

# Sembcorp Marine (SMM SP)

Energy &amp; Petrochemicals - Oil &amp; Gas Services

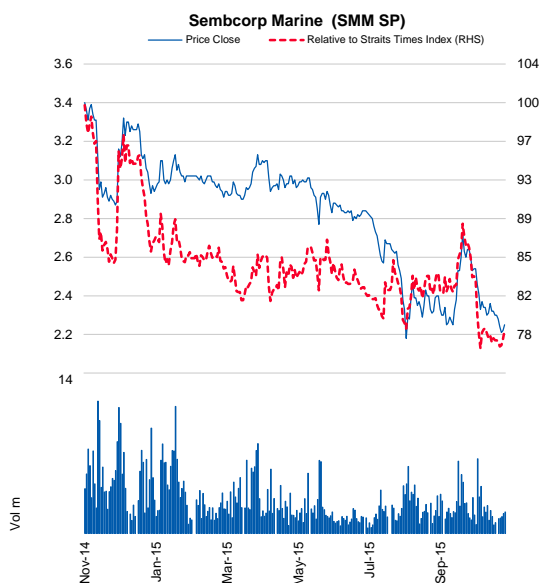
Market Cap: USD3,302m

**Sell** (Maintained)

 Target Price: **SGD2.00**

 Price: **SGD2.25**

## First Cracks In The Dam

 Macro ◆◆◆  
 Risks ◆◆◆  
 Growth ◆  
 Value ◆


Source: Bloomberg

Avg Turnover (SGD/USD)	5.81m/4.13m
Cons. Upside (%)	7.1
Upside (%)	-11.1
52-wk Price low/high (SGD)	2.18 - 3.40
Free float (%)	39
Share outstanding (m)	2,089
<b>Shareholders (%)</b>	
Sembcorp Industries	60.6

### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(31.0)	(14.8)	(12.1)	(25.5)	(33.4)
Relative	(17.7)	(11.0)	(7.2)	(9.7)	(22.1)

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SembMarine has suffered its first formal rig contract cancellation, with MP Drilling canning its USD214.3m Pacific Class 400 (PC400) premium jack-up rig on various factors, which include cracks on all three of the rig's legs. Maintain SELL and SGD2.00 TP (11% downside) as this has negative implications over the company's build quality. This is also the sixth in a growing number of rigs facing non-delivery from its yards.

- ◆ **Build quality the key point of contention.** Marco Polo Drilling (I) Pte Ltd (MP Drilling) has, according to its press statement, terminated its rig under construction at PPL Shipyard Pte Ltd (PPL) due to "various factors, including cracks found on all three legs of the new rig during two rounds of tests, notwithstanding repair works carried out by PPL after the first round of tests". We note that Sembcorp Marine's (SembMarine) announcement did not deny that cracks existed on the rig's legs, but stated that it "disagrees with the allegations" and "will regard this as repudiatory breach of the contract". Important details – such as the number, severity, exact locations of the cracks and whether the classification societies have had a chance to perform non-destructive testing to verify structural integrity – have not emerged.
- ◆ **Expect substantial profit reversal in 4Q15.** With the rig worth USD214.3m and at nearly full completion, we expect a SGD35m-40m profit reversal in 4Q15. This assumes mid-teen margins for the rig, above SembMarine's c.10% blended margins as this was being built to its proprietary design. This prompts us to lower FY15F earnings by 9%. Our TP, based on 11x blended FY15F/FY16F P/Es, is unaffected, being substantially weighted towards FY16 earnings.
- ◆ **Six jack-up rigs now facing non-delivery.** As stated in our 23 Oct report, [A Massive Miss](#), SembMarine may likely face cancellations on the jack-up rigs, on which it reversed profits in 3Q15. This first officially cancelled one is now the sixth potentially undelivered jack-up rig on its books, with a >USD1.2bn value in total. Should resale values fall below costs less deposits, SembMarine may have to take in further losses.
- ◆ **Negative outlook compounded.** This cancellation raises another angle into the negative outlook for SembMarine, with the issue of build quality now compounding the general market woes. Maintain SELL and SGD2.00 TP (11% downside) on 11x blended FY15F/FY16F P/Es.

