Asia Credit Research

OCBC Bank

Singapore Property: Sector Update

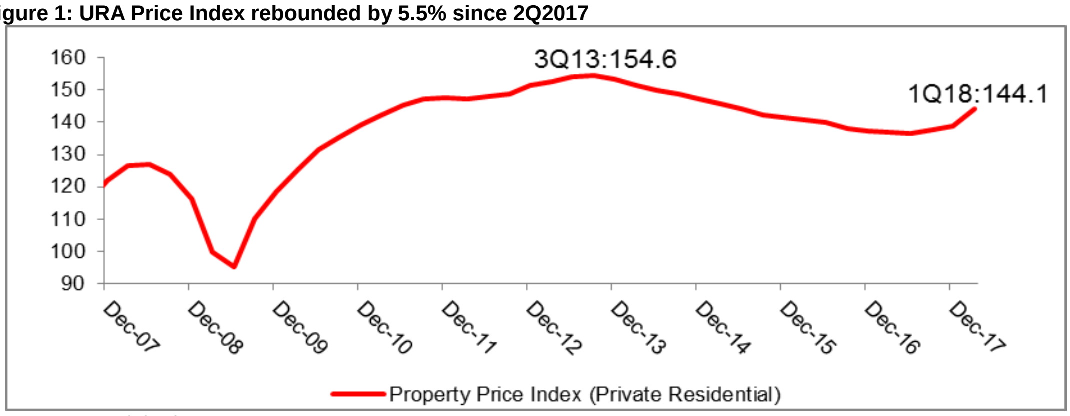
Thursday, 03 May 2018

Full speed ahead, for now

Summary and recommendation:

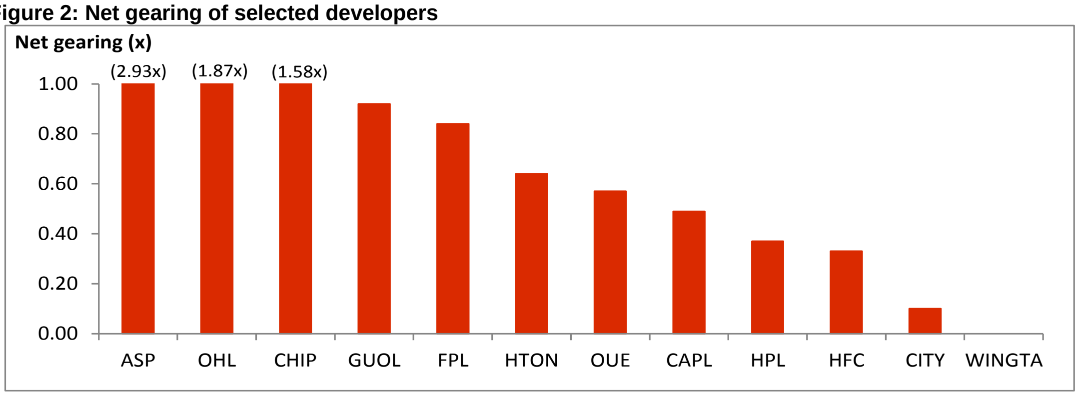
- **Prices have strongly rebounded: The** 1Q2018 URA private residential price index printed +3.9% q/q, which is the strongest q/q showing since 4Q2011. Prices as of 1Q2018 are 5.5% higher than the lows in 2Q2017, though still 6.8% shy from the all-time high achieved in 3Q2013.
- **Optimism may be sustained through 2018:** As mentioned in our Singapore Credit Outlook 2018, we expect the recovery to be sustained through 2018. The wave of en-blocs, still-low unsold units in the near-term and growth in Singapore's economy should lend support to property prices.
- **When will the party stop?:** While en-blocs fuel demand and withdraw supply in the near-term, we will be wary going into 2019 as we expect a ramp up in launches. Government intervention, changes in the economic environment and rising interest rates may also bring the party to a halt.
- **Credit metrics on a general downtrend:** Net gearing has continued to rise for the developers under our coverage as they acquire and complete land acquisitions. For the more levered developers, the ability to achieve strong sales and monetise the land bank will be crucial to support their credit profiles.
- **Recommendation:** As we approach 2H2018, we think investors should increasingly consider the dynamics in 2019 and Underweight the more aggressive developers (e.g. CHIPEN and OHLSP curve, ASPSP 5.9% '21s, GUOLSP 4.6% PERP, GUOLSP '19s and GUOLSP '20s). While rising prices have vindicated the aggressive bids, developers with higher leverage may have less room to maneuver in the event that units do not move. We Overweight the FPLSP curve, OUE curve and HTONSP curve, which we think are in the sweet spot as these developers have more moderate net gearing levels while providing still decent spreads.

