COMPANY REPORT

KB Securities VIETNAM

PV Drilling & Well (PVD)

Benefiting from tight rig supplies

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1H revenue dipped, but NPAT improved

PV Drilling & Well Services' (PVD) 1H23 revenue slightly dropped 0.9% YoY. The hired rigs did not generate any revenue, but the increase in average freight rates (+30% YoY) and the strong improvement in operating efficiency helped to cushion PVD's total revenue. This also helped 1H23 NPAT to reach VND207 billion (vs a loss of VND149 billion in 1H22). In addition, PVD also recorded an extra revenue of VND70.2 billion from customers' contract compensation.

Surging demand for rigs amid tight supplies will make freight rates and performance increase

High Brent oil prices and active exploration and production activities in the Middle East trigger a spike in demand for drilling rigs in the region. Meanwhile, the global supply of rigs is tightening because old rigs are gradually leaving the market while the production rate of new rigs cannot keep up with the demand. In particular, the fleet of Southeast Asian rigs is sharply shrinking due to the attraction from the Middle East, which will cause a shortage in the region.

The freight rates & operating efficiency of PVD's jack-up rigs should increase

We believe that PVD's four jack-up rigs, with the advantage of young ages in the region, can reach the freight rate of over USD100,000/day on their new contracts. The fleet should raise its average operating efficiency from 82.5% in 2022 to 92.1% and 96.0% in 2023 and 2024 respectively, given the high rental demand.

BUY recommendation with the target price of VND30,200/share

Based on FCFF, business outlook and possible risks of PVD, we recommend BUY for PVD stocks. The target price is VND30,200/share, equivalent to an upside of 25.8% compared to the price on August 22, 2023.

Buy maintain

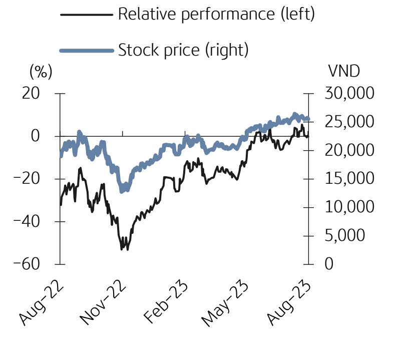
Target price	VND30,200
Upside	25.8%
Current price (Aug 28, 2023)	VND24,000
Consensus market price	VND30,200
Market cap (VNDbn)	13,341

Trading data

Free float	46.9%
3M avg trading value (VNDbn)	130.3
Foreign ownership	28.0%
Major shareholder	VN Oil & Gas (PVN, 50.5%)

Share price performance

(%)	1M	3M	6M	12M
Absolute	0.2	13.8	15.6	34.2
Relative	-4.7	-1.4	-0.7	38.6



Source: Bloomberg, KB Securities Vietnam

Forecast earnings & valuation

FY-end	2021A	2022A	2023F	2024F
Revenue (VNDbn)	3,996	5,432	5,337	5,948
Operating income (VNDbn)	-28	66	690	898
NPAT of the parent (VNDbn)	20	-103	443	570
EPS (VND)	-36	-250	796	1,025
EPS growth (%)	-113	594	-418	29
P/E (x)	-623.89	-71.40	37.81	29.37
P/B (x)	0.69	0.71	1.17	1.13
ROE (%)	0.3	-1.1	3.1	3.8
Dividend yield (%)	0.0	0.0	0.0	0.0

1H23 performance updates

1H revenue dipped, but NPAT improved

PVD's 1H23 revenue decreased slightly by 0.9% YoY. In the first half of the year, PVD did not hire more rigs while it recorded revenue from the leased Hakuryu-11 rig in the same period last year. However, the average rig rental rate gained 30% YoY and the operating efficiency increased 92% compared to 75% in 1H22, which helped to keep revenue from seeing a big drop.

This also helped 1H23 NPAT reach VND207 billion, compared to a loss of VND149 billion in 1H22. Rigs hired from other suppliers usually do not contribute much to PVD's gross profit due to their low gross profit margin (about 1.5 ~ 2%), so PVD's not renting more rigs does not affect the company's profit much. In addition, in 1H23, PVD also recorded an increase in dividends received from joint ventures and extraordinary income arising from customers' compensation for contract cancellation. Meanwhile, interest expenses surged by 107% YoY when the LIBOR rate has increased sharply since the beginning of the year.

