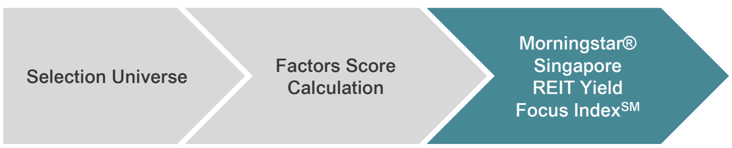
LION GLOBAL INVESTORS

Lion-Phillip S-REIT ETF

Low cost, easy access to Singapore REITs

Lion-Phillip S-REIT ETF is designed to provide investors with a low-cost access to 28 high-quality S-REITs[1] that offers a sustainable income stream. It is passively managed to fully replicate the Morningstar® Singapore REIT Yield Focus Index℠ (Index).

Index Construction Methodology



Morningstar® Singapore REIT Yield Focus Index℠

Assign scores for the following factors:
- Quality
- Financial Health
- Dividend Yield

Portfolio weights based on factors score: Adjusted for liquidity of underlying REIT

The Index is designed to screen for high-yielding REITs with superior quality and financial health

KEY FACTS

Full replication of the Morningstar® Singapore REIT Yield Focus Index℠("Index")

28[3] high quality S-REITs

Latest distribution of S$0.0289 per unit on ex-date 31 January 2020^

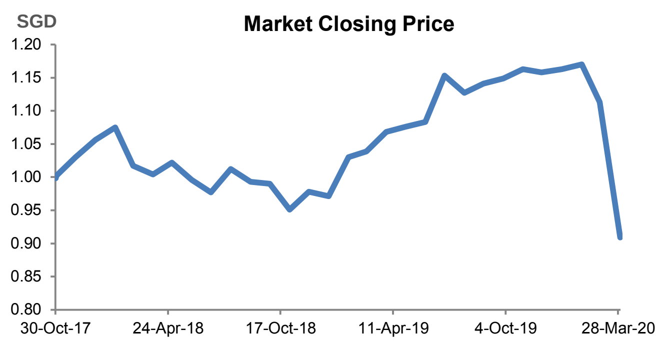
Gross current dividend yield of 6.2%[4]

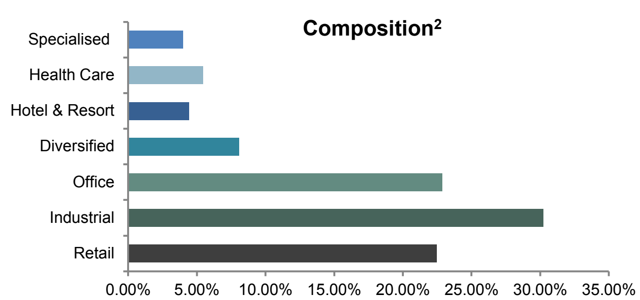
Total AUM: S$140.4million

Management fee: 0.50% p.a.

SGX stock code: CLR

Bloomberg ticker: SREIT SP





Source: Bloomberg, Lion Global Investors, as at 31 March 2020. ^Pay-date of 28 February 2020. Distribution is for the period from 1 July 2019 to 31 December 2019, and comprises of 100% distributable income[5] and 0% capital component. Past payout yields and payment do not represent future payout yields and payments. Distribution payments shall, at the sole discretion of the Manager, be paid out of either (a) income; or (b) net capital gains; or (c) capital of the fund or a combination of (a) and/or (b) and/or (c). The declaration and/or payment of distributions (whether out of income and/or capital) may have the effect of lowering the net asset value of the fund. For further detailed income statistics, please visit www.lionglobalinvestors.com

Singapore REITs Outlook

COVID-19 – A Black Swan Event

The start of 2020 has not been a good year for the markets, with MSCI World returning -22% year-to-date (as of 27 March 2020). This sharp correction in the equity market is mainly driven by what many described as a 'Black Swan event' – the emergence and global spread of the COVID-19 pandemic.

This pandemic has caused unprecedented lockdowns of borders globally, disrupting trade flows and supply chain movements and thus threatening global economic growth. Given the high level of uncertainty surrounding the virus and the global economy, investors have decided to adopt a risk-off approach by selling down riskier assets such as equities.

Singapore, given its open economy and borders, is not spared. As of 29 March 2020, we have more than 840 confirmed COVID-19 cases. The virus has also greatly impacted the Singapore economy, with 1st quarter of 2020 GDP contracting by 2.2%. Unsurprisingly, the equity market also suffered a hit, with the STI Index suffering a loss of 21.1% (as of 27 March 2020).

Perhaps more surprisingly, the REITs sector, which is often considered to be more resilient and defensive (given their long leases and stable income), also suffered a significant decline. The FSTREI Index generated a negative total return of 21.3% (as of 27 March 2020), in line with the general equity market. This has raised some concerns by investors, questioning the resilience of the sector.

Singapore REITs – Breaking It Down Fundamentally

Fundamentally, we do see some earnings pressure on the Singapore REITs sector. In particular, we believe that the hospitality REITs are most vulnerable. Given the lockdown of borders globally and a general aversion for people to travel, hotel occupancies and room rates are going to be severely affected. In February, Singapore revenue per available room declined by 41% year-over-year on the back of a 51% decline in tourist arrivals. We expect these figures to continue to be weak over the next few months, as we enter the worst stage of the spread of the virus globally.

To combat the spread of the virus within the community, the Singapore government has introduced a slew of social distancing measures. This includes the introduction of a circuit breaker between 7 April and 4 May 2020 to reduce movements and interactions in public and private places. Schools will move towards full home based learning and most physical workplaces premises (except those providing essential services) are also closed.

