

### COMPANY UPDATE

#### MISC (MISC MK)

Small Trading Upside On Tanker Market Recalibration

The recalibration of crude flows due to recent geopolitical events and the expected return of Iranian and Venezuela crudes in the medium term may offer some support on a gradual tanker recovery. We raise forecasts by 5% and expect trading upside as MISC's petroleum fleet may be a beneficiary. Global bonds are expected to support capex and refinancing, while MISC had enhanced decarbonisation targets and greenhouse gas disclosure. Maintain HOLD with a higher target price of RM7.15.

#### WHAT'S NEW

- Geopolitical events may support certain segments of tanker earnings.** The sanctions arising from the Russia-Ukraine conflict is expected to impact most of the 3.2m bpd of Russian crude exports that travel by sea. While tanker markets may take months to recalibrate the trade routes, the rush for energy security especially from crude importers like Europe, have pushed up US crude demand to substitute for sanctioned Russian cargoes. Very Large Crude Carriers' (VLCC) earnings have improved but still incur losses on spot routes; however the smaller Aframax and Suezmax segments exposed to the US Gulf routes benefitted the most from this. Aframax spot rates in those longer-haul routes were last heard to have improved significantly to US\$37,000-47,000 per day.
- We turned slightly more positive given MISC's dominant exposure in Aframax fleet.** MISC operates 28 Aframax (out of 59 for petroleum) and most of the Aframax serve in the US Gulf region. Even though the spike on tanker rates due to Russia sanction may be short-lived, an early return of Iranian and Venezuela crude barrels may further support tanker demand. Still, industry tanker recovery will remain gradual for 2022. This comes amid higher bunker fuel costs, and potential oil demand disruptions from China's COVID-19 lockdowns and higher inflation pressures.
- Key updates from 2021 Annual Report (AR).** As per guidance in MISC's 4Q21 briefing, approximately 83%/72% of MISC's long-term/total borrowings of RM8.7b/RM17.0b in 2021 are of fixed rates. The AR also revealed that a RM3.0b term loan was reclassified to current liability as certain conditions were not fulfilled. This is the outstanding loan for a significant local offshore platform that started the 25-year charter since Oct 14. The condition requires "quiet enjoyment consent" from the client, and this was impacted by the ongoing litigation with the client on cost disputes that started since 2016.
- We understand this is not a financial covenant default** even though accounting standards mandate the change. The client continues to pay the charter, given that the field's production remains healthy, while a Phase 3 expansion on the field is also underway. A key risk however, is that the banks may choose to exit the financing. Channel checks suggest that such conditions are typical for long-term charters (including FPSO).

#### KEY FINANCIALS

Year to 31 Dec (RMm)	2020	2021	2022F	2023F	2024F
Net turnover	9,401	10,672	8,850	9,228	9,513
EBITDA	4,108	3,898	3,907	4,300	4,474
Operating profit	2,017	1,948	1,794	1,999	1,986
Net profit (rep./act.)	(43)	1,831	1,552	1,733	1,846
Net profit (adj.)	1,802	1,319	1,552	1,733	1,846
EPS (sen)	40.4	29.6	34.8	38.8	41.4
PE (x)	18.2	24.9	21.1	18.9	17.8
P/B (x)	1.0	1.0	1.0	0.9	0.9
EV/EBITDA (x)	11.1	11.7	11.7	10.6	10.2
Dividend yield (%)	4.5	4.5	4.1	4.1	4.1
Net margin (%)	(0.5)	17.2	17.5	18.8	19.4
Net debt/(cash) to equity (%)	20.4	26.6	35.2	20.9	31.4
Interest cover (x)	11.2	9.3	7.7	9.3	10.1
ROE (%)	n.a.	5.5	4.5	5.0	5.3
Consensus net profit	-	-	1,942	2,063	2,155
UOBKH/Consensus (x)	-	-	0.80	0.84	0.86

Source: MISC, Bloomberg, UOB Kay Hian

\*Note: Our forecasts exclude finance lease construction gains, which may differ from consensus estimates

### HOLD

(Maintained)

Share Price	RM7.35
Target Price	RM7.15
Upside	-2.7%
(Previous TP)	RM6.75

#### COMPANY DESCRIPTION

Shipping Company

#### STOCK DATA

GICS sector	Industrials
Bloomberg ticker:	MISC MK
Shares issued (m):	4,463.7
Market cap (RMm):	32,808.5
Market cap (US\$m):	7,788.9
3-mth avg daily t'over (US\$m):	3.1

