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# Sembcorp Marine Ltd

(SMM SP/SCMN.SI)

## Looking beyond earnings as corporate actions await

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- SMM reported PATMI losses of S\$78mn in 4Q19 compared to S\$6mn PATMI in 4Q18. FY19 full-year PATMI losses widened to S\$137mn from S\$74mn in FY18.
- The year ahead looks challenging as the company grapples with industry overcapacity, weak margins and a significantly stretched balance sheet.
- Maintain NEUTRAL. We believe earnings are less likely to drive its share price performance going forward. Focus will instead be on the restructuring of Singapore's offshore & marine industry in 2020 and likely involve the privatisation of SMM.

### Financials & Key Operating Statistics

| YE Dec (\$\$ m)   | 2018   | 2019   | 2020F  | 2021F  | 2022F  |
|-------------------|--------|--------|--------|--------|--------|
| Revenue           | 4887.9 | 2882.6 | 2305.4 | 1965.4 | 1693.4 |
| PATMI             | -74.1  | -137.2 | -77.3  | 3.6    | 11.1   |
| Core PATMI        | -74.3  | -137.4 | -77.3  | 3.6    | 11.1   |
| Core EPS          | -3.6   | -6.6   | -3.7   | 0.2    | 0.5    |
| Core EPS grth (%) | na     | na     | na     | na     | na     |
| Core P/E (x)      | na     | na     | na     | 662.4  | 212.8  |
| DPS (SG Cents)    | 0.0    | 0.0    | 0.0    | 0.0    | 0.0    |
| Div Yield (%)     | 0.0    | 0.0    | 0.0    | 0.0    | 0.0    |
| Net Margin (%)    | -1.5   | -4.8   | -3.4   | 0.2    | 0.7    |
| Gearing (%)       | 144.4  | 181.8  | 147.6  | 147.4  | 136.4  |
| Price / Book (x)  | 1.0    | 1.1    | 1.1    | 1.1    | 1.1    |
| ROE (%)           | -3.2   | -6.2   | -3.5   | 0.2    | 0.5    |

Source: Company Data, KGI Research

**Event:** SMM's FY19 performance was a disappointment as it reported a S\$137mn PATMI loss, deepening from the losses of S\$74mn in FY18. This was on the back of a 41% YoY decline in revenues. Net order book declined to S\$2.4bn and is barely equivalent to a year's work. Order wins have been weaker-than-expected, with only S\$1.5bn of new projects secured in FY19. In comparison, Keppel Corp (KEP SP, Outperform, TP S\$7.44) secured S\$2.0bn (+18% YoY from S\$1.7bn in FY18) of new orders in FY19 and had a net orderbook which stood at S\$4.4bn as at end-2019.

**Stretched balance sheet.** SMM's net gearing increased to 1.8x as at end-2019, from 1.4x in the prior-year period, mainly due to higher working capital requirements. It also spent S\$312mn during the year towards capex on its Tuas Boulevard yard. SMM received consent from bondholders to revise the definition of its debt covenant to exclude the S\$1.5bn subordinated loan (from its parent Sembcorp Industries) from SMM's net debt ratio. As a result of the consent, net gearing excluding the subordinated loan would be 1.1x as at end-2019, which is still higher than global peers.

There should not be any concerns on the S\$310mn net current liability position as the group plans to refinance the short-term loans into longer-term maturities. However, it does point out that new projects will require higher working capital and a much stronger balance sheet, a tall order for the group given its current state.

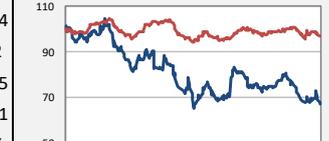
### NEUTRAL - Maintain

|                             |      |                               |       |
|-----------------------------|------|-------------------------------|-------|
| Price as of 27 Feb 20 (SGD) | 1.12 | <b>Performance (Absolute)</b> |       |
| 12M TP (\$)                 | 1.19 | 1 Month (%)                   | -7.4  |
| Previous TP (\$)            | 1.59 | 3 Month (%)                   | -11.6 |
| Upside (%)                  | 6.1  | 12 Month (%)                  | -33.9 |

### Trading data

|                           |       |
|---------------------------|-------|
| Mkt Cap (\$mn)            | 2,364 |
| Issued Shares (mn)        | 2,092 |
| Vol - 3M Daily avg (mn)   | 2.5   |
| Val - 3M Daily avg (\$mn) | 3.1   |
| Free Float (%)            | 37.9% |

### Perf. vs STI Index (Red)



### Major Shareholders

|                     |       |
|---------------------|-------|
| Sembcorp Industries | 61.1% |
|---------------------|-------|

### Previous Recommendations

|           |           |
|-----------|-----------|
| 31-Jul-19 | N \$1.59  |
| 21-Feb-19 | OW \$2.48 |
| 1-Jan-19  | OW \$2.50 |

**It's time for change – restructuring Singapore's offshore & marine industry.** We expect the consolidation of Singapore's offshore & marine industry to finally take shape this year, based on global trends, as well as the need to optimise Singapore's limited resources. We expect SMM's Tuas Boulevard Yard (TBY) - which now takes up 108 hectares and has room to at least double in size - to be Singapore's solution to the next generation of "smart" yard designs. TBY will be able to utilise advanced manufacturing capabilities to shorten development cycles and lead to cost reduction, and therefore be in a stronger position to compete against Chinese and South Korean yards (who have themselves undergone consolidation over the last few years).

