Asia credit compendium

Introduction to Asia credit, top-down views, and issuer updates

26 July 2024 | Chief Investment Office GWM | Investment Research

26 July 2024, 2:36PM UTC
Chief Investment Office GWM
Investment Research

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Asia Pacific bonds

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- **A deep dive into Asia credit:** Since 2010, the Asia credit market has expanded by more than five times to around USD 1 trillion in size, even after the decline over the past two years. We believe it offers unique characteristics and diversification benefits for global fixed income portfolios. In this report, we provide readers with a top-down perspective of the market microstructure, and bottom-up views on issuers under our coverage.
- **Rating composition skewed toward investment grade (IG):** The Asia credit market has seen a steady increase in the proportion of IG credits over the years, especially in the BBB segment. Geographically, China credits take the largest share of the pie (35% of the total), but we expect this to decline to around 24% by 2026, making the country composition more balanced.
- **Sound fundamentals but tight valuations:** Asia credit fundamentals remain broadly sound, driven by solid macroeconomic growth which has benefited sovereigns in particular. Valuation-wise, Asia IG spreads are close to historical tights, but all-in yields continue to be attractive. Asia high yield (HY) spreads remain elevated, but this is distorted by the beleaguered China HY property segment and distressed sovereigns.
- **Asia IG remains our preferred segment.** We expect Asia IG returns to pick up to around 4–5% in 2H24, driven by imminent Fed rate cuts and resilient spreads. We see the risk-reward for Asia ex-China HY as less appealing at this stage of the economic cycle. While we do not envision significant spread widening, we think Asia HY performance will likely be driven by carry going forward.
- Please see **Table 15** for ourselection of bonds. Please also refer to the Emerging Market Bond List published weekly for a full list of bonds under our coverage.

This report has been prepared by UBS AG Singapore Branch and UBS AG and UBS AG Hong Kong Branch. Please see important disclaimers and disclosures that begin on page 85.

Foreword: The emergence of Asia credit

In 2010, Asia credit was a very niche segment, with hardly around USD 200mn of outstanding bonds. Fast forward to today, and the market has topped USD 1tr in size, having blossomed into a universe that is now too big for global investors to ignore. Still a relatively nascent asset class, the information asymmetries and idiosyncratic intricacies within Asia credit allow for strong alpha generation and healthy return potential for investors, in our view. Historically, the asset class has generated attractive risk-adjusted returns, with Asia investment grade (IG) outperforming other global IG segments. In recent years, the market has faced some setbacks, particularly in Asia high yield (HY) where a wave of defaults has taken a toll on its performance. As the asset class starts to mature, it is inevitable that there will be fresh challenges and evolving risks that investors will have to carefully navigate. Nonetheless, we believe the opportunity set in Asia credit remains vast, with the asset class having a role to play in every investor's portfolio.

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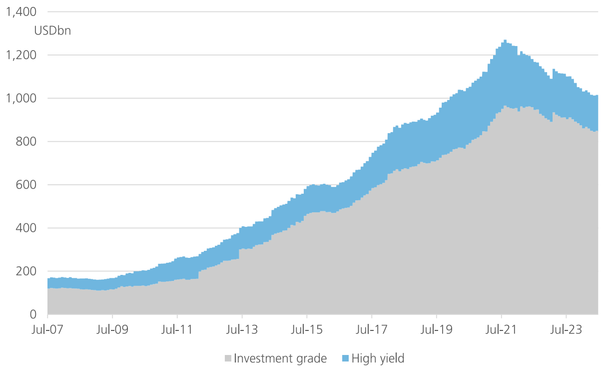
A deep dive into Asia credit

In this report, we provide readers with a top-down perspective of the market microstructure and composition of the Asia USD credit market. We explore what makes Asia USD credit unique and highlight several interesting themes within the asset class. Finally, we delve into the individual issuers across the region, assessing their latest earnings trends and shedding light on their fundamentals. From an investor perspective, we think the key to successful investing in this Asia USD credit boils down to 1) understanding the macroeconomic cycle of individual counties in Asia; 2) understanding the fundamentals of individual issuers in the region; and 3) identifying relative value across countries and sectors. Through this report, we aim to provide useful insights into these three key domains, which we hope will smoothen the investment journey for investors in this asset class.

Market size and development in recent years

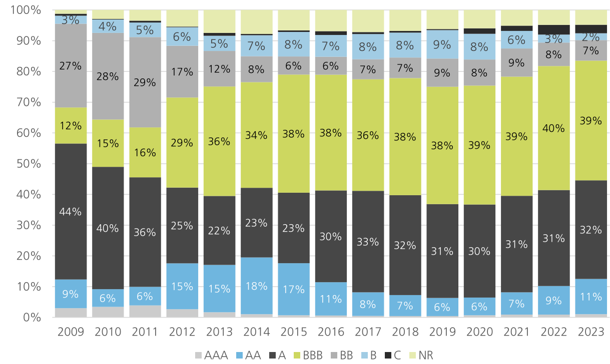
Over the past decade, the pace and scale of expansion in the Asia USD credit market has been remarkable, with the segment growing from USD 200mn in January 2010 to a peak of USD 1.2tr in mid-2021 (Fig. 1). This was driven by both push and pull factors, in our view. From a supply perspective, it was driven by cheap USD funding costs for issuers as US Treasury yields were close to historically low levels. From a demand perspective, the low-rate environment spurred global investors to hunt for yield in emerging markets, with Asia credit providing a decent yield pickup compared to developed market counterparts. However, after peaking in 2021, the Asia USD credit market has gradually declined over the past three years by about USD 200bn to around USD 1tr at present.

Figure 1 - Asia credit market has expanded by more than 5x since 2010



Source: UBS, JP Morgan

Figure 2 - Rating composition of Asia USD credit market



Source: UBS, JP Morgan

This is the first time in Asia USD credit's short history we are seeing a decline in its market size, which we attribute to several factors. First, aggressive rate hikes by the Federal Reserve which started in 2022 promptly increased the cost of funding in offshore markets for Asian corporations. As such, local currency bond and bank loan markets across Asia now offer competitive pricing versus USD funding. This is particularly true for Chinese corporations as historically low local government bond yields have supported cheap onshore funding. Second, sizable defaults in the China property sector have led to a material decline in the outstanding bonds in the high yield market. Third, from a demand perspective, bond investors have increasingly shifted their focus toward developed markets as yield differentials for Asian credits versus their similarly-rated developed market peers have narrowed significantly on the back of material spread compression. **We believe the market size of Asia USD credit should start to pick up again after 2024. As the Fed is poised to embark on a rate cutting cycle, funding costs should normalize for issuers and yield differentials should also improve sufficiently for investors to return to Asia credit.**

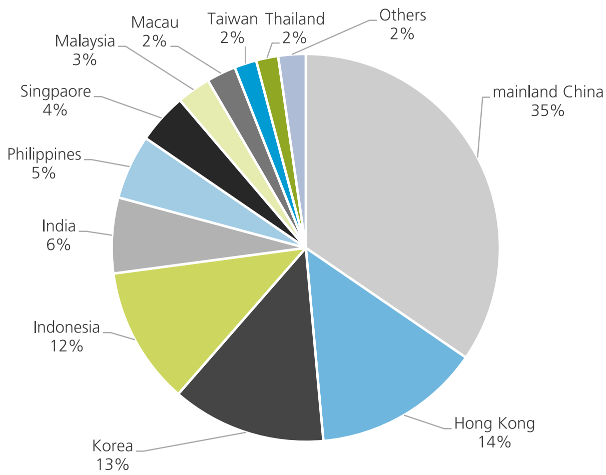
Rating composition skewed toward IG

The rating composition of the Asia credit market has also changed materially over time, marked by a steady increase in the proportion of investment grade credits (Fig. 2). Within the IG segment, the proportion of BBB rated credit has more than doubled since 2010, driven by rating upgrades for a couple of key sovereigns such as Indonesia and the Philippines as well as the emergence of BBB rated state-owned enterprises (SOEs) in China from 2015 to 2018. In the HY space, the portion of BB bonds fell to 7% of the overall market in 2023, from as high as 29% in 2011. In contrast, the proportion of C rated bonds has slightly increased over the past few years, driven by numerous rating downgrades and defaults by distressed China property credits.

China still has largest share of the pie, albeit it's declining

From a geographical perspective, **China credits take the biggest share of the pie, at around 35% of the overall market as of July 2024** (Fig. 3). Nonetheless, China's share of the Asia credit market has been gradually declining over the past two years due to negative net supply and defaults in the China property sector. After mainland China, Hong Kong and Korea take make up 14% and 13% of the market, respectively. It's also worth noting that China's weighting in the HY index is now significantly less at 21%, lower than its share of the overall market.

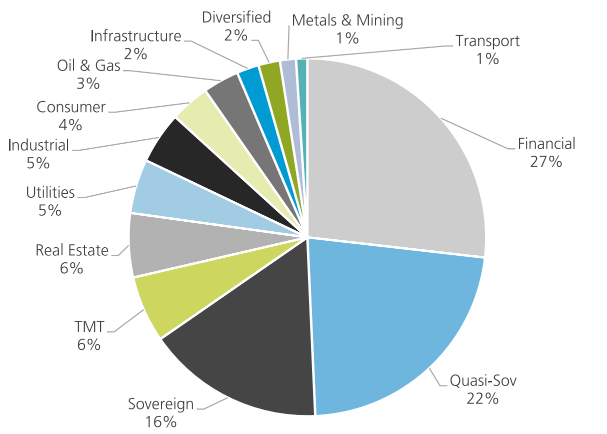
Figure 3 - Country breakdown



Source: UBS, JP Morgan

As far as sectors are concerned, the financial sector has the largest weighting at 27% of the Asia credit market (Fig. 4), followed by quasi-sovereigns (22%) and sovereigns (16%), as of July 2024. Notably, all three sectors are heavily influenced by macroeconomic conditions and policy direction in the region, with individual governments having a large impact on the credit profile of issuers in these sectors. This dynamic is unique to Asia as a sizable number of Asian issuers enjoy some form of state linkage, resulting in 1) their credit standing being determined by the likelihood of state support; and 2) their credit ratings being highly affiliated with the respective sovereign ratings.

Figure 4 - Sector breakdown

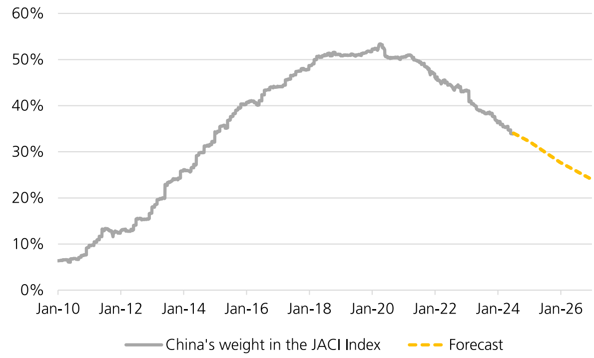


Source: UBS, JP Morgan

China becoming a smaller part of the market

The amount of USD bonds outstanding from Chinese corporations has dropped materially in the past two years due to several reasons. First, with Chinae government bond (CGB) yields trading at historically low levels, it has become much cheaper for Chinese issuers to issue debt in the local market. We have seen cases where investment grade issuers issued debt that was about 200bps cheaper in the local market. Second, given the macroeconomic challenges and overcapacity in certain sectors, companies are no longer looking at debt-funded expansion as we have seen in the past. Finally, a large number of China property issuers have defaulted and are no longer in the index. We believe some of these factors will continue to matter in the medium term, and hence the proportion of China USD bonds may decline further. **We estimate China's weighting in the JP Morgan Asia Credit Index will fall to around 24% by end-2026 from 34% at present (Fig. 5).**

Figure 5 - China's weighting in the JACI index

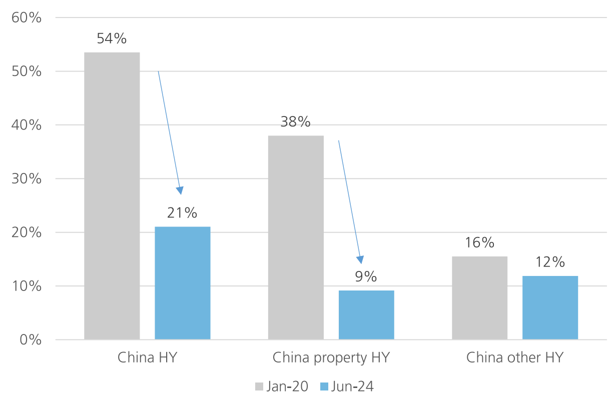


Source: UBS, JP Morgan

China property no longer a major portion of Asia HY

At its peak in early 2020, China HY accounted for 54% of the Asia HY market, led by the China property HY sector which made up 38% of Asia HY (Fig. 6). However, the China property market suffered a drastic downturn in 2021 and 2022, leading to a wave of defaults by numerous China property HY issuers. As such, the China property HY segment has shrunk materially since 2020, now amounting to just 9% of the Asia HY index. In contrast, the non-property China HY credit segment (12% of Asia HY), which has been declining only modestly, has now overtaken China property HY in size. Accordingly, the weighting of China HY has shrunk by more than half since 2020, now standing at 21% of the Asia HY index. **Given China property HY's significantly reduced weighting in the Asia HY segment, we believe this stressed segment will no longer be a major return driver going forward, unlike in previous years.**

Figure 6 - China HY weightings in Asia HY have dropped materially

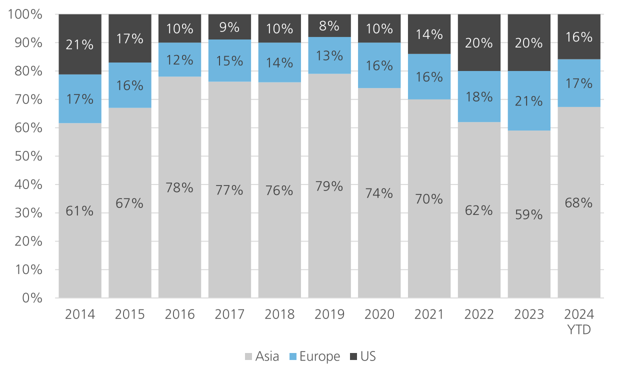


Source: UBS, JP Morgan

Who buys Asian USD credit?

To determine the investor base for Asian USD credit, we examine the new issue allocation of Asia credit by region. From 2014 to 2019, new issue allocation to Asian investors steadily increased from 61% to 79% (Fig. 7), with dwindling interest from European and US investors. After 2019, foreign interest in Asian credit picked up, with US and European investors allocated more than 40% of new issues in 2023. But year-to-date, it seems like the trend has reversed again (lower allocation to European and US investors), which we attribute to the narrowing spread differentials between Asian credit and developed market debt. **In view of the home bias effect, we expect buyers of Asian credit to remain dominated by Asian investors going forward, while foreign investor appetite will likely vary based on relative value considerations.**

Figure 7 - New issue allocation, by region

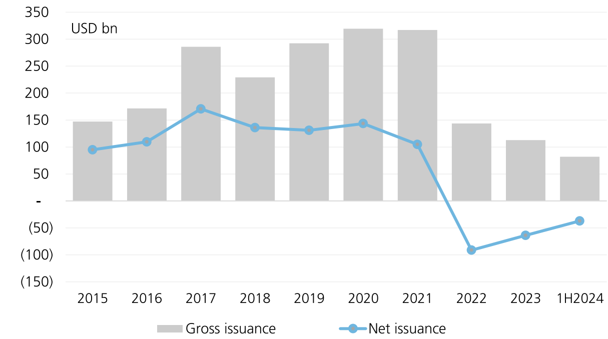


Source: UBS, JP Morgan

Net issuance has been negative since 2022

During the rapid expansion phase of the Asian credit markets, gross issuance ranged from USD 150bn to above USD 300bn, while net issuance was largely in the USD 10–50bn range (Fig. 8). However, this trend sharply reversed in 2022, with gross issuance down by 55% y/y while net issuance turned negative to –USD 91bn. In 2022, Asian issuers were afflicted by 1) rising funding costs due to the Fed's hiking cycle; and 2) USD bond markets being essentially shut to HY issuers following the stress in China HY property. Tepid gross issuance and negative net issuance continued into 2023 and 1H24, albeit showing some signs of improvement this year. **The recent dearth of USD supply from Asian issuers has been positive for technicals, and is a key reason why spreads have been compressing, in our view.**

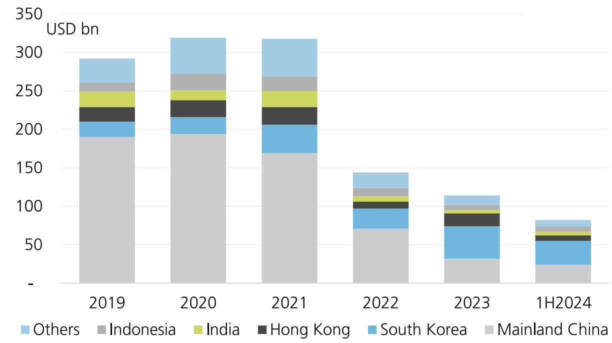
Figure 8 - Gross and net issuance trends



Source: UBS, Standard Chartered

Geographically, China has been the largest issuer of USD debt (Fig. 9), accounting for more than 60% of total issuance in 2019 and 2020. However, due to the struggles in the China property sector, coupled with cheaper onshore funding costs, USD issuance out of China has declined significantly in recent years. From an issuance perspective, the lone bright spot has been South Korea; the high credit ratings of issuers there have enabled them to borrow at reasonable costs, even in USD. **In 2023, South Korea surpassed China as the largest USD bond issuer, and this trend continued into 1H24.**

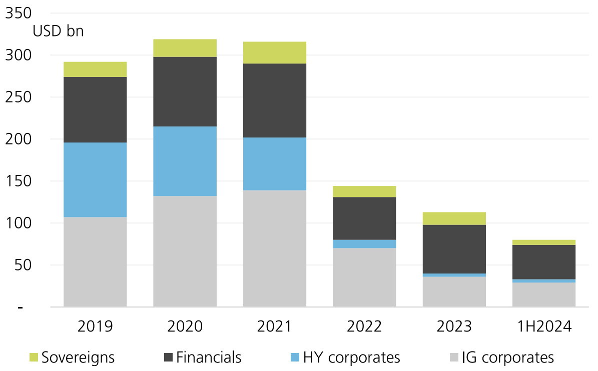
Figure 9 - Gross USD supply from Asia, by country



Source: UBS, Standard Chartered

From a sector perspective, financials now account for most of the USD debt issued out of Asia (Fig. 10), which is not surprising given the sector's regular issuances for refinancing and capital management. In contrast, HY corporate debt issuance has slowed to a trickle over the past two years as many of the weaker issuers were unable to access the USD bond market.

Figure 10 - Gross USD supply from Asia, by sector



Source: UBS, Standard Chartered

Sovereign fundamentals are stronger vs. past decade

Macroeconomic fundamentals in Asia have generally improved over the past decade and this is reflected in the sovereign ratings (Fig 11). Among these, it is worth highlighting that ratings of Indonesia and the Philippines have moved from high yield (HY) to investment grade (IG) and that has shifted all key Asian sovereign ratings to IG territory. Mainland China and Hong Kong were the only two economies to experience rating downgrades, but they were from very high rating categories. We are constructive on the near-term rating outlook for Asian sovereigns in the BBB segment. While the outcomes of recent elections in some countries may have put a pause to further improvements in fiscal positions, **we believe that the long-term fundamental improving trajectory is intact. This is quite important for the longer-term return outlook for Asia credit as sovereigns, quasi-sovereigns, and financials account for close to 65% of the market.**

Figure 11 - Sovereign rating changes since 2015

	S&P		Moody's	
Region	**2015**	**2024**	**2015**	**2024**
China	AA-	A+	Aa3	A1
India	BBB-	BBB-	Baa3	Baa3
Indonesia	BB+	BBB	Baa3	Baa2
Malaysia	A-	A-	A3	A3
South Korea	AA-	AA	Aa2	Aa2
Singapore	AAA	AAA	Aaa	Aaa
Hong Kong	AAA	AA+	Aa1	Aa3
Philippines	BBB	BBB+	Baa2	Baa2
Taiwan	AA-	AA+	Aa3	Aa3
Thailand	BBB+	BBB+	Baa1	Baa1

Rating upgrade

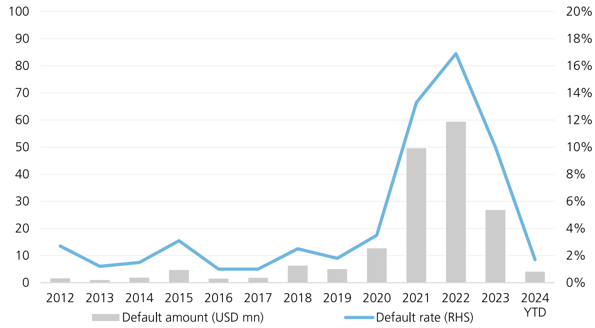
Rating downgrade

Source: Bloomberg

Default rates have normalized from the highs

From 2012 to 2020, Asia HY default rates were benign at under 4% (Fig. 12), before spiking to as high as 17% in 2022 amid the distress in the China property HY sector. With most of the defaults in the China property HY sector now behind us, Asia HY default rates have normalized, with the year-to-date default rate standing at a healthier 1.7%. **While we do not rule out further China property defaults going forward, we believe this will be largely idiosyncratic with limited contagion risk.** Likewise, we expect defaults from non-China HY issuers to be isolated events as well.

Figure 12 - Default rates in Asia HY

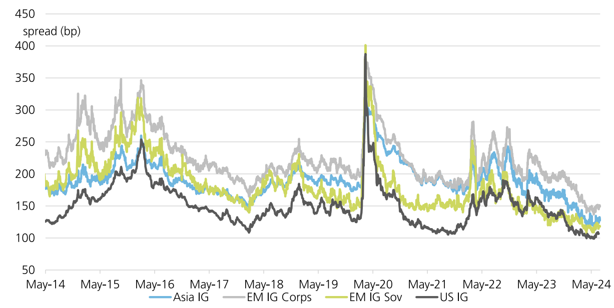


Source: UBS, JP Morgan

Asia IG spreads at historical tights

Asia IG spreads currently trade at around 130bps (Fig. 13), which like other IG segments are at or close to historical tights. Comparing Asia IG versus US IG, we find that Asia IG spreads have traded around 40–50bps wider than US IG during non-stressed periods, although this spread premium has widened to as high as 90bps during stressed periods such as the COVID-19 pandemic. Currently, Asia IG spreads are less than 20bps wider than US IG, which suggests that Asia IG is expensive compared to US IG.

Figure 13 - Historical spreads for Asia IG vs. other regions

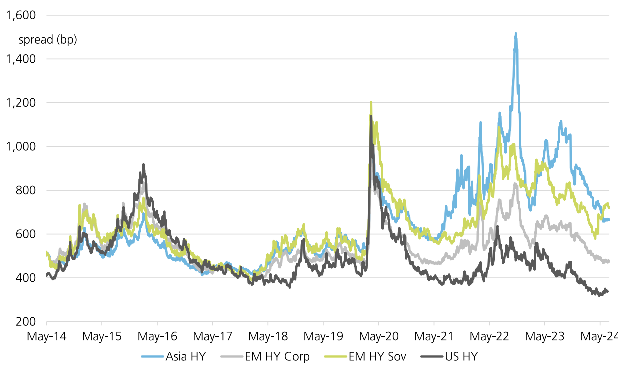


Source: UBS, JP Morgan

Asia HY spreads elevated, but distorted by China HY and sovereigns

Asia HY spreads are elevated at above 650bps (Fig. 14), but this is distorted by the beleaguered China HY property segment and distressed sovereigns. Excluding these segments, Asia HY spreads are well under 330bps, which is on the tight side from a historical perspective. From 2014 to 2019, Asia HY spreads traded in line or even inside US HY, but since the onset of the pandemic in 2020, Asia HY spreads have traded noticeably wider than US HY. This spread divergence was exacerbated by the stress in China HY property sector in 2021 and 2022, which at one point blew out Asia HY spreads to over 1,500bps. Since then, Asia HY spreads have compressed significantly, but still trade around 300-400bps wider than US HY.

Figure 14 - Historical spreads for Asia HY vs. other regions

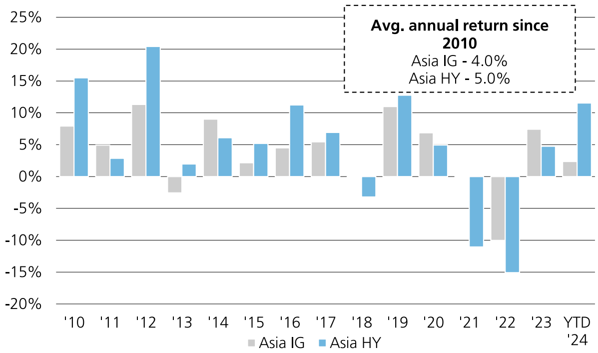


Source: UBS, JP Morgan

Historical returns dampened by recent correction

Since 2010, Asia IG has posted an average annual return of 4.0% (Fig. 15), which we think is respectable considering the low interest rate environment from 2010 to 2021. Asia HY returns were modestly better at 5.0% per annum as investors were duly compensated for the heightened volatility in the HY segment. Yet, historical returns of both Asia IG and HY were dampened by a steep double-digit correction in 2021–2022. Specifically, Asia IG fell 10% in 2022 as the Fed hiked rates in quick succession while Asia HY declined more than 10% in both 2021 and 2022 on the back of weakness in China HY property. Nonetheless, we have seen a turnaround in 2023 and year-to-date in 2024, with returns of both Asia IG and HY firmly back in positive territory.

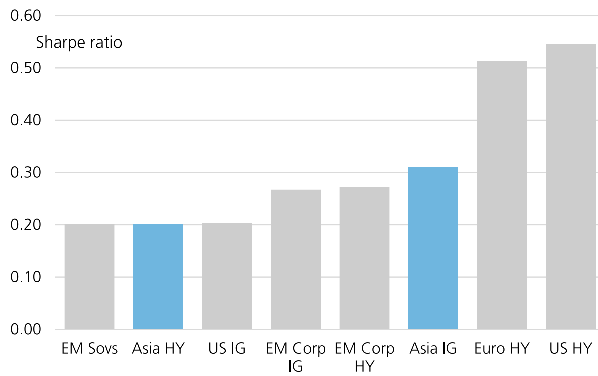
Figure 15 - Average annual returns of Asia IG and HY



Source: UBS, JP Morgan, Bloomberg

On a risk-adjusted basis, Asia IG has outperformed other global IG segments, as reflected in its higher Sharpe ratio (Fig. 16). We attribute the low volatility in Asia IG to the high proportion of stable state-linked credits, which have also benefited from improving sovereign fundamentals. In contrast, risk-adjusted returns of Asia HY have lagged, as evidenced by a lower Sharpe ratio compared to other global HY segments. This is due to the heavy negative returns attributable to the China property sector in recent years, which was a significant portion of the market.

Figure 16 - Sharpe ratio of regional credit markets (2010 to present)



Source: UBS, JP Morgan

Preference for Asia IG over HY

Asia IG continues to be our preferred segment in Asia credit. While performance year-to-date has been rather modest due to rate volatility, we expect returns to pick up over the next 6–12 months, driven by the Fed's expected interest rate cuts. We believe spreads will be resilient as we continue to see strong demand given elevated all-in yields, while activity in the new issue market remains modest. Over the next year, **we expect IG returns to be supported by coupon carry of around 5% plus some capital gains due to declining rates.**

With regard to Asia HY, we think risk-reward is a touch expensive at this stage of the economic cycle, given the stretched valuations in the Asia HY space outside of China. Away from China, we do not foresee any negative catalysts that may cause significant spread widening in Asia HY, but at the same time it is hard to envision much spread tightening from current levels. We do think a substantial portion of Asia HY's performance in 2024 was already front-loaded in the first six months of the year, and hence future returns will likely be driven by coupon carry. **We believe returns going forward will likely normalize in line with coupon carry and believe investors should look at bottom-up opportunities for alpha generation.**

Key risks and challenges in Asia credit

Despite the strong growth in the past decade, the Asia credit market is not as mature as the credit markets in the US. There are notable risks that investors have to accept. Firstly, secondary market liquidity for Asian credit is often weak due to the smaller issuance sizes for Asian companies and the predominance of buy-and-hold investors in the region. During times of volatility, investors may not be able to sell a sizable position without influencing the prices. Secondly, there is notable concentration risk in the Asia credit space, with China accounting for 35% of the index while sovereigns and quasi-sovereigns cumulatively account for 38% of the index. As such, any major credit developments in these countries/sectors may have an outsized impact on returns. A case in point was the defaults in the China property sector which have heavily impacted Asia HY returns in the past two years. Third, transparency is often not a priority for some of the smaller Asian issuers (for instance, LGFVs), hence financial disclosures may be lacking or not timely. Lastly, corporate governance concerns are often top of the mind regarding certain Asian issuers, where perception has been damaged by a few bad apples with idiosyncratic issues. There have been several reports of short sellers looking to expose some of these with varying success. Such governance-related concerns have led to added volatility in the market time and time again.

Asia credit: Bottom-up views, by region/sector

Region/ sector	CIO sector view	Rationale	Bond selection
Investment grade (IG)			
China state owned enterprises (SOEs)	Neutral	Chinese SOEs' fundamentals deteriorated in 2023 amid a challenging domestic macroeconomic backdrop and soft global demand. Nonetheless, we think government support remains intact, justifying the "SOE premium." A supply-demand imbalance will also support their performance, in our view. We are comfortable going down the credit spectrum for some yield pickup, and see buy-the-dip opportunities should any geopolitical tension-related weakness emerge.	The short-dated AMC complex, BOC Aviation 2026, Sinochem HK 2026, CSCI 2027, Power Construction Corp of China perp-NC27, Shandong Hi-speed Group perp-NC27
China privately owned enterprises (POEs)	Positive	Chinese tech names under our coverage reported largely stable or improving credit metrics in the latest earnings season. Despite significant spread compression year-to-date, we believe the tighter spreads are well-supported by these companies' solid fundamentals and favorable supply technicals. The space still currently offers compelling all-in yields for high-quality credit.	Baidu 2025, Tencent 2026, Lenovo 2028, Alibaba 2034, Tencent 2038, Alibaba 2047
Hong Kong	Neutral	Despite macro headwinds and pressure in the property sector, Hong Kong IG names have seen notable spread tightening year-to-date on their diversified businesses, solid balance sheet, and limited new supply. While a lack of near-term catalysts will likely limit further spread compression, the current all-in yield still looks decent for quality credit exposure. Investors could consider moderately extending duration in select solid A rated credit to enjoy capital gains, while remaining selective in BBB bonds.	Swire Properties 2026, Nan Fung 2027, Hong Kong Telecommunications 2029, Sun Hung Kai Properties 2030, CK Hutchison 2033, Airport Authority 2.1% perp, AIA 2.7% perp, BEA 2032 Tier 2, Dah Sing Bank 2033 Tier 2
Indonesia	Positive	We believe the recent concerns around a fiscal expansion is overdone and corporate issuance is likely to be subdued. On the back of healthy fundamentals and positive technicals, we believe spreads will remain well-supported and see Indonesian IG credit as a good way to play the falling rate narrative in 2H24.	Indonesia sovereign 2029, PLN 2030, Inalum 2028, Freeport Indonesia 2032, Tower Bersama 2027
India	Neutral	We believe credit fundamentals are in decent shape. Election results in June were a slight negative, but we do not believe fiscal consolidation will be materially derailed. Valuations in general are rather tight, but we believe Indian credit will continue to offer stable carry in the coming year.	REC Ltd 2028, Power Finance 2029, Reliance Industries 2032, Tata Steel 2028
South Korea	Positive	South Korean issuers have a wide dispersion of credit fundamentals, but we believe the credit standing of SOE names is primarily underpinned by a high likelihood of state support. Spreads are tight from a historical perspective, but all-in yields are attractive for one of the highest quality segments within Asia IG.	EXIM Korea 2028 FRN, Korea National Oil Corp 2026, Korea Hydro & Nuclear Power 2027, KDB 2033, SK hynix 2028, Shinhan Bank 2032
High yield (HY)			
China	Negative	We believe access to unsecured financing remains challenging for Chinese POEs, but secured financing remains accessible for companies with good quality assets as collateral.	Longfor Properties 2027
Hong Kong	Neutral	Recent bank loan rollovers and new credit facilities suggest our covered Hong Kong HY names still enjoy decent banking relationships. Still, divergence in profitability and liquidity will likely drive bond performance going forward. We stay selective in the space.	New World Development 6.15% perp
India	Neutral	Most outstanding Indian HY bonds in our coverage are quite short dated, and given the steady fundamental outlook, we are comfortable owning them for short-term carry. However, an average yield of around 6.5–7% is not particularly attractive from a valuation perspective, in our view.	Delhi Airport 2029, Tata Motors 2026
Indonesia	Neutral	Outstanding bonds in the Indonesian HY market are gradually declining as issuers tap the local market. Unlike India, fundamentals are largely mixed and issuers need to be assessed on a case-by-case basis. We believe commodity players will continue to outperform in 2H24.	Medco Energi 2029, Pakuwon Jati 2028, BNI 2026 Tier 2
Macau	Positive	Macau gaming operators' fundamentals are supported by healthy visit levels and mass gross gaming revenue. Overall, we take comfort in these operators' debt servicing capability, given their good liquidity, spread-out maturity profile, and strong support from banks and parent companies. With deleveraging still underway, we see good opportunities for investors with varying risk appetites.	Melco Resorts Finance 2026, SJM 2026, Studio City 2028, Wynn Macau 2028

Note: A positive view means we expect bonds in the sector to outperform similarly rated bonds. A negative view means we expect bonds in the sector to underperform similarly rated bonds. A neutral view means we expect bonds in the sector to perform in-line with similar rated bonds

Source: UBS. Please refer to Table 15 for the list of bonds.

Issuer updates

China's central SOEs

Figure 17 - China's central SOEs covered in this report and their respective credit views

Issuer	CIO outlook	Rating (Mdy/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
China Development Bank	Stable	A1/A+				
China Petrochemical Corporation	Stable	A1/A+				
CNOOC Ltd	Stable	A1/A+				
State Grid Corp of China	Stable	A1/A+				
China Huaneng Group	Stable	A2/A-				
China General Nuclear Power Corporation	Stable	A2/A-				
Sinochem Hong Kong	Stable	A3/A-				
China National Chemical Corporation	Stable	Baa2/A-				
China Jianyin Investment Ltd	Stable	A2/A				
CITIC Limited	Stable	A3/A-				
China Minmetals Corporation	Stable	Baa1/BBB+				
Power Construction Corp of China	Stable	Baa1/BBB+				
China State Construction International	Stable	Baa2/BBB				
China Merchants Port Holdings Company Limited	Stable	Baa1/BBB+				
AVIC International Holding Corporation	Stable	NR/BBB-				
China Taiping Insurance Holdings	Stable	NR/BBB+				
BOC Aviation	Stable	NR/A-				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 1 - Key financial & credit metrics (as of end-2023)

Issuer (Corporate)	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total liabilities / Total assets
China Petrochemical Corporation	456.6	7.8%	81.1	1.3x	29.0x	51%
CNOOC Ltd	57.4	59.1%	16.9	-0.3x	47.3x	34%
State Grid Corp of China	543.8	11.1%	179.0	2.7x	13.2x	54%
China Huaneng Group	57.7	29.9%	124.1	6.1x	5.8x	70%
China General Nuclear Power Corp	21.0	49.6%	84.0	7.7x	4.7x	69%
Sinochem Hong Kong *	12.5	17.5%	24.6	8.8x	1.8x	n.a.
China National Chemical Corporation	63.1	11.9%	82.8	9.7x	2.0x	86%
China Jianyin Investment Ltd	14.1	45.7%	90.1	11.1x	n.a.	45%
CITIC Limited	96.2	23.0%	205.8	5.3x	12.9x	88%
China Minmetals Corporation	131.5	5.7%	47.2	3.9x	5.9x	75%
Power Construction Corp of China *	93.7	7.0%	67.4	7.8x	3.1x	76%
China State Construction International	16.0	12.7%	11.0	3.4x	4.0x	70%
China Merchants Port Holdings Company	1.5	55.7%	5.5	3.6x	3.3x	30%
AVIC International Holding Corporation	26.1	7.1%	18.9	7.2x	3.9x	76%
Issuer (Insurer)	**Operating profit (USD bn)**	**Net investment yield**	**Investment Portfolio (USD bn)**	**Insurance contract liabilities (USD bn)**	**EBIT-to-fixed charges ratio**	**Life insurance's comprehensive solvency ratio**
China Taiping Insurance Holdings	2.1	3.6%	172.8	153.2	3.9x	284%
Issuer (Lessor)	**Lease rental income (USD bn)**	**Net lease yield**	**Funding cost**	**Total debt (USD bn)**	**EBIT / Interest**	**Total liabilities / Total assets**
BOC Aviation	1.9	7.1%	4.0%	16.5	1.8x	76%

* Latest available financials as of end-2022
Source: Company, UBS

China Development Bank

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Timothy Tay

Company updates

China Development Bank (CDB) is a state-funded and 100% state-owned development financial institution, directly overseen by the State Council. As a development bank, CDB has a mandate to provide medium-to long-term financing for the development of China's strategic industries, with a focus on the infrastructure industry and social housing projects.

In FY23, CDB reported a 5.9% decline in net interest income to CNY 160bn. However, its net profit rose 3.6% to CNY 87bn on the back of lower provisioning (–30.6%). Loan growth was steady (+2.9%), with gross loans amounting to CNY 14.9bn as of end-2023. Deposits declined 9% to CNY 3.4bn, but this was offset by a 5.5% increase in debt issued to CNY 13.4bn. While CDB relies heavily on wholesale funding, bonds issued by the policy bank have a 0% risk weighting for domestic bank investors, so funding costs are low. CDB's asset quality is healthy, with a low NPL ratio of 0.6% and loan loss reserves covering NPLs by more than five-fold. Capitalization is adequate, with its total capital adequacy ratio standing 11.7% as of end-2023.

Investment view

We view CDB as systemically important to the Chinese government, backed by its key policy role, 100% state ownership, and good track record of government support. CDB benefits from preferential regulatory treatment, with access to low-cost funding due to 0% risk weights for its issued bonds. We also take comfort in CDB's stable profitability, sound asset quality, and adequate capitalization profile. Credit weaknesses for CDB include a high reliance on market funding, and elevated risks for long-duration loans. We note that Moody's and Fitch have negative outlooks on CDB, in line with their outlook on the China sovereign. Valuation-wise, CDB trades in line with other state-owned policy banks, and slightly tighter than large commercial Chinese banks. We are comfortable owning CDB's USD bonds, as we view the issuer effectively as an extension of the Chinese government.

Key downside risks to our view include: 1) negative ratings actions on China's sovereign credit due to prolonged macroeconomic weakness; 2) an acceleration in NPL formation arising from the economic slowdown; and 3) a funding squeeze should market funding become unavailable.

China Petrochemical Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Zixuan Liu

Company updates

China Petrochemical Corporation (Sinopec) is a dominant player in China's oil and marketing industry. With operations along the entire oil and gas value chain, the company is less susceptible to oil price volatility than its pure upstream peers. It is 100% owned by China's central State-owned Assets Supervision and Administration Commission (SASAC), one of the world's largest producers of refined oil and petrochemical products. The company processed around 260 tons of crude oil in 2023 (one-third of China's total refinery throughput) and has a retail network of 30,000 gas stations (30% of China's total). As of end-2023, the company's total assets reached CNY 2.7tr (+7% y/y). It is expected to receive strong government support given its strategic role in China's energy security.

In 2023, Sinopec reported full-year revenue of CNY 3.2tr (–4% y/y). Though sales volumes increased thanks to China's post-COVID recovery, product prices were down across the board due to a decline in oil prices and domestic overcapacity issues. Margins were protected by lower oil and coal costs, with gross and EBITDA margins up slightly to 17% and 8%, respectively.

Operating in a capital-intensive industry, Sinopec's capex rose from CNY 150bn in 2019 to CNY 190bn in 2023. We expect a similar capex level to continue given the need to increase gas output and construct and upgrade refining and chemical production capacity. The company also aims to become China's largest hydrogen producer as part of its decarbonization initiative, which requires around CNY 30bn in investments by 2025. While this is may weaken the company's credit metrics, we believe it has a sufficient buffer against ratings agencies' downgrade triggers. The company's debt level was decent in 2023 with a debt-to-EBITDA at 2.3x (up from 1.9x in 2022), and EBITDA-to-interest coverage as high as 29x. Liquidity is still abundant, with cash-to-short-term-debt at 108%, down from 148% in 2022.

Investment view

We like Sinopec's robust credit profile, which enjoys both strong credit fundamentals and the high likelihood of government support. We have a Stable credit outlook on the issuer and a Fair rating on Sinopec's outstanding USD bonds, which offer a mid-4% to 5% yield-to-maturity. The company has been absent from the primary market for a few years (last issuance in 2021), resulting in strong technical support. It holds four tranches of bonds totaling USD 3bn maturing in 2H24. We recommend investors to participate in its refinancing deal, if there is one.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a significant deterioration of Sinopec's credit metrics due to sustained low oil prices, sector overcapacity, or higher-than-expected capex; and 3) potential US sanctions. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

CNOOC Ltd

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Zixuan Liu

Company updates

CNOOC Ltd is China's largest offshore crude oil and natural gas producer. It is the flagship subsidiary (65% ownership) of China National Offshore Oil Corporation, an SOE 100% owned by China's central SASAC. CNOOC takes up the latter's entire upstream business, contributing to around 40% and 90% of the parent's total revenue and EBITDA, respectively. As of end-2023, the company's total assets reached CNY 1tr (+8% y/y). The company is expected to receive strong government support given its strategic role in China's energy security.

CNOOC's balance sheet is robust, highlighted by its low leverage. The company is in a net cash position. As of end-2023, its total liabilities to total assets declined slightly to 34%, and debt-to-EBITDA was maintained at 0.5x. Liquidity was abundant with cash-to-short-term-debt at 890%, thanks to its strong cash generation. The company has maintained a positive net cash flow even with capex of CNY 120bn and a dividend payout of CNY 58bn. There was some weakness in profitability, with gross and EBITDA margins down to 42% and 59% respectively, due to softer oil prices in 2023. However, further downside should be manageable given the company's stringent cost controls.

Investment view

We like CNOOC's robust credit profile, which boasts both strong credit fundamentals and the high likelihood of government support. We have a Stable credit outlook on the name and a Fair rating on CNOOC's outstanding USD bonds, which offer a mid-4% to 5% yield-to-maturity. Due to net redemption in China's central SOE bond space, technical support has been strong, and we expect CNOOC's bonds to perform in line with the broader Asia IG segment.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a significant deterioration of CNOOC's credit metrics due to a sharp drop in oil prices, higher-than-expected capex, or large debt-funded acquisitions; and 3) potential US sanctions. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

State Grid Corp of China

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Timothy Tay

Company updates

As the largest grid company in China, State Grid Corporation of China (State Grid) constructs and operates transmission and distribution (T&D) power grid networks across the country. State Gride is 92.9% owned by SASAC, with the remaining 7.1% held by the National Council for Social Security Fund. It benefits from a stable asset-based regulatory framework, with a cost pass-through mechanism that protects it from significant price and volume risks and allows for reasonable returns over a three-year cycle.

State Grid has posted steady revenue and profit growth over the past few years, driven by increasing power demand in China. In FY23, State Grid recorded robust financial results, with revenue of CNY 3.9tr (+8.4% y/y), EBITDA of CNY 427bn (+2.2% y/y), and net profit of CNY 70bn (+19.5% y/y). The company's credit profile remained stable, with modest net leverage at 2.7x (FY22: 2.7x) and ample interest coverage of 13.2x (FY22: 12.2x). Capex has been on the rise (+9.4% in FY23) in recent years to fund investments in the power grid, but we do not expect this to pressure its credit profile as higher capex will likely be accompanied by healthy earnings growth with China's power demand set to continue rising.

Investment view

As State Grid is the sole provider of power T&D services in 26 provinces covering almost 90% of China, the company is effectively a monopoly in its service areas. As such, a default would have severe socio-economic consequences, potentially disrupting power supply to over 1.1 billion users. In light of this, we view State Grid as vital to the country and expect the Chinese government to provide timely support when needed to ensure the company's viability. As a state-owned utility company under a sound regulatory framework, State Grid enjoys a stable operating profile and consistent financial performance. Valuation-wise, State Grid trades roughly in line with similarly-rated Southern Power Grid, the second largest grid company in China. We view State Grid as a defensive name in the China IG utility space and see the bonds as a stable carry play.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; and 2) overly aggressive debt-funded acquisitions or higher-than-expected capital outlays which weaken cash flow.

