S&P Global
Ratings

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Summary:

Singapore Post Ltd.

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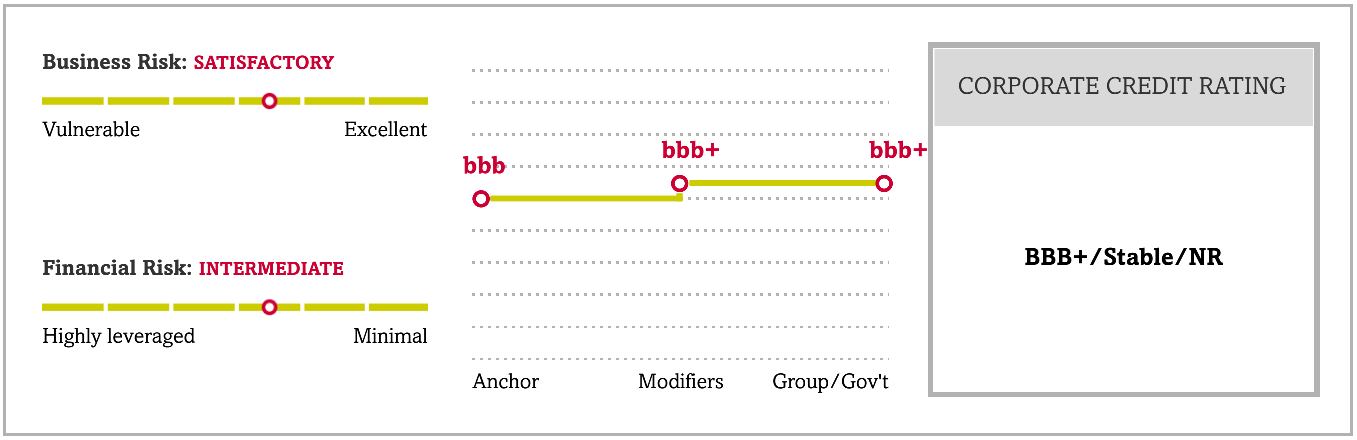

Rationale

Business Risk: Satisfactory	Financial Risk: Intermediate
• Dominant domestic market position. • Strong operating efficiency. • Less established e-commerce operations compared to the postal buisness. • Declining and more volatile profitability.	• Lower dividend payouts. • Reducing capital spending. • Limited financial headroom for the rating.

Outlook: Stable

The stable outlook reflects our expectation that Singapore Post Ltd. (SingPost) will consolidate its operations in the logistics and express delivery markets in Asia-Pacific and the U.S in the next six to 12 months. We anticipate that the Singapore-based postal and logistics services provider will manage its costs and logistics capacity to support earnings growth and control its profitability decline. In the absence of rating headroom, we also expect SingPost to rein in its acquisition spending and reduce its net debt through cash generation. We forecast the company's debt-to-EBITDA ratio to be close to 2.5x in the next 18 months.

Downside scenario

We could lower the rating if SingPost's debt-to-EBITDA ratio increases beyond 2.5x on a sustained basis. This could happen primarily if the company faces more revenue and cost pressures in its mail business and fiercer competition in the non-mail business than what we anticipate. This would be reflected by any early indications of unadjusted EBITDA being less than Singapore dollar (S$) 230 million in fiscal 2018 (year ending March 31). Higher-than-expected debt-funded capital expenditures and acquisitions or dividend payouts may also lead us to lower the rating.

Upside scenario

An upgrade looks unlikely for SingPost over the next two years, given the company's exposure to declining mail volumes and the strong competitive pressures in the logistics and express delivery businesses. We may raise the rating if the company establishes a record of consistent governance and successful strategy execution. We would also expect to see a reduction in leverage, with the debt-to-EBITDA ratio permanently below 2.0x. In a remote scenario, a stronger contribution of logistics and e-commerce to operating profit, with limited dilution of margin, could cause us to reassess the company's earnings quality.

Our Base-Case Scenario

Assumptions

- Solid growth in revenues in the next 12-24 months as recent acquisitions begin to contribute to full-year earnings and e-commerce activities continue to grow.
- Adjusted EBITDA of about S$260 million in 2017, increasing to about S$270 million in 2018.
- Capital expenditure of about S$250 million in 2017 and S$100 million in 2018, mainly for the redevelopment of the Singapore Post Centre. Spending will fall to S$60 million-S$80 million in subsequent years.
- Dividend payout of 60%-80% of underlying net profit.
- No meaningful acquisitions in the next 12-24 months.

Key Metrics

	2016A*	2017E*	2018E*
EBITDA margin (%)	20.6	18.5.0-19.0	17.5-18.0
DCF	(306.4)	(135.0)-(145.0)	(5.0)-(15.0)
Debt/EBITDA (x)§	2.3-2.5	2.3-2.5	2.3-2.5

*The fiscal year end is March 31. §S&P Global Ratings' fully adjusted figures. Adjustments to debt include operating lease commitments, the full amount of SingPost's S$350 million senior perpetual bond, and a 25% haircut on reported cash. A--Actual. E--Estimate. DSC--Discretionary cash flows.

Business Risk: Satisfactory

An efficient domestic postal infrastructure, higher profitability than peers, some diversity in operations and strategic geographical location support SingPost's earnings quality. Its transformation into an ecommerce enabler, however, has impaired its margin level and stability as the company establishes itself in a highly competitive space, and in ventures, which are markedly less profitable than its historical postal activity.

