

NAT US - Shipping - Company update - 05 April 2019

# Nordic American Tanker Shipping Ltd

## Arctic Buy

Risk	High
Target (USD)	3.10
Price (USD)	1.88
Market Cap (USDm)	304
Enterprise Value (USDm)	671
No of shares, fully dil. (m)	142.0

## Refinanced and out of the creditors' grip - market slump is temporary

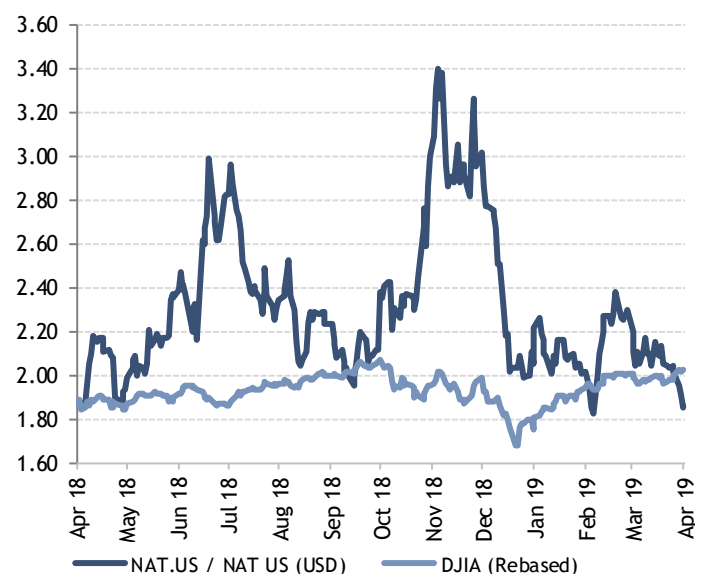
YTD, NAT has lagged listed tanker peers, and we attribute the weak share price performance to the poor development in Suezmax rates. However, the weakness in rates can be explained by factors that we think are about to reverse, and we remain upbeat about the prospects for the tanker market. With the new USD 306m senior secured credit facility in place, NAT is now in a better position to reap the rewards from what we believe will be a strong tanker market going forward. Although lowered OPEC output, higher than usual refinery maintenance and general seasonality are factors that are currently putting pressure on rates, we believe that US exports, the expected demand impact from IMO 2020 as well as lowered fleet productivity in preparation for IMO 2020 are all factors that point to a market rebound.

- Market slump is temporary:** Anyone in doubt as to whether or not refiners are preparing for the upcoming IMO regulations need look no further than the US. Seasonal maintenance is way up and the composition of output significantly changing. Refineries have cut runs by 1.7mbpd from the Q4 peak vs a typical drop of 1.3mbpd (similar trend in Asia). Bigger than normal refinery maintenance in Q1 is a drag and is being made worse by the fact that the widening discount on forward oil prices relative to spot is discouraging refiners from putting more oil into inventory. This is a transitory situation, in our view, and we foresee a sharp rebound in refinery activity into the spring, accentuated by the rush to produce more IMO compliant fuel. In such a situation, we expect rates to rebound, and we remain upbeat about the tanker market.
- Out of the creditors' grip, but lagging peers:** In February, NAT announced that it had entered into a 5yr USD 306m senior secured credit agreement, retiring the previous RCF in full. The facility has a 20yr profile, and according to NAT, it will see the effective interest be reduced compared to what was paid under the RCF at the end of 2018. As such, focus can once again return to dividends. On our estimates, NAT will generate more than USD 120m in FCFE in 2020. However, YTD, the NAT share is down by -7%, which compares to +15-23% for crude tanker peers FRO, DHT and EURN. As we are convinced that a rebound in tanker rates will be widespread, we see this as a buying opportunity.
- Arctic Buy and TP USD 3.1 reiterated:** We estimate Q1/19 NAV of USD 2.64/sh, implying P/NAV and EV/GAV of 0.71x and 0.85x, and implicitly valuing a 5yr old Suezmax at USD -42m. After the refinancing, NAT is again out of the grip of its creditors, and given our view on the tanker market, we believe that shareholders will be handsomely rewarded. Arctic Buy and TP USD 3.1 reiterated.

