

### SECTOR UPDATE

## REITs – Singapore

Weighing The Odds – Upside From Reopening Against Perceived Threat From Inflation

**Nascent signs of easing of inflationary pressure have emerged. The yield curve steepened again in May 22 and is currently upward-sloping, suggesting a soft landing. Economic expansion, if sustained despite geopolitical uncertainties, is positive for S-REITs. We stay invested in hospitality, retail and office REITs as reopening plays. BUY ART (Target: S\$1.25), FCT (Target: S\$2.79), FEHT (Target: S\$0.78) and LREIT (Target: S\$0.96). Maintain OVERWEIGHT.**

### WHAT'S NEW

- Freedom Day marks an orderly full-fledged reopening.** The easing of restrictions in Apr 22 marks the start of Singaporeans living with COVID-19 as an endemic disease. The easing benefits all sub-sectors of the S-REIT market, including hospitality, retail and office. Singapore's international borders are fully reopened to vaccinated travellers with the launch of the Vaccinated Travel Framework. Food & Beverage establishments are operating at full capacity as the cap on group size of 10 persons was lifted. All employees are allowed back to their workplaces.
- Nascent signs of easing of inflationary pressure have emerged.** US core PCE inflation peaked at 5.3% in Feb 22, the fastest pace in 30 years. Core PCE inflation eased 0.3ppt mom to 4.9% in Apr 22. The easing of inflationary pressure coincided with a pick-up in economic activities after new cases of the Omicron variant subsided. Implied inflation based on five-year Treasury Inflation-Protected Securities (TIPS) moderated from a peak of 3.6% in mid-April to the current 2.9%. The Congressional Budget Office expects CPI to ease to 4.7% in 4Q22 from 8.3% in Apr 22.
- Yield curve indicates a soft landing.** We expect a series of three successive 50bp hikes on 4 May 22, 15 Jun 22 and 27 Jul 22, followed by three successive 25bp hikes in September, November and December. US Fed Funds rate would thus hit 2.5% at end-22. The yield curve inverted temporarily in Apr 22, suggesting a potential slowdown. It steepened again in May 22 and is currently upward-sloping. Current short-end of the yield curve implies forward short-term interest rates at 2.1% for 1Y, 3.1% for 2Y and 3.1% for 3Y. The economy seems to be coping with external shocks.
- Commercial real estate is an important hedge against inflation.** Landlords could raise rents to keep abreast of inflation. Higher cost of construction reduces the competition for constrained future new supply. Appreciation in capital value could also lower loan-to-value ratio for mortgage debts. Landlords' ability to pass higher rents to tenants depends on fundamental factors, such as location of properties, demographics, migration trends, demand/supply dynamics and vacancy rate.

### ACTION

- Adapting to changes in macroeconomics and geopolitics.** S-REITs are not out of the woods yet but the gradual easing of inflationary pressure provides some respite. In light of the elevated government bond yields and inflationary pressure potentially pushing rents higher, we have utilised a higher risk-free rate of 3.0% (previous: 2.0%) and pushed terminal growth higher by 0.8ppt in our DDM valuations for S-REITs. On average, we have adjusted target prices for 20 S-REITs under our coverage lower by 5%.

### PEER COMPARISON

Name	Ticker	Rec	Price 31 May 22	Target Price	Mkt Cap (US\$m)	Yield (%) Hist	Yield (%) Curr	Yield (%) Fwd 1Y	Yield (%) Fwd 2Y	Debt to Equity (%)	Debt to Assets (%)	P/NAV (x)
Ascott Trust	ART SP	BUY	1.16	1.25	2,783	3.7	4.4	5.4	5.3	70.4	37.8	1.00
Far East HTrust	FEHT SP	BUY	0.65	0.78	941	4.0	4.4	5.9	6.1	44.8	33.4	0.77
Frasers CT	FCT SP	BUY	2.34	2.79	2,907	5.2	5.5	5.6	5.5	46.1	33.3	1.01
Lendlease REIT	LREIT SP	BUY	0.82	0.96	1,284	5.7	5.6	6.4	6.4	68.3	27.7	1.02

