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Research Update:

SoftBank Group Downgraded To 'BB', Subordinated Bonds To 'B' On Higher Asset Risk; Outlook Stable

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Rating Action Overview

- Asset risk in SoftBank Group Corp.'s investment portfolio is rising more than we had assumed; its liquidity and creditworthiness are likely to remain materially weakened for the next year or so.
- The company's disciplined financial management in severe business circumstances; abundant cash; and holdings of shares in U.K.-based chipmaker Arm Ltd., which could go public, support the rating.
- We lowered by one notch our long-term issuer credit and senior unsecured debt ratings on SoftBank Group to 'BB' and our issue rating on its subordinated bonds to 'B'.
- The outlook is stable.

Rating Action Rationale

SoftBank Group's investment portfolio is becoming more susceptible to changes in its external environment. The proportion of SoftBank Group's fund business, including SoftBank Vision Funds (SVFs) that invest in unlisted shares, has risen to nearly 40%. Unlisted companies are less competitive and more susceptible to the external environment, including financial market developments, than listed companies. SoftBank Group has therefore become more susceptible to the external environment than we had previously assumed. Unlisted companies made up 69% of SVF1's investment assets and 85% of SVF2's as of March 31, 2023.

The fund business invests intensively in global technology companies. These tend to be highly volatile. Cumulative investment losses of SVF1 and SVF2 since launch further widened to $8.5 billion as of March 31, 2023. The cumulative losses were $1.5 billion at the end of September 2022. We attribute the rise in losses to lower stock prices for companies in which SVF1 and SVF2 have invested and significant declines in the corporate value of unlisted companies.

The asset liquidity of SoftBank Group's investment portfolio is likely to remain substantially below the tolerance range for our previous 'BB+' long-term issuer credit rating on the company. The proportion of listed shares in its portfolio (including listed assets in SVF1 and SVF2 unless otherwise noted) has been declining rapidly and significantly. Ongoing sales of shares in China-based Alibaba Group Holding Ltd. (A+/Stable/--), previously a major asset for the company, have eroded the proportion of listed assets in its portfolio. Furthermore, the technology stocks in which the company has primarily invested have been depressed for a prolonged period.

The proportion of listed assets in the company's investment portfolio is likely to remain low for now. Arm, its largest investment asset, would need to go public for the proportion of listed assets to rise markedly, in our view. The proportion of listed assets declined to about 38% as of March 31, 2023. It was 43% in November 2022 (using Sept. 30, 2022, figures), when we revised to negative the outlook on our then 'BB+' long-term issuer credit rating on SoftBank Group. We assume the ratio will likely be 35%-40% over the next six to 12 months.

Asset liquidity should improve greatly if Arm is listed, in our view. Arm confidentially submitted a draft registration statement on its initial public offering plan with the U.S. Securities and Exchange Commission on April 29, 2023. This marks progress for a listing. However, the timing and value of a listing remain uncertain. Therefore, we do not incorporate a listing of Arm in our base-case scenario. Arm accounts for 26% of the investment portfolio as of March 31, 2023.

We regard SoftBank Group's holding of Arm shares as the largest asset in the portfolio as positive factor. This is because Arm as a listed stock would be a sizable listed asset. Listing would improve asset liquidity in the future.

SoftBank Group aims for disciplined financial management even in a difficult operating environment. This is likely to continue to underpin the company's creditworthiness, in our view. SoftBank Group secured a total of ¥5.7 trillion in cash mainly through the monetization of Alibaba shares. It repaid ¥2.4 trillion debt in fiscal 2022 (ended March 31, 2023). Throughout this period, stock markets were on a downward trend globally. Moreover, it secured ¥4.5 trillion in cash as of the end of fiscal 2022 by considerably curbing new investments. As a result, the company's loan-to-value (LTV) ratio (as we define it) improved to about 24% as of the end of fiscal 2022 from 31.7% a year earlier. Although asset value remains depressed, we expect the company to control its LTV ratio at 25%-30% over the next year or so.

