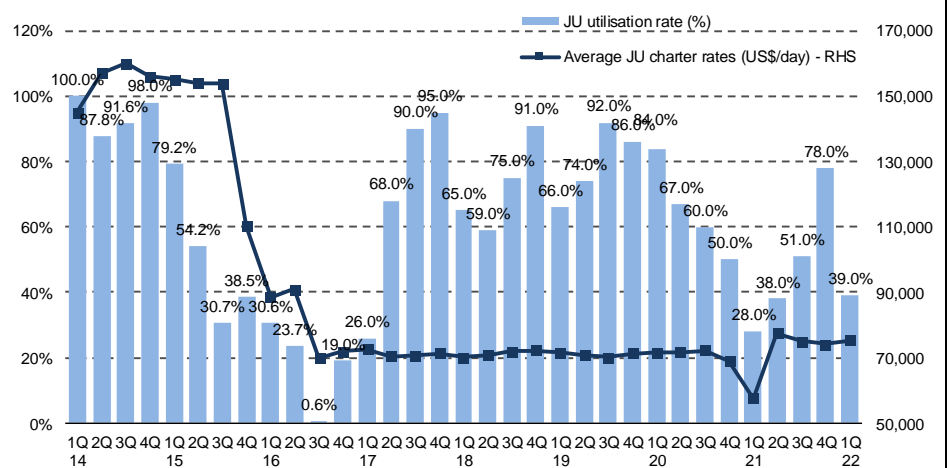
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 9: Capacity and utilisation rate of Velesto's drilling rigs (firm charters only)



SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 10: Average JU charter rates and utilisation rate of Velesto's drilling rigs



SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Sequential quarterly tables ►

Figure 11: Results comparison

FYE Dec (RM m)	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22
Revenue	176.3	140.9	130.7	99.1	43.9	83.6	91.5	158.5	77.4
Operating costs	(80.2)	(79.7)	(64.4)	(49.2)	(53.5)	(104.9)	(96.4)	(108.2)	(83.1)
EBITDA	96.1	61.3	66.2	49.8	(9.5)	(21.3)	(4.9)	50.2	(5.7)
EBITDA margin (%)	54.5	43.5	50.7	50.3	(21.7)	(25.5)	(5.3)	31.7	(7.4)
Depn & amort.	(60.8)	(59.4)	(50.8)	(49.0)	(41.2)	(39.0)	(37.5)	(39.3)	(35.6)
EBIT	35.2	1.9	15.4	0.8	(50.7)	(60.4)	(42.4)	11.0	(41.3)
Interest expense	(19.5)	(17.6)	(14.4)	(12.8)	(10.8)	(10.8)	(10.1)	(8.1)	(5.1)
Interest & invt inc	2.0	2.1	1.8	11.2	1.2	(6.2)	1.3	8.8	0.6
Associates' contrib	0.0	0.1	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Exceptionals	-	-	-	(483.3)	-	98.2	3.2	(6.5)	-
Pretax profit	17.7	(13.5)	2.8	(484.0)	(60.3)	20.8	(48.0)	5.2	(45.8)
Tax	(1.4)	(1.7)	(2.4)	(9.3)	(0.2)	(4.5)	(4.1)	0.2	(0.4)
Tax rate (%)	7.9	(12.7)	83.2	(1.9)	(0.3)	21.8	(8.5)	(4.1)	(0.9)
Minority interests	-	-	-	-	-	-	-	-	-
Net profit	16.3	(15.2)	0.5	(493.3)	(60.5)	16.3	(52.0)	5.4	(46.2)
Core net profit	16.3	(15.2)	0.5	(10.0)	(60.5)	(81.9)	(55.3)	12.0	(46.2)
EPS (sen)	0.2	(0.2)	0.0	(6.0)	(0.7)	0.2	(0.6)	0.1	(0.6)
Core EPS (sen)	0.2	(0.2)	0.0	(0.1)	(0.7)	(1.0)	(0.7)	0.1	(0.6)
Breakdown of exceptionals	-	-	-	(483.3)	-	98.2	3.2	(6.5)	-
- Gain/(loss) on disposal of PPE	-	-	-	-	-	-	-	-	-
- PPE written off	-	-	-	(22.7)	-	-	-	-	-
- Impairment of PPE	-	-	-	(460.6)	-	(460.5)	(3.8)	(1.7)	-
- Others	-	-	-	-	-	558.7	7.0	(4.9)	-

