



KNOT Offshore Partners LP (KNOP)

Updated November 20th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$16.98	5 Year CAGR Estimate:	10.3%	Market Cap:	\$570.2 M
Fair Value Price:	\$17.29	5 Year Growth Estimate:	0.0%	Ex-Dividend Date¹:	01/28/2022
% Fair Value:	98%	5 Year Valuation Multiple Estimate:	0.4%	Dividend Payment Date¹:	02/11/2022
Dividend Yield:	12.2%	5 Year Price Target	\$17.29	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	B	Last Dividend Increase:	N/A

Overview & Current Events

KNOT Offshore Partners LP owns and operates shuttle tankers under long-term charters in the North Sea and Brazil. The company provides loading, transportation, and storage of crude oil under time charters and bareboat charters. The company's sponsor, Knutsen NYK Offshore Tankers AS (Knutsen NYK) is responsible for identifying, ordering and dropping down ships to KNOP. As of its latest filings, it had a fleet of sixteen shuttle tankers. As a result of its mostly passive operations, the company has only one employee and executive, its CEO Mr. Gary Chapman, who oversees the company and ensures that all tankers maximize their charter periods, maximizing their value through long-term contracts. The company was founded in 2013 and is headquartered in Aberdeen, the United Kingdom.

On November 17th, 2021, KNOT Offshore Partners LP reported its Q3-2021 results for the quarter ending September 30th, 2021. KNOT's fleet operated with 91.9% utilization for scheduled operations during the quarter, generating total revenues of \$66.6 million, which was 6.0% lower compared to Q2. The decrease was mainly due to the lower utilization of Windsor Knutsen while idling/waiting to commence on the time charter contract with PetroChina and off-hire of Tordis Knutsen due to a technical fault on its azimuth thruster causing the vessel to be off-hire for 37 days.

Distributable cash flow was \$18.6 million, compared to \$24.0 million in the previous quarter. The decrease in distributable cash flow was mainly due to the lower utilization, as just mentioned, and higher operating and administration costs. On a per-share basis, quarterly DCFU² was \$0.52 vs. \$0.73 during the previous quarter.

As of June 30th, the partnership's fleet of seventeen vessels had charters with an average remaining fixed duration of 2.1 years. In addition, the partnership's time charter vessels have options to extend their charters by an additional 2.7 years on average. Following the third quarter's results, we are updating our FY2021 DCFU estimate at \$2.75.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
DCFU	---	---	\$3.07	\$4.15	\$4.49	\$2.81	\$2.53	\$3.15	\$3.18	\$3.36	\$2.47	\$2.47
DPS	---	---	\$1.19	\$1.85	\$2.06	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08
Shares³	---	---	17.5	20.2	25.8	27.8	30.6	33.3	33.3	33.3	33.7	35.0

The partnership's DCFU has hovered between \$2.50 and \$4.50 based on the charter rates the partnership is able to negotiate upon every renewal. While we could use a higher earnings power in our future estimates due to the on-off impact during Q1 for FY2021, KNOT has chartering gaps in four of its vessels in 2022 so far, so we remain prudent.

Distribution coverage has become slightly more worrying as of Q3 amid low option extensions resulting in a declined average fixed duration. However, KNOT has three potential drop-downs from its sponsor through 2022, which should add incrementally to its profitability. Hence, we expect stable DCFU and distributions going forward for the time being.

¹ Estimated dates.

² DCFU refers to Distributable Cash Flow per Unit.

³ Share count is in millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
P/DCFU	---	---	7.86	6.35	4.37	7.47	9.32	6.5	5.8	4.5	6.9	7.0
Avg. Yld.	---	---	4.8%	6.6%	10.6%	13.0%	9.1%	10.0%	11.1%	11.1%	12.2%	12.0%

KNOT has historically traded with a valuation multiple in the mid-single digits. Units are currently offering a massive yield of 12.2%. Despite its covered distributions, KNOT's long-term revenues are not guaranteed, as tankers have a limited life value. The risk of its sponsor not being able to drop down tankers in the future is worth considering, resulting in the low multiple and massive yield to compensate investors who are willing to hold shares. Due to the very high tangible returns making the stock increasingly attractive in the current low-rate environment, we believe a P/DCFU of 7 is fair.

