

Asia IG Technology

Prefer BBB to A bonds; more value in <3yr & >20yr A bonds post curve flattening

Rating Change - Credit

Revisiting valuation of different pockets of tech sector

We think Asian tech bonds' YTD strong run has been backed by improving fundamentals, low supply & stable regulatory environment. We continue to prefer BBB bonds to A ones. BBB bonds are a good carry given their decent c.55bp pickup over A ones. They may offer more upside if the recovery in hardware & semiconductor markets is stronger than expected and/or BBB firms turn more prudent in new investments. In the A space, we see more value in <3-yr & >20-yr bonds, given the YTD curve flattening & their higher pickup over Chinese oil majors'/ US A tech bonds. But we see less value in 10- to 20-yr bonds. We thus make some recommendation changes on BABA bonds to align with our latest views (see Exhibit 1 and inside).

A: more value in <3yr & >20yr bonds post curve flattening

YTD, BAT bonds have outperformed Chinese oil majors'/ US A tech bonds (-26bp vs. -5/+8bp); the spread curve of <20-yr BAT bonds has flattened from 61bp to 27bp only (vs. that of <20-yr Chinese oil majors'/ US A tech bonds: from 55/ 59bp to 41/ 53bp). Pickup over Chinese oil majors'/ US A tech bonds of <3-yr & >20-yr BAT bonds is relatively high at c.30-45bp/ 25-45bp but that of 10- to 20-yr ones is relatively low at c.15/ 20bp.

BBB: mildly reduced but still decent pickup over A bonds

YTD, BBB tech bonds' spread curves have generally flattened (e.g. HYUELE '31-26/ JD '30-26/ MEITUA '30-25: from 68/ 71/ 114bp to 58/ 51/ 89bp); LENOVO's curve is the only exception, with LENOVO '30-25 widening by 6bp to c.110bp. BBB tech bonds' pickup over BAT bonds has reduced mildly to c.55bp (c.-5bp YTD), which, in our view, is driven by BBB tech firms' more favorable fundamentals trend.

Favorable fundamentals trend

We believe fundamentals of Chinese hardware firms & Asian chipmakers may benefit from a recovery in demand for key hardware products (e.g. PCs, smartphones & servers) & rising AI adoption. Also, we expect Chinese internet firms' credit profiles to remain solid. Despite intensifying competition & anti-monopoly rules, they have increased their focus on cost optimization & turned disciplined in investing in new businesses.

Likely low net supply, stable regulatory environment

In our view, net supply from Chinese tech firms may remain low, given their strong cash flow generation & prudent investments. But we see scope for Asian semiconductor firms to tap the bond market opportunistically, given their large capex needs. Also, we think the regulatory environment in China may remain stable amid the government's efforts to support economic growth, but there may still be regulatory actions from time to time.

06 March 2024

Global Emerging Markets | Corporate Credit
Asia Pacific
Technology

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BAT: BIDU/ BABA/ TENCNT

Exhibit 1: Bond recommendation changes

We have OW recommendation on BABA '24/ '47/ '51/ '57/ '61, MW recommendation on BABA '27/ '31, and UW recommendation on BABA '34/ '37/ '41.

Bond	Yrs	Z-sprd	Old	New
BABA 3.6 '24	0.7	51	UW	OW
BABA 3.4 '27	3.8	92	MW	MW
BABA 2.125 '31	6.9	122	MW	MW
BABA 4.5 '34	10.7	143	OW	UW
BABA 4 '37	13.8	158	UW	UW
BABA 2.7 '41	16.9	177	OW	UW
BABA 4.2 '47	23.8	191	OW	OW
BABA 3.15 '51	26.9	198	OW	OW
BABA 4.4 '57	33.8	207	OW	OW
BABA 3.25 '61	37.0	214	OW	OW

Source: BofA Global Research, Bloomberg

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Refer to important disclosures on page 8 to 11. Analyst Certification on page 6. Valuation & Risk on page 6.

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Timestamp: 06 March 2024 08:01AM EST

Largely stable regulatory environment in China

We believe the regulatory environment in China will likely remain stable. Our view is supported by recent regulatory actions. **Online game:** National Press and Publication Administration (NPPA) published a proposal targeting the online game industry with new restrictions in Dec 2023. But it backtracked and said it would improve the proposal by earnestly studying public views. In Jan/ Feb 2024, it approved 111/ 115 domestic games (vs. on average 81 domestic games approved each month in 2023). **Online service:** The Ministry of Human Resources and Social Security released new guidelines targeting online platforms, including Meituan and Didi Chuxing, to improve protections for gig workers, including ensuring their salaries matching local minimum wages, providing them with enough time off, etc. But we note the provision of social insurance is not mentioned.

