

July 03, 2019

Credit Headlines: Sembcorp Industries Ltd, Sembcorp Marine Ltd, Frasers Property Ltd, Ascott Residence Trust, Ascendas Hospitality Trust, Industry Updates – REITs

Market Commentary

- The SGD swap curve bull-flattened yesterday, with the shorter tenors trading 0-1bps higher, while the belly and longer tenors traded 1-2bps lower.
- The Bloomberg Barclays Asia USD IG Bond Index average OAS remained unchanged at 133bps while the Bloomberg Barclays Asia USD HY Bond Index average OAS remained unchanged at 473bps.
- Flows in SGD corporates were light, with flows in SOCGEN 6.125%-PERPs.
- 10Y UST fell 5bps to 1.98%, after the post-G20 optimism wore off, and soft global manufacturing data boosted investor demand for US treasuries. This was compounded by dovish comments from BOE Governor Mark Carney regarding Brexit risks and trade conflicts. Spread between 3-month treasury bills and 10-year treasury notes continued to be inverted, with the spread widening to -18bps.

Credit Headlines

Sembcorp Industries Ltd (“SCI”) | Issuer Profile: Neutral (4) and Sembcorp Marine Ltd (“SMM”) | Issuer Profile: Unrated

- SCI’s ~61%-owned subsidiary SMM announced that Brazilian authorities have executed a search warrant on a subsidiary of SMM in Brazil, Esteves de Jesus (“EJA”). The search warrant was in connection with the on-going investigations related to Operation Car Wash in Brazil. Operation Car Wash is an on-going investigation being carried out by Brazilian authorities allegedly involving Petrobras and a former President of Brazil. Per SMM, the search is in relation to investigations against a former consultant engaged by EJA in Brazil. The current investigations also involve the former president of EJA.
- Petrobras is a shareholder and main client of Sete Brasil. In turn, Sete Brasil had in the past commissioned rigs to be built by subsidiaries of both SMM and Keppel Corporation Limited. We continue to monitor the developments at SMM. (Company, OCBC)

Frasers Property Ltd (“FPL”) | Issuer Profile: Neutral (4)

- FPL will be divesting 12 properties (9 in Germany, 3 in Australia) to its sponsored REIT Frasers Logistics Trust (“FLT”) for AUD644.7mn (SGD612.5mn), with target completion date by end-Aug 2019. This represents EUR320.3mn payment for the German properties and AUD125.5mn for the Australia properties. After adjusting for debt facilities and inter-company loans to be assumed by FLT, the purchase consideration by FLT is AUD507.2mn (SGD481.8mn). We view this asset recycling exercise as a credit positive for FPL. (Company, OCBC)

Credit Headlines (cont'd)

Ascott Residence Trust (“ART”) | Issuer Profile: Neutral (4) and Ascendas Hospitality Trust (“ASCHT”) | Issuer Profile: Unrated

