

26 July 2023

Property | REITS

Suntec REIT (SUN SP)

Neutral (Maintained)

Weighed Down By Cost Pressures

Target Price (Return): SGD1.40 (6.4%)
 Price (Market Cap): SGD1.32 (USD2,872m)
 ESG score: 3.2 (out of 4)
 Avg Daily Turnover (SGD/USD) 8.03m/5.99m

- **Still NEUTRAL, lower SGD1.40 TP from SGD1.47, 6% upside.** 1H23 results were below expectations due to higher-than-expected operating and interest costs. Operational performance continued to demonstrate resilience with high occupancy rates and healthy rent reversions, but these are expected to moderate in the coming quarters. While Suntec REIT remains undervalued at a c.40% discount to book value, we see limited catalysts – barring an earlier-than-expected peak in interest rates.
- **1H operational DPU down 30% YoY** due to higher financing costs, FX impact, and higher operating expenses. The REIT continued with a capital top-up of SGD11.5m for 1H, and has a SGD11.5m balance top-up from past gains, which is expected to be distributed in 2H. Revenue growth (+10% YoY) was dragged down by a 54% increase in net finance costs, which are expected to increase further in 2H and remain elevated next year. Property expenses rose 40% mainly from the increase of management corporation strata title (MCST) contributions for Suntec City. While no revaluations were done in 1H, based on its peer Keppel REIT's (KREIT SP, BUY, TP: SGD1.08) results and the REIT manager's guidance, overall valuations are expected to remain stable and unlikely to see a large decline of >3%.
- **Evaluating more divestment options.** SUN announced the divestment of three strata units at Suntec Office towers, which based on our estimates, works out to c.SGD30m in proceeds (c.20% above its carrying value). The REIT is exploring the possibility of divesting more Suntec strata office assets, including complete floors, to lower its gearing to 40% (from 42.6% currently). While divestment options are being evaluated for its Australian assets market, conditions remain challenging with limited buyers. SUN has also successfully negotiated with its lenders to lower the interest cover ratio on its loan covenants, giving it more flexibility in case of a prolonged high interest rate environment.
- **Operational metrics remain strong, but nearing peak levels.** Singapore committed office occupancy rose 0.4ppts QoQ to 99.3% with healthy 1H23 rent reversion of 10.8%. Australian office occupancy declined slightly by 0.7ppts QoQ to 96.6% and is likely to weaken further in 2H23. Singapore retail portfolio occupancy remains stable at 98.2% with Suntec City mall registering a strong +17.5% rent reversion in 1H23. Convention portfolio continues to see a strong recovery, with a full recovery expected in 2024.
- **We cut FY23-24F DPU by 6% and 7%** by adjusting our operating cost and interest cost assumptions higher. SUN's ESG score is raised to 3.2 based on our recently revised scoring methodology, which has higher weightage on the environmental metric. Our ESG premium is therefore raised to 4% (from 2%) to our DDM derived TP, based on an ESG score of 3.2.

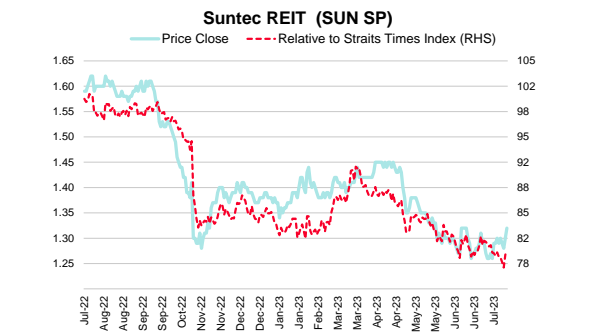
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(4.4)	4.8	(7.7)	(4.4)	(16.5)
Relative	(5.5)	1.8	(7.4)	(2.4)	(19.8)
52-wk Price low/high (SGD)				1.26	1.62



Source: Bloomberg

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (SGDm)	358	427	446	455	460
Net property income (SGDm)	255	316	318	322	323
Reported net profit (SGDm)	491	498	187	222	236
Total distributable income (SGDm)	247	256	202	201	208
DPS (SGD)	0.09	0.09	0.07	0.07	0.07
DPS growth (%)	16.9	2.7	(21.5)	(1.5)	2.6
P/B (x)	0.63	0.62	0.62	0.62	0.62
Dividend Yield (%)	6.5	6.7	5.3	5.2	5.3
Return on average equity (%)	8.3	8.2	3.0	3.6	3.8
Return on average assets (%)	4.3	4.3	1.6	1.9	2.0

Source: Company data, RHB

Overall ESG Score: 3.15 (out of 4)

E: EXCELLENT

All SUN's buildings are rated highly by respective green mark standards in respective countries. Has set net-zero carbon status by 2030 for assets with full ownership control and by 2050 for all assets across portfolio. Achieved 19.8%, 13.6% reduction in energy and water intensity in FY22 from FY19 levels.

