

## REAL ESTATE EQUITY RESEARCH

## Price Performance

## ARA US Hospitality Trust

SGX: XZL

Bloomberg: ARAUS:SP

ISIN Code: SGXC80011726

Country: Singapore

Industry: Real estate, Hotel

8 April 2020

RECOMMENDATION: BUY

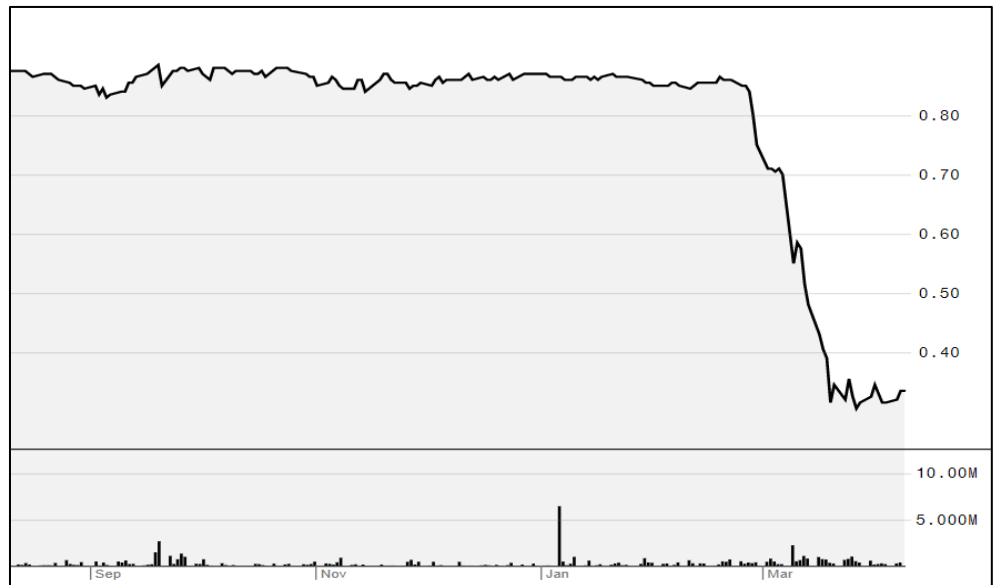
Current Price: US\$0.335

Target Price: US\$0.470

Stapled Securities: 567.34 million

Market Capitalisation: US\$190.06 million

52 Week Range: S\$0.280 - S\$0.900



Source: Bloomberg

## Company description

ARA US Hospitality Trust ("ARA H-Trust") is a Singapore-listed hospitality stapled security comprising ARA US Hospitality Property Trust ("ARA H-REIT") and ARA US Hospitality Management Trust ("ARA H-BT"). ARA H-Trust invests in income-producing real estate assets used primarily for hospitality purposes in the United States ("US"). As at 17 January 2020, ARA H-Trust's portfolio comprises 41 select-service hotels across 22 states in the US with a total of 5,340 rooms.

## Summary

ARA H-Trust's share price held up relatively well since the company's listing date to the end of 2019, maintaining close to the IPO price of US\$0.88 amid moderate growth in the US economy. However, an unprecedented coronavirus outbreak and lower-than-forecast earnings and distribution have led to a sharp decline in the share price since late February 2020. The ongoing Covid-19 situation will have a major negative impact on the US hotel market, leading to a deteriorating outlook for hotel revenue performance in 2020. In 2021, however, the US hotel market is predicted to experience a recovery, with hotel RevPAR forecasted to grow by 63.1%. Nonetheless, the virus situation remains uncertain and its impact is yet to be fully determined.

## Recommendation

ARA H-Trust has a low P/B of 0.39x, based on the current price of US\$0.335. This implies that the company is trading at a 61% discount to NAV, which could indicate that it is potentially undervalued. This is reinforced by a peer comparison which shows that ARA H-Trust's P/B ratio is lower than the peer average P/B of 0.54x. Adopting the peer average P/B as a benchmark, we estimate a target price of US\$0.470 per stapled security if ARA H-Trust's P/B were to adjust to the benchmark of 0.54x. Our target price implies a 40.3% upside from the current price of US\$0.335. Our target price also implies a 46% discount to NAV which we think is appropriate to account for the difficulty of realising the full value of the hotel properties if they are to be sold. We also note that ARA H-Trust is attractive in terms of dividend yield compared to the peer average. We recommend a buy and our target price is US\$0.470.

## Key Financials

	Revenue (US\$ million)	EPS (US cents)	P/E (x)	P/B (x)	DPS (US cents)	Dividend yield (%)	NAV per stapled security (US\$)	Gearing ratio (%)
Full year, ended Dec 31								
2019 actual*	115.0	1.89	11.82	0.39	4.21	18.8	0.87	32.1
2020 forecast	96.2	1.58	21.20	-	3.52	10.5	-	-
2021 forecast	157.7	2.59	12.93	-	5.77	17.2	-	-

Figures have been rounded

\*8-month period from 9 May 2019 (listing date) to 31 Dec 2019

\*Estimated P/E based on annualised earnings of 2.84 US cents in 2019 and current price of US\$0.335

\*Estimated P/B based on NAV per stapled security as at 31 Dec 19 and current price of US\$0.335

\*Estimated dividend yield based on annualised DPS of 6.31 US cents in 2019 and current price of US\$0.335. Reported annualised yield of 7.4% based on IPO price of US\$0.88

Source: ARA H-Trust, FPA Financial

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## OVERVIEW OF HISTORY AND BUSINESS

ARA US Hospitality Trust (“ARA H-Trust”) is a Singapore-listed hospitality stapled security comprising ARA US Hospitality Property Trust (“ARA H-REIT”) and ARA US Hospitality Management Trust (“ARA H-BT”). Listed on the Mainboard of the Singapore Exchange on 9 May 2019, ARA H-Trust is the first pure-play United States (“US”) upscale select-service hospitality trust listed in Asia. ARA H-Trust is established with the principal investment strategy of investing in a portfolio of income-producing real estate which is used primarily for hospitality and/or hospitality-related purposes, located in the US.

### (I) Overview of ARA H-Trust’s portfolio

ARA H-Trust’s initial portfolio comprised 38 upscale Hyatt-branded select-service hotels across 21 states in the US with a total of 4,950 rooms. The 38 hotels included 27 Hyatt Place and 11 Hyatt House. Following the completed acquisition of three Marriot-branded select-service hotels on 17 January 2020, ARA H-Trust’s portfolio currently comprises 41 upscale select-service hotels across 22 states in the US with a total of 5,340 rooms. The 41 hotels include 27 Hyatt Place, 11 Hyatt House, 1 AC Hotels by Marriot, 1 Residence Inn by Marriot and 1 Courtyard by Marriot. **Exhibit 1** below shows the list of hotel properties and the individual hotels’ geographical positioning, number of rooms and valuation.

