Global Markets Research

Fixed Income

Fixed Income Daily Market Snapshot

UST		
Tenure	Closing (%)	Chg (bps)
2-yr UST	2.93	2
5-yr UST	3.06	3
10-yr UST	3.23	3
30-yr UST	3.44	2

	MGS		GII*	
Tenure	Closing (%)	Chg (bps)	Closing (%)	Chg (bps)
3-yr	3.69	3	3.76	0
5-yr	3.80	1	3.91	0
7-yr	4.09	6	4.11	0
10-yr	4.14	8	4.25	0
15-yr	4.62	5	4.58	0
20-yr	4.82	5	4.79	0
30-yr	4.95	4	4.95	0

** Market indicative levels*

MYR IRS Levels		
IRS	Closing (%)	Chg (bps)
1-yr	3.71	0
3-yr	3.79	0
5-yr	3.89	1
7-yr	3.99	0
10-yr	4.20	0

Source : Bloomberg

Upcoming Government Bond Tender

Nil

US Treasuries

- US Treasuries ended weaker as overall benchmark yields ended 2-3bps higher as investors and traders looked forward to digesting the incoming results of the mid-term election results despite decent 10Y auction which notched a BTC ratio of 2.54x; averaging 3.209%. The benchmark 2Y ended at 2.93% whilst 10Y rose 3bps at 3.23%. (Note: At the time of writing however US stock futures are erasing losses whilst UST's edge higher as the Dollar slips). Interestingly, Republicans adding to their Senate majority would offer an extra layer of protection for Trump's Tax Cuts. Hence it is believed that controlling both Houses would boost expectations for tax-cut extensions and possibility drive interest rates higher.

MGS/GII

- Trading momentum in Govvies was tepid on Monday following the release of Budget 2019 and ahead of the Diwali mid-week break and incoming mid-term election in the US. Total volume was at a mere RM749m. Some investor interest was seen in the off-the-run 19's and 3Y GII bonds. Overall benchmark yields ended 1-8bps higher with odd-lot trades seen across the 10-30Y tenures. The 5Y MGS 4/23 edged 1bps higher at 3.80% whilst the 10Y MGS 6/28 spiked 8bps to 4.14%. GII bond trades dropped to 16% of overall trades. Up next on the data front are the Foreign Reserves numbers expected out today followed by the OPR decision tomorrow

Corp Bonds/Sukuk

- Corporate bonds/Sukuk similarly saw volume dissipate ahead of the mid-week break at a mere RM71m. Investors were mainly seen sidelined whist digesting the impact of the Budget 2019 and mid-term elections in US. Some token interest was seen in the AAA-AA-part of the curve with a total of 8 different bonds traded with overall yields ending lower. There were nil trades in the GG-space whereas AAA-rated Suria KLCC 12/24 closed 6bps lower compared to previous-done levels at 4.37%. In the AA-segment; short-tenured Tanjung Bin Power and JEV 19's rallied1-5bps lower between 4.18-21% levels. The banking sector saw RHB Islamic 24nc19 close unchanged at 4.16%

