

Singapore Company Guide

CapitaLand Retail China Trust

Edition 1 Version 1 | Bloomberg: CRCT SP | Reuters: CRCT.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

26 Oct 2015

BUY

Last Traded Price: S\$1.50 (STI : 3,068.46)
Price Target : S\$1.69 (12% upside plus 7% yield)

Potential Catalyst: Further acquisitions and delivery of positive rental reversions

Where we differ: Below consensus due to lower top line

Analyst

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Price Relative



Forecasts and Valuation

FY Dec (\$ m)	2014A	2015F	2016F	2017F
Gross Revenue	203	215	227	235
Net Property Inc	132	138	148	155
Total Return	145	81	86	90
Distribution Inc	81	90	95	99
EPU (S cts)	4.9	9.7	10.1	10.2
EPU Gth (%)	12	98	4	2
DPU (S cts)	9.8	10.6	11.0	11.1
DPU Gth (%)	9	8	4	2
NAV per shr (S cts)	163.0	168.7	164.8	161.0
PE (X)	30.8	15.5	14.9	14.7
Distribution Yield (%)	6.5	7.0	7.3	7.4
P/NAV (x)	0.9	0.9	0.9	0.9
Aggregate Leverage (%)	28.5	28.3	29.0	29.4
ROAE (%)	3.1	5.8	6.0	6.3

Distn. Inc Chng (%)	-	-	-
Consensus DPU (S cts)	10.8	11.0	11.7
Other Broker Recs:	B: 6	S: 0	H: 3

Source of all data: Company, DBS Bank, Bloomberg Finance L.P

ALLAYING GROWTH FEARS

Over-reaction to China slowdown vs a strong set of 3Q15 results. CRCT has corrected c.14% since end-Jun-15 on the back of Chinese growth fears. We believe this is an over-reaction as CRCT has delivered another strong set of results with 3Q15 DPU rising 12.3% y-o-y to 2.64 Scts. In addition, during 3Q15, CRCT's malls continue to deliver healthy tenants sales (+12.7%) and positive rental reversions (+8.9%). With CRCT trading at 0.9x book and offering an attractive FY15-17F DPU of 7.0-7.4% yield, we maintain our BUY recommendation and S\$1.69 TP.

Investment opportunity during earnings lull. With several of CRCT's malls still ramping up or in a transition phase, CRCT offers an opportunity to invest during an earnings lull before an uptick in growth. For example, Grand Canyon (acquired in 2014) is generating a 9M15 annualised NPI yield of only c.5% (based on the original acquisition price) versus target range of 7-8%. Meanwhile, Minzhongleyuan and Wuhu are incurring losses due to nearby road closures and reposition works respectively. Upon stabilisation of these three malls, we estimate 14% upside from our FY15F NPI. This is on top of the expected 4% CAGR in NPI for CRCT's other multi-tenanted malls over the next three years. Additional upside to earnings could also come from the strengthening of the CNY.

Low gearing provides upside from acquisitions. CRCT's gearing of only 28.5% (as at end Sep15) versus the new 45% limit imposed by MAS, places CRCT in a strong position to pursue DPU-accretive acquisitions.

Valuation:

With a 19% 12-month total return (12% capital upside and 7.0% yield), we maintain BUY and TP of S\$1.69. We expect the delivery of DPU growth in the coming year should allay investors' fears over possible negative rental reversions and trigger a re-rating from the current depressed levels.

Key Risks to Our View:

Significant downturn in China. The key risk to our positive view is if China experiences a hard landing which would result in lower-than-expected or negative growth in retail sales. This in turn would translate into lower rents and DPU for CRCT.

At A Glance

Issued Capital (m shrs)	842
Mkt. Cap (S\$m/US\$m)	1,263 / 903
Major Shareholders	
Retail Crown (%)	19.1
Capitamall Trust (%)	14.4
Matthews International (%)	6.9
Free Float (%)	54.2
3m Avg. Daily Val (US\$m)	1.2

ICB Industry : Real Estate / Real Estate Investment Trust

CRITICAL DATA POINTS TO WATCH

Earnings Drivers:

Momentum from past positive rental reversions to still flow through. CRCT's malls on average have achieved tenant sales of 14% (between 9.5-21.3%) over the last 2.5 years, resulting in underlying positive rental reversions of 10.0-24.9% each. We believe the momentum from the rental uplifts delivered over the last 11 quarters should continue to flow through especially as Grand Canyon (which was acquired in 2014) has yet to stabilise. Grand Canyon's 9M15 annualised NPI yield stood at c.5% versus CRCT's long-term target of 7-8%. Going forward, with continued growth in retail sales (China retail sales were up 10.8% in Aug-15) on the back of urbanisation trend and shift towards a consumption-based economy, we estimate that CRCT's multi-tenanted malls (excluding Minzhongleyuan and Wuhu) should deliver NPI CAGR of 4.5% over the next three years.