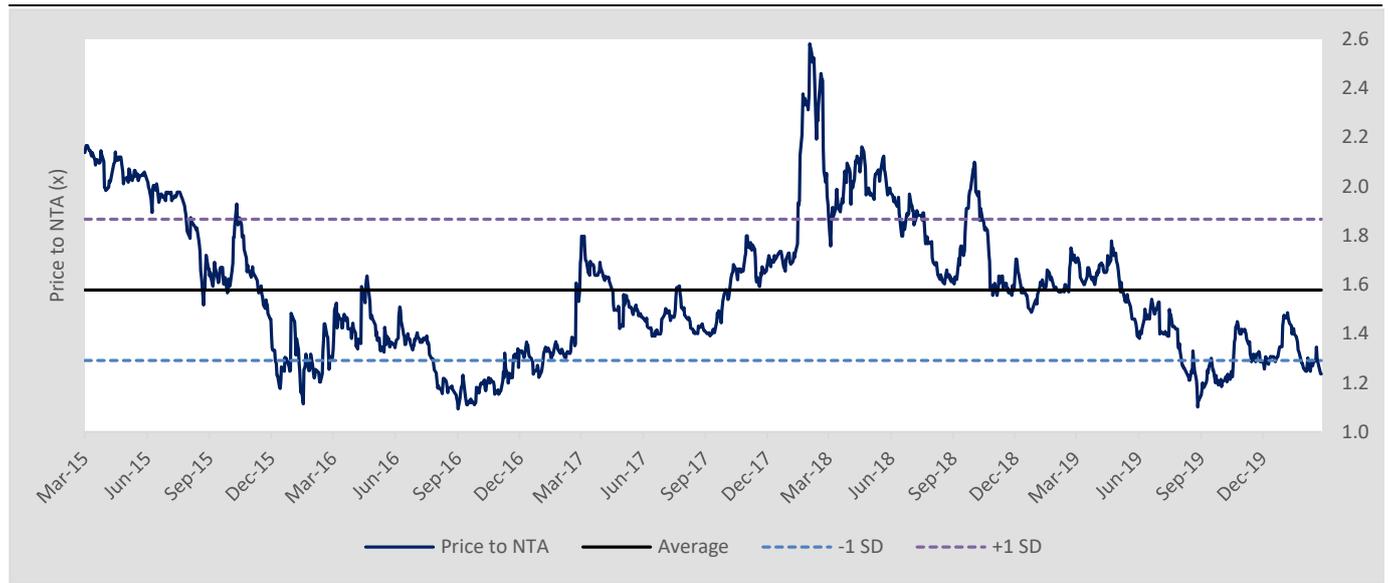
**For a sustainable future.** Out of the S\$1.5bn of new orders SMM secured in FY19, around 33% or S\$0.5bn included work/projects related to sustainability-related solutions. This included scrubber and ballast water management system retrofits, and gas and renewable energy projects. From a macro and long-term perspective, renewable energy investment in the Asia Pacific (ex-China) is forecasted to surpass spending on upstream oil & gas projects in the region by this year, according to Rystad Energy. Asian countries such as China, South Korea, Vietnam and Australia are already leading investments into renewables such as solar energy and wind farms.

**Valuation & Action:** We maintain our NEUTRAL recommendation and lower our fair value to S\$1.19, based on one standard deviation below its 5-year P/NTA average. The group is expected to remain loss-making in FY20F, but attention will likely focus on corporate actions.

**Risks:** Profit margins may continue to be under pressure as SMM diversifies into new projects. Equity rights issue or placement in order to strengthen its balance sheet. Brazil investigations are still ongoing.

## Historical valuations

Figure 1: 5-Years Historical P/NTA



Source: Bloomberg, KGI Research

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| <b>Rating</b>           | <b>Definition</b>   |
|-------------------------|---|
| <b>Outperform (OP)</b>  | We take a positive view on the stock. The stock is expected to outperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.  |
| <b>Neutral (N)</b>      | We take a neutral view on the stock. The stock is expected to perform in line with the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.   |
| <b>Underperform (U)</b> | We take a negative view on the stock. The stock is expected to underperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.  |
| <b>Not Rated (NR)</b>   | The stock is not rated by KGI Securities.   |
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