

SECTOR UPDATE

Offshore Marine – Singapore

Outlook Remains Strong, Supported By High Oil Prices

The rig market, particularly the semi-submersibles segment, has continued to gain strength in 2022 with higher utilisation and day rates. The industry continues to search for an equilibrium as supply destruction has persisted across asset classes this year. Heading into 4Q22 and 1Q23, we believe that oil prices will be well supported above the US\$100-110 range. Our sector rating remains **OVERWEIGHT**, and our top picks are Yangzijiang, Keppel and Sembcorp Marine.

WHAT'S NEW

- Since our Mar 22 report, the offshore market has continued to strengthen with utilisation rates back above pre-pandemic levels (see chart on RHS) while day rates for semi-submersibles in particular have been extremely strong. The supply-demand dynamics continue to shift positively in favour of rig owners as supply destruction has continued - on a yoy basis, the global offshore rig industry had lost 36 rigs (-7%) to 694 rigs as at 12 Aug 22. Importantly, this supply destruction was seen across all asset classes with semi-subs registering the largest decline in supply in percentage terms, decreasing 12% yoy to 106 rigs. In our view, this is positive as the extraction of excess supply should allow utilisation and day rates to continue to further firm up going forward.
- **Industry activity to pick up in 2022 and 2023.** Looking at future projects, the demand for production assets appears to have meaningful upside in the next few years, which could have positive ramifications for both Keppel Corp (KEP) and Sembcorp Marine (SMM). According to Rystad Energy, offshore investments in 2022 are set to increase 7% yoy from US\$145b to US\$155b. In addition we highlight that the US\$150b of greenfield projects sanctioned in 2021 (2020: US\$80b) will likely be repeated in 2022, thus underlining the positive outlook for the offshore marine sector in the near to medium term.
- **Oil price outlook.** Heading into winter in the northern hemisphere, we believe that Brent oil prices will be well supported above the US\$100-110 range. In late-Aug 22, Saudi Arabia warned that there was a significant disconnect between financial and physical markets and that this "extreme" volatility could prompt the OPEC+ alliance to act to throttle back production. This, together with OPEC spare capacity close to historic lows (see chart on RHS), and large scale gas-to-oil switching taking place in Europe due to a lack of Russian gas, oil prices should remain high in the near to medium term.

ACTION

- **Maintain sector view at OVERWEIGHT.** We continue to like Yangzijiang (YZJ) which remains inexpensive at 2022F P/B of 0.7x and will see margin expansion in the next few quarters. We also like KEP and SMM, which combined have seen nearly S\$10b worth of orders ytd. In our view, this bodes well for the merger which is expected to be completed by 4Q22.

PEER COMPARISON

Company	Ticker	Rec	----- Price (1cy) ----- 29 Aug 22	----- Target	Upside to TP (%)	Market Cap (US\$m)	----- PE (x) ----- 2022F	2023F	----- P/B (x) ----- 2022F	2023F	-- EV/EBITDA (x) -- 2022F	2023F	ROE% 2022F	Yield (%) 2022F
Keppel Corp	KEP SP	BUY	7.15	10.11	40.2	9,065	13.8	13.5	1.0	1.0	14.4	13.6	7.7	4.2
Sembcorp Industries	SCI SP	BUY	3.40	4.10	20.9	4,324	8.5	11.4	1.4	1.3	8.2	9.2	18.1	3.6
Sembcorp Marine	SMM SP	BUY	0.114	0.156	33.3	2,623	NM	85.7	1.0	1.0	22.3	17.7	NM	NA
Yangzijiang	YZJSGD SP	BUY	0.96	1.16	19.6	2,737	6.7	5.7	1.2	0.8	3.9	3.4	10.9	3.8
Average – Spore-listed							9.7	10.2	1.2	1.0	12.2	11.0	12.2	3.9
Daewoo Shipbldg	042660 KS	NR	20,250	NA	NA	1,610	NM	20.8	1.5	1.2	NM	11.8	NM	NA
Samsung Heavy Ind	010140 KS	NR	6,010	NA	NA	3,920	NM	86.8	1.2	1.1	NM	18.2	NM	NA
Korea Shipbuilding	009540 KS	NR	97,100	NA	NA	5,090	NM	11.3	0.7	0.7	NM	8.0	NM	NA
Average – Sector							9.7	12.5	1.1	1.0	12.2	11.7	12.2	3.9

