Investor's Guide to:

Real Estate Investment Trust

2024

How to earn Passive Income and retire early

Growing up in Singapore, it is common to hear our parents' talk about how much better their lives would be, if they had bought some extra shophouses back in the day…

That said, investing in Singapore properties was never easy. Most investors do not have the capital nor knowledge to be successful.

Today, we will show you how you can own real estate through an investment vehicle called **Real Estate Investment Trust (REIT)**.

With REITs, aspiring investors like you, not need to worry about large capital requirements, house mortgage or need extensive knowledge in real estate.

Let's jump right in, get you up to speed and kick start your REITs investing immediately.

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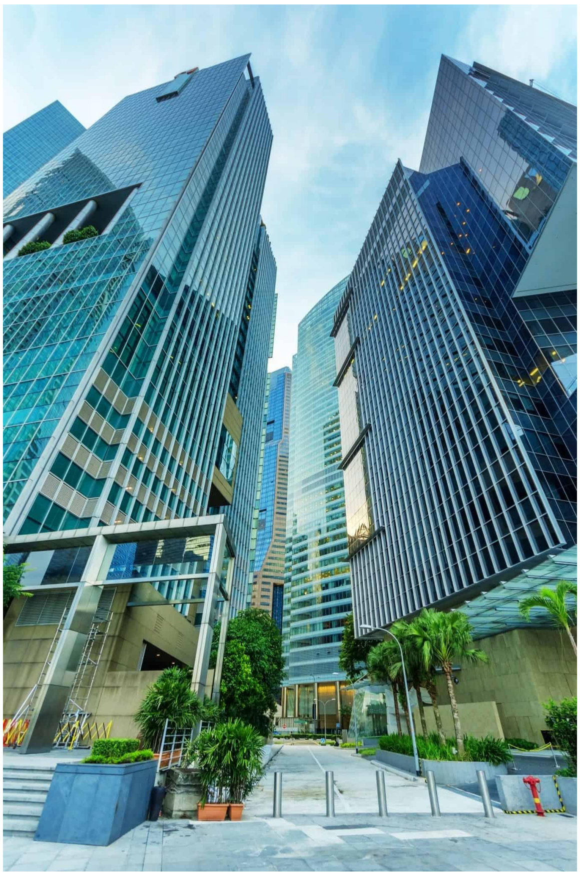
What Are REITs?

Singapore Real Estate Investment Trusts (also commonly referred to as S-REITs) are listed companies that pool investors' capital to invest, own and operate real estate properties.



The properties are then leased out to tenants in return for rents. Investors who invest in REITs are co-owners of the REITs.

They are entitled to earn rental income from the property assets which are distributed regularly. The returns they earn from the investment is called distribution yield.

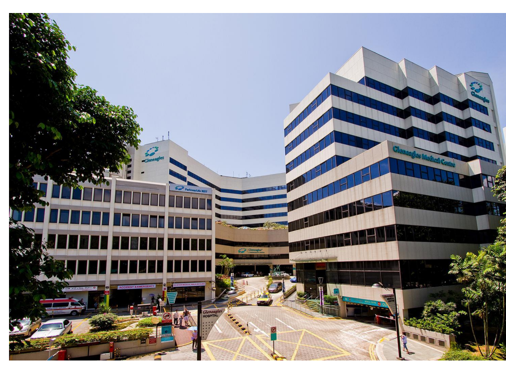
Aside from that, investors also stand to benefit from the capital gain as the property value increases.

Although REITs may not be a common term for many non-investors, Singaporeans are no stranger to the properties owned or managed by these REITs.

We list some of these popular landmarks below;

Marina Bay Financial Centre is owned by **Suntec REIT** with 33% ownership. Suntec REIT is known for their commercial real estate portfolio. Currently, the REIT owns 7 landmark buildings at valuation of approximately $12.3 billion.

Gleneagles Hospital is owned by **ParkwayLife REIT.** Plife REIT has a total portfolio size of 61 properties valuing at approximately S$2.2 billion which makes them one of the largest healthcare REITs listed in Asia.



Paragon is an upscale retail mall managed by **Paragon REIT** *(formerly known as SPH REIT)*. The REIT owns 5 properties, including 3 in Singapore; Paragon, The Clementi Mall and The Rail Mail. Its overall portfolio is valued at approximately $4.1 billion.

Why invest in REITs?

There are two main objectives for investing in REITs:

1. Steady and regular stream of dividend income

2. Gradual appreciation in property value

How to Buy REITs in Singapore

REITs are traded in the stock exchange just like common stocks. Before you can invest in local REITs, you will need 2 accounts:

- SGX CDP account
- Brokerage account

If you have been investing in the stock market, then chances are you already have both the accounts.

Next, all you need is to know the code of the REIT you are interested in. With that (and a funded account), you can then make your purchase via your online brokerage platform or by calling your broker.

However, if you are a new investor, you should be able to apply for both accounts in a single seating via a local brokerage firm.

The turnaround time takes less than 7 working days depending on your broker.

If you're using a discount broker that holds your stocks for you, you may not even need a CDP account. The only downside is that you will not directly own the stocks you bought. (learn more about how the CDP works here)

Singapore REITs Index and ETF

As with stocks, you can either choose to analyse and pick individual REITs or invest in a basket of REITs through the use of Exchange Traded Funds (ETFs).

ETFs are passive funds that aim to emulate the results of an underlying index. There are several REITs ETF listed in the SGX for investors to choose from.

Here's a quick explanation of the difference between a REITs Index and a REITs ETF:

Singapore REITs Index

SGX S-REIT Index aims to track the performance of real estate investment trusts (REITs) in Singapore.

