

# China / Hong Kong Company Update

## Regal REIT

Bloomberg: 1881 HK EQUITY | Reuters: 1881.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

1 Apr 2022

### HOLD

Last Traded Price (31 Mar 2022): HK\$1.48 (HSI : 21,997)

Price Target 12-mth: HK\$1.60 (8% upside)

#### Analyst

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### What's New

- FY21 distributable income fell 37% to HK\$311m and was 4% higher than our forecast due to lower-than-estimated cash financing costs
- Higher base rents for Regal branded hotels and two iclub hotels in Sheung Wan and Fortress Hill in FY22
- Cash finance costs set to increase on interest rate hikes
- Maintain HOLD with TP of HK\$1.60

#### Price Relative



#### Forecasts and Valuation

FY Dec (HK\$ m)	2020A	2021A	2022F	2023F
Gross Revenue	871	594	615	675
Net Property Inc	858	579	600	660
Net Profit	(2,310)	577	232	231
Distribution Inc	443	280	220	223
DPU (HK\$)	0.14	0.09	0.07	0.07
DPU Gth (%)	10	(37)	(22)	1
Div Yield (%)	9.2	5.8	4.6	4.6
Gross Gearing (%)	44	44	44	44
Book Value (HK\$)	3.66	3.73	3.72	3.72
P/Book Value (x)	0.4	0.4	0.4	0.4

DPU Rev (%): (13) New

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

### A mixed bag

#### Investment Thesis

**HOLD with HK\$1.60 TP.** Regal REIT offers distribution yield of 4.6% for FY22. The spread of the Omicron has inevitably delayed the border re-opening with Mainland China and thus the earnings recovery of Regal REIT. As such, we maintain our HOLD rating.

**Higher base rents offset by expected increase in cash financing costs.** For FY22, the base rent for the five Regal branded initial hotels has been set at HK\$475m, up 3.3% y-o-y. For iclub Sheung Wan Hotel and iclub Fortress Hill Hotel, the base rents will rise to HK\$27m in FY22 from FY21's HK\$26m. However, the growth in base rents should be offset by expected increase in cash financing costs led by interest rate hikes.

**Adapting to changing operating landscape led by the pandemic.** Regal Airport Hotel, Regal Kowloon Hotel, Regal Oriental Hotel, iclub Fortress Hill and iclub Ma Tau Wai now serve as quarantine hotels or other anti-pandemic purpose designated by the government. This should help to safeguard its overall RevPAR.

#### Valuation:

Our target price for Regal REIT is based on a Dividend Discount Model using 7.6% discount rate.

#### Where we differ:

We are more cautious on the long-term prospects of the hotel industry given expectations of reduced business travel in the future.

#### Key Risks to Our View:

A faster-than-expected resolution to the COVID-19 resurgence would help inbound tourism and hotel industry recover. Rmb appreciation would help the purchasing power of mainland guests and their demand for hotels when the border re-opens.

#### At A Glance

Issued Capital (m shrs)	3,257
Mkt Cap (HK\$/US\$m)	4,820 / 615
Major Shareholders (%)	
Regal Hotels International Holdings Ltd	74.6
Free Float (%)	25.4
3m Avg. Daily Val. (US\$m)	0.06
GICS Industry: Real Estate / Equity Real Estate Investment	



Watchlist the stock on Insights Direct to receive prompt updates



## Regal REIT

### WHAT'S NEW

#### Dragged by reduced rental income

Regal REIT's FY21 distributable income was 37% lower at HK\$311m, dragged by lower net rental income, partially offset by reduced cash finance costs.

Final DPU fell 46.1% to HK\$0.041, taking the full-year DPU to HK\$0.086. This represented payout ratio of 90.1% (FY20: 90.2%).

Total net rental and hotel income dropped 33% to HK\$578.9m, mainly dragged by lower base rents for five initial hotels and two iclub hotels in Sheung Wan and Fortress Hill. With stringent quarantine restrictions for incoming travellers led by the prolonged pandemic, inbound tourism remained at a standstill. Against this backdrop, Regal REIT has adapted its business strategy to the current operating landscape and targets self-quarantine and domestic long-stay guests, and those seeking staycation packages. Regal Hongkong Hotel, Regal Kowloon Hotel and Regal Riverside Hotel would cater to the local market while Regal Oriental Hotel, Regal Airport Hotel, iclub Fortress Hill Hotel and iclub Ma Tau Wai Hotel operated as designated quarantine hotels serving mostly returning residents in 2021.