Note: NR = Not Rated, based on Bloomberg consensus
Source: Bloomberg, UOB Kay Hian

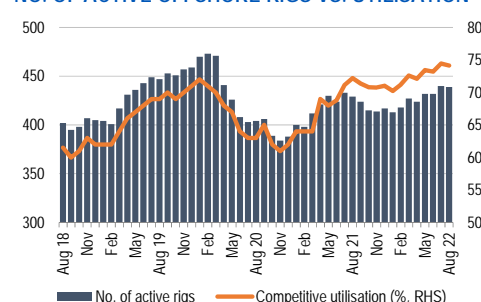
OVERWEIGHT (Maintained)

SECTOR PICKS

Company	Ticker	Rec	Price (\$S)	Target
Keppel Corp	KEP SP	BUY	7.15	10.11
Sembcorp Industries	SCI SP	BUY	3.40	4.10
Sembcorp Marine	SMM SP	BUY	0.114	0.156
Yangzijiang	YZJSGD SP	BUY	0.96	1.16

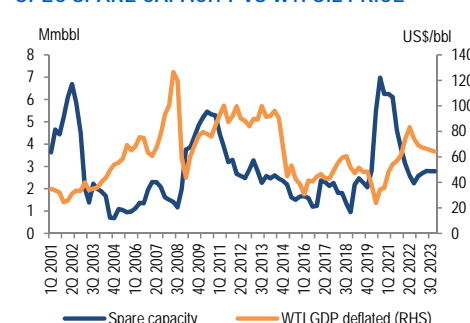
Source: Bloomberg, UOB Kay Hian

NO. OF ACTIVE OFFSHORE RIGS VS. UTILISATION



Note: Excludes rigs in repair/special survey which number c.2-3 per year
Source: Basso Analytics

OPEC SPARE CAPACITY VS WTI OIL PRICE



Source: US Energy Information Administration

ANALYST(S)

