OCBC Bank

Issuer Profile:

Neutral (4)

Ticker:

SPHRSP

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SPH REIT ("SPHR")

Issuer Profile	Bond Recommendation	
Neutral (4)	**SPHRSP 4.1% PERP**	**Neutral**
Fundamental Analysis Consideration ▪ Recovering industry outlook ▪ Manageable lease expiry profile ▪ Good access to bank debt and increasingly, capital markets ▪ Lower aggregate leverage relative to peers but significant encumbered assets	**Technical Analysis Consideration** ▪ Decent yield relative to its peers ▪ High probability of being called at first call at this point ▪ Lack of external credit rating by international rating agencies	

Summary

- SPH REIT ("SPHR") is a real estate investment trust ("REIT") listed on the SGX, focusing on investing in retail real estate in the Asia-Pacific region. SPHR has a portfolio of five assets in Singapore and Australia. SPHR is Sponsored by Singapore Press Holdings Ltd ("SPH"), where SPH is also SPHR's largest unitholder holding a ~66%-stake.
- The impact of the pandemic was largely captured in 2HFY2020. Following the gradual loosening of rules surrounding gathering in groups and the re-opening of Singapore's economy, we expect SPHR to benefit through higher footfall and tenants' sales.
- Credit metrics are highly manageable with EBITDA/Interest at 7.7x (6.2x if we include 50% perpetual distributions) in the first half of the financial year ended February 2021 ("1HFY2021"). SPHR does not have any debt maturing in the remaining of FY2021 except for a SGD50mn loan which will be refinanced in due course. While SPHR has been acquiring assets in Australia, its portfolio remains concentrated in Singapore. SPHR has a relatively healthy portfolio occupancy of 98.0% as at 28 February 2021.

Per SPH's annual report for the financial year ended August 2020 ("FY2020"), as at 7 October 2020, the Great Eastern Life Assurance Company Limited ("Great Eastern") and Oversea-Chinese Banking Corporation Limited ("OCBC Bank") owns 22.6% and 16.8% of SPH's management shares respectively. OCBC Bank holds an ~88%-stake in Great Eastern, as such OCBC Bank's effective interest in SPH is ~36.8%. We note that each ordinary share is entitled to one vote while each management share is entitled to 200 votes. More information on SPH is available here.

I) Company Background

SPH REIT ("SPHR") is a Singapore-based Real Estate Investment Trust established to invest in real estate for retail purposes. SPHR has been listed on the Singapore Stock Exchange ("SGX") since 24 July 2013 and has a market capitalization of SGD2.4bn as at 1 April 2021. Sponsor and major shareholder, Singapore Press Holdings Ltd ("SPH"), is a media organization (sole provider of print newspapers in Singapore) with real estate as a key business segment.

SPHR has a portfolio of three properties in Singapore – Paragon, The Clementi Mall and The Rail Mall, and interest in two properties in Australia – 85% stake in Figtree Grove Shopping Centre in Wollongong, New South Wales and 50% interest in Westfield Marion Shopping Centre in Adelaide. Total property valuation was SGD4.1bn as at 31 August 2020 (Singapore: 80%, Australia: 20%). SPHR had two properties in its portfolio at initial public offering, and subsequently acquired The Rail Mall on 28 June 2018 and its stake in Figtree Grove on 21 December 2018. At end-2019, SPHR acquired 50% stake in Westfield Marion.

SPH REIT Management Pte Ltd is the REIT manager. SPH Retail Property Management Services Pte. Ltd. is the property manager of the Singapore properties. Both are wholly owned subsidiaries of SPH.

II) Management & Ownership

Dr Leong Horn Kee is the Chairman of SPHR. Dr Leong is also the Chairman of CapitalCorp Partners Private Limited, a corporate finance advisory firm. He is currently Singapore's non-resident High Commissioner to Cyprus. Dr Leong was an executive director of Far East Organization, Chief Executive Officer ("CEO") of Orchard Parade Holdings Ltd and CEO of Yeo Hiap Seng Ltd from 1994 to 2008. He was a deputy director at the Ministry of Finance and Ministry of Trade & Industry from 1977 to 1983 and a Member of Parliament for 22 years from 1984 to 2006.

Ms Susan Leng Mee Yin, CEO of SPH REIT Management Pte Ltd since 2013, has 16 years of experience in shopping centre management and property development and eight years of accounting and finance experience prior to the appointment. Ms Leng was also the General Manager of Orchard 290 Ltd, a wholly owned subsidiary of SPH, from 1997 to 2004. She was a pioneer member of the management team which redeveloped Paragon and The Promenade into one fully integrated premier upscale retail mall with a medical and office tower.

Mr Benjamin Kuah was appointed Chief Financial Officer and Head of Investor Relations of SPH REIT Management Pte. Ltd. in January 2019. Mr Kuah was the Group Financial Controller of Nanshan Group Singapore from 2016 to 2018 where he was responsible for the group's real estate business and property development projects in Singapore.

