



# Sembcorp Industries

## Strategically important sale of SEIL

### SINGAPORE | ENERGY | UPDATE

**7 September 2022**

- Acquisition consideration of S\$2.059bn implies S\$0.8bn/GW of gross installed capacity, which is higher than average comparable transactions of S\$0.5-1bn/GW. We view the transaction as fair given the weak market environment for coal assets.
- Debt-capitalisation ratio improve to 62% from 66% for pro forma 1H22. We believe the Group will leverage its balance sheet and re-invest the proceeds into green assets.
- Sembcorp Industries (SCI) will still be exposed to operational risks of Sembcorp Energy India Limited (SEIL) after the sale through its 15-year exposure to the Deferred Payment Note (DPN).
- We upgrade to ACCUMULATE from NEUTRAL with higher target price of \$3.68 (prev. \$3.27).** We lower FY23e PATMI by 11% as we strip out SEIL's contribution and lower contribution from urban developments. Our target price is raised to \$3.68, still based on 1.2x P/BV, the average of its peers as we roll forward estimates to FY23e.

#### Terms and conditions of proposed sale

SCI announced the proposed sale of SEIL for the equivalent of \$2.059bn, or 1x NAV. The purchaser is the Tanweer Consortium led by Oman Investment Corporation S.A.O.C (OIC), the Ministry of Defence Pension Fund, Oman (MODPF) and Dar Investment SPC (Dar Investment).

On completion, Tanweer Consortium will settle the entire final purchase price through the DPN via a facility provided by SCI under the DPN. The DPN will bear interest at 9% interest (1.8% spread + 7.2% benchmark), minus a greenhouse gas (GHG) emissions intensity reduction incentive rate. This GHG reduction incentive rate is subject to a cap of 180 basis points if these emission targets are met. In other words, the current spread over the benchmark rate will be removed or reduced any time within the 15-year period if the Tanweer Consortium can meet the GHG emissions target. Such adjustments will affect the final purchase price. All outstanding payment under the DPN should be payable in full on the 15<sup>th</sup> anniversary date of the completion, which is also the maturity date. The yearly payments will be recorded under the Group's EBITDA section. Should the outstanding payment obligations not be met, the maturity date will be extended for two years, and for every two years till the monies are paid. The maturity date will not be extended beyond the 24<sup>th</sup> anniversary date of completion.

Shareholders approval is required for the transaction, which is expected in November this year, and the expected completion is six months after EGM.

#### The Positives

**+ Acquisition consideration implies S\$0.8bn/GW of gross installed capacity, higher than average comparable transactions of S\$0.5-1bn/GW.** The acquisition price implies 1x of NTA, which we view as fair given the weak market environment around coal-related assets. SCI will recognise ~\$11mn in gains from the sale.

**+ Debt-capitalisation ratio improve to 62% from 66% for pro-forma 1H22.** We believe the Group will leverage its stronger balance sheet to further its transition to green energy. On a pro forma basis, SCI's total debt as at 30 June 2022 will decrease to \$7.1bn from \$8.7bn due to the deconsolidation of SEIL in SCI's balance sheet. SCI's interest paying capacity will also improve with interest coverage rising to 6.3x in the same period from 5.1x. SCI still has ~\$5bn of borrowing facilities to tap on, which will accelerate the transformation of its portfolio from brown to green.

#### ACCUMULATE (UPGRADED)

LAST CLOSE PRICE	SGD 3.480
FORECAST DIV	SGD 0.160
TARGET PRICE	SGD 3.680
TOTAL RETURN	10.3%

#### COMPANY DATA

BLOOMBERG CODE:	SCI SP
O/S SHARES (MN):	1,786
MARKET CAP (USD mn / SGD mn):	4422 / 6214
52 - WK HI/LO (SGD):	3.51 / 1.78
3M Average Daily T/O (mn):	3.61

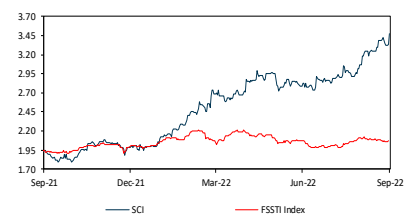
#### MAJOR SHAREHOLDERS (%)

TEMASEK HOLDINGS	49.5%
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#### PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	9.8	20.9	76.5
STI RETURN	(0.9)	0.9	8.6

#### PRICE VS. STI



Source: Bloomberg, PSR

#### KEY FINANCIALS

Y/E Dec (\$, 'mn)	FY20	FY21e	FY22e	FY23e
Revenue	5,447	7,795	9,909	8,844
Gross Profit	787	1,102	1,383	1,224
EBIT	442	614	988	746
NPAT	179	300	911	742
P/NAV (x)	1.8	1.6	1.3	1.1
P/E (x)	39.6	22.3	7.0	8.6
ROE (%)	3.2%	8.1%	20.8%	14.3%

Source: Company, PSR

#### VALUATION METHOD

P/B Multiple @ 1.2x FY23e

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### + \$700mn in receivables from SEIL expected to be repaid within the next 24-48 months.