Table 1. PVD – 1H23 business results

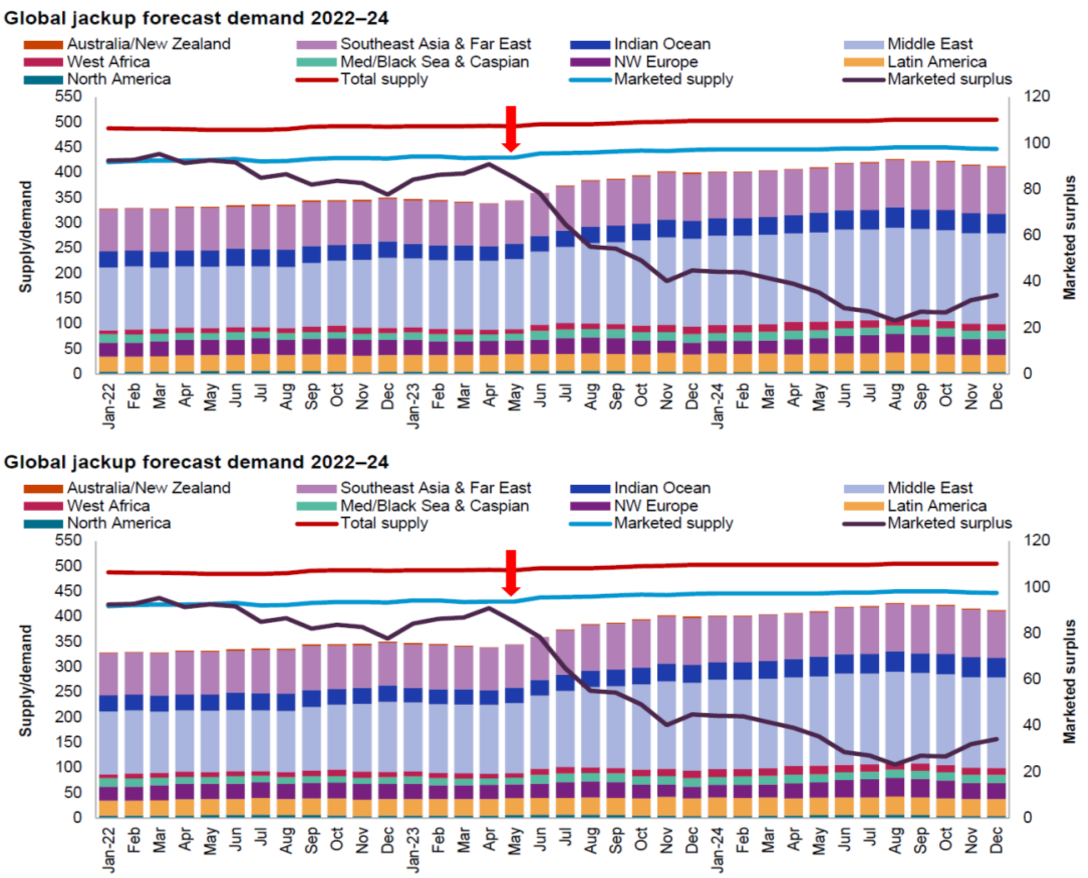
	1H22	1H23	YoY %	KBSV's notes
Revenue (VNDbn)	**2,660**	**2,637**	**-1%**	
Drilling services	1,737	1,884	8%	Jack-up rig freight rates gained 30% YoY, and operating efficiency increased by 92% compared to 75% in 1H22. However, PVD did not generate revenue from leasing rig as in the same period last year.
Commercial services	23	91	303%	
Well and other services	893	664	-26%	Subdued domestic exploitation and production activities in 1H23 directly affects engineering workload.
Gross profit (VDNbn)	**194**	**596**	**207%**	
Gross profit margin (%)	**7%**	**23%**		
Drilling service	-3%	19%		The GPM of rig leasing services dramatically increased thanks to the increase in freight rates and operational efficiency while the cost of capital remained unchanged. The absence of hired rigs also contributes to the improvement of GPM.
Commercial services	32%	7%		
Well and other services	27%	36%		
SG&A costs (VNDbn)	-221	-257		
% SG&A/revenue (%)	-8%	-10%		
Operating income (VDNbn)	-26	340	N.M	
Financial income (VDNbn)	56	52	-6.5%	
Financial expenses (VDNbn)	-134	-178	32.5%	Interest expenses increased mainly due to the surge in LIBOR interest rates.
Other incomes (net) (VDNbn)	-29	39	N.M	PVD received a compensation of about VND70.2 billion from the customers' compensation for contract cancelation.
Profit before taxes (VDNbn)	**-124**	**276**	**N.M**	
Profit after taxes (VDNbn)	**-149**	**207**	**N.M**	