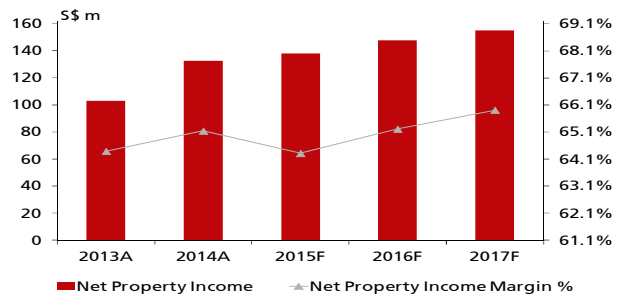
Couple of malls yet to make meaningful contribution. Two of CRCT's malls, Minzhongleyuan (MZLY) and Wuhu are currently making small losses. MZLY is impacted by road closures to facilitate the construction work of a new subway line which is due to be completed at end-2016. Meanwhile, the Wuhu mall is being repositioned given a softer operating environment in Wuhu (impact of change in catchment area and heightened completion). We estimate that the increased accessibility at MZLY from 2017 and successful repositioning of Wuhu could potentially result in a 9% uplift in CRCT's FY15F NPI over the next 3-5 years.

AEI and strategic initiatives to strengthen long-term positioning. To strengthen the competitive positioning of CRCT's portfolio and provide incremental earnings, CRCT is planning to undertake AEI at Wangjing. This will involve the construction of a link way to the new MRT station and rejuvenation of the mall façade. We believe this, combined with the recent decision to introduce popular international brands at Wangjing and Grand Canyon despite the short-term hit to rents (positive rental reversions dipped to 4.6% in 2Q15 from 12.8% in 1Q15), should ensure that CRCT's malls are well positioned and can generate sustainable NPI growth in the long term.

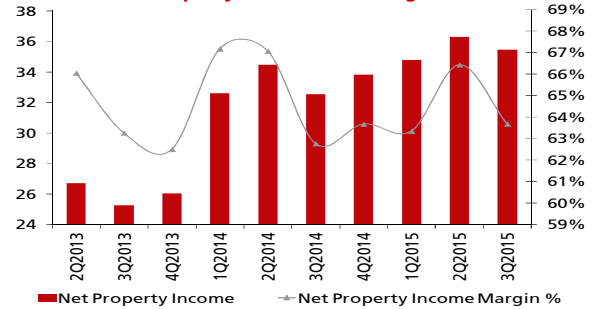
Income stability from master leased properties. CRCT's three master leased properties, Anzhen, Erqi and Shuangjing had a WALE (by GRI) of 10.6, 11.9 and 9 years respectively at end-Mar-15. Contributing an estimated c.22% of FY15F NPI, the three malls provide significant cashflow visibility and income stability for the REIT.

3Q15 results inline. CRCT delivered another good set of results despite the challenges at its MZLY and Wuhu malls with 3Q15 DPU increasing 12.3% y-o-y to 2.64 Scts. The results were underpinned by a stronger CNY versus SGD, as well as NPI in CNY terms for CRCT's core operating malls rising 7% (+8.7% excluding the master leased properties). Including MZLY and Wuhu, total group 3Q15 NPI in CNY terms was up 0.6% and up 9.1% in SGD terms.

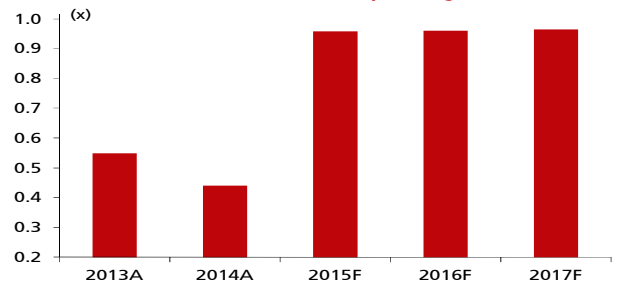
Net Property Income and Margins (%)



