Flight to quality amidst market headwinds

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- Market speculation over a U.S. interest rate hike in September appeared to have eased, following the release of meeting minutes for the July 28-29 Federal Open Market Committee (FOMC) session which occurred before China's unexpected devaluation of the yuan last week. Over the week, the 10-year yields ended 12bps lower at 2.07%.

  In Asia, China's surprise currency devaluation, remained in focus, with the latest development being the People's Bank of China's (PBOC) intervention to support the yuan during the week. Compounded by concern over a deepening economic slowdown on the back of weaker-than-expected manufacturing data, this continued to pummel the Chinese equities market and spill-over into the HY bond space, particularly the offshore CNH credits. In the words of our trading colleagues, the dyke around USD HY (and even Chinese property) may be on the verge of breaking in the face of sustained selling amidst the risk-aversion mood. Although, the HG property credits seem to be holding firm, with supportive technical for the more liquid US$-papers against a skinny issue pipeline.

  The week saw Noble Group (NOBLSP) in the spotlight again with the company updating the market on the litigation instituted against the 'short-seller attack' report author, and with much debate surrounding its liquidity issues. The NOBLSP curve was hit down to $84.60-86.40 level. Elsewhere, Pacific Andes Resources Development (PAHSP) and key subsidiary China Fishery Group (CFG) saw their '17 and '19 bonds retreating to record low levels of $93.60 and $60.50 respectively, as the companies are being investigated by regulators in Singapore and Hong Kong.

- Separately, with the 1H earnings season underway, the table below summarizes the key financials for some of the key Chinese HG and HY property developers (under our coverage) which have thus far announced their 1H15 results:-

1HFY2015 Key Financials for Chinese HG and HY Property Developers

Issuer	Issuer Ratings (M/S)	Revenue (RMBbn)	EBITDA (RMBbn)	Cash (RMBbn)	ST Debt (RMBbn)	Total Debt (RMBbn)	Debt/ EBITDA (x)	EBITDA Int. Cover (x)	7MFY15 Contracted Sales (RMBbn)	FY15 Contracted Sales Target (RMBbn)	FY15 Target Completion
CHIOLI	Baa1/BBB+	51.9 [1]	15.2 [1]	62.9 [1]	8.2 [1]	82.9 [1]	2.7	8.2	95.9 [2]	180.0 [2]	53%
SINOCE	Baa3/BBB-	15.1	2.6	14.0	5.7	48.6	9.0	1.4	16.1	42.0	38%
VANKE	Baa1/BBB+	47.6	10.0	43.8	23.8	63.2	2.9	3.9	133.8	220.0	61%
YUEXIU	Baa3/BBB-	6.6	1.3	6.7	6.9	31.9	10.9	1.5	13.0	24.8	52%
CAPG	B2/B	3.9	0.9	4.2	4.1	13.8	7.7	1.5	7.1	13.5	53%
CHINSC	B1/B	6.0	1.4	2.4	5.4	13.6	4.6	2.7	6.8	13.5	50%
COGARD	Ba1/BB+	47.3	8.4	17.2	19.4	67.3	4.0	3.0	61.6	135.0	46%
LNGFOR	Ba1/BB+	16.8	3.5	16.8	8.7	49.5	6.9	2.4	26.1	53.0	49%
PWRLNG	B2/B	4.7	1.0	4.3	5.0	21.0	9.8	1.3	8.1	13.0	62%
YLLG	Ba3/B+	3.4	0.8	8.0	4.5	19.5	11.3	7.5	12.9	18.0	72%

[1] calculated based on RMB/HKD=1.2501 as of 30 June 2015

[2] in HK$bn; and credit metrics on annualized basis for comparison purposes

Source: Company, DBS Bank

- Amidst renewed uncertainty over the impending U.S. interest rate hike, the primary market remained on a defensive tone with four new issues priced this week for US$1.6bn, comprising both HG and HY transactions. This brings gross isuance YTD to US$105.8bn.

