

MISC Bhd (MISC MK)

Dirty tanker market in the doldrums

Unusual spot rate weaknesses, but BUY maintained

Petroleum tanker spot rates failed to exhibit its usual seasonal strength in 4Q21, but the downside could potentially be limited by the favourable term-to-spot ratio in MISC's fleet. Our earnings forecasts and SOP-based TP of MYR7.75 are maintained at this juncture. MISC currently trades at an attractive 1Y forward PER of 13x (LT mean: 18x; -1SD: 15x), has a robust balance sheet, and offers a solid dividend yield of c.5%. Maintain BUY.

Absence of seasonal strength in petroleum segment

The long-expected winter season pick-up in the dirty tanker market failed to materialise towards the end 4Q21 (see Figs. 1-3) as global Omicron-induced lockdown fears and softer Chinese imports limited tonnage demand. FY21 average spot freight rates for VLCC and Suezmax saw its worst performance in a decade, while Aframax rates also hit an 8y low during the period. Despite an encouraging current orderbook-to-fleet ratio at a manageable c.8-14% for FY22-24, approx. a third of FY22 scheduled tanker deliveries are in the >60K DWT range and thus, likely to offset any significant NT rate increases as the market recovers from multi-year lows.

Downside likely to be mitigated by fleet split

Positively for MISC, its petroleum fleet has a favourable term-to-spot ratio that could provide some support for its 4Q21 performance (we expect the segment to break-even in FY21). MISC's spot charter exposure between its VLCC, Suezmax, Aframax vessels at end-3Q21 stood at 13%, 27%, 46% respectively. As such, notwithstanding a 32.6% MoM decrease in December spot rates for VLCCs (MISC's spot exposure is low), marginal MoM increases in Suezmax (+9.7%) and Aframax (+4.9%) rates could provide the necessary support as MISC's spot exposure in these segments are more substantial.

OPEC+ decision to provide a floor for tanker rates

Noting that MISC performed admirably in 3Q21 despite tepid spot rates in both the LNG/petroleum segments, we expect them to pull through an equally difficult 4Q21 (assuming no negative surprises). With the *Mero 3* FPSO continuing to accrete positively to MISC's bottom-line, coupled with OPEC+'s recent decision to stick by its planned output bumps in light of soaring global oil prices and record-low global crude inventories, we make no changes to our forecasts, pending better visibility post-4Q21 results.

FYE Dec (MYR m)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue	8,963	9,401	11,922	12,360	11,889
EBITDA	3,989	4,009	4,344	5,038	5,404
Core net profit	1,610	2,159	2,103	2,322	2,344
Core EPS (sen)	36.1	48.4	47.1	52.0	52.5
Core EPS growth (%)	24.2	34.1	(2.6)	10.4	0.9
Net DPS (sen)	33.0	33.0	33.0	33.0	33.0
Core P/E (x)	23.2	14.2	14.9	13.5	13.3
P/BV (x)	1.1	1.0	1.0	0.9	0.9
Net dividend yield (%)	4.0	4.8	4.7	4.7	4.7
ROAE (%)	4.1	(0.1)	6.5	7.0	7.0
ROAA (%)	3.1	4.2	3.9	4.0	3.8
EV/EBITDA (x)	11.1	9.5	9.7	8.8	8.6
Net gearing (%) (incl perps)	17.1	19.9	30.0	36.1	40.7
Consensus net profit	-	-	1,832	2,065	2,110
MKE vs. Consensus (%)	-	-	14.8	12.4	11.1

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BUY

Share Price	MYR 7.00
12m Price Target	MYR 7.75 (+15%)
Previous Price Target	MYR 7.75

Company Description

MISC is a leading provider of international energy-related maritime solutions and services.

