Singapore Company Guide

LendLease Global Commercial REIT

Version 1 | Bloomberg: LREIT SP | Reuters: LEND.SI **Refer to important disclosures at the end of this report**

DBS Group Research . Equity 11 Feb 2020

BUY

Last Traded Price (10 Feb 2020): S$0.905 (**STI :** 3,163.15)
Price Target 12-mth: S$1.05 (16% upside)

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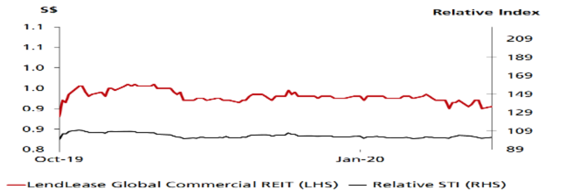
What's New

- DPU of 1.29 Scts for the quarter beats IPO forecast; in line with our estimates.
- 313@somerset could see an additional 1,008 sqm of GFA following an increase in plot ratio from 4.9+ to 5.6
- Low risk of non-renewal given a high tenant retention rate of 92.5%
- An acquisition, which we believe to be stakes in JEM or Parkway Parade, could happen earlier than expected

Price Relative



Forecasts and Valuation

FY Jun (S$m)	2021F	2022F	2023F
Gross Revenue	89.2	91.6	92.8
Net Property Inc	66.6	68.5	69.4
Total Return	46.6	48.3	49.1
Distribution Inc	63.8	63.7	64.6
EPU (S cts)	3.92	4.01	4.06
EPU Gth (%)	2	2	1
DPU (S cts)	5.39	5.33	5.38
DPU Gth (%)	3	(1)	1
NAV per shr (S cts)	80.4	79.6	78.9
PE (X)	23.1	22.6	22.3
Distribution Yield (%)	6.0	5.9	5.9
P/NAV (x)	1.1	1.1	1.1
Aggregate Leverage (%)	34.5	34.6	34.6
ROAE (%)	4.9	5.0	5.1
Other Broker Recs:	B: 2	S: 0	H: 0

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

313@somerset in a landlords' market

BUY, TP of S$1.05. Lendlease Global Commercial REIT (LLCGR)'s first set of results exceeded IPO forecasts. We remain positive on the dominant characteristics of both 313@somerset and Sky Complex. While Orchard retail malls had been in troubled waters recently given the coronavirus outbreak, 313@somerset remains resilient as it diversified away from the reliance on tourist receipts. With just 25 leases remaining across the portfolio, representing 3% of portfolio NLA and a high retention ratio, we remain confident of its ability to churn resilient cashflows in the medium term.

Potential for another 1,008 sqm of GFA at 313@somerset. After the latest Master Plan review, the permissible plot ratio for 313@somerset had been increased from 4.9+ to 5.6, translating into another 1,008 sqm of gross floor area to be potentially deployed. With existing tenants vying for expansion within 313@somerset, and high tenant retention ratio of 92.5%, we believe this provides an option for tenants to expand and grow at the mall. While no concrete plans had been shared, this extra GFA could come in the form of conversion of the sixth floor car park into commercial space, and act as a medium-term catalyst for LLGCR.

An acquisition could be on the horizon. The manager remains on the lookout for acquisition possibilities with metrics including the following: (i) stabilised assets with >80% occupancy, (ii) minimal AEI needed in the future, and (iii) value accretive to the REIT. We believe that the real surprise will come from the Sponsor's stake in JEM or Parkway Parade which are both dominant suburban malls that will anchor the REIT's longer-term earnings resilience and diversify away its earnings reliance on 313@somerset in the longer term.

Valuation:

Our TP remains at S$1.05 as our growth forecasts remain largely unchanged, and pricing in an acquisition will provide upside to our current TP.

Key Risks to Our View:

Key risks to our view include country risks in Singapore and Italy, tenant concentration risk, changes in withholding tax laws in Italy, foreign exchange risks and interest rate risks.

