

Keppel Corporation

De-risking inventory and deleveraging Keppel O&M

SINGAPORE | CONGLOMERATE | UPDATE

13 October 2022

- Keppel Corporation (Keppel) has entered into an amended and restated framework deed with Borr Drilling (Borr). Keppel Offshore & Marine (KOM) will accelerate the delivery of three yet-to-be delivered jackup rigs to Borr between October 2022 and July 2023.
- Resolution for the five rigs will de-risk KOM's inventory and deleverage KOM. All three jackup rigs will be delivered with full payments on delivery, amounting to at least US\$352mn, out of which at least US\$158mn will be payable in 2022.
- KOM secured repeat newbuild Floating Production, Storage and Offloading vessel (FPSO), for about US\$2.8bn, which brings its new orderbook to about S\$11.8bn. We believe latest contract win enhances proposition of KOM-Sembcorp Marine (SMM) merger.
- Maintain BUY with unchanged SOTP TP of \$8.95.** We valued the Group based on the four new segments unveiled during Vision 2030 to better reflect the Group's reporting segments going forward. Our TP translates to about 1.2x FY22e book value, a slight premium to its historical average as the Group's transformation plans gain traction and ROE expands to 8.8%. Catalysts expected from approvals obtained for the transaction.

The news

Keppel has entered into an amended and restated framework deed with Borr. Under the new framework deed, KOM will accelerate the delivery of three yet-to-be delivered jackup rigs to Borr between October 2022 and July 2023. There are five rigs that have not been delivered yet.

The five rigs form part of the identified assets that are slated to be transferred to RigCo as part of the agreements in connection with the proposed combination of KOM and SMM. The deliveries of the remaining two rigs will be deferred to 2025 in which Borr will pay holding costs and cost cover in respect of the deferred deliveries.

Positives

+ Resolution for five rigs will de-risk KOM's inventory and deleverage KOM. Keppel will receive cash payments earlier, which will reduce its overall financial exposure to Borr. All three jackup rigs will be delivered with full payments (including holding costs and cost cover) on delivery, amounting to at least US\$352mn, out of which at least US\$158mn will be payable in 2022. The new resolution will enable KOM to receive full payments for the three rigs faster, improve its cash flows, reduce counterparty risk and provide a resolution to its legacy rigs. The sale proceeds will be transferred to Asset Co upon completion of the combination, in line with the framework agreement.

+ No impairment will be recorded for third deferral of two of the five undelivered jackup rigs. The remaining two of the five undelivered jackup rigs will have their scheduled deliveries to Borr deferred to 2025. Recall that KOM and Borr had previously agreed on the deferral of the delivery of these five jackup rigs twice. Borr will pay holding costs and cost cover in respect of the deferred deliveries.

+ KOM secured repeat newbuild FPSO contract P-83 worth US\$2.8bn from Petrobras, net orderbook rise to ~\$11.8bn. The P-83 scheduled for delivery in 1H27, is a repeat order of the P-80 FPSO that KOM secured in August this year. The P-83 and P-80 is a larger FPSO compared to the P-78, which was awarded in May 2021. The P-83 and P-80 has a larger production capacity of 225,000 barrels of oil per day (bopd) vs. the P-78's 180,000 bopd.

We believe the latest contract win will enhance the proposition of the KOM-SMM merger as the orderbook under KOM will all be subsumed under the new entity – Bayberry.

BUY (Maintained)

LAST CLOSE PRICE	SGD 6.810
FORECAST DIV	SGD 0.330
TARGET PRICE	SGD 8.950
TOTAL RETURN	36.3%

COMPANY DATA

BLOOMBERG CODE:	KEP SP
O/S SHARES (MN) :	1,752
MARKET CAP (USD mn / SGD mn) :	8307 / 11931
52 - WK HI/LO (SGD) :	7.54 / 5.04
3M Average Daily T/O (mn) :	3.67

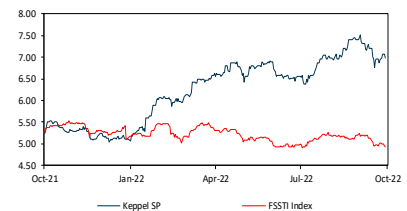
MAJOR SHAREHOLDERS (%)