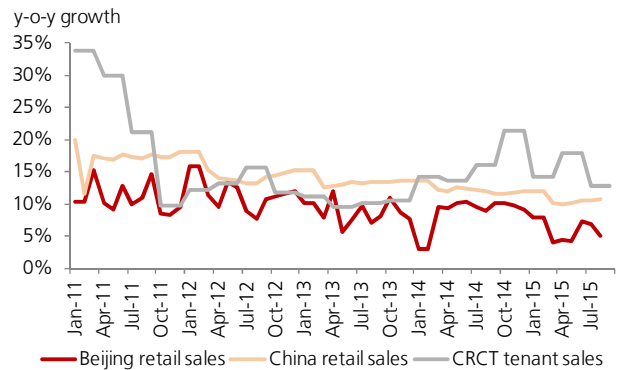
Net Property Income and Margins (%)



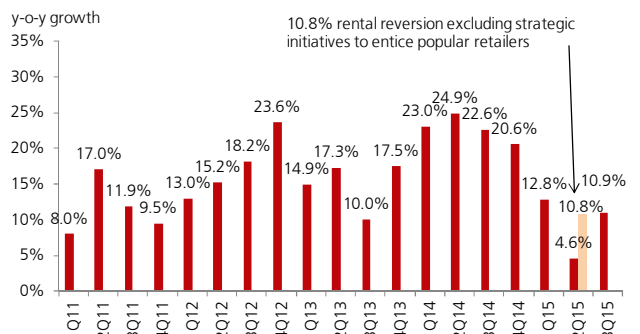
Distribution Paid / Net Operating CF



CRCT's tenants sales as well as China and Beijing retail sales still growing despite growth fears



Positive rental reversions



Source: Beijing Bureau of Statistics, Bloomberg, Company, DBS Bank

Balance Sheet:

Low gearing. CRCT had a low gearing of 28.5% as at end-Sep-15. This provides the REIT with the financial flexibility to pursue further acquisitions, especially in light of MAS's new 45% gearing limit. Previously, CRCT could only increase its gearing to 35% as it did not have a credit rating.

Moderate exposure to interest rates. With 77.5% of CRCT's debt fixed, the REIT has a moderate exposure to rising interest rates. Nevertheless, we have imputed a 50-bp increase in CRCT's current all-in cost of debt from the current 2.98% level over the next two years.

Share Price Drivers:

Strengthening CNY versus SGD. With all of CRCT's assets and earnings sourced from China, the strengthening CNY versus SGD should provide a tailwind to distributions paid in SGD as CRCT does not hedge its income exposure. In addition, the appreciation of CNY should also boost CRCT's NAV per share which now stands at S\$1.68 (net of distribution).

Positive rental revisions. Despite the concerns over the economic outlook for China weighing on CRCT, we believe delivery of positive rental reversions and DPU growth should allay such concerns. In our view, uplift in rents will be underpinned by continued tenant sales growth which was up 12.7% y-o-y in 3Q15. Furthermore, continued DPU growth should also be boosted by increased contribution from CapitaMall Grand Canyon as the full benefits from tenant remodeling have yet to be realised.

Key Risks:

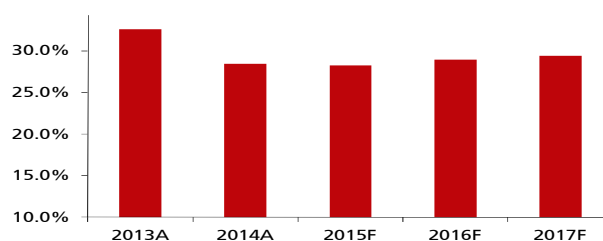
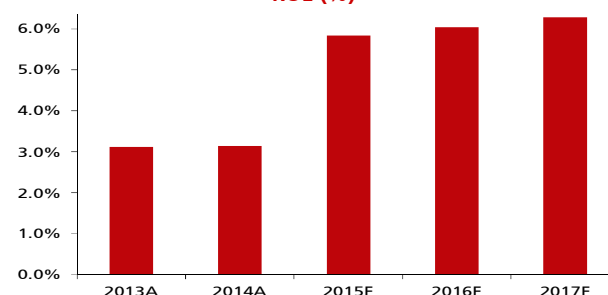
Threat from e-commerce. As consumers are now purchasing more goods online, sales at shopping malls may decline, causing rents at CRCT's properties to be negatively impacted. This threat is partially mitigated by the fact that c.42% of CRCT's GRI is sourced from tenants in the F&B (23% of GRI), supermarket (10%), leisure & entertainment (3%), education (3%) and beauty & healthcare (3%) sectors which are more immune to the e-commerce threat.

