

22 April 2019

Property | REITs

CapitaLand Commercial Trust (CCT SP)

Neutral (Maintained)

Risk-Reward Profile Finely Balanced

Target Price (Return)	SGD1.86 (-4%)
Price:	SGD1.93
Market Cap:	USD5,339m
Avg Daily Turnover (SGD/USD)	21.3m/15.7m

- **Maintain NEUTRAL, TP of SGD1.86 reflects 4% downside.** CapitaLand Commercial Trust's 1Q19 results are in line, at 24% of our full-year forecast. Key catalysts are the announcement of redevelopment plans for 21CQ, yield-accretive acquisition of the remaining stake in CapitaSpring and overseas assets. Despite its positive outlook, its valuation of 1.1x P/BV and FY19F yield of ~5% are not compelling enough, in our view. We recommend investors to buy the stock on dips.
- **Potential equity fund-raising on the cards if CCT pursues Duo Tower.** *Bloomberg* earlier reported that CCT is vying to acquire Duo office and retail tower, which could be valued at over SGD1.5bn. We believe that CCT may use a mix of 40% equity and 60% debt if it decides to pursue the acquisition, to keep net gearing optimal (~38%) post acquisition. This, however, will lead to major equity fund-raising of ~SGD600m (potentially from share placement and preferential offerings) – which may lead to a near-term overhang on its share price.
- **HSBC building redevelopment plans might gain favour from central business district rejuvenation theme.** With HSBC – currently the sole tenant of the property – vacating the premises on Apr 2020, CCT could potentially look at redeveloping the property and tapping into any additional benefits from the CBD rejuvenation theme in the draft master plan (2019). CCT has highlighted that the immediate focus will be on refurbishment and re-letting the premises. Management has, however, noted that it doesn't expect any significant increase to the current GFA, based on the draft master plan for 2019.
- **Office leasing momentum remains strong.** CCT signed leases for 225,000 sqf (4Q18:143,000 sqf), of which 18% were new leases. The tenant mix of new leases was well diversified across seven sectors. We believe that most of the lease renewals were higher than expiring rental rates (~5-10%). Based on CBRE preliminary data, Grade-A office rental rates rose 3.2% QoQ in 1Q19 to SGD11.15 psf, continuing on its 15% YoY increase in 2018. With limited Grade-A supply in the pipeline (~1.1m sqf), we expect the Grade-A property rental rates to rise 5-15% in 2019. CCT currently has about 11% of leases by rental income due for renewal in 2019, which should benefit from the current momentum.
- **Overall portfolio occupancy rate dipped 0.3ppt QoQ to 99.1%** due to the lower occupancy rate at Six Battery Road where it dropped to 97.6% from 100%. Considering the strong demand for prime office space, we believe CCT will be able to backfill the space in the coming quarters.
- **Slight reduction in debt costs.** Average cost of debt stood at 2.5% pa (4Q18:2.6%), with 92% of its debt on fixed rates. Weighted average debt to maturity currently stands at 3.6 years.
- **CapitaSpring – 24%-leased, additional leasing to commence soon.** Construction works are on track to be completed by 1H21. As of now, JP Morgan has signed up to be the anchor tenant for office space, taking up ~24% of the NLA. Management plans to open a show suite on the site and will commence leasing for the remaining space. Based on our calculations, the targeted yield on cost of 5% translates into office rental rates of SGD10-11 psf – which we believe is achievable, considering the strong momentum in office space.
- **DPU adjustments.** We trim FY19F-20F DPU by 1-2% factoring in revised income for Bugis Village and a slightly lower occupancy rate for Six Battery Road.

