

Singapore REITs

First rate hike in 2018 and the implications for S-REITs



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SINGAPORE | REAL ESTATE (REIT) | UPDATE

26 March 2018

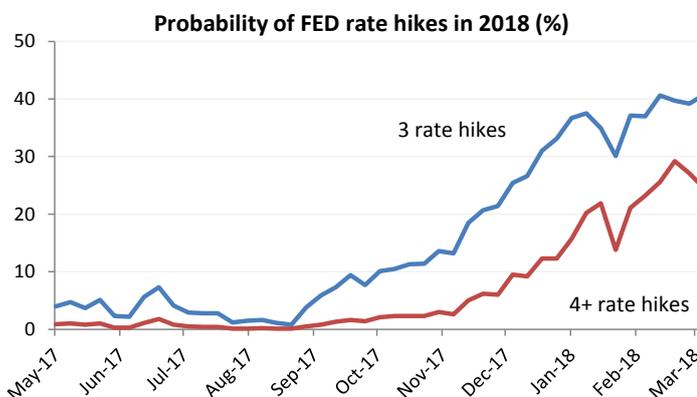
As widely expected, The Federal Reserve, raised rates by 25 basis points to 1.75% last week, while maintaining its forecast for three rate hikes total for 2018. Even as the Fed upgraded its outlook for the economy, it expects near term inflation in 2018 to remain benign, with both core and headline inflation projection coming in at 1.9%.

The news was largely shrugged off in terms of its impact on REITs with the FTSE S-REIT Index down a marginal -0.2% the day after the rate hike. Nonetheless, since the turn of the year, the S-REIT sector looks to be pricing in some of these headwinds from the macro front this year, with the FTSREI down -5.4% YTD vs the STI's +0.1%. We highlight some of the queries investors may have at this juncture in face of the impending further rate hikes.

1. The Fed just raised rates for the first time in 2018, and signaled for another two for 2018. What are the implications on the S-REIT sector?

- The rate hike was widely expected as per the Fed's earlier guidance. In fact, following the hike, market expectations of four rate hikes or more this year actually fell. This is probably due to Fed Chairman Powell's comments re-affirming gradual rate hikes and that the present Trump administration's trade policies could pose a concern for businesses.
- Interesting to note is that despite raising projections for economic growth to 2.7% from 2.5% and lowering unemployment forecast, headline inflation expectations remain unchanged at 1.9% and 2% for 2018 and 2019 respectively.
- Based on the Fed's latest assessment and if this pans out, it should continue to be an accommodative environment for S-REITs with strengthening economic growth and tepid inflation which allows the Fed to maintain a gradual pace of rate hikes.

Figure 1: Expectations of a fourth rate hike fell after the announcement of the first rate hike in 2018, on 21 March this year



Source: Bloomberg, PSR

2. What is the impact on S-REITs' DPU from these rate hikes?

- On average, we note that c.80% of S-REITs across the various sectors have at least 70% of their debt hedged on fixed rates in anticipation of higher interest costs. This helps mitigate the impact of rising interest rates on 2018e DPU.
- For the REITs under our coverage, we estimate DPU will be negatively impacted 1-3% by a 100bps increase in financing costs from current, assuming current interest rate hedging status.
- Assuming a zero hedging scenario, DPU could be negatively impacted 8-12%.

Equal Weight

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
FTSE REIT Index	0.9	(2.9)	15.9
Straits Times Index	(3.0)	1.4	12.9

