Singapore Company Update

LendLease Global Commercial REIT

Bloomberg: LREIT SP | Reuters: LEND.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

17 Sep 2020

BUY

Last Traded Price (16 Sep 2020): S$0.670 (**STI :** 2,505.15)
Price Target 12-mth: S$0.90 (34% upside) (Prev S$0.85)

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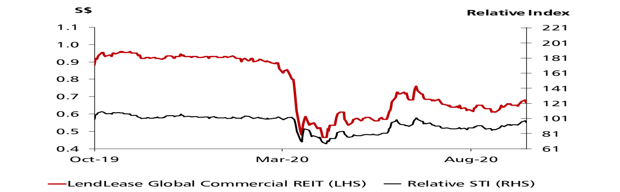
What's New

- Grange Road carpark redevelopment to extend LREIT's footprint to c.330k sqft within Somerset
- Acquisition of a stake in JEM overlooked at current valuations
- Rental disparity gap against Orchard peers may catch up with 313@Somserset's growing dominance
- Maintain BUY, TP S$0.90

Price Relative



Forecasts and Valuation

FY Jun(S$m)	2020F*	2021F	2022F
Gross Revenue	55.5	86.9	92.6
Net Property Inc	40.3	64.8	68.9
Total Return	(8.6)	44.0	48.1
Distribution Inc	35.7	61.0	63.6
EPU (S cts)	0.97	3.70	3.99
EPU Gth (%)	nm	281	8
DPU (S cts)	3.03	5.15	5.33
DPU Gth (%)	nm	70	3
NAV per shr (S cts)	83.8	83.1	82.3
PE (X)	69.1	18.1	16.8
Distribution Yield (%)	4.5	7.7	7.9
P/NAV (x)	0.8	0.8	0.8
Aggregate Leverage (%)	34.0	34.6	34.9
ROAE (%)	1.2	4.4	4.8
Distn. Inc Chng (%):	(37)	(2)	0
Consensus DPU (S cts):	4.0	4.8	5.0
Other Broker Recs:	B: 3	S: 0	H: 0

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.
** 2020F: 2 Oct 2019 (Listing Date) to 30 Jun 2020*

Brain Box
(Our NEW Pilot Research Platform) is available to Institutional Investors on Demand. Please contact your DBSV Institutional Sales contact for a demonstration.

Lotus flower in bloom

Investment Thesis

Undervalued Gem. We like Lendlease Global Commercial REIT (LREIT) for its compelling valuation of 0.78x P/NAV (retail peer average of 0.94x P/NAV), yield of 7.7%, anchored by resilient earnings.

Rocking to a new beat at 313@Somerset. We see more upside from the repositioning 313@Somerset's tenant mix in view of its enlarged footprint to c.330k sqft and shopper base following the launch of Grange Road carpark redevelopment in 2Q22. With projected returns of 18% from the redevelopment, we see DPU growing by 3% CAGR in FY21-22.

Acquisitions overlooked at current valuations. We believe that LREIT's first acquisition, which could be a stake in quality suburban mall JEM, may be just around the corner. Likely to be debt funded, the yield accretion will further boost the REIT's DPU profile. Higher DPU growth rates will be a catalyst for a share price re-rating.

Valuation:

Maintain BUY, TP S$ 0.90. Our discounted cash flow valuation factors in (i) 2.0% risk free rate, (ii) 1.0 beta, (iii) 6.31% WACC, and (iv) 2.0% terminal growth to derive a target price of S$0.90.

Where we differ:

Structured to weather storms. 313@Somerset continues to show resiliency with high tenant retention of >90% maintained, while churning a surprise value appreciation amid Covid-19. Sky Complex lease remains rock-solid with a 12-year triple net master lease expiring in 2032.

Key Risks to Our View:

Key risks to our view include the threat of a second wave of COVID-19 in Singapore.

At A Glance

Issued Capital (m shrs)	1,172
Mkt. Cap (Sm/USm)	785 / 578
Major Shareholders (%)	
Lendlease SREIT Pty Ltd	24.3
Temasek Holdings Pte Ltd	4.9
Blackrock Inc	4.9
Free Float (%)	65.9
3m Avg. Daily Val (US$m)	1.6
GIC Industry : Real Estate / Equity Real Estate Investment (REITs)	

