Asia Credit Research

Earnings Review: CapitaLand Ltd ("CAPL")

Issuer Profile:
Neutral (3)

Ticker: **CAPLSP**

Background

CapitaLand Ltd ("CAPL") is Singapore's leading real estate developer, operating across residential development, serviced residences, retail & office REITs and real estate fund management. Geographical segments include CL Singapore, Malaysia and Indonesia ("CLSMI"), CL China ("CLC"), CL Vietnam ("CLV") and CL International ("CLI"). CAPL reported SGD62.5bn in total assets as at 2Q2018 and it is 40.3%-owned by Temasek Holdings Ltd.

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Recommendation

- Without the consolidation of REITs which drove the largest y/y changes to revenue and net profit, CAPL's results appear decent still with higher handover of units from China. Although the residential pipeline in Singapore has largely depleted, we expect results to continue to be sustained, with further sales and handover of units in China as well as recurring income from its investment properties and holdings in REITs.
- With net gearing remaining stable q/q at 50%, we retain our Neutral (3) Issuer Profile on CAPL. The acquisitions of sites in China thus far, while sizeable, remain manageable though net gearing may drift higher if further land banking persists.
- We think that CAPLSP 4.35% '19s and CAPLSP 4.3% '20s look rich, preferring a switch to CITSP 3.78% '24s. The remainder of the CAPLSP curve looks fair though we again prefer the CITSP curve given higher yields while we rate City Developments Ltd with a stronger Issuer Profile of Positive (2).

Relative Value:

Bond	Maturity/Call date	Net Gearing	Ask Yield	Spread
CAPLSP 4.35% '19	31/10/2019	50%	2.30%	50bps
CAPLSP 4.3% '20	31/08/2020	50%	2.62%	67bps
CAPLSP 3.8% '24	28/08/2024	50%	3.18%	89bps
CAPLSP 3.08% '27	19/10/2027	50%	3.36%	89bps
CCTSP 2.96% '21	13/08/2021	43%	2.78%	73bps
CCTSP 3.17% '24	05/03/2024	43%	3.09%	84bps
CCTSP 3.327% '25	21/03/2025	43%	3.24%	92bps
CITSP 3.00% '20	27/10/2020	22%	2.67%	70bps
CITSP 3.78% '24	21/10/2024	22%	3.26%	97bps
CITSP 3.48% '26	15/06/2026	22%	3.49%	110bps

Indicative prices as at 16 Aug 2018 Source: Bloomberg
Net gearing based on latest available quarter

Key Considerations

- **Stronger topline mainly driven by REITs consolidation**: 2Q2018 revenue increased 35.3% y/y to SGD1.3bn, mainly due to the consolidation of revenue (since Aug 2017) from its REITs which include CapitaLand Mall Trust ("CMT") (SGD171.4mn), CapitaLand Retail China Trust ("CRCT") (SGD56.3mn) and RCS Trust (SGD22.9mn), while we note that Ascott Residence Trust and CapitaLand Commercial Trust are already consolidated. Without the consolidation from CMT, CRCT and RCS Trust, we estimate that revenue would have increased just 10.0% y/y to SGD1.09bn, with higher handover of units in China and rental revenue from newly opened properties in Singapore, China and Germany. As a result of higher revenue and higher revaluation gains of SGD620.1mn (2Q2017: SGD422.9mn), reported EBIT rose 36.6% y/y to SGD1.35bn (2Q2017: SGD989.4mn) and net profit increased 32.9% y/y to SGD1.08bn.

- **Running lower on Singapore landbank, which is not a bad thing**: CLSMI segment rose 27.6% y/y, which similar to overall revenue trends was due to the consolidation of the REITs. Excluding the consolidation, CAPL reported that revenue would have been lower due to lower residential revenue in Singapore as projects are progressively fully sold – 99% of launched projects were sold as of end June 2018. In 2Q2018, only 37 units were sold (2Q2017: 103 units sold) for SGD136mn (2Q2017: SGD289mn). The main landbank left would be Pearl Bank Apartments, which was acquired under a collective sale for SGD929.4mn (including lease top-up), with target completion of the acquisition in 4Q2018. We think it is not a bad thing that CAPL has only a small pipeline to Singapore residential property as we are wary going into 2019 given the upcoming supply and rise in interest rates. Meanwhile, CAPL is more active on the investment properties front with Jewel Changi Airport (GFA: 134,059 sqm) on track for completion in 2019 while it is undertaking capital recycling and asset redevelopment through its REITs, which we discussed in the earnings review for CapitaLand Mall Trust and CapitaLand Commercial Trust. In total, CLSMI contributed SGD722.2mn EBIT in 2Q2018, higher than revenue due to revaluation gains from investment properties.

- **Turning up the focus on China**: CAPL announced two significant China acquisitions totalling RMB7.75bn (~SGD1.60bn), in June 2018 and earlier this month. Thus far, y/y handover of units has surged to 1,486 units in 2Q2018 (2Q2017: 1,108 units) though sales value plunged to RMB2.2bn (2Q2017: RMB3.2bn) due to lower ASPs. However, revenue for CLC still grew 40.2% y/y to SGD588.0mn, mainly due to the contribution from projects at its subsidiaries and consolidation of CRCT. Going forward, CAPL guided that more than 4,000 units would be handed over in the next 6 months, which we estimate to have a value of RMB8bn (though we note that 3,089 units expected to be completed in 2H2018 are due to La Botanica, which CAPL only holds a 38% effective stake). Thus far, 97% of launched units were sold as of end-June 2018 with new launches deferred in view of tighter government measures. Reported EBIT for the segment increased 18.9% y/y to SGD526.6mn, mainly due to higher fair value gains and consolidation of CRCT.

- **FX and one-offs offset the growth from CLI**: Revenue surged 46.1% y/y for CLI mainly due to contribution from Synergy Global Housing (acquired Jul 2017) and acquisition of two properties in Germany. However, reported EBIT declined 2.9% y/y to SGD84.8mn mainly due to foreign exchange loss incurred and absence of divestment gains of ART's 18 rental housing properties in Japan in 2Q2017.

- **Stable credit metrics**: Net gearing inched up to 0.50x (1Q2018: 0.49x), mainly due to SGD504.1mn dividends paid for the declared full year dividends of 12 cts per share. Reported interest coverage ratio fell to 7.8x (FY2017: 8.2x) though this remains healthy. We continue to expect net gearing to hover around 0.50x still, after the acquisitions in China given the strong operating cashflow (2Q2018: SGD555.0mn).

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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.

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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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