Oiltek International Ltd

Beneficiary of the big push for sustainable fuel

SINGAPORE | ENGINEERING | UPDATE

8 April 2024

NOT RATED

LAST CLOSE PRICE SGD 0.250

- Oiltek provides design, engineering, maintenance, and turnkey solutions for refineries and processing plants in the vegetable oils industry. These include the major agricultural commodities such as palm, soybean, and rapeseed.
- FY23 net profit rose 50.9% to RM19.1mn on the back of strong order wins of RM322mn (FY22: RM196mn). The order book was a record RM382mn at end-2023 (FY22: RM210mn) to be completed in 18 to 24 months. Order wins are underpinned by higher oil consumption and downstream applications, increased use of renewable fuel such as biodiesel, and push for sustainable aviation fuel in the aviation industry.
- Balance sheet has net cash of RM132mn, or S$0.265/share. The business model is asset-light, with low capex needs and fixed assets of only RM3mn. FY23 free cash flow generated was S$0.137/share. The share trades at 1.86x P/FCF. The current market cap is below net cash.

Background

Oiltek is a design and engineering specialist for vegetable oil refineries and processing plants for major agricultural commodities, including palm, soybean, and rapeseed. These refineries produce edible and non-edible oil, related downstream products, and renewable energy such as biodiesel and biogas. Oiltek also possesses the know-how to process waste fats/oil into an intermediate feedstock for the production of sustainable aviation fuel. Key customers are major listed plantation companies. Indonesia accounts for 78% of FY23 revenue.

Highlights

- There has been a **regulatory push to raise biodiesel consumption**, driving investments in biodiesel refineries. The Indonesian government's biodiesel mandate was raised to B35 nationwide in August 2023 and is targeting B40 in the future. This directive blends 35% palm-based biodiesel with fossil diesel to reduce fuel imports, lift domestic demand for palm oil, and cut emissions.
- Malaysia has a similar proposed B20 mandate for the transport sector. However, this is not implemented nationwide due to limited blending facilities. We expect more investments into biodiesel plants as each state seeks to be self-reliant in supply.
- There is a **growing demand for sustainable aviation fuel (SAF)**. Oiltek will ride on this demand as the international aviation industry targets reaching net zero carbon emissions by 2050. Many countries have mandated flights use 3-10% of SAF by 2030.
- To this end, European oil refining companies such as Neste Oyj and Total S.A. are building new hydrogenated vegetable oil (HVO) refineries. HVO is the second largest renewable diesel alternative worldwide and can be upgraded to SAF. Oiltek has the solutions to treat palm oil mill effluent and used cooking oil, in compliance with the International Sustainability & Carbon Certification, as feedstock for the production of HVO.
- **Asset-light, strong ROE, and cash flow.** Oiltek's key assets are the proprietary process technology and know-how. Plant fabrication and installation work are outsourced to third-party fabrication plants, thus minimizing capex needs.

  Hence, the attractive FY23 ROE of 28%, despite the net cash of RM132mn in its balance sheet, and strong free cash flow. FY23 FCF/share was S$0.137. The share trades at 1.86x P/FCF and below net cash of S$0.265/share. It pays a dividend of 1.6 cents or a yield of 6.4% in FY23.

COMPANY DATA

BLOOMBERG CODE:	OTEK SP
O/S SHARES (MN) :	143
MARKET CAP (USD mn / SGD mn) :	27 / 36
52 - WK HI/LO (SGD) :	0.26 / 0.19
3M Average Daily T/O (mn) :	0.09

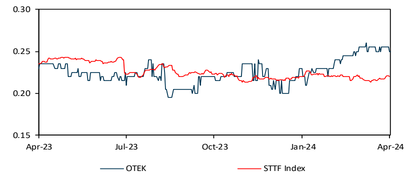
MAJOR SHAREHOLDERS (%)

KOH BROTHERS ECO ENGINEERING LTD	68.1%
YONG KHAI WENG	6.3%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	(2.0)	13.6	14.2
STTF RETURN	4.2	2.0	2.2

PRICE VS. STTF



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec (RM, 'mn)	FY20	FY21	FY22	FY23
Revenue	88	101	164	201
Gross Profit	28	24	31	39
EBIT	16	13	18	25
NPAT	12	10	13	19
P/NAV (x)	3.1	3.1	2.4	1.9
P/E (x)	8.6	10.9	9.9	6.6
ROE (%)	36.0%	28.2%	23.7%	28.2%

