Credit Brief on Singapore SMEs
Q2 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 July 04, 2019, using all available data up to June 30, 2019.

A. Key Highlights on Credit Risk

The NUS-CRI 1-year PD for Singapore SMEs increased to 26.27bps at the end of Q2 2019 amid a slower GDP growth of 0.1% on a year-on-year basis during the quarter. The SBF-DP SME Index[1], a forward looking measure of SME sentiment slightly improved from 50.4 to 50.8, suggesting a more optimistic outlook for Singapore SMEs between July 2019 and December 2019.

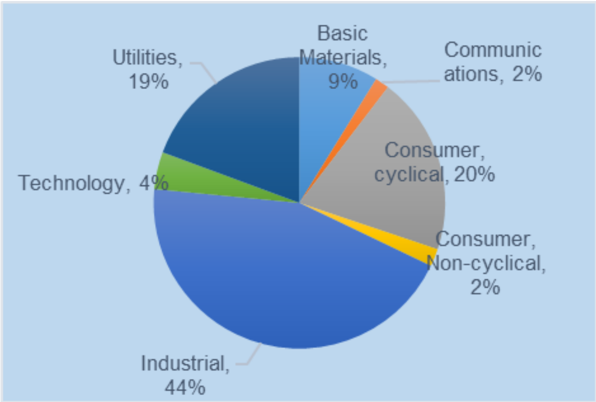
- CRI 1-year PDs for Singapore SMEs in Q2 2019 increased to its highest since the start of the year.
- Continuing from Q1 2019, the Energy and Utilities industries had the highest credit risk in Q2, while Consumer (non-cyclical) and Financial had the lowest credit risk.
- The Consumer (cyclical) sector witnessed the largest increase in default risk while the Energy sector saw the largest decrease in default risk.
- The aggregate credit quality of Medium- and Small-sized firms deteriorated during this quarter while the aggregate credit quality of Micro-sized firms improved during the quarter. The aggregate default risk for Medium Utilities firms increased the most by 10.33bps while the Micro Utilities sector witnessed the largest improvement of 17.85bps across any size and industry group.
- The overall multiple of medium term PD (1-year) to short term PD (1-month) increased to 11.93x from 10.93x 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.
- 65% 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:

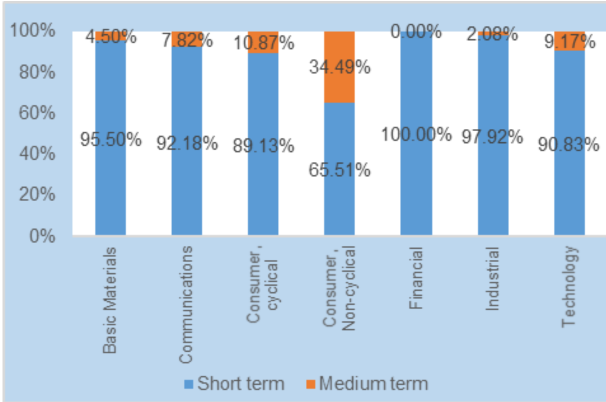
[1] SBF-DP SME Index is a six-month forward-looking business sentiment index by Singapore Business Federation and DP Information Group
[2] This report contains all loans funded through Validus

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



Source: Validus Capital, all figures are updated as of June 30, 2019

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

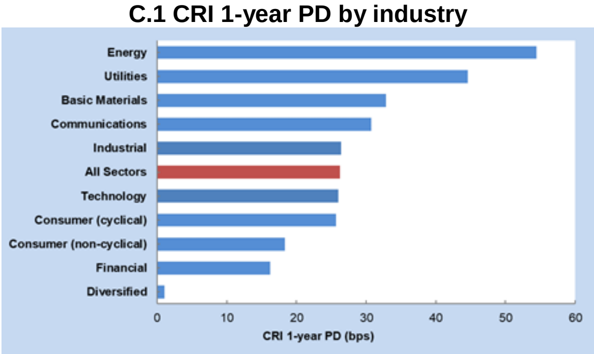


Source: Validus Capital, all figures are updated as of June 30, 2019

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

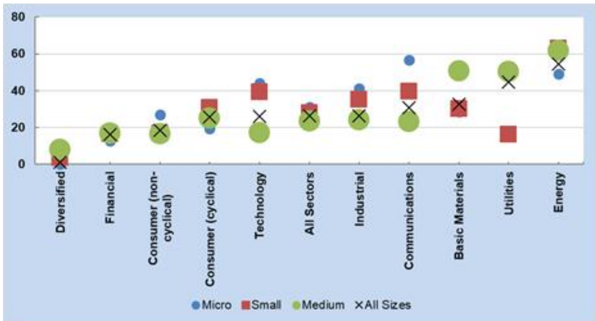


Source: CRI, all figures are updated as of June 30, 2019

The Energy industry had the highest CRI 1-year PD among all Singapore SMEs in Q2 2019, followed by Utilities and Basic Materials. In contrast, the Financial, Consumer (non-cyclical) and Consumer (cyclical) delivered the most robust performances.

