

# CapitaLand Retail China Trust

Declining rental reversions on back of slowing tenant sales

## SINGAPORE | REAL ESTATE (REIT) | RESULTS

- Weak RMB dragged down gross revenue by 2.7%. (Otherwise up 4.5% in RMB terms on comparable mall basis, excluding the new 5% VAT expensed from revenue from 1 May 2016).
- CapitaMall Xizhimen's -19.7% rental reversion in 4Q16 due to strategic entry of two new lifestyle retail concept tenants who will pay lower base rental versus the outgoing fashion tenants.
- 46% of debt to be re-financed in 2017, 30% of which is a bridging loan taken out this year for the acquisition.
- Outlook for rental reversion to remain in single digit.
- Downgrade from ACCUMULATE to NEUTRAL with lowered DDM-derived target price of S\$1.44 (from \$1.62).

### Results at a glance

(SGD mn)	FY16	FY15	y/y (%)	Comments
Gross Revenue	214.4	220.3	↓ -2.7%	Weaker RMB against SGD. In RMB terms, gross revenue from multi-tenanted malls rose 0.9% on a comparable mall basis, after factoring in 5% VAT expense from 1 May 2016. (Excluding the new VAT expense: up 4.5%)
Net property income	139.7	141.1	↓ -1.0%	Lower VAT offset by additional property tax for Beijing malls.
Distributable income	86.7	89.2	↓ -2.8%	
<b>DPU (SG Cents)</b>	<b>10.05</b>	<b>10.60</b>	<b>↓ -5.2%</b>	

Source: Company, Phillip Securities Research (Singapore)

### Operational Updates

	FY16	FY15	y-y (%)	Comments
Gearing Ratio	35.3%	27.7%		Increased gearing for CapitaMall Xinnan acquisition
% of SGD debt on fixed rate	87.5%	83.7%		RMB denominated loans are on variable rates
Portfolio Valuation (RMB\$m)	11,181	10,912	2.5	Comparable mall basis, net of new acquisitions
NAV/unit (S\$)	1.65	1.77	(6.8)	

Source: Company, Phillip Securities Research (Singapore)

### What is the news?

#### Xizhimen's -19.7% negative rental reversion in 4Q16 explained.

CapitaMall Xizhimen is the biggest mall (by NLA and gross revenue) in CRCT's portfolio, contributing 27% of FY16 total gross revenue. The -19.7% rental reversion in 4Q16 may have caused some uneasiness in investors. This was due to two new lifestyle retail concept tenants occupying large areas, who are paying lower base rents than the previous fashion retail tenants. The first is a hybrid bookstore/café and the second a premium textile seller. Management opined that lifestyle retailers such as the bookstore/café could help attract traffic into the mall and at the same time entice them to stay longer in the mall. Excluding these two tenants, 4Q16 and FY16 rental reversion for Xizhimen would have been 4.9% and 4.8% respectively.

As the threat of e-commerce grows, retail malls could increasingly turn to such lifestyle/entertainment/services tenants to attract shoppers to "hang out" in the mall. These trade sectors are also less affected by e-commerce. These tenants however, typically occupy larger floor areas and pay lower base rents. We think what CapitaMall Xizhimen faced would be a continuing future trend for retail malls as they reshape in the new economy.

31 January 2017

### NEUTRAL (Downgraded)

LAST CLOSE PRICE	SGD 1.410
FORECAST DIV	SGD 0.101
TARGET PRICE	SGD 1.440
<b>TOTAL RETURN</b>	<b>9.3%</b>

### COMPANY DATA

O/S SHARES (MN):	870
MARKET CAP (USD mn / SGD mn):	860 / 1226
52 - WK HI/LO (SGD):	1.67 / 1.33
3M Average Daily T/O (mn):	1.33

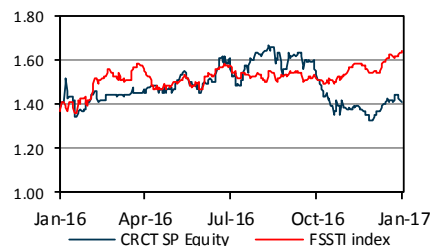
### MAJOR SHAREHOLDERS (%)

CAPITALAND LIMITED	18.6%
CAPITAMALL TRUST	14.1%
MATTHEWS INTERNATIONAL CAPITAL	6.67%
AMERICAN INTERNATIONAL ASSURANCE	5.72%
CAPITARETAIL CHINA TR. MGMT	4.59%

### PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	6.0	(9.0)	11.2
STI RETURN	6.4	8.4	24.6

### PRICE VS. STI



Source: Bloomberg, PSR

### KEY FINANCIALS

Y/E Dec	FY15	FY16	FY17e	FY18e
Gross Rev. (SGD mn)	220	214	243	241
NPI (SGD mn)	141	140	150	150
Dist. Inc (SGD mn)	89	87	87	87
P/NAV (x)	0.80	0.86	0.84	0.86
DPU (Cents)	10.6	10.1	10.0	9.9
Dist. Yield	7.4%	7.1%	7.1%	7.0%

Source: Company Data, Bloomberg

### Valuation Method

**DDM (Cost of equity 7.82%, Terminal Growth 1%)**

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### Other portfolio updates of note.