China Huaneng Group

UBS credit outlook: Stable
Moody's/S&P ratings: A2/A-
Analyst coverage: Zixuan Liu

Company updates

China Huaneng Group (Huaneng) is China's second largest power generation company. It is 90% owned by China's central SASAC and 10% owned by the China Social Security Fund. The company's assets are mainly located in China. As of end-2023, it had total generation capacity of 243 GW, comprising coal power (59% of its capacity), wind power (16%), solar power (14%), and hydropower (11%). In the past few years, the company has rapidly expanded its clean energy capacity. As a major power house and a strategic player in China's clean energy transition, we think it will likely enjoy strong government support.

In 2023, Huaneng's profitability rebounded thanks to declining coal prices. Its gross and EBITDA margins increased to 22% and 30%, respectively, from 15% and 23% in 2022. Due to an aggressive expansion in clean energy capacity to support China's decarbonization initiatives, the company has incurred increasing capex (CNY 135bn in 2022 and CNY 182bn in 2023). This is expected to remain in place over the next three years. As such, we think the company's leverage will remain elevated. As of end-2023, its total liabilities (including perpetual bonds)-to-total assets was 74% and debt-to-EBITDA was 7x. However, Huaneng's liquidity is abundant, in our view. The company's cash-to-short-term debt was 60%. It also has credit facilities of CNY 2.6tr from major Chinese banks, CNY 1.8tr of which are unused.

Investment view

Our Stable outlook on Huaneng reflects our conviction that high government support will be extended if needed. In addition, the company's financial risks are manageable, in our view. As it continues to expand its clean energy generation capacity, earnings are expected to become more stable and less vulnerable to coal price volatility. Its coal mining business also supplies around 30% of its coal consumption for power generation. Despite high capex demand, the company's strong bank relationship allows for cheap funding, in our view. As such, we are comfortable holding Huaneng's senior bonds to maturity, and think the non-call risk of its perpetual notes is low. We think the new Huaneng 5.3% perpetual offers a good coupon carry.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) deteriorating credit metrics in the case of persistent high coal prices and insufficient cost pass-through; and 3) debt-funded capex or acquisitions to ramp up its clean energy capacity at a more aggressive pace than expected.

China General Nuclear Power Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: A2/A-
Analyst coverage: Zixuan Liu

Company updates

China General Nuclear Power Corporation (CGNPC) is the largest nuclear energy operator in China. As of end-2023, its installed nuclear power generating capacity was 30.6GW, equivalent to over 50% of China's total installed capacity. The company, which is 90% owned by the central SASAC and 10% owned by the Guangdong provincial government, is strategically important to China's nuclear energy development and security.

CGNPC reported steady financial results for 2023. Total revenue and EBITDA increased 9% and 8%, respectively, driven by climbing installed capacities and on-grid power generation. Gross margin and EBITDA margin dipped slightly to 36% and 50%, respectively. Debt levels edged higher after a 14% increase in capex, with a debt-to-EBITDA ratio at 8x. Thanks to low onshore funding costs and the company's strong banking relationships due to government support, average funding costs fell to 2.8% and the EBITDA-to-interest multiple was maintained at a decent level of 4.7x.

Investment view

We have Fair ratings on CGNPC's USD and EUR bonds. We believe the company will maintain its leadership and strategic importance in China's nuclear power industry, and strengthen its position in clean energy. It will likely steadily expand its clean energy capacity in accordance with the government's long-term goal on the back of forceful policy and financial support. While this means high capex demand, we think the associated financial risks are mitigated by its strong financing capability.

US investors cannot trade CGNPC's bonds. The company was added to Executive Order (EO) 13959, signed by then-US President Donald Trump on 12 November 2020, which bans all US persons from purchasing and selling the securities of companies identified by the US government as "Chinese military companies." President Joe Biden expanded the scope of EO 13959 and signed EO 14032 on 3 June 2021, prohibiting US investors from investing in Chinese companies with ties to China's military or surveillance industry, as identified by the US government.

Key downside risks to our view include: 1) negative ratings actions on China's sovereign credit due to prolonged macroeconomic weakness; 2) a material deterioration of the company's standalone credit profile; 3) a decline in the strategic importance of the nuclear power industry in China; and 4) weakening government support. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

Sinochem Hong Kong

UBS credit outlook: Stable
Moody's/S&P ratings: A3/A-
Analyst coverage: Timothy Tay

Company updates

Sinochem HK is the 100%-owned sole offshore financing platform and the key overseas asset holding company of Sinochem Holdings. Sinochem Holdings, 100% owned by the central SASAC, was established in May 2021 from the merger of Sinochem Group and China National Chemical Corp (ChemChina). It is the largest chemical company in the world and the only chemical SOE in China that carries an important policy role in China's energy and food security. In 2022, the company's revenue reached CNY 1.2tr. We expect extraordinary government support to be extended to Sinochem Holdings and its key subsidiaries if needed.

Sinochem HK is the largest shareholder of China Jinmao Holding Group (Jinmao). It owns a 35% stake in Jinmao and fully consolidates its financials. In 2022, Jinmao accounted for almost all of Sinochem HK's revenue and EBITDA, and has been a main reason for its parent's high leverage. Sinochem HK's debt-to-EBITDA climbed from 9x in 2021 to 11x in 2022. Given the continuous softness in China's property sector, the company will likely see further margin erosion and leverage hovering on the high side.

Investment view

Sinochem HK's standalone financials are expected to be hurt by the protracted property downturn and Moody's has a negative outlook on the company given Jinmao's deteriorating fundamentals. However, we think the impact on Sinochem HK's creditworthiness is limited. As an extension of Sinochem Holdings, we believe it will likely receive extraordinary support from its parent and the Chinese government. We therefore keep our Stable credit outlook on the company. Due to the cyclical business nature of the chemical industry and Sinochem Holdings' high leverage, Sinochem HK's bonds offer a slight yield pickup against the bonds issued by other central SOEs. We think they offer good carry and are comfortable owning them over the medium to long term.

Sinochem and ChemChina were included in the US Executive Order 13959 in November 2020 under the Trump administration that banned US persons from investing in certain Chinese companies. That had led to a sell-off in their bonds, with a subsequent recovery taking around 6 months to complete. The Biden administration removed the two names via a new Executive Order 14032, but the US Department of Defense (DoD) added ChemChina to the list of "Chinese military companies" in 2022. While potential

US sanctions remain an overhang for the Sinochem-ChemChina complex, we do not see the fundamentals and financing capabilities as constrained by such sanctions. We therefore think any future sanctions-related sell-off could be a buying opportunity for investors.

Key downside risks to our view include: 1) negative rating actions on China's sovereign credit due to prolonged macroeconomic weakness; 2) negative developments in China's property market and economy that further weigh on Sinochem Holdings' fundamentals; 3) reckless debt-funded moves that further lift Sinochem Holdings' leverage; 4) a strategic shift from the parent that reduces the importance of Sinochem HK; and 5) further US sanctions on Sinochem Holdings and its subsidiaries. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China National Chemical Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/A-
Analyst coverage: Zixuan Liu

Company updates

China National Chemical Corporation (ChemChina) is a 100%-owned core subsidiary of Sinochem Holdings, the world's largest chemical company and China's sole chemical SOE with large strategic importance. ChemChina is mainly involved in life science (agrochemicals and animal nutrition, 54% of the 2023 revenue), basic chemicals (mainly petrochemicals, 15%), rubber and tire (15%) and material science (13%) businesses via a handful of global subsidiaries. ChemChina accounts for around 40%, 50%, and 70% of SinoChem Holdings' revenue, total assets, and total debt.

In 2017, ChemChina acquired Syngenta AG, with support from the Chinese government, and became highly leveraged as a result. The company has planned for an A-share listing of Syngenta to deleverage, but progress has been slow due to market volatility. The very high leverage, sizable interest expenses, and high capex are ChemChina's major credit risks. As of end-2023, ChemChina's total debt-to-EBITDA had climbed to 11x with EBITDA-interest-coverage ratio falling to 2.3x. Sector cyclicality is also another credit concern. In 2023, ChemChina's agrochemical and specialty chemical units suffered from both overcapacity and weak demand globally, seeing prices drop from the high 2022 base. As a result, the company's revenue and EBITDA fell 8% and 19% y/y, respectively. Its EBITDA margin was 12%, lower than its global and domestic peers (Bayer, Dupont, and Wanhua Chemical Group).

Investment view

ChemChina's credit profile was strengthened after the merger as the consolidated parent Sinochem Holdings sits in a more critical position among central SOEs. Despite mounting leverage, ChemChina will likely secure cheap refinancing with support from the parent and the Chinese government. ChemChina's bonds are now trading close to the same levels as Sinochem HK, despite a two-notch rating difference by Moody's. We think both pricings are Fair given the same ultimate parent and expected level of support.

ChemChina is included in the list of "Chinese military companies" issued by the US Department of Defense (DoD) in 2022. While the list itself does not impose any investment restrictions, it implies a higher possibility of future negative action. However, after a sell-off during 2020–21 when it was targeted by Trump's Executive Order 13959, we think most bondholders are non-US investors with high conviction on the company's credit strength. We therefore do not expect significant market volatility if future sanctions arise, and we see any sanctions-related sell-off as a buying opportunity. In addition, the listing of Syngenta is a future positive catalyst to watch.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a prolonged industry downturn that further squeezes ChemChina's margins; 3) a strategic shift from Sinochem Holdings that weakens ChemChina's asset base; 4) large capex or reckless debt-funded acquisitions that further increase its leverage; and 5) further US sanctions on Sinochem Holdings and its subsidiaries. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals (including a successful IPO of Syngenta AG), and a strengthening of government ties.

China Jianyin Investment Ltd

UBS credit outlook: Stable
Moody's/S&P ratings: A2/A
Analyst coverage: Timothy Tay

Company updates

China Jianyin Investment Ltd (JIC) is the wholly-owned investment platform of Central Huijin, which owns and manages key state-owned financial institutions on behalf of the central government and is 100%-owned by China Investment Corp (CIC), China's sovereign wealth fund. Supervised by the Ministry of Finance, JIC plays an important policy role in facilitating national strategy and plans. The company invests in companies in strategic industries such as advanced manufacturing, mass consumption, and information technology as part of its directive to enable China's economic transformation. Additionally, JIC has occasionally been tasked with restructuring underperforming financial institutions in order to safeguard the stability of China's financial system.

As of end-2023, JIC's total consolidated assets amounted to CNY 1.8tr. Equity investments and asset management account for around 35% of assets, while the balance is in financial services. JIC's investment portfolio is well-diversified by industry and geography and benefits from recurring investment income, which accounts for the bulk of its parent-level income. JIC's assets under management (AUM) is expected to grow over the next few years, primarily driven by its mutual fund unit Guotai Asset Management. By contrast, its trust business JIC Trust, which has seen sizable outflows, may face continued pressure from the stress in the Chinese property sector. In FY23, JIC posted EBITDA of CNY 46bn (+5.2% y/y), while net profit jumped 21.6% y/y to CNY 31bn. As of end-2023, JIC had CNY 640bn of interest-bearing debt, while its cash balance was healthy at CNY 132bn. Net leverage is high at 11.1x, but gearing (total debt/assets) remains reasonable at 44.7%.

Investment view
We view JIC as strategically important to the Chinese government and expect support if required. Due to its government linkage, JIC also enjoys favorable borrowing terms from major policy and state-owned banks. JIC's financial and credit profile is healthy, with the company boasting sound liquidity and manageable gearing. Valuation-wise, JIC's USD bonds trade at comparable levels to other state-owned investment companies and large Chinese banks. We are comfortable holding JIC's USD bonds, as we think the issuer's credit risk is tied to the China sovereign.

Key downside risks to our view include: 1) negative ratings actions on China's sovereign credit due to prolonged macroeconomic weakness; 2) a weakening of JIC's government ties; 3) sharper-than-expected AUM outflows; and 4) overly aggressive debt-funded investments or acquisitions to fulfil policy initiatives.

CITIC Limited
UBS credit outlook: Stable
Moody's/S&P ratings: A3/A-
Analyst coverage: Zixuan Liu

Company updates
CITIC Limited (CITIC Ltd) is the largest conglomerate in Asia. It has businesses in a wide range of industries, including financials, resources and energy, manufacturing, property and infrastructure development, construction, and others. Its financial segment, mainly run by China CITIC Bank Corporation Limited (CITIC Bank, 67% owned by CITIC Ltd) and CITIC Securities, makes up around 80% of its assets, 30% of revenue, and the majority of its profit. As of end-2023, its total assets were over CNY 12tr (+6% y/y).

CITIC Ltd is effectively 54%-owned by CITIC Group, which is ultimately 100% owned by China's Ministry of Finance. The company was established in 1979 to lead China's opening and reform initiatives, and is expected to continue playing a leading policy role. Its strong government ties suggest extraordinary support will be extended if needed.

In 2023, CITIC Ltd's financial segment CITIC Bank reported weaker earnings but improving asset quality. The net interest margin (NIM) edged down from 1.97% to 1.78%, pressured by lower loan yields. Fee income was 13% y/y lower as higher trading gains were offset by a weak wealth management business. Asset quality improved with the non-performing loan (NPL) ratio falling from 1.27% to 1.18% after active NPL disposals.

CITIC Ltd's non-financial segment has maintained a low leverage of 1.5x loans-to-EBITDA. Gross margins grew 10% y/y in 2023 despite a flat top line. Key profit contributors are CITIC Special Steel (focusing on high-end products) and Tianjin Pipe Corporation.

Investment view
We have a Stable credit outlook on CITIC Ltd and a Fair rating on its USD bonds. We expect CITIC Ltd to continue to enjoy strong government support, and its diversified business profile should allow it to maintain a decent financial performance. CITIC Group participated in the recapitalization of China Huarong Asset Management Company (renamed as China CITIC Financial Asset Management Company recently) in 2021, becoming its largest shareholder. This is slightly credit negative for CITIC Group and in turn CITIC Ltd, but we think the impact is limited.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a weakening of CITIC Group's government ties; and 3) large capex or reckless debt-funded acquisitions that further increase CITIC Group or CITIC Ltd's leverage. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China Minmetals Corporation
UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Zixuan Liu

Company updates
China Minmetals Corporation (CMC) is China's largest and a leading global metal and mining conglomerate. It is 90% owned by the central SASAC and 10% owned by the China Social Security Fund. It ranks in the first quartile among the 53 backbone central SOEs defined by the central SASAC. In 2023, its total assets exceeded CNY 1.1tr. The company's largest segment is metallurgical construction, which contributes 56% and 49% to its revenue and gross

profit, respectively. Those operations are mainly carried out by its listed subsidiary Metallurgical Corporation of China (MCC). The company's second largest segment is metals and mining (19% of revenue and 29% of gross profit). Its assets span across various geographies and include top-tier reserves of copper, zinc, antimony, and tin. That said, the metal and mining businesses are subject to high metal price volatility and high operational risks.

In 2023, CMC's metallurgical construction segment reported robust top-line growth of 12% y/y, thanks to a healthy contract pipeline of around four times annual revenue. Metals and mining was up 6% y/y, thanks to increasing domestic demand with policy support. However, gross margins saw a sequential year of decline to 16% (vs. 17% in 2022 and 35% in 2021) due to rising energy prices and high global inflation. Overall gross margin and EBITDA margin were maintained at 10% and 6%, respectively. Margin compression hurt leverage, with debt-to-EBITDA edging up to 6.3x. Liquidity is strong. Cash-to-short-term debt coverage reached 73%, with credit facilities of around CNY 1.5tr.

Investment view
We have a Stable credit outlook on CMC and a Fair rating on its USD bonds. Strong technicals support the bonds' relatively tight valuations. The company has a strong track record of receiving government support via policies, resources, funding, and taxes, and we expect this to continue. Fundamentally, CMC's metallurgical construction segment should continue to benefit from its strong order backlog, although rising counterparty credit risk is worth noting given China's macroeconomic situation. While the company's metal and mining segment will likely continue to be volatile given geopolitical uncertainty, its diversified product mix, and economics of scale should limit further margin downside, in our view.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a weakening of CMC's government ties; 3) large capex or reckless debt-funded acquisitions that further increase CMC's leverage; and 4) a sharp drop in revenue and EBITDA due to the underproduction of upstream metal and mining products or significantly lower commodity prices. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

Power Construction Corp of China

UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Zixuan Liu

Company updates
Power Construction Corp Of China (PCCC) is a leading Chinese construction company that specializes in power (in particular hydropower), power grid, and other infrastructure projects. 80% of the company's revenue and 70% of the gross profit come from its engineering and construction (E&C) segment. Compared to other construction SOEs, PCCC is more globally diversified. It participates in many overseas infrastructure projects that underpin important diplomatic ties with foreign countries, especially in Africa and the Middle East. The company is 100% owned by China's central SASAC.

PCCC has high leverage, with 10x debt-to-EBITDA and a 76% liabilities-to-assets ratio. It has been using perpetual notes to control its leverage. The company has high capex commitments in new energy markets to support China's decarbonization initiatives. Strong growth in wind and solar power projects is expected to buffer a slowdown in hydro and thermal power projects. From 2016 to 2022, the company had an annual capex of CNY 40–80bn, and it is expected to stay in this range over the next two years. That said, the investment has been concentrated in projects and power plants that have better yields. Its gross margin and EBITDA margin are stable at 12% and 7% respectively. EBITDA has grown steadily (+6% y/y in 2021 and +11% y/y in 2022), leading to relatively stable leverage levels.

Investment view
All of PCCC's outstanding USD bonds are perpetual notes with a 300bps coupon step-up on the call date. These perpetual notes are currently trading at a high-5% yield-to-call, with a limited yield pickup to other senior SOE bonds. We think the pricing is fair, given a low non-call risk and PCCC's low credit risk. The company recently called a USD 500mn perpetual note callable in June 2024. While its high leverage is a bit concerning, we think the risk is mitigated by its easy access to funding and high likelihood of receiving extraordinary government support, if needed.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a weakening of PCCC's government ties; and 3) failure to control leverage, triggering ratings downgrades, or large capex or reckless debt-funded acquisitions that further increase PCCC's leverage. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China State Construction International

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Zixuan Liu

Company updates

China State Construction International (CSCI) is a 65%-owned subsidiary of China State Construction Engineering Corporation (CSCEC), which in turn is a major SOE 100% owned by China's central SASAC and also the largest engineering and construction (E&C) contractor in the world. CSCI's business spans across Greater China and holds a leading position in both Hong Kong and Macau for large projects, including housing, hotel, and infrastructure construction. Despite a relatively smaller size compared to its central SASAC-owned E&C peers (total assets of CNY 249bn as of end-2023), we expect strong support from both the CSCEC and the Chinese government, if needed.

Thanks to its strong market competitiveness and solid order backlog, CSCI recorded 11% y/y revenue growth and 16% y/y EBITDA growth in 2023. Mainland China, Hong Kong, and Macau contribute to 58%, 27%, and 9% of CSCI's revenue and 79%, 9%, and 6% of its gross profit, respectively. Mainland China has a higher gross margin (19% vs. 5% for Hong Kong and 9% for Macau) due to its participation in high-margin investment-linked projects and public-private-partnership (PPP) projects. However, this is expected to trend lower as the company is in a business transformation to reduce long-term projects and focus on government targeted repurchase (GTR) projects with faster turnover and a shorter cash collection cycle. It has also been reducing its dependence on PPP projects. That said, the downside is expected to be partially compensated by better margins in Hong Kong as the company exits from lower-margin pandemic-related construction projects. More importantly, the new business mix has allowed CSCI to deleverage from 7.6x debt-to-EBITDA in 2020 to 5.4x. EBITDA-to-interest coverage also improved from 2.5x to 4x.

Investment view

We have a Stable credit outlook on CSCI and a Fair rating on its USD bonds. Credit metrics can further improve from here, in our view, supported by a strong order backlog, faster cash conversion, and controlled capex. The company will likely remain strategically important to CSCEC given its strong footing in the Greater Bay Area, and is expected to receive parent and government support. Both its PerpNC24 and PerpNC26 have a coupon step-up of 300bps if not called. We think the non-call risk is low, and the market has priced them close to the senior bonds at mid-5%. We think strong market technicals will support performance.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit ratings due to prolonged macroeconomic weakness; 2) a weakening of CSCEC's government ties and a weakening of CSCI's strategic importance to its parent; 3) margin deterioration, and 4) larger-than-expected capex or reckless debt-funded acquisitions that spike CSCI's leverage. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China Merchants Port Holdings Company Limited

UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Zixuan Liu

Company updates

China Merchants Port Holdings Company (CMPort) is mainland China's largest port developer and operator. It controls or invests in major port hubs in cities along the coast of Greater China, and is also a global port investor. As of end-2023, CMPort owned stakes in 46 ports across 26 countries and regions. In 2023, its container throughput reached 137.5mn twenty-foot equivalent units (TEUs), with Greater China and overseas operations accounting for 75% and 25%, respectively. CMPort's controlling shareholder, China Merchants Group (CMG, 69.6% ownership), is a conglomerate that is 100% owned by the central SASAC.

In 2023, CMPort's results were adversely affected by an ongoing restructuring of global supply chains and a soft global economy. The company saw revenue, EBITDA, and net income fall 8%, 6%, and 18%, respectively. EBITDA margin was stale at 56%, whereas net margin compressed from 72% to 64% due to the disposal of its Ningbo subsidiary. Other credit metrics were still robust, with EBITDA-to-interest coverage and debt-to-EBITDA unchanged at 3x and 6x. Its total liabilities accounted for around just 30% of total assets.

Investment view

Our Stable credit outlook on CMPort hinges on its significant strategic importance to CMG, a high likelihood of government support, and its globally diversified port portfolio. These should allow it to navigate global economic cycles and credit difficulties. In addition, the global economy has been doing better than expected this year, and the geopolitical tension in the Middle East has benefited the company's operations. Deleveraging may continue, in our view, in the absence of major acquisitions. As such, we rate CMPort's USD bond curve as Fair.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a worse-than-expected container throughput decline due to a softer global economy or rising geopolitical tensions; and 3) large acquisitions funded by debt that materially increase the company's financial risk. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

AVIC International Holding Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: NR/BBB-
Analyst coverage: Zixuan Liu

Company updates

AVIC International Holding Corporation (AVICIH) is 91% owned by the Aviation Industry Corporation of China (AVIC). AVIC in turn is 100% owned by China's central SASAC, and is dominant in R&D, operations, manufacturing, and financing in China's aviation industry. It is a key supplier for commercial aircraft manufactured in China, and is also a top global defense contractor. AVICIH is AVIC's sole supply chain service platform. It has a substantial market share of China's aviation import and export industry. In 2020, AVIC and some of its subsidiaries (excluding AVICIH) were included in the list of "Chinese military companies" issued by the US Department of Commerce.

Other than the aviation segment (19% of its 2023 revenue), AVICIH also engages in advanced manufacturing (28%), overseas utilities in Belt and Road countries (7%), and other services and trading (45%). These businesses are carried out by various listed and unlisted subsidiaries, with the parent company serving as an investment holding company. The diversified business portfolio allows the company to generate stable financial results. In 2023, total revenue edged up 1% and EBITDA rose 4% despite some headwinds to its international businesses amid geopolitical tensions. Consolidated total debt is high as the subsidiaries have strong funding capability. Including perpetual notes, it has a debt-to-EBITDA of 10x. Due to the company's strategy of adding and upgrading its electronics-related capacity, capex of CNY 7–9bn is expected in the next 12 months, which will keep leverage high. That said, the company enjoys low-cost funding, with EBITDA-to-interest at 4x. Liquidity is strong, with CNY 77bn in bank credit facilities as of March 2024 (CNY 53bn unused).

Investment view

We have a Stable credit outlook on AVICIH and a Fair rating on its USD bonds. We expect strong debt servicing capability thanks to the company's easy financing access. Government support is expected to be strong and timely, given parent AVIC's strategic importance to China's aviation sector development. On fundamentals, weak global demand for its electronics business should be compensated by a domestic consumption recovery and government support in the sector.

Key downside risks to our view include: 1) negative ratings action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a weakening of AVIC's government ties and a weakening of AVICIH's strategic importance to the parent; 3) margin deterioration due to a downturn in the electronics sector, and 4) larger-than-expected capex or reckless debt-funded acquisitions that spike AVICIH's leverage. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China Taiping Insurance Holdings

UBS credit outlook: Stable
Moody's/S&P ratings: NR/BBB+
Analyst coverage: Zixuan Liu

Company updates

China Taiping Insurance Holdings (CTIH) is a fully-owned subsidiary of China Taiping Insurance Group, which is ultimately 90% owned by mainland China's Ministry of Finance. Listed in Hong Kong, CTIH holds all the group's major insurance operations, including life, pension, property and casualty (P&C) insurance and reinsurance in mainland China and Hong Kong, and overseas P&C insurance.

In 2023, CTIH's fundamentals showed signs of stabilization with a narrowing investment loss and a higher after-tax profit (+23% y/y) despite a 5% decline in its contractual service margin. The company's investment portfolio grew 15% y/y to HKD 1,350bn, with the total investment yield at 2.7% (vs. 1.2% in 2022). New business value for Taiping Life climbed 28% y/y in yuan terms, reflecting higher premiums for savings-type policies and the company's leading individual agency and bancassurance channels. Solvency ratios at major subsidiaries remained adequate under C-ROSS Phase II and strengthened to top peers due to debt issuances in 2023, including the CNY 11bn perpetual capital issued by Taiping Life and the USD 2bn perpetual subordinated bond callable in 2028.

Investment view

We have a Fair rating on CTIH's 6.4% perpetual subordinated bond callable in 2028. The bond is trading at a 5.1% yield-to-call after massive spread tightening since its issuance, thanks to its high carry. While the company could continue to see improving fundamentals in light of a stabilizing property market in China, the optimism is already in the price, in our view.

Key downside risks to our view include: 1) falling onshore interest rates; and 2) a sharp correction in Chinese equity markets. Key upside risks for the bonds include faster-than-expected Fed cuts, stronger investment results due to rising onshore interest rate, and a strengthening of government ties.

BOC Aviation

UBS credit outlook: Stable
Moody's/S&P ratings: NR/A-
Analyst coverage: Eve Li

Company update

BOC Aviation (BOCA) is one of the world's largest aircraft leasing companies. Bank of China is BOCA's ultimate controlling shareholder, with a 70% stake as of end-2023. As of end-April 2024, BOCA had a total fleet of 688 aircraft owned, managed, or on order, with an average fleet age of 4.8 years and an average remaining lease term of 7.9 years. Its aircraft utilization rate remains high at 99%. BOCA's lease portfolio is diversified both by airline customers and geography. The top three customer regions were the Americas (27%), APAC excluding Greater China (23%), and Greater China (23%) as of end-2023.

In 2023, BOCA reported USD 764mn in net profit compared to just USD 20mn in 2022. The sharp rise was driven by a 7% increase in revenue and a significant reduction in aircraft impairments. Operating lease rental income continued to contribute the most to the top line, accounting for 78% of the total revenue of USD 2.5bn. The lease rate factor rebounded to 10% (from 9.2% in 2022). Net lease yield, however, increased at a milder pace to 7.1% (from 7%), due to a rising cost of debt of 4.1%. Supported by a high collection rate of over 100%, its operating cash flow net of interest continued to improve to USD 1.6bn in 2023 from USD 1.5bn in 2022.

The full-year capex was USD 3.6bn, slightly behind management's guidance of USD 4bn. With the supply of passenger aircraft still tight, the company has used the purchase and leaseback (PLB) channels to enrich its portfolio. In 2023, it acquired 45 aircraft under PLB, versus 21 from its orderbook. Total debt increased 9% y/y to USD 16.5bn to partly fund the capex. That said, debt-to-equity was stable at 2.9x. BOCA's total available liquidity was sufficient at USD 5.6bn as of end-2023, including USD 5.2bn in undrawn committed credit lines (of which USD 3.5bn was from Bank of China).

Investment view

We expect the operating environment to remain favorable for BOCA, with resilient global air passenger traffic demand. According to the company, the industry needs to fund around USD 95bn of aircraft this year, and USD 121bn in 2025. We believe operating lessors with cheaper funding costs and deep industry knowhow will continue to gain market share. While we estimate its rating buffer, measured by EBIT/interest expenses under S&P's methodology, slightly weakened in 2023 due to higher borrowing costs, we still expect a stable rating trajectory over the next 12 months. BOCA's issuer rating benefits from a two-notch uplift from its stand-alone credit profile, considering its strategic importance to Bank of China. We currently rate most of its curve as Fair.

Key downside risks to our view include: 1) an unexpected deterioration in BOCA's importance to its parent and a rating downgrade for Bank of China; 2) a weaker-than-expected industry operating environment, leading to a declining lease rate factor; and 3) an aggressive debt-funded fleet expansion. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

China's local SOEs/LGFVs

Figure 18 - China's local SOEs / LGFVs covered in this report and their respective credit views

Issuer	CIO outlook	Rating (Mdy/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
Shandong Hi-speed Group	Stable	A3/NR				
Guangzhou Metro Group	Stable	A1/NR				
Wuhan Metro Group	Stable	A3/NR				
Yiwu State-owned Capital Operation	Stable	Baa3/NR				
Chongqing Nan'an Urban Construction and Development Gro	Deteriorating	NR/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 2 - Key financial & credit metrics (as of end-2023)

Issuer (Corporate)	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total liabilities / Total assets
Shandong Hi-speed Group	36.6	20.0%	81.0	9.9x	3.0x	75%
Guangzhou Metro Group	2.0	14.6%	32.7	103.9x	0.7x	57%
Wuhan Metro Group	0.9	14.6%	35.4	247.5x	0.1x	67%
Yiwu State-owned Capital Operation	5.1	17.1%	16.4	16.7x	2.2x	74%
Chongqing Nan'an Urban Construction	0.7	20.1%	3.8	26.6x	1.1x	66%

Source: Company, UBS

Shandong Hi-speed Group

UBS credit outlook: Stable
Moody's/S&P ratings: A3/NR
Analyst coverage: Zixuan Liu

Company updates

Shandong Hi-speed Group (SDHS) is the largest SOE/ LGFV in Shandong in terms of total assets (CNY 1.5tr, +14% y/y in 2023) and its debt accounts for around 80% of the provincial-level LGFV debt. The company engages in expressway operations and other strategic businesses. Although its non-transportation commercial business has became more prominent over the past few years, such that 25% of its revenue came from the sales of petrol products, its mega-size and strategic role ensure a high likelihood of government support, in our view. Shandong is China's third-largest provincial economy, with a GDP of USD 1.3tr as of 2023. Despite high government leverage (including LGFV debt) and a relatively weak banking sector, the province's ability to support its SOEs is considered strong, in our view.

Mounting leverage is a major credit concern for SDHS, in our view. Due to its demanding capex and high interest and dividend spending, the company consistently generates negative free cash flow and depends on external funding to sustain its operations. SDHS saw debt-to-EBITDA climbing from 9.4x in 2021 to 11x in 2023. That said, the company has a strong track record of receiving government support in the form of asset injections, exclusive operation rights, and top management designation. Onshore capital market and bank financing remain sound. As of end-2023, SDHS had credit lines of around CNY 1.3tr, with nearly half unused.

Investment view
With the Chinese government focusing on containing tail risks in the LGFV sector and the financial system, we are comfortable taking on more risk and see relative value in SDHS's bonds. SDHS acts as a high beta candidate in the China IG space given its similarity to an LGFV company and inability to generate positive free cash flow. In addition, Shandong's history of debt issues only adds to investor concerns. That said, we believe the company is systemically important to the province's financial system. It is expected to maintain its strong debt servicing capability.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; 2) an aggressive debt-funded expansion by the company that significantly increases its leverage; and 3) any sign of declining government support. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

Guangzhou Metro Group
UBS credit outlook: Stable
Moody's/S&P ratings:A1/NR
Analyst coverage: Zixuan Liu

Company updates
Guangzhou Metro Group (GZ Metro), 100% owned by the Guangzhou municipal government, is the sole construction and operating entity of Guangzhou's metro system. It is one of the largest SOEs in Guangzhou, and its metro network is considered one of the most extensive in the world. It also engages in residential and commercial property development around its metro stations, and provides consulting services to other railway operators in China and overseas. Guangzhou, the capital of Guangdong province, is a top-tier city with healthy fiscal revenue and a below average debt ratio (local government and LGFV debt-to-GDP ratio at 27%). It possesses a strong ability to coordinate domestic financial resources to support the needs of its strategically important SOEs and LGFVs, in our view.

GZ Metro's operation relies heavily on financial and policy support from local and higher-tier governments. Preferrable arrangements for its land acquisitions, tax reductions, and financial subsidies are granted by the local government. Given its policy role, the company has low margins and high capex demand. Its metro operation had a negative gross margin of –30% and an overall gross margin of 8% in 2023. The company's debt has ramped up rapidly since 2017, with total liabilities-to-total assets rising from 39% to 58%, and EBITDA-to-interest coverage declining to 0.7x. As of end-2023, the company's railway projects under construction demanded a future capex of CNY 110bn (vs. its total debt of CNY 232bn), which must be met by external financing.

Investment view
We have a Stable credit outlook on GZ Metro and Fair rating on its USD bonds (keepwell structure with liquidity support deed). While GZ Metro has low profitability and elevated leverage, we expect it to enjoy easy funding access and strong debt servicing capability. It is considered strategically important to the local government, and any credit concern could raise systemic risk to the local financial market, in our view.

Since the Politburo meeting in July 2023, when the Chinese government prioritized defusing heightened LGFV debt risks, supervision over LGFV debt has been strict. Liquidity needs are closely monitored and various financial resources have been allocated to avoid any credit events. In addition, the local government bond to LGFV debt swap program has been carried out as planned, resulting in a sharp tightening of LGFV bond spreads in weaker regions. As such, we expect the Guangzhou government to proactively provide sufficient and forthcoming support to GZ Metro, if needed.

Key downside risks to our view include: 1) negative rating actions on China's sovereign credit due to prolonged macroeconomic weakness; 2) an aggressive debt-funded expansion by the company that significantly increases its leverage; and 3) any sign of a weakening role or declining government support. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

Wuhan Metro Group
UBS credit outlook: Stable
Moody's/S&P ratings:A3/NR
Analyst coverage: Zixuan Liu

Company updates
Wuhan Metro Group (WH Metro) is 88% owned by the Wuhan SASAC and 12% owned by the CDB Development Fund. It is the largest SOE controlled by the Wuhan SASAC in terms of scale, and the sole entity that constructs and operates the metro system in Wuhan. Wuhan is a major city in central China with strong industrial, commercial, and educational development. While its debt ratio (local government and LGFV debt-to-GDP) is relatively high at 78%, it has sufficient domestic financial resources to

support the refinancing needs of its strategically important local SOEs and LGFVs.

Given WH Metro's policy role, its metro operation segment remains loss-making (gross margin of –42% in 2023). In 2023, its resources development business was also adversely affected by the property downturn, dragging overall gross margin into negative territory as well. The company is highly leveraged due to its intensive expansion plan, with total liabilities-to-total assets at 67%, and EBITDA-to-interest coverage at 0.1x. Future capex demand remains high given its sizable projects under construction, which is expected to strain its credit profile.

Investment view

We have Stable credit outlook on WH Metro and a Fair rating on its USD bonds. While WH Metro has low profitability and elevated leverage, we expect it to maintain easy funding access and a strong debt servicing capability. It is considered strategically important to the local government, and any credit concern could raise systemic risk to the local financial market, in our view.

Since the Politburo meeting in July 2023, when the Chinese government prioritized defusing heightened LGFV debt risks, supervision over LGFV debt has been strict. Liquidity needs are closely monitored and various financial resources have been allocated to avoid any credit events. In addition, the local government bond to LGFV debt swap program has been carried out as planned, resulting in a sharp tightening of LGFV bond spreads in weaker regions. As such, we expect the Wuhan government to proactively provide sufficient and forthcoming support to WH metro, if needed.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; 2) an aggressive debt-funded expansion by the company that significantly increases its leverage; and 3) any sign of weakening policy role or declining government support. Key upside risks for the bonds include faster-than-expected Fed cuts, improving company fundamentals, and a strengthening of government ties.

Yiwu State-owned Capital Operation

UBS credit outlook: Stable
Moody's/S&P ratings:Baa3/NR
Analyst coverage: Zixuan Liu

Company updates

Yiwu State-owned Capital Operation (YSCO) is the largest LGFV that engages in public investments and services in Yiwu. The company is 85.6% owned by the Yiwu SASAC, with the remaining stake owned by Zhejiang Financial Development Company and Yiwu City Digital Intelligence Industry Development Group. Yiwu, known as "the capital of small commodity goods," is a county-level city in Zhejiang province that recorded a robust 8% y/y GDP growth and a top-ranking GDP per capita in 2023, driven by its tertiary industries. YSCO is the most important platform company under the local government and holds most of its state-owned assets. Its main business scope includes market operations, public transportation and water operations, affordable housing development, and regional infrastructure construction.

In 2023, YSCO's total revenue and gross margin jumped 36% and 135%, respectively, driven by a strong recovery in its small commodity market operation and property development segments. Thanks to the improving earnings, the company's leverage, as measured by debt-to-EBITDA, declined to 18.8x. YSCO has a strong track record of receiving government support. Its total subsidies and tax rebates from 2020 to 2023 reached CNY 8bn, accounting for close to half of its total EBITDA. EBITDA-to-interest coverage remained healthy at 2.2x. YSCO has multiple funding channels, thanks to abundant financial resources in the city, including banks and micro-lending companies. The company also has easy access to onshore and offshore debt capital markets.

Investment view

We have a Stable credit outlook on YSCO and a Fair rating on its USD bonds. The company is expected to continue carrying out its strategic role in Yiwu's development. Yiwu's municipal government has strong control and oversight over its daily operations, strategy, and personnel appointments. Any credit concern with the company could raise systemic risk in the local financial market, in our view.

Since the Politburo meeting in July 2023, when the Chinese government prioritized defusing heightened LGFV debt risks, supervision over LGFV debt has been strict. Liquidity needs are closely monitored and various financial resources have been allocated to avoid any credit events. In addition, the local government bond to LGFV debt swap program has been carried out as planned, resulting in a sharp tightening of LGFV bond spreads in weaker regions. As such, we expect Yiwu's government to proactively provide sufficient support to YSCO, if needed.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; and 2) any sign of a weakening policy role or declining government support. Key upside risks for the bonds include improving company fundamentals, and a strengthening of government ties.

Chongqing Nan'an Urban Construction and Development Group

UBS credit outlook: Deteriorating
Moody's/S&P ratings:NR/NR
Analyst coverage: Zixuan Liu

Company updates

Chongqing Nan'an Urban Construction and Development Group (CQNA) is the largest LGFV under the government of the Nan'an district of Chongqing. 92% owned by the Chongqing Nan'an District Bureau of Finance, the company holds over 70% of the district's state-owned assets and engages in infrastructure construction and primary land development. Nan'an is a core district that covers Chongqing's CBD area. It had GDP growth of 6.7% and tax income growth of 27.4% in 2023. Chongqing, one of China's four direct-controlled municipalities, is strategically important in central western China and is known for its industrial manufacturing of automobiles, electronics, chemicals, and machinery. Although the municipality's debt level is considered high with a local government and LGFV debt to GDP ratio of 93%, it has a track record of receiving significant fiscal support from the central government.

CQNA was commissioned by the local government to carry out capital intensive infrastructure projects and shantytown renovation projects that the government will pay back over a period of time. As a result, the company was stuck with a high debt-to-EBITDA of 33x in 2022 and 28x in 2023. Thanks to government backing, however, the company has easy funding access with onshore and offshore bond financing and bank loans accounting for 60% and 37% of its total debt, respectively. This is expected to compensate for its rising liquidity risk as its cash-to-short term debt coverage fell to 17% in 2023 (from 67% in 2022).

Investment view

We have a Deteriorating credit outlook on CQNA given Chongqing's high leverage and challenging financing situation for LGFVs in general. We think its USD bonds are trading at a Fair range. Despite its high leverage, the company's business model allows it to maintain an important policy role for the local government and receive solid financial support. The company has a track record of receiving subsidies in the CNY 400–500mn range annually, consisting of over 60% of its EBITDA. Any credit concern over the company could raise systemic risk in the local financial market, in our view.

Since the Politburo meeting in July 2023, when the Chinese government prioritized defusing heightened LGFV debt risks, supervision over LGFV debt has been strict. Liquidity needs are closely monitored and various financial resources have been allocated to avoid any credit events. In addition, the local government bond to LGFV debt swap program has been carried out as planned, resulting in a sharp tightening of LGFV bond spreads in weaker regions. As such, we expect the Chongqing government to proactively provide sufficient support to CQNA, if needed.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged macroeconomic weakness; 2) a further deterioration of the local government's fiscal conditions; and 3) any sign of a weakening policy role or declining government support. Key upside risks for the bonds include improving company fundamentals, and a strengthening of government ties.

China AMCs

Figure 19 - China AMCs covered in this report and their respective credit views

Issuer	CIO outlook	Rating (Mdy/S&P)	UBS risk flags: Senior			
			0-2y	2-5y	5-10y	>10y
China Cinda Asset Management Company	Deteriorating	Baa1/BBB+				
China Orient Asset Management Company	Deteriorating	Baa2/BBB				
China CITIC Financial Asset Management Company	Deteriorating	Ba1/BBB-				
China Great Wall Asset Management Company	Deteriorating	NR/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 3 - Key financial & credit metrics (as of end-2023)

Issuer (AMCs)	Net profit (USD bn)	Annualized ROAE	Impairment losses / Total income	Total assets (USD bn)	Capital adequacy ratio
China Cinda Asset Management Company	1.0	2.7%	13%	224.3	18.0%
China Orient Asset Management Company	0.3	1.3%	22%	179.0	14.8%
China CITIC Financial Asset Management Company	0.0	3.6%	45%	135.3	15.1%
China Great Wall Asset Management Company	0.3	2.8%	19%	77.9	n.a.

Source: Company, UBS

China Cinda Asset Management Company

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Zixuan Liu

Company updates

China Cinda Asset Management Company (Cinda AMC) is the largest distressed asset manager in China in terms of total assets (CNY 1.6tr as of 2023). It is 58% owned by the Ministry of Finance, was the first among the four major AMCs to be listed on the HKEX, and has remained the best-in-class among its peers, in our view. In 2023, net profit fell 3.3% to CNY 7bn, following a 44.4% decline in 2022. Income from restructured distressed assets decreased by 40% in 2023 as management proactively reduced the underlying asset balance by a similar magnitude in order to cut the portfolio's credit risk.

The asset quality of Cinda AMC's core distressed debt assets remains under pressure, in our view. This is reflected in the decreasing return on disposal-type distressed assets (from high-teens to 7.4% in 2023), and the heightened impaired asset ratio of its restructured distressed assets (13.7% in 2023). The proportion of impaired stage 3 assets also surged from 10.3% to 16.9%, alongside a significant increase in stage 2 assets (those with significant deterioration since origination). That said, Cinda AMC's overall exposure to the property sector is around 25.7%, materially lower than three years ago.

In 2023, Cinda AMC managed to decrease its risk-weighted assets by 4.2% to CNY 697bn. This supported the company's capital position, with its CET1 ratio, Tier 1 ratio, and total capital adequacy ratio (CAR) rising to 11.8%, 16.5%, and 18%, respectively.

Investment view

We think Cinda AMC has maintained its best-in-class position among the distressed asset managers given its sufficient capital buffer and lower property sector concentration. Despite a Deteriorating credit outlook, its bond performance will likely be supported by strong technicals. We are comfortable with our Fair rating on its senior bonds.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged property sector and macroeconomic weakness; and 2) weaker-than-expected government support for the AMCs via favorable shareholder restructuring or equity injections. Key upside risks for the bonds include improving company fundamentals resulting from stronger-than-expected recovery in China's property sector, and a strengthening of government ties.

China Orient Asset Management Company

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Zixuan Liu

Company updates

China Orient Asset Management Company (Orient AMC) ranks second in terms of total assets (CNY 1.3tr as of 2023) among the four major AMCs. It is 72% owned by the Ministry of Finance. Besides its core distressed asset management business, insurance and banking businesses make up a substantial part of its revenue and assets.

In 2023, Orient AMC's operating income and net profit were down 48% and 32%, respectively, squeezed by flat revenue growth and higher insurance costs (+17%). Credit impairment losses were impressively low at 6bps of its credit exposures (vs. 52bps in FY22 and 138bps in FY21), and total provisioning was stable for both loans to customers (4.6%) and debt assets (5.9%). The company also saw asset quality deteriorate, in line with a general trend among its peers, with the non-performing asset (overdue for longer than a year) ratio climbing to 9.1% from 7.7% in FY22 and 6% in FY21. That said, quality remains relatively healthy compared to the three other major AMCs. The total capital adequacy ratio improved from 13.8% in FY22 to 14.8%, above the regulatory requirement, but the CET1 ratio is undisclosed.

Investment view

Orient AMC's fundamentals have shown reasonable resilience over the past two years, when AMCs were required to focus on their core business and de-risk. Despite the non-disclosure of its CET1 ratio and other key metrics, the company's bonds are trading close to Cinda AMC's, reflecting high investor conviction in government support. We have a Fair rating on Orient AMC's USD curve, and believe in a smooth execution of any shareholder restructuring, if there is one.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged property sector and macroeconomic weakness; and 2) weaker-than-expected government support to the AMCs via favorable shareholder restructuring or equity injections. Key upside risks for the bonds include improving company fundamentals resulting from stronger-than-expected recovery in China's property sector, and a strengthening of government ties.

