COMPANY UPDATE

Sembcorp Industries (SCI SP)

Bigger, Bolder, Faster, Stronger

SCI's Investor Day 2023 provided much positive information and fuel for thought. With its upgrade of renewables capacity targets, guidance for relatively stable baseload earnings from conventional energy, and blue sky option via hydrogen, ammonia and renewable energy imports, SCI looks well-placed to remain a key holding in investors' portfolios in the long term. Maintain BUY. Target price: S$7.20.

WHAT'S NEW

- **Investor Day 2023 – plenty of positive information to digest.** Sembcorp Industries (SCI) held its Investor Day 2023 yesterday which involved its CEO and CFO as well as its various market CEOs speaking about the company's strategic direction and expansion plans out to 2028, and how it will look to fund these plans, as well as emissions targets and updates on its current portfolio of quality assets focusing on its key Singapore, China and India geographies.

- **Further growth in renewables capacity.** As expected, the company upgraded its target gross installed renewables capacity from its prior 10GW by 2023 (which it has easily achieved), and it is now targeting to grow this to 25GW by 2028 (see chart overleaf). This implies a 22% CAGR over 2023-28 which is higher than its peers' average CAGR of 17% over the same period.

- **More solar, and a more balanced geographic exposure.** Interestingly, the company's 2023-28 plans involve incrementally growing its solar exposure relative to wind given that the latter currently comprises 62% of gross installed capacity vs solar at 31%. Geographically, current exposure to China based on gross installed capacity is at 62% vs India and SE Asia at 27% and 10% respectively. However, SCI is ideally looking to increase exposure to India and SE Asia relative to China (see chart on pg. 4).

- **Emphasis on stability of earnings out to 2028.** SCI has guided for its gas & related services segment (previously known as the conventional energy segment) to witness a six-year net profit CAGR of -2% over the 2022-28 period which we view as better-than-expected. We attribute this mainly to the company's strategic signing of long-term power purchase agreements (PPAs). On a group-wide basis, 52% of its gas portfolio has been contracted for more than five years (weighted average: 12 years) while in Singapore this increases to 72%, with a further 23% contracted at between 0-5 years (see chart overleaf).

KEY FINANCIALS

Year to 31 Dec (S$m)	2021	2022	2023F	2024F	2025F
Net turnover	7,795	7,825	7,350	7,609	7,840
EBITDA	1,127	1,185	1,636	1,549	1,495
Operating profit	670	728	1,169	1,072	1,008
Net profit (rep./act.)	279	704	988	989	1,035
Net profit (adj.)	279	704	988	989	1,035
EPS (S$ cent)	15.4	38.6	53.1	53.1	55.5
PE (x)	31.9	12.7	9.3	9.3	8.9
P/B (x)	2.4	2.3	1.9	1.7	1.5
EV/EBITDA (x)	10.3	9.8	7.1	7.5	7.7
Dividend yield (%)	1.0	2.4	3.3	3.3	3.5
Net margin (%)	3.6	9.0	13.4	13.0	13.2
Net debt/(cash) to equity (%)	160.5	146.2	54.6	49.9	35.4
Interest cover (x)	1.7	2.7	4.3	3.9	3.7
ROE (%)	7.9	18.2	22.8	19.6	17.9
Consensus net profit	-	-	928	848	856
UOBKH/Consensus (x)	-	-	1.07	1.17	1.21

Source: Sembcorp Industries Ltd, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	S$4.92
Target Price	S$7.20
Upside	+46.3%

COMPANY DESCRIPTION

The company is a Singapore-based industrial conglomerate, with businesses encompassing wind, solar and conventional energy, utilities, water and waste treatment, and industrial parks. It divested of its stake in Semb Marine in 3Q20.