Adrian Loh
+65 6590 6633
adrianloh@uobkayhian.com

ESSENTIALS

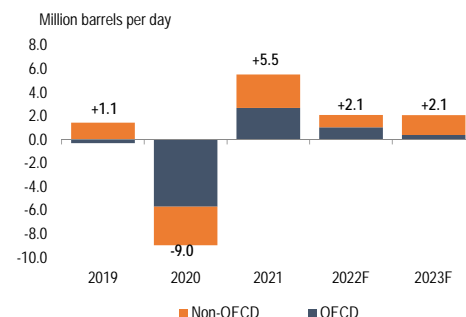
- Jack-up rigs seeing higher demand.** Global jack-up demand has risen ytd with jack-up contractors having secured 100 charters or 165 rig-years of work for the first five months of 2022 – this formed 76% of the jack-up time booked in all of 2021, thus signalling greater demand in 2022. With 45 known jack-up requirements that are still open this year, coupled with higher commodity prices and increased willingness by oil & gas companies to spend on capex, it would appear that jack-up awards in 2022 should easily exceed 2021's numbers. According to data from Bassoe, the Middle East region has been the main driver behind the increased demand, with Saudi Aramco and ADNOC leading the way, followed by India and Southeast Asia.
- Semi-submersibles see a significant increase in contracts awarded.** Despite day rates for mid-water semi-subs (5,000-8,000ft) having risen 40% ytd, with advanced semis priced around US\$400,000/day in Aug 22, the number of contracts for such rigs have significantly surpassed the contracts for jack-ups. As a result, the number of semi-sub contracts signed this year has outnumbered jack-ups by almost 2:1.
- Bullish FPSO outlook.** The latest 2Q22 floating production systems report by Energy Maritime Associates (EMA) shows 190 offshore production projects in the pipeline, an increase of seven from 1Q22, thus implying a bullish outlook for new orders. Importantly, EMA notes that 21 floating production systems have been awarded ytd, which is the highest level since 2013, and that SMM's yards are well placed for new orders.
- European bureaucracy holding back growth in offshore wind.** In 2021, the EU saw €41b invested in 25GW of new wind farms; however this falls far short of the 39GW/year needed to grow from the current wind capacity of 190GW to the targeted 510GW by 2030. Part of the reason is due to the EU's lengthy permitting procedures, which means that the region's energy transition has become more time consuming and expensive, eg the installation of three wind turbines in Germany requires over 30,000 pages of paperwork.
- Offshore wind in the US – growth off a very low base.** Wind power was the country's fastest growing energy source in 2021, forming 32% of total US energy capacity growth. However, we note that this is off a very low base (see chart on RHS) as the country only has two operating offshore wind farms off the Rhode Island and North Carolina totalling 42MW. While President Biden's Inflation Reduction Act provides US\$370b for climate and energy programmes, signalling a material expansion in clean electricity generation, developing offshore wind in the Gulf of Mexico (GOM) may be problematic given that on an annual basis, it is prone to hurricanes between July to November. Thus, industry studies have shown that 10-15% of any offshore wind infrastructure built in the GOM may be prone to hurricane destruction. Rystad nevertheless estimates that capex for offshore wind in the Americas will grow from c.US\$4b in 2022 to more than US\$15b by 2030 (or 18% CAGR).
- Oil demand expected to grow, but forecasts face heightened uncertainty.** In its latest Aug 22 update, the US Energy Information Administration (EIA) forecasts oil demand growth of 2.1mmbpd for both 2022 and 2023 (see chart on RHS). Note that in the past few months, the US EIA has gradually downgraded 2022 oil demand growth from its Mar 22 forecast of 3.1mmbpd growth. It has highlighted that its forecast is subject to "heightened levels of uncertainty" resulting from a variety of factors, including Russian oil sanctions as well as less robust global economic activity. Note that an additional Russian oil embargo goes into effect on 5 Dec 22, banning the provision of shipping, insurance and other services related to Russian oil. If the US successfully bans dollar clearing for Russian oil purchases, this would result in tighter oil and natural gas markets in the near term.

1H22 RESULTS RECAP

Yangzijiang Shipbuilding (YZJSGD SP/BUY/Target: S\$1.16)

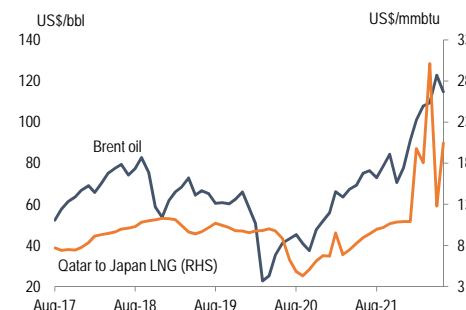
- Operationally a strong set of numbers.** YZJ reported 1H22 revenue growth of 70% to Rmb9.7b which resulted in a 32% yoy increase in net profit from continuing operations to Rmb1.2b. As guided by management and as previewed in our previous note, the company delivered 35 vessels during 1H22 which, on a run-rate basis, is ahead of its previous 2022 delivery target of 60 vessels. In our view, YZJ is highly likely to achieve its new target of 70

INCREMENTAL OIL DEMAND GROWTH PER YEAR



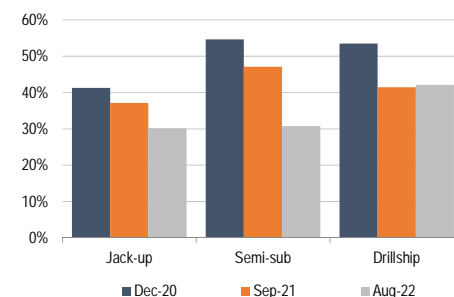
Source: US Energy Information Administration (Sep 21)