Figure 1: URA Price Index rebounded by 5.5% since 2Q2017



Source: URA, OCBC

Figure 2: Net gearing of selected developers



Source: Company, OCBC

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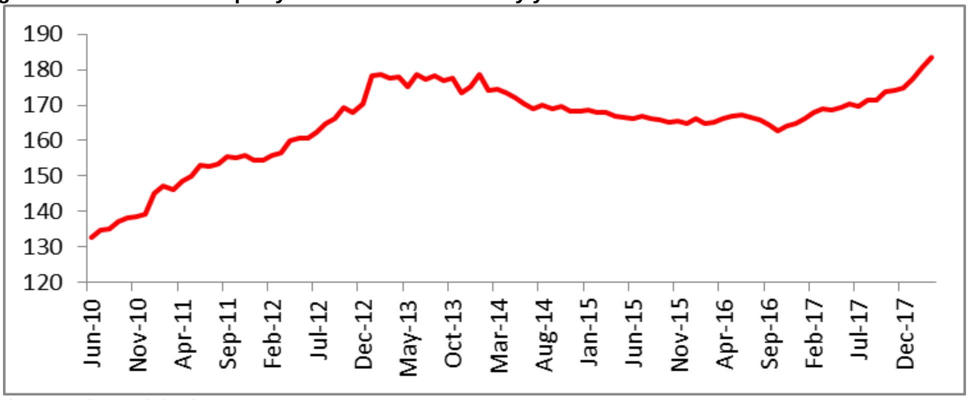
Optimism through 2018:

- **Broad-based recovery:** 1Q2018 URA private residential price index increased 3.9% y/y, led by Core Central Region (+5.5%) and Outside Central Region (+5.6%) while Rest of Central Region (+1.2%) grew more modestly. Since 2Q2017, prices have rebounded by 5.5%. The resale SRX Property Index also grew strongly (+8.6% y/y) in March 2018, with prices surpassing the Jan-14 peak by 2.6%.

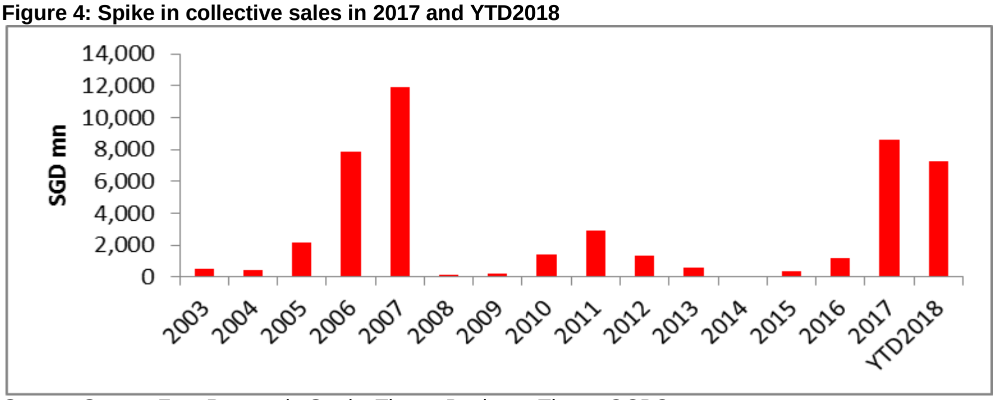
Figure 3: SRX Resale Property Index increased 8.6% y/y in March 2018



Source: SRX, OCBC

- **Spillover effect from collective sales fever:** SGD7.3bn of properties have been transacted via en-blocs since Jan-18, following SGD8.6bn of transactions in 2017. We believe this has been the dominant effect in lifting property prices as (1) displaced homeowners are likely to look for a replacement abode, (2) units are taken out of supply and (3) high prices paid by developers lead to higher price expectations by home buyers and sellers.

