

Champion REIT

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DBS Group Research . Equity

24 Jul 2023

HOLD

Last Traded Price (21 Jul 2023): HK\$2.79 (HSI : 19,075)
Price Target 12-mth: HK\$3.09 (11% upside) (Prev HK\$3.51)

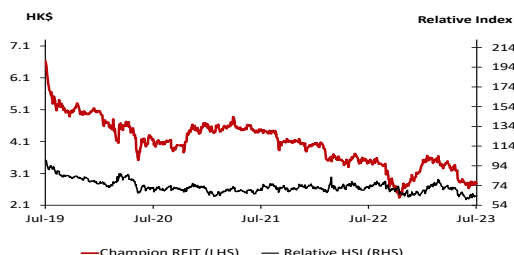
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What's New

- Leasing enquiries for Three Garden Road have improved but pace of transactions still slow
- Office reversionary growth for both Three Garden Road & Langham Office Tower to stay negative in FY23
- Tenant sales growth at Langham Place Mall outperformed the overall retail market
- Revised TP down to HK\$3.09 due to higher interest rate outlook, maintain HOLD

Price Relative



Forecasts and Valuation

FY Dec (HK\$ m)	2021A	2022A	2023F	2024F
Gross Revenue	2,769	2,625	2,554	2,549
Net Property Inc	2,197	2,031	1,959	1,950
Net Profit	(831)	(749)	1,012	911
Distribution Inc	1,353	1,168	1,000	909
DPU (HK\$)	0.23	0.20	0.17	0.15
DPU Gth (%)	(9)	(14)	(15)	(10)
Div Yield (%)	8.2	7.0	6.0	5.4
Gross Gearing (%)	23	22	22	22
Book Value (HK\$)	8.25	7.91	7.88	7.90
P/Book Value (x)	0.3	0.4	0.4	0.4

DPU Rev (%)			(5)	(14)
Consensus DPU (HK\$):			0.20	0.21
Other Broker Recs:		B:1	S:9	H:1

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

Recovery stays remote

Investment Thesis

Quality mix of commercial assets. Three Garden Road is the largest property held by Champion REIT, representing c.61% of the REIT's total portfolio valuation. With a GFA of 1.6msf, this prime Central Grade A Office tower is home to numerous MNCs and Chinese corporates. Sitting atop Mongkok station, Langham Place Office is a hub for lifestyle tenants, including fitness centre, beauty parlours and medical centres, which occupy c.71% of the property's gross lettable area. Its only retail asset, Langham Place Mall, is a popular shopping destination among locals and tourists with a GFA of 0.59msf.

Office earnings shortfall more than offset retail earnings recovery .

Occupancy at Three Garden Road currently stands at c.83%. Against the backdrop of subdued office demand, rental reversions for 40% of leases scheduled for renewal/rent review in FY23 should remain in negative territory. Meanwhile, Langham Place Office should see slightly lower income as a result of mild negative rental reversions. These, despite earnings recovery at Langham Place Mall led by the revival of tourist spending, should continue to drag on the REIT's rental earnings in the near term.

Uncertain office market outlook to cast a shadow on its unit price

performance. Despite increased enquiries following border re-opening, global macro uncertainties and lingering US-China tensions should continue to be a drag on Grade A office demand. This should cloud the near-term prospects of Three Garden Road, which contributed c.60% of the REIT's NPI in FY22, and hence its unit price performance.

TP adjusted to HK\$3.09 amid prolonged interest rate outlook, maintain

HOLD. The stock offers distribution yields of 6.0-5.4% for FY23-24. This translates into yield spreads of 2.3%-1.7%, below its 10-year average of 3.5%. We have revised down our target price to HK\$3.09 primarily reflecting higher interest rate outlook. Our target price for Champion REIT is based on the Dividend Discount Model using 7.7% discount rate and terminal growth rate of 1%.

Key Risks to Our View:

Any stronger-than-expected recovery of office leasing demand from MNCs and Chinese corporates should boost the income recovery of Three Garden Road and Champion REIT, and hence its unit price performance.

At A Glance

Issued Capital (m shrs)	5,974
Mkt Cap (HKm/US\$m)	16,667 / 2,132
Major Shareholders (%)	
Great Eagle Holdings Ltd	59.5
Eagle Asset Management (CP) Ltd.	9.2
Free Float (%)	31.2
3m Avg. Daily Val. (US\$m)	0.7
GICS Industry: Real Estate / Equity Real Estate Investment	

Champion REIT

WHAT'S NEW**Office reversionary growth stays in negative territory**

Leasing enquiries for Three Garden Road has picked up following the full relaxation of travel restrictions in early 2023, mainly driven by financial institutions within Central. Yet, transactions have remained stagnant as tenants remain cost conscious amid global macro uncertainties and are more selective on the back of high vacancy rate and increased supply. Despite the departure of Invesco in 1Q23, occupancy at Three Garden Road was stable at c.83% (Dec-22: 82.7%) thanks to in-house expansion of an existing tenant. In FY23, about 12% of leases in term of gross rental area, are scheduled for renewal with another 28% up for rent review. Of these, >50% has been concluded. While spot rents have stabilized at >HK\$80psf, rental reversion is expected to stay in negative territory due to high expiring rents of >HK\$100psf.

