Singapore Industry Focus

Singapore Hospitality

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DBS Group Research . Equity

25 Mar 2022

Time for a bounce as borders re-open

- Recent datapoints suggest that hospitality S-REITs are at the start of a convincing multi-year upcycle
- Spotlight returns to reopening in Asia with most markets slated to open in 1H22; hotel S-REITs to benefit with Asia the biggest revenue market at 42%-100% exposure
- Critical factor: close correlation between RevPAR and higher P/NAV, substantial potential upside as sector is still trading at -1 standard deviation of its P/NAV range
- Top picks: ART, CDLHT and FEHT

Stars are re-aligning for hospitality S-REITs to deliver a convincing recovery trajectory from 2022. Singapore announced the re-opening of borders from 25 February and resuming all Vaccinated Travel Lanes (VTLs) - ahead of market expectations. Alongside the recently relaxed entry requirements on quarantine and testing, the stars are finally aligning for Singapore's tourism sector. The hotel S-REITs first saw bright spots in 4Q21 with RevPAR at a 2-year high and we see them building on this momentum to deliver upside surprises through 2022-2023.

Time for Singapore to shine as borders in Asia reopen. Domestic travel markets are now ahead on the recovery track, with 4Q21 RevPAR at c.62% of normalized level, ahead of Singapore's c.47% . We see the reopening theme rotating to Asia, as key Asian markets have reopened or are committing to open in 1H22. Similarly, Singapore should reopen to 65%-70% of its key visitor source markets by mid-22 and potentially reach 90%-95% if Greater China eases border controls. The stars are aligning for our hotel S-REITs with Asia as the single largest revenue market with exposure ranging from 42% to 100%.

Critical factor: RevPAR recovery and capital value normalization are key factors to monitor. The sector currently trades at 0.8x P/NAV (-1 standard deviation). We see opportunity for this to head higher the close correlation between RevPAR and stock prices, driving a target P/NAV multiple of at least 0.9x. Furthermore, there is more potential upside as capital values are revalued up from currently 96% of normalized levels in 2019. P/NAV multiple on normalized book value of 0.78x will translate to a performance upside of c.15% to mean, or c.28% to +1 standard deviation levels, and on a compelling forward FY22F sector yield of 6.1%. Our top sector picks - Ascott Residence Trust (ART) and CDL Hospitality Trust (CDLHT) – are expected to benefit from both domestic and international recovery, while Far East Hospitality Trust (FEHT) is for exposure to Singapore tourism recovery.

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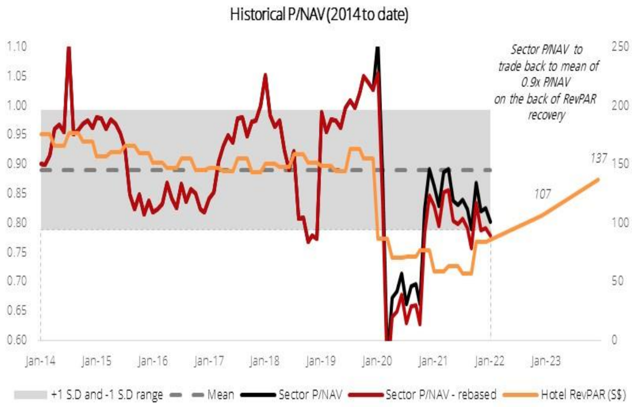
STOCKS

	Price S$	Mkt Cap US$m	12-mth Target S$	Performance (%) 3 mth	12 mth	Rating
Ascott Residence Trust	1.10	2,660	1.30	8.9	2.8	BUY
CDL Hospitality Trusts	1.24	1,124	1.40	6.9	0.0	BUY
Far East Hospitality Trust	0.63	910	0.78	5.9	0.8	BUY
Frasers Hospitality Trust	0.49	688	0.65	5.4	(8.5)	BUY

Source: DBS Bank, Bloomberg Finance L.P.
Closing price as of 24 Mar 2022

Strong correlation between RevPAR and P/NAV



Source: DBS Bank, Bloomberg Finance L.P.