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 12: Revenue metrics

	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22
Revenue (RM m)	176.3	140.9	130.7	99.1	43.9	83.6	91.5	158.5	77.4
- Drilling services	174.2	137.9	127.8	95.7	40.8	80.2	87.2	151.0	74.2
- Oilfield services	1.8	3.0	2.7	3.0	3.0	2.9	4.1	7.1	2.3
- Others	0.2	0.1	0.2	0.4	0.2	0.4	0.2	0.4	0.6
Number of rigs	7	7	7	7	7	6	6	6	6
Number of HWUs	4	4	4	4	4	4	4	4	4
Drilling calendar days	630	637	644	644	630	576	552	552	540
Days employed	529	427	386	322	176	219	282	431	211
Utilisation rate	84.0%	67.0%	60.0%	50.0%	28.0%	38.0%	51.0%	78.0%	39.0%
Charter rates (US\$/day)	71,000	72,000	72,000	66,000	53,000	77,396	74,926	74,222	75,319

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 13: Cost metrics and operating profit

	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22
Drilling costs (RM m)	129.4	128.8	100.8	96.2	79.5	137.9	115.1	128.7	105.3
- Cash operating costs	68.7	69.6	50.1	47.3	38.4	99.0	77.8	89.5	69.8
- Depreciation	60.7	59.2	50.7	48.9	41.1	38.9	37.4	39.1	35.5
Drilling EBIT (RM m)	44.9	9.1	27.0	(0.5)	(38.7)	(57.6)	(27.9)	22.4	(31.1)
EBIT margin (%)	25.8%	6.6%	21.1%	-0.5%	-94.9%	-71.8%	-32.0%	14.8%	-42.0%

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 14: Segmental profit after tax

	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22
Profit after tax (RM m)	16.3	(15.2)	0.5	(493.3)	(58.6)	16.3	(52.0)	5.4	(44.1)
- Drilling services	25.5	(8.6)	12.0	(484.3)	(49.0)	25.8	(41.4)	15.0	(36.3)
- Oilfield services	(2.4)	(0.9)	(1.0)	(0.9)	0.5	(3.0)	(1.8)	(1.5)	0.3
- Others	(6.8)	(5.7)	(10.6)	(8.1)	(10.1)	(6.6)	(8.9)	(8.0)	(8.1)

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS



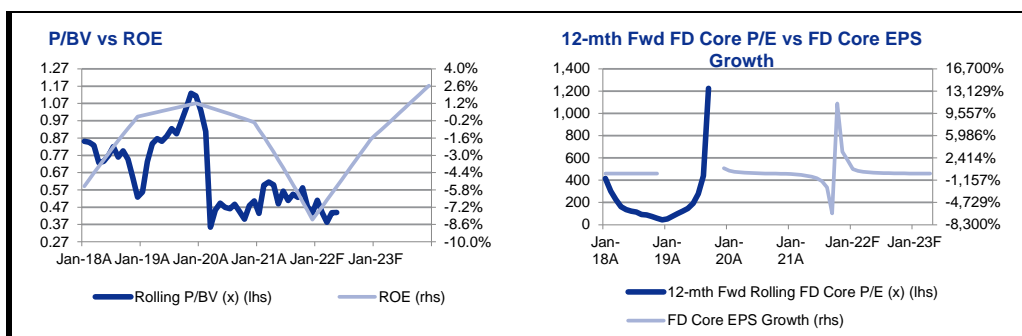
ESG in a nutshell

Velesto has been included in Bursa Malaysia's FTSE4Good Index since 2019, and was given a 4-star ESG ranking by Bursa Malaysia and FTSE Russell, with an overall rating of 3.1 (out of a full score of 5.0), principally on the strength of its Governance rating (Environmental rating of 2.0; Social 3.0; Governance 4.7). Nevertheless, Velesto has its work cut out for it, especially on the Environmental front, where it has been rated lowly by FTSE Russell. Velesto has not set any carbon emission targets, nor does it have any renewable energy assets that can help generate carbon offsets. It also does not yet have a plan of action or roadmap to reduce the carbon emissions from its operations. We look forward to further disclosures and developments in this area.

