

COMPANY UPDATE

Sembcorp Marine (SMM SP)

Weaker-than-expected Guidance For 2H22; Medium-term Outlook Remains Bright

SMM's 3Q22 business update contained weaker-than-expected guidance for 2H22. Though high labour costs were to blame, resulting in our increased loss estimates for 2022, it will not be an issue after end-22. Nevertheless, we maintain our bullish view on the company as the offshore marine industry remains strong, backed by high commodity prices, with the added benefit of the completion of the merger with KOM in 1Q23. Maintain BUY. Target price: S\$0.156.

WHAT'S NEW

- **Profitability delayed.** Sembcorp Marine (SMM) announced its 3Q22 business update which was slightly disappointing as it disclosed higher-than-expected labour costs which would negatively impact 2H22. The higher-cost labour resulted from SMM having to eschew its traditional low-cost markets like India and Bangladesh during the peak of the COVID-19 pandemic last year and instead resort to non-traditional markets. This labour was supposed to be demobilised in mid-22, however as a result of logistics-related delays, this higher-cost labour will only be sent back by end-22.
- **Other issues will impact profitability in 2H22.** Some of the other issues that SMM's management identified as being the cause of the guidance miss include the timing of new contract wins and its repairs & upgrades segment not receiving as many jobs as expected. During the analyst briefing, SMM also mentioned that while utilities costs have been materially higher on a yoy basis, it is trying to manage such costs. The company also highlighted that the current merger proposal with Keppel Offshore & Marine (KOM) has led to higher professional fees in 2022.
- **Outlook in 2023 remains solid.** While SMM has had a record amount of orders in 2022 (see chart on the next page), 2H22 will be a lull period for the company on the construction side as it undertakes a period of front-end engineering and design as well as and mobilisation of the necessary resources, and thus construction will only commence in earnest in 2023.
- **Watch out for re-entry.** Assuming that the merger between SMM and KOM is completed in 1Q23, the combined entity will have a market capitalisation of around S\$8.3b and a free float of 65%. Based on the market capitalisation of the STI's current component companies, SMM's potential size would qualify it for re-entry into the index after an absence of nearly seven years.

KEY FINANCIALS

Year to 31 Dec (\$m)	2020	2021	2022F	2023F	2024F
Net turnover	1,510	1,862	1,939	2,271	2,693
EBITDA	(380)	(1,028)	8	329	371
Operating profit	(582)	(1,224)	(189)	132	174
Net profit (rep./act.)	(583)	(1,171)	(249)	50	89
Net profit (adj.)	(583)	(1,171)	(249)	50	89
EPS (\$ cent)	(10.6)	(6.5)	(0.7)	0.1	0.2
PE (x)	n.m.	n.m.	n.m.	96.7	54.6
P/B (x)	0.2	0.6	1.2	1.2	1.2
EV/EBITDA (x)	n.m.	n.m.	815.4	19.8	17.6
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net margin (%)	(38.6)	(62.9)	(12.8)	2.2	3.3
Net debt/(cash) to equity (%)	75.7	45.8	57.7	60.9	62.5
Interest cover (x)	(4.1)	(14.8)	(1.4)	1.0	1.3
ROE (%)	n.a.	n.a.	n.a.	1.2	2.2
Consensus net profit	-	-	(0)	10	61
UOBKH/Consensus (x)	-	-	n.m.	5.20	1.46

Source: Sembcorp Marine Limited, Bloomberg, UOB Kay Hian
n.m. : not meaningful; negative P/E, EV/EBITDA reflected as "n.m."

BUY

(Maintained)

Share Price	S\$0.132
Target Price	S\$0.156
Upside	+18.1%

COMPANY DESCRIPTION

Sembcorp Marine is an integrated shipyard offering one-stop engineering solutions for the offshore, marine and energy industries. It demerged from Sembcorp Industries in 3Q20.

