

# MISC Berhad

*Ambitious Bid for Sizeable USD2bn Mero-3 FPSO*

**TP: RM6.30** (-12.0%)

Last Traded: RM7.16

**SELL**

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*Key takeaways from an engagement session with MISC Bhd's CEO include:- (1) Management is upbeat that current tender prospects (value: northwards of USD4bn) will enable the Group to achieve its FY19 target of USD1bn fresh investment capex, (2) MISC targets to submit an ambitious bid for Petrobras' massive USD2bn Mero-3 FPSO project in Dec-19, (3) IMO2020 Global Sulphur Cap regulations are net neutral to MISC in terms of operational and financial impact, and (4) MISC targets to operate a leaner fleet of Aframaxes over the longer term. We prefer to stay on the sidelines until MISC finally secures a major project to catalyse earnings growth. Maintain Sell on MISC with unchanged TP of RM6.30 based on 15x CY20 P/E.*

**Eyeing Ambitious Offshore Projects.** Management is upbeat on tender prospects, particularly in the Floating Production Offloading Storage (FPSO) space. Whilst bidding activities were slow in 1H19, traction has snowballed in 2H19. Therefore, management is pensive of achieving its target of securing fresh investment capex of USD1bn in FY19 (FY18: USD970mn). YTD, the Group has not secured any substantial amount of investments. When evaluating investments, MISC's decisions are based on project ROE over the asset's lifespan (internal hurdle rate: northwards of 10%). Management believes this is a more accurate gauge of profitability versus the conventional project IRR methodology. Separately, management pre-empted a potential contract announcement for its shipping segment in the next 2 months.

**Dark Horse in Bid for Massive Mero-3.** MISC unveiled prospective pipeline projects valued northwards of USD4bn. A sizeable chunk of this comprises bids for FPSOs - including a large USD2bn Mero-3 FPSO tender by Petrobras. Other details include:- (1) size: 180k bpd production capacity, (2) firm contract tenure: 22.5 years, (3) tender open date: Dec-19, (4) execution/ construction period: 3 years, (5) expected award: Mar-Apr 2020, (6) project start: 2024, and (7) location: Mero pre-salt field, Libra Block, Brazil. Management is sanguine on its prospects of securing this project - given that it is a tight 3-way race between MISC, SBM Offshore and MODEC. Although MISC's competitors are established large players, they have limited capacity for large new projects currently. This is following a slew of sizeable project wins, including SBM's recent success with Mero-2.

**Bid Requirements for Mero-3 Largely Ironed Out.** MISC has identified technical EPCC partners for Mero-3, namely Singapore yard Sembcorp Marine, and Siemens AG. Additionally, management has secured gap funding for the project, which will likely be 70% conventional debt financing (rate: circa 6%). Management is keen to fulfil local Brazilian content requirements, as it would be an advantage for future project bids. This is after investing in local Brazilian capabilities and infrastructure. Nevertheless, if MISC is unable to accommodate local content needs, the Group will opt to pay penalties instead - which is an industry norm. If MISC secures this project, the next step will be securing an equity partner. If the latter turns out to be a strategic collaboration, MISC will

## Share Information

Bloomberg Code	MISC MK
Stock Code	3816
Listing	Main Market
Share Cap (mn)	4,464
Market Cap (RMmn)	31,961
Par Value	1.00
52-wk Hi/Lo (RM)	5.48/7.50
12-mth Avg Daily Vol ('000 shrs)	1,719.0
Estimated Free Float (%)	15.0
Beta	0.9
Major Shareholders (%)	Petronas - 62.7
	EPF - 6.0
	Amanah Saham - 4.8

## Forecast Revision

	FY19	FY20
Forecast Revision (%)	0.0	0.0
Net profit (RMm)	1,715.4	1,876.1
Consensus	1,743	1,847
TA's / Consensus (%)	98.4	101.6
Previous Rating	Sell (Maintained)	

