

Fraser's Logistics & Commercial Trust

Bloomberg: FLT SP | Reuters: FRAE.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

21 Jun 2021

BUY

Last Traded Price (18 Jun 2021): S\$1.40 (STI : 3,144.16)

Price Target 12-mth: S\$1.85 (32% upside)

Analyst

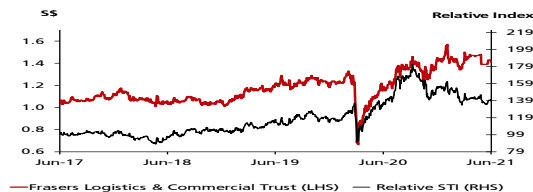
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What's New

- Recent acquisitions drive an acceleration in DPU growth into FY21-22F
- Potential c.20% upside to NAV if book values are marked to market
- Potential drop in P/NAV from 1.3x to 1.0x not priced in
- Maintain BUY with a TP of S\$1.85

Price Relative



Forecasts and Valuation

FY Sep (\$m)	2019A	2020A	2021F	2022F
Gross Revenue	241	332	447	481
Net Property Inc	199	270	362	390
Total Return	226	455	233	254
Distribution Inc	150	201	269	291
EPU (S cts)	4.59	3.52	6.69	6.86
EPU Gth (%)	(26)	(23)	90	3
DPU (S cts)	7.27	7.12	7.71	7.89
DPU Gth (%)	5	(2)	8	2
NAV per shr (S cts)	102	110	111	111
PE (X)	30.5	39.7	20.9	20.4
Distribution Yield (%)	5.2	5.1	5.5	5.6
P/NAV (X)	1.4	1.3	1.3	1.3
Aggregate Leverage (%)	33.2	38.9	39.2	39.2
ROAE (%)	4.9	4.0	5.9	6.2

Distn. Inc Chng (%): 2 (2)
 Consensus DPU (S cts): 7.80 8.00
 Other Broker Recs: B: 9 S: 0 H: 1

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

More expensive, yet more value for money

Investment Thesis

Cheapest large-cap logistics REIT in Singapore. With a TP of S\$1.85, FLCT's target yields are 4.2-4.3% for FY21F-FY22F, which is fair given its substantially freehold portfolio. In our view, there is room for further compression if we compare FLCT to its large-cap peers which are trading at target yields of 3.5-4.0%.

ROFR pipeline from Sponsor is worth more than S\$5.0bn. Since its merger with FCOT, the REIT has acquired more than S\$600m worth of assets from its Sponsor. Despite this, FLCT still has the largest ROFR pipeline valued at more than S\$5.0bn that could double its portfolio, a visibility like no other.

Robust DPU growth into FY21F. We project a robust 8% DPU growth in FY21F, driven by full-year contribution from its enlarged portfolio as well as subsequent acquisitions, with an additional 2% DPU growth in FY22F as it builds on its organic growth strategy.

Valuation:

Our DCF-based TP is maintained at S\$1.85. We have not assumed any further acquisitions in our projections.

Where we differ:

Exploring development projects. With a significantly larger portfolio (c.S\$6.8bn), FLCT has the capacity to undertake development projects or redevelopment of older assets that could drive upside to earnings in the longer term.

Key Risks to Our View:

Currency risk. As the Manager pays its distributions in SGD, the REIT is exposed to currency fluctuations in AUD, EUR and GBP. The Manager attempts to reduce foreign currency fluctuations by hedging distributions regularly.

At A Glance

Issued Capital (m shrs)	3,429
Mkt. Cap (S\$m/US\$m)	4,800 / 3,630
Major Shareholders (%)	
Fraser's Prop Ind Trust Hlds PI	20.6
PPGM Vermögensbeher BV	4.8
Free Float (%)	74.6
3m Avg. Daily Val (US\$m)	9.7
GIC Industry: Real Estate / Equity Real Estate Investment (REITs)	



Live more, Bank less

WHAT'S NEW

More expensive, yet more value for money

Tapping on the burgeoning e-commerce growth

Riding on the fast-growing e-commerce growth and demand for logistics properties, FLCT has recently announced the acquisition of a portfolio of six freehold properties in Germany, the UK and Netherlands. The S\$548.7m portfolio consists of five logistics assets, and one business park asset. The portfolio boasts a high occupancy rate of 97.4% and long WALE of 9.1 years. The five logistics assets have a 100% occupancy rate and are leased to major third-party logistics players and manufacturers. The business park asset in the UK is estimated to have an occupancy of c.90% currently but is supported by a 24-month rental guarantee from the vendor. This helps to address near-term fluctuations in its occupancy rates as several tenants go through lease renewals.

