Asian Credit Daily

OCBC Bank

May 7, 2018

Credit Headlines: HSBC Holdings PLC, Westpac Banking Corporation, Chip Eng Seng Corp Ltd, BNP Paribas SA, ASL Marine Holdings Ltd, Société Générale

Market Commentary

- The SGD swap curve flattened last Friday, with swap rates for the lower tenors trading 1-2bps lower while the longer tenors traded 3-4bps lower.
- Flows in SGD corporates were heavy last Friday.
- The Bloomberg Barclays Asia USD IG Bond Index average OAS widened 1bps to 1.33% while the Bloomberg Barclays Asia USD HY Bond Index average OAS widened 12bps to 407bps.
- 10Y UST yield fell 4bps to multiweek low of 2.91% intraday due to weaker-than-expected nonfarm payroll data. 10Y UST yield subsequently rose back to close with minimal change at 2.95% as investors concluded that the weaker-than–expected jobs report will not deter the Fed from raising interest rates at its current intended trajectory.

Credit Headlines

HSBC Holdings PLC (“HSBC”) | Issuer Profile: Positive (2)

- HSBC’s 1Q2018 reported profit before tax fell 4% y/y to USD4.8bn as 6% y/y growth in reported revenue and lower reported impairment costs were mitigated by a 13% rise in operating expenses due to business investment and enhancing digital capabilities. Elevated expenses are likely to continue as the bank continues to push into technology and the operating environment for HSBC remains supportive. Results also reflected USD897mn in provisions in relation to the Department of Justice investigations into prior year RMBS activities. Adjusting for the provisions and other significant items, adjusted profit before tax of USD6.0bn was still down 3% y/y.
- Revenue growth was driven by deposits and UK mortgage lending volume growth in Retail Banking & Wealth Management (‘RBWM’) as well as higher deposit margins. Within Commercial Banking, lending growth in Hong Kong and the UK supported Global Liquidity & Wealth Management performance. Global Banking and Markets performance was flat y/y as lower client activity in fixed income was mitigated by transaction banking and equities revenues. Overall, net interest margins improved q/q and y/y, up by 3bps and 4bps respectively due to a larger rise in gross yields (especially in Hong Kong) compared to the increase in the cost of funds.
- Supporting the higher business investment, HSBC’s balance sheet grew in 1Q2018 with net loans and advances to customers up 2% q/q. As mentioned previously, growth came from UK mortgage lending as well as commercial lending in Hong Kong and the UK. This likely helped segment performance by geography with reported profit before tax in Europe and Asia improving noticeably y/y. Middle East and North Africa and Latin America also improved y/y but their contribution to overall reported profit before tax is relatively small. North America generated a loss before tax of USD596mn, which was due to the higher provisions for investigations into RMBS.
- Given earnings and balance sheet growth as well as a transitional impact from implementation of IFRS9, HSBC’s CET1 capital ratio and leverage ratio remained stable q/q at 14.5% and 5.6% respectively. Risk weighted assets growth of 2.6% was marginally ahead of loans growth due to foreign currency translation differences, asset growth and changes in asset quality. Notwithstanding the stable q/q CET1 ratios, HSBC announced an up to USD 2bn share buyback as well as its intention to call USD6bn in AT1 capital instruments. Management has guided that given potential growth opportunities, there will be no more share buy-backs expected in 2018. (OCBC, Company)

Credit Headlines (cont'd):

Westpac Banking Corporation ("Westpac") | Issuer Profile: Positive (2)

