Singapore Industry Focus

Singapore REITs

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DBS Group Research . Equity

21 Jul 2021

How to position as Phase 2 returns

- Reversing back to Phase 2 (Heightened Alert) douses optimism in the re-opening trade
- Sputtering recovery in retail S-REITs; re-enter at lower levels
- Safe harbours in Industrial and Healthcare for certainty of income growth
- Office REITs offer good value

Back to a painful "square one"; re-enter at lower levels. The sharp rise in the number of community cases arising from recent clusters involving KTV and the Jurong fishery Port have forced the authorities' hand, as Singapore heads back to Phase 2 (Heightened Alert) with group sizes back down to 2 and the prohibition of dine-ins. The new curbs, starting 22 July 2021 will last about a month. This will be a painful pill for most, especially the retail and CBD focused S-REITs. In fact, a re-opening in late 3Q21 may be also be more gradual than anticipated, meaning that 2021 earnings momentum will likely be slower. A look back into the historical playbook (in 2H20, 2Q21) revealed that investors tend to position out of the retail, office, and hospitality sectors in the immediate term in anticipation of negative earnings surprises. That said, we noted that any downside had proven to be short lived and in fact opened an opportunity.

Sputtering re-opening for the retail subsector to cast a long shadow. Retailers and retail S-REITs have seen a number of "false dawns" in 2021 and now face the prospects of needing to provide extended help to their tenants given the expected drop in traffic and sales at the malls as traffic is likely to thin out. We have not priced in rebates at this moment but anticipate a 6-10% cut in earnings estimates post the upcoming results, especially for retail focused names. Among them, we believe that suburban focused names like FCT will be most resilient.

Safe harbours: Prime Office, Industrial and Healthcare. While the extended work-from-home (WFH) arrangement may result in more modest leasing momentum in 2H21, we remain watchful on shadow space risk in the sector. That said, office REITs like KREIT and MCT are better positioned to attract new economy tech firms. We see most clarity in earnings trajectory within selected industrial S-REITs (MLT, MINT, ALLT, AIMS) and highlight PLife for its resilient earnings profile.

STI : 3,111.20

Analyst

Derek TAN +65 6682 3716
derektan@dbs.com

Rachel TAN +65 6682 3713
racheltanlr@dbs.com

Dale LAI +65 66823715
dalelai@dbs.com

Geraldine WONG +65 6682 3719
geraldinew@dbs.com

STOCKS

	Price S$	Mkt Cap US$m	12-mth Target Price S$	Performance (%) 3 mth	12 mth	Rating
Mapletree Logistics Trust	2.10	6,597	2.35	6.1	2.9	BUY
Mapletree Industrial Trust	2.87	4,950	3.25	2.5	(2.4)	BUY
Mapletree Commercial Trust	2.12	5,162	2.25	0.0	10.4	BUY
Frasers Centrepoint Trust	2.42	3,015	3.00	(2.0)	4.3	BUY
Keppel REIT	1.18	3,177	1.40	(1.7)	9.3	BUY
Parkway Life REIT	4.79	2,125	5.75	16.8	43.8	BUY
ARA LOGOS Logistics Trust	0.89	940	0.85	19.6	48.7	BUY
AIMS APAC REIT	1.55	803	1.60	14.0	29.2	BUY

Source: DBS Bank, Bloomberg Finance L.P.
Closing price as of 19 Jul 2021

Legend:
MLT: Mapletree Logistics Trust
MCT: Mapletree Commercial Trust
MINT: Mapletree Industrial Trust
FCT: Frasers Centrepoint Trust
KREIT: Keppel REIT
PLife: Parkway Life REIT
ALLT: ARA LOGOS Logistics Trust
AIMS: Aims APAC REIT

"KO-ed by the KTV and Jurong KTV clusters"

In the wake of rising community cases from the KTV and Jurong Fishery Port clusters, the Multi-Ministerial Taskforce has decided to re-introduce community curbs that will effectively bring us back to Phase 2 (Heightened Alert). These curbs will last from 22 July' 2021 to 18 Aug 2021. Among the various measures, the curbs to dining-in is negative for Food & Beverage (F&B) outlets and will hit the retail S-REITs the most.

Measures to assist businesses impacted by the curbs will be unveiled by Ministry of Finance in a couple of days. Share price volatility expected within the "re-opening plays" and the retail focused S-REITs in the near term. A further dip is an opportunity to accumulate

Our thoughts

Spluttering re-opening at best; retailers and retail landlords to feel the brunt of the tighter curbs. The optimism that investors had on the re-opening theme is likely to be doused. The many "false starts" faced by the retailers and restauranters is a major setback to the growth momentum that many of us were looking for in 2H21. With restaurants now possibly facing up to 2 months of not having dine-in customers, we fear that some restaurants may be forced to throw in the towel.