BRENT OIL PRICE VS LNG CONTRACT PRICE



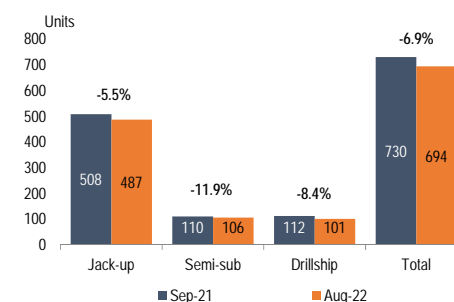
Source: Bloomberg

INACTIVE RIGS AS A % OF TOTAL RIGS AVAILABLE



Note: Excludes rigs in repair/special survey which number c.1-3 per year
Source: Bassoe Analytics

CHANGE IN NO. OF RIGS AVAILABLE FOR WORK: MAR 22 VS MAR 21



Source: Bassoe Analytics

vessels. At the bottom line however, the results missed expectations due to fair value loss on currency hedges.

- **Maintain BUY with an SOTP-based target price of S\$1.16.** We have used an 8x and 5x multiple for its shipbuilding and trading & other business segments respectively, thus arriving at a S\$1.14 and S\$0.04/share valuation for these two segments (see table below). By using publicly-sourced replacement cost for its shipping assets, we value this segment at Rmb4.8b or S\$0.26/share – this is double that of the company's carrying cost of these assets, or 3x higher than its book value of S\$0.09 as at end-21. At our target price, YZJ would trade at a 2022F PE of 6.9x which we do not view as stretched.

Keppel Corp. (KEP SP/BUY/Target: S\$10.11)

- **Solid contribution from all businesses.** KEP reported 1H22 revenue from continuing operations of S\$3.4b (+16.2% yoy), which resulted in a 26% yoy increase in net profit from continuing operations of S\$434m. The company declared a better-than-expected dividend of S\$0.15/share which represents a payout ratio of 62%, and higher than its historical payout ratio of 39-59% in the past 10 years.
- **A resurgent offshore marine business.** As at end-1H22, Keppel Offshore Marine (KOM) had S\$4.4b net orderbook with a further S\$8b worth of potential contract in advanced discussions. Importantly, the company managed to garner S\$255m worth of bareboat charters for four of its legacy rig assets (which are not going into the SMM merger); management appeared confident that it would be able to sell its other rigs sooner rather than later given the more bullish offshore marine environment.
- **We have a BUY rating on KEP with an SOTP-based target price of S\$10.11.** The company appears to be at an interesting crossroad in 2022 with the exit of its KOM segment and its move towards a more asset-light and recurring earnings business model. It also has a 15% ROE target vs 9.1% in 2021 and 1H22 annualised ROE of 8.4%. Of interest will be the pace of its asset monetisation which could bolster earnings again in 2022 and thus lead to another dividend surprise.

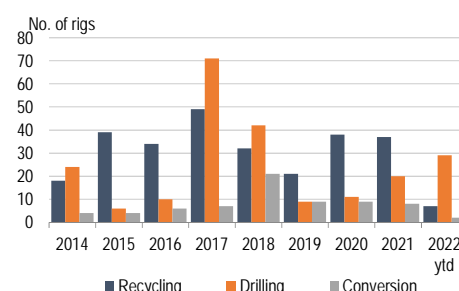
Sembcorp Marine (SMM SP/BUY/Target: S\$0.156)

