Asian Credit Daily

Feb 15, 2019

Credit Headlines: Singapore Airlines Limited, Commerzbank AG (CMZB), StarHub Ltd

Market Commentary

- The SGD swap curve traded little change yesterday, with most tenors trading unchanged (with the exception of the 12-year and 30-year swap rate trading 1bps lower).
- The Bloomberg Barclays Asia USD IG Bond Index average OAS widened 1bps to 147bps while the Bloomberg Barclays Asia USD HY Bond Index average OAS widened 1bps to 512bps.
- Flows in the SGD corporates were moderate yesterday, with flows seen in UBS 5.875%-PERPs, FPLSP 3.95-PERPs and ICICI 5.375%'28s.
- 10Y UST yields fell 4bps to close the trading session at 2.65%, on the back of safe haven demand as US retail sales dropped 1.2% in December, the largest drop in more than 9 years, signalling a slowdown in economic activity at the end of 2018. Germany's gross domestic product was also lower than economists' expectations, weighing in negatively on market sentiments. US consumer sentiment data will be released later today, as investors await for further signs regarding the strength of the US economy.

Credit Headlines

Singapore Airlines Limited ("SIA") | Issuer Profile: Neutral (3)

- SIA announced its third quarter results for the financial year ended March 2019 with revenue up 6.5% y/y to SGD4.3bn, on the back of stronger passenger growth numbers, stable cargo revenue and higher revenue contribution from 77.7%-owned SIA Engineering. Reported operating profit though was down 14.6% y/y to SGD387.6mn due to higher fuel cost, staff cost and depreciation.
- EBITDA (based on our calculation) was down 1.8% y/y to SGD742mn versus SGD31mn in interest expense, representing lower though still decent EBITDA/Interest coverage of 23.6x (3QFY2018: 29.7x).
- Capex was unsurprisingly high. In 3QFY2019, SIA spent SGD1.5bn largely for aircraft. For 9MFY2019, SIA had spent ~SGD4.6bn, out of SGD6.2bn projected for FY2019. Outside of the capex plan shared, SIA also made a large SGD184mn investment in associated companies in 3QFY2019 (2QFY2019: SGD19.6mn). We think this was for its Indian associate Vistara, to help Vistara funds its own plane purchase plans.
- The cash gap at SIA was funded by new debt and use of existing cash, including those from sale of advanced carriage (ie: cash received upfront prior to services being provided). Net gearing in end-Dec 2018 is now much higher at 0.31x versus 0.18x in the previous quarter.
- Apart from higher debt which was more or less expected, SIA took a SGD2.0bn loss in jet fuel derivatives contracts which hit book value of equity. This though is a non-cash item and could be used to offset fuel costs down the road. 80% of its fuel requirements for this quarter has been hedged at USD74 so we do not expect SIA to benefit much from the current lower oil price environment for 4QFY2019. SIA is on a leveraging trend, though for now we are maintaining SIA's issuer profile at Neutral (3).

Credit Headlines (cont'd)

Commerzbank AG (CMZB) | Issuer Profile: Neutral (4)

- CMZB released its 4Q2018 and FY2018 results with 4Q2018 income before risk results down 3.3% y/y. Key driver for the drop was a net fair value loss from financial assets and liabilities measured at fair value through profit and loss of EUR121mn against a EUR46mn gain in 4Q2017. This offset a 9.3% y/y rise in net interest income from volume growth that offset margin pressure. Overall however, a 5.2% y/y fall in operating expenses (lower personnel expenses offset higher digitilisation and growth expenses and higher regulatory project costs and levies) and 38.9% y/y fall in risk results contributed to a 97.1% y/y rise in operating profit to EUR240mn for 4Q2018.
- For FY2018, income before risk was down 2.2% y/y to EUR8.6bn due to both a 38.8% y/y fall in net fair value gains from financial assets and liabilities measured at fair value through profit and loss and 45.9% y/y fall in other income. Operating expenses also rose 0.7% y/y however a 42.9% y/y fall in risk result resulted in operating profit for FY2018 rising 8.4% y/y to EUR1.5bn. Overall pre-tax profit for FY2018 was up 168% to EUR1.2bn due to absence of restructuring expenses (EUR808mn recognized in FY2017).
- By segment, operating profit in the Private and Small-Business Customers segment fell 12.3% y/y for FY2018 due to absence of non-recurring items in 2018 and stable operating expenses. Operating profit in the Corporate Clients segment fell 7.0% y/y on margin pressure from competition as well as weaker capital markets business while operating expenses were constant on strategic investments that offset cost management. Finally the Asset & Capital Recovery segment continued its turnaround with operating income of EUR34mn in FY2018 against a loss of EUR264mn in FY2017 as legacy portfolios reduced by EUR5.1bn in FY2018.
- CMZB's balance sheet grew with total assets up 2.2% y/y. Growth occurred in its core operating segments (Private and Small Business Customers and Corporate Clients) in line with its "Commerzbank 4.0" strategy while its non-core exposures within the Asset & Capital Recovery segment continues to reduce as this business winds down. Overall, this appears to have improved the quality of CMZB's balance sheet and is consistent with the reducing risk results as well as the fall in the reported non-performing loan ratio to 0.9% for FY2018 (1.3% in FY2017).
- Given balance sheet growth as well as dividend accrual, CMZB's CET1 ratio fell to 12.9% as at 31 December 2018 against 13.2% as at 30 September 2018. Notwithstanding the fall, CMZB's CET1 ratio remains above its target CET1 ratio of 12.75% in 2019. This is following the 25bps reduction in the supervisory review and evaluation process ("SREP") requirements by the European Central Bank with its previous CET1 target ratio as per its "Commerzbank 4.0" strategy being 13.0% by 2020.
- In all, CMZB's results reflect the twin effects of its restructuring strategies on the plus side but the competitive operating environment on the negative side. The overhang from merger talk may also become a drag on CMZB from both a fundamental and technical basis. We continue to like the BNP and BPCE Tier 2s and within the CMZB curve prefer the CMZB 4.875% '27c22s against the CMZB 4.20% '28c23s. (OCBC, Company)

