Asia Credit Research

# Earnings Review: Singapore Post Ltd ("SPOST")

**Issuer Profile: Positive (2)**

Ticker: **SPOST**

**Background**

Singapore Post Ltd ("SPOST") is the incumbent mail operator in Singapore and was granted the Public Postal License in 1992. Other business segments SPOST participates in include logistics and e-commerce solutions. Through Singapore Telecom Ltd and a few other corporations, Temasek Holdings has an indirect ownership of ~22% of SPOST. Alibaba Group Holdings is the 2nd largest shareholder with ~14% of SPOST.

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## Recommendation

- Post and Parcel and Property segments continue to abate the persistent weakness seen in eCommerce. SPOST's credit health remains intact with a net cash position of SGD52.7mn as at 31 December 2018. We continue to hold SPOST's Issuer Profile at Positive (2).
- We prefer SPOST PERP over SPOST '20s as we think that the higher ask yield and wider spread more than compensate for the longer duration. Risk of non-call for the perpetual is low in our view as it resets to 10Y SDSW + 370bps (~5.97%, based on 10Y SDSW as at 22 February 2019) at first call date.
- Compared to SingTel, also an issuer profile of Positive (2), we think SPOST curve offer good value as its bonds trade slightly wider and is relatively less geared.

## Relative Value:

| Bond | Maturity/Call date | Net Gearing | Ask Yield | Spread |
|---|---|---|---|---|
| SPOST 3.5% '20s | 30/03/2020 | net cash | 2.3% | 36bps |
| SPOST 4.25%-PERP | 02/03/2022 | net cash | 3.2% | 123bps |
| STSP 3.4875% '20s | 08/04/2020 | 0.25x | 2.3% | 33bps |
| STSP 2.58% '20s | 24/09/2020 | 0.25x | 2.5% | 48bps |
| STSP 3.24% '22s | 29/09/2022 | 0.25x | 2.8% | 77bps |

*Indicative prices as at 22 Feb 2019 Source: Bloomberg*
*Net gearing based on latest available quarter*

## Key Considerations

- **eCommerce eroded year-on-year profit growth**: SPOST reported its third quarter results for financial year ending March 2019 ("3QFY2019"). Revenue was up by 7.6% y/y to SGD441.4mn, with growth across all business segments. While this is positive news at prima facie, the wider operating losses incurred by the US businesses within the eCommerce segment wiped out the y/y gains in operating profit recorded by the other business segments and largely brought about the overall 8.5% y/y decline in profit on operating activities. Specifically, while eCommerce revenue was 8.7% higher y/y at SGD82.5mn, costs rose significantly in particular hourly costs for contracted staff to support higher volume, and resulted in compressed margins and a wider operating loss of SGD13.4mn compared to SGD4.5mn in the corresponding quarter.

- **Resilience in Post and Parcel segment**: The segment saw higher revenue (up by 9.0% y/y) and stronger operating profit (up by 10.0% y/y). Increased SPOST's eCommerce deliveries on the domestic postal network helped offset the expected decline in traditional letter mails, and International mail was lifted by cross-border volumes from the Alibaba Group. Operating profit margin over the quarter improved to 22.3%, up from 22.1% a year ago. In particular, domestic mail margins improved on the back of operating synergies from the ongoing integration of the last mile delivery capabilities. While there is room for margins to climb further, given SPOST's efforts to improve processes, we should not discount the increase in costs following the implementations of measures (e.g. hire additional 100 postmen and redeploy 35 mail-drop driver as full-time postmen) to meet the standards of delivery of mail.

- **Firmness in Property segment**: In 3QFY2019, revenue rose 4.0% y/y while operating profit gained 18.2% y/y, largely due to rental income from the SingPost Centre retail mall. Despite having recorded steadily stronger figures since the commencement of operations of the mall in October 2017, we expect flattish figures going forward with the opening of Paya Lebar Quarter which is located 450 metres away. Both Post and Parcel and Property cumulatively account for ~52% of SPOST's revenue and more than offset the operating losses incurred by eCommerce.

- **eCommerce under review by Management**: The US business within the eCommerce segment, which comprises TradeGlobal and Jagged Peak, faces intensified competitive pressures and rising customer bankruptcies. With the view that eCommerce will continue to underperform and remain loss-making in the current financial year, management guided that they will review the business in detail and there exists the risk of impairment to the carrying value of the US business (~SGD90-100mn). We note that Jagged Peak became an indirect wholly-owned subsidiary of SPOST in Feb 2019, following the acquisition of additional ~5.95mn units of Jagged Peak shares. Operating profit margin for eCommerce was -16.2% in 3QFY2019.

- **Turnaround of Logistics continues**: Famous Holdings' freight forwarding business drove the 3.6% y/y revenue growth at Logistics. Operating profit was higher by ~SGD0.8mn y/y, largely due to a reduction in losses at Quantium Solutions due to the ongoing review of unfavourable customer contracts. Operating profit margin for Logistics remained low at 1.3%, though up from 0.8% in the corresponding quarter. While SPOST has made some headway in this segment, it continues to be a work-in-progress.

- **Defensive credit metrics**: In 3QFY2019, net operating cash flow fell by 8.8% y/y, largely due to lengthening of trade and other receivables. Free cash flow fell by a much smaller extent of 1.4% y/y as lower capex was incurred given the SingPost Centre retail mall redevelopment has been completed. Having said that, SPOST remained in the net cash position of SGD52.7mn (though expected to be lower at ~SGD35.8mn, should cash be used to acquire the additional Jagged Peak shares). Taking the perpetual (which rank *pari passu* with the claims of all its unsecured debt at the SPOST holding company level) as debt, adjusted net gearing was unchanged at 0.17x as at 30 December 2018 compared to a year ago. Based on our calculation, EBITDA/Interest improved slightly to 24.8x from 23.4x a year ago given interest expense fell more than EBITDA. SPOST's credit metrics remains intact.

| OCBC Global Treasury | |
|---|---|
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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.

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