Asia Credit Research

CWT Limited: Credit Update

Tuesday, 23 February 2016

Financial services helps mitigate softening core businesses

- **FY2015 performance held steady:** CWT's revenues fell 30% y/y to SGD9.9bn, driven by the decline in revenue from the Commodity Marketing ('CM') segment due to lower trading volume of naphtha and a general downturn in the commodity sector. Revenue and gross profit of CWT's core logistics business also declined by 3% y/y and 18% y/y respectively, reflecting softening demand and start-up costs from new logistics hubs during 2015. Despite the headline revenue decline however, consolidated EBITDA declined only 1.8% y/y to SGD200m whilst PAT (before minority interest) held steady at SGD113.9m (FY2014: SGD113.9m). This was largely attributable to the rising significance of the higher-margin Financial Services business, comprised of financial brokerage, risk management and trade facilitation services catering to end-customers in the commodities space. Proportionately, this segment contributed 18% to gross profit in FY2015, rising from 12% in FY2014. In FY2015, Financial Services reported gross margins of ~41% against the core logistics business of 14.6%. A combined effect from lower interest expense due to the drop in commodity prices and better gross margins (1.2% in FY2015 against 0.8% in FY2014) in CM business lifted reported bottom-line performance of this segment to SGD25.5m in FY2015 (FY2014:from SGD11.8m).

- **Improvement in credit ratios:** Overall, we saw an improvement in both leverage and coverage ratios. Gross debt-to-equity stands at 1.6x decreasing from 1.8x in FY2014 while EBITDA/ Gross Interest expense improved to 3.9x. Using an assumption of SGD3.2m as capitalised interest (ie: in line with that reported in FY2014), then EBITDA/Gross Interest expense would have improved to ~3.8x (FY2014: 3.2x). The improvement in coverage ratios was driven by a decline in capital expenditure to only ~SGD48m from an average of SGD150m during the two preceding years and a lower need for borrowings. This was due to a planned pull-back by management from aggressive expansion during FY2015, particularly within the logistics business.

- **Tilt to new risks:** CWT's core logistics business will continue to underpin the revenue and cash generation capability of the issuer although the Financial Services business will increase in prominence in the coming years. Via Straits Financial Group Pte Ltd (~98% owned subsidiary), the company has a significant Futures Commission Merchant ("FCM") business. CWT is exposed to heightened possibility of counter-party risk and off-balance sheet risk. As part and parcel of an FCM business, transactions with end-customers are often carried out on a margin basis and there may be instances where margin requirements are insufficient to fully cover customer losses. FCMs can take possession of margin deposits anytime to satisfy obligations from customer's futures position, providing a risk mitigation mechanism. We understand that CWT's FCM business does not engage in undue proprietary trading and focuses on serving as a broker.

- **Recommendation**: Since August 2015, there have been no new updates on the possible sale by major shareholders of the company, though any such changes could bring about an alteration in strategic direction and corollary, credit risk of the issuer. We **retain CWT's issuer profile at Neutral** for now and remain Neutral across the curve as we expect credit metrics to weaken from higher leverage over the next 1-2 years as CWT completes its mega logistics hub.