#### Price Performance (%)

52-week high/low RM7.38/RM6.36

1mth	3mth	6mth	1yr	YTD
0.7	4.3	7.6	6.7	4.3

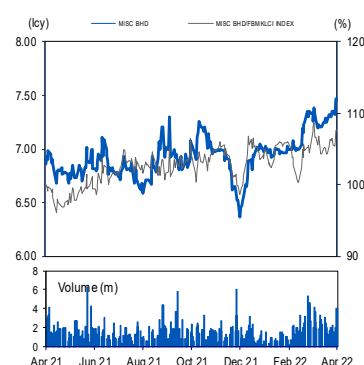
#### Major Shareholders

	%
Petroleum Nasional Bhd	51.1
Employees Provident Fund	12.4

FY22 NAV/Share (RM) 7.70

FY22 Net Debt/Share (RM) 2.71

#### PRICE CHART



Source: Bloomberg

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- **We assume a small financial risk on the project**, even if the litigation prolongs. As mentioned, repayment remains uninterrupted, and this can be observed as the loan has been reduced from the initial amount of US\$1.1b (RM4.7b) in 2015. In the event that the financiers choose to “exit”, MISC stated it has available options to refinance the RM3b loan. Recently, its subsidiary MISC Capital Two Labuan issued US\$1b bonds into the market, split into a three-year US\$400m and a five-year US\$600m respectively.
- **This is the first drawdown from a US\$3b unsecured global bond programme**, intended for capex and refinancing of existing loans, which we think may include the bridging loan of FPSO Mero-3. Assuming none of the bonds are used for refinancing/retained as cash, the secured debt portion from 76% in 2021 may drop to 58% (according to Moody’s), and net gearing may surge to 39% at our 2022 forecast. We largely expect peak gearing in 2022 as Mero-3 approaches the tail-end of construction, before a target divestment to potential equity partners (to 50% stake) by 2023.
- **Stepped up on ESG roadmap.** Its 2021 sustainability report estimates an emission reduction pathway to involve: a) 42% from liquefied natural gas (LNG) and petroleum shipping, via fleet renewal plans and carbon removal technology, b) 46% from offshore platforms with low-carbon emission and higher renewable energy, and c) 12% from “offset” via nature-based solutions (like mangrove rehabilitation). Although the fleet renewal plan is not mentioned, >30% of MISC’s fleet may approach 15 years old and may not comply with tougher green shipping regulations. It is expanding emission reporting from just assets within operational control (previously no disclosure from offshore division). The new disclosure is more detailed, including indirect (Scope 3) emissions to cover for assets that are: a) in-chartered or leased to other parties, b) of minority ownership, and c) of short-term leases.

### EARNINGS REVISION/RISK

- **Increased 2022-24 earnings by 4-5%**, after slight upgrades in average tanker rates and adjustments to offshore earnings. We expect small losses in petroleum for 2022, followed by a stronger recovery from 2023, assuming tightening global tanker tonnage as older vessels which are unable to comply with green shipping regulations will likely be retired.

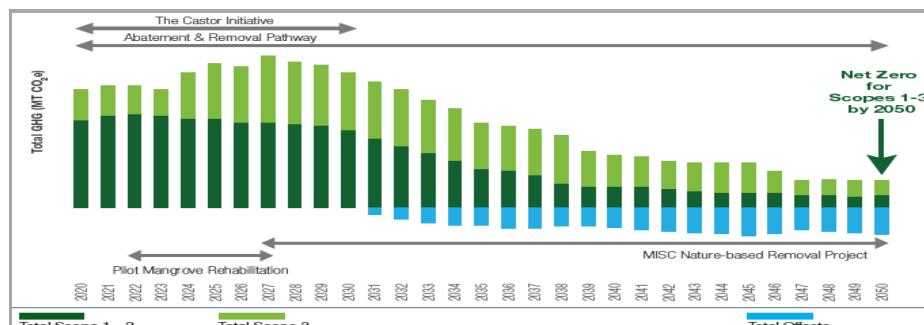
### VALUATION/RECOMMENDATION

- **Maintain HOLD, raise target price to RM7.15 (from RM6.75)**, implying 21x 2022F PE (at +1SD of five-year average PE band). We raised per-share petroleum valuation from RM1.21 following higher P/B from 0.7x, partly offset by higher net debt (LNG loans increased yoy from RM3b to RM5b). Offshore equity increased yoy, though offset by a 15% discount on Gumusut due to litigation uncertainties. EBITDA and dividends are expected to be stable. Despite retaining HOLD, we see a possible trading upside to RM7.75 (which assumes petroleum P/B re-rating to 1x) if near-term crude tanker rates continue to be strong.

### ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG) UPDATES

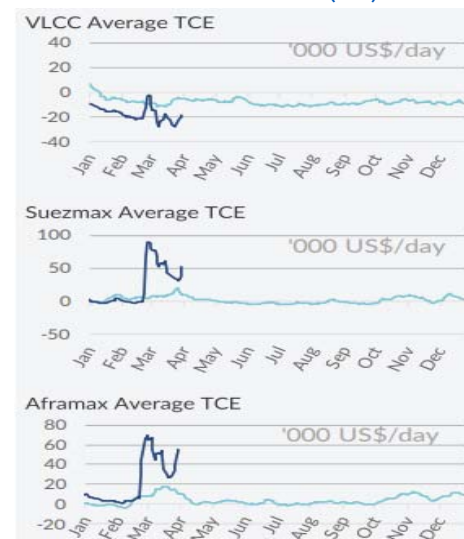
<ul style="list-style-type: none"> <li>• <b>Environmental</b> <ul style="list-style-type: none"> <li>- <b>Carbon (CO2) reduction.</b> Adding new vessels with LNG-dual/ammonia fuel to meet net-zero emission by 2050 (50% reduction of greenhouse gas by 2030)</li> <li>- <b>Promoting circular economy via green ship recycling.</b> Aims to avoid wastage while disposing of aged vessels that do not meet carbon reduction criteria</li> </ul> </li> <li>• <b>Social</b> <ul style="list-style-type: none"> <li>- <b>Diversity.</b> &gt;20 nationalities; &gt;40% female proportion among onshore staff</li> <li>- <b>Safety (HSE).</b> Lost Time Injury Frequency remains low at 0.15 (2020: 0.04)</li> </ul> </li> <li>• <b>Governance</b> <ul style="list-style-type: none"> <li>- <b>Achieved 5/5 rating (FTSE4Good)</b> for governance &amp; supply chain management</li> </ul> </li> </ul>
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### NET ZERO CARBON EMISSION PATHWAY



Source: MISC

### CRUDE TANKER SPOT EARNINGS (TCE)



Note: Dark blue line - YTD 2022; Light blue line - 2021  
Source: Allied Shipping Research

### SEGMENTAL FORECASTS

(RMm)	2022F	2023F	2024F
<b>Revenue</b>	8,850.1	9,228.5	9,512.8
LNG	2,788.8	2,567.7	2,463.0
Petroleum	3,407.1	4,069.3	4,333.4
MMHE	1,501.0	1,490.0	1,670.0
Offshore	1,153.3	1,101.4	1,046.5
<b>EBIT</b>	1,794.0	1,999.4	1,985.5
LNG	1,422.3	1,232.5	1,182.2
Petroleum	(37.5)	255.0	336.4
MMHE	(144.3)	(16.8)	(35.4)
Offshore	553.6	528.7	502.3

Source: UOB Kay Hian

### SOTP BREAKDOWN (AT RM4.1/US\$)

Segments	Valuation	RM/share
LNG	DCF, 6.5% WACC	3.53
Petroleum	0.8x P/B (from 0.7x)	1.64
MMHE (66.5%)	Based on RM0.46 TP	0.09
Gumusut	0.85x P/B (from 1x)	1.25
Kikeh (51%)	1x P/B	0.19
Other offshore	0.9x P/B	0.23
(-) Net debt	LNG (RM5b); others (<RM2b)	(0.68)
(+) New contracts	Higher potential contracts from FPSO, LNG or DPST	0.90
<b>SOTP</b>	21x 2022F PE, 4% yield	7.15