Ascendas REIT ACCUMULATE

BLOOMBERG CODE	AREIT SP
CLOSING PRICE	SGD 2.60
FORECAST DIV	SGD 0.16
TARGET PRICE	SGD 2.89
TOTAL RETURN	17.3%

Cache Logistics Trust ACCUMULATE

BLOOMBERG CODE	CACHE SP
CLOSING PRICE	SGD 0.83
FORECAST DIV	SGD 0.06
TARGET PRICE	SGD 0.93
TOTAL RETURN	20.1%

Dasin Retail Trust BUY

BLOOMBERG CODE	DASIN SP
CLOSING PRICE	SGD 0.87
FORECAST DIV	SGD 0.10
TARGET PRICE	SGD 0.98
TOTAL RETURN	23.9%

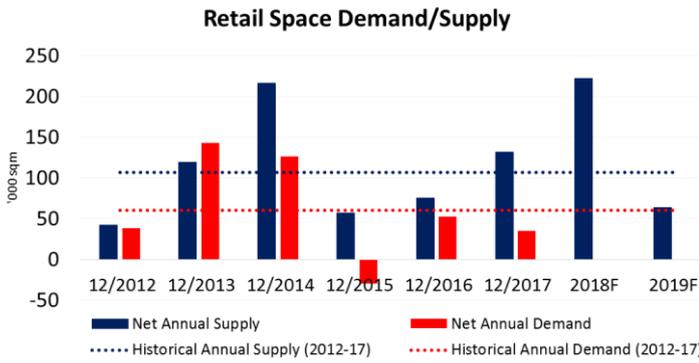
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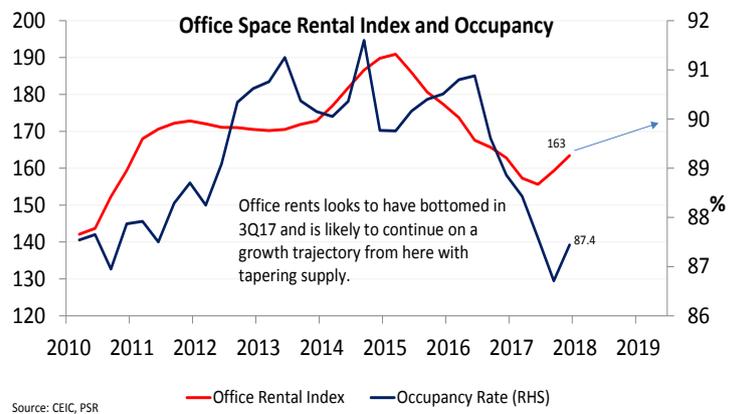
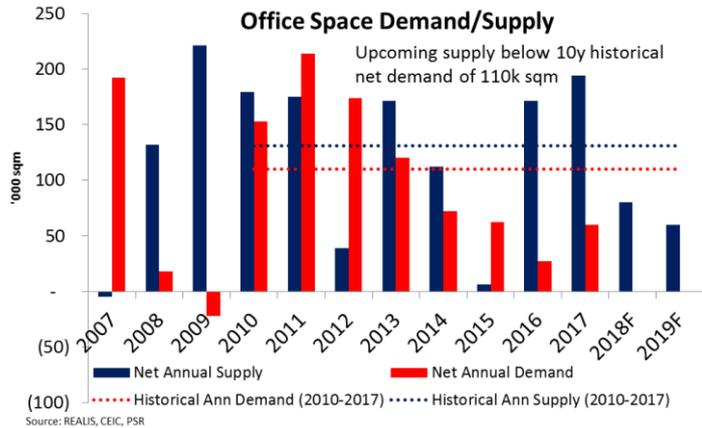
3. What is the outlook for each S-REIT sector?

- Apart from retail, all other sectors - office, industrial and hotels - generally face a positive scenario of tapering supply after a peak in supply in 2017.
- The easing of supply in 2018 should build a base for rentals to start climbing up. This should mitigate the magnitude of negative rental reversions we are expecting for the retail, industrial, and office sectors.

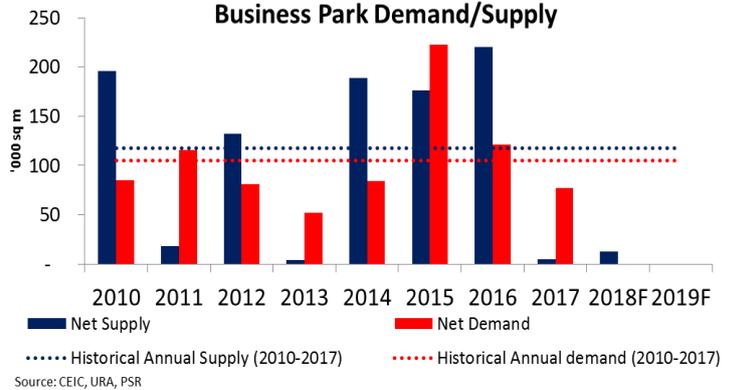
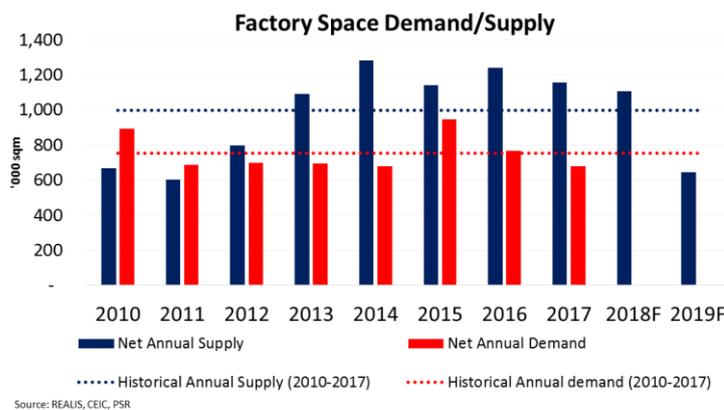
Figures 2 and 3: Retail is facing increased supply amidst falling demand and intense competition from e-commerce players. We expect rents to bottom in 2H2018.