Maiden entry into the UK logistics sector

The acquisition of the two adjacent assets, Connexion (five logistics properties) and Blythe Valley Park (16 business park properties) marks FLCT's maiden entry into the UK logistics sector. It is also FLCT's first acquisition from a third party, demonstrating the REIT's ability to tap on its established network to source for accretive deals.

Connexion is 100% occupied with a very healthy WALE of 9.5 years, echoing the strong demand for logistics facilities in the new township near to Birmingham in the UK. We understand that Blythe Valley Park occupancy is likely to inch down to c.90% as two tenants are rationalising their space in the area. However, we are not too concerned

with this as there is a 24-month rental guarantee in place. Included in the business park project is a 3-hectare development site for future developments. Given the strong demand for logistics facilities in the precinct, we believe that the site will be likely developed into a logistics facility. As planning permissions have already been granted, we expect the development of the site to commence in the near future and generate more income for Blythe Valley Park.

Delivering on portfolio growth sooner than expected

In our earlier projections, we had assumed a S\$600m acquisition by the end of FY21 (FLCT's financial year-end is in September). As five of the six assets have recently been completed (one remaining asset in Netherlands will be completed soon), the acquisition came in approximately one quarter sooner than our projections. The purchase consideration of S\$548.7 is relatively in line with our projections, but the blended NPI yield of 5.2% is slightly lower than our forecasts. The tighter yields are a function of cap rates compressing significantly over the past year, and we will discuss further on how it may actually work in FLCT's favour.

With the acquisitions in the UK coming from a third party, FLCT's pipeline from the Sponsor remains intact and continues to be valued at more than S\$5.0bn. This ROFR pipeline provides FLCT with access to quality assets for its next leg of growth, especially as demand for logistics properties heats up.

Properties snapshot

	Hermes Mainz Facility	Hermes Bad Rappenau	BASF Facility	Hendi Facility	Blythe Valley Park	Connexion
Location	Germany	Germany	Germany	Netherlands	UK	UK
Asset Type	Logistics	Logistics	Logistics	Logistics	Business Park	Logistics
Year of Completion	2017	2017	2019	2021	2000 - 2020	2018
NLA (sqm)	13,148	13,125	20,579	15,263	41,679	19,543
Appraised Value (\$'m)	88.9	66.1	48.5	34.2	251.2	73.4
Estimated Yield	4.4%	4.4%	4.4%	4.4%	6.3%	4.3%
Occupancy	100.0%	100.0%	100.0%	100.0%	95.7%	100.0%
WALE	11.50	11.00	8.60	20.00	7.50	10.40
Major Tenants	Hermes Germany GmbH	Hermes Germany GmbH	BASF SE	Hendi B.V.	Lounge Underwear, Gymshark, Regus	Gymshark, Lounge Underwear, Hofer Powertrain

Source: Fraser's Logistics & Commercial Trust, DBS Bank Estimates

Acquisition will be DPU and NAV accretive

On a blended basis, the acquisition portfolio has a NPI yield of c.5.2%. The tighter-than-expected yields were mainly due to the lower yields for the logistics assets which we estimate to be between 4.3% and 4.5%. Despite this, the acquisition will be c.0.5% accretive to our FY21 DPU estimates as we have revised our projections to include one quarter of income contribution.

Based on our revised projections, FLCT currently trades at FY21 and FY22 forward yields of 5.4% and 5.6% respectively. As compared to its other large-cap industrial REIT peers, FLCT offers a very attractive yield currently. Within the logistics REIT space, FLCT offers a forward yield that is c.120bps higher than its closest peer, MLT.

The acquisition will be funded by a mix of debt and equity (40:60), and this follows FLCT's oversubscribed private placement that raised S\$335.8m. The private placement was done at a P/NAV multiple of 1.23x, or a c.23% premium to FLCT's NAV. The 2.5% discount on the purchase price of the portfolio, together with the equity fund raising that was done at a premium, led to the 0.9% accretion to NAV.