TEMASEK HOLDINGS	21.0%
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PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	(6.1)	8.4	38.8
STI RETURN	(4.8)	0.6	3.8

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec (\$\$, 'mn)	FY20	FY21	FY22e	FY23e
Revenue	6,574	8,625	9,898	8,449
EBIT	37	1,009	1,206	1,148
NPAT	(508)	1,010	1,204	1,151
Dividend yield	1.3%	4.8%	5.4%	5.1%
P/NAV (x)	1.1	1.0	1.0	0.9
P/E (x)	(24.5)	12.1	10.3	10.7
ROE (%)	-4.5%	8.6%	9.5%	8.7%

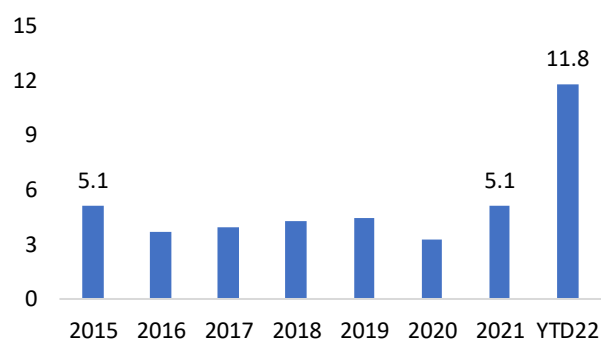
Source: Company, PSR

VALUATION METHOD

SOTP valuation

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Figure 1: KOM order book boosted by FPSO contracts



Source: Company data, PSR

Outlook

Preparations to complete the proposed O&M transactions are progressing well. Management is hopeful about meeting the time line for completion. KOM is showing encouraging progress with its legacy rigs, which are expected to be substantially monetised over the next three to five years.

We continue to monitor the approval of the combined entity, and outcome of the remaining 10% of the combined entity shares which will be deposited into a segregated account for certain identified contingent liabilities and its plans for the \$500mn cash.

We will provide updates of these developments as they come along.

ESG

Keppel Corp has the highest triple-A rating MSCI ESG ratings. It has held the triple-A rating since February 2020. Keppel is ranked among the top 8% of global industrial conglomerates, based on ESG criteria, in the MSCI All Country World Index.

Keppel has been recognised by Corporate Knight's Clean 200, as one of the companies leading the way in the transition to a cleaner energy future. We view its Vision 2030 plan to reach 7GW of renewable energy positively as it should lead to better profitability over time.

Maintain BUY with unchanged SOTP target price of \$8.95

We maintain our BUY recommendation with an unchanged SOTP TP of \$8.95. We valued the Group based on its four new segments unveiled during Vision 2030 to better reflect the Group's reporting segments. For its Energy & Environment business, we valued its O&M division at 0.8x book value but crank up the realisable value of its rigs. Keppel Infrastructure Holdings is valued at 10x FY22e earnings. For its Urban Development segment, we lowered the discount on Keppel Land's RNAV to 35% (prev.40%) on better clarity on the monetisation plans for its Urban Development portfolio and 1.5x price to book value of the Sino-Singapore Tianjin Eco-City. In the Connectivity segment, we valued M1 at 9x FY22e earnings. For the Asset Management division, we valued Keppel Capital at 10x FY22e earnings, a slight discount to its peers.

We also applied a holding-company discount of 20% to the Group. Our TP translates to about 1.2x FY22e book value, a slight premium to its historical average as the Group's transformation plans gain traction. As Keppel accelerates its transformation into an integrated asset-light business, we believe there is room for a further reduction in the Holdco discount we apply to the Group over time. We will review the discount we apply to the Group as the Group continues its transformation.

Risks to our view include: 1) a delay in the approvals required for the Keppel-Sembmarine transaction; and 2) a worsening global economy.

