

COMPANY UPDATE

Lendlease Global Commercial REIT (LREIT SP)

Deleveraging With Acceptable Trade-offs

Buoyant tenant sales and a limited new supply of retail space are supportive of continued positive rental reversions at 313@Somerset and Jem. LREIT has the option of divesting the office block at Jem combined with a private placement to redeem perpetual securities of S\$400m and deleverage. We estimate the negative impact to be manageable at 3.8% for DPU and 2.3% for NAV per unit. LREIT provides an attractive FY24 distribution yield of 8.0%. Maintain BUY. Target price: S\$0.83.

WHAT'S NEW

- **Higher occupancies reflect improving confidence for retailers.** Lendlease Global Commercial REIT's (LREIT) retail properties, which accounted for 75% of its portfolio valuation (Orchard Road: 28%, suburban: 47%) as of Jun 23, are resilient and benefitting from the buoyant retail scene in Singapore. 313@Somerset and Jem had maintained high committed occupancies of 99% and 100% respectively as of Jun 23. LREIT achieved positive rental reversion of 4.8% for retail properties in FY23 (1HFY23: 2.0%, 2HFY23: 6.1%). Tenant retention is high at 82.4% in FY23. Essential services accounted for approximately 58% of gross rental income. Management expects the positive momentum for rental reversion from its retail properties to be maintained in FY24.
- **Buoyant tenant sales support positive rental reversion.** Retail sales and retailers' confidence have recovered since Singapore reopened its economy in Apr 22. Tenant sales were 15-20% above pre-pandemic levels during 4QFY23. 313@Somerset benefits from employees returning to their offices within the CBD and tourists returning to shop at Orchard Road.
- **High cost of perpetual securities.** LREIT has issued two perpetual securities: a) S\$200m 4.2% Perp 1 with reset date on 4 Jun 26, and b) S\$200m 5.25% Perp 2 with reset date on 11 Apr 25. Interest rates for the two perpetual securities are expected to hit 6% after the reset. If interest rates remain higher for longer, LREIT would have to redeem as the cost of debt for the perpetual securities would be prohibitive.
- **Alternative avenues to deleverage.** LREIT can consider two options to raise funds to redeem the two tranches of perpetual securities:
 - Office block at Jem.** LREIT could consider divesting the office block at Jem, which is fully leased to the Ministry of National Development (MND) under a 30-year lease with a rent review every five years. It has a long WALE of 21 years with lease expiry in Dec 44. The 12 levels of office space have NLA of 311,000sf (35% of Jem's total NLA). The government through MND accounted for 11.1% of LREIT's gross rental income as of Jun 23. We estimated that the office block at Jem provides NPI yield of 3.5% and is valued at S\$480m.

KEY FINANCIALS

Year to 30 Jun (S\$m)	2022	2023	2024F	2025F	2026F
Net turnover	102	205	213	219	224
EBITDA	60	131	136	140	144
Operating profit	60	131	136	140	144
Net profit (rep./act.)	140	100	53	51	54
Net profit (adj.)	36	63	53	51	54
EPU (S\$ cent)	2.1	2.7	2.3	2.2	2.3
DPU (S\$ cent)	4.9	4.7	4.4	4.3	4.4
PE (x)	25.8	19.8	23.7	24.7	23.6
P/B (x)	0.7	0.7	0.7	0.7	0.8
DPU Yld (%)	8.9	8.6	8.0	7.9	8.0
Net margin (%)	138.1	48.8	24.8	23.5	24.1
Net debt/(cash) to equity (%)	64.4	65.4	69.2	73.0	77.1
Interest cover (x)	3.8	2.6	2.1	2.0	2.0
ROE (%)	8.4	4.5	2.4	2.4	2.6
Consensus DPU (S\$ cent)	n.a.	n.a.	4.4	4.5	4.6
UOBKH/Consensus (x)	-	-	1.00	0.95	0.95

Source: Lendlease Global Commercial REIT, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	S\$0.545
Target Price	S\$0.83
Upside	+52.3%
(Previous TP)	S\$0.890

COMPANY DESCRIPTION

LREIT invests in stabilised income-producing properties located globally, which are used for retail and/or office purposes. Its portfolio comprises two retail malls, 313@Somerset at Orchard Road and Jem at Jurong East, in Singapore and Sky Complex with three grade A office buildings in Milan, Italy.