Credit Headlines (cont'd)

StarHub Ltd ("StarHub") | Issuer Profile: Neutral (3)

- StarHub reported 4Q2018 results. Revenue fell 9.8% y/y to SGD619.5mn, mainly due to declines in service revenues (-6.8% y/y to SGD457.5mn) led by declines in Mobile (-13.7% y/y to SGD194.3mn) and Pay TV (-19.1% y/y to SGD71.3mn). Broadband also saw a small decline (-3.1% y/y to SGD45.7mn). Enterprise Fixed was the only segment delivering positive results (+12.0% y/y to SGD146.1mn).
    - For Mobile, part of the revenue decline is due to structural trends with the fall in usage of IDD and voice. However for data, despite the increase in usage y/y to 6.1GB (4Q2017: 4.6GB), data usage revenue fell due to declines in post-paid ARPU to SGD41/mth (4Q2017: SGD46/mth) with lower excess data usage revenue from higher take-up of DataJump and higher data bundled into base plans, higher phone subsidies and a higher mix of SIM-Only plans.
    - For Pay TV, the revenue fall is unsurprising given the continuous declines in subscriber base, which has fallen y/y to 409k (4Q2017: 458k) and a fall in ARPU to SGD48/mth (4Q2017: SGD51/mth). We note StarHub had lost the rights to air 11 channels from Discovery.
    - For Enterprise Fixed services, Managed Services saw the bulk of the increase (+42.2% y/y to SGD61.5mn) with higher demand for cyber security, cloud, cryptographic and digital security solutions. This also included revenue from Ensign (consolidated from Jul 2017) and D'Crypt (consolidated from Jan 2018).
- Reported EBITDA fell 22% y/y to SGD111mn, more than the drop in revenue as operating expenses fell just 4.2% y/y to SGD590.1mn with 7.7% y/y fall in cost of sales to SGD304.0mn and other operating expenses flattish y/y at SGD286.2mn.
    - Cost of sales decrease was mainly due to (1) decline in cost of equipment sold (-10.8% y/y to SGD156.8mn) and sale of equipment fell 17.3% y/y to SGD162.0mn and (2) 5.8% y/y decline in cost of services to SGD129.6mn with lower TV content, likely due to the loss of 11 channels from Discovery.
    - For other operating expenses, while staff costs declined 10.6% y/y to SGD75.7mn, which is in-line with StarHub's guidance to slash 300 employees over 2019-21, marketing and promotions increased (+12.8% y/y to SGD30.7mn) due to new product launches and increase in depreciation (+10.1% y/y to SGD78.3mn) mainly due to addition of 4G spectrum rights in 2Q2017.
- Going forward, we expect the results to continue deteriorating. StarHub expects service revenue to be stable to a decline of 2% y/y in 2019, with service EBITDA margin to be between 26% to 28% (2018: 28.4%). The breakup of bundling with Pay TV is likely to pose some vulnerability to StarHub as the bundling strategy previously allowed StarHub to increase customer stickiness and achieve cross-selling between products.
- Reported net debt to TTM EBITDA is 1.52x for 2018 (2017: 0.98x), mainly due to increase in net debt and weaker EBITDA. That said, we expect the deterioration in credit metrics to slow as StarHub will be cutting dividends from 4.0cts a quarter (~SGD69mn) to 2.25 cts a quarter (~SGD39mn). Based on management's EBITDA guidance, we expect EBITDA to fall to ~SGD515mn (2018: SGD567mn). This should be sufficient to cover (1) capex at SGD260mn (assumed to be 11% of 2018's revenue), (2) dividends of ~SGD156mn and (3) ~SGD39mn interest and perpetual distribution. We have not factored the SGD282mn spectrum payment given expiry of the spectrum rights in 2033. This leaves ~SGD60mn in adjusted free cashflow (after payments for dividends, interest, perpetuals distributions) – which may be deployed for 5G networks expenses in the future. As such, despite the deteriorating results, we continue to hold StarHub at Neutral (3) Issuer Profile as credit metrics should stabilise as the net cash outflow should be stemmed following the dividend cut. (Company, OCBC)