The index is a free-float market capitalisation weighted index which is reviewed bi-annually in March and September. Although the index is not commonly used by the media, investors can benchmark their performance against the index, and use it to determine the REIT market sentiment.

Alternatively, you can refer to the SGX S-REIT 20 Index. It is also a free-float market capitalisation weighted index, but it measures only 20 SGX-listed REITs, selected by size and trading volume.

For more information you can refer to SGX.

Singapore REITs ETF

There are four REIT ETFs listed on the SGX that you can choose from:

- Lion-Phillip S-REIT ETF
- NikkoAM-Straits Trading Asia Ex-Japan REIT ETF
- Phillip SGX APAC Dividend Leaders REIT ETF
- CSOP iEdge S-REIT Leaders Index ETF

	Lion-Phillip S-REIT ETF	NikkoAM-Straits Trading Asia Ex-Japan REIT ETF	Phillip SGX APAC Dividend Leaders REIT ETF	CSOP iEdge S-REIT Leaders Index ETF
Underlying Index	Morningstar® Singapore REIT Yield Focus Index	FTSE EPRA Nareit Asia ex Japan Net Total Return REIT Index	SGX APAC Ex-Japan Dividend Leaders REIT Index	CSOP iEdge S-REIT Leaders Index
12 Months Dividend Yield	5.6%	5.71%	4.13%	4.94%
Dividend Frequency	Semi-annually	Quarterly	Semi-annually	Semi-annually
Fund Size (AUM)	SGD 291.4m	SGD 393.77m	USD 10.1m	SGD 71.6m
Management Fee	0.6%	0.55%	1.13%	0.6%

*Dividend yields and AUM updated on Jan 2024, data from Morningstar (for latest updates on Singapore REIT ETFs, check this page!)

Roboadvisor REIT Portfolio

Syfe, a licensed roboadvisor, manages a REIT portfolio for investors to invest conveniently with enhanced risk management.

The Syfe REIT+ portfolio invests between Singapore listed REITs and Singapore Government bonds. The weightage would shift between REITs and bonds depending on the market condition. Such portfolio rebalancing is done automatically by Syfe, that you will not have to worry about keeping up with the markets.

As of Jan 2024, the indicative dividend yield is 4.43% and investor has a choice to decide between receiving the dividends in cash quarterly or have them automatically reinvested.

Investors can also choose to invest lump sum or on a monthly basis, and there is no minimum amount to start.

Syfe charges a 0.35% to 0.65% annual fee for the service, depending on the amount invested.

How to select REITs?

There are many ways to select REITs. This section describes just one of the ways to select or analyze the REITs market to generate superior returns.

Before we get into it, here're some caveats:

Unlike many suggestions offered by other information sources from the internet. We begin without any preconceived notions as to which strategies work in the Singapore markets for local REITs. Instead, we will test each strategy before deciding which strategy works.

Another feature of employing this strategy is that we can avoid a deep discussion on the relative merits of each REIT counter using this approach. Beginners need a safe way to be able to obtain dividend income without a long-drawn discussion into issues such as lease expiry, tenant mix and sensitivity of bank loans to interest rates.

This is our approach to REITs selection:

Step 1: Start with a universe of all Singapore REITs

The first step would be, to begin with, a universe of REITs. This is a small universe of ~43 stocks.

The first we do is to create a baseline that looks at Singapore REIT performance across different time frames.

In an actual course on investing, we cover multiple time frames but for this example, we consider the timeframe over 10 years ending 31 December 2019.

For the 10 years ending 31 December 2019, investing in an equal-weighted REIT portfolio returned 12.67% and has a semivariance (or downside risk) of 8.47%.

Step 2: Backtest different investment factors

The next step would be to select from this half of the REITs universe 21-22 counters with a superior factor to see whether the 10-year performance improves.

Suppose we want to see whether REITs with higher dividends do better than average, we will select 21 REITs with the highest dividends and back-test this result on Bloomberg to see what kind of returns we get compared to our baseline earlier.

We examine a huge range of factors. For this article, we only ask the question of whether high dividends or low gearing have done well over the past 10 years.

Our results are as follows:

Strategy	Return	Downside Risk
All REITs	12.67%	8.47%
Half REITs with **highest dividends**	12.02%	8.97%
Half REITs with **lowest gearing**	13.10%	8.73%

From our observations, we can note the high dividend strategy would not only give us lower overall returns, they are more volatile with higher downside risk. For months, retail investors have exhausted the high yielding strategy that it no longer works in the markets. Instead, by choosing a REIT with a lower gearing (or lower debt over assets), we might still be able to have superior returns although it corresponds to taking on higher risk.

Step 3: Backtest combinations of factors

If one factor will reduce the REITs universe by half and give us decent performance, can we find a different factor to improve the performance further?

This requires painstaking back-tests over hours on Bloomberg terminal to determine a combination of factors that lead to superior performance.

For example, superior performance can be derived from shortlisting the REITs with the lowest PE ratio followed by the lowest BETA or volatility relative to the rest of the stock market.

Our back-tested performance was 16.10% with a downside risk of 8.7%. This is a decent strategy to run our REIT portfolio.

Step 4: Screen stocks with a proven set of factors

Now we will screen for the REITs that meet our criteria.

We use a tool normally employed by retail investors like Stocks Café or REIT Screener to screen our REITs. In this example, we choose the 20 REITs with the lowest PE ratio, then we choose the REITs with the lowest BETA.

An example of a screen result looked like this:

- Frasers Centrepoint Trust
- ParkwayLife REIT
- First REIT
- Cromwell REIT SGD
- Sabana REIT
- MapleTree Com Trust
- BHG Retail Trust
- EC World REIT

Step 5: Apply qualitative analysis

With a much shorter list, a retail investor can begin to search for brokerage reports to review each REIT for suitability. At this stage, an investor can go deep into deciding which REIT to buy. Depending on his experience, he can look into multiple factors before making his final decision.