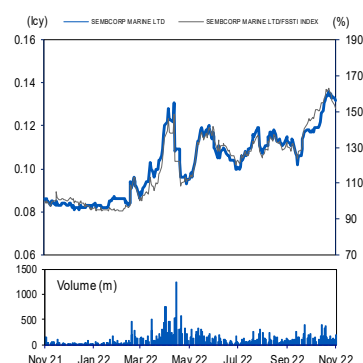
STOCK DATA

GICS sector	Industrials
Bloomberg ticker:	SMM SP
Shares issued (m):	31,389.1
Market cap (\$m):	4,143.4
Market cap (US\$m):	3,029.4
3-mth avg daily t'over (US\$m):	11.4
Price Performance (%)	
52-week high/low	S\$0.136/S\$0.081

1mth	3mth	6mth	1yr	YTD
12.8	23.4	38.9	53.5	61.0

Major Shareholders	%
Temasek Hldgs	54.6
-	-
-	-
FY22 NAV/Share (\$)	0.11
FY22 Net Debt/Share (\$)	0.06

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- **Higher gearing reported in 9M22.** As at end-9M22, SMM had a net debt-to-equity of 0.53x vs 0.44x as at end-1H22. The higher gearing is the result of higher working capital as the company prepares for the start of construction of its new orders.
- **Outlook for order wins.** SMM stated that it remains hopeful of winning more orders in the next 3-6 months and highlighted that it continues to increasingly focus on renewables-related projects. In the longer term, the company is targeting around 40-50% of its orderbook to be related to renewables. SMM highlighted that there are other second-hand cylindrical hulls available for conversion into floating LNG (FLNG) or hydrogen production facilities after its recent order win from New Fortress Energy for two of such conversions into FLNG liquefaction facilities.
- **Repairs & upgrades segment – slower than expected.** Despite the fact that shipping activities have resumed as the global economy has gradually opened up in 2022, SMM stated that the residual effect of COVID-19 means that it will take more time and planning for customers to resume their repair and maintenance programmes. Nevertheless, the company expects a constant base load of LNG carrier repairs, and that its repair & upgrading capacity should be full in 2023 from what it can see at present.

EARNINGS REVISION/RISK

- **Downgrading 2022 estimates.** We have expanded our 2022 loss estimate for SMM from S\$14m to S\$249m to take into account higher labour and other costs as guided by management during yesterday's analyst briefing. While we have not changed our estimates for 2023 and 2024, we highlight that labour costs should decline in 2023 as the company's high-cost labour will be repatriated by end-22.

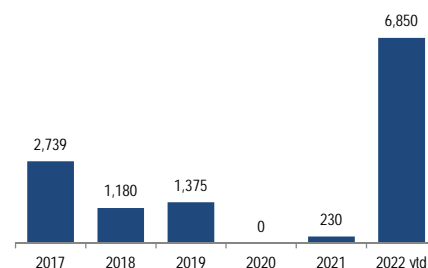
VALUATION/RECOMMENDATION

- **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 over the next 12 months and add to its orderbook instead of its earnings in 2022. That said, SMM will need to start delivering profits in 1H23 in order to prove that it is able to reliably and profitably construct its projects. Our target book-value multiple for SMM of 1.2x reflects our confidence that it will garner such orders, thus leading to positive share price performance. In our view, the offshore construction cycle for both conventional oil and gas and renewables has room for growth in the next few years, especially given the lack of spending by the global oil and gas industry, thus constraining energy supply.

SHARE PRICE CATALYST

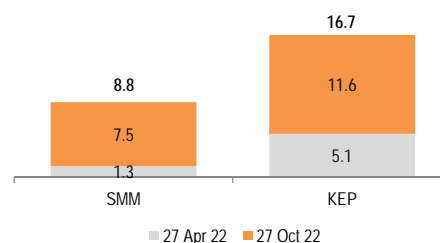
- New orders for rigs, offshore renewable installations or fabrication works as well as repairs and upgrade works for cruise ships and other commercial vessels.