CapitaMall Minzhongleyuan has benefitted from the re-opening of Zhongshan Avenue and commencement of the new metro line. Committed occupancy improved from 70.5% at end FY15 to 93.6% currently. NPI of this mall when CRCT acquired it in 2011 was ~RMB30mn (translating to gross revenue of ~RMB46mn assuming 65% NPI margin) versus FY16 gross revenue of RMB12.3mn. Management guided that it targets to bring mall revenue and NPI back to the acquisition levels in 3 years' time.

CapitaMall Wuhu continues to undergo tenancy adjustments and is expected to remain under pressure in FY17.

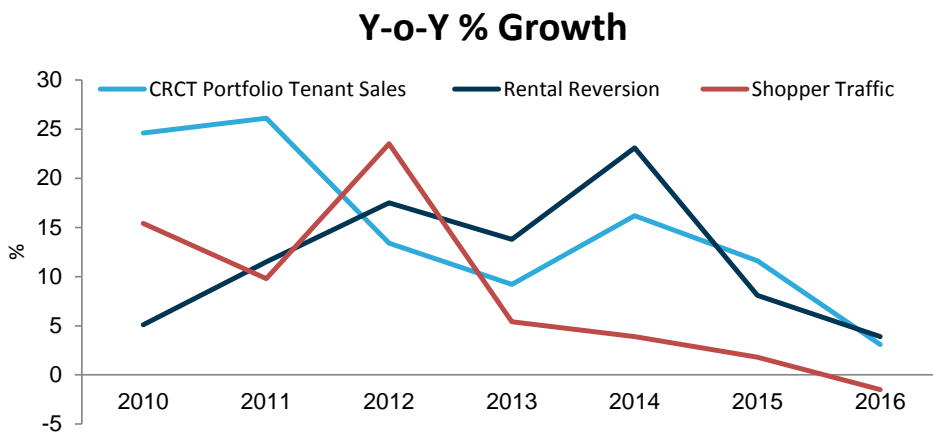
### 46% of debt (S\$450.5mn) to be re-financed in 2017, S\$300mn of which is a bridging loan taken out last year for the acquisition.

S\$300mn of debt to be refinanced this year is a bridging term loan taken out last year for the acquisition of CapitaMall Xinnan. Management guided that financing margins (spread that banks quote on top of the benchmark Swap Offer Rate or SOR) have stayed relatively stable, notwithstanding a rising SOR rate since November 2016. We have assumed an average cost of debt of 3% for FY17 versus 2.81% in FY16.

### Outlook for rental reversion to remain in single digit.

Since the high of 23.1% in 2014, rental reversion slowed to single digits in 2015 (8.1%) and 2016 (3.9%) on the back of slowing tenant sales in 2016. We expect the single digit rental reversion trend to continue into 2017.

Figure 1: CRCT Portfolio Statistics and Rental Reversions



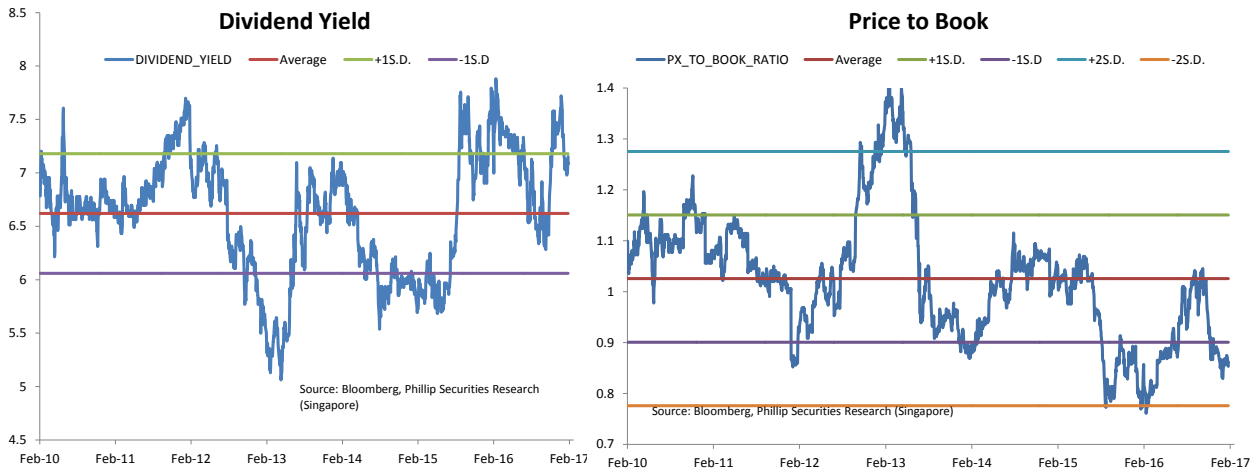
Source: Company, Phillip Securities Research (Singapore)

