

Downgrade of SDEB's Sukuk

What happened?

On 9 December 2021, Malaysia Rating Corporation Berhad (MARC) downgraded the credit rating of Senai-Desaru Expressway Berhad's (SDEB) RM1.89 billion Islamic Medium-Term Notes programme (Restructured Sukuk) to BB_{is} from BBB_{-is} due to SDEB's tight liquidity position, which has heightened the risk of the company not being able to address its upcoming financial obligations on a timely basis. According to MARC, the company's considerable challenges to address its current predicament have been compounded by the declining traffic levels that was made worse by the pandemic-induced closures and limited visibility on traffic recovery on Senai-Desaru Expressway.

SDEB is the concessionaire of the Senai-Desaru Expressway in Johor. SDEB had issued a RM1.46 billion Sukuk to part-finance the construction of the expressway in 2005. Given various construction delays and cost overruns, the Sukuk was first restructured in 2010. Due to slow traffic volume growth, the Sukuk was subsequently restructured again in 2014 resulting in the present Restructured Sukuk.

As a result of the downgrade, SDEB's Restructured Sukuk were repriced downwards by 51%-67%, with the longer dated ones the worst hit.

Our thoughts

The downgrade of SDEB's rating did not come as a surprise given its weak credit profile but the quantum of yield increase/price drop for the sukuk was larger than that for recent comparable downgrades. SDEB is likely to require remedial measures to address the company's financial obligations as its weak liquidity and expected poor performance made debt servicing an extremely challenging task.

Our position

Manulife Investment Balanced Fund (MABLF) has approximately RM9.3 million exposure to SDEB as of 30 November 2021 (~11% of Fund's NAV). The price drop of SDEB's Restructured Sukuk following the downgrade was the primary reason behind the 7.16% drop in MABLF fund price from RM0.3825 on 9 Dec 2021 to RM0.3551 on 10 December 2021.

Our investment team has been trying to dispose of all SDEB exposures since 2014 but had been unable to do so as SDEB's Sukuk has very poor liquidity, which was caused by its weak credit profile and the multiple restructuring history of the Sukuk. We will continue to monitor development pertaining to this Sukuk and provide updates should there be further development.

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