Credit Brief on Singapore SMEs
Q1 2019

Jointly by Credit Research Initiative Team and Validus Capital Pte. Ltd.

This brief is a jointly published quarterly article, between Validus and Credit Research Initiative at National University of Singapore (NUS-CRI), providing insights on industry-level Credit Risk of Singapore SMEs and provides a summary of how loans generated through the Validus' platform incorporates the learnings from the industry-level Credit Analysis. The Credit Risk of the industries is measured via the Probability of Default (PD) model developed by the NUS-CRI team (www.rmicri.org).This analysis is conducted across 10 industries (Bloomberg classification) and the loans funded through Validus. (www.validus.sg)

Data note: Analysis in this report is based on the sample of public SMEs. Due to the small sample size in Singapore and similar credit characteristics of public SMEs across Singapore, Australia, Hong Kong and Korea, all CRI sector PDs are calculated as an average of PDs for the public SMEs in the four economies. This methodology is in agreement with Validus Capital Pte. Ltd. and is expected to reflect the Credit Risk profile of Singapore SMEs. In this report, the PDs for each quarter were computed using model parameters that were calibrated on April 17, 2019, using all available data up to March 31, 2019.

A. Key Highlights on Credit Risk

The NUS-CRI 1-year PD for Singapore SMEs decreased to 22.68bps at the end of Q1 2019, despite a slower GDP growth of 1.3% during the quarter. The SBF-DP SME Index[1], a forward looking measure of SME sentiment worsened from 50.7 to 50.4, suggesting a less optimistic outlook for Singapore SMEs between April 2019 and September 2019.

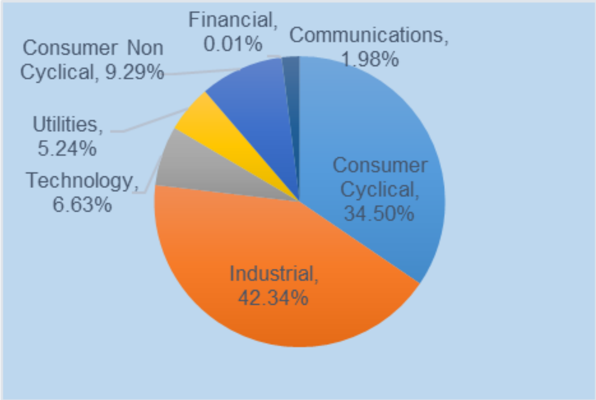
- CRI 1-year PDs for Singapore SMEs decreased at the end of Q1 2019 after reaching a high in Q4 2018.
- Continuing from Q4 2018, the Energy and Utilities industries had the highest credit risk in Q1, while Consumer (non-cyclical) and Financial had the lowest credit risk.
- While all industries witnessed a general improvement in credit quality, Utilities saw the biggest decrease in default risk.
- The aggregate credit quality of Medium-, Small- and Micro-sized firms improved during the quarter. The aggregate default risk for Micro Communications firms increased the most by 8.03bps compared to other sizes, while the Medium Utilities firms witnessed the largest improvement of 12.19bps across any size and industry group.
- The overall multiple of medium term PD (1-year) to short term PD (1-month) increased to 11.59x from 11.08x in the previous quarter. This is an indicator denoting the extent of the behaviour of medium term PD compared to the short term PD which is further used as a benchmark for industry-level PD multiple. Any industry level PD multiple that is higher than the overall multiple indicates that medium term loans for the industry are more risky than short term loans and vice versa.

