Credit Brief on Singapore SMEs
Q2 2017

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.

A. Key Highlights on Credit Risk

The NUS-CRI 1-year PD for Singapore SMEs decreased from 14.23bps to 13.82bps in Q2 2017, coinciding with Singapore's 2.5% Q2 GDP YoY growth. The SBF-DP SME Index[1] increased from 50.4 to 50.9, in tandem with the decline in NUS-CRI PD, suggesting a slight improvement of the credit profile of Singapore SMEs in Q2 2017.

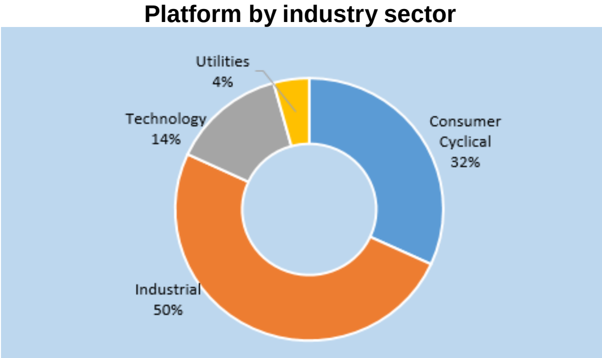
- CRI 1-year PDs for Singapore SMEs slightly improved in both Q1 2017 and Q2 2017.
- Energy and Utilities sectors saw the highest credit risk in Q2, while Consumer (non-cyclical) and Financial delivered the best credit performance among all industries.
- The Consumer (non-cyclical) sector became the best performer in Q2 2017.
- Small Firms performed better than All Sizes in the Utilities and Energy industry, while reversely for most of the other industries.
- The overall multiple of medium term PD (1-year) to short term PD (1-month) is 10.23x as compared to 10.52x from 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 those industry sectors 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, Industrial, Technology and Utilities.
- 82% 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 these two industries. NUS-CRI insights does not indicate any adverse risk on these two industry sectors.
- Profile of loans originated through Validus platform are displayed in the charts below:

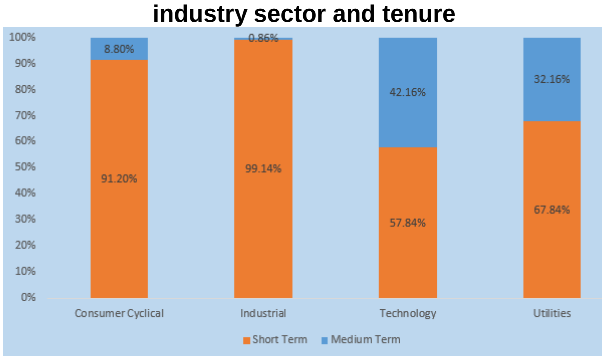
[1] SBF-DP SME Index is a six-month forward looking business sentiment index by Singapore Business Federation and DP Information Group
[2] This report contains all loans funded through Validus

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



Source: Validus Capital, all figures are updated as of June 30, 2017

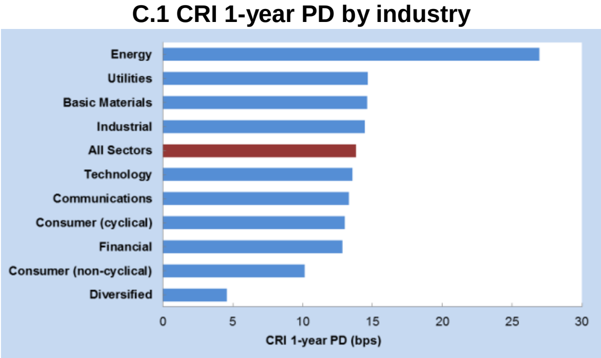
B.2 % of loans funded through Validus Platform by industry sector and tenure



Source: Validus Capital, all figures are updated as of June 30, 2017

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 sector. 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

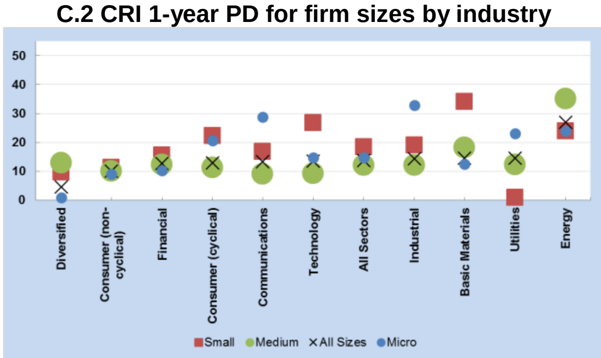


Source: CRI, all figures are updated as of June 30, 2017

Among all Singapore SMEs, the CRI 1-year PD for the Energy sector performed worst, followed by the Utilities and Basic Materials sectors in Q2 2017. In contrast, the Consumer (non-cyclical), Financial and Consumer (cyclical) sectors delivered robust performances.