#### Exhibit 1: ARA H-Trust’s portfolio - geographical positioning, number of rooms and valuation

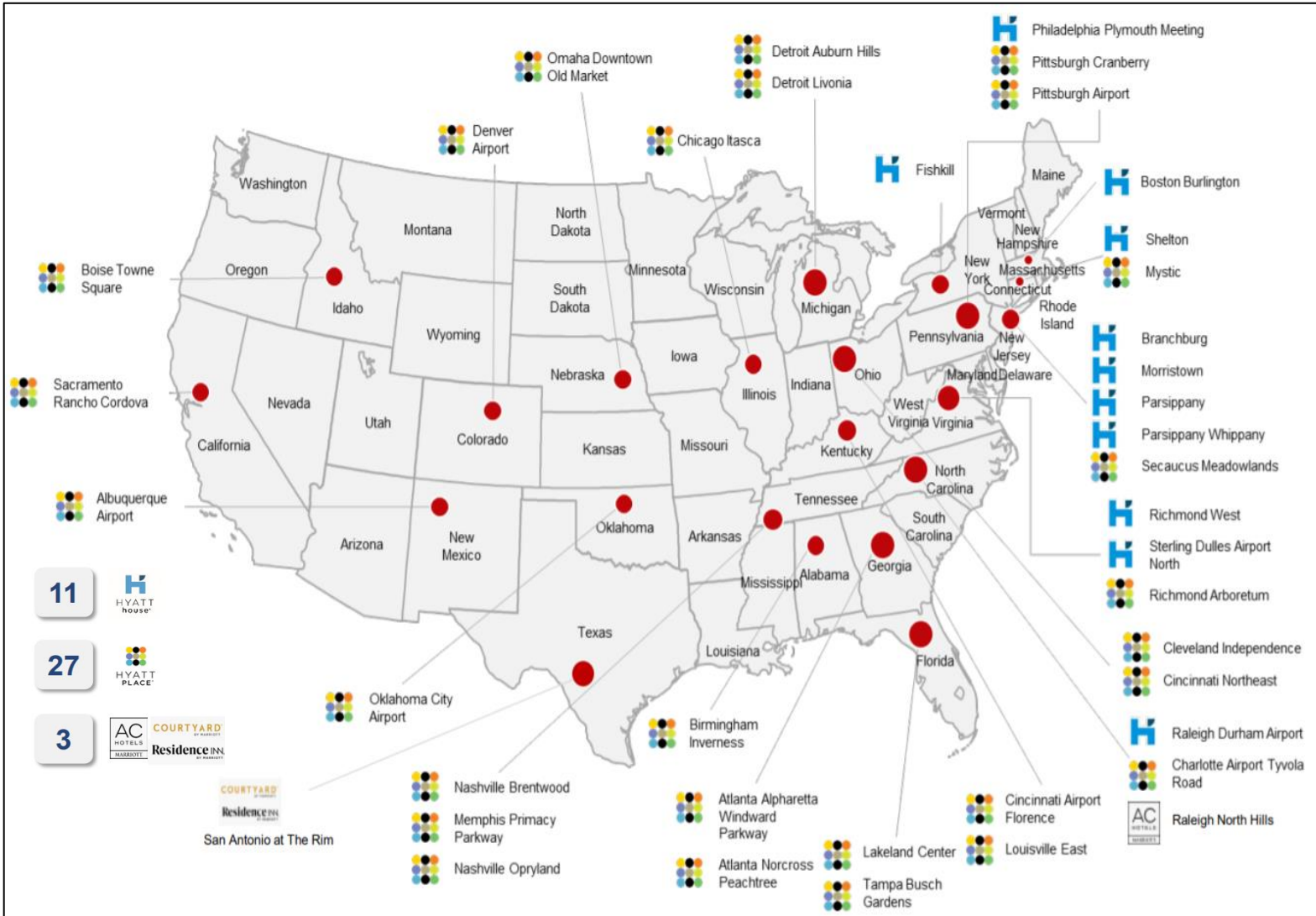
S/N	State	Brand	City	Name of Hotel	Number of Rooms	Valuation (US\$ million) <sup>(1)</sup>
1	Alabama	Hyatt Place	Birmingham	Hyatt Place Birmingham Inverness	126	9.6
2	California	Hyatt Place	Sacramento	Hyatt Place Sacramento Rancho Cordova	127	23.8
3	Colorado	Hyatt Place	Aurora	Hyatt Place Denver Airport	126	17.3
4	Connecticut	Hyatt Place	Mystic	Hyatt Place Mystic	79	11.0
5	Florida	Hyatt Place	Lakeland	Hyatt Place Lakeland Center	127	15.3
6	Florida	Hyatt Place	Tampa	Hyatt Place Tampa Busch Garden	126	16.6
7	Georgia	Hyatt Place	Alpharetta	Hyatt Place Atlanta Alpharetta Windward Parkway	127	21.9
8	Georgia	Hyatt Place	Norcross	Hyatt Place Atlanta Norcross Peachtree	126	12.9
9	Idaho	Hyatt Place	Boise	Hyatt Place Boise Towne Square	127	16.9
10	Illinois	Hyatt Place	Itasca	Hyatt Place Chicago Itasca	126	9.8
11	Kentucky	Hyatt Place	Florence	Hyatt Place Cincinnati Airport Florence	126	22.1
12	Kentucky	Hyatt Place	Louisville	Hyatt Place Louisville East	121	16.1
13	Michigan	Hyatt Place	Auburn Hills	Hyatt Place Detroit Auburn Hills	127	12.3
14	Michigan	Hyatt Place	Livonia	Hyatt Place Detroit Livonia	127	15.2
15	Nebraska	Hyatt Place	Omaha	Hyatt Place Omaha Downtown Old Market	159	28.9
16	New Mexico	Hyatt Place	Albuquerque	Hyatt Place Albuquerque Airport	127	14.5
17	New Jersey	Hyatt Place	Secaucus	Hyatt Place Secaucus Meadowlands	159	24.2
18	North Carolina	Hyatt Place	Charlotte	Hyatt Place Charlotte Airport Tyvola Road	127	19.2
19	Ohio	Hyatt Place	Independence	Hyatt Place Cleveland Independence	127	10.1
20	Ohio	Hyatt Place	Mason	Hyatt Place Cincinnati Northeast	127	10.1
21	Oklahoma	Hyatt Place	Oklahoma City	Hyatt Place Oklahoma City Airport	126	11.5
22	Pennsylvania	Hyatt Place	Cranberry Township	Hyatt Place Pittsburgh Cranberry	127	8.8
23	Pennsylvania	Hyatt Place	Pittsburgh	Hyatt Place Pittsburgh Airport	127	8.5
24	Tennessee	Hyatt Place	Brentwood	Hyatt Place Nashville Brentwood	124	17.0
25	Tennessee	Hyatt Place	Memphis	Hyatt Place Memphis Primacy Parkway	126	13.0
26	Tennessee	Hyatt Place	Nashville	Hyatt Place Nashville Opryland	123	23.4
27	Virginia	Hyatt Place	Richmond	Hyatt Place Richmond Arboretum	127	15.0
<b>Sub-total</b>	-	-	-	-	<b>3,424</b>	<b>425.0</b>
28	Connecticut	Hyatt House	Shelton	Hyatt House Shelton	127	17.8
29	Massachusetts	Hyatt House	Burlington	Hyatt House Boston Burlington	150	36.0
30	New Jersey	Hyatt House	Branchburg	Hyatt House Branchburg	139	24.7
31	New Jersey	Hyatt House	Morristown	Hyatt House Morristown	132	35.1
32	New Jersey	Hyatt House	Parsippany	Hyatt House Parsippany	140	23.9
33	New Jersey	Hyatt House	Whippany	Hyatt House Parsippany Whippany	135	29.0
34	New York	Hyatt House	Fishkill	Hyatt House Fishkill	135	20.2
35	North Carolina	Hyatt House	Morrisville	Hyatt House Raleigh Durham Airport	141	22.2
36	Pennsylvania	Hyatt House	East Norriton	Hyatt House Philadelphia Plymouth Meeting	131	14.7
37	Virginia	Hyatt House	Henrico	Hyatt House Richmond West	134	34.1
38	Virginia	Hyatt House	Sterling	Hyatt House Sterling Dulles Airport North	162	22.0
<b>Sub-total</b>	-	-	-	-	<b>1,526</b>	<b>279.7</b>
39	North Carolina	AC by Marriott	Raleigh	AC by Marriott Raleigh North Hills	135	45.1
40	Texas	Courtyard by Marriott	San Antonio	Courtyard San Antonio at The Rim	124	22.9
41	Texas	Residence Inn by Marriott	San Antonio	Residence Inn San Antonio at The Rim	131	20.9
<b>Sub-total</b>	-	-	-	-	<b>390</b>	<b>88.9</b>
<b>Grand total</b>	-	-	-	-	<b>5,340</b>	<b>793.6</b>

(1) Based on independent valuation conducted by HVS Consulting and Valuation Services as at 31 December 2019 for Hyatt hotels and 1 December 2019 for Marriott hotels

Source: Compiled using information from ARA H-Trust

The map in **Exhibit 2** below shows the location of the hotels in ARA H-Trust's portfolio.

**Exhibit 2: Map showing the location of hotels in ARA H-Trust's portfolio**



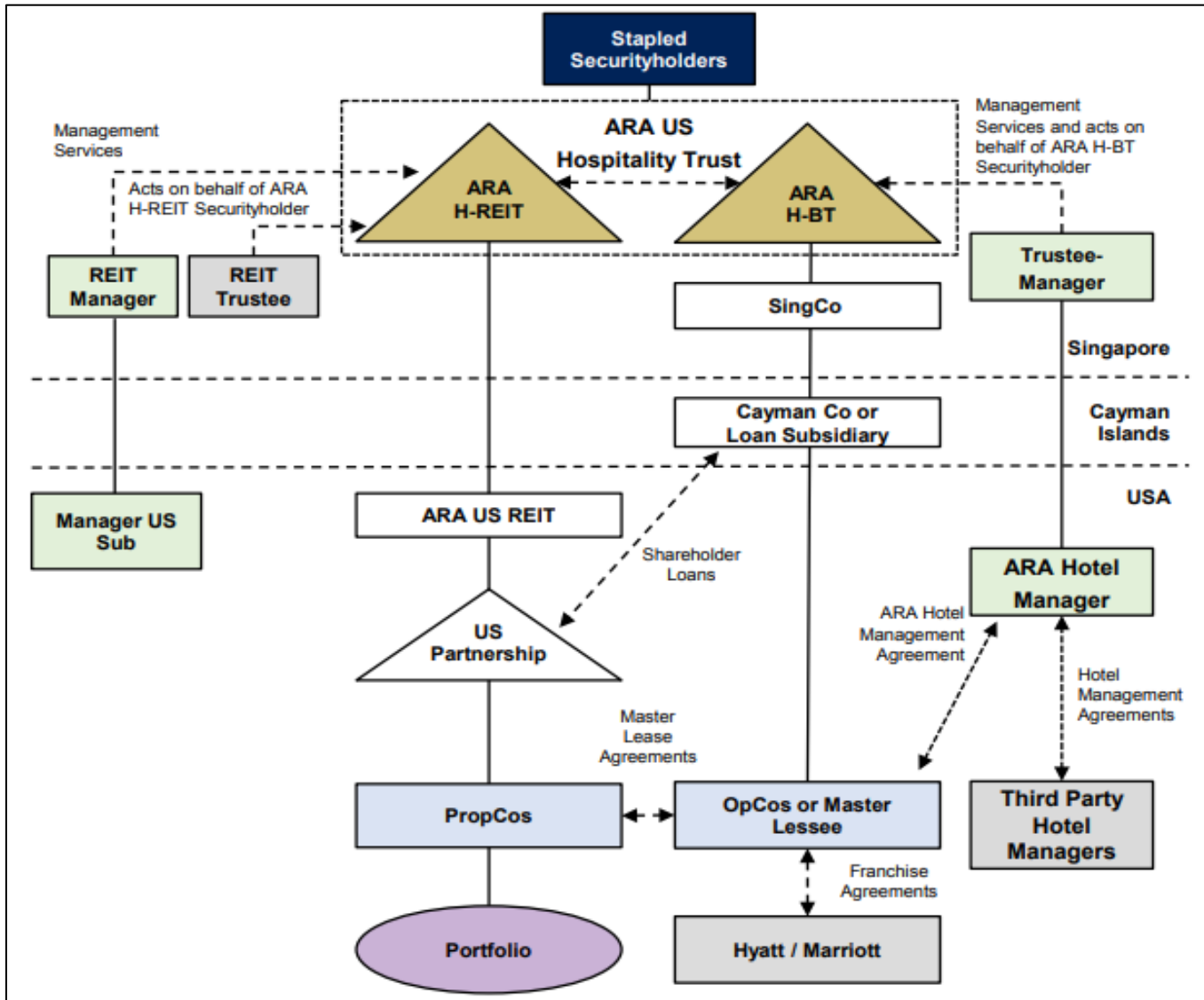
Source: ARA H-Trust, FY2019 Financial Results Presentation