There is a much lower risk of making a mistake in stock-selection. As most of the heavy lifting was done by the qualitative back-testing, absent a glaring possibility of mismanagement, or brushes with the law, the REIT is normally safe to invest in.

Interestingly, the screened portfolio resembles a barbell REIT portfolio with safe stalwarts like ParkwayLife REIT and high yielding REITs like EC World REIT. This was not a property anticipated before running the stock screener.

In this example, we are more likely to eliminate BHG REIT and tolerate the rest due to the absence of analyst reports on the counter.

In practice, we will review a combination of as much as 10 factors over 3, 5 and 10-year histories. Short-listed factor combinations are democratically voted into a class portfolio before the class is broken into teams that will then research each counter aggressively.

How to increase dividend yield with leverage?

Warning: This is NOT for everybody

Extending the example earlier, you would have a REIT strategy with a return of 16.10% and a downside risk of 8.70%. As it is a REIT portfolio, it should comfortably generate 6% dividends to give you an incentive to stay invested.

You can supercharge the portfolio by leveraging it and adopt a Leverage REIT strategy to reach their goal of financial independence much earlier.

Typically, when we leverage an investment, for each $1 we have injected into the portfolio, we can borrow another $1 from the broker to make the portfolio larger. The broker will not do this for free but will charge about a 3.5% interest rate on your borrowings.

The first effect of leverage is that the dividends you will receive from your investments will increase. In this example, your capital will give you a yield of 6%. The amount borrowed from the broker invested in the same portfolio will give you another 6%. The broker will then charge you 3.5% for lending money to you.

The yield you will receive from your initial investment is:

6% + 6% - 3.5% or 9.5%.

So, $100,000 invested in this strategy buying $200,000 of REITs would generate $9,500 of dividends a year after paying off the interest to the broker.

The second effect is that your leveraged returns will be phenomenal after accounting for capital gains. Accounting for both dividend yields and capital gains, the back-tested strategy returns 16.10%.

If you leverage by borrowing $1 for each $1 you have, your gains will potentially be:

16.10% x 2 – 3.5% or 28.7%!

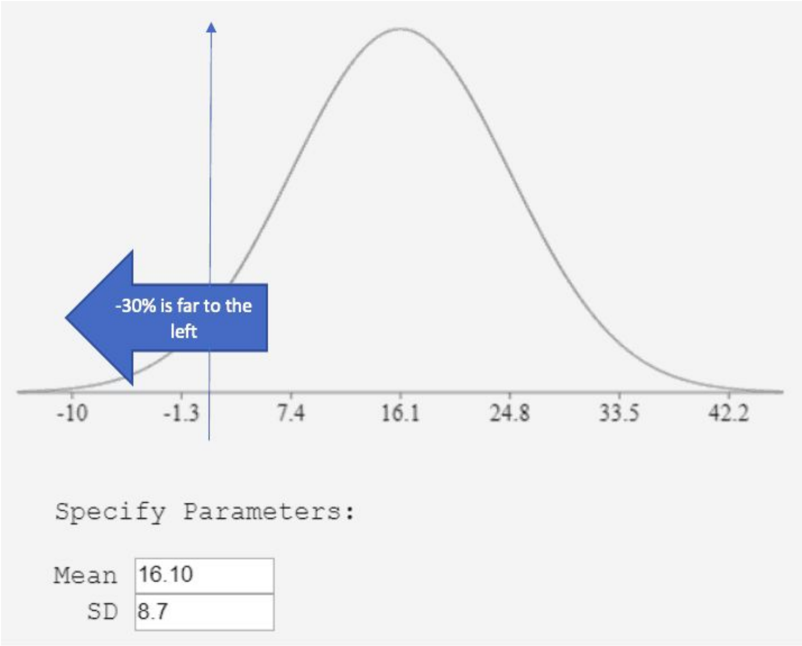
So, $100,000 invested in this strategy buying $200,000 of REITs would generate $9,500 of dividends a year after paying off the interest and also $19,200 of capital gains.

The problem of leverage is that it comes with risks that are hard to stomach for most retail investors.

In the above example, if your portfolio loses 30%, you will receive a margin call. If you cannot service your margin call within 48 hours, the broker can liquidate your investments and you will be stuck with a 60% loss of your initial investment.

This is why knowing the returns and downside risk is very important. If we plot a normal distribution curve using returns of 16.10% and downside risk of 8.7%, we will find that the probability of losing 30% in any particular year is close to 0.

This gives us a degree of confidence that this Leveraged REIT strategy is safe.



4 Key Characteristics of an Ideal REIT

Most investors assume that all REITs are equally safe and that the only difference is the dividend payouts they will receive.

That's a huge misconception.

The truth is, REITs investors face the same risks as any other stock investor. Hence, you have to do your due diligence and study the REIT that you are interested in.

We help you get started here with 4 key characteristics that you should look out for in an ideal REIT:

#1. Ideal REITs Shouldn’t Be Overvalued

REITs are an investment which relies on the underlying real estate’s ability to generate income. As with all real estate investments, valuation of the REIT is important.

While you can rely on the Greater Fool’s Theory to bail you out, most investors should aim not to overpay for any REIT (*or any other forms of investments*). You wouldn’t want to overpay when you buy your new home either. So why would you want to overpay for REITs?

#2. Ideal REITs Need Good Outlook

REITs that are worth investing in should be in sub-sectors that have a good investment outlook. This outlook can refer to any macro trend from interest rate and regulatory trends to industry and economic trends.