DBS
Live more, Bank less

ed: JS/ sa: JC, PY, CS

WHAT'S NEW

Rocking to a new beat at 313@Somerset

Going from strength to strength, 313@Somerset to emerge as the dominant mall within Somerset area. Contrary to investors perception, we believe that the dominant positioning of 313@Somerset and stickiness of its leases are not well understood and yet to be reflected with the stock trading at P/NAV of 0.78x with a forward yield of 7.7%. The mall has proven to be able to hold up amid the Covid-19 storm. We had previously shortlisted 313@Somerset as one of the dominant malls in Singapore due to its (i) prime location along Orchard Road with direct connectivity to Somerset MRT Station, (ii) sizeable footprint of 288k sqft with expansion potential from the uplift in unutilised plot ratio and with additional GFA from Grange Road car park redevelopment, (iii) strong positioning targeting millennials, and (iv) superior tenant sales generation. These qualities could be the factors behind the mall's historically high tenant retention rate at over 90%. With short term catalysts of plot ratio maximisation and redevelopment of Grange Road carpark, 313@Somerset will likely go from strength to strength, and further anchor the mall's strong positioning within the Somerset precinct.

Occupancy steady within 313@Somerset despite the circuit breaker disruption; traffic and sales to head towards pre-COVID levels in coming quarter. Occupancy rate at 313@Somerset dipped 1.4 ppts q-o-q to 97.8% as at end June 2020, with a high tenant retention rate of 87% (c.93% in the previous quarter). We believe the slightly lower occupancy is transitionary in nature. Footfall has recovered to 40% of pre-COVID levels for the month of June with tenant sales recovery led by the electronics and food & beverage trades. Since July 2020, based on our site visits, we understand that traffic and sales are rising towards pre-COVID levels which is a positive sign for LREIT.

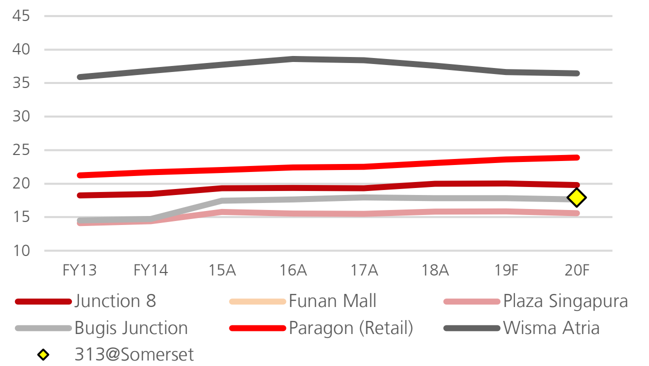
With tenants potentially doing better and starting to clock in more sales, we anticipate lower rental assistance will be required in the coming quarters, implying that the worst is most likely over for LREIT.

Eat play shop. The mall has a large percentage of tenant exposure to the food & beverage (39% of GRI) and fashion (29% of GRI) trade categories, but we note that there are currently only three entertainment tenants at the mall. The new plug-and-play event space at Grange Road carpark will be a step forward for 313@Somerset as a one stop entertainment hub with the inclusion of a cinema operator The Projector, and events promoter Live Nation. The repositioned mall will be able to better compete with neighbouring retail malls with cinema operators such as Orchard Cineleisure and Plaza Singapura, and extend the average shopper's length of stay per trip and dollars spent at the mall.

Valuation gain exceeded expectations. Valuations held up well at Sky Complex due to strong investment interest and solid cash flows from longstanding lease with quality tenant, Sky Italia. LREIT's quality assets were able to generate valuation gains for the latest quarter - 313@Somerset appreciated 0.5% from a year ago, as opposed to a c.3-4% decline in retail valuations reported by peers.

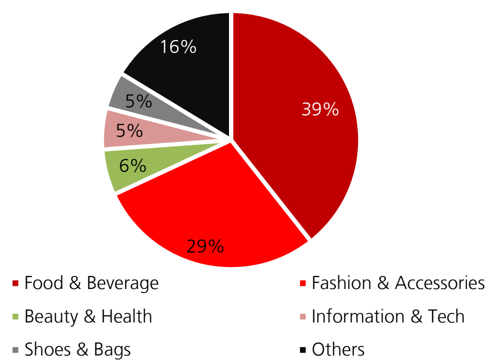
Rental disparity gap may play catch up in the medium term. Passing rent at 313@Somerset at c.S$18 psf pm continues to lag rents along prime Orchard Road which are in the range of c.S$25 - S$30 psf pm. We think that this rental disparity may see some compression in the medium to longer term given the mall's dominant characteristics. Moreover, we estimate tenant sales generation to match that of landmark malls in the precinct such as Paragon Mall.