Delivering on promises

Positive read from recent datapoints; upside surprise to DPUs expected in 2H22, which is a critical factor for share price. The hospitality S-REITs, namely Ascott Residence Trust ("ART"), CDL Hospitality Trust ("CDLHT"), Far East Hospitality Trust ("FEHT") and Frasers Hospitality Trust ("FHT") recorded sequential improvements in RevPar in their recent results and guided for a brighter outlook for 2022. This gives us confidence that 2022 will deliver upside surprises to dividend per unit ("DPU"), which historically exhibits a close correlation to share price performance.

While the impact of Omicron was a key discussion point in our meetings in recent weeks, we find comfort that the impact has been more muted than the previous Delta variant as more countries adopt a more endemic approach towards Omicron given the high vaccination rates.

A summary of the key guidance provided by the hospitality players is in the table below.

Key observations in recent hospitality S-REITs briefings

REITs	Key datapoints:	Forward guidance
Ascott Residence Trust	• Strongest quarter of RevPAR recovery since Covid, up 24% q-o-q to S$87 in 4Q21 • All markets across the portfolio have turned GOP positive in 2H21 and only two assets within the portfolio remain closed (two assets in Japan) • Stable rents make up 70% of portfolio contributions with lyf one-north (opened in Nov'21) added to the mix	• Medium term target to double exposure to longer-stay lodging assets to 25-30% • Exposure to the longer-stay lodging segment has ramped up substantially through c.S$780m worth of acquisitions from 2021 and contributes more than ART's rental housing portfolio in Japan. • Asset recycling a key strategy in 2022.
CDL Hospitality Trust	• DPU of 4.27Scts in FY21 slightly below due to lower capital distributions, core operations in line with estimates • NPI in 4Q21 of S$28.7m was the highest since the pandemic as geographical markets resume normalcy	• Room pipeline to be supplemented by development project 'The Casting', which will come onstream in xx, and the c.S$475m Moxy hotel acquisition in 2025 (part of Novotel Clarke Quay redevelopment deal). • UK and Maldives likely to lead the recovery on the back of domestic and tourist demand, with the latter seeing government incentives to boost tourism.
Far East Hospitality Trust	• Full year DPU of 2.63 Scts beats our estimates on interest savings • 4Q21 RevPAR saw an uptick of 23-29% q-o-q for serviced residences and hotels, driven by inbound travel boost from Vaccinated Travel Lanes and strong domestic staycation demand • Completion of Central Square divestment in 2Q22 to lower gearing (down to ~33.5% from 38.3%) and give rise to potential capital gain top-ups, which could be shared with investors	• Asia border reopening to propel recovery as the largest revenue market for Singapore • Pure-play Singapore exposure a proxy for recovery of Singapore hospitality and tourism • Recovery of book value and Central Square divestment deal completion to push NAV/share to c.S$0.91 • Debt funded acquisitions to move the needle and potentially yield double digit accretion to DPUs
Frasers Hospitality Trust	• RevPAR in all key markets posted sequential recovery as travel demand takes hold. • Singapore RevPAR rose 12.9% y-o-y and 5.9% q-o-q in 1Q22; InterContinental resecured government quarantine business in the quarter • Australia RevPAR rose 43.1% y-o-y and 32.1% q-o-q as Sydney and Melbourne exit lock down in Nov'21	• Divestment of Sofitel Sydney Wentworth crystalizes NAV, deployment of proceeds a key event to watch in 2022. • Expect stronger performance from Australia, one of FHT's key markets as Australia reopens international borders for the first time since the pandemic from 21 Feb 2022.

Source: Companies, DBS Bank

Where are we in the recovery trajectory?