New mall supply in Beijing. According to Savills, the supply of mid- to high-end malls in Beijing is expected to increase by 10% in 2015. This may pressurise the rents at CRCT's malls. This risk is partially mitigated by the fact that c.80% of the new supply is located out of the core retail areas where CRCT's malls are situated. In addition, approximately 19% of CRCT's Beijing NPI is underpinned by master leases.

Currency risk. As 100% of CRCT's income is derived in CNY and it does not hedge its income, depreciation of the CNY against the SGD would result in lower DPU to unitholders.

COMPANY BACKGROUND

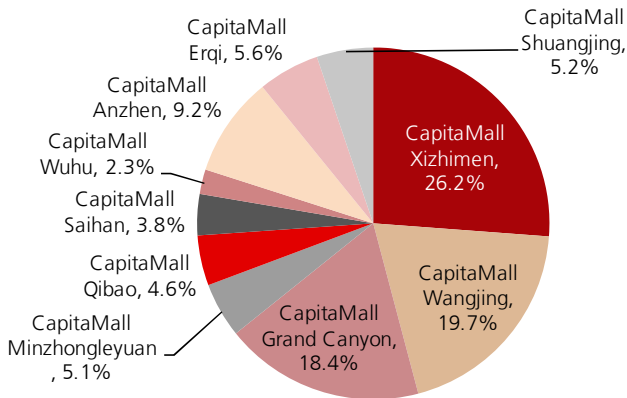
CapitaLand Retail China Trust (CRCT) is a real estate investment trust which invests in income-producing retail properties located mainly in China, Hong Kong and Macau.

Aggregate Leverage (%)**ROE (%)****Distribution Yield (%)****PB Band (x)**

Source: Company, DBS Bank

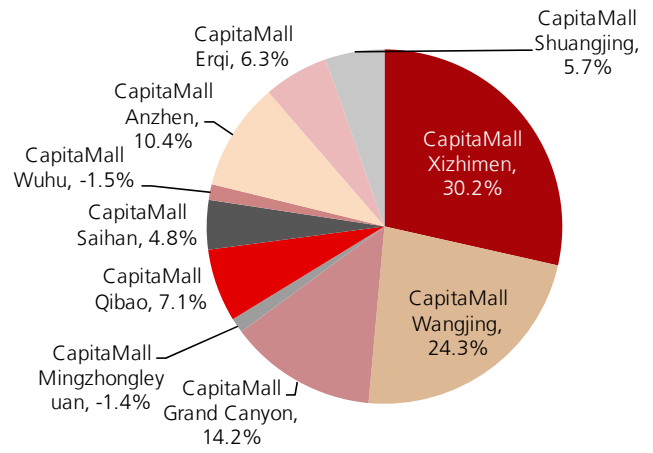
Appendix - Overview of CapitaLand Retail China Trust

Valuation by mall (30 June 2015)



