

Soilbuild Business Space REIT

Termination of lease at Technics Offshore

SINGAPORE | REAL ESTATE (REIT) | UPDATE

- Lease at 72 Loyang Way terminated
- Utilised security deposit can last for five more months
- Searching for new tenants to lease the property

What is the news?

Soilbuild Business Space REIT (SBREIT) announced that it has terminated the lease with Technics Offshore Engineering Pte Ltd for 72 Loyang Way with immediate effect from 9 December 2016. According to the announcement, S\$3.913 million of the S\$11.805 million bank guarantee that was received on 26 May 2016 remains unutilised; and that the unutilised sum "is equivalent to approximately five months' rent and property operating expenses".

How do we view this?

Near-term DPU remains unaffected, whereas there is uncertainty from 2Q FY17 onwards

Near-term cash flow remains unaffected by the termination of the lease, as the unutilised portion of the security deposit will continue to be drawn down. Thus, distribution per unit (DPU) will not be impacted for at least the next five months. The five months' time frame is on the assumption that the Manager is unable to secure a new tenant for the duration of the balance of the rental deposit. If a new tenant is signed on at a lower rental, the rental deposit will be used to top-up the shortfall, and it will last longer than five months.

We think that gross revenue is likely to be negatively affected after the security deposit is depleted. This is because we do not see a good chance of the entire property being leased out at the same existing rent, in view of the current oversupply situation and soft demand.

Slight change in our previous assumption, in terms of timing of the transition

Our assumption from our [update report](#) (11 October) and [results report](#) (13 October) was for 60% occupancy from 3Q FY17 onwards. In view of the security deposit being able to last for five more months, we bring forward the transition in our model to May 2017, but keep our 60% occupancy assumption.

During the last results briefing, the Manager shared that it is in negotiations with three potential tenants – two of whom are considering long-term leases of 5-10 years, while the third is short-term of one year. Occupancy at the property will be c.80%, if all three tenants each sign a lease. No update to the negotiations was given in this recent announcement.

Scope for aggregate leverage to rise at the end of the year

In line with our recent [sector report](#) on the Industrial sub-sector (11 November 2016), where we cautioned on downward revaluation of properties within the sector, we think it is likely that 72 Loyang Way will be revalued downwards at the end of this fiscal year ending December. While we are not able to forecast the new valuation for 72 Loyang Way with certainty, an impact of more than 10% would not surprise us. The property was valued at S\$97.0 million as of FY15, and all things held equal, for every 10% reduction in valuation for the property, we estimate a 0.93 cent reduction in net asset value (NAV), and an approximate 26 bps increase in aggregate leverage.

Other properties for potential downward revaluation would be Tuas Connection and West Park BizCentral. Occupancy at Tuas Connection was 86.3% as at 3Q FY16, which is lower than the 93.5% at the start of the year. Similarly, occupancy at West Park BizCentral was 90.8% as at 3Q FY16, which is lower than the 94.2% at the start of the year.

Maintain "Neutral" view with lower DDM-based target price of S\$0.67 (previous: S\$0.72)

Our FY16 forecast of 6.08 cents DPU is in line with consensus expectations of 6.1 cents. Further uncertainty lies in the actual occupancy and rent achievable from the transition to new tenants. We have raised our cost of equity from 7.4% to 7.9% in view of the greater uncertainty and risk going forward.

12 December 2016

Neutral (Maintained)

LAST CLOSE PRICE	SGD 0.650
FORECAST DIV	SGD 0.061
TARGET PRICE	SGD 0.670
TOTAL RETURN	12.4%

COMPANY DATA

O/S SHARES (MN) :	1042
MARKET CAP (USD mn / SGD mn) :	473 / 677
52 - WK HI/LO (SGD) :	0.77 / 0.63
3M Average Daily T/O (mn) :	169

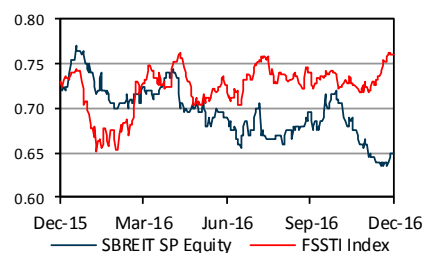
MAJOR SHAREHOLDERS (%)

CHAP HUAT LIM	25.5%
JINQUAN TONG	6.2%
SCHRODERS PLC	6.0%

PRICE PERFORMANCE (%)

	1M TH	3M TH	1YR
COMPANY	(0.8)	(4.6)	(5.5)
STI RETURN	6.1	3.1	7.4

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY 14	FY 15	FY 16e	FY 17e
Gross Rev. (SGD mn)	68.1	79.3	81.7	85.6
NPI (SGD mn)	57.4	67.8	71.1	73.5
Dist. Inc. (SGD mn)	50.2	57.9	55.0	60.8
P/NAV (x)	0.99	0.94	0.85	0.86
DPU (cents)	6.19	6.49	6.08	5.81
Distribution Yield (%)	7.9	8.7	9.3	8.9

Source: Company Data, PSR est.