**(II) Structure of ARA H-Trust**

This sub-section provides an overview of ARA H-Trust's structure. We also highlight the roles of the individual entities within the trust structure and the relationship between these entities.

The following diagram in **Exhibit 3** illustrates the relationship among ARA H-REIT, ARA H-BT, the Managers and the Stapled Securityholders.

**Exhibit 3: Trust structure**



Source: ARA H-Trust, FY2019 Financial Results Presentation

With reference to **Exhibit 3**, we will describe the role of the individual entities within the structure and highlight the relationship between these entities.

#### The Managers

As mentioned on page 3, ARA H-Trust is a stapled security comprising ARA H-REIT and ARA H-BT.

The company is externally managed by ARA Trust Management (USH) Pte Ltd, the REIT Manager of ARA H-REIT, and ARA Business Trust Management (USH) Pte Ltd, the Trustee-Manager of ARA H-BT, collectively known as the Managers. The Managers were incorporated in Singapore on 29 August 2018. They are wholly-owned subsidiaries of ARA Asset Management Limited (ARA or ARA Group), a leading APAC real assets fund manager with a global reach.

#### The REIT Trustee

The trustee of ARA H-REIT is DBS Trustee Limited (“REIT Trustee”), a Singapore-incorporated company that is licensed as a trust company under the Trust Companies Act.

#### ARA US REIT and the US Partnership

ARA H-REIT has ownership of all the common stock of ARA US REIT. ARA US REIT in turn holds the 38 hotel properties (“Properties”) in ARA H-Trust’s initial portfolio indirectly through the US Partnership, which is treated as a partnership for US federal income tax purposes, and is wholly-owned and controlled by ARA US REIT and its affiliates.

#### Manager US Sub

ARA USH Management, Inc, the Manager US Sub, is a wholly-owned subsidiary of the REIT Manager. The Manager US Sub had entered into an agreement with the REIT Manager and ARA US REIT, pursuant to which certain investment and asset management services for ARA US REIT and its subsidiaries will be provided.

#### SingCo and CaymanCo

ARA TRS Holding Pte Ltd (“SingCo”), a wholly-owned subsidiary of ARA H-BT, wholly owns CaymanCo, or the Loan Subsidiary. On 14 January 2019, CaymanCo acquired 99% of the issued and outstanding membership interests in ARA USH Chicago TRS, LLC (“Chicago TRS”) from the US Partnership. The remaining 1% interest was subsequently acquired on 17 April 2019. As CaymanCo is a wholly owned indirect subsidiary of ARA H-BT, the latter indirectly holds 100% of the equity interests of Chicago TRS as of 17 April 2019. In addition, CaymanCo had entered into a loan agreement on 17 April 2019 with the US Partnership to qualify for favourable tax treatment.

#### OpCo and PropCos

OpCo, or the Master Lessee, is wholly owned by CaymanCo indirectly through Chicago TRS. It is responsible for leasing the Properties from PropCos, pursuant to two lease agreements entered by the two entities on 12 November 2014, with OpCo as the lessee and PropCos as the lessor. Pursuant to the lease agreements, PropCo will receive rental payments comprising of a fixed component and a variable component from OpCo. The terms of the lease agreements will be up till 31 December 2024. For the period from 9 May 2019 (Listing date) to 31 December 2019, the total rental payments amounted to US\$33.4 million.

### The ARA Hotel Manager and Third Party Hotel Manager

The ARA Hotel Manager, ARA US Hospitality Management, Inc, is a wholly-owned subsidiary of the Trustee-Manager. The ARA Hotel Manager was appointed by OpCo on 22 April 2019 to operate and manage, through Aimbridge Hospitality, LLC, the Third Party Hotel Manager, the hotel operations of ARA H-Trust's initial portfolio in the US pursuant to the ARA Hotel Management Agreement, which was entered into between the ARA Hotel Manager and OpCo on 22 April 2019. OpCo had entered into 38 Aimbridge Hotel Management Agreements with the Third Party Hotel Manager, on 30 November 2018, to manage the operation and management of ARA H-Trust's initial portfolio. The 38 Aimbridge Hotel Management Agreements were novated to the ARA Hotel Manager on 22 April 2019 through an assignment, assumption, and novation agreement.

The second Third Party Hotel Manager is Concord Hospitality, which is responsible for managing the 3 Marriott-branded hotels that were acquired on 17 January 2020.

### Hyatt

On 30 November 2018, Hyatt Place Franchising, LLC and Hyatt House Franchising LLC, collectively "Hyatt", OpCo, PropCo, and the US Partnership entered into an agreement for consent to transfer and amendment of franchise agreements and guarantees, which allowed OpCo to continue operating the Hotels under the "Hyatt Place" and "Hyatt House" trademark.

### **(III) The Sponsor**

The Sponsor of ARA H-Trust is ARA Real Estate Investors 23 Pte Ltd, a wholly-owned subsidiary of ARA Group. ARA Group is a premier global integrated real assets fund manager headquartered in Singapore. As at 31 December 2019, the gross assets managed by ARA Group and its associates was approximately S\$87 billion across more than 100 cities in 28 countries.

Apart from ARA H-Trust, ARA Group directly manages 5 listed REITs, of which 2 are SGX-listed (Suntec REIT and Cache Logistics Trust), and indirectly manages other listed REITs in Singapore, Malaysia, Japan and Australia through its associate companies. In addition, ARA Group and its associates have businesses in private real estate funds, country desks, infrastructure and real estate management services. ARA H-Trust stands to benefit from the backing of a reputable Sponsor like ARA Group that has a multi-business platform and global presence.

## INDUSTRY OVERVIEW

In this section, we will review the overall performance of the US hotel industry in 2019 and the outlook for 2020 and 2021.

### Performance of the US Hotel Industry in 2019

In 2019, the US hotel industry registered growth in most performance indicators. According to STR, supply and demand rose at the same pace of growth at 2.0%. The average daily rate (ADR) rose by 1.0% to US\$131.21 while occupancy remained unchanged at 66.1%. As a result, revenue per available room (RevPAR) increased by 0.9% to US\$86.76. We have summarised the data in **Exhibit 4**.

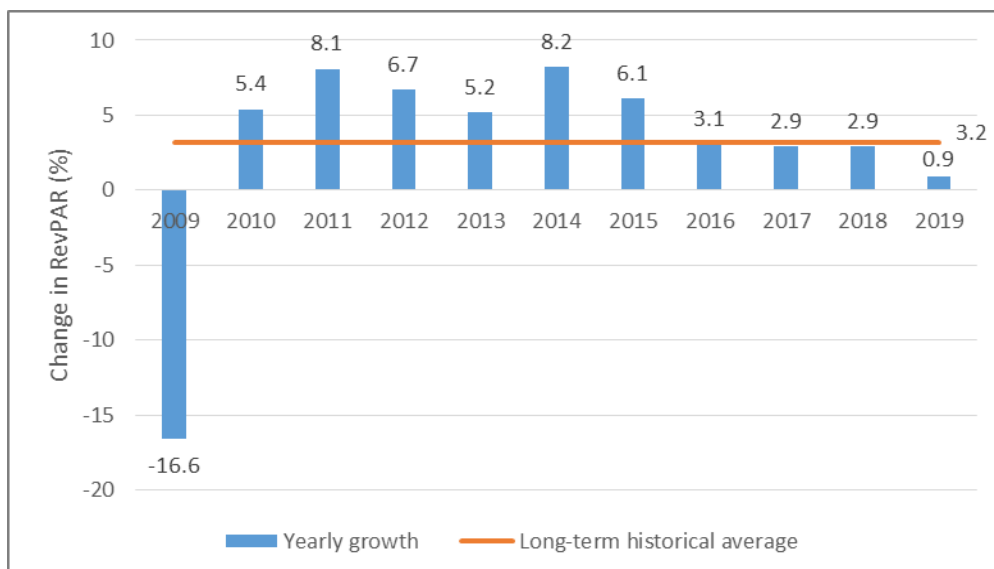
### Exhibit 4: US Hotel Performance Indicators in 2019, % Change vs 2018

Indicators	Actual 2019	
	US\$	% Change
Supply	-	2.0%
Demand	-	2.0%
Occupancy	66.1%	0.0%
ADR	131.21	1.0%
RevPAR	86.76	0.9%

Source: STR

However, RevPAR growth was the lowest since 2010 and below the long-term historical average (10-year period from 2009 to 2018) of 3.2%, as shown in **Exhibit 5**. According to STR, the weaker RevPAR growth was attributed to a slower pace of increase in ADR (1.0%) compared to the rate of inflation (US CPI inflation rate in 2019 was 2.3% as reported by the Bureau of Labour Statistics), thus revenue growth had not kept up with rising costs.

