



# KNOT Offshore Partners LP (KNOP)

Updated August 27<sup>th</sup>, 2022 by Nikolaos Sismanis

## Key Metrics

<b>Current Price:</b>	\$16.78	<b>5 Year CAGR Estimate:</b>	9.0%	<b>Market Cap:</b>	\$565.6 M
<b>Fair Value Price:</b>	\$15.40	<b>5 Year Growth Estimate:</b>	0.0%	<b>Ex-Dividend Date<sup>1</sup>:</b>	10/27/2022
<b>% Fair Value:</b>	109%	<b>5 Year Valuation Multiple Estimate:</b>	-1.7%	<b>Dividend Payment Date<sup>1</sup>:</b>	11/10/2022
<b>Dividend Yield:</b>	12.4%	<b>5 Year Price Target</b>	\$15.40	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	C	<b>Rating:</b>	Hold

## 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 17 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 enter profitable charter periods, maximizing their value through long-term contracts. The company was founded in 2013 and is headquartered in Aberdeen, the United Kingdom.

On August 24<sup>th</sup>, 2022, KNOT Offshore Partners LP reported its Q2-2021 results for the quarter ending June 30<sup>th</sup>, 2022. KNOT's fleet operated with 100% utilization for scheduled operations during the quarter, generating total revenues of roughly \$64 million, which was 9.8% lower sequentially. The decrease was mainly due to increased off-hire in connection with the scheduled dry-dockings.

Distributable cash flow was \$9.4 million, compared to \$14.5 million in the previous quarter. The decrease was mainly the result of lower utilization of the fleet from the scheduled dry dockings and higher vessel operating costs. On a per-unit basis, quarterly DCFU<sup>2</sup> was \$0.27 vs. \$0.43 during the previous quarter.

As of March 31<sup>st</sup>, the partnership's fleet of 17 vessels had charters with an average remaining fixed duration of 1.7 years. In addition, the partnership's time charter vessels have options to extend their charters by an additional 2.4 years on average. With scheduled dry-dockings depriving the company of key cash flows and disrupting chartering optimization, distributable cash flows for the year should come notably lower than last year's levels. Still, the recent non-dilutive acquisition of Synnøve Knutsen, which operates on a fixed five-year time charter contract with Equinor, should provide some lift to results. We estimate a DCFU power of \$2.20, even though this year's number will end notably lower compared to 2021.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>DCFU</b>	---	\$3.07	\$4.15	\$4.49	\$2.81	\$2.53	\$3.15	\$3.18	\$3.36	\$2.65	<b>\$2.20</b>	<b>\$2.20</b>
<b>DPS</b>	---	\$1.19	\$1.85	\$2.06	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	<b>\$2.08</b>	<b>\$2.08</b>
<b>Shares<sup>3</sup></b>	---	17.5	20.2	25.8	27.8	30.6	33.3	33.3	33.3	33.6	<b>33.8</b>	<b>35.0</b>

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, KNOT' earnings can be affected notably by various effects, including scheduled dry dockings and fluctuating charter rates based on several macro conditions. Hence, we remain prudent. Still, the order book for shuttle tankers is shrinking, which is a positive

<sup>1</sup> Estimated dates.

<sup>2</sup> DCFU refers to Distributable Cash Flow per Unit.

<sup>3</sup> 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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catalyst for rates. Distribution coverage should plummet this year, but KNOT believes paying the distribution is in the best interest of shareholders for now. Full coverage should resume next year amid a lack of scheduled dry-dockings.

## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/DCFU	---	7.86	6.35	4.37	7.47	9.32	6.5	5.8	4.5	6.4	7.6	7.0
Avg. Yld.	---	4.8%	6.6%	10.6%	13.0%	9.1%	10.0%	11.1%	11.1%	12.2%	12.4%	13.5%

KNOT has historically traded with a valuation multiple in the mid-single digits. Units are currently offering a massive yield of 12.4%. We stress that KNOT's long-term revenues are not guaranteed, as chartering rates can fluctuate. The risk of its sponsor not being able to drop down vessels in the future is also worth considering. This justifies the low multiple and massive yield to compensate investors who are willing to hold shares. Due to the various risks attached to KNOT's business, we believe a P/DCFU of 7.0 is a fairer multiple to value the stock going forward.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

