Singapore Company Guide

Starhill Global REIT

Version 11 | Bloomberg: SGREIT SP | Reuters: STHL.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

4 Feb 2020

BUY

Last Traded Price (3 Feb 2020): S$0.715 (**STI :** 3,116.31)
Price Target 12-mth: S$0.80 (12% upside)

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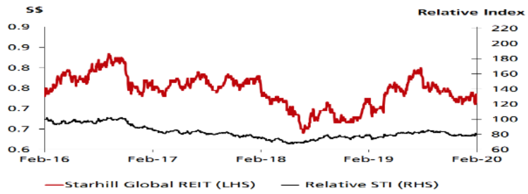
What's New

- DPU of 1.13 Scts was flat y-o-y, and 1HFY19/20 DPU makes up c.97% of our full-year forecast
- Starhill Gallery continues to take a toll on top and bottom lines as the asset is being future-proofed
- Overall portfolio performance remains healthy, with a 20-bp rise in occupancy rate to 96.5%
- Wisma Atria was the star of this quarter, with tenant sales growing 13.0% y-o-y

Price Relative



Forecasts and Valuation

FY Jun (S$m)	2018A	2019A	2020F	2021F
Gross Revenue	209	206	212	213
Net Property Inc	162	159	157	157
Total Return	84.2	65.6	94.6	91.5
Distribution Inc	103	101	102	99.8
EPU (S cts)	4.90	3.94	4.33	4.18
EPU Gth (%)	(8)	(20)	10	(4)
DPU (S cts)	4.55	4.48	4.46	4.46
DPU Gth (%)	(8)	(2)	0	0
NAV per shr (S cts)	91.2	88.5	88.1	87.6
PE (X)	14.6	18.2	16.5	17.1
Distribution Yield (%)	6.4	6.3	6.2	6.2
P/NAV (x)	0.8	0.8	0.8	0.8
Aggregate Leverage (%)	36.4	37.1	37.7	38.3
ROAE (%)	5.3	4.4	4.9	4.8
Distn. Inc Chng (%):			(4)	(5)
Consensus DPU (S cts):			4.60	4.60
Other Broker Recs:		B: 2	S: 1	H: 4

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Turning headwinds into tailwinds

Transitional phase with Malaysia redevelopment; maintain BUY. We like Starhill Global REIT (SGREIT) for its diversified earnings base supported by c.49% of revenues pegged to stable long-term leases with periodic rent reviews. This should help weather against a potential dip in tourist arrival receipts within the Singapore malls following the coronavirus outbreak. Yields are attractive at north of 6.1% within minimal downside risk.

Exposure to actively managed retail leases limited to just 25% of gross rents. Of the 51% actively managed leases under SGREIT, half pertains to office leases within Wisma Atria and Ngee Ann City, limiting exposure to actively managed retail leases to just 25%. Moreover, c.6% of leases by gross rents will be due for renewal in the next two quarters, including c.4% originating from Wisma Atria, for which we see upside given improving operating metrics.

Future-proofing of Starhill Gallery. Competition within the mid- to high-end retail in Kuala Lumpur is likely to intensify, with retail supply within a 10-km radius from Starhill Gallery and Lot 10 increasing by approximately 31% over a five-year period. Income visibility will be greatly enhanced with a new master lease agreement of 19.5 years and 9.0 years for Starhill Gallery and Lot 10 respectively, and in-built periodic rental escalations of 4.75-6.0% in every three-yearly review.

Valuation:

BUY; DCF-based TP maintained at S$0.80. We included the debt-funded redevelopment of Starhill Gallery and the associated rental upside in our forecasts, while adjusting retail rents from Wisma Atria considering a low base in FY19.

Key Risks to Our View:

Fall in tourist expenditure. A fall in tourist arrivals and receipts in the face of a WHO global emergency declaration could be detrimental to SGREIT's distribution prospects.

