MITA No. 010/06/2008

24 April 2009

Keppel Corporation

Downgrade to
SELL
Previous Rating: HOLD
S$6.02
Fair Value: S$4.90

Stock Code:	
Reuters:	KPLM.SI
ISIN Code	BN4
Bloomberg:	KEP SP
Event:	Results

General Data	
Issued Capital (m)	1,593
Mkt Cap (Sm/USm)	9,591 / 6,401
Major Shareholder	Temasek Holdings (21.2%)
Free Float (%)	78
NAV per share (S$)	3.05
Daily Vol 3-mth ('000)	7,527
52Wk High (S$)	12.500
52Wk Low (S$)	3.350

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Caution against over enthusiasm. Downgrade to SELL

Outlier 1Q09. Keppel Corporation's (KepCorp) topline grew 34.7% YoY to S$2.98b while PATMI rose 9% YoY to S$285m. The results exceeded our expectations in view of a strong show from the Offshore and Marine business. The other divisions performed largely in line with our expectations. A key highlight for KepCorp was an improvement in margins in all the divisions. These came in higher than our estimates.

Property, still a concern. Revenue declined to S$222m (-26% YoY) largely due to the completion of trading projects in FY08. Although the 33% YoY decline in bottom-line was faster than its revenue, it would have been worse if it was not mitigated by the increase in contributions from Marina Bay Residences and Reflections at Keppel Bay in 1Q09. Our property analyst has lowered our FY09 revenue and shareholders' profit forecasts to S$720.3m and S$222.7m respectively. Keppel Land has also declared a rights issue where KepCorp is committed to putting in up to S$678m.

Infrastructure: provides some silver lining. This division delivered a strong quarter as it recognised lump sum revenue from its Doha North project and its Keppel Merlimau Cogen plant obtained better market share in Singapore. On an annual basis, we think that the Doha project's lumpy contribution will be smoothened out. We are factoring its Cogen plant to sustain its market share.

Unfounded enthusiasm. We remain cautious on the enthusiastic 50% share price run since its recent low on 4 Mar 09 as fundamental positive changes in the industry have yet to be seen. Oil price continues to hover at sub-50s range while the group has seen a dearth of rig orders despite repeated assurances that the Oil Majors' and National Oil companies' E&P spending "will continue despite the slowdown in the world economy". We also caution investors on expecting similar quantums of dividend payouts as the group hunkers down to conserve cash and remain in a well capitalised position for acquisition opportunities. Our interim dividend is forecasted at 11 S cents, significantly below consensus of 17 S cents. We have shaved our revenue due to weaker property performance but PATMI improves due to upward revision of margins.

Downgrade to SELL. Our SOTP valuation has been bumped up to S$4.90 (prev. S$4.40) due to the run up market value of its associates plus an improvement in margins leading to better earnings. The 19% downside to our fair value is underpinned by weak industry fundamentals.

Year to 31-Dec	Turnover (S$m)	Operating Profit (S$m)	PATMI (S$m)	EPS (cents)	EPS Growth (%)	PER (x)	Div Yield (%)
FY 07	10,431.3	1,050.6	1,130.7	64.9	35.9	9.3	10.6
FY 08	11,805.4	1,238.5	1,098.0	69.0	6.7	8.7	5.6
FY 09F	10,029.5	922.4	957.0	60.0	-12.7	10.0	4.3
FY 10F	9,194.2	914.5	864.2	54.2	-9.7	11.1	4.2

