Asia Credit Research

Earnings Review: Golden Agri-Resources Ltd ("GGR")

Issuer Profile: Neutral (5)

Ticker: **GGRSP**

Background

Golden Agri-Resources Ltd ("GGR") is a major palm oil company, managing 500,345 ha of palm oil plantations in Indonesia. The company's integrated operations include oil palm cultivation, crude palm oil ("CPO") and palm kernel processing and downstream refining to produce consumer products such as cooking oil, margarine and shortening. The company is ~50.4%-owned by the Widjaja family and is listed on the SGX.

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Recommendation

- We are not overly concerned over the headline fall in revenue from GGR's core palm oil-related businesses given that this is driven by CPO price and volume declines which had affected the sector broadly. We are lowering our Overweight call on the GGRSP'21s to Neutral, in view of increased investments in financial assets which is a competing cash outflow to capital expenditure needs at GGR (eg: replanting and integration of downstream business). Given GGR's still manageable credit metrics, we are maintaining our Neutral (5) issuer profile on the company.
- Notwithstanding Olam International Ltd ("OLAM")'s stronger access to debt markets, a switch into the GGRSP 4.75% '21 from the OLAMSP 5.80% '19 allows a spread pick up of 190bps which more than compensates for the 1.5 years longer time to maturity. We also hold OLAMSP at Neutral (5) Issuer Profile.

Relative Value:

Bond	Maturity/Call date	Net gearing (%)	Ask Yield	Spread
GGRSP 4.75% '21	25/01/2021	72.9	5.27%	310bps
OLAMSP 5.80% '19	17/07/2019	149.3	3.05%	116bps

Indicative prices as at 18 May 2018 Source: Bloomberg
Net gearing based on latest available quarter

Key Considerations

- **Lower palm oil price and volume:** Revenue declined 11.3% y/y to USD1.8bn driven by declines in the Plantations and Palm Oil Mills, Palm and Laurics and the Oilseeds segments while reported EBITDA was down 33.7% y/y to USD121.1mn. The overall weaker results were driven by a 12% decline in palm product output as well as a 12% decline in CPO FOB prices (USD645 /MT in 1Q2018 versus USD734/MT in 1Q2017). In our view, the fall in prices and production volume is not idiosyncratic to GGR and we had observed large y/y EBITDA declines among palm oil producers focused on Indonesia for 1Q2018. With the decline in earnings, interest coverage as measured by reported EBITDA/Interest declined to 3.3x versus 5.2x in 1Q2017 (4Q2017: 4.3x). In FY2017, GGR took USD45.6mn in impairment losses on the back of its Tianjin oilseeds business (since sold to Louis Dreyfus in April 2018) and from its China noodles business. These were one-off items and no impairment losses were taken in 1Q2018. GGR ended the quarter with a profit attributable to owners of the company at USD11.9mn (1Q2017: USD37.6mn).

- **Unadjusted net gearing steady:** As at 31 March 2018, unadjusted net gearing was 0.73x, slightly higher from the median of 0.70x saw in FY2017, though in April 2018, GGR had paid down SGD200mn (~USD150mn) of bonds and with the completion of the sale of the business to Louis Dreyfus post-1Q2018, we expect the company to have received USD111mn in cash proceeds. On a proforma basis, we estimate net gearing to have fallen slightly back to ~0.7x.

- **Off-balance sheet items and post-employment benefit liabilities have increased:** In end-2017, corporate guarantees provided on borrowings of joint ventures (an off-balance sheet item) ballooned to USD433.0mn (from USD268.1mn in end-2016) while non-cancellable operating leases increased to USD24.8mn (up from USD22.3mn in end-2016). Estimated post-employment benefit liabilities, which we consider as debt-like, also increased to USD99.8mn (from USD80.6mn in end-2016). Assuming that these three items have stayed at similar levels as at 31 March 2018 and adding them into net debt, we find adjusted net gearing at 0.87x.

- **Short term debt coming due:** Having repaid the SGD bond, we estimate that

GGR has USD1.58bn in short term debt due until end-March 2019. A large portion of these relate to working capital requirements at GGR and is typically rolled forward. We have observed liquid working capital at GGR ranging from ~USD900mn to USD1.2bn and assuming that USD1.0bn relates to working capital, this leaves ~USD580mn that would still need to be refinanced against cash balance of USD67mn. Of these, MYR500mn (~USD126mn) relates to a MYR bond due in August 2018 and our base case assumes that GGR would seek out refinancing from the MYR bond market. The remaining are largely made up of USD bank debt taken at GGR's Indonesian operating companies due in July 2018 and February 2019 respectively. Adjusted tangible assets (we exclude intangible assets, bearer plants and long term investments) was USD6.3bn at GGR as at 31 March 2018, against total debt of USD3.1bn, which should help GGR in gaining access to debt markets for refinancing of existing debt.

- **Investments into technology fund is a competing cash outflow:** During the quarter, GGR's cash flow from operations (before interest and tax) was SGD26.0mn (1Q2017: SGD197.1mn), lower due to the lower earnings during the quarter as well as higher working capital needs. For example, a USD112.3mn increase in Deposits and Advances to Suppliers was noted. In 1Q2018, GGR's total cash outflow for investments was USD138.4mn, of which USD101.4mn went towards investment in financial assets (~USD80mn relates to investments in a technology fund which GGR had first subscribed to in December 2016). Notwithstanding that certain investees could be synergistic to GGR's business down the road; we think GGR's day-to-day management team has little control over end investments made by the fund as the fund is likely to be separately managed. Net-net, we do not expect these investments to be cash flow generative in the near term. The cash gap at GGR during the quarter was funded via borrowings, with net borrowings of USD124mn. Separate to the technology fund, USD220mn is projected to be spent in 2018 for capital expenditure into the upstream and downstream business and we estimate that only USD44.5mn has been spent in 1Q2018 and remains to be funded.

- **Sale of property interest:** In September 2017, GGR's wholly-owned subsidiary PT Purimas Sasmita ("PTPS") entered into binding agreements with PT Duta Cakra Pesona ("Cakra") for PTPS to transfer its rights and obligations on 23 floors of an office building in South Jakarta ("MSIG Tower") to Cakra for ~USD107.5mn in net cash consideration. Cakra is wholly-owned by PT Bumi Serpong Damai Tbk whom GGR share the same controlling shareholders with. We understand from company that the deal has completed and as at 31 March 2018, remaining receivables from Cakra were ~USD33mn, which should be received by end-2018.

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Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight ("OW") – The performance of the issuer's specific bond is expected to outperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral ("N") – The performance of the issuer's specific bond is expected to perform in line with the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight ("UW") – The performance of the issuer's specific bond is expected to underperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

Analyst Declaration
The analyst(s) who wrote this report and/or her or his respective connected persons did not hold securities in the above-mentioned issuer or company as at the time of the publication of this report.

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