China CITIC Financial Asset Management Company (formerly Huarong AMC)

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Ba1/BBB-
Analyst coverage: Zixuan Liu

Company updates

China CITIC Financial Asset Management Company (CITIC FAMC) is a major distressed asset manager in China. Its largest shareholder is CITIC Group (26.5%), followed by the Ministry of Finance (25%). It was listed on HKEX in 2014 following Cinda AMC's listing. Following an aggressive expansion before 2018, the company's accumulated high risk has weighed on its profitability over the past few years. From 2018 onwards, the company turned its focus toward its core distressed asset management business and off-loading non-core businesses. As of end-2023, the company's total assets fell to CNY 962bn (vs. CNY 1.7tr in 2018) and income earning assets stabilized around CNY 542.5bn.

CITIC FAMC reported marginally positive net profit in 2023 (vs. CNY –33.4bn in 2022), largely attributable to the one-off paper gains from its investments in China Everbright Bank and CITIC Limited, as well as bond repurchases at below par. The core business, however, remained loss-making. Weak asset quality remains our top concern. The softness is evident in its elevated impairment losses, which accounted for 6.1% of total income earning assets (vs. 5.1% in 2022 and 1.3% in 2021). The proportion of stage 3 assets to its total cash flow generating debt instruments also stayed high at 46.4%. Similar to Cinda AMC, the company reduced its property exposure by 12% to CNY 104bn (49% in its core restructured distressed assets).

Helped by a return to positive profit, CITIC FAMC managed to improve its CAR to 15.11% in 2023 (from 15.07% in 2022), above the regulatory requirement of 12.5%. The company still failed to disclose its CET1 and Tier 1 capital ratios, which we believe comes with implicit consent from the regulators.

Investment view
Looking ahead, we think the company's capitalization remains vulnerable as its core operations still struggle to turn a positive profit. That said, the risk is manageable given the company's access to onshore funding, in our view, and we expect support from its parent or the government to remain forthcoming for it to meet capital adequacy requirements. We have a Fair rating on its curve.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged property sector and macroeconomic weakness; and 2) weaker-than-expected government support for the AMCs via favorable shareholder restructuring or equity injections. Key upside risks for the bonds include improving company fundamentals resulting from stronger-than-expected recovery in China's property sector, capital replenishment by strategic investors, and a strengthening of government ties.

China Great Wall Asset Management Company

UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Zixuan Liu

Company updates
China Great Wall Asset Management Company (Great Wall AMC) is the smallest in terms of total assets (CNY 554mn as of 2023) among the four major AMCs. It is 73% owned by China's Ministry of Finance. The company delayed its FY22 reporting by a year, adding to concerns over the asset quality risk of the AMC complex. In the fiscal year, the company incurred CNY 23.5bn of fair value losses on assets and CNY 20.8bn of credit impairment losses (+48% y/y from an already-high base in FY21). The net loss came to CNY 45.4bn, nearly wiping out the company's entire capital base. While it did report a net profit in FY23 (CNY 1.8bn) as asset valuations and credit impairments stabilized, the company's capitalization remained under substantial pressure. Great Wall AMC did not disclose its capital adequacy ratios for either FY22 or FY23, which we believe likely fell below regulatory requirements to single-digit levels.

In addition, concerns over its asset quality persist. In FY22 and FY23, the company aggressively raised its total provisioning for debt investments to 31% and 37%, respectively, compared to 11% for its peer Orient AMC. This reflects its weak asset quality amid China's property downturn (the stage 3 asset ratio is undisclosed).

Investment view
We think a capital replenishment is needed for Great Wall AMC. This can be done by introducing new shareholders that provide a fresh capital injection. In January, S&P suggested that a shareholder restructuring was being considered, which had led to the delay in financial reporting. We think regulators will stay accommodative in the restructuring process and ensure Great Wall AMC's credit is intact, similar to the approach taken for Huarong AMC in 2022. This was evidenced by the calling of Great Wall AMC's CNY 10bn onshore Tier 2 bond in May 2023 at a time when the company was already short of capital. We expect a relatively smooth capital restoration by shareholder restructuring and limited market volatility for its bonds. As such, we maintain our Fair rating on Great Wall AMC's USD curve.

Key downside risks to our view include: 1) negative rating action on China's sovereign credit due to prolonged property sector and macroeconomic weakness; and 2) weaker-than-expected government support to the AMCs via favorable shareholder restructuring or equity injections. Key upside risks for the bonds include improving company fundamentals resulting from stronger-than-expected recovery in China's property sector, capital replenishment by strategic investors, and a strengthening of government ties.

China's state-owned property developers

Figure 20 - China state-owned developers covered in this report and their respective credit views

Issuer	CIO outlook	Rating (Mdy/S&P)	UBS risk flags: Senior			
			0-2y	2-5y	5-10y	>10y
China Overseas Land & Investments	Deteriorating	Baa2/A-				
China Resources Land	Deteriorating	Baa1/BBB+				
Yuexiu Property	Deteriorating	Ba1/NR				
Yuexiu Real Estate Investment Trust	Deteriorating	Ba2/BBB-				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 4 - Key financial & credit metrics (as of end-2023)

Issuer (Property developers)	Revenue (USD bn)	EBITDA margin	Net debt/ EBITDA	Net debt/ total equities	EBITDA/ Interest	Unrestricted cash/ Short-term debt
China Overseas Land & Investments	28.5	16.7%	4.5x	39%	3.3x	2.6x
China Resources Land	35.3	21.2%	2.5x	35%	4.9x	1.5x
Yuexiu Property	11.3	10.0%	7.3x	69%	1.8x	2.0x
Yuexiu Real Estate Investment Trust	0.3	62.5%	14.5x	112%	1.2x	0.2x

Source: Company, UBS

China Overseas Land & Investments

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa2/A-
Analyst coverage: Daniel Tam

Company updates

S&P has upgraded China Overseas Land & Investments (COLI) from BBB+ to A-, citing the potential for indirect state support to enable the company to maintain its smooth funding channels and business profile, while purchasing land and investing in commercial properties amid the industry downturn. COLI was one of China's top three real estate developers in 2023, with high exposure to first- and second-tier cities. It is 56% owned by China State Construction Engineering Corp, which in turn is 56.3% owned by central government-owned China State Construction Engineering Corporation. COLI reported strong 2023 results, with higher earnings, lower leverage, and strong liquidity. Revenue, EBITDA, and net profit increased by 12.3%, 8.5%, and 10.1% in 2023. Better earnings strengthened EBITDA/interest to 3.5x (2022: 3.2x), resulting in a positive operating cash flow of CNY 35.3bn (2022: –CNY 10.5bn) and a positive free cash flow of CNY 21.8bn in 2023. Total and net debt declined by 4.7% and 5.1%, respectively, lowering net debt/equity to 39% (45% in 2022), while unrestricted cash covered 2.6x of its short-term debt (2022: 2.8x). The average borrowing cost was 3.55%, among the lowest in the industry.

Investment view

COLI ranked first in land acquisition value in 2023, of which first-tier cities accounted for 62.4%. These newly acquired projects should support more robust sales growth and higher profitability in the medium term. The company's contracted sales outperformed the average 100 developers, increasing 5.1% to CNY 309.8bn in 2023 and declining 17.6% y/y to CNY 148.4bn in 1H24. COLI's liquidity is strong, supported by healthy recurrent income generated from its investment property portfolio and good access to capital market and bank financing. The company has a CNY 15bn onshore corporate bond quota and raised CNY 3bn in late April by issuing 3-year and 5-year bonds at a cost of around 2.68%. The company has also announced a USD 4bn offshore medium-term note (MTN) program, which would make it the first Chinese real estate developer to tap the offshore bond market in 2024.

Key downside risks to our view include a further weakness in property sales in upper-tier cities, more aggressive land acquisitions, and weakened access to capital markets. A key upside risk for the bonds is faster-than-expected recovery in property sales.

China Resources Land (CRL)

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Daniel Tam

Company updates

China Resources Land (CRL) is 59.6% owned by China Resources Holdings, which in turn is wholly owned by the central government. The company has one of the largest and highest-quality investment property portfolios in the Chinese real estate sector. It had 76 shopping malls at the end of 2023 and will have another 16 malls by end-2024. Strong recurrent income covered 1.08x of gross interest expenses, plus dividend payments in 2023. CRL reported solid 2023 results, with higher earnings, lower leverage, and healthy liquidity. Revenue, EBITDA, and net profit increased by 21.3%, 27.7%, and 15.2%, respectively, in 2023. Robust earnings strengthened EBITDA/interest to 4.9x (2022: 4.2x) and lowered total debt/EBITDA to 4.6x (2022: 5.5x). Operating cash flow increased to CNY 47.4bn (2022: CNY 1.2bn), while free cash flow narrowed to negative CNY 3.5bn (2022: –CNY 49.2bn). CRL ranked third in land acquisition value in 2023, and we believe the company can achieve positive free cash flow in 2024 by slowing down its pace of land acquisition.

Investment view

CRL's contracted sales decreased 24.3% to CNY 228bn in 2023, but increased 33% y/y to CNY 120.9bn in 1H24. Rental income increased 26% to CNY 4.4bn in 2023. The company raised CNY 6.9bn through a REIT listing in 2023 and is expected to list more REITs to control its leverage in the medium term. The company raised a CNY 5.9bn corporate bond with a cost of 2.5% in May 2024 and is planning to issue CNY 4.2bn worth of asset-backed securities (ABS). We expect the company's financial profile to remain solid in the medium term, as a result of its strong access to the capital market.

Key downside risks to our view include a weaker-than-expected sales performance, over-aggressive land acquisition, and weaker access to funding. A key upside risk for the bonds is faster-than-expected recovery in property sales.

Yuexiu Property

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Ba1/NR
Analyst coverage: Daniel Tam

Company updates

Yuexiu Property is 43.4% owned by Guangzhou Yue Xiu Holdings (GYX) and 19.9% by Guangzhou Metro Group; the Guangzhou government wholly owns the latter two companies. Yuexiu Property holds 41.4% of Yuexiu Real

Estate Investment Trust (REIT) and 66.9% of Yuexiu Services Group. GYX provides guarantees on Yuexiu Property's onshore bonds. First-tier cities account for 48% of the total land bank.

Yuexiu Property reported weak 2023 results, with lower earnings, higher leverage, and slightly weaker liquidity. Revenue increased 10.8%, but EBITDA and net profit declined 29.9% and 25.5%, respectively, on narrowed gross margin and revaluation loss of investment properties. Weaker earnings lowered EBITDA/interest to 1.8x (2022: 2.4x), while total debt/EBITDA rose to 13x (2022: 7.7x). Operating cash flow increased to CNY 8.6bn (2022: CNY 3.7bn), while free cash flow turned to a positive CNY 6.5bn (2022: –CNY 5.2bn). The aggressive land acquisition raised the total and net debt by 18.2% and 9.6%, raising net debt/equity to 68.7% (2022: 62.7%), despite a HKD 8bn rights issue. Also, unrestricted cash/short-term debt declined to 1.3x (2022: 1.4x).

Investment view

Yuexiu's contracted sales increased 13.9% to CNY 142bn in 2023, but declined 33.8% y/y to CNY 55.4bn in 1H24. With more projects to launch in 2H24 and the company's high exposure to first-tier cities, the company's 2H24 sales should be stronger than in 1H24. Benefiting from its state-owned background, Yuexiu maintains good access to the capital market. The company issued CNY 6.9bn in onshore bonds and CNY 510mn in offshore CNY bonds in 2023. It also issued CNY 700mn in offshore CNY bonds in January 2024 and a CNY 1.7bn 3-year green bond in July.

Key downside risks to our view include a weaker-than-expected sales performance, over-aggressive land acquisition, and weaker access to funding. A key upside risk for the bonds is faster-than-expected recovery in property sales.

Yuexiu Real Estate Investment Trust

UBS credit outlook: deteriorating
Moody's/S&P ratings: Ba2/BBB-
Analyst coverage: Daniel Tam

Company updates

Yuexiu Real Estate Investment Trust (REIT) is 42.6% owned by Yuexiu Property. Yuexiu REIT owns and operates a portfolio of 10 properties, of which Guangzhou accounted for 70% of its leasable area in 2023. The office, wholesale, retail, and hotel/serviced apartment segments accounted for 68.5%, 10.5%, 9.3%, and 11.7% of total net property income last year.

Yuexiu REIT reported a mixed set of 2023 results, with a significant reduction in net loss, but funding costs and leverage remained high. Revenue and EBITDA increased 11.4% and 9.7%, respectively, while net loss fell sharply to CNY 4mn (2022: CNY 511mn loss). By replacing high-cost HKD/USD debt with lower-cost CNY-denominated debt, the company's interest expense declined 29.7%, with EBITDA/interest strengthening to 1.2x (2022: 0.8x). The proportion of CNY-denominated borrowings increased to 39% of total borrowings at end-2023, up from 6% a year earlier. Leverage increased, with gross and net debt rising 1.7% and 1.5%, respectively, while gross debt/assets edged up to 46.2% (2022: 45.5%). The company's average funding cost rose to a record 4.6% in 2023 (2022: 3.05%).

Investment view

Yuexiu REIT is highly exposed to the office segment, which is suffering from rising supply and declining occupancy rates. As a result, Yuexiu REIT's earnings are expected to remain weak in the near term. The management aims to replace more HKD/USD debt with onshore loans to further reduce its interest costs, and may consider disposing non-core assets to lower its leverage. Yuexiu REIT's liquidity is inadequate, in our view, with cash/short-term debt at a record low of 24% (2022: 31%) because it has to pay out most of its distributable income as dividends. However, the company's weak liquidity is mitigated by its good track record of refinancing maturing debt over the past few years and strong banking relationships, owing to its good asset quality and state-ownership background. We think the company is also likely to receive parent support, if necessary.

Key downside risks to our view include further weakness in the office rental segment, higher USD and HKD interest rates, and weaker access to funding. A key upside risk for the bonds is faster-than-expected recovery in property sales.

China tech

Figure 21 - China tech issuers covered in this report and their respective credit views

Company	CIO credit outlook	Rating (Mdy/S&P)	CIO credit risk flags			
			0-2y	2-5y	5-10y	>10y
Tencent Holdings	Stable	A1/ A+				
Alibaba Group Holding	Stable	A1/ A+				
Baidu Inc	Stable	A3/ NR				
Meituan	Stable	Baa3/ BBB				
Weibo Corp	Stable	Baa2/ BBB				
Lenovo	Stable	Baa2/ BBB				
Huawei	Stable	NR/ NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 5 - Key financial & credit metrics (the latest full year)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ interest	Total debt/ Cap
Tencent	85.9	38.7%	52.3	-0.1x	19.8x	29.8%
Alibaba	130.3	20.4%	28.4	-1.9x	24.1x	15.7%
Baidu Inc	19.0	26.6%	11.9	-3.1x	11.0x	25.0%
Meituan	39.0	8.8%	8.5	-3.5x	17.1x	28.5%
Weibo Corp	1.8	35.9%	2.7	-0.8x	5.3x	43.5%
Lenovo	56.8	6.4%	4.0	0.1x	4.8x	39.4%
Huawei	99.3	9.7%	45.0	-2.3x	5.1x	38.6%

Source: Company reports, UBS. FY2024 for Alibaba and Lenovo

Alibaba Group Holding Limited

UBS credit outlook: Stable
Agency ratings: A1/A+
Analyst coverage: Eve Li

Company updates

Alibaba is the largest retail commerce e-company globally by gross merchandise value (GMV). Its Taobao and Tmall e-commerce platforms are household names in China. Founded in 1999 by Jack Ma and other partners, the company has evolved and cultivated an integrated ecosystem around its value chain, enabling purchase, payment, and order fulfillment for online shopping. Beyond domestic and overseas e-commerce, Alibaba also runs cloud, local services, digital media, and other online businesses.

In FY24 (fiscal year ended 31 March 2024), its total revenue increased 8% to CNY 941bn, and adjusted EBITA grew 12% to CNY 165bn. The company has seen some progress made across its core businesses after several quarters of adjustments. In the 4QFY24, its Taobao and Tmall Group (TTG) achieved double-digit y/y growth in GMV. That said, TTG's revenue growth was much slower at 4% y/y during the quarter due to a mix shift toward Taobao and its lower take rate. The segment EBITA margin also decreased to 41% (from 46% in 3QFY24) on higher subsidies and incentives. According to management, the company will gradually introduce new monetization mechanisms in 2HFY25, which will attract more SME merchants and drive its customer management revenue (CMR). The international commerce segment (AIDC) continued to report strong revenue growth of 45% y/y in 4QFY24, accounting for 11% of the consolidated revenues. That said, its EBITA margin deteriorated to –15% (from –11% in 3QFY24), led by increased overseas investment on user acquisition and logistics capacity. The cloud intelligent group continued to generate positive EBITA, albeit at a narrower margin of 6% (vs. 8% in 3QFY24).

The company maintained a stable total debt of CNY 205bn (including operating lease) and a strong net cash position of CNY 366bn (including short-term investments and equity investments) as of end-March 2024. Debt to adjusted EBITDA was stable at 1.1x, based on our calculations. We expect its shareholder returns and investment needs to be fully covered by its strong cash flow over the next 24 months.

Investment view

We think the latest quarterly results are slightly credit positive for Alibaba, given the signs of improving GMV and effectiveness of its strategy shift. Supported by the solid credit fundamentals, we think investors can still seek exposure to this quality credit and may prudently extend duration based on portfolio suitability amid expectations of falling interest rates.

Key risks to our view include 1) higher US Treasury rates for longer; 2) a weaker-than-expected Chinese economy, leading to tepid consumption and online marketing demand; 3) higher-than-expected investments to defend competition that result in substantially weaker margins on a sustained basis.

Tencent Holdings Limited

UBS credit outlook: Stable
Agency ratings: A1/A+
Analyst coverage: Eve Li

Company updates

Tencent is China's leading internet services company, providing services across communications and social networks, online games, digital content, online advertising, fintech, cloud, and more. MIH Internet Holdings, controlled by Naspers Limited, is the largest shareholder with a 25.0% stake. Ma Huateng, the chairman and CEO of the company, held 8.5% of the company as of end-2023.

In 1Q24, Tencent reported a strong set of results. Total revenue increased 6% y/y to CNY 160bn, mainly supported by the strong rebound in online advertising (+26% y/y to CNY 26.5bn), while fintech and business services' growth slowed to 7% y/y on moderated offline consumption. Online gaming revenue was stable at CNY 48bn, with domestic games down 2% y/y on a high base and international games up 3% y/y. Tencent has focused on both revitalizing its existing titles and launching new games. There're some early signs of progress, with deferred revenue increasing 10% y/y in 1Q24. DnF Mobile, launched on 21 May, also ranked top in terms of grossing.

With continuous cost discipline and more contribution from high-margin businesses, Tencent's gross margin improved to 53% in 1Q24 (compared to 45% in 1Q23 and 50% in 3Q23). The company further strengthened its net cash position, with CNY 71bn in net cash as of end-March 2024 considering operating leases. It also maintained a sizable investment portfolio of CNY 917bn, consisting of listed and unlisted investments. We estimate its gross leverage improved to 1.5x, and LTM interest coverage ratio also expanded to 20.5x. According to management, Tencent has no plans to issue convertible bonds as its strong cash flow can sufficiently fund capex, share buybacks, and dividends.

Investment view
We think the 1Q24 results and recent developments further solidify Tencent's foundation for further growth. The company has upgraded its ad tech platform and introduced AI tools to advertisers. Together with an 80% increase in user time spent, video ccounts' advertising revenue doubled in the quarter. Mini games also further ramped up, with gross receipts growing 30% y/y. These high-margin businesses will support a blended margin expansion for the company compared to previous years, in our view. Also, considering its strong cash flows and prudent investment approach, we expect Tencent to maintain a solid credit profile over the next 12–24 months. We think Tencent's bonds are suitable for quality credit exposure, and we hold some attractive calls along the curve.

Key risks to our view include 1) higher US Treasury rates for longer; and 2) unexpected regulation changes that lead to significant profitability erosion.

Baidu Inc.
UBS credit outlook: Stable
Agency ratings: A3/NR
Analyst coverage: Eve Li

Company updates
Founded in 2000, Baidu is a leading internet company in China providing services such as search, cloud, intelligent driving, and smart devices. Baidu is also a leading Chinese AI company, launching its generative AI model ERNIE in August 2023. In addition to the core businesses (Baidu Core), the company has also consolidated its 45.4%-owned subsidiary iQIYI (as of February 2024), a leading online video platform with over 100mn average daily subscribing members in 2023. As of end-January 2024, chairman, CEO and co-founder Robin Yanlong Li held an 18.2% stake and 59.3% of the voting power in Baidu.

In 1Q24, Baidu reported CNY 31.5bn in total revenues, +1.2% y/y. For Baidu Core, total revenue grew 4% y/y to CNY 23.8bn. The revenue growth of online marketing decelerated to 2.7% y/y in the quarter, compared to 6.4% y/yin 4Q23. The weaker performance was due to weak macro, despite incremental contributions from AI advertising (CNY 700mn, 4% of core ads). Management said that 11% of the search pages are loaded with AI content. Cloud remained a bright spot, with a 12% y/y revenue growth and a 7% contribution from AI cloud (vs. 5% in 4Q23). For iQIYI, total revenue declined 5% y/y to CNY 7.9bn, mainly due to a 13% y/y fall in membership services revenue. Thanks to continuous cost discipline, the consolidated reported EBITDA was 1.2% y/y higher on a stable margin. Baidu maintained a strong net cash position of CNY 91bn. We estimate its adjusted debt/LTM EBITDA rose slightly to 2.5x in 1Q24, from 2.4x in 2023.

Investment view
Due to its soft advertising outlook and the current insignificant revenue contribution from AI, we see limited room for Baidu's leverage to trend significantly lower this year. The company has guided for weaker advertising revenues in 2Q and 3Q due to the ongoing transition of its AI search. That said, we expect the company to maintain its strong net cash position and expect a stable credit rating trajectory over the next 12 months. We have attractive calls on Baidu's 2025 bonds. For its mid-to-longer tenor bonds, we think their valuation looks less appealing compared to the higher-rated Tencent and Alibaba, after the meaningful spread compression YTD.

Key risks to our view include 1) higher US Treasury rates for longer; 2) unexpected geopolitical events, such as US sanctions, that weaken market sentiment materially or create forced selling; and 3) a weaker-than-expected Chinese economy, leading to tepid online marketing demand.

Meituan
UBS credit outlook: Stable
Agency ratings: Baa3/BBB
Analyst coverage: Eve Li

Company updates
Meituan is a leading one-stop local service platform in China. By gross transaction value (GTV), Meituan is China's largest on-demand food delivery operator, with a market share of nearly 70%. This leadership has enabled it to explore cross-selling opportunities and expand into in-store, hotel, and travel businesses, as well as new initiatives.

In 1Q24, Meituan's revenue increased 25% y/y to CNY 73.3bn, supported by strong growth in both its core local commerce and new initiatives segments. Operating profit soared 45% y/y to CNY 5.2bn, thanks to a significant loss reduction in new initiatives. The segment's operating loss narrowed to CNY 2.8bn in 1Q24, compared to CNY 4.8bn in 4Q23, supported by the improving efficiency of Meituan Select. Also, reported EBITDA grew 29% y/y to CNY 8.1bn on a slightly higher margin of 11%. During the quarter, Meituan's on-demand delivery order volume grew 28% y/y. It also launched a new model called Branded Satellite Stores that enables well-known chain restaurants to open delivery-only stores. We think such initiatives, together with its Pinhaofan model, could further drive volume growth. For the in-store business, management expects to maintain healthy GTV growth and more rational competition from competitors.

Moody's and S&P both revised Meituan's outlook to Positive from Stable this year, reflecting its faster-than-expected deleveraging trend. Meituan's adjusted total debt decreased 13% q/q to CNY 53bn as of March 2024. We estimate its adjusted debt/LTM EBITDA improved to 2.1x, from 2.5x as of end-2023. The company also maintained a strong net cash position of CNY 86bn. In June, Meituan announced the intention to repurchase up to USD 2bn of shares from the open market. Year-to-date, the company has repurchased around USD 1bn under its previous share buyback program. We think the company has sufficient liquidity to fund share buybacks, and it may also tap the USD bond market for additional liquidity amid the convertible bonds puttable in April 2025 and USD bonds due October 2025.

Investment view
We expect Meituan to post solid EBITDA growth this year, thanks to improving operation efficiencies and narrowing losses of its new initiatives. That said, the better outlook is largely priced in by the market, reflected by the significant spread tightening year-to-date. Meaningful spread compression from here would require more evidence in normalized competition and resilient operations amid the current macro conditions, in our view. We therefore keep our neutral stance on its bonds.

Key risks to our view include 1) higher US Treasury rates for longer; 2) a weaker-than-expected Chinese economy, leading to tepid consumption demand; and 3) the loss of market-leading position due to competition.

Weibo Corp.

UBS credit outlook: Stable
Agency ratings: Baa2/BBB
Analyst coverage: Eve Li

Company updates
Weibo is a leading social media platform in China. Sina Corporation (SINA), a leading internet media company in China, is Weibo's parent and controlling shareholder with a 37.3% stake and 64.1% voting power.

In 1Q24, Weibo's top-line of USD 395mn decreased 4%/0% y/y in USD/CNY terms, with weaker performance in both advertising and value-added services. Adjusted EBITDA was 3% y/y lower at USD 136mn on a slightly improving margin. According to management, the growth in online games and consumer electronics advertisements was offset by the reduced budget of cosmetics customers due to competition from short-video platforms. Its user base also shrank slightly, with MAU and DAU decreasing by 10mn and 2mn to 588mn and 255mn, respectively, from a quarter ago. Value-added services revenue, mainly membership fees, therefore decreased 3% y/y to USD 57mn. In terms of outlook, management expects flat advertising revenues in 2Q24 in CNY terms, and a pickup in 2H24 driven by the Olympic Games and the Double 11 shopping festival.

Weibo still kept a net cash position of USD 545mn (including operating leases) as of end-March 2024. Adjusted debt/LTM EBITDA was stable q/q at 4.3x, while debt/cap was slightly higher at 45% (vs. 43%). Of its USD 3.3bn in cash, around 40% was offshore, which can fully cover the USD 800mn of bonds maturing in July.

In March 2024, Weibo announced USD 200mn in special dividends payable in May 2024; the amount was the same as the special dividends paid in 2023. Based on management's guidance, Weibo intends to pay regular dividends going forward.

Investment view
We think Weibo's healthy cash flow from operations can support its shareholder returns and manageable investment needs, assuming insignificant cash leakage to SINA. According to S&P, SINA turned net cash in 2023, reducing Weibo's pressure to upstream cash. The rating agency in June also affirmed Weibo's BBB rating with a Stable outlook.

Amid fierce competition from other social media platforms, we think Weibo may continue to underperform its peers in terms of user acquisition and advertising revenue growth. Its MAU and DAU declined for two consecutive quarters, though partly reflecting the company's focus shift from scale to quality. While we don't expect a sharp fall in user base this year, a sustained drop such as an accumulated 10% fall over a two-year horizon may lead to a reduced rating buffer, according to S&P. Weibo is trading wider than its BBB-rated China tech peers, which we think is fair given Weibo's less promising business outlook and smaller net cash position.

Key risks to our view include 1) higher US Treasury rates for longer; 2) higher-than-expected investments to defend competition that result in substantially weaker margins on a sustained basis; and 3) unexpected large cash leakage to SINA.

Lenovo Group

UBS credit outlook: Stable
Agency ratings: Baa2/BBB
Analyst coverage: Eve Li

Company updates

Lenovo is a leading technology products manufacturer and services provider globally. Through organic growth as well as acquisitions over the years, the company has gradually expanded its product portfolio. It has three reporting segments: 1) intelligent devices group (IDG), including PCs, smartphones, tablets, and other smart device businesses; 2) infrastructure solutions group (ISG), including server and storage products; and 3) solutions and services group (SSG), including support services and managed services. In FY24 (fiscal year ended 31 March 2024), IDG, ISG, and SSG accounted for 73%, 15% and 12%, respectively, of total revenue before segment eliminations. The operating margins of IDG, ISG, and SSG were 7.1%, -2.8%, and 20.7%, bringing the group consolidated operating profit margin (OPM) to 3.5% in FY24 (from 4.3% in FY23).

Specifically, IDG's revenue was 10% lower at USD 44.6bn, affected by the excessive channel inventory at the start of the fiscal year. That said, the year-over-year revenue growth turned positive for two consecutive quarters from the December quarter, supported by a rebound in commercial PC demand and market share gains in various products. Lenovo expects to maintain its largest PC market share globally (23% in 4QFY24). ISG's revenue declined 9% y/y to USD 9bn amid a sector budget shift away from general-purpose computing to AI. That said, the revenue resumed q/q growth for three consecutive quarters and the y/y growth also turned positive to 15% in the March quarter. While the segment's OPM was hurt by R&D, a slow DDR5 transition, and GPU supply constraints, management is focusing on the return to profitability. SSG maintained a solid revenue growth of 12% y/y and the highest OPM among the three segments.

Due to a 8% decline in group top-line and lower margins, we estimate Lenovo's adjusted EBITDA was 17% lower at USD 3.7bn in FY24. Total debt was 9% lower at USD 4bn due to the conversion of the 2024 convertible bond and lower notes outstanding. The company purchased around USD 136mn in principal amounts across its four USD bonds during the year. Lenovo has a small net debt of USD 336mn. Gross and net leverage was slightly higher at 1.1x and 0.1x in FY24, based on our calculation. Using S&P's rating methodology, we estimate Lenovo's adjusted net debt to EBITDA increased to 0.8x in FY24 (from 0.7x), still below the downgrade trigger of above 1x.

In May, Lenovo announced it has signed a strategic collaboration framework agreement with Alat, a wholly-owned subsidiary of Public Investment Fund (Saudi Arabia sovereign wealth fund). It will also issue USD 2bn of three-year zero-coupon convertible bonds to Alat, and net proceeds will be used for debt repayments as well as working capital needs. Concurrently, it will issue three-year 1.15bn warrants at an issue price of HKD 1.43 each, with a similar use of proceeds.

Investment view

We expect Lenovo's profit and debt metrics to improve over the next 12–24 months. Among the first to launch AI PCs, the company foresees a significant replacement cycle over the next 2–3 years driven by a 50–60% AI PC penetration rate. The company guides –0.5% to +2.5% y/y PC shipment growth this year, and 5–10% y/y growth in 2025. In addition, with the launch of AI server products, it has identified a USD 7bn pipeline and is working on conversion. The partnership with Alat and the issuance of CBs also bring business opportunities in MEA as well as interest expense savings. In terms of valuation, we're neutral on Lenovo's curve after the meaningful spread compression YTD.

Key risks to our view include 1) rising geopolitical tensions that impact the export of Lenovo's PCs from China and cause a significant increase in capex: and 2) worse-than-expected business performance and leverage that lead to a rating downgrade.

Huawei Investment & Holding Co Ltd

UBS credit outlook: Stable
Agency ratings: NR/NR
Analyst coverage: Eve Li

Company updates

Founded in 1987, Huawei is a leading global provider of information and communications technology (ICT) infrastructure and smart devices. The company has around 207,000 employees and operates in over 170 countries and regions. Huawei is a private company wholly owned by its employees. By region, the home market of China contributes about 67% of its revenue, followed by EMEA (21%), Asia Pacific (6%), Americas (5%), and others.

In 2023, Huawei witnessed a decent 10% growth in revenue to CNY 704bn. The ICT Infrastructure segment continued to be the largest contributor (51%) and grew 2%. Huawei serves carrier, government, and enterprise customers, and continues to lead the industry in technology innovation. Its consumer segment delivered a strong growth of 17% and grew its revenue share to 36%. Huawei launched various smartphone series such as Mate 60, and its HarmonyOS had been deployed on over 800mn devices by end-2023. Its intelligent automotive solution segment, while only accounting for 1% of the group's revenue, is gaining traction. The company cooperates with auto OEMs via various models to provide intelligent driving components and solutions. Currently, four Chinese automakers (Seres, BAIC, Chery, and JAC) are cooperating with Huawei under the "smart selection" model and some have already launched models which have been well received by the market. The segment turned profitable in 1Q24, according to the company. Huawei is in a strong net cash position, with CNY 319bn in total debt and USD 476bn in total liquidity (including short-term investments). The company also has ample undrawn committed bank facilities and good access to the onshore bond market. It has issued CNY 9bn in onshore short-term commercial paper year-to-date at a cost of 1.8–2.1%.

Investment view

Huawei's USD bond curve is offering a slight spread pickup versus its BBB rated tech peers, which we view as fair given its higher exposure to geopolitical risks. In July, media reports said that the US has revoked eight more licenses involving Huawei. That said, the company's strong R&D commitments (over 20% of revenue over the past few years) and continuous technology breakthroughs will likely reinforce its leading position in the core ICT infrastructure business and support its expansion into new opportunities.

Key risks to our view include a loss of its market leading position due to unexpected geopolitical events or intense competition.

China's privately-owned property developers

Figure 22 - China privately-owned property issuers covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior			
			0-2y	2-5y	5-10y	>10y
China Jinmao Holdings	Deteriorating	Ba2/BBB-				
China Vanke	Deteriorating	Ba3/BB+				
Greentown China Holdings	Deteriorating	B1/BB-				
Longfor Properties	Deteriorating	Ba3/BB+				
Seazen Group Ltd	Deteriorating	Caa1/B				
Shui On Land Limited	Deteriorating	NR/NR				
Yanlord Land	Deteriorating	B1/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 6 - Key financial & credit metrics (latest full year)

Issuer	Revenue (USD bn)	EBITDA margin	Net debt/ EBITDA	Unrestricted cash/Short-term debt	EBITDA/ Interest	Net debt/ equity
China Jinmao	10.2	4.4%	29.9x	1.3x	0.4x	81.5%
China Vanke	65.6	12.8%	4.1x	1.5x	3.9x	60.4%
Greentown China	18.5	7.6%	7.3x	1.4x	1.2x	64.0%
Longfor Properties	25.3	11.2%	7.3x	1.3x	2.3x	63.0%
Seazen Group	16.8	6.2%	5.9x	0.5x	1.5x	46.7%
Shui On Land	1.4	41.0%	6.3x	0.3x	1.7x	57.0%
Yanlord Land	16.8	11.0%	4.3x	0.9x	2.0x	47.0%

Source: Company reports, UBS

China Jinmao Holdings Group (Jinmao)

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Ba2/BBB-
Analyst coverage: Daniel Tam

Company updates

China Jinmao's shareholders include Sinochem HK (38.4%), Ping An Life Insurance (13.2%), and New China Life Insurance (9.2%). Sinochem HK is 98%-owned by Sinochem Group, which in turn is 100%-owned by the central government. As Sinochem Group's only real estate platform, it receives operational and financial support from the former. For example, Sinochem has provided shareholder loans to Jinmao at below market cost and has raised its stake in Jinmao by taking dividends in shares instead of cash. Sinochem HK's holding in Jinmao rose to 38.4% from 37.1% at the end of 2023, via share purchases in the secondary market. Sinochem recently tightened its control over Jinmao by replacing Jinmao's chairman with its own senior management and appointing an additional executive director to supervise Jinmao's daily operations and finances. This suggests that Jinmao will receive stronger parent support, if necessary. Jinmao reported a weak set of 2023 results, with a net loss, higher leverage, and weaker liquidity. Revenue and EBITDA declined 12.8% and 53.7%, respectively, leading to a net loss of CNY 4.9bn in 2023. The loss mainly stemmed from a lack of fair value gain and a one-off extraordinary gain in 2022. Sluggish earnings and higher finance costs weakened EBITDA-to-interest to 0.4x (2022: 1x) and raised total debt-to-EBITDA to 41.7x (2022: 18.9x). Operating cash flow strengthened to CNY 3.1bn (2022: CNY 1.8bn), while free cash flow fell to CNY 2.4bn (2022: CNY 3.6bn).

Investment view

Jinmao's contracted sales declined 8.9% to CNY 141.2bn in 2023 and 48.2% y/y to CNY 44.5bn in 1H24. The sluggish sales in 1H24 were partly due to limited new project launches, and partly because land banks acquired through city operation projects are mainly located in non-core areas in upper-tier cities that have weaker demand. The company has said it will also focus on property management and rental businesses to increase recurrent income and offset weaker property sales. Jinmao has good access to the capital market owing to its strong shareholder background and good quality assets. The company raised CNY 15.3bn in 2023 via the issuance of corporate bonds, medium-term notes (MTNs), and commercial mortgage-backed securities (CMBS). We are less concerned about Jinmao's repayment ability, given the expectation that it will receive extraordinary support from its state-owned parent, and given the cross-default provisions in Sinochem's offshore bonds. The company issued a CNY 3bn three-year onshore unsecured MTN on 17 June at a low funding cost of 2.8%, suggesting that the company's financing channels remain smooth.

Key downside risks include a sustained decline in contracted sales and deterioration in free cash flow, weaker access to funding, and weaker parent support. Key upside risks include accelerated onshore borrowing for repaying its offshore debts, and stronger-than-expected sales performance.

China Vanke Co.

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Ba3/BB+
Analyst coverage: Daniel Tam

Company updates

China Vanke has announced profit warning for 1H24, expecting a net loss of CNY 7–9bn attributable to shareholders. This compares with a net profit of CNY 9.9bn in 1H23. The company reported a net profit of CNY 331mn in 1Q24, suggesting that a CNY 6.7–8.7bn loss was incurred in 2Q24. Vanke said the loss is attributable to lower profit margins for property sales, impairment losses, and losses generated from asset disposals and financial investments in non-core businesses. Vanke has new borrowings of CNY 60bn and repaid CNY 50bn in 1H24, including three offshore bonds with a total of CNY 10.5bn (USD 2.1bn) and three onshore bonds totaling CNY 5bn. Vanke now has just one onshore bond (CNY 4.3bn) due in 2H24, which can be repaid via operating cash flows and bridge loans. The company raised CNY 9.3bn via asset disposals in 1H24, and plans to list two real estate investment trusts (REITs) backed by logistic warehouses and affordable housing.

Investment view

China Vanke's contracted sales declined 9.8% to CNY 376bn in 2023 and 37.6% y/y to CNY 127.3bn in 1H24. Cash collection in 1H24 was CNY 118.6bn, indicating a cash collection ratio of 93.2%, lower than the roughly 100% in 1H23. The company will have CNY 39.4bn in debt maturing/puttable in 2025, including two offshore bonds with a total of USD 933mn. The company has been in talks with banks for a club loan of CNY 50bn, which should support its 2025 debt repayment, if banks approve the loans.

Key downside risks include a sustained decline in contracted sales, failure to raise funds via the issuance of REITs and secured bank financing, and weaker-than-expected parent support. Key upside risks include a sustained recovery in contracted sales and raising more-than-expected funds through the issuance of REITs.

Greentown China Holdings

UBS credit outlook: Deteriorating
Moody's/S&P ratings: B1/BB-
Analyst coverage: Daniel Tam

Company updates

Greentown China is 29% owned by state-owned China Communications Construction Group (CCCG) and 23% by Wharf Holdings, which acts as a passive financial investor. CCCG in turn is 90%-owned by the Chinese government and 10% by the National Social Security Fund of China, and appoints four of the six executive directors in Greentown. Greentown reported a mixed set of 2023 results, with weaker earnings, but leverage and liquidity remain stable. Revenue increased 3.3%, but EBITDA and net profit declined 31.1% and 24.9%, respectively. The weaker earnings lowered EBITDA-to-interest to 1.2x (2022: 1.7x) and raised total debt-to-EBITDA to 14.7x (2022: 9.8x). Operating cash flow strengthened to CNY 23bn in 2023 (2022: CNY 14.6bn), turning free cash flow into a positive CNY 1.2bn in 2023 from a negative CNY 8.9bn in 2022. Total debt and net debt increased by 3.3% and 2.3%, respectively, but net debt-to-equity remained stable at 64% (2022: 65%) and unrestricted cash-to-short-term debt weakened slightly to 1.4x (2022: 1.6x).

Investment view

Greentown's contracted sales fell 8.8% to CNY 194.1bn in 2023 and 13% y/y to CNY 85.4bn in 1H24, outperforming its peers. The better sales performance can be attributed to the company's strong brand name recognition, high-quality projects, and focus on Hangzhou and the Yangtze River Delta region, which have more affluent households. Benefiting from its state-ownership background, the company also has good access to the onshore capital market.

Greentown issued CNY 4bn (USD 555.6mn) in onshore bonds in 1H24, with coupon rates of 4.13–4.38%. The proceeds were used to buy back USD 450mn in bonds, including a USD 150mn bond due in December 2024 and USD 300m due in January 2025. The company will likely issue more onshore bonds to repay the remaining USD 841mn in offshore bonds that are maturing in 2025.

Key downside risks include further weakness in property sales, aggressive land acquisitions, and reduced support from CCCG. Key upside risks include stronger-than-expected sales and the company being able to issue new offshore bonds at a reasonable cost.

Longfor Group Holdings
UBS credit outlook: Deteriorating
Moody's/S&P ratings:Ba3/BB+
Analyst coverage: Daniel Tam

Company updates

Longfor Group Holdings is a leading privately-owned residential and commercial property developer. It operates one of the largest shopping mall portfolios in China, which support the group's secured financing. Longfor has a prudential financial track record and has been prepaying its debts ahead of maturity to reduce the portion of short-term debt. Longfor Group reported a mixed set of 2023 results, with lower earnings, stable leverage, and adequate liquidity. Although revenue declined on sluggish property sales, liquidity was supported by rising recurrent income from its investment property portfolio (shopping malls and rental apartments) and its property management segment. Longfor's recurrent income covered 2.8x of gross interest expense and accounted for 44% of gross profit in 2023. Recurrent income is set to increase with more shopping malls and rental apartments commencing operations. Longfor's operating cash flow rose 70% to CNY 33bn in 2023, resulting in a positive CNY 10.2bn of free cash flow on reduced land acquisitions.

Investment view

Longfor's contracted sales fell 9.8% to CNY 114.8bn in 2023 and 41.9% y/y to CNY 38.1bn in 1H24. Despite the company's sluggish sales performance, it bought back USD 403mn of its 3.95% 2029 bond, the USD 220mn 3.85% 2032 bond, and the CNY 2.65bn CMBS on 28 June. The company's bond buybacks amid sluggish sales performance suggest the company can adequately manage its liquidity. Longfor has CNY 4.5bn of onshore bonds maturing in 2H24, which it should be able to repay on time.

Key downside risks include further weakness in property sales in upper-tier cities, and more aggressive land acquisitions. Key upside risks include higher valuation for its investment property portfolio.

Seazen Holdings/Seazen Group
UBS credit outlook: Deteriorating
Moody's/S&P ratings: Caa1/B
Analyst coverage: Daniel Tam

Company updates

Seazen Holdings is 61.1% owned by Seazen Group Limited and accounted for over 95% of its parent's revenue and assets in 2023. Seazen Group is 63.3%-owned by founder Wang Zhenhua, who also holds 68.9% of the property management company S-Enjoy Service Group. The group focuses on third- and fourth-tier cities where there is less commercial property competition. The company is the second-largest shopping mall operator in China in terms of the number of shopping malls. Seazen Group reported a stable revenue and gross profit in 2023, but posted a net loss as tax payments increased 86% y/y. Despite the net loss, the group reported positive operating and free cash flows. Net debt declined 7.3% y/y, lowering net debt-to-equity to 46.7% in 2023 (2022: 51%). Although unrestricted cash-to-short-term debt fell to 53% in 2023 from 63% in 2022, the company's recurrent income covered 46% of short-term debt, or 2.3x gross interest expense in 2023. Seazen has 160 malls under operation and generated CNY 10.6bn in rental income in 2023. Management expects rental income to increase to CNY 12.5bn in 2024, with 12 new malls commencing operation. Seazen also has 26 shopping malls under construction.

Investment view

Seazen's contracted sales declined 34.5% to CNY 76bn in 2023 and 44.4% y/y to CNY 23.6bn in 1H24. Despite the sluggish sales performance, the company's liquidity was supported by the growing rental income generated from its shopping mall portfolio and secured financing backed by the unpledged shopping malls. Seazen raised CNY 400bn from its shopping mall portfolio in 2022 and 2023 and still has 46 unpledged shopping malls that can raise CNY 18.4bn (USD 2.5bn). The proceeds should support the repayment of the CNY 7bn in onshore and offshore bonds due/puttable in 2024 and CNY 8bn in 2025. Seazen issued CNY 1.36bn (USD 187mn) of medium-term notes (MTNs) that are guaranteed by state-owned China Bond Insurance Corp (CBILC) and backed by the group's shopping malls.

Key downside risks include a further deterioration in property sales, weaker rental income from shopping mall portfolio, and uncertainty whether there will be changes in the management after the chairman was released from jail in July. Key upside risks include faster-than-expected completion of its shopping malls, which can be used for secured borrowings.

