KNOT Offshore Partners LP (KNOP)

Updated December 14th, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	$5.73	**5 Year CAGR Estimate:**	9.0%	**Market Cap:**	$200.1 M
Fair Value Price:	$6.75	**5 Year Growth Estimate:**	0.0%	**Ex-Dividend Date[1]:**	01/25/2024
% Fair Value:	85%	**5 Year Valuation Multiple Estimate:**	3.3%	**Dividend Payment Date[1]:**	02/09/2024
Dividend Yield:	1.8%	**5 Year Price Target**	$6.75	**Years Of Dividend Growth:**	0
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	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 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 December 13th, 2023, KNOT Offshore Partners LP reported its Q3 results for the period ending September 30th, 2023. KNOT's fleet operated with 98.8% utilization for scheduled operations during the quarter, generating total revenues of roughly $72.8 million, which was 1.5% lower sequentially. Revenues in Q3 2023 were lower compared to Q2 2023 owing to revenues from spot voyages and loss of hire insurance recoveries in the previous quarter, which was partly offset by an increase in time charter and bareboat revenues in this quarter.

There was no impairment recognized in this quarter, compared to $49.6 million in impairments in Q2 2023 with respect to the Dan Cisne and the Dan Sabia. As a result, operating income came in at $20.6 million, compared to an operating loss of $31.2 million in the previous quarter.

Given that the partnership has essentially suspended its distribution, it didn't report distributable cash flows. That said, we believe that the company's distributable cash flow per unit based on its 9M-2023 results, charters, and market condition has the potential to be about $1.35.

At the end of Q3, the partnership's fleet of 18 vessels had charters with an average remaining fixed duration of 1.9 years. Further, the partnership's charterers have options to extend their charters by an additional 2.0 years on average.

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***
Shares[2]	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] 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	***4.2***	***5.0***
Avg. Yld.	4.8%	6.6%	10.6%	13.0%	9.1%	10.0%	11.1%	11.1%	12.2%	10.8%	***1.8%***	***11.7%***

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 5.0.

Safety, Quality, Competitive Advantage, & Recession Resiliency

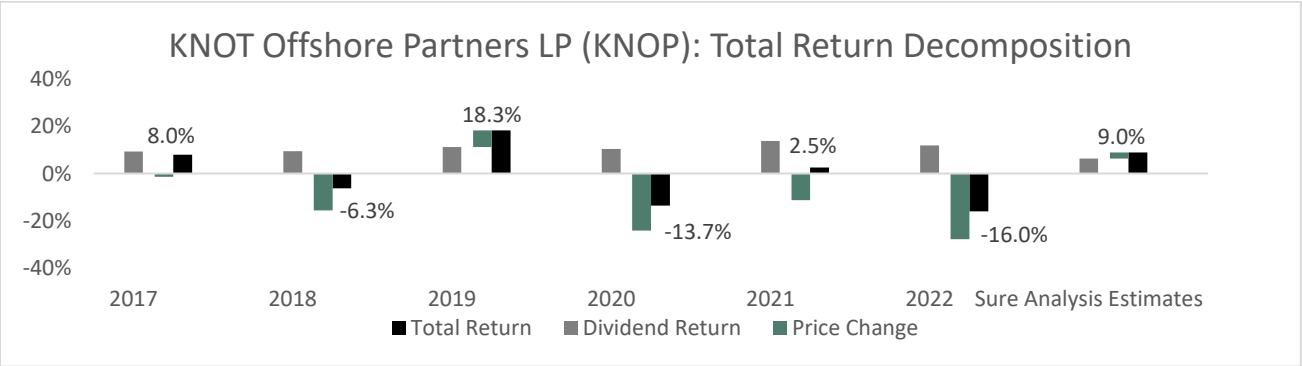
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	39%	45%	46%	74%	82%	66%	65%	62%	78%	120%	***8%***	***59%***

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 9.4 years, meaning that they 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 partnership'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 estimated returns for the stock are utterly speculative. We rate KNOP a hold, but warn that there are many 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	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	113	155	174	219	279	283	279	281	269
Gross Profit	55	79	87	101	134	133	128	109	72
Gross Margin	48.4%	50.7%	49.8%	46.0%	47.9%	46.9%	45.9%	38.8%	26.8%
SG&A Exp.	4	4	4	6	5	5	5	6	6
D&A Exp.	33	47	55	70	88	89	89	99	106
Operating Profit	50	74	82	95	129	128	123	103	66
Operating Margin	44.6%	48.0%	47.3%	43.5%	46.0%	45.2%	44.1%	36.7%	24.5%
Net Profit	27	40	61	68	82	59	65	54	59
Net Margin	24.3%	26.1%	35.2%	31.1%	29.4%	20.9%	23.3%	19.2%	21.9%
Free Cash Flow	59	88	108	154	149	166	169	155	98
Income Tax	0	(0)	(0)	(0)	(0)	0	0	0	1

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,071	1,220	1,292	1,793	1,837	1,738	1,780	1,677	1,734
Cash & Equivalents	31	24	28	46	42	44	53	62	48
Accounts Receivable	---	---	---	---	---	---	0	0	9
Inventories	1	1	1	2	2	2	3	3	6
Goodwill & Int. Ass.	6	---	---	2	2	1	1	0	0
Total Liabilities	651	699	771	1,064	1,105	1,026	1,083	1,004	1,082
Accounts Payable	2	2	2	5	5	3	3	4	4
Long-Term Debt	613	668	742	1,027	1,077	995	3,848	967	1,056
Shareholder's Equity	419	521	522	729	732	712	698	673	652

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	3.2%	3.5%	4.9%	4.4%	4.5%	3.3%	3.7%	3.1%	3.4%
Return on Equity	7.8%	8.6%	11.7%	10.9%	11.2%	8.2%	9.3%	7.9%	8.9%
ROIC	5.7%	6.3%	8.7%	7.7%	7.8%	5.7%	6.4%	5.4%	5.8%
Shares Out.	20.2	25.8	27.8	30.6	33.3	33.3	32.7	37.1	37.9
Revenue/Share	5.71	6.13	6.39	6.68	7.68	8.64	8.54	7.59	7.08
FCF/Share	3.00	3.47	3.96	4.69	4.08	5.07	5.17	4.18	2.58

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

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