In addition, in our previous reports, we had highlighted that dine-in customers are vital to a mall's traffic. Our experience back in Phase 2 (Heighted Alert) in May 2021-Jun 2021 has proven that despite the mall remaining open for business, the traffic tends to slow to a crawl especially when dine-ins are not allowed. Families which typically are bigger spenders will be staying home and thus we expect malls will be negatively impacted.

Retail landlords likely continue to support their tenants. While the government has provided some form of assistance to business (especially the SMEs) through rental assistance (of up to 2 weeks) for qualifying tenants and will likely do so in the coming month (18 July-Aug 2021), we feel that most of the assistance would have fallen onto the shoulders of landlords. This was especially seen in 2021 when landlords received lesser financial assistance (no property tax rebates etc) compared to circuit breaker (CB) days in 2020. We hope that some form of assistance to the landlords will be unveiled in a couple of days' time.

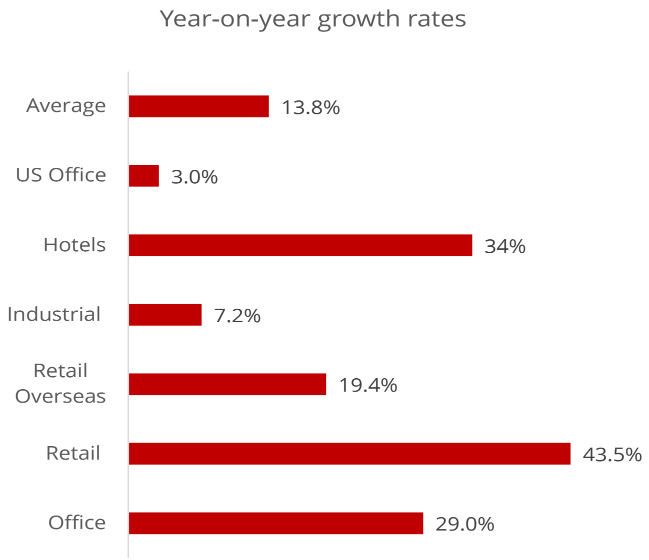
Retail S-REITs likely to face the most earnings risk. We anticipate that most retail landlords are likely to be reporting weaker than projected results for 2Q21 (due to rental assistance to tenants in 2Q21) and forward guidance will likely turn more cautious with a focus on further rental assistance to be disbursed for the upcoming month. In our previous report, we had highlighted that the landlords will likely be shouldering up to 2 weeks of rental assistance for Phase 2 (Heightened Alert) in May/June 2021, we now see rebates increasing to up to 4-6 weeks. This will effectively reduce our FY21F earnings by up to 10%.

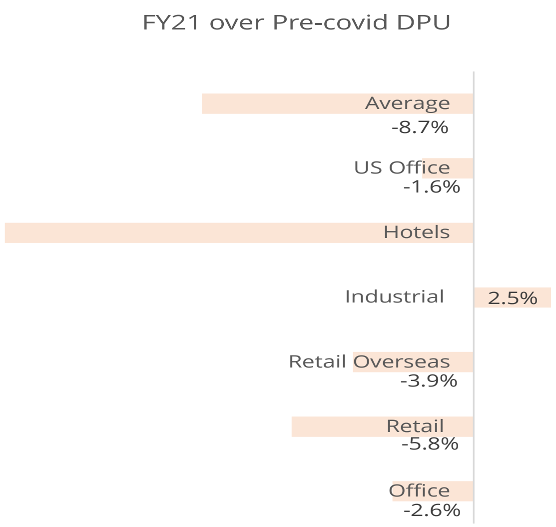
Summary of our views and impact on individual sectors

Sector	DBS Research View	Rising risk from Phase 2 (Heightened Alert)
Office	• Office sector is on a growth trajectory (CBD rents to show growth in 2021 on the back of a rebounding economy coupled with lack of new supply completions. • Rentals projected to rise by 3%-5% in 2021.	• Slowing rental rebound momentum in 2H21. • Possible more shadow space emerging or as firms pivot to co-working spaces if "work from home" is a default option for an extended period.
Retail Malls	• Focus on the dominant malls supported by a wide primary catchment with a preference for suburban. • Rentals and occupancy rates each projected to dip by 5% in 2021.	• Possible additional rental rebates not priced in by investors. • Occupancy risk if tenants decide to "throw in the towel"
Industrial	• Clearest growth trajectory as businesses likely to be most unaffected. • Warehouse and business parks to lead recovery.	• Downside to rental reversions if business sentiment turns down but most likely to remain stable.
Hotels	• RevPAR growth of 30%-45% in 2021. • Re-opening of Singapore borders to more countries to boost travel.	• RevPAR rebound likely delayed till 2022. • Support from government through extension of quarantine business at selected hotels.

Source: DBS Bank

Earnings projections and estimates





Source: DBS Bank

Where are possible drivers to earnings risk?

Retail: Most downside to earnings
We anticipate downside risk to our retail S-RETs growth rates and DPU projections. This comes on the back of possible extension of rental rebates to tenants with the economy moving back to Phase 2 (Heightened Alert).