About 42% of floor area at Langham Place Office Tower is scheduled for roll over in FY23. Thus far, Champion REIT has concluded >50% of these lease renewals. This should underpin its occupancy, which stood at 93.3% as of Dec-22, in the near term. The portion of space occupied by lifestyle tenants has remained stable at 71%. With the improved sentiment following the border reopening with China, spot rents at Langham Place Office have stabilized at >HK\$40psf. Hence, we forecast a mild negative rental reversion for the property in FY23 given expiring rents at c.HK\$46psf.

Tenant sales at Langham Place Mall has outperformed the general Hong Kong retail market, which registered 21% growth in 5M23. This was mainly driven by the robust sales growth from tourist-

oriented trades, cosmetics in particular. This points to robust turnover rent growth in FY23. Coupled with the rental correction over the past few years, occupancy cost ratio has lowered to 19-20%, on par with the level prior to the pandemic outbreak. Hence, rental reversions for 39% of leases to be renewed in FY23 is expected to resume positive growth. The mall remains fully let.

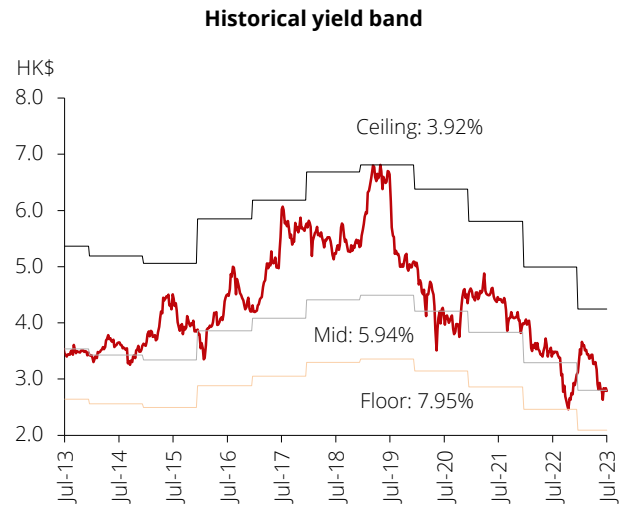
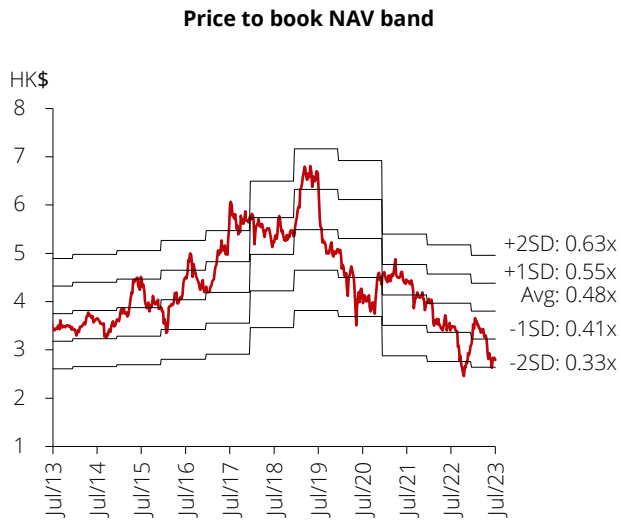
Champion REIT is trading at 6.0-5.4% distribution yield for FY23-24. This translates into yield spreads of 2.3-1.7%, below its 10-year average of 3.5%. High vacancy rate and subdued leasing demand should continue to cap rental growth at Three Garden Road in the near term. Hence, this would weigh on the performance of the REIT's largest property, which accounted for c.60% of its FY22 NPI. This, coupled with the negative rental reversions at Langham Place Office, should more than offset the earnings recovery from Langham Place Mall led by the revival of tourist spending. With earnings recovery still remote, we maintain our HOLD call with a DDM-based TP of HK\$3.09.

Company Background

Champion REIT has exposure to both office and retail sectors. Listed in May-2006, the REIT owns Three Garden Road in Central and Langham Place's office and retail portions in Mong Kok with total GRA of 2.93m sf. Champion REIT also owns 27% stake in 66 Shoe Lane, an office property in London.

