

# Singapore REITs

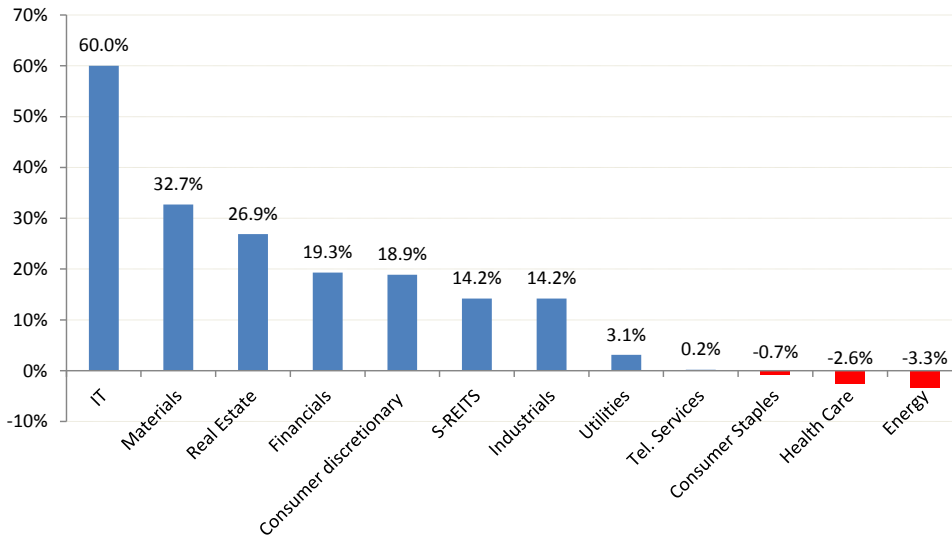
## The 10 most commonly asked questions

### SINGAPORE | REAL ESTATE (REIT) | UPDATE

6 October 2017

The S-REIT sector has returned 14.2% in the first 9 months (excluding dividends) this year despite the threat of rising interest rates. With interest rate continuing to rise, will S-REITs continue to perform? We answer some of the common questions S-REIT investors have in mind in the current environment.

**Figure 1: S-REITs returned 14.2% in 9M17, the sixth best performing sector within STI**

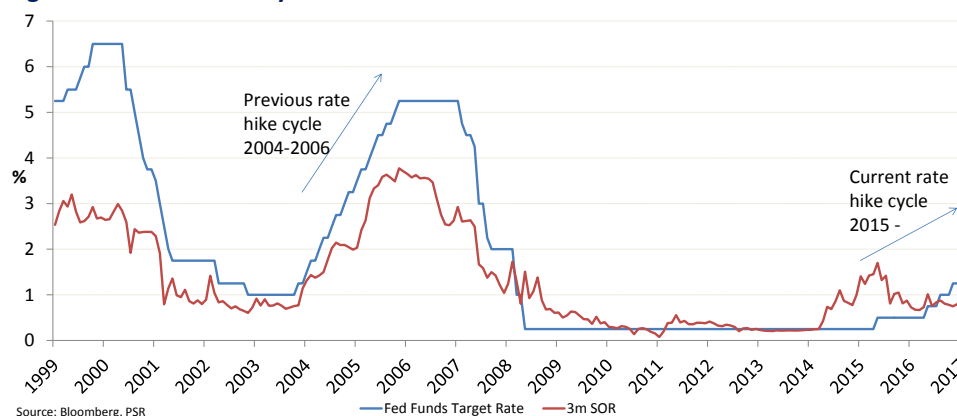


Source: SGX Stockfacts, Bloomberg, PSR

### 1. What is the impact of US rate hikes on REITs and is it still safe to buy REITs?

We are less worried about tightening monetary policies and US rate hikes if they are in response to better economic data instead of runaway supply-side inflation. The previous rate hike cycle from 2004-2006 saw phenomenal returns for S-REITs with a CAGR of 26.5% vs STI's 15.9% (Figure 3). This demonstrates that REITs can perform in rising interest rate environments. What is important is whether the accompanying economic growth is able to drive rental income higher for the REITs, which could then offset the increased borrowing costs for the REITs.

**Figure 2: Last rate hike cycle occurred in 2004-2006...**



Source: Bloomberg, PSR

### CapitaLand Commercial Trust ACCUMULATE

BLOOMBERG CODE	CCT SP
CLOSING PRICE	SGD 1.67
FORECAST DIV	SGD 0.09
TARGET PRICE	SGD 1.80
<b>TOTAL RETURN</b>	<b>13.0%</b>

### Mapletree Industrial Trust ACCUMULATE

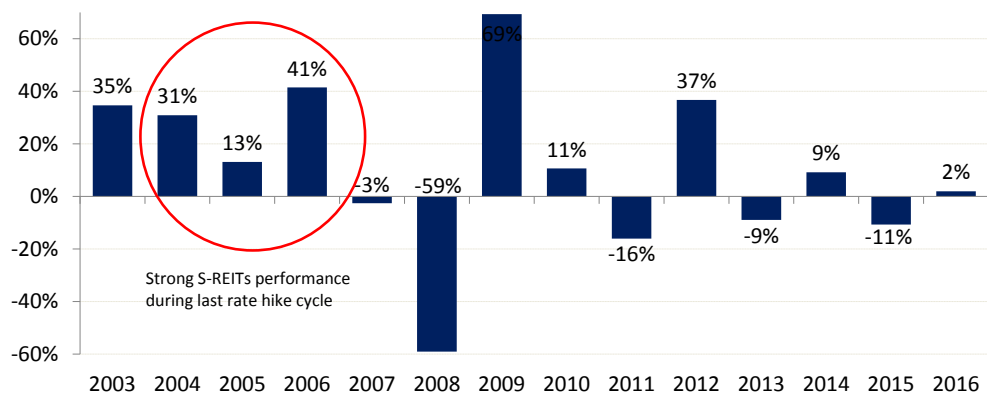
BLOOMBERG CODE	MINT SP
CLOSING PRICE	SGD 1.87
FORECAST DIV	SGD 0.11
TARGET PRICE	SGD 1.98
<b>TOTAL RETURN</b>	<b>12.0%</b>

