招银国际 CMB INTERNATIONAL

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CMBI Credit Commentary

BTSDF – Gradual deleveraging will be achievable. Buy with good relative value

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We see relative value in BTSDF now following its bond price correction of 15pts after its failed USD bond attempt in Jan'22. At BTSDF '24 (YTM~11%, 86-mid), we believe the current low bond price has reflected its higher leverage from acquisition and weak 2021 result. We expect H&H's successful refinancing of bridge loan in Sep'22 and its gradual deleveraging via operating cash flow, will help its bond yield to tighten, albeit gradually.

Operational challenge in 2021

Health & Happiness (H&H) saw operational challenge from low birth rate in China. FY2021 Sales +3% yoy to RMB 11.5bn but EBITDA fell 14%yoy to RMB 1.8bn. Net profit further declined by 55%yoy after write-down of one infant milk formula factory.

Rise in leverage from aggressive acquisition

By Dec'21, H&H's net debt rose substantially to RMB 7bn, from RMB 4.3bn at Dec'20, after an expensive Zesty Paws acquisition (USD 610mn) in Sep'21. This increased H&H's Net Debt/EBITDA to 3.8x, from 2.0x in 2020.

New bank loan for refinancing will be crucial given volatile offshore bond market

Management revealed at its annual result presentation that it has obtained internal credit approvals from certain banks for a new syndicated loan to refinance its bridge loan (USD 350mn due Sep'22 and USD 150mn due Nov'22). We believe H&H can successfully roll-over this bridge loan given its deleveraging track record via free cash flow from operation. The company recorded annual free cash flow of RMB 1.3bn – 1.4bn during 2019 – 2020.

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That said, we expect future deleveraging will be gradual

H&H's core BNC business (57% of revenue) will see flattish sales growth in next 2 years, under the backdrop of lower birth rate and intense competition. Overall management is targeting double digit revenue growth in 2022 (mainly through the newly acquired Pets Nutrition segment –PNC), while guiding 1-2pt lower EBITDA margin given cost inflation. At the same time, H&H lowered its dividend payout ratio to 30%, from 50% last 2 years. With that, we estimate H&H can generate RMB 500mn – RMB 1bn annual discretionary cash flow for debt repayment next 2 years.

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