Source: Bloomberg, UOB Kay Hian

### ABSOLUTE EMISSION PATHWAY TO 2050, VS BUSINESS AS USUAL



Source: MISC

### PROFIT & LOSS

Year to 31 Dec (RMm)	2021	2022F	2023F	2024F
Net turnover	10,672	8,850	9,228	9,513
EBITDA	3,898	3,907	4,300	4,474
Deprec. & amort.	1,949	2,113	2,301	2,489
EBIT	1,948	1,794	1,999	1,986
Total other non-operating income	512	n.a.	n.a.	n.a.
Associate contributions	301	286	272	379
Net interest income/(expense)	(417)	(506)	(462)	(444)
<b>Pre-tax profit</b>	<b>1,775</b>	<b>1,574</b>	<b>1,809</b>	<b>1,920</b>
Tax	(41)	(71)	(81)	(86)
Minorities	98	48	6	12
<b>Net profit</b>	<b>1,831</b>	<b>1,552</b>	<b>1,733</b>	<b>1,846</b>
Net profit (adj.)	1,319	1,552	1,733	1,846

### CASH FLOW

Year to 31 Dec (RMm)	2021	2022F	2023F	2024F
<b>Operating</b>	<b>2,909</b>	<b>3,836</b>	<b>4,219</b>	<b>4,388</b>
Pre-tax profit	1,775	1,574	1,809	1,920
Tax	(989)	(71)	(81)	(86)
Other operating cashflows	2,123	2,332	2,491	2,554
<b>Investing</b>	<b>(3,135)</b>	<b>(3,718)</b>	<b>(718)</b>	<b>(3,718)</b>
Capex (growth)	(3,775)	(4,358)	(4,358)	(4,358)
Others	640	640	3,640	640
<b>Financing</b>	<b>1,499</b>	<b>(979)</b>	<b>(4,465)</b>	<b>(979)</b>
Others/interest paid	1,499	(979)	(4,465)	(979)
<b>Net cash inflow (outflow)</b>	<b>1,272</b>	<b>(861)</b>	<b>(964)</b>	<b>(309)</b>
<b>Beginning cash &amp; cash equivalent</b>	<b>6,855</b>	<b>7,952</b>	<b>7,093</b>	<b>6,130</b>
Changes due to forex impact	(175)	1	1	1
<b>Ending cash &amp; cash equivalent</b>	<b>7,952</b>	<b>7,093</b>	<b>6,130</b>	<b>5,822</b>

### BALANCE SHEET

Year to 31 Dec (RMm)	2021	2022F	2023F	2024F
Fixed assets	23,386	25,565	27,744	29,923
Other LT assets	21,294	21,271	14,455	16,485
Cash/ST investment	7,952	7,093	6,130	5,822
Other current assets	4,889	4,287	4,458	4,593
<b>Total assets</b>	<b>57,521</b>	<b>58,216</b>	<b>52,787</b>	<b>56,823</b>
ST debt	8,309	9,905	7,000	2,905
Other current liabilities	4,118	2,472	2,464	2,519
LT debt	8,720	9,301	6,396	13,977
Other LT liabilities	1,449	1,449	1,449	1,449
Shareholders' equity	34,163	34,375	34,770	35,276
Minority interest	762	714	708	696
<b>Total liabilities &amp; equity</b>	<b>57,521</b>	<b>58,216</b>	<b>52,787</b>	<b>56,823</b>

### KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Profitability</b>				
EBITDA margin	36.5	44.1	46.6	47.0
Pre-tax margin	16.6	17.8	19.6	20.2
Net margin	17.2	17.5	18.8	19.4
ROA	3.3	2.7	3.1	3.4
ROE	5.5	4.5	5.0	5.3
<b>Growth</b>				
Turnover	13.5	(17.1)	4.3	3.1
EBITDA	(5.1)	0.2	10.1	4.1
Pre-tax profit	n.a.	(11.3)	14.9	6.1
Net profit	n.a.	(15.3)	11.7	6.5
Net profit (adj.)	(26.8)	17.6	11.7	6.5
EPS	(26.8)	17.6	11.7	6.5
<b>Leverage</b>				
Debt to total capital	32.8	35.4	27.4	31.9
Debt to equity	49.8	55.9	38.5	47.9
Net debt/(cash) to equity	26.6	35.2	20.9	31.4
Interest cover (x)	9.3	7.7	9.3	10.1

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