Figure 1: Major Unitholders as at 31 August 2020

Unitholder	Shares	Deemed interest
Singapore Press Holdings Ltd ("SPH")	1,823,886,304	66.01%
National Trade Union Congress	137,926,000	4.96%

Source: Annual Report 2020, Bloomberg

SPH, Sponsor of SPHR, is the largest unitholder with ~66% stake in SPHR. The National Trade Union Congress has a ~5% stake and the remaining unitholders holding the remaining ~29% stake held by the public, comprising institutional and retail investors.

SPH has announced on 30 March 2021 that it is undergoing a strategic review to consider options for its various businesses. SPH's Media business continues to face a challenging operating environment and outlook and the Board of Directors believes that SPH remains undervalued and the objective of the strategic review is to unlock and maximize long term shareholder value. That said, changes to shareholdings on SPH may be constrained due to the Newspaper and Printing Presses Act, which requires the approval of the Minister to become a substantial shareholder of SPH.

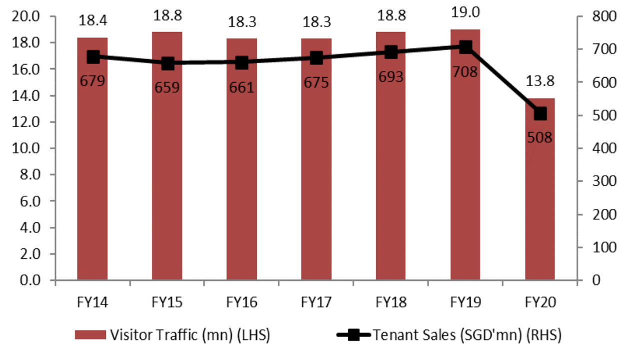
III) Portfolio Overview & Analysis

Paragon

A premier upscale retail mail and medical suite/office property located in the heart of Orchard Road, Singapore with net lettable area of 717,855 sq ft. Paragon is one of the handful of shopping malls in Singapore who has an entrenched position in the luxury retail segment. That said, Paragon also has exposure to department stores such as Metro. Uniquely, Paragon houses Paragon Medical that hosts ~90 medical and dental specialist clinics and offices. These specialist clinics provide medical services, among which include cardiology, orthopedics, urology, dermatology, obstetrics, gynecology, oncology, pediatrics, dentistry, anti-ageing, and traditional Chinese medicine. It focuses on targeting medical tourists, and the higher end of the local market. Paragon Medical is strategically located in Orchard Road and within the Mount Elizabeth medical cluster anchored by renowned healthcare establishments in Asia, Mount Elizabeth Hospital and Mount Elizabeth Medical Centre.

Paragon itself is a freehold property, and is owned by Orchard 290 Ltd, a wholly owned subsidiary of SPH and leased to SPHR on a 99-year leasehold basis at the REIT's listing date. The 99-year leasehold interest was sold to SPHR at IPO of SPHR. As at 28 February 2021, Paragon has an occupancy rate of 97.1%, slightly lower than a year ago (2019: 99.9%). In February 2021, tenant's sales have exceeded that of February 2020 while there was no disclosure on footfall. At the peak of the pandemic in Singapore, visitor traffic fell as much as ~59% y/y at Paragon between March and May 2020 (i.e. 3QFY2020). Lease expiry in FY2021 make up 13% of its gross rental income. Paragon recorded positive rental reversion of 1.3% for the leasing activities done in 1HFY2021 (21.0% of its property's NLA). Gross revenue fell 8.0% y/y to SGD81.8mn with net property income down 10.7% y/y to SGD63.2mn over 1HFY2021. As business activities return to normal in Singapore, we would expect the performance of Paragon to recover. That said, Paragon may take more time to fully recover as tourists (including medical tourists) which is an essential component of Paragon's patrons are unable to enter and exit Singapore without serving a stay-home-notice period for the time being.

Figure 2: Performance of Paragon



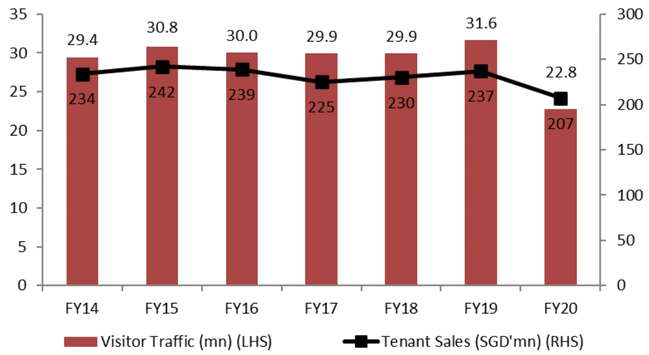
Source: Company

The Clementi Mall

The mall located on the west of Singapore, is a five-storey retail podium with 195,229 sq ft of retail NLA and 290,342 sq ft of GFA. It is a family-oriented mall that is directly linked to the Clementi MRT station and a bus interchange and is surrounded by blocks of residential units. Its location draws visitors to the retail mall regularly and brings about very strong footfall.

