

Credit Update: OUE Limited (“OUE”)

Rubik’s cube

- While OUE is better known as a Singapore-focused property developer, the company’s key business is as an investment holding company, holding significant stakes in two Singapore-listed REITs, investment properties and increasingly focused on its healthcare businesses outside of Singapore. In October 2018, OUE and its subsidiaries had bought SGD202mn in Indonesia-linked assets from its sister company. Concurrently, OUE sold the office components of OUE Downtown to ~56%-owned OUE-CT for ~SGD908mn (pocketing ~SGD580mn, net of the pro-rata rights units that OUE subscribed to). OUE is also in the midst of buying ~SGD150mn in land in South Jakarta, though on a standalone basis, OUE will be paying the seller in the form of a non-cash asset.
- **Recommendation:** While OUE is now more exposed to Indonesia, in our view, this is still a manageable quantum versus OUE’s total asset base. We estimate SGD4.7bn of assets are in quick assets (eg: cash and receivables) and properties located in the developed markets of Singapore, US, Japan. We are maintaining OUE’s issuer profile at Neutral (4) until such time there are further material changes to its asset base (eg: sales of developed market assets to buy more in Indonesia). With the curve trading at 140bps-190bps wider versus GuocoLand Ltd’s (“GUOLSP”) curve, we think the risk-return is now in favour of the OUE bonds. We hold GUOLSP’s issuer profile at Neutral (5).

Issuer Profile:
Neutral (4)

Ticker: **OUESP**

Background

OUE Limited (“OUE”) is a holding company with exposures in real estate development, investment holdings in property assets and healthcare. OUE is the sponsor and holds a significant stake in both OUE-Hospitality Trust (“OUE-HT”) and OUE Commercial REIT (“OUE-CT”). OUE is 68.6%-owned by the Lippo Group.

Figure 1: OUESP and Comparable SGD Bonds

Bond	Maturity date/ Reset Date	Net gearing	Ask Yield	Spread
OUESP 4.25% ‘19	30/10/2019	0.68x	4.18%	220bps
OUESP 3.8% ‘20	15/04/2020	0.68x	4.61%	256bps
OUESP 3.75% ‘22	17/04/2022	0.68x	5.37%	314bps
OUESP 3.55% ‘23	10/05/2023	0.68x	6.00%	371bps
GUOLSP 3.95% ‘19	01/04/2019	0.86x	2.55%	71bps
GUOLSP 4.1% ‘20	13/05/2020	0.86x	3.26%	120bps
GUOLSP 3.62% ‘21	30/03/2021	0.86x	3.64%	149bps
GUOLSP 4.0% ‘22	31/01/2022	0.86x	3.88%	166bps
GUOLSP 3.85% ‘23	15/02/2023	0.86x	4.08%	180bps

Indicative prices as at 14 November 2018, Source: Bloomberg
Net gearing based on latest available quarter

A) Background

Since our last earnings review of OUE dated 10 September 2018, OUE and its subsidiaries had completed several material transactions. These include the acquisition of First Real Estate Investment Trust (“FIRT”)’s REIT Manager (60% by OUE Ltd and 40% by ~64.4%-owned OUE Lippo Healthcare (“OUE-LH”), a 10.6% acquisition of FIRT by OUE-LH, selling the office components of OUE Downtown to 56%-owned OUE Commercial Trust (“OUE-CT”). We have resumed coverage of OUE on 5 November 2018 and have assessed the impact of these transactions along with its recently announced 3Q2018 in forming our view of OUE’s issuer profile.

Figure 2: Key Events and Parties Involved

Buyer / Investor	Seller / Issuer	Key Event
OUE-CT	An indirect wholly-owned subsidiary of OUE	11 September 2018: <ul style="list-style-type: none"> OUE announces the proposed sale of office components of OUE Downtown building to OUE-CT for SGD908mn OUE-CT would be part funding this via a ~SGD587.5mn rights issue
OUE	An indirect wholly-owned subsidiary of PT Lippo Karawaci	18 September 2018: <ul style="list-style-type: none"> OUE proposes to buy 60%-stake in FIRT’s REIT Manager for SGD59.3mn

