

Earnings Review: First Real Estate Investment Trust (“FIRT”)

Recommendation

- We see the introduction of OUE and OUE’s 64.4%-subsidiary OUE Lippo Healthcare as equity holders in FIRT and the REIT Manager as a credit positive. In our view, this would help FIRT gain better access to external liquidity, especially as FIRT faces near-term debt due.
- Nonetheless, the change in ownership is insufficient for us to lift our Issuer Profile of Negative (6) on FIRT as FIRT structurally still faces PT Lippo Karawaci Tbk (“LK”) and its subsidiaries as its main tenant (~82% to revenue in 2017).
- In our view, FIRTSP 5.68%-PERP should not trade tighter than Lippo Malls Indonesia Retail Trust (“LMRT”)’s LMRTSP 7.00%-PERP given that LMRT has a smaller concentration to LK-related entities as main tenant. We continue to be underweight the FIRTSP 5.68%-PERP on expectations that spreads could widen still from here.

Relative Value:

Bond	Call date	Aggregate leverage	Ask YTM ¹	Ask Yield-to-call	Spread on YTC
FIRTSP 5.68%-PERP	08/07/2021	34.3%	7.77%	12.4%	1,016bps
LMRTSP 7.00%-PERP	27/09/2021	36.0%	10.71%	19.2%	1,699bps

Note: (1) Indicative prices as at 09 November 2018 Source: Bloomberg

(2) Aggregate leverage based on latest available quarter

(3) YTM per Bloomberg assumes a 149 years to maturity; proxy of yield in perpetuity

Issuer Profile:
Negative (6)

Ticker: **FIRT**

Key Considerations

Background

Listed on the Singapore Stock Exchange with a market cap of SGD923mn as at 7 November 2018. FIRT is a REIT that invests primarily in real estate used for healthcare and healthcare-related sectors. Investment properties totaled SGD1.3bn as at 30 September 2018. We estimate that OUE Ltd has a 17.6%-deemed ownership stake in FIRT while PT Lippo Karawaci Tbk (“LK”)’s stake has declined to ~10.7%.

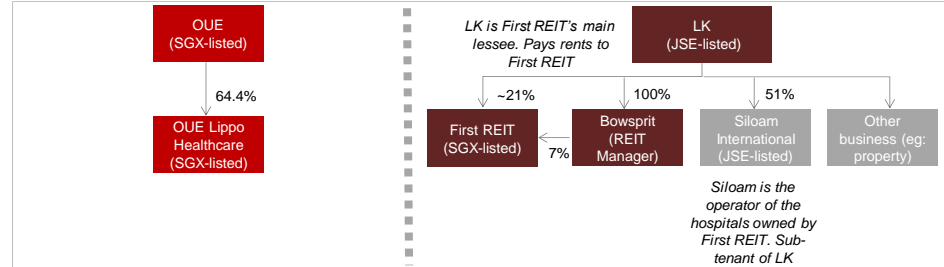
Ezien Hoo, CFA
+65 6722 2215

EzienHoo@ocbc.com

- **Interest coverage flat q/q:** In 3Q2018, gross revenue was up 5.1% y/y to SGD29.1mn while net property income (“NPI”) was up 5.4% y/y to SGD28.9mn. This was attributable to the full quarter contribution from Siloam Hospitals Buton & Lippo Plaza Buton and Siloam Hospitals Yogyakarta (bought in October 2017 and December 2017 respectively). EBITDA (based on our calculation which does not include other income and other expenses) was SGD25.9mn in 3Q2018 (up 5.3% y/y). Despite the stronger EBITDA generation, on the back of higher interest expense (up 25.3% y/y to SGD5.5mn), resultant EBITDA/Interest coverage was lower, though still manageable at 4.7x versus 5.6x in 3Q2017. On a y/y basis, interest had increased due to debt drawn down to finance the purchase of the two new hospitals and the second progress payment Siloam Hospitals Surabaya development. On a q/q basis though, finance cost had stayed relatively constant (2Q2018: EBITDA/Interest coverage of 4.7x). Assuming that FIRT pays out 5.68% p.a as perpetual distribution, EBITDA/(Interest plus 50% of perpetual distribution) was 4.1x in 3Q2018.
- **Trade receivables continue to pile up:** As at 30 September 2018, trade receivables at FIRT were SGD49.3mn, rising sharply from SGD29.1mn as at 30 June 2018, this (31 December 2017: SGD26.0mn). We find day sales outstanding (“DSO”) at 153 days in 3Q2018 versus 91 days in 2Q2018. The piling up of trade receivables is unsurprising to us given liquidity stresses at FIRT’s main tenant, LK. As a result, FIRT only generated SGD3.3mn in cash flow from operations (after tax but before interest) (“CFO”), the higher EBITDA generation. In contrast in 3Q2017, FIRT generated SGD17.5mn in CFO. In 2017, LK and its subsidiaries contributed 82.4% of FIRT’s revenue and this is likely to be similar in 3Q2018.
- **Introduction of a stronger equity holder:** In September 2018, OUE Limited (“OUE”, Issuer profile: Neutral (4)) and its 64.4%-owned subsidiary OUE Lippo Healthcare Limited (“OUE-LH”) announced the proposed purchase of FIRT’s REIT Manager (“FIRTM”) for SGD98.9mn from LK (FIRT’s Sponsor and largest unitholder then). Additionally, OUE-LH would buy a ~10.6%-stake in FIRT for SGD102.7mn, also from LK. The purchase was completed on 26 October 2018. OUE, OUE-LH, FIRT and LK were sister companies, sharing the same ultimate controlling shareholder. The deal

