

9 June 2020

Energy & Petrochemicals | Oil & Gas Services

Sembcorp Industries (SCI SP)

Buy (Maintained)

Future Focus: Energy And Urban; Keep BUY

- Keep BUY with a higher SOP-derived SGD2.11 TP from SGD2.00, 38% upside.** Sembcorp Marine (SMM SP, BUY, TP: SGD1.13) and Sembcorp Industries have jointly announced a proposal for SMM's SGD2.1bn recapitalisation and de-merger, as SCI's shareholders receive SMM shares. We view the proposal positively, as this will enable SCI to focus on its energy and urban development businesses. Hence, we lower our SOP conglomerate discount. Even if the offshore business takes a longer time to recover, SCI will not be adversely affected after the de-merger, in our view.
- 5-for-1 SMM rights issue.** SMM will issue rights at SGD0.20/rights share, representing a 31% discount to the theoretical ex-rights price based on a 5-day volume weighted average price of SGD0.74. SCI has undertaken to subscribe for up to SGD1.5bn of rights by setting off the SGD1.5bn subordinated loan previously extended to SMM. Temasek has agreed to sub-underwrite the remaining SGD0.6bn.
- De-merger of SMM and SCI via distribution in specie.** Post rights issue, SCI will distribute its holdings of SMM shares to its shareholders. The latter will receive between 427 and 491 SMM shares for every 100 SCI shares with no cash outlay required. This will allow both companies to focus on their respective industries, in our view. Temasek will become a significant direct shareholder of SMM, with a stake of at least 29%.
- SMM shareholders' approvals are required:** An ordinary resolution to approve the rights issue and a whitewash resolution in respect of the proposed distribution, as this may result in Temasek holding >30% of SMM's shares. SCI's shareholders will separately need to approve the resolution for proposed distribution. All these resolutions are inter-conditional.
- We cut FY20F-22F earnings.** As SMM will cease to be a subsidiary of SCI upon distribution, we have removed the former's impact on the latter's financials. We cut FY20F earnings by 9%, given the more challenging oil & gas sector – as the distribution should be done in 4Q20 – and cut FY21F-22F earnings, as SMM's forecasted positive earnings will not be consolidated into SCI.
- Our new TP of SGD2.11 factors in the proposal.** This is derived from SOP, incorporating SMM's new TP of SGD1.13 and a lower conglomerate discount of 20% (previously 25%) applied only on the energy and urban businesses (no discount for SMM). Post distribution, our SCI TP will fall to SGD1.30.

Target Price (Return): SGD2.11 (37.9%)
 Price: SGD1.53
 Market Cap: USD1,965m
 Avg Daily Turnover (SGD/USD): 13.7m/9.65m

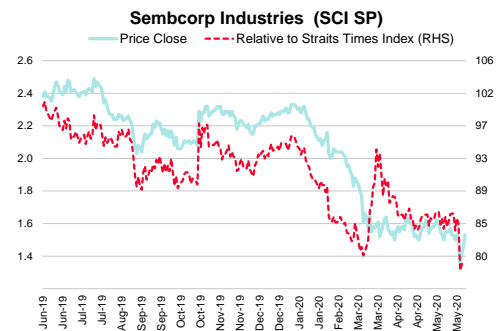
Analyst

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Share Performance (%)

| | YTD | 1m | 3m | 6m | 12m |
|----------------------------|-------------|--------|--------|--------|--------|
| Absolute | (33.2) | (5.6) | (17.8) | (29.5) | (35.7) |
| Relative | (20.0) | (12.2) | (10.4) | (17.6) | (25.2) |
| 52-wk Price low/high (SGD) | 1.36 – 2.49 | | | | |