SoftBank Group will likely gradually increase investments, mainly in its fund business, using the abundant cash that it gained by monetizing Alibaba shares. The company has articulated a very aggressive growth strategy. In fiscal 2021, the company invested US$44.3 billion, mainly in the fund business. Conversely, in fiscal 2022 when financial stress intensified, it sharply reduced its investment to US$3.1 billion.

Negative factors for the group far outweigh supporting factors. We therefore downgraded the company. The volatility of its investment portfolio and rising asset risk drive the negatives for the group. Meanwhile, financial management capability; a high level of cash; and holdings of shares in Arm, which could be listed, are positives.

We revised down our assessment of SoftBank Group's business risk profile by one notch to weak from fair. This is because the proportion of listed assets in its investment portfolio worsened further. Meanwhile, we affirmed our assessment of its financial risk profile as significant. We based this on the company's improved LTV ratio in severe business circumstances.

We think the improved ratio will allow the group to control leverage at a level commensurate with our rating, even though it is resuming investments. The significant assessment reflects our view that, despite recent improvement in its LTV ratio, the ratio could potentially move, given the high volatility of technology and unlisted stocks as the main investment assets.

We maintain our positive assessment of the company's comparable rating analysis. We have incorporated the likelihood of the company maintaining a high level of cash and the likelihood of Arm going public in the next six to 12 months into our positive assessment of the company's comparable rating analysis.

Outlook

The stable outlook reflects our view that SoftBank Group will continue to maintain a high level of cash and deposits as well as financial management that focuses on the LTV ratio. This is despite harsh financial market conditions. We expect the company's LTV ratio will remain 25%-30% (as we define it) if the company makes investments in risky fund business with a degree of discipline and does not suffer material deterioration of asset liquidity of its investment portfolio. Furthermore, we have incorporated into the outlook the likelihood of Arm going public in the next six to 12 months.

Downside scenario

We might consider lowering the rating on SoftBank Group if we see a heightened likelihood of either of the scenarios below.

- SoftBank Group spends a large amount of cash on investments and share repurchases and, at the same time, listing Arm is significantly delayed.
- SoftBank Group's LTV ratio approaches 40%. This could happen if a rapid and significant deterioration in market conditions causes a material decline in its asset value.

Upside scenario

We might consider upgrading the company if both of the scenarios below look likely to occur.

- The company manages its LTV ratio at 25%-30% through a cycle of the stock market by maintaining disciplined financial management.
- Its proportion of listed assets (including listed assets in SVF1 and SVF2) in the value of its investment portfolio increases to over 60% and remains at that level.

Company Description

SoftBank Group is a nonoperating investment holding company. It invests in domestic and overseas technology companies, including e-commerce entities in China and telecom businesses in Japan and the U.S. It manages a total of US$100 billion in its private investment funds SVF1 and the subsequent SVF2, both of which focus on unlisted companies in the technology field. It had ¥15.6 trillion in total investment assets as of March 31, 2023. Masayoshi Son, the founder, chairman of the supervisory board, and CEO, holds about 29% of the company's shares as the largest shareholder.

Our Base-Case Scenario

We assume the following as our base-case scenario of SoftBank Group.

- The value of the company's investment assets remains about ¥11 trillion-¥13 trillion, slightly lower than their current value, for about one year, given stock market volatility.
- The proportion of Alibaba shares in the investment portfolio declining to zero in the next six months or so as a result of their sale.
- Portfolio creditworthiness in the 'bb' category.
- No listing of Arm in our base-case scenario; however, a listing would likely improve asset liquidity.
- Sufficient cash and deposits on hand to cover redemption of corporate bonds that reach maturity over the next two years.
- About ¥160 billion-¥170 billion a year in total dividend income from its domestic telecom subsidiary.
- Low levels of distributions from the fund business of about ¥330 billion annually over the next year or so, due to impact of the downturn in technology stocks.
- Annual recurring expenses of ¥350 billion-¥400 billion (operating expenses, interest payments, and tax charges).
- Share buybacks not worsening its LTV ratio significantly.

