Transcript of 1H 2014 Results Webcast
Question & Answer Session
24 July 2014, 5:30PM

Speakers:

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CHC	Chan Hon Chew, CFO of Keppel Corporation
CYY	Chow Yew Yuen, CEO of Keppel Offshore & Marine

Kevin Chong, Deutsche: The ultra-deepwater space has been weak—everyone knows that—but now people are talking about the jackup market being weak in the second half of this year and perhaps in the next 12 months as well. What is your view on this?

CYY: Industry fundamentals are still quite strong and the jackup market is still resilient. For the standard KFELS B Class jackup, which means rigs that can be used anywhere in the world outside of the North Sea, we are still getting quite active enquiries.

We have the technology to provide specialised jackups or solutions for North Sea or deeper waters as well. So we are still quite bullish about the jackup market.

Kevin Chong, Deutsche: What is the potential of the PEMEX jackups being secured this year in the new Mexican yard?

CYY: PEMEX is progressing well. We are at the stage where we are finalising our shareholders' agreement. We will give you more updates when we come to a conclusion.

I think it's also public knowledge now that Mexico has approved the secondary law governing the reform. There is going to be some local content requirement amounting to about 25%, so having a facility there will help our prospects.

LCH: I would like to add that when we announced the completion of FEED (Front-End Engineering and Design) study for the Golar FLNG, we also received enquiries from the market on when we are going to sign the contract. We eventually got it signed. This is the Keppel way. We want to make sure that when we sign on the dotted line and we get the deal agreed upon, it is with very thoughtful deliberations and making sure that the risks are all appropriately accounted for. We want to make sure that we get paid for taking any risk that we have to take.

Kevin Chong, Deutsche: Which business does the $21 million write-back of impairment relate to?

CHC: That write-back arose from the sale of an investment by k1 Ventures. k1 Ventures owns 80% of a company called Long Haul Holding Corp in the US which holds a company known as Helm Holding Corporation. That was sold during the year and some provisions made were written off after the sale was done.

Kevin Chong, Deutsche: On the Infrastructure EPC projects, what are the prospects for potentially more provisions now that we are closer to delivery?

CHC: We have not made any additional provisions in 1H14, but we can only be certain when we complete the projects.

LCH: We are in the last mile for our EPC projects, but it is a challenging last mile, and the team at Keppel Infrastructure is working very hard to make sure that we get the projects completed.

Peter Gylfe, Balyasny Asset Management, United States: What is your confidence in being on-budget for the Golar FLNG conversion?

CYY: We have a high degree of confidence on the budget. As you know, we have been working on this project for quite a few years, and actually, a full complete FEED study has been done. So as far as the engineering scope is concerned, we have quite a high level of confidence.

Also, in the scope of the FLNG project, the responsibilities are well defined. Equipment supplier, Black & Veatch, supplies the topsides, the liquefaction facility and they are responsible to Golar. On top of that, our contract is based on certain quantities, so if there is any quantity change, there is a formula for adjustment.

Peter Gylfe, Balyasny Asset Management, United States: What is your view on the FLNG industry? You have secured the first conversion project and two more options with Golar. Apart from these, in future, do you see FLNG developing like the FSRU (Floating Storage and Regasification Unit) market where, potentially, in five years, there will be ten of these on the water?

CYY: We are quite bullish about the FLNG industry. In fact, FLNG is going to be one of our core businesses going forward. We've already done three FSRUs and we will be in the position to do more FSRUs. We are hopeful that our FLNG business will become one of our core businesses, just like our FPSO business. Our facilities are well-suited for this, as with our experience in FPSO conversion business.

LCH: If I can add—gas is becoming a very important part of the energy mix. The expectation is that from now until 2020, about US$ 65 billion will be invested in FLNG. The bulk of that is going to be in the Asia Pacific market. So I think this is an exciting market, but as this is our first conversion project, we'll take it one step at a time. Certainly, we believe that this is a market that holds a lot of promise.

