COMPANY UPDATE

Uzma (UZMA MK)

Expecting Better Outlook For O&G Maintenance

With a strong financial start in 1QFY23, Uzma is guiding for better contract demand in 2023, especially for certain maintenance works (decommissioning) and green solutions. Uzma's O&G earnings delivery remains crucial for the share price to recover sustainably from its all-time low, which has factored in solar project risks, especially on material costs vs returns. We revise our forecasts, with more optimism on 2023 earnings. Maintain BUY with an adjusted target price of RM0.67.

WHAT'S NEW

- **Uzma had strong 1QFY23 core earnings of RM12m and EBITDA of RM34m** (4QFY22: RM31m; 1QFY22: RM24m). Production solutions (PS) segment saw new revenues of close to RM20m for a new commodity urea/ammonia. Amid energy security, Uzma expects more urea shipments to be locked in from the spot markets, though it earns a small volume-based trading margin and is not exposed to the underlying price volatility. This offset lower qoq well services (WS) revenue, as some hydraulic workover units (HWU) transitioned to new contracts. Coiled tubing (CT) picked up in recent quarters, after experiencing delayed start-up in 3QFY22, which impacted subsidiary Setegap Ventures' (SVP) revenue in FY22 at only RM108m, vs RM120m-150m historically.
- **Uzma saw higher O&G bidbook, reflecting higher client demand** for certain local maintenance works. For example, there are tenders for up to three years for plug & abandonment (P&A), a decommissioning activity that theoretically should increase along with the ESG push, and made more viable when oil prices are high. Uzma was successful in the two-well P&A for Tanjung Baram, and had done >25 P&A wells over the years, and plans to offer up to six of its HWU for the tender. The cost to P&A one well can be about RM2m (including marine services), but on average, HWU rates had increased by about 30%, as the workover market is also getting tighter correlating to the jackup rig market, where rates had almost doubled, although Uzma opines this merely offsets opex increases. Locally, only Uzma and Velesto Energy are the larger local HWU owners.
- **Secured second extension of water injection facility (WIF)** by another five years until Oct 27**.** The WIF named MARSYA started its five-year firm contract of RM0.4b for Petronas in Oct 16, at the D18 field in offshore Sarawak, and was extended for another year until Oct 22. MARSYA, with a capex of US$70m, houses three pumps of 66k bpd of water injection each, and it has been operating at 100% uptime (including monsoon season). Hence, this unique solution to help boost O&G production is being positively recognised by the client. Although the extension value is unknown, gross and net profits should be almost similar at RM24m/RM12m each.

KEY FINANCIALS

Year to 30 Jun (RMm)	2021	2022	2023F	2024F	2025F
Net turnover	389	378	436	594	581
EBITDA	73	85	108	122	130
Operating profit	21	34	59	74	83
Net profit (rep./act.)	(8)	5	22	28	31
Net profit (adj.)	(6)	16	25	28	31
EPS (sen)	(1.8)	4.7	7.0	7.9	8.8
PE (x)	n.m.	11.5	7.7	6.7	6.1
P/B (x)	0.4	0.4	0.4	0.4	0.4
EV/EBITDA (x)	7.9	6.7	5.3	4.7	4.4
Dividend yield (%)	0.0	0.0	0.0	1.9	3.7
Net margin (%)	(2.0)	1.3	5.0	4.7	5.3
Net debt/(cash) to equity (%)	82.9	72.1	58.8	66.3	61.4
Interest cover (x)	2.9	4.2	4.1	4.4	4.3
ROE (%)	n.a.	1.0	4.3	5.3	5.6
Consensus net profit	-	-	18	21	21
UOBKH/Consensus (x)	-	-	1.36	1.30	1.50

Source: Uzma, Bloomberg, UOB Kay Hian
n.m. : not meaningful; negative P/E, EV/EBITDA reflected as "n.m."

