

Keppel Corporation 4Q and FY 2017 Results Briefing for Analysts and Media

Question & Answer Session

25 January 2018, 5.30pm, Keppel Leadership Institute

LCH	Loh Chin Hua, CEO of Keppel Corporation
CHC	Chan Hon Chew, CFO of Keppel Corporation
OTG	Ong Tiong Guan, CEO of Keppel Infrastructure
CO	Chris Ong, CEO of Keppel Offshore & Marine
CT	Christina Tan, CEO of Keppel Capital
TP	Thomas Pang, CEO of Keppel Telecommunications & Transportation

Opening remarks by LCH: Warm welcome to this result review at KLI. We have a very large turnout today, including a number of our friends from the local and foreign media. Some of you may have specific questions concerning the global resolution. I just want to say that when we announced the global resolution at the end of last year, we had also provided a comprehensive factsheet. The company in its agreement with the different authorities on the global resolution, is under quite specific restrictions in terms of any public statements that we make. We cannot say much more than what is already in the public announcement and factsheet, nor can we comment on the Statement of Facts released by the authorities or to comment on identities of individual officers.

This is a result briefing, and we are here to try and answer questions on the results. To the extent that the questions relating to the global resolution have an impact on our financial results, we will be more than happy to address them.

Cheryl Lee from UBS: I have four questions. The first one is with regards to the global resolution. The number in the accounts on page 24 of the SGX release is \$619 million, which is different from the original amount of \$570 million. Could you help us understand what the differences are?

My second question is about Offshore & Marine (O&M). In the fourth quarter, the operating loss was \$215 million although the quarter-on-quarter (qoq) revenue was comparable. And so even if I take into account the one-off charges, it was still a loss. Could you help us understand what the cause of the \$80 million loss was in the fourth quarter?

My third question is to clarify whether the Group gearing of 46% already reflects the financial penalty that you will have to pay?

The fourth question is about your property portfolio and refers to slide 14. In the comparable slide in the previous quarter, you said that the annual income on a stabilised basis would be \$75 million and in this quarter it says net operating income on a stabilised basis of \$300 million. Could you help us define the different metrics used, and what accounts for the increase in number?

LCH: Thanks Cheryl. I will ask CFO Hon Chew to answer the first three questions.

CHC: On the \$619 million, that comprises two components, the fine of \$570 million that you have just mentioned, and the remaining \$49 million which is in respect of accounting, forensic and legal costs related to the global resolution.

As for O&M, I think your question is comparing our fourth quarter to third quarter. The difference was in the fourth quarter where there were lower contributions from associated companies. A couple of associated companies also made some provisions, so the share of profit was also lower.

As for the gearing, do take note that we have yet to pay the fine as of December. The fine will be paid in the first half of 2018. 87.5% of the fine will be paid in 2018, and the remaining 12.5% will be paid three years later in 2020. Assuming all the fines have been paid as of December 2017, the gearing would have been 51%, so the impact is another 5 percentage points.

LCH: On the fourth quarter, Cheryl if you don't mind, I will ask my IR team to get in touch with you and run through the differences between the assumptions for the two slides.

Mayuko Tani from Nikkei: Firstly, when is the payment for the US\$422 million charge going to be? Is this going to be the last time we see a payment, or is there a possibility, depending on the investigation with individuals, that you may have to make more payments?

On the O&M business, you have an \$81 million provision for loss from Sete, and \$54 million in impairments for other assets. Can you please give more details on that? For Sete, you had made provisions some years back. Are we going to see more provisions in the future? Can you also tell us the market outlook, whether you see something coming in this year as revenue?

LCH: On the US\$422 million (\$570 million) financial penalty, about 25% of that has already been paid in January. We expect to pay another 12.5% sometime in March, and 50% in May. The balance will be paid probably at the end of the third year. This is a global settlement with the three criminal authorities, so this should be the final as far as these penalties are concerned.

On Sete, we made a provision in 2015, and we have said in numerous results briefings since then that we will check on the adequacy of the provision every quarter. This quarter, we did an update on the scenarios and there was a necessity for us to take a further provision of \$81 million. We believe that this provision is enough, but of course, we will have to continuously study the situation.

CO: On the outlook for the offshore and marine business, we are having a diversification drive as we have updated at the previous results briefings. Of this year's deliveries, 50% are of non-drilling products. That (diversification) itself is bearing fruit, and we will continue to work on our gas strategy and LNG products. We are hopeful that 2018 will be a more fruitful year than 2017, if all of our targets are met.