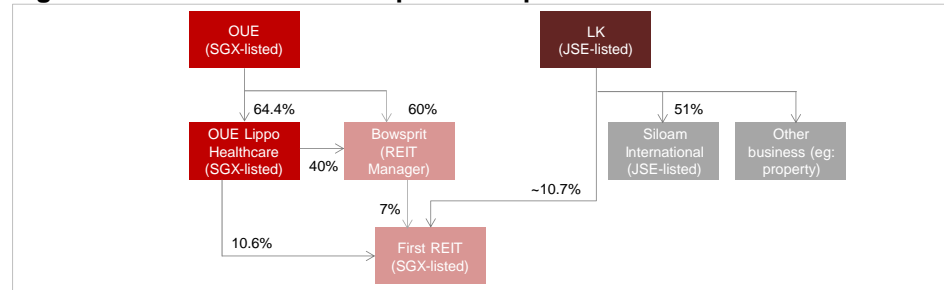
saw OUE buying 60% of FIRT with OUE-LH buying the remaining 40%. Apart from its REIT Manager function, FIRTM holds a 7%-stake in the REIT. We estimate that OUE now holds a 17.6% deemed ownership in FIRT while its effective stake is 11.0%, from its 60%-stake in FIRTM and 64.4%-stake in OUE-LH. LK's stake in FIRT had declined to ~10.7% based on our estimates and in total LK had received SGD201.6mn in cash from this sale.

Figure 1: Pre-transaction simplified corporate structure



Source: Bloomberg, OCBC Credit Research

Figure 2: Post-transaction simplified corporate structure



Source: Company, OCBC Credit Research estimates

- Aggregate leverage:** As at 30 September 2018, FIRT's unadjusted aggregate leverage was 34.3%, rising somewhat from the 33.6% as at 30 June 2018. FIRT had taken on additional debt to help fund dividends to unitholders, interest and distribution to perpetual holders (SGD22.1mn was paid to capital source providers in 3Q2018). SGD60mn of perpetuals outstanding at FIRT made up 4.4% of total capital and adding 50% of these as debt, we find adjusted aggregate leverage at 36.4%, still manageable. As at 30 September 2018, SGD385.6mn (representing 78% of gross debt) at FIRT was secured debt. We estimate this debt is collateralized by SGD976mn worth of investment properties.
- Short term debt coming due though access to external financing better:** As at 30 September 2018, FIRT faces SGD109.8mn in short term debt coming due in November 2018 and March 2019 respectively (represents 22% of total debt). An earlier short-term bridge loan was drawn down to take out FIRT's SGD100mn bond that was due in May 2018. Per company, FIRT is in negotiations with banks to extend and refinance this debt that is coming due. We assume that lenders holding the properties as collateral are willing to extend additional secured debt on the same collateral package. With secured debt-to-value ("LTV") of 40% as at 30 September 2018, FIRT still has a headroom of SGD102mn in secured debt, assuming that lenders are willing to go up to LTV of 50%. While the liquidity situation at FIRT has tightened, in our view the introduction of OUE as new equity holder of both FIRTM and FIRT should allow FIRT better access to financing markets. If need be, OUE-LH (and indirectly OUE) would be able to raise money and inject capital into FIRT. For example, via a shareholder's loan. We think FIRT would be recognized as an associated company given OUE's control over the REIT Manager. It would be considered par for course for OUE and/or OUE-LH to provide a corporate guarantee on FIRT's loans.

OCBC Global Treasury

Treasury Advisory

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Tel: 6349-1888 / 1881

Interest Rate Derivatives

Tel: 6349-1899

Investments & Structured Products

Tel: 6349-1886

GT Institutional Sales

Tel: 6349-1810

Credit Research

Andrew Wong

+65 6530 4736

WongVKAM@ocbc.com

Ezien Hoo, CFA

+65 6722 2215

EzienHoo@ocbc.com

Wong Hong Wei, CFA

+65 6722 2533

wonghongwei@ocbc.com

Seow Zhi Qi

+65 6530 7348

ZhiQiSeow@ocbc.com

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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.

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.

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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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Analyst Declaration

The analyst(s) who wrote this report and/or her or his respective connected persons did not hold securities in the above-mentioned issuer or company as at the time of the publication of this report.

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