Asia Credit Research

OCBC Bank

Mapletree Logistics Trust: Credit Update

Monday, 16 October 2017

Still yielding

- **MLT has completed the acquisition of Mapletree Logistics Hub Tsing Yi in Hong Kong for SGD848mn from its Sponsor on 12 October 2017. This transaction was first announced in August 2017. The deal represents 15% of MLT's total assets as at 30 June 2017. The acquisition followed other developments since 1QFY2018 (1) Divestments of two properties in Singapore for SGD82.5mn (one in progress) (2) Divestment of two properties in Japan for SGD165mn and (3) Redemption of an existing perpetual at first call.**
- **We have reviewed the impact of the proposed transactions and funding structure and resume our coverage on MLT with a Neutral issuer profile. We expect MLT's credit profile to improve somewhat though in our view, the improvement is insufficient to move MLT's issuer profile to positive territory.**
- **Recommendation:** We hold the MLTSP 3.65%-PERP and MLTSP 4.18%-PERP on Overweight. We are recommending a switch from AREIT 4.75%-PERP with YTW of 2.50% to the MLTSP curve. The MLTSP 3.65%-PERP provides a spread pick-up of 100bps versus the AREIT 4.75%-PERP, which more than compensates for its longer call date of 2.5 years and a one-notch rating differential. The MLTSP 4.18%-PERP provides a spread pick-up of 70 bps, which more than compensates for the longer call date of 1.1 years and the one-notch rating differential. The issuer MLTSP is rated at NR/Baa1/NR while AREIT is rated at NR/A3/NR.

- **Background:** On 29 August 2017, MLT announced that it is proposing to acquire Mapletree Logistics Hub Tsing Yi, located in New Territories, Hong Kong ("HK Property") from its Sponsor. The total acquisition cost including fees and other expenses was SGD847.6mn (HKD4.9bn). We had placed MLT's issuer profile on review, pending fundraising outcomes and subsequently halted our coverage of MLT due to OCBC's engagement in other business activities. On 13 September 2017, unitholders' have approved the HK Property acquisition and since then, MLT had completed a series of fundraising exercises to satisfy the perpetual redemption and to acquire HK Property (completed on 12 October 2017). As of report date, the MLT 5.375%-PERP has also been called. We have factored in the impact of the acquisition and updated developments in our credit update.

  MLT is listed on the Singapore Stock Exchange ("SGX") with a market cap of SGD3.7bn as at 16 October 2017. MLT is an Asian-focused logistics REIT headquartered in Singapore. Investment properties totaled SGD5.5bn as at 30 June 2017. Post 30 June 2017, MLT had completed the divestment of two assets in Japan and one in Singapore. Another asset (namely 7 Tai Seng Drive), is in the process of being divested to the Sponsor and this proposed transaction is pending regulatory approval. On a pro forma basis, assuming all of the asset movements have been completed, we expect MLT's investment properties to grow by net 11% to SGD6.1bn. Sponsor is in turn 100%-owned by Temasek, and the rest of MLT's shareholding is dispersed mainly across institutional investors.

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Figure 1: MLT SGD Perpetuals

Issue	Maturity / First Call Date	Outstanding Amount (SGDm)	Ask Price	Ask YTC (%)	I-Spread	Bond Rating
MLTSP 4.18%-PERP	25 Nov 2021	250	103.65	3.22	155	NR/NR/NR
MLTSP 3.65%-PERP	28 March 2023	180	100.55	3.54	171	NR/NR/NR

Note: (1) Indicative prices as at 16 October 2017

- **HK Property will help MLT diversify away from Singapore:** The HK Property is located in Tsing Yi Road, New Territories, Hong Kong. The property is a 10-storey modern ramp-up warehouse with direct vehicular ramp access to each floor which was only completed in 2016. Approximately 79% of warehouses in Hong Kong are more than 20 years old and only 12% are less than ten years old. While the HK Property is located away from the core terminals in Kwai Chung, it has large, regular-shaped floor plates which allows for higher efficiency. The property has a remaining land leasehold period of about 46 years and occupancy is 100% committed. Three tenants, namely Ever Gain Company Limited (a logistics company), adidas (sports apparels) and Angliss (food products) make up 57% of gross revenue at the property. In 1QFY2018, revenue from Hong Kong made up 14.8% of total revenue, we estimate that the contribution from Hong Kong will rise to ~26%, behind Singapore. We expect Singapore to contribute about 30% of revenues (down from 37.5% in 1QFY2018) going forward. We see this geographical diversification as a small positive given expectations that the Singapore warehouse sub-segment will continue to be challenging over the next 12 months.

- **Fundraising exercises:** In total, MLT needed SGD1.2bn to pay for the HK Property acquisition and to redeem the MLT 5.375%-PERP (amount outstanding of SGD350mn). MLT launched an equity fundraising on 13 September 2017 to raise gross proceeds of SGD640mn. Of these, SGD353.5mn was raised by way of an equity private placement on 13 September 2017 and a further SGD286.5mn was raised via a non-renounceable preferential offering completed on 12 October 2017. A smaller "replacement perpetual" of SGD180mn was issued on 28 September 2017, whilst the remainder is funded by bank debt. Post the REIT's equity private placement, MLT's Sponsor holds 36% in MLT, falling from 39.5% immediately prior to the HK Property announcement.