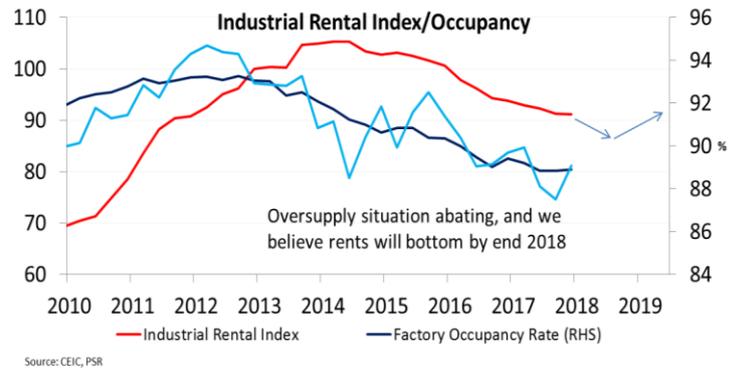
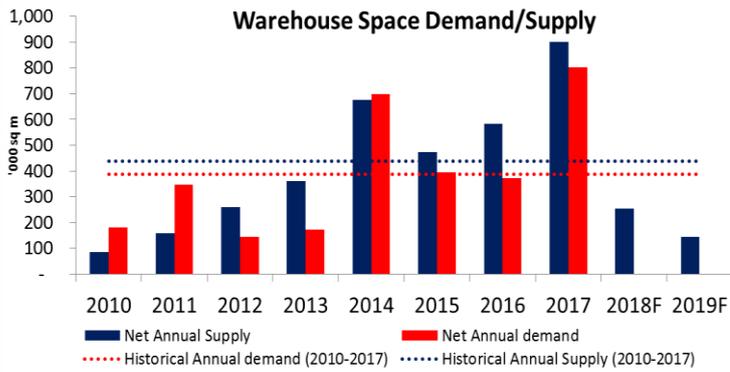


Figures 4 and 5: Upcoming Office Supply tapering off after 2017 and Office Rents bottoming, and expected to stabilise from 4Q2017.



Figures 6 and 7: Industrial Supply across all sub-sectors (except factory space) tapering off after 2017. We expect industrial rents to bottom by end-2018

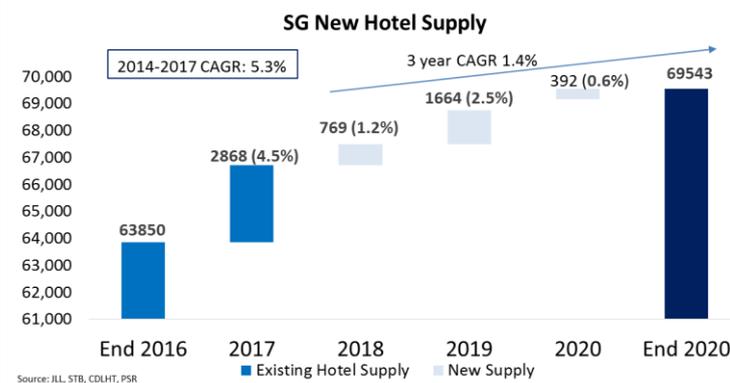




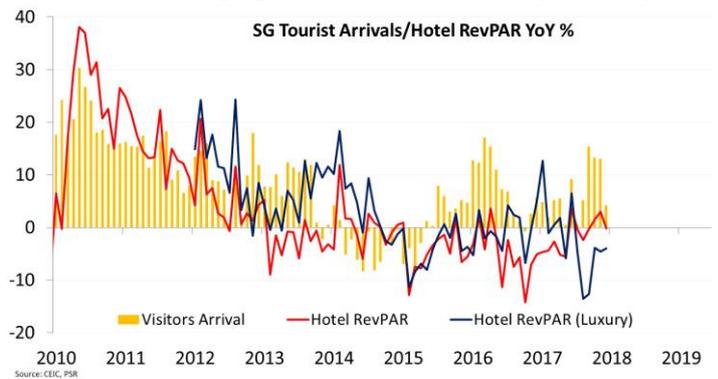
Source: REALIS, CEIC, PSR

Source: CEIC, PSR

Figures 8/9: SG hotel supply tapering off after 4.5% increase in 2017. RevPARs showing signs of stabilisation in the past half year.



