

13 July 2023

Energy & Petrochemicals | Energy

Petrosea (PTRO IJ)

Not Rated

Staying Afloat On Sound Fundamentals

- **IDR4,710 FV (30% upside) based on medium-term DCF calculations, c.7x FY24F target P/E (5x currently).** Petrosea's new coal venture could provide fair support to future revenues in addition to its stable coal mining contracting business. PTRO is projected to notch positive net earnings growth (management's target: 10-12% YoY for FY23 and NPMs stabilising at c.9%) against the normalising coal price trend downside. The latter is the main reason for the stock's negative movements. We also expect better operations ahead due to the drier weather season in the latter half of 2023.
- **New coal mining venture to improve future topline.** PTRO recently completed a USD90.5m transaction to acquire a coal mine asset in East Kalimantan (calorific value: c.4,200kcal/kg). The initial production is targeted at 750k tonnes and will gradually increase up to 5m tonnes pa by 2025-2026. Management said the estimated costs for mining operations are fairly low – the stripping ratio is at c.3x. We think this opportunity will provide substantial support for PTRO's topline going forward.
- **Mining contracting remains its backbone,** in our view, despite the inevitable challenges from normalising coal prices, as the company's mining fees are closely pegged to coal benchmark price changes (c.USD2.70/bcm currently). However, we still see the potential for an increase in the overburden (OB) removal target (FY22: 124m bcm), which will alleviate the negativity of lower fees. We hold the view that most coal companies are still thriving to increase their coal outputs for a couple more years ahead – hence, demand for mining services remains high. Moreover, PTRO is seeking more opportunities to provide services – not only for coal mining, but also other minerals too, eg gold, bauxite, and nickel.
- **Engineering services to provide support for mining contracting.** PTRO's initiative to engage in mining mineral services will be supported by its EPC division. PTRO's expertise in engineering solutions will add a trickledown effect to the mining contracting business, in our view. Once the preliminary infrastructure has been set up its EPC wing, ore extraction will be undertaken by the company's mining contractor. One of the highlights of PTRO's venture into the EPC segment was the involvement of Freeport Indonesia's pre-crusher construction services.
- **Valuation.** We plot moderate assumptions on PTRO's continuing operational profits (Figure 1), which includes scenarios of gradual decreases in mining contracting fees (at c.USD2/bcm) but with expansions in OB removal targets instead (+2% YoY pa), normalised coal sales ASPs (at c.USD55/tonne) vis-à-vis additional output (5m tonnes by 2026), and steady profit growth from the EPC wing. Our back-of-envelope view also matches with management's target to book 10-13% YoY net earnings growth for 2023, which justifies its current still-below-industry multiples (P/E) that is quite attractive (Figure 2). PTRO also regularly distributes dividends (at a 10-year average yield of 6%) and has a manageable balance sheet (1Q23 net gearing: 0.1x).

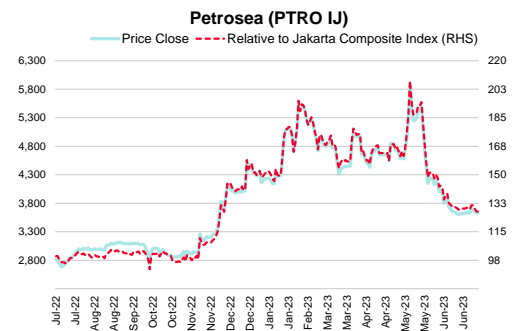
Target Price (Return):	IDR4,710 (30%)
Price:	IDR3,630
Market Cap:	USD242m
Avg Daily Turnover (IDR/USD)	6,968m/0.47m

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(16.2)	(9.3)	(22.8)	(14.4)	28.7
Relative	(15.6)	(10.6)	(22.9)	(17.1)	27.4
52-wk Price low/high (IDR)	2,690 – 5,850				



Source: Bloomberg

Forecasts and Valuation	Dec-20	Dec-21	Dec-22
Total turnover (USDm)	341	416	476
Recurring net profit (USDm)	33	34	41
Recurring net profit growth (%)	4.0	4.5	21.1
Recurring P/E (x)	7.39	7.07	5.84
P/B (x)	1.0	0.9	0.8
P/CF (x)	32.57	3.02	5.39
Dividend Yield (%)	2.9	3.3	31.0
EV/EBITDA (x)	19.36	3.13	3.97
Return on average equity (%)	14.8	13.9	14.9
Net debt to equity (%)	29.4	17.9	18.1

