Asia Credit Research

Singapore Post Limited: Credit Update

Monday, 15 February 2016

Turning Net Debt

- **Inorganic growth continues:** For 3QFY2016 (ending December 2015), Singapore Post Limited ("SPOST") reported SGD316.2mn in total revenue, up 32.0% y/y. With the mail segment showing flat growth, growth was driven by the logistics segment (+32.9% y/y) and retail & eCommerce segment (+138.4% y/y). Most of the growth was driven by acquisitions, such as Courier Please (acquired in December 2014) in the logistics segment and TradeGlobal (acquired in November 2015) in the retail & eCommerce segment. Today, logistics is the largest revenue contributor at ~49% of total revenue (9MFY2016) while the mail segment is ~40%. Comparatively, for FY2015, mail revenue was ~51% of total revenue. As most acquisitions made had mainly overseas operations, the revenue contribution from overseas increased as well from 31% (9MFY2015) to 42% (9MFY2016). Looking forward, we expect both trends to continue with revenue shifting towards non-mail and non-domestic sources.

- **Segment margins improved, overall margin poorer:** Mail segment operating margin improved from 29.2% (3QFY2015) to 29.8%, driven by efficiency improvements. Logistics operating margin improved from 5.7% (3QFY2015) to 7.5% (3QFY2016), driven by post-merger integration and efficiencies. The retail & eCommerce segment operating margin remained flat at 7.6%, despite the sharp increase in revenue. SPOST's newest acquisition, TradeGlobal (acquired for ~SGD236mn), generated SGD2.1mn in operating profit on SGD29.4mn in revenue (7.1% operating margin). With the shift in revenue mix, total operating margin actually fell from 21.2% (3QFY2015) to 17.3% (3QFY2016). If we exclude FX translation gains, operating margin would fall further to just 16.3%. Though operational improvements via integration may improve segment margins, the expected continued shift in revenue mix (given the secular decline in the lucrative domestic mail business) would see margins continue to decline.

- **Cash burn continues**: During 3QFY2016, though SPOST generated SGD50.0mn in operating cash flow, it spent SGD59.2mn in capex, SGD233.1mn in acquisitions (mainly TradeGlobal), and SGD32.4mn in dividends. The cash gap was met with SGD121.9mn in additional borrowings as well as SGD141.5mn from its cash balance. As a result, SPOST has gone from **net cash to net debt**, with a still healthy net gearing of 12%. On a gross and net debt to EBITDA though, leverage deteriorated to 2.1x and 1.0x respectively. Though we had expected SPOST to eventually turn net debt in the near future[1], it happened sooner than anticipated, as the second Alibaba investment (worth SGD187.1mn in equity infusion and SGD92mn to acquire part of a subsidiary) has been further delayed (with the long-stop date shifted to end-May 2016). Though the Alibaba investment may drive SPOST back to net cash, we still believe that SPOST would eventually revert to net debt, as it still has cash needs for capex, working capital and dividends. It is worth noting that SPOST seems to be taking a pause with regards to acquisitions, with the CFO indicating that SPOST will be taking a break to integrate the numerous

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[1] OCBC Asia Credit – Singapore Credit Outlook 2016 (7 Jan 2016)

acquisitions made in recent years[2]. Management also indicated that SPOST will be able to sustain its dividend payout.

- **Short-term borrowings jumped:** Cash / current borrowings fell from 16.8x (end-1HFY2016) to just 1.3x (end-3QFY2016) due to about SGD140.2mn in unsecured borrowings due in the next 12 months. This could be bridge financing taken to make the TradeGlobal acquisition (with management indicating that the financing will be repaid when some fixed deposits mature). Aside from this, the only other major borrowing will be its SGD200mn in bonds maturing in 2020.

- **Recommendation:** Though SPOST has turned net debt sooner than we expected, we are comfortable holding its **Issuer Profile at Neutral**, particularly given the infusion in capital from Alibaba, as well as the indication that acquisitions will slow. SPOST's credit profile remains strong, though it is likely to continue to deteriorate post the Alibaba investment. In terms of bond recommendation though, we continue to believe that SPOST's bond and perpetual security are trading rich. In addition, we believe that the corporate governance issues and abrupt departure / succession issues regarding the CEO role will continue to drive negative headlines. The negative credit watch by S&P is another potential negative catalyst as well. We are seeing better value at similarly rated issuers, such as Capitaland Mall Trust for the straight bond, and Ascendas REIT for the perpetual security (~100bps pickup more than compensates for one notch rating differential assuming SPOST downgrade, and the reset for AREIT offsetting the structural seniority of the SPOST perp). As such, we continue to **Underweight both the SPOST'20s and perpetual securities** on valuation.