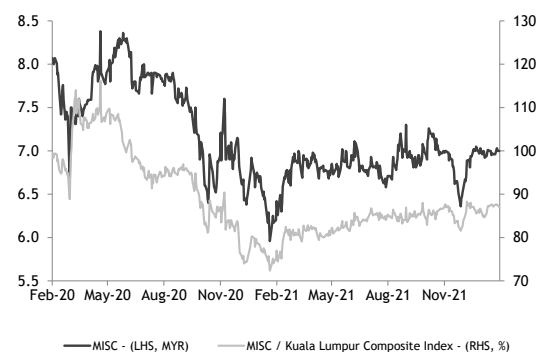
Statistics

52w high/low (MYR)	7.30/6.20
3m avg turnover (USDm)	1.9
Free float (%)	32.7
Issued shares (m)	4,464
Market capitalisation	MYR31.2B USD7.5B

Major shareholders:

Government of Malaysia	51.0%
Employees Provident Fund	12.4%
Permodalan Nasional Bhd.	5.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(0)	0	13
Relative to index (%)	1	1	17

Source: FactSet

Acronyms & Glossary

Aframax - vessel class of c.80-120K DWT capacity
 DWT - deadweight tonnage in metric tonnes (MT)
 FPSO - floating production storage & offloading
 OPEC+ - Organisation of Petroleum Exporting Countries (includes Russia and allies)
 Suezmax - vessel class of c.160K DWT capacity
 VLCC - Very Large Crude Carrier (vessel class of >250K DWT)

LT - long-term
 NT - near-term
 PER - price-earnings ratio
 SD - standard deviation
 SOP - sum-of-parts
 TP - target price

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 Tear Sheet Insert

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Risk Rating & Score ¹	19.1 (Low)
Score Momentum ²	-0.2
Last Updated	30 Nov 2021
Controversy Score ³ (Updated: 09 Dec 2021)	2 - Operations incidents (Emissions)

Business Model & Industry Issues

- MISC is among the world's 5 biggest shipping conglomerates by market capitalisation. It has businesses in energy shipping, offshore floating platform, marine engineering, construction, conversion and repair, as well as port management services.
- The group strictly complies with the various safety, regulatory and environmental standards in all its bases of operations globally. A member of the FTSE4Good Index for 7 consecutive years, it is also one of a few large Malaysian conglomerates that has made sustainability a core ethos, in line with the UN's Sustainable Development Goals (SDGs).
- Although the group has had its fair share of corporate governance issues in the past, it has displayed a resolute commitment towards reducing its environmental impacts and promoting fair labour practises. With an outward-looking management team keen on growing its international business and reducing revenue reliance on its parent (PETRONAS), MISC is well-placed to continue thriving as a global leader in the maritime energy trade.

Material E issues

- In 2017, the group formalised its Carbon Commitment policy to improve the energy efficiency of its fleet and it set clear carbon reduction targets to achieve by 2020, which it has. In 2020, carbon emissions were down 12% from the 2016 baseline while the fleet's SOx/NOx intensity was also down by 88%/8% YoY.
- By 2030, the group aims to replace half of its petroleum tanker fleet with the better energy efficiency tankers, namely the LNG dual-fuel tankers (<10% of fleet now).
- In 2020, c.100% of hazardous waste generated from non-shipping ops were either reused, recycled or recovered.
- The group has had no major spill incidents since 2013.
- In 2019, MISC joined the 'Getting to Zero Coalition' that is closely aligned to the UN IMO's Initial Greenhouse Gas Strategy. The group aims to reduce its GHG emissions by >50% (vs. 2008 levels) by 2050.

