OCBC Bank

Issuer Profile:
Neutral (5)

Ticker:
PREHSP

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Perennial Real Estate Holdings Ltd ("PREH")

Recommendation

- **Following a weak 1Q2019, 2Q2019 results remains lackluster with PBIT (before other income and share of results of associates/JVs) at a mere SGD0.7mn. We think weak results may persist through 2H2019 as Capitol Singapore and Perennial International Health and Medical Hub have yet to stabilize.**
- **Divestments will be required to tackle the upcoming bonds due in 2020 totaling SGD560mn. We think several assets (e.g. AXA Tower) can be divested to fund the bond redemptions though there have not been concrete plans announced.**
- **Credit metrics remains somewhat weak due to lackluster results and somewhat high net gearing of 75.9%. We expect the CNY volatility post 2Q2019 to continue impacting the balance sheet given that PREH is insufficiently hedged on FX.**
- **Without announced plans that are concrete on raising liquidity, we prefer to switch out from PREHSP 3.85% '20s, PREHSP 5.95% '20s and PREHSP 3.9% '21s as they are near or above par. We prefer OHLSP 5.15% '20s and LMRTSP 4.1% '20s given higher yields and better visibility over near-term liquidity.**

Relative Value:

Bond	Maturity / Call date	Net gearing	Ask YTW	Spread
PREHSP 4.55% 2020	29/04/2020	75.9%	5.32%	373bps
PREHSP 3.85% 2020	03/07/2020	75.9%	4.07%	243bps
PREHSP 5.95% 2020	28/08/2020	75.9%	4.16%	253bps
PREHSP 3.9% 2021	12/01/2021	75.9%	4.31%	269bps
OHLSP 5.15% 2020	18/05/2020	249%	5.20%	362bps
LMRTSP 4.1% 2020	22/06/2020	53.9%	5.12%	348bps

Indicative prices as at 8 August 2019 Source: Bloomberg
Aggregate leverage based on latest available quarter

Background

- Perennial Real Estate Holdings Ltd ("PREH") is an integrated real estate owner and developer focused primarily in China (70.5% by total assets) and Singapore (28.1%).
- PREH is developing large scale mixed-use developments in railway hubs of China. PREH also holds a portfolio of stabilised office and retail assets in Singapore and China which provide rental income.
- Listed on the SGX with a market cap of SGD997.0mn, PREH is 82.4%-owned by 4 key sponsors. This includes 36.5%-stake by Mr Kuok Khoon Hong (CEO of Wilmar International Ltd), 15.5%-stake by Mr Ron Sim (CEO of V3 Group Ltd, which owns OSIM), 20%-stake by Wilmar International Ltd and 10.4%-stake by Mr Pua Seck Guan (CEO of PREH).

Key Considerations

- **Higher revenue though core results still weak:** PREH reported 2Q2019 results for the quarter ending 30 Jun. Revenue rose 52.4% y/y to SGD27.6mn, mainly due to increased revenue from Singapore (+92.8% y/y to SGD10.0mn) and China (+37.5% y/y to SGD13.0mn) while the management business (+25.3% y/y to SGD6.5mn) recorded higher fee income. For Singapore, the increase is mainly due to increased revenue contribution from Capitol Singapore, which has been consolidated since May 2018. China's increase is attributable to higher contribution from Perennial International Health and Medical Hub ("PIHMH"), which commenced operations in June 2018. Despite higher revenue contributions from Capitol Singapore and PIHMH, core results remain weak with PBIT (before other income and share of results of associates and JVs) at a mere SGD0.7mn (2Q2018: -SGD2.4mn).

- **Will the weak results persist?** Part of the reason for the weak results is due to Capitol Singapore and PIHMH not contributing yet on a stabilised basis. While not all the tenants have fully moved in, both properties have committed occupancy over 90%. Management also highlighted that Renshoutang (which PREH has 49.9%-stake) is a significantly profitable business. However, Renshoutang has minimal impact on the financial statements as its financials are not consolidated. Meanwhile, cash generated from the business has been reinvested into more beds (with committed pipeline of over 8000 beds), which incurs start-up expenses and depreciation – thereby generating minimal impact to profitability. All said, without further clarity and insufficient explicit guidance, profitability of PREH going forward remains to be seen.

- **Divestments will be needed to tackle the 2020 wall of maturity:** Management is confident to refinance the remaining SGD122mn loans due in 2019 as PREH has been in talks with lenders. However, the SGD1,074mn 2020 maturities include SGD280mn PREHSP 4.55% '20s, SGD180mn 5.95% '20s, SGD100mn 3.85% '20s, with the rest made up of loans. Assuming the loans can be eventually refinanced, PREH has mentioned divesting as part of the strategy to tackle SGD560mn of bonds though nothing is concrete yet. Previously announced, PREH has been looking to dispose (at least in part) its 31.2%-stake in AXA Tower though we note that talks of disposal have been ongoing since 3Q2017. Given the buoyant office market, we think that the delay is most likely due to PREH holding out for better prices. If we assume AXA Tower can be sold for SGD1.65bn at least (which is the asking price in 3Q2017), we estimate PREH will receive at least ~SGD250mn in net proceeds (after repaying asset level debt). Other assets we think PREH can divest include 100%-owned Perennial Qingyang Mall (31 Dec 2018 valuation: RMB1,275mn, or SGD250mn), 51%-owned Xi'an North High Speed Railway Integrated Development Plot 4 (RMB1,198mn, or SGD234.9mn) which has been reclassified to investment property and 100%-owned Perennial Jihua Mall (RMB928mn, or SGD182.0mn). If need be, we think 51.61%-owned CHIJMES (SGD334mn) can also be divested though we think PREH may intend to keep this asset.

- **Still looking to expand in China:** Management is still keen on undertaking further healthcare integrated mixed-use developments connected to high speed railway ("HSR") stations in China, following the announcements to undertake HSR integrated developments at Xi'an North, Tianjin South and Kunming South. We estimate that at least another SGD400mn capital commitment may be required for future potential HSR integrated developments, assuming PREH proceeds with Phase 2 of the investment, noting that the Perennial-led consortium is planning to invest up to USD1.2bn eventually. We note PREH holds 45% stake in the consortium.

- **Credit metrics remains somewhat weak:** Despite receiving proceeds of SGD110.3mn from the sale of Chinatown Point, net gearing remains flattish q/q at 75.9% (1Q2019: 75.5%) due to SGD87.2mn loans to associates and JVs, which we think is most likely due to the capital commitments to the announced HSR integrated developments. In addition, total equity has fallen q/q to SGD3.9bn (1Q2019: SGD4.0bn) due to SGD103.6mn comprehensive income loss driven by foreign currency loss; SGD61.0mn FX translation loss and SGD34.8mn impact on share of other comprehensive income of associate was recorded. Noting further volatility in SGDCNY post Jun-2019 driven by the trade war, we are expecting further foreign currency loss given that PREH is largely unhedged from CNY currency movements while 70.5% of the assets are in China. Profitability also remains weak with SGD0.7mn PBIT (before other income and share of results of associates and JVs) not able to cover SGD31.8mn of finance costs in 2Q2019. That said, we think PREH should be focused on deleveraging given the debt maturity in 2020.

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

Please note that Bond Recommendations are dependent on a bond's price, underlying risk free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.

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.

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