Property Sector
2014 Real Estate Themes:
Weak residential, Resilient Retail

Phillip Securities Research Pte Ltd
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Report type: Update

Sector Overview
The Property Sector in our Singapore coverage consists of Property developers/holding companies, engaged in businesses of property development, trading, ownership/management and services.

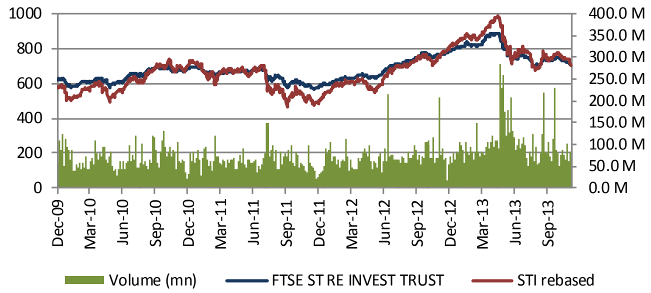
Policy: TDSR & beyond
In 1H2014, we may see the government further refining the property cooling measures. Since the onset of the first round in September 2009, the government has steadfastly pushed out waves of property cooling measures over the past 4 years. To date, this translated to a rough 6.25 months interval between each round. The longest interval between two cooling measures was about 11 months and that the most recent policy, which saw the introduction of Total Debt Service Ratio, was introduced in June 2013. Given the Singapore Government's consistent track record, its well established policy formulation/review process and the current market conditions, we are expecting further revisions/additions to the policies, sooner rather than later.

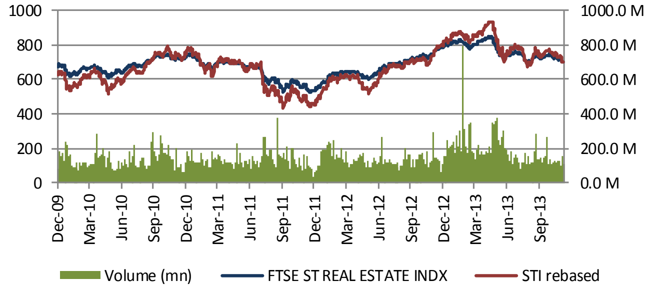
The price of private residential units has not corrected to our forecasted levels. We draw this conclusion by comparing the yields between the other real estate sub-sectors. Current residential rental yields stands at 1.8%-2.7%. This represents a huge deviation from other real estate classes which are enjoying substantially higher returns, at 5.1%-7.3%. Residential sector should experience a further pull-back in capital values.

The government has expressed its intention to see sustainable growth in residential prices beyond the horizon. However, anecdotal evidence and in-house estimates shows that the house price-to-income ratio is c.35x as compared to 8x-22x for developed countries. We do not expect full reversion of this ratio to Singapore's historic long term average of c.26x-29x. However, the residential segment is currently undergoing fundamental changes, and we believe occupant-buyers will behave more rationally in the midst of a shaky longer term residential outlook.

In our opinion, the Government will be incremental in its approach toward residential segment from here onwards. As more fine-tuning property cooling measures is introduced, the various players are increasingly being kept "in-line". Previous rounds of property cooling measures had taken out the sources of financing, the sellers, and the potential buyers (both local and foreign). The most recent policy starts to string up the various policies by enforcing more stringent adherence to the rules. With the players much weakened, the outlook looking increasingly unappetizing, the market will await further insights from the government before any signs of recovery will be in sight.

Property Sector





Source: Bloomberg

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Company	Price	Book Value	Comments
City Development limited	S$9.470	S$8.00	Heavy exposure to Singapore residential
Capitaland	S$2.960	S$3.74	Company focusing on China developments. Deepest discount to valuation.
Keppel Land	S$3.370	S$4.15	Largest exposure to china residential. Poised to benefit from CN residential earnings.

