

Keppel Corporation 1Q2019 Results Briefing

Transcript of the Question & Answer Session

18 April 2019, 5.30pm, Keppel Leadership Institute

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| LCH | Loh Chin Hua, CEO of Keppel Corporation |
| CHC | Chan Hon Chew, CFO of Keppel Corporation |
| OTG | Ong Tiong Guan, CEO of Keppel Infrastructure |
| CT | Christina Tan, CEO of Keppel Capital |
| CO | Chris Ong, CEO of Keppel Offshore & Marine |
| TSY | Tan Swee Yiow, CEO of Keppel Land |
| TP | Thomas Pang, CEO of Keppel T&T |
| MSM | Manjot Singh Mann, CEO of M1 |

LCH: Before we move to the Q&A, I'd like to introduce a new member of our panel. This is Manjot Singh Mann who is the CEO of M1. Welcome, Manjot, to the Keppel Group.

Questions from Mr Gerald Wong, Credit Suisse

What is the timeline in which you expect to achieve the 15% ROE target ?

LCH: The 15% ROE target is a medium- to long-term target. I think this is something that we believe is achievable, but it will depend on the industry cycles. Some of our businesses may reach it earlier than others. It is a target we have set for the group. Of course, within the group, as shown in the slide, there are also individual ROE targets for the different businesses.

The O&M ROE target of 15% appears high compared to its 2018 ROE. Could you share your new order and margin assumptions to get to a 15% ROE?

LCH: There are no assumptions per se, in coming out with the 15% ROE. We basically looked at what KOM has achieved in the past. Of course, in the past, the ROE was in fact much higher. The industry has changed, so we think that 15% is a realistic target to be set for the long term.

What are your plans for land sales at Tianjin Eco-City with the better residential outlook in China?

CHC: As you know, the Tianjin Eco-City project is a government-to-government project, a joint venture project with the Chinese. There are plans to list a number of land plots during the year but of course, we will have to watch the market to look for a conducive window to list those projects. So indeed, yes, we are looking at booking some land sales during the year.

Questions from Ms Cheryl Lee, UBS Singapore

In arriving at your RNAV of S\$10.3bn for Keppel Land, how are you valuing your landbank?

CHC: The RNAV calculation is based on a certain point in time as of 31 December 2018. Indeed, the calculation is derived based on an as-is valuation basis for the properties. Several factors are actually taken into consideration in calculating the RNAV. A combination of estimates including internal estimates based on prevailing selling prices for completed inventories and also market comparables

for undeveloped land, as well as valuations that are provided by independent valuers. So that's the basis that we use in determining Keppel Land's RNAV.

In your RNAV of S\$1.2 billion for Tianjin Eco-City, what are the key assumptions? Do you revalue unsold sites at current market prices?

CHC: Yes, in considering the RNAV for Tianjin Eco-City, it has taken into account the carrying value of SSTECC (Sino-Singapore Tianjin Eco-City Investment and Development Co, Ltd) as at 31 December 2018, and at the same time also, the remaining land that is to be developed or to be sold by SSTECC. And for that we take into account the prevailing land sale prices and less off our land cost.

Question from Mr Foo Zhi Wei, Macquarie Singapore

Could you share the post-tax amounts for two items: Fair value gain from acquisition of M1, gain from disposal of 70% interest in Dong Nai Waterfront?

CHC: The remeasurement gain is not subject to tax but it's after NCI at \$125 million, gross is \$158 million. The gain from disposal of Dong Nai, gross of tax is \$65 million; after tax, it is \$49 million.

Questions from Mr Jason Yeo, Goldman Sachs Singapore

Why was the O&M operating margin lower in 1Q19 than 1Q18 with similar levels of revenue?

LCH: The mix of projects that are recognised, or revenues that are recognised for projects over the year are different. So of course, the margins could differ from project to project.

Do you think the market is conducive to launch most of the launch-ready units in China and Vietnam this year?

