

Asian Credit Daily

Tuesday, October 8, 2019

Market Commentary

- The SGD swap curve bull-flattened yesterday, with the shorter tenors traded around 3bps lower, while the belly and longer tenors broadly traded 3-5bps lower.
- The Bloomberg Barclays Asia USD IG Bond Index average OAS tightened 1bps to 136bps while the Bloomberg Barclays Asia USD HY Bond Index average OAS tightened 5bps to 547bps.
- Flows in SGD corporates were light, with flows in STANLN 5.375%-PERPs.
- 10Y USTs yields rose 3bps, closing at 1.56% with a large supply of Treasury notes and bills coming up for auction this week. The FOMC meeting minutes for September will also be released this week. The spread between 3-month treasury bills and 10-year treasury notes tightened to -15bps and remains inverted.

Credit Summary:

- [Keppel Corporation Ltd](#) | **Neutral (4)**: KEP announced on 7 Oct that its indirect wholly-owned subsidiaries Fernvale and FELS have entered into a settlement agreement with Sete Brasil and its subsidiaries, in relation to the construction contracts on all six semisubmersible drilling rigs which KEP was earlier contracted to build for Sete Brasil. Under the agreement, the engineering, procurement and construction (“EPC”) contract on the remaining four rigs will be terminated, with Fernvale assuming full ownership over all four rigs. The parties will also unconditionally and fully release each other from any and all actual and potential claims in relation to the EPC contracts. We have factored in zero recovery from any of these rigs in our issuer profile of Neutral (4) for KEP and we continue to assume zero recoveries as our base case. Net-net, we maintain KEP’s issuer profile at Neutral (4).
- [Australia & New Zealand Banking Group Ltd](#) | **Positive (2)**: ANZ announced additional costs for customer remediation charges that will impact its 2HFY2019 and FY2019 results. With ongoing reviews into potential remediation ongoing, we think there could be more charges in coming periods. That said, taking into consideration current charges and ANZ’s current Level 2 APRA compliant CET1 ratio of 11.8% as at 30 June 2019, and its solid recurring annual net income, there is no impact to our Positive (2) issuer profile on ANZ.
- [Sembcorp Industries Ltd and Sembcorp Marine Ltd](#) | **Neutral (5) and Unrated**: SMM and its subsidiaries have reached a full and final settlement of the claims under contracts with Sete Brasil and its subsidiaries. Per the settlement agreement, SMM will keep all the works performed for five out of the seven drillships. For the other two where construction work has been most advanced, the titles to the works will be apportioned between Sete Brasil and SMM, in proportion to payments that have been made to Sete Brasil. SMM remains exposed to event risk following its July 2019 announcement that Brazilian authorities have executed a search warrant on its subsidiary in Brasil. We continue to monitor developments in SMM (and thereby SCI) though for now maintain our issuer profile at SCI at Neutral (5).

Credit Research

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Credit Headlines

Keppel Corporation Limited (“KEP”) | Issuer Profile: Neutral (4)

- On 7 October 2019, KEP announced that its’ indirect wholly-owned subsidiaries, namely Fernvale Pte Ltd (“Fernvale”) and FELS Offshore Pte Ltd (“FELS”) have entered into a settlement agreement with Sete Brasil and six of Sete Brasil’s subsidiaries (namely, Urca, Frade, Bracuhy, Portogalo, Mangaratiba and Botinas) in relation to the construction contracts on all six semisubmersible drilling rigs which KEP was earlier contracted to build for Sete Brasil, a Brazil-based rig charterer.
- **Background:** In end-2011 and August 2012, KEP (via indirect wholly-owned subsidiaries) entered into rig building contracts with Sete Brasil, which lifted Sete Brasil into becoming a significant customer of KEP’s offshore & marine business. Petrobras, an oil and gas company majority owned by the Brazilian government, was in turn Sete Brasil’s only customer. Since November 2014, Sete Brasil, stopped making progress payments to KEP on the rigs, with KEP ceasing work in 2015. In April 2016, Sete Brasil filed for bankruptcy protection and commenced a restructuring process. The lack of continued financing at Sete Brasil and the significantly reduced demand for its’ rigs, leading to the restructuring, was widely linked to Sete Brasil’s alleged involvement in Operation Car Wash, code name for an ongoing criminal investigation.
- In 1H2019, as part of Sete Brasil’s recovery process for creditors, Sete Brasil tendered out four rigs, including two semisubmersible drilling rigs that KEP was contracted to build. The media has reported that these four rigs have a 10-year leasing contract with Petrobras who will pay USD299,000 per day when they become operational.
- In April 2019, KEP announced that it had submitted a bid to buy back those two rigs. In addition to KEP, Magni Partners (Bermuda) Ltd (“Magni”), founded by the Vice Chairman and significant shareholder of Borr Drilling, was the only other serious bidder for these rigs.
- Along with the settlement agreement announcement, KEP shared that Magni has emerged as the winning bidder of these rigs which KEP had partially build (under the Urca and Frade entities), free from encumbrance.
- As part of the settlement agreement:
 - The engineering, procurement and construction (“EPC”) contract on the remaining four rigs will be terminated, with Fernvale assuming full ownership over all four when the agreement comes into effect. Rigs under the Bracuhy and Portogalo entities have been ~40% and ~21% completed respectively while the remaining two are less than 10% completed.
 - The parties shall unconditionally and fully release each other from any and all actual or potential claims in relation to the EPC contracts
- The rigs which Magni are buying over (namely those under Urca and Frade) is ~92% and ~70% completed respectively where the amounts owned to Fernvale of ~USD260mn will be recognised as part of the undisputed debt included in Sete Brasil’s restructuring plan. Fernvale is separately discussing with Magni on terms to complete the construction of these rigs.