Bond recommendation changes

YTD, BAT bonds have significantly outperformed Chinese oil majors'/ US A tech bonds (-26bp vs. -5/ +8bp). In our view, their YTD outperformance has been driven by (1) solid fundamentals of Alibaba, Baidu and Tencent, (2) a lack of bond supply, and (3) largely stable regulatory environment in China. Also, YTD, the spread curve of <20-yr BAT bonds has flattened from 61bp to 27bp only (vs. that of <20-yr Chinese oil majors'/ US A tech bonds: from 55/ 59bp to 41/ 53bp). As a result, spread pickup over Chinese oil majors'/ US A tech bonds of <3-yr & >20-yr BAT bonds is relatively high at c.30-45bp/ 25-45bp whereas that of 10- to 20-yr ones is relatively low at c.15/ 20bp.

We see more value in <3-yr & >20-yr BAT bonds and less value in 10- to 20-yr ones. We believe Alibaba may benefit more from potentially looser regulations as it has previously faced more regulatory headwinds. We think the regulatory risk of its business model is relatively low. We like its solid credit profile (e.g. sizeable net cash position) and dominant market position. We make the following bond recommendation changes on BABA bonds to align with the above views.

Exhibit 2: Bond recommendation changes

We have OW recommendation on BABA '24/ '47/ '51/ '57/ '61, MW recommendation on BABA '27/ '31, and UW recommendation on BABA '34/ '37/ '41.

Bond	Amt Out. (US\$ mn)	Years to maturity	YTM	Z-spread	Price	Old	New
BABA 3.6 '24	2,233	0.7	5.7	51	99	UW	OW
BABA 3.4 '27	2,550	3.8	5.0	92	95	MW	MW
BABA 2.125 '31	1,500	6.9	5.1	122	83	MW	MW
BABA 4.5 '34	698	10.7	5.2	143	94	OW	UW
BABA 4 '37	1,000	13.8	5.4	158	87	UW	UW
BABA 2.7 '41	1,000	16.9	5.6	177	69	OW	UW
BABA 4.2 '47	1,750	23.8	5.6	191	81	OW	OW
BABA 3.15 '51	1,500	26.9	5.6	198	66	OW	OW
BABA 4.4 '57	1,000	33.8	5.6	207	82	OW	OW
BABA 3.25 '61	1,000	37.0	5.6	214	63	OW	OW

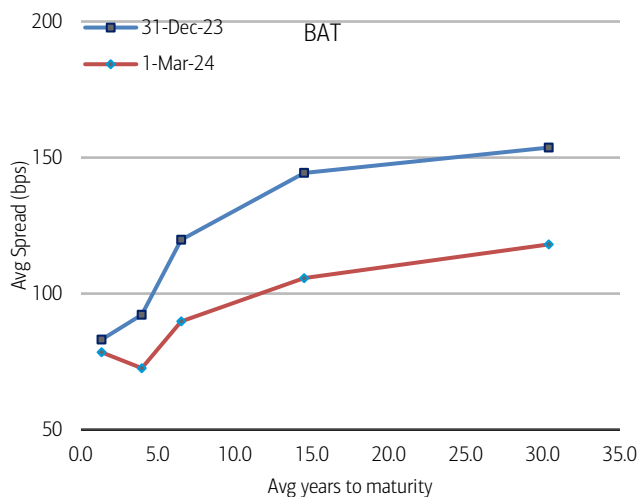
Rating changes are highlighted in blue.

Source: BofA Global Research, Bloomberg

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Exhibit 3: BAT bonds' spread curve

YTD, the spread curve of <20-year BAT bonds has flattened from 61bp to 27bp only.