For example, we know that the global economy has been slowing down in the past few years. The slowdown has affected the rental market in office REITs, causing negative rental reversion.

One other macro trend is the rising emergence of data science as corporations begin to harvest data to implement data analytics. This increases the demand for data centres.

Hence, we can look towards data storage REITs as a better alternative compared to office REITs in terms of investment outlook.

REITs that offer such data storage services become a more desirable investment compared to office REITs.

#3. Ideal REITs need a Growth Element

The nature of REITs lies between the behaviour of a stock and a bond.

REITs own a portfolio of properties and receive rental income from the properties' tenants. These rental incomes are then distributed to the shareholders after accounting for expenses. This gives REITs a bond-like feature of quarterly dividend payments to shareholders which is similar to the quarterly coupon payments that bondholders receive.

Also, REITs also have stock-like characteristics as they are affected by speculation, better valuation and forward outlook. These factors can push its share price higher to give capital gains. These capital gains can be driven by any catalyst.

One core characteristic that all profitable REIT investments should have is the growth element. Stock investors should be quite familiar with the idea of growth stocks.

Good REIT investments should be continuously growing its net income on a year-on-year basis.

Growth can come in two forms:

- Organic growth through Asset Enhancement Initiatives (AEIs), positive rental reversion and increasing occupancy or capital recycling.

- Inorganic growth through the acquisition of new properties or invest in undeveloped properties.

#4. Ideal REITs Need a Good Cap Rate, Not Just Good Dividend Yield

The capitalisation rate (cap rate) is the rate of return on a real estate investment property based on the expected income of a property.

Some investors confuse cap rate with distribution yield due to its similarity in measuring a REIT's income yielding ability.

Cap rate measures a REIT's income yielding ability against its underlying asset value whereas distribution yield measures a REIT's income against its market capitalisation.

Instead of using distribution yield as your basis for comparison, it's much better to use the cap rate as an indicator of the REIT's rental generating ability.

A high cap rate can signal the management or property's ability to command higher rental income.

This tells you if the REIT you're looking at is good at generating rental income or it's just using accounting shenanigans to fool investors into thinking it's a good investment.

3 Things to avoid when investing in REITs

After learning what an ideal REIT is, now let's take a look at the three factors you should avoid when investing in any REIT.

#1. Avoid Choosing REITs based on Dividends

This might sound counter-intuitive, but you shouldn't only focus on the potential dividend yield of the REIT when you buy REITs.

What do we mean by that?

Why did a troubled REIT like Sabana REIT have a double-digit yield of 11.8% in 2017 compared to Keppel DC REIT's 5.6%?

Isn't Keppel DC REIT supposed to be of better quality and growth prospects than Sabana REIT?

To answer that question, we first have to look at the total return that both REITs yield in the past year (let’s use CY2016 for a fair comparison):

Sabana REIT:

Source: Yahoo (Sabana REIT)

Keppel DC REIT:

Source: Yahoo (Keppel DC REIT)

In 2016, Sabana REIT share price fell by 25% (even if we exclude the significant drop in Jan 2017 from the rights issue announcement!). Now compare that with Keppel DC REIT's performance over the past year of 18% gain. Even after getting an 11.8% yield from dividends, shareholders of Sabana REIT are still making a loss of 13%!

This is in stark contrast to the shareholders of Keppel DC REIT, which made 23.6% in 2016.

As investors, we tend to have selection bias in focusing on REITs with higher dividend yields and avoid those with lower yields. This is so as we often think that the return we get from REITs is only from dividends, which isn't true!

Apart from dividends, we would expect to make capital gains as well. So rather than looking at dividend alone, we should be looking at both dividends and capital gains we can generate from the REIT.

#2. Avoid REITs with Poor Macro Outlook

REITs stand for Real Estate Investment Trust. This means that investing in REITs is like investing in real estate, and you don't have to worry about property cooling measures like ABSD.

For any real estate investment, the macro outlook of the economy will affect the return of the investment. For REITs, there are five sub-sectors: Office, Retail, Industrial, Hospitality and Healthcare.

Each sub-sector has a different outlook considering the economic factors affecting them.

There are still outstanding REITs within each sub-sector.

But bear in mind: There is a high opportunity cost of investing in outstanding REITs of sub-sectors with weak macro outlook. We can make much better investments if we can allocate our capital into REITs from sub-sectors with better growth potential.

For example: If the retail sub-sector is facing obstacles like turbulent global economy and increased competition from eCommerce... it might be a better idea to place your capital into REITs of other sub-sectors where there is clearer and more visible growth.

Another example is, if the retail sub-sector is projected to do poorly. You can give CapitaMall Trust (which is an outstanding Retail REIT) a miss, and put your capital in Keppel DC REIT which is in another better sub-sector.

#3. Avoid REITs with High Gearing

Most REITs use debt to finance the acquisition of new properties into their portfolio. Thus, investments in REITs will expose investors to interest rate risk. As interest rate increases, it will decrease the earnings of REITs and affect the distribution for REITs.

To determine the relative amount of debt a REIT has, we use gearing ratio as a gauge. Gearing ratio represents a REIT's amount of debt over its total assets. As the ratio increases, it means the REIT has taken more debt over each unit of asset.

Investors are exposed to higher interest rate risk when REITs are over-leveraged (high gearing level).