### Exhibit 5: RevPAR growth for the US Hotel Industry



Source: Compiled using data from STR



Outlook for the US Hotel Industry in 2020 and 2021

According to an initial 2020 forecast by STR and Tourism Economics (“TE”) released on 28 January 2020, the US hotel industry is projected to experience zero growth in RevPAR. Supply, demand and ADR are projected to increase in 2020 and 2021, but at a slower pace of growth than 2019. Occupancy is expected to decrease marginally in 2020 and 2021. RevPAR is projected to show zero growth in 2020 but expected to recover and record a 0.5% growth in 2021.

However, since then the coronavirus pandemic has further escalated. This is expected to have a major negative impact on the US hotel industry. According to a forecast revision by STR and TE, demand is projected to fall by 51.2%. This will exert a downward pressure on room rates. Occupancy and ADR are projected to fall by 42.6% and 13.9% respectively. As a result, STR and TE are projecting a 50.6% decline in RevPAR in 2020. In 2021, however, the hotel market is predicted to recover. Occupancy and ADR are projected to increase by 57.3% and 3.7% respectively, pushing up RevPAR by 63.1% to US\$69.86.

We have summarised the forecast data by STR and TE in **Exhibit 6**.

**Exhibit 6: Forecasts of US Hotel Performance Indicators in 2020 and 2021**

Indicators	Actual 2019		2020 forecast				2021 forecast			
		% Change	Initial		Revised		Initial		Revised	
				% Change <sup>(1)</sup>		% Change <sup>(1)</sup>		% Change <sup>(2)</sup>		% Change <sup>(3)</sup>
Supply	-	2.0%	-	1.9%	-	-14.9%	-	1.9%	-	15.6%
Demand	-	2.0%	-	1.6%	-	-51.2%	-	1.7%	-	81.8%
Occupancy	66.1%	0.0%	65.9%	-0.3%	37.9%	-42.6%	65.8%	-0.1%	59.7%	57.3%
ADR (US\$)	131.21	1.0%	131.63	0.3%	112.91	-13.9%	132.47	0.6%	117.05	3.7%
RevPAR (US\$)	86.76	0.9%	86.73	0.0%	42.86	-50.6%	87.18	0.5%	69.86	63.1%

*Figures have been rounded*

*(1) Compared to actual 2019 figures*

*(2) Compared to initial 2020 forecast figures*

*(3) Compared to revised 2020 forecast figures*

*Source: STR, Tourism Economics*

## FINANCIAL ANALYSIS

In this section, we will review ARA H-Trust's financial fundamentals in terms of profitability and financial leverage. We will also provide our financial projections for revenue, earnings per stapled security ("EPS") and dividends per stapled security ("DPS").

### (I) Profitability analysis

We will review ARA H-Trust's profitability through several metrics like the gross operating profit ("GOP") margin, adjusted funds from operation ("AFFO") margin and net profit margin. Given the absence of historical data for comparison (ARA H-Trust has been listed for less than a year), we will draw comparison with a close competitor in the US hotel market, Apple Hospitality REIT ("Apple REIT").

Apple REIT is a US-listed hospitality REIT that owns upscale, rooms-focused hotel properties in US. The company's portfolio consists of 231 hotels with more than 29,500 rooms, spanning across 34 US states. The portfolio comprises Marriott, Hilton and Hyatt-branded hotels. We thus note that there are many similarities across Apple REIT's and ARA H-Trust's portfolios – US-based; upscale, select-service hotels; same hotel brands. We do note that Apple REIT has been established since 2007 and is significantly larger than ARA H-Trust in terms of market capitalisation. Nonetheless, given the similarities across both company's portfolio, we think that it would be appropriate to use Apple REIT as a benchmark comparison for ARA H-Trust.

We noted that on a like-for-like basis, comparing between full-year results for both companies, ARA H-Trust recorded lower profitability margins for GOP, FFO and net profit, as shown in **Exhibit 7**. In particular, the largest variance was observed in the AFFO margin, with a 8.2 percentage points difference. In this regard, ARA H-Trust is seemingly less profitable compared to Apple REIT. However, we think that the results from the comparison are not too surprising, given that Apple REIT is much larger in market size. Also, Apple REIT has a stronger industry presence since it has been established for a longer period of time.

We are of the view that ARA H-Trust's profitability has held up relatively well against Apple REIT. We noted from ARA H-Trust that select-service hotels are increasingly favoured by hotel brands and developers due to superior demand and return profile. Thus, we see favourable growth conditions for ARA H-Trust's hotel properties which will potentially boost profitability as the company grows and develops a stronger presence in the US hotel market. Furthermore, the cost-effective nature of select-service hotels also helps to lower operational costs and increase profitability.

### Exhibit 7: Profitability metrics comparison

US\$ million	ARA H-Trust		Apple Hospitality REIT	Variance
	[a] 9 May 19 to 31 Dec 19	[b] Annualised	[c] Year ended 31 Dec 19	[b] vs [c] % points
Total revenue	115.0	172.5	1266.6	-
Gross operating profit (GOP)	43.1	64.7	542.2	-
GOP margin	37.5%	37.5%	42.8%	5.3
Adjusted funds from operations/Distributable income (AFFO)	23.9	35.9	365.9	-
AFFO margin	20.8%	20.8%	28.9%	8.1
Net profit	10.7	16.1	171.9	-
Net profit margin	9.3%	9.3%	13.6%	4.3

Source: Respective company data

**(II) Financial leverage analysis**

We analysed ARA H-Trust's financial leverage by comparing its gearing ratio, as typically computed for Singapore REITs ("S-REITs") by total debt over total assets, to its peers. The reported gearing ratios for ARA H-Trust and its peers are summarized in **Exhibit 8**.

We noted that ARA H-Trust's gearing ratio of 32.1% is relatively lower than SGX-listed hospitality REITs like Far East Hospitality Trust, CDL Hospitality Trust and Frasers Hospitality Trust, as shown in **Exhibit 8**. This implies that ARA H-Trust is less leveraged compared to its SGX-listed peers which provides more room for debt financing, given a maximum gearing limit of 45% for S-REITs.

**Exhibit 8: Financial leverage comparison**

Company	As at 31 Dec 19		
	Total assets (US\$ million)	Total debt (US\$ million)	Gearing (%)
ARA US Hospitality Trust	758.6	243.7	32.1
<b>Peers:</b>			
Apple Hospitality REIT <sup>(1)</sup>	4,942.4	1,320.4	26.7
Far East Hospitality Trust <sup>(2)</sup>	2,699.5	994.4	39.2
CDL Hospitality Trust <sup>(2) (3)</sup>	3,061.1	1,068.0	35.4
Frasers Hospitality Trust <sup>(2) (4)</sup>	2,462.3	870.0	35.5

*Gearing computation based on total debt over total assets. Company adjustments to the computation are annotated.*

<sup>(1)</sup> *Gearing based on analyst estimates*

<sup>(2)</sup> *Company reports in SGD currency*

<sup>(3)</sup> *For gearing computation, total assets excludes the effect of FRS 116/SFRS(I) Leases (adopted wef 1 Jan 2019)*

<sup>(4)</sup> *Impact of FRS116 Leases (adopted wef 1 Oct 19) has been excluded for the purpose of gearing computation*

*Source: Respective company data*

Given the gearing ratio of 32.1%, ARA H-Trust reported a debt headroom of US\$175 million as at 31 December 2019, based on the gearing limit of 45%. If ARA H-Trust were to take up a cash debt financing equal to the amount of debt headroom, it would generate a cash per stapled security of US\$0.308, based on 567.34 million stapled securities. This is close to the current price per stapled security of US\$0.335.

### (III) Financial projections

In this section, we will present our projections for revenue, EPS and DPS.

#### (a) Revenue projection

The methodology that we have adopted in our revenue projection is to estimate ARA H-Trust's room revenue in 2020 based on STR's RevPAR projection for the US hotel market in 2020.

For the period from 9 May 2019 (listing date) to 31 December 2019, ARA H-Trust's portfolio of 38 Hyatt Place and Hyatt House hotels comprised a total 4,950 rooms, as shown in **Exhibit 9** on the next page. Based on the room weightings and the RevPAR for the individual brands, the weighted RevPAR for ARA H-Trust's hotels was reported to be US\$94.

Upon the completed acquisition of the 3 Marriot-brand hotels on 17 January 2020, ARA H-Trust's portfolio has since expanded to a total of 5,340 rooms. The updated room weightings for the various brands are computed as shown in **Exhibit 9**. Hereon, we will assume no property acquisition or sale in 2020 and 2021, and thus the room weightings will remain the same.