Source: JLL, STB, CDLHT, PSR



Source: CEIC, PSR

4. Apart from interest rate hikes, how will some of the other regulatory changes announced during Singapore’s Budget 2018 affect S-REITs?

- Singapore-listed REIT exchange traded funds (ETFs) will no longer be subjected to the 17% corporate tax on the specified income distributed to the unitholders.
- Expected to be enacted on or before 1 July 2018, this change will even the parity of tax treatments between individual S-REIT counters and S-REIT ETFs.
- Demand will inevitably flow down to the three Singapore-listed ETFs and correspondingly, the S-REIT portion of the entire Singapore-listed REIT ETF pie. Total market capitalisation of all three REIT ETFs currently stands at S\$264.71 million, in comparison to the S\$80.9 billion market capitalisation of the entire S-REIT market.

The three Singapore listed ETFs are:

1. Lion-Phillip S-REIT ETF
2. Nikko AM Asia Ex Japan REIT ETF
3. Phillip SGX APAC Dividend Leaders REIT ETF

5. Where do S-REITs stand now compared to historical valuations and the valuations of regional REITs?

- At 5.3%, S-REITs offer one of the highest absolute yields amongst major REIT markets of the US, HK, Japan and Australia. (Figure 12)
- However, current yield spread of c.2.9% is at a -1s.d. level from post-GFC average. We note that post-GFC, there were only 2 periods of time when the yield spreads compressed below current levels: in 2010 (for a 2-month period) and 2013 (for an 8-month period). (Figure 11)

6. What are key risks going into S-REITs now?

- Macroeconomic factors - in particular, the US interest rate hikes - continue to be the paramount risks to look out for for S-REITs going forward. Fed’s balance sheet tapering could also cause upward pressures on yields.
- While three interest rate hikes are expected in 2018, word on the street – or rather, nuanced through Powell’s debut FOMC speech on 21 March 2018, indicate a likelihood of a fourth interest rate hike.
- However this does not necessarily spell doom and gloom if the rate hikes are in response to improving economic conditions.
- Rising interest rates is a headwind, but it does not necessarily mean lower prices.