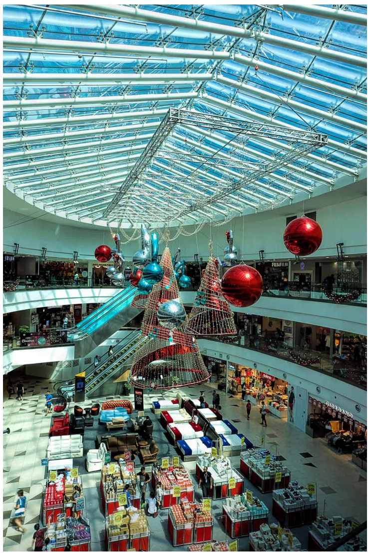
While not all REITs with high gearing ratio are poor investments, we have to remember that a higher gearing ratio exposes our portfolio to higher interest rate risk.

(Note that there are also some REITs that raise finance through equity via rights issue like Sabana REIT, Ascott Residence Trust and Keppel REIT).

6 Types of REITs in Singapore

#1. Retail REITs

Shopping malls you visit are most probably owned by a retail REIT.



If you consider investing in these REITs, you should assess the health of the retail industry itself, as it is one of the major factors of your future profits. Keep in mind that retail REITs generate profits by renting space to its tenants. If their tenants have cash flow issues, they may not be able to pay their rent on time. Some of them may even default on their payment.

In such situations, the REIT has to find a replacement quickly, and this isn't always possible. If you intend to invest in retail REITs, look out for those with very stable anchor tenants. Once you're done with your analysis of the industry, you have to analyse the REIT itself. Look for signs of strong balance sheets, sustainable profits and little debt.

In a troubled economy, retail REITs with cash on hand will be able to purchase good real estate at discounted prices. Retail investors like yourself should take advantage of such situations.

#2 Residential REITs

Residential REITs own and manage manufactured housing and rental apartments or buildings.

When analysing such REITs, consider how affordable homes are in the target area, compared to the country average. Wherever home affordability is low, the number of people who are forced to rent is higher, thus increasing the rental prices. As a result, most major residential REITs focus on big urban areas.

Investors also look at population and job growth. Cities with booming economies attract more people, therefore bringing a higher demand for rental homes.

Rising rents combined with low supply are ideal conditions for residential REITs.

#3 Office REITs

These are the REITs that focus their investments in office buildings.

Their income comes from the rental of office space.

The main advantage office REITs enjoy is that they usually deal with long term leases.

There are a few things to consider before investing in an office REIT:

- The state of the economy
- The unemployment rate and its trend
- The vacancy rates
- The economic well-being of the area in which the REITs makes its investments
- The capital available for acquisitions

Office REITs may also be seen as a subset of industrial REITs.

#4 Industrial REITs

Industrial REITs manage and own industrial facilities, they rent these spaces to their tenants. Some of the spaces are warehouses, distribution centres and specialised facilities.

It's important to take a look at the spaces and facilities that these REITs own and understand the industry players who are renting the spaces. Also note that due to the massive volume of space each facility holds, losing a tenant might be a huge problem for industrial REIT with little assets.

Industrial properties generally have shorter leases and 30 years are typical. As such the property value depreciate faster and investors are compensated with higher yields.

#5 Hospitality REITs

These REITs hold properties in the hospitality sector such as hotels, budget accommodations, serviced apartments or short-term lodging facilities.

It may sound attractive to be able to own hotels through Hospitality REITs, but there are a few considerations you will have to think about as well.

You have to understand how the hospitality sector is doing..

When the economy is poor, the hospitality sector would be expected to face lower sales and occupancy rates, especially if the hotel is focused on tourism.

It is good to take a look at the properties owned by the hospitality REIT and understand its average occupancy rate. As these properties are sustained by short term stays and lease, their performance can be volatile and highly affected by economic movements.

#6 Healthcare REITs

Healthcare REITS focus their investments in various medical facilities such as hospitals, medical centres, nursing homes and retirement facilities. Their success is tightly connected to the evolution of the healthcare system.

When looking to invest in healthcare REITs, you should choose REITs that have both:

1) A diversified group of clients
2) A wide range of property types.

Also check that the REITs of your choice have significant healthcare experience.

REITs vs Physical Properties

Buying REITs has often been seen as an alternative to buying physical properties. But which is a better form of investment? What is the difference between the two?

This section explores the differences between buying REITs and actually owning the physical properties.

While REITS have a similar exposure to the real estate market, they are somewhat different when considered from the perspective of an investment portfolio.

First, we will look at the advantages of REITs versus physical properties.

Advantages

- **High Liquidity**

One of the main advantages of REITs is that it is relatively easy for an investor to enter or exit the investment, since they are traded just like stocks on the stock exchange.

On the other hand, property owners will take a while to find a buyer at the right price and the transaction process generally takes a few months.

- **Invest with Minimum Capital Outlay**

The minimum cost of most property investments is substantial.

For example: A $500,000 property with 80% loan to valuation will require $100,000 down payment. (*not including other extra costs such as legal fees, stamp duty, etc*).

For REITs, the minimum outlay is 100 shares, some REITs may even cost less than $100. For example, Keppel REIT costs just $91.5 for 100 shares in Jan 2024.

- **Management Team Handles Tenants and Maintenance**

One of the most troublesome aspects of managing physical properties is dealing with tenants and maintenance of the property. There are many scary stories of bad tenants, tenants who don't pay rent, tenants who damage your property etc. Bad tenants can cause a lot of problems and headaches for the property owner.

It is also important to consider property maintenance such as the flooring, plumbing, painting, etc, since the properties age over time.

- **Diversification into Office, Retail, Industrial, Healthcare**

While it is easy to buy residential properties, investing in commercial properties takes a lot of more knowledge and experience. Commercial property investors typically invest in office, strata retail and industrial properties, but buying actual retail malls will be very tough due to the high costs. REITs not only allow investors to take part in the largest shopping malls, but also hospitals, prestigious office buildings and more.