At A Glance

Issued Capital (m shrs)	2,184
Mkt. Cap (Sm/USm)	1,562 / 1,141
Major Shareholders (%)	
YTL Corp Bhd	35.7
AIA Group Ltd	7.6
Free Float (%)	56.7
3m Avg. Daily Val (US$m)	1.00

GIC Industry : Real Estate / Equity Real Estate Investment (REITs)

WHAT'S NEW

(+/-) DPU marginally below as Starhill Gallery undergoes major refurbishment

- Starhill Global REIT's (SGREIT) 2QFY20 revenue and NPI of S$48.7m and S$37.2m was a 4.5% and 5.9% dip y-o-y respectively.
- This was mainly due to rental rebates extended to the master tenant in Starhill Gallery as the asset undergoes redevelopment.
- Excluding Starhill Gallery, revenue and NPI for SGREIT portfolio in 2QFY20 would have been stable, declining marginally by 0.4% and 0.6% over 2Q FY18/19 respectively. This mainly came from the weakening AUD coupled with a dip in revenues from its Singapore office properties due to lower occupancy rates at Ngee Ann City.
- Reported DPU of 1.13 Scts for the quarter was flattish y-o-y, bringing 1HFY20 DPU to 2.26 Scts, which makes up 45% of our forecasts.

(-) Rental rebates at Starhill Gallery (Malaysia) due to ongoing refurbishment works

- For Malaysia, revenue and NPI in 2Q FY19/20 were lower by 27.5% and 28.4% y-o-y respectively, as Starhill Gallery undergoes AEI works and redevelopment into an integrated development.
- The decline is mainly due to the loss in rental income as part of the mall is phased out for AEI, which is scheduled for completion by the end of next year (2021 or 1HFY22) and will be renamed "The Starhill" upon completion.
- Rental rebate is extended to SGREIT by sponsor (50% of annual rental of RM52m) and will be given for the first two years of its construction (up to June 2021).

(+) Other key markets remain healthy

- Higher revenue and NPI contributions from the Singapore retail (Revenue and NPI for 2Q FY19/20 rose by 1.5% and 1.4% y-o-y respectively) component neutralised the lower contributions from the Singapore office (revenue and NPI were lower by 6.4% and 8.7% y-o-y respectively) component.
- Wisma Atria demonstrated an uplift in popularity as tenant sales grew 13.0% y-o-y for the quarter, despite a 3.7% y-o-y fall in footfall traffic.
- As at 31 December 2019, Wisma Atria and Ngee Ann City stood at an occupancy of 100% and 99.4% respectively.
- Office occupancy at Ngee Ann City dipped from 93.6% to 89.2% q-o-q due to the pre-termination of a single tenant, while that for Wisma Atria rose from 87.7% to 91.3% for the same period.
- Australia assets posted stronger operational performance but reported a y-o-y decline from a weaker AUD with revenue and NPI declining 3.4% and 4.8% y-o-y respectively. From an operational standpoint, occupancies rose for both Perth properties (97.6% to 98% q-o-q) and Myer Centre Adelaide (90.0% to 92.6% q-o-q).
- Revenue and NPI from SGREIT's China and Japan properties inched up 1.1% and 2.3% y-o-y with full occupancies for the two Japanese assets.

(+) Future-proofing of Starhill Gallery

- Competition within the mid- to high-end retail in Kuala Lumpur is likely to intensify, with retail supply within a 10-km radius from Starhill Gallery and Lot 10 increasing by approximately 31% over a 5-year period to 27m sqft in 2023.
- The ongoing two-year asset enhancement initiative will aim to refresh the interior retail space with a modern and contemporary design and convert the upper three floors into hotel rooms, a necessary step forward to maintain Starhill Gallery's position as a prime mall within Kuala Lumpur.
- The master lease arrangement within Starhill Gallery and Lot 10 will be extended by another 19.5 years and 9.0 years respectively from June 2019.
- Income visibility is greatly enhanced with rents estimated to be 1.5% higher, with in-built periodic rental escalations of 4.75-6.0% in every three-yearly reviews, extending the long-term trajectory of the asset.