Exhibit 1: SOTP Valuation

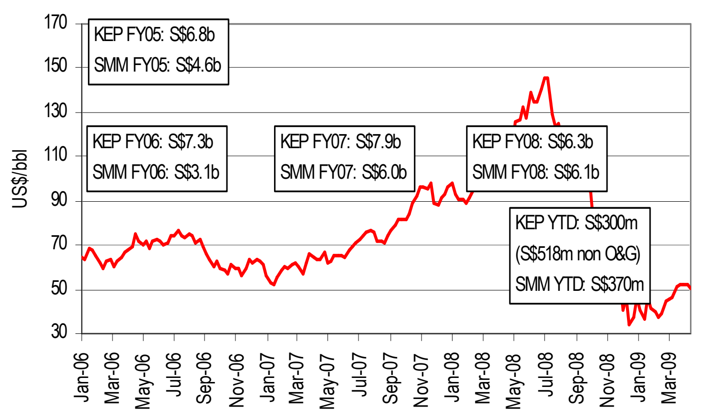
Entities	Direct stake (%)	Valuation	Mkt value (S$m)	% of SOTP	Comment
Offshore & Marine					
Keppel Offshore & Marine Ltd	100%	11x FY09 PER	4,674	54%	Prev 10x. Raised to match SMM
Property					
Keppel Bay Project	70%	Residual value	854	10%	Net profit est of S$1.36b
Keppel Land	53%	50% RNAV	551	6%	Current RNAV: 2613. Prev: 2,653
Infrastructure					
Keppel T&T	80%	Market value	450	5%	
Power & Environmental	100%	10x FY09 PER	1,182	14%	Discount to 13x peers due to thin margins
Investments					
Singapore Petroleum Company	45%	OIR valuation	701	8%	Changed to OIR valuation
K1 Ventures	36%	Market value	97	1%	
K-REIT	31%	Market value	140	2%	
Shares outstanding			1,596		
Total			**8,649**		Discount introduced as diversified businesses accentuate stress to valuation in declining economy.
Discount			**10%**		
SOTP Fair Value			4.90		

Keppel FY07 PER	9.3
Keppel FY08 PER	8.7
Keppel FY09F PER	10.0

Note: Market value based on 23 Apr 2009 closing prices

Source: OIR estimates

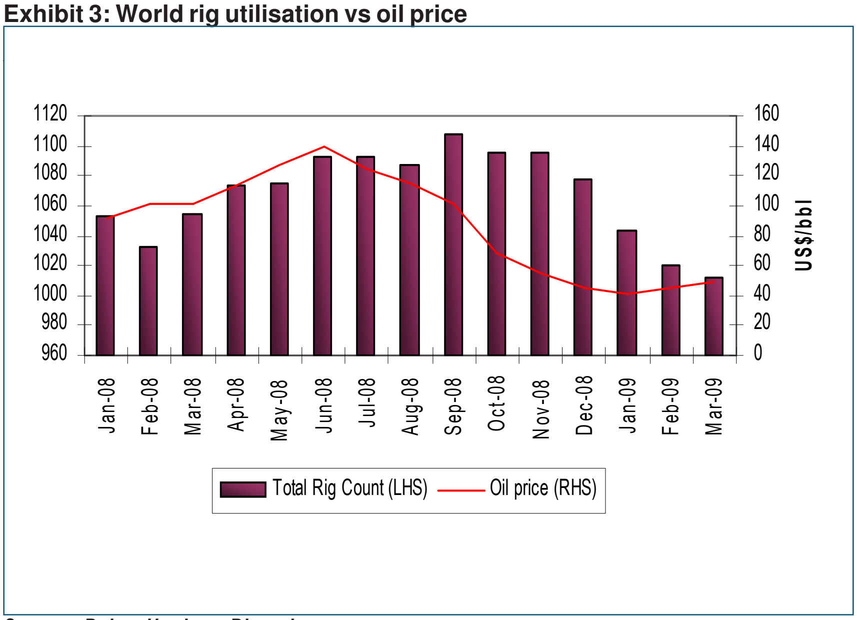
Exhibit 2: Contract win trends



Source: Company data

Offshore rig market. We are maintaining our assumptions of S$2b worth of FY09 contract wins for Keppel's Offshore and Marine division (vs FY08: S$5.2b, FY07: S$7.4b). While KepCorp's yards have their work cut out with a large order book to fulfil, we are mindful that tweaks in customer repayment schedules could occur (pushing payments further back) as the credit situation continues to be stuck in winter mode. Adding to slower capex plans, we iterate that new rig prices are expected to soften with lower steel and other commodity prices. This would mean that KepCorp would have to secure more projects to sustain its future revenue momentum. Exhibit 2 also shows that the downward trend of utilisation of rigs remains unabated. This could cause Oil Majors and National Oil Companies to hold off plans to purchase new deepwater capable equipment as rigs could go on the block at fire sale prices for companies that have been over stretched financially.

