

**HOTEL RESEARCH****ARA US Hospitality Trust (ARA H-Trust)**

SGX: XZL

Bloomberg: ARAUS:SP

ISIN Code: SGXC80011726

**RECOMMENDATION: BUY**

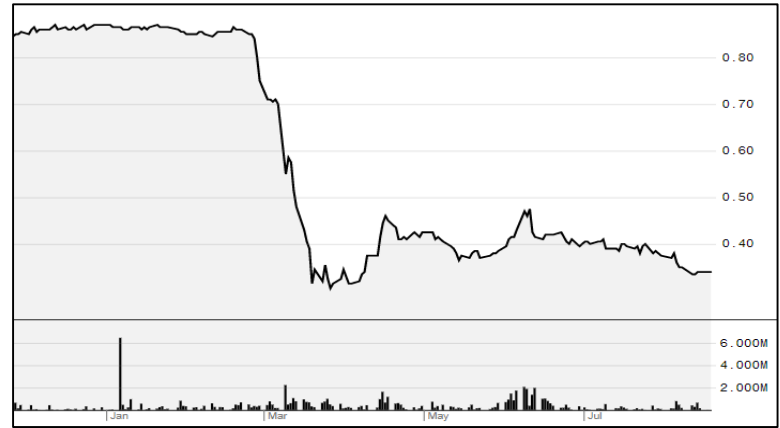
Current Share Price (as of 21 Aug 20): US\$0.330

Current Target Price: US\$0.493

Market Capitalisation: US\$187.22 million

Issued Stapled Securities: 567.34 million

52 Week Range: US\$0.280 - US\$0.895

**PRICE PERFORMANCE**

Source: Bloomberg

**COMPANY DESCRIPTION**

ARA H-Trust (The Group) is a Singapore-listed hospitality stapled group comprising ARA US Hospitality Property Trust (ARA H REIT) and ARA US Hospitality Management Trust (ARA H BT). The Group's portfolio comprises 41 Marriot and Hyatt-branded select-service hotels that span across 22 states in the US.

**SUMMARY**

Owing to the impact of COVID-19, ARA H-Trust's financial performance was severely impacted in 1H2020. Revenue registered US\$39.3 million in 1H2020, underperforming the Group's IPO forecasts by 58.4%. With the Group's efforts to reduce operating costs by temporary suspension and consolidation of hotel operations, a gross operating profit of US\$5.8 million was achieved. However, a net property loss of US\$2.0 million was incurred after deducting fixed costs. After accounting for non-operating expenses, an after-tax net loss of US\$22.2 million was incurred in 1H2020. As a result, a loss per stapled security of 3.91 US cents was reported for 1H2020. No distributable income was reported for 1H2020.

**RECOMMENDATION**

ARA H-Trust's share price hit a low closing price of US\$0.305 on March 26 but had then recovered on the back of improvements in the outlook for the US hotel market and overall economy. We note that it hit a recent high of US\$0.475 in June, surpassing our previous target price of US\$0.470. However, the share price began to decline in mid-June amid a resurgence of virus cases in the US. Nonetheless, we believe that there is further upside in ARA H-Trust's share price on the back of a stabilized virus situation since early August, as well as an improving outlook for the US hotel market and economy. Based on our valuation review, we estimate a current target price of US\$0.493 if ARA H-Trust's P/B were to readjust to an updated peer average P/B ratio of 0.64x. This current target price implies a 49.4% upside from the current share price of US\$0.330. We now maintain a buy recommendation and our current target price is US\$0.493.

**KEY FINANCIALS**

	Revenue (US\$ million)	EPS (US cents)	P/E (x)	DPS (US cents)	Dividend yield (%)	NAV per stapled security (US\$)	P/B (x)
Full year, ended Dec 31							
2019 actual*	115.0	1.89	11.64	4.21	19.1	0.87	0.38
2020 forecast**	93.1	(4.78)	n/m	-	-	0.77	0.43
2021 forecast	147.7	(1.45)	n/m	3.10	9.4	-	-

Figures have been rounded

n/m: not meaningful

\* 8-month period from 9 May 2019 (listing date) to 31 Dec 2019. P/E and dividend yield are based on annualised EPS and DPS figures.

\*\* NAV per stapled security as at 30 Jun 2020.