Of course, REITs investing is not a bed of roses. It comes with a few disadvantages that REITs investors should keep in mind:

Disadvantages

- **Volatility of REIT Prices**

Since REITs are traded on the stock exchange, the stock price of the REIT is subject to market volatility like any other stocks.

Physical property valuations are generally more stable and are unlikely to experience wild swings daily.

- **Management Fees**

While you save a lot of hassle with REITs, the management team does charge a handsome management fees which eats into your returns. Management fees are paid not only on the basis of asset valuation, but also each time a property is acquired or divested by the REIT.

- **Lower Leverage Power**

In general, most REITs have a leverage cap of 35% without a credit rating and up to 60% with a credit rating.

However, physical properties can easily get 60% to 80% loan to valuation ratio, so you can get much higher returns.

REITs Are a Good Addition to Any Portfolio

The combination of management fees and lower leverage power means that returns from REITs are unlikely to beat returns from property investments.

However, the high leverage in property investments also means that it's riskier. Bad property investments can seriously damage an investor's wealth.

All in all, REITs provide an easy, low risk investment option to gain exposure to diversified portfolio of properties.

REITs Fee Structure

Here’re some of the key people managing your REIT, what they do and how much they get paid:

REIT Manager

The REIT manager is akin to a fund manager, making all the investment decisions on behalf of all the unitholders.

- Base Fee: 0.25% – 0.5% per annum of Deposited Property
- Performance Fee: 3% – 4% of Net Property Income
- Acquisition Fee: 1% of property value
- Divestment Fee: 0.5% of property value

Property Manager

The property manager is akin to a facilities manager, maintaining and operating the properties under their watch.

- 2% - 3% of gross revenue and/or
- 2% - 3% of Net Property Income or leasing commissions

Trustee

The trustee role is usually performed by a bank. It is necessary because the bank act as an independent party to the REIT manager, a check and balance when it comes to handling unitholders' funds.

- 0.01% - 0.1% of assets or Deposited Property

How do REITs raise funds

REITs often have to raise funds to acquire new properties.

This is because there aren’t sufficient retained earnings due to the regular large dividend distributions.

There are a few ways REITs can carry out their fundraising:

1) Debt

Debt is usually the first option and the underlying properties are being collateralized to secure a lower interest rate with the banks.

However, REITs in Singapore can only gear up to a maximum 45% debt-to-asset ratio. This would limit the ability of REITs to borrow more money.

2) Rights Issue

REITs are likely to turn to rights issue when there are insufficient debt room to borrow.

A rights issue is a right to buy additional shares / units in a REIT. It is issued to the REIT's existing unit holders, usually at a discounted market price in proportion to their holdings.

For example, a rights issue of 1:4 means for every four shares you own, you have the option to purchase 1 share at a discounted price as stated in the rights issue.

A unitholder can choose to subscribe or not. The latter would mean that he would suffer dilution as the percentage ownership of the REIT would shrink since more units would be created.

A unitholder may also choose to subscribe more units and may be granted the rights if other unitholders decided not to take them up.

REITs often use rights issue to raise capital for potential acquisition which are deemed to be yield accretive. Unlike raising through debt, rights issue does not increase the financial gearing of the REITs. In fact, it lowers the gearing.

3) Perpetual Securities

There were instances whereby REITs issued perpetual securities to raise funds.

They promised a fixed interest rate like a bond but they are treated as equity. Hence they are not counted as debt and do not increase the gearing ratio.

This seems like sidestepping the gearing criterion and investors could always treat it as debt to be conservative.

REIT vs Business Trust: 5 Differences You Must Know

Many investors are always confused about Real Estate Investment Trust (REIT) and Business Trust (BT). Although both of them sound similar, the nature of both instruments is quite different. Due to these differences, both trusts behave differently in the market.

Louis has shared about the difference in a video series as well, click on the image below to watch the videos:

As REIT investors, you should know these differences as they will affect the dividends payout you are entitled to, and may expose you to different level of risks:

	REITs	Business Trust
Trust Objective	Primarily passive investment vehicles	Actively engage in undertaking business operations
Dividend	Must distribute more than 90% of income as dividend	Not mandatory distribution of dividend, can distribute from operating cash flow
Gearing Limit	45%	No gearing limit
Voting Rights	>50%	>75%
Investment Restriction	At least 90% income must be generated from rental	No restriction, typically own high operating cash flow business

Differences between REITs and Business Trusts

- **Trust Objective**

The objective for both trusts is very different. REITs look for passive income while Business Trust actively engage in undertaking business operations.

If you are an investor looking for passive income, you should invest in REITs rather than Business Trust.

- **Dividend**

The regulation for dividend distribution is not the same for REIT and Business Trust. REIT is mandatory to distribute at least 90% of disposable income to the unitholders while Business Trust is not mandatory to distribute dividend.

However, Business Trust can distribute dividend from operating cash flow. This means that even though the net profit of Business Trust is less than zero, Business Trust still can distribute dividend if the operating cash flow is positive.

Because of this reason, Business Trust tends to own businesses that have high operating cash flow.

- **Gearing Limit**

REIT maximum gearing limit is only 35% for non-rated REIT and 60% for rated REIT. But for Business Trust, there is no gearing limit.

Both has pro and con for this gearing limit. Gearing limit for REIT is good for investors who have a low-risk appetite while Business Trust can increase their leverage without limit is suitable for investors who have a high-risk appetite.

- **Voting Right**

REIT requires at least 50% of voting right to pass through certain proposals while Business Trust requires at least 75% of voting right.

This means that the controlling interest for Business Trust is only required to hold more than 25% of the company. Because of this reason, Business Trust tends to have a higher free float and can raise more fund from issuing units to public investors.

- **Investment Restriction**

At least 90% of income for REIT must be generated from the rental income while there is no restriction for Business Trust.