Ajay Mirchandani, JP Morgan: Are there any internal budgetary targets that management has kept for the gas business over the next three to five years?

LCH: Whilst we believe it holds a lot of promise, we are also looking at other new markets. At Keppel, we are not just resting on our laurels. So we are constantly looking for not just existing markets but new markets. There are, of course, targets—but Ajay, as you know, we will not disclose those targets.

Ajay Mirchandani, JP Morgan: How big is the revenue contribution from Brazil today, as a percentage of the overall Offshore & Marine (O&M) business?

LCH: As mentioned in my speech, it is currently about 20% of O&M's top line.

Ajay Mirchandani, JP Morgan: Could you give us a quick sense on jackup's pricing and payment terms as well?

CYY: As you know, competition from China has and will always put pressure on pricing and payment terms. But we have been adopting a policy where we will, first of all, use our IP and differentiate ourselves, and offer different solutions and create value for the customer.

Secondly, we are working very hard on our own productivity. As you know, we have been embarking on productivity improvements for many years now. We are still keeping up with that. We have set new targets about how much productivity we can improve year-on-year.

The third point is, we are also looking at how we can make use of our satellite yards. We have satellite yards in China, the Philippines and Indonesia. In fact, in some of these locations, our cost structure could be even lower than in China. So those are areas where we are trying to differentiate. We will continue to work on our IP. We are offering life-cycle cost benefits to the customer because of our quality, reliability and safety. There will always be pressure on margins and payment terms and so on, but this is something we are working very hard on, to try and differentiate ourselves from the rest. We may not necessary be the lowest-priced but we certainly will give the best value.

LCH: Absolutely. As I've also said in my opening remarks, we continue to be very selective. Whilst the top line is important, we must have a reasonable chance of converting that top line into a bottom line with reasonable margins. That's what all investors or shareholders expect of us.

Abhijit Attavar, Jefferies: It's Abhijit from Jefferies. I wanted to ask a question on your receivables. They seem to have jumped quite a bit. Your working capital has deteriorated in this half. Can you just tell us if it's from any particular customer? In particular, can you clarify if the payments from Sete Brasil, the milestone payments you are receiving, are coming on time?

CHC: Just to clarify your question—you're asking for the reason for the increase in receivables?

CHC: To your first question, the total receivables have gone up if you look at the balance as of end of June. That's because there were some receivables that were booked at the end of the quarter, some lumpy ones. But I'm not able to disclose who those customers are. Those receivables we actually receive in the subsequent months.

As our businesses grow, our working capital requirements would also grow. As you know—and YY has also mentioned earlier on— with competition, there is, of course, pressure on payment terms and so on.

In the past few years, on the offshore side, some of the projects, and increasingly, we have more on 20-80 payment terms as opposed to progressive payment, which used to be cash flow neutral. But now, going forward, for more of our projects, we have to fund the customer, basically. So that increases our working capital requirements.

Abhijit, Jefferies: Specifically on the Sete Brasil milestone payments. On the first semi you already hit about 70% completion, are you receiving the milestone payments on time?

CHC: For that particular one, we have received progressive payments. It's not on 20-80 payment terms.

LCH: There is a lot of pressure on the payment terms. We are holding our lines as best we can. The recent FLNG with Golar—that one is cash flow neutral to us.

Abhijit, Jefferies: I'll also just quickly put a question on the jackup side. You've said that there are healthy enquiries. But are your customers looking at the jackup deliveries scheduled for 2015, looking at 60 jackups being delivered to the market, most of them are uncontracted? Are they any holding back on signing because they expect some of these to come to the secondary market?

LCH: I think the question, YY, is on unchartered jackups being built in China.

CYY: I thought you asked a question about whether it is because of the number of rigs that are coming on in 2015, 2016—is that the reason why we are not getting more jackups?

Abhijit, Jefferies: Is that the reason why customers are holding back on signing newbuild contracts, because they expect these jackups to hit the market?