CHC: You also had a question on the provisions over \$135 million – CEO has already explained that the \$81 million is in respect of the Sete rigs. The remaining \$54 million includes a number of items. The large items are actually pertaining to provisions at the associate level for impairment. That is one of the biggest items. Also, impairments in respect of investments in associates. And lastly, losses arising from the closure of one of the yards.

Joshua Lee from Deutsche Bank: Would management consider a periodic revaluation of Keppel Land's Tianjin JV land? Secondly, what are the examples of enhanced compliance controls? Thirdly, what sort of strategies will UrbanFox undertake to gain market share in Singapore?

LCH: If land is held for sale, it is part of our inventory, and we will always keep it at book cost. We will not revalue that, and that will not change. You can get a sense of what the valuation of land in Tianjin Eco-city is over a period of time from the land sales as SSTECH continues to develop Tianjin Eco-city. On the second question, CFO can give some examples.

CHC: I will give some specific examples, which includes an enhanced Code of Conduct containing detailed anti-corruption provisions and guidance on dealing with intermediaries. This also includes the establishment of a Group-wide compliance and governance framework. We have also established an independent Group-wide compliance function with clear reporting lines to the Board Risk Committee and also expanded the team of experienced compliance personnel. We have introduced an extensive risk-based due diligence for third parties who represent Keppel in business dealings. We have a rigorous and regular training programme to enhance the compliance culture across the Group, including a very comprehensive annual compliance-related e-learning and attestations exercise.

Other examples include a new Supplier Code of Conduct, with very specific anti-bribery provisions. We have also updated our Group whistleblower policy with centralised procedures and also set up a new whistleblower committee. Last but not least, a Group policy on agent fees to strengthen procedures and requirements on the hiring of agents was put in place.

TP: UrbanFox provides end-to-end e-commerce solutions. The services range from omnichannel management for e-commerce to warehousing and inventory control and last-mile fulfilment services. So it is differentiated from a lot of the logistics companies out there. In working closely with its parent company Keppel Logistics, UrbanFox has access to potential customers, who are existing clients with whom we have strong relationships.

Angela Teng from Mediastream: Regarding the recent bribery scandal at Keppel O&M, are there any customers who have stopped dealing with the company? Is the company still receiving orders from existing customers? What are the strategies employed to maintain the working relationship with customers in this post-bribery situation?

LCH: We have been engaging with customers. Some of them have asked certain questions to get a better understanding of our enhanced compliance framework. By and large, we have not seen any of our customers stop working with us. Of course, the company will have to continue to work very hard to demonstrate that we have a very strict compliance regime, and that we will only engage in ethical and legal activities. This is something that we will have to work very hard on but that has not stopped customers from working with us.

Saurabh Chaturvedi from Wall Street Journal: Two questions. Is it the first ever quarterly loss for Keppel? Second, how important are the Brazilian operations in terms of contributions to overall revenue or overseas revenue? What percentage comes from the Brazilian operations?

CHC: It is the first quarterly loss for the Group.

Saurabh Chaturvedi from Wall Street Journal: Before 2003 it was annual results I would believe. You have had losses in the past right? Like in 1980 when you got listed.

LCH: The key here is that this \$619 million that we had to take for the fourth quarter is a very significant amount and is a one-off which led to this loss. I think we should focus on now and going forward. As explained by our colleague, this would have been the first loss since 2003 when quarterly reporting was put in place. But as I said, the key is that this is one-off, and it is a significant amount of \$619 million.

Saurabh Chaturvedi from Wall Street Journal: What is the contribution of the Brazilian operations to the overseas revenue and the overall Group revenue? In terms of the offshore business.

CO: Operations in Brazil remain an important part of our *Near Market, Near Customer* strategy. Right now besides the Sete projects, our team is still working hard to deliver projects like P-69. We delivered P-66 last year, ahead of schedule. What we are trying to do is to enhance our offerings by providing on-time, on-budget solutions to customers. Brazil is a very important part and still remains relevant to our global presence in terms of operations.

LCH: This is also perhaps an important point to make that global resolution allows the company to draw a line under the chapter and we can continue to work in all these markets, including Brazil and the US. And as Chris said, Brazil remains a very important offshore market and we intend to be engaged in the Brazilian market.

CHC: Brazil's revenue is about 7% of the Group's revenue, assets is about 2%.

Gerald Wong from Credit Suisse: To follow up on the additional \$80 million of provisions. What has really changed over the last 12 months which led you to take this additional provision, especially since there were no provisions taken back in 2016?

Secondly, the revaluation gain from overseas properties of \$180 million, which market did you change your cap rate assumption for and what was the key change made?