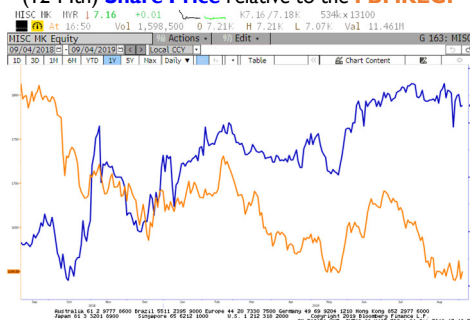
## Financial Indicators

	FY19	FY20
Net Debt/equity (x)	0.2	0.2
FCFPS (sen)	21.0	21.5
P/CFPS (x)	34.1	33.2
ROE (%)	4.8	5.2
ROA (%)	3.3	3.6
NTA/Share (RM)	7.8	7.9
Price/NTA (x)	0.9	0.9

## Share Performance (%)

Price Change	MISC	FBM KLCI
1 mth	(0.7)	-1.7
3 mth	3.6	-2.7
6 mth	5.0	-5.6
12 mth	21.4	-11.7

## (12-Mth) Share Price relative to the FBMKLCI



Source: Bloomberg

likely rope-in the partner during the early project execution stage. On the other hand, a financial partner will likely enter into partnership during the latter stage of completion. Management is keen to de-consolidate project debt financing, which likely alludes to an associate stake in Mero-3.

**Hungry and Not Giving Up on Petrobras FPSOs.** In the worst case scenario whereby MISC does not secure Mero-3, all is not lost. This is because management will submit a fresh bid for Petrobras' ensuing project tenders, including Mero-4. Recall that the Group had previously bid for Mero-2 as well. According to management, knowledge and experience gained from tendering for Mero 2 & 3 will be applicable for Mero-4. Nevertheless, the latter is slightly smaller and less complicated in terms of size and technical requirements.

**IMO2020 is a Non-event for MISC.** Management reiterated that MISC is IMO2020 compliant and ready for its implementation. This is after lead preparation and planning of 2 years. Based on the Group's estimates, implementation of IMO2020 Global Sulphur Cap regulations is net neutral to MISC in terms of operational and financial impact. This is because 6 out of MISC's fleet of 14 VLCCs are installed with scrubbers. Whereas for the rest of MISC's petroleum fleet, there is full cost pass through via time charters. Furthermore, the bulk of MISC's fleet historically operate at ECA (Emission Control Area) zones, which have enforced sulphur caps since 2010.

**Plans to Trim Aframax Fleet.** MISC believes that the lightering business for its Aframaxes will remain robust and profitable in the near term. This is because new port infrastructure for oil exports and pipelines to refineries need at least 5 years to progressively commission in US. Meanwhile, MISC would also progressively shrink its Aframax fleet via disposals of older vessels etc. This is in-line with management's strategy, namely to:- (1) operate a leaner fleet of Aframaxes over the longer term, and (2) charter 3<sup>rd</sup> party vessels for lightering to ease stress on the crew and boat.

**Cautious of Drag in Project Awards.** Whilst MISC's funnel of prospective bids appear exciting, we are cautious of project award delays, particularly for Petrobras' Mero-3. Nevertheless, if the Group manages to secure this ambitious project, we view it as a rerating catalyst. This is because future opportunities for MISC in the lucrative FPSO space will be promising after securing this prestigious contract. In the meanwhile, MISC's earnings growth will be subdued-underpinned by minor fleet expansion from 7 shuttle tankers (delivery: 2H19-20). Apart from Mero-3, another potential catalyst is award of the USD750mn Limbayong FPSO from Petronas. Maintain Sell with unchanged target price (TP) of RM6.30 based on 15x CY20 P/E.