Clementi Mall is owned by CM Domain Pte Ltd which is a joint venture by SPH's wholly-owned subsidiary – Times Properties Pte Ltd (60%), NTUC Fairprice Co-operative Ltd (20%) and NTUC Income Insurance Co-operative Ltd (20%). The mall has a 99-year leasehold tenure commencing on 31 August 2010. Clementi Mall was 100% occupied as at 28 February 2021 (2019: 100%). Rental reversion at -7.8% in 1HFY2021 where 8.2% of the property's NLA was renewed or leased. In FY2021, just 1% of the leases by gross rental income would be expiring. Clementi Mall's tenants' sales in February 2021 have slightly exceed that of February 2020 while there is no disclosure on footfall. Both gross revenue and net property income for Clementi Mall only fell y/y in 1HFY2021 by 3.5% and 3.0% respectively.

Figure 3: Performance of Clementi Mall



Source: Company

The Rail Mall

The property is a retail strip with ~360 metres of main road frontage to Upper Bukit Timah Road, Singapore, comprising 43 single-storey shop units and 95 private carpark lots. It is on a 99-year lease which will expire in 2046 (25 years away). The Rail Mall is fully occupied as at 28 February 2021 (2019: 92.2%). There are no leases expiring in the remaining of FY2021. We note that SPHR has settled leases making up 12.1% of property's NLA at a positive rental reversion of 5.4% in 1HFY2021. The Rail Mall generated SGD2.8mn revenue (+9.7% y/y) and SGD2.3mn net property income (+14.9 y/y) in 1HFY2021. The mall was acquired on 28 June 2018 for SGD63.2mn from Pulau Properties, a related party(?). Pulau Properties is owned by the Lee Foundation (founded by the late Mr Lee Kong Chian) and members of the Lee family. The transaction was funded by ~71% debt and ~29% cash. Assuming flat net property across the lease tenure of the property, the Rail Mall may potentially generate ~SGD100mn net property income in total throughout its balance lease tenure. As at 30 August 2020, the Rail Mall was valued at SGD62.2mn (-2.5% y/y).

Figtree Grove Shopping Centre

Located in Wollongong, New South Wales, Australia, the mall sits on a freehold land area of 552,898 sq ft and has a gross lettable area of 236,678 sq ft. It is an established sub-regional shopping centre which focuses on non-discretionary spending with its anchor tenants being supermarkets – Coles and Woolworths and departmental stores – Kmart.

SPHR acquired an 85% stake in the shopping centre on 21 December 2018 for a total acquisition cost of AUD188.2mn (SGD188.2mn) (property price was AUD175.1mn (SGD175.1mn)) from an unrelated third-party, Swordfish Australian Mid TC Pty Ltd ("Swordfish"). The balance 15% stake is held by entities managed by the asset management division of Moelis Australia Ltd. NPI yield was ~5.7% after taking into account the transaction costs. SPHR receives rental guarantee from Swordfish capped at AUD800k up till 21 December 2019. As of writing, this rental guarantee has expired.

The property has an occupancy rate of 97.9% as at 28 February 2021 (2019: 99.2%), with rental reversion of 2.3% of property NLA at -9.8% in FY2020. Figtree Grove will see 9% by NLA expire in the remaining of FY2021. Bulk of the expiry leases by NLA (64% of total) is in FY2025 and beyond. In February 2021, tenants' sales appear to have lagged that of the same period a year ago slightly though the amount was not disclosed. The property generated SGD8.5mn revenue (+4.2%y/y) and SGD6.6mn net property income (+5.0%y/y) in 1HFY2021.

Westfield Marion

Westfield Marion is the largest shopping centre in South Australia with gross lettable area of 1,472,125 sq ft. It is a freehold property located ~10km south west of Adelaide's Central Business District. The mall is anchored by three departmental stores – David Jones, Myer and Harris Scarfe, three supermarkets – Aldi, Coles and Woolworths, three discount departmental stores – Big W, Kmart and Target.

SPHR acquired a 50% interest in Westfield Marion on 6 December 2019 from an unrelated third party, Lendlease Real Estate Investments Limited for a total acquisition cost of AUD691.3mn (SGD656.7mn). The purchase consideration was AUD670.0mn (SGD636.5mn) while the independent valuation of a 50% interest in the mall was AUD679.5mn (SGD645.5mn) on 6 August 2019. SPHR funded the acquisition with a combination of proceeds from the SGD300mn of perpetual securities issued on 30 August 2019, the SGD162.4mn raised from the private placement of units and SGD190.0mn of bank debt. Assuming perpetual securities as debt, this roughly translates to 75% debt and 25% equity. As at 31 August 2020, the 50% interest in Westfield Marion was valued at AUD646.5mn. This translates to a 4.9% decline in valuation since the property was valued by an independent valuer prior to acquisition on 6 August 2019 and a 3.5% decline from the purchase consideration.