  In the HG space, Bank of Communications (BOCOM; A2/A-) issued a dual-curency, dual-tranche offering, which comprised a US$385mn 3.125% 5-year bond at CT5+165bps and a €100mn 3-year FRN. Both tranches attracted a combined order book of US$2.2bn, with the dollar bond priced 25bps inside its initial price guidance. Though, demand for the new bonds appeared to be weaker, compared to the Chinese bank's US$2.45bn additional Tier 1 (AT1) offering last month which received an order book of US$9bn. Everbright Securities (EVBSF; Baa3/NR) made its maiden bond debut with a US$450mn 2.875% 3-year credit-enhanced bond with a SBLC from China Merchants Bank's Shanghai branch (Baa1/BBB+). The deal was more than 4x oversubscribed, and priced 15bps inside initial guidance.

  Philippines corporates returned to the primary market for the first time since Vista Land & Lifescapes' issuance in mid-June. International Container Terminal Services Inc. (ICTPM; un-rated) sold a US$450mn 5.5% perpetual non-call 5.75-year bond at par, its second perpetual of the year. The perpetual deal was more than 4x oversubscribed, before being upsized from around US$300-350mn level and priced 25bps inside initial guidance. It subsequently traded as high as 100.75 before closing at par on its first day in the secondary market. SMC Global Power Holdings (SMCGL; un-rated) issued a US$300mn 6.75% perpetual non-call 5.5-year bond at par, its first perpetual deal since 2013. However, unlike the upsized new ICTPM perpetual, SMCGL's deal attracted an order book of only about US$600mn and had to settle for a US$300mn issue size from the initial US$500mn level. Furthermore, its pricing did not tighten from initial guidance of 6.75%.

  Looking ahead, potential USD deals in the pipeline could include PT Bank Permata (Baa3/NR) which met investors this week for a Basel III-compliant offshore Tier 2 offering; and the Philippines government (Baa2/BBB) which is mulling a US$750mn bond later this year to meet its funding needs in 2016.

- The secondary market continued to see broad-based weakness in performance of both HG and HY credits. Spreads for most Chinese HG corporates widened by 1-9bps. GRNLGR '24s was a distinct underperformer, widening 29bps to T+396bps. Following Moody's revision of outlook on the state-owned company's ratings to negative in end-July, S&P downgraded its ratings to BBB- from BBB on Wednesday, noting that its financial position has deteriorated more than expected.

  In the HY space, bond prices for most Chinese corporates dropped 0.1-1.4pts, led by single-B rated property developers YUZHOU '19s and GZRFPR '19s. Chinese industrials underperformed the rest of the pack, with MIEHOL '19s and YINGDZ '18s shedding 7.6pts and 6.2pts to $62 and $88 respectively. For MIEHOL, the decline comes ahead of its earnings announcement this morning, in which the company reported a net loss in 1H15 compared to net profit in 1H14. At the point of writing, the '19s fell further to $60. In the case of YINGDZ, the company's ratings were downgraded by Moody's to B1 from Ba3 last Friday, reflecting its weakened liqudity profile – for more details on the credit, please refer to ACW dated Aug 13. Meanwhile, Indonesian corporates were under severe pressure over the week as bond prices fell 0.9-6.1pts, led by GJTLIJ '18s and JPFAIJ '18s which tumbled to $65 and $70 respectively.

Other key corporate development:-

China Vanke <VANKE> '18 (Baa2/BBB Stable)

1H15 result update – healthy sales performance and strong balance sheet

- As of 1H15, revenue and EBITDA came in at RMB47.6bn (+24% yoy) and RMB10bn (+36% yoy), with EBITDA margin higher at 21%

risk-return perspective when compared to peers in the 'BBB' rating bucket, given that their spreads have been fairly stable in recent weeks of volatility amidst the Chinese equities rout since mid-June. We believe its 40bps spread differential inside of POLYRE '18s is fairly valued, given the latter's higher gearing and smaller scale of operations.