## Key Figures

USDm	2016	2017	2018	2019e	2020e
Sales	237	155	124	185	282
Adj. EBITDA	144	54	22	107	205
Adj. EBIT	53	-46	-38	39	136
Adj. EBIT margin	22.5%	n.m.	n.m.	21.4%	48.1%
EPS (USD)	0.4	-0.7	-0.7	0.0	0.7
Adj. dil. EPS (USD)	0.4	-0.7	-0.7	0.0	0.7
Adj. EPS growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Net IB debt	361	330	387	349	288
ROE	3.6%	-9.0%	-15.7%	0.9%	17.4%
ROCE	3.9%	-3.7%	-3.6%	4.0%	13.9%
DPS (USD)	1.1	0.4	0.1	0.3	0.6
Dividend yield	13.9%	14.6%	5.0%	15.4%	32.4%
FCFE yield	-7.1%	-4.3%	24.3%	24.3%	54.7%
EV/Sales	5.0x	4.4x	5.4x	3.3x	2.0x
Adj. EV/EBITDA	8.3x	12.5x	30.4x	5.8x	2.7x
Adj. EV/EBIT	22.4x	n.m.	n.m.	15.6x	4.1x
P/E	22.1x	n.m.	n.m.	50.2x	2.6x
P/B	0.9x	0.4x	0.5x	0.5x	0.4x

## Share Price



## Arctic vs Consensus

USDm	Arctic			Consensus			Deviation		
	2019e	2020e	n.a.	2019e	2020e	n.a.	2019e	2020e	n.a.
Sales	185	282	n.a.	183	209	n.a.	1%	35%	n.a.
EBITDA	107	205	n.a.	93	127	n.a.	15%	61%	n.a.
EBIT	39	136	n.a.	25	56	n.a.	56%	142%	n.a.
EPS	0.0	0.7	n.a.	(0.1)	0.2	n.a.	162%	287%	n.a.

## Forecast Changes

USDm	New			Old			Change		
	2019e	2020e	n.a.	2019e	2020e	n.a.	2019e	2020e	n.a.
Sales	185	282	n.a.	232	282	n.a.	-20%	0%	n.a.
EBITDA	107	205	n.a.	154	205	n.a.	-31%	0%	n.a.
EBIT	39	136	n.a.	82	133	n.a.	-52%	2%	n.a.
EPS	0.0	0.7	n.a.	0.4	0.9	n.a.	-90%	-15%	n.a.

# Nordic American Tanker Shipping Ltd

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## Company description

Nordic American Tankers is the world's 4<sup>th</sup> largest owner of Suezmaxes, and the fleet counts 23x vessels, of which 3x are on long-term finance leases from Ocean Yield. NAT was incorporated in Bermuda in 1995, and was listed on the NYSE in September the same year. Since inception, NAT's focus has been to have a relatively low leverage and to distribute cash to its shareholders. Since inception, NAT has distributed USD 48.5 in cash dividends per share.

## Arctic case

After nine dreadful months, last year finished off with a surge in tanker spot rates. The rally was widespread, and all major size segments in both dirty and clean enjoyed healthy returns in the last three months of the year. We believe that the Q4 rate surge is evidence that the market was, in fact, not structurally oversupplied, and expect that there is more to come for the tanker owners. Although the busy 2019 delivery schedule, lowered OPEC output and general seasonality are likely to lead to some bumpiness in rates, we expect the improvements seen in late 2018 to continue in 2019 and 2020. Increasing US exports, the expected demand impact from IMO 2020 as well as lowered fleet productivity in preparation for IMO 2020 are all factors that point to continued improvements. We keep our rate estimates unchanged, and expect Suezmax rates to average USD 28k/d and USD 35k/d in 2019 and 2020, respectively.

## Bull case

The crude tanker market turns out to be better than expected - lifting asset values. Upside potential could be highly attractive should the rate environment improve and lift asset values higher. A 10% increase in asset values corresponds to a ~19% increase in NAT's NAV.

## Bear case

Crude tanker freight rates dwindle back to depressed levels when the winter season comes to an end. Newbuild prices once again fall as yards work to attract business, and secondhand values come under pressure again. Downside risk is in our view around 5-10% on asset values.

