

26 October 2022

Property | REITS

Keppel REIT (KREIT SP)

Buy (Maintained)

Operating Metrics Remain Strong

Target Price (Return): SGD1.15 (+30%)
 Price (Market Cap): SGD0.89 (USD2,331m)
 ESG score: 3.22 (out of 4)
 Avg Daily Turnover (SGD/USD) 9.31m/6.62m

- **Keep BUY, with new SGD1.15 TP from SGD1.31, 30% upside and 7% yield.** 3Q updates show continued positive momentum in the Singapore office portfolio with healthy occupancy improvement and strong rent growth. Outlook remains positive although slightly moderated lower, and should mitigate increasing interest costs' impact. Service charges are also being raised across all Keppel REIT's assets to counter higher utility charges. Unitholders will receive additional capital distribution (SGD20m pa over the next five years) from past divestment gains, thereby boosting dividends.
- **3Q/9M22 distributable income rose 1% and 3% YoY,** driven by rent growth and acquisitions that were partially offset by lower associate contributions. KREIT announced that it will reward unitholders and leading up to its 20th anniversary in 2026, it has set aside SGD100m from past capital gains or ~53 SG cents/share pa over the next five years, starting in 2H22 (~27 SG cents for 2H). This will be paid by drawing down debt from its revolving facilities. We are neutral on this move as we believe a targeted share buyback strategy or conserving cash could be a better option under current market conditions. Service charges at Marina Bay Financial Centre and One Raffles Quay have been raised by 20% from 3Q22 in light of rising utility charges and there are plans to implement a similar hike across all its Singapore assets in 2023.
- **Strong operational improvement across its Singapore assets.** Portfolio occupancy rose 1.3ppts QoQ to 96.8%, driven by healthy occupancy improvement across all its Singapore assets but partially offset by slight occupancy decline in Australia and South Korea. YTD rent reversion remains strong at 9.2% (3Q +9.7%), and excluding one large strategic lease, it would have been even higher at c.14% for the quarter. Management remains positive on rent growth outlook in Singapore as demand supply dynamics are still favourable. Physical occupancy (employees returning to the office) has reached a high 70% in Singapore and South Korea but remains low in Australia at 35-45%.
- **72% of its debt is hedged,** with every 50bps increase impacting DPU by 2.1%. It has SGD645m of loans (19%) due for expiry in 1H23 – management expects interest cost to increase by 150-200bps from the existing interest based on a 5-year fixed tenure. Currently, 22% and 4% of its borrowings are in AUD and KRW, providing a natural FX hedge; management also hedges a portion of its FX income 12-18 months forward.
- **We lift FY22-24F DPU by 3-4%,** factoring in capital top-ups and higher financing charges. We also raise our COE assumptions by 80bps to factor in light of rising cost of capital from a sharp hike in interest rates. ESG score of 3.2 out of 4.0 is two notches above the country median, as such, we apply a 4% premium to our intrinsic DDM value.

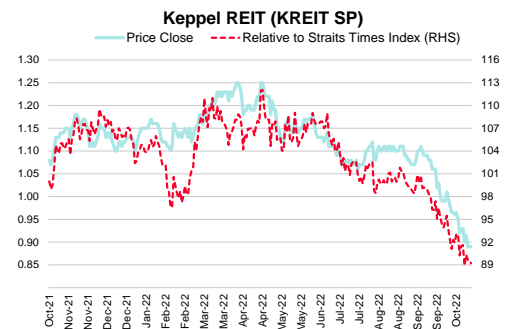
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(21.2)	(16.0)	(17.6)	(26.5)	(17.6)
Relative	(16.7)	(8.5)	(11.4)	(15.8)	(10.8)
52-wk Price low/high (SGD)	0.89 – 1.25				



Source: Bloomberg

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (SGDm)	170	217	223	229	232
Net property income (SGDm)	205	261	272	280	284
Reported net profit (SGDm)	74	367	313	345	346
Total distributable income (SGDm)	195	212	232	245	249
DPS (SGD)	0.06	0.06	0.06	0.06	0.06
DPS growth (%)	1.6	0.5	8.0	4.2	0.4
P/B (x)	0.67	0.68	0.68	0.68	0.68
Dividend Yield (%)	6.4	6.5	7.0	7.3	7.3
Return on average equity (%)	1.6	7.8	6.4	7.0	6.9
Return on average assets (%)	1.0	4.5	3.6	3.9	3.9

Source: Company data, RHB

Overall ESG Score: 3.22 (out of 4)

E: EXCELLENT

All of KREIT's Singapore buildings are Green Mark Platinum certified, with Keppel Bay Tower being the country's first zero-energy commercial building that is fully powered by renewable energy. Greenhouse gas emissions, energy, and water usage intensity were down 11%, 13%, and 32% in FY20, partly helped by COVID-19 lockdowns.

