Asia Credit Research

Earnings Review: Frasers Commercial Trust ("FCOT")

Recommendation

- We see continued weakness at FCOT and think it will take some time to normalise occupancy rates across its assets. That being said, FCOT has room to pursue asset injections by the sponsor given its significantly low aggregate leverage and financial flexibility. We will retain our Neutral (4) Issuer Profile.
- We prefer SUNSP 3% '21s and SUNSP 2.85% '23s to FCOTSP '21s and FCOTSP 3.185% '23s respectively as SUNSP offers a spread pick-up of ~10bps despite maturing minimally a month earlier for both tenors. We have both FCOT and Suntec REIT at Neutral (4) Issuer Profile.
- For FCOTSP '20s, we think MCTSP 3.6% '20s provide somewhat better value as it has a stronger credit profile at Neutral (3) Issuer Profile worth ~10bps on top of a 5bps spread pick-up for six months extension in maturity.

Issuer Profile: Neutral (4)

Ticker: **FCOTSP**

Background

Frasers Commercial Trust ("FCOT") holds office and business park assets and is sponsored by Frasers Property Ltd ("FPL", which holds a 26.8% interest in FCOT). FCOT reported a portfolio value of SGD2.13bn as at 30 September 2018 which comprises China Square Central ("CSC") and Alexandra Technopark ("ATP") in Singapore, and 357 Collins Street, Melbourne Caroline Chisholm Centre, Canberra and 50% of Central Park, Perth in Australia and 50% of Farnborough Business Park in the UK.

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Relative Value:

Bond	Maturity/Call date	Aggregate leverage	Ask Yield	Spread
FCOTSP 2.625% '20	**28/02/2020**	**28.3%**	**2.62%**	**50bps**
FCOTSP 2.783% '21	**15/03/2021**	**28.3%**	**3.00%**	**73bps**
FCOTSP 2.835% '21	**11/08/2021**	**28.3%**	**3.02%**	**71bps**
FCOTSP 3.185% '23	**28/02/2023**	**28.3%**	**3.37%**	**95bps**
MCTSP 3.6% '20	24/08/2020	34.7%	2.75%	55bps
SUNSP 3% '21	16/07/2021	36.6%	3.13%	83bps
SUNSP 2.85% '23	02/08/2023	36.6%	3.51%	106bps

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

Key Considerations

- **Weakness stems largely from low occupancy:** Reported gross revenue for 4Q2018 was 14.2% lower y/y at SGD32.5mn while NPI declined by 19.2% y/y to SGD21.6mn. This is mainly due to lower occupancy rates for the ATP, CSC Central Park and 55 Market Street (which was divested on 31 August 2018) and the effects of the average weaker AUD. This is largely as expected, given the partial exit of HP Enterprises on 30 September 2017 from ATP and CSC closed its retail podium for its SGD38mn asset enhancement initiative in January 2018. For ATP, occupancy fell from 76% a year ago to 70.2% with property NPI down 33.4% y/y. CSC saw property NPI fall 13.9% y/y and Central Park, whose occupancy declined from 89% as at 30 September 2017 to 70%, saw NPI fall 20.3% y/y. Also, AUD weaken against SGD from AUD/SGD1.0636 in 4Q2017 to 0.9904 (~6.88% dip) leading to translation losses y/y.

- **Portfolio statistics improved slightly q/q:** In aggregate, committed occupancy recovered to 83.4% from 81.9% in 3Q2018 though actual occupancy remained unchanged at 79.5%. While ATP recorded the largest jump in occupancy rate by 5.4%, we note that the lease by HP Singapore which constitutes 9.0% of the NLA of the property will be expiring on 31 December 2018. Therefore, the improvement may not be sustained. That said, portfolio's WALE improved q/q to 4.7 years (3Q2018: 4.0 years) and the WALE of FCOT's top ten tenants contributing ~53% of portfolio gross rental income is higher at 5.7 years from 5.3 years in 3Q2018. While there is no q/q comparison, total portfolio value was up 3% relative to 30 September 2017 with all valuation for five assets (excluding Farnborough Business Park which was acquired on 29 January 2018) reporting higher valuation in local currency.

- **Performance of Singapore assets is key in FY2019:** Occupancy rate at CSC (excluding the retail podium closed for asset enhancement) and ATP improved in 4Q2018 to 94.4% and 70.2% respectively (3Q2018: CSC: 93.9% and ATP: 64.8%) which translate to a 1.79% q/q increase in NPI collectively. While this is positive news, we see a substantial amount of expiring leases in FY19 at both assets. CSC has leases amounting to 41.0% of its gross rental income expiring while expiring leases at ATP is 42.8% of the property's gross rental income. As at 30 September 2018, CSC has secured lease commitments for 26.8% of its gross rental income, leaving a balance of 14.2%. ATP, on the other hand, has a larger balance of 33.7% of its gross rental income. Jointly, they contribute to ~44% of portfolio's NPI (NPI includes FCOT's 50% interest in Farnborough Business Park) but make up ~80% of the portfolio's expiring leases by total portfolio rental income after adjusting for secured committed leases. Therefore, performance of these assets in the near term is crucial to FCOT. It is worth noting that the SGD45mn asset enhancement initiative for ATP announced in January 2017 is nearing completion while works at CSC is expected to be completed by 2H2019 to better position the asset for when Capri Hotel opens in 2019. As such, we think it can take some time for occupancies at both assets to normalise.

- **Financial flexibility given significant debt headroom:** Aggregate leverage is considerably low at 28.3% (3Q2018: 35.4%) following the pay down of SGD197mn debt which includes the prepayment of SGD157mn debt maturing in 2019 with the divestment proceeds of 55 market street. Reported interest coverage stood at 4.2x (3Q2018: 3.5x), with the average borrowing rate at 3.02% (3Q2018: 3.05%). Floating rate borrowings are 18.8% of gross borrowings. Near-term borrowings look very manageable with just SGD17mn debt maturing in 2019 as at 30 September 2018. Also, all of FCOT's assets are unencumbered, which offers flexibility. The low leverage level provides substantial headroom for FCOT to acquire assets from sponsor. Additionally, FCOT has over SGD4bn in right of first refusal properties from sponsor, Frasers Property Ltd.

<table>
<tr><th colspan="2"><u>OCBC Global Treasury</u></th></tr>
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Explanation of Issuer Profile Rating ("IPR") / Issuer Profile Score ("IPS")

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 ("IPR") into a 7 point Issuer Profile Score ("IPS") scale.

<table>
<tr><td>IPR</td><td colspan="2">Positive</td><td colspan="3">Neutral</td><td colspan="2">Negative</td></tr>
<tr><td>IPS</td><td>1</td><td>2</td><td>3</td><td>4</td><td>5</td><td>6</td><td>7</td></tr>
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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.

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