The Indian Ministry of Power has recently directed Telangana and Andhra Pradesh to settle the overdue receivables within 20-48 months. Should this be adhered to, the Group is expected to receive ~\$700mn in receivables in the next 1-2 years, which will lower the credit risk of SEIL, and by extension the risk for the DPN.

### The Negatives

- **SCI will still be exposed to operational risks of SEIL for at least 15 years after sale.** Even though SEIL will be deconsolidated from SCI's books after the sale, the DPN, which is a form of vendor financing means that SCI will still be exposed to the operational risks of SEIL for at least 15 years after the sale. Should the outstanding payment obligations not be met, the maturity date will be extended for two years, and for every two years till the monies are paid. The maturity date will not be extended beyond the 24<sup>th</sup> anniversary date of completion.

However, we believe this risk is mitigated by both mid- and long- term contracts for SEIL, totalling 85% of SEIL's thermal plant capacity. SEIL will have 570MW up for renewal in 2024 (22% of the power purchase agreement). That said, we view the risk of non-renewal as low given the strong current energy environment. IEX prices remain elevated at ~7,500 Rupees/hr in September vs. an average ~7,600 Rupees/hr in 1H22.

### Outlook

Shareholders approval is required for the transaction, which is expected in November this year, and the expected completion is six months after EGM.

For dividends, we model a ~30% payout ratio, in line with FY21's payout. We expect SCI to pay out 16 cents of dividends (split between final and special due to the special circumstances for FY22) for FY22e, translating to a ~4.9% dividend yield

### ESG

The sale of SEIL will accelerate the Group's transformation to have more of its net profit come from sustainable solutions. As such, we view the transaction as strategically important to the Group's transformation plans (% share of net profit from sustainable solutions will rise to 31% for pro forma 1H22 vs. 25% previously).

SCI's environmental score of 1.28 still lags behind its peers according to data from Bloomberg. We believe the Group's transition from brown to green has the potential to lift its environmental score rating over time. The Group has committed to grow its profit contribution from its sustainable solutions to 70% by 2025 (35% in 2021), which could see greater interest from institutional investors looking for high ESG ranked companies.

### Upgrade to ACCUMULATE from NEUTRAL with higher target price of \$3.68 (prev. \$3.27)

We lower FY23e PATMI by 11% as we strip out SEIL's contribution and lower contribution from urban development. Our target price is raised to \$3.68, still based on 1.2x P/BV, the average of its peers as we roll forward estimates to FY23e.

### Tanweer Consortium and the purchaser

*The Tanweer Consortium is led by OIC, in partnership with MODPF and Dar Investment. OIC is a leading Omani private equity investment company with a strong track record of investments in energy and infrastructure projects amongst others. MODPF is one of Oman's largest pension funds, with significant investments across power and infrastructure. Dar Investment represents the family office of H.E. Sheikh Abdullah Al Salmi, who is the Executive President of Oman's Capital Market Authority and a board member of the Oman Investment Authority.*

*OIC has been SCI's long-term partner in Oman. Both SCI and OIC jointly developed and operated the country's US\$1bn Salalah Independent Power and Water Plant since 2009.*

**Financials**
**Income Statement**

Y/E Dec, (\$'mn)	FY19 #	FY20	FY21	FY22e	FY23e
<b>Revenue</b>	<b>6,735</b>	<b>5,447</b>	<b>7,795</b>	<b>9,909</b>	<b>8,844</b>
Cost of sales	(5,753)	(4,660)	(6,693)	(8,525)	(7,620)
<b>Gross Profit</b>	<b>982</b>	<b>787</b>	<b>1,102</b>	<b>1,383</b>	<b>1,224</b>
General and Administrative expe	(356)	(344)	(432)	(535)	(478)
Other operating income	189	126	140	137	-
Other items	(109)	(127)	(196)	3	-
<b>EBIT</b>	<b>706</b>	<b>442</b>	<b>614</b>	<b>988</b>	<b>746</b>
Net finance expenses	(444)	(464)	(397)	(398)	(385)
Share of results of associates an	186	233	206	513	546
<b>Profit before tax</b>	<b>448</b>	<b>211</b>	<b>423</b>	<b>1,104</b>	<b>907</b>
Taxation	(115)	(32)	(123)	(192)	(166)
<b>Net Profit</b>	<b>333</b>	<b>179</b>	<b>300</b>	<b>911</b>	<b>742</b>
<b>Net Profit (excl. SCM from FY20e)</b>	<b>333</b>	<b>179</b>	<b>300</b>	<b>911</b>	<b>742</b>
<b>Profit attributable to owners</b>	<b>305</b>	<b>157</b>	<b>279</b>	<b>893</b>	<b>724</b>

