

3 January 2020

Property | REITs

Suntec REIT (SUN SP)

Buy (Maintained)

A Turnaround Year; Top Pick

Target Price (Return) SGD2.08 (+13%)
 Price: SGD1.84
 Market Cap: USD3,762m
 Avg Daily Turnover (SGD/USD) 8.0m/5.9m

- **Keep BUY and SGD2.08 TP, 13% upside plus 5% yield.** It is our commercial REIT Top Pick on attractive valuation and organic earnings growth. Key catalysts are healthy positive rent reversion from key asset, Suntec City, and earnings contributions from three development assets. Suntec REIT was a laggard in 2019 – we believe the market was focusing on headline DPU fall, instead of operational income growth. Valuation remains attractive as it trades at 0.86x P/BV (vs office REITs' 1x).

- **Expecting high single-digit rent reversions for Suntec City offices.** Suntec REIT's office portfolio rents have been on an uptrend, with six consecutive quarters of positive rental reversions, which should contribute positively to earnings. Looking ahead, c.14% of office leases by NLA are up for renewal in 2020. With expiring rent in the low SGD8 psf level vs passing rent of SGD9-10 psf, we expect strong double-digit rent growth from its office portfolio.

- **Exposure to co-working sector is minimal** at c.2% of the total. While co-working, which has been a key driver of office demand over the last few years, is expected to see a considerable slowdown, we believe demand from the technology, media, and telecommunication sectors will continue to hold up, keeping office portfolio occupancy at high 90% levels.

- **Three development assets to be completed by 1H20.** A key drag on Suntec REIT's earnings has been upfront development costs for assets currently under development without income contribution. The assets, which have yet to start contributions are 9 Penang Road (9PR), Olderfleet, and 21 Harris Street (21HS), and are slated for completion by 1H20.

In terms of pre-commitments, 9PR has been 100% pre-committed to UBS on a long lease, while Olderfleet has secured commitments for 87% of its space, with additional heads of agreement signed for 5%. 21HS, which was acquired recently, is currently 65% pre-committed and comes with a 3-year rent guarantee for the remaining spaces. Overall, these three assets are expected to contribute c.SGD30m in net income for 2020F, or c.8% of overall (including JV contributions).

- **Retail and conventions: rising above market challenges.** Despite the challenging retail climate, Suntec City has seen an improved operational performance – driven by higher tenant sales and increased footfall. We believe this is mainly being driven by management's active efforts. The mall has been registering positive rent reversions for nine consecutive quarters, and we expect this to continue in 2020 – with mid-single digit rental growth. Meanwhile, the Suntec Singapore Convention & Exhibition Centre should also benefit from the strong pipeline of corporate events lined up for 2020.

- **Key risks and earnings revisions.** Risks include a sharp slowdown in the economy that would result in a pullback in office demand and reversal of fund flows from the REIT sector. We also fine-tune our FY20F-21F DPU by 0-1%.

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (SGDm)	354.2	363.5	367.4	395.9	413.2
Net property income (SGDm)	244.5	241.0	238.0	256.4	265.6
Reported net profit (SGDm)	229.0	318.2	337.4	357.5	329.5
Distributable income (SGDm)	263.0	266.8	266.1	274.4	283.3
DPS (SG cents)	10.0	10.0	9.6	9.7	9.9
DPS growth (%)	0.0	(0.2)	(3.6)	0.6	2.4
P/BV (x)	0.86	0.87	0.87	0.86	0.85
Dividend yield (%)	5.5	5.5	5.3	5.3	5.4
Return on average equity (%)	4.1	5.6	5.7	5.9	5.4
Return on average assets (%)	2.5	3.3	3.4	3.5	3.1
Interest coverage (x)	3.6	4.1	3.6	3.4	3.6

Source: Company data, RHB

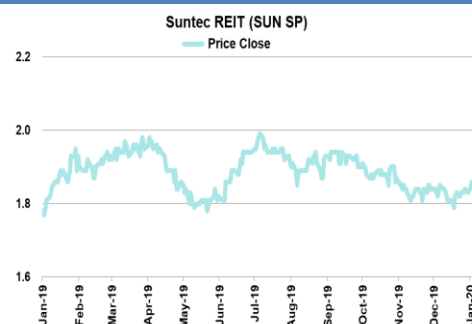
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	0.5	0.5	(2.6)	(5.1)	4.5
Relative	(0.2)	(1.1)	(5.8)	(1.4)	(1.2)
52-wk Price low/high (SGD)	1.76 – 2.01				



