Deutsche Bank
Markets Research

Rating
Buy

Asia
China

Energy
Oil & Gas

Company
Sinopec Oilfield Service Alert

Reuters	Bloomberg	Exchange	Ticker
1033.HK	1033 HK	HKG	1033

Date
24 March 2015

Results

Price at 24 Mar 2015 (HKD)	3.07
Price target - 12mth (HKD)	2.78
52-week range (HKD)	3.97 - 1.55
HANG SENG INDEX	24,495

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Stock data

Market cap (HKDm)	39,324
Market cap (USDm)	5,070
Shares outstanding (m)	12,809.0
Major shareholders	Sinopec (42%)
Free float (%)	52
Avg daily value traded (USDm)	4.8

Source: Deutsche Bank

Key data

FYE 12/31	2013A	2014E	2015E
Sales (CNYm)	89,729	81,704	86,892
Net Profit (CNYm)	1,515.4	2,427.1	3,510.0
DB EPS (CNY)	0.12	0.19	0.25
PER (x)	9.3	13.0	10.0
Yield (net) (%)	0.0	0.5	4.0

Source: Deutsche Bank

FY14 results meets guidance on margin improvements

Bottom line up 60% yoy helped by margin expansion

SSC announced its first full year results post the restructuring with NPAT of RMB2.4bn, up 58% yoy, in line with DBe and consensus estimates. SSC's FY14 revenue (excl. its chemical fibre business which is to be spun off) declined by 12% yoy, slightly softer than SSC's guidance of RMB81.7bn after spending cuts by E&P companies in lieu of falling oil prices. The highlight of the results are 1) improvement in profitability on margin expansion; 2) net gearing ratio increased to 67% in FY14 vs. 55% in FY13; and 3) lower dependency on Sinopec as revenue contribution declined to 55% from 66% in FY13.

Margins trending up post re-organization

SSC gross margin improved (FY14: 9.8% vs. FY13: 7.9%) on the back of cost reduction initiatives and enhanced synergies from re-organization. We note SSC's GPM is still on the lower side of industry average indicating more room for margin expansion from a lower base. Among its five major business segments, Geophysics, Drilling and Well logging achieved significant GPM margin expansion of 5ppts, 4ppts and 3ppts yoy in FY14, respectively, after improvement in operating efficiency and cost reduction. We note AR days increased to 104 days in FY14 vs. 82 days in FY13, likely due to delayed payments of domestic oil majors as a result of anti-corruption probes.

FY2015 outlook

SSC is our preferred oilfield services play for FY15 as it will remain a preferred service provider for its parent (Sinopec), guaranteeing order flows even in difficult times unlike independents. However, earnings visibility for FY16 is low and company lacks track record for now. With a slash down in budgeted E&P spending (15% yoy) by Sinopec in FY15, a downward revision in earning growth expectation (guided 45% yoy in FY15) is more likely. Nevertheless, we see some positive catalysts such as a) continued investments in shale gas projects by its parent, (b) expansion in Middle-East region (contributes c.47% of overseas revenue) where production cut is unlikely despite fall in oil prices, and (c) cost reduction initiatives after re-organization (RMB800mn in cost cuts guided for FY15) driving earnings growth even in tough times.

What to do with stock?

Over the past three months, SSC's share price has outperformed independent OFS players by 35% (SSC up by 22% vs. industry down by 13%). We will revisit our model post its analyst briefing in Grand Hyatt Hotel at 12.30 PM on March 25.