The overall occupancy for the five Regal-branded hotels improved to 57.3% in 2021 from 2020's 37.2%. Even though their combined room rate declined 12.9%, the average RevPAR was 34.1% higher. Since total net property income from the hotel operations from these five hotels was just HK\$104.5m, well below the aggregate base rents, no variable rents were earned in FY21.

The combined RevPAR of iclub Sheung Wan Hotel and iclub Fortress Hill Hotel registered 15.1% growth as room rates grew 6.7% with occupancy 5.6ppts higher at 77.7%. As the NPI for each hotel fell short of the rent, only base rents were earned. RevPAR of self-operated iclub Wan Chai Hotel grew 14.4% higher in FY21 on increased occupancy and room rates. However, NPI was minimal at c.HK\$1m.

Cash finance costs fell sharply by 35% to HK\$130m thanks to lower HIBOR. As of Dec-21, Regal REIT had total debt of HK\$10.1bn (Jun-21: HK\$9.9bn). This put its gearing at 43.9%. (Jun-21: 44.8%) All outstanding loans are subject to floating rates.

For FY22, the base rents for the five "initial hotels", including Regal Airport Hotel, Regal Hongkong Hotel, Regal Kowloon

Hotel, Regal Oriental Hotel and Regal Riverside Hotel, has been set at HK\$475m in aggregate, representing an increase of 3.3% y-o-y.

While base rents of Regal Hongkong Hotel, Regal Kowloon Hotel, Regal Oriental Hotel and Regal Riverside Hotel will rise 8.2%, 3.2%, 5.7% and 6.3% to HK\$66m, HK\$96m, HK\$37m and HK\$101m respectively, that of Regal Airport Hotel will fall by a marginal 0.6% to HK\$175m.

For iclub Sheung Wan Hotel and iclub Fortress Hill Hotel, the base rents will rise modestly to HK\$27m in FY22 from FY21's HK\$26m. In addition, Regal REIT will take 50% of the excess of NPI over base rents as variable rent. For iclub Ma Tau Wai, the initial fixed rental period of five years is still effective till Sep-22. With higher base/fixed rents, we project Regal REIT's gross rental revenue to be 3% higher in FY22.

With the COVID resurgence in early 2022, four quarantine hotels and Regal Kowloon Hotel joined the Community Isolation Facility Scheme to accommodate those COVID-19 patients with mild or no symptoms, commencing from late Feb. With the lifting of flight ban on nine countries, the usage of these five hotels has been changed to serve as quarantine facilities or other anti-pandemic purpose designated by the government.

Regal REIT is trading at a distribution yield of 4.6% for FY22. While the revenue should grow modestly under the new rental package, expected higher financing costs led by interest hike would drag distribution income. The fifth wave of COVID outbreak has delayed the border re-opening with Mainland China which plays a crucial in full recovery of hotel sector. Hence we maintain HOLD with DDM-based TP of HK\$1.60.

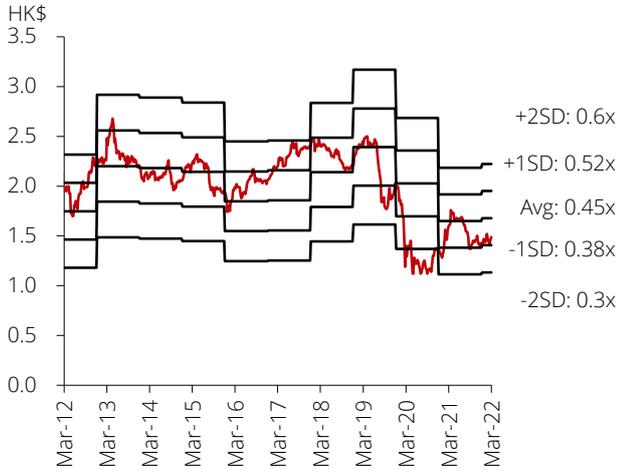
#### Company Background

Listed in Mar-07, Regal REIT is the first hotel REIT in Hong Kong with an initial portfolio of five "Regal" branded hotels. Following the acquisition of four "iclub" branded hotels from its sponsor, Regal REIT currently owns a portfolio of nine hotels across Hong Kong Island, Kowloon Peninsula, New Territories and Lantau Island with a total of 4,909 guest rooms. Regal Hotels International Holdings Ltd (78.HK) holds c.75% of outstanding issued units in Regal REIT.