Material S issues

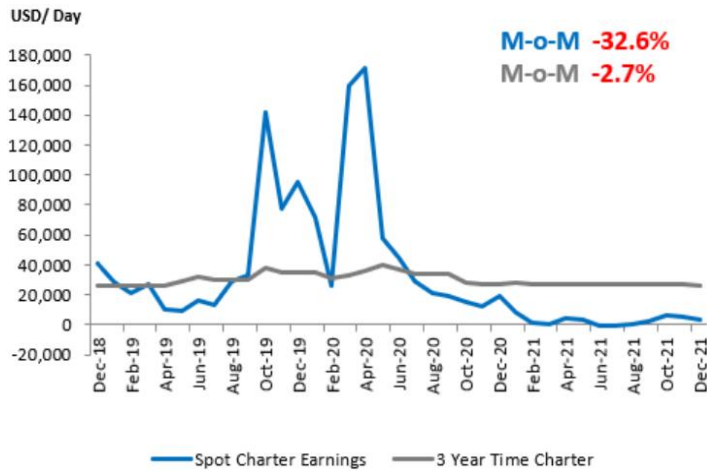
- In FY19, its 8,632-strong workforce consisted of 43 nationalities (66% Malaysian) with 66% of them under the age of 40. Female employment is relatively low at 13% but the group aims to hire more female employees by 2022.
- Management also continuously strives to upskill its workforce. In 2020, it invested MYR47.7m in various functional and leadership competency programmes (8,120 participants across 412 programs).
- Both Lost Time Injury Frequency (LTIF) and Total Recordable Case Frequency reduced to 0.04 (FY19: 0.1) and 0.18 (FY19: 0.26). MISC was also ranked in the industry's top quartile for Occupational Health & Safety (OSH) standards by INTERTANKO.
- The group has a zero tolerance policy towards workplace discrimination and harassment. There is also a Whistleblowing Policy in place.
- In 2020, MISC contributed c.MYR7.5 million for the COVID-19 national pandemic response and COVID-19 related aids.

Key G metrics and issues

- PETRONAS is the group's largest shareholder, with its latest controlling shareholding at 51%.
- Out of the total 12 Board members, 9 are independent directors (IDs), representing 75% of the Board. FY20 has been a turbulent year for the group's leadership which saw the independent chairman stepping down and subsequently replaced by a non-independent political appointee. Following intervention from the PM's Office, the latter resigned after just 17 days in office. This was followed by the resignation of a non-independent director and the appointment of 3 new IDs, one of whom was appointed Chairman on 10th Dec.
- Female representation on the Board is now 33% (a Malaysian Code on Corporate Governance or MCGG best practise) with 4 of the 12 members being women. This is also in line with PETRONAS' board diversity policy.
- Average tenure among the independent Board members is 4.8 years (longest-serving at 10.5 years and shortest at 1.3 months). The Board has adopted a formal policy of limiting the tenure of its IDs to 9 years and although the longest serving ID has been in his role for collectively more than 10 years, this was across 2 stints (5.7 & 4.8 years respectively) over a 17.2-year period.
- The position of Non-Executive Chairman and Group President (CEO) are held by different individuals.
- All three Board committees (audit, nomination & remuneration, governance & risk) are chaired by and comprised of an independent majority.
- Total directors' remuneration is low at 0.1% of FY20 group core net profit (FY19: 0.13%).
- Ernst & Young has been the group's external auditor for 18 years.
- Owing to PETRONAS being the group's parent and key customer, there are significant related party transactions (RPTs). In FY19, c.35% of MISC's revenue was derived from such related parties - however, this share could fall in the coming years as external contracts (secured in FY19-20) would contribute more meaningfully from FY22E.
- In 2018, four senior employees were investigated by MACC for corruption, but no charges were pressed.