Forecasts and Valuations	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F	
Total turnover (SGDm)	5,526	5,833	4,829	5,726	5,540	
Reported net profit (SGDm)	556	554	308	405	388	
Recurring net profit (SGDm)	553	558	330	405	388	
Recurring net profit growth (%)	2.3	0.9	(40.9)	22.8	(4.3)	
Recurring EPS (SGD)	0.27	0.27	0.16	0.19	0.19	
DPS (SGD)	0.13	0.13	0.10	0.10	0.10	
Recurring P/E (x)	8.5	8.4	14.2	11.6	12.1	
P/B (x)	1.75	1.58	1.59	1.54	1.50	
P/CF (x)	5.0	na	na	11.0	5.9	
Dividend Yield (%)	5.8	5.8	4.4	4.4	4.4	
EV/EBITDA (x)	4.4	6.0	11.1	9.1	8.9	
Return on average equity (%)	21.7	19.6	10.4	13.5	12.6	
Net debt to equity (%)		net cash	21.2	73.0	79.5	67.5
Our vs consensus EPS (adjusted) (%)			(28.0)	(8.6)	(7.1)	

Source: Company data, RHB

## Financial Exhibits

<b>Profit &amp; Loss (SGDm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Total turnover	5,526	5,833	4,829	5,726	5,540
Cost of sales	(4,818)	(4,989)	(4,219)	(4,969)	(4,808)
<b>Gross profit</b>	<b>708</b>	<b>844</b>	<b>610</b>	<b>758</b>	<b>731</b>
Gen & admin expenses	(148)	(152)	(150)	(177)	(172)
Other operating costs	85	16	5	30	30
<b>Operating profit</b>	<b>644</b>	<b>707</b>	<b>465</b>	<b>610</b>	<b>590</b>
Operating EBITDA	745	822	591	759	743
Depreciation of fixed assets	(101)	(115)	(126)	(148)	(153)
<b>Operating EBIT</b>	<b>644</b>	<b>707</b>	<b>465</b>	<b>610</b>	<b>590</b>
Net income from investments	16	10	(25)	(25)	(25)
Interest income	10	10	9	10	10
Interest expense	(8)	(21)	(49)	(85)	(93)
Exceptional income - net	3	(5)	(26)	-	-
<b>Pre-tax profit</b>	<b>665</b>	<b>701</b>	<b>374</b>	<b>509</b>	<b>482</b>
Taxation	(77)	(106)	(60)	(92)	(82)
Minority interests	(33)	(41)	(6)	(13)	(12)
<b>Profit after tax &amp; minorities</b>	<b>556</b>	<b>554</b>	<b>308</b>	<b>405</b>	<b>388</b>
<b>Reported net profit</b>	<b>556</b>	<b>554</b>	<b>308</b>	<b>405</b>	<b>388</b>
<b>Recurring net profit</b>	<b>553</b>	<b>558</b>	<b>330</b>	<b>405</b>	<b>388</b>

Source: Company data, RHB

<b>Cash flow (SGDm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
<b>Operating profit</b>	<b>644</b>	<b>707</b>	<b>465</b>	<b>610</b>	<b>590</b>
<b>Depreciation &amp; amortisation</b>	<b>101</b>	<b>115</b>	<b>126</b>	<b>148</b>	<b>153</b>
<b>Change in working capital</b>	<b>369</b>	<b>(1,322)</b>	<b>(1,077)</b>	<b>(163)</b>	<b>213</b>
Other operating cash flow	(123)	84	(26)	-	(0)
<b>Operating cash flow</b>	<b>991</b>	<b>(417)</b>	<b>(512)</b>	<b>596</b>	<b>956</b>
Interest received	11	11	9	10	10
Interest paid	(11)	(19)	(49)	(85)	(93)
Dividends received	1	-	-	-	-
Tax paid	(54)	(83)	(60)	(92)	(82)
<b>Cash flow from operations</b>	<b>938</b>	<b>(508)</b>	<b>(612)</b>	<b>429</b>	<b>791</b>
Capex	(815)	(739)	(700)	(400)	(150)
Other new investments	(2)	-	-	-	-
Other investing cash flow	18	(5)	2	-	-
<b>Cash flow from investing activities</b>	<b>(799)</b>	<b>(744)</b>	<b>(698)</b>	<b>(400)</b>	<b>(150)</b>
Dividends paid	(272)	(272)	(313)	(313)	(313)
Proceeds from issue of shares	1	(12)	-	-	-
Increase in debt	438	964	1,200	(199)	(198)
Other financing cash flow	(32)	(13)	-	-	-
<b>Cash flow from financing activities</b>	<b>135</b>	<b>668</b>	<b>887</b>	<b>(512)</b>	<b>(511)</b>
Cash at beginning of period	1,409	1,695	1,079	653	170
<b>Total cash generated</b>	<b>275</b>	<b>(584)</b>	<b>(424)</b>	<b>(484)</b>	<b>130</b>
Forex effects	11	(7)	-	-	-
<b>Implied cash at end of period</b>	<b>1,695</b>	<b>1,103</b>	<b>655</b>	<b>170</b>	<b>300</b>