Source: ARA H-Trust, FPA Financial

Contributor: Glendon Hoon  
(+65 6323 1788)

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**FINANCIAL REVIEW FOR 1H2020****Financial performance**

Owing to the COVID-19 pandemic, ARA H-Trust's financial performance was significantly impacted in 1H2020. Gross revenue registered US\$39.3 million in 1H2020, underperforming the Group's IPO Prospectus forecast by 58.4%. The weaker revenue performance was attributed to a significant drop in hotel occupancies and temporary hotel closures in March-June. In mid-March, ARA H-Trust had temporarily closed 30 out of its 41 hotels as part of its cost-mitigation efforts. The closed hotels had gradually re-opened from April to July – 12 in April; 6 in May; 10 in June; 2 in July. As of 1 July, we note that all hotels have resumed operations. Operating expenses were 40.6% lower than forecast, given the temporary suspension & consolidation of hotel operations, and comprehensive cost & labor reductions. This resulted in a gross operating profit of US\$5.8 million for 1H2020, which is 84.7% lower than forecasted. However, a net property loss of US\$2.0 million was incurred in 1H2020 after accounting for US\$7.9 million in fixed costs which include hotel management fee and property taxes. Following further adjustments of US\$20.1 million in expenses relating to depreciation and amortization, Trustee-Manager's and REIT's management and trustee fees, net finance costs, and other trust expenses, together with taxation of US\$9,000, an after-tax net loss of US\$22.2 million was incurred. As a result, negative earnings per stapled security (EPS) of 3.91 US cents was reported, based on a weighted average number of issued stapled securities of 567.2 million. At the same, there would be no distribution income. The financial results are summarized in **Exhibit 1**.

**Exhibit 1: Financial results for 1H2020**

US\$ million	1H2020		
	Actual	Forecast	% change
Revenue	39.3	94.5	(58.4)
Gross operating profit	5.8	38.1	(84.7)
Net property income/(loss)	(2.0)	29.5	n/m
Net income/(loss) after tax	(22.2)	7.3	n/m
EPS (US cents)	(3.91)	n/a	n/a
Distributable income	-	19.7	(100.0)
DPS (US cents)	-	3.47	(100.0)

*n/m: not meaningful*

*n/a: not available*

Source: ARA H-Trust, FPA Financial

**Capital management**

ARA H-Trust reported total assets of US\$817.7 million as at 30 June 2020, compared with US\$758.6 million as at the end of 2019. This was due to the acquisition of the 3 new Marriot hotels in January 2020. We note that the Group's hotels were not revalued in 1H2020, and thus the reported total assets value do not reflect any asset revaluation. Total liabilities registered US\$381.2 million as at 30 June 2020, compared with US\$265.4 million as at the end of 2019. This resulted in net assets amounting to US\$436.5 million, and in turn a net asset value (NAV) per stapled security of US\$0.77 was reported as at the end of 1H2020, based on 567.3 million issued stapled securities. The balance sheet data are as summarized in **Exhibit 2**.

**Exhibit 2: Balance sheet data as 31 Dec 2019 and 30 June 2020**

	<u>As at 30 Jun 2020</u>	<u>As at 31 Dec 2019</u>
	US\$ million	US\$ million
Total assets	817.7	758.6
Total liabilities	381.2	265.4
Net assets	436.5	493.2
Issued stapled securities	567.3	567.0
NAV per stapled security (US\$)	0.77	0.87
Total debt	347.9	243.7
Gearing ratio (%)*	42.5%	32.1%

\*Refers to total debt over total assets

Source: ARA H-Trust, FPA Financial

As noted above, ARA H-Trust's total debt had increased over the half-year period to 30 June 2020. As at the end of 1H2020, the Group had drawn down on all unsecured loan and credit facilities amounting to US\$94.2 million and drawn down on US\$247.3 million of secured facilities. With the addition of lease liabilities of US\$7.2 million, due to the adoption of SFRS(I) 16 Leases from 1 January 2020, and netting out unamortised upfront debt-related costs of US\$828,000, the total debt outstanding amounted to US\$347.9 million, compared to US\$243.7 million as at the end of 2019. As a result, ARA H-Trust's aggregate leverage, or gearing ratio, registered at 42.5%.

Meanwhile, we note that ARA H-Trust secured a 12-month loan covenant waiver (April 2020-March 2021) from Singapore-based relationship banks, which would apply to the Group's leverage limit and interest coverage ratio. In contrast, we note from the Group that US peers under commercial mortgage-backed securities (CMBS) loans have not been able to receive any form of relief.

**PORTFOLIO PERFORMANCE REVIEW FOR 1H2020**

Overall performance was significantly impacted by the COVID-19 pandemic and the temporary closure of hotels in March-June. Overall portfolio occupancy registered 43.2% while revenue per available room (RevPAR) stood at US\$48, as shown in **Exhibit 3**. Specifically, occupancy and RevPAR for the Hyatt portfolio (38 hotels) registered 42.6% and US\$47 respectively, while that for the newly acquired Marriott portfolio (3 hotels) registered 52.5% and US\$71 respectively. Throughout 1H2020, we note that the performance by the Marriott portfolio has been more resilient compared to the Hyatt portfolio. We further note from the Group that the Marriott portfolio had outperformed the US upscale hotel segment consistently throughout 1H 2020.