### Investment Action

#### Downgrade to NEUTRAL from ACCUMULATE with lower target price of S\$1.44 (from S\$1.62).

We downgrade our ACCUMULATE rating to NEUTRAL with a lower DDM-derived target price of S\$1.44, at an implied FY17e dividend yield of 7.2%. This compares with CRCT's average yield of 6.6% since 2010 (post GFC). On the back of slowing fundamentals and rising interest rates posing more headwinds, we deem the higher yield justifiable in current economic climate.

Figure 2: Historical Dividend Yield and P/NAV Charts



**Financials**
**Statement of Total Return and Distribution Statement**

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
<b>Gross Revenue</b>	<b>203.3</b>	<b>220.3</b>	<b>214.4</b>	<b>242.5</b>	<b>241.4</b>
Total Property expenses	(70.9)	(79.2)	(74.6)	(92.2)	(91.7)
<b>Net Property Income</b>	<b>132.4</b>	<b>141.1</b>	<b>139.7</b>	<b>150.4</b>	<b>149.7</b>
Net Finance (Expense)/Inc	(18.5)	(19.2)	(19.4)	(28.5)	(33.3)
Net Income before tax and FV changes	98.7	108.3	105.5	106.6	106.1
FV changes and forex gain/(loss)	104.8	44.8	41.2	-	-
Tax expense	(57.1)	(43.4)	(41.6)	(23.4)	(23.3)
<b>Net Income after tax and FV changes</b>	<b>146.4</b>	<b>109.3</b>	<b>104.0</b>	<b>83.1</b>	<b>82.7</b>
Net Inc attributable to Unitholders	144.6	114.0	106.6	81.3	80.9
Distribution adjustments	(63.7)	(24.8)	(19.9)	6.0	6.0
<b>Income available for distribution</b>	<b>80.9</b>	<b>89.2</b>	<b>86.7</b>	<b>87.3</b>	<b>86.9</b>

**Balance Sheet**

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
<b>ASSETS</b>					
Investment properties	2,251	2,413	2,628	2,628	2,628
Trade and Other Receivables	11.3	12.8	12.8	15.0	14.9
Cash and Cash Equivalents	86.6	126.3	136.1	130.6	114.9
<b>Total Assets</b>	<b>2,358</b>	<b>2,570</b>	<b>2,783</b>	<b>2,789</b>	<b>2,771</b>
<b>LIABILITIES</b>					
Trade and other payables	51.1	59.5	64.5	76.7	76.3
Security deposit	41.2	43.3	48.8	46.2	46.0
Interest bearing borrowings	671.7	706.0	977.8	977.8	977.8
Other liabilities	216.2	246.4	240.7	216.2	216.2
<b>Total Liabilities</b>	<b>980.2</b>	<b>1,055.2</b>	<b>1,331.8</b>	<b>1,316.8</b>	<b>1,316.3</b>
<b>EQUITY</b>					
<b>Shareholder Equity</b>	<b>1,377.8</b>	<b>1,515.1</b>	<b>1,451.7</b>	<b>1,471.8</b>	<b>1,454.7</b>

**Per share data (SGD)**

Y/E Dec	FY14	FY15	FY16	FY17e	FY18e
NAV	1.63	1.77	1.65	1.68	1.66
DPU (cents)	9.8	10.6	10.1	10.0	9.9