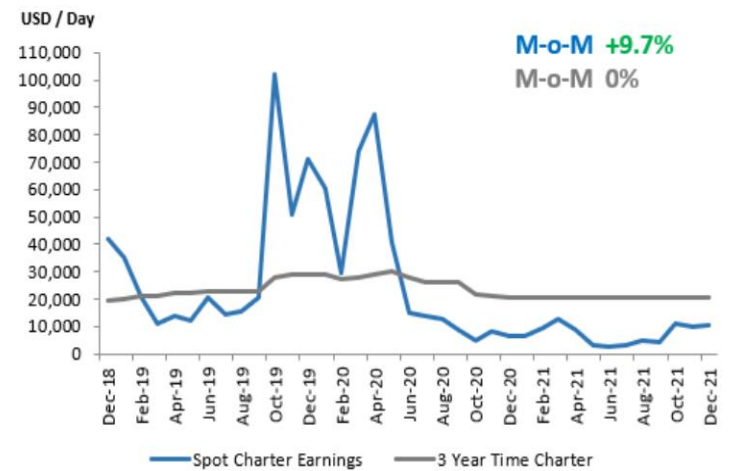
¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Figure 1: VLCC Tanker Rates (as of 31 Dec 2021)



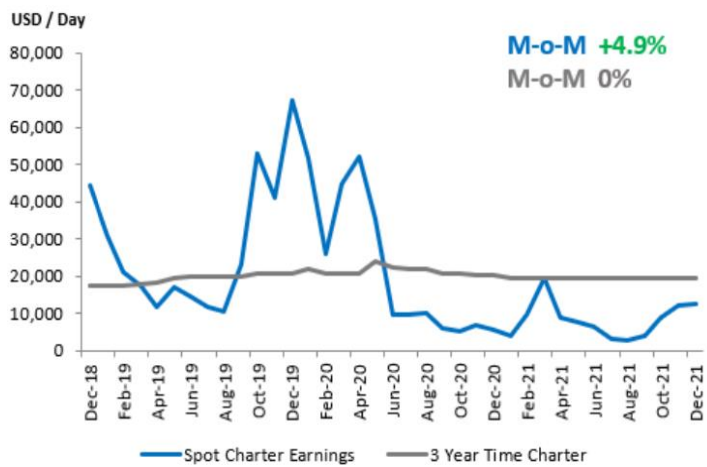
Source: Company data, Clarksons

Figure 2: Suezmax Tanker Rates (as of 31 Dec 2021)



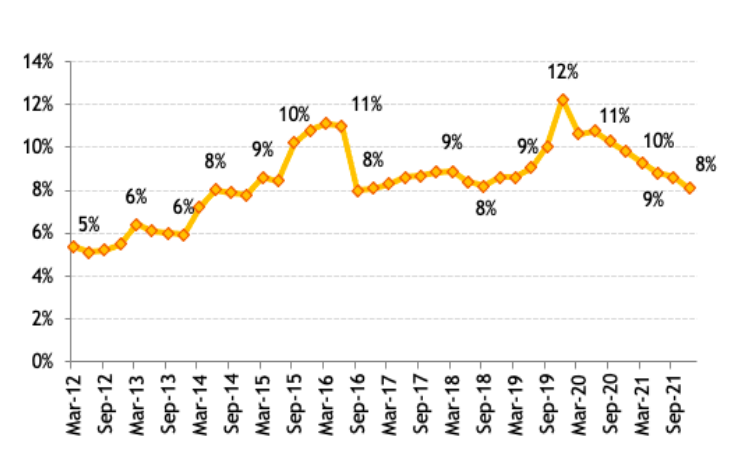
Source: Company data, Clarksons

Figure 3: Aframax Tanker Rates (as of 31 Dec 2021)