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

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Financial Exhibits

Asia	Financial summary (USD)	Dec-20	Dec-21	Dec-22
Indonesia	Recurring EPS	0.03	0.03	0.04
Energy & Petrochemicals	DPS	0.01	0.01	0.07
Petrosea	BVPS	0.23	0.26	0.29
PTRO IJ	Return on average equity (%)	14.8	13.9	14.9
Not Rated				
	Valuation metrics	Dec-20	Dec-21	Dec-22
	Recurring P/E (x)	7.39	7.07	5.84
	P/B (x)	1.0	0.9	0.8
	FCF Yield (%)	49.8	14.4	11.4
	Dividend Yield (%)	2.9	3.3	31.0
	EV/EBITDA (x)	19.36	3.13	3.97
	EV/EBIT (x)	6.50	6.45	4.86
	Income statement (USDm)	Dec-20	Dec-21	Dec-22
	Total turnover	341	416	476
	Gross profit	75	75	95
	EBITDA	16	92	75
	Depreciation and amortisation	32	(48)	(14)
	Operating profit	48	45	61
	Net interest	(7)	(3)	(6)
	Pre-tax profit	36	41	50
	Taxation	(3)	(7)	(9)
	Reported net profit	33	34	41
	Recurring net profit	33	34	41
	Cash flow (USDm)	Dec-20	Dec-21	Dec-22
	Change in working capital	14	6	(0)
	Cash flow from operations	7	80	45
	Capex	113	(45)	(17)
	Cash flow from investing activities	113	(45)	(17)
	Dividends paid	(7)	(8)	(75)
	Cash flow from financing activities	(35)	(148)	(48)
	Cash at beginning of period	84	134	89
	Net change in cash	85	(113)	(21)
	Ending balance cash	134	89	62
	Balance sheet (USDm)	Dec-20	Dec-21	Dec-22
	Total cash and equivalents	134	89	62
	Tangible fixed assets	231	229	233
	Total assets	530	533	596
	Short-term debt	79	64	71
	Total long-term debt	123	72	44
	Total liabilities	298	273	298
	Total equity	231	260	298
	Total liabilities & equity	530	533	596
	Key metrics	Dec-20	Dec-21	Dec-22
	Revenue growth (%)	(28.5)	22.0	14.6
	Recurrent EPS growth (%)	4.0	4.5	21.1
	Gross margin (%)	22.0	17.9	20.0
	Operating EBITDA margin (%)	4.7	22.2	15.7
	Net profit margin (%)	9.6	8.2	8.7
	Dividend payout ratio (%)	21.4	23.4	181.1
	Capex/sales (%)	(33.1)	10.9	3.6
	Interest cover (x)	4.90	8.03	8.21

Source: Company data, RHB

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Figure 1: DCF calculation

(USDm)	2023F	2024F	2025F	2026F	2027F	2028F	2029F	2030F
EBIT	86	93	115	128	130	133	136	139
Tax on EBIT	(22)	(23)	(29)	(32)	(33)	(33)	(34)	(35)
Depreciation and amortisation	21	22	22	25	27	30	32	35
Capital expenditures	(43)	(21)	(21)	(92)	(72)	(79)	(86)	(94)
Changes in net working capital	(42)	(2)	(12)	(12)	(2)	(2)	(2)	(2)
FCF	1	69	76	17	51	49	46	43
Terminal value								449
PV FCF	1	63	63	13	36	31	27	260
Enterprise value	493							
Cash at end-FY23	23							
Debt at end-FY23	181							
Equity value (USD)	334							
o/s shares (m units)	1,008							
DCF/share (IDR; rounded up)	4,710							
Upside	30%							
Last price	3,630							

Note: *WACC at 9.5% with 0% terminal growth value

Note 2: Assumption on EBIT was based on our back-of-envelope observations of the company's existing business

