

## Scorpio Tankers Inc.

**Lower to Neutral; Product tanker rates undershoot, PO \$45**

Rating Change: NEUTRAL | PO: 45.00 USD | Price: 42.36 USD

**Downgrade to Neutral, PO to \$45; A non-consensus call**

We lower our rating on Scorpio Tankers' (STNG) shares to Neutral (from Buy) and lower our PO to \$45 (from \$60) on 6.5x our 2024e EBITDA (from 4.6x 2023e) as we see rising risk to earning targets as we move past peak product tanker rates. Our non-consensus rating shift leaves us as the sole non-Buy on the Street. We decrease our 2Q23, 2023, and 2024 EPS estimates 33%, 13%, and 1%, respectively, to \$2.33, \$7.55, and \$3.10, from \$3.50, \$8.70, and \$3.15 given accelerated moderation in product tanker rates from multi-year highs. Our 2Q and 2023 EPS estimates are now 12% and 30%, respectively, below the Street.

**Normalizing rates imply pressure on estimate outlook**

Product tanker rates have declined materially on a time-charter-equivalent (TCE) basis to \$31k/\$26k per day for LR2/MR vessels from \$53k/\$37k per day at STNG's 2QTD Update (with [1Q23 earnings \(see report\)](#)). The lower rates are driven by weaker Asia petrochem feedstock demand, a prolonged maintenance cycle, and a slower ramp in China. We lower our 2Q fleet avg TCE to \$32k/day from \$39k/day, below the Street's target for \$34k/day, as we expect rates to decline for the second quarter on a sequential basis. Our 2Q23 TCE estimate would be its first year-year decline (-16%) after six quarters of increases.

**Newbuild orders portends increasing vessel capacity**

Orderbook-to-fleet ratio, a leading capacity indicator, increased to 9% in July from 8% in 1Q23, its highest since 2019 and up from a record low of 5% in 4Q22, as newbuilding orders have picked up. While new orders may take until 2H25 for delivery and scrapping may offset some increased capacity, we believe record product tanker tightness has peaked given sensitivity in rates to demand shortfalls. We also expect incremental adds to the Russia-market serving (shadow) fleet may absorb demand for Western carriers.

**Cash generation still robust and capital strategy sound**

We maintain a balanced view on STNG's shares as rates ease yet see support from its near 30% 2023e free cash flow yield. We remain positive on Scorpio's move to reduce debt (repurchased \$325m in sale leasebacks, refinanced debt with a facility at 100+ bps discount), its move to dispose older assets (sold an MR (medium-range) tanker for \$33 mil, near its purchase price 10 years prior) and repurchase shares (it bought ~10% of shares in 2Q).

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	-4.17	11.42	7.55	3.10	1.55
GAAP EPS	(4.29)	11.49	7.51	3.10	1.55
EPS Change (YoY)	NM	NM	-33.9%	-58.9%	-50.0%
Consensus EPS (Bloomberg)			10.69	10.44	11.09
DPS	0.40	0.40	0.95	1.00	1.00
<b>Valuation (Dec)</b>					
P/E	NM	3.7x	5.7x	13.8x	27.6x
GAAP P/E	NM	3.7x	5.7x	13.8x	27.6x
Dividend Yield	0.9%	0.9%	2.2%	2.3%	2.3%
EV / EBITDA*	21.9x	3.1x	4.3x	6.7x	8.3x
Free Cash Flow Yield*	0.9%	30.3%	26.6%	15.6%	13.1%

\* For full definitions of *iQmethod*<sup>SM</sup> measures, see page 6.