- Westpac's 1HFY2018 results for the 6 months ended 31 March appear on trend with domestic peers as a benign operating environment translated into broad based growth across business segments.
- Net operating income rose 4% y/y due to 9% y/y growth in net interest income from loans growth and the reported net interest margin improving 11bps to 2.16%. This was balanced by a 9%y/y fall in non-interest income from lower net trading income and economic hedges impact on New Zealand earnings.
- Expenses rose 2% y/y due to higher salary and technology expenses as well as an increase in regulatory and compliance costs. Of interest is that the cost increases already factor in costs associated with the ongoing Royal Commission into misconduct in the Banking industry. That said, given the lower growth in expenses (versus income), net profit before impairment charges rose 5% y/y to AUD6.4bn.
- Impairment charges fell 20% y/y, primarily in individual provisions, as portfolio quality appears sound according to management. Westpac's reported stressed exposures as a percentage of total committed exposures was 1.09% as at 31 March 2018, down 5bps from 31 March 2017. In kind, the ratio of gross impaired asset provisions to gross impaired assets fell to 45.5% as at 31 March 2018 from 52.1% as at 31 March 2017. This trend should be watched considering the mortgages 90+ day delinquencies ratio rose marginally, albeit from a low base.
- Given solid earnings, capital ratios improved 50bps y/y to 10.5% as at 31 March 2018, in line with the Australian Prudential Regulation Authority (APRA)'s minimum CET1 requirement by Jan 1, 2020 for 'unquestionably strong' capital ratios. This remains above the bank's minimum CET1 requirement of at least 8.0%. Improvement was driven by higher growth in CET1 capital (+8%) y/y against growth in risk weighted assets (+3% y/y). H/h trends were different with CET1 ratios marginally lower as 102bps improvement in cash earnings was offset by the impacts of final dividend payment (-70bps), regulatory model changes (-22bps) and RWA growth (-8bps). (OCBC, Company)

Chip Eng Seng Corp Ltd ("CES") | Issuer Profile: Negative (6)

- CES reported 1Q2018 results. Revenue increased 22.3% y/y to SGD204.3mn, largely driven by stronger contribution from property developments (+52.3% y/y to SGD137.2mn) due to higher progressive recognition from High Park Residences, Grandeur Park Residences and Williamsons Estate. Hospitality (+147.4% y/y to SGD18.1mn) also did well with contribution from Grand Park Kodhipparu Resort (which opened in 2017), 2 hotels which were acquired in 2H2017 (The Sebel Mandurah and Mercure & Ibis Styles Grosvenor Hotel) and improved occupancy at Park Hotel Alexandra. The underperformer was the construction segment, with revenue declining 29.4% y/y to SGD47.1mn as the newer projects were not sufficient to replenish segment revenue. Despite higher revenues, net profit fell 13.1% y/y to SGD11.6mn as administrative expenses increased 42.6% y/y to SGD22.3mn, primarily due to higher depreciation (+249% y/y to SGD4.4mn) and FX loss (1Q2018: SGD4.1mn loss, 1Q2017: SGD1.5mn gain).
- Net gearing inched up q/q to 1.57x (4Q2017: 1.54x), mainly due to AUD43mn (SGD43.8mn) acquisition of Mercure & Ibis Styles Grosvenor Hotel in Adelaide and commercial properties at Hindley Street in Adelaide. Going forward, net gearing may continue increasing as CES looks to replenish its land bank.
- CES will launch Colonial Park in 3Q2018 (formerly Woodleigh Lane) and complete the enbloc acquisition of Changi Garden in June 2018. In our view, strong execution of the upcoming sales launches will be crucial to support CES's credit profile. Meanwhile, CES has topped up its construction order book to SGD524.6mn (4Q2017: SGD403.6mn) with the award of a SGD168mn contract in 1Q2018.

Credit Headlines (cont'd):