Central mall estimated passing rents (S$ psf pm)



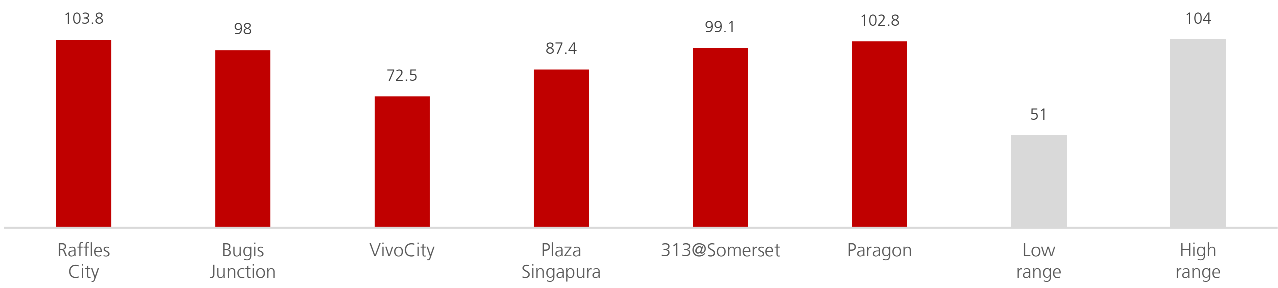
Source: Companies, DBS Bank

313@Somerset tenant breakdown by gross rental income



Source: Mediacorp, DBS Bank

Monthly tenant sales of dominant malls in the central region (S$ psf pm)



Source: Companies, DBS Bank

Leading the pack: Grange Road carpark redevelopment to augment 313@Somerset's leadership in Somerset area.

313@Somerset repositioning in anticipation of an enlarged shopper base. LREIT will be repositioning 313@Somerset's tenant mix given the enlarged shopper base following the launch of Grange Carpark redevelopment in 2Q22. Focus will remain on tenants that embrace omnichannel retail concepts with strong appeal to millennial shoppers. 313@Somerset has continued to deliver resilient performance during a trough, with a high tenant retention ratio of c.90% that provides occupancy stability and pockets of opportunities for LREIT to refresh its portfolio tenant mix.

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Grange Road car park to be transformed into a designed event space next to 313@somerset. LREIT won the tender to redevelop the neighbouring car park at Grange Road into a new 48,200 sqft multi-functional event space, as part of the 2019 URA Master Plan to rejuvenate the Orchard and Somerset areas. The tender stipulates a total tenancy term of not more than 10 years, or 3+3+3+1 years. We see this as a coup for the REIT as the car park's location next to 313@Someset is strategic for the Manager. This will effectively expand LREIT's footprint in the Somerset area to c.330k sqft, making it one of the largest malls in this submarket.

With visible frontage along Orchard Road and Grange Road, we see the expanded 313@Somerset pulling itself ahead of the other malls in the Somerset precinct with wider offerings to attract consumers to open their wallets, and experience new concepts. The proposed new concept replacing the carpark will include multiple dedicated event spaces, an independent cinema and local food & beverage attractions, targeted at millennials and tourists.

Working with Live Nation to infuse new life and exciting concepts to Somerset area. LREIT is collaborating with Live Nation, an American events promotor, to host concerts, films and events all year round. They have organized concerts and events for the likes of Taiwanese band Mayday and Korea's girl group TWICE. Cinema operator was revealed to be The Projector, a local independent cinema operator currently based in Golden Mile Tower. This will boost the variety of entertainment related tenants at 313@Somerset, which currently comprises of Fat Cat Arcade, HaveFun Family KTV and K Bowling Club.

Target completion in 2Q22; funded by internal working capital. Target completion date for the curated space will be 2Q22, with an estimated development cost of c.S$10m. The development cost will be funded via LREIT's working capital, spread across the development time frame. No additional debt will be expected to be undertaken for the project, with minimal impact on gearing (c.36% at 31 March 2020). While returns have not been provided, we believe that an ROI of at least in the double-digit level will most likely commensurate for the short tenure of 10 years in order for the investment to make sense. We have priced in a conservative ROI of 18% in our estimates, boosting our FY23 revenue by 3.2%.

Why will this concept work in our view. The redevelopment serves as another short to medium term catalyst for LREIT, in addition to the deployment of additional plot ratio at 313@Somerset. Various retail concepts had been previously tested at Grange Road Car Park, including the Flashbang street market, but we believe that the long tenure period will help anchor the area as a designated event space within the Orchard and Somerset precinct. Moreover, we envision that the lease terms for non-anchor tenants will be shorter for this event space to keep concepts fresh and may serve as an expansion or test bed option for new retail concepts for existing tenants at 313@Somerset, putting the mall in the heart of the retail ecosystem.