Source: PV Drilling & Well Services, KB Securities Vietnam

Surging demand for rigs amid tight supplies will make freight rates and performance increase

We maintain our forecast that Brent prices would average USD80 and USD75 per barrel for 2023 and 2024, respectively. This will encourage exploration and production activities (E&P) around the world. We see a sudden increase in demand for drilling rigs in the region as Middle East countries take advantage of promoting E&P activities in the period of 2023-2030 to gradually reduce their dependence on revenue from crude oil. S&P Global forecasts that demand for jack-up rigs in this region will increase from 125 rigs in 2022 to 169 and 184 rigs in 2023 and 2024. Meanwhile, the world supply of jack-up rigs is very limited. According to IHS Market, the total supply of jack-up rigs in the world as of July 2023 is 495 rigs, of which 160 rigs are over 30 years old (including 63 inoperable rigs) that will be difficult to lease. due to low stability and increased risk of failure, fire and explosion. Southeast Asia also faces a supply shortage when from 2022 to June 2023, up to 21 out of 53 rigs moving to the Middle East are from Southeast Asia. S&P Global forecasts that the world supply surplus will continue to shrink until the end of 2024, possibly even falling to a negative level for the Southeast Asian market. Currently, the world has only 20 new rigs expected to come into operation in the period 2023-2025 but have been ordered by Middle Eastern customers. Orders to build new rigs, if arriving in the near future, will also take an average of two or three years to complete. Therefore, we believe that the shortage of supply in the market will persist.

Fig 2. Global & Southeast Asia – Forecasts on rig supplies in 2023-2024

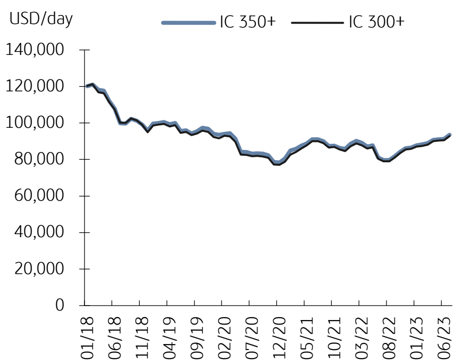


Source: S&P Global, KB Securities Vietnam

The freight rates & operating efficiency of PVD's jack-up rigs should increase

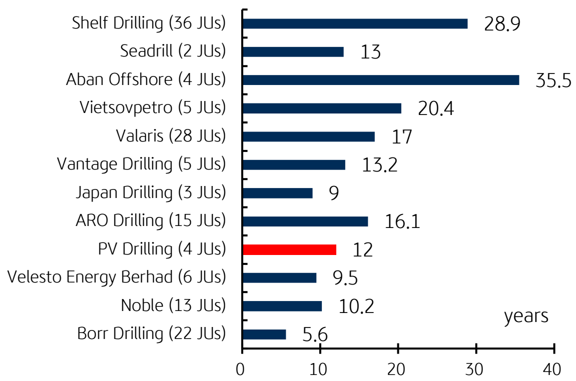
Jac-up rigs will be the growth engine for PVD in the period 2023-2027. PVD I, II and VI rigs have been occupied until the end of 2024. PVD III has a contract until the end of May 2024. PVD's contracts in 2023 include rental rates of about USD75-80 thousand per day. Rates of contracts in 2024 are USD80-90 thousand per day. The rates in PVD's current contracts are quite low compared to the market level. We believe that PVD's four jack-up rigs, with the advantage of young ages in the region, can reach the freight rate of over USD100,000/day on their new contracts. The fleet should raise its average operating efficiency from 82.5% in 2022 to 92.1% and 96.0% in 2023 and 2024 respectively, given the high rental demand in the region.

Fig 3. Global – The rates of jack-up rigs IC 300+ and IC 350+ (USD/day)



Source: Bloomberg, KB Securities Vietnam

Fig 4. PVD – Average age of rig fleet in comparison with regional peers



Source: PV Drilling & Well Services, KB Securities Vietnam

The drilling services segment should grow thanks to the expansion of the rig fleet

PVD plans to invest in one more jack-up rig after considering the sudden increase in demand in the near future. The total investment is about USD130 million, the loan to equity ratio is 70/30. It is expected that the company will approach to buy the rigs under construction (60-70% completed), disburse capital at the end of 2023, and receive the rig in 2024. We believe that this new rig will be immediately offered attractive rates. However, we have not yet included this rig in our forecast model because PVD is still in the process of finding investment partners.