STOCK DATA

GICS sector	Real Estate
Bloomberg ticker:	LREIT SP
Shares issued (m):	2,323.7
Market cap (S\$m):	1,266.4
Market cap (US\$m):	924.3
3-mth avg daily t'over (US\$m):	3.0

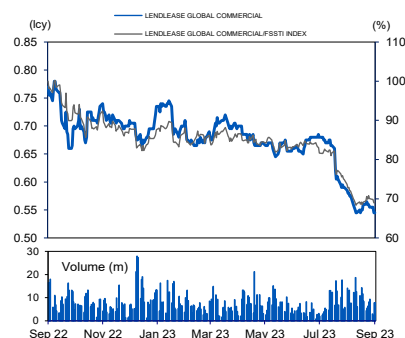
Price Performance (%)

52-week high/low	S\$0.78/S\$0.545			
1mth	3mth	6mth	1yr	YTD
(7.6)	(16.8)	(21.0)	(30.1)	(22.7)

Major Shareholders

	%
Lendlease Corp Ltd	26.3
FY24 NAV/Share (S\$)	0.77
FY24 Net Debt/Share (S\$)	0.65

PRICE CHART



Source: Bloomberg

ANALYST(S)

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b) Sky Complex. LREIT could consider divesting Sky Complex located at Milano Santa Giulia, a vibrant office area that is 20 minutes' drive from Milan CBD and 10 minutes' drive from Linate Airport. It is 150m from the Rogoredo high-speed railway and metro station. Sky Complex is fully leased to Sky Italia on a triple net basis till 15 May 32 (WALE: 8.9 years). Sky Complex was valued at €290.5m, or S\$428.8m, as of Jun 23.

- **Completed refinancing for euro loan.** LREIT has obtained a €300m unsecured five-year sustainability-linked loan (drawdown in Oct 23) to refinance its euro loan due in FY24. It has already met the target set for its sustainability-linked euro loan. The all-in interest rate for the new sustainability-linked euro loan is expected to be mid-3%. We estimate that LREIT's all-in cost of debt will increase by 0.8ppt yoy to 4.6% yoy in 2HFY24. LREIT does not have any loans due for refinancing until FY25.

STOCK IMPACT

- **Retail in recovery mode.** Leasing activities were boosted by new mall openings, such as Woodleigh Mall and Komo Shoppes. Demand was driven by F&B (especially cafes), fashion and beauty & health. Retailers have gained confidence due to a tourism recovery and the return of office crowds. Rents at Orchard Road and suburban malls increased 2.9% and 3.1% yoy respectively in 2Q23. CBRE expects a recovery of retail rents in 2023 due to the tourism recovery and below-average new retail supply. Retailers are paying higher rents to secure prime retail spaces.
- **Divestment of Jem's office block is the preferred option.** We expect the potential sale of the office block at Jem to attract interest from investors as Singapore is a safe haven with a resilient office market. Conversely, a divestment of Sky Complex is more problematic as the transaction volume for office properties in Europe is fairly thin.
- **Manageable negative impact from deleveraging.** We expect LREIT to divest the office block at Jem and utilise the proceeds to redeem Perp 1 and Perp 2 (S\$400m) and repay borrowings (S\$80m). The office block provides NPI yield of 3.5%, which is lower than the cost of Perp 1 and Perp 2 at 4.2% and 5.25% respectively. The divestment will increase aggregate leverage by 4ppt. We have assumed a private placement of 258m new units at S\$0.52 each (5% discount to closing price) to restore aggregate leverage to the original level. On a combined basis, the divestment and equity fund raising will reduce DPU by 3.8% and NAV per unit by 2.3%.