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (SGDm)	337.5	394.0	397.3	383.4	397.1
Net property income (SGDm)	265.5	473.3	324.6	310.3	318.5
Net profit (SGDm)	264.9	331.3	344.3	342.6	347.1
Distributable income (SGDm)	288.1	331.3	347.5	346.0	350.7
DPS (SGD - cents)	8.7	8.7	9.3	9.2	9.3
DPS growth (%)	(4.6)	0.5	6.4	(0.6)	1.2
P/BV (x)	1.1	1.0	1.0	1.0	1.0
Dividend Yield (%)	4.5	4.5	4.8	4.8	4.8
Return on average equity (%)	4.1	4.8	5.0	4.9	5.0
Return on average assets (%)	2.8	3.4	3.5	3.4	3.4
Interest coverage (x)	3.7	5.6	3.9	3.6	3.5

Source: Company data, RHB

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Results At a Glance

Figure 1: 1Q19 results summary

(SGDm)	1Q19	4Q18	QoQ (%)	1Q18	YoY (%)	Comments
Revenue	99.8	99.0	0.7%	96.4	3.5%	Higher occupancy rate and contribution from Galileo
NPI	79.8	79.3	0.7%	77.2	3.4%	In line with revenue growth
NPI (%)	80.0%	80.0%	-	80.1%	-0.1ppt	
JV contribution	22.1	26.0	-15.0%	23.0	-3.7%	Lower contribution from Raffles City and One George Street
Distributable income	82.7	83.1	-0.4%	76.6	8.0%	Includes SGD 3.4m of tax-exempt income
DPU (SGD cents)	2.2	2.2	-0.9%	2.1	3.8%	
Committed Occupancy (%)	99.1	99.4	-0.3ppt	97.3	1.8ppt	Lower occupancy at Six Battery Road

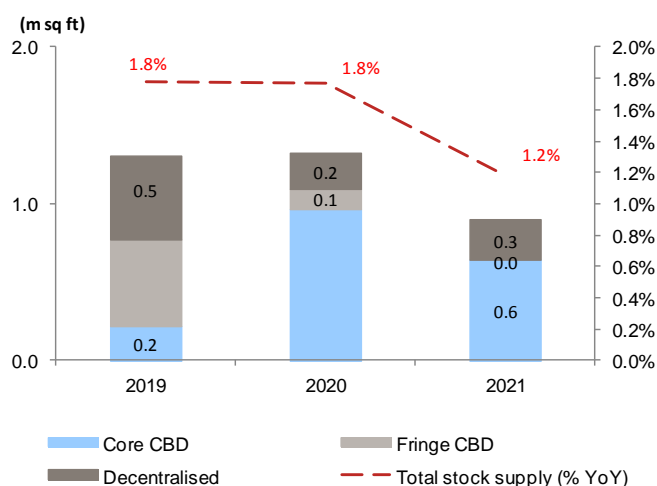
Source: Company data, RHB

Figure 2: CCT's DDM valuation

	FY19F	FY20F	FY21F	FY22F	Terminal Value
DPU (SG cts):	9.07	9.12	9.31	9.49	206.05
Fair Value:	1.86				
Current Price:	1.93				
Price Upside (%):	(3.6)				
Distribution Yield (%):	4.7				
<u>Assumptions:</u>					
Risk-free rate(%)	3.0				
Beta:	0.8				
Cost of Equity (%):	7.3				
Terminal Growth (%):	2.0				

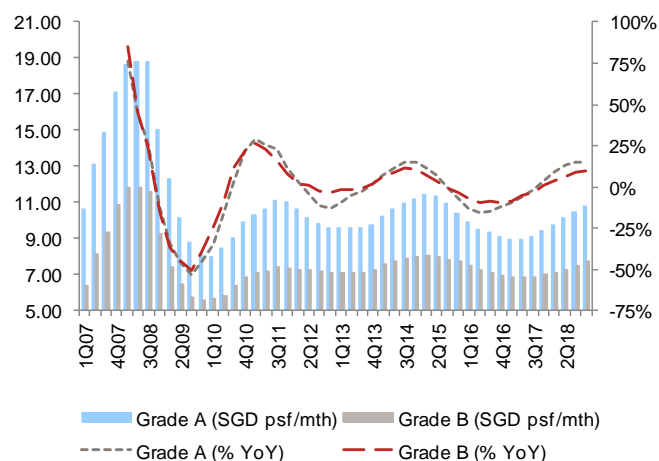
Source: Company data, RHB

Figure 3: Office supply pipeline



Source: CBRE

Figure 4: Singapore office rental rates



Source: CBRE, RHB

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