(+) Portfolio and financial metrics remain robust

- Overall portfolio occupancy inched up 20 bps to 96.5% for the quarter, while portfolio WALE remains very well-staggered at 9.1 and 5.9 years (by NLA and gross rent respectively), extended by the Toshin master lease, master tenancy agreements for Malaysia Properties and the anchor leases in Australia and China.
- There remains a good mix between master anchor leases and actively managed leases at a proportion of 49:51.
- Only 3.3% and 6.0% of leases by NLA and gross rent respectively will be expiring in the remaining two quarters of FY19/20.
- Gearing and cost of debt stood at 36.3% and 3.29% respectively, with 89% of borrowings hedged on a fixed rate.

Quarterly / Interim Income Statement (S$m)

FY Jun	2Q2019	1Q2020	2Q2020	% chg yoy	% chg qoq
Gross revenue	51.0	48.0	48.7	(4.5)	1.6
Property expenses	(11.5)	(11.1)	(11.6)	0.3	4.5
Net Property Income	39.5	36.9	37.2	(5.9)	0.7
Other Operating expenses	(5.0)	(4.8)	(5.3)	6.5	11.4
Other Non Opg (Exp)/Inc	(5.2)	(0.5)	0.0	nm	nm
Associates & JV Inc	0.0	0.0	0.0	-	-
Net Interest (Exp)/Inc	(9.6)	(9.7)	(9.7)	(1.7)	(0.5)
Exceptional Gain/(Loss)	0.0	0.0	0.0	-	-
Net Income	**19.7**	**22.0**	**22.1**	**12.2**	**0.6**
Tax	(0.9)	(0.7)	(0.7)	(20.6)	3.8
Minority Interest	0.0	0.0	0.0	-	-
Net Income after Tax	**18.9**	**21.3**	**21.4**	**13.7**	**0.5**
Total Return	0.0	0.0	0.0	-	-
Non-tax deductible Items	6.30	4.00	3.72	(40.9)	(6.9)
Net Inc available for Dist.	24.6	24.7	24.7	0.3	0.1
Ratio (%)					
Net Prop Inc Margin	77.4	76.9	76.3		
Dist. Payout Ratio	98.0	97.4	98.2		

Source of all data: Company, DBS Bank

CRITICAL DATA POINTS TO WATCH

Critical Factors

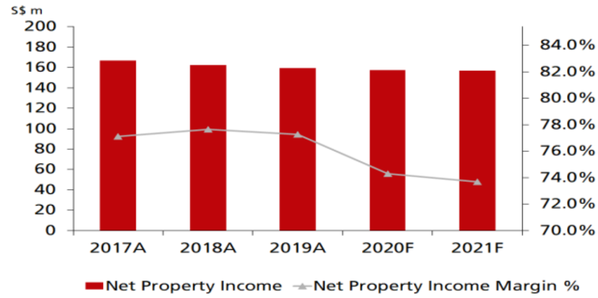
A proxy for Singapore tourist spending. The most distinctive feature for SGREIT is its exposure to Orchard Road, Singapore's prime shopping district. Historical operational performance shows that performance for malls along Orchard road has more volatility and is more sensitive to non-discretionary spending which can be boosted by higher tourist arrivals and spending.

We found that tourist arrivals have a high correlation coefficient of 0.74 with SGREIT's price. This could be explained by high tourist spending translating into retail sales and in turn SGREIT's earnings and distribution, given that its Singapore assets (Wisma Atria and Ngee Ann City) contributed c.63% of SGREIT's NPI in FY18/19. Downside risk to our forecast would be the risk of falling tourist spending at Orchard Road prolonging in the coming quarters as tourist arrivals dip in the face of a WHO global emergency declaration.