The domestic E&P market will be more active from 2024, benefiting well engineering services

Well technical and other services are expected to benefit directly from the large volume of work at projects such as Te Giac Trang, Ca Ngu Vang, Dai Hung phase 3, Camel Vang, Lot 05. -1b/c, Lot 09-2, Lot 11-2, and Lot 15-2/17 in 2024.

The Block B O Mon project has not yet made much progress because the problems at the mid-downstream stage have not been resolved. We forecast the project's FID will be delayed until mid-2024.

Forecast & valuation

Table 5. PVD – 2023F results

	2022	2023F	+/-%YoY	KBSV's notes
Average cost of jack-up rigs (USD thousand/day)	61	78	28.0%	
Jack-up rig efficiency (%)	82.5%	92.1%		
Revenue (VNDbn)	**5,432**	**5,337**	**-1.7%**	
Drilling services	3,535	3,607	2.0%	Fees and operational efficiency may increase but PVD would not hire rigs as in 2022
Commercial services	115	126.35	10.0%	
Well technical services and other services	1,781	1,603	-10.0%	Domestic E&P activities have not progressed much in 2023
Gross profit (VNDbn)	**577**	**1,169**	**102.4%**	
Gross profit margin (%)	**10.6%**	**21.9%**		
Drilling services	3.6%	23.3%		The spike in GPM is attributable to increased rates and operational efficiency while the cost of capital remains unchanged. The absence of leased rigs also contributes to the improvement of GPM.
Commercial services	24.3%	6.0%		
Well technical and other services	23.7%	20.0%		
SG&A costs (VNDbn)	511	479	-6.3%	
% SG&A/revenue (%)	9.4%	9.0%		
Operating income (VNDbn)	66	690	945.5%	
Financial income (VNDbn)	118	124	5.1%	
Financial expenses (VNDbn)	313	323	3.2%	LIBOR interest rate in the market increased strongly but PVD successfully negotiated to change the loan interest structure (from LIBOR +3% to LIBOR +1%)
Other incomes (net) (VNDbn)	-56	14	N.M	PVD should generate revenue from customers in compensation for contract cancelation in 1H23
Profit before taxes (VNDbn)	**-139**	**568**	**N.M**	
Profit after taxes (VNDbn)	**-155**	**454**	**N.M**	

Source: PV Drilling & Well Services, KB Securities Vietnam

Valuation: BUY recommendation – target price VND30,200/share

We use the FCFF model to make a BUY recommendation for PVD with a target price of VND30,200/share, equivalent to an upside 25.8% compared to the closing price of VND24,000/share on August 22, 2023.

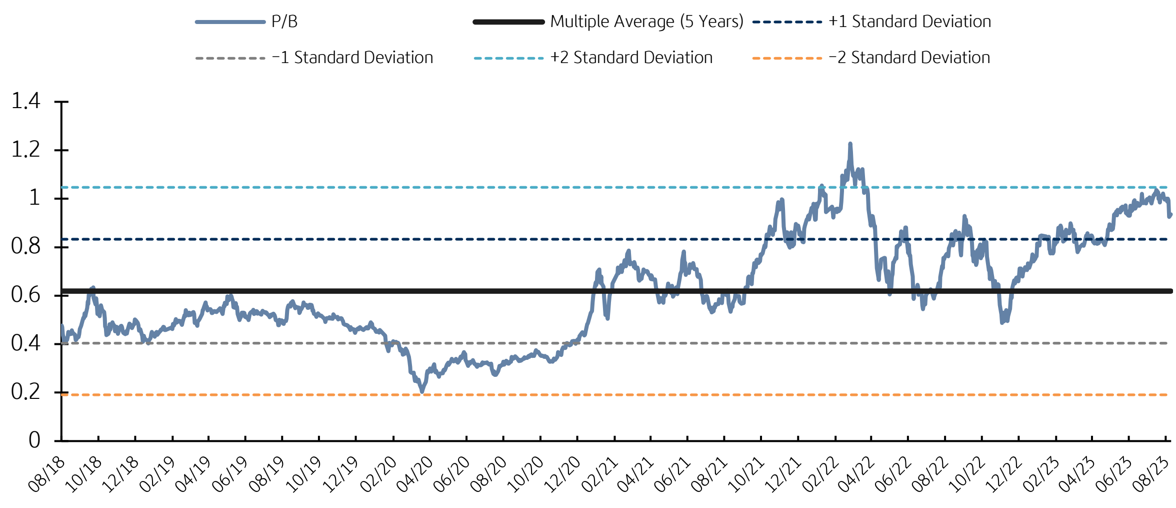
Table 6. PVD – Valuation according to FCFF model