21 July 2023

## Equity

**Key Changes**

(US\$)	Previous	Current
Inv. Opinion	C-1-7	C-2-7
Inv. Rating	BUY	NEUTRAL
Price Obj.	60.00	45.00

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**Stock Data**

Price	42.36 USD
Price Objective	45.00 USD
Date Established	21-Jul-2023
Investment Opinion	C-2-7
52-Week Range	36.38 USD - 64.20 USD
Mrkt Val (mn) / Shares Out (mn)	2,408 USD / 56.8
Average Daily Value (mn)	42.86 USD
BofA Ticker / Exchange	STNG / NYS
Bloomberg / Reuters	STNG US / STNG.N
ROE (2023E)	16.0%
Net Dbt to Eqty (Dec-2022A)	49.2%
ESGMeter™	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

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Timestamp: 21 July 2023 05:00AM EDT

# iQprofile<sup>SM</sup> Scorpio Tankers Inc.

## iQmethod<sup>SM</sup> – Bus Performance\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	-1.7%	17.5%	12.6%	6.9%	5.1%
Return on Equity	-11.7%	33.2%	16.0%	5.8%	2.8%
Operating Margin	-16.8%	54.5%	46.0%	30.7%	22.5%
Free Cash Flow	21	735	646	379	318

## iQmethod<sup>SM</sup> – Quality of Earnings\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	NM	1.1x	1.6x	2.7x	4.8x
Asset Replacement Ratio	0.2x	0.2x	0.1x	0.1x	0x
Tax Rate	NM	NM	NM	NM	NM
Net Debt-to-Equity Ratio	144.5%	49.2%	32.3%	34.0%	31.3%
Interest Cover	-0.6x	5.4x	3.6x	2.0x	1.5x

## Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	541	1,563	1,210	922	824
% Change	-41.0%	189.0%	-22.6%	-23.8%	-10.6%
Gross Profit	541	1,563	1,210	922	824
% Change	-41.0%	189.0%	-22.6%	-23.8%	-10.6%
EBITDA	150	1,058	763	492	394
% Change	-70.6%	607.8%	-27.9%	-35.6%	-19.9%
Net Interest & Other Income	(138)	(149)	(145)	(136)	(118)
<b>Net Income (Adjusted)</b>	<b>(228)</b>	<b>722</b>	<b>411</b>	<b>148</b>	<b>68</b>
<b>% Change</b>	<b>NM</b>	<b>NM</b>	<b>-43.0%</b>	<b>-64.1%</b>	<b>-54.1%</b>

## Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	(235)	726	409	148	68
Depreciation & Amortization	240	207	207	208	208
Change in Working Capital	14	(176)	28	0	0
Deferred Taxation Charge	0	0	0	0	4
Other Adjustments, Net	53	12	17	47	42
Capital Expenditure	(52)	(34)	(16)	(23)	(5)
<b>Free Cash Flow</b>	<b>21</b>	<b>735</b>	<b>646</b>	<b>379</b>	<b>318</b>
<b>% Change</b>	<b>-91.4%</b>	<b>NM</b>	<b>-12.1%</b>	<b>-41.2%</b>	<b>-16.3%</b>

## Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	230	377	509	339	15
Trade Receivables	38	277	234	234	234
Other Current Assets	17	34	18	18	18
Property, Plant & Equipment	3,842	3,089	2,898	2,689	2,481
Other Non-Current Assets	887	783	774	774	774
<b>Total Assets</b>	<b>5,014</b>	<b>4,559</b>	<b>4,432</b>	<b>4,054</b>	<b>3,522</b>
Short-Term Debt	235	32	69	69	69
Other Current Liabilities	293	442	439	439	439
Long-Term Debt	2,649	1,579	1,290	1,101	676
Other Non-Current Liabilities	NA	NA	NA	NA	NA
<b>Total Liabilities</b>	<b>3,177</b>	<b>2,052</b>	<b>1,799</b>	<b>1,610</b>	<b>1,185</b>
<b>Total Equity</b>	<b>1,837</b>	<b>2,507</b>	<b>2,633</b>	<b>2,444</b>	<b>2,337</b>
<b>Total Equity &amp; Liabilities</b>	<b>5,014</b>	<b>4,559</b>	<b>4,432</b>	<b>4,054</b>	<b>3,522</b>

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 6.