Shui On Land
UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates

Shui On Land is the largest commercial property landlord in Shanghai, holding 1.6mn sqm of grade A office space, shopping spaces, and serviced apartments in the city. The company also operates in four other cities with total land bank of 6.2mn sqm. Shanghai and Wuhan account for 31% and 43%, respectively, of the company's total land bank, while Foshan, Chongqing, and Nanjing account for 14%, 10% and 2%, respectively. Shui On Land reported a weak set of 2023 results, with lower earnings, higher leverage, and weaker liquidity. Revenue, EBITDA, and net profit declined 37.3%, 29.2%, and 5.3%, respectively. The weaker earnings lowered EBITDA-to-interest coverage to 1.7x (2022: 2.9x) and raised total debt-to-EBITDA to 8x (2022: 5.9x). Operating cash flow remained positive at CNY 1.1bn (2022: CNY 4bn), but free cash flow turned to a negative CNY 1.3bn (2022: CNY 200mn).

Investment view
The media reported that the company obtained a CNY 4bn (USD 555.6mn) commercial property loan backed by its Shanghai Xintiandi project and another CNY 2–3bn loan backed by the Wuhan Tiandi project. The proceeds should be sufficient to cover its USD 500mn bond and a USD 100mn offshore loan due in August 2024. Shui On Land has two projects for pre-sale in Shanghai in 2H24, including one in Yangpu Binjang with an estimated attributable saleable value of CNY 2.7bn (USD 375mn), and Taipingqiao Lot 122 with an estimated attributable saleable value of CNY 9.6bn (USD 1.33bn). The proceeds will be used for the repayment of its 2025 bond and syndicated loans.

Key downside risks include further weakness in property sales in Shanghai, smaller-than-expected sales proceeds for the two Shanghai projects, and larger-than expected offshore loans. Key upside risks include strong-than-expected sales for its two Shanghai projects.

Yanlord Land
UBS credit outlook: Deteriorating
Moody's/S&P ratings: B1/NR
Analyst coverage: Daniel Tam

Company updates
Yanlord Land is a Singapore-listed Chinese property developer, 73%-owned by the chairman. The company has a prudent financial track record, with positive operating and free cash flows over the past five years. The chairman has been cautious on China's real estate sector since 2022, taking a 10% or below stake in new acquisitions and acting as constructor and project manager. Yanlord reported a mixed set of 2023 results, with a net loss and weaker liquidity, while leverage declined. Revenue increased 51%, but EBITDA declined 10% on lower profitability and increased impairment loss. The company posted a net loss of CNY 700mn in 2023, compared with a net profit of CNY 2.9bn in 2022. Despite the weaker earnings, EBITDA/interest was unchanged at 2x as a result of lower finance costs. The company maintained positive operating and free cash flows. Total debt declined 26% and lowered total debt/EBITDA to 7x (2022: 8.5x).

Investment view
Yanlord's contracted sales fell 52% to CNY 32.4bn in 2023 and 47% y/y to CNY 11.2bn in 1H24, owing to a lack of project launches in Shanghai. The company has an investment property portfolio which generated around CNY 3.9bn rental income in 2023. Yanlord plans to launch CNY 60bn of projects for sale in 2024 and had CNY 20bn worth of unpledged investment properties at the end of 2023. As Yanlord has disposed of a project in Singapore to fund the repayment of its USD 400mn bond due in April, it now only has USD 500mn in senior notes due in May 2026. No onshore and offshore bonds are maturing before the USD bond. The company is working on a commercial mortgage-backed security and may also pledge more investment property projects to support its liquidity.

Key downside risks include further weakness in property sales and a lack of saleable projects in the coming years after a significant reduction in land acquisitions over the past two years. Key upside risks include stronger-than-expected sales in mainland China and in Singapore.

Others

Far East Horizon
UBS credit outlook: Stable
Agency ratings: NR/BBB-
Analyst coverage: Eve Li

Company updates
Far East Horizon (FEH) is one of the leading financial leasing companies in China. Under its "finance + industry" strategy, the company has diversified into industrial operations, including leasing (Horizon Construction Development, HCD) and hospital operations Horizon Healthcare). Sinochem Group is FEH's largest shareholder, holding a 21.3% stake as of end-2023.

FEH has delivered steady growth over the past few years and reported solid results in 2023, with total revenue +4% to CNY 38bn. Its financial leasing segment (61% of total revenue) saw largely steady net interest earning assets of CNY 269bn (-1% y/y) and a net interest income of CNY 12.5bn (-1% y/y). Net interest margin (NIM) faced some pressure and declined 10bps to 4.58%, while average yield improved to 8.24% (+24bps). Net interest spread (NIS) was 4bps higher at 3.98% on stable financing costs. Industrial operations (39% of total revenue) remained a bright spot, with revenue growing 11% to CNY 14.7bn and gross profit expanding 16% to CNY 4.8bn on a better margin. In terms of asset quality, FEH's non-performing asset (NPA) ratio continued to trend down to 1.04% (-1bp y/y), and special mention assets (30 days overdue) accounted for 5.97% of net interest-earning assets (vs. 7% at end-2022). NPA provision coverage ratio was still robust at 228%. FEH has proactively optimized its asset allocation and reduced its exposure to urban public utility customers to 39.8% (vs. 43.6% in 2020). The segment's asset quality has been in line or better than the company's average over the past three years.

For 2024, the company has guided flattish interest-earning assets amid weak macro and likely delayed investments by its customers. NIM may continue to trend down, albeit more resilient than banks', given manageable pressure on asset yield. The management has also said that Sinochem has limited incentive to divest its stake in FEH, and there may be a lack of buyers among the other SOEs. Most of FEH's onshore credit lines are granted on a standalone basis. Note that S&P views FEH as a non-strategic company to Sinochem and FEH's rating does not contain any uplift for group support. In April, FEH announced a plan to distribute a 25% stake in listed HCD to FEH's shareholders as a special dividend. While FEH's stake in HCD will decrease to below 50% after the transaction, the proposal is overall credit neutral, in our view.

Investment view
We expect FEH to maintain its market-leading position and deliver resilient performance thanks to its strong customer coverage and comprehensive risk management. The company also maintained diversified funding channels, including bank loans (61%), bonds (29%), and others as of end-2023. After the strong performance year-to-date, FEH's bonds are trading wider than bank-affiliated lessors which are generally rated 3–4 notches higher, and tighter than same-rated asset management companies. We're currently neutral on the curve.

Key risks to our view include an unexpected deterioration in asset quality and a weaker asset yield due to intense competition.

Figure 23 - Hong Kong issuers covered in this report and their respective credit views

Issuer	CIO outlook	Rating (Mdy/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
AIA Group	Stable	A1/A+				
Airport Authority Hong Kong	Stable	NR/AA+				
Cathay Pacific Airways Limited	Stable	NR/NR				
Champion REIT	Deteriorating	Baa2/NR				
CK Hutchison	Stable	A2/A				
CK Infrastructure Holdings	Stable	NR/A				
CLP Power Hong Kong	Stable	A1/A+				
Far East Consortium	Deteriorating	NR/NR				
FWD Group Holdings Limited	Stable	Baa2/NR				
Henderson Land	Stable	NR/NR				
Hong Kong Telecommunications	Stable	Baa2/BBB				
Hong Kong Land	Stable	A3/A				
Hutchison Port Holdings Trust	Deteriorating	Baa1/A-				
Hysan Development Company	Deteriorating	Baa1/NR				
Li & Fung Limited	Stable	Ba3//BB				
Lifestyle International	Deteriorating	NR/NR				
LINK REIT	Stable	A2/A				
Nan Fung International	Stable	Baa3/BBB-				
New World Development	Deteriorating	NR/NR				
NWS Holdings	Deteriorating	NR/NR				
Pacific Century Premium Developments	Deteriorating	NR/NR				
Regal Hotels	Deteriorating	NR/NR				
Sun Hung Kai Properties	Stable	A1/A+				
Swire Pacific	Stable	A3/A-				
Swire Properties	Stable	A2/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 7 - Key financial & credit metrics (the latest full year)

Conglomerates

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ interest	Total debt/ Capital
CK Hutchison	35.3	30.5%	44.1	1.5x	7.0x	33.9%
CK Infrastructure	0.8	76.8%	3.1	2.5x	4.8x	15.6%
NWS #	5.8	6.8%	4.4	4.9x	5.3x	42.9%
Swire Pacific	12.1	17.0%	8.9	3.4x	6.3x	18.0%

 # Fiscal year ended 30 June 2023

Landlords

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ interest	Total debt/ Capital
Nan Fung International *	0.5	77.0%	4.2	6.5x	2.1x	23.7%
PCPD	0.1	10.2%	1.2	102.1x	0.2x	98.4%
Hysan Development	0.4	72.1%	4.1	12.3x	1.6x	44.4%
Champion REIT	0.3	67.5%	1.9	7.8x	2.8x	23.8%
LinK REIT *	1.7	74.7%	7.6	4.9x	4.2x	24.9%
Hongkong Land	1.8	49.9%	6.6	5.8x	3.6x	17.0%
Swire Properties	1.9	58.9%	5.3	4.2x	5.8x	12.7%

** Fiscal year ended 31 March 2024*

Real estate developers

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ interest	Total debt/ Capital
Far East Consortium *	0.8	21.9%	3.9	11.8x	1.2x	72.0%
New World Development #	12.1	16.3%	23.7	12.2x	1.5x	52.4%
Sun Hung Kai Properties #	9.1	49.0%	16.0	3.2x	7.6x	17.0%

** Fiscal year ended 31 March 2024*
 # Fiscal year ended 30 June 2023

Source: Company reports, UBS

Table 8 - Key financial & credit metrics (the latest full year)

Other Hong Kong issuers

Issuer	Net profit (USD bn)	Contractual service margin (CSM) (USD bn)	Value of new business (VNB) (USD bn)	Total premium (TWPI) (USD bn)	Group LCSM cover ratio	Return on equity
AIA Group	3.8	53.1	4.0	37.9	537%	14.5%
FWD Group Holdings	-0.7	5.0	1.0	6.4	336%	5.7%
Issuer	**Revenue (USD bn)**	**EBITDA margin**	**Total debt (USD bn)**	**Net debt/ EBITDA**	**EBITDA/ interest**	**Total debt/ Capital**
Hong Kong Telecom	4.4	39.0%	5.7	3.2x	6.3x	56.5%
Hutchison Port Holdings Trust	1.4	58.4%	3.3	2.8x	7.4x	40.0%
CLP Power *	6.4	36.4%	6.1	2.6x	11.9x	n.a.
Airport Authority Hong Kong #	1.7	39.5%	15.7	17.1x	1.6x	62.0%
Cathay Pacific Airways	12.1	26.9%	8.7	2.1x	6.4x	53.0%
Li & Fung Limited	0.8	2.1%	0.0	-1.1x	1.8x	17.9%
Lifestyle International	0.3	54.5%	2.4	13.0x	1.4x	134.9%
Regal Hotel	0.2	36.4%	2.1	23.9x	0.7x	63.3%

** We used total debt/ EBITDA due to data availability*
 # Fiscal year ended 31 March 2024

Source: Company reports, UBS

AIA Group

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Zixuan Liu

Company updates

AIA Group (AIA) is a leading life and health insurer in Asia-Pacific with a strong position in mainland China, Hong Kong, Malaysia, Singapore, and Thailand. In 2023, it reported strong top-line growth, with annualized new premiums (ANP) and value of new business (VoNB) rising 41% and 30%, respectively, on an actual exchange rate basis. This was primarily driven by a sharp rebound for mainland China after its reopening (ANP +53% y/y) and a spike for Hong Kong on a recovery in mainland Chinese visitor (MCV) customers (ANP +123% y/y). The momentum extended into 1Q24 and management expects it to continue, given AIA's unique value proposition in providing differentiated healthcare services and wealth management products for mainlanders, helped by an increasing number of active agents. The balance of contractual service margins (CSMs) grew 6% to USD 53.1bn in 2023, coupled with a 6% gain in investment results. However, the upside was offset by higher pandemic-related medical claims, resulting in a 2% contraction in operating profit after tax (OPAT). Net profit, on the other hand, rose 13%as the impact of the rate hikes in the US became smaller compared to a year ago.

AIA has maintained strong capitalization. Its group LCSM coverage ratio (on a prescribed capital requirement basis) remained materially above the regulatory threshold at 275% after a USD 3.6bn share buyback. Supported by a strong capital buffer, the company proposed in April an additional share buyback of USD 2bn in the next 12 months. Management is also committed to maintaining its shareholder total capital resources to required capital ratio comfortably above 200%.

Investment view

We like AIA's dominant position in Asia and vast geographic diversification. We believe mainland Chinese customers and

MCVs in Hong Kong will continue to be growth drivers of its business. We also expect a stable investment performance, with the global economy appearing likely to achieve a soft landing. We have an Attractive rating on AIA's 2.7% subordinated perpetual note callable in 2026 (YTC at 6.5%), as we think the non-call risk is low. We have Fair ratings on other AIA bonds.

Key downside risks to our view include: 1) a sharp deterioration of economic conditions in mainland China and Hong Kong that slow down AIA's VoNB growth; and 2) aggressive capital management policies (dividend payouts and share buybacks). A key upside risk for the bonds is faster-than-expected Fed cuts.

Airport Authority Hong Kong

UBS credit outlook: Stable
Moody's/S&P ratings: NR/AA+
Analyst coverage: Eve Li

Company updates

The Airport Authority Hong Kong (AAHK) is a statutory body corporate whose primary function is to provide, operate, develop, and maintain Hong Kong International Airport (HKIA). It was established under the Airport Authority Ordinance and is wholly owned by the Hong Kong SAR government. Based on expectations for extraordinary government support, S&P has assigned an AA+ issuer credit rating to AAHK, the same as the Hong Kong government.

In FY24 (fiscal year ended 31 March 2024), AAHK reported HKD 13.7bn in total revenue, a 67% y/y increase. The rebound was mainly supported by the post-COVID recovery in passenger traffic and retail rental revenue. With a relatively milder increase in operating expenses, EBITDA increased to HKD 5.4bn (from HKD 0.8bn in FY23). To fund its three-runway system (3RS) and SKYCITY projects, AAHK tapped the US dollar bond market and increased its total debt (perpetuals as debt) to HKD 123bn as of end-March 2024. Net gearing inched higher to 121%, from 92% a year ago. While interest expenses were also 39% y/y higher due to a higher debt burden and larger costs, EBITDA/interest expenses improved to 1.6x (from 0.3x in FY23). AAHK's liquidity is strong, as it has HKD 30.6bn in cash versus HKD 10bn in short-term debt.

In 1Q24, AAHK's passenger traffic reached 12.7mn, 68% of its 1Q19 level. The progress was slightly below our previous expectations, due to delayed capacity normalization from airlines. Cathay Pacific Airways, which contributed to nearly half of HKIA's passenger volumes in 2019, now expects a full normalization of its passenger capacity by 1Q25 (from the previous guidance of end-2024).

Investment view

We expect AAHK's total debt to continue trending higher due to its large capex commitments, with HKD 46.9bn outstanding for its 3RS and other projects as of end-March 2024. That said, with its issuer rating linked to the Hong Kong government's rating, we expect a stable rating trajectory over the next 12 months. Furthermore, AAHK has maintained smooth funding access and has a back-loaded maturity profile. Investors can still find decent carry opportunities along its curve for high grade bond exposure, in our view. In addition, we still think the call probability at the first call date is not low for its two perpetuals callable in 2026 and 2028, given their high coupon reset. We rate them as Attractive.

Key downside risks to our view include: 1) a further delayed business recovery, especially in passenger traffic and retail sales; 2) a larger-than-expected capital expenditure and higher-than-expected leverage; 3) unexpected events such as strikes that impact its normal operations; and 4) a weaker status as an international aviation hub due to increasing competition from other regional airports.

Cathay Pacific Airways Limited

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Eve Li

Company updates

Cathay Pacific Airways Limited (CX) is the flagship carrier of Hong Kong. As of end-2023, the company had a fleet of 230 aircraft, of which 181 were held by Cathay Pacific (the premium full-service airline), 33 by HK Express (a low-cost airline), and 16 by Air Hong Kong (an express all-cargo carrier). CX's largest shareholder is the Hong Kong conglomerate Swire Pacific, which acquired the company in 1948 and currently holds a 45% stake. Air China, one of mainland China's big three airlines, owns 30%. CX, in turn, owns a 16% stake in Air China via a cross shareholding. The rest of CX's shareholdings include a 10% stake by Qatar Airways and a 6.5% voting share by the Financial Secretary Incorporated (representing the Hong Kong SAR government).

In 2023, CX reported a 85% rebound in revenue to HKD 94.5bn, mainly driven by the jump in passenger revenue (+329% y/y to HKD 61.4bn, 65% of total revenue) on pent-up travel demand. Available seat kilometers (ASK) recovered to 52% of 2019 levels to 85.6bn for the full year, and revenue passenger kilometers (RPK) soared to 73.3bn (from 14.8bn). Its passenger load factor increased to 85.7% (from 73.6%), while passenger yield normalized and declined 14% y/y to HKD 0.73 (still beyond 2019's level at HKD 0.55). Its cargo business (27% of total revenue) reported a lower revenue of HKD 22bn (–18% y/y) as industry supply increased and yield continued to normalize (albeit still higher than pre-COVID levels).

As of end-2023, CX had HKD 20bn in available unrestricted liquidity, including HKD 4.5bn in undrawn facilities. This represented a decrease from the highs seen during COVID, but was flattish compared to the 2019 level. Adjusted net debt decreased to HKD 41bn, and adjusted net gearing further improved to 0.69x (from 0.71x in 2022, against 2x borrowing covenants).

Supported by its strong operating cash flows, the company repurchased HKD 9.75bn (50%) worth of preference shares from the government in December 2023. It plans to repurchase the remaining 50% by end-July 2024. The company also delivered earlier-than-expected dividends of HKD 0.43 per ordinary share for FY23. We think the size is manageable and the resumption of dividends is positive for Swire Pacific. While CX has 75 aircraft on its order book, we expect the annual capex to be sufficiently covered by cash flows over the next few years given supply constraints. 2023 capex was HKD 6.8bn, up from HKD 3.7bn in 2022.

Investment view
We think CX will continue to rebuild its financials along with the recovery of its businesses. The company expects a full recovery of passenger flights in 1Q25 (a one-quarter delay compared to the previous guidance), up from 70% in December 2023 and 80% in 2Q24. The company's bonds, on which we are neutral, are trading at a narrow range compared to BBB rated Hong Kong issuers.

Key risks to our view include an unexpected deterioration in passenger flight activities and larger-than-expected capex activities.

Champion REIT
UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa2/NR
Analyst coverage: Eve Li

Company updates
Champion REIT's HKD 69bn commercial property portfolio is concentrated in Hong Kong, and includes 1) Three Garden Road (3GR), a Grade A commercial complex consisting of two office towers (47-storey and 37-storey) in the Central District; 2) Langham Place Office Tower (LP Office), a 59-storey Grade A property in Mong Kok; and 3) Langham Place Mall (LP Mall), a 15-level vertical mall. 3GR remains the most important property for Champion REIT, accounting for 61% of its total investment properties' valuation and 56% of net property income (NPI) in 2023. The company also has a minority stake of 27% in 66 Shoe Lane in Central London. Its largest shareholder is Great Eagle Holdings Limited, which has a 69.2% stake.

Champion REIT reported lackluster FY23 results. Overall rental income and net property income (NPI) declined 2% and 4% y/y, respectively. Notably, 3GR's NPI fell 10.6%, with passing rent 8% lower at HKD 91.7/sqft and the vacancy rate remaining high at 17.2%. As 3GR will see 19% and 43% of its leases expiring in 2024 and 2025, respectively, we think its rental income is still under pressure amid nearby new supply; we thus expect negative rental reversions to continue. LP Mall was a bright spot, doubling its turnover rent and growing NPI by 13% y/y despite a slightly lower occupancy rate of 98.6% (from 100%).

The company's adjusted EBITDA decreased by 2.5% to HKD 1.7bn in 2023. Interest expenses, however, expanded 38% to HKD 619mn due to exposure to floating-rate borrowings and higher benchmark rates. As a result, adjusted EBITDA/interest deteriorated to 2.8x in 2023, from 4.0x in 2022. Net debt was roughly unchanged at HKD 13.5bn, and net debt/EBITDA increased slightly to 7.8x. Due to the weaker credit metrics, Moody's downgraded Champion REIT by one notch to Baa2 Negative after the results. As of end-2023, Champion REIT had HKD 981mn in cash on hand and HKD 5.1bn in short-term debt (primarily bank loans due in 2Q24). In June, the company announced the signing of a new HKD 5.05bn three-year unsecured loan facility, with a cost of 3-month HIBOR+88bps. We believe the credit facility has removed Champion REIT's refinancing risk this year, and it reflects banks' continuous support to the company.

Investment view
We think Champion REIT still has lingering rating downgrade risks. On one hand, we expect it to experience some pressure on rental income due to continuous negative office rental reversion for both 3GR and LP Office. LP Office may also see a lower occupancy rate due to the downsizing of an anchor tenant. On the other hand, we think its financing costs may trend higher due to a larger exposure to floating-rate borrowings after the new loan facility. As of end-2023, its floating-rate borrowing exposure was already relatively high at 46%. As a result, we expect its adjusted EBITDA to interest expense to further deteriorate in 2024 and 2025. Its US dollar bonds are trading at the widest range of its BBB rated Hong Kong investment grade peers, having largely priced in its weaker fundamentals. We will continue monitoring its Central portfolio performance and any capital management activities.

Key downside risks to our view include 1) a significant deterioration in the Hong Kong office market; 2) higher-for-longer interest rates, leading to a continuously weaker interest expense servicing ability; and 3) any unexpected weakening in banking relationships. **A key upside risk** to our view is a quicker-than-expected turnaround in the Central office market.

CK Hutchison

UBS credit outlook: Stable
Moody's/S&P ratings: A2/A
Analyst coverage: Eve Li

Company updates

CK Hutchison Holdings (CKH) is a Hong Kong-based conglomerate that is 30% owned by tycoon Li Ka-Shing. Through its subsidiaries, joint ventures and associates (JV&A), the company runs diversified businesses globally. In 2023, the group reported HKD 462bn in revenue (including JV&A), +1% y/y. Pre-IFRS 16 EBITDA decreased 12% y/y to HKD 105bn, or decreased 1% y/y, excluding one-off gains from disposals in 2022. By geography, Europe contributed to 49% of EBIDTA (21% from the UK), followed by Asia, Australia, and others (23%). By business division, infrastructure, telecommunications, retail, and ports accounted for 28%, 25%, 15%, and 13%, respectively, of EBITDA.

In 2023, the infrastructure division (through its 75.7%-owned CK Infrastructure, CKI) maintained a stable performance and EBITDA increased by 3% in local currency terms. CKI has been distributing a steady and mildly increasing dividend to the group. Without a regulatory reset in 2024, the segment should continue to deliver steady results, in our view. Telecommunications (through the wholly-owned CH Hutchison Group Telecom, CKHGT) reported a 9%decrease in underlying EBITDA in local currencies, mainly led by cost inflation in Italy and the UK. The proposed merger between Three UK and Vodafone's UK operation was conditionally approved by the UK government in May. The company expects the division to deliver improving results this year. The retail division delivered solid EBITDA growth of 11% in local currency terms, supported by growth across different regions. The ports division's EBITDA was 14% lower in local currency terms, partly due tothe normalization of storage income. As a new container facility in Egypt commenced operations in 1Q24, the company expects moderate earnings growth this year.

Investment view

We expect CKH to continue to reduce its total debt, supported by strong cash flows and disciplined capex. As of end-2023, the company had HKD 143bn in consolidated cash and liquid investments, compared to HKD 275bn in consolidated debt. Net debt was slightly lower at HKD 132bn, and the net debt-to-net total capital ratio further improved to 16.1% (from 16.7%). We foresee a stable rating trajectory for CKH over the next 12–18 months. CKH is trading in line or slightly tighter compared to its similarly-rated Hong Kong investment grade peers thanks to its solid credit profile and diversified business. While we're neutral on most parts of the curve, we think lower benchmark rates will be a tailwind for its longer-duration bonds.

Key risks to our view include higher rates for longer and a sustained margin deterioration due to intense competition in Europe's telecom market.

CK Infrastructure Holdings

UBS credit outlook: Stable
Moody's/S&P ratings: NR/A
Analyst coverage: Eve Li

Company updates

CK Infrastructure (CKI) is a Hong Kong-based infrastructure conglomerate focused on the investment of utility assets globally, particularly in regulated businesses such as power generation, gas, and water distribution. It owns 36% of the associate Power Asset Holdings (PAH), which mainly invests in gas and electricity infrastructure. CKI was 75.7% owned by the conglomerate CK Hutchison (CKH) as of end-2023.

In 2023, CKI reported HKD 6bn in consolidated revenue, HKD 6.3bn in a share of revenue from joint ventures and associates, and HKD 8bn in net profit. The UK remained the largest profit contributor at 36%, followed by PAH in Hong Kong (25%), Australia (22%), Canada (8%), continental Europe (6%), and others. As of end-2023, the company had HKD 13bn in cash on hand, and decreased its consolidated debt to HKD 24bn (from HKD 28bn in 2022). Net debt-to-net total capital ratio was largely stable at 7.7% (vs. 7.3%).

CKI continues to look at global investment opportunities to expand its business. In April, CKI, PAH, and CK Asset (CKA) announced plans to acquire Phoenix Energy Group, one of the three gas distribution network operators in Northern Ireland. The consortium will pay GBP 313mn, of which 40%/40%/20% is shared by CKI/CKA/PAH, respectively. In May, CKI also acquired UU Solar, a 69-megawatt portfolio of renewable assets in the UK through UK Power Network (40%/40%/20% held by CKI/PAH/CKA, respectively) for a consideration of GBP 91mn.

Investment view

We expect a Stable issuer rating for CKI over the next 12 months despite the pickup in acquisition activities. Factoring in the recently announced deals, CKI still maintains a good rating buffer for its standalone rating. In addition, CKI's issuer rating contains a one-notch uplift and is equalized to that of its parent CK Hutchison given its core status in the group, according to S&P. We also expect CKI to continue to deliver resilient operating results. Its high earnings visibility is underpinned by limited regulatory resets over the next couple of years. There's no reset in 2024, and a few in 2025 (including Northumbrian Water and Wellington Electricity, etc.). We're neutral on CKI's fixed-for-life perpetuals given the limited call incentive based on our current assessment.

Key downside risks to our view include more aggressive-than-expected acquisition activities and rate sell-offs.

CLP Power Hong Kong

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Eve Li

Company updates

CLP Power Hong Kong (CLPP) is the larger of the two vertically integrated utility companies in Hong Kong, and it has a 70% stake in the power generation operator Castle Peak Power Company (Capco). CLPP serves around 2.8mn customers in Kowloon, the New Territories, and most of the outlying islands, covering over 80% of the city's population. CLPP has a diversified user base across residential (28%), commercial (39%), infrastructure & public services (29%), and manufacturing (4%). The company is wholly owned by CLP Holdings (CLPH), which also invests in power businesses in mainland China, Australia, India, Taiwan, and Thailand.

In 2023, CLPP's electricity sales increased 1.6% to 35.4bn kWh and revenue was stable at HKD 50.5bn. The company's revenue comes mostly from electricity sales (volume) and tariffs (basic tariffs plus fuel clause charges). Under the Scheme of Control (SoC) agreements, CLPP can pass its fuel and operating costs to customers. It has therefore maintained a stable EBITDA margin of around 36% over the past two years despite fluctuating energy costs. The current SoC (expiring in end-2033) also sets a permitted return of 8% on average net fixed assets, and the Tariff Stabilization Fund enables excesses or deficiencies to be held or released, based on the difference between the actual net income and permitted return.

CLPP has been growing its net fixed assets (HKD 139bn as of end-2023) steadily at a low- to mid-single-digit over the past few years via capex. Under its approved 2024–2028 development plan, CLPP projects it will spend HKD 53bn over the next five years. As a comparison, it spent HKD 11.7bn in capex in 2023, and a combined HKD 53bn between 2019 and 2023. Ongoing projects include a gas generation unit and the enhancement of a clean energy transmission system between Hong Kong and mainland China, to facilitate the phasing out of coal-fired generation. Despite the sizable capex needs, its total debt was largely stable over the past two years at around HKD 48bn, thanks to its cash-generative business and strong cash flows. Debt/EBITDA was also stable at 2.6–2.7x during the period. CLPP (together with Capco) also had HKD 13bn in undrawn facilities as of end-2023.

Investment view

We view CLPP as a defensive play due to its regulated business. The company has a higher standalone rating of aa-, versus CLPH's group credit profile of a, according to S&P. CLPP's curve is trading slightly tighter compared to similarly-rated HK developers, which we view as Fair.

Key risks to our view include an unexpected change in regulatory schemes that could lead to lower profitability, and more aggressive-than-expected debt-funded capex initiatives.

Far East Consortium

UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates

Far East Consortium (FEC) has a diverse business with projects in various geographical areas. Property development and investment accounted for 68% of revenue and 75.5% of segment profit in FY24 (fiscal year ended March 2024), while hotel operations accounted for 20% of revenue and 10.4% of segment profit. Australia generated around 51.2% of revenue and 53.1% of segment profit, while Singapore generated 18.7% and 11.3%. Hong Kong only generated 10% of revenue and 11% of segment profit. FEC reported a mixed set of FY24 results, with higher earnings, lower leverage, and weak liquidity. Revenue, EBITDA, and net profit increased 168.8%, 74.2%, and 18.5% in FY24. The strong earnings growth was mainly due to property sales in Australia and Singapore. Gross interest expense increased 40% to HKD 1.9bn, but strong earnings growth strengthened EBITDA/interest to 1.2x (FY23: 0.6x) and lowered total debt/EBITDA to 13.7x (FY23: 42.4x). Net debt/adjusted total equity also declined to 68.1% (FY23: 73.8%). Liquidity remained weak, with total cash/short-term debt of 38.8% (FY23: 30.6%) after repaying the USD 385mn bond due in January 2024.

Investment view

Media reports have said that FEC plans to repurchase one-third of the USD 360mn 7.375% perpetual notes callable on 18 October, swapping one-third of the issue into new bullet notes, and leaving the remaining one-third outstanding until the next call date in April 2025. The new bullet notes are likely to have a two- to three-year maturity with a coupon of 9%. Under the loan covenants, FEC must maintain an adjusted net gearing of below 80%, compared with 68.1% reported as of end-March 2024. If the perpetual note is not called on 18 October, the coupon will reset at the prevailing 5-year US Treasury yield plus 8.924%, or around 13% at the current 5-year Treasury yield of 4.2%.

Key risks include weaker-than-expected sales for its projects in Australia, Hong Kong, and the United Kingdom, lower occupancy rates for its hotel operations, and interest rates remaining high.

FWD Group Holdings Limited

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/NR
Analyst coverage: Daniel Tam

Company updates
FWD Group Holdings Limited (FWDGHL, formerly known as PCGI Intermediate Holdings Limited), became the ultimate parent of the FWD Group after the restructuring was completed in August 2023. FWDGHL assumed all the debt issued by its subsidiaries and became the principal entity for future debt issuances. FWDGHL raised USD 1.825bn between December 2023 and June 2024 by issuing three bonds to refinance its maturing bonds and perpetual notes callable in 2H24. FWDGHL also raised a USD 685mn club loan in February this year to support the repayment of a USD 1bn bank loan due in December 2024. After the repayments of the bonds and perpetual notes this year, FWDGHL will not have any offshore bonds maturing before 2029.

FWDGHL reported a net loss of USD 717mn in 2023, primarily due to adverse capital market movements and a USD 505mn loss on disposal of financial investments related to the Athene Reinsurance transaction in Japan. Annualized premium equivalent (APE) sales increased 18%to USD 1.65bn, while the value of new business (VNB) rose 20.4% to USD 991mn in 2023. Its new business contractual service margin (CSM) declined 4.3% to USD 1.35bn, and its total weighted premium income grew 1.9% to USD 6.4bn. In our view, FWDGHL has strong capitalization after several rounds of equity injections from pre-IPO investors. The company's local capital summation method (LCSM) tier-1 cover ratio increased to 336% in 2023 (2022: 327%) and its leverage ratio rose to 27.2% in 2023 (2022: 23.6%). Group embedded value decreased 6.3% to USD 5.7bn and comprehensive tangible equity declined 13.9% to USD 7.2bn. Return on equity expanded to 5.7% in 2023, from 4.1% in 2022.

Investment view
FWDGHL's capital buffer is sufficient to support the ongoing expansion of its operating insurance subsidiaries and to withstand near-term asset volatility, in our view. While FWDGHL recorded an accounting loss of USD 505mn from the Athene reinsurance arrangement in 2023, the deal also enabled the group to produce USD 440mn in new business CSM. We expect the group's earnings and fixed-charge coverage ratio to steadily improve in the next year or two once non-recurrent costs ease.

Key risks include weaker-than-expected profitability, adjusted financial leverage rising substantially from current levels, and regulatory risk in less-developed countries.

Henderson Land

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates
Henderson Land is one of the leading real estate developers in Hong Kong and it holds several listed companies—62.3% of Henderson Investment Limited (Exchange code 0097.HK), 50.1% of Miramar Hotel and Investment (0071.HK), 41.5% of Hong Kong and China Gas (0003.HK), 33.4% of Hong Kong Ferry (0050.HK), and 20.5% of Sunlight Real Estate Investment Trust (0435.HK). Henderson Land reported a weak set of 2023 results, with flattish earnings, higher leverage, and weak liquidity. Revenue and net profit grew 7.9% and 2.2%, while EBITDA declined 3.3%. Total debt (including shareholder loans) increased 7.9% to HKD 158.2bn, raising total debt/EBITDA to 22.8x (2022: 20.4x) and total debt/capitalization to 31% (2022: 30%). Interest expense shot up 90% to HKD 6.9bn as average funding cost almost doubled to 4.32% (2022: 2.2%), weakening EBITDA/interest to 1x (2022: 2x). Liquidity remained weak, with cash holdings and rental income covering 37.8% of short-term debt (2022: 28.3%). The group sold 1,515 units for HKD 11.1bn in 1H24 and returned undeveloped land to the government for another HKD 5.8bn, which may improve the group's near-term liquidity.

Investment view
Henderson Land has high exposure to the Kai Tak Development Area, with over 5,000 units for sale in 2H24. Owing to the high land acquisition cost and declining selling price in the area, the company may need to sell some of its units at a loss. The group is the largest agricultural landowner in Hong Kong—it owns land covering 45.8mn square feet, of which 85% is located in the Northern Metropolis. The company may return more land to the government to strengthen its liquidity. Given the company's strong shareholder support and large operating scale across different industries, we expect its banking access to continue supporting its liquidity and debt repayment ability.

Key risks include weaker-than-expected sales in Hong Kong and mainland China, which we think will force the company to raise additional debt to support its liquidity.

Hong Kong Telecommunications

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Daniel Tam

Company updates
HK Telecommunications (HKT) is a quad-play telecommunications services provider in Hong Kong with a leading market position in every major service it provides,

including fixed line, broadband, mobile, and pay television. HKT Trust is the immediate parent of HKT, and both companies operate under a trust structure. CAS Holdings, which is wholly-owned by PCCW Limited, holds 52.3% of HKT Trust. HKT reported a mixed set of 2023 results, with stable earnings, higher leverage, and stronger liquidity. Revenue, EBITDA, and net profit increased 0.6%, 2.6% and 1.9%, respectively. EBITDA margin rose to a four-year high of 39% in 2023 on higher profitability from the fixed line and mobile services. Higher finance cost weakened EBITDA/interest to 6.3x (2022: 8.6x), while net debt/equity increased to 121.4% (2022: 114.9%). Operating and free cash flows rose 5.3% and 8.1% to HKD 11.3bn and HKD 9.1bn, respectively, while cash/short-term debt strengthened to 1.6x (2022: 0.5x). On 26 June, HKT announced it would sell 40% of its fiber-based connection service to China Merchant Group's subsidiary for USD 870mn. The transaction should lower HKT's leverage and reduce its financial burden for future investments.

Investment view

HKT's revenue growth largely tracks Hong Kong's economic growth, supported by digitalization and surging data consumption from remote education, home office trends, and other emerging applications. HKT's EBITDA margin is expected to improve gradually on pent-up demand for its new mobile phone, a recovery in roaming services, and the increasing adoption of 5G. We also expect the loss from other businesses to narrow with better operating efficiency and monetization initiatives.

Key risks include intensifying broadband and mobile competition, and weaker enterprise IT spending in Hong Kong if macroeconomic weaknesses ensue.

Hongkong Land Holdings Limited

UBS credit outlook: Stable
Moody's/S&P ratings: A3/A
Analyst coverage: Eve Li

Company update

Founded in 1889, Hongkong Land Holdings (HKL) primarily focuses on developing and managing prime commercial investment properties, while also opportunistically engaging in a premium properties-for-sale business. As of end-2023, it owned and managed 0.85mn sqm of prime office and retail assets across key gateway cities including Hong Kong, Singapore, Beijing, and Jakarta. Its Central portfolio, at the heart of Hong Kong's financial district, is one of its crown jewel assets and contributed 78% to its investment properties' operating profit in 2023. Hongkong Land Company Limited (HKLC, A2 Stable/ A Stable), a wholly-owned subsidiary of HKL, holds the group's Hong Kong investment property portfolio and acts as the guarantor of the USD bonds. Conglomerate Jardine Matheson is the ultimate parent of HKL with a 53% stake.

HKL achieved USD 1.8bn in revenue in 2023, –18% y/y. The decline was led by the development property (DP) segment, while investment property (IP) still delivered a modest 2% growth in revenue to USD 1.1bn. For its Central office portfolio, revenue was 5% lower as the negative rental reversion continued. The physical vacancy rate also rose to 7.4% at end-2023 (or 6.8% on a committed basis), from 4.7% a year ago. That said, compared to the 9.9% vacancy rate of the overall Central grade A office market, HKL still outperformed, thanks to a flight to quality in demand. For its luxury-focused Central retail segment, revenue increased 16%, with mildly positive rental reversions and vacancies staying low at 1.5%.

In 2023, the company trimmed its committed capital for new projects to USD 1.3bn, compared to USD 2.1bn on average during the previous five years. Net debt was also lower at USD 5.4bn, driven by smaller share buybacks and land costs paid during the year. Nonetheless, we estimate its adjusted net leverage increased to 6.2x or 5.5x under S&P and Moody's methodology (from 5.7x and 5.1x, respectively) due to a 12% drop in EBITDA led by fewer earning contributions from property sales. On a brighter note, net gearing slightly improved to 16.8% (from 17.5%) despite a 5% valuation loss in its IP portfolio. HKL's average borrowing costs increased to 3.9% in 2023 (from 3.3% in 2022), with the impact of higher interest rates partially mitigated by the higher portion of fixed-rate borrowings (62%).

Investment view

Backed by USD 2.8bn in attributable sold but not yet recognized contracted sales, we think a rebound in DP earnings is likely this year. In addition, HKL launched a luxury residential project in its 43%-owned West Bund Financial Hub in Shanghai in April. Despite an average unit cost of CNY 50mn, all 80 units were sold upon launch, reflecting homebuyers' strong reception even amid the weak primary property market. HKL will also launch two residential JV projects in Singapore this year. Along with continuous prudent capital management, we expect the company's leverage to trend lower in 2024.

Despite some spread tightening year-to-date, HKL's bonds are still trading slightly wider compared to similarly-rated Hong Kong investment grade bonds. We think this is due to its sizable Central portfolio and higher mainland China development property exposure. We see room for the gap to further narrow if the company can deleverage, with more earnings from property for sales over the next 12–18 months. Without many catalysts in the near term, we keep our neutral view across the curve.

Key downside risks to our view include weaker-than-expected DP earnings and more-aggressive-than-expected investments.

Hutchison Port Holdings Trust

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa1/A-
Analyst coverage: Daniel Tam

Company updates

Hutchison Port Holdings Trust (HPHT) is a developer and operator of deep-water container ports in Hong Kong and Shenzhen. It is managed by HPH Management Pte. Limited, a wholly-owned subsidiary of CK Hutchison Holdings Limited (CKHH). HPHT is 80%-owned by CKHH and 20% by PSA International (PSA). The company reported a weak set of 2023 results, with lower earnings, higher leverage, and weaker liquidity. Revenue, EBITDA, and net profit declined 12.6%, 14.7%, and 41.2%, respectively. The weaker earnings raised total debt/EBITDA to 4.1x (2022: 3.7x) and net debt/equity to 40.5% (2022: 36.2%), while EBITDA/interest weakened to 7.4x (2022: 11.3x). Although operating and free cash flows remain in positive, both declined by over 30% in 2023. Cash/short-term debt also weakened to 1.7x (2022: 2.1x).

Investment view

HPHT's declining Hong Kong throughput should be offset by the rising throughput of its mainland China terminals. Due to rising US trade frictions and competition from rail transportation, HPHT's revenue and profit are both expected to remain under pressure. However, the company is expected to maintain positive cash flows on limited new capital investment and improving operating efficiency.

Key downside risks include an escalation in US-China trade tensions and a weaker-than-expected global economy. Key upside risks include a recovery in Hong Kong throughput and Chinese local governments reducing subsidiaries to Chinese ports that are not controlled by HPHT.

Hysan Development Company Limited

UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa1/NR
Analyst coverage: Eve Li

Company updates

Hysan Development is the largest landlord in Causeway Bay (Hong Kong's prime shopping area), with 4.5mn square feet in rental properties valued at HKD 96bn. In 2023, Hysan's revenue was 7% lower at HKD 3.2bn, with a weaker performance across retail, office, and residential segments. The ongoing Lee Gardens asset enhancement project and a weak office market partly explained the revenue decline. Reported net gearing was 4 percentage points higher at 27.2% compared to the end-2022 level. Counting its perpetual bonds as debt (50% equity credit for the subordinated perp), we estimate its adjusted net debt-to-EBITDA increased to 12.3x (from 10.1x in FY22), and EBITDA to adjusted interest (including capitalized interest) weakened to 1.6x (from 2.2x). The company's liquidity remained adequate, with HKD 3.9bn in cash and term deposits, while short-term debt was minimal. It also has HKD 6.4bn in undrawn committed revolving loans. Hysan cut the full-year dividend by 25%, the first cut since 2003.

The Caroline Hill Road commercial property project, a 60/40 joint venture (JV) between Hysan and Chinachem Group, is still under construction and is scheduled for opening in late 2026. Hysan has HKD 5bn in secured undrawn term loans to fund the construction. Annual total capex, including the Caroline Hill Road project and Lee Gardens rejuvenation, is guided to be HKD 2bn till 2026.

In April, Hysan launched a tender offer targeting its 4.1% subordinated perpetuals and accepted USD 100mn in aggregate principal. The outstanding amount of the perpetuals was then reduced to USD 750mn.

Investment view

We think the weak FY23 results raise Hysan's downgrade risks. The company has expanded into Caroline Hill Road and some residential projects, and has also invested in Shanghai commercial properties, flexible workspaces, and healthcare services over the past few years. These investments have led to a siginificant increase in its total debt, which has also raised its interest costs in a higher rate environment. We think its leverage may stay elevated over the next 12–18 months as it may further draw down loans to fund capex activities.

In December 2023, Moody's revised the outlook of Hysan's Baa1 issuer rating to Negative from Stable. We estimate Hysan's adjusted credit metrics (pro-rata numbers considering the JV-level debt and interest expenses) breached Moody's downgrade triggers for both the net leverage and interest coverage ratio in 2023. A rating downgrade, should it happen, will move its 4.1% subordinated perpetual note (perp) to the high-yield (HY) category due to the two-notch rating difference versus the issuer's rating. We view the valuation of Hysan's senior bullet bonds as being not that appealing compared to other Hong Kong BBB names. We're neutral on its subordinated perps considering the greater upside if called on the first call date, although we are aware of the currently high uncertainty surrounding its call decision. We also rate its fixed-for-life perp as Fair.

Key upside risks to our view include 1) a better-than-expected recovery in Hong Kong's retail and office rental markets; 2) better-than-expected sales of its luxury residential units; and 3) a redemption of the subordinated perp on the first call date. **Key downside risks** to our view include 1) an unexpected deterioration in Hysan's banking relationship; and 2) an aggressive investment appetite and larger-than-guided capex needs.

Li & Fung Limited

UBS credit outlook: Stable
Moody's/S&P ratings: Ba3/BB
Analyst coverage: Daniel Tam

Company updates

Li & Fung (L&F), privatized in 2020, is one of the world's leading consumer product sourcing and trading companies. Based in Hong Kong, the company's long operating history and extensive network of suppliers and partners support efficient sourcing and distribution. The company reported a mixed set of 2023 results. Revenue and EBITDA declined 19.3% and 27.1%, respectively, but net profit increased 41.3%, partly due to higher interest income. L&F reported a positive operating cash flow of USD 117mn in 2023, but free cash flow turned negative USD 265mn after bond repayments. At the end of 2023, L&F had a total cash holding of USD 452mn and no bank loans or short-term debt. The USD 313mn bond due in 2025 is L&F's only outstanding debt; hence, it had a net cash position of USD 139mn. EBITDA/interest remained unchanged at 1.8x, and total debt/EBITDA declined to 2.4x in 2023 from 2.9x in 2022.

