Sector updates

Singapore Hospitality – Beneficiary of vaccine development

Chu Peng
Equity Research

Singapore | Real Estate

The Path to a New Normal

Investment summary

Hospitality REITs' share price performances have been boosted by rapid vaccine progress from companies such as Pfizer and BioNTech, Moderna, and AstraZeneca and Oxford University's potential Covid-19 vaccine etc. We have turned more positive on hospitality REITs following these encouraging developments and believe the worst is likely over with gradual recovery ahead. However, near-term challenges remain with resurgence of Covid-19 in Europe, US and Hong Kong and depressed travel demand. RevPAR/RevPAU and profitability could remain under pressure in 4Q20 and 1H21. While we see a recovery in 2021, particularly stronger in 2H21, we expect a full recovery of RevPAR/RevPAU to pre-Covid-19 levels only in 2022 or 2023, assuming the vaccine will be widely available by mid-2021.

For the three hospitality REITs under our coverage, our order of preference is **Ascott Residence Trust (ART SP) [BUY; FV: S$1.20], CDL Hospitality Trusts (CDREIT SP) [HOLD; FV: S$1.39]** and **Far East Hospitality Trust (FEHT SP) [HOLD; FV: S$0.66]**. While the three hospitality names under our coverage rallied 13%-27% in November, we believe valuations are still undemanding, especially given the positive progress on vaccines and a more visible roadmap to recovery in 2021. The re-rating of hospitality REITs could continue given the forward-looking nature of investors who are likely to focus more on normalised FY22 earnings, although volatility in share prices is likely.

- Worst is likely over
- Recovery to pick up in 2H21
- Improved outlook on rapid vaccine development

Sequential improvement in RevPAR/RevPAU

While RevPAR/RevPAU was still down YoY due to headwinds from Covid-19, we saw some recovery in 3Q20 as compared to 2Q20, driven by easing travel restrictions, reopening of temporarily closed properties, recovery in domestic travel in some markets, block bookings from government as well as bookings from foreign workers affected by border closures. (Exhibit 1)

Ascott Residence Trust's (ART) 3Q20 portfolio RevPAU fell 70% YoY to S$47 but improved 27% on a QoQ basis. Average portfolio occupancy increased from 30% in 2Q to 40% in 3Q20. For CDL Hospitality Trusts's (CDLHT) Singapore (excluding W Hotel) portfolio, RevPAR fell 60.9% YoY in 3Q to S$64 but improved 8.5% QoQ. Including W Hotel, RevPAR would have fallen 58.2% YoY but improved 27% QoQ on strong staycation demand at W Hotel. Performances of CDLHT's overseas hotels were generally weaker despite some recovery QoQ. The only exceptions were New Zealand (RevPAR of +0.4% YoY in 3Q, helped by government's isolation business) and Australia (essentially on fixed rent structure).

For Far East Hospitality Trust (FEHT), its Hotel segment's RevPAR was down 56% YoY to S$67 (+4.4% QoQ), while RevPAU for its Serviced Residences' (SR) segment fell 20% YoY to S$157 (+2.6% QoQ). Overall, the performances of Serviced Residences (SR) remained more resilient as compared to Hotels, helped by SRs' long-stay leases from corporate business.

Exhibit 1: 3Q20 RevPAR/RevPAU summary

	Far East Hospitality Trust	Ascott Residence Trust	CDL Hospitality Trusts
3Q20 RevPAR growth (YoY) (for SG hotels)	-56%		-61%
3Q20 RevPAU growth (YoY) (for SG Serviced Residences)	-20%	-70%	
3Q20 RevPAR growth (QoQ) (for SG hotels)	4%		9%
3Q20 RevPAU growth (QoQ) (for SG Serviced Residences)	3%	27%	

Source: REIT manager

Occupancies continued to be supported by alternative sources of income but demand likely to taper off in 4Q20

Overall, we observe that 1) Japan, Europe, UK, US and Maldives were among the worst performing countries for ART and CDLHT due to travel bans and lockdowns; 2) countries with large domestic markets such as China led the recovery; 3) countries catering to transient travellers e.g. Japan, UK, US were more impacted than those catering to long-stay travellers e.g. China, Singapore and Vietnam; 4) occupancies continued to be supported by alternative sources of income such as bookings for self-isolation, healthcare personnel and workers affected by border shutdown, student accommodation for some countries such as Singapore, Australia etc.

While occupancies have largely been supported by alternative sources of income for Singapore in 9M20, we expect the demand for 'isolation business' and Malaysian Control Order (MCO) related-businesses to taper offer in 4Q20 as border reopens and the number of Covid-19 cases becomes more stabilised in Singapore. We understand from the management that the contracts with government for isolation business can be terminated after a short period of notice i.e. 21 days from the government.

Driving domestic tourism

To make up for losses in occupancies from Covid-19 and potential termination of government bulk-bookings in the coming months, ART, CDLHT and FEHT are tapping on opportunities relating to staycation to boost domestic tourism in Singapore. While hotel operators have received healthy demand from staycation due to pent-up demand, we believe that competition is intense and hotel operators likely to keep a cap on the occupancy rates due to social distancing and safety measures. We believe that staycation would remain largely a weekend business and it is unlikely to make up for losses in weekday occupancies and compensate for the income shortfall from Covid-19.