Thirdly, when you acquired Keppel Land, you mentioned that the through-cycle ROE for the property division can be 12%. Given the ROE of 8% in 2017, and the 9% over the last five years, do you think that the 12% through-cycle ROE is still achievable?

LCH: As I answered earlier to the question from Nikkei, the Sete situation is fluid. Every quarter, we will go through the scenarios to make sure that the provision made is adequate. In the fourth quarter of last year, through our discussion with Alvarez, who is working with Sete Brasil on their restructuring, we came to a certain conclusion on what the scenario might likely be, and that has resulted in a shift in the way that we look at the outcomes. This has resulted in the additional provision. Of course, we will look at the assumptions that are used as well, in terms of day rates, exchange rates..., etc. All these are factored in and we will review this every quarter.

On property, you mentioned the \$180 million mostly from the revaluation of overseas properties. The bulk of it would be pertaining to developments that have reached a certain stage, and we will then factor in revaluation above the original cost. Some of this land was purchased some time ago. As the land value has gone up, this will be reflected in the increase in value of the investment. To be clear, this is for investment properties, not land that is part of our landbank to be developed for sale.

Third question on 12% ROE. You are right, and it is good that you remind all of us. That is still something we are targeting. We believe through the cycle, it is possible. Keppel Land's net gearing in 2017 is actually not very high, at only about 25%. So we will be looking to see how we can turn our assets a bit faster. And if appropriate, we might also look at the gearing at Keppel Land. We believe that with a bit of tweaks, we should be able to hit that 12% through-cycle ROE. That will be the target.

Lim Siew Khee from CIMB: On O&M, there were some impairment and provisions at the associate level but at the EBIT level, excluding the associates, there was also a loss this quarter. Was that mainly because of cost incurred to close certain yards, plus the provision for doubtful debts and WIP?

CHC: Yes, and also because the topline has also come down by another 39% this year.

Lim Siew Khee from CIMB: So how much was the cost incurred for the yard closure? And was the \$26 million provision for doubtful debt related to Sete?

CHC: The yard closure is part of the \$54 million, roughly above \$10 million. The provision for doubtful debt was not related to Sete.

Lim Siew Khee from CIMB: What was it related to?

CHC: It was related to the O&M division, and a number of customers. But it is not appropriate for us to mention which customers.

Lim Siew Khee from CIMB: Was it related to all the undelivered rigs?

CHC: No, it was not related to the undelivered rigs.

Lim Siew Khee from CIMB: Can you comment on the potential plans to sell the undelivered rigs to Borr Drilling?

CO: On the Borr engagement, we have made an SGX announcement. We are in discussion with Borr, but there are no terms and conditions firmed yet. Discussions will continue and when there is a material contract in view we will make the appropriate announcement.

Lim Siew Khee from CIMB: Chin Hua, you mentioned you have not seen any customers that have stopped working with you. But do you think with this event it might actually put you at a slightly disadvantageous position when you tender for jobs?

LCH: I do not believe so. As I said in my opening remarks, Keppel O&M has a lot of strengths in terms of our solutions, our on time and safe delivery. We can rely on these strengths to win contracts legally and ethically. I believe that many of our customers appreciate us for these strengths. As Chris mentioned, we are still very engaged in Brazil. We are working with SBM, Petrobras and different parties in Brazil. Of course it is really up to us to continue to stay as a disciplined company, and make sure that we do things right and do the right things. If we can do that and continue to focus on our strengths in execution and solutions, I think we will be fine.

Lim Siew Khee from CIMB: Chris, you mentioned that this year would be fruitful. I actually wanted to understand the potential for drilling rig newbuilds and whether you have had any enquiries. I know the oversupply situation is well documented but just from the ground, how do people look at it?

LCH: We do not give a forecast. Maybe Chris can give a very broad outlook for the market.

CO: As mentioned in CEO's speech, there is an uptick in sentiment from the market, purely from the economics and the oil price. As mentioned, we think that rates and utilisation will have to recover before we see a meaningful uptick in new orders for drilling rigs. And that's the reason why through the quarterly results announcements we have

always mentioned we are looking at diversification, LNG strategy, and engaging our customers to ensure we have products in different verticals to serve all of them.

Lim Siew Khee from CIMB: If I could have two more questions, please: Investments Division, there is a loss in share of associates in 4Q. Why was that? Was that just purely KrisEnergy? Secondly, 4Q saw no land sales in Tianjin but did you see any sales in January?

LCH: The land sale programme in Tianjin Eco-City on a quarter by quarter basis is very lumpy, we do not sell every quarter. But in the years ahead, we expect that it will provide a steady contribution to the Group. To answer your question, we would expect to see some, in fact it would be part of the business plan, land sales in the first and second halves of this year.