Exhibit 3: World rig utilisation vs oil price



Source: Baker Hughes, Bloomberg

Korean yards still hold sway for drillships. Petrobras recently visited Korea and Singapore in an effort to explore methods to deploy their exploration plans in the upcoming decade. In a statement issued while in Korea, Petrobras' CFO indicated that the company required about 240 vessels to fulfil its needs for the next 5-6 years. He also said that Petrobras would also issue tenders for eight floating product storage and offloading (FPSO) units and seven drill ships "soon". While the market has turned positive on the Singapore yards on the basis of winning some contracts, we caution against over enthusiasm as it seems contracts to be initially awarded are new drillships and new FPSOs, a forte that the Korean yards hold. Should FPSO conversions take precedent in view of tighter credit and faster build cycles, KepCorp and SMM would stand in good stead for contract wins. Petrobras has also indicated that it would "prefer" projects to engage its local workforce in Brazil. However, we think that there would be concessions as it might not be possible for it to meet its massive vessel delivery schedule with labour constraints in Brazil.

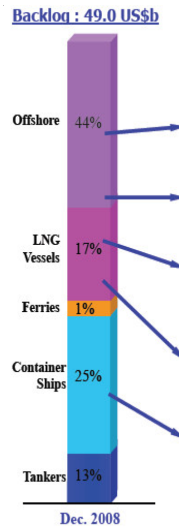
Exhibit 4: Drillship Dominance by Korean yards