Scentre Group Limited ("Scentre", Issuer profile: Positive (2)), the largest Australian Retail REIT, owning and operating Westfield in Australia and New Zealand, was already the co-owner of Westfield Marion, leading to a tenancy in common arrangement between Scentre and SPPHR. As such, SPHR's 50% interest in Westfield Marion was accounted for as a joint operation where SPHR recognizes its assets, liabilities, revenue, and expenses in relation to its interest in the joint operation. Westfield Marion is managed by Scentre.

The property has an occupancy rate of 97.9% as of 28 February 2021 (At acquisition in December 2019: 99.3%). Westfield Marion will see 15% by NLA expire in the remaining of FY2021. Tenants' sales have recovered substantially and is marginally lower than that of February 2020 in February 2021. The property generated SGD26.4mn revenue and SGD17.2mn net property income in 1HFY2021.

Figure 4: Portfolio of Assets

Property	Location	Interest	Lease Tenure	Valuation as at 31 Aug 2020 (SGD'mn)
Paragon	Singapore	100%	99-year lease commencing 24 July 2013	2,640.0 (-3.8%y/y)
Clementi Mall	Singapore	100%	99-year lease commencing on 31 August 2010	584.0 (-2.2%y/y)
The Rail Mall	Singapore	100%	99-year lease commencing on 18 March 1947	62.2 (-2.5%y/y)
Figtree Grove	Wollongong, NSW, Australia	85%	Freehold	190.6[1] (-7.5%y/y)
Westfield Marion	Adelaide, Australia	50%	Freehold	648.6[2] (-4.9%y/y)

Source: Company
[1] Based on 100% interest
[2] Based on 50% interest

IV) Business Consideration

- **Highly concentrated to Paragon:** SPHR's assets are predominantly located in Singapore (80% Singapore exposure, 20% Australia exposure by valuation) with Paragon alone accounting for 64% of SPHR's total portfolio valuation and 80% of the Singapore portfolio valuation. In 1HFY2021, Paragon contributed 58% to the REIT's total revenue. Though Paragon used to contribute to as much as 75% of the REIT's total revenue, prior to its acquisition of Westfield Marion on 6 December 2019, Paragon continues to be key to SPHR. By gross rental income, 'Luxury Brands, Jewelry & Watches' trade segment contribute the most at 34% even though it takes up just 12% of the net lettable area of the property in FY2020. Paragon Medical, on the other hand, take up 32% of the net lettable area but contribute 19% to gross rental income. At the peak of the pandemic in Singapore, visitor traffic fell as much as ~59% y/y at Paragon between March and May 2020 (i.e. 3QFY2020). In February 2021, tenant's sales have exceeded that of February 2020 while there was no disclosure on footfall. As at 28 February 2020, Paragon has an occupancy rate of 97.1%, slightly lower than a year ago (2019: 99.9%). Nonetheless, as further re-opening of the economy and loosening of restrictions take place, allowing business activities to return to normal in Singapore, we would expect the performance of Paragon too recover. That said, Paragon may take more time to fully recover as tourists (including medical tourists) which is an essential component of Paragon's patrons are unable to enter and exit Singapore without quarantine for the time being.

- **Paragon Medical is a plus for Paragon:** Paragon Medical houses some 90 medical specialists and caters to medical clients and medical tourists. Paragon Medical also benefits from being near five-star accommodations, making it very convenient for medical tourists. We view patrons at Paragon for medical services as a separate group from regular shoppers given that the motive of their visit is different. Though we expect this group of clients to be more resilient than regular shoppers along the Orchard Road shopping belt, they are likely to come from the region and are significantly impacted by the travel restrictions put in place amid the pandemic. Lease expiry for the remaining of FY2021 make up 13% of its gross rental income. Paragon recorded positive rental reversion of 1.3% for the leasing activities done in 1HFY2021 (21.0% of its property's NLA). Retention rate was 84.3% in FY2020. We note that medical tenants tend to be sticky because they benefit from clustering and equipment used is often bulky and may require opening of the mall's façade to fit. These factors no doubt deter the medical tenants from moving. In fact, management shared that they think medical tenants are more likely to sell their clinics (along with the equipment) than relocate their equipment. This is positive for Paragon as it suggests medical tenants are likely to be locked-in for as long as their medical equipment remain useful. On clustering, tenants at Paragon Medical also benefit from having hospital (e.g. Gleneagles Hospital and Mouth Elizabeth Hospital) and medical centres (e.g. Camden Medical) in the vicinity. These established medical groups cumulatively form a hub and create positive synergy. Having said that, Paragon Medical differentiates itself from these medical-centric facilities through its complementary and diversified retail and dining options. As such, we think Paragon has a unique and valuable positioning, and this helps to attract and retain its medical tenants.

- **Built on its Australia exposure:** Following the issuance of a SGD300mn of perpetuals securities in August 2019 where management shared that they are "currently conducting due diligence on a potential acquisition", SPHR announced the acquisition of 50% interest in Westfield Marion in November 2019. This is SPHR's second Australian property. As a result, SPHR's exposure to Australia rose from ~5% to ~19% and Australia now contributes to ~25% of SPHR's total revenue. Given that net property income was SGD17.2mn in 1HFY2021, the implied net property income yield is ~5.3% based on our estimation. We note that this is less than the 5.6% estimated at acquisition. We think the difference can be attributed to the allowance for rental arrears and relief amidst the pandemic which accounting in a separate line item from net property income. We do not expect this to be a recurring cost to SPHR.