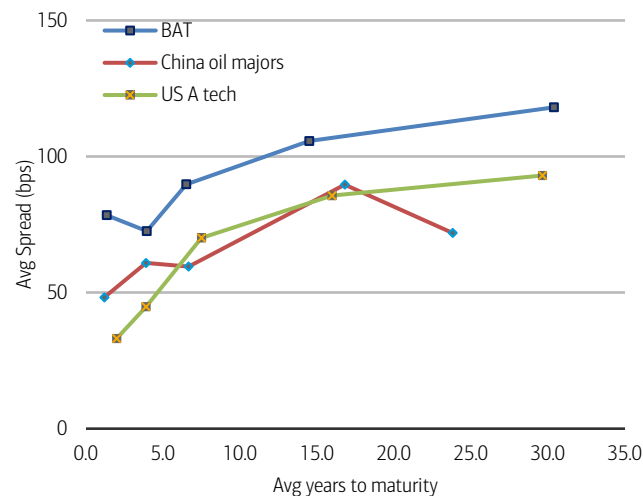


Source: ICE Data Indices, LLC. BofA Global Research

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Exhibit 4: Spread curves of BAT, Chinese oil majors' and US A tech bonds

YTD, the spread curve of <20-year Chinese oil majors' / US A tech bonds has flattened from 55/ 59bp to 41/ 53bp.

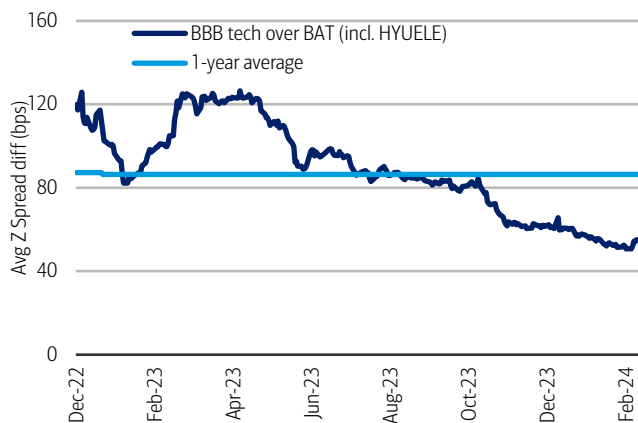


Source: ICE Data Indices, LLC. BofA Global Research

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Exhibit 5: We prefer BBB tech bonds to BAT bonds on decent pick-up

Average z-spread pick up of BBB tech (incl. HYUELE) bonds over BAT bonds

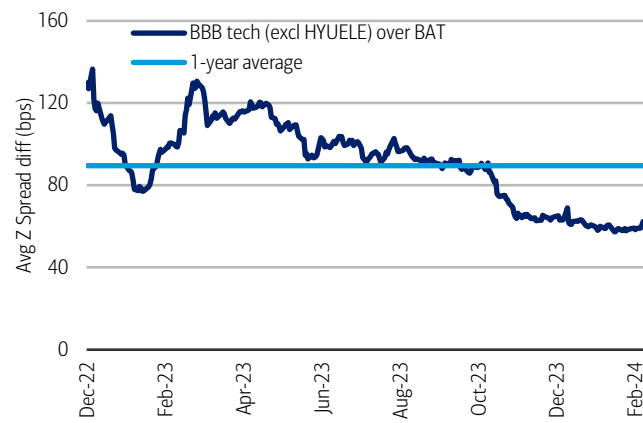


Source: Bloomberg, BofA Global Research

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Exhibit 6: We prefer BBB tech bonds to BAT bonds on decent pick-up

Average z-spread pick up of BBB tech (excl. HYUELE) bonds over BAT bonds



Source: Bloomberg, BofA Global Research

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Exhibit 7: BAT bonds have outperformed Chinese oil majors' & US A-rated tech bonds

YTD spread performance of BAT, Chinese oil majors' and US A-rated tech bonds by tenor

YTD	Overall	0 to 3	3 to 5	5 to 10	10 to 20	>20
BAT	-26	-5	-20	-30	-39	-36
China oil majors	-5	-4	10	0	-17	-6
US A-rated tech	8	6	9	17	-1	10

Source: ICE Data Indices, LLC. BofA Global Research

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Exhibit 8: Yearly average of spread differential between BAT bonds and Chinese oil majors' bonds

<3-year and >20-year BAT bonds offer relatively high pickup over Chinese oil majors' bonds whereas 10- to 20-year BAT bonds offer relatively low pickup over Chinese oil majors' bonds.