- **Loss for 1H22 but financials should strengthen in 2H22.** SMM reported a 1H22 loss of S\$143m which was significantly better than the S\$1.2b loss in 1H21. We assess the results as being largely in line with our expectations. We believe that the company's financials will witness sequential strength in 2H22 given its higher order wins ytd. In addition, we highlight that the company is on track to deliver Transocean's Deepwater Titan which would then enable it to collect S\$350m in revenue in 2H22. No significant delays were reported for current and new projects.
- **New order wins in 1H22 bode well.** SMM disclosed that ytd order wins total S\$1.9b, with around S\$300m of this being repair and upgrading works. Given that order wins for the wind turbine installation vessel and Brazilian Navy total S\$850m, it would imply that the recent order win for gas topsides from an oil major is worth around S\$750m. During the analyst briefing, SMM's management stated that it was unable to disclose any details on neither the project nor the client at present. The company's current net orderbook is >S\$2.5b.
- **Maintain BUY with S\$0.156 target price.** With the SMM/Keppel merger terms largely in place and the uncertainty out of the way, the focus on SMM will be to garner new orders in 2022 and add to its orderbook. Our target book-value multiple for SMM of 1.2x reflects our confidence that it will garner such order thus leading to positive share price performance.

RISKS TO OUR THESIS

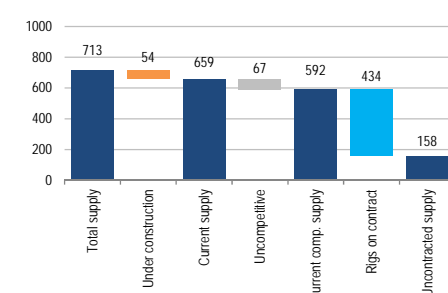
- Delays in project sanctioning due to supply chain inflationary pressures
- Lack of financing for industries that are seen to be related to the fossil fuel industry
- Despite the high oil price resulting in super-normal free cash flow, oil companies may remain wary of committing to offshore capex and instead focus on share buybacks or paying dividends

RIG SALES BY TYPE



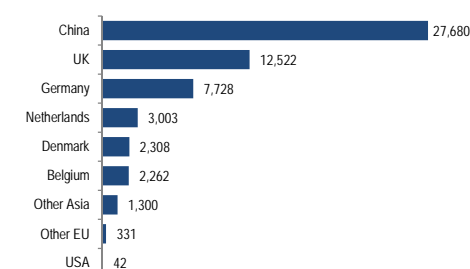
Source: Bassoe Analytics

TOTAL SUPPLY OF RIGS IN THE GLOBAL MARKET



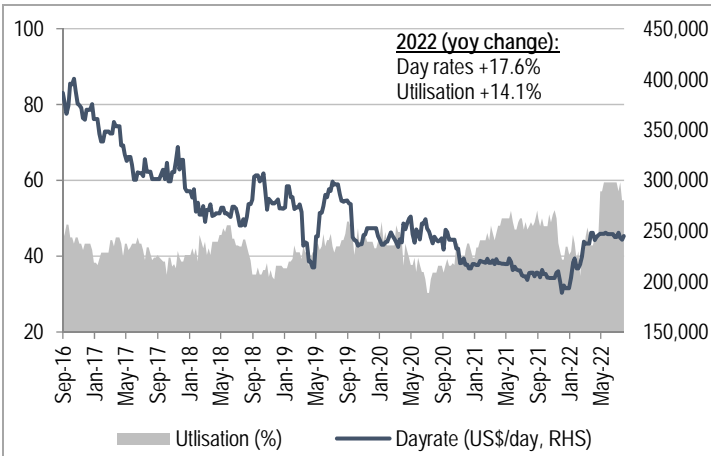
Source: Bassoe Analytics

COUNTRIES WITH OFFSHORE WIND CAPACITY (MW)