Drillships

Owner (Manager)	Rig Name	Design	Water depth (ft)	Order Year	Shipyard	Est. Cost (USDm)	In Service	Contract status at time of order
MPF	MPF-01	MPF MPF 1000	10,000	2006		950		Speculative
Stena	Stena Forth	Stena Stena/Samsung	7,500	2006	Samsung Heavy Industries	760	Jul-09	Speculative
Transocean	Dhirubhai Deepwater KG1	Samsung/Saipem Saipem 10000	12,000	2006	Samsung Heavy Industries	738	May-09	Speculative
Transocean	Dhirubhai Deepwater KG2	Samsung/Saipem Saipem 10000	10,000	2006	Samsung Heavy Industries	733	Oct-09	Speculative
Transocean	Discoverer Americas	Transocean Offshore Enhanced Enterprise Class	10,000	2006	Daewoo	664	Apr-09	Hydro
Transocean	Discoverer Clear Leader	Transocean Offshore Enhanced Enterprise Class	12,000	2006	Daewoo	674	Mar-09	Chevron
Transocean	Discoverer Inspiration	Transocean Offshore Enhanced Enterprise Class	12,000	2006	Daewoo	712	Oct-09	Chevron
Transocean	Petrobras 10000		10,000	2006	Samsung Heavy Industries	750	Jun-09	Petrobras
Frontier Drilling	Bully 1	GustoMSC PRD12,000	12,000	2007	Shanghai Shipyard & Chengxi Shipyard Co., Ltd.	610	Jan-10	Shell
Frontier Drilling	Bully 2	GustoMSC PRD12,000	12,000	2007	Shanghai Shipyard & Chengxi Shipyard Co., Ltd.	632	Jul-10	Shell
Ocean Rig	Cardiff Marine Drsh Tbn1		10,000	2007	Samsung Heavy Industries	713	Dec-10	Speculative
Ocean Rig	Cardiff Marine Drsh Tbn2		10,000	2007	Samsung Heavy Industries	713	Mar-11	Speculative
Pacific Drilling Services	Tanker Pacific Drsh Tbn1	Samsung 10000	7,500	2007	Samsung Heavy Industries	632	Sep-10	Speculative
Pacific Drilling Services	Tanker Pacific Drsh Tbn2	Samsung 10000	7,500	2007	Samsung Heavy Industries	632	Mar-11	Speculative
Pride	Pride Drsh Tbn1	Samsung/Saipem Saipem 10000	10,000	2007	Samsung Heavy Industries	730	Feb-10	Speculative
Pride	Pride Drsh Tbn2		10,000	2007	Samsung Heavy Industries	725	Jun-10	Speculative
Pride	Pride Drsh Tbn3		10,000	2007	Samsung Heavy Industries	720	Jan-11	Petrobras
Saipem	Saipem 12000	Samsung/Saipem Saipem 10000	12,000	2007	Samsung Heavy Industries	660	Mar-10	Total
Schahin	Petrobras Drsh Tbn2		10,000	2007	Samsung Heavy Industries	830	Jun-10	Petrobras
Seadrill	West Gemini	Samsung 10000	10,000	2007	Samsung Heavy Industries	615	Jul-10	Speculative
Transocean	Deepwater Champion	GustoMSC P10000	10,000	2007	Hyundai Heavy Industries	786	Sep-10	Speculative
Transocean	Discoverer Luanda	Transocean Offshore Enhanced Enterprise Class	7,500	2007	Daewoo	690	Jul-10	BP
Vantage Drilling	Platinum Explorer		10,000	2007	Daewoo	761	Nov-10	Speculative
Vantage Drilling	Titanium Explorer		12,000	2007	Daewoo	782	Jul-11	Speculative
Delba	Delba VII		10,000	2008	Samsung Heavy Industries	700	Mar-12	Petrobras
Delba	Delba VIII		10,000	2008	Samsung Heavy Industries	740	Jun-12	Petrobras
Etesco	ET-VIII		10,000	2008	Samsung Heavy Industries	709	Jan-12	Petrobras
Noble	Noble Drsh Tbn1	Huisman Globetrotter	10,000	2008	STX Heavy Industries	585	Oct-11	Speculative
Ocean Rig	DryShips Drsh Tbn1		10,000	2008	Samsung Heavy Industries	790	Jul-11	Speculative
Ocean Rig	DryShips Drsh Tbn2		10,000	2008	Samsung Heavy Industries	792	Sep-11	Speculative
Odebrecht	Norbe IX	Samsung 10000	10,000	2008	Daewoo	690	Apr-11	Petrobras
Odebrecht	Norbe VIII	Samsung 10000	10,000	2008	Daewoo	690	Apr-11	Petrobras
Odfjell Drilling	Deepsea Metro I	GustoMSC P10000	10,000	2008	Hyundai Heavy Industries	668	May-11	Speculative
Odfjell Drilling	Deepsea Metro II	GustoMSC P10000	10,000	2008	Hyundai Heavy Industries	668	Nov-11	Speculative
Pacific Drilling Services	Tanker Pacific Drsh Tbn3	Samsung 12000	7,500	2008	Samsung Heavy Industries	650	May-11	Speculative
Pacific Drilling Services	Tanker Pacific Drsh Tbn4	Samsung 12000	7,500	2008	Samsung Heavy Industries	650	Jul-11	Speculative
Petroserv	Petroserv Drsh Tbn1		10,000	2008	Daewoo	755	Jun-11	Petrobras
Pride	Pride Drsh Tbn4		10,000	2008	Samsung Heavy Industries	745	Dec-11	Speculative
Schahin	Schahin Drsh Tbn1		10,000	2008	Samsung Heavy Industries	682	May-11	Petrobras
Schahin	Schahin Drsh Tbn2		10,000	2008	Samsung Heavy Industries	709	Jan-12	Petrobras
Stena	Stena DrillMAX ICE	Stena Stena/Samsung	10,000	2008	Samsung Heavy Industries	1150	Dec-11	Speculative
Transocean	Discoverer India	Transocean Offshore Enhanced Enterprise Class	10,000	2008	Daewoo	775	Oct-10	Reliance
Vantage Drilling	TMT Drsh Tbn3		12,000	2008	Daewoo	672	Dec-11	Speculative