Hysan Development <HYSAN> '23 (A3/BBB+ Stable)

1H15 result update

- HYSAN's 1H15 revenue rose to HK$1.7bn (+7% yoy), largely attributed to positive rental reversions across its portfolio with average rental increases of c.35% and c.30% in retail and office segments respectively. Occupancy rates also remained strong (98% in retail, 100% in office and 95% in residential). Resultantly, 1H15 EBITDA rose to HK$1.4bn (+8% yoy) with EBITDA margins marginally higher at 83% (1H14: 82.5%). Going forward, key growth drivers could come from asset enhancement projects in Causeway Bay (due for completion in 2H'16) and the Mid-Levels (scheduled to commence in 4Q'15), as well as the combined re-development of Sunning Plaza and Sunning Court which is on schedule for completion in 2018.

- As at end-1H15, total debt decreased to HK$5.8bn (-17% yoy), largely driven by repayment of approximately HK$1.2bn of floating rate debt since the end of Jun'14, as part of their funding cost management initiative against expectation of a rising interest rate environment. Against the growth in EBITDA, on 1H15 annualized basis, gearing improved to 1.9x (1H14: 2.4x) while EBITDA interest coverage rose to 13.5x (1H14: 11.4x). Though, the average cost of funding climbed slightly to 3.3% (1H14: 3.1%) primarily due to repayment of the lower cost floating rate debt (vis-à-vis fixed rate debt). Still, the group remains relatively protected against potential interest rate hikes in the future, as its share of fixed rate debt rose to 81.1% of total debt (1H14: 76.3%).

  Meanwhile, the group's liquidity position remained healthy. Though unrestricted cash dipped slightly to HK$3.6bn (-2% yoy), these together with HK$1bn undrawn committed facilities, could comfortably cover HK$1.2bn of short-term debt as at end-1H15. At the same time, the group is not expecting any immediate lumpy repayment/refinancing risk, with the average debt maturity largely unchanged at 5.7 years (1H14: 5.6 years). About 21% of outstanding debt will mature within one year, 8% due > two years but < five years and the balance due > five years. All the outstanding debt are on an unsecured basis and account for 7.3% of total assets (1H14: 9%).

- *Thoughts on bonds: As mentioned in our last report ('Asia Credit Wrap – Jumbo issuance revives primary market' dated Mar 13), while we continue to see improvement in Hysan's operating capabilities for its existing retail and office portfolios, its concentration risk remains high with almost all its properties located in the Causeway Bay vicinity in Hong Kong. Though management has not disclosed any information on further investment opportunities in other parts of Hong Kong and overseas, we would closely monitor such developments, if any, to assess its execution risk outside its usual stronghold. Overall, we remain Marketweight on HYSAN '23s in light on the potential increase in interest rate environment. Trading at 24bps tighter than HLPPY '21s (un-rated), we believe investors are better compensated in HLPPY '21s for the shorter duration risk despite an exposure to its China rental portfolio.*

China Aoyuan Property Group <CAPG> '17, '18 & '19 (B3/B- Stable)

1H15 update – overall slight improvement in financial profile, but gearing remains elevated

- For 1H15, the group registered improvement in revenues and EBITDA to RMB3.9bn (+48% yoy) and RMB895m (+54% yoy), though it should be noted that generally 1H14 was a difficult period and starting from a weaker comparative base. Still, the better result was underpinned by the increase in recognized GFA delivered of 342k sqm (+14% yoy) and recognized ASP of 11.2k/sqm (+31% yoy). Resultantly, operating margin improved marginally to 22.7% (vs 21.8% in 1H14). This was mainly attributable to the

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properties delivered mainly in Guangzhou with higher selling prices. Sales from Guangzhou, Chongqing, Shenyang, Zhongshan and other cities accounted for 75%, 12%, 4%, 4% and 5% respectively. By product segmentation, sale of commercial apartments (/SOHO type) accounted for the bulk at 54%, followed by residential apartments (23%), retail shops (21%) and others (the remaining 2%).