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

- BNPP's 1Q2018 results continue to reflect somewhat challenging operating conditions for French banks with revenues down 4.4% y/y due to unfavorable foreign exchange movements as well as weak markets performance, particularly in fixed income, currencies and commodities. In addition, operating expenses rose 1.7% y/y due to the booking of full year anticipated tax increases from application of IFRIC 21 and this translated to gross operating income down 20.1% y/y as well as EUR211mn from exceptional business transformation and acquisition restructuring costs. Excluding the impact of IFRIC 21, costs were broadly stable.
- In a change of prior period trends, BNPP's cost of risk rose 3.9% and this translated to operating income down 25.6% y/y. This was offset by EUR171mn in other non-operating items from sale of a building which moderated the y/y fall in pre-tax income to 18.1% or EUR2.2bn.
- Q/q trends are more positive with revenues up 2.5% and cost of risk down 37.6%. This however was offset by an 8.4% rise in operating expenses which resulted in broadly stable operating income of EUR1.9bn q/q. However due to the aforementioned EUR171mn in other non-operating items, pre-tax income was up 6.3% q/q.
- Segment wise, International Financial Services continues to mitigate somewhat the weaker performance in Domestic Markets and Corporate and Institutional Banking ('CIB') with better relative performance at the operating income level. However, cost of risk in International Financial Services rose noticeably y/y and marginally q/q. Together though with share of earnings from equity method entities, pre-tax income from International Financial Services was up 4.8% y/y while Domestic Markets and CIB were down 6.5% and 28.2% respectively y/y.
- BNPP's CET1 ratio at 11.6% as at 31 March 2018 was slightly weaker q/q (11.9% as at 31 December 2017) due to the impact of full implementation of IFRS9. Excluding this impact, CET1 ratios would have been stable as quarterly earnings and a fall in risk weighted assets from foreign exchange impacts were offset by dividend payments. Absent foreign exchange effects, risk weighted assets rose q/q. BNPP's Tier1 and Total Capital ratios were also weaker marginally q/q (13.0%/17.7% as at 31 March 2018 against 13.2%/14.8% as at 31 Dec 2017 respectively). Nevertheless, BNPP's capital ratios remain well above minimum transitional requirements of 9.125%/10.625%/12.625% for 2018 as disclosed in BNPP's 2017 annual report. (Company, OCBC)

ASL Marine Holdings Ltd ("ASL") | Issuer Profile: Negative (6)

- ASL has provided a profit guidance for 3QFY2018 (ending March 2018), indicating that the company expects to report a net loss for the quarter. ASL has attributed the expected loss to weak contribution from the shipbuilding segment.
- Results will be released on 15/05/18. We will monitor its performance closely, particularly its EBITDA-to-Interest covenant (required to be at least 2.0x on a trailing 12 month basis). (Company, OCBC)

Credit Headlines (cont'd):

Société Générale ("SG") | Issuer Profile: Neutral (4)

- SG reported 1Q2018 results last Friday with gross operating income down 14.5% y/y. Driving the weaker performance was a 2.8% y/y fall in net banking income from lower French Retail Banking and markets performance and a 1.8% y/y rise in operating expenses from higher transformation and regulatory costs. Underlying performance (which is adjusted for non-economic and exceptional items and impact of IFRIC 21) was slightly better with a 8.7% fall in underlying gross operating income.
- By segment, French Retail Banking performance continues to be weak due to low interest rates as well as lower renegotiation and prepayment volumes y/y in 1Q2018, while Global Banking & Investor Solutions performance was also lower y/y due to a weaker dollar, weaker trading performance and comparing to a relatively strong 1Q2017. Conversely (and similar to BNP Paribas S.A.'s 1Q2018 results), International Retail Banking & Financial Services performance was improved y/y due to better performance in SG's overseas markets compared to France and improved insurance performance. On the expense front, French Retail Banking continues to be weighed down by transformation costs while cost inflation at International Retail Banking & Financial Services was due to business growth.
- SG's cost of risk continues to fall y/y in line with improved operating environments both domestically and abroad as well as a write-back in provisions in the Global Banking & Investor Solutions segment. In line with the trend in risk costs, the reported gross doubtful outstandings ratio was lower at 4.2% as at 31 March 2018 against 4.4% as at 31 December 2017. Despite the fall in risk costs, the reported gross coverage ratio for doubtful outstandings was slightly improved at 55% as at 31 March 2018 against 54% as at 31 December 2017.
- SG's balance sheet was stable q/q but contained a 1.5% fall in net customer loan outstandings (excluding assets and securities sold under repurchase agreements). That said, risk weighted assets rose 1% q/q and this, along with implementation of IFRS9 (-14bps) and inclusion of Single Resolution Fund guarantees (-8bps) translated to a q/q fall in CET1 ratios to 11.2% as at 31 March 2018 (11.4% as at 31 December 2017). This still remains above SG's minimum phased in CET1 ratio requirement of 8.63% as disclosed in SG's annual report. Including senior non-preferred debt issues and other TLAC adjustments, SG's reported TLAC ratio was 21.8% as at 31 March 2018, up from 21.4% as at 31 December 2017 and above the Financial Stability Board's 2019 minimum requirement.
- Earnings challenges appear to be mitigated by solid capital ratios insulating the credit profile for now. That said, earnings could remain under pressure from ongoing litigation and recent management changes which could lead to additional restructuring activities in addition to execution of SG's 2020 Strategic and Financial Plan. (Company, OCBC)