Company	Price	TP	Comments
OUE	S$2.460	S$2.82 Accumulate	Potential listing of OUE Commercial REIT Huge war chest to embark on new projects
Amara	S$0.545	S$0.74 Buy	Completing of overseas projects. Expecting growth to recurring income
Ho Bee	S$2.030	2.45 Accumulate	Revaluation gain expected with strong performance of The Metropolis

Market Fundamentals –Housing Supply Overhang

Over the next 3 years, it would be an oversupply situation within the Singapore residential segment. Inclusive of both public and private sectors, we project the physical completion of 168,200 residential units from 2014 to 2016 (please refer to figure 2). In contrast, we look into the underlying *'real'* demand that stems from population growth. We estimate that the increase in population will provide take-up of c. 71,400 residential units. Beside the local government intervention in the aforementioned portion, the oversupply situation will be a major factor in the gloomy outlook for residential.

What are some factors that could potentially change the grim outlook for residential segment?

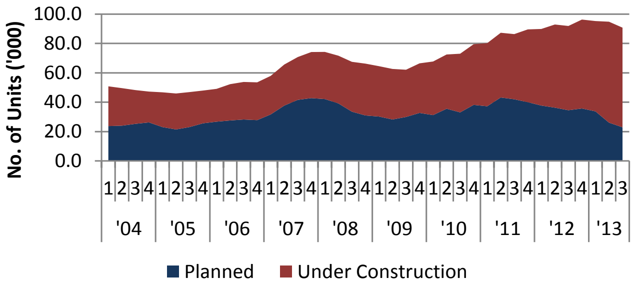
1. The mass market continues the trend of having lesser individuals per residential units. Currently, based on the total residents and the total residential units, the ratio stands at an estimated 4.07 individuals per unit. We do acknowledge that this ratio is exhibiting a downwards trend. However, for the market to absorb the upcoming 3-yr supply, we would need this ratio to lower a further 7%, at 3.78 individual per unit. We do foresee residents continuing to favor having fewer individuals under a single roof. Nonetheless, with the aging population and the affordability issues, the ratio should not decrease much further. Within these 3 years, this factor will not substantially negate the oversupply effects.

2. Investment capital influx. Under current conditions, there would be an excess of close to 100,000 residential units. Initially, we analyzed the demand stemming from the occupant-buyers, with neglecting potential absorption from investment capital. While opportunistic investment-buyers could possibly still pick up residential units in the market, most investors would steer clear in the midst of unattractive rental yields, policy risks and a likely oversupply situation.

Major players' comments on residential market:
CDL – expect residential prices to correct further
Capitaland – expects prices and sales volume to moderate from measures but long term prospect are in-tact. Remain optimistic.
Keppel Land – remain cautious. Highly selective of sites/projects going forward.

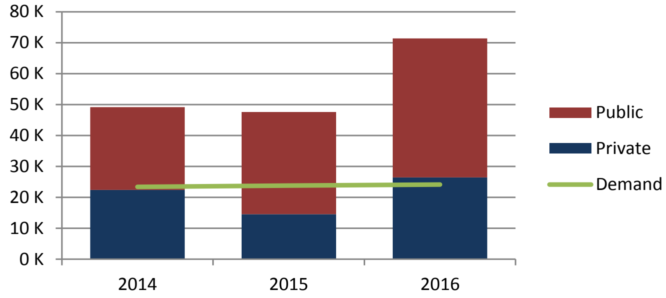
Impact on Singapore Developers
Amongst the "big-3" developers, City Development Limited (CDL) has the greatest exposure to the Singapore residential market, with 40-45% of their Gross Asset Value (GAV) accruing to this sector. The company's heavy bet on this sector previously, saw the company amassing a huge land bank in Singapore, estimated to yield more than 12,000 residential units in total. In contrast, Keppel Land and Capital Land have only 10% - 14% of their GAV allotted to Singapore residential sector. Any further deterioration on the policy front or the supply situation will be a major factor in the price movement of CDL, in the short term. Management has turn prudent and

Figure 1: Pipeline Units (Private - Planned and Under Construction)



Source: URA, PSR

Figure 2: Upcoming Residential Units Supply & Demand



Source: URA, PSR

is seeking to diversify into other sectors and geographic areas. We look forward to seeing CDL's ability to secure value accretive projects.

Interest rates and effects

While the broad market has long accepted that interest rates will increase eventually, the price movement of real estate related stocks prices has not been fully factored in the interest rates effects. Qualitatively, an increase in interest rates implies a higher discount rate, utilized towards forecasted cash flow returns. This will lower the valuations of assets. While it awaits the imminent QE tapering, the market will continue to grapple with the change in outlook of interest rates, we expect to see some weakness in real estate companies with a large asset base.