## Catalysts

- Rise in spot rates, hence rise in 1-year charter rates, leading to asset value appreciation
- Change in trade dynamics creating an increase in ton-miles (i.e. more Atlantic Basin output)
- Turning inventory cycle
- Scrapping of older tonnage

## Risks

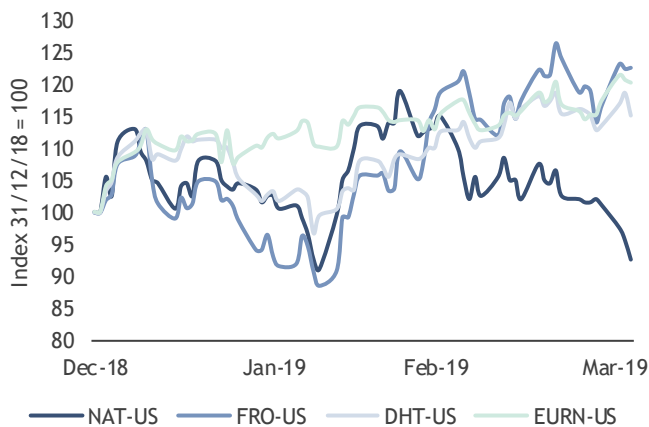
- Sustained pressure on asset values
- Shipowners tempted by low newbuilding prices at struggling shipyards
- Change in trade routes leading to a decrease in ton-miles (i.e. Atlantic Basin producers remain under pressure and increased output from MEG and Asia)

## Investment case

**NAT has lagged tanker peers** - Relative to other listed tanker owners, NAT has performed very weakly so far in 2019. While VLCC owners FRO, DHT and EURN are up by 15-23%, NAT is actually down by ~7% since the end of last year. We believe that the main reason for it lagging is the weak development in Suezmax tanker rates, while part of the optimism in the other tanker names can possibly be explained by the unseasonably strong VLCC rates seen until mid-March.

### Share price performance

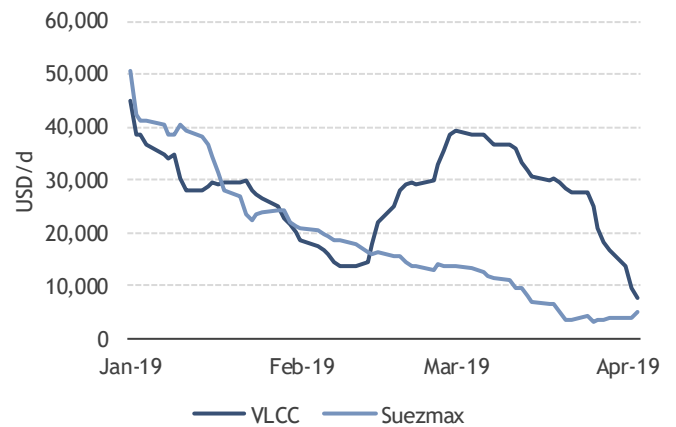
*NAT has significantly underperformed tanker peers...*



Source: Arctic Securities Research, Company data

### VLCC vs. Suezmax rates

*...which is likely due to the weak development in Suezmax rates*

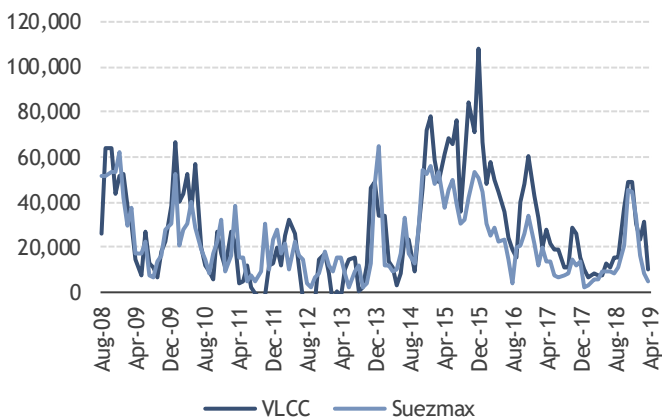


Source: Arctic Securities Research, Company data

**We expect the historical relationship between VL and Suezmax rates to hold** - However, historically, VLCC and Suezmax rates have been highly correlated, and in our view, the rates for the two different ship types are likely to continue to move in tandem. Both ship types carry crude, and hence, the demand drivers are basically the same. This was the case when rates surged in Q4, and in our view, the strength in VL rates was more surprising than the weakness in Suezmax rates.