This can be bad if the property market is in a downturn, the income for REIT may be affected, and thus there might be a lower dividend for the unit holders.

So, which one should you invest? REIT or Business Trust? That depends on your investing objective.

Here's a quick summary:

If you are looking for passive income, REIT may be a better choice. If you are looking for higher return, Business Trust tends to give higher return but come with higher volatility and high risk.

REITs Glossary: Essential Terms All REITs Investors Must Know

You now know what to look for and avoid in REITs. But that's not all. In your REITs investing journey, you will need to understand REIT specific terms. This section highlights the essential terms you should know.

Weighted Lease Average Expiry (WALE)

Weighted Lease Average Expiry (WALE) is a metric used by investors to access the likelihood of REITs' properties portfolio being vacant. As we all know, income generated by REITs is derived from leasing out spaces. Hence, occupancy would hurt REITs' earnings and therefore resulting in a distribution loss.

There are two ways to measure WALE. Either by using rentable area or rental income, measured across all tenants' remaining lease in years.

An example based on gross rental income:

- Property #1: 15% of gross rental income with 5 years of remaining lease term
- Property #2: 70% of gross rental income with 2 years of remaining lease term
- Property #3: 15% of gross rental income with 10 years of remaining lease term

Therefore, the WALE is:

(0.15 * 5) + (0.7 * 2) + (0.15 * 10) = 3.65 years

What it tells us is that the average lease expiry of the properties portfolio is 3.65 years.

As with all metrics, the figure has to be measured across similar sectors to conclude whether it is over or below the industry average.

High WALE implies stronger income protection due to later lease expiry term. However, the main downside is that the REIT is not able to capitalise on the higher rental during a market boom as its average lease expiry is longer.

Low WALE, on the other hand, has higher susceptibility towards rental market movement as shorter expiry term means frequent rental renewal. This allows the REIT to capitalize on higher rental but at the same time means that it is susceptible to a lower rental yield during bad times.

Weighted Average Debt Maturity (WADM)

REITs have to gear up to invest in the capital-intensive properties. Each debt has its own tenure and maturity dates.

REITs would usually rollover their debts as each one matures. But this practice comes with risks as interest rate might be higher or some of the terms may become more onerous. Worst is that the REITs couldn't borrow the amount that they intended.

WADM gives a REIT investor an indication how much debt is due. It is expressed in years. For example, 4.3 years means a large chunk of loans are likely to be settled in about 4 years' time. Hence, a longer WADM is better than shorter WADM, generally speaking.

Distribution Per Unit (DPU)

DPU = (Total Dividend / Distribution) ÷ Number Of Shares.

DPU is known as distribution per unit. It tells investors how much dividend / distribution they would get for every share they own.

Net Asset Value (NAV)

NAV Per Share = (Assets Market Value – Liabilities Value) ÷ Number of Shares.

Net Asset Value gives us an indicative value of what investors would get if the Company liquidates all of its assets and pays off its liability.

NAV is usually used to compare against market prices to determine above or under valuation of the assets.

Since most of a REIT's assets are investment properties, the NAV is close to the net valuation of the underlying properties it owns. Hence, investors often compared to the REIT price to its NAV. Crudely put, if a REIT is selling at less than its NAV, it is undervalued.

Revalued Net Asset Value (RNAV)

RNAV Per Share = (Revised Assets Market Value – Revised Liabilities Value) ÷ Number of Shares.

This is similar to NAV except that the assets and liabilities are adjusted to market value. RNAV is mostly used on property stocks with land which are valued at old prices.

Gearing

Gearing (Debt Ratio) = Total Debt ÷ Total Assets

Gearing is a metric used by investors to access a REIT's financial leverage.

A company with high gearing is said to be more vulnerable during a recession as it has to continue to pay interest no matter how bad the earnings are.

Should the REIT be unable to pay its interest or principal on time, the REIT may fold up. Since 2020, MAS has increased the gearing limit from 45% to 50% for all REITs, in light of the tough economical situations due to the pandemic.

Net Property Income (NPI)

NPI = Gross Revenue – Maintenance Costs - Property Tax – Operating Expenses

NPI is an absolute measure in dollars that gives us an idea about how lucrative the REIT properties are.

A more meaningful way for a retail investor to understand NPI is to look at how much it has changed over time. Increases in NPI of a REIT bode as for investors of the counter.

Capitalization Rate (aka Property Yield)

Cap rate = Net Operating Income / Property Value

Cap Rate is known as Capitalization Rate or property yield.

It is a measure of the property income yielding capability. Most REITs have their individual property Cap Rate stated in their annual report.

A high Cap Rate suggests either the REIT managers' abilities to negotiate for higher income or could also mean the property value has depressed.

Average Interest Rate

The average interest of a REIT measures how expensive their loans are from the banks they borrow the money from. The higher the interest rate, the more expensive the debt funding is.