Near-term challenges remain but turning more positive over medium-term on vaccine developments

Hospitality REITs' share price performances have been boosted by rapid vaccine progress from companies such as Pfizer and BioNTech, Moderna, and AstraZeneca and Oxford University's potential Covid-19 vaccine etc. On 14 December, Singapore's Prime Minister Lee Hsien Loong announced in a nation address that Singapore has approved Pfizer and BioNTech's Covid-19 vaccine, with the first shipment expected to arrive by the end of 2020 and other vaccines to arrive in Singapore in the coming months. PM Lee also highlighted that there will be "enough vaccines for everyone" by 3Q21 if everything goes according to plan. Other measures already put in place such as social distancing and mass testing will continue alongside the vaccinations to help ensure that the virus is kept under control. These could continue for possibly a year or longer, according to PM Lee.

We have turned more positive on hospitality REITs following these encouraging developments and believe the worst is likely over with recovery ahead. However, near-term challenges remain with resurgence of Covid-19 in Europe, US and Hong Kong and depressed travel demand. RevPAR/RevPAU and profitability could remain under pressure in 4Q20 and 1H21. While we see a recovery in 2021, particularly stronger in 2H21, we expect a full recovery of RevPAR/RevPAU to pre-Covid-19 levels only in 2022 or 2023, assuming the vaccine will be widely available by mid-2021.

For the three hospitality REITs under our coverage, our order of preference is **Ascott Residence Trust (ART SP) [BUY; FV: S$1.20]**, **CDL Hospitality Trusts (CDREIT SP) [HOLD; FV: S$1.39]** and **Far East Hospitality Trust (FEHT SP) [HOLD; FV: S$0.66]**. ART remains our top hospitality pick as we like ART's defensive and geographically diversified portfolio amid a still uncertain outlook, coupled with its strong financial position. In addition, ART's geographically diversified portfolio with 68% of its assets in the Asia Pacific region could benefit from the earlier recovery given the more stabilised infection rates in the region.

As at 17 Dec's close, CDLHT is trading at 0.92x forward P/B which is slightly below its historical mean of 0.95x. We find valuations undemanding, especially given the positive vaccine development. While we still see headwinds from Europe (18% of FY19 NPI) with the resurgence of Covid-19 cases, the reopening of borders and easing travel restrictions in Singapore (62% of FY19 NPI) amid a stabilised Covid-19 situation could provide some buffer. Positive vaccine development could drive the recovery of international travel which would benefit Singapore given its lack of a domestic market.

As a pure-play hospitality REIT in Singapore, FEHT's recovery will largely depend on international tourists' arrivals which we believe will in turn depend on the availability of Covid-19 vaccines. While near-term demand will likely be driven by staycation and government bookings, FEHT will benefit as Singapore gradually reopens its borders amid low infection rates, easing travel restrictions and introduction of special travel arrangements. FEHT's fixed rent component which formed about 72% of the master lease rental in FY19, and its commercial segment i.e. office and retail (19% of FY19 gross revenue) could also provide some buffer and downside protection in the near-term.

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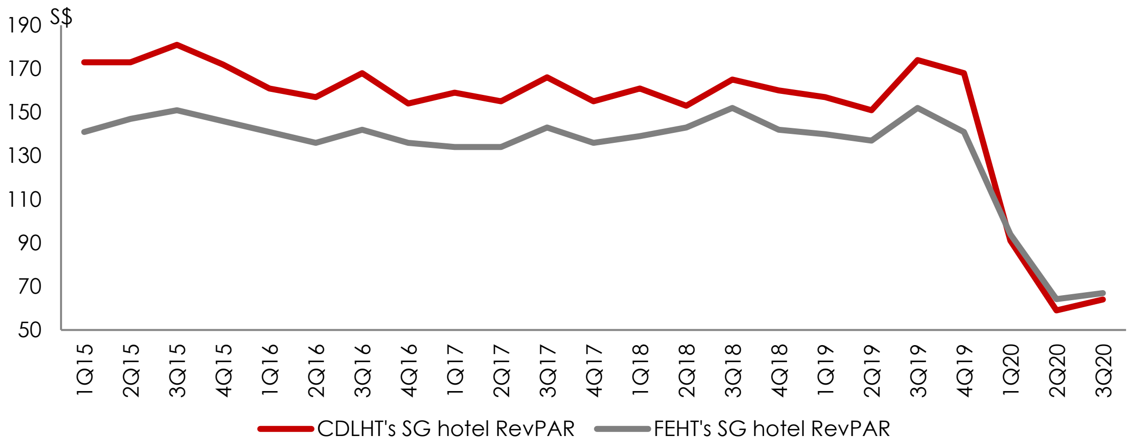
Exhibit 2: Ratings, potential returns, and dividend yield