B. Loans originated through Validus Platform

- Loans funded[2] through Validus include firms in Consumer Cyclical, Consumer Cyclical, Industrial, Technology, Financial and Utilities.
- 80% of loans originated from Validus platform are to companies within the Industrial and Consumer Cyclical sectors. The loans are mostly short term in nature for all the industries. NUS-CRI insights do not indicate any adverse risk on these two industry sectors.
- Profile of loans originated through Validus platform are displayed in the charts below:

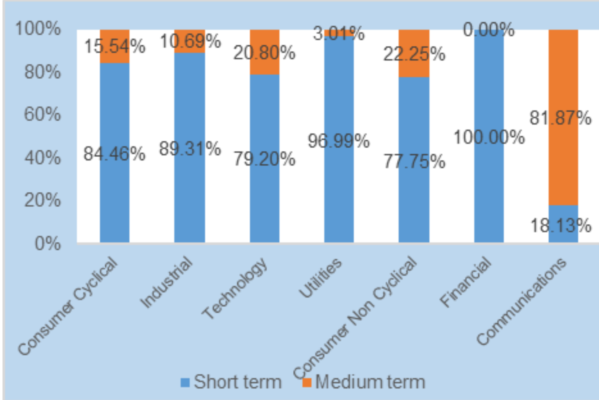
[1] SBF-DP SME Index is a six-month forward-looking business sentiment index by Singapore Business Federation and DP Information Group
[2] This report contains all loans funded through Validus

B.1 % of total loans funded through Validus Platform by industry sector



Source: Validus Capital, all figures are updated as of March 31, 2019

B.2 % of loans funded through Validus Platform by industry sector and tenure

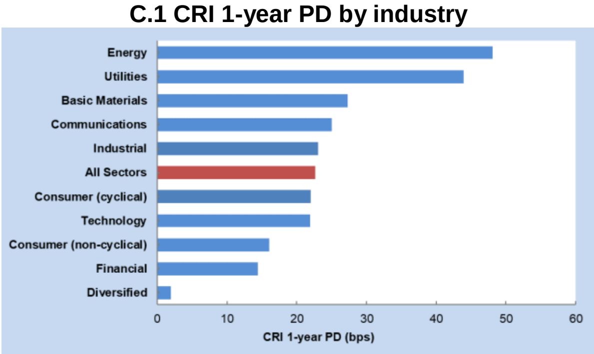


Source: Validus Capital, all figures are updated as of March 31, 2019

C. Credit Risk for Singapore Industries

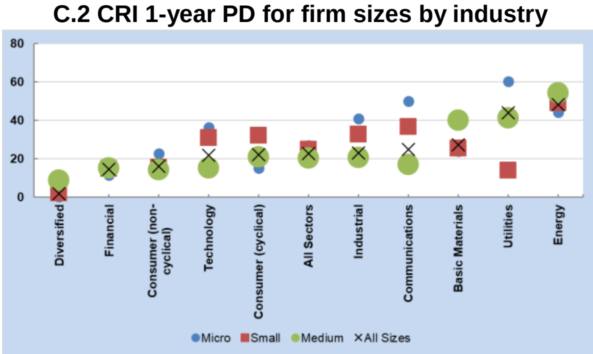
The CRI 1-year PD assesses the credit risk in the future one year. The comparison of PD trends and PD multipliers across industries gives a clear picture of the relative credit performance of each industry. The relative credit performance by firm size within each industry is also provided. By definition[3], firms with annual turnover equal to or below USD 2mn are considered Micro Firms, between USD 2-10mn are considered Small Firms, while larger than USD 10mn and equal to or below USD 100mn are considered Medium Firms.

C.1 CRI 1-year PD by industry



Source: CRI, all figures are updated as of March 31, 2019

C.2 CRI 1-year PD for firm sizes by industry



Source: CRI, all figures are updated as of March 31, 2019

The Energy industry had the highest CRI 1-year PD among all Singapore SMEs in Q1 2019, followed by Utilities and Basic Materials. In contrast, the Financial, Consumer (non-cyclical) and Technology delivered the most robust performances.

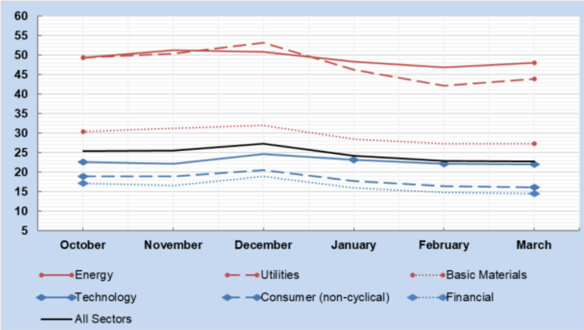
- The aggregate CRI 1-year PD of all sectors in Q1 2019 decreased by 4.60bps from the last quarter. The credit performance of every industry improved in Q1 2019.
- While Utilities was the most risky industry in Q4 2018, during Q1 2019 it switched places with the Energy industry.
- Overall, the Financial industry was the least risky.

