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Research Update:

First Pacific Co. Ltd. Assigned 'BBB-' Rating; Outlook Stable

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Rating Action Overview

- First Pacific Co. Ltd. has a portfolio of liquid, high quality, and moderately diversified assets that yield steady dividends. The Hong Kong-based investment holding company also has a record of moderate leverage over the past decade.
- First Pacific's small scale, concentrated holdings, and limited recent record of rotating assets temper these strengths.
- We assigned our 'BBB-' long-term issuer credit rating to First Pacific.
- The stable rating outlook over the next 24 months reflects our view that First Pacific will maintain its loan-to-value (LTV) ratio below 30% even through downcycles, and proactively manage its debt maturities and cash outlay to keep adequate liquidity.

Rating Action Rationale

First Pacific has high-quality investments and a stable dividend income stream. The company owns controlling or material stakes in several listed companies in the Philippines and Indonesia--for example, 50.1% in PT Indofood Sukses Makmur Tbk. (Indofood), 25.6% in PLDT Inc. (BBB+/Stable/--) and 44.6% in Metro Pacific Investments Corp. These three companies accounted for about 92% of First Pacific's US$5.2 billion portfolio as of March 31, 2022, and contributed 98% of its dividend income in 2021. Key investee companies have leading market positions and strong cash flows. We estimate the weighted average credit quality of the portfolio to be 'bbb-'.

The dividend stream from First Pacific's investment portfolio was stable through the COVID-19 pandemic, largely reflecting the resilient business of PLDT and Indofood. The company's stakes in these listed investments are highly liquid. These investments and the dividends thereof are not subject to encumbrance. Furthermore, legacy covenants regarding PLDT's share disposal and the use of disposal proceeds are suspended as long as First Pacific maintains an investment grade rating.

First Pacific's small scale and high portfolio concentration tempers its strengths. First Pacific's portfolio is among the smallest of the investment holding companies in our 'BBB' rating category, and its investee companies operate mainly in the Philippines and Indonesia. The top three holdings account for 92% of the portfolio--this share is high relative to that of other investment holding companies. The long-term nature of First Pacific's investments also means limited asset rotation going forward.

While the top three assets are performing well, the high concentration constrains upside to our asset diversification assessment, absent any meaningful portfolio rotation. Moreover, as a result of the concentration, the valuation of First Pacific's portfolio is dependent on the inherent cycles of the local capital markets. Ongoing geopolitical tensions and the potential of a deterioration of economic conditions due to increasing inflation and supply chain disruptions could hit overall equity valuations over the next 12 months.

The investment performance beyond the top-three investee companies is mixed. FPM Power Holding's subsidiary PacificLight Power Pte Ltd. faced multi-year losses and ultimately required restructuring and recapitalization in 2019. However, PacificLight's operations have turned around since the restructuring, supporting the management's acumen. We see an investment holding company's willingness to financially support investees as an exception, rather than the norm.

We expect First Pacific to take proactive action to maintain its LTV ratio below 30%, even during market turmoil. The company intends to maintain the ratio around 25% during stable market conditions and not higher than 30% during market volatility. First Pacific's LTV ratio averaged about 22% over the past 10 years. The ratio was 25% as of Dec. 31, 2021, and 26% as of March 31, 2022. The ratio provides some headroom to accommodate volatility in asset values, which is an intrinsic risk for investment holding companies. First Pacific has a record of reducing debt at the head office level using divestment proceeds. The LTV ratio declined in 2016 and 2019, following the partial divestment of Metro Pacific and the divestment of Goodman Fielder, respectively.

We anticipate First Pacific will sustain a strong cash flow adequacy ratio of 2.8x-3.2x over the next two years. The ratio improved to 3x in 2021, from 1.8x in 2019, because of higher dividend income and lower interest costs. We forecast the company will have stable cash returns from its portfolio. This stems from our expectation that First Pacific, as the controlling or largest single shareholder, has strong influence on investees' business strategy and dividend policy.