Source: Petrodata, Mar 09

Exhibit 5: Samsung Heavy Industries Market Share and Backlog



Vessels	Portion of backlog	Global M/S	Remarks
Drill ship	34%	66%	· +10,000ft water depth
FPSO	4%	30%	· +80,000 DWT
LNG carrier	13%	32%	· +90,000 CBM
LNG FPSO	4%	100%	· First order in 2008
Large container	16%	30%	· +10,000 TEU
Total	71%		

※ M/S Source: Clarkson, SHI, orders from 2005 to end-November 2008

Source: Samsung Heavy Industries

Keppel Corp's Key Financial Data

Keppel Corp Results **Year Ended 31 Dec (S$ m)**	**1Q08 (S$m)**	**1Q09 (S$m)**	**% Chg (YoY)**	**4Q08 (S$m)**	**% Chg (QoQ)**
Offshore & Marine	1,399.7	2,118.6	56.4%	2,988.5	-26.8%
% of revenue	63.3%	71.1%		80.0%	
Property	299.7	221.9	-26.0%	227.4	-2.4%
% of revenue	13.6%	7.4%		6.1%	
Infrastructure	505.4	634.4	25.5%	490.6	29.3%
% of revenue	22.9%	21.3%		13.1%	
Investments	6.5	3.0	-53.3%	28.5	-89.3%
% of revenue	0.3%	0.1%		0.8%	
Total revenue	2,211.4	2,978.0	34.7%	3,735.0	-20.3%
Materials and subcon costs	-1599.2	-2256.8	41.1%	-2707.3	-16.6%
Staff costs	-306.6	-311.1	1.5%	-549.2	-43.4%
Gross profit	305.6	410.1	34.2%	478.5	-14.3%
Other operating costs	-11.0	-54.2	395.0%	-50.4	7.6%
Depreciation and amortisation	-32.4	-40.6	25.5%	-37.5	8.4%
Profit from operations	262.3	315.2	20.2%	390.7	-19.3%
Investment income	0.4	0.1	-73.4%	5.9	-98.4%
Finance income	18.9	13.3	-29.4%	17.6	-24.1%
Finance expense	-17.0	-12.3	-27.6%	-27.5	-55.3%
Share of associates	101.6	83.9	-17.4%	10.4	708.9%
Profit before income tax	366.1	400.3	9.3%	397.0	0.8%
Income Tax	-55.8	-73.9	32.6%	-75.1	-1.5%
Profit after tax	310.4	326.3	5.1%	334.5	-2.4%
Minority Interests	-48.6	-41.0	-15.6%	-70.4	-41.7%
PATMI	261.7	285.3	9.0%	264.1	8.0%

