Asia Credit Research

OCBC Bank

GuocoLand Ltd: Credit Update

Friday, 28 October 2016

Expending the cash pile

- GuocoLand's cash pile strengthened considerably after divesting Dongzhimen last year. However, 1Q17 results revealed that net gearing rose 14pp q/q to 0.84x due to the acquisition of Martin Place for SGD595.1mn.
- GuocoLand currently has the highest net gearing amongst its peers amongst our coverage. We expect net gearing to increase to 0.93x following the subscription of 27% stake in Eco World International Berhad (est. SGD180mn) and after paying c.SGD100mn of dividends.
- We are downgrading GUOLSP '18s and GUOLSP '19s from Overweight to Neutral, and prefer the OUESP 4.25 19c17 for a switch trade with a healthier net gearing of 0.67x and a 64-78 bps pickup.

Recent Developments

- **Subscription of stake in Eco World International Berhad**: After news since May 2016 that GuocoLand has been in talks, it was announced yesterday that GuocoLand will be subscribing for a 27% stake in Eco World International Berhad ("EWI") when the IPO is launched (expected in 1Q17). More than 2bn ringgit (SGD666mn) is expected to be raised to fund four development projects in London and Sydney with a gross development value of c.SGD4.1bn. This allows GuocoLand to quickly enter other markets, as it operates mainly in Singapore, China, Malaysia and Vietnam. GuocoLand's share is estimated to be worth at least SGD180mn. While the move diversifies GuocoLand from the Singapore property market, this will further elevate GuocoLand's net debt levels.

- **Summary of 1QFY17 results**: On 24th Oct 2016, GuocoLand announced its 1Q17 results. As a recap[1], revenue fell 54% y/y due to absence of contribution from the sale of an office block in Shanghai Guoson Centre a year ago. Net profit fell 95% y/y, mainly due to absence of divestment gains related to the Dongzhimen project a year ago. However, we are not overly concerned over the large y/y declines, as revenues only inched down 5.5% q/q without the one-offs.

Business and Financial Analysis

- **Twists in credit profile since Dongzhimen divestment**: We were upbeat about GuocoLand's credit profile after divesting Dongzhimen last year. In addition to the sizeable divestment gains of c.SGD580mn, the proceeds from divestments halved the net gearing from 1.40x in end-FY2015 to 0.70x in end-FY2016. However, the credit trend did not continue as GuocoLand acquired a residential site at Martin Place for SGD595.1mn, increasing net gearing to 0.84x as of end-1QFY17. With c.SGD100mn of dividends to be paid following higher declared dividends of 9 SGD cts per share, and an estimated SGD180m to subscribe for the stake in EWI, net gearing may increase to 0.93x. Net gearing may deteriorate further in the medium-term as capex is likely to increase due to Martin Place.

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Tel: 6349-1886

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Tel: 6349-1810

OCBC Credit Research
Wong Hong Wei
+65 6722-2533
WongHongWei@ocbc.com

[1] OCBC Asian Credit Daily – 25 October 2016

- **Boost in recurring income once Tanjong Pagar Centre comes on stream:** The completion is expected sometime in early 2017, following which higher revenue and income contributions may follow. Already, the office component was 80% committed as of Oct 2016, and we expect this to contribute c.SGD20mn to rental income per quarter. Other sources of recurring income include the 222-room Sofitel Singapore City Centre and the 100,000 sqft retail component, which is already more than 75% committed.

- **Slowing property market to drag down sales:** Singapore private residential property prices continued to fall for the 12th consecutive quarter. We think this may pressure sales of the remaining units at Leedon Residence and negatively impact Wallich Residence, which is expected to be launched in early 2017. If the property down cycle is extended, sales at Sims Urban Oasis may be affected. Malaysia, where GuocoLand is also operating, similarly faces a weak property outlook. While 20 Collyer Quay (office investment property) has been mitigating weaknesses from the residential front, we note that CBD office rents have been facing pressure in recent quarters.

- **Manageable credit metrics but no longer comparable to peers:** We expect net debt/equity to increase to 0.93x, which is manageable as recurring cashflow may increase and provide better cover over the interest expense. However, the gearing ratio currently towers over peers such as OUE (0.67x), CapitaLand (0.49x) and City Development (0.28x). We also note large refinancing needs, with short-term debt of SGD2.8bn exceeding cash of SGD1.1bn on hand.

Recommendation: Despite the deterioration in gearing ratio, we keep GuocoLand's Issuer Profile at Neutral as the credit metrics remains manageable with a larger recurrent income base. However, we are downgrading our OW recommendation to Neutral on GUOLSP '18s and GUOLSP '19s as 1) net gearing, which currently exceeds peers, may deteriorate further and 2) both bonds have seen yield compression of 19 to 48 bps since our OW recommendation in July 2016[2]. With the GUOLSP complex trading higher and above par following the improvement of the credit profile after the Dongzhimen divestment, we see the potential of supply risk while chunky short-term debt of SGD2.8bn matures over the next 12 months. We currently favour OUESP 4.25 19c17 for a switch trade, for 78 bps pick up over GUOLSP '18s or 64 bps pick up over GUOLSP '19s.

