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Cash wanted

Fabiano Santin writes:

Highlights of last week's SoftBank Group Corp. March 31 fiscal year-end news dump were a two-for-one stock split and the doubling of the dividend yield, to 0.8%. Given that the new payout will return more than the yield on 30-year Japanese government bonds (all of 0.5%) and cost less than $900 million a year (immaterial relative to SoftBank's $100 billion market cap), it looks like a promising plan to seduce yield-starved Japanese savers.

SoftBank (9984 on the Tokyo Stock Exchange and SFTBY in the American pink sheets) is the topic at hand. Analysis of financial results and of CEO Masa Son's latest plans to conquer the world (and the threats thereto) are the subtopics. To anticipate, we remain bearish on this global avatar of growth-at-any-cost.

Since the opening *Grant's* salvo of Dec. 15, 2017, shares are up by 12%. This year's 27% rally in Alibaba Group Holding, Ltd. (BABA on the Big Board), SoftBank's top position—it represents just about half of SoftBank's assets—has been the principal bullish driver. The SoftBank treasury department has likewise pitched in, as the stock took off in February with the announcement of a ¥600 billion ($5.4 billion) buyback program (64% completed as of May 8).

Masa Son needs a strong share price to placate the lenders who see him divesting older, slow-growing investments—for instance, $4.8 billion worth of shares in Yahoo! Japan Corp.—to make room for unicorns. Whatever the promise of these VC-funded startups, for the most part they burn cash rather than pay it. Something else that Masa Son needs, both he and his creditors agree, is the next Alibaba.

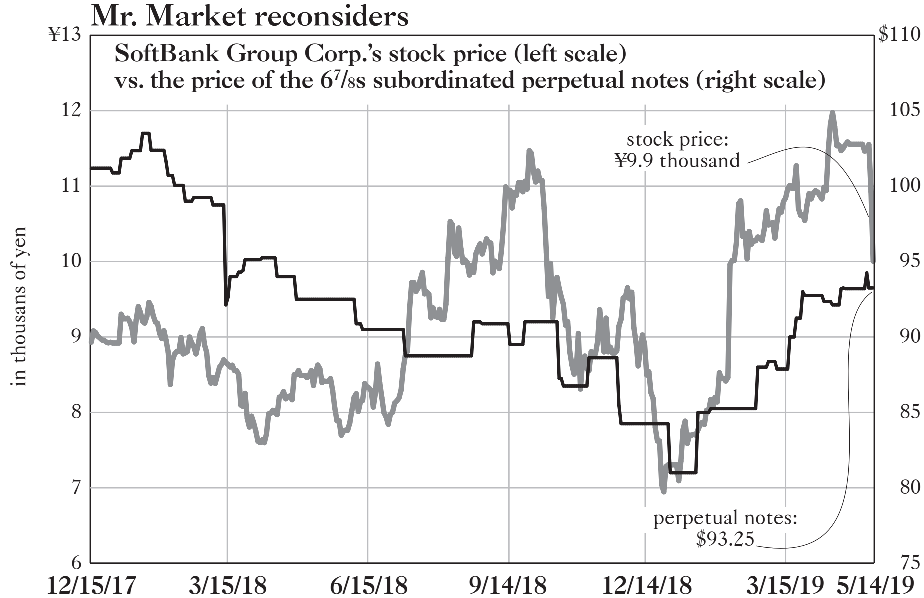
Last month, *The Wall Street Journal* reported that SoftBank's Vision Fund was trying to raise money from new investors, which is odd given that that vehicle has yet to deploy fully its $97 billion in committed capital. Then, too, there is capital still to be called from existing investors. The *Journal* also reported that there was talk about listing the fund itself. Such circumstances, including the debut of several Vision Fund stakes in recent and prospective initial public offerings, raise questions about SoftBank's liquidity.

Supposedly non-recurring, one-time items blur SoftBank's consolidated operating results. For instance, excluding the Vision Fund, operating income increased by ¥96.5 billion ($880 million) year-over-year to ¥1.1 trillion ($10 billion). But don't be misled by those large figures. They do not represent cash that is available to shareholders.

One must bear in mind that $6.5 billion of the $10 billion in consolidated operating income came from SoftBank's 66.5%-owned Japanese telecom subsidiary. But that unit generated only $2.6 billion in free cash flow, i.e., funds that could be distributed as dividends. Tax considerations and high capital expenditures, not to mention the threat posed by increasing competition, keep most of the $6.5 billion on ice (*Grant's*, Nov. 30).

Another $2.5 billion came from SoftBank's 84.4%-owned Sprint Corp. seg-

Mr. Market reconsiders



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ment, which is itself a drain on owners' coffers. In April, Sprint told U.S. regulators that it misreported the number of customer lines it had been signing up and that its performance was not so strong as it first appeared. The quarter ended March 31 was the third in a row of post-paid subscriber losses (minus 189,000 subscribers vs. the expected drop of 117,000).

Including payments for handset financing, Sprint had a cash burn of $539 million in that quarter, according to estimates by Craig Moffett, one-half of the eponymous research firm MoffettNathanson, LLC. "A debt restructuring in Sprint's case isn't only possible, it seems to us to be, by far, the most likely path forward if the deal is rejected," Moffett writes in a May 7 report. SoftBank's stake in Sprint is worth $20 billion at current market price, or 20% of SoftBank's market cap.

The Vision Fund reported operating income of ¥1.2 trillion ($10.9 billion) for the fiscal year ended March 31, mostly driven by ¥1 trillion ($9.1 billion) in unrealized gains from the valuation of investments including Uber ($3.8 billion), Guardant Health ($1.8 billion) and OYO ($1.4 billion). But after the IPO flop, the Vision Fund's stake in Uber is worth about $8.6 billion, not much more than the $7.7 billion it cost to acquire the shares. It's unclear what type of lockup agreement, if any, SoftBank may have with Uber underwriters, which could prevent it from dumping the stock in the market.

SoftBank has $63.5 billion in debt (excluding non-recourse subsidiary debt) and carries $25.6 billion in cash (including expected proceeds from the sale of that stake in Yahoo! Japan). But there are still $15.6 billion in capital commitments to the Vision Fund that have yet to be called, which may explain some of the recent moves to raise cash. Assuming that all unicorns, Arm and other publicly listed assets are correctly valued by SoftBank, the company's loan-to-value ratio stands at a relatively low 26%.

From a different perspective, considering only the earnings before interest, tax, depreciation and amortization of SoftBank's 66.5% stake in the Japanese telecom subsidiary, which is its most relevant, majority-owned, cash-generative business, the company's net leverage stands at 5.2 times, or 8.7 times on a gross basis. Thus, absent a path to solid profitability for its numerous unicorns, SoftBank is leveraged to the goodwill of capital markets—and of the People's Republic of China.

Apropos of the capital markets, *The Wall Street Journal* on Tuesday quoted "bankers" who said they were keen to continue lending to "the world's largest technology investor." Why was that?

"One reason is the big fees a relationship with SoftBank can bring in," the *Journal* continued, "especially the hundreds of millions of dollars in investment banking fees generated each year by Chief Executive Masayoshi Son's constant stream of deals."

The "bankers" were unnamed, but could Chuck Prince—the former Citigroup, Inc. chief who, a dozen years ago, would dance for as long as the music was playing—possibly be among them?

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