S: GOOD

SUN has a diverse work profile with 68% of total employees being female. There were zero cases of reportable work-related injuries for employees in FY22. Average training hours was 35 hours per employee in FY22 – exceeding its target of 26 hours per employee.

G: GOOD

SUN has a well drawn-out whistleblowing policy for its employees. It has an experienced board with a balanced mix of independent directors. Transparent and timely disclosures of market-sensitive information and updates.

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Financial Exhibits

Asia	Financial summary	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Singapore	Recurring EPS (SGD)	0.17	0.17	0.06	0.08	0.08
Property	EPS (SGD)	0.17	0.17	0.06	0.08	0.08
Suntec REIT	DPS (SGD)	0.09	0.09	0.07	0.07	0.07
SUN SP	BVPS (SGD)	2.11	2.12	2.11	2.12	2.12
Neutral	Return on average equity (%)	8.3	8.2	3.0	3.6	3.8
	Weighted avg adjusted shares (m)	2,845.34	2,871.80	2,908.83	2,931.23	2,953.71
Valuation basis	Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Dividend Discount Model	Recurring P/E (x)	7.66	7.62	20.54	17.44	16.54
	P/E (x)	7.66	7.62	20.54	17.44	16.54
	P/B (x)	0.6	0.6	0.6	0.6	0.6
	FCF Yield (%)	6.3	6.8	5.8	6.3	6.3
	Dividend Yield (%)	6.5	6.7	5.3	5.2	5.3
	EV/EBITDA (x)	- 14.86	- 11.62	- 11.57	- 11.57	- 11.67
	EV/EBIT (x)	- 14.84	- 11.64	- 11.57	- 11.57	- 11.67
Key drivers	Income statement (SGDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
i. Continued recovery in Singapore office/retail demand;	Total turnover	358	427	446	455	460
ii. High quality office and retail assets offer resilience;	EBITDA	190	249	251	254	255
iii. Attractive valuation.	Depreciation and amortisation	0	(0)	(0)	0	0
	Operating profit	191	249	251	254	255
	Net interest	(94)	(112)	(155)	(164)	(160)
	Income from associates & JVs	103	145	144	146	147
	Pre-tax profit	516	514	205	240	254
	Taxation	(25)	(16)	(18)	(18)	(18)
	Recurring net profit	491	498	187	222	236
Key risks	Cash flow (SGDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Downside risks:	Change in working capital	(61)	(123)	(128)	(111)	(113)
i. Weaker performance from overseas assets and FX impact;	Cash flow from operations	243	273	253	275	276
ii. Continued increase in interest rates; and	Capex	(8)	(14)	(30)	(30)	(30)
iii. Sharp reduction in demand from WFH trends.	Cash flow from investing activities	(83)	126	114	116	118
	Dividends paid	(246)	(263)	(202)	(201)	(208)
	Cash flow from financing activities	(120)	(398)	(369)	(365)	(348)
	Cash at beginning of period	227	268	270	268	294
	Net change in cash	40	1	(2)	26	45
	Ending balance cash	267	269	268	294	340
Upside risk:	Balance sheet (SGDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
i. Major divestments at significant premium.	Total cash and equivalents	268	270	268	294	340
	Tangible fixed assets	1	1	1	1	1
	Total investments	11,384	11,413	11,520	11,548	11,549
	Total assets	11,689	11,710	11,825	11,881	11,927
	Short-term debt	500	646	650	580	600
	Total long-term debt	4,419	4,198	4,274	4,324	4,284
	Total liabilities	5,190	5,126	5,209	5,196	5,183
	Shareholders' equity	6,052	6,116	6,144	6,209	6,265
	Minority interests	99	120	123	127	131
	Total equity	6,499	6,584	6,616	6,684	6,744
	Net debt	4,651	4,574	4,656	4,610	4,544
	Total liabilities & equity	11,689	11,710	11,825	11,881	11,927
	Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Revenue growth (%)	13.5	19.3	4.4	2.0	1.1
	Recurrent EPS growth (%)	0.0	0.5	(62.9)	17.8	5.4
	Operating EBITDA margin (%)	53.1	58.3	56.2	55.9	55.4
	Net profit margin (%)	137.0	116.5	41.9	48.8	51.3
	Dividend payout ratio (%)	50.4	51.3	108.2	90.5	88.1
	Capex/sales (%)	2.2	3.3	6.7	6.6	6.5
	Interest cover (x)	2.02	2.22	1.62	1.55	1.59