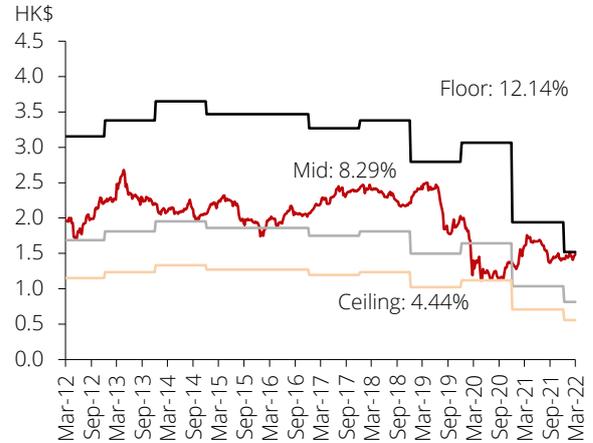
**Regal REIT**

**Price to book NAV band and historical yield band**

**Price to book NAV band**



**Historical yield band**



Source: Bloomberg Finance L.P. DBS HK

## Regal REIT

### Result Summary

FY Dec (HK\$m)	FY20	FY21	% Chg	Comments
Initial hotels	710.0	460.0	(35.2)	Only base rents are earned in both periods
iclub Wan Chai - non hotel portion	5.0	5.8	15.1	
iclub Sheung Wan	41.0	26.0	(36.6)	Only base rents are earned in both periods
iclub Fortress Hill	41.0	26.0	(36.6)	Only base rents are earned in both periods
iclub Ma Tau Wai	61.3	61.2	(0.3)	Only fixed rents are earned in both periods
Other income	2.1	2.1	0.6	
<b>Gross rental revenue</b>	<b>860.4</b>	<b>581.0</b>	<b>(32.5)</b>	
Gross hotel revenue	11.0	12.5	14.1	FY21: RevPAR at iclub Wanchai increasd 14.4% y-o-y
<b>Revenue</b>	<b>871.4</b>	<b>593.5</b>	<b>(31.9)</b>	
Property & hotel operating expenses	(13.3)	(14.6)	10.0	
<b>Net rental and hotel income</b>	<b>858.1</b>	<b>578.9</b>	<b>(32.5)</b>	
Interest and other income	1.2	0.3	(75.4)	
Depreciation	(8.3)	(7.7)	(6.7)	
FV change on investment prop.	(2,748.0)	309.3	n.a.	
REIT manager fee	(93.9)	(86.1)	(8.3)	
Trust, professional and other expense	(10.9)	(11.5)	5.4	
Finance cost	(220.6)	(151.4)	(31.4)	FY21: cash finance cost fell 35%
<b>Profit before tax</b>	<b>(2,222.4)</b>	<b>631.7</b>	<b>n.a.</b>	
Taxation	(87.4)	(54.6)	(37.5)	
Profit before distribution	(2,309.8)	577.1	n.a.	
<b>Distributable income</b>	<b>491.4</b>	<b>310.8</b>	<b>(36.8)</b>	
Interim DPU (HK\$)	0.060	0.045	(25.0)	
Final DPU (HK\$)	0.076	0.041	(46.1)	
Total DPU (HK\$)	0.136	0.086	(36.8)	

Source: Regal REIT

## Regal REIT

### Key Assumptions (%)

	2022F	2023F
Hotel RevPAR	10	100

Source: Company, DBS HK

### Segmental Breakdown (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
<b>Revenues (HK\$ m)</b>					
Rental Revenue	949	860	581	598	650
Hotel Revenue	27	11	13	17	25
<b>Total</b>	<b>976</b>	<b>871</b>	<b>594</b>	<b>615</b>	<b>675</b>

Source: Company, DBS HK

### Income Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Gross revenue	976	871	594	615	675
Property expenses	(20)	(13)	(15)	(15)	(16)
<b>Net Property Income</b>	<b>956</b>	<b>858</b>	<b>579</b>	<b>600</b>	<b>660</b>
Other expenses	(125)	(113)	(105)	(107)	(111)
Interest (Exp)/Inc	(317)	(219)	(151)	(212)	(268)
Exceptionals	(2,532)	(2,748)	309	0	0
<b>Pre-Tax Profit</b>	<b>(2,018)</b>	<b>(2,222)</b>	<b>632</b>	<b>282</b>	<b>281</b>
Tax	(84)	(87)	(55)	(50)	(50)
<b>Net Profit</b>	<b>(2,102)</b>	<b>(2,310)</b>	<b>577</b>	<b>232</b>	<b>231</b>
<b>Distribution income</b>	<b>404</b>	<b>443</b>	<b>280</b>	<b>220</b>	<b>223</b>
Revenue Gth (%)	(5)	(11)	(32)	4	10
NPI Gth (%)	(3)	(10)	(33)	4	10
Dist. Inc Growth (%)	(17)	10	(37)	(22)	1
DPU Growth (%)	(17)	10	(37)	(22)	1