**Per share data (\$\$ cents)**

Y/E Dec	FY19 #	FY20	FY21	FY22e	FY23e
BVPS	4.4	1.9	2.2	2.7	3.1
DPS	5.0	4.0	5.0	16.0	13.0
EPS	17.1	8.8	15.6	50.0	40.5

**Cash Flow**

Y/E Dec, (\$'mn)	FY19 #	FY20	FY21	FY22e	FY23e
<b>CFO</b>					
<b>Net income</b>	<b>333</b>	<b>179</b>	<b>300</b>	<b>911</b>	<b>742</b>
Adjustments	1,122	872	1,004	1,648	1,695
WC changes	(379)	(453)	(49)	(521)	1
<b>Cash generated from ops</b>	<b>1,076</b>	<b>598</b>	<b>1,255</b>	<b>2,039</b>	<b>2,438</b>
Others	(99)	(103)	(36)	(192)	(166)
<b>Cashflow from ops</b>	<b>977</b>	<b>495</b>	<b>1,219</b>	<b>1,846</b>	<b>2,273</b>
<b>CFI</b>					
CAPEX, net	(925)	(318)	(282)	(510)	(1,108)
Others	474	(963)	182	(577)	127
<b>Cashflow from investments</b>	<b>(451)</b>	<b>(1,281)</b>	<b>(100)</b>	<b>(1,087)</b>	<b>(981)</b>
<b>CFF</b>					
Dividends paid to owners	(71)	(54)	(107)	18	(143)
Proceeds from borrowings, net	86	862	(364)	(200)	(200)
Interest paid	(544)	(515)	(330)	(421)	(417)
Others	(163)	(237)	(54)	-	-
<b>Cashflow from financing</b>	<b>(692)</b>	<b>56</b>	<b>(855)</b>	<b>(603)</b>	<b>(760)</b>
<b>Net change in cash</b>	<b>(166)</b>	<b>(730)</b>	<b>264</b>	<b>156</b>	<b>532</b>
Cash at the start of the period	1,922	1,739	1,013	1,297	1,453
Currency translation	(27)	(27)	(27)	(27)	(26)
Others	-	-	-	-	-
<b>Ending cash</b>	<b>1,739</b>	<b>1,013</b>	<b>1,297</b>	<b>1,453</b>	<b>1,985</b>