Does this mean, we should all avoid every counter with a large fixed asset? No, the more prudent real estate companies have taken up fixed rate bonds over the next 2-3 years. In addition, Real estate stocks valuations are currently at its historic low. We should focus on companies that have strong growth impetus, either organically or through acquisitions. The increase in intrinsic valuations through increasing value accretive purchases or through asset enhancement initiatives can possibly negate the downward effects of increased interest rates.

4) Why Retail?

We continue to favor companies that are exposed to the retail and hospitality sub-sectors.

Retail

Rental rates are expected to grow at c.5% pa as there is strong demand for retail space. International brands continue to seek entry/expansion into local retail scene as they continue to view the consumer base favorably. This can be evidenced by the recent Bedok Mall, which opened on 3rd December 2013. The shopping mall is fully leased and includes popular brands like UNIQLO, Cotton On, FairPrice Finest and Charles & Keith. Another CapitaMallAsia's shopping mall, Westgate, will open in late 4Q13/early 1Q14. Upcoming retail malls in 2014 should see strong pre-commitment levels and command higher rental rates.

In 2014, existing retail landlord will continue to actively reinvent their mall through constant revising of tenant mix and embarking on asset enhancement initiatives. Retail yields have proven to be highly resilient, supported by strong macroeconomic fundamentals. Island wide retail occupancy will likely remain above 90%.

Hospitality

While a large supply of new hotel rooms is expected in 2014, majority of the supply will be clustered within the midscale hotels. The luxury hotel segment is relatively unaffected and should see current high room rates sustaining throughout 2014. The same cannot be said for the midscale hotel. While competition stiffens, the new or

Figure 3: Government Securities Yield Graph

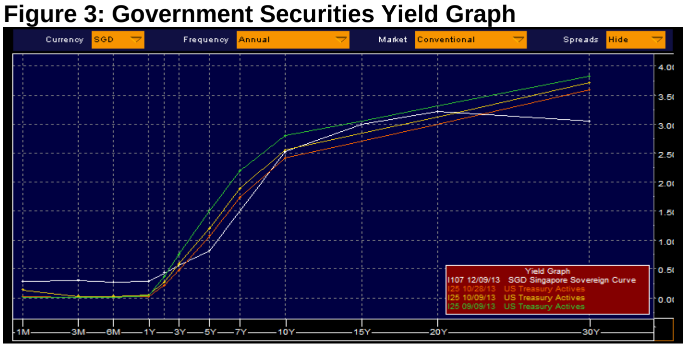
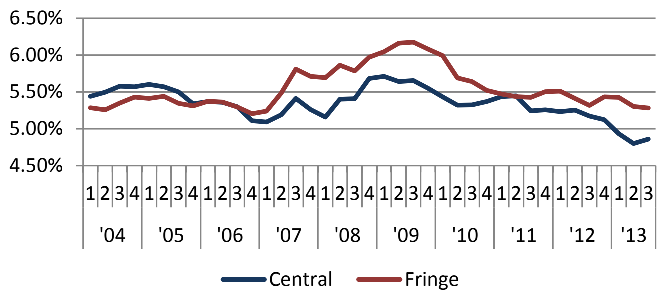
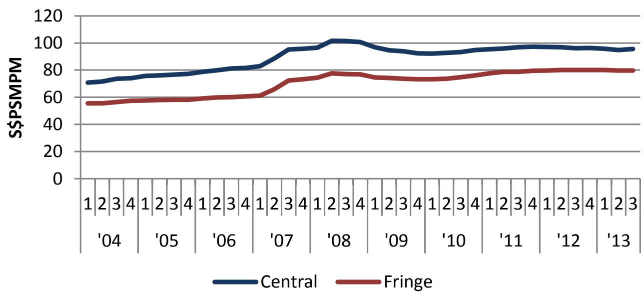