S: GOOD

In 2020, together with the staff of Keppel Capital, the REIT contributed a total of c.790 hours for various community initiatives. 74% of KREIT's full-time employees are female.

G: GOOD

Majority independent board. There is improving transparency levels in earnings and information disclosures, as well as well-established corporate governance frameworks related to board matters.

Financial Exhibits

Asia	Financial summary	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Singapore	Recurring EPS (SGD)	0.02	0.10	0.08	0.09	0.09
Property	EPS (SGD)	0.02	0.10	0.08	0.09	0.09
Keppel REIT	DPS (SGD)	0.06	0.06	0.06	0.06	0.06
KREIT SP	BVPS (SGD)	1.32	1.32	1.31	1.32	1.32
Buy	Return on average equity (%)	1.6	7.8	6.4	7.0	6.9
	Weighted avg adjusted shares (m)	3,396.80	3,636.75	3,724.97	3,772.97	3,821.30
Valuation basis						
DDM	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Recurring P/E (x)	40.63	8.82	10.59	9.75	9.82
	P/E (x)	40.63	8.82	10.59	9.75	9.82
	P/B (x)	0.7	0.7	0.7	0.7	0.7
	FCF Yield (%)	5.4	8.8	1.9	3.9	3.8
	Dividend Yield (%)	6.4	6.5	7.0	7.3	7.3
	EV/EBITDA (x)	1.36	3.15	2.57	2.90	2.84
	EV/EBIT (x)	3.43	3.32	3.47	3.60	3.60
Key drivers						
i.	Positive outlook for Singapore office sector with firm demand and limited supply;					
ii.	Strong quality Grade-A assets and sponsor;					
iii.	Inorganic and merger opportunities.					
Key risks						
i.	Sharp slowdown in economy and re-imposition of COVID-19 restrictions;					
ii.	Sharp deceleration in tech demand and increase in shadow spaces;					
iii.	Downsizing and right-sizing of office spaces by key tenants.					
Company Profile						
Keppel REIT is a real estate investment trust listed on the Singapore Exchange Securities Trading Limited. Sponsored by Keppel Land, the trust owns and invests in a portfolio of income-producing commercial real estate and real estate related-assets in Singapore and across Asia.						
	Income statement (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total turnover	170	217	223	229	232
	EBITDA	407	208	273	258	269
	Depreciation and amortisation	(246)	(11)	(71)	(50)	(57)
	Operating profit	161	197	202	208	212
	Net interest	(32)	(36)	(37)	(43)	(51)
	Income from associates & JVs	118	119	120	123	128
	Pre-tax profit	74	367	313	345	346
	Recurring net profit	74	367	313	345	346
	Cash flow (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Change in working capital	47	150	(83)	(13)	(15)
	Cash flow from operations	176	298	76	145	145
	Capex	(11)	(12)	(14)	(14)	(15)
	Cash flow from investing activities	(147)	(352)	25	28	143
	Dividends paid	(192)	(203)	(222)	(239)	(247)
	Cash flow from financing activities	2	88	(141)	(170)	(302)
	Cash at beginning of period	125	155	189	149	151
	Net change in cash	31	34	(40)	2	(14)
	Ending balance cash	155	189	149	151	137
	Balance sheet (SGDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total cash and equivalents	155	189	149	151	137
	Total investments	7,589	8,262	8,522	8,747	8,863
	Total assets	7,764	8,488	8,709	8,936	9,039
	Short-term debt	153	188	200	300	500
	Total long-term debt	2,222	2,539	2,664	2,694	2,509
	Total liabilities	2,544	2,898	3,057	3,194	3,213
	Shareholders' equity	4,498	4,866	4,912	4,987	5,055
	Minority interests	420	422	438	454	470
	Total equity	5,220	5,590	5,651	5,743	5,826
	Net debt	2,220	2,538	2,715	2,843	2,872
	Total liabilities & equity	7,764	8,488	8,709	8,936	9,039
	Key metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Revenue growth (%)	3.8	27.2	2.7	2.9	1.3
	Recurrent EPS growth (%)	(66.5)	360.7	(16.7)	8.7	(0.8)
	Operating EBITDA margin (%)	239.2	96.0	122.7	112.8	115.9
	Net profit margin (%)	43.7	169.4	140.7	150.5	149.3
	Dividend payout ratio (%)	261.6	57.8	74.1	71.1	71.9
	Capex/sales (%)	6.3	5.5	6.1	6.2	6.3
	Interest cover (x)	3.19	3.83	3.62	3.36	3.03

