

27 March 2018

Energy & Petrochemicals | Exploration & Production

GSS Energy

A Visit To GSS Batam

We visited GSS' Batam factory and came away quite positive on the company's outlook. We understand that it is currently operating at >80% utilisation and has earmarked another bigger site to shift to in 2019. This is to cope with additional orders (+10-20% YoY) from existing and new customers. In addition, we also expect it to produce and sell oil by 1H18, it is likely to benefit from the rising trend in oil prices. We think that the current weakness represents a good opportunity to accumulate at lower levels. Maintain BUY with a SOP-based SGD0.25 TP (47% upside).

GSS Energy's (GSS) high precision engineering with Japanese roots for excellence. GSS was formally set up by the Japanese, and hence its focus and expertise lie in high precision engineering (PE) capabilities, accompanied with high quality standards. This has enabled the company to secure several blue chip names like Phillip, Panasonic as well as being the only listed SGX manufacturer to have Lego as a customer, whom we know to have very high standards. A majority of their machines are also from European and Japanese brand names.

New factory earmarked – robust growth from existing and new customers. Management revealed that the demand from its existing customers like Phillips and Lego has stayed strong, with orders growing 10-20% YoY. GSS has also been engaged in ongoing testing with a new customer in the consumer space, and expects to start full-scale production by 1H18 (this could boost the PE division's topline additionally by 15-20% in FY18F).

Improving on automation to reduce cuts and increase yields. We understand that GSS has its own engineering, team which focuses on automating some of the labour intensive processes. This would be done by designing and customising some of the machines to better suit its needs, including writing its own software. That has driven down the total number of workers despite revenue increasing YoY.

Proxy to rising oil prices. On 13 Dec 2017, GSS made a hydrocarbon discovery in its Trembul operating area. Management has stated that it expects production of gas to commence in 4Q18. The company is re-entering a makeover well and we expect it to start producing 100-200 bbls of oil a day by 1H18 – and to enjoy better margins and profitability if oil prices continue to increase (an ongoing trend for the past few weeks). Brent crude oil has since hit USD70/bbl compared to the USD60/bbl we use in our forecasts.

Twin engines point to a positive outlook - Maintain BUY. With a positive outlook ahead affirmed by its recently implemented dividend policy, we think GSS is currently at an inflection point. At its current share price level, the stock is significantly undervalued. It also provides a unique opportunity for investors to ride on the manufacturing boom and the oil price recovery. We think that the current weakness represents a good opportunity to accumulate at lower levels. Maintain BUY with a SOP-based SGD0.25 TP (47% upside).

Buy (Maintained)

Target Price: SGD0.25
 Price: SGD0.17
 Market Cap: USD63.1m
 Bloomberg Ticker: GSSE SP

Share Data

Avg Daily Turnover (SGD/USD) 1.14m/0.86m
 52-wk Price low/high (SGD) 0.14 - 0.19
 Free Float (%) 57
 Shares outstanding (m) 496
 Estimated Return 47%

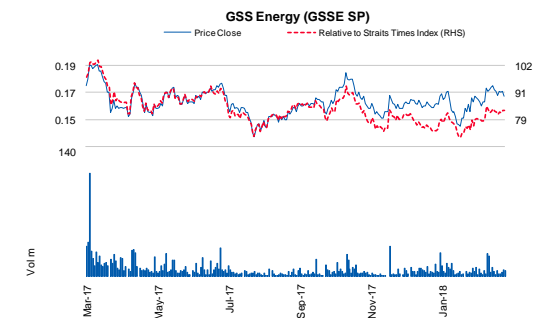
Shareholders (%)

Roots Capital Asia Limited 18.3
 Sundan Pacific Limited 17.3

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	3.1	0.6	5.7	5.0	(5.7)
Relative	2.6	3.8	4.6	(1.2)	(15.1)

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Total turnover (SGDm)	94	76	94	121	138
Reported net profit (SGDm)	(28.0)	22.2	5.3	7.9	10.1
Recurring net profit (SGDm)	(31.2)	13.4	4.3	7.9	10.1
Recurring net profit growth (%)	0.0	0.0	(67.8)	82.2	29.1
Recurring EPS (SGD)	(0.07)	0.03	0.01	0.02	0.02
DPS (SGD)	na	na	na	0.003	0.004
Recurring P/E (x)	na	6.0	19.2	10.5	8.2
P/B (x)	5.94	2.18	1.92	1.67	1.44
P/CF (x)	178	26	27	42	8
Dividend Yield (%)	na	na	na	1.9	2.4
EV/EBITDA (x)	na	3.83	9.65	6.03	4.72
Return on average equity (%)	0.0	86.7	13.0	17.0	18.9
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted)					