Daily Trades : Government Bonds

Securities		Closing YTM	Vol (RM mil)	Previous YTM	Previous Trade Date (dd/mm/yyyy)	Chg (bp)
MGS	03/19	3.275	64	3.469	11/01/2018	-19
MGS	10/19	3.491	240	3.455	11/02/2018	4
MGS	11/19	3.501	16	3.451	11/02/2018	5
MGS	03/20	3.564	3	3.512	11/02/2018	5
MGS	10/20	3.550	3	3.513	11/02/2018	4
MGS	07/21	3.684	2	3.670	11/01/2018	1
MGS	09/21	3.702	37	3.674	11/01/2018	3
MGS	11/21	3.694	41	3.665	11/02/2018	3
MGS	03/22	3.752	5	3.736	11/02/2018	2
MGS	08/22	3.819	9	3.776	11/02/2018	4
MGS	09/22	3.830	23	3.808	11/02/2018	2
MGS	09/24	4.001	19	4.000	11/02/2018	0
MGS	03/25	4.092	1	4.029	11/02/2018	6
MGS	09/25	4.123	42	4.077	11/02/2018	5
MGS	11/26	4.153	15	4.138	11/01/2018	1
MGS	11/27	4.218	27	4.163	11/01/2018	5
MGS	06/28	4.140	61	4.062	11/02/2018	8
MGS	04/32	4.601	1	4.561	11/01/2018	4
MGS	04/33	4.650	19	4.628	11/01/2018	2
MGS	04/37	4.813	2	4.805	11/01/2018	1
MGS	09/43	4.970	3	4.970	11/01/2018	0
GII	03/22	3.757	100	3.757	11/02/2018	0
GII	07/23	3.969	6	3.917	10/31/2018	5
GII	05/24	4.047	10	4.010	11/02/2018	4
GII	07/27	4.195	1	4.192	11/01/2018	0
			749			

Daily Trades: Corp Bonds / Sukuk

Securities		Rating	Closing YTM	Vol (RM mil)	Previous YTM	Previous Trade Date (dd/mm/yyyy)	Chg (bp)	Spread Against MGS*
Suria KLCC Sdn Berhad	12/24	AAA	4.368	10	4.431	07/27/2018	-6	41
Teknologi Tenaga Perlis Consortium Sdn Berhad	01/20	AA1	4.229	10	4.357	07/24/2017	-13	80
Tanjung Bin Power Sdn Berhad	08/19	AA2	4.179	10	4.230	09/13/2018	-5	75
Kesas Sdn Berhad	10/19	AA2	4.165	5	4.252	02/08/2018	-9	74
Jimah Energy Ventures Sdn Berhad	11/19	AA3	4.210	10	4.224	03/13/2018	-1	78
AmBank Islamic Berhad	03/24	AA3	4.143	10	4.149	10/19/2018	-1	33
RHB Islamic Bank Berhad	05/24	AA3	4.156	15	4.161	10/26/2018	0	20
GENM Capital Berhad	07/23	AAA	4.570	1	4.607	10/30/2018	-4	75
				71				