Figure 4: Retail Net Rental Yields



Source: URA, PSR

Figure 5: Retail Rental Value



Source: URA, PSR

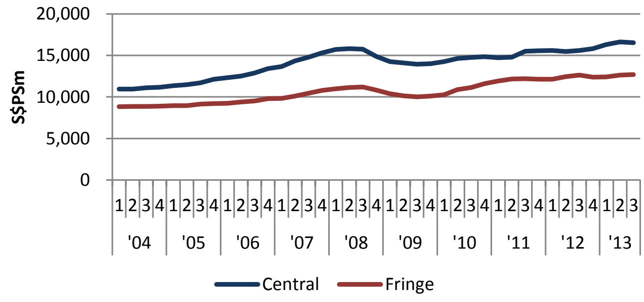
newly refurbished ones should stand out. In 2014, we anticipate a higher number of mid-scale hotels embarking on asset enhancement initiatives (AEIs), in an attempt to reinvent/reposition the hotel. The increase in total number of room nights will be slightly mitigated by the retiring of existing stock, for AEIs. We expect islandwide available room nights to see an 8.2% increase in 2014.

Amara Holdings
We continue to favor Amara Holdings as the market continues to deeply undervalue the company's assets. While there are concerns that the recent Carlton Hotel opening beside Amara Singapore (flagship hotel) will post strong competition, we continue to believe that the new hotel will start to bring about greater activities in the vicinity and improve the overall attractiveness of hotels in the core-CBD area. This bodes well for Amara Holdings. Additionally, the completion of its Bangkok hotel and on-schedule construction of its Shanghai mixed development, will provide impetus for the market to realize the company's fair value. Thus, we have a BUY call on Amara Holdings, with Fair Value at S$0.74.

Comments on China residential

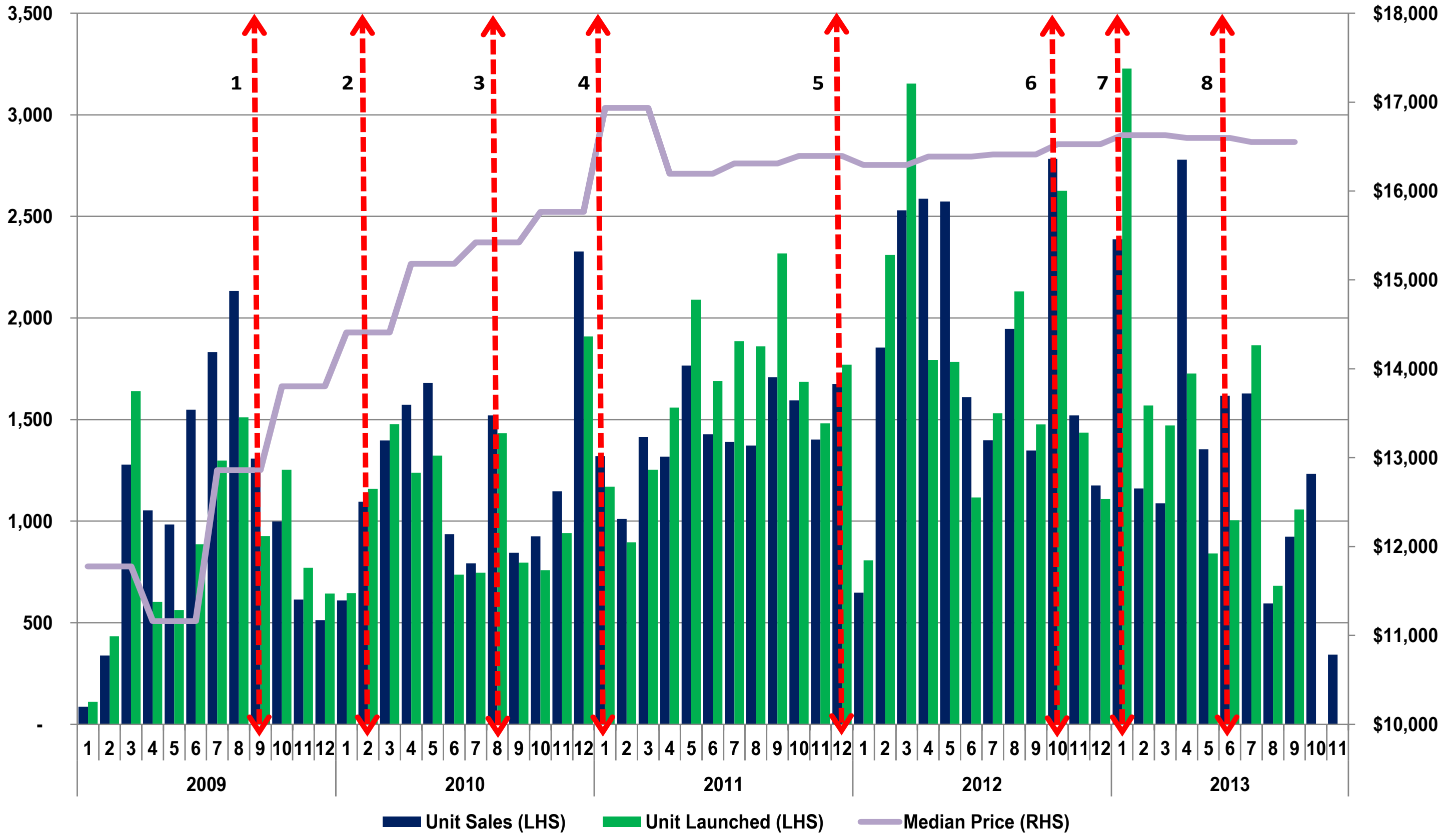
- Residential prices are continuing to trend upwards
- Tier 1 cities: Governments are still issuing property cooling measures. Price growth are still positive, but slowing down.
- Tier 2 cities: Governments are seemingly starting to be active on the policy front, with the aim of avoiding a housing price hike.
- Urbanization is still the main theme of the day, driving the increase in residential prices. Developers are speeding up development of their land bank in China.
- Investment capital is still a net inflow for the real estate sector of the economy.