Year	Overall	0-3Y	3-5Y	5-10Y	10-20Y	>20Y
2017	-25	-10	-13	-9	-49	-10
2018	-3	-22	-11	2	-10	10
2019	12	-12	4	13	-1	13
2020	-2	-14	-2	3	-24	-10
2021	0	-11	-12	6	-51	0
2022	55	31	51	57	8	55
2023	48	17	45	63	34	73
Now*	29	30	12	30	16	46

Source: ICE Data Indices, LLC. BofA Global Research

*Now as of 01 Mar 2024

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Exhibit 9: Yearly average of spread differential between BAT bonds and US A-rated tech bonds

<3-year BAT bonds offer relatively high pickup over US A-rated tech bonds whereas 5- to 10-year & 10- to 20-year BAT bonds offer relatively low pickup over US A-rated tech bonds.

Year	Overall	0-3Y	3-5Y	5-10Y	10-20Y	>20Y
2017	25	50	50	43	21	36
2018	40	33	41	50	43	48
2019	47	38	54	57	36	27
2020	43	63	62	63	26	14
2021	48	51	44	59	48	45
2022	76	63	67	73	90	91
2023	51	43	55	52	59	65
Now*	27	45	28	20	20	25

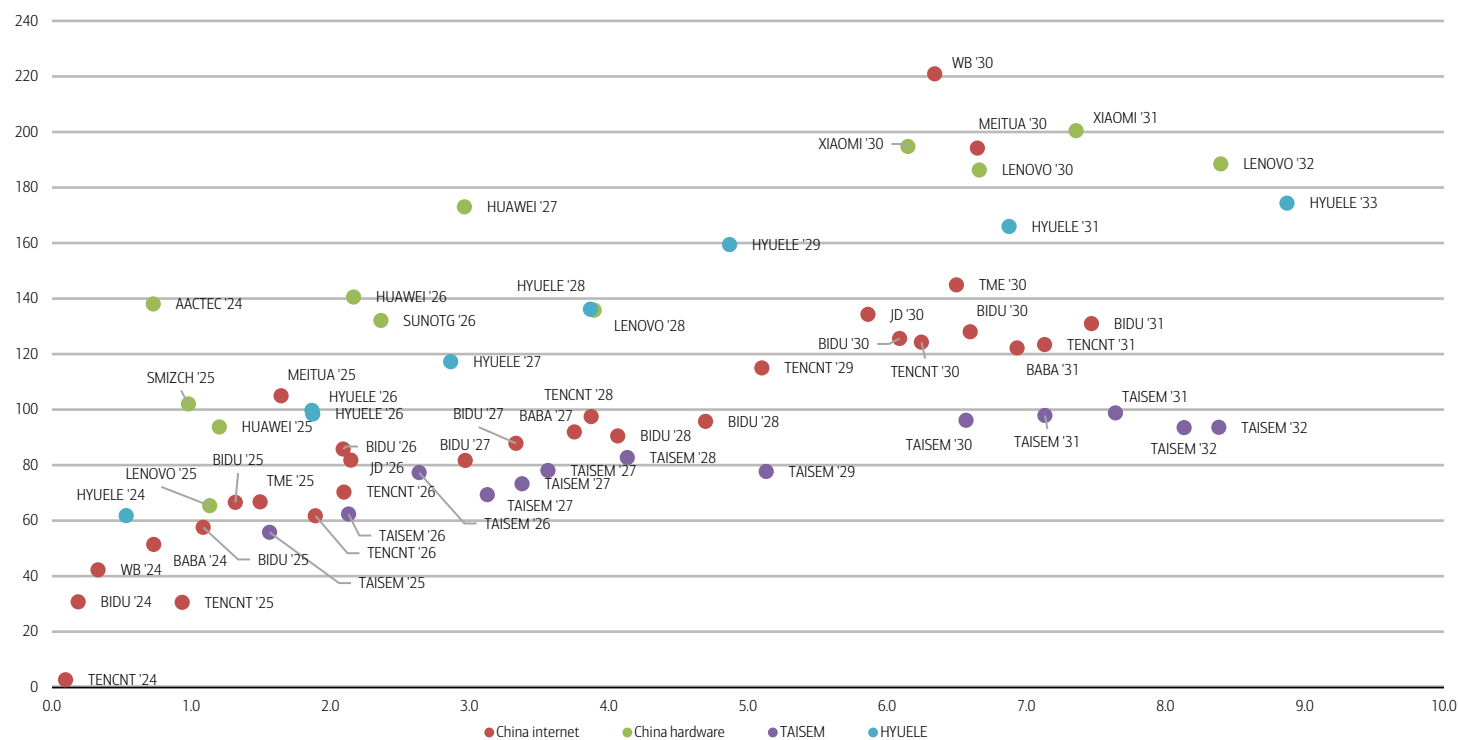
Source: ICE Data Indices, LLC. BofA Global Research

*Now as of 01 Mar 2024

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Exhibit 10: Asian tech bonds (<10-year) - z-spread (y) vs years to maturity (x)

We prefer BBB bonds to A ones. In the A space, we see more value in <3-yr bonds.