As referenced on page 9, STR has projected a 50.6% decline in RevPAR for the US hotel market in 2020. We utilised STR's projection as a proxy for the expected changes in RevPAR for ARA H-Trust's hotels. Thus, we derived the 2020 RevPAR forecast for each of the hotel brands by discounting their 2019 RevPAR by 50.6% as shown in **Exhibit 9**. As for 2021, STR has projected a RevPAR growth of 63.1%. We thus derived the 2021 RevPAR forecasts by applying a 63.1% growth on our 2020 RevPAR forecasts.

The computations for the expected weighted RevPAR for each brand in 2020 and 2021 are as follows:

- 2020 Weighted RevPAR (Hyatt House) = 28.6% x US\$56 = US\$16
- 2020 Weighted RevPAR (Hyatt Place) = 64.1% x US\$42 = US\$27
- 2020 Weighted RevPAR (AC by Marriot) = 2.5% x US\$69 = US\$2
- 2020 Weighted RevPAR (Courtyard by Marriot) = 2.3% x US\$51 = US\$1
- 2020 Weighted RevPAR (Residence Inn by Marriot) = 2.5% x US\$49 = US\$1
  
- 2021 Weighted RevPAR (Hyatt House) = 28.6% x US\$91 = US\$26
- 2021 Weighted RevPAR (Hyatt Place) = 64.1% x US\$68 = US\$44
- 2021 Weighted RevPAR (AC by Marriot) = 2.5% x US\$113 = US\$3
- 2021 Weighted RevPAR (Courtyard by Marriot) = 2.3% x US\$84 = US\$2
- 2021 Weighted RevPAR (Residence Inn by Marriot) = 2.5% x US\$81 = US\$2

Taking the sum of all the brands' weighted RevPAR for the respective years would yield a total weighted RevPAR of US\$47 in 2020 and US\$77 in 2021, as shown in **Exhibit 9**.

**Exhibit 9: Weighted RevPAR projection for 2020 and 2021**

Hotel brand	Total rooms			Room weighting			RevPAR (US\$)			Weighted RevPAR (US\$)		
	2019	2020	2021	2019	2020	2021	2019 actual <sup>(1)</sup>	2020 forecast	2021 forecast	2019 actual	2020 forecast	2021 forecast
Hyatt House	1,526	1,526	1,526	30.8%	28.6%	28.6%	113	56	91	35	16	26
Hyatt Place	3,424	3,424	3,424	69.2%	64.1%	64.1%	85	42	68	59	27	44
AC by Marriot	-	135	135	-	2.5%	2.5%	140	69	113	-	2	3
Courtyard by Marriot	-	124	124	-	2.3%	2.3%	104	51	84	-	1	2
Residence Inn by Marriot	-	131	131	-	2.5%	2.5%	100	49	81	-	1	2
<b>Total</b>	<b>4,950</b>	<b>5,340</b>	<b>5,340</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	-	-	-	94	47	77

For 2019: period from 9 May 19 (listing date) to 31 Dec 19

For 2020 and 2021: full year period

(1) Based on period from listing date to 31 Dec 19 for Hyatt-brand hotels and year-end results for Marriot-brand hotels

Source: ARA H-Trust, FPA Financial

With reference to **Exhibit 10**, we estimated the total room revenue for 2020 and 2021 to be US\$91.6 million and US\$150.1 million, respectively. The computation are as follows:

- Total room revenue in 2020 = 5,340 rooms x US\$47 x 365 days = US\$91.6 million
- Total room revenue in 2021 = 5,340 rooms x US\$77 x 365 days = US\$150.1 million

**Exhibit 10: Room revenue projection for 2020 and 2021**

Year	Total rooms	Weighted RevPAR (US\$)	No. of days	Total room revenue (US\$ million)
2019 actual	4,950	94	236 <sup>(1)</sup>	109.5
2020 forecast	5,340	47	365 <sup>(2)</sup>	91.6
2021 forecast	5,340	77	365 <sup>(2)</sup>	150.1

(1) Approximate figure

(2) Assumed no. of days in a year

Source: ARA H-Trust, FPA Financial

Based on ARA H-Trust's latest financial statements, we noted that room revenue made up 95.2% of total revenue in 2019, with the remaining 4.8% contributed by revenue generated by other operations, as shown in **Exhibit 11**. We would assume this proportioning to be the same in 2020 and 2021. We then estimated a total revenue of US\$96.2 million and US\$157.7 million in 2020 and 2021, respectively. The computations are as follows:

- Total revenue in 2020 =  $[100/95.2] \times \text{US\$}91.6 \text{ million} = \text{US\$}96.2 \text{ million}$
- Total revenue in 2020 =  $[100/95.2] \times \text{US\$}150.1 \text{ million} = \text{US\$}157.7 \text{ million}$

**Exhibit 11: Total revenue projection for 2020 and 2021**

Revenue breakdown	2019 actual	2020 forecast		2021 forecast	
	US\$ million	US\$ million	% of total	US\$ million	% of total
Room revenue	109.5	91.6	95.2%	150.1	95.2%
Other operating revenue	5.5	4.6	4.8%	7.6	4.8%
Total revenue	115.0	96.2	100.0%	157.7	100.0%

*For 2019: period from 9 May 19 (listing date) to 31 Dec 19*

*For 2020 and 2021: full year period*

*Source: ARA H-Trust, FPA Financial*

**(b) EPS and DPS projection**

For the period from 9 May 2019 to 31 December 2019, ARA H-Trust reported an EPS of 1.89 US cents. The annualised EPS for the whole of 2019 is estimated to be 2.84 US cents. For the same period from 9 May 2019 to 31 December 2019, ARA H-Trust announced a DPS of 4.206 US cents, with an ex-date and payment date on 27 February 2020 and 27 March 2020, respectively. The 4.206 US cents payout was achieved through tax-exempt income (2.677 US cents) and capital (1.529 US cents). The annualised DPS for the whole of 2019 is estimated to be 6.31 US cents.

In our EPS and DPS projections, we assumed the revenue growth for 2020 as a proxy for the growth in earnings and distributions in the same period. We first annualised the 8-month period revenue of US\$115.0 million to yield an estimated total revenue for the whole of 2019 at US\$172.5 million, as shown in **Exhibit 12**. As mentioned on page 14, we projected a total revenue of US\$96.2 million in 2020 and US\$157.7 million in 2021. Our projections would imply a 44.2% yoy decline in total revenue in 2020 and a 63.9% yoy growth in total revenue in 2021. We then assumed these changes in total revenue for the respective years to yield the EPS and DPS for each year, as shown in **Exhibit 12**. The computations are as follows:

- Projected EPS in 2020 =  $0.558 \times 2.84$  US cents = 1.58 US cents
- Projected DPS in 2020 =  $0.558 \times 6.31$  US cents = 3.52 US cents
  
- Projected EPS in 2021 =  $1.639 \times 1.58$  US cents = 2.59 US cents
- Projected DPS in 2021 =  $1.639 \times 3.52$  US cents = 5.77 US cents

**Exhibit 12: EPS and DPS projection for 2020**

	2019 actual		2020 forecast		2021 forecast	
	8-month period <sup>(1)</sup>	Annualised	US\$ million	% change yoy <sup>(2)</sup>	US\$ million	% change yoy <sup>(3)</sup>
	US\$ million	US\$ million				
Total revenue	115.0	172.5	96.2	-44.2%	157.7	63.9%
EPS (US cents)	1.89	2.84	1.58	-44.2%	2.59	63.9%
DPS (US cents)	4.206	6.31	3.52	-44.2%	5.77	63.9%

(1) Period from 9 May 19 (listing date) to 31 Dec 19

(2) As compared to annualised 2019 figures

(3) As compared to 2020 forecast

Source: ARA H-Trust, FPA Financial

We recognise that the US government recently announced a US\$2 trillion stimulus package to provide economic relief in response to the coronavirus pandemic. The hotel industry, which is one of the sectors hardest hit by the Covid-19 outbreak, is expected to receive aid to weather the impact. However, we are still unable to fully determine the impact of the coronavirus and the effectiveness of the relief measures to deal it. Thus, we would assume our revenue and EPS projections to be appropriate as of now.

**VALUATION ANALYSIS**

We will present our valuation analysis in three segments. We will first provide a balance sheet analysis, followed by a peer comparison analysis, and lastly an income capitalisation approach.

**(I) Balance sheet analysis**

We performed a balance sheet analysis for ARA H-Trust to determine how the company is trading on the market relative to its book value. In other words, we reviewed how much of a premium or discount to book value has ARA H-Trust been trading on the market. This would provide a better understanding of whether ARA H-Trust's share could be potentially undervalued or overvalued.

As at 8 April 2020, ARA H-Trust traded at US\$0.335 per share on the market, with a total market value of US\$190.1 million, based on a total of 567.34 million stapled securities as at 31 December 2019, as shown in **Exhibit 13**. Based on ARA H-Trust's balance sheet as at 31 December 2019, ARA H-Trust reported total assets of US\$758.6 million and total liabilities of US\$265.4 million, implying a net asset value (NAV) of US\$493.2 million. This would yield a NAV or book value per stapled security of US\$0.87, based on 567.34 million stapled securities. Comparison with the current share price of US\$0.335 would indicate that ARA H-Trust's share is trading at a 61% discount to book value. Thus, it is trading at a low P/B ratio of 0.39x. As such, we think that ARA H-Trust could potentially be undervalued.