Figure 10: S-REIT Comparison Table and PSR Coverage

	Mkt. Cap. (\$\$mn)	Price (\$\$)	PSR RATING	PSR TARGET PRICE (\$\$)	P/NAV	Trailing yield (%)	Total Returns YTD (%)	Gearing (%)	Approximate % of debt on fixed rate	ROE (%)	Average borrowing cost (%)	% debt expiring in 2018/current FY	% debt expiring in 2019/next FY	Year End
Healthcare														
PARKWAYLIFE REAL ESTATE	1,706	2.82			1.60	4.7	-4.6	36.4	99.0	9.6	1.0	3.0	20.0	December
FIRST REAL ESTATE INVST TRUST	1,081	1.38	NEUTRAL	1.32	1.36	6.2	0.1	33.6	70.0	8.9	4.1	41.6	49.0	December
<i>Average</i>					1.48	5.47	-2.28	35.00			2.55	22.30		
Hospitality														
ASCOTT RESIDENCE TRUST	2,481	1.15			0.92	7.2	-2.9	36.2	81.0	6.2	2.4	13.0	5.0	December
CDL HOSPITALITY TRUSTS	2,027	1.69			1.10	5.5	2.9	32.6	59.1	7.6	2.1	0.0	51.3	December
FAR EAST HOSPITALITY TRUST	1,337	0.72			0.83	5.4	1.4	34.4	41.6	0.9	2.5	14.6	12.5	December
OUE HOSPITALITY TRUST	1,544	0.85			1.12	6.0	2.0	38.8	71.0	5.5	2.5	0.0	0.0	December
FRASERS HOSPITALITY TRUST	1,461	0.785			1.00	6.4	0.0	33.0	88.5	11.3	2.8	15.0	55.4	September
ASCENDAS HOSPITALITY TRUST	977	0.865			1.01	6.6	0.0	33.2	77.2	0.8	2.7	31.6	0.0	March
<i>Average</i>					1.00	6.20	0.57	34.70			2.50	12.37		
Retail														
CAPITALAND MALL TRUST	7,345	2.07	NETURAL	2.03	1.06	5.4	-2.0	34.2	97.0	9.7	3.2	15.9	11.7	December
MAPLETREE GREATER CHINA COMM	3,307	1.17			0.94	6.4	-5.7	39.3	75.0	11.1	2.7	0.0	3.0	March
SPH REIT	2,555	0.995			1.06	5.6	-4.0	25.4	85.3	6.6	2.8	37.6	14.7	September
FRASERS CENTREPOINT TRUST	2,037	2.2	NEUTRAL	2.14	1.09	5.5	-0.5	29.0	55.0	10.7	2.4	12.0	14.7	September
STARHILL GLOBAL REIT	1,592	0.73			0.79	6.5	-5.0	35.3	99.0	5.3	3.1	0.0	5.8	June
CAPITALAND RETAIL CHINA TRUST	1,552	1.6	NEUTRAL	1.66	1.00	6.3	-1.3	28.4	80.0	9.7	2.5	0.0	20.0	December
LIPPO MALLS INDONESIA RETAIL	1,104	0.39			1.21	8.8	-0.5	33.7	47.0	6.3	N.A.	38.8	0.0	December
BHG REIT	383	0.765			0.92	7.2	6.9	32.5	45.0	5.0	3.7	32.6	8.8	December
DASIN RETAIL TRUST	485	0.875	BUY ¹	0.98	0.57	8.2	4.2	31.5	NA	NA	4.8	NA	NA	December
<i>Average</i>					0.96	6.63	-0.89	32.14			3.15	17.11		
Commercial														
CAPITALAND COMMERCIAL TR	6,609	1.83	NEUTRAL	1.8	1.03	4.7	-3.1	33.9	80.0	9.9	2.7	4.0	36.0	December
SUNTEC REIT	5,136	1.93			0.91	5.2	-9.6	36.4	75.0	4.0	2.6	8.0	24.5	December
KEPPEL REIT	4,135	1.22			0.86	4.7	-1.3	38.7	77.0	3.6	2.6	0.0	22.0	December
MAPLETREE COMMERCIAL TR	4,608	1.6			1.16	5.1	-0.5	36.3	78.0	9.7	2.7	0.0	11.0	March
FRASERS COMMERCIAL TRUST	1,250	1.42			0.90	5.6	-2.6	34.8	81.0	8.4	3.0	24.2	21.1	September
OUE COMMERCIAL REIT	1,104	0.715			0.79	8.6	2.5	37.3	84.3	10.4	3.5	37.8	0.0	December
MANULIFE US REIT	958	0.925			1.12	6.0	5.1	33.7	100.0	8.3	2.8	0.0	23.5	December
KEPPEL-KBS US REIT	556	0.885			1.04	6.8	-2.2	36.0	NA	2.3	3.4	0.0	0.0	December
<i>Average</i>					0.97	5.69	-1.36	35.89			2.92	9.25		
Industrial														
ASCENDAS REAL ESTATE INV TR	7,710	2.67	ACCUMULATE	2.89	1.29	6.0	-1.1	35.2	70.5	7.2	2.9	23.8	13.5	March
MAPLETREE INDUSTRIAL TRUST	3,808	2.02	NEUTRAL	2.15	1.43	5.8	1.4	33.8	60.7	11.0	2.9	10.9	12.8	March
MAPLETREE LOGISTICS TRUST	3,700	1.21			1.16	6.2	-6.9	37.8	78.0	8.0	2.3	0.0	11.0	March
KEPPEL DC REIT	1,601	1.42	NEUTRAL	1.47	1.47	5.0	1.7	32.1	86.0	6.0	2.2	0.0	23.8	December
AIMS AMP CAPITAL INDUSTRIAL	950	1.39			1.03	5.5	2.8	33.8	88.7	0.1	3.6	0.0	38.7	March
CACHE LOGISTICS TRUST	888	0.83	ACCUMULATE	0.93	1.16	8.0	-0.5	36.3	76.8	3.3	3.6	28.1	40.2	December
SOILBUILD BUSINESS SPACE REIT	694	0.66			1.04	8.7	0.5	40.6	70.1	-4.0	3.2	30.9	8.3	December
SABANA SHARIAH COMP IND REIT	442	0.42			0.77	7.9	8.5	38.2	76.2	-4.8	3.9	32.0	35.4	December
VIVA INDUSTRIAL TRUST	854	0.88			1.15	8.3	-4.0	39.8	84.4	5.2	3.9	19.0	0.0	December
ESR REIT	720	0.545			0.93	7.0	-0.1	39.6	69.2	0.1	3.6	23.1	15.9	December
EC WORLD REIT	585	0.745			0.81	8.1	-0.7	29.2	100.0	6.6	5.4	N.A.	N.A.	December
FRASERS LOGISTICS & INDUSTRIAL	1,657	1.09			1.22	6.4	-5.2	30.9	68.0	7.8	2.8	0.0	27.6	September
<i>Average</i>					1.12	6.90	-0.30	35.61			3.35	15.26		

Source: Bloomberg (Updated 22 March 2018). Debt data from latest Company Results as of 31 Dec 2017, PSR Covered by PSR on the SGX Stockfacts Scheme

Figure 11: S-REITs yield spreads are at -1s.d. levels, reflecting valuations on the more expensive side...