At A Glance

Issued Capital (m shrs)	1,168
Mkt. Cap (Sm/USm)	1,057 / 761
Major Shareholders (%)	
Lendlease SReit	24.3
OCBC	10.9
Temasek Holdings	5.0
Free Float (%)	54.8
3m Avg. Daily Val (US$m)	1.8

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

WHAT'S NEW

(+) DPU of 1.29 Scts for the quarter beats IPO forecast; in line with our estimates.

- LLGCR reported gross revenue and net property income for the quarter of S$21.4m and S$16.2m, outperforming IPO forecast by 1.0% and 3.2% respectively. DPU of 1.29 Scts exceeded forecast by 3.1% but is in line with our estimates.
- Better-than-expected top-line performance was mainly contributed by higher rents from 313@somerset, while lower property operating expenses flowed through to the bottom line.
- The portfolio maintained high committed occupancy of 99.8% and WALE at 10.1 years by NLA, supported by healthy leasing momentum at 313@somerset and the stability of Sky Complex asset which is under an extended lease term until 2032.
- Growth momentum will continue to be underpinned by rental escalations from 313@somerset and Sky Complex. Approximately 60% of leases at 313@somerset have built-in escalations of 3% per annum while rental escalation at Sky Complex is tied to 75% of the ISTAT consumer price index variation.

(+) Potential for another 1,008 sqm of GFA at 313@somerset

- The permissible plot ratio for 313@somerset had been increased from 4.9+ to 5.6 in the latest Master Plan review. This will translate into another 1,008 sqm of gross floor area to be potentially deployed.
- While no concrete plans had been laid out, we understand that key considerations would include the expansion plans of current tenants, potential operational disruptions and cost factors.
- One option would be the conversion of the sixth floor car park into commercial space.

(+) 313@somerset's operations holding strong; ongoing tenant remix

- Several new concepts introduced to 313@somerset included a home grown fashion brand and several F&B tenants to draw shopper footfall. Leases renewed in the past quarter were at a positive 0.5% rental reversion.
- There is an additional 11% of its GRI to be renewed in the 2HFY20, which we anticipate the manager to continue to actively manage the portfolio tenant mix in order to continue to the evolving retail landscape and changing consumer preferences.
- Given the historical tenant retention rate of c.93% at 313@somerset, we do not see potential non-renewals as a risk to the mall's current high occupancy.

(+) Financial metrics remain healthy; interest rate and exchange rate risk substantially lowered

- LLGCR's gearing ratio stood at 34.9% for the quarter on a debt maturity of 3.6 years.
- Weighted average running cost of debt is at a low 0.86% per annum, with almost 100% of debt on a fixed rate.
- Euro-denominated income from Sky Complex is also hedged until end FY2021.
- This substantially lowers most of LLGCR's interest rate and exchange rate risks for at least FY20 and FY21.

(+) Acquisitions; targeting to grow the portfolio

- The manager remains on the lookout for acquisition possibilities with metrics including the following:(i) stabilised with >80% occupancy, (ii) minimal AEI needed in the future, and (iii) value accretive to the REIT.
- In our view, while investors remain on the lookout for the potential injection of Paya Labar Quarters (PLQ) in Singapore in phases (office towers; followed by retail) into LLCGR, we believe that the real surprise will come from the Sponsor's stake in JEM or Parkway Parade (or if possible the entire property subject to fund investors' agreement). If successful, we believe that these dominant suburban malls will anchor the REIT's longer-term earnings resilience and diversify away its earnings reliance on 313@somerset.
- We have not priced in any acquisitions in our estimates.