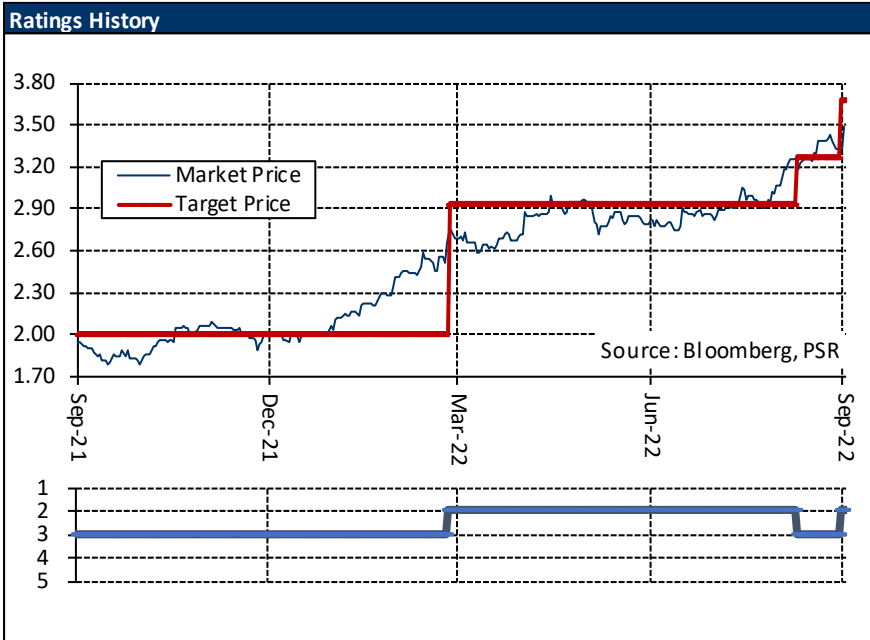
\*nm - not meaningful

**Balance Sheet**

Y/E Dec, (\$'mn)	FY19	FY20	FY21	FY22e	FY23e
<b>ASSETS</b>					
PPE & Investment Properties	11,867	7,339	7,232	8,142	8,750
Others	5,290	3,219	3,230	4,608	4,956
<b>Total non-current assets</b>	<b>17,157</b>	<b>10,558</b>	<b>10,462</b>	<b>12,750</b>	<b>13,706</b>
Cash and cash equivalents	1,767	1,032	1,344	1,429	1,982
Inventories	386	196	222	341	305
Trade and other receivables	2,048	1,571	1,986	2,123	1,894
Others	1,894	205	381	381	381
<b>Total current assets</b>	<b>6,095</b>	<b>3,004</b>	<b>3,933</b>	<b>4,274</b>	<b>4,562</b>
<b>Total Assets</b>	<b>23,252</b>	<b>13,562</b>	<b>14,395</b>	<b>17,024</b>	<b>18,268</b>
<b>LIABILITIES</b>					
Trade and other payables	2,844	1,159	1,708	2,171	1,938
ST borrowings	2,643	627	765	768	768
Others	525	341	432	1,465	2,713
<b>Total current liabilities</b>	<b>6,012</b>	<b>2,127</b>	<b>2,905</b>	<b>4,404</b>	<b>5,418</b>
LT borrowings	8,627	7,350	6,881	6,681	6,481
Others	734	609	691	1,074	886
<b>Total non-current liabilities</b>	<b>9,361</b>	<b>7,959</b>	<b>7,572</b>	<b>7,755</b>	<b>7,367</b>
<b>Total liabilities</b>	<b>15,373</b>	<b>10,086</b>	<b>10,477</b>	<b>12,159</b>	<b>12,786</b>
<b>EQUITY</b>					
Share Capital	566	566	566	566	566
Retained profits	5,827	3,153	3,349	4,278	4,877
Others	1,482	(243)	3	21	39
<b>Total equity</b>	<b>7,875</b>	<b>3,476</b>	<b>3,918</b>	<b>4,865</b>	<b>5,482</b>
<b>Total equity and liabilities</b>	<b>23,248</b>	<b>13,562</b>	<b>14,395</b>	<b>17,024</b>	<b>18,268</b>
<b>Valuation Ratios</b>					
Y/E Dec	FY19 #	FY20	FY21	FY22e	FY23e
P/E (x)	20.4	39.6	22.3	7.0	8.6
P/B (x)	0.8	1.8	1.6	1.3	1.1
EV/EBITDA (x)	22.3	10.6	9.7	7.3	7.4
Dividend yield (%)	1.4%	1.1%	1.4%	4.6%	3.7%
<b>Growth &amp; Margins (%)</b>					
<b>Growth</b>					
Revenue	-42.4%	-19.1%	43.1%	27.1%	-10.7%
Gross profit	6.7%	-19.9%	40.0%	25.5%	-11.5%
EBIT	5.8%	-37.4%	38.9%	60.9%	-24.5%
PBT	6.7%	-52.9%	100.5%	161.0%	-17.8%
<b>Margins</b>					
Gross profit margin	14.6%	14.4%	14.1%	14.0%	13.8%
EBIT margin	10.5%	8.1%	7.9%	10.0%	8.4%
Net profit margin	4.9%	3.3%	3.8%	9.2%	8.4%
<b>Key Ratios</b>					
ROE	4.2%	3.2%	8.1%	20.8%	14.3%
ROA	1.4%	1.0%	2.1%	5.8%	4.2%
Net Gearing (%)	120.7%	199.8%	160.8%	123.7%	96.1%

Source: Company, Phillip Securities Research (Singapore) Estimates

# On September 11, 2020, the Company distributed its holdings of ordinary shares in the capital of a subsidiary, Sembcorp Marine (SCM) to its shareholders. Consequent to the distribution, the performance of the marine segment in the current financial year, for the period from Jan 1, 2020 to Sept 11, 2020 is reported as a discontinued operation with comparative information re-presented accordingly.



### PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

### Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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