Credit Note

Real Estate ▪ Singapore

CapitaLand 1.85% 06/19/20

(CAPL SP/CATL.SI)

Defensive positioning with positive carry

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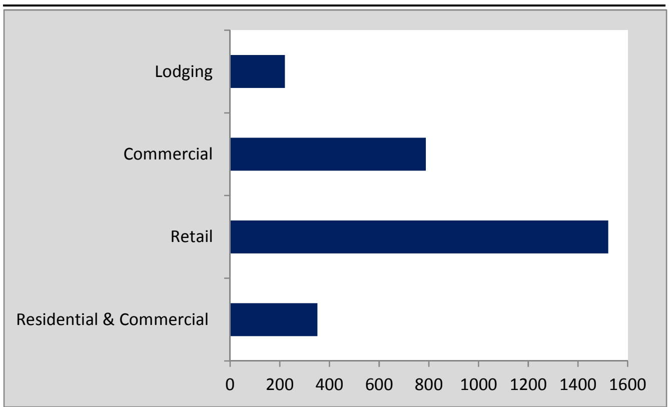
Company Background: CapitaLand is one of Asia's largest real estate companies. Headquartered and listed in Singapore with 40% ownership by Temasek Holdings. The group is an owner and manager of a global portfolio worth over S$92 billion as at 30 September 2018, comprising integrated developments, shopping malls, lodging, offices, homes, real estate investment trusts (REITs) and funds.

Credit Considerations:

3Q18 results declined 17% YoY to SGD 1.26bn due to lower contributions from development projects in Singapore and China. Net profits however, declined by 2.1% YoY to SGD 566.6mn due to higher contributions from rental revenue, which led to stronger gross margins of 46% (3Q17:33%).

Higher contribution from recurring revenues can help the group weather macroeconomic uncertainties. As of 3Q18, revenue from investment properties, increased to 85.5% of the group's total EBIT from 84.7% in 3Q17. YTD, the contribution from investment properties rose to 87.8% of EBIT from 77.4% in 9M17, driven by newly acquired properties, revaluation gains and the consolidation of CapitaLand Mall Trust (CMT, CapitaLand Retail China Trust (CRCT) and RCS Trust (RCST).

Figure 1: Investment Properties Contribute 88% of Total EBIT (SGD mn)

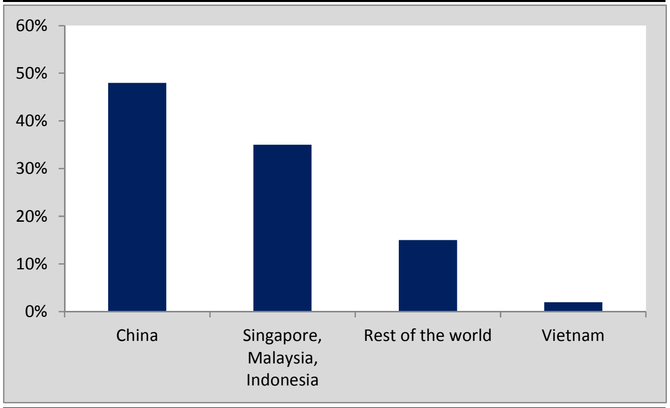


Source: Company Data, KGI Research

Going forward, we expect contributions from rental income to continue increasing as the group strengthens its lodging platforms after the acquisition of 16 freehold multifamily properties for US$835mn in the US in September 2018. Together with a US$26mn investment for a 70% stake in TAUZIA Indonesia, CapitaLand currently manages more than 94,000 lodging units globally, surpassing its 2020 target of 80,000.

Chinese property exposure provides upside potential if trends in office rentals and residential properties persist. While China is the 2nd largest contributor to CapitaLand's revenues and EBIT, 48% of the group's assets under management comes from China. The company continues to expand in China with YTD divestments and investments of S$2bn and S$2.3bn respectively. For FY19, the company is expecting demand of office space to remain strong in light of reducing new supply in Shanghai and Beijing, where 52% of the group's commercial space are located.

Figure 2: 3Q18 Real Estate Assets under Management



Source: Company Data, KGI Research

For residential properties, take-up rates continue to be strong with 96% of the Group's launched units already sold despite property cooling measures implemented by the Chinese government in the 1st and 2nd tier cities.

Credit Recommendations: In line with our defensive portfolio positioning, we recommend an exposure to CAPLSP's 2020 convertible currently trading at 97.46 with a YTW of 3.5% and duration of 1.4.

While net debt/equity rose to 50.5% at 9M18 from 48.6% in FY17, liquidity remains strong with S$5.3bn in cash reserves compared to short-term borrowings of S$3.2bn. Additionally, the group has undrawn facilities of ~S$2.7bn with free cash flows of S$1.1bn.

Given the group's strong balance sheet and stakeholder relationship with Temasek Holdings, we believe the convertible provides good protection for investors looking for safe carry in light of recent market volatility.

Financials

FYE 31 December

INCOME STATEMENT (SGD mn)	2016A	2017A	9M18
Revenue	5,252.3	4,609.8	3,978.0
EBITDA	1,272.5	1,491.4	1,532.0
EBIT	1,203.5	1,415.1	1,478.7
Gross Interest Expense	512.2	553.8	468.3
Profit Before Tax	1,906.9	2,623.8	2,399.6
Net Profit	1,504.3	2,326.0	2,141.3

BALANCE SHEET and CASH FLOW (SGD mn)	2016A	2017A	9M18
Cash and Bank Deposits	4,792.6	6,105.3	5,346.6
Net Debt	10,059.0	15,590.0	16,549.8
Shareholders Equity	24,300.0	32,083.0	32,754.3
Total Assets	45,740.6	61,445.3	63,065.2
CFO	3,305.2	2,166.3	1,215.9
Capex	75.9	149.3	74.1
Acquisitions	(899.9)	(4,311.2)	(1,671.5)
Disposals	325.7	2,724.8	522.3
Free Cash Flow	3,229.3	2,017.1	1,141.8

KEY RATIOS	2016A	2017A	9M18
EBITDA Margin (%)	24.2	32.4	38.5
Net Margin (%)	28.6	50.5	53.8
Net Debt to EBITDA (x)	7.9	10.5	10.8
Net Debt to Equity (x)	0.4	0.5	0.5
Net Debt to Total Assets (x)	0.2	0.3	0.3
EBITDA to Interest (x)	2.5	2.7	3.3

Source: Company Data, KGI Research

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Rating	Definition
	KGI Securities Research's recommendations are based on an Absolute Return rating system.
BUY	>10% total return over the next 12 months
HOLD	-10% to +10% total return over the next 12 months
SELL	<-10% total return over the next 12 months

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