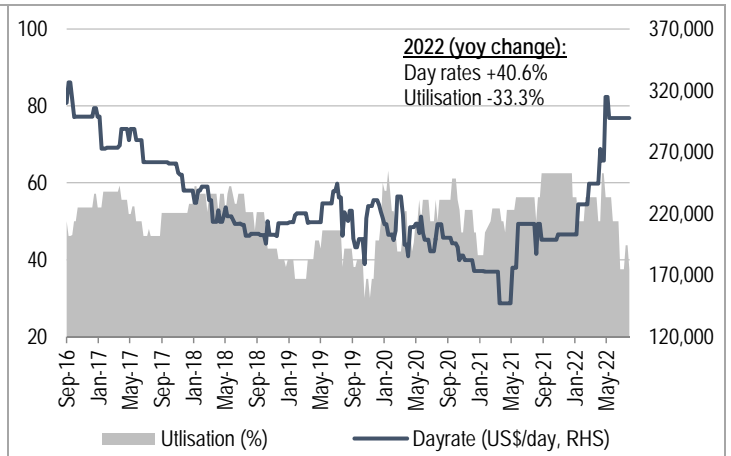
Source: Global Wind Energy Council

DAYRATE & UTILISATION: SEMISUB 8000'



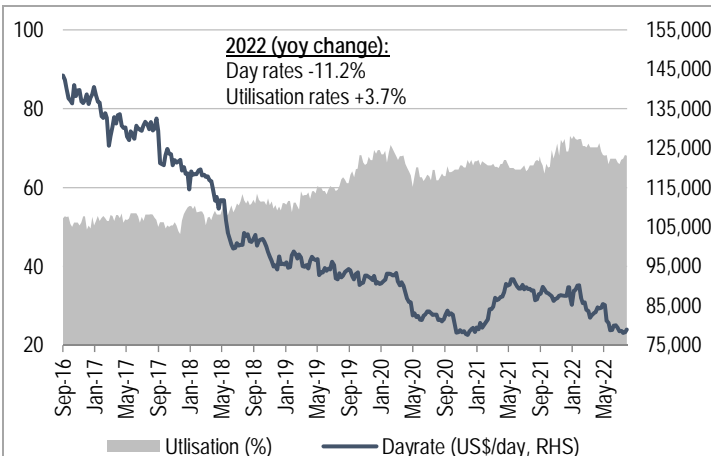
Source: Rigzone, Bloomberg

DAYRATE & UTILISATION: SEMISUB 5000-8000'



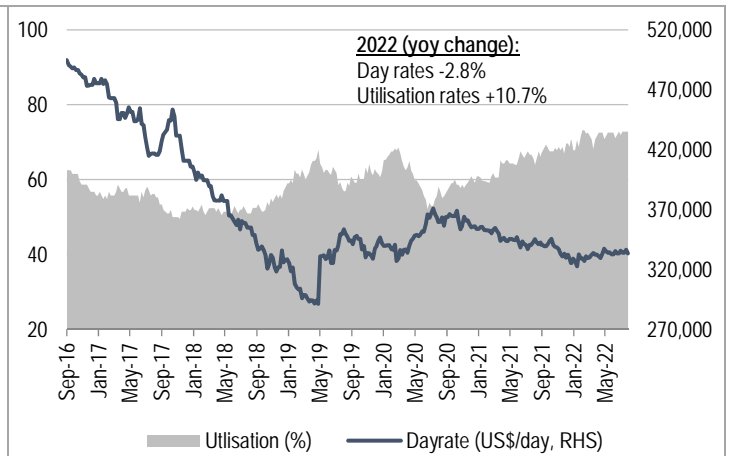
Source: Rigzone, Bloomberg

DAYRATE & UTILISATION: JACKUP 300+ IC



Source: Rigzone, Bloomberg

DAYRATE & UTILISATION: DRILLSHIP



Source: Rigzone, Bloomberg

Disclosures/Disclaimers

This report is prepared by UOB Kay Hian Private Limited ("UOBKH"), which is a holder of a capital markets services licence and an exempt financial adviser in Singapore.

This report is provided for information only and is not an offer or a solicitation to deal in securities or to enter into any legal relations, nor an advice or a recommendation with respect to such securities.