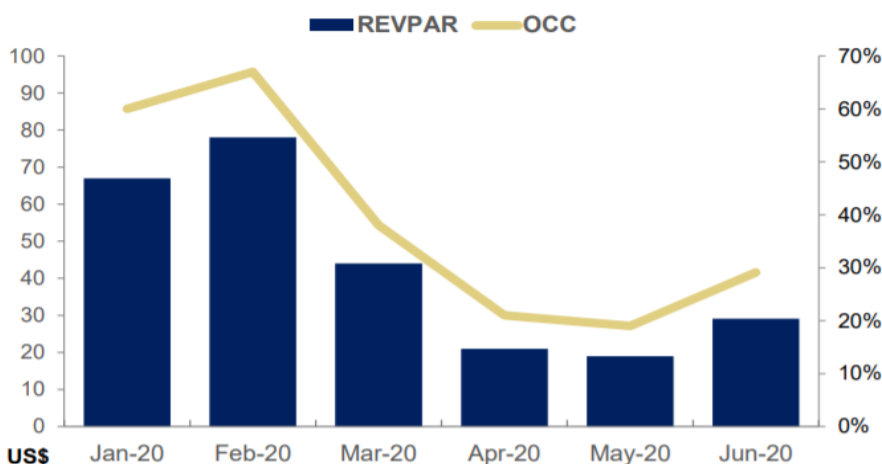
**Exhibit 3: Portfolio performance for 1H2020**

Hotel Brand	1Q 2020		2Q 2020		1H 2020	
	Occ	RevPAR	Occ <sup>1</sup>	RevPAR	Occ <sup>1</sup>	RevPAR
<b>Hyatt Portfolio</b>	54.1%	US\$61	23.7%	US\$23	<b>42.6%</b>	<b>US\$47</b>
Hyatt Place	52.8%	US\$56	22.2%	US\$20	42.3%	US\$44
Hyatt House	57.2%	US\$71	25.8%	US\$28	43.2%	US\$52
<b>Marriott Portfolio</b>	65.2%	US\$97	35.7%	US\$37	<b>52.5%</b>	<b>US\$71</b>
AC Hotels	64.0%	US\$119	34.4%	US\$43	55.1%	US\$96
Courtyard by Marriott	66.3%	US\$87	25.4%	US\$24	51.2%	US\$64
Residence Inn	65.3%	US\$83	40.5%	US\$41	51.7%	US\$60
<b>ARA H-TRUST</b>	<b>54.8%</b>	<b>US\$61</b>	<b>24.6%</b>	<b>US\$24</b>	<b>43.2%</b>	<b>US\$48</b>

Source: ARA H-Trust

On monthly performance, portfolio occupancy and RevPAR dropped sharply in March before hitting a trough in April-May. In June, however, both indicators showed signs of recovery amid a pickup in domestic travel demand. The data for ARA H-Trust’s monthly portfolio performance are summarized in **Exhibit 4**.

**Exhibit 4: Monthly portfolio performance for 1H2020**

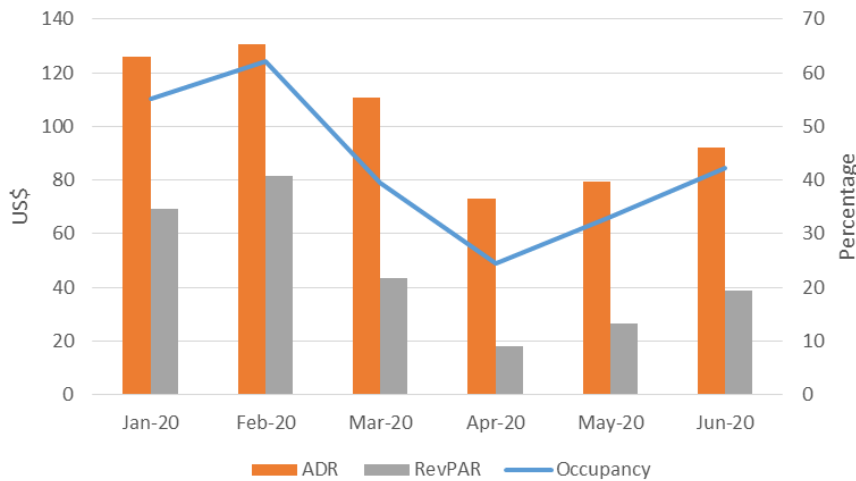


Source: ARA H-Trust

**PERFORMANCE OUTLOOK**

After a performance trough in April-May, ARA H-Trust’s portfolio occupancy and RevPAR have shown signs of improvement in June. We note that this is consistent with the overall performance trajectory of the US hotel market, as reflected by STR data that are summarized in **Exhibit 5**.

**Exhibit 5: US hotel performance for 1H2020**



Source: STR, FPA Financial

Meanwhile, we note that STR has slightly downgraded its forecasts for the US hotel market. According to the updated forecasts, US hotel RevPAR is expected to decline by 52.3% (previously: -50.6%) in 2020, followed by a 37.9% (previously: 63.1%) growth in 2021. The latest forecast data by STR are summarized in **Exhibit 6**.