Source: Bloomberg

| Forecasts and Valuation | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
|---------------------------------|--------|--------|---------|---------|---------|
| Total turnover (SGDm) | 11,689 | 9,618 | 9,135 | 6,501 | 6,940 |
| Recurring net profit (SGDm) | 347 | 395 | 315 | 390 | 403 |
| Recurring net profit growth (%) | (9.4) | 13.8 | (20.3) | 23.9 | 3.3 |
| Recurring P/E (x) | 7.87 | 6.92 | 8.68 | 7.00 | 6.78 |
| P/B (x) | 0.5 | 0.5 | 0.8 | 0.7 | 0.7 |
| P/CF (x) | 6.50 | 4.13 | 29.24 | na | na |
| Dividend Yield (%) | 2.6 | 3.3 | 2.3 | 2.9 | 3.0 |
| EV/EBITDA (x) | 9.01 | 8.26 | 7.65 | 8.79 | 10.44 |
| Return on average equity (%) | 5.8 | 4.1 | 6.6 | 10.6 | 10.1 |
| Net debt to equity (%) | 110.9 | 114.6 | 196.6 | 209.3 | 249.8 |

Source: Company data, RHB

9 June 2020

Energy & Petrochemicals | Oil & Gas Services

Financial Exhibits

| Asia | Financial summary (SGD) | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
|---|-------------------------------------|---------------|---------------|----------------|----------------|----------------|
| Singapore | Recurring EPS | 0.19 | 0.22 | 0.18 | 0.22 | 0.23 |
| Energy & Petrochemicals | DPS | 0.04 | 0.05 | 0.04 | 0.04 | 0.05 |
| Sembcorp Industries | BVPS | 3.36 | 3.40 | 1.98 | 2.15 | 2.31 |
| SCI SP | Return on average equity (%) | 5.8 | 4.1 | 6.6 | 10.6 | 10.1 |
| Buy | | | | | | |
| | Valuation metrics | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
| Valuation basis | Recurring P/E (x) | 7.87 | 6.92 | 8.68 | 7.00 | 6.78 |
| SOP. | P/B (x) | 0.5 | 0.5 | 0.8 | 0.7 | 0.7 |
| | FCF Yield (%) | (25.2) | (9.6) | (36.8) | (49.9) | (70.0) |
| Key drivers | Dividend Yield (%) | 2.6 | 3.3 | 2.3 | 2.9 | 3.0 |
| Start-up of key utilities projects. | EV/EBITDA (x) | 9.01 | 8.26 | 7.65 | 8.79 | 10.44 |
| | EV/EBIT (x) | 17.05 | 16.20 | 15.80 | 15.49 | 19.45 |
| Key risks | | | | | | |
| De-merger with SMM not completed. | | | | | | |
| Company Profile | | | | | | |
| SCI is a leading energy, water, and urban group operating globally. | | | | | | |
| | Income statement (SGDm) | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
| | Total turnover | 11,689 | 9,618 | 9,135 | 6,501 | 6,940 |
| | Gross profit | 920 | 892 | 639 | 488 | 694 |
| | EBITDA | 1,262 | 1,391 | 1,361 | 1,267 | 1,284 |
| | Depreciation and amortisation | (595) | (682) | (702) | (548) | (595) |
| | Operating profit | 667 | 709 | 659 | 719 | 689 |
| | Net interest | (421) | (450) | (481) | (432) | (432) |
| | Pre-tax profit | 420 | 295 | 341 | 481 | 504 |
| | Taxation | (88) | (78) | (45) | (71) | (86) |
| | Reported net profit | 347 | 247 | 315 | 390 | 403 |
| | Recurring net profit | 347 | 395 | 315 | 390 | 403 |
| | Cash flow (SGDm) | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
| | Change in working capital | (389) | (379) | (863) | (1,471) | (1,989) |
| | Cash flow from operations | 420 | 662 | 93 | (513) | (1,031) |
| | Capex | (1,107) | (925) | (1,100) | (850) | (880) |
| | Cash flow from investing activities | (1,384) | (680) | (1,490) | (1,167) | (1,219) |
| | Dividends paid | (71) | (71) | (89) | (63) | (78) |
| | Cash flow from financing activities | 520 | 633 | 2,136 | 2,056 | 1,431 |
| | Cash at beginning of period | 2,687 | 1,925 | 1,767 | 1,566 | 2,832 |
| | Net change in cash | (444) | 615 | 739 | 376 | (819) |
| | Ending balance cash | 2,218 | 2,523 | 2,493 | 1,932 | 2,001 |
| | Balance sheet (SGDm) | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
| | Total cash and equivalents | 1,925 | 1,767 | 1,566 | 2,832 | 2,001 |
| | Tangible fixed assets | 11,672 | 11,739 | 8,614 | 9,436 | 10,285 |
| | Total investments | 2,113 | 2,090 | 2,695 | 3,240 | 3,820 |
| | Total assets | 23,321 | 23,252 | 18,255 | 20,623 | 22,532 |
| | Short-term debt | 1,862 | 2,643 | 2,388 | 3,645 | 4,645 |
| | Total long-term debt | 8,870 | 8,157 | 8,402 | 9,659 | 10,659 |
| | Total liabilities | 15,383 | 15,373 | 13,564 | 15,620 | 17,206 |
| | Total equity | 7,938 | 7,879 | 4,691 | 5,003 | 5,326 |
| | Total liabilities & equity | 23,321 | 23,252 | 18,255 | 20,623 | 22,532 |
| | Key metrics | Dec-18 | Dec-19 | Dec-20F | Dec-21F | Dec-22F |
| | Revenue growth (%) | 29.5 | (17.7) | (5.0) | (28.8) | 6.8 |
| | Recurrent EPS growth (%) | (9.2) | 13.8 | (20.3) | 23.9 | 3.3 |
| | Gross margin (%) | 7.9 | 9.3 | 7.0 | 7.5 | 10.0 |
| | Operating EBITDA margin (%) | 10.8 | 14.5 | 14.9 | 19.5 | 18.5 |
| | Net profit margin (%) | 3.0 | 2.6 | 3.4 | 6.0 | 5.8 |
| | Capex/sales (%) | 9.5 | 9.6 | 12.0 | 13.1 | 12.7 |
| | Interest cover (x) | 1.31 | 1.22 | 1.12 | 1.50 | 1.39 |