These measures, plus the fear of the virus itself, have caused a sharp decline in footfall and retail sales in malls, especially those malls in the city which focus on discretionary spending. A new law that obliges commercial property owners to unconditionally pass on their property tax rebate in full to their tenants has been passed, potentially putting pressure on their earnings. We estimate that distribution per unit ('DPU') could fall up to 10% year-over-year for the retail REITs.

We believe that the negative impact of COVID-19 on office sector will be muted. Tenants, especially the Multinational Corporations, usually take a longer term view when planning for their office space needs. Given that the impact of the virus is likely to be short-lived (less than 1 year), we do not expect much disruption to office demand over the longer term. That said, given the impending recession, we expect tenants to be more price sensitive during their rental negotiation. As such, it will be tough for office landlords to eke out high positive rental reversion for their portfolios this year. We expect DPU decline for the office REITs to be slight, at less than -3% this year.

Similarly, the industrial sector is likely to be largely unaffected by the virus. In fact, the sector could actually be a beneficiary from this unfortunate episode. Due to the social distancing measures, people are staying at home more, hence turning to online shopping to cater to their daily needs. This will drive up the demand for logistics space. Also, people at home are likely to turn to online channels for social (Facebook, Instagram) and entertainment (Netflix, Disney Plus) reasons. This will help to drive demand for data centres, which is another growth driver for the industrial REITs.

Balance sheet – Not A Problem

Apart from operating fundamentals, we also examine the balance sheet strength of the Singapore REITs sector. Compared to the Global Financial Crisis ("GFC"), the Singapore REITs' balance sheet is in a much better shape. Gearing level is healthy at below 35% (as of end-2019) and debt expiry is well spaced out. More importantly, Singapore REITs have secured multiple funding channels (Medium Term Note, corporate and retail bonds etc), instead of solely relying on bank loans like they did during the GFC.

As such, we believe that most of the Singapore REITs are in a strong financial position to weather this COVID-19 storm.

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Decline Exacerbated by Margin Calls

While COVID-19 has put some downward pressure on earnings on the Singapore REITs sector, the volatile intraday trading and the drastic 20+% decline in FSTREI Index (as of 27 March 2020) since the start of the year suggest to us that there are other factors behind this correction.

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As discussed in a Business Times[6] article, Chinese tycoon Tong Jinquan have sold almost S$14 million worth of Singapore REITs over the past few weeks. The article suggests that this significant selling could be due to margin calls by his private banks.

Buoyed by low interest rates and high demand for yield-producing assets, private banks have, over the past few years, extended leverage to their high net worth clients to buy into Singapore REITs, which they deem to be stable and low risk investments. Our channel checks suggest that this recent round of correction is exacerbated by margin calls on these Singapore REITs investments, hence creating a vicious selling cycle for the sector.

Unfortunately, it is difficult to quantify the magnitude of this forced selling on the Singapore REITs due to margin calls; nor do we know when this wave of selling would end. However, we firmly believe that the fundamentals of the Singapore REITs are solid and the drastic correction on the sector has created an attractive buying opportunity for investors seeking long term, stable investment returns.

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Looking ahead

While the economic disruption caused by COVID-19 is unprecedented, we believe that the Singapore economy has the ability to bounce back quickly. On 26 March, Deputy Prime Minister Heng Swee Keat delivered the Resilience Budget, a landmark S$48 billion package to help steer Singapore through this challenging period. Apart from offering cash handouts to all Singaporeans, the Budget also introduced targeted stimulus to support sectors that are most affected by the virus. In particular, the property tax rebate to commercial landlords would be able to help REITs mitigate some loss of income due to the crisis.

Following the 20+% correction in FSTREI Index (as of 27 March 2020), the Singapore REITs sector is currently trading at an attractive forward yield of 6.3% and this compares favorably against the US 10-year Treasury yield of about 0.7%. In fact, this 5.6% yield spread is more than 1 standard deviation above historical mean, suggesting that the sector valuation is very attractive relative to history.

With the Fed fund rate back to near-zero levels and the Fed resuming its quantitative easing (QE) program, we expect interest rates to remain low for a long time. We believe that the Singapore REITs sector has the ability to do well under this low and supportive interest rate environment. For long term yield seeking investors, the recent correction may be an opportunity to buy into good quality Singapore REITs for a more broad-based sector exposure.

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Notes

[1]S-REITs are securities constituting the Morningstar® Singapore REIT Yield Focus Index℠.

[2]Composition chart does not add up to 100%. Cash and cash equivalents as at 31 March 2020 was approximately 2.55%.

[3]As at 31 March 2020. The number of S-REITs which constitutes the Index may be changed by Morningstar Research Pte Ltd from time to time.

[4]Based on the weighted average 12-month trailing dividend yield of the underlying S-REITs as at 31 March 2020. Past payout yields and payments of the underlying S-REITs do not represent future payout yields and payments.

[5]Distributable income refers to the interest and dividend income, taking into consideration the net realised gains, a collective investment scheme receives from its portfolio holdings and are payable to its investors.

[6]https://www.businesstimes.com.sg/companies-markets/china-tycoon-sells-s14m-of-esr-reit-and-ireit-units-in-a-fortnight

For more information on the Lion-Phillip S-REIT ETF, please visit:
http://www.lionglobalinvestors.com/en/disclaimer-etf.html or email us at contactus@lionglobalinvestors.com.

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