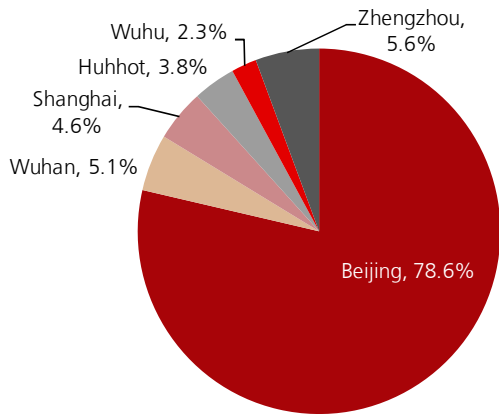
Source: CRCT, DBS Bank

9M15 NPI by mall



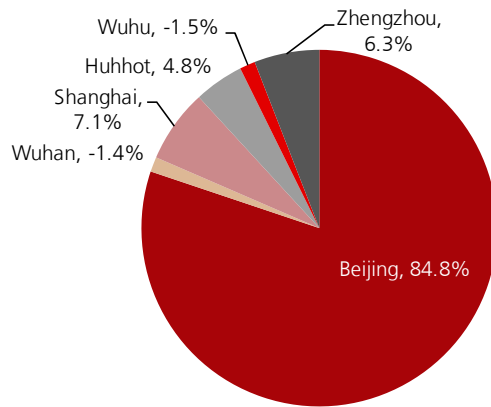
Source: CRCT, DBS Bank

Valuation by city as at 30 June 2015



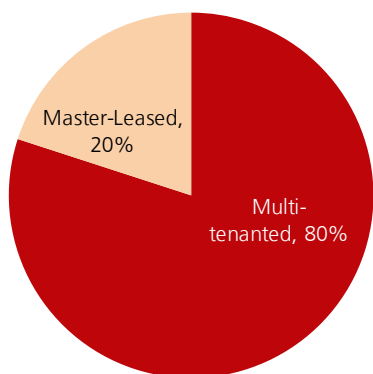
Source: CRCT, DBS Bank

9M15 NPI by city



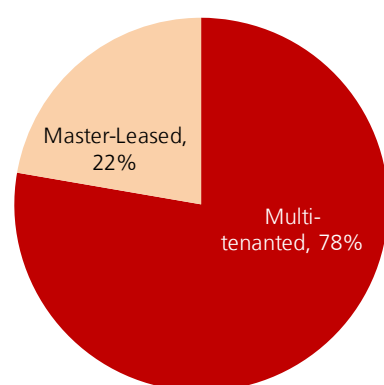
Source: CRCT, DBS Bank

Valuation by multi-tenant/master leased (30 June 2015)