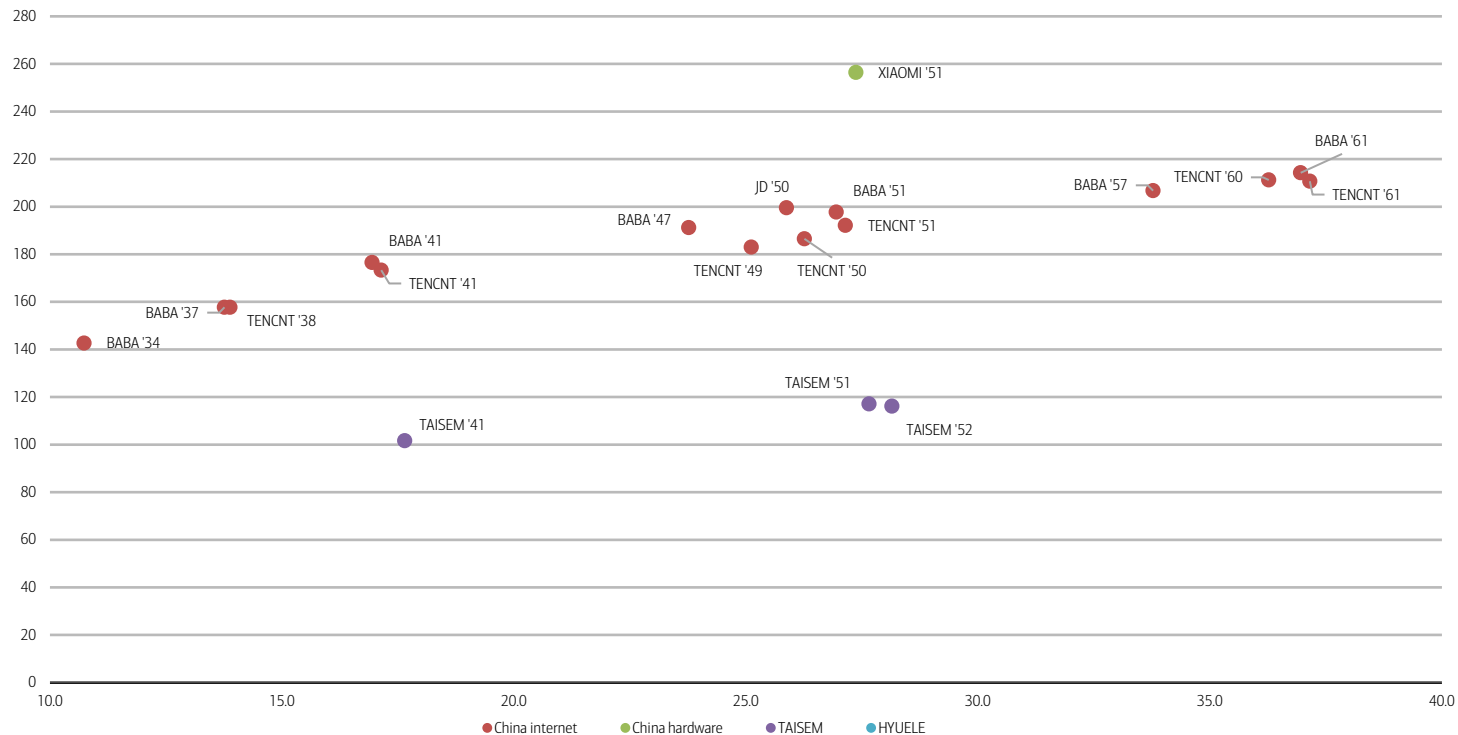


Source: BofA Global Research, Bloomberg

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Exhibit 11: Asian tech bonds (>10-year) - z-spread (y) vs years to maturity (x)

In the A space, we see more value in >20-yr bonds, but we see less value in 10- to 20-yr ones.



