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Research Update:

Singapore-Based CapitaLand Mall Trust Assigned 'A-' Rating With Stable Outlook

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Rating Action Overview

- CapitaLand Mall Trust (CMT) has strong asset quality as the largest retail REIT in Singapore. It will be the second-largest REIT in Asia-Pacific by market capitalization after CapitaLand Commercial Trust (CCT) merges with CMT.
- Post the merger, which is scheduled to be completed by November 2020, CMT will have an enlarged and diversified portfolio of competitive and well-positioned retail, commercial, and integrated assets that have had stable operating metrics through the COVID-19 pandemic.
- The partial debt-funded merger and consolidation of the more indebted CCT will increase CMT's leverage.
- On Sept. 30, 2020, S&P Global Ratings assigned its 'A-' long-term issuer credit rating to CMT. At the same time, we assigned our 'A-' long-term issue rating to CMT's guaranteed senior unsecured multicurrency medium-term note (MTN) and euro MTN programs.
- The stable outlook on CMT reflects our expectation that the REIT will successfully integrate CCT's assets. We also anticipate CMT will maintain or enhance its solid asset quality and stable profitability over the next 24 months.

Rating Action Rationale

The rating on CMT reflects our view of the REIT's leading market position (post-merger with CCT) as a landlord of retail and commercial space in Singapore. CMT's large asset portfolio with high quality assets, diverse rental income and tenant base, and above-average operating metrics support its credit profile. The REIT's high initial leverage due to the consolidation of the more leveraged CCT temper these strengths. The merger of CCT will be partially debt-funded.

The merger will solidify CMT's pre-eminent position among REITs in Singapore. CMT will then be the second-largest integrated REIT in Asia-Pacific by market capitalization, behind Hong Kong-based Link REIT, and the largest in Singapore. CMT will have a sizable portfolio of Singapore dollar (S$) 22.4 billion, with 24 prime assets and a balanced portfolio comprising retail, commercial, and integrated development across Singapore. CMT is already the largest shopping mall owner in Singapore with 10.6% market share by net lettable area (NLA) as of June 30, 2020 (based on CBRE Pte. Ltd.'s basket of private retail stock, which includes retail space from shopping malls, retail podiums and mixed-use developments). Its market share is almost twice that of the second-largest player. The REIT will also be the largest owner of "Grade A" office assets in Singapore's central business district (CBD) by NLA post-merger.

CMT's enlarged portfolio is smaller and less diversified than that of similar rated global peers. The REIT's portfolio size will double to S$22.4 billion post-merger. This will help it to benefit from economies of scale and cost rationalization.

However, CMT's portfolio is smaller and less geographically diversified than that of global peers such as Simon Property Group and Brookfield Property Partners, who have leading market positions in their respective regions. The global peers operate in deeper real estate markets and need a larger scale to maintain strong market positions. CMT will have a dominant market position in the smaller and dense Singapore market, which has high barriers of entry. This factor will partially offset CMT's smaller scale and greater concentration to a single country.

CMT has very competitively positioned assets. All of the REIT's retail and integrated properties are strategically located near core transportation nodes in Singapore, providing it a strong captive shopper market.

CMT's periodical asset enhancement initiatives (AEIs) have sustained the quality of these assets and boosted their attractiveness for tourists and shoppers. The REIT's portfolio will also consist of high-quality office properties. About 72% (by NLA) of its commercial assets are Grade A assets located in the core markets of Singapore and Frankfurt, Germany.

Above-average operating metrics support CMT's earnings. The REIT will likely have stable performance and outperform peers in the next 12-24 months. This is despite market headwinds from the ongoing COVID-19 pandemic. CMT's retail and commercial portfolios have shown good stability and resilience through industry cycles, with sustained high occupancies and satisfactory increases in rent on lease renewal. This is due to good quality assets protected by "flight to quality" sentiment. As of June 30, 2020, the occupancy for CMT's retail portfolio was 97.7% and it was 95.2% for CCT's commercial portfolio, compared with the Singapore islandwide retail occupancy of 90.4% and Singapore CBD occupancy of 94.4%.