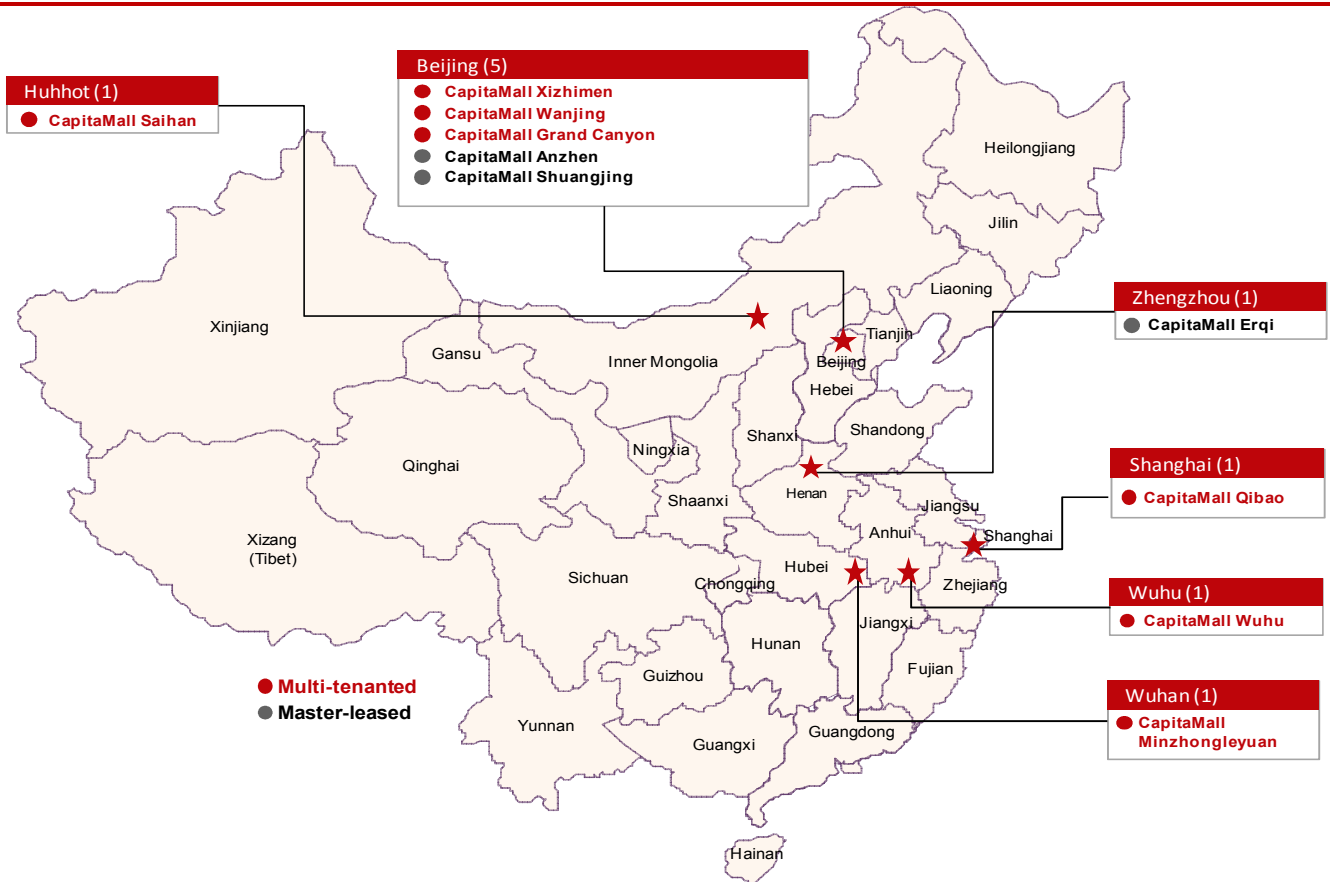
Source: CRCT, DBS Bank

9M15 NPI by multi-tenanted/master leased



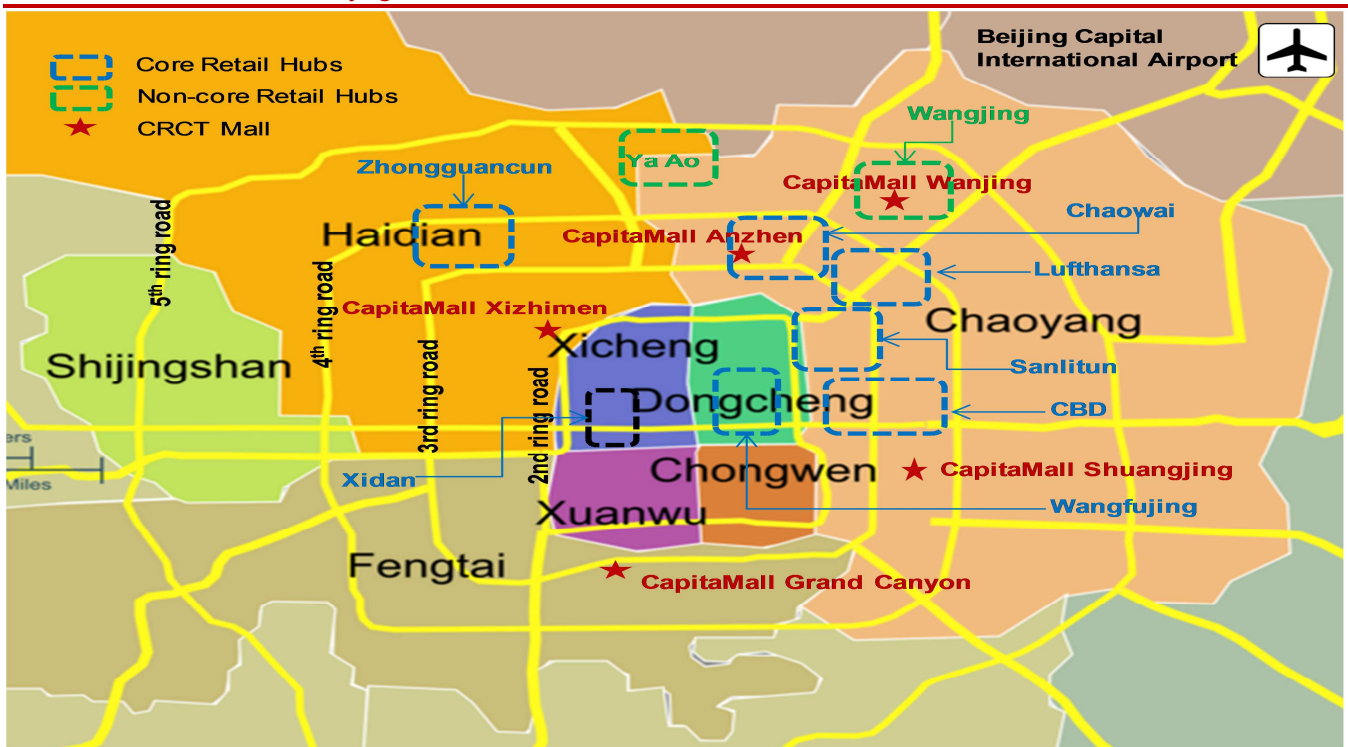
Source: CRCT, DBS Bank

Location of CRCT's malls in China



Source: CRCT, DBS Bank

Location of CRCT's malls in Beijing



* Not to scale and approximate locations
Source: CRCT, DBS Bank

Majority of new mall supply in Beijing are outside the core retail regions

Project (EN)	Project (CN)	Opening date	Retail GFA (sq m)	Location	Retail type	Comments
Jinbao Place II	金宝汇二期	1Q15	12,000	Wangfujing	Shopping Mall	n/a
FUNMIX	Funmix 半岛广场	2Q15	130,000	Others-Fangshan	Shopping Mall	n/a
Carrefour Siyuan Shopping Mall	家乐福四元广场购物中心	3Q15	70,000	Wangjing	Shopping Mall	In CapitaMall Wanjing's district but we understand the mall has a lower market positioning
Xanadu Plaza	禧瑞汇	3Q15	38,000	CBD	Shopping Mall	n/a
Topwin Centre	通盈商业中心	4Q15	45,000	Sanlitun	Shopping Mall	n/a
Hualian Shopping Centre (Pinggu)	北京华联平谷购物中心	4Q15	59,000	Others-Pinggu	Shopping Mall	n/a
Zhuzong Vanke Plaza	住总万科广场	4Q15	61,000	Others-Daxing	Shopping Mall	n/a
Hualian Shopping Centre (Datun)	北京华联大屯购物中心	4Q15	79,000	Others-Datun	Shopping Mall	n/a
BaoYuan International Shopping Centre	宝苑国际购物中心	4Q15	160,000	Others-Fengtai	Shopping Mall	30 minutes drive from CapitaMall Grand Canyon so not in direct competition
Longfor Time Walk	龙湖时代天街	4Q15	300,000	Others-Daxing	Shopping Mall	n/a

Source: Savills, DBS Bank

Income Statement (\$S m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Gross revenue	160	203	215	227	235
Property expenses	(57)	(71)	(77)	(79)	(80)
Net Property Income	103	132	138	148	155
Other Operating expenses	(10)	(14)	(15)	(16)	(16)
Other Non Opg (Exp)/Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(10)	(21)	(20)	(22)	(24)
Exceptional Gain/(Loss)	2	1	0	0	0
Net Income	85	99	103	110	115