Champion REIT

Price to book NAV band and historical yield band



Source: Bloomberg Finance L.P. DBS HK

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Key Assumptions (%)

	2023F	2024F
Office rental - HK	(5)	0
Retail rental (Shopping centre) - HK	5	5

Source: Company, DBS HK

Segmental Breakdown (HK\$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Revenues (HK\$ m)					
Rental income	2,558	2,417	2,286	2,199	2,181
Carpark income	41	47	44	48	49
Building management fee	287	274	266	276	287
Rental related income	34	31	29	31	32
Total	2,920	2,769	2,625	2,554	2,549

Source: Company, DBS HK

Income Statement (HK\$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Gross revenue	2,920	2,769	2,625	2,554	2,549
Property expenses	(573)	(572)	(595)	(595)	(599)
Net Property Income	2,347	2,197	2,031	1,959	1,950
Other expenses	(308)	(290)	(273)	(263)	(263)
Joint ventures	0	22	(43)	19	19
Interest (Exp)/Inc	(418)	(349)	(421)	(527)	(637)
Exceptionals	(13,847)	(2,156)	(1,818)	0	0
Pre-Tax Profit	(12,226)	(575)	(524)	1,187	1,069
Tax	(271)	(256)	(225)	(175)	(158)
Net Profit	(12,497)	(831)	(749)	1,012	911
Distribution income	1,477	1,353	1,168	1,000	909
Revenue Gth (%)	(5)	(5)	(5)	(3)	0
NPI Gth (%)	(5)	(6)	(8)	(4)	0
Dist. Inc Growth (%)	(6)	(8)	(14)	(14)	(9)
DPU Growth (%)	(6)	(9)	(14)	(15)	(10)

Source: Company, DBS HK

Champion REIT

Balance Sheet (HK\$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Fixed Assets	67,318	65,296	63,555	63,570	63,903
Long-term Investments	320	301	253	253	253
Other LT Assets	0	16	112	112	112
Associates/JVs	0	313	239	239	239
Bank Balance/Cash & Liquid	1,834	1,629	735	778	878
Debtors	317	286	233	233	233
Other Non Cash Current	1,904	33	102	102	102
Total Assets	71,693	67,873	65,229	65,287	65,720
ST Debt	3,442	2,026	4,244	5,364	1,654
Creditors	2,115	1,505	1,423	1,423	1,423
Other Current Liab	1,564	1,387	1,275	1,204	1,199
LT Debt	12,956	13,262	10,276	9,155	12,865
Deferred Tax Liabilities	0	0	0	0	0
Other LT Liabilities	759	730	784	784	784
Unitholders' funds	50,858	48,963	47,228	47,357	47,795
Total Capital	71,693	67,873	65,229	65,287	65,720
Share Capital (m)	5,906	5,937	5,974	6,012	6,054
Gross Debt	(16,397)	(15,289)	(14,519)	(14,519)	(14,519)
Working Capital	(3,066)	(2,971)	(5,871)	(6,877)	(3,062)
Book NAV (HK\$)	8.61	8.25	7.91	7.88	7.90
Gross Gearing (%)	23	23	22	22	22

Source: DBS HK

Cash Flow Statement (HK\$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Pre-Tax Income	(12,226)	(575)	(524)	1,187	1,069
Tax Paid	(467)	(269)	(225)	(175)	(158)
Joint Venture	0	(22)	43	(19)	(19)
Chg in Wkg.Cap.	(191)	136	(30)	0	0
Other Non-Cash	13,961	2,226	1,846	65	59
Operational CF	1,076	1,495	1,110	1,058	952
Net Capex	0	(27)	(15)	(15)	(15)
Net change in asso/jv	0	(291)	0	0	0
Associates' div	0	2	(43)	19	19
Assoc, MI, Invsmt	(1,104)	1,441	(93)	53	58
Investment CF	(1,104)	1,125	(151)	56	62
Net Chg in Debt	1,416	(1,170)	(643)	0	0
New issues/Unit Buyback	0	0	0	0	0
Distribution Paid	(1,507)	(1,463)	(1,276)	(1,071)	(913)
Other Financing CF	0	0	0	0	0
Financing CF	(91)	(2,633)	(1,919)	(1,071)	(913)
Chg in Cash	(119)	(13)	(960)	43	100

Source: Company, DBS HK

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Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	Target Price	Rating
1	22-Aug-22	HK\$3.48	HK\$3.70	HOLD
2	21-Oct-22	HK\$2.67	HK\$3.21	HOLD
3	15-Feb-23	HK\$3.55	HK\$3.53	HOLD
4	27-Feb-23	HK\$3.51	HK\$3.51	HOLD

Source: DBS HK

Analyst: Percy Leung

Jeff Yau

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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