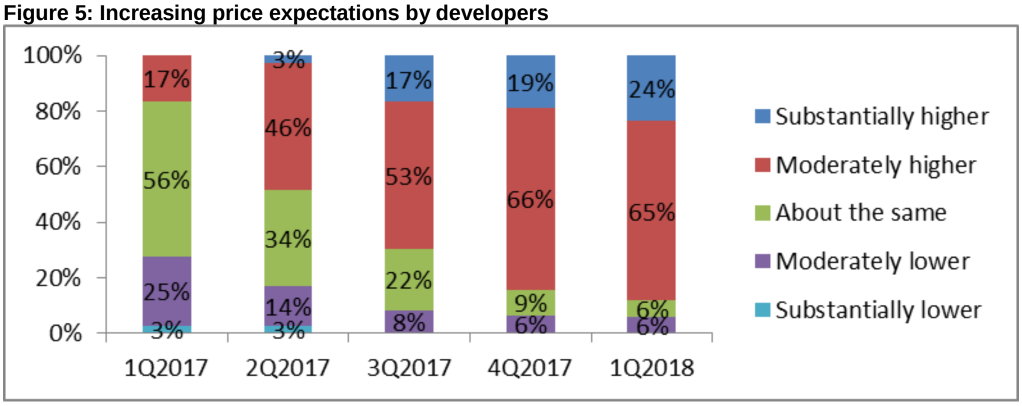
Figure 4: Spike in collective sales in 2017 and YTD2018



Source: Square Foot Research, Straits Times, Business Times, OCBC

- **Property developers are increasingly bullish:** Developers have expressed their bullishness via aggressive land bids. For example, the recent government land sale ("GLS") along Cuscaden Road received a record bid of SGD2,377 psf ppr. We think the aggressive bids in turn support higher property prices as expectations have increased. We also expect developers to hold up prices (and be less willing to lower prices) as their breakeven costs are higher. Through a survey by NUS-REDAS, 88.2% of developers expect prices to increase in the next 6 months, perhaps as bids previously seen to be aggressive have been vindicated.

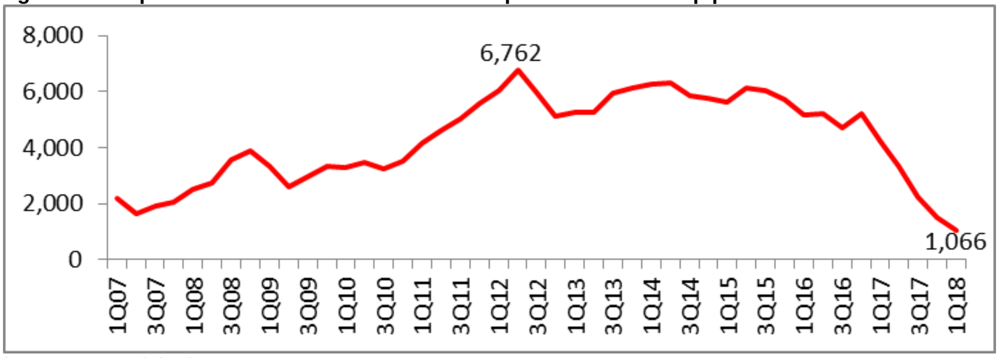
Figure 5: Increasing price expectations by developers



Source: NUS-REDAS, OCBC

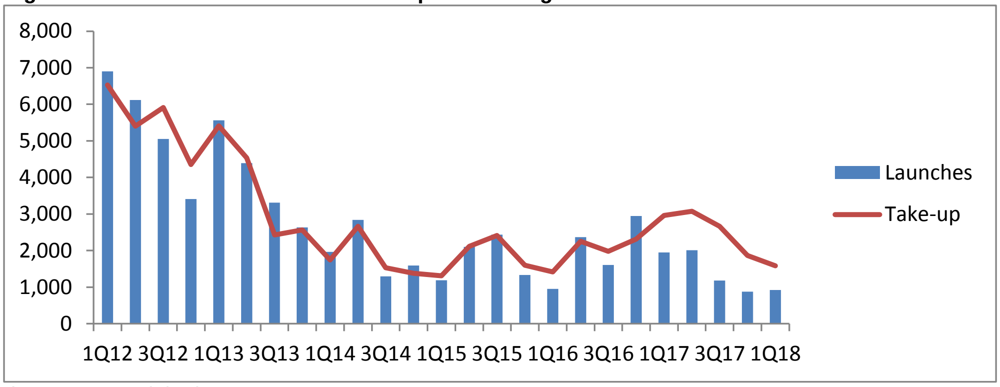
- **Healthy state of the economy:** Singapore 1Q2018 GDP grew 4.3% y/y, with our colleagues at OCBC Treasury Research forecasting growth for 2018 at 3.0%.
- **Pick up in rentals:** Perhaps due to displaced homeowners from collective sales, 1Q2018 private residential vacancy rates improved to 7.4% (4Q2017: 7.8%), with 0.3% q/q increase in rental rates.
- **Favourable supply-demand dynamics, for now:** Through 1Q2017 to 1Q2018, take-ups have outnumbered launches. While the number of unsold units in 1Q2018 (saw a pick up since 3Q2017, we think that the available supply of units in the market has in fact fallen significantly, with only 1,066 uncompleted units in 1Q2018 launched but unsold (1Q17: 4,183 units). This decline in immediately available supply is perhaps also due to developers withholding launches (amidst expectations of prices rising further), with take-ups outnumbering launches since 1Q2017.

