Asia Credit Research

# Earnings Review: Cache Logistics Trust ("CACHE")

**Issuer Profile: Neutral (4)**

Ticker: **CACHE**

**Background**

Cache Logistics Trust ("CACHE") is structured as a real estate industrial trust ("REIT") and listed on the Singapore Stock Exchange ("SGX") with a market cap of ~SGD831mn as at 29 July 2019 with total assets of SGD1.41bn as at 30 June 2019. CACHE focuses on logistics warehouse properties with properties located across Singapore and Australia. ARA Asset Management ("ARA"), who also owns the REIT Manager and Property Manager, holds a 9.6%-stake in CACHE.

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## Recommendation

- CACHE's 2Q2019 revenue was weaker than expected, declining 7.4% y/y and 9.8% on a q/q basis, with EBITDA sliding to SGD18.5mn and resulting in a thinner EBITDA/Interest coverage of 3.9x in 2Q2019 versus 4.2x in 2Q2018 and 4.8x in 1Q2019, not including lease liabilities.
- Admittedly, we were caught unaware that a master lessee at a Singapore property had signal its intention to discontinue its master lease as early as 2Q2019. We think this explains up to ~40% of the q/q revenue decline.
- We are Overweight the CACHE 5.5%-PERP, while this perpetual has an ask yield to call that is 26bps lower than the EREIT 4.6%-PERP and a first call date that is three months later, we still prefer the CACHE 5.5%-PERP as we think this perpetual has a lower risk of non-call at first call.
- We are maintaining CACHE's Neutral (4) issuer profile on the back of its still manageable, albeit weaker credit metrics.
- We may lower CACHE's issuer profile should the situation at CWT SG deteriorate and/or the Singapore warehouse sub-segment deteriorate beyond expectations. We hold a somewhat negative outlook for the Singapore warehouse sub-segment sector for the next 12 months, with rents of this sub-segment declining 0.2% q/q despite a q/q uptick in overall industrial space rentals.

## Relative Value:

| Bond | Call date | Aggregate leverage | Ask Yield to Call | Ask Yield to Maturity | Spread to call (bps) |
|---|---|---|---|---|---|
| CACHE 5.5%-PERP | 01/02/2023 | 37.9% | 5.12% | 5.51% | 347 |
| EREIT 4.6%-PERP | 3/11/2022 | 39.0% | 5.38% | 4.67% | 373 |
| MLTSP 3.65%-PERP | 28/03/2023 | 36.8% | 3.71% | 3.70% | 206 |

*Indicative prices as at 29 July 2019 Source: Bloomberg*
*Aggregate leverage based on latest available quarter; not inclusive of perpetuals as debt*

## Key Considerations

- **Weaker y/y results due to two properties in Singapore and asset divestments:** CACHE's 2Q2019 gross revenue was down 7.4% y/y to SGD27.8mn, driven by lower revenue from Cache Gul LogisCentre (until recently known as Precise Two) which had been converted from a master lease into a multi-tenancy structure (as the original master lessee discontinued), absence of revenue from 40 Alps Avenue sold in May 2018 and Jinshan Chemical Warehouse sold in December 2018 absence of revenue from the sale of 40 Alps Avenue in May 2018 and Jinshan Chemical Warehouse in December 2018 and some downtime at CWT Commodity Hub due to tenant change. This was partly offset by contribution from the Maidstone Street warehouse in Australia bought in April 2019.

- **Fall in q/q results driven by non-renewal of master lease and transitory downtime at Commodity Hub (known as CWT Commodity Hub until 1Q2019):** On a q/q basis, the fall in gross revenue was higher at 9.8%. The only asset movement was the purchase of Maidstone Street warehouse. Based on our estimation, removing the positive contribution from Maidstone Street, CACHE's gross revenue would have fallen 11.6% q/q instead. In our view, the main driver for the q/q fall was due to lower occupancies, especially in Singapore. In 2Q2019, overall committed occupancy for the portfolio was only 90% (86.1% for Singapore and 98.0% for Australia) whereas in 1Q2019, this was 94.8% (92.2% for Singapore and 98.8% for Australia). Post quarter end though, CACHE had managed to bring up overall committed occupancy to 92.6%. The master lessee at the Cache Gul Logis Centre contributed gross revenue of SGD5.4mn in 2018 (SGD1.35mn per quarter) which may explain up to ~40% of the q/q decline based on our estimation, adjusting out the positive impact from Maidstone Street. Transitory downtime at Commodity Hub would explain the rest of the q/q decline.

- **Thinner than expected EBITDA/Interest coverage:** EBITDA (based on our calculation which excludes other income and other expenses) was SGD18.5mn (down 5.7% y/y and down 15.0% q/q), driven by the fall in top line. Interest expense (excluding finance expenses on lease liabilities) was higher at SGD4.7mn, despite lower average debt balance. We think this was mainly due to higher all-in financing cost of 3.86% versus 3.61% in 2Q2018. Resultant EBITDA/Interest coverage was lower at 3.9x (2Q2018: 4.3x and 1Q2019: 4.8x). Perpetuals outstanding was SGD100mn, assuming CACHE fully pays its perpetual distributions, this is SGD5.4mn p.a (SGD1.38mn per quarter) and taking 50% of this as interest, we find EBITDA/(Interest plus 50% perpetual distribution) at 3.4x, still manageable though thinner.

- **Aggregate leverage slightly higher:** As at 30 June 2019, CACHE's reported aggregate leverage was 37.9%, while we estimate that including 50% of perpetual as debt would be 41%, still on the high side versus our coverage universe. Secured debt though is still only 5% of total assets, having improved significantly post 3Q2018. Short term debt as at 30 June 2019 remains manageable at SGD90.0mn, representing 18% of gross debt and is within its historical range.

- **Receivership over CWT Pte Ltd ("CWT SG") possibly lifted:** We think CWT SG is still the largest tenant of CACHE though with contribution to gross rental income declining to 14.8% as at 30 June 2019, falling from 16.5% as earlier disclosed in April 2019. This indicates that CWT SG had reduced its space leased from CACHE (eg: at Commodity Hub). In April 2019, the parent company of CWT SG (namely CWT International Ltd ("CWTI")) defaulted on a loan facility that led to CWT SG being put under receivership (stakes in CWT SG used by CWTI as collateral). At time of writing, CWTI has reached an agreement with the lenders of the facility agreement, with the receivership at CWT SG possibly lifted in the near term. That being said, even assuming the lifting of the receivership, given the stretched liquidity at CWTI, we still consider the credit counterparty risk of this income contribution to be high.

| OCBC Global Treasury | |
|---|---|
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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 |

**Please note that Bond Recommendations are dependent on a bond's price, underlying risk free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.**

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.

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.

We may also suspend our issuer rating and bond level recommendation in the ordinary course of business if (1) we believe the current issuer profile is incorrect and we have incomplete information to complete a review; or (2) where evolving circumstances and increasingly divergent outcomes for different investors results in less conviction on providing a bond level recommendation.

**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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