- **Diversified tenants mix**: SPHR has close to 850 tenants across its properties. By gross rental income, SPHR is sufficiently diversified across the various segments – Luxury (21.4%), Lifestyle/General Retail (17.4%), F&B (16.5%), Departmental Stores/Supermarket (12.6%), Fashion (12.6%), Medical/Office (12.4%) and Non-Retail Services (7.1%). Its largest tenant contributes just 3.2% of rental income with the total ten tenants contributing a total of 19.6% of rental income. We think overall SPHR is substantially diversified across tenants. Having said that, SPHR has exposure to department stores such as Metro (through Paragon) and we note that department stores appears to have broadly underperformed in recent times.

- **Manageable lease expiry profile:** Overall portfolio occupancy was at 98.0% as at 28 February 2021 with a weighted average lease expiry ("WALE") of 3.0 years by gross rental income, up from 2.7 years a year ago. By gross rental income, there is 14% of lease expiries coming due in 2HFY2021 as at 28 February 2021. This was down from 29% as at 30 November 2020, indicating that SPHR was able to renew more than half of leases that are coming due. We note that lease expiries for SPHR looks very well distributed with no more than 25% of leases expiring in any year on an overall portfolio basis. Even though Clementi Mall recorded negative rental reversion in 1HFY2021, we note that the leases renewed or newly leased were a small portion of the entire mall (8.2% of property's net lettable area). The Singapore assets overall recorded a mildly positive rental reversion of 0.4% for 1HFY2021.

- **Acquisition pipeline:** SPHR has a ROFR granted by Sponsor, SPH which extends to The Seletar Mall and The Woodleigh Mall held by SPH. SPH owns 70% of Seletar Mall and 50% of Woodleigh Mall by way of a joint venture. Given The Seletar Mall (a family-oriented mall located in Seng Kang) officially opened on 21 May 2015, some 5+ years ago, we think the mall has stabilized and could possibly be ready to be pumped into SPHR. United Engineers Ltd owns the balance 30% of The Seletar Mall. The property was valued at SGD480mn as at 31 August 2020 (-3.2%y/y), with SPH's stake valued at SGD336mn. The Woodleigh Mall, on the other hand, is under construction and expected to TOP only in 3Q2022. Comparatively, we think The Woodleigh Mall is less likely to be a near-term acquisition target.

- **New code of conduct on lease negotiations:** Major landlords and retail tenants have committed to adopt the new guidelines by 1 June 2021. While the adoption of the code is currently voluntary, it may become law in the future to enforce compliance. The new guidelines encompass different aspects of lease negotiation. First, rents must follow a single rental computation formula instead of "whichever-is-higher" though exceptions can be allowed if mutually agreed and declared to the Fair

Tenancy Industry Committee ("FITC") within 14 days of signing the lease. This change disallows landlords from gaining in both good and bad times. Second, tenants may terminate their leases early under exceptional conditions (such as insolvency, loss of distributorship or franchise rights through no fault of the retailer) with at least six months' prior notice while a tenant's failure to meet specific targets set by the landlord will not qualify as a reason for the landlord to terminate leases. Another change is that exclusivity clause cannot be included in lease agreements unless mutually agreed and declared to FTIC within 14 days of signing of lease. A total of six changes can be expected with the other three involving sales audits, public liability insurance and electricity charges. We think these changes serve to promote more balanced risk sharing between the landlord and the tenant.

Financial Considerations

- **Performance impacted by COVID-19:** Although both gross revenue and net property income grew y/y in 1HFY2021, it was due to the full six months contributions from Westfield Marion acquired in December 2019. Excluding Westfield Marion, we find gross revenue down by 6.0% y/y to SGD105.1mn and net property income down by SGD7.8% y/y to SGD87.6mn. We think this is likely due to the rental reliefs granted to tenants though the amount was not disclosed. In FY2020, SPHR extended SGD39.9mn of rent relief to tenants in Singapore and Australia. With the rollout of vaccinations, both in Singapore and globally, management is expecting relaxation of international travelers requirements though expect a full recovery to still take some time. These positive developments could translate to less rent relief given out as well as a stronger operating environment thereby allowing SPHR's properties to record positive rental reversions.

- **Manageable debt maturity profile and strong interest coverage:** Reported aggregate leverage was 30.4% as at 28 February 2020, slightly higher than a year ago (29.3%). If we were to adjust for 50% of its outstanding perpetual security as debt, we find aggregate leverage higher at ~34%. While SPHR's aggregate leverage has been rising on the back of acquisitions of properties, it remains below that of its peer group. EBITDA/Interest based on our calculation is strong at 7.7x and lower at 6.2x after adjusting for 50% of the distribution to perpetual bondholders as interest. We note that interest expense of SPHR has fallen by 29.6% y/y as its average cost of debt fell to 1.84%p.a. from 2.83% p.a. a year ago. SPHR has also refinanced SGD215mn loan for a new term of five years and does not have any debt maturing in the remaining of FY2021 as at 28 February 2021 except for a SGD50mn loan which will be refinanced in due course.