### Ascendas REIT ACCUMULATE

BLOOMBERG CODE	AREIT SP
CLOSING PRICE	SGD 2.67
FORECAST DIV	SGD 0.16
TARGET PRICE	SGD 2.86
<b>TOTAL RETURN</b>	<b>13.0%</b>

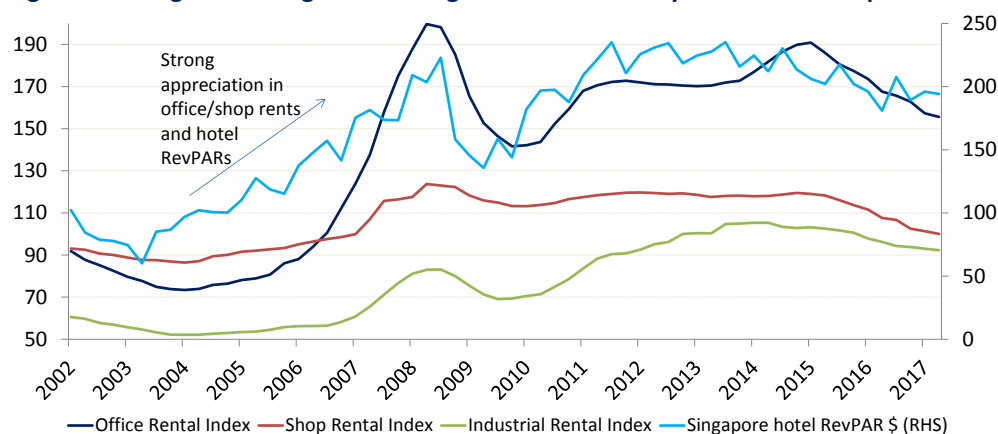
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**Figure 3: .... But S-REITs managed a CAGR of c.26.5% during the period (2004-06)**



Source: Bloomberg, PSR

**Figure 4: Strong economic growth during the last rate hike cycle drove rents upwards**



Source: Bloomberg, PSR

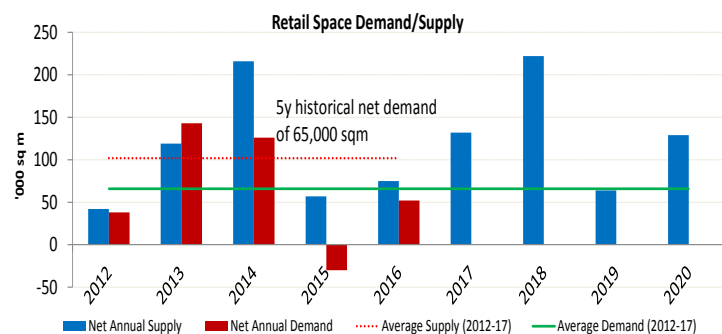
**2. Apart from higher financing costs, what other ways do higher interest rates affect REITs?**

Increase in long-term interest rates decreases the yield appeal of REITs as an asset class. However, in terms of financing costs, due to the competitive banking landscape so far, banks are tightening spreads for loans to REITs despite slightly rising SORs over the past 2 years. This has kept borrowing costs in check for REITs. The SGD strength also meant the uptick in SOR rates had remained relatively muted over the last two years.

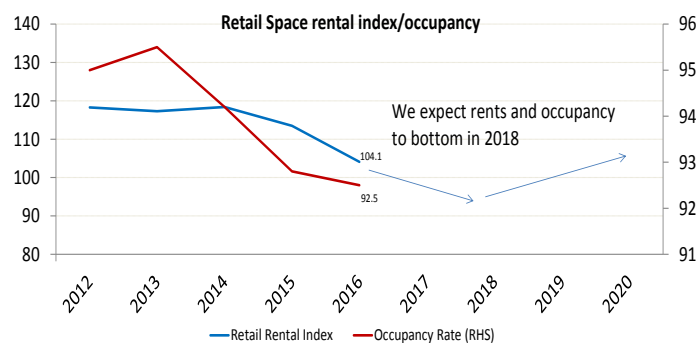
**3. What is the outlook for each S-REIT sector – retail/commercial/industrial/hospitality?**

Apart from retail, all other sectors - office, industrial and hotels - generally face a positive scenario of tapering supply after a peak/surge in supply in 2017. The easing of supply post-2017 should build a base for rentals to start climbing up (Figure 5 to 12).

**Figures 5 and 6: Retail is facing increased supply amidst falling demand and the threat of online retailers like Amazon. Nonetheless, retail sales showing signs of stabilization. We expect rents to bottom in 2018.**

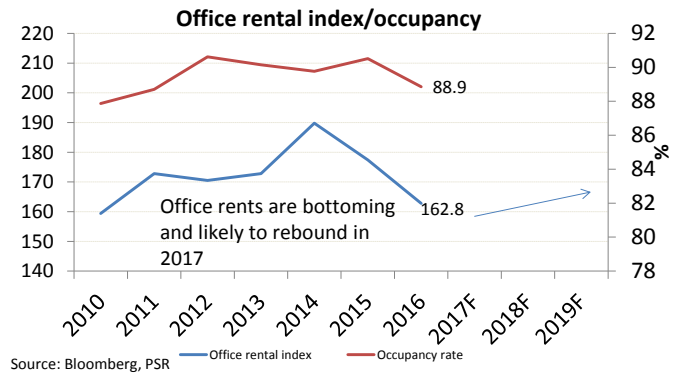
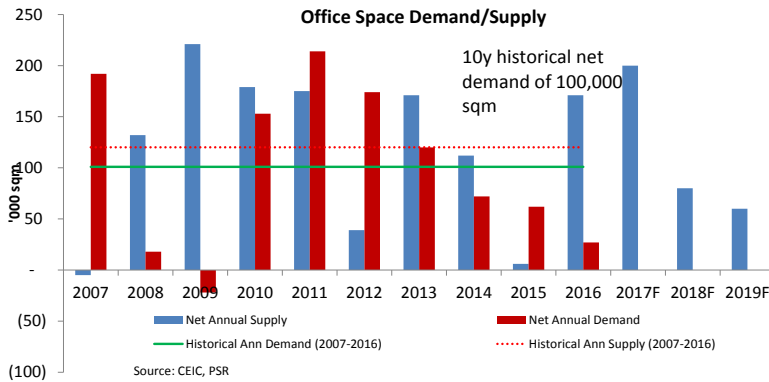