Source: Company data, RHB

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Financial Exhibits

Financial model updated on : 2018-03-12

Asia	Financial summary	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Singapore	Recurring EPS (SGD)	(0.07)	0.03	0.01	0.02	0.02
Energy & Petrochemicals	EPS (SGD)	(0.06)	0.05	0.01	0.02	0.02
GSS Energy	DPS (SGD)	0.000	0.000	0.000	0.003	0.004
Bloomberg GSSE SP	BVPS (SGD)	0.03	0.08	0.09	0.10	0.12
Buy	Weighted avg adjusted shares (m)	473	484	496	496	496
Valuation basis	Valuation metrics	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
SOP of SGD0.25 backed by DCF	Recurring P/E (x)	na	6.0	19.2	10.5	8.2
Key drivers	P/E (x)	na	3.6	15.7	10.5	8.2
i. Undervalue oil & gas business segment;	P/B (x)	5.94	2.18	1.92	1.67	1.44
ii. Growth in the precision engineering (PE) business segment.	FCF Yield (%)	(12.3)	(3.0)	(13.7)	(9.3)	1.3
Key risks	Dividend Yield (%)	0.0	0.0	0.0	1.9	2.4
i. Foreign currency risk;	EV/EBITDA (x)	na	3.83	9.65	6.03	4.72
ii. Vulnerable to manufacturing slowdown;	EV/EBIT (x)	na	4.2	12.4	7.6	5.7
iii. Oil & gas sale prices risk.	Income statement (SGDm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Company Profile	Total turnover	93.8	75.7	94.3	120.5	137.6
GSS Energy (GSS) has two core operating businesses: oil & gas and PE. Previously known as Giken Sakata (S) Limited (Giken), it operated the PE business division and was listed on the Singapore Stock Exchange in Feb 1993. The listing status was then transferred to GSS effective 12 Feb 2015 and Giken became a wholly-owned operating subsidiary of GSS. In 2014, GSS ventured into the energy business, and today GSS is operating a twin business model, PE and oil & gas, to build greater resilience to meet the increasing uncertainty in the business environment and global economy.	Gross profit	26.4	17.9	19.1	24.2	30.3
	EBITDA	(24.1)	16.3	7.5	12.9	16.0
	Depreciation and amortisation	(2.4)	(1.6)	(1.6)	(2.7)	(2.7)
	Operating profit	(26.4)	14.7	5.8	10.3	13.3
	Net interest	0.1	0.2	0.2	0.2	0.2
	Income from associates & JVs	(0.0)	(0.0)	0.0	0.0	0.0
	Exceptional income - net	0.0	0.2	0.0	0.0	0.0
	Pre-tax profit	(24.5)	23.8	7.1	10.5	13.5
	Taxation	(3.5)	(1.6)	(1.8)	(2.6)	(3.4)
	Recurring net profit	(31.2)	13.4	4.3	7.9	10.1
	Cash flow (SGDm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
	Change in working capital	(9.0)	(2.6)	(0.2)	(7.1)	(2.8)
	Cash flow from operations	0.4	3.1	3.0	2.0	10.8
	Capex	(10.2)	(5.5)	(14.4)	(9.7)	(9.7)
	Cash flow from investing activities	(22.7)	(5.8)	(16.4)	(6.6)	(6.2)
	Proceeds from issue of shares	24.0	7.9	0.1	0.0	0.0
	Dividends paid	0.0	0.0	0.0	(1.6)	(2.0)
	Cash flow from financing activities	27.7	6.8	1.8	0.4	(2.0)
	Cash at beginning of period	4.4	10.2	14.9	4.7	0.6
	Net change in cash	5.4	4.1	(11.5)	(4.1)	2.5
	Ending balance cash	9.9	14.7	4.2	0.8	3.1
	Balance sheet (SGDm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
	Total cash and equivalents	10.7	18.9	13.8	9.6	12.1
	Tangible fixed assets	8.1	12.2	24.2	29.8	33.4
	Intangible assets	0.2	0.1	0.2	0.2	0.2
	Total investments	0.0	0.0	0.0	0.0	0.0
	Total assets	38.1	57.5	75.0	86.2	98.3
	Short-term debt		0.1	2.9	4.9	4.9
	Other liabilities	1.1	1.3	1.4	1.4	1.4
	Total liabilities	24.4	19.6	31.8	36.8	40.8
	Shareholders' equity	13.3	38.0	43.2	49.5	57.6
	Minority interests	0.5	(0.1)	(0.1)	(0.1)	(0.1)
	Total equity	13.7	37.9	43.1	49.4	57.6
	Net debt	(10.7)	(18.8)	(10.9)	(4.7)	(7.2)
	Total liabilities & equity	38.1	57.5	75.0	86.3	98.3
	Key metrics	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
	Revenue growth (%)	0.0	(19.3)	24.6	27.8	14.2
	Recurrent EPS growth (%)	0.0	0.0	(68.5)	82.2	29.1
	Gross margin (%)	28.1	23.6	20.2	20.1	22.0
	Operating EBITDA margin (%)	(25.6)	21.5	7.9	10.7	11.6
	Net profit margin (%)	(29.8)	29.4	5.6	6.5	7.4
	Capex/sales (%)	10.9	7.2	15.3	8.0	7.0
	Interest cover (x)	(26,417)	983	277		