- The aggregate CRI 1-year PD of all sectors in Q2 2019 increased by 0.99bps from the last quarter. However, the credit performance for the Basic Materials, Energy and Utilities sectors improved in Q2 2019.
- The energy sector remained the most risky industry in Q2 2018.
- Overall, the Financial industry was the least risky.

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



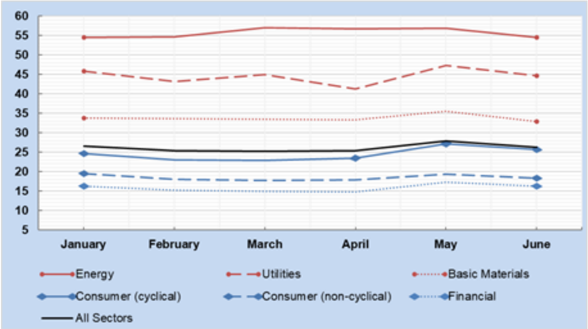
Source: CRI, all figures are updated as of June 30, 2019

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 12.82bps, 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.
- Small Energy firms carried the highest credit risk among every other firm of any size or industry. The CRI 1-year PD for Small Energy firms is 62.94bps.

[3] Defined by Validus Capital Pte. Ltd.

C.3 CRI 1-year PD trend by industry

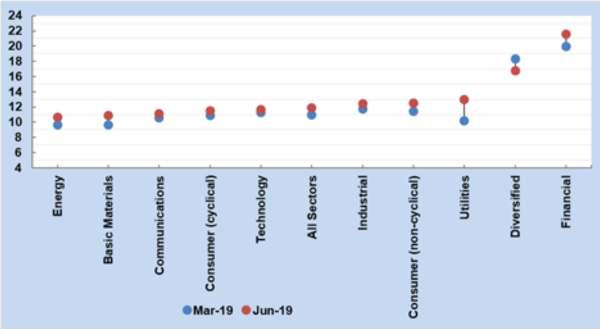


Source: CRI, all figures are updated as of June 30, 2019

The credit performances for the majority of Singapore SMEs worsened in Q2 2019.

- The most risky industry, Energy, saw a decrease in CRI 1-year PD by 2.52bps during Q2 2019. PDs for the second and third most risky industry, Utilities and Basic Materials, dropped by 0.41bps and 0.59bps, respectively.
- Comparing the trends within the three least risky industries, the CRI 1-year PDs for Consumer (non-cyclical) and Consumer (cyclical) increased by 0.65bps and by 2.76bps, respectively. The Financial industry was the best credit performer this quarter despite its CRI 1-year PD increasing by 1.24bps during Q2 2019.

C.4 CRI PD multiple by industry



Source: CRI, all figures are updated as of June 30, 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. An increase in the multiplier indicates that credit risk has improved in the short term faster than the medium term.
- The Utilities industry recorded the largest increase in PD multiple. Its CRI PD multiple increased to 12.95X from 10.16X between March 2019 and June 2019.

D. Conclusion

Overall, the NUS-CRI 1-year PD increased slightly during Q2, from 25.28bps in March to 26.27bps in June. The credit profile of Singapore SMEs deteriorated amid the slower than expected GDP growth at 0.1% in Q2 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 remain cautiously optimistic about business prospects despite slower economic growth and ongoing geopolitical conflicts. SMEs in the commerce/ trading sectors continue to expect depressed profitability and saw the biggest drop in expectations on access to financing as lenders become more cautious in injecting funds into a sector directly affected by the global trade tensions. However, SMEs in other sectors saw an uptick in general sentiments as SMEs are planning to take advantage of Budget 2019 and the year-end holiday season. In addition, growing global headwinds may be driving SMEs to pursue new growth opportunities. For instance, the retail / F&B sectors continued to see an increase in business expansions expectations as they saw greater expansion opportunities while the transport/ storage sectors also saw a boost in expectations due to seeing longer-term opportunities within ASEAN and China.