Tightening of cap rates to boost value of logistics properties

Over the past year, demand for well-located modern logistics facilities has been heating up. With the e-commerce sector still booming, we believe that competition for logistics facilities will likely drive further compressions in cap rates and rental rates. This will benefit landlords like FLCT whose portfolio cap rates have not reflected this tightening.

In the Australian and European markets where FLCT has the largest exposure to industrial and logistics properties, recent transactions have been driving down yields significantly. In April 2021, GIC and ESR Cayman jointly acquired a A\$3.8bn portfolio of industrial and logistics properties in Australia at an estimated yield of 4.5%. In Europe, record-low vacancy rates and the unprecedented spike in transaction values have driven prime yields for logistics properties down significantly. In the key markets of Germany, the UK and Netherlands, prime yields are currently between 3.0% and 4.0%.

Room for FLCT's NAV to increase by more than 20%

Based on our estimates, the average yield of FLCT's enlarged Logistics and Industrial (L&I) portfolio is c.5.6%. Yields of the individual markets range from 4.3-6.2%, the

lowest-yielding market being the UK while Australia is the highest. With cap rates for industrial and logistics assets compressing faster than the other asset classes, we expect FLCT to report a tightening in yields for its L&I portfolio come September 2021. Evident from recent market transactions, as well as this latest transaction, yields are now tighter than FLCT's L&I portfolio by as much as 170bps.

FLCT's portfolio yields vs. recent transactions

	Estimated yields of FLCT's L&I portfolio	Recent transactions	Yield compression
Australia	6.2%	4.5%	170 bps
Germany	5.0%	4.4%	60 bps
UK	4.3%	4.3%	-
Netherlands	5.3%	4.4%	90 bps
Average	5.6%	4.4%	80 bps

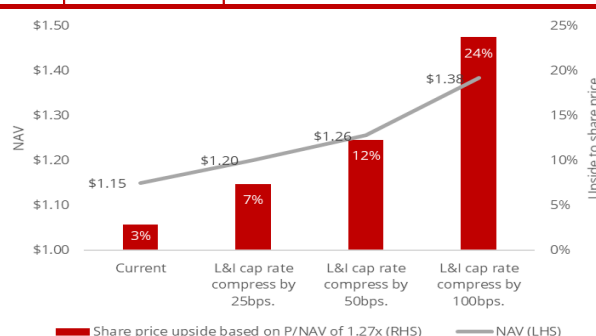
Source: DBS Bank Estimates

We looked at how various scenarios of cap rate compressions between 25-100bps will affect FLCT's portfolio. In our scenarios, we only assumed cap rate compressions for the L&I portfolio while maintaining the yields of FLCT's office and business park portfolio. Based on our analysis, FLCT's NAV could increase by up to c.20% if yields of its L&I portfolio compress by 100bps. This implies a NAV of c.\$1.38, as compared to its current NAV of \$1.15.

Higher NAV as a share price catalyst

Next, we analysed the potential upside to FLCT's share price assuming it trades at its historical average P/NAV multiple. For our comparison, we used FLCT's average 5-year and 2-year P/NAV multiples of 1.20x and 1.27x respectively. Assuming the maximum cap rate compression of 100bps, there could be a c.24% upside to FLCT's share price.

24% upside to share price



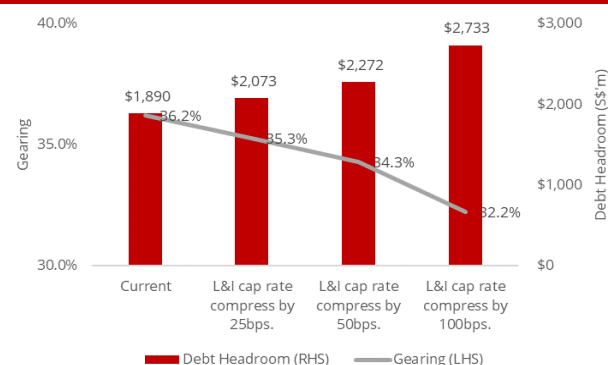
Source: DBS Bank Estimates

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Enlarged debt headroom with higher NAV

An increase in NAV would also help to lower FLCT's gearing from 36.2% currently. With a compression in its L&I yield by 100bps, gearing would fall to 32.2%. This would provide FLCT with ample debt headroom of more than S\$2.7bn. As interest rates in Australia and Europe remain at record-low levels, the debt headroom will be absolutely beneficial for FLCT to embark on more debt-funded acquisitions. Even if cap rates continue to compress, the low borrowing costs would help FLCT to make accretive acquisitions. Although unlikely, the enlarged debt headroom suggests that FLCT will be able to pursue more than half of its Sponsor's ROFR pipeline by relying entirely on debt.