### VLCC vs. Suezmax rates

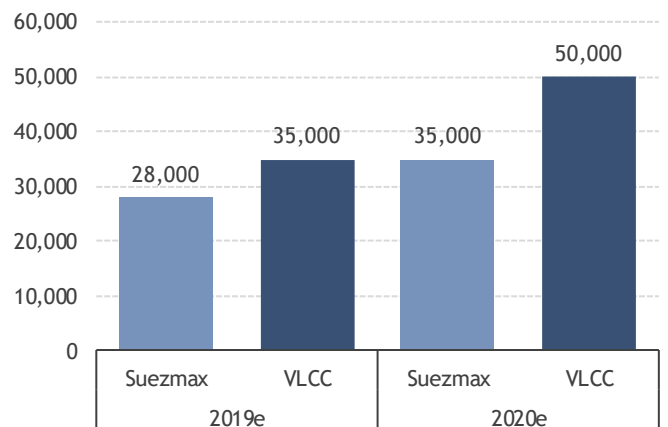
*High historical correlation between Suezmax and VLCC rates...*



Source: Arctic Securities Research, Company data

### Rate estimates

*...which we expect will continue going forward*



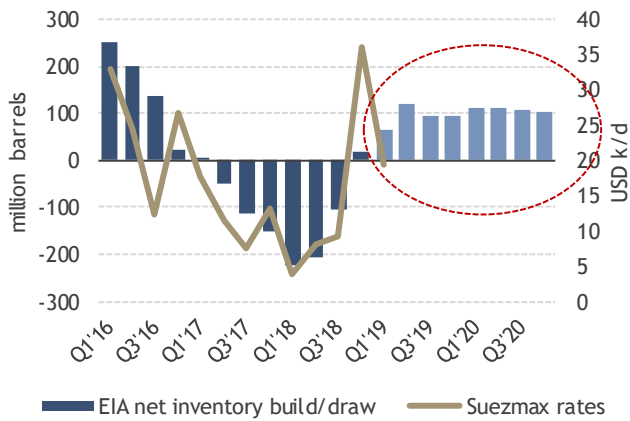
Source: Arctic Securities Research, Company data

**Favourable market dynamics** - We remain very optimistic for the tanker market, and see several factors that are likely to lead to strong demand dynamics going forward. Firstly, we foresee a sharp rebound in refinery activity into the spring, accentuated by the rush to produce more IMO compliant fuel. Also, we view the current inventory cycle as supportive for tanker demand; the inventory overhang was effectively eliminated through the draw-downs in 2017 and 2018, and we believe that incremental oil demand will now be served by oil imports/exports. The balanced inventory

levels, combined with increasing US exports are factors that make us less concerned about OPEC production cuts. OPEC is cutting due to increased supply from other countries - predominantly the US - and sailing distances from the US are roughly twice as long as from the Arabian Gulf.

### Favourable inventory cycle

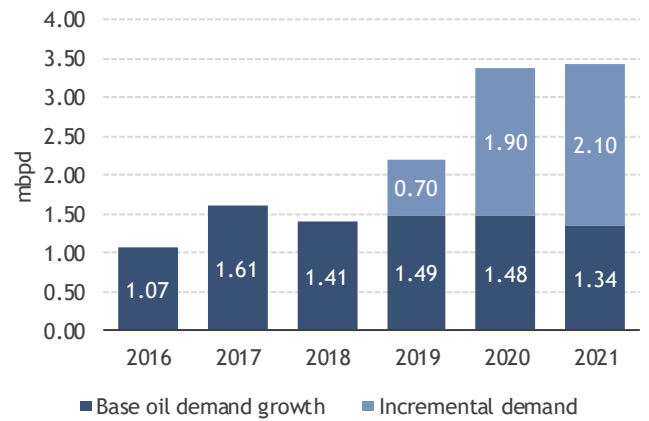
We are getting out of a period with significant inventory draw-downs



