Singapore Company Guide

CapitaLand Commercial Trust

Edition 1 Version 1 | Bloomberg: CCT SP | Reuters: CACT.SI **Refer to important disclosures at the end of this report**

DBS Group Research . Equity 28 Oct 2015

BUY

Last Traded Price: S$1.435 **(STI** : 3,052.53)
Price Target : 12-Month S$ 1.48 (3% upside)

Potential Catalyst: Acquisition of the remaining 60% stake in CapitaGreen
Where we differ: We are in line with peers

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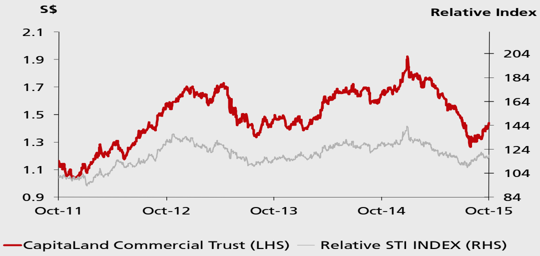
Price Relative



Forecasts and Valuation

FY Dec (S$ m)	2014A	2015F	2016F	2017F
Gross Revenue	263	270	269	272
Net Property Inc	205	213	211	214
Total Return	449	238	246	259
Distribution Inc	249	254	262	275
EPU (S cts)	12.6	8.1	8.3	8.7
EPU Gth (%)	38	(36)	3	5
DPU (S cts)	8.5	8.6	8.9	9.3
DPU Gth (%)	3	2	3	5
NAV per shr (S cts)	174.8	174.3	173.6	173.0
PE (X)	11.4	17.8	17.2	16.4
Distribution Yield (%)	5.9	6.0	6.2	6.5
P/NAV (x)	0.8	0.8	0.8	0.8
Aggregate Leverage (%)	30.4	30.0	30.0	30.0
ROAE (%)	7.3	4.6	4.8	5.0
Distn. Inc Chng (%):		-	(4)	(4)
Consensus DPU (S cts):		8.7	9.0	9.1
Other Broker Recs:		B: 14	S: 4	H: 7

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

SHOOTS OF GROWTH AT CAPITAGREEN

CapitaGreen boosts earnings visibility amid uncertain market. Despite an uncertain office market outlook in 2016, CCT offers investors earnings certainty in the form of additional contribution from CapitaGreen. This should more than offset the risk of negative rental reversions and lower occupancies for the rest of the portfolio in the next few years. Upside will come from acquisitions given its low gearing of 30%.

Defensive portfolio with >70% of leases expiring in FY18 and beyond. CCT has maintained a defensive leasing posture amid stiff competition for larger tenants by locking in longer term leases for most of its top 10 tenants.With >70% of office leases expiring in FY18 and beyond, the Trust offers investors a measure of earnings stability and certainty amid record office completions over the next two years.

3.7% DPU CAGR for FY15-17. Looking ahead, we expect CCT to deliver 2-year DPU CAGR of 3.7%, driven by new contribution from CapitaGreen, which was opened in Dec-2014, and has a committed occupancy rate of 87.7% as of 3Q15. In addition, the REIT has a call option to acquire the remaining 60% of the asset in FY15-17 at the higher of valuation or development cost compounded at 6.3% p.a.

Valuation:

We have a DCF-backed TP of S$1.48. We believe that dividend yield of 6.2-6.5% is attractive given its large market cap and trading liquidity. We have a BUY call premised on cheap valuations (stock is trading at 0.8x P/Bk) and total return of >10% However, we note that in the near term, share price could be more newsflow driven.

Key Risks to Our View:

Risk of higher vacancies and negative rental reversions for FY16. In FY16-17, close to 30% of CCT's office leases will be due for expiry, the majority of which stems from One George Street (7%) and Six Battery Road (10%), where expiring rents are close to or slightly higher than market rents. As the Manager has prioritized tenant retention, there is a possibility of negative rental reversions, which would impede earnings growth.