Debt headroom of more than S\$2.7bn



Source: DBS Bank Estimates

Sensitivity analysis

	Current	Compress by 25bps	Compress by 50bps	Compress by 100bps
NPI Yield (L&I only)	5.6%	5.4%	5.1%	4.6%
Portfolio AUM (\$'m)	6,847	7,033	7,235	7,704
NAV	\$1.15	\$1.20	\$1.26	\$1.38
P/NAV	1.2	1.2	1.1	1.0
Share price upside based on 5-year historical P/NAV	-	1%	6%	17%
Share price upside based on 2-year historical P/NAV	3%	7%	12%	24%
Gearing	36.2%	35.2%	34.3%	32.2%
Debt Headroom (\$'m)	1,890	2,076	2,278	2,747

Source: DBS Bank Estimates

Our thoughts

In our previous projections, we had assumed that S\$600m worth of acquisitions by the end of FY21. As FLCT continues to benefit from record-low interest rates and a sizeable ROFR pipeline from its Sponsor, the projected growth came in ahead of our expectations by approximately one quarter. This is the basis of our upward revision in FY21's earnings and the 0.5% increase in DPU estimates.

FLCT's maiden third-party acquisition demonstrates the REIT's ability to tap on its established network and presence in the European market. This leaves them with more than S\$5.0bn worth of Sponsor pipeline that FLCT can look to tap on for its next leg of growth.

As capital continues to pour into stable income-producing logistics properties, NPI yields of this acquisition was slightly lower than anticipated. However, this also presents a revaluation gain opportunity for FLCT's L&I portfolio during its financial year-end in September 2021. We believe that this potential growth in NAV has not been factored into its share price. The higher NAV could lead to a c.24% upside to share price and a significantly enlarged debt headroom of more than S\$2.7bn. As such, we are maintaining our **BUY** recommendation with a TP of **S\$1.85**.

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Company Background

FLCT offers investors the opportunity to invest in prime logistics and commercial properties strategically located within five major developed markets. FLCT currently manages 103 properties across Australia, Singapore, Germany, the UK, and the Netherlands, totaling c.2.6m sqm. The appraised value of FLCT's portfolio was S\$6.8bn as of 31 May 2021.

Income Statement (\$m)

FY Sep	2018A	2019A	2020A	2021F	2022F
Gross revenue	196	241	332	447	481
Property expenses	(34.0)	(41.4)	(62.2)	(85.0)	(91.6)
Net Property Income	162	199	270	362	390
Other Operating expenses	(17.1)	(22.7)	(33.4)	(44.6)	(47.0)
Other Non Opg (Exp)/Inc	(4.1)	(1.2)	(0.8)	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(22.5)	(26.7)	(40.9)	(54.2)	(56.5)
Exceptional Gain/(Loss)	23.4	1.65	1.42	0.0	0.0
Net Income	142	150	196	263	286
Tax	(34.4)	(44.5)	(71.7)	(28.9)	(31.5)
Minority Interest	(0.9)	(2.3)	(4.0)	(1.2)	(1.2)
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Income After Tax	106	104	120	233	254
Total Return	179	226	455	233	254
Non-tax deductible Items	(62.4)	(80.0)	(254)	35.7	37.8
Net Inc available for Dist.	118	150	201	269	291
Growth & Ratio					
Revenue Gth (%)	20.1	23.0	37.9	34.6	7.7
N Property Inc Gth (%)	20.8	23.2	35.3	34.1	7.7
Net Inc Gth (%)	23.2	(2.5)	16.2	93.4	8.9
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	100.0
Net Prop Inc Margins (%)	82.6	82.8	81.3	81.0	81.0
Net Income Margins (%)	54.3	43.0	36.3	52.1	52.7
Dist to revenue (%)	60.4	62.2	60.6	60.1	60.5
Managers & Trustee's fees	8.7	9.4	10.1	10.0	9.8
ROAE (%)	6.5	4.9	4.0	5.9	6.2
ROA (%)	4.2	3.0	2.3	3.3	3.5
ROCE (%)	4.4	3.7	2.9	4.1	4.3
Int. Cover (x)	6.4	6.6	5.8	5.9	6.1

Increase in revenues due mainly to full-year contribution from recent acquisitions.