					Recommendation	
Issue	Maturity	Ask Price	Ask YTW	Bond Ratings	Current	Previous
GUOLSP 3.4 '18	04/09/2018	100.85	2.92	NR/NR/NR	N	OW
GUOLSP 3.95 '19	01/04/2019	102.05	3.06	NR/NR/NR	N	OW
OUESP 4.25 '19c17	30/10/2019	101.55	3.70	NR/NR/NR	OW	OW

Indicative prices from Bloomberg as of 27 October 2016

[2] OCBC Asian Credit Monthly – 12 July 2016

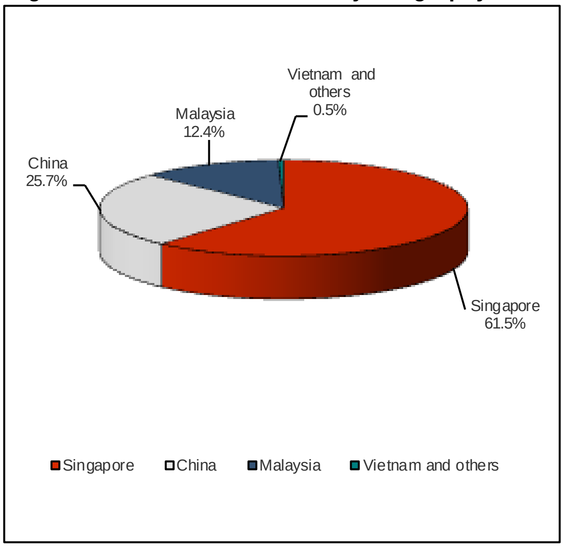
Guocoland Limited

Table 1: Summary Financials

Year Ended 30th Jun	FY2015	FY2016	1Q2017
Income Statement (SGD'mn)			
Revenue	1,159.9	1,059.8	202.8
EBITDA	299.4	223.0	29.7
EBIT	290.4	213.0	28.2
Gross interest expense	183.6	159.8	7.6
Profit Before Tax	318.7	773.2	31.5
Net profit	226.4	606.7	25.6
Balance Sheet (SGD'mn)			
Cash and bank deposits	663.1	1,430.2	1,125.2
Total assets	9,511.8	7,906.6	8,145.0
Gross debt	5,280.0	3,830.3	4,053.6
Net debt	4,616.9	2,400.0	2,928.4
Shareholders' equity	3,296.2	3,442.2	3,466.9
Total capitalization	8,576.3	7,272.5	7,520.5
Net capitalization	7,913.2	5,842.3	6,395.3
Cash Flow (SGD'mn)			
Funds from operations (FFO)	235.4	616.8	27.2
* CFO	-79.9	389.7	-507.1
Capex	231.5	286.9	24.7
Acquisitions	11.6	0.0	0.0
Disposals	20.7	2,251.6	0.0
Dividend	66.6	66.7	0.0
Free Cash Flow (FCF)	-311.3	102.8	-531.7
* FCF Adjusted	-368.7	2,287.7	-531.7
Key Ratios			
EBITDA margin (%)	25.8	21.0	14.6
Net margin (%)	19.5	57.2	12.6
Gross debt to EBITDA (x)	17.6	17.2	34.2
Net debt to EBITDA (x)	15.4	10.8	24.7
Gross Debt to Equity (x)	1.60	1.11	1.17
Net Debt to Equity (x)	1.40	0.70	0.84
Gross debt/total capitalisation (%)	61.6	52.7	53.9
Net debt/net capitalisation (%)	58.3	41.1	45.8
Cash/current borrowings (x)	0.4	0.7	0.4
EBITDA/gross interest (x)	4.6	3.8	3.9

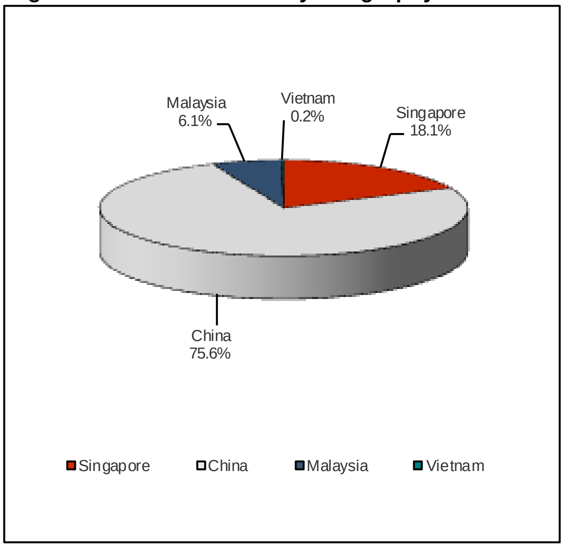
Source: Company, OCBC estimates

Figure 1: Revenue breakdown by Geography - FY2016



Source: Company

Figure 2: PBT breakdown by Geography - FY2016



Source: Company

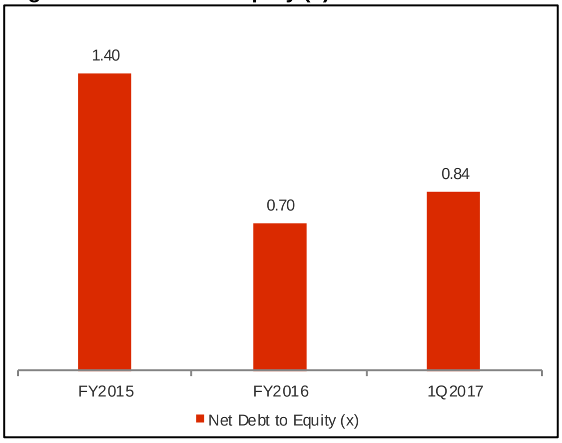
**FCF Adjusted = FCF - Acquisitions - Dividends + Disposals | *CFO after deducting interest expense*

Figure 3: Debt Maturity Profile

Amounts in (SGD'mn)	As at 30/9/2016	% of debt
Amount repayable in one year or less, or on demand		
Secured	1675.1	41.3%
Unsecured	1127.9	27.8%
	2803.0	**69.1%**
Amount repayable after a year		
Secured	617.0	15.2%
Unsecured	633.6	15.6%
	1250.6	**30.9%**
Total	**4053.6**	**100.0%**

Source: Company

Figure 4: Net Debt to Equity (x)



Source: Company, OCBC estimates