At A Glance

Issued Capital (m shrs)	2,951
Mkt. Cap (Sm/USm)	4,234 / 3,031
Major Shareholders	
Capitaland Ltd (%)	31.5
Blackrock (%)	6.5
CBRE Clarion (%)	5.0
Free Float (%)	57.0
3m Avg. Daily Val (US$m)	10.2

ICB Industry : Real Estate / Real Estate Investment Trust

CRITICAL DATA POINTS TO WATCH

Earnings Drivers:

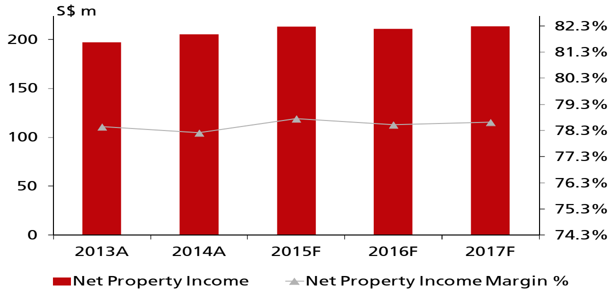
Renewal of GIC lease to drive earnings growth for FY15. GIC, which occupies c.40% of NLA at Capital Tower, recently renewed its lease at what we understand to be a 25% uplift in rents. We estimate this lease renewal to contribute to c.3% growth in CCT's topline, and will be the significant driver of income and DPU growth in FY15. However, this will be partially mitigated by the vacation of Mizuho, which occupies c8% of NLA.

Moderate 3% uplift in FY16 DPU from CapitaGreen, FY17 to see full impact. CCT's FY16 earnings will be driven by fresh contribution from CapitaGreen, which has achieved commitments for 87.7% of NLA as of 3Q15. Majority of leases secured at the asset expires beyond 2018, thereby protecting the asset from the anticipated spike in office supply from 2016-2018. While leases signed in 2014 have begun operations, we note that most tenants who signed their leases in 2015 will likely begin to contribute gradually from 1Q16 onwards. Full year contribution from FY17 will add another visible boost to DPU in the medium term.

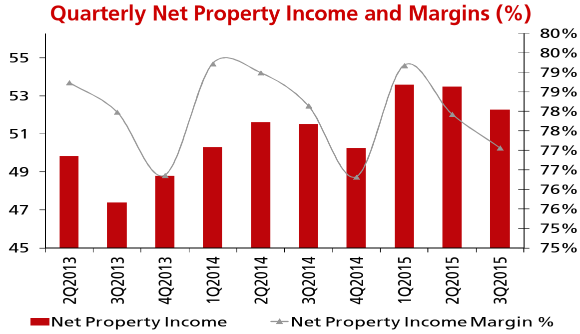
Staggered weighted lease expiry profile will mitigate negative rental reversions. We have factored in lower occupancies and negative reversions at Capital Tower, Six Battery Road, and One George Street for FY16 and FY17. CCT's defensive WALE of 7.7 years (by NLA) should ensure that the negative impact from an anticipated decline in rents over the next two years will be gradual rather than immediate.

3Q15 DPU of 2.14Scts (+2.4% y-o-y) was in line with our estimates. Earnings were driven by higher rental income from Capital Tower (post renewal of GIC lease), Six Battery Road, and Raffles City, mitigated by slight losses at Capitagreen, where most tenants are still in the process of fitting out. Portfolio occupancy fell to 96.4%, largely due to low occupancies at Capital Tower (92.2%), where the Manager has yet to backfill space vacated by Mizuho, which previously occupied 9.5% of NLA.

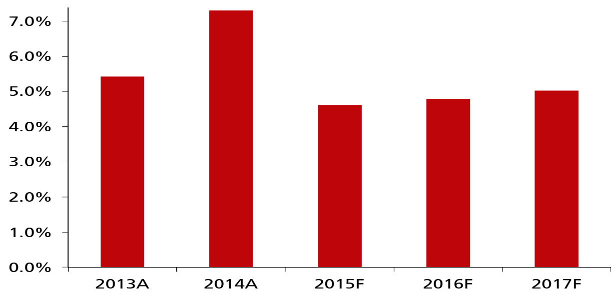
Net Property Income and Margins (%)



