

Sabana Reit's proposed merger with ESR-Reit



In the run-up to the extraordinary general meetings of Sabana Shari'ah Compliant Industrial Real Estate Investment Trust (Sabana Reit) and ESR-Reit on Dec 4, where unitholders will vote on the proposed merger of the two Reits, *The Business Times* posed questions to the manager of Sabana Reit and to activist fund managers Quarz Capital and Black Crane Capital – which are objecting to the merger. Below is a summary of their responses. **BY RAE WEE**

SABANA'S RESPONSE

Why should investors accept/reject the discounted price at which Sabana is entering the merger with ESR?

The merger offers investors the option of owning part of a larger, stronger and more resilient platform. This gives investors potential upside for their investment.

Additionally, the board believes the merger offers the best opportunity for a re-rating and for reducing the discount-to-NAV (net asset value) at which Sabana Reit currently trades, as the enlarged Reit will be supported by a developer-sponsor.*

QUARZ AND BLACK CRANE'S RESPONSE

The discount to NAV is substantial when compared against all Reit transactions in the last 18 years.

More than 21 per cent of ESR-Reit's portfolio has lease terms of less than 21 years. There have been no confirmed updates from the authorities that any of the leases will be renewed.

On the other hand, more than 80 per cent of Sabana's portfolio has lease terms exceeding 30 years.

What are the benefits/drawbacks of proceeding with the merger instead of seeking another buyer?

The merger is the only offer the board has received since conducting a strategic review in 2017.

Sabana Reit, being the smallest industrial Reit in the industrial Reit space, has been facing intense competition from the bigger players. These will become more pronounced with uncertainties arising from the Covid-19 pandemic.

The merger would allow Sabana Reit to be more resilient. The enlarged Reit would also be better positioned to take advantage of any opportunities that may become available, including the recovery in the demand for logistics/industrial space as the global trade and economy begins its recovery process.

We are optimistic on the prospects of seeking another buyer. With the effects of Covid-19 subsiding from Q2 2021, and global interest rates remaining low, Sabana's portfolio provides institutional investors such as private equity funds, real estate managers and family offices a high return and sizeable footprint in the attractive Singapore industrial property sector. Given the high structural growth in e-commerce, industrial and logistics assets such as Sabana's are in even higher demand in the post Covid-19 world.

We intend to conduct a fair and transparent sale process, giving interested parties the opportunity to do due diligence on Sabana's assets and make their offers at close to book value.

What are the potential outcomes of not proceeding with the merger but pursuing internalisation instead?

When internalised, the Reit will have to compete with bigger players for attractive assets. There is no certainty of cost savings as the Reit will have to fund its own operating expenses.

If the current sponsor is removed, Sabana Reit's bankers must agree not to recall loans and to refinance them without increasing the interest rate.

An internal manager may also have difficulty attracting and retaining talent, and the management will not have the benefit of an asset pipeline from a developer-sponsor.

The internal manager setup will be similar to NetLink Trust, which is one of the best performing trusts year-to-date. The management structure of such an internal manager has complete alignment with the interest of unitholders. NetLink Trust has ranked first in the Governance Index for Trusts since its inclusion.

By removing the underperforming Reit manager, unitholders will no longer need to pay hefty management fees. Profits currently generated by the Reit manager will go to unitholders.

How can Sabana Reit improve its performance if the merger does not take place?

Sabana Reit will continue to divest matured assets and enhance portfolio returns through AEIs (asset enhancement initiatives). The manager will do its very best to provide stable returns to its unitholders.

The internal manager will work on increasing occupancy rates, decreasing financing costs, undertaking redevelopment for unutilised gross floor area, and purchasing yield accretive assets. It will also undertake AEI to refresh a number of properties. In particular, a new retail component at 151 Lorong Chuan will increase its appeal.

*BT's note: Both Sabana Reit and ESR-Reit are controlled by ESR Cayman, a Hong Kong-listed manager of logistics real estate.