Source: Company data, RHB

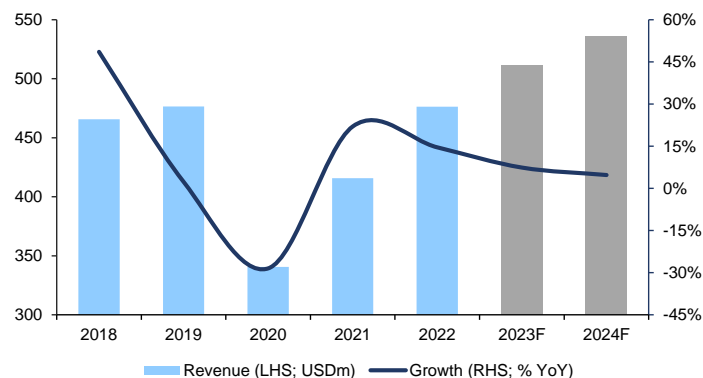
Figure 2: Peers comparison – coal and related players

Company	Price (IDR)	Target (IDR)	Market cap (IDRbn)	P/E (x)		EPS growth (%)		EV/EBITDA (x)		Div yield (%)		ROE (%)	
				FY23F	FY24F	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F
United Tractors	24,475	29,000	91,295	5.7	6.4	(24.2)	(10.3)	2.2	2.3	7.0	6.3	19.7	16.1
Adaro Energy	2,430	3,050	77,725	3.5	5.1	(35.0)	(31.6)	1.1	1.5	14.4	12.1	22.4	15.1
Bukit Asam	2,760	3,750	31,797	3.7	4.4	(31.6)	(16.8)	2.0	2.4	17.1	14.2	27.5	21.0
Harum Energy*	1,590	-	21,493	6.8	7.3	(28.0)	(8.0)	1.8	2.3	5.3	4.7	21.7	21.5
Bumi Resources*	128	-	47,529	9.6	10.3	(36.0)	(7.3)	13.0	16.5	0.0	0.0	11.9	11.9
Delta Dunia*	392	-	3,379	10.1	10.8	(21.0)	(6.4)	0.8	1.0	2.6	3.1	8.9	8.9
ABM Investama*	3,420	-	9,415	3.3	3.6	(27.5)	(8.7)	2.8	3.5	5.3	5.0	31.7	31.1
Indo Tambangraya	25,300	38,500	28,587	2.7	4.1	(38.4)	(34.0)	0.4	0.7	17.8	18.2	29.3	19.2
Petrosea	3,630	-	3,661	5.4	5.3	12.0	2.7	4.1	3.7	10.3	7.9	18.2	16.6
Astrindo	125	230	7,963	4.1	4.6	63,213.1	(10.8)	3.0	3.4	0.0	0.0	18.2	15.0
Simple avg.				5.5	6.2	(25.5)	(13.1)	3.1	3.7	8.0	7.1	21.0	17.6
Weighted avg.				5.3	6.2	(30.6)	(17.3)	3.4	4.1	9.4	8.3	21.2	16.7

