Asian Credit Daily

Aug 2, 2018

Credit Headlines: BreadTalk Group Ltd, BNP Paribas SA, DBS Group Holdings Ltd

Market Commentary

- The SGD swap curve steepened yesterday, with swap rates for the shorter tenors trading around 1bps higher while the longer tenors traded 2-4bps higher.
- Flows in SGD corporates were moderate yesterday, with better buying seen in UOBSP 4.75% PERPc19.
- The Bloomberg Barclays Asia USD IG Bond Index average OAS was unchanged at 138bps while the Bloomberg Barclays Asia USD HY Bond Index average OAS widened 2bps to 466bps.
- 10Y UST yields rose 5bps to close at 3.0%, the first time in nearly two months after strong jobs data in the US above estimates and the announcement that the US government intends to increase its borrowing from the bond market in the next quarter which will cause a supply pressure.

Credit Headlines:

BreadTalk Group Ltd ("BGL") | Issuer Profile: Neutral (5)

- BGL reported 2Q2018 results. Revenue is flattish (+0.8% y/y to SGD148.8mn) with mixed results from the various divisions. Bakery continued its poor performance with 2Q2018 revenue declining 5.2% y/y to SGD68.8mn, largely due to lower revenue from direct operated stores (with 13.5% y/y fall in the number of direct operated stores) and franchise revenue from China. However, Food Atrium (+4.0% y/y to SGD38.8mn) and Restaurant (+7.1% y/y to SGD37.3mn) performed well, with the former reporting strong same store growth and the latter adding 3 more outlets in Singapore (1) and Thailand (2).
- Reported EBITDA fell 1.9% y/y to SGD18.1mn, dragged mainly by a significant 40.0% y/y fall in Bakery, which we think is due to the high operating leverage. Restaurant also performed poorer (-2.2% y/y to SGD7.1mn) which we think is due to the expenses incurred by the newly opened restaurants. Food Atrium has become the highest reported EBITDA contributor (+44.3% y/y to SGD7.7mn). Despite weaker reported EBITDA, net profit increased 7.7% y/y to SGD4.4mn, largely due to 11.5% y/y decline in depreciation to SGD9.3mn.
- Liquidity looks ample for BREAD, with SGD206.6mn of cash which is sufficient to repay SGD75mn BREAD 4.6% '19s and SGD 35.4mn of short-term loans. Operating cashflows before working capital remains strong still at SGD20.9mn in 2Q2018, increasing 10.8% y/y though cash generated from operations is lower at SGD14.4mn due to working capital requirements which may be due to the numerous recent JVs entered. However, we think that the cash pile may continually be drawn down, as we think there will be increases in capital and operating expenditures to turn around the decline in revenue. As a recap, BGL has also committed to deploying significant capital (~SGD80mn) to subscribe for a 5%-stake in a Perennial-led China JV for property development in China.
- Reported net gearing inched up slightly though still looks manageable at 0.29x (1Q2018: 0.27x). We estimate that net debt/EBITDA remains healthy at ~0.7x, though this has increased from 1Q2018's reported net debt/EBITDA of 0.28x. As we expect BREAD's credit metrics to weaken as it consumes its cash balance for growth, we continue to hold BREAD at a Neutral (5) Issuer Profile. (Company, OCBC)

Credit Headlines (cont'd):

BNP Paribas SA ("BNPP") | Issuer Profile: Neutral (3)