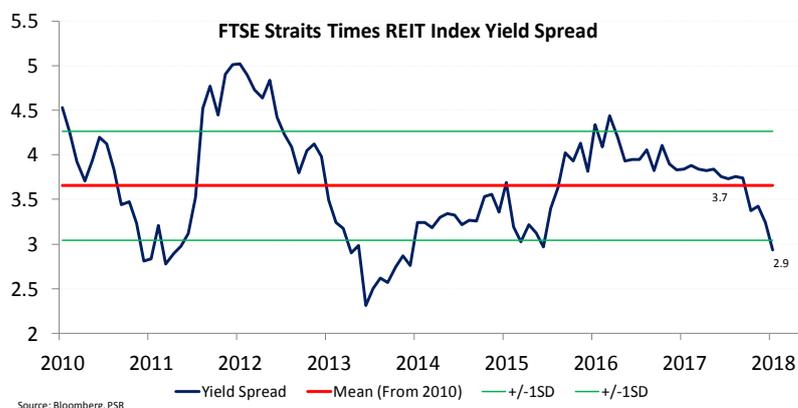
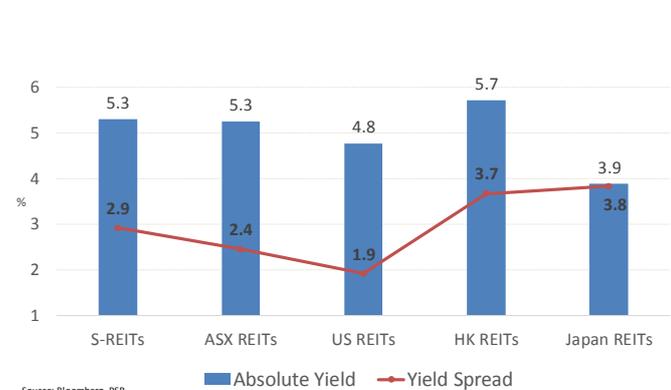


Figure 12: ...Though in absolute yield terms, S-REITs still offer one of the highest amongst major REIT markets.



Appendix

Figure 13: Notable upcoming shopping mall openings

Notable upcoming retail space launches

Project	Location	Estimated NLA (sq ft)	Completion
Paya Lebar Quarter	Paya Lebar	340,000	2018
Northpoint City	Yishun	330,000	2018
TripleOne Somerset Podium	Somerset	70,000	2018
Raffles Hotel A/A	City Hall	219,000	2018
Wisteria Mall	Yishun	58,000	2018
Jewel Changi Airport	Changi Airport	576,000	2019
Funan	North Bridge Road	324,000	2019
City Gate	Beach Road	76,000	2019

Source: URA, JLL, CBRE, PSR

Figure 14: Notable upcoming office openings

Notable Office launches 2018-2021

Office Project	NLA (sq ft)	Location	Expected launch
18 Robinson	145,000	Robinson Road	2018
Frasers Tower	663,000	Shenton Way	2018
Redevelopment of Funan Digitalife Mall	204,000	City Hall	2019
Park Mall Redevelopment	352,000	Orchard Road	2019
79 Robinson Road	500,000	Robinson Road	2020
Hub Synergy Point Redevelopment	128,000	Anson Road	2020
Afra-Asia Building Redevelopment	154,000	Shenton Way	2020
Redevelopment of Golden Shoe Car Park	635,000	Raffles Place	2021