Note: *Projection figures were taken from consensus

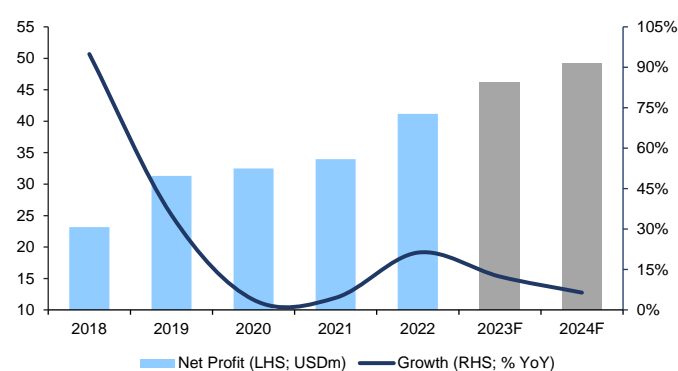
Source: Bloomberg, RHB

Figure 3: PTRO's revenue trends



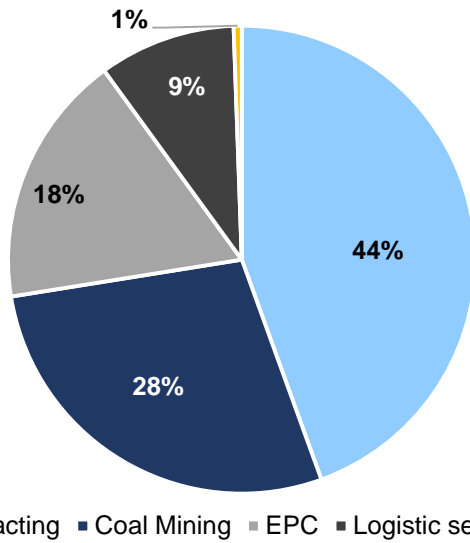
Source: Company data, RHB

Figure 4: PTRO's earnings trends



Source: Company data, RHB

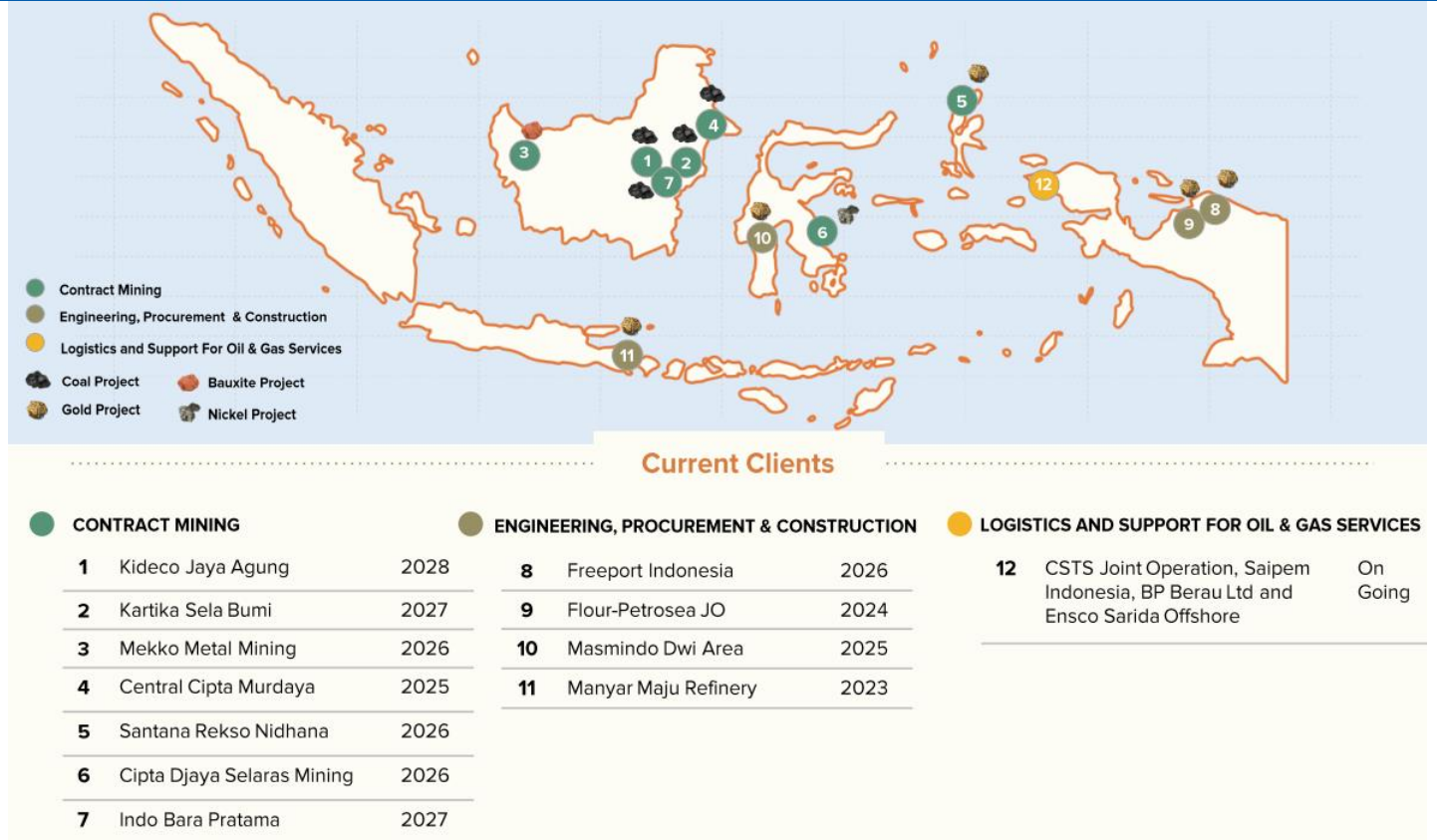
Figure 5: PTRO's future revenue contributions