Figure 6: Steep fall in launched but unsold uncompleted units in the pipeline



Source: URA, OCBC

Figure 7: Decline in launches with take-ups exceeding launches

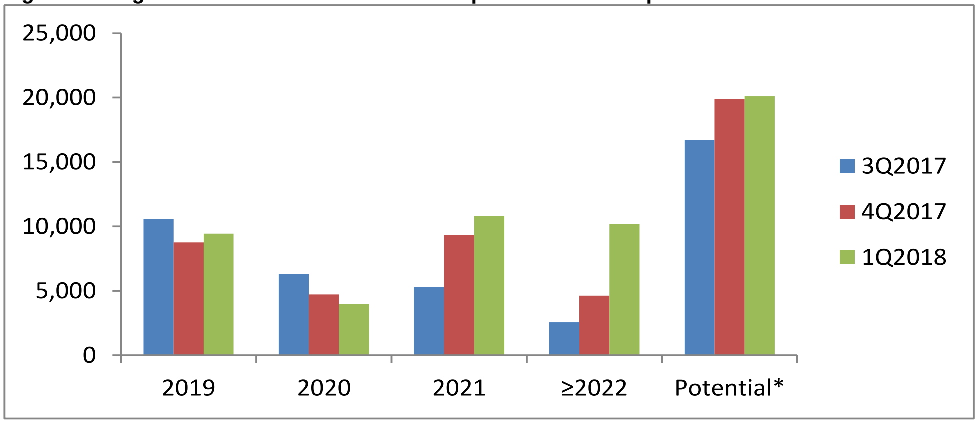


Source: URA, OCBC

Turning cautious in the medium term:

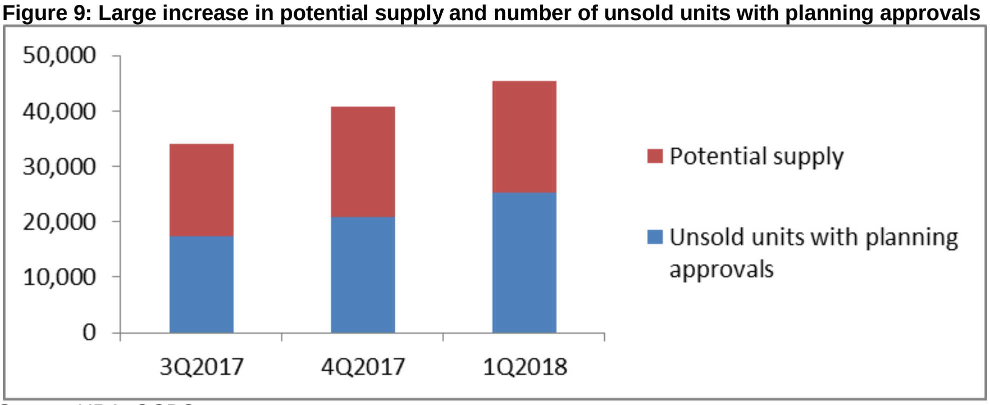
- **Surge in supply:** MAS, through the Financial Stability Review (Nov 2017), cautioned of the uncertainty if the new supply in the market can be fully absorbed. We formerly opined that the market need not be overly alarmed as there should be room to digest the increase in units. However, it were a mere uncertainty in Nov 2017, we are turning cautious as the risks have skewed towards an oversupplied market following a further flood of supply. The number of unsold units with planning approvals and potential supply in 1Q2018 is higher by 33.2% compared to 3Q2017.