STOCK DATA

GICS sector	Utilities
Bloomberg ticker:	SCI SP
Shares issued (m):	1,779.3
Market cap (S$m):	8,754.1
Market cap (US$m):	6,487.4
3-mth avg daily t'over (US$m):	27.2

Price Performance (%)

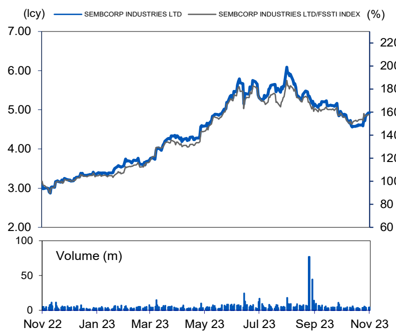
52-week high/low S$6.09/S$2.87

1mth	3mth	6mth	1yr	YTD
(1.8)	(13.6)	5.9	64.5	44.5

Major Shareholders	%
Temasek Hldgs	48.9

FY23 NAV/Share (S$)	2.57
FY23 Net Debt/Share (S$)	1.41

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- **How will SCI fund the growth?** SCI outlined an ambitious S$14b capital allocation plan over 2024-28, comprising of funding from operating cash flow (50%), project debt (30%) and corporate debt, capital recycling & partnerships (20%) (see chart on RHS). At present, the company has S$2b of undrawn committed facilities with 71% of its S$7.5b total debt at fixed rates. Thus, the company does not foresee the need for an equity raising unless there is a major acquisition, and it will look to continue to tap green & sustainable financing. Importantly, SCI plans to introduce long-term capital partners in both China and India which it anticipates will lead to valuation uplift for its assets.

- **Higher interest rates – not always bad.** Management disclosed that its strategic plans incorporate “higher for longer” interest rates and pointed out that in China, it is able to optimise its financing terms due to its state-owned enterprise (SOE) partnerships (see paragraph below). Moreover, SCI pointed out that in the past 12 months, higher interest rates have weeded out competition for renewables projects and thus it sees some near-term opportunities for 16,000-18,000MW of wind-specific bids in India.

- **Tangible and intangible benefits.** Management also highlighted that these SOE links bring with them lower borrowing costs – not just because SCI is operating in China where interest rates have been declining as opposed to increasing globally – since SOEs in China have even lower borrowing costs relative to China’s market rates. In addition, SCI pointed out that its SOE partners also provide guidance on government policy and relationships within the Chinese market.

- **Capital recycling – looking for the right price and time.** With its current renewables portfolio at 8.7GW and growing, SCI stated that it does not rule out recycling capital in this segment. Clearly, the company is not a distressed seller, but we did get the sense that even some of its Singapore assets could, given the right price, timing and opportunity, be recycled. On the acquisition front, SCI stated that it remains on the lookout for distressed assets and we believe some manner of activity may take place in the next 6-12 months.

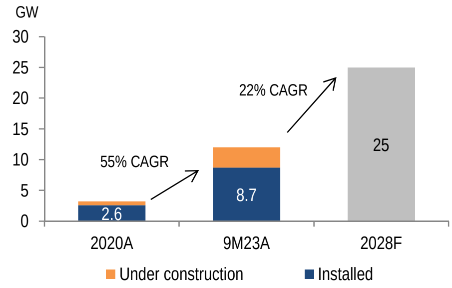
- **Falling short in IUS segment.** The integrated urban solutions (IUS) business segment has seen significant headwinds in the past few years given the lack of progress in Vietnam, with the management admitting that its performance has not met expectations. SCI disclosed that it is in the process of appointing a new CEO in this segment as well as reviewing its strategy.

- **Long-term PPAs – more of the same please.** In Singapore, SCI has been able to transform itself from a merchant business into a more stable one via the signing of long-term PPAs with blue-chip customers in the past 12 months. This gives the company secure base revenue for its Singapore power assets which would in turn fund its long-term green-energy transition. In our view, SCI will likely continue to sign more of such PPAs over the next 12-24 months. While some investors interpret the long-term PPAs as giving up upside to power prices, we prefer the inherent stability of PPAs vs regulatory volatility as seen by the Energy Market Authority’s recent re-regulation of the gas market.