Source: BofA Global Research, Bloomberg

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Valuation & risk

Alibaba Group (BABA)

In the Chinese A tech sector, we generally see more value in <3-year & >20-year bonds, given the YTD curve flattening & their higher pickup over Chinese oil majors'/ US A tech bonds. We believe Alibaba may benefit more from potentially looser regulations as it has previously faced more regulatory headwinds. We think the regulatory risk of its business model is relatively low. We like its solid credit profile (e.g. sizeable net cash position) and dominant market position. Taking the above into account, we have OW recommendation on BABA '24/ '47/ '51/ '57/ '61, MW recommendation on BABA '27/ '31, and UW recommendation on BABA '34/ '37/ '41.

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Security/Loan pricing

Alibaba Group Holding Ltd. / BABA

Security	Amt	Maturity date	Ratings		Price	Price date	Yield	Spread
			Moody's/S&P/Fitch				(%)	(Govt+bps)
3.6, Senior, USD, 2024:B	2,233	28-NOV-2024	A1/A+/A+		98.52	06-Mar-2024	5.71	80
3.4, Senior, USD, 2027:B	2,550	06-DEC-2027	A1/A+/A+		94.74	06-Mar-2024	4.96	61
2.125, Senior, USD, 2031:B	1,500	09-FEB-2031	A1/A+/A+		83.08	06-Mar-2024	5.05	89
4.5, Senior, USD, 2034:B	698	28-NOV-2034	A1/A+/A+		94.20	06-Mar-2024	5.21	105
4, Senior, USD, 2037:B	1,000	06-DEC-2037	A1/A+/A+		86.85	06-Mar-2024	5.36	120
2.7, Senior, USD, 2041:B	1,000	09-FEB-2041	A1/A+/A+		69.09	06-Mar-2024	5.54	111
4.2, Senior, USD, 2047:B	1,750	06-DEC-2047	A1/A+/A+		81.65	06-Mar-2024	5.61	118
3.15, Senior, USD, 2051:B	1,500	09-FEB-2051	A1/A+/A+		66.06	06-Mar-2024	5.61	130
4.4, Senior, USD, 2057:B	1,000	06-DEC-2057	A1/A+/A+		81.80	06-Mar-2024	5.61	130
3.25, Senior, USD, 2061:B	1,000	09-FEB-2061	A1/A+/A+		63.40	06-Mar-2024	5.61	130

For pricing information refer to "Other Important Disclosures" below.

B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); CDS=Credit Default Swap; EP=Equity Preferred

Disclosures

Important Disclosures

Credit opinion history

Alibaba Group Holding Ltd. / BABA

Security	Date ^{R1}	Action	Recommendation	Price
3.6, Senior, USD, 2024:B	28-Feb-2023		Marketweight	
	26-Sep-2023	Downgrade	Underweight	97.23
3.4, Senior, USD, 2027:B	28-Feb-2023		Overweight	
	31-Aug-2023	Downgrade	Marketweight	92.75
2.125, Senior, USD, 2031:B	28-Feb-2023		Marketweight	
	28-Feb-2023		Marketweight	
4.5, Senior, USD, 2034:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	89.46
4, Senior, USD, 2037:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	81.02
	11-Dec-2023	Downgrade	Underweight	83.08
2.7, Senior, USD, 2041:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	63.64
4.2, Senior, USD, 2047:B	28-Feb-2023		Marketweight	
	19-Jun-2023	Upgrade	Overweight	79.02
3.15, Senior, USD, 2051:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	60.21
4.4, Senior, USD, 2057:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	73.48
3.25, Senior, USD, 2061:B	28-Feb-2023		Marketweight	
	31-Aug-2023	Upgrade	Overweight	57.53

Table reflects credit opinion history as of previous business day's close.^{R1} First date of recommendation within the last 36 months, if for an issuer or within the last 12 months, if for a security or loan. The investment opinion system is contained at the end of the report under the heading "BofA Global Research Credit Opinion Key."

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B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); EP=Equity Preferred; CDS=Credit Default Swap

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Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R2}	Count	Percent
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Hold	193	49.87%	Hold	163	84.46%
Sell	50	12.92%	Sell	37	74.00%

^{R2} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only corporate credit issuer recommendations. A corporate credit issuer rated Overweight is included as a Buy, a corporate credit issuer rated Marketweight is included as a Hold, and a corporate credit issuer rated Underweight is included as a Sell.

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