Source: Company, PSR

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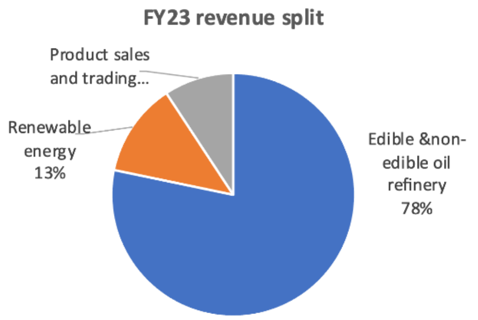
Background

Oiltek is a design and engineering specialist for vegetable oil refineries and processing systems for major agricultural commodities, including palm, soybean, and rapeseed. These refineries produce edible and non-edible oil, related downstream products, and renewable energy such as biodiesel and biogas. Its key customers are major listed plantation companies.

Edible and non-edible oil refinery construction and upgrade accounted for 78% of revenue share in FY23 (Figure 1). Still, renewable energy, comprising biodiesel and biogas plants, grew at a faster rate of 83% YoY (Figure 2).

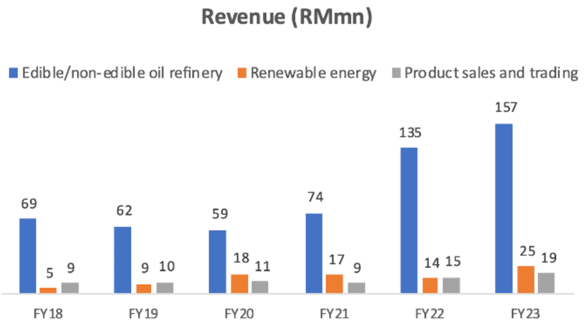
Oiltek has the technology solution to process waste fats/oil, such as palm oil mill effluent (POME) and used cooking oil (UCO), as well as other vegetable oil-based raw materials, into the feedstock for production of hydrogenated vegetable oil (HVO), which is used as sustainable aviation fuel. Its process technology complies with the International Sustainability and Carbon Certification (ISCC). Oiltek has delivered its first HVO feedstock treatment plant that uses POME to a customer in Malaysia.

Figure 1: Edible and non-edible oil refinery takes 78% of revenue share



Source: PSR, Company

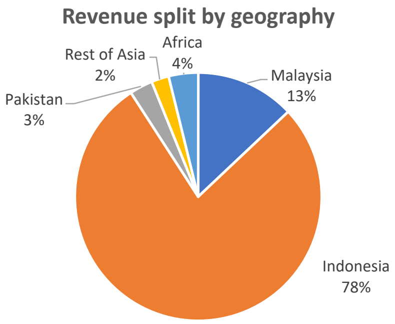
Figure 2: Renewable energy grew the fastest at 5-year CAGR of 39%



Source: PSR, Company

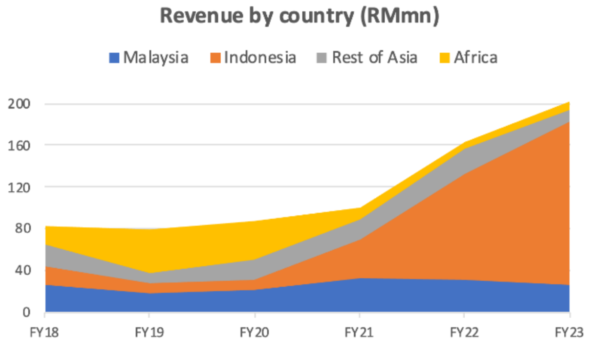
The two largest markets are Indonesia and Malaysia (Figure 3), the largest palm oil producers globally. The two countries are advocating the use of biodiesel produced from oil palm.