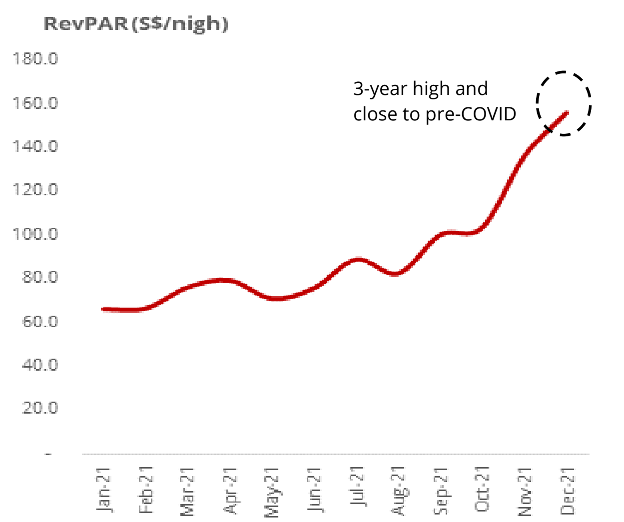
Recovery in 2021 despite borders remaining substantially closed. With borders remaining substantially closed in 2021, the Singapore tourism board recently reported that overall hotel revenues totalled S$978m, a c.21% drop y-o-y. While headlines suggest a weaker year, we note that the comparison year in 2020 included 1Q20, prior to lockdowns from the start of COVID-19. Stripping out the impact of 1Q20 prior to the shutdown, overall revenues in 2021 was up 36% instead, which tracks in line with our expectations.

In 2021, we note that the Government quarantine business was the key demand driver, but overall occupancy rates declined slightly to c.60% as government gradually reduced their quarantine block bookings for hotels through the course of the year as Singapore tweaked the approach towards treating COVID-19 as an endemic given the high vaccination rates. Staycation business was the key driver, with revenue in Dec'21 seeing a new high (S$127.8m with RevPAR of S$156/night) since the pandemic began. This has set the stage for a gradual recovery from the claws of COVID-19.

Bright spots started to appear in 4Q21, and markets have just started to take notice of this. Hoteliers had seen suppressed revenues for full year 2021 but we see bright spots emerging. In fact, Dec'21 numbers were very encouraging in our view, with RevPAR hitting a 2-high of S$156/night. Occupancy rates in Nov'21/Dec'21 were back to pre-pandemic levels of 71%-78% which essentially means that rooms were largely full.

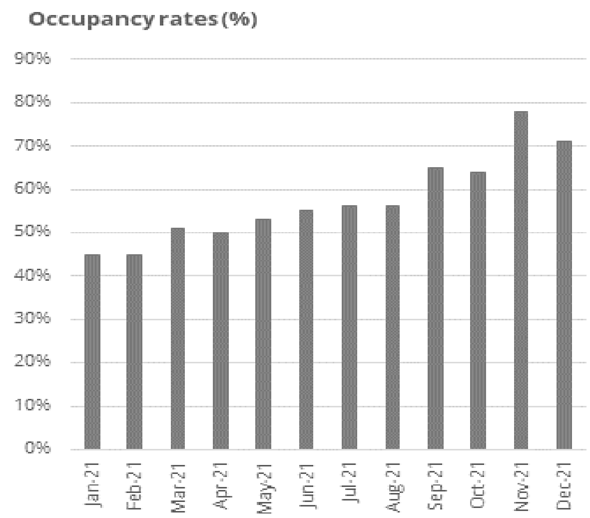
A gradual step to normalcy in 2022. Based on our understanding, the weaker occupancy rates back in 2021 were multi-fold. While staycation demand and travellers on vaccinated travel lanes ("VTL") partially took up the incremental demand, we generally noticed a drop in corporate demand as workers that were temporarily put up in hotels when the pandemic first hit had switched to alternative lodging options such as renting apartments in Singapore. Government contracts that had generally supported the industry for over close to 2 years now is tapering down. We do understand that some contracts under our hotel REITs have seen extensions to 1Q22. Staycation demand was also affected by periodic lock down measures that hammered peak staycation periods such as the September holidays. December RevPAR numbers remain robust at 36% higher y-o-y.

Industry RevPAR hit a new high in Dec'21 with more upside as VTLs reopen in 2022



Source: STB, DBS Bank

Occupancy rates have consistently remained above 60%, which is the break-even level



Source: STB, DBS Bank

Critical Factor: Border reopening repositions S-REITS on a recovery track

Domestic markets lead recovery as RevPARs are now 50%-70% of pre-COVID levels. Zooming beyond the local context, large domestic travel markets continue to lead in terms of recovery. The largest uptick in RevPAR amongst our hotel S-REITs was in 1H21, which coincided with inter-border travel relaxation in markets such as Europe, Australia, and Japan. Correspondingly, RevPAR in these same markets has recovered ahead of Singapore, which is a market that is generally more international driven.