Source: Bloomberg, PSR

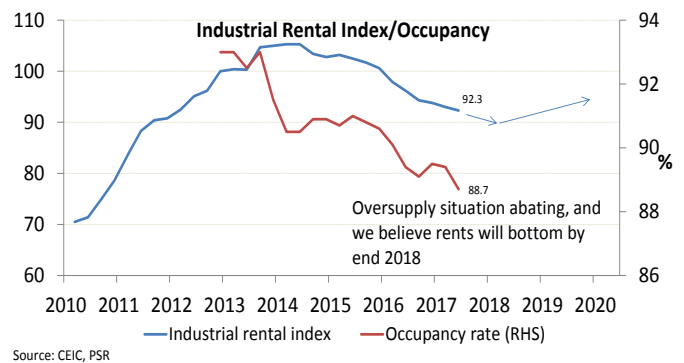
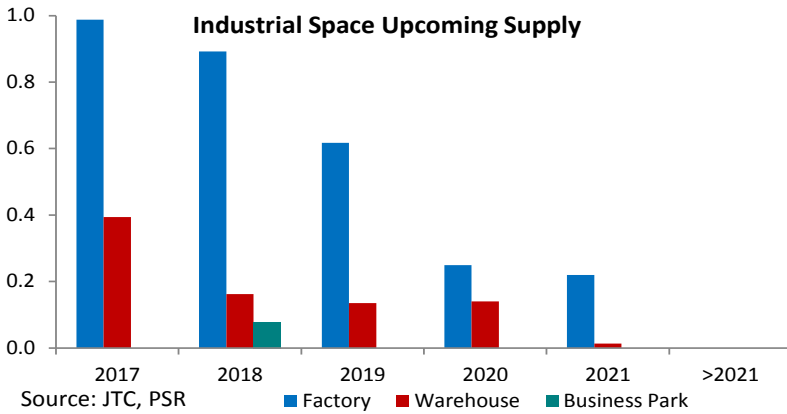


Source: Bloomberg, PSR

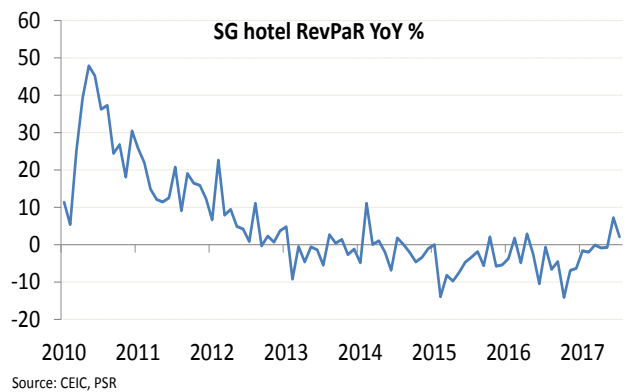
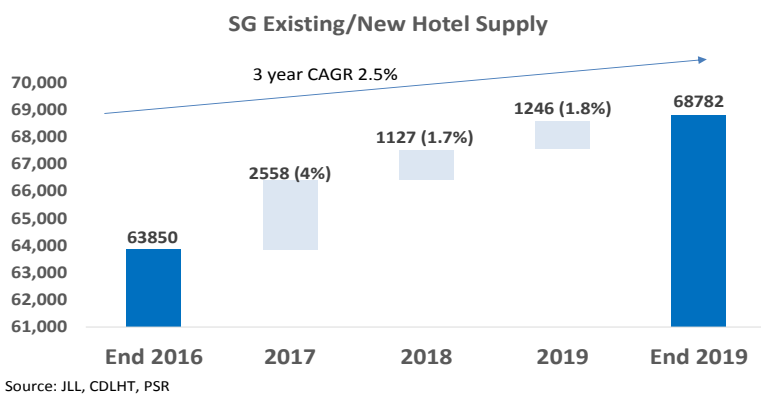
**Figures 7 and 8: Office Supply tapering off after 2017. Office rents showing signs of stabilising. We expect office rents to rebound this year**



**Figures 9 and 10: Industrial Supply is tapering off after 2017. Industrial activities are also picking up. We expect industrial rents to bottom by end-2018**



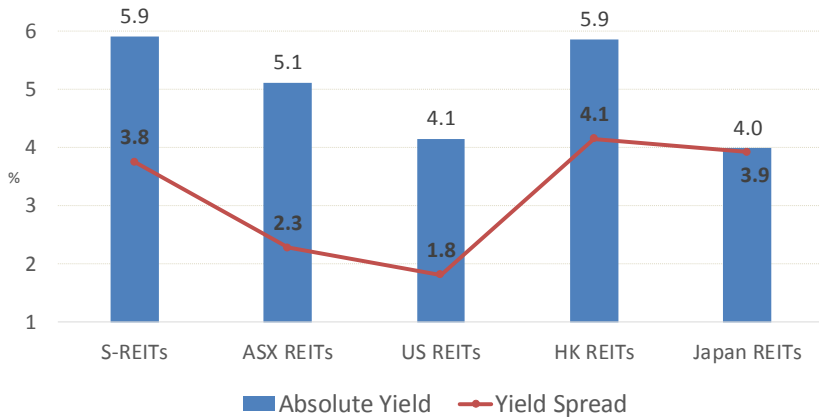
**Figures 11 and 12: Hotel Supply is tapering off after the 4% increase in 2017. SG Hotel RevPAR showing signs of stabilisation over the past half year.**