Source: Company, DBS Bank

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Balance Sheet (\$m)

FY Sep	2018A	2019A	2020A	2021F	2022F
Investment Properties	2,978	3,554	6,352	6,904	6,909
Other LT Assets	1.13	2.12	34.2	34.2	34.2
Cash & ST Invt	106	128	169	119	118
Inventory	0.0	0.0	0.0	0.0	0.0
Debtors	9.97	16.2	30.9	23.2	25.0
Other Current Assets	0.0	18.0	149	149	149
Total Assets	3,095	3,719	6,735	7,229	7,235
ST Debt	220	206	677	677	677
Creditor	40.4	53.2	86.7	23.2	25.0
Other Current Liab	6.89	11.5	21.0	28.9	31.5
LT Debt	845	1,030	1,944	2,158	2,158
Other LT Liabilities	39.7	75.6	199	199	199
Unit holders' funds	1,924	2,314	3,770	4,105	4,105
Minority Interests	18.9	28.9	36.2	37.5	38.7
Total Funds & Liabilities	3,095	3,719	6,735	7,229	7,235
Non-Cash Wkg. Capital	(37.3)	(30.5)	71.9	120	117
Net Cash/(Debt)	(959)	(1,107)	(2,452)	(2,716)	(2,717)
Ratio					
Current Ratio (x)	0.4	0.6	0.4	0.4	0.4
Quick Ratio (x)	0.4	0.5	0.3	0.2	0.2
Aggregate Leverage (%)	34.4	33.2	38.9	39.2	39.2
Z-Score (X)	2.0	2.0	1.7	1.7	1.7

Increase in debt to fund recent acquisitions.

Source: Company, DBS Bank

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Cash Flow Statement (\$m)

FY Sep	2018A	2019A	2020A	2021F	2022F
Pre-Tax Income	142	150	196	263	286
Dep. & Amort.	0.0	0.0	0.0	0.0	0.0
Tax Paid	(11.4)	(15.9)	(18.4)	(18.3)	(28.9)
Associates & JV Inc/(Loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	(5.3)	(14.2)	(28.6)	(58.4)	0.0
Other Operating CF	(1.0)	37.1	65.7	35.7	37.8
Net Operating CF	124	158	215	222	295
Net Invnt in Properties	(490)	23.8	(4.6)	(552)	(5.0)
Other Invnts (net)	0.0	(13.3)	(448)	0.0	0.0
Invnts 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	0.0	(5.9)	(0.9)	0.0	0.0
Net Investing CF	(490)	4.54	(453)	(552)	(5.0)
Distribution Paid	(91.9)	(125)	(153)	(269)	(291)
Chg in Gross Debt	61.4	43.4	482	214	0.0
New units issued	470	274	0.0	335	0.0
Other Financing CF	(26.6)	(28.9)	(39.1)	0.0	0.0
Net Financing CF	412	164	290	280	(291)
Currency Adjustments	3.58	1.23	1.02	0.0	0.0
Chg in Cash	49.6	327	52.9	(49.5)	(1.2)
Operating CFPS (\$ cts)	7.58	7.60	7.13	8.05	7.99
Free CFPS (\$ cts)	(21.5)	8.03	6.15	(9.5)	7.85

Source: Company, DBS Bank

Target Price & Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	05 Aug 20	1.36	1.60	BUY
2:	25 Sep 20	1.42	1.85	BUY
3:	09 Nov 20	1.34	1.85	BUY
4:	06 May 21	1.47	1.85	BUY

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

Source: DBS Bank

Analyst: Dale LAI

Derek TAN

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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: 21 Jun 2021 06:43:34 (SGT)

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Sources for all charts and tables are DBS Bank unless otherwise specified.

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