Potential acquisitions on the horizon. The acquisition of quality suburban malls JEM (Jurong) and possibly Parkway Parade (Marine Parade) or a partial stake in Paya Lebar Quarter (office component) may unfold in the near to medium term horizon. We believe that the acquisition of stakes in either property will likely utilise a greater proportion of debt given its high cost of equity. With a gearing headroom ranging from S$280m (based on 45% gearing) to S$450m (50% gearing), there is capacity for LREIT to drive higher growth in DPUs.

That said, a more sustained recovery in share price will increase the REIT's potential to tap the equity market in order to grow its AUM more meaningfully given its attractive pipeline of properties for acquisition

Maintain BUY, TP S$0.90. We have priced in LREIT's Grange Road carpark redevelopment at 18% ROI, to start contributing to topline income from 2H22, while rolling forward valuations into FY21. Our underlying earnings assumptions remain unchanged at both 313@Somerset and Sky Complex.

Company Background

Lendlease Global Commercial REIT ("LLGCR") was listed on 2 October as a real estate investment trust with the principal objective of owning in-producing real estate across the globe.

The initial portfolio will comprise full ownership stakes in two assets, namely retail mall 313@somerset (Singapore) and office asset Sky Complex (Italy).

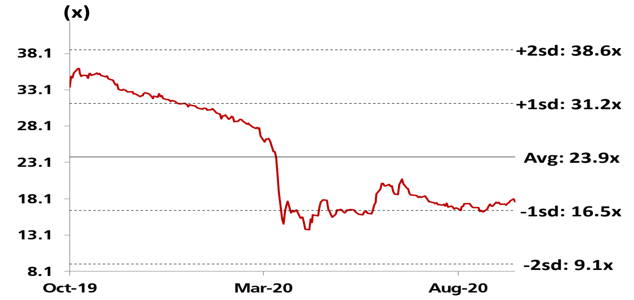
Quarterly / Interim Income Statement (S$m)

FY Jun	3Q2020	4Q2020	% chg qoq
Gross revenue	21.7	12.5	(42.5)
Property expenses	(5.1)	(5.0)	(2.2)
Net Property Income	16.6	7.51	(54.7)
Other Operating expenses	(0.4)	(0.6)	74.6
Other Non Opg (Exp)/Inc	0.0	0.0	-
Associates & JV Inc	0.0	0.0	-
Net Interest (Exp)/Inc	(2.2)	(2.2)	0.6
Exceptional Gain/(Loss)	(18.5)	27.2	-
Net Income	**(6.4)**	**30.4**	**-**
Tax	0.0	0.0	-
Minority Interest	0.0	0.0	-
Net Income after Tax	**(6.4)**	**30.4**	**(578.0)**
Total Return	(6.4)	30.4	nm
Non-tax deductible Items	21.3	(24.7)	(215.8)
Net Inc available for Dist.	15.0	5.69	(62.0)
Ratio (%)			
Net Prop Inc Margin	N/A	60.3	
Dist. Payout Ratio	100.0	100.0	

Source of all data: Company, DBS Bank

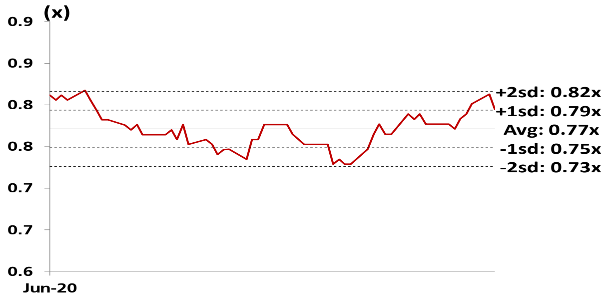
Historical PE and PB band

Forward PE band (x)



Source: Bloomberg Finance L.P., DBS Bank estimates

PB band (x)



Source: Bloomberg Finance L.P., DBS Bank estimates

Income Statement (S$m)