- **Reduction in perpetuals and adjusted aggregate leverage kept in check:** Prior to the HK Property announcement, Moody's held MLT's credit rating at Baa1 with a Negative outlook. As at 30 June 2017, MLT's adjusted aggregate leverage (including 50% of perpetuals as debt) was 44%, nearing the 45% level which may trigger a credit rating downgrade. In our view, MLT had opted to use the opportunity to raise more straight equity and by doing so, helped reduce its leverage profile to levels more in line with the parameters of its Baa1 credit rating. As at 30 June 2017, total perpetual outstanding stood at ~SGD600mn (representing 11% of total capital). This would have declined to ~SGD430mn post-transaction and we expect perpetuals to make up 7% of total capital. In addition to a lower aggregate leverage which we estimate at 41%, we also expect coverage levels to improve to 5.7x on an EBITDA/Interest basis and 4.9x, including 50% of perpetual distribution as interest. As of report date, Moody's has lifted MLT's credit rating outlook to Stable.

- **Recommendation:** We expect MLT's credit profile to improve somewhat, though insufficient to move the needle to a positive issuer profile. As such, we are resuming our coverage of MLT with a **Neutral** issuer profile. We hold the MLTSP 3.65%-PERP and MLTSP 4.18%-PERP on Overweight and are recommending a switch from AREIT 4.75%-PERP with a YTW of 2.50% to the MLTSP curve.

We have considered the following:

A) A switch from the AREIT 4.75%-PERP to the MLTSP 3.65%-PERP allows a spread pick-up of 100bps, which more than compensates for the longer call date of 2.5 years on the MLT perp and a one-notch rating differential.
B) A switch into the MLTSP 4.18%-PERP allows a pick-up of 70 bps, which more than

compensates for the longer call date of 1.1 years and a one-notch rating differential.

C) Structurally, all perpetuals faces call risk (call risk fluctuates during the lift of perpetual based on the interest rate environment and issuer-specific events). Technicals for REIT perpetuals are constructive in the immediate-to-near term. In our view, the market has adopted a stance that both MLT and AREIT perpetuals would be called at their next call. We have assumed the same in our switch recommendation.

D) AREIT's weighted average cost of straight debt as at 30 June 2017 was 2.9% p.a while weighted average debt tenure was 3.1 years. While this is not strictly comparable to cost of funding in the fixed income market, it is worth highlighting that the AREIT 4.75%-PERP is trading at only YTW of 2.5%. The AREIT perp is 3.3 years away from its next call as at 30 June 2017.

E) MLT's weighted cost of debt as at 30 June 2017 of 2.3% p.a while weighted average debt tenure was 4.0 years. The REIT Manager had assumed a 2.75% p.a for new debt to be taken for the HK Property acquisition. There are no straight bonds at MLT and all senior debt is unsecured. While cost of bank debt is not strictly comparable to cost of funding in the fixed income market, we find the MLT 4.18%-PERP at a YTW of 3.2%, higher than cost of debt. The MLT 4.18%-PERP is 4.4 years away from its next call as at 30 June 2017.