VALUATION METHOD

DDM (Cost of Equity: 7.9%; Terminal g: 0.5%)

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Peer relative valuation

SBREIT is at a discount to the peer average P/NAV multiple, and has a higher 12M-trailing yield than both the peer average and the larger-capitalised peers.

Peer relative data (arranged by Mkt. Cap.)

	Mkt. Cap. (S\$ mn)	Price (S\$)	Trailing P/NAV (x)	12M-trailing yield (%)
Ascendas REIT	6,789	2.39	1.17	6.4
Mapletree Industrial Trust	2,973	1.650	1.21	6.9
AIMS AMP Capital Industrial REIT	825	1.295	0.88	8.7
Viva Industrial Trust	703	0.755	0.94	10.0
Cambridge Industrial Trust	698	0.535	0.80	8.1
Soilbuild Business Space REIT	677	0.650	0.84	9.4
Sabana Shari'ah Compliant REIT	381	0.515	0.64	10.2
Average			0.93	8.5

Source: Bloomberg (Updated: 12 December 2016)

Financials

Statement of Total Return and Distribution Statement

Y/E Dec, SGD mn	FY14	FY15	FY16e	FY17e	FY18e
Gross revenue	68.1	79.3	81.7	85.6	85.1
Property expenses	(10.8)	(11.6)	(10.5)	(12.0)	(13.6)
Net property income	57.4	67.8	71.1	73.5	71.5
Net Finance (Expense)/Inc.	(9.7)	(12.8)	(13.1)	(14.0)	(15.7)
Manager's fees	(5.5)	(6.4)	(6.0)	(6.1)	(5.7)
Other items	(1.1)	(1.4)	(1.3)	(1.5)	(1.5)
Exceptional items	-	-	-	-	-
Net income	41.2	47.1	50.7	51.9	48.6
FV change, Invmnt. properties	0.9	4.5	-	-	-
Total Return Before Tax	42.1	51.7	50.7	51.9	48.6
Taxation	-	-	-	-	-
Total Return After Tax	42.1	51.7	50.7	51.9	48.6
Distribution adjustments	8.1	6.2	4.3	8.9	8.5
Income available for distribution	50.2	57.9	55.0	60.8	57.1
Income distributed	50.2	57.9	55.0	60.8	57.1

Per share data (cents)

Y/E Dec	FY14	FY15	FY16e	FY17e	FY18e
NAV	80.0	79.8	76.7	75.6	74.6
EPU	5.09	5.28	5.13	4.96	4.60
DPU	6.19	6.49	6.08	5.81	5.40

Cash Flow

Y/E Dec, SGD mn	FY14	FY15	FY16e	FY17e	FY18e
CFO					
Net income	41.2	47.1	50.7	51.9	48.6
Adjustments	16.7	21.8	16.2	21.7	22.3
WC changes	3.4	(0.5)	22.0	1.5	(0.2)
Cash generated from ops	61.3	68.4	88.9	75.2	70.6
Others	(7.4)	(11.4)	(14.6)	(15.7)	(16.6)
Cashflow from ops	53.9	57.1	74.3	59.5	54.1
CFI					
CAPEX, net	(0.2)	(25.5)	(32.0)	-	-
Purchase of Inv. Propty.	(94.6)	(98.1)	(100.5)	-	-
Others	-	-	-	-	-
Cashflow from investments	(94.8)	(123.6)	(132.5)	-	-
CFF					
Share issuance, net	(0.1)	88.6	59.4	-	-
Loans, net of repayments	91.5	29.3	66.0	-	-
Dividends	(49.4)	(55.7)	(58.9)	(62.3)	(57.6)
Others	-	-	-	-	-
Cashflow from financing	41.9	62.3	66.5	(62.3)	(57.6)
Net change in cash	1.0	(4.2)	8.3	(2.7)	(3.6)
Effects of exchange rate	-	-	-	-	-
Ending cash	21.0	16.8	25.0	22.3	18.7