Source: Arctic Securities Research, EIA, Company data

### IMO is expected to positively impact oil demand

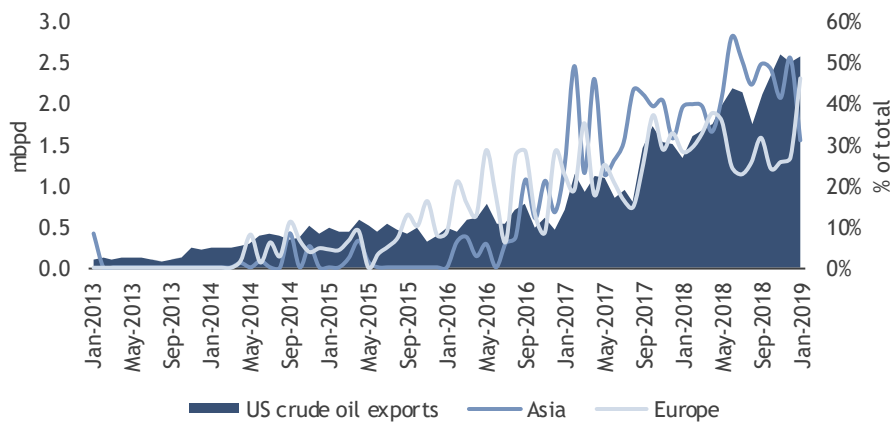
Refineries will need to adjust to IMO regulations



Source: Arctic Securities Research, Frontline

### US crude oil exports

US crude oil exports are currently hovering around the ~2.5mbpd mark



Source: Arctic Securities Research, EIA, Company data

**Recent weakness easily explained** - Anyone in doubt as to whether or not refiners are preparing for the upcoming IMO regulations need look no further than the US. Seasonal maintenance is way up and the composition of output significantly changing. Refineries have cut runs by 1.7 mbd from the Q4 peak vs a typical drop of 1.3 mbd, as they prepare for an all-out effort in H2 when distillate demand is expected to pick up sharply. Bigger than normal refinery maintenance in Q1 is a drag and is being made worse by the fact that the widening discount on forward oil prices relative to spot is discouraging refiners from putting more oil into inventory. This is most definitely a transitory situation, in our view, as we foresee a sharp rebound in refinery activity into the spring, accentuated by the rush to produce more IMO compliant fuel. Furthermore, this week, Reuters reported that crude flows into Asia fell to -24.1mbpd for March, a sharp 9% (2.4mbpd) drop from the estimated 26.5mbpd the agency saw in February. While Feb lows may have been inflated, we believe such a plunge can only be explained by Asian refiners also undergoing extended maintenance. As with the US refiners, we expect this to be temporary and we see March imports as unsustainably low. Nonetheless, we believe that these factors are behind the weak tanker market seen over the past weeks.

**Surging period market** - Another interesting development over the past weeks has been a surge in period market interest with leading trading names stepping up to the plate and booking tonnage in



the clean and aframax crude segments. Oil traders have a front row seat to refinery operations and short-term inventory trends, both key drivers of tanker activity. These latest moves suggest they expect a tightening market in the second half of the year.

**Out of the creditors' grip, but lagging peers:** In February, NAT announced that it had entered into a 5yr USD 306m senior secured credit agreement, retiring the previous RCF in full. The facility has a 20yr profile, and according to NAT, it will see the effective interest be reduced compared to what was paid under the RCF at the end of 2018. As such, focus can once again return to dividends. On our estimates, NAT will generate more than USD 120m in FCFE in 2020. However, YTD, the NAT share is down by ~7%, which compares to +15-23% for crude tanker peers FRO, DHT and EURN. As we are convinced that a rebound in tanker rates will be widespread, we see this as a buying opportunity.

## Q1/19e NAV

Trading at P/NAV 0.71x

USDm	# of units	Average age	NAV	Implied
Suezmax	23x	11.2	713	606
<b>Fleet</b>	<b>23x</b>	<b>11.2</b>	<b>713</b>	<b>606</b>
Debt			424	424
Cash			41	41
Rem. Capex			0	0
Net other			44	44
NAV / mcap			374	267
# of shares			142	142
NAV /share USD			2.64	1.88
NAV /share USD			2.64	1.88
Share price USD			1.88	
P/NAV			.71x	
EV/GAV			.85x	
Net LTV			53.7%	63.2%