**Exhibit 6: STR forecasts for the US hotel market**

Metric	2019 actual	2020 forecast		2021 forecast	
			y-o-y change		y-o-y change
Occupancy (%)	66.1	39.8	-39.7%	52.0	30.5%
ADR (US\$)	131.13	103.71	-20.9%	109.56	5.6%
RevPAR (US\$)	86.64	41.31	-52.3%	56.95	37.9%

Source: STR, FPA Financial

Similarly, CBRE expects a strong US hotel revenue recovery in 2021 and 2022, though recovery to pre-recession levels could only come by mid-2023. According to latest forecasts by CBRE, US hotel RevPAR is projected to decline by 51.9% in 2020, followed by a 48.4% and 29.3% growth in 2021 and 2022, respectively. The recovery will, however, be uneven across the hotel segments. Higher priced chain scale hotels are likely to lag in recovery timing due to their dependence on corporate, group and inbound international demand. In contrast, hotels in the lower-priced segments are likely to experience stronger demand and achieve higher occupancies. The latest forecast data by CBRE are summarized in **Exhibit 7**.

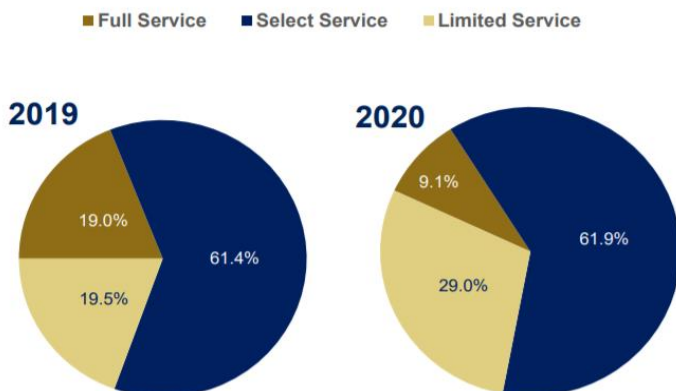
**Exhibit 7: CBRE baseline hotel performance forecast**

Year	Occ	ΔOcc	ADR	ΔADR	RevPAR	ΔRevPAR	ΔSupply	ΔDemand
2018	66.1%	0.4%	\$129.91	2.4%	\$85.90	2.9%	2.0%	2.4%
2019	66.1%	-0.1%	\$131.11	0.9%	\$86.64	0.9%	2.0%	2.0%
2020	41.0%	-38.0%	\$101.67	-22.5%	\$41.67	-51.9%	1.5%	-37.0%
2021	55.9%	36.3%	\$110.69	8.9%	\$61.83	48.4%	-1.1%	34.8%
2022	65.0%	16.4%	\$122.93	11.1%	\$79.95	29.3%	0.0%	16.4%
2023	66.6%	2.4%	\$130.47	6.1%	\$86.92	8.7%	0.5%	3.0%
2024	66.5%	-0.2%	\$135.63	4.0%	\$90.18	3.7%	0.9%	0.7%

Source: CBRE

Given the overall outlook for the US hotel market, we expect a stronger revenue performance from ARA H-Trust’s hotels in 2H2020. Further, we note three factors that could indicate that ARA H-Trust’s portfolio is better positioned to weather through the COVID-19 crisis. First, the Group’s select-service hotels pre-dominantly cater to the US domestic market, which provides insulation from weak inbound international demand due to imposed international travel restrictions. Second, we note from the Group that its hotels, which are situated in regional and non-gateway markets, are expected to benefit from work-from-home dynamics that have shifted hotel demand in favour of non-gateway markets. Third, we note from the Group that limited service and select-service hotels are leading the recovery trajectory in the US hotel market. In terms of demand, the select-service segment made up the largest proportion of the total US market in June 2020 at 61.9% compared with 61.4% a year ago, as shown in **Exhibit 8**.

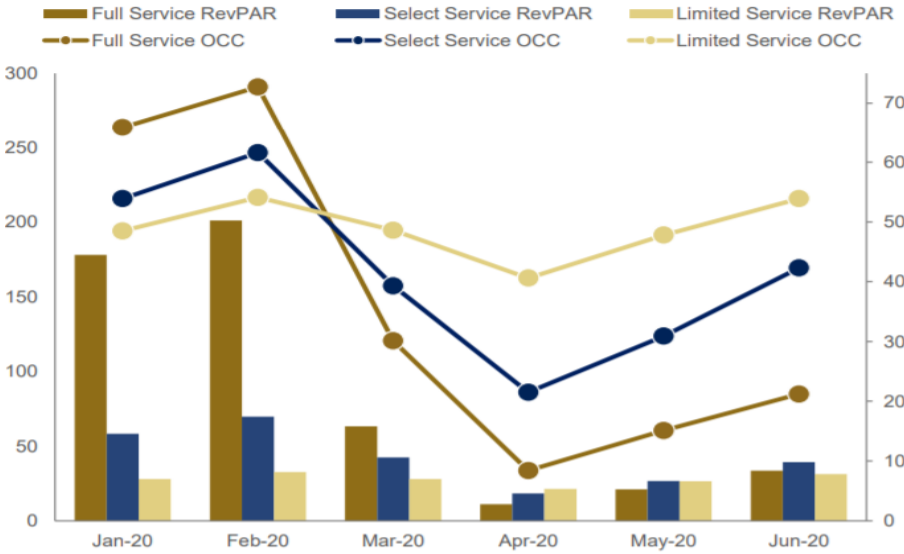
**Exhibit 8: US demand by segment comparison in June**



Source: ARA H-Trust

Further, the recovery in RevPAR for the select-service segment in April-June has been stronger compared to the full-service and limited service segments. Occupancy for the select service segment has also experienced a steeper rebound in over April-June as compared to the other segments. The performance trends for occupancy and RevPAR for the individual segments are summarized in **Exhibit 9**.

