Asia Credit Research

Oxley Holdings Ltd: Credit Update

Wednesday, 14 February 2018

Going all in on Singapore properties

- Following the completion of OCBC's engagement, we resume coverage on Oxley Holdings Ltd ("OHL") with an **Issuer Profile of Negative (6)**.
- Credit metrics are expected to be significantly stretched in the near-term as OHL will need to settle the numerous acquisitions and collective sales. The recent bond issuance provides some liquidity buffer, though ultimately OHL's credit profile in the longer term will hinge on the sales performance of the upcoming launches and management's commitment (if any) to deleverage.
- Given the very aggressive profile and high asset encumbrance, **we rate the recent OHLSP 5.7% '22s with an Underweight recommendation as we see fair value around 6.15%.**

S&P: Not rated

Moody's: Not rated

Fitch: Not rated

Ticker: OHLSP

Background: Oxley Holdings Ltd ("OHL") is a property developer listed on the SGX in Oct 2010. Beginning with a portfolio of development projects in Singapore, OHL has expanded to overseas projects in the UK, Malaysia, Ireland, China, Cambodia, Myanmar and Indonesia. OHL is also building a pipeline of investment and hospitality properties. OHL's key shareholders are its CEO Mr Ching Chiat Kwong (42.7%-stake), its deputy CEO Mr Low See Ching (28.7%) and Mr Tee (12.1%) who appears to be a passive shareholder.

Discussions on net gearing, potential use of proceeds and liquidity

Net gearing to surge due to acquisitions: We expect net gearing to peak at ~2.9x (2QFY2018: 1.9x) in 4QFY2018 (ending Jun 18) pending settlement of acquisitions, including:

- SGD575mn acquisition (35%-stake) of Rio Casa (refer to OCBC Asian Credit Daily – 26 May 2017)
- SGD499mn acquisition (40%-stake) of Serangoon Ville (refer to OCBC Asian Credit Daily – 27 Jul 2017)
- SGD311mn acquisition (100%-stake) of Mayfair Gardens (refer to OCBC Asian Credit Daily – 20 Nov 2017)
- SGD121mn acquisition (100%-stake) of Pasir Panjang (refer to OCBC Asian Credit Daily – 13 Jul 2017)
- SGD660mn acquisition (100%-stake) of Chevron House (refer to OCBC Asian Credit Daily – 14 Dec 2017)
- SGD418mn acquisition (100%-stake) of Vista Park (refer to OCBC Asian Credit Daily – 15 Dec 2017)

The cash outflows should be partly mitigated over time by the handover of keys from projects (e.g. Royal Wharf), which should deliver SGD1.1bn cash proceeds over the next 12 months (and hence OHL may begin to deleverage after 30 Jun 2018). Thereafter, we recognise that OHL has the potential to de-lever further, if management chooses to, given the significant amount of unbilled progress billings (SGD1.8bn in total inclusive of Royal Wharf).

Proceeds from bond issuance to act as buffer: According to OHL, there is no immediate use of proceeds from the bond issuance. In case sales and cash receipts take a longer time than anticipated, the proceeds would provide a buffer for OHL's liquidity needs. The bond has a 4Y tenor, which coincides with the expected TOP of the various Singapore developments from the acquisitions (likely around 2021-22). Separately, OHL mentioned financing has been obtained for all acquisitions except for Vista Park (SGD418mn purchase cost). Cash on hand of SGD272.2mn is insufficient, though OHL expects this to be funded through bank loans eventually. OHL has also mentioned the possibility to monetise Novotel / Mercure Singapore (indicative valuation: SGD886mn).

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Key credit considerations

- **Decent 2QFY2018 results:** 2QFY2018 results for the quarter ending 31 Dec 2017 remains decent though weaker on a y/y basis. Revenue declined 33% y/y to SGD406.1mn mainly due to the absence of recognition of revenue from Oxley Tower (completed in 2QFY2017). Revenue in 2QFY2018 comprised the handover of plots in The Royal Wharf Phase 1A and 1B and recognition of revenue from The Rise @ Oxley-Residences, rental income and hotel operations. Due to the change in revenue mix, gross profit declined by a larger 66% y/y to SGD68.8mn. Net profit declined by 45% y/y to SGD68.2mn, which is smaller than the decline in gross profit due to contribution from equity-accounted associates and JVs of SGD60.6mn (2QFY2017: losses of SGD4.5mn) from 20%-owned Galliard (UK developer) and 50%-owned The Bridge (Cambodia development project). However, other losses deepened to SGD16.7mn (2QFY2017: loss of SGD6.1mn) mainly due to fair value loss of SGD16.9mn from the marked-to-market position of financial instrument.