Overseas retail S-REITs to lead the rebound, especially those with a China (North Asia) focus.

Hotels: More downside as borders remain closed.
Downside to our estimates as we have priced in a recovery in RevPAR in 2H21. Depending on the ability to contain the most recent community cases, staycation demand will likely be curbed. We expect DPUs to remain flattish y-o-y vs 2020 except for ARA US Hospitality Trust, which is likely to see a strong rebound.

Office: Limited downside for now.
Ongoing capital recycling activities for most landlords has resulted in optimization of portfolio returns and we expect acquisitions to drive DPU performance. We do not expect major downside to earnings.

US office names will likely see upside surprises on the back of acquisitions while 2H21 may see a turnaround in occupancy and rental outlook.

Industrial: Clearest visibility
We anticipate the industrial S-REITs to be safe harbours in the immediate term given the strong rebound in DPUs on the back of acquisitions while organic growth has remained positive.

Re-opening plays could be impacted this time round

Stocks may retreat near term. Markets have been positioning for a re-opening theme in recent months but we sense that the spike in the delta variant cases in the region (Malaysia, Thailand, Japan, Taiwan) may result in investors turning more cautious on the re-opening themes of retail and office in the immediate term.

We looked at the relative price performance of the various S-REIT subsectors and found that in 2020 / 2021, hotels and retail S-REITs saw the most downside risk whenever the economy move into a "new phase" of more community restrictions. This is due to community curbs having a more direct impact on earnings.

The share prices of retail-focused S-REITs are now on average up by 7.4% year to date (YTD-2021) which we attribute to the mainly the overseas focused S-REITs (especially focused on North Asia and China) which are seeing brighter operational prospects.

While the move back into Phase 2 (Heightened Alert) is seen to be negative to investor sentiment, we believe any potential correction would be short lived and urge investors to pick the strong names in the suburban retail space and selectively in Orchard. Among the retail S-REITs, our pick is Frasers Centrepoint Trust (FCT), given its exposure to the more resilient "essential tenant trades" while Lendlease Global REIT (LREIT) and Starhill Global Commercial REIT (SGREIT) may have an additional "indexation" catalyst that will drive valuations higher.

Share price performance by subsectors (through the COVID-19 pandemic)

Periods:	office	retail	hotel	industrial	health	reit
Year 2020						
Start of COVID-19 Pandemic to trough in 1Q20	-28.4%	-28.6%	-36.4%	-6.8%	17.0%	-17.5%
Phase 2 re-opening (2H20) – Start to trough	-15.0%	-14.6%	-13.1%	0.7%	16.4%	0.0%
Performance in 2020	-18.2%	-16.9%	-21.3%	-1.5%	14.8%	-8.0%
Year 2021						
Phase 2 (Heightened Alert): May-Jun'21 - Start to trough	-7.8%	-7.4%	-9.0%	-4.6%	-0.5%	-6.8%
Phase 2 (HA) trough to last close	5.9%	8.5%	2.6%	8.7%	14.9%	6.8%
Year-to-date	3.6%	7.4%	-4.6%	9.1%	23.8%	2.9%

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

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:
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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)
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**Share price appreciation + dividends*

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DBS Regional Research Offices

HONG KONG
DBS (Hong Kong) Ltd
Contact: Carol Wu
13th Floor One Island East,
18 Westlands Road,
Quarry Bay, Hong Kong
Tel: 852 3668 4181
Fax: 852 2521 1812
e-mail: dbsvhk@dbs.com

MALAYSIA
AllianceDBS Research Sdn Bhd
Contact: Wong Ming Tek
19th Floor, Menara Multi-Purpose,
Capital Square,
8 Jalan Munshi Abdullah 50100
Kuala Lumpur, Malaysia.
Tel.: 603 2604 3333
Fax: 603 2604 3921
e-mail: general@alliancedbs.com
Co. Regn No. 198401015984
(128540-U)

SINGAPORE
DBS Bank Ltd
Contact: Janice Chua
12 Marina Boulevard,
Marina Bay Financial Centre Tower 3
Singapore 018982
Tel: 65 6878 8888
e-mail: groupresearch@dbs.com
Company Regn. No. 196800306E

THAILAND
DBS Vickers Securities (Thailand) Co Ltd
Contact: Chanpen Sirithanarattanakul
989 Siam Piwat Tower Building,
9th, 14th-15th Floor
Rama 1 Road, Pathumwan,
Bangkok Thailand 10330
Tel. 66 2 857 7831
Fax: 66 2 658 1269
e-mail: research@th.dbs.com
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INDONESIA
PT DBS Vickers Sekuritas (Indonesia)
Contact: Maynard Priajaya Arif
DBS Bank Tower
Ciputra World 1, 32/F
Jl. Prof. Dr. Satrio Kav. 3-5
Jakarta 12940, Indonesia
Tel: 62 21 3003 4900
Fax: 6221 3003 4943
e-mail: indonesiaresearch@dbs.com