Quarterly / Interim Income Statement (S$m)

FY Jun	2Q20	IPO Forecast	Variance % chg
Gross revenue	21.4	21.2	1.0
Property expenses	(5.2)	(5.5)	(5.3)
Net Property Income	16.2	15.7	3.2
Other Operating expenses	(0.5)	(0.4)	n.m
Other Non Opg (Exp)/Inc	0.1	-	n.m
Management Fees	(2.0)	(1.9)	(3.4)
Net Interest (Exp)/Inc	(2.5)	(2.7)	(9.2)
Exceptional Gain/(Loss)	(44.0)	(48.2)	9.2
Net Income	(32.7)	(37.6)	(13.1)
Tax	-	(0.0)	-
Minority Interest	-	-	-
Net Income after Tax	(32.7)	(37.6)	(13.2)
Total Return	(32.7)	(37.6)	(13.2)
Non-tax deductible Items	47.7	52.3	(8.8)
Net Inc available for Dist.	15.0	14.7	2.4
Ratio (%)			
Net Prop Inc Margin	75.6%	74.0%	
Dist. Payout Ratio	100.0%	100.0%	

Source of all data: Company, DBS Bank

CRITICAL DATA POINTS TO WATCH

Critical Factors

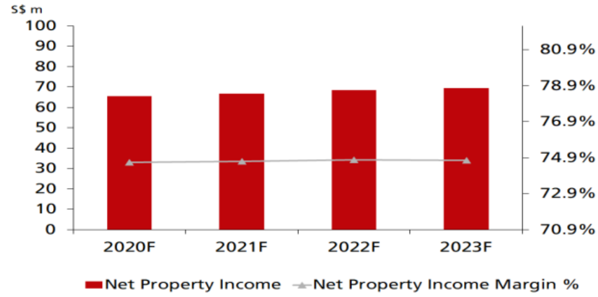
An initial portfolio that is predominantly in Singapore. LLGCR offers an opportunity to invest in a diversified portfolio of stabilised income-producing real estate assets that cater primarily to retail and/or office purposes. While the REIT holds a global investment mandate, its initial portfolio comprises 100% ownership of a 99-year leasehold interest in 313@somerset, a retail property located in prime Orchard Road, Singapore and full ownership of a freehold interest in Sky Complex, which comprises three commercial office buildings located in Milan, Italy. The total appraised valuation of the initial portfolio is c.S$1.4bn as of June 2019, anchored by Singapore (c.71.5% of value) and Italy (c.28.5% of value).

Lease structure is a balance between stability and growth. LLCGR offers investors a visible earnings stream backed by a long weighted average lease expiry (WALE) of 4.9 years by gross rental income (GRI) and 10.4 years by net lettable area (NLA). This is anchored by a long lease at Sky Complex where the sole tenant (blue chip tenant) at SKY Italia has another c.12.9 years to go on its lease. In Singapore, 313@somerset is projected to deliver steady growth given ongoing tenant retention and remixing strategies. As at June 2019, 92.8% of the portfolio's leases by GRI had step-up structures in the base rent over the term of the lease, of which The Sky Complex, which contributes 28.9% of total GRI, has rental escalation that is pegged to 75% of ISTAT's index variation

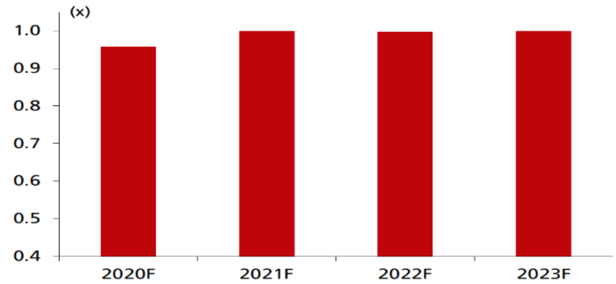
Backed by established Sponsor with a proven global reach. LLGCR's sponsor, Lendlease Corporation Limited, is part of the Lendlease Group, and has a long track record of successfully managing and operating commercial assets globally. The Lendlease group has A$32.5bn worth of assets under management globally. In Singapore, the Lendlease Group is managing some of the highly successful and iconic shopping malls including 313@somerset, Parkway Parade, Jem and Paya Lebar Quarter (PLQ) which was officially launched in October last year.

Additional GFA at 313@somerset. The reversion of plot ratio from 4.9+ to 5.6 according to URA's draft Master Plan 2019 could translate into an additional 1,008 GFA to be deployed at 313@somerset, and act as a medium-term catalyst for LLGCR. The Manager is currently reviewing potential plans to deploy the additional plot ratio, taking into account expansion plans of current tenants, potential operational disruptions and cost considerations. One option would be the conversion of the sixth floor car park into commercial space.