## Company Sector

Shipping

## Company Description

Scorpio Tankers (STNG) provides seaborne transport of refined petroleum products worldwide, such as gasoline, heating oil, and fuel oil. Product tankers move refined products from global refineries to points near consuming markets. STNG operates the world's largest, youngest, and most modern fleet of publicly traded product tankers consisting of 112 owned product tankers. STNG largely operates in the spot shipping markets.

## Investment Rationale

After its recent vessel sale and rate gains, STNG shares may see impacts from moderating market rates with slowing refined product demand. However with 112 product tanker vessels (post sale) generating robust cash flow, shares could also see support from its high FCF yield. It could stabilize within its 5x-9x EBITDA band as rate outlook moderates, offset by its moves to decrease leverage and improve returns. We thus maintain a balanced view on STNG shares with our Neutral rating.

## Stock Data

Average Daily Volume 1,011,781

## Quarterly Earnings Estimates

	2022	2023
Q1	-0.15A	3.31A
Q2	3.13A	2.33E
Q3	4.29A	1.19E
Q4	4.24A	0.51E

## Charter rate weakness can lead to outsized EPS downside

We target Scorpio Tanker's 2Q23 time-charter equivalent rates of \$37k/\$29k/\$26k per day for its LR2/MR/Handymax vessels (down 20%/17%/28% from our prior \$46k/\$35k/\$36k targets). Current market rates have eased to \$31k/\$26k/\$21k per day (per Clarksons Research), from \$53k/\$37k/\$37k per day in May, when Scorpio provided a market update, noting it had booked 39%/35%/34% of its 2Q23 days.

We now see spot LR2 rate levels converging near its charter-out (contractual) average rate of \$31k/day and below its recent charter-out agreement of \$40k/day. Given the high EPS sensitivity to TCE rates (\$1k/day could result in 3% +/- in quarterly EPS), our 2Q23 estimate is now 12% below the Street.

### Exhibit 1: 2Q23 EPS Sensitivity to Vessel Charter Rates

Earnings are highly sensitive to slight changes in vessel charter rates

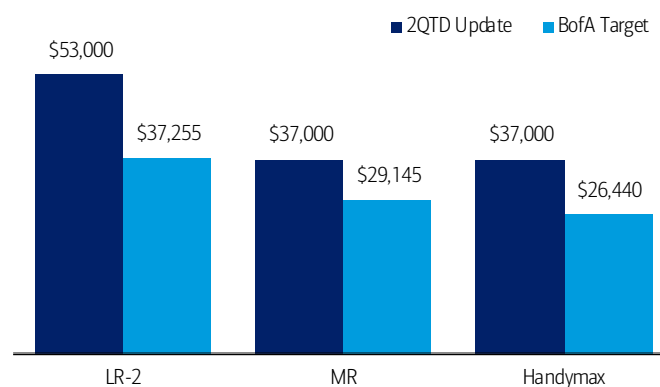
		LR-2 TCE Rates					
		-20%	-10%	BofAe	+10%	+20%	
		EPS	\$29,804	\$33,530	\$37,255	\$40,981	\$44,706
MR TCE Rates	-20%	\$23,316	-45.7%	-35.3%	-24.9%	-14.6%	-4.2%
	-10%	\$26,230	-33.2%	-22.8%	-12.5%	-2.1%	+8.3%
	BofAe	\$29,145	-20.7%	-10.4%	-	+10.4%	+20.7%
	+10%	\$32,059	-8.3%	+2.1%	+12.5%	+22.8%	+33.2%
	+20%	\$34,974	+4.2%	+14.6%	+24.9%	+35.3%	+45.7%

Source: BofA Global Research estimates

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### Exhibit 2: 2Q23 Time Charter Equivalent Rate Targets

Our 2Q23 rate targets assume a material intra-quarter deceleration



Source: BofA Global Research estimates and company reports.

