

OUE REIT

DPU supported by resilient rental reversion


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Singapore | REIT | 3Q24 Update

25 October 2024

- Gross revenue for 3Q24 slipped by 1.2% YoY to S\$74.8mn, in line with our forecast. 9M24 revenue forms 74% of our FY24e estimates. NPI was down by 3.7% YoY to S\$60.3mn and was within our estimates, forming 73% of our FY24e forecast. The decline was mainly due to both hotels' upward revision of property tax.
- While the DPU was not disclosed. Hospitality generated a lower contribution due to reduced variable rent, as the ADR is normalizing from last year's peak. OUE REIT will resume paying 50% of base management fees in cash, with the remaining in units which we expect to partially offset the weaker contribution from hospitality segment in FY24e.
- FY24e earnings are expected to be supported by high single-digit rental reversion in both the retail and office segments. However, we anticipate high interest rate to persist into 1H25, as OUE REIT increased its fixed-rate debt by 9.5ppt to 70.5% in 3Q24. We have revised down our FY24e-25e DPU forecast by 2%/15%, respectively, after factoring in a lower NPI margin, weaker hospitality contribution, and persistently high interest expenses. We reiterate our BUY recommendation with an unchanged DDM-based TP of S\$0.40 and FY24e-25e DPU of 1.81 to 2.25 cents. A 25bp interest rate decrease could potentially lead to a 0.03 cent (or 1.5%) improvement in DPU.

BUY (Maintained)

LAST CLOSE PRICE	SGD 0.30
FORECAST DIV	SGD 0.02
TARGET PRICE	SGD 0.40
TOTAL RETURN	41.0%

COMPANY DATA

BLOOMBERG CODE:	OUEREIT SP Equity
O/S SHARES (MN):	5,493
MARKET CAP (USD mn / SGD mn):	1248 / 1648
52 - WK HI/LO (SGD):	0.35 / 0.22
3M Average Daily T/O (mn):	3.83

MAJOR SHAREHOLDERS

OUE Reality Pte Ltd	22.3%
Tang Gordon	9.1%

PRICE PERFORMANCE (%)

	1MTH	3MTH	YTD
COMPANY	(6.3)	5.2	13.1
STTF RETURN	(1.0)	6.2	15.9

Result at a glance

(\$ mn)	3Q24	3Q23	YoY	Comments
Gross Revenue	74.80	75.80	-1.3%	Lower contribution from the hospitality segment compared to the same period last year
Net Property Income	60.30	62.70	-3.8%	Upward revision of prior years' property tax for Hilton Singapore Orchard and Crowne Plaza Changi Airport
Revenue from Hospitality	27.80	28.30	-1.8%	Lower variable rents
Cost of debt	4.80%	4.20%	0.6ppt	
Gearing	39.30%	39.40%	(0.1ppt)	
NAV per share	0.59	0.58	1.7%	

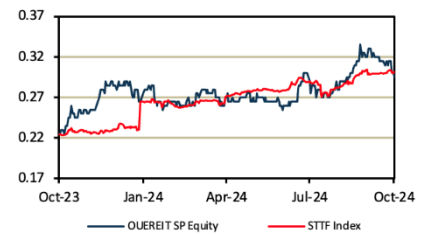
Source: Company, PSR

The Positives

+ Resilient Singapore rental reversion. Rental reversion in Singapore is holding up well, with 16% for the Mandarin Gallery and 10.8% for the Singapore office segment in 3Q24. Occupancy in the CBD area dropped marginally by 1.7ppt to 92.2% amid the completion of IOI Central Boulevard Towers. We expect pressure on the vacancy rate to alleviate in 2025 in the face of the construction delay of Shaw Tower. With the postponement of the 614k sqft upcoming supply, which is more than 2 times the IOI phase 2 entered into the market this year, we expect rental reversion to maintain at the mid-single digits in FY25e.

+ Cost of borrowing on the downward trajectory. OUE REIT launched a 7-year investment-grade green note at a historically low rate of 3.9%, achieving 3.2 times oversubscription. The REIT is taking a more conservative view on interest rate cut expectations compared to the general market and has increased its hedging by 9.5 ppt to 70.5%. We believe the cost of borrowing is already at its peak, and interest rate headwinds will significantly unwind in 2025. However, since most of the borrowing has been hedged for at least 1 year, the all-in cost of borrowing could still be much higher than the pre-rate-hike period (3Q21: 3.2%) in FY25, which may negatively impact the DPU.