Counter	Ticker	Last Close as at 17 Dec (S$)	Fair Value (S$)	Distribution Yield FY20	Distribution Yield FY21	Potential Total Returns	Rating
Ascott Residence Trust	ART SP	1.10	1.20	2.5%	4.4%	11.5%	**BUY**
CDL Hospitality Trusts	CDREIT SP	1.30	1.39	2.6%	4.8%	9.5%	**HOLD**
Far East Hospitality Trust	FEHT SP	0.625	0.66	3.8%	5.1%	9.4%	**HOLD**

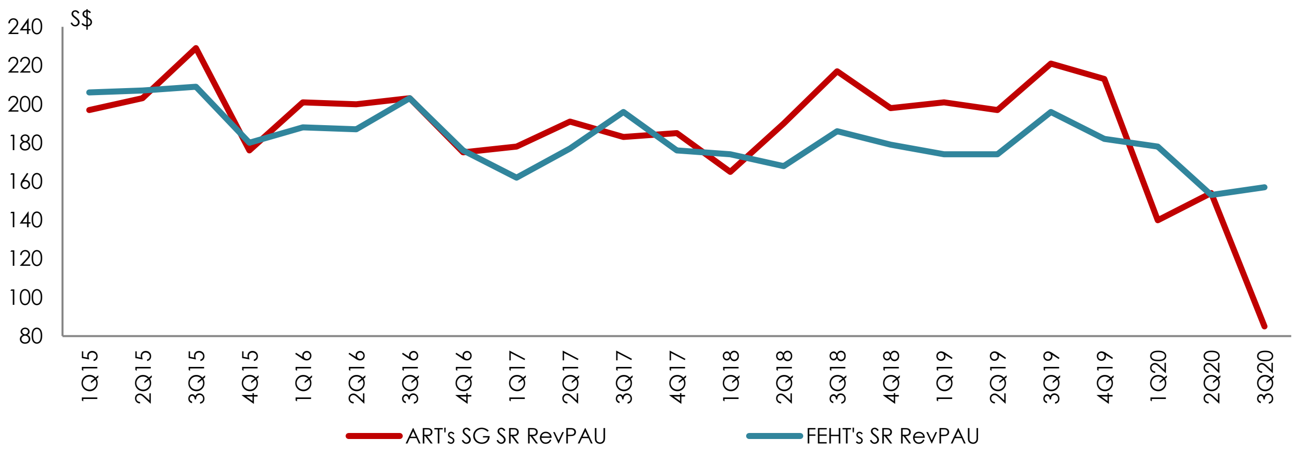
Source: Bloomberg, Internal estimates

Exhibit 3: SG Hotels RevPAR trend for S-REIT counters under our coverage since 2015



Source: REIT Managers, internal estimates

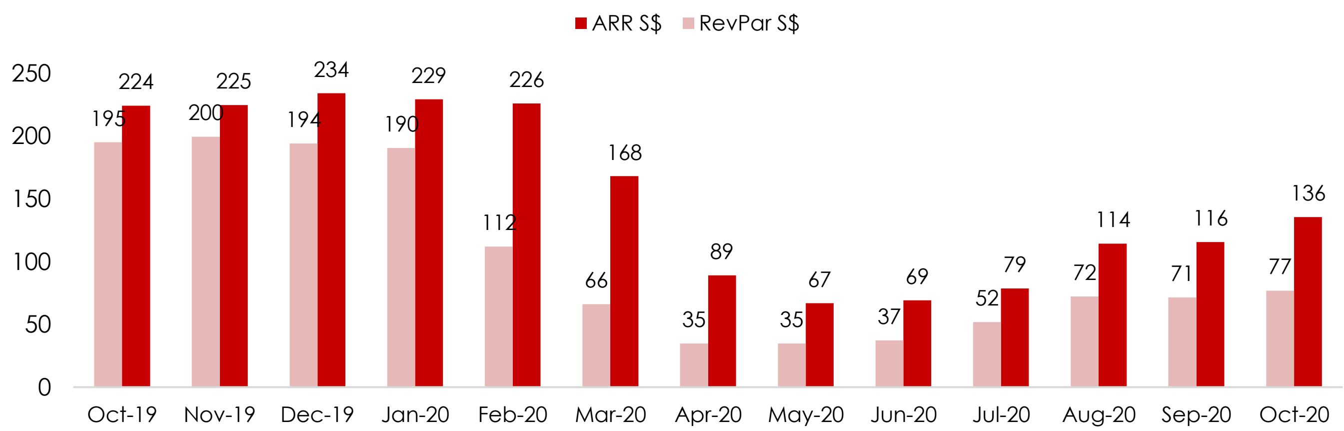
Exhibit 4: SG Serviced Residences RevPAU trend for S-REIT counters under our coverage since 2015



Source: REIT Managers, internal estimates

Note: ART's Somerset Liang Court Singapore was divested and ceased revenue recognition in July 2020

Exhibit 5: Monthly Trend of ARR and RevPAR for SG hotels



Source: Singapore Tourism Board

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