**4. How does SG REITs compare with regional REITs?**

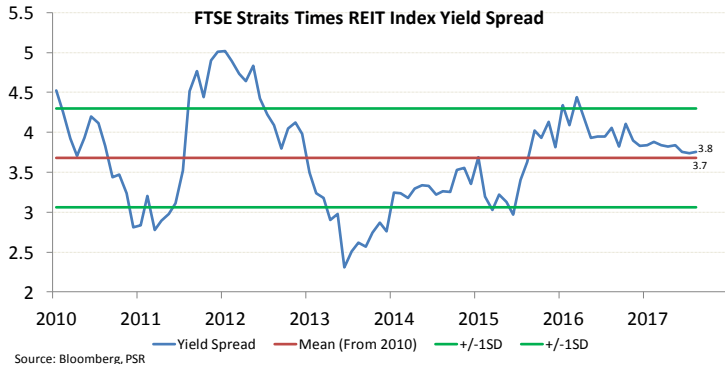
On an absolute yield basis, S-REITs trade at the highest yield of 5.9% vs the other major REIT markets (Figure 13). Nonetheless, the yield spread of 3.8% is third behind that of HK and Japan REITs. With the exception of Hong Kong (using data available from 2012-present), the yield spreads for all other major REIT indices are trading above post-GFC average (Figures 14-18).

**Figure 13: Regional REIT markets absolute and yield spreads - S-REITs offer the highest absolute yield and also one of the highest yield spreads**