Figure 3: Indonesia is its largest and fastest-growing market



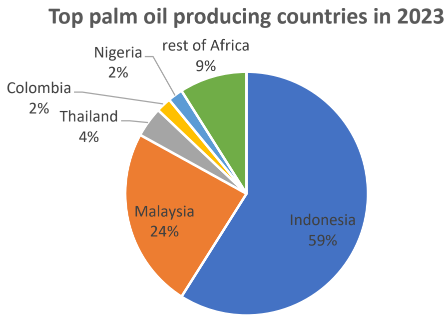
Source: PSR, Company

Figure 4: Projects in Indonesia took off in FY21



Source: PSR, Company

Figure 5: Indonesia accounts for 59% of world's palm oil production



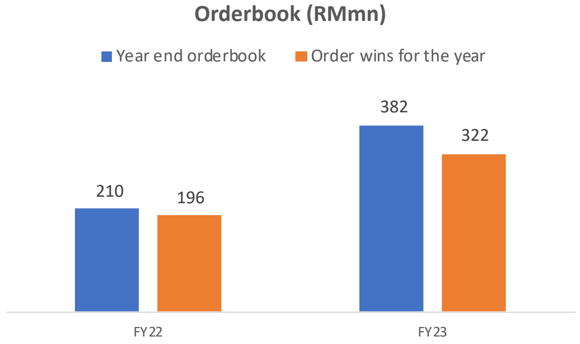
Source: USDA

Orderbook

The orderbook at the end of December was a record RM382mn (Figure 6). Order wins rose 64% in FY23. The following factors drive demand for the construction and upgrade of vegetable oil refineries:

- Higher consumption demand for vegetable oil used in food and downstream applications
- Palm oil products as a substitute for some food ingredients, such as cocoa butter
- Push for the use of biodiesel as a greener fuel. Biodiesel can be produced from vegetable oil or waste oil.

Figure 6: Record order book

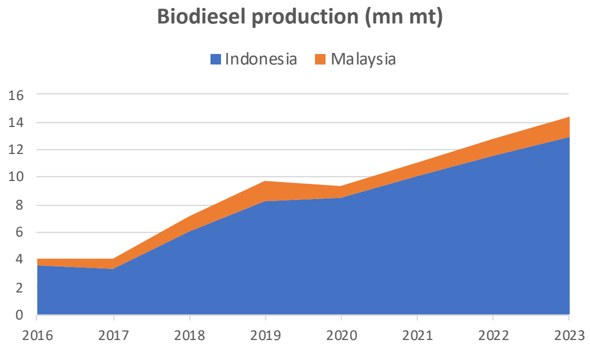


Source: PSR, Company

Biodiesel mandate

Driven by national biodiesel mandates, biodiesel production has risen by a 6-year CAGR of 23.3% in Indonesia and Malaysia (Figure 7).

Figure 7: Biodiesel output



Source: MPA, MPOB, APROBI

Indonesia's national biodiesel mandate aims to blend diesel with palm-based Fatty Acid Methyl Ester (FAME). The blending rate was raised to 35% across all regions in Aug 2023, and targeting B40 in the future. The objective is to reduce fuel imports, generate domestic demand for palm oil, and cut emissions.

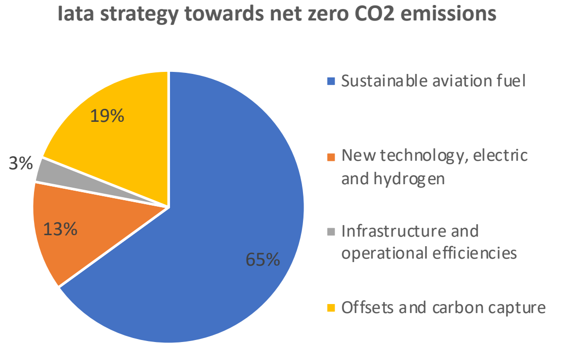
Malaysia has a similar proposed mandate for B20 for the transport sector. However, this has not yet been implemented nationwide due to limited blending facilities. If the B20 mandate is met, FY23 biodiesel production could be 79% higher at 2.5mn mt, according to the Malaysian Biodiesel Association.

We expect more investments in biodiesel plants as each state seeks to be self-reliant in biodiesel supply. Under the 12th Malaysian plan, the transport sector must implement the B30 blending mandate by 2025.

Sustainable aviation fuel

The international aviation industry targets to reach net zero CO_2 emissions by 2050. This will require a ramp-up in the production of sustainable aviation fuel, which could contribute around 65% of the reduction in emissions needed by aviation, according to Iata (Figure 8). Many countries have mandated flights to use 3-10% of SAF by 2030.

Figure 8: Iata strategy towards net zero CO2 emissions



Source: Iata

SAF is a liquid fuel currently used in commercial aviation. It can reduce CO2 emissions by up to 80%. It can be produced from various sources, including waste oil and fats, green and municipal waste, and non-food crops.