**spread against nearest indicative tenured MGS (Source : BPAM)*

Market/Corporate News: What's Brewing

NEARLY a year after its big demerger exercise, Sime Darby Bhd remains a work in progress. With its plantation and property businesses spun off, the challenge now is to create more value with what is left. The plan, for group CEO Jeffri Salim Davidson, is clear — continue whipping the group into shape while expanding its core businesses. In his first interview since the demerger in Nov 30 last year, he acknowledges that next to the other Sime Darby companies, the group he leads is "almost an afterthought" to investors. "We are what is left — 100 years' worth of heirlooms and silverware acquired over the group's lifetime, all now left in Sime Darby [after the demerger]," Jeffri jokes, although he is clearly excited about its prospects. The break-up was long anticipated as the conglomerate had publicly acknowledged before that it could unlock value by spinning off some divisions. The larger Sime Darby group had been shackled by a conglomerate discount since the 2007 merger that created it. In general, the diversity of its core businesses made it difficult to sustain a healthy earnings growth trajectory given differing fortunes in any given financial year. The cyclical nature of many of its divisions also posed a hurdle. For example, it worked towards the listing of its motor business back in 2015 but missed the opportunity when market conditions turned. On whether the motor listing is still on the cards, Jeffri says no. He feels that the current structure provides a more substantial offering to shareholders. "What we want to be is a trading company, focusing on motor and industrial. We also have a healthcare arm, which has been run well but which we now need to grow bigger." Apart from the three core focuses, the sprawling "heirlooms and silverware" are diverse. The group has four ports in Shandong, China, as well as a 30% stake in hypermarket chain Tesco Stores (M) Sdn Bhd and 12% equity interest in property developer Eastern & Oriental Bhd. It also has an insurance business. Eventually, Sime Darby will trim away the non-core segments, though it is in no hurry, says Jeffri (see story below). Also part of the group's five-year value creation plan is a continuing drive to optimise cost and enhance recurring revenue. Driving Sime Darby's push for growth is the strong recovery of its industrial division, which had been in a slump since around 2012 due to dampened coal prices. The division is underpinned by its Caterpillar dealership, one of the largest in the world with 131 branches in 15 countries and territories throughout Asia-Pacific. The multi-year slump saw the division's pre-tax profit fall from a high of RM1.35 billion in the financial year ended June 30, 2012 (FY2012), to RM253 million in FY2017 — dragging the wider group's earnings pre-demerger. But the tide is turning. Recovering coal prices of late have released pent-up demand for parts and the servicing of heavy vehicles, which is the first wave of recovery, says Jeffri.In FY2018, the industrial business, primarily based in Australia, saw a pre-tax income surge of 72% year on year to RM434 million while its order book jumped 80% year on year to RM2.7 billion. “To me, the second wave is fleet replacement, so players will buy a new fleet of trucks to replace the old ones. That is coming and we will see that over the next 18 months to two years,” Jeffri explains. “If coal prices continue to be where they are or get better, then the next wave is the opening up of new mines. Then it will be a different ball game because it will not just be replacement capex (capital expenditure) anymore but also new capex for new capacity.” To some extent, the resurgent industrial segment will make up for a tougher road ahead for the motor business.Analysts note that the motor division is facing a more challenging outlook due to intensifying competition in China, its largest market, accounting for 44% of FY2018 sales volume. While its motor division represents more than 30 brands across nine markets in Asia-Pacific, BMW is a key component as Sime Darby is one of the marque’s largest dealers globally. “We are cautious over the motor division, which has seen lower overall volume sales, especially in the Australia and New Zealand region despite ongoing product refreshment,” Maybank Research says in a Sept 3 note, adding that trade tensions may also deter purchases in China. While Sime Darby’s motor business is spread across 18 countries in Asia-Pacific, China is a key market, representing 38% of its FY2018 revenue. The other key region is Australasia, contributing 30% to revenue. Only 15% of group revenue comes from Malaysia, while 70% of its 20,000-strong workforce are based overseas — making Sime Darby a multinational listed on Bursa Malaysia. In FY2018, the group’s net profit moved sideways year on year at RM618 million while revenue rose 8.8% year on year to RM33.83 billion. On concerns that the motor woes may drag group performance in FY2019, Jeffri says he is confident that this will not be the case. While the group’s FY2019 targets are still being finalised, he expects Sime Darby’s bottom line for the year to be “significantly higher”. “I think what will happen is that the industrial division will be very strong and the motor business will be there or thereabouts compared with last year. There may even be a small drop but [it will be] offset by the performance of the industrial division,” says Jeffri. Beyond industrial and motor, Sime Darby is in