**Exhibit 13: Balance sheet analysis**

	US\$'000
Share price (US\$), as at 8 Apr 20	0.335
Stapled securities ('000)	567,342
Market capitalisation	190,060
<b>Balance Sheet</b>	<b>31-Dec-19</b>
Non-current assets	706,488
Current assets	52,123
Total assets	758,611
Less:	
Non-current liabilities	(253,714)
Current liabilities	(11,681)
Total liabilities	(265,395)
Net asset value/Book value	493,216
Issued stapled securities ('000)	567,342
NAV per stapled security (US\$)	0.87
Price-to-book (x)	0.39

Source: ARA H-Trust



**(II) Peer comparison analysis**

We also performed a peer comparison analysis to analyse how the company is performing relative to its peers. We selected Apple REIT, CDL Hospitality Trusts (“CDL”), Frasers Hospitality Trust (“Frasers”) and Far East Hospitality Trust (“Far East”). We selected the peers by taking into account how similar their portfolio types and location are to those of ARA H-Trust. As discussed earlier on page 10, Apple REIT is a close competitor of ARA H-Trust as both are hospitality REITs with hotels that are solely based in the US. CDL, Frasers and Far East are SGX-listed REITs that have hospitality assets which span across several countries worldwide.

We first noted that ARA H-Trust’s price-to-earnings (P/E) ratio of 11.82x is lower than the peer average of 12.25x, as shown in **Exhibit 14**. Apple REIT’s P/E ratio is close to that of ARA H-Trust, while the other three SGX-listed REITs have P/E ratios that are less similar. A possible explanation could be due to portfolio location. ARA H-Trust’s and Apple REIT’s hotels are solely based in the US while the portfolios of CDL, Frasers and Far East span across several countries such as Singapore and Australia. The lower P/E ratio for ARA H-Trust could be due to weaker earnings expectations induced by relatively lower confidence on the stability of the US economy amid the uncertainties over the US-China trade war and geopolitical tensions between the US and Middle East. In addition, the absence of country diversification for ARA H-Trust’s portfolio induces higher risks which potentially depresses the earnings expectations. We also note that ARA H-Trust’s P/B ratio of 0.39x is lower than the peer average of 0.54x (**Exhibit 14**), which is supportive of our earlier conclusion in the balance sheet analysis that ARA H-Trust is seemingly undervalued. Additionally, we noted that ARA H-Trust’s dividend yield of 18.83% appears to be very attractive. We still see that ARA H-Trust’s yield is relatively attractive in comparison to the peer average of 11.32%, as shown in **Exhibit 14**.

**Exhibit 14: Peer comparison**

Company	Portfolio type	SGX ticker	Share price (US\$) as at 8 Apr 20	Market capitalisation (US\$ million)	EPS (US cents)	P/E (x)	NAV (US\$)	P/B (x)	DPS (US cents)	Dividend yield (%)
ARA US Hospitality Trust <sup>(1)</sup>	Hospitality	XZL/ARAUS.SI	0.335	190.06	2.835	11.82	0.87	0.39	6.31	18.83
<b>Peers:</b>										
Apple Hospitality REIT <sup>(2)</sup>	Hospitality	APLE:US	9.050	2025.93	77.00	11.75	14.70	0.62	120.00	13.26
CDL Hospitality Trusts <sup>(3)</sup>	Hospitality	J85/CDLT.SI	0.795	967.22	9.27	8.58	1.52	0.52	9.02	11.35
Frasers Hospitality Trust <sup>(3)</sup>	Hospitality	ACV/FRHO.SI	0.395	754.32	2.52	15.67	0.72	0.55	4.49	11.36
Far East Hospitality Trust <sup>(3)</sup>	Hospitality	Q5T/FAEH.SI	0.410	799.88	3.15	13.02	0.86	0.48	3.81	9.29
<b>Average</b>	-	-	-	-	-	<b>12.25</b>	-	<b>0.54</b>	-	<b>11.32</b>

Companies own properties in the US and report in USD, unless otherwise specified. Companies are SGX-listed, unless otherwise specified

P/E are based on total EPS in 2019 and current price as at 8 Apr 20, unless otherwise specified

P/B are based on NAV per share or stapled security as at 31 Dec 19 and current price as at 8 Apr 20, unless otherwise specified

Dividend yield are based on total DPS in 2019 and current price as at 8 Apr 20, unless otherwise specified

<sup>(1)</sup> Listed for less than a year. P/E and dividend yield are based on estimated annualised EPS and DPS in 2019

<sup>(2)</sup> Listed in the US

<sup>(3)</sup> Portfolio not based in the US and company reports in SGD currency

Source: SGX, Bloomberg, Individual company data

Following the peer comparison analysis, we adopted a valuation method using the P/B peer average as a benchmark. Specifically, we estimated a valuation for ARA H-Trust if its P/B were to adjust to the peer average of 0.54x. We estimated a target price of US\$0.470 per stapled security, which would generate a potential upside of 40.3% from the current price of US\$0.335. The computations are as follows:

- Target price = [P/B peer average] x [reported NAV per stapled security] = 0.54 x US\$0.87 = US\$0.470
- Potential upside from current price = [US\$0.470/US\$0.335] – 1 = 40.3%

Our estimated target price of US\$0.470 implies a 46% discount to the reported NAV per stapled security of US\$0.87. We think that the discount is appropriate to account for the uncertainties in realising the full value of the hotels if they are placed for sale. Firstly, we are still unable to fully determine the impact of Covid-19 at this juncture. This implies that the impact on ARA H-Trust's hotels' revenue and NOI cannot be appropriately estimated. Secondly, in the event of a property sale, the selling price of the hotels would vary across different buyers. In this period of uncertainty due to the coronavirus, buyers are likely to bargain for a discount. The negotiation terms will vary across different buyers which would create variations in the final selling price of the hotels. Thus, we reiterate our view that it would be appropriate for the 46% discount to NAV to account for the difficulty in realising the full value of the hotel properties.

**(III) Income capitalisation approach**

We have also considered an income capitalisation approach to estimate the market value of the individual hotels in ARA H-Trust's portfolio, based on the income they generate. This would be done by estimating the market value for the individual hotels owned by ARA H-Trust by dividing each property's net operating income ("NOI") by a capitalisation rate ("cap rate").

In our estimation of value of the hotels, we have referred to the latest CBRE North America Cap Rate Survey for H2 2019 to obtain a suitable cap rate, as shown in **Exhibit 15**. According to CBRE, US cap rates were stable in 2019 and are expected to remain stable in 2020, despite the uncertainty created by the coronavirus. This is attributed to high domestic and foreign investor demand for US real estate assets. Thus, we think that it would be appropriate to utilize the H2 2019 hotel cap rates in our estimates. With reference to **Exhibit 15**, we note that CBRE segmented H2 2019 cap rates for select-service hotels into the CBD and suburban area at 8.0% and 8.5% respectively.

**Exhibit 15: US hotel industry capitalisation rates**

Property type	Segment	Class	Cap rate	
			H2 2019 (%)	H1 2019 (%)
Hotel	CBD	All	7.99	8.01
		Luxury	7.01	7.05
		Full service	7.76	7.75
		Select service	8.00	8.04
		Economy	9.22	9.20
	Suburban	All	8.55	8.55
		Luxury	7.61	7.61
		Full service	8.28	8.26
		Select service	8.50	8.53
		Economy	9.76	9.74

Source: CBRE, North America Cap Rate Survey 2H 2019

ARA H-Trust's portfolio comprises select-service hotels in urban and suburban areas. Thus, we sorted the hotels into the CBD and suburban segments, as shown in **Exhibit 16** on the next page. Generally, hotels that are situated in the downtown area of the respective hotels' cities were classified as CBD, while those not within the city downtown were classified as suburban. The CBD and suburban segment cap rates from CBRE were then used as a proxy for the cap rate for the individual hotels.