Investment view

L&F's cash holding is sufficient to repay its 2025 bond, but we believe L&F is unlikely to redeem the USD 650mn fixed-for-life (FFL) perpetual note until the company can refinance it at a lower cost. Global deglobalization is positive for the company's onshore wholesale business, which operates as a domestic supplier in America, UK/Europe, and Asia.

Key risks include a further deterioration in US/EU consumer sentiment and the company conducting large-scale acquisitions that weaken its liquidity.

Lifestyle International

UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates

Lifestyle International, privatized in 2022, is a premier retail operator based in Hong Kong. The company's flagship SOGO department store in Causeway Bay became the only store under operation after its Tsim Sha Tsui store closed in March 2023. The company has a commercial property in London, whose current lease will expire in May 2025. The company's Kai Tak Project, which includes The Twins and the SOGO Kai Tak store, will commence operation in September 2024. Around 50% of the leasable area has been filled, and management aims to achieve around 80% by September 2024.

Lifestyle reported a mixed set of 2023 results, with improved earnings, lower leverage and weak liquidity. Revenue and EBITDA increased 24.9% and 38.7%, respectively, and returned to a net profit of HKD 1.4bn in 2023 (a net loss of HKD 611mn in 2022). The stronger earnings lowered EBITDA/interest to 1.4x (1.5x), while net debt/equity declined to 5.5x (9.5x). The company's operating cash flow increased 47.5% to HKD 1.4bn, while negative free cash flow narrowed to HKD 421mn (HKD 948mn). At the end of 2023, Lifestyle invested in listed equities with a fair value of HKD 1.2bn (USD 149mn) and had an unutilized committed secured loan facility of HKD 2.8bn (USD 128mn). The company completed a HKD 7.85bn (USD 1bn) 5-year club loan on 3 July to refinance the HKD 6.95bn loan maturing in July and support the repayment of the USD 266mn bond, both of which were due in July. The loan is secured by the group's Kai Tak Project, with an estimated market value of HKD 18bn (USD 2.3bn) at the end of 2023.

Investment view

Lifestyle's earnings were negatively affected by the closure of its Kowloon store and weaker retail sales in Hong Kong. We expect the company's earnings to improve in 2025 after the commencement of operation for The Twins and the SOGO store in Kai Tak.

Key downside risks include weaker-than-expected domestic consumption, lower-than-expected occupancy rates for The Twins, and high interest rates. Upside risks include a higher-than-expected take-up rate for The Twins project and a recovery in retail sales in Hong Kong.

Link REIT

UBS credit outlook: Stable
Moody's/S&P ratings: A2/A
Analyst coverage: Eve Li

Company updates

Established with retail and carpark facilities divested by the Hong Kong Housing Authority, Link REIT has enriched its portfolio with office and logistics assets, and expanded its footprint to other major cities over the years. As of March 2024, its portfolio value had reached HKD 241bn, consisting of 130 assets in Hong Kong, 12 in mainland China, and 12 overseas (Australia, Singapore, and the UK). Hong Kong accounted for 76% of its total revenue in FY24, mainly from local retail. Its Hong Kong retail assets are non-discretionary in nature and are integral to the city's consumption infrastructure. Link REIT (823 HK) is listed on the Hong Kong Stock Exchange with no controlling shareholder.

In FY24 (fiscal year ended in March 2024), Link REIT reported HKD 13.6bn in total revenue, +11% y/y. The overseas market's share of revenue increased to 13% (from 5%), as the contribution from its Singapore acquisitions kicked in. Operating metrics remained solid, with the occupancy rate at 98% for Hong Kong retail and healthy levels observed across other geographies. Tenant sales growth moderated to +0.4% y/y, mainly affected by the supermarket segment (–5%). The performance was impacted by cross-border consumption in the second half of FY24. That said, occupancy costs remained healthy at 12.6%. Management has guided for a flattish rental reversion in FY25 (from 7.9% in FY24).

Net debt edged higher to HKD 49.3bn (from HKD 47.6bn), bringing the reported net gearing (net debt over total assets) to 19.5% (from 17.8%). That said, supported by an increase in EBITDA, net debt-to-adjusted EBITDA improved to 4.9x (from 5.4x). Interest expenses soared over 30% to HKD 2.5bn amid the higher interest rate environment, while the interest coverage ratio remained resilient at 4x. The portion of fixed-rate borrowings increased to 70%, from 57% a year ago. The company expects average borrowing costs to stay below 4%, compared to 3.78% in FY24.

Investment view
While the sales leakage to nearby cities has posed near-term challenges to Hong Kong's local consumption recovery, it remains to be seen whether this will structurally damage landlords' operations. Given the non-discretionary nature of Link REIT's retail assets and the current healthy occupancy cost, we do not expect a collapse in its related rental revenue over the next 12 months. As a result, we still expect an adequate rating buffer over the same period of time. We remain neutral on its US dollar bonds.

Key downside risks to our view include 1) aggressive debt-funded acquisitions; and 2) northbound spending posing structural challenges to its tenants, leading to a weaker-than-expected performance of its non-discretionary retail portfolio and a significant negative rental reversion.

Nan Fung International
UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Daniel Tam

Company updates
Nan Fung was privatized in 2020 and is wholly owned by the Chen family. The company has not made any major acquisitions for property development since 2017 and sold most of its large-scale residential projects by the end of 2023. Revenue from property development declined to 18.6% of total revenue in 2024 (fiscal year ended March 2024), down from 73.7% a year earlier. Nan Fung has a rental portfolio with 34 assets, generating HKD 2.1bn of rental income in FY24, covering 1.4x of gross interest expense. Rental income should rise further, in our view, as more investment properties commence operations. The company also has an unleveraged investment portfolio of around HKD 15.3bn (FY23: USD 2.1bn) as of 31 March 2024. The portfolio includes private equity funds (19% of the portfolio), unquoted direct investments (43%), fixed income fund (4%), venture capital fund (22%), and others (12%).

Nan Fung reported a mixed set of FY24 results, with a net loss, lower leverage, and strong liquidity. Revenue declined 61.7%, as property development revenue dropped 90.3%, while EBITDA plunged by 99.4%. The company postedo a loss of HKD 3.7bn (FY23: HKD 1.2bn profit) because of an HKD 4.8bn revaluation loss on its investment properties. Despite the weaker EBITDA, rental income covered 1.4x of gross interest expense (FY23: 1.3x). Total debt declined 10.6%, lowering total debt/capitalization to 24% (FY23: 25%), while cash/short-term debt remained strong at 4.1x (FY23: 6.8x). Operating cash flow increased 5.6% to HKD 3.6bn, while free cash flow fell 21.9% to HKD 1.7bn.

Investment view
Following the disposal of most of its development projects, rental income and hotel revenue will account for more than half of total revenue over the next few years. The company is unlikely to redeem its fixed-for-life perpetual note until it can refinance the note at a lower cost, and its next offshore bond will be due in October 2027. Its bank loans are mostly secured with assets and are expected to roll over upon maturity.

Key risks include weaker rental income from its investment property portfolio, weaker financial markets, and more aggressive land bank replenishment activities.

New World Development
UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates
After the Hong Kong government announced the development of the Northern Metropolis (NM), NWD signed strategic partnership agreements with three state-owned enterprises, including China Resources Land, China Merchants Shekou, and Shum Yip. The company plans to form joint ventures with them and sell its farmland in NM to the joint-venture companies. NWD has also announced that it completed the refinancing and repayment of a total of HKD 35bn in short-term debt due before the end of 2024. The company has also refinanced a HKD 9.5bn hotel joint venture loan with the Abu Dhabi Investment Authority, which includes HKD 260mn in new funding. The average offshore loan cost is around HIBOR plus 1.1%. NWD has also

raised CNY 2.6bn in onshore commercial operating loans at 2.9–3% and targets to raise an additional CNY 8.6bn in 2024 to repay its offshore debt.

NWD reported mixed 1HFY24 results (fiscal year ended in June 2024), with higher earnings and lower leverage, but liquidity remained weak. Revenue declined 25%, while EBITDA and net profit increased 19.6% and 15.9%, respectively. Total debt fell 12.6% after the disposal of NWS, lowering total debt/EBITDA to 15.6x (1HFY23: 18x). Although average funding cost rose to 5.1% (3.8%), gross interest expense (including distribution to perpetual note holders) declined 20.3%. Stronger earnings and lower interest expense strengthened EBITDA/interest to 1.5x (1HFY23: 1x), but liquidity weakened with cash/short-term debt of 0.6x (0.9x). As NWD likely achieved its HKD 8bn non-core asset disposal in 2HFY24, its liquidity should also have improved in 2HFY24.

Investment view

The monetarization of NWD's onshore investment property portfolio and its farmland in the Northern Metropolis likely improved the company's liquidity in FY24; while FY24 has eneded, NWD has yet to report FY24 results. NWD also has several projects in Hong Kong and mainland China which will be launched in 2H24. Given the company's continued access to onshore and offshore bank financing, the ability to monetarize land reserves, and continued shareholder support, NWD should be able to deleverage gradually. NWD will likely redeem its high step-up perpetual notes, while keeping the fixed-for-life perpetual notes outstanding until they can be refinanced at a lower cost.

Key downside risks include a further weakness in mainland China and Hong Kong's real estate markets, a slowdown in the development of the Northern Metropolis, and a failure to monetize its farmland in NM as planned. Key upside risks include further refinancing of its offshore debts with lower-cost onshore borrowings and a faster-than-expected deleveraging pace.

NWS Holdings

UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates

NWS is 77.8%-owned by Chow Tai Fook Enterprise, which also holds 45.2% of New World Development. The company classifies its operation into six key segments—roads (38.3% of attributable operating profit in 1HFY24), insurance (19.4%), construction (18.5%), logistics (16.7%), facilities management (5.8%), and others (1.3%). NWS owns concession rights for 15 expressways in mainland China. NWS issued a CNY 3.5bn 3-year Panda bond with an annual interest rate of 3.9% in early 2024. Issuing lower-cost CNY-denominated bonds will lower NWS's funding cost and expand its funding channels, in our view. The bonds also work as a natural hedge for the company's onshore revenue, such as toll roads and logistics infrastructure. The company reported healthy 1HFY24 results (fiscal year ended June 2024), with higher earnings, lower leverage, and stable liquidity. Revenue, EBITDA, and net profit increased 6.7%, 26.8%, and 15.6%, respectively. The stronger earnings improved EBITDA/interest to 4.1x (3.6x in 1HFY23) and lowered total debt/EBITDA to 5.2x (7.2x). Total debt/capitalization also declined to 44% (50%). Liquidity weakened, as cash/short-term debt fell to 1.8x (3.1x) after the company redeemed the USD 1bn perpetual note in January 2024.

Investment view

NWS's leverage increased after the special dividend payment in April 2024, but we expect it to subsequently decline over the next few years. The company's strong cash generation ability should support its debt repayments, but the company's free-float issue remains below 25% after the special dividend, and this will need to be addressed in a timely manner.

Key downside risks include its persistent insufficient free-float, a weaker-than-expected domestic and mainland China economy, and unexpected large-scale acquisitions. Key upside risks include a faster-than-expected decline in leverage, and the continued refinancing of its offshore debts with lower-cost onshore borrowings.

Pacific Century Premium Developments Limited

UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates

Pacific Century Premium Developments (PCPD) is principally engaged in the development and management of premium-grade property infrastructure projects as well as premium-grade property investments. It operates in Japan, Indonesia, Thailand, and Hong Kong. Japan and Indonesia accounted for 90% of PCPD's total revenue and 65% of its total assets in 2023. The company's 2023 results remained weak. Although revenue increased 46.5% and EBITDA turned to a positive HKD 84mn (2022: an EBITDA loss of HKD 20mn), PCPD saw a net loss of HKD 466mn in 2023 (2022: HKD 598mn net loss). Years of net losses have also eroded the company's equity base, resulting in a 43.4% drop in total equity and raising net debt/equity to 12.6x (6.9x). Operating cash flow increased to HKD 245mn in 2023 from HKD 101mn in 2022, but free cash flow declined 86.2% to HKD 261mn. Leverage remains high, with total debt/EBITDA at 112.3x and total cash covering 1.6x of short-term debt.

Investment view
PCPD's HKD 865mn cash holdings and operating cash flow should support the repayment of its HKD 1.06bn debt maturing in 2024 and 2025. However, it would be challenging for the company to repay the HKD 8.4bn debt across USD bonds and secured bank loans maturing in 2026. We believe PCPD may have to rely on support from its largest shareholder PCCW and related parties for a smooth refinancing. PCCW, together with its shareholder, should have the ability and the intention to avoid defaulting on its subsidiaries' debt, as it would negatively affect funding costs and funding accessibility for PCCW and its other subsidiaries.

Key downside risks include unexpected events that prevent PCCW from supporting PCPD's refinancing and aggressive debt-funded expansion initiatives. Key upside risks include a large-scale equity-financing to strengthen its equity base and the ability to dispose of its assets at higher-than-expected valuations.

Regal Hotel
UBS credit outlook: Deteriorating
Moody's/S&P ratings: NR/NR
Analyst coverage: Daniel Tam

Company updates
Regal Hotel (exchange code: 78.HK) is 69.3%-owned by Paliburg Holdings (617.HK) and holds 75% of Regal Real Estate Investment Trust (1881.HK). Chairman Lo Yuk Sui holds 61.9% of Century City International Holdings, which has a 62.3% stake in Paliburg Holdings. Regal Hotel is one of the largest hotel groups in Hong Kong, operating and controlling hotel properties in Hong Kong though its investment in Regal REIT. It also operates and controls hotels in mainland China.

Regal Hotel reported a weak set of 2023 results, with a wider net loss, higher leverage, and weak liquidity. Revenue and EBITDA declined 2.1% and 27.5% respectively, owing to a lower profit margin. Net loss widened to HKD 1.9bn (2022: HKD 411mn net loss) due to a 92.4% rise in interest expense and fair value losses on financial assets, mainly reflecting its shareholding in Cosmopolitan International (0120.HK), which saw a net loss. Total debt (perpetual as equity) increased 3.8% to HKD 16.17bn, raising total debt/EBITDA to 30.2x (2022: 21.1x) and net debt/equity of 180% (2022: 136%). Liquidity remained weak, with total cash covering just 33% of short-term debt (2022: 19%). However, operating cash flow increased to HKD 556mn (2022: HKD 210mn) and free cash flow turned to a positive HKD 435mn (2022: a negative HKD 155mn).

Investment view
Regal Hotel has been able to roll over its bank loans, secured by its hotel assets. It also disposed of two aircrafts for HKD 347mn in April. The company should benefit from the Hong Kong government's efforts to promote Hong Kong as a major tourist destination.

Key downside risks include weaker spending by mainland Chinese tourists and high interest rates that keep the company's financial costs high. Key upside risks include a stronger-than-expected recovery of tourists visiting Hong Kong.

Sun Hung Kai Properties
UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Eve Li

Company updates
Sun Hung Kai Properties (SHKP) is one of the largest property developers and landlords in Hong Kong. The Kwok Family Trust is its largest shareholder. As of end-2023, SHKP had a land bank comprising a total of 58.8mn square feet in Hong Kong and 67.2mn square feet in mainland China, including properties under development. In FY23 (ending 30 June 2023), the company reported HKD 34.7bn in segment operating profit (OP, including joint venture and associates). By segment, property rental was the largest contributor (53%), spanning Hong Kong (72%), mainland China (25%), and Singapore (3%). The second largest contributor was property sales (33%), of which 75% was from Hong Kong and 25% from mainland China. The rest of the segment OP was from hotel, telecom, transportation, and other businesses.

In the first half of FY24, SHKP achieved HKD 12.9bn in attributable contracted sales, of which 74% was in Hong Kong. Major contributors such as YOHO WEST Phase 1, NOVO Land Phase 2A, and University Hill were well received by the market. Gross rental revenue (including JV&A) rose 4% y/y to HKD 12.5bn, driven by retail rental growth and the withdrawal of onshore rental concessions. Over the next few years, recurrent income is expected to further expand due to new investment properties, including the High Speed Rail West Kowloon Terminus Development JV project. Its Hong Kong office segment (one-third of Hong Kong rental revenue) saw revenue declining a modest 3% y/y amid the rising supply, but was supported by flight-to-quality demand. The company's Hong Kong office occupancy was steady h/h at 92%.

SHKP's total debt rose 9% to HKD 136bn as of end-2023, and net gearing was higher at 21.2% (from 18.2% six months ago). Using S&P's methodology, we estimate its adjusted debt (deducting 75% of cash on hand and adding lease liabilities plus guarantees) was also higher by 13% h/h on a reduced cash balance. As a result, adjusted debt/LTM EBITDA increased to 3.95x (from 3.4x in FY23). A leverage ratio above 3.5x on a sustained basis may trigger a downgrade by S&P, in our view. That said, we think the full-year number will improve given that SHKP expects to receive HKD 20bn in sales proceeds in the next few months. Its prudent financial management and disciplined capex will also prevent a sharp increase in debt, in our view. Despite higher interest costs, we estimate that SHKP has maintained a satisfactory adjusted interest coverage ratio at above 6x. The company has a strong liquidity position, including ample undrawn committed banking facilities.

Investment view
We view SHKP as a resilient credit due to its leading market position, robust recurring income, and a strong balance sheet. Based on our analysis above, we expect a stable rating trajectory over the next 6–12 months. We currently have Fair ratings across the curve.

Key downside risks to our view include a worse-than-expected softening in the property market and aggressive debt-funded investments.

Swire Pacific
UBS credit outlook: Stable
Moody's/S&P ratings: A3/A-
Analyst coverage: Eve Li

Company updates
Swire Pacific is a Hong Kong-based conglomerate with property investment and trading, beverages, aviation, trading, and industrial businesses. It principally operates in Hong Kong, mainland China, and Southeast Asia, after the disposal of its beverage franchise business in the US in 2023. The company has three core divisions: 1) property (Swire Properties), which consists of the development and operation of commercial properties, as well as property trading activities; 2) beverages (Swire Coca-Cola), which runs the manufacturing, marketing and distribution of products from the Coca-Cola company exclusively in certain regions across mainland China, Hong Kong, Taiwan, Vietnam, and Cambodia; and 3) aviation, which includes an associate interest in Cathay Group and the wholly-owned Hong Kong Aircraft Engineering Company (HAECO). As of end-2023, JS&S owned 60.3% of Swire Pacific, with 68.1% of voting rights.

In 2023, Swire Pacific reported HKD 94.8bn in revenue, +3% y/y. By revenue contribution, beverages, aviation, and property accounted for 55%, 19%, and 15%, respectively, of the top-line. The reported recurring underlying profit jumped to HKD 10.4bn (from HKD 3.8bn), led by the turnaround of the aviation business. Property, aviation, and beverages contributed to 57%, 34%, and 23% of the recurring underlying profit, respectively. Despite elevated capex and an investment of HKD 23bn in the year, the company managed to lower its net debt by 2% to HKD 60.2bn. The reduction was mainly supported by operating cash flows and HKD 36bn in disposal proceeds. As of end-2023, it had HKD 34.9bn in undrawn committed facilities. Net gearing also improved to 18.5% (from 19.5%). While its adjusted interest expenses may further increase over the next 1–2 years from HKD 3.4bn in 2024, its high exposure to fixed-rate borrowings (76%) provides some buffer, in our view.

Investment view
Swire Pacific remains active in investing in its core markets and segments. In February 2024, it conditionally agreed to acquire a majority stake of franchise businesses in Thailand and Laos. In May 2024, it also completed the acquisition of a controlling stake in DeltaHealth in China. Healthcare-related investments may continue to pick up, in our view, and its total debt could grow amid the ongoing investment plans. That said, with the resumption of Cathay Pacific's dividends, the ramp-up of its newly acquired business and the launch of some property projects, we think the company's EBITDA growth may gradually pick up over the next two years. We expect the company to invest prudently over the period to maintain a leverage ratio that is in line with its current rating (4.1x in 2023, versus S&P's 4.5x downgrade trigger). We remain neutral on its curve due to less appealing valuations.

Key risks include 1) more aggressive-than-expected investments and a slow ramp-up of newly acquired businesses that lead to a higher leverage; and 2) a worse-than-expected rental performance from Swire Properties for a sustained period.

Swire Properties
UBS credit outlook: Stable
Moody's/S&P ratings: A2/NR
Analyst coverage: Eve Li

Company updates
Founded in 1972, Swire Properties is a leading developer, owner, and operator of prime mixed-used properties. As of end-2023, its completed leasing and hotel portfolio had an attributable gross floor area of 24.4mn sqft and was diversified in offices (50%), retail (37%), hotel (10%), and service apartments (3%). The company also had a pipeline of 10mn square feet of investment properties and 4.7mn square feet in trading properties. Its flagship properties include Pacific Place and Taikoo Place in Hong Kong, and Taikoo Li and Taikoo Hui projects in top-tier cities in mainland China. The valuation of its investment property portfolio has reached HKD 281bn currently, excluding hotels and joint-venture projects. Out of its HKD 15.2bn in attributable gross rental income in 2023, the biggest contributor was Hong Kong office (38%), followed by mainland China retail (34%), Hong Kong retail (17%), and others. The company is 82% owned by the conglomerate Swire Pacific, accounting for nearly half of the parent's recurring attributable profit in 2023.

In 2023, Swire Properties grew its attributable gross rental income by 8% to HKD 15.2bn in 2023, as its retail portfolio posted significant growth post-border reopening and the acquisition of additional interests in Taikoo Li Chengdu. Rental revenue from Hong Kong offices, however, declined 3% due to negative rental reversion. The company continued its HKD 100bn investment plan and had committed 60% at end-2023 (from 39% at end-2022). Among the investments last year, it acquired a 40% stake in two mixed-use projects in Shanghai and obtained ownership in several redevelopment projects in Hong Kong.

Despite capital recycling including the disposal of 12 office floors at One Island East to the Securities and Futures Commission, the debt-funded expansion led to a higher debt level, and net debt nearly doubled to HKD 36.7bn. That said, net gearing stayed low at 12.7% and its undrawn committed facilities further increased to HKD 12.7bn (from HKD 9.9bn). In 2023, its weighted average borrowing cost edged up to 4.1% (from 3.2%), with the portion of fixed-rate borrowings staying high at 68%.

In May, Swire Properties released its 1Q24 operating update, revealing weakness across the board. For the Hong Kong office segment, while occupancy was largely unchanged at 98% and 91% in Pacific Place and overall Taikoo Place, respectively, negative rental reversion widened to –17%/–13% in the quarter, compared to –12%/–6% in 2023. Its mainland China retail portfolio also saw tenants' sales declining due to renovation and a high base, except for Taikoo Li Qiantan in Shanghai, which posted a modest gain of 1%. Occupancy, however, remained healthy at 92–100% for its six retail projects.

Investment view

Adding attributable net debt of JVs and associates, we estimate that the company's net leverage increased to 4.9x as of end-2023 (from 3.7x a year ago) under Moody's methodology. Adjusted interest coverage also weakened to around 6x (from 9.2x) amid the higher interest rate environment. That said, we think the company still maintains some rating buffer against the downgrade triggers. Swire Properties' US dollar bonds still offer a slight premium versus similarly-rated Hong Kong investment grade bonds, reflecting market concerns over their Hong Kong investment property exposure—we view this as Fair.

Key downside risks to our view include 1) more aggressive debt-funded investments; and 2) a worse-than-expected rental performance for a sustained period.

Figure 24 - Indian issuers covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
Adani Ports	Stable	Baa3/BBB-				
Adani Transmission	Stable	Baa3/NR				
Bharti Airtel	Stable	Baa3/BBB-				
Delhi International Airport	Improving	B1/BB-				
Export-Import Bank of India	Stable	Baa3/BBB-				
HPCL-Mittal Energy	Stable	Ba1/NR				
Indian Railway Finance Corporation	Stable	Baa3/BBB-				
NTPC Limited	Stable	Baa3/BBB-				
Oil & Natural Gas Corp	Stable	Baa3/BBB-				
Power Finance Corporation	Stable	Baa3/NR				
REC Ltd	Stable	Baa3/NR				
Reliance Industries	Stable	Baa2/BBB+				
Tata Motors	Improving	Ba3/BB+				
Tata Steel	Stable	Baa3/BBB-				
Vedanta Resources	Stable	Caa3/CCC+				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 9 - Key financial & credit metrics (FY2024, year ending March 2024)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total debt/ capital
Adani Ports	3.2	59.4%	5.9	2.5x	5.9x	47.5%
Adani Transmission Limited	2.1	36.7%	4.4	5.5x	3.3x	73.0%
Bharti Airtel Limited	18.0	52.7%	25.8	2.6x	3.5x	67.1%
Delhi International Airport	0.6	26.4%	1.8	10.9x	1.1x	89.5%
HPCL-Mittal Energy	11.0	8.9%	4.4	4.1x	3.1x	69.5%
NTPC Limited	21.5	28.6%	28.4	4.5x	4.2x	47.7%
Oil & Natural Gas Corp	77.6	15.8%	18.3	1.1x	10.0x	19.9%
Reliance Industries	109.7	17.7%	41.5	1.5x	7.0x	27.2%
Tata Motors	52.5	13.6%	13.6	0.9x	6.9x	33.8%
Tata Steel	27.5	9.7%	10.4	3.3x	3.0x	48.5%
Vedanta Resources	17.1	28.2%	14.3	2.6x	2.9x	106.3%

Source: Company reports, UBS

Adani Ports

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Devinda Paranathanthri

Company updates

Adani Ports is one of the largest privately-owned port operators in India. FY24 results were strong, with the company achieving 24% growth in cargo handled, representing around a quarter of the country's total cargo volumes. Consolidated revenue and EBITDA for FY24 were up 28% and 24%, respectively, while its debt declined modestly. As a result, overall net debt to EBITDA improved to 2.5x in FY24 from 3.5x in FY23. Given the stable GDP growth backdrop for India, the near-term earnings outlook for Adani Ports is also constructive, and we believe the company in on track to achieve 10–15% growth in EBITDA. Following the negative headlines relating to a short-seller report, management vowed to take a more measured approach to capex. However, we note that FY24 capex still exceeded previous guidance. Given that access to funding has somewhat normalized after last year's concerns, we would not be surprised to see management embark on some acquisitions going forward. With net leverage now at 2.5x, we believe there is a bit more headroom for the company's ratings to cope with potential M&As.

Investment view

We expect the corporate governance premium on the bonds (vs. its Indian BBB peers) to remain throughout the remainder of the year. While recent developments suggest the regulator's inquiry may end without an unfavorable outcome for Adani, we will not be surprised to see negative headlines pop up time and time again. Therefore, we continue to expect increased volatility in the bonds. From a credit perspective, a rating downgrade or material issues regarding access to funding are unlikely, in our view. We note that all the major rating agencies now have a stable outlook on Adani Ports, and its overall credit metrics have improved materially over the past year. Adani Energy issued a USD bond in 1Q24, and we believe Adani Ports will also be able to issue debt in the primary market to meet its near-term debt maturities albeit at a higher cost than in the past. We are comfortable owning bonds up to 4–5 years but take a more cautious approach to the longer-dated ones.

Key risks include an unfavorable outcome from the regulator's investigation and aggressive M&As at the expense of the company's balance sheet.

Adani Transmission

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Devinda Paranathanthri

Company updates

Adani Transmission is one of the largest private sector power transmission companies in India. FY24 earnings overall showed strong growth, with revenue and EBITDA increasing 25% and 33%, respectively. However, annual capex remained high at nearly INR 55bn, leaving limited room for debt reduction. The company has previously guided that annual capex will likely stay at this level in the medium term, which is likely to limit free cash flow generation. Net leverage improved to 5.5x in FY24 from 6.9x in FY23.

Investment view

The transmission business is a highly regulated one, with revenues under both cost-plus and tariff-based competitive bidding frameworks likely to offer relatively stable earnings going forward. While Adani Transmission's net leverage of above 5x looks optically high, we are comfortable with these leverage levels as it is a stable utility business. We expect the corporate governance premium on the bonds (vs. its Indian BBB peers) to remain for the remainder of the year. While recent developments suggest the regulator's inquiry may end without an unfavorable outcome for Adani, we will not be surprised to see negative headlines pop up from time to time. Therefore, we continue to expect increased volatility in the bonds. We are comfortable owning the 2026 bond, but stay cautious on the 2036 bond until the governance-related headlines settle down.

Key risks include an unfavorable outcome from the regulator's investigation and aggressive M&As at the expense of the company's balance sheet.

Bharti Airtel

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Joel Tan

Company updates

Bharti Airtel is India's largest integrated communications provider and the second-largest mobile operator in Africa. The company has posted robust revenue and EBITDA growth over the past few years, driven by a growing consumer base and improved pricing power. FY24 results were mixed, as revenue rose 7.8% to INR 1.1tr, EBITDA increased 12.3% to INR 790bn, but profits declined 19.5% to INR 65bn. During FY24, Bharti Airtel rolled out more than 46,000 network towers and increased its subscriber base by 43.5 million customers, which boosted its top-line performance. Region-wise, Bharti Airtel's Indian operations outperformed, while its African operations were bogged down by the devaluation of African currencies during the year. Higher finance costs also ate into Bharti Airtel's profitability. Bharti Airtel's credit metrics remained broadly stable in FY24, with net leverage at 2.6x (FY23: 3.1x) and interest coverage at 3.5x (FY23: 3.7x). Gearing (total debt/capital) marginally improved to 67.1% (FY23: 68%). Going forward, we expect Bharti Airtel to continue on its deleveraging trend, buoyed by strong free cash flow generation.

Investment view

Bharti Airtel's established presence in the Indian and African telecom markets, a growing subscriber base, and improved pricing power following sector consolidation should continue to support its financial and credit profile, in our view. We think Bharti Airtel's credit metrics are on solid footing for a low BBB credit, and we do not expect the issuer to be a fallen angel candidate in the near term. Bharti Airtel also enjoys operational support from dominant shareholder Singtel, which is majority owned by Temasek Holdings. We see Bharti's senior bonds as fairly valued compared to other Indian low BBB credits. For investors looking for yield enhancement, Bharti Airtel's subordinated perpetual notes provide a decent yield pickup over the senior bonds, with their reasonable reset spreads reducing extension risk.

Key risks include unfavorable regulatory changes which negatively impact its operational performance, heightened geopolitical risks in the countries that the company operates in, and foreign exchange risk in relation to its African operations.

Delhi International Airport

UBS credit outlook: Improving
Moody's/S&P ratings: B1/BB-
Analyst coverage: Devinda Paranathanthri

Company updates

Delhi International Airport (DIAL) operates, manages, and develops India's Indira Gandhi International Airport. India's air passenger traffic has now fully recovered to pre-COVID levels, with Delhi International Airport's FY24 traffic reaching 73.7mn, up 13% y/y. The multi-year Phase 3A expansion is finally coming to an end, with the new terminal likely to be operational in 3Q24. The company does not expect much expansion capex in the coming year. Therefore, we believe the company's leverage metrics likely peaked in FY24 and should start to gradually improve in the coming two to three years. We expect FY24 debt to EBITDA to be around 11x and we believe this can improve to around 7x in FY26. Assuming around 8–9% growth in passenger traffic annually, we believe this metric will improve to around 5–6x in the next three years as the new capacity generates more earnings. Rating agencies have already taken into account potential improvements, and the company has received a few rating upgrades after passenger traffic recovered over the past year.

Tariffs for the next control period (FY25–29) are due for renewal, but there may be a delay judging by past trends. However, as the company's relationship with the regulator becomes more mature, we do not expect to see an extended delay and believe there could be a finalization in the current calendar year. DIAL's larger asset base after the phase 3A capex will likely increase the tariffs as they are determined based on the return-on-assets model.

Investment view

While any potential delays in finalizing the new tariffs remain a risk, we believe Delhi International Airport's fundamentals are on the right track. If its leverage can improve based on our above estimate, we believe its credit rating can improve to a low BB by all three agencies. The company has also shown its ability to access the onshore bond market, which alleviates any near-term refinancing concerns. We believe most of the positive developments mentioned above are already priced into the bonds as they currently trade in line with their BB peers. We see the 2029 bond as a stable carry play in the near term.

Key risks include extended delays in finalizing the tariffs for the next control period resulting in a slower deleveraging process.

Export-Import Bank of India

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Timothy Tay

Company updates

Set up under an Act of Parliament in 1981 by the Government of India, Export-Import Bank of India (EXIM India) is a 100% state-owned policy institution that provides financial assistance to exporters and importers with the objective of promoting India's international trade. EXIM India's loan book is fairly evenly split between policy loans (backed by government guarantees) and commercial loans, with are generally to high quality issuers (87% rated BBB and above). In FY24 (financial year ending March), EXIM India recorded robust net interest income of INR 149bn (+36.2% y/y) and a very healthy profit of INR 25bn (+612.9% y/y), driven by robust loan growth and reduced provisioning. As at end-March 2024, total loans amounted to INR 1.6tr (+17.2% y/y), accompanied by a 20.3% y/y rise in debt issued and borrowings to INR 1.5tr. Asset quality improved significantly in FY24, with gross non-performing assets (NPAs) declining to 1.9% (FY23: 4.1%), while provision coverage ticked slightly higher to 97% (FY23: 95%). On the capitalization front, EXIM India's CET1 and total capital adequacy ratio weakened to 19.6% (FY23: 23.7%) and 21.2% (FY23: 25.4%), albeit still at healthy levels.

Investment view

We view EXIM India's as strategically important to the state, on the back of its key policy role, 100% state ownership, and strong track record of liquidity support by the government during periods of stress. EXIM's founding act mandates strong government oversight and control via its representation on EXIM India's board. Aside from its state backing, EXIM India's credit quality is also underpinned by healthy profitability, improved asset quality, and a robust regulatory capital position. EXIM India is typically viewed as a proxy to the Indian sovereign in the international bond market, allowing it to enjoy better funding rates than its similarly-rated Indian peers. Likewise, we view EXIM India as effectively an effective extension of the Indian government, and investors who want USD exposure to the Indian sovereign (which does not issue USD debt) can consider EXIM India's USD bonds as an equivalent.

Key risks for EXIM India include sharp asset quality deterioration from its commercial loan exposure, a heavy reliance on wholesale funding, and negative developments relating to India's sovereign rating

HPCL-Mittal Energy

UBS credit outlook: Stable
Moody's/S&P ratings: Ba1/NR
Analyst coverage: Devinda Paranathanthri

Company updates

HPCL-Mittal Energy (HMEL) is a leading integrated refining and petrochemical company in India and is a joint venture between Hindustan Petroleum Corporation Ltd (HPCL) and Mittal Energy Investments Pte Ltd (MEI). Given the complexity of the refinery, it has been able to achieve higher gross refining margins (GRMs) than the Singapore benchmark GRM. The multi-year petrochemical expansion was completed in 2023 but will only gradually start to contribute to earnings. Combining potential earnings from the new petrochemical business, HMEL believes it will be able to achieve EBITDA of around USD 800–900mn annually. Fitch expects the company's leverage to improve from 5x in FY24 to around 4.5x in FY25. No major capex is planned going forward, which should limit significant debt additions.

Investment view

Credit metrics should gradually improve as significant capex is now behind us, but we believe this is already factored into its ratings. HMEL does not have major debt repayments until the USD bond maturity in 2026. The company could look to refinance the 2026 bond at least partly over the coming year by either issuing onshore or offshore debt. We are comfortable with the credit profile for HMEL but believe bond yields at low 6% will likely limit further upside.

Key risks include a big correction in GRMs limiting any improvement in its balance sheet over the next year.

Indian Railway Finance Corporation

UBS credit outlook: Stable
Agency ratings: Baa3/BBB-
Analyst coverage: Joel Tan

Company updates

Indian Railway Finance Corporation (IRFC) is the dedicated financing arm of the Ministry of Railways (MoR), with 86.4% ownership by the Indian government. As a non-banking financial company (NBFC), IRFC finances the acquisition of rolling stock assets and railway infrastructure assets, which are then leased to the Ministry of Railways (MoR). In FY24, IRFC posted healthy growth in both interest income (+16.9% y/y) and lease income (+10.2% y/y), driven by higher lease receivables (+6.7% y/y) of INR 2.6tr and a stable net interest margin of 1.38% (FY23: 1.39%). Despite the strong top-line performance, IRFC's net profit only increased by a modest 4% y/y to INR 64.1bn, mainly due to a notable rise in interest expenses (+15.2% y/y) to INR 201bn. On the back of margin compression, its return on assets and return on equity declined to 1.3% (FY23: 1.4%) and 13.7% (FY23: 14.5%), respectively. With regard to asset quality, IRFC continues to record zero non-performing assets, given that almost 99% of its assets are exposed to the MoR, essentially guaranteed by the Indian government. IRFC's gearing (total debt/equity) improved to 8.4x in FY24 (FY23: 9.4x), comfortably below the 10x internal guideline set by management. The NBFC's capitalization profile also strengthened in FY24, with its capital adequacy ratio rising to 616% (FY23: 485%).

Investment view

IRFC's stable credit profile is underpinned by its majority government ownership and strategic policy role, high quality loan book predominantly exposed to MoR, and stable profitability arising from its long-term leases based on a cost-plus model. We believe IRFC's credit risk is inherently tied to the sovereign, on the basis that state support will be forthcoming if needed. Valuation-wise, IRFC's bonds are trading slightly tighter than other Indian NBFCs such as Power Finance and REC, which we think is justified given IRFC's higher government shareholding and lower counterparty risk.

Key risks for IRFC include aggressive expansion in commercial financing which may result in asset quality deterioration, a high reliance on wholesale funding which may be costly during periods of economic stress, and negative developments relating to India's sovereign rating.

NTPC Limited

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Devinda Paranathanthri

Company updates

NTPC is a power generation company, which is 51% owned by the Indian government. It is the largest power generator in India in terms of both installed capacity and generated output. The company generates relatively stable earnings generated based on availability-based tariffs. The current tariff framework assures returns on its regulated asset base with cost pass-throughs. FY24 earnings were rather flat versus FY23. Total debt to EBITDA stood at about 4.6x and we expect it to stay around that level in the medium term due to ongoing capex requirements. According to S&P, the company is likely to spend around INR 250–320bn a year to add around 5GW of capacity. This, along with annual dividends, will limit any improvement in credit metrics, but we expect such fundamental factors to play a secondary role given the government ownership.

Investment view

Given the strategic importance, NTPC is an issuer where we see high likelihood of government support. Its metrics are slightly weak compared to its BBB rated peers, but given the likelihood of support we expect rating agencies to continue to rate the company in line with the sovereign rating.

Key risks include any negative developments relating to India's sovereign rating.

Oil and Natural Gas Corporation (ONGC)

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Devinda Paranathanthri

Company updates

ONGC is an integrated oil & gas producer based in India and majority owned by the Indian government. Its production volumes have been in a modest decline over the past few years, but management expects an improvement in the next two years driven by production ramp-up at one of its deep-water offshore fields. Improving production amid the current oil price environment, as well as positive contributions from the downstream business, will likely contribute to ONGC's earnings in the coming year. ONGC's FY24 revenues fell 6% due to lower oil prices, but EBITDA grew 27%. Total debt to EBITDA likely stood at around 1.4x in FY24, which is quite comfortable for its rating. The acquisition of an additional stake in OPaL will entail some cash outlay in the coming years. The company is expected to spend around INR 184bn to repurchase convertible debentures and to restructure debt and turnaround its operations. This will likely limit a further improvement in credit metrics.

Investment view

We consider ONGC as a strategically important entity for the Indian government as there is a high likelihood of support should there be any need. The acquisition of HPCL back in 2018 further strengthened its strategic importance. Overall, we believe valuations will be driven by India's sovereign fundamentals which we assess to be fairly stable at this point. ONGC's credit metrics are in line with its rating, and we expect credit fundamentals to be fairly stable in the medium term. The company has a bond maturing in July 2024, and we could see a new issue to refinance this.

Key risks include any negative developments relating to India's sovereign rating**.**

Power Finance Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Joel Tan

Company updates

Power Finance Corporation (PFC) is the largest state-owned non-banking financial company (NBFC) in India with the mandate of lending to India's power sector, primarily to government sector borrowers. The company is 56% owned by the Indian government. Over the past few years, PFC has steadily grown its loan book, boosting its interest income and profitability as a result. Asset quality and capital adequacy have also improved progressively since the pandemic. In FY24, PFC posted a strong set of results; interest income rose 17.8% to INR 901bn while net profit increased 24.9% to INR 265bn. Strong top-line growth came on the back of robust loan growth (+15.5% y/y), while net interest margin (NIM) inched higher to 3.46% (FY23: 3.36%). PFC's asset quality also strengthened, with gross non-performing loan (NPL) ratio falling to 3.34% (FY23: 3.91%). PFC's capital position remained solid, as reflected by a capital adequacy ratio of 25.4% (FY23: 24.4%).

In early May, the Reserve Bank of India (RBI) proposed new tighter rules for infrastructure project financing, which may potentially result in NBFCs such as PFC requiring higher provisions and hence reducing capital buffers. If finalized, the RBI's new rules may optically weaken PFC's capitalization metrics, but we do not expect a material impact on its credit profile, especially as higher provisioning may be construed as a credit positive.

Investment view

PFC's healthy credit profile is supported by its solid profitability, improving asset quality, and an ample capital position. Moreover, we view PFC as strategically important to India's power sector and expect a high likelihood of state support if required. Given the close links with the Indian government, we expect any rating changes to be driven by the sovereign rather than at a standalone level. Valuation-wise, PFC's senior bonds are largely trading in line with other comparable state-owned NBFCs, and we do not see any reasons for divergence in the near term. We are comfortable holding PFC's bonds for decent carry in the Indian IG space.

Key risks for PFC include a deterioration in its capitalization metrics in the event that tighter project financing rules are finalized, a heavy reliance on wholesale funding which may be costly during periods of economic stress, and negative developments relating to India's sovereign rating.

REC Ltd

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Devinda Paranathanthri

Company updates

REC Ltd, formerly Rural Electrification Corporation Ltd, is a non-banking financial company (NBFC) that extends financing to various entities within India's power sector. REC is majority owned by state-owned Power Finance Corporation (PFC) and is under the administrative control of the Ministry of Power. REC has enjoyed robust loan growth over the past few years, with interest income and profits showing a healthy uptrend. The NBFC's asset quality and capitalization metrics have also improved steadily since the pandemic. In FY24, REC posted net interest income of INR 464bn (+19.5% y/y), while net profit amounted to INR 141bn (+26.7% y/y). REC's strong financial performance came on the back of healthy loan growth (+17.2% y/y) and an expansion in its NIM to 3.57% (FY23: 3.38%). On the asset quality front, REC's gross NPL ratio improved to 2.71% (FY23: 3.42%) although its provision coverage ratio marginally weakened to 68.45% (FY23: 70.64%). REC's capital buffers remain healthy, with the NFC boasting a capital adequacy ratio of 25.82% (FY23: 25.78%). We highlight that the RBI's proposed new rules for infrastructure project financing may weaken REC's capitalization ratios, but we do not expect REC's credit profile to deteriorate significantly.

Investment view

Similar to its parent PFC, we see REC as strategically important in implementing power sector reform in India. While REC is not directly owned by the Indian government, we expect the NBFC to receive state support via parent PFC when needed. On a standalone basis, REC's credit profile has improved over the past few years, marked by growing profitability, improving asset quality, and solid capitalization. On the rating front, we expect its rating to be closely tied with PFC and the Indian sovereign rating. Valuation-wise, REC's bonds are largely trading in line with bonds issued by parent PFC and marginally wider than other majority state-owned NBFC credits such as Indian Railway Finance. We view REC's bonds as a decent carry play within the Indian IG space.

Key risks for REC include a deterioration in its capitalization metrics in the event that tighter project financing rules are finalized, a heavy reliance on wholesale funding which may be costly during periods of economic stress, and negative developments relating to India's sovereign rating.

Reliance Industries

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB+
Analyst coverage: Devinda Paranathanthri

Company updates

Reliance Industries is a diversified conglomerate in India engaged in oil & gas, telecom, and other digital services. The company reported FY24 revenues of INR 9.1tr (+2% y/y) and EBITDA of INR 1.7tr (+16% y/y). Muted growth in the top line was due weaker oil-to-chemicals revenues, which were offset by other segments which reported healthy growth. Overall, credit metrics remained healthy, with debt to EBITDA at 2.1x and EBITDA coverage at 7.0x. We are also constructive on Reliance's earnings outlook for FY25, with the company set to generate EBITDA growth of 10–15% driven by the telecom and retail businesses.