Contracted sales during the period totalled RMB6.1bn (+17% yoy) or about 45% of full year target of RMB13.5bn, which puts the group within average peers in the HY Chinese property space where cumulative contracted sales to full year target was about 45-50% level. The result was supported by higher GFA sold of 822k sqm (+53% yoy), though this was negated by lower ASP of RMB7.4k/sqm (-23% yoy). 67% came from sale of residential apartments, retail shops @ 17%, commercial apartments (/SOHO) at 15% and low density residential 1%. By cities breakdown, reflective of the more diversified market spread, with Guangzhou accounting for 28% (vs 48% a year ago), followed by Guangdong (others) @ 18%, Chongqing @ 22%, Hunan 9%, Shenyang 5%, Guangxi (10%), Jiangsu & Jiangxi (1% each). During the period, the group achieved a sell through rate of 45% (vs full year target of 55%) and cash collection ratio of c.88%. The management advised that the lower sell through rate was because the group was focused on de-stocking inventories during the period. Back in FY14, the management had attributed slower sales momentum experienced in cities such as Shenyang (Liaoning), Chongqing and Zhuzhou (Hunan), and in striving to move some of the inventories there, the group had offered price discounts of 8-10% (on average). As of end 1H15, the group's completed but unsold stock stood at c.510k sqm.

With the soft launch of its One30 Hyde Park Sydney which garnered contracted sales of c.A$150mn, and subscribed sales totalling RMB250mn, the management advised that preliminary contracted sales for July was about RMB1bn. As of end 1H15, the group has about RMB14bn of un-booked revenue, and on average about RMB8-10bn could be recognized, which will help to seal earnings visibility for the year.

- *Gearing remain elevated, due to the active land acquisition and sales of commercial property (CP) tends to be unpredictable.* On the back of its active land renewal, total borrowing @ 1H15 rose to RMB13.8bn (FY14: RMB11.5bn). As part of its funding cost management initiative, CAPG issued a US$100mn 9.25% offshore bonds to ABCI through private offering (in Apr), a US$250mn offshore bonds at 10.875% (in May), and a RMB2.4bn domestic bonds at 5.80% (in July). These have allowed the group to lower its effective borrowing cost to 9.3% and is targeting to bring this down to 9%. As the proceeds were partially used for refinancing, its proportion of trust loans to total borrowings dipped to 10% (vs 15% a year ago), while onshore bank borrowings stood at 40% (vs 51% previously), offshore bank borrowings @ 11% (vs 6% previously), and senior notes @ 39% (vs 28% previously).

- In light of the yuan devaluation, at current borrowing currencies weighting, we think the risk of currency mismatch is manageable for the group. The management advised that should the yuan continues to depreciate and US$ borrowing becomes more costly, CAPG could further tap the onshore bond route and would need to carefully consider hedging options in light of incremental costs. On a 1H annualized basis, gearing remained high at 7.7x (albeit an improvement over FY14's 8.6x), and slight improvement in EBITDA interest coverage at 1.5x (FY14: 1x). This is because CPs tends to tie up capital resources and demand (particularly retail shops) less predictable, although margins tend to be higher than residential properties.

  During the period, the group's cash holdings totalled RMB6.8bn (almost two-third was unrestricted), whereas as of end FY14 almost RMB2bn was 'earmarked' for obtaining certain loans which was eventually 'released' upon their settlement. Further, the higher than usual cash balance was temporarily influenced by the un-used proceeds from the sale of debt securities (as outlined above). The latter has also helped to extend the group's debt maturity profile and ease re-financing risk. Aside from the ST-debt (totalling RMB4.1bn), the group's other borrowings will mature within 1-2 years @ 18%, 2-5 years @ 51%

and >5years @ 1%. In addition, CAPG has undrawn banking facilities of c.RMB5.5bn.