<p>Keep your eye on</p> <p>One of Velesto's seven JU rigs, the Naga 7, sank offshore Sarawak on 3 May 2021 while positioning itself on the seabed in preparation to drill. Fortunately, this incident did not result in loss of life, and all crew members were evacuated safely.</p>	<p>Implications</p> <p>No element of blame or responsibility has been attributed to Velesto, and it has been successful in its insurance claims. Velesto has also not lost potential drilling jobs because of the sinking incident.</p>
<p>ESG highlights</p> <p>Velesto disclosed that its operations emitted 62,860 tonnes of CO₂-equivalent (CO₂-e) Scope 1 and Scope 2 emissions in 2020, which was 11% lower yoy. However, when juxtaposed against the 20% fall in rig employment days, with emissions per day of rig employment rose 11% yoy in 2020. The emissions per drilling day metric rose because 35% of available rig days were unemployed in 2020 (vs. just 20% in 2019). The fall in rig utilisation negatively affects the emissions per drilling day metric, as the unemployed rigs are kept on hot layup while waiting for work, and so diesel consumption continues.</p> <p>However, Velesto's emissions track record in 2019 was not favourable either. CO₂-e emissions rose 17% yoy in 2019, which outpaced the 11% rise in rig employment days, resulting in a 5% rise in emissions per drilling day.</p>	<p>Implications</p> <p>Velesto has not yet established any short- or long-term targets for emissions reduction. Any emissions reduction measures will have to address the volume of diesel consumed by its drilling rigs, which are driven by five diesel-powered generators on each rig.</p> <p>Each rig has a rig power management system (RPMS) that is able to detect when the rig equipment requires a lower power load and, with that, automatically shuts down or revs the engine(s) down. This enables more efficient use of energy for drilling activities. Velesto did not disclose if it is exploring additional measures to increase fuel efficiency.</p> <p>However, Velesto did mention in its 2020 Sustainability Report that it will explore the use of lower-carbon fuels. We presume that Velesto is referring to the B7 biodiesel blend (containing 7% palm oil methyl ester) that has been mandated by the Malaysian government for use in industry since Jul 2019.</p>
<p>Trends</p> <p>We expect fossil fuel consumption in Asia to continue growing in the 2020s and into the 2030s, but may plateau and slowly decline from the 2040s onwards as a result of the gathering pace of energy transition. This raises the issue of whether Velesto's existing JU drilling rigs will be obsolete, and also if Velesto will be able to thrive in the post-fossil fuel era.</p>	<p>Implications</p> <p>Assuming 30-year JU useful lives, Velesto's oldest JU (the Naga 2) will reach the end of its useful life in 2039F, while its youngest JU (the Naga 8) will reach the end of its useful life in 2045F. As such, we do not expect that Velesto's existing assets will face issues of obsolescence in the foreseeable future. However, we are unsure if Velesto will have the financial capacity to future-proof itself and reinvent itself in light of the energy transition.</p>

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

(RMm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Net Revenues	546.9	377.5	420.1	519.0	509.8
Gross Profit	273.4	14.5	135.8	235.5	237.0
Operating EBITDA	273.4	14.5	135.8	235.5	237.0
Depreciation And Amortisation	(220.0)	(157.0)	(147.5)	(142.9)	(142.5)
Operating EBIT	53.4	(142.5)	(11.6)	92.5	94.5
Financial Income/(Expense)	(57.5)	(39.0)	(30.1)	(26.9)	(23.3)
Pretax Income/(Loss) from Assoc.	0.2	0.2	0.5	0.5	0.5
Non-Operating Income/(Expense)	10.1	4.3	3.0	3.0	3.0
Profit Before Tax (pre-EI)	6.3	(177.1)	(38.3)	69.1	74.7
Exceptional Items	(483.3)	94.9	0.0	0.0	0.0
Pre-tax Profit	(477.0)	(82.2)	(38.3)	69.1	74.7
Taxation	(14.8)	(8.6)	(0.1)	(9.4)	(10.2)
Exceptional Income - post-tax					
Profit After Tax	(491.7)	(90.8)	(38.4)	59.7	64.5
Minority Interests	0.0	0.0	0.0	0.0	0.0
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	(491.7)	(90.8)	(38.4)	59.7	64.5
Recurring Net Profit	(8.5)	(185.7)	(38.4)	59.7	64.5
Fully Diluted Recurring Net Profit	(8.5)	(185.7)	(38.4)	59.7	64.5