- **Earnings and cashflow visibility from significant amount of unbilled contracts:** The projects, which will obtain TOP in the next 12 months, have an unbilled contract value of SGD1.13bn, of which SGD0.88bn is related to the Royal Wharf project (Phase 1A, 1B, 2). The dropout rate at Royal Wharf has been minimal as many buyers are owner-occupiers. We understand from management that prices have risen significantly and a 20% non-refundable deposit is required, hence buyers are unlikely to walk out. In the near-term, OHL will also handover units to buyers at The Bridge and The Peak in Cambodia. The total unbilled value across all projects stands at SGD1.8bn as of 2QFY2018.

- **Raising huge stakes in Singapore property:** OHL returned to Singapore in a big way through a number of en-bloc acquisitions. Several of the purchased prices look reasonable compared to other developers, for example Serangoon Ville's SGD835 psf ppr is lower than a nearby land site (along Serangoon North Ave 1) bought by Keppel-WingTai JV for SGD965 psf ppr. Rio Casa's SGD669 psf ppr also looks cheap compared to Florence Agency's SGD842 psf ppr purchased by Logan Property. In total, OHL's landbank in Singapore has reached 3,800 units with an estimated gross development value of SGD5bn. In the commercial space, OHL has acquired Chevron House for SGD660mn and purchased a 15%-stake in United Engineers for SGD255mn.

Acquisitions in Singapore

Project	Stake	Purchase Price	Launch Date
Rio Casa	40%	SGD575mn	2Q2018
Serangoon Ville	35%	SGD499mn	2Q2018
Vista Park	100%	SGD418mn	3Q2018
Mayfair Gardens	100%	SGD311mn	2Q2018-3Q2018
Lotus @ Pasir Panjang	100%	SGD121mn	1Q2018
1,3,5,7,9,7A,9A,11 Balestier Road	100%	SGD38mn	TBC
21 Meyappa Chettair Road	100%	SGD22mn	2Q2018
3 Tessensohn Road	100%	SGD14.5mn	3Q2018
16 Lorong 35 Geylang	100%	SGD13.0mn	TBC
494 Upper East Coast Road	100%	SGD10.5mn	1Q2018
208 Yio Chu Kang Road	100%	SGD8.4mn	1Q2018
Chevron House	100%	SGD660mn	N/A
United Engineers	15%	SGD255mn	N/A

Indicative prices as at 12 February 2018
Source: Bloomberg

- **Expanding the investment and hospitality portfolio:** In FY2017, investment properties generated only SGD10.9mn rental income but OHL expects this to grow to above SGD13mn after FY2019. National Treasury Management Agency in Ireland will take up 13,395 sqm in Dublin Landings and begin to move in by summer 2018. Novotel / Mercure Singapore on Stevens (GDV: SGD980mn) has opened in Oct 2017, which OHL expects to generate SGD46mn recurring profit based on 88% occupancy, while 11 commercial units at the same site will contribute SGD2.1m p.a. In Malaysia, OHL is building Jumeirah Kuala Lumpur Hotel and Jumeirah Living Kuala Lumpur Residences. By FY2021, OHL expects the hospitality portfolio to deliver SGD153.5mn p.a. income.

View on the recent OHLSP 5.7% '22s

The recent SGD150mn 4-year issue was priced at 5.7% on 24th Jan, tightening from an initial price guidance of 5.75% on the back of SGD200mn orderbook.

We see the fair value around 6.15%, by comparing with OHLSP 5.15% '20s (retail tranche) and OHLSP 6.375% '21s (USD issue). We work off the mid YTM of OHLSP 5.15% '20s (5.15%) given the wide bid-ask spread. Swapping OHLSP '21s (USD) into SGD, we derive 5.72% YTM. Extrapolating the 40bps credit spread difference between OHLSP '20s and '21s, we derive a required 414bps credit spread (~6.15%) for OHLSP 5.7% '22s.