**Exhibit 16: Hotel segmentation and cap rates**

Brand	Name of Hotel	State	City	Zoning <sup>(1)</sup>	Segment	Cap rate
Hyatt Place	Hyatt Place Birmingham Inverness	Alabama	Birmingham	B1-Neighborhood Business District	Suburban	8.50%
Hyatt Place	Hyatt Place Sacramento Rancho Cordova	California	Sacramento	OPMU-Office Professional Mixed Use	Suburban	8.50%
Hyatt Place	Hyatt Place Denver Airport	Colorado	Aurora	Business commercial	Suburban	8.50%
Hyatt Place	Hyatt Place Mystic	Connecticut	Mystic	TC-80 Tourist Commercial	Suburban	8.50%
Hyatt Place	Hyatt Place Lakeland Center	Florida	Lakeland	C-6-Commercial	CBD	8.00%
Hyatt Place	Hyatt Place Tampa Busch Garden	Florida	Tampa	PD-Planned Development	Suburban	8.50%
Hyatt Place	Hyatt Place Atlanta Alpharetta Windward Parkway	Georgia	Alpharetta	OI-Office Institutional	CBD	8.00%
Hyatt Place	Hyatt Place Atlanta Norcross Peachtree	Georgia	Norcross	M1-Light Industrial	Suburban	8.50%
Hyatt Place	Hyatt Place Boise Towne Square	Idaho	Boise	R-3D-Multi-Family Residential	Suburban	8.50%
Hyatt Place	Hyatt Place Chicago Itasca	Illinois	Itasca	B-3-Service Business	Suburban	8.50%
Hyatt Place	Hyatt Place Cincinnati Airport Florence	Kentucky	Florence	C-2-Commercial Two	Suburban	8.50%
Hyatt Place	Hyatt Place Louisville East	Kentucky	Louisville	OR3 SMC-Office Residential, Suburban Marketplace Corridor	Suburban	8.50%
Hyatt Place	Hyatt Place Detroit Auburn Hills	Michigan	Auburn Hills	B2-General Business District	CBD	8.00%
Hyatt Place	Hyatt Place Detroit Livonia	Michigan	Livonia	C2-General Business	Suburban	8.50%
Hyatt Place	Hyatt Place Omaha Downtown Old Market	Nebraska	Omaha	CBD-ACI-1(PL)-Central Business District-Area of Civic Importance	CBD	8.00%
Hyatt Place	Hyatt Place Albuquerque Airport	New Mexico	Albuquerque	IP-Industrial Park Zone	Suburban	8.50%
Hyatt Place	Hyatt Place Secaucus Meadowlands	New Jersey	Secaucus	RC-Regional Commercial	Suburban	8.50%
Hyatt Place	Hyatt Place Charlotte Airport Tyvola Road	North Carolina	Charlotte	L-1-Light Industrial	Suburban	8.50%
Hyatt Place	Hyatt Place Cleveland Independence	Ohio	Independence	U-5-HR-MU-Office Building HI-Rise Mixed Use	Suburban	8.50%
Hyatt Place	Hyatt Place Cincinnati Northeast	Ohio	Mason	General Business PUD	Suburban	8.50%
Hyatt Place	Hyatt Place Oklahoma City Airport	Oklahoma	Oklahoma City	I-1,SRODD-Light Industrial District Scenic River Overlay Design District	Suburban	8.50%
Hyatt Place	Hyatt Place Pittsburgh Cranberry	Pennsylvania	Cranberry Township	SU-1-Special Use	Suburban	8.50%
Hyatt Place	Hyatt Place Pittsburgh Airport	Pennsylvania	Pittsburgh	C-5-Research and Development	Suburban	8.50%
Hyatt Place	Hyatt Place Nashville Brentwood	Tennessee	Brentwood	CL,OV-COM-Commercial Limited Commercial PUD Overlay	Suburban	8.50%
Hyatt Place	Hyatt Place Memphis Primacy Parkway	Tennessee	Memphis	OG-Office General	Suburban	8.50%
Hyatt Place	Hyatt Place Nashville Opryland	Tennessee	Nashville	CA-OV-COM-Commercial Attraction, Commercial PUD Overlay	Suburban	8.50%
Hyatt Place	Hyatt Place Richmond Arboretum	Virginia	Richmond	O-2-Corporate Office District	Suburban	8.50%
Hyatt House	Hyatt House Shelton	Connecticut	Shelton	PDD-Planned Development District	Suburban	8.50%
Hyatt House	Hyatt House Boston Burlington	Massachusetts	Burlington	IG-General Industrial	Suburban	8.50%
Hyatt House	Hyatt House Branchburg	New Jersey	Branchburg	I-IP-Industrial	Suburban	8.50%
Hyatt House	Hyatt House Morristown	New Jersey	Morristown	IP-Industries, Offices & Labs	Suburban	8.50%
Hyatt House	Hyatt House Parsippany	New Jersey	Parsippany	COD-Corporate Office District	Suburban	8.50%
Hyatt House	Hyatt House Parsippany Whippany	New Jersey	Whippany	OBRL-Office Building & Labs	CBD	8.00%
Hyatt House	Hyatt House Fishkill	New York	Fishkill	PSC-Planned Shopping Centre	Suburban	8.50%
Hyatt House	Hyatt House Raleigh Durham Airport	North Carolina	Morrisville	RAC-Regional Activity Centre	Suburban	8.50%
Hyatt House	Hyatt House Philadelphia Plymouth Meeting	Pennsylvania	East Norriton	EC-Executive Campus	Suburban	8.50%
Hyatt House	Hyatt House Richmond West	Virginia	Henrico	B-3C-Commercial	Suburban	8.50%
Hyatt House	Hyatt House Sterling Dulles Airport North	Virginia	Sterling	PDIP-Commercial/Industrial	Suburban	8.50%
AC by Marriott	AC by Marriott Raleigh North Hills	North Carolina	Raleigh	-	Suburban	8.50%
Courtyard by Marriott	Courtyard San Antonio at The Rim	Texas	San Antonio	-	Suburban	8.50%
Residence Inn by Marriott	Residence Inn San Antonio at The Rim	Texas	San Antonio	-	Suburban	8.50%

(1) Zoning based on HVS valuation report as in ARA H-Trust's prospectus

Source: ARA H-Trust, CBRE, FPA Financial

For the individual hotels' NOI, we had referred to projected 2021/22 NOI figures by HVS as stated in ARA H-Trust's prospectus. However, we noted that the projections exclude the impact of the coronavirus, and thus would not be the most appropriate figures for our estimations. To consider the impact of the coronavirus on the hotels' income, we referred to a CBRE study which provided a relationship between GOP, hotel occupancy and room rates as follows:

➤  $\text{GOP change} = -0.01 + 1.9 \times \text{occupancy change} + 1.8 \times \text{ADR change}$

With the above relationship, we were able to estimate the impact of the coronavirus on the hotels' income through its effect on occupancy and ADR. Thus, we estimated the expected change in the hotels' GOP by inputting the revised occupancy and ADR forecast by STR and TE (on page 9) into the above formula. We then adopted the expected change in GOP as a proxy for the change in NOI across ARA H-Trust's portfolio to derive an adjusted NOI for the individual hotels. The estimated results are summarized in **Exhibit 17**.

### Exhibit 17: 2020 adjusted NOI estimates for ARA H-Trust's portfolio

Brand	Name of Hotel	NOI (US\$ million) <sup>(1)</sup>	2020 STR projections		Expected GOP change <sup>(2)</sup>	Adjusted NOI (US\$ million)
			Occupancy change	ADR change		
Hyatt House	Hyatt House Shelton	1.31	-42.6%	-13.9%	-107.0%	-0.09
Hyatt House	Hyatt House Boston Burlington	3.06	-42.6%	-13.9%	-107.0%	-0.21
Hyatt House	Hyatt House Branchburg	2.19	-42.6%	-13.9%	-107.0%	-0.15
Hyatt House	Hyatt House Morristown	2.88	-42.6%	-13.9%	-107.0%	-0.20
Hyatt House	Hyatt House Parsippany	2.19	-42.6%	-13.9%	-107.0%	-0.15
Hyatt House	Hyatt House Parsippany Whippany	2.17	-42.6%	-13.9%	-107.0%	-0.15
Hyatt House	Hyatt House Fishkill	1.60	-42.6%	-13.9%	-107.0%	-0.11
Hyatt House	Hyatt House Raleigh Durham Airport	1.73	-42.6%	-13.9%	-107.0%	-0.12
Hyatt House	Hyatt House Philadelphia Plymouth Meeting	1.10	-42.6%	-13.9%	-107.0%	-0.08
Hyatt House	Hyatt House Richmond West	2.69	-42.6%	-13.9%	-107.0%	-0.19
Hyatt House	Hyatt House Sterling Dulles Airport North	1.63	-42.6%	-13.9%	-107.0%	-0.11
Hyatt Place	Hyatt Place Birmingham Inverness	0.89	-42.6%	-13.9%	-107.0%	-0.06
Hyatt Place	Hyatt Place Sacramento Rancho Cordova	1.95	-42.6%	-13.9%	-107.0%	-0.14
Hyatt Place	Hyatt Place Denver Airport	1.68	-42.6%	-13.9%	-107.0%	-0.12
Hyatt Place	Hyatt Place Mystic	1.01	-42.6%	-13.9%	-107.0%	-0.07
Hyatt Place	Hyatt Place Lakeland Center	1.43	-42.6%	-13.9%	-107.0%	-0.10
Hyatt Place	Hyatt Place Tampa Busch Garden	1.36	-42.6%	-13.9%	-107.0%	-0.09
Hyatt Place	Hyatt Place Atlanta Alpharetta Windward Parkway	1.94	-42.6%	-13.9%	-107.0%	-0.14
Hyatt Place	Hyatt Place Atlanta Norcross Peachtree	1.17	-42.6%	-13.9%	-107.0%	-0.08
Hyatt Place	Hyatt Place Boise Towne Square	1.53	-42.6%	-13.9%	-107.0%	-0.11
Hyatt Place	Hyatt Place Chicago Itasca	1.00	-42.6%	-13.9%	-107.0%	-0.07
Hyatt Place	Hyatt Place Cincinnati Airport Florence	1.73	-42.6%	-13.9%	-107.0%	-0.12
Hyatt Place	Hyatt Place Louisville East	1.24	-42.6%	-13.9%	-107.0%	-0.09
Hyatt Place	Hyatt Place Detroit Auburn Hills	1.33	-42.6%	-13.9%	-107.0%	-0.09
Hyatt Place	Hyatt Place Detroit Livonia	1.57	-42.6%	-13.9%	-107.0%	-0.11
Hyatt Place	Hyatt Place Omaha Downtown Old Market	2.37	-42.6%	-13.9%	-107.0%	-0.16
Hyatt Place	Hyatt Place Secaucus Meadowlands	2.14	-42.6%	-13.9%	-107.0%	-0.15
Hyatt Place	Hyatt Place Albuquerque Airport	1.11	-42.6%	-13.9%	-107.0%	-0.08
Hyatt Place	Hyatt Place Charlotte Airport Tyvola Road	1.75	-42.6%	-13.9%	-107.0%	-0.12
Hyatt Place	Hyatt Place Cleveland Independence	1.04	-42.6%	-13.9%	-107.0%	-0.07
Hyatt Place	Hyatt Place Cincinnati Northeast	0.94	-42.6%	-13.9%	-107.0%	-0.07
Hyatt Place	Hyatt Place Oklahoma City Airport	1.09	-42.6%	-13.9%	-107.0%	-0.08
Hyatt Place	Hyatt Place Pittsburgh Cranberry	1.09	-42.6%	-13.9%	-107.0%	-0.08
Hyatt Place	Hyatt Place Pittsburgh Airport	0.77	-42.6%	-13.9%	-107.0%	-0.05
Hyatt Place	Hyatt Place Nashville Brentwood	1.74	-42.6%	-13.9%	-107.0%	-0.12
Hyatt Place	Hyatt Place Memphis Primacy Parkway	1.24	-42.6%	-13.9%	-107.0%	-0.09
Hyatt Place	Hyatt Place Nashville Opryland	2.19	-42.6%	-13.9%	-107.0%	-0.15
Hyatt Place	Hyatt Place Richmond Arboretum	1.24	-42.6%	-13.9%	-107.0%	-0.09
AC by Marriott	AC by Marriott Raleigh North Hills	- <sup>(3)</sup>	-42.6%	-13.9%	-107.0%	-
Courtyard by Marriott	Courtyard San Antonio at The Rim	- <sup>(3)</sup>	-42.6%	-13.9%	-107.0%	-
Residence Inn by Marriott	Residence Inn San Antonio at The Rim	- <sup>(3)</sup>	-42.6%	-13.9%	-107.0%	-