First Pacific's exposure to rising interest costs over the next two years is limited because 65% of its debt has fixed interest rates. The company also proactively manages its foreign currency exposure. All its interest-servicing obligations are denominated in U.S. dollar, while dividend income is denominated in Philippines peso or Indonesia rupiah. The company hedges all foreign currency-denominated dividend income upon dividend declaration by the investee companies.

First Pacific will likely continue its conservative dividend policy of 25% of annual recurring profit. We expect the company to maintain flexibility in its share-buyback program to ensure future shareholder returns do not drain excessive cash from reinvestment opportunities.

First Pacific will likely maintain its clear investment strategy and long investment record. We believe the company's investment discipline and risk management capabilities built over three decades are comparable with peers. That said, like many of its investment holding peers, First Pacific's record of investments is not without blemishes, such as in the case of Goodman Fielder and PacificLight. The former was sold at a loss and the latter was fully written off.

First Pacific's investment evaluation criteria, including environment, social, and governance (ESG) considerations, are well documented. New investments are subject to approval by the board and the finance committee, which mainly comprises independent non-executive directors (INEDs). Connected-party transactions are reviewed by committees comprising INEDs, and substantial connected party transactions require majority approval by non-connected shareholders (for example Indofood's acquisition of Pinehill Co. Ltd. in 2020).

First Pacific addresses ESG risk as part of its risk management framework and sustainable development. The risk assessment committee maintains a risk matrix with reference to the probability and potential consequences of major risks identified. The board reviews the matrix on a semi-annual basis. First Pacific also conducted various scenario analysis to assess any potential impacts of adverse foreign exchange movements and earnings volatility on First Pacific's liquidity during the COVID-19 pandemic.

Outlook

The stable outlook on First Pacific over the next 24 months stems from our view that the company will prudently manage its investments and debt such that its LTV ratio remains below 30% through market cycles. We also expect First Pacific to proactively manage its debt maturities and cash outlay to keep adequate liquidity.

Upside scenario

Rating upside is limited over the next two to three years due to the high portfolio concentration. However, we could consider a positive rating action if: (1) First Pacific formally adjusts its leverage threshold to below 20%; or (2) the asset diversity of the company's investment portfolio substantially improves, while current leverage and portfolio quality are maintained.

Downside scenario

We would lower the rating if:

- First Pacific deviates from its prudent financial management or allows its LTV ratio to rise above 30% irrespective of market conditions. This could happen if the company takes on excessive debt or fails to take the necessary steps to protect its balance sheet in the context of declining equity markets; or
- The creditworthiness of First Pacific's assets deteriorates because of substantial debt-funded discretionary spending at the investee level, or if their competitive position deteriorates. Clear credit deterioration in any key investees or a decline in the weightage of PLDT in the portfolio could indicate a weakening in credit quality.

Company Description

First Pacific is a Hong Kong-based investment holding company that was established in 1981 and listed on the Hong Kong Stock Exchange in 1988. First Pacific's investment assets are located mainly in the Philippines and Indonesia, with focus on four key industries: consumer food products, telecommunications, infrastructure, and natural resources.

First Pacific's key investee companies include Indofood, PLDT, and Metro Pacific. Other investments include Philex Mining Corp., PacificLight Power Pte Ltd., and PXP Energy Corp.

Mr. Anthoni Salim is the largest shareholder of First Pacific with 45.1% interest. First Pacific had a market capitalization of approximately US$1.7 billion as of April 14, 2022.

Our Base-Case Scenario

Assumptions:

- First Pacific's continued prudent investment policy and proactive management actions are aimed at maintaining its LTV at 25%-27%.
- Cash dividend and interest income of US$200 million-US$220 million in 12 months ending Dec. 31, 2022.
- No material increase in operating costs, which we expect will be about US$20 million per year.
- Interest payment of US$55.0 million-US$60.0 million in 2022.
- Dividend payment to shareholders of US$85 million-US$95 million over the period.
- Share buyback of approximately US$30 million over the period.

