Asia Credit Research

Frasers Commercial Trust: New Issue View

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New Issue View: Frasers Commercial Trust ("FCOT") has priced a SGD60mn 5-year bond issue at a coupon of 3.185% (5Y SDSW + ~95bps).

We currently hold FCOT at a **Neutral (4) Issuer Profile**. Peers with comparable issuer profile include Suntec REIT ("SUN", Neutral (4)) and Keppel REIT ("KREITS", Neutral (4)).

The new FCOTSP 3.185% '23s look to offer a pickup of ~30bps over its existing FCOTSP 2.835% '21s bonds for a duration extension of ~1.5 years. This looks wide assuming a ~10bps increase in credit spread per year.

When comparing against its peers, the new FCOTSP 3.185% '23s look to be trading 30-40bps wider despite having lower aggregate leverage. Though we expect aggregate leverage to tick higher to ~35% due to its acquisition of 50% of Farnborough Business Park and the subsequent equity placement raising ~SGD100mn, leverage would still be lower than SUN and KREITS. Investors are likely to let SUN and KREITS trade tighter due to their much larger scale of SGD9.6bn and SGD8.5bn respectively. Comparatively, FCOT has SGD2.1bn in assets. Even then, the spread concession looks to be too wide.

In aggregate, based on FCOT's existing curve, as well as its peers, the new FCOTSP 3.185% '23s looks to have provided a new issue concession of 10bps – 15bps. This translates into a fair value price of 100.5 – 100.7 (based on the spread over 5Y SDSW of 80bps – 85bps). That being said, it would seem that the upside to fair value looks slight. As such, **we are Neutral on the new FCOTSP 3.185% '23s**.

Peer Comparison:

Bond	Aggregate Leverage	Int. Cover	Issuer Rating S&P/Moody's/Fitch	Ask Yield	Spread (bps)
FCOTSP 3.185% '23	34.8%	4.3x	NR/Baa2/NR	3.185%	95
FCOTSP 2.835% '21	34.8%	4.3x	NR/Baa2/NR	2.71%	66
FCOTSP 2.625% '20	34.8%	4.3x	NR/Baa2/NR	2.37%	57
SUNSP 2.85% '23	36.4%	3.9x	NR/Baa3/NR	2.80%	51
KREITS 3.275% '24	38.7%	4.3x	NR/NR/NR	3.00%	65

Source: Bloomberg

Background: Frasers Commercial Trust ("FCOT") is a REIT that holds largely office and business park assets and is sponsored by Frasers Property Ltd ("FPL", which holds a ~25% interest in FCOT). FCOT reported a portfolio value of SGD2,055mn (end-1QFY2018), which comprises of China Square Central ("CSC"), Alexandra Technopark ("ATP") and 55 Market Street in Singapore, as well as 357 Collins Street, Melbourne Caroline Chisholm Centre, Canberra and 50% of Central Park, Perth in Australia. Subsequently, FCOT had acquired a 50% stake in Farnborough Business Park in the UK for ~SGD158mn with the transaction completed towards the end of January 2018.

Key credit considerations

- **Recent performance impacted by HP departure and AEI:** For 1QFY2018 results, gross revenue fell 11.0% y/y to SGD35.3mn while NPI fell a sharper 14.9% y/y to SGD24.9mn. This was largely as expected, given the exit of HP Enterprise and the staggered exit of HP Singapore from Alexandra Technopark (current committed occupancy stands at 79.9%), which caused property NPI to fall 25% y/y to just SGD7.6mn (Alexandra Technopark is FCOT's largest asset by NPI contribution). China Square Central also saw property NPI fall by 15% to SGD4mn due to the closure of the retail podium for its SGD38mn AEI (construction to start in 1Q2018), to

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better position the asset for when the Capri hotel opens in 2019.

- **Other assets were also a drag**: The performance of FCOT's other assets were also unexpectedly weak, with 55 Market Street seeing NPI fall 12% y/y as well due to occupancy issues while FCOT's Australian assets were affected by the weaker AUD. Occupancy issues (property actual occupancy only 64.6%) too caused the Central Park's NPI to decline 19% y/y (on top of the AUD impact).

- **Things look unlikely to improve in the near-term**: In aggregate, portfolio occupancy has fallen sharply from 93.0% (1QFY2017) to 80.3% (1QFY2018). Lease expiry for FY2018 looks heavy at 19.3% of NLA expiring, of which a sizable amount is due to HP Singapore leaving Alexandra Technopark. Given the expected AEI work across various properties, we expect FCOT's numbers to remain weak for the next two quarters. WALE remained stable at 3.6 years, supported by the longer leases on the Australian assets. Curiously, FCOT had stopped disclosing rental reversion numbers during the quarter, when it was previously available.

- **Acquisition of Farnborough Business Park mitigated by equity placement**: Aggregate leverage had remained stable at 34.8% (4QFY2017: 34.7%). That said, FCOT had acquired 50% of Farnborough Business Park with a GBP88mn (~SGD160mn) 6-month unsecured bridge loan, with the transaction completed end-January 2018. FCOT had subsequently raised SGD100mn via an equity private placement as permanent funding for the Farnborough Business Park acquisition. The current SGD60mn 5-year new bond would nicely fund the balance of the transaction. We estimate that aggregate leverage for FCOT would inch higher to 35.0% after considering the final financing structure of the acquisition.

- **Future Europe acquisitions may stretch balance sheet**: Liquidity looks manageable with reported interest coverage at 4.3x. Floating rate borrowings increased somewhat to 19.3%, compared to 15% in 1QFY2017. Near-term borrowings look manageable, with SGD140mn in AUD bank loans and SGD40mn in SGD bank loans due. FCOT had managed to issue 3 bonds in 2017, before the current new issue. One thing worth noting is that with the previously announced expansion of FCOT's investment mandate to include European assets, FCOT had highlighted that it now has a SGD4.0bn acquisition pipeline. This is due to ROFR assets from its sponsor, Frasers Property Limited, with properties in Singapore, Australia and the UK. Should FCOT start to ramp up its portfolio via acquisitions, it could pressure FCOT's credit profile if more debt is taken to fund its growth. We are currently holding FCOT at Neutral (4) Issuer Profile.

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