**Exhibit 9: US occupancy and RevPAR by segment (Jan-Jun 2020)**



Source: ARA H-Trust



## SHARE PRICE PERFORMANCE REVIEW

ARA H-Trust's share price held up relatively well from its listing date on 9 May 2019 till the start of 2020, maintaining close to the IPO price of US\$0.88. However, the share price declined sharply in late February, hitting a low closing price of US\$0.305 on March 26. The severe drop reflected concerns over the outlook of the US hotel market, and in turn the Group's financial performance, as hotel occupancies and RevPAR dipped to unprecedented low levels. However, since bottoming out on March 26, the share price began to recover and has hit a recent high of US\$0.475 on June 10, which is above the target price of US\$0.470 in our initiation report issued on April 8.

We believe that the share price recovery has been fueled by positive developments in the US hotel market, and US economy in general. With the lifting of lockdown measures and reopening of US states, there has been a return in domestic travel that has supported demand for hotel accommodation. This has helped to push up hotel occupancy levels, with STR data reflecting that US hotel occupancy rose to about 33% in May and 42% in June, after hitting a trough in April at about 25%. As a result, hotel RevPAR has also recovered and in turn overall hotel revenue performance has improved. At the same time, improvements in economic indicators have pointed to signs of an economic recovery in the US.

However, the share price began to decline in mid-June to early August and has since hovered between US\$0.33 to US\$0.35. This has been largely attributed to a resurgence of virus cases in several US states, including Florida, California and Texas which were the worst hit states. We note that the Group has 5 hotels across these 3 US states – 1 in California, 2 in Texas and 2 in Florida. Nonetheless, we note that the number of infection cases in the US have declined since early August, and the current virus situation in the US appears to have stabilized.

**FINANCIAL PROJECTION REVISION****Revenue projection for 2020**

In our projection for total revenue in 2020, we will first estimate total revenue for 2H2020. To do so, we will adopt 3 scenarios. The first would be a conservative baseline scenario where portfolio RevPAR remains unchanged in 2H2020 from 1H2020 at US\$48. We would also consider two other scenarios where portfolio RevPAR would be US\$50 and US\$52. Thus, we project room revenue to be US\$47.2 million if portfolio RevPAR were to be US\$48; US\$49.1 million if portfolio RevPAR were to be US\$50; and US\$51.1 million if portfolio RevPAR were to be US\$52, as shown in **Exhibit 10**.

**Exhibit 10: Projected room revenue for 2H2020**

Period	Total rooms*	Portfolio RevPAR (US\$)	No. of days**	Room revenue (US\$ million)
2H2020	5,340	48	184	47.2
2H2020	5,340	50	184	49.1
2H2020	5,340	52	184	51.1

\*All of the Group's hotels have resumed operations since 1 July

\*\*Total no. of days from Jul to Dec 2020

Source: FPA Financial

Meanwhile, we note from the Group that room revenue typically makes up about 93%-95% due to the room-focused nature of the Group's select-service hotels, which can be seen from the data in **Exhibit 11**. We would hereon assume room revenue to make up 95% of total revenue.

**Exhibit 11: Breakdown of the Group's total revenue**

Revenue breakdown	3Q 2019		4Q 2019		2019 actual*	
	US\$ million	% of total	US\$ million	% of total	US\$ million	% of total
Room revenue	44.7	95.5%	37.2	94.7%	109.5	95.2%
Other operating revenue	2.1	4.5%	2.1	5.3%	5.5	4.8%
Total revenue	46.8	100.0%	39.3	100.0%	115.0	100.0%

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

Source: ARA H-Trust, FPA Financial

Given the above, the projected total revenue for 2H2020 would be US\$49.7 million for Scenario 1, US\$51.7 million for Scenario 2 and US\$53.8 million for Scenario 3. Consequently, we would derive a projected total revenue in 2020 of US\$89.0 million for Scenario 1; US\$91.0 million for Scenario 2; and US\$93.1 million for Scenario 3. The projected revenue figures for 2H2020 and full-year 2020 are summarized in **Exhibit 12** below.