Based on the scenario above, we assume the company's key metrics as follows:

- The proportion of listed shares in the portfolio will remain 35%-40%.
- Its LTV ratio will be 25%-30%.

Liquidity

We assess SoftBank Group's liquidity as adequate. We expect its liquidity sources to exceed 2x its uses, backed by abundant cash over the next 12 months. However, the ratio will likely drop if it resumes investments. The company conducts relatively prudent financial management. For example, it maintains a policy of securing cash and deposits equal to two years of redemptions of bonds by proactively raising redemption funds. Furthermore, we view it as having room to monetize assets as necessary. Accordingly, the company can maintain liquidity without relying on refinancing, in our view. In addition, SoftBank Group has an ample record of access to capital markets, as demonstrated by its continued issuance of bonds in domestic and overseas markets.

Our assumptions of the company's liquidity sources and uses for the 12 months from the end of March 2023 follow.

Principle liquidity sources

- Cash and equivalents of about ¥4.5 trillion; and

- Dividend or distributions income of about ¥500 billion.

Principle liquidity uses

- Debt repayments totaling about ¥930 billion;
- Execution of investment commitments of about ¥430 billion;
- Interest payments, operating expenses, and tax expenses of ¥350 billion-¥400 billion; and
- Dividend payouts of a little less than ¥70 billion.

Covenants

SoftBank Group's debt does not contain material covenants that would have a major effect on its financial activities.

Environmental, Social, And Governance

ESG credit indicators: E-2, S-3, G-3

Governance factors are a moderately negative consideration in our credit rating analysis of SoftBank Group. Its largest shareholder (29% ownership, as of the end of September 2022) is Masayoshi Son, the growth-focused founder, chairman of the supervisory board, and CEO. He will continue to exert meaningful influence on the company's corporate culture and financial policy, in our view. On the other hand, we consider SoftBank Group's management to have strong management and execution capabilities. We also acknowledge that the company has been enhancing its governance structure in recent years, including by increasing the ratio of external members on its board of directors to 55.5% and hiring a chief risk officer.

Social factors are also a moderately negative consideration. We think SoftBank Group is still exposed to social risk related to Chinese antitrust laws because it has invested 14% of investment portfolio assets (as of March 31, 2023) in Chinese corporations, mainly through its Vision Funds. We hold this view even after recognizing that SoftBank Group has reduced its exposure to Chinese internet companies by diversifying its investment portfolio and proceeding with the sale of Alibaba shares. The company also focuses on investments in unlisted technology companies utilizing artificial intelligence. These factors lead us to believe SoftBank Group is exposed to social risk through privacy and data security regulations.

Ratings Score Snapshot

Issuer Credit Rating	BB/Stable/--
Business risk:	Weak
Country risk	Low
Industry risk	Intermediate
Investment position	Weak

Issuer Credit Rating	BB/Stable/--
Financial risk:	Significant
Leverage/cash flow	Significant
Funding and capital structure	Neutral
Anchor	bb-
Modifiers:	
Liquidity	Adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Positive (+1 notch)

Related Criteria

- Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Group Rating Methodology, July 1, 2019
- Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Methodology: Investment Holding Companies, Dec. 1, 2015
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Methodology: Industry Risk, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- SoftBank Group Corp., April 10, 2023
- SoftBank Group's Exposure To Market Volatility Strains Creditworthiness, March 17, 2023
- SoftBank Group Outlook Revised To Negative From Stable On Continuing Investment Weakness; 'BB+' Ratings Affirmed, Nov. 17, 2022

Ratings List

Downgraded; Outlook Action

	To	From
SoftBank Group Corp.		
Issuer Credit Rating	BB/Stable/--	BB+/Negative/--

Downgraded

	To	From
SoftBank Group Corp.		
Senior Unsecured	BB	BB+
Subordinated	B	B+

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.