

24 April 2019

Property| REITs

Frasers Commercial Trust (FCOT SP)

Neutral (Maintained)

Slow Leasing Progress At ATP

Target Price (Return)	SGD1.50(+1%)
Price:	SGD1.49
Market Cap:	USD989m
Avg Daily Turnover (SGD/USD)	2.3m/1.7m

- Maintain NEUTRAL, with unchanged TP of SGD1.50, 1% upside.** 2QFY19 (Sep) DPU met expectations. We remain NEUTRAL pending more visibility on ATP leases (where occupancy has been sub-optimal) and redeployment of divestment proceeds. DPU in the meantime is expected to maintain stable, aided by higher capital distribution and payment of management fees in units. Key catalyst would be strong occupancy improvement at ATP, and accretive acquisitions. Key risks are a slowdown in office leasing momentum and forex fluctuations.
 - Flattish DPU in line.** Revenue and NPI were lower 11% and 15%YoY, impacted mainly by lower occupancy at Alexandra Technopark (ATP), divestment of 55 Market Street (55MS), and the weaker AUD. Impact to DPU was however mitigated by higher JV contribution, increased capital distribution of SGD4.9m (2QFY18: SGD2.9m), and 100% of management fee paid in units. We expect higher capital distributions to offset the loss of income from divestments and lower portfolio occupancies for the next few quarters. Management guided that it still has about SGD159m of divestment gains from the disposal of hotel development rights and the sale of 55MS.
 - Slow leasing progress at ATP.** Occupancy at ATP has bottomed at 59.2%, with the exit of anchor tenants, Hewlett-Packard Enterprise Singapore Pte Ltd and Hewlett-Packard Singapore. Take-up rate for the office space has been fairly slow in our view despite the reasonably healthy demand for Grade-B office space. Management said that this is partly due to the fact that it has been holding up asking rents at around SGD4psf. [The Business Times](#) had earlier indicated that Google has been in talks to take up about 400,000 sqf of space at average rentals of SGD4psf. Management noted that it has been in discussions with a few large and smaller tenants for the vacant space, but nothing has been firmed up yet.
- We also note that there would be a likely fit-out period of 3-6 months after the signing of the lease during which there would be no income contribution resulting in lower near-term income from the asset. As ATP is the largest income contributing asset in its portfolio, any strong occupancy improvement should be a key rerating catalyst in our view.
- Looking for acquisitions in UK and Australia.** Frasers Commercial Trust's gearing of 29.1% is one among the lowest among S-REITs, presenting a good debt headroom of c.SGD350m (assuming 40% levels) for acquisitions. We believe it may potentially look at acquiring the remaining 50% stake in the Farnborough Business Park (FBP), and look at other sponsor assets in UK once the Brexit uncertainty is cleared, due to its attractive yields and long WALE. When queried on the possible acquisition of Frasers Tower (sponsor asset), management guided that it is currently not looking at the asset and believes that current yields are not attractive enough to do an accretive acquisition.
 - AEI plans for Central Park.** Central Park will undergo a SGD23m (FCOT's 50% share: SGD 11.5m) asset enhancement initiative (AEI) to upgrade lobby and forecourt areas. The is mainly to enhance the buildings competitiveness (no GFA improvements) and will be carried out in a way that there is minimal disruption to occupancy. Works are expected to commence in 2Q19 and expected to be completed by 3Q20.
 - CSC retail podium ~50% pre-committed.** China Square Central's (CSC), SGD38m AEI works are on track to be completed by 2H19, which should see 17% uplift to malls' NLA. Pre-commitments currently stand at c.50% (40% as of last quarter), with average rents expected to be in high single digits. The 304-room Capri by Fraser, CSC is also expected commence operations in 2Q19 and bring more vibrancy to the area and benefit retail tenants.