Source: Company data, RHB

## Financial Exhibits

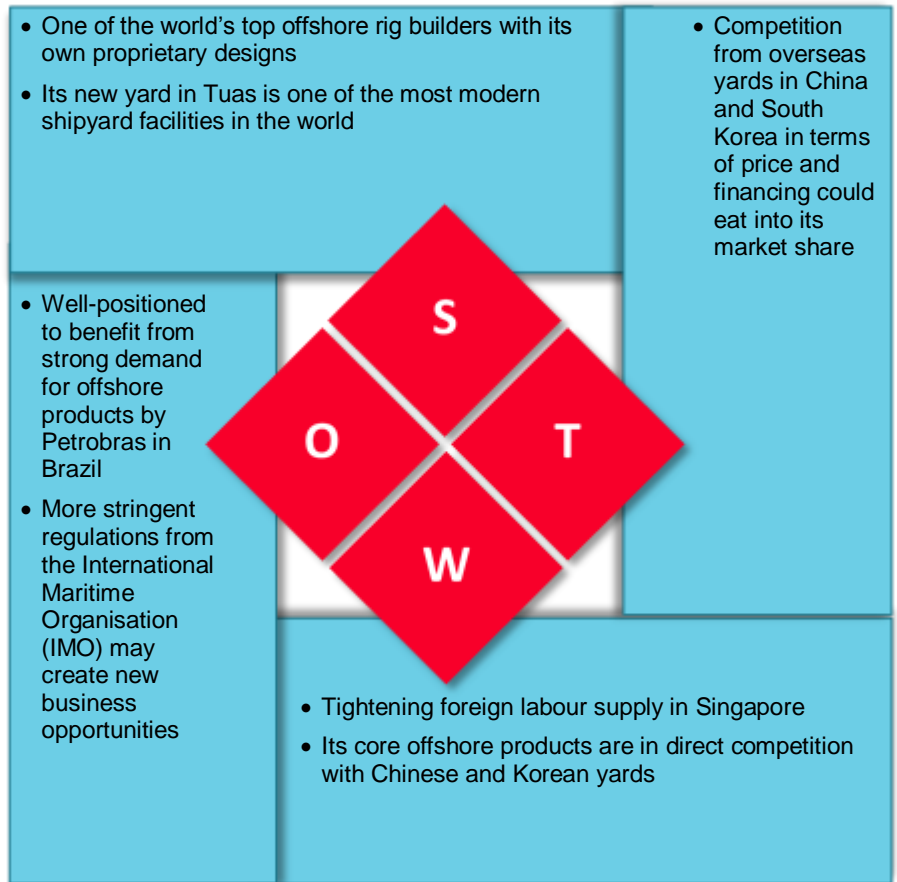
<b>Balance Sheet (SGDm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Total cash and equivalents	1,695	1,079	653	170	300
Inventories	2,084	3,005	3,175	3,765	3,491
Accounts receivable	442	469	926	941	911
Other current assets	0	14	14	14	14
<b>Total current assets</b>	<b>4,221</b>	<b>4,567</b>	<b>4,769</b>	<b>4,890</b>	<b>4,715</b>
Total investments	597	602	577	552	527
Tangible fixed assets	2,394	3,009	3,583	3,835	3,832
Intangible assets	30	53	53	53	53
Total other assets	7	8	8	8	8
Total non-current assets	3,029	3,671	4,221	4,447	4,419
<b>Total assets</b>	<b>7,250</b>	<b>8,238</b>	<b>8,990</b>	<b>9,338</b>	<b>9,134</b>
Short-term debt	166	434	434	434	434
Accounts payable	1,781	1,826	1,588	1,883	1,821
Other current liabilities	1,583	1,189	978	1,125	1,094
<b>Total current liabilities</b>	<b>3,530</b>	<b>3,449</b>	<b>2,999</b>	<b>3,441</b>	<b>3,349</b>
Total long-term debt	600	1,308	2,508	2,309	2,111
Other liabilities	310	350	350	350	350
<b>Total non-current liabilities</b>	<b>910</b>	<b>1,658</b>	<b>2,858</b>	<b>2,659</b>	<b>2,461</b>
<b>Total liabilities</b>	<b>4,441</b>	<b>5,106</b>	<b>5,857</b>	<b>6,100</b>	<b>5,810</b>
Share capital	484	484	484	484	484
Retained earnings reserve	2,193	2,481	2,476	2,568	2,642
<b>Shareholders' equity</b>	<b>2,677</b>	<b>2,965</b>	<b>2,960</b>	<b>3,052</b>	<b>3,126</b>
Minority interests	132	167	173	186	198
<b>Total equity</b>	<b>2,810</b>	<b>3,132</b>	<b>3,133</b>	<b>3,237</b>	<b>3,324</b>
<b>Total liabilities &amp; equity</b>	<b>7,250</b>	<b>8,238</b>	<b>8,990</b>	<b>9,338</b>	<b>9,134</b>

