Asia Credit Research

Earnings Review: Ascendas Hospitality Trust (“ASCHT”)

Issuer Profile: Neutral (4)

Ticker: **ASCHTS**

Background

Ascendas Hospitality Trust (“ASCHT”) is a hospitality trust which owns a portfolio of 11 hotels in Australia, China, Japan and Singapore. As of report date, 2 hotels in China are being divested while ASCHT is also in the midst of buying its first property in South Korea. ASCHT is a stapled group comprising Ascendas Hospitality Real Estate Investment Trust (“A-HREIT”) and Ascendas Hospitality Business Trust (“A-HBT”).

Ezien Hoo, CFA
+65 6722 2215
EzienHoo@ocbc.com

Recommendation

- Operating weakness in ASCHT’s Australian portfolio and on-going renovations had dragged financial performance for 4QFY2018 though ASCHT continues to post commendable credit metrics with aggregate leverage only 30.8% as at 31 March 2018 and EBITDA/Interest coverage of 5.3x.
- On 21 May 2018, ASCHT completed its maiden acquisition of a hotel in Dongdaemun, Seoul, South Korea for ~SGD100.7mn (proposed acquisition announced in April 2018). This comes on the back of Friday’s sale completion of two China hotels (both located in Beijing) which would help in managing the short term debt coming due of SGD155.7mn (proposed sale was announced in January 2018).
- We maintain ASCHT’s issuer profile at Neutral (4). A switch from ASCHTS 3.3% ’20s into ESR-REIT’s EREIT 3.95% ‘20s allow a spread pick up of 50 bps, which more than compensates for the 1.4 months longer tenor.

Relative Value:

Bond	Maturity/Call date	Aggregate leverage (%)	Ask Yield	Spread
ASCHTS 3.3% ‘20	07/04/2020	30.8	2.75%	71 bps
EREIT 3.95% ‘20	21/05/2020	30.0	3.24%	118 bps

Indicative prices as at 22 May 2018 Source: Bloomberg
Aggregate leverage based on latest available quarter

Key Considerations

- **Operating performance decline:** ASCHT announced its financial results for the quarter and financial year ended 31 March 2018 (“FY2018”). Gross revenue for the full year was stable at SGD203.3mn, driven by +0.7% y/y improvement in gross rental revenue which mitigated the slightly weaker food & beverage revenue (-0.1% y/y). Net property income though underperformed y/y (down 4.4%) due to a 3.2% rise in total property expenses. Cost inflation was broad based, although higher services and other taxes and staff costs which make up 39% of FY2018’s total property expenses were the main contributors. For the quarter, ASCHT saw gross revenue for continued operations (ie: excluding China which had been earmarked to be sold) decline 5.9% y/y to SGD49.7mn while net property income was down 9.0% y/y to SGD22.0mn. This was driven by performance decline in Australia and Japan while Singapore stayed flat. ASCHT has six hotels in Australia (one in Melbourne and Brisbane each and four across Sydney). The Australian portfolio saw revenue per available room (“RevPAR”) fall 3.1% y/y to AUD154 in 4QFY2017, despite average daily rates increasingly somewhat by 1.1%, occupancy fell to only 84.1% (from 87.7%). ASCHT’s Brisbane hotel was worst hit in our view, negatively affected by room oversupply and 20% decline in valuation while the hotel in Melbourne saw weaker convention and exhibition revenue. The weaker performance in the Japan property was driven by ongoing renovation, which in our view is temporary.

- **Fair value gains from investment properties drove bottom line growth:** In 4QFY2018, other trust income was SGD4.7mn, this relates to the look fee that was received by ASCHT as part of the sale of its China hotels. A further SGD22.0mn was recorded as net fair value gains from investment properties (1Q2017: SGD9.4mn was recorded). The largest gains in SGD terms was seen from the Pullman Sydney Hyde Park and Hotel Sunroute Ariake and Oakwood hotels which helped offset declines in (1) Pullman and Mercure Melbourne (2) Pullman and Mercure Brisbane King George Hotel and (3) Novotel Sydney Paramatta. The fair value gains helped drive profit before tax from continuing operations higher at SGD34.5mn in 1QFY2018 against SGD18.9mn in 1QFY2017.

- **Interest coverage healthy:** EBITDA (based on our calculation which does not include other income and other expenses) was SGD19.7mn (down 9.8% y/y), while interest coverage as measured by EBITDA/Interest was stronger at 5.3x, relatively flat y/y. Interest expense continues to fall due to lower interest rates (4QFY2018 effective interest rate was 2.6% against 2.9% for 4QFY2017) amidst relatively unchanged gross debt levels.

- **Short term debt significant though low refinancing risk:** As at 31 March 2018, reported aggregate leverage improved to 30.8% compared to 33.2% as at 31 December 2017. As at 31 March 2018, short term debt was SGD155.7mn, largely made up of secured bank loans. This represents 29% of total gross debt. We see refinancing risk as low given that ASCHT has sold down its China hotel portfolio where proceeds can be used to repay such debt. The two hotels were sold to a joint venture made up of China Lodging Group and TPG (a financial investor) for RMB1.16bn (~SGD235.9mn), to be adjusted for working capital.

- **Completed maiden acquisition of South Korea hotel:** On 21 May 2018, ASCHTS announced that it has acquired KY-Heritage Hotel Dongdaemun in South Korea for KRW75.4bn (~SGD93.1mn) (the deal was first announced on 27 April 2018). ASCHT has acquired a 98.7% stake in the hotel while the remaining 1.3% stake is owned by Ascendas (Korea) Pte Ltd, an entity which is indirectly owned by the Sponsor of ASCHT. Total acquisition cost (including transaction costs) attributable to ASCHT's 98.7% stake amounts to KRW81.6bn (~SGD100.7mn). We assume that debt was first used to pay for the acquisition, with aggregate leverage rising to ~33%. Assuming that SGD160mn in cash is subsequently used to repay debt and the rest kept as war chest for further investment, ASCHT may end up with an aggregate leverage of ~27%.

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Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight ("OW") – The performance of the issuer's specific bond is expected to outperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral ("N") – The performance of the issuer's specific bond is expected to perform in line with the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight ("UW") – The performance of the issuer's specific bond is expected to underperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

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