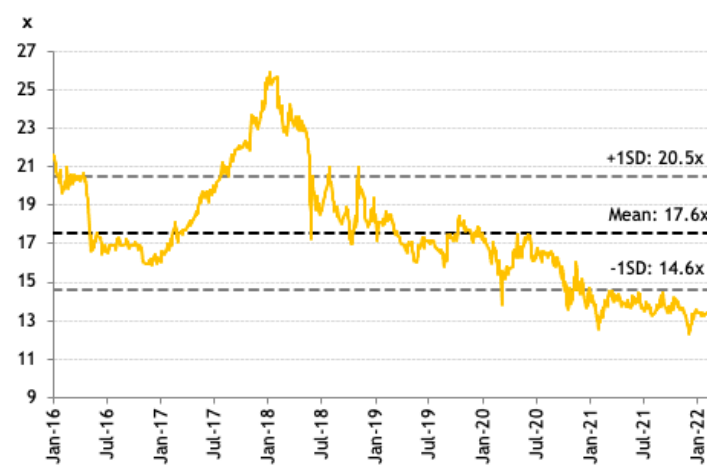
Source: Company data, Clarksons

Figure 4: MISC's foreign shareholding (end-Dec 2021: 8%)



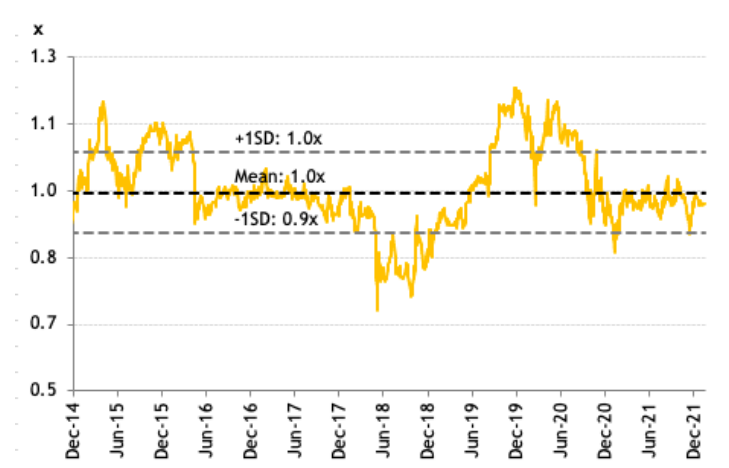
Source: Company data, Maybank IBG (compilation)

Figure 5: MISC's 12M rolling fwd PER (currently trades at 13x)



Source: Bloomberg, Maybank IBG (compilation)

Figure 6: MISC's 12M rolling fwd PBV (currently trades at 0.9x)



Source: Bloomberg, Maybank IBG (compilation)

Risk statement

There are several risk factors affecting our earnings estimates, target price and rating for MISC. Abrupt changes in the momentum of petroleum tanker rates and bunker prices may lead to lower earnings for MISC. The reimposition of global economic lockdowns as a result of new Covid-19 virus strains and abrupt changes in OPEC+ policy could also result in near-term earnings volatility for MISC. Additionally, sharp appreciation of MYR vis-a-vis USD will also affect its earnings, as the group's revenue is almost entirely derived in USD. Lastly, disruptive *force majeure* events in relation to the construction of the *Mero 3* FPSO could also pose a drag on MISC's earnings.