**Exhibit 12: Projections for total revenue in 2H2020 and full-year 2020**

Revenue breakdown	Forecast		
	Scenario 1	Scenario 2	Scenario 3
	US\$ million	US\$ million	US\$ million
Room revenue	47.2	49.1	51.1
Other operating revenue	2.5	2.6	2.7
Total revenue for 2H2020	49.7	51.7	53.8
Total revenue for 1H2020 (actual)	39.3	39.3	39.3
Total revenue for 2020	89.0	91.0	93.1

Scenario 1: portfolio RevPAR of US\$48; Scenario 2: portfolio RevPAR of US\$50; Scenario 3: portfolio RevPAR of US\$52

Source: FPA Financial

We will now further assess the feasibility of the 3 projection scenarios by comparing the projected total revenue for each scenario with a projected total revenue for 2020 based on STR's RevPAR forecast for the US hotel industry. To do so, we will be adopting, as a proxy, STR's projection of a 52.3% decline in US hotel RevPAR for 2020 as the change in the Group's room revenue in 2020. This will imply a room revenue of US\$82.3 million for 2020, based on an estimated annualised total revenue figure of US\$172.5 million in 2019, as shown in **Exhibit 13**. Assuming room revenue to be 95% of total revenue, the total revenue figure would be US\$86.6 million.

**Exhibit 13: Projected total revenue for 2020 based on STR RevPAR forecast**

	2019 actual		2020 forecast	
	Listing to 31 Dec 19	Annualised	US\$ million	y-o-y change
	US\$ million	US\$ million		
Total revenue	115.0	172.5	82.3	-52.3%

Source: ARA H-Trust, STR, FPA Financial

Given the above, we believe that Scenario 3 would be the most appropriate. The projected total revenue figure of US\$86.6 million based on the STR RevPAR forecast only considers the contributions by the Group's Hyatt portfolio, given that the Marriot portfolio was only acquired in mid-January 2020. Factoring in the contributions by the Marriot portfolio, we believe that the total revenue figures for Scenario 1 and 2 would be too low. At the same time, we note that STR's projection applies across all US hotel segments and we do expect the Group's select-service hotels to outperform other segments such as luxury hotels. Thus, we will hereon adopt the projected revenue figure of US\$93.1 million for 2020 based on Scenario 3.

**Revenue projection for 2021**

As noted above, we have adopted Scenario 3 which would imply a projected portfolio RevPAR of US\$52 for 2020. In our revenue projection for 2021, we will first adopt STR's projection of a 37.9% RevPAR growth in 2021 as a proxy for the change in the Group's portfolio RevPAR. We would thus expect portfolio RevPAR in 2021 to be US\$72 = [1.379 x US\$52]. Assuming no new property sale or acquisition in 2021 and that all of the Group's hotels remain opened throughout the year, we will derive a projected room revenue of US\$140.3 million, as shown in **Exhibit 14**.

**Exhibit 14: Projected room revenue for 2021**

Period	Total rooms*	Portfolio RevPAR (US\$)	No. of days	Room revenue (US\$ million)
2021	5,340	72	365	140.3

Source: FPA Financial

Assuming room revenue to be 95% of total revenue, we expect total revenue in 2021 to be US\$147.7 million = [1/0.95 x US\$140.3 million].

**EPS projection for 2020 and 2021**

Given our projected total revenue figures for 2020 and 2021, we then estimate the Group's after-tax net income and derive a projected EPS for the respective years. To do so, we will have to project the Group's expenses and will now discuss our approach.

**Operating expenses**

To estimate operating expenses, we will be adopting its proportion of total revenue, or the operating expense ratio, as a proxy. This is given that components such as room expenses are variable costs that scale according to changes in revenue. At the same time, there are also fixed costs components such as employee and General Manager salaries within operating expenses. However, given that we do not have the detailed breakdown for operating expenses based on the latest financial statements, our projections will consider operating expenses as a whole. We note that the Group's operating expense ratio registered 85.2% for 1H2020, compared to 64.3% in 2H2019, as shown in **Exhibit 15**.

**Exhibit 15: Group's operating expense ratio**

	3Q 2019	4Q 2019	2H2019	1H2020
	US\$ million	US\$ million	US\$ million	US\$ million
Revenue	46.8	39.3	86.1	39.3
Operating expenses	29.1	26.3	55.4	33.5
Operating expense ratio	62.2%	66.9%	64.3%	85.2%

Source: ARA H-Trust, FPA Financial

The higher ratio for 1H2020 is likely due to time required for the Group's hotels' performance to pick up after they were gradually reopened from April. With weaker revenue performance during the initial stages after the hotel reopenings, it is unsurprising that the Group's operating expense ratio would be higher in 1H2020. Nonetheless, given that all hotels had resumed operations since July 1, we would expect greater operating efficiency as hotel revenue performance improves, and thus 2H2020 operating expense ratio should be closer to the 60% range as seen during pre-COVID periods. In our projections, we will assume operating expense ratio at 70% for 2020. In 2021, we would expect operating expense ratio to decrease to pre-COVID times, given an expected rebound in US hotel performance. Thus, we will assume operating expense ratio at 65% for 2021. With our projected total revenue of US\$91.3 million for 2020, projected operating expenses in the period would be US\$63.9 million = [0.70 x US\$91.3 million]. Based on a projected total revenue of US\$147.7 million in 2021, operating expenses in the period would amount to US\$96.0 million = [0.65 x US\$147.7 million].