Figure 8: Large increase in number of units expected to be completed in 2021 and onwards



Source: URA, OCBC
**Potential supply from GLS and awarded en-bloc sale not granted planning approvals*

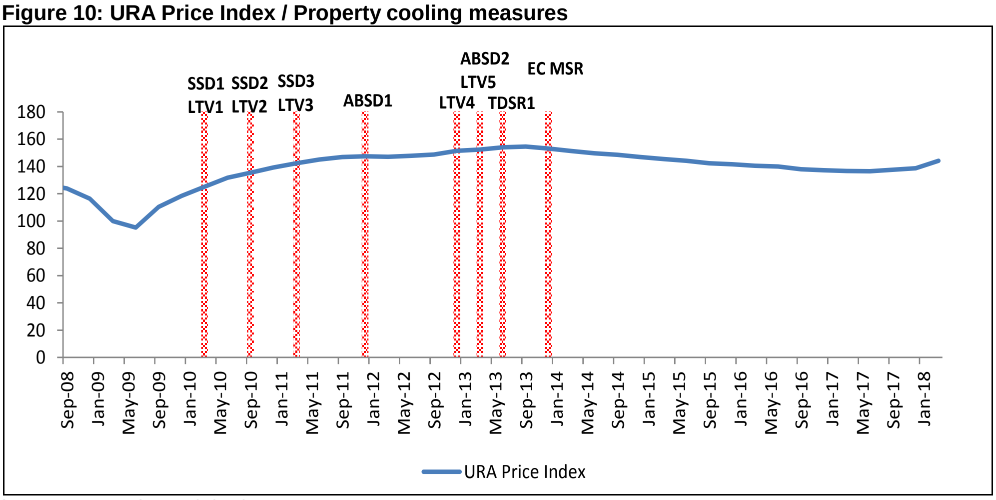
Figure 9: Large increase in potential supply and number of unsold units with planning approvals



Source: URA, OCBC

- **Potential crowding of launches:** While the near-term demand-supply dynamics look favourable, with enblocs driving prices higher, we think this may turn into a double-edged sword. A significant proportion of projects which undertook collective sales in 2H2017 can likely launch by 4Q2018 (assuming 12 months turnaround) while the enbloc projects in YTD2018 may launch in 1H2019. If take up rates prove to fall short given the significant supply, we believe developers may race to rush inventories out of the door given the hefty Additional Buyer's Stamp Duty ("ABSD") that will be imposed if there are unsold units.
- **Would the pace of enblocs be sustained?:** With developers having undertaken SGD15.8bn of enblocs since 2017, we think they are no longer as hungry for land. We expect the pace of enblocs to slow and the spillover effects from the collective sales fever to subside.
- **Risks of further government regulations:** In addition to the warnings made by MAS and caution of "excessive exuberance" by National Development Minister Lawrence Wong, the government has hiked the development charges rates. The 3.9% price increase in 1Q2018 has exceeded the pace of quarterly price increase over 2011-13 (when a series of property cooling measures were implemented). We opine that further interventions are likely if prices continue to surge at the same pace as 1Q2018.

Figure 10: URA Price Index / Property cooling measures



Source: URA, SRX, OCBC

- **Rise in interest rates:** According to NUS-REDAS, 87.3% of developers think that rising inflation / interest rates is a potential risk in the next 6 months. Already, 3M SIBOR has surged to ~1.5%. If rates continue to increase, this may dampen demand.

Recommendation: In general, we recommend to Underweight the more aggressive developers including the CHIPEN and OHLSP curve, ASPSP 5.9% '21s, GUOLSP 4.6% PERP, GUOLSP '19s and GUOLSP '20s. While higher prices have vindicated the aggressive bids, developers with higher leverage may have less room to maneuver in the event that units do not move. We think that bond yields of the higher-levered developers should widen and provide closer to equity-like returns[1] given their 1) high net gearing levels

[1] As a reference, we note that the bonds of single 'B' rated Chinese property companies are trading around 7-8% yield (USD)

and 2) substantial encumbered debt. That said, if the Singapore economy and property market continues to remain rosy, we see the potential for several of the higher levered developers' credit profile to improve (which may lift bond prices) when the units are monetized and the cashflows are used to deleverage.

We recommend an Overweight for the FPLSP curve, OUE curve and HTONSP curve, which we think are in the sweet spot as they have more moderate net gearing levels while providing still decent spreads. We are largely Neutral on the larger developers as their lower net gearing levels commensurate with their thinner spreads.

Analyst Declaration
The analyst(s) who wrote this report and/or her or his respective connected persons held securities in the following above-mentioned issuers or companies as at the time of the publication of this report: GuocoLand Ltd

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