There is no other close comparable given OHL's expansionistic stance. However, we note that amongst the Singapore developers with higher net gearing (aside from OHL), the bonds yields range between 4%-6%. As such, we think it is reasonable for the OHLSP curve to trade at a yield beyond 6% due to its elevated net gearing levels.

Outside the property developer sector, investors chasing after yield can consider switching to LMRTSP 7% PERP (Overweight) and LMRTSP 6.6% PERP (Overweight) for a similar yield. We rate Lippo Malls Indonesia Retail Trust ("LMRT") at Neutral (5) (refer to Singapore Credit Outlook 2018). Though not closely comparable as these are perpetuals while OHLSP 5.7% '22s is a straight bond, we prefer the LMRTSP perpetuals as LMRT has far healthier net gearing, recurring income and we perceive a high certainty that the perpetuals will be called.

Relative Value:

Issue	Maturity/ First Call	Net gearing	Ask YTW	I-Spread
OHLSP 5.7% 2022	31-Jan-22	1.87x (Forecast: 2.9x)	5.76%	376.1
OHLSP 5.15% 2020	18-May-20	1.87x (Forecast: 2.9x)	5.08% (mid)	341.0
OHLSP 6.375% 2021 (USD)	21-Apr-21	1.87x (Forecast: 2.9x)	5.72% (SGD)	381.1
LMRTSP 7% PERP	27-Sep-21	0.53x	5.64%	367.8
LMRTSP 6.6% PERP	29-Dec-22	0.53x	5.85%	370.6

Indicative prices as at 13 February 2018
Source: Bloomberg

Separately, we acknowledge that OHL has a great track record, with the OHL management selling shoe-box units in Singapore in the earlier days (before the cooling of Singapore property market), then moving to UK property market (before Brexit hits) and coming back to Singapore while the property market is in the early stages of the up-cycle. The equity market has rewarded OHL richly with a P/B ratio of 1.8x – seldom seen for Singapore developers. However, we think it is reasonable for OHLSP 5.7% '22s to provide closer to equity-like returns given (1) the high net gearing levels, (2) a very substantial portion of assets are likely to be encumbered given that SGD1.5bn of debt is secured (out of SGD2.5bn borrowings) and (3) pending sales performance of the upcoming launches in Singapore. That said, barring any unforeseen deterioration in the Singapore economy and property market, we see the potential for OHL's credit to improve (which may lift bond prices) as OHL has obtained land bank at a reasonable cost compared to its peers, which may allow OHL room (e.g. cut prices) to monetise development units more quickly.