TSY: Well, when we get the units launch-ready, we will also be carefully evaluating each city and each site. We will look at the market conditions before we push out each project.

Questions from Ms Lim Siew Khee, CIMB Singapore

What is your current staff strength at O&M?

CO: The present direct headcount is 10,843.

When do you expect Sete's resolution, considering that this has dragged on for so long?

CO: I am afraid I don't have an answer on when exactly is the resolution, but it is at a stage whereby they are evaluating the bids. So we are awaiting their notification of when they are ready.

Is there any one-off in O&M's associate profit for the quarter?

CHC: The O&M's share of results from associates for the quarter is about \$10 million. I think that's a much better performance than last year, driven mainly by Floatel. I wouldn't say it's one-off, but of course, the performance would be very much dependent on Floatel's underlying performance, basically in terms of the charter of the floating accommodation units. So it's not one-off, but it can be variable depending on the performance of the associate.

What is your definition of medium term for ROE to be achieved? Is it 3 or 5 years?

LCH: We are looking at this as a target for the group. As I shared earlier, looking at the past, we believe that this is something that is realistic. It will depend on how quickly some of the industries that are going through downturns pick up. Of course, if all the industries that we are in continue to improve, then it will be shorter; if not, it may be a bit longer.

Question from Ms Tay Peck Gek, Business Times

Could you share on Keppel's performance in the Singapore residential market?

TSY: In Singapore, in the first quarter, we managed to sell about 50 units, mainly from Garden Residences. This is arising from the release of plans for the Cross Island MRT Line in January 2019, and the future Serangoon Garden MRT station which will be located just 5 minutes away. With the announcement, we see the renewed interest in our project.

Question from Mr Bobby Goh, a shareholder from Singapore

Congratulations on the 1Q results, may I ask if there are any plans to reduce the net gearing of 0.72x to the long-term average of 0.3x to 0.5x?

LCH: The net gearing, as Hon Chew has explained, has risen. We have said before that we are very concerned about keeping our balance sheet strong, and by that, we define it as not crossing the 1.0 mark. There is still some headroom, of course, but we are always watching our net gearing very closely. At this level, we are still very comfortable.

Questions from Ms Jane Tan, a retail shareholder from Singapore

Can you comment on the contracting terms and the margins outlook for the new-build market? Are you seeing some improvements?

CO: In terms of the new-build market, there are different segments. As we have informed, our strategy is to diversify into different new-build markets. We have, over the years, gotten contracts for construction vessels like dredgers so that it will not only limit us to offshore rigs. Margins and contract terms depend on different geographies, different customers. But on the whole, I would say that for drilling rigs, it remains quite challenging due to the overhang. There are opportunistic niches in the market and we will look at good contracts, strategic contracts. In terms of improvements in the market, again, there are different segments in the new-build market, and we will be quite selective. But we see that the production market will probably be a little bit more optimistic compared to offshore drilling.

Keppel has been named as one of the two bidders for Sete Brasil's rigs, why are you bidding for your own rigs?

CO: The bid reflects our confidence in the Brazil market. Moreover, the rigs come with a long-term charter, 10 years, at a charter rate of \$299,000 per day. So we see that as an opportunistic bid and also a show of our confidence.

Question from Mr Conrad Werner, Macquarie Singapore

Can you add any more colour on the strength of your property markets... the end-purchasers' market in China?

LCH: I think as I shared in my speech, things seem to be a bit more positive now in China in the first quarter, in the tier 1 and tier 2 cities, where there's high growth. As you can see from our Nanjing project, we have met with very strong demand at launch. Of course, not every project will be like this. The projects that we are in, we have confidence that they will do well. The market now seems a bit more favourable, developers are a bit more positive, and more importantly, I think the buyers are now also more positive. We think this is a good sign and we are carefully watching this.

Question from Ms Aravindan, Reuters News

Is this the first time Keppel is adding to its O&M staff since it started making cuts due to the downturn? When did Keppel last add to its workforce in O&M?