FY Jun	2020F	2021F	2022F
Gross revenue	55.5	86.9	92.6
Property expenses	(15.2)	(22.0)	(23.7)
Net Property Income	**40.3**	**64.8**	**68.9**
Other Operating expenses	(6.8)	(9.7)	(9.5)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0
Net Interest (Exp)/Inc	(6.7)	(11.2)	(11.3)
Exceptional Gain/(Loss)	(15.3)	0.0	0.0
Net Income	**11.5**	**44.0**	**48.1**
Tax	0.0	0.0	0.0
Minority Interest	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0
Net Income After Tax	**11.5**	**44.0**	**48.1**
Total Return	(8.6)	44.0	48.1
Non-tax deductible Items	44.3	17.1	15.5
Net Inc available for Dist.	35.7	61.0	63.6
Growth & Ratio			
Revenue Gth (%)	N/A	56.4	6.6
N Property Inc Gth (%)	nm	60.9	6.3
Net Inc Gth (%)	nm	282.8	9.4
Dist. Payout Ratio (%)	100.0	100.0	100.0
Net Prop Inc Margins (%)	72.5	74.6	74.4
Net Income Margins (%)	20.7	50.6	51.9
Dist to revenue (%)	64.2	70.3	68.7
Managers & Trustee's fees to sales %)	12.3	11.1	10.2
ROAE (%)	1.2	4.4	4.8
ROA (%)	0.7	2.8	3.1
ROCE (%)	2.3	3.8	4.1
Int. Cover (x)	5.0	4.9	5.3

Source: Company, DBS Bank

S$1.5m revenue estimated from Grange carpark redevelopment

Balance Sheet (S$m)

FY Jun	2020F	2021F	2022F
Investment Properties	1,443	1,449	1,455
Other LT Assets	14.0	14.0	14.0
Cash & ST Invts	83.7	67.6	68.0
Inventory	0.0	0.0	0.0
Debtors	10.6	10.6	10.6
Other Current Assets	4.66	4.66	4.66
Total Assets	1,555	1,546	1,552
ST Debt	0.0	0.0	0.0
Creditor	21.8	5.79	6.17
Other Current Liab	0.32	0.32	0.32
LT Debt	529	535	542
Other LT Liabilities	12.1	12.1	12.1
Unit holders' funds	992	992	992
Minority Interests	0.0	0.0	0.0
Total Funds & Liabilities	1,555	1,546	1,552
Non-Cash Wkg. Capital	(6.9)	9.11	8.72
Net Cash/(Debt)	(445)	(468)	(473)
Ratio			
Current Ratio (x)	4.5	13.6	12.8
Quick Ratio (x)	4.5	13.6	12.8
Aggregate Leverage (%)	34.0	34.6	34.9
Z-Score (X)	NA	NA	NA

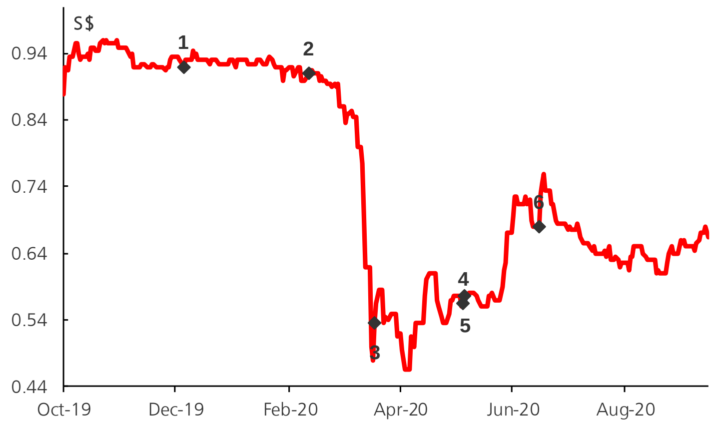
Source: Company, DBS Bank

Cash Flow Statement (S$m)

FY Jun	2020F	2021F	2022F
Pre-Tax Income	(8.6)	44.0	48.1
Dep. & Amort.	3.87	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.	(3.4)	(16.0)	0.38
Other Operating CF	44.5	17.1	15.5
Net Operating CF	**36.4**	**45.0**	**64.0**
Net Invt in Properties	(1,452)	(6.2)	(6.3)
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	0.53	0.0	0.0
Net Investing CF	**(1,451)**	**(6.2)**	**(6.3)**
Distribution Paid	(15.1)	(61.0)	(63.6)
Chg in Gross Debt	511	6.22	6.30
New units issued	1,002	0.0	0.0
Other Financing CF	0.0	0.0	0.0
Net Financing CF	**1,498**	**(54.8)**	**(57.3)**
Currency Adjustments	0.23	0.0	0.0
Chg in Cash	83.7	(16.0)	0.38
Operating CFPS (S cts)	3.36	5.13	5.28
Free CFPS (S cts)	(120)	3.26	4.79

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
2:	11 Feb 20	0.91	1.05	BUY
3:	18 Mar 20	0.54	0.94	BUY
4:	05 May 20	0.57	0.94	BUY
5:	06 May 20	0.58	0.85	BUY
6:	15 Jun 20	0.68	0.85	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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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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Dissemination Date: 17 Sep 2020 07:11:30 (SGT)

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