

CHINA
DEVELOPMENT
FINANCIAL

Sembcorp Marine Ltd

(SMM SP/SCMN.SI)

Firming industry outlook

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- SMM's 1Q19 PATMI declined 68% to S\$1.7mn on the back of lower revenues and margins. This is in line with our view that earnings would be weak in FY19F and only recover gradually from FY20F onwards.
- From a bigger perspective, industry fundamentals are improving. We expect new orders to start flowing from 2H19 and accelerate in 2020.
- Re-iterate our BUY recommendation.

Financials & Key Operating Statistics

YE Dec (\$\$ m)	2017	2018	2019F	2020F	2021F
Revenue	2387.4	4887.9	3359.8	4079.8	5399.7
PATMI	14.1	-74.1	3.2	61.1	88.6
Core PATMI	-37.4	-74.3	3.2	61.1	88.6
Core EPS	-1.8	-3.6	0.2	2.9	4.2
Core EPS grth (%)	-138.3	98.6	na	1817.4	45.1
Core P/E (x)	-91.0	-45.8	1069.0	55.8	38.4
DPS (SG Cents)	2.0	0.0	0.0	0.0	0.0
Div Yield (%)	1.2	0.0	0.0	0.0	0.0
Net Margin (%)	0.6	-1.5	0.1	1.5	1.6
Gearing (%)	111.1	144.4	107.6	106.1	97.9
Price / Book (x)	1.4	1.5	1.4	1.4	1.3
ROE (%)	0.6	-3.2	0.1	2.5	3.5

Source: Company Data, KGI Research

Event: SMM posted a set of 1Q19 results which did not offer any surprises. Revenues are still on a downward trend (YoY and QoQ) while margins continue to be under pressure. Its balance sheet is still weighed by a net gearing ratio of 1.47x as at end 1Q19, a slight increase from 1.44x as at end 4Q18. New order wins in 1Q19 was lacklustre at only S\$175mn, bringing its net order book to S\$2.66bn (excluding the Sete Brasil orders), down from S\$3.1bn in FY18.

Sete Brasil near resolution. According to media reports, Sete Brasil may be reaching a resolution on the four rigs being constructed by Keppel Corp (KEP SP) and SMM. The tender to sell the rigs received two proposals, one from Magni Partners and the other from KEP. Magni Partners is owned by Tor Olav Troim, the chairman of Borr Drilling. The best-case scenario (which is highly likely given that the rigs have 10-year contracts) is that a deal is concluded in 2H19 and the shipyards (SMM and KEP) complete the construction of the four rigs, but at a cost that will have to be negotiated between the new owners and the yards. Overall, we think the resolution of Sete Brasil would be slightly positive for SMM as it would provide greater certainty on the construction timeline.

Positioning for the future. SMM will realise \$48mn of cost savings per annum when it returns its Tanjong Kling Yard (TKY) by end 2019, four years ahead of schedule. It will consolidate its operations at its Tuas Boulevard Yard (TBY). TBY is currently carrying out significant projects worth around US\$3bn for international offshore firms such as Shell, Transocean and Heerema. As at end Dec-18, SMM had spent more than S\$1.8bn on the yard and has built up automated processes to secure projects higher up the value chain.

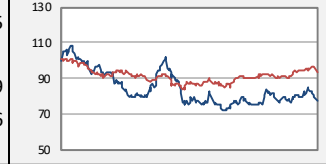
BUY - Maintain

Price as of 6 May 19 (SGD)	1.63	Performance (Absolute)	
12M TP (\$)	2.48	1 Month (%)	-3.6
Previous TP (\$)	2.50	3 Month (%)	5.0
Upside (%)	52.2	12 Month (%)	-22.7

Trading data

Mkt Cap (\$mn)	3,405
Issued Shares (mn)	2,089
Vol - 3M Daily avg (mn)	6.9
Val - 3M Daily avg (\$mn)	11.6
Free Float (%)	37.8%

Perf. vs STI Index (Red)



Major Shareholders

Sembcorp Industries	61.1%
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Previous Recommendations

21-Feb-19	BUY \$2.48
1-Jan-19	BUY \$2.50
7-May-18	BUY \$2.64

Samba time. With 27% of SMM's fixed assets in Brazil, SMM is well-positioned to gain when the oil industry recovers in South America. Already, Rystad Energy reports that final investment decisions (FIDs) for projects over 25mn barrels of oil equivalent (boe) are set to triple YoY in South America in 2019. Brazil is set to lead with 8 projects in 2019 out of a total of 16 FIDs in South America. Globally, the number of project FIDs (>25m boe) has increased from 56 in 2016, to 72 in 2017, 103 in 2018 and is forecasted by Rystad Energy to reach 115 in 2019.

Valuation & Action: Rock-bottom valuations; new order wins to provide catalyst in 2H 2019. We reiterate our BUY recommendation on SMM. SMM's share price has had the highest correlation to oil prices among the Singapore blue-chips but remained relatively resilient when oil prices declined 40% in 4Q18. The resilience can partly be attributed to its 15-year low P/B valuations. Hence with downside mostly mitigated by its rock-bottom valuations, we are of the view that any positive news from new order wins would result in a significant re-rating catalyst.

Low expectations in the short-term. Even with Sete Brasil overhang likely to be out of the way by 2H19, SMM's management has guided for production activity to remain low on the back of intense competition. However, we think that this is already priced into SMM's current share price.

Risks: Cancellations from customers remain the most significant risk. Profit margins may continue to be under pressure as SMM diversifies into new projects.

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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