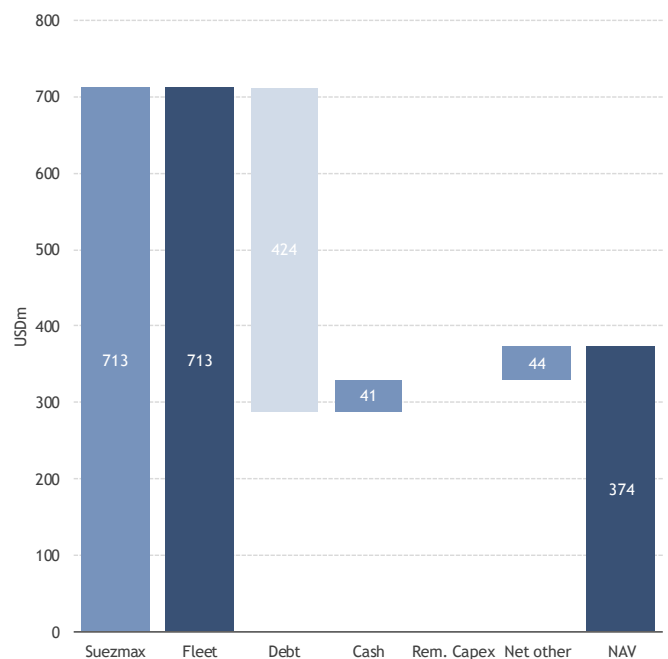
  

Per unit (USDm)	Value per unit	Implied per unit
Suezmax	31.0	26.3
Suezmax resale	64.0	54.4
Suezmax 5yr	49.5	42.0

Source: Arctic Securities Research, Company data

## NAV build-up

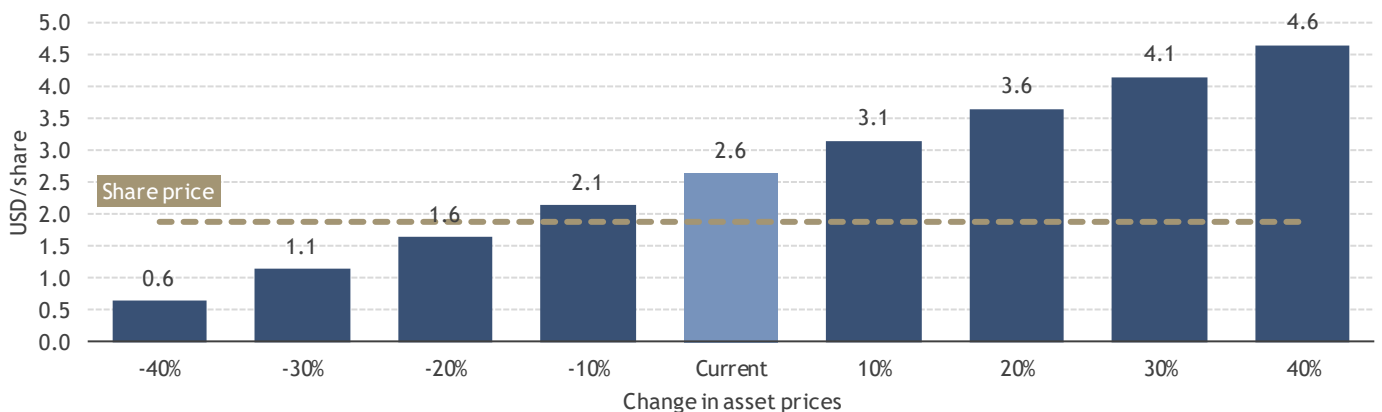
We estimate a total fleet value of USD 713m



Source: Arctic Securities Research, Company data

## NAV sensitivity

We estimate that a 10% change in asset values would lead to a ~19% (USD ~0.50/sh) change in NAV