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Credit Headlines

Keppel Corporation Limited (“KEP”) | Issuer Profile: Neutral (4) [cont’d]

- KEP has not disclosed if it would need to take further impairments/write-downs on the rigs, although we believe the company will need to carry out an assessment given the settlement agreement and sale of two rigs by Sete Brasil. As of end-2018, KEP booked total cumulative expected loss of SGD476mn (~USD345mn) in relation to the Sete Brasil contracts, significantly higher than the first provision of SGD230mn (~USD167mn) in 2015.
- In our view this may still be insufficient to cover the full impairment/write-downs, though by necessity our assessment is subject to judgement calls given the absence of details over (1) Profit margins (if any) which KEP may have booked on completed work (2) Whether KEP will book margins on the rigs to be completed for Magni (3) What KEP will do with the remaining four rigs (4) Approximate completion on Mangaratiba and Botinas. A further impairment/write-down (if any) are non-cash and we take comfort that there is finally a resolution to these rigs.
- We have factored in zero recovery from any of these Sete Brasil rigs in our issuer profile of Neutral (4) for KEP and we continue to assume zero recoveries as our base case. Net-net, we maintain KEP’s issuer profile at Neutral (4). (Company, OCBC, Bloomberg, Reuters)

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Credit Headlines

Australia & New Zealand Banking Group Ltd (“ANZ”) | Issuer Profile: Positive (2)

- ANZ has [announced additional costs](#) for customer remediation charges that will impact its 2HFY2019 and FY2019 results which will be released on October 31.
- Remediation costs of AUD405mn after tax will be recognised in 2HFY2019 results for previous customer compensation programs as well as adjustments for existing programs and associated costs related to continuing operations as a result of product reviews in Australia Retail & Commercial.
- An additional AUD154mn after tax charge will also be recognised for discontinued operations, primarily in relation to Wealth products.
- This brings total expected customer remediation charges to AUD682mn for FY2019 and AUD1.1bn including previous charges in FY2018.
- With reviews into potential remediation ongoing, there could be more charges in coming periods. That said, using the current charges as a base and considering ANZ’s current Level 2 (or group level) APRA compliant CET1 ratio as at 30 June 2019 of 11.8% and its solid recurring annual net income, there is no impact to our Positive (2) issuer profile on ANZ.
- We continue to monitor ongoing profitability for Australian banks in light of expected inflation in compliance costs and charges (Company, OCBC)

Asian Credit Daily**Credit Headlines****Sembcorp Industries Ltd (“SCI”) | Issuer Profile: Neutral (5) and Sembcorp Marine Ltd (“SMM”) | Issuer Profile: Unrated**

- SMM (61%-owned subsidiary of SCI) and its subsidiaries has reached a full and final settlement of the claims under contracts with Sete Brasil and Sete Brasil’s subsidiaries. Upon fulfilment of the conditions precedent, all seven drillship contracts will be terminated and the parties will mutually release each other from all claims in relation to the contracts.
- **Background:** In 2012, SMM won a total of seven ultra-deepwater drillship contracts from Sete Brasil with deliveries ranging from 2Q2015 to 4Q2019. Payments from Sete Brasil to SMM stopped in November 2014, following which SMM had ceased construction of the drillships. In April 2016, SMM commenced arbitration proceedings against various subsidiaries of Sete Brasil to preserve its interest under the contracts.
- Per the settlement agreement:
 - SMM will keep all the works performed for five out of the seven drillships
 - For the other two where construction work has been the most advanced, the titles to the works will be apportioned between Sete Brasil and SMM, in proportion to payments that have been made by Sete Brasil
- A buyer had been found by Sete Brasil on these two drillships, though no details of the buyers identity were provided. The buyer is expected to negotiate with SMM on entering into new contracts to complete the drillships.
- In our view, there is a good chance that the buyer is Magni Partners (Bermuda) Ltd (“Magni”), as part of a packaged deal with two semisubmersibles that was being built by indirect wholly-owned subsidiaries of Keppel Corp Ltd (Issuer profile: Neutral (4)).
- Unlike KEP, SMM did not disclose the percentage completion of the seven drillships except to say these are in various stages of completion. As of end-2018, total provisions SMM took on the Sete Brasil contracts remained at SGD329mn (~USD238mn), a number that had remained unchanged since the first time SMM took provisions in 2015. Net-net we have insufficient information to form a judgement call as to whether or not this suffice. A further impairment/write-down (if any) are non-cash and we take comfort that there is finally a resolution to these drillships.
- Aside from the seven drillships, SMM remains exposed to event risk following its July 2019 announcement that Brazilian authorities have executed a search warrant on its subsidiary in Brazil in connection with Operation Car Wash. While it is too premature for us to comment on the knock on effects, we continue to monitor developments at SMM (and thereby SCI) though for now maintain our issuer profile at SCI at Neutral (5). (Company, OCBC, Bloomberg, Reuters)