PRICE VS. STTF



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY22	FY23	FY24e	FY25e
Gross Rev (\$mn)	241.5	285.1	299.3	308.8
Dist. Inc. (\$mn)	116.2	115.3	99.6	123.5
P/NAV (x)	0.51	0.50	0.50	0.50
DPU (cents)	2.12	2.09	1.81	2.25
Dist. Yield (%)	7.07	6.97	6.04	7.49

Source: Company, PSR

VALUATION METHOD

DDM (Cost of Equity: 8.0%; Terminal g: 1%)

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The Negative

- **RevPAR tapering off.** Although RevPAR increased by 0.3% YoY to S\$269 in 3Q24, revenue from the hotel segment declined by 1.8% YoY due to lower variable rent from the master lease. The Singapore market has experienced a softening in ADR from its peak in 2023 as a trade-off to maintain occupancy rates, driven by the normalization of tourist spending on accommodation. RevPAR for Hilton Orchard declined by 8.6% YoY in 3Q24, while Crowne Plaza delivered a strong performance with a 30.3% YoY increase since corporate demands such as aircrew remain robust. Margin deteriorates on the back of lower ADR and higher operating expenses such as manpower and utility costs, and we expect the gross operating margin to stay at the current level in 2025, thus translating into lower master lease income.

Outlook

The retention rate for office space remains strong for OUE REIT, given its connectivity and the cost-consciousness of corporates when considering relocation. Sixty percent of the IOI building has been pre-committed, with an additional 10-20% under negotiation. With this healthy pre-commitment rate and lower-than-market rental rates (CBD Grade A office market rent in 3Q24: S\$11.95 psf pm vs. OUE REIT's average passing rent: S\$10.61 psf pm), we expect rental reversion in FY24e to be in the high single digits, with FY25e maintaining at the mid-single digits.

OUE REIT has observed more constrained spending patterns in Mandarin Gallery, as shoppers shy away from luxury products and instead turn towards health and wellness offerings. Occupancy costs have risen, with Mandarin Gallery seeing a 1-2% uplift. As tenant sales continue to trend at 85% of pre-COVID levels and inflationary pressures exacerbate margin constraints, we foresee rental reversion moderating from its current high in FY25e to the high single digits.

We expect transaction volume to increase amid improved investor sentiment following the Fed's rate cut in Sept24. OUE REIT is eyeing acquisitions when the macroenvironment and capital market conditions become more favorable. The REIT is shifting away from the hotspot in Japan and redirecting its focus to Australia, with the hospitality segment remaining its key area of interest.

Maintain BUY with an unchanged TP of S\$0.40

OUE REIT is currently trading at an FY24e dividend yield of 6.0%, with an attractive valuation of 0.5x P/NAV. A well-absorbed office supply, F&B expansion demand and restoration of 50% base management fee in units will support FY24e DPU. We have lowered our FY24e-25e DPU forecasts by 2%/15%, respectively, due to weaker contributions from the hospitality segment and persistently high interest expenses. Despite this, we maintain our BUY recommendation with an unchanged DDM-backed TP of S\$0.40 and FY24e-25e DPU of 1.81 to 2.25 cents.

Financials

Income Statement

Y/E Dec, (S\$'000)	FY21	FY22	FY23	FY24e	FY25e
Revenue	249,884	241,507	285,055	299,293	308,813
Property Expense	45,679	44,592	50,088	63,151	65,160
Net Property Income	204,205	196,915	234,967	236,142	243,653
Net financing cost	(71,793)	(54,966)	(111,843)	(113,709)	(92,255)
Total return before tax	69,968	298,874	208,258	116,427	146,715
Tax Expense	(14,061)	(11,191)	(12,502)	(8,150)	(10,270)
Net income after Tax	55,907	287,683	195,756	108,277	136,445
Amount to be distributed	131,632	111,626	115,307	99,646	123,486
Distribution to unitholders	142,032	116,226	115,307	99,646	123,486

Per unit data

Y/E Dec, (S\$)	FY21	FY22	FY23	FY24e	FY25e
NAV (S\$)	0.57	0.59	0.60	0.61	0.60
DPU (S cents)	2.60	2.12	2.09	1.81	2.25