Risk-free rate	5.0%	Present value of terminal value	10,004
Equity risk premium	8.2%	Total present value for the period 2023-2027	6,730
Beta	1.5	**Total present value for the period 2023-2027**	**16,734**
Average interest rate	7.5%	Plus: Cash & Short-term investments	3,543
Taxes	20.0%	Minus: Net Debt	-3,226
Weighted cost of capital	**13.9%**	Minus: Minority interest	-226
Terminal growth rate	1.5%	**Equity value**	**16,825**
		Number of shares outstanding (million shares)	556.30
		Equity value/share (VND)	**30,200**
		Market price (22/08/2023)	24,000
		Upside	25.8%

Source: Bloomberg, KB Securities Vietnam

Our target price is equivalent to a 2023F P/B of 1.18x, +2 SD above PVD's five-year average P/B. We think this P/B is reasonable because (1) the period 2018-2021 is in the low cycle of the whole industry, so the average P/B is low; (2) PVD has only been profitable since 2022, so it cannot fully recover in 2023 to fully reflect its value into BVPS; and (3) the growth catalysts for PVD in the coming time are very clear, deserving a considerable premium compared to the past.

Fig 7. PVD – P/B in 2018-2023 (x)



Source: Bloomberg, KB Securities Vietnam

PVD – 2021A-2024F financials

Income Statement (VND billion)	2021	2022	2023F	2024F
Net sales	3,996	5,432	5,337	5,948
Cost of sales	-3,624	-4,854	-4,168	-4,594
Gross Profit	371	577	1,169	1,354
Financial income	164	118	124	130
Financial expenses	-171	-313	-323	-308
of which: interest expenses	-109	-168	-194	-185
Gain/(loss) from joint ventures (from 2015)	104	45	45	45
Selling expenses	-13	-18	-18	-20
General and admin expenses	-386	-493	-461	-436
Operating profit/(loss)	69	-84	536	765
Other incomes	52	5	74	5
Other expenses	58	60	60	60
Net other income/(expenses)	-6	-55	14	-55
Income from investments in other entities	0	0	0	0
Net accounting profit/(loss) before tax	63	-139	550	710
Corporate income tax expenses	-26	-16	-110	-142
Net profit/(loss) after tax	37	-155	440	567
Minority interests	17	-52	-3	-3
Attributable to parent company	20	-103	443	570

Margin ratio -	2021	2022	2023F	2024F
Gross profit margin	9.3%	10.6%	21.9%	22.8%
EBITDA margin	12.7%	15.6%	32.9%	32.0%
EBIT margin	-0.7%	1.2%	12.9%	15.1%
Pre-tax profit margin	1.6%	-2.6%	10.3%	11.9%
Operating profit margin	1.7%	-1.5%	10.0%	12.9%
Net profit margin	0.9%	-2.9%	8.2%	9.5%

Cash Flow Statement (VND billion)	2021	2022	2023F	2024F
Net profit/(loss) before tax	63	-139	550	709
Depreciation and amortisation	534	783	1,064	1,008
Profit/loss from investing activities	133	-104	-104	-104
Interest expense	109	168	194	185
Operating profit/(loss) before changes in Working Capital	468	945	1,704	1,798
(Increase)/decrease in receivables	-289	-357	110	-235
(Increase)/decrease in inventories	195	-132	123	-80
Increase/(decrease) in payables	271	-440	292	98
(Increase)/decrease in prepaid expenses	-796	32	32	32
Net cash inflows/(outflows) from operating activities	-376	-84	1,962	1,291
Purchases of fixed assets and other long term assets	-608	-155	-300	-333
Proceeds from disposal of fixed assets	0	1	0	0
Loans granted, purchases of debt instruments	-558	-787	-671	-686
Collection of loans, proceeds from sales of debts instruments	1,299	1,907	466	410
Investments in other entities	0	0	0	0
Proceeds from divestment in other entities	0	0	0	0
Dividends and interest received	324	243	243	243
Net cash inflows/(outflows) from investing activities	457	1,208	-262	-366
Proceeds from issue of shares	0	0	0	0
Payments for share returns and repurchases	0	0	0	0
Proceeds from borrowings	346	76	210	87
Repayment of borrowings	-192	-311	-819	-229
Finance lease principal payments	0	0	0	0
Dividends paid	-3	-3	0	0
Interests, dividends, profits received	0	0	0	0
Net cash inflows/(outflows) from financing activities	151	-238	-609	-142
Net increase in cash and cash equivalents	232	886	1,091	783
Cash and cash equivalents at the beginning of period	925	1,131	2,079	3,170
Cash and cash equivalents at the end of period	1,131	2,079	3,170	3,953