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## Orderbook ratio moves above 9% in July

Vessel orderbook for product tankers with 10k+ deadweight ton capacity has risen to more than 9% of active fleet, up from 8% in 1Q23, and 5% (its historic quarterly low) in 4Q22. Although the ratio remains below the historical average of 20% and shipyard slots remain highly limited (earliest delivery 2H25), we view this as a leading indicator of a gradual increase in product tanker vessel capacity, especially as vessel scrapping has slightly trended below average given the more active secondhand market. We also could see a more active shadow fleet absorb non-G7 ton-miles from Western carriers.

### Exhibit 3: Product Tanker 10k+ Deadweight Ton Capacity Orderbook % of Fleet

Orderbook ratio has risen to 9% (from prior low of 5% in 4Q22) as ordering activity picks up



Source: BofA Global Research estimates and Clarksons

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## Demand outlook remains volatile

Incremental product tanker ton-mile demand also appears under increasing pressure, led by slowing industrial demand (PMI is below 50 for eight consecutive months) and a slower-than-expected ramp in China refined product demand, as its economic growth lags expectations. We also see any potential sanction relief on Russian seaborne product may also lead to lower rates given the normalization of trade routes.

## Harvesting elevated rate environment; Buying back shares

Scorpio Tankers announced the sale of a 2013-built MR product tanker (*STI Ville*) for \$32.5 million in July 2023, near its new-build purchase price 10 years ago. It has repurchased 5.4 million shares over 2Q23 (~10% of outstanding shares; along with 880k since quarter end). It also plans to further reduce its debt levels, while adding contractual (charter-out) exposure selectively. We view its moves as reflective of a more conservative spot rate view. It continues to work to reduce its breakeven charter rate, targeting \$15k/day (from \$17k/day), led by its lower debt costs. While we are positive on its strategy to scale down leverage, we believe near-term macroeconomic pressures and lower rate levels may continue to balance its improved financial structure. As such, we move to Neutral on STNG's shares.

## Price objective basis & risk

### Scorpio Tankers Inc. (STNG)

Our \$45 price objective is based on an 6.5x EV/EBITDA multiple on our 2024 EBITDA estimate. Our valuation multiple nears the middle of its 5x-9x historical trading range, as global mobility strengthens, pricing rebounds as inventories reach decade-lows, orderbook remains at historic-lows, and ton mile demand is rising. The negative impacts from COVID disruptions are fading (North America and Europe stronger, Asia stabilizing) though softening economic outlook may weaken demand for refined products. Our multiple is below the bottom end of its range as earnings are set to significantly compound.

Upside risks to our PO are volatile charter rates, better-than-expected spot product tanker rates in 2022-23, lower-than-expected vessel deliveries in 2022-24, a spike in global oil demand, and higher-than-expected levels of scrapping in the market.

Downside risks to our PO are drop off in mobility (return of lockdowns, war disruptions, which have shown to increase ton mile demand), liquidity risk given rolling debt through 2024 versus cash generation (which depends on day rates rising above the daily fixed cost base), a weaker-than-expected rate environment, overcapacity due to greater-than-expected vessel deliveries and lower-than-expected scrapping rates, and weaker global demand for refined products.

## Analyst Certification

I, Ken Hoexter, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

### US - Transportation Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Canadian National	CNI	CNI US	Ken Hoexter
	Canadian Pacific Kansas City Ltd	CP	CP US	Ken Hoexter
	CSX Corporation	CSX	CSX US	Ken Hoexter
	FedEx Corp.	FDX	FDX US	Ken Hoexter
	J.B. Hunt Transport Services	JBHT	JBHT US	Ken Hoexter
	Kirby Corp	KEX	KEX US	Ken Hoexter
	Knight-Swift Transportation Holdings Inc	KNX	KNX US	Ken Hoexter
	Norfolk Southern	NSC	NSC US	Ken Hoexter
	Old Dominion Freight Line	ODFL	ODFL US	Ken Hoexter
	RXO, Inc.	RXO	RXO US	Ken Hoexter
	Saia Inc.	SAIA	SAIA US	Ken Hoexter
	Schneider National	SNDR	SNDR US	Ken Hoexter
	Union Pacific	UNP	UNP US	Ken Hoexter
	Werner Enterprises	WERN	WERN US	Ken Hoexter
	XPO, Inc.	XPO	XPO US	Ken Hoexter
<b>NEUTRAL</b>				
	Scorpio Tankers Inc.	STNG	STNG US	Ken Hoexter
	Teekay Tankers Limited	TNK	TNK US	Ken Hoexter
	TFI International	TFII	TFII US	Ken Hoexter
	TFI International	YTFII	TFII CN	Ken Hoexter
	UPS	UPS	UPS US	Ken Hoexter
	Wabtec Corp.	WAB	WAB US	Ken Hoexter
<b>UNDERPERFORM</b>				
	ArcBest Corporation	ARCB	ARCB US	Ken Hoexter
	C.H. Robinson	CHRW	CHRW US	Ken Hoexter
	The Greenbrier Companies	GBX	GBX US	Ken Hoexter