Table 1: Key Financial Indicators

	15-Feb	1W chg (bps)	1M chg (bps)
iTraxx Asiax IG	76	-6	-12
iTraxx SovX APAC	58	-2	-8
iTraxx Japan	60	-4	-17
iTraxx Australia	73	-3	-15
CDX NA IG	65	-2	-11
CDX NA HY	106	0	2
iTraxx Eur Main	71	-3	-10
iTraxx Eur XO	309	-11	-26
iTraxx Eur Snr Fin	89	-4	-13
iTraxx Sovx WE	24	-1	-2
AUD/USD	0.709	0.08%	-1.49%
EUR/USD	1.129	-0.33%	-1.11%
USD/SGD	1.359	-0.16%	-0.14%
China 5Y CDS	54	-4	-7
Malaysia 5Y CDS	77	-6	-19
Indonesia 5Y CDS	112	-5	-16
Thailand 5Y CDS	45	3	1

	15-Feb	1W chg	1M chg
Brent Crude Spot ($/bbl)	65.02	4.70%	7.22%
Gold Spot ($/oz)	1,312.68	-0.12%	1.80%
CRB	178.72	0.35%	-0.14%
GSCI	416.24	2.05%	2.93%
VIX	16.22	-0.92%	-12.80%
CT10 (bp)	2.652%	1.79	-5.94
USD Swap Spread 10Y (bp)	3	1	1
USD Swap Spread 30Y (bp)	-18	1	3
US Libor-OIS Spread (bp)	28	-1	-8
Euro Libor-OIS Spread (bp)	5	0	0
DJIA	25,439	1.07%	5.71%
SPX	2,746	1.47%	5.19%
MSCI Asiax	645	1.17%	4.94%
HSI	27,964	0.06%	4.23%
STI	3,241	1.22%	0.89%
KLCI	1,689	0.16%	0.59%
JCI	6,398	-1.89%	-0.16%

New issues

- CIFI Holdings (Group) Co Ltd has priced a USD300mn 4NC2 bond (sub guarantors: certain non-PRC subsidiaries of issuer) at 7.625%, tightening from price guidance of 8.0% area.
- China Cinda Finance (2017) I Limited has priced a USD1.0bn deal (guarantor: China Cinda (HK) Holdings Co Ltd) across three tranches, with the USD200mn 3-year bond at CT3+135bps (tightening from IPT +160bps area), the USD200mn 5-year bond at CT5+170bps (tightening from IPT +205bps area) and the USD600mn 10-year bond at CT10+210bps (tightening from IPT of +245bps area).
- Jiangxi Railway Investment Group Corporation has priced a USD300mn 3-year bond at 4.85%, tightening from IPT of 5.25% area.
- China CITIC Bank International Ltd has scheduled investor calls from 15 Feb for its potential USD Tier 2 bond issuance.

Date	Issuer	Size	Tenor	Pricing
14-Feb-19	CIFI Holdings (Group) Co Ltd	USD300mn	4NC2	7.625%
14-Feb-19	China Cinda Finance (2017) I Ltd	USD200mn USD200mn USD600mn	3-year 5-year 10-year	CT3+135bps CT5+170bps CT10+210bps
14-Feb-19	Jiangxi Railway Investment Group Corporation	USD300mn	3-year	4.85%
13-Feb-19	Shimao Property Holdings Ltd	USD1.0bn	5NC3	6.125%
13-Feb-19	Times China Holdings Ltd	USD500mn	3NC2	7.625%
13-Feb-19	Airport Authority	USD500mn	10-year	CT10+78bps
12-Feb-19	Sunac China Holdings Ltd	USD800mn	3NC2	7.875%
12-Feb-19	Korea Development Bank	USD500mn USD500mn	3-year 5-year	CT3+65bps CT5+85bps
12-Feb-19	Bank of New Zealand	USD750mn	5-year	CT5+108bps
12-Feb-19	RHB Bank Berhad	USD300mn	5-year	CT5+128bps
12-Feb-19	Perusahaan Penerbit SBSN Indonesia III	USD750mn USD1.25bn	5.5-year 10-year	3.9% 4.45%
11-Feb-19	China Aoyuan Group Ltd	USD225mn	4NC3	7.95%
11-Feb-19	Zhenro Properties Group Ltd	USD230mn	2.5-year	10.75%
31-Jan-19	Towngas (Finance) Ltd (The Hong Kong and China Gas Company Ltd)	USD300mn	NC5-perpetual	4.75%

Source: OCBC, Bloomberg

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