Source: Company, DBS HK

## Regal REIT

### Balance Sheet (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Fixed Assets	24,539	21,829	22,149	22,161	22,187
Other LT Assets	614	545	589	591	592
Bank Balance/Cash & Liquid	196	333	153	134	133
Debtors	17	15	12	9	12
Other Non Cash Current	5	14	9	9	9
<b>Total Assets</b>	<b>25,370</b>	<b>22,735</b>	<b>22,912</b>	<b>22,905</b>	<b>22,934</b>
ST Debt	747	4,756	248	5,071	405
Creditors	82	82	57	57	57
Other Current Liab	54	26	26	26	26
LT Debt	9,184	5,292	9,744	4,921	9,587
Deferred Tax Liabilities	619	643	674	691	709
Other LT Liabilities	12	4	16	16	16
Unitholders' funds	14,671	11,931	12,147	12,122	12,133
<b>Total Capital</b>	<b>25,370</b>	<b>22,735</b>	<b>22,912</b>	<b>22,905</b>	<b>22,934</b>
Share Capital (m)	3,257	3,258	3,258	3,258	3,258
Gross Debt	(9,980)	(10,049)	(9,992)	(9,992)	(9,992)
Working Capital	(666)	(4,503)	(156)	(5,001)	(333)
Book NAV (HK\$)	4.50	3.66	3.73	3.72	3.72
Gross Gearing (%)	39	44	44	44	44

Source: DBS HK

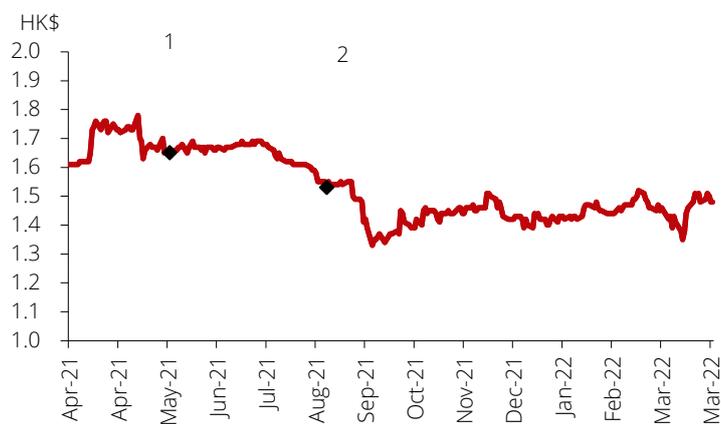
### Cash Flow Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Income	(2,018)	(2,222)	632	282	281
Tax Paid	(18)	(79)	(30)	(32)	(33)
Depr/Amort	9	8	8	8	8
Chg in Wkg.Cap.	6	13	(26)	(4)	(3)
Other Non-Cash	2,545	2,757	(305)	7	0
<b>Operational CF</b>	<b>525</b>	<b>478</b>	<b>278</b>	<b>260</b>	<b>254</b>
Net Capex	(46)	(60)	(17)	(22)	(35)
Assoc, MI, Invsmt	11	3	0	0	0
<b>Investment CF</b>	<b>(35)</b>	<b>(57)</b>	<b>(17)</b>	<b>(22)</b>	<b>(35)</b>
Net Chg in Debt	(3)	96	(56)	0	0
Distribution Paid	(469)	(378)	(394)	(257)	(220)
Other Financing CF	(18)	(27)	0	0	0
<b>Financing CF</b>	<b>(490)</b>	<b>(308)</b>	<b>(451)</b>	<b>(257)</b>	<b>(220)</b>
Chg in Cash	0	113	(190)	(19)	(1)

Source: Company, DBS HK

**Regal REIT**

**Target Price & Ratings History**



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	28-May-21	HK\$1.65	HK\$1.60	Hold
2:	25-Aug-21	HK\$1.55	HK\$1.60	Hold

Source: DBS HK

Analyst: Jeff Yau

## Regal REIT

DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**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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**Regal REIT**

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