CYY: Yes and no. As you know, there are lots of jackups built in China. But a lot of them are built by speculators. We know that there are some delays in those jackups coming out from the Chinese market. On top of that, maybe for the Tier 1 and Tier 2 drilling contractors, they also have some concerns about the life cycle, the reliability of those units, and so on.

But as long as somebody spends the money to build something, that jackup will somehow be utilised. In our industry, we always say that there are jackups that are built for trading and there are jackups that are built for drilling. There are a lot of jackups built in China that are probably built for trading.

Now, the second issue is about our own deliveries. Right now, we are in quite a good position because for 2015, we are quite full; for 2016, we are near capacity.

If a customer desires to have one of our units, we could bend over backwards to see whether we can deliver it in 2016. But if an enquiry comes along, I think we probably would say that it would probably be at least in the fourth quarter of 2016 but likely to be in 2017.

Adrian Loh, Daiwa: Thanks very much for your presentation. Just wanted to ask a couple of questions. My first one is on investments and CAPEX. We are in $18 million for the first half. Just wondering if you can break that down for us - you mentioned O&M and property being in there. I also want to get an update on your China yard JV with Titan PetroChem.

CHC: The CAPEX number as you mentioned, it's largely coming from O&M and on the property side. We don't really give a breakdown of that number.

LCH: You know the agreement we signed with Titan is a conditional one. So they are currently going through their process. It's conditional upon them being able to restructure the company and get re-listed on the Hong Kong Stock Exchange. That process, as far as we know, is ongoing. It's on track. But that part of the process is being done by Titan.

Ling Xin Jin, Morgan Stanley: I have three questions. First, how long is the study with Seafox Group on the Plug & Abandonment jackup expected to take, and how is the contract outlook? Second question, what are the opportunities for the FLNG vessels with other customers in addition to Golar? The third question, on infrastructure, could you provide details on the $20 million write-back?

CYY: On the P&A Jackup, we have been working with Seafox now for quite some time. The study is ongoing and I can't exactly give you the timeline as to when the study will be completed, but I would think we are at a fairly advanced stage of that study.

The P&A jackup market is a very specialised one. We work very closely with Seafox and when they decide that they are ready to go forward, I think that's when the project will be consummated.

With Golar, we have an agreement where they have option for two more. Other customers have come to us, and every customer has their own requirements and own solutions. So there are some enquiries right now. But we have not yet gone into the detail as to the configuration for another customer just yet. So let's see how we do on the first one.

CHC: I'll take the third question which is on Infra – could you provide details on the $20 million write-back. I believe this number must have been picked up from the SGX announcement on page 2 of 27. But there's some contradiction in that question. The $20.9 million is actually a write-back of impairment of associated companies. That has nothing to do with Infrastructure. That was what I explained earlier. This is actually a write-back, a provision arising from sale of investments by k1 Ventures. Provision was made some years back on investments in Long Haul Holding Company in the US, and because we sold the investment at above the netbook value, we could actually write-back that provision.

Well just in case the question is referring to the other write-back under Infrastructure; that write-back was actually in 2013, not in 2014. That arose from the sale of the power barge business in the first quarter of 2013 in Ecuador, and because some provisions were made before, we were able to write-back those provisions upon the sale of the power barge business. So I hope I have covered all grounds, just in case.

Clement Chen, Barclays: I just have two questions, firstly can you give us an update on the drillship you are currently building, how's the progress? And in light of the earlier comments that were made that we're seeing weakness in the ultra deepwater markets, are you still as optimistic on the prospect of eventually selling off the unit or even getting further orders for that particular rig class? For my second question - we are seeing some of your competitors actually facing delays in equipment deliveries, so not so much on their end but more from their equipment providers. Are you seeing any pressures as well from your suppliers or equipment providers?

CYY: On our *Can-Do!* drillship – we're not really competing with the Koreans, in what I call "commodity exploration drillship". We have shared on several occasions that we are designing and building a vessel that is for the niche market of development and completion. And yes, in the market today, we believe there's a temporary softening.