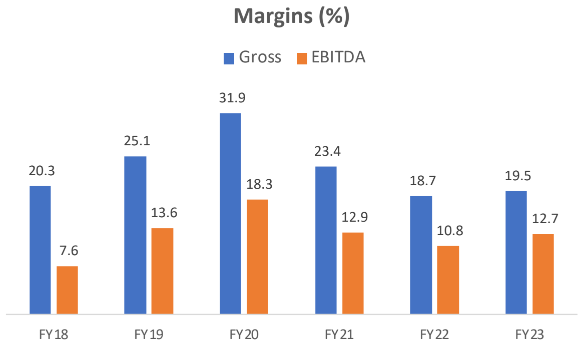
Hydrogenated vegetable oil (HVO), also known as hydroprocessed esters and fatty acids (HEFA), is one of the frontrunner technical pathways for SAF output in the near term. HVO is a synthetic paraffinic diesel reprocessed from vegetable oils or waste with added hydrogen. Unlike previous biofuels, it is a drop-in replacement fuel that can be used without modifying existing engines. Europe is currently the largest producer of HVO.

Oiltek has the solutions to treat palm oil mill effluent (POME) and used cooking oil, as well as any other vegetable oil-based raw materials for use as feedstock in the production of HVO. Its solutions are in compliance with the International Sustainability & Carbon Certification. It delivered its first HVO feedstock treatment plant, which uses POME, to a customer in Malaysia. We expect more order wins for these plants in tandem with the growth in SAF consumption.

Financials

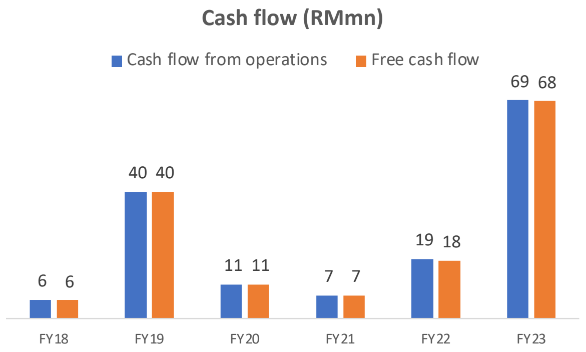
Gross margins corrected in the last two years (Figure 9) as Oiltek took on more turnkey projects but outsourced the plant fabrication and installation work to third-party contractors.

Figure 9: Margins contracted due to a higher proportion of turnkey projects



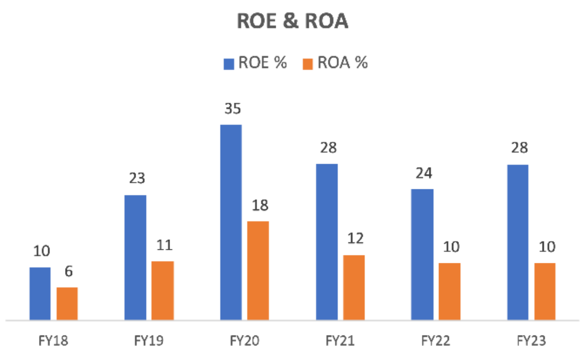
The asset-light and strong cash flow generative model lift ROE to 28% and FCF/share to RM0.48 in FY23 (Figures 10 & 11).

Figure 10: Low capex needs to lift free cash flow



Source: PSR, Company

Figure 11: Strong ROE despite net cash of RM132mn



Source: PSR, Company

PhillipCapital

Financials

Income Statement

Y/E Dec, (RM'mn)	FY19	FY20	FY21	FY22	FY23
Revenue	**80**	**88**	**101**	**164**	**201**
Cost of sales	(60)	(60)	(77)	(133)	(162)
Gross Profit	**20**	**28**	**24**	**31**	**39**
Other operating income	(0)	(0)	1	4	3
Administration	(11)	(10)	(13)	(17)	(17)
Other expenses	2	(2)	2	(0)	0
Share of results of associates and	-	-	-	-	-
EBIT	**11**	**16**	**13**	**18**	**25**
Net finance expenses	-	-	-	-	-
Profit before tax	**11**	**16**	**13**	**18**	**25**
Taxation	(2)	(4)	(3)	(5)	(6)
Net Profit	**9**	**12**	**10**	**13**	**19**
Minority interests	-	-	-	-	-
Profit attributable to owners	**9**	**12**	**10**	**13**	**19**