EARNINGS FORECAST Year Ended 31 Dec (S$ m)	FY07	FY08	FY09F	FY10F
Revenue	10,431.3	11,805.4	10,029.5	9,194.2
Gross profit	1,261.7	1,647.9	1,150.2	1,051.7
Operating and admin expenses	-85.4	-270.3	-70.2	-64.4
EBITDA	1,176.3	1,377.6	1,079.9	987.4
Operating profit	1,050.6	1,238.5	922.4	814.5
Other income	91.4	83.1	68.2	61.5
Finance expenses	-62.7	-78.7	-69.0	-64.8
Associates/JVs	476.9	354.0	451.3	413.7
Pre-tax profit	1,556.2	1,596.8	1,373.0	1,225.0
Exceptionals	564.9	12.6	0.0	0.0
Tax	-468.6	-288.0	-247.1	-208.2
Net profit	1,652.5	1,321.4	1,125.8	1,016.7
PATMI (before property reval)	1,025.6	1,096.7	957.0	864.2
PATMI (after property reval)	1,130.7	1,098.0	957.0	864.2
Earnings per share (S$cents)	64.9	69.0	60.0	54.2
Fully diluted earnings per share (S$cents)	64.4	68.7	60.0	54.2
EPS growth	35.9%	6.7%	-12.7%	-9.7%
Gross profit margin (%)	12.1%	14.0%	11.5%	11.4%
EBIT margin (%)	10.1%	10.5%	9.2%	8.9%
Net profit margin (%)	15.8%	11.2%	11.2%	11.1%
Revenue revision	NA	NA	-1.5%	-0.5%
Net profit revision	NA	NA	3.9%	8.2%
Segment revenue				
Offshore & Marine revenue	7,258.4	8,569.2	6,070.0	4,259.9
Property revenue	1,834.9	949.6	774.5	961.9
Infrastructure revenue	1,276.9	2,232.5	3,125.6	3,907.0
Investments revenue	61.1	54.1	59.5	65.5

BALANCE SHEET As at 31 Dec (S$ m)	FY07	FY08	FY09F	FY10F
Cash and equivalents	1,600.9	2,244.9	1,842.2	1,662.7
Other current assets	5,685.9	5,845.6	5,013.9	4,153.5
Fixed assets	1,698.2	1,872.6	2,115.0	2,242.2
Other long term assets	6,812.2	6,783.4	6,804.9	6,929.3
Total assets	15,797.2	16,746.4	15,776.1	14,987.7
ST & LT Debt	2,234.4	1,970.2	1,850.0	1,650.0
Other current liabilities	6,138.6	7,646.5	6,306.1	5,300.3
Other long term liabilities	389.0	381.2	329.5	281.7
Total liabilities	8,762.0	9,997.9	8,485.6	7,232.0
Shareholders equity (incl reserves)	7,035.2	6,748.5	7,290.5	7,755.7
Total equity and liabilities	15,797.2	16,746.4	15,776.1	14,987.7
NTA per share (S$ cents)	325.0	284.1	317.0	346.2
NAV per share (S$ cents)	329.2	289.0	321.9	351.1

CASH FLOW Year Ended 31 Dec (S$ m)	FY07	FY08	FY09F	FY10F
Profit/(Loss) before working cap. changes	1,189.6	1,395.7	1,079.9	987.4
Working capital changes	507.7	651.1	-795.7	-495.4
Net cash from operations	1,697.3	2,046.8	284.3	491.9
Capex	-255.9	-399.6	-400.0	-300.0
Other investing flows	-290.4	228.4	248.2	227.6
Total investing cash flow	-546.3	-171.2	-151.8	-72.4
Change in equity	64.3	233.7	0.0	0.0
Net change in debt	-722.4	-288.2	-120.2	-200.0
Dividends and other payables	-511.0	-1,201.2	-415.0	-399.0
Total financing cash flow	-1,169.1	-1,255.6	-535.1	-599.0
Net cash flow	-18.1	620.0	-402.6	-179.5
Cash at beginning of year	1,615.2	1,600.9	2,244.9	1,842.2
Cash at end of year (incl FD pledged)	1,600.9	2,244.9	1,842.2	1,662.7
Key Ratios				
PER (x)	9.3	8.7	10.0	11.1
Price/NTA (x)	1.9	2.1	1.9	1.7
Dividend yield (%)	10.6	5.6	4.3	4.2
ROA (%)	10.5	7.9	7.1	6.8
ROE (%)	23.5	19.6	15.4	13.1
Net gearing (%)	0.1	Net Cash	0.0	Net Cash
PE growth (x)	0.3	1.4	-0.8	-1.1

Source: Company data, OIR estimates

For OCBC Investment Research Pte Ltd

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