We know that day rate for the exploration drillships has come down sometimes 10%, and sometimes even 15%. But I think we are quite confident because we feel that this vessel is differentiated when it comes to development drilling, that's where the customer will take into consideration the added features that we've put in into our vessel.

In the deepwater play, if you look at the number of rigs that have been ordered, there's quite a bit of deliveries this year and next year. But the year after that, the number of deliveries will actually start to dwindle down and we will start to talk about how there are no real orders for deepwater drillships going forward, or delivery beyond 2017/2018 other than the one Transocean ordered from Sembcorp. So I think it's a question of how the market absorbs this. We have stated that our intended delivery of our *Can-Do!* drillship is going to be sometime in 4Q 2016. So I think we will monitor the market but we feel that it's differentiated enough and there will be demand for it.

LCH: To add on to that, we remain confident that we will do well. We have done our homework. I think this is a unit we believe our customer would want, and we believe that it will do well.

CYY: I think it is a well-known fact that our Korean competitors are facing some difficulty. In fact, all three major Korean yards are experiencing delays, some of them, due to equipment, mainly the subsea packages. But they may also be delays due to variation orders and so on. We currently have eight packages that are in the deepwater segment – 6 of them are for the Sete semi, one for our *Can-Do!* drillship and another of our DSS™38M for SOCAR in the Caspian Sea. We have put up a team to monitor the progress and we are engaging early with the equipment suppliers to ensure that the delivery of equipment will not impact our deliveries.

Saurabh Chugh, CLSA: Just two questions from me. In your financials, your share for the offshore and marine sector fell quite significantly from $46 million for the first half of last year to $25 million this year. Can you explain which segment or which associate was responsible for this? And secondly, my question on the FLNG contract, if I understand correctly, the fleet study was partly funded by Golar, so I just wanted to check the IP for the entire conversion sits with Keppel or would it be sitting with Golar, or how does that arrangement work?

CHC: I'll take the question on the associates. I think it was also mentioned in the previous quarter that last year's number was actually higher because of Floatec – we benefitted from some form of variation orders last year. So as a result, this year when you look at y-o-y comparison, the number is lower. So that's one of the main contributors.

CYY: On the Golar FLNG, the IP, the fleet study that we did, we jointly own those IP with Golar.

Ke Yen, Religare: Question one, is there an update on potential sale of the *Can-Do!* drillship, how do you look at the drillship market now? Second question, any updates on the management agreement of the Quanzhou shipyard?

LCH: I believe both those questions have been answered.

Ke Yen, Religare: Recently you've made progress in deepsea mining, what do you plan to do with this business? Do you intend to focus on related sea-mining technology? Or act as a mining company?

LCH: To be more accurate, we haven't started, we have just gotten to the starting point. Mr Ong Ye Kung just came back from Jamaica and we have successfully lodged our application for the first area. Of course, it is still subject to the contract being signed. But this is a very long-term project, and we see that there is going to be a very interesting opportunity here. There's still a lot of things that need to be worked out. We need the environmental areas to be very supportive, the regulations, and of course the technology, will still have to be developed. So I would say that it's a bit early for us to comment on that.

Rujun Shen, Thomson Reuters: Do you see staff cost in offshore and marine continue to rise and eat into profit? What does the company plan to do to keep staff cost in check?

LCH: As the volume of work goes up, you would expect that staff cost would go up. But I think that is just answering it from the financial statements point of view. But I think on the longer term, you've heard what YY said, we are looking at how we can make better use of our regional yards and we've been investing in them.

We have two in the Philippines, one in Bintan and one in Nantong, and of course when Quanzhou gets concluded, we will have another yard in China. So we will see some of the work shifted to them over time. The reality is that cost of doing business in Singapore is getting more expensive, the land cost is going up and of course, there are various ratios that we have to look at. So our goal is to try to look for opportunities to do more work in our sister yards in the region.

<End of Q&A session>

Transcribed by: CL & EW