Source: Company data, RHB

Figure 1: Optical sensing unit manufactured by GSS



Source: RHB

Figure 2: Toys manufactured by GSS



Source: RHB

Figure 3: Plastic toy parts manufactured by GSS



Source: RHB

Figure 4: Plastic components for consumer goods



Source: RHB

Figure 5: CNC machine production line



Source: RHB

Figure 6: Plastic iron stand



Source: RHB

Figure 7: Shaver production line



Source: RHB

Figure 8: Plastic component for shaver to be shipped



Source: RHB

Figure 9: New clean room capacity for new orders



Source: RHB

Figure 10: Plastic toy components manufactured



Source: RHB

Figure 11: CNC drop system



Source: RHB

Figure 12: Lines set up for new key project



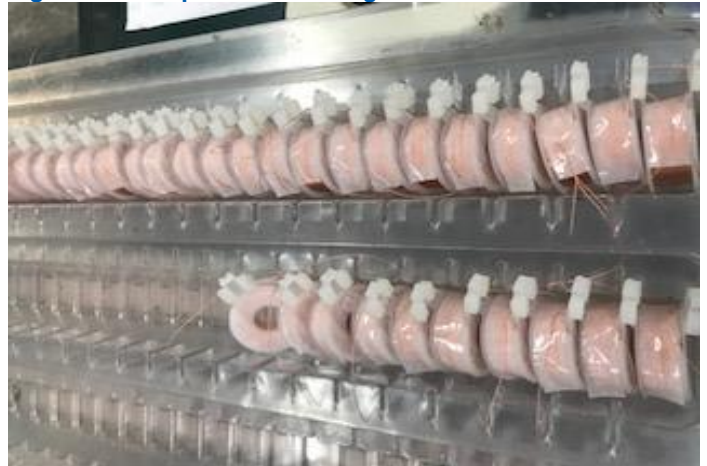
Source: RHB

Figure 13: Automation of wiring coils



Source: RHB

Figure 14: End product of wiring coils



Source: RHB

Figure 15: Freezer by product



Source: RHB

Figure 16: Assembled and ready to be shipped



Source: RHB

Figure 17: PCBA floor line



Source: RHB

Figure 18: PCBA floor line 2



Source: RHB

Figure 19: Centralised GSS self-written software



Source: RHB

Figure 20: PCB production line



Source: RHB

Figure 21: PCBs to be shipped



Source: RHB

Figure 22: PCB board



Source: RHB

Figure 23: Assembly line



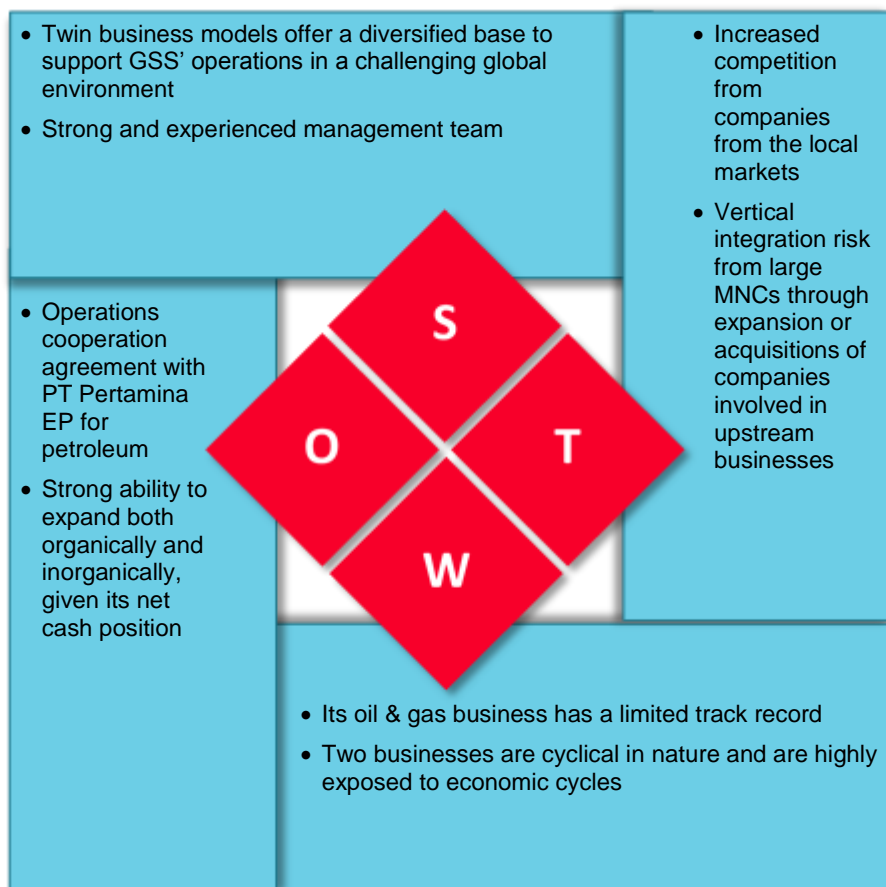
Source: RHB

Figure 24: Goods to be shipped



Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2018-03-06	Buy	0.25	0.16
2015-08-24	Neutral	0.09	0.08
2015-01-05	Buy	0.65	na
2014-11-05	Buy	0.65	na

Source: RHB, Bloomberg

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Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated: Stock is not within regular research coverage

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