A research report of REITs dated 2 Jan 2019 by DBS Group Research can give you an idea of how typical numbers can look like when you compare the average interest cost of the REIT against each other:

Potential impact on DPU with 1% increase in interest rates

REIT	Percentage Fixed rate debt (%)	Current Cost of Debt (Sep-18)	Percentage of Debt Due for Refinancing		%Chg in DPU on 1% Increase in Debt Cost Assumptions	
			FY19F	FY20F	FY18F	FY19F
AIMS AMP Capital Industrial REIT	87	3.60%	12%	25%	-1.1%	-2.3%
Ascendas Hospitality Trust	78	1.90%	0%	13%	0.0%	-1.0%
Ascendas India Trust	84	6.10%	20%	12%	-1.5%	-0.7%
Ascendas REIT	85	3.00%	13%	11%	-0.9%	-0.8%
Ascott Residence Trust	82	2.30%	7%	15%	-0.9%	-1.8%
CDL Hospitality Trusts	66	2.40%	19%	8%	-1.4%	-0.6%
Cache Logistics Trust	61	3.72%	6%	10%	-0.5%	-0.7%
ESR REIT	91	3.76%	23%	31%	-0.9%	-1.2%
CapitaLand Commercial Trust	92	2.60%	9%	7%	-1.1%	-0.8%
CapitaLand Retail China Trust	83	2.67%	12%	10%	-1.2%	-0.9%
CapitaLand Mall Trust	95	3.10%	9%	8%	-0.7%	-0.6%
Far East Hospitality Trust	54	2.60%	12%	0%	-1.2%	0.0%
Frasers Centrepoint Trust	64	2.60%	27%	28%	-1.9%	-2.0%
Frasers Commercial Trust	81	3.02%	3%	28%	-0.2%	-1.9%
Frasers Hospitality Trust	73	2.60%	47%	0%	-4.2%	0.0%
Frasers Logistics & Industrial Trust	82	2.50%	28%	26%	-1.3%	-1.2%
Keppel DC REIT	86	1.90%	19%	7%	-1.2%	-0.4%
Keppel REIT*	76	2.80%	20%	17%	-3.6%	-2.9%
Mapletree Commercial Trust	100	2.93%	0%	2%	0.0%	-0.2%
Mapletree North Asia Commercial Trust	75	2.48%	0%	7%	0.0%	-0.8%
Mapletree Industrial Trust	78	3.00%	9%	20%	-0.5%	-1.1%
Mapletree Logistics Trust	78	2.50%	0%	9%	0.0%	-0.9%
Manulife US REIT	100	3.27%	23%	15%	-1.9%	-1.2%
OUE Commercial REIT	75	3.50%	0%	11%	0.0%	-1.5%
OUE Hospitality Trust	71	2.40%	0%	49%	0.0%	-4.5%
Parkway Life REIT	95	0.94%	0%	25%	0.0%	-2.1%
Soilbuild Business Space REIT	67	3.42%	8%	4%	-0.7%	-0.3%
SPH REIT	70	2.85%	23%	31%	-1.4%	-1.9%
Starhill Global REIT	92	3.28%	10%	13%	-1.0%	-1.4%
Suntec REIT*	70	2.86%	23%	9%	-3.0%	-1.1%
S-REIT Average	**80**	**2.89%**	**17%**	**18%**	**-1.1%**	**-1.2%**

Source: Bloomberg Finance L.P., DBS Bank
**includes debt at associate level*

It should be interesting to note from the above table that Ascendas India Trust attracts high rates because Indian interest rates tend to be higher than in other countries.

Asset Enhancement Initiative (AEI)

Refurbishment, revamp, and upgrades of existing property assets are examples of Asset Enhancement Initiatives.

The goal is to optimise the value of a REIT's existing asset properties value to increase rental income. This is very common in Singapore, especially in shopping malls.

Accretive Acquisition

When an acquisition is accretive, the company would expect to produce higher EPS when it acquires properties. Therefore it's able to give a higher distribution to investors.

In REITs, managers often ensure their property acquisitions are yield accretive to win investors votes to pursue an acquisition and raise capital, usually through a rights issue.

Acquisition that is not yield accretive would be seen as destroying investor value.

Rights Issue

A rights issue is a right to buy additional shares / units in a REIT. It is issued to the REIT's existing unit holders, usually at a discounted market price in proportion to their holdings.

For example, a rights issue of 1:4 means for every four shares you own, you have the option to purchase 1 share at a discounted price as stated in the rights issue.

REITs often use rights issue to raise capital for potential acquisition which are deemed to be yield accretive. Unlike raising through debt, rights issue does not increase the financial gearing of the REITs.

Benefit

Existing unit holders are allowed to purchase more of their holdings at a lower price than what they get from the stock market.

Disadvantage

As rights issue requires REITs to create more units. Investors who do not participate in the offering would find their proportion of unit holdings diluted.

Rental Reversion

Rental reversions measure the changes in rental rates when expiring leases become renewed. A positive rental reversion rate is good for the REIT because it signifies that new tenants are willing to pay higher rents compared to existing tenant rates. Similarly, negative rental reversion rates may signify flagging demand or oversupply in the rental markets.

Occupancy Rate

The occupancy rate of a REIT measures the proportion of the lettable area that is currently occupied by a tenant. A 100% occupancy means that the property is fully occupied and has no more room for new tenants. A low occupancy rate of 60% may signify a poor location and lack of demand by the potential tenant.

Conclusion

If you are an aspiring investor looking to own a piece of Singapore real estate trust with low starting capital, while earning a regular income, we hope this complete guide to Singapore REITs has convinced you to start looking at REITs as an option.

We have provided the key fundamentals to REITs investing in Singapore via the various sections above.

You should be able to understand frequently used terms in REITs, understand what to look out for in a profitable REIT, and how to actually invest and buy a REIT.

Our Early Retirement Masterclass trainer, Christopher Ng Wai Chung has had frequent discourse with us on the power of REITs as a dividend investing tool. His results back up his actions. He retired at 39 with a passive income of $6,000 - $8,000/month. And his retirement was never threatened by the birth of his second child or his desire to go to law school at SMU. He also shares his methodology at a live masterclass held occasionally, you can reserve a seat here, if you wish to learn more.

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LWT, Course graduate

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"The courses are a great start for beginners, would recommend for complete newbies."

Shaun Toh, Manufacturing Engineer

"Thank you for kindling in me a great passion to start investing! And for providing such a great support."

Ethan Lim, VFX artist