We estimate that RevPAR for these markets had recovered to c.52% - 72% of their normalized levels (2019 average RevPAR) in 4Q21, as opposed to Singapore, which stands at about c.47% of normalized basis as of year-end 2021. Europe posted an impressive recovery with inter-border travel relaxed in mid-May, ahead of peak travel months, ending the year at c.72% of normalized RevPAR.

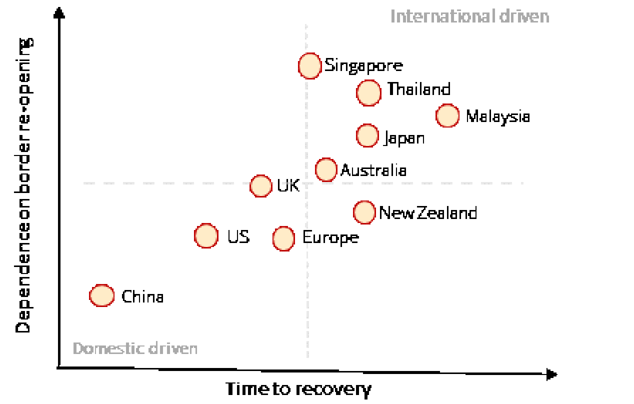
Three cheers as VTLs resume operations and broaden to more markets. As major travel markets relaxed inter-state borders, international border relaxation will be the next catalyst to add another layer of demand, especially for international driven markets such as Singapore. The current 25 vaccinated travel lanes (VTLs) arrangements, including the newly announced VTLs to Greece and Vietnam represent just over 60% of total inbound visitor arrivals back in 2019. We estimate that Singapore could reopen to 70% and 95% of historical inbound markets by June and December this year respectively, with China the elephant in the room at c.20% of historical visitor arrivals.

Roaring start for Singapore hoteliers as Asia opens borders. Narrowing down into the Singapore hotel recovery story, sequential international border relaxation announced in Asia generally came ahead of market expectations. Four out of five of our largest inbound markets, except for China which continues to prioritize its zero-case tolerance policy ahead of border reopening. These same markets are also covered under VTL arrangements with Singapore as early as November last year.

Simplified testing requirements and reduced cost of travel associated with test and quarantine requirements on entry and exit touch points will further incentivize both leisure and corporate demand for travel within Asia. Asia is the single largest revenue market for our S-REITs with a 42% to 100% market share.

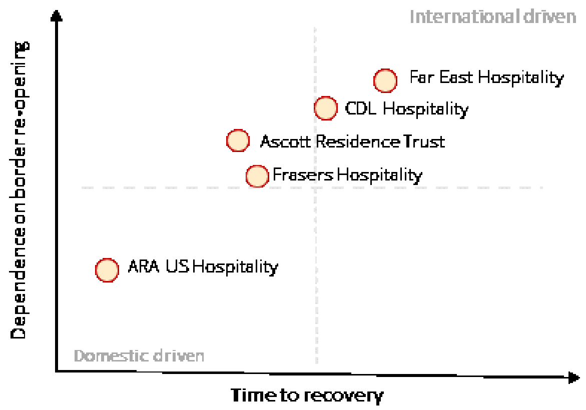
Looking ahead in 2022, we expect to see c.40% and 29% y-o-y recovery in sector RevPAR to reach c.70% and 90% of pre-COVID levels in FY22/FY23 and this remains on track in our view.

Key markets with hospitality exposure



Source: Companies, DBS Bank

How do the hospitality S-REITs compare



Source: Companies, DBS Bank

Largest historical inbound markets and opening progress (% inbound market share, 2019):

