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'Oil slides unlikely next year'

Price drops not likely to continue into 2015, say industry experts

BY SUPRIYA SURENDRAN

KUALA LUMPUR: Oil prices are unlikely to continue slumping into 2015, say some industry experts.

The market is already seeing a slight but gradual rebound as the benchmark Brent crude, which slipped to below US$59 (RM206.50) on Dec 16 for the first time since May 2009, climbed to US$62 last Monday on expectations that Brent crude futures would likely remain above US$60 for the rest of the year, according to *Reuters*.

"We are sanguine that prices shall revert higher in due course to reflect fiscal as well as asset break-even levels of major producers. Nonetheless, we do not expect prices to rebound back to the levels last seen in the second quarter of 2014," said MIDF Research in its 2015 outlook report on Dec 10 titled *2015 — Adjusting to the New Normal*.

Reach Energy Bhd, the largest special purpose acquisition company (Spac) in the country based on fundraising size, also believes that the swift decline in oil prices will not continue into 2015, according to its chief executive officer Shahul Hamid Mohd Ismail. The Spac is in the oil and gas industry with the intention of acquiring O&G brownfields.

"Oil prices are getting closer to the median breakeven of cost for US shale oil production. In my estimation, oil prices could hover around US$70 to US$90 per barrel in 2015," Shahul Hamid told *The Edge Financial Daily*.

The market is already seeing a slight but gradual rebound as the benchmark Brent crude climbed to US$62 last Monday on expectations that Brent crude futures would likely remain above US$60 for the rest of the year.

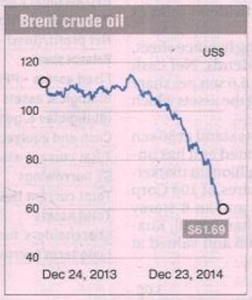
However, he cautions that O&G players will still need to be vigilant to possible impacts should oil prices continue to weaken, such as deferment of projects and cutbacks that will affect the industry globally.

2014 has seen many O&G stocks on Bursa Malaysia taking a beating, and some unfairly so, according to MIDF O&G analyst Aaron Tan, who believes that the local market had overreacted to the drop in oil prices.

"I believe the local market has overreacted with the consolidation of oil prices as most, if not all, O&G companies on the local bourse are service providers and not upstream oil producers," he told *The Edge Financial Daily*.

That said, there are still clear challenges in 2015 for the O&G sector to overcome, he noted, such as the increase in production, engineering, raw material and human capital costs.

"More importantly, the challenge ahead would be the fear of capital expenditure (capex) reduction by major O&G players," said Tan.



In its Dec 9 research note on the sector, BIMB Securities Research said Petroliam Nasional Bhd's (Petronas) announcement that it will be cutting capex by 15% to 20% in 2015 in view of the falling oil prices had hammered stocks across the board as there was a huge outflow of foreign investments upon investors selling down after the announcement was made.

"Petronas has said that it will not award new marginal fields unless oil settles at above the US$80 per barrel level even though breakeven cost is at US$65 per barrel," said BIMB in its note.

Shahrul Hamid: In my estimation, oil prices could hover around US$70 to US$90 per barrel in 2015. **Photo by Suhaimi Yusuf**

But MIDF, in its 2015 outlook, noted that offshore production activities are expected to continue to remain robust, benefiting offshore service providers.

"Offshore support vessel operators are confident that the charter rates will stay firm at US$1.85 to US$2 per brake horsepower, while offshore engineering and services providers noted that tenders are still being called," said MIDF in its note.

The research house also commented that 2015 could be a year of mergers and acquisitions (M&A) within the industry.

"We could expect to see some small service providers merging among themselves or with the larger ones in order to offer more holistic services and product offerings, better compete with regional service providers, and protect their profitability margins," said MIDF.

Apart from M&A activities, MIDF also expects 2015 to be a year of increased acquisitions of O&G assets such as offshore hydrocarbon fields.

"The main [driver of] asset acquisitions is the rationalisation of valuations," said MIDF in its note.

On the performance of O&G Spacs in 2015, Tan said that there are two schools of thought on this.

"The first is that investors will definitely be very cautious and would most likely avoid O&G upstream Spacs as the soft crude oil prices could be a dampener to the company's growth.

"The second is that 2015 could be an opportune time to acquire O&G assets as valuations could be depressed, and Spacs could be a beneficiary to cheap assets," he said.

On which O&G stocks would garner interest in 2015, Tan said MIDF is advocating the idea of "large order books with long burn rates" for the sector.

"With that said, we still favour SapuraKencana Petroleum Bhd, Dayang Enterprise Holdings Bhd and Bumi Armada Bhd for their large order books with long tenures," he said.