- BNPP reported 2Q2018 and 1H2018 results with 2Q2018 total revenues up 2.5% y/y (+1.0% y/y for the operating divisions which includes Domestic Markets ("DM"), International Financial Services ("IFS") and Corporate & Institutional Banking ("CIB")) due to strong performance in IFS (+8.7% y/y) which mitigated marginally weaker y/y performance in DM (-0.3% from on-going low interest rates which was partially offset by loan growth) and CIB (-6.8%) from unfavourable FX movements, weaker FICC activity and absence of capital gains from 2Q2017.
- As such, IFS (comprises retail banking outside of Eurozone, Personal Finance, Insurance and Wealth and Asset Management activities) is now the highest contributor to operating division revenue at 38.2% while DM contribution was relatively stable at 35.2% and CIB contribution fell to 26.6% in 2Q2018.
- Operating expenses for 2Q2018 rose faster than revenues (+4.2% y/y: +2.8% y/y for operating divisions) due to business growth in DM (in particular specialized businesses (leasing businesses) while operating expenses in retail networks fell 0.5% y/y) and IFS and as a result, gross operating income was slightly lower (-0.7% y/y; -1.7% y/y for operating divisions). Operating expenses fell in CIB (-0.9% y/y), so while overall expenses increased, we think growth trends in expenses are supportive of future profitability. 2Q2018 operating expenses also include exceptional and acquisitions' restructuring costs of EUR275mn, up from EUR168mn in 2Q2017 .
- Cost of risk has resumed its positive trend after a y/y rise in cost of risk in 1Q2018, down 14.4% y/y in 2Q2018 (-2.5% y/y for operating divisions) due to improved performance of BNPP's Italian portfolio and the low interest rate environment, and this resulted in operating income (before non-operating items) improving 2.1% y/y for 2Q2018 to EUR3.3bn (-1.6% y/y for operating divisions).
- As mentioned above, business activity appears sound with broad based loans growth across DM (+5.2% y/y), Personal Finance loans within IFS (+12.0% y/y) and Corporate Banking within CIB (+4.6%). Loan quality appears to be improving with reported doubtful loans down h/h by 2.8% and the reported ratio of doubtful loans to gross outstanding loans falling marginally to 2.9% as at 30 June 2018 from 3.0% as at 1 January 2018. The coverage ratio as at 30 June 2018 was relatively stable at 79.4%.
- BNPP's fully loaded CET1 ratio at 11.5% as at 30 June 2018 was slightly weaker q/q (11.6% as at 31 March 2018) due to a 15bps impact from dividends as well as a 15bp increase in risk weighted assets from credit and operational risk. Nevertheless, BNPP's capital ratios remain well above minimum transitional CET1 requirements of 9.125% for 2018 as disclosed in BNPP's 2017 annual report. Although future minimum regulatory requirements will rise, BNPP's capital ratios are expected to remain satisfactory given plans to issue around EUR10bn of senior non-preferred debt until January 2019.
- We see underlying fundamentals for BNPP remaining sound from on-going business growth and BNPP's scale and business diversity (Company, OCBC)

Credit Headlines (cont'd):

DBS Group Holdings Ltd ("DBS") | Issuer Profile: Positive (2)

- DBS has announced solid 2Q2018 and 1H2018 results. 2Q2018 total income is up 10% y/y to SGD3.2bn due to strong performance in net interest income (+18% y/y due to 9bps y/y improvement in net interest margin to 1.85% and 12% y/y growth in customer loans) and net fee and commission income (+11% y/y due to Cards and Wealth Management performance). Other non-interest income was down 32% y/y due to falls in net trading income and net income from investment securities.
- Expenses rose 12% y/y due to consolidation of ANZ's Private Banking business; excluding this one-off adjustment, underlying expenses rose 5% y/y. Expenses increased across the board, most notably on % terms in revenue-related expenses indicating expenses growth is supporting DBS's solid total income performance. The cost to income ratio deteriorated mildly to 44.3% in 2Q2018 against 43.4% in 2Q2017.
- Allowances for credit and other losses fell 65% y/y in recognition of an improved operating environment and the challenging environment in the past which saw a pro-active recognition of problem loans and as a result profit before tax rose 24% y/y to a record SGD1.7bn.
- By segment, total income from Consumer Banking/Wealth Management rose 22.7% y/y on higher loan and deposit volumes and an improved net interest margin while Institutional Banking total income rose 9.5% y/y as lower income from loan-related activities was mitigated by higher income from cash management, trade finance and investment banking activities. Total income from Treasury Markets fell 58.5% y/y from broad based softness in its businesses.
- Business volumes remain robust with 12% y/y and 3% q/q loan growth. As expected given the buoyant property sector, building and construction loans and housing loans (42.1% of total loans as at 30 June 2018) rose the most y/y growing 16.3% and 14.1% y/y.
- Non-performing loans rose 19.2% y/y and as such the non-performing loan ratio deteriorated mildly y/y to 1.6% as at 30 June 2018 (1.5% as at 30 June 2017) however as mentioned above, this was due to the pro-active recognition of problem loans in FY2017. Compared to 1Q2018 and 4Q2017, the non-performing loan ratio actually improved marginally.
- Given the strong rise in loans, y/y growth in risk weighted assets was higher than movement in CET1 and Tier 1 capital. These were lower y/y and impacted by SGD2.8bn in dividends paid (including a SGD1.3bn special dividend) and maturity of Tier 1 instruments. Total capital however rose y/y due to issuance of a USD750mn Tier 2 note in June. As such CET1 and Tier 1 capital ratios fell marginally y/y and q/q but at 13.6%, the CET1 ratio remains well above the CET1 regulatory minimum requirement of 8.7%.
- In our view, DBS remains well poised to benefit from improved conditions for financial institutions through rising short term interest rates and a solid market position in retail banking. Its fundamentals and issuer profile at Positive (2) remain very much intact. (Company OCBC)