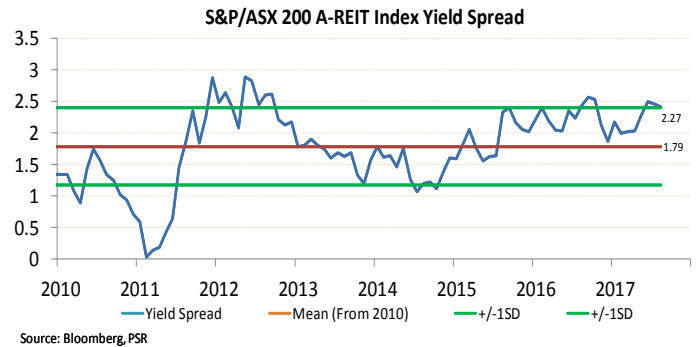
Source: Bloomberg, PSR

**Figure 14: S-REITs yield spread at 3.8%, close to post-GFC average spreads**



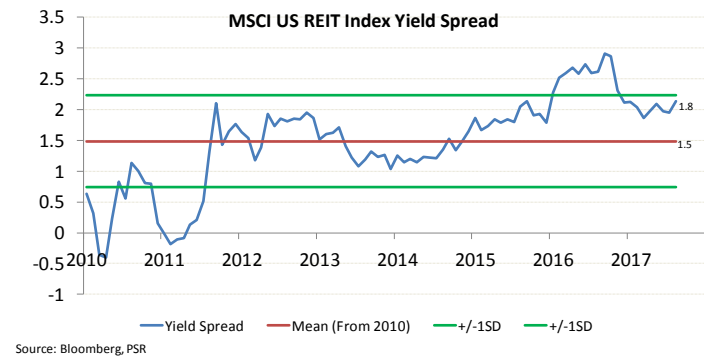
Source: Bloomberg, PSR

**Figure 15: Australian REITs yield spread at 2.3%, close to +1 s.d.**



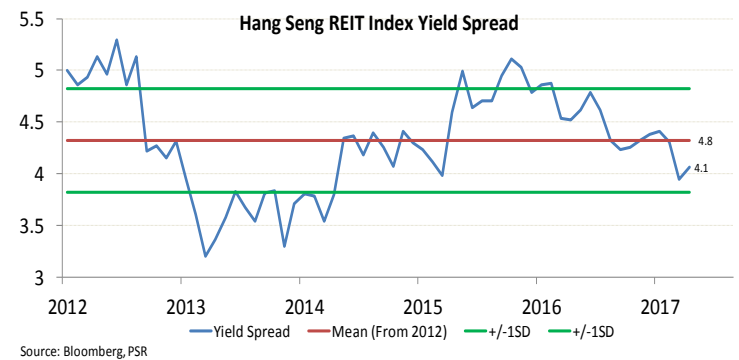
Source: Bloomberg, PSR

**Figure 16: US-REITs yield spread at 1.8%, close to +1s.d.**



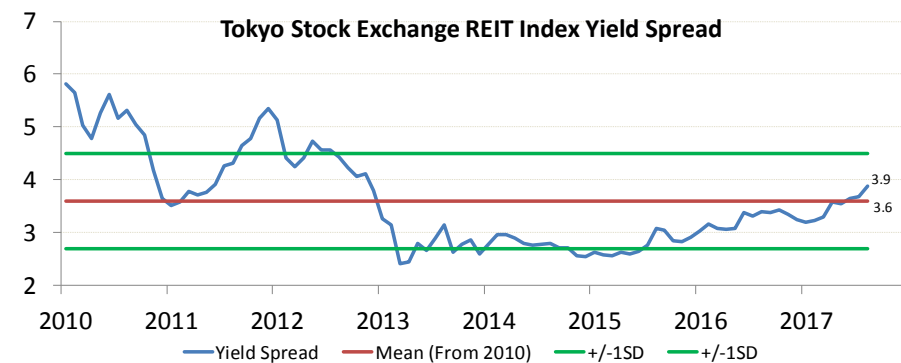
Source: Bloomberg, PSR

**Figure 17: HK-REITs yield spread at 4.2%, below post-GFC average spreads (using data available from 2012)**



Source: Bloomberg, PSR

**Figure 18: J-REITs yield spread at 3.9%, above post-GFC average**

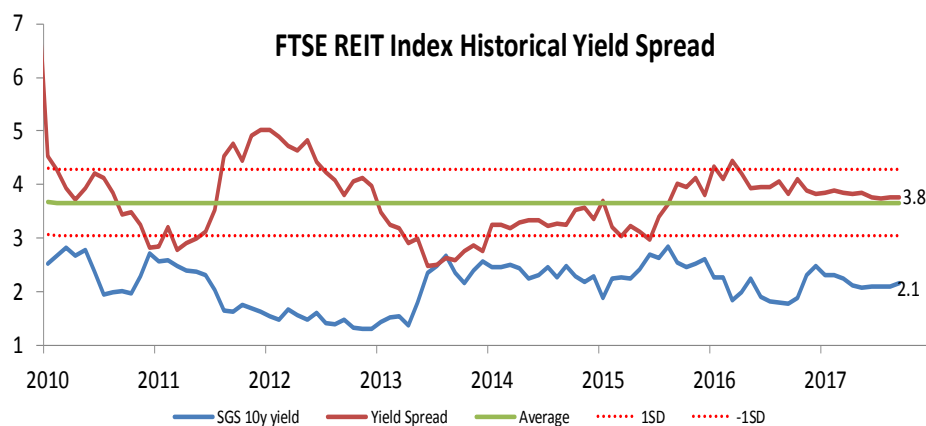


Source: Bloomberg, PSR

### **5. Is valuation attractive from a yield angle? How does S-REITs' valuation stand now compared with historical valuations?**

S-REITs currently trade at a yield spread of 3.8 (S-REIT average yield 5.9% - Risk-free rate 2.1%) which is around post-GFC (2010-present) average (Figure 19).

**Figure 19: S-REITs yield spread close to post-GFC average**



Source: Bloomberg, Phillip Securities Research (Singapore)

### **6. Is book value a good way to judge if a REIT is under or overvalued?**

Price/NAV is one metric to determine the valuation of a REIT. It is useful to across the industry vs peers and also compares a REIT's own historical P/NAV vs the economic outlook too. Big cap REITs typically trade at higher valuations than smaller REITs. Mapletree Industrial, for example, trades at an average Price/NAV of 1.23 post-GFC. Reasons being these big cap REITs typically are able to obtain lower costs of funding, which makes it easier for accretive acquisitions. They also enjoy economies of scale in the management of a larger portfolio. A more meaningful comparison is if you compare it with a basket of similar size market cap peers instead of widely across the sector. Even similar size companies can have portfolios with different geographic exposures too so it is important to take that into account when comparing. When comparing over its own historical P/NAV investors should note if the macro environment is similar to the historical period and whether changes in the environment can justify it trading at a premium/discount to the average over the historical period.

So a REIT trading at a huge discount to book and high yield may mean that the market is pricing in potential future deterioration in rental power of the portfolio properties and not necessarily imply it is a value buy. Investors will need to assess market conditions to judge if the discount/premium is warranted.

### **7. Growth in global economies is accelerating. Wouldn't investors be better off looking at growth stocks instead of stable stocks like REITs/telcos/utilities?**

Unlike telcos and utilities whose fees and tariffs are more highly regulated necessities, REITs are exposed to commercial rents and prices which are more market-driven, based on demand and supply. Therefore REITs will also be able to capture upside in rents in an improving economy, and at the same time still continue paying out at least 90% of rental income. This would appeal to investors desiring stable passive income, and at the same time participate in growth from improving economies.

### **8. Is a REIT with a larger portfolio of freehold properties better than another REIT with a portfolio of shorter leasehold properties?**

Land tenure is only one consideration but just by looking at the land tenure of the REIT portfolio alone is insufficient to conclude if the portfolio is better or worse off. Typically, when we compare like-for-like two properties in the same vicinity, one with a freehold tenure vs another with a shorter leasehold, the freehold building usually trades at a lower

cap rate (i.e. higher valuation, valuation is inversely related to cap rate) than the shorter leasehold property. So the NAV of the REIT would have already priced in the freehold factor. Another example of REIT pricing already reflecting the shorter land tenures is this: one of the reasons industrial REITs trade at higher yields is due to the fact that industrial properties in Singapore tend to have shorter 30-year leases vs retail or office properties. The higher yield compensates investors for the shorter tenure and the lower potential for capital gains over the long run.

**9. How would you calculate and compare REITs' metrics and duration vs fixed income in falling, flat, rising interest rate environments?**

Unlike fixed income, REITs do not have fixed "maturities", so calculating a duration that measures the sensitivity of the REIT's price to fluctuations in interest rates is not as straightforward. An easier metric for investors to watch out for instead is the sensitivity of the REIT's earnings (not price) to fluctuations in interest rates or forex movements in the annual report under "sensitivity analysis".

**10. What are key risks of investing in REITs now?**

Accelerating inflation could lead to faster than expected rate hikes/tightening by the Fed. So far inflation has been tepid despite improving economic data, presenting a Goldilocks situation of moderate economic growth with low inflation that is able to accommodate market-friendly monetary policies. This has supported the strong performance in S-REITs. Any sharp upturn in inflation could reverse these trends.