Source: JLL, CBRE, PSR

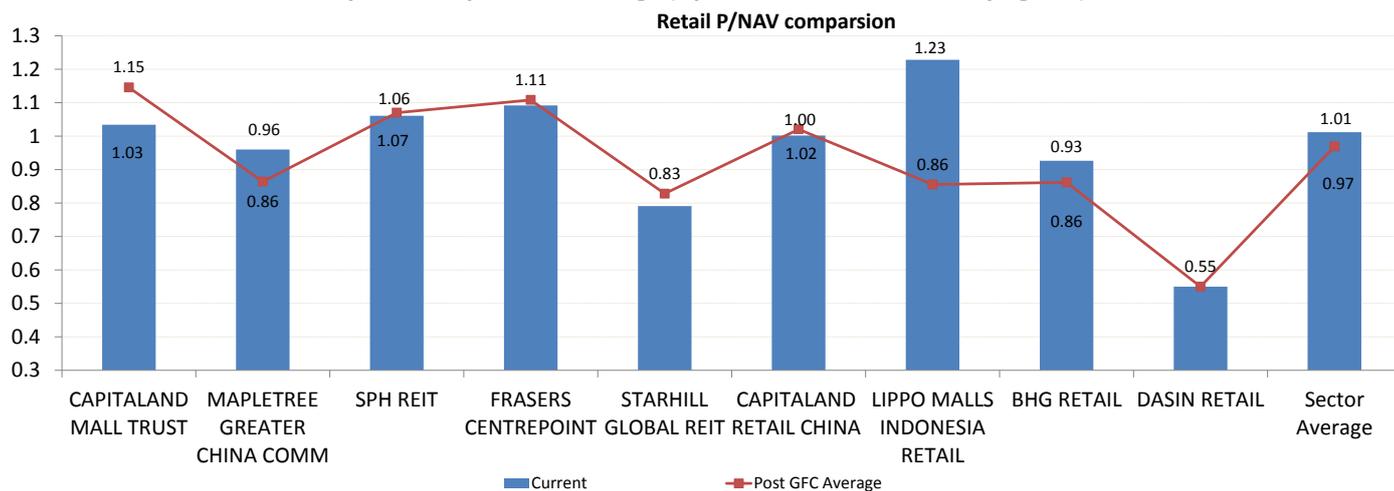
Figure 15: Notable upcoming hotel openings from 2017-19

Notable Hotel openings 2018-2020

Hotel Name	No of Rooms	Target Segment	Location	Expected launch
Swissotel The Stamford	97	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	111	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
Swissotel The Stamford	329	Upscale/Luxury	City Centre	2019
Capri 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
The Outpost@Sentosa	193	Upscale/Luxury	Sentosa	2019
Artillery Avenue Palawan@Sentosa	40	Upscale/Luxury	Sentosa	2019
The Clan	292	Mid-tier	City Centre	2020
Aqueen Hotel Geylang	100	Economy	Outside City Centre	2020

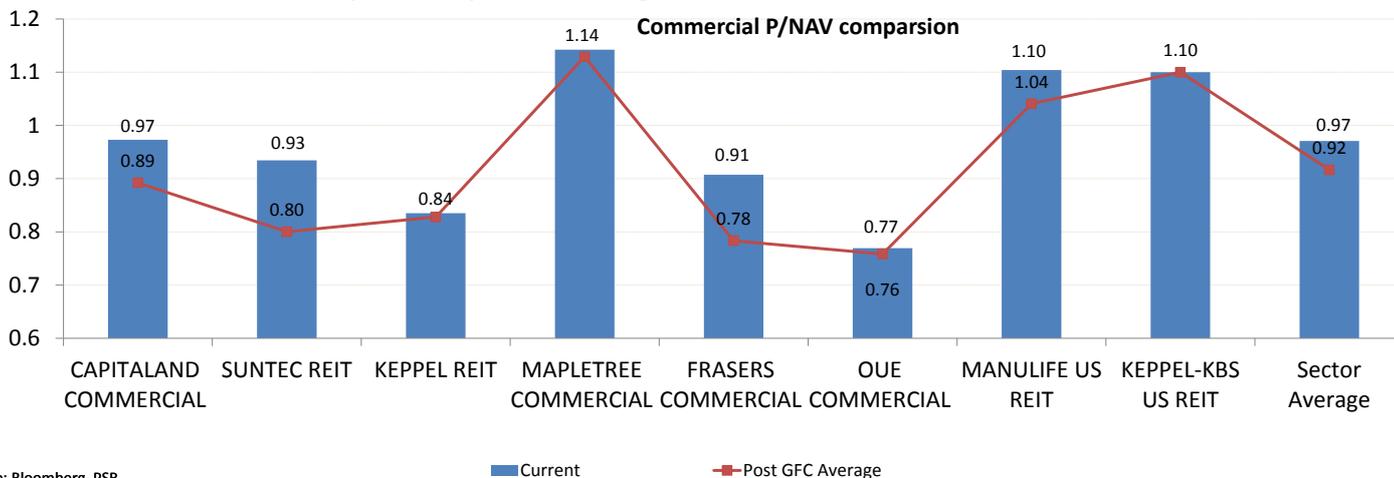
Source: CDLHT, JLL, PSR

Figure 16: Retail S-REITs P/NAV comparison vs post-GFC average (Updated with latest monthly figures)