Source: Bloomberg, UOB Kay Hian

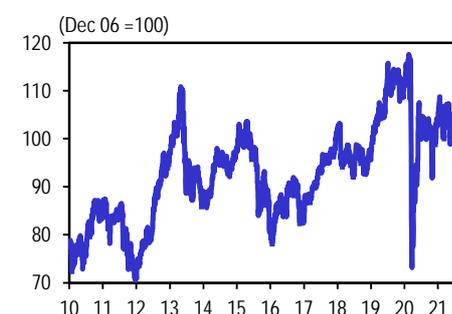
## OVERWEIGHT (Maintained)

### TOP PICKS

Company	Rec	Share Price (S\$)	Target Price (S\$)
ART	BUY	1.16	1.25
FCT	BUY	2.34	2.79
FEHT	BUY	0.65	0.78
LREIT	BUY	0.82	0.96

Source: UOB Kay Hian

### FTSE ST ALL-SHARE REITS INDEX



Source: UOB Kay Hian

### S-REIT YIELD SPREAD\*



\*Yield spread above 10-year Singapore government bond yield.

Source: UOB Kay Hian

### ANALYST(S)

**Jonathan Koh, CFA**  
 +65 6590 6620  
 jonathankoh@uobkayhian.com

- **BUY hospitality REITs as reopening plays.** Hospitality REITs benefit from the resurgence and pent-up demand for travel. Tickets for Formula 1 Singapore Grand Prix in Sep 22 have already sold out and MICE events should pick-up in 2H22.

### Ascott Residence Trust (BUY/ART SP/Target: S\$1.25).

- ART benefits from strong pick-up since Mar 22 in countries with large domestic markets, such as the US, the UK, Japan and Australia. Longer-stay properties already accounted for 28% of gross profit in 1Q22.

### CDL Hospitality Trusts (BUY/CDREIT SP/Target: S\$1.48).

- Singapore fully reopened its international borders to vaccinated travellers in Apr 22. UK and Maldives are expected to turn in good performances.

### Far East Hospitality Trust (BUY/FEHT SP/Target: S\$0.78).

- Completed the divestment of Central Square for S\$313.2m on 24 Mar 22. Aggregate leverage has dropped 4.9ppt qoq to 33.4% in 1Q22.

- **BUY retail REITs as reopening plays.** Downtown malls benefit from the return of office workers in 2Q22 and tourists in 2H22. Tourists accounted for 22.3% of retail sales excluding motor vehicles in 2019 (pre-COVID-19).

### Frasers Centrepoint Trust (BUY/FCT SP/Target: S\$2.79)

- Tenant sales have surpassed pre-COVID-19 levels since Oct 21. Occupancy cost has eased to 16.2% in 1HFY22 (FY21: 17.5%).

### Lendlease Global Commercial REIT (BUY/LREIT SP/Target: S\$0.96)

- Jem became LREIT's largest asset (46.8% of AUM) after the acquisition of the remaining 68.2% stake was completed on 22 Apr 22. Multi-functional event space at Grange Road Car Park is scheduled to be operational by early-23.

- **BUY office REITs as reopening plays.** CBRE forecast rents for Grade A Core CBD to recover 6.9% to S\$11.55psf/month in 2022. Amazon and Meta Platforms are said to be taking office space at IOI Central Boulevard Towers, which is to be completed in 4Q23.

### Keppel REIT (BUY/KREIT SP/Target: S\$1.41).

- KREIT is finalising lease documentation with a few prospective tenants, which would improve portfolio occupancy by 1.9ppt to 97% if successfully signed.

- **Selective BUYs for defensive and counter-cyclical yield plays.** From a bottom-up basis, we have picked three defensive S-REITs ELITE, KORE and UHU that provide attractive yields of 7.7%, 8.7% and 9.8% respectively.

### Elite Commercial REIT (BUY/ELITE SP/Target: £0.83).

- Renegotiation of lease terms led to break clauses being removed from 108 DWP leases. We estimate the step-up in rents at 15.4% for Apr 23.

### Keppel Pacific Oak US REIT (BUY/KORE SP/Target: US\$1.01).

- Management guided positive rent reversion at mid-single-digit in 2022, driven by Seattle and Sacramento. The redevelopment of multi-family units atop the car park at The Plaza Buildings will be finalised over the next two quarters.