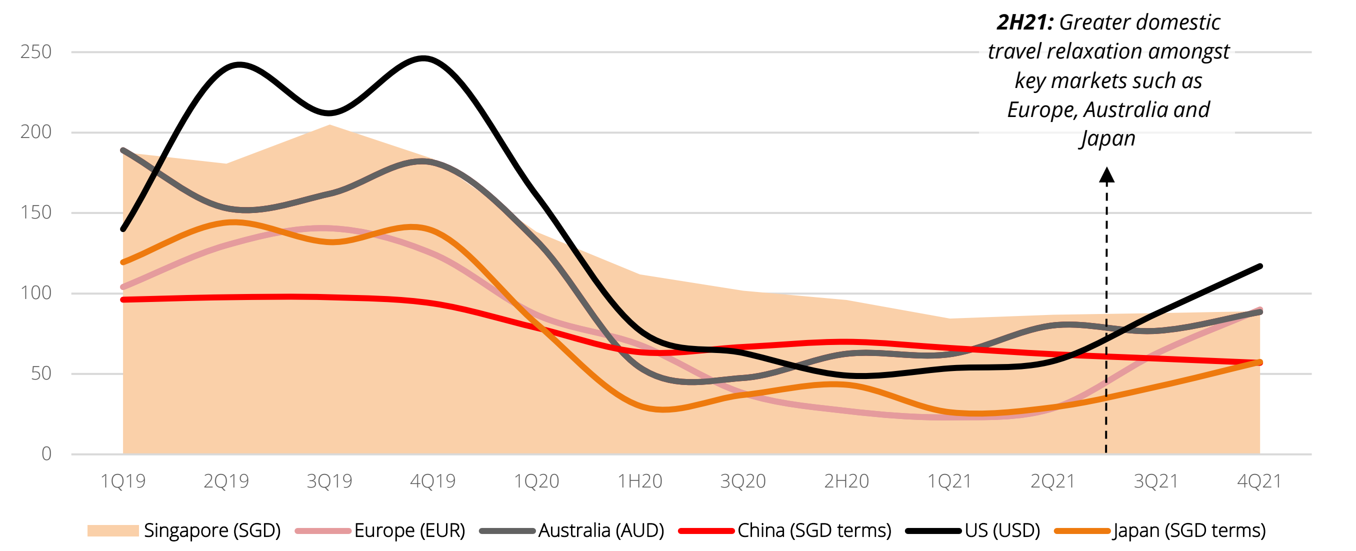
- China (19%) – Border reopening will depend on how China move forward with its zero-case policy. The recent lockdown in Shenzhen shows that sentiment around the pandemic spread continues to be severely regarded.
- Indonesia (16%) – International borders re-opened on 12 January 2022. Fully vaccinated travellers are required to hold a visit visa and show a negative PCR test result.
- India (7%) – International border to open from 27 March 2022 through the resumption of international flights.
- Malaysia (6%) – International borders to open from 1 April 2022 to travellers while foregoing quarantine requirements for fully vaccinated travellers who have tested negative.
- Australia (6%) – Full border reopening from 21 February 2022. Travellers will need to be fully vaccinated, have proof of a negative ART test and hold a valid entry visa.

Summary of exposure and border re-opening

	Geographical exposure			NPI exposure			Scheduled and/or potential month of border reopening
	ART	CDLHT	FHT	ART	CDLHT	FHT	
Singapore	7%	43%	19%	11%	45%	21%	Feb'22
Asia (ex-SG)	35%	15%	14%	38%	10%	15%	Jan'22 - Cambodia, Thailand Mar'22 – Indonesia, India Apr'22 - Malaysia May'22 - Vietnam Jun'22 - Japan 2H22 - China
Australia / NZ	24%	19%	46%	13%	27%	43%	Feb'22
Europe (ex-UK)	13%	6%	7%	24%	8%	4%	Reopened to selective regions
UK	6%	16%	13%	7%	9%	17%	Feb'22
US	14%	0%	0%	7%	0%	0%	Nov'21

Source: Companies, DBS Bank

Quarterly hotel S-REITs RevPAR tracker by geographical markets (same-store basis)



Source: Companies, DBS Bank

Critical Factor: RevPAR recovery to drive valuations higher, target P/NAV back to mean of 0.9x is possible

RevPAR recovery to drive sector valuation to 0.9x-1.0x P/NAV, representing upside of over 20%. While the market has focused on impact of rate hikes on the S-REITS generally, the impact on hospitality S-REITs is smaller. And the hospitality sector is one of the remaining "re-opening" plays that have yet to record a convincing share price recovery. Based on our analysis, there is a close correlation with RevPAR and share price and we believe RevPAR is set to deliver a sustained recovery through the course of 2022 and beyond.