Tax	(49)	(57)	(21)	(22)	(23)
Minority Interest	(3)	(2)	(2)	(2)	(2)
Preference Dividend	0	0	0	0	0
Net Income After Tax	34	40	81	86	90
Total Return	133	145	81	86	90
Non-tax deductible Items	36	41	9	9	9
Net Inc available for Dist.	70	81	90	95	99
Growth & Ratio					
Revenue Gth (%)	4.9	27.0	5.7	5.4	3.8
N Property Inc Gth (%)	3.4	28.5	4.4	6.9	4.9
Net Inc Gth (%)	4.6	17.8	103.8	6.5	4.0
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	100.0
Net Prop Inc Margins (%)	64.4	65.1	64.3	65.2	65.9
Net Income Margins (%)	21.1	19.6	37.7	38.1	38.2
Dist to revenue (%)	43.8	39.8	41.7	42.0	42.1
Managers & Trustee's fees to sales %)	6.1	6.9	7.1	6.9	6.8
ROAE (%)	3.1	3.1	5.8	6.0	6.3
ROA (%)	1.8	1.8	3.4	3.5	3.6
ROCE (%)	2.6	2.6	4.9	5.1	5.4
Int. Cover (x)	9.1	5.6	6.3	6.0	5.7

Improvement in earnings on the back of positive rental reversion and ramp-up of Grand Canyon Mall

Source: Company, DBS Bank

Quarterly / Interim Income Statement (\$\$ m)

FY Dec	3Q2014	4Q2014	1Q2015	2Q2015	3Q2015
Gross revenue	51	53	55	54	55
Property expenses	(19)	(19)	(20)	(18)	(20)
Net Property Income	32	34	35	36	35
Other Operating expenses	(4)	(4)	(4)	(4)	(4)
Other Non Opg (Exp)/Inc	0	0	1	0	0
Net Interest (Exp)/Inc	(5)	(5)	(5)	(5)	(5)
Exceptional Gain/(Loss)	0	1	0	0	0
Net Income	24	26	26	28	27
Tax	(7)	(19)	(8)	(16)	(8)
Minority Interest	0	0	1	1	0
Net Income after Tax	16	7	19	13	19
Total Return	16	44	19	43	19
Non-tax deductible Items	3	(24)	3	(20)	3
Net Inc available for Dist.	19	21	22	23	22
Growth & Ratio					
Revenue Gth (%)	1	2	4	(1)	2
N Property Inc Gth (%)	(6)	4	3	4	(2)
Net Inc Gth (%)	nm	(55)	155	(30)	42
Net Prop Inc Margin (%)	62.8	63.7	63.3	66.4	63.7
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	100.0

Improvement in earnings due to strengthening of CNY versus SGD and improvement in CRCT's core multi-tenanted properties.