Cash Flow

(RMm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
EBITDA	273.4	14.5	135.8	235.5	237.0
Cash Flow from Inv. & Assoc.					
Change In Working Capital	73.4	(33.4)	(3.0)	(46.4)	6.7
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	756.2	103.8	150.6	142.4	142.0
Other Operating Cashflow	(692.9)	(57.7)	(144.0)	(139.4)	(139.0)
Net Interest (Paid)/Received	(51.0)	(33.1)	(30.1)	(26.9)	(23.3)
Tax Paid	(12.3)	(20.6)	(0.1)	(9.4)	(10.2)
Cashflow From Operations	346.7	(26.5)	109.2	155.8	213.1
Capex	(55.3)	(82.1)	(45.2)	(75.3)	(135.5)
Disposals Of FAs/subsidiaries	0.1	78.3	0.0	0.0	0.0
Acq. Of Subsidiaries/investments	0.0	0.0	0.0	0.0	0.0
Other Investing Cashflow	26.5	561.8	0.0	0.0	0.0
Cash Flow From Investing	(28.7)	558.1	(45.2)	(75.3)	(135.5)
Debt Raised/(repaid)	(239.5)	(518.4)	(102.5)	(43.4)	(64.9)
Proceeds From Issue Of Shares	0.0	0.0	0.0	0.0	0.0
Shares Repurchased					
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Preferred Dividends					
Other Financing Cashflow					
Cash Flow From Financing	(239.5)	(518.4)	(102.5)	(43.4)	(64.9)
Total Cash Generated	78.5	13.2	(38.4)	37.1	12.7
Free Cashflow To Equity	78.5	13.2	(38.4)	37.1	12.7
Free Cashflow To Firm	375.9	566.9	95.6	108.8	102.4

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS... cont'd

Balance Sheet

(RMm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Cash And Equivalents	359	294	255	292	305
Total Debtors	145	178	198	244	240
Inventories	202	174	136	136	130
Total Other Current Assets	21	56	56	56	56
Total Current Assets	727	700	644	728	731
Fixed Assets	2,726	2,303	2,201	2,133	2,126
Total Investments	2	1	2	2	3
Intangible Assets	0	0	0	0	0
Total Other Non-Current Assets	0	0	0	0	0
Total Non-current Assets	2,728	2,304	2,202	2,135	2,129
Short-term Debt	183	280	47	69	95
Current Portion of Long-Term Debt					
Total Creditors	94	95	74	74	71
Other Current Liabilities	31	64	64	64	64
Total Current Liabilities	307	439	185	207	230
Total Long-term Debt	871	302	432	367	277
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	6	6	0	0	0
Total Non-current Liabilities	877	308	432	367	277
Total Provisions	0	0	0	0	0
Total Liabilities	1,184	746	618	574	506
Shareholders' Equity	2,270	2,258	2,229	2,289	2,353
Minority Interests	1	0	0	0	0
Total Equity	2,271	2,258	2,229	2,289	2,353

Key Ratios

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue Growth	(18.5%)	(31.0%)	11.3%	23.6%	(1.8%)
Operating EBITDA Growth	(12%)	(95%)	838%	73%	1%
Operating EBITDA Margin	50.0%	3.8%	32.3%	45.4%	46.5%
Net Cash Per Share (RM)	(0.085)	(0.035)	(0.027)	(0.018)	(0.008)
BVPS (RM)	0.28	0.27	0.27	0.28	0.29
Gross Interest Cover	0.83	-3.58	-0.37	3.27	3.81
Effective Tax Rate	0.0%	0.0%	0.0%	13.6%	13.7%
Net Dividend Payout Ratio	NA	NA	NA	NA	NA
Accounts Receivables Days	142.8	156.2	163.0	155.3	173.7
Inventory Days	260.5	188.8	198.6	174.7	178.4
Accounts Payables Days	142.2	94.9	108.6	95.5	97.5
ROIC (%)	1.07%	(3.60%)	(0.34%)	2.83%	2.92%
ROCE (%)	1.63%	(4.60%)	(0.37%)	3.46%	3.52%
Return On Average Assets	0.90%	(4.84%)	(0.54%)	2.80%	2.86%