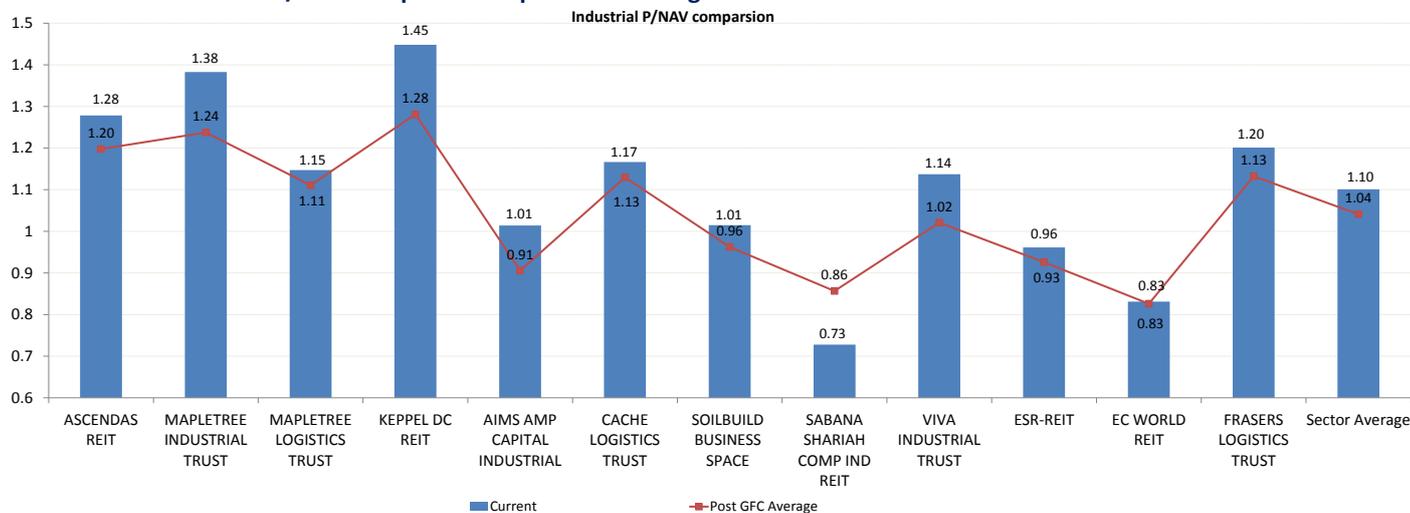
Source: Bloomberg, PSR

Figure 17: Office S-REITs P/NAV comparison vs post-GFC average



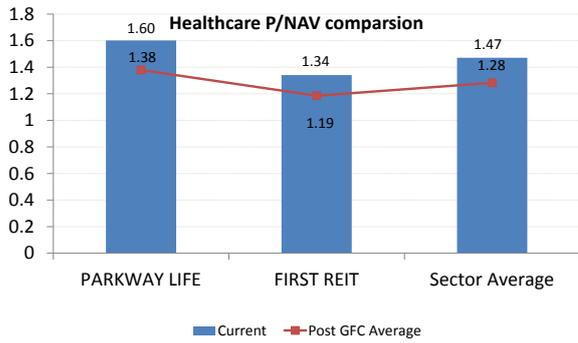
Source: Bloomberg, PSR

Figure 18: Industrial S-REITs P/NAV comparison vs post-GFC average

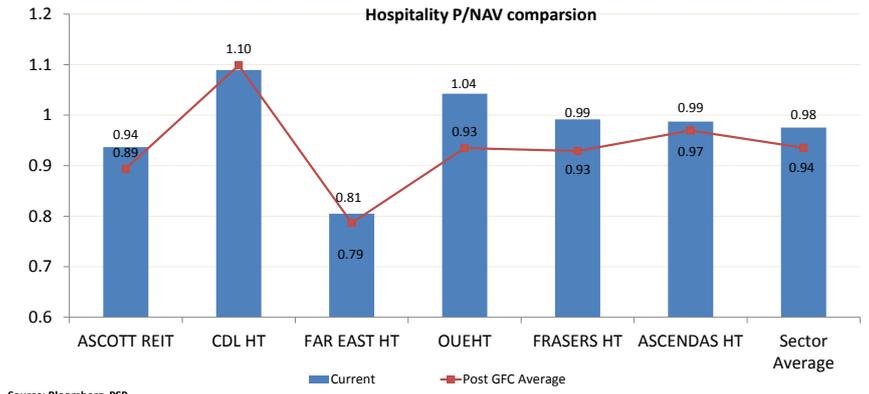


Source: Bloomberg, PSR

Figures 19 and 20: Healthcare and Hospitality S-REITs comparison



Source: Bloomberg, PSR



Source: Bloomberg, PSR

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