**Hotel management fee**

The Group's hotel management fee is computed based on 3% of total revenue. With our projected total revenue of US\$91.3 million in 2020, this would imply hotel management fee of US\$2.7 million for the period. Meanwhile, hotel management fee for 2021 would be US\$4.4 million, based on the projected total revenue of US\$147.7 million for the period.

Trustee-Manager's trustee fee and REIT Trustee's fee

We will assume the amount for the Trustee-Manager's trustee fee and REIT Trustee's fee based on the minimum amount of US\$10,000 per month and S\$10,000 per month respectively. This will be assumed in our projections for 2H2020 and 2021. Additionally, we will adopt a currency exchange rate of US\$1 = S\$1.36 in our projections.

Net finance costs

We will assume net finance costs to remain the same in 2H2020 from 1H2020 at US\$5.7 million, bringing the total expected finance costs for 2020 to US\$11.4 million. We will also then assume these costs to remain the same in 2021.

For other expense items such as property taxes, depreciation & amortization and other trust expenses, we have assumed the figures for 2H2020 to remain the same as 1H2020, given that we are unable to appropriately provide projections for these items. We will also then assume these costs to remain the same in 2021 from 2020.

REIT Manager's and Trustee-Manager's management fees

REIT Manager's and Trustee-Manager's management fees are based on 10% of the distributable income of ARA H-Trust before accounting for the management fees. Given no distributable income expected for 2020, this in turn implies no REIT Manager's and Trustee-Manager's management fees for 2020. For 2021, a projected distributable income of about US\$19.4 million (before accounting for the management fees), as shown in **Exhibit 16**, would imply REIT Manager's and Trustee-Manager's management fees of US\$1.9 million.

Exhibit 16: Group's operating expense ratio

	2020 forecast	2021 forecast
	US\$ million	US\$ million
Net property income	13.1	33.9
Less:		
Trustee-Manager's trustee fee	(0.12)	(0.12)
REIT Trustee's fee	(0.10)	(0.10)
Net finance costs	(11.4)	(11.4)
Other trust expenses	(2.8)	(2.8)
Taxation*	(0.0)	(0.0)
Distributable income	-	19.4

\*Taxation for full-year 2020 and 2021 is assumed to be US\$18,000.

Source: FPA Financial

Based on the above expenses projections for the Group, we derive an after-tax net loss of US\$27.1 million in 2020 and US\$8.2 million in 2021. Based on a weighted average number of issued stapled securities of 567.2 million, which we would assume to remain unchanged in 2020 and 2021, we project negative EPS of 4.78 US cents and 1.45 US cents in 2020 and 2021 respectively. We have summarised our expenses and earnings projections in **Exhibit 17** below.

**Exhibit 17: Expenses and earnings projections for 2020 and 2021**

	Full-year 2020 forecast	Full-year 2021 forecast
	US\$ million	US\$ million
Total revenue	93.1	147.7
Operating expenses	(63.9)	(96.0)
<b>Gross operating profit</b>	29.2	51.7
Hotel management fee	(2.7)	(4.4)
Property taxes	(11.2)	(11.2)
Other expenses	(2.2)	(2.2)
<b>Net property income</b>	13.1	33.9
Depreciation and amortisation	(25.8)	(25.8)
REIT Manager's and Trustee-Manager's management fees	-	(1.9)
Trustee-Manager's trustee fee	(0.12)	(0.12)
REIT Trustee's fee	(0.10)	(0.10)
Net finance costs	(11.4)	(11.4)
Other trust expenses	(2.8)	(2.8)
<b>Net income/(loss) for the period before tax</b>	(27.1)	(8.2)
Taxation*	(0.0)	(0.0)
<b>Net income/(loss) for the period after tax</b>	(27.1)	(8.2)
Weighted average no. of stapled securities in issue (million)	567.2	567.2
<b>EPS (US cents)</b>	(4.78)	(1.45)

*Figures have been rounded*

*\*Taxation of US\$9,000 in 1H2020 is assumed to be the same for 2H2020. Taxation for full-year 2020 and 2021 is assumed to be US\$18,000.*

*Source: ARA H-Trust, FPA Financial*

**DPS projection for 2020 and 2021**

With our projected figures for after-tax net income in 2020 and 2021, we will now estimate the Group's distributable income, and in turn DPS, for the respective years. To derive distributable income, we will need to account for distribution adjustments by adding back items such as depreciation & amortization and deferred tax expenses to after-tax net income. We will, however, consider the adjustments pertaining to depreciation and amortization, given that we do not have sufficient information to appropriately project the other items. After accounting for the addition of depreciation and amortization to after-tax net income, we expect no distributable income for 2020 and US\$17.6 million for 2021, as shown in **Exhibit 18**. This translates to no DPS for 2020 and a DPS of 3.10 US cents for 2021, based on 567.3 million issued stapled securities.