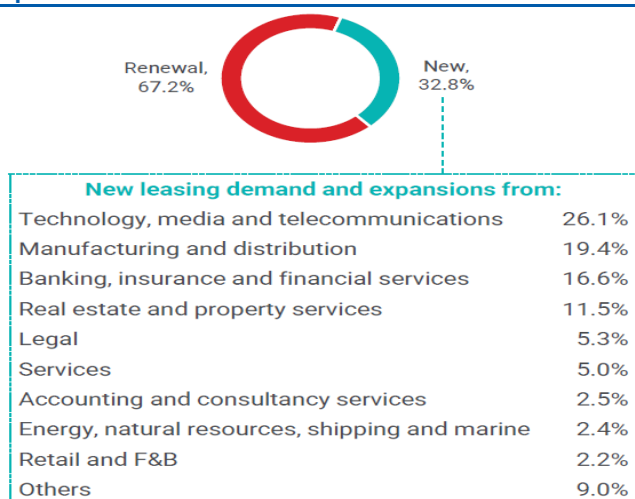
Source: Company data, RHB

Figure 1: KREIT – fair value based on dividend discount model

DDM	FY22F	FY23F	FY24F	FY25F	Terminal Value
DPU (SG cents)	6.20	6.46	6.49	6.67	120.46
Fair value (SGD)	1.11				
ESG Premium/(discount)	0.04				
Target Price (SGD)	1.15				
Current price (SGD)	0.89				
Price upside (%)	29.7%				
Distribution yield (%)	7.0%				
Total returns (%)	36.7%				
Assumptions					
Risk-free rate (%)	2.8				
Beta	0.9				
Cost of equity (%)	7.6				
Terminal growth (%)	2.0				

