

CHINA
DEVELOPMENT
FINANCIAL

Keppel Corporation Ltd

(KEP SP/KPLM.SI)

Offer for M1 and KT&T; EPS-accretive deals leveraging on its strong balance sheet

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- KEP is offering S\$2.06 for M1 and S\$1.91 for Keppel T&T.
- Following the analyst briefing earlier this morning, we view the deal as a net positive for KEP as it is immediately EPS-accretive while only increasing KEP's net gearing to between 0.49x and 0.62x, comfortably well below >1.0x of peers.
- We think that shareholders of M1 and Keppel T&T would most likely accept the offer by KEP for the deal to go through. There are certain conditions to be met but assuming the deals are successful, KEP would recognise the EPS-accretion in 2Q19.

Financials & Key Operating Statistics					
YE Dec (\$\$ m)	2016	2017	2018F	2019F	2020F
Revenue	6767.3	5963.8	6182.1	6855.4	8218.7
PATMI	783.9	216.7	1136.0	1173.1	1307.0
Core PATMI	768.8	815.5	1136.0	1173.1	1307.0
Core EPS	42.3	44.9	62.5	64.6	71.9
Core EPS grth (%)	-49.1	6.1	39.3	3.3	11.4
Core P/E (x)	16.9	16.0	11.5	11.1	10.0
DPS (\$G cents)	20.0	22.0	26.0	28.0	30.0
Div Yield (%)	2.8	3.1	3.6	3.9	4.2
Net Margin (%)	11.6	3.6	18.4	17.1	15.9
Gearing (%)	54.3	44.5	56.9	48.8	44.5
Price / Book (x)	1.1	1.1	1.1	1.0	1.0
ROE (%)	6.4	1.8	8.9	8.7	9.1

Source: Company Data, KGI Research

Post-briefing analysis. Following our meeting with KEP's management this morning, we believe the deal for M1 and Keppel T&T is net positive for KEP as it is immediately EPS-accretive and only increases KEP's net gearing to between 0.49x and 0.62x (assuming 100% M1 shares at close of offer), still comfortably below the >1.0x of peers.

Only looking for controlling stake. We believe that KEP is primarily looking to take a controlling stake in M1 to drive change in the company. That would mean that KEP's management would be content to have the minimum stake of 50% and 1 share to gain control over M1, and would prefer to keep M1 as a listed entity.

High chance of getting >50% for KEP and partners. The offer for M1 is conditional upon KEP and its partners receiving >50% shares of M1, which is not that difficult given that KEP and SPH already own 32.8% of M1. For M1 shareholders, the offer by KEP would be a good exit opportunity as plans that KEP has for M1 may only bear fruit in the medium and long-term. We also think there is the risk that dividends may be reduced at M1 in the event that KEP takes a controlling stake as cash flows are redirected to transform the business. However, in the event that Axiata, M1's other major shareholder rejects the offer and offers a higher counter bid for M1, that would still be a win-win for M1 shareholders and for KEP as well.

Buy - Maintain			
Price as of 26 Sep 18 (SGD)	7.16	Performance (Absolute)	
12M TP (\$)	9.43	1 Month (%)	7.3
Previous TP (\$)	9.43	3 Month (%)	3.2
Upside, inL div (%)	35.4	12 Month (%)	14.0
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	12,977		
Issued Shares (mn)	1,812		
Vol - 3M Daily avg (mn)	3.7		
Val - 3M Daily avg (\$mn)	25.0		
Free Float (%)	99.9%		
Major Shareholders		Previous Recommendations	
Temasek	20.5%	23-Apr-18	BUY \$9.43
Blackrock	5.3%	15-Dec-17	BUY \$8.67
		24-Jul-17	BUY \$7.02

Valuation & Action

We reiterate our Buy recommendation and maintain that KEP is an attractive long-term growth story, especially now that it is more active in M&A deals to leverage on its strong balance sheet. We believe valuations are cheap and investors should use the recent share price weakness to accumulate shares.

We have not factored in the EPS-accretion from M1 and Keppel T&T for now. The despatch of offer document for M1 is expected in 9 weeks, or around December 2018. For Keppel T&T, the scheme meeting is in 19 weeks, or around March 2019.

Our fair value is based on SOTP valuation of its businesses and mainly driven by property (55% of valuation), O&M (20%) and Keppel Capital (13%). These three businesses contribute 87% of our fair value estimates of the group. KEP's track record of unlocking value via divestments may provide further upside to earnings and dividends forecasts.

Risks

KEP's property segment now contributes the largest share of profits. As a result, a slowdown in the property sector in its key markets like China and Singapore will have the largest impact on KEP's valuations.

KGI's Ratings**Rating Definition**

KGI Securities Research's recommendations are based on an Absolute Return rating system.

BUY >10% total return over the next 12 months

HOLD -10% to +10% total return over the next 12 months

SELL <-10% total return over the next 12 months

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