Issuer Profile:
Neutral (4)

Ticker:
KREITS

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Keppel REIT ("KREIT")

Recommendation

- **Results for 9M2019 were weak, though 3Q2019 saw y/y improvements on the back of full quarter results from T Tower (acquired in May 2019) with adjusted NPI higher by 2.9% y/y to SGD29.0mn.**
- **Post 3Q2019, KREIT had divested Bugis Junction Towers in Singapore for SGD547.5mn in Oct and completion is scheduled for 4Q2019. Although the sale will realise capital gains of SGD378.1mn, we expect the top line figures of KREIT to shrink given the absence of contributions from the property. That said, lease at newly constructed 311 Spencer Street in Melbourne which KREIT has a 50% stake in is estimated to commence in 2Q2020, two quarters after the above-mentioned divestment.**
- **Reported aggregate leverage inched higher to 38.9% from 38.4% in the preceding quarter, though lower relative to a year ago (3Q2018: 39.1%). Reported EBITDA/Interest was 3.8x (2Q2019: 3.7x, 3Q2018: 4.0x). KREIT does not have any borrowings coming due in 2019. For 2020, KREIT has SGD637mn of bank loans maturing, which we think will be manageable as it has SGD100.5mn of cash on hand and will receive SGD547.5mn from divestment of Bugis Junction Towers for in the next quarter. In addition, KREIT's assets are 73% unencumbered. We are maintaining KREIT at Neutral (4) Issuer Profile.**
- **We are Overweight on KREITS 4.98% PERP and Neutral on the bullets – KREITS 3.15% '22s and KREITS 3.275% '24s. Comparatively, we think that the perp offers better value.**

Bond	Outstanding Amount	Maturity	Aggregate Leverage	Ask Yield	Spread
KREITS 3.15% '22	SGD50mn	11/02/2022	38.9%	2.66%	126bps
KREITS 3.275% '24	SGD75mn	08/04/2024	38.9%	2.89%	139bps
KREITS 4.98% PERP	SGD250mn	02/11/2020	38.9%	2.89%	148bps

Indicative prices as at 12 Nov 2019 Source: Bloomberg
Aggregate leverage based on latest available quarter

Background

- Listed on the Singapore Exchange on 28 Apr 2006, KREIT's portfolio comprises interests in ten office assets located in the central business districts of Singapore, Australian cities – Sydney, Melbourne, Brisbane and Perth, as well as Seoul, South Korea.
- Assuming Bugis Junctions Towers was divested on 30 Sep 2019, total asset under management would be SGD7.9bn as at 30 Sep 2019 (Singapore: 81%, Australia: 15%, South Korea: 4%).
- KREIT is 43.5% owned by Keppel Land Ltd, it's Sponsor.
- Key assets are Ocean Financial Centre ("OFC", 79.9% interest), Marina Bay Financial Centre ("MBFC", 33% interest) and One Raffles Quay ("ORQ", 33% interest).

Key Considerations

- **Newly acquired South Korea property provides support:** 9M2019 revenue was down by 4.5% y/y to SGD122.3mn while 9M2019 net property income ("NPI") was down by 6.9% y/y to SGD95.5mn. Although KREIT reported a 15.6% y/y increase in revenue to SGD42.4mn from SGD36.7mn and a 17.6% y/y gain in net property income ("NPI") to SGD33.2mn from SGD28.2mn in 3Q2019, this was before adjusting out NPI attributable to minority investors. Excluding the 20.1% stake in OFC which was divested in Nov 2018 and consolidated into its financial statements, we find adjusted NPI higher by just 2.9% y/y at SGD29.0mn instead. This was largely driven by T Tower (acquired on 27 May 2019) where full quarter results were consolidated in 3Q2019.

- **Divestment of Bugis Junction Towers, Singapore:** Post 3Q2019, KREIT had on 1 Oct 2019 sold Bugis Junction Towers in Singapore for SGD547.5mn (SGD2,200 psf). Completion is scheduled for 4Q2019. Over 9M2019, the property contributed to 12.1% of total portfolio NPI (i.e.

SGD11.6mn). Although the sale will realise capital gains of SGD378.1mn based on the difference between the sale price and purchase price, after taking into consideration capitalised expenditures and divestments costs, we expect the top line figures of KREIT to shrink given the absence of contributions from the property. We think how KREIT deploys the gains from the transaction will be crucial.

- **311 Spencer Street in Melbourne has topped out:** The structure of the 40-storey office tower was completed on 19 Aug 2019 and is in the midst of fitting out. 311 Spencer Street which KREIT has a 50% stake in will be fully leased to the Victoria Police for 30 years. The lease is expected to commence in 2Q2020, and includes a market rent review at the commencement of Year 16 subject to a cap and collar, and options to review for three additional terms of 5 years each. While new contributions from 311 Spencer Street may be able to offset the absence of contributions from Bugis Junction Towers, there seems to be a timing mismatch as the new contributions are only expected to come in two quarters after the divestment. Having said that, the lease at the property will nevertheless contribute a steady income stream to KREIT.

- **Contributions from MBFC, Singapore grew:** Although KREIT accounts for its stake in MBFC via share of results of associates, we estimate that MBFC will make up ~29% of total portfolio adjusted NPI (which excludes contributions of Bugis Junction Towers and NPI attributable to minority investors, and includes contributions of associates and joint ventures), behind OFC which contributes ~33%. 9M2019 contributions from MBFC rose 10.6% y/y to SGD43.7mn (3Q2019: +27.3% y/y). We note that these contributions do not include rental support (which has ceased since 2Q2019) and interest income relating to the MBFC. As at 30 Sep 2019, MBFC is 99.0% occupied, above the average occupancy in core CBD of 96.0%.

- **Portfolio statistics remains healthy:** Overall portfolio committed occupancy was 98.9%, up from 98.0% a year ago, with a weighted average lease expiry of 5.1 years. In 2020, KREIT will see 8.3% of leases based on net lettable area expire and 3.6% up for rent review (11.9% in total). 9.8% of which will come from its Singapore portfolio. We think this is very manageable and KREIT has much room lock in higher rents as the average signing rents for its Singapore properties was SGD12.35 psf pm in 9M2019, above the average expiring rents of Singapore office leases of SGD9.59 psf pm in 2020. Over the year, KREIT has also diversified its tenant base further by increasing the number of tenants to 355 from 340 in 3Q2018 as well as the percentage of NLA the top 10 tenants occupy to 37.2% from 40.2% in 3Q2018.

- **Manageable credit metrics:** Reported aggregate leverage inched higher to 38.9% from 38.4% in the preceding quarter, though lower relative to a year ago (3Q2018: 39.1%). This was due to marginally lower deposited property value and slightly higher borrowings. All-in interest rate was 2.82% (2Q2019: 2.86%, 3Q2018: 2.80%) while reported EBITDA/Interest was 3.8x (2Q2019: 3.7x, 3Q2018: 4.0x). KREIT does not have any borrowings coming due in 2019. For 2020, KREIT has SGD637mn of bank loans maturing. We think this will be manageable for KREIT as it has SGD100.5mn of cash on hand and is looking to complete the divestment of Bugis Junction Towers for SGD547.5mn in the next quarter. Should the funds received from the divestment be used to pay down its debt, we see the resultant aggregate leverage at 34.6%. Separately, we note that KREIT's assets are 73% unencumbered. We are maintaining KREIT at Neutral (4) Issuer Profile.

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

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.

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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