This report is prepared for general circulation. It does not have regard to the specific investment objectives, financial situation and the particular needs of any recipient hereof. Advice should be sought from a financial adviser regarding the suitability of the investment product, taking into account the specific investment objectives, financial situation or particular needs of any person in receipt of the recommendation, before the person makes a commitment to purchase the investment product.

This report is confidential. This report may not be published, circulated, reproduced or distributed in whole or in part by any recipient of this report to any other person without the prior written consent of UOBKH. This report is not directed to or intended for distribution to or use by any person or any entity who is a citizen or resident of or located in any locality, state, country or any other jurisdiction as UOBKH may determine in its absolute discretion, where the distribution, publication, availability or use of this report would be contrary to applicable law or would subject UOBKH and its connected persons (as defined in the Financial Advisers Act, Chapter 110 of Singapore) to any registration, licensing or other requirements within such jurisdiction.

The information or views in the report ("Information") has been obtained or derived from sources believed by UOBKH to be reliable. However, UOBKH makes no representation as to the accuracy or completeness of such sources or the Information and UOBKH accepts no liability whatsoever for any loss or damage arising from the use of or reliance on the Information. UOBKH and its connected persons may have issued other reports expressing views different from the Information and all views expressed in all reports of UOBKH and its connected persons are subject to change without notice. UOBKH reserves the right to act upon or use the Information at any time, including before its publication herein.

Except as otherwise indicated below, (1) UOBKH, its connected persons and its officers, employees and representatives may, to the extent permitted by law, transact with, perform or provide broking, underwriting, corporate finance-related or other services for or solicit business from, the subject corporation(s) referred to in this report; (2) UOBKH, its connected persons and its officers, employees and representatives may also, to the extent permitted by law, transact with, perform or provide broking or other services for or solicit business from, other persons in respect of dealings in the securities referred to in this report or other investments related thereto; (3) the officers, employees and representatives of UOBKH may also serve on the board of directors or in trustee positions with the subject corporation(s) referred to in this report. (All of the foregoing is hereafter referred to as the "Subject Business"); and (4) UOBKH may otherwise have an interest (including a proprietary interest) in the subject corporation(s) referred to in this report.

As of the date of this report, no analyst responsible for any of the content in this report has any proprietary position or material interest in the securities of the corporation(s) which are referred to in the content they respectively author or are otherwise responsible for.

IMPORTANT DISCLOSURES FOR U.S. PERSONS

This research report was prepared by UOBKH, a company authorized, as noted above, to engage in securities activities in Singapore. UOBKH is not a registered broker-dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution by UOBKH (whether directly or through its US registered broker dealer affiliate named below) to "major U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). All US persons that receive this document by way of distribution from or which they regard as being from UOBKH by their acceptance thereof represent and agree that they are a major institutional investor and understand the risks involved in executing transactions in securities.

Any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through UOB Kay Hian (U.S.) Inc ("UOBKHUS"), a registered broker-dealer in the United States. Under no circumstances should any recipient of this research report effect any transaction to buy or sell securities or related financial instruments through UOBKH.

UOBKHUS accepts responsibility for the contents of this research report, subject to the terms set out below, to the extent that it is delivered to and intended to be received by a U.S. person other than a major U.S. institutional investor.

The analyst whose name appears in this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA") and may not be an associated person of UOBKHUS and, therefore, may not be subject to applicable restrictions under FINRA Rules on communications with a subject company, public appearances and trading securities held by a research analyst account.

Analyst Certification/Regulation AC

Each research analyst of UOBKH who produced this report hereby certifies that (1) the views expressed in this report accurately reflect his/her personal views about all of the subject corporation(s) and securities in this report; (2) the report was produced independently by him/her; (3) he/she does not carry out, whether for himself/herself or on behalf of UOBKH or any other person, any of the Subject Business involving any of the subject corporation(s) or securities referred to in this report; and (4) he/she has not received and will not receive any compensation that is directly or indirectly related or linked to the recommendations or views expressed in this report or to any sales, trading, dealing or corporate finance advisory services or transaction in respect of the securities in this report. However, the compensation received by each such research analyst is based upon various factors, including UOBKH's total revenues, a portion of which are generated from UOBKH's business of dealing in securities.