Source: Company, Phillip Securities Research (Singapore) Estimates

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

Balance Sheet

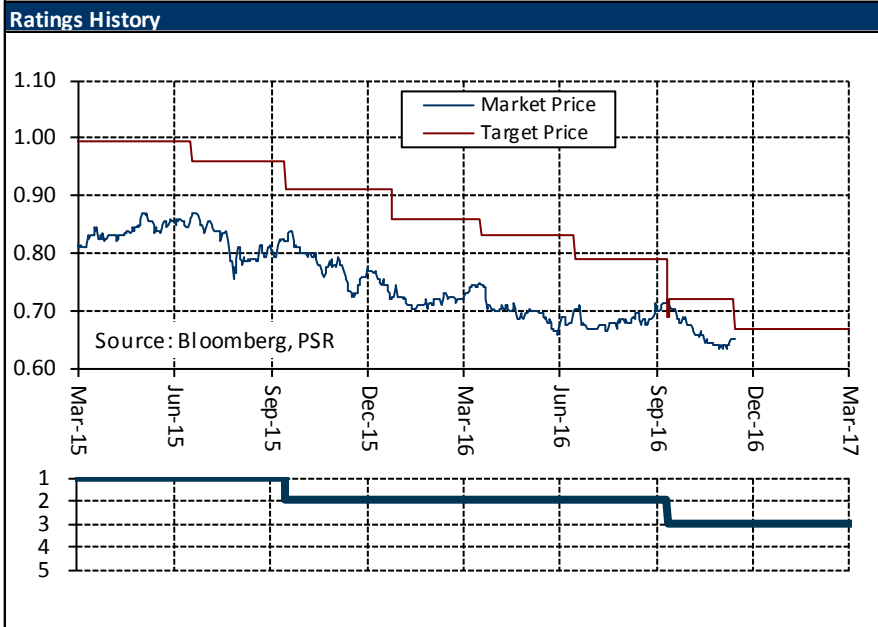
Y/E Dec, SGD mn	FY14	FY15	FY16e	FY17e	FY18e
ASSETS					
Investment properties	1,031	1,191	1,291	1,291	1,291
Inv. Propty. Under Devmnt.	-	-	-	-	-
Others	1.0	3.4	3.4	3.4	3.4
Total non-current assets	1,032	1,194	1,295	1,295	1,295
Cash	21.0	16.8	25.0	22.3	18.7
Trade receivables	0.8	2.4	2.5	2.6	2.6
Others	0.5	1.2	1.3	1.3	1.3
Total current assets	22.3	20.4	28.8	26.2	22.6
Total Assets	1,054	1,215	1,323	1,321	1,317
LIABILITIES					
Trade payables	8.7	10.1	10.4	10.9	10.8
Borrowings	94.6	-	-	155.0	97.5
Rental deposits	2.5	2.7	2.7	2.7	2.7
Others	0.1	-	-	-	-
Total current liabilities	105.9	12.8	13.1	168.6	111.1
Borrowings	274.3	398.5	464.5	309.5	367.0
Rental deposits	23.0	24.2	46.0	47.2	47.0
Others	-	33.0	1.0	1.0	1.0
Total non-current liabilities	297.3	455.7	511.5	357.7	415.0
Total Liabilities	403.2	468.6	524.6	526.3	526.1
Net assets	650.8	746.0	798.8	794.5	791.1
Represented by:					
Unitholders' funds	650.8	746.0	798.8	794.5	791.1

Valuation Ratios

Y/E Dec	FY14	FY15	FY16e	FY17e	FY18e
P/NAV (x)	0.99	0.94	0.85	0.86	0.87
P/DPU (x)	12.7	11.5	10.7	11.2	12.0
Distribution Yield (%)	7.9	8.7	9.3	8.9	8.3
NPI yield (%)	5.6	6.1	5.7	5.7	5.5

Growth & Margins (%)

	FY14	FY15	FY16e	FY17e	FY18e
Growth					
Revenue	16.4%	2.9%	4.8%	-0.6%	
Net property income (NPI)	18.2%	5.0%	3.4%	-2.8%	
Distributable income	15.3%	-4.9%	10.5%	-6.2%	
DPU	4.7%	-6.4%	-4.4%	-7.0%	
Margins					
NPI margin	84.2%	85.4%	87.1%	85.9%	84.0%
Key Ratios					
Net Debt or (Net Cash)	348.0	381.8	439.5	442.2	445.8
Aggregate Leverage	35.0%	32.8%	35.1%	35.2%	35.3%



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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