Source: Company data, RHB

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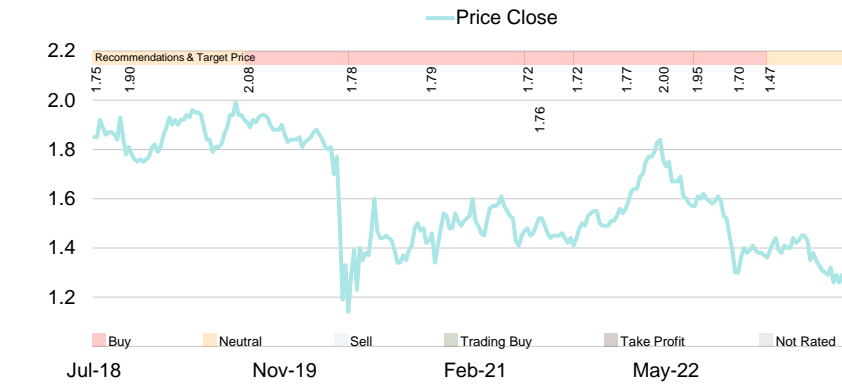
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Figure 1: SUN – fair value based on DDM

DDM	FY23F	FY24F	FY25F	FY26F	Terminal value
DPU (SGD cts)	6.95	6.85	7.03	7.37	146.05
Intrinsic value (SGD)	1.35				
ESG premium/(discount)	0.05				
TP (SGD)	1.40				
Current price (SGD)	1.380				
Price upside (%)	(2.2)				
Distribution yield (FY23F%)	5.0				
Total return (%)	2.9				
Assumptions					
Risk-free rate (%)	2.8				
Beta	0.8				
Cost of equity (%)	7.2				
Terminal growth (%)	2.0				

Source: RHB

Recommendation Chart

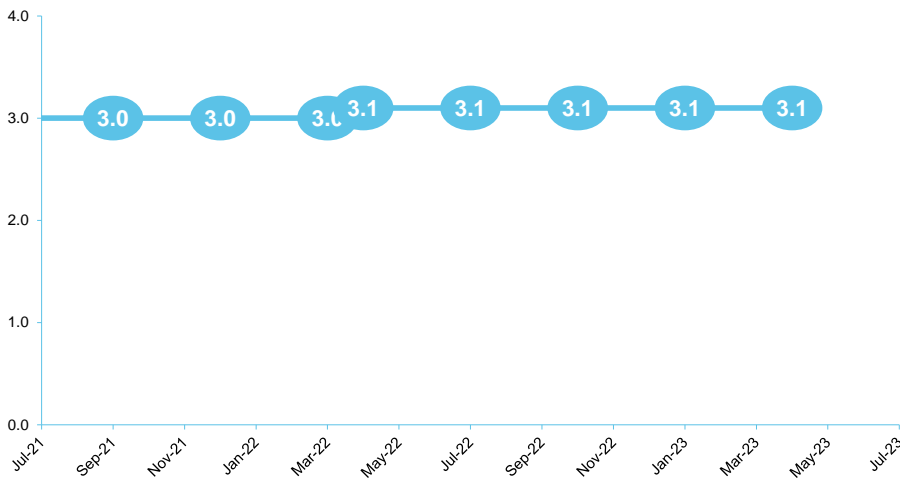


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2023-01-24	Neutral	1.47	1.39
2023-01-09	Neutral	1.47	1.37
2022-10-26	Buy	1.70	1.41
2022-07-17	Buy	1.95	1.57
2022-04-26	Buy	2.00	1.84
2022-01-27	Buy	1.77	1.55
2021-09-29	Buy	1.72	1.41
2021-07-01	Buy	1.76	1.47
2021-06-17	Buy	1.72	1.47
2021-06-02	Buy	1.72	1.46
2021-01-27	Buy	1.79	1.58
2020-10-11	Buy	1.79	1.42
2020-06-30	Buy	1.78	1.41
2020-04-02	Buy	1.78	1.20
2020-01-03	Buy	2.08	1.85

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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