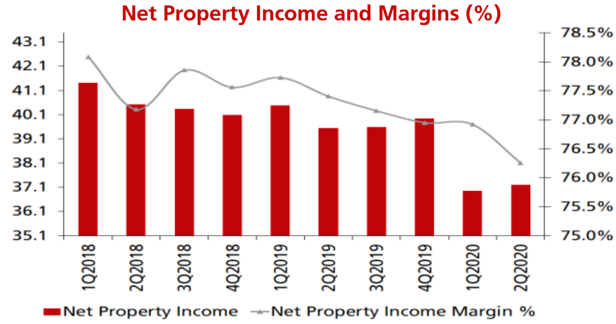
Strong earnings visibility with close to 50% of income pegged to master leases or long leases. Income from master leases and long-term leases with key anchors (Myer Pty Ltd and David Jones Limited) accounts for 49% of revenues, implying good income visibility and steady revenues. The new master lease agreement post Starhill Gallary's redevelopment at end-2021 will provide full occupancy for SGREIT's Malaysia properties upon redevelopment. Due to expire in June 2019, the new proposed master leases will further extend the WALE for its properties in Malaysia by 19.5 years and 9.0 years for Starhill Gallery and Lot 10 Mall respectively. The other major anchor tenant leases at Myer Centre Adelaide and David Jones in Perth have either annual or periodic rent reviews which could form a medium-term boost to earnings.

Future-proofing of Starhill Gallary. SGREIT will undertake a two-year asset enhancement initiative to refresh and reposition the ageing mall, which will cost an estimated RM175m. During AEI, the Sponsor will also provide a rent rebate of approximately six months' rent p.a. (or RM26m a year), which will help to mitigate disruption in earnings as the asset undergoes transformation. Competition within the mid- to high-end retail in Kuala Lumpur is likely to intensify, with retail supply within a 10-km radius from Starhill Gallery and Lot 10 increasing by approximately 31% over a five-year period to 27m sqft in 2023. Not only will the redevelopment allow Starhill Gallery to reposition and maintain competitive within its precinct, the new rents from the renewed master lease is estimated to be 1.5% higher, coupled with in-built periodic rental escalations (every three years).

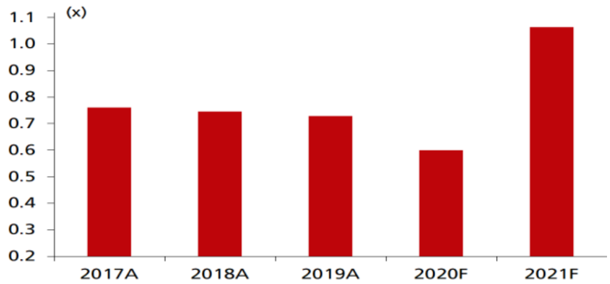
Net Property Income and Margins (%)



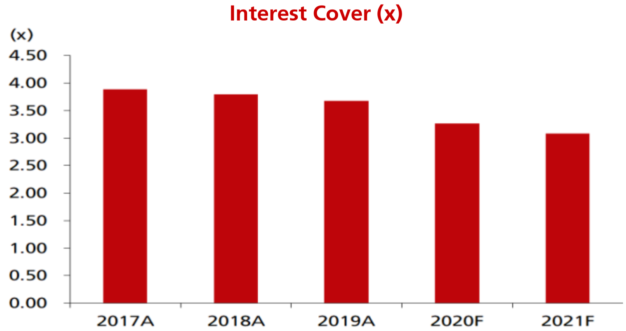
Net Property Income and Margins (%)



Distribution Paid / Net Operating CF



Interest Cover (x)



Source: Company, DBS Bank

Balance Sheet:

Future acquisitions to be partly funded via equity. Gearing is expected to remain stable at around 36% post its asset enhancement initiative for Starhill Gallery, within the manager's comfortable gearing level. This presents the REIT with acquisition capacity to acquire opportunistically when the right opportunity comes along.

Low debt renewal in FY19. Weighted debt tenure is c.2.9 years (as at 31 December 2019) at an average all-in interest cost of 3.3%. With c.90% of debt hedged into fixed rates and minimal debt expiring in FY20, we see limited impact of interest rates on the REIT.

Share Price Drivers:

Turnaround signs from Wisma Atria. Operational metrics have been soft at Wisma Atria, with potential upside in passing rents following a recent outperformance in tenant sales figures (double-digit y-o-y growth).