Figure 20: REIT universe and PSR coverage

	Mkt. Cap. (\$\$mn)	Price (\$\$)	PSR RATING	PSR TARGET PRICE (\$\$)	P/NAV	Trailing yield (%)	Total Returns YTD (%)	Gearing (%)	% of debt on fixed rate	ROE (%)	Average borrowing cost (%)	% debt expiring in 2017/current FY	% debt expiring in 2018/next FY	Year End
<b>Healthcare</b>														
PARKWAYLIFE REAL ESTATE	1,627	2.69			1.57	4.73	18.81	37.4	99.0	9.5	1.1	2.0	0.0	December
FIRST REAL ESTATE INVST TRUST	1,058	1.36	NEUTRAL	1.32	1.34	6.34	11.56	31.0	90.9	5.4	4.1	34.1	35.9	December
<b>Hospitality</b>														
ASCOTT RESIDENCE TRUST	2,566	1.195			0.97	6.98	17.28	32.4	85.0	6.0	2.4	8.0	12.0	December
CDL HOSPITALITY TRUSTS	1,947	1.625			1.08	5.86	32.44	38.7	54.7	2.6	2.3	0.0	41.6	December
FAR EAST HOSPITALITY TRUST	1,269	0.685			0.76	6.09	18.14	32.8	71.0	1.8	2.5	5.1	28.2	December
OUE HOSPITALITY TRUST	1,434	0.795			1.04	6.46	27.07	38.2	100.0	1.7	2.8	0.0	34.2	December
FRASERS HOSPITALITY TRUST	1,384	0.75			0.99	6.58	18.76	34.1	87.8	6.2	2.5	14.4	15.4	September
ASCENDAS HOSPITALITY TRUST	947	0.84			0.95	6.76	23.87	32.7	78.3	5.2	2.8	11.6	37.0	March
<b>Retail</b>														
CAPITALAND MALL TRUST	7,163	2.02	NEUTRAL	2.01	1.07	5.36	15.07	34.7	97.0	9.0	3.2	3.9	15.7	December
MAPLETREE GREATER CHINA COM	3,276	1.165			0.93	6.36	25.37	39.4	76.0	11.1	2.7	0.0	18.0	March
SPH REIT	2,582	1.01			1.07	5.52	8.63	25.6	85.9	5.6	2.8	0.0	37.6	September
FRASERS CENTREPOINT TRUST	1,983	2.15	NEUTRAL	2.14	1.11	5.49	18.12	30.0	55.0	7.1	2.2	9.9	9.0	September
STARHILL GLOBAL REIT	1,680	0.77			0.82	6.52	7.00	35.3	99.0	5.5	3.2	0.0	19.3	June
CAPITALAND RETAIL CHINA TRUST	1,470	1.63	NEUTRAL	1.64	1.04	6.13	27.11	35.3	87.5	7.6	2.4	44.7	5.3	December
LIPPO MALLS INDONESIA RETAIL	1,228	0.435			1.18	8.09	26.75	30.6	70.0	3.7	N.A.	19.2	37.6	December
CROESUS RETAIL TRUST	899	1.165	ACCEPT OFFER		1.16	6.58	50.54	44.6	100.0	13.5	1.7	46.7	13.2	June
BHG REIT	369	0.74			0.89	7.22	21.70	32.4	45.0	7.3	3.7	37.2	5.2	December
<b>Commercial</b>														
CAPITALAND COMMERCIAL TR	5,970	1.655	ACCUMULATE	1.8	0.92	5.43	22.24	35.2	85.0	9.5	2.6	4.0	14.0	December
SUNTEC REIT	4,954	1.87			0.89	5.35	18.49	36.1	65.0	4.6	2.4	0.0	21.1	December
KEPPEL REIT	3,925	1.17			0.83	5.09	18.92	38.5	77.0	3.5	2.6	0.0	13.0	December
MAPLETREE COMMERCIAL TR	4,417	1.535			1.11	5.32	14.92	36.4	73.7	10.9	2.7	0.0	13.0	March
FRASERS COMMERCIAL TRUST	1,115	1.385			0.92	6.95	18.66	35.9	91.0	6.0	3.1	0.0	24.4	September
OUE COMMERCIAL REIT	1,110	0.72			0.82	8.80	7.92	36.4	80.7	5.4	3.4	0.0	46.6	December
MANULIFE US REIT	729	0.915			1.14	6.82	29.45	34.5	100.0	10.0	2.8	0.0	0.0	December
<b>Industrial</b>														
ASCENDAS REAL ESTATE INV TR	7,705	2.67	ACCUMULATE	2.86	1.30	5.83	23.67	33.9	72.2	8.0	2.9	18.0	21.5	March
MAPLETREE INDUSTRIAL TRUST	3,380	1.875	ACCUMULATE	1.98	1.32	6.18	18.39	29.8	72.8	10.9	2.8	10.0	16.2	March
MAPLETREE LOGISTICS TRUST	3,499	1.24			1.20	5.99	26.75	39.0	79.0	8.0	2.3	0.0	13.0	March
KEPPEL DC REIT	1,522	1.35	NEUTRAL	1.28	1.37	4.83	17.20	27.7	83.0	6.2	2.2	0.0	17.3	December
AIMS AMP CAPITAL INDUSTRIAL	915	1.43			1.03	7.55	14.44	36.3	83.3	1.1	3.6	0.0	40.6	March
CACHE LOGISTICS TRUST	793	0.845	NEUTRAL	0.86	1.10	8.57	12.04	43.4	62.9	-3.7	3.5	0.0	41.1	December
SOILBUILD BUSINESS SPACE REIT	735	0.7	NEUTRAL	0.73	0.98	8.46	21.09	37.9	87.0	0.2	3.4	0.0	32.3	December
SABANA SHARIAH COMP IND REIT	495	0.47			0.83	7.62	31.31	37.0	87.8	-6.6	4.0	15.7	24.5	December
VIVA INDUSTRIAL TRUST	912	0.94			1.19	7.71	32.43	39.1	85.2	7.6	3.9	0.0	19.6	December
ESR REIT	759	0.58			0.92	6.80	13.06	37.9	90.0	0.6	3.7	0.0	29.8	December
EC WORLD REIT	607	0.775			0.83	7.14	8.15	29.2	100.0	8.3	5.4	N.A.	N.A.	December
FRASERS LOGISTICS & INDUSTRI	1,632	1.08			1.16	6.55	22.94	29.3	79.0	4.1	2.8	0.0	0.0	September