In term of working capital management, its past due account (>180days to >3 years) spiked up to 60.9% (vs 36% FYE14) of total receivables. The management explained that the spike in aged receivable was reflective of the group's surge in pre-sales growth from 91% yoy in FY13 and 22% yoy in FY14. No impaired provision has been established, as the management is confident that these receivables are recoverable. As it takes about 3 years (on average) for a project to be completed-delivered, considerations under such pre-sale contracts are 'protected' as about half of the property titles value are still vested with the developer (CAPG) and thereby providing adequate buffer.

- *Overseas (One30 Hyde Park Sydney) and other non-residential projects*: the management advised that since Mar'15, CAPG (70% equity stake holder in this Sydney project) has procured a A$60mn loan from CBA (which covers about 50% of the land acquisition and funding cost of not more than 5% p.a.). As previously guided, the Sydney project which has an estimated value of c.A$400mn (RMB2bn equivalent) was 'soft launched' in Aug'15, and to-date, it has achieved pre-sales of c.A$150mn. The management advised that the project acquisition cost was c.A$120mn (about RMB540mn), and about half has been funded through the CBA loan, about RMB200mn CAPG equity and the balance from JV partner (Ecove).

  Based on ASP of A$2.5-2.7k/sm, the management is expecting the project to yield GPM of some 25-28% and could contribute about RMB1bn towards the group for the year. The project is not without execution risks, as CAPG has yet to establish a brand name there, and all pre-sale proceeds are restricted until delivery at final closing of the units. Though, some of these concerns are partly negated by the project prime location and the limited land supply in that area. The management reiterated that the group has no other overseas plan and the focus will be on this Sydney project for now.

  As for the other cultural/tourism/leisure-related projects (in Shaoguan and Songjiang District), the management reiterated that their involvement is only to build/develop the complex and these are in collaboration with the local governments. Still, as previously outlined in our last reports, as we have seen some developers that had ventured into tourism/travel related theme projects which have not panned out as desired, these developments and associated investment outlay will be on our credit monitoring radar.

  On expectation of cash collection ratio of c.80-85% and based on sell-through rate of 55-60%; FYE15, the management has guided contracted sales collection of RMB12bn, relative to construction capex of RMB6.8bn, land acquisition RMB5bn (committed land premium of RMB1.3bn will be fully settled by this year), SG&A c.RMB700mn, interest expense c.RMB1.2bn, tax c.RMB1.3bn, dividend payout c.RMB300mn & debt repayment c.RMB6bn. In all, ending net cash for the year (considering cash c/f & new borrowing drawn-down), is estimated at c.RMB2.5-3bn. However, should CAPG continue to be aggressive with its land acquisition, it would need to tap on more fund raising exercises, although it needs to be mindful of its gearing profile which remain high. Assuming no major incremental debt drawdown, we expect FCF to remain in negative territory for the year.

- *Thoughts on bond: With concerns by investors over negative headline risks amidst the slew of anti-graft investigations earlier in the year seemingly reduced, the CAPG curve has rebounded close to levels previously seen. Although, in recent weeks on the heels of concern over the yuan devaluation, the curve has shed about 50-80bps. Still, given that more than two-thirds of CAPG's projects are in tier I/II cities, and its residential and commercial dual model, we think the company is in a position to weather changes in market conditions. Its recent sale of notes (both in the offshore and onshore space) have helped to extend CAPG's debt maturity profile. Though, its gearing is likely to remain elevated for the year and its pace of land acquisition/growth (viz. its overseas expansion and foray into travel related/tourism projects) will remain on our monitoring radar. In light of all*

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these, and considering the management's intention to redeem the bonds, we are maintaining our Overweight on the '17 and initiating coverage on the '18 with an Overweight rating. We are keeping to MarketWeight on the longer-tenure '19. We think the '17 still provides decent pick-up on YTW basis and as a short-tenor carry trade play. From a risk-return perspective, we think the bonds still offer better relative value compared to peers in the 'B' rating bucket (like FTHDGR complex which valuation has been affected by lingering concern over anti-graft investigation headline risks and awaiting a re-rating story).