CHC: On the 4Q loss on the share of associates in Investments, KrisEnergy is one of the main contributors.

Tan Hwee Hwee from The Straits Times: Your published SGX statement reflects \$26.5 million provision for doubtful debts. Can you provide more colour on the nature of these doubtful debts? Also where does Keppel O&M stand today in respect to impairments for the undelivered jackup rigs?

LCH: I think the first part of your question was addressed by CFO five minutes ago. On the second part of your question – so far, we have not made any impairments on the undelivered rigs. The jackup rigs go through the same process every quarter as that for Sete. We will evaluate to see whether there's a need to make provisions. As it stands today, we do not believe that there is a need for us to make provisions.

Foo Zhi Wei from UOB Kay Hian: For property, you've seen quite a bit of developments in China. First part is where China's actually talking about a policy shift towards a more rental model. There's also a lot of activity in the first few weeks of this year, where Chinese land developers saw a lot of sales. I'm curious about what strategy has Keppel adopted to adapt in this shift in the landscape, as well as capitalise on the higher property sales in the first few weeks of this month?

LCH: Property-wise, China is one of our key markets, we certainly are very actively involved. As you have seen in 2017, we have sold over 3,000 units in China, and we will continue to look for opportunities to turn our landbank there faster. We have also taken opportunities in 2017 to sell some of our projects en bloc, when the opportunity there is better than for us to hold. You've also seen us replenish land; in late December when we bidded successfully for a site in Wuxi. During the year, Keppel Land has also entered into the Shanghai office market to acquire an office building. This is also part of our more multi-dimensional approach to property, so we don't just buy land to develop. Sometimes when it makes sense, we can sell the project en bloc, and at other times, we can also buy an existing investment and add value through asset management, as we have done very successfully with the Jinqiao shopping mall a couple of years ago.

The market in China will go through quite a lot of ups and downs, there will be a lot of policy risk that we have to be watchful of. But at the end, I think it's a market that we are quite well entrenched in. We've been in China for more than 20 years, we've developed capabilities and a network in those areas, and the ability to execute well, and most importantly we've also built up quite a significant landbank. That gives us an advantage – we can be more selective when we purchase land. More recently, we've also started to look not just at buying land, but at buying finished assets where it makes sense.

Foo Zhi Wei from UOB Kay Hian: In the previous quarters you talked about how you want to make Infrastructure a key earnings driver. We've seen growth this year, but just what else should we expect going forward. I suppose data centres are one of them with the Alpha Data Centre Fund something to watch for, but it's been a bit quiet on this front, could we get an update?

LCH: For Infrastructure, I think they have had a very busy 2017. Not only has Keppel Infrastructure delivered in terms of higher net profits, significantly higher than the year before, they have also been very active in securing projects namely the Keppel Marina East Desalination Plant, as well as the Hong Kong Integrated Waste Management Facility. We expect these projects to contribute to Keppel Infrastructure over time. We also announced the gasification project in the early part of last year. That's a bit longer-term, it will take us a bit more time to get to FID. But again, this project would also be a significant contributor to the Group. Thomas, would you like to talk about data centres?

TP: The data centre market continues to be growing at a very fast pace due to the demand from cloud service providers. And we are not just seeing the interest from American cloud service providers, but also increasingly from the Chinese giants as well. Keppel Data Centres, with the support from the Alpha Data Centre Fund, will be able to capture the opportunities that are coming into the Tier-1 cities around Europe and Asia. The team is targeting new developments as well as brownfield developments in all these Tier-1 cities.

Aradhana Aravindan from Reuters: As a company which has gone through this now, is it time for Singapore to strengthen these anti-corruption laws which have been around for a long time?

LCH: Your question is very broad. All I can say for Keppel is, we have a strong core value of integrity. What integrity means is that we have to do business legally and ethically. So for Keppel, as I said earlier, it is very clear to us that we have the capabilities and the solutions which will allow us to win business legitimately, within the laws and rules, and also ethically. That is something that we will pursue.

Joshua Lee from Deutsche Bank: Two questions: why is Keppel in talks with Borr Drilling to sell the 6 jackups? Second, with reference to slide 48, these 6 jackups in question are all slated to be delivered in 2018?

CO: As to why Keppel is in talks with Borr, this is the secondary jackup sale market, and Borr has their own strategy to build up their fleet with premium jackups. Not to forget, they are also a customer in the yard and we have a daily working relationship with Borr. We have five contracts from Transocean to them.

The terms and conditions are not firm – so we are not confirming that there are six. We are just in talks on opportunities that we want to take a look at. We have not landed on which are the jackups. In fact, all the jackups in the yard still have valid contracts with the current customers.