Key Drivers

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Number of drilling rigs	7.0	6.0	6.0	6.0	6.0
Utilisation rate (%)	66.0%	0.0%	57.0%	70.0%	70.0%
Average daily charter rate (US\$/day)	71,207.3	72,305.1	74,261.5	74,857.1	72,712.3

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

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Score Range:	90 - 100	80 – 89	70 - 79	Below 70	No Survey Result
Description:	Excellent	Very Good	Good	N/A	N/A

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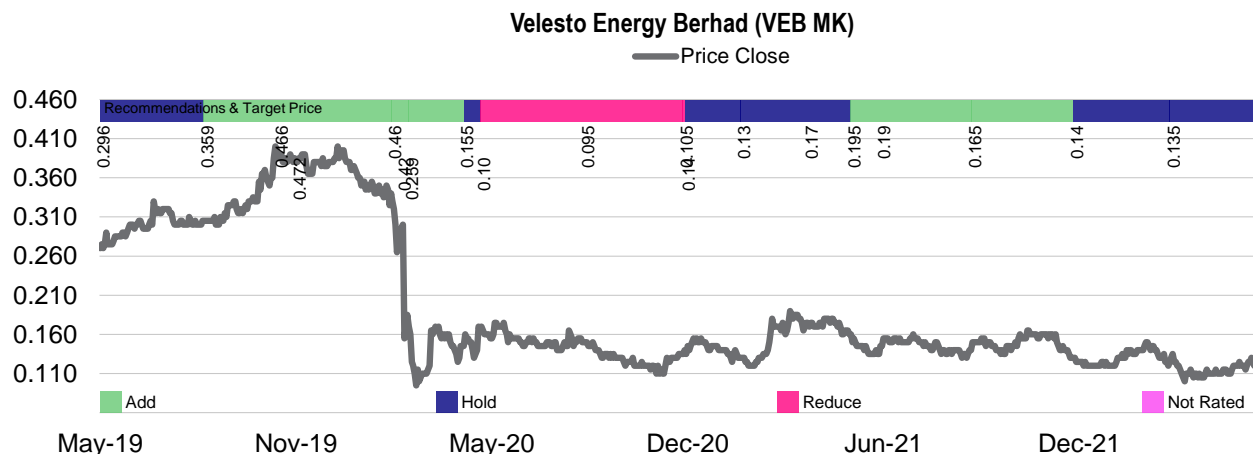
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Distribution of stock ratings and investment banking clients for quarter ended on 31 March 2022		
632 companies under coverage for quarter ended on 31 March 2022		
	Rating Distribution (%)	Investment Banking clients (%)
Add	70.3%	0.8%
Hold	22.0%	0.0%
Reduce	7.8%	0.2%

Spitzer Chart for stock being researched (2 year data)



Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2021, Anti-Corruption 2021

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** – Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a, **BH** – Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** – Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** – Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** – Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** – Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** – Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Excellent, n/a, **HANA** – Excellent, Certified, **HMPRO** – Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** – Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** – Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** – Excellent, Certified, **KCE** – Excellent, Certified, **KEX** – Very Good, Declared, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** – Excellent, Certified, **KTC** – Excellent, Certified, **LH** – Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** – Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** – Excellent, Certified, **PTTEP** – Excellent, n/a, **PTTGC** – Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** – Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** – Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** – Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified, **TISCO** – Excellent, Certified, **TKN** – Very Good, n/a, **TOP** – Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2021 from Thai Institute of Directors Association (IOD)

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Recommendation Framework	
Stock Ratings	Definition:
Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.
<i>The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.</i>	
Sector Ratings	Definition:
Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.
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Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.