

Gallant Venture Ltd: Credit Update

Friday, 14 October 2016

Err on the side of caution

- Re-statement and re-audit increases complexity/uncertainty in assessing the actual profits of the company and the potential knock-on effects on the calculation of Net Tangible Assets (“NTA”). Company’s credit risks as earlier highlighted persist.
 - Per media reports, company is in negotiations with banks to secure standby facilities in the event expected liquidity (from proceeds of sale of assets) is delayed.
 - While we take this as a positive signal, until such time there is further certainty on the liquidity situation at GALV, we maintain our Negative issuer profile on the company and bond ratings on all 3 bonds at Underweight¹.
- GALV announced that the Singapore Accounting Corporate Regulatory Authority (“ACRA”) had on 10 October 2016 issued an Advisory Letter to the board which requires the company to re-state and re-audit its consolidated financial statements for FY2014 and FY2015. In addition, ACRA has also issued warning letters in relation to non-compliance with certain accounting standards.
 - **Next action:** The Company has added that the issues raised pertain to specific Financial Reporting Standards (“FRS”). GALV (i) intends to voluntarily comply with the Advisory Letter (ii) currently in discussions with its auditors and (iii) expects further discussions with ACRA. The re-stated and re-audited financial statements will be laid before the shareholders during the same time as the next annual general meeting (to be held by 30 April 2017). A shareholder’s circular will be dispatched (containing further information) in due course.
 - **Preliminary Views on Advisory Letter Items:** All 3 items highlighted in the announcement pertains to transactions recorded historically. We have attempted to diagnose the impact of ACRA’s action as it pertains to credit analysis.

Treasury Advisory

Corporate FX & Structured Products

Tel: 6349-1888 / 1881

Interest Rate Derivatives

Tel: 6349-1899

Investments & Structured Products

Tel: 6349-1886

GT Institutional Sales

Tel: 6349-1810

OCBC Credit Research

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| Paragraph | Items Raised | Preliminary View |
|--|---|---|
| Paragraphs 20(b) and 28 of FRS 7 Statement of Cash Flow | Currency translation differences from converting subsidiaries functional currency in IDR to GALV’s presentation currency in SGD should not have been classified as an adjustment to profit before tax in cash flow statement | Credit impact insignificant in our view due to the small net effect |
| Paragraph 37 of FRS 103 Business Combinations and Paragraph 43 of FRS 39 Financial Instruments | In respect of unsecured non-convertible bonds issued by GALV in 2012, in connection with the acquisition of PT Indonomobil Sukses Internasional Tbk (“IMAS”), GALV should have recognized the purchase consideration for such business acquisition based on fair value of the bonds (~SGD82mn) instead of principal amount (~SGD105mn). | Historical profits overstated, potential knock-on impact on NTA. |
| Paragraph 7 of FRS 110 Consolidated | GALV’s investment in Market Strength Limited (“MSL”) by way of holding ~USD203mn principal amount of notes | MSL is a holding company (owns a property project in Shanghai) and likely to be |

¹ OCBC Asian Credit Daily 13 October 2016

| | | |
|----------------------|--|---|
| Financial Statements | and detachable warrants issued by MSL. This transaction should have been accounted for by way of consolidating MSL as a subsidiary of GALV. ² | loss-making during the early years of property development. Historical profits likely overstated, potential knock-on impact on NTA. These notes were divested in April 2016. A gain may be allowed to be recorded in FY2016, offsetting some of the earlier accumulated losses. |
|----------------------|--|---|

Source: Company's announcement on 12 October 2016, OCBC Credit Research

- **Implications:**

- (i) **Heightened second-order effect:** Company's credit risks as earlier highlighted persist (ie: stretched liquidity, lackluster operating performance at IMAS)³. The latest development is likely to cause a further compression in GALV's standalone financial flexibility.
- (ii) **Uncertainty on assessing actual profits and Net Tangible Asset ("NTA"):** As part of its bond terms, GALV needs to meet two covenants relating to NTA⁴, and such covenants exclude the Indonesia vehicle financing arm of the group (ie: PT Indomobil Finance Indonesia "IMFI"). While we do not have the standalone financials of IMFI, this entity is likely profitable and vehicle financing has been a growth area of IMAS. In 1H2016, the direct parent company of IMFI reported ~SGD9.4mn in net profits (based on SGD1:IDR9,437 as exchange rate). Based on unaudited financials for the period ended 30 June 2016, our calculation of unadjusted NTA was SGD1.2bn and net-net there is a strong possibility that calculations based on covenant terms are lower. The latest announcement increases complexity/uncertainty in assessing the actual profits of the company and the knock-on effect on the calculation of Net Tangible Assets ("NTA"). We are unable to determine whether or not the company will meet its covenants post the re-statement and re-audit. In the event that this causes a covenant breach, the company will likely convene a consent solicitation exercise for bondholders to decide on a proposed change in terms.

- **Recommendation:** We maintain our Negative issuer profile of the company and are lowering all 3 bonds to Underweight. We would be willing to take a small hit to principal versus the uncertainties of outcomes with regards to the re-statement and re-audit.

| Issuer | Issue | Maturity | Outstanding Amount (SGDm) | Ask Price | Ask YTW | I-Spread | Rating |
|--------|----------------|------------|---------------------------|-----------|---------|----------|----------|
| GALV | GALVSP 5.9 '17 | 12/05/2017 | 150 | 97.25 | 11.3 | 1,022 | NR/NR/NR |
| GALV | GALVSP 7.0 '17 | 02/08/2017 | 75 | 97.25 | 11.0 | 977 | NR/NR/NR |
| GALV | GALVSP 7.0 '18 | 06/04/2018 | 230 | 91.00 | 14.0 | 1,262 | NR/NR/NR |

Note: Indicative prices as at 13 October 2016

² Historically, this investment was recorded as "Notes Receivable" in non-current assets

³ OCBC Asia Credit – Gallant Venture – Credit Update – 11 Oct 2016

⁴ (i) Consolidated NTA shall not be less than SGD1bn (ii) Net debt-to-NTA shall not exceed 2.25x

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