Source: Bloomberg

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Property | REITS

Financial Exhibits

Asia	Financial summary	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
Singapore	Recurring EPS (SGD)	0.08	0.12	0.12	0.12	0.11
Property	EPS (SGD)	0.08	0.12	0.12	0.12	0.11
Suntec REIT	DPS (SGD)	0.10	0.10	0.10	0.10	0.10
Bloomberg SUN SP	BVPS (SGD)	2.15	2.10	2.11	2.14	2.16
	Weighted avg adjusted shares (m)	2661	2671	2765	2833	2857
Valuation basis	Valuation metrics	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
We use DDM:	Recurring P/E (x)	21.8	16.0	15.4	15.0	16.5
i. COE of 6.7%;	P/E (x)	21.8	16.0	15.4	15.0	16.5
ii. Risk free rate of 2.75%;	P/B (x)	0.9	0.9	0.9	0.9	0.9
iii. 2% terminal growth.	FCF Yield (%)	3.4	4.1	3.4	4.0	4.1
	Dividend Yield (%)	5.4	5.4	5.2	5.3	5.4
Key drivers	EV/EBITDA (x)	29.9	28.6	28.0	26.6	24.9
i. Strong uptick in office rent;	EV/EBIT (x)	29.9	28.6	28.0	26.6	24.9
ii. Positive contribution from development assets;						
iii. Better-than-expected performance from the Suntec City retail component.						
Key risks	Income statement (SGDm)	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
i. Unexpected slowdown in retail and office demand;	Total turnover	354	364	367	396	413
ii. Delays in potential acquisition.	Gross profit	244	241	238	256	266
	EBITDA	274	298	309	336	359
	Depreciation and amortisation	0	0	0	0	0
	Operating profit	274	298	309	336	359
	Net interest	(76)	(72)	(85)	(98)	(101)
	Income from associates & JVs	0	0	0	0	0
	Exceptional income - net	0	0	0	0	0
	Pre-tax profit	247	331	337	358	330
	Taxation	(18)	(13)	0	0	0
	Minority interests	9	11	6	11	11
	Recurring net profit (adj)	229	318	337	358	330
Company Profile	Cash flow (SGDm)	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
Suntec REIT is a Singapore-based REIT established with the objective of investing in income-producing real estate properties that are used primarily for retail and office purposes.	Change in working capital	(5)	(17)	31	9	8
	Cash flow from operations	227	210	241	236	244
	Capex	(8)	(6)	(70)	(30)	(30)
	Cash flow from investing activities	6	(137)	(334)	(190)	122
	Dividends paid	(257)	(267)	(266)	(274)	(283)
	Cash flow from financing activities	(242)	(108)	145	(107)	(361)
	Cash at beginning of period	182	173	137	189	128
	Net change in cash	(10)	(34)	52	(61)	5
	Ending balance cash	173	137	189	128	132
	Balance sheet (SGDm)	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
	Total cash and equivalents	173	137	189	128	132
	Tangible fixed assets	6389	6496	6855	7120	7191
	Intangible assets	0	0	0	0	0
	Total investments	6389	6496	6855	7120	7191
	Total other assets	2680	2880	2976	3107	3139
	Total assets	9242	9512	10020	10354	10462
	Short-term debt	237	514	300	350	330
	Total long-term debt	2994	2978	3381	3531	3561
	Other liabilities	244	252	265	275	284
	Total liabilities	3475	3744	3946	4156	4175
	Shareholders' equity	5639	5637	5943	6067	6156
	Minority interests	128	132	132	132	132
	Total equity	5767	5768	6074	6199	6288
	Net debt	3058	3355	3492	3753	3759
	Total liabilities & equity	9242	9512	10020	10354	10462
	Key metrics	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
	Revenue growth (%)	7.8	2.6	1.1	7.7	4.4
	Recurrent EPS growth (%)	15.3	(26.7)	(3.9)	(2.0)	9.7
	Gross margin (%)	69.0	66.3	64.8	64.8	64.3
	Operating EBITDA margin (%)	77.3	81.9	84.2	84.8	87.0
	Net profit margin (%)	64.7	87.5	91.8	90.3	79.7
	Dividend payout ratio (%)	112.4	117.1	110.8	107.9	103.7
	Capex/sales (%)	2.4	1.6	19.1	7.6	7.3
	Interest cover (x)	3.6	4.1	3.6	3.4	3.6