NEW ORDER WINS BY YEAR (\$M)



Source: Bloomberg

GROWTH IN SMM & KEP'S NET ORDERBOOK BETWEEN 1ST AND 2ND MERGER ANNOUNCEMENT (\$B)



Source: SMM

PROFIT & LOSS

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Net turnover	1,862	1,939	2,271	2,693
EBITDA	(1,028)	8	329	371
Deprec. & amort.	197	197	197	197
EBIT	(1,224)	(189)	132	174
Total other non-operating income	0	0	0	0
Associate contributions	1	1	1	1
Net interest income/(expense)	(32)	(80)	(80)	(80)
Pre-tax profit	(1,255)	(267)	54	96
Tax	79	17	(3)	(6)
Minorities	5	1	(0)	(0)
Preferred dividends	0	0	0	0
Net profit	(1,171)	(249)	50	89
Net profit (adj.)	(1,171)	(249)	50	89

BALANCE SHEET

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Fixed assets	3,993	3,911	3,830	3,748
Other LT assets	2,581	2,652	2,818	3,041
Cash/ST investment	1,104	661	102	78
Other current assets	1,922	1,601	1,927	2,244
Total assets	9,600	8,825	8,676	9,111
ST debt	821	800	600	600
Other current liabilities	1,713	1,231	1,431	1,677
LT debt	2,255	2,200	2,000	2,100
Other LT liabilities	486	519	519	519
Shareholders' equity	4,301	4,052	4,102	4,192
Minority interest	24	23	23	23
Total liabilities & equity	9,600	8,825	8,676	9,111

CASH FLOW

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Operating	(589)	(315)	(138)	(102)
Pre-tax profit	(1,224)	(189)	132	174
Tax	(5)	(27)	(18)	(8)
Deprec. & amort.	197	197	197	197
Associates	0	0	0	0
Working capital changes	295	(165)	(319)	(334)
Non-cash items	30	0	0	0
Other operating cashflows	118	(130)	(130)	(130)
Investing	(44)	(85)	(21)	(21)
Capex (growth)	(46)	(100)	(100)	(100)
Capex (maintenance)	0	0	0	0
Investments	0	5	69	69
Proceeds from sale of assets	4	10	10	10
Others	(2)	0	0	0
Financing	964	(43)	(400)	100
Dividend payments	(0)	0	0	0
Issue of shares	1,499	0	0	0
Proceeds from borrowings	0	0	0	100
Loan repayment	(512)	(76)	(400)	0
Others/interest paid	(22)	33	0	0
Net cash inflow (outflow)	331	(443)	(559)	(23)
Beginning cash & cash equivalent	772	1,104	661	102
Changes due to forex impact	1	0	0	0
Ending cash & cash equivalent	1,104	661	102	78

KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
Profitability				
EBITDA margin	(55.2)	0.4	14.5	13.8
Pre-tax margin	(67.4)	(13.8)	2.4	3.5
Net margin	(62.9)	(12.8)	2.2	3.3
ROA	n.a.	n.a.	0.6	1.0
ROE	n.a.	n.a.	1.2	2.2
Growth				
Turnover	23.3	4.1	17.1	18.6
EBITDA	n.a.	n.a.	4,023.7	12.7
Pre-tax profit	n.a.	n.a.	n.a.	77.3
Net profit	n.a.	n.a.	n.a.	77.3
Net profit (adj.)	n.a.	n.a.	n.a.	77.3
EPS	n.a.	n.a.	n.a.	77.3
Leverage				
Debt to total capital	41.6	42.4	38.7	39.0
Debt to equity	71.5	74.0	63.4	64.4
Net debt/(cash) to equity	45.8	57.7	60.9	62.5
Interest cover (x)	(14.8)	(1.4)	1.0	1.3

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