◆ PTRO's revenue is still mostly reliant on developments in mining contracting, but additional topline contributions from coal sales (starting this year) will subside the proportion, in our view

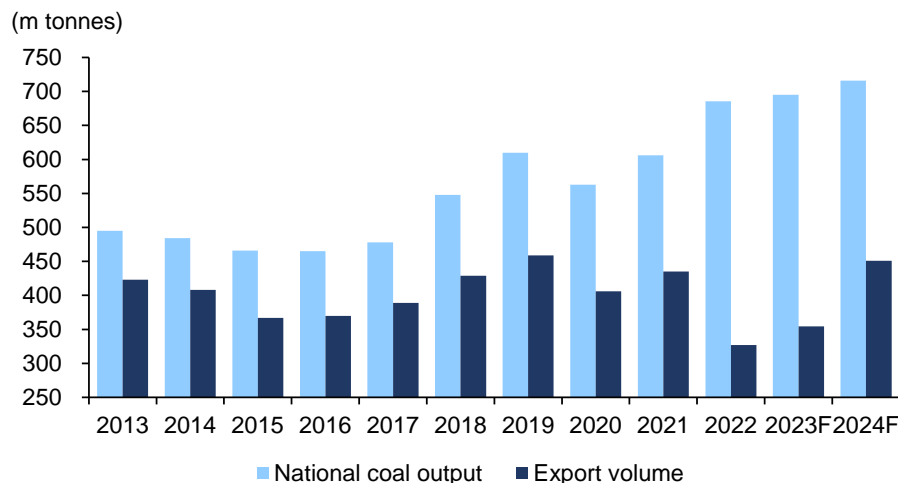
Source: Company data, RHB

Figure 6: PTRO's operational map and major clients



Source: Company data

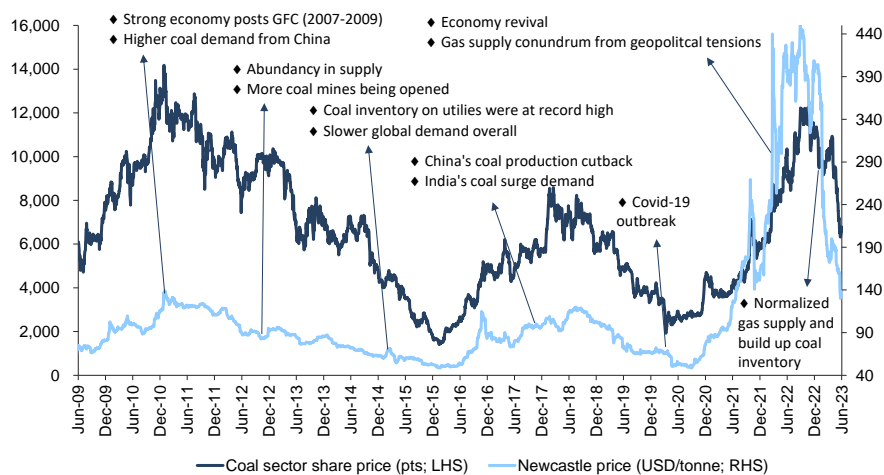
Figure 7: Indonesia's total coal output – coal is still the preferred fuel choice to generate power



- ◆ Given its large coal reserves, Indonesia is still focusing on coal production by ramping up domestic demand for electricity. It is also catering to the offshore market, eg Indonesian coal makes up c.60% of China's total coal imports
- ◆ Coal is still needed to generate power through conventional means, as the transition to renewable energy (RE) will take time. RE currently accounts for only c.14% of Indonesia's total power output

Source: Ministry of Energy and Mineral Resources, RHB

Figure 8: Newcastle benchmark price trends point to new turbulence in the cycle ahead, albeit for the short term. This would also determine the sensitivity of share prices ahead



- ◆ The volatility of coal prices is often related to weather changes and disruptions in energy supplies
- ◆ Despite the inevitable decline in the price of coal (from the apex of the current cycle), we expect the Newcastle Coal Futures price to average USD150 and USD90/tonne in 2023 and 2024. We estimate the price to be around USD75/tonne during the downtrend, although domestic coal producers should still chalk up decent margins

Source: Bloomberg, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-12-06	Not Rated	na	1,560

Source: RHB, Bloomberg

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