- The credit performance of most sectors improved in Q2 2017 except Energy, Basic Materials and Utilities sectors which saw an increase in CRI 1-year PD.
- The Energy remained to be the most risky sector in Q2 2017. The Utilities sector, which maintained the position of the least risky sector from Q4 2016 to Q1 2017, became the second most risky sector in this quarter.
- The Consumer (non-cyclical) sector which was the second least risky sector in Q1 2017 was the least risky sector in Q2 2017.

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



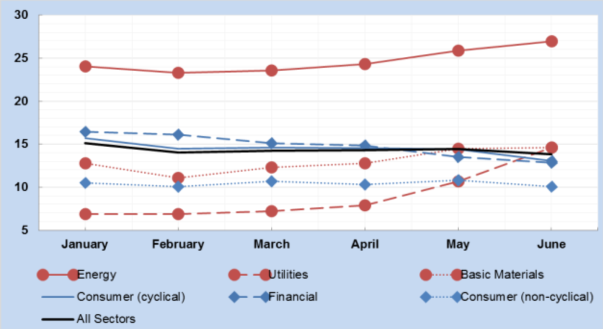
Source: CRI, all figures are updated as of June 30, 2017

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

- The small firms in the Utilities and Energy sectors performed better than All Sizes in the same sector. Small Utilities firms also performed much better than small sized firms across the other sectors. Small Utilities firms had the CRI 1-year PD of 1.04bps, lower than every other firm of any size or sector.
- Utilities sector companies displayed the highest variance of the CRI 1-year PDs among all sectors. Small Basic Material firms were the second most risky, slightly less risky than medium Energy firms.
- Medium Energy firms carried the highest credit risk among firms of all sizes in all industries. The CRI 1-year PD for medium Energy firms was 35.12bps.

[3] Defined by Validus Capital Pte. Ltd.

C.3 CRI 1-year PD trend by industry

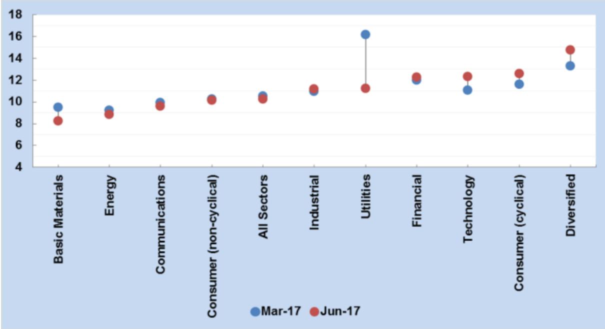


Source: CRI, all figures are updated as of June 30, 2017

The credit performances for all Singapore SMEs had performed slightly improved in Q2 2017.

- Among the three most risky sectors, the Energy sector's CRI 1-year PD deteriorated by 3.46bps during Q2. The Utilities and Basic Materials sectors deteriorated by 7.40bps and 2.35bps respectively.
- Comparing the trends within the three least risky sectors, the CRI 1-year PDs for the Consumer (cyclical) and Financial sectors improved by 1.56bps and 2.25bps respectively. The 1-year PD for the Consumer (non-cyclical) sector continue to improve, although the magnitude is not as substantial as the previous quarter. The Utilities sector, which was the best credit performer last quarter, saw its CRI 1-year PD increase considerably during Q2 2017.

C.4 CRI PD multiple by industry



Source: CRI, all figures are updated as of June 30, 2017

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

- The PD multipliers showed varied changes. The PD multipliers increased for the Industrial, Financial, Technology and Consumer (cyclical) sectors, while the multipliers decreased for the remaining sectors. An increase in the multiplier indicates that credit risk has worsened in the medium term faster than the short term.
- The Utilities sector recorded the largest decrease in PD multiple. The CRI PD multiple for the sector decreased to 11.2X in June 2017 from 16.2X in March 2017.

D. Conclusion

Singapore SMEs are slightly more optimistic about prospects in the next 6 months, marking the second consecutive quarter that the outlook has improved. The Singapore Business Federation – DP Info SME Index, a measure of business sentiment among SMEs, increased slightly from the previous quarter. The improvement resonates with the decline in NUS-CRI 1-year PD, which suggests that the credit performance in most sectors witnessed a recovery. In addition to strengthening credit profile, Singapore SMEs are also expected to benefit from the government's support. Government agencies have lined up a range of assistance schemes, programmes and network of partners to support SME's capability development efforts. For example, the government and participating financial institutions have stepped in to help viable SMEs with cash flow concerns to co-share 50% of the default risk for loans up to SGD 300,000 per SME. Despite a more optimistic outlook, the index is still at the region of its multi-year low reflecting tough business environment.