Reports are distributed in the respective countries by the respective entities and are subject to the additional restrictions listed in the following table.

General	This report is not intended for distribution, publication to or use by any person or entity who is a citizen or resident of or located in any country or jurisdiction where the distribution, publication or use of this report would be contrary to applicable law or regulation.
Hong Kong	This report is distributed in Hong Kong by UOB Kay Hian (Hong Kong) Limited ("UOBKHHK"), which is regulated by the Securities and Futures Commission of Hong Kong. Neither the analyst(s) preparing this report nor his associate, has trading and financial interest and relevant relationship specified under Para. 16.4 of Code of Conduct in the listed corporation covered in this report. UOBKHHK does not have financial interests and business relationship specified under Para. 16.5 of Code of Conduct with the listed corporation covered in this report. Where the report is distributed in Hong Kong and contains research analyses or reports from a foreign research house, please note: (i) recipients of the analyses or reports are to contact UOBKHHK (and not the relevant foreign research house) in Hong Kong in respect of any matters arising from, or in connection with, the analysis or report; and (ii) to the extent that the analyses or reports are delivered to and intended to be received by any person in Hong Kong who is not a professional investor, or institutional investor, UOBKHHK accepts legal responsibility for the contents of the analyses or reports only to the extent required by law.
Indonesia	This report is distributed in Indonesia by PT UOB Kay Hian Sekuritas, which is regulated by Financial Services Authority of Indonesia ("OJK"). Where the report is distributed in Indonesia and contains research analyses or reports from a foreign research house, please note recipients of the analyses or reports are to contact PT UOBKH (and not the relevant foreign research house) in Indonesia in respect of any matters arising from, or in connection with, the analysis or report.
Malaysia	Where the report is distributed in Malaysia and contains research analyses or reports from a foreign research house, the recipients of the analyses or reports are to contact UOBKHM (and not the relevant foreign research house) in Malaysia, at +603-21471988, in respect of any matters arising from, or in connection with, the analysis or report as UOBKHM is the registered person under CMSA to distribute any research analyses in Malaysia.
Singapore	This report is distributed in Singapore by UOB Kay Hian Private Limited ("UOBKH"), which is a holder of a capital markets services licence and an exempt financial adviser regulated by the Monetary Authority of Singapore. Where the report is distributed in Singapore and contains research analyses or reports from a foreign research house, please note: (i) recipients of the analyses or reports are to contact UOBKH (and not the relevant foreign research house) in Singapore in respect of any matters arising from, or in connection with, the analysis or report; and (ii) to the extent that the analyses or reports are delivered to and intended to be received by any person in Singapore who is not an accredited investor, expert investor or institutional investor, UOBKH accepts legal responsibility for the contents of the analyses or reports only to the extent required by law.
Thailand	This report is distributed in Thailand by UOB Kay Hian Securities (Thailand) Public Company Limited, which is regulated by the Securities and Exchange Commission of Thailand.
United Kingdom	This report is being distributed in the UK by UOB Kay Hian (U.K.) Limited, which is an authorised person in the meaning of the Financial Services and Markets Act and is regulated by The Financial Conduct Authority. Research distributed in the UK is intended only for institutional clients.
United States of America ('U.S.')	This report cannot be distributed into the U.S. or to any U.S. person or entity except in compliance with applicable U.S. laws and regulations. It is being distributed in the U.S. by UOB Kay Hian (US) Inc, which accepts responsibility for its contents. Any U.S. person or entity receiving this report and wishing to effect transactions in any securities referred to in the report should contact UOB Kay Hian (US) Inc. directly.

Copyright 2022, UOB Kay Hian Pte Ltd. All rights reserved.

<http://research.uobkayhian.com>

RCB Regn. No. 197000447W