- **Significant encumbered assets compared to peers:** All SPHR's borrowings, totaling SGD1.3bn are secured against its properties. Specifically, SGD995mn is secured against Paragon, AUD105mn is secured against Figtree Grove and SUD200mn is secured against Westfield Marion. That said, we are not overly concerned as SPHR's secured debt can most likely be rolled over in our view and Clementi Mall is fully unencumbered. Clementi Mall was last valued at SGD584mn (as at 31 August 2020) with another ~88 years to go on its leasehold tenure. We also expect Clementi Mall's valuation to be relative stable given that it is a heartland mall located within the transport node. While the Rail Mall is also unencumbered, the property is a leasehold property with less than 25 years. Comparatively, we think the Rail Mall would be a harder asset to pledge for funding from banks. SPHR also has SGD225mn of unsecured credit facilities which it can tap on if needed.

- **Dividends continued to be paid through the pandemic though significantly reduced:** While SPHR has reduced distribution per unit ("DPU") significantly in FY2020, we note that SPHR still paid dividends every quarter. This is important for the SPHR perpetual security holders because with the dividend stopper, any deferral of perpetual distributions would block the REIT from paying a dividend. Therefore, the dividend stopper encourages timely and continued distributions to perpetual holders. SPHR had also in FY2020 deferred SGD14.5mn of income available for distribution as allowed under COVID-10 relief measures. Though in 1HFY2021, SPHR released ~SGD7.3mn of the FY2020 distributable income deferred as allowed by IRAS. We would expect SPHR to release the balance in the subsequent quarters so long as COVID-19 pandemic situation controls to improve.

- **Revaluation losses moderated in 1HFY2021:** SPHR recorded fair value losses on its investment properties of SGD8.4mn in 1HFY2021. This amount is estimated by the Manager. This was on top of the SGD179.9mn fair value losses on its investment properties (~4%y/y decline in asset valuation) recognized in FY2020 based on independent valuations (SGD126.0mn from Singapore, SGD53.9mn from Australia). We note that in FY2020 the revaluation losses were across all properties, on the back of the impact of the pandemic on the retail sector. Although the uncertain outlook of the COVID-19 pandemic could continue to cast a shadow over SPHR's asset valuations in the near future, the fair value losses on its investment properties have slowed since FY2020, as such we think the worst could be over for these properties. Even though SPHR has seen significant revaluation losses, its aggregate leverage has held up relatively well on the back of the acquisition of Westfield Marion which has helped to increase its overall asset base.

Figure 5: Assets Valuation as at 31 August (SGD'mn)

Property	FY2020	FY2019	FY2018	FY2017	FY2016	FY2015	FY2014
Paragon	2,640	2,745	2,719	2,695	2,656	2,641	2,588
Clementi Mall	584	597	586	583	574	572	571
The Rail Mall	62	64	63	-	-	-	-
Figtree Grove	191	192	-	-	-	-	-
Westfield Marion	649						
Total	4,126	3,598	3,368	3,278	3,230	3,213	3,159

Source: Company

- **Expanded funding sources:** SPHR has demonstrated improved access to more funding sources. On top of its cash reserves (~SGD127mn) and undrawn banking facilities (unsecured ~SGD225mn), SPHR tapped the debt capital market in 2019, raising its first SGD300mn perpetual securities at 4.1% perpetual distribution p.a. in August 2019. With the issuance, SPHR's funding from debt capital markets increased to 7% of total capital. Subsequently, the net proceeds from the issuance were utilized to fund the acquisition of Westfield Marion, Australia in December 2019. We would expect SPHR to continue to tap the debt capital markets to help fund its future inorganic growth opportunities.

III) Perpetual Structure

Step-up/reset and call date: The call date is at the end of year 5 (30 Aug 2024), which matches the first reset date. The perpetual bond is callable at any coupon payment date thereafter while it reset every 5 years thereafter. There is no step-up to the distribution rate if not called.

Deferred distribution: Issuer can elect not to pay distributions on the perpetuals. Deferred distribution payments are non-cumulative and will not accrue interest.

Seniority: SPHRSP 4.1% PERPs are subordinated perpetuals - senior to common equity though junior to straight debt. SPHR's multicurrency debt issuance programme allows the flexibility for SPHR to issue senior perpetual although to date no senior perpetuals have been issued.

Dividend stopper: If distribution payments are deferred, a dividend stopper would restrict SPHR from declaring or paying dividends to its unitholders (i.e.: common equity holders). SPHR would also be restricted from redeeming, reducing, cancelling, buying-back to redeem, reduce, cancel, buy-back common equity. Given that SPHR must distribute 90% of its taxable income each year to enjoy tax exempt status by IRAS, the dividend stopper encourages timely and continued distributions to perpetual holders in our view.