SMEs with different firm sizes delivered variable CRI 1-year PD performances within each industry. Industries with the highest PD variance of sizes were Utilities, Communications and Technology.

- Micro firms in the Financial industry had better credit performances than All Sizes in the same industry. Micro Financial firms had a CRI 1-year PD of 11.39bps, the lowest of any size or industry.
- The Utilities industry displayed the highest variance of the CRI 1-year PDs among any of its peers. On the opposite end of the spectrum, the Financial industry displayed the lowest variance.
- Micro Utilities firms carried the highest credit risk among every other firm of any size or industry. The CRI 1-year PD for Micro Utilities firms is 60.45bps.

[3] Defined by Validus Capital Pte. Ltd.

C.3 CRI 1-year PD trend by industry

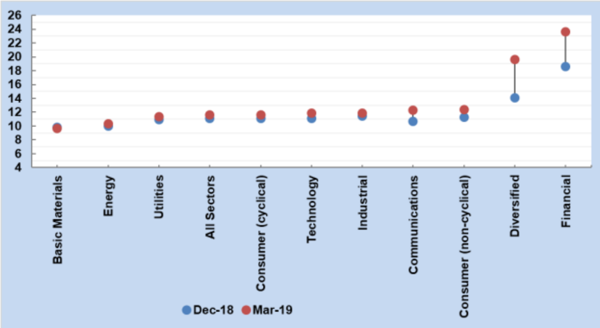


Source: CRI, all figures are updated as of March 31, 2019

The credit performances for all Singapore SMEs improved in Q1 2019.

- The most risky industry, Energy, saw a decrease in CRI 1-year PD by 2.69bps during Q1 2019. PDs for the second and third most risky industry, Utilities and Basic Materials, dropped by 9.22bps and 4.69bps, respectively.
- Comparing the trends within the three least risky industries, the CRI 1-year PDs for Technology and Consumer (non-cyclical) decreased by 2.75bps and by 4.45bps, respectively. The Financial industry was the best credit performer this quarter, with its CRI 1-year PD decreasing by 4.43bps during Q1 2019.

C.4 CRI PD multiple by industry



Source: CRI, all figures are updated as of March 31, 2019

The multiples of medium term PD (1-year) to short term PD (1-month) for all industries are shown above.

- The PD multiplier increased for all industries, except for Basic Materials. An increase in the multiplier indicates that credit risk has improved in the short term faster than the medium term.
- The Financial industry recorded the largest increase in PD multiple. Its CRI PD multiple increased to 23.66X from 18.58X between December 2018 and March 2019.

D. Conclusion

Overall, the NUS-CRI 1-year PD decreased during Q1, from 27.28bps in December to 22.68bps in March. The credit profile of Singapore SMEs improved despite the slower than expected GDP growth at 1.3% in Q1 2019 based on advance estimates from the Ministry of Trade and Industry (MTI). According to the survey conducted by the Singapore Business Federation and DP Information Group, Singapore SMEs show more wariness and exhibit weaker business sentiment amid slower economic growth and ongoing geopolitical conflicts. However, the survey shows an increase in capital investment expectations across all sectors and manufacturing saw the biggest rise. This could be due to the SME-related funding initiatives announced in Singapore Budget 2019. The Budget has plans to help SMEs to get access to capital and adopt digital technologies. Some of the initiatives include extending the SME working capital loan scheme for two more years and the government to take on up to 70% of risk for bank loans to companies incorporated for less than five years. The automation support package will also be extended by two years to help companies reduce their automation costs. Despite the more challenging environment, SMEs in Singapore continue to invest in their business with the assistance from the government which may help these companies to keep pace with changes and stay ahead in the long run.