Figure 2: Keppel SOTP valuation

SOTP valuation S\$mn	Basis	% owned	Multiple (x)	Book value / RNAV / Earnings	Share of Book value / RNAV / Earnings	/ share
Business Segments						
Energy & Environment						
Keppel O&M	Net asset	100%	0.8	4,882	4,882	2.68
Keppel Infrastructure Holdings	10x FY22e earnings	100%	10.0	158	1,581	0.87
Urban Development						
Keppel Land	35% discount to RNAV	100%	35%	12,938	8,410	4.62
Sino-Singapore Tianjin Eco-City (SSTEC)	Net asset	50%	1.5	420	315	0.17
Connectivity						
M1 Limited	9x FY22e earnings	84%	9.0	62	468	0.26
Asset Management						
Keppel Capital	10x FY22e earnings	100%	10.0	131	1,314	0.72
Listed entities						
Market values						
- Keppel REIT		49.0%	1.0	3,906	1,914	1.05
- Keppel DC REIT		20.9%	1.0	4,304	900	0.49
- Keppel Infra Trust		18.2%	1.0	2,720	495	0.27
- Keppel Pacific Oak US REIT		7.3%	1.0	1,093	80	0.04
Fair value of Keppel Corp (before Holdco discount)						11.18
Holdco discount						20%
Fair value of Keppel Corp						8.95

Source: Company data, PSR

Financials
Income Statement

Y/E Dec, (\$'mn)	FY19	FY20	FY21	FY22e	FY23e
Revenue	7,580	6,574	8,625	9,898	8,449
Materials and Subcontract costs	(5,267)	(4,591)	(6,603)	(7,324)	(6,126)
Staff costs	(1,163)	(1,120)	(1,116)	(1,386)	(1,183)
Depreciation and amortisation	(375)	(414)	(406)	(425)	(431)
Other items	167	(412)	510	443	438
EBIT	941	37	1,009	1,206	1,148
Net finance expenses	(135)	(130)	(141)	(138)	(148)
Share of results of associates	147	(162)	467	478	478
Profit before tax	954	(255)	1,335	1,546	1,478
Taxation	(192)	(253)	(325)	(342)	(327)
Net Profit	761	(508)	1,010	1,204	1,151
Net Profit (excl. Impairments)	761	143	1,374	1,204	1,152
Profit attributable to owners	707	(506)	1,023	1,209	1,156

Per share data (\$)

Y/E Dec	FY19	FY20	FY21	FY22e	FY23e
BVPS	6.41	6.13	6.83	7.14	7.40
DPS	0.20	0.09	0.33	0.37	0.35
EPS	0.39	(0.28)	0.56	0.66	0.63

Cash Flow

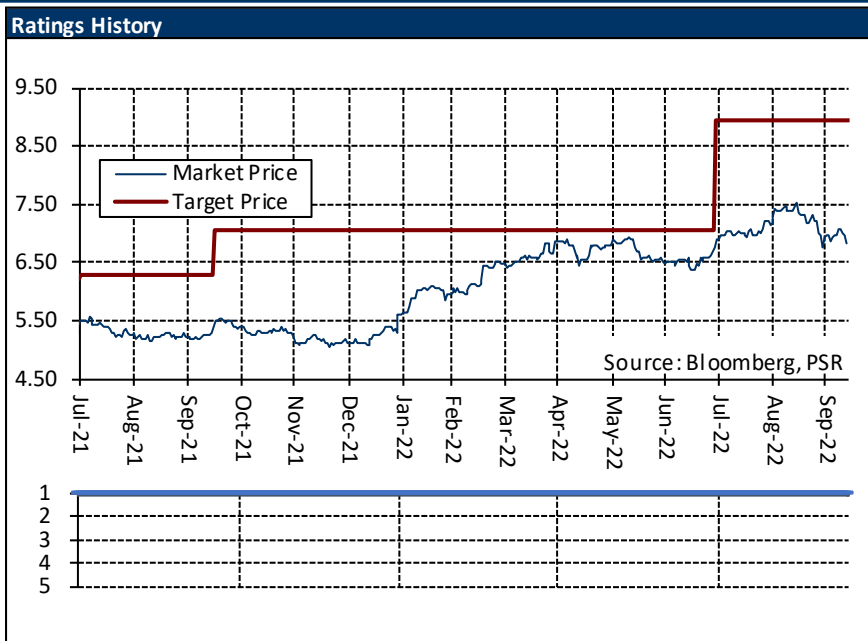
Y/E Dec, (\$'mn)	FY19	FY20	FY21	FY22e	FY23e
CFO					
Operating profit	877	8	898	1,012	914
Adjustments	117	91	(570)	(12)	(6)
WC changes	(1,437)	595	(187)	(5,799)	4,466
Cash generated from ops	(443)	694	142	(4,798)	5,374
Others	(382)	(430)	(417)	(480)	(474)
Cashflow from ops	(825)	263	(276)	(5,278)	4,900
CFI					
CAPEX, net	(517)	(488)	(538)	(557)	(562)
Others	(1,171)	214	2,564	2,112	1,923
Cashflow from investments	(1,688)	(274)	2,025	1,555	1,361
CFF					
Dividends paid to owners	(418)	(273)	(346)	(655)	(674)
Proceeds from borrowings, net	3,003	1,028	(668)	(628)	(656)
Proceeds from equity issuance	0	-	-	-	-
Others	(239)	(42)	345	(11)	(11)
Cashflow from financing	2,346	713	(668)	(1,295)	(1,341)
Net change in cash	(167)	702	1,082	(5,017)	4,920
Cash at the start of the period	2,429	1,778	2,408	3,544	(1,474)
Currency translation	(27)	(27)	(27)	(27)	(26)
Others	-	-	-	-	-
Ending cash	1,778	2,408	3,544	(1,474)	3,446