Investment view

Reliance Industries has invested quite aggressively in the past two years, with annual capex spending of around INR 1.4–1.5tr. Such aggressive spending has essentially absorbed most of its operating cash flows, leaving less room for debt reduction. However, with earnings essentially doubling over the past four years, leverage metrics such as debt to EBITDA remain relatively healthy at 2.1x. We see some scope for an annual capex drop as 5G rollouts and other petrochemical expansion related spending falls. Therefore, there is room for credit metrics to improve from FY25 onwards although we expect this to be modest. Nonetheless, upside for credit spreads are also limited at current tight valuations.

Key risks include further aggressive capex or M&As which could increase balance sheet debt meaningfully in the medium term.

Tata Motors

UBS credit outlook: Improving
Moody's/S&P ratings: Ba3/BB+
Analyst coverage: Devinda Paranathanthri

Company updates

Tata Motors is one of India's largest automobile manufacturers and owns 100% of Jaguar Land Rover (JLR). Overall, earnings have been quite solid, with both Tata Motors and JLR recording strong growth in the past year. FY24 consolidated revenues and EBITDA were up 26% and 70%, respectively. On a standalone basis, JLR's FY24 results continued to be strong, with record revenues of GBP 29bn, up 23% y/y. Both entities have been reducing their net debt positions in the past two years. The Indian domestic business is already in net cash position, and management has previously guided JLR should be net cash by end-FY25. With positive free cash flows, the Indian business should be able to reduce debt further.

In March 2024, the company announced plans to split its commercial vehicle (CV) and passenger vehicle (PV) businesses into two separate listed entities. The two bonds issued by TML Holdings will be under the PV business after the de-merger is completed. The October 2024 bond issued by Tata Motors will likely mature before the exercise is completed. We expect the deleveraging process to continue after the de-merger and the company to achieve an overall net cash position over time. S&P expects total debt to EBITDA to improve to 0.7x in FY25 from 3.0x in FY23, and we believe these metrics will increasingly support a rating upgrade in the next two years.

Investment view

We remain constructive of Tata Motors' fundamental outlook. We believe a rating upgrade is likely by Moody's in the coming year as it rates the company at Ba3, two notches below S&P. With debt levels coming down, the company may not refinance the maturing 2024 bond in the market, and the amount of outstanding bonds could drop in 2024. We see Tata Motors' bonds as a comfortable carry play although upside is limited at current yield levels.

Key risks to our view include a major slowdown in revenues, which will increase leverage and limit further rating upgrades.

Tata Steel

UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Devinda Paranathanthri

Company updates

Tata Steel is one of the largest steel producers in India under the Tata Group of companies. In January, the company announced the shutdown of blast furnaces at its UK Port Talbot plant. This should be a small positive as it will help to cut losses in the Europe business. However, the UK and Europe assets remain a weak link in its portfolio due to their lower profitability. In contrast, the India business remains strong, and we expect a sizable growth in earnings after the Kalinganagar expansion starts to contribute upon completion. Tata Steel's consolidated EBITDA for FY24 was down 29% at INR2 34bn from the high base in FY23 due to weaker contributions from the overseas businesses. India business EBITDA was still up 10% y/y at INR 310bn. During the fourth quarter, per ton losses from the UK and Europe businesses narrowed meaningfully. Due to lower EBITDA, net debt to EBITDA increased to 3.3x in FY24 from 2.1x in FY23.

Investment view

We believe Tata Steel's credit metrics are relatively healthy despite a modest weakening since 2022. The overall earnings outlook for the India business remains constructive as we see robust domestic steel demand given the Indian government's focus on infrastructure spending. The Kalinganagar expansion is likely to be completed in FY25. With the company's expansion starting to contribute to earnings, leverage should improve to below 3x by end-2025. Due to cost considerations, we believe Tata Steel will increasingly look at the onshore market for debt funding, but we will not rule out issuance in the USD market if rates move lower. We are comfortable owning the 2028 bond.

Key risks include further capex at the expense of its balance sheet and deterioration in profitability in the Europe operations.

Vedanta Resources

UBS credit outlook: Stable
Moody's/S&P ratings: Caa3/B-
Analyst coverage: Devinda Paranathanthri

Company updates

Vedanta Resources is a diversified resources company with assets mainly located in India. With the maturity extension out of the way, the focus of bondholders will likely shift to the company's asset sales plans and its operating performance. On asset sales, Vedanta Resources is looking to sell its iron ore and steel businesses in the coming year. This will be the next key catalyst to watch for the bonds, with the focus on how much debt can be reduced with the proceeds. While the extension of the USD bonds has improved Vedanta Resources' bond maturity schedule materially, the company still has a sizable amount of loans maturing annually. We believe the upcoming maturities can be refinanced in the loan market although any delays to the asset sale plans need to be closely watched.

With the coupon rate of three of Vedanta Resources' bonds increased to 13.875% and the new USD 1.25bn funding raised for bond repayment reported at a cost of 18%, Vedanta Resources' total interest expense will be around USD 800mn annually. This would need to be funded by inflows from dividends and brand fees. Based on the prevailing commodity prices, we believe the company will be able to upstream sufficient funds to cover interest payments. Vedanta Ltd has approved plans to raise USD 1bn of equity after the meaningful rally in its share price. The share price rally also increases the possibility of the company again monetizing a part of its stake in Vedanta Ltd. Based on the current market value, Vedanta holdco could raise around USD 1bn by selling a 5% stake; this could lead to a meaningful debt reduction.

Vedanta Ltd's FY24 results were stable, with EBITDA up 3% driven by better oil & gas, and aluminum and iron ore earnings, despite being offset by its weaker zinc business. Vedanta Resources' key commodity prices have risen by around 10% this calendar year, and we think prices will remain well-supported for the remainder of the year, boosting earnings visibility for FY25.

Investment view

Our view that commodity prices will remain resilient for the next six months will likely give the company more financial flexibility, allowing it to upstream enough dividends to service its debt. Additionally, the recent rally in India-listed Vedanta Ltd's share price also increases fundraising options as it now gets more bang for the buck should it decide to monetize more of this stake. The outcome of the asset sale plan will still be closely watched, and based on management guidance it will likely be delayed until 3Q24. On balance, we see more positive catalysts for Vedanta Resources in the next six months, leaving us more constructive on the 2026 bond as a short-term tactical play. However, we do not believe the bond is ideal for hold-to-maturity type investors. The company is yet to have access to the USD bond market and if management fails to reduce debt in the next 12 months, the maturity wall from 2026 onwards can be challenging.

Key risks to our view include a commodity price correction, the company abandoning its asset sale plan, and any aggressive M&A.

Figure 25 - Indonesian issuers covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior			
			0-2y	2-5y	5-10y	>10y
PT Cikarang Listrindo	Stable	Ba1/BB+				
PT Indofood CBP	Improving	Baa3/NR				
Lippo Karawaci	Deteriorating	Caa1/NR				
Lippo Malls Indonesia Trust	Deteriorating	Ca/NR				
Medco Energi	Stable	B1/BB				
Pakuwon Jati	Stable	Ba1/BB+				
Pertamina	Stable	Baa2/BBB				
PLN	Stable	Baa2/BBB				
PT Freeport Indonesia	Improving	Baa3/NR				
PT Mineral Industri Indonesia / Indonesia Asahan Aluminium	Stable	Baa2/NR				
Paiton Energi	Stable	Baa3/BBB				
Tower Bersama Infrastructure	Stable	NR/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 10 - Key financial & credit metrics (FY2023)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total debt/ capital
PT Cikarang Listrindo	0.5	31.0%	199.0	0.4x	6.8x	41.5%
PT Indofood CBP	4.4	23.7%	2.9	1.5x	7.9x	41.5%
Lippo Karawaci	1.1	0.3	1.3	4.3x	5.0x	50.8%
Lippo Malls Indonesia Trust	0.1	54.5%	801.5	8.5x	1.5x	71.0%
Medco Energi	2.2	55.8%	3.5	2.5x	4.5x	63.5%
Pakuwon Jati	0.4	53.7%	0.4	net cash	9.1x	21.5%
Pertamina	75.7	18.0%	22.3	0.2x	9.3x	35.0%
PLN	22.3	27.0%	25.3	3.6x	4.6x	28.0%
PT Freeport Indonesia	8.4	67.0%	3.2	0.3x	26.2x	17.2%
PT Mineral Industri Indonesia / Indonesia Asahan Aluminium	7.0	12.3%	6.0	4.1x	2.2x	41.6%
Paiton Energi	0.9	55.3%	2.1	4.0x	3.7x	59.7%
Tower Bersama Infrastructure	0.4	86.3%	1.9	5.1x	3.1x	70.8%

Source: Company reports, UBS

PT Cikarang Listrindo

UBS credit outlook: Stable
Moody's/S&P ratings: Ba1/BB+
Analyst coverage: Devinda Paranathanthri

Company updates

Cikarang Listrindo (CL) is an Indonesia-based independent power producer (IPP). It has a total 1.1GW of generation capacity, including two gas fired plants (864MW) and one coal-fired plant (280MW). About 15% of its revenues are from the state electricity company Perusahaan Listrik Negara (PLN) under a long-term power purchase contract. The remaining 85% is from power sold to industrial customers in various sectors. Given the nature of the business, CL's earnings have been relatively stable in the past three years, with EBITDA around the USD 180–200mn range. Its debt structure is relatively simple, with just a USD 500mn bond maturing in 2026. As a result, debt to EBITDA was around 2.7x for 2023 and is relatively healthy for its rating. Cikarang has been generating free cash flows in the past few years and used that to build its cash balance to around USD 428mn as of 1Q24. As a result, the net debt position is very low at USD 62mn.

Investment view

We consider CL to be a relatively stable credit with simple debt structure and lower leverage than other IPP players. The company needs to look at refinancing the 2026 bond soon, but we do not believe it will be a big challenge. CL had around USD 428mn in cash as of March 2024, which it can use to refinance a significant portion of the bond. However, given the sizable coal power generation capacity, CL will have to pay some ESG premium should it decide to return to the USD market. There is limited upside to the current BB+ rating given the size of the generation capacity, in our view. We consider the bonds to be a fairly stable short-term carry play.

Key risks to our view include any operational issues with its power plants which result in lower availability.

PT Indofood CBP Sukses Makmur

UBS credit outlook: Improving
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Joel Tan

Company updates

PT Indofood CBP Sukses Makmur Tbk (ICBP) is the largest packed good company in Indonesia by retail value share, with over 70% domestic market share in the instant noodle category. ICBP is 80.5% owned by PT Indofood Sukses Makmur Tbk (INDF), which is ultimately controlled by the Salim family. Since the Pinehill acquisition in 2020, ICBP has experienced steady earnings growth and healthy free cash flow, allowing the company to steadily deleverage over the past few years. ICBP posted solid FY23 results, with revenue of IDR 67.9bn (+4.8% y/y) and EBITDA of IDR 16.1bn (+6.6% y/y). As for its bottom line, net income rose 47.9% y/y to IDR 8.5bn although this came off a low base given the sizable FX loss incurred in FY22. ICBP's free cash flow remained robust at IDR 5.3bn (+38.1% y/y), resulting in a 22.9% increase in its cash balance to IDR 19.4bn and a 18.6% y/y decline in net debt to IDR 24.6bn. ICBP's credit metrics strengthened in FY23, with net leverage at 1.5x (FY22: 2x) and interest coverage at 7.9x (FY22: 2.4x). Gearing (total debt/capital) also declined to 41.5% from 44.5% in FY22. In 1QFY24, ICBP maintained healthy revenue growth (+4.8% y/y) although earnings were dragged down (-37.1% y/y) by a non-cash foreign exchange loss on the back of IDR depreciation (against USD). Nonetheless, ICBP's credit metrics remained healthy in 1QFY24, with annualized net leverage improving to 1.1x and gearing staying broadly stable at 41.1%.

Investment view
ICBP's strong credit quality is underpinned by its leading market position and strong brand recognition in the Indonesian consumer food market. The company boasts sound credit metrics with a sizable cash balance and low net leverage, and we expect deleveraging to continue in the short to medium term on the back of robust cash generation. Both Moody's and Fitch currently have positive outlooks on ICBP, and we would not be surprised if a rating upgrade materializes in the next 6–12 months. Valuation-wise, ICBP's bonds are trading slightly inside similarly-rated quasi-sovereign Indonesian IG credits, which we think reflects ICBP's stronger standalone credit metrics and the likelihood of an imminent rating upgrade. As privately-owned IG issuers in Indonesia are rare, ICBP's bonds benefit from an element of scarcity value, which should keep bond prices well supported, in our view.

Key risks for ICBP are a spike in raw material prices that pressures margins, a sharp depreciation in the IDR that entails higher borrowing costs (as borrowings are predominantly in USD), and unfavorable related-party transactions within the Indofood Group.

Lippo Karawaci
UBS credit outlook: Deteriorating
Moody's/S&P ratings: Caa1/NR
Analyst coverage: Devinda Paranathanthri

Company updates
Lippo Karawaci (LK) is an Indonesia-based property developer. The company announced in May 2024 that it had signed an agreement to sell a 10.4% stake in Siloam Hospital for USD 240mn. After the stake sale, LK's ownership in Siloam will drop to 47.7% from 58.1% currently. While total EBITDA will drop materially (Siloam accounted for 53% of LK's EBITDA in 2023) after deconsolidation, it will bring some much-needed liquidity to the holding company to refinance the upcoming debt. Therefore, while credit metrics will deteriorate after the transaction, we do not see it as a material negative particularly if it paves the way to monetize further stakes. That said, even before the transaction, LK's metrics were not particularly strong (1Q24 debt to EBITDA was 4.4x) although they have improved in the past two years. 1Q24 marketing sales were IDR 1.5tr, or around 28% of the full-year sales target of IDR 5.4tr. Given the decent pre-sales performance in the past year, we believe the company will be able to meet the full-year sales target.

Investment view
The focus over the next year for bond investors will be how the company refinances its remaining 2025 (USD 66mn) and 2026 bonds (USD 145mn). To that end, the Siloam stake sale is positive, in our view. That also values the remaining stake in Siloam at around USD 1.1bn, opening a new avenue for management to raise funds for the holding company. We believe the risk of default or restructuring has come down materially for the 2025 and 2026 bonds but the higher bond prices largely reflect this. We see little risk-reward to hold the bonds at current levels.

Key risks to our view include the company not being able to refinance the remaining USD bonds.

Lippo Malls Indonesia Retail Trust
UBS credit outlook: Deteriorating
Moody's/S&P ratings: Ca/NR
Analyst coverage: Devinda Paranathanthri

Company updates
Lippo Malls Indonesia Retail Trust (LMIRT) is an Indonesia-focused retail REIT listed in Singapore. LMIRT's 1Q24 results were flat year over year, with gross revenues of SGD 49mn. The occupancy rate for the quarter was at 79.5%, a modest improvement from the 79% achieved for full-year 2023 and well below the 2019 level of 91.5%. In comparison, assets of other industry players, such as Pakuwon and Ciputra, are showing occupancy rates of over 90%. The lower occupancy for LMIRT appears to be a company-specific issue with its mall portfolio. Additionally, based on LMIRT's data, 1Q24 shopper traffic was only 75% of what it was in 1Q19. Total debt dropped by around SGD 82mn in 1Q24 to SGD 731mn, but net leverage (excluding the perpetuals) remained high at 6.4x.

Investment view
With the bond exchange, a portion of the 2024 maturities will be pushed back by two years, but this will not improve the maturity profile very much, in our view. We believe the market will start to worry within a year about the maturity pile in 2026. Additionally, along with the incremental secured debt raised from banks in the past six months, these bonds are getting structurally subordinated in the capital structure. The company announced recently that its IDR 2.5tr credit facility it secured in May 2024 was upsized to IDR 4.5tr. LMIRT has launched a tender offer for the remaining USD 149mn outstanding 2026 bond. We believe investors should tender any holdings at the current market price.

A key risk to our negative view is if the company buys back all remaining bonds at par.

Medco Energi
UBS credit outlook: Stable
Moody's/S&P ratings: B1/BB-
Analyst coverage: Devinda Paranathanthri

Company updates
Medco Energi is an upstream oil & gas company based in Indonesia. Close to 70% of the company's production

estimate for 2024 will be from gas of which over 65% is sold under fixed price contracts. As a result, Medco's earnings are less sensitive to oil price movements. Cash costs for 1Q24 were around USD 6.3/boe and the company estimates this will remain below USD 10/boe going forward. Medco's 2023 earnings were impacted by lower realized oil prices, with EBITDA declining 21% y/y. However, credit metrics remained relatively strong with gross leverage at 2.8x in 2023. Going forward, Medco is guiding for production to remain rather flat at 145-150 mboepd. Given our expectation that oil prices will stay resilient for the remainder of 2024, we believe the company will be able to record full-year EBITDA of close to USD 1.2bn, with total debt to EBITDA staying just below 3.0x for 2024. Capex and potential M&As will likely be key areas of focus for credit investors. Medco has guided full-year capex of USD 430mn for 2024, notably higher than the USD 300mn in 2023. However, this should not lead to any additional debt as the company should be able to fund it internally given our EBITDA estimate above. Medco has also engaged in sizable but EBITDA accretive acquisitions in the past five years. We believe these purchases have so far helped to expand its operational profile without putting stress on the balance sheet. Given that the company has adequate access to funding from banks as well as the bond market, we cannot rule out more of such acquisitions going forward. However, judging by management's past track record, we do not believe they will be at the expense of its ratings.

Investment view
We consider Medco to be one of the more stable credits in the Indonesia HY space. While earnings are likely to be somewhat volatile due to oil prices, we believe the overall credit profile is strong enough to manage this. Fitch & S&P has upgraded the rating to BB-, in line with our view. The company did a partial tender offer for the 2026 and 2027 bonds, and we believe such corporate actions could continue as and when the company builds liquidity. Given the medium-term rating upgrade trajectory, our preference is for the 2028 and 2029 bonds.

Key risks include aggressive debt-funded acquisitions.

Pakuwon Jati

UBS credit outlook: Stable
Moody's/S&P ratings: Ba1/BB+
Analyst coverage: Devinda Paranathanthri

Company updates
Pakuwon Jati is a property developer and one of the largest retail mall owners in Indonesia. Earlier this year, its ratings were upgraded to Ba1 by Moody's, and it now has BB + equivalent ratings from all three major rating agencies. Recurring revenues from its mall portfolio contributed to 78% of total revenues in 1Q24, making the earnings profile resilient to volatility in residential sales. Based on the 1Q24 EBITDA of IDR 833bn (up 8% y/y), annualized debt to EBITDA stood at 1.9x. Its debt profile is also quite simple, with just a USD 400mn 2028 bond in its balance sheet. Cash and cash equivalents as of 1Q24 stood at IDR 8.2tr, resulting in a net cash position. We expect Pakuwon to continue to generate positive cash flows in the next year, which will help to increase its cash position further.

Investment view
Among the Indonesian property developers with USD bonds, we consider Pakuwon to be the strongest credit. It has a strong balance sheet with a net cash position. If the company doesn't see many investment opportunities for its hefty cash balance, it could consider purchasing its bonds early using a tender offer. Valuations now reflect the strong BB rating, and we see its bond as a steady carry play.

Key risks include a material acquisition that could bring down its hefty cash position.

Pertamina

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Devinda Paranathanthri

Company updates
Pertamina is a fully government-owned entity, which engages in a broad range of upstream and downstream oil and gas operations in Indonesia. The company's downstream earnings have been impacted as it has not been able to adjust pump prices to reflect prevailing prices for oil because pump prices are controlled by the government. The 30% hike for subsidized fuel prices in September 2022 alleviated some pressure on this front, but not enough to compensate the company for higher costs. The government's compensation for these losses has improved in the past 18 months. According to S&P, the company has received close to USD 21bn over this period, versus receipts of just USD 1.7bn in 2021 and USD 2.7bn in 2020. Meanwhile, upstream earnings will likely be supported by prevailing oil prices and are likely to account for a significant part of group earnings. Credit metrics are quite strong with leverage at 1.8x for 2023, having improved since the government increased the frequency of the subsidy calculation. Annual capex requirements (USD 5–6bn) can be funded by its healthy cash balance of USD 20bn as of end-2023.

Investment view
We consider Pertamina to be a strategically important entity for the Indonesian government, and as a result support is very likely if needed. Its credit metrics are some of the strongest among the Indonesian SOEs and have improved after the government restructured the subsidy payment mechanism. Pertamina bonds are largely a pickup opportunity over the Indonesian government, but the

premium is at historically low levels. Due to a high cash balance of USD 20bn, we believe issuance in the near term will be limited to refinancing.

Key risks include any negative developments relating to the Indonesia sovereign rating.

PLN

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Devinda Paranathanthri

Company updates

PT Perusahaan Listrik Negara (PLN) is a fully state-owned vertically integrated utility company in Indonesia mandated by the government to provide electricity. The company is the sole operator and distributor of Indonesia's electricity transmission and distribution while also owning the majority of the country's energy generation capacity. The government decided not to increase electricity tariff for 2Q24, and we expect the same for the rest of the year. The quarterly compensation mechanism for subsidy payments enacted in 2022 has helped to reduce its overall debt. However, power capacity needs for the country will likely keep annual capex high at around USD 5–7bn in the coming years and this will keep free cash flows in negative territory, limiting any meaningful improvement in credit metrics. Debt to EBITDA stood at 4.0x in 2023, which is relatively high for its ratings.

Investment view

We view PLN as a strategically important entity for the Indonesian government as it plays a critical role supporting the country's power needs. The company is also entrusted by the government to carry out its green transition plans. Therefore, we consider it as an entity with a high likelihood of government support, and its relatively weak standalone credit profile is likely to be a less important driver in bond valuations. Given the capex needs, we think PLN will increase its total USD bonds outstanding over the next five years. This may not be a factor for valuations in the current year as technicals in the Asia credit markets are relatively strong. However, this, along with its weaker fundamentals, could be a reason for its bonds to trade at a modest premium to other SOEs such as Pertamina in the medium term.

Key risks include delays in government subsidy payments as that could put pressure on cash flows.

PT Freeport Indonesia

UBS credit outlook: Improving
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Devinda Paranathanthri

Company updates

Freeport Indonesia (PTFI) is an Indonesian mineral mining company with exclusive rights to the exploration and mining operations of the Grasberg Minerals District (Grasberg) in Indonesia. The company mines and processes ores and concentrates containing copper, gold, and silver. The company is 51%-owned by PT Mineral Industri Indonesia (MIND ID), which is fully state owned, and 49%-owned by Freeport McMoran Inc. (FCX). On the back of resilient commodity prices, PTFI has posted strong earnings in the past year. Its 1Q24 results were even stronger, with EBITDA up 93% y/y on the back of higher commodity prices. Based on its FY23 EBITDA of USD 5.6bn, total debt to EBITDA stood 0.6x. The company's strong credit metrics should provide enough buffer for future commodity price volatility, in our view. We are relatively bullish on our commodity price forecasts for gold and copper, and hence expect 2024 to be another strong year for the company. Smelter capex should be largely completed in 2024 and that should improve free cash flows for PTFI going forward. Additionally, the 3mtpa of smelter capacity should be sufficient to process its copper concentrate and this should allow PTFI to save the amount spent on tariffs for copper concentrate exports from next year onwards.

Investment view

PTFI has a solid credit profile underpinned by its low leverage owing to prevailing commodity prices. We believe 2024 will be another strong year for the company on the earnings front. We expect PTFI to start paying higher dividends from next year as free cash flows are likely to increase once its capex program comes to an end. We also see the possibility of early tenders to further deleverage should the company take a more balanced approach to managing its balance sheet.

Key risks include a significant correction in gold and copper prices.

PT Mineral Industri Indonesia (MIND ID) / PT Indonesia Asahan Aluminium (Inalum)

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/NR
Analyst coverage: Devinda Paranathanthri

Company updates

PT Mineral Industri Indonesia (MIND ID) was established in 2023 to replace Indonesia Asahan Aluminum (Inalum) and is the new holding company for the state's mining assets. The entity is fully owned by the government. Media reports last year had suggested MIND ID might do an IPO in 2024 but this could take time to materialize as some of these plans may need the support of the new government. As a holding company, its cash flows for debt servicing primarily come from dividends from its wholly-owned subsidiaries Antam (nickel, gold, silver), Bukit Asam (coal), and Freeport Indonesia (copper, gold, silver). Its overall dividend base has increased from 2021 onwards after PTFI started paying meaningful dividends. Total dividend inflows for the full year 2023 were around USD 1bn and they comfortably cover the company's annual interest expense of around USD 360mn. Under our commodity price assumptions, we expect annual dividends for 2024 to be close to USD 1bn.

Investment view
We consider MIND ID to be a strategically important entity to the government, with likely support from the state in times of need. Its key subsidiaries control a significant portion of the country's reserves, while also playing a role in the government's plans to develop downstream processing capacity. MIND ID also has diversified exposure to several key commodities and its competitive cost profile should help to keep the operations profitable. The holding company structure with dividends to service its debt is a weakness, but we currently see sufficient dividend inflows in the medium term to effectively service its debt. Potential M&As will remain a risk as we believe the company is looking to expand its portfolio. However, we do not see such moves leading to any negative rating actions. MIND ID's bonds offer a premium over other SOEs such as Pertamina.

Key risks include a significant correction in commodity prices and potential debt-funded M&As.

Paiton Energi
UBS credit outlook: Stable
Moody's/S&P ratings: Baa3/BBB-
Analyst coverage: Devinda Paranathanthri

Company updates
Paiton Energi is an independent power producer (IPP) in Indonesia which operates three coal-fired power plants with a total capacity of 2,045MW. The company's business model offers fairly stable and predictable cash flows given its power purchase agreement (PPA) with PLN where input costs can be fully passed through. However, earnings were hit in 2021 and 2022 due to unexpected operational problems which led to plant shutdowns. The company has now fixed some of these issues and EBITDA has recovered to an annual run rate of close to USD 500mn, translating to debt to EBITDA of 4.2x. One key overhang for the credit has been the announced shareholder change where Mitsui & Co divested its 45% stake to Ratch Group (36%) and Medco Energi (9%). This makes Medco Daya Energi the largest shareholder with a 38% stake, while Ratch Group and Nebras Power will hold 36% and 26%, respectively. This ownership transfer was completed in May 2024, but did not trigger a change of control in the bonds.

Investment view
Paiton's 2030 bond started amortizing in February 2024 with USD 84mn semi-annual payments. The company's internal cash flows should be sufficient to make these payments but this will likely mean that dividend payments to the shareholders need to be curtailed. Based on the bond documents, Paiton can obtain additional debt only if the debt service coverage ratio is above 1.4x. Following the commencement of amortization, this ratio is closer to 1.5x which should protect bondholders from debt-funded dividends, in our view. That said, the new shareholders could look to make some changes to the financial policies in the coming year. As a coal-fired power plant operator, Paiton bonds will continue to carry some ESG premium versus its BBB rated peers. We believe the amortizing structure will help with the ultimate refinancing burden for the company.

Key risks include any operational issues with the plant that could lead to unscheduled shutdowns.

Tower Bersama Infrastructure
UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Joel Tan

Company updates
As the third largest tower operator in Indonesia, Tower Bersama Infrastructure (TBI) builds, owns, and operates telecommunication towers for mobile operators. Given the oligopolistic nature and high entry barriers of the tower industry, TBI benefits from a stable business profile, as reflected in consistent revenue and earnings over the past few years. Additionally, long-term lease agreements with telco clients entail high earnings and cash flow visibility for the company. In FY23, TBI posted stable revenue of IDR 6.6tr (+1.8% y/y) and EBITDA of IDR 5.7tr (+1.2% y/y). The company continued to grow its tower portfolio, with 605 net tower additions in FY23, bringing its total tower count to 22,475. TBI's tenancy ratio (number of tenants per tower) remained healthy at 1.84x in FY23 (FY 22: 1.87x). As for its bottom line, TBI's net income was marginally lower (-4% y/y) at IDR 1.6tr although free cash flow improved to IDR 283bn (FY22: IDR 63bn). TBI's credit metrics were largely unchanged in FY23, with net leverage at 5.1x (FY22: 5.1x) and interest coverage at 3.1x (FY22: 3.1x). Gearing (net debt/capital) strengthened to 63.9% in FY23, from 68.7% in FY22. TBI's stable financial performance continued into 1Q24, with revenue higher by 5.4% y/y at IDR 1.7tr, EBITDA up 5% y/y at IDR 1.5tr, and net income rising 4.5% y/y to IDR 363bn. The company's credit metrics, on an annualized basis, also held steady during the quarter, with net leverage at 5.1x and interest coverage at 3x.

Investment view
Tower Bersama's credit metrics are on the weak side for an investment grade (IG) credit (rated BBB- by Fitch), with the company's leverage being elevated compared to other IG names. Nonetheless, the company's stable business model and high cash flow visibility allow for a higher leverage threshold, and we expect TBI to maintain its IG rating by Fitch in the near to medium term. TBI's bonds are trading slightly wider than other Indonesian IG credits, which can be attributed to its weaker credit metrics and a lack of state connection unlike many other Indonesian IG names. We view TBI's bonds, which are generally short-dated, as decent carry play for a stable IG credit.

Key risks for TBI include further consolidation of Indonesia's telco industry, which may lead to a reduction in tower contract renewals, and potential debt-funded acquisitions, which will put pressure on its credit metrics.

Figure 26 - South Korean issuers covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
Export-Import Bank of Korea	Stable	Aa2/AA				
Hanwha TotalEnergies Petrochemical	Stable	Baa1/BBB				
Hyundai Capital America	Stable	A3/BBB+				
Hyundai Capital Services	Stable	A3/BBB+				
Korea Development Bank	Stable	Aa2/AA				
Korea Electric Power Corporation	Stable	Aa2/AA				
Korea Gas Corporation	Stable	Aa2/AA				
Korea Hydro & Nuclear Power	Stable	Aa2/AA				
Korea Mine Rehabilitation and Mineral Resources	Stable	A1/A+				
Korea National Oil Corporation	Stable	Aa2/AA				
LG Chem	Stable	A3/BBB+				
Mirae Asset Securities	Stable	Baa2/BBB				
POSCO	Stable	Baa1/A-				
SK Battery America Inc.	Deteriorating	Baa3/NR				
SK hynix Inc.	Stable	Baa2/BBB-				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 11 - Key financial & credit metrics (FY2023)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total debt/ capital
Hanwha TotalEnergies Petrochemical	9.0	4.1%	1.9	4.9x	5.8x	39.6%
Korea Electric Power Corporation	69.0	9.6%	104.9	15.3x	1.6x	78.3%
Korea Gas Corporation	34.9	7.7%	30.5	11.1x	2.1x	79.9%
Korea Hydro & Nuclear Power	8.6	47.7%	10.8	2.4x	5.8x	35.6%
Korea Mine Rehabilitation and Mineral Resources	0.8	-3.9%	4.3	-115.0x	-0.2x	180.0%
Korea National Oil Corporation	2.6	44.9%	11.8	9.9x	3.2x	109.8%
LG Chem	43.2	10.5%	17.2	2.2x	6.4x	34.9%
POSCO	60.4	9.5%	20.3	2.6x	1.7x	30.3%
SK Battery America Inc.*	60.5	5.1%	22.7	4.0x	3.4x	49.1%
SK hynix Inc.	25.6	16.9%	23.1	3.9x	3.5x	35.5%

*Financial information based on SK Innovation (guarantor of 2026 bond)
Source: Company reports, UBS

Export-Import Bank of Korea

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Timothy Tay

Company updates

The Export-Import Bank of Korea (KEXIM) is a wholly state-owned policy bank in Korea with a mandate of promoting the international business of South Korean companies. As South Korea's official export credit agency, KEXIM provides loans to eligible entities related to exports, imports, and overseas investments and also acts as a guarantor for eligible loans. The policy bank is 73% directly owned by the Korean government, with 27% indirect ownership via the Bank of Korea (7.9%) and the Korea Development Bank (19.1%). In FY23, KEXIM's net interest income fell 5.3% to KRW 935bn, but this was more than offset by a 29.8% increase in net commission income to KRW 434bn. At the bottom line, net profit jumped by 89.4% to KRW 787bn, boosted by a significant decline in credit impairment loss to KRW 284bn (FY22: KRW 683bn). The policy bank's total loan and guarantees remained stable (+0.5% y/y) at KRW 126.6tr, while its total debt was also fairly steady at KRW 99.8tr (+0.9% y/y). During the year, KEXIM's asset quality improved as its gross non-performing loan (NPL) ratio declined to 0.5% as of 3Q23 (FY22: 1.1%) while its provision coverage ratio strengthened to 386% (FY22: 208%). KEXIM's capitalization remains robust, with its total capital adequacy ratio rising to 14.6% in FY23, from 13.5% in FY22.

Investment view

Our Stable credit outlook on KEXIM is underpinned by its 100% government ownership, its important policy role for South Korea, and the government's de-facto solvency guarantee arising from its statutory obligation under the KEXIM Act. KEXIM's intricate government linkage and near-certain likelihood of extraordinary support have led rating agencies to equalize KEXIM's ratings with that of the South Korean sovereign. KEXIM's credit fundamentals are sound, in our view, supported by healthy profitability, improving asset quality, and robust capitalization metrics. While the policy bank is entirely reliant on wholesale funding, its government-related entity status allows for easy access to capital markets, in our view. Valuation-wise, KEXIM's USD bonds are trading slightly wider than South Korean sovereign paper, and in line with bonds issued by other state-owned policy banks. We see KEXIM's longer-dated bonds as a high-quality duration play for investors who want to extend duration with minimal credit risk.

Key risks for KEXIM include concentrated exposure to certain volatile sectors such as overseas plants and vessel manufacturing projects, its full reliance on wholesale funding which increases refinancing risks, and any negative developments relating to South Korea's sovereign rating.

Hanwha TotalEnergies Petrochemical (HTP)

UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/BBB
Analyst coverage: Daniel Tam

Company updates

HTP is a 50:50 joint venture between South Korea's Hanwha Group and France's TotalEnergies SE (A1/Stable, A+/Stable). HTP is a leading petrochemical manufacturer in South Korea with a diversified product portfolio, partly offset by its exposure to volatile petrochemical market conditions. HTP reported a mixed set of 2023 results with revenue and EBITDA declining 18% and 32.8%, respectively. The lower profitability and higher interest costs led to a net loss of KRW 80bn in 2023, compared to a net profit of KRW 69bn in 2022. The weaker earnings increased total debt/EBITDA to 5.2x (2022: 3.7x), but net debt declined 8.4% and lowered net debt/total capital to 47.5% (2022: 49.9%). The company maintained positive operating and free cash flows of KRW 890bn and KRW 380bn, respectively, in 2023, up from KRW 400bn and KRW 181bn in 2022.

Investment view
HTP's EBITDA margin weakened to low single digits in 2022 and 2023, owing to capacity additions in China and subdued chemical demand globally. S&P has revised the company's rating outlook to negative from stable on expectations that lower profitability could result in elevated leverage metrics. However, the rating agency has also affirmed HTP's BBB rating on expectations that the company's operating performance should gradually improve. The rating agency expects China to slow down capacity expansion and restocking needs amid rising oil prices, which should stabilize demand for chemical products. HTP's liquidity should remain strong as capital expenditure will likely be low in 2024 and 2025 and major shareholders should allow HPT to reduce dividend payments in 2024. In view of the company's prudent financial track record of maintaining positive operating and free cash flows, we believe the company's debt repayment ability will remain strong. TotalEnergies SE is expected to provide strong financial and operational support to HTP, if necessary, because of HTP's important role in TE's Asian business.

Key risks include China resuming capacity expansion and a weaker-than-expected global economy that results in reduced demand for petrochemical products.

Hyundai Capital America Inc
UBS credit outlook: Stable
Moody's/S&P ratings: A3/BBB+
Analyst coverage: Eve Li

Company updates
Hyundai Capital America (HCA) is the captive finance arm that supports the sales of Hyundai and Kia vehicles in the US. Founded in 1989, it is wholly owned by Hyundai Motor Group (HMG) via Hyundai Motor Company (HMC) and Kia Corp, which have indirect ownership of 80% and 20%, respectively. HCA offers retail automobile loans, operating leases, and wholesale loans to dealers.

In 1Q24, HCA's earning assets grew 4% q/q to USD 61bn. HCA's earning assets can be divided into consumer loans (65%), operating leases (28%), and dealer loans (7%). The consumer loan portfolio maintained sound quality, with the weighting of subprime loans continuing to trend down to 1.7% (versus 1.8% in 2023 and 4.1% in 2019) and the net charge-offs ratio below 1%. The delinquency ratio (30 days overdue) also improved to 2.3%, from 2.6% in 2023. Its operating lease portfolio also saw an improvement in asset quality thanks to high-quality originations. While operating lease exposure was higher at USD 17.3bn as of end-March 2024 (up 5% y/y) and used car prices have been moderating, the company expects residual gains due to its favorable portfolio mix and manageable lease maturities in the near term. HCA's leverage, measured by debt/equity, was higher at 8.9x as at end-1Q24, compared to 8.7x as at end-2023. The company maintained diversified funding sources, including bonds (49%), ABS (24%), and conduit (15%), as well as affiliate borrowings (7%). 62% of its USD 55bn debt was unsecured.

HCA has enjoyed a support agreement with HMC since 2012, under which HMC shall 1) hold 100% direct or indirect ownership in HCA; 2) ensure HCA has a positive consolidated tangible net worth; and 3) support HCA in maintaining a fixed-charge coverage ratio of no less than 1.1x via cash contributions, if needed. Given HMC's strong support and HCA's role as a core subsidiary, the rating of HCA is equalized to that of HMC. In January, S&P revised the outlook on HMC and Kia Corp to positive from stable on robust earnings outlook and improving credit metrics in 2024–2025. HMG has been gaining market share over the past few years in the US, with a combined market share of 10% for HMC-Kia in 1Q24 (versus 10.6% in 2023 and 7.8% in 2019). The group became the fourth-largest auto OEM in the US in 2023. The rating agency also views HMC and Kia's liquidity as exceptional. The outlook for HCA was also revised to positive to mirror the actions on the group. In February, Moody's upgraded HMC and Kia to A3 from Baa1, reflecting their improving profitability and balance sheet. Moody's also upgraded HCA to A3, following the action on parent ratings.

Investment view
We maintain Attractive recommendations on select bonds in the HCA curve as they look attractive compared to bonds of other captive arms of global automakers. HMC and HCA's positive rating trajectory should continue to support the bonds' performance, but we will also monitor the development of the US auto market and HMG's performance.

Key risks to our view include HMC achieving worse-than-expected profitability and a significant deterioration in HMC's balance sheet that leads to a rating downgrade.

Hyundai Capital Services, Inc.

UBS credit outlook: Stable
Agency ratings: A3/BBB+
Analyst coverage: Eve Li

Company updates

Hyundai Capital Services (HCS) is the captive finance arm of Hyundai Motor Group (HMG). It provides automotive financing and leasing for new and used vehicles sold by HMG's Hyundai Motor Company (HMC) and Kia Corporation (Kia) in South Korea. It also provides consumer loans such as mortgage loans and other personal loans to individuals and small business owners. HMG owns 99.8% of HCS through HMC (59.7%) and Kia (40.1%).

In the first nine months of 2023, HMG's global car units sold increased 8% y/y to 5.5mn units. Growth was observed across different regions, led by North Americas (+18%), South Korea (+11%), and Europe (+11%). With a more favorable product mix, both HMC and Kia also enjoyed a higher average sales price (ASP) and higher operating margin. The group's sales growth as well as stronger leasing demand for higher ASP models also benefited HCS. In the first nine months of 2023, HCS's financial assets were up 2% at KRW 33.8tr, of which 82% was auto-related. Operating revenue grew 35% y/y to KRW 3.3bn, driven by lease revenues. Its asset quality remained solid, with the 30-day delinquency ratio continuing to trend lower to 0.93%, compared to 1.04% in 2022. Its regulatory reserve coverage also improved to 131%, well above the regulatory threshold of 100%. Asset leverage was also better at 7.2x (from 7.4x).

HCS' role as a core subsidiary of HMG is reinforced by its overseas footprint to support the group's sales globally. The company has a 20% stake in Hyundai Capital Canada and has a presence in the UK, China, and Brazil through joint ventures or associates. As a result, HCS' ratings move in tandem with those on HMC and Kia. In January, S&P revised the outlook on HMC and Kia Corp to positive from stable on their robust earnings outlook and improving credit metrics in 2024–2025. In February, Moody's upgraded HMC and Kia to A3 from Baa1, reflecting their improving profitability and balance sheet.

Investment view

We're comfortable to hold HCS' bonds given the positive rating outlook. The curve is trading closely to that of Hyundai Capital America, which we view as Fair. HMC's and HCA's solid business performance should lend support to the bonds' performance, but we will also monitor their sales trend over the medium term.

Key risks to our view include HMC achieving worse-than-expected profitability, and a significant deterioration in HMC's balance sheet that leads to a rating downgrade.

Korea Development Bank

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Timothy Tay

Company updates

Korea Development Bank (KDB) was founded in 1954 in accordance with the KDB Act to supply industrial capital to develop South Korean industries and the national economy. As a 100% state-owned policy bank, KDB provides long-term loans to corporations in line with its development financing role and extends liquidity support to South Korea's weaker corporate sectors such as shipbuilding, shipping, and construction. The policy bank also has a market stabilization role, aiding in the restructuring of stressed South Korean corporations and purchasing corporate bonds and commercial paper to stabilize troubled companies and sectors.

In FY23, KDB recorded a 10.2% decline in net interest income to KRW 2.4tr, primarily due to a 12bps decline in its net interest margin to 0.51%. Total operating income jumped 74% to KRW 1.5tr, driven by higher non-interest income and significantly lower provisioning. At the bottom line, net profit was robust at KRW 3.5tr, boosted by valuation gains from its security portfolio and impairment gains from investments in associates. This contrasts drastically with the KRW 7.9tr loss incurred in FY22, where KDB suffered both valuation and impairment losses. KDB's loan portfolio grew 1.9% to KRW 214.3tr in FY23, while its total debt crept 1.1% higher to KRW 197.3tr. Asset quality deteriorated slightly, with the NPL ratio rising to 0.81% (FY22: 0.73%), while NPL coverage also fell to 237% (FY22: 365%) albeit still at a healthy level. KDB's capital position remained sound, with the total capital adequacy ratio (CAR) improving to 13.7%, from 13.4% in FY22. We note that the government is committed to maintaining the bank's total CAR at above 13%.

Investment view

We treat KDB as an extension of the South Korean government, in view of its 100% state-ownership, strategically important policy role, and strong track record of state support (capital injection of KRW 1.3tr in 2022 and KRW 0.8tr in 2023). KDB also benefits from a de-facto solvency guarantee by the government, allowing it to maintain stable access to wholesale funding. KDB's high concentration to the volatile shipbuilding, shipping, and construction sectors is a key credit weakness, as this may strain its asset quality during periods of economic weakness. We expect KDB's asset quality to deteriorate modestly in the near term, driven by weakness in South Korea's construction and housing sectors. Nevertheless, we remain comforted by KDB's strong access to capital markets through credit cycles and believe that the South Korean government will inject capital on a timely basis if needed. Valuation-wise, KDB's

USD bonds are trading in line with other state-owned policy banks, offering high quality long-dated paper for investors looking to add duration exposure.

Key risks for KDB include high concentration risk in volatile sectors, marked asset quality deterioration in the event of a sharp economic downturn, weak liquidity due to its large holdings of illiquid securities (as a result of debt restructuring), and any negative developments relating to South Korea's sovereign rating.

Korea Electric Power Corporation (KEPCO)

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Timothy Tay

Company updates

Korea Electric Power Corporation (KEPCO) is the sole electricity transmission and distribution company in South Korea, and it has more than 60% market share in the power generation business through its six power generation subsidiaries. The company was established by the South Korean government under the Korea Electric Power Corporation Act (KEPCO Act). KEPCO is 51% owned by the South Korean government. KEPCO has experienced healthy revenue growth over the past few years, driven by higher power sales from rising electricity demand and continuous electricity tariff increases. However, the company's operating performance and EBITDA have been volatile due to a timing mismatch between tariff adjustments and fuel cost changes. KEPCO has also been loss-making in recent years, although its profitability has picked up since 2H23. In FY23, KEPCO posted a revenue of KRW 88.2tr (+23.8% y/y), EBITDA of KRW 8.5tr, and a net loss of KRW 4.7tr (FY22: net loss of KRW 24.4tr). In order to fund its high capex requirements, KEPCO's debt burden has grown significantly over the past few years, pressuring its credit profile. As at end-2023, KEPCO's net leverage was elevated at 15.3x, while gearing (total debt/capital) was weak at 78%.

Investment view

While KEPCO's credit metrics are weak, we view liquidity risk as low due to its status as a major government-related entity (GRE), which allows the company easy access to capital markets. The KEPCO Act legally requires the government to hold at least 51% of KEPCO, eliminating the risk of privatization. Given KEPCO's monopoly over South Korea's T&D network, a default may potentially disrupt power supply in the country, hence we think there is a very strong incentive for the government to provide direct support if needed. In view of this, credit rating agencies have equalized KEPCO's ratings with that of the South Korean sovereign. We note that the South Korean government aims to resolve KEPCO's accumulated debt by 2027, hence electricity tariffs are likely to remain high to enhance KEPCO's profitability.