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Key Market Movements

	08-Oct	1W chg (bps)	1M chg (bps)		08-Oct	1W chg	1M chg
iTraxx Asiax IG	79	2	21	Brent Crude Spot (\$/bbl)	58.59	-0.51%	-4.79%
iTraxx SovX APAC	37	0	1	Gold Spot (\$/oz)	1,489.08	0.67%	-0.67%
iTraxx Japan	63	1	8	CRB	173.10	-0.48%	0.28%
iTraxx Australia	68	1	10	GSCI	399.21	-1.09%	-1.30%
CDX NA IG	61	1	9	VIX	17.86	9.98%	19.07%
CDX NA HY	106	0	-1	CT10 (%)	1.567%	-6.88	0.63
iTraxx Eur Main	58	3	10				
iTraxx Eur XO	253	20	13	AUD/USD	0.673	0.39%	-1.92%
iTraxx Eur Snr Fin	68	4	10	EUR/USD	1.097	0.33%	-0.72%
iTraxx Eur Sub Fin	143	4	19	USD/SGD	1.382	0.25%	-0.13%
iTraxx Sovx WE	13	0	-2	AUD/SGD	0.930	-0.13%	1.86%
USD Swap Spread 10Y	-8	2	3	ASX 200	6,596	-2.18%	-0.78%
USD Swap Spread 30Y	-39	1	2	DJIA	26,478	-1.63%	-1.19%
US Libor-OIS Spread	36	-1	6	SPX	2,939	-1.27%	-1.34%
Euro Libor-OIS Spread	5	1	-2	MSCI Asiax	613	-0.62%	-1.58%
				HSI	25,821	-0.85%	-3.26%
China 5Y CDS	50	1	10	STI	3,099	-0.66%	-1.43%
Malaysia 5Y CDS	54	1	9	KLCI	1,559	-1.57%	-2.83%
Indonesia 5Y CDS	95	4	17	JCI	6,001	-2.73%	-4.89%
Thailand 5Y CDS	30	-1	3	EU Stoxx 50	3,471	-2.75%	-0.69%
Australia 5Y CDS	20	0	2				

Source: Bloomberg

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New Issues

- There were no new issues or mandates.

Date	Issuer	Size	Tenor	Pricing
04-Oct-19	Helenbergh China Holdings Ltd	USD300mn	2-year	13.5%
04-Oct-19	Fullerton India Credit Co., Ltd	SGD150mn	3.5-year	3.7%
03-Oct-19	Adani Renewable Energy (RJ) Ltd Kodangal Solar Parks Pte Ltd Wardha Solar (Maharashtra) Pte Ltd	USD362.5mn	20-year	4.625%
27-Sep-19	Zhongliang Holdings Group Co. Ltd	USD100mn	ZHLGHD 11.5%'21s	11.75%
27-Sep-19	Hongkong Ideal Investment Ltd	USD100mn	3NP2	14.75%
26-Sep-19	BOC Aviation Ltd	USD150mn	BOCAVI 3.0%'29s	T+150bps
26-Sep-19	Li & Fung Ltd	USD400mn	5-year	T+290bps
26-Sep-19	PCPD Capital Ltd	USD130mn	PCPDC 4.75%'22s	4.53%
26-Sep-19	ReNew Power Ltd	USD90mn	RPVIN 6.67%'24s	6.3%
26-Sep-19	Central China Real Estate Ltd	USD200mn	CENCHI 6.75%'21s	7.375%
26-Sep-19	Jinan Hi-tech Holding Group Co., Ltd	USD300mn	3-year	4.5%
25-Sep-19	CNOOC Finance (2013) Ltd	USD1.0bn USD500mn	10-year 30-year	T+120bps 3.3%
25-Sep-19	Woori Bank	USD550mn	Perp-NC5	4.25%
25-Sep-19	Hongkong International (Qingdao) Co., Ltd	USD300mn	5-year	4.0%

Source: OCBC, Bloomberg

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