Historically, sector P/NAV generally trades within -1 standard deviation to +1 standard deviation of 0.8x and 1.0x P/NAV. The current valuation at 0.8x has only partially priced in reopening optimism, and normalization of RevPAR back to normal trading levels should propel P/NAV multiple back to 0.9x to 1.0x P/NAV, which presents potential upside of c.13%.

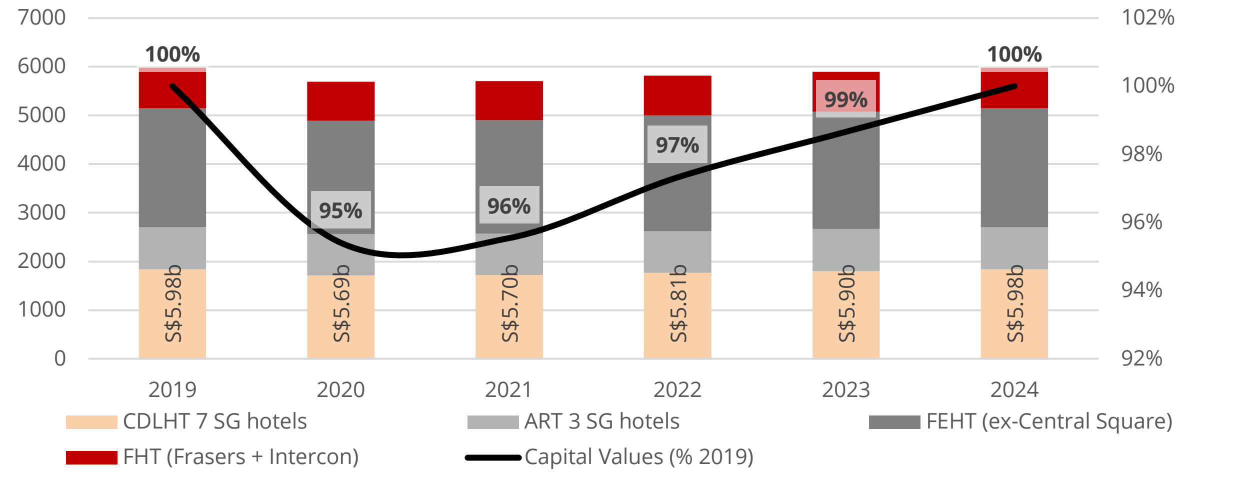
Trading range also penalized by current capital values. The recovery in the hotels sector has lagged other reopening subsectors of retail and office despite Singapore's positioning as a highly international hospitality market. We note that the challenging operating climate for Singapore hoteliers last year has been reflected on sector capital values. On a like-for-like basis, we estimate that write back of portfolio valuations between 2020 and 2021 were limited but we believe there is more in store in 2022.

Sector upside of 15% to 28% on return to normalised trading range. Based on end-2021 valuations, we estimate capital values are at c.96% of normalized levels. We are of the view that the sector has been penalized twice by both a soft operating environment and suppressed book values. The markets should expect that the write back in capital values is a matter of time as valuers' price in a full recovery by year 2024. Rebasing current P/NAV on a normalized book value term at 0.78x, the gap to mean P/NAV translate to an even higher upside of c.15% or c.28% when pegged to +1 standard deviation.

Maintain sector top picks of ART and CDLHT, FEHT for Singapore focused recovery. Sector peers continue to trade between -1 standard deviation and mean P/NAV or 0.69x to 0.80x. The FY22F sector dividend yield is attractive at 6.1%. Using normalized capital values, the P/NAV range is even more compelling at 0.65x to 0.83x.