Figure 6 Retail Capital Value



Source: URA, PSR

Fig 7: Total non-landed residential properties launch/sold by developers and dates of cooling measures introduced previously



Source: URA, PSR

No.	Date	Description
1	14 September 2009	Removal of Interest Absorption Scheme and Interest-Only Housing Loans
2	19 February 2010	Introduce Seller's Stamp Duty (SSD) on all residential properties and residential lands sold within 1 year of purchase Lower Loan-to-Value (LTV) limit to 80% for all housing loans provided by financial institutions regulated by Monetary Authority of Singapore (MAS)
3	30 August 2010	Increase holding period for imposition of SSD from 1 year to 3 years For buyers with 1 or more outstanding housing loans, Increase minimum cash payment from 5% to 10% of valuation limit, and decrease the LTV limit from 80% to 70%
4	13 January 2011	Increase holding period for SSD from 3 years to 4 years Raise SSD rates to 16%, 12%, 8% and 4% for sale of properties in the 1st, 2nd, 3rd and 4th year respectively Lower the LTV limit to 50% on housing loans granted to purchasers who are not individuals Lower LTV limit on housing loans granted to individuals with 1 or more housing loans from 70% to 60%
5	7 December 2011	Foreigners and non-individuals buying residential property will pay Additional Buyer's Stamp Duty (ABSD) of 10% Permanent Residents (PRs) owning one and buying second or subsequent residential property will pay ABSD 3% Singapore Citizens owning 2 and buying third or subsequent residential property will pay ABSD 3%
6	5 October 2012	Max tenure of all new residential property loans will be capped at 35 years. Loans with >30 years tenure, or extends beyond retirement age 65 years old, there will be a tighter LTV limits – 40% for borrower with one or more outstanding residential property loan & 60% for borrower with no outstanding loan.
7	11 January 2013	Additional Buyer's Stamp Duty (ABSD) rates will be: - Raised between 5 and 7 percentage points across the board. - Imposed on Permanent Residents (PRs) purchasing their first residential property and on Singaporeans purchasing their second residential property. Loan-to-Value limits on housing loans will be tightened for individuals who already have at least one outstanding loan, as well as to non-individuals such as companies. Min cash down payment for individuals applying for a second or subsequent housing loan will also be raised from 10% to 25%.
8	28 June 2013	TDSR – any property loan not to exceed TDSR threshold of 60%

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