LCH: The answer is, we are expecting - so I won't say that we have started - to add. Since late 2014, we have been rightsizing Keppel Offshore & Marine. As reflected in my speech, we are starting to see that with the expected increase in workflow as well as preparing for the upturn, we would be looking to add to our workforce this year and this would be the first time we are doing it since when we started rightsizing in early 2015.

Question from Jason Yeo, Goldman Sachs Singapore

What drove the QoQ decline in O&M net profit from \$39 million in 4Q18 (excluding RIDs) to \$6 million in 1Q19?

CHC: Again, I think Chin Hua mentioned earlier the margins for Offshore & Marine on a quarter-by-quarter basis is very much dependent on the mix of the projects that the offshore & marine yards are working on. So for instance, if a lot of the proportion of that comes from say rigs like Borr Drilling rigs, the margins are lower, because these rigs were actually sold to Borr Drilling at a certain price which gives us a margin that is not very high.

Question from Mr Sankaran, a retail shareholder in Singapore

Can you please give some insights into the Group's plan on sustainable and growing positive cash flow?

LCH: We do watch the free cash flow very closely, but it will vary from quarter to quarter. I think it's also important to see the reasons why there is an outflow. For this first quarter, this is driven primarily by the fact that we are seeing better workflow and therefore a need for higher working capital at KOM. We have also seen some replenishment of our landbank. We have gone through a number of divestments in the last few years, en-bloc sales in Keppel Land. So it's not a bad thing because you do need to spend cash in order to grow our businesses. But of course, we do keep a very close watch on our cash flow.

Questions from Ms Lim Siew Khee, CIMB Singapore

Will you consider developing Plot 4 and 6 of Keppel Bay in the near term?

TSY: Yes, we are reviewing the development plan. Probably Plot 4 will launch first before Plot 6.

Can you elaborate on why the conditions were not met and caused the cancellation of Stolt Nielsen's LNG vessels contract recently?

CO: We are unable to disclose the exact conditions other than to say that they were due to commercial considerations and those were options that have lapsed.

Questions from Ms Cheryl Lee, UBS Singapore

What is the net debt carried under Keppel Land?

LCH: The net gearing for Keppel Land is quite low but we do not disclose that.

What are your plans for KrisEnergy, given the drag on earnings?

LCH: It's true, KrisEnergy has been a drag on our earnings. We have mentioned before, it is not a strategic investment for us. This is an investment, so we will watch and see how we can get the best out of the situation.

What is the status of the third FLNG conversion with Golar, the Gandria?

CO: We still have a valid contract for the conversion of Gandria. The owner is marketing the prospect with different customers. We will await updates from the customer for further development.

Questions from Ms Lim Siew Khee, CIMB Singapore

How are you going to optimise cost in M1?

MSM: We are in the process of understanding our strategic moves and transformation at this point in time and addressing every part of the business, cost being one of them. So the first exercise will be trying to understand and benchmark our cost against the best-in-class in the region to understand where the cost can be rationalised. Secondly, when we redefine and reassess our business processes in the transformation exercise, that would also give rise to some areas where we can look to optimise cost. So it all depends on our transformation strategic exercise that we are in today.

Will you need to spend upfront restructuring costs in the coming quarters?

LCH: I don't believe anything is forecast at the moment.

Question from Ms Cheryl Lee, UBS Singapore

With regards to the ROE target of 12% for Keppel Logistics, could you share how this might be achieved, as this segment's profit contribution is generally quite low?

LCH: Cheryl, you are right. I think the Logistics Division has faced a lot of headwinds but we are also in the midst of remaking our logistics business. We have been integrating our traditional third party logistics. We have bolted on last mile delivery, and also gone into omni-channel. We believe that we have quite a good value proposition now. So it's really now up to us to execute on that strategy and deliver something that perhaps would have to be a bit more asset-light than what it is today in order to achieve that 12% target. Thomas, see if you want to elaborate.

