



KNOT Offshore Partners LP (KNOP)

Updated March 15th, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	\$6.01	5 Year CAGR Estimate:	11.1%	Market Cap:	\$204.8 M
Fair Value Price:	\$8.10	5 Year Growth Estimate:	0.0%	Ex-Dividend Date¹:	04/27/2023
% Fair Value:	74%	5 Year Valuation Multiple Estimate:	6.2%	Dividend Payment Date¹:	05/12/2023
Dividend Yield:	1.7%	5 Year Price Target	\$8.10	Years Of Dividend Growth:	0
Dividend Risk Score:	C	Retirement Suitability Score:	D	Rating:	Buy

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 18 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 January 12th, 2023, Knot Offshore Partners LP slashed its quarterly distribution by 95% to \$0.026, noting heightened uncertainty in the shuttle tanker market in the near term.

On March 15th, 2023, KNOT Offshore Partners LP reported its Q4-2022 and full-year results for the quarter ending December 31st, 2022. KNOT's fleet operated with 96.1% utilization for scheduled operations during the quarter, generating total revenues of roughly \$71.6 million, which was 5.3% higher sequentially. Despite the lower utilization, the increase was mainly due to Synnøve Knutsen, KNOT's newest shuttle tanker, also contributing to results.

Given that the partnership has essentially suspended its distribution, it didn't report distributable cash flows. However, we can manually calculate it. These are not official numbers, but we estimate DCF for the quarter was about \$11.4 million, up 4.6% compared to \$10.9 million in the previous quarter. On a per-unit basis, quarterly DCFU² should be close to \$0.34 versus \$0.31 during the previous quarter.

As of December 31st, 2022, the partnership's fleet of 18 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 2.2 years on average. For fiscal 2023, we expect the company's DCFU to benefit from higher offshore deep-water oil production in Brazil, offset by lower utilization rates and softer time charters. Our initial estimate is DCFU of \$1.35.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
DCFU	\$3.07	\$4.15	\$4.49	\$2.81	\$2.53	\$3.15	\$3.18	\$3.36	\$2.65	\$1.33	\$1.35	\$1.35
DPS	\$1.19	\$1.85	\$2.06	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	\$2.08	\$1.59	\$0.10	\$0.79
Shares³	17.5	20.2	25.8	27.8	30.6	33.3	33.3	33.3	33.9	33.9	33.9	37.0

The partnership's DCFU has fluctuated based on the charter rates the partnership is able to negotiate upon every renewal. KNOT's future earnings are highly unpredictable, as they can be affected notably by various effects, including scheduled dry dockings and volatile charter rates based on several macro conditions. One positive catalyst moving forward is the shrinking order book for shuttle tankers against a growing demand for oil. Still, we remain prudent and

¹ Estimated dates.

² DCFU refers to Distributable Cash Flow per Unit.

³ Share count is in millions.

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forecast stable DCFU ahead. After years of paying hefty distributions, the partnership chose to slash its payouts to preserve liquidity during an uncertain shuttle tanker environment ahead. We have assumed gradually growing distributions over the medium-term, though this is entirely speculative. Shuttle tanker rates are highly unpredictable.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
P/DCFU	7.86	6.35	4.37	7.47	9.32	6.5	5.8	4.5	6.4	11.0	4.5	6.0
Avg. Yld.	4.8%	6.6%	10.6%	13.0%	9.1%	10.0%	11.1%	11.1%	12.2%	10.8%	1.7%	9.8%

KNOT has historically traded with a valuation multiple in the mid-single digits. Units are currently offering a tiny yield following the recent distribution cut. Units are currently trading at a depressed multiple, as there are multiple uncertainties regarding the partnership's future earnings and distributions. That said, we believe the stock is undervalued from an earnings and NAV standpoint and retain our fair multiple at 6.0.

Safety, Quality, Competitive Advantage, & Recession Resiliency

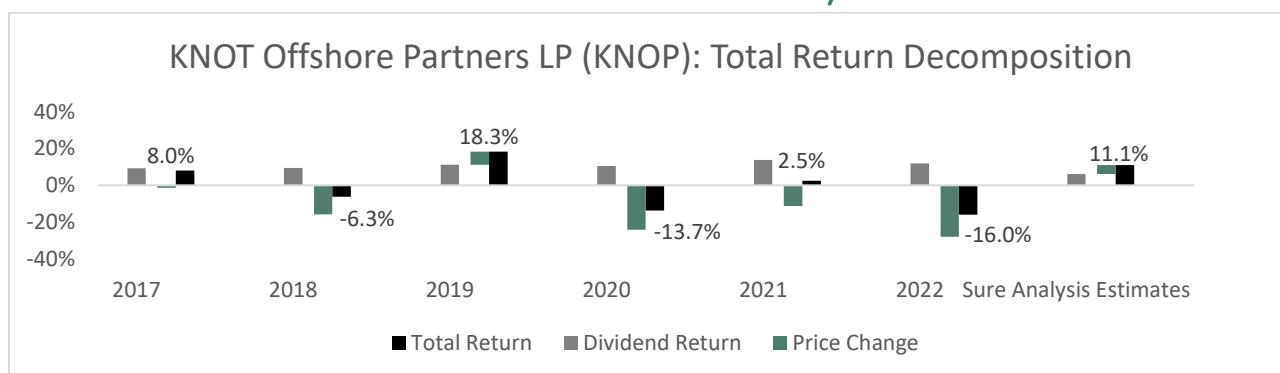
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	39%	45%	46%	74%	82%	66%	65%	62%	78%	120%	8%	59%

KNOT Offshore is one of the highest-quality shipping partnerships, offering relative stability compared to its peers. 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. The partnership's earnings are covered by charters that usually last a couple of years. Thus, despite the adverse effect on the energy sector during the pandemic, for instance, the partnership was able to deliver resilient results due to its fixed charters. Still, earnings can fluctuate wildly following renegotiations, as was the case in 2022. KNOT's earnings are not necessarily susceptible to a recession if oil prices remain elevated, nonetheless. Still, noteworthy risks remain in terms of the partnership's future lifetime value. Its fleet currently has an average age of 8.7 years. It should provide cash flows for the next couple of decades.

Final Thoughts & Recommendation

KNOT's investment case has transformed following the ongoing uncertainty in the shuttle tanker market and the parenthesis's distribution cut. The stock no longer appeals to income-oriented investors, though there could be a significant upside if rates were to rebound, leading to higher earnings and gradually higher distributions. Our projected returns for the stock are utterly speculative. We rate KNOP a speculative buy, but warn that there are multiple uncertainties regarding future returns. One massive risk at the moment is the partnership being taken private by its sponsor at a substantial discount, which could deprive current investors of the stock's bullish case. This was the case with Höegh LNG Partners LP (HMLP) following an identical setup.

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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