As the national postal service provider of Singapore and member of the Universal Postal Union (UPU), SingPost has historically enjoyed well-entrenched, protected market positions in the domestic and international mail business. However, we believe that SingPost's terminal dues (the cost of last mile delivery in a foreign country) are likely to increase 2018 onward. With Singapore now considered as a "developed" country by the UPU, SingPost is required to pay higher terminal dues on outbound mail. We expect that this, combined with increasing cross border mail volumes driven by SingPost's ecommerce initiatives, is likely to give rise to margin pressure in this segment. Nevertheless, we view that the company's highly efficient domestic postal infrastructure, strengthened by its newly opening e-commerce logistics hub, and high population density in Singapore, should help to mitigate the margin erosion.

In our view, SingPost will continue to consolidate its competitive positions in its e-commerce and logistics markets. Through its acquisitions of e-commerce companies Trade Global and Jagged Peak, synergies with Alibaba Group Holding Ltd., and the development of its commercial network in Southeast Asia and Oceania (provided by 76%-owned subsidiary Quantium Solutions International and wholly owned subsidiary SingPost Logistics Pte Ltd.), SingPost is transforming into a global end-to-end e-commerce enabler. While this has helped to stem the structural decline in mail volumes, we believe that SingPost has less established competitive positions in its new ventures compared to that as a postal provider in Singapore. The company faces strong competition from other e-commerce enablers, as well as the traditional logistics and express delivery providers that benefit from their ownership of strong infrastructure throughout the delivery process, scale, and high service standards. In our opinion, SingPost's asset-light structure that relies on its partnerships with other delivery companies outside Singapore, minimizes capital expenditure, but could compromise service standards and efficiencies. However, through leveraging on its unique blend of postal and commercial networks, SingPost has been able to compete with its offering of a low-cost range of e-commerce and logistics solutions.

We anticipate that increasing earnings contribution from e-commerce and logistics will translate into lower and more volatile margins over time. For the nine months ended Dec. 31, 2016, operating margin for the company's traditional mail business was around 28%, compared with less than 5% for its logistics and loss-making e-commerce operations. Operating performance to date has reflected faster-than-expected margin erosion, particularly from the logistics and ecommerce segments, which are facing pricing pressures and rising costs in a highly competitive environment. As of Dec. 31, 2016, the company reported EBITDA of about S$155 million, which represented 70% of our fiscal 2017 forecasts (year ending March 31, 2017). We expect SingPost's unadjusted EBITDA margins to decline to around 15% in fiscal 2017, from 17% in fiscal 2016 and 23% in fiscal 2015, as the e-commerce and logistics segments start to contribute more significantly to earnings.

Financial Risk: Intermediate

We project SingPost's free operating cash flows to be negative S$40 million-S$50 million in fiscal 2017, growing to S$90million-S$110 million in fiscal 2018. With the completion of the new Singapore Post Centre mall in fiscal 2017, we expect that capital spending will reduce.

We also expect that the company will continue to moderate its acquisition spending as it prioritizes the integration and broadening of its existing operations and network. Furthermore, while SingPost has the option to divest its minority stakes in non-core assets, we do not expect this will occur in the near term at the expense of appropriate valuations, given these subsidiaries are profitable.

The recent change in SingPost's dividend policy, which now better reflects the profitability of the company as it evolves into an e-commerce enabler, will support discretionary cash flow generation. The revision of the company's payout policy to 60%-80% of the underlying net profit, offers more financial flexibility than its previous commitment to maintaining an absolute payout amount of 7.0 cents a share per year.

As a consequence of reduced spending and less aggressive distributions to shareholders, we expect a gradual improvement in SingPost's cash flow adequacy. We project the adjusted debt-to-EBITDA ratio to be close to our ceiling of 2.5x in both fiscal 2017 and 2018. However, leverage could improve toward 2.3x in fiscal 2019, driven by higher operating cash flows as volumes from the logistics and e-commerce segments gain momentum, costs stabilize, and capital spending reduces. We believe that absolute debt levels will remain stable, hence the company's ability to remain within its headroom will be largely driven by its capacity to stem its margin deterioration.

Liquidity: Adequate

We view SingPost's liquidity as adequate because its sources of liquidity will cover needs by more than 1.2x in the next 12 months to December 2017. We also forecast that liquidity sources will exceed uses even if EBITDA were to decline by 15%.

Principal Liquidity Sources	Principal Liquidity Uses
• Cash and equivalents of S$234 million as of Dec. 31, 2016. • Funds from operations that we estimate at about S$190 million in the period. • Net equity infusion of S$184 million from Alibaba in January 2017.	• Debt maturities of about S$198 million in the next 12 months. • Capital expenditure of about S$140 million. • Dividends including cash distributions of equity-like instruments of about S$130 million in the period.

Other Credit Considerations

After recent turbulence surrounding SingPost's governance practices and lack of transparency, we believe the company has implemented procedures to prevent those issues from reoccurring. Furthermore, with the appointment of a new group CEO, we believe that SingPost has now established the core of the management and governance structures it needs for executing its strategy in becoming an e-commerce enabler. This is despite the recent departure of the CEO of SP Commerce, which we view will not cause operational disruption.

Ratings Score Snapshot

Corporate Credit Rating

BBB+/Stable/NR

Business risk: Satisfactory

- **Country risk:** Low
- **Industry risk:** Low
- **Competitive position:** Satisfactory

Financial risk: Intermediate

- **Cash flow/Leverage:** Intermediate

Anchor: bbb

Modifiers

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)

- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Fair (no impact)
- **Comparable rating analysis:** Positive (+1 notch)

Related Criteria And Research

Related Criteria

- Standard & Poor's National And Regional Scale Mapping Tables, Jan. 19, 2016
- National And Regional Scale Credit Ratings, Sept. 22, 2014
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Railroad And Package Express Industry, Aug. 12, 2014
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios and Adjustments, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	Modest	**Intermediate**	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	**bbb/bbb-**	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-