

Daya Materials gains foothold in North Sea

BY BEN SHANE LIM

Emerging upstream oil and gas service provider Daya Materials Bhd could become one of the first Malaysian companies to secure long-term upstream O&G contracts in the highly competitive Norwegian market.

According to group managing director Nathan Tham, Daya Materials is close to securing both short-term and long-term contracts in the North Sea for its chartered vessel *Siem Daya 1* (SD1), ensuring that the subsea service vessel is deployed for jobs immediately upon its delivery in September.

Meanwhile, the group is in negotiations to acquire a major stake in a similar vessel in Norway, which could be completed as early as December, along with service contracts in the North Sea. It plans to name the second vessel SD2.

"We are negotiating several contracts with oil majors and global offshore contractors for both the short-term and long-term deployment of SD1 in the North Sea. If we are successful, we will be the first Malaysian company to bag a long-term

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More than 40 experts hired for push into upstream O&G sector

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contract in the Norwegian market," says Tham.

SD1 is a new build, offshore subsea construction and dynamic positioning diving support vessel and the group's first long-term charter. Once it is delivered in September, it is expected to jump straight into action under a short-term contract for about six months with an oil major. After that, the group is lining up a long-term contract with an offshore contractor that will keep the vessel busy until 2020.

According to Tham, Daya Materials has the option to acquire SD1 from its owner Siem Offshore Inc.

"We are also in negotiations to buy a number of these vessels (SD1 and SD2). The value of each vessel will be in excess of US\$100 million (RM327.6 million). We plan to deploy these vessels not only in Malaysia, but also worldwide. Ultimately, we want to be regarded as a Malaysian O&G company with a global reach."

Tham adds that the group has hired more than 40 engineers and specialists, mostly expatriates, for its push into the upstream O&G sector.

The securing of contracts for SD1, and potentially SD2, by the end of the year will mark the group's most significant foray into the upstream business to date and will be a catalyst for a re-rating.

A report by DBS Vickers Securities is estimating a 7% boost to Daya Materials' FY2013 (ending Dec 31) earnings if a contract can be secured soon. Moving forward, FY2014 and FY2015 earnings are expected to reach RM45 million and RM52 million respectively, notes the research house, which has a target price of 45 sen a share. The stock closed at 33.5 sen last Friday, giving it a market capitalisation of RM417.9 million.

Offshore subsea service contracts typically command about 10% to 50% margins, but internally, Daya Materials is targeting to achieve 20% margins for its venture in the North Sea. For SD1, the group has negotiated a daily charter rate of US\$63,500 from Oslo-listed Siem Offshore Inc.

The second vessel, SD2, will have the same specs as SD1, the latest generation Norwegian build. Tham aims to also have a contract lined up for SD2 by the time it is delivered, tentatively by year-end. This vessel will pursue similar jobs in the highly competitive North Sea region, potentially doubling the group's upstream business by next year.

"We could compete for jobs at home, but we decided to make things challenging early on so that they would be easier later. How many Malaysian companies can say they have done



Tham: From 2010 to 2015, we want to grow the company fivefold and achieve a market cap and revenue of RM1 billion by going upstream

jobs in Norway? Once we have that sort of track record, it will be much easier to secure future jobs. On the other hand, if we do jobs locally, it will take longer to be recognised internationally," remarks Tham.

Acquiring a vessel, however, will be a breakaway from Daya Materials' traditionally asset-light model. Currently, the group only has a gearing of 0.1 times and with the amount of steady cash that its other businesses generate, the group could even be in a net cash position by the end of next year — if it does not make any acquisitions. It is worth noting that Daya Materials does not need to acquire an entire vessel but split the ownership with the shipbuilder.

"At the end of the day, we want to come back to Malaysia for our upstream business. To participate in some of Petronas' tenders, one of the requirements is having a Malaysian-flagged vessel. Acquiring a vessel would allow us to make it Malaysian flagged, qualifying us for other opportunities in the future," Tham points out.

Each of these vessels could cost in excess of US\$100 million. Assuming Daya Materials buys half the ownership of a vessel and funds it with 70% borrowings and 30% of its own money, it will only need to fork out upwards of RM50 million from its coffers.

"A private placement is our last choice when it comes to raising funds. If we stick to our business plan, there shouldn't be any need for a private placement. The directors collectively

control the majority of the group and the last thing we want is to be diluted at this stage. That said, we have already been approached by fund managers asking if we are interested in placing out shares," says Tham.

Instead, he reveals, the group will likely pursue a convertible bond issue of about RM50 million to RM70 million to finance acquisitions.

Given the group's relatively strong balance sheet, Tham says banks are also happy to lend and will continue to be the group's first choice when raising funds.

While returns in the upstream O&G sector are lucrative, it is not without risks. The group is able to pursue this because it spent about five years building up its downstream business, which provides the group with steady cash flow that can help sustain its upstream foray.

"The difference between downstream and upstream is that a RM50 million contract downstream is considered big. Upstream, a RM50 million contract is small. From 2005 to 2010, we ventured into downstream O&G and grew our business fivefold. From 2010 to 2015, we want to replicate this by going upstream and grow the company another fivefold and achieve a market cap and revenue of RM1 billion. Given our small base, this is very achievable," says Tham.

One only has to look at the stellar performance of Yinson Holdings Bhd to see that a successful venture upstream can see a huge leap in a company's earnings and lift the market cap of a small company above RM1 billion. Yinson's

market cap has ballooned from RM150 million as at end-2012 to over RM1.2 billion this year since it ventured into the upstream business in Vietnam.

In comparison, Daya Materials currently boasts a market cap of RM418 million at 34 sen a share. This also values it at 13 times forward earnings estimates, not including the potential earnings of its two new vessels.

"We secured our first subsea contract [in Malaysian waters] about two to three years ago in partnership with a couple of companies. While executing that contract, we recognised the potential and size of this business. That was when we decided to zero in on the offshore subsea sector. Being successful in the downstream sector gave us the experience and confidence to venture upstream aggressively," says Tham.

In the downstream sector, Daya Materials has a fleet of 25 cranes ranging from 25 tonnes to 400 tonnes as well as almost a dozen auxiliary trucks and forklifts. Its downstream chemicals business includes supplying virtually all the odorant for liquid petroleum gas (LPG) in Malaysia. Odorant is injected into LPG to give the typically odourless gas used for cooking its distinctive smell to detect leakages.

The group kicked off its upstream business by undertaking two pipe-laying jobs in Miri and Terengganu worth about RM80 million, in which Daya Materials' stake was about a third. Since then, the group has groomed a highly experienced management team with 25 to 30 years of experience in the industry.

Its upstream business is now helmed by Mark Midgley, formerly with the internationally renowned Subsea7. Another key figure in the team of 40 to 50 people is Shahul Hamid, former CEO of Shell Refining Co Bhd, says Tham.

The group is also tapping the upstream business with a small stake in Reach Energy Bhd, a special purpose acquisition vehicle (SPAC) that will venture into brownfield projects, which will be headed by Shahul.

While Daya Materials' stake in the SPAC will be very small, it will tap into its performance by offering services. At the same time, Daya Materials will be shielded from the risky nature of the exploration and production business.

"This is both an exciting and challenging time for us. Exciting because we are growing very rapidly and only beginning to realise our potential as an O&G player. Opportunities are immense. At the same time, it is very challenging as we have to compete with international players with more resources and deal with multinational clients with more stringent demands while managing our own resource allocation and asset deployment," says Tham.