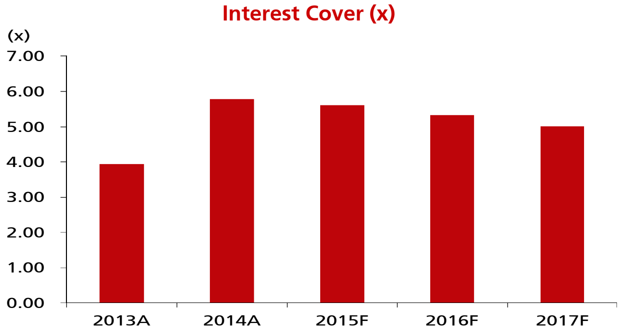
Quarterly Net Property Income and Margins (%)



ROE (%)



Interest Cover (x)



Source: Company, DBS Bank

Balance Sheet:

Low gearing of 29.5% allows for opportunistic acquisitions. CCT has a healthy aggregate gearing ratio of 30%, which gives it ample headroom to make opportunistic acquisitions. 83% of borrowings are fixed at an average cost of 2.4%, which provides a measure of protection against near term fluctuations in interest rate.

Share Price Drivers:

Obvious acquisition pipeline CCT has a call option to acquire the remaining 60% interest in CapitaGreen within 3 years after completion (from 2015-2017), at market value or development cost compounded at 6.3% p.a. Based on Jun-15 valuation of S$1.57bn, we estimate acquisition price to be in the range of c.S$950m-S$1bn, which would bring gearing to c.37%. Given historical gearing levels of 30-35% however, any acquisition could be accompanied by an equity fund raising exercise.

Key Risks:

Risk of higher vacancies and negative rental reversions for FY16. In FY16-17, close to 30% of CCT's office leases will be due for expiry, the majority of which stems from One George Street (7%) and Six Battery Road (10%), where expiring rents are close to or slightly higher than market rents. As the Manager has prioritized tenant retention, there is a possibility of negative rental reversions, which would impede earnings growth.

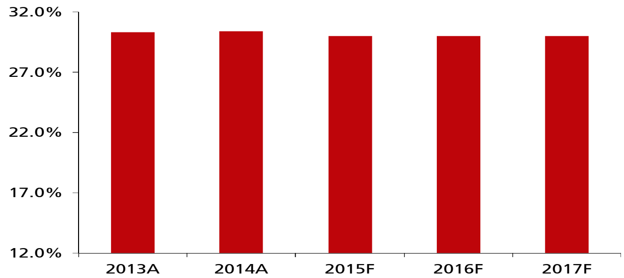
Competition from other landlords. Between 2016 and 2018, c.5.3m sqft of office net lettable area (NLA) will be completed within the downtown core, translating to a 15% increase in existing stock, or 3-year CAGR of 4.6%. Due to weaker net absorption rates of <1m sqft in recent years, CCT could face higher competition for large tenants from landlords of newer buildings, which have large floor plates of 30-40k sqft.

Pressure on rents from shadow space. We see some downsizing activity from banks and financial institutions, and these shadow space particularly in the Marina Bay area could put some pressure on rents for CCT's portfolio, which is located primarily in the Raffles Place/Tanjong Pagar area.

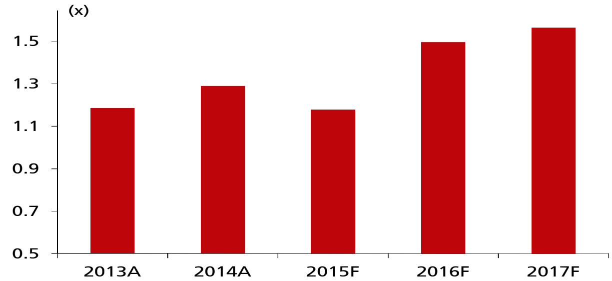
COMPANY BACKGROUND

CapitaCommercial Trust (CCT) is a real investment trust investing exclusively in commercial properties in Singapore.