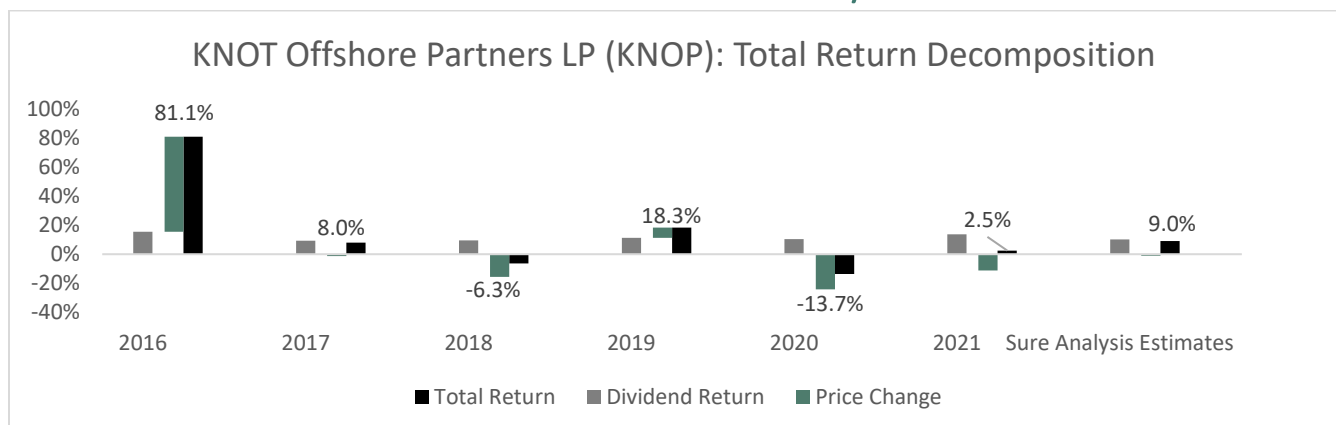
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	---	39%	45%	46%	74%	82%	66%	65%	62%	78%	95%	95%

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 shuttle 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, especially if oil prices remain elevated. Still, noteworthy risks remain in terms of the partnership's future lifetime value. Its fleet currently has an average age of 8.5 years. It should provide cash flows for the next several decades.

## Final Thoughts & Recommendation

KNOT Offshore Partners is a trustworthy shipping partnership for income-orienting investors, featuring a massive yield. Coverage has become more ambiguous lately, but should improve next year. We believe that the partnership should achieve somewhat steady revenues and distributions in the medium-term. We estimate annualized returns of around 9.0% through 2027, largely powered by the stock's distributions, offset by the potential for valuation headwinds ahead. KNOP earns a hold rating. Conservative income investors should remain cautious regarding KNOT's distributions.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	73	113	155	174	219	279	283	279	281
Gross Profit	35	55	79	87	101	134	133	128	109
Gross Margin	48.2%	48.4%	50.7%	49.8%	46.0%	47.9%	46.9%	45.9%	38.8%
SG&A Exp.	5	4	4	4	6	5	5	5	6
D&A Exp.	22	33	47	55	70	88	89	89	99
Operating Profit	30	50	74	82	95	129	128	123	103
Operating Margin	40.8%	44.6%	48.0%	47.3%	43.5%	46.0%	45.2%	44.1%	36.7%
Net Profit	15	27	40	61	68	82	59	65	54
Net Margin	20.5%	24.3%	26.1%	35.2%	31.1%	29.4%	20.9%	23.3%	19.2%
Free Cash Flow	44	59	88	108	154	149	166	169	155
Income Tax	3	0	(0)	(0)	(0)	(0)	0	0	0

## Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	660	1,071	1,220	1,292	1,793	1,837	1,738	1,780	1,677
Cash & Equivalents	29	31	24	28	46	42	44	53	62
Accounts Receivable	---	---	---	---	---	---	---	0	0
Inventories	1	1	1	1	2	2	2	3	3
Goodwill & Int. Ass.	6	6	---	---	2	2	1	1	0
Total Liabilities	378	651	699	771	1,064	1,105	1,026	1,083	1,004
Accounts Payable	1	2	2	2	5	5	3	3	4
Long-Term Debt	350	613	668	742	1,027	1,077	995	3,848	967
Shareholder's Equity	282	419	521	522	729	732	712	698	673

## Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	2.6%	3.2%	3.5%	4.9%	4.4%	4.5%	3.3%	3.7%	3.1%
Return on Equity	7.9%	7.8%	8.6%	11.7%	10.9%	11.2%	8.2%	9.3%	7.9%
ROIC	4.3%	5.7%	6.3%	8.7%	7.7%	7.8%	5.7%	6.4%	5.4%
Shares Out.	17.5	20.2	25.8	27.8	30.6	33.3	33.3	32.7	37.1
Revenue/Share	4.28	5.71	6.13	6.39	6.68	7.68	8.64	8.54	7.59
FCF/Share	2.58	3.00	3.47	3.96	4.69	4.08	5.07	5.17	4.18

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

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