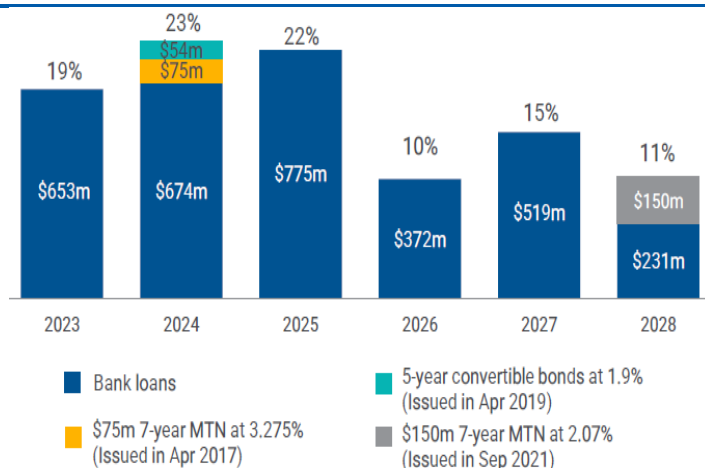
Source: RHB

Figure 2: Leasing demand doubled in 3Q with higher proportion of new demand



Source: Company data. RHB

Figure 3: Debt maturity profile



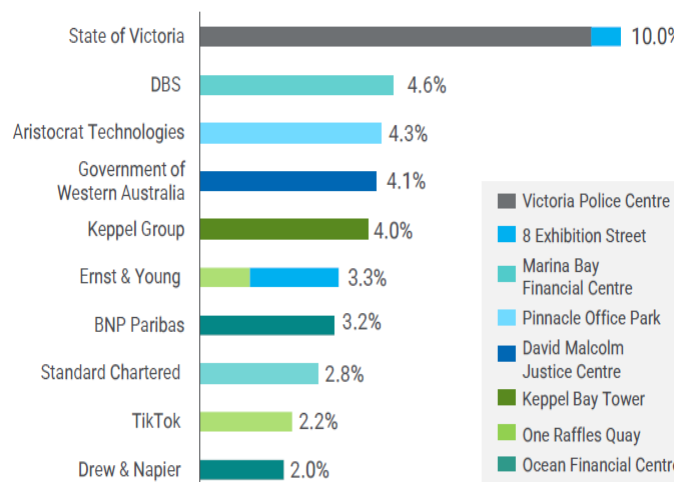
Source: Company data. RHB

Figure 4: Tenant mix by sector

Tenant Business Sector	%
Banking, insurance and financial services	29.0%
Government agency	14.9%
Technology, media and telecommunications	14.1%
Manufacturing and distribution	7.5%
Legal	7.0%
Energy, natural resources, shipping and marine	6.7%
Real estate and property services	6.3%
Accounting and consultancy services	5.2%
Services	3.2%
Retail and food & beverage	2.7%
Others	3.4%
Total	100%

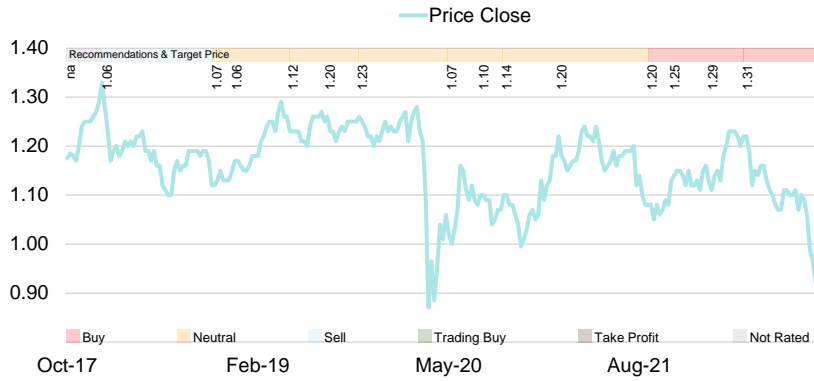
Source: Company data. RHB

Figure 5: High quality Top 10 tenants



Source: Company data. RHB

Recommendation Chart

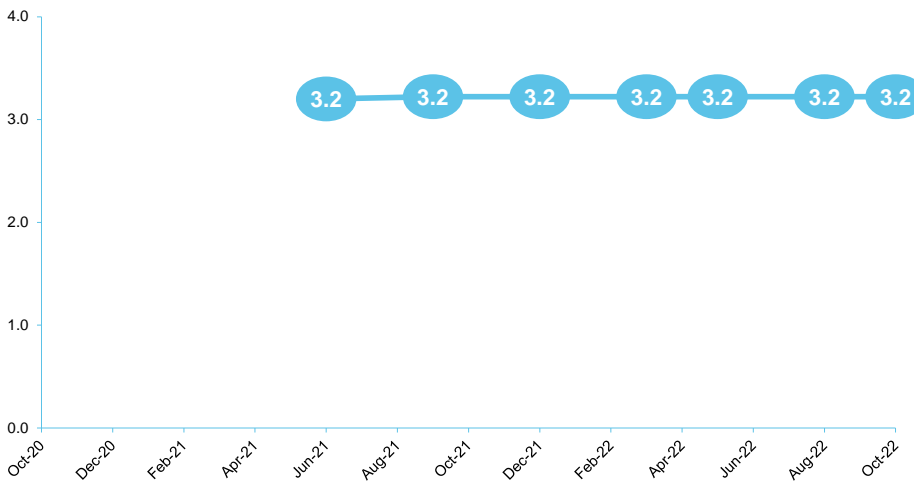


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-04-20	Buy	1.31	1.19
2022-01-26	Buy	1.29	1.16
2021-10-26	Buy	1.25	1.07
2021-08-31	Buy	1.20	1.05
2021-01-26	Neutral	1.20	1.20
2020-09-14	Neutral	1.14	1.08
2020-07-20	Neutral	1.10	1.09
2020-05-04	Neutral	1.07	1.03
2019-10-17	Neutral	1.23	1.25
2019-10-02	Neutral	1.23	1.26
2019-07-16	Neutral	1.20	1.27
2019-04-18	Neutral	1.12	1.23
2019-01-22	Neutral	1.06	1.17
2018-12-03	Neutral	1.06	1.17
2018-10-16	Neutral	1.07	1.12

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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