

Money Talk

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Treasury China Trust
An undiscovered commercial property gem in China

NOT RATED --%
Price/Target S\$2.15/S\$--
Mkt. Cap/F. Float S\$548.0m/30%

Fundamental View

Investment Highlights

- Pioneer in commercial asset enhancement in China.** Treasury China Trust (TCT) undertook asset enhancement initiatives (AEI) on its underperforming asset Central Plaza (2007/08) at a capital expenditure of Rmb47.0m (3.2% of initial cost), transforming the asset from an income stream of 5.5% yield on cost to 6.7% yield on cost. The AEI resulted in a 17.5% increase in capital values and a 25.1% increase in rent roll for the building. More such AEIs are in place for its other underperforming assets, City Center and Huai Hai Mall. This is likely to result in a significant boost to its income stream and NAV.
- Repositioning of City Center to significantly boost its recurring income.** City Center is a large retail-office project (40%/60%) in Shanghai's Hongqiao Area, and is currently TCT's largest income-producing asset, accounting for 71% of its gross rental income in 1Q11. The development comprises a gross floor area (GFA) of 180,000sqm, including twin 25-storey office towers, a seven-level retail podium and a pedestrian-oriented food and beverage mall. TCT plans to undertake a comprehensive renovation and develop Phase 2 and Phase 3 of the project at an estimated capex of Rmb1b. The project is expected to be completed by 2013. The repositioning of the mall from a low mid-end segment to mid high-end market and revamping of its tenant mix are likely to double the average rental of the mall from the current Rmb2.50psm/day to Rmb5.00psm/day. This presents good upside potential for its recurring income.
- Qingdao mall – A strategic acquisition.** In Dec 10, TCT announced the acquisition of a 55% stake in the Central Avenue mall at Qingdao from Trio group for Rmb477.0m, at a steep 54% discount to the market price. The acquisition also comes along with a five-year Rmb51m rental guarantee which translates into a 10% yield to cost. The mall comprises an existing 43,463sqm GFA shopping mall and three adjoining retail zoned sites of 335,000sqm of GFA expected to be developed as three separate projects by 2015. TCT will retain a majority equity and managerial control of these projects. Upon full completion of the mall, TCT expects to obtain a 15% yield to cost from the development.
- Huai Hai Mall acquired at an attractive price.** In Feb 11, TCT announced the acquisition of Huai Hai Mall in Shanghai for Rmb575.0m, a 21% discount to its open market value of Rmb724m and at 4.9% yield to cost. The property is currently 70% occupied with average rental of Rmb18psm/day, much lower than some of the nearby high-end mall rentals of Rmb40-45psm/day. TCT plans to undertake an AEI by 2013 with the lease expiry of all but two tenants, which should nearly double the existing rental income from the asset.

Price Chart



Financials

FYE 31 Dec (S\$ '000)	2010*	1Q11
Gross Revenue	39.6	19.5
Net property Income	22.6	12.5
EBIT	90.9	16.7
Profit Before Tax	52.6	9.3
Net profit	39.6	7.0
EPS (cents)	16.3	2.7
P/E (x)**	13.2	19.9
P/NAV (x)	0.57	0.59
Dividend yield (%)**	4.7	4.7
Net profit margin (%)	100	36
Net gearing (%)	27.6	28.1
Interest cover (x)	2.4	2.3
ROE (%)	4.1	3.0

*- 2010 is a six month period since TCT's listing on 21/6/10 ** - Annualised
Source: TCT, Bloomberg, UOB Kay Hian

Background

Treasury China Trust (TCT) is a Singapore-based business trust and is a leading owner, manager and developer of commercial real estate in China. It has assets under management in excess of Rmb12.0b and a portfolio of more than 800,000sqm office and retail properties. Its portfolio comprises of four income-producing assets and five development assets strategically located in the prime business areas of Shanghai, Beijing and Qingdao. TCT is powered by Treasury Holdings Group, Ireland's largest property group.