BUY
(Maintained)

Share Price	RM0.54
Target Price	RM0.67
Upside	+25.0%
(Previous TP	*RM0.60)*

COMPANY DESCRIPTION

Uzma is an oil & gas company that provides integrated reservoir services to upstream players. Its three main businesses are: a) geoscience and petroleum engineering services, b) drilling and well services, and c) project oilfield and operation services.

STOCK DATA

GICS sector	Energy
Bloomberg ticker:	UZMA MK
Shares issued (m):	352.0
Market cap (RMm):	188.3
Market cap (US$m):	42.9
3-mth avg daily t'over (US$m):	0.2

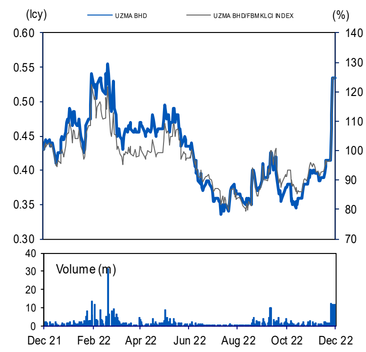
Price Performance (%)

52-week high/low RM0.555/RM0.335

1mth	3mth	6mth	1yr	YTD
37.2	42.7	23.0	24.4	20.2

Major Shareholders	%
Tenggiri Tuah	34.4
FY23 NAV/Share (RM)	1.35
FY23 Net Debt/Share (RM)	0.86

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- **No major new capex for D18…** as this is a business-as-usual contract, and MARSYA is usually required to provide 50% of its nominal water injection capacity (ie two pumps working with one on standby). The design life is 10 years, but this is just a certification issue by the relevant agencies, and Uzma guided it can be extended easily for at least two more years after every test, without the need to dry dock for modification. We believe the outstanding loan related to D18, including those of the Sukuk Wakalah issued in 2018, is roughly similar vs the last disclosure of RM140m in FY20.
- **…except for potential green solutions.** Petronas has committed to zero continuous venting (ie releases of methane gas into the air) by 2024 and zero flaring (ie burning unnecessary gases) by 2030. We expect Petronas to accelerate its review of local production fields, especially those of high gas-to-oil ratio like D18, to be ready for the 2024 ESG policy. We understand from channel checks that some fields may require additional platforms to recover vented/flared gas. However, it is not clear what Petronas' demand is in 2023 horizon, and there is a scarcity of O&G players with this expertise. The gases can either be reused to generate power for the platforms or sold as volumes. Given that this green capex is not small, the latter will only be viable with tie-in solutions to other gas productions and gas prices have to remain high for the volume to be economical enough to be sold.
- **A bumpy ride to reach long-term solar targets.** Solar is expected to drive non-O&G diversification, with potential revenue targets to hit RM0.5b in the near term (by 2025), and long-term revenue base of >RM1b (beyond 2030), assuming >1.5GW of operated renewable capacities. This is positive on ESG, as very few O&G players have laid out such roadmaps. However, the ride continues to be bumpy, with solar panels having increased by at least 30% vs the time when the Large Solar Scale4 (LSS4), which means the overall project costs have surged by at least 20%. Uzma remains focused to offset these risks via engineering optimisation, and still targets high single-digit IRR.
- **Associate Rockwash Geodata (24% stake) not expected to be an ESG concern.** The UK company was acquired in 2015 for 30% stake, and it specialises in analysing rock samples for geological works. Uzma's cost of investment as of FY22 is about RM4.4m. Despite being an associate, Rockwash's earnings is considered substantial to the group's, at RM2m associate profit for FY22/FY21 each. We understand the geology revenue base will be sustainable in the mid-term, but opine there is a real risk of long-term revenue decline as the world is transitioning out of fossil fuels. But this is not an ESG concern in our view as Uzma had pared down their stake to 24% in 2022 for RM0.9m, and it intends to further dispose the associate if a right price offer comes along.