Extracting value from development in Singapore and Australia. The manager has several AEI opportunities to reposition its assets in Singapore and Australia. SGREIT has undertaken AEI works in Central Plaza, Perth, renovating the shop façade to incorporate anchor tenants, as well as converting some of the upper floors from office and storage into retail use. Other potential development/AEI opportunities include activating 116,000 sqft of vacant retail space on the fourth and fifth floors of Myer Centre, Adelaide, as well as developing the area between Wisma Atria and Ngee Ann City, where the REIT has unutilised gross floor area of c.100,000 sqft. Capital gains, should divestment of Japanese and China assets be executed, could be used to buffer dividend payouts in the future.

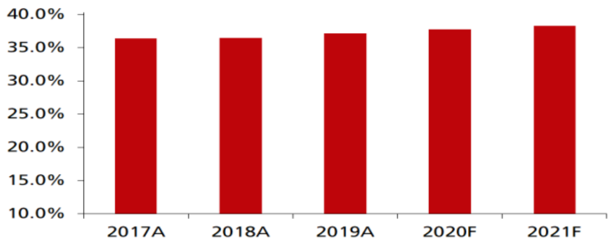
Key Risks:

Fall in tourist expenditure. A fall in tourist arrivals and receipts in the face of a WHO global emergency declaration could be detrimental to SGREIT's Singapore retail assets.

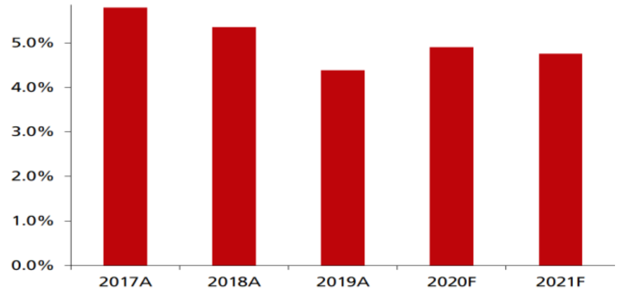
Company Background

Starhill Global REIT (SGREIT) is a real estate investment trust that invests in income-producing upscale retail and/or office assets in the Asia Pacific region. In Singapore, it owns portions of Ngee Ann City and Wisma Atria. It also owns assets in China, Japan, Malaysia and Australia.

Aggregate Leverage (%)

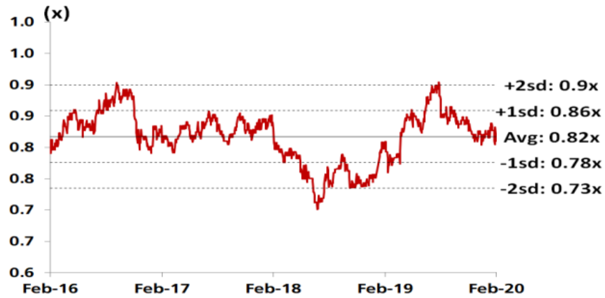


ROE (%)



Distribution Yield (%)

PB Band (x)



Source: Company, DBS Bank

Income Statement (S$m)

