Asia Credit Research

Earnings Review: BreadTalk Group Ltd ("BGL")

Issuer Profile: Neutral (5)

Ticker: **BREAD**

Background

Listed on the SGX in 2003, BreadTalk Group Ltd ("BGL") is a household F&B brand owner. BGL has expanded beyond Singapore and currently operates 930 outlets in China, Singapore, Thailand and other parts of Asia and Middle East. BGL classifies its businesses into Bakery, Food Atrium and Restaurants, with prominent brands including BreadTalk, Toast Box and Food Republic. BGL also operates Din Tai Fung ("DTF") as a franchisee. The company is majority owned by founders George Quek (34.0%) and Katherine Lee (18.6%).

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Recommendation

- Results are decent with reported EBITDA from core segments of Bakery, Food Atrium and Restaurants up 5.0% y/y to SGD20.9mn. Food Atrium is the key driver this quarter, with higher revenue from net new openings while EBITDA margin for the segment improved considerably (+5.5 ppts to 25.6%) due to decline in stall vacancy rates.
- Liquidity is ample with SGD185.0mn of cash sufficient to cover SGD97.8mn of current debt and bonds outstanding. Net gearing and net debt/reported EBITDA are also healthy at 26% and 0.52x respectively though we think debt levels may rise as BGL is guiding for higher capex.
- Overall, we think BREAD '23s are trading fair. That said, it does provide some yield pickup over FCTSP 2.77% '24s and CAPITA 3.2115% '23s which are similarly exposed to the retail sector. BREAD also offers higher yields than FNNSP '22s for exposure to the F&B sector.

Relative Value:

Bond	Maturity/Call date	Net gearing	Ask Yield	Spread
BREAD 4% '23s	17/01/2023	0.26x	4.00%	191bps
CAPITA 3.2115% '23s	09/11/2023	0.44x	2.88%	82bps
FCTSP 2.77% '24s	08/11/2024	0.41x	3.23%	98bps
FNNSP 3.09% '22s	23/03/2022	0.10x	3.32%	132bps

Indicative prices as at 28 Feb 2018 Source: Bloomberg, OCBC, Company
Net gearing based on latest available quarter

Key Considerations

- **Decent results though underlying trends look mixed…:** BGL reported 4Q2018 results. Revenue rose 3.1% y/y to SGD154.8mn with higher contribution from Food Atrium (+7.5% y/y to SGD39.7mn) and Restaurant (+9.8% y/y to SGD39.5mn) though Bakery segment saw a decline (-5.3% y /y to SGD70.0mn).
  - i) **Bakery not yet seeing light at the end of the tunnel:** Revenue fell likely due to lower revenue from direct operated stores with store count decreasing y/y from 240 to 221, though this is partly mitigated by increase of franchise outlets which increased from 631 to 642.
  - ii) **Food Atrium:** Revenue grew with net opening of 2 new food atriums (Opened 1 in Shenzhen, 1 in Hong Kong, 1 in Cambodia and closed 1 outlet in Hangzhou). In addition, BGL has opened 3 Direct Operated Restaurants (in total, BGL now operates 5 of such restaurants) under the "Sergeant Kitchen" brand.
  - iii) **Restaurant:** Revenue grew with net addition of 3 outlets (opened 1 in Singapore, 2 in Thailand, 1 in UK though 1 outlet was closed in Singapore.

- **… with Food Atrium as the outperformer and largest EBITDA contributor:** Reported EBITDA from core segments (Bakery, Food Atrium, Restaurant) increased 5.0% y/y to SGD20.9mn, mainly due to the outperformance in Food Atrium (36.6% y/y to SGD10.1mn) due to growth in revenue (e.g. in Beijing) while EBITDA margin improved 5.5ppts to 25.6% with decline in stall vacancy rates with pro-activate management of tenants. Bakery also delivered 60.3% y/y growth to SGD6.9mn though this is merely a partial rebound when compared to 4Q2016 (SGD7.6mn). We understand that bakery in Singapore is doing well though China has been underperforming. Meanwhile, Restaurant EBITDA fell 23.4% y/y to SGD6.0mn due to higher staff and administrative costs as a result of opening of Din Tai Fung outlet in the UK.

- **Deploying the cash pile:** BGL holds SGD185.0mn of cash, which exceeds current debt and bonds outstanding of SGD97.8mn. That said, we could see BGL deploying the cash, noting capex has been ramped up significantly with

SGD23.1mn spent just in 4Q2018 which is mainly for the UK expansion. BGL is guiding for higher capex of SGD45mn-SGD55mn in 2019, due to increased store openings and relocation of factories from Shanghai to another part of China to better support franchises and rationalise costs. In addition, cash is needed as working capital for the new outlets.

- **Changes in accounting:** BGL highlighted that changes due to SFRS(I) 16 will frontload expenses, which should impact new leases more than old leases. We also note that previously in 1Q2018, there was a huge increase in investment securities (+SGD51.7mn to SGD123.8mn) due to the restatement upon adoption of SFRS(I) 9. However, the restatements appear to have been reversed in 4Q2018 which resulted in total equity falling to SGD162.7mn (3Q2018: SGD213.0mn).

- **Still healthy credit metrics, for now:** Net gearing increased q/q to 26% (3Q2018: 20%) though this is mainly due to changes in accounting. Meanwhile, net debt/reported EBITDA is healthy at 0.52x with reported EBITDA/Interest Expense at 8.7x. Crucially, BGL's businesses are highly cashflow generative, with SGD65.6mn of net cash from operating activities in 2018. That said, with capex on the rise and potential for BGL to expand aggressively, we continue to hold BGL at a Neutral (5) Issuer Profile.

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Explanation of Issuer Profile Rating ("IPR") / Issuer Profile Score ("IPS")

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 financial interests in the above-mentioned issuer or company as at the time of the publication of this report.

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