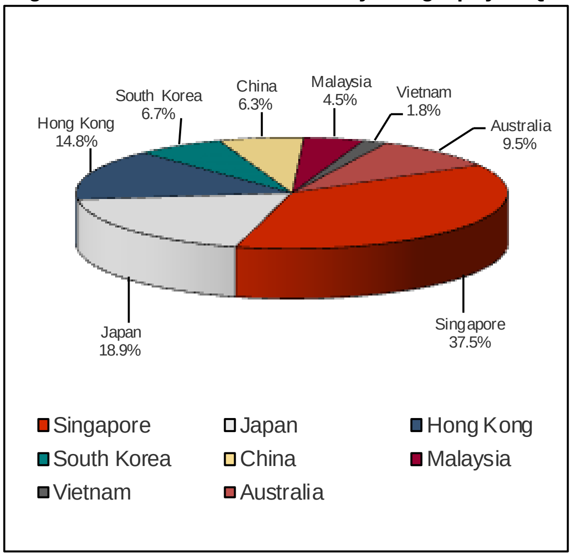
Mapletree Logistics Trust

Table 1: Summary Financials

Year Ended 31st March	FY2016	FY2017	1Q2018
Income Statement (SGD'mn)			
Revenue	349.9	373.1	95.8
EBITDA	255.9	274.3	71.0
EBIT	254.7	272.9	70.6
Gross interest expense	44.0	48.7	12.9
Profit Before Tax	235.4	252.8	49.3
Net profit	190.2	184.3	37.6
Balance Sheet (SGD'mn)			
Cash and bank deposits	93.3	92.6	95.8
Total assets	5,207.4	5,686.7	5,663.4
Gross debt	2,058.3	2,184.1	2,201.9
Net debt	1,965.0	2,091.5	2,106.1
Shareholders' equity	2,878.5	3,189.7	3,149.4
Total capitalization	4,936.8	5,373.8	5,351.3
Net capitalization	4,843.5	5,281.2	5,255.5
Cash Flow (SGD'mn)			
Funds from operations (FFO)	191.3	185.6	38.0
* CFO	231.0	266.9	58.9
Capex	0.0	0.0	0.0
Acquisitions	422.5	374.0	13.8
Disposals	33.2	14.1	0.0
Dividends	178.3	200.0	52.1
Free Cash Flow (FCF)	231.0	266.9	58.9
* FCF Adjusted	-336.7	-293.0	-7.0
Key Ratios			
EBITDA margin (%)	73.1	73.5	74.2
Net margin (%)	54.4	49.4	39.2
Gross debt to EBITDA (x)	8.0	8.0	7.7
Net debt to EBITDA (x)	7.7	7.6	7.4
Gross Debt to Equity (x)	0.72	0.68	0.70
Net Debt to Equity (x)	0.68	0.66	0.67
Gross debt/total capitalisation (%)	41.7	40.6	41.1
Net debt/net capitalisation (%)	40.6	39.6	40.1
Cash/current borrowings (x)	0.4	0.4	0.4
EBITDA/Total Interest (x)	5.8	5.6	5.5

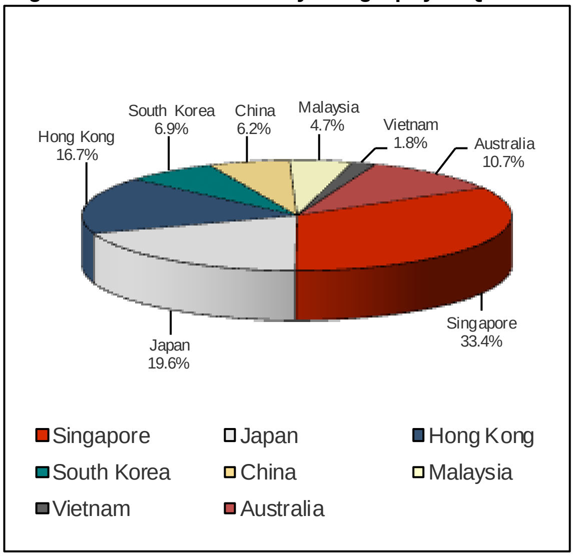
Source: Company, OCBC estimates

Figure 1: Revenue breakdown by Geography - 1Q2018



Source: Company

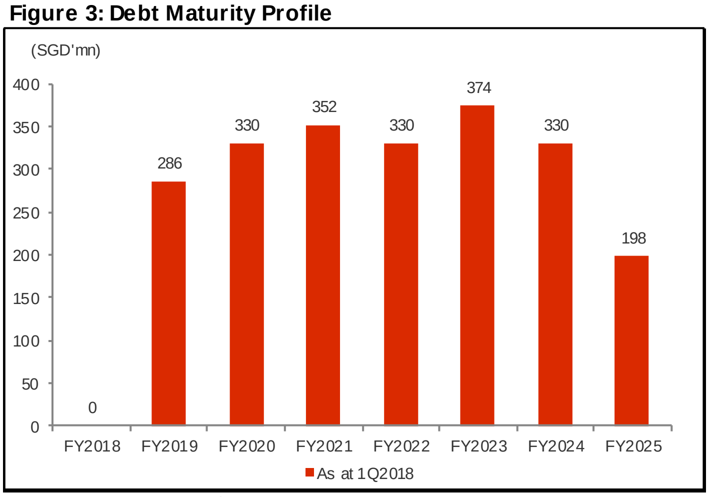
Figure 2: NPI breakdown by Geography - 1Q2018



Source: Company

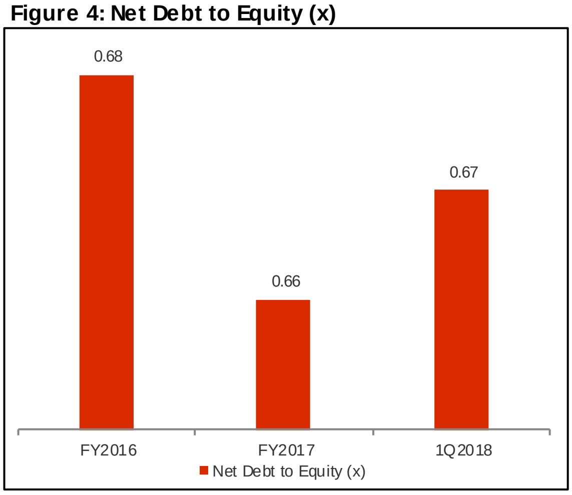
*FCF Adjusted = FCF - Acquisitions - Dividends + Disposals | *CFO before deducting interest expense*

Figure 3: Debt Maturity Profile



Source: Company, OCBC estimates

Figure 4: Net Debt to Equity (x)



Source: Company, OCBC estimates

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