Table 1: Key Financial Indicators

	2-Aug	1W chg (bps)	1M chg (bps)
iTraxx Asiax IG	81	1	-14
iTraxx SovX APAC	11	-2	-4
iTraxx Japan	55	0	-7
iTraxx Australia	75	1	-7
CDX NA IG	59	-1	-9
CDX NA HY	107	0	1
iTraxx Eur Main	62	-1	-14
iTraxx Eur XO	287	2	-41
iTraxx Eur Snr Fin	75	-1	-17
iTraxx Sovx WE	24	0	-1
AUD/USD	0.740	0.34%	0.84%
EUR/USD	1.166	0.16%	0.20%
USD/SGD	1.362	0.10%	0.51%
China 5Y CDS	60	0	-12
Malaysia 5Y CDS	85	0	-27
Indonesia 5Y CDS	115	6	-27
Thailand 5Y CDS	43	0	-7

	2-Aug	1W chg	1M chg
Brent Crude Spot ($/bbl)	72.44	-2.82%	-6.29%
Gold Spot ($/oz)	1,217.59	-0.42%	-1.97%
CRB	191.64	-1.55%	-2.97%
GSCI	457.52	-1.67%	-4.60%
VIX	13.15	7.00%	-15.71%
CT10 (bp)	3.001%	2.44	12.97
USD Swap Spread 10Y (bp)	7	2	-1
USD Swap Spread 30Y (bp)	-5	3	1
TED Spread (bp)	33	-1	-9
US Libor-OIS Spread (bp)	33	-1	-7
Euro Libor-OIS Spread (bp)	4	0	0
DJIA	25,334	-0.32%	4.22%
SPX	2,813	-1.15%	3.18%
MSCI Asiax	674	-0.62%	0.92%
HSI	28,341	-2.01%	-2.12%
STI	3,329	0.06%	2.78%
KLCI	1,788	1.39%	6.13%
JCI	6,033	1.68%	4.99%

New issues

- Power Finance Corp Ltd has hired banks for its potential 10-year USD bond issuance.

Date	Issuer	Size	Tenor	Pricing
31-Jul-18	Lotte Property & Development Co Ltd	USD200mn	3-year	3mL+92.5bps
31-Jul-18	KWG Group Holdings Limited	USD350mn	3NC2	7.875%
31-Jul-18	China Mengniu Dairy Co Ltd	USD500mn	5-year	CT5+148bps
30-Jul-18	CMHI Finance BVI Co Ltd	USD900mn	5-year	CT5+162.5bps
30-Jul-18	CMHI Finance BVI Co Ltd	USD600mn	10-year	CT10+215bps
30-Jul-18	Woori Bank	USD300mn	10-year	CT10+220bps
27-Jul-18	Legend Fortune Ltd	USD300mn	3-year	3mL+128bps
26-Jul-18	Trade Horizon Global Ltd (JUDA)	USD400mn	3-year	3mL+257.5bps
26-Jul-18	China Aoyuan Property Group Ltd (re-tap)	USD175mn	CAPG 6.35%’20s	98.516
26-Jul-18	Industrial Bank of Korea	USD500mn	3-year	3mL+60bps
25-Jul-18	Greenland Global Investment Ltd (re-tap)	USD300mn	GRNLGR’21s	3mL+485bps
25-Jul-18	Temasek Financial I Ltd	USD1.35bn	10-year	CT10+72bps
25-Jul-18	Posco	USD500mn	5-year	CT5+130bps
25-Jul-18	Export-Import Bank of China	USD140mn	3-year	3mL+60bps
24-Jul-18	CFLD Cayman Investment Ltd	USD200mn	3-year	9.0%
24-Jul-18	Sino-Ocean Land Treasure IV Ltd	USD700mn	3-year	3mL+230bps
24-Jul-18	Sunac China Holdings Ltd	USD400mn	2-year	8.625%

Source: OCBC, Bloomberg

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