Per share data (RM sen)

Y/E Dec	FY19	FY20	FY21	FY22	FY23
BVPS	30.6	28.3	28.5	37.4	47.4
DPS (S$ cents)	-	-	-	1.2	1.6
EPS	7.2	10.2	8.1	8.9	13.4

Cash Flow

Y/E Dec, (RM'mn)	FY19	FY20	FY21	FY22	FY23
CFO					
Pretax profit	**11**	**16**	**13**	**18**	**25**
Adjustments	0	(0)	0	1	(3)
WC changes	30	(3)	(3)	4	51
Cash generated from ops	**41**	**13**	**11**	**23**	**74**
Others	(1)	(2)	(3)	(4)	(5)
Cashflow from ops	**40**	**11**	**7**	**19**	**69**
CFI					
CAPEX, net	(0)	(0)	(0)	(0)	(0)
Others	-	-	-	-	0
Cashflow from investments	**(0)**	**(0)**	**(0)**	**(0)**	**(0)**
CFF					
Dividends paid to owners	(18)	(10)	(14)	(9)	(6)
Proceeds from borrowings, net	-	-	-	-	-
Others	-	-	(1)	16	-
Cashflow from financing	**(18)**	**(10)**	**(15)**	**7**	**(6)**
Net change in cash	**22**	**1**	**(8)**	**25**	**63**
Cash at the start of the period	29	51	51	43	67
Currency translation	(1)	(0)	(0)	(0)	2
Ending cash	**51**	**51**	**43**	**67**	**132**

Source: Company, Phillip Securities Research (Singapore) Estimates

Balance Sheet

Y/E Dec, (RM'mn)	FY19	FY20	FY21	FY22	FY23
ASSETS					
PPE & Investment Properties	3	3	3	3	3
Others	0	-	0	0	0
Total non-current assets	**3**	**3**	**3**	**3**	**4**
Cash and cash equivalents	51	51	43	67	132
Inventories	1	1	1	1	1
Trade and other receivables	14	7	17	11	27
Others	10	6	18	40	22
Total current assets	**75**	**65**	**79**	**119**	**181**
Total Assets	**79**	**68**	**82**	**122**	**185**
LIABILITIES					
Trade and other payables	15	22	31	44	38
ST borrowings	-	-	-	-	-
Others	27	11	17	25	79
Total current liabilities	**42**	**33**	**48**	**69**	**117**
LT borrowings	-	-	-	-	-
Others	-	0	-	-	-
Total non-current liabilities	**-**	**0**	**-**	**-**	**-**
Total liabilities	**42**	**33**	**48**	**69**	**117**
EQUITY					
Share Capital	2	2	84	99	99
Retained profits	34	32	32	36	49
Others	-	-	(81)	(81)	(80)
Total equity	**37**	**34**	**34**	**53**	**68**
Minority interests	-	-	-	-	-
Total equity and liabilities	**79**	**68**	**82**	**122**	**185**

Valuation Ratios

Y/E Dec	FY19	FY20	FY21	FY22	FY23
P/E (x)	12.2	8.6	10.9	9.9	6.6
P/B (x)	2.9	3.1	3.1	2.4	1.9
EV/EBITDA (x)	4.9	3.4	4.8	3.3	-0.3
Dividend yield (%)	0.0	0.0	0.0	4.8	6.4
Growth & Margins (%)					
Growth					
Revenue	-3.7%	9.2%	15.0%	62.7%	22.8%
Gross profit	18.9%	38.8%	-15.4%	29.7%	28.3%
EBIT	72.7%	46.2%	-18.7%	36.3%	44.1%
PBT	72.7%	46.2%	-18.7%	36.3%	44.1%
Margins					
Gross profit margin	25.1%	31.9%	23.4%	18.7%	19.5%
EBIT margin	13.6%	18.3%	12.9%	10.8%	12.7%
Net profit margin	10.8%	14.0%	9.6%	7.7%	9.5%
Key Ratios					
ROE	23.5%	36.0%	28.2%	23.7%	28.2%
ROA	11.0%	18.2%	11.8%	10.3%	10.3%
Net Gearing	0.0%	0.0%	0.0%	0.0%	0.0%

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