- ART announced the proposed combination of ART and ASCHT by way of a trust scheme of arrangement. ASCHT is a stapled group comprising of a business trust and a REIT.
- ART would be buying all the stapled units of ASCHT for a consideration of SGD1.0868 per unit, comprising of SGD0.0543 in cash and 0.7942 units of new ART equity to be issued at SGD1.30 each. (ie: 5% cash and 95% in units). Immediately prior to the announcement, ART units trading at SGD1.30 per unit. Post-transaction, ASCHT and ART unitholders would be unitholders of the enlarged ART. ASCHT's bonds contain a delisting put although with both bonds trading above par, our base case assume that ASCHT bondholders will not exercise the put option.
- We expect the combined EBITDA/Interest coverage to increase given ASCHT's healthier standalone EBITDA/Interest coverage of 6.5x in 1Q2019 against ART's 1Q2019 EBITDA/Interest of 3.8x. The combined REIT will be significantly larger with a total assets of SGD7.6bn (ART standalone: SGD5.7bn as at 31 March 2019) which should allow even better access to financing markets given both equity and debt capital markets' increased preference for larger REITs.
- In January 2019, [CapitaLand Ltd \(“CAPL”, Issuer profile: Neutral \(3\)\)](#), the Sponsor of ART announced the proposed acquisition of [Ascendas Pte Ltd and Singbridge Pte Ltd \(“Ascendas Singbridge”\)](#) whose subsidiary is Sponsor of ASCHT. On 30 June 2019, this transaction completed, effectively with ART and ASCHT becoming “sister REITs” under the same Sponsor, CAPL. Despite this, ART's REIT Manager will be receiving SGD9.4mn (payable in units as acquisition fee) and the estimated professional and other fees and expenses to be incurred by the combined entity is SGD22.5mn. We expect the professional and other fees to be paid out in cash. Along with the 5% cash consideration, the professional fees and transaction expenses will cap the aggregate leverage benefits from the combination.
- Including 50% of ART perpetuals as debt, we estimate the combined adjusted aggregate leverage at ~38%, factoring (1) Ascott Raffles Place that have been sold (2) new Sydney property acquired by ART and (3) Assuming full outlay on ART's greenfield development of Iyf at One-North. As at 31 March 2019, ART's standalone adjusted aggregate leverage was ~39%.
- We think unitholders are likely to approve the combination and are reviewing ART for an upgrade of its issuer profile from its current issuer profile of Neutral (4). (Company, OCBC)

Credit Headlines (cont'd)

Industry Updates – REITs

- Monetary Authority of Singapore (MAS) is consulting the industry on potentially raising the current leverage limit of 45% to up to 55% for Singapore real estate investment trusts (“S-REITs”). We are expecting updates after 1 Aug 2019, the last day for submission of written comments.
- The reason cited was to provide S-REITs with more flexibility to use debt to manage their capital structure and hence better able to compete against private capital and foreign REITs when making real estate acquisitions from third parties, as such acquisitions tend to involve a competitive bidding process and are highly time-sensitive.
- MAS is also considering implementing a minimum interest coverage requirement of 2.5x as an additional safeguard for REITs that are allowed to have their aggregate leverage exceed 45% but not more than 50%. MAS is also seeking views on whether it is appropriate for a REIT to be allowed a higher leverage of 55%, for example, REITs that have a higher interest coverage ratio. As of the first quarter ended March 2019, all the issuers under our REIT coverage universe have interest coverage of above 2.5x.
- Should a higher aggregate leverage cap kick in, we think REITs would seek out more debt-funded acquisition as debt tends to be a cheaper source of capital than equity and it could be credit negative for the REITs, in our view.
- Historically, within our coverage universe, REIT bonds and perpetuals trade as a lower credit risk sector, justifying their tight credit spreads. This was despite of REIT's high liquidity risk, though offset by their recurring income generation and contained aggregate leverage cap, with REITs generally keeping internal management threshold of 40%.
- Should REITs be allowed to raise their aggregate leverage cap by up to 22%, it will no longer be our base case to assume that REITs are a lower credit risk sector. Assuming REITs are able to stretch aggregate leverage to 50% (broadly, this translates to a net gearing of 1.0x with REITs not keeping minimal cash balance) and assuming aggregate leverage of 55% (translates to a net gearing of 1.2x).
- For REIT perpetuals, the risks of non-call at first call may not necessarily increase as the higher leverage limit allows REITs to raise more senior debt which are cheaper to replace perpetuals.
- We see this as a credit positive for developers as the larger-sized assets can be more easily injected into the REIT, allowing these assets to be more easily monetised. We think the following issuers could be interesting, given their high contribution from investment properties while allowing spread pick up versus REITs: Hotel Properties Limited, Shangri-La Asia Limited, CapitaLand Ltd, Frasers Property Limited and City Development Ltd. (Business Times, OCBC)

