China Oilfield Services (2883.HK)

Drilling Operations Forcefully Facilitate Performance Growth
Bloomberg | Reuters | POEMS
2883.HK | 2883.HK | 2883.HK
Sector: Oil & Gas Services

Strategic Analysis
Rating: Buy  Closing Price: 20.50  TP: 27.00

Summary

COSL gains in Q3 a revenue of 7.60 billion Yuan and net profit of 2.18 billion Yuan in a season, with a year-on-year growth of 25% and 53% separately, and a quarter-on-quarter growth of 9% and 11% respectively. During the former three quarters, the corporate revenue is 20.31 billion Yuan and the net profit belonging to shareholders of the listed company is 5.36 billion Yuan, with a year-on-year growth of 24% and 40% separately, and EPS1.19 is 1.19 Yuan.

The performance continues growing more than expected. There are three reasons: First, there is an increase in the number of operation equipment. In the first half year, new equipment like COSL Promoter, NH7 and Investigation II are put on the market, and the normal operation of COSL Innovator and NH2 results in a year-on-year growth of 16% in the company's drilling days. Second, there is an increase in the fullness of workload and efficiency. COSL and its oversea workload is full, and the improved efficiency in the company's drilling platform cause an increased calendar day usage of 2.8 PCT in drilling ship and 3.0 PCT in service marine equipment. Third, the daily use charge rate of drilling platform has grown up.

The performance growth of drilling operation depends on the increased usage of stock equipment, the number of newly added drilling platforms and the average daily revenue of drilling platform, and the main driving factor is the demands of markets home and abroad. In recent years, with the rebound of offshore oil and gas perambulation, COSL has been rapidly expanding its equipment scale by means of its "buying, renting and building" strategy, which leads to a strong growth in its performance and a remarkably increased market share. The main focus on the company's drilling operation will still be semisubmersible drilling platform that will be used in deepwater drilling in the future.

Overseas performance becomes the main driving force in the development of COSL. Four main centers in the company's overseas market have formed: the North Sea market with its center in Norway, the Mexico-based Mexico Gulf market, the UAE-and-Iraq-based Middle East market, and the Southeast Asia market with its center in Indonesia. The overseas business of the company shows relatively strong endogenous growth.

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In the past few years, the overseas business of COSL Limited (COSL) has experienced exponential growth, and the revenue proportion has increased stably. In 2011, the growth of overseas business of the company reached 20%, accounting for 27% of gross income; while in the mid-term of 2013, these two values reached 40% and 37% respectively. The overseas business has become the important support for the growth of company.

Currently, under the circumstance of relatively high daily rate and utilization ratio, the profit incremental drilling platform makes an important contribution to the business growth. In 2014, the incremental drilling platforms of COSL Limited mainly include two sets of self-elevation drilling platforms and two sets of semi-submersible drilling platforms. Two well-placed sets of self-elevation drilling platforms can take service all the year around basically, while two sets of semi-submersible drilling platforms can take service for three quarters and half year respectively. It is expected that four sets of drilling platforms will contribute a profit of 0.65 billion RMB in 2014, which will constitute the main part of profit growth of the company in 2014. Moreover, the growth visibility of oilfield service field is relatively high, which will serve as another important driving force for the growth.