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CWT Ltd

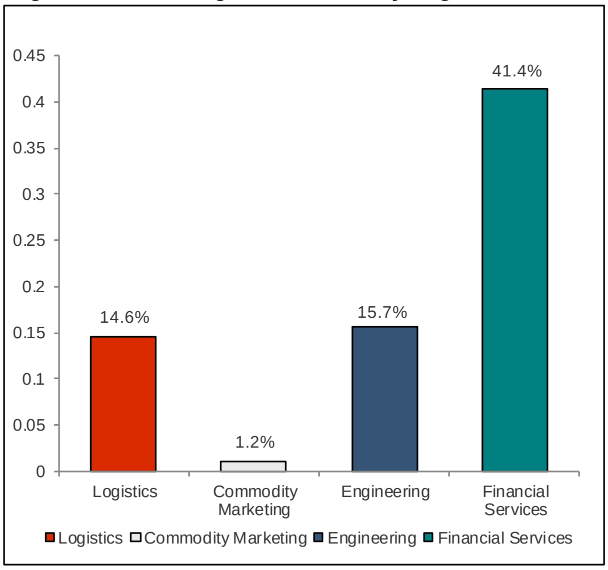
Table 1: Summary Financials

Year End 31st Dec	FY2013	FY2014	FY2015
Income Statement (SGD'mn)			
Revenue	9,097.1	14,194.4	9,931.6
EBITDA	157.6	203.4	199.8
EBIT	124.2	162.7	152.1
Gross interest expense	47.0	63.5	51.0
Profit Before Tax	115.7	131.6	131.7
Net profit	106.0	112.4	108.9
Balance Sheet (SGD'mn)			
Cash and bank deposits	197.3	342.0	310.3
Total assets	4,052.2	4,356.6	4,549.8
Gross debt	1,293.3	1,430.6	1,427.4
Net debt	1,096.0	1,088.6	1,117.1
Shareholders' equity	687.2	791.5	868.1
Total capitalization	1,980.6	2,222.1	2,295.5
Net capitalization	1,783.2	1,880.1	1,985.1
Cash Flow (SGD'mn)			
Funds from operations (FFO)	139.4	153.0	156.6
CFO	-390.8	237.1	317.3
Capex	181.0	113.7	259.1
Acquisitions	21.7	20.5	24.9
Disposals	35.1	5.3	28.2
Dividend	21.1	23.4	46.2
Free Cash Flow (FCF)	-571.8	123.4	58.2
FCF adjusted	-579.6	84.8	15.3
Key Ratios			
EBITDA margin (%)	1.7	1.4	2.0
Net margin (%)	1.2	0.8	1.1
Gross debt to EBITDA (x)	8.2	7.0	7.1
Net debt to EBITDA (x)	7.0	5.4	5.6
Gross Debt to Equity (x)	1.88	1.81	1.64
Net Debt to Equity (x)	1.6	1.4	1.3
Gross debt/total capitalisation (%)	65.3	64.4	62.2
Net debt/net capitalisation (%)	61.5	57.9	56.3
Cash/current borrowings (x)	0.2	0.4	0.4
EBITDA/Total Interest (x)	3.4	3.2	3.9

Source: Company, OCBC estimates

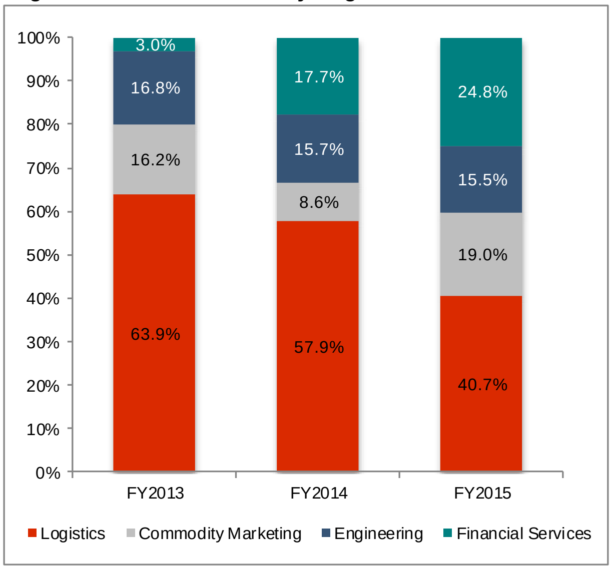
** FCF Adjusted = FCF - Acquisitions - Dividends + Disposals*

Figure 1: Gross Margin breakdown by Segment - FY2015



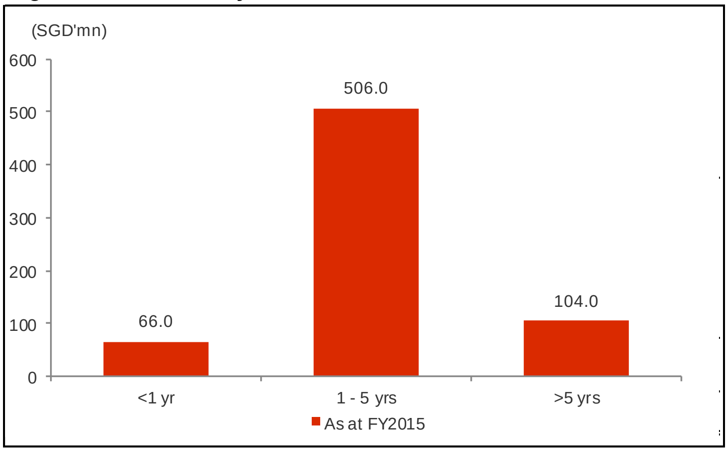
Source: Company

Figure 2: PBT breakdown by Segment - FY2015



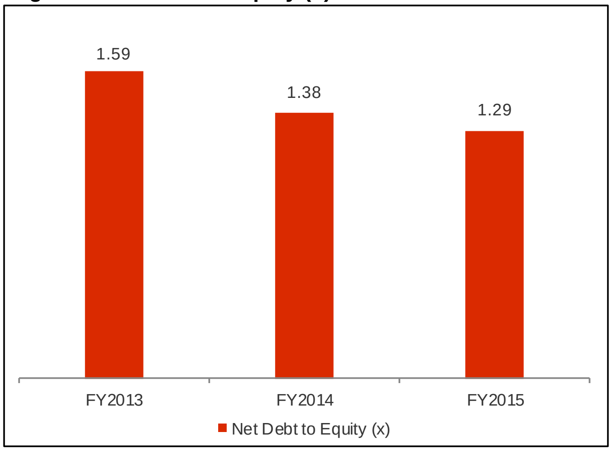
Source: Company

Figure 3: Debt Maturity Profile



Source: Company

Figure 4: Net Debt to Equity (x)



Source: Company, OCBC estimates