

20 October 2020

Property | REITS

## Keppel REIT (KREIT SP)

### Another Stable Quarter

**Neutral** (Maintained)

Target Price (Return): SGD1.14 (+8%)  
 Price: SGD1.06  
 Market Cap: USD2,654m  
 Avg Daily Turnover (SGD/USD): 6.52m/4.77m

#### Analyst

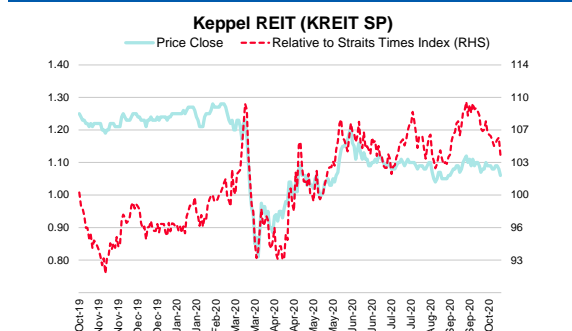
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- **NEUTRAL and SGD1.14 TP, 8% upside.** Keppel REIT's 3Q20 distributable income rose 4.6% YoY, aided by the recently completed 311 Spencer Street and lower interest expenses. Despite COVID-19, Management noted 3Q office leasing demand surpassed expectations with strong double-digit rent reversions (+15%). KREIT has been pivoting towards rental stability with recent Australian acquisitions offering long weighted average lease expiry. One concern, however, is the anticipated downsizing by financial institution tenants (36% of total) in the medium term.
- **A decent quarter in terms of leasing driven by financial institutions.** KREIT signed ~330,000 sqf of new leases in 3Q20, primarily driven by office demand from smaller fund houses and insurance companies. Overall occupancy remained high at 98.3%, with 97% of 3Q rents collected. Average signing rents (3Q) were higher 1% QoQ at SGD11.03 psf/month (psfpm) despite the overall market decline due to a good size of spaces that were leased and relocation demand from financial institutions.
- **Rent reversion (3Q) was healthy at 15% (YTD: +15.4%).** Management however cautioned that it expects rental pressure in the coming quarters as companies reassess leasing options post COVID-19, but overall, it still expects high single-digit rent reversions for 2021 as average expiring rents are still ~15% below current signing rents. As at 3Q20, only SGD1.7m of rents have been deferred (2Q: SGD1.6m) and KREIT has provided SGD13.8m in tenant relief (2Q: SGD12.5m) including an estimated SGD10m of government property tax rebates and cash grants.
- **Keppel Bay Tower potential near-term acquisition target.** With the recent asset enhancement initiative (AEI) completion and achievement of the Green Mark Platinum standard, KREIT sees Keppel Bay Tower as a good fit to its portfolio, if the sponsor chooses to divest. The acquisition, however, will depend on pricing and DPU accretion. The REIT in September announced the acquisition of Pinnacle Office Park – a Grade-A commercial building located near Macquarie Park metro station in Sydney – for AUD306m (SGD303.3m), which is expected to be completed in 4Q. It also issued SGD300m of perpetual securities in 3Q, part of which will be used to fund the acquisition. Gearing post acquisition stands comfortable at 36.9% providing >SGD 500m of debt headroom for future acquisitions (assuming 40% as a comfortable level). All-in interest costs have also come down by 43bps to 2.39% pa, aided by lower interest rates. KREIT also has >SGD50m in capital gains, which can be used to smoothen out distribution and potential share buybacks.
- **No changes to our earnings estimates.**

#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(14.5)	(4.5)	(1.9)	8.7	(14.5)
Relative	6.9	(5.6)	1.6	11.7	4.7
52-wk Price low/high (SGD)				0.81	1.28



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (SGDm)	166	164	157	173	174
Net property income (SGDm)	199	199	191	213	215
Reported net profit (SGDm)	230	223	270	307	286
Total distributable income (SGDm)	189	92	193	210	220
DPS (SGD)	0.06	0.06	0.06	0.06	0.06
DPS growth (%)	(2.5)	0.4	1.5	7.2	3.6
P/B (x)	0.76	0.78	0.77	0.76	0.77
Dividend Yield (%)	5.2	5.3	5.3	5.7	5.9
Return on average equity (%)	4.8	4.8	5.8	6.5	5.9
Return on average assets (%)	3.0	2.9	3.5	3.9	3.6