EARNINGS REVISION/RISK

- We reduce our existing DPU forecasts by 4% for FY24 and 7% for FY25 after factoring in the new sustainability-linked euro loan.

VALUATION/RECOMMENDATION

- **Maintain BUY.** Our target price of S\$0.83 is based on DDM (cost of equity: 7.25%, terminal growth: 2.2%).

SHARE PRICE CATALYST

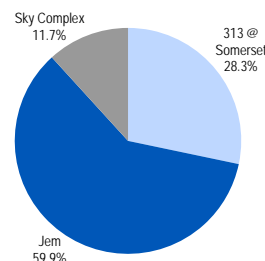
- 313@Somerset benefits from employees returning to their offices in the CBD and tourists flocking back to shop at Orchard Road. The new multi-functional event space at Grange Road Car Park will increase shopper traffic to 313@Somerset.
- Jem benefits from the development of Jurong Gateway as Singapore's second CBD.

KEY OPERATING METRICS - LREIT

	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	yoy % Chg	qoq % Chg*
DPU (S cents)	2.45	n.a.	2.45	n.a.	2.25	-8.2%	-8.2%
Occupancy	99.8%	99.7%	99.8%	99.8%	99.9%	0.1ppt	0.1ppt
Aggregate Leverage	40.0%	39.4%	39.2%	39.3%	40.6%	0.6ppt	1.3ppt
Average Cost of Debt	1.69%	2.24%	2.35%	2.51%	2.69%	1ppt	0.2ppt
% Borrowings on Fixed Rate	59%	61%	61%	61%	61%	2ppt	0ppt
Weighted Debt Maturity (years)	2.8	2.8	2.6	2.3	2.1	-0.7yrs	-0.2yrs
WALE by NLA (years)	8.7	8.5	8.3	8.3	8.2	-0.5yrs	-0.1yrs

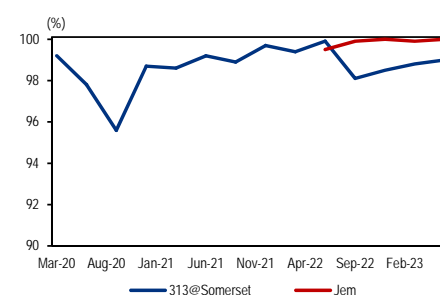
Source: LREIT, UOB Kay Hian * hoh % chg for DPU

PORTFOLIO VALUATION BY PROPERTY (JUN 23)



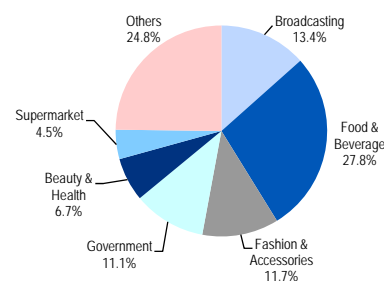
Source: LREIT

OCCUPANCY FOR JEM AND 313@SOMERSET



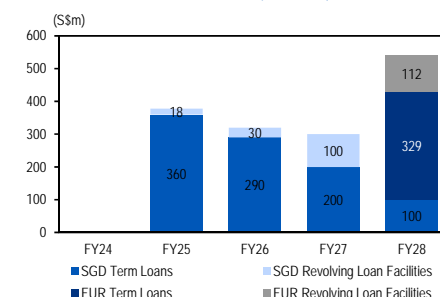
Source: LREIT

GROSS RENTAL INCOME BY TRADE SECTOR (JUN 23)



Source: LREIT

DEBT MATURITY PROFILE (JUN 23)