CMT's stable performance is also underpinned by its active management of lease expiries and diverse revenue streams. Although the REIT's retail lease expiry profile of 2.3 years (by NLA, as of June 30, 2020) is shorter than that of retail peers in other developed markets, this is tempered by CMT's high retail retention rate. The REIT had a retention rate of 90% for its retail portfolio in the first half of 2020 despite the COVID-19 disruption. CMT's diverse revenue streams post the consolidation of CCT's commercial portfolio (which has a longer lease expiry of 5.7 years by NLA, as of June 30, 2020) will also help offset the shorter retail lease profile. Such diversification to office assets will provide CMT with more stable cash flows in the event of a downturn in any one real estate segment. Yet, the REIT will remain largely exposed to the Singapore market, with less than 5% of net property income (NPI) contribution from Frankfurt.

CMT's assets are well placed to withstand sectoral disruption from digital services and market headwinds from COVID-19. The REIT is not immune to structural headwinds due to acceleration of online shopping and e-commerce since the COVID-19 outbreak. However, CMT's strategically located and high quality retail assets, and active tenant management underpin its resilience. The REIT has detailed tenant profile segmentation, and a secure tenant base that can withstand disruption of digital service. Singapore's dense population and strong shopping mall culture help to create more stable and recurrent traffic volumes than for mall operators in other regions. As such, we consider CMT to be well positioned to manage potential digital disruption in the retail segment.

We estimate the disruption of operations due to COVID-19 will dampen CMT's (excluding proposed merger proforma adjustments) 2020 NPI by 17%-20% to S$460 million–S$470 million, compared with S$558 million in 2019. The lower NPI is due to a combination of factors, including a two-month rental waiver provided by the landlord, decline in gross turnover revenue, and lower car park income. This will result in a fall in the ratio of funds from operations (FFO) to debt to about 8% for the full year of 2020 from 11% in 2019.

We expect CMT's retail operation to gradually rebound as Singapore eases social distancing restrictions and shopper traffic recovers. About half of CMT's retail portfolio consists of suburban retail malls that have been major beneficiaries in past three months since Phase 2 of the government's "Circuit Breaker" lockdown to limit the spread of COVID-19. By the end of August 2020, CMT's shopper traffic had recovered to 58% of pre-COVID-19 levels.

Over the next six to 12 months, we anticipate a gradual recovery in the more centrally located malls, which are dependent on office workers returning to work following relaxation of remote working requirements. We forecast CMT's 2021 NPI will recover to S$530 million-S$540 million, still about 5% lower than the 2019 level.

We expect a milder impact of COVID-19 on CCT's office assets, earnings, and cash flows, as compared with retail assets. Requests for rental relief or deferrals from the REIT's tenants as per the government rental relief framework are low. We estimate the total rental rebate (mostly NPI neutral) to be S$10 million-S$11 million in 2020.

Overall, we anticipate CCT's stand-alone 2020 NPI will be 5% lower than in 2019, and will gradually recover to about 2019 levels in 2021 due to increasing contribution from AEIs at its Six Battery Road and 21 Collyer Quay office buildings.

CMT's leverage to worsen due to the CCT merger. This is because CMT may take on an additional S$1 billion in debt to fund the merger.

In addition, CMT's financial profile will weaken because it will consolidate the more leveraged CCT. We forecast CMT's pro forma debt post-merger will be S$9.4 billion over the next two years, leading to a FFO-to-debt ratio of 7.5%-8.5%.

We expect CMT to maintain an aggregate gearing ratio (ratio of gross borrowings to total assets on a look-through basis) less than 40%. Post-merger, we forecast CMT's aggregate gearing ratio will be about 39%, leaving CMT with limited headroom for more significant debt-funded acquisitions or developments.

Outlook

The stable outlook on CMT reflects our expectation that the REIT will integrate CCT's assets before the long stop date of Nov. 30, 2020. We also anticipate CMT will maintain its solid asset quality, stable profitability, and operate in line with its financial policy of maintaining a gearing ratio of below 40% over the next 24 months.

Downside scenario

We could lower the rating on CMT if the REIT's FFO-to-debt ratio weakens below 7% on a sustained basis. The most likely cause for this deterioration could be CMT embarking on an aggressive debt-funded growth strategy that results in the gearing ratio being above 40%. A prolonged economic downturn that results in lower tenant occupancy, declining rentals, and weakened operating efficiency could also weaken CMT's credit profile.

Upside scenario

We could raise the rating if CMT adopts a more conservative financial stance such that its FFO-to-debt ratio increases above 9% on a sustained basis.