TP: Thank you for the question, Cheryl. As Chin Hua has mentioned, we are in the middle of transforming the logistics business and part of it includes a strategic review of our assets including the assets in China, and also bolting on new innovative services to better serve our customer. We are also in the middle of targeting new segments and new verticals in order to bring about more profitable returns.

Questions from Mr Foo Zhi Wei, Macquarie Singapore

On your RNAV of SSTECH, what was the price assumption that was used that has been valued in arriving at the S\$1.2b valuation?

LCH: I believe that has been answered by Hon Chew earlier.

Considering the volatility of land prices in 2017 and 2018, at RMB13,800psm and RMB9,500psm respectively, what guides your confidence in that price assumption going into your valuation?

LCH: The differences in price are not necessarily just related to market volatility. It also reflects a bit on the difference in that particular site's plot ratio and uses. So obviously we factor all of that in looking at the assumptions, as you've heard from Hon Chew. We look at market comparables in coming up with these numbers.

Questions from Mr Gerald Wong, Credit Suisse

Keppel Capital now has a ROE target of 20% on top of doubling its AUM within 5 years. How do you see this being achieved? Which assets provide the best opportunities?

CT: We are confident in terms of achieving our targets. For fund management, in terms of our historical performances, this ROE target of 20% is actually quite achievable. I think the fact that we have the various Keppel entities, our sister companies that provide very good alternative asset classes to our investor base, that helps us a lot because instead of being just a financial investor, we now have the capability of being a developer of assets, creator of assets, and we have deep operational expertise as well within the group. So for example, the Gimi project which we have talked about, the FLNG, this is actually a great asset for our infrastructure fund that we are looking to establish. It's because of Keppel's proprietary deals that we are actually able to obtain this. Otherwise, if you are any other financial investor, it's almost impossible to get hold of this asset. So we are quite happy that with the support of the group, we are able to move into alternative asset classes which provide very good returns. For the FLNG, we have a 20-year charter with an established player, an oil major, so that actually provides very good returns for our investors.

Question from Yeo Zhi Bin, Tokio Marine Life Insurance

Does the recent master plan give you added impetus to redevelop Keppel Towers or is the residential cycle still not that conducive, hence this could be more of a mid-term opportunity instead?

TSY: You are right to observe that Keppel Towers is within the recently announced CBD incentive plan within the draft master plan. We are reviewing the different combinations because the incentive does give you options of developing more residential, hotel or combinations of different usage. So we are looking at different options and once we have concluded our study, we will make a recommendation to move forward.

Question from Mr Bobby Goh, a retail shareholder

What is your outlook in the oil & gas business going forward? Any plans to get involved in the US Permian Basin for shale oil exploration?

CO: We are cautiously optimistic about the market. There is an increase of activities in tendering and bidding, as can be seen from FIDs of a lot of projects in the different segments of oil & gas. Our strategy in this area will be to stay close to the customers, provide the relevant solutions and work with them.

Any plans to get involved in shale oil exploration? The answer is not at the moment. We are not involved in this part of the sector.

Questions from Ms Lim Siew Khee, CIMB Singapore

Other than the one-off of S\$7 million in infrastructure, the division appeared to be weaker this quarter, is this due to consolidation of higher proportion of logistics losses? Or is there downward trend in the business?

LCH: As you've heard from my speech and also from Hon Chew's elaboration, Keppel Infrastructure is still doing well, just bar this share of one-off cost related to the acquisition of Ixom. Our Logistics Division, as we reposition it, we are also taking on additional headcounts as we look to grow the new wings. So that has contributed to the losses we have in logistics.

CHC: Sorry, there is one other portion of the question: Is it due to the consolidation of higher proportion of logistics losses? The answer is no, because the scheme only took place after the quarter ended.

Keppel Capital's strength this quarter, is it exceptional or normalised?

LCH: I think there are some one-offs.

CT: That's right. For this quarter, we have the acquisition of Ixom, so the fees are actually recognised here, as well as our divestment of a stake in OFC. I think for the fund management business, it's always in the business of acquiring and selling assets. So we hope to make this a more normal trend.

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