Source: LREIT

PROFIT & LOSS

Year to 30 Jun (\$m)	2023	2024F	2025F	2026F
Net turnover	204.9	213.3	218.8	224.2
EBITDA	130.9	135.9	139.8	143.6
Deprec. & amort.	0.0	0.0	0.0	0.0
EBIT	130.9	135.9	139.8	143.6
Associate contributions	1.1	0.0	0.0	0.0
Net interest income/(expense)	(50.7)	(66.3)	(71.7)	(72.8)
Pre-tax profit	118.5	69.6	68.1	70.8
Tax	0.0	0.0	0.0	0.0
Minorities	0.4	0.0	0.0	0.0
Preferred dividends	(18.9)	(16.8)	(16.8)	(16.8)
Net profit	99.9	52.8	51.3	54.0
Net profit (adj.)	62.6	52.8	51.3	54.0

BALANCE SHEET

Year to 30 Jun (\$m)	2023	2024F	2025F	2026F
Fixed assets	3,650.0	3,652.0	3,654.0	3,656.0
Other LT assets	111.2	111.2	111.2	111.2
Cash/ST investment	54.2	55.1	56.2	57.0
Other current assets	10.9	12.9	13.0	13.2
Total assets	3,826.4	3,831.2	3,834.4	3,837.3
ST debt	433.6	433.6	433.6	433.6
Other current liabilities	58.7	60.2	61.8	63.3
LT debt	1,078.6	1,130.0	1,180.0	1,230.0
Other LT liabilities	24.7	24.7	24.7	24.7
Shareholders' equity	2,228.8	2,180.7	2,132.3	2,083.8
Minority interest	2.0	2.0	2.0	2.0
Total liabilities & equity	3,826.4	3,831.2	3,834.4	3,837.3

CASH FLOW

Year to 30 Jun (\$m)	2023	2024F	2025F	2026F
Operating	174.0	137.5	143.2	147.0
Pre-tax profit	99.9	52.8	51.3	54.0
Working capital changes	16.0	(0.4)	1.4	1.4
Non-cash items	(3.5)	31.1	31.3	31.5
Other operating cashflows	61.6	54.0	59.1	60.1
Investing	(85.8)	(2.0)	(2.0)	(2.0)
Capex (growth)	(87.9)	0.0	0.0	0.0
Capex (maintenance)	(4.6)	(2.0)	(2.0)	(2.0)
Proceeds from sale of assets	0.0	0.0	0.0	0.0
Others	6.7	0.0	0.0	0.0
Financing	(83.1)	(134.6)	(140.1)	(144.2)
Distribution to unitholders	(67.9)	(100.9)	(99.6)	(102.6)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	66.8	51.4	50.0	50.0
Others/interest paid	(82.0)	(85.1)	(90.5)	(91.6)
Net cash inflow (outflow)	5.2	0.9	1.1	0.8
Beginning cash & cash equivalent	49.2	54.2	55.1	56.2
Changes due to forex impact	(0.2)	0.0	0.0	0.0
Ending cash & cash equivalent	54.2	55.1	56.2	57.0

KEY METRICS

Year to 30 Jun (%)	2023	2024F	2025F	2026F
Profitability				
EBITDA margin	63.9	63.7	63.9	64.1
Pre-tax margin	57.8	32.6	31.1	31.6
Net margin	48.8	24.8	23.5	24.1
ROA	2.7	1.4	1.3	1.4
ROE	4.5	2.4	2.4	2.6
Growth				
Turnover	101.5	4.1	2.6	2.5
EBITDA	119.4	3.8	2.9	2.8
Pre-tax profit	(22.4)	(41.2)	(2.2)	4.0
Net profit	(28.8)	(47.1)	(2.8)	5.3
Net profit (adj.)	72.6	(15.7)	(2.8)	5.3
EPU	30.2	(16.4)	(3.7)	4.3
Leverage				
Debt to total capital	40.4	41.7	43.1	44.4
Debt to equity	67.8	71.7	75.7	79.8
Net debt/(cash) to equity	65.4	69.2	73.0	77.1
Interest cover (x)	2.6	2.1	2.0	2.0

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