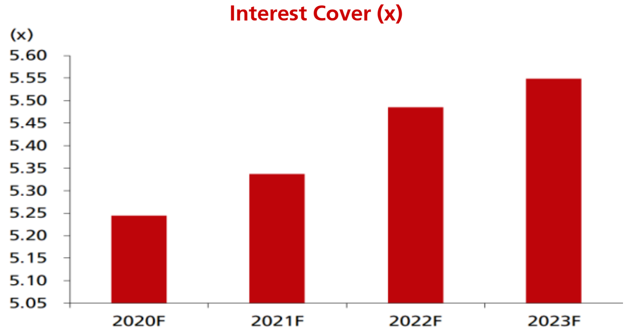
Net Property Income and Margins (%)



Distribution Paid / Net Operating CF



Interest Cover (x)



Source: Company, DBS Bank

Balance Sheet:
LLGCR's gearing ratio stood at c.35% as at end-2019, well within MAS's 45% gearing limit. Debt headroom stands at c.S$280m based on our estimates and a 45% target gearing, and could be deployed for future acquisitions.

Share Price Drivers:
Rejuvenation of Orchard Road. The Singapore government has plans to rejuvenate the Orchard Road precinct to further enhance the vibrancy of the area. This could potentially result in increased foot traffic and retail spending in Orchard, benefitting LLGCR's 313@somerset property coupled with potential upside in plot ratio.

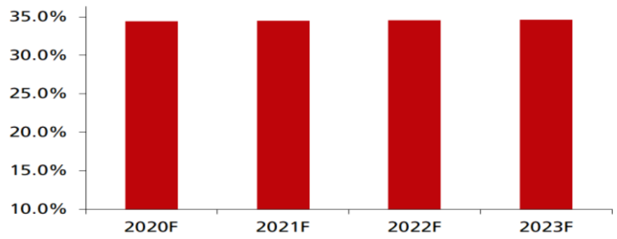
Additional GFA at 313@somerset. The reversion of plot ratio from 4.9+ to 5.6 according to URA's draft Master Plan 2019 could translate into an additional 1,008 GFA to be deployed at 313@somerset, and act as a medium-term catalyst for LLGCR.

Visible acquisition pipeline. Sponsor, Lendlease Group, has a A$100bn global development pipeline and properties, which includes A$35.2bn held under funds. In Singapore, the Lendlease Group manages highly successful and iconic shopping malls including 313@somerset, Parkway Parade, and Jem and more recently Paya Lebar Quarter (PLQ) which was launched in 3Q19.
(i) Parkway Parade – Sponsor owns 6.1% stake via Parkway Parade Partnership Limited.
(ii) JEM - Sponsor owns 20.1% stake via Lendlease Asian Retail Investment Fund 3.
(iii) Paya Lebar Quarter - Sponsor directly owns a 30.0% interest in the development

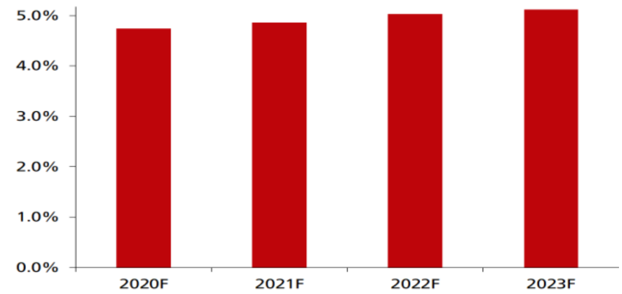
Key Risks:
Concentration risk. Despite LLGCR's initial portfolio being diversified across two countries and various sectors, there is a tight concentration on Sky Italia (single tenant), which contributed c.28.9% to revenues in June 2019. Therefore, a downturn in either key markets of Singapore and Italy could have a disproportionately large impact on the REIT's earnings.