Company Description

CMT is one of the largest retail REITs in Singapore. CMT owns and invests in assets that are predominantly used for retail purposes. The REIT manages 15 properties, with a portfolio value of S$11.4 billion as of June 30, 2020.

Our Base-Case Scenario

- Singapore's real GDP to contract by 5.8% in 2020 and grow by 6.3% in 2021.
- Our forecast on CMT is on pro forma, look-though basis, with full year consolidation of subsidiaries CCT and RCS Trust, and pro rata consolidation of joint ventures One George Street and CapitaSpring.
- A recession in Singapore will likely pressure growth in rental rates.
- Rentals for CMT's retail portion will decline by 3%-5% for at least the next six months. The negative trend will gradually ease to low-single-digits because malls have reopened since July and shopper traffic is recovering.
- Rentals for CCT's office portion will decline by 2%-3% over the next 12 months due to COVID-19. The negative trend will ease as the economy rebounds, but growth in rental rates will likely remain slightly negative or nil due to the coming supply wave in 2022.
- Occupancy of CMT's entire portfolio will remain above 95%, helped by the strategic location of its assets.
- Pro forma revenue to be S$1.43 billion-S$1.45 billion in 2021 and S$1.50 billion-S$1.52 billion in 2022.
- NPI margin will remain stable at 71%-73% in 2021 and 2022.
- Capital expenditure will be manageable relative to operating cash flows for the next 12-24 months.
- Pro forma debt to be S$9.40 billion-S$9.42 billion in 2021 and 2022.

CapitaLand Mall Trust -- Key Metrics*

	--Fiscal year ended Dec. 31--	
	2021f	2022f
(Mil. S$)		
Revenue	1,430-1,440	1,490-1,500

CapitaLand Mall Trust -- Key Metrics* (cont.)

	--Fiscal year ended Dec. 31--	
	2021f	2022f
EBITDA	970-980	1,020-1,030
Funds from operations (FFO)	720-730	770-780
Debt	9,400-9,410	9,400-9,410
Debt to EBITDA (x)	9.5-10.0	9.0-9.5
FFO to debt (%)	7.5-8.0	8.0-8.5
EBITDA interest coverage (x)	3.5-4.0	3.8-4.3

*All figures adjusted by S&P Global Ratings. f--Forecast.

Liquidity

We assess CMT's liquidity as adequate because the REIT's consolidated sources of liquidity are about 1.4x its liquidity uses over the 12 months to June 2021. We expect sources of liquidity to exceed uses even if EBITDA decreases by 10%.

We believe CMT has sound banking relationships and a satisfactory standing in domestic capital markets, reflected in its record of successful refinancing and note issuance. The REIT's funding is well diversified between bank facilities, MTN, and euro MTN notes. In addition, CMT has sufficient committed undrawn bank facilities as of June 30, 2020.

Liquidity sources include:

- Cash equivalents of S$81 million as of June 30, 2020.
- Estimated consolidated cash FFO of about S$535 million over the 12 months to June 30, 2021.
- Estimated positive working capital inflow of S$30 million during the period.

Liquidity uses include:

- Short-term debt maturities of S$647 million as of June 30, 2020.
- Estimated capital expenditure of S$90 million over the 12 months to June 30, 2021.
- Estimated dividends of about S$475 million during the period.

Covenants

We believe CMT has adequate headroom in the financial covenants related to its bank loans over the next 12 months. Major covenants include interest coverage ratio no less than 1.5x, and aggregate leverage limit of 50%, as construed in accordance with Property Funds Guidelines.

Issue Ratings - Subordination Risk Analysis

Capital structure

As of June 30, 2020, CMT's capital structure consisted of about S$4.0 billion of unsecured debt on a look-through basis.

Analytical conclusions

We rate CMT's guaranteed senior unsecured S$3.5 billion MTN program and US$3.0 billion euro MTN program 'A-', the same as the issuer credit rating. We do not view CMT's capital structure as having any material structural or contractual subordination risks. As of June 30, 2020, all of CMT's assets are unencumbered.

Ratings Score Snapshot

Issuer Credit Rating: A-/Stable

Business risk: Excellent

- Country risk: Very low risk
- Industry risk: Low risk
- Competitive position: Excellent

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: a-

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry, Feb. 26, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013

- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

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New Rating Action	
CapitaLand Mall Trust	
Issuer Credit Rating	A-/Stable/--
CMT MTN Pte.Ltd.	
Senior Unsecured Notes.	A-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.