Source: Bloomberg (Updated 4 Oct 2017), Debt data from Company Results as of 31 June 2017, PSR

## Appendix

**Figure 21: Notable upcoming shopping mall openings**

Project	Location	Estimated NLA (sq ft)	completion
Marina One (The Heart)	Marina Bay	140,000	2017
Singapore Post Centre	Paya Lebar	177,000	2017
Paya Lebar Quarter	Paya Lebar	340,000	2018
Northpoint City	Yishun	330,000	2018
TripleOne Somerset Podium	AlSomerset	70,000	2018
Jewel Changi Airport	Changi Airport	576,000	2019
Funan	North Bridge Road	324,000	2019
City Gate	Beach Road	76,000	2019
Total		2,033,000	

Source: URA, PSR

**Figure 22: Notable upcoming office openings**

Office Project	NLA (sq ft)	Location	Expected launch
Marina One (About 70% pre-committed)	1,876,000	Marina Bay	2017
EON Shenton (Strata Office)	101,000	Shenton Way	2017
Redevelopment of International Factors Building and Robinson Towers	145,000	Robinson Road	2018
Fraser's Tower	663,000	Shenton Way	2018
Redevelopment of Funan DigitalLife Mall	204,000	City Hall	2019
Park Mall Redevelopment	352,000	Orchard Road	2019
79 Robinson Road	500,000	Robinson Road	2020
Afra-Asia Building Redevelopment	154,000	Shenton Way	2020

Source: JLL, PSR

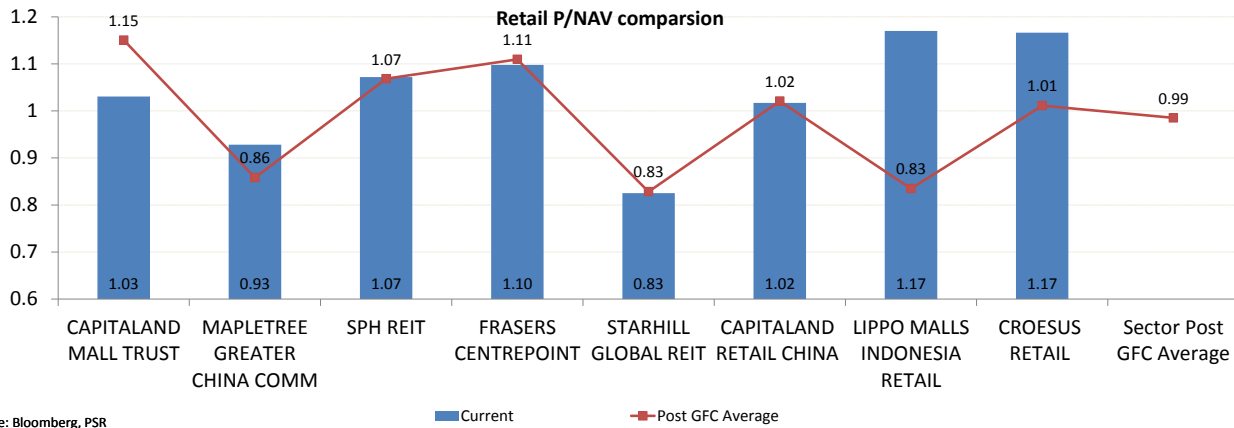
**Figure 23: Notable upcoming hotel openings from 2017-19**

Hotel Name	No of Rooms	Target Segment	Location	Expected launch
Sofitel Singapore City Centre	223	Upscale/Luxury	City Centre	3Q17
InterContinental Singapore Robertson Quay	225	Upscale/Luxury	City Centre	3Q17
Courtyard Marriott at Novena	250	Upscale/Luxury	Outside City Centre	4Q17
Andaz Singapore	342	Upscale/Luxury	City Centre	4Q17
Novotel Singapore on Stevens	254	Upscale/Luxury	City Centre	4Q17
Duxton House	49	Upscale/Luxury	City Centre	4Q17
Mercure Singapore on Stevens	528	Mid-tier	City Centre	4Q17
Grand Park City Hall	181	Mid-tier	City Centre	4Q17
YOTEL Orchard Road	610	Economy	City Centre	4Q17
Swissotel The Stamford	400	Upscale/Luxury	City Centre	2018
The Patina Capitol Singapore	157	Upscale/Luxury	City Centre	2018
Duxton Terrace	109	Upscale/Luxury	City Centre	2018
Raffles Hotel	103	Upscale/Luxury	City Centre	2018
Dusit Thani Hotel and Resort	208	Upscale/Luxury	Outside City Centre	2018
Aqueen Hotel Little India	81	Economy	Outside City Centre	2018
Aqueen Hotel Lavendar	69	Economy	Outside City Centre	2018
THE EDITION by Marriott	190	Upscale/Luxury	City Centre	2019
Caprr by Fraser @ China Street	306	Mid-tier	City Centre	2019
Yotel Changi Jewel	130	Economy	Outside City Centre	2019
Village Hotel Sentosa	620	Economy	Outside City Centre	2019