[2] Business Times - SingPost takes a break from acquisitions (05 Feb 2016)

Singapore Post Limited

Table 1: Summary financials

Year ended 31st March	FY2014	FY2015	9M2016
Income statement (SGD'mn)			
Revenue	821.1	919.6	834.0
EBITDA	170.9	169.1	128.2
EBIT	140.6	134.6	104.5
Gross interest expense	6.7	4.4	9.4
Profit Before Tax	227.7	192.5	176.6
Net profit	192.0	157.6	143.5
Balance Sheet (SGD'mn)			
Cash and bank deposits	404.4	584.1	185.1
Total assets	1,740.5	2,197.8	2,368.7
Gross debt	234.1	238.3	361.1
Net debt	-170.3	-345.8	176.0
Shareholders' equity	1,114.5	1,467.7	1,489.5
Total capitalization	1,348.6	1,706.1	1,850.6
Net capitalization	944.2	1,121.9	1,665.5
Cash Flow (SGD'mn)			
Funds from operations (FFO)	222.2	192.2	167.2
CFO	229.5	230.2	67.6
Capex	37.8	104.4	229.9
Acquisitions	3.0	120.7	270.0
Disposals	1.4	11.0	52.5
Dividend	133.6	143.0	142.1
Free Cash Flow (FCF)	191.8	125.8	-162.3
FCF adjusted	56.5	-126.8	-521.8
Key Ratios			
EBITDA margin (%)	20.8	18.4	15.4
Net margin (%)	23.4	17.1	17.2
Gross debt to EBITDA (x)	1.4	1.4	2.1
Net debt to EBITDA (x)	-1.0	-2.0	1.0
Gross Debt to Equity (x)	0.21	0.16	0.24
Net Debt to Equity (x)	-0.15	-0.24	0.12
Gross debt/total capitalisation (%)	17.4	14.0	19.5
Net debt/net capitalisation (%)	-18.0	-30.8	10.6
Cash/current borrowings (x)	28.8	34.5	1.3
EBITDA/Total Interest (x)	25.6	38.7	13.6

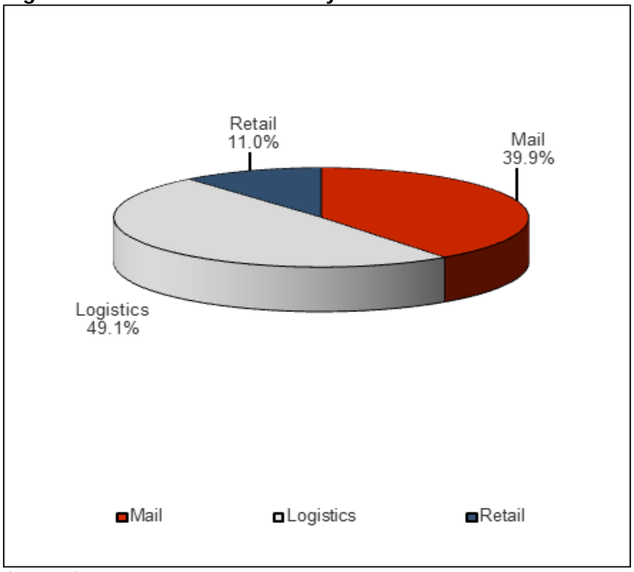
Source: Company, OCBC estimates
**Adjusted FCF = FCF –Acquisitions – Dividends + Disposals*

Figure 3: Debt Maturity Profile

Amounts in SGD mn	As at 31/12/2015	% of debt
Amount repayable		
One year or less, or on demand		
Secured	2.4	0.7%
Unsecured	140.2	38.8%
After one year		
Secured	15.2	4.2%
Unsecured	203.2	56.3%
Total	**361.1**	**100.0%**

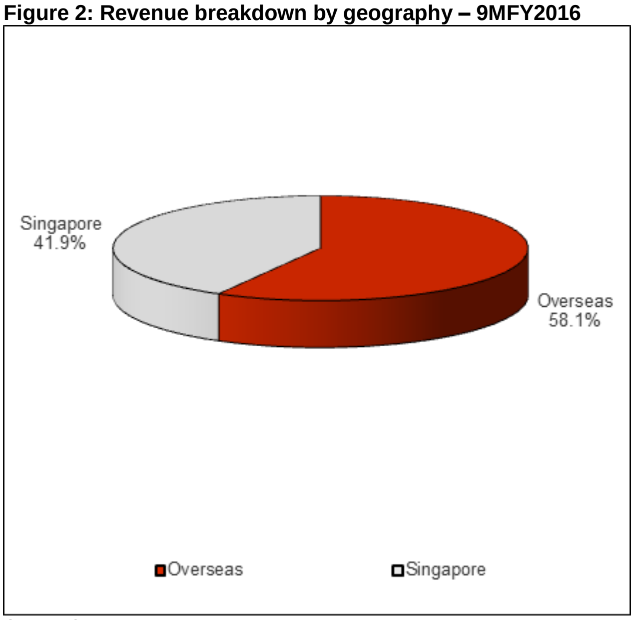
Source: Company

Figure 1: Revenue breakdown by business – 9MFY2016



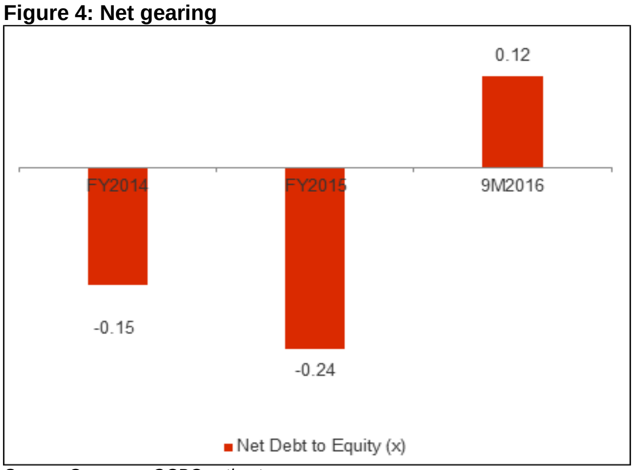
Source: Company

Figure 2: Revenue breakdown by geography – 9MFY2016



Source: Company

Figure 4: Net gearing



Source: Company, OCBC estimates

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