**Exhibit 18: Expenses and earnings projections for 2020 and 2021**

	2020 forecast	2021 forecast
	US\$ million	US\$ million
After-tax net income	(27.1)	(8.2)
Add/(less): Distribution adjustments		
Depreciation and amortisation	25.8	25.8
Net distribution adjustments	25.8	25.8
Distributable income	-	17.6
Issued stapled securities (million)	567.3	567.3
DPS (US cents)	-	3.10

Source: FPA Financial

## VALUATION

In our initiation report's valuation analysis, we derived an estimated target price for ARA H-Trust by adopting a relative valuation approach. Specifically, we first derived a peer average P/B ratio of 0.54x based on a peer comparison analysis. We then estimated a target price for ARA H-Trust if its P/B ratio were to adjust to the peer average P/B ratio. Given an NAV per stapled security of US\$0.87 as at 31 December 2019 and a peer average P/B ratio of 0.54x, we estimated a target price of US\$0.470 then.

We now perform an updated peer comparison analysis to account for the changes in the financial position of the peer companies. **Exhibit 19** summarises the data for the updated peer comparison analysis.

### Exhibit 19: Updated peer comparison

Company	Portfolio type	SGX ticker	Share price (US\$) as at 21 Aug 20	Market capitalisation (US\$ million)	EPS <sup>(1)</sup> (US cents)	P/E (x)	NAV <sup>(2)</sup> (US\$)	P/B (x)	DPS <sup>(3)</sup> (US cents)	Dividend yield (%)
ARA US Hospitality Trust	Hospitality	XZL/ARAUS.SI	0.330	187.22	(2.77)	n/m	0.77	0.43	2.85	8.62
Peer companies:										
Apple Hospitality REIT <sup>(5)</sup>	Hospitality	APLE:US	9.390	2,096.04	(0.04)	n/m	13.94	0.67	90.00	9.58
CDL Hospitality Trusts <sup>(4)</sup>	Hospitality	J85/CDLT.SI	1.010	1,233.40	6.43	15.71	1.47	0.69	6.37	6.31
Frasers Hospitality Trust <sup>(4) (6)</sup>	Hospitality	ACV/FRHO.SI	0.425	818.55	1.87	22.73	0.71	0.60	2.50	5.89
Far East Hospitality Trust <sup>(4)</sup>	Hospitality	Q5T/FAEH.SI	0.505	987.34	2.39	21.13	0.86	0.59	3.02	5.98
Average	-	-	-	-	-	19.85	-	0.64	-	6.94

Figures have been rounded

Companies are Singapore-listed, unless otherwise specified

n/m: not meaningful

(1) Based on trailing diluted EPS over the last 4 quarters

(2) As at 30.06.20, unless otherwise specified

(3) Based on trailing DPS over the last 4 quarters

(4) Company reports in SGD currency

(5) Company is listed in the US

(6) NAV as at 31.03.20

Source: Respective company data, FPA Financial

Given the above, we note that ARA H-Trust's current P/B ratio of 0.43x is lower than the peer average P/B ratio of 0.64x. If ARA H-Trust's P/B ratio were to adjust to the peer average of 0.64x, the estimated target price would be US\$0.493. The estimations are as follows:

➤ Target price = [peer average P/B] x [NAV per stapled security as at 30 June 2020] = 0.64 x US\$0.77 = US\$0.493

We note that this estimated target price of US\$0.493 is higher than our previous target price of US\$0.470, which will provide an upside of 49.4% from the current price of US\$0.330.



**INVESTMENT RECOMMENDATION**

ARA H-Trust's share price reached a low of US\$0.305 on March 26 but had then recovered on the back of improvements in the outlook for the US hotel market and overall economy. We note that it hit a recent high of US\$0.475 on June 10, surpassing our previous target price of US\$0.470. However, the share price began to decline in mid-June amid a resurgence of virus cases in the US. Nonetheless, we note that the virus situation in the US appears to have stabilized since early August, and while we are still concerned on the potential of new waves of infection, we are currently more inclined to be positive on the outlook for the US hotel market. This is given that hotel occupancies and RevPAR have shown signs of recovery since April amid a return of domestic travel demand. In addition, we note that industry projections are pointing towards a rebound in the US hotel market in 2021. At the same time, we also note that an US economic recovery appears to be underway, as reflected by improvements in economic indicators such as consumer spending and manufacturing activity. Against this backdrop, we believe that there is further upside in ARA H-Trust's share price. Our valuation review shows that ARA H-Trust's current P/B ratio of 0.43x is lower than the peer average P/B ratio of 0.64x. Adopting a relative valuation approach, the estimated target price would be US\$0.493 if ARA H-Trust's P/B were to readjust to the peers' average of 0.64x. This current target price implies a 49.4% upside from the current share price of US\$0.330 and is higher than our previous target price of US\$0.470. Given that the share price has recently hit a high of US\$0.475 in June, we believe that the upgrade in our target price is warranted. We are therefore maintaining a buy recommendation on ARA H-Trust and our current target price is US\$0.493.

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