

Sabana Industrial REIT (M1GU.SI)

NON RATED



Partial offer by Volare unlikely to lead to counter-bid

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- Volare Group AG has made an offer to buy a further 10% shares in Sabana Industrial REIT at S\$0.465 per share, raising its stake from 5.4% currently.
- We believe that Volare has no intention to privatise or take control of Sabana REIT on its own. However, this could prompt ESR, another significant shareholder of Sabana REIT, to act. In our view, is unlikely that ESR will launch a counter-bid as Sabana REIT is less important to ESR than before.
- Sabana REIT's distribution growth is expected to slow down with the redevelopment cost of 1 Tuas Avenue 4 and significant increase in supply of industrial land.
- Sabana REIT currently offers a dividend yield of 6.7%. It trades at a premium to other industrial REITs, except for Mapletree Logistics Trust.

What happened?

Volare Group AG has made an offer to buy a further 10% old shares at S\$0.465 per share. The price includes Sabana's final distribution of 1.46 cents for 2H22. If this deal successfully completes after this distribution, the offer price drops to S\$0.45 per share.

Volare is one of Switzerland's leading suppliers of fossil fuels. It has investments in real estate and real estate companies in Europe.

Our view

A potential tussle for control

Volare has no intention to privatize and take control of Sabana on its own, in our view, given that it only wants to buy 10% additional stake. This will take their stake to 15.4%, if successful.

However, if it were to join hands with Quarz, another significant shareholder of Sabana, their combined stakes will be larger than ESR's. They could demand board seats, and could replace or seek control of the REIT manager.

Potentially, this could prompt ESR to act, either to launch a counter bid at a higher price, or sell out completely.

Sabana is not as important to ESR as before

A previous attempt by ESR REIT (now known as ESR Logos REIT) to acquire Sabana fell through in Dec 2020, at S\$0.377 a unit. At that time, Quarz and another shareholder, Black Crane, contended that the offer price was too low. Sabana unitholders rejected the amendments to the trust deed, which led to the termination of the deal.

This time round, we think it is unlikely that ESR Group will launch a counter bid, or re-initiate the previous exercise. ESR-Logos currently trades at 7.7% yield and 1 time Price to book. Sabana trades at a distribution yield of 6.7%, and price to book value of 0.85x. A share swap into Sabana's shares at current price puts ESR-Logos shareholders at a disadvantage, given that Sabana's valuation is at a premium to that of ESR-Logos.

Debt funding option is also limited given that ESR-Logos' aggregate leverage is at 40.6%. With an adjusted interest cover of 3.1 times, an increase in debt could lift aggregate leverage and lower interest coverage. The limit on leverage is 45% if interest cover falls below 2.5x.

ESR's market cap is S\$13.2b. Its holding in Sabana is worth S\$100m, and in ESR-Logos, \$366m. Sabana accounts for less than 1% of ESR's market cap.

DPU growth to slow

The redevelopment of the property at 1 Tuas Avenue 4 will commence in 1Q23 and complete by 4Q23, at an estimated cost of about S\$20m. The cost of development will eat into distributions to unitholders.

Sabana is in the midst of securing tenants for this asset. We estimate that it would generate 0.16 cents/share to DPU and raise NAV by 1 cent to 54 cents/share if fully occupied.

Supply of new industrial property picked up in 4Q22. According to JTC, this has lowered overall occupancy rate by 0.3 percentage points in 4Q22, compared to 3Q22. Nonetheless, rental and prices still rose 2.1% and 1.7% in 4Q22, compared to 3Q22.

In addition, potential supply of new industrial properties is expected to increase in 2023 and 2024. MTI's Industrial Government Land Sales programme for 1H23 will release 7.16 hectares of land for tender, compared with 4.48 hectares and 6.36 hectares offered in 1H22 and 2H22, respectively. The significant increase in potential supply could exert pressure on rental and occupancy rates.

What would Beansprout do?

Sabana commands a premium to other industrial REITs, except for Mapletree Logistics Trust. It is trading at a distribution yield of 6.7%, compared with AIMS APAC REIT (7.5%) and ESR-Logos Industrial REIT (7.7%). This priced in Sabana's stronger debt/asset ratio of 32.4% and interest cover of 3.8x.

About Sabana Industrial REIT

Sabana Industrial REIT owns 18 industrial properties in Singapore with total net lettable area of 3.5 million sq ft. It is the smallest listed industrial REIT in Singapore with a portfolio value of S\$0.9b.

Major shareholders are ESR Group Ltd (20.7%), Quarz Capital Asia (Singapore) Pte Ltd (11.7%), and Volare Group AG (5.4%). The parent company of ESR Group also owns the REIT manager. ESR Group also has a 14% stake in another listed larger industrial REIT, ESR-Logos REIT, which owns 82 properties at portfolio value of S\$4.9bn.

Disclosure Appendix

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