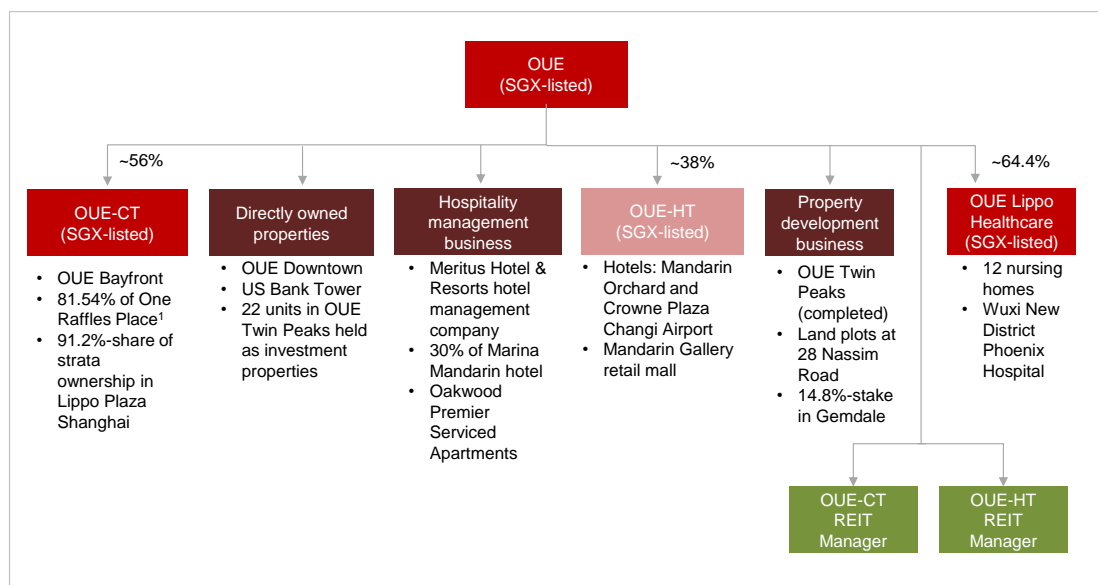
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	Tbk ("LK")	
OUE-LH and an indirect wholly-owned subsidiary of OUE-LH	LK	<p>18 September 2018:</p> <ul style="list-style-type: none"> OUE-LH proposes to buy 40%-stake in FIRT's REIT Manager for SGD39.6mn OUE-LH proposes to buy 10.6%-stake in FIRT for SGD102.7mn OUE-LH would be funding this purchase via a rights issue to raise ~SGD150mn Remaining gross proceeds to fund general corporate/working capital and transaction costs and fees
PT Megafeat Internasional Indonesia and Mr. Mas Agoes Ismail Ning	Indirect wholly-owned subsidiaries of OUE	<p>25 September 2018:</p> <ul style="list-style-type: none"> Sale of OUE-owned PT Alpha Sentra Prima group of companies reaches legal completion Proposed transaction was first announced in March 2018. OUE Beta (a wholly-owned subsidiary of OUE) had extended ~SGD228.9mn in shareholder loans to PT Alpha. With the sale, PT Alpha's obligation to OUE Beta has been novated to the buyer Rather than paying cash upfront to cancel out this obligation, the buyer has issued a promissory note to OUE Beta OUE Beta is a creditor to buyer and the promissory notes have been recorded as a current asset on OUE's 3Q2018 balance sheet
An indirect partly-owned subsidiary of OUE	PT Asiatower Sudirman	<p>25 September 2018:</p> <ul style="list-style-type: none"> Enters into conditional agreement to buy land in the central business district of South Jakarta for ~SGD150mn Proposed deal is a non-cash deal, with consideration to be paid via the assignment of a promissory note held by buyer to PT Asiatower Sudirman. In a nutshell, an asset held on OUE's balance sheet will be transferred to seller
Existing shareholders (including a wholly-owned subsidiary of OUE) and underwriter	OUE-LH	<p>17 October 2018</p> <ul style="list-style-type: none"> OUE-LH rights issue closes, 94.1% taken up (including from excess applications) Underwriter takes up remaining rights Gross proceeds of SGD150mn in equity raised
Existing shareholders (including wholly-owned subsidiaries of OUE)	OUE-CT	<p>23 October 2017</p> <ul style="list-style-type: none"> OUE-CT rights issue closes, 108.5% taken up (including from excess applications) Gross proceeds of SGD587.5mn in equity raised
		<p>26 October 2018</p> <ul style="list-style-type: none"> OUE and OUE-LH completes acquisition of FIRT REIT Manager Wholly-owned subsidiary of OUE-LH completes acquisition of 10.6% stake in FIRT
		<p>1 November 2018</p> <ul style="list-style-type: none"> Completion of the sale of office components of OUE Downtown building to OUE-CT