Source: Arctic Securities Research, Company data

## Profit & loss statement

Profit & loss (USDm)	2016	2017	2018	2019e	2020e
<b>Sales</b>	<b>237</b>	<b>155</b>	<b>124</b>	<b>185</b>	<b>282</b>
Operating expenses	-93	-100	-93	-78	-78
<b>Adj. EBITDA</b>	<b>144</b>	<b>54</b>	<b>22</b>	<b>107</b>	<b>205</b>
<b>EBITDA</b>	<b>144</b>	<b>54</b>	<b>22</b>	<b>107</b>	<b>205</b>
Depreciation	-91	-101	-60	-67	-69
<b>EBITA</b>	<b>53</b>	<b>-46</b>	<b>-38</b>	<b>39</b>	<b>136</b>
Amortisation & impairment					
Other expenses or revenues					
<b>Adj. EBIT</b>	<b>53</b>	<b>-46</b>	<b>-38</b>	<b>39</b>	<b>136</b>
<b>EBIT</b>	<b>53</b>	<b>-46</b>	<b>-38</b>	<b>39</b>	<b>136</b>
Net interest	-11	-20	-34	-34	-31
Other financial items	-10	-9	-22		
<b>Pre-tax profit</b>	<b>33</b>	<b>-76</b>	<b>-94</b>	<b>5</b>	<b>104</b>
Minority interests					
Taxes					
<b>Net profit</b>	<b>33</b>	<b>-76</b>	<b>-94</b>	<b>5</b>	<b>104</b>
Reported EPS (USD)	0.37	-0.71	-0.66	0.04	0.74
Adj. EPS (USD)	0.37	-0.71	-0.66	0.04	0.74
<b>Adj. EPS fully diluted (USD)</b>	<b>0.37</b>	<b>-0.71</b>	<b>-0.66</b>	<b>0.04</b>	<b>0.74</b>
Sales growth	-17.5%	-34.7%	-19.8%	48.8%	53.0%
Adj. EBITDA growth	-31.5%	-62.3%	-59.4%	384.1%	91.4%
Adj. EBIT growth	-58.4%	n.m.	n.m.	n.m.	244.2%
Adj. Pre-tax profit growth	-72.0%	n.m.	n.m.	n.m.	1,861.8%
Adj. Net profit growth	-72.0%	n.m.	n.m.	n.m.	1,861.8%
EPS reported growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Adj. EPS growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Adj. EPS fully diluted growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Adj. EBITDA margin	60.9%	35.2%	17.8%	57.9%	72.4%
Adj. EBITA margin	22.5%	n.m.	n.m.	21.4%	48.1%
Adj. EBIT margin	22.5%	n.m.	n.m.	21.4%	48.1%
Adj. Pre-tax margin	13.9%	-48.8%	-76.1%	2.9%	37.0%
Adj. Net margin	13.9%	n.m.	n.m.	2.9%	37.0%

Source: Arctic Securities research

## Balance sheet & cash flow

Balance sheet (USDm)	2016	2017	2018	2019e	2020e
Goodwill	19	19			
Other intangible assets					
Property, plant & equipment	1,140	1,096	954	894	853
Other fixed financial assets					
Other fixed assets	64	28	4	4	4
<b>Total non-current assets</b>	<b>1,224</b>	<b>1,144</b>	<b>958</b>	<b>899</b>	<b>857</b>
Inventories	21	23	20	20	20
Receivables	18	22	23	23	23
Other current assets	43	23	21	21	21
Cash & cash equivalents	82	58	49	59	98
<b>Total current assets</b>	<b>164</b>	<b>127</b>	<b>113</b>	<b>122</b>	<b>162</b>
<b>Total assets</b>	<b>1,387</b>	<b>1,271</b>	<b>1,071</b>	<b>1,021</b>	<b>1,019</b>
<b>Total shareholders' equity</b>	<b>908</b>	<b>841</b>	<b>602</b>	<b>581</b>	<b>600</b>
Minorities					
Provisions					
Long-term IB debt	443	389	418	386	363
Other long-term liabilities	15	16	15	15	15
<b>Total non-current liabilities</b>	<b>457</b>	<b>405</b>	<b>433</b>	<b>401</b>	<b>378</b>
Short-term IB debt			19	22	23
Payables	4	3	4	4	4
Other current liabilities	17	22	14	14	14
<b>Total current liabilities</b>	<b>22</b>	<b>25</b>	<b>36</b>	<b>40</b>	<b>40</b>
<b>Total liabilities</b>	<b>479</b>	<b>430</b>	<b>469</b>	<b>440</b>	<b>418</b>
<b>Total equity and liabilities</b>	<b>1,387</b>	<b>1,271</b>	<b>1,071</b>	<b>1,021</b>	<b>1,019</b>
Cash & cash equivalents	82	58	49	59	98
Gross IB debt	443	389	437	408	386
Net IB debt	361	330	387	349	288
Working capital	35	42	39	39	39
Capital employed	1,366	1,245	1,035	981	978
Net IB debt/Equity	39.7%	39.3%	64.3%	60.1%	47.9%
Equity/Assets	65.5%	66.2%	56.2%	56.9%	59.0%
<b>Cash flow (USDm)</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>
Net profit	33	-76	-94	5	104
Non-cash adjustments	95	107	78	67	69
Change in working capital					
<b>Operating cash flow</b>	<b>128</b>	<b>32</b>	<b>-16</b>	<b>73</b>	<b>173</b>
Capital expenditures	-188	-38	85		
<b>Free cash flow (FCF)</b>	<b>-59</b>	<b>-15</b>	<b>69</b>	<b>65</b>	<b>146</b>
Change in debt	117	-55	-68	-29	-22
Dividend paid	-126	-54	-10	-26	-85
Share issues & buybacks	120	104	-0		
Other non-cash adjustments	-0	-3	0		
<b>Financing cash flow</b>	<b>111</b>	<b>-9</b>	<b>-78</b>	<b>-55</b>	<b>-107</b>
<b>Change in cash</b>	<b>52</b>	<b>-24</b>	<b>-9</b>	<b>9</b>	<b>39</b>