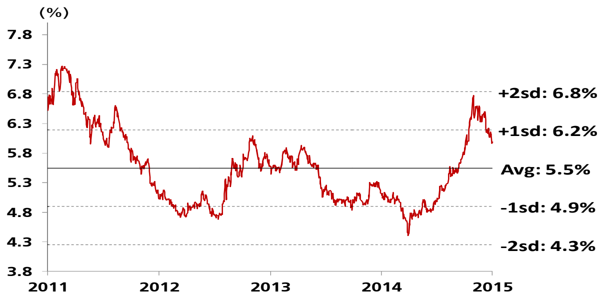
Aggregate Leverage (%)



Distribution Paid / Net Operating CF



Distribution Yield (%)



P/Bk NAV (x)

Source: Company, DBS Bank

Income Statement (S$ m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Gross revenue	251	263	270	269	272
Property expenses	(54)	(57)	(58)	(58)	(58)
Net Property Income	**197**	**205**	**213**	**211**	**214**
Other Operating expenses	(15)	(16)	(19)	(19)	(19)
Other Non Opg (Exp)/Inc	(5)	(4)	0	0	0
Net Interest (Exp)/Inc	(46)	(33)	(35)	(36)	(39)
Exceptional Gain/(Loss)	3	(2)	0	0	0
Net Income	**261**	**368**	**238**	**246**	**259**
Tax	0	0	0	0	0
Minority Interest	0	0	0	0	0
Preference Dividend	0	0	0	0	0
Net Income After Tax	**261**	**368**	**238**	**246**	**259**
Total Return	367	449	238	246	259
Non-tax deductible Items	(139)	(200)	16	16	16
Net Inc available for Dist.	234	249	254	262	275
Growth & Ratio					
Revenue Gth (%)	(33.1)	4.4	2.9	(0.5)	1.1
N Property Inc Gth (%)	(33.3)	4.1	3.7	(0.8)	1.3
Net Inc Gth (%)	26.9	40.9	(35.2)	3.5	5.2
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	100.0
Net Prop Inc Margins (%)	78.4	78.2	78.7	78.5	78.6
Net Income Margins (%)	103.8	140.0	88.1	91.6	95.3
Dist to revenue (%)	93.1	94.9	94.0	97.6	101.2
Operating expenses (%)	6.0	6.2	7.0	7.0	7.0
ROAE (%)	5.4	7.3	4.6	4.8	5.0
ROA (%)	3.9	5.8	3.6	3.8	4.0
ROCE (%)	2.8	3.0	3.0	3.0	3.0
Int. Cover (x)	3.9	5.8	5.6	5.3	5.0

Earnings growth will be driven by contribution from CapitaGreen, which should offset income loss from lower occupancies and negative rental reversions at existing office assets such as Capital Tower, 6 Battery Road and One George Street

Source: Company, DBS Bank

Quarterly / Interim Income Statement (S$ m)

FY Dec	3Q2014	4Q2014	1Q2015	2Q2015	3Q2015
Gross revenue	66	66	68	69	68
Property expenses	(15)	(16)	(14)	(15)	(16)
Net Property Income	52	51	54	54	53
Other Operating expenses	(5)	(4)	(5)	(4)	(4)
Other Non Opg (Exp)/Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(8)	(8)	(8)	(8)	(8)
Exceptional Gain/(Loss)	(1)	0	(19)	0	0
Net Income	**58**	**157**	**39**	**77**	**57**
Tax	0	0	0	0	0
Minority Interest	0	0	0	0	0
Net Income after Tax	**58**	**157**	**39**	**77**	**57**
Total Return	0	0	0	0	0
Non-tax deductible Items	0	0	0	0	0
Net Inc available for Dist.	62	64	63	64	63
Growth & Ratio					
Revenue Gth (%)	1	0	3	1	(1)
N Property Inc Gth (%)	0	(2)	7	0	(2)
Net Inc Gth (%)	(40)	172	(75)	96	(26)
Net Prop Inc Margin (%)	78.1	76.3	79.2	77.9	77.1
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	100.0