Yanlord Land Group <YLLG> 6.2% '17 & 10.625% '18 (Ba3/B+)

1H15 update – encouraging improvements, thanks to the policies easing

General comments

- As outlined in our last report (Asia Credit Wrap dated May 15), characteristic of q-o-q results with seasonal volatility, what a difference in term of financial improvement that was reflected by YLLG group's 1H15 results.

- With the series of lending rate cuts by the PBOC and further easing of regulatory measures, we as well as according to checks with friendly channels, are of the view that these effects will take some time to filter through and gradually are helping to lift buying sentiments. As earlier advised by YLLG's management, they have seen the policies easing working to their advantage with effect gradually kicking-in. As we mentioned previously, the effects from policies relaxation by the government are not something that will result in overnight transformation, as buyers are likely to wait out for a while to re-assess the situation. Moreover, certain lower tier cities (III/IV type) that have experienced supplies overhang, could take some time to work through the excess situation.

  Based on our observation, 7M15 YTD contracted sales achieved in the Chinese property HY space averaged 50-55% of developers (under our credit coverage) full year targets. In YLLG's context, 7M15 YTD cumulative contracted sales totalled RMB12.9bn or about 72% of full year target of RMB18bn which puts them above average among the HY Chinese property developer peers.

- For 1H15, YLLG group's revenues and EBITDA improved to RMB3.4bn (+2.4% yoy) and RMB828mn (+21% yoy). While recognized GFA delivered was lower at 116.1k sqm (-8.4%), the effect was offset by the higher ASP of RMB25.5k/sqm (+9.6% yoy) which was an encouraging indicator. Resultantly, operating margin improved to 24.7% (vs 21% in 1H14). Against the policies easing (as discussed above), this has allowed the group to push out sales of mid- to high-end projects such as Yanlord Yangtze Riverbay Town Phase 3 (Nanjing) that was delivered during the period. Other key contributing projects included: Chengdu Yanlord Riverbay Phase I, Shanghai Yanlord Sunland Gardens Phase I, Suzhou Yanlord Lakeview Bay (Land parcel A2 & A5). By cities breakdown, sales from Nanjing accounted for 57%, followed by Suzhou (18%), Shanghai (14%), Chengdu (7%) and others (the remaining 4%). As outlined above, for 7M15 YTD, YLLG has recorded contracted sales totalling RMB12.9bn or about 72% of full year target of RMB18bn which puts them above average among the HY Chinese property developer peers. At the same time, YLLG also have an additional RMB2.3bn in subscription sales that is likely to be converted into contracted sales by July end. Against lower pressure to meet sales target, this would allow the management better flexibility in setting ASPs which may support future margins. While 1H15 sales were mainly supported by existing inventory, the group plans to unveil 80% of its new launches (c.RMB18bn out of total planned saleable resources of RMB36bn for FY15) in 2H which will continue to support sales momentum. Some of the key projects that the group intends to launch in 2H include: Yanlord Riverbay Phase 2 (Chengdu); Yanlord Eastern, Sunland (Phase 2) and Western Gardens (all in Shanghai); Oasis New Island Gardens Phase 2 & Yangtze Riverbay Town Phase 4 (Nanjing) and Marina Peninsular Gardens Phase 1 (Zhuhai).

  Total debt was marginally lower at RMB19.5bn (FY14: RMB19.8bn). Against a better EBITDA, on 1H annualized basis, cash flow metrics – gearing and EBITDA interest coverage ratios stood at 11x

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