the mood for mergers and acquisitions, particularly to grow its healthcare business, says Jeffri. Sime Darby has six private hospitals with 1,500 beds between them. Three are in Malaysia while the other three are in Indonesia, all in a 50:50 joint venture with Australian healthcare group Ramsay Health Care. While not set in stone, the group aspires to double the bed count over the next five years. “What we have done really well is improving efficiency and the profits from existing hospitals, but we have not done a great job of growing the number of beds,” says Jeffri. He adds that Sime Darby is eyeing potential healthcare acquisitions in Malaysia and Indonesia as well as in more populous and fast-growing countries in the region such as China, Vietnam and the Philippines. “Of course, valuations are an issue as a lot of hospitals are very expensive from a price-earnings ratio perspective,” he observes, adding that a number of potential deals had fallen through. That said, Sime Darby has plenty of dry powder. Post-demerger, its gross gearing has fallen to 20% based on its annual report and Jeffri indicates that a comfortable upper limit is about 40%. A back-of-the-envelope calculation shows that gearing up to 40% would raise about RM2.9 billion. That is on top of an existing cash pile of RM1.67 billion. Also on Sime Darby’s radar is to build on its new BMW engine assembly capability. Recall that it opened a RM132 million facility in Kulim, Kedah, back in May. The second BMW engine assembly facility in Southeast Asia, the plant has a 10,000-engine capacity and had assembled 1,800 engines between April and September — 20% more than scheduled. By June 2019, the plant is expected to have assembled 6,000 BMW engines, Jeffri says, adding that the possibility of Sime Darby assembling engines for other car brands has not been ruled out. “Yes, we are talking to some of the other carmakers. We have the capacity and quite a few car manufacturers are not selling CKD (completely knocked down) vehicles in Malaysia yet, so there is an opportunity,” he says without elaborating further. Planned asset disposals may boost dividends. or investors keen on Sime Darby’s ongoing asset monetisation drive, this may present a buying opportunity since upcoming divestments may yield more special dividends. When asked, group CEO Jeffri Salim Davidson was non-committal but did not rule out such a possibility. “If we suddenly sold something for RM2 billion cash, you’ve got to ask what will the management do with it? We can repay our borrowings, use it for acquisitions if any or return it to shareholders. “And if we wanted to buy something big, I think, at the moment, we’ve got the capacity to gear up, so shareholders can work out which scenario is most likely,” says Jeffri. There is precedent. In September, it completed the sale of a water treatment business in Shandong province, China, for RMB450 million (RM275 million). The sale in turn contributed to a special two sen dividend for the financial year ended June 30, 2018 (FY2018). That year, Sime Darby paid a total of 8 sen per share in dividends. Sime Darby’s dividend policy is to pay out at least 50% of net earnings but the FY2018 dividends represented an 88% payout ratio. However, Sime Darby is not in fire-sale mode, clarifies Jeffri. “We’re not in a desperate situation. We don’t need the cash and many of these businesses are profitable, so we’re in no hurry to sell them.” “But in the long run, the direction is to get out of these businesses. We will find buyers at the right time and divest over the next few years,” Jeffri adds. Its Chinese assets remain front and centre at the moment. With the water business sold, Sime Darby’s remaining assets in Shandong are four ports in Weifang and Jining. These logistics assets are next on the list, says Jeffri. “But these are trickier and will take a bit more time to divest. It’s difficult to put a timeline to it but hopefully, we can do it in the next 1½ years.” According to him, among the challenges in finding a suitable buyer is the local government’s drive to consolidate local ports. Ports aside, Sime Darby’s motley collection of assets and businesses ranges from its insurance business to a 30% stake in Tesco Stores (Malaysia) Sdn Bhd and a 12% stake in property developer Eastern & Oriental Bhd (E&O). It is difficult to pinpoint a specific valuation for the insurance business and the Tesco stake. The E&O shareholding is worth about RM179 million on the open market based on the company’s market capitalisation of RM1.49 billion as at Oct 25. As for the logistics assets in Shandong, a Sept 3 note by CIMB Research pegged their valuation at RM2.3 billion based on last year’s invested capital. But perhaps the crown jewel in Sime Darby’s stable of assets is its Malaysia Vision Valley (MVV) land of about 9,900 acres in Labu, Negeri Sembilan. “The land is valuable. We valued it at RM2.5 billion, but it’s in our books at historical prices, so it’s sort of a hidden asset,” Jeffri remarks. Recall that Sime Darby Property Bhd has a five-year option to buy the MVV land from Sime Darby. Any transaction will be based on the prevailing market price during the point of sale, Jeffri says. *(Source: The EdgeMarkets)*

Rating Action

Issuer	PDS Description	Rating/Outlook	Action
Edra Energy Sdn Bhd	Sukuk Wakalah of up to RM5.085 billion in nominal value (2018/2038) (the Sukuk).	AA3/Stable	Reaffirmed
Edra Power Holdings Sdn Bhd	Corporate Credit ratings	AA1/Stable/P1	Reaffirmed

Source: RAM, MARC

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