### United Hampshire US REIT (BUY/UHU SP/Target: US\$0.88).

- Occupancy of Grocery & Necessity Retail Properties improved 1.1ppt qoq to 96.4% in 1Q22. UHU plans to focus on acquisition of strip centres along the East Coast.

## SECTOR CATALYSTS

- Hospitality, retail and office REITs benefitting from reopening of the economy.
- Limited new supply for office, logistics and retail segments in 2021.

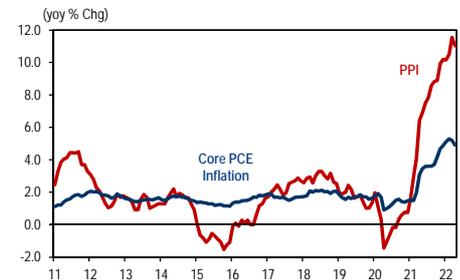
## ASSUMPTION CHANGES

- We keep our earnings forecasts unchanged.

## RISKS

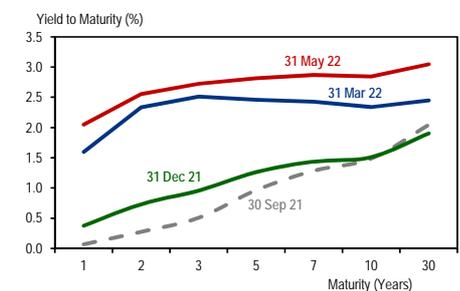
- Escalation of the Russia-Ukraine war beyond Ukraine.