**Cash Flow**

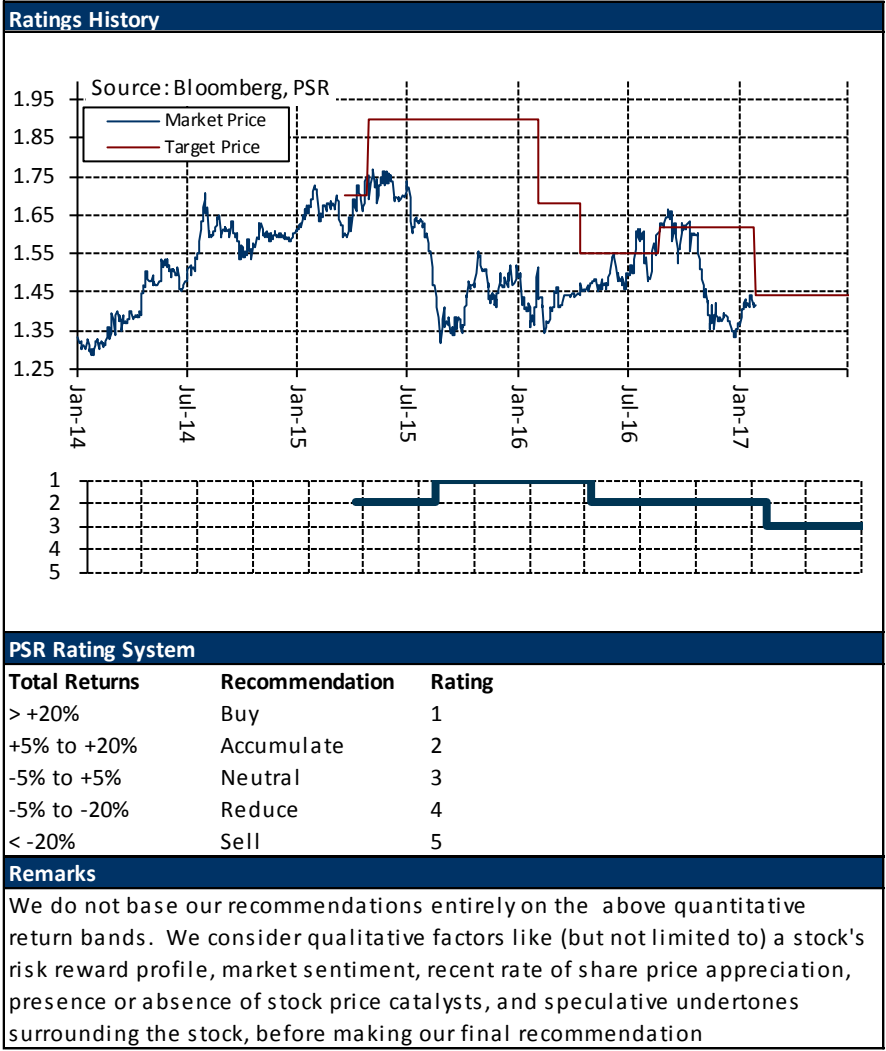
Y/E Dec, SGD mn	FY14	FY15	FY16	FY17e	FY18e
<b>CFO</b>					
Net Income after tax	146.4	109.3	104.0	83.1	82.7
Adjustments	(37.0)	5.9	9.3	34.3	39.2
WC changes	2.0	2.5	6.6	10.0	(0.3)
Cashflow from ops	111.4	117.7	119.9	127.4	121.7
<b>CFI</b>					
Cashflow from investments	(16.7)	(16.0)	(313.0)	(16.3)	(16.3)
<b>CFF</b>					
Share issuance	-	-	-	-	0.0
Distributions to unitholders	(49.0)	(66.1)	(52.5)	(87.3)	(86.9)
<b>Cashflow from financing</b>	<b>(117.3)</b>	<b>(65.8)</b>	<b>211.0</b>	<b>(116.6)</b>	<b>(121.1)</b>
<b>Net change in cash</b>	<b>(22.5)</b>	<b>35.9</b>	<b>17.9</b>	<b>(5.5)</b>	<b>(15.7)</b>
<b>CCE, end</b>	<b>86.6</b>	<b>126.3</b>	<b>136.1</b>	<b>130.6</b>	<b>114.9</b>

**Valuation Ratios**

Y/E Dec	FY14	FY15	FY16	FY17e	FY18e
P/NAV	0.98	0.80	0.86	0.84	0.86
Distribution yield (%)	6.1%	7.4%	7.1%	7.1%	7.0%
NPI yield (%)	5.9%	5.8%	5.3%	5.7%	5.7%
<b>Growth &amp; Margins (%)</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16</b>	<b>FY17e</b>	<b>FY18e</b>
<b>Growth</b>					
Revenue	28.9%	9.4%	-3.3%	14.1%	-0.5%
Net property income (NPI)	28.3%	6.7%	-1.0%	7.6%	-0.4%
DPU	8.9%	7.9%	-5.2%	-0.1%	-1.0%
<b>Margins</b>					
NPI margin	65.1%	64.0%	64.0%	62.0%	62.0%
Operating Income Margin	48.5%	49.1%	48.5%	47.5%	47.5%
<b>Key Ratios</b>					
Net Gearing	28.7%	27.7%	35.3%	35.1%	35.3%

Source: Company, Phillip Securities Research (Singapore) Estimates

\*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.



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