Cash Flow

Y/E Dec, (S\$'000)	FY21	FY22	FY23	FY24e	FY25e
CFO					
Total return before tax	55,907	287,683	205,779	108,277	136,445
Adjustments	142,231	(93,599)	16,003	100,643	75,087
WC changes	(3,086)	941	(1,139)	(5,070)	(865)
Tax paid and interest received	(15,749)	(11,615)	(11,253)	(8,150)	(10,270)
Cash generated from ops	166,801	183,534	213,387	196,801	201,757
CFI					
CAPEX	(56,896)	(47,639)	(10,568)	-	-
Cashflow from investments	902,523	(30,848)	1,458	31,688	32,191
CFF					
Proceeds from borrowing	764,973	-	-	-	-
Proceeds from issue of Notes	150,000	150,000	-	-	-
Interest Paid	(66,487)	(65,289)	(85,912)	(128,728)	(107,273)
Cashflow from financing	(1,100,651)	(159,120)	(209,647)	(236,574)	(238,958)
Net change in cash	(31,327)	(6,434)	5,198	(8,084)	(5,011)
Cash at the start of the period	88,508	59,549	49,482	53,522	45,438
Ending cash	59,549	49,482	53,522	45,438	40,427

Source: Company, Phillip Securities Research (Singapore) Estimates

Balance Sheet

Y/E Dec, (S\$'000)	FY21	FY22	FY23	FY24e	FY25e
ASSETS					
Cash and short term deposit	59,549	49,482	54,225	45,438	40,427
Trade and other receivables	27,028	20,592	22,138	27,208	28,074
Total current assets	86,577	76,464	79,637	75,921	71,775
Investment properties	5,409,748	5,539,164	5,630,357	5,630,357	5,630,357
Trade and other receivables	3,867	4,334	4,805	4,988	5,147
Total non-current assets	5,745,944	5,912,641	5,989,074	5,989,244	5,989,398
Total Assets	5,832,521	5,989,105	6,068,711	6,065,165	6,061,173
LIABILITIES					
Trade and other payables	87,132	76,271	-	-	-
Loans and borrowings	172,199	327,618	90,340	90,340	90,340
Current tax liabilities	14,594	14,741	16,151	16,151	16,151
Total current liabilities	2,244,006	2,281,738	2,290,681	2,268,966	2,270,326
Borrowings	1,813,196	1,721,841	2,055,119	2,055,119	2,055,119
Trade and other payables	38,860	39,878	41,655	42,756	44,116
Total non-current liabilities	1,967,536	1,862,974	2,184,090	2,162,475	2,163,835
Total Liabilities	2,244,006	2,281,738	2,290,681	2,268,966	2,270,326
Net assets	3,588,515	3,707,367	3,778,030	3,796,199	3,790,847

Valuation Ratios

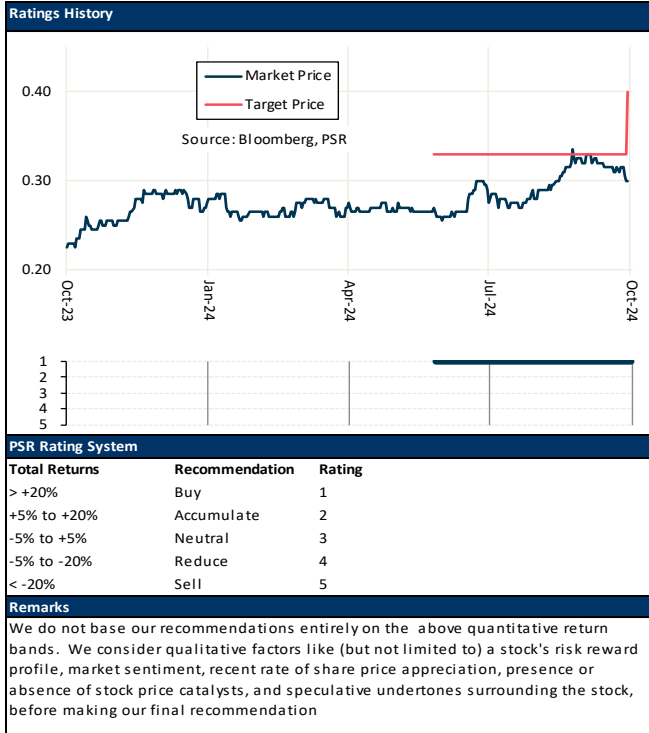
Y/E Dec, (S\$)	FY21	FY22	FY23	FY24e	FY25e
P/NAV (x)	0.52	0.51	0.50	0.50	0.50
Distribution Yield (%)	8.67	7.07	6.97	6.04	7.49

Growth & Margins (%)

	FY21	FY22	FY23	FY24e	FY25e
Growth					
Revenue	-	-3.4%	18.0%	5.0%	3.2%
Distributable income	-	-15.2%	3.3%	-13.6%	23.9%
DPU	-	-18.5%	-1.4%	-13.3%	23.9%

Key Ratios

	FY21	FY22	FY23	FY24e	FY25e
ROE	1.5%	7.7%	5.2%	2.9%	7.2%
Gearing	34.0%	34.2%	35.4%	35.4%	35.4%



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