Benefiting from several positive factors of fundamental aspects, including definite growth of capitals of China National Offshore Oil Corporation, acceleration of the development of oil gas in South China Sea and high degree of economy among global oil gas industry, COSL Limited is equipped with solid foundation of business growth. With new platforms going into operation continuously, the business may further exceed the expectation in the future. COSL Limited is an excellent target for investors to share the rapidly growth of global and Chinese oil-gas exploration industry, as well as the best choice of the oilfield service industry among Hong Kong stocks. Above all, we give COSL Limited the rating of "buy" and the target price of 12 months reaches 27 HKD, amounting to 12.2 times of prospective P ratio in 2014.
<table>
<thead>
<tr>
<th>FYE</th>
<th>FY11</th>
<th>FY12</th>
<th>FY13F</th>
<th>FY14F</th>
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<tbody>
<tr>
<td><strong>Valuation Ratios</strong></td>
<td></td>
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<tr>
<td>P/E (X), adj.</td>
<td>10.39</td>
<td>12.05</td>
<td>15.66</td>
<td>12.20</td>
</tr>
<tr>
<td>P/B (X)</td>
<td>1.55</td>
<td>1.78</td>
<td>2.50</td>
<td>2.02</td>
</tr>
<tr>
<td>EV/EBITDA (X), adj.</td>
<td>9.77</td>
<td>9.86</td>
<td>9.92</td>
<td>10.16</td>
</tr>
<tr>
<td>Dividend Yield (%)</td>
<td>1.84%</td>
<td>2.43%</td>
<td>1.92%</td>
<td>2.45%</td>
</tr>
<tr>
<td><strong>Per share data (RMB)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EPS, reported</td>
<td>0.90</td>
<td>1.01</td>
<td>1.35</td>
<td>1.66</td>
</tr>
<tr>
<td>EPS, adj</td>
<td>0.90</td>
<td>1.01</td>
<td>1.35</td>
<td>1.88</td>
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<tr>
<td>DPS</td>
<td>0.18</td>
<td>0.31</td>
<td>0.40</td>
<td>0.50</td>
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<tr>
<td><strong>Growth &amp; Margins (%)</strong></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>Growth</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue</td>
<td>4.93%</td>
<td>19.97%</td>
<td>24.72%</td>
<td>18.95%</td>
</tr>
<tr>
<td>Operating profit</td>
<td>-0.50%</td>
<td>12.70%</td>
<td>31.46%</td>
<td>22.63%</td>
</tr>
<tr>
<td>EBT</td>
<td>-0.50%</td>
<td>12.99%</td>
<td>32.59%</td>
<td>23.38%</td>
</tr>
<tr>
<td>Net income, adj</td>
<td>-2.10%</td>
<td>12.87%</td>
<td>32.69%</td>
<td>23.32%</td>
</tr>
<tr>
<td>Margins</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating margin</td>
<td>27.04%</td>
<td>25.42%</td>
<td>20.60%</td>
<td>26.35%</td>
</tr>
<tr>
<td>Net profit margin</td>
<td>21.92%</td>
<td>20.62%</td>
<td>21.94%</td>
<td>23.34%</td>
</tr>
<tr>
<td><strong>Key Ratios</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROCE (%)</td>
<td>14.90%</td>
<td>15.00%</td>
<td>15.50%</td>
<td>16.50%</td>
</tr>
<tr>
<td>ROA (%)</td>
<td>6.30%</td>
<td>6.50%</td>
<td>6.50%</td>
<td>6.39%</td>
</tr>
<tr>
<td>Net Debt/(Cash)</td>
<td>21.551</td>
<td>19.600</td>
<td>18.908</td>
<td>22.025</td>
</tr>
<tr>
<td>Net Gearing (X)</td>
<td>75.00%</td>
<td>60.00%</td>
<td>52.00%</td>
<td>45.00%</td>
</tr>
<tr>
<td><strong>Income Statement (RMB mn)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue</td>
<td>18,426</td>
<td>22,106</td>
<td>27,670</td>
<td>31,987</td>
</tr>
<tr>
<td>Operating profit</td>
<td>4,993</td>
<td>5,019</td>
<td>7,380</td>
<td>9,052</td>
</tr>
<tr>
<td>EBT</td>
<td>4,812</td>
<td>5,437</td>
<td>7,209</td>
<td>8,933</td>
</tr>
<tr>
<td>Tax</td>
<td>(772)</td>
<td>(967)</td>
<td>(1,163)</td>
<td>(1,423)</td>
</tr>
<tr>
<td>Tax rate</td>
<td>18.04%</td>
<td>15.95%</td>
<td>15.00%</td>
<td>16.00%</td>
</tr>
<tr>
<td>Profit for the year</td>
<td>4,040</td>
<td>4,570</td>
<td>6,056</td>
<td>7,470</td>
</tr>
<tr>
<td>Minority interests</td>
<td>1</td>
<td>11</td>
<td>6</td>
<td>10</td>
</tr>
<tr>
<td>Net profit</td>
<td>4,039</td>
<td>4,669</td>
<td>6,060</td>
<td>7,480</td>
</tr>
</tbody>
</table>

Source: BLOOMBERG, COSL and Phillip Securities
PHILLIP RESEARCH STOCK SELECTION SYSTEMS

<table>
<thead>
<tr>
<th>Total Return</th>
<th>Recommendation</th>
<th>Rating</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>+20%</td>
<td>Buy</td>
<td>1</td>
<td>&gt;20% upside from the current price</td>
</tr>
<tr>
<td>+5% to +20%</td>
<td>Accumulate</td>
<td>2</td>
<td>+5% to +20% upside from the current price</td>
</tr>
<tr>
<td>-5% to +5%</td>
<td>Neutral</td>
<td>3</td>
<td>Trade within ±5% from the current price</td>
</tr>
<tr>
<td>-5% to -20%</td>
<td>Reduce</td>
<td>4</td>
<td>-5% to -20% downside from the current price</td>
</tr>
<tr>
<td>&lt; -20%</td>
<td>Sell</td>
<td>5</td>
<td>&gt;20% downside from the current price</td>
</tr>
</tbody>
</table>

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock’s risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation.

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