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Metrics					
P/E (reported) (x)	22.9	nm	14.9	13.5	13.3
Core P/E (x)	23.2	14.2	14.9	13.5	13.3
P/BV (x)	1.1	1.0	1.0	0.9	0.9
P/NTA (x)	2.6	1.6	1.4	1.1	1.0
Net dividend yield (%)	4.0	4.8	4.7	4.7	4.7
FCF yield (%)	9.2	1.6	nm	nm	0.3
EV/EBITDA (x)	11.1	9.5	9.7	8.8	8.6
EV/EBIT (x)	25.2	20.0	18.9	17.0	16.8
INCOME STATEMENT (MYR m)					
Revenue	8,962.7	9,401.2	11,922.4	12,359.9	11,888.6
EBITDA	3,989.3	4,009.0	4,344.3	5,038.1	5,403.7
Depreciation	(2,215.5)	(2,091.0)	(2,092.0)	(2,397.9)	(2,631.4)
Amortisation	(13.8)	(13.3)	(13.3)	(13.3)	(13.3)
EBIT	1,760.0	1,904.7	2,239.0	2,626.9	2,759.0
Net interest income / (exp)	(315.1)	(255.5)	(339.0)	(448.1)	(521.7)
Associates & JV	250.6	429.0	386.1	347.5	312.7
Exceptionals	(183.2)	(2,201.8)	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	1,512.3	(123.6)	2,286.1	2,526.2	2,550.1
Income tax	(76.1)	(46.2)	(160.0)	(176.8)	(178.5)
Minorities	(9.9)	126.8	0.0	0.0	0.0
Discontinued operations	0.0	0.0	68.6	0.0	0.0
Reported net profit	1,426.3	(43.0)	2,102.8	2,322.5	2,344.0
Core net profit	1,609.5	2,158.8	2,102.8	2,322.5	2,344.0
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	7,030.8	6,855.0	6,860.7	6,971.9	6,983.5
Accounts receivable	2,441.2	3,956.6	5,017.7	5,201.8	5,003.4
Inventory	165.7	91.3	115.8	120.0	115.5
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	23,287.2	23,309.2	26,717.2	29,319.4	31,688.0
Intangible assets	840.7	819.2	805.9	792.6	779.3
Investment in Associates & JVs	926.2	873.8	1,259.9	1,607.4	1,920.1
Other assets	17,172.0	15,915.9	15,915.9	15,915.9	15,915.9
Total assets	51,863.8	51,821.0	56,693.1	59,929.0	62,405.7
ST interest bearing debt	5,599.5	2,005.5	2,005.5	2,005.5	2,005.5
Accounts payable	2,109.3	3,427.3	4,346.4	4,505.9	4,334.1
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	7,552.7	11,434.9	14,934.9	17,334.9	19,234.9
Other liabilities	848.0	1,802.0	1,802.0	1,802.0	1,802.0
Total Liabilities	16,110.0	18,669.7	23,088.8	25,648.3	27,376.5
Shareholders Equity	34,727.2	32,273.0	32,702.7	33,352.2	34,073.1
Minority Interest	1,026.6	878.3	901.5	928.5	956.0
Total shareholder equity	35,753.8	33,151.3	33,604.3	34,280.6	35,029.2
Total liabilities and equity	51,863.8	51,821.0	56,693.1	59,929.0	62,405.7
CASH FLOW (MYR m)					
Pretax profit	1,512.3	(123.6)	2,286.1	2,526.2	2,550.1
Adj net interest (income)/exp	315.1	255.5	339.0	448.1	521.7
Change in working capital	1,560.3	1,559.8	(166.4)	(28.9)	31.1
Cash taxes paid	(47.5)	(62.0)	(160.0)	(176.8)	(178.5)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	5,579.1	5,587.9	3,817.8	4,632.3	5,106.4
Capex	(2,161.0)	(5,108.3)	(5,500.0)	(5,000.0)	(5,000.0)
Free cash flow	3,418.1	479.6	(1,682.2)	(367.7)	106.4
Dividends paid	(1,342.1)	(1,476.0)	(1,473.1)	(1,473.1)	(1,473.1)
Change in Debt	(1,937.8)	502.1	3,500.0	2,400.0	1,900.0
Other invest/financing cash flow	135.2	375.5	(339.0)	(448.1)	(521.7)
Net cash flow	273.4	(118.8)	5.7	111.1	11.6