Table 1: Key Financial Indicators

	<u>3-Jul</u>	<u>1W chg (bps)</u>	<u>1M chg (bps)</u>
iTraxx Asiax IG	61	-5	-20
iTraxx SovX APAC	39	-3	-13
iTraxx Japan	58	-6	-14
iTraxx Australia	60	-5	-20
CDX NA IG	52	-5	-18
CDX NA HY	108	1	3
iTraxx Eur Main	50	-5	-20
iTraxx Eur XO	245	-18	-62
iTraxx Eur Snr Fin	60	-7	-29
iTraxx Sovx WE	16	-1	-3
AUD/USD	0.699	0.11%	0.23%
EUR/USD	1.129	-0.68%	0.45%
USD/SGD	1.355	-0.03%	0.84%
China 5Y CDS	42	-3	-19
Malaysia 5Y CDS	49	-7	-27
Indonesia 5Y CDS	86	-6	-29
Thailand 5Y CDS	33	-1	-6

	<u>3-Jul</u>	<u>1W chg</u>	<u>1M chg</u>
Brent Crude Spot (\$/bbl)	62.77	-5.59%	2.43%
Gold Spot (\$/oz)	1,431.88	1.62%	8.04%
CRB	177.84	-1.68%	1.79%
GSCI	414.50	-2.39%	2.28%
VIX	12.93	-20.58%	-31.44%
CT10 (bp)	1.960%	-8.65	-11.07
USD Swap Spread 10Y (bp)	-4	3	0
USD Swap Spread 30Y (bp)	-32	2	-4
US Libor-OIS Spread (bp)	21	4	0
Euro Libor-OIS Spread (bp)	5	0	1
DJIA	26,787	0.90%	7.92%
SPX	2,973	1.91%	8.33%
MSCI Asiax	661	2.05%	6.44%
HSI	28,876	1.27%	7.37%
STI	3,371	2.01%	7.92%
KLCI	1,691	0.86%	2.16%
JCI	6,385	1.02%	2.83%

New issues:

- Shandong Guohui International (BVI) Co., Ltd (guarantor: Shandong Guohui Investment Co., Ltd) has priced a USD800mn 3-year bond at 4.37%, tightening from IPT of 4.8% area.
- Sumitomo Corporation has priced a USD500mn 5-year bond at T+87.5bps, tightening from IPT of T+110bps area.
- Tongfang Aqua Ltd (guarantor: Tsinghua Tongfang Co., Ltd) has priced a USD300mn 2.5-year bond at 7.0%, tightening from IPT of 7.125% area.
- Yuzhou Properties Co., Ltd has priced a USD400mn re-tap of its existing YUZHOU 6.0%'23s at 7.7%, tightening from IPT of 8.2% area.
- The Export-Import Bank of China has priced a USD100mn 4-year FRN at 3-month US LIBOR+60bps.
- Vietnam Prosperity Joint-Stock Commercial Bank has scheduled investor meetings commencing on 3 July for its potential USD bond issuance.
- Dafa Properties Group Ltd has scheduled investor roadshows commencing 3 July for its potential USD bond issuance.
- Chong Hing Bank Ltd has scheduled investor roadshows commencing on 3 July for its potential USD AT1 issuance.
- PT Perusahaan Listrik Negara (PLN) has scheduled investor roadshows commencing on 4 July for its potential USD bond issuance.

<u>Date</u>		<u>Size</u>	<u>Tenor</u>	<u>Pricing</u>
02-Jul-19	Shandong Guohui International (BVI) Co., Ltd	USD800mn	3-year	4.37%
02-Jul-19	Sumitomo Corporation	USD500mn	5-year	T+87.5bps
02-Jul-19	Tongfang Aqua Ltd	USD300mn	2.5-year	7.0%
02-Jul-19	Yuzhou Properties Co., Ltd	USD400mn	YUZHOU 6.0%'23s	7.7%
02-Jul-19	Export-Import Bank Of China	USD100mn	4-year	3m-US LIBOR+60bps
01-Jul-19	Skyfame Realty Holdings Ltd	USD105mn	3-year	13.0%
01-Jul-19	Tahoe Group Global (Co.,) Ltd	USD400mn	3-year	16.0%
27-Jun-19	Sunshine 100 China Holdings Ltd	USD200mn	2-year	12.5%
27-Jun-19	Mitsubishi Corporation	USD500mn	5-year	T+84bps
27-Jun-19	ESR Cayman Ltd	USD175mn	ESRCAY 7.875%'22s	7.25%

Source: OCBC, Bloomberg

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