Company Background
Lendlease Global Commercial REIT ("LLGCR") was listed on 2 October as a real estate investment trust with a principal objective to own in-producing real estate across the globe. The initial portfolio will comprise of full ownership stakes in two assets, retail mall 313@somerset (Singapore) and office asset, Sky Complex (Italy)..

Aggregate Leverage (%)



ROE (%)



Source: Company, DBS Bank

Balance Sheet (S$m)

FY Jun	2021F	2022F	2023F
Investment Properties	1,405	1,406	1,407
Other LT Assets	22.4	22.4	22.4
Cash & ST Invts	37.1	37.3	37.3
Inventory	0.0	0.0	0.0
Debtors	9.05	9.05	9.05
Other Current Assets	0.70	0.70	0.70
Total Assets	1,474	1,475	1,477
ST Debt	0.0	0.0	0.0
Creditor	5.95	6.10	6.19
Other Current Liab	0.0	0.0	0.0
LT Debt	509	510	511
Other LT Liabilities	0.0	0.0	0.0
Unit holders' funds	959	959	959
Minority Interests	0.0	0.0	0.0
Total Funds & Liabilities	1,474	1,475	1,477
Non-Cash Wkg. Capital	3.81	3.65	3.57
Net Cash/(Debt)	(472)	(473)	(474)
Ratio			
Current Ratio (x)	7.9	7.7	7.6
Quick Ratio (x)	7.9	7.7	7.6
Aggregate Leverage (%)	34.5	34.6	34.6

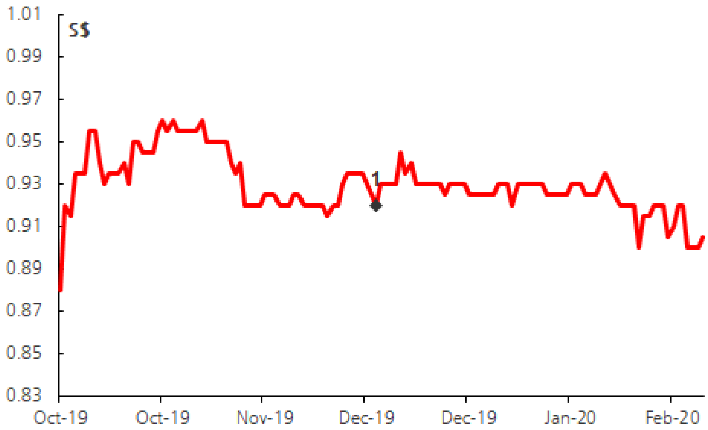
Source: Company, DBS Bank

Cash Flow Statement (S$m)

FY Jun	2021F	2022F	2023F
Pre-Tax Income	46.6	48.3	49.1
Dep. & Amort.	0.0	0.0	0.0
Tax Paid	0.0	0.0	0.0
Associates &JV Inc/(Loss)	0.0	0.0	0.0
Chg in Wkg.Cap.	0.10	0.16	0.08
Other Operating CF	17.2	15.4	15.4
Net Operating CF	**63.9**	**63.8**	**64.6**
Net Invt in Properties	(1.3)	(1.3)	(1.3)
Other Invts (net)	0.0	0.0	0.0
Invts in Assoc. & JV	0.0	0.0	0.0
Div from Assoc. & JVs	0.0	0.0	0.0
Other Investing CF	0.0	0.0	0.0
Net Investing CF	**(1.3)**	**(1.3)**	**(1.3)**
Distribution Paid	(63.8)	(63.7)	(64.6)
Chg in Gross Debt	1.26	1.30	1.32
New units issued	0.0	0.0	0.0
Other Financing CF	0.0	0.0	0.0
Net Financing CF	**(62.6)**	**(62.4)**	**(63.2)**
Currency Adjustments	0.0	0.0	0.0
Chg in Cash	0.10	0.16	0.08
Operating CFPS (S cts)	5.37	5.29	5.33
Free CFPS (S cts)	5.27	5.19	5.23

Source: Company, DBS Bank

Target Price & Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	05 Dec 19	0.92	1.05	BUY

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

Source: DBS Bank

Analyst: Singapore Research Team
Derek TAN

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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*

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