Source: Company data, RHB

Figure 1: SOP valuation

| Segments | Shares (m) | Stake | Price (SGD) | Value (SGDm) | Value/share (SGD) | Remarks |
|---|------------|-------|-------------|--------------|-------------------|---------------------------|
| SMM | 1,274.3 | 61% | 1.13 | 1,440 | 0.81 | Based on RHB's TP for SMM |
| Energy | | | | 2,212 | 1.24 | 9x FY20F P/E |
| Urban development | | | | 688 | 0.39 | 9x FY20F P/E |
| Total SOP | | | | 4,340 | 2.43 | No. of SCl shares =1786m |
| Conglomerate discount (only for energy and urban) | | | | 20% | | |
| SOTP after discount | | | | 3,760 | 2.11 | |

Note: After the distribution in specie, SCl's TP will fall to SGD1.30 – based on a 20% discount to the energy and urban businesses' value
 Source: Company data, RHB

Recommendation Chart



| Date | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 2020-05-20 | Buy | 2.00 | 1.55 |
| 2020-02-24 | Buy | 2.33 | 1.95 |
| 2020-02-07 | Buy | 2.68 | 2.03 |
| 2019-11-15 | Buy | 0.68 | 2.26 |
| 2019-09-18 | Buy | 2.68 | 2.18 |
| 2017-05-04 | Neutral | 3.20 | 3.15 |

Source: RHB, Bloomberg

Source: RHB, Bloomberg

RHB Guide to Investment Ratings

| | |
|---------------------|--|
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| Trading Buy: | Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain |
| Neutral: | Share price may fall within the range of +/- 10% over the next 12 months |
| Take Profit: | Target price has been attained. Look to accumulate at lower levels |
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| Not Rated: | Stock is not within regular research coverage |

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