Balance Sheet (\$\$ m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Investment Properties	2,058	2,251	2,347	2,363	2,370
Other LT Assets	7	8	8	8	8
Cash & ST Invt	105	87	101	115	128
Inventory	0	0	0	0	0
Debtors	11	11	12	13	13
Other Current Assets	2	2	2	2	2
Total Assets	2,184	2,358	2,469	2,500	2,521
ST Debt	0	0	0	0	0
Creditor	58	51	54	57	59
Other Current Liab	165	216	216	216	216
LT Debt	712	672	698	724	741
Other LT Liabilities	35	41	41	41	41
Unit holders' funds	1,187	1,350	1,430	1,430	1,430
Minority Interests	27	28	30	31	33
Total Funds & Liabilities	2,184	2,358	2,469	2,500	2,521
Non-Cash Wkg. Capital	(210)	(254)	(257)	(259)	(261)
Net Cash/(Debt)	(607)	(585)	(597)	(610)	(613)
Ratio					
Current Ratio (x)	0.5	0.4	0.4	0.5	0.5
Quick Ratio (x)	0.5	0.4	0.4	0.5	0.5
Aggregate Leverage (%)	32.6	28.5	28.3	29.0	29.4
Z-Score (X)	1.2	1.2	1.2	1.2	1.2

Low gearing provides debt headroom for acquisitions

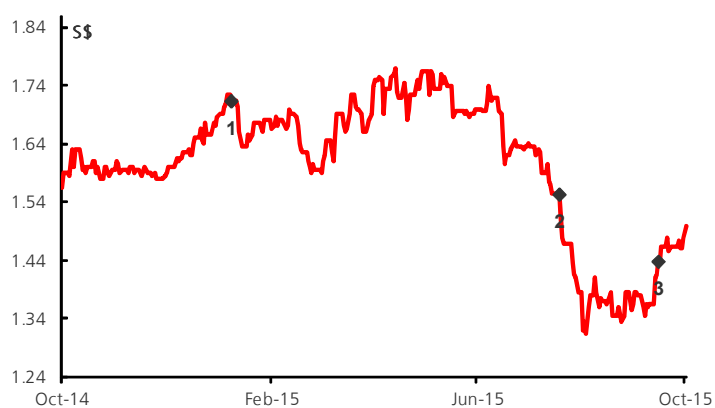
Source: Company, DBS Bank

Cash Flow Statement (\$\$ m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Pre-Tax Income	85	99	103	110	115
Dep. & Amort.	2	3	2	2	2
Tax Paid	(20)	(18)	(21)	(22)	(23)
Associates & JV Inc/(Loss)	0	0	0	0	0
Chg in Wkg.Cap.	(11)	2	2	2	2
Other Operating CF	13	26	6	7	7
Net Operating CF	69	111	94	99	103
Net Invnt in Properties	(143)	(15)	(16)	(16)	(7)
Other Invnts (net)	0	0	0	0	0
Invnts in Assoc. & JV	0	0	0	0	0
Div from Assoc. & JVs	0	0	0	0	0
Other Investing CF	(1)	(2)	0	0	0
Net Investing CF	(143)	(17)	(16)	(16)	(7)
Distribution Paid	(38)	(49)	(90)	(95)	(99)
Chg in Gross Debt	29	(44)	26	26	17
New units issued	58	0	0	0	0
Other Financing CF	(5)	(17)	0	0	0
Net Financing CF	45	(110)	(63)	(69)	(82)
Currency Adjustments	(5)	(4)	0	0	0
Chg in Cash	(35)	(19)	14	14	14
Operating CFPS (\$ cts)	10.3	13.4	10.9	11.3	11.5
Free CFPS (\$ cts)	(9.5)	11.9	9.2	9.7	10.9

Source: Company, DBS Bank

Target Price & Ratings History



S.No.	Date	Closing Price	Target Price	Rating
1	30 Jan 15	1.72	1.64	HOLD
2	10 Aug 15	1.56	1.80	BUY
3	07 Oct 15	1.44	1.69	BUY

Note: Share price and Target price are adjusted for corporate actions.

Source: DBS Bank

DBS Bank recommendations are based on 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 catalysts within this time frame)

Share price appreciation + dividends

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