## Earnings Summary

### Income Statement

FYE 31 Dec (RMmn)	2017	2018	2019E	2020F	2021F
Revenue	10,037.7	8,780.3	8,649.2	9,053.4	9,128.6
<b>EBITDA</b>	<b>4,047.7</b>	<b>3,318.9</b>	<b>4,111.9</b>	<b>4,180.2</b>	<b>4,161.9</b>
Depreciation & Amortisation	(2,066.6)	(1,904.2)	(2,143.9)	(2,062.2)	(1,998.7)
Net Financing Cost	(265.0)	(394.6)	(441.5)	(431.3)	(421.2)
Associate & JV	194.8	283.3	233.0	237.6	242.4
El	92.6	40.7	0.0	0.0	0.0
PBT	2,003.5	1,344.1	1,759.5	1,924.3	1,984.4
Tax	(12.9)	(59.8)	(80.7)	(88.3)	(91.0)
MI	(9.2)	27.2	36.7	40.2	41.4
PAT	1,981.4	1,311.5	1,715.4	1,876.1	1,934.8
<b>Core Net Profit</b>	<b>1,888.8</b>	<b>1,270.8</b>	<b>1,715.4</b>	<b>1,876.1</b>	<b>1,934.8</b>

### Per Share Data

Core EPS	(sen)	42.3	28.5	38.4	42.0	43.3
DPS	(sen)	30.0	30.0	30.0	30.0	30.0
Book Value	(RM)	7.8	7.9	8.0	8.1	8.3
NTA	(RM)	7.6	7.7	7.8	7.9	8.1

### Ratios

FYE 31 Dec		2017	2018	2019E	2020F	2021F
<b>Valuations</b>						
Core PER	(x)	16.9	25.2	18.6	17.0	16.5
Dividend yield	(%)	4.2	4.2	4.2	4.2	4.2
EV/EBITDA	(x)	17.2	21.4	17.2	16.8	16.7
P/BV	(x)	0.9	0.9	0.9	0.9	0.9
P/NTA	(x)	0.9	0.9	0.9	0.9	0.9
FCFE Yield	(%)	3.1	0.7	2.9	3.0	3.0

### Profitability ratios

EBITDA margin	(%)	40.3	37.8	47.5	46.2	45.6
EBIT margin	(%)	19.7	16.1	22.8	23.4	23.7
PBT margin	(%)	19.0	14.8	20.3	21.3	21.7
Core Net margin	(%)	18.8	14.5	19.8	20.7	21.2
ROE	(%)	5.2	3.6	4.8	5.2	5.3
ROA	(%)	3.5	2.5	3.3	3.6	3.7

### Liquidity ratios

Current Ratio	(x)	1.0	1.3	1.3	1.4	1.5
Quick Ratio	(x)	1.0	1.2	1.3	1.4	1.4

### Leverage ratios

Total Debt/ Assets	(x)	0.2	0.3	0.2	0.2	0.2
Total Debt/Equity	(x)	0.3	0.4	0.3	0.3	0.3
Net Gearing	(x)	0.2	0.2	0.2	0.2	0.2
Interest coverage	(x)	7.5	3.6	4.5	4.9	5.1

### Growth ratios

Revenue	(%)	4.6	(12.5)	(1.5)	4.7	0.8
EBITDA	(%)	(10.6)	(18.0)	23.9	1.7	(0.4)
PBT	(%)	(31.8)	(32.9)	30.9	9.4	3.1
Core Net Profit	(%)	(32.7)	(32.7)	35.0	9.4	3.1
Core EPS	(%)	(32.7)	(32.7)	35.0	9.4	3.1