Safety, Quality, Competitive Advantage, & Recession Resiliency

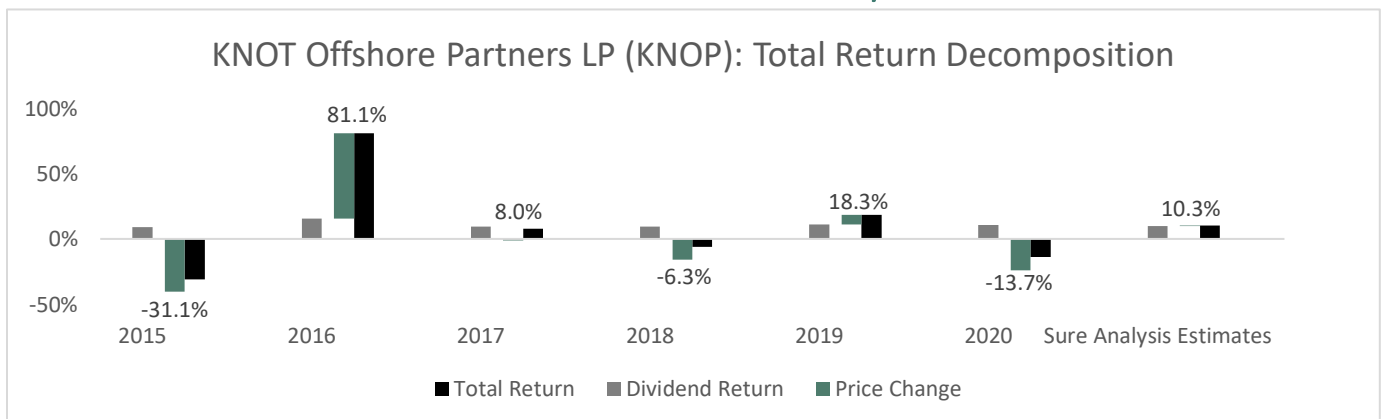
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	---	39%	45%	46%	74%	82%	66%	65%	62%	84%	84%

KNOT Offshore is one of the highest quality shipping partnerships, offering relative stability compared to its peers. Unlike most shipping partnerships, which report wildly fluctuating financials, KNOT's performance has been relatively stable due to its ability to negotiate fixed contracts. Further, due to the limited available supply of tankers, the partnership does not face significant competition, as its contracts are mostly based on the energy industry's performance. Despite the adverse effect on the energy sector during the pandemic, the partnership was able to deliver resilient results; hence we believe operations should remain steady under a potential recession. Still, noteworthy risks remain in terms of the partnership's future lifetime value. Its fleet currently has an average age of 7.8 years. It should provide cash flows for the next couple of decades. We believe that the partnership's distributions will remain covered in the next few years due to fixed contracts, though the risk has grown amid more off-higher days due to chartering gaps and dry-dockings.

Final Thoughts & Recommendation

KNOT Offshore Partners is a trustworthy shipping partnership for income-orienting investors, featuring a massive, well-covered yield. We believe that the partnership should achieve steady revenues and distributions in the medium term. We estimate annualized returns of around 10.3%, wholly powered by the stock's distributions and stable valuation assumptions. KNOP earns a buy rating, but conservative income investors should remain cautious regarding KNOT's distributions.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	66	73	113	155	174	219	279	283	279
Gross Profit	31	35	55	79	87	101	134	133	128
Gross Margin	47.9%	48.2%	48.4%	50.7%	49.8%	46.0%	47.9%	46.9%	45.9%
SG&A Exp.	5	5	4	4	4	6	5	5	5
D&A Exp.	20	22	33	47	55	70	88	89	89
Operating Profit	27	30	50	74	82	95	129	128	123
Operating Margin	40.6%	40.8%	44.6%	48.0%	47.3%	43.5%	46.0%	45.2%	44.1%
Net Profit	1	15	27	40	61	68	82	59	65
Net Margin	1.1%	20.5%	24.3%	26.1%	35.2%	31.1%	29.4%	20.9%	23.3%
Free Cash Flow	19	44	59	88	108	154	149	166	169
Income Tax	1	3	0	(0)	(0)	(0)	(0)	0	0

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	512	660	1,071	1,220	1,292	1,793	1,837	1,738	1,780
Cash & Equivalents	1	29	31	24	28	46	42	44	53
Accounts Receivable	0	---	---	---	---	---	---	---	0
Inventories	1	1	1	1	1	2	2	2	3
Goodwill & Int. Ass.	6	6	6	---	---	2	2	1	1
Total Liabilities	415	378	651	699	771	1,064	1,105	1,026	1,083
Accounts Payable	0	1	2	2	2	5	5	3	698
Long-Term Debt	348	350	613	668	742	1,027	1,077	995	3,848
Shareholder's Equity	97	282	419	521	522	729	732	712	698

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	0.1%	2.6%	3.2%	3.5%	4.9%	4.4%	4.5%	3.3%	3.7%
Return on Equity	0.9%	7.9%	7.8%	8.6%	11.7%	10.9%	11.2%	8.2%	9.3%
ROIC	0.2%	4.3%	5.7%	6.3%	8.7%	7.7%	7.8%	5.7%	6.4%
Shares Out.	---	17.5	20.2	25.8	27.8	30.6	33.3	33.3	32.7
Revenue/Share	3.83	4.28	5.71	6.13	6.39	6.68	7.68	8.64	8.54
FCF/Share	1.12	2.58	3.00	3.47	3.96	4.69	4.08	5.07	5.17

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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