- **The Chinese market – a great place to be.** SCI has had material success in growing its renewables portfolio in China given that the country is around five years ahead of schedule in growing its own renewables capacity. Importantly, with 70% of the Chinese market dominated by nine SOEs, and SCI having strategic partnerships with four of them, the country remains a key focus area for its organic and inorganic growth plans. For example, SCI acquired a minority stake in 1.9GW of renewables capacity from SDIC Power in 2021, and this portfolio has since organically grown to 3.6GW in 2023. Interestingly, management commented that it is less concerned about capital inflow into China to fund its projects, but more concerned about deploying the cash given that it bought mature assets in 2021 and 2022 which were income-generating straight away.

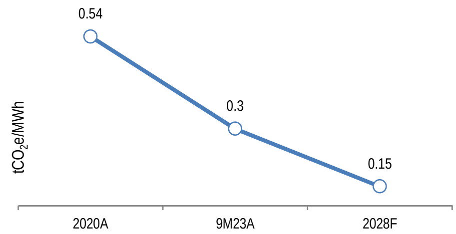
- **India – a much improved situation.** With a supportive rules-based regulatory environment, SCI believes the country’s renewables sector has further room for growth given government incentives to increase investments, promote the usage of renewables as well as solar manufacturing activities. In addition, on the back of the introduction of India’s Late Payment Surcharge, its distribution companies have materially reduced their payment issues in the

GROWTH IN RENEWABLES CAPACITY



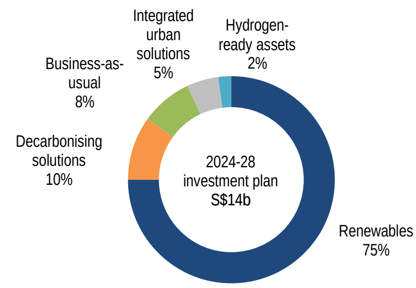
Source: SCI

SCI’S PLANNED REDUCTION IN EMISSIONS



Source: SCI

2024-28 CAPITAL ALLOCATION PLAN



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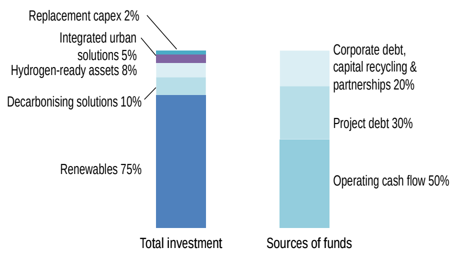
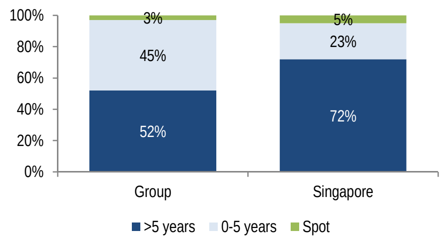
ACCESS TO DIVERSIFIED FUNDING SOURCES



Source: SCI

HIGH CONTRACTED POSITION OF GAS PORTFOLIO



Source: SCI

past 12-18 months. Operationally, SCI highlighted that its in-house capabilities has led to lower cost, lower execution cycle time and higher IRR for its projects, eg at Vector Green, its efforts have led to an annual increase of 9,00MWh in power generation and a 200bp hike in IRR.

- **Regional power imports – an evolving theme with Singapore at the epicentre.** SCI noted that demand for "green electrons" is high in Singapore and thus will look to source this from brownfield projects in Vietnam and greenfield projects in Indonesia. The news may not be so great for Singapore residential consumers in the medium to long term given that these "green electrons" are higher cost and will be passed on to the customer.

- **Positioning for the future: ammonia and hydrogen.** In our view, ammonia may take a long time to gain commerciality (with the added problem of its competing usage as fertiliser). Hydrogen, however, appears to be at the forefront of SCI's thinking with it taking the lowest-risk pathway towards incorporating it into Singapore's future energy mix. Given that energy comprises around 65% of the cost of hydrogen production, renewables (which SCI has in abundance in countries that have supportive policies) will be a key ingredient for success. In Singapore, SCI's current J-class power plants can be retrofitted to use 30% (and up to 50%) of hydrogen, thus potentially extending the life of the power plants.

EARNINGS REVISION/RISK

- None at present although the abundance of information presented at the company's Investor Day will likely lead to earnings upgrades as we work through our financial model.