Oxley Holdings Limited

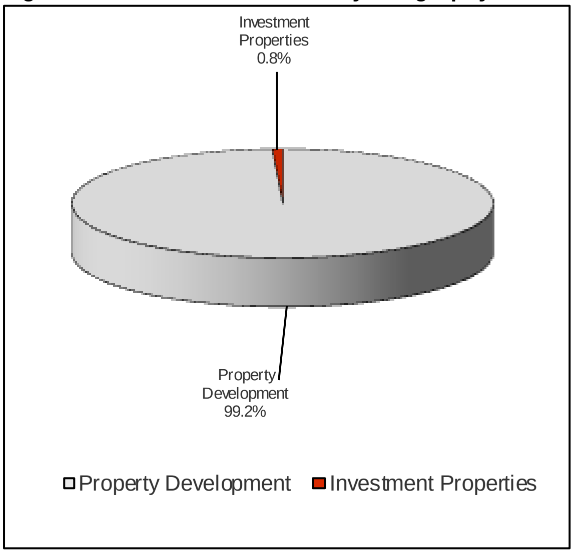
Table 1: Summary Financials

Year Ended 30th Jun	FY2016	FY2017	1H2018
Income Statement (SGD'mn)			
Revenue	981.4	1,343.0	716.7
EBITDA	252.0	333.3	96.3
EBIT	251.5	332.6	92.9
Gross interest expense	131.9	131.5	24.7
Profit Before Tax	363.4	299.5	138.7
Net profit	206.0	218.1	116.8
Balance Sheet (SGD'mn)			
Cash and bank deposits	551.3	413.5	272.2
Total assets	4,732.5	4,607.9	4,747.5
Gross debt	2,633.4	2,458.0	2,533.4
Net debt	2,082.2	2,044.4	2,261.3
Shareholders' equity	965.2	1,088.9	1,214.1
Total capitalization	3,598.6	3,546.9	3,747.6
Net capitalization	3,047.4	3,133.3	3,475.4
Cash Flow (SGD'mn)			
Funds from operations (FFO)	206.5	218.8	120.2
* CFO	196.6	361.1	240.3
Capex	33.0	124.3	99.0
Acquisitions	153.6	92.2	3.0
Disposals	29.1	3.3	5.6
Dividend	80.3	176.9	69.7
Free Cash Flow (FCF)	163.6	236.8	141.3
* FCF Adjusted	-41.1	-29.0	74.2
Key Ratios			
EBITDA margin (%)	25.7	24.8	13.4
Net margin (%)	21.0	16.2	16.3
Gross debt to EBITDA (x)	10.4	7.4	6.6
Net debt to EBITDA (x)	8.3	6.1	5.9
Gross Debt to Equity (x)	2.73	2.26	2.09
Net Debt to Equity (x)	2.16	1.88	1.86
Gross debt/total capitalisation (%)	73.2	69.3	67.6
Net debt/net capitalisation (%)	68.3	65.2	65.1
Cash/current borrowings (x)	0.4	0.7	1.1
EBITDA/Total Interest (x)	1.9	2.5	3.9

Source: Company, OCBC estimates

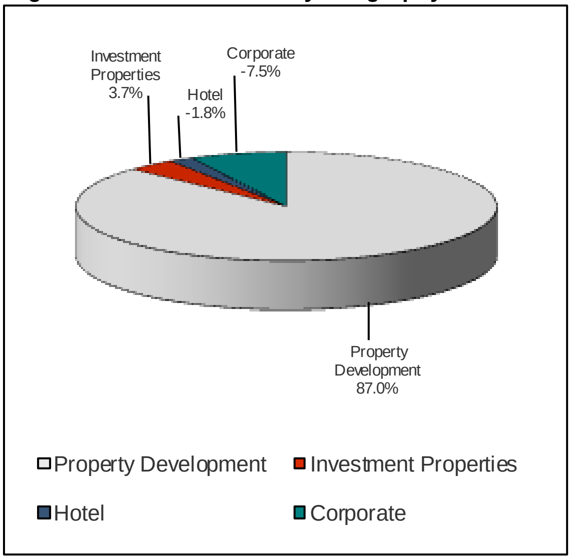
**FCF Adjusted = FCF - Acquisitions - Dividends + Disposals | *CFO after deducting interest expense*

Figure 1: Revenue breakdown by Geography - FY2017



Source: Company

Figure 2: PBT breakdown by Geography - FY2017



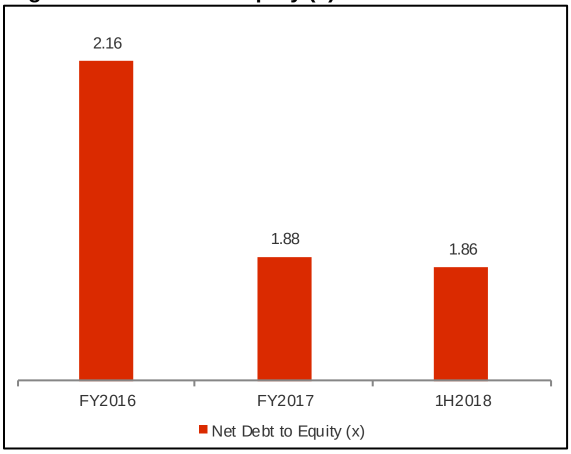
Source: Company| Hotel and Corporate made losses before tax

Figure 3: Debt Maturity Profile

Amounts in (SGD'mn)	As at 31/12/2017	% of debt
Amount repayable in one year or less, or on demand		
Secured	184.0	7.3%
Unsecured	84.0	3.3%
	268.0	**10.6%**
Amount repayable after a year		
Secured	1,323.7	52.2%
Unsecured	941.8	37.2%
	2,265.5	**89.4%**
Total	**2,533.4**	**100.0%**

Source: Company, OCBC estimates

Figure 4: Net Debt to Equity (x)



Source: Company

Explanation of Issuer Profile Rating / Issuer Profile Score

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 into a 7 point Issuer Profile Score 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.