## US - Transportation Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	TuSimple	TSP	TSP US	Ken Hoexter
	World Kinect	WKC	WKC US	Ken Hoexter
<b>RSTR</b>				
	Triton International, Ltd	TRTN	TRTN US	Ken Hoexter

**iQmethod<sup>SM</sup> Measures Definitions****Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

**Numerator**

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

**Denominator**

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

**Quality of Earnings**

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

**Numerator**

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash &amp; Equivalents

EBIT

**Denominator**

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

**Valuation Toolkit**

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

**Numerator**

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

**Denominator**

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

EV / EBITDA

Basic EBIT + Depreciation + Amortization

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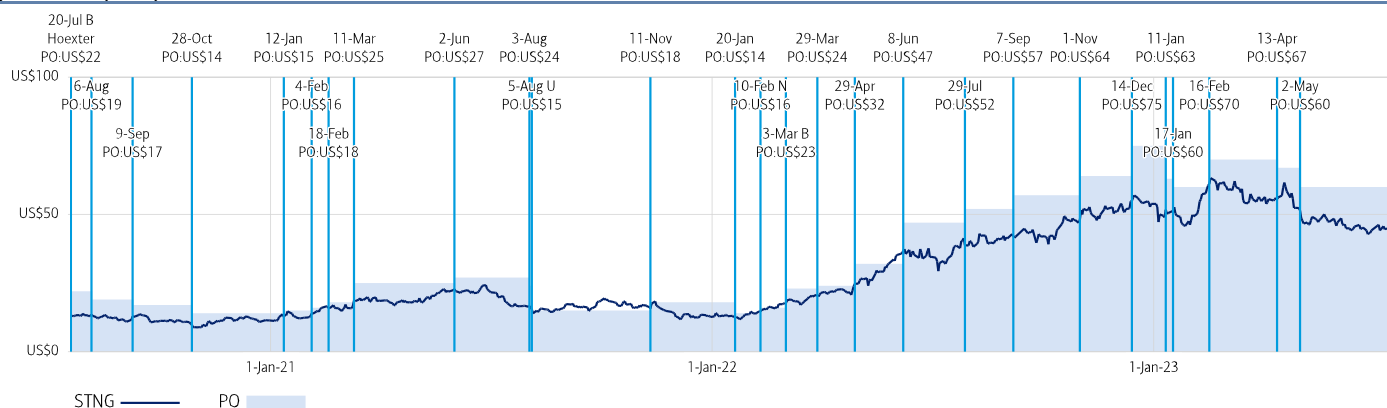
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### Scorpio Tankers (STNG) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

### Equity Investment Rating Distribution: Transport/Infrastructure Group (as of 30 Jun 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	72	52.94%	Buy	42	58.33%
Hold	29	21.32%	Hold	13	44.83%
Sell	35	25.74%	Sell	17	48.57%

### Equity Investment Rating Distribution: Global Group (as of 30 Jun 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1877	53.28%	Buy	1040	55.41%
Hold	815	23.13%	Hold	464	56.93%
Sell	831	23.59%	Sell	385	46.33%

<sup>R1</sup> Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster <sup>R2</sup>
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

<sup>R2</sup> Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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