Source: Arctic Securities research



## Key ratios & Valuation

Share data	2016	2017	2018	2019e	2020e
Shares outstanding (m)	102.0	142.0	142.0	142.0	142.0
Shares fully diluted (m)	102.0	142.0	142.0	142.0	142.0
Shares fully diluted average (m)	102.0	142.0	142.0	142.0	142.0
Share price USD (year-end)	8.18	2.46	2.00	1.88	1.88
Market capitalisation (USDm)	834	349	284	267	267
Adj. enterprise value (USDm)	1	1	1	1	1
EPS reported (USD)	0.37	-0.71	-0.66	0.04	0.74
Adj. EPS (USD)	0.37	-0.71	-0.66	0.04	0.74
Adj. EPS fully diluted (USD)	0.37	-0.71	-0.66	0.04	0.74
DPS (USD)	1.14	0.36	0.10	0.29	0.61
Growth	2016	2017	2018	2019e	2020e
Sales growth	-17.5%	-34.7%	-19.8%	48.8%	53.0%
Adj. EBITDA growth	-31.5%	-62.3%	-59.4%	384.1%	91.4%
Adj. EBIT growth	-58.4%	n.m.	n.m.	n.m.	244.2%
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EPS reported growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Adj. EPS growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Adj. EPS fully diluted growth	-71.9%	n.m.	n.m.	n.m.	1,861.8%
Margins	2016	2017	2018	2019e	2020e
Adj. EBITDA margin	60.9%	35.2%	17.8%	57.9%	72.4%
Adj. EBITA margin	22.5%	n.m.	n.m.	21.4%	48.1%
Adj. EBIT margin	22.5%	n.m.	n.m.	21.4%	48.1%
Adj. Pre-tax margin	13.9%	-48.8%	-76.1%	2.9%	37.0%
Adj. Net margin	13.9%	n.m.	n.m.	2.9%	37.0%
Valuation	2016	2017	2018	2019e	2020e
EV/Sales	5.0x	4.4x	5.4x	3.3x	2.0x
Adj. EV/EBITDA	8.3x	12.5x	30.4x	5.8x	2.7x
Adj. EV/EBIT	22.4x	n.m.	n.m.	15.6x	4.1x
P/E	22.1x	n.m.	n.m.	50.2x	2.6x
Adj. P/E	22.1x	n.m.	n.m.	50.2x	2.6x
P/B	0.9x	0.4x	0.5x	0.5x	0.4x
Profitability	2016	2017	2018	2019e	2020e
FCFE yield	-7.1%	-4.3%	24.3%	24.3%	54.7%
ROE	3.6%	-9.0%	-15.7%	0.9%	17.4%
ROCE	3.9%	-3.7%	-3.6%	4.0%	13.9%
Dividend yield	13.9%	14.6%	5.0%	15.4%	32.4%

Source: Arctic Securities research



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