Valuation-wise, KEPCO's USD bonds are trading modestly wider than South Korean sovereign paper, and largely in line with bonds issued by other South Korean quasi-sovereign issuers. Despite KEPCO's weak standalone metrics, we are comfortable holding its bonds as we think it is ultimately supported by the government.

Key risks for KEPCO include a spike in fuel costs which is not matched by tariff increases, weaker ties between KEPCO and the South Korean government, and any negative developments relating to South Korea's sovereign rating.

Korea Gas Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Timothy Tay

Company updates

Korea Gas Corporation is the sole wholesale distributor and the largest importer of natural gas in South Korea. It supplies gas primarily to city gas companies, the power generating subsidiaries of Korea Electric Power Corporation (KEPCO), and other power generating companies in South Korea. The South Korean government has majority ownership in Korea Gas via a 26.2% direct stake, a 20.5% stake via KEPCO, and a 7.9% stake by local governments. Gas prices in South Korea are regulated via a sales price adjustment mechanism, allowing Korea Gas to pass through its raw material costs. However, the implementation of this price adjustment mechanism has not always been timely, especially in times of surging LNG prices, resulting in volatile financial performance for Korea Gas over the past few years. In FY23, Korea Gas reported a weak set of results, with revenue down 13.9% at KRW 44.6tr and EBITDA falling 18.5% to KRW 3.4tr as both sales price and volumes declined during the year. The company recorded a net loss of KRW 747bn (FY22: net profit of KRW 1.5tr), bogged down by higher interest expense and impairment losses. On a positive note, Korea Gas reported improved financial performance in 1Q24, with EBITDA of 1.4tr (+33.4% y/y) and net income of KRW 407bn (+192% y/y). However, its credit metrics remain weak, with annualized net leverage of 6.9x and gearing (total debt/capital) of 80% as of 1Q24.

Investment view

On a standalone basis, Korea Gas' credit fundamentals are weak, with high leverage, volatile earnings and cash flow, and elevated gearing. The company also has substantial capex plans to increase its storage capacity and expand its pipeline network, which may further put pressure on its leverage metrics. Nevertheless, Korea Gas is a key SOE providing a critical service to the South Korean economy, hence, a default event would have a significant socio-economic impact, which we believe is a scenario that the government will be keen to avoid. On that basis, we expect forthcoming state support if required. Not surprisingly, its credit ratings have also been equalized with the sovereign, making its standalone credit profile less of a consideration for bond investors. Korea Gas recently issued a 5-year USD bond which was met with decent demand, highlighting its strong access to capital markets. Korea Gas's USD bonds are trading slightly outside bonds issued by fully state-owned policy banks but in line with bonds issued by comparable quasi-sovereigns and its shareholder KEPCO. We view Korea Gas' bonds as a high-quality carry play.

Key risks for Korea Gas include cash flow and earnings volatility arising from late implementation or suspension of the price adjustment mechanism, unfavorable regulatory changes in the natural gas sector, a reduced stake or weaker ties with the South Korean government, and any negative developments relating to South Korea's sovereign rating.

Korea Hydro & Nuclear Power Co Ltd (KHNP)

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Timothy Tay

Company updates

Korea Hydro & Nuclear Power Co Ltd (KHNP) is one of the wholly-owned six power generation subsidiaries (gencos) of Korea Electric Power Corporation (KEPCO), which is in turn 51% owned by the South Korean government. KHNP owns numerous nuclear, hydroelectric, and renewable power generation units, generating more than 30% of total power generated in South Korea. KHNP's sales benefit from low cyclicality in the country's electricity demand, which has been growing at a steady rate. KHNP is able to mitigate volatility in fuel costs by selling all electricity generated to KEPCO, as the pricing mechanism allows for an effective cost pass-through. In FY23, KHNP posted a revenue of KRW 11.0tr (+3.5% y/y), EBITDA of KRW 5.2tr (+10.9% y/y), and net income of KRW 122bn, as compared to a net loss of KRW 62bn in FY22. The genco's strong FY23 operating results can be attributed to both higher electricity prices and an increase in the volume of electricity sold. KHNP's capex is elevated due to its continuous expansion needs, in line with the government's plan for nuclear energy to make up at least 30% of total power generation by 2030. Due to the high capex, KHNP's debt burden has been rising, with total debt increasing 9.8% y/y to KRW 13.8tr as at end-2023. KHNP's credit metrics are sound, with net debt/EBITDA at 2.4x (FY22: 2.5x), interest coverage at 5.8x (FY22: 4.4x) and gearing (total debt/capital) at 36% (FY22: 32%).

Investment view

As the sole nuclear power generator in South Korea, KHNP is strategically important to the country's economy, in our view. KHNP is also a core subsidiary of KEPCO and the largest contributor to KEPCO's total power generation, hence we believe KHNP will enjoy extraordinary support from KEPCO via the South Korean government if needed. Accordingly, KHNP's credit ratings have also been equalized with those of KEPCO and the South Korean sovereign. On a standalone basis, KHNP's credit profile is also solid, supported by modest leverage and healthy gearing. Going forward, KHNP's high capex needs may increase its debt load, but we think this is mitigated by strong access to capital markets due to its government linkage and high credit ratings. We are cognizant that KHNP is exposed to liabilities relating to the decommissioning of nuclear power plants, which is a lengthy and onerous process, but we believe KHNP is adequately equipped to manage this obligation. Valuation-wise, KHNP's USD bonds generally trade in line or marginally wider than those of its parent, KEPCO. We are comfortable taking credit exposure to KHNP, given our expectations of state support if needed.

Key risks for KHNP include operational risks arising from nuclear power generation and decommissioning of nuclear power plants, a weaker relationship between KHNP and KEPCO or KEPCO and the Korean government, and any negative developments relating to Korea's sovereign rating.

Korea Mine Rehabilitation and Mineral Resources Corp (KOMIR)

UBS credit outlook: Stable
Moody's/S&P ratings: A1/A+
Analyst coverage: Daniel Tam

Company updates

Korea Mine Rehabilitation and Mineral Resources Corp (KOMIR) was incorporated in September 2021 through the merger between Korea Resources Corp (KORES) and Mine Reclamation Corporation (MIRECO) to address KORES' complete equity erosion and liquidity problems. The company is 100% owned by the South Korean government and is mandated to secure a stable supply of critical strategic and rare minerals for South Korea, which imports 93% of its required strategic minerals. The company reported a weak set of 2023 results, with a widened net loss, higher leverage and weaker liquidity. Revenue was flat, while EBITDA and net loss worsened to KRW –44bn and KRW –312bn (2022: KRW –12bn and KRW –18bn), respectively. The company remained in negative equity because of net losses in previous years, with its equity position reaching KRW –2.5tr at the end of 2023. Total debt increased 13.3% to KRW 5.6tr, raising total debt/capital to 1.8x (2022: 1.9x). Operating and free cash flows remained negative and deteriorated to KRW –340bn and KRW –347bn (2022: KRW –108bn and KRW –112bn), respectively.

Investment view

Established under the KOMIR Act, the South Korean government is required to contribute authorized capital of up to KRW 3tr to the company. KOMIR can only be privatized through an amendment of the KOMIR Act by the National Assembly. Pursuant to the KOMIR Act, the government may provide capital injections and subsidize part of the costs required for KOMIR's projects within the limits of the budget. The government may also guarantee the repayment of the principal and interest of corporate bonds issued by KOMIR. Deficiencies in the legal reserve may also be compensated by the government. We believe KOMIR will remain in negative equity unless the government injects a significant amount of cash to the company, but the negative equity position should not affect the company's operations and repayment ability.

Key risks include the company's weaker importance to the South Korean government, or in the event that the government assigns another state-owned institution to take on the role of KOMIR.

Korea National Oil Corporation (KNOC)

UBS credit outlook: Stable
Moody's/S&P ratings: Aa2/AA
Analyst coverage: Daniel Tam

Company updates

Korea National Oil Corporation (KNOC) was established to secure South Korea's long-term energy security by owning oil and gas fields in the country and overseas. It is the only oil stockpiling company in South Korea and is responsible for managing the country's strategic petroleum reserves (SPRs). The company also operates 1,276 gas stations in South Korea, with an approximate market share of 11.6%. KNOC reported a weak set of 2023 results, with lower earnings, higher leverage, and weaker liquidity. Revenue, EBITDA, and net profit declined 16.9%, 43.8%, and 40.6%, respectively. The weaker earnings lowered EBITDA/interest to 3.2x (5.8x in 2022) and raised total debt/EBITDA to 10.3x (2022: 5.8x). Operating cash flow remained positive at KRW 823bn (2022: KRW 902bn) and free cash flow declined to KRW 316bn (2022: KRW 439bn).

Investment view

KNOC's international credit ratings are equivalent to South Korea's sovereign ratings, reflecting its 100% ownership by the government from which it receives strong financial support, such as capital injections and government loans. Due to the company's strategic importance to Korea's energy security and state ownership, we believe the government will provide extraordinary support to KNOC, if necessary.

Key risks include a change in the KNOC Act that allows the government to reduce its ownership in the company, and a sharp decline in crude oil price that weakens the company's earnings.

LG Chem

UBS credit outlook: Stable
Moody's/S&P ratings: A3/BBB+
Analyst coverage: Daniel Tam

Company updates

LG Chem is one of Asia's largest petrochemical producers and the world's third-largest EV battery manufacturer via its listed subsidiary LG Energy Solution (LGES). LGES had a 13.6% market share of the global EV battery manufacturing market as of end-1Q24. The debt-funded expansion of its EV battery and battery material segments has improved LG Chem's sales performance and profitability, but the higher capital expenditure has also increased the company's operational and financial risks. LG Chem reported a weak set of 1Q24 results, with lower earnings, higher leverage and deteriorated liquidity. Revenue, EBITDA, and net profit declined 18.7%, 21.7%, and 48.9% from a year earlier. Total debt increased 38%, raising total debt/EBITDA to 18.3x (1Q23: 10.4x) and increasing net debt/total capitalization to 22.7% (1Q23: 19.7%). Liquidity also weakened as operating cash flow declined 9.7%.

Investment view

LG Chem plans to dispose of non-core assets, but it has no plan to slow down or reduce its capital expansion agenda. Rising leverage and weakened credit metrics should likely result in negative rating actions. Moody's and S&P have affirmed the company's credit ratings, but have revised LG Chem's outlook to negative from stable. Unless the petrochemical and EV battery sectors recover, or the company implements actions to lower its leverage, further negative rating action may likely be on the way. One avenue for LG Chem to reduce leverage is via equity placements and listing of subsidiaries, which it has done in the past.

Key risks include prolonged weakness in the petrochemical and EV battery sectors and further deterioration in its credit metrics.

Mirae Asset Securities

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB
Analyst coverage: Daniel Tam

Company updates

Mirae Asset Securities (MAS) is the largest securities house in South Korea in terms of total assets, shareholders' equity and the number of onshore and offshore branches. The company also has the largest overseas investments amongst all South Korean securities houses. The company reported a weak set of 1Q24 results, with lower earnings, higher leverage, and weaker cash flow. Revenue, operating income, and net profit declined 8.5%, 4%, and 28.4% y/y, respectively. Total debt increased 25%, raising total debt/

capitalization to 91% in 1Q24 (89% in 2023). Net capital ratio and leverage ratio remained stable at 21.5x (2023: 21.4x) and 695% (2023: 693%), respectively.

Investment view
Mirae Asset Securities' profitability is likely to stay subdued, in our view, as potential impairment losses and/or additional provisions for property exposures could add to its financial burden over the next one to two years. This is despite Mirae Asset Securities' lower exposure to such risks, compared with the industry average. Recently, S&P revised MAS's rating outlook to negative, citing the securities sector's overall property risks. The South Korean government has been providing operational and financial support to the country's securities companies, which are treated as important financial institutions and are closely monitored by the government. We believe MAS should be able to weather the current sector downturn. The company is also the first South Korean securities company which tapped the offshore bond market in January 2024.

Key risks include weaker government support to the securities sector, a further deterioration in onshore and offshore property markets, and a sharp deterioration in the company's liquidity.

POSCO
UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/A-
Analyst coverage: Timothy Tay

Company updates
POSCO is the largest fully-integrated steel producer in South Korea. The company was incorporated in March 2022 following a vertical spin-off of the steel business by POSCO Holdings, with POSCO Holdings retaining 100% ownership of POSCO. Given the close linkage between POSCO and POSCO Holdings (e.g., equalized credit ratings; POSCO also contributes 75–80% of POSCO Holdings' operating profit), we base our credit assessment on POSCO Holdings' financials instead of solely on a standalone basis for POSCO. In recent years, POSCO Holdings' operating performance has been on a weakening trend, bogged down by tough steel market conditions amid persistent overcapacity in Asia's steel industry.

In FY23, POSCO Holdings' revenue amounted to KRW 77.1tr (–9% y/y), while EBITDA fell 13.9% to KRW 7.4tr and net income declined by 48.2% to KRW 1.8tr. Key steel subsidiary POSCO saw production volume rise 4.3%, but this was more than offset by a decline in sales, resulting in a lower revenue (–8.7% y/y) and weaker operating profit (9.2% y/y). POSCO Holdings' credit metrics deteriorated in FY23, with net leverage rising to 2.6x (FY22: 1.9x) and gearing (total debt/capital) marginally higher at 30% (FY22: 29%). POSCO Holdings' weak operating performance continued into 1Q24, with EBITDA down 5.2% y/y at KRW 1.5tr and net income down 27.7% y/y at KRW 608mn. On an annualized basis, its net leverage deteriorated to 3.4x —above rating agencies' downgrade triggers, which may potentially put pressure on its ratings.

Investment view
POSCO has a dominant position in South Korea's steel market with a diversified customer base; the company typically adopts a prudent financial policy, which keeps its credit profile healthy. However, both its high exposure to commodity prices and the steel market's notable correlation with global economic growth (which is slowing) entails greater earnings volatility. Parent POSCO Holdings' growing non-steel business provides some earnings diversity, with the battery materials business set to expand in the coming years. Nonetheless, the bulk of POSCO Holdings' earnings are still driven by the steel business (POSCO), which may remain under pressure in the near term, given the current oversupply situation. Based on its track record, we expect POSCO to maintain a disciplined financial policy, which should limit a material deterioration in its credit metrics, in our view. Valuation-wise, POSCO's USD bonds trade generally in line with similarly rated South Korean peers such as LG Chem, and we do not see any reason for divergence from its peer group.

Key risks for POSCO include substantial weakness in the global steel market, environmental and social risks stemming from more onerous carbon and pollution regulations, and potential rating downgrades if its credit metrics exceed the downgrade thresholds for a sustained period.

SK Battery America
UBS credit outlook: Deteriorating
Moody's/S&P ratings: Baa3/NR
Analyst coverage: Daniel Tam

Company updates
SK Battery America (SKBA) operates battery production plants in the United States. It is a wholly-owned subsidiary of SK On, which is in turn 96.5%-owned by SK Innovation (SKI, Baa3/BB+). SK On is the world's fifth-largest producer of rechargeable lithium-ion batteries, with a market share of around 4.5% in 1Q24. SKBA and SK On do not release individual financial information. SKI reported a mixed set of 1Q24 results, with a widened net loss, lower leverage, and stable liquidity. Revenue declined 1.5% y/y, while EBITDA increased 33.2% y/y on improved profit margin and higher depreciation. Net loss widened by 88% to KRW 98bn, owing to large non-operating losses including FX-related and derivative trading losses, and higher interest expense. Higher total debt was offset by increased equity, which lowered total debt/capitalization to 61.5% (1Q23: 72.2%) while cash/short-term debt increased to 1.18x

(1Q23: 0.89x). Operating cash flow increased 2.7% y/y to KRW 829bn, while negative free cash flow widened by 15.6% y/y to KRW 1.4tr.

Investment view
SKBA's 2026 senior unsecured note is unconditionally and irrevocably guaranteed by its parent SK Innovation (SKI, Baa3/BB+), while its 2027 senior unsecured note is guaranteed by Kookmin Bank (Aa3/A+). SKI announced that it is considering various strategic plans, including mergers, to improve shareholder returns. We believe SKBA bonds' performance is tied to the financial performance of its guarantors, which will likely support the bond repayment, in case the company is unable to repay by its own.

Key risks include better-than-expected EV battery demand for SK On, and an improvement in guarantor SKI's financial profile.

SK hynix Inc.
UBS credit outlook: Stable
Agency ratings: Baa2/BBB-
Analyst coverage: Eve Li

Company updates
SK hynix is one of the world's leading memory semiconductor companies. It designs, manufactures, and sells advanced memory semiconductors including DRAM and NAND flash memory chips. SK Square was SK hynix's largest shareholder with a 20.1% stake as of end-2023. The two companies are in turn member companies of SK Group, the second-largest conglomerate in South Korea in terms of total assets.
In 1Q24, SK hynix reported above-consensus results, with profitability and debt metrics showing significant sequential recovery. Strong AI-related demand in HBM and enterprise SSD contributed to 20%+ q/q and 30% q/q hikes in the average selling price for DRAM and MANDY, while other product lines also witnessed improved pricing. This more than offset softer bit shipments due to the relatively weak demand from PCs and smartphones, leading to a 10% q/q or 144% y/y growth in revenue to KRW 12.4tr. Together with ongoing cost-cutting efforts and a reversal of inventory valuation losses, operating profit expanded to KRW 2.9tr, with a 23% y/y rise in the profit margin (versus –67% y/y in 1Q23). Notably, its NAND business saw an earlier-than-expected operating profit turnaround, thanks to a favorable product mix and rapid ASP improvement for two consecutive quarters. Also, reported EBITDA rose 70% q/q to KRW 6.1tr, while total debt was largely stable at KRW 29.5tr. As a result, total debt-to-last-twelve-month EBITDA improved sharply to 2.5x in 1Q24, from 5.5x in 2023.

The company believes the memory market is entering a full recovery cycle, supported by ongoing strength in AI memory chips as well as improving demand from conventional applications from 2H24. To meet the growing demand, management has guided higher capex this year than initially planned. Earlier this year, SK hynix announced its plan to build a M15X fab in Korea for producing next-generation DRAM including HBM. Construction work is set to be completed in November 2025 for early mass production at a cost of KRW 5.3tr, while total investments in the long term are likely to exceed KRW 20tr, in our view. The company has also announced that it will invest around USD 3.87bn (KRW 5.3tr) to build an advanced packaging fab in Indiana in the US, which is scheduled to begin mass production in 2H28.

Investment view
We believe SK hynix's strong operating cash flow can help to fully cover its rising capex needs, which we expect to be KRW 14–15tr this year (versus KRW 8.3tr in 2023). In 1Q24, its net operating cash flow improved 36% q/q to KRW 5.3tr while its capex amounted to KRW 3.1tr. Factoring in the soaring 1Q24 EBITDA, we estimate SK hynix's adjusted debt to LTM EBITDA improved to below 2x using S&P's methodology, from 4.8x in 2023. Given an upward memory cycle, we expect its metrics to further improve toward 1x by year-end, which may trigger a rating upgrade by S&P. Similarly, the adjusted leverage using Moody's methodology could also improve toward 1.5x this year, indicating a higher chance of a rating outlook revision back to Stable. We maintain Fair ratings on most of its curve due to less appealing valuations.

Key risks to our view include 1) a weaker-than-expected memory upcycle, leading to a short-lived profitability recovery; 2) more-aggressive-than-expected capex, leading to higher leverage; and 3) unexpected geopolitical events.

Figure 27 - Macau gaming issuers covered in this report and their respective credit views

Company	CIO credit outlook	Rating (Mdy/S&P)	CIO credit risk flags			
			0-2y	2-5y	5-10y	>10y
Sands China	Stable	Baa2/ BBB				
Wynn Macau	Stable	B1/ BB-				
Melco Resorts Finance	Stable	Ba3/ BB-				
Studio City	Stable	B1/ B+				
SJM Holdings	Stable	Ba3/ NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 12 - Key financial & credit metrics (as of end-2023)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ interest	Total debt/ Capital
Sands China	6.5	32.3%	8.3	3.3x	4.0x	100.0%
Wynn Macau	3.1	25.8%	6.8	5.8x	1.9x	142.4%
Melco Resorts Finance	3.2	15.1%	5.2	9.1x	1.4x	104.7%
Studio City	0.4	31.9%	2.3	15.0x	1.1x	77.9%
SJM Holdings	2.8	7.8%	3.8	14.8x	0.9x	67.6%

Source: Company reports, UBS

Sands China

UBS credit outlook: Stable
Moody's/S&P ratings: Baa2/BBB-
Analyst coverage: Eve Li

Company updates
Sands China (Sands) is one of six casino operators in Macau. Its portfolio includes the Venetian Macao, The Londoner Macao, The Parisan Macao, The Plaza Macao, and Sands Macao. The company also owns some large convention and exhibition centers, such as the Cotai Expo, the Cotai Arena, and the Londoner Arena. As of end-2023, Sands operates over 12,000 hotel rooms, the most among gaming operators; it also accounts for around 40% of market share. Sands' US-based parent, Las Vegas Sands (LVS), which also runs the Marina Bay Sands in Singapore, increased its stake in Sands to 71% in April 2024. The Macau operations accounted for 51% of LVS's adjusted property EBITDA in 1Q24.

In 1Q24, Sands achieved USD 1.7bn in GGR. This was a stable q/q performance, reaching 73% of the 1Q19 level. Mass/slot GGR recovered more meaningfully to 95% of the pre-COVID level. Non-gaming revenues were 11% lower q/q at USD 412mn, contributing to 23% of total net revenues. The operations were impacted by the ongoing renovation of Londoner Phase 2 and Cotai Arena, which took out nearly 5% of the group room inventory in 1Q24 and disrupted revenue from non-gaming events. The renovation projects are scheduled for completion in phases by the Chinese New Year holiday in 2025.

Adjusted property EBITDA in the quarter was USD 610mn, 7% lower q/q and 71% of the 1Q19 level. Total debt was 2% q/q lower at USD 8.1bn, including USD 7.1bn in bonds and USD 1bn in shareholder loans (maturing in July 2028). With cash balances slightly higher, net debt was reduced by USD 276mn to USD 6.6bn. Net debt to last-twelve-months adjusted property EBITDA further improved to 2.7x (from 3.1x in 2023). Total liquidity was largely stable at USD 4.1bn, consisting of USD 1.6bn in cash and USD 2.5bn in undrawn credit facilities. The next major maturity of Sands will be the dollar bondsdue in August 2025 (USD 1.6bn outstanding).

Investment view
Sands's credit rating is impacted by LVS's credit metrics under both rating agencies' methodology. LVS is bidding for a casino license in New York and the projected cost of the building is USD 6bn, according to management. The final result of the bidding is expected to be revealed in late 2025, and S&P indicated some tolerance for a temporary spike in the group's leverage. Overall, we believe LVS will maintain a prudent financial policy, leading to a stable rating trajectory over the next 12 months.

We expect Sands to continue generating positive free cash flow due to its improving EBITDA and unaggressive capex. Under the 10-year concession, Sands commits to invest USD 4.5bn through 2032, including USD 3.4bn in capex and USD 1.1bn in opex. The company has guided for USD 700mn in capex in Macau this year, which looks manageable compared to USD 2.4bn in annual EBITDA using the current run rate. We also expect the company to make further progress in deleveraging. While the renovation projects should bring near-term disruptions, we think they will strengthen Sands's product attractiveness over the medium to long term. Given the improving fundamentals, we remain constructive on Sands and hold some attractive calls along the curve.

Key risks include 1) a worse-than-expected market share loss due to the renovation projects; 2) a worse-than-expected margin decline due to aggressive player reinvestment; and 3) a larger-than-expected capex or capital return by the parent, leading to a deteriorating rating outlook.

Wynn Macau

UBS credit outlook: Stable
Moody's/S&P ratings: B1/BB-
Analyst coverage: Eve Li

Company updates

Wynn Macau, Limited (WML) is one of six casino operators in Macau, running two properties, namely Wynn Macau and Wynn Palace. As of end-2023, WML was 71.6% owned by Wynn Resorts. The US-based parent also operates Wynn Las Vegas and Encore Boston Harbor. Macau operations accounted for 53% of the group's adjusted property EBITDA in 1Q24, compared to over 70% in 2019.

In 1Q24, WML's GGR grew 11% q/q to USD 1bn, reaching 69% of the 1Q19 level. The mass/slot GGR recovered at a faster pace, exceeding the pre-COVID level by 22%. We estimate that WML's mass GGR market share increased to 13.6% in the quarter, compared to 11.8% in 1Q19. Non-gaming revenue also fully recovered to USD 179mn, accounting for 18% of net revenues. With a more favorable mix, adjusted property EBITDA increased 14% q/q to USD 340mn. In addition, WML further reduced its net debt to USD 4.6bn in 1Q24, brining its net leverage using LTM adjusted property EBITDA to 4.1x (from 5x at end-2023).

The company's liquidity remains sufficient at USD 2.2bn, including cash and short-term investments, as well as USD 150mn in undrawn credit facilities. WML's major maturities till end-2025 include the USD 600mn bond due in October 2024 and the USD 1.3bn revolver due in September 2025, which should be fully covered by cash on hand and future cash flows. The company may also tap the USD bond market or renew the bank facilities for additional liquidity, in our view. Management has guided for USD 350–500mn in concession-related capex in 2024–2025, in addition to USD 50mn in maintenance capex annually during the two years.

Investment view

We expect Wynn Macau to further deleverage due to EBITDA recovery and manageable capex over the next 12–18 months. While there are various expansion plans at the group level, we expect its credit rating to be stable during the same period. We're therefore comfortable holding Wynn Macau's bonds and currently see better value in the 2028 bond due to yield pickup and a flat curve in the long end.

Wynn Resorts continues to look for diversification opportunities; it has announced the Wynn Al Marjan Island project located in United Arab Emirates, in which it has a 40% equity ownership. The estimated project cost is USD 3.9bn and the expected opening date is in 1Q27. Together with its joint bid with Related Co. for a New York casino license, these future development projects may increase group-level leverage. Given the long development period and uncertainty in the license bidding, we don't expect the group to incur significant capex over the next 12–18 months.

Key risks include 1) a weaker-than-expected GGR and EBITDA recovery; and 2) an unexpected aggressive debt-funded expansion of the group that leads to a rating downgrade.

Melco Resorts Finance

UBS credit outlook: Stable
Moody's/S&P ratings: Ba3/BB-
Analyst coverage: Eve Li

Company updates

As a wholly-owned subsidiary of Melco Resorts & Entertainment (MLCO), Melco Resorts Finance (MRF, the USD bond issuer), owns 85% of Melco Resorts (Macau) (MRM). MRM is one of six gaming concessionaires in Macau, operating a portfolio that includes City of Dreams, Altira, and the Mocha clubs. Studio City, the other Macau entity and 55% held by MLCO, owns the Studio City integrated resorts, and these resorts' gaming activities are also operated by MRM. MLCO also owns and operates integrated resorts in the Philippines (City of Dreams Manila) and Cyprus (City of Dreams Mediterranean). Melco International Development (MID) is the ultimate parent of MLCO, with a 51.7% stake as of end-2023. The founder, Lawrence Ho, holds around 61% of MID.

In 1Q24, MLCO's Macau operations continued to be the biggest contributor to the group's results. Mass/slot GGR in Macau recovered to 111% of the 1Q19 level, while the recovery of the VIP segment was in line with the sector at 23%. Adjusted property EBITDA in Macau was flattish q/q at USD 250mn, reaching 72% of the 1Q19 level and accounting for 84% of the group's total adjusted property EBITDA.

In April, MRF issued a new USD 750mn senior bond maturing in 2032 at a coupon rate of 7.625%. The proceeds will be used for a partial redemption of its 2020 credit facilities, with an outstanding amount of USD 900mn pre-deal. Meanwhile, MLCO also announced a two-year maturity extension of the credit facilities to April 2027. While the new issuance doesn't impact total debt, we think the company has meaningfully reduced its debt burden in 2025 with these refinancing efforts. Together with Studio City's USD 100mn tender offer in April, we estimate MLCO's pro-forma total debt and net debt to be USD 7.3bn and USD 6.2bn, respectively. Pro-forma net leverage at the group level improved to 5.2x (using annualized 1Q24 adjusted property EBITDA), compared to 5.9x at end-2023.

On 30 April, MLCO announced that it was awarded a 20-year casino license by the Sri Lanka government, and it will partner with John Keells Holdings to operate the gaming area at City of Dreams Sri Lanka, as well as some hotel rooms. MLCO expects to commence the casino operations in mid-2025, and expects the initial investment to be USD 125mn.

MLCO's liquidity is adequate, in our view, with its cash on hand fully covering the next major maturing debt (the USD 1bn June 2025 dollar bond). In addition, we estimate the group to have USD 1.8bn in pro-forma undrawn credit lines, factoring the repayment using net proceeds of the new dollar bonds. Full-year capex at the group level stands at USD 415mn, according to management.

Investment view

The recovery pace of MLCO's property EBITDA in Macau is behind that of its HY peers, partly due to unfavorable VIP luck in 1Q24. With management's focus on customer experience and enhanced product offerings, we expect the gap to gradually narrow. Ultimately, MLCO is the credit driver of MRF's bonds under both Moody's and S&P's methodologies. According to S&P, it plans to solve the current Positive outlook in mid-2024 (to upgrade or to revise it to Stable). We think a few more data points of market share movements are still needed for the agency to make a decision. That said, with the deleveraging still on track, we see carry opportunities along the curve.

Key risks include 1) a weaker-than-expected EBITDA recovery due to market share loss or aggressive reinvestment; 2) a more-than-expected cash leakage to MID.

Studio City

UBS credit outlook: Stable
Moody's/S&P ratings: B1/B+
Analyst coverage: Eve Li

Company updates

Studio City International, 55% held by Melco Resorts & Entertainment (MLCO), owns the Studio City integrated resorts in Macau. Its gaming activities are operated by the gaming concessionaire MRM, pursuant to certain agreements. Studio City receives the residual amount of its GGR after deducting gaming taxes and operating costs from MRM. With its focus on the mass market, Studio City is critical to MLCO's overall strategy in Macau. In 1Q24, it contributed to 31% and 35% to MLCO's total and mass GGR in Macau, respectively.

In 1Q24, Studio City saw its casino GGR reaching USD 318mn, +8% q/q and 91% of the 1Q19 level. Adjusted property EBITDA grew 14% q/q to USD 88mn, also recovering to 91% of the 1Q19 level. Deducting the fees and shared service charges as well as intercompany costs, Studio City's reported adjusted EBITDA of USD 66mn was around 20% lower compared to the pre-COVID level. Adjusted debt/LTM EBITDA, however, improved meaningfully to 10.9x (from 16.6x in 2023), thanks to a stable debt level and the rebound in EBITDA. The company has repurchased USD 203mn of its 2025 bond since November 2023, reducing its pro-forma total debt to USD 2.2bn, according to our estimates.

Investment view

We expect Studio City's standalone credit profile to further improve, supported by EBITDA normalization and limited capex after the opening of Studio City Phase 2. Its issuer rating contains a one-notch and a two-notch uplift under Moody's and S&P's methodologies, reflecting its role as a strategically important subsidiary of MLCO. The group supported Studio City during COVID, including subscribing twice to Studio City's private placements at a total cost of around USD 450mn. We still like Studio City's longer-end bonds for yield pickup among gaming bonds.

Key risks include a weaker-than-expected EBITDA recovery due to market share loss or an aggressive reinvestment strategy.

SJM Holdings

UBS credit outlook: Stable
Moody's/S&P ratings: Ba3/NR
Analyst coverage: Eve Li

Company updates

SJM Holdings (SJM), 61.9% owned by STDM, is one of six casino operators in Macau. SJM owns and operates the Grand Lisboa Palace Resort (GLP), and the Grand Lisboa hotel and casino, as well as other self-operated casinos. The profit-sharing agreements for its nine third-party-owned satellite casinos (14 previously) will end at end-2025. In 1Q24, SJM achieved MOP 6.9bn GGR, up 9% q/q and reaching 66% of the 1Q19 level. More notably, its mass/slot GGR at self-promoted casinos exceeded the 1Q19 level by 37%, mainly supported by the phased opening of GLP in July 2021.

Backed by the recovering GGR, SJM's adjusted EBITDA improved 23% q/q to MOP 864mn in 1Q24 (80% of the 1Q19 level), while net debt was largely stable at MOP 23.5bn. As a result, net leverage using the last-twelve-months adjusted EBITDA decreased to 9.2x as of March 2024, from 13.7x at end-2023. The interest coverage ratio also improved to 1.3x (from 0.9x). Based on the current run rate of profitability, we expect SJM's net leverage to further trend down to mid-to-high 6x by end-2024. The company's liquidity is sufficient, in our view, with MOP 7.7bn in cash and undrawn credit facilities as of March 2024.

Investment view

We expect a stable rating trajectory for SJM over the next 12 months. Its Ba3 issuer rating is anchored by an estimated adjusted debt/EBITDA of below 5x in 2025, according to Moody's. A further ramp up of GLP will support the EBITDA improvement, in our view. The property generated MOP 88bn in adjusted property EBITDA in 1Q24, from only MOP 2mn in 4Q23, and losses in previous quarters. With the full opening of Palazzo Versace in March 2024, management said that GLP's market share increased to 2.2% in April, against a target of 5%. According to the Macau Cultural Affairs Bureau, the government plans to build an outdoor performance venue capable of accommodating up to 50,000 people near GLP. The facility is scheduled to open in 2025, aiming to attract large-scale performances to the city. Together with better connectivity, plus additional retail and F&B offerings, we expect GLP to contribute more to the group's results.

In light of the guided MOP 1.5–1.6bn in capex and the expected MOP 2bn in interest expenses, we do not expect a significant reduction in total debt this year. That said, we think its leverage ratio will continue to trend down, and expect the absolute debt level to decline more meaningfully from next year. Strong parent support, indicated by the 6-year shareholder loans and subscription to its right issue in 2022, is also credit positive, in our view. After the strong rebound year-to-date, SJM's US dollar bonds are trading in line or slightly tighter compared to those from Melco Resorts Finance. We think its relative valuation is less appealing currently and have Fair ratings on the company's 2026 and 2028 bonds.

Key risks include 1) a weaker-than-expected ramp up of GLP and EBITDA improvement; and 2) a significant loss in market share and irrational sector competition.

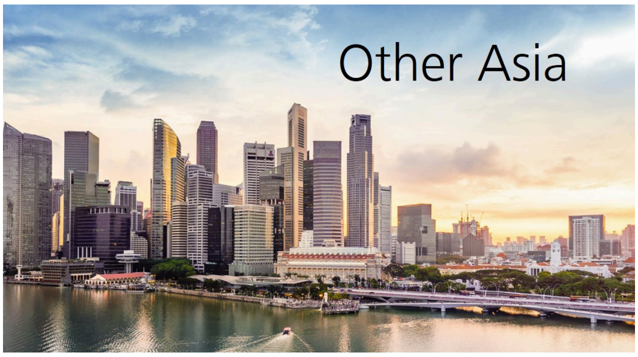


Figure 28 - Other Asian issuers covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
Ayala Corp	Stable	NR/NR				
International Container Terminal Services	Stable	NR/NR				
Jollibee Corporation	Stable	NR/NR				
San Miguel Corp	Stable	NR/NR				
Export-Import Bank of Thailand	Stable	Baa1/NR				
PTT Exploration & Production	Stable	Baa1/BBB+				
Genting Overseas Holdings	Stable	Baa2/NR				
Tenaga Nasional Berhad	Stable	A3/A-				
Mong Duong 2	Stable	Ba2/NR				
Taiwan Semiconductor Manufacturing Company	Stable	Aa3/AA-				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 13 - Key financial & credit metrics (FY23)

Issuer	Revenue (USD bn)	EBITDA margin	Total debt (USD bn)	Net debt/ EBITDA	EBITDA/ Interest	Total debt/ capital
Ayala Corp	5.2	14.5%	11.2	13.0x	1.3x	47.9%
International Container Terminal Services	2.4	63.0%	5.1	2.9x	4.1x	79.5%
Jollibee Corporation	4.4	13.6%	2.4	3.2x	4.7x	70.3%
San Miguel Corp	26.1	14.3%	26.9	6.0x	2.4x	68.7%
PTT Exploration & Production	8.5	73.8%	3.6	net cash	21.7x	20.0%
Tenaga Nasional Berhad	13.9	29.3%	20.2	3.9x	4.3x	60.3%
Mong Duong 2	0.3	72.1%	0.6	2.3x	3.7x	52.2%
Taiwan Semiconductor Manufacturing Company	70.5	67.2%	31.2	-0.4x	121.1x	21.5%

Source: Company reports, UBS

Ayala Corp

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Devinda Paranathanthri

Company updates

Ayala Corp is one of the Philippines' largest conglomerates, with businesses spanning a wide range of industries, including real estate, utilities, telecommunications, finance, energy, and infrastructure. On a consolidated basis, 2023 revenues and EBITDA increased by 10% and 22%, respectively. This was driven by strong performances from Bank of the Philippine Islands and Ayala Land. Consolidated total debt in the group also increased gradually over the past three years from PHP 377bn in 2020 to PHP 546bn in 2023 as key subsidiaries has added more debt. Therefore, consolidated debt-to-EBITDA remains weak at 14.8x. Ayala also disclosed in May 2024 its plans to sell a 22.3% stake for a consideration of USD 252mn. This sale is part of its strategy to monetize non-core assets to generate around USD 1bn to reduce debt and fund other investments.

Investment view

While consolidated metrics look weak, we believe this is less of a focus for the credit as subsidiaries can independently take care of their debt. Ayala's key strength is the market value of its key listed subsidiaries, which adequately covers the total debt at the holdco level. In our view, the holding company can also look at monetizing stakes to generate liquidity at times of need. All three remaining bonds from Ayala are fixed-for-life perpetuals, and given the low coupons (3.9%, 4.85%, and 5.125%), they are relatively cheap funding channels for the company. We believe the bonds are not very likely to be called in the coming years, and investors should view them as very long-term instruments. As such, the current yield to maturity, which is at a low 6% level, is not particularly attractive, in our view. Rather, we prefer owning a 30-year bond of a BBB-rated issuer in Asia offering a mid-to-high 5% yield, which should directly benefit from lower interest rates in the coming year.

Key risks include debt-funded acquisitions at the holdco level and a more general slowdown in the Philippine economy.

International Container Terminal Services

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Devinda Paranathanthri

Company updates

International Container Terminal Services (ICT) is an international operator of container terminals under long-term concession agreements. Asia, including its home base of the Philippines, accounts for around half of its business while the US and EMEA account for the rest. ICTSI processed 12.7mn TEUs for the full-year 2023 leading to USD 2.4bn in revenues (up 6% y/y). EBITDA for 2023 was USD 1.5bn, increasing by 7% y/y. The company reported operating cash flows of USD 954mn, and post-capex and dividends, generated free cash flows of USD 209mn. Free cash flows also helped to build its cash position, which stood at USD 716mn at end=2023. Debt-to-EBITDA for 2023 was around 3.4x, improving from the peak at 5.6x in 2020.

Investment view

We believe ICT is set to generate free cash flows of around USD 200mn in the next two years, barring any new capex plans. As a result, we expect to see a moderate improvement in its credit metrics this year. The company has a good operating track record and management has shown the ability to successfully execute its expansion plans. Given the scale and diversity in operations as well as its stable credit profile, we see this as a weak BBB rated credit. However, currently tight valuations for the bonds largely reflect this.

We expect the perpetual bond to be called in 2026 and believe the company has enough access to both offshore and onshore funding to fund this call.

Key risks include any significant capex plans that could put pressure on its balance sheet and significant currency fluctuations that can impact ICT's earnings.

Jollibee Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Devinda Paranathanthri

Company updates

Jollibee is one of the largest restaurant groups based in the Philippines. The business was heavily impacted during the COVID-19 years. But it was able to tap into the hefty cash balance it had built up by issuing USD debt in 2020 to avoid liquidity stress. The company has now improved its earnings and profitability to a level that is markedly better than the pre-COVID years, particularly for its North America operations. In 1Q24, EBITDA rose 14.7% y/y, driven by top-line growth. System-wide sales grew by 10.4% y/y in 1Q24. Net leverage as of end-1Q24 was around 3.1x. Jollibee has also announced plans to acquire a 75% stake in South Korean coffee brand Compose Coffee for a total consideration of USD 340mn. Compose Coffee's third-largest store network has a 7.5% market share in South Korea. It is also a net cash company with no outstanding debt. It is not clear how Jollibee plans to fund this acquisition, but we expect some debt addition during the year. Jollibee has made a few acquisitions in the past decade to expand its presence outside of its home base of the Philippines, and some of these acquisitions, such as Smashburger, have dragged on profitability. However, Compose Coffee appears to be more profitable than some previous transactions and is likely to be margin accretive, in our view.

Investment view

The recovery in earnings and profitability for Jollibee is a key credit positive, in our view. However, the recent acquisition is likely to lead to higher debt in the current year, but credit metrics could improve as Compose Coffee is EBITDA-accretive without any debt. We believe the perpetual bond are likely to be called in January 2025 as the coupon reset is relatively high (5Y+4.78%) and this bond offers decent short-term carry. The dated senior bond is trading at an investment grade-like valuation, though we view it as a BB credit. As such, we see less value in the 2026 and 2030 bonds.

Key risks include further acquisitions that could put pressure on its balance sheet and a general slowdown in consumer spending in the Philippines.

San Miguel Corporation

UBS credit outlook: Stable
Moody's/S&P ratings: NR/NR
Analyst coverage: Devinda Paranathanthri

Company updates

San Miguel Corporation (SMC) is one of the largest conglomerates in the Philippines, and it is engaged in the food & beverage, oil refining, power, and infrastructure businesses. SMC's 2023 revenues fell 4% but EBITDA grew 24% to PHP 205bn, driven by a strong performance across all segments. SMC Global Power's EBITDA improved by 34% as lower thermal coal prices and better cost pass-through improved margins significantly. Petron's EBITDA rose sharply (+36% y/y) as well, driven by better refining margins and volume growth. Given that SMC is a holding company, debt servicing is done through dividends from its key subsidiaries. Total dividend-related inflows were around PHP 35bn in 2023 and were not sufficient to cover the annual interest cost of PHP 38bn for the holdco. Additionally, the financial support to SMC Global Power led to a significant drop in cash balances to PHP 56bn from PHP 137bn in 2022.

Investment view

We believe the holdco's liquidity position will remain tight until some of the key subsidiaries start to upstream dividends. However, the company has demonstrated its ability to tap the bank loan market and the onshore bond market in recent times. For example, SMC secured a USD 2bn 5-year syndicated loan from 35 banks earlier in the year and raised PHP 20bn in domestic bonds to fund airport capex. These transactions should address the company's near-term funding needs. As its subsidiary SMC Global Power has called its first perpetual, this has removed a key overhang for the perpetual bond outstanding at SMC level. While its liquidity position will likely remain tight, we are comfortable owning the perp on the back of SMC's ability to access various funding channels. Our base case is for this bond to be called in July 2025 as the company is unlikely to retain it with +500bps step-up.

Key risks include further funding support for key subsidiaries such as SMC Power and other potential capex or M&As putting further pressure on holdco liquidity.

Export-Import Bank of Thailand

UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/NR
Analyst coverage: Joel Tan

Company updates

The Export-Import Bank of Thailand (EXIM Thailand) is a 100% state-owned policy bank under the supervision of the Ministry of Finance (MoF). The bank provides credit facilities, guarantees, insurance against risk, and other services in order to promote and support Thai exports, imports, and investments. Unlike commercial banks, EXIM Thailand does not accept retail deposits and only sources deposits from government agencies and state-owned enterprises (SOEs), and hence relies heavily on wholesale funding. EXIM Thailand has grown its loan book steadily over the past few years, often taking a countercyclical role with regard to loan disbursement in line with its policy role. In FY23, EXIM Thailand recorded strong net interest income of THB 4.3bn (+12.8% y/y), buoyed by healthy loan growth of 4.3%. However, expected credit losses more than doubled to THB 2.8bn (FY22: THB 1.1bn), resulting in a 69.7% decline in net profit to THB 456mn. Higher provisioning came on the back of deteriorating asset quality, with EXIM Thailand's NPL ratio rising to 4.7% (FY22: 2.9%). EXIM Thailand's provision coverage ratio also weakened to 190.7%, from 263% in FY22. EXIM Thailand's capitalization metrics improved in FY23, following the MoF's capital injection in March 2023, with its Tier 1 ratio at 12.1% (FY22: 11.3%) and total capital adequacy ratio at 13.4% (FY22: 12.1%), well above regulatory minimums.

Investment view
We view EXIM Thailand as an extension of the Thai government, given its 100% state ownership and important policy bank status. We are moderately concerned with the sharp deterioration in asset quality in FY23, but we believe that the policy bank will continue to enjoy forthcoming state support if required, as evidenced by the MoF's recent capital injection in March 2023. Due to its government linkage, EXIM Thailand also enjoys good access to capital markets at a reasonably low funding cost, mitigating refinancing risks from its sizable debt burden. Valuation-wise, EXIM Thailand's USD bonds generally trade in line with than those issued by similarly-rated Thai commercial banks such as Bangkok Bank and Kasikornbank. Investors who want USD exposure to the Thai sovereign (which does not have outstanding USD debt) can consider EXIM Thailand's USD bonds as an equivalent, in our view.