Balance Sheet (VND billion)	2021	2022	2023F	2024F
CURRENT ASSETS	20,761	20,704	20,722	21,201
Cash and cash equivalents	5,429	5,646	6,401	7,526
Short-term investments	1,131	2,079	3,170	3,953
Accounts receivable	1,544	424	373	381
Inventories	1,936	2,163	2,053	2,288
LONG-TERM ASSETS	758	909	786	866
Long-term trade receivables	15,332	15,058	14,321	13,675
Fixed assets	50	19	19	19
Investment properties	12,962	13,567	12,830	12,184
Long-term incomplete assets	921	8	8	8
Long-term investments	0	0	0	0
TOTAL ASSETS	0	0	0	0
LIABILITIES	6,930	6,626	6,278	6,265
Current liabilities	3,030	2,868	2,821	3,078
Trade accounts payable	780	568	860	958
Advances from customers	16	86	65	40
Short-term unrealized revenue	748	835	526	654
Short-term borrowings	3,899	3,757	3,457	3,187
Long-term liabilities	0	0	0	0
Long-term trade payables	0	0	0	0
Long-term advances from customers	0	0	0	0
Unrealized revenue	3,206	3,000	2,700	2,430
Long-term borrowings	13,832	14,079	14,444	14,936
OWNER'S EQUITY	4,215	5,563	5,563	5,563
Paid-in capital	2,434	2,434	2,434	2,434
Share premium	1,923	436	804	1,299
Undistributed earnings	5,041	5,438	5,438	5,438
Minority interests	240	229	226	223

Key ratios -				
Multiple				
P/E	-623.9	-71.4	37.9	29.5
P/E diluted	-623.9	-71.4	37.9	29.5
P/B	0.7	0.7	1.2	1.1
P/S	2.4	1.8	3.2	2.8
P/Tangible Book	0.7	0.7	1.2	1.1
P/Cash Flow	-25.2	-118.2	8.6	13.0
EV/EBITDA	24.7	14.0	9.7	8.5
EV/EBIT	-446.8	180.2	24.7	18.0
Operating performance				
ROE	0.3%	-1.1%	3.1%	3.8%
ROA	0.2%	-0.8%	2.1%	2.7%
ROIC	-0.2%	0.4%	4.5%	6.1%
Financial structure				
Cash Ratio	0.9	0.9	1.3	1.4
Quick Ratio	1.5	1.6	2.0	2.2
Current Ratio	1.8	2.0	2.3	2.5
LT Debt/Equity	0.2	0.2	0.2	0.2
LT Debt/Total Assets	0.2	0.1	0.1	0.1
Debt/Equity	0.1	0.1	0.0	0.0
Debt/Total Assets	0.0	0.0	0.0	0.0
ST Liabilities/Equity	0.2	0.2	0.2	0.2
ST Liabilities/Total Assets	0.1	0.1	0.1	0.1
Total Liabilities/Equity	0.5	0.5	0.4	0.4
Total Liabilities/Total Assets	0.3	0.3	0.3	0.3
Activity ratios				
Account Receivable Turnover	2.1	2.7	2.5	2.7
Inventory Turnover	4.2	5.8	5.3	5.3
Account Payable Turnover	5.4	8.1	7.5	6.5

Source: PV Drilling & Well Services, KB Securities Vietnam

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Investment ratings & definitions

Investment Ratings for Stocks
(based on expectations for absolute price gains over the next 6 months)

Buy:	Hold:	Sell:
+15% or more	+15% to -15%	-15% or more

Investment Ratings for Sectors
(based on expectations for absolute price gains over the next 6 months)

Positive:	Neutral:	Negative:
Outperform the market	Perform in line with the market	Underperform the market