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Ratios					
Growth ratios (%)					
Revenue growth	2.1	4.9	26.8	3.7	(3.8)
EBITDA growth	22.1	0.5	8.4	16.0	7.3
EBIT growth	27.9	8.2	17.6	17.3	5.0
Pretax growth	12.5	nm	nm	10.5	0.9
Reported net profit growth	8.8	nm	nm	10.4	0.9
Core net profit growth	24.2	34.1	(2.6)	10.4	0.9
Profitability ratios (%)					
EBITDA margin	44.5	42.6	36.4	40.8	45.5
EBIT margin	19.6	20.3	18.8	21.3	23.2
Pretax profit margin	16.9	nm	19.2	20.4	21.4
Payout ratio	103.3	nm	70.1	63.4	62.8
DuPont analysis					
Net profit margin (%)	15.9	nm	17.6	18.8	19.7
Revenue/Assets (x)	0.2	0.2	0.2	0.2	0.2
Assets/Equity (x)	1.5	1.6	1.7	1.8	1.8
ROAE (%)	4.1	(0.1)	6.5	7.0	7.0
ROAA (%)	3.1	4.2	3.9	4.0	3.8
Liquidity & Efficiency					
Cash conversion cycle	(61.5)	(92.7)	(67.3)	(91.3)	(121.0)
Days receivable outstanding	100.4	122.5	135.5	148.8	154.5
Days inventory outstanding	18.8	10.5	5.6	6.6	7.5
Days payables outstanding	180.6	225.6	208.4	246.7	283.0
Dividend cover (x)	1.0	(0.0)	1.4	1.6	1.6
Current ratio (x)	1.4	2.2	2.1	2.1	2.1
Leverage & Expense Analysis					
Asset/Liability (x)	3.2	2.8	2.5	2.3	2.3
Net gearing (%) (incl perps)	17.1	19.9	30.0	36.1	40.7
Net gearing (%) (excl. perps)	17.1	19.9	30.0	36.1	40.7
Net interest cover (x)	5.6	7.5	6.6	5.9	5.3
Debt/EBITDA (x)	3.3	3.4	3.9	3.8	3.9
Capex/revenue (%)	24.1	54.3	46.1	40.5	42.1
Net debt/ (net cash)	6,121.4	6,585.4	10,079.7	12,368.5	14,256.9

Source: Company; Maybank

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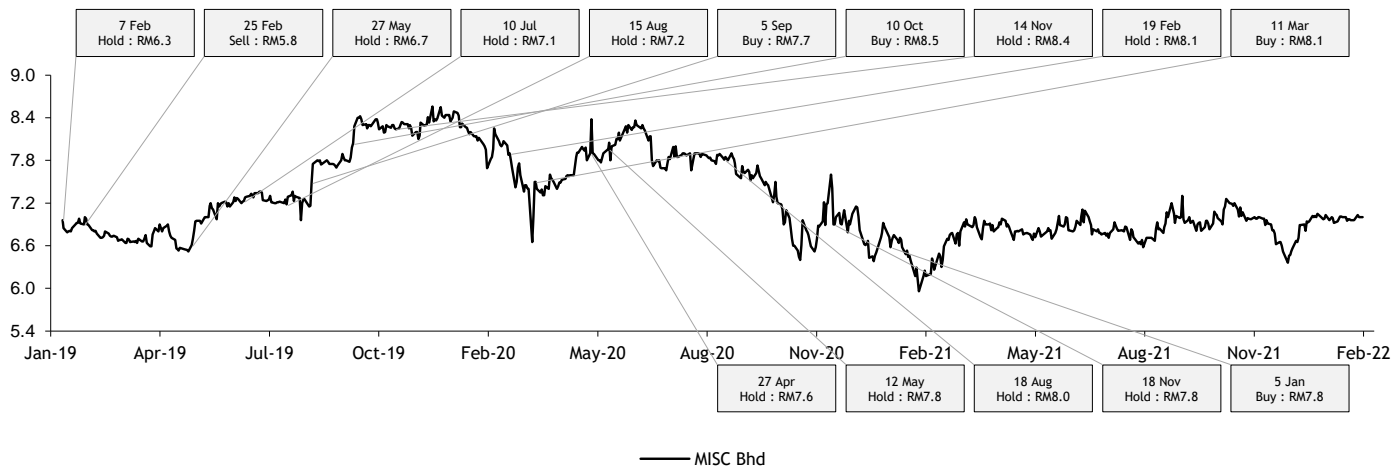
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