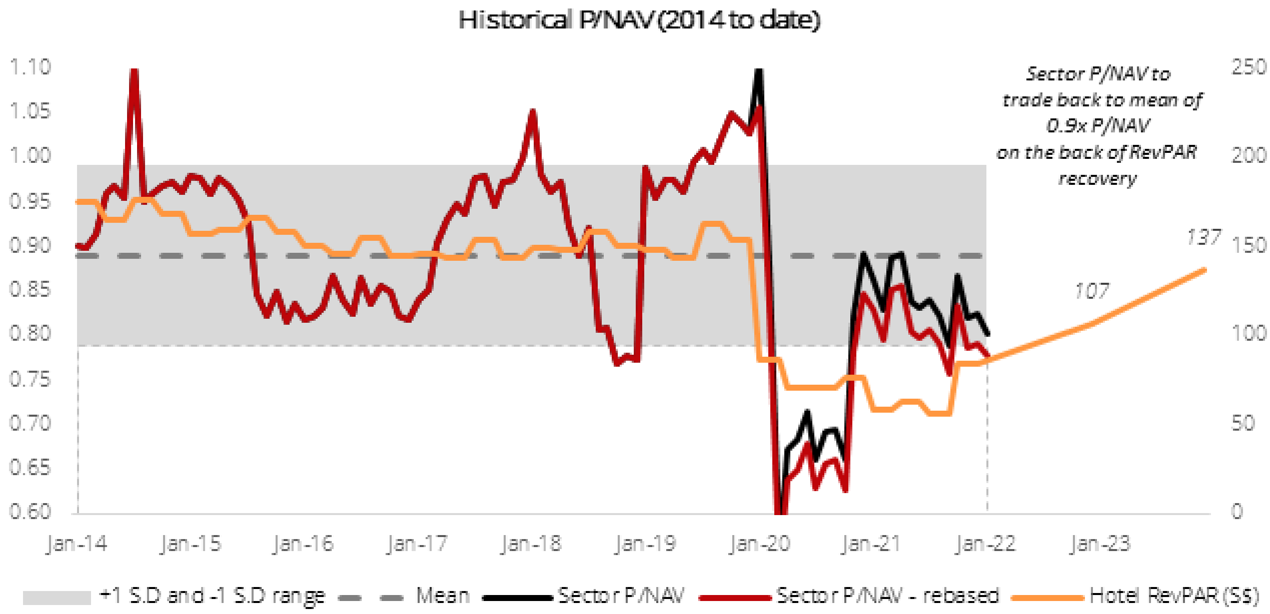
We maintain our top picks- ART and CDLHT- for their global footprint that will benefit from both domestic recovery and international demand. We like FEHT as a proxy for the Singapore reopening theme given that 100% of its revenue is within Singapore, and there is potential upside surprise from acquisitions (FEHT: Early bird catches the worm).

Portfolio valuation as a % of normalised levels (2019 levels), like-for-like-basis



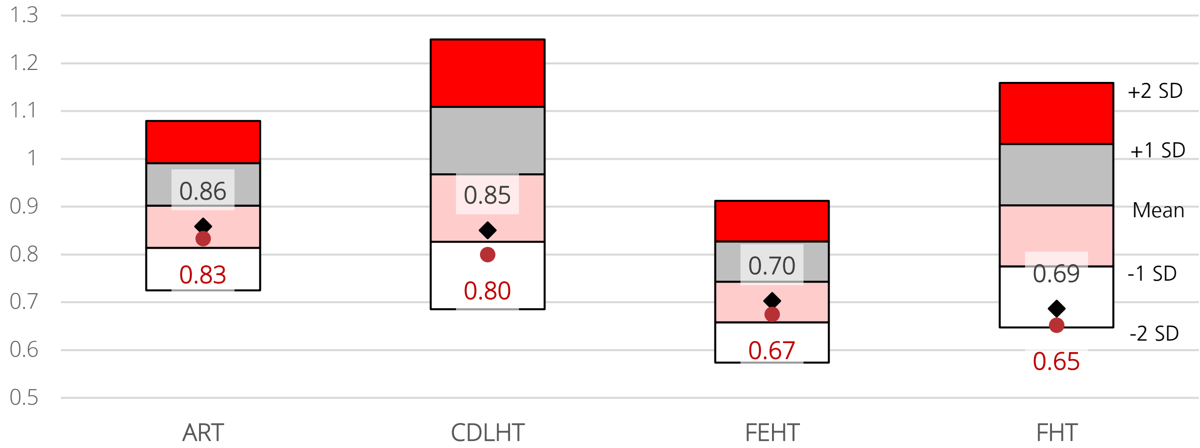
Source: STB, DBS Bank

Industry RevPAR near -1 Standard Deviation levels on re-based P/NAV and forward hotel RevPAR projections



Source: STB, DBS Bank

Hotel S-REITs historical trading range (2014 to date) vs current and re-based P/NAV on normalised capital values



Source: STB, DBS Bank

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BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

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