EARNINGS REVISION/RISK

- **Adjust 2023F-25F earnings by +17%/-7%/-7%.** The overall downward adjustment in the forecast years is to reflect updates from the Annual Report, in which we also restated downwards the core earnings for FY21/FY22, and also lowered non-O&G revenue forecasts. 2023F earnings reflect a bullish O&G outlook for 2023, even if 2QFY23 is expected to be a weak quarter due to the monsoon season, which came slightly earlier for East Malaysia this year due to the typhoon events that hit Taiwan and Philippines.

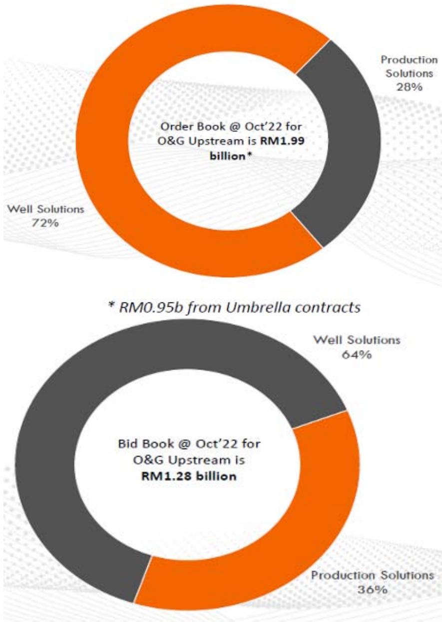
VALUATION/RECOMMENDATION

- **Maintain BUY with an adjusted target price of RM0.67 (from RM0.60),** based on an unchanged valuation of 10x FY23F PE. Although Uzma remains highly dependent on Petronas' work orders, and there may be O&G contract momentum in 2023, earnings delivery will still be its most crucial earning rerating factor, in order for the share price to sustainably rise from close to its five-year low of RM0.40. We believe the stock remains discounted relative to historical average due to investor concerns on the LSS4, and hence it can be attractive for investors who are taking a longer term view and prepared for the near-term volatilities.

ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG) UPDATES

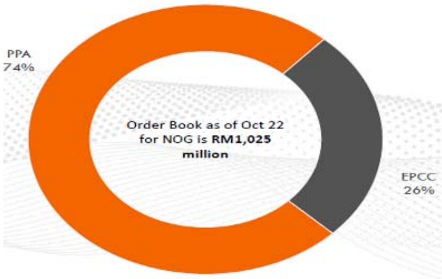
• **Environmental**
- **Carbon (CO_2) reduction.** Uzma is in the midst of formulating emissions disclosure, and is clearly serious on net-zero carbon targets in line with the below point. - **Clear non-O&G diversification roadmap.** Non-O&G targeted to be 40% of revenue mix by FY25. Long-term target revenue generation from solar at >RM1b beyond 2030.
• **Social**
- **Diversity.** >20% female proportion among 880 staff force (as per FY21 report). - **Safety (HSE).** Lost Time Injury Frequency (LTIF) remains low at almost 0.
• **Governance**
- **5 out of 8 board members are independent,** with wide industry expertise.

O&G ORDERBOOK AND BIDBOOK, OCT 22



Source: Uzma, UOB Kay Hian.

NON-O&G (NOG) ORDERBOOK, OCT 22



Source: Uzma Note: PPA: Power Purchase Agreement; EPCC: Engineering, Procurement, Construction and Commissioning

REVENUE BY SEGMENT (RM MILLION)

