Issuer Profile:
Neutral (5)

Ticker:
GGRSP

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Golden Agri-Resources Ltd ("GGR")

Recommendation

- **GGR saw a weaker 2Q2019, culminating in a net loss of SGD61.4mn, although the company reported a narrower fall in gross profit against peers. EBITDA/Interest coverage ratio fell to only 1.9x (2Q2018: 2.9x) driven by the y/y fall in CPO FOB prices by 22% y/y.**
- **Unadjusted net gearing was 0.67x, inching up versus 31 March 2019, though we take some comfort this is below the more than 0.70x seen in 2018.**
- **We continue to view GGR's diversions into the technology fund as a competing outflow. Debtholders have to be contractually paid, which helps mitigates some of this risk, though we are increasingly cautious over such outflow. The company faces other uses of capital which are important for the long term credit health of the company (chiefly, replanting and investments to improve sustainability of palm products)**
- **There are no close comparables to GGR in the same industry sector. Comparing to Aspial Corp Ltd's ASPSP 5.25% '20s, we think the GGRSP 4.75% '21s is trading at overly punitive levels at 636bps spread, notwithstanding the lower liquidity associated with a true high yield paper in SGD.**
- **We are maintaining GGR's issuer profile at Neutral (5) and hold Aspial Corp Ltd's issuer profile at Negative (6).**

Relative Value:

Bond	Maturity / Call date	Net gearing	Ask YTM	Spread to call
GGRSP 4.75% '21s	25/01/2021	0.67x	7.95%	636bps
ASPSP 5.25% '20s	28/08/2020	2.23x	6.43%	480bps

Indicative prices as at 28 August 2019 Source: Bloomberg
Net gearing based on latest available quarter

Background

- Golden Agri-Resources Ltd ("GGR") is a major palm oil company, managing 499,235 ha of palm oil plantations in Indonesia. The company's integrated operations include palm oil cultivation, crude palm oil ("CPO") and palm kernel processing and downstream refining to produce consumer products such as cooking oil, margarine and shortening.
- The company is ~50.4%-owned by the Widjaja family and is listed on the SGX with a market cap of SGD3.3bn as at 28 August 2019.
- While palm oil as a sector continues to face sustainability challenges (eg: Europe biofuel ban), it is a high yielding oilseed that is unlikely to lose its usage in the long term. GGR is part of the FTSE4Good index (inclusion since 2018) though reportedly has been removed from the Dow Jones Sustainability Indices in 1Q2019.

Key Considerations

- **Loss making in 2Q2019:** Revenue was down by 17% y/y to USD1.5bn, mainly driven by the fall of palm prices. CPO Free on Board ("FOB") price per metric tonne was USD479 in 2Q2019, falling by 22% y/y though the 6% y/y decline in palm product output (albeit from a high base in 2018) did not help either. Reported gross profit fell 31% y/y to USD151.8mn as cost was unable to be spread across a larger production base per company. While GGR's gross profit had declined y/y, this was a smaller fall versus other Indonesia focused palm oil peers listed on the SGX who is less integrated. Notably, despite the fall in CPO prices, which had affected its upstream Plantations and Palm Oil Mills segment, GGR's Palm, Laurics and Others segment helped buffer the fall somewhat. EBITDA margin of 2.7% was recorded in 2Q2019 versus 0.7% in 2Q2018. Per company, this was partly attributable to biodiesel where 85% of GGR's capacity is for the Indonesian biodiesel mandate and stronger demand for its sustainability palm oil products. Since September 2018, Indonesia mandated diesel engines to use a fuel blend consisting of 20% vegetable oil (predominantly palm oil) and 80% petroleum. There are plans to increase this fuel mix to 30% vegetable oil by early 2020. While GGR's gross profit suffered less versus peers in 2Q2019, GGR's has higher overheads and this was only down 19% y/y, which dragged the company to report an operating loss of USD 10.5mn (2Q2018: USD19.1mn). The company ended the quarter with a loss for the period of SGD61.4mn (2Q2018: USD 37.8mn).

- **Reported EBITDA at five year lows though we think can tilt up:** Reported EBITDA fell by 34% y/y to USD77.3mn, which is the worst quarter in the past five years, though interest cost held steady at USD40.0mn, which resulted in a much thinner EBITDA/Interest coverage of 1.9x (2Q2018: 2.9x and 1Q2019: 2.9x). Assuming the Palm, Laurics and Others segment hold up, we do not expect interest coverage ratio to drop below 1.5x in 3Q2019 as palm prices in has rose from the YTD trough of MYR1,865 in end-June 2019. The average price from July 2019 to writing was MYR 2,017 per MT (at similar levels to 2Q2019). OCBC Treasury Research & Strategy is currently forecasting CPO prices at MYR 2,100 for 3Q2019 and 4Q2019 respectively. Production and inventory levels are looking tight which could push palm prices higher still.

- **Increasing focus on investing outflow:** In the beginning of 2019, GGR had projected capex of USD250mn (for the upstream and downstream segment) and in 1H2019, had spent USD125mn in capex. The company is in the midst of refreshing its capex plans in light of the current environment. In 1H2019, GGR had spent USD81.7mn (net of inflows) as investments in financial assets, which we think a large portion went into technology fund(s). GGR's cash flow from operating activities (before interest but after tax) comfortably covered cash interest payments in 1H2019, though we continue to view GGR's diversions into the technology fund as a competing outflow to cash accumulation for debt pare down. Debtholders have to be contractually paid, which helps mitigates some of this risk, though we are increasingly cautious over such outflow. The company faces other uses of capital which are important for the long term credit health of the company. Chiefly, 15% of GGR's plantation comprises of palm trees are more than 25 years old (beyond commercial lifespan) and replanting would need to happen progressively. With sustainability fast rising as a core concern of customers, end-consumers, financiers and green groups, we envisage continuous capex spent would be required as well, for example, to further improve traceability in the logistics chain. As it stands, there is a lack of detailed disclosure over such technology investments (eg: composition of investments, returns outlook etc).

- **Net gearing within range:** As at 30 June 2019, unadjusted net gearing was 0.67x, slightly higher than the 0.64x as at 31 March 2019, though we take some comfort this is below the more than 0.70x seen in 2018. Short term debt was high at USD1.8bn as at 30 June 2019, however post quarter end, we note that MYR375mn (~USD89mn) in MYR-denominated bonds had been redeemed while we estimate ~USD1.0bn relates to working capital which tends to get rolled forward. Excluding the working capital related debt, we think GGR still has USD0.7bn in short term debt (representing 22% of total debt) though we expect the company to refinance this rather than pay the debt down given its thin cash flow generation versus its potential investing outflows. That being said, while short term debt coming due appears high, it is not unusually large relative to GGR's recent history and as such despite the likely weaker palm prices for full year 2019 versus 2018, we think bank lenders will remain supportive. Nevertheless, with the equity markets bearish over the palm oil sector, financial flexibility from capital markets is somewhat crimped.

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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