Table 1: Key Financial Indicators

	7-May	1W chg (bps)	1M chg (bps)
iTraxx Asiax IG	75	1	-2
iTraxx SovX APAC	13	1	-1
iTraxx Japan	51	0	-3
iTraxx Australia	66	1	-3
CDX NA IG	62	2	-4
CDX NA HY	107	0	1
iTraxx Eur Main	56	2	-2
iTraxx Eur XO	274	3	-11
iTraxx Eur Snr Fin	60	4	-3
iTraxx Sovx WE	17	0	-1
AUD/USD	0.753	-0.07%	-2.23%
EUR/USD	1.196	-1.00%	-2.95%
USD/SGD	1.334	-0.60%	-1.66%
China 5Y CDS	59	1	-4
Malaysia 5Y CDS	77	5	5
Indonesia 5Y CDS	116	10	15
Thailand 5Y CDS	45	1	0

	7-May	1W chg	1M chg
Brent Crude Spot ($/bbl)	75.00	-0.23%	11.76%
Gold Spot ($/oz)	1,314.41	-0.07%	-1.64%
CRB	203.25	0.93%	5.72%
GSCI	479.46	1.33%	8.05%
VIX	14.77	-4.15%	-31.27%
CT10 (bp)	2.950%	-0.71	14.70
USD Swap Spread 10Y (bp)	3	0	1
USD Swap Spread 30Y (bp)	-11	-1	5
TED Spread (bp)	54	-1	-9
US Libor-OIS Spread (bp)	52	-1	-7
Euro Libor-OIS Spread (bp)	3	0	0
DJIA	24,263	-0.20%	1.38%
SPX	2,663	-0.24%	2.26%
MSCI Asiax	706	-2.06%	-0.60%
HSI	29,927	-0.27%	0.27%
STI	3,545	-0.69%	2.99%
KLCI	1,842	-0.56%	0.26%
JCI	5,792	-1.98%	-6.20%

Source: OCBC, Bloomberg

New issues

- China Huadian Overseas Development 2018 Ltd has scheduled for investor meetings from 7 May for its potential USD bond issuance (guaranteed by China Huadian Corp).
- Guangzhou Finance Holdings Group Co Ltd scheduled for investor meetings from 7 May for its potential USD bond issuance.
- Excel Capital Global Ltd has scheduled for investor meetings from 7 May for its potential USD perpetual bond issuance (guaranteed by Minmetals Land Ltd, keepwell provider: China Minmetals Corp).
- BlueScope Steel has scheduled for investor meetings from 8 May for its potential USD bond issuance. Guorui Properties Ltd is said to have hire banks for its potential USD bond issuance.
- China Great Wall Asset Management Co Ltd is said to hire banks for its potential USD bond issuance.
- Korean Air Lines Co Ltd is said to hire banks for its potential USD hybrid bond issuance.

Date	Issuer	Size	Tenor	Pricing
3-May-18	Suntec REIT MTN Pte Ltd	SGD100mn	5-year	3.4%
3-May-18	Yuzhou Properties Co Ltd	USD200mn	3NC2	7.90%
3-May-18	Fantasia Holdings Group Co Ltd	USD150mn	FTHDGR 8.375%'21	9.9%
3-May-18	GLP Pte Ltd	EUR365mn	5-year	3%
2-May-18	CMT MTN Pte Ltd	SGD130mn	5-year	3.212%
2-May-18	China Aoyuan Property Group Ltd	USD200mn	3NC2	7.50%
2-May-18	PT Federal International Finance	USD300mn	3-year	CT3+160bps
2-May-18	Hydoo International Holdings Ltd	USD130mn	2-year	12%
30-May-18	Global Prime Capital Pte Ltd	USD50mn	BSDEIJ 7.25% '21	100.125+accrued
27-Apr-18	Central American Bank for Economic Integration	CNH2bn	5-year	4.85%
27-Apr-18	Hong Seng Ltd	USD250mn	363-day	8.75%
27-Apr-18	Ease Trade Global Ltd	USD150mn	POLHON 5.2%'21	99.996

Source: OCBC, Bloomberg

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