Balance Sheet (S$ m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Investment Properties	4,769	4,882	4,890	4,894	4,899
Other LT Assets	1,359	1,499	1,499	1,499	1,499
Cash & ST Invts	84	101	142	145	149
Inventory	0	0	0	0	0
Debtors	34	38	17	17	17
Other Current Assets	0	0	0	0	0
Total Assets	**6,245**	**6,521**	**6,547**	**6,555**	**6,564**
ST Debt	0	270	270	270	270
Creditor	51	47	63	62	63
Other Current Liab	12	11	11	11	11
LT Debt	1,218	970	981	989	997
Other LT Liabilities	52	69	69	69	69
Unit holders' funds	4,913	5,153	5,153	5,153	5,153
Minority Interests	0	0	0	0	0
Total Funds & Liabilities	**6,245**	**6,521**	**6,547**	**6,555**	**6,564**
Non-Cash Wkg. Capital	(29)	(20)	(57)	(57)	(58)
Net Cash/(Debt)	(1,134)	(1,139)	(1,110)	(1,114)	(1,118)
Ratio					
Current Ratio (x)	1.9	0.4	0.5	0.5	0.5
Quick Ratio (x)	1.9	0.4	0.5	0.5	0.5
Aggregate Leverage (%)	30.3	30.4	30.0	30.0	30.0
Z-Score (X)	2.1	2.1	2.0	2.0	2.0

Assuming acquisition of the remaining 60% of CapitaGreen, gearing would rise to slightly less than 40%.

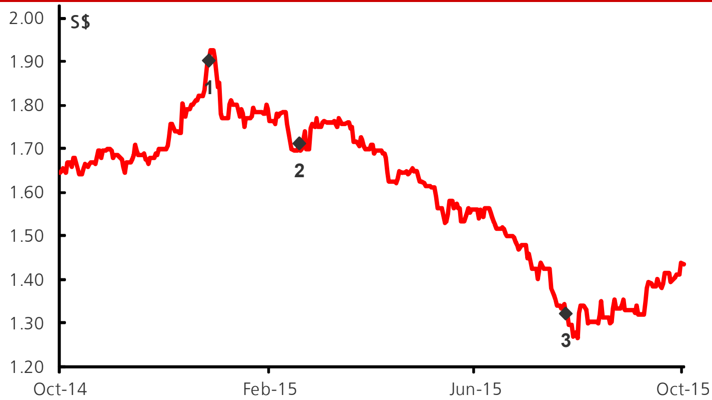
Source: Company, DBS Bank

Cash Flow Statement (S$ m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Pre-Tax Income	261	368	238	246	259
Dep. & Amort.	1	4	4	4	4
Tax Paid	0	0	0	0	0
Associates &JV Inc/(Loss)	(127)	(217)	(79)	(90)	(103)
Chg in Wkg.Cap.	8	(5)	37	0	1
Other Operating CF	53	39	16	16	16
Net Operating CF	**195**	**189**	**216**	**175**	**176**
Net Invt in Properties	(21)	(30)	(11)	(8)	(8)
Other Invts (net)	(1)	0	0	0	0
Invts in Assoc. & JV	(526)	(397)	0	0	0
Div from Assoc. & JVs	83	86	79	90	103
Other Investing CF	526	392	0	0	0
Net Investing CF	**61**	**52**	**68**	**82**	**95**
Distribution Paid	(231)	(243)	(254)	(262)	(275)
Chg in Gross Debt	40	50	11	8	8
New units issued	0	0	0	0	0
Other Financing CF	(99)	(31)	0	0	0
Net Financing CF	**(290)**	**(223)**	**(243)**	**(254)**	**(267)**
Currency Adjustments	0	0	0	0	0
Chg in Cash	(34)	17	40	3	4
Operating CFPS (S cts)	6.6	6.6	6.1	5.9	5.9
Free CFPS (S cts)	6.1	5.5	6.9	5.7	5.7

Source: Company, DBS Bank

Target Price & Ratings History



S.No.	Date	Closing Price	Target Price	Rating
1	22 Jan 15	1.91	1.81	HOLD
2	16 Mar 15	1.72	1.81	HOLD
3	19 Aug 15	1.33	1.48	BUY

Source: DBS Bank

DBS Bank recommendations are based 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 catalysts within this time frame)

Share price appreciation + dividends

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