Source: Company filings, OCBC Credit Research

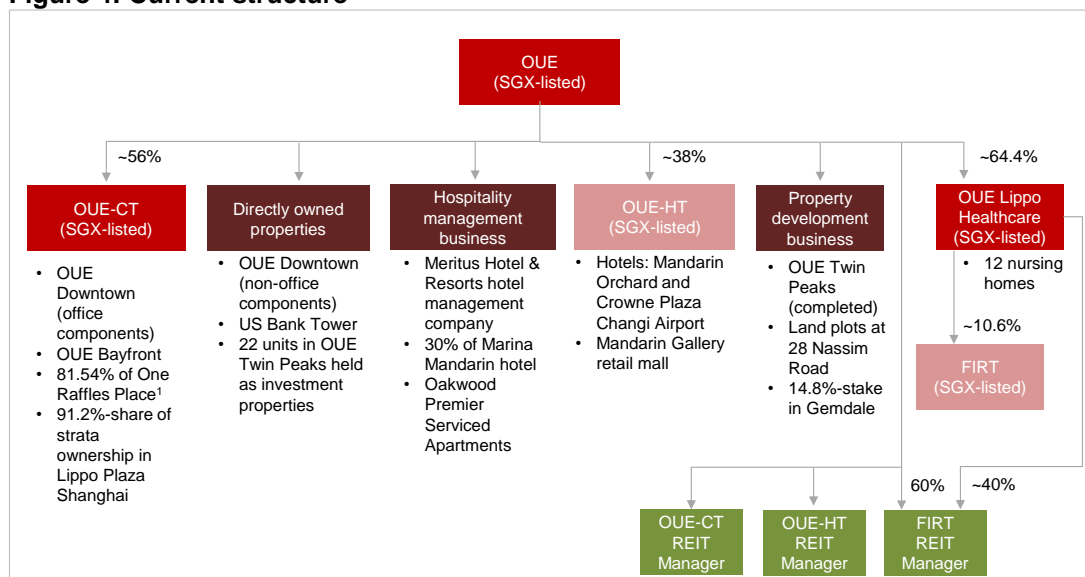
B) Simplified corporate structure

Figure 3: Previous structure



Note: (1) Remaining ~18% of One Raffles Place owned by UOB, a third party
 Source: Company fillings, Bloomberg, OCBC Credit Research

Figure 4: Current structure



Note: (1) Remaining ~18% of One Raffles Place owned by UOB, a third party
 (2) Wuxi New District Phoenix Hospital has been deconsolidated
 Source: Company fillings, Bloomberg, OCBC Credit Research

C) Recent performance and outlook

Profitability in 3Q2018 had declined: OUE's 3Q2018 revenue was relatively flat y/y at SGD183.3mn. Its Development and Hospitality segments saw revenue growth which helped offset declines in Healthcare (from 64.4%-owned OUE Lippo Healthcare Limited ("OUE-LH"), dividend income and others. Investment properties income was relatively flat. Revenue from Development had increased 13% y/y to SGD43.6mn following transaction completion of some properties at OUE Twin Peaks (earlier sold under the deferred payment scheme). Hospitality income grew 6% y/y to SGD61.8mn, driven by the ramp up of the Oakwood Serviced Apartments which opened in June 2017. Despite a flat gross profit, EBITDA (based on our calculation which does not include other income and other expenses) was

SGD52.8mn (up 27% y/y) following the declines in overheads. EBITDA/Interest was thus higher at 1.5x (3Q2017: 1.2x). OUE ended the quarter with net profit of only SGD7.4mn (3Q2017: SGD18.4mn) as it had recognised SGD13.4mn in other losses (mainly due to mark-to-market losses on mutual fund investments). OUE also recorded other comprehensive loss of SGD97.5mn during the quarter (we think from decline of value in Gemdale), albeit this is a non-cash item, book value of equity had narrowed by 2% q/q to SGD4.8bn from SGD4.9bn as at 30 June 2018.