### Balance Sheet (RM'mn)

FYE 31 Dec	2017	2018	2019E	2020F	2021F
PPE	22,982.6	23,335.9	22,704.6	22,155.0	21,668.9
Intangibles	844.4	856.9	844.3	831.7	819.1
Others	16,239.7	17,903.2	18,136.2	18,373.8	18,616.2
<b>Non-current Assets</b>	<b>40,066.7</b>	<b>42,096.0</b>	<b>41,685.0</b>	<b>41,360.4</b>	<b>41,104.2</b>
Inventories	198.6	250.0	275.0	302.5	332.8
Trade & Other Receivable	4,034.5	3,803.1	4,183.4	4,601.8	5,061.9
Others	264.0	160.7	160.7	160.7	160.7
Cash & Bank Balances	5,900.7	5,755.6	5,989.9	6,273.4	6,522.1
<b>Current Assets</b>	<b>10,397.8</b>	<b>9,969.4</b>	<b>10,609.0</b>	<b>11,338.3</b>	<b>12,077.5</b>
<b>Total Assets</b>	<b>50,464.5</b>	<b>52,065.4</b>	<b>52,294.0</b>	<b>52,698.8</b>	<b>53,181.7</b>
Borrowings	3,946.3	7,271.4	7,031.4	6,791.4	6,551.4
Other	666.5	650.6	650.6	650.6	650.6
<b>Non-current Liabilities</b>	<b>4,612.8</b>	<b>7,922.0</b>	<b>7,682.0</b>	<b>7,442.0</b>	<b>7,202.0</b>
Borrowings	7,717.6	5,778.5	5,718.5	5,658.5	5,598.5
Trade & Other Payables	2,126.8	1,890.2	2,079.2	2,287.1	2,515.9
Others	107.9	110.5	110.5	110.5	110.5
<b>Current Liabilities</b>	<b>9,952.3</b>	<b>7,779.2</b>	<b>7,908.2</b>	<b>8,056.1</b>	<b>8,224.9</b>
<b>Total Liabilities</b>	<b>14,565.1</b>	<b>15,701.2</b>	<b>15,590.2</b>	<b>15,498.1</b>	<b>15,426.9</b>
Share Capital	8,923.3	8,923.3	8,923.3	8,923.3	8,923.3
Share Premium	0.0	0.0	0.0	0.0	0.0
Others	5,954.2	6,583.8	6,583.8	6,583.8	6,583.8
Retained Earnings	19,961.3	19,844.1	20,220.4	20,757.4	21,353.0
MI	1,060.6	1,013.0	976.3	936.1	894.7
<b>Total Equity</b>	<b>35,899.4</b>	<b>36,364.2</b>	<b>36,703.8</b>	<b>37,200.6</b>	<b>37,754.8</b>
<b>Total Equity + Liabilities</b>	<b>50,464.5</b>	<b>52,065.4</b>	<b>52,294.0</b>	<b>52,698.8</b>	<b>53,181.7</b>

### Cash Flow Statement

FYE 31 Dec (RMmn)	2017	2018	2019E	2020F	2021F
PBT	2,003.5	1,344.1	1,759.5	1,924.3	1,984.4
Depreciation	2,066.6	1,904.2	2,143.9	2,062.2	1,998.7
Taxation	(12.9)	(59.8)	(80.7)	(88.3)	(91.0)
Changes in WC	(574.4)	(339.9)	(449.3)	(475.5)	(504.1)
Others	1,668.6	1,249.0	0.0	0.0	0.0
<b>CFO</b>	<b>5,151.4</b>	<b>4,097.6</b>	<b>3,373.4</b>	<b>3,422.6</b>	<b>3,387.9</b>
Capex	(2,839.2)	(2,292.2)	(1,500.0)	(1,500.0)	(1,500.0)
Other	(330.9)	(1,344.7)	0.0	0.0	0.0
<b>CFI</b>	<b>(3,170.1)</b>	<b>(3,636.9)</b>	<b>(1,500.0)</b>	<b>(1,500.0)</b>	<b>(1,500.0)</b>
Dividend	(1,830.2)	(1,339.1)	(1,339.1)	(1,339.1)	(1,339.1)
Net Borrowing	254.1	1,096.3	(300.0)	(300.0)	(300.0)
Others	(486.5)	(579.8)	0.0	0.0	0.0
<b>CFF</b>	<b>(2,062.6)</b>	<b>(822.6)</b>	<b>(1,639.1)</b>	<b>(1,639.1)</b>	<b>(1,639.1)</b>
<b>Net Cash Flow</b>	<b>(81.3)</b>	<b>(361.9)</b>	<b>234.3</b>	<b>283.5</b>	<b>248.8</b>

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### Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.  
**HOLD** : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.  
**SELL** : Total return is lower than the required rate of return.  
**Not Rated:** The company is not under coverage. The report is for information only.

**Total Return** is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

**Required Rate of Return** of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

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As of Thursday, September 05, 2019, the analyst, Kylie Chan Sze Zan, who prepared this report, has interest in the following securities covered in this report:  
(a) nil

**Kaladher Govindan – Head of Research**

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