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 SGD64.6bn in total assets as at 4Q2018 and it is 40.4%-owned by Temasek Holdings Ltd.

Wong Hong Wei, CFA
+65 6722 2533
wonghongwei@ocbc.com

Recommendation

- CAPL reported good 4Q2018 results which showed a healthy 34% y/y revenue increase to SGD1.62bn with reported PBT rising 62.3% y/y to SGD964.0mn. The rise in contribution from China and International has more than mitigated the dry development landbank in Singapore.
- Net gearing rose q/q to 55.8% (3Q2018: 50.5%) due to acquisitions. Net gearing may continue to increase to ~70% post the acquisition of Ascendas Pte Ltd and Singbridge Pte Ltd. While CAPL targets to cut net gearing to 0.64x by Dec 2020 through asset recycling and cash from operations, this will have to be balanced against the target to achieve a ROE that exceeds cost of equity.
- We prefer switching into the CITSP curve given that City Developments Ltd ("CDL") has a lower net gearing, though both CAPL and CDL are on a leveraging path. Investors looking for rated papers can consider the CCTSP curve.

Relative Value:

Bond	Maturity/Call date	Net Gearing	Ask Yield	Spread
CAPLSP 4.35% '19	31/10/2019	56%	2.24%	26bps
CAPLSP 4.3% '20	31/08/2020	56%	2.62%	65bps
CAPLSP 3.8% '24	28/08/2024	56%	3.18%	112bps
CAPLSP 3.08% '27	19/10/2027	56%	3.43%	120bps
CCTSP 2.96% '21	13/08/2021	35%	2.70%	73bps
CCTSP 3.17% '24	05/03/2024	35%	3.04%	101bps
CCTSP 3.327% '25	21/03/2025	35%	3.20%	111bps
CITSP 3.00% '20	27/10/2020	33%	2.75%	78bps
CITSP 3.78% '24	21/10/2024	33%	3.15%	109bps
CITSP 3.48% '26	15/06/2026	33%	3.39%	123bps

Indicative prices as at 27 Feb 2018 Source: Bloomberg
Net gearing based on latest available quarter

Key Considerations

- **Strong results from higher sales and rental revenue…:** CAPL announced 4Q2018 results, which show clearer underlying trends as prior quarter results were distorted by the consolidation of revenue (since Aug 2017) from its REITs. 4Q2018 revenue rose 34% y/y to SGD1.62bn with higher handover of units from residential development in China (+86.9% y/y to RMB4.8bn) and rental revenue from acquisitions overseas, including that in USA (16 multifamily properties which cost USD835mn) and Germany (by 30%-owned CapitaLand Commercial Trust, which acquired Gallileo, a Grade A office building which cost SGD548.3mn). On the back of stronger revenue, net profit rose 44.6% y/y to SGD708.5mn.

- **…with contribution mainly from outside Singapore**: As a proportion, segments other than CL SMI (which comprises mainly Singapore) saw revenue grow 71.2% y/y to SGD1.07bn, which accounts for 66% of CAPL's total revenue.
  - **i)** CL SMI: Revenue fell 5.8% y/y to SGD551.9mn as the development landbank in Singapore has been drying up. However, reported EBIT for the segment rose 7.2% y/y to SGD342.0mn due to higher writeback of impairment for residential projects upon sale of units.
  - **ii)** CL China: Revenue rose 105.5% y/y to SGD759.6mn with reported EBIT higher by 76.6% y/y to SGD774.1mn with 2,764 units handed over from residential projects (4Q2017: 2,156 units).
  - **iii)** CL Vietnam: Revenue rose 124.1% y/y to SGD52.2mn with the handover of units from subsidiaries' project though reported EBIT fell to a negative SGD12.9mn (4Q2017: SGD34.4mn) due to FX losses, which materialised upon the divestment of a project.
  - **iv)** CL International: Revenue rose 22.1% y/y to SGD289.5mn with reported EBIT rising to SGD68.7mn (4Q2017: negative SGD14.6mn) due to the

acquisition of the multifamily properties.

- **Development revenue may remain volatile though we are not overly worried:** Despite the strong results bolstered by higher contribution from the development front, the contribution can swing the other way given the volatility of the development pipeline. In China, residential sales have fallen to RMB12.5bn (2017: RMB15.8bn). The soft results may persist in the short term as CAPL has been deferring launches due to tight government measures (e.g. price caps). In Singapore, CAPL is no longer really positioned as a property developer with residential sales plunging to SGD371mn (2017: SGD1.5bn) with launched projects already substantially sold and the pipeline in Singapore is not sufficiently replenished. That said, CAPL's results will be underpinned by investment properties (which forms 79% of total assets as of end-2018).

- **Credit profile anchored by strong recurring income which looks set to grow**: Without factoring in portfolio gains and revaluation gains, CAPL recorded SGD2.0bn in operating reported EBIT in 2018 from recurring sources (retail, commercial, lodging). This has already outweighed reported EBIT of SGD838.3mn from residential and commercial strata. Aside from the acquisitions in 2018, recurring income looks set to grow with retail portfolio expanding from the opening of Jewel Changi Airport (GFA: 134,059 sqm) and Funan in 1H2019 and CapitaSpring joining the Singapore Grade A office market in 2021. Meanwhile, we expect CAPL's listed REITs to contribute ~SGD320mn dividends p.a. to CAPL.

- **Credit metrics to weaken due to significant acquisitions:** Net gearing rose q/q to 55.8% (3Q2018: 50.5%) due to cash outflows for (1) acquisition of Pearl Bank Apartment site (SGD677.4mn) in Singapore, (2) deposits placed for acquisition of residential sales in China and (3) SGD1.39bn used for acquisition of 16 multi-family properties in USA, as well as acquisitions in China and Indonesia. We continue to expect net gearing to increase to over 70%, mainly due to the proposed acquisition of Ascendas Singbridge with an enterprise value of SGD10.9bn and the acquisition of Pufa Tower in China. If we exclude the REITs from the balance sheet (noting that ~SGD13bn of minority interests that contribute to total equity of SGD33.3bn are due to listed REITs), we estimate that net gearing of CAPL standalone (less listed REITs) may exceed 1x upon the acquisition of Ascendas Singbridge. That said, we note that CAPL continues to benefit from recurring income from its investment properties. Meanwhile, reported interest coverage ratio remains healthy at 8.3x (2017: 8.6x) with a well staggered debt maturity profile.

OCBC Global Treasury	
Treasury Advisory **Corporate FX & Structured Products** Tel: 6349-1888 / 1881 **Interest Rate Derivatives** Tel: 6349-1899 **Investments & Structured Products** Tel: 6349-1886 **GT Institutional Sales** Tel: 6349-1810	**Credit Research** **Andrew Wong** +65 6530 4736 WongVKAM@ocbc.com **Ezien Hoo, CFA** +65 6722 2215 EzienHoo@ocbc.com **Wong Hong Wei, CFA** +65 6722 2533 wonghongwei@ocbc.com **Seow Zhi Qi** +65 6530 7348 ZhiQiSeow@ocbc.com

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 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.

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.

Analyst Declaration
The analyst(s) who wrote this report and/or her or his respective connected persons did not hold financial interests in the above-mentioned issuer or company as at the time of the publication of this report.

Co.Reg.no.:193200032W