Forecasts and Valuation	Sep-17	Sep-18	Sep-19F	Sep-20F	Sep-21F
Total turnover (SGDm)	156.6	133.3	143.5	155.0	157.4
Net property income (SGDm)	113.8	89.3	105.0	113.5	115.2
Reported net profit (SGDm)	111.4	141.7	112.4	101.1	102.8
Distributable income (SGDm)	78.6	82.7	86.7	89.8	91.5
DPS (SGD - cents)	9.8	9.6	9.7	9.9	9.9
DPS growth (%)	(2.2)	0.9	2.2	0.4	0.3
P/BV (x)	1.0	0.9	1.0	1.0	1.0
Dividend Yield (%)	6.6	6.4	6.5	6.6	6.7
Return on average equity (%)	8.6	10.3	8.0	7.1	7.1
Return on average assets (%)	5.2	7.8	5.5	4.8	4.9
Interest coverage (x)	5.6	6.7	6.3	5.8	5.8

Source: Company data, RHB

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Results At a Glance

Figure 1: 2QFY19 results summary

FYE Sep (SGDm)	2QFY19	2QFY18	YoY (%)	1QFY19	QoQ (%)	Comments
Gross Revenue	30.4	33.0	-7.9%	31.5	-3.6%	Lower occupancy at ATP weaker AUD and divestment of 55 Market Street Car Park
NPI	20.1	22.4	-10.5%	21.1	-4.9%	Higher property tax and amortisation of lease incentives
NPI Margin (%)	66.1%	67.9%	-1.8ppt	67.0%	-0.9ppt	
Net Income	13.6	11.3	20.2%	14.1	-3.1%	
Unitholders distribution	21.7	20.6	5.2%	21.6	0.6%	Higher capital distribution, 100% management fees in units and contribution from FBP
DPU (cents)	2.40	2.40	0.0%	2.40	0.0%	

Source: Company data, RHB

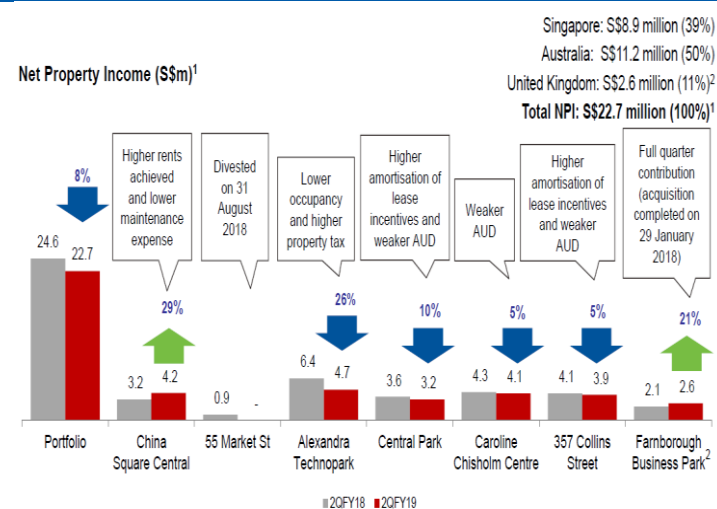
Figure 2: FCOT – fair value based on DDM

	FY19F	FY20F	FY21F	FY22F	Terminal value
DPU (SGD cents)	9.68	9.89	9.93	9.96	148.49
Fair Value (SGD)	1.50				
Current price	1.49				
Price upside (%)	0.9%				
Distribution yield (%)	6.5%				

Assumptions	
Risk-free rate (%)	3.0%
Beta	0.9
Cost of equity (%)	8.0%
Terminal growth (%)	1.25%

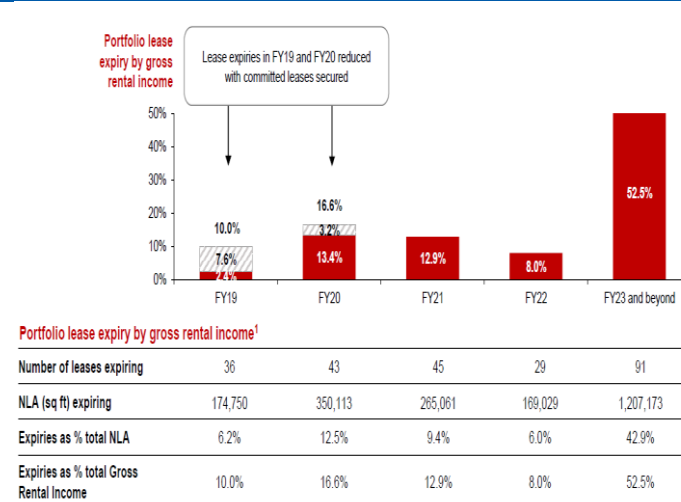
Source: RHB

Figure 3: NPI breakdown by property



Source: Company data

Figure 4: Lease expiry profile



Source: Company data

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