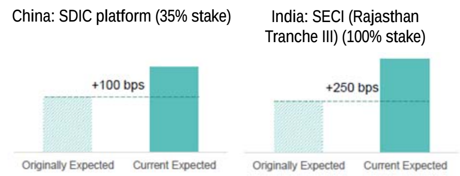
VALUATION/RECOMMENDATION

- **Maintain BUY with a target price of S$7.20** based on a target PE multiple of 13.6x. This target PE multiple is 1.5SD above the company's past five-year average PE of 10.1x (excluding 2020 where the company reported impairment-related losses) and is applied to our 2024 EPS estimate which we believe is a better reflection of the company's "normalised" earnings compared to 2022's earnings. SCI, cognizant of its funding needs for growth, will likely keep its dividend payout ratio at 25%.

SHARE PRICE CATALYST

- Execution of its renewables energy targets via organic and inorganic means; capital recycling in its energy portfolio; rejuvenation of its urban solutions business.

ABILITY TO ENHANCE RETURNS OF PORTFOLIO



Source: SCI

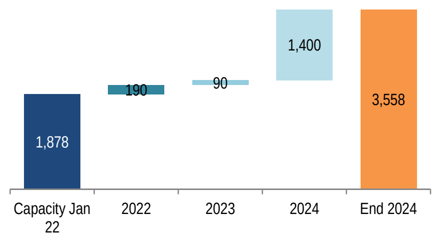
GUIDANCE

	Net profit¹	Expected investment²	2028 ROE
Gas & related services	-2%	S$1b	15%
Renewables	+25%	S$11b	10%
Integrated urban solutions	• Stable performance expected • Continue to build up landbank		
Decarbonisation solutions	• Capitalise on existing expertise to drive energy transition • Positive earnings by 2027-28, acceleration post 2028		

Note: ¹ Six-year CAGR over 2022-2028; ² 2024-2028
Source: SCI

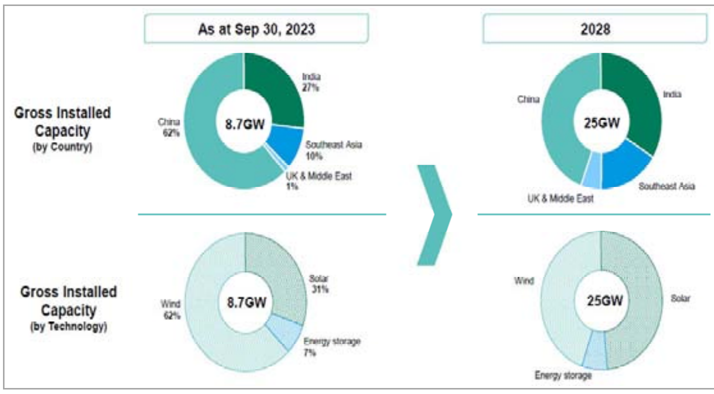
BENEFITS FROM PARTNERING WITH SDIC (MW)