Derrick Heng from Maybank: Now that the global resolution is settled, will the construction of the balance order book from Sete commence again soon?

LCH: The global resolution means that we can draw a line underneath this. We are able to operate in Brazil with this resolution. But whether this signals or leads to the re-commencement of construction on the Sete rigs, that will depend on other matters such as the restructuring of Sete. This will also of course depend on their negotiations with Petrobras.

Kristie Neo from CNBC: There are some reports on a potential merger between Keppel O&M and Sembcorp Marine. Are you able to comment on that, and where is your threshold at least where Keppel O&M is concerned?

LCH: This question comes up every once in a while. The way I have addressed it and look at it is – if you look at Keppel O&M, we have undertaken quite a significant right-sizing exercise starting from 2015. At the peak we had about 36,000 direct employees. Today we're down to about 14,000. So it's quite a significant reduction. And our footprint has also been made more efficient. We believe that this is the right size for us, and we do not see at this point in time any upside in terms of having capacity. But that's of course our evaluation at this present time. In other words, if there's no value in adding capacity, any merger – not necessarily with Sembcorp, so I'm not commenting directly – or acquisition for that matter, may not make sense for us at this point in time.

Conrad Werner from Macquarie: Just a quick question on the property volumes which were down in 2017 over 2016, and the ongoing reason for that was measures, especially in China and Vietnam. Could you give us a bit more colour on the outlook for 2018, both in terms of volume and the overall health of the Chinese and Vietnamese property markets from your perspective? Maybe specifically in the areas where your projects are also located. And if there is any risk that if these measures continue, that some of the completion dates for these projects, which also trigger profit recognition, get pushed out?

LCH: I'll answer your second question first. The measures may not have a direct impact on the completion date, particularly if a project is already sold or substantially sold. We would be very motivated to get it completed on time. There wouldn't be any recognition of cooling measures to affect that pace of construction. As far as the market is concerned, I think that Vietnam still remains very constructive, we see very good demand, not just for our projects but also for other developers. The fact that our sales rate in Vietnam for 2017 is slightly lower compared to 2016, is more to do with the timing of the launches that we have, rather than a reflection of the market demand there.

As far as China is concerned, we are in China for the long-term. We have quite significant projects in a number of cities like Tianjin, Shanghai, Wuxi, Beijing etc., and we will continue to develop these. If you look at the market, the cooling measures are still in place, but the demand side is still constructive. Some developers are holding back on their sales because they may not be able to achieve the targeted sales price that they have in mind. This is not because the market cannot support it but because they may not be able to get the presales permit from the authorities. So they would have held back, to try and get a better pricing. So when you see the sales in China being a bit lower, I'm talking about it as a market; it is not because the demand is weak, it is just that on the supply side, some of the developers are holding back on their launches.

Katie Foley from CNBC: You mentioned at the beginning of your speech, "This is not Keppel". Could you elaborate on your message to your shareholders about this Q4 net loss, about this fine?

LCH: I think it's very clear. As I said earlier, Keppel has a set of core values and integrity is very much centre in those core values, and those values do not allow us to act unethically or illegally. We do want to encourage all our Keppelites, as we call ourselves, to take legitimate business risks for which we get a suitable return for taking those risks. But there are some bright lines that we should not cross, and it is very clear to the team here and to the Board, that we cannot engage in anything that is unethical or illegal. That's why I said, this is not Keppel.

Mayuko Tani from Nikkei: May I find out if any of the current Board members are under investigation? This is just to find out if there is any uncertainty in terms of the management.

LCH: The management team, the investigation that we embarked on was very thorough, when these allegations came up in 2015. And this is led by external counsels, and you can also I suppose see from the fact that the other costs associated with this, about S\$48 million, that there was a lot of legal fees as well as forensics that were employed. So it was a very thorough investigation, we have reached resolutions with the three criminal authorities and we are only able to do that if it has been thorough. And I think this is really about drawing a line and looking forward. So those affected persons, as you can read from the Statement of Facts, have already been separated from the Group.

Kevin Kwang from Channel NewsAsia: To follow up on that question and your reply, you mentioned that you were very thorough in the way you investigated the incident. There were reports that the inquiry started in 2015, but management's stance changed in October 2016. When exactly did you pour resources into the forensic reporting and investigations?

LCH: I think we are getting a bit too far into this. As I said, the Group has taken its responsibility very seriously. We had made the announcement in October 2016, when we found a suspicious transaction. So we have done our part as a responsible organisation.

If there are no further questions, thank you all for coming.

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