Source: JLL, PSR

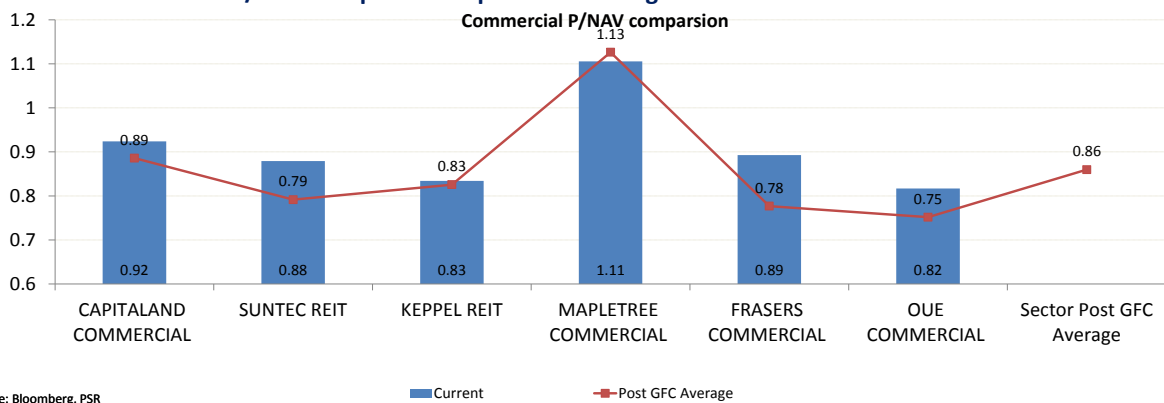


Figure 24: Retail S-REITs P/NAV comparison vs post-GFC average



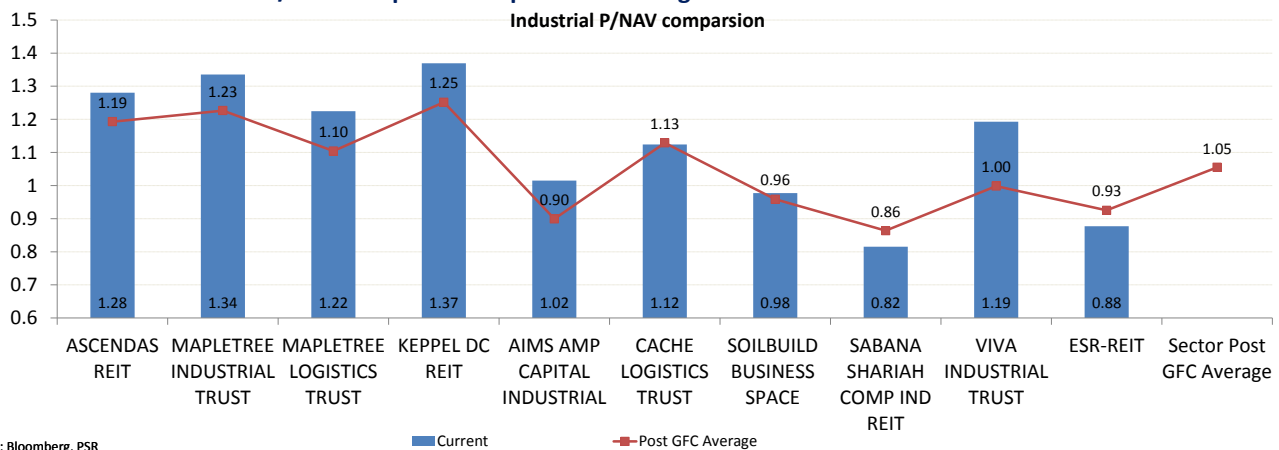
Source: Bloomberg, PSR

Figure 25: Office S-REITs P/NAV comparison vs post-GFC average



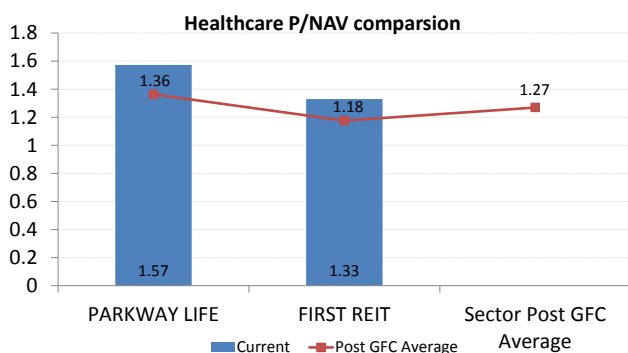
Source: Bloomberg, PSR

Figure 26: Industrial S-REITs P/NAV comparison vs post-GFC average



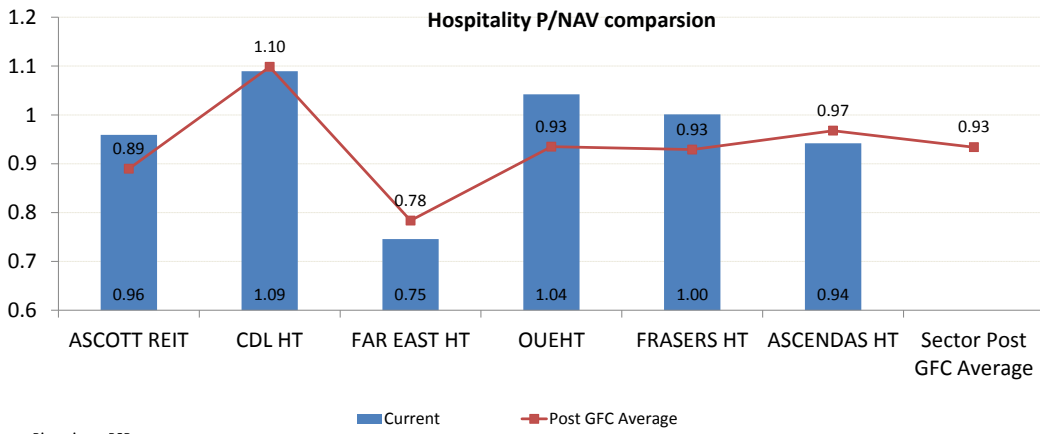
Source: Bloomberg, PSR

Figure 27: Healthcare S-REITs P/NAV comparison vs post-GFC average



Source: Bloomberg, PSR

Figure 28: Hospitality S-REITs P/NAV comparison vs post-GFC average



Source: Bloomberg, PSR

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