Source: Company data, RHB

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## Financial Exhibits

<b>Asia</b>	<b>Financial summary</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
Singapore	Recurring EPS (SGD)	0.07	0.07	0.08	0.09	0.08
Property	EPS (SGD)	0.07	0.07	0.08	0.09	0.08
<b>Keppel REIT</b>	DPS (SGD)	0.06	0.06	0.06	0.06	0.06
KREIT SP	BVPS (SGD)	1.40	1.36	1.38	1.39	1.39
Neutral	Return on average equity (%)	4.8	4.8	5.8	6.5	5.9
	Weighted avg adjusted shares (m)	3,397.64	3,397.14	3,393.13	3,434.58	3,475.88
<b>Valuation basis</b>	<b>Valuation metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
DDM methodology	Recurring P/E (x)	15.64	16.12	13.34	11.87	12.89
	P/E (x)	15.64	16.12	13.34	11.87	12.89
<b>Key drivers</b>	P/B (x)	0.8	0.8	0.8	0.8	0.8
i. Rebound in Singapore economy resulting in better office sector demand;	FCF Yield (%)	3.3	(10.3)	2.7	2.9	2.0
ii. Strong quality Grade-A assets and sponsor;	Dividend Yield (%)	5.2	5.3	5.3	5.7	5.9
iii. Bottoming out of Singapore office supply.	EV/EBITDA (x)	1.30	0.99	1.70	1.54	1.34
	EV/EBIT (x)	2.08	1.55	2.33	1.99	1.97
<b>Key risks</b>	<b>Income statement (SGDm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
i. Prolonged recession and increased risk of second COVID-19 wave;	Total turnover	166	164	157	173	174
ii. Rising trend of work from home and flex office space;	EBITDA	206	204	167	190	217
iii. Downsizing and right sizing of office space by key tenants.	Depreciation and amortisation	(77)	(75)	(45)	(43)	(70)
	Operating profit	129	130	122	147	148
	Net interest	(44)	(37)	(34)	(37)	(37)
	Income from associates & JVs	104	106	130	144	148
	Pre-tax profit	230	223	270	307	286
	Recurring net profit	230	223	270	307	286
<b>Company Profile</b>	<b>Cash flow (SGDm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
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	Change in working capital	2	(471)	3	3	(35)
	Cash flow from operations	130	(361)	108	118	87
	Capex	(11)	(12)	(11)	(12)	(12)
	Cash flow from investing activities	30	605	(141)	161	165
	Dividends paid	(190)	(141)	(143)	(201)	(215)
	Cash flow from financing activities	(410)	(378)	53	(261)	(275)
	Cash at beginning of period	198	259	125	144	162
	Net change in cash	(251)	(134)	19	18	(22)
	Ending balance cash	(52)	125	144	162	140
	<b>Balance sheet (SGDm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Total cash and equivalents	259	125	144	162	140
	Total investments	7,510	7,307	7,689	7,798	7,882
	Total assets	7,784	7,449	7,850	7,979	8,040
	Short-term debt	60	100	670	874	0
	Total long-term debt	2,226	2,022	1,714	1,520	2,404
	Total liabilities	2,449	2,286	2,547	2,571	2,582
	Shareholders' equity	4,757	4,585	4,710	4,800	4,836
	Minority interests	429	429	444	458	472
	Total equity	5,336	5,164	5,303	5,408	5,458
	Net debt	2,027	1,997	2,240	2,232	2,264
	Total liabilities & equity	7,784	7,449	7,850	7,979	8,040
	<b>Key metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Revenue growth (%)	0.8	(1.1)	(4.4)	10.3	0.8
	Recurrent EPS growth (%)	(15.1)	(3.0)	20.9	12.4	(7.9)
	Operating EBITDA margin (%)	124.2	124.4	106.8	109.6	124.6
	Net profit margin (%)	138.8	136.1	172.0	177.4	163.9
	Dividend payout ratio (%)	82.1	41.3	0.0	0.0	0.0
	Capex/sales (%)	6.7	7.2	6.9	6.9	7.0
	Interest cover (x)	1.86	2.01	2.09	2.40	2.41