FY Jun	2017A	2018A	2019A	2020F	2021F
Gross revenue	216	209	206	212	213
Property expenses	(49.5)	(46.6)	(46.8)	(54.3)	(55.9)
Net Property Income	**167**	**162**	**159**	**157**	**157**
Other Operating expenses	(19.8)	(20.2)	(20.5)	(21.5)	(21.7)
Other Non Opg (Exp)/Inc	6.01	5.75	(11.8)	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(37.8)	(37.4)	(37.7)	(41.5)	(43.8)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Net Income	**115**	**110**	**89.4**	**94.2**	**91.2**
Tax	1.27	(3.4)	(3.5)	0.32	0.31
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Income After Tax	**117**	**107**	**85.9**	**94.6**	**91.5**
Total Return	100	84.2	65.6	94.6	91.5
Non-tax deductible Items	10.2	18.9	35.7	6.99	8.26
Net Inc available for Dist.	110	103	101	102	99.8
Growth & Ratio					
Revenue Gth (%)	(1.5)	(3.5)	(1.3)	2.6	0.5
N Property Inc Gth (%)	(2.0)	(2.8)	(1.7)	(1.3)	(0.4)
Net Inc Gth (%)	35.7	(8.3)	(19.7)	10.1	(3.2)
Dist. Payout Ratio (%)	97.2	96.2	96.4	96.0	98.0
Net Prop Inc Margins (%)	77.1	77.7	77.3	74.3	73.7
Net Income Margins (%)	53.9	51.2	41.7	44.7	43.0
Dist to revenue (%)	51.0	49.4	49.1	48.0	46.9
Managers & Trustee's fees	9.1	9.7	10.0	10.2	10.2
ROAE (%)	5.8	5.3	4.4	4.9	4.8
ROA (%)	3.6	3.3	2.7	3.0	2.8
ROCE (%)	4.6	4.3	4.3	4.4	4.3
Int. Cover (x)	3.9	3.8	3.7	3.3	3.1

Source: Company, DBS Bank

S$11m downward adjustment to 20F forecast due to lower occupancies in Singapore offices, and lower contributions from Starhill Gallery

Quarterly / Interim Income Statement (S$m)

FY Jun	2Q2019	3Q2019	4Q2019	1Q2020	2Q2020
Gross revenue	51.0	51.3	51.9	48.0	48.7
Property expenses	(11.5)	(11.7)	(12.0)	(11.1)	(11.6)
Net Property Income	39.5	39.6	39.9	36.9	37.2
Other Operating expenses	(5.0)	(5.0)	(5.5)	(4.8)	(5.3)
Other Non Opg (Exp)/Inc	(5.2)	(1.7)	(4.2)	(0.5)	0.0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(9.6)	(9.4)	(9.5)	(9.7)	(9.7)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Net Income	**19.7**	**23.5**	**20.6**	**22.0**	**22.1**
Tax	(0.9)	(0.9)	(0.8)	(0.7)	(0.7)
Minority Interest	0.0	0.0	0.0	0.0	0.0
Net Income after Tax	**18.9**	**22.5**	**19.8**	**21.3**	**21.4**
Total Return	0.0	0.0	0.0	0.0	0.0
Non-tax deductible Items	6.30	2.50	25.4	4.00	3.72
Net Inc available for Dist.	24.6	24.0	24.0	24.7	24.7
Growth & Ratio					
Revenue Gth (%)	(2)	0	1	(7)	2
N Property Inc Gth (%)	(2)	0	1	(8)	1
Net Inc Gth (%)	(24)	20	(12)	8	0
Net Prop Inc Margin (%)	77.4	77.2	77.0	76.9	76.3
Dist. Payout Ratio (%)	98.0	95.8	96.3	97.4	98.2

Balance Sheet (S$m)

FY Jun	2017A	2018A	2019A	2020F	2021F
Investment Properties	3,136	3,118	3,065	3,097	3,129
Other LT Assets	0.10	2.01	0.03	0.03	0.03
Cash & ST Invts	76.6	66.7	72.9	136	128
Inventory	0.0	0.0	0.0	0.0	0.0
Debtors	6.34	4.19	3.85	8.98	9.02
Other Current Assets	0.09	0.24	0.30	0.30	0.30
Total Assets	**3,219**	**3,192**	**3,142**	**3,242**	**3,267**
ST Debt	406	63.4	128	158	188
Creditor	38.8	38.6	32.5	106	106
Other Current Liab	4.12	2.21	3.18	3.18	3.18
LT Debt	728	1,067	1,004	1,004	1,004
Other LT Liabilities	32.9	30.0	44.1	44.1	44.1
Unit holders' funds	2,009	1,990	1,930	1,927	1,921
Minority Interests	0.0	0.0	0.0	0.0	0.0
Total Funds & Liabilities	**3,219**	**3,192**	**3,142**	**3,242**	**3,267**
Non-Cash Wkg. Capital	(36.5)	(36.4)	(31.5)	(99.7)	(100)
Net Cash/(Debt)	(1,058)	(1,064)	(1,059)	(1,026)	(1,064)
Ratio					
Current Ratio (x)	0.2	0.7	0.5	0.5	0.5
Quick Ratio (x)	0.2	0.7	0.5	0.5	0.5
Aggregate Leverage (%)	36.4	36.4	37.1	37.7	38.3
Z-Score (X)	0.9	0.9	0.9	0.9	0.9