- **Trust structure to balance growth vs yields.** TCT is listed as a business trust vehicle as compared to a REIT and hence not subject to the development cap restriction of 10% and gearing limit of 35%. This provides TCT with better opportunity to capitalise on the attractive development opportunities in China while balancing a stable income from its assets. As at Jun 11, 37% of its portfolio value is derived from stabilised assets while 21% of its assets are under development and 42% in landbank.
- **Looking at potential acquisition opportunity in Xian.** TCT is currently looking at a potential acquisition opportunity in Xian, the capital of Shanxi province. The acquisition is likely to be a mix of development and income-producing assets targeting retail space. The trust currently has a gearing of 35.4% and has potential debt headroom of S\$200m before it hits a self-imposed gearing cap of 45%. Management noted it will continue to focus on commercial assets in major Chinese cities with Shanghai remaining its key market.

Industry Outlook

- **Retail:** Based on DTZ Research, Shanghai high-end retail has a total stock of 2.2m sqm with average rental of Rmb54.7psm/day and average occupancy of 97.5%. Over the next three years, an estimated supply of 1.1m sqm (about 50% of existing stock) is likely to cap rental growth.
- **Office:** According to DTZ Research, Shanghai Grade-A office has current stock of 4.4m sqm with average rental of Rmb7.34psm/day and an availability ratio of 9.42%. Over the next four years, total new supply of about 4.32m sqm (about 100% of existing stock) is expected to come on stream. Although we believe the demand drivers are in place, the huge supply is likely to slow down the pace of growth in rental markets.

Catalysts

- Upside potential from the AEI, repositioning of its underperforming assets City Centre and Huai Hai Mall and its development asset at Qingdao.
- Key beneficiary of urbanisation drive and rising consumerism in China with assets located at prime locations in Shanghai and Qingdao
- Trading at a discount of 41% to its net asset value and 48% to peers' average.

Key Risks

- Huge incoming supply in office and retail space in Shanghai.
- Stringent measures targeting commercial property segment in China
- TCT's inability to retain its key corporate client base.

Valuation

- TCT is currently trading at a steep discount of 41% to its NAV of S\$3.67/share and a 47% discount to peers' average.
- The stock is currently trading at 4.7% dividend yield based on the committed distribution of 10 cents for 2011.

Peer Comparison

Company	Price (S\$)	Market Cap (S\$ m)	FY 11 Yield	NAV per Unit	Prem/(disc) to NAV
Perennial China Retail Trust*	0.7	785.2	5.3%	0.67	4%
CRCT	1.22	763.7	6.9%	1.12	9%
CMA	1.57	6099.6	1.1%	1.5	5%
Average			4.4%		6%
TCT	2.15	548.0	4.7%	3.67	-41%

* Based on listing data

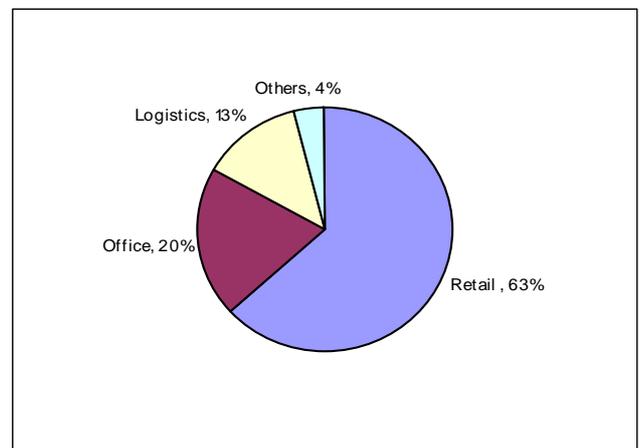
Source: Bloomberg, UOB Kay Hian

TCT Portfolio



Source: TCT.

Asset Portfolio breakdown by GFA*



*Includes development and income-producing assets; assumes 100% ownership of Central Avenue Mall

Source: TCT, UOB Kay Hian

TCT major corporate clients.



Source: TCT.

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