Source: Company data, RHB

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

	FY20F	FY21F	FY22F	FY23F	Terminal Value
DPU (SG cents)	5.66	6.07	6.22	6.29	123.9
<b>Fair value (SGD)</b>	<b>1.14</b>				
Current price (SGD)	1.06				
Price upside (%)	7.5%				
Distribution yield (%)	5.3%				
Total returns (%)	12.8%				
<b>Assumptions</b>					
Risk-free rate (%)	2.8				
Beta	0.8				
Cost of equity (%)	7.2				
Terminal growth (%)	2.0				

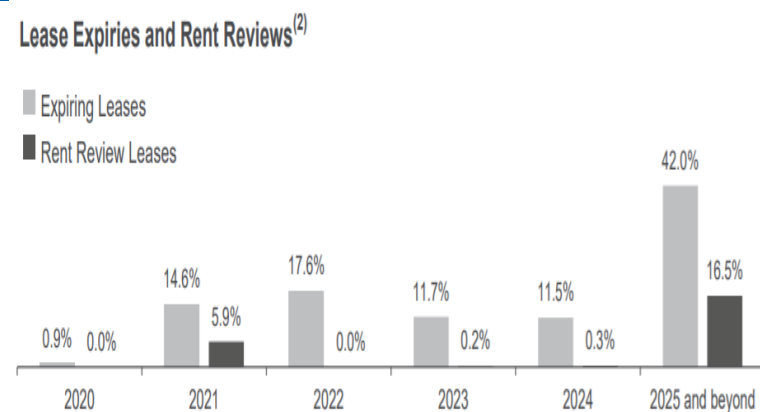
Source: RHB

Figure 2: 3Q20 financial performance summary (SGDm)

	3Q 2020	3Q 2019	+/(−)	9M 2020	9M 2019	+/(−)
<b>Property Income<sup>(1)</sup></b>	\$44.8m	\$42.4m	+5.7%	\$120.3m	\$122.3m	(1.6%)
<b>Net Property Income (NPI)</b>	\$35.6m	\$33.2m	+7.2%	\$94.6m	\$95.5m	(0.9%)
Less: Attributable to Non-controlling Interests	(\$4.3m)	(\$4.2m)	+2.4%	(\$12.7m)	(\$12.5m)	+1.6%
<b>NPI Attributable to Unitholders</b>	\$31.3m	\$29.0m	+7.9%	\$81.9m	\$83.0m	(1.3%)
<b>Share of Results of Associates<sup>(2)</sup></b>	\$23.1m	\$21.3m	+8.5%	\$63.6m	\$60.4m	+5.3%
<b>Share of Results of Joint Ventures<sup>(3)</sup></b>	\$8.2m	\$7.3m	+12.3%	\$21.9m	\$21.6m	+1.4%
<b>Distributable Income from Operations</b>	\$47.6m	\$45.5m	+4.6%	\$132.4m	\$134.1m	(1.3%)
<b>Capital Gains Distribution</b>	N.a. <sup>(4)</sup>	\$2.0m	N.m.	\$10.0m <sup>(4)</sup>	\$8.0m	+25.0%

Source: Company data

Figure 3: Lease expiries post 3Q20



Source: Company data

Figure 4: Tenant sector breakdown



Source: Company data

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## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-09-14	Neutral	1.14	1.08
2020-07-20	Neutral	1.10	1.09
2020-05-04	Neutral	1.07	1.03
2019-10-02	Neutral	1.23	1.26
2019-07-16	Neutral	1.20	1.27
2019-04-18	Neutral	1.12	1.23
2018-12-03	Neutral	1.06	1.17
2018-10-16	Neutral	1.07	1.12
2018-01-24	Sell	1.06	1.30

Source: RHB, Bloomberg

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<b>Not Rated:</b>	Stock is not within regular research coverage

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