Source: Uzma Note: IWS: Well Solutions; PS: Production Solutions

SEGMENTAL FORECASTS

RMm	FY23F	FY24F	FY25F
Group revenue	435.7	593.6	581.1
- Services	308.8	364.2	396.7
- Trading	56.9	59.4	64.4
- Setegap (85%)	123.8	123.8	123.8
- Non-O&G	70.0	170.0	120.0
EBIT	58.7	73.6	82.6
- Services	25.0	41.4	49.3
- Trading	7.0	7.5	8.5
- Setegap (85%)	26.7	24.8	24.8
- Non-O&G	4.2	8.5	6.0
EBIT margins (%)	13.5%	12.4%	14.2%
- Services (%)	8.1%	11.4%	12.4%
- Trading (%)	12.3%	12.6%	13.2%
- Setegap (%)	21.5%	20.0%	20.0%
- Non-O&G y	6.0%	5.0%	5.0%
FCF	27.9	(48.6)	12.5

Source: UOB Kay Hian

PROFIT & LOSS

Year to 30 Jun (RMm)	2022	2023F	2024F	2025F
Net turnover	378	436	594	581
EBITDA	85	108	122	130
Deprec. & amort.	52	50	48	47
EBIT	34	59	74	83
Total other non-operating income	14	n.a.	n.a.	n.a.
Associate contributions	1	1	1	1
Net interest income/(expense)	(20)	(26)	(28)	(31)
Pre-tax profit	17	31	47	53
Tax	(10)	(8)	(12)	(14)
Minorities	(2)	(2)	(7)	(8)
Net profit	5	22	28	31
Net profit (adj.)	16	25	28	31

BALANCE SHEET

Year to 30 Jun (RMm)	2022	2023F	2024F	2025F
Fixed assets	521	513	513	518
Other LT assets	229	221	214	196
Cash/ST investment	111	152	130	174
Other current assets	400	397	566	579
Total assets	1,260	1,283	1,422	1,467
ST debt	220	225	274	319
Other current liabilities	223	237	322	315
LT debt	247	230	214	201
Other LT liabilities	45	45	45	45
Shareholders' equity	495	517	541	565
Minority interest	30	29	25	21
Total liabilities & equity	1,260	1,283	1,422	1,467

CASH FLOW

Year to 30 Jun (RMm)	2022	2023F	2024F	2025F
Operating	51	72	0	66
Pre-tax profit	17	31	47	53
Tax	(10)	(8)	(12)	(14)
Deprec. & amort.	52	50	48	47
Working capital changes	(23)	(1)	(83)	(20)
Other operating cashflows	16	0	0	0
Investing	(19)	(44)	(49)	(54)
Capex (growth)	(22)	(44)	(49)	(54)
Investments	0	0	0	0
Proceeds from sale of assets	0	0	0	0
Others	4	0	0	0
Financing	(64)	20	24	28
Dividend payments	(5)	(5)	(5)	(5)
Issue of shares	27	0	0	0
Proceeds from borrowings	1	86	89	93
Loan repayment	(81)	(60)	(60)	(60)
Others/interest paid	(5)	0	0	0
Net cash inflow (outflow)	(31)	48	(25)	40
Beginning cash & cash equivalent	91	62	112	90
Changes due to forex impact	51	42	43	44
Ending cash & cash equivalent	111	152	130	174

KEY METRICS

Year to 30 Jun (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	22.6	24.9	20.5	22.4
Pre-tax margin	4.5	7.1	8.0	9.2
Net margin	1.3	5.0	4.7	5.3
ROA	0.4	1.7	2.1	2.1
ROE	1.0	4.3	5.3	5.6
Growth				
Turnover	(2.8)	15.3	36.2	(2.1)
EBITDA	16.8	26.9	12.5	6.7
Pre-tax profit	n.a.	81.7	52.9	12.8
Net profit	n.a.	327.5	29.5	10.9
Net profit (adj.)	n.a.	49.6	13.8	10.9
EPS	n.a.	49.6	13.8	10.9
Leverage				
Debt to total capital	47.1	45.5	46.3	47.0
Debt to equity	94.4	88.1	90.2	92.1
Net debt/(cash) to equity	72.1	58.8	66.3	61.4
Interest cover (x)	4.2	4.1	4.4	4.3

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