Asia Credit Research

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

Recommendation

- While we expect 2Q2018 income to be dragged lower by the decline in operating performance at West Park BizCentral and Eightrium, this is insufficient to move SBREIT's issuer profile in our view. We maintain SBREIT's issuer profile at Neutral (4).
- Relative to EREIT 3.95% '20s, we see better value in the SBREIT 3.6% '21s. Adjusting for the 11 months longer time to maturity, the SBREIT 3.6% '21s allows for a 40bps spread pick-up which more than compensates for its lack of external credit rating. We also have EREIT at an issuer profile of Neutral (4).

Relative Value:

Bond	Maturity	Aggregate leverage	Ask Yield	Spread
SBREIT 3.6% '21	08/04/2021	40.2%	4.0%	191
EREIT 3.95% '20	21/05/2020	39.6%	3.3%	130

Indicative prices as at 18 April 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 SGD1.2bn as at 31 March 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 28.7% stake.

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Key Considerations

- **Decline in profitability in 1Q2018:** SBREIT reported its first quarter results for the financial year 2018 ("1Q2018"). Reported gross revenue was down 11.5% y/y to SGD19.4mn. This was driven by revenue declines at 72 Loyang Way, West Park BizCentral, Eightrium and KTL Offshore building. 72 Loyang Way was affected by the absence of security deposits (used up by mid-2017), which held up 1Q2017 revenue. West Park BizCentral and Eightrium both saw reduction in occupancies while only two months of revenue was recognised at KTL Offshore building (property was divested to the Sponsor on 28 February 2018). SBREIT reported a SGD1.7mn gain from divestment of KTL Offshore building as the asset was sold above book value. This tenant at the building was previously in arrears. One of the stated reasons for the sale of the building was to minimise SBREIT's counterparty credit risk exposure. On 5 April 2018, the tenant had terminated the lease agreement with Sponsor (ie: a termination that SBREIT would have had to face if a sale did not happen). We see it as a positive sign that management had taken creditor-friendly steps in managing the REIT.

- **Interest coverage manageable against peers:** Based on our EBITDA calculation (excludes gain on divestment from the KTL Offshore building and other expenses), we find EBITDA to have fallen 11.7% y/y to SGD15.5mn. Interest expense was down 3.8% y/y to SGD3.8mn, driven by interest savings from refinancing of a bank loan. Despite the reduction in EBITDA, interest coverage as measured by EBITDA/Interest was still healthy at 4.1x (1Q2017: 4.5x). On the back of rental arrears, during the quarter, SBREIT had also taken possession of 39 Senoko Way (ie: Tellus Marine building) which is a small contributor to gross revenue at 1.9% in FY2017. Removing the contribution from KTL Offshore building (since sold) and 39 Senoko Way, we find adjusted EBITDA/Interest at 3.9x, still manageable versus its immediate peers.

- **Aggregate leverage to fall following redemption of the SBREIT'18s:** Reported aggregate leverage was 40.2% as at 31 March 2018, in line with end-2017 figures though this is expected to fall to 37% following the repayment of the SGD bond SBREIT'18s with an outstanding amount of SGD93.5mn on 21 May 2018. We see low refinancing risk for this bond. The bond is expected to be repaid by the ~SGD54.7mn net proceeds from the sale of KTL Offshore building, committed debt facility of SGD15.0mn and some additional new debt. As at 31 March 2018, unencumbered properties were SGD751.3mn (end-2017: SGD803mn). Secured debt-to-total asset was still manageable at 15.5%.

- **Weaker operating performance at West Park BizCentral and Eightrium:** As at 31 March 2018, SBREIT's portfolio occupancy was 87.5%, significantly lower than the 92.7% recorded in end-2017 and more in line with market. Sector wide numbers for 1Q2018 has not been released though in 4Q2017, the industrial property sector saw occupancies of 88.9% (up 0.3% from 3Q2017). We understand from management that the decline in West Park BizCentral (down to 81.5% from 90.4% in end-2017) is due to certain tenants who have downsized/closed and tenants who have moved out into purchased space. Occupancy on Eightrium (a business park property) is down to 84.9% from 97.7% in end-2017 and this was driven by a tenant's back office operations moving out of Eightrium. Collectively, West Park BizCentral and Eightrium make up 34% of portfolio value.

- **Negative rental reversions though narrowed from last quarter:** In 1Q2018, thirteen leases were renewed (including forward renewals) at a rental reversion of -7.2% while five new leases were entered at rates that were 11.9% below the previous rates. Overall, -7.8% in rental reversion on 302,994 sq ft area was recorded. On the plus side, this had narrowed from the -15.7% seen in 4Q2017 where SBREIT entered into nine leases for 212,187 sq ft area.

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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.

<u>Other</u>

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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