*nm - not meaningful

Source: Company, Phillip Securities Research (Singapore) Estimates

Balance Sheet

Y/E Dec, (\$'mn)	FY19	FY20	FY21	FY22e	FY23e
ASSETS					
PPE & Investment Properties	6,684	6,973	6,830	8,172	8,494
Others	10,339	10,745	10,647	10,647	10,647
Total non-current assets	17,023	17,717	17,477	18,819	19,141
Cash and cash equivalents	1,784	2,480	3,617	(1,474)	3,446
Stocks	5,543	4,959	4,604	5,076	5,076
Contract assets	3,497	2,657	3,170	9,204	4,173
Others	3,475	3,284	2,927	3,664	3,596
Total current assets	14,298	13,380	14,318	16,470	16,291
Assets classified as held for sale	-	1,009	528	528	528
Total Assets	31,322	32,106	32,323	35,817	35,960
LIABILITIES					
Trade and other payables	4,605	4,604	5,099	4,848	4,668
ST borrowings	4,623	4,502	4,749	4,749	4,749
Others	2,720	2,866	2,072	5,215	5,590
Total current liabilities	11,947	11,971	11,920	14,812	15,007
LT borrowings	7,034	8,101	7,268	6,977	6,650
Others	694	762	655	996	791
Total non-current liabilities	7,729	8,863	7,923	7,973	7,441
Liabilities classified as held for sale	-	115	38	38	38
Total liabilities	19,676	20,950	19,882	22,824	22,486
EQUITY					
Share Capital	1,292	1,306	1,306	1,306	1,306
Retained profits	9,933	9,436	10,354	10,903	11,381
Others	421	414	782	785	788
Total equity	11,646	11,156	12,441	12,993	13,474
Total equity and liabilities	31,322	32,106	32,323	35,817	35,960
Valuation Ratios					
Y/E Dec	FY19	FY20	FY21	FY22e	FY23e
P/E (x)	17.6	-24.8	12.2	10.4	10.8
P/B (x)	1.1	1.1	1.0	1.0	0.9
EV/EBITDA (x)	15.7	2434.5	21.9	19.4	21.5
Dividend yield (%)	2.9%	1.3%	4.8%	5.3%	5.1%
Growth & Margins (%)					
Growth					
Revenue	27.1%	-13.3%	31.2%	14.8%	-14.6%
EBITDA	1.2%	-89.5%	619.4%	17.7%	3.3%
EBIT	-11.6%	-96.0%	nm	19.5%	-4.8%
PBT	-23.4%	-126.7%	nm	15.8%	-4.4%
Margins					
EBITDA margin	16.5%	2.0%	10.9%	11.2%	13.6%
EBIT margin	12.4%	0.6%	11.7%	12.2%	13.6%
Net profit margin	10.0%	-7.7%	11.7%	12.2%	13.6%
Key Ratios					
ROE	6.6%	-4.5%	8.6%	9.5%	8.7%
ROA	2.6%	-1.6%	3.1%	3.5%	3.2%
Net Gearing (%)	83.7%	89.5%	67.3%	101.4%	58.8%



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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