(1) Based on projected NOI figures for 2021/22 by HVS as in ARA H-Trust's prospectus

(2)  $\text{GOP change} = -0.01 + 1.9 \times \text{occupancy change} + 1.8 \times \text{ADR change}$

(3) NOI information unavailable for the 3 newly acquired Marriot hotels

Source: ARA H-Trust, FPA Financial

As shown in the last column of **Exhibit 17**, the NOI of the individual hotels have turned negative for the year 2020. This is unsurprising given the adverse Covid-19 situation. Given the Covid-19 situation, we reconsidered our initial consideration of using an income capitalisation approach to value ARA H-Trust's portfolio and do not think this approach would be appropriate. This is because we think that it would not be fair to determine the market value of ARA H-Trust's hotels based on estimated NOI that is skewed by an anomalous event like the coronavirus outbreak. We do not expect such drastic changes in the hotels' NOI in normal circumstances and hotel incomes are not expected to remain at the negative levels that we have estimated in **Exhibit 17**. Thus, we are of the view that it may not be appropriate to estimate the value of the hotels via the income capitalisation approach.

## SWOT AND COMPETITIVE ANALYSIS

In this section, we undertake a SWOT analysis in **Exhibit 18** to evaluate the various components of the analysis thus far.

### Exhibit 18: SWOT analysis

## SWOT analysis

### Strengths

- Strong backing by a reputable Sponsor
- Well-branded portfolio
- Cost-effective portfolio

### Weaknesses

- Absence of country diversification in portfolio

### Opportunities

- Recovery of the US hotel market

### Threats

- Recession risk
- Natural disasters

### (I) Strengths

As highlighted on page 7, ARA H-Trust's Sponsor is ARA Real Estate Investors 23 Pte Ltd, an indirect wholly-owned subsidiary of ARA Group, a leading APAC real assets fund manager with global reach. ARA H-Trust stands to benefit from the backing of a reputable Sponsor like ARA Group that has a multi-business platform and global presence.

In addition to strong backing from its Sponsor, ARA H-Trust is also backed up by its Hyatt and Marriot- branded portfolio. Hyatt and Marriot International are world-renowned brands and among the largest hotel chains in the world. The branding profile of ARA H-Trust's portfolio helps to drive higher demand for lodging due to favourable brand presence. This in turn drives stronger hotel revenue performance.

Further, ARA H-Trust's portfolio consists of select-service hotels which is beneficial in terms of operational cost. Select-service hotels are primarily room-focused and offer lesser amenities and services compared to full-service hotels. Thus, they are more cost-effective as lower costs are incurred for the operation and maintenance of hotel amenities. Labour cost are expected to be kept lower with a limited range of services. Furthermore, lower operational costs allow select-service hotels the option to charge lower room rates which increase the affordability of their properties.

**(II) Weaknesses**

ARA H-Trust's portfolio spans across 22 US states which provides geographical diversification within the US. This will help to hedge against state-based downside risks within the US. A state-based natural disaster, for instance, will not impact ARA H-Trust as greatly due to its presence in other states, which would help to support overall business. However, as ARA H-Trust's hotel properties are solely based in the US, there is an absence of country diversification in the portfolio. This implies that there is no hedging against country-based downside risks. A US-based economic downturn, for instance, would leave ARA H-Trust with little room to manoeuvre due to the absence of overseas properties to compensate for the weaker performance in the US.

**(III) Opportunities**

As it stands, the outlook of the US hotel market, and in turn ARA H-Trust's revenue performance, is currently dictated by the impact and length of the coronavirus pandemic. Nonetheless, the hotel market is predicted to recover in late 2020, bringing about potential growth opportunities. Yet, this is not for certain as we are yet to be able to determine how long the pandemic would last.

**(IV) Threats**

With the ongoing battle against the coronavirus, the US economy has been severely impacted due to massive disruption in the flow of goods, services and people. There is an elevated risk of a recession which will further impact the US hotel industry. In addition, the US is also prone to natural disasters such as hurricanes which have previously caused major disruptions to the hotel market. We will further discuss these factors in our risk section.



## INVESTMENT RECOMMENDATION

From our valuation analysis, we noted that ARA H-Trust has a low P/B of 0.39x, based on the current price of US\$0.335. This implies that the company is trading at a 61% discount to NAV, which could indicate that it is potentially undervalued.

This is reinforced by a peer comparison with other hospitality REITs, as ARA H-Trust's P/B ratio is lower than the peer average P/B of 0.54x. Adopting the peer average P/B as a benchmark, we estimate a target price of US\$0.470 per stapled security if ARA H-Trust's P/B were to adjust to the benchmark of 0.54x. Our target price implies a 40.3% upside from the current price of US\$0.335. Our target price also implies a 46% discount to NAV which we think is appropriate to account for the difficulty of realising the full value of the hotel properties on sale. This is because the coronavirus impact on the hotels' NOI cannot yet be fully determined and the selling price of hotels will vary due to different negotiation terms. We also note that ARA H-Trust is attractive in terms of dividend yield compared to the peer average.

Nonetheless, we expect ARA H-Trust's financial performance to weaken in 2020 due to the coronavirus. The US hotel market is projected to experience declines in all hotel performance indicators. Hotel RevPAR is projected to fall by 50.6% in 2020, which would drag down hotel room revenue. In 2021, however, the US hotel market performance is predicted to improve, which would provide opportunities for ARA H-Trust to recover its fundamentals. This will, however, be based on the expectation that the coronavirus situation would be resolved.

Given all of the above consideration, we think that given the severe sell-down, a buy recommendation is warranted. Our estimated target price is US\$0.470. However, there are still risks to our target price which we will highlight in the risk section.

## RISKS TO THE TARGET PRICE

In this section, we highlight a few potential scenarios that may pose as risks to our target price.

### (I) Risk of a recession in US due to the Covid-19 outbreak

The direct impact of the coronavirus on the US hospitality sector has materialised as ARA H-Trust recently announced on 25 March 2020 that its portfolio has faced increasing booking cancellations and a reduced pace in new reservations. As a consequence, there has been a significant decline in room occupancies for the portfolio since mid-March 2020. ARA H-Trust expects this trend to continue in the weeks or months ahead.

On an indirect level, the risk of a recession in the US would negatively impact the hospitality sector, and in turn the performance of ARA H-Trust's hotels, through weaker consumer spending, which in part reduces the domestic demand for travel and accommodations. The Covid-19 outbreak has created a high potential likelihood of a recession in the US. The virus outbreak has rapidly escalated in the US, forcing the need for state lockdowns and the implementation of travel bans by the US government, which are drastic measures that will lead to significant negative impact on the economy. The US Federal Reserve has reacted to the deteriorating outlook by drastically lowering its federal funds rate, as well as introducing debt-buying programs to alleviate the impact on the economy. Fiscal stimulus has also been deployed as the US government announced a US\$2 trillion stimulus to deal with the economic fallout. Despite the monetary and fiscal stimulus, the potential of a recession in the US remains highly likely due to the serious economic impact that has already been inflicted on the economy. Furthermore, the economic fallout could be more severe as the Covid-19 situation is expected to be protracted.

### (II) Risk of natural disasters

ARA H-Trust reported that its portfolio had been hit by demand dislocations due to Hurricane Dorian in September 2019. Hurricane Dorian was a Category 5 Atlantic Hurricane that affected US states like Florida, Georgia, North and South Carolina and Virginia. During that period, ARA H-Trust's portfolio in these states made up approximately 25% of its total portfolio of 38 hotels. Thus, if there are unforeseen natural disasters in the months ahead, this will have a negative impact on the hotels' revenue.

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