## US CORE PCE INFLATION VS PPI



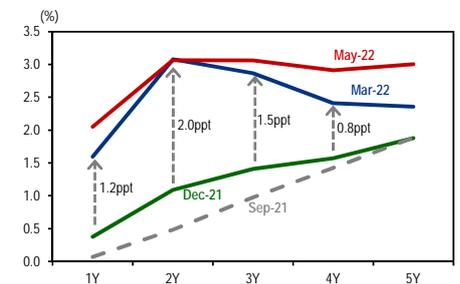
Source: CEIC

## US YIELD CURVE



Source: Bloomberg, UOB Kay Hian

## IMPLIED SHORT-TERM INTEREST RATES



Source: Bloomberg, UOB Kay Hian

### PEER COMPARISON

Name	Ticker	Rec	Curr	Price 31 May 22	Old TP	New TP	Mkt Cap (US\$m)	Yield (%)				Debt to Equity (%)	Debt to Assets (%)	P/NAV (x)
								Hist	Curr	Fwd 1Y	Fwd 2Y			
<b>HEALTHCARE</b>														
First REIT	FIRT SP	NR	S\$	0.285	n.a.	n.a.	427	9.2	n.a.	n.a.	n.a.	66.3	35.5	0.82
PLife REIT	PREIT SP	HOLD	S\$	4.94	4.82	4.65	2,182	2.9	3.0	3.0	3.1	55.2	34.4	2.08
<b>HOSPITALITY</b>														
Ascott Trust	ART SP	BUY	S\$	1.16	1.32	1.25	2,783	3.7	4.4	5.4	5.3	70.4	37.8	1.00
CDL HTrust	CDREIT SP	BUY	S\$	1.25	1.57	1.48	1,127	3.4	4.2	5.3	5.9	68.6	39.8	0.94
Far East HTrust	FEHT SP	BUY	S\$	0.65	0.82	0.78	941	4.0	4.4	5.9	6.1	44.8	33.4	0.77
Fraser HTrust	FHT SP	NR	S\$	0.65	n.a.	n.a.	914	1.5	3.2	3.4	5.4	78.7	42.3	0.99
<b>INDUSTRIAL</b>														
AIMS APAC REIT	AAREIT SP	NR	S\$	1.38	n.a.	n.a.	722	6.9	7.1	7.4	7.5	85.9	37.5	0.99
Ascendas REIT	AREIT SP	BUY	S\$	2.79	3.92	3.70	8,550	5.5	6.0	6.1	6.1	61.6	36.8	1.17
DigiCore REIT USD	DCREIT SP	HOLD	US\$	0.965	1.10	1.03	1,088	n.a.	4.2	4.9	4.4	35.4	26.0	1.10
ESR-LOGOS REIT	EREIT SP	NR	S\$	0.41	n.a.	n.a.	1,997	7.3	7.3	7.6	7.8	74.5	39.5	1.11
Keppel DC REIT	KDCREIT SP	NR	S\$	2.06	n.a.	n.a.	2,583	4.8	4.9	5.1	5.2	56.3	36.1	1.54
Mapletree Ind Trust	MINT SP	BUY	S\$	2.48	3.65	3.41	4,847	5.6	5.4	5.6	5.7	58.3	38.4	1.33
Mapletree Log Trust	MLT SP	BUY	S\$	1.64	2.23	2.09	5,726	5.4	5.6	5.6	5.7	70.1	36.8	1.11
<b>OFFICE</b>														
Keppel REIT	KREIT SP	BUY	S\$	1.15	1.50	1.41	3,125	5.1	5.1	4.9	5.4	71.6	38.4	0.89
<b>RETAIL</b>														
Fraser CT	FCT SP	BUY	S\$	2.34	2.96	2.79	2,907	5.2	5.5	5.6	5.5	46.1	33.3	1.01
Lendlease REIT	LREIT SP	BUY	S\$	0.82	1.01	0.96	1,284	5.7	5.6	6.4	6.4	68.3	27.7	1.02
Mapletree NAC Trust	MAGIC SP	NR	S\$	1.21	n.a.	n.a.	3,126	5.6	5.8	5.9	6.2	82.3	41.5	0.98
Sasseur REIT	SASSR SP	BUY	S\$	0.825	1.12	1.12	736	8.6	9.2	9.3	9.7	42.5	26.2	0.83
SPH REIT	SPHREIT SP	NR	S\$	0.945	n.a.	n.a.	1,935	5.7	5.8	5.9	6.1	50.2	30.2	1.03
Starhill Global	SGREIT SP	NR	S\$	0.585	n.a.	n.a.	956	6.8	6.7	7.2	7.4	61.8	36.1	0.73
<b>DIVERSIFIED</b>														
CapLand China Trust	CLCT SP	NR	S\$	1.16	n.a.	n.a.	1,416	7.5	7.9	8.5	8.7	78.6	38.1	0.74
CapLand Int Comm Trust	CICT SP	HOLD	S\$	2.19	2.50	2.33	10,599	4.7	5.2	5.5	5.6	63.2	39.1	1.06
Fraser L&C Trust	FLT SP	BUY	S\$	1.36	1.79	1.68	3,665	5.6	5.6	5.7	5.8	55.7	33.1	1.03
Mapletree Comm Trust	MCT SP	BUY	S\$	1.78	2.52	2.36	4,324	5.4	5.8	5.7	5.8	52.0	33.5	1.02
OUE Comm REIT	OUECT SP	NR	S\$	0.395	n.a.	n.a.	1,573	6.6	6.6	6.3	3.0	73.8	39.4	0.69
Suntec REIT	SUN SP	HOLD	S\$	1.68	1.90	1.80	3,520	5.2	6.1	6.0	5.7	81.8	43.3	0.79
<b>INTERNATIONAL REITS</b>														
Cromwell REIT EUR	CERT SP	NR	€	2.05	n.a.	n.a.	1,237	8.3	8.3	8.5	8.8	72.1	38.6	0.83
Elite Comm REIT GBP	ELITE SP	BUY	£	0.645	0.87	0.83	390	8.4	7.9	7.7	8.2	79.6	42.8	1.09
IREIT Global	IREIT SP	NR	S\$	0.62	n.a.	n.a.	523	6.9	7.1	7.1	8.1	53.7	32.1	0.79
KepPacOak REIT USD	KORE SP	BUY	US\$	0.695	1.07	1.01	726	9.1	9.1	8.7	8.6	66.4	37.5	0.85
Manulife REIT USD	MUST SP	BUY	US\$	0.60	0.80	0.80	1,058	8.9	9.4	9.7	10.0	81.8	42.8	0.89
Prime US REIT USD	PRIME SP	NR	US\$	0.715	n.a.	n.a.	841	9.5	9.8	9.9	10.1	66.9	39.1	0.85
Utd Hampshire REIT USD	UHU SP	BUY	US\$	0.615	0.92	0.88	344	9.9	10.1	9.8	9.8	65.1	38.9	0.82

Source: Bloomberg, UOB Kay Hian

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