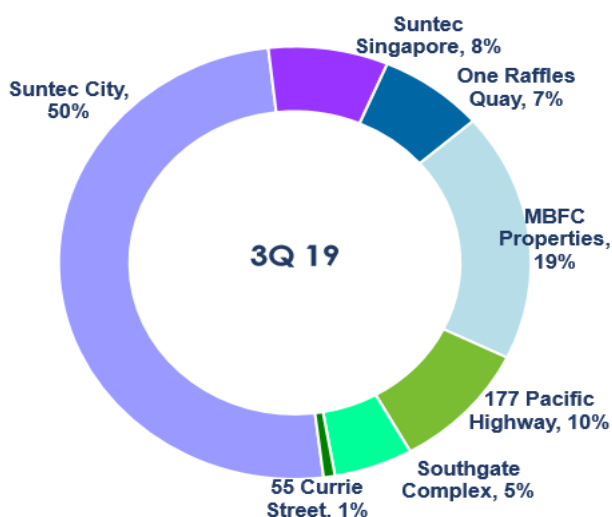
Source: Company data, RHB

Figure 1: Suntec REIT – fair value based on dividend discount model

DDM	FY19F	FY20F	FY21F	FY22F	FY23F	Terminal Value
DPU (SG cents)	9.62	9.69	9.92	10.29	10.62	230.03
Fair value (SGD)	2.08					
Current price (SGD)	1.84					
Price upside (%)	13.0					
Distribution yield (%)	5.2					
Total return (%)	18.3					
Assumptions						
Risk-free rate (%)	2.8					
Beta	0.6					
Cost of equity (%)	6.7					
Terminal growth (%)	2.0					

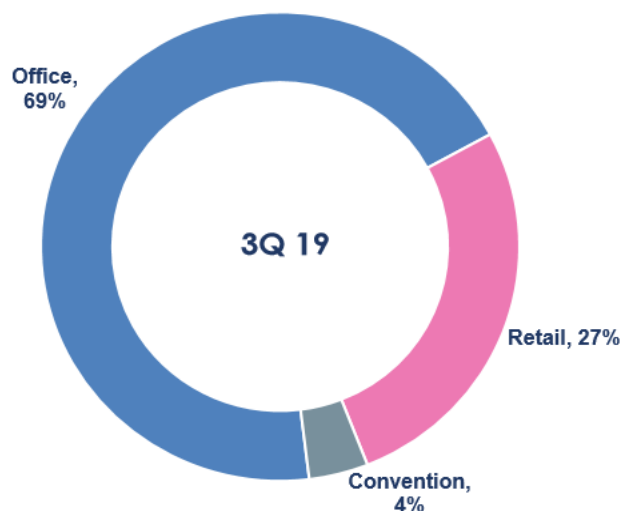
Source: Company data, RHB

Figure 2: Income contribution by asset



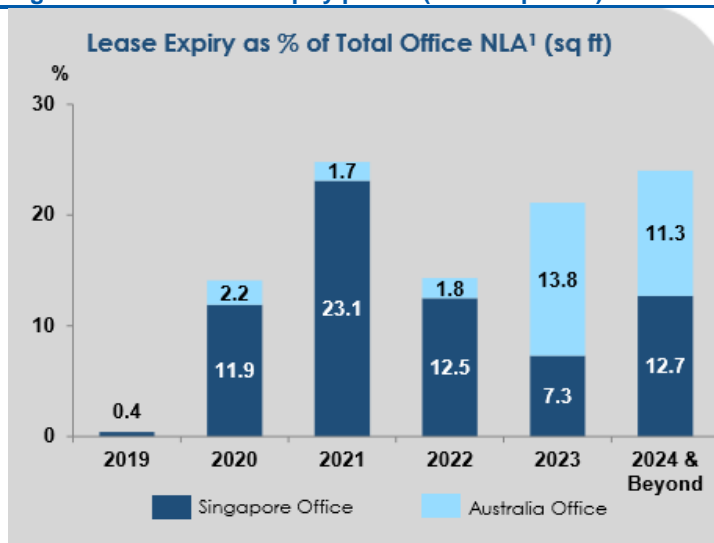
Source: Company data

Figure 3: Income contribution by segment



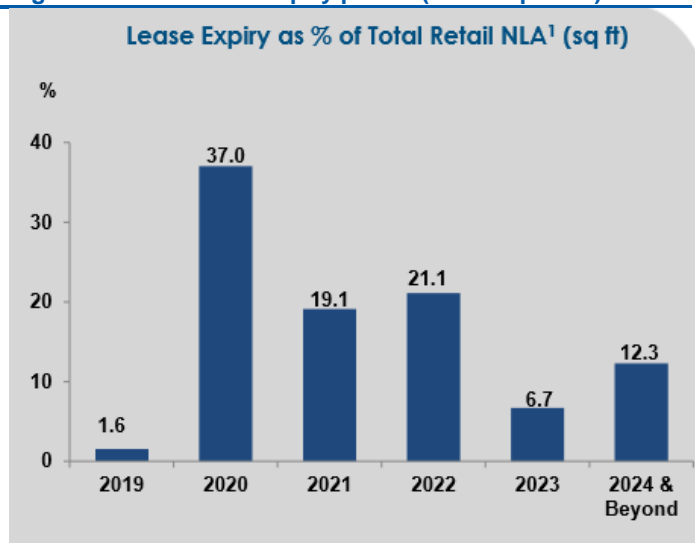
Source: Company data

Figure 4: Office lease expiry profile (as at Sep 2019)



Source: Company data

Figure 5: Retail lease expiry profile (as at Sep 2019)



Source: Company data

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