IV) Technical Considerations

Positive	Negative
▪ Dividend stopper encourages timely and consistent distribution payments to perpetual holders especially as a REIT that regularly pay out dividends to its unitholders to be tax exempted ▪ Good name recognition via the association with SPH	▪ Lack of external credit rating ▪ No change of control clause ▪ No delisting put ▪ No step-up margin

Figure 6: Relative Value

Bond	Maturity / Call date	Reset Rate	Aggregate leverage	Ask YTW	Spread
SPHRSP 4.1% PERP	30 Aug 2024	5Y SGD Swap +2.517%	30.4%	3.80%	301bps
SPHSP 4.5% PERP	07 Jun 2024	5Y SGD Swap + 3.612%	~39%	3.54%	275bps
SPHSP 4.0% PERP	12 May 2025	5Y SGD Swap + 3.545%	~39%	3.73%	278bps
SGREIT 3.85% PERP	15 Dec 2025	5Y SGD Swap + 3.292%	35.8%	4.19%	307bps
SUNSP 3.8% PERP	27 Nov 2025	5Y SGD Swap + 3.295%	44.3%	3.82%	277bps

Indicative prices as at 1 April 2021 Source: Bloomberg
Gross gearing based on latest available quarter

SPHRSP 4.1% PERP appears to be trading closest to its Sponsor and major shareholder's SPHSP 4.5% PERP. SPHR being a REIT, holds its assets under investment properties (unlike its Sponsor) and these properties generate recurring rental income. REITs are also subjected to the 50% aggregate leverage cap in Singapore. In addition, event risk is lower for SPHR than its Sponsor in our view given it is a REIT. While SPHR may pursue further inorganic growth in the future, assets purchased are typically supported by rental income to some extent. Therefore, we see event risk as low relative to its Sponsor. While bonds and perpetual securities of REITs typically trades tighter than its Sponsor, SPHR PERP is trading 26bps wider than SPHSP 4.5% PEPR. As such, we think there is room for SPHRSP's perpetual security to trade tighter relative to SPHSP 4.5% PERP.

SPHR is larger than Starhill Global REIT ("SGREIT") but smaller than Suntec REIT ("SUN") in terms of assets base. We think SPHR's sole perpetual is attractive relative to SUNSP's sole perpetual given its significantly lower aggregate leverage. As compared to SGREIT's sole perpetual, we think SPHR's perpetual is trading fair.

SPHRSP 4.1% PERP will reset to 5Y SGD Swap + 2.517% with no step-up margin if not called at first call in 2024. The 5Y SGD Swap rate is 1.145%, implying a reset rate of 3.662% while the forward 5Y swap rate is 2.332%, implying a reset rate of 4.849%. We see a high probability of SPHR PERP being called at first call at this point.

Overall, we are Neutral on SPHR 4.1% PERP.

V) Conclusion

SPHR holds a portfolio of SGD4.1bn retail estate in Singapore and Australia and is anchored by Paragon which is two-third retail and one-third medical/office by net lettable area. It is sponsored by SPH, a media organization (sole provider of print newspapers in Singapore) with real estate as a key business segment. Growth in the recent years was driven largely by acquisition. While this was at the expense of a higher leverage, we think the credit metrics of SPHR remain very manageable albeit weaker than at time of IPO. Having said that, it is worth noting that SPHR was lowly geared to begin with. Aggregate leverage of SPHR was 30.4% as at 28 February 2021 and higher at ~35% when adjusted for 50% perpetual as debt. EBITDA/Interest is strong at 7.7x before factoring in distributions for perpetual security. SPHR also has a healthy portfolio occupancy rate of 98.0%. Constraining its credit profile is its concentration in the retail property segment and medium scale, versus large cap mixed assets REITs in an increasingly dual-tier market where those larger cap REITs are seeing a lower cost of funding and a higher percentage of unencumbered properties. We are initiating SPHR with a Neutral (4) issuer profile.