We arrive at the following key metrics based on the above assumptions:

- LTV of 25%-27% in 2022, compared with 25% at end-2021.
- Cash flow adequacy ratio of 2.8x-3.2x over the next two years, compared with 3x in 2021.

Liquidity

We view First Pacific's liquidity as adequate. We estimate the company's liquidity sources will exceed its needs by about 1.4x for the 12 months ending March 31, 2023.

We believe First Pacific has good standing in the debt capital markets and maintains sound banking relationships with various local and regional banks. These factors will continue to support the company's liquidity. The management also has a history of proactively managing its debt maturity profile.

First Pacific will likely absorb a high-impact, low-probability event over the next six to 12 months with limited need for refinancing. Such a scenario would likely be a severe correction of market values for listed shares, as was seen during the COVID-19 pandemic.

Principal liquidity sources include:

- Cash and cash equivalents that we estimate at US$135.0 million as of March 31, 2022.
- Dividends from portfolio companies and interest income of US$180 million-US$190 million for the 12 months ending March 31, 2023, after assuming a 15% haircut from our base-case estimate.

Principal liquidity uses include:

- No debt maturities due in the 12 months to March 31, 2023.
- Operating and tax expense of US$20 million in the period.
- No committed spending for business acquisitions and addition of new investments over the period.

- Interest payment of US$55.0 million-US$60.0 million in the 12 months ending March 31, 2023.
- Dividend payment to shareholders of US$85 million-US$95 million during the period.
- Share buyback of up to US$30 million over the period.

Covenants

First Pacific has incurrence based financial covenants for its indebtedness. For example, the company cannot incur additional debt if its interest coverage ratio is less than 2.5x. First Pacific's interest coverage ratio was 3.8x as at end-2021.

Environmental, Social, And Governance

E-2, S-2, G-2

We believe ESG credit factors have no material influence on our rating analysis on First Pacific. The company's portfolio is mainly exposed to consumer food products, telecommunications, and infrastructure sectors (92% of portfolio), which we view as having neutral environmental and social risk. We do not expect First Pacific's exposure to upstream metals and mining (copper and gold), palm oil, as well as oil and gas as having a material impact on its credit quality.

Governance factors are an overall neutral consideration in our credit analysis of First Pacific. The company could be subject to the influence of the Salim family due to Mr. Anthoni Salim's 45.1% interest. Mr. Anthoni Salim is the non-executive chairman while his son Mr. Axton Salim is a non-executive director of the board. Mr. Anthoni Salim holds executive positions at key investee companies such as Indofood. Mr. Axton Salim also holds management positions at Indofood and its key subsidiary and is involved in day-to-day operations.

Indofood has a record of past and ongoing material related-party transactions, including the Pinehill acquisition from the Salim family in 2020. These risks are balanced by First Pacific's effective board, with 50% independent non-executive directors, corporate governance committee comprising INEDs who provide oversight on related-party transactions, and good disclosures and transparency. First Pacific also has a professional management and comprehensive risk management policy.

Ratings Score Snapshot

Issuer Credit Rating: BBB-/Stable/--

Business risk: Satisfactory

- Country risk: Moderately High
- Industry risk: Intermediate
- Investment position: Satisfactory

Financial risk: Intermediate

- Cash flow/Leverage: Intermediate

Anchor: bbb-

Modifiers:

- Liquidity: Adequate (No impact)
- Management and governance: Satisfactory (No impact)
- Comparable rating analysis: Neutral (No impact)

Stand-alone credit profile: bbb-

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Corporates | Industrials: Methodology: Investment Holding Companies, Dec. 1, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

New Rating; CreditWatch/Outlook Action	
First Pacific Co. Ltd.	
Issuer Credit Rating	BBB-/Stable/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.