Development costs of c.S$30m per year over 20F and 21F for Starhill Gallery's redevelopment

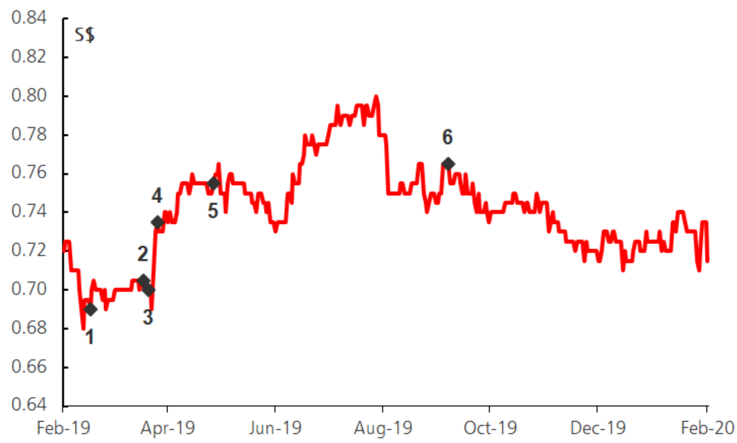
Source: Company, DBS Bank

Cash Flow Statement (S$m)

FY Jun	2017A	2018A	2019A	2020F	2021F
Pre-Tax Income	115	110	89.4	94.2	91.2
Dep. & Amort.	0.36	0.0	0.0	0.0	0.0
Tax Paid	(2.4)	(3.4)	(3.5)	0.32	0.31
Associates &JV Inc/(Loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	27.9	29.0	48.1	68.2	0.44
Other Operating CF	0.0	0.0	0.0	0.0	0.0
Net Operating CF	141	136	134	163	92.0
Net Invt in Properties	(4.1)	(6.6)	(6.7)	(32.1)	(32.1)
Other Invts (net)	(0.1)	0.0	0.0	0.0	0.0
Invts in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc. & JVs	0.0	0.0	0.0	0.0	0.0
Other Investing CF	1.09	0.0	0.0	0.0	0.0
Net Investing CF	(3.1)	(6.6)	(6.7)	(32.1)	(32.1)
Distribution Paid	(107)	(101)	(97.5)	(97.5)	(97.8)
Chg in Gross Debt	7.89	1.21	(22.0)	30.0	30.0
New units issued	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(38.5)	(39.1)	0.0	0.0	0.0
Net Financing CF	(138)	(139)	(120)	(67.5)	(67.8)
Currency Adjustments	(0.5)	(0.1)	(1.5)	0.0	0.0
Chg in Cash	(0.4)	(9.9)	6.22	63.1	(7.9)
Operating CFPS (S cts)	5.19	4.90	3.94	4.33	4.18
Free CFPS (S cts)	6.28	5.93	5.83	5.98	2.73

Source: Company, DBS Bank

Target Price & Ratings History



***Note**: Share price and Target price are adjusted for corporate actions.*

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	18 Feb 19	0.69	0.75	BUY
2:	20 Mar 19	0.71	0.75	BUY
3:	23 Mar 19	0.70	0.75	BUY
4:	28 Mar 19	0.74	0.75	BUY
5:	29 Apr 19	0.76	0.80	BUY
6:	09 Sep 19	0.77	0.80	BUY

Source: DBS Bank

Analyst: Singapore Research Team

Derek TAN

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:
STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)
BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

Completed Date: 4 Feb 2020 08:30:29 (SGT)
Dissemination Date: 4 Feb 2020 08:34:18 (SGT)

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