Office components of OUE Downtown monetized: On 1 November 2018, OUE had completed the sale of the office components of OUE Downtown to OUE-CT for SGD908mn. Total acquisition cost borne by OUE-CT was SGD955.9mn, including acquisition fees and transaction costs. OUE Downtown is an iconic commercial property at Shenton Way, Singapore. SGD587.5mn (or 61.5% of total acquisition cost) was equity funded via a rights issue, with OUE-CT taking up additional debt for the funding. On a per sq ft basis factoring in rental support provided by OUE to OUE-CT of SGD60mn costs OUE-CT SGD1,713 per sq ft, 3.0% lower than the average of two independent valuation as at 30 June 2018. SGD1,713 per sq ft is relatively flat against the average of two independent valuation without factoring rental support. While OUE would continue to consolidate OUE Downtown, given its majority ownership in OUE-CT, SGD bondholders at OUE would now be structurally subordinated to debtholders at OUE-CT with regards to OUE Downtown's office components. OUE Downtown office components makes up 56.2% of the value of OUE Downtown (whole building together with Oakwood Premier Serviced Apartment and retail components was valued at SGD1.59bn in end-2017). In our view, this is less of a credit concern given that OUE-CT as a Singapore listed REIT is subject to an aggregate leverage cap of 45% which limits the amount of debt that can be taken up by OUE-CT. Carving out OUE-CT, OUE had also received SGD579.6mn in cash, net of the amounts it had subscribed in the OUE-CT equity rights issue. OUE had taken up its pro-rata portion, keeping its shareholding at OUE-CT intact at ~56%. As at 30 September 2018, OUE-CT's aggregate leverage was at 41.4%, while on a pro-forma basis, factoring the rights issue and purchase, this is expected at 40.4%. While higher than REIT peers, this leave ~SGD2.7bn of asset coverage to its equity holders such as OUE.

Changing nature of OUE Lippo Healthcare: Healthcare revenue at OUE-LH is historically attributable to its 12 nursing homes in Japan and Wuxi New District Phoenix Hospital Co., Ltd ("Wuxi") (owns the license and operates a 163-bed hospital in Wuxi, China). In 3Q2018, revenue from Healthcare declined 57% y/y to only SGD4.9mn following the deconsolidation of Wuxi as OUE-LH deemed that it has lost control over Wuxi. On a standalone basis, OUE-LH had reported a loss after tax of SGD4.9mn in 3Q2018 widening from a loss after tax of SGD3.7mn in 3Q2017. OUE-LH's subsidiaries are subject to various litigations, including those brought about by Weixin Hospital Investment Management (Shanghai) Co. Ltd ("Weixin"), claiming Weixin is the rightful owner of Wuxi, instead of OUE-LH's subsidiaries. This stems from business dealings prior to OUE buying a stake in OUE-LH in early-2017 as related litigations over Wuxi's ownership had occurred as early as 2014. OUE-LH was a distressed acquisition. The medical equipment, land and building for the Wuxi hospital is held by another of OUE-LH's subsidiary though Weixin has commenced legal proceedings seeking to declare the land transfer to this other subsidiary as void. In 3Q2018, rental income from the Japan nursing home business remains stable and we only take investment property value from these nursing homes (end-2017: SGD287.8mn) into our issuer profile assessment. On 26 October 2018, OUE and OUE-LH had bought a 60% and 40%-stake respectively in the [REIT Manager of FIRT](#). With OUE-LH also buying a 10.6% in FIRT itself. The funding for the purchases was from a ~SGD150mn rights issue, of which OUE had taken its full pro-rata share amounting to ~SGD96.6mn.

Increased links with Indonesia: We estimate that OUE's sister company PT Lippo Karawaci Tbk ("LK") had received SGD202mn from the sale of its stake in FIRT and FIRT REIT Manager from OUE and OUE-LH. Given that OUE's two other REIT Managers provides stable and recurring income, we acknowledge the business reasons for OUE in buying over FIRT REIT Manager. In our view though, as long as FIRT structurally still faces LK and its subsidiaries as main tenant (~82% of revenue in 2017), the counterparty credit risk to this income stream is high. Additionally, given OUE's control over the REIT Manager, we think it would be considered par for course for OUE and/or OUE-LH to provide a corporate guarantee on FIRT's upcoming refinancing needs (if not outright shareholder's loan). Net-net, we are not factoring in a credit uplift from the investments into FIRT/FIRT REIT Manager, rather we view the short-term debt at FIRT (SGD109.8mn as at 30

September 2018) as a contingent liability for OUE. On 25 September 2018, OUE had entered into a conditional agreement to buy land in the central business district of South Jakarta for ~SGD150mn where consideration is non-cash, though a promissory note (an asset of OUE) would be assigned to the seller upon deal completion. LK still holds a ~10.7%-stake in FIRT with a market value of SGD98.7mn and there is a possibility that it will monetize this stake down the road. In our view, OUE/OUE-LH is the most natural buyer in our view.