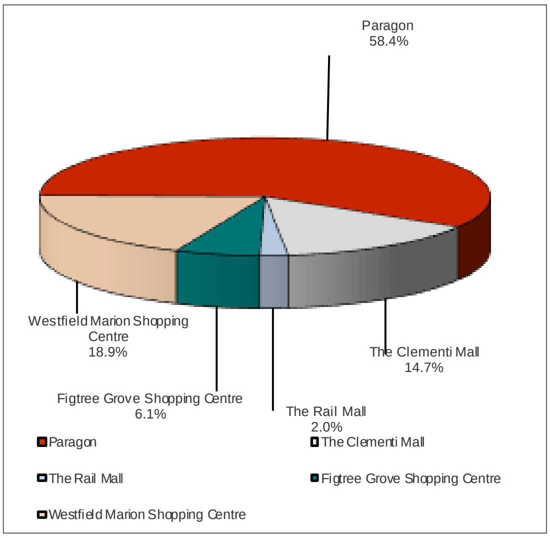
SPH REIT

Table 1: Summary Financials

Year End 31st Aug	FY2019	FY2020	1H2021
Income Statement (SGD'mn)			
Revenue	228.6	241.5	140.0
EBITDA	159.6	158.5	91.8
EBIT	159.5	158.3	91.7
Gross interest expense	30.5	32.9	11.9
Profit Before Tax	149.2	-60.0	69.9
Net profit	148.8	-64.0	69.7
Balance Sheet (SGD'mn)			
Cash and bank deposits	342.7	82.0	127.5
Total assets	3,948.4	4,240.7	4,281.3
Short term debt	279.6	214.9	50.0
Gross debt	1,091.1	1,298.6	1,305.7
Net debt	748.5	1,216.6	1,178.3
Shareholders' equity	2,771.4	2,814.7	2,852.7
Cash Flow (SGD'mn)			
CFO	180.5	166.3	114.0
Capex	0.1	0.2	4.0
Acquisitions	215.5	636.6	0.0
Disposals	0.0	0.0	0.0
Dividends	144.2	108.9	54.4
Interest paid	28.9	31.9	11.2
Free Cash Flow (FCF)	180.4	166.1	110.1
Key Ratios			
EBITDA margin (%)	69.82	65.64	65.63
Net margin (%)	65.09	-26.52	49.82
Gross debt to EBITDA (x)	6.84	8.19	7.11
Net debt to EBITDA (x)	4.69	7.68	6.41
Gross Debt to Equity (x)	0.39	0.46	0.46
Net Debt to Equity (x)	0.27	0.43	0.41
Gross debt/total asset (x)	0.28	0.31	0.30
Net debt/total asset (x)	0.19	0.29	0.28
Cash/current borrowings (x)	1.23	0.38	2.55
EBITDA/Total Interest (x)	5.24	4.82	7.75

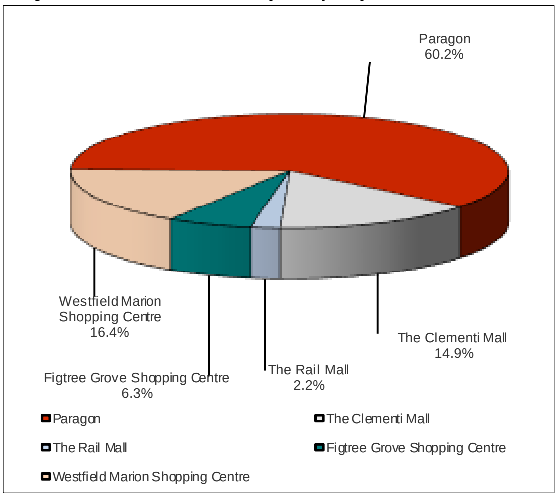
Source: Company, OCBC estimates

Figure 1: Revenue breakdown by Property - 1H2021



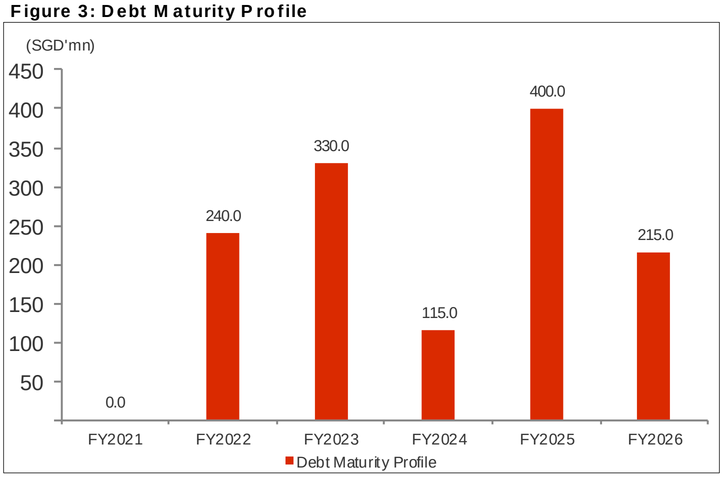
Source: Company

Figure 2: NPI breakdown by Property - 1H2021



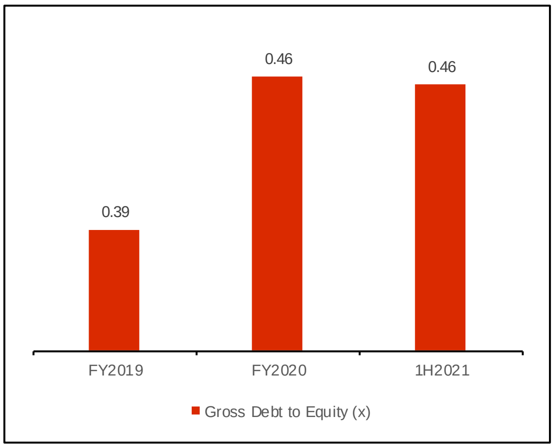
Source: Company

Figure 3: Debt Maturity Profile



Source: Company

Figure 4: Gross Debt to Equity (x)



Source: Company, OCBC estimates

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 bond represents **better relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Neutral ("N") – The represents **fair relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Underweight ("UW") – The represents **weaker relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

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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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.