

Earnings Review: Soilbuild Business Space REIT ("SBREIT")

Recommendation

- 2Q2018 income was dragged by decline in operating performance at West Park BizCentral as expected though encouragingly, Eightrium's occupancy increased 1ppt to 88.5%. Future new supply at One-North may pose some pressure to lease rates at Solaris in the next 12 months though we maintain SBREIT's issuer profile at Neutral (4) given its manageable credit metrics.
- Comparing to EREIT 3.95% '20s, we now see SBREIT 3.6% '21s trading at fair value following SBREIT '21s yield tightening since end-June 2018. We also have ESR-REIT ("EREIT") at an issuer profile of Neutral (4).

Relative Value:

Bond	Maturity	Aggregate leverage	Ask Yield	Spread
SBREIT 3.6% '21	08/04/2021	37.6%	3.66%	164bps
EREIT 3.95% '20	21/05/2020	30.0%	3.32%	141bps

Indicative prices as at 23 July 2018 Source: Bloomberg
Aggregate leverage based on latest available quarter

Issuer Profile: Neutral (4)

Ticker: **SBREIT**

Background

Listed in 2013, Soilbuild Business Space REIT ("SBREIT") is an Industrial REIT in Singapore, with total assets of SGD1.1bn as at 30 June 2018. SBREIT currently owns a portfolio of 11 properties in Singapore. The REIT is Sponsored by Soilbuild Group Holdings Ltd ("Soilbuild") and Soilbuild is wholly owned by Mr. Lim Chap Huat. The Lim family is the REIT's largest unitholder, with a 28.9% stake.

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Key Considerations

- Flat same-store revenue in 2Q2018:** Gross revenue declined 13.1% y/y in 2Q2018 to SGD18.7mn, on the back of declines at 72 Loyang Way, absence of revenue from the divestment of KTL Offshore building (sold to Sponsor in February 2018) and weaker performance at West Park BizCentral and Eightrium. Net property income declined in tandem to SGD16.2mn. On a quarter-on-quarter basis though, gross revenue only fell 3.7% mainly due to the KTL Offshore divestment. Removing the impact from KTL Offshore (on a same-store basis), revenue was relatively flat q/q.
- Aggregate leverage fell following redemption of the SBREIT'18s:** Reported aggregate leverage was lower at 37.6% (31 March 2018: 40.2%) as SBREIT had paid down its SGD93.5mn bond due in May 2018 in part from the net proceeds of SGD54.7mn from the sale of KTL Offshore building. The only remaining short term debt due is the SGD55mn in interest-free loan extended by the Sponsor in 2015 and 2016 for SBREIT to pay JTC an upfront land premium on Solaris. This loan will come due in August 2018. On 18 July 2018, SBREIT announced that it has entered into an unsecured bank debt facility of SGD70.0mn. It is likely that part of this new loan will be used for refinancing of the interest free loan. Only Solaris has been mortgaged for bank debt while SGD752.1mn of investment properties remains unencumbered and can be used as collateral, if need be.
- Interest coverage within expectations:** EBITDA (based on our calculation which does not include other income and other expenses) declined q/q by 4.4% to SGD14.9mn while finance expense was relatively steady. In 1Q2018, SBREIT took back Tellus Marine (39 Senoko Way) from the master lessee, who had been arrears. 39 Senoko Way is a small contributor (2% of 1Q2018 gross revenue). Assuming that a cost of 3.34% p.a is applied on the new loan taken to refinance the interest free loan, interest expense may increase by SGD459k per quarter. Under the downside scenario where 39 Senoko Way is non-contributing and adding the additional interest expense, we find adjusted EBITDA/Interest manageable at 3.5x. That being said, there are still three tenants who are contributing rents at 39 Senoko Way (which make up ~40% of original master lease's rent).
- Portfolio occupancy stabilised though West Park BizCentral continued to drag:** Overall SBREIT portfolio occupancy had stabilised at 87.6% (up slightly from 87.5% as at 31 March 2018), with improvements seen in Eightrium (88.5% from 84.9% as at 31 March 2018). West Park BizCentral continued to dip, with

occupancy now at 81.0% (81.5% as at 31 March 2018 and falling significantly in 90.4% in end-2017). SBREIT's overall rental reversion was negative 11.9% in 2Q2018, on 251,556 sq ft (6.8% of total net lettable area). While 11.9% looks high, it is worth noting that these negative reversions were down from lease rates signed three to four years ago (while not signed at peak cycle was still prior to the current down cycle). On a quarter by quarter basis, sector rents are pointing towards stabilization rather than a continuation of the downtrend. We expect the stabilization of rents to continue going into 2H2018.

- **New supply at One-North:** In March 2018, Boustead launched a new business park development "Alice" at One-North where Solaris is located in. Solaris is SBREIT's crown jewel, located five minutes away from the One-North MRT station. "Alice" is a speculative build (not commissioned by end-user) and construction is expected to complete in the later part of the year. Given Solaris' established profile, we think key tenants may continue to stay with Solaris. That being said, we think the completion of Alice may lead to higher bargaining power by Solaris' tenants over renewal lease rates.

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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.

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

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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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Analyst Declaration

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