Unadjusted net gearing to decline: As at 30 September 2018, OUE's net gearing on a consolidated basis was 0.68x, marginally higher than 0.67x as at 30 June 2018. On a proforma basis, we estimate that net gearing at OUE would decline to ~0.62x given that OUE-CT's purchase of the office component of OUE Downtown was 61% equity-funded while OUE-LH's purchases were fully equity funded. We expect minority investor's contribution to book value equity to be higher going forward though (23% against 18% as at 30 September 2018) since OUE had received cash from the sale of office components of OUE Downtown to OUE-CT. ~44% of OUE-CT is owned by minority investors. Barring any new purchases, debt repayment or dividend payments, we also expect OUE's cash balance to be higher at ~SGD809mn (30 September 2018: SGD386.7mn).

Figure 5: Preliminary asset coverage analysis for debt holders:

Item	SGDmn
Market value of OUE-CT stake	752
Market value of OUE-HT stake	466
Nursing homes owned by OUE-LH ¹	288
US Bank Tower, Los Angeles	816
Non-office components of OUE Downtown (Oakwood Premier serviced apartments and retail gallery)	708
30%-stake in Marina Mandarin Singapore hotel	224
Market value of Gemdale stake	315
Other investments (largely from mutual fund investments)	171
Assumed amounts to be collected from OUE TwinPeaks sold under deferred payment schemes	355
22 units of OUE TwinPeaks held as investment properties	60
28 Nassim Road plots of land	66
Cash	776
Total	4,997
(-) Proforma gross debt (excluding debt at OUE-CT but including debt at OUE-LH) ¹	2,268
(-) Short term debt at FIRT (we assume this is a contingent liability)	110
Asset-to-debt coverage	2.1x

Source: OCBC Credit Research estimates

Note: (1) Conservatively given that OUE-LH is still loss-making, we assume that the entity is reliant on parent company for its external financing, we take full value of its nursing homes