Key risks for EXIM Thailand include a severe slowdown in the Thai economy leading to further asset quality deterioration, a heavy reliance on wholesale funding which would pose refinancing risks, and less state support.

PTT Exploration & Production (PTTEP)

UBS credit outlook: Stable
Moody's/S&P ratings: Baa1/BBB+
Analyst coverage: Devinda Paranathanthri

Company updates
PTT Exploration & Production (PTTEP) is a large integrated energy company in Thailand and is 65% owned by PTT Public Co. Ltd, which is majority owned by Thailand's Ministry of Finance. PTTEP has long-term contractual agreements with PTT, where it sells close to 70% of the production. The company has generated very strong EBITDA margins above 70% over the past three years. PTT's credit metrics are currently very strong, with the balance sheet in a net cash position. Total debt-to-EBITDA stood at 0.6x for 2023. PTTEP recently announced the acquisition of a 10% stake in Ghasha Concession, one of the largest natural gas fields in the United Arab Emirates. We think this is likely to be funded by its internal resources. According to S&P, this will increase its reserve life from 6.2 years in December 2023 to 7.3 years.

Investment view
As a key government-linked company engaged in oil & gas exploration activities, we believe there is a high likelihood of government support if the need arises. PTTEP also has solid credit fundamentals and is one of the stronger entities within the PTT Group umbrella. Given its strong balance sheet, we believe the company will be on the lookout for sizable acquisitions. However, good acquisitions that can materially improve its reserve life will be a credit positive, in our view. The company has not issued USD bonds for some time and given the strong cash position of USD 5.2bn, we do not see any immediate need to return to the USD bond market.

Key risks include any negative developments relating to its Myanmar operations and a significant drop in oil prices.

Genting Overseas Holdings

UBS credit outlook: Stable
Agency ratings: Baa2/NR
Analyst coverage: Eve Li

Company updates
Genting Overseas Holdings (GOHL) is a wholly-owned subsidiary of Genting Berhad (GENT). GOHL's main holding is a 52.6% stake in Genting Singapore (GENS), and its primary source of cash flow is dividends from GENS. GENS owns Resorts World Sentosa (RWS) in Singapore, which houses one of the only two casinos in the country. Other attractions include S.E.A. Aquarium, Adventure Cove Waterpark, Universal Studios Singapore, hotels, and MICE facilities.

In 2023, Singapore's tourism sector captured a strong post-COVID rebound, with international visitor arrivals and tourism receipts reaching 71% and 98%, respectively, of 2019 levels (from 33% and 51% in 2022). GENS also witnessed a full normalization of its gaming business, and net revenues including non-gaming grew 41% to SGD 2.4bn. The consolidated adjusted EBITDA was SGD 1.02bn, or SGD 1.06bn for the Singapore leisure and hospitality segment only, representing a 86% recovery compared to the 2019 level. The relatively lower EBITDA recovery was due to an increase in the gaming tax rate in 2022, leading to a lower EBITDA margin of 43.7% (vs. 49.7% in 2019). GENS maintained a strong net cash position, with SGD 3.6bn cash on hand, no borrowings outstanding, and only SGD 3mn in lease liabilities. Its operating cash flows improved to SGD 959mn, comfortably covering SGD 328mn capex, minimal interest, and SGD 423mn in dividends. Based on its stake in GENS, GOHL received SGD 222mn in dividends in 2023, more than sufficient to cover its annual coupon costs of USD 64mn (SGD 86mn).

We expect GENS to incur higher capex over the next few years for its strategic transformation. Its RWS 2.0 plan includes a waterfront development, a new theme zone at Universal Studios Singapore, and an expanded aquarium. That said, we don't expect higher investment needs to derail its ability to distribute regular and steady (if not higher) dividends, thanks to its strong cash flows and abundant cash on hand.

Investment view

GOHL and its wholly-owned subsidiary GOHL Capital (the issuer) are supported by a keepwell deed from GENT. We believe the parent will lend support to GOHL in its redemption or refinancing of the bonds upon maturity in 2027. To ensure GENS renews its casino licenses every three years, in our view, the solvency of GOHL is crucial. GENS is also one of the key contributors to GENT's adjusted EBITDA (40% in 2023). We rate the bonds as Fair given ther similar trading level as Sands China's 2027 bonds.

Key risks to our view include an unexpected significant decline in GENS's dividends due to larger-than-expected capex.

Tenaga Nasional Berhad

UBS credit outlook: Stable
Moody's/S&P ratings: A3/A-
Analyst coverage: Joel Tan

Company updates

Tenaga Nasional Berhad (TNB) is the largest vertically integrated electricity utility in Malaysia, with core business activities including the generation, transmission, and distribution of electricity. 60% of TNB is indirectly owned by the Malaysian government, with the country's sovereign wealth fund Khazanah Nasional Berhad owning a 22.6% stake in TNB, while other government-related agencies cumulatively hold 44.9% of TNB's shares. Malaysia's electricity transmission and distribution (T&D) business is highly regulated, with the regulatory framework allowing TNB to pass through any variation in fuel costs and other generation costs via an imbalance cost pass-through (ICPT) mechanism.

In FY23, TNB revenue declined 13% to MYR 63.7bn, though this was a function of a higher ICPT cost recovery in the prior year. Revenue excluding ICPT cost recovery, which is more reflective of TNB's operating performance, was up 4.3% at MYR 53.1bn on the back of increased electricity demand. However, EBITDA was 10.5% lower at MYR 18.6bn, and net income fell 26.8% to MYR 2.6bn. TNB's credit profile strengthened in FY23, underpinned by an improved liquidity position following robust free cash flow. Net leverage declined to 3.9x (FY22: 4.4x) while gearing (total debt/capital) improved to 60.3% (FY22: 61.4%). In 1Q24, TNB's revenue excluding ICPT cost recovery was 8% y/y higher at MYR 13.6bn on strong electricity demand growth. However, EBITDA was 1.6% y/y lower at MYR 4.4tr while net profit slumped 27.2% y/y to MYR 678mn, largely attributable to a sizable forex translation and higher tax expenses. Despite this, TNB's credit metrics remained stable, with annualized net leverage at 3.7x and gearing at 60.1%.

Investment view

As Malaysia's primary electricity generation enterprise, TNB boasts a dominant market position and plays a strategically important role in Malaysia's electricity sector. TNB also benefits from a well-diversified customer base and a predominance of long-term contracts, which allows for stable cash flow. A key credit weakness for TNB is the six-month timing mismatch between upfront generation costs and ICPT cost recovery, which results in a spike in receivables and high working capital needs during periods of elevated fuel costs. Nevertheless, we take comfort from its strong track record of timely and adequate ICPT cost recovery, with the government also providing a MYR 6bn guarantee to support TNB's working capital requirements. TNB's credit profile has improved in the past 12–18 months, supported by a stabilization in fuel costs and an improvement in receivables collection, prompting a rating upgrade by S&P from BBB+ to A-. On a standalone basis, we view TNB's credit profile as weak for a high investment grade credit, but we think this is well mitigated by the high likelihood of state support if required. Valuation-wise, TNB's USD bonds are trading at similar levels to other quasi-sovereign Malaysian credits, and we view the bonds as a decent carry trade for investors looking for quality Malaysian credit.

Key risks for TNB include a timing mismatch between upfront generation costs and cost recovery granted by the government, and foreign exchange (FX) risks due to a currency mismatch between costs and revenues.

Mong Duong 2

UBS credit outlook: Stable
Moody's/S&P ratings: Ba2/NR
Analyst coverage: Devinda Paranathanthri

Company updates

Mong Duong 2 (MD2) is an independent power producer (IPP) in Vietnam holding a 25-year concession to operate a 1,120MW aggregate capacity coal-fired power plant. MD2 operates under a long-term power purchase agreement

(PPA) with the state electricity company which allows for full cost pass-throughs. MD2's 1Q24 EBITDA was USD 63mn versus USD 56mn in 4Q23. In general, annual EBITDA has been around the USD 240mn level, without much volatility given the stable business model. Gross leverage for 1Q24 on an annualized basis stood at 2.5x. The bonds started amortizing in November 2023 with annual payments of around USD108mn which should be funded by internal cash flows and its cash position of around USD 97mn as of March 2024. Since the amortization commenced in November 2023, cash flows left for dividends are likely to be much less than previous years, in our view.

Back in December 2023, AES Corp announced that it had signed an agreement to sell its 51% stake in MD2 to Sev.en Global Investments. This will not trigger a change of control as the acquirer is considered to be a qualified transferee. Such ownership changes in coal-fired generation capacity are a broader theme we have observed in other IPPs. We note that the company's ability to pay dividends following the bond amortization is now limited. But the new owners have limited options to change the financial policies given the bond covenants, in our view.

Investment view
MD2 has a stable credit profile and its PPA ensures adequate cost pass-throughs. We believe the debt position should gradually come down over the next two years with the bond amortization. This also alleviates some refinancing risk at the final maturity and reduces the weighted average life of the bond to less than three years. The bonds are trading at a ESG premium over other BB rated bonds as MD2 runs a coal-fired power plant. Taking this into consideration and despite the headlines around ownership changes, the current yields just above 7% look decent to us for a stable BB credit.

Key risks include any operational issues that could impact the capacity availability of the power plant and any negative developments relating to the ownership change.

Taiwan Semiconductor Manufacturing Company

UBS credit outlook: Stable
Agency ratings: Aa3/AA-
Analyst coverage: Eve Li

Company updates
Founded in 1987, Taiwan Semiconductor Manufacturing Company (TSMC) is the world's largest semiconductor foundry and was the pioneer of the pure-play foundry business model in the semiconductor industry. Its annual manufacturing capacity exceeded 16mn 12-inch equivalent wafers in 2023, with nine wafer fabs in Taiwan, two in mainland China, and one in the US. The company is also constructing two fabs in Arizona, and the first fab is targeted to start production in 1H25. A new fab in Kumamoto, Japan is also scheduled for production in late 2024.

In 2Q24, TSMC reported NTD 674bn in net revenue, +13.6% q/q and +40.1% y/y. 5nm remains the biggest revenue contributor (35%), followed by 7nm (17%), 3nm (15%), and 16nm (9%). By platform, HPC and smartphone accounted for 52% and 33% of net revenue, respectively. It maintained a largely stable gross margin at 53.2%, in line with its long-term target. The company further strengthened its net cash position to over NTD 1tr as of end-June. For 3Q24, the company has guided USD 22.4–23.2bn in revenue, implying a 8–11% q/q growth. Gross margin and operating margin are expected to be 53.5–55.5% and 42.5–44.5%, respectively.

Investment view
The rising AI demand and constant developments will likely benefit TSMC thanks to its technology leadership and close relationships with its customers. This will drive the company's revenue growth over the next few years, in our view. We also expect its margin to be supported by its crucial role in the value chain and potential price hikes for certain products to key customers. While its capex will likely remain high over the next 1–2 years due to continuous capacity expansion, we believe it can be fully covered by the strong operating cash flow. We view TSMC's financial risk as minimal over the next 1–2 years and think its USD bonds are suitable for investors wanting quality bond exposure. That said, we're mindful of higher volatilities of its longer-end bonds due to rate movements.

Key risks to our view include higher rates for longer and unexpected negative geopolitical events.

Figure 29 - Banks covered in this report and their respective credit views

Issuer	CIO credit outlook	Rating (Mdy's/S&P)	UBS risk flags: Senior 0-2y	2-5y	5-10y	>10y
Bank Of China	Stable	A1/A-				
Bank Of Communications	Stable	NR/A-				
China Construction Bank	Stable	A1/A				
Industrial & Commercial Bank Of China	Stable	A1/A				
Bank of East Asia	Deteriorating	A3/A-				
Citic Bank International	Deteriorating	A3/NR				
CMB Wing Lung Bank	Deteriorating	NR/NR				
Dah Sing Bank	Stable	A2/NR				
Nanyang Commercial Bank	Deteriorating	NR/NR				
Axis Bank	Stable	Baa3/BBB-				
HDFC Bank	Stable	Baa3/BBB-				
ICICI Bank	Stable	Baa3/NR				
State Bank Of India	Stable	Baa3/BBB-				
PT Bank Mandiri	Stable	Baa2/BBB				
PT Bank Negara Indonesia	Stable	NR/BBB				
PT Bank Tabungan Negara	Stable	NR/NR				
Keb Hana Bank	Stable	Aa3/A+				
Kookmin Bank	Stable	Aa3/A+				
Shinhan Bank	Stable	Aa3/A+				
Woori Bank	Stable	A1/A+				
DBS Group	Stable	Aa2/NR				
OCBC	Stable	Aa1/AA-				
UOB	Stable	Aa1/AA-				
Bangkok Bank	Stable	Baa1/NR				
Kasikornbank	Stable	Baa1/NR				
Krung Thai Bank	Stable	Baa1/NR				

Source: UBS. Please see the back of the report for the definition of risk flags

Table 14 - Key financial & credit metrics (as of end-2023)

Issuer (Bank)	Net interest margin	NPL ratio	CET1 ratio
Mainland China			
Bank Of China	1.6%	1.3%	11.6%
Bank Of Communications	1.3%	1.3%	10.2%
China Construction Bank	1.7%	1.4%	13.1%
Industrial & Commercial Bank Of China	1.6%	1.4%	13.7%
Hong Kong			
Bank of East Asia	2.1%	2.7%	17.3%
Citic Bank International	1.8%	2.3%	13.4%
CMB Wing Lung Bank	1.8%	1.5%	13.9%
Dah Sing Bank	2.0%	1.9%	16.2%
Nanyang Commercial Bank	1.6%	2.3%	13.2%
India			
Axis Bank	4.1%	1.6%	13.7%
HDFC Bank	3.4%	1.3%	16.3%
ICICI Bank	4.6%	2.3%	16.0%
State Bank Of India	3.3%	2.4%	9.1%
Indonesia			
PT Bank Mandiri	5.5%	1.2%	20.3%
PT Bank Negara Indonesia	4.6%	2.1%	18.8%
PT Bank Tabungan Negara	3.8%	3.0%	17.5%
South Korea			
Keb Hana Bank	1.6%	0.3%	16.1%
Kookmin Bank	1.8%	0.3%	14.9%
Shinhan Bank	1.6%	0.2%	14.6%
Woori Bank	1.6%	0.2%	13.2%
Singapore			
DBS Group	2.2%	1.2%	14.6%
OCBC	2.3%	1.0%	15.9%
UOB	2.1%	1.5%	13.4%
Thailand			
Bangkok Bank	3.0%	2.7%	15.4%
Kasikornbank	3.7%	3.2%	16.5%
Krung Thai Bank	3.2%	3.1%	16.5%

Source: Company reports, UBS

Mainland China banks

FY23 results

Our covered banks reported lackluster FY23 earnings. CCB, ICBC, and BOCOM saw their pre-provision operating profit (PPoP) decline 2–6% due to NIM compression and lower non-interest income after policy adjustments (mortgage repricing and fee cuts). BOC outperformed thanks to stronger loan growth and a narrower NIM decline. Except for BOCOM, all our covered banks reported accelerated RWA expansion, likely due to the extension of loans to support the real economy. This resulted in capital ratios declining 20–55bps. BOCOM's capitalization improved marginally, but remained the weakest among its peers. It has been designated as a G-SIB since October 2023 and faces capital-raising pressure. Asset quality was better than feared; NPL ratios remained broadly stable and provision coverage ratios improved.

Key credit drivers

Rate cuts and policy risk: We expect NIM pressure to persist due to 1) loan prime rate cuts; 2) continued mortgage repricing; and 3) its loan mix skewing toward lower-yield corporate loans in policy-supported sectors. Future earnings should be constrained, in our view, but banks could release provision buffers to offset negative NIM impact.

Capital management: Muted earnings and accelerated RWA expansion will likely add downward pressure on capital ratios. In addition, these banks face additional TLAC capital requirements by January 2025. ICBC and BOC have announced TLAC issuance totaling CNY 210bn this year. We expect most of the supply, if not all, to be fulfilled onshore.

Investment view
We have Fair ratings on most mainland Chinese state-owned banks' senior and Tier 2 bonds given strong technical support. Despite challenges, we think the banks have sufficient capital buffers.

Key risks
Key downside risks include 1) wide scale credit asset repricing due to persistent property downturn; and 2) regulatory risks which can include sanctions. An upside risk is stronger-than-expected domestic economic recovery, which should support asset quality and balanced loan growth.

Hong Kong banks

FY23 results
Our covered Hong Kong banks reported NIM expansion of 16-49bps in FY23, resulting in PPoP rising by 11–34% (except for Dah Sing Bank, which was weighed down by its cost-to-income ratio). However, mainland China property-related loans drove credit costs higher, with CWB Wing Lung, Nanyang Commercial Bank, and CITIC Bank International reporting credit costs of 215bps, 105bps, and 126bps, respectively. NPL ratios worsened across the board, ranging from 1% to 2.7%, with non-performing Hong Kong loans on the rise, reflecting sluggish domestic economic growth and concerns over commercial real estate (CRE). Provision coverage ratios took another step down, with some falling into the uncomfortable 20–40% territory. CET1 ratios mostly improved, helped by reduced or flat RWAs.

Key credit drivers
Peaking NIMs and challenged loan growth: Our expectations for the Federal Reserve to lower interest rates this year should translate into peaking NIMs for Hong Kong banks. In addition, loan growth remains challenging due to a lack of demand, coupled with the banks' cautious stance. As such, we expect earnings to be constrained.

Property sector exposure and continued provisioning: The mainland China property sector will still be a key driver of credit cost. The banks with high exposure to mainland China loans include CMB WL (42%), NCB (37%), BEA (33%), and Chong Hing Bank (31%). The Hong Kong commercial real estate (CRE) sector is also starting to show signs of stress as vacancy rates rise and rents fall. Hong Kong banks will likely continue reporting elevated provisions as coverage ratios have fallen for three consecutive years.

Investment view
We like select Hong Kong banks' TLAC and Tier 2 bonds. We take comfort from their high capital ratios which should buffer asset quality deterioration.

Key risks
A key downside risk is a worse-than-expected property downturn in mainland China and stress in the Hong Kong CRE sector, which may result in higher NPL formation. A key upside risk is a faster-than-expected recovery in mainland China's property sector, which should stabilize the asset quality of Hong Kong banks.

Indian banks

FY23 results
Indian private banks (Axis, ICICI) reported resilient FY23 earnings driven by NIM expansion and robust loan growth. HDFC bank merged with HDFC Limited in July 2023 and reported stable metrics after the merger. State-owned State Bank of India saw NIMs decline as its cost of funds rose quicker than loan yields, and earnings were affected by one-off wage provisions.

Asset quality trends were encouraging, with marked declines in NPL ratios while provision coverage ratios remained stable. Capitalization declined across all covered banks due to: 1) regulatory changes affecting risk weights on personal and credit card loans; and 2) robust loan growth (14–22%).

Key credit drivers
Funding costs to constrain NIMs: Indian banks may have to increase deposit rates to raise funding in order to support robust demand for loans. This could cap NIMs going forward if loan yields do not rise in tandem with funding costs. Banks will need to balance between pursuing higher-yielding retail loans versus the higher risk weightings that these loans now attract.

Capital management in focus: With higher risk weightings on several loan categories and higher risk-weighted assets overall, Indian banks will need to manage CET1 ratios prudently. Within our coverage, SBI has the lowest CET1 ratio, but it also enjoys the highest probability of state support due to its 57% government ownership.

Investment view
We think Indian bank senior bonds are fairly valued, and like HDFC's floating rate 2026 senior bond currently as the quarterly coupon reset serves as a hedge against a higher rate scenario.

Key risks
A key downside risk is a rapid increase in funding costs as Indian banks compete for deposits to bolster lending activities. A key upside risk is India's economic growth, which is expected to be a tailwind for bank asset quality and loan growth.

Indonesian banks

FY23 results
Indonesian banks under our coverage recorded solid profitability in FY23 as earnings grew between 14% and 34%. NIM trends varied as Bank Mandiri maintained a stable NIM while BNI and BTN witnessed compressions. All three banks registered healthy loan growth ranging from 7% to 16%, which boosted net interest incomes. Indonesian banks also cut back on provisioning in 2023 as asset quality improved, with NPL ratios declining 40–70bps during the year. Of the three banks, BTN had the weakest asset quality (NPL at 3%, provision coverage at 155%), primarily from its concentrated housing loan exposure due to its policy role of supporting government housing programs. Capitalization metrics for Indonesian banks under our coverage remained sound, with CET1 ratios strengthening to 17.5–20.5%.

Key credit drivers
Sustained loan growth: Indonesian bank profitability will largely depend on whether recent healthy loan growth can be sustained, especially as NIM compression is likely to continue with Bank Indonesia expected to cut rates this year.

Policy continuity: As Prabowo Subianto has been formally declared as Indonesia's next president, this should entail policy continuity, which should be supportive for Indonesian banks.

Investment view
On the credit front, Indonesian bank bonds are trading at fairly tight valuations, a clear reflection of their healthy credit fundamentals. As such, we have Fair ratings on most of the senior bonds of Indonesian banks under our coverage. We like select short-dated Tier 2 notes for yield enhancement. We think investors who seek stable carry with low volatility can consider Indonesian bank credits given their steady fundamentals and short tenors.

Key risks
Key downside risks for Indonesian banks include sharp NIM compressions, and steep declines in loan growth in the event of a significant slowdown in the Indonesian economy. A key upside risk is stronger-than-expected economic growth in Indonesia, which should boost loan formation and augment asset quality.

South Korean banks

FY23 results
Our covered South Korean banks reported relatively resilient metrics in FY23, and their pre-provision operating profit rose 2–20%. However, the banks took larger provisions as a pre-emptive measure against a weakening economic backdrop and domestic real estate project financing loan exposure. Net interest margins were stable to marginally lower, except for Kookmin Bank which saw its NIM rise 10bps to 1.83%. NPL ratios worsened at Hana Bank (+5bps to 0.25%) and Kookmin Bank (+11bps to 0.3%), but all South Korean banks continued to report ratios well below the Asian bank averages. Also, provision coverage ratios at these two banks declined, but remained above 200% of NPLs. CET1 ratios were also higher across the board, rising 40–150bps to 13.2–16.1%.

Key credit drivers
Real estate project finance: With declining property prices in South Korea and media reports of developers unable to service debt, Korean banks have come under scrutiny for their real estate project financing loan exposure. As of September 2023, our covered banks had between 0.5% and 1.7% of loans exposed to real estate project finance although precise delinquency rates have not been reported. If the Korean property sector continues to deteriorate, we could see an uptick in NPLs (although from a low base).

Investment view
We continue to favor South Korean banks' subordinated bonds, which offer yield pickup versus senior notes. Compared with their Asian bank peers, South Korean banks abide by a more stringent version of Basel III capital amortization rules, in which capital amortization for their Tier 2 bonds start five years before the call or maturity date. This effectively reduces the risk of non-call as the bonds do not have any capital value past the first call date.

Key risks
A key downside risk for South Korean banks is further weakness in the counrry's housing market, which may result in higher NPL formation. A key upside risk is a sustained recovery in South Korea's real estate sector, which should boost the asset quality of the country's banks.

Singapore banks

FY23 results
All three Singapore banks reported robust FY23 earnings, with pre-provision operating profit growing 26–30%. Earnings were driven by the continued expansion of NIMs (+23–40bps) during the year although we think NIMs are likely to have peaked. This allowed the banks to increase provisions while keeping capital ratios robust. Loan growth was tepid, with banks reporting 0.4–0.6% increases in gross

loans. Asset quality improved across the board, with NPL ratios declining 2–20bps, coupled with healthier provision coverage ratios.

Key credit drivers

Capital management: Strong earnings growth and tepid loan growth kept CET1 ratios stable or improving, which prompted the banks to increase dividend payouts in 2023. We expect the banks to manage their capital ratios prudently and keep CET1 ratios above 13%.

Peaking NIMs and lower provision coverage ratios: Our expectations for the Federal Reserve to lower interest rates this year should translate into peaking NIMs for Singapore banks although this might not be apparent as loan yields take time to adjust. Peaking NIMs could result in lower earnings growth in 2024 with smaller buffers for provisions. However, we think asset quality is likely to remain sound and see current provisions as adequate.

Investment view

Singapore banks' subordinated debt continue to be well sought after by investors as the banks remain fundamentally sound and yields are relatively attractive relative to the banks' credit ratings. The Tier 2 bonds offer decent yields with relatively short durations.

Key risks

A key downside risk for Singapore banks is a sharp slowdown in the domestic economy, leading to higher NPL formation and weaker asset quality. A key upside risk is stronger-than-expected economic growth in Singapore, which should boost asset quality and enhance profitability for Singapore banks.

Thai banks

FY23 results

Thai banks under our coverage posted robust FY23 results, bolstered by higher NIMs (+30–60bps) which boosted profitability and more than offset weaker non-interest income. Loan growth was tepid, with the banks adopting a more prudent approach toward loan disbursement. Asset quality strengthened, with NPL ratios largely declining in 2023, except for Kasikornbank where NPLs remained flat. There was a spike in credit costs at Kasikornbank and KTB, with the former continuing to clean up its balance sheet and the latter dealing with one large loan delinquency. Provision coverage remained ample, with provision coverage ratios ranging from 150% to 300%. Capitalization metrics improved in 2023, with CET1 ratios in the 15–17% range.

Key credit drivers

Peaking NIMs: With the Thai central bank under pressure to cut rates in the near term, we think net interest margins are likely to peak for Thai banks this year, which may curtail profitability.

Loan growth uncertainty: With total loans for our covered Thai banks declining marginally in 2023, it remains to be seen if loan disbursement can pick up in 2024 to drive top-line growth.

Credit costs: Credit costs may remain elevated as the banks continue to clean up their loan books amidst stronger profitability.

Investment view

Within the Thai banking space, we retain our preference for Tier 2 bonds over senior bonds as we view the spread pickup as attractive in the context of stable credit profiles. As such, for quality Thai banks under our coverage, we are willing to take on subordination risk for yield enhancement. We thus have Attractive ratings on select Tier 2 instruments issued by our covered Thai banks.

Key risks

A key risk for Thai banks is a sharp slowdown in the domestic economy, exacerbated by already high household debt. A key upside risk is stronger-than-expected loan growth which augments profitability.

Table 15 - Selection of Asia USD bonds

CIO View	ISIN	Issuer	Cpn (%)	Maturity	Next Call Date	Subordination	Ask Price	YTM (%)	YTC (%)	Rating (Mdy's/S&P)	Coupon Reset
China IG SOE											
Fair	XS2471127584	China Great Wall AMC	4.250	4/28/2025	3/28/2025	Sr Unsecured	98.7	6.0	6.2	-/NR	
Fair	XS2281795075	China Cinda AMC	1.875	1/20/2026	10/20/2025	Sr Unsecured	95.0	5.4	6.1	-/BBB+	
Fair	US09681MAB46	BOC Aviation	3.875	4/27/2026	1/27/2026	Sr Unsecured	97.8	5.2	5.4	-/A-	
Fair	XS1515240015	China CITIC Financial AM (Huarong)	4.875	11/22/2026		Sr Unsecured	97.5	6.1		-/BBB-	
Fair	XS2408001365	Sinochem HK	2.250	11/24/2026	10/24/2026	Sr Unsecured	93.6	5.2	5.3	A3/A-	
Fair	XS2757520452	China Orient Asset Management	5.500	2/1/2027	11/1/2026	Sr Unsecured	99.8	5.6	5.6	-/BBB	
Fair	XS1721386917	China State Construction Intl	3.875	11/29/2027		Sr Unsecured	94.8	5.6		Baa2/-	
Fair	XS2455411558	Power Construction Corp Of China	4.250	Perpetual	1/14/2027	Subordinated	97.1	8.1	5.5	Baa2/-	H15T5Y + 4.575%
Attractive	XS2824215425	Shandong Hi-Speed Group	6.500	Perpetual	5/30/2027	Sr Unsecured	102.3	8.3	5.6	A3/-	H15T3Y + 4.781%
China IG POE											
Attractive	US056752AG38	Baidu Inc	4.125	6/30/2025		Sr Unsecured	99.0	5.2		A3/-	
Fair	US88032XAM65	Tencent Holdings	3.575	4/11/2026	2/11/2026	Sr Unsecured	97.7	5.0	5.1	A1/A+	
Fair	USY5257YAL12	Lenovo Group	5.831	1/27/2028	12/27/2027	Sr Unsecured	102.2	5.1	5.1	Baa2/BBB	
Fair	US01609WAR34	Alibaba Group Holding	4.500	11/28/2034	5/28/2034	Sr Unsecured	94.7	5.2	5.2	A1/A+	
Attractive	US88032XAH70	Tencent Holdings	3.925	1/19/2038	7/19/2037	Sr Unsecured	86.2	5.4	5.4	A1/A+	
Attractive	US01609WAV46	Alibaba Group Holding	4.200	12/6/2047	6/6/2047	Sr Unsecured	81.5	5.6	5.6	A1/A+	
Hong Kong IG											
Fair	XS1341169867	Swire Properties	3.625	1/13/2026		Sr Unsecured	97.9	5.1		A2/NR	
Fair	XS1691798240	Nan Fung International	3.875	10/3/2027		Sr Unsecured	94.4	5.8		-/BBB-	
Fair	XS2055636109	Hong Kong Telecommunications	3.250	9/30/2029		Sr Unsecured	92.6	4.9		Baa2/BBB	
Attractive	XS2099130382	Sun Hung Kai Properties	2.875	1/21/2030		Sr Unsecured	90.3	4.9		A1/A+	
Attractive	USG4672CAC94	CK Hutchinson	7.450	11/24/2033		Sr Unsecured	116.4	5.2		A2/A	
Attractive	XS2264054706	Airport Authority HK	2.100	Perpetual	3/8/2026	Sr Unsecured	95.2	8.3	5.2	-/AA	H15T5Y + 4.697%
Attractive	XS2328261263	AIA Group	2.700	Perpetual	4/7/2026	Subordinated	94.9	5.9	5.9	A2/-	H15T5Y + 1.758%
Attractive	XS2423359459	Bank of East Asia	4.875	4/22/2032	4/22/2027	Subordinated	96.3	6.4	6.4	Baa2/BBB-	H15T5Y + 2.3%
Attractive	XS2701169901	Dah Sing Bank	7.375	11/15/2033	11/15/2028	Subordinated	105.7	6.4	5.9	Baa1/-	H15T5Y + 2.95%
Indonesia IG											
Fair	US455780DT06	Republic of Indonesia	4.400	3/10/2029	2/10/2029	Sr Unsecured	98.1	4.9	4.9	Baa2/BBB	
Attractive	US71568QAL14	Perusahaan Listrik Negara	3.375	2/5/2030		Sr Unsecured	90.7	5.3		Baa2/BBB	
Fair	USY7140WAC20	PT Indonesia Asahan Aluminium (Inalum) / MIND ID	6.530	11/15/2028		Sr Unsecured	104.4	5.4		Baa2/-	
Fair	USY7141BAB90	PT Freeport Indonesia	5.315	4/14/2032	1/1/2032	Sr Unsecured	98.5	5.6	5.6	Baa3/-	
Attractive	XS2390472624	Tower Bersama Infrastructure	2.800	5/2/2027	11/2/2026	Sr Unsecured	92.9	5.6	6.2	-/-	
India IG											
Fair	US74947MAD48	REC Ltd	5.625	4/11/2028		Sr Unsecured	101.3	5.2		Baa3/-	
Attractive	XS2051369671	Power Finance Corp	3.900	9/16/2029		Sr Unsecured	93.6	5.3		Baa3/-	
Fair	USY72570AS69	Reliance Industries	2.875	1/12/2032		Sr Unsecured	85.7	5.2		Baa2/BBB+	
Fair	XS1753595328	Tata Steel	5.450	1/24/2028		Sr Unsecured	99.8	5.5		-/BBB- *+	
Korea IG											
Attractive	XS2716680744	Export-Import Bank of Korea	6.249	11/21/2028		Sr Unsecured	101.6	5.8		Aa2/AA	SOFR + 0.88%
Fair	US50066RAD89	Korea National Oil Corp	2.500	10/24/2026		Sr Unsecured	94.8	5.0		Aa2/AA	
Attractive	USY4899GFA68	Korea Hydro & Nuclear Power	4.250	7/27/2027		Sr Unsecured	98.2	4.9		Aa2/AA	
Attractive	US500630DX39	Korea Development Bank	4.375	2/15/2033		Sr Unsecured	96.8	4.8		Aa2/AA	
Fair	USY8085FBK58	SK hynix Inc	6.375	1/17/2028		Sr Unsecured	103.6	5.2		Baa2/BBB-	
Attractive	US82460EAR18	Shinhan Bank	4.375	4/13/2032		Subordinated	93.2	5.5		Baa1/BBB+	
China HY											
Fair	XS2098539815	Longfor Properties	3.375	4/13/2027		Sr Unsecured	80.8	11.8		Ba3/BB	
Hong Kong HY											
Fair	XS2435611327	New World Development	6.150	Perpetual	3/16/2025	Sr Unsecured	96.6	10.4	11.8	-/-	H15T3Y + 6.201%
India HY											
Fair	USY2R40TAB40	Delhi Intl Airport	6.450	6/4/2029		1st lien	100.9	6.2		B1/BB-	
Fair	XS2350621517	Tata Motors	4.350	6/9/2026	8/19/2024	Sr Unsecured	96.7	6.2	81.7	-/BB+ *+	
Indonesia HY											
Attractive	USY5951MAA00	Medco Energi	8.960	4/27/2029	10/27/2025	Sr Unsecured	105.7	7.5	7.5	B1/BB-	
Fair	XS2327392234	Pakuwon Jati	4.875	4/29/2028	4/29/2025	Sr Unsecured	95.1	6.4	15.0	Ba1/BB+	
Attractive	XS2314514477	Bank Negara Indonesia	3.750	3/30/2026		Subordinated	96.1	6.2		Ba2/-	
Macau HY											
Attractive	USG5975LAC03	Melco Resorts Finance	5.250	4/26/2026	8/19/2024	Sr Unsecured	97.1	7.0	44.5	Ba3/BB-	
Fair	XS2289202587	SJM	4.500	1/27/2026	7/29/2024	Sr Unsecured	96.4	7.0	958.6	B1/-	
Attractive	USG85381AF13	Studio City Finance	6.500	1/15/2028	8/19/2024	Sr Unsecured	95.8	7.9	87.5	B1/B+	
Attractive	USG98149AH33	Wynn Macau	5.625	8/26/2028	7/29/2024	Sr Unsecured	94.9	7.1	424.6	B1/BB-	

Source: UBS, as of 19 July 2024 06:30 GMT. Yield-to-call as calculated by UBS. Indicative pricing only.

Asia Pacific bonds

12 month rating history

ISSUER_LEGAL_NAME	ISSUER_NAME	PREVIOUS_ISSUER_VALUATION_VIEW	ISIN	PREVIOUS_BOND_RECO
CHINA GREAT WALL ASSET MANAGEMENT CORPORATION	CN GT WALL INTL		XS2471127584	Fair (2023-08-21)
REC LTD	REC		US74947MAD48	Attractive (2023-09-04)
CHINA GREAT WALL ASSET MANAGEMENT CORPORATION	CN GT WALL INTL		XS2471127584	Expensive (2023-11-20)
REC LTD	REC		US74947MAD48	Fair (2023-07-31)
SUN HUNG KAI PROPERTIES	SHK PROP.(CAP MRKT)		XS2099130382	Fair (2023-11-20)
PLN	PERUSAHAAN LISTRIK		US71568QAL14	Attractive (2023-09-04)
PLN	PERUSAHAAN LISTRIK		US71568QAL14	Fair (2023-07-31)
WYNN MACAU	WYNN MACAU		USG98149AH33	Attractive (2023-08-14)
PT FREEPORT INDONESIA	FREEPORT ID		USY7141BAB90	Fair (2023-08-21)
DAH SING BANK	DAH SING BANK		XS2701169901	Fair (2023-12-11)
BOC AVIATION	BOC AVIATION		US09681MAB46	Attractive (2023-08-21)
BANK OF EAST ASIA	BK OF EAST ASIA		XS2423359459	Fair (2024-02-23)
PT FREEPORT INDONESIA	FREEPORT ID		USY7141BAB90	Fair (2024-04-29)
LONGFOR PROPERTIES	LONGFOR GRP		XS2098539815	Fair (2023-10-23)
REC LTD	REC		US74947MAD48	Attractive (2024-04-29)
WYNN MACAU	WYNN MACAU		USG98149AH33	Fair (2024-01-08)
PLN	PERUSAHAAN LISTRIK		US71568QAL14	Fair (2024-03-18)
REC LTD	REC		US74947MAD48	Fair (2024-03-18)
PT FREEPORT INDONESIA	FREEPORT ID		USY7141BAB90	Attractive (2024-03-18)
RELIANCE INDUSTRIES	RELIANCE INDUSTRIES		USY72570AS69	Fair (2024-03-18)
CK HUTCHISON	HUTCHISON WHAMPOA		USG4672CAC94	Fair (2023-10-30)
KOREA HYDRO & NUCLEAR POWER CO LTD	KHNP		USY4899GFA68	Fair (2024-01-16)
MEDCO ENERGI	MEDCO MAPLE		USY5951MAA00	Fair (2024-03-18)
RELIANCE INDUSTRIES	RELIANCE INDUSTRIES		USY72570AS69	Attractive (2024-06-24)
RELIANCE INDUSTRIES	RELIANCE INDUSTRIES		USY72570AS69	Attractive (2023-10-30)
STUDIO CITY	STUDIO CITY FIN		USG85381AF13	Fair (2024-01-29)
LONGFOR PROPERTIES	LONGFOR GRP		XS2098539815	Expensive (2024-05-21)
MELCO RESORTS FINANCE	MELCO RESORTS		USG5975LAC03	Fair (2024-07-08)
PT FREEPORT INDONESIA	FREEPORT ID		USY7141BAB90	Attractive (2024-05-28)
PT TOWER BERSAMA INFRASTRUCTURE TBK	TOWER B INFRA		XS2390472624	Fair (2024-05-21)
SJM HOLDINGS	CHAMPION PATH		XS2289202587	Attractive (2024-07-08)
PT BANK NEGARA INDONESIA (PERSERO) TBK	BK NEGARA INDONESIA		XS2314514477	Fair (2024-07-08)
ALIBABA GROUP HOLDING LIMITED	ALIBABA GRP		US01609WAR34	Fair (2024-07-15)
TENCENT HOLDINGS LIMITED	TENCENT HLDG		US88032XAM65	Fair (2024-07-16)
POWER FINANCE CORPORATION	POWER FINANCE		XS2051369671	Fair (2024-06-10)
SHANDONG HI-SPEED GROUP	COASTAL EMER		XS2824215425	Attractive (2024-07-15)

UBS CIO risk views

Credit risk flags

CIO attaches a credit risk flag to the instruments under its coverage. Credit risk is assessed based on the remaining tenor and / or instrument type. The flag indicates the likelihood that a holder of the instrument will not receive a coupon or principal payment when it comes due. For subordinated and hybrid instruments, which are usually callable and have a remote or no fixed maturity date, we apply one uniform credit risk flag per issuer and instrument type. The idea is to reflect the possibility of contractual trigger events or regulatory intervention occurring. Either can impose losses on bondholders regardless of the remaining term of the instrument or a specific issuer default event. Credit risk flags only indicate our view of the riskiness of a particular instrument. Credit risk flags should not be seen as recommendations to buy, hold or sell. In fact, any combination of risk flags and relative value recommendations is possible.

Very low credit risk

We believe that the probability of debt payments not being made when they come due is very low (cumulative probability of less than 2%).

Medium credit risk

We believe that the probability of debt payments not being made when they come due is low to medium (cumulative probability of non-payment between 2% and less than 20%).

High credit risk

We believe that the probability of debt payments not being made when they come due is at least one in five cumulatively.

UBS credit rating

The UBS credit rating reflects our view of the creditworthiness of a company (consistent with our risk flags) and represents a long-term (senior) debt rating. The symbols are similar to those of rating agencies but UBS credit ratings solely reflect UBS's opinion, and are distinct from evaluations assigned by rating agencies. The UBS credit rating is not a recommendation to buy, hold or sell a particular bond, nor is it reflective of market pricing and/or market sentiment. All combinations of a credit rating and relative valuation recommendations are possible.

Issuer credit outlook

We complement the instrument-specific risk information of the credit risk flags by indicating our outlook for the credit quality of an issuer over the next 12 months. Depending on instrument pricing, all combinations of an issuer credit outlook and relative valuation recommendations are possible.
Improving: We expect the credit profile of the issuer to improve, to an extent that may result in upgrades by rating agencies.
Stable: We do not expect the credit profile of the issuer to change meaningfully.
Deteriorating: We expect the credit profile of the issuer to deteriorate, to an extent that may result in downgrades by rating agencies.
Note that the credit views in this report are those of UBS Financial Services and may differ from those of other parts of UBS regarding the same issuer.

UBS CIO valuation views

Relative value bond recommendations

Our relative value bond recommendations are based on an average investment horizon of six to 12 months. They reflect our assessment of a bond's attractiveness relative to comparable instruments under CIO coverage. Comparable instruments typically exhibit similar credit quality, are denominated in the same currency, and belong to the same segment of the bond market.
Views on a particular instrument can change within the six- to 12-month time frame, and those that apply to one instrument do not necessarily apply to others of the same issuer. Views on a particular instrument may be withdrawn if it does not have a sizeable basket of comparable instruments under CIO coverage.

Attractive Bonds seen as "attractive" are expected to generate a total return exceeding the average return of comparable instruments. Our recommendation can stem from a positive view on the issuer's credit profile not fully reflected in the price, unduly high risk premiums, our take on an instrument's call probability, the risk of coupon deferrals, and external factors including regulatory intervention.

Fair Bonds seen as "fair" are expected to produce a total return broadly in line with the average return of comparable instruments.

Expensive Bonds seen as "expensive" are expected to earn a total return that is less than the average return of comparable instruments. Our recommendation can stem from a negative view on the issuer's credit profile not fully reflected in the price, unduly tight risk premiums, our take on an instrument's call probability, the risk of coupon deferrals, and external factors including regulatory intervention.

Sell recommendations

Sell A Sell recommendation is assigned when the risk of an adverse outcome for an instrument exceeds what is reflected in its current valuation. Such situations can include those in which the instrument appears likely to post negative total returns until redemption, either due to a highly negative yield to maturity or an imminent call at a price below market valuations.

For Credit Suisse clients

Please note that Credit Suisse channels might temporarily display a different rating terminology when referencing UBS CIO bond recommendations.

While terminology might differ due to technical limitations, the definitions of the UBS valuation methodology apply.

UBS bond recommendation	Credit Suisse channels
Attractive	Buy
Fair	Neutral
Expensive	*no equivalent in CS channels*
Sell	Sell

For more information about our present and past recommendations, please contact ubs-cio-wm@ubs.com.

In addition to the relative value bond recommendations, CIO provides issuer valuation views for selected issuers from developed countries. Large, frequent issuers often provide a relatively consistent bond curve in their main issuing currencies. A general valuation view on them provides useful guidance when constructing a bond portfolio or assessing new issues. Issuer valuation views cannot simply be broken down to the instrument level. Any combination of our credit risk flags and issuer valuation views is generally possible. Issuer views do not restrict CIO from having different valuation views on individual bonds.
Preferred list: Bonds of issuers on our Preferred list are generally expected to offer a more attractive relative valuation than those of similarly rated peers.
Core list: Bonds of issuers on our Core list are generally expected to generate total returns in line with those of similarly rated peers. Core issuers offer relatively liquid bond curves and comparatively stable credit profiles.
Avoid list: Bonds of issuers on our Avoid list are generally expected to offer a less attractive relative valuation than those of similarly rated peers. The decision to include an issuer on the Avoid list reflects, in most cases, relative value considerations, which can but do not have to be based on an expected deterioration in credit quality. As long as we have not issued a Sell recommendation existing positions may be held.

For details please see "Understanding bonds: A guide to CIO's credit offering", published 16 April 2021.

Statement of Risk
Fixed income - Bond market returns are difficult to forecast because of fluctuations in the economy, investor psychology, geopolitical conditions and other important variables. Corporate bonds are subject to a number of risks, including credit risk, interest rate risk, liquidity risk, and event risk. Though historical default rates are low on investment-grade corporate bonds, perceived adverse changes in the credit quality of an issuer may negatively affect the market value of securities. As interest rates rise, the value of a fixed-coupon security will likely decline. Bonds are subject to market value fluctuations, given changes in the level of risk-free interest rates. Not all bonds can be sold quickly or easily on the open market. Prospective investors should consult their tax advisors concerning the federal, state, local, and non-US tax consequences of owning any securities referenced in this report.

Appendix

Contact
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Version B/2024. CIO82652744