- Total portfolio increased to 3.6GW from 1.9GW when acquired in 2021



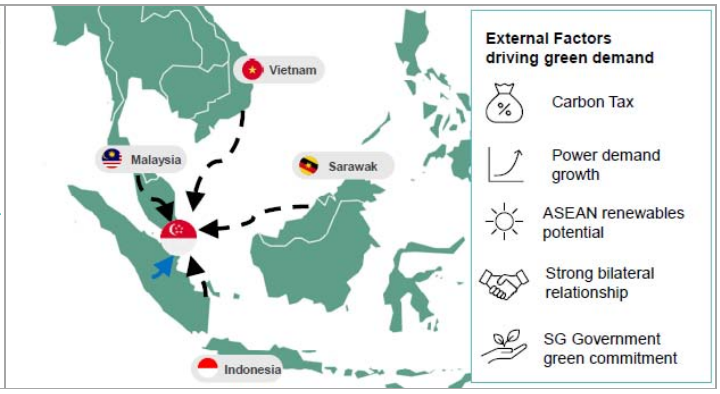
Source: SCI

SCI'S STRATEGY TO BROADLY DIVERSIFY ACROSS KEY MARKETS AND GEOGRAPHIES



Source: SCI

SINGAPORE WELL PLACED AS A DEMAND AGGREGATOR FOR ENERGY CARRIERS



Source: SCI

PROFIT & LOSS

Year to 31 Dec (S$m)	2022	2023F	2024F	2025F
Net turnover	7,825	7,350	7,609	7,840
EBITDA	1,185	1,636	1,549	1,495
Deprec. & amort.	457	467	477	487
EBIT	728	1,169	1,072	1,008
Total other non-operating income	162	35	47	81
Associate contributions	248	333	420	508
Net interest income/(expense)	(273)	(273)	(273)	(273)
Pre-tax profit	865	1,264	1,266	1,324
Tax	(138)	(253)	(253)	(265)
Minorities	(23)	(23)	(24)	(24)
Preferred dividends	0	0	0	0
Net profit	704	988	989	1,035
Net profit (adj.)	704	988	989	1,035

BALANCE SHEET

Year to 31 Dec (S$m)	2022	2023F	2024F	2025F
Fixed assets	5,305	5,098	4,881	4,654
Other LT assets	4,207	4,488	4,937	5,470
Cash/ST investment	1,254	4,507	4,369	4,890
Other current assets	5,254	1,588	1,646	1,699
Total assets	16,020	15,681	15,833	16,712
ST debt	1,095	1,095	1,095	1,095
Other current liabilities	3,726	2,636	2,031	2,121
LT debt	5,974	5,974	5,974	5,974
Other LT liabilities	947	962	977	992
Shareholders' equity	3,977	4,693	5,410	6,158
Minority interest	239	262	286	310
Total liabilities & equity	16,020	15,681	15,833	16,712

CASH FLOW

Year to 31 Dec (S$m)	2022	2023F	2024F	2025F
Operating	1,692	449	612	1,285
Pre-tax profit	865	1,264	1,266	1,324
Tax	(64)	(56)	(238)	(231)
Deprec. & amort.	457	467	477	487
Associates	(248)	(333)	(420)	(508)
Working capital changes	24	(1,111)	(690)	(4)
Non-cash items	0	0	0	0
Other operating cashflows	658	217	217	217
Investing	(1,385)	3,349	(206)	(204)
Capex (growth)	(1,588)	(300)	(300)	(300)
Capex (maintenance)	(2)	0	(2)	0
Investments	55	3,553	0	0
Proceeds from sale of assets	40	40	40	40
Others	110	56	56	56
Financing	(203)	(545)	(545)	(560)
Dividend payments	(137)	(297)	(297)	(312)
Issue of shares	21	25	25	25
Proceeds from borrowings	310	0	0	0
Loan repayment	0	0	0	0
Others/interest paid	(397)	(273)	(273)	(273)
Net cash inflow (outflow)	104	3,253	(139)	521
Beginning cash & cash equivalent	1,297	1,322	4,575	4,436
Changes due to forex impact	(79)	0	0	0
Ending cash & cash equivalent	1,322	4,575	4,436	4,956

KEY METRICS

Year to 31 Dec (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	15.1	22.3	20.4	19.1
Pre-tax margin	11.1	17.2	16.6	16.9
Net margin	9.0	13.4	13.0	13.2
ROA	4.6	6.2	6.3	6.4
ROE	18.2	22.8	19.6	17.9
Growth				
Turnover	0.4	(6.1)	3.5	3.0
EBITDA	5.1	38.1	(5.3)	(3.5)
Pre-tax profit	104.5	46.2	0.1	4.6
Net profit	152.3	40.4	0.1	4.7
Net profit (adj.)	152.3	40.4	0.1	4.7
EPS	150.2	37.3	0.0	4.6
Leverage				
Debt to total capital	62.6	58.8	55.4	52.2
Debt to equity	177.7	150.6	130.7	114.8
Net debt/(cash) to equity	146.2	54.6	49.9	35.4
Interest cover (x)	2.7	4.3	3.9	3.7

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