Source: Company data, RHB

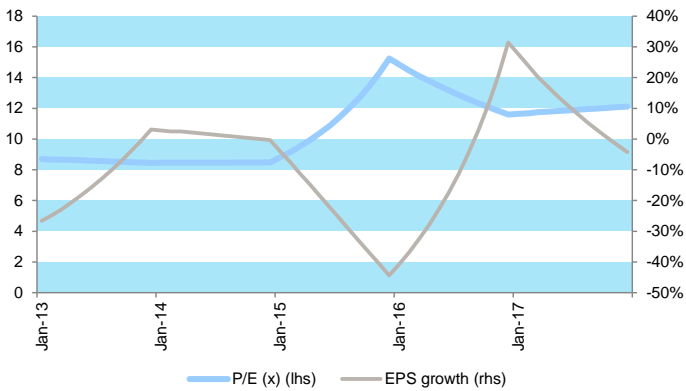
<b>Key Ratios (SGD)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Revenue growth (%)	24.7	5.6	(17.2)	18.6	(3.3)
Operating profit growth (%)	16.2	9.7	(34.2)	31.1	(3.4)
Net profit growth (%)	3.2	(0.3)	(44.4)	31.4	(4.3)
EPS growth (%)	3.1	(0.3)	(44.4)	31.4	(4.3)
BVPS growth (%)	9.8	10.8	(0.2)	3.1	2.4
Operating margin (%)	11.7	12.1	9.6	10.7	10.6
Net profit margin (%)	10.1	9.5	6.4	7.1	7.0
Return on average assets (%)	8.5	7.2	3.6	4.4	4.2
Return on average equity (%)	21.7	19.6	10.4	13.5	12.6
Net debt to equity (%)	(33.1)	21.2	73.0	79.5	67.5
DPS	0.13	0.13	0.10	0.10	0.10
Recurrent cash flow per share	0.45	(0.24)	(0.29)	0.21	0.38

Source: Company data, RHB

# SWOT Analysis

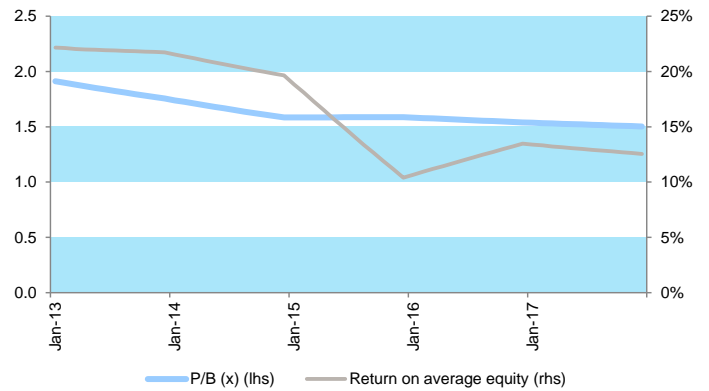


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

## Company Profile

Sembcorp Marine (SembMarine) is a leading marine and offshore engineering group and is renowned for its rig building and offshore conversion.

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-10-23	Sell	2.00	2.46
2015-09-01	Neutral	2.60	2.39
2015-07-30	Neutral	2.60	2.66
2015-07-20	Neutral	2.70	2.84
2015-05-06	Neutral	2.90	3.03
2015-03-31	Neutral	3.10	2.92
2015-02-17	Neutral	3.10	3.02
2014-11-06	Neutral	3.80	3.59
2014-10-09	Buy	4.50	3.68
2014-05-04	Buy	5.00	4.06

Source: RHB, Bloomberg

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**Buy:** Share price may exceed 10% over the next 12 months

**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

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