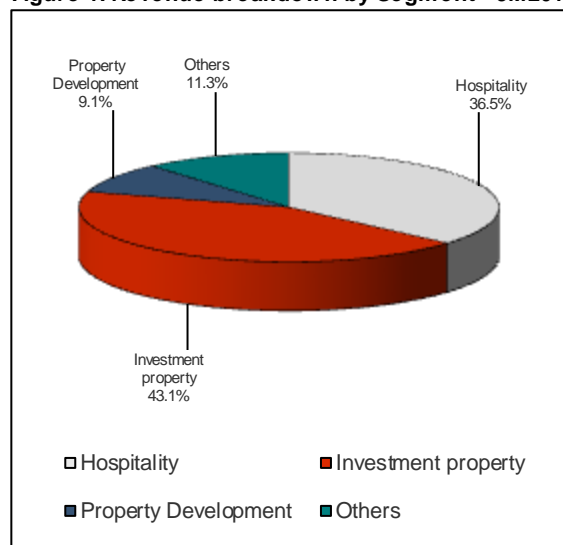
OUE Ltd

Table 1: Summary Financials

Year Ended 31st Dec	FY2016	FY2017	9M2018
Income Statement (SGD'mn)			
Revenue	884.2	754.1	479.6
EBITDA	225.0	163.9	152.2
EBIT	220.5	156.1	146.1
Gross interest expense	127.8	130.9	108.2
Profit Before Tax	212.6	193.7	48.4
Net profit	177.1	161.2	28.3
Balance Sheet (SGD'mn)			
Cash and bank deposits	239.0	535.2	386.7
Total assets	8,083.4	9,034.1	9,094.2
Short term debt	656.0	1,081.8	772.6
Gross debt	2,901.5	3,480.9	3,654.6
Net debt	2,662.5	2,945.7	3,267.9
Shareholders' equity	4,643.8	4,875.7	4,824.3
Cash Flow (SGD'mn)			
CFO	466.2	249.2	93.2
Capex	2.2	10.5	4.2
Acquisitions	254.5	234.7	696.8
Disposals	236.3	39.0	311.7
Dividend	73.8	59.9	64.9
Interest paid	107.6	124.7	81.9
Free Cash Flow (FCF)	464.0	238.7	89.0
Key Ratios			
EBITDA margin (%)	25.4	21.7	31.7
Net margin (%)	20.0	21.4	5.9
Gross debt to EBITDA (x)	12.9	21.2	18.0
Net debt to EBITDA (x)	11.8	18.0	16.1
Gross Debt to Equity (x)	0.62	0.71	0.76
Net Debt to Equity (x)	0.57	0.60	0.68
Gross debt/total assets (x)	0.36	0.39	0.40
Net debt/total assets (x)	0.33	0.33	0.36
Cash/current borrowings (x)	0.4	0.5	0.5
EBITDA/Total Interest (x)	1.8	1.3	1.4

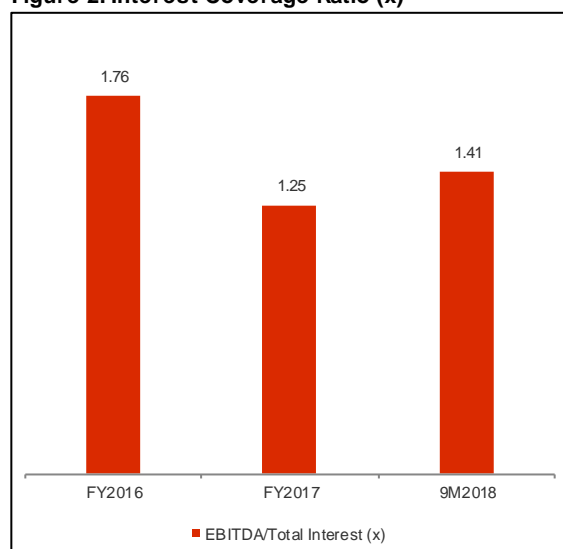
Source: Company, OCBC estimates

Figure 1: Revenue breakdown by Segment - 9M2018



Source: Company

Figure 2: Interest Coverage Ratio (x)



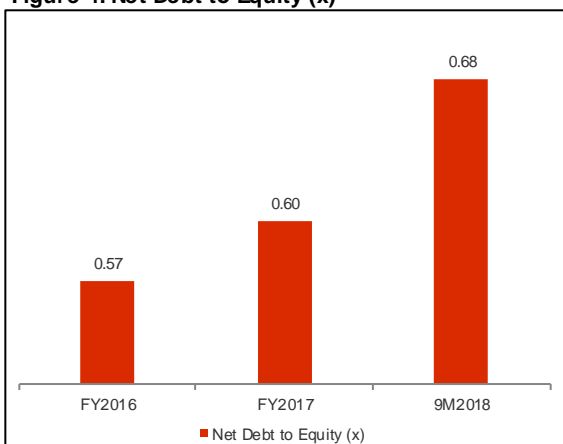
Source: Company

Figure 3: Debt Maturity Profile

Amounts in (SGD'mn)	As at 30/9/2018	% of debt
Amount repayable in one year or less, or on demand		
Secured	742.5	20.3%
Unsecured	30.1	0.8%
	772.6	21.1%
Amount repayable after a year		
Secured	1,037.4	28.4%
Unsecured	1,844.6	50.5%
	2,882.0	78.9%
Total	3,654.6	100.0%

Source: Company, OCBC estimates

Figure 4: Net Debt to Equity (x)



Source: Company

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Positive (“Pos”) – The issuer’s credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral (“N”) – The issuer’s credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative (“Neg”) – The issuer’s credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings (“IPR”) into a 7 point Issuer Profile Score (“IPS”) scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight (“OW”) – The performance of the issuer’s specific bond is expected to outperform the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral (“N”) – The performance of the issuer’s specific bond is expected to perform in line with the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight (“UW”) – The performance of the issuer’s specific bond is expected to underperform the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal (“WD”) – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

Analyst Declaration

The analyst(s) who wrote this report and/or her or his respective connected persons did not hold securities in the above-mentioned issuer or company as at the time of the publication of this report.

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